

OFFERING CIRCULAR

KAUPTHING

KAUPTHING BUNADARBANKI HF.

(incorporated in Iceland as a public limited company)

€2,000,000,000

Euro Medium Term Note Programme

Under this €2,000,000,000 Euro Medium Term Note Programme (the “**Programme**”), Kaupthing BunadarbANKI hf. (the “**Issuer**”) may from time to time issue notes (the “**Notes**”) denominated in any currency agreed between the Issuer and the relevant Dealer (as defined below).

The maximum aggregate nominal amount of all Notes from time to time outstanding under the Programme will not exceed €2,000,000,000 (or its equivalent in other currencies calculated as described herein), subject to increase as described herein.

The Notes may be issued on a continuing basis to one or more of the Dealers specified under “**Summary of the Programme**” and any additional Dealer appointed under the Programme from time to time by the Issuer (each a “**Dealer**” and together the “**Dealers**”), which appointment may be for a specific issue or on an ongoing basis. References in this Offering Circular to the “**relevant Dealer**” shall, in the case of an issue of Notes being (or intended to be) subscribed by more than one Dealer, be to all Dealers agreeing to purchase such Notes.

Application has been made to the Luxembourg Stock Exchange for Notes issued under the Programme during the period of 12 months from the date of this Offering Circular to be listed on the Luxembourg Stock Exchange. Notice of the aggregate nominal amount of Notes, interest (if any) payable in respect of Notes, the issue price of Notes and any other terms and conditions not contained herein which are applicable to each Tranche (as defined under “**Terms and Conditions of the Notes**”) of Notes will be set out in a pricing supplement (the “**Pricing Supplement**”) which, with respect to Notes to be listed on the Luxembourg Stock Exchange, will be delivered to the Luxembourg Stock Exchange on or before the date of issue of the Notes of such Tranche.

The Programme provides that Notes may be listed on such other or further stock exchange(s) as may be agreed between the Issuer and the relevant Dealer. The Issuer may also issue unlisted Notes.

The Issuer may agree with any Dealer that Notes may be issued in a form not contemplated by the Terms and Conditions of the Notes herein, in which event (in the case of Notes intended to be listed on the Luxembourg Stock Exchange) a supplementary Offering Circular, if appropriate, will be made available which will describe the effect of the agreement reached in relation to such Notes.

The Programme is rated by Moody’s Investors Service Limited (“**Moody’s**”). Senior Notes issued under the Programme may be rated or unrated. Where an issue of Senior Notes is rated, its rating will not necessarily be the same as the rating applicable to the Programme. A rating is not a recommendation to buy, sell or hold securities and may be subject to suspension, change or withdrawal at any time by the assigning rating agency.

Arranger
Citigroup

Dealers

Barclays Capital	CDC IXIS Capital Markets
Citigroup	Commerzbank Securities
Daiwa Securities SMBC Europe	Dresdner Kleinwort Wasserstein
Handelsbanken Capital Markets	Nordea
SEB Merchant Banking	

The date of this Offering Circular is 24th June, 2003

The Issuer, having made all reasonable enquiries, confirms that this Offering Circular contains or incorporates all information which is material in the context of the issuance and offering of Notes, that the information contained or incorporated in this Offering Circular is true and accurate in all material respects and is not misleading, that the opinions and intentions expressed in this Offering Circular are honestly held and that there are no other facts the omission of which would make this Offering Circular or any of such information or the expression of any such opinions or intentions misleading. The Issuer accepts responsibility accordingly.

This Offering Circular is to be read in conjunction with all documents which are deemed to be incorporated herein by reference (see “*Documents Incorporated by Reference*” below). This Offering Circular shall be read and construed on the basis that such documents are incorporated and form part of this Offering Circular.

The Dealers have not independently verified the information contained herein. Accordingly, no representation, warranty or undertaking, express or implied, is made and no responsibility or liability is accepted by the Dealers as to the accuracy or completeness of the information contained or incorporated in this Offering Circular or any other information provided by the Issuer in connection with the Programme. No Dealer accepts any liability in relation to the information contained or incorporated by reference in this Offering Circular or any other information provided by the Issuer in connection with the Programme.

No person is or has been authorised by the Issuer to give any information or to make any representation not contained in or not consistent with this Offering Circular or any other information supplied in connection with the Programme or the Notes and, if given or made, such information or representation must not be relied upon as having been authorised by the Issuer or any of the Dealers.

Neither this Offering Circular nor any other information supplied in connection with the Programme or any Notes (i) is intended to provide the basis of any credit or other evaluation or (ii) should be considered as a recommendation by the Issuer or any of the Dealers that any recipient of this Offering Circular or any other information supplied in connection with the Programme or any Notes should purchase any Notes. Each investor contemplating purchasing any Notes should make its own independent investigation of the financial condition and affairs, and its own appraisal of the creditworthiness, of the Issuer. Neither this Offering Circular nor any other information supplied in connection with the Programme or the issue of any Notes constitutes an offer or invitation by or on behalf of the Issuer or any of the Dealers to any person to subscribe for or to purchase any Notes.

Neither the delivery of this Offering Circular nor the offering, sale or delivery of any Notes shall in any circumstances imply that the information contained herein concerning the Issuer is correct at any time subsequent to the date hereof or that any other information supplied in connection with the Programme is correct as of any time subsequent to the date indicated in the document containing the same. The Dealers expressly do not undertake to review the financial condition or affairs of the Issuer during the life of the Programme or to advise any investor in the Notes of any information coming to their attention. Investors should review, *inter alia*, the most recently published documents incorporated by reference into this Offering Circular when deciding whether or not to purchase any Notes.

The Notes have not been and will not be registered under the United States Securities Act of 1933, as amended, (the “*Securities Act*”) and are subject to U.S. tax law requirements. Subject to certain exceptions, Notes may not be offered, sold or delivered within the United States or to U.S. persons (see “*Subscription and Sale*” below).

This Offering Circular does not constitute an offer to sell or the solicitation of an offer to buy any Notes in any jurisdiction to any person to whom it is unlawful to make the offer or solicitation in such jurisdiction. The distribution of this Offering Circular and the offer or sale of Notes may be restricted by law in certain jurisdictions. The Issuer and the Dealers do not represent that this Offering Circular may be lawfully distributed, or that any Notes may be lawfully offered, in compliance with any applicable registration or other requirements in any such jurisdiction, or

pursuant to an exemption available thereunder, or assume any responsibility for facilitating any such distribution or offering. In particular, no action has been taken by the Issuer or the Dealers which would permit a public offering of any Notes or distribution of this document in any jurisdiction where action for that purpose is required. Accordingly, no Notes may be offered or sold, directly or indirectly, and neither this Offering Circular nor any advertisement or other offering material may be distributed or published in any jurisdiction, except under circumstances that will result in compliance with any applicable laws and regulations. Persons into whose possession this Offering Circular or any Notes may come must inform themselves about, and observe, any such restrictions on the distribution of this Offering Circular and the offering and sale of Notes. In particular, there are restrictions on the distribution of this Offering Circular and the offer or sale of Notes in the United States, the United Kingdom, Japan and Iceland, see “*Subscription and Sale*”.

All references in this document to “*U.S. dollars*”, “*U.S.\$*” and “*\$*” refer to United States dollars, to “*ISK*”, “*krona*” or “*krónur*” refer to the currency of Iceland, to “*Japanese Yen*” and “*Yen*” refer to the currency of Japan, to “*Swiss francs*” refer to the currency of Switzerland, to “*Sterling*” and “*£*” refer to pounds sterling and to “*euro*” and “*€*” refer to the currency introduced at the start of the third stage of European economic and monetary union pursuant to the Treaty establishing the European Community, as amended.

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In connection with the issue and distribution of any Tranche of Notes, the Dealer (if any) disclosed as the stabilising manager in the applicable Pricing Supplement or any person acting for him may over-allot or effect transactions with a view to supporting the market price of the Notes of the Series (as defined below) of which such Tranche forms part at a level higher than that which might not otherwise prevail for a limited period after the issue date. However, there may be no obligation on the stabilising manager or any agent of his to do this. Such stabilising, if commenced, may be discontinued at any time and must be brought to an end after a limited period.

DOCUMENTS INCORPORATED BY REFERENCE

The following documents published or issued from time to time after the date hereof shall be deemed to be incorporated in, and to form part of, this Offering Circular:

- (a) the most recently published audited non-consolidated annual financial statements and the most recently published audited consolidated financial statements (if any) of the Issuer and, if published later, the most recently published interim non-consolidated financial statements and the most recently published interim consolidated financial statements (if any) of the Issuer; and
- (b) all supplements or amendments to this Offering Circular circulated by the Issuer from time to time,

save that any statement contained herein or in a document which is deemed to be incorporated by reference herein shall be deemed to be modified or superseded for the purpose of this Offering Circular to the extent that a statement contained in any such subsequent document which is deemed to be incorporated by reference herein modifies or supersedes such earlier statement (whether expressly, by implication or otherwise). Any statement so modified or superseded shall not be deemed, except as so modified or superseded, to constitute a part of this Offering Circular.

The Issuer will provide, without charge, to each person to whom a copy of this Offering Circular has been delivered, upon the request of such person, a copy of any or all of the documents deemed to be incorporated herein by reference unless such documents have been modified or superseded as specified above. Requests for such documents should be directed to the Issuer at its offices set out at the end of this Offering Circular. In addition, such documents will be available, free of charge, from the principal office in Luxembourg of Banque Générale du Luxembourg S.A. (the “**Luxembourg Listing Agent**”) for Notes listed on the Luxembourg Stock Exchange.

The Issuer will, in connection with the listing of the Notes on the Luxembourg Stock Exchange, so long as any Note remains outstanding and listed on such exchange, in the event of any material change in the condition of the Issuer which is not reflected in this Offering Circular, prepare a supplement to this Offering Circular or publish a new Offering Circular for use in connection with any subsequent issue of the Notes to be listed on the Luxembourg Stock Exchange.

If the terms of the Programme are modified or amended in a manner which would make this Offering Circular, as so modified or amended, inaccurate or misleading, a new offering circular will be prepared.

GENERAL DESCRIPTION OF THE PROGRAMME

Under the Programme, the Issuer may from time to time issue Notes denominated in any currency, subject as set out herein. A summary of the terms and conditions of the Programme and the Notes appears below. The applicable terms of any Notes will be agreed between the Issuer and the relevant Dealer prior to the issue of the Notes and will be set out in the Terms and Conditions of the Notes endorsed on, attached to, or incorporated by reference into, the Notes, as modified and supplemented by the applicable Pricing Supplement attached to, or endorsed on, such Notes, as more fully described under “*Form of the Notes*” below.

This Offering Circular and any supplement will only be valid for listing Notes on the Luxembourg Stock Exchange during the period of 12 months from the date of this Offering Circular in an aggregate nominal amount which, when added to the aggregate nominal amount then outstanding of all Notes previously or simultaneously issued under the Programme, does not exceed €2,000,000,000 or its equivalent in other currencies. For the purpose of calculating the euro equivalent of the aggregate nominal amount of Notes issued under the Programme from time to time:

- (a) the euro equivalent of Notes denominated in another Specified Currency (as specified in the applicable Pricing Supplement in relation to the relevant Notes, described under “*Form of the Notes*”) shall be determined, at the discretion of the Issuer, either as of the date on which agreement is reached for the issue of Notes or on the preceding day on which commercial banks and foreign exchange markets are open for business in London, in each case on the basis of the spot rate for the sale of the euro against the purchase of such Specified Currency in the London foreign exchange market quoted by any leading international bank selected by the Issuer on the relevant day of calculation;
- (b) the euro equivalent of Dual Currency Notes, Index Linked Notes and Partly Paid Notes (each as specified in the applicable Pricing Supplement in relation to the relevant Notes, described under “*Form of the Notes*”) shall be calculated in the manner specified above by reference to the original nominal amount on issue of such Notes (in the case of Partly Paid Notes regardless of the subscription price paid); and
- (c) the euro equivalent of Zero Coupon Notes (as specified in the applicable Pricing Supplement in relation to the relevant Notes, described under “*Form of the Notes*”) and other Notes issued at a discount or a premium shall be calculated in the manner specified above by reference to the net proceeds received by the Issuer for the relevant issue.

SUMMARY OF THE PROGRAMME

The following summary does not purport to be complete and is taken from, and is qualified in its entirety by, the remainder of this Offering Circular and, in relation to the terms and conditions of any particular Tranche of Notes, the applicable Pricing Supplement. Words and expressions defined in “Form of the Notes” and “Terms and Conditions of the Notes” below shall have the same meanings in this summary.

Issuer:	Kaupthing Bunadarbanki hf.
Description:	Euro Medium Term Note Programme
Arranger:	Citigroup Global Markets Limited
Dealers:	Barclays Bank PLC CDC IXIS Capital Markets Citigroup Global Markets Limited Commerzbank Aktiengesellschaft Daiwa Securities SMBC Europe Limited Dresdner Bank Aktiengesellschaft Nordea Bank Danmark A/S Skandinaviska Enskilda Banken AB (publ) Svenska Handelsbanken AB (publ) and any other Dealers appointed in accordance with the Programme Agreement.
Certain Restrictions:	Each issue of Notes denominated in a currency in respect of which particular laws, guidelines, regulations, restrictions or reporting requirements apply will only be issued in circumstances which comply with such laws, guidelines, regulations, restrictions or reporting requirements from time to time (see “ <i>Subscription and Sale</i> ”) including the following restrictions applicable at the date of this Offering Circular.

Swiss Francs

Issues of Notes denominated in Swiss francs or carrying a Swiss franc-related element with a maturity of more than one year (other than Notes privately placed with a single investor with no publicity) will be effected in compliance with the relevant regulations of the Swiss National Bank based on article 7 of the Federal Law on Banks and Savings Banks of 8th November, 1934 (as amended) and article 15 of the Federal Law on Stock Exchanges and Securities Trading of 24th March, 1995 in connection with article 2, paragraph 2 of the Ordinance of the Federal Banking Commission on Stock Exchanges and Securities Trading of 2nd December, 1996. Under the said regulations, the relevant Dealer or, in the case of a syndicated issue, the lead manager (the “**Swiss Dealer**”), must be a bank domiciled in Switzerland (which includes branches or subsidiaries of a foreign bank located in Switzerland) or a securities dealer duly licensed by the Swiss Federal Banking Commission pursuant to the Federal Law on Stock Exchanges and Securities Trading of 24th March, 1995. The Swiss Dealer must report certain details of the relevant transaction to the Swiss National Bank no later than the Issue Date of the relevant Notes.

Notes having a maturity of less than one year

Notes having a maturity of less than one year will, if the proceeds of the issue are accepted in the United Kingdom, constitute deposits for the purposes of the prohibition on accepting deposits contained in section 19 of the Financial Services and Markets Act 2000 unless they are issued to a limited class of professional investors and have a denomination of at least £100,000 or its equivalent, see “Subscription and Sale”.

Issuing and Principal Paying Agent:	Citibank, N.A.
Programme Size:	Up to €2,000,000,000 (or its equivalent in other currencies calculated as described under “ <i>General Description of the Programme</i> ”) outstanding at any time. The Issuer may increase the amount of the Programme in accordance with the terms of the Programme Agreement.
Distribution:	Notes may be distributed by way of private or public placement and in each case on a syndicated or non-syndicated basis.
Currencies:	Subject to any applicable legal or regulatory restrictions, any currency agreed between the Issuer and the relevant Dealer.
Redenomination:	The applicable Pricing Supplement may provide that certain Notes may be redenominated in euro. The relevant provisions applicable to any such redenomination are contained in Condition 4.
Maturities:	Such maturities as may be agreed between the Issuer and the relevant Dealer, subject to such minimum or maximum maturities as may be allowed or required from time to time by the relevant central bank (or equivalent body) or any laws or regulations applicable to the Issuer or the relevant Specified Currency.
Issue Price:	Notes may be issued on a fully-paid or a partly-paid basis and at an issue price which is at par or at a discount to, or premium over, par.
Form of Notes:	The Notes will be issued in bearer form as described in “ <i>Form of the Notes</i> ”.
Fixed Rate Notes:	Fixed interest will be payable on such date or dates as may be agreed between the Issuer and the relevant Dealer and on redemption and will be calculated on the basis of such Day Count Fraction as may be agreed between the Issuer and the relevant Dealer.
Floating Rate Notes:	<p>Floating Rate Notes will bear interest at a rate determined:</p> <ul style="list-style-type: none">(i) on the same basis as the floating rate under a notional interest rate swap transaction in the relevant Specified Currency governed by an agreement incorporating the 2000 ISDA Definitions (as published by the International Swaps and Derivatives Association, Inc., and as amended and updated as at the Issue Date of the first Tranche of the Notes of the relevant Series); or(ii) on the basis of a reference rate appearing on the agreed screen page of a commercial quotation service; or(iii) on such other basis as may be agreed between the Issuer and the relevant Dealer.

	The margin (if any) relating to such floating rate will be agreed between the Issuer and the relevant Dealer for each Series of Floating Rate Notes.
Index Linked Notes:	Payments of principal in respect of Index Linked Redemption Notes or of interest in respect of Index Linked Interest Notes will be calculated by reference to such index and/or formula or to changes in the prices of securities or commodities or to such other factors as the Issuer and the relevant Dealer may agree.
Other provisions in relation to Floating Rate Notes and Index Linked Interest Notes:	<p>Floating Rate Notes and Index Linked Interest Notes may also have a maximum interest rate, a minimum interest rate or both.</p> <p>Interest on Floating Rate Notes and Index Linked Interest Notes in respect of each Interest Period, as agreed prior to issue by the Issuer and the relevant Dealer, will be payable on such Interest Payment Dates, and will be calculated on the basis of such Day Count Fraction, as may be agreed between the Issuer and the relevant Dealer.</p>
Dual Currency Notes:	Payments (whether in respect of principal or interest and whether at maturity or otherwise) in respect of Dual Currency Notes will be made in such currencies, and based on such rates of exchange, as the Issuer and the relevant Dealer may agree.
Zero Coupon Notes:	Zero Coupon Notes will be offered and sold at a discount to their nominal amount and will not bear interest.
Redemption:	<p>The applicable Pricing Supplement will indicate either that the relevant Notes cannot be redeemed prior to their stated maturity (other than in specified instalments, if applicable, or for taxation reasons or following an Event of Default) or that such Notes will be redeemable at the option of the Issuer and/or the Noteholders upon giving notice to the Noteholders or the Issuer, as the case may be, on a date or dates specified prior to such stated maturity and at a price or prices and on such other terms as may be agreed between the Issuer and the relevant Dealer.</p> <p>The applicable Pricing Supplement may provide that Notes may be redeemable in two or more instalments of such amounts and on such dates as are indicated in the applicable Pricing Supplement.</p> <p>Notes having a maturity of less than one year may be subject to restrictions on their denomination and distribution, see “<i>Certain Restrictions – Notes having a maturity of less than one year</i>” above.</p>
Denomination of Notes:	Notes will be issued in such denominations as may be agreed between the Issuer and the relevant Dealer save that the minimum denomination of each Note will be such as may be allowed or required from time to time by the relevant central bank (or equivalent body) or any laws or regulations applicable to the relevant Specified Currency, see “ <i>Certain Restrictions – Notes having a maturity of less than one year</i> ” above.
Taxation:	All payments in respect of the Notes will be made without deduction for or on account of withholding taxes imposed by any Tax Jurisdiction, subject as provided in Condition 8. In the event that any such deduction is made, the Issuer will, save in certain limited circumstances provided in Condition 8, be required to pay additional amounts to cover the amounts so deducted.

Negative Pledge:	The terms of the Notes will contain a negative pledge provision as further described in Condition 3.
Cross Default:	The terms of the Notes will contain a cross default provision as further described in Condition 10.
Status of the Senior Notes:	The Senior Notes will constitute direct, unconditional, unsubordinated and, subject to the provisions of Condition 3, unsecured obligations of the Issuer and will rank <i>pari passu</i> among themselves and (save for certain obligations required to be preferred by law) equally with all other unsecured obligations (other than subordinated obligations, if any) of the Issuer, from time to time outstanding.
Subordination:	Payments in respect of the Subordinated Notes will be subordinated as described in Condition 2(b).
Rating:	The Programme is rated by Moody's. Senior Notes issued under the Programme may be rated or unrated. Where an issue of Senior Notes is rated, its rating will not necessarily be the same as the rating applicable to the Programme. A rating is not a recommendation to buy, sell or hold securities and may be subject to suspension, change or withdrawal at any time by the assigning rating agency.
Listing:	<p>Application has been made for Notes issued under the Programme to be listed on the Luxembourg Stock Exchange. The Notes may also be listed on such other or further stock exchange(s) as may be agreed between the Issuer and the relevant Dealer in relation to each Series.</p> <p>Unlisted Notes may also be issued.</p> <p>The applicable Pricing Supplement will state whether or not the relevant Notes are to be listed and, if so, on which stock exchange(s).</p>
Governing Law:	The Notes will be governed by, and construed in accordance with, English law, except the provisions of Condition 2(b) which will be governed by Icelandic law.
Selling Restrictions:	There are restrictions on the offer, sale and transfer of the Notes in the United States, the United Kingdom, Japan and Iceland and such other restrictions as may be required in connection with the offering and sale of a particular Tranche of Notes, see " <i>Subscription and Sale</i> ".

FORM OF THE NOTES

Each Tranche of Notes will be in bearer form and will be initially issued in the form of a temporary global note (a “**Temporary Global Note**”) or, if so specified in the applicable Pricing Supplement, a permanent Global Note (a “**Permanent Global Note**”) which, in either case, will be delivered on or prior to the original issue date of the Tranche to a common depository (the “**Common Depositary**”) for, Euroclear Bank S.A./N.V. as operator of the Euroclear System (“**Euroclear**”) and Clearstream Banking, société anonyme (“**Clearstream, Luxembourg**”). Whilst any Note is represented by a Temporary Global Note, payments of principal, interest (if any) and any other amount payable in respect of the Notes due prior to the Exchange Date (as defined below) will be made against presentation of the Temporary Global Note only to the extent that certification (in a form to be provided) to the effect that the beneficial owners of interests in such Note are not U.S. persons or persons who have purchased for resale to any U.S. person, as required by U.S. Treasury regulations, has been received by Euroclear and/or Clearstream, Luxembourg and Euroclear and/or Clearstream, Luxembourg, as applicable, has given a like certification (based on the certifications it has received) to the Agent.

On and after the date (the “**Exchange Date**”) which is 40 days after a Temporary Global Note is issued, interests in such Temporary Global Note will be exchangeable (free of charge) upon a request as described therein either for (i) interests in a Permanent Global Note of the same Series or (ii) for definitive Notes of the same Series with, where applicable, receipts, interest coupons and talons attached (as indicated in the applicable Pricing Supplement and subject, in the case of definitive Notes, to such notice period as is specified in the applicable Pricing Supplement), in each case against certification of beneficial ownership as described above unless such certification has already been given. The holder of a Temporary Global Note will not be entitled to collect any payment of interest, principal or other amount due on or after the Exchange Date unless, upon due certification, exchange of the Temporary Global Note for an interest in a Permanent Global Note or for definitive Notes is improperly withheld or refused.

Payments of principal, interest (if any) or any other amounts on a Permanent Global Note will be made through Euroclear and/or Clearstream, Luxembourg against presentation or surrender (as the case may be) of the Permanent Global Note without any requirement for certification.

The applicable Pricing Supplement will specify that a Permanent Global Note will be exchangeable (free of charge), in whole but not in part, for definitive Notes with, where applicable, receipts, interest coupons and talons attached upon either (i) not less than 60 days’ written notice from Euroclear and/or Clearstream, Luxembourg (acting on the instructions of any holder of an interest in such Permanent Global Note) to the Agent as described therein or (ii) only upon the occurrence of an Exchange Event. For these purposes, “**Exchange Event**” means that (i) an Event of Default (as defined in Condition 10) has occurred and is continuing, (ii) the Issuer has been notified that both Euroclear and Clearstream, Luxembourg have been closed for business for a continuous period of 14 days (other than by reason of holiday, statutory or otherwise) or have announced an intention permanently to cease business or have in fact done so and no successor clearing system is available or (iii) the Issuer has or will become subject to adverse tax consequences which would not be suffered were the Notes represented by the Permanent Global Note in definitive form. The Issuer will promptly give notice to Noteholders in accordance with Condition 14 if an Exchange Event occurs. In the event of the occurrence of an Exchange Event, Euroclear and/or Clearstream, Luxembourg (acting on the instructions of any holder of an interest in such Permanent Global Note) may give notice to the Agent requesting exchange and, in the event of the occurrence of an Exchange Event as described in (iii) above, the Issuer may also give notice to the Agent requesting exchange. Any such exchange shall occur not later than 45 days after the date of receipt of the first relevant notice by the Agent.

The following legend will appear on all Notes which have an original maturity of more than 365 days and on all receipts and interest coupons relating to such Notes:

“ANY UNITED STATES PERSON WHO HOLDS THIS OBLIGATION WILL BE SUBJECT TO LIMITATIONS UNDER THE UNITED STATES INCOME TAX LAWS, INCLUDING THE LIMITATIONS PROVIDED IN SECTIONS 165(j) AND 1287(a) OF THE INTERNAL REVENUE CODE.”

The sections referred to provide that United States holders, with certain exceptions, will not be entitled to deduct any loss on Notes, receipts or interest coupons and will not be entitled to capital gains treatment of any gain on any sale, disposition, redemption or payment of principal in respect of such Notes, receipts or interest coupons.

Notes which are represented by a Global Note will only be transferable in accordance with the rules and procedures for the time being of Euroclear or Clearstream, Luxembourg, as the case may be.

Pursuant to the Agency Agreement (as defined under “*Terms and Conditions of the Notes*”), the Agent shall arrange that, where a further Tranche of Notes is issued which is intended to form a single Series with an existing Tranche of Notes, the Notes of such further Tranche shall be assigned a common code and ISIN which are different from the common code and ISIN assigned to Notes of any other Tranche of the same Series until at least the expiry of the distribution compliance period (as defined in Regulation S under the Securities Act) applicable to the Notes of such Tranche.

Any reference herein to Euroclear and/or Clearstream, Luxembourg shall, whenever the context so permits, be deemed to include a reference to any additional or alternative clearing system specified in the applicable Pricing Supplement.

A Note may be accelerated by the holder thereof in certain circumstances described in Condition 10. In such circumstances, where any Note is still represented by a Global Note and the Global Note (or any part thereof) has become due and repayable in accordance with the Terms and Conditions of such Notes and payment in full of the amount due has not been made in accordance with the provisions of the Global Note then the Global Note will become void at 8.00 p.m. (London time) on such day. At the same time, holders of interests in such Global Note credited to their accounts with Euroclear and/or Clearstream, Luxembourg, as the case may be, will become entitled to proceed directly against the Issuer on the basis of statements of account provided by Euroclear and/or Clearstream, Luxembourg on and subject to the terms of a deed of covenant (the “*Deed of Covenant*”) dated 24th June, 2003 and executed by the Issuer.

Applicable Pricing Supplement

Set out below is the form of Pricing Supplement which will be completed for each Tranche of Notes issued under the Programme.

[Date]

KAUPTHING BUNADARBANKI HF.

Issue of [Aggregate Nominal Amount of Tranche] [Title of Notes] under the €2,000,000,000 Euro Medium Term Note Programme

This document constitutes the Pricing Supplement relating to the issue of Notes described herein. Terms used herein shall be deemed to be defined as such for the purposes of the Conditions set forth in the Offering Circular dated 24th June, 2003. This Pricing Supplement is supplemental to and must be read in conjunction with such Offering Circular.

[Include whichever of the following apply or specify as “Not Applicable” (N/A). Note that the numbering should remain as set out below, even if “Not Applicable” is indicated for individual paragraphs or sub-paragraphs.]

[If the Notes have a maturity of less than one year from the date of their issue, the minimum denomination may need to be £100,000 or its equivalent in any other currency.]

- | | | |
|----|-----------------------------------|--|
| 1. | Issuer: | Kaupthing Bunadarbanski hf. |
| 2. | (i) Series Number: | [] |
| | (ii) Tranche Number: | [] |
| | | <i>(If fungible with an existing Series, details of that Series, including the date on which the Notes become fungible)</i> |
| 3. | Specified Currency or Currencies: | [] |
| 4. | Aggregate Nominal Amount: | |
| | (i) Series: | [] |
| | (ii) Tranche: | [] |
| 5. | (i) Issue Price: | [] per cent. of the Aggregate Nominal Amount
[plus accrued interest from [insert date] (in the case of fungible issues only, if applicable)] |
| | (ii) Net proceeds | [] |
| 6. | Specified Denominations: | [] |
| 7. | (i) Issue Date: | [] |
| | (ii) Interest Commencement Date: | [] |
| 8. | Maturity Date: | <i>[Fixed rate – specify date/
Floating rate – Interest Payment Date falling in or nearest to [specify month]]</i> |
| 9. | Interest Basis: | [[] per cent. Fixed Rate]
[[LIBOR/EURIBOR] +/- [] per cent. Floating Rate]
[Zero Coupon] |

- [Index Linked Interest]
[Dual Currency Interest]
[specify other]
(further particulars specified below)
10. Redemption/Payment Basis: [Redemption at par]
[Index Linked Redemption]
[Dual Currency Redemption]
[Partly Paid]
[Instalment]
[specify other]
11. Change of Interest Basis or Redemption/
Payment Basis: [Specify details of any provision for change of
Notes into another Interest Basis or
Redemption/ Payment Basis]
12. Put/Call Options: [Investor Put]
[Issuer Call]
[(further particulars specified below)]
13. Status of the Notes: [Senior/Subordinated]
14. Listing: [Luxembourg/specify other/None]
15. Method of distribution: [Syndicated/Non-syndicated]

PROVISIONS RELATING TO INTEREST (IF ANY) PAYABLE

16. **Fixed Rate Note Provisions** [Applicable/Not Applicable]
(If not applicable, delete the remaining sub-
paragraphs of this paragraph)
- (i) Rate(s) of Interest: [] per cent. per annum [payable
[annually/semi-annually/quarterly] in arrear]
(If payable other than annually, consider
amending Condition 5(a))
- (ii) Interest Payment Date(s): [[] in each year up to and including the
Maturity Date]/[specify other]
(NB: This will need to be amended in the case
of long or short coupons)
- (iii) Fixed Coupon Amount(s): [] per [] in nominal amount
- (iv) Broken Amount(s): [Insert particulars of any initial or final broken
interest amounts which do not correspond with
the Fixed Coupon Amount]
- (v) Day Count Fraction: [30/360 or Actual/Actual (ISMA) or specify
other])
- (vi) Determination Date(s): [] in each year
[Insert regular interest payment dates, ignoring
issue date or maturity date in the case of a long
or short first or last coupon
NB: This will need to be amended in the case of
regular interest payment dates which are not of
equal duration
NB: Only relevant where Day Count Fraction
is Actual/Actual (ISMA)]

(vii) Other terms relating to the method of calculating interest for Fixed Rate Notes:	[None/Give details]
17. Floating Rate Note Provisions	[Applicable/Not Applicable] <i>(If not applicable, delete the remaining sub-paragraphs of this paragraph)</i>
(i) Specified Period(s)/Specified Interest Payment Dates:	[]
(ii) Business Day Convention:	[Floating Rate Convention/Following Business Day Convention/Modified Following Business Day Convention/Preceding Business Day Convention/[specify other]]
(iii) Additional Business Centre(s):	[]
(iv) Manner in which the Rate of Interest and Interest Amount is to be determined:	[Screen Rate Determination/ISDA Determination/specify other]
(v) Party responsible for calculating the Rate of Interest and Interest Amount (if not the Agent):	[]
(vi) Screen Rate Determination:	
- Reference Rate:	[] <i>(Either LIBOR, EURIBOR or other, although additional information is required if other – including fallback provisions in the Agency Agreement)</i>
- Interest Determination Date(s):	[] <i>(Second London business day prior to the start of each Interest Period if LIBOR (other than Sterling or euro LIBOR), first day of each Interest Period if Sterling LIBOR and the second day on which the TARGET System is open prior to the start of each Interest Period if EURIBOR or euro LIBOR)</i>
- Relevant Screen Page:	[] <i>(In the case of EURIBOR, if not Telerate Page 248 ensure it is a page which shows a composite rate or amend the fallback provisions appropriately)</i>
(vii) ISDA Determination:	
- Floating Rate Option:	[]
- Designated Maturity:	[]
- Reset Date:	[]
(viii) Margin(s):	[+/-] [] per cent. per annum
(ix) Minimum Rate of Interest:	[] per cent. per annum
(x) Maximum Rate of Interest:	[] per cent. per annum

- (xi) Day Count Fraction: [Actual/365
Actual/365 (Fixed)
Actual/365 (Sterling)
Actual/360
30/360
30E/360
Other]
(See Condition 5 for alternatives)
- (xii) Fall back provisions, rounding provisions and any other terms relating to the method of calculating interest on Floating Rate Notes, if different from those set out in the Conditions: []
18. **Zero Coupon Note Provisions** [Applicable/Not Applicable]
(If not applicable, delete the remaining subparagraphs of this paragraph)
- (i) Accrual Yield: [] per cent. per annum
- (ii) Reference Price: []
- (iii) Any other formula/basis of determining amount payable: []
(Consider applicable day count fraction if not U.S. dollar denominated)
- (iv) Fall back provisions, rounding provisions and any other terms relating to the method of calculating interest on Floating Rate Notes, if different from those set out in the Conditions: [Conditions 7(e)(iii) and 7(j) apply/specify other]
(Consider applicable day count fraction if not U.S. dollar denominated)
19. **Index Linked Interest Note Provisions** [Applicable/Not Applicable]
(If not applicable, delete the remaining subparagraphs of this paragraph)
- (i) Index/Formula: [give or annex details]
- (ii) Calculation Agent responsible for calculating the principal and/or interest due: []
- (iii) Provisions for determining coupon where calculation by reference to Index and/or Formula is impossible or impracticable: []
- (iv) Specified Period(s)/Specified Interest Payment Dates: []
- (v) Business Day Convention: [Floating Rate Convention/Following Business Day Convention/Modified Following Business Day Convention/Preceding Business Day Convention/specify other]
- (vi) Additional Business Centre(s): []
- (vii) Minimum Rate of Interest: [] per cent. per annum
- (viii) Maximum Rate of Interest: [] per cent. per annum

- (ix) Day Count Fraction: []
20. **Dual Currency Note Provisions** [Applicable/Not Applicable]
(If not applicable, delete the remaining sub-paragraphs of this paragraph)
- (i) Rate of Exchange/method of calculating Rate of Exchange: [give details]
- (ii) Calculation Agent, if any, responsible for calculating the principal and/or interest payable: []
- (iii) Provisions applicable where calculation by reference to Rate of Exchange impossible or impracticable: []
- (iv) Person at whose option Specified Currency(ies) is/are payable: []

PROVISIONS RELATING TO REDEMPTION

21. Issuer Call: [Applicable/Not Applicable]
(If not applicable, delete the remaining sub-paragraphs of this paragraph)
- (i) Optional Redemption Date(s): []
- (ii) Optional Redemption Amount of each Note and method, if any, of calculation of such amount(s): []
- (iii) If redeemable in part:
- (a) Minimum Redemption Amount: []
- (b) Maximum Redemption Amount: []
- (iv) Notice period (if other than as set out in the Conditions): []
22. Investor Put: [Applicable/Not Applicable]
(If not applicable, delete the remaining sub-paragraphs of this paragraph)
- (i) Optional Redemption Date(s): []
- (ii) Optional Redemption Amount of each Note and method, if any, of calculation of such amount(s): []
- (iii) Notice period (if other than as set out in the Conditions): []
23. Final Redemption Amount of each Note: [Nominal Amount/specify other/see Appendix]

24. Early Redemption Amount of each Note payable on redemption for taxation reasons or on event of default and/or the method of calculating the same (if required or if different from that set out in Condition 7(e)): []

GENERAL PROVISIONS APPLICABLE TO THE NOTES

25. Form of Notes: [Temporary Global Note exchangeable for a Permanent Global Note which is exchangeable for Definitive Notes [on 60 days' notice given at any time/only upon an Exchange Event]]
[Temporary Global Note exchangeable for Definitive Notes on and after the Exchange Date]
[Permanent Global Note exchangeable for Definitive Notes [on 60 days' notice given at any time/only upon an Exchange Event]]
26. Additional Financial Centre(s) or other special provisions relating to Payment Dates: [Not Applicable/give details]
(Note that this item relates to the place of payment and not Interest Period end dates to which items 17(iii) and 19(vi) relate)
27. Talons for future Coupons or Receipts to be attached to Definitive Notes (and dates on which such Talons mature): [Yes/No. If yes, give details]
28. Details relating to Partly Paid Notes: amount of each payment comprising the Issue Price and date on which each payment is to be made and consequences of failure to pay, including any right of the Issuer to forfeit the Notes and interest due on late payment: [Not Applicable/give details. NB: a new form of Temporary Global Note and/or Permanent Global Note may be required for Partly Paid issues]
29. Details relating to Instalment Notes:
- (i) Instalment Amount(s): [Not Applicable/give details]
- (ii) Instalment Date(s): [Not Applicable/give details]
30. Redenomination applicable: Redenomination [not] applicable
[(If Redenomination is applicable, specify the applicable Day Count Fraction and any provisions necessary to deal with floating rate interest calculation (including alternative reference rates))][(if Redenomination is applicable, specify the terms of the redenomination in an Annex to the Pricing Supplement)]
31. Other terms or special conditions: [Not Applicable/give details]

DISTRIBUTION

32. (i) If syndicated, names of Managers: [Not Applicable/*give names*]
(ii) Stabilising Manager (if any): [Not Applicable/*give name*]
33. If non-syndicated, name of relevant Dealer: []
34. Whether TEFRA D or TEFRA C rules applicable or TEFRA rules not applicable: [TEFRA D/TEFRA C/TEFRA not applicable]
35. Additional selling restrictions: [Not Applicable/*give details*]

OPERATIONAL INFORMATION

36. Any clearing system(s) other than Euroclear and Clearstream, Luxembourg and the relevant identification number(s): [Not Applicable/*give name(s) and number(s)*]
37. Delivery: Delivery [against/free of] payment
38. Additional Paying Agent(s) (if any): []
-
- ISIN: []
- Common Code:
- (*insert here any other relevant codes*) []
-

[LISTING APPLICATION

This Pricing Supplement comprises the details required to list the issue of Notes described herein pursuant to the €2,000,000,000 Euro Medium Term Note Programme of Kaupthing Bunadabanki hf.]

RESPONSIBILITY

The Issuer accepts responsibility for the information contained in this Pricing Supplement.

Signed on behalf of the Issuer:

By:
Duly authorised

If the applicable Pricing Supplement specifies any modification to the Terms and Conditions of the Notes as described herein, it is envisaged that, to the extent that such modification relates only to Conditions 1, 4, 5, 6, 7 (except Condition 7(b)), 11, 12, 13, 14 (insofar as such Notes are not listed or admitted to trade on any stock exchange) or 16, they will not necessitate the preparation of a supplement to this Offering Circular. If the Terms and Conditions of the Notes of any Series are to be modified in any other respect, a supplement to this Offering Circular will be prepared, if appropriate.

TERMS AND CONDITIONS OF THE NOTES

The following are the Terms and Conditions of the Notes which will be incorporated by reference into each Global Note (as defined below) and each definitive Note, in the latter case only if permitted by the relevant stock exchange or other relevant authority (if any) and agreed by the Issuer and the relevant Dealer at the time of issue but, if not so permitted and agreed, such definitive Note will have endorsed thereon or attached thereto such Terms and Conditions. The applicable Pricing Supplement in relation to any Tranche of Notes may specify other terms and conditions which shall, to the extent so specified or to the extent inconsistent with the following Terms and Conditions, replace or modify the following Terms and Conditions for the purpose of such Notes. The applicable Pricing Supplement (or the relevant provisions thereof) will be endorsed upon, or attached to, each Global Note and definitive Note. Reference should be made to “Form of the Notes” for a description of the content of Pricing Supplements which will specify which of such terms are to apply in relation to the relevant Notes.

This Note is one of a Series (as defined below) of Notes issued by Kaupthing Bunadarbanski hf. (the “**Issuer**”) pursuant to the Agency Agreement (as defined below).

References herein to the “**Notes**” shall be references to the Notes of this Series and shall mean:

- (i) in relation to any Notes represented by a global Note (a “**Global Note**”), units of the lowest Specified Denomination in the Specified Currency;
- (ii) any Global Note; and
- (iii) any definitive Notes issued in exchange for a Global Note.

The Notes, the Receipts (as defined below) and the Coupons (as defined below) have the benefit of an Agency Agreement (such Agency Agreement as amended and/or supplemented and/or restated from time to time, the “**Agency Agreement**”) dated 24th June, 2003 and made between the Issuer, Citibank, N.A. as issuing and principal paying agent and agent bank (the “**Agent**”, which expression shall include any successor agent) and the other paying agents named therein (together with the Agent, the “**Paying Agents**”, which expression shall include any additional or successor paying agents).

Interest bearing definitive Notes have interest coupons (“**Coupons**”) and, if indicated in the applicable Pricing Supplement, talons for further Coupons (“**Talons**”) attached on issue. Any reference herein to Coupons or coupons shall, unless the context otherwise requires, be deemed to include a reference to Talons or talons. Definitive Notes repayable in instalments have receipts (“**Receipts**”) for the payment of the instalments of principal (other than the final instalment) attached on issue. Global Notes do not have Receipts, Coupons or Talons attached on issue.

The Pricing Supplement for this Note (or the relevant provisions thereof) is attached to or endorsed on this Note and supplements these Terms and Conditions (the “**Conditions**”) and may specify other terms and conditions which shall, to the extent so specified or to the extent inconsistent with these Conditions, replace or modify these Conditions for the purposes of this Note. References to the “**applicable Pricing Supplement**” are to the Pricing Supplement (or the relevant provisions thereof) attached to or endorsed on this Note.

Any reference to “**Noteholders**” or “**holders**” in relation to any Notes shall mean the holders of the Notes and shall, in relation to any Notes represented by a Global Note, be construed as provided below. Any reference herein to “**Receiptholders**” shall mean the holders of the Receipts and any reference herein to “**Couponholders**” shall mean the holders of the Coupons and shall, unless the context otherwise requires, include the holders of the Talons.

As used herein, “**Tranche**” means Notes which are identical in all respects (including as to listing) and “**Series**” means a Tranche of Notes together with any further Tranche or Tranches of Notes which are (i) expressed to be consolidated and form a single series and (ii) identical in all respects (including as to listing) except for their respective Issue Dates, Interest Commencement Dates and/or Issue Prices.

The Noteholders, the Receiptholders and the Couponholders are entitled to the benefit of the Deed of Covenant (the “**Deed of Covenant**”) dated 24th June, 2003 and made by the Issuer. The original of the Deed of Covenant is held by the common depositary for Euroclear (as defined below) and Clearstream, Luxembourg (as defined below).

Copies of the Agency Agreement and the Deed of Covenant are available for inspection during normal business hours at the specified office of each of the Paying Agents. Copies of the applicable Pricing Supplement are obtainable during normal business hours at the specified office of each of the Paying Agents save that, if this Note is an unlisted Note of any Series, the applicable Pricing Supplement will only be obtainable by a Noteholder holding one or more unlisted Notes of that Series and such Noteholder must produce evidence satisfactory to the Issuer and the relevant Paying Agent as to its holding of such Notes and identity. The Noteholders, the Receiptholders and the Couponholders are deemed to have notice of, and are entitled to the benefit of, all the provisions of the Agency Agreement, the Deed of Covenant and the applicable Pricing Supplement which are applicable to them. The statements in these Terms and Conditions include summaries of, and are subject to, the detailed provisions of the Agency Agreement.

Words and expressions defined in the Agency Agreement or used in the applicable Pricing Supplement shall have the same meanings where used in these Terms and Conditions unless the context otherwise requires or unless otherwise stated and provided that, in the event of inconsistency between the Agency Agreement and the applicable Pricing Supplement, the applicable Pricing Supplement will prevail.

1. FORM, DENOMINATION AND TITLE

The Notes are in bearer form and, in the case of definitive Notes, serially numbered, in the Specified Currency and the Specified Denomination(s). Notes of one Specified Denomination may not be exchanged for Notes of another Specified Denomination.

This Note may be a Fixed Rate Note, a Floating Rate Note, a Zero Coupon Note, an Index Linked Interest Note, a Dual Currency Interest Note or a combination of any of the foregoing, depending upon the Interest Basis shown in the applicable Pricing Supplement.

This Note may be an Index Linked Redemption Note, an Instalment Note, a Dual Currency Redemption Note, a Partly Paid Note or a combination of any of the foregoing, depending upon the Redemption/Payment Basis shown in the applicable Pricing Supplement.

This Note may also be a Senior Note or a Subordinated Note, as indicated in the applicable Pricing Supplement.

Definitive Notes are issued with Coupons attached, unless they are Zero Coupon Notes in which case references to Coupons and Couponholders in these Terms and Conditions are not applicable.

Subject as set out below, title to the Notes, Receipts and Coupons will pass by delivery. The Issuer and the Paying Agents will (except as otherwise required by law) deem and treat the bearer of any Note, Receipt or Coupon as the absolute owner thereof (whether or not overdue and notwithstanding any notice of ownership or writing thereon or notice of any previous loss or theft thereof) for all purposes but, in the case of any Global Note, without prejudice to the provisions set out in the next succeeding paragraph.

For so long as any of the Notes is represented by a Global Note held on behalf of Euroclear Bank S.A./N.V. as operator of the Euroclear System (“**Euroclear**”) and/or Clearstream Banking, société anonyme (“**Clearstream, Luxembourg**”), each person (other than Euroclear or Clearstream, Luxembourg) who is for the time being shown in the records of Euroclear or of Clearstream, Luxembourg as the holder of a particular nominal amount of such Notes (in which regard any certificate or other document issued by Euroclear or Clearstream, Luxembourg as to the nominal amount of such Notes standing to the account of any person shall be conclusive and binding for all purposes save in the case of manifest error) shall be treated by the Issuer and the Paying Agents as the holder of such nominal amount of such Notes for all purposes other than with respect to the payment of principal or interest on such nominal amount of such Notes, for which purpose the bearer of the

relevant Global Note shall be treated by the Issuer and any Paying Agent as the holder of such nominal amount of such Notes in accordance with and subject to the terms of the relevant Global Note and the expressions “**Noteholder**” and “**holder of Notes**” and related expressions shall be construed accordingly. Notes which are represented by a Global Note will be transferable only in accordance with the rules and procedures for the time being of Euroclear and Clearstream, Luxembourg, as the case may be.

References to Euroclear and/or Clearstream, Luxembourg shall, whenever the context so permits, be deemed to include a reference to any additional or alternative clearing system specified in the applicable Pricing Supplement.

2. STATUS OF THE SENIOR NOTES AND SUBORDINATION

(a) Status of the Senior Notes

The Senior Notes and any relative Receipts and Coupons are direct, unconditional, unsubordinated and (subject to the provisions of Condition 3) unsecured obligations of the Issuer and rank *pari passu* among themselves and (save for certain obligations required to be preferred by law) equally with all other unsecured obligations (other than subordinated obligations, if any) of the Issuer, from time to time outstanding.

(b) Subordination

The Subordinated Notes and any relative Receipts and Coupons are unsecured and unconditional obligations of the Issuer, subordinated in accordance with and for the purposes of Chapter VI; Liquid Assets and Own Funds; Article 54 of the Act on Commercial Banks and Savings Banks No. 161/2002 (the “**Act**”) of the Icelandic Parliament, and rank *pari passu* and ratably and without any preference among themselves and accordingly, on the insolvency or liquidation of the Issuer, the Subordinated Notes rank in right of payment:

- (i) after payment of all obligations of the Issuer which are not expressed to be subordinated in accordance with and for the purposes of Chapter VI; Liquid Assets and Own Funds; Article 54 of the Act (or any provision in any other Act of the Icelandic Parliament which modifies or replaces those provisions);
- (ii) at least *pari passu* with all other obligations of the Issuer which are expressed to be subordinated in accordance with and for the purposes of Chapter VI; Liquid Assets and Own Funds; Article 54 of the Act (or any provision in any other Act of the Icelandic Parliament which modifies or replaces those provisions);
- (iii) before the refund of any share capital and/or establishment funds (*hlutafé eda stofnfé*) and/or comparable capital and reserves (*sambærilegt eiginfé*) of the Issuer.

The Issuer undertakes that for so long as any of the Subordinated Notes, Receipts or Coupons remain outstanding (as defined in the Agency Agreement) it will not create any subordinated obligation other than in accordance with and for the purposes of Chapter VI; Liquid Assets and Own Funds; Article 54 of the Act or any provision in any other Act of the Icelandic Parliament which modifies or replaces these provisions). The provisions of this Condition 2(b) shall be governed by, and construed in accordance with, Icelandic law.

3. NEGATIVE PLEDGE

So long as any of the Notes, Receipts or Coupons remains outstanding the Issuer undertakes that it will not and that it will procure that none of its Subsidiaries will create or have outstanding any mortgage, charge, pledge, lien or other security interest (each a “**Security Interest**”) upon the whole or any part of its undertaking, assets or revenues (including any uncalled capital), present or future, in order to secure any Relevant Indebtedness (as defined below) or to secure any guarantee of or indemnify in respect of any Relevant Indebtedness unless (a) all amounts payable by it under the Notes, Receipts and Coupons are equally and ratably secured therewith by such Security Interest or

(b) such other Security Interest or other arrangement (whether or not it includes the giving of a Security Interest) is provided as shall be approved by an Extraordinary Resolution (as defined in the Agency Agreement) of the Noteholders.

For the purposes of these Conditions:

“Excluded Indebtedness” means any Relevant Indebtedness in respect of which the person or persons to whom any such Relevant Indebtedness is or may be owed by the relevant borrower has or have no recourse whatsoever to the Issuer or any Subsidiary (whether or not also the relevant borrower) for the repayment thereof other than:

- (i) recourse to such borrower for amounts limited to the cash flow or net cash flow (other than historic cash flow or historic net cash flow) from a Specified Asset; and/or
- (ii) recourse to such borrower for the purpose only of enabling amounts to be claimed in respect of such Relevant Indebtedness in an enforcement of any encumbrance given by such borrower over a Specified Asset or the income, cash flow or other proceeds deriving therefrom (or given by a shareholder or the like in the borrower over its shares or the like in the capital of the borrower) to secure such Relevant Indebtedness, provided that (a) the extent of such recourse to such borrower is limited solely to the amount of any recoveries made on any such enforcement, and (b) such person or persons is/are not entitled, by virtue of any right or claim arising out of or in connection with such Relevant Indebtedness, to commence proceedings for the winding up or dissolution of the borrower or to appoint or procure the appointment of any receiver, trustee or similar person or officer in respect of the borrower or any of its assets (save for the assets the subject of such encumbrance); and/or
- (iii) recourse of such borrower generally, or directly or indirectly to the Issuer or any Subsidiary, under any form of assurance, undertaking or support, which recourse is limited to a claim for damages (other than liquidated damages and damages required to be calculated in a specified way) for breach of an obligation (not being a payment obligation or an obligation to procure payment by another or an indemnity in respect thereof or any obligation to comply or to procure compliance by another with any financial ratios or other tests of financial condition) by the person against which such recourse is available;

“Relevant Indebtedness” means any present or future indebtedness (which term shall be construed so as to include any obligation (whether incurred as principal or as surety) for the payment or repayment of money, whether present or future, actual or contingent) in the form of, or represented or evidenced by, bonds, debentures, notes or other securities which are, or are intended to be, with the agreement of the issuer thereof, quoted, listed, dealt in or traded on any stock exchange or over-the-counter or other securities market other than such indebtedness which by its terms will mature within a period of one year from its date of issue and other than Excluded Indebtedness;

“Specified Asset” means an asset of the Issuer or any Subsidiary over which security is given in connection with any limited recourse securitisation or other asset-backed financing; and

“Subsidiary” means any entity whose affairs are required by law or in accordance with generally accepted accounting principles applicable to Iceland to be consolidated in the consolidated accounts of the Issuer.

4. REDENOMINATION

(a) Redenomination

Where redenomination is specified in the applicable Pricing Supplement as being applicable, the Issuer may, without the consent of the Noteholders, the Receiptholders and the Couponholders, on giving prior notice to the Agent, Euroclear and Clearstream, Luxembourg and at least 30 days' prior notice to the Noteholders in accordance with Condition 14, elect that, with effect from the Redenomination Date specified in the notice, the Notes shall be redenominated in euro.

The election will have effect as follows:

- (i) the Notes and the Receipts shall be deemed to be redenominated into euro in the denomination of euro 0.01 with a principal amount for each Note and Receipt equal to the principal amount of that Note or Receipt in the Specified Currency, converted into euro at the Established Rate, provided that, if the Issuer determines, with the agreement of the Agent, that the then market practice in respect of the redenomination into euro of internationally offered securities is different from the provisions specified above, such provisions shall be deemed to be amended so as to comply with such market practice and the Issuer shall promptly notify the Noteholders, the stock exchange (if any) on which the Notes may be listed and the Paying Agents of such deemed amendments;
 - (ii) save to the extent that an Exchange Notice has been given in accordance with paragraph (iv) below, the amount of interest due in respect of the Notes will be calculated by reference to the aggregate principal amount of Notes presented (or, as the case may be, in respect of which Coupons are presented) for payment by the relevant holder and the amount of such payment shall be rounded down to the nearest euro 0.01;
 - (iii) if definitive Notes are required to be issued after the Redenomination Date, they shall be issued at the expense of the Issuer in the denominations of euro 1,000, euro 10,000, euro 100,000 and (but only to the extent of any remaining amounts less than euro 1,000 or such smaller denominations as the Agent may approve) euro 0.01 and such other denominations as the Agent shall determine and notify to the Noteholders;
 - (iv) if issued prior to the Redenomination Date, all unmatured Coupons denominated in the Specified Currency (whether or not attached to the Notes) will become void with effect from the date on which the Issuer gives notice (the “*Exchange Notice*”) that replacement euro-denominated Notes, Receipts and Coupons are available for exchange (provided that such securities are so available) and no payments will be made in respect of them. The payment obligations contained in any Notes and Receipts so issued will also become void on that date although those Notes and Receipts will continue to constitute valid exchange obligations of the Issuer. New euro-denominated Notes, Receipts and Coupons will be issued in exchange for Notes, Receipts and Coupons denominated in the Specified Currency in such manner as the Agent may specify and as shall be notified to the Noteholders in the Exchange Notice. No Exchange Notice may be given less than 15 days prior to any date for payment of principal or interest on the Notes;
 - (v) after the Redenomination Date, all payments in respect of the Notes, the Receipts and the Coupons, other than payments of interest in respect of periods commencing before the Redenomination Date, will be made solely in euro as though references in the Notes to the Specified Currency were to euro. Payments will be made in euro by credit or transfer to a euro account (or any other account to which euro may be credited or transferred) specified by the payee or, at the option of the payee, by a euro cheque;
 - (vi) if the Notes are Fixed Rate Notes and interest for any period ending on or after the Redenomination Date is required to be calculated for a period ending other than on an Interest Payment Date, it will be calculated by applying the Rate of Interest to each Specified Denomination, multiplying such sum by the applicable Day Count Fraction, and rounding the resultant figure to the nearest sub-unit of the relevant Specified Currency, half of any such sub-unit being rounded upwards or otherwise in accordance with applicable market convention;
 - (vii) if the Notes are Floating Rate Notes, the applicable Pricing Supplement will specify any relevant changes to the provisions relating to interest;
- (b) *Definitions*

In these Conditions, the following expressions have the following meanings:

“Established Rate” means the rate for the conversion of the Specified Currency (including compliance with rules relating to roundings in accordance with applicable European Community regulations) into euro established by the Council of the European Union pursuant to Article 123 of the Treaty;

“euro” means the currency introduced at the start of the third stage of European economic and monetary union pursuant to the Treaty;

“Redenomination Date” means (in the case of interest bearing Notes) any date for payment of interest under the Notes or (in the case of Zero Coupon Notes) any date, in each case specified by the Issuer in the notice given to the Noteholders pursuant to paragraph (a) above and which falls on or after the date on which the country of the Specified Currency first participates in the third stage of European economic and monetary union; and

“Treaty” means the Treaty establishing the European Community, as amended.

5. INTEREST

(a) *Interest on Fixed Rate Notes*

Each Fixed Rate Note bears interest on its outstanding nominal amount (or, if it is a Partly Paid Note, the amount paid up) from (and including) the Interest Commencement Date at the rate(s) per annum equal to the Rate(s) of Interest. Interest will be payable in arrear on the Interest Payment Date(s) in each year up to (and including) the Maturity Date.

Except as provided in the applicable Pricing Supplement, the amount of interest payable on each Interest Payment Date in respect of the Fixed Interest Period ending on (but excluding) such date will amount to the Fixed Coupon Amount. Payments of interest on any Interest Payment Date will, if so specified in the applicable Pricing Supplement, amount to the Broken Amount so specified.

As used in these Terms and Conditions, **“Fixed Interest Period”** means the period from (and including) an Interest Payment Date (or the Interest Commencement Date) to (but excluding) the next (or first) Interest Payment Date.

If interest is required to be calculated for a period other than a Fixed Interest Period, such interest shall be calculated by applying the Rate of Interest to each Specified Denomination, multiplying such sum by the applicable Day Count Fraction, and rounding the resultant figure to the nearest sub-unit of the relevant Specified Currency, half of any such sub-unit being rounded upwards or otherwise in accordance with applicable market convention.

“Day Count Fraction” means, in respect of the calculation of an amount of interest in accordance with this Condition 5(a):

(i) if **“Actual/Actual (ISMA)”** is specified in the applicable Pricing Supplement:

(a) in the case of Notes where the number of days in the relevant period from (and including) the most recent Interest Payment Date (or, if none, the Interest Commencement Date) to (but excluding) the relevant payment date (the **“Accrual Period”**) is equal to or shorter than the Determination Period during which the Accrual Period ends, the number of days in such Accrual Period divided by the product of (1) the number of days in such Determination Period and (2) the number of Determination Dates (as specified in the applicable Pricing Supplement) that would occur in one calendar year; or

(b) in the case of Notes where the Accrual Period is longer than the Determination Period during which the Accrual Period ends, the sum of:

(1) the number of days in such Accrual Period falling in the Determination Period in which the Accrual Period begins divided by the product of (x) the number of days

in such Determination Period and (y) the number of Determination Dates that would occur in one calendar year; and

- (2) the number of days in such Accrual Period falling in the next Determination Period divided by the product of (x) the number of days in such Determination Period and (y) the number of Determination Dates that would occur in one calendar year; and
- (ii) if “30/360” is specified in the applicable Pricing Supplement, the number of days in the period from (and including) the most recent Interest Payment Date (or, if none, the Interest Commencement Date) to (but excluding) the relevant payment date (such number of days being calculated on the basis of a year of 360 days with 12 30-day months) divided by 360.

In these Terms and Conditions:

“**Determination Period**” means each period from (and including) a Determination Date to but excluding the next Determination Date (including, where either the Interest Commencement Date or the final Interest Payment Date is not a Determination Date, the period commencing on the first Determination Date prior to, and ending on the first Determination Date falling after, such date) ; and

“**sub-unit**” means, with respect to any currency other than euro, the lowest amount of such currency that is available as legal tender in the country of such currency and, with respect to euro, one cent.

(b) *Interest on Floating Rate Notes and Index Linked Interest Notes*

(i) *Interest Payment Dates*

Each Floating Rate Note and Index Linked Interest Note bears interest on its outstanding nominal amount (or, if it is a Partly Paid Note, the amount paid up) from (and including) the Interest Commencement Date and such interest will be payable in arrear on either:

- (A) the Specified Interest Payment Date(s) in each year specified in the applicable Pricing Supplement; or
- (B) if no Specified Interest Payment Date(s) is/are specified in the applicable Pricing Supplement, each date (each such date, together with each Specified Interest Payment Date, an “**Interest Payment Date**”) which falls the number of months or other period specified as the Specified Period in the applicable Pricing Supplement after the preceding Interest Payment Date or, in the case of the first Interest Payment Date, after the Interest Commencement Date.

Such interest will be payable in respect of each Interest Period (which expression shall, in these Terms and Conditions, mean the period from (and including) an Interest Payment Date (or the Interest Commencement Date) to (but excluding) the next (or first) Interest Payment Date).

If a Business Day Convention is specified in the applicable Pricing Supplement and (x) if there is no numerically corresponding day on the calendar month in which an Interest Payment Date should occur or (y) if any Interest Payment Date would otherwise fall on a day which is not a Business Day, then, if the Business Day Convention specified is:

- (1) in any case where Specified Periods are specified in accordance with Condition 5(b)(i)(B) above, the Floating Rate Convention, such Interest Payment Date (i) in the case of (x) above, shall be the last day that is a Business Day in the relevant month and the provisions of (B) below shall apply *mutatis mutandis* or (ii) in the case of (y) above, shall be postponed to the next day which is a Business Day unless it would thereby fall into the next calendar month, in which event (A) such Interest Payment Date shall be brought forward to the immediately preceding Business Day and (B) each subsequent Interest Payment Date shall be the last Business Day in the month which falls the Specified Period after the preceding applicable Interest Payment Date occurred; or

- (2) the Following Business Day Convention, such Interest Payment Date shall be postponed to the next day which is a Business Day; or
- (3) the Modified Following Business Day Convention, such Interest Payment Date shall be postponed to the next day which is a Business Day unless it would thereby fall into the next calendar month, in which event such Interest Payment Date shall be brought forward to the immediately preceding Business Day; or
- (4) the Preceding Business Day Convention, such Interest Payment Date shall be brought forward to the immediately preceding Business Day.

In these Terms and Conditions, “**Business Day**” means a day which is both:

- (A) a day on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealing in foreign exchange and foreign currency deposits) in London and any Additional Business Centre specified in the applicable Pricing Supplement; and
- (B) either (1) in relation to any sum payable in a Specified Currency other than euro, a day on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealing in foreign exchange and foreign currency deposits) in the principal financial centre of the country of the relevant Specified Currency (if other than London and any Additional Business Centre and which if the Specified Currency is Australian dollars or New Zealand dollars shall be Sydney or Auckland, respectively) or (2) in relation to any sum payable in euro, a day on which the Trans-European Automated Real-Time Gross Settlement Express Transfer (TARGET) System (the “**TARGET System**”) is open.

(ii) *Rate of Interest*

The Rate of Interest payable from time to time in respect of Floating Rate Notes and Index Linked Interest Notes will be determined in the manner specified in the applicable Pricing Supplement.

(A) *ISDA Determination for Floating Rate Notes*

Where ISDA Determination is specified in the applicable Pricing Supplement as the manner in which the Rate of Interest is to be determined, the Rate of Interest for each Interest Period will be the relevant ISDA Rate plus or minus (as indicated in the applicable Pricing Supplement) the Margin (if any). For the purposes of this subparagraph (A), “**ISDA Rate**” for an Interest Period means a rate equal to the Floating Rate that would be determined by the Agent under an interest rate swap transaction if the Agent were acting as Calculation Agent for that swap transaction under the terms of an agreement incorporating the 2000 ISDA Definitions, as published by the International Swaps and Derivatives Association, Inc. and as amended and updated as at the Issue Date of the first Tranche of the Notes (the “**ISDA Definitions**”) and under which:

- (1) the Floating Rate Option is as specified in the applicable Pricing Supplement;
- (2) the Designated Maturity is a period specified in the applicable Pricing Supplement; and
- (3) the relevant Reset Date is either (i) if the applicable Floating Rate Option is based on the London inter-bank offered rate (“**LIBOR**”) or on the Euro-zone inter-bank offered rate (“**EURIBOR**”), the first day of that Interest Period or (ii) in any other case, as specified in the applicable Pricing Supplement.

For the purposes of this sub-paragraph (A), “**Floating Rate**”, “**Calculation Agent**”, “**Floating Rate Option**”, “**Designated Maturity**” and “**Reset Date**” have the meanings given to those terms in the ISDA Definitions.

(B) *Screen Rate Determination for Floating Rate Notes*

Where Screen Rate Determination is specified in the applicable Pricing Supplement as the manner in which the Rate of Interest is to be determined, the Rate of Interest for each Interest Period will, subject as provided below, be either:

- (1) the offered quotation; or
- (2) the arithmetic mean (rounded if necessary to the fifth decimal place, with 0.000005 being rounded upwards) of the offered quotations,

(expressed as a percentage rate per annum) for the Reference Rate which appears or appear, as the case may be, on the Relevant Screen Page as at 11.00 a.m. (London time, in the case of LIBOR, or Brussels time, in the case of EURIBOR) on the Interest Determination Date in question plus or minus (as indicated in the applicable Pricing Supplement) the Margin (if any), all as determined by the Agent. If five or more of such offered quotations are available on the Relevant Screen Page, the highest (or, if there is more than one such highest quotation, one only of such quotations) and the lowest (or, if there is more than one such lowest quotation, one only of such quotations) shall be disregarded by the Agent for the purpose of determining the arithmetic mean (rounded as provided above) of such offered quotations.

The Agency Agreement contains provisions for determining the Rate of Interest in the event that the Relevant Screen Page is not available or if, in the case of (1) above, no such offered quotation appears or, in the case of (2) above, fewer than three such offered quotations appear, in each case as at the time specified in the preceding paragraph.

If the Reference Rate from time to time in respect of Floating Rate Notes is specified in the applicable Pricing Supplement as being other than LIBOR or EURIBOR, the Rate of Interest in respect of such Notes will be determined as provided in the applicable Pricing Supplement.

(iii) *Minimum Rate of Interest and/or Maximum Rate of Interest*

If the applicable Pricing Supplement specifies a Minimum Rate of Interest for any Interest Period, then, in the event that the Rate of Interest in respect of such Interest Period determined in accordance with the provisions of paragraph (ii) above is less than such Minimum Rate of Interest, the Rate of Interest for such Interest Period shall be such Minimum Rate of Interest.

If the applicable Pricing Supplement specifies a Maximum Rate of Interest for any Interest Period, then, in the event that the Rate of Interest in respect of such Interest Period determined in accordance with the provisions of paragraph (ii) above is greater than such Maximum Rate of Interest, the Rate of Interest for such Interest Period shall be such Maximum Rate of Interest.

(iv) *Determination of Rate of Interest and calculation of Interest Amounts*

The Agent, in the case of Floating Rate Notes, and the Calculation Agent, in the case of Index Linked Interest Notes, will at or as soon as practicable after each time at which the Rate of Interest is to be determined, determine the Rate of Interest for the relevant Interest Period. In the case of Index Linked Interest Notes, the Calculation Agent will notify the Agent of the Rate of Interest for the relevant Interest Period as soon as practicable after calculating the same.

The Agent will calculate the amount of interest (the “**Interest Amount**”) payable on the Floating Rate Notes or Index Linked Interest Notes in respect of each Specified Denomination

for the relevant Interest Period. Each Interest Amount shall be calculated by applying the Rate of Interest to each Specified Denomination, multiplying such sum by the applicable Day Count Fraction, and rounding the resultant figure to the nearest sub-unit of the relevant Specified Currency, half of any such sub-unit being rounded upwards or otherwise in accordance with applicable market convention.

“Day Count Fraction” means, in respect of the calculation of an amount of interest in accordance with this Condition 5(b):

- (i) if “Actual/365” or “Actual/Actual” is specified in the applicable Pricing Supplement, the actual number of days in the Interest Period divided by 365 (or, if any portion of that Interest Period falls in a leap year, the sum of (A) the actual number of days in that portion of the Interest Period falling in a leap year divided by 366 and (B) the actual number of days in that portion of the Interest Period falling in a non-leap year divided by 365);
 - (ii) if “Actual/365 (Fixed)” is specified in the applicable Pricing Supplement, the actual number of days in the Interest Period divided by 365;
 - (iii) if “Actual/365 (Sterling)” is specified in the applicable Pricing Supplement, the actual number of days in the Interest Period divided by 365 or, in the case of an Interest Payment Date falling in a leap year, 366;
 - (iv) if “Actual/360” is specified in the applicable Pricing Supplement, the actual number of days in the Interest Period divided by 360;
 - (v) if “30/360”, “360/360” or “Bond Basis” is specified in the applicable Pricing Supplement, the number of days in the Interest Period divided by 360 (the number of days to be calculated on the basis of a year of 360 days with 12 30-day months (unless (a) the last day of the Interest Period is the 31st day of a month but the first day of the Interest Period is a day other than the 30th or 31st day of a month, in which case the month that includes that last day shall not be considered to be shortened to a 30-day month, or (b) the last day of the Interest Period is the last day of the month of February, in which case the month of February shall not be considered to be lengthened to a 30-day month)); and
 - (vi) if “30E/360” or “Eurobond Basis” is specified in the applicable Pricing Supplement, the number of days in the Interest Period divided by 360 (the number of days to be calculated on the basis of a year of 360 days with 12 30-day months, without regard to the date of the first day or last day of the Interest Period unless, in the case of the final Interest Period, the Maturity Date is the last day of the month of February, in which case the month of February shall not be considered to be lengthened to a 30-day month).
- (v) *Notification of Rate of Interest and Interest Amounts*

The Agent will cause the Rate of Interest and each Interest Amount for each Interest Period and the relevant Interest Payment Date to be notified to the Issuer and any stock exchange on which the relevant Floating Rate Notes or Index Linked Interest Notes are for the time being listed and notice thereof to be published in accordance with Condition 14 as soon as possible after their determination but in no event later than the fourth London Business Day thereafter. Each Interest Amount and Interest Payment Date so notified may subsequently be amended (or appropriate alternative arrangements made by way of adjustment) without prior notice in the event of an extension or shortening of the Interest Period. Any such amendment will be promptly notified to each stock exchange on which the relevant Floating Rate Notes or Index Linked Interest Notes are for the time being listed and to the Noteholders in accordance with Condition 14. For the purposes of this paragraph, the expression **“London Business Day”**

means a day (other than a Saturday or a Sunday) on which banks and foreign exchange markets are open for general business in London.

(vi) *Certificates to be final*

All certificates, communications, opinions, determinations, calculations, quotations and decisions given, expressed, made or obtained for the purposes of the provisions of this Condition 5(b), whether by the Agent or, if applicable, the Calculation Agent, shall (in the absence of wilful default, bad faith or manifest error) be binding on the Issuer, the Agent, the Calculation Agent (if applicable), the other Paying Agents and all Noteholders, Receiptholders and Couponholders and (in the absence as aforesaid) no liability to the Issuer, the Noteholders, the Receiptholders or the Couponholders shall attach to the Agent or the Calculation Agent (if applicable) in connection with the exercise or non-exercise by it of its powers, duties and discretions pursuant to such provisions.

(c) *Interest on Dual Currency Interest Notes*

The rate or amount of interest payable in respect of Dual Currency Interest Notes shall be determined in the manner specified in the applicable Pricing Supplement.

(d) *Interest on Partly Paid Notes*

In the case of Partly Paid Notes (other than Partly Paid Notes which are Zero Coupon Notes), interest will accrue as aforesaid on the paid-up nominal amount of such Notes and otherwise as specified in the applicable Pricing Supplement.

(e) *Accrual of interest*

Each Note (or in the case of the redemption of part only of a Note, that part only of such Note) will cease to bear interest (if any) from the date for its redemption unless, upon due presentation thereof, payment of principal is improperly withheld or refused. In such event, interest will continue to accrue until whichever is the earlier of:

- (1) the date on which all amounts due in respect of such Note have been paid; and
- (2) five days after the date on which the full amount of the moneys payable in respect of such Note has been received by the Agent and notice to that effect has been given to the Noteholders in accordance with Condition 14.

6. PAYMENTS

(a) *Method of payment*

Subject as provided below:

- (i) payments in a Specified Currency other than euro will be made by credit or transfer to an account in the relevant Specified Currency (which, in the case of a payment in Japanese yen to a non-resident of Japan, shall be a non-resident account) maintained by the payee with, or, at the option of the payee, by a cheque in such Specified Currency drawn on, a bank in the principal financial centre of the country of such Specified Currency (which, if the Specified Currency is Australian dollars or New Zealand dollars, shall be Sydney and Auckland, respectively); and
- (ii) payments in euro will be made by credit or transfer to a euro account (or any other account to which euro may be credited or transferred) specified by the payee or, at the option of the payee, by a euro cheque.

Payments will be subject in all cases to any fiscal or other laws and regulations applicable thereto in the place of payment, but without prejudice to the provisions of Condition 8.

(b) *Presentation of definitive Notes, Receipts and Coupons*

Payments of principal in respect of definitive Notes will (subject as provided below) be made in the manner provided in paragraph (a) above only against presentation and surrender (or, in the case of part payment of any sum due, endorsement) of definitive Notes, and payments of interest in respect of definitive Notes will (subject as provided below) be made as aforesaid only against presentation and surrender (or, in the case of part payment of any sum due, endorsement) of Coupons, in each case at the specified office of any Paying Agent outside the United States (which expression, as used herein, means the United States of America (including the States and the District of Columbia, its territories, its possessions and other areas subject to its jurisdiction)).

Payments of instalments of principal (if any) in respect of definitive Notes, other than the final instalment, will (subject as provided below) be made in the manner provided in paragraph (a) above against presentation and surrender (or, in the case of part payment of any sum due, endorsement) of the relevant Receipt in accordance with the preceding paragraph. Payment of the final instalment will be made in the manner provided in paragraph (a) above only against presentation and surrender (or, in the case of part payment of any sum due, endorsement) of the relevant Note in accordance with the preceding paragraph. Each Receipt must be presented for payment of the relevant instalment together with the definitive Note to which it appertains. Receipts presented without the definitive Note to which they appertain do not constitute valid obligations of the Issuer. Upon the date on which any definitive Note becomes due and repayable, unmatured Receipts (if any) relating thereto (whether or not attached) shall become void and no payment shall be made in respect thereof.

Fixed Rate Notes in definitive form (other than Dual Currency Notes, Index Linked Notes or Long Maturity Notes (as defined below)) should be presented for payment together with all unmatured Coupons appertaining thereto (which expression shall for this purpose include Coupons falling to be issued on exchange of matured Talons), failing which the amount of any missing unmatured Coupon (or, in the case of payment not being made in full, the same proportion of the amount of such missing unmatured Coupon as the sum so paid bears to the sum due) will be deducted from the sum due for payment. Each amount of principal so deducted will be paid in the manner mentioned above against surrender of the relative missing Coupon at any time before the expiry of 10 years after the Relevant Date (as defined in Condition 8) in respect of such principal (whether or not such Coupon would otherwise have become void under Condition 9) or, if later, five years from the date on which such Coupon would otherwise have become due, but in no event thereafter.

Upon any Fixed Rate Note in definitive form becoming due and repayable prior to its Maturity Date, all unmatured Talons (if any) appertaining thereto will become void and no further Coupons will be issued in respect thereof.

Upon the date on which any Floating Rate Note, Dual Currency Note, Index Linked Note or Long Maturity Note in definitive form becomes due and repayable, unmatured Coupons and Talons (if any) relating thereto (whether or not attached) shall become void and no payment or, as the case may be, exchange for further Coupons shall be made in respect thereof. A “**Long Maturity Note**” is a Fixed Rate Note (other than a Fixed Rate Note which on issue had a Talon attached) whose nominal amount on issue is less than the aggregate interest payable thereon provided that such Note shall cease to be a Long Maturity Note on the Interest Payment Date on which the aggregate amount of interest remaining to be paid after that date is less than the nominal amount of such Note.

If the due date for redemption of any definitive Note is not an Interest Payment Date, interest (if any) accrued in respect of such Note from (and including) the preceding Interest Payment Date or, as the case may be, the Interest Commencement Date shall be payable only against surrender of the relevant definitive Note.

(c) *Payments in respect of Global Notes*

Payments of principal and interest (if any) in respect of Notes represented by any Global Note will (subject as provided below) be made in the manner specified above in relation to definitive Notes and otherwise in the manner specified in the relevant Global Note against presentation or surrender, as the case may be, of such Global Note at the specified office of any Paying Agent outside the United States. A record of each payment made against presentation or surrender of any Global Note, distinguishing between any payment of principal and any payment of interest, will be made on such Global Note by the Paying Agent to which it was presented and such record shall be prima facie evidence that the payment in question has been made.

(d) *General provisions applicable to payments*

The holder of a Global Note shall be the only person entitled to receive payments in respect of Notes represented by such Global Note and the Issuer will be discharged by payment to, or to the order of, the holder of such Global Note in respect of each amount so paid. Each of the persons shown in the records of Euroclear or Clearstream, Luxembourg as the beneficial holder of a particular nominal amount of Notes represented by such Global Note must look solely to Euroclear or Clearstream, Luxembourg, as the case may be, for his share of each payment so made by the Issuer to, or to the order of, the holder of such Global Note.

Notwithstanding the foregoing provisions of this Condition, if any amount of principal and/or interest in respect of Notes is payable in U.S. dollars, such U.S. dollar payments of principal and/or interest in respect of such Notes will be made at the specified office of a Paying Agent in the United States if:

- (i) the Issuer has appointed Paying Agents with specified offices outside the United States with the reasonable expectation that such Paying Agents would be able to make payment in U.S. dollars at such specified offices outside the United States of the full amount of principal and interest on the Notes in the manner provided above when due;
- (ii) payment of the full amount of such principal and interest at all such specified offices outside the United States is illegal or effectively precluded by exchange controls or other similar restrictions on the full payment or receipt of principal and interest in U.S. dollars; and
- (iii) such payment is then permitted under United States law without involving, in the opinion of the Issuer, adverse tax consequences to the Issuer.

(e) *Payment Day*

If the date for payment of any amount in respect of any Note, Receipt or Coupon is not a Payment Day, the holder thereof shall not be entitled to payment until the next following Payment Day in the relevant place and shall not be entitled to further interest or other payment in respect of such delay. For these purposes, "**Payment Day**" means any day which (subject to Condition 9) is:

- (i) a day on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealing in foreign exchange and foreign currency deposits) in:
 - (A) the relevant place of presentation;
 - (B) London;
 - (C) any Additional Financial Centre specified in the applicable Pricing Supplement; and
- (ii) either (1) in relation to any sum payable in a Specified Currency other than euro, a day on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealing in foreign exchange and foreign currency deposits) in the principal financial centre of the country of the relevant Specified Currency (if other than the place of presentation, London and any Additional Financial Centre and which if the Specified Currency is Australian dollars or New Zealand dollars shall be Sydney or Auckland,

respectively) or (2) in relation to any sum payable in euro, a day on which the TARGET System is open.

(f) *Interpretation of principal and interest*

Any reference in these Terms and Conditions to principal in respect of the Notes shall be deemed to include, as applicable:

- (i) any additional amounts which may be payable with respect to principal under Condition 8;
- (ii) the Final Redemption Amount of the Notes;
- (iii) the Early Redemption Amount of the Notes;
- (iv) the Optional Redemption Amount(s) (if any) of the Notes;
- (v) in relation to Notes redeemable in instalments, the Instalment Amounts;
- (vi) in relation to Zero Coupon Notes, the Amortised Face Amount (as defined in Condition 7(e)); and
- (vii) any premium and any other amounts (other than interest) which may be payable by the Issuer under or in respect of the Notes.

Any reference in these Terms and Conditions to interest in respect of the Notes shall be deemed to include, as applicable, any additional amounts which may be payable with respect to interest under Condition 8.

7. REDEMPTION AND PURCHASE

(a) *Redemption at maturity*

Unless previously redeemed or purchased and cancelled as specified below, each Note (including each Index Linked Redemption Note and Dual Currency Redemption Note) will be redeemed by the Issuer at its Final Redemption Amount specified in, or determined in the manner specified in, the applicable Pricing Supplement in the relevant Specified Currency on the Maturity Date.

(b) *Redemption for tax reasons*

The Notes may be redeemed at the option of the Issuer in whole, but not in part, at any time (if this Note is neither a Floating Rate Note, an Index Linked Interest Note nor a Dual Currency Interest Note) or on any Interest Payment Date (if this Note is either a Floating Rate Note, an Index Linked Interest Note or a Dual Currency Interest Note), on giving not less than 30 nor more than 60 days' notice to the Agent and, in accordance with Condition 14, the Noteholders (which notice shall be irrevocable), if:

- (i) on the occasion of the next payment due under the Notes, the Issuer has or will become obliged to pay additional amounts as provided or referred to in Condition 8 as a result of any change in, or amendment to, the laws or regulations of a Tax Jurisdiction (as defined in Condition 8) or any change in the application or official interpretation of such laws or regulations, which change or amendment becomes effective on or after the date on which agreement is reached to issue the first Tranche of the Notes; and
- (ii) such obligation cannot be avoided by the Issuer taking reasonable measures available to it,

provided that no such notice of redemption shall be given earlier than 90 days prior to the earliest date on which the Issuer would be obliged to pay such additional amounts were a payment in respect of the Notes then due.

Prior to the publication of any notice of redemption pursuant to this Condition, the Issuer shall deliver to the Agent a certificate signed by two Directors of the Issuer stating that the Issuer is entitled to effect such redemption and setting forth a statement of facts showing that the conditions precedent to the right of the Issuer so to redeem have occurred, and an opinion of independent legal advisers of recognised standing to the effect that the Issuer has or will become obliged to pay such additional amounts as a result of such change or amendment.

Notes redeemed pursuant to this Condition 7(b) will be redeemed at their Early Redemption Amount referred to in paragraph (e) below together (if appropriate) with interest accrued to (but excluding) the date of redemption.

(c) *Redemption at the option of the Issuer (Issuer Call)*

If Issuer Call is specified in the applicable Pricing Supplement, the Issuer may, having given:

- (i) not less than 15 nor more than 30 days' notice to the Noteholders in accordance with Condition 14; and
- (ii) not less than 15 days before the giving of the notice referred to in (i), notice to the Agent;

(which notices shall be irrevocable and shall specify the date fixed for redemption), redeem all or some only of the Notes then outstanding on any Optional Redemption Date and at the Optional Redemption Amount(s) specified in, or determined in the manner specified in, the applicable Pricing Supplement together, if appropriate, with interest accrued to (but excluding) the relevant Optional Redemption Date. Any such redemption must be of a nominal amount not less than the Minimum Redemption Amount and not more than the Maximum Redemption Amount, in each case as may be specified in the applicable Pricing Supplement. In the case of a partial redemption of Notes, the Notes to be redeemed ("**Redeemed Notes**") will be selected individually by lot, in the case of Redeemed Notes represented by definitive Notes, and in accordance with the rules of Euroclear and/or Clearstream, Luxembourg, in the case of Redeemed Notes represented by a Global Note, not more than 30 days prior to the date fixed for redemption (such date of selection being hereinafter called the "**Selection Date**"). In the case of Redeemed Notes represented by definitive Notes, a list of the serial numbers of such Redeemed Notes will be published in accordance with Condition 14 not less than 15 days prior to the date fixed for redemption. The aggregate nominal amount of Redeemed Notes represented by definitive Notes shall bear the same proportion to the aggregate nominal amount of all Redeemed Notes as the aggregate nominal amount of definitive Notes outstanding bears to the aggregate nominal amount of the Notes outstanding, in each case on the Selection Date, provided that such first mentioned nominal amount shall, if necessary, be rounded downwards to the nearest integral multiple of the Specified Denomination, and the aggregate nominal amount of Redeemed Notes represented by a Global Note shall be equal to the balance of the Redeemed Notes. No exchange of the relevant Global Note will be permitted during the period from (and including) the Selection Date to (and including) the date fixed for redemption pursuant to this paragraph (c) and notice to that effect shall be given by the Issuer to the Noteholders in accordance with Condition 14 at least five days prior to the Selection Date.

(d) *Redemption at the option of the Noteholders (Investor Put)*

If Investor Put is specified in the applicable Pricing Supplement, upon the holder of any Note giving to the Issuer in accordance with Condition 14 not less than 15 nor more than 30 days' notice the Issuer will, upon the expiry of such notice, redeem, subject to, and in accordance with, the terms specified in the applicable Pricing Supplement, such Note on the Optional Redemption Date and at the Optional Redemption Amount together, if appropriate, with interest accrued to (but excluding) the Optional Redemption Date.

To exercise the right to require redemption of this Note the holder of this Note must, if this Note is in definitive form and held outside Euroclear and Clearstream, Luxembourg, deliver, at the specified office of any Paying Agent at any time during normal business hours of such Paying Agent falling

within the notice period, a duly completed and signed notice of exercise in the form (for the time being current) obtainable from any specified office of any Paying Agent (a “**Put Notice**”) and in which the holder must specify a bank account (or, if payment is required to be made by cheque, an address) to which payment is to be made under this Condition accompanied by, if this Note is in definitive form, this Note or evidence satisfactory to the Paying Agent concerned that this Note will, following delivery of the Put Notice, be held to its order or under its control. If this Note is represented by a Global Note or is in definitive form and held through Euroclear or Clearstream, Luxembourg, to exercise the right to require redemption of this Note the holder of this Note must, within the notice period, give notice to the Agent of such exercise in accordance with the standard procedures of Euroclear and Clearstream, Luxembourg (which may include notice being given on his instruction by Euroclear or Clearstream, Luxembourg or any common depositary for them to the Agent by electronic means) in a form acceptable to Euroclear and Clearstream, Luxembourg from time to time and, if this Note is represented by a Global Note, at the same time present or procure the presentation of the relevant Global Note to the Agent for notation accordingly.

Any Put Notice given by a holder of any Note pursuant to this paragraph shall be irrevocable except where prior to the due date of redemption an Event of Default shall have occurred and be continuing in which event such holder, at its option, may elect by notice to the Issuer to withdraw the notice given pursuant to this paragraph and instead to declare such Note forthwith due and payable pursuant to Condition 10.

(e) *Early Redemption Amounts*

For the purpose of paragraph (b) above and Condition 10, each Note will be redeemed at its Early Redemption Amount calculated as follows:

- (i) in the case of a Note with a Final Redemption Amount equal to the Issue Price, at the Final Redemption Amount thereof;
- (ii) in the case of a Note (other than a Zero Coupon Note but including an Instalment Note and a Partly Paid Note) with a Final Redemption Amount which is or may be less or greater than the Issue Price or which is payable in a Specified Currency other than that in which the Note is denominated, at the amount specified in, or determined in the manner specified in, the applicable Pricing Supplement or, if no such amount or manner is so specified in the applicable Pricing Supplement, at its nominal amount; or
- (iii) in the case of a Zero Coupon Note, at an amount (the “**Amortised Face Amount**”) calculated in accordance with the following formula:

$$\text{Early Redemption Amount} = \text{RP} \times (1 + \text{AY})^y$$

where:

“**RP**” means the Reference Price;

“**AY**” means the Accrual Yield expressed as a decimal; and

“**y**” is a fraction the numerator of which is equal to the number of days (calculated on the basis of a 360-day year consisting of 12 months of 30 days each) from (and including) the Issue Date of the first Tranche of the Notes to (but excluding) the date fixed for redemption or (as the case may be) the date upon which such Note becomes due and repayable and the denominator of which is 360,

or on such other calculation basis as may be specified in the applicable Pricing Supplement.

(f) *Instalments*

Instalment Notes will be redeemed in the Instalment Amounts and on the Instalment Dates. In the case of early redemption, the Early Redemption Amount will be determined pursuant to paragraph (e) above.

(g) *Partly Paid Notes*

Partly Paid Notes will be redeemed, whether at maturity, early redemption or otherwise, in accordance with the provisions of this Condition and the applicable Pricing Supplement.

(h) *Purchases*

The Issuer or any Subsidiary of the Issuer may at any time purchase Notes (provided that, in the case of definitive Notes, all unmaturing Receipts, Coupons and Talons appertaining thereto are purchased therewith) at any price in the open market or otherwise. If purchases are made by tender, tenders must be available to all Noteholders alike. Such Notes may be held, reissued, resold or, at the option of the Issuer, surrendered to any Paying Agent for cancellation.

(i) *Cancellation*

All Notes which are redeemed will forthwith be cancelled (together with all unmaturing Receipts, Coupons and Talons attached thereto or surrendered therewith at the time of redemption). All Notes so cancelled and any Notes purchased and cancelled pursuant to paragraph (h) above (together with all unmaturing Receipts, Coupons and Talons cancelled therewith) shall be forwarded to the Agent and cannot be reissued or resold.

(j) *Late payment on Zero Coupon Notes*

If the amount payable in respect of any Zero Coupon Note upon redemption of such Zero Coupon Note pursuant to paragraph (a), (b), (c) or (d) above or upon its becoming due and repayable as provided in Condition 10 is improperly withheld or refused, the amount due and repayable in respect of such Zero Coupon Note shall be the amount calculated as provided in paragraph (e)(iii) above as though the references therein to the date fixed for the redemption or the date upon which such Zero Coupon Note becomes due and payable were replaced by references to the date which is the earlier of:

- (i) the date on which all amounts due in respect of such Zero Coupon Note have been paid; and
- (ii) five days after the date on which the full amount of the moneys payable in respect of such Zero Coupon Notes has been received by the Agent and notice to that effect has been given to the Noteholders in accordance with Condition 14.

8. TAXATION

All payments of principal and interest in respect of the Notes, Receipts and Coupons by the Issuer will be made without withholding or deduction for or on account of any present or future duties of whatever nature imposed or levied by or on behalf of any Tax Jurisdiction unless such withholding or deduction is required by law. In such event, the Issuer will pay such additional amounts as shall be necessary in order that the net amounts received by the holders of the Notes, Receipts or Coupons after such withholding or deduction shall equal the respective amounts of principal and interest which would otherwise have been receivable in respect of the Notes, Receipts or Coupons, as the case may be, in the absence of such withholding or deduction; except that no such additional amounts shall be payable with respect to any Note, Receipt or Coupon:

- (i) presented for payment by or on behalf of a holder who is liable for such taxes or duties in respect of such Note, Receipt or Coupon by reason of his having some connection with a Tax Jurisdiction other than the mere holding of such Note, Receipt or Coupon; or
- (ii) presented for payment more than 30 days after the Relevant Date (as defined below) except to the extent that the holder thereof would have been entitled to an additional amount on presenting the same for payment on such thirtieth day assuming that day to have been a Payment Day (as defined in Condition 6(e)); or
- (iii) where such withholding or deduction is imposed on a payment to an individual and is required to be made pursuant to any European Union Directive on the taxation of savings implementing the conclusions of the ECOFIN Council meeting of 26th-27th November 2000 (the “**Directive**”) or any law implementing or complying with, or introduced in order to conform to, the Directive; or
- (iv) presented for payment by or on behalf of a holder who would have been able to avoid such withholding or deduction by presenting the relevant Note, Receipt or Coupon to another Paying Agent in a Member State of the European Union.

As used herein:

- (A) “**Tax Jurisdiction**” means Iceland or any political subdivision or any authority thereof or therein having power to tax or any other jurisdiction or any political subdivision or any authority thereof or therein having power to tax to which the Issuer becomes subject in respect of payments made by it of principal and interest on the Notes, Receipts and Coupons; and
- (B) “**Relevant Date**” means the date on which such payment first becomes due, except that, if the full amount of the moneys payable has not been duly received by the Agent on or prior to such due date, it means the date on which, the full amount of such moneys having been so received, notice to that effect is duly given to the Noteholders in accordance with Condition 14.

9. PRESCRIPTION

The Notes, Receipts and Coupons will become void unless presented for payment within a period of 10 years (in the case of principal) and five years (in the case of interest) after the Relevant Date (as defined in Condition 8) therefor.

There shall not be included in any Coupon sheet issued on exchange of a Talon any Coupon the claim for payment in respect of which would be void pursuant to this Condition or Condition 6(b) or any Talon which would be void pursuant to Condition 6(b).

10. EVENTS OF DEFAULT

(a) *Events of Default relating to Senior Notes*

If any one or more of the following events (each an “**Event of Default**”) shall occur with respect to any Senior Note:

- (i) if default is made in the payment of any principal, premium (if any) or interest due in respect of the Notes or any of them and the default continues for a period of three days in the case of principal or premium (if any) and seven days in the case of interest; or
- (ii) if the Issuer fails to perform or observe any of its other obligations under these Conditions and (except in any case where the failure is incapable of remedy when no such continuation or notice as is hereinafter mentioned will be required) the failure continues for the period of 30 days next following the service by a Noteholder on the Issuer of notice requiring the same to be remedied; or

- (iii) if any borrowed money of the Issuer or any of its Principal Subsidiaries is not paid when due or becomes (whether by declaration or automatically in accordance with the relevant agreement or instrument constituting the same) due and payable prior to the date when it would otherwise have become due or any creditor of the Issuer or any of its Principal Subsidiaries becomes entitled to declare any such Borrowed Money due and payable or any facility or commitment available to the Issuer or any of its Principal Subsidiaries relating to Borrowed Money is withdrawn, suspended or cancelled by reason of any default (however described) of the company concerned, provided that, for the purposes of this sub-clause (iii), the Borrowed Money must, when aggregated with all other Borrowed Money to which any part of this Condition 10(a)(iii) applies, exceed U.S.\$5,000,000 (or its equivalent in any other currency); or
- (iv) if any order is made by any competent court or resolution passed for the winding up or dissolution of the Issuer or any of its Principal Subsidiaries, save for the purposes of reorganisation on terms approved by an Extraordinary Resolution of the Noteholders; or
- (v) if the Issuer or any of its Principal Subsidiaries ceases or threatens to cease to carry on the whole or a substantial part of its business, save for the purposes of reorganisation on terms approved by an Extraordinary Resolution of the Noteholders, or the Issuer or any of its Principal Subsidiaries stops or threatens to stop payment of, or is unable to, or admits inability to, pay, its debts (or any class of its debts) as they fall due, or is deemed unable to pay its debts pursuant to or for the purposes of any applicable law, or is adjudicated or found bankrupt or insolvent; or
- (vi) if (A) proceedings are initiated against the Issuer or any of its Principal Subsidiaries under any applicable liquidation, insolvency, composition, reorganisation or other similar laws, or an application is made for the appointment of an administrative or other receiver, manager, administrator or other similar official, or an administrative or other receiver, manager, administrator or other similar official is appointed, in relation to the Issuer or any of its Principal Subsidiaries or, as the case may be, in relation to the whole or a part of the undertaking or assets of any of them, or an encumbrancer takes possession of the whole or a part of the undertaking or assets of any of them, or a distress, execution, attachment, sequestration or other process is levied, enforced upon, sued out or put in force against the whole or a part of the undertaking or assets of any of them and (B) in any case (other than the appointment of an administrator) the same is not discharged within 14 days; or
- (vii) if the Issuer or any of its Principal Subsidiaries initiates or consents to judicial proceedings relating to itself under any applicable liquidation, insolvency, composition, reorganisation or other similar laws or makes a conveyance or assignment for the benefit of, or enters into any composition or other arrangement with, its creditors generally (or any class of its creditors) or any meeting is convened to consider a proposal for an arrangement or composition with its creditors generally (or any class of its creditors),

then any holder of a Senior Note may, by written notice to the Issuer at the specified office of the Agent, effective upon the date of receipt thereof by the Agent, declare any Senior Notes held by the holder to be forthwith due and payable whereupon the same shall become forthwith due and payable at its Early Redemption Amount (as described in Condition 7(e)), together with accrued interest (if any) to the date of repayment, without presentment, demand, protest or other notice of any kind.

For the purposes of this Condition:

“Principal Subsidiary” at any time shall mean a Subsidiary of the Issuer inter alia:

- (A) whose gross revenues (consolidated in the case of a Subsidiary which itself has Subsidiaries) or whose total assets (consolidated in the case of a Subsidiary which itself has Subsidiaries) represent not less than five per cent. of the consolidated gross revenues, or, as the case may be, consolidated total assets, of the Issuer and its Subsidiaries taken as a whole, all as calculated

respectively by reference to the then latest audited accounts (consolidated or, as the case may be, unconsolidated) of the Subsidiary and the then latest audited consolidated accounts of the Issuer and its Subsidiaries; or

- (B) to which is transferred the whole or substantially the whole of the undertaking and assets of a Subsidiary of the Issuer which immediately before the transfer is a Principal Subsidiary,

all as more particularly defined in the Agency Agreement.

A report by the Auditors of the Issuer that in their opinion a Subsidiary of the Issuer is or is not or was or was not at any particular time or throughout any specified period a Principal Subsidiary shall, in the absence of manifest error, be conclusive and binding on all parties.

(b) *Enforcement relating to Subordinated Notes*

- (i) If the Issuer fails to meet its obligations under the Subordinated Notes, any Noteholder may, at its own discretion and without further notice, institute proceedings in Iceland for the compulsory winding-up of the Issuer in accordance with Act No. 161/2002 on Commercial Banks and Savings Banks.
- (ii) Any Noteholder may at its discretion and without further notice institute such proceedings against the Issuer as it may think fit to enforce any obligation, condition or provision binding on the Issuer under the Subordinated Notes provided that the Issuer shall not by virtue of the institution of any such proceedings be obliged to pay any sum or sums sooner than the same would otherwise have been payable by it.
- (iii) If an order is made or an effective resolution is passed for the winding-up or liquidation of the Issuer, then the Subordinated Notes shall become due and payable at the Early Redemption Amount together with interest accrued to the date of repayment, without presentment, demand, pretext or other notice of any kind.

11. REPLACEMENT OF NOTES, RECEIPTS, COUPONS AND TALONS

Should any Note, Receipt, Coupon or Talon be lost, stolen, mutilated, defaced or destroyed, it may be replaced at the specified office of the Agent upon payment by the claimant of such costs and expenses as may be incurred in connection therewith and on such terms as to evidence and indemnity as the Issuer may reasonably require. Mutilated or defaced Notes, Receipts, Coupons or Talons must be surrendered before replacements will be issued.

12. PAYING AGENTS

The names of the initial Paying Agents and their initial specified offices are set out below.

The Issuer is entitled to vary or terminate the appointment of any Paying Agent and/or appoint additional or other Paying Agents and/or approve any change in the specified office through which any Paying Agent acts, provided that:

- (a) there will at all times be an Agent; and
- (b) so long as the Notes are listed on any stock exchange, there will at all times be a Paying Agent with a specified office in such place as may be required by the rules and regulations of the relevant stock exchange (or any other relevant authority); and
- (c) if any European Union Directive on the taxation of savings implementing the conclusions of the ECOFIN Council meeting of 26th-27th November, 2000 or any law implementing or complying with, or introduced in order to conform to such Directive is introduced, the Issuer will ensure that it maintains a Paying Agent in a Member State of the European Union that will not be obliged to withhold or deduct tax pursuant to any such Directive or law.

In addition, the Issuer shall forthwith appoint a Paying Agent having a specified office in New York City in the circumstances described in Condition 6(d). Any variation, termination, appointment or change shall only take effect (other than in the case of insolvency, when it shall be of immediate effect) after not less than 30 nor more than 45 days' prior notice thereof shall have been given to the Noteholders in accordance with Condition 14.

In acting under the Agency Agreement, the Paying Agents act solely as agents of the Issuer and do not assume any obligation to, or relationship of agency or trust with, any Noteholders, Receiptholders or Couponholders. The Agency Agreement contains provisions permitting any entity into which any Paying Agent is merged or converted or with which it is consolidated or to which it transfers all or substantially all of its assets to become the successor paying agent.

13. EXCHANGE OF TALONS

On and after the Interest Payment Date on which the final Coupon comprised in any Coupon sheet matures, the Talon (if any) forming part of such Coupon sheet may be surrendered at the specified office of the Agent or any other Paying Agent in exchange for a further Coupon sheet including (if such further Coupon sheet does not include Coupons to (and including) the final date for the payment of interest due in respect of the Note to which it appertains) a further Talon, subject to the provisions of Condition 9.

14. NOTICES

All notices regarding the Notes will be deemed to be validly given if published (i) in a leading English language daily newspaper of general circulation in London, and (ii) if and for so long as the Notes are listed on the Luxembourg Stock Exchange, a daily newspaper of general circulation in Luxembourg. It is expected that such publication will be made in the *Financial Times* in London and the *Luxemburger Wort* or the *Tageblatt* in Luxembourg. The Issuer shall also ensure that notices are duly published in a manner which complies with the rules of any stock exchange (or any other relevant authority) on which the Notes are for the time being listed or by which they have been admitted to listing. Any such notice will be deemed to have been given on the date of the first publication or, where required to be published in more than one newspaper, on the date of the first publication in all required newspapers.

Until such time as any definitive Notes are issued, there may, so long as any Global Notes representing the Notes are held in their entirety on behalf of Euroclear and/or Clearstream, Luxembourg, be substituted for such publication in such newspaper(s) the delivery of the relevant notice to Euroclear and/or Clearstream, Luxembourg for communication by them to the holders of the Notes and, in addition, for so long as any Notes are listed on a stock exchange or are admitted to listing by another relevant authority and the rules of that stock exchange or relevant authority so require, such notice will be published in a daily newspaper of general circulation in the place or places required by those rules. Any such notice shall be deemed to have been given to the holders of the Notes on the seventh day after the day on which the said notice was given to Euroclear and/or Clearstream, Luxembourg.

Notices to be given by any Noteholder shall be in writing and given by lodging the same, together (in the case of any Note in definitive form) with the relative Note or Notes, with the Agent. Whilst any of the Notes are represented by a Global Note, such notice may be given by any holder of a Note to the Agent through Euroclear and/or Clearstream, Luxembourg, as the case may be, in such manner as the Agent and Euroclear and/or Clearstream, Luxembourg, as the case may be, may approve for this purpose.

15. MEETINGS OF NOTEHOLDERS, MODIFICATION AND WAIVER

The Agency Agreement contains provisions for convening meetings of the Noteholders to consider any matter affecting their interests, including the sanctioning by Extraordinary Resolution of a modification of the Notes, the Receipts, the Coupons or any of the provisions of the Agency

Agreement. Such a meeting may be convened by the Issuer or Noteholders holding not less than five per cent. in nominal amount of the Notes for the time being remaining outstanding. The quorum at any such meeting for passing an Extraordinary Resolution is one or more persons holding or representing not less than 50 per cent. in nominal amount of the Notes for the time being outstanding, or at any adjourned meeting one or more persons being or representing Noteholders whatever the nominal amount of the Notes so held or represented, except that at any meeting the business of which includes the modification of certain provisions of the Notes, the Receipts or the Coupons (including modifying the date of maturity of the Notes or any date for payment of interest thereon, reducing or cancelling the amount of principal or the rate of interest payable in respect of the Notes or altering the currency of payment of the Notes, the Receipts or the Coupons), the quorum shall be one or more persons holding or representing not less than two-thirds in nominal amount of the Notes for the time being outstanding, or at any adjourned such meeting one or more persons holding or representing not less than one-third in nominal amount of the Notes for the time being outstanding. An Extraordinary Resolution passed at any meeting of the Noteholders shall be binding on all the Noteholders, whether or not they are present at the meeting, and on all Receiptholders and Couponholders.

The Agent and the Issuer may agree, without the consent of the Noteholders, Receiptholders or Couponholders, to:

- (a) any modification (except as mentioned above) of the Notes, the Receipts, the Coupons or the Agency Agreement which is not prejudicial to the interests of the Noteholders; or
- (b) any modification of the Notes, the Receipts, the Coupons or the Agency Agreement which is of a formal, minor or technical nature or is made to correct a manifest error or to comply with mandatory provisions of the law.

Any such modification shall be binding on the Noteholders, the Receiptholders and the Couponholders and any such modification shall be notified to the Noteholders in accordance with Condition 14 as soon as practicable thereafter.

16. FURTHER ISSUES

The Issuer shall be at liberty from time to time without the consent of the Noteholders, the Receiptholders or the Couponholders to create and issue further notes having terms and conditions the same as the Notes or the same in all respects save for the amount and date of the first payment of interest thereon and so that the same shall be consolidated and form a single Series with the outstanding Notes.

17. CONTRACTS (RIGHTS OF THIRD PARTIES) ACT 1999

No person shall have any right to enforce any term or condition of this Note under the Contracts (Rights of Third Parties) Act 1999, but this does not affect any right or remedy of any person which exists or is available apart from that Act.

18. GOVERNING LAW AND SUBMISSION TO JURISDICTION

(a) *Governing law*

The Agency Agreement, the Deed of Covenant, the Notes (other than Condition 2(b)), the Receipts and the Coupons are governed by, and shall be construed in accordance with, English law. Condition 2(b) of the Notes is governed by, and shall be construed in accordance with, Icelandic law.

(b) *Submission to jurisdiction*

The Issuer agrees, for the exclusive benefit of the Noteholders, the Receiptholders and the Couponholders, that the courts of England are to have jurisdiction to settle any disputes which may arise out of or in connection with the Notes, the Receipts and/or the Coupons and that accordingly any

suit, action or proceedings (together referred to as “*Proceedings*”) arising out of or in connection with the Notes, the Receipts and the Coupons may be brought in such courts.

The Issuer hereby irrevocably waives any objection which it may have now or hereafter to the laying of the venue of any such Proceedings in any such court and any claim that any such Proceedings have been brought in an inconvenient forum and hereby further irrevocably agrees that a judgment in any such Proceedings brought in the English courts shall be conclusive and binding upon it and may be enforced in the courts of any other jurisdiction.

Nothing contained in this Condition shall limit any right to take Proceedings against the Issuer in any other court of competent jurisdiction, nor shall the taking of Proceedings in one or more jurisdictions preclude the taking of Proceedings in any other jurisdiction, whether concurrently or not.

(c) *Appointment of Process Agent*

The Issuer appoints the Ambassador of the Republic of Iceland to the Court of St James’ of 2A Hans Street, London SW1X OJE, England as its agent for service of process, and undertakes that, in the event of the Ambassador ceasing so to act or ceasing to be registered in England, it will appoint another person as its agent for service of process in England in respect of any Proceedings. Nothing herein shall affect the right to serve proceedings in any other manner permitted by law.

(d) *Waiver of immunity*

The Issuer hereby irrevocably and unconditionally waives with respect to Notes, the Receipts and the Coupons any right to claim sovereign or other immunity from jurisdiction or execution and any similar defence and irrevocably and unconditionally consents to the giving of any relief or the issue of any process, including without limitation, the making, enforcement or execution against any property whatsoever (irrespective of its use or intended use) of any order or judgment made or given in connection with any proceedings.

(e) *Other documents*

The Issuer has in the Agency Agreement and the Deed of Covenant submitted to the jurisdiction of the English courts and appointed an agent for service of process in terms substantially similar to those set out above.

USE OF PROCEEDS

The net proceeds from each issue of Notes will be applied by the Issuer for its general corporate purposes.

CAPITALISATION

Capitalisation of the Issuer

The following table sets forth the pro-forma capitalisation of the Issuer as at 31st December, 2002.

	<i>Kaupthing Bunadarbanki Pro forma 31/12/2002</i>
ISK mio	
Equity	
Share capital	4,092
Other equity	29,287
Borrowing	
Issued Bonds	31,026
Loans from credit institutions	70,764
Other borrowings	239
Deposits	164,570
Subordinated Loans	
Tier I	31,868
Tier II	9,765
Total capitalisation	<u><u>341,611</u></u>

Notes:

- (1) There has been no material change in the capitalisation of the Issuer since 31st December, 2002.
- (2) As at 31st December 2002, the authorised and issued share capital of the Issuer was ISK 4,155,000,000 at nominal value was fully paid up and comprised of 415,500,000 ordinary shares.
On 26th May 2003, The Board of Directors of the Issuer is authorised to increase the share capital of the Company by up to ISK 500,000,000 nominal value by issuing up to 50,000,000 new shares for Kaupthing Bunadarbanki. The authorised capital being 4,655,000,000 and issued share capital 4,155,000,000.

Capitalisation of Kaupthing Bank hf.

The following table sets forth the capitalisation of Kaupthing Bank hf. as at 31st December, 2002 and 31st December, 2001.

	<i>Kaupthing</i>			
	<i>Group</i>		<i>Parent</i>	
ISK mio	<i>31/12/2002</i>	<i>31/12/2001</i>	<i>31/12/2002</i>	<i>31/12/2001</i>
Equity				
Share capital	2,124	1,626	2,124	1,626
Other equity	16,198	7,569	16,198	6,569
Borrowing				
Issued Bonds	9,269	8,946	9,299	8,506
Loans from credit institutions	0	15,528	0	10,453
Other borrowings				
Deposits	71,797	10,592	9,158	0
Subordinated Loans				
Tier I	15,608	8,830	17,212	9,195
Tier II	4,343	2,873	4,343	2,873
Total Capitalisation	<u><u>119,339</u></u>	<u><u>55,964</u></u>	<u><u>58,334</u></u>	<u><u>39,222</u></u>

Note:

There has been no material change in the capitalisation of Kaupthing Bank hf. since 31st December, 2002.

Capitalisation of Bunadarbanki Islands hf.

The following table sets forth the capitalisation of Bunadarbanki Islands hf. as at 31st December, 2002 and 31st December, 2001.

ISK mio	<i>Bunadarbanki</i>			
	<i>Group</i>		<i>Parent</i>	
	<i>31/12/2002</i>	<i>31/12/2001</i>	<i>31/12/2002</i>	<i>31/12/2001</i>
Equity				
Share capital	5,351	5,233.3	5,351	5,233.3
Other equity	9,841	7,726.7	9,841	7,725.7
Borrowing				
Issued Bonds	21,757	10,295.9	19,622	7,175.1
Loans from credit institutions	70,764	74,548.4	65,377	64,766.6
Other borrowings	239	432.9	56	58.8
Deposits	92,733	72,881.0	86,924	74,872.0
Subordinated Notes				
Tier I	16,260	14,026	16,250	14,026.0
Tier II	5,422	4,159	5,288	4,159.0
Total capitalisation	222,407	189,301.2	208,709	178,016.5

Note:

There has been no material change in the capitalisation of Bunadarbanki Islands hf. since 31st December, 2002.

DESCRIPTION OF THE ISSUER

General Information

On 26th May, 2003, Kaupthing Bank hf. and Bunadarbanki Islands hf. merged to form Kaupthing Bunadarbanki hf. (the “**Issuer**”). In the merger the surviving entity was Kaupthing Bank hf. By operation of Icelandic law, the Issuer succeeded universally to all the assets, liabilities and rights of Bunadarbanki Islands hf. and is fully liable to honour all the obligations of Bunadarbanki Islands hf. as if it had been an original party thereto, including any obligations in respect of the Notes. At the effective time of the merger, Bunadarbanki Islands hf. ceased to exist as a separate legal entity.

The Issuer comprises of two banks Kaupthing Bank hf. (**Kaupthing Bank hf.**) and Bunadarbanki Islands hf. (**Bunadarbanki Islands**) which both enjoyed strong market positions in Iceland. The share capital of the Issuer is ISK 4,155,000,000 at nominal value or 415,500,000 ordinary shares. The Board of Directors of the Issuer is authorised to increase the share capital of the Company by up to ISK 500,000,000 nominal value by issuing up to 50,000,000 new shares. The Issuer’s total assets amounted to ISK 432 billion (figures refer to pro forma balance sheet of 31st December, 2002). The Issuer is the largest bank in Iceland and a leading player in many areas of the Icelandic financial market. The Issuer has the highest market capitalisation of any company on the Iceland Stock Exchange and amongst the ten largest banks in the Nordic countries. The Issuer operates 36 branches and sub-branches throughout Iceland and operates subsidiaries in nine countries. The total number of bank employee positions at the end of March 2003 was approximately 1260.

The Principal Subsidiaries and Affiliated Companies of the Issuer include the following:

Principal Subsidiaries in Iceland

Rekstrarfélag Veróðrefasjóðs Bunadabanka hf
 Lýsing hf
 Gen hf
 Urður ehf
 BI Management Company S.A. Luxembourg.....
 Vesturvík sf
 ITC Ísland ehf.
 Ráðgjöf Kaupthings ehf.
 Hávöxtunarfélagið hf.
 Ævisjóðurinn hf.
 Kirna ehf.
 Sjávarútvegssjóðurinn hf.
 Sparisjóður Kaupthings
 Arion Custody Services hf.
 Althjoda liftryggingafélagid
 Sóltún ehf.
 Grænabaer

Principal Area of Activity

Management Company
 Leasing Company
 Holding Company
 Holding Company
 Offshore Management Company
 Holding Company
 Service providing Company
 Management Company
 Management Company
 Fund
 Securities Trading Company
 Securities Trading Company
 Saving Bank
 Custody Services Company
 Life Insurance company
 Real Estate Company
 Holding Company

Principal Subsidiaries outside of Iceland:

Kaupthing New York Inc.	
Kaupthing Bank Luxembourg S.A.	International Banking Operation
Kaupthing Management Company S.A.	Management Company
Kaupthing Föroyar Virðisbrævarneklarefelag P/F	Securities Company
Kaupthing Services S.A., Switzerland	
Handsal Asset Management S.A.R.L., Switzerland	Asset Management Company
Kaupthing Bank A/S, Denmark.....	Bank
Alpha Management Company S.A.	Management Company
Kaupthing Sofi Oyj., Finland	Securities Company
Global Arbitrage & Trading S.A., Switzerland	Arbitrage and Trading Company
Kaupthing Limited, London	Corporate Finance Company
Kaupthing Bank Sverige	Bank

Affiliated Companies Principal Area of Activity

Greiðslumiðlun hf	Visa Iceland
Kreditkort hf	Europay Iceland
Reiknisstofa bankanna	Icelandic Banks' Data Centre
Intrum á Íslandi ehf	Debt Collection
Lánstraust hf	Financial Data Company
Scandinavian Holding S.A.	
DSK A/S	

Increasing deregulation in the Icelandic financial markets over the past decade has presented the Issuer with ample growth opportunities. The Issuer now provides comprehensive financial services, retail banking, corporate banking, securities services and investment banking. All this enables the Issuer to be a full participant in the major changes that are taking place in savings and corporate finance in Iceland. Retail banking at the Issuer is built on a firm foundation from its establishment in 1930. The branch network extends to all the most populated parts of Iceland and all the branches operate at a profit.

The Issuer has significantly developed its Internet-based services for individuals and corporations and the Issuer website www.bi.is is the fourth most visited website in Iceland. Self-service Internet use has increased enormously, over 55 per cent. of the Issuer's customers are registered, reflecting the fact that Iceland has one of the highest internet penetrations in the world today. This has led to operational economies within the Issuer because costs have not risen to meet increase in transaction volume, and scope has also been created for streamlining in other areas.

New channels for savings have also been emerging in recent years, through pension funds and domestic and international securities funds. Through the development of its asset management and foreign securities units, the Issuer has been engaged in this evolution, which undoubtedly will continue in the years to come. The Asset Management unit offers private banking services and runs both securities funds- and pension schemes.

A brief history of the Issuer

The Issuer can trace its roots back to 1929 when the Icelandic parliament, the Althing, approved the founding of Bunadarbanks Islands, which formally commenced operations on 1st July, 1930.

During the next few decades Bunadarbanks Islands flourished in an atmosphere of increasing prosperity in Iceland. During the 1960s, operations underwent considerable change as Bunadarbanks Islands began to expand into rural areas and open up branches, usually by taking over local savings banks. Several restrictions on the Icelandic capital market were lifted during the next few years and Bunadarbanks Islands was one of many organisations to benefit. In 1982, for example, the Ministry of Commerce granted Bunadarbanks Islands the long-awaited licence for foreign exchange trading, and in 1986 new laws concerning the Central Bank of Iceland came into force, giving the commercial banks almost total freedom to set interest rates. In 1992 sweeping changes were made, when restrictions were lifted on foreign exchange

trading in connection with imports and exports and other movements of capital. The decades of government control of movements of capital to and from Iceland finally came to an end at the beginning of 1995.

Over the years Bunadarbanki Islands became an associate of several companies, including the Icelandic Banks' Data Centre and VISA-Iceland. At the beginning of 1998 Bunadarbanki Islands became a limited liability company and work began on privatising the company. This was completed in 2003 in stages.

Kaupthing Bank was founded by eight Icelanders in February 1982, or when the Icelandic financial market was just beginning to open up. Kaupthing Bank flourished along with the Icelandic financial market. In 1986 the founding members sold 49 per cent. of their shares to the Icelandic savings banks. The same year, 1986, the Iceland Stock Exchange began operations, with Kaupthing Bank as one of the five founding partners. Four years later, in 1990, Bunadarbanki Islands acquired 50 per cent. of the shares in Kaupthing Bank, thereby receiving an equal holding to the savings banks, which at the same time increased their holdings by 1 per cent. In 1996, the Icelandic savings banks acquired the remaining shares in Kaupthing Bank from Bunadarbanki Islands. The ownership of Kaupthing Bank remained virtually unchanged until September 2000 when Kaupthing Bank was listed on the Iceland Stock Exchange. Following the listing, the Icelandic savings banks reduced their holdings, while individuals and institutional investors increased their stakes.

Kaupthing Bank has grown rapidly since 1995, performing a key role on the Icelandic investment banking market. Kaupthing Bank opened the first international mutual fund in Iceland and was the first Icelandic financial company to establish an overseas subsidiary (in Luxembourg). Kaupthing Bank was granted an investment banking licence in 1997 and received a commercial banking licence in January 2002.

In recent years Kaupthing Bank has increased its activities abroad by means of acquiring financial companies and setting up subsidiaries. This includes the acquisition of the Swedish bank JP Nordiska in 2002 (now Kaupthing Bank Sverige), which has completely changed the position of Kaupthing Bank in the Nordic countries, the bank's home market.

Legal Status

The Issuer is a public limited liability company incorporated in Iceland and operating under Icelandic law. The Issuer is registered with the registrar of companies in Iceland. The registered office and principal place of business of the Issuer is Austurstræti 5, 155 Reykjavík, Iceland.

Strategy

- To maximise the bank's value and long-term shareholder value.
- To be a leading all-round bank in Iceland and one of the main investment banks in the Nordic countries.
- To maintain rapid growth without reducing demands on profitability.
- To develop a positive image as a progressive and independent all-round bank.
- To develop and maintain dependable long-term relationships with its customers.
- To employ motivated, well-educated and enterprising staff who are experts in their respective fields.
- To continue to develop the bank's workforce as its most valuable resource.
- To utilise the most up-to-date information technology in order to improve the bank's competitiveness.

The Issuer's basic driving force is its ambition to create value for shareholders and through the knowledge that achieving this successfully goes hand in hand with the professional service and success of its clients. The Issuer's reputation as a trusted advisor and partner depends critically on the delivery of quality services. Customer driven, the Issuer offers high quality products and services provided by creative, dedicated professionals. The management places emphasis on close, responsive relationships with clients to evolve the business in line with changing customer needs and market sentiment.

The Issuer has maintained a portfolio of interlinked value-added financial services, where private and investment banking, wealth management, corporate services and brokerage are included. This interlink age

allows the business to cross-sell and up-sell effectively and has led to long-standing relationships with the Issuer as a full service provider.

The Issuer seeks to build both independent and profitable business units in each geographic location, as well as to leverage each unit as a component within the group. The business has always sought to recruit the best people, and has built a strong ethical and professional culture. The Issuer values the international and multi-cultural base of its staff and leverages these differences as a strength to the business. Employees are encouraged to strive for continual improvement and constantly to learn from each other. To expand the business rapidly demands constant innovation and the Issuer's management style promotes exceptional internal networking and informality to achieve this.

The Issuer vigorously pursues business opportunities, actively promoting and selling its products and client services. The group is continually looking to build its base of customers for whom it can add value and where the relationship can be profitable for the group across all service areas. During recent years, the Issuer has actively been executing its strategy of international expansion. The strategy has consisted of both organic growth and strategic acquisitions.

Current Operations

The main divisions of the Issuer are:

- Corporate Finance
- Capital Markets
- International Division
- Treasury
- Corporate Banking
- Retail Banking and Branches
- Asset Management and Private Banking
- Pension and Insurance
- Finance and Accounting
- Information and Technology
- Risk Management
- Internal Auditing

Corporate Finance

The Issuer's Corporate Finance Division operates in most of the Issuer's offices. The Issuer has been a leading player in corporate finance on the Icelandic financial market in recent years, both in the number and size of offerings the Issuer has managed and the mergers and acquisitions on which it has acted as an adviser. Recently an even greater focus has been placed on cross-border projects, particularly in the Nordic countries, the United Kingdom and the United States, and this has led to positive results.

Capital Markets

The Issuer's Capital Markets Division trades shares and bonds on the international securities markets. With the aim of providing its clients with first-class service in securities trading, the Issuer is a member of seven stock exchanges in Europe and the United States. Capital Markets' expert employees offer clients the best service in securities trading on international securities markets. Clients are primarily institutional investors, such as pension funds, mutual funds, investment funds, financial institutions and high net-worth individuals.

The Issuer engages in proprietary trading in Reykjavík, Stockholm, Helsinki and New York. All trading inherently involves risk, and increased risk can lead to greater profits. It is therefore seen as essential that risk limits in proprietary trading are clearly defined and that risk management and supervision are effective.

Treasury

The Issuer's Treasury and Banking division has three main operations: inter-bank trading, derivatives and funding. Treasury and Banking is centrally administrated from the Issuer's head office in Reykjavik, where the majority of activities take place. However, Treasury also has operations in Luxembourg, Denmark and Sweden. This arrangement results in more efficient financing and enhances the possibility of increasing the interest rate differential with respect to risk.

Asset Management and Private Banking

The Issuer's Asset Management and Private Banking is organised into four units: Mutual Fund Management, Alternative Fund Management, Asset Management for Institutional Investors and Private Banking. The Issuer operates its Asset Management services in Reykjavik, Luxembourg, Helsinki, the Faroe Islands, Copenhagen, Geneva, Stockholm and New York. In Geneva there is no distribution of investment funds.

The Issuer's Private Banking Service is divided into two separate parts, Customer Relations and Asset Management. Asset Management is conducted in close cooperation with account managers, who focus on improving service and financial advice to each customer. The main role of the account manager is to meet the individual client's needs and suggest portfolio changes as the situation dictates. Investments for private individuals involve many variables. Investment decision making for private individuals extend beyond the country where the client is based, and in many cases it can be beneficial to take advantage of the financial and legal environments of other countries.

Retail Banking and Branches

The Issuer's personal banking services offer a diverse range of products and service lines, which are easily tailored to the needs of different groups. The Issuer was a pioneer in introducing many of these services, such as the Home Line payments service where the Bank handles payment of all fixed household expenses by automatic debit, to spread monthly payments equally over the year. Customers are thereby free from bills in the mail, bank queues and fluctuations in their expenses from one month to the next.

The Issuer is the first bank in Iceland to offer dedicated financial services for senior citizens. Many senior citizens own valuable real estate, free of mortgage, but little in the way of liquid assets. The Issuer therefore focused on designing simple loans for them, on favourable terms with collateral in their real estate (Real Estate Pensions), on which they do not need to pay instalments or interest until the real estate changes ownership. Loans can be paid out on a monthly basis or in a lump sum. Another focus was to provide simple and very favourable investment options through the Asset Pension Savings Book.

Payments intermediation has been evolving very rapidly in Iceland in recent years, headed by increased debit card transactions and an enormous increase in automation of services. The Issuer now has a total of 55 ATMs and Pay banks with an average of 107,000 transactions per month and average monthly turnover of ISK 550 million. The Issuer's share of total domestic debit card turnover in Iceland is now 22.0 per cent. The Issuer issues a wide selection of payments cards (both credit and debit cards) in co-operation with the Icelandic issuers of VISA and MasterCard. The Issuer owns a 21 per cent. share in Greidslumidlun (Visa) and 20 per cent. in Kreditkort (Europay).

Corporate Banking

The Issuer has targeted corporate clients in the last few years with particular emphasis on listed companies. This strategy has proven successful and the Issuer has increased its share in corporate banking significantly especially among larger companies.

The Issuer's growth last year has further increased its possibilities to provide services to the largest companies in Iceland. Some of these companies also have operations abroad and therefore the Issuer emphasises on being able to support them in their international expansion and to create the appropriate financial environment.

The overall operations of the department are built on qualified staff and a strong customer base from all lines of business. Special emphasis has been put on providing the companies with tailor-made, professional services that at the same time are speedy and efficient. The Issuer considers it very important to create the best solutions to fit each corporate client, and close co-operation exists between the Corporate Banking Division and the Issuer's branches to attain this goal. Surveys done among the leaders in the business community show that a great majority of the Issuer's clients are very satisfied with the services the Issuer offers them.

An ever-increasing number of clients choose to handle a large part of their banking business via electronic banking and see that as a considerable advantage. The Issuer has always been at the forefront with technical innovations in this field, and two years ago introduced a new and user-friendly corporate bank on the Internet that offers numerous possibilities of self-service. The Issuer attaches great importance to further developing its service to corporate clients to ensure that it is always at the forefront and fully covers their requirements at all times.

Information and Technology

The Information and Technology Division supplies the Issuer and its subsidiaries with trading systems, operates them and changes data into information for employees and clients. The speedy access of employees to information irrespective of their location, combined with the centralised operation of all systems, is the objective of the Division.

Internal Auditing

The Internal Auditing of the Issuer is an independent unit within the Issuer, which comes directly under its board and works in close co-operation with external auditors. The role of Internal Auditing is supervision of the operation and management of the Issuer. It operates as an independent party within the Issuer, which inspects and evaluates the quality and competence of systems and procedures.

The Insurance Industry

Co-operation between banking and insurance is a recent development in the Icelandic market. The Issuer's strategy has been to participate in the life insurance industry. The Issuer owns also 26.77 per cent. share in VIS – one of the largest insurance companies in Iceland. The Issuer's subsidiary, Althjoda liftryggingarfélagid is an insurance company that offers life- and accidents insurance.

Short Description of the Bank's Main Subsidiaries

Kaupthing Bank Sverige

The Issuer's largest subsidiary is Kaupthing Bank Sverige (previously JP Nordiska AB). JP Nordiska was created by the merger of a bank and securities companies. In 2001 Nordiska acquired the financial company Matteus, forming JP Nordiska. One year later the securities company Aragon, which was owned at the time by Kaupthing Bank, was merged with JP Nordiska and Kaupthing Bank acquired 28 per cent. of the merged bank. In August 2002 Kaupthing Bank made an offer for JP Nordiska. Following a successful acquisition of JP Nordiska, Kaupthing Bank was listed on Stockholmbörsen.

Kaupthing Bank Sverige offers a wide range of financial services, with a particular emphasis on equities trading, corporate finance and asset management. These activities are directed at institutions and individuals and is separated into three divisions: private banking, investment banking and asset management. There is also a fourth division, proprietary trading. Kaupthing Bank Sverige has one of the largest equities turnovers on Stockholmsbörsen, with a market share of 6 per cent. in 2002.

Kaupthing Bank Sverige employed 207 people as of 31st March, 2003. Kaupthing Bank Sverige operates in three Swedish cities, Stockholm, Gothenburg and Malmö.

Kaupthing Bank Luxembourg S.A.

In early 1998 the Issuer began operating an investment bank in Luxembourg, Kaupthing Bank Luxembourg S.A., which became the first overseas bank fully owned by an Icelandic party. The range of services has increased at a rapid rate from the beginning. In 1999 it was decided to further expand the activities and for this purpose a request for a commercial banking licence was filed. Kaupthing Bank Luxembourg S.A. began operating on 1 January, 2000.

The main operations of Kaupthing Bank Luxembourg S.A. are private banking and specialised corporate services. The private banking services of Kaupthing Bank Luxembourg S.A. includes asset management, securities brokerage, issuing of credit cards and the establishment of holding companies besides providing general deposit accounts and loans. Kaupthing Bank Luxembourg S.A.'s Corporate Division specialises in the establishment and operation of holding companies, debt-syndication and in the financing of the Issuer. The financial climate in Luxembourg and the international connections of Kaupthing Bank Luxembourg S.A. enables the bank to sell multi-bank loans for Icelandic companies and banks.

On 31st March, 2003, Kaupthing Bank Luxembourg S.A. had 54 employees.

Kaupthing New York Inc.

In 2000, the Issuer began operating in the US under the name Kaupthing New York Inc. Its operations are divided into three categories: Securities Brokerage, Asset Management and Corporate Finance. Brokerage of shares and bonds takes place through the subsidiary Kaupthing Securities Inc. (a member of NASD – the National Association of Securities Dealers), which obtained a brokerage licence in April 2001. The company has direct access to the New York Stock Exchange and the NASDAQ market. Kaupthing New York Inc.'s Corporate Finance has been engaged in various assignments, for US as well as Nordic companies. On 31 March, 2003, there were ten employees at Kaupthing New York Inc.

Kaupthing Sofi Oyj., Finland

Kaupthing Sofi Oyj. is a Finnish securities company located in Helsinki. Kaupthing Sofi Oyj. specializes in Asset Management and Securities Brokerage for companies, institutional investors and high net-worth individuals. The Issuer acquired Sofi in late 2001 and thereby established a position in Finland, as a part of the Issuer's growth as a Nordic bank. Kaupthing Sofi oyj. is one of the owners of the Helsinki Stock Exchange. Kaupthing Sofi Oyj.'s market share in the Finnish stock market has increased at a steady pace in recent years, and is currently at just over 6 per cent. On 31st March, 2003, there were 29 people employed by the company.

Kaupthing Bank A/S, Denmark

Preparations for the establishment of Kaupthing Bank A/S in Denmark began in the second half of 2000 and the license was granted by the end of June 2001. The main operations of Kaupthing Bank A/S in Denmark are International Private Banking, Brokerage, Asset Management and Corporate Services. A mutual fund investing in Icelandic bonds has been established and is listed in Danish currency and marketed to Danish investors. Kaupthing Bank A/S is a member of the Copenhagen Stock Exchange. At the end of 2001, Kaupthing Bank A/S also set up the management company, TEMA Kapital Management A/S, to operate mutual funds and in 2002 it founded Geysir Investment Company A/S which buys and sells mortgages. The Issuer owns 80 per cent. of the shares in Kaupthing Bank A/S and Føroya Sparikassi owns the remaining 20 per cent. On 31st March, 2003, there were 23 employees at Kaupthing Bank Denmark.

Arion Custody Services hf, Iceland

Arion Custody Services hf. ("Arion") is a wholly owned subsidiary of Kaupthing Bunadarbanki. The company has taken over all custody of assets, which were previously under the custody of the Issuer. The assets currently under custody of Arion amount to approximately ISK 350 billion. Arion has obtained an operating license for securities transactions from the Ministry of Commerce.

The company operates under the supervision of the Financial Supervisory Authority, Iceland. Arion was founded in April 2002 with the aim of being one centralised unit for the Issuer as a whole, to execute settlement, clearing, custody and corporate actions. All of the 27 employees are former employees of the back office, custody and asset management divisions of the Issuer, which has acted as Custodian or Administrator for various funds since 1985. Arion also offers accounting for various funds and has 21 funds utilising its services in this regard.

The aim of Arion is to use economies of scale to obtain better prices and lower the trading and safe keeping costs for the Group. Arion intends to expand its services outside the Issuer and offer its custody services to large institutional clients. Arion's premises are located in Reykjavik.

Lysing hf., Iceland

Lysing hf. is a leasing company which was wholly acquired by the Issuer in November 2001. Before the acquisition the Issuer owned 40 per cent. of the share capital in the company. Lysing hf. was founded in 1986 and the company's objective is to serve Icelandic business and industry reliably and professionally by financial lease of industrial machinery and business premises, by the extension of loans for purchase of machinery, and by offering performance guarantees to contractors. Lysing employed 33 people as of 31 March, 2003.

The Issuer in changing financial environment

To help ensure necessary returns with shrinking margins, the cost structure of the Issuer is continuously being reviewed. Certain measures have already been taken, such as consolidation of back office functions, and investments in information technology should also benefit such areas as clearing and accounting. The financial markets in Iceland are developing at a rapid rate. The Issuer has responded to these changes with heavy investments in information technology and strong entry into the capital markets. The Issuer has in that way been able to successfully adapt to the changing environment as can be seen by rapidly expanding balance sheet and increased share in the domestic market.

SOURCES OF FUNDS

The Issuer's principal sources of funding are customer deposits and foreign borrowing. Other sources of funding include capital markets and financial institutions. Core funding at the end of year 2002 was 48.6 per cent. while borrowing was 23.6 per cent.

A breakdown of the group's sources of funds as of 31st December, 2001 to 2002:

ISK mio	<i>Kaupthing Bunadarbanks pro forma</i>	<i>Kaupthing – Group</i>		<i>Bunadarbanks – Group</i>	
	<i>31/12/2002</i>	<i>31/12/2002</i>	<i>31/12/2001</i>	<i>31/12/2002</i>	<i>31/12/2001</i>
Equity.....	33,379	18,322	9,195	15,192	12,959
Minority interest in subsidiaries' equity...	1,114	1,114	223	0	0
Subordinate loans	11,010	4,457	2,947	6,553	5,417
Deposits	164,570	71,797	10,592	92,773	72,881
Core Funding	210,073	95,690	22,957	114,518	91,257
Borrowings	102,029	9,269	24,474	92,760	85,276
Credit institutions	109,865	75,457	67,295	35,809	20,871
Other liabilities	10,034	7,383	2,937	2,651	2,179
Provision for tax liabilities	411	204	317	207	0
Finance in the Market	222,339	92,313	95,023	131,427	108,326
Total Funds	432,412	188,003	117,980	245,945	199,583

In response to the changed character of Kaupthing Bank and Bunadarbanks Islands hf. in recent years, the composition of the groups funding has changed significantly. The banks have moved from being primarily serving individuals, small businesses and the agriculture to serving larger corporations in the domestic market and the Nordic market. Consequently, intermediation of foreign funds has grown rapidly which is the main explanation for the increased share of borrowing in the banks' balance sheet.

Equity

As of 31st December, 2002, the equity of the Issuer was 33,379 ISK million.

The 20 largest shareholders of the Issuer as of 27th May, 2003 are as follows:

<i>Shareholder</i>	<i>Shares</i>	<i>%</i>
Meiður ehf.....	62,107,464	15.05
Egla ehf.....	39,202,254	9.50
Fjármálaráðuneyti.....	36,713,224	8.89
Lífeyrissjóðir Bankastræti 7.....	21,460,727	5.20
Arion verðbréfavarsla - Safnr/saensk bréf.....	20,763,307	5.03
Eignarhaldsfélagið Sveipur ehf.....	18,441,615	4.47
Lífeyrissjóður verslunarmanna.....	17,698,199	4.29
Vátryggingafélag Íslands hf.....	12,191,638	2.95
Kaupthing Luxembourg S.A.	8,801,706	2.13
Samvinnulífeyrissjóðurinn	7,498,002	1.82
Lífeyrissjóðurinn Framsýn	6,735,861	1.63
Lífeyrissjóður sjómanna.....	6,233,060	1.51
Bankakteibolaget JP Nordiska.....	6,091,725	1.48
Fjárfestingafélagið Freyr ehf.....	5,811,592	1.41
Ferradis Holding S.A.....	5,363,014	1.30
Føroya Sparikassi	4,867,411	1.18

<i>Shareholder</i>	<i>Shares</i>	<i>%</i>
Kaupping hf, fjárfest.verðbréf.....	4,772,684	1.16
Eftirlaunasj starfsm Búnaðarb.....	4,653,817	1.13
Eignarhaldsf Samvinnutrygg svf.....	4,344,646	1.05
Holt Holding S.A.....	3,877,296	0.94

Subordinated Loans

The Issuer has issued subordinated loans in the domestic and international market both of the type Tier 1 and Tier 2. The CAD ratio at year-end 2002 was 12.4 per cent., full utilisation of Tier 1 and Tier 2 would allow the CAD ratio of 16.1 per cent. The Tier 1 ratio being 9.5 per cent., full utilisation of Tier 1 allows a ratio of 10.8 per cent.

The breakdown of subordinated loans is as follows:

<i>ISK mio</i>	<i>Tier</i>	<i>Currency</i>	<i>Interest at start</i>	<i>Interest changes</i>	<i>Interest after change</i>	<i>Payment date</i>	<i>31/12/2002</i>
Issued 1998	2	ISK	6.00%	2003	7.50%	2008	938
Issued 1999	2	ISK	5.50%	2004	7.00%	2009	1,532
Issued 2000	2	ISK	6.00%	2005	7.50%	2010	1,259
Issued 2000	2	ISK	6.00%	2005	7.50%	2010	231
Issued 2001	2	ISK	6.00%	2006	7.50%	2011	67
						no payment	
Issued 2001	1	ISK	8.65%	2011		date	1,131
Issued 2002	2	ISK	6.00%	2007	7.50%	2012	837
Issued 2002	2	EUR	-	-	-	2012	425
Issued 1997	2	ISK	6.30%	-	-	2004	185
Issued 1998	2	ISK	5.90%	2003	7.40%	2008	186
Issued 2001	2	ISK	8.00%	2006	10.00%	2011	1,326
Issued 2000	2	ISK	7.00%	2007	9.00%	2012	1,958
Issued 2002	2	ISK	7.50%	2009	10.00%	2014	802
Subordinated loans parent							10,877
Subordinated loans of subsidiaries							133
Subordinated loans consolidated							11,010

Capital Adequacy

According to the provisions of Art. 54 and 55 of the Act on Commercial Banks, subordinated loans and equity capital, after subtraction of the book value of shares held in other financial institutions, may not at any time fall below 8.0 per cent. of the Issuer's risk-adjusted asset base, as defined by law. The risk-adjusted asset base is comprised of total assets as well as guarantees issued and calculated risk factors after the deduction of various figures in the Balance Sheet, according to the rules of the Financial Supervisory Authority. At the end of the year, the Issuer complies with other statutory ratios in accordance with the provisions of Art. 46, 51 and 53 of the Act on Commercial Banks. Together with subordinated loans, total capital and reserves amounted to ISK 41,036 as at 31st December, 2002 of which ISK 31,868 million consisted of Tier 1 capital. It is the Issuer's policy to seek to maintain a 10 per cent. capital ratio for the Group with a minimum of 8 per cent. Tier one ratio.

Capital and capital adequacy ratio according to law:

		<i>Kaupthing Bunadarbanki</i>	
		<i>Pro forma</i>	
ISK mio		31/12/2002	31/12/2001
Tier I: Capital recorded in the Financial Statements		31,868	22,865
Tier II: Subordinated loans.....		9,765	7,032
Deductions according to Art. 55 of Act No. 161/2002		-597	-1,133
		<u>41,036</u>	<u>28,755</u>
Risk-adjusted asset base		329,204	262,950
Capital adequacy ratio.....		12.5%	10.9%

		<i>Bunadarbanki</i>			
		<i>Group</i>		<i>Parent</i>	
ISK mio.....		31/12/2002	31/12/2001	31/12/2002	31/12/2001
Tier I: Capital recorded in the Financial					
Statements		16,260	14,026	16,250	14,026
Tier II: Subordinated loans.....		5,422	4,159	5,288	4,159
Deductions according to Art. 55 of					
Act No. 161/2002.....		-515	-458	-515	-458
		<u>21,167</u>	<u>17,727</u>	<u>21,023</u>	<u>17,727</u>
Risk-adjusted asset base.....		193,694	168,110	169,307	150,922
Capital adequacy ratio.....		10.9%	10.5%	12.4%	11.8%

		<i>Kaupthing</i>			
		<i>Group</i>		<i>Parent</i>	
ISK mio		31/12/2002	31/12/2001	31/12/2002	31/12/2001
Tier I: Capital recorded in the					
Financial Statements		15,608	8,830	17,212	9,195
Tier II: Subordinated loans.....		4,343	2,873	4,343	2,873
Deductions according to Art. 55 of					
Act No. 161/2002.....		-82	-675	-82	-639
		<u>19,869</u>	<u>11,028</u>	<u>21,473</u>	<u>11,429</u>
Risk-adjusted asset base.....		135,510	94,840	89,147	82,276
Capital adequacy ratio.....		14.7%	11.6%	24.2%	13.9%

Deposits

The Issuer had approximately 260,000 deposit accounts that include current accounts, savings accounts and currency accounts. As of 31st December, 2002 the Issuer's total deposits amounted to 25 per cent. of the total deposits in all of Iceland's commercial banks and savings banks.

The deposits from customers are well diversified, with a majority of the customers with relatively low deposits. Deposit accounts bear interest according to floating rate.

Breakdown of the Issuer's deposits as at 31st December, 2001 to 2002:

ISK mio	<i>Kaupthing Bunadarbanki</i>	<i>Kaupthing – Group</i>		<i>Bunadarbanki – Group</i>	
	<i>pro forma</i>	<i>31/12/2002</i>	<i>31/12/2001</i>	<i>31/12/2002</i>	<i>31/12/2001</i>
Deposits on demand	80,270	14,566	4,039	65,704	49,602
Time deposits	83,781	57,231	6,553	26,550	23,203
Special deposits	519	0	0	519	76
Total	164,570	71,797	10,592	92,773	72,881
Savings deposits by maturity					
Up to 3 months	59,556	50,262	4,513	9,294	7,247
Over 3 months and up to 1 year	11,520	2,802	1,529	8,718	7,359
Over 1 year and up to 5 years	11,476	2,419	473	9,057	8,673
Over 5 years	1,748	1,748	38		
Total	84,300	57,231	6,553	27,069	23,279

Other Funding

In recent years, the domestic money market has developed greatly. The interbank market (Reibor Market), established in 1997 has evolved rapidly. This market has become the most important instrument in the short-term treasury operations of the Issuer. Bills and other short-term instruments have also become more important and in 2001 a new forward (SWAP) inter-bank market was established, thereby giving the banks additional means for their treasury operations.

Outstanding bonds and notes issued by the group in ISK amounted to ISK 31,026 million at year-end 2002.

The following table sets out a breakdown of the Issuer's borrowings from bonds and notes issued, as well as borrowings from other credit institutions, as at 31st December, 2001 to 2002. Borrowings in foreign currency, International syndicated loans and private placements are generally with maturity from 2-4 years.

ISK mio	<i>Kaupthing Bunadarbanki</i>	<i>Kaupthing – Group</i>		<i>Bunadarbanki – Group</i>	
	<i>pro forma</i>	<i>31/12/2002</i>	<i>31/12/2001</i>	<i>31/12/2002</i>	<i>31/12/2001</i>
Bonds issued	31,026	9,269	8,946	21,757	10,295
Borrowings from credit institutions	70,764	0	15,528	70,764	74,548
Other borrowings	239			239	433
Total	102,029	9,269	24,474	92,760	85,276

Uses of Funds

Portfolio of Marketable Securities and Loans

The predominant lending activity of the Issuer consists of loans to private individuals and an extensive range of corporate customers.

ISK mio	<i>Kaupthing Bunadarbanki</i>	<i>Kaupthing – Group</i>		<i>Bunadarbanki – Group</i>	
	<i>pro forma</i> 31/12/2002	31/12/2002	31/12/2001	31/12/2002	31/12/2001
Cash and amounts from credit institutions.....	38,519	20,494	8,204	19,427	9,492
Loans to customers	250,278	82,453	48,884	167,825	139,431
Mortgages foreclosed	2,030	0	36	-	-
Appropriated assets.....	-	-	-	2,030	997
Lease agreements/settlements.....	17,025	-	-	17,025	15,203
Bonds and other fixed-income securities	69,298	49,095	29,431	20,203	14,833
Shares and other variable-income securities	32,882	21,088	22,892	11,928	12,451
Shares in associated and affiliated companies	3,528	2,311	1,113	1,217	884
Other assets.....	18,852	12,562	7,420	6,290	6,292
Total assets.....	432,412	188,003	117,980	245,945	199,583

Securities held by the Issuer consist of trading securities and investment securities. Investment securities are marketable securities, which the Issuer's management has made a formal decision to hold for more than one year. Trading securities include all other securities.

Marketable securities and corporate shares were ISK 105.7 billion in year-end 2002. Of total marketable securities and corporate shares, bonds were ISK 69.2 billion, shares ISK 32.9 billion and shares in associated and affiliated companies were ISK 3.5 billion. A part of the Issuer's portfolio is not fully its property because the Issuer has entered into forward contracts with its customers against securities. The Issuer however owns the largest part of the securities.

The Issuer provides services to all sectors of the economy. The Issuer has diversified its portfolio of marketable securities and loans to minimise the risk in lending. The portfolio of loans and marketable securities is well distributed between economic sectors. Loans to individuals accounted for 29.04 per cent. of the Issuer's total lending and marketable securities. Services were the largest sector within commercial loans, at 32.68 per cent. Followed by retail sector with 11.73 per cent., the fishery sector with 8.49 per cent., the manufacturing industry with 8.9 per cent., the agriculture sector with 3.46 per cent., and credit facilities for government institutions at 1.61 per cent. Loans and marketable securities were widely spread between industrial sectors, as has been the case for some time.

Total of loans and marketable securities by customer categories:

ISK mio	<i>Kaupthing Bunadarbanki</i>	<i>Kaupthing – Group</i>		<i>Bunadarbanki – Group</i>	
	<i>pro forma</i> 31/12/2002	31/12/2002	31/12/2001	31/12/2002	31/12/2001
Governmental Institutions	1.61%	0.30%	0.60%	2.20%	2.80%
Agriculture	3.46%	0.00%	0.00%	5.00%	5.80%
Fishing industry	8.49%	0.40%	2.90%	12.10%	14.20%
Commerce	11.73%	6.20%	0.00%	14.20%	13.50%
Manufacturing	8.90%	4.20%	4.70%	11.00%	8.10%
Building contractors	4.08%	0.00%	0.00%	5.90%	6.10%
Services	32.68%	43.40%	68.10%	27.90%	25.10%
Individuals	29.04%	45.50%	23.70%	21.70%	24.40%
	100.00%	100.00%	100.00%	100.00%	100.00%

Loans to customers and leasing agreements amounting to ISK 154,634.6 million specified by maturity:

ISK mio	<i>Kaupthing Bunadarbanki</i>	<i>Kaupthing – Group</i>		<i>Bunadarbanki – Group</i>	
	<i>pro forma</i> 31/12/2002	31/12/2002	31/12/2001	31/12/2002	31/12/2001
On demand	22,139	8,875	4,068	13,264	7,016
Up to 3 months	81,960	45,570	29,103	36,390	33,683
Over 3 months and up to 1 year	48,502	11,834	6,710	36,668	33,290
Over 1 year and up to 5 years	89,576	15,943	5,548	73,633	63,843
Over 5 years	25,126	231	3,455	24,895	16,802
Total	267,303	82,453	48,884	184,850	154,634

Risk Management

The Issuer faces various types of risks related to its business as a financial institution, which arise from its day to day operations. The most significant of these risks are listed below. Management devotes a significant portion of its time to the management of these risks. Effective risk management involves the identification of the significant risks, the quantification of the Issuer's exposure to these risks and taking actions to limit these risks and the constant monitoring of the risks.

Some of the Issuer's techniques in managing these risks include the establishment of limits, the respect of these limits, as well as the quantification of the exposures to the different risks. It is management's responsibility to identify where the established limits have been exceeded and to take the appropriate action. The Issuer has documented these responsibilities and limits.

Approval and Revision of Risk Policy

The Issuer's Risk Policy is adopted and approved by the Board of Directors of the Issuer. It should be revised at least annually. Amendments or minor changes can be made more frequently but each change needs the approval of the Issuer's CEOs before it is effective and then needs to be approved by the Board of the Issuer at first convenience.

Credit Risk and Collateral Management

Credit risk is managed by two entities on a group wide level: Group Credit Committee and Group Credit Manager (or Head of Credit Risk). The role of the Credit Committee is described in the description

of the Credit Procedure but the role of the Credit Manager is to manage the process and make sure all the requirements set out by the credit committee such as requirements on documentation and collateral are satisfied. The Credit Manager monitors collateral quality on a daily basis and reacts to any lack thereof. The collateral quality is valued based on haircuts, which are different for each asset class depending on estimated liquidation quality. The collateral system integrates the loan, fx and derivative information with the custody data and values directly the pledged securities in the clients' portfolios and calculates the collateral level daily.

The credit and collateral risk is managed on a local level in the bank's subsidiaries according to the same rules and in addition in accordance with any further requirements postulated by local regulation. The local credit committees and credit managers receive their credit limits from the global credit committee and all larger credits require approval from the global credit committee.

Monitoring

At least twice a year the risk management submits to the Board an overview of at least 10 largest credits of the Issuer. The statement shall include long- and short-term obligations, stock holdings, collateral and major financial information.

At least twice a year a list shall be made of the largest credits in doubt and be presented to the board.

Market Risk Management

Market Risk Limits

The position limits or any changes to them are proposed by the Issuer's Head of Trading and accepted by the Issuer's Head of Risk Management (Head of Risk) and reviewed by the Issuer's CEOs which can interfere in limit decisions.

Each position limit size is based on, among other things, underlying liquidity, the Issuer's risk appetite as well as legal limitations on individual positions posed by Icelandic, Danish, Swedish, Finnish, Swiss, US, Luxembourg or other relevant authorities. Head of Risk maintains a document detailing current limits and a journal of changes to them. Final approval of the position limits is required by the the Issuer's CEOs.

All trades outside of position limits are prohibited and the penalty will be decided by Head of Risk and paid by the relevant Trading Department from the department's P&L to cover Kaupthing Bunadarbanki Bank Group Risk Management costs. The penalty amount will in general be based on the profit or loss generated by the unauthorised trades and will be twice that amount or 1 per cent. per day of the limit overrun, whichever is larger. Disputes on breaches of position limits or amounts can be referred to the Issuer's CEOs. All violations of this risk policy need to be documented in journal maintained by Head of Risk and made available to the the Issuer's CEOs.

Limits allocated to each type of risk are stipulated in separate documents maintained by Head of Risk.

Risk Monitoring

The Issuer monitors the different risks incurred carefully. The different types of risks (excluding credit risk) are specified in the following sections. The overall responsibility of complying with the set up limits lies with the Board of Directors of the Issuer. Management is however responsible for the day-to-day routines aiming at controlling the different risk parameters. The positions are continuously monitored against the limits where possible and otherwise daily.

Risk Models

Risk models employed will be position based (risk limits), volatility based i.e. based on the volatility of market variables and their related covariance and scenario base i.e. based on some prescribed scenario which is likely to cause severe drawdown in profits.

Risk measures are generated by proprietary systems that utilise the counter party, market data and trade databases generated and used by the Issuer's trade systems. Additionally the risk management systems are augmented by various third party solutions.

Risk Reporting

Intra-Day Reports

All trades and intra-day profit or loss is reported continuously to Head of Risk through a position monitoring system. Head of Risk appoints a person and a backup person whose responsibility it is to monitor the intra-day positions and alert Head of Risk on any deviations or exceptions observed.

Daily Reports

Kaupthing Bundarbanski Bank Risk Management sends a daily report on profit and loss and turnover to Head of Risk, Head of Trading and The Issuer's CEOs.

Monthly Reports

Kaupthing Bundarbanski Bank Risk Management sends a monthly risk assessment report to Head of Trading, the Issuer's CEOs, the Issuer's Board of Directors detailing volatility based and scenario based measures such as Value-at-Risk, Earnings-at-Risk and Stress tests based on current position limits.

Quarterly Reports

Head of Trading sends a quarterly report to Head of Risk and the Issuer's CEOs on activities, profit and loss and general observations on the market and their view on future prospects for the trading operations.

Types of Risks

Security market risk

Trading departments are only permitted to trade certain listed stocks on certain exchanges within the prescribed limits and in some cases on an intra-day basis only.

It is understood that prudence be exercised with respect to position size and the prevailing market liquidity of any individual stock.

Currency risk

Currency risk is the risk associated with fluctuations in assets and liabilities denominated in different currencies due to movements in exchange rates. The currency risk is controlled by the Issuer's Treasury and is subject to limits similarly to other market risk and is estimated using the risk models described above.

Interest rate risk

The interest rate risk arises due to the maturity or interest rate reset periods of assets and liabilities not coinciding. Fluctuations in market interest rates cause fluctuations in interest income. Short to medium term interest risk is controlled by the Issuer's Treasury using limits on mismatch in expected in- and outgoing payments as well as limits on interest rate sensitivity of overall interest bearing assets and liabilities. The Issuer's Trading is responsible for positions in long term bonds and is controlled using position limits and estimated using various risk models as described above.

Liquidity risk

The Issuer is subject to the risk of being unable to repay its depositors on demand, or as and when due, through holding insufficient cash or near-cash assets. This risk is measured by constant monitoring of liquidity ratios. The Issuer Treasury is responsible for maintaining sufficient liquidity by maintaining a

sufficiently high ratio of liquid assets and available funding to near term liabilities and possible payment outflows. The liquidity measures are calculated at the end of each trading day and monitored by Head of Risk and reported to CEOs.

Operational risks

The Operational risk is defined as a risk of cash difference and of sundry loss or errors, which can be defined as compensation paid to or received from counter parties for losses/profits incurred due to errors on the part of either traders or settlement staff.

These operational risks are monitored through the system of internal control set up at different levels in the the Issuer and its subsidiaries (daily controls – supervisory controls – management controls).

PROVISIONS AND NON-PERFORMING LOANS

Concerning evaluation of non-performing loans, the Issuer is working according to the rules of the Financial Supervisory Authority, which are based on EU Directive no. 554/1994 regarding rules on the annual accounts of commercial banks.

Non-performing loans amounted to ISK 4,469 million in year-end 2002 and are specified as follows:

ISK mio	<i>Kaupthing Bunadarbanki</i>				
	<i>pro forma</i>	<i>Kaupthing – Group</i>		<i>Bunadarbanki – Group</i>	
	<i>31/12/2002</i>	<i>31/12/2002</i>	<i>31/12/2001</i>	<i>31/12/2002</i>	<i>31/12/2001</i>
Loans with specific provision for losses	5,340	1,161	618	4,179	2,875
Specific provision for losses.....	-3,633	-575	-246	-3,058	-2,046
Total	1,707	586	372	1,121	829
Other non performing loans	2,762	117	162	2,645	1,826
Total non-performing loans	4,469	703	534	3,766	2,655

Coverage for non-performing assets is as follows:

ISK mio	<i>Kaupthing Bunadarbanki</i>				
	<i>pro forma</i>	<i>Kaupthing – Group</i>		<i>Bunadarbanki – Group</i>	
	<i>31/12/2002</i>	<i>31/12/2002</i>	<i>31/12/2001</i>	<i>31/12/2002</i>	<i>31/12/2001</i>
Total non-performing loans	4,469	703	534	3,766	2,655
Specific provisions for losses	3,633	575	246	3,058	2,046
Appropriated assets.....	2,030	0	0	2,030	997
Total non-performing assets	10,132	1,278	780	8,854	5,698
Specific provision for losses	3,633	575	246	3,058	2,046
General provisions	2,131	582	604	1,549	1,375
Appropriated assets.....	2,030	0	0	2,030	997
Total provision.....	7,794	1,157	850	6,637	4,418
Total provision/Total non-performing assets	76.9%	90.5%	109.0%	75.0%	77.5%

Provisions for losses on the loan portfolio have been made each year by the Issuer to meet the estimated risk attached to these assets. These provisions do not represent a final write-off. Certain risk factors are evaluated in addition to a regular contribution for this purpose. On the one hand, there are specific

provisions and on the other hand, there are general provisions to meet the general risk of lending operations. Interest from loans, which are defined non-performing, have not been entered as income as well as other non-performing loans.

The changes in provisions are as follows:

ISK mio	<i>Kaupthing Bunadarbanks</i>	<i>Kaupthing – Group</i>		<i>Bunadarbanks – Group</i>	
	<i>pro forma</i> 31/12/2002	31/12/2002	31/12/2001	31/12/2002	31/12/2001
Provision at January 1st 2001					
Provision for losses over the year					
Losses during the year	-1,255	-172	-	-1,083	-349
Payment of loans previously written off	17	-	-	17	8
Provision	<u>4,899</u>	<u>292</u>	<u>425</u>	<u>4607</u>	<u>3420</u>
Provision for losses on loan portfolio as a percentage of loans and guarantees issued	2.05%	1.40%	1.00%	2.33%	1.98%

Board of Directors

The Board of Directors for the Issuer will consist of nine members and nine alternates. The Issuer has two Chief Executive Officers, whom the Board of Directors appoints and assigns areas of responsibility.

Board of Directors of the Issuer

Sigurdur Einarsson – resident in Iceland, elected on to Board of Kaupthing Bank in 2003. Executive Chairman of Kaupthing Bank.

Hjörleifur Jakobsson – resident in Iceland, elected on to Board of Bunadarbanks in 2003. CEO of Olúfélagið hf.

Tommy Persson – resident in Sweden, elected on to Board of Kaupthing Bank in 2002. CEO of Länsförsäkringar AB.

Gunnar Páll Pálsson – resident in Iceland, elected on to Board of Kaupthing Bank in 2001. CEO of Verslunarmannafélag Reykjavíkur, Store and Office Worker's Union of Reykjavík.

Jón Helgi Guðmundsson – resident in Iceland, elected on to Board of Bunadarbanks in 2002. CEO of BYKO.

Finnur Ingólfsson – resident in Iceland, elected on to Board of Bunadarbanks in 2003. CEO of VÍS, Iceland Insurance Company Ltd.

Ásgeir Thoroddsen – resident in Iceland, elected on to Board of Kaupthing Bank in 2003. Attorney at Law.

Peter Gatti – resident in Germany, newly elected. Managing Director of Hauck & Aufhäuser.

Bjarnfredur Ólafsson – resident in Iceland, newly elected. Attorney at Law.

Chief Executive Officers

Solon R. Sigurdsson

Born 1942, Manager of several divisions and Branch Manager, Landsbanki.

He has been with Bunadarbanks since 1983 and a Member of the Management Board from 1990.

Hreidar M. Sigurdsson

Born 1970, Cand Oecon from University of Iceland.

He has been with Kaupthing since 1994, and Deputy CEO the last three years.

Senior Management of the Issuer

Armann Thorvaldsson – Managing Director of Corporate Finance

Born 1968, a History graduate with an MBA from Boston University. He has been with Kaupthing Bank since 1994.

Gudbjörn Maronsson – Managing Director of Asset Management and Private Banking

Born 1963, a Business Studies graduate with an MBA from Golden Gate University. He has been with Kaupthing Bank since 2001.

Haflídi Kristjánsson – Managing Director of Pension and Insurance

Born 1962, a Psychology graduate with an MBS from the University of South Carolina. He has been with Kaupthing Bank since 1997.

Ingolfur Helgason – Managing Director of Capital Markets

Born 1967, a Business Studies graduate from the University of Iceland. He has been with Kaupthing Bank since 1993.

Gudmundur Gislason – Managing Director of International Div.

Born 1941, Manager and Senior Manager at Utvegsbanki since 1960. Has been with Bunadabanki since 1990.

Kristin Petursdóttir – Managing Director of Treasury

Born 1965, a Business Studies graduate with an MS in International Business from the Norwegian School of Management in Bergen. Has been with Kaupthing Bank since 1997.

Gudny Arna Sveinsdóttir – Managing Director of Finance and Accounting

Born 1966, a Business Studies graduate with an MS from the University of Uppsala in Sweden. She has been with Kaupthing Bank since 2001.

Karl Thorsteins – Managing Director of Corporate Banking

Born 1964, a Business Studies graduate from the University of Iceland. Has been with Bunadabanki since 1990.

Dr. Steingrímur P. Karason – Managing Director of Risk Management

Born 1968, an Engineering graduate with an ScD in Mechanical Engineering from MIT in Boston. He has been with Kaupthing Bank since 1997.

Fridrik Halldorsson – Managing Director of Retail Banking

Born 1959, BA in Business Administration, Senior Manager Treasury Bunadabanki 1992-1999. Deputy Managing Director of Retail Banking since 2002.

Ingi Örn Geirsson – Managing Director of Information Technology

Born 1951, a Business Administration and Computer Science graduate from the University of Lund. He has been with Bunadabanki since 1985.

AUDITORS' REPORT

Endorsement of the Auditors

We have audited the pro-forma balance sheet of Bunadarbanki Islands hf. and Kaupthing Bank hf. and it is based on the audited annual accounts of the banks for 2002 and the decision of both Boards of Directors on the merger of the banks.

It is our opinion that, with reference to Article 122 of Act no. 2/1995 on Public Limited Companies, the balance sheet gives a clear picture of the assets and liabilities of both banks, the changes which the merger will entail and the balance sheet of the bank following the merger.

Reykjavik, 12 April, 2003

Deloitte & Touche hf.
Knútur Þórhallsson

Sigurdur Jónsson
KPMG Endurskodun hf.

To the Board of Directors and the shareholders of Bunadarbanki Islands hf.

We have audited the Annual Accounts of Bunadarbanki Islands hf. for the year ending 31 December, 2002. The Annual Accounts comprise the Consolidated Financial Statements and the Annual Accounts of the Parent Company and consist of Profit and Loss Account, Balance Sheet, Cash Flow Statement and Notes. The Annual Accounts are presented by the Bank's management and are their responsibility in accordance with laws and regulations. Our responsibility is to express an opinion on the Annual Accounts based on our audit. We conducted our audit in accordance with generally accepted auditing standards in Iceland Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Annual Accounts are free of material misstatements.

An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the Annual Accounts. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the accounts. We believe that our audit provides a reasonable basis for our opinion. In our opinion the Annual Accounts present fairly, in all material respects, the financial position of Búnaðarbanki hf. as of 31 December, 2002, and the results of its operations and its cash flow for the year then ended, in accordance with law, the bank's by-laws and generally accepted accounting principles.

Reykjavík, 7 February, 2003.

Deloitte & Touche hf.
Knútur Þórhallsson
State Authorised Public Accountant.

The National Audit Office
Sigurður Þórðarson
Auditor General

To the Board of Directors and Shareholders of Kaupthing Bank hf.

We have audited the accompanying Balance Sheet and Consolidated Balance Sheet of Kaupthing Bank hf. as of 31 December, 2002 and the related Profit and Loss Account, Statement of Cash Flows for the year then ended and a fiveyear summary. These Annual Accounts are the responsibility of the Company's management. Our responsibility is to express an opinion on these Annual Accounts based on our audit. We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Annual Accounts are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts

and disclosures in the Annual Accounts. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall Annual Accounts presentation. We believe that our audit provides a reasonable basis for our opinion. In our opinion the Annual Accounts give a true and fair view of the financial position of Kaupthing Bank hf. as of 31 December, 2002, and the results of its operations and its cash flows for the year then ended, in accordance with the law and generally accepted accounting principles in Iceland.

Stockholm, 19 February, 2003

Sigurdur Jónsson
Hildur Árnadóttir
KPMG Endurskodun hf.

Profit and Loss Account – the Issuer

*Kaupthing
Bunadarbanki
Pro forma
31/12/2002*

ISK mio

Interest income

Interest from credit institutions.....	2,062
Interest on loans to customers.....	18,781
Interest on bonds and fixed-income securities	2,598
Other interest income.....	2,713
	<hr/> 26,154

Interest expenses

Interest on loans from credit institutions	6,108
Interest on deposits	6,811
Interest on borrowings	5,242
Interest on subordinated loans	807
Other interest expenses	188
Calculated inflation adjustment	0
	<hr/> 19,156

Net interest income 6,998

Other operating income

Dividends from shares and other capital holdings	507
Fees and commissions received.....	7,061
Fees and commissions paid.....	-893
Net profit/(loss) on securities and foreign	5,900
Miscellaneous operating income.....	1,783
	<hr/> 14,358

Net operating income 21,356

Other operating expenses

Salaries and related expenses	6,505
Other administrative expenses	5,186
Depreciation of fixed assets	757
Miscellaneous operating expenses.....	38
	<hr/> 12,486

Provision for possible loan losses..... -2,794

Net profit before taxes 6,076

Income tax -769

Net worth tax

Net profit for the year 5,307

Profit and Loss Account – Kaupthing

ISK mio	<i>Kaupthing Group</i>	
	<i>31/12/2002</i>	<i>31/12/2001</i>
Interest income		
Interest from credit institutions	1,095	984
Interest on loans to customers	2,845	1,707
Interest on bonds and fixed-income securities	1,352	1,807
Other interest income	2,698	2,217
	<u>7,990</u>	<u>6,715</u>
Interest expenses		
Interest on loans from credit institutions	4,220	3,375
Interest on deposits	1,565	9
Interest on borrowings	1,137	2,699
Interest on subordinated loans	331	400
Other interest expenses	162	102
Calculated inflation adjustment	0	317
	<u>7,415</u>	<u>6,902</u>
Net interest income	575	-187
Other operating income		
Dividends from shares and other capital holdings	382	858
Fees and commissions received	3,581	4,283
Fees and commissions paid	-468	-331
Net profit/(loss) on securities and foreign exchange trading	4,172	725
Miscellaneous operating income	1,668	702
	<u>9,335</u>	<u>6,237</u>
Net operating income	9,910	6,050
Other operating expenses		
Salaries and related expenses	3,098	2,396
Other administrative expenses	2,594	2,478
Depreciation of fixed assets	259	168
Miscellaneous operating expenses		
	<u>5,951</u>	<u>5,042</u>
Provision for possible loan losses	-582	-415
Net profit before taxes	3,377	593
Income tax	-302	260
Net worth tax		
Net profit for the year	<u>3,075</u>	<u>853</u>

Profit and Loss Account – Bunadarbanki

ISK mio	<i>Bunadarbanki Group</i>	
	<i>31/12/2002</i>	<i>31/12/2001</i>
Interest income		
Interest from credit institutions	998	1,402
Interest on loans to customers	15,936	17,218
Interest on bonds and fixed-income securities	1,246	1,828
Other interest income	15	14
	<u>18,195</u>	<u>20,462</u>
Interest expenses		
Interest on loans from credit institutions	1,919	1,925
Interest on deposits	5,246	6,794
Interest on borrowings	4,105	4,586
Interest on subordinated loans	476	689
Other interest expenses	26	79
Calculated inflation adjustment	0	391
	<u>11,772</u>	<u>14,464</u>
Net interest income	<u>6,423</u>	<u>5,998</u>
Other operating income		
Dividends from shares and other capital holdings	125	18
Fees and commissions received	3,508	2,709
Fees and commissions paid	-397	-350
Net profit/(loss) on securities and foreign exchange trading	1,728	-667
Miscellaneous operating income	115	92
Net operating income	<u>11,502</u>	<u>7,800</u>
Other operating expenses		
Salaries and related expenses	3,407	2,885
Other administrative expenses	2,592	2,189
Depreciation of fixed assets	498	413
Miscellaneous operating expenses	38	36
	<u>6,535</u>	<u>5,523</u>
Provision for possible loan losses	-2,212	-1,276
Net profit before taxes	<u>2,755</u>	<u>1,001</u>
Income tax	-462	66
Net worth tax	-5	-5
Net profit for the year	<u><u>2,288</u></u>	<u><u>1,062</u></u>

Balance Sheet – the Issuer

*Kaupthing
Bunadarbanki
Pro forma
31/12/2002*

ISK mio

Assets

Cash and amounts due from credit institutions

Cash and balances on call with the Central Bank	763
Treasury bills.....	802

Amounts due from credit institutions

Reserve requirements on deposits at the Central Bank	5,832
Balances with other credit institutions.....	31,122
	<hr/> 38,519

Loans

Loans to customers	250,278
Appropriated assets	-
Mortgages foreclosed	2,030
Lease agreements/settlements	17,025
	<hr/> 269,333

Market securities and corporate shares

Bonds and other fixed-income securities	69,298
Shares and other variable-income securities	32,882
Shares in associated and affiliated companies.....	3,528
	<hr/> 105,708

Other assets

Goodwill	3,002
Fixed assets	5,377
Various assets	6,223
Deferred income tax assets	
Prepaid expenses and accrued uncollected income	4,250
	<hr/> 18,852

Total assets	<hr/>432,412<hr/>
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ISK mio

Balances due to credit institutions	109,865
Deposits	
Demand deposits	80,270
Time deposits	83,781
Special terms deposits	519
	<u>164,570</u>
Borrowings	102,029
Other liabilities	
Sundry liabilities	5,925
Accrued expenses and pre-collected income	4,109
	<u>10,034</u>
Provision for deferred tax liability	411
Subordinated loans	11,010
Total liabilities	<u>397,919</u>
Minority interest in subsidiaries equity	1,114
Equity	
Share capital	4,092
Share premium account	17,508
Statutory reserve	
Revaluation account	
Accrued stock options	120
Retained earnings	11,659
	<u>33,379</u>
Total liabilities and equity	<u>432,412</u>

Balance Sheet – Kaupthing Bank hf.

ISK mio	<i>Kaupthing Group</i>	
	<u>31/12/2002</u>	<u>31/12/2001</u>
Assets		
Cash and amounts due from credit institutions		
Cash and balances on call with the Central Bank	1	0
Treasury bills	0	0
Amounts due from credit institutions		
Reserve requirements on deposits at the Central Bank	2,321	464
Balances with other credit institutions	18,172	7,740
	<u>20,494</u>	<u>8,204</u>
Loans		
Loans to customers	82,453	48,884
Appropriated assets	-	-
Mortgages foreclosed	-	36
Lease agreements/settlements		
	<u>82,453</u>	<u>48,920</u>
Market securities and corporate shares		
Bonds and other fixed-income securities	49,095	29,431
Shares and other variable-income securities	21,088	22,892
Shares in associated and affiliated companies	2,311	1,113
	<u>72,494</u>	<u>53,436</u>
Other assets		
Goodwill	3,002	365
Fixed assets	1,377	897
Various assets	5,194	2,619
Deferred income tax assets		
Prepaid expenses and accrued uncollected income	2,989	3,539
	<u>12,562</u>	<u>7,420</u>
Total assets	<u><u>188,003</u></u>	<u><u>117,980</u></u>

ISK mio	<i>Kaupthing Group</i>	
	<i>31/12/2002</i>	<i>31/12/2001</i>
Balances due to credit institutions	75,457	67,295
Deposits		
Demand deposits	14,566	4,039
Time deposits	57,231	6,553
Special terms deposits	0	0
	71,797	10,592
Borrowings	9,269	24,474
Other liabilities		
Sundry liabilities	4,869	1,851
Accrued expenses and pre-collected income	2,514	1,086
	7,383	2,937
Provision for deferred tax liability	204	317
Subordinated loans	4,457	2,947
Total liabilities	168,567	108,562
Minority interest in subsidiaries equity	1,114	223
Equity		
Share capital	2,124	1,626
Share premium account	9,996	4,302
Statutory reserve		
Revaluation account		
Accrued stock options	120	98
Retained earnings	6,082	3,169
	18,322	9,195
Total liabilities and equity	188,003	117,980

Balance Sheet – Bunadarbanki Islands hf.

ISK mio	<i>Bunadarbanki Group</i>	
	<i>31/12/2002</i>	<i>31/12/2001</i>
Assets		
Cash and amounts due from credit institutions		
Cash and balances on call with the Central Bank	762	715
Treasury bills	802	0
Amounts due from credit institutions		
Reserve requirements on deposits at the Central Bank	3,511	494
Balances with other credit institutions	14,352	8,283
	19,427	9,491
Loans		
Loans to customers	167,825	139,431
Appropriated assets	17,025	997
Mortgages foreclosed	-	-
Lease agreements/settlements	2,030	15,203
	186,880	155,632
Market securities and corporate shares		
Bonds and other fixed-income securities	20,203	14,834
Shares and other variable-income securities	11,928	12,451
Shares in associated and affiliated companies	1,217	884
	33,348	28,168
Other assets		
Goodwill		
Fixed assets.....	4,000	4,033
Various assets	1,029	955
Deferred income tax assets.....	0	256
Prepaid expenses and accrued uncollected income.....	1,261	1,047
	6,290	6,291
Total assets	<u>245,945</u>	<u>199,583</u>

ISK mio	<i>Bunadarbanki Group</i>	
	2002	2001
Balances due to credit institutions	35,809	20,871
Deposits		
Demand deposits	65,704	49,602
Time deposits	26,550	23,203
Special terms deposits	519	76
	92,773	72,881
Borrowings	92,760	85,276
Other liabilities		
Sundry liabilities	1,056	1,775
Accrued expenses and pre-collected income	1,595	403
	2,651	2,179
Provision for deferred tax liability	207	0
Subordinated loans	6,553	5,417
Total liabilities	230,753	186,624
Minority interest in subsidiaries equity		
Equity		
Share capital	5,351	5,233
Share premium account	3,915	3,546
Statutory reserve	349	349
Revaluation account	0	1,597
Accrued stock options		
Retained earnings	5,577	2,234
	15,192	12,959
Total liabilities and equity	245,945	199,583

THE REPUBLIC OF ICELAND

Iceland is one of the Nordic countries, located in the North Atlantic between Norway, Scotland and Greenland. Iceland is the second largest island in Europe and the third largest in the Atlantic Ocean with a land area of some 103,000 square kilometres and an exclusive 200 nautical mile economic zone of 758,000 square kilometres in the surrounding waters. Because of the Gulf Stream, Iceland enjoys a warmer climate than its northerly location would indicate.

The population of Iceland is about 288,200 in year-end 2002. Iceland was first settled late in the 9th century. The majority of the settlers were undoubtedly of Norse origin, but it is generally assumed that a certain element of the early settlers were of Celtic origin. In 930, a general legislative and judicial assembly, the Althingi, was established, and a uniform code of laws for the country was adopted. In 1262, Iceland entered a treaty, which established a union with the Norwegian monarchy. When Norway came under the rule of Denmark in 1380, Iceland became a Danish dominion. Iceland was granted limited home rule in 1874, which was extended in 1904. With the act of Union in 1918, Iceland became an autonomous state in monarchical union with Denmark. In 1944 Iceland terminated its union with Denmark and became an independent republic.

Modern economic history spans about one century. In the early years of industrialization the economy was based on fisheries and agriculture. Rapid developments in these areas formed the basis for improved living standards and a fundamental change in the economic structure. In recent decades the economy has diversified into the export of manufactured goods, process industries and a range of services for export and domestic use. At the same time the marine sector has diversified significantly. Hence, the Icelandic economy has taken the shape of a modern industrial state.

With GDP (gross domestic product) of approximately U.S.\$10.7 billion in 2002, the size of the economy is relatively small. However, the per capita GDP is very high by international standards, being approximately U.S.\$30,400 in 2002. The economy relies on foreign trade and services in maintaining the high standard of living.

Iceland is endowed with rich fishing grounds in the exclusive 200 nautical mile economic zone. The marine sector, including fishing and fish processing, is of fundamental importance to the Icelandic economy. Iceland has developed a comprehensive fisheries management policy in order to manage the fish stocks, based on biological estimates of the status of the fish stocks and forecasts for their development in the near future. The fish processing industry employs modern technology and management techniques. The production systems are flexible and the processing methods are to a large extent interchangeable. The fishing fleet is technologically advanced and includes vessels designed to perform high-quality processing at sea. The diversification in the marine sector extends not only to the species and methods of processing, but also to marketing. Icelandic marine products have developed established brand names in the United States, Europe and Japan.

Iceland is also richly endowed with energy resources consisting of hydro and geothermal energy. Almost all of the electricity consumed in Iceland is produced from indigenous energy resources. Hot water from geothermal sources and natural steam are extensively used for residential heating. Only a small fraction of the country's vast hydro and geothermal resources has been exploited so far. Hence, the potential for large scale development of power-intensive industry is substantial.

Industrial expansion in Iceland is to a considerable extent based on the abundant energy resources and their attractiveness for power-intensive industries, aided by tariff-free access to the European market. Among the largest manufacturing enterprises in Iceland are two aluminium smelters, a ferrosilicon plant and a diatomic plant. Currently, further power-intensive projects are being proposed in East Iceland. These are very large projects relative to the size of the Icelandic Economy and will increase the positive output gap and inflationary pressures, especially in 2005 and 2006 when 2/3 of the investment will be made. With appropriate economic policy responses, it will prove possible to contain inflation well within the tolerance limits when it peaks.

Smaller scale manufacturing is also important and growing. This includes production of high technology and heavy equipment for fishing and fish processing, largely for exports. With the development of the economy, the share of services in GDP has grown rapidly. The tourism sector has been one of the fastest growing industries in recent years, due to a rapid increase in the number of foreign visitors to Iceland.

Iceland is a member of the United Nations and its affiliates, the International Monetary Fund (IMF) and the World Bank. Iceland is also a member of the Organisation for Economic Co-operation and Development (OECD) and a number of other multinational organisations, including the Nordic Council and the Council of Europe. Iceland joined the European Free Trade Association (EFTA) in 1970 and is a member of the European Economic Area (EEA), an 18 nation free-trade zone of the European Union (EU) and EFTA countries. Iceland is a contracting party to the General Agreement on Tariffs and Trade (GATT) and ratified the agreement establishing the World Trade Organization (WTO) in December 1994, thus becoming a founding member of the WTO.

	2004	2003	2002	2001	2000	1999	1998
	(forecast)	(forecast)	(estimate)				
Volume changes on previous year, percent.							
Gross domestic product.....	3.25	2.50	-0.50	2.90	4.90	3.90	4.50
Exports of goods and services.....	3.75	1.25	3.00	7.90	6.30	4.80	2.20
Imports of goods and services.....	7.00	4.00	-2.50	-9.00	9.30	5.70	23.30
Percentage changes on previous year							
Consumer price index (Y/Y change).....	2.10	2.20	4.80	6.70	5.00	3.40	1.70
Real disposal income per capita	3.50	2.00	2.10	2.30	1.30	3.00	8.70
Effective price of foreign currency*.....	0.00	-7.00	-3.00	20.10	0.10	-0.20	-1.80
Real exchange rate*	1.00	8.00	5.60	-12.60	2.90	1.80	1.60
Unemployment rate.....	2.50	3.00	2.50	1.40	1.30	1.90	2.80
Percentage of GDP							
Current account balance....	-2.25	-1.00	0.25	-3.90	-10.00	-6.90	-6.90
Net external debt position-	-68.00	-69.00	-75.00	-75.40	-62.30	-50.50	-49.00

Recent developments

Iceland's economy has been characterized by robust growth since the middle of the last decade. In 2001 economic growth begun to slow down and a better balance has now been achieved. A successful landing has been made and international credit rating agencies have either affirmed or raised Iceland's sovereign rating. In February, Fitch affirmed its rating of AA- for foreign currency sovereign debt and AAA for domestic debt. The outlook was changed from stable to negative. In October, Moody's Investor Service raised its foreign currency sovereign debt rating to Aaa, the highest that it awards. In November, Standard & Poor's affirmed ratings for Iceland of AA+/A-1+ for domestic debt and A+/A-1+ for foreign debt, and altered its outlook from negative to stable.

GDP growth in 2002 is estimated at zero or a slight contraction, but annual growth for the six preceding years averaged almost 5 per cent. Over the past two years both private consumption and investment have shrunk between the years, but GDP has been sustained by favourable foreign trade developments. This represents a major turnaround from earlier years when GDP growth was driven by increases in private consumption and investment, while the contribution made by foreign trade was negative as a result of current account deficits. Developments over the past two years reflect a swift adjustment

towards better internal and external balance in the Icelandic economy. Sharp swings in the exchange rate have been experienced whereby the króna strengthened by 13.5 per cent. against major trading currencies after weakening by 14.8 per cent. the previous year.

Only a small current account deficit, or none at all, is expected to be shown for the year, compared with 7 per cent. and 10 per cent. deficits for the two preceding years respectively. Likewise, inflation slowed down and moved within the upper tolerance limit of the monetary policy target around the middle of the year. The consumer price index (CPI), on which indexation is calculated, rose by 2.0 per cent. in 2002 and the Central Bank's inflation target was thereby attained. Imported goods have a 35 per cent. weighting in the CPI, so that exchange rate trends are a crucial factor in price developments.

External conditions developed satisfactorily. Prices of marine products, measured in SDR, rose by 3.3 per cent. between the years, but aluminium prices, measured in foreign currencies, were 6.3 per cent. lower on average than the year before. World crude oil prices were favourable at the beginning of the year but rose towards the end, in part because of the mounting threat of war in Iraq. On average, crude oil prices were 1.6 per cent. higher than the year before. Foreign interest rates continued to go down which, coupled with the strengthening of the króna, greatly eased the foreign debt service burden. On the whole, the terms of trade have been improving. In pace with declining economic activity, the wage trend slowed down somewhat. Day wages in the general labour market rose by 5.4 per cent. between the years, while a clause on increased employers' pension fund contributions matched by extra wage earners' contributions was incorporated into wage agreements. Unemployment as a percentage of the labour force measured 2.5 per cent., which was some rise between the years. As the year wore on, unemployment increased somewhat. Public sector performance improved during the year. The fiscal surplus is estimated at ISK 17 billion, or the equivalent of 2.2 per cent. of GDP. Of this figure, almost ISK 10 billion derived from the sale of assets – the treasury sold its largest shareholding in Landsbanki Íslands. The municipalities' deficit can be expected to have increased during the year, from ISK 9 billion in 2001 on a cash basis.

FINANCIAL MARKETS IN ICELAND

The Icelandic financial system has been substantially reformed over the last decade. Iceland participates in the European Single Market for financial services. As a member of the European Economic Area (EEA) since 1994, Iceland is obliged to transpose into national law all existing and future EU legislation in the field of financial services. Iceland has thus implemented all the EC directives on banking, insurance and securities trading. Since the beginning of 1995, in accordance with the EEA agreement, capital movements have been fully liberalised, with the exception of certain restrictions that apply to foreign direct investments in fisheries and fish processing, energy production and distribution, and aviation companies.

The commercial and savings banks' funding is chiefly based on retail deposits and domestic bond issues although they are also frequent borrowers in international markets. There are currently four commercial banks in Iceland, i.e. Kaupthing Bunadabanki hf., Íslandsbanki hf., Landsbanki Íslands hf., and Sparisjóðabanki Íslands hf. (Icebank). The first three provide all conventional banking and securities services. There are 25 savings banks in Iceland and Icebank serves as a banking institution for them. Twelve other credit institutions currently operate in Iceland, five of which are state owned investment banks, four are investment funds and three are leasing companies.

Several investment funds were merged and subsequently privatised in 1998. The merged investment bank, FBA, was granted a licence to operate as a commercial bank and subsequently merged with Íslandsbanki in April 2000.

In 2002 and 2003 the state finalised the sale of its majority stake in Landsbanki and Bunadabanki. Following the privatisation of Bunadabanki the new owners decided to merge the bank with Kaupthing Bank to form Kaupthing Bunadabanki hf. The merged bank is Iceland's largest bank and the largest company on the Iceland Stock Exchange by market capitalisation.

A new State Housing Fund was established at the beginning of 1999. The new fund is the result of legislation approved by Parliament in June 1998, which aims to rationalise the existing state housing fund system. The bulk of housing loans to individuals in Iceland are made by the State Housing Fund rather than by the commercial banks.

There are currently five securities firms and four securities brokerages operating in Iceland. The Act on Undertakings for Collective Investments in Transferable Securities (UCITS) provides for rules on, among other things, authorisation, registration, articles of association of UCITS, management and depository companies, investment policy, management, annual accounts and supervision. There are currently nine UCITS authorised in Iceland and five management companies of UCITS.

There are 14 insurance companies authorised to operate in Iceland. Sjóvá-Almennar Tryggingar hf., Vátryggingafélag Íslands hf. and Tryggingarmiðstöðin hf. are by far the largest with a combined market share around 85 per cent. Almost 60 per cent. of the insurance companies' portfolio consists of marketable securities, which make them fairly sizeable investors in the Icelandic securities market. The insurance companies are also increasingly becoming active in the financial markets through their lending operations.

The Icelandic old age pension system is composed of a tax financed public pension scheme, mandatory funded occupational pension schemes and voluntary pension saving with tax incentives. Membership of a fully funded occupational pension fund is mandatory for all employees and self-employed. The funds were established through a collective labour agreement in the late 1960s and early 1970s. The funds have been increasing relatively to the public system and they will overtake it in the years to come as they approach maturity and means testing reduces the public pensions.

The Bank Inspectorate of the Central Bank and the Insurance Supervisory Authority were merged into a separate entity, the Financial Supervisory Authority (FSA), on 1st January, 1999. The main task of the FSA is to ensure that the activities of the above institutions and firms are conducted in accordance with the relevant laws and regulations and that they remain sound in other respects. These institutions and firms are obligated to provide all the information considered necessary by the FSA to facilitate statutory supervision of their activities.

Since the beginning of 1995, in accordance with the EEA agreement, capital movements have been fully liberalised, with the exception of certain restrictions that apply to foreign direct investments in fisheries and fish processing, energy production and distribution, and aviation companies. The target of monetary policy is price stability. Required reserves are made with the Central Bank by credit institutions. The required reserves ratio is 1.5 per cent. for the part of the required reserves base, which is tied for one year or longer, and 4 per cent. for the part tied for a shorter term.

The Icelandic Stock Exchange currently has 17 members. The stocks of around 60 companies, government securities and various bond issues, primarily made by credit institutions, are listed on the exchange. The Iceland Stock Exchange signed a formal agreement to join the NOREX Alliance in June 2000. The SAXESS trading system, which has been in operation since March 2000 in Sweden and since June 2000 in Denmark, became operational on the Icelandic market on 30th October 2000.

Source: Statistics Iceland, The Central Bank of Iceland)

ICELANDIC TAXATION

1. Icelandic Taxation

The comments below are of a general nature based on the Issuer's understanding of current law and practice in Iceland. They relate only to the position of persons who are the absolute beneficial owners of the Notes, Receipts and/or Coupons. They may not apply to certain classes of person such as dealers. Prospective holders of the Notes who are in any doubt as to their personal tax position or who may be subject to tax in any other jurisdiction, should consult their professional advisers.

1. There are no taxes or other governmental charges payable under the laws of Iceland or any authority of, or in, Iceland in respect of the principal or interest on the Notes by a holder who is not a resident of Iceland, or in respect of any amount payable under the Programme Agreement or the Agency Agreement.
2. There are no estate or inheritance taxes, succession duties, gift taxes or capital gains taxes imposed by Iceland or any authority of, or in, Iceland in respect of the Notes if, at the time of the death of the holder or the transfer of the Notes, such holder or transferor is not a resident of Iceland.
3. The Issuer is not required by the current laws of Iceland to make any deductions or withholding from any payment of principal or interest due or to become due under the Notes or from any amount payable under the Programme Agreement or the Agency Agreement, if the recipient is not a resident of Iceland.

2. Proposed EU Tax Directive

The member states of the European Union are considering proposals to adopt a directive regarding the taxation of savings income. Under the proposals, member states would be required to provide to the tax authorities of another member state details of payments of interest made by a person within its jurisdiction to an individual resident in that other member state, subject to the right of certain member states to opt instead for a withholding system for a transitional period in relation to such payments. These proposals are at an advanced stage but the terms of the directive finally approved may differ from such proposals. Investors should rely on their own analysis of the proposals and should take advice from appropriate legal or taxation professionals.

SUBSCRIPTION AND SALE

The Dealers have, in a programme agreement (the “*Programme Agreement*”) dated 24th June, 2003, agreed with the Issuer a basis upon which they or any of them may from time to time agree to purchase Notes. Any such agreement will extend to those matters stated under “*Form of the Notes*” and “*Terms and Conditions of the Notes*”. In the Programme Agreement, the Issuer has agreed to reimburse the Dealers for certain of their expenses in connection with the establishment of the Programme and the issue of Notes under the Programme and to indemnify the Dealers against certain liabilities incurred by them in connection therewith.

United States

The Notes have not been and will not be registered under the Securities Act and may not be offered or sold within the United States or to, or for the account or benefit of, U.S. persons except in certain transactions exempt from the registration requirements of the Securities Act.

The Notes are subject to U.S. tax law requirements and may not be offered, sold or delivered within the United States or its possessions or to a United States person, except in certain transactions permitted by U.S. tax regulations. Terms used in this paragraph have the meanings given to them by the U.S. Internal Revenue Code of 1986 and regulations thereunder.

Each Dealer has represented and agreed, and each further Dealer appointed under the Programme will be required to represent and agree, that it will not offer, sell or deliver Notes (i) as part of their distribution at any time or (ii) otherwise until 40 days after the completion of the distribution, as determined and certified by the relevant Dealer or, in the case of an issue of Notes on a syndicated basis, the relevant lead manager, of all Notes of the Tranche of which such Notes are a part, within the United States or to, or for the account or benefit of, U.S. persons. Each Dealer has further agreed, and each further Dealer appointed under the Programme will be required to agree, that it will send to each dealer to which it sells any Notes during the distribution compliance period a confirmation or other notice setting forth the restrictions on offers and sales of the Notes within the United States or to, or for the account or benefit of, U.S. persons. Terms used in this paragraph have the meanings given to them by Regulation S under the Securities Act.

Until 40 days after the commencement of the offering of any Series of Notes, an offer or sale of such Notes within the United States by any dealer (whether or not participating in the offering) may violate the registration requirements of the Securities Act if such offer or sale is made otherwise than in accordance with an available exemption from registration under the Securities Act.

Each issuance of Index Linked Notes or Dual Currency Notes shall be subject to such additional U.S. selling restrictions as the Issuer and the relevant Dealer may agree as a term of the issuance and purchase of such Notes, which additional selling restrictions shall be set out in the applicable Pricing Supplement.

United Kingdom

Each Dealer has represented and agreed, and each further Dealer appointed under the Programme will be required to represent and agree, that:

- (i) in relation to Notes which have a maturity of one year or more, it has not offered or sold and, prior to the expiry of the period of six months from the issue date of such Notes, will not offer or sell any such Notes to persons in the United Kingdom except to persons whose ordinary activities involve them in acquiring, holding, managing or disposing of investments (as principal or agent) for the purposes of their businesses or otherwise in circumstances which have not resulted and will not result in an offer to the public in the United Kingdom within the meaning of the Public Offers of Securities Regulations 1995 (as amended);
- (ii) in relation to any Notes having a maturity of less than one year, (a) it is a person whose ordinary activities involve it in acquiring, holding, managing or disposing of investments (as principal or agent) for the purposes of its business and (b) it has not offered or sold and will

not offer or sell any Notes other than to persons whose ordinary activities involve them in acquiring, holding, managing or disposing of investments (as principal or as agent) for the purposes of their businesses or who it is reasonable to expect will acquire, hold, manage or dispose of investments (as principal or agent) for the purposes of their businesses where the issue of the Notes would otherwise constitute a contravention of Section 19 of the FSMA by the Issuer;

- (iii) it has only communicated or caused to be communicated and will only communicate or cause to be communicated an invitation or inducement to engage in investment activity (within the meaning of Section 21 of the FSMA) received by it in connection with the issue of any Notes in circumstances in which Section 21(1) of the FSMA does not apply to the Issuer; and
- (iv) it has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to any Notes in, from or otherwise involving the United Kingdom.

Japan

The Notes have not been and will not be registered under the Securities and Exchange Law of Japan (the “***Securities and Exchange Law***”) and each Dealer has agreed and each further Dealer appointed under the Programme will be required to agree that it will not offer or sell any Notes, directly or indirectly, in Japan or to, or for the benefit of, any resident of Japan (which term as used herein means any person resident in Japan, including any corporation or other entity organised under the laws of Japan), or to others for re-offering or resale, directly or indirectly, in Japan or to a resident of Japan except pursuant to an exemption from the registration requirements of, and otherwise in compliance with, the Securities and Exchange Law and any other applicable laws, regulations and ministerial guidelines of Japan.

Iceland

Each Dealer has agreed and each further Dealer appointed under the Programme will be required to agree that it will not offer Notes to the public in Iceland, except in compliance with the Icelandic Securities Transaction Law and any applicable laws or regulations of Iceland.

General

Each Dealer has agreed and each further Dealer appointed under the Programme will be required to agree that it will (to the best of its knowledge and belief) comply with all applicable securities laws and regulations in force in any jurisdiction in which it purchases, offers, sells or delivers Notes or possesses or distributes this Offering Circular and will obtain any consent, approval or permission required by it for the purchase, offer, sale or delivery by it of Notes under the laws and regulations in force in any jurisdiction to which it is subject or in which it makes such purchases, offers, sales or deliveries and neither the Issuer nor any of the other Dealers shall have any responsibility therefor.

None of the Issuer and the Dealers represents that Notes may at any time lawfully be sold in compliance with any applicable registration or other requirements in any jurisdiction, or pursuant to any exemption available thereunder, or assumes any responsibility for facilitating such sale.

With regard to each Tranche, the relevant Dealer will be required to comply with such other restrictions as the Issuer and the relevant Dealer shall agree and as shall be set out in the applicable Pricing Supplement.

GENERAL INFORMATION

Authorisation

The establishment of the Programme and the issue of Notes have been duly authorised by a resolution of the Board of Directors of the Issuer dated 13th June, 2003.

Listing of Notes

Application has been made to list Notes issued under the Programme on the Luxembourg Stock Exchange. A legal notice relating to the Programme and the constitutional documents of the Issuer are being lodged with the Luxembourg trade and companies register (*Régistre de Commerce et des Sociétés, Luxembourg*) where such documents may be examined and copies obtained. The Luxembourg Stock Exchange has allocated the number 12730 to the Programme for listing purposes.

Documents Available

So long as Notes are capable of being issued under the Programme, copies of the following documents will, when published, be available from the registered office of the Issuer and from the specified offices of the Paying Agents for the time being in London and Luxembourg:

- (i) the articles of association (with an English translation thereof) of the Issuer;
- (ii) the audited financial statements of each of Kaupthing Bank hf. and Bunadarbanki Islands hf. in respect of the financial years ended 31st December, 2002, 2001 and 2000;
- (iii) the most recently published audited annual financial statements of the Issuer and the most recently published unaudited interim financial statements (if any) of the Issuer (with an English translation thereof);
- (iv) the Programme Agreement, the Agency Agreement, the Deed of Covenant and the forms of the Global Notes, the Notes in definitive form, the Receipts, the Coupons and the Talons;
- (v) a copy of this Offering Circular;
- (vi) any future offering circulars, prospectuses, information memoranda and supplements including Pricing Supplements (save that a Pricing Supplement relating to an unlisted Note will only be available for inspection by a holder of such Note and such holder must produce evidence satisfactory to the Issuer and the Paying Agent as to its holding of Notes and identity) to this Offering Circular and any other documents incorporated herein or therein by reference; and
- (vii) in the case of each issue of listed Notes subscribed pursuant to a subscription agreement, the subscription agreement (or equivalent document).

Clearing Systems

The Notes have been accepted for clearance through Euroclear and Clearstream, Luxembourg. The appropriate Common Code and ISIN for each Tranche of Notes allocated by Euroclear and Clearstream, Luxembourg will be specified in the applicable Pricing Supplement. If the Notes are to clear through an additional or alternative clearing system the appropriate information will be specified in the applicable Pricing Supplement.

Significant or Material Change

Save as disclosed in this Offering Circular, there has been no significant change in the financial or trading position of the Issuer and Bunadarbanki Islands hf. their respective subsidiaries, taken as a whole, since 31st December, 2002 and there has been no material adverse change in the financial position or prospects of the Issuer and their respective subsidiaries, taken as a whole, since 31st December, 2002.

Litigation

Neither the Issuer nor any of its subsidiaries is or has been involved in any legal or arbitration proceedings (including any proceedings which are pending or threatened of which the Issuer is aware) which may have or have had in the 12 months preceding the date of this document a significant effect on the financial position of the Issuer or the Group.

Auditors

The auditors of the Bunadarbanki Islands hf. are Deloitte & Touche hf., who have audited Bunadarbanki Islands hf.'s accounts, without qualification, in accordance with generally accepted auditing standards in Iceland for each of the three financial years ended on 31st December, 2002, 2001 and 2000.

The auditors of Kaupthing hf. are KMPG Endurskodun hf., who have audited Kaupthing hf.'s accounts, without qualification, in accordance with generally accepted auditing standards in Iceland for each of the three financial years ended on 31st December, 2002, 2001 and 2000.

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