Group

Condensed
Interim Financial Statements
January 1 to June 30 2008

Landsvirkjun
Háaleitisbraut 68
103 Reykjavík

Reg. no. 420269-1299

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Endorsement by the Board of Directors and the Director

Landsvirkjun's objective is to operate in the energy sector and to engage in other business and financial operations according to the decision of the Board of Directors at each time. In addition to the parent company, the Company's Consolidated Financial Statements include five subsidiaries, Fjarski ehf., Hraunaveita ehf., Icelandic Power Insurance Ltd., Landsnet hf. and Landsvirkjun Power ehf. Landsvirkjun's Interim Financial Statements are prepared in accordance with International Accounting Standard on Interim Financial Reports, IAS 34. The Interim Financial Statements are prepared in US Dollars, which is the functional currency of Landsvirkjun as from the beginning of the year 2008. Amounts are presented in thousands of USD, unless otherwise specified.

According to the Consolidated Income Statement the profit for the period amounted to USD 83,449 thousand. The total consolidated revenue amounts to USD 239,623 thousand during the period. According to the Consolidated Balance Sheet consolidated equity amounted to USD 1,758,031 thousand at the end of the period.

Statement of the Board of Directors and the Director

According to the best knowledge of the Board of Directors and the Managing Director, the Interim Financial Statements are in accordance with International Financial Reporting Standards as adopted by the EU, and it is the opinion of the Board of Directors and the Managing Director that the Interim Financial Statements give a fair view of the Company's assets, liabilities and financial position as at June 30, 2008, and the Company's profit and changes in cash in the period January 1 to June 30, 2008.

Furthermore, it is the opinion of the Board of Directors and the Managing Director, that the Interim Financial Statements and the Endorsement by the Board of Directors for the period January 1st to June 30th, 2008 give a fair view of the Company's profit, financial position and development, and describe the main risk factors faced by the Company.

The Board of Directors and the Managing Director hereby confirm these Consolidated Financial Statements with their signature.

Reykjavík, August 27, 2008.

The Board of Directors:

Ingimundur Sigurpálsson
Bryndís Hlöðversdóttir
Gylfi Árnason
Jóna Jónsdóttir
Páll Magnússon

Managing Director:

Friðrik Sophusson

Independent Auditor's Report

To the Board of Directors and owners of Landsvirkjun

Introduction

We have reviewed the accompanying condensed consolidated financial statements of Landsvirkjun, which comprise the consolidated balance sheet as at June 30, 2008 and the consolidated income statement, statement of changes in equity and cash flow statement for the six-month period then ended, and a summary of significant accounting policies and other explanatory notes. Management is responsible for the preparation and fair presentation of this interim financial information in accordance with International Financial Reporting Standards as adopted by the EU. Our responsibility is to express a conclusion on this interim financial information based on our review.

Scope of Review

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

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the accompanying interim financial information does not give a true and fair view of the financial position of the entity as at 30 June 2008, and of its financial performance and its cash flows for the six-month period then ended in accordance with IAS 34, *Interim Financial Reporting* .

Reykjavík, August 27, 2008.

KPMG hf.

Jón Eiríksson
Reynir Stefán Gylfason

Income Statement January 1 to June 30, 2008

	Notes	2008 1.1.-30.6.	2007 1.1.-30.6.
Operating revenues			
Power sales		207,132	140,898
Transmission		30,671	30,377
Other income		1,820	2,152
		239,623	173,427
Operating expenses			
Energy production costs		59,653	43,268
Transmission costs		20,862	18,038
Cost of general research		2,554	7,727
Other operating expenses	7	18,514	16,188
		101,583	85,221
Operating profit		138,040	88,206
Financial income and (financial expenses)			
Interest income		9,287	2,851
Interest expenses		(91,350)	(37,097)
Net income (expenses) on financial assets and liabilities		79,467	365,656
Effect of Associated Companies		(1,018)	0
	8	(3,614)	331,409
Profit before taxes		134,426	419,616
Income tax	9	(50,977)	(111,032)
Net Profit		83,449	308,584
Attributable to:			
Owners of the parent company		105,421	309,174
Subsidiaries minority interest		(21,972)	(591)
		83,449	308,584

The notes numbered 1 through 26 are an integral part of these Condensed Interim Financial Statements

Interim Financial Statements of Landsvirkjun, June 30, 2008 5 Amounts in thousands of USD

Balance Sheet June 30, 2008

Assets

	Notes	30.06. 2008	31.12. 2007
Non-current assets			
Property, plant and equipment	10	3,576,937	3,651,660
Projects under construction	20	339,781	234,650
Intangible assets	11	118,264	94,113
Associated companies		20,430	6,918
Shares in other companies		41	2,313
Derivative financial instruments	13	1,016,309	659,516
Long-term notes receivable		57	494
Deferred tax asset	9	35,140	106,797
Total fixed assets		5,106,959	4,756,460
Current assets			
Inventories		4,245	5,437
Accounts receivable and other receivables		91,265	73,337
Assets held for sale		11,721	0
Derivative financial instruments	13	153,670	127,491
Cash and cash equivalents		137,459	179,578
Total current assets		398,360	385,843
Total assets		5,505,319	5,142,303

Equity and liabilities

	Notes	30.06. 2008	31.12. 2007
Equity			
Owners' contributions		586,512	586,512
Revaluation account	3	56,221	0
Other equity		1,082,375	985,174
		1,725,108	1,571,686
Minority interest		32,923	28,459
Total equity		1,758,031	1,600,145
Long-term liabilities			
Long-term debt	16	3,016,116	2,735,753
Accrued pension liabilities		31,907	38,153
Obligation due to demolition	18	5,818	7,212
Income tax liability		3,095	0
Derivative financial instruments	13	290,408	105,191
		3,347,344	2,886,310
Current liabilities			
Accounts payable and other short-term liabilities		202,341	247,277
Current maturities of long-term debt	17	142,175	347,329
Derivative financial instruments	13	55,428	61,242
		399,944	655,848
Total liabilities		3,747,288	3,542,158
Total equity and liabilities		5,505,319	5,142,303

The notes numbered 1 through 26 are an integral part of these Condensed Interim Financial Statements

Interim Financial Statements of Landsvirkjun, June 30, 2008 6 Amounts in thousands of USD

Statement of Equity January 1, 2007 to June 30, 2008

January 1 to June 30, 2007	Notes	Owners' contribution	Revaluation Account	Other equity	Majority Owner's Equity	Minority interest	Total equity
Equity on January 1, 2007		586,512		530,169	1,116,681	26,591	1,143,272
Translation difference				(673)	(673)		(673)
Profit (loss) for the period				309,174	309,174	(591)	308,584
Total profit for the period				308,501	308,501	(591)	307,910
Dividends paid				(8,065)	(8,065)		(8,065)
Equity at June 30, 2007		586,512		830,606	1,417,117	26,001	1,443,118

January 1 to June 30, 2008		Owners' contribution	Revaluation Account	Other equity	Majority Owner's Equity	Minority interest	Total equity
Equity on January 1, 2008		586,512		985,174	1,571,686	28,459	1,600,145
Translation difference				(388)	(388)	(4,198)	(4,586)
Revaluation	3		66,142		66,142	36,040	102,182
Tax effect due to revaluation ...			(9,921)		(9,921)	(5,406)	(15,327)
Profit (loss) for the period				105,421	105,421	(21,972)	83,449
Total profit for the period		586,512	56,221	105,033	161,254	4,464	165,718
Dividends paid				(7,831)	(7,831)		(7,831)
Equity at June 30, 2008		586,512	56,221	1,082,376	1,725,108	32,923	1,758,031

The notes numbered 1 through 26 are an integral part of these Condensed Interim Financial Statements

Amounts in thousands of USD

Statement of Cash Flows January 1 to June 30, 2008

	2008	2007
Operating activities	1.1.-30.6.	1.1.-30.6.
Cash received from customers	220,018	182,296
Cash expenses	(59,418)	(47,027)
Cash from operation activities excluding interest	160,600	135,269
Interest income received	9,220	2,862
Interest expenses and foreign exchange differences paid	(61,616)	(39,416)
Hedging	(31,848)	(33,783)
Cash flow from operating activities	76,356	64,932
Investment activities		
Kárahnjúkar project - hydropower station	(121,273)	(231,417)
Transmission	(8,137)	(20,178)
Development costs	(23,208)	(8,809)
Purchased shares	(11,067)	(2,308)
Sold shares	8,023	0
Other capital expenditure	(10,993)	(8,482)
Assets sold	55	151
(Decrease) increase in paid investments	(47,023)	46,809
	(213,623)	(224,235)
Other receivables, change	0	33,182
Investment activities	(213,623)	(191,053)
Financing activities		
New loans	272,802	302,188
Amortization of long term debt	(167,900)	(52,027)
Cash dividends	(7,831)	(8,065)
Financing activities	97,071	242,097
(Decrease) increase in cash during the period	(40,196)	115,976
Effect of exchange diff. on cash and cash equivalents	(1,923)	(673)
Cash and cash equivalents at the beginning of the period	179,578	74,963
Cash and cash equivalents at the end of the period	137,459	190,266

The notes numbered 1 through 26 are an integral part of these Condensed Interim Financial Statements

Interim Financial Statements of Landsvirkjun, June 30, 2008 8 Amounts in thousands of USD

Notes

General information

1. **The Company**

Landsvirkjun is a partnership having its place of business in Iceland and its headquarters at Háaleitisbraut 68, Reykjavik. Landsvirkjun operates on the basis of the Act on Landsvirkjun no. 42/1983. The Interim Financial Statements are for the period from January 1 to June 30, 2008.

2. **Statement of compliance with International Accounting Standards**

The Condensed Interim Financial Statements of Landsvirkjun, are prepared in accordance with International Accounting Standard, IAS 34. The Condensed Interim Financial Statements do not contain all the information required in Annual Financial Statements, and should therefore be read along with the Company's Financial Statements for the year 2007.

The Company's Board of Directors approved the presentation of the Financial Statements on August 27, 2008.

3. **Significant accounting methods**

In preparation of the Interim Financial Statements the same accounting methods as in preparation of the Consolidated Financial Statements for the year 2007, were applied, with the exception of the following regarding revaluation of property, plant and equipment. The Financial Statements are available at the Company's office or at its website, www.landsvirkjun.is. The Financial Statements are also available at the Icelandic Stock Exchange; www.omxnordicexhcange.com. For comparison purposes, key figures in the 2007 Consolidated Financial Statements have been translated to correspond with the presentation of the Interim Financial Statements for the period.

The Interim Financial Statements are prepared in US Dollars, the functional currency of Landsvirkjun as from the beginning of the year 2008. Amounts are in thousands of USD, unless otherwise specified. The Interim Financial Statements have been prepared on historical cost basis, except for the following assets and liabilities, which have been measured at fair value: derivative financial instruments, transmission assets, current financial assets and liabilities and shares in other companies.

In accordance with provision in the International Accounting Standards, IAS 16, Landnet's connecting structures and power lines were recorded using revaluation method. Thus, lines and connecting structures are recorded on the Balance Sheet at the revalued cost, which is the fair value on the day of revaluation, less revalued depreciation from the time the asset was acquired. All increase in value due to the revaluation, is recorded on a revaluation account, among equity, taking into consideration income tax effect. Depreciation of the revalued assets are posted to the Income Statement. At the time of sale or disposal of the asset, the portion of the revaluation account pertaining to the respective asset is posted to retained earnings.

4. **Use of estimates and decisions**

Preparation of Interim Financial Statements in accordance with International Accounting Standards, requires management to make decisions, evaluate and make assumptions which affect the accounting methods used, the recorded amounts of assets and liabilities, revenues and costs. Actual results may differ from these estimates.

Segment reporting

5. Statement of segments

Segment information is presented by sectors. The main segment statement is presented according to the nature of the operation, and it is based on the Group's organization and internal disclosure.

Inter-segment pricing is determined on an arm's length basis.

Segment operating income includes the segments pertaining directly to specific segments and the items that can be logically divided between the segments. Assets and liabilities of the Group are in the same manner divided between segments based on the beforementioned premises.

Operating segments 1.1. - 30.6 2008	Electricity production	Electricity transmission	Adjustments	Total
Income from third parties	208,880	30,743		239,623
Income within the Group	17,897	36,626	(54,523)	0
Segment income	226,777	67,369	(54,523)	239,623
Segment operating expenses	(78,303)	(26,469)	54,523	(50,249)
EBITDA	148,474	40,900		189,374
Depreciation	(39,597)	(11,974)	237	(51,333)
Segment earnings, EBIT	108,877	28,926	237	138,040
Segment assets	5,378,606	730,834	(624,551)	5,484,889
Shares in associated companies	19,887	543	0	20,430
Total assets	5,398,493	731,377	(624,551)	5,505,319
Segment liabilities	3,614,739	638,032	(505,483)	3,747,288
Total liabilities	3,614,739	638,032	(505,483)	3,747,288
Operating segments 1.1. - 30.6 2007				
Income from third parties	142,935	30,491		173,426
Income within the Group	13,971	21,163	(35,134)	0
Segment income	156,906	51,654	(35,134)	173,426
Segment operating expenses	(58,374)	(24,838)	35,134	(48,078)
EBITDA	98,532	26,816		125,348
Depreciation	(27,995)	(9,174)	27	(37,142)
Segment earnings, EBIT	70,537	17,642	27	88,206
Segment assets on 31.12.2007	5,071,638	794,512	(730,765)	5,135,386
Shares in associated companies on 31.12.2007	6,255	663	0	6,918
Total assets 31.12.2007	5,077,893	795,175	(730,765)	5,142,303
Segment liabilities on 31.12.2007	3,435,451	714,747	(608,040)	3,542,158
Total liabilities on 31.12.2007	3,435,451	714,747	(608,040)	3,542,158

Salaries and salary related expenses

6. Salaries and salary related expenses are specified as follows:

	2008 1.1.-30.6.	2007 1.1.-30.6.
Salaries	17,512	17,645
Retirement pension and pension increase	3,318	3,355
Other salary related expenses	3,952	4,242
	24,782	25,242

Salaries and salary related expenses are divided as follows in the income statement:

Energy production costs	7,653	7,887
Transmission costs	6,267	6,597
Cost of general research	108	806
Other operating expenses	10,754	9,952
	24,782	25,242

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Notes, contd.:

Other operating cost

7. Other operating expenses are specified as follows:

	2008 1.1.-30.6.	2007 1.1.-30.6.
Corporate office	2,118	2,016
Finance	2,144	1,758
Human resources	706	629
Information technology	1,811	1,532
Engineering and construction	538	1,516
Pension	3,165	2,806
Other shared cost	891	839
	11,373	11,097
Other cost - relating to subsidiaries	5,199	3,073
Depreciation	1,942	2,018
	18,514	16,188

Financial income and (expenses)

8. Financial income and (expenses) are specified as follows:

	2008	2007
Interest income	9,287	2,851
Interest expenses	(93,144)	(67,805)
Guarantee fee paid to owners	(3,553)	(3,264)
Capitalized interest costs	5,347	33,972
Total interest expenses	(91,350)	(37,097)
Exchange rate difference	(144,475)	300,183
Fair value changes in derivatives	223,942	65,473
Net income (expense) on financial assets and liabilities	79,467	365,656
Effect of associated and other companies	(1,018)	0
Financial income and (expenses)	(3,614)	331,409

The borrowing cost on new long-term debt used for financing construction expenditure was 4.01%. The interest cost capitalized, including the guarantee fee, was 4.26% on funds invested in assets under construction.

9. Income tax

In May of 2008 the Icelandic Parliament approved a decrease in the income tax rate from 26% to 23,5% for partnerships and from 18% to 15% for corporations, as of January 1, 2008, effective for the 2009 tax year. The effect of this change results in a decrease in the tax asset of USD 10,4 million at the beginning of 2008, which is expensed in the income statement. Also due to the effect from the results of the portion from associated companies, and subsidiaries, the actual income tax rate for the group in the first half of the year 2008 is 37,9% compared to 26,5% for the same period 2007.

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Non-current assets

10. Property, plant and equipment, their initial value and depreciation is specified as follows:

Cost value	Power stations	Trans- mission	Communicat. equipment	Other assets	Total
Total value on 1.1.2007	2,697,778	474,287	11,856	70,698	3,254,619
Additions during the period	7,509	49,253	878	8,015	65,655
Transferred from assets					
in construction	1,708,553	163,184	0	(147)	1,871,590
Sold and disposed of	0	0	0	(1,509)	(1,509)
Total value on 31.12.2007	4,413,840	686,724	12,734	77,057	5,190,355
Translation difference		(149,545)	(2,773)	(8,144)	(160,462)
Revaluation	0	102,182	0	0	102,182
Additions during the period	14,971	5,886	446	2,144	23,447
Sold and disposed of	0	0	0	(285)	(285)
Total value on 30.6.2008	4,428,811	645,248	10,407	70,772	5,155,237
Depreciation and impairment loss					
Total value on 1.1.2007	1,428,413	17,258	4,746	19,590	1,470,006
Depreciation of the period	48,677	17,217	834	3,251	69,978
Sold and disposed of	0	0	0	(1,291)	(1,291)
Total value on 31.12.2007	1,477,090	34,474	5,579	21,550	1,538,694
Translation difference		(8,536)	(1,250)	(776)	(10,562)
Depreciation of the period	37,802	10,675	373	1,547	50,397
Sold and disposed of	0	0	0	(228)	(228)
Total value on 30.6.2008	1,514,892	36,614	4,702	22,093	1,578,301
Book value					
1.1.2007	1,269,365	457,029	7,110	51,108	1,784,613
31.12.2007 og 1.1.2008	2,936,750	652,250	7,154	55,507	3,651,660
30.6.2008	2,913,919	608,634	5,704	48,679	3,576,937

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11. Intangible assets are specified as follows:

	Capitalized development cost	Water and geothermal heat rights	Software	Total
Cost value				
Total value on 1.1.2007	65,347	14,207	3,516	83,070
Additions during the year	28,413	26,361	2,175	56,949
Total value on 31.12.2007	93,760	40,568	5,691	140,019
Translation difference	(1,493)	0	(535)	(2,028)
Additions during the period	26,140	0	863	27,003
Total value on 30.6.2008	118,407	40,568	6,019	164,994
Depreciation and impairment loss				
Total value on 1.1.2007	32,268	0	1,654	33,922
Depreciation and impairment loss during the year	11,247	0	735	11,982
Total value on 31.12.2007	43,515	0	2,389	45,904
Translation difference	(4)	0	(108)	(112)
Depreciation and impairment loss during the period ...	516	0	420	936
Total value on 30.6.2008	44,027	0	2,701	46,728
Book value				
1.1.2007	33,079	14,207	1,862	49,148
31.12.2007 og 1.1.2008	50,245	40,568	3,302	94,113
30.6.2008	74,380	40,568	3,317	118,264

12. The Group´s depreciation and impairment loss is divided as follows:

	2008	2007
Power stations	37,802	22,380
Transmission	10,769	8,139
Other assets	1,825	2,069
Depreciation of assets in operation	50,397	32,588
Impairment loss on development cost	516	4,215
Depreciation of software	420	339
	51,333	37,142

The Group´s depreciation and impairment loss is divided as follows by sector:

Energy production costs	38,105	22,744
Transmission costs	10,769	8,165
Cost of general research	516	4,215
Other operating expenses	1,943	2,018
	51,333	37,142

Interim Financial Statements of Landsvirkjun, June 30, 2008 13 Amounts in thousands of USD

13. Derivative financial instruments in the balance sheet are specified as follows:

Assets		
Embedded derivatives in electricity sales agreements	1,110,969	685,551
Currency swaps	56,926	86,939
Interest rate swaps	1,294	1,622
Other derivatives	790	12,895
	1,169,979	787,007
Derivative financial instruments are divided as follows:		
Long-term component of derivative agreements	1,016,309	659,516
Short-term component of derivative agreements	153,670	127,491
	1,169,979	787,007
Liabilities		
Embedded derivatives in electricity sales agreements	30,892	20,393
Aluminium hedges	229,732	121,457
Currency swaps	29,281	6,358
Interest rate swaps	50,160	18,185
Other derivatives	5,771	40
	345,836	166,433
Derivative financial instruments are divided as follows:		
Long-term component of derivatives	290,408	105,191
Short-term component of derivatives	55,428	61,242
	345,836	166,433

14. **Subsidiaries**

Landsvirkjun's subsidiaries are specified as follows:

	Share
Fjarski ehf.	100.0%
Hraunaveita ehf.	100.0%
Icelandic Power Insurance Ltd.	100.0%
Landsnet hf.	64.7%
Landsvirkjun Power ehf.	100.0%

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Notes, contd.:

Equity

15. The parent company is a partnership owned by the Icelandic State and Eignarhlutir ehf. The State owns a 99.9% share in the Company and Eignarhlutir ehf. holds 0.1%. The Company is an independent taxable entity.

Long-Term Debt

16. Long-term debt are specified as follows by currencies:

	Maturity date	2008 Average interest	Remaining balance	2007 Average interest	Remaining balance
Liabilities in ISK, indexed	2009-2020	3.8%	470,216	3.8%	563,549
Liabilities in ISK, unindexed	2009	13.3%	5,951	13.3%	7,613
Liabilities in CHF	2012-2022	2.5%	97,691	2.5%	88,452
Liabilities in EUR	2008-2026	4.6%	1,602,862	4.2%	1,576,710
Liabilities in GBP	2011-2016	11.4%	18,459	11.4%	18,984
Liabilities in JPY	2009-2013	1.0%	112,576	1.6%	43,871
Liabilities in USD	2008-2026	3.0%	850,535	4.8%	783,905
			3,158,290		3,083,082
Current maturity of long-term debt			(142,175)		(347,329)
Total long-term debt			3,016,116		2,735,753

Interest terms on the parent company's loans range from 1.0-14.5%. On average, nominal interests for the period were approximately 4.36%, but they were approximately 4.69% in the previous year.

The city of Reykjavik and the town of Akureyri provide, together with the State, a Guarantee of Collection for all obligations of Landsvirkjun, entered into before the end of year 2006. From the beginning of the year 2007 the State and Eignarhlutir ehf. provide such a guarantee for all of Landsvirkjun's obligations entered into after that date.

17. According to loan agreements, current maturities of long-term debt are as follows:

	2008
01.07.2008-30.06.2009	142,175
01.07.2009-31.12.2009	3,452
2010	214,039
2011	257,492
2012	230,890
2013	172,225
After 2013	2,138,017
	3,158,290

As in past years, it is assumed that the parent company's long-term loans will be partially refinanced and maturities extended. Therefore, it can be assumed that the amortization schedule will be different from the above.

Interim Financial Statements of Landsvirkjun, June 30, 2008 15 Amounts in thousands of USD

18. Obligation due to demolition

Change in obligation due to demolition is specified as follows:	2008	2007
Balance at 1.1.	5,642	6,781
Expensed during the period	176	431
Balance at the end of the period	5,818	7,212

In accordance with International Accounting Standards, the initial value of fixed operating assets shall include estimated cost of their demolition after their use. Estimated demolition cost of power lines has been assessed and discounted on the basis of useful life. In return, an obligation has been written up among long-term liabilities. An increase in the obligation is expensed on the income statement, amounting to the discounted value in addition to depreciation of the demolition cost.

Other notes

19. On August 22, 2007, a special evaluation committee issued a ruling on a settlement amount for water rights due to the Kárahnjúkar Hydropower Project and the division thereof between owners. The total settlement amounted to 26,4 million USD. The majority of water rights owners in Jökuldalur valley and three owners in Fljótsdalur valley announced that they would not accept the ruling of the committee and filed a case in court on February 22, 2008. Forty cases were confirmed in the District Court of East Iceland on January 15, 2008. The parties involved are owners of one third of the water rights.

    Settlement payments for land rights due to Hálslón in the land of Brú in Jökuldalur valley has been put on hold subsequent to the ruling of the Committee for the Interior, which deemed the land as public land. Land owners will take their case to the courts to put this ruling to the test.

20. The construction of Kárahnjúkar started in 2003 after power sales contracts were entered into with Fjarðarál, a subsidiary of Alcoa Inc. The power station's capacity is 690 MW and transmission lines have been erected to Reyðarfjörður. Five out of six units of the power station were operational in the fourth quarter of year 2007 and the last machine was put on stream in February 2008. Further information on the project can be found at the project's website: www.karahnjukar.is.

    Capitalized construction cost of the part of the power plant of Kárahnjúkar taken into operation amounted to USD 1.720 million at the end of june 2008. At the end of June 2008 construction cost due to that part of the plant not already in operation amounted to USD 320 million.

Financial Risk

21. Risk management

    One of the most important factors in effective risk management is the analysis of risk factors, risk measurement, response in order to limit the risk and monitoring. The Company's Board of Directors has approved a risk management policy, which is based on the following factors:

    - That risk is defined and its origin is known
    - That generally accepted methods are used in assessing the risk
    - That effective management is applied in accordance with authorizations
    - That effective monitoring on risk factors is ensured
    - That information provided to the risk committee and the Board of Directors is accurate and provided on a regular basis

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Landsvirkjun's risk management strategy defines a benchmark in each risk category with respect to hedging limits. The Company's Board of Directors receives on an ongoing basis an overview over the Company's risks and performance of risk management.

Decisions and the supervision of how hedging is implemented are entrusted to a risk management committee. The risk management committee consists of the Managing Director, his deputy and the Financial Director. The Managing Director is the chairman of the risk management committee. Daily risk management is the responsibility of the Head of Risk Management.

The objectives of risk management are to analyze, manage and monitor Landsvirkjun's risks in order to stabilize operating income by reducing operating volatility due to exchange rate, interest and aluminium price changes.

Financial risk is divided into market risk, liquidity risk and counterparty risk.

The Company's market risk consists mainly in three risk categories:
- Risk due to fluctuations in world market price of aluminium
- Interest rate risk due to the Company's liabilities
- Exchange rate risk due to liabilities and income in foreign currencies

Liquidity risk and counterparty risk also fall under financial risk but these risk factors do not significantly affect the Company's operation.

22. Aluminium price risk

Landsvirkjun's risk is based on potential decrease in future aluminium price. The Company has in that respect entered into derivative agreements in order to ensure its income base and reduce fluctuations. In most cases such agreements consist in fixing aluminium price within a certain price range. At the end of June, fair value of such hedge agreements was negative by USD 230 million and the agreements are effective over the next six years. Risk management's authority to make forward hedging on aluminium price gradually decreases. Risk management may hedge up to 100% of next year's aluminium price risk and up to 50% of the equvalent risk six years into the future. About 70% of authorizations has been used as of end of June 2008.

According to IFRS, embedded derivatives are considered as derivative agreements that are a part of other agreements, but are handled as separate derivative agreements when economic characteristics and risk are not closely related to the original agreement. Landsvirkjun has defined the part of electricity sales agreement which are linked to aluminium price level as embedded derivatives. Therefore, the fair value of embedded derivatives in the Company's electricity sales agreements, changes parallel to changes in the aluminium prices. Fair value changes of the agreements are recognized in the income statement. Fair value changes of embedded derivatives have limited effect on the Company's cash flow as the agreements tenor are up to 40 years.

In evaluating embedded derivatives generally accepted evaluation methods are used. The fair value of the agreements is calculated on the basis of the forwards price of aluminium present value with US zero-coupon curve taking volatility effects into account. An effective aluminium forward market is approximately 7 years and therefore the aluminium price must be estimated from that time until the end of the term of the underlying energy agreement.

The price of aluminium has been estimated by extending the forwards aluminium process based on the last effective price in the process. In calculating the fair value of embedded derivatives account has been taken for uncertainty of forward aluminium in relation to long agreement terms.

Landsvirkjun has entered into agreements on the purchase of energy for resale to power intensive industries. Those agreements are linked to price of aluminium and do thus have embedded derivatives. The fair value of the agreements is calculated in the same way and on the basis of the same conditions as the Company's energy agreements.

The fair value of embedded derivatives is specified as follows:	30.06.2008	31.12.2007
Fair value of embedded derivatives at the beginning of the year	667	431
Fair value changes during the period	413	236
Fair value of embedded derivatives at end of period	1,080	667
Division of embedded derivatives is specified as follows:		
Long-term components of embedded derivatives	937	589
Short-term components of embedded derivatives	143	78
Total embedded derivatives	1,080	667

Fair value of embedded derivatives, taken into account derivative agreements entered into in order to hedge amounted to USD 850 million at the end of June 2008. The accompanying table shows fair value changes of agreements related to aluminium price and interest rate changes, but effects due to volatility are insubstantial.

Amounts in the table, which are shown in USD million, are before taxes.

		Aluminium price		
		-10%	0%	10%
Interests	+bp100	-306	-150	3
	0	-172	0	167
	-bp100	-13	175	358

23. Foreign exchange risk

Foreign exchange risk consists in the risk of losses on transactions in relation to the USD. The risk arises due to a difference in the in- and outflow of cash by currency and composition of loan portfolios.

There can be considerable fluctuations in the Company's loan portfolio against the US Dollar over the accounting period, as approx. 50% of the loan portfolio is unprotected against the dollar. The risk from changes in the loan portfolio is limited compared to risk benchmarks determined by the Board at each time. The Company also ensures the fixed rate of cash flow against the functional currency for up to three years with forward agreements and options.

The fair value of foreign exchange swaps was positive by USD 28 million at the end of June 2008. The underlying principal amounts to USD 572 million. The fair value of foreign exchange forward contracts was negative by USD 233 thousand, but the underlying principal amounted to USD 24 million. The fair value of foreign exchange option contracts was negative by USD 6 million and the underlying principal amounted to USD 807 million.

24. Interest rate risk

Landsvirkjun faces interest rate risk as the Company has interest bearing assets and liabilities. Interest bearing financial liabilities are considerable higher than interest bearing financial assets. In the case of fixed interest rates of financial liabilities the market risk consists in that interests can decrease in the future and the Company must therefore carry a higher financing cost than otherwise. In the case of financial instruments with floating interest rate the risk consists in interest increase.

Landsvirkjun has entered into agreements on interest rate swaps, which aim at reducing the Company's interest expenses and risk exposure. At the end of June 2008, the fair value of interest rate swaps was negative by USD 49 million. The underlying amount was USD 438 million. Changes in fair value of interest swap agreements are posted in the income statement.

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25. Liquidity risk

Liquidity risk consists in the risk of losses should the Company not be able to keep to its obligations at maturity date. In order to react to such risk, the Company's liquidity balance is monitored by analyzing inflow of income and outflow of expenses and the maturity dates of financial assets and liabilities. Effective control on liquidity ensures sufficient access to cash flow at each time. In order to ensure clear access to cash and maintain flexible financing possibilities Landsvirkjun has used different funding methods. In the past years financing has mostly taken place through a framework agreement with EMTN (Euro Medium Term Note). With this agreement the Company's visibility on foreign bond market is ensured. The total amount that the Company can borrow through the EMTN agreement is USD 2,5 billion.

Guarantee of Collection from the State for Landsvirkjun's loans and a good credit rating has facilitated the Company's access to capital markets. Landsvirkjun pays an annual guarantee fee of 0.25% on capital of loans at each time. The Company's refinancing risk is limited with an even distribution of amortizations and interest payments and with a long contractual term of outstanding debt.

Landsvirkjun aims at having unreserved access to liquid assets corresponding to the average of the Company's net liquidity need for six months. Falling under liquid assets are cash, short-term securities and open loan lines with financial institutions. At end of June 2008, this amount was USD 137 million, but Landsvirkjun also has access to a Revolving Credit Facility in the amount of USD 350 million, or a total of USD 487 million. The company has therefore ensured liquid assets until the year 2010.

26. Counterparty risk

Counterparty risk is the risk that a counterparty to an agreement does not comply with provisions of the agreement. Landsvirkjun's counterparty risk arising is first and foremost due to the Company's energy agreements and derivatives entered into for hedging purposes, but such agreements are only entered into with financial institutions. Though the amounts involved are considerably high the risk is limited with the Company's requirements for counterparty quality. Landsvirkjun has set a benchmark for derivatives which involves that no derivative agreements are made with financial institutions that have a lower rating than A- from Standard and Poor’s or a comparable rating from other recognized credit rating agencies. An exception to this is if special insurance agreements are made between parties limiting Landsvirkjun's risk. Before energy agreements are made the financial standing of the relevant companies and their parent companies are thoroughly reviewed.