



# Iceland's Return to the Capital Markets

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*September 2011*

# Iceland's return to the capital markets: Overview

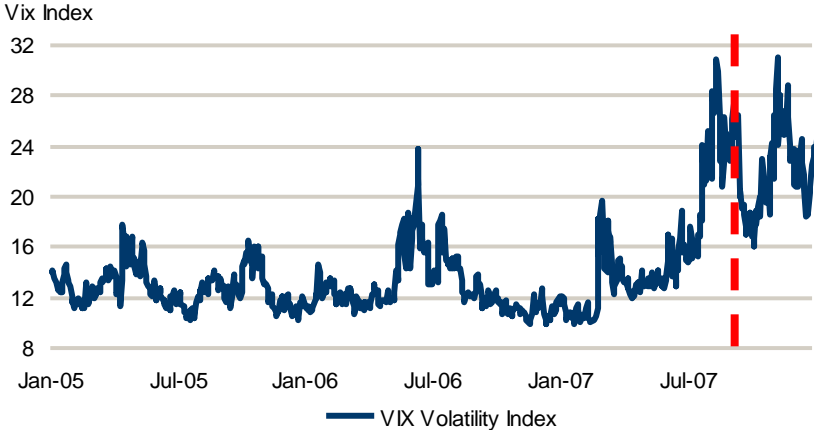
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- The first European sovereign impacted by the financial crisis and denied access to the capital markets
- Despite unprecedented impact on the domestic economy, decisive policy response has restored market confidence
- The first European sovereign to restore access to the international capital markets

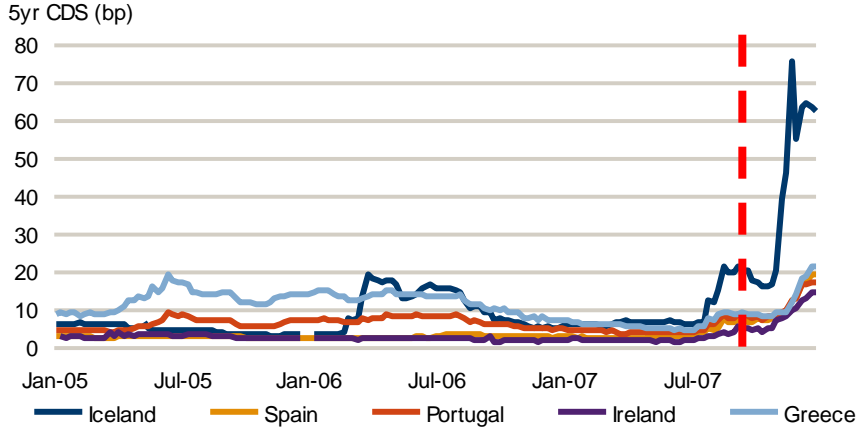
# Pre-crisis market: False sense of security

## Low volatility and high rates across Europe prior to the financial crisis

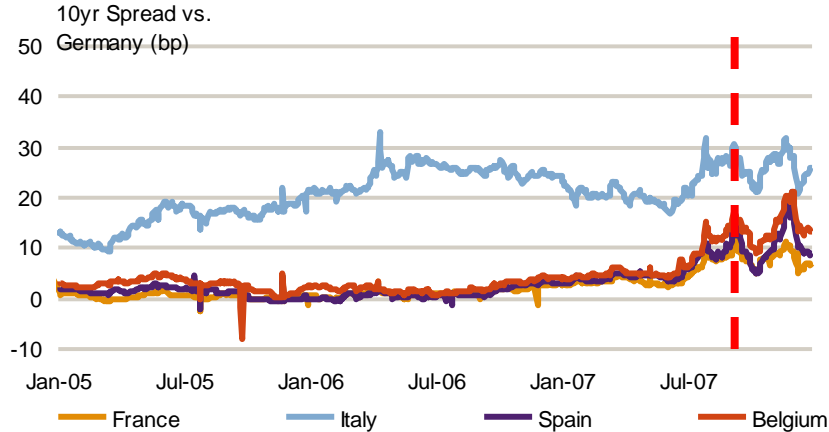
### Low Market Volatility



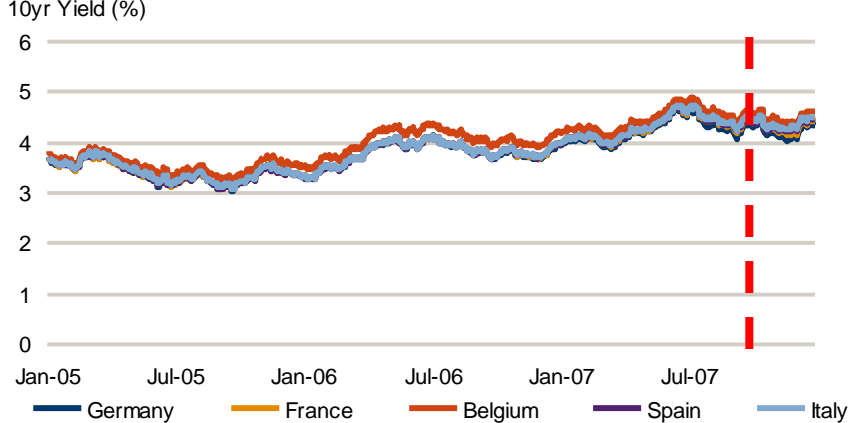
### Low Sovereign CDS spreads enjoyed across Europe



### Narrow Inter-Sovereign Bond Spreads



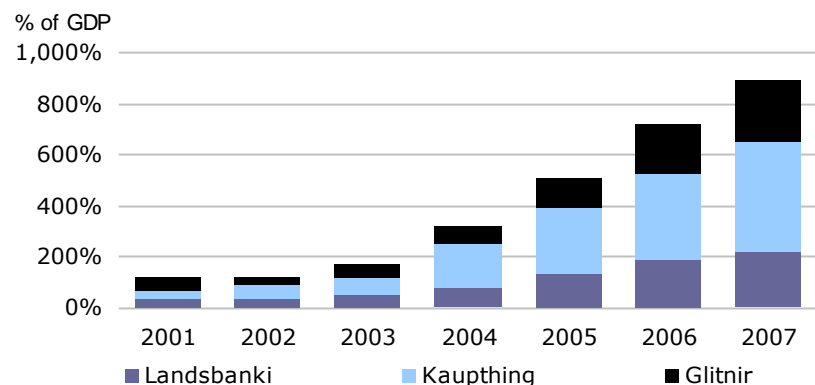
### A High Rate Environment



# Crisis in Iceland: A product of a mistaken paradigm

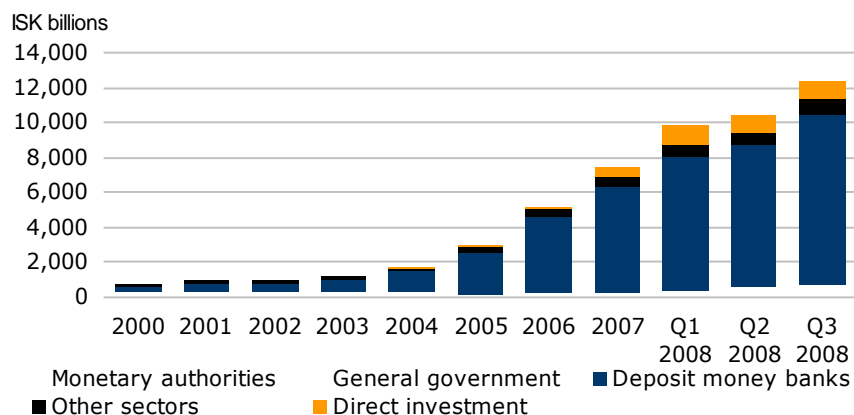
A large banking sector, reliant on international wholesale funding sources, was the key factor

## Large and leveraged banking sector...



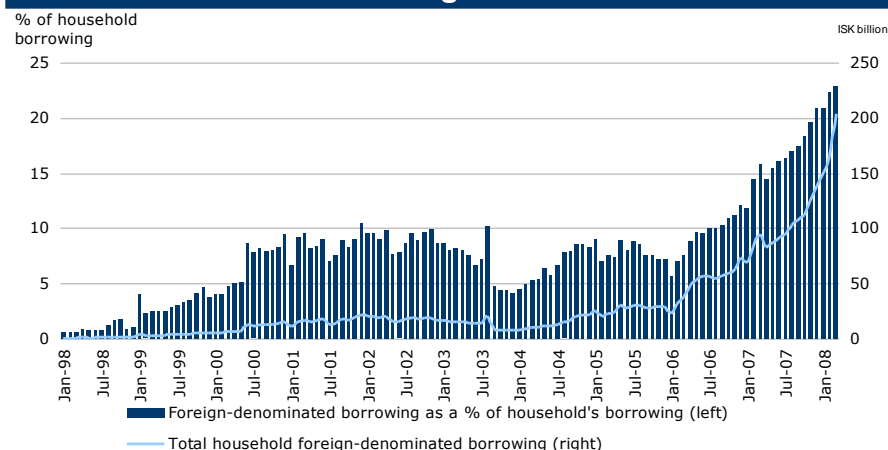
The 3 major banks had loans equivalent to ~9x GDP Iceland

## Rising external debt...



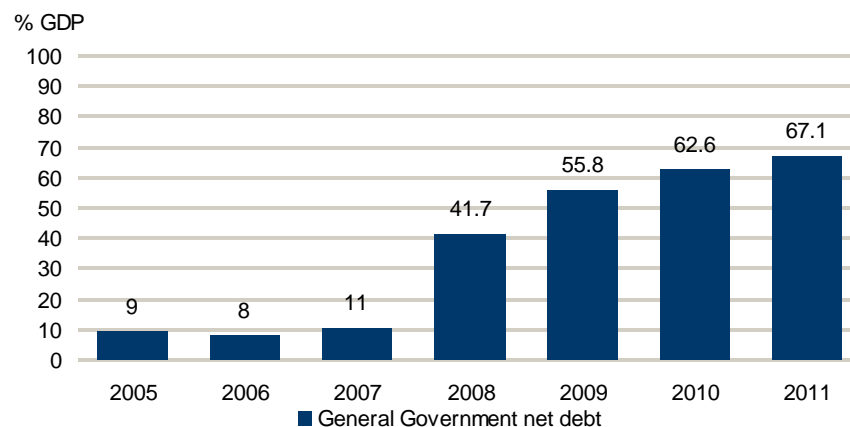
Bank funding strategies were focussed on US & European debt markets

## ...and increasing household debt



Household debt had risen to 213% of disposable income by 2006

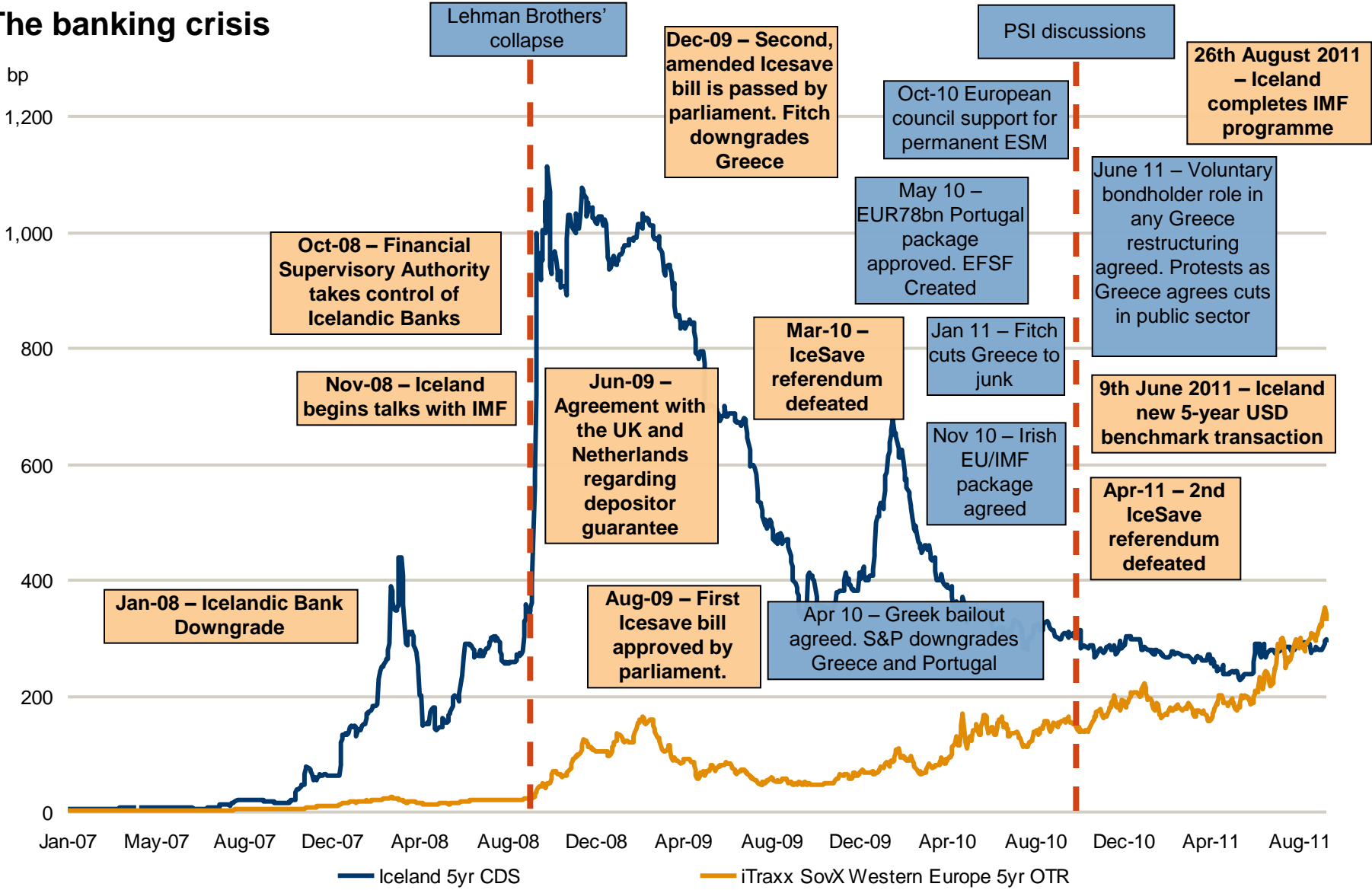
## ...but low levels of government debt



Source: IMF & Market Data

# Evolution of the financial crisis part

## The banking crisis



# Key elements in Iceland's crisis response

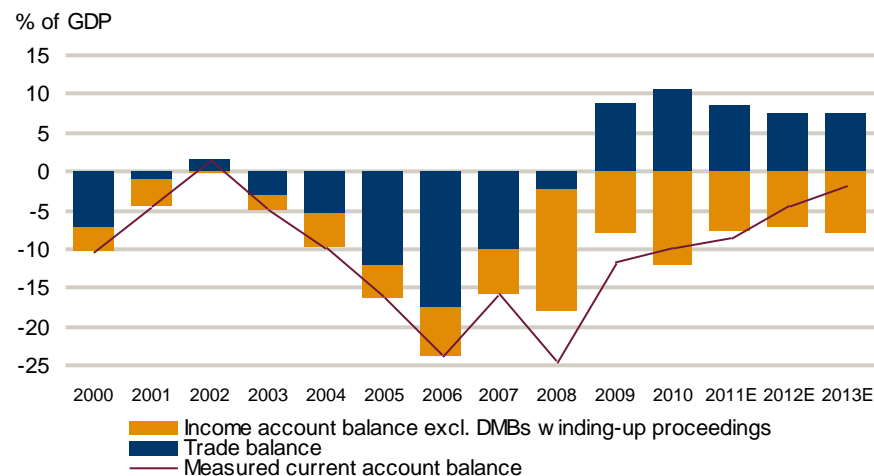
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<b>Iceland</b>	<b>Eurozone</b>
<b>Rapid and decisive action</b>	<b>Slow and reactive</b>
Banking sector Capital controls	
<b>Well defined credit concerns</b>	<b>Complex credit concerns</b>
Banking sector / capital controls	Banking sector (Ireland - NAMA)
<b>Credible financing plan</b>	<b>Adequacy of response questioned</b>
IMF Nordics	
<b>Flexible economy</b>	<b>Inflexible common currency area</b>
Exchange rates Fiscal consolidation	
<b>Strong initial position of sovereign</b>	<b>Weak sovereign fiscal position</b>
Debt Deficit Pensions	Excluding Ireland
<b>Good execution of programme</b>	<b>Slow and mixed execution</b>
Strong track record Expectations managed	

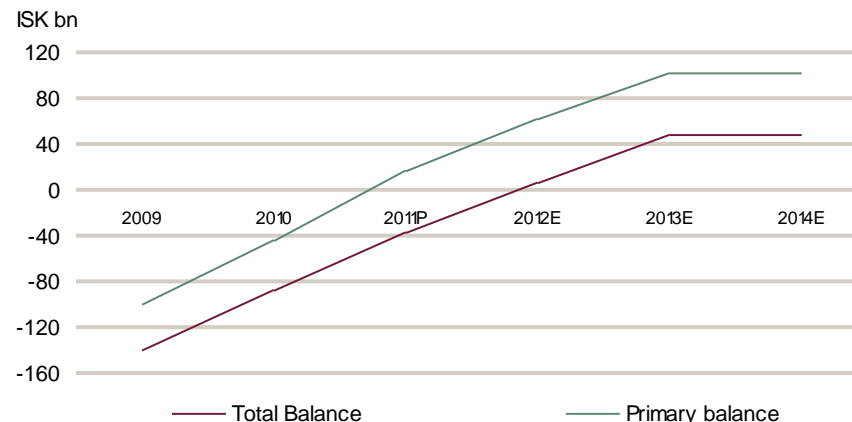
# Icelandic recovery

The Icelandic recovery is supported by a number of strong fundamentals across both GDP growth, reduced inflation and balanced public budgets

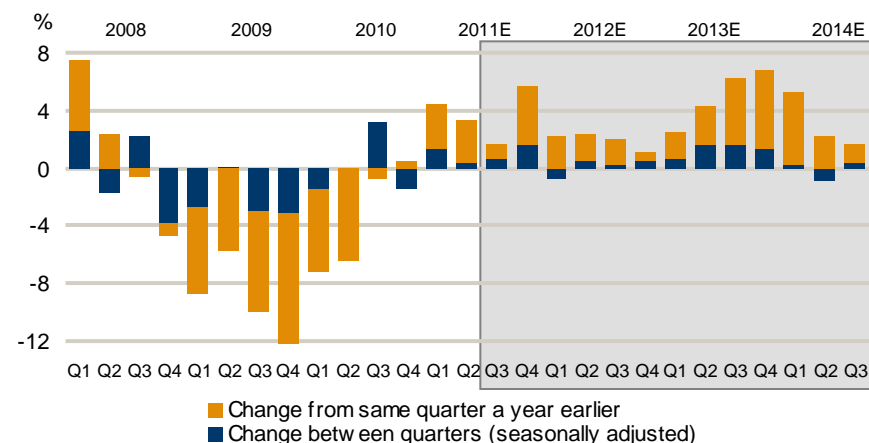
**Current account balance**



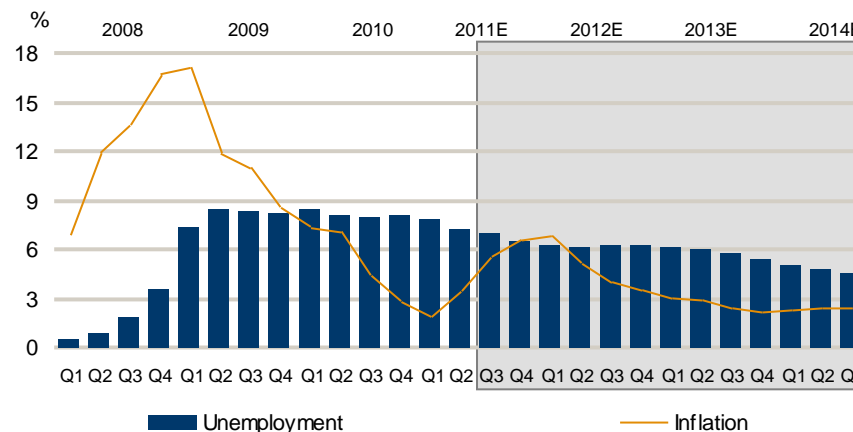
**Primary and Ordinary budget**



**Gross domestic product (% q-o-q change)**



**Inflation and Unemployment**



Source: Central bank of Iceland, Statistics Iceland, Monetary Bulletin 2011/3

# Iceland's access to the international markets

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- Restructuring of the domestic banking sector and execution of recovery plan provided an opportunity to access the market
  - ▶ International investors appreciated the clear recovery plan provided by Iceland, as well as the credible milestones reached thus far as well as forecasted for the future
  - ▶ In addition, IMF and rating agency comments were positively perceived
- Positive feedback from discussions with investors led to the formal process of issuing a benchmark bond. The mandate was announced on the 31<sup>st</sup> May and a 6 day road show followed
- Successful issue executed on 9<sup>th</sup> June

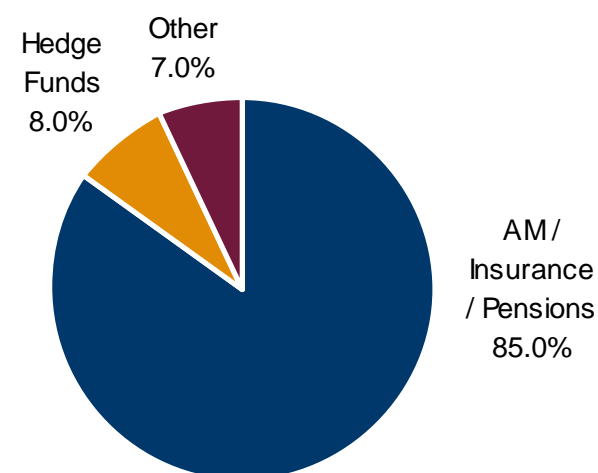
# Republic of Iceland – US\$1bn 4.875% Jun-16

Iceland achieved a very successful return to the capital markets on 9<sup>th</sup> June 2011, following an absence of two and a half years.

## New issue terms

Issuer:	Iceland
Issue Rating:	Baa3/BBB-/BB+
Format:	Reg S / 144A
Amount:	US\$1bn
Maturity date:	16-June-2016
Coupon (p.a):	4.875%
Reoffer spread vs. m/s	+320bp
Reoffer spread vs. Bmk	+343.6bp
Bookrunners:	Barclays +2

## Distribution by investor type



Final orderbook : USD 2bn +, with 110 tickets

# Why did investors buy Iceland in US Dollars?

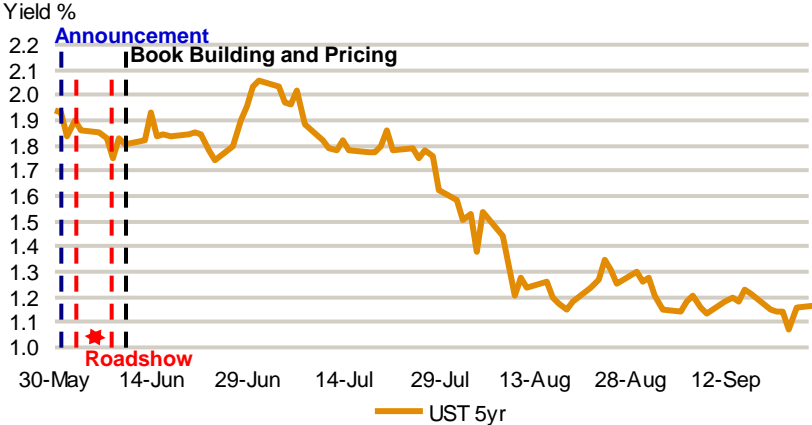
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- Credible programme of fiscal consolidation adhered to
- Positive endorsement by the IMF
- Credit rating confirmations
- US Dollar market offers an alternative to Euro with detail oriented investors participating after making specific value analysis
- Non-Eurozone country
  - ▶ EMU countries have been effectively 'shut off' from US Dollar markets in recent months
  - ▶ US Dollar market is deeper and more flexible set of investors

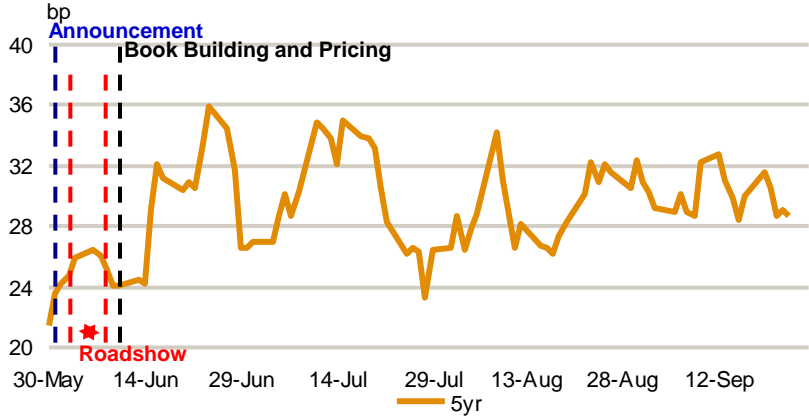
# Market Backdrop Pre- and Post Pricing

Iceland has performed well versus US Treasuries since pricing, in line with Eastern European Sovereigns

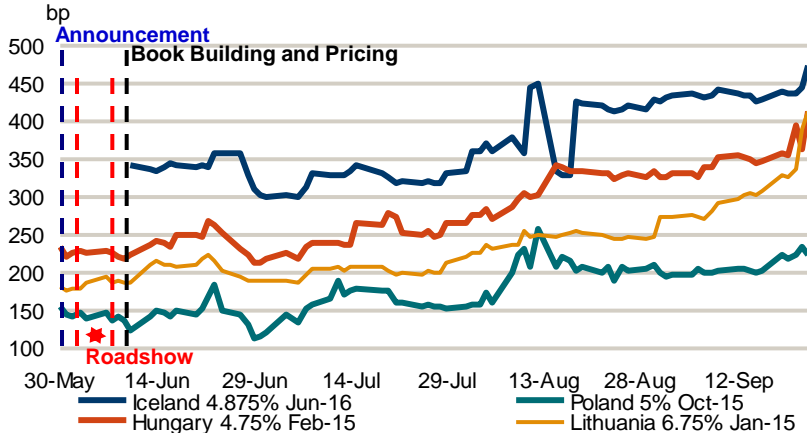
### 5yr Treasury Yield



### 5yr US Swap Spread



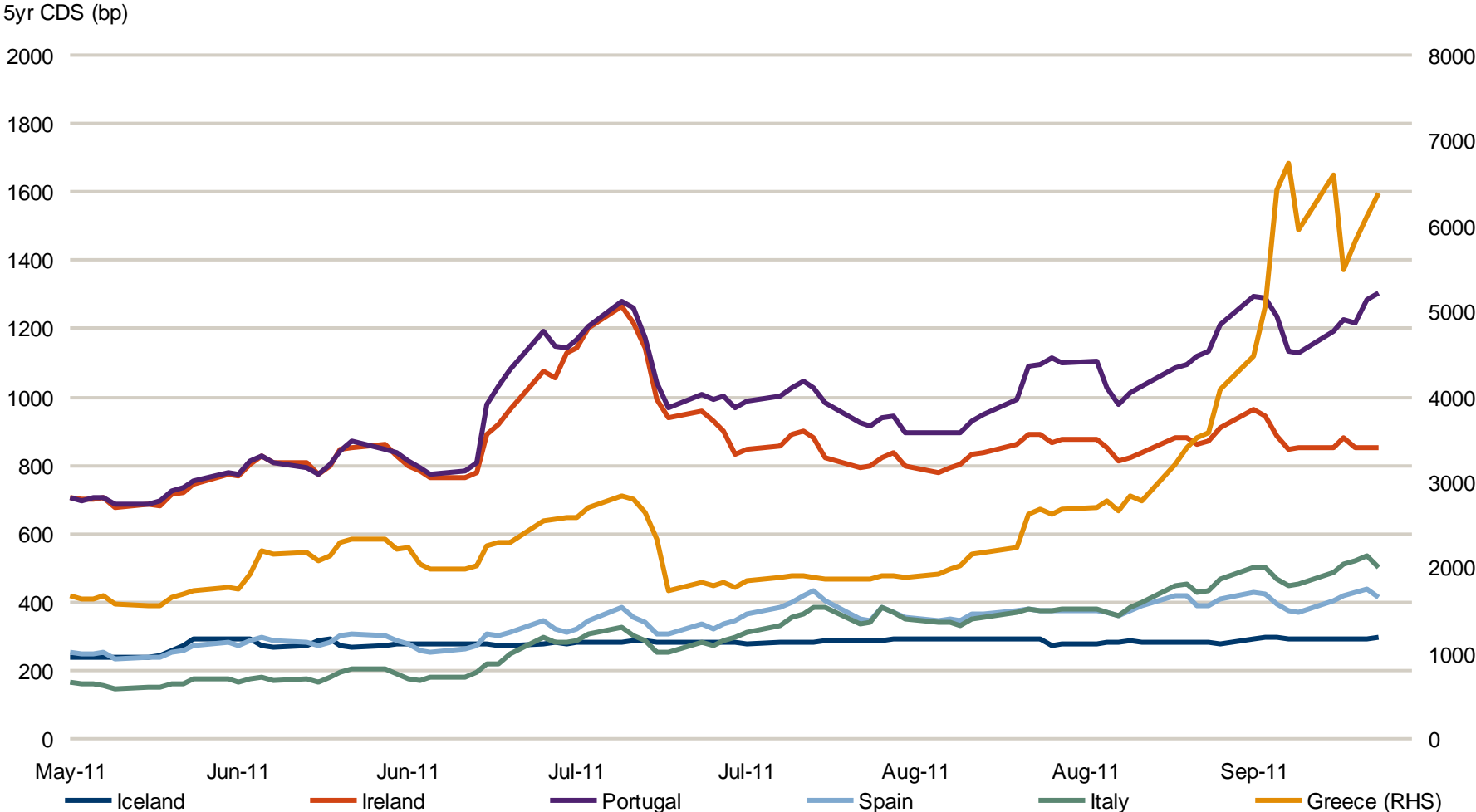
### Iceland and Comparable 5yr UST spread evolution



Source: Bloomberg and Barclays Capital Research

# Sovereign CDS performance since pricing

## 5-year CDS performance post pricing of Iceland USD benchmark



# Lessons

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- Markets can be very volatile and psychologically driven
  - ▶ Lack of liquidity
  - ▶ Misleading market signals
- Key is to provide strong leadership to guide markets
- Manage expectations and deliver on plan
- Iceland has been a good success story

# Positive sentiment continues

The Republic of Iceland's successful bond transaction in June was well received by the broader investor and "stake holder" universe

The  
Economist

*"Latvia and Iceland successfully issued sovereign bonds at yields approaching Spain's last week. There are rumours that Dubai may follow suit. That the countries which started the sovereign debt crisis are returning to the market while peripheral euro-zone sovereigns continue to struggle has led to crowing from those who see austerity as a misguided strategy for Greece, Ireland and Portugal.*

*The facts certainly suggest that the yoke of a single currency is a barrier to recovery. Iceland's krona has halved in value since the crisis began, providing a stimulus to exports unavailable to euro-zone governments. Iceland let its banks go bust, whereas Ireland's decision to stand behind hers led directly to the spike in Irish bond yields"*

Date: 13 June, 2011

The Banker  
GLOBAL FINANCIAL INTELLIGENCE SINCE 1926

*Iceland's capital markets return - Confidence building*

*"Investors sought comfort on four key issues: Iceland's macroeconomic and fiscal position; the status and leverage of its banks; the progress on exchange controls imposed after the financial crisis; and Icesave, the Landebanki savings brand. The first three were relatively straightforward as Iceland was doing all the right things and could prove it with solid facts and figures. Icesave was more challenging.*

*"According to the latest estimate, the asset recovery at the Landsbanki's estate should provide the UK and Dutch authorities with [the] bulk of the priority claims"*

Date: 1 August, 2011

PAUL  
KRUGMAN

*"Iceland still has high unemployment and is a long way from a full recovery; but it's no longer in crisis, it has regained access to international capital markets, and has done all that with its society intact.*

*And it has done all that with very heterodox policies — debt repudiation, capital controls, and currency depreciation. It was as close as you can get to the polar opposite of the gold standard. And it has worked"*

Date: 1 September 2011

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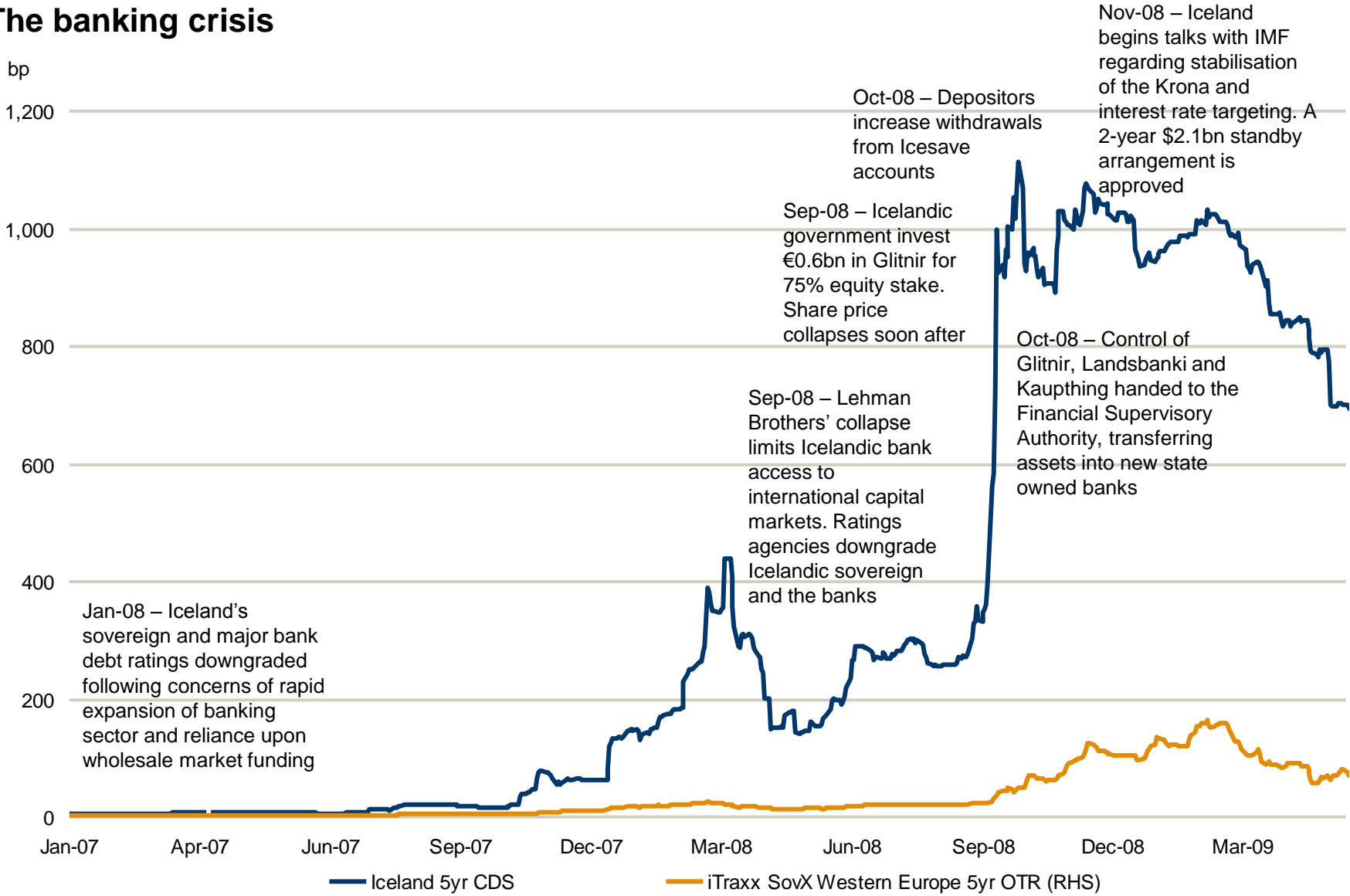
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# Evolution of the financial crisis part (i)

## The banking crisis



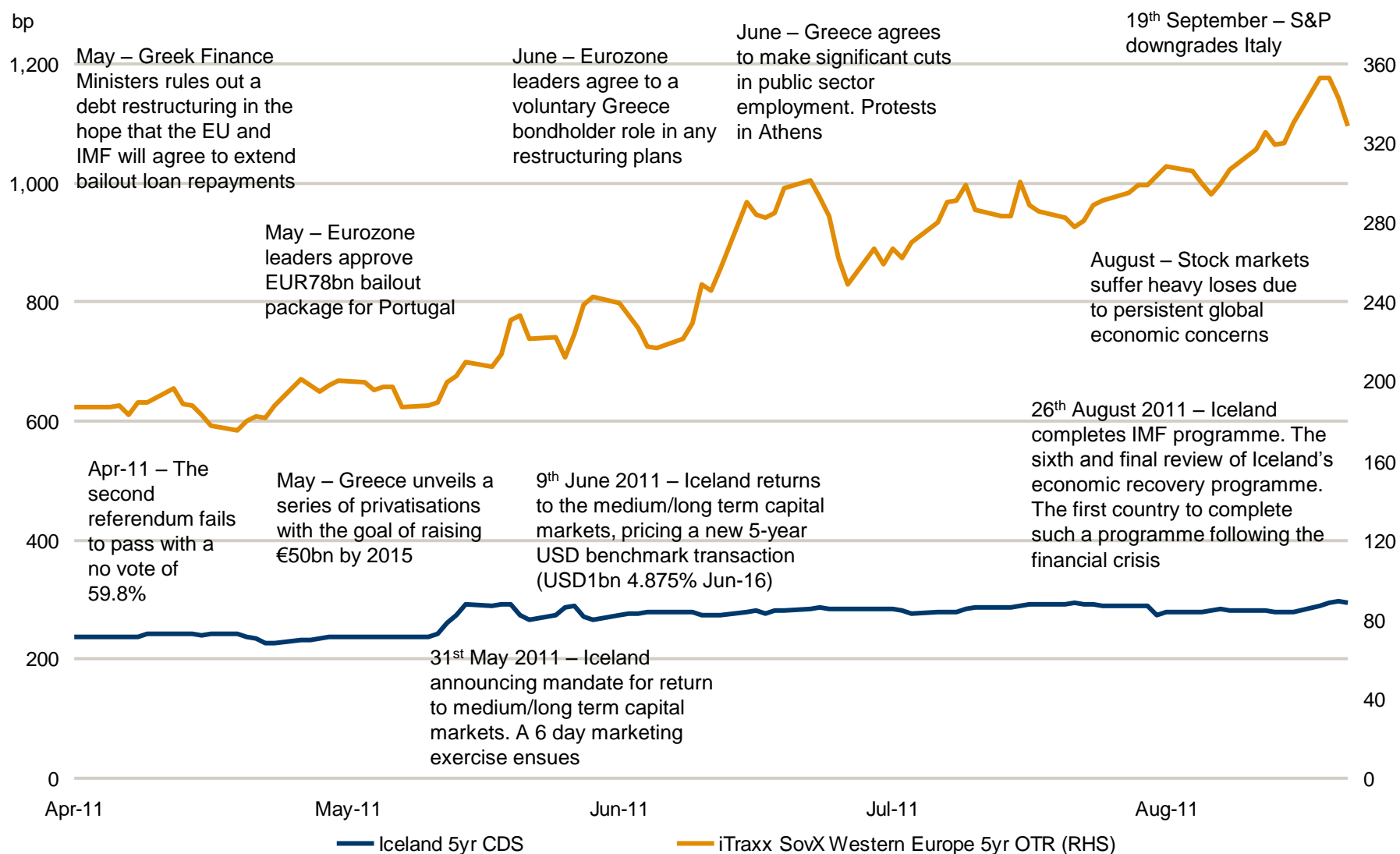
# Evolution of the financial crisis part (ii)

## IceSave referendums and European sovereign crisis



# Evolution of the financial crisis part (iii)

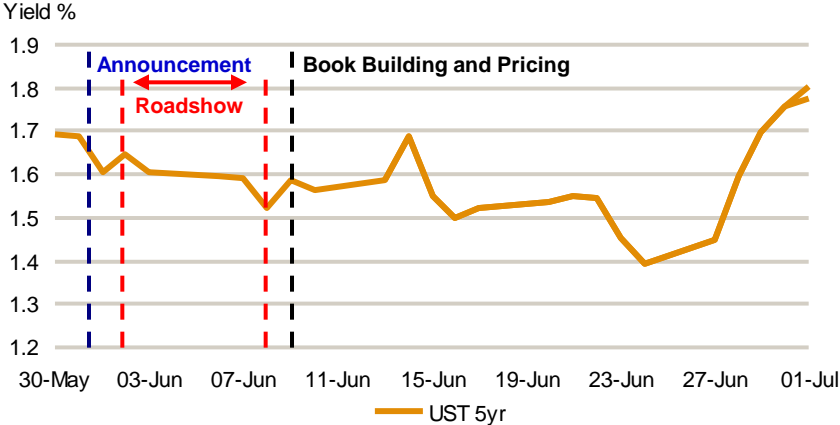
## European sovereign crisis continues



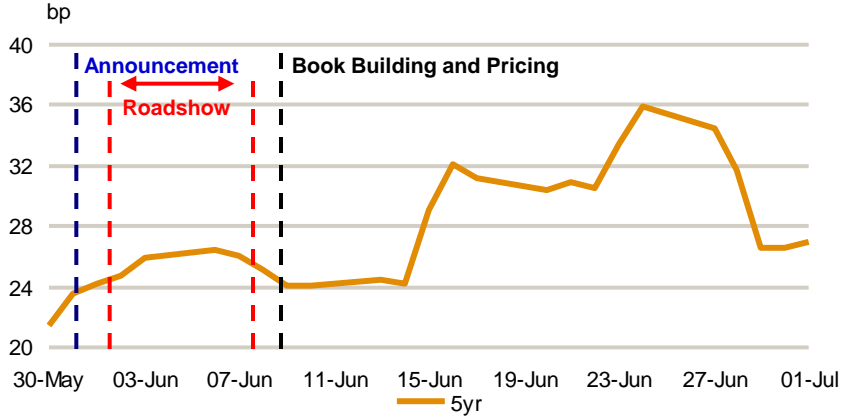
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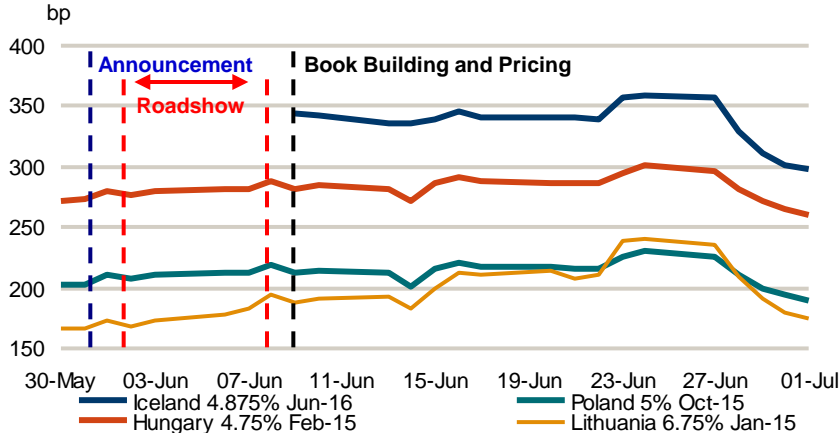
### 5yr Treasury Yield



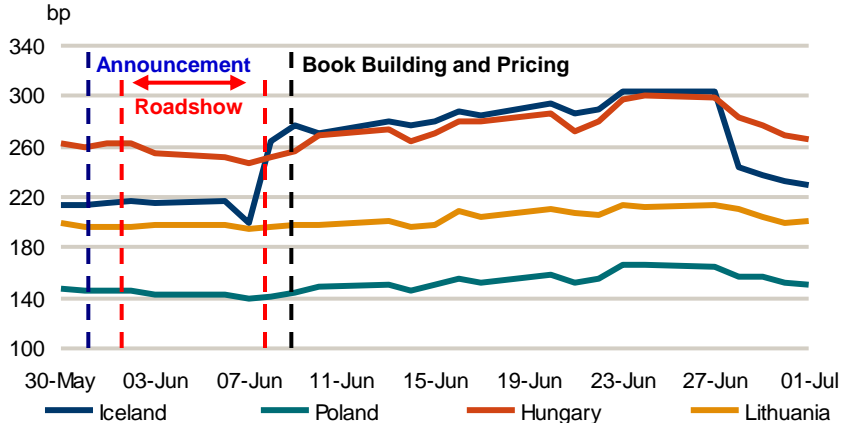
### 5yr US Swap Spread



### Iceland and Comparable 5yr UST spread evolution

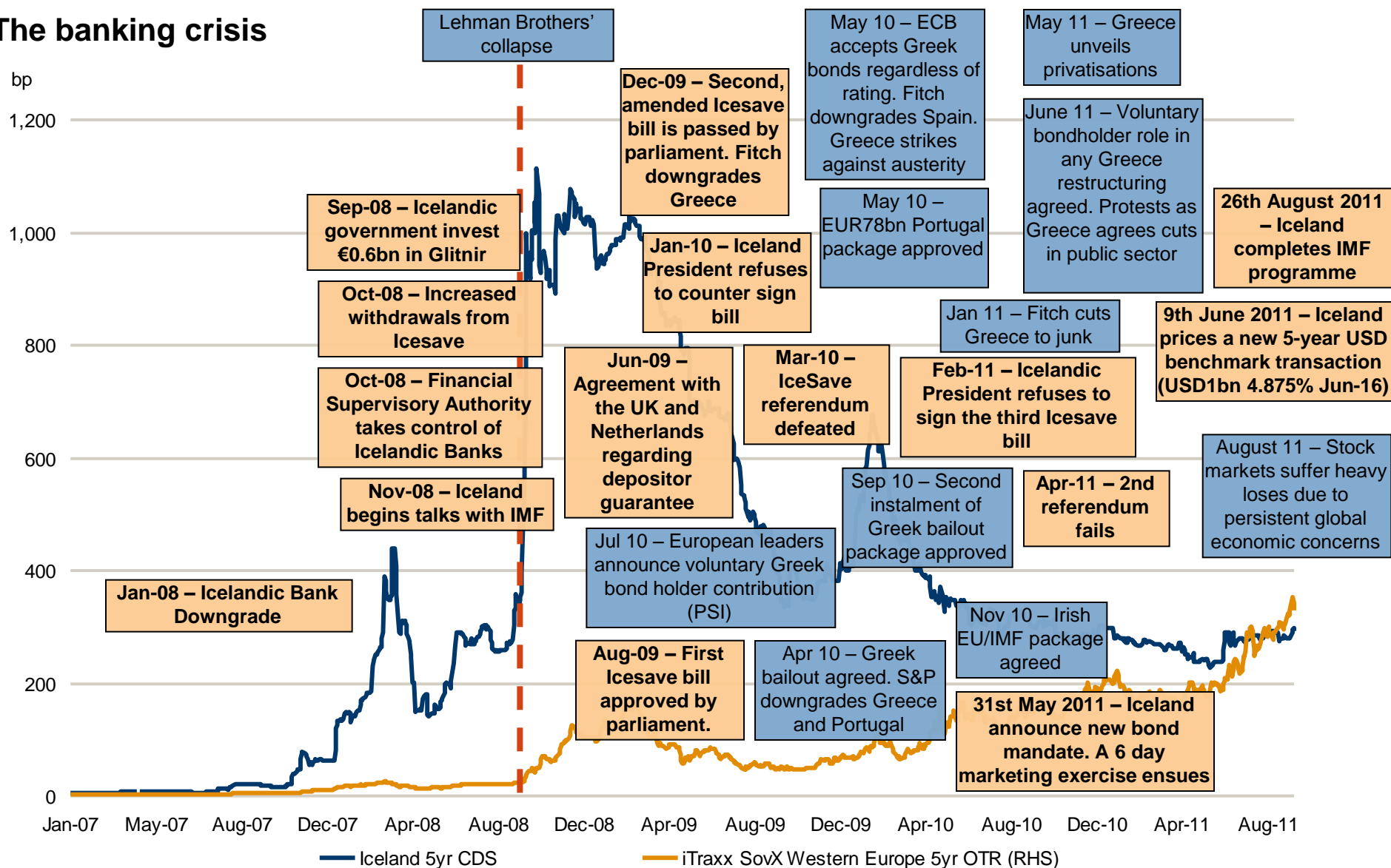


### 5yr CDS Evolution



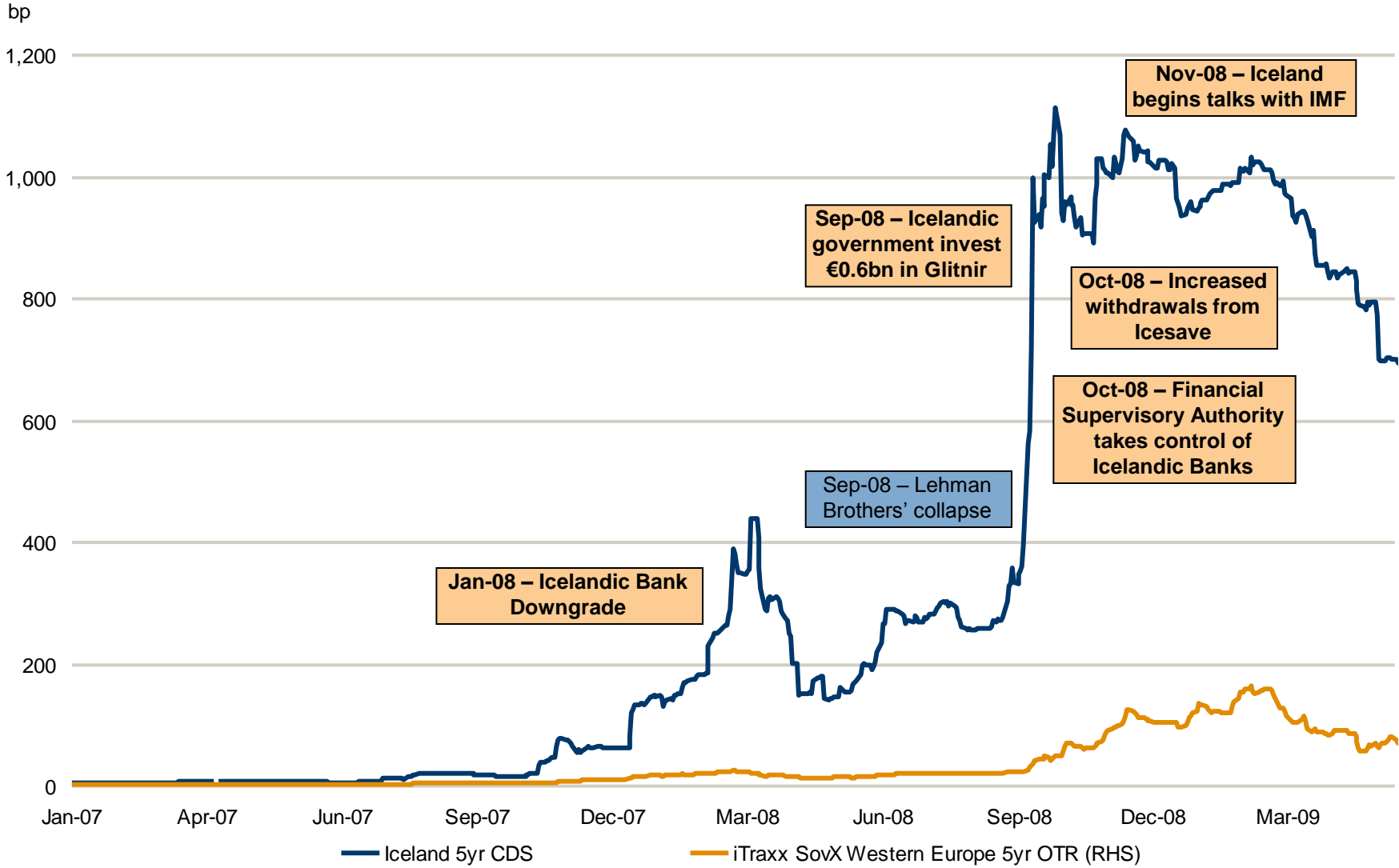
# Evolution of the financial crisis part

## The banking crisis



# Evolution of the financial crisis part (i)

## The banking crisis



# Evolution of the financial crisis part (ii)

## IceSave referendums and European sovereign crisis

