

# Economic and monetary chronicle

## April 2008

On April 7, the Minister of Social Affairs issued a regulation raising rent subsidy allowances effective April 1, as an element in the Government's pledges related to the contractual wage agreements signed on February 17.

On April 10, the Board of Governors of the Central Bank of Iceland decided to raise the Bank's policy interest rate by 0.5 percentage points, to 15.5%.

On April 17, the third auction of RIKB 19 0226 was held. Offers were accepted for 2.9 b.kr. nominal value at an average yield of 10.64%.

On April 17, Standard & Poor's Rating Services lowered its foreign- and local-currency sovereign credit ratings on the Republic of Iceland to A and AA-, from A+ and AA, respectively. The ratings for short-term local-currency obligations (A-1+) and short-term foreign currency obligations (A-1) were affirmed. The outlook for the long-term sovereign ratings remains negative.

On April 21, Standard & Poor's lowered the long-term credit rating for Glitnir from A- to BBB+. The rating for short-term obligations was affirmed at A-2. The outlook for long-term obligations is negative.

## May 2008

On May 9, Fitch Ratings lowered its credit ratings for Kaupthing and Glitnir. The banks' ratings for long- and short-term obligations were lowered from A to A-, and from F1 to F2, respectively. The banks' individual ratings of B/C and their support ratings of 2 were unchanged. The outlook for long-term obligations is negative.

On May 13, securities lending facilities to each primary dealer in series RIKB 08 1212 and RIKB 09 0612 were increased from 5 b.kr. to 7 b.kr. nominal value in response to demand for short-term nominal Treasury notes.

On May 15, Parliament passed a law abrogating the taxation of businesses' capital gains on the sale of equity securities and transferred the administration of tax matters for large corporations to the Regional Tax Director in the Reykjavík district. Previously, it was possible to defer the payment of taxes by reinvesting in other equities within two years.

On May 16, the Central Bank announced the conclusion of bilateral currency swap agreements with the central banks of Norway, Sweden, and Denmark. The agreements are a contingency measure, and the Central Bank can draw on them at need. Each of the agreements provides access to a maximum of 500 million euros.

On May 20, Moody's Investor Service lowered the Republic of Iceland's sovereign credit rating by one notch, from Aaa to Aa1. The country ceiling for bank deposits in foreign currency was also down-

graded from Aaa to Aa1. The outlook for the sovereign credit ratings was changed from negative to stable.

On May 22, the Board of Governors of the Central Bank of Iceland decided to hold the Bank's policy interest rate unchanged at 15.5%.

On May 23, new agreements were signed by the Central Bank of Iceland in connection with the issue of Government securities and market making in the secondary market. The objectives of the agreements are to maintain the Treasury's access to loan financing and to enhance price formation in the secondary market for Government securities. The agreements were concluded with seven financial institutions and remain valid for one year.

On May 27, a special auction of short-term Treasury notes was held. The series offered was RIKB 08 1212. Offers were accepted for 15 b.kr. nominal value at an average yield of 12.45%.

On May 28, Parliament approved an amendment to the Act on Electronic Registration of Title to Securities, stipulating that settlement instructions for electronic securities denominated in foreign currencies and held in a domestic securities depository shall take place through the intermediation of a securities depository that fulfils requirements comparable to those set forth in the Act on the Security of Transfer Orders in Payment Systems. The settlement system shall have ready access to the foreign currency in question.

On May 29, the fourth auction of RIKB 19 0226 was held. Offers were accepted for 6.5 b.kr. nominal value at an average yield of 9.55%.

On May 29, Parliament passed an act of law abolishing the stamp fee on a purchaser's first apartment.

On May 30, Parliament approved amendments to the Income Tax Act in accordance with Government pledges related to the signing of the private sector wage settlements in February 2008. The amendments involve raising the personal tax credit, raising the income threshold for child subsidy allowances, reducing the income-linkage of child benefits, raising the asset threshold for mortgage interest allowances, and reducing the corporate income tax rate. In addition, the exchange rate differential for legal entities' operations can be distributed over three years.

#### **June 2008**

On June 4, the Central Bank of Iceland issued new Rules on Foreign Exchange Balance, which took effect on July 1, superseding the previous Rules no. 318/2006. The principal change is that the maximum mismatch between foreign-denominated assets and liabilities has been reduced from 30% to 10%. However, financial undertakings can apply for authorization to maintain a separate positive foreign exchange balance in order to hedge against the effects of adverse exchange rate movements on their equity ratio.

On June 19, the Government approved special measures related to the housing market and the arrangements for Housing Financing Fund

(HFF) loans. The ceiling was raised from 18 m.kr. to 20 m.kr., with the maximum loan amount set at 80% of the purchase price of the property instead of the fire insurance value, as it was previously. Furthermore, two new bond series were established for the purpose of financing mortgages granted by financial institutions.

On June 19, the Government announced a supplementary issue of Treasury notes in series, RIKB 08 1212, RIKB 09 0612, and RIKB 10 0317, which will be issued on the domestic market for a total of 75 b.kr.

On June 19, the Board of Governors of the Central Bank of Iceland decided that its certificates of deposit (SI 08 0924) will be reissued upon the maturity of the CDs issued in March. The current CD issue matures in September 2008. Decisions concerning the issuance of certificates of deposit next year will be made in view of market conditions at that time.

On June 23, the Housing Financing Fund (HFF) decided, following the June 20 auction of HFF housing bonds, to lower the Fund's lending rates by 0.15 percentage points. HFF bonds with a prepayment clause now bear 5.05% interest, and bonds without a prepayment clause bear 5.55% interest.

On June 27, Kaupthing held an auction of covered bonds. The issue is intended to finance the bank's mortgage loans to individuals, and offers were accepted for 4.8 b.kr. nominal value. The weighted average yield in the auction was 5.17%, and the bank's lending rates will be based on that yield plus a premium of 0.9%. The bank's lending rates will therefore fall from 6.4% to 6.05% following of the auction.

