



# INTERIM REPORT

June 30, 2005

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The main feature of the second quarter of Municipality Finance's current financial year has been the good development of its operations. The financial performance can be looked on as satisfactory. The balance sheet total rose to EUR 5,855.7 million during the period, compared with a corresponding figure of EUR 4,870.1 million one year earlier.

### **Acquisition of funding successful**

The company's acquisition of funding, which set off at a brisk pace at the beginning of the year, continued to grow in the second quarter. During January-June the company acquired long-term funding to the value of EUR 625.8 million compared with a corresponding figure of EUR 409.6 million one year earlier.

During the period under review the acquisition of funding has expanded to take in not only Europe and Japan but also other Asian countries. It has also diversified.

During the period under review seven Municipal Bonds were issued.

### **Success with lending, too**

The half-year period, which concluded at the end of June, proved to be the second-best for lending in the company's history. The focusing on improved customer service in

line with the company's strategy and the new organizational model to support it have produced the expected result in this sector.

The company's long-term lending portfolio at the end of June totalled EUR 4,323.5 million, the equivalent figure one year earlier being EUR 3,834.5 million. The loan portfolio has risen 7.3% from the end of last year and 12.8% compared with the corresponding period last year.

The figure for long-term loans withdrawn (EUR 476.2 million) showed a clear increase over last year, the equivalent figure being EUR 327.1 million.

### **Municipal indebtedness continues**

The general prospects for the local government economy are still very gloomy, because indebtedness will continue to accelerate, thus creating greater difficulties for local government economies. It is vital for the local government sector to keep its economy stable, so that their creditworthiness will remain good and, as a result, the costs of funding reasonable.

Helsinki, August 23, 2005

Pekka Averio  
Managing Director

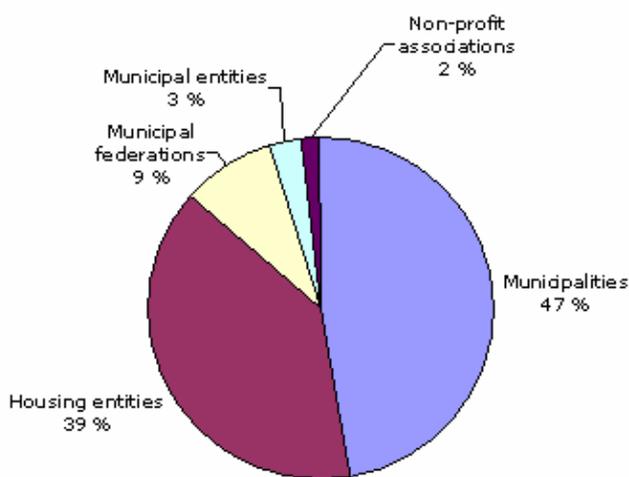
At the end of June Municipality Finance's balance sheet totalled EUR 5,855.7 million (June 30, 2004: EUR 4,870.1 million). The operating profit for January-June was EUR 2.5 million (January 1-June 30, 2004: EUR 2.0 million). The company's long-term loan portfolio stood at EUR 4,323.5 million, an increase of 7.3% from the end of 2004.

### Lending

Municipality Finance's long-term loan portfolio stood at EUR 4,323.5 million at the end of June (June 30, 2004: EUR 3,834.5 million). The loan portfolio increased by 7.3% from the end of 2004 and by 12.8% from the end of June 2004.

In January-June EUR 476.2 million in long-term loans were withdrawn (January 1-June 30, 2004: EUR 327.1 million). At the end of June about EUR 239.3 million in offers had also been accepted (June 30, 2004: EUR 112.8 million). During 2005 the company's marketshare has risen over 50 % of new loans.

Demand for loans at the beginning of the year was livelier than in the previous year. About 11% more invitations to tender came by the end of June compared with the corresponding period in 2004.



Lending by borrower types on June 30, 2005

### Funding

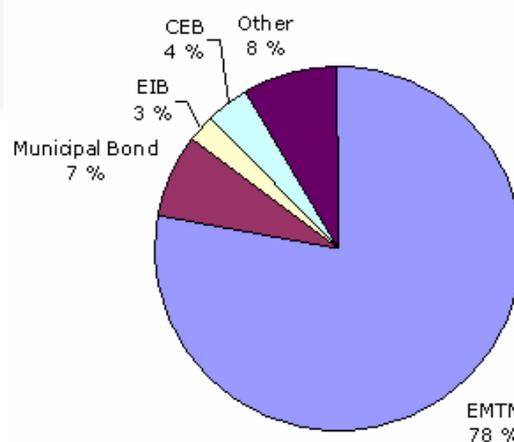
Funding by Municipality Finance is based on several key capital markets, mainly within the following debt programmes:

EMTN	EUR 5,000,000,000
Domestic debt programme	EUR 500,000,000
Treasury Bill programme	EUR 500,000,000

In January-June the company acquired EUR 625.8 million in long-term funding (January 1-June 30, 2004: EUR 409.6 million). Short-term debt instruments under the Treasury Bill programme were issued for a total of EUR 632.3 million during the financial period (January 1-June 30, 2004: EUR 520.3 million). Total funding at the end of June stood at EUR 5,654.8 million (June 30, 2004: EUR 4,664.5 million). 52% of this was in the euro and 48% was denominated in other currencies.

Seven Municipal Bonds were issued.

During the period January-June 2005 funding was livelier than in the previous year. During 2005 funding has been raised besides Japan also from other Asian markets.



Long-term funding sources on June 30, 2005

## Risk management and internal control

Decisions on the general principles of Municipality Finance's risk management are taken by the Board of Directors and implemented by the Managing Director, who is assisted by the Board of Management. Actual risk management and related supervisory functions are separate.

The company's risk standing is monitored regularly by the Board of Management and the Board of Directors on the basis of limits reporting. Derivative instruments are used solely for hedging. The company is fully protected against foreign exchange risks. All funding in foreign currencies is converted into euros through derivative contracts.

In credit risk management, principles and limits approved by the Board of Directors and based on external ratings are applied when choosing counterparties. Counterparty risk is monitored using the real mark to market method.

The Municipality Finance Board of Directors has set limits on the following market risks:

- value-at risk
- refinancing risk/sustainability of financing
- refinancing gap
- interest rate risk based on duration
- minimum and maximum amounts of liquid assets
- currency position risk.

Apart from this, the management receives monthly interest rate sensitivity analyses and value-at-risk calculations.

The company has access to altogether EUR 140 million in arrangements to safeguard its liquidity.

Internal auditing has been outsourced. Deloitte Touche Oy performs the internal auditing.

## Credit ratings

The company's credit ratings have been confirmed the best possible:

	Long-term funding	Short-term funding	Outlook
Moody's Investors Service	Aaa	P1	stable
Standard & Poor's	AAA	A-1+	stable

## Capital adequacy and own funds

Municipality Finance's capital adequacy on June 30, 2005 was 31.79% (June 30, 2004: 54.50%). Capital adequacy is affected by the volume of funds obtained directly via advance funding and invested in debt securities before lending to customers.

The company has never had any non-performing loans or credit losses.

The company's share capital on June 30, 2005 stood at EUR 16.5 million. Own funds totalled EUR 96.6 million.

## Operating result

Municipality Finance's results for the period under review were slightly better than budgeted. The profit before appropriations and taxes for the period January 1-June 30, 2005 was EUR 2.5 million (January 1-June 30, 2004: EUR 2.0 million).

Net income from financial operations was EUR 6.4 million (January 1-June 30, 2004: EUR 5.8 million). The net income of EUR 0.4 million from available-for-sale financial assets comprised profits from the sale of debt securities (January 1-June 30, 2004: EUR 0.1 million). Assets from advance funding are invested in these instruments before the money is issued in loans to customers.

An entry of EUR 2.4 million was made in voluntary provisions as an appropriation from operating profit.

## Personnel and administration

Municipality Finance's personnel is 32.

In accordance with the Articles of Association, Municipality Finance's Board of Directors has nine members.

The Board members are (main job outside the company given in brackets):

- Asko Koskinen (Director, City of Tampere) as Chairman
- Timo Viherkenttä (Deputy Managing Director, Local Government Pensions Institution)
- Juhani Alanen (Deputy Mayor, City of Mikkeli)
- Esa Katajamäki (Director of Finance and Planning, City of Oulu)
- Tapio Korhonen (Finance Director, City of Helsinki)
- Jouko Lehmusto (Head of City Office, City of Turku)
- Eva Liljebloom (Professor, Swedish School of Economics and Business Administration, Helsinki)
- Kari Nars (D.Sc.(Econ & Bus.Adm.), Advisor to the Council of Europe Development Bank, Helsinki)
- Raija Peltonen (Municipal Manager, Municipality of Hartola)

The company's Board of Management includes

- Pekka Averio, Managing Director
- Jukka Reijonen, Deputy Managing Director
- Marjo Tomminen, Director
- Kimmo Lehto, Director

The Annual General Meeting elected KPMG Oy Ab as company auditors, with Riitta Pyykkö, Authorized Public Accountant, as senior responsible auditor.

## Profit and loss account

	1.1. - 30.6.2005	1.1. - 30.6.2004	1.1. - 31.12.2004
Interest income	68,465,190.62	58,777,387.76	122,669,072.90
Interest expenses	-62,108,524.88	-52,972,584.25	-110,861,240.39
<b>NET INCOME FROM FINANCIAL OPERATIONS</b>	<b>6,356,665.74</b>	<b>5,804,803.51</b>	<b>11,807,832.51</b>
Commission expenses	-1,144,925.90	-1,040,263.56	-2,383,824.15
Net income from securities transactions and foreign exchange dealing	2,514.61	514.12	207.83
Net income from available-for-sale financial assets	409,666.95	77,756.69	78,078.12
Other operating income	43,466.41	34,529.47	85,110.69
Administrative expenses			
Staff costs			
Salaries and fees	-958,321.30	-841,236.88	-1,890,289.24
Staff-related costs			
Pension costs	-158,357.79	-133,088.83	-319,421.01
Other staff-related costs	-96,282.90	-76,513.68	-153,543.21
Other administrative expenses	-845,608.48	-831,902.45	-1,693,947.22
Total administrative expenses	-2,058,570.47	-1,882,741.84	-4,057,200.68
Depreciation and write-downs on tangible and intangible assets	-299,028.02	-250,886.08	-535,192.54
Other operating expenses	-848,810.10	-739,422.15	-1,573,889.30
<b>NET OPERATING PROFIT</b>	<b>2,460,979.22</b>	<b>2,004,290.16</b>	<b>3,421,122.48</b>
<b>PROFIT BEFORE APPROPRIATIONS AND TAXES</b>	<b>2,460,979.22</b>	<b>2,004,290.16</b>	<b>3,421,122.48</b>
Appropriations *)	-2,447,000.00	-1,988,000.00	-3,389,455.10
Income taxes	-10,540.19	-11,524.92	-28,077.66
<b>PROFIT FOR THE FINANCIAL YEAR</b>	<b>3,439.03</b>	<b>4,765.24</b>	<b>3,589.72</b>

\*) Appropriations: Voluntary provisions affecting taxation for the period have been entered under the profit for each quarter.

## Key indicators

	30.6.2005	30.6.2004	31.12.2004
Turnover, EUR million	68.9	58.9	122.8
Net operating profit, EUR million	2.5	2.0	3.4
% of turnover	3.57	3.40	2.79
Balance sheet total, EUR million	5,855.7	4,870.1	5,367.6
Return on equity (ROE), %	7.71	7.03	5.55
Yield-expense ratio	1.57	1.51	1.40

Turnover consists of income from interests, leasing operations, commissions, net income from securities transactions and foreign exchange dealing and other operating income.

Return on equity (ROE) is calculated as follows:

$$\frac{\text{net operating profit} - \text{taxes}}{\text{equity capital} + \text{voluntary provisions} - \text{deferred tax liabilities}} \times 100$$

(average of year beginning and year end)

Yield-expense ratio:

$$\frac{\text{net income from financial operations} + \text{commission income} + \text{net income from securities transactions and foreign exchange dealing} + \text{other operating income}}{\text{commission expenses} + \text{administrative expenses} + \text{depreciation} + \text{other operating expenses}}$$

## Balance sheet

<b>ASSETS</b>	<b>30.6.2005</b>	<b>30.6.2004</b>	<b>31.12.2004</b>
Liquid assets			
Cash	1,276.60	1,673.10	1,277.80
Liquid assets	70,723.33	3,098,095.54	3,997,083.11
Debt securities eligible for refinancing with central banks	869,692,502.41	423,324,969.14	588,846,522.22
Claims on credit institutions			
Repayable on demand	40,394.43	110,108.27	478,038.19
Other	54,312,421.12	54,424,020.57	59,778,439.44
Claims on the public and public sector entities	4,323,519,798.33	3,834,450,782.54	4,029,574,609.44
Debt securities			
Public sector entities	252,555,264.81	235,218,937.46	195,645,149.46
Other	251,119,239.99	253,161,655.88	389,939,339.30
Shares and participations	24,219.06	24,219.06	24,219.06
Derivative contracts	28,530,248.90	0.00	15,035,316.12
Intangible assets	768,863.50	922,909.64	901,890.21
Tangible assets			
Other tangible assets	1,240,594.85	1,204,622.11	1,264,260.42
Accrued income and prepayments	73,803,759.77	64,200,381.80	82,070,418.51
<b>TOTAL ASSETS</b>	<b>5,855,679,307.10</b>	<b>4,870,142,375.11</b>	<b>5,367,556,563.28</b>
<b>LIABILITIES</b>	<b>30.6.2005</b>	<b>30.6.2004</b>	<b>31.12.2004</b>
<b>LIABILITIES</b>			
Liabilities to credit institutions and central banks			
To credit institutions			
Other	423,076,744.07	477,271,307.74	452,247,106.73
Liabilities to the public and public sector entities	412,317,552.24	303,771,560.63	311,929,783.28
Debt securities issued to the public			
Bonds	4,593,223,349.12	3,641,187,192.16	4,016,308,974.61
Other	226,205,730.28	242,233,979.44	273,934,258.28
Derivative contracts and other trading liabilities	4,060,326.43	31,953,387.52	115,340,711.06
Other liabilities	582,680.46	519,049.55	596,287.02
Accrued expenses and deferred income	88,937,071.18	70,530,142.36	93,123,407.01
Subordinated liabilities	57,664,296.09	57,664,296.09	57,664,296.09
<b>APPROPRIATIONS</b>			
Voluntary provisions	31,135,000.00	27,286,544.90	28,688,000.00
<b>EQUITY CAPITAL</b>			
Share capital	16,522,000.00	16,522,000.00	16,522,000.00
Other restricted reserves			
Reserve fund	276,711.01	276,711.01	276,711.01
Non-restricted reserves			
Fair value reserve	749,379.00	0.00	0.00
Profit brought forward	925,028.19	921,438.47	921,438.47
Profit for the financial year	3,439.03	4,765.24	3,589.72
<b>TOTAL LIABILITIES</b>	<b>5,855,679,307.10</b>	<b>4,870,142,375.11</b>	<b>5,367,556,563.28</b>
Irrevocable commitments given in favour of a customer	406,685,140.15	240,011,077.00	246,197,466.00

## Off-balance-sheet commitments and capital adequacy

(EUR 1,000)	Values of underlying instruments, for hedging purposes		
	30.6.2005	30.6.2004	31.12.2004
<b>DERIVATIVE CONTRACTS</b>			
Interest rate derivatives			
Interest rate swaps	6,139,082	5,192,414	5,340,261
Currency derivatives			
Forward exchange contracts	164	0	0
Interest rate and currency swaps	3,237,660	1,842,803	2,433,085
Index linked derivatives	114,306	48,682	111,819
Other derivatives			
Commodity linked derivatives	4,500	0	0
	Credit value of contracts without netting		
	30.6.2005	30.6.2004	31.12.2004
Interest rate derivative contracts	406,407	143,714	247,785
Currency derivative contracts	430,169	173,784	225,908
Index linked derivative contracts	19,964	6,044	20,747
Commodity linked derivatives	1,165	0	0
<b>COMMITMENTS AND SECURITY GIVEN</b>	<b>30.6.2005</b>	<b>30.6.2004</b>	<b>31.12.2004</b>
Bonds pledged to the Local Government Pensions Institution	41,387	43,772	42,504
Bonds pledged to the Municipal Guarantee Board	4,277,223	3,781,953	3,981,973
Debt securities pledged to the Municipal Guarantee Board	1,124,700	669,152	975,873
<b>CAPITAL ADEQUACY</b>	<b>30.6.2005</b>	<b>30.6.2004</b>	<b>31.12.2004</b>
Own funds			
Original own funds including capital loans	62,798	59,527	62,798
Deductions, intangible assets	-769	-923	-902
Additional own funds (net)	34,568	33,819	33,819
Total	96,597	92,423	95,715
Risk-weighted claims, investments and off-balance-sheet commitments	303,846	169,569	251,055
<b>Capital adequacy ratio</b>	<b>31.79 %</b>	<b>54.50 %</b>	<b>38.13 %</b>
Ratio of original own funds against risk-weighted claims, investments and off-balance sheet commitments	20.41 %	34.56 %	24.43 %

The profit of the financial period by June 30, 2005 as stated in this interim report, is not included in the original own funds. In the calculation of the company's own funds used for the capital adequacy a latent tax liability calculated at a rate of 26 per cent has been deducted from the voluntary provisions. This interim report has not been audited and no separate auditor's report has been prepared.