# Iceland's $1 Billion Commercial Paper Program Rated 'A-1+'; Other Ratings Affirmed

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LONDON (Standard & Poor's) Nov. 15, 2001--Standard & Poor's today assigned its 'A-1'-plus short-term unsecured debt rating to the $1 billion U.S. Commercial Paper Program launched by the Republic of Iceland last month. At the same time, Standard & Poor's affirmed all its ratings on Iceland, including its single-'A'-plus/'A-1'-plus foreign-currency and double-'A'-plus/'A-1'-plus local-currency issuer credit ratings. The outlook is negative.

The ratings on Iceland are supported by a strengthened fiscal position and a high standard of living. The government, supported by a buoyant economy, has partly counteracted a decline in the domestic savings rate (to less than 14% of GDP) by running fiscal surpluses since 1998. This compares very favorably with its 'A' rated peers, which generally run deficits. Reflecting this fiscal adjustment, Iceland's general government debt ratios have declined to 49% of GDP in 2001 from 59% in 1995. The increase of the ratio from 41.5% of GDP in 2000 is entirely due to the inflation of foreign currency denominated debt in the wake of the depreciation of the krona this year. Standard & Poor's expects that the 2001 central government budget will be in surplus for the fifth year running. A deficit is expected for 2002, as the economic slowdown deepens and continues to erode government revenue. With per capita income of about $26,000, Iceland is easily the most prosperous of 'A' rated sovereigns.

Iceland's ratings are constrained by its high level of external indebtedness and its low trend of growth. Whereas other 'A' rated countries' GDP grew somewhat faster over 1995-2000 than Iceland's average of 4.1%, they managed to do so while reducing their external imbalances, whereas Iceland's current account balance turned to a deficit of 10% of GDP in 2000 from a surplus in 1995. Although it is now falling in line with domestic demand, the current account deficit is expected to be 6.5% and 3% of GDP in 2001 and 2002, respectively. Accordingly, Iceland's international investment position has weakened considerably, and external debt accounts for an estimated 287% of exports at the end of 2001, or 111% of GDP.

In Standard & Poor's view, leading indicators of financial stress are present in Iceland, including a credit-driven demand boom, real estate price inflation, and external imbalances. The ratings on Iceland could improve if the government is able to maintain the structural fiscal surplus position over the medium term despite the cyclical slowdown. A hard economic landing leading to difficulties in the financial sector and/or fiscal slippage could exert downward pressure on the ratings.

A detailed comment on the fiscal outlook and the prospects for the Icelandic economy has been published by Standard & Poor's (see commentary article titled "Slowdown Raises Challenges for Economic Policy in Iceland", published on Oct. 22, 2001, which can be found on RatingsDirect, Standard & Poor's Web-based credit analysis system).