

Address

Thórunn Gudmundsdóttir, Chair of the Central Bank of Iceland Supervisory Board, at the 56th Annual General Meeting of the Central Bank, 30 March 2017

Honourable Prime Minister; Minister of Finance and Economic Affairs, Directors, and Ambassadors; Ladies and Gentlemen: I welcome you to the 56th Annual General Meeting of the Central Bank of Iceland and hereby call the meeting to order. This year marks the 60th anniversary of Iceland's first step towards independent central banking activity, with the separation within Landsbanki Íslands when it was divided into two independent units, the central banking unit and the commercial bank. It is therefore particularly satisfying to see that some of the people who participated in those first steps are here with us today, among them Jóhannes Nordal, former Chief Economist at Landsbanki Íslands and then Governor of the Central Bank. Also with us today are former Central Bank employees Sigurdur Örn Einarsson and Pétur Urbancic. Pétur still works for the Bank as an independent contractor.

The principal role of the Central Bank's Supervisory Board is to oversee operations and to confirm rules and the Governor's proposals. The Board comprises seven members who are elected following each Parliamentary election. Sometimes changes take place during the term, but there has been no change in the Board's main membership since last year. The Supervisory Board held 14 meetings in the course of 2016.

As is described in the Annual Report, which is available here today, the Central Bank is responsible for a number of regular functions and various special projects each year. As in the previous year, the Bank's largest special projects centred on lifting the capital controls on the basis of the liberalisation strategy introduced in 2015. The first phase of the strategy entailed winding up the failed commercial and banks' estates, the second focused on defining and releasing offshore króna assets, and the third centred on general liberalisation of capital controls on households and businesses. From the end of March until the year-end, offshore króna assets shrank from 320 b.kr. to 191 b.kr., with most of the reduction taking place through the June auction. With the entry into force of amending legislation in late October, steps were taken towards nearly full capital account liberalisation at the end of the year, which laid the foundation for the welcome announcement earlier this month of the removal of capital controls on individuals, firms, and pension funds. Extensive preparation work on the latter two phases of the strategy was carried out in the Central Bank last year, in cooperation with other Government authorities. The same is true of the adoption of rules in June to affect carry trade-related capital inflows.

By law, the principal objective of the Central Bank of Iceland is to promote price stability. The Central Bank of Iceland shall also promote financial stability. Inflation was below the inflation target throughout 2016. The Bank's Monetary Policy Committee lowered interest rates in August and again in December, for a total rate cut of 0.75 percentage points, as is described in Chapter II of the Bank's Annual Report.

Economic conditions in the financial system were broadly favourable in 2016. Private sector debt levels were relatively low in historical terms, and households' and businesses' resilience to shocks was greater than it had been in a long while. Stress test results showed that on the whole, the large commercial banks were relatively well prepared to face shocks. The commercial banks' position was sound at the year-end, the terms offered to them in foreign credit markets improved, and market access was facilitated by rising sovereign credit ratings. However, demand pressures surfaced in the labour and housing markets during the year, and the swift growth of the tourism sector is a potential source of growing risk, as is discussed in Chapter III of the Annual Report.

The Central Bank works specifically to promote the security, effectiveness, and efficiency of core financial market infrastructure in Iceland. Work on renewing the real-time gross settlement system and the retail netting system, two important infrastructure elements, moved forward during the year. System operations went smoothly in 2016. A new trading system was implemented during the year.

The digitisation of cash has been a topic of discussion, and the Bank has been following developments closely. As before, conventional cash held its ground during the year, with banknotes and coin in circulation rising slightly as a share of GDP, to 2.3%, although this is a small percentage in international context. The Central Bank's role in this area is to satisfy demand for currency. The 10,000 kr. banknote has gained ground and accounted for 47% of the value of issued banknotes by the year-end.

The foreign exchange reserves held by the Central Bank grew significantly, to 815 b.kr. by the end of the year. The Governor will present further detail on the costs and benefits of the reserves for the economy as a whole. As he will discuss, the benefits of the reserves are distributed throughout the economy, but the costs are recognised in the Central Bank's accounts.

According to the profit and loss account, the Bank recorded a loss of nearly 35 b.kr. in 2016, as opposed to a profit of 5.6 b.kr. in 2015 and a profit of 11.2 b.kr. in 2014. The negative operating results stem mainly from the foreign exchange reserves, as I have mentioned – more specifically, from a negative exchange rate difference, as can be seen in the annual accounts, which are available to you today. One of the Bank's tasks is to maintain the foreign exchange reserves, and the larger the reserves are, the more exchange rate movements affect the Bank's operating performance. Wages and related expenses rose by 9% between years, owing mainly to contractual pay increases and a heavy workload during the year. The Bank's assets totalled 876 b.kr. at the year-end, and equity declined from 79 b.kr. at the end of 2015 to 44 b.kr. at the end of 2016. The year-end capital ratio was 5%, as opposed to 8.6% at year-end 2015. There is no profit for disposal, and the Bank does not consider it timely to take a decision to call in equity on the basis of Article 34 of the Central Bank Act, no. 36/2001, as is mentioned in the Annual Report.

In 2016, the Central Bank employed 180 members of staff. The gender ratio remained relatively equal: just over 51% of staff members are male and just under 49% female. The gender ratio among directors and middle management was more unequal during the year, with 61% of managers male and 39% female. At present, six departmental directors are male and four are female. Two female directors resigned last year.

I would like to take this opportunity to thank Central Bank staff members for very satisfying collaboration in 2016. In particular, I would like to thank my fellow Supervisory Board members and the Governor, Deputy Governor, Supervisory Board secretary, and Internal Auditor for fruitful cooperation. I will now turn the floor over to Prime Minister Bjarni Benediktsson. Following his speech, Governor Már Gudmundsson will address the meeting.