



Capacent Glacier

FOREIGN INVESTMENT IN ICELAND

PAST LESSONS - PRESENT SITUATION FUTURE OPPORTUNITIES



At a glance...

Population: 320,000

Size: 103,000 square kilometers

Currency: Króna (ISK)

Iceland is a Mid-Atlantic island 103,000 square kilometers in size or roughly equal to Kentucky. It's larger in geographical area than many European countries including Ireland, Switzerland, Belgium, Denmark, Hungary and Portugal. It has the lowest population density in Europe with close to three inhabitants per square kilometer.

Economy

Iceland's economy has long been export driven with fishing historically being the main export product. Iceland is Europe's second largest fishing nation after Norway and the world's 14th largest based on the 2004 catch.

In 2008, with Alcoa's Fjarðarál smelter kicking in, aluminum overtook fish for the first time in export income. 35.8% of Iceland's export in 2008 were marine products and 40.9% derived from the power intensive industry.

Politics

Iceland is a liberal, parliamentary democracy with a free-market economy containing a strong social element.

The last elections were held in April 2009 and resulted in Iceland's first left wing government for decades. Iceland's next elections are scheduled in 2013.

Iceland has close political ties to the Nordic countries and is a founding member of NATO and the European Economic Area, allowing the free movement of goods, labor, capital and service within the 27 member states of the European Union as well as Norway and Liechtenstein.

Taxation

The Icelandic tax system is classical and relatively simple and effective. The corporate tax rate of 15% is one of the lowest in the OECD. There are double taxation treaties available for most major countries.

Investment Restrictions

The main restrictions on investment in Iceland are related to fishing and energy. Foreign legal entities are only allowed to invest in the fishing industry but Icelandic legal entities with up to 25% (33% in some circumstances) foreign ownership can invest in the Icelandic fishing industry. Investment in companies with energy exploitation rights is limited to legal entities from the EEA area. Entities from outside the EEA are only allowed a maximum stake of 49% in Icelandic airlines.

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FUTURE OPPORTUNITIES**



Icelanders Welcome Foreign Investors

Iceland's image has been based on its spectacular nature, richness of natural resources and an educated and prosperous population.

Following the collapse of its financial system in October 2008, Iceland has had to come to terms with a new situation.

The rebuilding of the financial system has and will be a major task. The next step on the road to recovery is to reconnect Iceland and the global economy and foreign direct investment, will play a crucial role in this process.

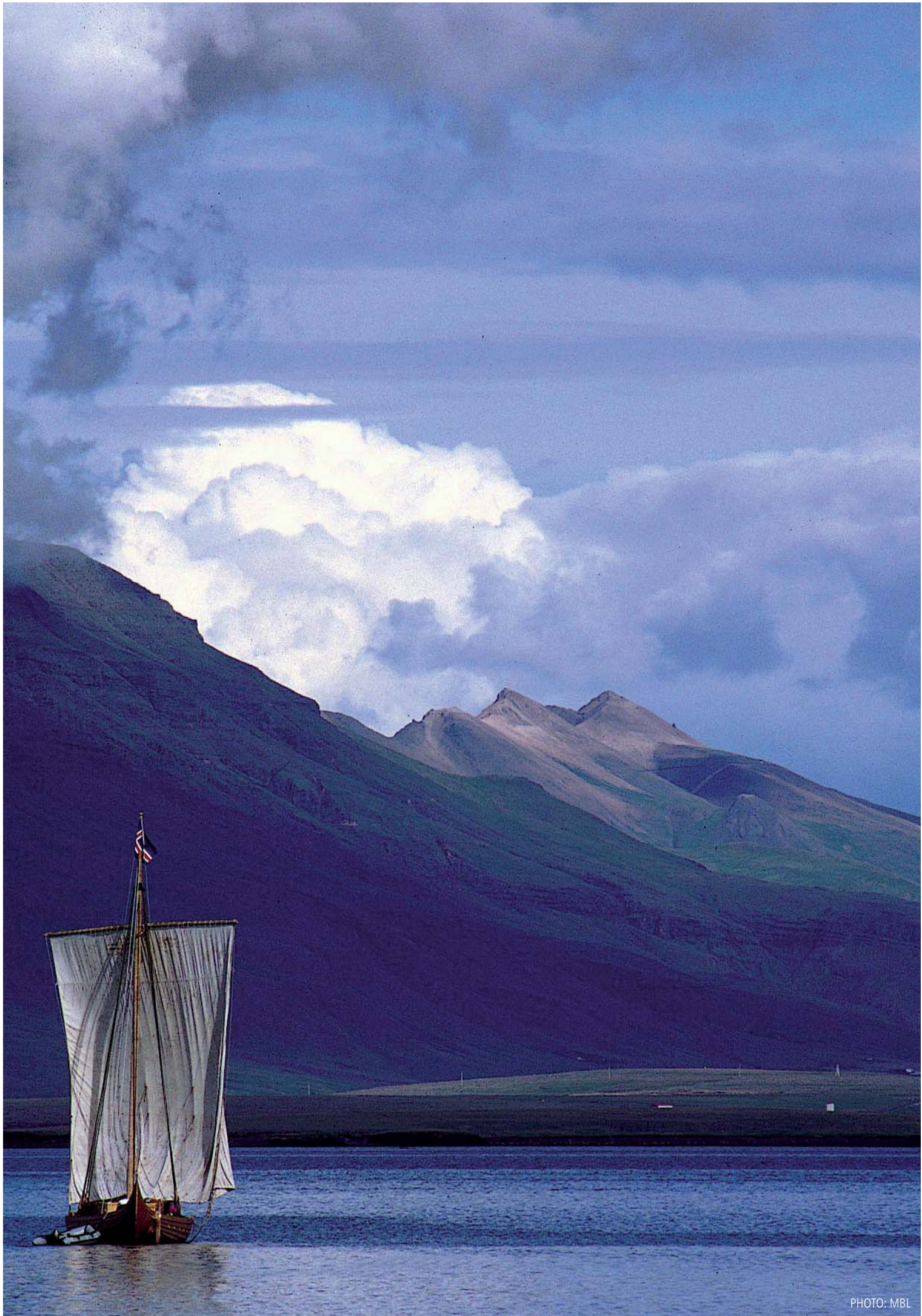
Presently there is general agreement in Iceland about the necessity of foreign investment with 92% of Icelandic executives and 81% of the general public believing it

to be important to economic recovery according to a Capacent Gallup poll.

Only 0,4% of respondents among executives and 2,6% among the general public are of the opinion that foreign investment does not matter at all in this regard.

According to the same poll 86% of executives declare themselves to be in favor of foreign investment. 8% are indifferent and 6% are opposed and 70% of the general public.

Foreign investment played a crucial role in Iceland's development in the 20th century with the harnessing of its energy resources being a key factor in the emergence of a highly developed, educated and technologically savvy society.



A highly developed nation...

The history of Iceland goes back to the island's settlement in the 9th century by Norsemen and Celts. After several centuries of independence, Iceland became a part of the Norwegian kingdom in 1261 and later fell under the influence of the Danish crown. It was not until 1944 that Iceland became fully independent and able to take its destiny in its own hands. Iceland became a part of the European Economic Area at its establishment in 1994 and applied for full membership of the European Union in 2009.

The post-war period marked the start of Iceland's economic rise with the country utilizing its vast resources to create a liberal free market economy combined with a Nordic style welfare system and a top ranking in the UNDP Human Development Index.

Iceland has, for decades spent a high share of GDP on education and health, ahead of most other OECD countries. The country prides itself on its well educated and young population, with a median age of only 35, as well as one of the highest life expectancies in the world, just over 80 years. Only 13% of the population is over 65 years old.

In addition there is no pension time bomb threatening the economy as is the case in many western countries. This is not only due to a young working population. Iceland's pension funds are fully funded in spite of taking a hit with the rest of the financial system. Iceland does not have a pay-as-you-go system of pension financing but a system based on accumulating funds which stood at close to € 9 billion at the beginning of 2009 with a high proportion of the funds invested in foreign assets.

In spite of the 2008 financial meltdown Iceland still ranks among the top 30 nations in the world in the 2009 World Competitiveness Report of the World Economic Forum.

... and richness in natural and human resources

What has made this possible are the island's natural resources not least the marine stocks and energy. Iceland is a leading fishing nation on a global scale, annually fishing close to 2% of the global catch despite its small population. Along with Norway, it is a leading European fishing nation with Iceland fishing close to a fifth of the European total catch.

In addition to fish, Iceland has an abundance of green energy, both hydroelectrical and geothermal. The total economically (and socially responsible) viable electric power potential is estimated at 45-55,000 GWh/year with only approximately 30-40% of that currently being harnessed.

Iceland is currently in the top 5 league internationally when it comes to the utilization of geothermal energy.

Recently leading companies have emerged from the country's research and technology environment in cooperation with investors adding an important pillar to the economic foundation.

Resources have made this economic success story a possibility. What made it a reality was foreign investment and an emphasis on infrastructure, education and research.

SUPPORT FOR FDI BY SECTOR

General public

In general	70%
Financial sector	73%
Telecommunications	69%
Industry	73%

TOP EXPORTERS OF SEAFOOD

(2005 - US\$ millions)

China	7674	Netherlands	2838
Norway	4922	Vietnam	2747
Thailand	4474	Spain	2603
USA	4287	Russian Fed.	1960
Denmark	3695	UK	1890
Canada	3615	Indonesia	1851
Chile	3043	Iceland	1794

... But How Welcoming Is Iceland?

Four out of five welcome foreign investors....

Iceland's strengths are found in its societal foundation. A liberal and prosperous western country with a strong social network and a highly educated and skilled population. A country full of vast natural resources but still relatively untouched by industrialization.

It should come as no surprise that Icelanders in general have a very favorable outlook towards foreign investment. A poll conducted by Capacent Gallup in September 2009 showed an overwhelming majority of both Icelandic executives and the general population being favorably inclined towards foreign investors. Of those polled 81% responded that foreign investment was important for Iceland's economy and 70% were generally in favor of foreign investment.

Even more support is to be found among Icelandic executives with 92% deeming foreign investment important and 86% being favorable towards foreign investment. Only 9% of the general public and 3.4% of executives were of the opinion that foreign investment was of little or no importance.

...in large sectors of the economy...

There is widespread support for foreign investment, most notably in the financial sector and in the telecommunications sector.

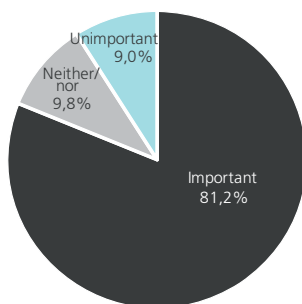
88% of executives and 73% of the general public support foreign investment in the financial sector. Only 3% of executives and 9% of the general public are opposed with the remaining being indifferent.

When asked about foreign investment in the Icelandic industrial sector 85% of executives and 73% of the general public are in favor. 4% of executives are opposed and 9% of the general public.

In the telecommunications sector 82% of executives and 69% of the general public support foreign investment but 5% of executives and 10% of the general public are opposed.

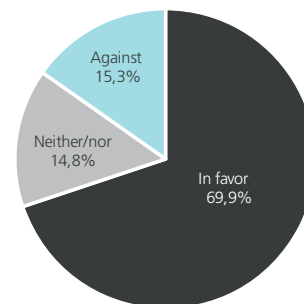
HOW IMPORTANT IS FOREIGN INVESTMENT FOR THE ECONOMY?

General Public



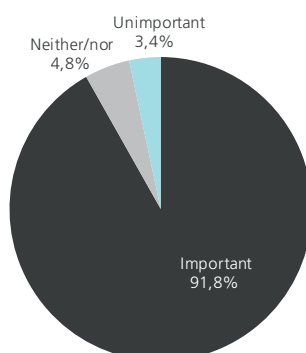
ARE YOU IN FAVOR OF FOREIGN INVESTMENT IN ICELAND?

General Public



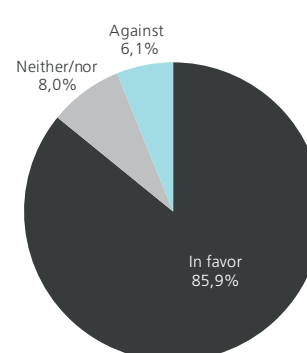
HOW IMPORTANT IS FOREIGN INVESTMENT FOR THE ECONOMY?

Executives



ARE YOU IN FAVOR OF FOREIGN INVESTMENT IN ICELAND?

Executive



... but there is always a caveat!

In spite of Icelanders being generally in favor of foreign investment they are more hesitant when it comes to investments in Iceland's natural resources, notably fishing and energy.

When asked an open question whether or not they supported foreign investment in the fishing industry 55.6% of the general public were opposed, 23.6% in favor and 20.8% undecided. Among executives 45.4% were against, 37.7% in favor and 16.9% undecided.

Asked an open question about foreign investment in the energy sector 50.2% of the general public were originally against, 29.3% in favor and 20.5% undecided. Among executives 45.6% were against, 40% in favor and 14.4% undecided.

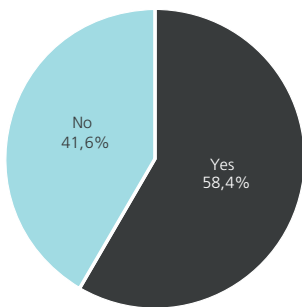
Those opposed were asked further whether it would change their opinion if it was ensured that the resource remained Icelandic and a fair fee paid for its utilization.

With these conditions ensured 64% of executives were in favor of foreign investment in the fishing sector and 36% were opposed. The result was similar among the general public with 58% in favor of foreign investment in fishing companies under such conditions and 42% being opposed.

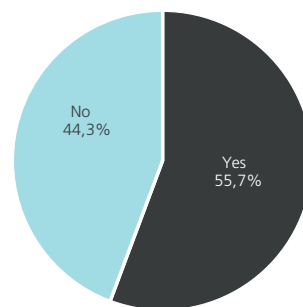
A similar pattern emerges regarding foreign investment in the energy sector. If it was ensured that the resource itself would remain in Icelandic hands with a fair fee paid for its utilization 66% of executives and 56% of the general public were in favor of foreign investment in the energy sector. 34% of executives and 44% of the general public were opposed.

Icelandic legislation already reflects this regarding the energy sector with a legal distinction being made concerning foreign investment in energy resources, which is restricted, and foreign investment in the utilization of energy resources, which is permitted. Legislation concerning the fishing industry is more prohibitive with severe restrictions on foreign investment.

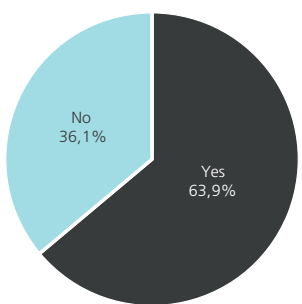
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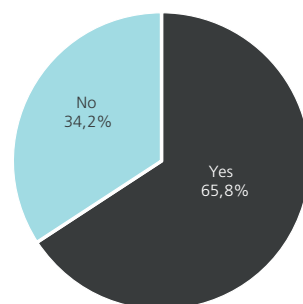
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Executives





The Icelandic Investment Environment

A small domestic market...

The Icelandic investment environment poses great opportunities as well as challenges for foreign investors. As we have seen, foreign investors are welcomed by both the Icelandic business community and the general public. So what have been the major factors working against foreign investment?

The size of the economy and the domestic market has clearly been an inhibiting factor with a population of only 320,000.

With the exception of the largest sectors like finance, insurance, retail, international transportation, real estate and telecommunications there have been limited large scale investment possibilities.

For decades most major investments had the main purpose of gaining access to energy and other natural resources. More recently there have been major investments in technology or processes developed in Iceland that have been able to develop economies of scale globally.

It must also be kept in mind that the largest sector of the Icelandic economy - the fishing industry - has been off limits to foreign investors. But other country-specific factors have also played a role.

... and a strong króna kept investors out...

In the years leading up to the 2008 crash, Icelandic companies were outward looking mostly in one sense; the focus was on foreign acquisitions made possible by cheap and readily accessible capital.

Speculative money was drawn to Iceland through the "carry trade" with billions of dollars being invested in Icelandic króna bonds, fueling the strength of the Icelandic króna..

Long term private equity investment in the Icelandic economy on the other hand was scarce, and almost non-existent, if you exclude positions taken by off-shore holding companies under Icelandic control.

Foreign investment was primarily based on debt and equity in Iceland's financial institutions and bonds issued in that industry as well as the large scale metal industry of the country.

This should come as no surprise, since the incentives to invest in other sectors of the economy were hardly there. The same currency strength that made foreign investment cheap to Icelandic investors served as a deterrent to foreign investors interested in taking a stake in Icelandic companies. The strong króna and a bullish domestic stock market served as barriers to entry.

...but will a weak króna lure foreign investors in?

Now the tables have turned. The króna is at an all time low offering great possibilities to those entering the market at current FX levels. Many Icelandic firms are showing sound operational results but are struggling with refinancing and/or a crushing debt burden.

The profit and loss statement of Icelandic companies are often in the black while the balance sheets are a mess, due to foreign currency-linked debt and excess leverage. Many companies are crumbling under the debt burden of investments made in the bullish and risk-welcoming years leading up to the crash.

Here we see numerous step-in opportunities for foreign investors.

New possibilities are emerging...

Aluminum and other energy intensive industries have been the sectors attracting the largest share of foreign direct investment in Iceland over the last few decades. Due to environmental concerns and increasing worries about the need to diversify the economy away from a sole dependence on fish and metals there are limits to how much more large scale investment Iceland is prepared to absorb in energy intensive industry.

On the other hand the uniqueness of the economic situation in Iceland following the 2008 crash has opened up totally new fields of investment possibilities in sectors previously dominated by domestic players.

...with traditional...

Take the large service and telecommunication industries as an example. Most of Iceland's largest firms have been severely affected by the fall of the banks and the devaluation of the króna. In many cases, the problems are not related to the operations of the firms but instead a heavy debt burden.

... and greenfield opportunities aplenty!

The abundance of green energy that Iceland offers investors could lead to the emergence of entirely new possibilities.

Iceland is seen by many as a prime location for data centers. In a report written by PriceWaterhouseCoopers Belgium in 2007 for the Invest in Iceland Agency, Iceland was benchmarked against the United States, the United Kingdom and India as a data center location and was found to be "best in class". Iceland is helped by cheap and "green" energy, good connectivity and a naturally cool climate.

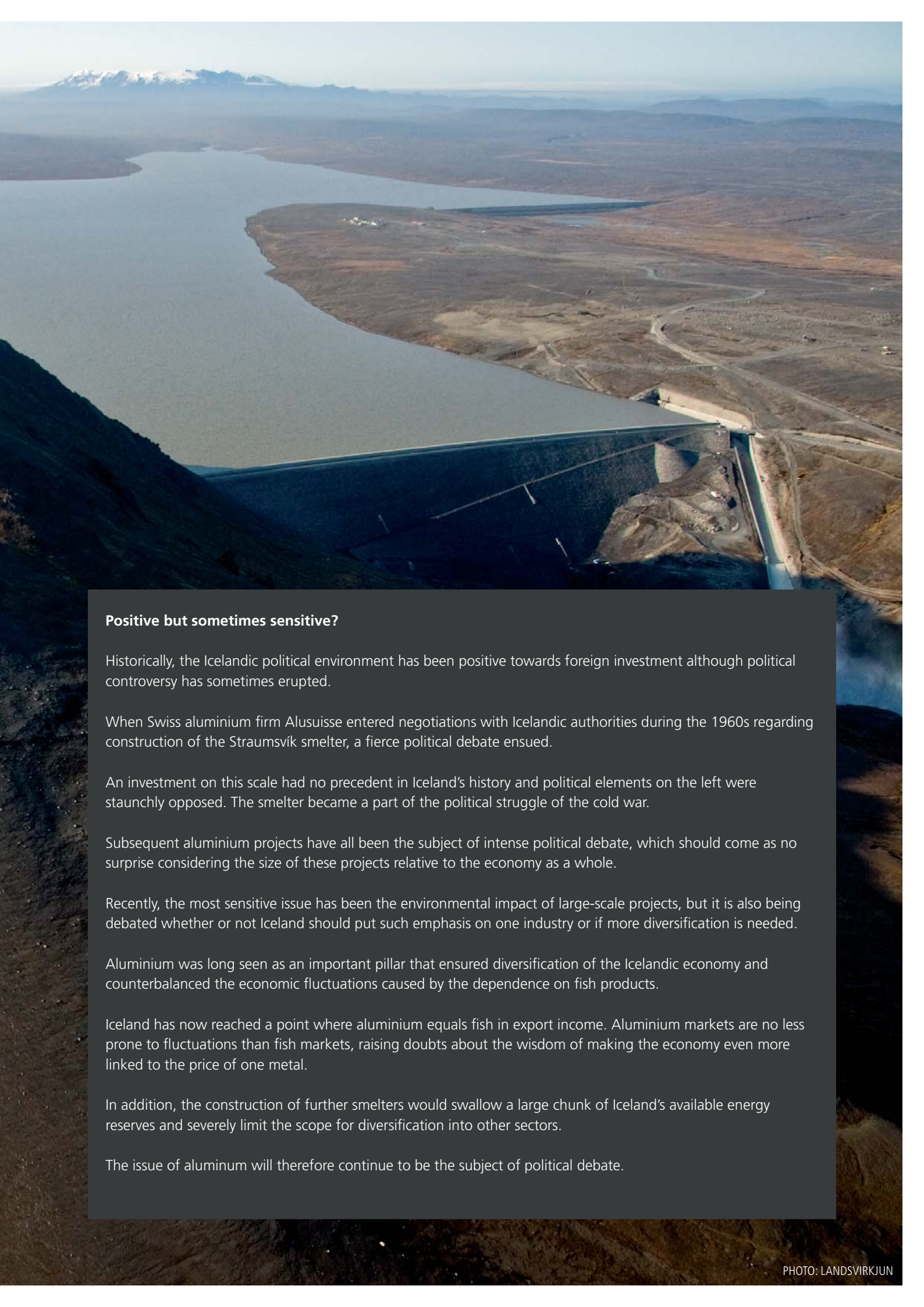
Several data center projects have been in the pipeline for a while with the planned center of Verne Global in Reykjanesbær, a joint venture between General Catalyst Partners and Novator, already being well advanced.

But opportunities are not limited to the use of energy.

Iceland's highly developed health care system has also been the catalyst for several interesting projects. In the Reykjavík suburb of Mosfellsbær, the construction of a private hospital and hotel is scheduled to start in the spring of 2010. The hospital will specialize in hip- and knee-operations. It intends to serve the US market, starting operations by the end of 2011. The project is run by PrimaCare in cooperation with Shiboomi of the US, Skanska of Sweden and financed by the Oppenheimer Investment Group.

Another health related project is planned in Reykjanesbær at the hospital at the former US Naval Base in Keflavík.





Positive but sometimes sensitive?

Historically, the Icelandic political environment has been positive towards foreign investment although political controversy has sometimes erupted.

When Swiss aluminium firm Alusuisse entered negotiations with Icelandic authorities during the 1960s regarding construction of the Straumsvík smelter, a fierce political debate ensued.

An investment on this scale had no precedent in Iceland's history and political elements on the left were staunchly opposed. The smelter became a part of the political struggle of the cold war.

Subsequent aluminium projects have all been the subject of intense political debate, which should come as no surprise considering the size of these projects relative to the economy as a whole.

Recently, the most sensitive issue has been the environmental impact of large-scale projects, but it is also being debated whether or not Iceland should put such emphasis on one industry or if more diversification is needed.

Aluminium was long seen as an important pillar that ensured diversification of the Icelandic economy and counterbalanced the economic fluctuations caused by the dependence on fish products.

Iceland has now reached a point where aluminium equals fish in export income. Aluminium markets are no less prone to fluctuations than fish markets, raising doubts about the wisdom of making the economy even more linked to the price of one metal.

In addition, the construction of further smelters would swallow a large chunk of Iceland's available energy reserves and severely limit the scope for diversification into other sectors.

The issue of aluminium will therefore continue to be the subject of political debate.



TOTAL CATCH 2005
Tonnes Live Weight

EU-27	5.632.045
ES	768.267
UK	669.493
IS	1.661.139
NO	2.392.528
<hr/>	
EEA	9.685.711
WORLD	93.813.943

Fish and energy. Off limits for eternity?

It is clear that foreign investment in certain sectors is more sensitive than in others. Icelanders are very much in favor of foreign investment in the service sector, be it telecommunication services or financial services. However, when it comes to the utilization of Iceland's resources, the public is much more wary. This wariness is in part due to the island's past.

Historically, Iceland has had to fight hard for the right to manage the island's natural wealth. The strive towards independence was not only about political independence, but about gaining economic autonomy from the outside world and gaining control over Iceland's resources.

The last battle to be fought on this road was the cod wars with Britain in the 1970s which ensured Iceland the sole right to manage its fishing stock within 200 nautical miles.

These hard fought rights have been guarded fiercely in all international negotiations. Indeed the autonomy over fishing stocks is probably the sole issue that has kept – and might keep – Iceland outside of the European Union.

Foreign investment in Iceland's fishing sector has been largely off limits, although limited indirect ownership in the fish processing industry is allowed.

There is regular discussion in Iceland about the risks and opportunities in loosening the stringent rules on foreign investment in the fishing industry. These discussions started to gain momentum during the mid-1990s when Icelandic companies started to invest heavily in European fishing companies.

The question of foreign investment in the fishing industry is bound to emerge in the upcoming negotiations for EU-membership and will most likely be one of the most contentious issues in the negotiation process.

Similar sentiments apply for the country's other natural resources, in particular, the energy sector.

Unlike marine resources, a legal solution has recently been created where there is a clear distinction between ownership of the natural resources and its temporary utilization by energy companies. This paved the way for Magma Energy Corporation to acquire a stake in HS Orka, the power generation arm of the former Hitaveita Suðurnesja.

Magma's investment is the first foreign investment in Iceland's energy utilities and created a political controversy during the summer of 2009 with ministers of the Left Green Party trying to find an alternative solution. After intense governmental scrutiny the deal went through

With the exception of HS Orka, most of Iceland's energy utilities are publicly owned and there are currently no plans for privatization. Ideas about Iceland's pension funds taking a stake in hydroelectric giant Landsvirkjun were recently floated. These ideas received a lukewarm reception from the government with ministers insisting that a majority stake and control over the company must remain in government hands .

Iceland's supply of natural energy is abundant but the sacrifices in term of nature preservation that are an inevitable part of their utilization have also made energy a political hot potato. Several large projects have been halted or dramatically altered due to the political sensitivity of the issue.

The 700 MW Kárahnjúkar project built in 2003-2007 to supply Alcoa's Fjardaral-smelter was an enormous project in scale, not just by Icelandic standards. The project met political resistance and the controversy still lingers in Icelandic society.

In spite of this, polls indicate a strong general support for investments in large-scale industrial projects. A 2005 Capacent Gallup poll for the Confederation of Icelandic Employees showed close to 80% of the population having a positive or neutral position towards the aluminum industry and almost 2/3 being neutral or positive towards further expansion of the sector.



The Economic Environment In Iceland

A boom...

After a few years of sluggish growth around the turn of the century, Iceland's economy boomed and soon became the most overheated economy in the OECD.

The upswing was kick-started with the construction of the Alcoa smelter in eastern Iceland and the corresponding construction of the Kárahnjúkar hydroelectric project. This pumped billions of dollars into the Icelandic economy fueling both economic growth and inflation and prompting the Central Bank to hike its base rate to counteract inflationary pressure. The base rate soon hit the double digit mark.

Simultaneously, Iceland's business environment was undergoing radical changes. With the privatisation of the country's major banks, Iceland entered a new era. The banks started to focus on international expansion and a strategy based on risk-taking.

At the same time, global financial markets were more bullish than ever and the Icelandic banks had no problems finding investors in wholesale markets willing to finance their expansion with cheap capital.

The banks' balance sheets seemed to grow exponentially (reaching 880% of GDP in 2007) along with most other economic indicators, fueled by foreign capital flowing into the banks as well as through the carry trade – with the base rate making króna bonds an attractive option.

Soon worries started to emerge internationally about the Icelandic economy which was getting stretched to the limit with a growing current account deficit and external debt reaching 142% of GDP in 2007.

...and bust of epic proportions

The first serious warning sign came on February 21st 2006 when the Fitch rating agency downgraded the outlook on Iceland's sovereign debt to negative causing a widespread sell-off of krónas and other Icelandic assets.

Iceland's banks made a concerted effort to reduce risk and calm investors' fear.

When the global financial system tumbled into the worst financial crisis since the Great Depression, it slowly became clear that Iceland's banks were in serious trouble and their risk-taking strategies and quick expansion would come back to haunt them. Financial wholesale markets started to close and Iceland's bankers had increasing difficulties in rolling over the banks' debt.

After the fall of Lehman Brothers, all doors closed and it became painfully clear that a banking system almost ten times the size of the economy was not too large to fail but too big to save.

The behavior of the banks in the years leading up to their fall has lately come under scrutiny. Several factors made them vulnerable to an inevitable crunch in the credit markets. Government control was lax and Icelandic authorities have been criticized for failing in the supervision of the country's overgrown financial system. The banks themselves indulged in reckless behavior including heavy lending to major shareholders and extensive cross-ownership in the Icelandic market which eroded their capital base and paved the way for a domino effect.

In less than a week in early October 2008 Kaupthing, Glitnir and Landsbanki, representing 85% of Iceland's financial system, collapsed.

Iceland is still dealing with the fallout of the crisis. A special prosecutor has been appointed to investigate indications of illegal activity by Iceland's financial institutions and a "truth commission" appointed by parliament is working on an extensive report on the circumstances that led to the financial collapse. It's report is due in early 2010.

The IMF came to the rescue...

On October 24th 2008, the government of Iceland and the International Monetary fund agreed on an economic programme for Iceland. Under the programme, Iceland would receive a credit of approximately US\$ 5 billion from the fund and several individual countries.

The programme was welcomed by all parties and came at a crucial time during Iceland's financial crisis. Iceland's financial credit was drying up and the country had limited access to international financial transactions.

...but is increasingly under attack...

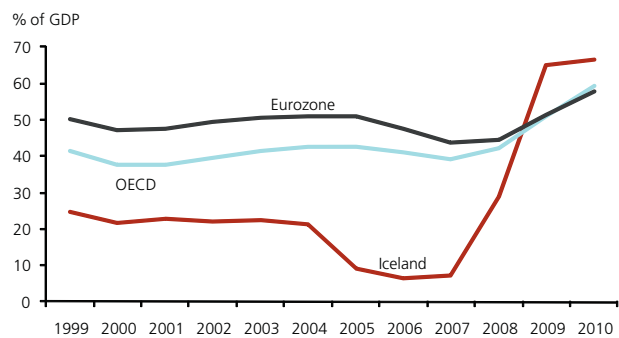
Since then, the IMF has come under increasing domestic criticism for linking the continuation of the programme with the resolution of Iceland's Icesave dispute with the United Kingdom and the Netherlands, concerning reimbursement of depositors at Landsbanki in these countries.

In spite of this, most experts agree that the IMF programme represents a key milestone on the way to regain economic stability, paving the way for recovery. The IMF funding boosts Iceland's currency reserves and gives authorities a foundation to begin scaling back the currency restrictions. The first steps in this regard were announced on October 31st 2009.

ECONOMIC GROWTH IN ICELAND



PUBLIC DEBT



...while positive signs start to appear

With the fall of its financial system, Iceland entered the first recession since 1992. Iceland's Ministry of Finance predicts that the economy will shrink by 8.4% in 2009 and 1.9% in 2010. The economy actually grew in 2008 by some 1.3%. Unemployment grew to 8.6% and is predicted to peak at 10.6% in 2010 before falling back to around 9% in 2011.

The value of the króna fell to its lowest historical level against most currencies and has not recovered since. This has had serious implications for most Icelandic companies and many households with debt linked to foreign currencies. Such loans were immensely popular during the past 5 years, offering interest rates far below the rates on loans in Icelandic krónas.

The Central Bank of Iceland estimates that 20% of households have foreign currency linked mortgages and car payments and that up to 70% of corporate debt is linked to foreign currencies. Approximately a fifth of households had negative equity in the beginning of 2009.

But the fall of the króna has also had positive implications. After years of a soaring foreign trade debt, the króna level has led to drastically reduced imports and boosted Iceland's export industries.

Domestic products have gained a competitive advantage to such a degree that the local McDonald's franchise was forced to cease operations. While hamburger chains utilizing local suppliers of meat, bread and ice-cream were faced with a 25% price increase, the McDonald's franchise, which had to import all its raw material, saw its supply bill double.

After its toughest year in recent history, there are several indications that Iceland is slowly on the road to recovery. The Icesave dispute is being resolved and current estimates suggest that Landsbanki assets will cover up to 90% of the Icesave debt.

Several large scale projects, including the Helguvík smelter of Norðurál and the Verne Global data center, are hopefully about to clear the final hurdle.

Iceland's Consumer Confidence Index, which Capacent Gallup measures monthly, rose to 47.9 points in October. This is the third consecutive monthly increase and the highest value during 2009. Consumers are still wary about the immediate situation, but most predict that the economy will be in a better state in six months.

How stable is the stability pact?

Iceland's labor market has been marked by calm since the country's social partners reached an historical understanding in 1990 to combat inflation and increase living standards.


Major labor market disputes have since primarily been in the public sector.

With the last year being marked by growing unemployment, falling wages and rising inflation, a stable labor market is seen as a major factor to ensure recovery.

In June 2009, the government of Iceland and the social partners, the Confederation of Icelandic Labor Unions (ASÍ), and the Confederation of Icelandic Employers (SA) signed a stability pact with the aim to ensure economic stability in Iceland for the coming year.

The pact, which is valid until the end of 2010, included several commitments on behalf of both the government and the social partners.





Political environment and other stakeholders

A government falls...

Political stability has traditionally been a hallmark of Iceland. The country has usually been ruled by a coalition of 2-3 parties and a change of government has not meant a drastic change of policy.

From 1991 to 2009 the conservative Independence Party was in power with either the Progressive Party or the Social Democratic Party as a government coalition partner. The party was in charge of implementing wide ranging economic liberalization and privatization of the economy, including the privatization of formerly government owned banks. During a period of unprecedented prosperity, the Independence Party reaped its electoral rewards.

When the financial system imploded the electorate held it accountable.

....after civil unrest...

The months following the crash were marked by political turmoil on an unprecedented scale. The angry public seeing its savings vanish, mortgages soaring and its future threatened took to the street.

Unlike many European countries, Iceland has no tradition of civil unrest. The scale of the protests therefore came as a surprise to many, initially people gathered for peaceful protests, but in January these protests evolved to large-scale demonstrations.

The government imploded and a minority government of the Social Democrats and the Left Green Alliance took the reign with the support of the Progressive Party.

Elections were held in late April with the two left-wing government parties gaining a majority of seats in the 63 member Icelandic parliament, the Althingi.

...and the new coalition tackles Europe and Icesave...

Two controversial issues have dominated the government's agenda since the April elections; applying for EU membership and resolving the Icesave dispute.

The EU issue is highly sensitive within the government with the Social Democrats being the main political advocate for membership and the Left Green Party being the main advocate against membership. A compromise was reached when the parties negotiated the government's agenda with both parties agreeing on applying for membership but the Left Green Party reserving its right to fight against the eventual outcome of EU negotiations.

Parliament debated the issue throughout early summer with the opposition demanding a binding referendum at the end of negotiations. Eventually parliament approved Iceland's application for EU membership and the application was handed over in July.

The Icesave issue has proved harder to resolve. After an intense political debate during which one government minister left the cabinet in protest, parliament put strict restrictions on the sovereign guarantee of the Icesave loans. The final bill placed certain restrictions on the government guaranty. This was not accepted by the British and Dutch governments and the government has been forced to present a new bill in parliament.

The Icesave controversy has been politically difficult for the government and the issue has probably fueled anti-European sentiment within the electorate. Under the prospective agreement the Icelandic government commits itself to reimburse British and Dutch citizens who deposited funds in the "Icesave"-accounts of the defunct Landsbanki. There has been heated political debate in Iceland on how extensive the governmental guarantees should be.

... while downsizing its budget ...

Another challenge facing the government is to downsize government expenditures in accordance with guidelines set out in the IMF programme. This calls for a balanced budget by 2013 at a time when tax revenue is falling due to decreased economic activity and social spending is soaring in light of increased unemployment.

The Ministry of Finance bases its budget on a projected contraction of the economy of 1.9% in 2010, an unemployment rate of 10.6% and a fall in real household income of 11.4%.

These are not rosy figures. To get closer to the goal of a balanced budget, government spending will be cut by 7.3% in 2010 in real terms. In addition, it is clear that taxes will have to be raised. The government has announced that it plans to raise both existing taxes as well as adding new taxes.

Taxes in Iceland have been among the most favorable in Europe. It is inevitable that taxes will be raised, some considerably, to close the budget gap.

...and infuriating industry with tax plans.

A planned tax on energy use has proved enormously controversial with several planned projects, including the latest enlargement of Rio Tinto's Straumsvík smelter, causing the project to be put on hold.

The tax will most likely be scaled back or abolished to ensure the continuation of the stability pact signed with the social partners in June.

In addition, the decision by the Minister of the Environment to annul a decision by the Icelandic Planning Agency that the Helguvík smelter of Norðurál would not have to go through a joint environmental impact assessment, has also come under heavy fire.

This decision has infuriated the industrial sector as well as the social partners who criticize the government for endangering the stability pact signed in September. According to the stability pact, the government committed itself to facilitating large scale projects already on the table.

Following declarations from the government that these decisions would all be revised, the social partners decided to stick to the stability pact and extend existing wage contracts to the end of November 2010.

At the end of October, the Icelandic Planning Agency confirmed its earlier decision that a joint environmental impact assessment was not required.

Foreign Investment In Iceland – The Short Version

A late industrial revolution...

For the most part of last century, the fishing industry was the only game in town. Up to the mid-1960s, fishing accounted for close to 95% of Iceland's export income. Industry was almost non-existent and engineers and people with specialized technical education and skills were scarce.

Industry attributed less than 1% of export income.

...initiated by chance ...

It can be argued that Iceland's industrial revolution did not start until the 1960s. In 1961, two Swiss aluminium executives passed through Iceland on their way back from the United States. Flying over Iceland they saw a mountainous country rich in water. Coming from an alpine country, they recognised the obvious hydroelectric possibilities.

Shortly afterward, the Swiss company AIAG (later Alusuisse) declared its interest in constructing an aluminium smelter to the Icelandic government.

The decision was one of the largest economic decisions that an Icelandic government had faced. The smelter would have an enormous impact on the economy and the society as a whole.

The Straumsvík smelter started production in 1969 with an initial capacity of 33,000 tonnes. Its present capacity, after a series of expansions, is 180,000 tonnes with further expansion being planned.

...that came just in time...

Iceland's fishing industry was simultaneously going through a crisis due to diminishing stocks and a slump in global prices. The industrial output of the Alusuisse smelter had a welcome impact with industry accounting for almost a fifth of Iceland's export income in 1970.

The industrial revolution Part II...

The need to diversify the economy was one of the decisive factors when Iceland chose to compete for the construction of aluminium smelters. The reliance on fishing was a mixed blessing. It assured prosperity, but was also the primary factor behind the great fluctuations of the Icelandic economy in the 1970s and 1980s. To reduce this volatility and take advantage of the energy potential, Iceland decided to seek further industrial investment.

The only viable way to make use of Iceland's energy resources was to sell the electricity to large-scale end users. In spite of an abundance of energy and relatively low prices, the investments did not materialize as easily as hoped.

...adding ferro-silicon ...

The next major step was taken in the late 1970s with the construction of a ferro-silicon plant at Grundartangi, north of Reykjavík. The plant was initially supposed to be a joint venture between Icelandic authorities and American firm Union Carbide.

Union Carbide withdrew from the project in 1976 and was replaced by Norwegian firm Elkem. In 1984, the Sumitomo Corporation of Japan became a shareholder. In 2003, Elkem took full control of the company, purchasing the shares of both Sumitomo and the Icelandic government, which had kept a 10% stake.

... and seeking more aluminium.

Efforts to attract new investors in the aluminum sector gained strength in the beginning of the 1990s. In 1990, Iceland's hydroelectric plants churned out a total of 4,000 Gwh per year, which still amounted to only 8% of the power potential.

A consortium of three large industrial companies, Atlantsál, was formed in 1990 by Granges of Sweden, Hoogovens of Holland and Alumax of the United States. Atlantsál's plans for a large smelter at Keilisnes were postponed repeatedly due to uncertainty in the metal markets. With the break-up of the Soviet Union in 1989, cheap aluminium flooded global markets during the 1990s making investors wary of new and large commitments.

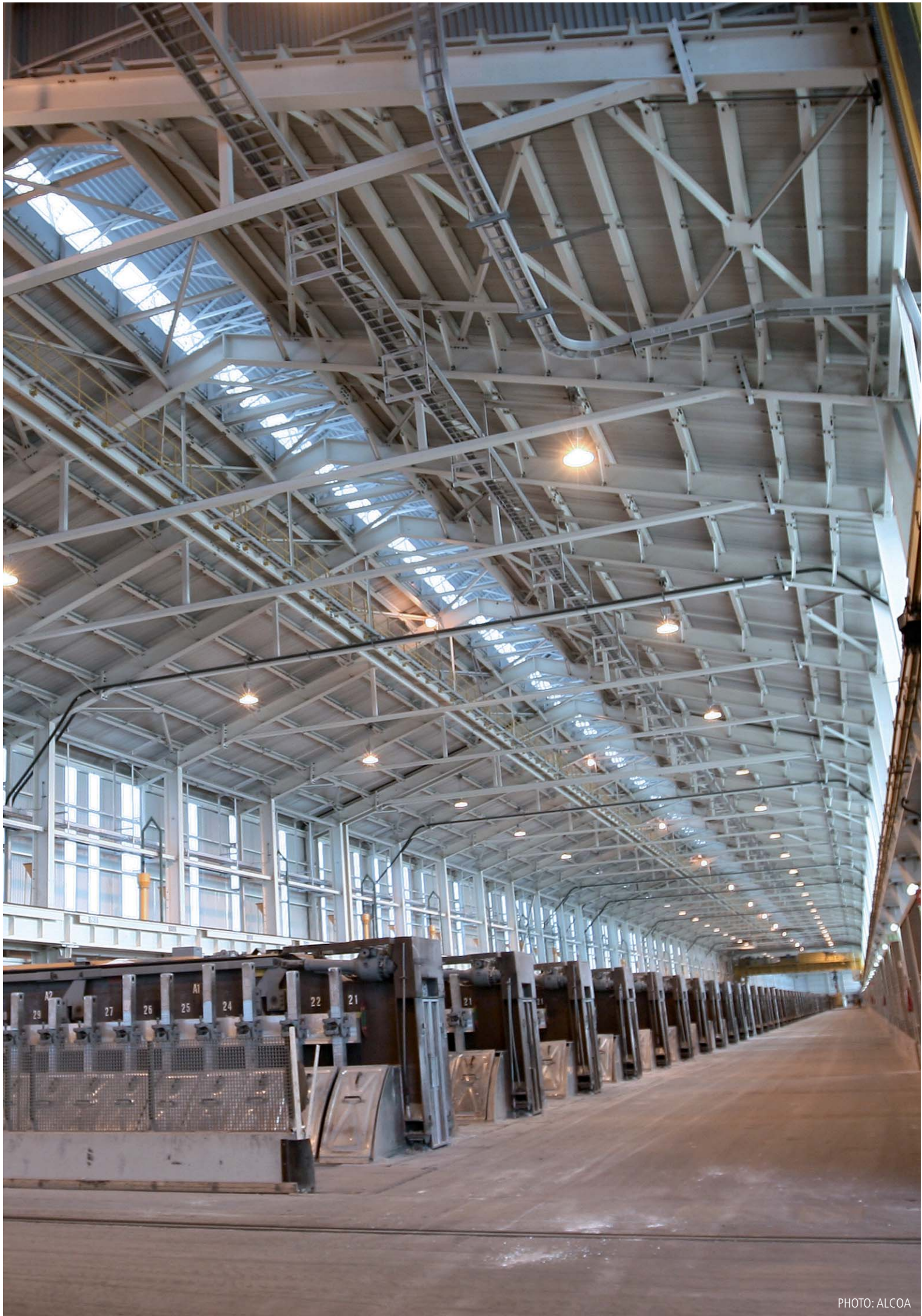


PHOTO: ALCOA

An American enters the scene...

In the mid 1990s, Kenneth Peterson, a lawyer in his 40s whose firm Columbia Ventures Corporation operated four smelters in the US, suddenly entered the scene. Peterson had been on the lookout for a site for a new aluminium smelter and decided to have a look at the possibilities in Iceland.

Peterson decided to build the plant in Iceland and said publicly that a major factor had been how easily things moved in Icelandic society, both on the private and public side. Decisions were taken and implementations were swift.

In June 1998, only 32 months after Peterson first showed interest in investing in Iceland, the smelter at Grundartangi began production.

Peterson has since been an active figure in Iceland's business environment. He took a stake in a telecom start-up, Halló fjarskipti, in 2000. Halló later became Íslandssími in 2002 and eventually Vodafone. Peterson sold his 35% stake in Vodafone in 2004 after having received a bid for the shares from Northern Lights (later 365 Media/Teymi).

...and another one goes east.

The next major project was already being discussed with Norwegian industrial giant Norsk Hydro (then Hydro Aluminium). The Noral-project envisaged a large smelter in Reyðarfjörður on the east coast of Iceland. Norsk Hydro backed out of the project in the final stages in the spring of 2002. It had invested heavily in a German aluminium firm and declared that its investment capacity was too stretched to commit itself to the Noral-smelter.

Almost immediately, the American firm Alcoa declared itself willing to step into the void left by Norsk Hydro. Negotiations were finalized and the largest project in the history of Iceland culminated in the opening of the Fjarðarál-smelter in 2007.

A changing society...

The industrial revolution in Iceland has had far reaching consequences in tandem with other societal trends. Iceland's path from economical insularity to being a part of a larger, global playing field took a leap during this period. The 1960s had been a continuous period of economic and trade liberalisation in Iceland culminating in membership of the European Free Trade Association in 1970.

Iceland was now firmly tied with both Europe and the United States, economically as well as politically, through its membership in EFTA and as a founding member of NATO.

...looking east and west...

Icelandic authorities have always been keenly aware of Iceland's Mid-Atlantic position and with it the need to look towards both east and west.

The impact of the United States in Iceland has been of a major importance. Thousands of Americans were stationed at the Keflavík naval base during the Cold War and American cultural influence was rampant. The proportion of US-made SUVs is still higher on the streets of Reykjavík than any other European capital and Icelandic supermarkets are stocked with American products as well as European.

Since the 1990s, the focus has increasingly moved towards the east. With the end of the cold war, the American presence was continuously downsized until the final closure of the Keflavík base in 2006. Europe on the other hand moved closer. In 1989 Jacques Delors, the President of the European Commission, offered the Nordic countries to become a fully integrated part of the European Union's inner market.

Iceland along with Sweden, Finland and Norway entered the European Economic Area in 1994, but Iceland chose not to follow Sweden and Finland into full EU membership in 1995. Norway negotiated for membership but the agreement was rejected in a national referendum.

Iceland, Norway and Liechtenstein still make up the EFTA part of the European Economic Area with Switzerland rejecting membership even of EEA in a referendum.



...and educating itself globally

Another important trend during the last decades was the education revolution. In 1970, Iceland spent some 3.6% of its national product on education. Some three decades later, Iceland spent over 8% of GDP on education, more than any other OECD nation.

Iceland now has one of the highest proportions in the world of people graduating from college. A high percentage of the student body, not least on the graduate and post-graduate level, is educated outside of Iceland, mainly in Northern Europe and the US.

Spending on research has also been considerable with Iceland reaching the 3% of GDP threshold in 2001.

The mix of internationalization, liberalization, foreign investment and research and development has added additional foundations to the Icelandic economy.

From metals to Marel...

During the last two decades of the 20th century, a new breed of Icelandic company started to emerge out of the country's research environment.

At the end of the 1970s, a government report highlighted the need for technological improvement in Iceland's fish processing industry, prompting researchers and entrepreneurs to team up, eventually leading in 1983 to the foundation of Marel.

The company was initially focused on developing technological solutions for the domestic fish processing industry, which was a large and quality-demanding market. The solutions developed in bone detection and laser vision portioning were applied to poultry processing and other segments of the food processing industry and the company soon outgrew its Icelandic roots.

Exports were close to 80% of sales by the end of the 1980s and the domestic market accounted for just 1% of sales in 2008.

The company has continued to grow organically and through acquisitions of foreign firms such as Scanvægt and Stork Food System.

Marel has also attracted several foreign institutional investors. In September 2009, Columbia Wanger Asset Management, a subsidiary of Bank of America, acquired a 5.2% stake in the company, bringing the total share of foreign investors in Marel to 16%.

... a leading position in prosthetics...

This is also the case with Össur, another company growing out of the Icelandic research environment. Its origins are indeed modest with Mr. Össur Kristjánsson founding a small prosthetic clinic in 1971. The company's research and development led to the patenting of prosthetics solutions in the 1980s and through an ambitious acquisition policy, the company is now the second largest orthopedic company globally.

In 2004, Danish health care company William Demant took a position in Össur and is now the largest shareholder along with Danish pension fund ATP which is the fourth largest.

...and generics, genetics and eventually online-gaming

The Delta pharmaceutical company was founded in 1981 and based its production on generic drugs. It grew quickly and started exporting 1988. The development of new generics expanded its scope and the company gained new markets. In 2001 it merged with Omega Farma, an Icelandic pharmaceutical company founded in 1991. Together, the two companies merged with Bulgarian pharmaceutical company Balkanpharma and formed generics giant Actavis Group.

Decode Genetics was founded in the United States in 1996 and established Íslensk erfðagreining in Iceland focusing on genetic research. The NASDAQ-listed company has become an important pillar of the Icelandic research environment with up to 40% of the annual R&D of private companies.

Software technology was another growth area of the Icelandic economy in the 1990s with companies like Oz (now Oz Communications owned by Nokia), TM Software, Hugvit and later CCP leading the way.

Where have investors come from?

United States and Scandinavia are prominent...

When looking over the field of foreign investors in Iceland during the last century, a few curious facts stand out. One is the fact that most major investments have been made by either North American or Nordic investors, the big exception being the construction of the Straumsvík aluminium smelter by Alusuisse of Switzerland.

Another interesting fact is that the most successful investments have been long-term investments with a strong commitment to the Icelandic economy.

...proximity is a factor...

In a September 2009, Capacent Gallup poll respondents were asked whether the origin of foreign investment was an important factor.

Not surprisingly, the preference of investor origin forms concentric circles with geographical, cultural and political proximity being key factors.

The preferred choice is investment from the neighboring Scandinavian countries with Norway in particular being a popular choice. Following Scandinavia is Europe, the United States and "western" countries in general.

...while UK investors have been absent

Icelandic investments on the other hand have predominantly been in Denmark and the United Kingdom. Interestingly, from a historical perspective, there has until lately been an almost total absence of UK investors entering the Icelandic economy.

History is telling...

While the largest investments by foreign firms in Iceland have either been in energy intensive industry or technological leaders like Össur and Marel, there are numerous examples of foreign firms entering the Icelandic economy with long term investment in various sectors.

ÍSAGA - AGA

One of the oldest foreign investments in Iceland is the firm ÍSAGA, founded in 1919 as a subsidiary of Swedish gas producer AGA (now part of the Linde Group). AGA had built its first light tower in Iceland in 1909 and the Icelandic subsidiary's original purpose was to service light towers around the island with gas. AGA had an 85% stake in ÍSAGA for decades, but sold its shares in all foreign subsidiaries that were not fully owned in 1974. In 1990, AGA made a bid for shares in ÍSAGA and again became the largest shareholder. ÍSAGA currently operates three plants in Iceland supplying industry with gas.

NORTHERN DIATOMITES

Lake Mývatn in northern Iceland is immensely rich in minerals and has a huge potential for diatomite production. Plans for a diatomite plant started to emerge in the late 1950s, and Dutch firm AIME was heavily involved in the development of the plant. The Dutch opted out of the project due to uncertainty about European markets, but were quickly replaced by American investors. In 1967, the Icelandic Diatomite Company started operation as a joint venture between the American firm Johns-Manville (later the Celite Corporation), the government of Iceland and 18 local municipalities in Northern Iceland. Initially, an operational period of 20 years was foreseen, but the plant continued operating until the end of 2004. Originally, the annual production of the plant was 12,000 tonnes, but capacity was soon increased to 30,000 tonnes annually. The plant was closed due to soaring production of diatomite globally, falling world market prices and environmental concerns.

ÍSTAK – E. PHIL & SÖN

E. Phil & Sön is Denmark's most important contracting firm and one of the world's 80 largest. Its origin though was partly in Iceland. Kay Langvad, a civil engineer working for E. Phil & Sön, worked on the construction of the first geothermal district heating system in Reykjavik in the 1940s, and in 1947 he acquired a 50% stake in E. Phil & Sön. The company was heavily involved in various projects in Iceland throughout the 1950s and 1960s. The Danish construction company founded an Icelandic subsidiary in 1970 called Ístak. The Danish company still holds a 90% stake in Ístak, which quickly grew into one of Iceland's largest construction companies. Ístak's first project was building a hydroelectric plant and it has been a part of most major construction projects in Iceland in the last three decades.

INVESTING IN OIL DISTRIBUTION

The Icelandic oil market has traditionally been divided between three firms; Oliufélagið, Skeljungur and Olís. The size of the market has attracted some foreign investment with the firms not only supplying the domestic transport market with fuel, but also the large marine fleet as well as aviation. Shell Petroleum was for decades the largest shareholder in Skeljungur or Shell of Iceland. Shell held a fifth of the company's shares with Shell Asia also holding close to 10%. Shell sold off its stake in the company in 2003 to a consortium of Icelandic investments companies, primarily Burðarás and Sjóvá. In 1986 an Icelandic entrepreneur, Mr. Óli Kr. Sigurðsson, made a surprise bid for one of Iceland's three main oil import and distribution firms, Olís. Mr. Sigurðsson had made his fortune in import and retail, but soon ran into difficulties in the running of Olís. In 1989, he was faced with an ultimatum from his bank to recapitalize the company. He entered negotiations with Texaco and in September 1989, Texaco Denmark announced that it was taking a 28% stake in the company. Texaco later increased its stake in the company and made a joint bid for Olís with Oliufélagið, another domestic firm, in an effort to preempt a possible entry of Canadian Irving Oil. Texaco sold off its shares in Olís in a 2003 management buy-out.

STEINULL – ICELANDIC ROCK WOOL

The Icelandic Rock Wool Company began operating in 1985 producing mineral fiber insulation at its plant in Sauðárkrókur, northern Iceland. The company uses local basalt sand and crushed seashells to produce rock fiber insulation and has an annual production capacity of 8,000 tonnes. The company was founded as a joint venture between Finnish company Partek (later Paroc Group Oy) and local public and private partners. Paroc currently holds a 11.5% stake in the plant.

REITAN – BAUGUR

The Norwegian firm Reitangruppen took a 20% stake in Baugur in 1998. Baugur was starting to build its retail empire on the back of low-cost chain Bónus. The firm had recently acquired the up-scale retailer Hagkaup and was in need of additional capital. Baugur was delisted in 2003 with sister company Gaumur buying the shares of Reitan Handel.

ALUMINIUM FOIL IN AKUREYRI

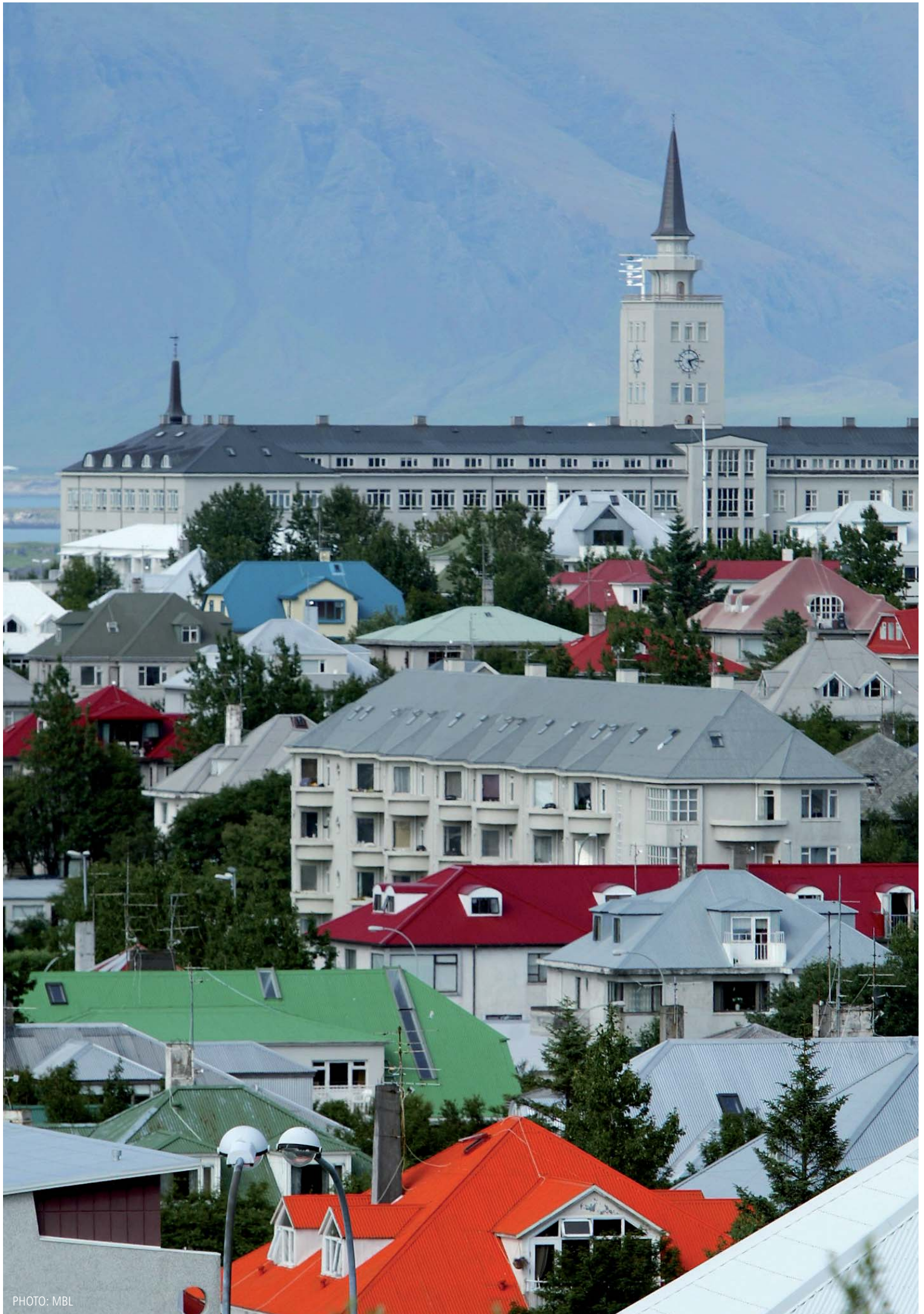
In 2007, the Italian firm Becromal (now part of German group Epcos) teamed up with local partners in constructing an aluminum foil plant in Akureyri, northern Iceland. The plant started production in 2009 producing high voltage foils and will soon have the capacity to produce one million square meters of high quality foil per month.

IRISH MINE SEA MINERALS

A plant constructed by Irish firm Celtic Sea Minerals started mining sea minerals in Bíldudalur, western Iceland in 2007. These minerals are used in several food products as well as cattle feed. Celtic Sea Minerals, which was licensed to harvest seaweed off the coasts of Ireland and Wales in 1991, was facing increasing demand which it was not able to meet with its local resources. In Iceland, they found the right mineralized red seaweed that met production standards in abundance. The Celtic Sea Minerals plant in Bíldudalur is the largest of its kind globally. Celtic Sea holds a 75% stake in the plant with local partner Björgun as the remaining shareholder.

ROCHE NIMBLEGEN – NIMBLEGEN SYSTEMS ICELAND

NimbleGen (now Roche NimbleGen) a Madison, Wisconsin, firm producing DNA Micro Arrays for research opened a subsidiary in Iceland in 2002. The director of the company said the reason for the choice of Iceland was the country's location, transport system, the education and skill level of the work force, fluency of english, and a positive patent legislation. Roche NimbleGen uniquely produces high-density arrays of long oligo probes that provide greater information content and higher data quality necessary for studying the full diversity of genomic and epigenomic variation.



The Case For Investing In Iceland

In the immediate aftermath of the 2008 financial collapse, Iceland was flooded with prospective investors hoping to reap quick profits.

In most cases they left empty handed with both authorities and bank resolution committees determined to take a long-term view on the situation. The only actual fire-sale was on sensitive foreign assets which had to change hands quickly to retain any value.

Today there are opportunities in the Icelandic market for foreign investors but also challenges that have to be taken into account.

Iceland wants and needs foreign investment

The need for foreign investment is clear and independent polling of the population shows strong support for foreign investment by both the general public and Icelandic executives.

There will be many opportunities for investors to enter different sectors of the Icelandic economy when companies now in the hand of asset management firms will be put up for sale.

In spite of the generally positive sentiment towards foreign investment there is wariness among the general public, the business community and the authorities against short term vulture investors.

We believe that both the Icelandic authorities and financial institutions will be looking for investors ready to commit themselves to the purchased firms, with a medium- to long-term investment horizon.

It is important for potential investors to be aware of these sentiments and to have the necessary insights into the key dynamics of Icelandic society.

In addition, the short to medium-term volatility of the Icelandic situation is well suited for long-term investors but poses potential risks for those looking for short-term profit.

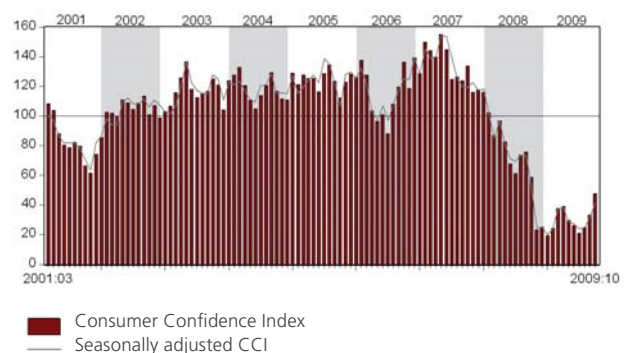
A fragile recovery

There are several indications that the Icelandic economy is on its way to recovery. In September 2009, the Consumer Confidence Index rose for the third consecutive month and polling also shows signs of increased confidence among Icelandic executives with EBITDA-expectations rising to their highest level since October 2008.

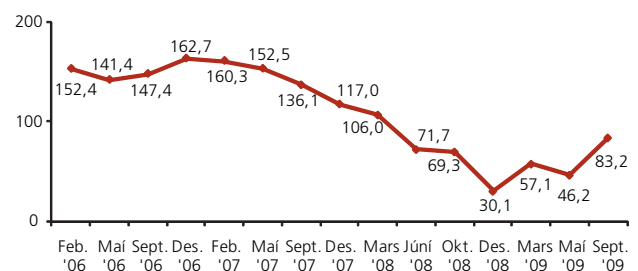
At the same time, several major hurdles to recovery have been overcome. With the resolution of the Icesave dispute, the IMF finally approved its first review of Icelandic economic performance under the 2008 loan agreement.

With increased confidence of both consumers and executives consumption is likely to begin to increase, slowly stimulating economic activity and growth.

CONSUMER CONFIDENCE INDEX



EBITDA
Future Expectations Index



A risky currency

The strength of the Icelandic króna to other currencies had been a major factor in inhibiting foreign investors from entering the Icelandic market. Following the financial crisis, the value of the króna plummeted from a high of ISK 60 to the dollar to presently ISK 125 to the dollar and at present levels there are great entry opportunities for investors.

There is still considerable uncertainty regarding the future FX-levels of the króna. The Icelandic Central Bank has started dismantling foreign exchange restrictions that were applied in 2008 with the goal of abolishing them totally by the end of 2010.

A major risk-factor for the króna are the ISK 500 billion still locked in króna bonds inside the economy as a legacy of the speculative carry trade. When currency restrictions are totally abolished these investors are likely to stampede out of the economy, which could weaken the króna further, at least temporarily, unless the Central Bank manages to orchestrate a controlled exit of these funds out of the economy.

Additionally Iceland is facing a steep increase in interest rate payments due to soaring public debt and the Icesave-agreement with the United Kingdom and the Netherlands. The base rate of the Central Bank is still in the double digits, despite the Central Bank lowering it by 100 basis points to 11% on November 5th.

A favorable tax regime ... ?

The corporate tax environment in Iceland is still one of the most favorable in Europe with corporate tax currently at 15%. However the present government has announced tax increases to reach the goal of a balanced budget by 2013. How this will affect corporate taxation is still not clear.

The bulk of government revenue in Iceland comes from indirect taxation, with VAT being the most important tax revenue source. The government intends to raise more taxes through increased duties on alcohol, tobacco and gasoline as well as raising personal income taxes and the capital gains tax, which is now 15% up from a previous level of 10%.

A planned tax on energy is likely to be scaled back significantly or withdrawn after coming under heavy criticism from both labor unions and the business community. However, the surprise announcement of the tax with the presentation of the 2010 budget shows that radical changes of the tax environment cannot be excluded due to the government's need to balance the state budget.

UNEMPLOYMENT RATES
Q2 2009



A skilled and educated workforce

Iceland has one of the most educated and skilled English speaking workforces in the world. According to the 2009 World Competitiveness Report Iceland scores number 3 globally regarding the quality of the educational system and is the world leader regarding availability of latest technologies in companies and regarding firm-level technology absorption.

A side-effect of the collapse of the financial system is that a large pool of highly skilled and educated people is now available to re-enter the market. The collapsed banks employed a very high proportion of those with a higher education in finance, engineering and accounting.

Political stability

The year 2009 has been a rollercoaster ride for Iceland. The first weeks of the year were marked by demonstrations, a governmental crisis and, finally, elections in April. Iceland has applied for EU-membership and formal negotiations are likely to commence in 2010.

So what lies in the future? In spite of a turbulent year, history suggests that political stability will remain the norm. Iceland has a strong tradition of broad coalitions on major issues. The most contentious issues faced by the government in the upcoming months and years are, on the one hand, a possible membership of the European Union and, on the other hand, economic diversification.

Although the question of EU-membership is politically controversial the issue has been channeled into a clear process. Iceland will negotiate for membership but whether or not these will lead to an eventual membership will be settled by a national referendum at the end of the negotiation process. Opinion polls on the issue have shown great fluctuations in public opinion with a clear majority being currently opposed to membership.

The second contentious issue is resource utilization which will be hotly debated. Whether or not Iceland chooses to concentrate on increased aluminum production, data centers or other industries there will be need for increased energy utilization. The need for a balanced budget in accordance with the IMF-criteria will put a great strain on the government. Public expenditure will have to be cut drastically and revenue increased.

What is the opportunity?

Finally there remains the question of what will be on offer for investors, domestic and foreign, and when. So far, the banks have not presented a clear vision on how and when they will divest or capitalize companies that have fallen into their hands.

At present their strategy seems to be to wait and hope for the value of assets to rise. The banks also seem to be hesitant to take action due to the risk of a public opinion backlash.

However, it is clear, that in the coming months and years, many of Iceland's major companies will be sold off to new owners and recapitalized. What is still uncertain is how swift this process will be.

The government sees Foreign Direct Investment as an important factor of the economic recovery process. In the October 2009 IMF review of the agreement with Iceland, the fund stresses that the Icelandic authorities have acknowledged the need to boost the perception of Iceland as an attractive destination for foreign investment.

As we have seen, most foreign private equity investors entering, and exiting, the Icelandic economy during the last century have been successful and have in addition had a beneficiary effect on the economy as a whole.

Insurance, finance, telecom....

There will be opportunities in most sectors of the Icelandic economy, including finance, insurance, telecom, retail, industry and tourism with major firms intending to seek new private equity investment in the coming years.

The insurance sector is a good example. Sjóva, one of Iceland's largest insurers, was part of the Milestone group, but is now under the control of a new company, SA insurance. Sjóva has de facto been taken over by the Icelandic government through Glitnir and Íslandsbanki, with the stated intention of selling the company in due time.

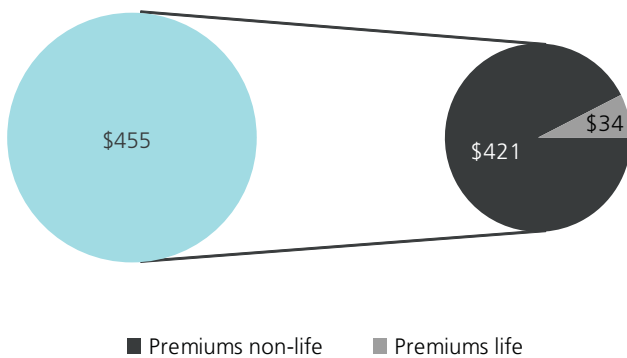
Vörður, another major insurer, has also changed hands with Føroya Banki taking a 51% stake in the company. A large part of the remaining shares are in the hands of Icelandic financial institutions. The sellers have under certain circumstances options to sell their remaining shares to Føroya Banki in the first half of 2012.

VÍS, Iceland largest insurer, is a part of the Exista Group and therefore de facto indirectly under the control of creditors. Exista was the largest shareholder in Kaupthing Bank and has been in dire straits since the fall of the bank.

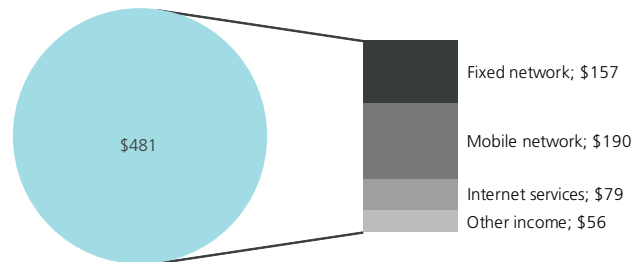
Skipti, the operator of Iceland Telecom or Síminn, Iceland's largest telecommunications company, is also part of Exista. Although it has been run independently from the mother company, it has been affected by Exista's difficulties. Skipti started a restructuring of its operations in early 2008 prior to the crash and is also helped by the fact that a large part of the company's revenues are derived from its operations in Scandinavia.

The second largest telecommunications company of Iceland, Vodafone, has recently gone through restructuring with Landsbanki taking a 62% stake in the company through its asset management arm, Vestia. The main objective of the restructuring is to prepare the company for a sale to new investors.

THE INSURANCE MARKET 2008
(Millions USD)



THE TELECOMMUNICATIONS MARKET 2008
(Millions USD)



A brighter future

The Icelandic economy is still going through a rough patch and there will be difficulties in the years ahead due to a weak currency, soaring public debt and a fledgling financial system being built on the ruins of the old banks.

In spite of that most analysts are in unison that the long-term prospects of Iceland are brighter than for many other developed countries, due to an abundance of resources and a highly educated, skilled and young population.

Foreign investors, have in 2009 already shown interest in investing in Iceland on an unprecedented scale.

Some major investments this year include

- Magma Energy acquiring a 43% stake in the energy utility company HS Orka for a sum of US\$ 125 million, additionally committing itself to participate in the construction of new energy plants with a capacity of 250 MW at an estimated cost of US\$ 600 million.
- British Seafood acquiring a 70% stake in Iceland Seafood.
- The Faroese Føroya Banki taking a 51% stake in the insurance company Vörður with an option to acquire the remaining shares in 2012.
- A US investment fund becoming a major shareholder in shipping company Eimskip.
- Columbia Wanger Asset Management acquiring a 5.2% stake in Marel.

We believe firmly, that there are currently more opportunities for foreign investors than previously in history. Not only due to the advantages of a low króna but, in addition, a change in general sentiment in Iceland.

As polls show, the Icelandic public is generally very favorable towards foreign investment.

In addition there is a growing understanding of the need for a diversification, not only of the economy as a whole but of company ownership.

Iceland's troubles are partly due to the close bonds between individuals and firms in the Icelandic market and there is strong public and political demand for new players to enter the scene.

Foreign investment is therefore not only viewed as a source of necessary private equity but as a tool to internationalize and diversify the business community.



Capacent Glacier is an independent Finance Advisory Boutique, licensed by the Icelandic FSA. We provide services related to mergers and acquisitions, capital raising, fairness opinions, Purchase Price Allocations, impairment tests, balance sheet restructuring and general strategic corporate matters.

The firm focuses on the Icelandic market and globally on the seafood and geothermal energy sectors. Capacent Glacier operates under a strategic alliance with Glacier Partners in New York and Capacent consulting group in the Nordic countries.

Our senior professionals advise clients on mergers and acquisitions, debt and capital raising, as well as balance sheet restructuring transactions. We provide knowledge-based strategic and financial advice, with a view to build long term relationships with our focus industries. Glacier Partners was formed by the founding members of Glitnir Capital Corp's International Banking Division (North America, LATAM and Asia).

The North American team was responsible for deploying and managing a \$780 million merchant banking portfolio tailored to the specialized requirements of the Seafood and Geothermal Energy Industries. The team's professionals also completed several benchmark M&A and financing transactions, and have been recognized as a leading practice in these two niche industries.



Capacent is the leading Nordic business consultancy with more than 500 employees, including 100 in Iceland. Capacent is deeply rooted in the Nordic countries and has offices in Denmark, Sweden, Iceland, Finland and Norway. We focus on improving our clients' business performance by providing sustainable, no-nonsense results.

With our unique combination of Management Consulting, Market Research and People Services, Capacent offers a unique set of cross-functional capabilities.

Our business philosophy is to focus on the entire value chain when helping our clients improve their businesses. The service offering is therefore focused on generating critical knowledge, developing strategies and optimising processes with a strong focus on developing human resources.



Founded in 2001, Pritchard Capital Partners, LLC is an independent and institutional financial services firm, focused on idea generation and intelligence in the oil, gas and power markets. With an emphasis on all segments of the energy sector - exploration and production, oilfield services and renewable energy - Pritchard Capital Partners has quickly proven to be a recognized leader and provider of value-added financial advisory expertise in corporate finance, institutional sales and equity research.

Since 2005, Pritchard Capital has been involved in approximately \$12 billion worth of capital transactions. The Investment Banking division offers a broad array of services and aftermarket support for companies in all segments of the energy industry: exploration and production, oil services, seismic, marine transportation, coal, tankers, utilities and renewable energy.

The Team



Magnús Bjarnason

Magnus Bjarnason has a B. Sc. In Business Administration and holds an MBA degree from Thunderbird, Arizona. Mr. Bjarnason served as the Managing Director of

Corporate and Investment Banking for region Asia and Americas at Glitnir Banki hf. where he lead all niche related activities within the bank. Mr. Bjarnason served as Minister Counselor and Deputy Chief of Mission at the Icelandic Embassy in China 2003-05. He was the Trade Commissioner for Iceland in the USA and Canada 1997-2003 and Consul General in New York 2000-2003. He worked for Landsbanki Islands in corporate credit and business development for seafood customers, Islandsflug and OLIS (Icelandoil) in Reykjavik prior to joining the Foreign Service in 1996. Mr. Bjarnason has served as a board member for numerous organizations.



Jón Diðrik Jónsson

Jón Diðrik Jónsson is Chairman of Capacent Glacier. He was CEO for Iceland, Glitnir Bank 2007, EVP for Corporate and Investment Banking and Business

Development 2005-2007. Jón Diðrik worked for years in the beverage industry, as CEO of Egils Beverages from 2001-2004, General Manager of CCHBC Slovenia 2000-2001, Commercial Director/Marketing Director of CCHB Poland 1997-2000, Marketing Manager of Coca-Cola Singapore/Malaysia 1995-1997, TCCC Nordic Region Business Development Manager 1994-1995, Operational Marketing Manager for Nordic & Northern European Division of TCCC 1992- 1993, Food Department Manager for Vífilfell, Coca-Cola Bottlers of Iceland 1990-1992. Marketing Manager for Icelandoil (Olís), 1988. Jón Diðrik holds an MBA-degree (management) from Thunderbird, School of Global Management, Arizona, and a B.Sc degree in management from the Florida Institute of Technology.



Kristján Arason

Kristján has a B.Sc. Degree in business administration from the University of Iceland. He has 15 years of banking experience. He has served as a Managing

Director of Retail Banking, head of Private Banking, branch manager and an equities trader.



Sturla Geirsson

Sturla has a B.Sc. degree in business administration, M.Sc. degree in corporate finance from the University of Iceland and is a licensed securities broker. Sturla has

extensive experience in various managerial positions, mainly in wholesale, but also in the retail sector. He was CFO/CEO of Icelandic Pharmaceuticals, managing director of Litis ehf., focusing on investments in the health sector of the Baltic republics, among other positions. Sturla has been a project manager of Valuation services, Purchase price allocation and Impairment assignments for companies in various sectors, operating in Iceland and abroad.



Jón Garðar Guðmundsson

Jón Gardar holds a Cand Oecon. degree in Business Administration from the University of Iceland and a MBA degree from IESE Business School, Barcelona, Spain. He served

as MD at Glitnir's seafood team from 2003-2008, where he lead the Asian & Latin American region, originating numerous high profile seafood transactions, including the IPO of Copeinca ASA at the Oslo Stock Exchange and the financing of Europacifico in Spain.

Previously, Jón Garðar worked as CFO at Icelandic Iberica S.A. in Barcelona, Spain, at VSÓ Ráðgjöf, Iceland and at PwC in Brisbane, Australia. Jón Garðar worked his way through his studies in Iceland on fishing vessels and at a salmon farm, among other industries. Jón Garðar is a trilingual English, Spanish and Icelandic speaker.



Timothy Spanos

Mr. Spanos earned a B.S. in Aerospace and Ocean Engineering from Virginia Tech in June 1981. He received an M.B.A. from Emory University in May 1984 where he

was a Robert W. Woodruff Fellow in Graduate Business Administration. Mr. Spanos served as Managing Director of International Corporate Credit for Glitnir Banki hf. where he was the senior credit officer responsible for the Bank's International credit portfolio. Mr. Spanos was also a member of the Bank's Corporate Credit Committee for loans originated in International Banking. Mr. Spanos has over 22 years experience in various corporate banking and risk management roles at Glitnir and Bank of America. He currently serves on the Board of Directors of the Icelandic Fulbright Commission and the Icelandic American Business Forum.

**Sigurður Valgeir Guðjónsson**

Sigurður is a lawyer from the University of Iceland (1999) and District Court Attorney since 2000. He worked in the banking sector from 1999, both in Iceland and

abroad, mostly in Corporate Finance, where he has participated in various local and cross border transactions. For the last two years before joining Capacent Glacier, Sigurður worked at Glitnir bank as Director in the Investment Banking unit.

**Sigurður Jón Björnsson**

Sigurður has a B.Sc. degree in business administration from the University of Iceland '94, and is a licensed securities broker.

Since graduation, Sigurdur worked as CFO and investment manager at Framtak Venture bank. His experience is in the field of management of real estate, software development, financial services for medium and big industrial companies in Iceland and abroad. Sigurður joined the Capacent consulting team in 2007 and has worked on various projects connected with capital structure, real estate management, valuation, and public relations.

**Ignacio Kleiman**

Ignacio Kleiman is a founding member of Glacier Partners serving as Managing Director of Corporate Finance.

Prior to forming Glacier Partners, Mr.

Kleiman served as Managing Director and Head of Corporate Finance for the Americas at Glitnir Capital Corp. where he was responsible for the advisory practice. Mr. Kleiman has close to 20 years of M&A, private equity and turn around experience, transacting both in the U.S. and internationally. Prior to joining Glitnir, Mr. Kleiman served as Managing Director with Rabobank International's Mergers & Acquisitions/Financial Sponsors Group in New York. Past professional experience also includes positions with Deutsche Bank/Bankers Trust and JP Morgan. Mr. Kleiman holds an MBA from Columbia University Graduate School of Business and a double B.A. degree in Engineering Science and International Economics from Dartmouth College. He is fluent in English, Spanish, Portuguese and Italian.

**Rafn Árnason**

Rafn Árnason joined Glacier Partners at its inception as Associate of Corporate Finance having previously been an Analyst with Glitnir Capital Corp. where he was

influential on many transactions. Rafn has 6 years of experience within finance. He worked as a research specialist at The Central Bank of Iceland in 2002 (The Monetary Department) and again in 2003 (The Financial Department) after completing his B.Sc. degree in Industrial Engineering. In 2003 Rafn joined Islandsbanki hf. as a financial advisor and in 2004 he joined Reykjavik Savings Bank (SPRON) as a trader in the equity and bond market. At SPRON Rafn took part in restructuring department operations which led to a substantial increase in revenue and market share. Rafn was born in Reykjavik, Iceland and earned a B.Sc. degree in Industrial Engineering from the University of Iceland in 2003 and in May 2007 Rafn graduated with a M.Sc. degree in Industrial Engineering from Columbia University in the City of New York.

**Charles J. Arrigo II**

Charles Arrigo joined Glacier Partners at its inception serving as Director of Renewable Energy. As in his previous role with Glitnir Capital Corp., Mr. Arrigo spearheads the

firm's Renewable Energy business. Prior to joining Glitnir Mr. Arrigo was with BNP Paribas for 5 years as a member of its Energy and Utilities Debt Capital Markets group where he advised clients on a wide range of debt and capital structure related issues and was responsible for the origination of over \$5 billion of debt as a lead manager. During this time Charles work closely with BNP's Project and Structured Finance groups and arranged project bond financings for numerous energy projects including wind farms and cogeneration assets. Mr. Arrigo's past professional experience also includes positions with Citigroup's Utilities Debt Capital Markets Group and at its predecessor, Salomon Brothers. Mr. Arrigo holds a B.Sc. in Business Administration with dual concentrations in Finance and International Management from Boston University.

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