

CENTRAL BANK OF ICELAND



2021

# ANNUAL REPORT

- Symbols:**
- \* Preliminary or estimated data.
  - 0 Less than half of the unit used.
  - Nil.
  - ... Not available.
  - . Not applicable.

**Icelandic letters:**

ð/Ð (pronounced like th in English this)

þ/Þ (pronounced like th in English think)

In this report, ð is transliterated as d and þ as th in personal names, for consistency with international references, but otherwise the Icelandic letters are retained.

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# Objectives, policies, and execution



The Central Bank of Iceland is an independent institution owned by the State and operating under the auspices of the Prime Minister. Furthermore, the Ministry of Finance and Economic Affairs administers matters relating to financial stability and financial markets. The Act on the Central Bank of Iceland, no. 92/2019, stipulates that the Bank shall promote price stability, financial stability, and sound and secure financial activities. The Bank shall also undertake such tasks as are consistent with its role as a central bank, such as maintaining international reserves and promoting a safe, effective financial system, including domestic and cross-border payment intermediation. Since the beginning of 2020, when the Bank and the Financial Supervisory Authority merged, the Central Bank administers all functions previously entrusted to the Financial Supervisory Authority by law and Governmental directive.

The Bank is also required under the Act to promote the implementation of the Government's economic policy as long as it does not consider such policy inconsistent with the Bank's objectives.

The Monetary Policy Committee, Financial Stability Committee, and Financial Supervision Committee, operate in accordance with the provisions of the Central Bank Act, each of them taking strategic decisions and other legally mandated decisions in its own field. The three committees have adopted rules of procedure that are published on the Bank's website.

The Governor directs and is responsible for the Bank's activities and operations and is authorised to take decisions on all matters not entrusted to others by law. The Governor is responsible for the execution of decisions taken by the Bank's committees.

## Price stability

With the approval of the Minister, the Central Bank may declare a quantitative target for inflation. According to the joint declaration issued by the Government of Iceland and the Central Bank of Iceland on 27 March 2001, the Bank shall aim at a rate of inflation, measured as the twelve-month increase in the consumer price index (CPI), of about 2½%.<sup>1</sup> The Act on the Central Bank of Iceland grants the Bank full independence in applying its monetary policy instruments so as to achieve the price stability objective.

The Central Bank's monetary policy instruments are its interest rates, facilities for credit institutions (apart from loans of last resort), minimum reserve requirements, foreign exchange market transactions, and securities transactions.

A five-member Monetary Policy Committee (MPC) takes strategic decisions on the application of the Bank's monetary policy instruments, with the aim of achieving the price stability objective. Members of the Committee are the Governor (who acts as chair), the Deputy Governor for Monetary Policy, the Deputy Governor for Financial Stability, and two outside experts appointed by the Prime Minister.

The MPC meets at least six times a year and issues a statement on its decisions following each meeting. The minutes of its meetings are published two weeks after each meeting.

<sup>1</sup> The declaration was published in *Monetary Bulletin* 2001/2 and on the Bank's website. Minor changes were made to it in November 2005.

## Financial stability

The Financial Stability Committee (FSN) assesses the current situation and outlook for the financial system, systemic risk, and financial stability. It discusses and defines the actions deemed necessary at any given time in order to affect the financial system so as to strengthen and preserve financial stability, and make comments to the appropriate authorities when warranted. It is also entrusted with deciding which supervised entities, infrastructure elements, and markets shall be considered systemically important and of such a nature that their activities could affect financial stability.

The seven-member FSN takes decisions on the application of the Central Bank's financial stability policy instruments. Members of the Committee are the Governor (who acts as chair), the Bank's three deputy governors, and three outside experts appointed by the Minister of Finance and Economic Affairs. The Permanent Secretary or an appointed official from the Ministry responsible for financial stability shall also participate in Committee meetings as a non-voting member with the right to address the meeting and present proposals.

The FSN meets at least four times a year and issues a statement on its decisions following each meeting. The minutes of its meetings are published within a month after each meeting.

## Sound and secure financial activities

The purpose of financial supervision is to ensure that the activities of supervised entities comply with the laws, regulations, rules, and articles of association governing these activities at any given time.

The Financial Supervision Committee (FMEN) takes decisions previously entrusted to the Financial Supervisory Authority by law and Governmental directive. The Committee is authorised to entrust the Deputy Governor for Financial Supervision with taking non-major decisions. As is provided for in the Act on the Central Bank, the Committee is chaired by the Governor or the Deputy Governor for Financial Supervision, depending on circumstances. When the FMEN takes decisions on the adoption of rules of procedure and on the transfer of authority to the Deputy Governor for Financial Supervision, as well as decisions pertaining to systemically important financial institutions' capital, liquidity, and funding, the Governor takes a seat on the FMEN as its chair and the Deputy Governor for Financial Supervision acts as vice-chair.

In other instances, the Deputy Governor for Financial Supervision chairs the Committee and the Deputy Governor for Financial Stability acts as vice-chair. In addition to the Governor and two deputy governors, the FMEN comprises three outside experts appointed by the Minister of Finance and Economic Affairs.

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This *Annual Report* presents the highlights of the Bank's activities in these three main areas of operation and the developments that took place. Additional topics covered include international reserve maintenance, payment intermediation, Government debt management, international cooperation, and other activities. The Bank's consolidated annual accounts can be found at the end of the *Annual Report*.



The Supervisory Board as of year-end 2021, together with the Governor and the Board secretary. Seated, from left: Ásgeir Jónsson (Governor), Thorunn Guðmundsdóttir, Gylfi Magnússon (Chairman), and Guðún Sóley Gunnarsdóttir (Secretary). Standing, from left: Una María Óskarsdóttir, Sigurdur Kári Kristjánsson, Jóhanna Vígdís Guðmundsdóttir, Frosti Sigurjónsson and Jacqueline Clare Mallett. Jóhanna Vígdís Guðmundsdóttir is alternate for Bolli Hédinsson who was unable to attend on the day the photo was taken.

# Monetary policy

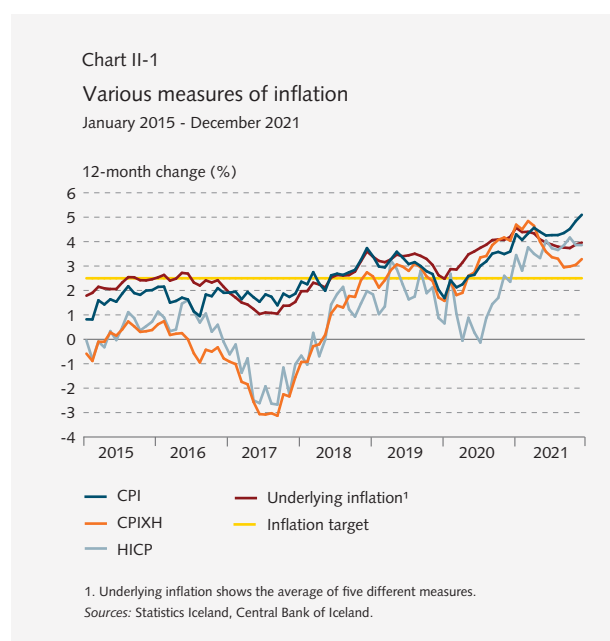


The Central Bank of Iceland is required by law to promote price stability. According to the joint declaration issued by the Central Bank and the Government on 27 March 2001, the price stability objective is defined as a 2½% rise in the consumer price index (CPI) over a twelve-month period. The Act also stipulates that the Monetary Policy Committee (MPC) shall take decisions on the application of the Bank's monetary policy instruments with the aim of achieving this objective.

## Developments in inflation, interest rates, and exchange rate in 2021

Inflation averaged 4.4% in 2021, as compared with 2.8% in 2020. It measured 4.3% at the beginning of 2021 and remained broadly unchanged until late in the year, whereupon it rose swiftly, measuring 5.1% in December. Inflation excluding housing measured 3.8% in 2021, and the spread between inflation including and excluding housing widened over the course of the year. Underlying inflation fell during the year, measuring 4% in December 2021, according to the median of various measures, as compared with 4.2% a year earlier.

The main drivers of inflation in 2021 were house prices, private services, and fuel prices. In December 2021, the cost of owner-occupied housing was up 13.3% year-on-year. House prices nationwide rose by 15.9% over the same period, as compared with 7.8% a year earlier. This was offset in part by lower real mortgage interest expense. Exchange rate pass-through to domestic goods prices subsided as the year progressed, and imported inflation gradually eased. The rise in fuel prices made a strong impact, however, as global oil prices were above the pre-pandemic level by November

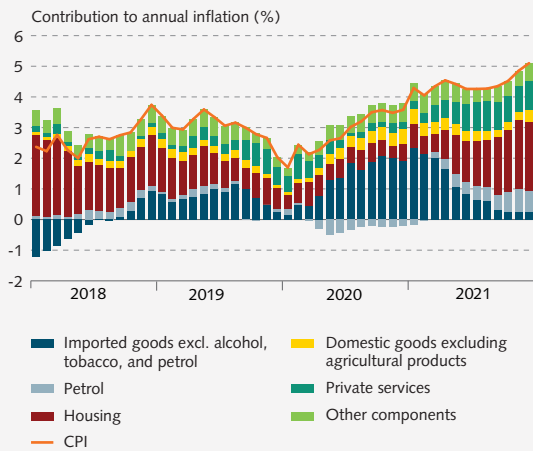


2021. Imported goods prices were up 2.9% year-on-year in December. Private services prices also inched upwards over the course of the year, particularly in H1, when public health measures were eased. The year-on-year increase measured 4.1% in December.

Central Bank interest rates remained unchanged until May 2021, when the MPC decided to raise them by 0.25 percentage points. In both August and October, the Committee decided to raise rates again, by 0.25 percentage points each time, and in November they were raised by 0.5 percentage points. At the end of 2021, the Bank's key interest rate (the rate on seven-day term deposits) was 2% and had been raised by 1.25 percentage points over the course of the year. The grounds for the rate hikes were that the economic outlook had improved,



Chart II-2  
Components of CPI inflation  
January 2018 - December 2021



Sources: Statistics Iceland, Central Bank of Iceland.

fuelled by strong domestic demand, and that the slack in output looked set to close earlier than previously thought. The inflation outlook had worsened, however, and it was expected to take longer to bring inflation back to target than previously projected. Furthermore, there was the risk that elevated global inflation, supply-chain disruptions, and domestic wage rises would cause inflation to remain high, potentially leading to a further rise in inflation expectations.

In terms of the Central Bank's real interest rate, the monetary stance eased at the beginning of 2021 but then tightened in tandem with the Bank's nominal rate increases over the course of the year. The Bank's real rate

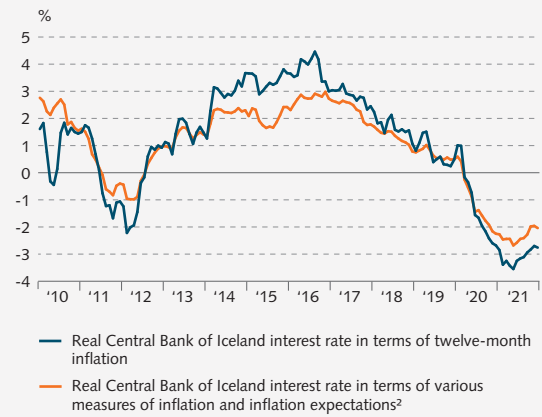
Chart II-3  
Central Bank of Iceland key interest rate<sup>1</sup>  
Daily data 3 January 2001 - 31 December 2021



1. The Central Bank's key interest rate is defined as follows: the 7-day collateralised lending rate (until 31 March 2009), the rate on deposit institutions' current accounts with the Central Bank (1 April 2009 - 30 September 2009), the average of the current account rate and the rate on 28-day certificates of deposit (1 October 2009 - 20 May 2014), and the rate on 7-day term deposits (from 21 May 2014 onwards).

Source: Central Bank of Iceland.

Chart II-4  
Real Central Bank of Iceland interest rates<sup>1</sup>  
January 2010 - December 2021

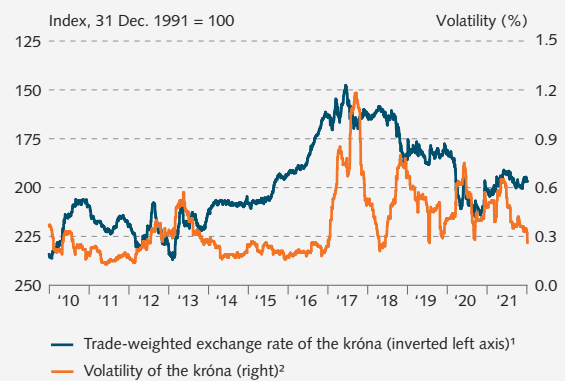


1. From 2010 to May 2014, the nominal policy rate was the average of the current account rate and the maximum rate on 28-day CDs. From May 2014, the policy rate has been the seven-day term deposit rate. 2. Until January 2012, according to twelve-month inflation, one-year business inflation expectations, one-year household inflation expectations, the one-year breakeven inflation rate, and the Central Bank forecast of twelve-month inflation four quarters ahead. From February 2012 onwards, according to the above criteria, plus one-year market inflation expectations based on a quarterly Central Bank survey.

Sources: Gallup, Statistics Iceland, Central Bank of Iceland.

in terms of the average of various measures of inflation and one-year inflation expectations measured -2.1% at the year-end, after rising by 0.7 percentage points since the May 2021 rate hike. The real rate in terms of twelve-month inflation rose by 0.7 percentage points over the same period, to -2.9% at the end of the year. At its August meeting, the MPC decided that the Bank should temporarily stop placing bids in the secondary market for Treasury bonds. The Committee was of the view that the purchases had been successful and had prevented a rise

Chart II-5  
Exchange rate and volatility of the króna  
Daily data 4 January 2010 - 31 December 2021



1. Price of foreign currency in terms of the króna. Inverted axis shows a stronger króna as a rise. 2. Volatility is measured by the standard deviation of daily changes in the past 3 months.

Source: Central Bank of Iceland.



in long-term yields when the pandemic reached Iceland and fiscal uncertainty was high. Committee members also agreed that this policy instrument should remain available so that it could be activated if conditions warranted its use.

The Central Bank intervened more actively in the foreign exchange market after the pandemic began, and in September 2020 it began a programme of regular foreign currency sales with the aim of deepening the market and improving price formation. In March 2021, the Bank decided to scale down its regular currency sales, and at the beginning of May it discontinued them altogether, as the foreign exchange market appeared better balanced. Over the course of the summer, the króna began to depreciate in spite of a strong recovery in tourism and increased use of foreign payment cards in Iceland, but some outflows relating to new investment continued, and the goods account was in deficit. The króna began to strengthen again in November, probably due in part to an increase in forward currency sales. By the end of 2021, the króna had depreciated by 2.5% in trade-weighted terms during the year, as compared with a depreciation of 10.4% in 2020.

In 2021 as a whole, the Bank bought currency for 26.9 b.kr. and sold currency for 49.6 b.kr. The Bank's net foreign currency sales in the market therefore totalled 22.7 b.kr. The Bank's transactions accounted for 21% of interbank market turnover in 2021, as compared with 37% in 2020. Total turnover in the market contracted by 12% relative to 2020.

Nominal Treasury bond yields rose during the year, in spite of a dip during the summer. Yields on most nomi-

nal Treasury bonds lay in the 3.2-4.1% range at the end of the year, an increase of 1.5 percentage points since year-end 2020. Indexed long-term rates rose early in the year but began to fall in H2. The yield on the longest indexed Treasury bonds was 0.5-0.7% at the year-end, up to 0.2 percentage points lower than it had been a year earlier.

To pursue forward-looking monetary policy, a central bank needs models for assessing the economic outlook, especially inflation. The Bank is constantly developing models for use in assessing the economic outlook and analysing the impact of monetary policy. As an element in this, the Bank publishes its main forecasting model and database on its website.

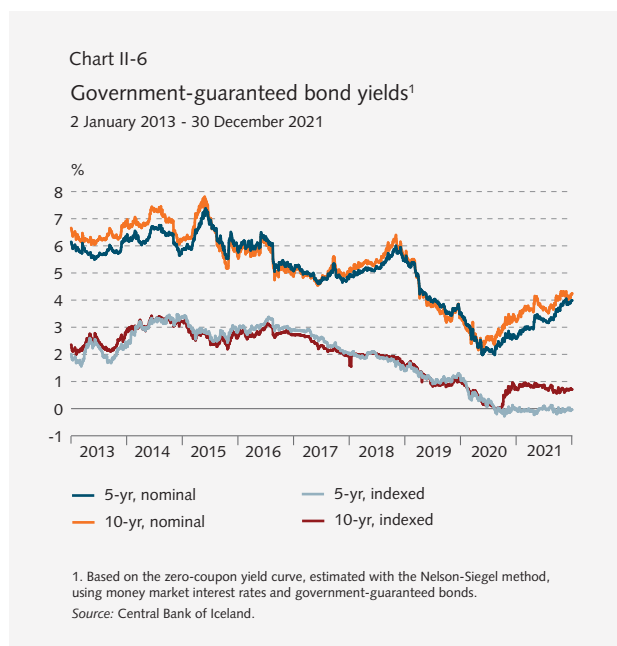
Further discussion of developments in monetary policy, exchange rate and currency matters, and the Bank's policies and actions in these areas during the year can be found in the minutes of MPC meetings and in the Bank's quarterly *Monetary Bulletin*.

## Monetary Policy Committee

By law, the MPC takes decisions on the application of the Bank's monetary policy instruments. In this context, the Bank's monetary policy instruments are its interest rate decisions, transactions with credit institutions other than loans of last resort, decisions on reserve requirements, and foreign exchange market transactions.

In 2020, MPC members were Governor Ásgeir Jónsson, who chairs the Committee by law; Rannveig Sigurdardóttir, Deputy Governor for Monetary Policy and vice-chair of the Committee; Gunnar Jakobsson, Deputy Governor for Financial Stability; Gylfi Zoëga, professor at the University of Iceland; and Katrín Ólafsdóttir, Associate Professor at Reykjavík University.

The Committee met six times in 2021 and issued a statement on its decision after each meeting. Furthermore, two weeks after the announcement of each interest rate decision, the Committee published the minutes of its meetings, containing the rationale for its decisions and the assumptions on which they were based. The minutes included the Committee's assessment of economic and monetary developments and prospects, the rationale for members' position, and information on individual members' votes. As is provided for by law, the MPC reported to Parliament on its activities twice during the year.



## Decisions of the Monetary Policy Committee in 2021

The MPC's decisions on the application of the Bank's monetary policy instruments were as follows:

*3 February:* The Governor proposed that the Bank's interest rates be held unchanged. All Committee members voted in favour of the proposal.

*24 March:* The Governor proposed that the Bank's interest rates be held unchanged. All Committee members voted in favour of the proposal.

*19 May:* The Governor proposed that the Bank's interest rates be raised by 0.25 percentage points. All members voted in favour of the Governor's proposal, although Gunnar Jakobsson would have preferred to raise rates by 0.5 percentage points.

*25 August:* The Governor proposed that the Bank's interest rates be raised by 0.25 percentage points. All members voted in favour of the Governor's proposal, although Gunnar Jakobsson and Gylfi Zoëga would have preferred to raise rates by 0.5 percentage points.

*6 October:* The Governor proposed that the Bank's interest rates be raised by 0.25 percentage points. Ásgeir Jónsson, Rannveig Sigurdardóttir, and Katrín Ólafsdóttir voted in favour of the proposal. Gunnar Jakobsson and Gylfi Zoëga voted against the Governor's proposal and wanted to raise rates by 0.5 percentage points.

*17 November:* The Governor proposed that the Bank's interest rates be raised by 0.5 percentage points. All Committee members voted in favour of the proposal.



The Monetary Policy Committee at year-end 2021, together with the Committee secretary. Seated, from left: Ásgeir Jónsson Governor, (Chairman) and Rannveig Sigurdardóttir, Deputy Governor for Monetary Policy. Standing, from left: Karen Áslaug Vignisdóttir (Secretary); Gunnar Jakobsson, Deputy Governor for Financial Stability; Katrín Ólafsdóttir, Assistant Professor at Reykjavik University; and Gylfi Zoëga, Professor at the University of Iceland.

# Financial stability



## General information

One of the Central Bank of Iceland's tasks is to promote financial stability. Financial stability means that the financial system is resilient enough to withstand shocks to the economy and financial markets, to mediate credit and payments, and to redistribute risks appropriately.

The Bank monitors and analyses the position of the financial system and payment intermediation and responds as needed to counteract developments that could undermine the stability of the system. The Bank also closely monitors individual credit institutions, financial markets, households and businesses, the external position of the economy, capital flows, and the refinancing risk faced by domestic participants in foreign credit markets. By law, the Central Bank Financial Stability Committee (FSN) takes decisions on the application of the Bank's financial stability policy instruments.

The new Foreign Exchange Act, no. 70/2021, entered into force in June 2021, repealing the previous Foreign Exchange Act and the Act on the Treatment of Króna-Denominated Assets Subject to Special Restrictions (also called Offshore Króna). A number of rules and regulations relating to the capital controls were repealed at the same time, including restrictions on derivatives trading. The new Act eliminated the last of the capital controls that had been in place since the economic crisis of 2008. The fundamental principles of the Foreign Exchange Act are the same as before: foreign exchange transactions, cross-border movement of capital, and cross-border payments shall be unrestricted. However, the Bank is authorised to take measures to preserve economic and financial stability if necessary. These measures fall into two broad categories: preventive measures, called macroprudential tools, and protec-

tive measures (restrictions), which can be adopted with ministerial authorisation in exceptional cases and under extraordinary conditions.

The Central Bank's new Rules on Credit Institutions' Minimum Net Stable Funding Ratio, no. 750/2021, for all currencies combined, took effect during the year, replacing the previous Rules on Stable Funding Ratios in Foreign Currencies from 2014. The new Rules are based on the EU Regulation on stable funding. They have a broader scope of applicability than their predecessor, and they now apply to all credit institutions and not only the commercial banks. According to the Rules, credit institutions are required to maintain a total stable funding ratio of at least 100%, and they must ensure that the currency composition of their assets is aligned with the currency composition of their liabilities.

The Central Bank's goal is to promote security, efficiency, and efficacy of core infrastructure in the Icelandic financial system; i.e., systemically important financial market infrastructure. The constant increase in cyberthreats has prompted central banks all over the world to place stronger emphasis on cyber risk, including the necessity of joint responses to it. It is generally acknowledged that severe or repeated cyberattacks can pose a threat to financial stability. In 2021, the Central Bank established a special cooperative forum on the operational security of financial market infrastructure, known by the acronym SURF. SURF aims to create a common vision for measures to enhance the resilience of the cyber- and IT systems of important financial infrastructure elements and coordinate measures in case of operational disruptions that could affect financial system security and efficacy. Particular emphasis is to be placed on shoring up cybersecurity defences and finan-

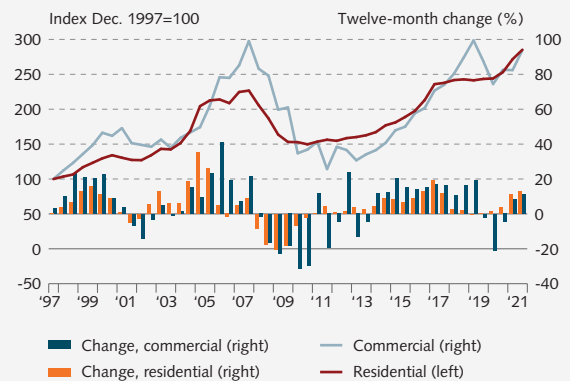
cial system resilience against cyberattacks. In this context, consideration shall be given to the Government's cybersecurity framework, with reference to possible overlapping, interactions, and views on harmonisation. The forum's work shall also be guided by the Act on Network and Information Security, no. 78/2019, with which systemically important financial institutions and operators of regulated securities markets and multilateral trading facilities must comply. Participation in SURF is voluntary. Participants other than the Central Bank include representatives from Arion Bank, the Electronic Communications Office of Iceland (ECOI), the Ministry of Finance and Economic Affairs, Íslandsbanki, the Nasdaq Iceland exchange, Landsbankinn, the Nasdaq CSD securities depository, the Computer Emergency Response Team (CERT-IS), and the Icelandic Financial Services Association.

Late in 2021, the shareholders of the Icelandic Banks' Data Centre (RB) reached an agreement to change the focus of the company's operations, with the objective of strengthening security and promoting greater efficacy and efficiency in the operation of financial market infrastructure in Iceland. The changes entail explicitly defining RB activities to include joint operation of systems of importance to the financial market, operation of payment intermediation systems, and operation of related infrastructure. In order to achieve greater synergy in the operation of joint financial market infrastructure, RB purchased the ARK system and the SWIFT services of Central Bank-owned company Greidsluveitan ehf. In the future, RB will be solely owned by deposit-taking financial institutions and Greidsluveitan, which administers the Central Bank of Iceland's holding. Concurrent with the changes to RB, the Central Bank established a Payment Council, a Rulebook Council, and a so-called Forum for the Future, in order to support payment intermediation objectives even more effectively. Greidsluveitan will be responsible for this on behalf of the Central Bank.

The Central Bank of Iceland operates a separate unit called the resolution authority on the basis of the Act on Resolution of Credit Institutions and Investment Firms, no. 70/2020. The resolution authority is empowered with taking decisions on resolution and applying resolution measures in cases involving financial institutions that are failing or likely to fail.

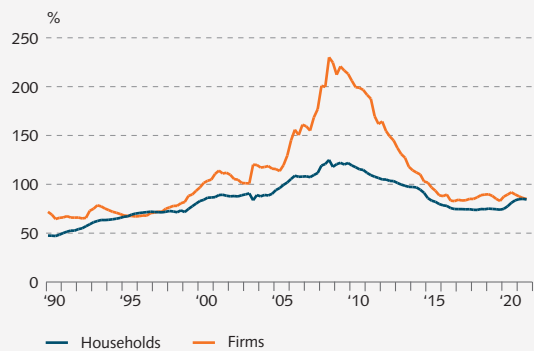
Among the authority's first tasks was to formulate proposals for a bill of legislation on claim hierarchy during resolution and winding-up proceedings. The bill was subsequently passed as Act no. 38/2021, thereby incorporating into Icelandic law the provisions of Directive

Chart III-1  
Real property prices<sup>1</sup>



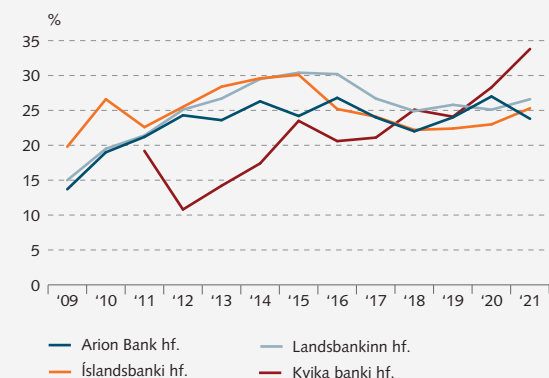
1. Price indices for the greater Reykjavik area (Dec. 1997-Dec. 2021), deflated with the CPI. Commercial property prices are the avg. of industrial, retail, and office property.  
Sources: Statistics Iceland, Central Bank of Iceland.

Chart III-2  
Credit to households and firms as percentage of GDP<sup>1</sup>



1. Total claim value credit to households and nonfinancial firms, excluding holding companies, divided by the GDP of the last four quarters.  
Sources: Statistics Iceland, Central Bank of Iceland.

Chart III-3  
Commercial banks' capital adequacy ratios<sup>1</sup>



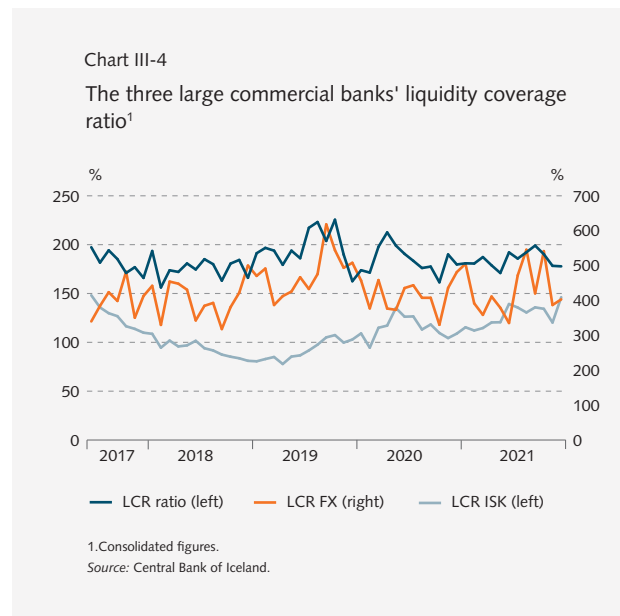
1. Consolidated figures. Capital base as % of risk-weighted base.  
Sources: Commercial banks' annual accounts.



(EU) 2017/2399 on the ranking of unsecured debt instruments in insolvency hierarchy. The passage of Act no. 38/2021 was one of the first steps towards the formulation of the Central Bank's policy on minimum required own funds and eligible liabilities, or MREL (discussed more fully below). A large number of EEA instruments concerning MREL, preparation of resolution plans, and execution of resolution measures on the basis of Directive 2014/59/EU (the first Bank Recovery and Resolution Directive, BRRD I) were implemented with the adoption of Governmental directives by the Ministry of Finance and Economic Affairs and the Central Bank. The resolution authority has posted the European Banking Authority's (EBA) guidelines on resolution on its website and will use them as a reference when preparing and executing resolution measures in Iceland. With these steps, the implementation of BRRD I is well advanced in Iceland. Preparation for the implementation of BRRD II is also underway. In substance, BRRD II focuses in particular on MREL, and the impact of BRRD II is discussed in the Bank's MREL policy. The provisions of BRRD II relate in part to the provisions of the Capital Requirements Regulation (CRR II), including those on new requirements for eligible liabilities.

The resolution authority prepares resolution plans for financial institutions. The resolution plans, which will only be accessible to the resolution authority itself, will be prepared based on data from the Bank's financial supervisory authority and the undertakings concerned. Resolution plans are based on a strategic business analysis that entails an overview of all critical functions and core activities of financial institutions. They shall lay down the preferred resolution strategy, describe the possible versions of the preferred resolution strategy and other strategies, and specify the measures that the resolution authority will take if a given company is deemed to be failing or likely to fail.

Before a resolution plan is approved, a resolvability assessment must be carried out. In 2021, resolvability assessments for Iceland's domestic systemically important banks were conducted. Furthermore, a public interest assessment was conducted for other credit institutions to determine whether resolution or normal insolvency proceedings should be considered as the preferred option in case of a failing institution. Towards the end of 2021, the Central Bank's MREL policy was approved and published. The policy describes the methodology the Bank uses in determining minimum requirements for own funds and eligible liabilities, or MREL requirements.



## The state of financial stability

The battle with the COVID-19 pandemic continued during the year. A wide range of Government support measures, coupled with accommodative monetary and macroprudential policies, mitigated the economic fall-out from the pandemic and supported households and businesses. As the year progressed, both monetary and macroprudential policies were tightened again as the impact of the pandemic began to subside.

The state of financial stability was good at the year-end, although pandemic-related uncertainty remained, particularly because of the spread of the Omicron variant of the virus towards the end of the year. The commercial banks were highly resilient, and their capital and liquidity were well above regulatory minima. On the other hand, systemic risk increased due to steep rises in the price of equity securities and real estate during the year, particularly as a result of growing household debt alongside the surge in house prices. A tighter monetary and macroprudential policy stance should counteract this trend. Uncertainty and risk stemming from events and/or shocks abroad increased during the year and could pose a threat to financial stability.

A strong banking system has been of pivotal importance in maintaining financial stability and a smoothly functioning financial system. The Central Bank's interest rate cuts at the beginning of the pandemic, together with the suspension of the countercyclical capital buffer and other measures to boost financial system liquidity, made it easier for financial institutions to offer borrowers moratoria on payment while maintaining their lending capacity. This strongly supported asset markets.

All of the commercial banks generated robust profits in 2021, and their returns were all in line with or above their targets. Strong returns stemmed in part from the banks' reversal of a portion of year-2020 impairment; an increase in commissions, fees, and income from financial activities alongside favourable developments in asset markets; and continued balance sheet growth, which was due largely to increased mortgage lending to households. The banks' cost-cutting measures have enabled them to strengthen returns on core activities still further.

Non-performing loan (NPL) ratios declined over the course of the year, and by the year-end household NPL ratios were below the pre-pandemic level. Although corporate NPL ratios declined during the year, they were considerably higher than at the start of the pandemic, as companies in tourism and other services sectors affected by public health measures have particularly needed payment assistance measures.

Even though the commercial banks paid sizeable dividends in 2021, their liquidity was ample at the year-end, and well above both Central Bank minima and the banks' own internal benchmarks. In part, the strong liquidity position reflects an increase in deposits. All of the banks took advantage of ready access to foreign credit markets and refinanced debt during the year.

## Financial Stability Committee

By law, decisions on the application of the Central Bank's financial stability policy instruments are taken by the Financial Stability Committee (FSN). The FSN's role is to assess developments and prospects for the financial system, systemic risk, and financial stability. The Committee is also tasked with discussing and defining the actions deemed necessary at any given time in order to affect the financial system so as to strengthen and preserve financial stability, and to this end, the Committee is required to direct comments to the appropriate Governmental authorities when warranted. In addition, the FSN is required to approve Governmental directives and take the decisions entrusted to it by law. It is also entrusted with deciding which supervised entities, infrastructure elements, and markets shall be considered systemically important and of such a nature that their activities could affect financial stability.

The FSN comprises the Governor, all three Deputy Governors, and three outside experts. The Permanent Secretary or an appointed official from the Ministry responsible for financial stability also participates in Committee meetings as a non-voting member with

the right to address the meeting and present proposals. Members of the FSN in 2021 were Governor Ásgeir Jónsson, who chaired the Committee; Gunnar Jakobsson, Deputy Governor for Financial Stability and vice-chair; Rannveig Sigurdardóttir, Deputy Governor for Monetary Policy; Unnur Gunnarsdóttir, Deputy Governor for Financial Supervision; Axel Hall, Assistant Professor at Reykjavík University; Bryndís Ásbjarnardóttir, Economist at Statistics Iceland; and Gudmundur Kristján Tómasson, former Director of Financial Market Infrastructure at the Central Bank of Iceland.

The Committee is required by law to meet at least four times a year. In 2021 it met five times. The Committee made its decisions public in four statements issued during the year, in which it explained the application of financial stability policy instruments and presented its assessment of developments and prospects for the financial system, systemic risk, and financial stability. The minutes of FSN meetings are posted on the Central Bank website. Further discussion of financial stability and the Bank's policy and actions in this area can be found in the FSN minutes and in the Bank's semi-annual *Financial Stability* reports.

## Financial Stability Committee decisions in 2021

In March, the FSN decided to hold the countercyclical capital buffer unchanged at 0%.

In June, the Committee decided to set special rules on derivatives trading on the basis of the new Foreign Exchange Act. The Rules provide for fewer and simpler restrictions on foreign exchange transactions than before. The Committee also decided to lower the maximum loan-to-value ratio on consumer mortgages from 85% to 80% for all but first-time buyers, for whom the maximum was held unchanged at 90%. Furthermore, it decided to examine further the possibility of capping the debt service-to-income ratio on household mortgages. The FSN decided to hold the countercyclical capital buffer on financial institutions unchanged at 0%.

In September, the Committee decided to set rules on maximum debt service-to-income ratios on consumer mortgages. Effective 1 December 2021, the maximum ratio would be 35% of the borrower's disposable income, and 40% for first-time buyers. Under the rules, the ratio may be calculated based on an annuity mortgage amortisation schedule and a specified maximum loan term. Lenders were granted an exemption from the rules for up to 5% of the total amount of new mortgage loans issued each quarter. In view of the build-

up of cyclical systemic risk, the FSN decided to increase the countercyclical capital buffer from 0% to 2%. The decision will take effect at the end of September 2022, in accordance with the rules applying to the buffer. Also in September, the FSN completed its annual review of systemically important financial institutions, carried out in accordance with EBA methodology, and confirmed the systemic importance of Arion Bank hf., Landsbankinn hf., and Íslandsbanki hf. The Committee held the buffer for systemic importance (O-SII buffer) unchanged at 2% on all exposures at the parent company level and on a consolidated basis.

In November, the FSN discussed matters relating to the resolution authority and approved the assessment of the systemically important commercial banks' resolvability.

In December, the FSN approved the Central Bank's MREL policy, which, among other things, specifies how credit institutions' MREL requirements are determined. MREL requirements represent the own funds and eligible liabilities a financial undertaking must hold so as to ensure that it can absorb unforeseen losses and recapitalise its activities without Government support if it should be deemed failing or likely to fail. The Committee also decided to hold the countercyclical capital buffer unchanged at 2%.



Financial Stability Committee, as composed in 2021. Seated, from left: Rannveig Sigurdardóttir, Deputy Governor for Monetary Policy; Ásgeir Jónsson, Governor (Chairman); Gunnar Jakobsson, Deputy Governor for Financial Stability; and Unnur Gunnarsdóttir, Deputy Governor for Financial Supervision. Standing, from left: Eggert Thröstur Thorarinsson (Secretary); Tómas Brynjólfsson, Director General, Ministry of Finance and Economic Affairs, with the right to address the meeting but without voting rights; Bryndís Ásbjarnardóttir, Economist, Statistics Iceland; Gudmundur Kristján Tómasson, former Director of Financial Market Infrastructure, Central Bank of Iceland; and Axel Hall, Assistant Professor, Reykjavik University.



# Financial supervision

## IV

The Central Bank of Iceland is tasked with promoting sound and secure financial activities. It is responsible for the tasks entrusted by law and Governmental directives to the financial supervisory authority. The Bank monitors supervised entities to ensure that their activities are in compliance with the law and with Governmental directives, and that they are in other respects consistent with sound and appropriate business practice; cf. the Act on Official Supervision of Financial Activities. The Bank also ensures that supervised entities are attentive to consumer protection in their activities.

### Financial Supervision Committee

The Financial Supervision Committee (FMEN) takes decisions entrusted to the financial supervisory authority by law or Governmental directives. The Committee is authorised to entrust the Deputy Governor for Financial Supervision with taking non-major decisions.

In 2021, the FMEN held eleven meetings, in addition to handling nine cases outside meetings, as it is authorised to do.

Members of the Financial Supervision Committee are Ásgeir Jónsson, Governor; Unnur Gunnarsdóttir, Deputy Governor for Financial Supervision; Gunnar Jakobsson, Deputy Governor for Financial Stability; economist Ásta Thórarinsdóttir; Andri Fannar Bergthórsson, Assistant Professor at Reykjavík University; and Guðrún Thorleifsdóttir, Director General at the Ministry of Finance and Economic Affairs. As is provided for in the Act on the Central Bank, the Committee is chaired by the Governor or the Deputy Governor for Financial Supervision, depending on circumstances. When the FMEN takes decisions on the adoption of rules of pro-

cedure and on the transfer of authority to the Deputy Governor for Financial Supervision, as well as decisions pertaining to other systemically important financial institutions' (O-SIs) capital, liquidity, and funding, the Governor takes a seat on the FMEN as its chair and the Deputy Governor for Financial Supervision acts as vice-chair. In other instances, the Deputy Governor for Financial Supervision chairs the Committee and the Deputy Governor for Financial Stability acts as vice-chair.

In a statement dated 13 January 2021, the FMEN published amended guidelines on financial institutions' and insurance companies' dividend payments and share buybacks. In the amended guidelines, the FMEN encouraged financial institutions to observe the utmost caution in paying dividends and buying back their own shares through 30 September 2021. With a statement dated 30 June 2021, the FMEN withdrew its guidelines earlier than originally planned, as COVID-19 appeared to have less impact on financial institutions than had been feared at the beginning of the year. Nevertheless, the FMEN urged financial institutions to continue observing the utmost caution in decisions to pay dividends and preparation of plans to buy back their own shares.

### Supervision of financial institutions

The Central Bank's supervision of financial undertakings includes supervision of commercial banks, savings banks, credit undertakings, investment firms, payment institutions, and electronic money institutions. Regular supervision of financial undertakings is carried out in accordance with the Bank's risk-based supervision approach, which defines the frequency with which key risk factors in the companies' operations are examined. It entails a

review of data regularly submitted by the institutions concerned, as well as an examination of key metrics and business plans. Proactive checks and analyses are carried out as well, and interviews are taken with key employees of supervised entities.

The Bank's Financial Stability Committee (FSN) has designated three commercial banks – Arion Bank hf., Íslandsbanki hf., and Landsbankinn hf. – as other systemically important institutions (O-SIIs). Because O-SIIs are so important from the standpoint of financial stability, supervising them is much more intrusive than supervising other entities.

The quality of loans granted by the banks and other credit undertakings that have suffered the effects of COVID-19 is monitored closely, and supervision of credit risk has been given greater priority, including with more frequent on-site inspections. The most extensive measure taken domestically in response to borrowers' COVID-19-related difficulties was the grant of general moratoria on payment, although these expired in late 2021. In the wake of the general moratoria, many borrowers have been granted extended moratoria on payments of interest and/or principal. Loans protected by such concessions are no longer classified in the usual manner but are most frequently classified as *forborne*. Under these conditions, the fundamental principle of prudence and accounting – i.e., that both long-term and short-term credit risk on credit undertakings' balance sheets must be appraised correctly – is put even more to the test. It is important that credit undertakings' framework support timely identification of risk, appropriate processing of loans that have been in moratorium, effective handling of loan impairment, and effective oversight of non-performing loans.

There is still some uncertainty about the O-SIIs' loan quality, but their non-performing loan ratio as defined by the European Banking Authority (EBA) was historically low at the end of 2021, or close to 2%. At the same time, the share of forborne loans in Iceland has been well above the European average, although it is declining. Furthermore, the banks' optimistic forecasts concerning loan quality have caused impairment to be reversed to considerable extent. This, plus rapidly rising mortgage lending, explains much of the decline in their impairment ratios in 2021.

During the year, continued emphasis was placed on operational risk in assessing risk in the financial market, with particular attention given to outsourcing, in accordance with financial supervision priorities. In view of the EBA's focus on cyber risks, and owing to the growing threat stemming from cyberattacks, emphasis

was also placed on examining financial institutions' cyber risks and cyber-resilience. Preparation for the implementation of EU Directive 2015/2366 on payment services (PSD2) into Icelandic law began, including the use of a new deviation reporting system based on EBA guidelines for PSD2. The Directive was implemented in Iceland with the passage of the Payment Services Act, no. 114/2021.

### **Supervisory review and evaluation process (SREP)**

Every year, the Bank's financial supervisory authority carries out a detailed supervisory review and evaluation process (SREP) on the O-SIIs. In the SREP, the Bank evaluates the key risks entailed in the banks' operations and the methods they use to handle those risks, including risk management and control. The Bank also assesses and determines the banks' capital requirement under Pillar II-R, which indicates how much capital the bank in question must hold in view of the risks it faces or could face. The Pillar II-R capital requirement is in addition to the minimum capital requirement provided for under Pillar I. The SREP is carried out in accordance with the *Guidelines for common procedures and methodologies for the supervisory review and evaluation process* (SREP Guidelines). The guidelines are revised regularly and are in line with the EBA guidelines on the same topic.

In July 2021, the results of the systemically important banks' supervisory review and evaluation process were published. The results pertained to additional capital requirements over and above the minimum capital requirement and the combined capital buffer requirement. According to the FMEN's decision, the additional capital requirement for systemically important banks at the group level lies in the 2.5-3.5% range, bringing the overall capital requirement to 17.8-18.9%. The banks' capital ratios were well above these thresholds at the end of 2021.

For less significant financial institutions, the SREP is carried out less often than for the systemically important banks; i.e., generally every third year, unless circumstances call for greater frequency. In intervening years, less extensive annual risk analyses are carried out for these institutions. This accords with the fundamental principle of risk-based supervision: that primary emphasis should be placed on supervision of institutions that could jeopardise financial stability or expose a large group of customers to severe inconvenience or loss.

### **Recovery plans**

At the end of 2021, the O-SIIs submitted recovery plans to the Bank for the fourth time. The financial conglomerate created by the merger of Kviká banki and TM

tryggingar hf. joined the subset of financial institutions required to submit full recovery plans. The Kvika group submitted its first such recovery plan at the end of the year.

Less significant financial institutions submitted simplified recovery plans for the second time in October 2021.

## Supervision of insurance activities

In 2021, emphasis was placed on governance practices, market risk, operational risk, and insurance risk in the supervision of the insurance market.

Regulatory supervision of insurance companies centres on their solvency margins and their ability to cover financial obligations. The Bank monitors closely to ensure that the entities concerned satisfy the requirements for their operating licences, that their operating practices are in compliance with regulatory provisions, and that appropriate measures are taken at all times. In addition, it reviews regularly submitted reports and takes interviews with CEOs, key function holders, and external auditors. Furthermore, each year the Bank carries out an assessment of risks relating to insurance companies' operations in accordance with its *General criteria and methodology for supervision of insurance companies*, as well as analysing developments in the market. Cooperation with the European Insurance and Occupational Pensions Authority (EIOPA) is an important aspect of regular monitoring of insurance companies. EIOPA's priorities are reflected in the Bank's supervisory project timetable, for example, and the regulatory framework for the insurance market is prepared in consultation with EIOPA. The Bank keeps close track of this work.

Proactive checks of insurance companies' activities were carried out in 2021 and, among other things, key functions were examined with reference to regulatory requirements, including compliance and risk management. An investment-related proactive check was also carried out and self-evaluations requested from the companies' boards of directors. In addition, the assumptions underlying solvency margin calculations were examined. Where applicable, comments resulting from these checks were communicated to the companies concerned.

## Supervision of pension funds and pension savings custodians

The Central Bank supervises pension funds and third-pillar pension savings custodians. This entails, on the

one hand, regular monitoring in accordance with the Bank's risk-based supervision model, which defines the frequency with which key risk factors in the pension funds' operations are examined, and on the other hand, proactive checks carried out based on the circumstances in each given instance. The Bank analyses key risks and developments in the markets; furthermore, it monitors closely to ensure that the entities concerned satisfy the requirements for their operating licences, that their operating practices are in compliance with regulatory provisions, and that appropriate measures are taken at all times. Furthermore, the pension funds' risk assessments are examined, and interviews are taken with selected key employees.

Regular supervision of pension funds and third-pillar pension savings custodians entails monitoring their compliance with regulatory provisions. In addition, the Bank conducts an annual assessment of the risks in pension fund operations. In 2021, particular emphasis was placed on pension funds' governance, operational risk, outsourcing, and market risk, and proactive checks were carried out in connection with these, including risk management and outsourcing, as well as checks on the funds' actuarial position. The Bank reviewed the pension funds' own risk assessments and took interviews with managing directors, internal and external auditors, and actuaries. Comments and recommendations were communicated to the pension funds following these checks.

## Supervision of markets and business conduct

During the year, retail investors were more active in the domestic securities markets than over the previous several years. They invested sizeable amounts in UCITS and alternative investment funds and the number of retail investors as shareholders in listed companies also increased.

### Supervision of the securities markets

The objective of securities market supervision is to promote a secure and effective market. This is done through ongoing supervision of information disclosures made by issuers, supervision of market participants' business conduct – including potential insider trading and market abuse – and examination of reports submitted to the Bank by supervised entities. Furthermore, the Bank supervises the activities of securities exchanges (one party) and central securities depositories (two parties).

In 2021, the Bank opened investigations into 24 cases stemming from the securities market, 15 of which

resulted from tips submitted by Nasdaq Iceland. As in previous years, most of the cases involved alleged insider misconduct and issuers' information disclosure requirements. Of the cases investigated, 16 were concluded in 2021, and as in previous years, most of them (12 cases in 2021) were closed with the determination that a violation had not been committed. Three of the cases were concluded with comments to the parties in question, and one case of alleged market abuse was referred to the police.

An on-site inspection of a commercial bank's transactions reporting was concluded. Nasdaq Iceland submitted a total of 13 requests for waivers of pre-trade transparency requirements for specified types of orders placed by market agents in the exchange's order management systems. The waiver requests were approved during the year. Approved prospectuses and notifications of short positions declined in number relative to the prior year. Even though prospectuses decreased in number, large prospectuses for Íslandsbanki hf. and Sildarvinnslan hf. were approved in connection with the admission of the companies' shares for trading in the Nasdaq Iceland Main Market.

### **Supervision of business conduct**

The Central Bank conducts monitoring to ensure that supervised entities' business conduct is sound and appropriate. This entails, among other things, proactive checks and checks carried out in response to tips submitted to the Bank. Analysis is also carried out, including analysis of investments by retail investors. The Bank's objectives in this regard are to promote improved financial market conduct and strengthen consumer protection. Business conduct includes all types of communications between supervised entities and their current and prospective customers in connection with the sale of goods and services; i.e., provision of information to customers, advisory services, pricing transparency, marketing, and handling of complaints. During the year, the Bank regularly published announcements on matters relating to consumers and/or market participants, as well as passing warnings from European supervisory agencies on to market agents and consumers via the Bank's website.

In 2021, the Bank received 176 tips and complaints pertaining to business conduct and consumer affairs in the financial market. Several checks were carried out during the year, including a check on one entity's marketing of UCITS funds on social media and checks on three pension funds' provision of information on the division of pension rights between spouses.

In addition, an analysis of retail investors' investments in financial instruments was carried out. Settlements were reached with two supervised entities. The first pertained to the entity's selling and marketing to retail investors without having fulfilled its obligations regarding measures to prevent conflicts of interests, information disclosure, classification of customers, and assessment of their suitability. The second case centred on the entity's failure to enter and store data.

Furthermore, staff involved with supervision of business conduct devoted considerable time to the incorporation of EU regulations and directives into Icelandic law during the year, as well as participating in various committees established by European supervisory bodies.

### **Supervision of UCITS management companies, UCITS funds, and alternative investment fund management companies**

The Central Bank carries out supervision of UCITS management companies, UCITS funds, and alternative investment fund management companies. Such supervision revolves mainly around whether or not the funds in question invest in accordance with statutory authorisations and their own internal rules. Factors such as UCITS funds' risk management, conflicts of interests, and liquidity management are monitored as well, as are the obligations of fund custodians. During the year, the Bank processed a large number of applications from non-EEA management companies seeking authorisation to market alternative investment funds in Iceland. In addition, UCITS funds' costs and fees were examined in connection with a common supervisory action.

## **On-site inspections**

On-site inspections are conducted in support of regular monitoring of supervised entities. They are among the methods the Central Bank uses to carry out its legally mandated role. The aim of on-site inspections is to analyse risks in supervised entities' activities in depth and evaluate their business plans, governance practices, and internal controls. Decisions about on-site inspections are based on supervised entities' impact category, as well as supervision emphasis at each time. Supervised entities' size, activities, and risk profile are also taken into account.

The COVID-19 pandemic continued to make some impact on the on-site inspections planned for the year, in that some of them could not be carried out on the entities' premises and instead were conducted in part via remote meetings held with representatives of the entities concerned.

A total of 24 on-site inspections were completed in 2021. Continued emphasis was placed on supervised entities' anti-money laundering and terrorist financing measures, as well as credit risk, operational risk, governance practices, and internal controls in supervised entities' activities.

## Suitability assessments, qualifying holdings, and operating licences

### Assessment of board members' and senior executives' fitness and suitability

The Central Bank assesses the suitability and qualifications of supervised entities' board members and managing directors. A suitability assessment is carried out when board members and managing directors begin work for supervised entities, although the Bank may reassess the suitability if necessary. However, the entities concerned are always responsible for ensuring that their board members and managing directors satisfy the regulatory requirements for eligibility.

The Bank assessed the suitability of 94 board members and managing directors in 2021. The majority of the assessments focused on board members. The suitability assessments that were postponed in 2020 due to the COVID-19 pandemic were largely completed in 2021. Nevertheless, because of the pandemic, it was still not possible to interview all of the board members concerned, and those assessments could not be completed by the year-end. They are scheduled for completion in H1/2022.

### Qualifying holdings

The Central Bank assesses the eligibility of parties intending to acquire qualifying holdings in supervised entities. Ownership of supervised entities remained broadly unchanged in 2021. One notification of a qualifying holding in three insurance companies during the year.

### Operating licences and other permits

There were several changes relating to supervised entities' operating licences in 2021. The Bank granted a company a licence to operate as an electronic money institution but simultaneously revoked the same company's licence to operate as a payment institution. In addition, the merger of three companies in the financial market and the establishment of a financial conglomerate was approved. Five new alternative investment fund managers were registered during the year. Two investment firms, one UCITS management company, and one alternative investment fund management company were

granted expanded operating licences. Furthermore, the operating licences of three UCITS management companies were revoked, while the same companies retained their licences to operate as alternative investment fund managers. One insurance company's operating licence was revoked, two alternative investment fund managers were deregistered, and one collections licence was cancelled.

## Anti-money laundering and terrorist financing measures

The Central Bank carries out risk-based supervision of entities subject to notification requirements (obliged entities) in accordance with the Act on Measures Against Money Laundering and Terrorist Financing. There were 95 such obliged entities at the end of 2021.

The Bank carried out a number of supervisory actions, including eight on-site inspections and other follow-up checks on risk assessments and risk-based measures taken by supervised entities. The Bank also began during the year to take interviews with obliged entities' money laundering reporting officers to discuss anti-money laundering and terrorist financing measures. Furthermore, it issued a list of occupations classified as high-level public positions in connection with its assessment of politically exposed persons. In addition, the Bank issued educational materials on risk-based and preventative anti-money laundering and terrorist financing measures during the year, and held educational meetings for obliged entities.

## Cases concluded with sanctions in 2021

In 2021, the Central Bank concluded four cases involving violations by reaching a settlement with the parties concerned. When a settlement is reached, the party involved acknowledges having violated statutory provisions or decisions taken by the Bank's financial supervisory authority, provides full information on the violation, and makes an agreement with the Bank on payment of a fine to the Treasury. In the four cases concluded by settlement, the fines ranged from 700,000 kr. to 18 m.kr. In one case, the party agreed to take specified remedial action within a specified time limit, in accordance with the Bank's demands. More detailed discussion of sanctions and other related matters can be found in the Bank's annual *Financial Supervision* report.





Financial Supervision Committee, 2021. Seated, from left: Gunnar Jakobsson, Deputy Governor for Financial Stability; Ásgeir Jónsson, Governor; and Unnur Gunnarsdóttir, Deputy Governor for Financial Supervision. Standing, from left: Guðrún Thorleifsdóttir, Director General, Ministry of Finance and Economic Affairs; Andri Fannar Bergthórsson, Assistant Professor, Reykjavik University; Ásta Thórarinsdóttir, Economist; and Guðrún Finnborg Thórdardóttir, Committee secretary. Governor Ásgeir Jónsson takes a seat on the FMEN as its chair when the Committee takes decisions on the adoption of rules of procedure and on the transfer of authority to the Deputy Governor for Financial Supervision, as well as decisions pertaining to systemically important financial institutions' capital, liquidity, and funding. In those cases, Deputy Governor Unnur Gunnarsdóttir serves as vice-chair. Otherwise, Unnur Gunnarsdóttir chairs the Committee and Gunnar Jakobsson serves as vice-chair.

# Other tasks



## International reserves

### Role of the reserves

The Central Bank of Iceland maintains international reserves in accordance with its objectives and role as described in Act no. 92/2019. The international reserves comprise the Bank's holdings in foreign currencies; i.e., foreign bank deposits, bonds, special drawing rights and deposits with the International Monetary Fund (IMF), gold, and other foreign assets.

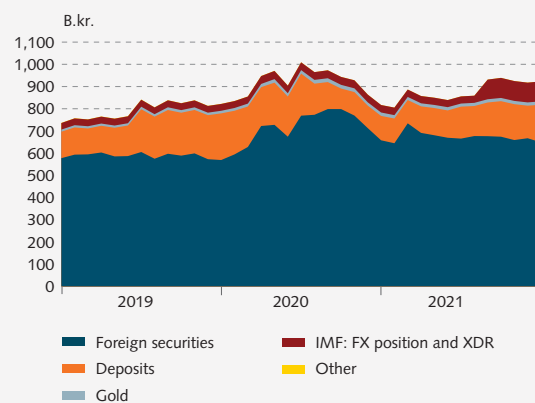
The role of the reserves is fourfold: first, to mitigate volatility in Iceland's balance of payments; second, to reduce the likelihood that movement of capital to and from Iceland will compromise financial stability; third, to play a part in the Treasury and Central Bank's management of assets and liabilities, so that the Icelandic Government can service its foreign debt, pay foreign expenses, and honour other international obligations; fourth, to serve as a reserve fund that can be tapped in the event of shocks.

At any given point in time, the optimum size of the international reserves is determined by Iceland's external debt, monetary policy, financial system structure and position, scope of international trade, and capital flows to and from the country.

### Developments in the reserves in 2021

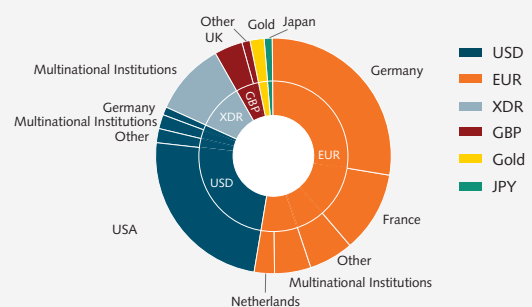
At the end of 2021, the international reserves totalled 923 b.kr., the equivalent of 7.1 billion US dollars. The reserves had grown by 106 b.kr. during the year. The main reason for the increase is the Treasury's issuance of a eurobond in the amount of 750 million euros, and the International Monetary Fund's (IMF) allocation of special drawing rights (SDR) equivalent to 55 b.kr. in

Chart V-1  
International reserves



Source: Central Bank of Iceland.

Chart V-2  
Reserve assets by currency and issuer/counterparty country



Source: Central Bank of Iceland.



August. These were offset by foreign exchange market intervention equivalent to 23 b.kr. (net foreign currency sales) and instalments on Treasury foreign loans in the amount of 2 b.kr. At the end of the year, the international reserves totalled 29% of GDP and 39% of broad money holdings (M3), and they covered nine months' worth of goods and services imports.

### Returns and interest income

Returns on the management of the reserves were negative in the amount of 28 b.kr. in 2021, owing mainly to the appreciation of the króna. The recognised exchange rate difference was negative by 19 b.kr. Interest income on the reserves was positive by 2 b.kr., and recognised changes in the market value of securities reduced the reserves by 10 b.kr. During the year, the return on bonds and deposits was negative by 1%, excluding the effects of exchange rate differences.

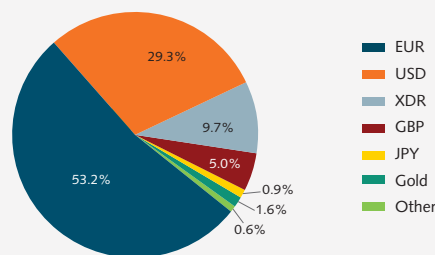
### Reserve maintenance

The Rules on Reserve Maintenance are adopted with reference to Article 3, Paragraph 3 and Article 30, Paragraph 1 of Act no. 92/2019. They are set by the Governor and Deputy Governors. The rules contain provisions on key points concerning reserve maintenance, including purpose, structure, investment authorisations, and outside limits of acceptable risk.

In maintaining and investing the international reserves, the Central Bank takes risks that must be managed. The most important risk lies in the possibility that the Bank will be unable to use the reserves to achieve its objectives or carry out its role as a central bank. Foreign exchange risk, on the other hand, is the risk that has the greatest impact on the Bank's balance sheet. The reserves are in foreign currencies, while most of the Bank's liabilities are in Icelandic krónur. As a result, exchange rate movements strongly affect the Bank's income and expenses, as well as the value of assets and liabilities calculated in krónur. However, the value in krónur terms is of minor importance in comparison with the above-described risk and given the role of the reserves.

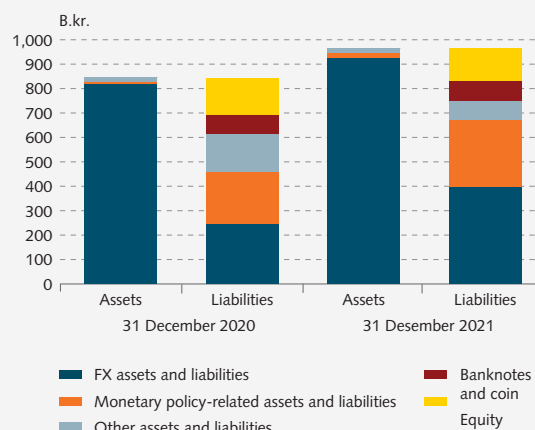
Foreign securities accounted for 70% of the international reserves at the end of 2021. Deposits comprised 18% of the reserves, the vast majority of them held in central banks. The Bank's gold holdings, which were unchanged year-on-year in volume terms, were valued at 15.2 b.kr., or about 1.6% of the reserves, at the end of 2021. The Bank's foreign exchange balance – i.e., its foreign-denominated assets net of foreign-denominated liabilities – was positive by 529 b.kr., the equivalent of 4.1 billion US dollars, at the end of 2021.

Chart V-3  
Foreign exchange balance by currency



Source: Central Bank of Iceland.

Chart V-4  
Central Bank of Iceland balance sheet



Source: Central Bank of Iceland.

Issuers must have a credit rating of at least AA in order for their securities to be classified as highly liquid assets. For the purposes of reserve management, highly liquid assets include bonds denominated in US dollars or euros and issued by the state in the state's own currency, and deposits with the central banks in these countries/regions or the Bank for International Settlements. Highly liquid assets accounted for 59% of the Central Bank's foreign exchange reserves at the end of 2021.

Chart V-2 gives a breakdown of reserve assets by country and currency as of end-2021. Further discussion of the management of the Bank's financial risk can be found in the notes to the financial statements.

## Government debt management

### Agreement on Treasury debt management

In accordance with an agreement made with the Ministry of Finance and Economic Affairs, the Central Bank of Iceland oversees Treasury foreign borrowing;

conducts domestic auctions, buybacks, and Treasury bond redemptions; executes primary dealer agreements; and oversees securities lending to primary dealers. The Bank handles risk management, debt management, and information disclosure on Treasury debt. Under the agreement, the Bank handles tasks relating to issuance of marketable Treasury securities and Treasury guarantees and relending. The Bank also oversees issuance of bonds for Treasury relending.

### Domestic debt management

The Government Debt Prospect for 2021 assumed that Treasury issuance would total 200 b.kr. According to the Government's fiscal plan for 2022-2026, published in Q1/2021, it was clear that the Treasury's position was stronger than had been anticipated when the previous fiscal plan was prepared. In view of this, it was decided to lower the Treasury bond issuance target from 200 b.kr. to 180 b.kr. market value. At the end of the year, Treasury issuance totalled 152.1 b.kr. in nominal terms, or 179.7 b.kr. market value.

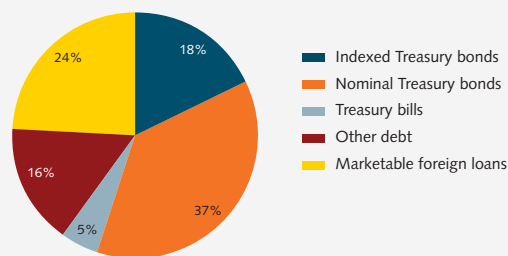
Treasury bond series RIKB 21 0805 matured during the year, with an outstanding amount of 47 b.kr. The issuance of a new two-year Treasury series, RIKB 24 0415, was expedited by one year in order to meet the Treasury's increased financial need. The response to the bond was favourable, and the outstanding stock in the series totalled 44 b.kr. market value at the year-end.

Uncertainty about the negative impact of COVID-19 on the domestic economy subsided markedly in Q1/2021, with the publication of the 2022-2026 fiscal plan indicating that the Treasury was stronger than previously assumed. Uncertainty also declined with the roll-out of vaccinations against the virus in Iceland and abroad, boosting expectations that the domestic tourism industry would begin to recover over the course of the year. This boosted optimism among market agents, as the vaccinations appeared to deliver the intended results and it was decided to allow visitors from outside the Schengen area to come to Iceland. Continued supply-chain disruptions, higher shipping costs, rising energy and commodity prices, and soaring house prices pushed inflation higher, dampening this optimism. Inflation proved persistent, rising from 4.3% at the beginning of 2021 to 5.1% at the year-end.

### Foreign debt management

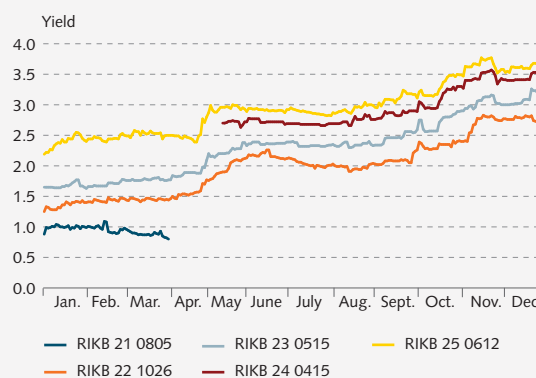
According to the Medium-Term Debt Management Strategy for 2021-2025, new Treasury loans taken in foreign currencies are used mainly to expand the Central Bank's international reserves, to refinance outstanding

Chart V-5  
Brakedown of Government debt  
31 December 2021



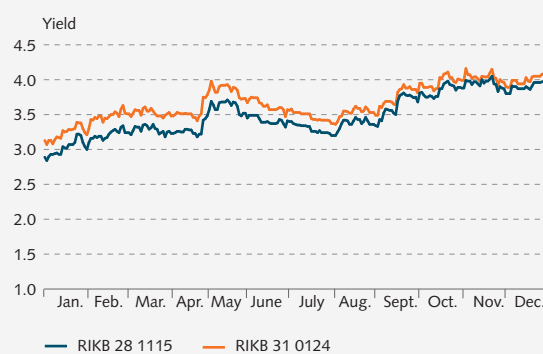
Source: Central Bank of Iceland.

Chart V-6  
Nominal Treasury bonds longer than 5 years



Source: Central Bank of Iceland.

Chart V-7  
Nominal Treasury bonds longer than 5 years



Source: Central Bank of Iceland.

market issues, and to maintain access to foreign credit markets.

In 2021, the Treasury issued a foreign-denominated bond in the amount of 750 million euros. The bonds bear 0% fixed interest and were issued for seven years at a yield of 0.1177%.

### State guarantees

The Central Bank of Iceland handles tasks relating to Treasury guarantees and the State Guarantee Fund. The State Guarantee Fund oversees State guarantees and is tasked with keeping abreast of the activities of entities that have received State guarantees and maintaining a record of the obligations bearing such guarantees. The majority of State guarantees derive from the Government's holding in the Housing and Construction Authority. Parties that enjoy State guarantees due to Government ownership are required to obtain the Central Bank's approval of the terms and conditions for loans they intend to take abroad. Treasury guarantees totalled 845 b.kr. at the end of 2021, as opposed to 897 b.kr. at year-end 2020.

## International co-operation

The Central Bank of Iceland communicates and conducts transactions with international institutions in its field. Because of the COVID-19 pandemic, meetings with all of the Bank's partner institutions were held remotely during the year.

### International Monetary Fund

The Central Bank formally represents Iceland at the International Monetary Fund (IMF). A mission from the IMF held its annual Article IV consultation with the Icelandic authorities in May, focusing on economic developments and prospects and the response to the pandemic. The mission's annual report on Iceland was discussed by the Fund's Executive Board and published in June. All of the IMF's reports on its regular monitoring of the Icelandic economy are published on the Fund's website and that of the Central Bank.

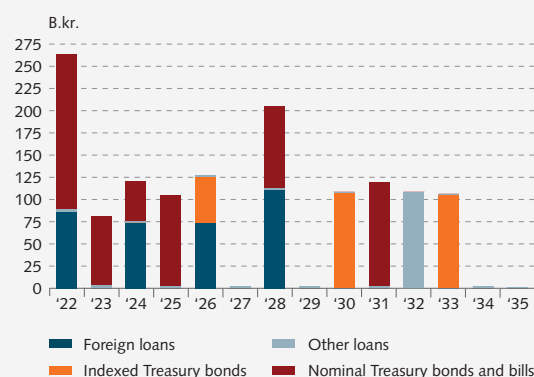
Iceland collaborates with the Nordic and Baltic countries at the IMF and forms a Constituency with them. These countries together elect one permanent representative to the Executive Board, which comprises 24 members. The Constituency's representative on the Executive Board in 2021 was Mika Pösö from Finland. Each year, the Nordic-Baltic office compiles a report on the salient issues on the agenda of the Fund and the Executive Board during the year, including the

Chart V-8  
Inflation linked Treasury Bonds



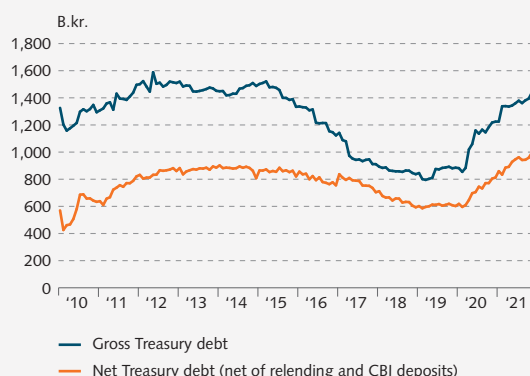
Source: Central Bank of Iceland.

Chart V-9  
Redemption profile of government debt

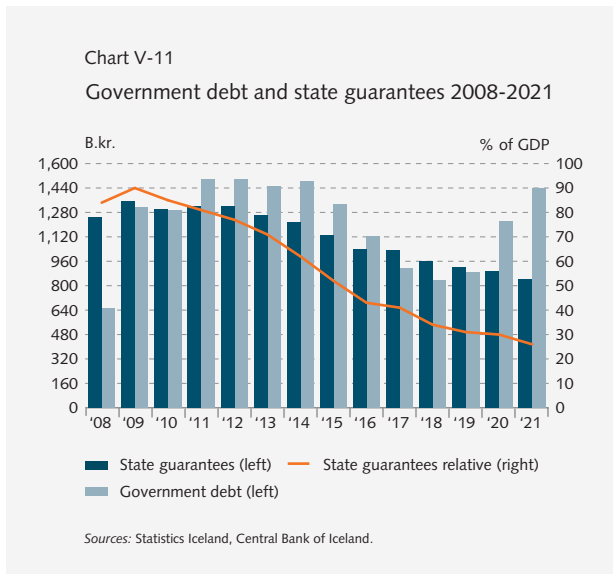


Source: Central Bank of Iceland.

Chart V-10  
Treasury debt development



Source: Central Bank of Iceland.



Constituency's views on them. These reports are published on the Central Bank website.

The Fund's International Monetary and Financial Committee (IMFC), which generally holds two meetings a year, met twice in 2021. The Governor of the Central Bank is Iceland's representative on the IMF Board of Governors, which convenes each year at the Fund's annual meetings. All meetings were held remotely during the year.

### Bank for International Settlements

The Central Bank is a shareholder in the Bank for International Settlements (BIS) in Basel, Switzerland, and participates in a range of collaborative work through the BIS. During the year, the Governor participated in both the BIS annual meeting and the regular governors' meetings, which are held every other month. All of the meetings were held remotely.

In 2021, the BIS established the Innovation Hub Nordic Centre in Stockholm, in cooperation with the central banks of Iceland, Sweden, Norway, and Denmark. The Central Bank will contribute one employee to the Centre. The BIS Innovation Hub Nordic Centre's role is to act as a forum for innovation in the fintech sector, research on fintech trends and currents of significance for central bank activities, and the furtherance of international cooperation aimed at bolstering global financial system efficacy.

### Organisation for Economic Co-operation and Development (OECD)

The Central Bank of Iceland participates in the work of the Organisation for Economic Co-operation and Development (OECD). Experts from the OECD also visit Iceland regularly in order to acquaint themselves with economic developments, and they issue a biennial report on Iceland. The last OECD report was published in July 2021.

### Network for Greening the Financial System

The Central Bank of Iceland is a member of the Network for Greening the Financial System (NGFS) and participates actively in its work. The NGFS is a worldwide network of central banks and financial supervisors that have declared their willingness and commitment to working together to promote and develop best practices for managing climate- and environment-related risk in the financial sector and to promote sustainable and environment-friendly investment.

### Collaboration in connection with financial supervision

The Central Bank of Iceland participates in the work of European financial supervisory bodies, including the European Banking Authority (EBA), the European Insurance and Occupational Pensions Authority (EIOPA), and the European Securities and Markets Authority (ESMA). In these fora, the Bank has the same rights and responsibilities as the supervisory authorities in EU member countries but does not have voting rights. Participation in the Board of Supervisors, permanent committees, and work groups of European supervisory bodies enables the Bank to keep abreast of legislative amendments and participate in developing European financial market legislation. With its participation, the Central Bank also does its part to ensure harmonised implementation of European financial market legislation in the EEA. Participation also underpins the implementation of new European legislation in Iceland, facilitates it, and contributes to more effective supervision after implementation is complete.

The Bank participated actively in international cooperation on measures to combat money laundering and terrorist financing, including through EBA committees and a task force representing the Nordic and Baltic financial supervisory authorities.

The Central Bank also collaborates with other Nordic supervisory bodies in a task force entrusted with harmonising supervision of the Nasdaq securities exchanges in the Nordic region. The task force's chief role, in addition to conducting proactive investigations, is to assess and monitor key risks in the exchanges' operations.

### Cooperation in connection with financial stability

The Central Bank participates in the work of the European Systemic Risk Board (ESRB) and subgroups on its behalf, and thus has access to European analyses of systemic risk. The Governor attends meetings of the ESRB as an auditing member.

Furthermore, the Central Bank participates in the work of the Financial Stability Board (FSB), a cooperative forum for global financial stability.

The Bank also takes an active part in Nordic-Baltic cooperation, including through the Nordic-Baltic Macroprudential Forum, where the countries in the region exchange information on developments in systemic risk and the application of macroprudential tools. Moreover, the Bank participates with the Ministry of Finance and Economic Affairs in the activities of the Nordic-Baltic Cross-Border Stability Group, whose role is to coordinate responses to financial shocks affecting more than one country and to share information on financial stability among the institutions in the Nordic-Baltic region.

As in previous years, the Bank participated actively in international cooperation on developments in payment intermediation, including on interbank systems, digital cash, and cybersecurity.

## Cash

At the end of 2021, cash issued by the Central Bank of Iceland amounted to 82.0 b.kr., including 77.6 b.kr. in banknotes and 4.4 b.kr. in coin. Cash issued by the Central Bank is recorded on the liabilities side of the Bank's balance sheet. Table 3 in the Appendix shows the breakdown by banknote and coin denomination.

Discussions of cash in circulation usually refer to cash outside deposit institutions and the Central Bank. The difference between this figure and the total in Table 3 in the Appendix, called the overnight cash balance, consists of cash on the assets side of deposit institutions' balance sheets at the close of business. At the end of 2021, deposit institutions' overnight cash balance was 7.7 b.kr. Cash in circulation outside deposit institutions and the Central Bank (i.e., held by companies, individuals, etc.) totalled 74.3 b.kr. at the end of 2021, an increase of 0.6 b.kr., or 0.8%, between years. Use of cash declined in 2020 and 2021 because of the COVID-19 pandemic, as can be seen in the significant reduction in the number of unfit banknotes relative to prior years. In 2021, the Bank destroyed 1.9 million notes that were considered unfit for use, as opposed to 2.9 million in 2020.

At the end of 2021, there were 15.7 million banknotes in circulation in Iceland.

## Jóhannes Nordal cultural heritage grants

The cultural heritage grant in the name of former Central Bank Governor Jóhannes Nordal was awarded for the tenth time on 10 June 2021. A total of 29 applications were received, and grants were awarded to three projects.

Skáldaskinna ehf. received 1.6 m.kr. for the project skáld.is, a website devoted to women and their writings. The aim of the project is to gather information on Icelandic women's literature in once place and maintain an ongoing repository of information on the lives and works of Iceland's female poets and authors.

Ásta Soffía Thorgeirsdóttir received 1.4 m.kr. for the project Blómaskeid íslenska tangósins á 20. öldinni, which entails documenting the heyday of tango music composition in Iceland, which began after World War II and continued in the latter half of the twentieth century.

Prentsögusetur received 1 m.kr. for the project Thróun bókagerdar á Íslandi 1535-1877, an exhibition of tools and equipment for book making, typesetting, printing, and bookbinding. Small tools and equipment will be on display at the exhibition site, and developments in book making in Iceland will be explained via a collection of photographs, drawings, and videos. The project is the joint endeavour of Skálholt and Prentsögusetur.

# Management, and organisation



## Central Bank management

During the year, Ásgeir Jónsson served as Governor of the Central Bank. He was appointed for a term of five years beginning on 20 August 2019. The Governor directs and is responsible for the Bank's activities and operations and is authorised to take decisions on all matters not entrusted to others by law.

In 2020, Rannveig Sigurdardóttir was Deputy Governor for Monetary Policy, Unnur Gunnarsdóttir was Deputy Governor for Financial Supervision, and Gunnar Jakobsson was Deputy Governor for Financial Stability. The Deputy Governors oversee the Bank's affairs in the areas they are appointed to lead, under the direction of the Governor.

Decisions on reserve management and the grant of guarantees or loans to credit institutions in liquidity difficulties are taken by the Governor and Deputy Governors at a meeting called by the Governor, as is provided for in Article 3, Paragraph 3 of the Act on the Central Bank of Iceland, no. 92/2019. Decisions on setting rules on special reserve requirements for new foreign currency inflows on the basis of the Foreign Exchange Act, decisions on setting rules on the operation of regulated foreign exchange markets, and decisions on organisation and the setting of rules on the Bank's activities are taken in the same manner.

## Supervisory Board

The Supervisory Board monitors the Bank's compliance with the statutory provisions applying to its activities. In other respects, the Board undertakes such tasks as are outlined in Article 8 of the Central Bank Act. The Board must be elected after each Parliamentary election.

In 2021, the Bank's Supervisory Board was chaired by Gylfi Magnússon. Other members were Thórunn Gudmundsdóttir (vice-chair), Bolli Hédinsson, Una María Óskarsdóttir, Sigurdur Kári Kristjánsson, Jacqueline Clare Mallett, and Frosti Sigurjónsson. Thórlindur Kjartansson, Jóhanna Vigdís Gudmundsdóttir, Hildur Traustadóttir, Vilborg Sveinsdóttir, Kristín Thoroddsen, Ólafur Margeirsson, and Bára Ármannsdóttir served as alternates. The Supervisory Board held 12 meetings over the course of 2021.

## Central Bank committees

The Monetary Policy Committee (MPC) takes decisions on the application of the Bank's monetary policy instruments. These decisions must be based on the Bank's price stability objective and a thorough assessment of economic and monetary developments and prospects. The Committee takes interest rate decisions in support of the Bank's monetary policy objectives. It also takes decisions on transactions with credit undertakings other than loans of last resort. Furthermore, the Committee takes decisions on minimum reserve requirements, foreign exchange market transactions, and securities transactions undertaken with the aim of achieving the Bank's price stability objectives.

In 2021, MPC members were Governor Ásgeir Jónsson, who chairs the Committee; Rannveig Sigurdardóttir, Deputy Governor for Monetary Policy and vice-chair; Gunnar Jakobsson, Deputy Governor for Financial Stability; Gylfi Zoëga, professor at the University of Iceland; and Katrín Ólafsdóttir, Associate Professor at Reykjavík University.



The Central Bank Financial Stability Committee (FSN) takes decisions on the application of the Bank's financial stability policy instruments. Decisions taken by the Financial Stability Committee must be based on the law and on a thorough assessment of the current situation and outlook for the financial system. The tasks of the FSN are: (a) to assess developments and prospects for the financial system, systemic risks, and financial stability; (b) to define and discuss the measures deemed necessary at any given time to affect the financial system so as to strengthen and preserve financial stability, and submit comments to the relevant authorities when warranted; (c) to approve Government directives and take decisions with which the Committee is entrusted by law; and (d) to determine which supervised entities, infrastructure elements, and markets shall be designated as systemically important and of such a nature that their activities could affect financial stability.

Members of the Financial Stability Committee in 2021 were Governor Ásgeir Jónsson, who chaired the Committee; Gunnar Jakobsson, Deputy Governor for Financial Stability, who served as vice-chair; Rannveig Sigurdardóttir, Deputy Governor for Monetary Policy; Unnur Gunnarsdóttir, Deputy Governor for Financial Supervision; Axel Hall, Assistant Professor at Reykjavík University; Bryndís Ásbjarnardóttir, Economist at Statistics Iceland; and Gudmundur Kristján Tómasson, former Director of Financial Market Infrastructure at the Central Bank of Iceland. The Permanent Secretary or an appointed official from the Ministry responsible for financial stability, currently the Ministry of Finance and Economic Affairs, also participates in Committee meetings and has the right to address the meeting and present proposals.

The Financial Supervision Committee (FMEN) takes decisions entrusted to the financial supervisory authority by law or Governmental directives. The Committee is authorised to entrust the Deputy Governor for Financial Supervision with taking non-major decisions.

During the year, members of the FSN were Ásgeir Jónsson, Governor; Unnur Gunnarsdóttir, Deputy Governor for Financial Supervision; Gunnar Jakobsson, Deputy Governor for Financial Stability; Andri Fannar Bergthórsson, Assistant Professor at Reykjavík University; Ásta Thórarinsdóttir, Economist; and Gudrún Thorleifsdóttir, Director General at the Ministry of Finance and Economic Affairs. When decisions specified in Article 15, Paragraph 2 of the Act on the Central Bank of Iceland are taken, Governor Ásgeir Jónsson takes a seat on the Committee as its chair. In those cases, Unnur Gunnarsdóttir, Deputy Governor for Financial Supervision, acts as vice-chair. In other

instances, Unnur Gunnarsdóttir chairs the Committee and Gunnar Jakobsson, Deputy Governor for Financial Stability, acts as vice-chair.

## Organisational structure

According to the organisational chart, the Bank has seven core departments: Economics and Monetary Policy; Treasury and Market Operations; Financial Stability; Banking; Pensions and Insurance; Markets and Business Conduct; and Compliance and Inspections. There are four support departments: Operations, Information Technology and Statistics, Finance, and Human Resources. The organisational chart also includes the centralised General Secretariat. Each department is overseen by a departmental director.

The Supervisory Board oversees internal audit for the Bank and engages the Internal Auditor, as is provided for in Article 8, Item (d) of the Central Bank Act.

## Departmental tasks

The General Secretariat oversees the affairs and activities of the Bank and formulates and enforces its policies, in cooperation with other departments. It provides advice and services to the Governor, Deputy Governors, Supervisory Board, committees, and departments of the Bank. The department's tasks include legal advice; preparation of rules; regulatory compliance; communications with ministries, Parliament, and other domestic institutions; processing of and follow-up on communications and queries received by the Bank; oversight of presentations and information disclosure by the Bank; and editorial and oversight of the Bank's *Annual Report*, website, and social media. Oversight of the Bank's own risk is carried out by the General Secretariat's Risk Management team, which is led by the Risk Officer. The Bank's Security Officer is an employee of the Risk Management unit. The General Secretariat also handles international cooperation, including with the International Monetary Fund. Furthermore, it oversees the publication of *Kalkofn*, a web-based publication containing papers and articles by Bank staff members.

The Economics and Monetary Policy Department carries out economic and monetary research, prepares macroeconomic and inflation forecasts, participates in formulating policy in monetary and exchange rate matters, and analyses developments in domestic and foreign economic and monetary affairs, including the macroeconomic elements of financial stability. The Department oversees the issuance of various Bank publications,



including *Peningamál/Monetary Bulletin*, *Hagvísar/Economic Indicators*, and *Working Papers*. The department also oversees a range of projects relating to the work of the Bank's Monetary Policy Committee.

The Markets Department oversees the domestic money market and currency market, as well as transactions with domestic financial institutions. It also manages the Bank's balance sheet, handles the custody and investment of the international reserves, and manages Treasury debt, Treasury guarantees, and Treasury re-lending. The Department also oversees communications with the foreign financial institutions with which the Central Bank and the Treasury conduct business. It handles securities administration, payments for securities transactions, and payments in connection with borrowing and swap agreements. Furthermore, it administers the Bank's interbank payment system and SWIFT system, as well as overseeing domestic and cross-border payments for the Bank, the Treasury, and State enterprises.

The Financial Stability Department analyses financial system risks, monitors credit institutions' liquidity and foreign exchange balance, and participates in formulating prudential rules for the financial system. The department also oversaw the Foreign Exchange Act, the Act on the Treatment of Króna-Denominated Assets Subject to Special Restrictions, until it was repealed. In addition, it monitors the position of credit institutions, households, and businesses; payment flows to and from Iceland; and the external position of the economy. Moreover, the department monitors systemically important financial market infrastructure. The Bank's resolution authority is part of the Financial Stability Department. The department publishes the Bank's *Financial Stability* reports and oversees a variety of projects relating to the work of the Bank's Financial Stability Committee.

The Banking Department monitors the activities of commercial banks, savings banks, credit institutions, investment firms, and payment institutions. The department's primary tasks centre on the supervisory review and evaluation process. This includes assessments of capital and liquidity requirements; reviews of recovery plans; analysis and assessment of risks in supervised entities' operations; and communications with boards of directors, senior management, and external auditors. The Banking Department works with the Financial Stability Department on systemic risk assessments.

The Pensions and Insurance Department monitors the activities of insurance companies, pension funds, and private pension savings custodians. This entails, on the one hand, regular monitoring of insurance companies in accordance with the Bank's risk-based supervision model,

which defines the frequency with which key risk factors in the companies' operations are examined; and on the other hand, proactive checks carried out based on the circumstances in each given instance. The department analyses key risks and developments in the markets and monitors closely to ensure that the entities concerned satisfy the requirements for their operating licences, that their operating practices are in compliance with regulatory provisions, and that appropriate measures are taken at all times. It reviews insurers' own risk and solvency assessments (ORSA) and pension funds' own risk assessments, for example, and interviews key employees.

The Markets and Business Conduct Department supervises entities in the securities market, including issuers of financial instruments, securities exchanges, central securities depositories, fund management companies, and alternative investment funds. The department also oversees transactions and conduct in the securities market (market abuse and insider trading). One of the tools it uses for this is an automated monitoring system that analyses transactions based on data submitted by financial institutions. Markets and Business Conduct also oversees consumer affairs, investor protection, and the business conduct of supervised financial market entities. Monitoring of business conduct and investor protection entails, among other things, ensuring that supervised entities' customers are sold appropriate products and services, that information provided to them is neither misleading nor deceptive, and that action is taken in response to potential conflicts of interests.

The Compliance and Inspections Department works across other Bank departments involved in financial supervision. It conducts fitness and suitability assessments of supervised entities' managing directors and board members, grants and revokes operating licences, and processes notifications of qualifying holdings and applications for approval of mergers. The department also carries out on-site inspections with the aim of thoroughly analysing risks in supervised entities' activities and evaluating their internal controls, business plans and governance practices. Furthermore, it monitors obliged entities' measures to combat money laundering and terrorist financing.

The Operations Department carries out tasks involving the Bank's internal operations and the service it provides. Among these tasks are operation and administration of the Bank's real estate and oversight of modifications to the Bank's premises; oversight of and responsibility for specified security matters; purchasing for all Bank departments; expenditure control, including budget preparation; cafeteria and catering; manage-

ment of the Bank's records in compliance with the Act on Public Archives; implementation of a digital work environment; and operation of the Bank's library and numismatic collection.

The Finance Department oversees the Bank's financial information and that of companies owned by the Bank, as well as handling accounting for the National Festival gift from Norway and the Greenland Fund, which are administered by the Bank. It enters, processes, and discloses information in accordance with standard accounting and financial reporting practices and handles payroll processing for the Bank. The department also handles the administration of banknotes and coin and operates the Bank's vaults.

The Information Technology and Statistics Department oversees and is responsible for the development, architecture, and operation of the Bank's information systems. It also handles the gathering, entry, and processing of statistics collected by the Bank, both for its own activities and for official statistical reporting. The Bank systematically collects information on the domestic credit market, the balance of payments, and the external position of the economy. These data form the basis for the Bank's assessment of important aspects of monetary developments and the financial system, and for regular disclosure of statistical information on its website and in its publications. The Bank publishes statistical information on the Statistics pages of its website.

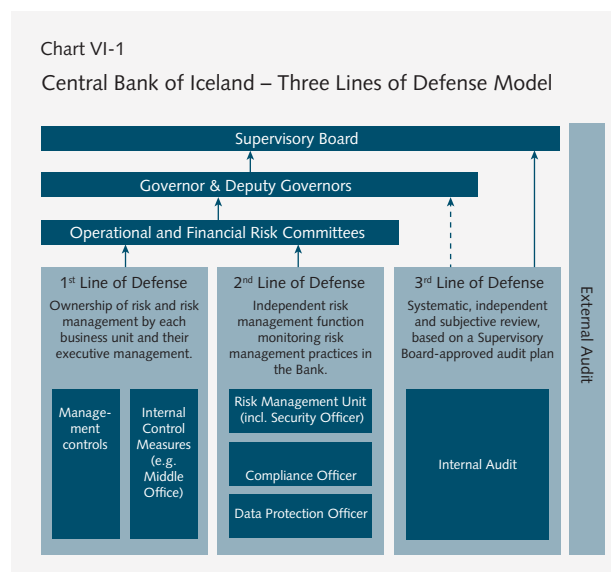
The Human Resources Department is responsible for supporting the Bank's human resources policy at all times. The department's objective is to ensure harmonised implementation of personnel policies and provide targeted advice to management and employees so as to build up a workplace characterised by trust, professionalism, knowledge, and progressiveness. The main tasks of Human Resources are to manage staff recruitment and hiring, termination of employment, staff training, job development, workplace analysis and other analytical work, feedback interviews, decisions on remuneration, employee health and well-being, and equal rights.

The Internal Audit Department operates under the oversight of the Supervisory Board and is accountable to the Board for its activities.

## Internal audit and risk management

The Central Bank's activities entail financial and operational risk of various types, including risks that could make it more difficult, or even impossible, to carry out its role and achieve its legally mandated objectives satisfactorily, and risks stemming from the fact that these

objectives take priority over profit considerations and the Bank's own financial interests. The Bank's risk policy aims to define more fully the risk the Bank faces, enhance understanding of that risk, gain an overview of it, and manage or minimise it without sacrificing the Bank's ability to achieve its legally mandated goals. Bank officers, the Risk Management team, and Internal Audit form three lines of defence in terms of internal monitoring, as can be seen in Chart 1.



The Governor appoints a Financial Risk Council and an Operational Risk Council, which are responsible for the risk management framework, as well as acting as advisors to the Governor and helping the Governor to carry out his role in ensuring effective risk management.

The Governor hires a Risk Officer who is tasked with leading the independent Risk Management team within the General Secretariat and is responsible for ensuring that the Bank operates in accordance with the risk management framework set by the Financial Risk Council and the Operational Risk Council. The Risk Management team commenced operation in 2021, after the Risk Officer was hired.

Departmental directors are responsible for risk in their own departments and for managing such risk.

The Internal Auditor, who operates under the auspices of the Supervisory Board, conducts systematic, impartial, and objective assessments of the efficacy of the risk management, internal monitoring, and governance practices of the Central Bank. Internal Audit operates in accordance with a risk-based audit plan that is confirmed by the Supervisory Board and updated on a regular basis.

Financial risk consists of market risk, liquidity risk, and claims risk. Market risk is due mainly to exchange

rate and interest rate risks deriving from revaluation of securities owned by the Bank, as well as interest rate mismatches between assets and liabilities. Changes in exchange rates and market yields directly affect equity, and both the composition of interest-bearing assets and liabilities and developments in the associated interest rates affect future income. In order to understand this risk, the Bank carries out scenario analyses and stress tests, among other things, so as to assess the sensitivity of assets and liabilities to various market events. The Financial Risk Council carries out monitoring to ensure that risk in the Bank's balance sheet is consistent with its risk appetite. The Council also advises on measures to mitigate risk and enhance the balance sheet's resilience to decisions relating to the Bank's legally mandated objectives. Furthermore, the Council reviews the Bank's environmental, social, and governance (ESG) priorities.

Operational risk – the risk of financial or non-financial losses stemming from inadequate internal processes and systems, human error, or external events – is associated with the Central Bank's activities as a central bank and as the operator of systemically important financial market infrastructure; i.e., the interbank payment system. The Operational Risk Council oversees the operational risk management system and conducts monitoring to ensure that there are documented procedures for the Bank's most important tasks, that risk assessments are carried out on key procedures and computer systems, and that remedial action is taken swiftly when deviations from set procedures occur.

## Human resources

At the end of 2021, the Central Bank employed 294 members of staff in 291.9 full-time position equivalents. At the end of the year, the Bank employed 143 women and 151 men.

There were 13 departmental directors: seven men and six women. In addition, there were 26 deputy directors and unit heads: 12 women and 14 men. At the year-end, 89% of the Bank's staff were university-educated. Fourteen new employees were hired during the year, and 18 left the Bank. There were 13 summer employees in 2021.

At the end of the year, the Central Bank-owned company Greidsluveitan ehf. employed five members of staff: three men and two women.

The equal pay analysis conducted during the year showed that there was no unexplained wage gap between the sexes at the time.

## Construction and renovation

Work continued on moving all of the Bank's activities into its premises at Kalkofnsvegur in Reykjavík, following the merger with the Financial Supervisory Authority at the beginning of 2020. Renovation and maintenance continued, with the aim of opening up space to make it available for more efficient use. Construction work was completed on the second and third floors of the Bank's headquarters and was well advanced on the fourth and fifth floors. The offices at Katrínartún, previously used by the Financial Supervisory Authority, were emptied and temporary housing at Kalkofnsvegur 2 was leased for the duration of the renovation project.

Table VI-1. Number of employees, by department (table next to Human Resources subchapter)

<i>Department</i>	<i>Number</i>
Banking	22
Governors	4
Finance	12
Financial Stability	28
Economics and Monetary policy	24
Internal Audit	3
Compliance and Inspections	25
Pensions and Insurance	13
Human Resources	7
Markets and Business Conduct	16
Markets	32
Operations	35
General Secretariat	27
Information Technology and Statistics	46
Total	294

## The COVID-19 pandemic continued to affect the Bank's activities

For the second year in a row, a large number of employees were forced to work outside the Bank's premises for a large share of the year. Employees continued to conduct remote meetings when the status of the pandemic required it. Visits to the Bank remained prohibited for much of the year, and the exhibition hall on the first floor was closed for part of the year. For work carried out on the premises throughout most of the year, employees were divided into pods or "quaranteams", in accordance with the instructions of the public health authorities, and cafeteria, cleaning, and other services were adapted to the criteria applying at any given time.

## Central Bank of Iceland 31 Desember 2021

### Governor

Ásgeir Jónsson

### Deputy Governors

Gunnar Jakobsson

Rannveig Sigurdardóttir

Unnur Gunnarsdóttir

### Supervisory Board

#### Principal members

Gylfi Magnússon, chair

Thórunn Gudmundsdóttir, vice-chair

Bolli Hédinsson

Una María Óskarsdóttir

Sigurdur Kári Kristjánsson

Jacqueline Clare Mallett

Frosti Sigurjónsson

#### Alternates

Thórlindur Kjartansson

Jóhanna Vigdís Gudmundsdóttir

Hildur Traustadóttir

Valgerdur Sveinsdóttir

Kristín Thoroddsen

Ólafur Margeirsson

Bára Valdís Ármannsdóttir

### Principal Officers

#### General Secretariat:

Rannveig Júníusdóttir, Director

#### Finance:

Erla Gudmundsdóttir, Director

#### Financial Stability

Haukur C. Benediktsson, Director

#### Economics and Monetary Policy:

Thórarinn G. Pétursson, Chief Economist

#### Human Resources:

Íris Guðrún Ragnarsdóttir, Director

#### Markets:

Sturla Pálsson, Director

#### Operations:

Thóra Helgadóttir, Director

#### Information Technology and Statistics:

Logi Ragnarsson, Director

#### Compliance and Inspections:

Björk Sigurgísladóttir, Director

#### Pensions and Insurance:

Rúnar Gudmundsson, Director

#### Banking:

Elmar Ásbjörnsson, Director

#### Markets and Business Conduct:

Páll Fridriksson, Director

#### Internal Auditor:

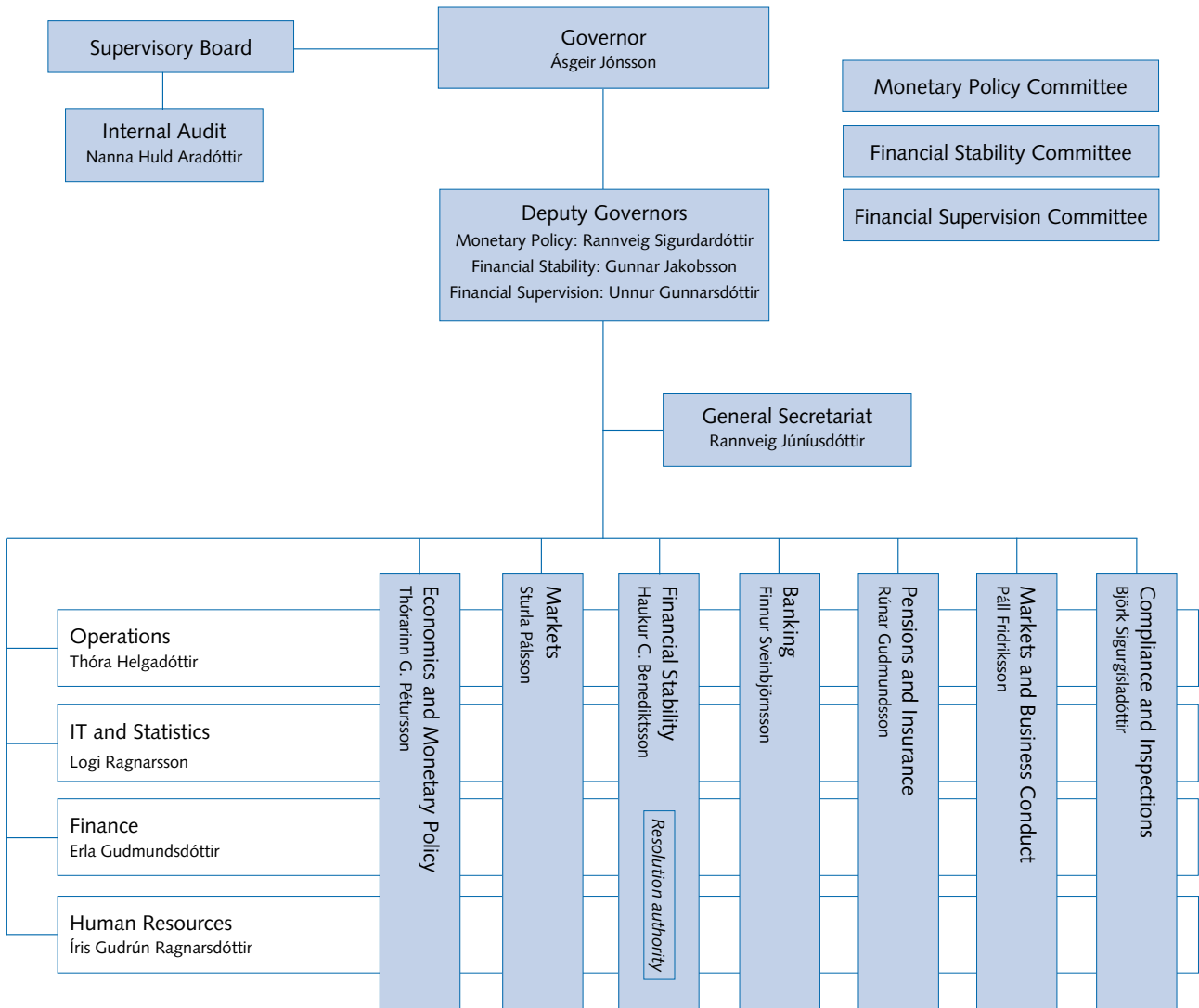
Nanna Huld Aradóttir

### Company owned by the Central Bank of Iceland

#### Greidsluveitan ehf.:

Vigdís Ósk Helgadóttir, Director

## Central Bank of Iceland — organisational chart



# Sustainability



The Central Bank of Iceland aims to be an exemplary institution in the area of sustainability and took important steps in this direction during the year. Sustainability is not only a matter of environmental affairs but also one involving welfare, health, social justice, and governance practices that promote sustainability. Environmental, social, and governance criteria, often referred to collectively by the acronym ESG, are often referenced in this context. The underpinnings of sustainability are a society, environment, and economy that support one another and, among other things, lay the foundations for the United Nations Sustainable Development Goals.

For the Central Bank, sustainability entails robust governance and consideration of environmental and social factors in its activities and operations. The Central Bank's role is also to contribute to the economic welfare of the Icelandic nation by promoting price stability, financial stability, and sound and secure financial activities.

## Environmental issues

The aim of the Central Bank's environmental and climate policy, adopted in May 2021, is to systematically reduce greenhouse gas emissions from the Bank's operations, thereby ensuring that the Bank contributes to Iceland's fulfilment of its climate obligations. The Bank is committed to reducing the greenhouse gas emissions from its operations by 40% between 2019 and 2030. In November 2021, the Bank published an action plan outlining measures that will contribute to the attainment of the Bank's objectives. Examples of such measures are swapping out the Bank's motor vehicles for electric cars, using eco-friendly rental vehicles, reducing air travel,

and increasing recycling. The environmental and climate policy and the action plan will be reviewed annually.

The Bank's incorporation of green steps in government operations into its activities has been successful, although the COVID-19 pandemic complicated matters somewhat. The Bank is working towards implementing a special environment management system.

In May 2021, the Bank held a series of meetings on climate issues where staff members gave monthly talks on various projects relating to climate affairs and the Bank's fields of responsibility. Some of the topics centred on the Bank's climate-related journey as it relates to financial supervision, monetary policy, and financial supervision. In the first issue of *Kalkofn*, the Bank's new web-based publication launched in September 2021, a scenario analysis of climate risk was published.

The Central Bank of Iceland practises green accounting and keeps track of its purchases and waste from the standpoint of sustainability targets. The Bank's carbon footprint is calculated using green accounting methods, and a transportation survey is carried out annually among staff members. The Bank's sustainability accounting based on ESG criteria will be published concurrent with its sustainability report. The report will also contain a more detailed discussion of sustainability targets and the ways in which climate issues will be incorporated into the Bank's core activities and risk analyses.

### Cooperation on climate issues and climate risk

During the year, the Central Bank spearheaded regular consultation among the Nordic and Baltic central banks concerning their work relating to climate issues and climate risk, and the Bank participated in the first Nordic central banks' symposium on climate risk and



its impact on central bank activities. The Bank also met with a number of domestic stakeholders in areas relating to climate and climate risk during the year, in order to enhance Bank staff members' knowledge of climate issues and create a forum for cooperation in this field.

The Bank became a member of the Network for Greening the Financial System (NGFS) in late 2020 and began participating actively in its work in 2021. The Central Bank has representatives on three NGFS task forces and, among other work, participated in the NGFS annual meeting and the publication of the recommendations issued by the Network. In connection with NGFS cooperation, an advisory group has been established within the Bank in order to address and follow up on matters relating to the Network. In addition, a Bank expert worked with representatives from other NGFS members on preparing a special report on a scenario analysis of climate risk from the standpoint of financial supervision and central banking.

In November, the Bank issued a statement describing its climate obligations in connection with the UN Climate Change Conference in Glasgow. In the statement, the Bank outlined its climate-related goals, which include reducing its own carbon footprint; preparing guidelines for supervised entities to use in defining, assessing, and monitoring the climate risk on their balance sheets; and taking account of climate risk in its stress testing of the financial system and financial market entities.

## Social issues

### Equal rights

The Central Bank supports equal rights, equal treatment, and respect for staff members. The Bank adheres to an equal rights policy in accordance with the Act on Gender Equality, no. 150/2020, and the Act on Equal Treatment in the Labour Market, no. 86/2018.

In March 2021, the Bank renewed its equal rights policy, which states, among other things, that the Bank shall make it easier for employees to harmonise their obligations towards their work and their family, that employees shall be treated equally in terms of hiring and professional advancement, and that no harassment of any kind will be tolerated within the Bank. The Bank appointed a new equal rights committee, which maintains an overview of regulatory instruments on equal rights and equal treatment of employees. The committee works on the regular renewal of the Bank's equal rights plan, monitors its implementation, and evaluates the validity of tips and pointers on equal rights and equal treatment of staff members.

The Central Bank's equal pay policy was approved during the year. According to the policy, all employees shall receive equal pay and enjoy equal terms of employment and rights for the same jobs or jobs of equal value, so that there is no gender-based pay gap within the Bank.

The Bank's equal pay certification was renewed in the autumn. For the second year in a row, an equal pay analysis showed that there was no unexplained wage gap between the sexes at the time.

### Human resources

Human resources are the key to effective, sustainable operations at the Central Bank. The Bank's human resources policy aims to build up a strong team spirit, with emphasis on respect, mental and physical well-being, equal rights, expertise, professionalism, and progressiveness. The Bank's work environment is based on flexibility and trust, and it supports employee well-being, job satisfaction, an improved balance between employees' work and private life, equal rights, and reduced greenhouse gas emissions.

The Central Bank dedicated the month of October to employees' health. Staff members were encouraged to be physically active, and health metrics monitoring and health-related education were offered.

In addition, the Bank adheres to a special transportation policy that encourages employees to use eco-friendly, economical, and healthy modes of transport and supports them in that endeavour. At the end of 2021, a total of 86 transportation agreements between employees and the Bank were in effect. Under these agreements, employees pledge to use eco-friendly methods of transport to and from the workplace.

## Governance

The Central Bank prioritises responsible governance practices. During the year, the Bank's senior officers received management training aimed at strengthening the management team and formulating the Bank's vision and values in the wake of the merger between the Bank and the Financial Supervisory Authority in 2020.

Central Bank of Iceland employees shall demonstrate integrity, decisiveness, humility, and professionalism in their work and overall conduct. The Bank's values reflect its professional practices, form the foundation for confidence in the Bank, and foster the achievement of the Bank's objectives. The Bank's Code of Conduct is based on its fundamental values and discusses further



the ethical criteria that Bank employees must adopt and be guided by in their work.

During the year, senior Central Bank officers discussed the challenges and risks associated with climate matters and other aspects of sustainability, and their impact on the Bank's management, operations, and sphere of responsibility. The Bank also keeps abreast of its suppliers' sustainability obligations, with the aim of encouraging and supporting them in improving their performance if necessary.

# Operating results and balance sheet



According to its profit and loss account, the Central Bank of Iceland recorded a net operating loss of 15,834 m.kr. in 2021, compared with a profit of 68,253 m.kr. in the previous year. The loss on the Bank's activities during the year is largely attributable to changes in asset values. The loss on financial instruments before exchange rate differences totalled 11,211 m.kr. during the year, as compared with a profit of 10,137 m.kr. in 2020. The tables in the margin show the year-on-year changes in key items in the profit and loss account and balance sheet.

Net interest expense totalled 209.4 m.kr. in 2021, as opposed to net interest income of 74.5 b.kr. in the previous year. Interest income on domestic assets increased year-on-year by 516 m.kr., or 131.5%, whereas interest income on foreign assets declined by 2.7 b.kr., or 39.3%. The increase in interest income from domestic assets is due mainly to increased income from Treasury bonds, owing to Treasury bond purchases during the year. The decline in interest income from foreign assets is due to lower yields in foreign markets. Interest expense on domestic liabilities declined by 3.4 b.kr., whereas interest expense on foreign liabilities and assets increased by 1.5 b.kr. The year-on-year reduction in interest expense on domestic liabilities is due mainly to a lower policy interest rate in 2021 than in 2020. The increase in interest expense on foreign assets and liabilities is due mainly to lower yields in foreign markets, which resulted in higher negative interest on foreign assets.

The exchange rate loss in 2021, totalling 819 m.kr., is due to the small difference between the exchange rate at the beginning and end of the year. In 2020, exchange rate gains totalled 62,116 m.kr.

Asset valuation adjustments were negative in the amount of 11,099 m.kr. in 2021 but were positive by

Table VIII-1 Profit and loss accounts highlights

<i>M.kr.</i>	2021	2020	<i>Change</i>
Net interest income (interest expense)	(209)	75	(284)
Changes in asset value	(11,099)	10,063	(21,162)
Revenues from shareholdings	98	–	98
Exchange rate difference	(819)	62,116	(62,935)
Gains on financial instruments	(12,029)	72,254	(84,283)
Operating revenues	3,657	3,354	303
Operating expenses	(7,778)	(7,413)	(365)
Effects of affiliated companies			
outside the group	302	55	247
Income tax	14	3	11
Outcome for the year	(15,834)	68,253	(84,087)

Table VIII-2 Balance sheet highlights

<i>M.kr.</i>	2021	2020	<i>Change</i>
<i>Assets</i>			
Gold	15,212	15,404	(192)
Foreign-den. claims against non-residents	907,828	801,469	106,359
Foreign-den. claims against residents	1	–	1
Monetary policy-related claims			
against residents	23,646	9,520	14,126
Króna-den. claims against residents	5,981	5,809	172
Other assets	11,101	10,620	481
Assets, total	963,769	842,821	120,948
<i>Equity and liabilities</i>			
Equity	134,051	150,802	(16,751)
Issued banknotes and coin	82,047	81,462	585
Foreign-den. debt to non-residents	89,371	30,556	58,815
Foreign-denominated debt to residents	304,575	214,164	90,411
Króna-den. debt to non-residents	5,546	9,262	(3,716)
Monetary policy-related debt to			
domestic credit institutions	274,526	210,577	63,949
Króna-denominated debt to residents	71,992	144,926	(72,934)
Other liabilities	1,661	1,072	589
Equity and liabilities, total	963,769	842,821	120,948

10,063 m.kr. in 2020. Asset valuation adjustments in 2021 are due to falling prices, which in turn are due to higher inflation expectations in the eurozone, the US, and the UK.

The Bank's assets totalled 963,769 m.kr. at year-end 2021, as opposed to 842,821 m.kr. at the end of 2020. Foreign assets increased by 106.4 b.kr. during the year. This rise is due primarily to the issuance in foreign markets of a Treasury bond in the amount of 750 million euros and an allocation by the International Monetary Fund (IMF) of special drawing rights (SDR) to its member countries during the year, which increased Iceland's reserve holdings by SDR 308 million (56.2 b.kr. at the year-end exchange rate). This was offset by a reduction in foreign assets due to foreign exchange market intervention by the Bank, which bought euros for 20.9 b.kr. and sold them for 51.9 b.kr. The Bank's capital totalled 134,051 m.kr. at year-end 2021, and its capital ratio was 13.9%, as compared with 17.9% at year-end 2020. Foreign assets accounted for 96% of the Bank's total assets at the end of 2021.

The Central Bank's accounts are presented later in this report, together with explanatory notes on individual items.

## Outlook and capital adequacy criteria

The Central Bank is required by law have the financial strength needed to enable it to carry out its legally mandated role. In keeping with this, each year the Bank must determine capital adequacy criteria that reflect its need for capital and interest-bearing assets. The capital adequacy criteria are based on the Bank's operating expenses and the risks and uncertainties it faces at any given time. The decision on capital adequacy criteria is endorsed by the Supervisory Board. The capital benchmark was set at 150 b.kr. in 2021.

The Bank's operating results deteriorated during the year, owing mainly to the revaluation of securities in the reserves due to increased yields abroad. Because of this, the Bank's capital declined after having grown during the years beforehand, owing to the depreciation of the Icelandic króna and an unusually small interest rate spread between assets and liabilities. At the end of 2021, the Bank's capital totalled 134,1 b.kr., which is below the benchmark endorsed by the Supervisory Board. At the end of 2020, it was 150.8 b.kr., and at the end of 2019 it was 82 b.kr. The Bank did not call in capital from the Treasury in 2021, despite the statutory authorisation providing for callable capital ranging up to

57.2 b.kr. at the price level from the date the Act entered into force.

The economic outlook is highly uncertain, not least because of rising global inflation and the war in Europe. As a result, there is still uncertainty about the Bank's operations and need for capital in the long term.

A scenario analysis of developments in the Bank's performance and capital over the next five years broadly suggests continued operating losses and therefore declining capital, owing to negative carry, exchange rate risk, and interest rate risk. Analysing the Bank's capital requirement therefore does not give cause to change the capital adequacy benchmark set in 2021, which has been endorsed unchanged by the Supervisory Board at 150 b.kr.

Each year, a decision is taken on the disposition of the Bank's profit, in accordance with a method introduced with Act no. 122/2014. The Bank's profit, net of allocations made to the reserve fund, is transferred to the Treasury, to the extent that it is not used to strengthen the Bank's capital. In accordance with Article 40, Paragraph 2 of the Act on the Central Bank of Iceland, no dividend will be paid to the Treasury for 2021, owing to operating losses and a capital position below the capital adequacy benchmark.

Consolidated  
Annual Accounts 2021

IX

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# Independent auditor's report

## To the Supervisory Board and the Governor of the Central Bank of Iceland

### Report on the Audit of the Consolidated Financial Statements

#### Opinion

We have audited the consolidated financial statements of the Central Bank of Iceland ("the Group") for the year 2021, which comprise the consolidated balance sheet as of 31 December 2021, the consolidated income statement, consolidated statement of cash flows, and consolidated changes in equity for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies and other explanatory information.

In our opinion, the accompanying consolidated financial statements give a true and fair view of the financial position of the Group as of 31 December 2021, and of its consolidated financial performance and its consolidated cash flows for the year then ended, in accordance with the Icelandic Annual Accounts Act.

#### Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISA). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with the ethical requirements that are relevant to our audit of consolidated financial statements in Iceland, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

#### Other information

The Supervisory Board and the Governor of the Central Bank are responsible for the other information. The other information comprises the Annual Report but does not include the consolidated financial statements and our auditor's report thereon. Our opinion on the consolidated financial statements does not cover the other information, and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or the knowledge we obtained in our audit, or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. The Annual Report is not available on our reporting date but is expected to be made available to us after that date.

#### Responsibilities of the Supervisory Board and the Governor of the Central Bank for the Consolidated Financial Statements

The Supervisory Board and the Governor are responsible for the preparation and fair presentation of the consolidated financial statements in accordance with the Icelandic Annual Accounts Act, the Act on Financial Undertakings, and the Act on the Central Bank of Iceland, and for such internal control as they deem necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the Supervisory Board and the Governor are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless they either intend to dissolve the Group or to cease operations, or have no realistic alternative but to do so.

The Supervisory Board and the Governor of the Central Bank are responsible for overseeing the Group's financial reporting process.



### **Auditor's Responsibilities for the Audit of the Consolidated Financial Statements**

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free of material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with the ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions taken by users on the basis of these consolidated financial statements.

As part of an audit in accordance with the ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risk of material misstatement in the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of the management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure, and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision, and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with the Supervisory Board regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

Reykjavík, 16 March 2022

KPMG ehf.

Hrafnhildur Helgadóttir

# Confirmation by the management of the Central Bank of Iceland

The Supervisory Board and Governor of the Central Bank of Iceland hereby confirm the Bank's annual financial statements for the year 2021 with their signatures. Frosti Sigurjónsson expresses the reservation that he does not consider it appropriate to include banknotes and coin with liabilities in the balance sheet.

Reykjavík, 16 March 2022

## Confirmation by the Supervisory Board

*Gylfi Magnússon*  
chair

*Thórunn Guðmundsdóttir*  
*Sigurdur Kári Kristjánsson*  
*Frosti Sigurjónsson*

*Bolli Hédinsson*  
*Una María Óskarsdóttir*  
*Jacqueline Clare Mallett*

## Confirmation by the Governor

*Ásgeir Jónsson*

## Confirmation by the Prime Minister's Office

With reference to the statements by the auditors, the Supervisory Board, and the Governor, I hereby ratify these financial statements.

Reykjavík, 31 March 2022

*Katrín Jakobsdóttir*

## Profit and Loss Account 2021

	Notes	2021	2020
Interest income on domestic assets	5	907,838	392,160
Interest income on foreign assets	5	4,157,099	6,852,230
Interest expense on domestic liabilities	6	(3,107,047)	(6,537,436)
Interest expense on foreign liabilities and assets	6	(2,167,258)	(632,422)
Net (interest expense) interest income		<u>(209,368)</u>	<u>74,532</u>
Changes in foreign asset values		(10,376,547)	9,771,472
Changes in domestic asset values		(722,827)	291,187
Changes in asset value, total	7	<u>(11,099,374)</u>	<u>10,062,659</u>
Revenues from shareholdings	8	97,933	-
(Losses) Gains on financial instruments before exchange rate difference		(11,210,809)	10,137,191
Exchange rate difference	9	<u>(818,984)</u>	<u>62,116,426</u>
(Losses) Gains on financial instruments		<u>(12,029,793)</u>	<u>72,253,617</u>
Supervisory revenues	10	2,209,804	2,359,005
Service revenues	11	1,187,155	903,831
Other revenues		259,880	91,451
Other revenues, total		<u>3,656,839</u>	<u>3,354,287</u>
Salaries and related expenses	12	(4,921,342)	(5,146,535)
Other operating expenses	13	(1,919,039)	(1,503,283)
Service expenses	14	(674,529)	(536,903)
Depreciation of property and equipment	21.1	(146,035)	(129,080)
Depreciation of software	21.2	(116,368)	(96,898)
Operating expenses, total		<u>(7,777,313)</u>	<u>(7,412,699)</u>
Effects of subsidiaries outside the group	21.3	302,038	55,016
(Loss) profit before taxes		<u>(15,848,229)</u>	<u>68,250,221</u>
Income tax	15	13,750	3,226
(Loss) Profit for the year		<u>(15,834,479)</u>	<u>68,253,447</u>

## Balance Sheet 31 December 2021

	Notes	31.12.2021	31.12.2020
<b>Assets</b>			
Gold	16	15,211,571	15,403,715
Foreign-denominated claims against non-residents	17	907,827,623	801,469,348
Foreign bank deposits	17.1	169,478,923	109,886,615
Balance with IMF	17.2	89,747,098	33,696,074
Foreign securities and other reserve assets	17.3	648,601,088	657,805,606
Non-reserve assets	17.4	514	81,053
Foreign-denominated claims against residents	18	781	-
Monetary policy-related claims against residents	19	23,646,485	9,519,749
Treasury	19.1	21,834,841	7,770,361
Deposit institutions	19.2	1,811,644	1,749,388
Króna-denominated claims against residents	20	5,980,855	5,808,631
Deposit institutions	20.1	302,014	-
Other entities	20.2	5,678,841	5,808,631
Other assets	21	11,102,026	10,619,730
Fixed operational assets	21.1	8,401,020	7,928,990
Software	21.2	933,039	983,598
Other assets	21.3	1,767,967	1,707,142
Assets, total		<u>963,769,341</u>	<u>842,821,173</u>

	Notes	31.12.2021	31.12.2020
<i>Equity and liabilities</i>			
<i>Equity</i>			
Capital		94,240,804	91,160,430
Uncalled capital		(62,739,804)	(59,659,430)
Value adjustment reserve		29,310,057	67,056,063
Revaluation of real estate and liquid assets		7,117,895	7,330,069
Unrealised share in profit of associates		224,688	26,896
Other equity		65,896,874	44,888,080
Total equity	22	<u>134,050,514</u>	<u>150,802,108</u>
<i>Liabilities</i>			
Issued banknotes and coin	23	82,046,661	81,462,111
Foreign-denominated debt to non-residents	24	89,371,007	30,555,938
Deposits	24.1	12,601,875	9,927,305
Counterpart to IMF	17.2	76,769,132	20,628,633
Foreign-denominated debt to residents	25	304,575,082	214,163,804
Króna-denominated debt to non-residents	26	5,546,351	9,262,364
Deposits	26.1	5,546,351	2,494,998
Certificates of deposit	26.2	-	6,767,366
Monetary policy-related debt to domestic credit institutions	27	274,525,854	210,577,243
Deposits	27.1	78,666,995	66,011,866
Reserve requirements	27.2	26,818,504	24,487,312
Term deposits	27.3	169,040,355	112,948,802
Certificates of deposit	27.4	-	7,129,263
Króna-denominated debt to residents	28	71,991,797	144,925,801
Treasury and Government institutions	28.1	67,832,527	142,289,342
Other entities	28.2	4,159,270	2,636,459
Other liabilities	29	1,662,075	1,071,804
Liabilities, total		<u>829,718,827</u>	<u>692,019,065</u>
Equity and liabilities, total		<u>963,769,341</u>	<u>842,821,173</u>

## Consolidated Statement of Changes in Equity

	Capital	Uncalled capital	Value adjustment reserve	Real estate revaluation	Unrealised share in profit of associates	Other equity (negative)	Equity, total
<b>2021</b>							
Equity 1 January 2020	91,160,430	(59,659,430)	67,056,063	7,330,069	26,896	44,888,080	150,802,108
Indexation of uncalled capital	3,080,374	(3,080,374)	-	-	-	-	-
Dividend paid to the Treasury	-	-	-	-	-	(802,109)	(802,109)
(Loss) for the year 2021	-	-	(37,746,006)	-	197,792	21,713,735	(15,834,479)
Real estate revaluation 2021	-	-	-	(115,006)	-	-	(115,006)
Depreciation of revalued assets 2021	-	-	-	(97,168)	-	97,168	-
<b>Equity 31 December 2021</b>	<b>94,240,804</b>	<b>(62,739,804)</b>	<b>29,310,057</b>	<b>7,117,895</b>	<b>224,688</b>	<b>65,896,874</b>	<b>134,050,514</b>
<b>2020</b>							
Equity 31 December 2019	89,763,819	(58,262,819)	55,126,282	7,540,925	251,966	(12,438,271)	81,981,902
Effect of new Central Bank Act	(1,062,819)	1,062,819	-	-	-	-	-
Effect of merger with Financial Supervisory Authority	-	-	-	-	-	690,870	690,870
<b>Equity 1 January 2020</b>	<b>88,701,000</b>	<b>(57,200,000)</b>	<b>55,126,282</b>	<b>7,540,925</b>	<b>251,966</b>	<b>(11,747,401)</b>	<b>82,672,772</b>
Indexation of uncalled capital	2,459,430	(2,459,430)	-	-	-	-	-
Profit for the year 2020	-	-	11,929,781	-	124,930	56,198,736	68,253,447
Dividend from subsidiaries	-	-	-	-	(350,000)	350,000	-
Real estate revaluation 2020	-	-	-	(124,111)	-	-	(124,111)
Depreciation of revalued assets 2020	-	-	-	(86,745)	-	86,745	-
<b>Equity 31 December 2020</b>	<b>91,160,430</b>	<b>(59,659,430)</b>	<b>67,056,063</b>	<b>7,330,069</b>	<b>26,896</b>	<b>44,888,080</b>	<b>150,802,108</b>

Note 22 discusses the accounting treatment of equity items, gives an itemisation of changes in the revaluation reserve, and shows developments in the Bank's capital ratio in recent years.



## Consolidated Statement of Cash Flows

	Notes	2021	2020
<i>Operating activities</i>			
Collected interest income		10,776,066	11,246,831
Paid interest expense		(6,458,100)	(18,914,962)
Collected interest (paid)		<u>4,317,966</u>	<u>(7,668,131)</u>
Collected supervisory revenues		2,359,005	-
Collected service revenues and other revenues		1,001,850	980,169
Paid service expense		(538,344)	(529,433)
Paid-in dividends on shareholdings	9	-	45,550
Paid operating expense		(6,518,721)	(4,010,678)
Paid taxes		(23,446)	(54,923)
Net cash from (to) operating activities		<u>598,310</u>	<u>(11,237,446)</u>
<i>Investment activities</i>			
Securities purchased in international reserves	18.3	(364,111,453)	(114,825,299)
Securities sold and collected in international reserves		340,426,089	150,384,547
Changes in foreign non-reserve assets		100,738	146,573
Treasury securities purchased	20.1	(7,566,030)	-
Collected króna-denominated instalments on securities		186,460	160,196
Other assets		(1,748,243)	(1,343,630)
Operational assets purchased	22.1	(341,406)	(26,029)
Software purchased	22.2	(310,349)	(241,099)
Net investment in subsidiaries outside the group	22.3	-	(757,789)
Dividends paid by companies outside the group	22.3	350,000	4,282,055
Claims against subsidiaries outside the group	33	1,390,798	-
Investment activities, total		<u>(31,623,396)</u>	<u>37,779,525</u>
<i>Financing activities</i>			
Issued banknotes and coin	24	6,727,692	1,961,281
Foreign-denominated deposits		39,851,539	34,917,961
Króna-denominated deposits		(114,699,545)	20,964,526
Certificates of deposit		(26,316,554)	4,113,588
Other liabilities		(196,371)	69,950
Financing activities, total		<u>(94,633,239)</u>	<u>62,027,306</u>
Foreign bank deposits, increase (decrease)		(125,658,325)	88,569,385
Exchange rate difference on foreign bank deposits	10	25,387,239	2,493,526
Foreign cash balance at beginning of year		<u>210,157,700</u>	<u>119,094,789</u>
Foreign cash balance at end of year	18	<u>109,886,615</u>	<u>210,157,700</u>

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## General

### Note 1 – Information on the Central Bank of Iceland

The Central Bank of Iceland is an independent institution owned by the State and operating under the auspices of the Prime Minister. Its objective is to promote price stability, financial stability, and sound and secure financial activities. The Bank

shall also undertake such tasks as are consistent with its role as a central bank, such as maintaining international reserves and promoting a safe, effective financial system, including domestic and cross-border payment intermediation.

### Note 2 – Basis for accounting methods

The Central Bank of Iceland's consolidated annual accounts for the year ended 31 December 2021 are prepared in accordance with the Act on the Central Bank of Iceland, no. 92/2019, and the Annual Accounts Act, no. 3/2006. The consolidated annual accounts are based on cost-price accounting methods, except for financial assets held for trading and real estate, which are entered at fair value. Financial assets held for trading include

marketable bonds and derivatives. The consolidated annual accounts have been prepared using the same accounting methods as in the prior year. The consolidated annual accounts are prepared in Icelandic krónur. All amounts are presented in thousands of Icelandic krónur. Information on the accounting methods can be found in Note 43.

### Note 3 – Accounting estimates and decisions

In preparing the annual accounts, management must take decisions, make estimates, and draw conclusions that affect the application of accounting principles, as well as affecting the presented amounts of assets and liabilities, and income and expenses. The final results may differ from these estimates.

Management reviews estimates and underlying assumptions and makes changes as is deemed necessary. Changes in accounting estimates are recognised in the period in which they take place.

### Note 4 – The group

Subsidiaries are companies controlled by the group. Control exists if the group bears the risk, is entitled to enjoy the variable benefits of its participation in the company, and can, through its decision-making power, affect the returns on the investment. The accounts of Greidsluveitan are included in the consolidated accounts from the time control was established until that control ends. The accounts of real estate company F fasteignafélag ehf. are held outside the group because they do not have a material

impact on the operations and balance sheet of the group. The holding in F fasteignafélag ehf. is entered using the equity method.

Positions and transactions and all unrealised revenues and expenses between companies in the group are omitted from the consolidated financial statements.

	<i>Ownership share</i>	<i>Activities</i>
<i>Companies within the group</i>		
Greidsluveitan ehf., Álfheimar 74, Reykjavík	100%	Payment system operations
<i>Company outside the group</i>		
F fasteignafélag ehf., Ránargata 18, Reykjavík	100%	Holding company

## Notes to the profit and loss account

### Note 5 – Interest income

	2021	2020
<i>Interest income from domestic assets</i>		
Interest income on overnight loans and credit lines	321	766
Interest income on collateralised loans	21,603	6,638
Interest income on non-indexed securities	496,022	23,276
Interest income on indexed securities	387,679	348,888
Interest income on other domestic assets	2,213	12,592
Interest income on domestic assets, total	<u>907,838</u>	<u>392,160</u>
<i>Interest income on foreign assets</i>		
Interest income on balance with IMF	28,258	64,237
Interest income on bank accounts	7,462	197,164
Interest income on securities	4,121,379	6,365,574
Interest income on other foreign assets	0	225,255
Interest income on foreign assets, total	<u>4,157,099</u>	<u>6,852,230</u>

Interest income on domestic assets rose by 515.7 m.kr. from the year 2020, or by 131.5%.

The Bank stopped offering conventional overnight loans when the new interbank payment system was launched in H2/2020. Instead, banks have access to credit lines through the interbank payment system. The credit lines were used seldom in 2021.

Interest income on collateralised loans in 2021 is due to support loans. Interest income on collateralised loans is due mainly to the special collateralised loans offered by the Bank to commercial banks and savings banks beginning in September 2020, in connection with support loans bearing a 100% Treasury guarantee.

The Bank began buying Treasury bonds in the secondary market at the beginning of May 2020 and continued the purchases in 2021. Its bondholdings grew from 7.8 b.kr. at year-end 2020 to 21.8 b.kr. at the end of 2021, which explains the rise in interest income on nominal bonds.

Interest income on domestic assets declined 2.7 b.kr. from the year 2020, or by 39.3%.

Interest income on foreign bank accounts declined by 189.7 m.kr. year-on-year. At present, most of the Bank's foreign bank accounts bear no interest or negative interest. Negative interest on foreign bank accounts is recognised as interest expense. Total interest on foreign bank accounts, adjusted for accounts bearing negative interest rates, was negative in the amount of 590 m.kr., resulting in a 236 m.kr. increase in net interest expense relative to 2020.

Interest income on foreign securities fell by 2.2 b.kr. year-on-year, or 35.3%. This was due to a decline in foreign market yields. Interest on bonds with negative yields is recognised as interest expense. Net interest on foreign bondholdings was 2.6 b.kr. in 2021, a year-on-year decline of 3.8 b.kr., or 59.3%.

## Note 6 – Interest expense

	2021	2020
<i>Interest expense on domestic liabilities</i>		
Interest expense on term deposits	1,712,199	3,951,380
Interest expense on current accounts	1,325,827	2,272,057
Interest expense on FX-accounts	78	542
Interest expense on other domestic liabilities	68,943	313,457
Interest expense on domestic assets, total	<u>3,107,047</u>	<u>6,537,436</u>
<i>Interest expense on foreign liabilities and assets</i>		
Interest expense on balance with IMF	21,480	41,149
Interest expense on foreign bank accounts	597,544	551,169
Interest expense on foreign securities in international reserves	1,548,234	40,104
Interest expense on foreign assets, total	<u>2,167,258</u>	<u>632,422</u>

Interest expense on domestic liabilities declined by 3.4 b.kr., or 52.5,% between years. This is due to a lower policy interest rate in 2021 than in 2020.

Interest expense on term deposits totalled 1.7 b.kr. in 2021, as opposed to 4 b.kr. in 2020, a decline of 2.2 b.kr., or 56.7%.

Interest expense on current accounts declined by 0.9 b.kr., or 41.6%.

Interest expense on foreign assets increased by 1.5 b.kr., owing to reduced yields in foreign markets, which caused higher negative interest rates on foreign assets.

Interest expense on foreign bank accounts increased by 46.3 m.kr., or 8.4%, owing to negative interest on deposit balances.

Interest expense on foreign reserve securities derives from negative bond interest.

## Note 7 – Changes in asset value

	2021	2020
<i>Realised revaluation</i>		
Domestic securities	-	(4,217)
Foreign securities and securities funds	1,908,952	3,186,360
Realised revaluation, total	<u>1,908,952</u>	<u>3,182,143</u>
<i>Unrealised revaluation</i>		
<i>Domestic securities</i>	(722,827)	86,956
Domestic derivatives	-	208,448
Foreign securities and securities funds	(12,285,499)	6,791,345
Foreign derivatives	-	(206,233)
Unrealised revaluation, total	<u>(13,008,326)</u>	<u>6,880,516</u>
Changes in asset value, total	<u>(11,099,374)</u>	<u>10,062,659</u>

## Note 8 – Revenues from shareholdings

Revenues from shareholdings are due to dividends from the Bank for International Settlements (BIS). Because of the

spread of the COVID-19 pandemic, the BIS decided not to pay dividends in 2020.



## Note 9 – Exchange rate difference

	2021	2020
<i>Realised exchange rate difference</i>		
Foreign bank deposits	(6,321,655)	25,387,239
Foreign securities and funds	11,413,826	57,339,798
Domestic foreign-denominated bank deposits	18,493,971	(26,817,912)
Derivatives	-	(2,215)
Other	136,261	17,992
Realised exchange rate difference, total	<u>23,722,403</u>	<u>55,924,902</u>
<i>Unrealised exchange rate difference</i>		
Gold	(192,144)	3,683,579
International Monetary Fund	(95,920)	1,142,998
Foreign securities and funds	(24,257,471)	1,369,903
Other	4,148	(4,956)
Unrealised exchange rate difference, total	<u>(24,541,387)</u>	<u>6,191,524</u>
Exchange rate difference, total	<u>(818,984)</u>	<u>62,116,426</u>

	<i>Average exchange rate for the year</i>		<i>Year-end exchange rate</i>		<i>Change in year-end exchange</i>
	2021	2020	2021	2020	%
Euro (EUR)	150,2	154,5	147,6	156,1	-5.4%
US dollar (USD)	127,1	135,3	130,4	127,2	2.5%
Pound sterling (GBP)	174,7	173,6	175,7	173,6	1.3%
Japanese yen (JPY)	1,2	1,3	1,1	1,2	-8.1%
Danish krone (DKK)	20,2	20,7	19,9	21,0	-5.4%
Norwegian krone (NOK)	14,8	14,4	14,8	14,9	-1.1%
Swedish krona (SEK)	14,8	14,8	14,4	15,6	-7.6%
Swiss franc (CHF)	139,0	144,3	142,8	144,4	-1.1%
Canadian dollar (CAD)	101,3	101,0	102,4	99,9	2.5%
Chinese yuan (CNY)	19,7	19,6	20,5	19,5	5.6%
Special drawing rights (XDR)	180,9	188,5	182,5	183,9	-0.7%
Gold (XAU)	228,444,7	240,145,8	238,478,1	240,817,4	-1.0%

### Total foreign-denominated assets and liabilities, in ISK thousands

	31.12.2021		31.12.2020	
	<i>Assets</i>	<i>Liabilities</i>	<i>Assets</i>	<i>Liabilities</i>
Euro	518,941,143	340,663,951	359,763,714	230,693,054
US dollar	308,062,722	32,194,482	317,398,872	8,495,056
Pound sterling	53,560,841	6,277,089	91,287,299	1,653,105
Yen	15,691,537	6,435,881	27,699,601	1,647,806
Other currencies	11,678,389	8,383,240	5,458,728	2,233,515
Gold	15,211,571	-	15,403,715	-
Total	<u>923,146,203</u>	<u>393,954,644</u>	<u>817,011,929</u>	<u>244,722,536</u>

A further itemisation of total foreign-denominated assets and liabilities can be found in Note 42. Special drawing rights (SDR) are a currency basket determined by the IMF. The basket comprises five currencies: US dollar, euro, Chinese yuan, pound sterling, and Japanese yen. The Bank's only asset

denominated in SDR is its balance with the IMF, and its only SDR-denominated liability is the counterpart to the IMF. The Bank's SDR-denominated assets and liabilities are converted to the currencies comprising the currency basket, using the weight of each at the year-end.

## Note 10 – Supervisory revenues

	2021	2020
Regular supervision	2,180,000	2,330,500
Extra supervision	29,804	28,505
Supervisory revenues, total	<u>2,209,804</u>	<u>2,359,005</u>

Supervised entities and other entities subject to fees as specified in the Act on the Payment of Costs for Official Supervision of Financial Activities and Resolution, no. 99/1999, shall pay the cost of operating the Central Bank financial supervisory authority by means of a special supervision fee.

If the Central Bank financial supervisory authority considers supervision of specific supervised entities to be considerably more costly and labour-intensive than the estimate for regular supervision provides for, the Central Bank may decide that the supervised entity concerned shall be required to pay for the necessary extra supervision.

## Note 11 – Service revenues

	2021	2020
Payment intermediation	1,020,911	748,169
Market transactions	166,244	155,662
Service revenues, total	<u>1,187,155</u>	<u>903,831</u>

## Note 12 – Salaries and related expenses

	2021	2020
Wages and salaries	4,052,838	4,188,471
Pension fund	595,331	588,247
Salary-related expenses	339,322	351,299
Contribution to pension obligations	(66,149)	18,518
Salaries and related expenses, total	<u>4,921,342</u>	<u>5,146,535</u>
Number of man-years	301	297

## Note 13 – Other operating expenses

	2021	2020
Operation of assets and liquid assets	572,002	415,070
Information technology	425,999	286,414
Outsourced services	291,065	296,398
Office expense	307,089	277,046
Sundry operational items	301,027	228,355
Expense due to banknotes and coin	21,857	-
Operating expenses, total	<u>1,919,039</u>	<u>1,503,283</u>

### Remuneration to auditors

	2021	2020
<i>Auditing of annual accounts</i>		
KPMG ehf.	10,503	10,753
<i>Consultancy and other services</i>		
Deloitte ehf.	2,554	4,166
PricewaterhouseCoopers ehf.	-	2,501
Remuneration to auditors, total	<u>13,057</u>	<u>17,420</u>

The Icelandic National Audit Office outsources the audit of the Central Bank of Iceland's consolidated annual accounts to KPMG ehf.

## Note 14 – Service expenses

	2021	2020
Payment intermediation	568,128	402,895
Expense due to custodial fees	66,546	71,264
Portfolio investment	39,855	62,744
Service expenses, total	<u>674,529</u>	<u>536,903</u>

## Note 15 – Income tax

The Central Bank of Iceland is exempt from income tax pursuant to Article 4 of the Income Tax Act, no. 90/2003. The income tax capitalised in the consolidated annual accounts is due to Greidsluveitan ehf., a subsidiary of the Central Bank of Iceland.

Income tax is calculated and recognised in the accounts, and the amount capitalised in the profit and loss account is 13.7 m.kr. (2020: 3.2 m.kr.). No income tax will be paid in 2021 because Greidsluveitan's income tax base is negative.

## Notes to the balance sheet

### Note 16 – Gold

	2021	2020
Balance at beginning of year	15,403,715	11,720,136
Exchange rate difference	(192,144)	3,683,579
Balance at end of year	<u>63,797</u>	<u>63,797</u>
Gold holdings at the year-end, in ounces	63,797	63,797

### Note 17 – Foreign-denominated claims against non-residents

#### Note 17.1 – Foreign bank deposits

	31.12.2021	31.12.2020
Deposits with foreign central banks	167,773,216	108,970,004
Balance with other foreign banks	1,705,707	916,611
Foreign bank deposits, total	<u>169,478,923</u>	<u>109,886,615</u>
Deposits available for withdrawal	157,001,557	104,492,911
Term deposits, available within three months	<u>12,477,366</u>	<u>5,393,704</u>
Foreign bank deposits, total	<u>169,478,923</u>	<u>109,886,615</u>

#### Note 17.2 – International Monetary Fund

Iceland's quota with the International Monetary Fund (IMF) totalled SDR 321.8 million at year-end 2021 (31.12.2020: SDR 321.8 m). The Bank's end-2021 balance with the Fund totalled SDR 69.8 million (31.12.2020: SDR 69.8 m), which is the difference between the quota and the Fund's króna-denominated deposits with the Bank, adjusted for the balance on the IMF's current account with the Bank. The SDR allocation totalled SDR 420.7 million at the end of 2021 (31.12.2020: SDR 112.3 m).

The International Monetary Fund (IMF) allocated special drawing rights (SDR) to its member countries on 23 August 2021, increasing Iceland's reserve holdings by SDR 308 million (56.2 b.kr. at the year-end exchange rate). The allocation increases the Central Bank's deposit balance with the IMF, which is a separate item on the Bank's balance sheet. It also increases the Bank's debt to the IMF by the same amount.

	31.12.2021		31.12.2020	
	SDR	ISK	SDR	ISK
<i>Assets</i>				
Central Bank of Iceland quota	321,800	58,728,500	321,800	59,162,930
IMF deposit with Central Bank of Iceland	(252,002)	(45,990,412)	(252,002)	(46,330,568)
IMF current account with Central Bank of Iceland	6	1,207	6	1,103
Central Bank foreign currency balance with IMF	69,804	12,739,295	69,804	12,833,465
Central Bank foreign currency balance with IMF	69,804	12,739,295	69,804	12,833,465
Central Bank deposit balance with IMF	421,917	76,999,682	113,245	20,857,231
Accrued interest	44	8,121	226	5,378
Balance with IMF	491,765	89,747,098	183,275	33,696,074
<i>Liabilities</i>				
Counterpart to IMF allocations	420,654	76,769,132	112,198	20,627,530
IMF current account with Central Bank of Iceland	6	1,207	6	1,103
Balance with IMF	420,660	76,770,339	112,204	20,628,633

### Note 17.3 – Foreign securities and other reserve assets

	31.12.2021	31.12.2020
Foreign securities	646,934,672	656,288,133
Foreign securities funds	1,666,416	1,517,47
Foreign securities and other reserve assets, total	648,601,088	657,805,606

### Changes in foreign securities and securities funds

	2021	2020
Balance at beginning of year	657,805,606	568,923,818
Purchases during the year	206,569,486	364,111,453
Sold and collected during the year	(175,192,112)	(279,899,931)
Change in accrued interest	(343,690)	(628,260)
Changes in premiums and discounts	(3,695,401)	(2,862,722)
Unrealised value adjustments	(12,285,499)	6,791,345
Exchange rate difference	(24,257,303)	1,369,903
Balance at end of year	648,601,088	657,805,606



## Note 17.4 – Non-reserve assets

Non-reserve assets consist of short-term claims against non-residents.

## Note 18 – Foreign-denominated claims against residents

Foreign-denominated claims against residents at the end of 2021 consisted solely of a euro-denominated account with a domestic commercial bank. The Central Bank had no foreign-denominated claims against residents at the end of 2020.

## Note 19 – Monetary policy-related claims against residents

### Note 19.1 – Treasury

Monetary policy-related claims against the Treasury consist solely of Treasury securities

#### Changes in foreign securities and securities funds

	2021	2020
Balance at beginning of year	7,770,361	-
Purchases during the year	15,481,336	7,779,958
Collected during the year	(200,000)	-
Change in accrued interest	(3,569)	(12,267)
Changes in premiums and discounts	(468,257)	(35,574)
Unrealised value adjustments	(745,030)	38,244
Balance at end of year	<u>21,834,841</u>	<u>7,770,361</u>

### Note 19.2 – Deposit institutions

Monetary policy-related claims against deposit institutions consist solely of support loans.

## Note 20 – Króna-denominated claims against residents

Claims on non-residents, króna-denominated consist solely of housing bonds.

### Note 20.1 – Deposit institutions

Claims against deposit institutions denominated in domestic currency consist of loans granted for participation in the cost of implementing the Central Bank of Iceland's interbank payment system.

## Note 20.2 – Other entities

Króna-denominated claims against other residents consist solely of housing bonds.

## Note 21 – Other assets

### Note 21.1 – Fixed operational assets

31.12.2021	Real estate	Liquid assets	Libraries and collections	Total
<i>Cost price and valuation</i>				
Cost price at beginning of year	4,929,088	385,935	310,572	5,625,595
Valuation at beginning of year	3,353,457	-	-	3,353,457
Special revaluation	(115,006)	-	-	(115,006)
Capitalised during the year	655,979	77,092	-	733,071
Balance at end of year	<u>8,823,518</u>	<u>463,027</u>	<u>310,572</u>	<u>9,597,117</u>
<i>Depreciation</i>				
Balance at beginning of year	875,808	174,254	-	1,050,062
Depreciation for the year	102,268	43,767	-	146,035
Balance at end of year	<u>978,076</u>	<u>218,021</u>	<u>-</u>	<u>1,196,097</u>
Book value at beginning of year	<u>7,406,737</u>	<u>211,681</u>	<u>310,572</u>	<u>7,928,990</u>
Book value at end of year	<u>7,845,442</u>	<u>245,006</u>	<u>310,572</u>	<u>8,401,020</u>
Annual depreciation rate	0-3%	10-33%	0%	

The official end-2021 property valuation of tangible operational assets was 6.2 b.kr.

The year-end insurance valuation of fixed operational assets was 9.5 b.kr.

31.12.2020	Real estate	Liquid assets	Libraries and collections	Total
<i>Cost price and valuation</i>				
Cost price at beginning of year	4,698,232	253,862	310,567	5,262,661
Valuation at beginning of year	3,477,568	-	-	3,477,568
Merger with Financial Supervisory Authority	-	50,968	5	50,973
Special revaluation	(124,111)	-	-	(124,111)
Capitalised during the year	230,856	112,760	-	343,616
Sold and discontinued during the year	-	(31,655)	-	(31,655)
Balance at end of year	<u>8,282,545</u>	<u>385,935</u>	<u>310,572</u>	<u>8,979,052</u>
<i>Depreciation</i>				
Balance at beginning of year	787,715	162,712	-	950,427
Depreciation for the year	88,093	40,987	-	129,080
Sold and discontinued during the year	-	(29,445)	-	(29,445)
Balance at end of year	<u>875,808</u>	<u>174,254</u>	<u>-</u>	<u>1,050,062</u>
Book value at beginning of year	<u>7,388,085</u>	<u>91,150</u>	<u>310,567</u>	<u>7,789,802</u>
Book value at end of year	<u>7,406,737</u>	<u>211,681</u>	<u>310,572</u>	<u>7,928,990</u>
Annual depreciation rate	0-3%	10-20%	0%	

The official end-2020 property valuation of tangible operational assets was 5.9 b.kr.

The year-end insurance valuation of fixed operational assets was 9.4 b.kr.

## Note 21.2 – Software

	2021	2020
<i>Cost price</i>		
Balance at beginning of year	1,296,783	1,555,780
Merger with Financial Supervisory Authority	-	2,140
Capitalised during the year	65,809	310,349
Sold and discontinued during the year	-	(571,486)
Balance at end of year	<u>1,362,592</u>	<u>1,296,783</u>
<i>Depreciation</i>		
Balance at beginning of year	313,185	787,773
Depreciation for the year	116,368	96,898
Sold and discontinued during the year	-	(571,486)
Balance at end of year	<u>429,553</u>	<u>313,185</u>
Book value at beginning of year	<u>983,598</u>	<u>768,007</u>
Book value at end of year	<u>933,039</u>	<u>983,598</u>

The depreciation rates for software are 10-20% for the group. The group does not begin to depreciate software until it is brought into use. The new interbank system was brought into use on 23 October 2020 and is depreciated from that date onwards. The group capitalised software developments work in

the amount of 160 m.kr. in connection with the implementation of a new function in the ARK system over the period 2018-2021. The group began to depreciate the software development work when the new function was brought into use in September 2021.

### Note 21.3 – Other assets

	31.12.2021	31.12.2020
Shareholdings in subsidiary outside the group	632,477	680,439
Shareholdings in company	200,000	-
Shareholdings in Bank for Int'l Settlements	184,486	184,486
Payment intermediation claims	375,605	352,244
Pre-paid expenses	187,462	207,739
Accounts receivable	111,682	236,757
Income tax credit	24,811	11,061
Investment tax withheld	1,032	1,833
Other assets	50,412	32,583
Other assets, total	<u>1,767,967</u>	<u>1,707,142</u>

### Shareholdings in subsidiary outside the group

	2021	2020
Balance at beginning of year	680,439	975,423
Dividends	-	(350,000)
Share capital reduction	(350,000)	-
Share in earnings	302,038	55,016
Balance at end of year	<u>632,477</u>	<u>680,439</u>

#### Shareholdings in company

Shareholdings in company consist of 8,795,075 shares in the Icelandic Banks' Data Centre (RB), the equivalent of 7.33% of RB shares.

#### Shareholdings in Bank for Int'l Settlements

Shareholdings in the Bank for International Settlements (BIS) are entered at cost price. The Central Bank owned 1,070 shares at the end of 2020. Each share has a nominal value of

SDR 5,000. Payment has been made for 25% of the nominal value, or SDR 1,250 per share. The book value at year-end 2021 was 184.5 m.kr., and the nominal value of the portion that has been paid is SDR 1.3 million. The Central Bank of Iceland is obliged to pay for a subscription for capital shares to the Bank for International Settlements (BIS) upon request. 25% of the subscription has already been paid. The 75% share could come due for payment and totalled 711.2 m.kr. (SDR 4 million) at the end of 2021.

## Income tax credit

	2021	2020
Balance at beginning of year	11,061	6,226
Calculated income tax for year	13,750	3,226
Other items	-	1,609
Balance at end of year	<u>24,811</u>	<u>11,061</u>

## Deferred tax is allocated as follows to individual balance sheet items:

	2021	2020
Tax loss carryforward	32,537	12,531
Fixed operational assets	( 7,714)	( 892)
Exchange rate difference	( 12)	( 27)
Accounts receivable	-	( 551)
Income tax credit, total	<u>24,811</u>	<u>11,061</u>

## Note 22 – Equity

### Callable capital

At the beginning of 2015, the Central Bank of Iceland and the Government entered into an agreement providing for callable capital for the Bank. With the agreement, the Treasury pledges, based on the authority contained in the National Budget, to contribute capital to the Central Bank in the form of marketable assets if the Bank calls in such capital so as to satisfy the minimum requirement for paid-in capital.

The total amount of callable capital was 58.3 b.kr. at the end of 2019. With the entry into force of the new Act on the Central Bank of Iceland, no. 92/2019, on 1 January 2020, the callable capital declined by 1.1 b.kr., to 57.2 b.kr. The balance of callable capital is adjusted at each year-end to reflect the rise in the consumer price index.

### Value adjustment reserve and transfer to the Treasury

The Bank's profit from the prior fiscal year, adjusted for unrealised calculated revenues and expenses, shall revert to the Treasury to the extent that it is not used to strengthen the Bank's capital position. The Bank is authorised to keep separate accounts in the equity accounts for unrealised revenues and expenses. The Bank has such an account, called the *Value adjustment reserve*, in its equity accounts. Unrealised revenues due to the share in the profits of subsidiaries in excess of divi-

dends received are recognised in the equity item *Unrealised share in profit of associates*.

The main objective of maintaining the value adjustment reserve is to ensure that only realised gains are used as the basis for the transfer to the Treasury or for the strengthening of the Bank's equity. Unrealised profits are entered to the value adjustment reserve. Unrealised losses in excess of previously entered unrealised gains are used to reduce the profit available for disposition.

The revaluation consists of updated market prices and currency exchange rate movements, and it extends to financial assets and liabilities, derivatives, and gold. Financial instruments denominated in domestic and foreign currencies are appraised individually.

Both realised and unrealised gains are recognised in the profit and loss account. Contributions to the value adjustment reserve consist of the difference between cost price and recorded market price. Both because of systemic changes and because there was no balance in the valuation adjustment reserve at the end of 2017, it was decided that the cost price should reflect the market price as of 31 December 2017.

The value adjustment reserve specifies as follows:

	2021	2020
Balance at beginning of year	67,056,063	55,126,282
Unrealised value adjustment of foreign securities	(16,348,410)	8,823,313
Value adjustment of domestic securities	(722,827)	291,187
Exchange rate difference on foreign assets	(35,399,622)	9,499,853
Exchange rate difference on gold	(192,144)	3,683,579
Realised during the year (transferred from value adjustment reserve to other equity)	14,916,997	(10,368,151)
Balance at end of year	<u>29,310,057</u>	<u>67,056,063</u>

Disposed of the following:

	2021	2020
(Loss) Profit for the year	(15,834,479)	68,253,447
Decrease (increase) in value adjustment reserve	37,746,006	(11,929,780)
(Increase) Decrease in restricted earnings	(197,792)	225,071
Allocation of profit for the year	<u>21,713,735</u>	<u>56,548,738</u>

According to the Act on the Central Bank of Iceland, the Bank shall have the financial strength to enable it to fulfil its legally mandated role. To this end, the Bank is required to set for itself a capital adequacy benchmark. The benchmark reflects the Bank's need for capital and interest-bearing assets and shall take into account the Bank's operating expenses and the risks and uncertainty it faces at any given time.

In 2021, the Bank's capital adequacy benchmark was set at 150 b.kr. The Bank's equity at the end of 2021 was 134.1 b.kr. The loss for the year according to the annual accounts is 15.8 b.kr. The value adjustment reserve decreased by 37.7 b.kr., and the restricted earnings account increased by 197.8 m.kr. The allocation for 2021 is 21.7 b.kr. Because the Bank's operations generated a loss in 2021 and the Bank's year-end equity was below the capital adequacy benchmark, the Bank will not pay a dividend to the Treasury in 2022.

Developments in the Bank's capital ratio

	31.12.2021	31.12.2020	31.12.2019	31.12.2018
Equity (excl. value adjustments)	126,932,619	143,472,039	74,440,977	51,923,012
Revaluation of assets	<u>7,117,895</u>	<u>7,330,069</u>	<u>7,540,925</u>	<u>6,411,632</u>
Equity	<u>134,050,514</u>	<u>150,802,108</u>	<u>81,981,902</u>	<u>58,334,644</u>
Equity ratio	13.9%	17.9%	9.8%	7.7%

#### Real estate revaluation

The Bank's real estate is designated at fair value. A fair value assessment is carried out annually. Valuation changes are entered to a separate revaluation reserve account among equity items. The revaluation reserve is reduced by an amount equivalent to the annual depreciation of the difference between the restated price and the cost price.

#### Restricted earnings

If the share in the earnings of a subsidiary exceeds dividends received from that company, the difference is entered as restricted earnings.



## Note 23 – Issued banknotes and coin

	31.12.2021	31.12.2020
<i>Banknotes</i>		
10,000 krónur	51,287,500	49,942,500
5,000 krónur	17,818,500	18,826,000
2,000 krónur	210,000	212,000
1,000 krónur	6,608,500	6,415,000
500 krónur	1,699,250	1,669,750
Banknotes, total	<u>77,623,750</u>	<u>77,065,250</u>
<i>Coin</i>		
100 krónur	2,811,300	2,791,400
50 krónur	736,040	730,190
10 krónur	620,400	620,560
5 krónur	133,259	132,779
1 króna	121,912	121,932
Coin, total	<u>4,422,911</u>	<u>4,396,861</u>
Issued banknotes and coin, total	<u>82,046,661</u>	<u>81,462,111</u>

## Note 24 – Foreign-denominated debt to non-residents

Foreign-denominated debt to non-residents consists of deposits and the counterpart to the IMF. Note 17.2 contains an explanation of matters relating to the IMF.

### Note 24.1 – Deposits

Foreign-denominated deposits with non-resident entities consist solely of euro-denominated deposits with international institutions.

## Note 25 – Foreign-denominated debt to residents

	31.12.2021	31.12.2020
Deposits – Treasury and Government institutions	304,564,191	214,152,243
Deposits – Other entities	10,891	11,561
Total	<u>304,575,082</u>	<u>214,163,804</u>

## Note 26 – Króna-denominated debt to non-residents

### Note 26.1 – Deposits

Non-residents' króna-denominated deposits consist entirely of deposits with international institutions.

### Note 26.2 – Certificates of deposit

Króna-denominated certificates of deposit held by non-residents derived from capital account liberalisation measures. They were redeemed in July 2021.

## Note 27 – Monetary policy-related debt to domestic credit institutions

### Note 27.1 – Deposits

	31.12.2021	31.12.2020
Real-time gross settlement accounts	77,783,576	61,544,062
Current accounts	-	115,023
Collateral accounts	883,419	4,352,781
Deposits, total	<u>78,666,995</u>	<u>66,011,866</u>

### Note 27.2 – Reserve requirements

Minimum reserve requirements consist of two parts: a fixed non-remunerated 1% reserve requirement and an average reserve requirement, which is included with deposits under *Monetary policy-related debt to domestic credit institutions*.

In the Monetary Policy Committee's 11 March 2020 statement, it was announced that the Committee had decided to lower the average reserve requirement to 0% but maintain the fixed reserve requirement at 1%.

### Note 27.3 – Term deposits

	31.12.2021	31.12.2020
Seven-day term deposits	166,128,457	107,362,237
Term deposits, > 1 month	2,911,899	5,586,566
Term deposits, total	<u>169,040,355</u>	<u>112,948,802</u>

The Central Bank decided in mid-2020 to stop offering one-month term deposits.

A new type of term deposit with a commitment period longer than one month was introduced in 2020, in order to provide collateral for payment system overdrafts.

### Note 27.4 – Certificates of deposit

Certificates of deposit derived from capital account liberalisation measures. They were redeemed in July 2021.

## Note 28 – Króna-denominated debt to residents

### Note 28.1 – Treasury and Government institutions

	31.12.2021	31.12.2020
Deposits	67,636,700	142,098,010
Other liabilities	195,827	191,332
Total	<u>67,832,527</u>	<u>142,289,342</u>

### Note 28.2 – Other entities

	31.12.2021	31.12.2020
Deposits	4,159,270	2,631,228
Other liabilities	-	5,231
Total	<u>4,159,270</u>	<u>2,636,459</u>

## Note 29 – Other liabilities

	31.12.2021	31.12.2020
Vacation pay obligation	652,643	665,716
Unpaid salaries and related expenses	52,474	50,643
Pension obligations	66,312	162,676
Trade credit	150,177	186,329
Pre-paid income	468,726	-
Pre-paid purchase price for sale of systems	270,000	-
Other liabilities	1,743	6,440
Other liabilities, total	<u>1,662,075</u>	<u>1,071,804</u>

### Unpaid salaries and related expenses

Unpaid salaries and related expenses that are included with other liabilities consist of debt to pension funds and labour unions. Unpaid payroll tax and pay-as-you-earn tax are included with debts to the Treasury under *Króna-denominated debt to residents*.

### Pension obligations

According to actuarial assessments, the Central Bank of Iceland's obligations due to pension payments to former governors and their spouses totalled 66.3 m.kr. as of year-end 2021. Payments related to these obligations totalled 30.2 m.kr. in 2021 and reduce the previously entered obligation. Reductions in the Bank's obligations, after adjusting for payments, totalled 66.1 m.kr. in 2021 and are capitalised.

### Changes during the year specify as follows:

	2021	2020
Pension obligations at beginning of year	162,676	174,487
Paid due to retirement	(30,215)	(30,328)
Change during the year	(66,149)	18,517
Pension obligations at end of year	<u>66,312</u>	<u>162,676</u>

### Pre-paid purchase price for sale of systems

On 10 December 2021, the group signed an agreement with the Icelandic Banks' Data Centre (RB) concerning the sale of the ARK system and RB's SWIFT service. The purchase price was

paid with RB shares and cash in December 2021. Delivery of the systems took place on 1 January 2022. The gain on the sale of the systems, which will be capitalised in 2022, totals 108 m.kr.

## Other information

### Note 30 – The króna system

	31.12.2021	31.12.2020
Deposit institutions	247,707,350	178,960,668
Financial institutions	1,021,926	21,844
Treasury	67,636,731	142,103,288
Non-residents	5,545,158	2,493,654
Other entities	3,138,009	1,939,787
Payment systems	375,605	352,244
Issued banknotes and coin	82,046,661	81,462,111
Total	<u>407,471,440</u>	<u>407,333,595</u>

The table shows total term deposits and sight deposits, issued banknotes and coin, and outstanding payment system balances at the year-end.

### Note 31 – Foreign exchange transactions

Foreign exchange transactions against the króna in 2021, in ISK thousands

	<i>Purchases</i>	<i>Sales</i>	<i>Total</i>
Euro (EUR)	20,999,400	(51,911,884)	(30,912,484)
US dollar (USD)	<u>5,856,814</u>	<u>(688,245)</u>	<u>5,168,569</u>
Total	<u>26,856,214</u>	<u>(52,600,129)</u>	<u>(25,743,915)</u>

### Cross-border payments by the Central Bank and its customers in 2021, in ISK thousands

	<i>Incoming payments</i>	<i>Outgoing payments</i>	<i>Total</i>
Euro (EUR)	119,381,217	(11,695,584)	107,685,633
US dollar (USD)	6,294,886	(8,708,494)	(2,413,608)
Pound sterling (GBP)	74,227	(428,690)	(354,463)
Japanese yen (JPY)	42,992	(138,045)	(95,053)
Danish krone (DKK)	61,469	(574,907)	(513,438)
Norwegian krone (NOK)	1,960	(165,813)	(163,853)
Swedish krona (SEK)	88,323	(252,683)	(164,360)
Swiss franc (CHF)	208,029	(318,594)	(110,565)
Canadian dollar (CAD)	1,526	(108,011)	(106,485)
<b>Total</b>	<b>126,154,629</b>	<b>(22,390,821)</b>	<b>103,763,808</b>

### Foreign exchange transactions against the krona in 2020, in ISK thousands

	<i>Purchases</i>	<i>Sales</i>	<i>Total</i>
Euro (EUR)	11,702,237	(149,426,928)	(137,724,691)
US dollar (USD)	35,769	(801,138)	(765,370)
Pound sterling (GBP)	110,830	-	110,830
Danish krone (DKK)	535	-	535
Norwegian krone (NOK)	18,333	-	18,333
<b>Total</b>	<b>11,867,704</b>	<b>( 150,228,066)</b>	<b>(138,360,362)</b>

### Cross-border payments by the Bank and its customers in 2020, in ISK thousands

	<i>Incoming payments</i>	<i>Outgoing payments</i>	<i>Total</i>
Euro (EUR)	1,577,101	(6,098,449)	(4,521,348)
US dollar (USD)	12,867	(6,325,994)	(6,313,128)
Pound sterling (GBP)	8,628	(873,644)	(865,016)
Japanese yen (JPY)	-	(567,668)	(567,668)
Danish krone (DKK)	36,893	(583,076)	(546,183)
Norwegian krone (NOK)	788	(149,854)	(149,067)
Swedish krona (SEK)	330	244	574
Swiss franc (CHF)	244,303	(354,478)	(110,176)
Canadian dollar (CAD)	132	(93,889)	(93,756)
<b>Total</b>	<b>1,881,042</b>	<b>(15,046,809)</b>	<b>(13,165,766)</b>

## Note 32 – Related parties

Related parties are the State (owner of the Central Bank of Iceland), F fasteignafélag ehf. (a subsidiary outside the group), the Governor, senior management, and the Supervisory Board.

Positions and transactions and all unrealised revenues and expenses between companies in the group are omitted from both the consolidated financial statements and this explanatory note.

### Treasury

Interest income and expense vis-à-vis the Treasury specify as follows:

	2021	2020
Interest income from Treasury securities	496,022	23,276
Interest expense on current accounts	1,873,680	3,501,006
Interest expense on FX-accounts	78	542
Interest expense on derivatives contracts	-	225,255
Interest expense vis-à-vis the Treasury, total	<u>1,873,757</u>	<u>3,726,802</u>
Net interest expense vis-à-vis the Treasury	<u>( 1,377,735)</u>	<u>( 3,703,527)</u>

Net interest-bearing assets specify as follows:

	31.12.2021	31.12.2020
Treasury bonds	21,834,841	7,770,361

Net interest-bearing debt specifies as follows:

	31.12.2021	31.12.2020
Treasury and Government institutions' deposits	67,832,527	142,289,342
Treasury FX account	<u>304,564,191</u>	<u>214,152,243</u>
Total	<u>372,396,718</u>	<u>356,441,585</u>

### F fasteignafélag ehf. (subsidiary outside the group)

The group conducted no business with F fasteignafélag ehf. in 2020-2021. F fasteignafélag ehf. paid the Bank 350 m.kr. due to a share capital reduction in 2021 and paid the Bank a 350 m.kr. dividend in 2020.

The group had a claim against F fasteignafélag ehf. in the amount of 1,390 m.kr. at the end of 2019, which F fasteignafélag ehf. paid to the group in 2020. F fasteignafélag ehf. had no claims against the group at the end of 2021 or 2020.



### Governor, senior management, and Supervisory Board

In 2021, total remuneration to the Governor, senior management, and the Supervisory Board amounted to 435 m.kr. The Governor is not remunerated for participation in boards and committees jointly operated by institutions in

the financial market or to which the Central Bank of Iceland appoints a representative by law. Total remuneration to the Governor, senior management, and the Supervisory Board in 2021 specifies as follows:

	2021	2020
<i>Governor</i>		
Ásgeir Jónsson	27,757	25,078
<i>Deputy Governors</i>		
Rannveig Sigurdardóttir, Monetary Policy	26,224	24,203
Gunnar Jakobsson, Financial Stability, from 1 March 2020 onwards	22,854	17,692
Unnur Gunnarsdóttir, Financial Supervision	24,840	23,049
<i>Senior management</i>		
Principal officers <sup>1</sup>	312,251	319,623
<i>Supervisory Board</i>		
Gylfi Magnússon, chair	4,800	3,804
Thórunn Gudmundsdóttir, vice-chair	3,600	2,853
Other Supervisory Board members and alternates	12,200	9,727
<b>Total remuneration to Governor, senior management, and Supervisory Board</b>	<b>434,526</b>	<b>426,029</b>

1. Directors as of year-end 2021: Thórarinn G. Pétursson, Director, Economics and Monetary Policy; Sturla Pálsson, Director, Markets; Haukur C. Benediktsson, Director, Financial Stability; Elmar Ásbjörnsson, Director, Banking; Rúnar Gudmundsson, Director, Pensions and Insurance; Páll Fridriksson, Director, Markets and Business Conduct; Björk Sigurgísladóttir, Director, Compliance and Inspections; Rannveig Jóníusdóttir, Director, General Secretariat; Thóra Helgadóttir, Director, Operations; Logi Ragnarsson, Director, IT and Statistics; Erla Gudmundsdóttir, Director, Finance; Íris Guðrún Ragnarsdóttir, Director, Human Resources; and Vigdís Ósk Helgadóttir, Director, Greidsluveitan ehf.

### Note 33 – Cost analysis

2021	Salaries and related expenses	Other operating expenses and depreciation	Service expenses	Joint expenses	Total
Senior management	800,384	87,274	-	( 887,657)	-
Monetary policy	892,753	466,370	484,882	1,691,076	3,535,080
Financial stability	457,818	27,244	-	796,608	1,281,671
Financial Supervision	1,228,669	115,250	-	1,172,011	2,515,930
Support departments	1,371,561	1,400,422	55	( 2,772,037)	-
Greidsluveitan	170,158	84,881	189,593	-	444,632
<b>Total</b>	<b>4,921,342</b>	<b>2,181,442</b>	<b>674,529</b>	<b>-</b>	<b>7,777,313</b>

2020	Salaries and related expenses	Other operating expenses and depreciation	Service expenses	Joint expenses	Total
Senior management	680,865	81,112	-	( 734,351)	27,626
Monetary policy	919,285	223,240	293,474	1,241,176	2,677,175
Financial stability	447,970	24,050	-	614,392	1,086,412
Financial Supervision	1,238,257	89,825	-	1,089,673	2,417,755
Support departments	1,677,373	1,207,400	39	( 2,210,891)	673,922
Greidsluveitan	182,786	103,633	243,389	-	529,808
<b>Total</b>	<b>5,146,535</b>	<b>1,729,260</b>	<b>536,903</b>	<b>-</b>	<b>7,412,698</b>

## Note 34 – Financial supervision

	2021	2020
Supervisory revenues	2,130,215	2,359,005
Salaries and related expenses	(1,228,669)	(1,238,257)
Other operating expenses	(115,250)	(89,825)
Joint expenses	(1,172,011)	(1,089,673)
Operating loss for the year	<u>(385,715)</u>	<u>(58,750)</u>

According to the Act on the Payment of Expenses for Official Supervision of Financial Activities and Resolution, no. 99/1999, operating surpluses and losses shall be taken into account in the determination of the supervision fee. At the time of the merger with the Central Bank of Iceland on 1 January 2020, the Financial Supervisory Authority's equity totalled 690.9 m.kr.

The Central Bank financial supervisory authority recorded an operating loss of 385.7 m.kr. in 2021 (2020: 58.8 m.kr.). The financial supervisory authority's cumulative operating surplus was therefore 246.1 m.kr. at the end of 2021 (31.12.2021: 632.1 m.kr.). The cumulative operating surplus has been taken into account in the determination of supervision fees for 2022.

## Note 35 – Other matters

The impact of the COVID-19 pandemic could be felt in the foreign exchange market during the year. The Central Bank conducted transactions in the foreign exchange market in order to mitigate volatility as it deemed warranted, and to improve price formation in the market, albeit to a much lesser degree than in the previous year.

The Central Bank has access to loan facilities from the Bank for International Settlements in the form of securities repurchase agreements, in the amount of 400 million US dollars, or 52.1 b.kr. at the end-2021 exchange rate. The Bank did not use these facilities in 2020 or 2021.

## Note 36 – Events after the financial reporting date

No events occurred after the financial reporting date that call for corrections or additions to the consolidated annual accounts for the year ended 31 December 2021.

## Risk management

The Central Bank of Iceland is a public institution that, by law, has a specific role focusing primarily on monetary policy, via its interest rate decisions and the investment of the nation's international reserves. Risk in its operations is therefore of a somewhat different type than in the operation of financial institutions, although the same terminology is used. The Central Bank of Iceland's financial risk entails claims risk, liquidity risk, and market risk. Claims risk is the risk of loss due to counterparties' or issuers' inability to fulfil their financial obligations at the designated time. Claims risk comprises issuer risk/counterparty risk and settlement risk. Liquidity risk is the risk that the Central Bank will be unable to fulfil its tasks and commitments due to insufficient assets, inability to sell assets in time, or inability to

sell assets except at significant discounts. Market risk is defined as the risk of loss due to changes in the market value of financial assets and liabilities. Market risk comprises exchange rate risk, interest rate risk, and gold price risk. In addition, the Bank operates under operational risk, which is the risk of human error or the failure of internal processes and systems.

The assets side of the Central Bank's consolidated accounts consists primarily of foreign assets, which are held in the Bank's international reserves, and domestic financial assets that are either issued or guaranteed by the Treasury. The following is a statement on the main financial risk of the Central Bank, which is primarily due to the international reserves.

## Note 37 – International reserves

The international reserves are managed in accordance with rules of procedure on the maintenance of the reserves, which were updated in October 2021. The rules specify the purpose and structure of the reserves, as well as defining the outside limits for

acceptable financial risk. The investment mandate, which is set on the basis of the rules, stipulates how reserve management shall be carried out.

## Note 38 – Claims risk

Below is an itemisation of the Bank's international reserves, by type, credit rating, country of issuance, and issuer/counterparty.

### International reserves, by issuer/counterparty

	31.12.2021	31.12.2020
Treasuries	48.9%	53.1%
Government institutions	14.1%	15.2%
Multinational institutions	4.8%	8.8%
Federal states	2.1%	2.7%
Financial institutions	0.4%	0.7%
Deposits with central banks and BIS	18.2%	13.3%
Deposits with IMF	9.7%	4.1%
Deposits with financial institutions	0.2%	0.1%
Gold	1.6%	1.9%
Total	100%	100%

### Credit ratings of issuers/counterparties in international reserves

	31.12.2021	31.12.2020
AAA	71.4%	67.2%
AA+	7.7%	7.3%
AA	10.9%	8.7%
AA-	4.7%	8.6%
A+	0.0%	0.0%
A	1.2%	1.0%
A-	2.0%	4.7%
BBB+	0.3%	0.5%
BBB	0.0%	0.1%
Gold	1.6%	1.9%
Total	100%	100%

Deposits with central banks and the Bank for International Settlements in the foreign exchange reserves comprise 18% of the reserves. In general, central banks are not assigned credit ratings, and their creditworthiness is deemed to be the same as that of the sovereign. It is assumed that the Bank for International Settlements has a credit rating of AAA.

Deposits with commercial banks in the foreign exchange reserves generally account for less than 1% of the reserves and are in various currencies at various banks. The Bank attempts to keep these deposits at a minimum (counterparty risk).

## International reserves, by country of issuer/counterparty

	<i>Credit rating</i>	<i>31.12.2021</i>	<i>31.12.2020</i>
Germany	AAA	30.3%	23.5%
US	AAA	23.8%	26.5%
Multinational institutions	AAA	17.0%	14.0%
France	AA	11.2%	9.2%
UK	AA-	3.9%	7.8%
Netherlands	AAA	3.6%	5.3%
Austria	AA+	2.9%	2.5%
Canada	AA+	1.4%	1.7%
Spain	A-	1.2%	1.0%
Japan	A	1.0%	3.3%
Ireland	A+	0.5%	0.6%
Sweden	AAA	0.5%	0.7%
Belgium	AA-	0.3%	0.4%
Finland	AA+	0.3%	0.8%
Denmark	AAA	0.3%	0.4%
China	A+	0.2%	0.2%
Switzerland	AAA	0.0%	0.0%
Luxembourg	AAA	0.0%	0.0%
Norway	AAA	0.0%	0.3%
Bank for International Settlements (BIS) <sup>1</sup>	AAA	0.0%	0.0%
Gold		1.6%	1.9%
Total		<u>100.0%</u>	<u>100.0%</u>

1. The Bank for International Settlements is owned by a large number of central banks and is therefore not classified under a given country.

## Note 39 – Liquidity risk

Liquidity risk is the risk that the Central Bank will be unable to fulfil its tasks and commitments due to insufficient assets, inability to sell assets in time, or inability to sell assets except at significant discounts. The vast majority of the Bank's foreign exchange reserves are invested in highly liquid securities, deposits in central banks, and deposits with the Bank for International Settlements. Highly liquid assets are defined as bonds issued by the state in the state's own currency, and deposits with the central banks in these countries/regions or the

Bank for International Settlements, denominated in US dollars or euros. Issuers of securities must have a minimum credit rating of AA in order for the securities to be classified as highly liquid assets. Highly liquid assets accounted for 59% of the Central Bank's international reserves at the end of 2021, as opposed to 53% at the end of 2020.

The following tables specify the Central Bank's total assets and liabilities, by maturity. The tables show the difference based on foreign and domestic maturities.

### Outstanding balance of financial assets and liabilities, 31 December 2021

	Available for withdrawal	< 3 months	3-12 months	1-5 years	> 5 years	Total
Gold	15,211,571	-	-	-	-	15,211,571
Claims on non-residents, foreign-denominated	895,350,257	12,477,366	-	-	-	907,827,623
Foreign bank deposits	157,001,557	12,477,366	-	-	-	169,478,923
Balance with IMF	89,747,098	-	-	-	-	89,747,098
Foreign sec. and other reserve assets	648,601,088	-	-	-	-	648,601,088
Non-reserve assets	514	-	-	-	-	514
Foreign-denominated claims against residents	781	-	-	-	-	781
Monetary policy-related claims against residents	21,834,841	1,811,644	-	-	-	23,646,485
Króna-denominated claims against residents	5,980,855	-	-	-	-	5,980,855
Other assets	1,320,796	-	-	-	184,486	1,505,282
	<u>939,699,101</u>	<u>14,289,010</u>	<u>-</u>	<u>-</u>	<u>184,486</u>	<u>954,172,597</u>
Banknotes and coin	82,046,661	-	-	-	-	82,046,661
Foreign-denominated debt to non-residents	89,371,007	-	-	-	-	89,371,007
Foreign-denominated debt to residents	304,575,082	-	-	-	-	304,575,082
Króna-denominated debt to non-residents	5,546,351	-	-	-	-	5,546,351
Deposits	5,546,351	-	-	-	-	5,546,351
Monetary policy-related debt to domestic credit institutions	78,666,995	195,858,859	-	-	-	274,525,854
Deposits	78,666,995	-	-	-	-	78,666,995
Reserve requirements	-	26,818,504	-	-	-	26,818,504
Term deposits	-	169,040,355	-	-	-	169,040,355
Króna-denominated debt to residents	71,991,797	-	-	-	-	71,991,797
Other liabilities	1,743	231,946	740,529	417,857	-	1,392,075
	<u>632,199,636</u>	<u>196,090,805</u>	<u>740,529</u>	<u>417,857</u>	<u>-</u>	<u>829,448,827</u>
Net outstanding in foreign currency	<u>516,616,520</u>	<u>12,477,366</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>529,093,886</u>
Net outstanding in domestic currency	<u>(209,117,055)</u>	<u>(194,279,161)</u>	<u>(740,529)</u>	<u>(417,857)</u>	<u>184,486</u>	<u>(404,370,116)</u>
Net outstanding	<u>307,499,465</u>	<u>(181,801,795)</u>	<u>(740,529)</u>	<u>(417,857)</u>	<u>184,486</u>	<u>124,723,770</u>

Analysis of outstanding financial assets and liabilities, 31 December 2020

	Available for withdrawal	< 3 months	3-12 months	1-5 years	> 5 years	Total
Gold	15,403,715	-	-	-	-	15,403,715
Foreign-denominated claims against non-residents	796,075,644	5,393,704	-	-	-	801,469,348
Foreign bank deposits	104,492,911	5,393,704	-	-	-	109,886,615
Balance with IMF	33,696,074	-	-	-	-	33,696,074
Foreign securities and other reserve assets	657,805,606	-	-	-	-	657,805,606
Non-reserve assets	81,053	-	-	-	-	81,053
Króna-denominated claims against residents	5,808,631	-	-	-	-	5,808,631
Other assets	1,271,273	-	-	-	184,486	1,455,759
	<u>826,329,624</u>	<u>7,143,092</u>	<u>0</u>	<u>0</u>	<u>184,486</u>	<u>833,657,202</u>
Banknotes and coin	81,462,111	-	-	-	-	81,462,111
Foreign-denominated debt to non-residents	30,555,938	-	-	-	-	30,555,938
Foreign-denominated debt to residents	214,163,804	-	-	-	-	214,163,804
Króna-denominated debt to non-residents	2,494,998	-	-	-	6,767,366	9,262,364
Deposits	2,494,998	-	-	-	-	2,494,998
Certificates of deposit	-	-	-	-	6,767,366	6,767,366
Monetary policy-related debt to domestic credit institutions	66,011,866	137,436,114	-	-	7,129,263	210,577,243
Deposits	66,011,866	-	-	-	-	66,011,866
Reserve requirements	-	24,487,312	-	-	-	24,487,312
Term deposits	-	112,948,802	-	-	-	112,948,802
Certificates of deposit	-	-	-	-	7,129,263	7,129,263
Króna-denominated debt to residents	144,925,801	-	-	-	-	144,925,801
Other liabilities	6,440	236,972	665,716	162,676	-	1,071,804
	<u>539,620,958</u>	<u>137,673,086</u>	<u>665,716</u>	<u>162,676</u>	<u>13,896,629</u>	<u>692,019,065</u>
Net outstanding in foreign currency	<u>566,759,617</u>	<u>5,393,704</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>572,153,321</u>
Net outstanding in domestic currency	<u>(280,050,951)</u>	<u>(135,923,698)</u>	<u>(665,716)</u>	<u>(162,676)</u>	<u>(13,712,143)</u>	<u>( 430,515,184)</u>
Net outstanding	<u>286,708,666</u>	<u>(130,529,994)</u>	<u>(665,716)</u>	<u>(162,676)</u>	<u>(13,712,143)</u>	<u>141,638,137</u>

## Note 40 – Settlement risk

Settlement risk is the risk that settlement will not take place as expected; for instance, if a counterparty does not deliver securities when the Bank has delivered payment, etc. Because of the low number of transactions, settlement risk in the international reserves is generally very limited. The largest

transactions are usually bond trades, which are not settled by a securities depository until both securities and payment are delivered; therefore, settlement risk is limited. The Bank's framework for claims risk and liquidity risk sets boundaries for settlement risk.



## Note 41 – Market risk

### Exchange rate risk

Exchange rate risk is the risk of loss due to changes in the exchange rate of foreign currencies vis-à-vis the Icelandic króna. Attempts are made to minimise the exchange rate risk in the Bank's international reserves at all times by keeping a portion of the assets in the same currencies and the same amounts

as the Bank's and the Treasury's foreign liabilities, insofar as is possible. The exchange rate risk exposure of the Bank's net foreign exchange assets (foreign exchange balance) is then kept in a given currency composition. The Bank may use derivatives to manage its exchange rate risk. The Central Bank's foreign exchange balance was as follows at year-end 2021 and 2020:

### Currencies in financial assets and liabilities 31 December 2021

	<i>Euro</i>	<i>US dollar</i>	<i>Pound sterling</i>	<i>Yen</i>	<i>Gold and other currencies</i>	<i>Total</i>
<i>Assets</i>						
Gold					15,211,571	15,211,571
Foreign-denominated claims against non-residents	518,871,339	308,034,959	53,553,820	15,691,537	11,675,968	907,827,623
Foreign bank deposits	146,127,531	13,196,828	1,729,791	8,215,604	209,169	169,478,923
Balance with IMF	27,758,777	37,451,464	7,260,540	7,475,933	9,800,383	89,747,098
Foreign securities and other reserve assets	344,985,031	257,386,152	44,563,488	-	1,666,416	648,601,088
Non-reserve assets	-	514	-	-	-	514
Other assets	69,803	27,763	7,021	-	2,421	107,009
Assets, total	<u>518,941,143</u>	<u>308,062,722</u>	<u>53,560,841</u>	<u>15,691,537</u>	<u>26,889,960</u>	<u>923,146,203</u>
<i>Liabilities</i>						
Foreign-denominated debt to non-residents	36,346,568	32,035,759	6,210,623	6,394,869	8,383,189	89,371,007
Deposits	12,601,875	-	-	-	-	12,601,875
Counterpart to IMF	23,744,693	32,035,759	6,210,623	6,394,869	8,383,189	76,769,132
Foreign-denominated debt to residents	304,311,775	155,822	66,465	41,012	7	304,575,082
Other liabilities	5,608	2,901	1	-	44	8,554
Liabilities, total	<u>340,663,951</u>	<u>32,194,482</u>	<u>6,277,089</u>	<u>6,435,881</u>	<u>8,383,240</u>	<u>393,954,644</u>
Net assets	<u>178,277,192</u>	<u>275,868,240</u>	<u>47,283,752</u>	<u>9,255,656</u>	<u>18,506,720</u>	<u>529,191,559</u>

## Currencies in financial assets and liabilities 31 December 2020

	<i>Euro</i>	<i>US dollar</i>	<i>Pound sterling</i>	<i>Yen</i>	<i>Gold and other currencies</i>	<i>Total</i>
<i>Assets</i>						
Gold					15,403,715	15,403,715
Foreign-denominated claims against non-residents	359,655,561	317,374,001	91,281,457	27,699,601	5,458,728	801,469,348
Foreign bank deposits	77,645,399	5,586,333	1,435,056	25,007,973	211,854	109,886,615
Balance with IMF	11,029,176	13,628,462	2,698,460	2,691,628	3,648,348	33,696,074
Foreign securities and other reserve assets	270,980,986	298,159,206	87,147,941	-	1,517,473	657,805,606
Non-reserve assets					81,053	81,053
Other assets	108,153	24,871	5,842	-	-	138,866
Assets, total	<u>359,763,714</u>	<u>317,398,872</u>	<u>91,287,299</u>	<u>27,699,601</u>	<u>20,862,443</u>	<u>817,011,929</u>
<i>Liabilities</i>						
Foreign-denominated debt to non-residents	16,679,333	8,343,302	1,651,989	1,647,806	2,233,508	30,555,938
Deposits	9,927,305					9,927,305
Counterpart to IMF	6,752,028	8,343,302	1,651,989	1,647,806	2,233,508	20,628,633
Foreign-denominated debt to residents	214,012,492	150,190	1,115	-	7	214,163,804
Other liabilities	1,229	1,564	1	-	-	2,794
Liabilities, total	<u>230,693,054</u>	<u>8,495,056</u>	<u>1,653,105</u>	<u>1,647,806</u>	<u>2,233,515</u>	<u>244,722,536</u>
Net assets	<u>129,070,660</u>	<u>308,903,816</u>	<u>89,634,194</u>	<u>26,051,795</u>	<u>18,628,928</u>	<u>572,289,393</u>

### Interest rate risk

Interest rate risk is the risk of loss due to changes in market interest rates. The Bank's investment strategy aims at enabling the Bank to be able to fulfil its tasks and commitments at all times. As a consequence, the Bank attempts to invest in foreign assets that are liquid and issued by reliable parties. However, returns are also considered. Interest rate risk in foreign currencies is reduced by using assets to offset liabilities.

### Gold price risk

Gold is a part of the international reserves, and changes in its market price therefore constitute a risk for the Bank. Gold does not comprise a large share of the reserves, however; the Bank owns about 64,000 ounces of gold, or 1.6% of the international reserves as of 31 December 2021. The Bank did not loan gold to other financial institutions during the year.

## Note 42 – Risk relating to domestic market transactions and deposits

The Bank's market transactions with domestic financial institutions are of two types: short-term collateralised loans granted by the Bank to financial institutions, and financial institutions' deposits with the Bank.

The claims risk attached to Central Bank loan facilities is negligible. Collateral accepted by the Central Bank for loan facilities includes Treasury bonds, Government-guaranteed bonds, and covered bonds. The Central Bank grants loans for short periods of time. If a counterparty is unable to repay the loan, the Bank retains the underlying collateral. The Bank always takes delivery of the collateral before granting the loan

and does not return it until the loan has been repaid. As a result, its settlement risk is negligible.

Market risk is limited. The Bank monitors the market price of collateral it accepts for loans or as payment system collateral. A haircut is always taken from the market price before the loan is granted. In case of a change in the market price of assets, the Bank may require immediate delivery of additional collateral.

The Central Bank's liquidity risk in connection with domestic market transactions and deposits is negligible, as all regular transactions with financial institutions are in Icelandic krónur.

## Important accounting principles

### Note 43 – Important accounting principles

#### Note 43.1 – Foreign currencies

Transactions in foreign currencies are entered at the exchange rate on the date the transaction takes place. Monetary assets and liabilities in foreign currencies are entered at the central exchange rate at the close of the day on the financial reporting date. Exchange rate differences that are created are recognised in the profit and loss account.

#### Note 43.2 – Portfolio investment

Securities are recognised at fair value, and valuation changes are recognised in the profit and loss account. All of the Bank's securities are listed on active securities exchanges. The Bank estimates the fair value of securities based on the listed price on an active securities exchange on the financial reporting date.

#### Note 43.3 – Interest income and expense

Interest income is recognised in the profit and loss account, using the effective interest rate method. The effective interest rate is the rate that discounts estimated future cash flows on a financial instrument over its expected life or a shorter period, as applicable, to the book value of the instrument concerned. The calculation of the effective interest rate takes account of all contractual terms and conditions applying to the financial instrument, as well as transaction costs, premia, and discounts.

The effective interest rate is determined when the financial instrument is initially recognised and is not updated.

#### Note 43.4 – Supervisory revenues, service revenues, and other revenues

Supervisory revenues, service revenues, and other revenues are entered when accrued. Income received during the accounting year but relating to a subsequent accounting year is expensed in the balance sheet as deferred income. Income relating to the accounting year but received after the year-end is capitalised in the balance sheet.

#### Note 43.5 – Entry of fees

Expenses incurred in connection with acquisition of income during the period are recognised as operating expenses. Expenses incurred during the accounting year but relating to a subsequent accounting year are capitalised in the balance sheet as prepaid expenses. Expenses relating to the accounting year but payable in a subsequent accounting year are expensed in the balance sheet as accrued expenses.

#### Note 43.6 – Taxation

Income tax is calculated and entered in the annual financial statements. Its calculation is based on earnings before taxes, adjusted for permanent differences between taxable earnings and earnings according to the annual accounts. The income tax rate is 20%.

Income tax payable is income tax that is estimated to become due and payable in the next year due to taxable profit for the year, plus an adjustment of income tax payable for previous years.

Deferred tax derives from the difference between balance sheet items in the tax settlement, on the one hand, and the annual accounts, on the other. The difference stems from the fact that the group's income tax base is obtained by means other than those used in the preparation of the annual accounts.

The income tax credit is assessed on the financial reporting date and is only recognised to the extent that it is likely to be used to offset taxable profit in the future.

#### Note 43.7 – Fixed operational assets

Assets are listed among fixed operational assets when it is likely that the economic benefits of the asset concerned will be useful to the group and when it is possible to estimate the cost due to the asset in a reliable manner. Fixed operational assets are recognised using either the cost-price method or the revaluation method.

According to the cost-price method, fixed operational assets are entered at original cost price less accumulated depreciation and impairment. The cost price of fixed operational assets consists of the purchase price and all direct costs relating to putting the asset into revenue-generating condition.

The revaluation method uses fair value on the date the fixed operational assets are revalued, less depreciation and impairment. Upward value adjustments due to revaluation are entered to the revaluation reserve account as equity. When an asset is sold, depreciated, or scrapped, the portion of the revaluation reserve account that pertains to that asset is recognised as retained earnings.

Fixed operational assets are depreciated linearly over their estimated useful life, after adjusting for their expected scrap value. Profit or loss due to the sale of assets is the difference between the sale price and the book value of the asset on the date of sale and is recognised in the profit and loss account at the time of the sale.

#### Note 43.8 – Intangible assets

Intangible assets are capitalised only when it is deemed likely that the economic benefits of the assets concerned will be useful to the group and when it is possible to estimate the cost associated with the assets in a reliable manner. The group's intangible assets consist solely of software. Intangible assets are depreciated linearly over their expected useful life, after adjusting for their expected scrap value. Profit or loss due to the sale of assets is the difference between the sale price and the book value of the asset on the date of sale and is recognised in the profit and loss account at the time of the sale.

#### Note 43.9 – Impairment of non-financial assets

On the financial reporting date, the book value of assets is estimated with a view to impairment. If there is an indication of impairment, the recoverable value of the asset is estimated so as to make it possible to determine the impairment amount (if any).

Recoverable value is either the asset's net selling price or its value in use, whichever is higher. Impairment is recognised in the profit and loss account if the book value of the asset or income-generating unit is higher than its expected recoverable value. If previously recognised impairment no longer applies, the book value of the asset is increased again, but not to a level above the original cost price or depreciated cost price if the asset has a limited useful life. Impairment of goodwill cannot be reversed.

#### Note 43.10 – Gold

The gold held in the Bank's international reserves is recognised as a foreign asset denominated in gold as a currency, and changes in the value of gold are recognised as exchange rate differences in the profit and loss account.

#### Note 43.11 – Issued banknotes and coin

Issued banknotes and coin are recognised at nominal value.

#### Note 44.12 – Obligations

Obligations are written up in the balance sheet if it is considered likely that the group will be faced with financial expense in the future due to a specified event or transaction and it is possible to assess the monetary amount in a reliable manner.

# Appendix



## Press releases from the Central Bank of Iceland 2021

No.		No.	
1	13 January Statement of the Financial Supervision Committee 13 January 2021	11	31 March Announcement concerning Central Bank purchases of Treasury bonds
2	15 January Foreign exchange market, exchange rate developments, and international reserves 2020	12	14 April Statement of the Financial Stability Committee 14 April 2021
3	21 January Nordic-Baltic countries engage the IMF to conduct an analysis of cross-border money laundering and terrorist financing risks in the region	13	30 April Central Bank discontinues regular foreign currency sales
4	29 January Central Bank to continue regular programme of foreign currency sales	14	19 May Statement of the Monetary Policy Committee
5	3 February Statement of the Monetary Policy Committee	15	1 June Current account deficit 27.1 b.kr. in Q1/2021 – net IIP positive by 36.2% of GDP
6	26 February Central Bank to continue regular programme of foreign currency sales	16	30 June Statement of the Financial Stability Committee 30 June 2021
7	2 March Current account surplus 22.1 b.kr. in Q4/2020 – net IIP positive by 1,039 b.kr.	17	30 June Statement of the Financial Supervision Committee 30 June 2021
8	24 March Statement of the Monetary Policy Committee	18	1 July Announcement concerning Central Bank purchases of Treasury bonds
9	29 March Countercyclical capital buffer held unchanged	19	25 August Statement of the Monetary Policy Committee 25 August 2021
10	31 March Central Bank to reduce the extent of its regular programme of foreign currency sales		

- No.
- 20 27 August  
IMF general allocation expands Iceland's international reserves
- 21 2 September  
Current account deficit 31.1 b.kr. in Q2/2021 – net IIP positive by 36.6% of GDP
- 22 29 September  
Statement of the Financial Stability Committee 29 September 2021
- 23 29 September  
Central Bank sets new rules capping debt service-to-income ratios on consumer mortgages
- 24 29 September  
Increase in countercyclical capital buffer
- 25 6 October  
Statement of the Monetary Policy Committee 6 October 2021
- 26 17 November  
Statement of the Monetary Policy Committee 17 November 2021
- 27 1 December  
Current account surplus 13.1 b.kr. in Q3/2021 – net IIP positive by 41.1% of GDP
- 28 8 December  
Statement of the Financial Stability Committee 8 December 2021
- 29 10 December  
Icelandic Bank's Data Centre shifts focus to financial market infrastructure

## Publications by the Central Bank of Iceland 2021

### In Icelandic

*Ársskýrsla [Annual Report] 2020.*

*Fjármálaeftirlit [Financial Supervision] 2021, one issue.*

*Fjármálastöðugleiki [Financial Stability] 2021, two issues.*

*Peningamál [Monetary Bulletin] 2021, four issues*

*Hagvísar [Economic Indicators] 2021, four issues*

*Efnahagsmál [Economic Affairs], no. 10: Fullveldi og peningastefna [Sovereignty and monetary policy], June 2021.*

*Sérrit [Special Publication] no. 15: Eiginfjárkröfur og fjármálastöðugleiki, [Capital requirements and financial stability], June 2021.*

*Sérrit [Special Publication] no. 14: Greiðslujöfnuður þjóðarbúsins, ytri staða og áhættuþættir [Iceland's balance of payments and international investment position], May 2021.*

### In English

*Annual Report 2020*

*Financial Supervision 2021, one issue.*

*Financial Stability 2021, two issues.*

*Monetary Bulletin 2021, four issues.*

*Economic Indicators 2021, four issues.*

*Special Publication, no. 14, Iceland's balance of payments and international investment position, May 2021.*

*Working Paper, no. 87, Wages and prices of foreign goods in the inflationary process in Iceland, by Ásgeir Daníelsson (May 2021).*

*Working Paper, no. 86, The currency that came in from the cold: Capital controls and the information content of order flow, by Francis Breedon, Thórarinn G. Pétursson, and Paolo Vitale (June 2021).*

*Working Paper, no. 85, Exchange rate pass-through, monetary policy, and real exchange rates: Iceland and the 2008 crisis, by Sebastian Edwards and Luis Cabezas (March 2021).*



# Tables



Table 1 Central Bank interest rates<sup>1</sup>

%	<i>Bank's current accounts, nominal rates</i>	<i>Reserve requirements, nominal rates</i>	<i>Overnight lending, discount rates</i>	<i>7 day collateral lending, nominal rates</i>	<i>7 day term deposit</i>
7 February 2018	4.00	4.00	6.00	5.00	4.25
14 March 2018	4.00	4.00	6.00	5.00	4.25
16 May 2018	4.00	4.00	6.00	5.00	4.25
13 June 2018	4.00	4.00	6.00	5.00	4.25
29 August 2018	4.00	4.00	6.00	5.00	4.25
3 October 2018	4.00	4.00	6.00	5.00	4.25
7 November 2018	4.25	4.25	6.25	5.25	4.50
12 December 2018	4.25	4.25	6.25	5.25	4.50
6 February 2019	4.25	4.25	6.25	5.25	4.50
20 March 2019	4.25	4.25	6.25	5.25	4.50
22 May 2019	3.75	3.75	5.75	4.75	4.00
26 June 2019	3.50	3.50	5.50	4.50	3.75
28 August 2019	3.25	3.25	5.25	4.25	3.50
2 October 2019	3.00	3.00	5.00	4.00	3.25
6 November 2019	2.75	2.75	4.75	3.75	3.00
11 December 2019	2.75	2.75	4.75	3.75	3.00
5 February 2020	2.50	2.50	4.50	3.50	2.75
11 March 2020	2.00	2.00	4.00	3.00	2.25
18 March 2020	1.50	1.50	3.50	2.50	1.75
20 May 2020	0.75	0.75	2.75	1.75	1.00
26 August 2020	0.75	0.75	2.75	1.75	1.00
7 October 2020	0.75	0.75	2.75	1.75	1.00
18 November 2020	0.50	0.50	2.50	1.50	0.75
3 February 2021	0.50	0.50	2.50	1.50	0.75
24 March 2021	0.50	0.50	2.50	1.50	0.75
19 May 2021	0.75	0.75	2.75	1.75	1.00
25 August 2021	1.00	1.00	3.00	2.00	1.25
6 October 2021	1.25	1.25	3.25	2.25	1.50
17 November 2021	1.75	1.75	3.75	2.75	2.00

1. Rates on published day.

Source: Central Bank of Iceland.

Table 2 Exchange rate indices

	<i>Narrow trade</i> index <sup>1</sup>	<i>Average exchange rate index<sup>2</sup></i>			<i>Real exchange rate<sup>3</sup></i>			
		<i>Average</i>	<i>Import weights</i>	<i>Export weights</i>	<i>Based on relative prices</i>		<i>Based on unit labour cost</i>	
					<i>Index</i>	<i>%-change</i>	<i>Index</i>	<i>%-change</i>
2000	101.5	96.1	96.3	95.7	87.0	2.8	84.5	2.8
2001	121.4	115.4	115.1	115.3	75.7	-13.0	72.7	-14.0
2002	118.5	112.0	111.7	112.0	80.1	5.9	78.0	7.3
2003	113.4	105.3	104.8	105.4	85.4	6.5	84.7	8.6
2004	112.1	103.1	102.4	103.5	88.2	3.3	86.4	2.0
2005	100.8	92.6	91.9	93.0	100.1	13.5	100.0	15.8
2006	112.7	103.4	102.6	104.0	93.6	-6.6	96.4	-3.6
2007	110.9	100.9	99.9	101.5	98.6	5.4	101.1	4.8
2008	157.3	141.9	140.9	142.4	78.1	-20.8	72.8	-27.9
2009	210.6	191.0	190.0	191.4	63.5	-18.6	50.2	-31.1
2010	204.0	185.0	184.4	185.0	67.8	6.7	56.2	12.0
2011	204.5	183.5	183.0	183.3	68.4	0.9	59.6	6.0
2012	209.1	189.0	188.6	188.8	68.8	0.5	60.4	1.4
2013	206.5	186.3	185.9	186.1	71.4	3.8	62.5	3.5
2014	195.1	177.2	176.2	177.5	76.2	6.7	68.4	9.5
2015	189.5	176.3	175.0	177.1	79.1	3.9	74.3	8.6
2016	169.4	158.9	158.1	159.1	89.3	12.8	86.9	16.9
2017	151.2	141.1	140.6	141.1	99.9	11.9	101.5	16.9
2018	157.2	147.0	146.2	147.2	96.9	-2.9	100.9	-0.6
2019	170.6	160.0	159.1	160.4	90.4	-6.7	91.2	-9.6
2020	189.4	178.2	177.1	178.7	83.2	-7.9	82.2	-9.9
2021	184.9	173.0	171.9	173.6	86.4	3.8	86.4	5.1

1. The index shows the average exchange rate of foreign currencies against the Icelandic króna. 3 January 2000 = 100.

2. The index shows the average exchange rate of foreign currencies against the Icelandic króna. 31 December 1994 = 100.

3. The index shows the real exchange rate of the króna in terms of relative prices and wages in Iceland's main trading partner countries. 2005 = 100.

Source: Central Bank of Iceland.

Table 3 Cash issued by the Central Bank at the year-end

	2017		2018		2019		2020		2021	
	ISK thousands	%	ISK thousands	%	ISK thousands	%	ISK thousands	%	ISK thousands	%
<i>Notes:</i>										
10,000 kr.	33,577,500	52.3	38,892,500	56.6	42,607,500	60.4	49,942,500	64.8	51,287,500	66.1
5,000 kr.	22,788,500	35.5	21,593,500	31.4	19,621,000	27.8	18,826,000	24.4	17,818,500	23.0
2,000 kr.	220,000	0.3	216,000	0.3	214,000	0.3	212,000	0.3	210,000	0.3
1,000 kr.	6,084,500	9.5	6,333,500	9.2	6,344,000	9.0	6,415,000	8.3	6,608,500	8.5
500 kr.	1,559,250	2.4	1,704,500	2.5	1,730,250	2.5	1,669,750	2.2	1,699,250	2.2
Total	64,229,750	100.0	68,740,000	100.0	70,516,750	100.0	77,065,250	100.0	77,623,750	100.0
<i>Coin:</i>										
100 kr.	2,335,500	61.8	2,521,200	62.5	2,660,000	63.1	2,791,400	63.5	2,811,300	63.6
50 kr.	638,090	16.9	679,790	16.9	706,590	16.8	730,190	16.6	736,040	16.6
10 kr.	561,430	14.9	584,190	14.5	600,780	14.2	620,560	14.1	620,400	14.0
5 kr.	125,169	3.3	128,359	3.2	130,304	3.1	132,779	3.0	133,259	3.0
1 kr.	117,455	3.1	119,599	3.0	119,995	2.8	121,932	2.8	121,912	2.8
Total	3,777,644	100.0	4,033,138	100.0	4,217,669	100.0	4,396,861	100.0	4,422,911	100.0
Total in circulation	68,007,394		72,773,138		74,734,419		81,462,111		82,046,661	

Source: Central Bank of Iceland.

Table 4 Liquidity and reserve ratios in %<sup>1</sup>

Effective date:	Total reserve requirement ratio:	Applied reserve requirement, fixed	Applied reserve requirement, averaging	Effective date:	Total reserve requirement ratio:	Applied reserve requirement, fixed	Applied reserve requirement, averaging
1 March 1989	11.0		11.0	21 May 1998	4.0 (1.5)2		4.0
1 May 1990	10.0		10.0	21 March 2003	3.0 (1.0)2		3.0
1 June 1990	7.0		7.0	21 December 2003	2.0 (0.0)3		2.0
31 October 1991	6.0		6.0	21 October 2015	4.0 (0.0)4		4.0
1 January 1992	7.0		7.0	21 December 2015	2.5 (0.0)4		2.5
1 November 1992	6.0		6.0	21 June 2016	2.0 (0.0)4		2.0
1 December 1992	5.0		5.0	21 June 2018	2.0 (0.0)5	1.0	1.0
1 November 1993	4.0 (2.5)2		4.0	21 March 2020	1.0 (0.0)	1.0	0.0

1. Percentage of bank total deposits as of 1 June 1979, of domestic disposable funds as of 1 March 1989, and of all disposable funds as of 21 May 1998.

2. Figure in parentheses refers to the reserve ratio for bond issues and term deposits.

3. Figure in parentheses refers to the reserve ratio for deposits and bond issues with an original maturity of more than two years, and securities eligible as collateral for transactions with the Central Bank.

4. Figure in parentheses refers to the reserve ratio for deposits and bond issues with maturity more than two years, according to rules on reserves ratio no. 870 from 30 September 2015.

5. Change in credit institutions minimum reserve requirements according to rules on reserves ratio no. 585 from 4 June 2018.

Source: Central Bank of Iceland.

Table 5 Main interest rates announced pursuant to Article 10, Paragraph 2, and Temporary Provision III of the Act on Interest and Price Indexation, no. 38/2001

2021	General interest on non-indexed loans	General interest on indexed loans	Penalty rates	Interest on damage claims
1 January	3.30	1.90	8.50	2.20
1 February	3.30	1.90	8.50	2.20
1 March	3.30	1.90	8.50	2.20
1 April	3.30	1.90	8.50	2.20
1 May	3.30	1.90	8.50	2.20
1 June	3.30	1.90	8.75	2.20
1 July	3.45	1.90	8.75	2.30
1 August	3.45	1.90	8.75	2.30
1 September	3.45	1.90	8.75	2.30
1 October	3.65	1.90	9.00	2.43
1 November	3.65	1.90	9.25	2.43
1 December	3.80	1.90	9.75	2.53
Average 2021	3.44	1.90	8.79	2.29
Average 2022	4.08	2.35	9.33	2.72

Source: Central Bank of Iceland.

Table 6 Selected annual nominal yields of deposit money banks and penalty rates in % per annum

	Non-indexed loans <sup>1</sup>		Indexed loans <sup>1</sup>		Penalty rates		Credit terms index, 12-month change <sup>3</sup>
	Nominal <sup>2</sup>	Real	Nominal <sup>2</sup>	Real	Nominal <sup>2</sup>	Real	
2013	8.2	4.4	9.1	5.3	13.0	9.0	3.7
2014	7.8	6.7	6.4	5.3	13.0	11.8	1.0
2015	7.6	5.5	7.3	5.2	12.7	10.5	2.0
2016	8.3	6.0	7.5	5.3	13.4	11.1	2.1
2017	7.3	5.5	7.0	5.2	12.4	10.5	1.7
2018	6.9	3.6	8.6	5.2	12.0	8.5	3.3
2019	7.0	4.2	8.1	5.3	11.7	8.8	2.7
2020	5.8	2.2	8.3	4.6	9.3	5.6	3.5
2021	5.4	0.5	9.0	4.0	8.8	3.8	4.8

1. Weighted average interest rate on new loans.

2. Flat interest.

3. Change in credit terms index (between January values), according to Statistics Iceland.

Source: Central Bank of Iceland.

Table 7 Number of entities regulated by the Financial Supervisory Authority

Categories of regulated entities at each year-end	2016	2017	2018	2019	2020	2021
Subject to licence or operating under special legislation:						
Commercial banks	4	4	4	4	4	4
Savings banks	4	4	4	4	4	4
Credit undertakings	5	5	5	5	4	3
Housing Financing Fund (HFF)	1	1	1	0	0	0
Deposit departments of co-operative societies	1	1	0	0	0	0
Investment firms	10	9	9	9	9	9
UCITS management companies	10	10	9	9	9	6
Alternative investment fund managers <sup>1</sup>	0	0	0	0	16	19
Securities exchanges	1	1	1	1	1	1
Central securities depositories	1	2	2	2	1	1
Pension funds <sup>2</sup>	25	22	21	21	21	21
Insurance companies	12	11	11	11	11	10
Insurance brokerages	9	9	7	8	9	9
Entities with debt collection licences	8	7	8	8	9	8
Payment institutions	1	1	1	1	2	1
Electronic money institutions	0	0	0	1	1	2
Currency exchange services	1	1	1	1	1	1
Guarantee funds	2	2	1	1	1	1
Registered lenders	0	1	1	1	0	0
Virtual currency service providers	0	0	1	1	3	3
<b>Total</b>	<b>95</b>	<b>91</b>	<b>87</b>	<b>88</b>	<b>106</b>	<b>103</b>
Other regulated entities:						
UCITS funds	47	42	40	37	37	36
Alternative investment funds for retail investors <sup>3</sup>	60	60	60	54	61	69
Other alternative investment funds <sup>4</sup>	106	111	117	114	116	121
Pension savings custodians <sup>5</sup>	8	8	8	8	8	8
Issuers of listed shares	21	20	23	24	23	26
Issuers of listed bonds	57	65	50	57	51	51
Holding companies <sup>6</sup>	9	6	6	5	6	5
Financial conglomerates <sup>7</sup>	0	0	0	0	1	1
Financial undertakings in winding-up proceedings	2	1	0	0	0	0
<b>Total</b>	<b>405</b>	<b>404</b>	<b>391</b>	<b>387</b>	<b>409</b>	<b>420</b>

1. Including 9 licenced management companies, 6 of which are also UCITS management companies; and 10 registered entities, one of which is an investment firm.

2. Many pension funds are divided into divisions. There were 69 divisions at year-end 2021.

3. Previously investment funds.

4. Previously institutional investment funds.

5. Commercial banks and savings banks. Pension funds and foreign custodians are not included.

6. Holding companies in the financial or insurance sector, or mixed holding companies.

7. Financial conglomerates in the financial or insurance sector.

Source: Central Bank of Iceland.

Table 8 Activities by foreign parties in Iceland

<i>Number at year-end</i>	2020	2021
Credit institutions and other financial institutions without establishments	297	303
Credit institutions and financial institutions without establishments	303	236
UCITS (no. of subsidiary funds)	113 (1,291)	124 (1,347)
Investment firms with establishments/branches	1	1
Investment firms without establishments/branches	2,630	581
Central securities depositories with establishments/branches	1	1
Central securities depositories without establishments/branches	0	5
Insurance companies with establishments/branches	2	2
Insurance companies without establishments/branches	440	351
Insurance brokers with establishments/branches	2	2
Insurance brokers and insurance agents	6,821	2,837
Payment institutions with agents (no. of agents)	3 (6)	3 (5)
Electronic money institutions with distributors (no. of distributors)	1 (1)	0
Payment institutions and electronic money institutions without establishments	516	332
Credit intermediaries without establishments	18	4
Alternative investment fund managers without establishments	205	152
<i>Number of companies registered outside Europe and authorised to provide services in Iceland according to national law</i>		
Alternative investment fund managers (no. of funds)	46 (87)	30 (65)

Source: Central Bank of Iceland.

Table 9 Balance sheet of the Central Bank of Iceland

M.kr.	2016	2017	2018	2019	2020	2021
<b>Assets:</b>	900,649	764,530	755,189	840,240	843,515	964,183
Foreign assets	816,596	687,452	736,589	822,244	817,058	923,224
Gold	8,310	8,732	9,576	11,720	15,404	15,212
SDR	16,963	16,674	18,249	19,021	20,861	77,007
Currency balance with the IMF	10,596	10,389	11,314	11,723	12,835	12,740
Foreign deposits	111,841	96,728	119,095	210,158	109,887	169,479
Foreign securities	667,109	553,236	577,285	568,924	657,806	648,601
Other reserve assets	938	837	606	385	0	0
Other foreign assets	839	856	464	313	266	185
Domestic assets	84,053	77,077	18,600	17,996	26,457	40,960
Deposit money banks	162	78	0	38	1,749	2,107
Collateral loans	0	0	0	0	1,749	1,812
Other claims in foreign currency	162	78	0	38	0	1
Other claims	0	0	0	0	0	294
Other financial institutions	2,267	6,168	5,996	5,935	5,809	5,679
Listed securities	2,267	6,168	5,996	5,935	5,809	5,679
Central government	40,815	55,516	0	0	7,770	21,835
Listed securities	12,060	55,516	0	0	7,770	21,835
Bonds receivable	28,755	0	0	0	0	0
Other sectors	36,183	9,195	5,478	3,600	2,335	2,115
Sundry accounts	295	334	470	444	807	683
Equity holdings	35,889	8,861	5,007	1,773	1,528	1,425
Securities	0	0	0	1,382	0	0
Unlisted bonds	0	0	0	0	0	8
Properties	4,102	5,441	6,260	7,388	7,407	7,845
Other assets	524	681	866	1,035	1,387	1,378
<b>Liabilities and Capital:</b>	900,649	764,530	755,189	840,240	843,515	964,183
Foreign liabilities	43,885	40,334	45,581	34,310	39,818	94,917
Short term	2,893	590	3,038	7,951	12,422	18,148
Long term	23,961	23,046	24,357	7,516	6,767	0
IMF SDR allocation	17,030	16,698	18,186	18,843	20,629	76,769
Domestic liabilities	812,697	701,994	651,274	723,948	652,839	735,160
Notes and coin	62,328	68,007	72,773	74,734	81,462	82,047
Deposit money banks	377,922	371,184	285,633	352,465	210,572	274,526
Sight deposits	44,762	79,678	72,454	57,154	66,012	78,667
Time deposits	283,537	277,441	200,789	262,619	137,436	195,859
Certificates of deposit	48,451	13,526	11,818	32,692	7,124	0
Other claims	2	0	0	0	0	0
Sight deposits in foreign currency	1,170	538	573	0	0	0
Other financial institutions	77,824	93,005	95,467	61,519	27	1,022
Sight deposits	70,815	80,984	77,131	57,807	22	1,022
Time deposits	7,010	12,021	18,307	3,706	0	0
Certificates of deposit	0	0	30	5	5	0
Central government	255,995	160,473	194,975	233,428	356,302	372,265
Treasury current accounts	66,379	76,281	104,833	70,153	134,615	56,375
Government institutions, current accounts	2,085	1,107	1,077	80	213	93
Treasury sight deposits in foreign currency	184,917	81,148	86,583	151,458	214,124	304,564
Governm. institutions foreign exch. deposits	454	498	532	44	29	0
Other claims	2,160	1,438	1,950	11,693	7,321	11,233
Other liabilities	38,628	9,324	2,425	1,802	4,476	5,301
Capital and reserves	44,067	22,202	58,335	81,982	150,857	134,105

Source: Central Bank of Iceland





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