Iceland

Full Rating Report

Ratings

Foreign Currency

Long-Term IDR	BBB
Short-Term IDR	F3

Local Currency

Long-Term IDR	BBB+
Country Ceiling	BBB

Outlooks

Foreign-Currency Long-Term IDR	Stable
Local-Currency Long-Term IDR	Stable

Financial Data

Iceland

(USDbn)	2013
GDP	14.2
GDP per head (USD 000)	44.1
Population (m)	0.3
International reserves	4.5
Net external debt (% GDP)	503.4
Central government total debt (% GDP)	84.7
CG foreign-currency debt	3.5
CG domestically issued debt (ISKbn)	-

Related Research

Global Economic Outlook (September 2013)

Analysts

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Key Rating Drivers

Strong Wealth, Social Indicators: Iceland's rating is underpinned by high income per capita and by measures of governance, human development, and ease of doing business more akin to those of 'AAA' rated countries.

Economic Growth Steady: Economic growth has remained consistent during debt restructuring in both the household and corporate sectors. Fitch Ratings expects GDP growth to be 1.9% in 2013 before accelerating to an average 2.5% over the next two years.

Public Finances a Credit Weakness: There has been fiscal slippage in 2013. The general government deficit reached 1.3% of GDP in the second quarter. Fitch estimates the deficit for the full year will be 3.0% of GDP. Gross government debt was 99.5% in 2012. The government has signalled its intention to introduce further household debt relief, but would be likely to seek to protect the sovereign balance sheet due to its stated commitment to fiscal consolidation.

Budget Proposal Addresses Slippage: The new government has taken steps to address the slippage through a package of spending and revenue measures worth around ISK30bn (1.5% of GDP). Fitch expects large primary surpluses to drive the government debt to GDP ratio below 90% by 2015.

External Finances a Credit Weakness: The legacy of the financial crisis and the winding-up of the old banks will weigh on the country's external position and the balance of payments in the near future. In 2012 the country's net external debt (including the estates of the old banks) was more than 5x the size of the economy.

Capital Controls Remain: A substantial amount of non-residents' claims are "locked in" krona assets. The authorities are not committed to a precise date for the removal of capital controls, and appear committed to avoiding a disorderly unwinding. Fitch expects this factor to continue to weigh on Iceland's fundamental economic and financial stability at least until 2015, as well as on the credit profile.

Rating Sensitivities

Fiscal Policy Reversals: A weakening commitment to fiscal consolidation – eg through further household debt relief affecting the sovereign balance sheet – resulting in slower-than-expected government debt ratio reduction would be rating negative.

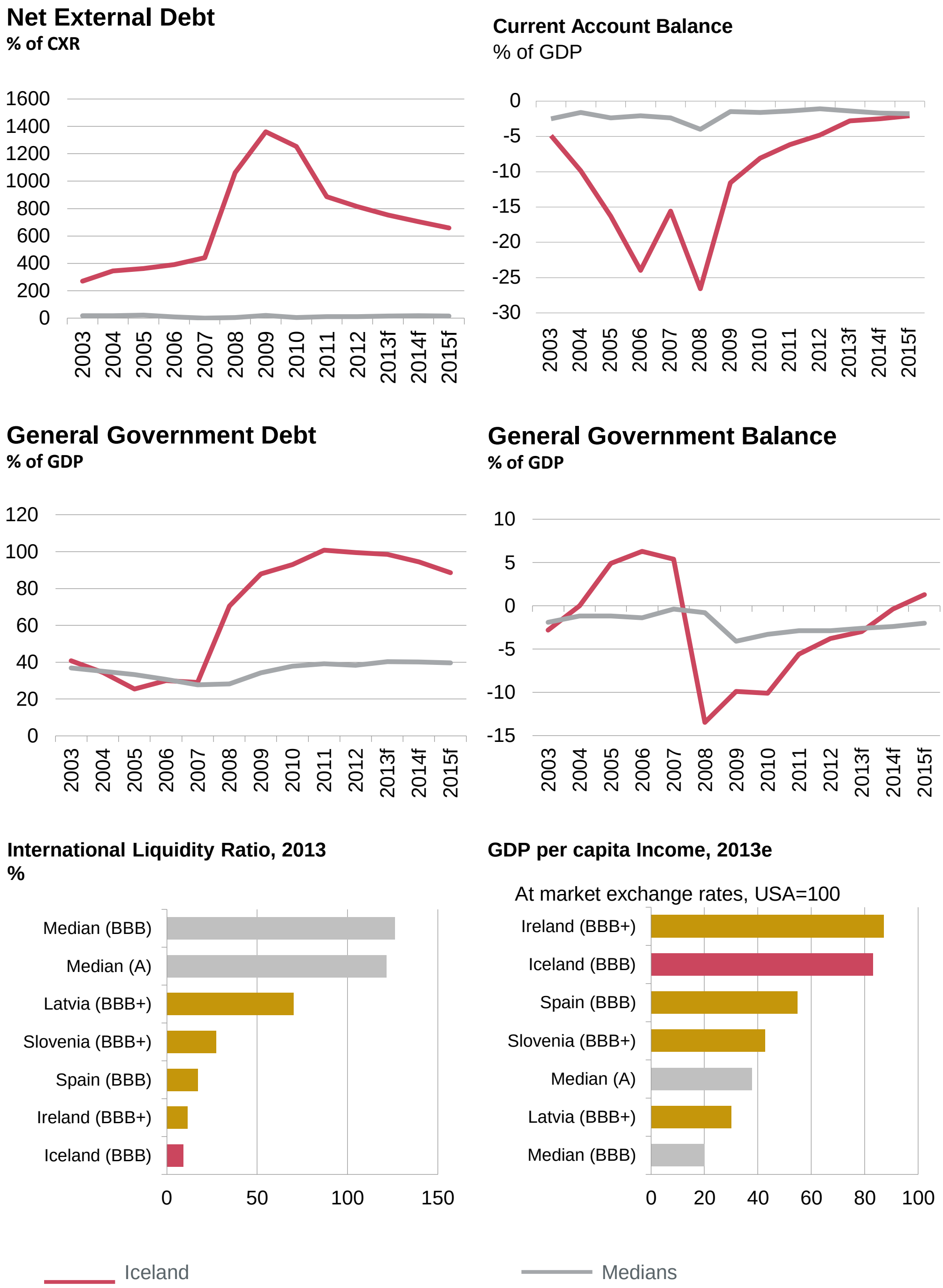
Growth Slowdown: A substantially weaker-than-expected economic performance, resulting in trend growth falling significantly below Fitch's assumptions, would be a rating negative.

Contingent Liabilities: A crystallisation of contingent liabilities from the financial sector, and especially the Housing Finance Fund (HFF), over and above the amounts already assumed in Fitch's debt sensitivity analysis, would be a rating negative.

Debt Declines and Restructuring: Continued reductions in external and public debt ratios would be rating positives. Evidence of continued and successful debt restructuring in the private sector would be also be a rating positive.

Monetary Stability, Capital Controls: Enduring monetary and exchange-rate stability in the context of continued steady economic growth would be a rating positive. Greater clarity about the evolution of the process for lifting capital controls would be a rating positive.

Peer Comparison



Related Criteria

Sovereign Rating Criteria (August 2012)

Peer Group

Rating	Country
BBB+	Ireland
	Italy
	Kazakhstan
	Latvia
	Lithuania
	Mexico
	San Marino
	Slovenia
	Thailand
BBB	**Iceland**
	Aruba
	Bahrain
	Brazil
	Panama
	Peru
	Russia
	South Africa
	Spain
BBB−	Azerbaijan
	Bulgaria
	Colombia
	India
	Indonesia
	Morocco
	Namibia
	Philippines
	Romania
	Turkey
	Uruguay

Rating History

Date	Long-Term Foreign Currency	Long-Term Local Currency
14 Feb 13	BBB	BBB+
17 Feb 12	BBB−	BBB+
05 Jan 10	BB+	BBB+
08 Oct 08	BBB−	A−
30 Sep 08	A−	AA
15 Mar 07	A+	AA+
03 Feb 00	AA−	AAA

Rating Factors

Summary: Strengths and Weaknesses

Rating factor	Macroeconomic	Public finances	External finances	Structural issues
Status	Neutral	Weakness	Weakness	Strength
Trend	Stable	Positive	Stable	Stable

Note: Relative to 'BBB' category
Source: Fitch

Strengths

- Iceland has high income per capita and measures of governance, human development, and ease of doing business that are like those of 'AAA' rated countries. Its relative standing according to these indicators has not been affected by the financial crisis.
- Iceland's relatively high income per head is indicative of a greater level of debt tolerance than rating peers with lower income levels. Its robust private pension assets and wide tax base also support the rating.
- There is a strong political consensus regarding the long-term objective of reducing the public debt to GDP ratio from its post-crisis peak of over 100% to 60%. The new government's budget proposals aimed at addressing this year's fiscal slippage underline the commitment to fiscal consolidation.
- Having regained market access in mid-2011, the sovereign has continued to regularly issue securities, and has managed to increase the average maturity of its debt.

Weaknesses

- Despite some reduction of public debt, the public finances remain a weakness. Gross government debt was 99.5% in 2012, much higher than the 'BBB' median.
- Extensive capital controls remain, leading to around EUR2bn of non-resident krona-denominated assets being "locked in" the country.
- The legacy of the financial crisis in 2008-2009 will weigh on the country's external position and the balance of payments in the near future. Iceland is a stand-out on measures of external debt, pending the resolution of the winding-up of the estates of the old banks. In 2012, the country's net external debt (including the old bank estates) was more than 5x the size of the economy.
- External debt repayments in the private sector could create balance-of-payments tensions in the near future. However, the public sector's scheduled foreign loan repayments are small compared with the stock of foreign exchange reserves.

Local Currency Rating

The one-notch difference between the Long-Term Foreign- (BBB) and Local-Currency IDRs (BBB+) reflects the comparative sophistication and depth of the domestic financial market.

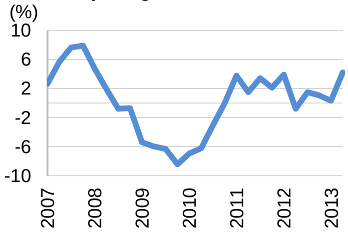
Country Ceiling

The Country Ceiling is aligned with the sovereign's Long-Term Foreign Currency IDR, reflecting the imposition of capital controls since 2008, which ring-fenced sovereign debt service but trapped a substantial amount of non-resident assets in local-currency debt instruments.

Figure 1

Real GDP Growth

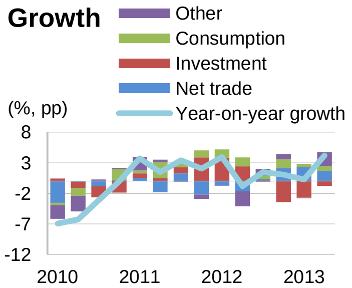
Year-on-year growth



Source: Statistics Iceland

Figure 2

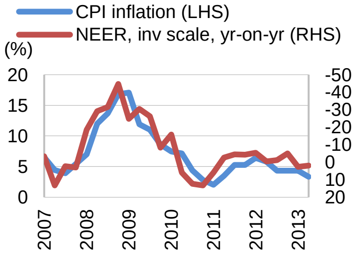
Contributions to GDP Growth



Source: Statistics Iceland

Figure 3

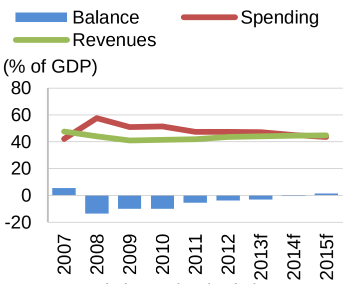
Inflation and the Exchange Rate



Source: Datastream

Figure 4

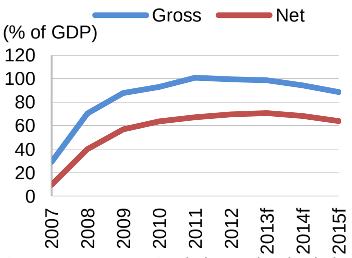
Government Finances



Source: Statistics Iceland, Fitch

Figure 5

Gross and Net General Government Debt



Source: Eurostat, Statistics Iceland, Fitch

Key Credit Developments

Recent Macroeconomic Developments

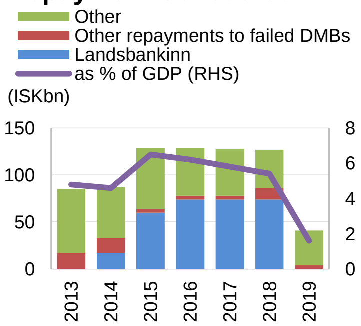
- Economic growth remained steady in H113 while debt restructuring has been taking place in the household and corporate sectors. In H113 real GDP was 2.2% higher than in the same period a year ago, with weak investment offset by net trade and domestic demand.
- Annual growth of both private and government consumption was just over 1% in H113, while whole economy investment fell sharply, driven by a drop of almost 20% in real business investment. Net trade contributed positively to growth in the half, thanks to falling imports and strong growth in exports of services (due to strong tourist inflows).
- Fitch expects real GDP growth of 1.9% for the year as a whole, up from (a revised down) 1.4% in 2012. The agency forecasts private consumption to rise in line with GDP. Investment is set to fall sharply this year. Net trade will continue to support growth.
- Fitch expects GDP growth to pick up in 2014 and 2015, to 2.4% and 2.6%, respectively. The agency also expects business investment to rebound strongly in 2014, and private consumption to grow broadly in line with GDP. It also forecasts net exports to rise over the next two years, in conjunction with the improved economic prospects in Iceland's main trading partners.
- Inflation edged down in H113, but remains well above the CBI 2.5% target (4.2% in August). Fitch expect inflation to average 3.8% in 2013, before falling towards 3% over the next two years, under the assumption that the CBI will maintain a comparatively tight monetary policy over the projections horizon, and that there will be only a moderate depreciation of the nominal exchange rate (of 2% a year).

Some Fiscal Slippage This Year – Draft Budget to Tighten Policy in 2014

- There has been a degree of fiscal slippage in 2013. The previous government had indicated a target of 1.3% of GDP for the overall deficit in 2013, and a balanced budget for 2014. The most recent outturns indicate that the government deficit had already reached 1.3% of GDP by Q213. Fitch assumes the deficit will be 3.0% of GDP for 2013 as a whole.
- The new government announced its first draft budget on 1 October, and addressed this slippage through a package of spending and revenue measures worth around ISK30bn (about 1.5% of GDP) for 2014. Fitch projects, on the basis of the budget proposal, that the deficit will fall substantially in 2014, to 0.4% of GDP. The government expects a surplus of 1.3% in 2015. Iceland had already achieved a primary balance in 2012, and the government expects a primary balance of 2.2% of GDP in 2013. It also forecasts large primary surpluses in 2014 and 2015.
- Fitch estimates general government gross debt to have peaked at just below 101% of GDP in 2011, and to have been 99.5% of GDP in 2012. The forecast primary surpluses would drive the debt ratio below 90% by 2015. The sovereign remains highly liquid, with central government deposits at the central bank equivalent to around 30% of GDP. This implies that net public debt is around 70% of GDP.
- As in its February rating review, Fitch's projections for government debt assume a stock-flow adjustment of ISK13bn (around 0.7% of GDP) in 2013, reflecting the government's recapitalisation of the HFF. After discussions with the Icelandic authorities, Fitch now assumes that there will be further equity injections by the government in subsequent years, averaging ISK4.5bn a year (around 0.2% of GDP).

Figure 6

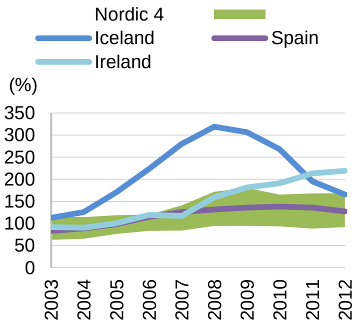
Private Sector Debt Repayment Schedules



Source: Fitch

Figure 7

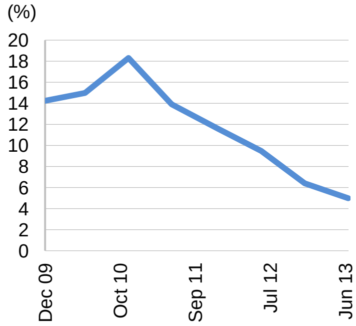
Corporate Debt to GDP Ratio



Source: CBI, Eurostat

Figure 8

Default Ratios of Commercial Banks



Source: CBI, FME

Capital Controls and External Finances

- Capital controls remain in place. This implies that a substantial amount of non-resident claims – estimated by the CBI to be around ISK341bn (EUR2bn, or 20% of GDP) – are "locked in" krona assets. Currency auctions by the central bank designed to swap krona securities into long-term investments have reduced the stock of "locked-in" assets.
- There are indications that the presence of capital controls has an unfavourable impact on business conditions. But a premature and disorderly unwinding of them would lead to substantial capital outflows, exchange rate depreciation, increased inflation and potential stress in the financial sector. The Icelandic authorities recognise the risks, and the new government has emphasised that the removal should be state contingent, rather than constrained by a precise timetable.
- The legacy of the financial crisis and the winding-up of the estates of the old banks weigh on Iceland's external position. Despite the positive outlook for net trade, Fitch expects current account deficits – albeit smaller than in the recent past – until 2015. In 2012 external debt was 750% of GDP, while the net international investment position was around −470% of GDP. Estimates from the CBI suggest that in the absence of the old banks' estates the NIIP would be around −30% of GDP.
- Recent estimates by the CBI indicate that although around 35% of the estates' assets are domestic, 95% of underlying claims are foreign. The difference between foreign creditors' share of the value of domestic assets and those of domestic creditors will create an external liability (CBI estimates point to around ISK800bn, or 45% of GDP).
- The winding-up of the old banks' estates may also result in private sector flows with the potential to create tensions in the country's external position, at least in the private sector. At the time of the restructuring of the financial sector, the new Landsbanki issued bonds to the old banks in lieu of assets taken on to their balance sheets from the latter. Repayments on these bonds will rise from 2015 – there is a risk that these will require rescheduling.

Private Sector Debt Restructuring and the Banking Sector

- Household and corporate indebtedness are still high by international standards, even though debt ratios for households and corporates have fallen from the post-crisis peaks. The ongoing debt restructuring in the corporate sector may be holding back investment, and explain the relative weakness of business investment (see above).
- Default ratios for the three largest commercial banks have fallen from a peak of 18% to 6% at end-2012. Household debt is set to fall further, thanks also to the impact of the recent Supreme Court ruling on the legality of exchange rate-linked loans. But despite the decline in default rates among households, household debt remains high, and the actual number of individuals on the default register is at an all-time high.
- The Icelandic commercial banks have further strengthened their capital buffers, and the capital adequacy ratio of the three main commercial banks reached almost 25% in 2012.
- The HFF faces major difficulties. These result from increased prepayments and prepayment risk; an insufficient interest margin; and high defaults. At end-2012 the HFF's equity was less than 2% of its assets. The sovereign has already intervened to strengthen the HFF's equity position and this is reflected in Fitch's debt sustainability analysis.

Forecast Summary

	2009	2010	2011	2012	2013f	2014f	2015f
Macroeconomic indicators and policy							
Real GDP growth (%)	-6.6	-4.1	2.9	1.6	1.9	2.4	2.6
Unemployment (%)	7.3	8.1	7.5	5.8	5.2	4.3	4.2
Consumer prices (annual average % change)	16.3	7.5	4.2	6.0	3.8	3.1	3.0
Short-term interest rate (%)[a]	13.7	7.8	4.4	5.4	6.0	6.0	6.0
General government balance (% of GDP)	-9.9	-10.1	-5.6	-3.8	-3.0	-0.4	1.3
General government debt (% of GDP)	87.9	93.0	100.9	99.5	98.6	94.4	88.6
ISK per USD (annual average)	123.6	122.2	116.0	125.1	125.5	123.2	125.7
Real effective exchange rate (2000 = 100)	71.4	75.0	76.0	75.7	70.9	72.3	73.7
External finance							
Current account balance (USDbn)	-1.4	-1.0	-0.9	-0.7	-0.4	-0.4	-0.3
Current account balance (% of GDP)	-11.6	-8.1	-6.2	-4.8	-2.8	-2.5	-2.1
Current account balance plus net FDI (% of GDP)	-29.8	13.7	1.5	24.0	8.6	8.7	9.3
Net external debt (USDbn)	97.5	95.1	84.8	71.9	71.5	71.0	70.4
Net external debt (% of GDP)	804.8	757.2	603.9	529.4	503.4	467.0	449.1
Net external debt (% of CXR)	1,361.4	1,254.2	887.0	815.1	753.1	705.2	659.0
Official international reserves including gold (USDbn)	3.9	5.8	8.6	4.2	4.5	4.9	5.4
Official international reserves (months of CXP cover)	5.4	8.1	9.8	5.3	5.4	5.7	5.9
External interest service (% of CXR)	52.0	38.4	32.4	24.5	21.5	20.5	17.2
Gross external financing requirement (% int. reserves)	512.4	436.3	290.7	96.8	83.1	63.1	128.4
Memo: Global forecast summary							
Real GDP growth (%)							
US	-2.8	2.5	1.9	2.8	1.6	2.6	3.0
Japan	-5.5	4.7	-0.6	2.0	1.8	1.5	1.2
Euro area	-4.4	2.0	1.6	-0.7	-0.4	0.9	1.3
World	-2.2	3.9	3.2	2.6	2.3	2.9	3.2
Commodities							
Oil (USD/barrel)	61.9	79.6	111.0	112.0	105.0	100.0	100.0

[a] Central Bank of Iceland seven-day collateralised lending rate
Source: Fitch

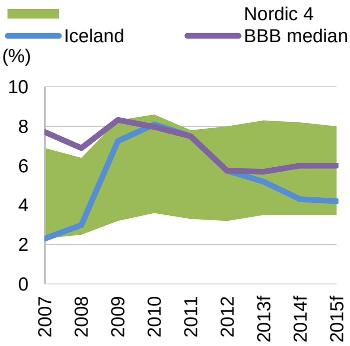
Comparative Analysis: Macroeconomic Performance and Policies

Iceland

	2013						
	Ireland BBB+	Latvia BBB+	Slovenia BBB+	Iceland BBB	Spain BBB	BBB median	A median
Real GDP (5yr average % change)	-1.0	-0.7	-2.1	-0.8	-1.4	2.9	2.6
Volatility of GDP (10yr rolling SD)	4.1	8.8	4.3	4.7	2.7	3.0	2.5
Consumer prices (5yr average)	0.2	1.9	2.7	7.6	1.8	3.8	2.3
Volatility of CPI (10yr rolling SD)	1.7	4.7	1.5	4.7	1.2	1.8	1.5
Years since double-digit inflation	30.0	5.0	17.0	4.0	29.0	n.a.	n.a.
Unemployment rate	14.5	13.5	11.0	5.2	27.0	6.9	6.6
Type of exchange rate regime	EMU	Peg	EMU	Managed float	EMU	n.a.	n.a.
Dollarisation ratio	-	-	-	-	-	-	-
REER volatility (10yr rolling SD)	7.2	11.1	2.8	10.9	3.9	5.0	5.0

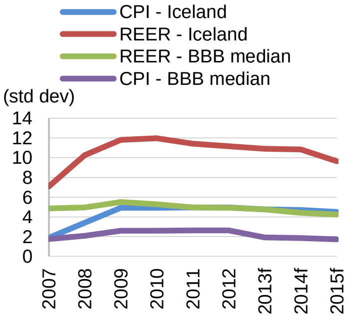
Source: Fitch

Figure 9
Unemployment Rate



Source: Fitch

Figure 10
Exchange Rate and Inflation Volatility



Source: Fitch

Strengths

- The first country to suffer the full force of the global financial crisis, Iceland has achieved renewed access to international capital markets.
- Flexible labour and product markets have already ensured a substantial degree of economic adjustment to the shock brought about by the global financial crisis. Unemployment has already fallen from a post-crisis high of 8.1% in 2010, and Fitch expects it to average 5.2% in 2013. This is substantially lower than for rating peers, and relatively low compared with other Nordic countries.
- Economic growth remained steady in H113 during debt restructuring by the household and corporate sectors. Real GDP growth prospects for the year are markedly more positive than those of rating peers such as Ireland and Spain.

Weaknesses

- Iceland is a stand-out among rating peers on measures of inflation and exchange rate volatility. Inflation expectations are anchored at a high level, and there is a very high degree of pass-through from changes in the exchange rate to inflation.
- The severe macroeconomic imbalances that built up in 2004-2007 – mounting corporate and household debt, soaring private consumption, rising real estate prices, an unsustainable current account deficit – are taking time to unwind, constraining the recovery, especially of investment prospects.
- As a very small, open economy, weakened by the collapse of its banking system and a subsequent sharp rise in public and external debt, Iceland is vulnerable to external shocks.

Comparative Analysis: Structural Features

Iceland

	2013						
	Ireland BBB+	Latvia BBB+	Slovenia BBB+	Iceland BBB	Spain BBB	BBB median	A median
GNI per capita PPP (USD, latest)	35,110	21,020	26,470	33,550	31,780	15,480	23,580
GDP per capita (USD, mkt exchange rates)	46,287	14,817	22,617	44,064	29,122	10,739	18,318
Human development index (percentile, latest)	96.2	76.8	88.7	93.0	88.1	65.6	82.0
Ease of doing business (percentile, latest)	92.4	87.0	81.6	93.0	76.7	66.1	79.9
Trade openness (CXR and CXP % GDP)	144.0	71.1	79.4	68.2	41.3	44.5	78.5
Gross domestic savings (% GDP)	35.0	23.1	22.6	20.2	21.2	21.9	26.8
Gross national savings (% GNP)	16.7	25.3	19.8	10.8	20.5	22.0	22.2
Gross domestic investment (% GDP)	9.2	26.6	17.9	12.5	18.9	22.7	21.8
Private credit (% GDP)	181.8	60.7	81.2	92.3	170.7	59.0	106.2
BSR indicators	b/2	b/1	ccc/1	n.a./1	bb/2	n.a.	n.a.
Bank system CAR[a]	10.1	17.7	11.9	24.7	11.5	14.5	12.6
Foreign bank ownership (% assets)[a]	63	71	42	43.1	8	25.3	6.7
Public bank ownership (% assets)[a]	7	17.5	22.8	36.4	16.5	18.3	49.4
Default record (year cured)[b]	-	-	1996	-	-	n.a.	n.a.

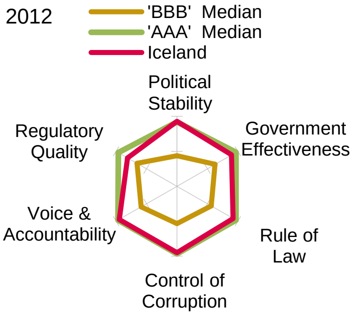
[a] 2012 data for except for Ireland (2011)
[b] Former Yugoslavia: 1984, 1985, 1986, 1988 (official creditors); 1983, 1984, 1985, 1998 (commercial banks). Debt agreements related to Slovenia's secession: 1995

Source: Fitch and World Bank

Figure 11

Governance Indicators

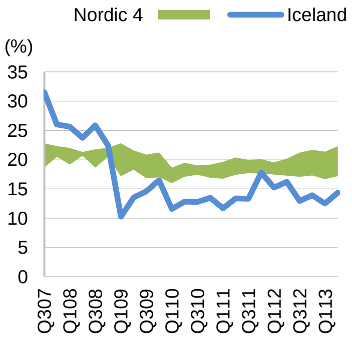
2012



Source: World Bank

Figure 12

Investment/GDP Ratio



Source: Datastream

Strengths

- On measures of governance, human development and ease of doing business, Iceland is far superior to 'BBB' medians, and is very similar to 'AAA' countries.
- Iceland's income per capita is a clear stand-out in the 'BBB' range; whether measured at market prices or on a purchasing power parity basis, it is closer to the 'AAA' median.
- Iceland's rich natural resource endowment – marine products and abundant renewable energy resources – coupled with a relatively young population and robust private pension assets support the rating.

Weaknesses

- There are indications that the continued presence of capital controls has an unfavourable impact on business conditions. Investment as a share of GDP in Iceland has remained below that of other Nordic countries since the financial crisis. Low investment could adversely affect the economy's supply side and growth potential.
- Despite the progress in debt restructuring, high private sector debt poses a risk to financial stability and economic recovery. Banks' capacity for new lending remains limited.

Comparative Analysis: External Finances

Iceland

	2013					Last 10 years	
	Ireland BBB+	Latvia BBB+	Slovenia BBB+	Iceland BBB	Spain BBB	BBB median	A median
GXD (% CXR)	219.8	205.9	135.9	1,088.6	422.2	106.9	83.0
GXD (% GDP)	321.1	144.9	111.4	727.7	176.8	48.3	48.8
NXD (% CXR)	55.0	64.2	44.0	753.1	200.0	11.3	-23.4
NXD (% GDP)	80.3	45.2	36.1	503.4	83.8	3.9	-16.4
GSXD (% GXD)	42.4	22.3	35.9	6.2	36.7	30.5	20.1
NSXD (% CXR)	84.5	8.5	24.7	20.2	124.3	-9.2	-23.1
NSXD (% GDP)	123.5	6.0	20.3	13.5	52.1	-5.0	-16.2
SNFA (USDbn)	-258.8	-1.8	-9.5	-1.9	-710.0	3.6	8.2
SNFA (% GDP)	-121.0	-6.0	-20.3	-13.4	-53.7	5.1	15.6
Ext. debt service ratio (% CXR)	25.1	30.1	16.1	54.0	57.7	15.5	10.0
Ext. interest service ratio (% CXR)	5.5	6.1	3.9	21.5	11.0	4.2	2.1
Liquidity ratio (latest)	11.6	70.3	27.2	9.2	17.2	135.9	128.2
Current account balance (% GDP)	4.2	-1.6	4.0	-2.8	1.2	-1.8	1.6
CAB plus net FDI (% GDP)	9.0	-0.2	4.9	8.6	2.2	0.7	3.1
Commodity dependence (% CXR, latest)	5.4	27.4	12.9	48.1	15.6	27.6	12.6
Sovereign net FX debt (% GDP)	-0.8	32.2	-1.5	-7.2	-3.4	-7.4	-12.6

Source: Fitch

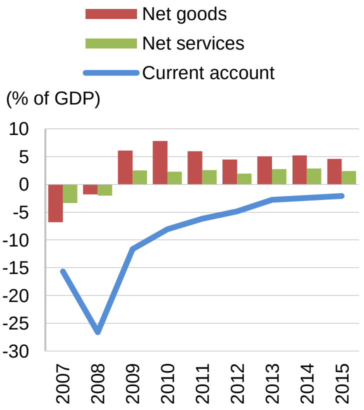
Strengths

- The current account deficit has narrowed sharply since the financial crisis – from 26.6% of GDP in 2008 to 4.8% of GDP in 2012. Fitch expects a further fall in deficit in 2013 driven by strong net exports, to 2.8% of GDP. The agency also forecasts the current account to strengthen further over the forecast horizon, but a deficit of around 2% is still likely in 2015.
- International reserves were bolstered by IMF and associated bilateral funding and renewed access to international capital markets. However, reserves declined to USD4bn (5.3 months of current external payments at end-2012) as Iceland prepaid loans to IMF and the Nordic countries.

Weaknesses

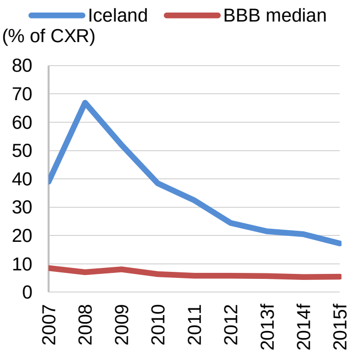
- External finances are a credit weakness. The legacy of the financial crisis and the winding-up of the estates of the old banks weighs on the external position. In 2012 net external debt in 2012 (including the old banks' estates) was 5x larger than the economy – a clear stand-out among rating peers. Despite the positive outlook for net trade, Fitch expects current account deficits until 2015, although they are likely to be smaller than in the recent past.
- Commodity dependence is much higher than the 'BBB' median, reflecting Iceland's narrow export base.

Figure 13
Net Trade and Current Account



Source: Fitch

Figure 14
External Debt Service



Source: Fitch

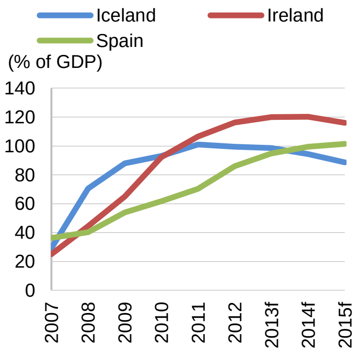
Comparative Analysis: Public Finances

Iceland

	2013					Last 10 years	
	Ireland BBB+	Latvia BBB+	Slovenia BBB+	Iceland BBB	Spain BBB	BBB median	A median
Budget balance (% GDP)	-7.5	-1.4	-5.4	-3.0	-6.8	-2.6	-2.0
Primary balance (% GDP)	-2.6	0.0	-2.6	2.2	-3.4	-0.2	-0.3
Revenues and grants (% GDP)	35.8	36.0	43.9	44.0	37.5	32.8	33.6
Volatility of revenues/GDP ratio	3.0	2.8	2.1	5.8	5.2	5.8	6.7
Interest payments (% revenue)	14.0	4.0	6.3	12.0	9.0	6.8	4.7
Debt (% revenue)	335.6	118.4	156.0	224.0	252.6	127.1	146.1
Debt (% GDP)	120.0	42.6	68.5	98.6	94.7	36.8	39.1
Net debt (% GDP)	104.3	35.2	56.2	70.8	89.8	30.2	30.6
FC debt (% total debt)	0.0	75.8	1.0	24.7	0.3	34.9	18.2
CG debt maturities (% GDP)	8.3	7.3	5.3	17.3	12.6	5.5	5.2
Average duration of CG debt (years)[a]	5.8	3.5	5.0	4.8	4.4	5.3	3.8

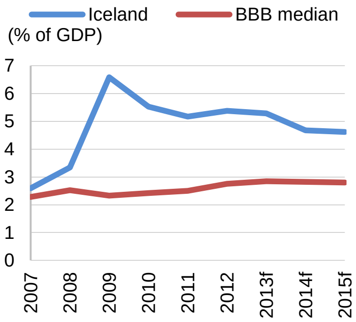
[a] 2009 data for Ireland, 2012 data for Slovenia, 2011 data for the other countries
Source: Fitch

Figure 15
General Government Debt



Source: Fitch

Figure 16
Interest Payments on Public Debt



Source: Fitch

Strengths

- The new government has taken steps to address this year's fiscal slippage through a package of spending and revenue measures worth around ISK30bn (around 1.5% of GDP) for 2014. This reinforces Fitch's view that a strong cross-party consensus exists on the need for fiscal consolidation. This is also confirmed by the government's intention to introduce a fiscal responsibility law.
- The revenue to GDP ratio is markedly superior to that of rating peers, reflecting a wealthy economy with a broad and sophisticated tax base.
- Iceland has a well-developed government debt market relative to peers that benefits from regular auctions and a clear medium-term financing strategy.

Weaknesses

- Despite the recent progress in fiscal consolidation, both gross and net government debt are well above the rating peer group median.
- Public debt service is therefore high relative to rating peers and vulnerable to exchange-rate fluctuations, reflecting a high proportion of foreign currency-denominated debt (around 28% according to latest estimates).
- Capital controls have denied non-resident investors in krona-denominated government instruments unfettered access to principal (but not interest) since 2008.

Figure 17
Fiscal Accounts Summary

(% of GDP)	2010	2011	2012	2013f	2014f	2015f
General government						
Revenue	**41.5**	**41.8**	**43.6**	**44.0**	**44.6**	**44.8**
Expenditure	**51.6**	**47.4**	**47.4**	**47.1**	**45.0**	**43.5**
O/w interest payments	5.5	5.2	5.4	5.3	4.7	4.6
Primary balance	-4.5	-0.4	1.5	2.2	4.3	5.9
Overall balance	**-10.1**	**-5.6**	**-3.8**	**-3.0**	**-0.4**	**1.3**
General government debt	**93.0**	**100.9**	**99.5**	**98.6**	**94.4**	**88.6**
% of general government revenue	224.1	241.3	228.3	224.0	211.5	197.7
General government deposits	29.2	33.8	30.0	27.8	26.2	24.7
Net general government debt	63.7	67.2	69.5	70.8	68.1	63.9
Central government						
Revenue	**30.6**	**30.4**	**31.6**	**32.0**	**32.4**	**32.6**
O/w grants	0.5	0.6	0.6	0.6	0.5	0.5
Expenditure and net lending	**40.0**	**36.1**	**35.2**	**34.9**	**33.4**	**32.3**
O/w current expenditure and transfers	29.3	29.0	28.4	28.2	26.9	26.0
- Interest	5.0	4.6	4.9	4.8	4.1	4.0
O/w capital expenditure	7.7	4.3	3.8	-	-	-
Current balance	-4.9	-4.5	-2.9	-3.0	-1.0	0.3
Primary balance	0.2	0.2	2.0	1.8	3.1	4.3
Overall balance	**-9.4**	**-5.7**	**-3.5**	**-3.0**	**-1.0**	**0.3**
Central government debt	95.6	90.2	88.4	84.7	80.8	78.5
% of central government revenues	312.3	296.3	279.4	264.9	249.4	241.2
Central government debt (ISKbn)	**1,468.3**	**1,468.3**	**1,501.4**	**1,509.3**	**1,514.5**	**1,548.1**
By residency of holder						
Domestic	758.3	865.9	885.4	890.0	893.1	912.9
Foreign	527.6	602.4	616.0	619.3	621.4	635.2
By place of issue						
Domestic	-	-	-	-	-	-
Foreign	-	-	-	-	-	-
By currency denomination						
Local currency	941.9	1,125.9	1,151.3	1,086.7	1,090.4	1,114.7
Foreign currency	344.0	342.4	350.1	422.6	424.1	433.5
In USD equivalent (eop exchange rate)	3.0	2.8	2.7	3.5	3.4	3.4
By maturity						
Less than 12 months (residual maturity)	-	-	-	-	-	-
Average maturity (years)	5.5	5.4	6.4	6.5	6.5	6.5
Average duration (years)	4.8	4.8	4.8	4.8	4.8	4.8
Memo						
Nominal GDP (ISKbn)	1,535.9	1,628.7	1,698.5	1,782.7	1,874.8	1,971.6

Source: Ministry of Finance, Statistics Iceland and Fitch estimates and forecasts

Figure 18
External Debt and Assets

(USDbn)	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013f
Gross external debt	**26.9**	**46.2**	**72.3**	**119.9**	**122.4**	**121.4**	**120.5**	**110.8**	**102.0**	**103.4**
% of GDP	202.7	283.6	434.3	586.9	727.2	1,002.3	959.1	789.2	750.9	727.7
% of CXR	537.3	698.7	909.5	1,037.5	1,323.0	1,695.4	1,588.7	1,159.2	1,156.2	1,088.6
By maturity										
Medium- and long-term	21.8	38.8	60.1	78.8	76.3	65.2	52.0	44.7	30.7	31.2
Short -term	5.1	7.4	12.2	41.1	46.1	56.3	68.5	66.2	71.2	72.2
% of total debt	18.9	15.9	16.9	34.3	37.6	46.3	56.9	59.7	69.9	69.9
By debtor										
Monetary authorities	**0.0**	**0.0**	**0.0**	**0.0**	**2.5**	**1.6**	**2.4**	**3.2**	**1.5**	**1.5**
General government	**3.5**	**2.5**	**3.4**	**4.0**	**6.9**	**6.8**	**7.3**	**8.6**	**6.4**	**6.4**
O/w central government	2.6	1.9	3.2	3.9	6.2	5.8	4.6	4.9	4.8	5.1
Banks	**20.0**	**37.9**	**59.3**	**96.1**	**5.6**	**2.4**	**1.8**	**1.2**	**1.0**	**1.0**
Other sectors	**3.4**	**5.9**	**9.5**	**19.8**	**109.9**	**112.2**	**111.4**	**101.0**	**94.6**	**96.0**
Gross external assets (non-equity)	**9.6**	**22.2**	**41.3**	**68.8**	**24.1**	**23.9**	**25.4**	**26.0**	**30.1**	**31.9**
International reserves, incl. gold	1.1	1.1	2.3	2.6	3.6	3.9	5.8	8.6	4.2	4.5
Other sovereign assets nes	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Deposit money banks' foreign assets	2.9	8.5	18.6	76.3	5.3	2.4	2.5	3.0	3.0	3.1
Other sector foreign assets	1.3	3.5	6.4	8.7	17.0	17.9	17.1	14.6	23.0	24.3
Net external debt	**17.2**	**24.0**	**31.0**	**51.1**	**98.3**	**97.5**	**95.1**	**84.8**	**71.9**	**71.5**
% of GDP	130.1	147.4	186.1	250.0	584.2	804.8	757.2	603.9	529.4	503.4
% of CXR	344.9	363.1	389.8	441.9	1,062.7	1,361.4	1,254.2	887.0	815.1	753.1
Net sovereign external debt	2.4	1.4	1.1	1.3	3.3	2.9	1.5	0.1	2.2	1.9
% of GDP	18.2	8.6	6.6	6.5	19.7	23.9	12.2	0.7	16.5	13.5
Net bank external debt	12.7	20.2	26.8	38.7	2.1	0.3	-0.6	-1.7	-1.9	-2.1
Net other external debt	2.1	2.4	3.1	11.1	92.9	94.3	94.3	86.4	71.6	71.7
Net international investment position	**-10.3**	**-13.7**	**-16.8**	**-23.6**	**-84.8**	**-84.9**	**-85.4**	**-75.5**	**-63.8**	**-62.9**
% of GDP	-77.5	-84.3	-100.6	-115.5	-503.7	-700.7	-679.3	-537.9	-470.1	-443.1
Sovereign net foreign assets	**-2.4**	**-1.4**	**-1.1**	**-1.3**	**-3.3**	**-2.9**	**-1.5**	**-0.1**	**-2.2**	**-1.9**
% of GDP	-18.1	-8.5	-6.4	-6.3	-19.5	-23.7	-12.0	-0.5	-16.3	-13.4
Debt service (principal & interest)	**3.8**	**6.6**	**11.0**	**20.4**	**32.9**	**20.6**	**18.8**	**19.1**	**9.8**	**5.1**
Debt service (% of CXR)	76.8	99.5	138.5	176.7	355.6	287.7	248.4	199.4	110.8	54.0
Interest (% of CXR)	10.5	15.0	29.9	39.0	66.9	52.0	38.4	32.4	24.5	21.5
Liquidity ratio (%)	31.6	33.0	51.1	63.0	105.4	12.9	8.1	9.3	14.9	9.2
Net sovereign FX debt (% of GDP)	9.4	1.8	0.6	-0.7	-5.6	-8.5	-22.3	-41.0	-10.9	-7.2
Memo										
Nominal GDP	13.3	16.3	16.7	20.4	16.8	12.1	12.6	14.0	13.6	14.2
Gross sovereign external debt										
Inter-company loans	0.5	1.5	2.6	10.1	11.0	12.2	11.7	12.2	11.0	11.9

Source: NBP, IMF, World Bank and Fitch estimates and forecasts

Figure 19
Balance of Payments

(USDbn)	2010	2011	2012	2013f	2014f	2015f
Current account balance	**-1.0**	**-0.9**	**-0.7**	**-0.4**	**-0.4**	**-0.3**
% of GDP	-8.1	-6.2	-4.8	-2.8	-2.5	-2.1
% of CXR	-13.3	-9.0	-7.5	-4.1	-3.7	-3.1
Trade balance	**1.0**	**0.8**	**0.6**	**0.7**	**0.8**	**0.7**
Exports, fob	4.6	5.3	5.0	5.4	5.8	6.2
Imports, fob	3.6	4.5	4.4	4.7	5.0	5.5
Services, net	**0.3**	**0.4**	**0.3**	**0.4**	**0.4**	**0.4**
Services, credit	2.5	3.0	3.0	3.3	3.6	3.8
Services, debit	2.2	2.6	2.8	2.9	3.2	3.5
Income, net	**-2.2**	**-2.0**	**-1.4**	**-1.4**	**-1.5**	**-1.3**
Income, credit	0.5	1.2	0.7	0.7	0.7	0.6
Income, debit	2.7	3.2	2.2	2.1	2.2	1.9
O/w: Interest payments	2.9	3.1	2.2	2.0	2.1	1.8
Current transfers, net	**-0.1**	**-0.1**	**-0.1**	**-0.1**	**-0.1**	**-0.1**
Memo						
Non-debt-creating inflows (net)	2.2	-0.2	5.5	0.8	0.8	0.9
O/w equity FDI	1.2	-0.3	5.4	0.7	0.8	0.9
O/w portfolio equity	1.1	0.1	0.1	0.1	0.1	0.1
O/w other	0.0	0.0	0.0	0.0	0.0	0.0
Change in reserves (- = increase)	2.0	2.9	-4.4	0.3	0.4	0.5
Gross external financing requirement	16.9	16.8	8.3	3.5	2.8	6.3
Stock of international reserves, incl. gold	5.8	8.6	4.2	4.5	4.9	5.4

Source: IMF and Fitch estimates and forecasts

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