

The Icelandic Economic Situation

- Status Report -



VIÐSKIPTARÁÐ ÍSLANDS

ICELAND CHAMBER
OF COMMERCE

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1. INTRODUCTION

During the past year, the Icelandic economy has gone through dramatic changes due to the collapse of its financial sector. Despite these substantial difficulties, general economic activity is still well functional and many Icelandic businesses remain strong and prosperous. Due to inadequate external information flow, a lot of misconceptions have developed concerning the chain of events in the recent scenario and the current status of the Icelandic economy. This status report is meant to give further insight into those issues.

The status report is split into two main parts, part A and part B. Part A, consists of the first 7 chapters and focuses on the general historical background leading up to the collapse and immediate consequences. Part B, from chapter 8 through 17, focuses in more detail on more recent economic developments and policy actions.

The current economic turmoil in Iceland is part of a complex global financial crisis and is by no means an isolated event. Governments around the world have introduced emergency measures to protect their financial system and rescue their banks, as they suffer from a severe liquidity shortage. Thus far, Iceland has been hit particularly hard by this unprecedented financial storm due to the large size of the banking sector in comparison to the overall economy. The Icelandic Government, both past and present, has taken measures and is working hard to resolve the situation. Iceland has been cooperating with its Nordic and European partners and is actively cooperating with the IMF on measures toward further stabilization of the Icelandic economy.

A timeline of the financial crisis in Iceland and the Icesave dispute can be found in [appendix 1 and 7](#).

PART A - HISTORICAL PERSPECTIVE

2. WHAT HAPPENED?

A globalized economy, and an active participant in the EU's common market through the EEA, Iceland is among the first nations to be seriously affected by the global financial turmoil. The situation has hit Icelandic households hard and many have lost a sizeable portion of their savings. Inflation was in double-digit numbers but has now come down to 7.5% and rapidly decreasing, unemployment is around 8% and on the rise. The domestic currency, the Icelandic Krona (ISK), has depreciated significantly, but has now stabilized, i.a. due to measures in the financial exchange markets.

The large size of the banking sector in comparison to Iceland's overall economy is undoubtedly a driving factor behind the current economic turmoil. However, it should be underlined that the Icelandic banks operated under Icelandic and European banking legislation and the strictest of international regulatory standards. Nevertheless, as the liquidity crisis deepened, Iceland's three largest banks, Glitnir, Landsbanki and Kaupthing, whose balance sheets were several times larger than the total output of the Icelandic economy (around 10 times GDP), were no longer able to re-finance their operations.

As a response to these circumstances, the Icelandic Parliament (Althingi) passed a new law, the new Emergency Bank Act, allowing the Icelandic Financial Supervisory Authority (FSA) to take over the operations of the banks.

On the basis of this new law, all three banks are now being restructured and re-capitalized. More information on the new banks is provided in [chapter 8](#) and in [appendix 2](#).

3. WHAT WAS DONE?

Progress in ensuring continued functioning of the Icelandic financial system was achieved at quite an early stage. The Icelandic government prioritized the tasks facing the economy based on their importance for the general public. The first task was to secure the functioning of the domestic banking, payment and settlement systems. The stock market was been re-opened even though the operations are obviously limited considering that the turnover of the stock exchange consisted mostly of transactions related to the financial sector. See further information in [chapters 9 and 15](#).

Furthermore, Iceland was working closely and constructively with other countries to address problems that had aroused in connection with the government takeover of Iceland's three largest commercial banks. The government of Iceland had clearly stated that it intended to honor its legal commitments and seek close cooperation with other countries' authorities. See [chapter 10](#) and [appendix 7](#) on the Icesave Dispute.

In order to prevent a potential shortage of foreign currency, the Central Bank of Iceland implemented temporary restrictions on foreign exchange transactions with the Icelandic krona. These restrictions caused some initial frictions and problems with payments and settlements of international transfers between Iceland and other countries. However, there are no restrictions on currency transactions relating to the import and export of goods and services, see further information in [chapter 9](#) and [appendix 3](#).

4. INTERNATIONAL MONETARY FUND (IMF)

The Icelandic government reached an agreement with the International Monetary Fund (IMF), on 24th of October 2008, on a comprehensive stabilization program, which includes a \$2.1 billion loan from the IMF. The agreement has been approved by the IMF's executive board. There are three main objectives of the IMF program:

1. To contain the negative impact of the crisis on the economy by restoring confidence and stabilizing the exchange rate in the near-term.
2. To promote a viable domestic banking sector and safeguard international financial relations by implementing a sound banking system strategy that is nondiscriminatory and collaborative.
3. To safeguard medium-term fiscal viability by limiting the socialization of losses in the collapsed banks and implementing an ambitious multi-year fiscal consolidation program.

Significant progress was made towards attaining these goals as is confirmed in the IMF's first progress report, which was issued in the first week of February. A statement from the IMF issued in March can be found [here](#) and further information on the Economic Program can be found [here](#). The most up to date statements from the IMF regarding Iceland can be found [here](#).

On 28th of October 2009 the IMF's Executive Board approved the 1st review of the Economic Recovery Program. See [chapters 10 and 11](#).

According to the IMF's economic forecast for Iceland, the Icelandic economy is expected to adjust further in the near term under the program. Given the high leverage in the economy and significant dependence of the private sector on foreign currency and inflation-indexed debt, the economy is expected to enter into a serious recession in 2010. The anticipated large import compression will, however, lead to a rapid swing of the current account into surplus, providing significant support to the exchange rate going forward. See [chapter 12](#). Once confidence is restored and balance sheets readjusted, domestic demand—both investment and consumption—is projected to rebound strongly in 2011. Long-term growth prospects are favorable, in line with Iceland's very strong fundamentals, not least its highly educated labor force, fully funded pension scheme, favorable investment climate and rich natural resource endowment.

5. WHAT HAPPENED TO ICELANDIC BANKS ABROAD?

The Icelandic banks' operations abroad were inevitably affected by the restructuring of the Icelandic banking system. Some of the banks continued to operate abroad as before, like Glitnir in Norway and Kaupthing in Luxemburg, most under new names and owners. Others e.g., Landsbankin's operations in the UK, were shut down and their assets will be used to reimburse deposits and other outstanding liabilities – with the backup of the Deposit Guarantee Funds in the respective country according to EU/EEA regulations.

The deposits of foreign customers in Icelandic banks within the EEA are generally guaranteed according to EU rules. Depending on whether the bank is operated as a subsidiary or a branch, different deposit-guarantee schemes may come into play if assets do not cover commitments. Any foreign subsidiary of an Icelandic bank is fully covered by the deposit-guarantee scheme in the country it operates. All branches of Icelandic banks are covered by the Icelandic Depositor's and Investor's Guarantee Fund, which operates according to the EU-directive relating to these issues. According to the directive, the amount covered is €20,887 for each depositor in each financial institution. These are the basic rules that apply throughout the EU and the EEA, of which Iceland is a part.

One of the provisions approved in the new Emergency Bank Act, is that deposits are to be considered a priority claim on the bank's estates. This was done in order to secure the interests of depositors in the foreign branches. Ideally, a bank's assets will be worth enough to cover all or most outstanding deposits.

In several countries, the respective Government has stepped in and offered further support to their banks, including Icelandic owned subsidiaries. In Sweden and Norway, for example, measures have been taken by the Government to ensure the ongoing operation of banks. This is the best way to safeguard assets and investments, which might otherwise be sold prematurely or liquidated at a price well below true value.

However, the assets of Landsbanki in the UK were frozen via provisions in the Anti Terrorism, Crime and Security Act from 2001. This has been forcefully opposed through diplomatic channels with British authorities, as this clearly had a very damaging effect on the Icelandic banking sector and put Icelandic companies in Britain in a difficult situation. Iceland has also taken the issue up for discussion within NATO and Icelandic authorities have considered legal action. This is also one of the main factors leading to disruptions in Iceland's international payments and settlements system. See [chapter 10](#) and [appendix 7](#) on the Icesave Dispute.

Further information about the old banks can be found [here](#) (for Kaupthing Bank), [here](#) (for Landsbanki) and [here](#) (for Glitnir Bank).

Re-capitalization and reconstruction of the banking system has been concluded. See [chapter 8](#) for more information.

6. FOREIGN EXCHANGE MARKETS

On November 28th, the Icelandic Parliament approved an amendment of Act no. 87/1992 on Foreign Exchange. The Act gave the Central Bank temporary authorization to set rules limiting international capital movements, with the aim of restricting the outflow of foreign currency, for instance, by imposing obligations to repatriate foreign currency. The amended Act makes it clear that all transactions connected to import and export of goods and services are - and will continue to be - unrestricted. It includes a temporary clause which will be in effect for two years and authorizes the Central Bank to impose rules that prohibit foreign exchange related to capital account transactions. The purpose is to prevent excessive short term volatility in the ISK and is in line with the conditions of the IMF Stand-by Arrangement.

On April 4th 2009 the Parliament approved amendments to the Act on Foreign currency. The ISK exchange rate had been sliding steadily, and there were strong indications that the objective of building up foreign currency reserves through mandatory currency repatriation might be in jeopardy. This was attributed primarily to the fact that exporters were not obliged to receive payment for their products in foreign currency.

The amendment was intended to plug this loophole in the legislation. It adds a temporary provision to the Act on Foreign Currency, stipulating that exports of goods and services must be concluded in foreign currency. Following the amendment to the Customs Act, the price of exports recorded on export declarations must be in foreign currency and the enforcement of these provisions will be monitored

On 28th of November 2009 the Act was amended further. See [chapter 9](#) for a further discussion.

7. POLITICAL ENVIRONMENT: NEW GOVERNMENT

Due to strong social pressure and extraordinary circumstances, former Prime Minister Mr. Geir H. Haarde made an announcement in late January that national elections were to be held in May 2009. The coalition Government of the right-wing Independence Party and the Social Democratic Alliance came to an end a few days later.

A week later, a new Government of the Social Democratic Alliance and the Left-Green Movement was formed. According to its official announcement its goal was to assure an effective administration to carry out urgent measures, particularly for the benefit of households and businesses, for rebuilding the banking system, in the field of administrative reform and to carry out measures in favor of increased democracy.

The economic policy of the Government was based on the program already established by the authorities and the IMF. The Government announced it would conduct a prudent fiscal policy according to which the fundamentals of the welfare system would be protected. The two parties agreed on holding early elections, set for 25th of April 2009. The Progressive Party defended the Government in the event of motions of no-confidence.

Following the outcome of the national elections, the Social Democrats and Left-Greens now hold a majority of seats in the Parliament, 34 MP's against the oppositions 29 MP's. The parties decided to continue their coalition partnership and have formed a new Government. According to its announcement the central aim of the Government is to rebalance the state budget by 2013 while at the same time implementing an ambitious plan of job creation and innovation to restore Iceland's position among the most energetic and competitive states in the world by 2020.

A press release with further information on the agenda for the first 100 days of the new Government as well as the co-operation statement by the new Government can be found [here](#).

For more information on the fiscal policies and updated political framework see the respective chapters in Part B of the report, particularly [chapters 13, 14 and 16](#).

There have also been made some amendments to the Act on the Central Bank of Iceland, which are outlined in [appendix 4](#)

PART B - SPRING '09 UNTIL JAN '10

Significant progress has been made over the last five months, both in terms of the financial sector and the Government's program with the IMF.

Icesave dispute: Referendum date set in late February early March. (Ch. 10)

The IMF Program: 1st review concluded and a visit to prepare for the 2nd review. Uncertainty regarding timing of the 2nd review. (Ch. 11)

The Capital Restrictions: First stage of liberalization concluded. (Ch. 9)

Policy Interest Rates: Lowered from 12% to 10% in two steps. At 10% since December. (Ch.12)

The Banks: Reconstruction has been concluded. (Ch. 8)

The European Union: Application in Process (Ch. 13)

The State Treasury: Hit Hard by the Turmoil (Ch. 14)

The NasdaqOMX: Slowly Picking up Pace (Ch. 15)

The Stability Pact: Renewed in October (Ch. 16)

8. BANK RESTRUCTURING CONCLUDED

Since the Icelandic FSA took over the operations of the banks in October 2008 they have been appointed Special Resolution Committees and new banks have been established around the old banks domestic operations, in accordance with the FSA's decision on the disposal of assets and liabilities between the old and new banks. The Government also appointed boards to govern the new state owned banks.

The decision of the FSA on the disposal of assets and liabilities can be found [here](#). Information about the resolution committees can be found [here](#) and various FAQ can be found [here](#).

In April 2009 Deloitte delivered its valuation of the assets that were moved from the old banks to the new banks and Oliver Wyman consulting firm also issued its independent assessment report, see [here](#). The Government also engaged with the corporate advisory firm Hawkpoint to negotiate with creditors of the old banks the appropriate compensation for assets transferred and also to advice on the capitalization and the imbalance issues.

On 20th of July the Government, the boards of the new banks and the resolution committees of the three old banks announced that an agreement had been made on the initial capitalization of the new banks and the basis for the compensation payable to the creditors of the old banks for the transfer of assets into the new banks.

The Government provided both the Resolution Committee of Glitnir and Kaupthing with options to acquire the majority of the Government's shares in the new banks. The announcement can be found [here](#).

On 15th of October the Resolution Committee of Glitnir, on behalf of its creditors, decided to utilize that option and acquired 95% of the share capital in Islandsbanki The Government will continue to own 5%. See [here](#).

Similarly, on December 1st ,the Resolution Committee of Kaupthing Bank decided to utilize the option to acquire 87% of common equity in Arion Bank. The Government will continue to own 13%. See [here](#).

On December 16th the Ministry of Finance and the Resolution Committee of Landsbanki Íslands hf announced that a final agreement had been reached on the settlement of assets and liabilities following the division of Landsbanki Íslands into old and new bank (NBI).

The government acquires 81% of the share capital in Landsbankinn (NBI hf, the new bank) and the Resolution Committee of Landsbanki, on behalf of creditors, will control 19% of NBI. The Icelandic Government's equity contribution will be ISK 122 billion, 5 billion lower than previously estimated. See [here](#).

More information and updates can be found [here](#).

8.1. OVERVIEW OF THE RESTRUCTURED BANKS

Following the restructuring of all three commercial banks the Ministry of Finance issued a press release outlining the contribution of the state in the bank restructuring. See [here](#).

The cost of capitalizing the new banks, ISK 135 billion, is significantly lower than the estimated commitment of ISK 385 billion at the time of the original transfer in October 2008. An overview of the state's contribution can be found below in table 1.

The agreement reached between the Icelandic authorities and the new banks, on the one hand, and the Resolution Committees of all three Banks on behalf of their creditor on the other hand concerns the settlement of assets which were transferred from the old banks to the new ones established in October 2008.

Table 1: Overview of the total contribution to the restructured banks

	Total equity	State's equity (ISKbn)	State's holding (%)	Subordinated loans from the state (ISKbn)	Total state financing
Arion banki	72	9,36	13	24	33,36
Íslandsbanki	65	3,25	5	25	28,25
Landsbankinn	150	122,00	81	0	122
Total	287	134,61	-	49	183,61

In January the FSA authorized Kaupskil ehf., on behalf of the creditors of Kaupthing, to acquire a qualifying holding in Arion Bank hf. Similarly the FSA authorized ISB Holding ehf. on behalf of the creditors of Glitnir, to own a qualifying holding in Íslandsbanki. See [here](#) and [here](#).

8.2. THE ICELANDIC BANKING AGENCY

The Government has furthermore set up a Banking Agency (The Icelandic State Banking Agency-ISBA) which is intended to control the state's holding in financial undertakings in compliance with currently applicable law, good administrative and business practices, and the state's current ownership strategy, and provide them with funding on behalf of the state based on budget allocations. See more on ISBA [here](#). Further information on the ownership policy can be found [here](#). Further updates can be found on the ISBA website, see [here](#).

ISBA is set up in accordance with an expert report from the Coordination Committee led by Mr. Mats Josefsson, see [here](#) for further information. The Committee had the overall responsibility of developing, implementing and communicating a comprehensive strategy for bank restructuring. Another expert report, by Mr. Kaarlo Jännäri, on Banking Regulation and Supervision in Iceland was published in March, see [here](#).

9. THE CAPITAL RESTRICTIONS AND FOREIGN EXCHANGE

The Central Bank did not see any reason to lift the capital restrictions in the first six months of 2009. The restrictions were put in place to prevent excessive short term volatility in the ISK. This was, among other things, due to the delay in receiving approval from IMF on the 1st review of the Economic Recovery Program, according to the Monetary Policy Committee, see [here](#).

On 5th of August the Central bank introduced a Capital Account Liberalization Strategy. The first step of the strategy was implemented on 1st of November allowing for foreign direct investments into Iceland. Liberalizing outflows will be initiated gradually at the Central Bank's discretion. No specific timeline has been set. See more information on the Liberalization strategy [here](#) and on the first step of the liberalization [here](#).

Surveillance on the foreign exchange rules has also been tightened. The Capital Controls Surveillance Unit within the Bank has been reorganized and fortified and the Central Bank's information gathering has been improved. In late October the rules on foreign exchange were tightened to hinder parties being able to exchange ISK abroad and import them at a more favorable exchange rate.

There has been a considerable difference between the off-shore and domestic exchange rate of the krona. Many have tried to gain from this arbitrage opportunity. The tighter regulation hinders bank deposits in ISK abroad being transported to an Icelandic bank. The ISK must be exchanged through the Central Bank. Consequently, the tighter regulation aided the MPC in lowering policy rates. See [chapter 12](#) on the decision and further information on the amended Act can be found [here](#).

Guidelines on foreign exchange can be found [here](#) and in [appendix 3](#). Information on the CB exchange rate can be found [here](#). Further information about the the off-shore exchange rate can be found [here](#).

10. THE ICESAVE DISPUTE

One part of the collapse of the Icelandic banking sector was the insolvency of Landsbanki in December 2008. A part of the bank was an online savings bank, called Icesave, operating in the United Kingdom (UK) and the Netherlands. See [appendix 7](#) for a timeline of the dispute and possible outcomes.

During the restructuring process of Iceland's financial system Landsbanki has been in moratorium and therefore creditors have not yet received reimbursements. Nevertheless, the governments of UK and the Netherlands reimbursed depositors of Icesave in their respective country. According to the European Economic Area legal framework the Depositors' and Investors' Guarantee Fund of Iceland is responsible for reimbursing the depositors up to certain amount, approximately 20.900 Euros. The reimbursement by the local governments (UK & Dutch) was therefore effectively a loan to the Depositors' and Investors' Guarantee Fund of Iceland. The Icesave dispute surrounds the terms of the loan and what conditions should apply to the state guarantee of the loan.

10.1. THE AUGUST ICESAVE ACT

On August 28th 2009 the Icelandic parliament passed an Act authorizing a state guarantee for the loans granted by the Governments of the UK and the Netherlands to the Depositors' and Investors' Guarantee Fund of Iceland. The law was signed with pre-conditions. The pre-conditions stipulated certain economic conditions for the repayments of the loans as well as legal rights regarding natural resources. A proposal of the preconditions can be found [here](#).

The president of Iceland signed the Act on 2 September 2009. His statement can be found [here](#).

10.2. THE DECEMBER ICESAVE ACT

In light of the pre-conditions the Icelandic Government had to re-negotiate with the Governments of the UK and the Netherlands. The re-negotiations process was concluded on 18th of October with the Governments of the UK and the Netherlands accepting some of the conditions set by the Parliament. Further information can be found [here](#).

Since the agreement was not identical to the law passed in August a new law needed to be ratified as a successor to the earlier law. Many Icelanders felt that the key pre-conditions set forward in the Act that was passed in August had been removed and put tremendous pressure on the Icelandic parliament not to pass the bill. After several weeks of discussions in the Icelandic Parliament a new law was passed on December 30th 2009 with a majority of 33 votes against 30. Further information can be found [here](#).

10.3. THE ACT WAS NOT CONFIRMED BY THE PRESIDENT

According to the Icelandic constitution the president needs to sign every law that is passed. If the president does not sign a law it must go under a national referendum as soon as possible. The president does not have the power to veto or block the law from going into force.

Over 60 thousand Icelanders, about a quarter of the electorate, signed a petition urging the president of Iceland not to sign the law that was passed on December 30th and calling for the Act to be subjected to a referendum. Further information can be found [here](#) (site only available in Icelandic).

On January 5th 2010 the President of Iceland declined to sign the law passed on December 30th. According to the constitution the law remains in force but is put under a national referendum as soon as possible. The Minister of Justice, Ms. Ragna Arnadóttir, has set the date for the referendum which is to be held on 6th March. Further information on the president's decision can be found [here](#), and on the national referendum can be found [here](#).

10.4. WHAT WILL FOLLOW?

If the Act is approved in the referendum then naturally, it will remain in force. If the law is not passed in a referendum, the Act passed on August 28th will continue to be in force, recognizing that the e of Iceland acknowledge their obligations to the Governments of the UK and the Netherlands. The third potential outcome would be that the Government withdraws the law before the referendum. The old law from August would then be automatically re-instated.

Considering the fact that the Governments of the UK and the Netherlands did not accept the previous law with the pre-conditions, re-negotiations would most likely take place if the current Act will not be passed in a referendum. The Government and the opposition have appointed a negotiation committee to discuss the possibility of settling the issue before the referendum date.

In summary, the short term effects due to the decision of the president not to confirm the law are minimal. However, the uncertainty regarding the economic restructuring program in Iceland is unfortunate and hopefully this issue will be resolved successfully for all parties in near future.

In a press release regarding the matter the Government of Iceland emphasized that it remains fully committed to implementing the bilateral loan agreements with the UK and the Netherlands and thus the state guarantee provided for by the law. The Government views the loan agreements with the UK and the Netherlands as an integral part of Iceland's economic program. The Government economic recovery plan developed in cooperation with and supported by the International Monetary Fund and with financing from the IMF and governments of the Nordic countries and Poland, remains in effect. The press release can be found [here](#).

The Icelandic Minister of Finance conferred with his Nordic counterparts explaining the situation that arose following the denial of the President. The parties discussed the impact and repercussions this could have on the continuation of disbursements and the implementation of the loan agreements which are in place between Iceland and the Nordic countries, which are a key factor in Iceland's economic recovery program agreed with the IMF. See [here](#).

For information on the impact of the decision on Iceland's EU application see [chapter 13](#).

The prime minister of Iceland wrote an article in the UK Observer explaining the commitment of the Icelandic government to honoring its obligations which can be found [here](#). Another interview with the PM following the decision can be found [here](#).

The Ministry of foreign Affairs has published background information and some basic facts about the Icesave debate. See [here](#) and [here](#).

10.4. IMPACT ON CREDIT RATING

Following the decision of the president the credit rating of Iceland was lowered by Fitch ratings to BB+/BBB+; with a negative outlook. The lower credit rating does however not impact the ability or the cost of borrowing for Icelandic authorities since it is funded by the IMF and other loans from Nordic countries.

Therefore the ratings have minimal effect on the cost of funding for the Icelandic Authorities. However, the decision could have some impact on Icelandic firms, in the short run, if the uncertainty surrounding the issue is not resolved.

The president was interviewed by Bloomberg business news network on January 7th 2010 where he explains the implications of his decision and his view on the impact on the credit rating of Iceland. See [here](#) (subscription required).

Other rating agencies have put Iceland on a watch list with negative outlook. Like was mentioned before this has little practical significance for Iceland since it is funded by the IMF program and political lending from Nordic nations. Standard & Poor's placed Iceland on a watch list after the decision not to sign. See further information [here](#).

The Japanese rating agency R&I confirmed the BBB- credit rating of Iceland with a view to downgrade. See further information [here](#).

11. THE IMF PROGRAM

The 1st review of the Economic Recovery Program, which was scheduled to be concluded in May/June, was substantially delayed because of the Parliamentary debate over the Icesave Act. See [here](#).

On 28th of October 2009 the IMF's Executive Board approved the 1st review of the Economic Recovery Program, giving Iceland access to \$167,4 million from the IMF and also to \$675 million from the Nordic countries and Poland, see here. The Governments statement regarding the approval and the Letter of Intent can be found [here](#). In connection with the 1st review of the IMF program a staff report was published. See [here](#).

As a part of the 1st review of the IMF program the first tranche of Nordic loans was disbursed to Iceland on December 21st 2009. The first tranche amounted to 300 million euro's. See [here](#).

Representatives from the IMF visited Iceland from December 1-14th to undertake discussions for the 2nd review under the IMF program. In a statement following the visit the IMF anticipated that by January all policy actions for the 2nd review would be in place provided that financing assurances could be secured from Iceland's Nordic counterparts. See [here](#).

However, some uncertainty remains whether financing from the Nordic counterparts will be available until after the referendum on the Icesave Act. Hence, a delay of the 2nd review is probable until after the referendum. Icelandic authorities have been deliberating with their Nordic counterparts on the issue in an effort to resolve some of the uncertainty which had arisen. See [here](#).

The Prime Minister of Iceland urged the IMF to continue the Economic Program in a recent press release regardless of the planned national referendum on the Icesave Act. See [here](#) and [here](#).

Mr. Strauss-Kahn, Managing director of the IMF, recently answered a couple of questions on Iceland and the delay of the 2nd review. See [here](#).

12. MONETARY POLICY - GRADUAL EASING

The MPC of the Central Bank kept the collateral loan and deposit rates constant, at 12% and 9,5%, from June until November. Since then the MPC has lowered both the deposit and loan rates on two occasions, first on November 5th to 11% and 9% and then on December 10th to 10% and 8.5%. For more information on the November decision see [here](#) and [here](#). For more information on the December decision see [here](#) and [here](#).

Inflation has not come down as fast as expected due in part by the weakness of the exchange rate in the first half of 2009. Albeit, inflation being 18.6% at the beginning of 2009 and 7.5% at the end of the year. Inflation is expected to come down further in the coming months even though tax increases at the turn of the year might raise inflation in the first couple of months of 2010. The exchange rate is assumed to remain stable in 2010, and inflation to average 5.0 per cent for the year but approach 2.5 per cent by year end. For 2011, a 2.3 per cent inflation rate is forecasted. See also [chapter 14](#) on fiscal policy.

The decisions in late 2009 represent a gradual monetary easing process by the MPC. In the statement issued by the committee explaining the reasoning behind the December decision it is noted that the intervention in the foreign exchange intervention has been limited. Tighter regulation, enhanced surveillance, and more effective enforcement have made circumvention of the capital controls more difficult. Provided that the króna remains stable or appreciates and inflation continues to fall as forecasted the MPC expects that conditions for further easing of monetary policy should soon be in place.

There have also been other signs of improvement, e.g. lesser need for foreign exchange intervention by the Central Bank due to the ISK being broadly stable and the trade surplus is estimated to be ISK 72 billion in 2009. In comparison compared to an ISK 6 billion deficit in 2008 and ISK 92 billion in 2007. Unemployment is forecast to average 8.6% in 2009 and reach 10.6% in 2010, but decline in 2011 to 9 %.

Some uncertainty regarding further monetary easing arose after the President declined to sign the Icesacve Act and put the Act under a national referendum. However, the governor of the Central bank, Mar Gudmundsson, stated in an interview on Bloomberg that there is still room for monetary easing despite the uncertainty following the decision. See [here](#). See also [chapter 10](#) on the Icesave dispute.

Information on Iceland's CDS spread can be found [here](#). The Central Bank of Iceland's report Financial Stability 2009 can be found [here](#).

More information on the monetary policy of the central bank and their current stance can be found in the Monetary Bulletin Published in November 2009. See [here](#).

A report on the work of the Monetary Policy Committee was published in December 2009. See [here](#).

13. THE EUROPEAN UNION: APPLICATION IN PROCESS

The Parliament voted on 16th of July 2009 in favor of applying for membership to the European Union (EU). Proposals from the Parliament's Foreign Affairs Committee regarding the application can be found [here](#).

Iceland's application was submitted to the Swedish Government, which holds the EU presidency, on 17th July and on 27th of July the Foreign Ministers of the EU invited the Commission to formulate an opinion on Iceland's application. A copy of the application can be found [here](#). The Commission questionnaire was formally presented to the Icelandic Prime Minister Ms. Johanna Sigurdardóttir by Mr. Olli Rehn, the European Commissioner for Enlargement on 8th of September and the answers were submitted on 22th of October. See the questionnaire and the answers [here](#).

The Minister for Foreign Affairs, Mr. Ossur Skarphedinsson, appointed Ambassador Mr. Stefan Haukur Johannesson on November 2nd to serve as Iceland's Chief negotiator in the upcoming accession negotiations with the European Union. Mr. Johannesson is an experienced international negotiator which has served as Iceland's Ambassador to the European Union in Brussels since 2005. See [here](#).

More information on Mr. Johannesson and other members of the negotiation committee can be found [here](#). An interview with Mr. Johannesson can be found [here](#).

In November an agreement was signed on the establishment of a European Commission Delegation in Iceland. Information regarding new developments concerning Iceland can be found in the press corner of the European Commission Enlargement webpage. See [here](#).

In January 2010 the Foreign Minister of Iceland met with Mr. Miguel Ángel Moratinos, who holds the Presidency of the European Union, regarding the impact of the Icesave debate on Iceland's application. Mr. Moratinos stated that the Spanish EU Presidency viewed the Icesave issue and Iceland's EU application as separate issues, and that the new situation that has arisen in Iceland would not have any impact on EU's treatment of the application. See [here](#).

According to Mr. Audunn Atlason, Director of the Communications and Public Diplomacy department of the Ministry of Foreign Affairs, the EU Commission aims at finishing its opinion on Iceland's application before the March meeting of the European Council. At its meeting the Council will decide on whether Iceland will be given a formal candidate status which is a precondition for the opening of accession negotiations.

13.1. FURTHER INFORMATION ON ICELANDS' EU APPLICATION

The Ministry of Foreign Affairs has dedicated a section on their website to Iceland's EU application process where up to date information and a timeline of events can be found. See [here](#) and [here](#).

Iceland's historic relations with the EU can be found [here](#).

Information on the Enlargement Strategy and Main Challenges of the EU for 2009-2010 can be found [here](#).

Iceland's country profile at the European Commission can be found [here](#).

14. THE STATE TREASURY: HIT HARD IN THE TURMOIL

The aftermaths of the financial crisis has hit the State Treasury and municipalities significantly, both in terms of revenue and expenditure: The Ministry of Finance published a Macroeconomic forecast for 2009-2014 this fall. A few highlights of the report are listed below. The report in its entirety can be found [here](#).

Net Government (and Central Bank) debt has increased as a direct result of the failure of the banks by around 13% of GDP. Most of this figure reflects funds advanced to the banks by the CBI and, to a much lesser extent, the Treasury. In addition, the Government will incur debt to meet minimum EU deposit guarantee requirements on Landsbanki's Icesave accounts in the United Kingdom and the Netherlands. Assuming a 75% recovery ratio, (the Resolution Committee is expecting 90% recovery) the CBI estimates that the present value of the cost to the Icelandic Government of meeting this obligation is ISK 240 billion (17% of estimated GDP in 2009).

Treasury revenues contracted significantly towards the end of 2008 and in 2009 with most of the tax bases shrinking with increased bankruptcies in the private sector, especially company and capital taxes. Due to reduced private consumption revenues from VAT and excises taxes have also contracted. There has been a major overhaul, and controversial, of the tax system in Iceland which was geared towards generating more revenue and closing the fiscal deficit.

The 2010 budget is based on the premises set out in, and aimed at achieving the objectives of, the report on Government plans for fiscal balance in 2009-2013 which is based on the IMF Economic Recovery Program. The Budget Highlights for 2010 from the Ministry of Finance can be found [here](#) and the Treasury finances for January-November 2009 can be found [here](#).

The nation's gross foreign debt is predicted to be about 320% of GDP at the end of 2010. However, out of that about 260% is private debt which the state is not responsible for. The foreign debt of the state and municipalities, which is about 60% of GDP, will decrease in the coming years and this will prove to be decisive.

The growth in public debt has slowed. A year ago the deficit was ISK 218 billion ISK but the 2010 budget estimates it at ISK 99 billion. The budget approved by Althingi is in line with the government's plan to return to surplus in 2013. At that point repayment of public debt will commence.

Treasury cyclical expenditures have increased with the sharp increase in unemployment which has put the unemployment benefit scheme under considerable pressure. The revenue balance amounted to 13% of GDP that year. In 2009, the deficit is estimated to reach 17.2% of GDP. The Government took various measures over its summer session to dampen the hit and it has also put forth legislation on the national budget for the year 2010 with further measures. The economic plan assumes considerable fiscal consolidation in coming years to bring about a surplus and debt reduction.

Policy actions

The Government has put forward a series of policy actions initiative in response to the crisis. Some highlights of policy initiatives are listed below:

- » Personal income tax rates were increased by 1.25% and a temporary 8% surcharge was introduced on high incomes at the beginning of 2009. A new three bracket progressive tax system put in place for 2010.
- » Various benefits were decreased, such as maternity/paternity leave benefits, and income thresholds for others were lowered.
- » Social security contribution, paid by Icelandic companies, was increased to a level that is expected to balance the unemployment fund's accounts.
- » Government expenditure measures of restriction around 1.5% for the Ministries and their institution were introduced in June. The Icelandic National Audit Office issued a statement that this goal was not achieved.
- » The national budget for 2010 entails increased taxes, e.g. new energy, environmental and resource taxes, increased capital and income taxes, as well as changes to commodity taxes and a expansion of the VAT base and reclassification of VAT levels.
- » The national budget also entails expenditure measures of restriction around 10% in the Government's administration, 7% in educational matters and 5% in welfare matters. Public investments will be reduced and further decreases in benefits, such as child support benefits, have been introduced.
- » Various initiatives to guarantee partial payment relief for households have been adopted
- » Major debt restructuring is ongoing for individuals and firms. Freezing of auctions has also been in place for several months. Despite the efforts it is still estimated that around 12% of households are facing serious debt problems.

A general overview of the economic recovery can be found [here](#) and [here](#).

An article from the Prime Minister stating some fiscal policy initiatives can be found [here](#).

The new macroeconomic forecast from the Ministry of Finance can be found [here](#) and the forecast for 2009-2014 can be found [here](#).

15. THE STOCK MARKET: SLOWLY PICKING UP PACE

Before the financial crisis hit Iceland seriously, market cap on the equity market amounted to around 120% of GDP. This number has now been brought down to around 20% of GDP after the collapse of the three biggest banks, Glitnir, Landsbanki and Kaupthing. After trading was suspended for three trading days in the second week of October 2008 the OMX Iceland 15 index closed at 678.4, which corresponds to a plunge of about 77% compared with 3,004.6 closing on October 8th, 2008. This reflects the fact that the value of the three big banks, which formed 73.2% of the value of the OMX Iceland 15, had been set to zero.

On 2nd of January 2009 the OMX Iceland 15 index was replaced with a new index, the OMXI6. The new index comprised of 6 companies instead of 15, which have the most trading volume of the listed companies and which are mostly industry based. The index combination will be revised 1st of January and 1st of July each year.

Despite the heavy blow the NasdaqOMX Iceland Stock Exchange is on a good recovering phase. The OMXI6 index has risen by nearly 45% from Spring 2009 until January 2010 and trading volume of bonds has already transcended its yearly record of ISK 21 billion. More information on the NasdaqOMX Iceland Stock Exchange can be found [here](#). Information on the bond market can be found [here](#).

16. THE LABOR MARKET STABILITY PACT WAS EXTENDED

Near the end of June 2009 the Government, both central and local, and the Confederation of Employers and the Confederation of Employees signed an agreement, The Stability Pact. The Pact's aim is to secure broad social consensus for adjustment measures necessary to ensure economic recovery. Its aim is also to "create conditions for increased investment by both domestic and foreign parties, stronger growth, boosting employment and laying the foundation for improved living standards in the future."

The objective of the agreement was to deter a rise in inflation due to the interdependence of wage increases and inflation, i.e. hindering that a rise in wages due to collective wage agreements would lead to a rise in inflation. Additionally, the agreement was signed in an effort to secure stability in the labor market and create a foundation for further growth.

The Pact stipulates e.g. that collective wage agreements shall remain valid until the end of November 2010; that the balance in the national budget shall be attained with a suitable mix of cuts in expenditure and higher taxes; that the Government shall pave the way for major investment projects and seek co-operation with Icelandic pension funds to finance infrastructure projects. It also stipulated some monetary and economic conditions. For further information see [here](#) and [here](#).

16.1. THE STABILITY PACT RENEWED

In the Stability Pact certain economic and monetary objectives needed to be met before November 1st 2009. Since it was foreseen that some conditions, e.g. monetary condition, would not be met the Government and the Confederation of Employers and the Confederation of Employees signed an extension to the agreement on 28th October 2009 that secures the Pact will be in force until the end of November 2010. In the agreement modest wage increases were implemented from November 1st 2009 but a considerable part of previously agreed wage increases were postponed until 1st July 2010.

17. ICELAND'S FUTURE IS BRIGHT

Despite the current economic setbacks, Iceland's future is bright. Iceland is a dynamic, technology-driven society with a young and well educated workforce. The country is endowed with abundant natural resources, which include rich fishing grounds, vast renewable energy sources (of which only a third has been harnessed), a plentiful supply of clean water and a natural environment and culture that draw an increasing number of tourists to the country each year.

Other major strengths of the economy include diverse export industries, a flexible labor market, a strong fiscal position, an efficient pension system and an excellent education system.

Armed with these strengths, Iceland's future is bright and prosperous

Appendix 1: Timeline of the Icelandic Financial Crisis

September 29	Government announces takeover of 75% share in Glitnir and EUR 600 m equity injection. S&P downgrades Glitnir to BBB; Sovereign to A-.
September 30	Fitch downgrades sovereign to A-; Landsbanki to BBB;Kaupthing to BBB;Glitnir to BBB. Moody's downgrades sovereign to Aa1;Landsbanki to A2;Kaupthing to A1;Glitnir to Baa2.
October 4-5	Government evaluates crisis in an attempt to save banking sector.
October 6	Emergency law is introduced and passed by parliament; government guarantees all domestic deposits. Icelandic FSA seizes control of Landsbanki under terms of emergency law. S&P downgrades sovereign to BBB.
October 7	Assets of Landsbanki seized by UK authorities;Landsbanki Luxembourg goes into administration. FSA seizes control of Glitnir under terms of emergency law. Central Bank extends EUR 500 m loan to Kaupthing; announces intentions to negotiate EUR 4 bn loan with Russian Government. Central Bank announces exchange rate peg and starts by selling EUR 6 m. at ISKEUR 131. Fitch downgrades sovereign to BBB-;Landsbanki to B;Glitnir to B. S&P downgrades Glitnir to CCC.
October 8	Central Bank announces intention to maintain currency peg; later announces that peg is not sustainable and has been abandoned. Swedish Central Bank extends SEK 5 bn loan to Kaupthing Sweden. British authorities put Kaupthing Edge and Kaupthing Singer & Friedlander into administration. British PM threatens to sue Icelandic Government to claim guarantee for Icesave deposits. Icelandic PM states that sale of Landsbanki assets will be used to refund Icesave depositors. Fitch downgrades sovereign to BBB-;Landsbanki to D;Kaupthing to CCC;Glitnir to D. Moody's downgrades sovereign to A1 and puts on review for further downgrade;Kaupthing to Baa3;Glitnir to Caa2. Board of Kaupthing requests FSA to assume control of bank.
October 9	New Landsbanki starts operations. Dutch finance minister threatens to sue Icelandic Government over Icesave deposit guarantee; British PM reiterates threats. Fitch downgrades Kaupthing to CC Moody's downgrades Kaupthing to Caa2. S&P downgrades Glitnir to D.
October 10	Dutch delegation arrives in Reykjavik; initiates talks with treasury department about Icesave Central Bank announces limits on currency outflow; low amounts for travel and import restricted to necessities, companies must apply for currency to the CB.
October 11	British delegation initiates talks with treasury department about Icesave deposits. Accord signed with Dutch Government on loan to guarantee a refund of Icesave deposits. Outlines of an accord with British Government on loan to guarantee refund of Icesave deposits.

October 14	Central Bank delegation starts talks in Moscow with Russian Finance Ministry on loan to Iceland. Central Bank draws on swap facility arrangements with Denmark and Norway, each by EUR 200 m. Moody's confirms sovereign credit rating issued on October 8 (A1).
October 15	Central Bank lowers policy rate by 350 bp to 12%. Central Bank introduces auction system to meet demand for foreign currency, resulting in an allocation of EUR 25m. at a ISKEUR rate of 150. Fitch issues credit update for sovereign debt holding rating steady at BBB- on negative watch. Iceland and Russia agree to continue discussions on a possible loan. New Glitnir starts operations.
October 16	Central Bank announces that it guarantees that all payments will reach ultimate beneficiaries' accounts with local banks in an attempt to revitalize payment system.
October 22	New Kaupthing starts operations. Norwegian delegation arrives in Iceland to gather information about the the situation.
October 24	Government announces an agreement ad referendum with an IMF mission of USD 2 bn stand-by-facility programme. Government formally requests assistance from the Nordic countries, the ECB and the FED. Delegation from the US Treasury Department arrives in Reykjavik.
October 27	High-level Nordic committee established to present proposals for Nordic assistance to Iceland in cooperation with the IMF.
October 28	Central Bank raises policy rate by 600 bp to 18%. Faroe Islands pledge DKK 300 million loan for Iceland.
November 19	The Icelandic Government enters into a program with the IMF which approves a two-year SDR 1.4 billion (about US\$2.1 billion) Stand-By Arrangement to support the country's program to restore confidence and stabilize the economy.
November 28	New foreign exchange regulation is implemented

2009

January 1	OMX Iceland 15 index replaced with a new index, the OMXI6.
January 2	Mr. Geir H. Haarde, Prime minister at the time, announces that national elections will be held in May 2009. Coalition government of the Independence Party and the Social Democratic Alliance comes to an end. New government is formed - a coalition of the Social Democratic Alliance and the Left-Green Movement. The coalition does not have parliamentary majority but receives a neutrality support by the Progressive Party. Election date set for April 25th 2009.
February	Parliament passes new act on Central Bank, subsequently Mr. Svein Harald Øygard is appointed interim Governor of the bank and Mr. Arnór Sighvatsson is appointed interim Duputy Governor.
April 4	Parliament approved amendments to the Act on Foreign currency
April 24	National elections for Parliament, in the elections the Social Democrats and Left-Greens get majority of seats in the Parliament. Coalition Government of the two parties continued, now with parliamentary majority.
June	Local and central governments, Confederation of Employers and Confederation of Employees sign The Stability Pact
June 26	Prime minister appoints Mr. Már Guðmundsson as new Governor of Central Bank, for a five year term, and Mr. Arnór Sighvatsson as Deputy Governor, for a four year term.
July 16	Parliament votes in favor of applying for membership to the EU.
July 17	Iceland's application for the EU submitted to the Swedish Government, which holds EU presidency.

July 20	Agreement announced on the initial capitalization of the new banks.
August 2	Laws passed on the Icelandic Banking Agency
August 5	Central bank introduces Capital Account Liberalization Strategy – First step implemented November 1st.
August 28	IceSave - Parliament passes an Act authorizing a state guarantee for the loans granted by the Government of the UK and the Netherlands to the Depositors' and Investors' Guarantee Fund of Iceland
September 2	IceSave – President of Iceland signs IceSave act with a special reference to preconditions set by the Parliament.
October	Rules on foreign exchange tightened to hinder parties being able to exchange ISK abroad and import them at a more favorable exchange rate.
October 15	Resolution Committee of Glitnir acquires 95% of the share capital in Islandsbanki against 5% held by the Government
October 18	IceSave – Re-negotiations concluded with Governments of the UK and Netherlands
October 22	Answers to EU Commission questionnaire formally presented to Olli Rehn, the EU Commissioner for Enlargement
October 28	IMF's Executive Board approves first review of the Economic Recovery Program for Iceland. Local and central governments, Confederation of Employers and Confederation of Employees sign an extension to The Stability Pact.
November 2	Minister of Foreign Affairs, Mr. Ossur Skarphedinsson, appoints Ambassador Mr. Stefan Haukur Johannesson to serve as Iceland's Chief negotiator in EU negotiations
November 5	Monetary Policy Committee (MPC) lowers the deposit and loan rates to 11% and 9%.
December	Representatives from the IMF visit Iceland to undertake discussions for second review
December 1	Resolution Committee of Kaupthing acquires 87% of common equity in Arion Bank against 13% held by the Government
December 10	Monetary Policy Committee (MPC) lowers both the deposit and loan rates to 10% and 8.5%.
December 16	Final agreement announced between Ministry of Finance and the Resolution Committee of Landsbanki Íslands hf. The government acquires 81% of the share capital in Landsbanki (NBI hf.) against 19% held by the Resolution Committee of Landsbanki Íslands hf.
December 30	IceSave – New law passed in the Parliament on conditions of the October re-negotiations
2010	
January	FSA authorizes ISB holding ehf on behalf of creditors of Glitnir to own a qualifying holding in Íslandsbanki. Similarly the FSA authorizes Kaupskil ehf. on behalf of creditors of Kaupthing to acquire a qualifying holding in Arion Bank.
January 5	IceSave - President of Iceland, Ólafur Ragnar Grímsson, declines to sign law passed on December 30th. Law will be put under national referendum as soon as possible.
January 19	Minister of Justice, Ragna Árnadóttir, sets a date on national referendum. The referendum is set for March 6 2009.
March 6	Scheduled date for the referendum on the Icesave Act

Appendix 2: More on the new Bank Act

As previously mentioned the Icelandic parliament passed on October 6th a new law, allowing the Financial Supervisory Authority (FSA) to take over the operations of the banks in unusual and extraordinary circumstances in order to limit damage or the risk of damage in the financial markets.

These unusual and extraordinary circumstances are stipulated further in art. 1 ph. 2. This list of circumstances is however not exhaustive; the FSA can thus, in other circumstances, apply its authority given by the law as long as the board of the FSA approves. The Central bank, which monitors liquidity status of financial institutions, appoints one member to the FSA board. The Central bank therefore has first hand information about the status of financial institutions and probable FSA actions in that regard.

The FSA has, on basis of this new law, taken over Iceland's three biggest banks and the procedure has been as follows:

1. The boards were dismissed.
2. Special Resolution Committees were appointed to take over board activities and management.
3. New companies were founded around the old banks domestic operations.
4. The FSA decides on disposal of assets and liabilities of the old banks to the new companies.
5. The Government, the Resolution Committees and the new banks came to an agreement on capitalization of the new banks and compensation to creditors of the old banks.
6. The Resolution Committee of Glitnir, on behalf of its creditors, decided to acquire 95% of the new bank, Islandsbanki.
7. The Resolution Committee of Kaupthing, on behalf of its creditors, has a deadline until 31st October to decide on acquisition of the new bank, New Kaupthing.
8. NBI bank, built on the domestic operations of Landsbankinn, will be owned by the Government.

Appendix 3: Q&A about Foreign Exchange Matters

The Central Bank of Iceland has published questions and answers about the recent changes in the Foreign Exchange Act of 1992 and the Bank's new Rules on Foreign Exchange, see [here](#).

Appendix 4: The New Act on the Central Bank

Act no. 5/2009 amending the Act on the Central Bank of Iceland, no. 36/2001, was passed by Parliament in late February. The new Act provides for one Governor and one Deputy Governor within the Central Bank instead of a Board of Governors. Decisions on applying the Central Bank's monetary policy instruments will henceforth be taken by a Monetary Policy Committee. In other respects, the Bank's direction will be in the hands of the Governor.

According to the new law, the Board of Governors of the Central Bank of Iceland has been abolished, together with the positions of the three Governors who sat on the Board, including the position of Chairman of the Board of Governors.

Pursuant to the new law, the Prime Minister appointed Mr. Svein Harald Øygard to act as interim Governor and Mr. Arnór Sighvatsson, the Bank's Chief Economist, to act as interim Deputy Governor. Information on Svein Harald Øygard can be found [here](#). The interim Governor and Deputy Governor held these positions until appointments were made by the Prime Minister on the basis of advertisements, in accordance with the provisions of the Act.

On 26th of June the Prime Minister appointed Mr. Már Guðmundsson as the new Governor of the Central Bank, for a term of five years, and Mr. Arnór Sighvatsson as Deputy Governor, for a term of four years. The Governor appointed on 15th of September Mr. Þórarinn G. Pétursson as the Chief Economist of the Central Bank. Information about the Central Bank's new Governors' and new Chief Economist can be found [here](#) and [here](#).

Appendix 5: The IMF Loan Package

On November 19th the IMF approved Iceland's request for a two year stand-by arrangement. Iceland will receive USD 2.1 billion from the IMF. Additional loans of up to USD 3 billion have been secured from Denmark, Finland, Norway, Sweden, and Poland. These loans are based on Iceland's agreement with IMF. The Faroe Islands have announced that they would lend Iceland USD 50 million.

The loans main purpose is to buttress Iceland's liquid foreign exchange reserves, and by doing so increasing the economy's credibility and its capabilities to address potential capital outflow, and protect the ISK, once the currency restrictions are lifted. The loans will up to some extent also be used by the Government to pay loans maturing in the near future.

a) The IMF Loan

On 19th of November the Executive Board of the IMF approved a two-year SDR 1.4 billion (about USD 2.1 billion) Stand-By Arrangement for Iceland.

The approval made SDR 560 million (about USD 827 million) immediately available and the remainder is available in eight equal installments of SDR 105 million (about USD 155 million), subject to quarterly reviews. Iceland has already drawn the initial USD 827 million and is now able to draw the first of eight installments as the 1st Review of the IMF Economic Program has been approved by IMF's Executive Board.

Further information on the IMF loan can be found [here](#), [here](#) and [here](#). Further information on the IMF program can be found [here](#).

b) The Nordic Loans

In July 2009 the Nordic countries agreed to loan Iceland in total of EUR 1.775 billion, which is equivalent to USD 2.5 billion or ISK 317 billion. The loan agreements with Denmark, Finland, and Sweden are between the Icelandic Government and the governments concerned, while the agreement with Norway is between the two countries' central banks. The loans will be disbursed in four equal tranches tied to the IMF's reviews of the Icelandic economic program.

The loans will be disbursed in Euros with an overall maturity of 12 years, with installment payments of principal deferred for the first five years during which time interest will be paid quarterly. At the end of the five-year period, the principal amount will be repaid in equal quarterly installments for the remainder of the loan period. The loans will bear variable (floating) interest based on three-month EURIBOR rates, plus a 2.75% premium. Further information on the Nordic loans can be found [here](#).

As a part of the 1st review of the IMF program the first tranche of Nordic loans was disbursed to Iceland on December 21st 2009. The first tranche amounted to 300 million euro's. See [here](#).

c) The Polish Loan

In October 2009 The Republic of Poland agreed to lend Iceland PLN 630 million, the approximate equivalent of USD 200 million. The loan's overall maturity of 12 years, with a grace period of five years. The loan will be disbursed in three equal tranches tied to the second, third and fourth reviews of Iceland's IMF program, with the payment of each tranche conditional on the approval of the respective review.

The loan will be denominated and disbursed in Polish z³oty (PLN). The net cost to the borrower will consist only of an interest margin to be paid simultaneously with interest payments on the Polish Treasury Bonds issued by the Polish Treasury. This interest margin will be 2% per annum until 31 December 2015 and 1.3% per annum thereafter. The loan will be repaid in four installments coinciding with the maturity dates of the selected Polish Treasury Bonds, in October 2015, 2017 and 2019, and in September 2022.

Further information on the Polish loan can be found [here](#).

d) The Faroe Islands' Loan

A loan agreement was signed between the Government of the Faroe Islands and Iceland in March 2009. Under the agreement, the Government of the Faroe Islands will lend the Republic of Iceland DKK 300 million. The loan was the first bilateral loan of this type extended to Iceland, and it is not based upon the IMF economic program.

Further information on the Faroe Islands' loan can be found [here](#).

e) The Russian Loan

The Russian Government indicated in November 2008 its willingness to lend up to 500 million dollars. The loan agreement negotiations have come to a halt.

Appendix 6: Macroeconomic Forecasts

For further information on macroeconomic forecasts, please review:

- » Central Bank of Iceland, [Monetary Bulletin](#), Issued four times per year.
- » OECD [Economic Outlook](#), November 2008.
- » OECD [Economic Survey](#), September 2009.
- » Ministry of Finance updated [macroeconomic forecast](#) for 2009.
- » Ministry of Finance [macroeconomic forecast](#) for 2009-2014.
- » On overview of [economic indicators](#) in Iceland.
- » Report on [financial stability](#) published in October 2009.

For information on the IMF stabilization program and the progress being made, please refer to the [IMF's website](#) and for the most recent publications on Iceland from the IMF please refer to the section on [Iceland](#).

Appendix 7: Further Information

For further information on this Status Report contact:

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For further information on the Iceland Chamber of Commerce visit www.vi.is/english

For further information on reports issued by the Central bank contact:

- » sedlabanki@sedlabanki.is or +354-569-9600

For further information on the Resolution Committees and the disposal of assets and liabilities between the old and new banks contact the FSA:

- » fme@fme.is or +354-525-2700