HALF YEAR REPORT

1 JANUARY–30 JUNE 2017

2017

MuniFin
MUNICIPALITY FINANCE

CEO's review

The Finnish economy developed positively in the first half of 2017. The industrial turnover and the gross domestic product increased, consumer confidence strengthened and, most importantly, export and employment showed signs of improvement. Construction, which is seen as a good economic indicator, is growing rapidly and Finland's growth outlooks for 2017 and 2018 have improved.

However, for the customers of Municipality Finance (MuniFin), the first half was characterised by overall uncertainty about the schedule of the health care, social welfare and regional government reform and the effects it will have on the future municipalities. In July 2017 the Government of Finland decided, based on a statement issued by the Constitutional Law Committee, to postpone the reform's entry into force until the beginning of 2020. Also, the narrowing of the Finnish government base may create more uncertainty factors related to the progress of the long-prepared health care, social welfare and regional government reform.

During the first half of the year, the economic situation of municipalities was better than expected, and this reflected in MuniFin's operations as a slight decrease in the demand for financing when compared to the previous year. In addition, the decrease in demand may have been partly caused by the uncertainty over the implementation of the health care, social welfare and regional government reform and the transition period related to the changes in municipal councils, which may stall some investment decisions.

MuniFin's green lending gained momentum as customer demand exceeded estimations. A new green bond for international investors is likely be issued during the second half of the year 2017. In addition to municipalities, operators involved in government-subsidised housing production discovered the green financing that was launched last year. We believe that housing production that promotes sustainable construction and energy efficiency will form a significantly larger share of the project portfolio of green financing in the future.

Price competition in financing tightened significantly during the first half of the year. Despite this, MuniFin was able to maintain its position as the market leader in both of its main customer segments: the municipal sector and government-subsidised housing production.

Furthermore, despite the tough price competition, MuniFin's profit developed positively, and the company's net operating profit for January–June increased to EUR 95.9 million. This shows that our funding operations were extremely successful.

Uncertainty seems to have become the new normal in politics and the economy. MuniFin intends to maintain its competitiveness even in changing circumstances through investments in development and with its efficient and flexible organisation. Our organisation grew significantly in the first half of the year and we will continue with new recruitments throughout the year.

Once again, I thank our customers for past cooperation and their confidence in us. I'm grateful for our employees for their expertise, commitment to our company and customers and for their desire to renew. We will do our utmost to help our customers succeed in the midst of upheavals.

Helsinki, 9 August 2017

Pekka Averio
President and CEO

Half year report
1 January–30 June 2017 [1)]

The first half of 2017 in brief

- The Group's net interest income grew by 13.4% compared to the previous year, reaching EUR 110.6 million (1 January–30 June 2016: EUR 97.5 million).
- The Group's net operating profit amounted to EUR 95.9 million (1 January–30 June 2016: EUR 68.8 million). This represents a 39.4% difference from the previous year. The profit development is a result of successful funding, which has improved the net interest income. The profit includes EUR 7.0 million of unrealised changes in the fair value of financial items (1 January–30 June 2016: EUR -8.5 million).
- The balance sheet total was EUR 33,793 million (31 December 2016: EUR 34,052 million). The reduction compared to the end of 2016 was 0.8%.
- The Group's capital adequacy remained strong, with the ratio of own funds to risk-weighted assets being 72.52% at the end of June (31 December 2016: 66.89%), and the ratio of Common Equity Tier 1 (CET1) to risk-weighted assets was 51.83% (31 December 2016: 46.21%).
- At the end of June, the Group's leverage ratio amounted to 3.72% (31 December 2016: 3.54%).
- The total of new loans withdrawn in January–June amounted to EUR 1,046 million (1 January–30 June 2016: EUR 1,495 million). The lending portfolio stood almost steady at EUR 20,913 million (31 December 2016: EUR 20,910 million).
- At the end of June 2017, the total amount of allocated green financing amounted to EUR 903 million (31 December 2016: EUR 443 million). MuniFin's green financing, launched in 2016, is targeted for environment-friendly investments.
- The leasing portfolio stood at EUR 349 million at the end of June (31 December 2016: EUR 286 million). Growth compared to the end of last year was 22.0%.
- In January–June, EUR 5,411 million was acquired in long-term funding (1 January–30 June 2016: EUR 4,249 million). A total of EUR 4,305 million was issued in short-term debt instruments under the Euro Commercial Paper programme during the first half of the year (1 January–30 June 2016: EUR 4,431 million). The total amount of funding grew to EUR 29,272 million (31 December 2016: EUR 28,662 million). This represents a growth of 2.1% from the end of 2016.
- At the end of June, total liquidity was EUR 8,163 million (31 December 2016: EUR 7,505 million). Growth compared to the end of last year was 8.8%.
- The turnover of MuniFin's subsidiary Inspira was EUR 1.4 million (1 January–30 June 2016: EUR 1.1 million). Net operating profit at the end of June was EUR 0.2 million (1 January–30 June 2016: EUR 0.1 million).

Key Figures (Group)

	30 Jun 2017	31 Dec 2016	30 Jun 2016
Net interest income (EUR million)	110.6	206.1	97.5
Net operating profit (EUR million)	95.9	174.2	68.8
New loans issued (EUR million)	1,046	2,924	1,495
New funding acquisition (EUR million)	5,411	6,702	4,249
Balance sheet total (EUR million)	33,793	34,052	35,850
Common Equity Tier 1 (CET1) (EUR million)	870	776	727
Tier 1 capital (EUR million)	1,218	1,124	1,074
Total own funds (EUR million)	1,218	1,124	1,074
Ratio of Common Equity Tier 1 (CET1) to risk-weighted assets, %	51.83	46.21	45.33
Ratio of Tier 1 capital (T1) to risk-weighted assets, %	72.52	66.89	66.99
Ratio of total own funds to risk-weighted assets, %	72.52	66.89	66.99
Leverage ratio, %	3.72	3.54	3.19
Return on equity (ROE), %	12.57	12.51	10.31
Cost-to-income ratio	0.19	0.17	0.22
Personnel	119	106	107

The calculation formulas for the key figures are given on page 15. All figures presented in this half year report are those of the Municipality Finance Group, unless otherwise stated.

[1)] This half year report is a translation of the original report, "Puolivuosikatsaus 1.1.-30.6.2017", written in Finnish. In case of conflict between the two versions, the Finnish version shall take precedence.

The first half of 2017 in brief

In the first half of 2017, economic growth in Finland showed promising signs of recovery. The industrial turnover and the gross domestic product increased, consumer confidence strengthened and employment and export showed signs of improvement. Construction, which is seen as a good economic indicator, was growing rapidly.

There are still several factors that cause uncertainty over the health care, social welfare and regional government reform's realisation. In July 2017, the Finnish government decided to delay the reform's commencement until the beginning of 2020. The decision followed the statement issued by the Constitutional Law Committee, proposing changes in the Counties Act, the Act on Organising Health and Social Services, and the Act on Freedon of Choice. The narrowing of the Finnish government base adds to the uncertainty related to the implementation of the reform.

The new municipal operating environment after the health care, social welfare and regional government reform is still unclear, and this is reflected in the municipalities' demand for financing for investments not linked to the reform. During the first half, the demand for financing decreased somewhat mainly because the economic situation of municipalities was stronger than expected. In addition, the municipal elections held last spring, and the subsequent period preceding the changes, resulted in a reduced number of investment decisions within municipal councils.

MuniFin's funding operations are carried out globally and, for this reason, the trends in the international capital markets have a strong impact on the company. In the European political arena, the threat of extremist movements rising to power was avoided in the Netherlands and France, but the Brexit plans put a strain on the continent, and there are prevailing risks related to the banking sector, especially in Italy. The world political situation has become substantially tenser as a result of several factors such as terror attacks and increased tension between superpowers.

In the euro area, market rates remain at a historically low level, and the ECB's extensive purchase programmes have maintained market liquidity at a high level. However, the tone of the markets maintained positive, and in the prevailing market conditions MuniFin was able to obtain funding for a very competitive price in the first half of 2017.

Since 1 January 2016, MuniFin has been under the direct supervision of the European Central Bank (ECB). In 2017, this has continued to pose new demands for MuniFin's risk management, reporting and the standardisation of processes. This is one of the reasons the amount of personnel grew significantly in the beginning of 2017 and the company will continue recruiting new staff towards the end of the year.

The great amount of regulatory requirements and the difficulty to predict their implementation schedule pose challenges to financial institutions in general. Banking regulation places special emphasis on the adequacy of own funds. For many years, MuniFin has been preparing for the EU's Capital Requirements Directive (CRD IV) and the Capital Requirements Regulation (CRR) by improving own funds through profit. However, the timetable for the implementation of even the currently known requirements is still somewhat uncertain. For example, the leverage ratio requirement that was expected to take effect in 2018 will most likely take effect in 2020. In addition, the Directive and Regulation are undergoing changes, which adds to the uncertainty about the future.

During 2017, MuniFin has continued to invest heavily in process automation and the development of the organisation's operation and reporting. The company has developed its organisation further in order to fulfil not only various customer requirements, but also the requirements of regulation, the authorities and to do this even better than before. Furthermore, investments in ensuring and developing corporate social responsibility have been increased.

Income Statement and Statement of Financial Position

The Group's business operations remained strong during the first half of 2017. Net operating profit for the review period amounted to EUR 95.9 million (1 January–30 June 2016: EUR 68.8 million). The profit includes EUR 7.0 million of unrealised changes in the fair value of financial items (1 January–30 June 2016: EUR -8.5 million). Of this figure, net income from securities and foreign exchange transactions accounted for EUR 5.5 million (1 January–30 June 2016: EUR -7.2 million) and net income from hedge accounting for EUR 1.5 million (1 January–30 June 2016: EUR -1.3 million). These value changes are related to fluctuations in interest rates, the credit risk arising from counterparties in derivative transactions (CVA), and the market conditions of own derivative liabilities (DVA). The CVA and DVA value changes accounted for EUR -0.2 million of the total value changes (1 January–30 June 2016: EUR -4.5 million).

Net interest income continued developing well, with a growth of 13.4%. At the end of June, net interest income stood at EUR 110.6 million (1 January–30 June 2016: EUR 97.5 million). The improvement in net interest income was attributable to favourable funding. Net interest income includes EUR 0.3 million in commissions from the repurchase of own bonds (1 January–30 June 2016: EUR 0.8 million). In consolidated accounts, the AT1 capital loan is treated as an own equity instrument. The related interest expenses are not recognised through profit or loss in the consolidated accounts, but they are treated similar to dividend distribution, i.e. as a decrease in retained earnings under shareholders' equity upon realisation of payment on an annual basis.

The group's commission expenses totalled EUR 1.9 million at the end of June 2017 (1 January–30 June 2016: EUR 1.8 million). Operating expenses for the period increased by 21% compared to the previous year, amounting to EUR 20.6 million (1 January–30 June 2016: EUR 17.1 million). This was mainly due to financial supervision costs paid to the ECB and to the Financial Supervisory Authority, contributions paid to the EU-level crisis resolution fund and the ongoing regulation projects. The contributions paid to the crisis resolution fund for 2017 have been recorded in their entirety as an expense during the period. Administrative expenses totalled EUR 10.3 million (1 January–30 June 2016: EUR 9.3 million), of which personnel expenses accounted for EUR 6.3 million (1 January–30 June 2016: EUR 5.8 million). Depreciation of tangible and intangible assets amounted to EUR 0.9 million (1 January–30 June 2016: EUR 0.9 million). Other operating expenses were EUR 9.3 million (1 January–30 June 2016: EUR 6.8 million).

The consolidated balance sheet total amounted to EUR 33,793 million at the end of June 2017 (31 December 2016: EUR 34,052 million). The reduction in the balance sheet is mainly due to the strengthening of the euro in relation to other currencies, which has led to diminishing of the on-balance sheet exposures in foreign currencies.

The turnover of MuniFin's subsidiary Inspira was EUR 1.4 million for the period of January–June (1 January–30 June 2016: EUR 1.1 million), while its net operating profit amounted to EUR 0.2 million (1 January–30 June 2016: EUR 0.1 million).

Financing and other services for customers

MuniFin's customers consist of municipalities, municipal federations, municipality-controlled entities and non-profit corporations nominated by the Housing Finance and Development Centre of Finland (ARA). The company offers its customers diverse financial services and is by far the biggest single provider of financing in its customer segments.

MuniFin has continued to actively invest in developing overall customer service in cooperation with and its subsidiary Inspira, which offers advisory services. This enables us to provide our customers with more customised services and a wider range of service products.

Municipalities' demand for financing decreased slightly during January–June 2017. The municipalities need less loans than in previous years because their financial situation is now better. Furthermore, the decrease in demand is partly caused by the uncertainty over the effects of the health care, social welfare and regional government reform. In July 2017, the Finnish government announced that the reform's entry into force is delayed until the beginning of 2020. The upcoming reform has already effected municipalities' willingness to invest by slowing down and delaying even some necessary decisions. In addition to municipal customers, the uncertainty factors related to the health care, social welfare and regional government reform also have an impact on housing production for special groups. Another reason for the decrease in demand in the municipal sector may have been the transition period related to the changes in municipal councils, which may stall some investment decisions.

At the same time, price competition tightened clearly compared to previous years. As the interest rate level is exceptionally low, customers have been able to obtain financing with very favourable terms.

The total volume of loan tender requests received by MuniFin in the period from January to June was EUR 2,367 million (1 January–30 June 2016: EUR 2,179 million). The volume of new loans drawn down in the first six months of the year was somewhat smaller than in the same period the year before, totalling EUR 1,046 million (1 January–30 June 2016: EUR 1,495 million). At the end of June, MuniFin's long-term loan portfolio stood at EUR 20,913 million (31 December 2016: EUR 20,910 million).

MuniFin's Green Financing launched in 2016 has rapidly gained a foothold among the company's customers. The initiatives suitable for green financing are assessed by a green evaluation team comprising external experts. Green financing is believed to increase the municipal sector's environmental investments as the customer costs of green lending and green leasing are lower than the costs of other financial instruments. The discount on the margin for environmental investments is MuniFin's contribution to promoting environmental investments in Finland, as the pricing of green bonds in funding does not yet differ from that of MuniFin's other comparable bonds. During spring 2017, the first government-subsidised housing production projects were approved to receive green financing. At the end of June, the total amount of green financing granted by MuniFin was EUR 903 million (31 December 2016: EUR 443 million).

During the period, the comprehensive reporting and analysis service, Apollo, which was created to manage customers' finance portfolios, was taken into use by an increasing number of municipal enterprise groups and health care districts. This is the first step in providing digital services to MuniFin's customers. The functionalities of Apollo are developed in close cooperation and in accordance with customer feedback and development ideas. In 2017, the service expanded to include, among other things, the real-time management of guarantee liabilities.

In addition to lending, MuniFin's financial leasing is steadily becoming more popular among big investments such as buildings. The pricing of real estate leasing is very close to the price level of lending, enabling us to provide our customers with an alternative form of financing. At the end of June, MuniFin's leasing portfolio stood at EUR 349 million (31 December 2016: EUR 286 million).

January–June 2017 was yet again a quiet period in the market for interest rate hedging. The customers' loss of interest in interest rate hedging was mainly caused by exceptionally low interest rates. MuniFin only offers derivatives for hedging short-term interest rate risk.

Inspira's services were in great demand during the first half of the year. In particular, reports related to preparations for the health care, social welfare and regional government reform were in demand. The major assignments this year included consulting services in several life cycle construction projects and in an arrangement for joint solar energy investments between four Finnish energy companies.

Inspira's turnover in January–June was EUR 1.4 million (1 January–30 June 2016: EUR 1.1 million) and its net operating profit was EUR 0.2 million (1 January–30 June 2016: EUR 0.1 million).

Operations in international capital markets

During the first six months of 2017, the tone of the international markets was good, and the availability of financing was at a good level. MuniFin obtains all of its funding in the international capital markets, and the company benefits from the excellent reputation that Finland and the Finnish municipalities have as targets for investments. In the capital markets, MuniFin is a well-known and active operator: a total of 152 long-term funding transactions were carried out in the period (1 January–30 June 2016: 124).

In January–June 2017, EUR 5,411 million was acquired in long-term funding (1 January–30 June 2016: EUR 4,249 million). A total of EUR 4,305 million was issued in short-term debt instruments under the Euro Commercial Paper programme during the first half of the year (1 January–30 June 2016: EUR 4,431 million) and funding under the programme amounted to EUR 2,535 million at the end of June (31 December 2016: EUR 1,139 million).

Total funding at the end of June 2017 amounted to EUR 29,272 million (31 December 2016: EUR 28,662 million).

During the period, MuniFin issued two benchmark bonds – one denominated in US dollars and one in euros. The issues were one billion euros and one billion US dollars in value. Issuing benchmark bonds denominated in various currencies is part of the diversification measures included in MuniFin's funding strategy. Overall, the company issued bonds denominated in 12 different currencies in the first half of 2017 (1 January–30 June 2016: 13). In addition to currencies, funding is dispersed across various markets, maturities and investor groups.

The domestic demand for green financing has been so strong that, during the second half of 2017, MuniFin plans to issue in the international capital markets the Group's second green bond, i.e. a bond earmarked for environmental investments.

Besides diversification, MuniFin's funding strategy is based on reliability, speed and flexibility. The majority of funding is carried out as standardised issues under debt programmes.

MuniFin credit ratings

Rating agency	Long-term funding	Outlook	Short-term funding
Moody's Investors Service	Aa1	Stable	P–1
Standard & Poor's	AA+	Stable	A–1+

Minimum capital requirements and capital buffers (%) 30 Jun 2017	Capital requirement	Capital conservation buffer [1]	Counter-cyclical buffer [2]	O-SII [3]	Total capital buffers	Total
Common Equity Tier 1 (CET1)	4.5%	2.5%	0.0%	0.5%	3.0%	7.5%
Tier 1 Capital (T1)	6.0%	2.5%	0.0%	0.5%	3.0%	9.0%
Total own funds	8.0%	2.5%	0.0%	0.5%	3.0%	11.0%

Minimum capital requirements and capital buffers (EUR 1,000) 30 Jun 2017	Capital requirement	Capital conservation buffer [1]	Counter-cyclical buffer [2]	O-SII [3]	Total capital buffers	Total
Common Equity Tier 1 (CET1)	75,568	41,982	0	8,396	50,379	125,947
Tier 1 Capital (T1)	100,757	41,982	0	8,396	50,379	151,136
Total own funds	134,343	41,982	0	8,396	50,379	184,722

[1] Act on Credit Institutions (610/2014), Chapter 10, Section 3, and the EU capital requirements Regulation (575/2013; CRR) and Directive (2013/36/EU; CRD IV). Valid from 1 January 2015.

[2] Act on Credit Institutions (610/2014), Chapter 10, Sections 4–5, and the EU capital requirements Regulation (575/2013; CRR) and Directive (2013/36/EU; CRD IV). On 26 June 2017, the Board of the Financial Supervisory Authority decided not to set a capital buffer requirement.

[3] The additional capital requirement for other systemically important institutions: Act on Credit Institutions (610/2014), Chapter 10, Section 8, and the EU capital requirements Regulation (575/2013; CRR) and Directive (2013/36/EU; CRD IV). The additional capital requirement (O-SII) imposed on MuniFin is 0.5% as per the decision of the Financial Supervisory Authority made on 6 July 2015, valid from 7 January 2016.

Capital Adequacy

Minimum capital requirements and capital buffers

The Group's capital adequacy has remained strong and clearly above the statutory requirements and the minimum capital adequacy requirements set by the authorities. The minimum capital adequacy is 8% and that of CET1 capital adequacy 4.5%. The fixed additional capital requirement under the Act on Credit Institutions is 2.5%, while the additional capital requirement for other systemically important credit institutions is 0.5%, and together they increase the minimum CET1 capital adequacy to 7.5% and the overall minimum capital adequacy to 11.0%. The Financial Supervisory Authority decides on the additional capital requirements on a quarterly basis. In June 2017, the Financial Supervisory Authority decided not to impose a variable additional capital requirement on MuniFin.

Furthermore, as part of the annual supervisor's review (SREP), the European Central Bank (ECB) has imposed an additional capital requirement of 1.5% (P2R) on MuniFin, effective from 1 January 2017. This requirement is assessed by the ECB at least once a year. Taking into account the P2R additional capital requirement, the minimum for the CET1 capital adequacy is 9%, and the minimum for the overall capital adequacy 12.5%. In addition, the ECB proposed an indicative additional capital requirement of 4.2% (P2G), the violation of which does not have an effect on, for example, the distribution of profit. When this indicative additional capital requirement is taken into account, the minimum level for CET1 capital adequacy is 13.2%. MuniFin's capital adequacy is many times higher than these capital requirements.

Key figures for capital adequacy

Municipality Finance Group's own funds totalled EUR 1,218 million at the end of June 2017 (31 December 2016: EUR 1,124 million). Common Equity Tier 1 capital (CET1) amounted to EUR 904 million (31 December 2016: EUR 777 million). Tier 1 capital amounted to EUR 1,218 million (31 December 2016: EUR 1,124 million). The unrealised profits from assets measured at fair value (fair value reserve) have been included in CET1 capital (transitional provision for the period 1 January 2015–31 December 2017). Common Equity Tier 1 capital includes the net profit for the period of 1 January–30 June 2017 as the result for the period has been subject to a review by the auditors and can, therefore, be included in CET1 capital based on the permission granted by the ECB in accordance with the Capital Requirements Regulation. Adjustments caused by filters applied to Common Equity Tier 1 consist of MuniFin's own debt valuation adjustment (DVA) and additional value adjustments (AVA). There was no Tier 2 Capital (T2) at the end of the period or during the comparison year.

The assets of MuniFin's subsidiary Financial Advisory Services Inspira Ltd were not taken into account in the Group's own funds. According to the interpretation of the Finnish Financial Supervisory Authority (27 January 2016), shares that the company, according to its Articles of Association, has the right to redeem as stipulated in Chapter 3, Section 7 of the Limited Liability Companies Act (624/2006), cannot be classified as CET1 instruments.

At the end of June, the Parent Company's own funds stood at EUR 1,217 million (31 December 2016: EUR 1,123 million). Common Equity Tier 1 capital (CET1) amounted to EUR 869 million (31 December 2016: EUR 776 million), and Tier 1 capital (T1) amounted to EUR 1,217 million (31 December 2016: EUR 1,123 million). There was no Tier 2 Capital (T2) at the end of the period or during the comparison year.

Consolidated Own Funds

(EUR 1,000)	30 Jun 2017	31 Dec 2016
Common Equity Tier 1 before adjustments	903,641	827,393
Adjustments to Common Equity Tier 1	-33,264	-50,760
COMMON EQUITY TIER 1 (CET1)	**870,377**	**776,633**
Additional Tier 1 capital before adjustments	347,454	347,454
Adjustments to Additional Tier 1 capital	-	-
ADDITIONAL TIER 1 CAPITAL (AT1)	**347,454**	**347,454**
TIER 1 CAPITAL (T1)	**1,217,830**	**1,124,086**
Tier 2 capital before adjustments	-	-
Adjustments to Tier 2 capital	-	-
TIER 2 CAPITAL (T2)	**-**	**-**
TOTAL OWN FUNDS	**1,217,830**	**1,124,086**

Parent Company own funds

(EUR 1,000)	30 Jun 2017	31 Dec 2016
Common Equity Tier 1 before adjustments	902,871	826,865
Adjustments to Common Equity Tier 1	-33,418	-50,865
COMMON EQUITY TIER 1 (CET1)	**869,454**	**776,000**
Additional Tier 1 capital before adjustments	347,669	347,426
Adjustments to Additional Tier 1 capital	-	-
ADDITIONAL TIER 1 CAPITAL (AT1)	**347,669**	**347,426**
TIER 1 CAPITAL (T1)	**1,217,123**	**1,123,426**
Tier 2 capital before adjustments	-	-
Adjustments to Tier 2 capital	-	-
TIER 2 CAPITAL (T2)	-	-
TOTAL OWN FUNDS	**1,217,123**	**1,123,426**

Consolidated key figures for capital adequacy

	30 Jun 2017	31 Dec 2016
Ratio of Common Equity Tier 1 (CET1) to risk-weighted assets (%)	51.83	46.21
Ratio of Tier 1 capital (T1) to risk-weighted assets (%)	72.52	66.89
Ratio of total own funds to risk-weighted assets (%)	72.52	66.89

Key figures for capital adequacy, parent company

	30 Jun 2017	31 Dec 2016
Ratio of Common Equity Tier 1 (CET1) to risk-weighted assets (%)	52.30	46.35
Ratio of Tier 1 capital (T1) to risk-weighted assets (%)	73.22	67.11
Ratio of total own funds to risk-weighted assets (%)	73.22	67.11

The ratio of total own funds to risk-weighted assets was 72.52% (31 December 2016: 66.89%). At the end of June, CET1 capital adequacy was 51.83% (31 December 2016: 46.21%). The Parent Company's capital adequacy was 73.22% (31 December 2016: 67.11 %) and its CET1 capital adequacy was 52.30% (31 December 2016: 46.35%).

For further information on capital adequacy, see Note 10. Descriptions of the capital adequacy management principles are included in the Financial Statements for 2016, and they correspond with the company's currently valid principles.

The leverage ratio and liquidity coverage ratio

A proposal concerning the leverage ratio is currently under consideration at the EU level. The leverage ratio of MuniFin at the end of June 2017 was 3.72% (31 December 2016: 3.54%), calculated using currently valid calculation principles.

At the end of June, the liquidity coverage ratio (LCR) was 141% (31 December 2016: 149%). This clearly exceeds the present regulatory requirement of 80%. The requirement will gradually increase in such a manner that, as of 1 January 2018, in order to comply with the new capital adequacy regulations, the LCR must be 100% or higher.

MuniFin also prepares for the Net Stable Funding Ratio (NSFR) that is being prepared at the EU level and is expected to take effect in 2020.

Governance

In addition to corporate legislation, MuniFin complies with the governance requirements of the Finnish Act on Credit Institutions. The company's governance policy is described in more detail on the company's website. Pursuant to Chapter 7, Section 7 of the Finnish Securities Market Act, upon publication of the Annual Report, MuniFin publishes a Corporate Governance Statement on its website, which includes the description of the main features of the internal audit and risk management systems pertaining to the financial reporting process. The statement also includes the governance descriptions required by the Act on Credit Institutions and information on how the company complies with the Finnish Corporate Governance Code for listed companies published by the Finnish Securities Market Association. Since MuniFin is exclusively an issuer of listed bonds, and since its shares are not subject to public trading, it is not appropriate to directly apply this Code with respect to MuniFin. However, the company has used the Corporate Governance Code as the basis for preparing its own internal Corporate Governance Policy.

Annual General Meeting

The Annual General Meeting of MuniFin was held on 23 March 2017. The AGM confirmed the financial statements for 2016 and discharged the members of the Board of Directors and the CEO from liability for the financial year 2016. In addition, the AGM adopted the proposal of the Board of Directors not to distribute a dividend and to retain the distributable funds of EUR 61,496,269.28 in equity.

Based on the proposal of the Shareholders' Nomination Committee, the AGM appointed the Board of Directors for the 2017–2018 term of office (from the 2017 AGM to the end of the 2018 AGM). The AGM also adopted the proposal of the Shareholders' Nomination Committee on the remuneration of Board members.

In addition, the AGM decided to amend MuniFin's Articles of Association so that the age limitation applied to the election of Board members be removed.

The meeting also elected KPMG Oy Ab as the auditor of the company, with Marcus Tötterman, APA, as the principal auditor. Marcus Tötterman was also the principal auditor in the previous financial year.

The Board of Directors

At the Annual General Meeting of 23 March 2017, the Shareholders' Nomination Committee made a proposal to the meeting regarding the Board members to be elected for the term beginning at the end of the 2017 AGM and concluding at the end of the following AGM. The AGM elected the following members to the Board of Directors:

Helena Walldén (b.1953), Chair of the Board, member of the Board since 2016
- M.Sc. (Eng.)
- Primary occupation: Board professional
- Independent of the company and its significant shareholders

Tapani Hellstén (b.1957), Vice Chair, member of the Board since 2014
- M.A. (Adm. Sc.)
- Primary occupation: Deputy CEO, Keva
- Independent of the company

Fredrik Forssell (b. 1968), member of the Board since 2011
- M.Sc. (Econ.)
- Primary occupation: CIO, Internal equity & FI, Keva
- Independent of the company

Minna Helppi (b. 1967), member of the Board since 2017
- M.Sc. (Econ.)
- Primary occupation: SVP Group Treasurer, Metso Corporation
- Independent of the company and its significant shareholders

Teppo Koivisto (b.1966), member of the Board since 2011
- M.A. (Pol. Sc.)
- Primary occupation: Head of Division, State Treasury
- Independent of the company

Jari Koskinen (b. 1960), member of the Board since 2017
- M.A. (Pol. Sc.)
- Primary occupation: Director General, Association of Finnish Local and Regional Authorities
- Independent of the company and its significant shareholders

Vivi Marttila (b.1966), member of the Board since 2016
- M.Sc. (Econ.)
- Primary occupation: Mayor of the municipality of Simo
- Independent of the company and its significant shareholders

Tuula Saxholm (b. 1961), member of the Board since 2013
- M.Sc. (Econ.)
- Primary occupation: Finance Director, City of Helsinki
- Independent of the company (employed by a significant customer)

In order to organise its work as efficiently as possible, the Board of MuniFin has established Audit, Risk and Remuneration Committees for the assistance and preparation of matters.

The members of the Audit Committee are Tuula Saxholm (chair), Jari Koskinen and Vivi Marttila. The members of the Risk Committee are Fredrik Forssell (chair), Minna Helppi and Teppo Koivisto. The members of the Remuneration Committee are Helena Walldén (chair), Tapani Hellstén and Teppo Koivisto.

From the 2016 AGM to the 2017 AGM, the members of the Board of Directors were: Helena Walldén (Chair), Tapani Hellstén (Vice Chair), Fredrik Forssell, Teppo Koivisto, Sirpa Louhevirta, Vivi Marttila, Tuula Saxholm and Juha Yli-Rajala.

The operations of the Board of Directors and its committees are described in more detail on the company's website.

Personnel

At the end of June 2017, Municipality Finance Group had 119 employees (31 December 2016: 106), of whom 103 were staff of the Parent Company (31 December 2016: 90). Significant increase in staff numbers is a result of changes in the operating environment and customer needs and – most of all – of the need to develop the company administration and processes to comply with the requirements of bank regulation. During the first half of 2017, MuniFin hired new employees for almost all of its functions, including customer service, business development, administrative services, IT, accounting, reporting and risk management.

The President and CEO of MuniFin is Pekka Averio. The Executive Vice President Esa Kallio acts as Deputy to the CEO. In addition, the Executive Management Team of MuniFin includes Senior Vice President Toni Heikkilä, Senior Vice President Jukka Helminen, Senior Vice President Marjo Tomminen and Senior Vice President Mari Tyster.

The CEO of MuniFin's subsidiary Inspira is Kimmo Lehto.

Internal Audit

The internal audit function is outsourced to Deloitte & Touche Ltd, which reports directly to the Board of Directors and its Audit Committee. The company's President and CEO is responsible for the operational coordination of cooperation. Internal audit is tasked with monitoring the reliability and accuracy of MuniFin's financial and other management information. Other tasks include ensuring that the company has sufficient and appropriately organised manual and IT systems for its operations, and that the risks associated with the operations are adequately managed.

Risk management principles and the Group's risk position

MuniFin's operations require sufficient risk management mechanisms to ensure that the company's risk position remains within the limits confirmed by the Board of Directors. MuniFin applies very conservative principles in its risk management. The aim is to keep the overall risk status at such a low level that the company's strong credit rating (Aa1/AA+) is not compromised.

MuniFin regularly maps risks related to its operations and continuously develops methods for recognising and managing them. The company's Risk Management Policy requires the risks to be identified, measured, controlled, monitored and reported on a regular basis. The aim is to recognise new challenges and risks created by changes in the operating environment and to prioritise risks and their management. The company's risks are regularly monitored against the Risk Appetite Framework, which is approved by the Board of Directors and updated at least once a year. The Framework includes numerous limits and targets for different categories. The development of the figures is followed on a monthly basis, or more often if needed.

There were no material changes in the company's risk exposure in the first half of 2017. Risks remained within the set limits, and according to the company's assessment, risk management was performed according to requirements. The Board receives regular reports on the company's risk position as part of monthly risk reporting. Additionally, the Executive Vice President for Risk Management gives the Board's Risk Committee, at least semi-annually, a more extensive overall view of the company's risk position in relation to various risk areas.

The company's risk management is described in more detail in the financial statements for 2016. During 2017, MuniFin has developed its risk management principles by creating more comprehensive, risk type specific policies that the Board of Directors has approved. During the first six months of the year, the company compiled a separate Risk Management Policy document which covers the company's general risk management principles. Additionally, MuniFin defined a Stess-testing Policy which covers all stress tests used by the company and principles related to them. Risk type specific principles, instructions and processes related to credit risk management were updated in addition to an update in the principles of operational risk management. The key principles applied to risk management have not been and will not be changed.

Strategic risks

Strategic risk refers to MuniFin choosing the wrong strategy in pursuit of financially profitable operations, or to the inability of the company to adapt the chosen strategy to changes in the operating environment. The Group's management of strategic risks is based on continuous monitoring and analyses of customer needs, market trend forecasts and changes in the competition and the operating environment. Risks and their significance are evaluated on an annual basis as part of the strategy process and in connection with the annual review carried out by the Executive Management Team. The existing strategy extends to 2022, and it is updated at least annually.

Credit risk

Credit risk refers to the risk of a counterparty defaulting on its commitments to the company. MuniFin may grant loans and leasing financing without separate securities only directly to municipalities or joint municipal authorities. Other loans must be secured with an absolute guarantee issued by a municipality or joint municipal authority or with a state deficiency guarantee. A primary pledge is required when the loan is given a deficiency guarantee by a municipality or the state. The amount of the primary pledge must equal 1.2 times the amount of the loan. The use of these guarantees to reduce credit risk enables the classification of all granted loans as zero-risk when calculating capital adequacy. The company does not bear the residual value risk for the objects of its leasing services. In its history, MuniFin has never incurred credit losses from financing its customers. The company has no customer-specific limits because, in the capital adequacy calculations, all lending is carried out to zero risk customers. However, the company analyses the credit risks and payment behaviour of its customers on a regular basis.

MuniFin is also exposed to credit risk from its liquidity portfolio investments and derivative counterparts. In selecting counterparties, MuniFin evaluates credit risk with principles and limits based on external credit ratings, approved by the Board of Directors. The company also conducts its own credit risk analyses of its derivative counterparts and investment targets. The nominal values of debt securities and equivalent credit values of derivatives (fair value method) are used to monitor credit risk.

With derivative counterparties, MuniFin limits the credit risk of derivative contracts with ISDA Credit Support Annexes. The company has 47 Credit Support Annexes in force. Additionally, the Municipal Guarantee Board's guarantees are used to reduce the counterparty risk related to the derivative transactions with certain counterparties.

Credit Valuation Adjustments (CVA) that take credit risk into account and MuniFin's own Debt Valuation Adjustment (DVA) are applied to the counterparties of derivatives. CVA is calculated for each derivative counterparty by simulating MuniFin's expected positive exposures throughout the maturity of the portfolio, taking into account the probability of default and the estimated amount of loss in the possible event of default. The input information for calculating credit risk adjustments for counterparties includes, for example, the information in the Credit Support Annexes, general market assumptions concerning the probable loss incurred as a result of a default and the expected probabilities of default based on a credit assessment matrix. Similarly, DVA is determined based on MuniFin's expected negative exposures, taking into account the probability of MuniFin's default and loss in case of default.

In May 2016, MuniFin switched to using central counterparties (CCPs) in the clearing of standard over-the-counter (OTC) derivative contracts, as required by "EMIR", the European Markets Infrastructure Regulation. In this model, at the end of a daily clearing process, a CCP becomes the counterparty to each cleared trade. The purpose of CCP clearing is to reduce the counterparty risk. MuniFin uses two global banks as the counterparties for CCP clearing, i.e. as the providers of clearing broker services.

Market risk

Market risk refers to the risk of the company incurring a loss as a result of an unfavourable change in market price or its volatility. Market risks include interest rate, exchange rate, share price and other price risks. MuniFin manages the interest rate risk arising from business operations by means of derivatives. Interest rate risk mainly arises from the differences in interest rate lying between the receivables and liabilities in the balance sheet. In its normal business operations, the company is practically not exposed to exchange rate risks. However, the CCP clearing process of counterparties, as required by the EMIR regulation, makes it necessary to manage collateral in the currency of the derivative contracts. This creates some exchange rate risk for the company. The risk is kept at a low level in line with the company's risk profile. Derivatives are also used to hedge against other market risks. Derivative contracts may only be concluded for hedging purposes.

The company has specified limits for the following market risks:

- currency position risk
- interest rate risk
  - duration
  - Value-at-Risk
  - Economic Value
- income risk
- price risk of pre-funding investments

Liquidity risk

Liquidity risk refers to the risk of the company not being able to perform payment obligations arising from the implementation of financing agreements or other financing activities on their due date. The company manages liquidity risk by limiting the average maturity between customer financing and funding. In addition, the company has set a minimum level (survival horizon) for the available liquidity that should be sufficient for the liquidity needs of, at minimum, six months. Based on the regulatory demands, the company also monitors its liquidity position against Liquidity Coverage Ratio (LCR). The Board of Directors of MuniFin has set the following limits on liquidity risks: refinancing gap, sufficiency of liquid assets measured as a minimum time period and LCR.

The company is a monetary policy counterparty of the Bank of Finland. The company has pledged loans to the Bank of Finland and can obtain credit from the central bank against these collaterals.

Market liquidity risk

Market liquidity risk refers to the company failing to realise or cover its position at market price due to the market lacking depth or not functioning due to disruption.

The company continuously monitors the liquidity of markets and investment products. In addition, derivative contracts are concluded in accordance with established market standards. Nearly all market values of debt securities valued at fair value are calculated based on quotations received from the market. For the remaining debt securities, the market value is calculated using other market information.

Operational risks

Operational risk refers to the risk of financial loss or other negative consequence due to insufficient or failed internal processes, deficient or unsuccessful procedures, systems or external factors. Operational risks also include risks arising from failure to comply with internal and external regulations (compliance risk), legal risks and reputational risk. Operational risks may result in costs, compensation payable, loss of reputation, false information on position, risk, and results or the interruption of operations.

The operational risks have been recognised as part of the company's functions and processes through an annual operational risk assessment project that departments carry out as a self-assessment. Each function and department is responsible for the management of its operational risks. In addition, the company's Risk Management function and Legal and Compliance departments support the other functions and departments in these tasks and have company-wide responsibility for the coordination of operational risk management.

The realisation of operational risks is monitored through systematic operational risk reporting, based on which operating principles are changed or other measures implemented to reduce operational risks if necessary. Operational risk events are reported to the Executive Management Team and the Board of Directors. No material losses were incurred as a result of operational risks in the first half of 2017.

Events after the review period

No material events occurred after the review period.

Outlook for the second half of 2017

After a period of slow growth, the outlook for the Finnish economy is now encouraging. There are uncertainty factors related to the European economy, but they are not expected to have a significant direct effect on MuniFin's funding, its other operations or the customers' situation.

The health care, social welfare and regional government reform that the Finnish government is preparing transfers some tasks related to the social welfare and health care system from municipalities to the new regions. In July 2017, the Finnish government decided to postpone the reform's entry into force by a year until the beginning of 2020. Despite this, MuniFin does not expect substantial changes to take place in its customers' operating environment or the company's operations.

MuniFin continues to invest heavily in meeting the needs of its customers in a changing operating environment: the development of customer service, service offering and systems continues, just as well as digitalisation of services. The company also further develops the responsibility of all operations in a long-term and systematic manner.

The profitability of MuniFin is expected to remain at a strong level also in 2017.

Helsinki, 9 August 2017
Municipality Finance Plc
The Board of Directors

Further information:
Pekka Averio, President and CEO,
tel. +358 500 406 856

Esa Kallio, Executive Vice President, Deputy CEO,
tel. +358 50 337 7953

Marjo Tomminen, Executive Vice President, CFO,
tel. +358 50 386 1764

The Group's Development

	30 Jun 2017	31 Dec 2016	30 Jun 2016
Turnover (EUR million)	101.2	183.7	82.8
Net interest income (EUR million)	110.6	206.1	97.5
% of turnover	109.2	112.2	117.7
Net operating profit (EUR million)	95.9	174.2	68.8
% of turnover	94.7	94.8	83.0
Cost-to-income ratio	0.19	0.17	0.22
Loan portfolio (EUR million)	20,913	20,910	20,513
Total funding acquired (EUR million)	29,272	28,662	30,255
Balance sheet total (EUR million)	33,793	34,052	35,850
Return on equity (ROE) (%)	12.57	12.51	10.31
Return on assets (ROA) (%)	0.45	0.41	0.32
Equity ratio (%)	3.71	3.48	3.05
Common Equity Tier 1 (CET1) (EUR million)	870	777	727
Tier 1 capital (EUR million)	1,218	1,124	1,075
Total own funds (EUR million)	1,218	1,124	1,075
Ratio of Common Equity Tier 1 (CET1) to risk-weighted assets (%)	51.83	46.21	45.33
Ratio of Tier 1 capital (T1) to risk-weighted assets (%)	72.52	66.89	66.99
Ratio of total own funds to risk-weighted assets (%)	72.52	66.89	66.99
Leverage ratio (%)	3.72	3.54	3.19
Personnel	119	106	107

Calculation of key figures

Turnover

Interest income + commission income + net income from securities and foreign exchange transactions + net income from available-for-sale financial assets + net income from hedge accounting + other operating income

Cost-to-income ratio

$$\frac{\text{Commission expenses + administrative expenses + depreciation + other operating expenses}}{\text{Net interest income + commission income + net income from securities and foreign exchange transactions + net income from available-for-sale financial assets + net income from hedge accounting + other operating income}}$$

Return on equity (ROE) (%)

$$\frac{\text{Net operating profit - taxes}}{\text{Equity and non-controlling interest (average of values at the beginning and end of the reporting period)}} \times 100$$

Return on assets (ROA) (%)

$$\frac{\text{Net operating profit - taxes}}{\text{Average balance sheet total (average of values at the beginning and end of the reporting period)}} \times 100$$

Equity ratio (%)

$$\frac{\text{Equity and non-controlling interest}}{\text{Balance sheet total}} \times 100$$

Ratio of Common Equity Tier 1 (CET1) to risk-weighted assets (%)

$$\frac{\text{Common Equity Tier 1 (CET1)}}{\text{Risk-weighted assets}} \times 100$$

Ratio of Tier 1 capital to risk-weighted assets (%)

$$\frac{\text{Tier 1 capital}}{\text{Risk-weighted assets}} \times 100$$

Ratio of total own funds to risk-weighted assets (%)

$$\frac{\text{Total own funds}}{\text{Risk-weighted assets}} \times 100$$

Leverage ratio (%)

$$\frac{\text{Tier 1 capital}}{\text{Total exposure}} \times 100$$

Loan portfolio

Loans and advances to the public and public sector entities - Leasing assets

Consolidated statement of financial position

(EUR 1,000)	30 Jun 2017	31 Dec 2016
ASSETS		
Cash and balances with central banks	2,089,438	988,949
Loans and advances to credit institutions	749,463	438,811
Loans and advances to the public and public sector entities	21,261,996	21,195,739
Debt securities	7,316,545	7,469,437
Shares and participations	9,706	9,695
Derivative contracts	2,046,683	3,634,302
Intangible assets	7,453	6,776
Tangible assets	2,640	2,462
Other assets	122,427	62,946
Accrued income and prepayments	186,789	243,068
TOTAL ASSETS	**33,793,141**	**34,052,186**
LIABILITIES AND EQUITY		
LIABILITIES		
Liabilities to credit institutions	3,990,275	5,362,317
Liabilities to the public and public sector entities	819,504	872,919
Debt securities issued	25,501,771	24,584,169
Derivative contracts	1,868,341	1,676,859
Other liabilities	32,292	4,444
Accrued expenses and deferred income	137,055	194,860
Subordinated liabilities	-	-
Deferred tax liabilities	189,500	172,185
TOTAL LIABILITIES	**32,538,737**	**32,867,753**
EQUITY AND NON-CONTROLLING INTEREST		
Share capital	42,583	42,583
Reserve fund	277	277
Fair value reserve	25,430	19,519
Reserve for invested non-restricted equity	40,366	40,366
Retained earnings	798,092	734,107
Total equity attributable to parent company equity holders	**906,748**	**836,852**
Non-controlling interest	**202**	**127**
Other equity instruments issued	**347,454**	**347,454**
TOTAL EQUITY	**1,254,403**	**1,184,433**
TOTAL LIABILITIES AND EQUITY	**33,793,141**	**34,052,186**

Consolidated income statement

(EUR 1,000)	1 Jan-30 Jun 2017	1 Jan-30 Jun 2016
Interest income	93,422	92,702
Interest expense	17,143	4,836
NET INTEREST INCOME	**110,564**	**97,538**
Commission income	1,822	1,303
Commission expense	-1,903	-1,836
Net income from securities and foreign exchange transactions	4,425	-9,333
Net income from available-for-sale financial assets	-46	-569
Net income from hedge accounting	1,533	-1,305
Other operating income	62	45
Administrative expenses	-10,335	-9,336
Depreciation and impairment on tangible and intangible assets	-932	-900
Other operating expenses	-9,338	-6,822
NET OPERATING PROFIT	**95,852**	**68,785**
Income tax expense	-19,193	-13,776
PROFIT FOR THE PERIOD	**76,659**	**55,009**
Profit attributable to:		
Equity holders of the parent company	76,585	54,978
Non-controlling interest	75	30

Statement of comprehensive income

(EUR 1,000)	1 Jan-30 Jun 2017	1 Jan-30 Jun 2016
Profit for the period	76,659	55,009
Components of other comprehensive income		
Items to be reclassified to profit or loss in subsequent periods		
Available-for-sale financial assets (fair value reserve):		
Net change in fair value	7,253	-277
Net amount transferred to profit or loss	136	-35
IAS 39 reclassification adjustment	-	19
Taxes related to components of other comprehensive income	-1,478	59
TOTAL COMPREHENSIVE INCOME FOR THE PERIOD	**82,571**	**54,774**
Total comprehensive income attributable to:		
Equity holders of the parent company	82,496	54,744
Non-controlling interest	75	30

Consolidated statement of cash flows

(EUR 1,000)	1 Jan - 30 Jun 2017	1 Jan - 30 Jun 2016
CASH FLOW FROM OPERATING ACTIVITIES	**1,133,099**	339,029
Net change in long-term funding	978,391	533,501
Net change in short-term funding	1,544,985	888,747
Net change in long-term loans	-157,331	-351,987
Net change in short-term loans	-285,111	-40,014
Net change in investments	402,377	-497,990
Net change in collaterals	-1,452,357	-271,533
Interest on assets	49,881	63,493
Interest on liabilities	59,547	22,605
Other income	17,713	13,090
Payments of operating expenses	-24,792	-19,483
Taxes paid	-206	-1,401
CASH FLOW FROM INVESTING ACTIVITIES	**-1,758**	**-1,588**
Acquisition of tangible assets	-487	-478
Acquisition of intangible assets	-1,271	-1,110
CASH FLOW FROM FINANCING ACTIVITIES	**-15,750**	**-7,989**
Dividends paid and other profit distribution	-15,750	-7,989
CHANGE IN CASH AND CASH EQUIVALENTS	**1,115,591**	**329,452**
CASH AND CASH EQUIVALENTS AT 1 JANUARY	**996,480**	**1,945,709**
CASH AND CASH EQUIVALENTS AT 30 JUNE	**2,112,071**	**2,275,160**

Cash and cash equivalents include the following balance sheet items:
Cash and balances with central banks and loans and advances to credit institutions payable on demand.

(EUR 1,000)	30 Jun 2017	30 Jun 2016
Cash and balances with central banks	2,089,438	2,269,773
Loans and advances to credit institutions	22,633	5,387
TOTAL CASH AND CASH EQUIVALENTS	**2,112,071**	**2,275,160**

Consolidated statement of changes in equity

	Total equity attributable to parent company equity holders								
(EUR 1,000)	Share capital	Reserve fund	Fair value reserve	Reserve for invested non-restricted equity	Retained earnings	Total	Non-controlling interest	Other equity instruments issued	Total equity
EQUITY AT 31 DECEMBER 2015	**42,583**	**277**	**11,354**	**40,366**	**601,065**	**695,645**	**216**	**347,454**	**1,043,314**
Interest paid on Additional Tier 1 capital loan	-	-	-	-	-6,300	-6,300	-	-	-6,300
Dividends paid for 2015	-	-	-	-	-	-	-114	-	-114
Profit for the period	-	-	-	-	139,342	139,342	26	-	139,367
Components of other comprehensive income									
Items to be reclassified to profit or loss in subsequent periods									
Available-for-sale financial assets (fair value reserve):									
Net change in fair value	-	-	10,281	-	-	10,281	-	-	10,281
Net amount transferred to profit or loss	-	-	-98	-	-	-98	-	-	-98
IAS 39 reclassification adjustment	-	-	24	-	-	24	-	-	24
Taxes related to components of other comprehensive income	-	-	-2,041	-	-	-2,041	-	-	-2,041
EQUITY AT 31 DECEMBER 2016	**42,583**	**277**	**19,519**	**40,366**	**734,107**	**836,852**	**127**	**347,454**	**1,184,433**
Interest paid on Additional Tier 1 capital loan	-	-	-	-	-12,600	-12,600	-	-	-12,600
Dividends paid for 2016	-	-	-	-	-	-	-	-	-
Profit for the period	-	-	-	-	76,585	76,585	75	-	76,659
Components of other comprehensive income									
Items to be reclassified to profit or loss in subsequent periods									
Available-for-sale financial assets (fair value reserve):									
Net change in fair value	-	-	7,253	-	-	7,253	-	-	7,253
Net amount transferred to profit or loss	-	-	136	-	-	136	-	-	136
IAS 39 reclassification adjustment	-	-	-	-	-	-	-	-	-
Taxes related to components of other comprehensive income	-	-	-1,478	-	-	-1,478	-	-	-1,478
EQUITY AT 30 JUNE 2017	**42,583**	**277**	**25,430**	**40,366**	**798,092**	**906,748**	**202**	**347,454**	**1,254,403**

Notes to half year report

Note 1. Basis of preparation of the half year report

The half year report has been prepared in accordance with International Financial Reporting Standards (IFRS). This half year report complies with IAS 34 Interim Financial Reporting and the accounting principles presented in the 2016 consolidated financial statements.

The figures in the notes to the financial statements are presented in thousand euro. All figures in the half year report have been rounded, so the total of individual figures may differ from the total figure presented. The half year report has been subject to a review by the auditors.

Application of new and amended standards and interpretations

IFRS 9 Financial Instruments

IFRS 9 Financial Instruments and subsequent amendments (effective for financial years beginning on or after 1 January 2018): IFRS 9 replaces the current IAS 39. The new standard includes updated guidelines on the recognition and measurement of financial instruments. It also includes new accounting methodology on expected credit losses for defining financial asset impairment. In addition, requirements concerning general hedge accounting have been revised. The guidelines of IAS 39 regarding the recognition and derecognition of financial instruments have been retained.

In 2016, the company started its IFRS 9 implementation project, and an impact assessment was performed during the second half of 2016. During the first half of 2017, MuniFin has developed an expected credit loss model and continued analysing and documenting classification changes. The company will continue to update its accounting and monitoring processes. The Municipality Finance Group will adopt IFRS 9 on its mandatory application date 1 January 2018. The quantitative impact of applying IFRS 9 cannot be estimated with certainty, as the impact depends on the financial instruments the company owns at the end of the reporting period in question, the selected accounting principles and management discretion.

Classification and measurement

According to IFRS 9 financial assets are classified at amortised cost, at fair value through other comprehensive income or at fair value through profit and loss. The classification of financial assets is dependent on the business model applied to managing the financial assets and the characteristics of their contractual cash flows. In the business model assessment, MuniFin has divided financial assets into portfolios based on how the financial assets are managed in order to meet business objectives. As part of the evaluation of the portfolio-specific business model in accordance with IFRS 9, the company has analysed its objectives for the management of financial assets, the content of management reporting and the historical sales behaviour of these the portfolios.

The asset classification is not expected to have a large impact on MuniFin's income statement or statement of financial position. The company's business models for the management of various financial assets match the current classification fairly well. Based on the business model, most of the investments currently classified as available-for-sale can be classified at fair value through other comprehensive income (FVOCI), while loans and receivables and held-to-maturity investments can be measured at amortised cost. For the contractual cash flows of its financial assets, the company has carried out SPPI tests in order to evaluate whether the contractual cash flows fulfil the IFRS 9 requirement of being solely payments principal and interest. The majority of MuniFin's financial assets fulfil the SPPI criterion, with some exceptions that will be measured at fair value through profit and loss instead of measuring them in accordance with the category defined by the business model. Items which will be measured through profit and loss as a result of the SPPI test are not expected to have a significant impact on MuniFin's income statement or statement of financial position. This reclassification is not expected to have a major impact on capital adequacy.

The company will continue its assessment of the classification of liabilities. The objective of the assessment is to identify possibilities for reducing or eliminating accounting mismatch by classifying liabilities at fair value through profit and loss (fair value option).

Impairment

The IFRS 9 requirements for impairment are based on a model of expected credit losses instead of the current model that is based on incurred losses. The general expectation is that with the adoption of the standard, the expected credit losses calculated in accordance with IFRS 9 will increase the amount of impairment and thus reduce equity and weaken capital adequacy. The impairment test will be carried out in accordance with IFRS 9 for all financial assets measured at fair value through other comprehensive income or amortised cost, finance lease receivables and off-balance sheet binding loan commitments. Based on an initial analysis, MuniFin estimates that the expected credit loss model will impact MuniFin's profit and the amount of recorded impairment will increase, but its effect will not be significant.

The assets in the scope of the expected credit loss impairment model are classified into three categories. Stage 1 includes assets with no significant increase in credit risk. Stage 2 includes assets with significantly increased credit risk, and stage 3 includes assets that fulfil the definition of default. The definition of default is in line with the company's capital adequacy calculations and risk management. The provision for stage 1 is equivalent to the credit loss expected for 12 months. For stages 2 and 3, the provision is equivalent to the expected credit losses for the entire life time. Based on the current analysis, the majority of the company's assets are included in stage 1. During the first half of 2017, the company has developed a model for calculating the expected credit losses, while simultaneously developing its customer analysis tools in order to take all required input information into account. Expected credit losses are calculated by using the formula Probability of Default * Loss Given Default * Exposure At Default and modelled risk parameters. In addition, the model takes account of forward looking information and macroeconomic scenarios.

Hedge accounting

MuniFin will continue portfolio hedge accounting in accordance with IAS 39. For other fair value hedge accounting, the company will evaluate impact of implementing hedge accounting in accordance with IFRS 9.

Note 2. Derivative Contracts

30 Jun 2017 (EUR 1,000)	Nominal value of underlying instrument	Fair value Positive	Fair value Negative
Contracts in hedge accounting			
Interest rate derivatives			
Interest rate swaps	32,025,149	532,867	-399,809
Cleared by the central counterparty*	6,008,165	49,463	-68,825
Interest rate options	2,368	0	0
Currency derivatives			
Cross currency interest rate swaps	18,997,216	1,315,159	-1,150,273
Total	**51,024,733**	**1,848,026**	**-1,550,082**
Contracts held-for-trading			
Interest rate derivatives			
Interest rate swaps	6,157,629	143,483	-140,235
Cleared by the central counterparty*	794,471	7,093	-69
Interest rate options	102,245	598	-599
Currency derivatives			
Cross currency interest rate swaps	35,701	495	-568
Forward exchange contracts	2,539,432	-	-122,775
Equity derivatives	2,459,919	53,910	-53,910
Other derivatives	20,000	172	-172
Total	**11,314,926**	**198,657**	**-318,258**
Grand total	**62,339,659**	**2,046,683**	**-1,868,341**

Contracts held-for-trading contains all derivatives of the company which are not included in hedge accounting, even if they are entered into for risk management purposes. The category contains derivatives used for hedging financial assets and liabilities which are measured using the fair value option, all derivatives with municipalities, all derivatives hedging derivatives with municipalities. In addition to these, the category contains derivatives used for hedging interest rate risk of the balance sheet, for which no hedged item has been specified, the derivatives which hedge embedded derivatives and the embedded derivatives which have been bifurcated from the financial liability.

* In May 2016 Municipality Finance Plc commenced to clear OTC derivative contracts through central counterparty.

31 Dec 2016 (EUR 1,000)	Nominal value of underlying instrument	Fair value Positive	Fair value Negative
Contracts in hedge accounting			
Interest rate derivatives			
Interest rate swaps	31,802,532	650,615	-470,835
Cleared by the central counterparty*	2,492,040	11,776	-5,749
Interest rate options	6,006	0	0
Currency derivatives			
Cross currency interest rate swaps	18,805,844	2,590,972	-843,870
Total	**50,614,382**	**3,241,587**	**-1,314,705**
Contracts held-for-trading			
Interest rate derivatives			
Interest rate swaps	6,331,530	190,920	-193,443
Cleared by the central counterparty*	385,752	2,575	-172
Interest rate options	42,245	546	-550
Currency derivatives			
Cross currency interest rate swaps	9,708	841	-841
Forward exchange contracts	1,193,691	35,502	-2,412
Equity derivatives	3,230,889	158,284	-158,284
Other derivatives	55,500	6,622	-6,622
Total	**10,863,563**	**392,715**	**-362,153**
Grand total	**61,477,945**	**3,634,302**	**-1,676,859**

Note 3. Pledged assets

(EUR 1,000)	30 Jun 2017	31 Dec 2016
Loans pledged to the central bank	2,286,041	2,284,380
Loans pledged to the Municipal Guarantee Board	18,451,192	18,364,852
Total	**20,737,233**	**20,649,231**

Pledged assets:

1) Municipality Finance is a monetary policy counterparty approved by the central bank (the Bank of Finland), and for this purpose, a sufficient amount of collateral has been pledged to the central bank for possible operations related to this counterparty position.

2) Municipality Finance has pledged the amount of loans shown in the table to the Municipal Guarantee Board. The Municipal Guarantee Board guarantees Municipality Finance's funding and Municipality Finance places collateral for the Municipal Guarantee Board's guarantees as defined in the Act on the Municipal Guarantee Board.

Off-balance-sheet commitments (EUR 1,000)	30 Jun 2017	31 Dec 2016
Loan commitments	2,375,660	1,883,319
Total	**2,375,660**	**1,883,319**

Note 4. Contingent assets and liabilities

The accrued interest on the company's AT1 capital loan is a contingent liability, totaling 3.1 million as per 30th June 2017. The contingent liability will be realised as a deduction of equity once the company decides on the payment of interest. At the end of the comparative period of 2016, the company had a contingent liability of 9.5 million, which realised upon interest payment on 3rd April 2017.

The group does not have any contingent assets on 30th June 2017 or at the end of the comparative period of 2016.

Note 5. Related-party transactions

Municipality Finance's related parties are shareholders whose ownership and corresponding voting in the company exceed 20%, the CEO, the Deputy to the CEO, members of the board of Management and members of the Board of Directors, the spouses and minor children of the persons and corporations controlled by them. Municipality Finance's operations are restricted by the Act on the Municipal Guarantee Board and the framework agreement concluded between the company and the Municipal Guarantee Board, pursuant to which the company may only grant loans to parties stripulated by law (municipalities, municipal federations, corporations that are wholly owned by municipalities or under their control and corporations designated by government authorities and engaged in the renting or production and maintenance of housing on social grounds). Municipality Finance has not carried out any business transactions with related parties with the exception of employment-based remuneration. Municipality Finance does not have loan or financial receivables from related parties.

Municipality Finance's related parties also include its subsidiary Inspira. Transactions with Inspira comprise of fees related to administrative services and advisory services bought by the parent company.

Transactions with, receivables from and liabilities to the subsidiary

Transactions with the subsidiary (EUR 1,000)	1 Jan - 30 Jun 2017	1 Jan - 30 Jun 2016
Sales	31	21
Purchases	67	40

Intercompany receivables and liabilities (EUR 1,000)	30 Jun 2017	30 Jun 2016
Receivables	-	-
Liabilities	14	7

Note 6. Financial assets and liabilities

Financial assets

30 Jun 2017 (EUR 1,000)	Loans and receivables	Available-for-sale financial assets	Held-to-maturity investments	Fair value option	Held-for-trading	Derivatives in hedge accounting	Total	Fair value
Cash and balances with central banks	2,089,438	-	-	-	-	-	2,089,438	2,089,438
Loans and advances to credit institutions	749,463	-	-	-	-	-	749,463	749,463
Loans and advances to the public and public sector entities	21,094,939	-	-	167,056	-	-	21,261,996	23,060,785
Debt securities	-	5,808,580	1,284,202	223,764	-	-	7,316,545	7,317,106
Shares and participations	-	9,706	-	-	-	-	9,706	9,706
Derivative contracts	-	-	-	-	198,657	1,848,026	2,046,683	2,046,683
Total	**23,933,841**	**5,818,286**	**1,284,202**	**390,820**	**198,657**	**1,848,026**	**33,473,832**	**35,273,182**

Loans and advances to the public and public sector entities includes EUR 348,884 thousand receivables based on leasing agreements.

Fair value hedge accounting is applied to EUR 3,959,482 thousand of debt securities available-for-sale in 2017.

Loans and advances to the public and public sector entities includes EUR 6,916,957 thousand in loans and receivables included in fair value hedge accounting for interest rate risk.

Financial liabilities

30 Jun 2017 (EUR 1,000)	Financial liabilities at amortised cost	Fair value option	Held-for-trading	Derivatives in hedge accounting	Total	Fair value
Liabilities to credit institutions	3,990,275	-	-	-	3,990,275	4,067,618
Liabilities to the public and public sector entities	819,504	-	-	-	819,504	823,027
Debt securities issued	22,966,934	2,534,837	-	-	25,501,771	25,519,340
Derivative contracts	-	-	318,258	1,550,082	1,868,341	1,868,341
Subordinated liabilities	-	-	-	-	-	-
Total	**27,776,714**	**2,534,837**	**318,258**	**1,550,082**	**32,179,891**	**32,278,326**

Fair value hedge accounting for interest rate risk is applied to EUR 23,939,578 thousand of financial liabilities at amortised cost in 2017.

Financial assets

31 Dec 2016 (EUR 1,000)	Loans and receivables	Available-for-sale financial assets	Held-to-maturity investments	Fair value option	Held-for-trading	Derivatives in hedge accounting	Total	Fair value
Cash and balances with central banks	988,949	-	-	-	-	-	988,949	988,949
Loans and advances to credit institutions	438,811	-	-	-	-	-	438,811	438,811
Loans and advances to the public and public sector entities	21,009,974	-	-	185,765	-	-	21,195,739	23,246,456
Debt securities	-	6,024,134	995,858	449,445	-	-	7,469,437	7,469,787
Shares and participations	-	9,695	-	-	-	-	9,695	9,695
Derivative contracts	-	-	-	-	392,715	3,241,587	3,634,302	3,634,302
Total	**22,437,735**	**6,033,829**	**995,858**	**635,209**	**392,715**	**3,241,587**	**33,736,934**	**35,788,002**

Loans and advances to the public sector entities includes EUR 285,987 thousand receivables based on leasing agreements.

Fair value hedge accounting is applied to EUR 4,052,339 thousand of debt securities classified as available-for-sale financial assets in 2016. Loans and advances to the public and public sector entities includes EUR 6,819,068 thousand in loans and receivables included in fair value hedge accounting.

Financal liabilities

31 Dec 2016 (EUR 1,000)	Financial liabilities at amortised cost	Fair value option	Held-for-trading	Derivatives in hedge accounting	Total	Fair value
Liabilities to credit institutions	5,362,317	-	-	-	5,362,317	5,531,362
Liabilities to the public and public sector entities	872,919	-	-	-	872,919	888,677
Debt securities issued	23,444,821	1,139,348	-	-	24,584,169	24,650,226
Derivative contracts	-	-	362,154	1,314,705	1,676,859	1,676,859
Subordinated liabilities	-	-	-	-	-	-
Total	**29,680,057**	**1,139,348**	**362,154**	**1,314,705**	**32,496,265**	**32,747,124**

Fair value hedge accounting is applied to EUR 23,907,845 thousand of financial liabilities at amortised cost in 2016.

Note 7. Fair values of financial assets and liabilities

30 Jun 2017 (EUR 1,000)	Carrying amount	Fair value			
		Level 1	Level 2	Level 3	Total
Financial assets at fair value					
Available-for-sale financial assets					
Debt securities	1,849,097	1,849,097	-	-	1,849,097
Shares in investment funds	9,706	9,706	-	-	9,706
Fair value option					
Debt securities	223,764	43,088	180,676	-	223,764
Loans and advances to the public and public sector entities	167,056	-	167,056	-	167,056
Held-for-trading					
Derivative assets	198,657	-	161,984	36,674	198,657
Derivatives in hedge accounting	1,848,026	-	1,848,026	-	1,848,026
Total financial assets at fair value	**4,296,307**	**1,901,891**	**2,357,742**	**36,674**	**4,296,307**
In fair value hedge accounting					
Loans and receivables					
Loans and advances to the public and public sector entities	6,916,957	-	7,394,654	-	7,394,654
Available-for-sale financial assets					
Debt securities	3,959,482	3,959,482	-	-	3,959,482
Total in fair value hedge accounting	**10,876,440**	**3,959,482**	**7,394,654**	-	**11,354,136**
Financial assets at amortised cost					
Loans and receivables					
Cash and balances with central banks	2,089,438	-	2,089,438	-	2,089,438
Loans and advances to credit institutions	749,463	-	749,463	-	749,463
Loans and advances to the public and public sector entities	14,177,982	-	15,499,075	-	15,499,075
Held-to-maturity					
Debt securities	1,284,202	-	1,284,762	-	1,284,762
Total financial assets at amortised cost	**18,301,085**	**-**	**19,622,739**	-	**19,622,739**
Total financial assets	**33,473,832**	**5,861,374**	**29,375,135**	**36,674**	**35,273,182**

30 Jun 2017 (EUR 1,000)	Carrying amount	Fair value			
		Level 1	Level 2	Level 3	Total
Financial liabilities at fair value					
Fair value option					
Debt securities issued	2,534,837	-	2,534,837	-	2,534,837
Held-for-trading					
Derivative liabilities	318,258	-	281,585	36,674	318,258
Derivatives in hedge accounting	1,550,082	-	1,550,082	-	1,550,082
Total financial liabilities at fair value	**4,403,177**	-	**4,366,504**	**36,674**	**4,403,177**
In fair value hedge accounting					
Liabilities to credit institutions	2,943,415	-	3,020,745	-	3,020,745
Liabilities to the public and public sector entities	657,150	-	661,264	-	661,264
Debt securities issued	20,339,013	-	20,353,146	-	20,353,146
Total in fair value hedge accounting	**23,939,578**	-	**24,035,155**	-	**24,035,155**
Financial liabilities at amortised cost					
Liabilities to credit institutions	1,046,860	-	1,046,874	-	1,046,874
Liabilities to the public and public sector entities	162,355	-	161,763	-	161,763
Debt securities issued	2,627,921	-	2,631,357	-	2,631,357
Total financial liabilities at amortised cost	**3,837,136**	-	**3,839,994**	-	**3,899,994**
Total financial liabilities	**32,179,891**	-	**32,241,652**	**36,674**	**32,278,326**

31 Dec 2016 (EUR 1,000)	Carrying amount	Fair value			
		Level 1	Level 2	Level 3	Total
Financial assets at fair value					
Available-for-sale financial assets					
Debt securities	1,971,795	1,968,603	3,193	-	1,971,795
Shares in investment funds	9,695	9,695	-	-	9,695
Fair value option					
Debt securities	449,445	15,573	433,872	-	449,445
Loans and advances to the public and public sector entities	185,765	-	185,765	-	185,765
Held-for-trading					
Derivative assets	392,715	-	325,262	67,453	392,715
Derivatives in hedge accounting	3,241,587	-	3,241,587	-	3,241,587
Total financial assets at fair value	**6,251,002**	**1,993,871**	**4,189,678**	**67,453**	**6,251,002**
In fair value hedge accounting					
Loans and receivables					
Loans and advances to the public and public sector entities	6,819,068	-	7,271,774	-	7,271,774
Available-for-sale financial assets					
Debt securities	4,052,339	4,052,339	-	-	4,052,339
Total in fair value hedge accounting	**10,871,407**	**4,052,339**	**7,271,774**	**-**	**11,324,113**
Financial assets at amortised cost					
Loans and receivables					
Cash and balances with central banks	988,949	988,949	-	-	988,949
Loans and advances to credit institutions	438,811	438,811	-	-	438,811
Loans and advances to the public and public sector entities	14,190,906	-	15,788,918	-	15,788,918
Held-to-maturity					
Debt securities	995,858	-	996,208	-	996,208
Total financial assets at amortised cost	**16,614,525**	**1,427,760**	**16,785,126**	**-**	**18,212,887**
Total financial assets	**33,736,934**	**7,473,970**	**28,246,578**	**67,453**	**35,788,002**

31 Dec 2016 (EUR 1,000)	Carrying amount	Fair value			
		Level 1	Level 2	Level 3	Total
Financial liabilities at fair value					
Fair value option					
Debt securities issued	1,139,348	-	1,139,348	-	1,139,348
Held-for-trading					
Derivative liabilities	362,153	-	294,700	67,453	362,153
Derivatives in hedge accounting	1,314,705	-	1,314,705	-	1,314,705
Total financial liabilities at fair value	**2,816,207**	**-**	**2,748,754**	**67,453**	**2,816,207**
In fair value hedge accounting					
Liabilities to credit institutions	3,162,981	-	3,332,007	-	3,332,007
Liabilities to the public and public sector entities	693,109	-	710,025	-	710,025
Debt securities issued	20,051,756	-	20,063,292	-	20,063,292
Total in fair value hedge accounting	**23,907,846**	-	**24,105,324**	-	**24,105,324**
Financial liabilities at amortised cost					
Liabilities to credit institutions	2,199,337	-	2,199,355	-	2,199,355
Liabilities to the public and public sector entities	179,811	-	178,652	-	178,652
Debt securities issued	3,393,064	-	3,447,585	-	3,447,585
Total financial liabilities at amortised cost	**5,772,211**	-	**5,825,592**	-	**5,825,592**
Total financial liabilities	**32,496,265**	-	**32,679,671**	**67,453**	**32,747,124**

Level 1 Valuation is based on quoted prices for identical assets or liabilities on active and functioning markets. A market is considered to be functioning if trading is frequent and price data is regularly available. Level 1 financial assets comprise investments in debt securities.

Level 2 Valuation is based on input data other than Level 1 quoted prices. Prices can be observed either directly or indirectly. Level 2 financial instruments are not actively traded on functioning markets and the fair value is determined by using generally accepted valuation models and methods. Valuation is based on methods in which contractual cash flows are modeled using forward curves after which the cash flows are discounted using currency and interest based discount curves. Valuation of contracts containing options is performed using interest and option pricing models which are generally accepted on the financial markets. The valuation methods utilise observable input data. Level 2 financial instruments primarily comprise OTC derivatives, the company's own issued bonds and lending.

Level 3 Valuation is based on inputs other than level 1 quoted prices or the observable inputs used in level 2 in valuation methods. Valuation is based on methods in which contractual cash flows are modeled using forward curves after which the cash flows are discounted using currency and interest based discount curves. Valuation of contracts containing options is performed using interest and option pricing models which are generally accepted on the financial markets. These valuation methods may utilise input data, which is not directly observable from the market. Level 3 financial instruments primarily comprise OTC-derivatives and embedded derivatives which have been bifurcated from the company's issued debt securities.

Transfers in the fair value hierarchy

During 2017 and 2016 financial years, no reclassifications have been made between Level 1 and Level 2.

During 2017 no financial assets or liabilities have been transfered into level 3. Due to changes in input data used in the valuation, certain derivatives and embedded derivatives separated from issued bonds have been transferred from level 3 to level 2 in 2016. The transfers are presented using fair values of 31 December 2015.

2017 (EUR 1,000)	Derivative assets Held-for-trading	Derivative liabilities Held-for-trading	Total
1 Jan 2017	**67,454**	**-67,454**	**0**
Change in fair value in the income statement	-17,925	17,925	0
Purchases	6,139	-6,139	0
Sales	-18,994	18,994	0
Transfers into level 3	-	-	-
Transfers out of level 3	-	-	-
30 Jun 2017	**36,674**	**-36,674**	**0**

2016 (EUR 1,000)	Derivative assets Held-for-trading	Derivative liabilities Held-for-trading	Total
1 Jan 2016	121,720	-121,720	0
Change in fair value in the income statement	-13,078	13,078	0
Purchases	18,843	-18,843	0
Sales	-32,510	32,510	0
Transfers into level 3	-	-	-
Transfers out of level 3	-27,521	27,521	0
31 Dec 2016	**67,454**	**-67,454**	**0**

Note 8. Capital instruments

30 Jun 2017 (EUR 1,000)	Currency	Nominal value	Carrying amount	Interest rate	Earliest repayment
1) AT1 capital loan	EUR	350,000	347,454	Fixed	1st April 2022
Total		**350,000**	**347,454**		

31 Dec 2016 (EUR 1,000)	Currency	Nominal value	Carrying amount	Interest rate	Earliest repayment
1) AT1 capital loan	EUR	350,000	347,454	Fixed	1st April 2022
Total		**350,000**	**347,454**		

1) The loan is an unsecured debenture loan included under Additional Tier 1 capital, with special terms designed to fulfil the requirements set for so-called AT1 capital loans in the Capital Requirements Regulation (EU 575/2013). The loan does not have a maturity date. Interest on the loan may only be paid out of distributable funds in accordance with the terms set in the Capital Requirements Regulation, and the company will decide whether interest will be paid on the interest date. The cancellation of interest payments is final, and unpaid interest will not be added to the loan capital. The loan capital will be written off if the proportion of the company's Common Equity Tier 1 (CET1) capital to risk-weighted receivables falls below 5.125%. The company may decide to re-book the loan capital partially or entirely if the Capital Requirements Regulation permits this based on an improvement in the company's finances. The company has the right but not the obligation to buy back the loan on 1 April 2022 or, after that, annually on the interest date, as long as the buy-back is approved in advance by the regulatory authority. The regulatory authority may authorise the repayment of the loan also for particular reasons, for example if legislation or regulatory practice should change in such a way that the company loses the right to deduct the interest in full, or if the company should be forced to make the additional payments mentioned in the loan terms. The authorities may also permit repayment of the loan if the loan's official classification changes in such a way that the loan would be likely to be excluded from the company's own funds, or if it is reclassified as lower-value funds. The loan capital, interest payments and other repayments shall take lower priority than all other higher-level debts in case of the company's liquidation or bankruptcy. AT1 capital loan is recognised in equity in consolidated financial statements. In parent company's financial statements AT1 capital loan is recognised in balance sheet item Subordinated liabilities.

Note 9. Interest income and expense

30 Jun 2017 (EUR 1,000)	Interest income	Interest expense	Net
Assets			
Loans and advances to credit institutions and central banks	907	-5,880	-4,973
Loans and advances to the public and public sector entities	102,515	-	102,515
Debt securities	13,984	-1,069	12,915
Derivatives in hedge accounting	-60,403	-	-60,403
Derivatives held-for-trading	32,767	-15,933	16,835
Other interest income	602	-	602
Interest on assets	**90,373**	**-22,882**	**67,491**
Liabilities			
Liabilities to credit institutions	3,049	-28,954	-25,905
Liabilities to the public and public sector entities	-	-8,868	-8,868
Debt securities issued	-	-171,489	-171,489
Derivatives in hedge accounting	-	249,649	249,649
Subordinated liabilities	-	-	-
Other interest expense	-	-313	-313
Interest on liabilities	**3,049**	**40,024**	**43,073**
Grand Total	**93,422**	**17,143**	**110,564**

Interest expenses on loans and advances to credit institutions and central banks consists of interest paid on central bank deposits and collaterals. Interest expenses on debt securities consists of interest paid on ECPs. Derivative contracts treated as items adjusting interest income and included in hedge accounting are used as hedges for loans and advances to the public and public sector entities and debt securities.

Interest income on liabilities to credit institutions consists of interest received on collaterals. Derivative contracts treated as items adjusting interest expense and included in hedge accounting are used as hedges for liabilities to credit institutions, liabilities to the public and public sector entities and debt securities issued.

30 Jun 2016 (EUR 1,000)	Interest income	Interest expense	Net
Assets			
Loans and advances to credit institutions and central banks	11	-5,082	-5,070
Loans and advances to the public and public sector entities	108,053	-	108,053
Debt securities	-7,660	-482	-8,142
Derivatives in hedge accounting	-35,225	-	-35,225
Derivatives held-for-trading	24,270	-14,238	10,032
Other interest income	527	-	527
Interest on assets	**89,977**	**-19,802**	**70,175**
Liabilities			
Liabilities to credit institutions	2,692	-27,891	-25,199
Liabilities to the public and public sector entities	-	-9,831	-9,831
Debt securities issued	33	-228,831	-228,798
Derivatives in hedge accounting	-	291,818	291,818
Subordinated liabilities	-	-559	-559
Other interest expense	-	-67	-67
Interest on liabilities	**2,725**	**24,638**	**27,363**
Grand Total	**92,702**	**4,836**	**97,538**

Note 10. Capital adequacy

Own funds

Consolidated own funds (EUR 1,000)	30 Jun 2017	31 Dec 2016
Share capital	42,583	42,583
Reserve for invested non-restricted equity	40,366	40,366
Retained earnings	798,092	734,107
Fair value reserve, transitional provision	25,430	19,519
Other reserves	277	277
Accrued interest net of deferred taxes of AT1 capital loan treated as equity	-3,107	-9,459
Common Equity Tier 1 (CET1) capital before regulatory adjustments	**903,641**	**827,393**
Intangible assets	-7,453	-6,776
Deductions due to prudential filters on Common Equity Tier 1	-25,811	-43,985
Common Equity Tier 1 (CET1) capital	**870,377**	**776,633**
Instruments included in Additional Tier 1 capital	347,454	347,454
Additional Tier 1 (AT1) capital	**347,454**	**347,454**
Tier 1 (T1) capital	**1,217,830**	**1,124,086**
Tier 2 (T2) capital	**-**	**-**
Total own funds	**1,217,830**	**1,124,086**

Own funds, parent company (EUR 1,000)	30 Jun 2017	31 Dec 2016
Share capital	43,008	43,008
Reserve for invested non-restricted equity	40,743	40,743
Retained earnings	131,591	61,496
Fair value reserve, transitional provision	25,430	19,519
Other reserves	662,099	662,099
Common Equity Tier 1 (CET1) capital before regulatory adjustments	**902,871**	**826,865**
Intangible assets	-7,606	-6,881
Deductions due to prudential filters on Common Equity Tier 1	-25,811	-43,985
Common Equity Tier 1 (CET1) capital	**869,454**	**776,000**
Instruments included in Additional Tier 1 capital	347,669	347,426
Additional Tier 1 (AT1) capital	**347,669**	**347,426**
Tier 1 (T1) capital	**1,217,123**	**1,123,426**
Tier 2 (T2) capital	**-**	**-**
Total own funds	**1,217,123**	**1,123,426**

Based on EU Capital requirements regulation and FIN-FSA regulations and guidelines 25/2013 unrealised gains on assets measured at fair value (fair value reserve) are included in Common Equity Tier 1 (during 1 January 2015 - 31 December 2017). Common Equity Tier 1 capital includes the net profit for the period of 1 January - 30 June 2017. The result for the period has been subject to a review by the auditors, and therefore can be included in CET1 capital on the basis of permission granted by the ECB in accordance with the Capital Requirements Regulation. Deductions due to prudential filters on Common Equity Tier 1 are made up of MuniFin's debt value adjustment (DVA) and other value adjustments (AVA).

Additional Tier 1 capital contains MuniFin's AT1 capital loan EUR 350 million which was issued on October 1st 2015.

The own funds of the subsidiary Financial Advisory Services Inspira Ltd have not been taken into account in the Group's own funds because, according to the interpretation of the Finnish Financial Supervisory Authority (27 January 2016), shares which a company, according to its Articles of Association, has the right to redeem as stipulated in Chapter 3, Section 7 of the Limited Liability Companies Act (624/2006), cannot be classified as CET1 instruments.

Key figures for capital adequacy

Consolidated key figures for capital adequacy	30 Jun 2017	31 Dec 2016
Ratio of Common Equity Tier 1 (CET1) to risk-weighted assets (%)	51.83	46.21
Ratio of Tier 1 capital (T1) to risk-weighted assets (%)	72.52	66.89
Ratio of total own funds to risk-weighted assets (%)	72.52	66.89

Key figures for capital adequacy, parent company	30 Jun 2017	31 Dec 2016
Ratio of Common Equity Tier 1 (CET1) to risk-weighted assets (%)	52.30	46.35
Ratio of Tier 1 capital (T1) to risk-weighted assets (%)	73.22	67.11
Ratio of total own funds to risk-weighted assets (%)	73.22	67.11

Minimum requirement for own funds

Consolidated minimum requirement for own funds (EUR 1,000)	30 Jun 2017		31 Dec 2016	
	Capital requirement	Risk-weighted assets	Capital requirement	Risk-weighted assets
Credit and counterparty risk, standard method	**105,752**	**1,321,897**	**107,756**	**1,346,956**
Exposures to central governments or central banks	195	2,439	778	9,725
Exposures to regional governments or local authorities	351	4,384	379	4,735
Exposures to multilateral development banks	954	11,920	965	12,068
Exposures to institutions	78,366	979,572	79,937	999,213
Exposures to public sector entities	5,608	70,100	4,275	53,435
Exposures in the form of covered bonds	19,324	241,555	20,303	253,793
Items representing securitisation positions	376	4,706	423	5,284
Exposures in the form of shares in CIUs	107	1,333	107	1,331
Other items	471	5,888	590	7,372
Market risk	**671**	**8,383**	**794**	**9,930**
Credit valuation adjustment risk (CVA VaR), standard method	**1,138**	**14,223**	**1,304**	**16,299**
Operational risk, basic indicator approach	**26,783**	**334,786**	**24,589**	**307,364**
Total	**134,343**	**1,679,288**	**134,444**	**1,680,550**

Minimum requirement for own funds, parent company (EUR 1,000)	30 Jun 2017		31 Dec 2016	
	Capital requirement	Risk-weighted assets	Capital requirement	Risk-weighted assets
Credit and counterparty risk, standard method	**105,738**	**1,321,726**	**107,749**	**1,346,863**
Exposures to central governments or central banks	195	2,439	778	9,725
Exposures to regional governments or local authorities	351	4,384	379	4,735
Exposures to multilateral development banks	954	11,920	965	12,068
Exposures to institutions	78,359	979,488	79,933	999,157
Exposures to public sector entities	5,608	70,100	4,275	53,435
Exposures in the form of covered bonds	19,324	241,555	20,303	253,793
Items representing securitisation positions	376	4,706	423	5,284
Exposures in the form of shares in CIUs	107	1,333	107	1,331
Other items	464	5,802	587	7,334
Market risk	**671**	**8,383**	**794**	**9,930**
Credit valuation adjustment risk (CVA VaR), standard method	**1,138**	**14,223**	**1,304**	**16,299**
Operational risk, basic indicator approach	**25,441**	**318,019**	**24,083**	**301,035**
Total	**132,988**	**1,662,350**	**133,930**	**1,674,128**

Exposure by class

Consolidated exposure by class 30 Jun 2017 (EUR 1,000) Exposure class	On-balance sheet exposure	Off-balance sheet exposure	Derivatives exposure	Total exposure	Risk-weighted assets
Exposures to central governments or central banks	2,593,835	-	-	2,593,835	2,439
Exposures to regional governments or local authorities	10,049,076	854,259	161,037	11,064,372	4,384
Exposures to international organisations	86,976	-	-	86,976	-
Exposures to multilateral development banks	244,051	-	-	244,051	11,920
Exposures to institutions	3,792,196	-	674,041	4,466,237	979,572
Exposures to public sector entities	298,302	-	-	298,302	70,100
Exposures to corporates	5,062,269	503,801	-	5,566,070	-
Exposures secured by mortgages on immovable property	7,413,283	1,017,600	-	8,430,883	-
Exposures in the form of covered bonds	1,969,538	-	-	1,969,538	241,555
Items representing securitisation positions	23,530	-	-	23,530	4,706
Exposures in the form of shares in CIUs	9,679	-	-	9,679	1,333
Other items	79,215	-	-	79,215	5,888
Total	**31,621,950**	**2,375,660**	**835,078**	**34,832,688**	**1,321,897**

Consolidated exposure by class 31 Dec 2016 (EUR 1,000) Exposure class	On-balance sheet exposure	Off-balance sheet exposure	Derivatives exposure	Total exposure	Risk-weighted assets
Exposures to central governments or central banks	1,564,884	-	-	1,564,884	9,725
Exposures to regional governments or local authorities	10,126,880	716,850	223,150	11,066,880	4,735
Exposures to international organisations	133,691	-	-	133,691	-
Exposures to multilateral development banks	256,452	-	-	256,452	12,068
Exposures to institutions	3,670,578	-	741,487	4,412,065	999,213
Exposures to public sector entities	267,177	-	-	267,177	53,435
Exposures to corporates	4,832,744	337,577	-	5,170,321	-
Exposures secured by mortgages on immovable property	7,208,747	828,892	-	8,037,639	-
Exposures in the form of covered bonds	2,055,196	-	-	2,055,196	253,793
Items representing securitisation positions	26,419	-	-	26,419	5,284
Exposures in the form of shares in CIUs	9,668	-	-	9,668	1,331
Other items	92,442	-	-	92,442	7,372
Total	**30,244,877**	**1,883,319**	**964,637**	**33,092,833**	**1,346,956**

Exposure by class, parent company 30 Jun 2017 (EUR 1,000) Exposure class	On-balance sheet exposure	Off-balance sheet exposure	Derivatives exposure	Total exposure	Risk-weighted assets
Exposures to central governments or central banks	2,593,835	-	-	2,593,835	2,439
Exposures to regional governments or local authorities	10,049,076	854,259	161,037	11,064,372	4,384
Exposures to international organisations	86,976	-	-	86,976	-
Exposures to multilateral development banks	244,051	-	-	244,051	11,920
Exposures to institutions	3,791,775	-	674,041	4,465,817	979,488
Exposures to public sector entities	298,302	-	-	298,302	70,100
Exposures to corporates	5,062,269	503,801	-	5,566,070	-
Exposures secured by mortgages on immovable property	7,413,283	1,017,600	-	8,430,883	-
Exposures in the form of covered bonds	1,969,538	-	-	1,969,538	241,555
Items representing securitisation positions	23,530	-	-	23,530	4,706
Exposures in the form of shares in CIUs	9,679	-	-	9,679	1,333
Other items	78,746	-	-	78,746	5,802
Total	**31,621,060**	**2,375,660**	**835,078**	**34,831,798**	**1,321,726**

Exposure by class, parent company 31 Dec 2016 (EUR 1,000) Exposure class	On-balance sheet exposure	Off-balance sheet exposure	Derivatives exposure	Total exposure	Risk-weighted assets
Exposures to central governments or central banks	1,564,884	-	-	1,564,884	9,725
Exposures to regional governments or local authorities	10,126,880	716,850	223,150	11,066,880	4,735
Exposures to international organisations	133,691	-	-	133,691	-
Exposures to multilateral development banks	256,452	-	-	256,452	12,068
Exposures to institutions	3,670,300	-	741,487	4,411,787	999,157
Exposures to public sector entities	267,177	-	-	267,177	53,435
Exposures to corporates	4,832,744	337,577	-	5,170,321	-
Exposures secured by mortgages on immovable property	7,208,747	828,892	-	8,037,639	-
Exposures in the form of covered bonds	2,055,196	-	-	2,055,196	253,793
Items representing securitisation positions	26,419	-	-	26,419	5,284
Exposures in the form of shares in CIUs	9,668	-	-	9,668	1,331
Other items	92,046	-	-	92,046	7,334
Total	**30,244,204**	**1,883,319**	**964,637**	**33,092,159**	**1,346,863**

Leverage ratio

Consolidated leverage ratio (EUR 1,000)	30 Jun 2017	31 Dec 2016
Tier 1 capital (T1)	1,217,830	1,124,086
Total exposure	32,762,752	31,738,039
Leverage ratio (%)	3.72	3.54

Exposures (EUR 1,000)	30 Jun 2017	31 Dec 2016
Consolidated exposure (excl. derivatives and intangible assets)	30,789,180	29,773,440
Derivatives exposure	845,578	1,022,941
Off-balance sheet exposure	1,127,995	941,659
Total	**32,762,752**	**31,738,039**

Breakdown of on-balance sheet exposure (EUR 1,000)	30 Jun 2017 Leverage ratio exposure value	31 Dec 2016 Leverage ratio exposure value
Covered bonds	1,969,538	2,055,196
Exposures treated as sovereigns	10,564,893	9,341,332
Exposures to regional governments, multilateral development banks, international organisations and public sector entities	16,017,202	15,895,000
Institutions	2,125,123	2,363,052
Other exposures	112,424	118,861
Total	**30,789,180**	**29,773,440**

Report on review of the interim report of Municipality Finance Plc as of and for the six-month period ending June 30, 2017

To the Board of Directors of Municipality Finance Plc

Introduction

We have reviewed the consolidated balance sheet as of 30 June, 2017 and the consolidated income statement, the statement of comprehensive income, the statement of changes in equity and the cash flow statement of Municipality Finance Plc for the six-month period then ended, as well as a summary of significant accounting policies and other explanatory notes to the financial statements. The Board of Directors and the Managing Director are responsible for the preparation and fair presentation of this interim financial information in accordance with the International Financial Reporting Standards (IFRS), as adopted by the EU, and other Finnish rules and regulations governing the preparation of interim reports. We will express our conclusion on the interim report based on our review.

Scope of review

We conducted our review in accordance with the Standard on Review Engagements ISRE 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 the standards on auditing and other generally accepted auditing practices and consequently does not enable us to obtain a level of assurance that would make us 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 interim report does not give a true and fair view of the consolidated financial position as at 30 June, 2017 and the consolidated result of its operations and cash flows for the six-month period then ended, in accordance with the International Financial Reporting Standards (IFRS), as adopted by the EU and other applicable rules and regulations governing interim financial reporting preparation in Finland.

Helsinki 9 August, 2017

KPMG OY AB

Marcus Tötterman
Authorised Public Accountant, KHT

Municipality Finance Plc
P.O. BOX 744, Jaakonkatu 3 A
FI–00101 HELSINKI
Tel. +358 9 6803 5666
www.munifin.fi
firstname.lastname@munifin.fi