ICELAND CHAMBER OF COMMERCE

Cutting the Gordian Knot

Concluding the Winding-Up Proceedings of the Failed Banks' Estates

Iceland Chamber of Commerce

24 June 2014

Executive Summary

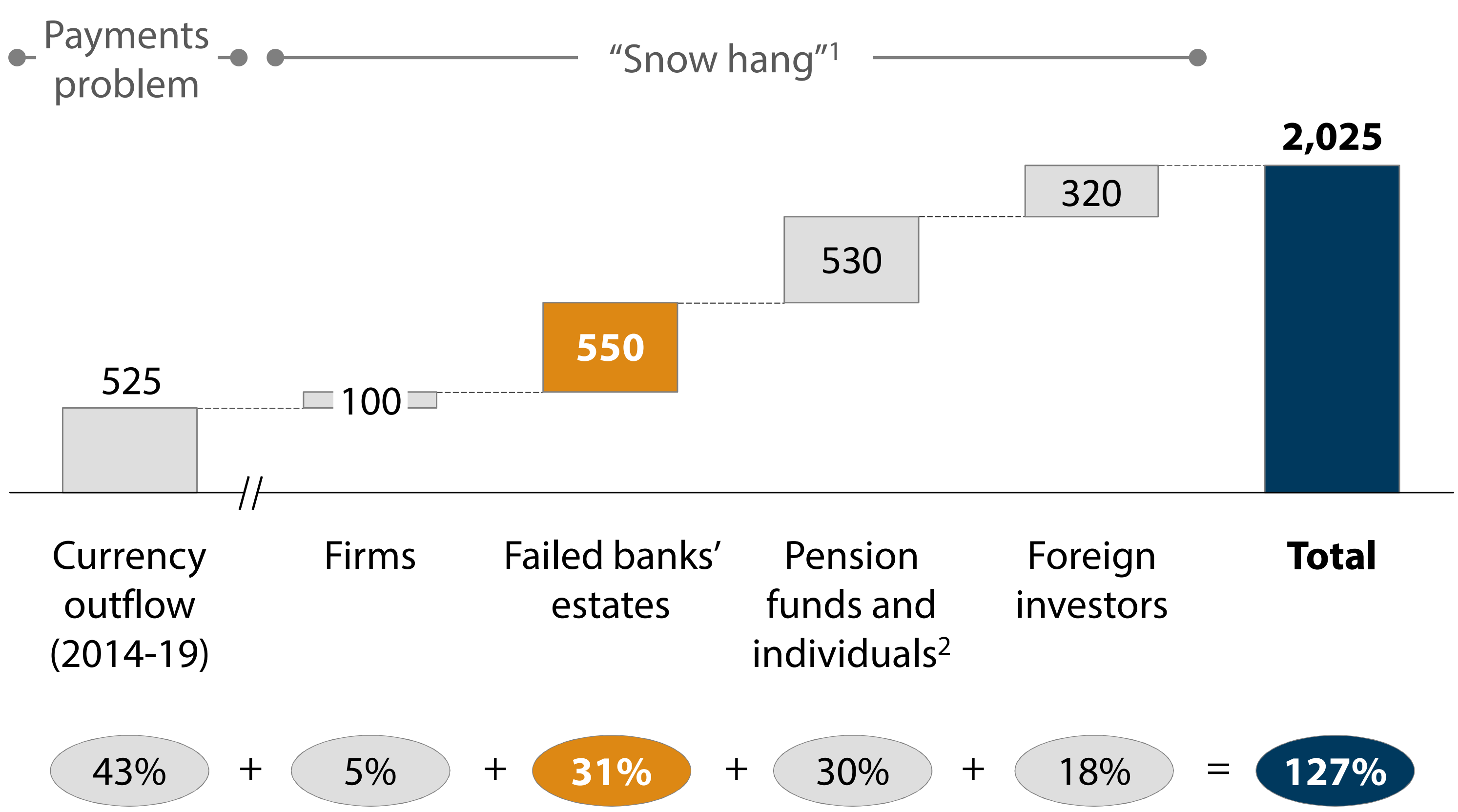
Excerpt from the full report[1]

- Iceland has been **unable to lift the capital controls due to a shortage of foreign currency**. This is in large part due to the **currency need of the failed banks' estates**.
- **Creditor expectations of domestic asset recovery exceed the Chamber's estimated scope for exemptions** from the capital controls. **A disbursement of domestic assets needs to be approx. 600 bn. ISK below book value** to fall within this scope.
- **The optimal solution to the current stalemate is through composition agreements** within the current scope for capital control exemptions. This has benefits for both creditors and the national economy:
  - **Creditors** stop accumulating losses through lost time value of capital, operating costs and the bank tax. In total **these losses amount to 260 bn. ISK per annum.**
  - **The Icelandic economy** gains through a **more rapid relief of the capital controls** once the estates' situations has been resolved.
- If such agreements cannot be reached, **bankruptcy proceedings are a better alternative than a continued stalemate** without any disbursement of assets. This holds true for both creditors and the national economy.

1 The full report from 18 June 2014 is only available in Icelandic and can be accessed through the following link: http://www.vi.is/files/Skodun%20throtabu_1795107629.pdf. Please contact the Chamber for additional information, tel. +354 510 7100.

Iceland may need up to 130% of GDP in foreign currency to lift the capital controls, in large part due to the estates

Iceland's Currency Need (ISK billions / % of GDP)

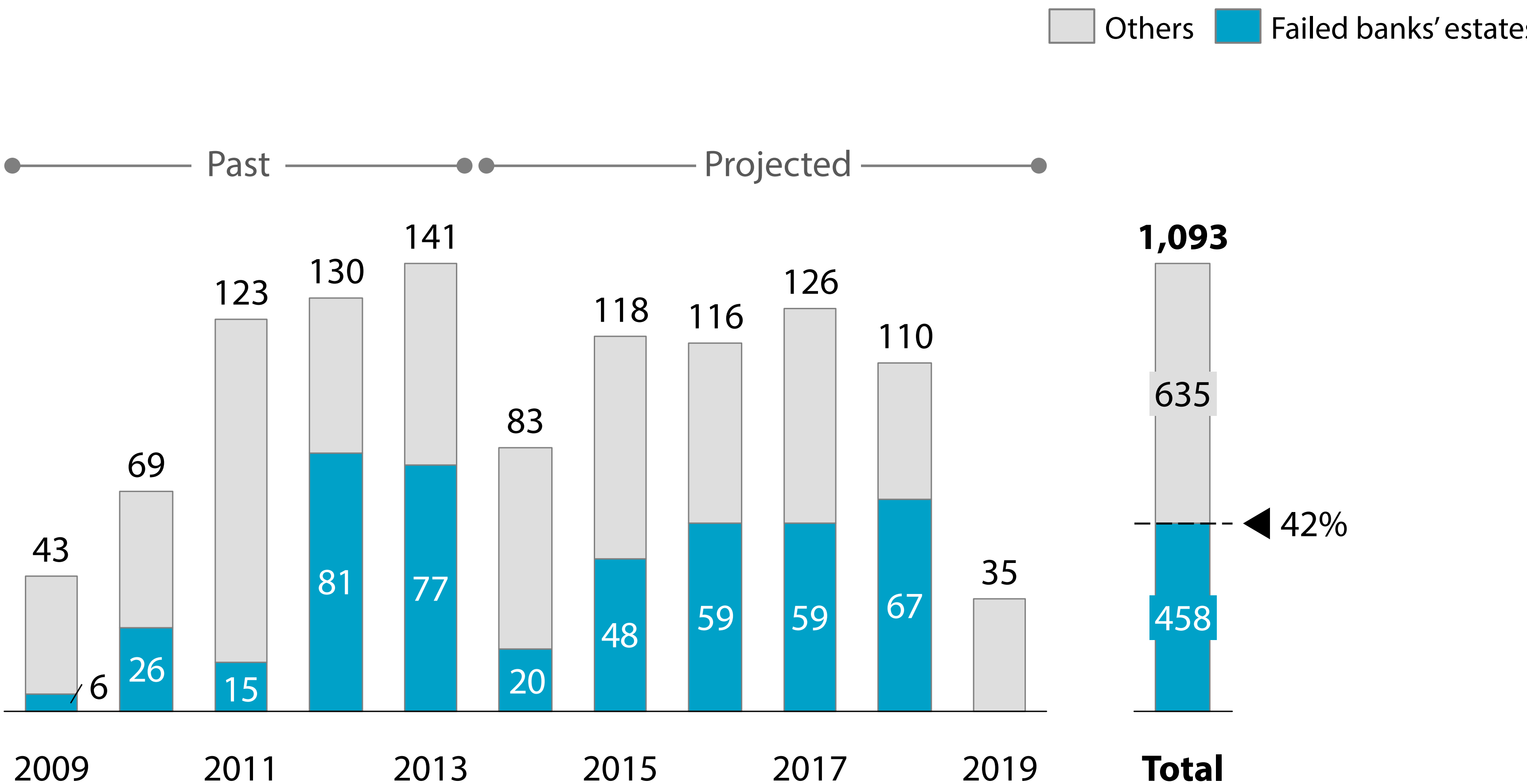


1 Key assumptions behind the size estimates is covered in further detail in the ICoC's opinion piece (only available in Icelandic)
2 There of 470 bn. ISK from pension funds and 60 bn. ISK from individuals

Sources: Central Bank of Iceland; ICoC analysis

The estates receive high payments on foreign loans, reducing the economy's ability to accumulate currency

Estimated payments on foreign loans (ISK billions)[1]



1 Estimated payments by parties other than the Treasury and Central Bank of Iceland on foreign loans and foreign denominated loans to the failed banks

Sources: Statistics Iceland; Central Bank of Iceland

No resolution committee has submitted a request for capital controls exemptions that has been approved

1 Resolution Committee
- Submits a request for an exemption from the capital controls to pass a proposed composition agreement

2 Central Bank of Iceland
- Assesses whether the request puts economic or financial stability at risk

No request has passed this stage of the approval process

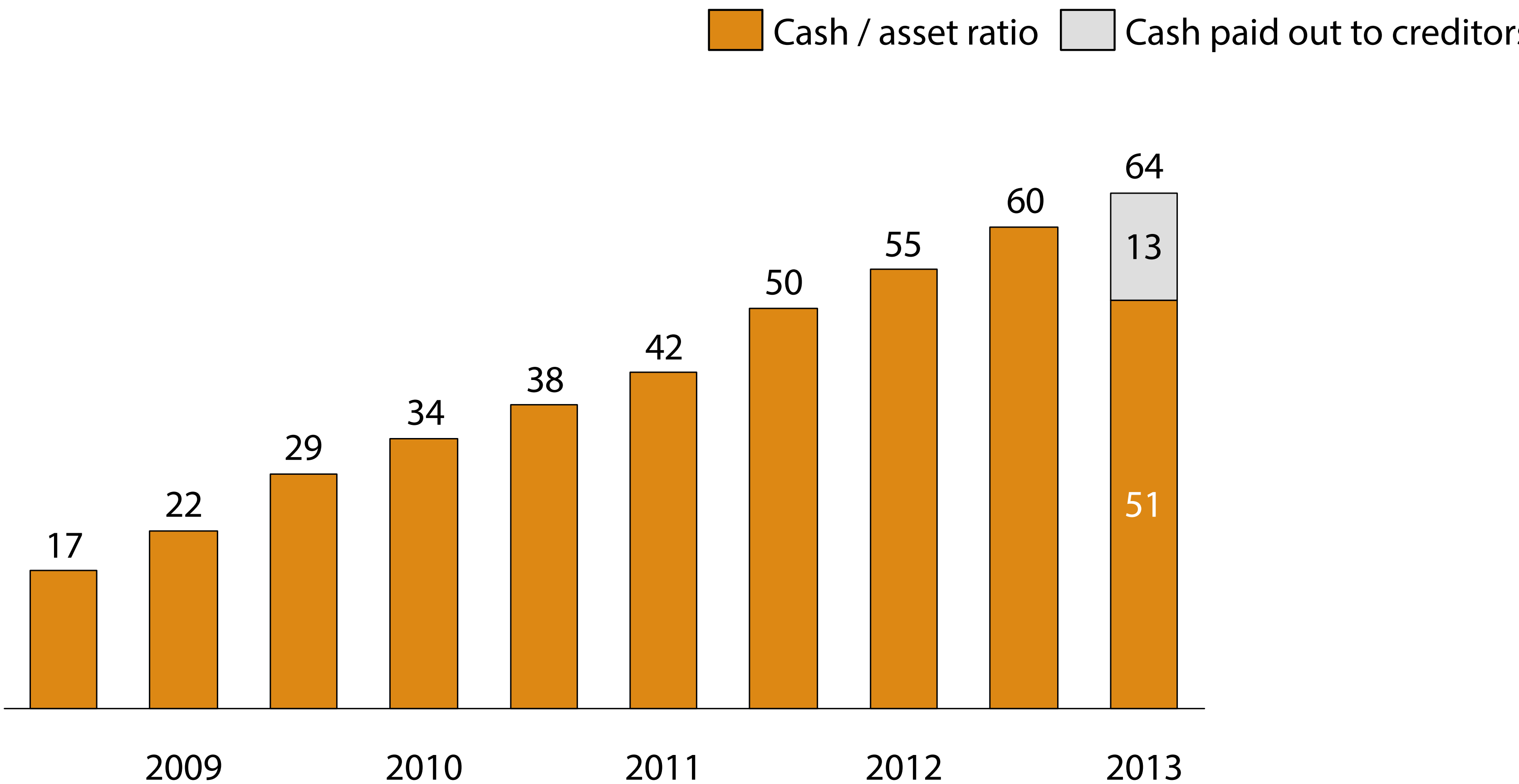
3 Minister of Finance
- Assesses whether the request has a negative impact on the national economy

4 Creditors
- Approve or reject a composition agreement through a voting process in a creditors' meeting

Sources: Central Bank of Iceland; Minister of finance's speech at the CBI annual meeting 2014; ICoC analysis

The resolution committees have liquidated two thirds of the assets, resulting in a lower yield for creditors

Cash / asset ratio of the failed banks‘ estates (%)[1]

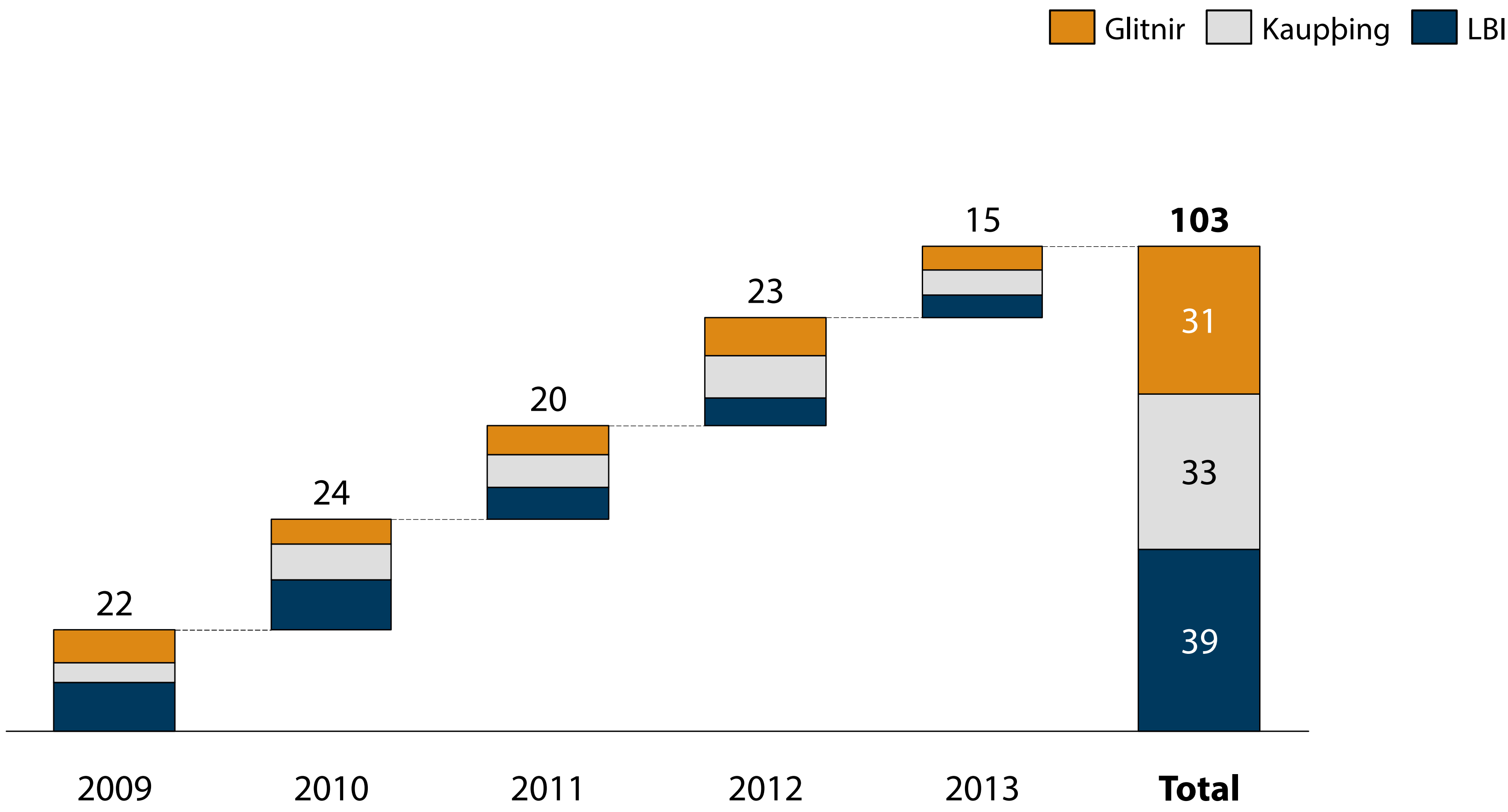


1 Balance at the end of each 6 month period, From H1 2009 to H2 2013. Weighted average of Glitnir, Kaupþing and LBI according to the value of their assets at EOY 2013. 13% of assets has already been paid out to creditors, which is only indicated on the most recent column

Sources: Central Bank of Iceland (Financial Stability 2014/1); ICoC

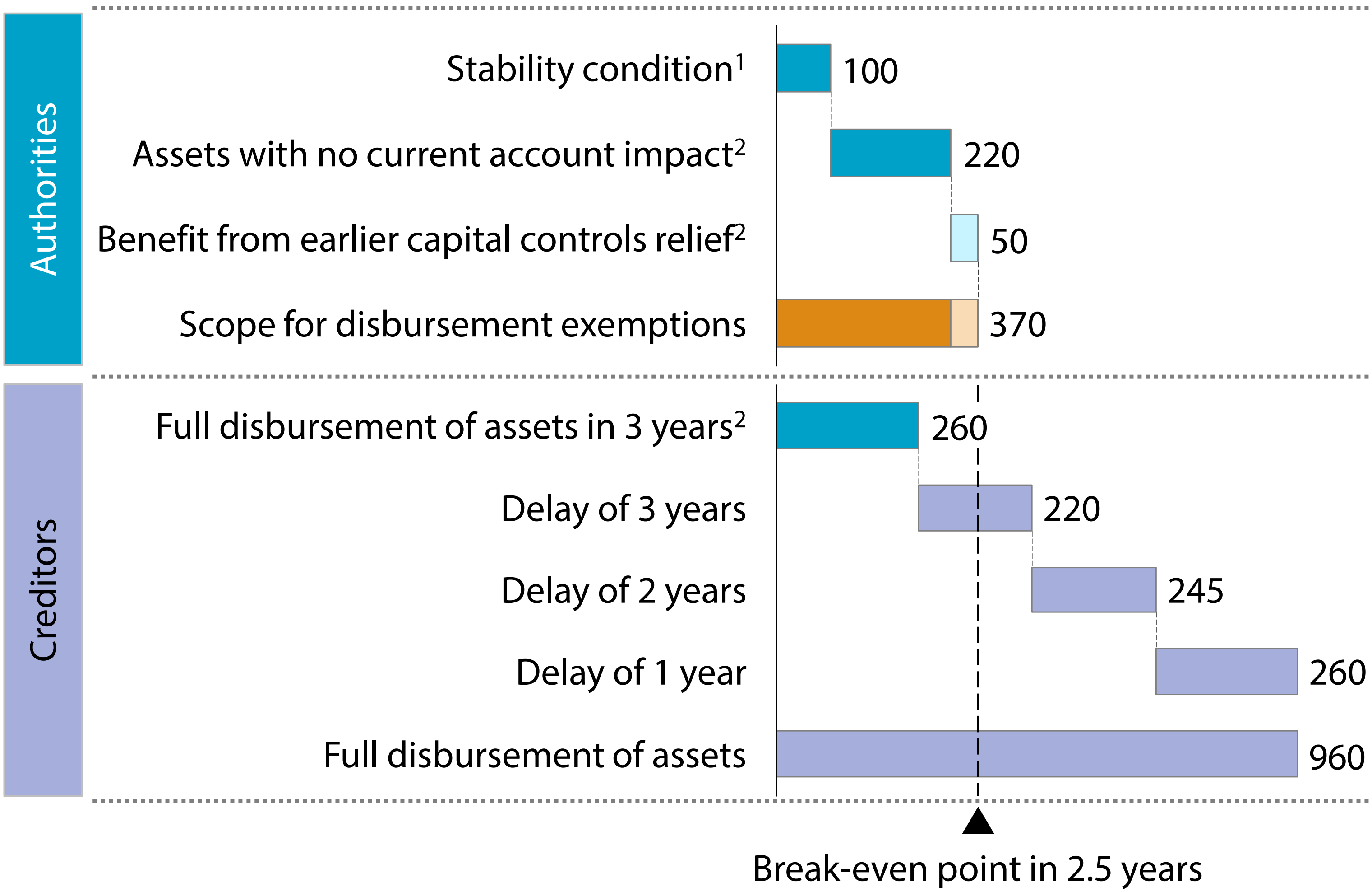
Accumulated operating costs of the estates exceed 100 bn. ISK, further reducing the value of the assets

Operating costs of the failed banks‘ estates (ISK bn., 2014 prices)



Feasible composition agreements require an asset write-down equivalent to additional 2.5 years of delay

Creditor recovery of domestic assets of the estates (ISK bn.)

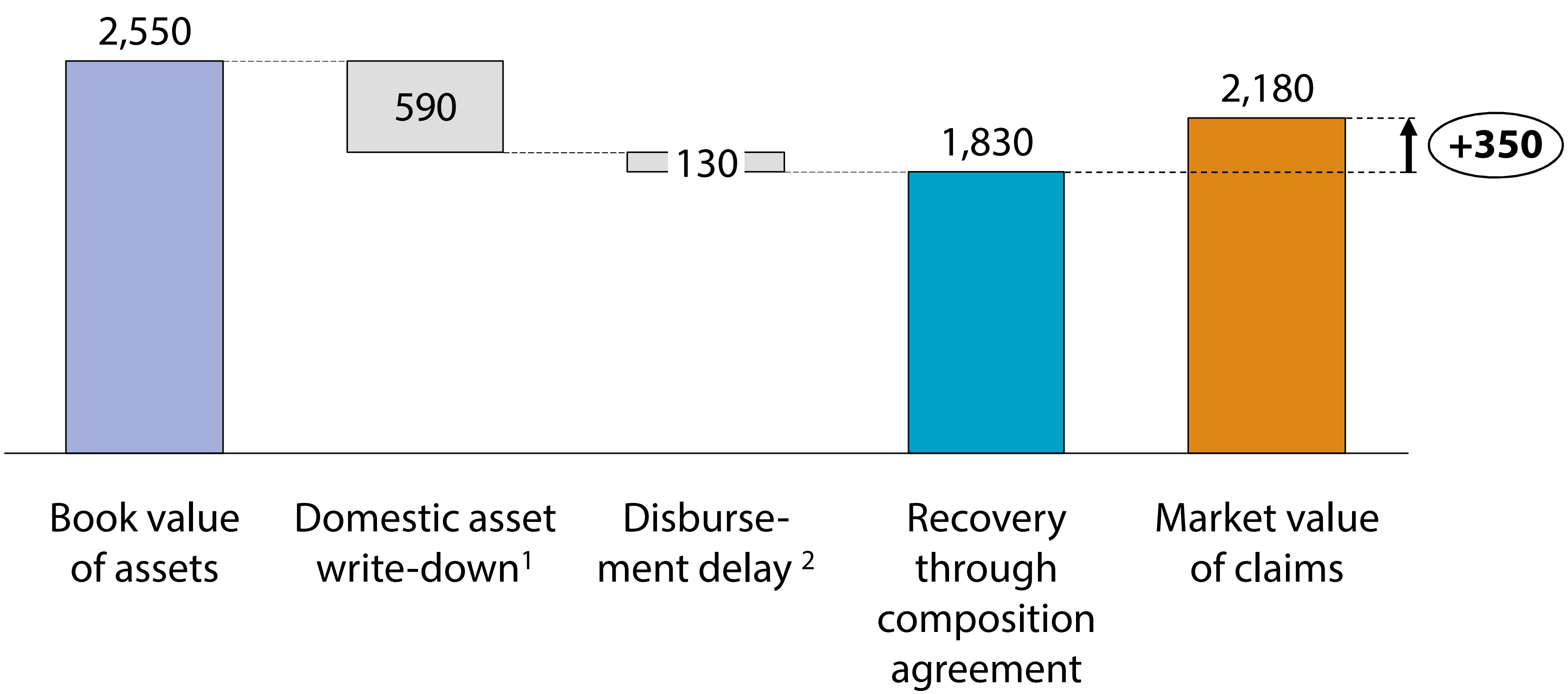


1 The authorities' preconditions for capital controls exemptions are that such esuch exceptions do not negatively impact the balance of payments.
2 Iceland Chamber of Commerce analysis/estimates. Key assumptions can be accessed in Icelandic in the full report.

Sources: Central Bank of Iceland; Minister of finance; Resolution Committees of the Failed Banks' Estates; ICoC estimates

Creditor expectations exceed the estimated scope for authorities to grant exemptions from capital controls

Creditor recovery of all assets of the estates (ISK bn.)

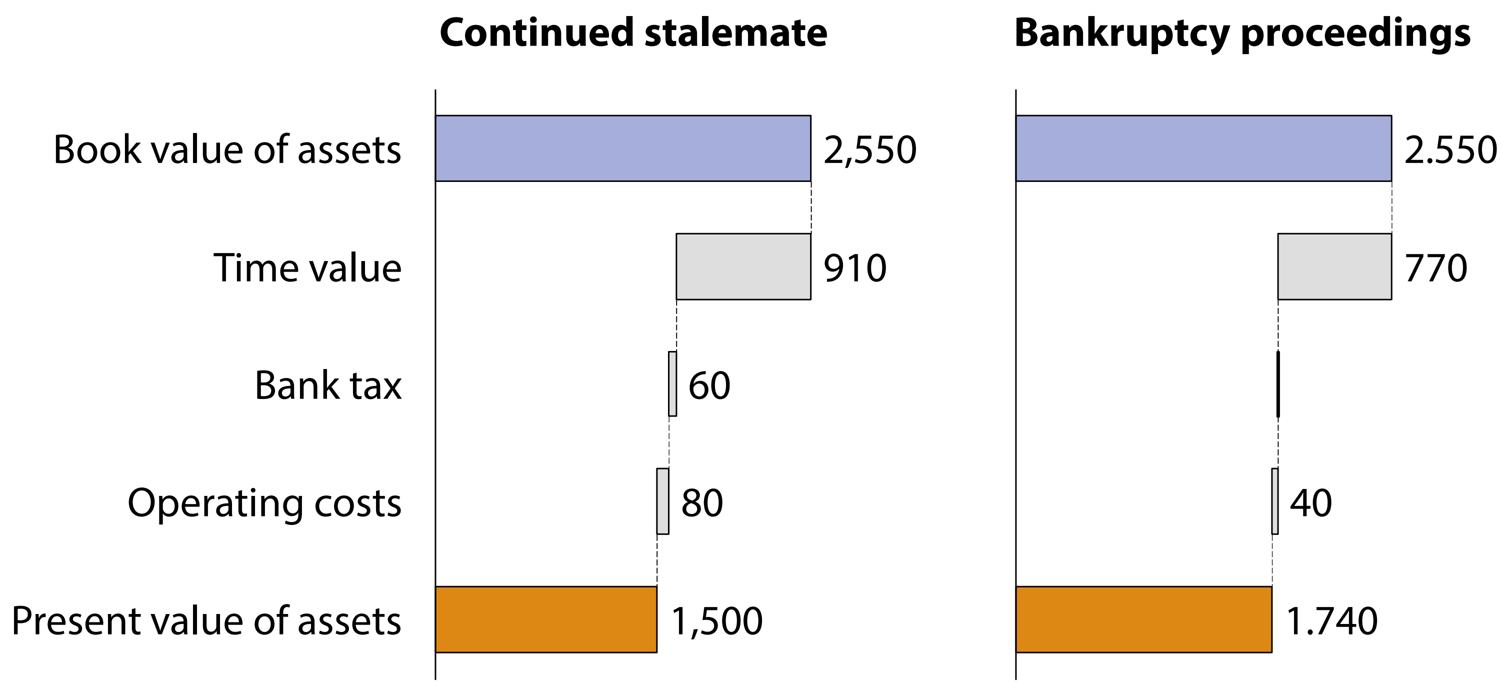


1 Assuming full utilization of the scope for capital controls exemptions
2 Assuming 12% required rate of return and disbursement of assets in 6 months

Sources: Keldan; Central Bank of Iceland; ICoC estimates

Creditors would lose more from a continued stalemate than a disbursement from bankruptcy proceedings

Creditor recovery of all assets of the estates (ISK bn.)[1]

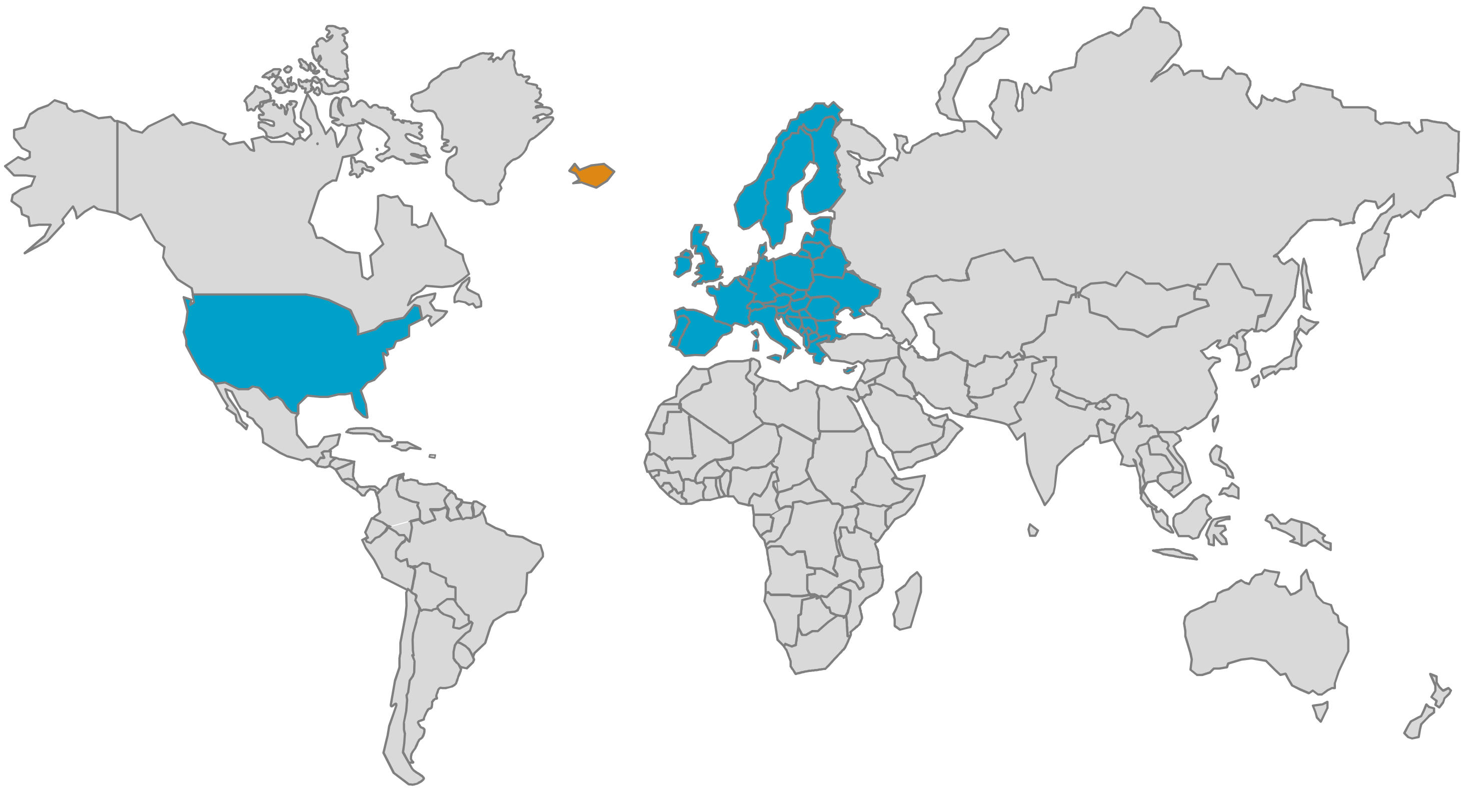


1 Present value of assets. Assuming end of period in mid-year 2019, required rate of return of 12% and a 51% cash to total asset ratio. In the case of continued impasse a 0% return on cash and 5% return on non-cash assets is assumed as well as 49 bn. ISK annual costs from operating costs and bank tax. In the case of bankruptcy proceedings, a 40 bn. ISK operating costs is assumed.

The current winding-up proceedings are protected from creditor intervention in the US and EEA

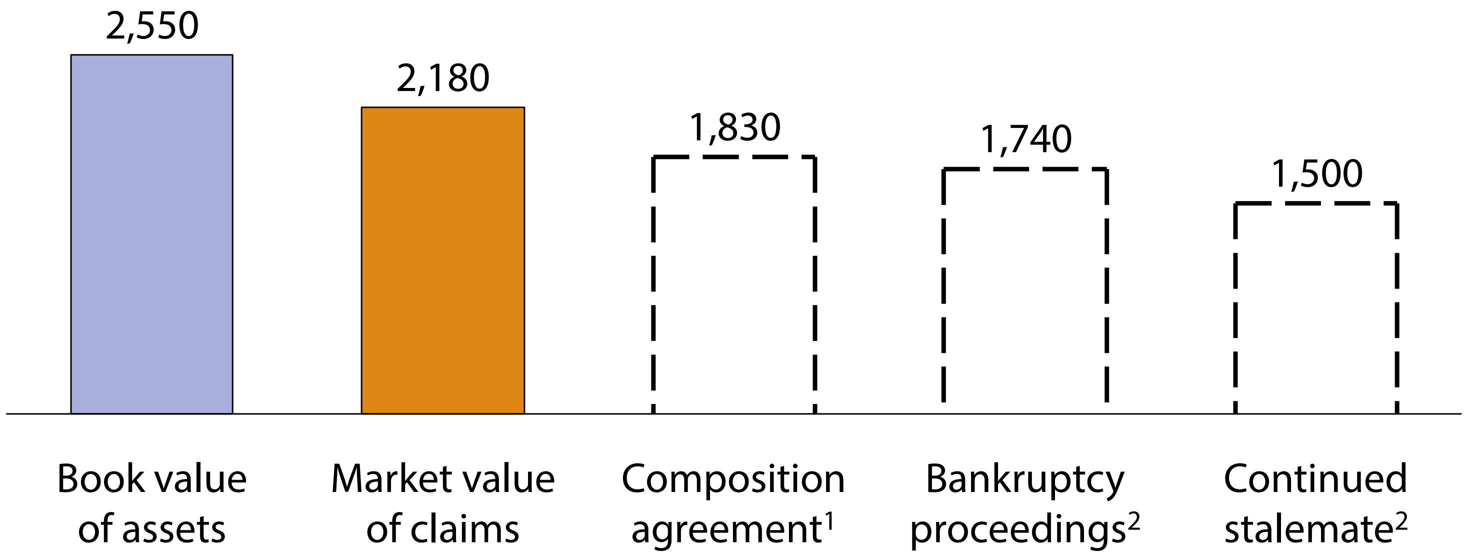
Cash / asset ratio of the failed banks' estates (%)[1]

Legal venue of the estates
Protection from creditor intervention
No assets



A composition agreement within the scope for exemptions is the best option for creditors

Creditor recovery of all assets of the estates (ISK bn.)[1]



1 Assuming full utilisation of the scope for capital controls exemptions and a disbursement of assets in 6 months
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