

Iceland

Quantitative Factors (Relative Weight in any Rating or Outlook Change)

30-Jan-2015 **Date of This Review**

28-Jul-2014 **Date of Last Review**

Weight	Factor	2012		2013		2014		2015		2016	
		A	A	A	A	F	F	F	F	F	F
Low	GDP per capita (USD, mkt exchange rates)	42,362	44,222	45,054	47,461	49,786	51,929	52,822	50,245	55,648	51,704
Low	Real GDP Growth (%)	1.5	1.2	3.3	3.5	2.8	1.9	3.1	3.2	3.1	3.0
Low	Consumer prices (annual average % change)	6.0	6.0	4.1	4.2	1.6	1.0	2.0	2.0	2.0	2.3
Low	General government balance (% of GDP)	-3.8	-3.7	-2.1	-1.7	-0.1	0.1	-0.5	-0.8	-0.3	-0.5
Medium	General government debt (% of GDP)	96.9	93.1	94.7	86.3	90.7	82.0	85.9	77.7	81.4	71.3
Low	Current account balance plus net FDI (% of GDP)	25.9	25.7	3.6	4.6	2.4	9.2	2.5	4.3	1.6	2.6
Low	Net external debt (% of GDP)	530.2	508.0	511.6	486.4	459.4	442.2	429.7	443.6	405.4	423.1

Colour key

n/a IMF Development Classification

DM

Improvement relative to previous review

n/a CDS Market Implied Rating

BB+

Deterioration relative to previous review

Qualitative Factors (Relative Weight in any Rating or Outlook Change)

Weight	Factor	Change since last review
Low	Fiscal Financing Flexibility	Stable
Medium	Public Debt Sustainability	Positive
High	External Vulnerability	Positive
Low	Banking System Strength	Stable
Low	Political Risk/Uncertainty	Stable
Low	Macro-economic Outlook, Policy Coherence and Credibility	Stable
High	Business Environment and Competitiveness	Positive
Low	Other Factors	Stable

Summary: Strength and Weaknesses

Factor	Status	Trend
Macroeconomic	Neutral	Stable
Public Finances	Weakness	Positive
External Finances	Weakness	Positive
Structural Issues	Strength	Stable

Footnotes

- 1 The risks, limitations and uncertainties associated with the ratings are detailed in the Rating Action Commentary.
- 2 Weights - 'High'/'Medium'/'Low' - reflect the relative importance of each Quantitative and Qualitative Factor in the context of a change in the rating or Outlook. Weights for Economic Development (IMF Development Classification) and Indicator of Default (CDS Market Implied Rating) will always be n/a because these indicators are not referenced in the Fitch Sovereign Rating Criteria.
- 3
- 4 All other relevant rating factors are referenced in the Rating Action Commentary

Discussion Note

Issuer: Iceland

Date of Rating Committee: 28-Jan-15

Before beginning the committee, the committee chair verbally confirmed all committee members were free from any relevant recusals. (Y)

Data was sufficient and robust relative to the rating decision. (Y)

Were there any significant deviations from the relevant rating criteria? (N)

Summary of Discussion

The rating committee discussed the following key issues:

Balance-of-payments implications of the Landsbankinn bond deal; current account forecasts and external debt servicing capacity

Lifting of capital controls: timing and potential options

Banking sector capital ratios, asset quality and risks

Risks to Central Bank independence

GDP growth outlook and GDP data revisions

Fiscal performance and public debt sensitivity analysis

Housing Finance Fund: risks to the public finances

Credit strengths and weaknesses, and rating peer comparisons

Potential rating actions, drivers, sensitivities and assumptions

The main opinions and conclusions of the committee are recorded in the RAC.



Definitions

Per capita income: GDP per capita (USD, mkt exchange rates)

Gross domestic product at current market prices in the local currency and converted into US dollars at annual *average* market exchange rates. GDP is the sum of consumption (private and government) *plus* gross fixed capital formation *plus* the change in inventories *plus* exports of goods and services *minus* imports of goods and services. Source: National authorities, international institutions.

GDP growth: Real GDP growth (%)

Annual percentage change (calendar year on calendar year) of a country's GDP in constant prices (ie, volume terms). Source: National authorities, international institutions, Datastream.

Inflation: Consumer prices (annual average % change)

Annual percentage change in the national consumer price index (CPI). Note: these are period averages, *not* year-end to year-end. Source: National authorities, international institutions, mainly IMF IFS.

Fiscal Balance: General government balance (% of GDP)

Consolidated balance of central government, provincial, regional and local governments, social security funds and other extra-budgetary funds; data may be presented on a cash or, more generally and preferably, on an accruals basis. Net lending is treated as an expenditure item and is *included* in the general government balance. Privatisation receipts are treated as a financing item and are *excluded* from the general government balance.

Note: in some countries data are available only for a fiscal year not coinciding with the calendar year. Where this is so, fiscal data are allocated to that calendar year in which the larger part of the fiscal year falls. For fiscal years running July-June, fiscal data are allocated to the year ending 30 June (ie, 1990/91 = 1991). Also note that for euro area countries, the figures may differ from those produced by Eurostat due to Fitch's treatment of UMTS receipts. Source: National authorities, international institutions.

Fiscal Debt: General government debt (% of GDP)

Year-end debt stock of the general government (as defined above); data comprise domestic and externally contracted debt regardless of maturity, and include monetary authorities' debt issued on behalf of the government. Contingent liabilities such as guaranteed debt are excluded, except where these are specified as a line item in the budget. Source: National authorities, international institutions.

External Balance: Current account balance plus net FDI (% of GDP)

Current account balance plus the net annual flow of foreign direct investment (US dollar value of FDI in the economy less resident FDI abroad), expressed as a percentage of GDP. Source: Fitch estimates based on national authorities and IMF.

External Debt: Net external debt (% of GDP)

Calculated by deducting certain classes of gross external assets from a country's gross external debt (GXD). All figures are converted into US dollars at year-end exchange rates and are expressed as a percentage of GDP. A minus sign indicates that the country is a net external creditor (ie, contractual external claims exceed liabilities). For all countries, the definition of gross external assets mirrors the definition of GXD, ie, exclusion of equity FDI and portfolio equity investment.

Fitch has therefore modified the definition of gross external assets for emerging countries, as it previously used "narrow" gross external asset definition, which excluded non-bank private-sector external assets for these countries. Therefore, the claims of the non-bank private sector would be included, on the grounds that these are the product of rational portfolio management and generate an identifiable income stream for the country of origin. Note that for those emerging markets that have entered into Brady debt deals collateralised by US zero-coupon bonds, the US dollar value to date of that collateral is included in official assets. Source: IMF IFS, national authorities, international institutions.

Economic Development: IMF Development Classification

Countries classified as Advanced Economies in the latest IMF World Economic Outlook are reported as Developed Markets (DM). Emerging Market and Developing Economies are reported as Emerging Markets (EM). Source: IMF World Economic Outlook, Fitch classifications for sovereigns not referenced in the IMF World Economic Outlook.

Indicator of Default : CDS Market Implied Rating

Derived from the Fitch CDS Implied Ratings (CDS-IR) model, which processes the collective marketplace view of issuers' credit condition based on its current CDS pricing and region. It then calculates and converts these into implied ratings. Source: Fitch Solutions.



The ratings above were solicited by, or on behalf of, the issuer, and therefore, Fitch has been compensated for the provision of the ratings.

ALL FITCH CREDIT RATINGS ARE SUBJECT TO CERTAIN LIMITATIONS AND DISCLAIMERS. PLEASE READ THESE LIMITATIONS AND DISCLAIMERS BY FOLLOWING THIS LINK: [HTTPS://FITCHRATINGS.COM/UNDERSTANDINGCREDITRATINGS](https://fitchratings.com/understandingcreditratings). IN ADDITION, RATING DEFINITIONS AND THE TERMS OF USE OF SUCH RATINGS ARE AVAILABLE ON THE AGENCY'S PUBLIC WEB SITE AT WWW.FITCHRATINGS.COM. PUBLISHED RATINGS, CRITERIA, AND METHODOLOGIES ARE AVAILABLE FROM THIS SITE AT ALL TIMES. FITCH'S CODE OF CONDUCT, CONFIDENTIALITY, CONFLICTS OF INTEREST, AFFILIATE FIREWALL, COMPLIANCE, AND OTHER RELEVANT POLICIES AND PROCEDURES ARE ALSO AVAILABLE FROM THE CODE OF CONDUCT SECTION OF THIS SITE. FITCH MAY HAVE PROVIDED ANOTHER PERMISSIBLE SERVICE TO THE RATED ENTITY OR ITS RELATED THIRD PARTIES. DETAILS OF THIS SERVICE FOR RATINGS FOR WHICH THE LEAD ANALYST IS BASED IN AN EU-REGISTERED ENTITY CAN BE FOUND ON THE ENTITY SUMMARY PAGE FOR THIS ISSUER ON THE FITCH WEBSITE.

Copyright © 2014 by Fitch, Inc., Fitch Ratings Ltd. and its subsidiaries. 33 Whitehall Street, NY, NY 10004. Telephone: 1-800-753-4824, (212) 908-0500. Fax: (212) 480-4435. Reproduction or retransmission in whole or in part is prohibited except by permission. All rights reserved. In issuing and maintaining its ratings, Fitch relies on factual information it receives from issuers and underwriters and from other sources Fitch believes to be credible. Fitch conducts a reasonable investigation of the factual information relied upon by it in accordance with its ratings methodology, and obtains reasonable verification of that information from independent sources, to the extent such sources are available for a given security or in a given jurisdiction. The manner of Fitch's factual investigation and the scope of the third-party verification it obtains will vary depending on the nature of the rated security and its issuer, the requirements and practices in the jurisdiction in which the rated security is offered and sold and/or the issuer is located, the availability and nature of relevant public information, access to the management of the issuer and its advisers, the availability of pre-existing third-party verifications such as audit reports, agreed-upon procedures letters, appraisals, actuarial reports, engineering reports, legal opinions and other reports provided by third parties, the availability of independent and competent third-party verification sources with respect to the particular security or in the particular jurisdiction of the issuer, and a variety of other factors. Users of Fitch's ratings should understand that neither an enhanced factual investigation nor any third-party verification can ensure that all of the information Fitch relies on in connection with a rating will be accurate and complete. Ultimately, the issuer and its advisers are responsible for the accuracy of the information they provide to Fitch and to the market in offering documents and other reports. In issuing its ratings Fitch must rely on the work of experts, including independent auditors with respect to financial statements and attorneys with respect to legal and tax matters. Further, ratings are inherently forward-looking and embody assumptions and predictions about future events that by their nature cannot be verified as facts. As a result, despite any verification of current facts, ratings can be affected by future events or conditions that were not anticipated at the time a rating was issued or affirmed.

The information in this report is provided "as is" without any representation or warranty of any kind. A Fitch rating is an opinion as to the creditworthiness of a security. This opinion is based on established criteria and methodologies that Fitch is continuously evaluating and updating. Therefore, ratings are the collective work product of Fitch and no individual, or group of individuals, is solely responsible for a rating. The rating does not address the risk of loss due to risks other than credit risk, unless such risk is specifically mentioned. Fitch is not engaged in the offer or sale of any security. All Fitch reports have shared authorship. Individuals identified in a Fitch report were involved in, but are not solely responsible for, the opinions stated therein. The individuals are named for contact purposes only. A report providing a Fitch rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed or withdrawn at anytime for any reason in the sole discretion of Fitch. Fitch does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Fitch receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US\$1,000 to US\$750,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US\$10,000 to US\$1,500,000 (or the applicable currency equivalent). The assignment, publication, or dissemination of a rating by Fitch shall not constitute a consent by Fitch to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act 2000 of the United Kingdom, or the securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing and distribution, Fitch research may be available to electronic subscribers up to three days earlier than to print subscribers.