

## FITCH COMMENTS ON ICELAND REFERENDUM REJECTION

Fitch Ratings-London-11 April 2011: Fitch Ratings says popular rejection of the latest 'Icesave Agreement' in a national referendum on 9 April has diminished the prospects of Iceland regaining an investment grade rating in the relatively near future. Fitch downgraded Iceland's Long-term foreign currency Issuer Default Rating to 'BB+' from 'BBB-' with a Negative Outlook on 5 January 2010, following a decision to refer an earlier Icesave Agreement to a referendum.

"Fitch has consistently maintained that the resolution of Icesave, a bilateral agreement with the UK and Dutch governments to finance the compensation of 'Icesave' depositors, is an important step towards the restoration of sovereign creditworthiness and the normalisation of relations with international creditors," says Paul Rawkins, Senior Director in Fitch's London-based Sovereign Rating Group.

Fitch now expects the Icesave dispute to be referred to the EFTA Surveillance Authority (ESA) and, in all likelihood, the EFTA court. Fitch understands that these proceedings could take up to 18 months. The immediate impact on Iceland's IMF programme is likely to be limited: the programme remains on track and encouraging progress has been made with fiscal consolidation. However, the fifth review of the programme (scheduled to take place on 27 April 2011) may be delayed, pending a reassessment of the underlying macroeconomic assumptions following the Icesave decision and its likely impact on investment and growth. Some uncertainty also surrounds Nordic countries' bilateral funding of the programme, although this has not been explicitly linked to resolution of the Icesave dispute.

Fitch says this latest setback could potentially lead to further delays in the relaxation of capital controls (that continue to trap significant non-resident investments in Icelandic krona) and the establishment of a credible market-determined exchange rate necessary to restore the economy's access to international capital over the medium term. More limited foreign direct investment could slow economic recovery, while the sovereign's access to international capital markets at affordable rates of interest is likely to be constrained. That said, however, Fitch does not consider sovereign debt service to be at immediate risk. International reserves now stand at close to USD6bn, significantly in excess of sovereign foreign currency maturities of around EUR900m in 2011-12.

Fitch notes that while the Icesave dispute has tended to dominate the credit outlook on Iceland in recent months, it is important not to overlook broader macroeconomic improvements. The economy is expected to grow by 2% in 2011, headline inflation is close to the central bank's target of 2.5%, allowing a decline in interest rates to low single digits, and the trade balance has moved into strong surplus. Admittedly, downside risks remain, most notably the weight of private sector debt restructuring, but incipient signs of recovery should help to ameliorate the negative implications of Icesave over time.

### Contact:

Paul Rawkins  
Senior Director  
+44 (0) 20 3530 1046  
Fitch Ratings Limited  
30 North Colonnade  
London, E14 5GN

Maria Malas-Mroueh  
Director  
+44 (0) 20 3530 1081

Media Relations: Peter Fitzpatrick, London, Tel: +44 20 3530 1103, Email: peter.fitzpatrick@fitchratings.com.

Additional information is available at [www.fitchratings.com](http://www.fitchratings.com)

Applicable criteria, "Sovereign Rating Methodology", dated 13 August 2010, are available on [www.fitchratings.com](http://www.fitchratings.com).

Applicable Criteria and Related Research:

Sovereign Rating Methodology

[http://www.fitchratings.com/creditdesk/reports/report\\_frame.cfm?rpt\\_id=547765](http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=547765)

ALL FITCH CREDIT RATINGS ARE SUBJECT TO CERTAIN LIMITATIONS AND DISCLAIMERS. PLEASE READ THESE LIMITATIONS AND DISCLAIMERS BY FOLLOWING THIS LINK: [HTTP://FITCHRATINGS.COM/UNDERSTANDINGCREDITRATINGS](http://FITCHRATINGS.COM/UNDERSTANDINGCREDITRATINGS). IN ADDITION, RATING DEFINITIONS AND THE TERMS OF USE OF SUCH RATINGS ARE AVAILABLE ON THE AGENCY'S PUBLIC WEBSITE '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.