



# ICELAND

## 2026 ARTICLE IV CONSULTATION—PRESS RELEASE; AND STAFF REPORT

July 2026

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2026 Article IV consultation with Iceland, the following documents have been released and are included in this package:

- A **Press Release**
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on a lapse-of-time basis, following discussions that ended on June 11, 2026, with the officials of Iceland on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on July 10, 2026.
- An **Informational Annex** prepared by the IMF staff.

The documents listed below have been or will be separately released.

### Selected Issues

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

Copies of this report are available to the public from

International Monetary Fund • Publication Services  
PO Box 92780 • Washington, D.C. 20090  
Telephone: (202) 623-7430 • Fax: (202) 623-7201  
E-mail: [publications@imf.org](mailto:publications@imf.org) Web: <http://www.imf.org>

**International Monetary Fund**  
**Washington, D.C.**



## IMF Executive Board Concludes 2026 Article IV Consultation with Iceland

FOR IMMEDIATE RELEASE

- *Tight macroeconomic policies have helped slow domestic demand, but wage growth and inflation remain elevated, raising concerns about a de-anchoring of inflation expectations and erosion of export competitiveness.*
- *The economy is projected to recover, led by a rebound in net trade, while inflation is expected to remain elevated in the near term. Risks to growth are tilted to the downside while risks to inflation are to the upside.*
- *The policy priorities now are to return inflation sustainably to target and increase resilience to shocks by further building fiscal buffers and advancing productivity-enhancing structural reforms.*

**Washington, DC – July 30, 2026:** The Executive Board of the International Monetary Fund (IMF) completed the Article IV Consultation with Iceland<sup>1</sup> and considered and endorsed the staff appraisal on a lapse-of-time basis without a meeting.<sup>2</sup> The authorities have consented to the publication of the Staff Report prepared for this consultation.<sup>3</sup>

Economic activity recovered in 2025, with GDP expanding by 1.3 percent after a 1.3 percent contraction in 2024. Growth was driven primarily by private consumption—supported by strong wage growth—and investment—reflecting a continued expansion of data centers, though leakages to imports were significant. Meanwhile, exports remained subdued in 2025 partly due to a series of idiosyncratic shocks. The labor market has cooled though wage and inflation pressures persist in spite of a broader tightening of policies.

Growth is projected to strengthen to 1.8 percent in 2026 and 2.1 percent in 2027, led by a rebound in net exports as imports normalize, marine exports recover, and data center exports increase, more than offsetting external headwinds from weaker trading-partner growth. Despite a negative output gap, inflation is projected to remain elevated, averaging around 5.2

---

<sup>1</sup> Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

<sup>2</sup> The Executive Board takes decisions under its lapse-of time procedure when the Board agrees that a proposal can be considered without convening formal discussions.

<sup>3</sup> Under the IMF's Articles of Agreement, publication of documents that pertain to member countries is voluntary and requires the member consent. The staff report will be shortly published on the [www.imf.org/Iceland](http://www.imf.org/Iceland) page.

percent in 2026 and 3.2 percent in 2027, before declining toward the 2.5 percent target in early 2028. While medium-term growth prospects remain favorable, risks to growth are tilted to the downside and risks to inflation are to the upside.

### **Executive Board Assessment**

In concluding the 2026 Article IV consultation with Iceland, Executive Directors endorsed the staff's appraisal, as follows:

**Economic activity moderated in recent years, while inflationary pressures remained elevated.** Growth has slowed since mid-2023 amid appropriately tight macroeconomic policies and idiosyncratic shocks, yet inflation, inflation expectations, and wage growth remain elevated. The current account deficit widened in 2025, due to imports for data centers and other idiosyncratic factors. The external position is assessed to be moderately weaker than implied by fundamentals and desirable policies.

**The economy is expected to recover gradually, but risks to growth are tilted to the downside and inflation risks to the upside.** Staff projects growth at 1.8 percent in 2026 and 2.1 percent in 2027, supported by a rebound in net trade and easing financial conditions. Inflation is projected to remain elevated at 5.2 percent in 2026 and 3.2 percent in 2027, before declining toward target in early-2028. Key risks include an escalation of geopolitical tensions, stronger-than-expected wage growth, and disruptions to key export sectors. Medium-term growth prospects remain well-supported by continued diversification towards new export-oriented sectors. Policy priorities are thus to lower inflation sustainably to target, anchor inflation expectations, and increase resilience to shocks by further building fiscal buffers and advancing structural reforms.

**The fiscal stance is appropriately contractionary and the medium-term fiscal targets are appropriately ambitious and should be fully implemented.** The fiscal stance in 2026 and beyond will help lower inflation and build buffers. The temporary reduction in the VAT rate on fuel should remain time-bound and be phased out as planned. Medium-term targets—which place public debt on a firm downward trajectory—are well-calibrated given the economy's exposure to shocks. Longer-term spending pressures from healthcare and infrastructure underscore the importance of sustained discipline and credible medium-term planning, as well as transparent monitoring of credit risk related to below-the-line on-lending. There is scope to raise revenues and reduce spending if needed to meet the MTFS targets, mitigate long-term spending pressures, or scale up infrastructure investment. Options include raising the preferential VAT rate and/or narrowing its coverage, increasing housing-related taxation, streamlining R&D support, and further rationalizing public spending, including through spending efficiency and public sector wage restraint. Plans to establish a state-owned infrastructure company could help mobilize financing, but should have strong safeguards to contain fiscal risks, including careful monitoring and transparent recording of contingent liabilities and off-balance-sheet exposures.

**Strengthening the fiscal framework would boost the credibility of the consolidation effort.** The amended fiscal rule should help contain spending over the medium term and reduce procyclicality. The authorities' efforts to strengthen the Fiscal Council are welcome, but a meaningful increase in its capacity and resources will be needed. Regular publication of timely and independently-verifiable quarterly fiscal data consistent with the fiscal-rule perimeter would further strengthen transparency and accountability. Expanding the coverage

of the budget and the fiscal rules to encompass the entirety of the central government would also improve transparency.

**The monetary policy stance remains appropriately restrictive, but vigilance is warranted alongside clear and forceful communication.** Further tightening may be needed in the near term if inflationary pressures persist or intensify and policy should remain restrictive until inflation and inflation expectations are firmly anchored at target. Strengthening communication, including using alternative scenarios, would help enhance transparency and anchor expectations. As uncertainty recedes, a gradual transition toward a more forecast-based inflation targeting framework would improve predictability and reduce volatility.

**Reserves are adequate for precautionary purposes.** Further strengthening of foreign exchange reserves toward the upper end of the Fund's ARA range would enhance resilience to external shocks, while efforts to deepen the foreign exchange market would support broader market participation and improve hedging opportunities.

**Systemic risks in the financial sector are contained and the current macroprudential stance is broadly appropriate.** Banks remain well-capitalized, profitable, and liquid, with strong asset quality. However, vulnerabilities in parts of the corporate sector—notably construction and tourism-related activities—require vigilance. Borrower-based measures should remain broadly unchanged for now, especially given the slowing housing market. Efforts to reduce reliance on CPI-indexed mortgages may strengthen monetary transmission over time, but should be carefully timed and sequenced given their role in supporting borrower resilience and financial stability.

**Financial sector reforms should build on the significant progress achieved in implementing FSAP recommendations.** Remaining priorities include strengthening pension fund governance and safeguarding the independence of financial supervision. Efforts to strengthen operational resilience, including against cyber and payments-related risks, remain essential.

**Structural reforms should focus on raising productivity and further diversification.** Priorities include reducing regulatory barriers and streamlining licensing and permitting processes; addressing skills shortages through education reform, vocational training, and improved reskilling; reforming wage-setting arrangements to better align wage growth with productivity and the inflation target; closing infrastructure gaps; and improving the efficiency of R&D support while strengthening the broader innovation ecosystem. The authorities' recent Growth Plan to 2035 is well aligned with these priorities, and successful implementation will require strong cross-ministerial coordination, prioritization, monitoring and reporting.

**EU accession and euro adoption are ultimately political choices that involve balancing deeper integration and potential credibility gains against reduced macroeconomic policy autonomy.** While EU membership and euro adoption could deepen integration and potentially enhance policy credibility, it would result in the loss of independent monetary policy and exchange rate flexibility. Should the process move forward, maintaining low inflation, sound public finances, and an exchange rate aligned with fundamentals, while advancing structural reforms to increase productivity and aligning wages with productivity, will be critical to safeguard stability and competitiveness.

Table 1. Iceland: Selected Economic Indicators, 2021–31

|                                                | 2021                                           | 2022   | 2023   | 2024   | 2025   | 2026   | 2027   | 2028   | 2029   | 2030   | 2031   |
|------------------------------------------------|------------------------------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
|                                                | Projections                                    |        |        |        |        |        |        |        |        |        |        |
|                                                | (Percentage change unless otherwise indicated) |        |        |        |        |        |        |        |        |        |        |
| National Accounts (constant prices)            |                                                |        |        |        |        |        |        |        |        |        |        |
| Gross domestic product                         | 5.2                                            | 8.9    | 5.0    | -1.3   | 1.3    | 1.8    | 2.1    | 2.4    | 2.4    | 2.4    | 2.4    |
| Total domestic demand                          | 7.9                                            | 8.0    | 2.5    | 1.4    | 3.9    | 0.4    | 2.1    | 2.4    | 2.5    | 2.5    | 2.5    |
| Private consumption                            | 8.1                                            | 7.6    | 0.4    | 0.9    | 4.3    | 1.7    | 2.1    | 2.5    | 2.5    | 2.5    | 2.5    |
| Public consumption                             | 2.5                                            | 1.7    | 2.4    | 1.8    | 1.2    | 1.5    | 1.5    | 1.5    | 1.5    | 1.5    | 1.5    |
| Gross fixed investment                         | 13.5                                           | 15.3   | 6.2    | 6.5    | 4.0    | -2.9   | 2.7    | 3.2    | 3.6    | 3.6    | 3.6    |
| Net exports (contribution to growth)           | -2.8                                           | 0.6    | 2.5    | -2.6   | -2.7   | 1.4    | -0.1   | -0.1   | -0.2   | -0.2   | -0.3   |
| Exports of goods and services                  | 12.4                                           | 26.1   | 3.9    | -2.2   | 1.0    | 0.5    | 4.0    | 3.5    | 3.2    | 3.1    | 3.1    |
| Imports of goods and services                  | 20.3                                           | 22.6   | -1.9   | 4.2    | 7.2    | -2.4   | 3.8    | 3.5    | 3.4    | 3.4    | 3.4    |
| Output gap (percent of potential output)       | -3.8                                           | 1.6    | 3.6    | 0.3    | -0.1   | -0.3   | -0.3   | -0.1   | 0.0    | 0.0    | 0.0    |
| Selected Indicators                            |                                                |        |        |        |        |        |        |        |        |        |        |
| Gross domestic product (ISK bn.)               | 3,332                                          | 3,947  | 4,373  | 4,578  | 4,956  | 5,351  | 5,645  | 5,937  | 6,259  | 6,590  | 6,937  |
| Gross domestic product (\$ Mn.)                | 26,235                                         | 29,176 | 31,702 | 33,187 | 38,583 | 43,664 | 46,316 | 48,777 | 51,189 | 53,619 | 56,153 |
| GDP per capita (\$ thousands)                  | 73.2                                           | 80.0   | 84.5   | 86.5   | 99.1   | 109.7  | 114.0  | 117.6  | 121.0  | 124.2  | 127.5  |
| Private consumption (percent of GDP)           | 51.2                                           | 49.8   | 48.7   | 49.1   | 49.6   | 49.2   | 49.1   | 49.1   | 48.9   | 48.9   | 48.8   |
| Public consumption (percent of GDP)            | 27.4                                           | 25.5   | 25.2   | 25.9   | 26.1   | 26.0   | 26.0   | 26.0   | 25.9   | 25.8   | 25.7   |
| Gross fixed investment (percent of GDP)        | 22.5                                           | 23.8   | 24.9   | 26.8   | 26.7   | 24.6   | 24.8   | 25.0   | 25.2   | 25.4   | 25.6   |
| Gross national saving (percent of GDP)         | 20.2                                           | 22.5   | 24.2   | 23.0   | 23.0   | 23.3   | 24.0   | 24.5   | 25.0   | 25.5   | 25.8   |
| Unemployment rate (percent of labor force)     | 5.8                                            | 3.6    | 3.4    | 3.4    | 4.3    | 4.3    | 4.2    | 4.0    | 4.0    | 4.0    | 4.0    |
| Employment                                     | 3.4                                            | 7.0    | 3.6    | 4.1    | -0.6   | -0.4   | 0.6    | 1.1    | 1.1    | 1.1    | 0.0    |
| Labor productivity                             | 1.7                                            | 1.7    | 1.4    | -5.1   | 1.9    | 2.2    | 1.5    | 1.3    | 1.3    | 1.3    | 1.3    |
| Real wages                                     | 3.7                                            | 0.0    | 0.9    | 0.7    | 3.7    | 1.2    | 1.2    | 1.4    | 1.3    | 1.3    | 1.3    |
| Nominal wages                                  | 8.3                                            | 8.3    | 9.8    | 6.6    | 7.9    | 6.5    | 4.5    | 3.9    | 3.9    | 3.8    | 3.8    |
| Consumer price index (average)                 | 4.5                                            | 8.3    | 8.7    | 5.9    | 4.1    | 5.2    | 3.2    | 2.5    | 2.5    | 2.5    | 2.5    |
| Consumer price index (end period)              | 5.1                                            | 9.6    | 7.7    | 4.7    | 4.5    | 5.1    | 2.6    | 2.5    | 2.5    | 2.5    | 2.5    |
| Core CPI (average)                             | 4.3                                            | 7.6    | 8.6    | 6.1    | 4.2    | 6.1    | 2.7    | 2.5    | 2.5    | ...    | ...    |
| ISK/€ (average)                                | 148                                            | 159    | 163    | 164    | 152    | ...    | ...    | ...    | ...    | ...    | ...    |
| ISK/\$ (average)                               | 127                                            | 135    | 138    | 138    | 128    | ...    | ...    | ...    | ...    | ...    | ...    |
| Terms of trade (average)                       | 4.0                                            | 2.1    | -4.9   | 1.7    | 3.4    | 3.1    | -0.7   | -0.3   | 0.4    | 0.1    | 0.1    |
| Money and Credit (end period)                  |                                                |        |        |        |        |        |        |        |        |        |        |
| Base money (M0)                                | 9.0                                            | 1.5    | -21.5  | 16.7   | 2.9    | 13.5   | 11.8   | 10.9   | 9.9    | 9.2    | 8.7    |
| Broad money (M3)                               | 10.9                                           | 8.9    | 8.3    | 11.7   | 5.6    | 10.9   | 9.5    | 7.6    | 6.7    | 6.2    | 5.9    |
| Credit to nonfinancial private sector          | 10.5                                           | 11.3   | 5.2    | 8.1    | 5.3    | 5.9    | 7.0    | 6.3    | 5.7    | 5.3    | 5.2    |
| Central bank 7 day term deposit rate 1/        | 2.00                                           | 6.00   | 9.25   | 8.50   | 7.25   | 7.75   | ...    | ...    | ...    | ...    | ...    |
| (Percent of GDP unless otherwise indicated)    |                                                |        |        |        |        |        |        |        |        |        |        |
| General Government Finances 2/3/               |                                                |        |        |        |        |        |        |        |        |        |        |
| Revenue                                        | 40.7                                           | 42.3   | 43.1   | 42.9   | 42.6   | 43.2   | 43.6   | 43.7   | 43.8   | 43.8   | 43.8   |
| Expenditure 4/                                 | 48.7                                           | 46.2   | 45.2   | 47.1   | 45.0   | 44.7   | 44.2   | 44.1   | 44.0   | 43.9   | 43.8   |
| Overall balance 4/                             | -8.0                                           | -3.8   | -2.1   | -4.2   | -2.4   | -1.4   | -0.6   | -0.4   | -0.2   | -0.1   | 0.0    |
| Cyclically-adjusted primary balance            | -3.7                                           | -1.3   | -0.8   | -1.2   | 0.5    | 1.7    | 2.2    | 2.1    | 2.2    | 2.3    | 2.3    |
| Structural primary balance 5/                  | -0.3                                           | 0.1    | -0.2   | 0.9    | 0.9    | 2.0    | 2.3    | 2.1    | 2.3    | 2.3    | 2.3    |
| Gross debt                                     | 73.6                                           | 66.4   | 61.5   | 60.4   | 56.1   | 54.7   | 53.2   | 52.3   | 50.7   | 49.3   | 48.2   |
| Net debt                                       | 58.8                                           | 55.3   | 52.1   | 50.4   | 45.8   | 45.1   | 44.2   | 43.7   | 42.5   | 41.5   | 40.8   |
| Balance of Payments                            |                                                |        |        |        |        |        |        |        |        |        |        |
| Current account balance                        | -2.6                                           | -1.7   | -1.2   | -3.2   | -3.6   | -1.3   | -0.8   | -0.5   | -0.1   | 0.1    | 0.2    |
| of which: services balance                     | 2.5                                            | 5.6    | 7.4    | 5.8    | 5.5    | 5.2    | 5.3    | 5.8    | 6.4    | 6.8    | 7.2    |
| Capital and financial account (+ = outflow)    | -0.5                                           | -1.0   | -3.0   | 0.0    | 2.4    | -1.3   | -0.8   | -0.5   | -0.1   | 0.1    | 0.2    |
| of which: direct investment, net (+ = outflow) | -1.7                                           | -3.9   | -4.8   | -7.6   | -1.9   | -3.2   | -3.2   | -3.2   | -3.2   | -3.0   | -3.0   |
| Gross external debt                            | 83.1                                           | 74.3   | 73.7   | 67.9   | 61.7   | 56.0   | 54.2   | 52.8   | 51.5   | 50.4   | 49.3   |
| Central bank reserves (\$ Mn.)                 | 7,091                                          | 5,879  | 5,720  | 6,387  | 7,643  | 7,916  | 8,248  | 8,565  | 8,978  | 9,308  | 9,642  |

Sources: Central Bank of Iceland; Ministry of Finance; Statistics Iceland; and IMF staff projections.

1/ For 2026, policy rate as of the May MPC meeting.

2/ In April 2025, an agreement was reached on the settlement of remaining outstanding liabilities in the IL Fund (HFF).

3/ There is large uncertainty on the 2025 fiscal outcome, and numbers may be revised.

4/ Costs related to the purchase of houses in Grindavík (1.2 percent of GDP) that in the 2024 Article IV were classified below the line are now classified above the line due to uncertainty about the future value of these properties.

5/ Cyclically-adjusted primary balance excluding one offs.



# ICELAND

## STAFF REPORT FOR THE 2026 ARTICLE IV CONSULTATION

July 10, 2026

### KEY ISSUES

**Context.** Tight macroeconomic policies have helped slow domestic demand, but wage growth and inflation remain elevated, raising concerns about a de-anchoring of inflation expectations and erosion of export competitiveness. The priorities now are to return inflation to target, strengthen fiscal resilience, and advance productivity-enhancing reforms to support sustained gains in living standards and enhance resilience to shocks.

**Economic Developments and Outlook.** Growth has slowed since mid-2023, amid tight macro policies, slower labor inflows, and idiosyncratic shocks. The economy is expected to recover gradually despite headwinds due to the war in the Middle East, while inflation is projected to remain elevated amid strong wage growth. The medium-term outlook is favorable under the baseline, though subject to increased risks related to future labor inflows, competitiveness, and the sustainability of new higher value-added sectors. Overall, risks to growth are tilted to the downside and inflation risks to the upside.

**Monetary Policy.** While the monetary policy stance remains appropriately restrictive, further tightening may be needed in the near term to contain inflationary pressures. Once inflation begins to decline, a gradual easing would be appropriate, though the monetary policy stance should remain restrictive until inflation and inflation expectations—persistently above target since 2021—are firmly anchored at the target. Clear and forceful communication should reinforce policy actions.

**Fiscal Policy.** The envisaged fiscal consolidation will support disinflation and help rebuild buffers. Over the medium term, the pace of debt reduction may be balanced against the need to scale up public investment to support growth, while ensuring that fiscal risks are carefully contained and transparently recorded. Measures to mitigate the impact of the war in the Middle East should be phased out as planned.

**Financial Policies.** The banking system remains resilient. While the financial cycle is easing due to the cooling housing market and declining credit growth, the current tight macroprudential policy stance remains appropriate given pockets of vulnerabilities: notably in construction and tourism-related sectors—and ample supply of credit.

**Structural Policies.** As tourism is maturing, sustaining gains in living standards will require diversification toward higher value-added sectors and stronger productivity growth. Priorities include enhancing competition and business dynamism, boosting innovation and skills, and alleviating infrastructure bottlenecks.

Approved By  
**Kristina Kostial (EUR)**  
**and Cemile Sancak (SPR)**

The mission took place virtually May 26–29 and in Reykjavik during June 2–11, 2026. The team comprised Metodij Hadzi-Vaskov (head), Thomas Gade, Amit Kara, and Harri Kemp (all EUR). Magnus Saxegaard (WHD) joined the virtual meetings. Rogelio Celaya and Caitlin Aingé (EUR) supported the mission. Ragnheidur Jonsdottir (OED) joined the discussions. The mission met with Prime Minister Kristrún Frostadóttir, CBI Governor Ásgeir Jónsson, Minister of Finance Daði Már Kristófersson, and other representatives of the public and private sectors.

## CONTENTS

|                                           |           |
|-------------------------------------------|-----------|
| <b>CONTEXT</b>                            | <b>4</b>  |
| <b>RECENT ECONOMIC DEVELOPMENTS</b>       | <b>4</b>  |
| <b>OUTLOOK AND RISKS</b>                  | <b>9</b>  |
| <b>POLICY DISCUSSIONS</b>                 | <b>11</b> |
| A. Monetary Policy                        | 11        |
| B. Fiscal Policy                          | 13        |
| C. Financial Sector Policies              | 17        |
| D. Structural Policies                    | 19        |
| <b>STAFF APPRAISAL</b>                    | <b>22</b> |
| <b>FIGURES</b>                            |           |
| 1. Real Sector Developments               | 25        |
| 2. Labor Market Developments              | 26        |
| 3. Fiscal Developments and Issues         | 27        |
| 4. External Sector Developments           | 28        |
| 5. Banking Sector Developments            | 29        |
| 6. Housing Market Developments            | 30        |
| 7. Structural Developments                | 31        |
| <b>TABLES</b>                             |           |
| 1. Selected Economic Indicators, 2021–31  | 32        |
| 2. Money and Banking, 2021–31             | 33        |
| 3. General Government Operations, 2021–31 | 34        |

|                                                        |    |
|--------------------------------------------------------|----|
| 4. General Government Financial Balance Sheet, 2021–31 | 35 |
| 5. Balance of Payments, 2021–31                        | 36 |
| 6. International Investment Position, 2015–25          | 37 |
| 7. Financial Soundness Indicators, 2016–25             | 37 |

## ANNEXES

|                                                                                                                                       |    |
|---------------------------------------------------------------------------------------------------------------------------------------|----|
| I. External Sector Assessment                                                                                                         | 38 |
| II. Risk Assessment Matrix                                                                                                            | 41 |
| III. Sovereign Risk and Debt Sustainability Assessment                                                                                | 44 |
| IV. Previous Article IV Recommendations                                                                                               | 52 |
| V. Update on the Implementation of FSAP Recommendations                                                                               | 55 |
| VI. Data Issues                                                                                                                       | 63 |
| VII. Observations from Benchmarking of Public Spending                                                                                | 66 |
| VIII. Pros and Cons of the Choice of Exchange Rate Regime for Iceland in the Context of Possibly Restarting EU Accession Negotiations | 71 |

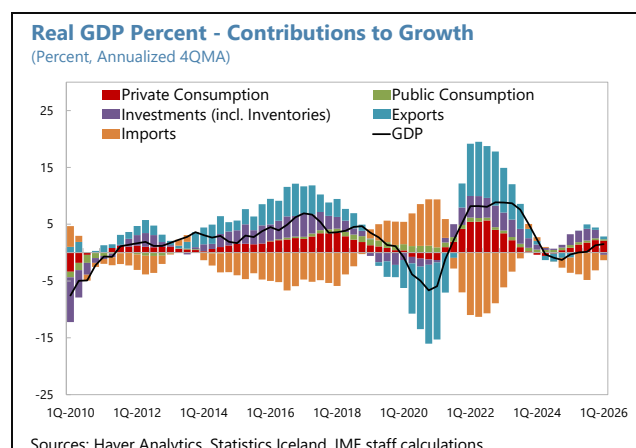
## CONTEXT

- 1. Following a decade of strong growth, economic activity has weakened amid persistently high inflation, raising concerns about competitiveness and medium-term growth prospects.** Growth over the past decade averaged 2.8 percent—among the highest in advanced economies—driven largely by labor-intensive sectors such as tourism and construction. However, productivity growth and gains in living standards have been more modest, with GDP per capita growth averaging 0.9 percent over the same period. Since mid-2023, growth has slowed sharply amid tight macroeconomic policies and idiosyncratic shocks. Despite this, wage growth and inflation remain elevated, partly due to sticky expectations, raising concerns about the future inflation path and erosion in export competitiveness. Together with weaker labor inflows amid the waning tourism boom and uncertainty about the sustainability of new higher value-added sectors, this has increased risks to Iceland's medium-term growth outlook.
- 2. The challenge is to lower inflation sustainably to target and increase resilience to shocks by building fiscal buffers and advancing structural reforms.** Against the backdrop of rising global energy prices and the economy's susceptibility to shocks, a tight macroeconomic policy stance remains appropriate to prevent further entrenching de-anchored inflation expectations while increasing fiscal buffers. Continued efforts are needed to diversify the economy and strengthen productivity to support sustained gains in living standards and enhance resilience. These priorities have also gained importance given the decision to hold a referendum in August 2026 on resuming EU membership negotiations and potential euro adoption, which would increase reliance on sound fiscal policy, wage moderation, and productivity-enhancing structural reforms to maintain macroeconomic stability and competitiveness.

## RECENT ECONOMIC DEVELOPMENTS

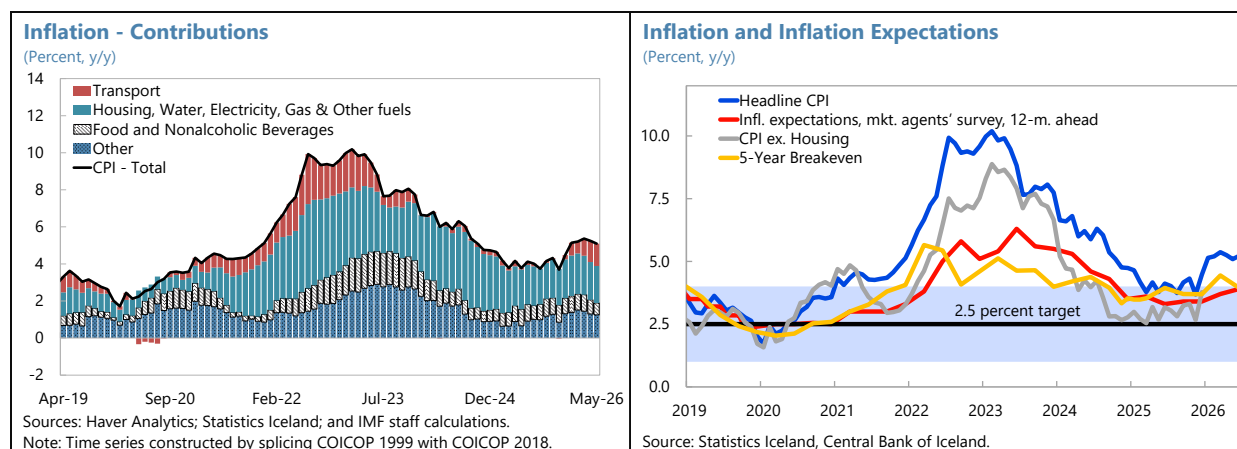
*Economic activity has remained subdued amid a restrictive macroeconomic policy stance and idiosyncratic shocks. However, macroeconomic imbalances persist, with inflation still above target, wage growth elevated, and the current account deficit widening.*

- 3. Economic activity recovered in 2025, with GDP expanding by 1.3 percent after a 1.3 percent contraction in 2024.** Growth was driven primarily by private consumption—supported by strong wage growth—and investment—reflecting a continued expansion of data centers, though leakages to imports were significant. Meanwhile, exports remained subdued in 2025 partly due to a series of idiosyncratic shocks, including the bankruptcy of Play Airlines, disruptions to aluminum production,

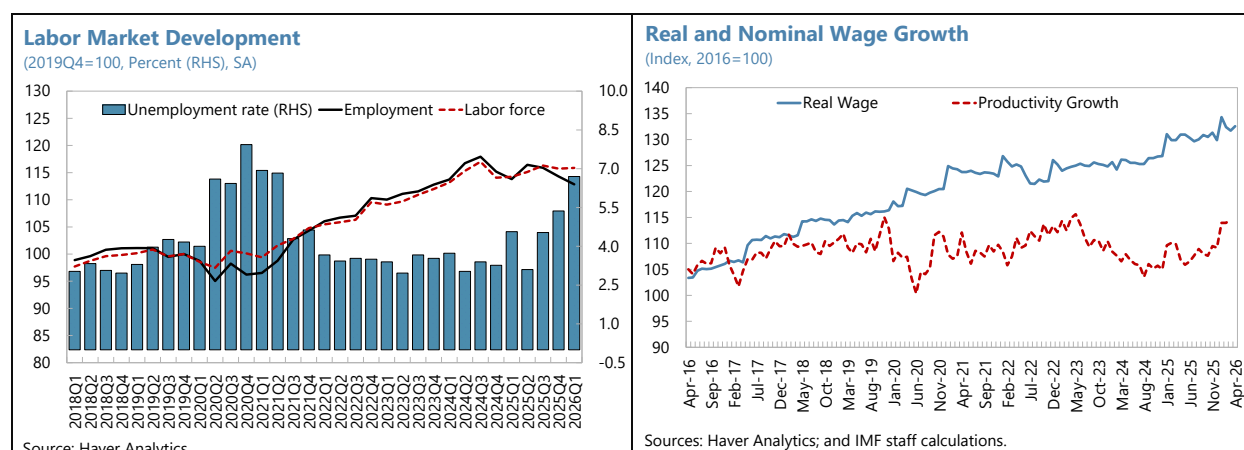


and a disappointing fishing season. The sharp increase in fish catch in January-May 2026—close to 20 percent year-over-year—points to a rebound in the sector.

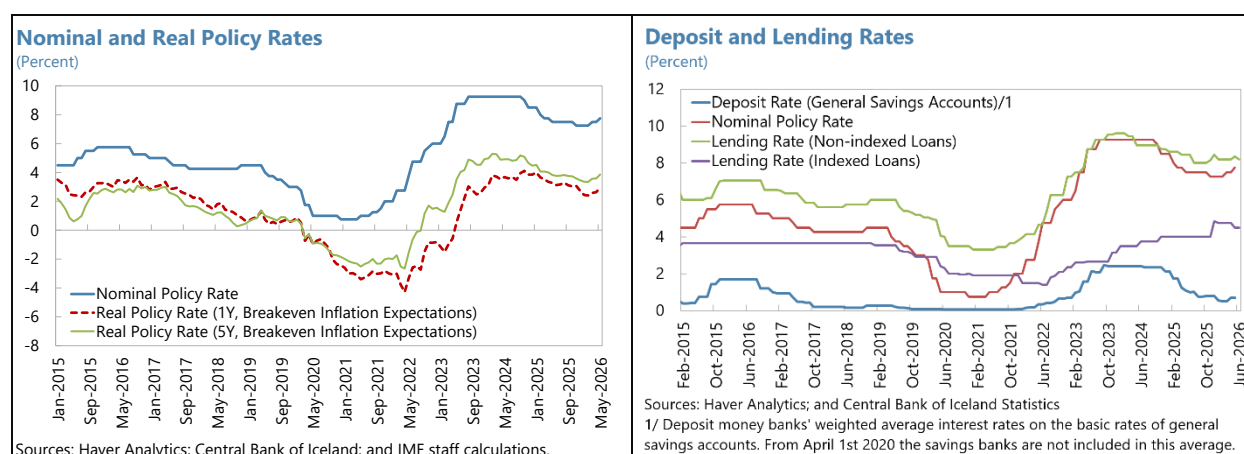
**4. Inflation has increased and is well above the Central Bank of Iceland's (CBI's) 2.5 percent target, while inflation expectations remain elevated.** Inflation declined to 4.1 percent in 2025 but increased in January following tax hikes on fuel and vehicles and has remained elevated at 5.2 percent in June mainly due to transport costs. Underlying inflationary pressures remain elevated, reflecting rapid wage growth and persistent housing cost pressures. While five-year break-even inflation expectations eased somewhat in 2025, they have risen again more recently and remain elevated at 4 percent in June, also reflecting a history of above-target inflation.



**5. The labor market has cooled though wage pressures persist.** The unemployment rate (3m/3m) rose to 5.4 percent at end-2025—above the estimated 4.1 percent neutral rate—reflecting a drop in employment that more than offset a contraction in the labor force, and increased further to 5.8 percent in April. The contraction of the labor force despite continued population growth provides further evidence of labor market slack. Nominal wage growth accelerated to 7.9 percent in 2025 despite lower inflation, partly reflecting the timing of public sector wage settlements that led many workers to receive multiple wage settlements during the year. As a result, real wage growth jumped to 3.7 percent, outpacing productivity growth. Wage pressures have eased somewhat since then but remain elevated.



**6. Monetary policy has been tightened further in response to increasing inflationary pressures.** The CBI raised the policy rate in March and May (by 25 bps each) to 7.75 percent, citing persistently high inflation, elevated inflation expectations, and the increase in commodity prices. These increases follow a cumulative 200 bps easing since October 2024. The monetary stance remains tight, with a real policy rate of around 3.9 percent—above the estimated 2.7 percent neutral real rate—although the prevalence of CPI-indexed loans (54 percent of outstanding household debt) has cushioned the impact of high nominal rates on borrowers.<sup>1</sup>

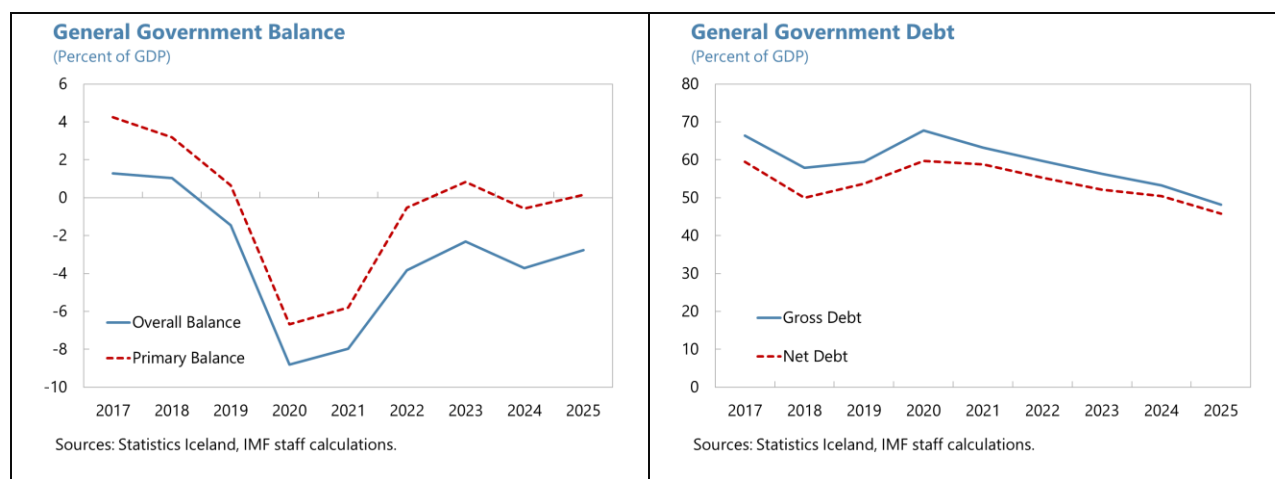


**7. Fiscal consolidation is broadly on track despite uncertainty about the size of the 2025 deficit.** Preliminary data suggest the general government deficit declined to 2.4 percent of GDP in 2025 from 4.2 percent in 2024, largely due to the expiry of one-off measures related to the volcanic activity on the Reykjanes peninsula and new revenue measures.<sup>2</sup> The 2025 outcome is subject to significant uncertainty, however, with high-frequency fiscal data and top-down estimates

<sup>1</sup> For details on indexation in Iceland see [CBI Economic Affairs](#).

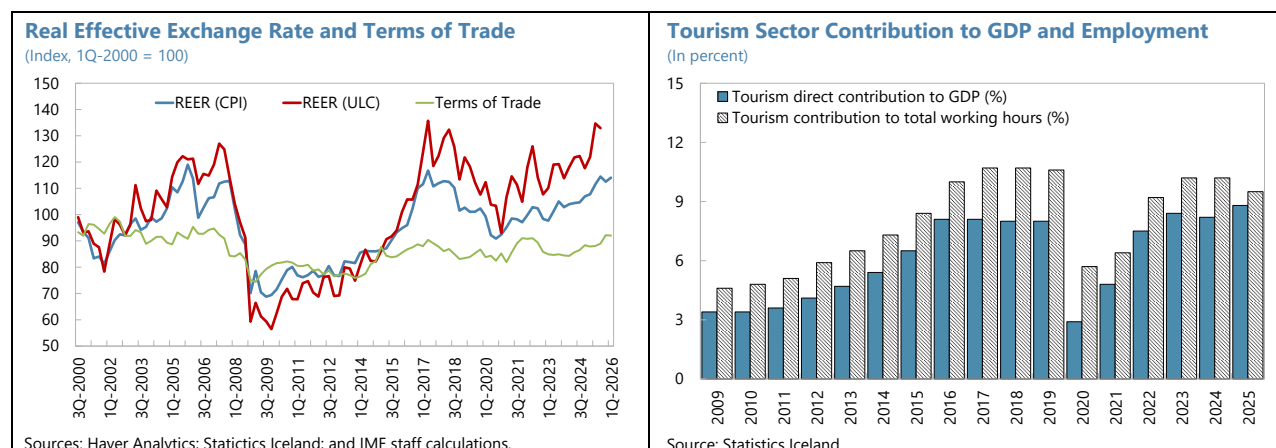
<sup>2</sup> In the wake of the volcanic activity, the government and main lenders set up a Special Purpose Vehicle (SPV) to purchase properties in Grindavík, which had become uninhabitable.

suggesting the deficit may be revised further down. Public debt declined to 56.1 percent of GDP from 76.1 percent in 2020.<sup>3</sup>



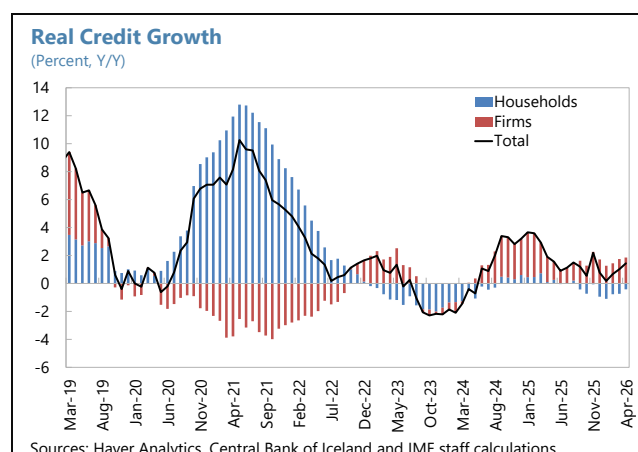
**8. The current account deficit has widened amid weaker exports and strong imports.** The current account has remained in deficit since 2021. The deficit widening to 3.6 percent of GDP in 2025 reflected a surge in imports of computer equipment and vehicles, and subdued exports. This was partly offset by an improvement in the terms of trade—driven by higher marine and aluminum prices—and a strengthening of the primary income balance due to lower dividend and retained earnings outflows. Iceland's external position is assessed to be moderately weaker than the level implied by fundamentals and desirable policies, largely due to a negative trade balance (Annex I). Both the CPI- and ULC-based real effective exchange rate (REER) appreciated modestly in 2025 and have risen by 50 and 100 percent, respectively, since 2010. This coincides with the emergence of tourism as a key export sector, with its contribution to GDP more than doubling from 3.4 percent in 2010 to 8.7 percent in 2024 and the employment share rising from 4.8 percent to 9.9 percent over the same period. While the appreciating REER has thus far not been associated with a deterioration in Iceland's external position—the current account averaged 1.6 percent of GDP between 2010 and 2024—competitiveness pressures could emerge as growth in the tourism sector moderates and future growth increasingly depends on the development of higher value-added export sectors.

<sup>3</sup> Public debt at end-2025 was significantly higher than projected in the 2025 Article IV consultation—47.7 percent of GDP—mainly due to a smaller-than-anticipated impact of the settlement of securities issued by the Housing Finance Fund (HFF) of around 5 percent of GDP on general government debt.



## 9. Credit growth has weakened amid tight financial conditions. Household credit

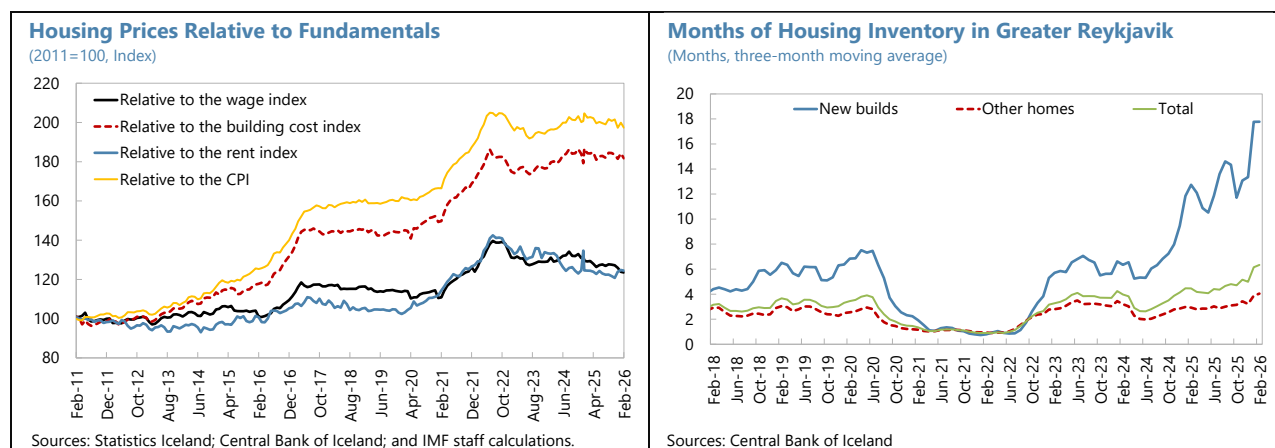
contracted due to elevated interest rates and weaker housing-market turnover, while corporate credit growth remained subdued amid weak economic activity. A Supreme Court ruling in October 2025 on the legality of interest rate terms on variable-rate mortgages prompted many lenders to withdraw such mortgages from the market, resulting in tighter financial conditions that were largely reversed after the CBI eased borrower-based measures (BBMs) and lowered the policy rate.<sup>4</sup> Still, the range of mortgage products remains more limited and interest rates on new indexed mortgages higher than before the ruling.



## 10. The housing market is cooling.

While nominal house prices rose modestly in 2025, real growth slowed through the year before turning negative in late 2025 and into early 2026, reflecting elevated interest rates and the slowdown in immigration, with rising inventories adding to downward pressures, particularly for new construction. As a result, house prices are now better aligned with standard valuation metrics and appear broadly in line with fundamentals. In December 2025, the CBI responded to the emergence of joint-ownership schemes between construction-company-backed funds and homebuyers by expanding the scope of BBMs. These arrangements were assessed as riskier than conventional mortgages due to lower upfront equity contributions and slower equity accumulation, potentially increasing systemic risk if deployed at scale. As a result, the use of such financing structures has remained limited. Housing affordability remains a concern, reflecting still-elevated house prices and high financing costs.

<sup>4</sup> The easing of BBMs included raising the loan-to-value limit for first-time buyers from 85 to 90 percent and increasing the share of mortgage loans that may exceed the debt-service-to-income (DSTI) limit from 5 to 10 percent.



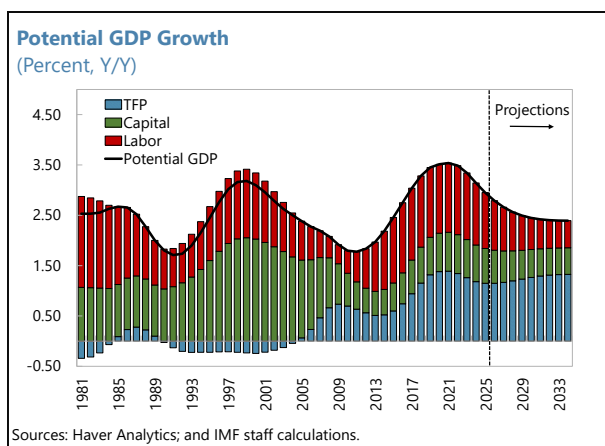
## OUTLOOK AND RISKS

**11. The economy is projected to recover, led by a rebound in net trade, while inflation is expected to remain elevated.** Growth is projected to strengthen to 1.8 percent in 2026, led by a rebound in net exports as imports normalize, marine exports recover, and data center exports increase, more than offsetting external headwinds from weaker trading-partner growth. Overall, geopolitical tensions are projected to subtract about 0.5 percentage points from growth over two years under the baseline (consistent with the April WEO reference forecast, with updated commodity prices through May 19). Domestic demand is expected to remain weak, with consumption dampened by the increase in inflation triggered by the war and the effects of high interest rates, alongside a moderation in data-center investments after the recent surge. In 2027, growth is projected to rise to 2.1 percent as lower inflation and a less restrictive monetary policy stance boost domestic demand. Despite a negative output gap, inflation is projected to remain elevated in 2026, averaging around 5.2 percent, reflecting higher global energy prices, before reaching the 2.5 percent target in early 2028.

**12. Medium-term growth prospects remain favorable.** Under the baseline, growth is expected to outpace that of many advanced economies, reaching 2.4 percent by the end of the projection period. Medium-term growth is supported by productivity gains from continued diversification toward new export-oriented sectors, including aquaculture, biotech, renewable energy, and digital infrastructure (data centers). The outlook is contingent on sustained efforts to boost business dynamism, reduce skills shortages and mismatches, and foster innovation (see ¶34).

### 13. Risks to growth are tilted to the downside, while risks to inflation are to the upside (Annex II).

The principal downside risk is an escalation of geopolitical tensions, which would trigger larger and more persistent commodity price increases, disrupt global supply chains, and weaken external demand, with adverse implications for the growth and inflation outlook. Further increases in energy prices, combined with a tightening in financial conditions, as assumed in the April 2026 WEO severe scenario could reduce GDP growth in 2026 and 2027 by 0.5 and 0.6 percentage points relative to the baseline, raise inflation by 0.8 and 1.7 percentage points, and worsen the fiscal and external balances (text table). In such a scenario, the monetary stance should be tightened decisively given elevated inflation expectations while fiscal support should rely primarily on automatic stabilizers and, if needed, limited, well-targeted, and temporary measures to protect low-income households, preserving price signals. Additional external downside risks include a disorderly AI-related equity market correction and rising fiscal risks globally, which could raise risk premia and increase exchange-rate volatility. Cyberattacks on physical or digital infrastructure could disrupt cross-border financial flows, triggering financial instability and weighing on activity.



| Main Macroeconomic Indicators under the Baseline and Severe Scenarios<br>(Percent)                                                                                                                 |        |          |                 |        |          |                 |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------|----------|-----------------|--------|----------|-----------------|
|                                                                                                                                                                                                    | 2026   |          |                 | 2027   |          |                 |
|                                                                                                                                                                                                    | Severe | Baseline | Difference (pp) | Severe | Baseline | Difference (pp) |
| <b>GDP growth</b>                                                                                                                                                                                  | 0.9    | 1.9      | -1.0            | 1.2    | 2.1      | -0.9            |
| <b>CPI inflation</b>                                                                                                                                                                               | 6.0    | 5.0      | 1.0             | 5.1    | 3.1      | 2.0             |
| <b>General government fiscal balance</b>                                                                                                                                                           | -1.4   | -1.1     | -0.3            | -0.8   | -0.5     | -0.3            |
| <b>Current account balance</b>                                                                                                                                                                     | -1.3   | -0.7     | -0.6            | -0.8   | -0.1     | -0.7            |
| Note: The severe scenario is calibrated using the assumptions of the April 2026 World Economic Outlook Severe Scenario. Difference refers to the severe minus the baseline (in percentage points). |        |          |                 |        |          |                 |

On the domestic side, stronger-than-expected wage pressures could raise firms' costs, lift inflation and inflation expectations, and erode competitiveness, weighing on exports and investment, while triggering further monetary tightening that would weigh on domestic demand. Meanwhile, idiosyncratic shocks to key export sectors—including delays in pharmaceutical patent approvals, or a decline in fish stocks and quotas—could reduce exports. In addition, uncertainties around medium-term assumptions have increased, notably regarding the tourism sector and associated inflows of foreign workers, and the sustainability of new higher value-added sectors. Finally, uncertainty surrounding EU accession could trigger asset price volatility. Key upside risks include stronger-than-expected growth in aquaculture and data centers, sustained by faster expansion of energy capacity.

## Authorities' Views

### 14. The authorities broadly concurred with staff's assessment of the outlook and risks.

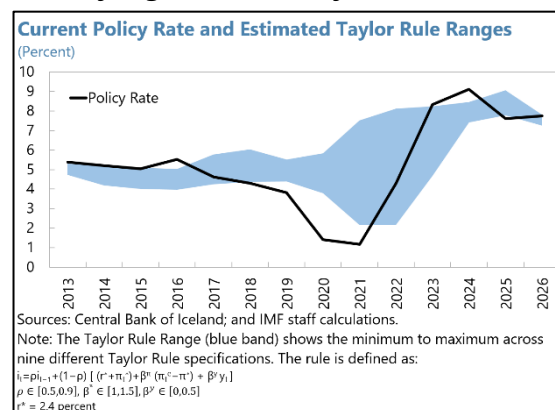
They agreed that growth is expected to strengthen in 2026 and 2027 as the drag from recent shocks fades, and net exports recover, while inflation is likely to remain elevated in 2026 before returning to target in early-2028. At the same time, they emphasized that the baseline remains subject to unusually high uncertainty, particularly due to global factors. They also noted that stronger-than-expected wage growth could complicate the disinflation process and further weigh on competitiveness. They underscored that medium-term growth prospects remain favorable, supported by continued diversification into higher value-added sectors and ongoing efforts to strengthen resilience to shocks.

## POLICY DISCUSSIONS

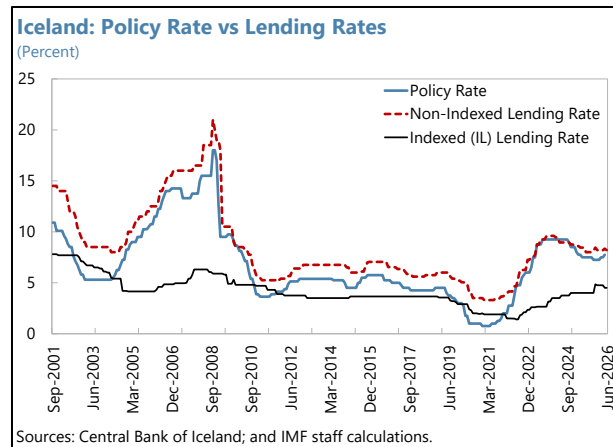
*Discussions focused on calibrating the policy mix to mitigate spillovers from the war in the Middle East, bring inflation to target, rebuild fiscal buffers, and safeguard financial stability. Structural reform priorities aimed at supporting sustained gains in living standards and enhancing resilience to shocks—including broad product market reforms to boost competition and aid in the disinflationary process—were also discussed.*

### A. Monetary Policy

**15. With inflation expectations persistently stubbornly high for several years, the CBI has limited scope to look through inflationary shocks that have emerged from the Middle East war.** While the policy stance remains appropriately restrictive—with the policy rate within the range implied by a standard Taylor rule—further tightening may be needed in the near term to contain inflationary pressures. Such pressures could also emerge if inflation exceeds the 4.7 percent August threshold, potentially triggering a reopening of the multi-year wage agreement.



**16. When current inflationary shocks fade, a sustained resumption of disinflation may allow for a carefully calibrated easing of the monetary policy stance.** Under the baseline, inflation is projected to start declining from 2027Q1 as the impact of the energy-price shock recedes and wage growth moderates, reaching the 2.5 percent target in early-2028. Erring on the tighter side is warranted until inflation and inflation expectations are firmly anchored at target. Materialization of upside risks to inflation—notably stronger-than-expected wage growth or a more persistent increase in global energy prices—would warrant keeping the policy rate higher for longer. Conversely, clear signs that inflation is likely to undershoot the target on a sustained basis would call for a faster reduction of the policy rate toward its neutral level. Uncertainty about potential growth and the amount of slack also argues for caution regarding the pace of monetary easing.



**17. Elevated uncertainty calls for a flexible, data-dependent monetary policy, supported by clear communication.** Amid elevated uncertainty, monetary policy should remain nimble, data-dependent and focused on returning inflation to target. It should be supported by clear and forceful communication that includes the systematic use of scenarios, such as those that relate wage dynamics and inflation expectations, and how those could influence the future policy path. As uncertainty recedes, a gradual transition toward a more forecast-based inflation-targeting approach would help increase policy predictability and reduce financial market volatility.

**18. Structural factors are expected to ease inflation pressures over time, but sustaining price stability will require complementary structural reforms.** The maturation of the labor-intensive tourism sector should ease pressures on labor demand and, in turn, moderate wage growth, while also helping to contain housing pressures—two key drivers of inflation over the past decade. Maintaining inflation durably at target will also depend on reforms to collective wage-setting arrangements to ensure wage growth—including in the public sector—remains aligned with productivity, alongside measures to lower market concentration and markups that contribute to persistently high service-sector inflation (see 134).

**19. While foreign currency reserves are adequate for precautionary purposes, a further increase would enhance resilience.** FX purchases totaling €473 million in 2025 raised reserves to around 123 percent of the Fund's Reserve Adequacy (ARA) metric at year-end. While this is well within the 100-150 percent range considered adequate for precautionary purposes, increasing reserves toward the upper end of the ARA range would strengthen resilience and limit the risk of disruptive exchange rate movements, while the cost of larger reserves would remain manageable. The €138 million FX purchase program announced on May 8 will further strengthen reserves. In addition, as highlighted in the 2024 Article IV consultation, gradually deepening the foreign

exchange market, including the FX derivatives market, would support foreign investor participation in the domestic bond market and facilitate hedging of FX risk. Consideration could be given to allowing a larger number of market makers in the FX interbank market, recalibrating the individual counterpart limits on banks' FX derivatives trades, and overall broadening foreign holdings of ISK government bonds.

### Authorities' Views

**20. The authorities reiterated their commitment to maintaining a restrictive monetary policy stance until there is clear evidence that inflation and inflation expectations return durably to target.** In that context, they emphasized that they would monitor indicators of inflation, inflation expectations and wage developments in assessing the appropriate policy stance and are prepared to tighten policy still further to ensure that inflation eases towards the inflation target, even though this could further curtail economic activity. They broadly agreed with staff that policy should remain data dependent and that caution is warranted in calibrating any eventual easing, given persistent upside risks to inflation. The authorities agreed that current levels of reserves are adequate for managing disruptive exchange rate movements, and that the ongoing FX purchase program will keep the reserves buffers adequate. They saw merit in staff's recommendation to deepen the foreign exchange derivatives market but emphasized the importance of proceeding cautiously.

## B. Fiscal Policy

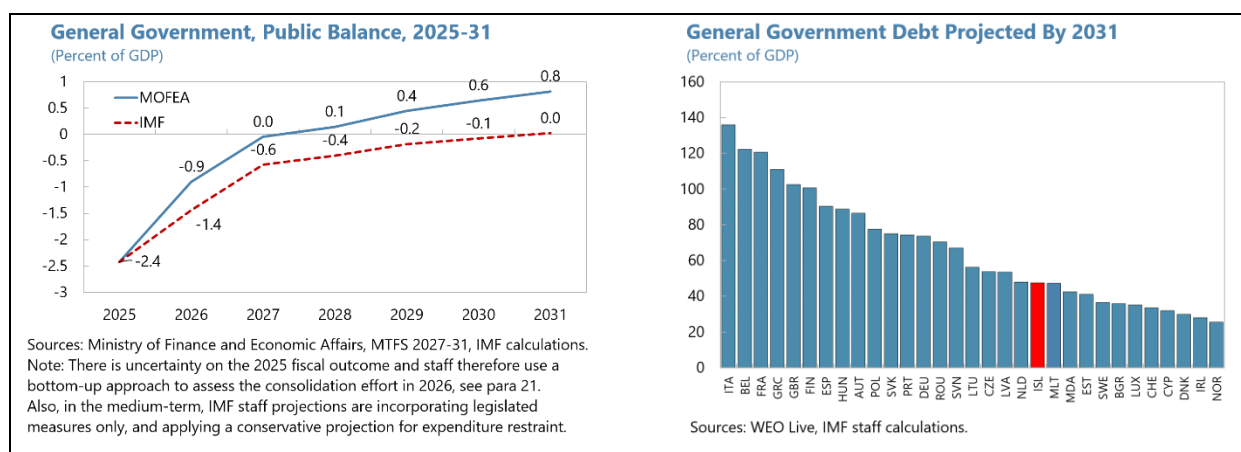
**21. Fiscal policy in 2026 is appropriately contractionary given the need to reduce inflation and rebuild fiscal buffers.** The Medium-Term Fiscal Strategy 2027-31 (MTFS) projects a general government deficit of 0.9 percent of GDP in 2026, broadly in line with staff's forecast. Given the uncertainty of the 2025 fiscal outturn, staff used a bottom-up assessment of adopted measures, which suggests a consolidation effort of 0.6 percent of GDP, resulting in a modest negative fiscal impulse of around 0.2 percent of GDP in 2026. These measures include the introduction of a kilometer tax for all vehicles alongside a switch toward levying excise duties on internal combustion engine vehicles, the full-year impact of the fisheries' levy introduced in 2025, and various expenditure cuts (Text Table 1). To mitigate the impact of the war in the Middle East, the authorities announced in

| Text Table 1. Revenue and Expenditure Measures, 2026<br>(Percent of GDP)                           |              |
|----------------------------------------------------------------------------------------------------|--------------|
| <b>Revenue</b>                                                                                     |              |
| Kilometer Fee: all motor vehicles                                                                  | 0.70         |
| Excise duty on vehicles (lower on electric/higher on fossil)                                       | 0.14         |
| Fisheries Levy decrease resulting from carbon tax increase                                         | 0.10         |
| Carbon tax raised by 15%                                                                           | 0.06         |
| PIT bracket sharing repealed                                                                       | 0.05         |
| Kilometer Fee: heavy vehicles                                                                      | -0.04        |
| VAT decrease: side effect from fuel excises repealed                                               | -0.05        |
| Kilometer Fee: electric and plug-in hybrids                                                        | -0.07        |
| Fuel excises on petrol repealed                                                                    | -0.23        |
| Fuel excise on diesel repealed                                                                     | -0.31        |
| Other revenue, including interest revenue                                                          | -0.40        |
| <b>Sum total revenue</b>                                                                           | <b>0.05</b>  |
| <b>of which primary revenue</b>                                                                    | <b>0.45</b>  |
| <b>Expenditure</b>                                                                                 |              |
| Mergers, streamlining, and review of operations.                                                   | -0.15        |
| Interest payments on public debt                                                                   | -0.50        |
| Review of budgetary allocations .                                                                  | -0.05        |
| System change and reorganisation of services                                                       | -0.04        |
| Postponement or cancellation of projects                                                           | -0.02        |
| Technologisation and digitalisation                                                                | -0.01        |
| <b>Sum total expenditure</b>                                                                       | <b>-0.65</b> |
| <b>of which primary expenditures</b>                                                               | <b>-0.15</b> |
| Source: Ministry of Finance                                                                        |              |
| Note: Minor revenue measures are excluded from the list, but included in the sum of total revenue. |              |

April 2026 a temporary reduction in the VAT rate on fuels from 24 to 11 percent, alongside measures to strengthen price monitoring and ensure the VAT rate cut is passed through to consumers. While the cost of these measures (around 0.1 percent of GDP) will be accommodated within the existing budget envelope, it will be important to phase out the VAT rate cut as legislated by end-August, as such measures mute price signals and are not well targeted. If the energy price shock lasts longer than anticipated, the authorities should target support measures to the vulnerable. As automatic stabilizers are already large in Iceland and given the current cyclical context, the authorities should offset any discretionary support measures that would compromise the adopted budget targets for 2026 and 2027.

**22. The fiscal consolidation envisaged over the medium term is appropriately ambitious and should be fully implemented.** The MTFS envisages a balanced budget for the general government in 2027 and a surplus of 0.8 percent of GDP by 2031. These targets are appropriately ambitious given that the current debt level—56.1 percent of GDP at end-2025—exceed those of most other Nordic countries despite Iceland’s economy being more shock-prone. These targets also ensure a gradual decline in debt over the medium term, strengthening fiscal buffers, and creating fiscal space for long-term spending needs. The envisaged fiscal adjustment is underpinned by substantial measures; the greater reliance on expenditure restraint is welcome given significant revenue measures in recent years, though further details about the nature of expenditure measures will be important to support credibility.<sup>5</sup> Staff projections that only include measures presented to Parliament in a legislative proposal suggest the budget will return to balance by 2031 and public debt will decline to 48 percent of GDP. In those projections, staff include about 1.5 percent of GDP in annual net borrowing, reflecting mainly higher on-lending to the Housing Fund and the Student Educational Fund, as well as other items impacting the net borrowing requirement and debt level, such as a mismatch between the assets and liabilities governing public pension payments and valuation changes due to indexation. These below-the-line operations will account for about 10 percent of GDP of projected debt by 2031, but the debt assessment of an overall low risk of sovereign stress will remain valid (See Annex III). Spending pressures are set to intensify beyond 2031, mainly driven by rising healthcare costs—projected to increase spending by 1.4 percent of GDP by 2037—alongside potentially significant but uncertain climate-related expenditures. Debt is projected to continue declining under staff’s baseline, even as aging and healthcare costs materialize. But a prudent fiscal stance—including full implementation of the ambitious consolidation targets—would be essential to manage the risks from future shocks and the rise in below-the-line on-lending and related credit risks; it would also support progress toward the fiscal rule’s 30 percent net debt target.

<sup>5</sup> The MTFS targets expenditure restraint through consolidation and streamlining. Staff adopts a conservative approach on non-legislated expenditure consolidation and include around half of the non-legislated planned consolidation of primary expenditure.



**23. Scaling up infrastructure investments is needed to sustain potential growth, but any increase in fiscal risks should be carefully contained.** The authorities established a state-owned infrastructure company, financed through user fees and market borrowing, and able to enter into public-private partnerships.<sup>6</sup> While the intention to scale up infrastructure investment is welcome given existing infrastructure gaps, it will be important to ensure that any increase in fiscal risks—including through guarantees or off-balance-sheet liabilities—is carefully contained, transparently recorded, and subject to regular fiscal risk reporting. In addition, streamlining permitting and licensing procedures, which remain more onerous than the OECD average, would help accelerate infrastructure deployment.

**24. Should additional measures be needed to meet the MTFS targets, mitigate long-term spending pressures, or scale up infrastructure investment, the authorities could consider:**

- *Revenue-raising measures:* As noted in the 2025 Article IV, closing around half of the gap in the VAT revenue ratio—for instance by raising the preferential VAT rate and/or narrowing the range of eligible goods and services—could generate additional revenues of close to 0.5 percent of GDP. Housing taxation could also be increased, including by restricting the capital gains exemption on housing and raising the property tax rate on vacant land. In addition, there is scope to streamline tax expenditures, including by reassessing the 2020 increase in the ceiling on business R&D expenditures eligible for tax relief.
- *Rationalizing government spending:* Staff analysis suggests scope for rationalization and reallocation, including by improving education outcomes for a given level of spending, reducing relatively high spending on recreational services, and containing growth in the public sector wage bill. Such reforms could help support medium-term growth while strengthening fiscal sustainability (Annex VII).

<sup>6</sup> See the [bill on the establishment of an infrastructure company](#).

- *A more gradual reduction in net debt.* Should revenue-raising and spending rationalization measures prove insufficient to create the fiscal space needed to scale up infrastructure investment, the authorities could consider a more gradual convergence toward the debt target. This should be accompanied by clear communication to reinforce the authorities' commitment to the fiscal rules and the medium-term debt anchor.

**25. A strong fiscal framework, supported by timely and accurate data, would bolster the credibility and transparency of the consolidation effort.** The amended fiscal rule should help contain spending over the medium term, while the existing legislation provides a sound basis to regularly reassess the current 2 percent expenditure-growth limit given uncertainty around Iceland's future growth prospects and exposure to shocks.<sup>7</sup> Ongoing efforts to strengthen the Fiscal Council are welcome but will require a meaningful increase in its capacity and resources. Regular publication of timely and independently-verifiable quarterly fiscal data consistent with the fiscal rule perimeter—supported by the completion of Statistics Iceland's accrual-based quarterly accounts under IPSAS—would further strengthen fiscal transparency. In this context, the recent uncertainty surrounding the 2025 outcome of the general government deficit underscores the importance of timely information sharing and institutional coordination. Finally, expanding the coverage of the budget and the fiscal rules to encompass the entirety of the central government (A1-A3) would increase transparency and reduce incentives to shift spending and borrowing to parts of the government not covered by the rules.

### ***Authorities' Views***

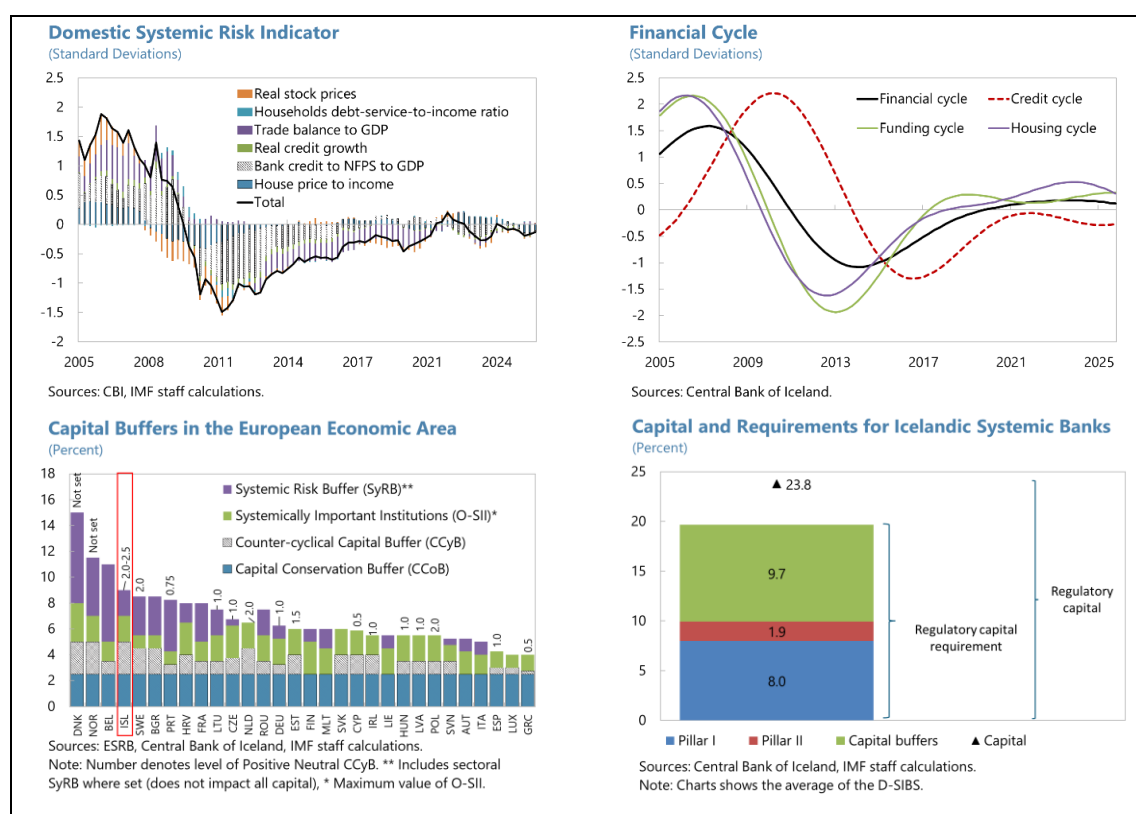
**26. The authorities are committed to fiscal consolidation in line with their ambitious targets in the 2027-31 MTFS.** The authorities are confident that the 2026 deficit will be broadly in line with the target adopted with the 2026 budget. They expect to implement the consolidation measures outlined in the 2027-31 MTFS, which should build fiscal buffers and thus strengthen resilience, and put emphasis on restraining growth of the public wage bill as an important component of the fiscal consolidation. The authorities opted for a simple and visible measure when deciding to lower the VAT rate on fuels temporarily. They acknowledge that there are significant infrastructure spending gaps, which they plan to mitigate within the projection period. The authorities have started to put in place greater institutional coordination to strengthen the compilation of statistics for public finances and agree on the merits of continued improvements in the consistency and transparency of data available to assess fiscal policy. They are supportive of strengthening the Fiscal Council.

---

<sup>7</sup> The amended rule was adopted in July 2025.

## C. Financial Sector Policies

**27. The banking sector remains resilient while systemic risks are contained and broadly unchanged from last year.** Capital ratios increased in 2025, partly due to a reduction in effective risk weights under CRR III. Profitability strengthened, driven mainly by higher net interest income amid balance-sheet expansion and a wider interest-rate differential. Asset quality remains strong, with non-performing loans at around 1.6 percent, while liquidity buffers are ample, with the aggregate liquidity coverage ratio above 200 percent. The pension fund sector remains resilient, supported by continued net inflows and positive real asset returns. The CBI's cyclical systemic risk indicator remains below its historical average and broadly stable, reflecting weakening credit growth and declining real house prices. Meanwhile, the financial cycle appears to have peaked due to an easing of the housing and credit cycles, suggesting overall moderately lower financial risks.



**28. Credit risk remains contained overall, though pockets of vulnerabilities persist which suggest continued vigilance is warranted.** While mortgage portfolios remain sound, an abrupt decline in residential house prices combined with increasing unemployment could weaken asset quality. This risk is mitigated by moderate loan-to-value ratios, strong borrower equity, and accumulated household savings. Corporate credit quality remains sound overall, though risks are evident in construction and tourism-related sectors which together account for 38 percent of all corporate lending. In the construction sector weaker demand, declining real house prices, and high inventory levels for new housing have increased vulnerabilities, with stage two loans rising to 11 percent at end-February from six percent in 2025. These risks are partly mitigated by higher risk

weights on construction loans under CRR III and a relatively strong equity ratio of around 36 percent, broadly in line with Nordic peers. In tourism-related sectors resilience is weaker with an equity ratio of 24 percent, well below other Nordic countries, heightening sensitivity to a downturn in tourist arrivals. In response to increasing operational and cyber risks, the authorities are strengthening resilience through cybersecurity testing, contingency planning, and measures to safeguard payment system continuity.

**29. The macroprudential policy settings are broadly appropriate.** Capital requirements on Icelandic banks are relatively high by European standards and include a 2.5 percent countercyclical capital buffer (CCyB)—at the upper end of 2.0–2.5 positive neutral range—as well as a two percent systemic risk buffer (SyRB). While systemic risks remain contained, the overall level of capital requirements remains appropriate, as lending surveys show no evidence of a tightening in lending standards, with the recent moderation in credit driven mainly by weaker demand rather than supply constraints. While developments in co-ownership loans needs to be assessed, the recent easing of borrower-based measures (BBMs) helped offset the tightening of financial conditions following the Supreme Court ruling on variable-rate mortgages; with housing-market risks now receding, BBMs should remain on hold to avoid reinforcing the housing slowdown while continuing to serve as a structural backstop.<sup>8</sup>

**30. Proposed housing finance reforms are welcome but warrant careful monitoring.** The government has unveiled plans to reduce reliance on index-linked mortgages, notably by introducing minimum repayment requirements from 2027.<sup>9</sup> While this may strengthen the transmission of monetary policy, these measures should be carefully assessed given the beneficial impact indexation has had on the resilience of borrowers and financial stability.

**31. Strengthening pension fund governance and the independence of the CBI’s supervisory activities remain important priorities (Annex V).** As noted in the 2025 Article IV consultation, pursuing legislative changes to strengthen pension fund governance, internal controls, and risk management in an incremental manner could help facilitate implementation. Staff welcomes ongoing efforts to explore options to introduce a more streamlined and independent budgetary process for financial supervision and stronger legal protection for supervisors.

### ***Authorities’ Views***

**32. The authorities concurred with staff’s assessment that the financial system is resilient, aided by sound supervision and a tight macroprudential policy stance.** They see key risks in the financial system stemming from the housing market and cyber events. They emphasized that the financial sector is overall resilient to a more severe housing market slowdown. While there are pockets of vulnerabilities, mainly from property developers, equity ratios are high, and the

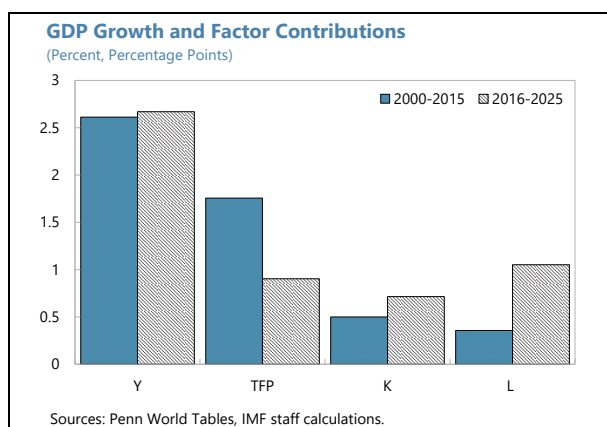
<sup>8</sup> See Valderrama, L. (2023), “Calibrating Macroprudential Policies in Europe”, IMF Working Paper 23/75.

<sup>9</sup> The housing package also includes potential adjustments to housing credit regulations and targeted support to expand housing supply, particularly strengthening affordable rental housing for specific groups (low-income earners, students, and social housing).

authorities are confident that financial institutions have sufficient buffers to deal with a deterioration in asset quality. The authorities shared staff's view that the current tight macroprudential stance is broadly appropriate. They noted continued progress on FSAP recommendations, which are largely implemented. There are ongoing discussions on improving the legal protection of supervisors and the funding framework for financial supervision, as legal issues are complex. The authorities also noted continued progress with the ongoing FATF assessment, expected to be published in 2027.

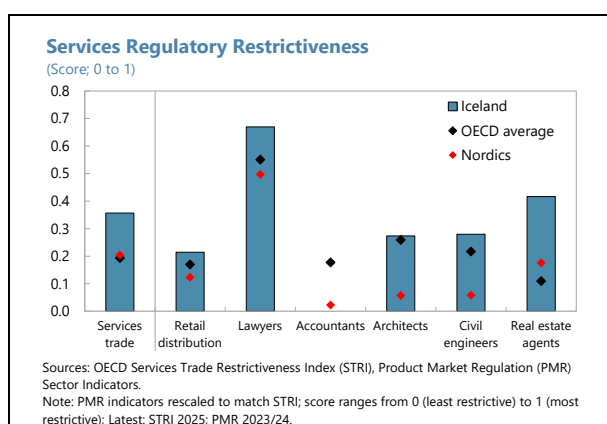
## D. Structural Policies

**33. Future income gains will increasingly hinge on productivity-enhancing structural reforms.** GDP growth over the last decade has been driven largely by the expansion of tourism and associated foreign-labor inflows. As tourism is maturing, sustaining medium-term growth will require stronger productivity growth, diversification into higher-value-added sectors, and structural reforms to support business dynamism, innovation, labor supply, skills, and infrastructure.<sup>10</sup>



**34. Structural reforms in the following areas would strengthen productivity and lift the economy's growth potential.**

- Business regulation reforms:** Iceland maintains relatively high barriers to entry, particularly in parts of the services sector, with business regulation more restrictive than the OECD average.<sup>11</sup> FDI regulations are among the most stringent across OECD countries, with strict restrictions on foreign ownership in sectors including fisheries, electricity, and air transport. While ongoing efforts to simplify the regulatory framework are welcome, including measures in the authorities' [Growth Plan to 2035](#), future priorities should include further streamlining of licensing and permitting procedures, reducing overly restrictive FDI regulation, digitization of



<sup>10</sup> See Budina et al. (2025), "Europe's National-Level Structural Reform Priorities", IMF Working Paper 25/104, [OECD Economic Surveys: Iceland 2025](#), and accompanying Selected Issues Paper.

<sup>11</sup> See [OECD Product Market Regulation \(PMR\) indicators](#) and [OECD STRI for Iceland](#).

government services, and simplifying the insolvency regime for SMEs to facilitate the reallocation of resources to more productive firms/sectors.<sup>12</sup>

- *Innovation:* Total R&D spending in Iceland is already relatively high at around 2.5 percent of GDP in 2024, and the goal is to increase it further to 3.5 percent of GDP by 2035. However, innovation outcomes have been mixed: Iceland produces fewer innovation outputs than expected given its level of R&D spending.<sup>13</sup> In this context, recommendations in the 2025 Article IV to enhance the efficiency of Iceland's generous R&D support scheme remain valid.

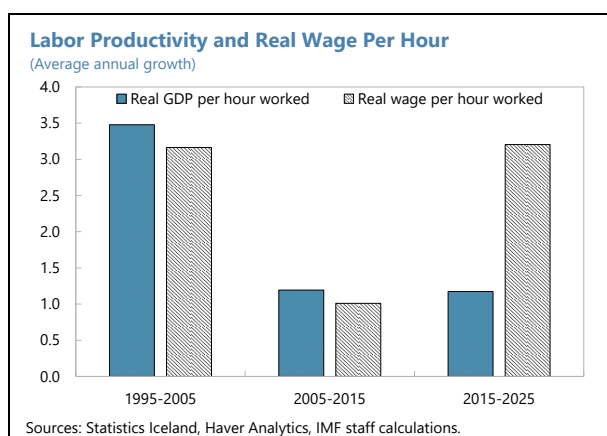
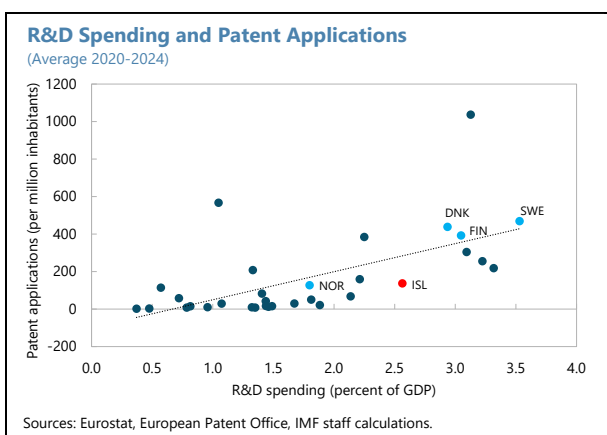
Additional priorities include better

monitoring and reporting of the impact of R&D support on innovation outcomes, streamlining research grant application processes, expanding research-industry linkages to facilitate commercialization, and further developing the nascent venture capital and startup ecosystem.

- *Labor market reforms:* Iceland's labor market is characterized by high unionization and centralized collective bargaining. While this model supports relatively equitable wage outcomes, average wage growth has markedly outpaced productivity growth over the last decade (also see ¶15 and ¶16). To safeguard competitiveness, it will be important that wage settlements—including in the public sector—remain consistent with anticipated productivity growth and the inflation target. In this context, the

authorities should consider including public-sector unions in the coordinated bargaining round alongside the private sector and better synchronizing negotiation rounds to strengthen coordination and help preserve wage discipline. Strengthening the state mediator's authority to trigger binding votes on proposed settlements would help resolve protracted bargaining impasses.

- *Skills shortages and mismatches:* Iceland's Program for International Student Assessment (PISA) scores have declined markedly over the past two decades in all main categories (reading, math, science) and now lie well below the OECD average, with potentially significant implications for



<sup>12</sup> See accompanying Selected Issues Paper.

<sup>13</sup> See [Global Innovations Index, 2025](#).

long-term productivity (Figure 7).<sup>14</sup> Stepping up education reform as envisaged in the authorities' Education Policy 2030 framework and improving Science, Technology, Engineering, and Mathematic (STEM) training (as envisaged in the [Growth Plan to 2035](#)) should help address these challenges. Expanding vocational training and reskilling programs would help ease skill mismatches and support labor reallocation. Further progress in integrating immigrants could also help alleviate skill shortages. Finally, while Iceland ranks high on digital skills metrics, further strengthening through education and training could increase adoption and integration of new technologies, such as AI.

- *Infrastructure investment:* Public investment—while above the European average—lags that of Nordic peers (Figure 7), pointing to scope to strengthen infrastructure in key network sectors to raise productivity and support economic diversification. In the energy sector, planned increases in generation capacity are insufficient to meet projected demand growth, and parts of the transmission grid—much of it not upgraded for decades—are operating at full capacity.<sup>15</sup> Fast-tracking new green generation projects and streamlining approval processes would help strengthen energy security and expand the economy's ability to accommodate new high-growth, high-value-added sectors such as aquaculture and data centers. Infrastructure also remains a constraint,<sup>16</sup> with the cumulative infrastructure gap, including maintenance, estimated at around 14 percent of GDP in 2025.<sup>17</sup> Timely implementation of the National Transportation Plan would improve access to domestic and international markets, supply-chain efficiency, and regional integration. The state-owned infrastructure company (see ¶23) could help accelerate delivery of major projects, though associated fiscal risks should be carefully managed.

### **35. EU accession and euro adoption are ultimately political choices that involve balancing deeper integration and credibility gains against reduced macroeconomic policy autonomy.**

Iceland is scheduled to hold a referendum on August 29, 2026 on whether to resume EU accession negotiations. Joining the EU (and, ultimately, the euro area) would deepen trade and financial integration, eliminate exchange-rate risk vis-à-vis the euro area, and could support investment and productivity.

- Iceland's membership in the European Economic Area (EEA) means that it already applies a large share of the EU *acquis communautaire*, including single-market rules on the four freedoms, competition, state aid, and horizontal policies such as energy and environment. The main outstanding areas are the Common Agricultural Policy and, most critically, the Common Fisheries Policy, where accession could require Iceland to adjust control over fisheries quota management. EU membership would also bring Iceland inside the customs union, shielding it

<sup>14</sup> OECD research suggests that the 40 points decline in Iceland's average PISA score between 2006 and 2022 could reduce long-term productivity by over 5 percent. See [Andrews, Egert and de la Maisonnette \(2024\)](#).

<sup>15</sup> See [Landsnet electricity forecast 2024-50](#) and OECD Economic Surveys: Iceland 2025, [Chapter 3](#).

<sup>16</sup> See [World Bank Enterprise Survey](#).

<sup>17</sup> See [Infrastructure in Iceland 2025: Status and Future Prospects](#).

from EU trade defense measures such as the 2025 ferro-alloy safeguard tariff-rate quotas that were applied to EEA members.

- Euro adoption could also help anchor inflation expectations, facilitate the gradual convergence of market interest rates toward euro-area peers, and provide access to euro-area financial architecture, including the Banking Union. However, adopting the euro would entail the loss of independent monetary policy and exchange-rate flexibility—tools that have helped absorb large and sometimes asymmetric shocks over the last decade and a half. Losing monetary autonomy would increase reliance on fiscal policy for stabilization and placing greater demands on a strong countercyclical fiscal framework, while increasing exposure to euro-area-wide tail risks through shared backstops and crisis mechanisms. As labor market flexibility is already high, the focus should be on aligning wage growth with productivity gains and advancing productivity-enhancing structural reforms—important factors for external competitiveness, but especially critical in the absence of the exchange rate as an adjustment tool. Should the process move forward, these considerations underscore the importance of adopting the euro from a position of low inflation, sustainable public finances, and a parity consistent with fundamentals to avoid locking in an overvalued real exchange rate that would undermine competitiveness and force adjustment through internal devaluation.

### ***Authorities' Views***

**36. The authorities broadly shared staff's structural reform priorities and highlighted the recently published Growth Plan to 2035 as the central vehicle for advancing them.** They noted that the Plan's key priorities—strengthening energy supply and infrastructure, simplifying regulation and licensing, and supporting innovation and export-driven industries—are closely aligned with staff's recommendations, and that an associated Action Plan 2026–27 provides concrete implementation targets. The authorities emphasized that the focus has shifted from diagnosing structural constraints to ensuring effective delivery of reforms. They welcomed staff's holistic assessment of the multiple elements/dimensions related to potential EU accession and euro adoption.

## **STAFF APPRAISAL**

**37. Economic activity moderated in recent years, while inflationary pressures remained elevated.** Growth has slowed since mid-2023 amid appropriately tight macroeconomic policies and idiosyncratic shocks, yet inflation, inflation expectations, and wage growth remain elevated. The current account deficit widened in 2025, due to imports for data centers and other idiosyncratic factors. The external position is assessed to be moderately weaker than implied by fundamentals and desirable policies.

**38. The economy is expected to recover gradually, but risks to growth are tilted to the downside and inflation risks to the upside.** Staff projects growth at 1.8 percent in 2026 and 2.1 percent in 2027, supported by a rebound in net trade and easing financial conditions. Inflation is

projected to remain elevated at 5.2 percent in 2026 and 3.2 percent in 2027, before declining toward target in early-2028. Key risks include an escalation of geopolitical tensions, stronger-than-expected wage growth, and disruptions to key export sectors. Medium-term growth prospects remain well-supported by continued diversification towards new export-oriented sectors. Policy priorities are thus to lower inflation sustainably to target, anchor inflation expectations, and increase resilience to shocks by further building fiscal buffers and advancing structural reforms.

**39. The fiscal stance is appropriately contractionary and the medium-term fiscal targets are appropriately ambitious and should be fully implemented.** The fiscal stance in 2026 and beyond will help lower inflation and build buffers. The temporary reduction in the VAT rate on fuel should remain time-bound and be phased out as planned. Medium-term targets—which place public debt on a firm downward trajectory—are well-calibrated given the economy’s exposure to shocks. Longer-term spending pressures from healthcare and infrastructure underscore the importance of sustained discipline and credible medium-term planning, as well as transparent monitoring of credit risk related to below-the-line on-lending.

**40. There is scope to raise revenues and reduce spending if needed to meet the MTF5 targets, mitigate long-term spending pressures, or scale up infrastructure investment.** Options include raising the preferential VAT rate and/or narrowing its coverage, increasing housing-related taxation, streamlining R&D support, and further rationalizing public spending, including through spending efficiency and public sector wage restraint. Plans to establish a state-owned infrastructure company could help mobilize financing, but should have strong safeguards to contain fiscal risks, including careful monitoring and transparent recording of contingent liabilities and off-balance-sheet exposures.

**41. Strengthening the fiscal framework would boost the credibility of the consolidation effort.** The amended fiscal rule should help contain spending over the medium term and reduce procyclicality. The authorities’ efforts to strengthen the Fiscal Council are welcome, but a meaningful increase in its capacity and resources will be needed. Regular publication of timely and independently-verifiable quarterly fiscal data consistent with the fiscal-rule perimeter would further strengthen transparency and accountability. Expanding the coverage of the budget and the fiscal rules to encompass the entirety of the central government would also improve transparency.

**42. The monetary policy stance remains appropriately restrictive, but vigilance is warranted alongside clear and forceful communication.** Further tightening may be needed in the near term if inflationary pressures persist or intensify and policy should remain restrictive until inflation and inflation expectations are firmly anchored at target. Strengthening communication, including using alternative scenarios, would help enhance transparency and anchor expectations. As uncertainty recedes, a gradual transition toward a more forecast-based inflation targeting framework would improve predictability and reduce volatility.

**43. Reserves are adequate for precautionary purposes.** Further strengthening of foreign exchange reserves toward the upper end of the Fund’s ARA range would enhance resilience to

external shocks, while efforts to deepen the foreign exchange market would support broader market participation and improve hedging opportunities.

**44. Systemic risks in the financial sector are contained and the current macroprudential stance is broadly appropriate.**

Banks remain well-capitalized, profitable, and liquid, with strong asset quality. However, vulnerabilities in parts of the corporate sector—notably construction and tourism-related activities—require vigilance. Borrower-based measures should remain broadly unchanged for now, especially given the slowing housing market. Efforts to reduce reliance on CPI-indexed mortgages may strengthen monetary transmission over time, but should be carefully timed and sequenced given their role in supporting borrower resilience and financial stability.

**45. Financial sector reforms should build on the significant progress achieved in implementing FSAP recommendations.**

Remaining priorities include strengthening pension fund governance and safeguarding the independence of financial supervision. Efforts to strengthen operational resilience, including against cyber and payments-related risks, remain essential.

**46. Structural reforms should focus on raising productivity and further diversification.**

Priorities include reducing regulatory barriers and streamlining licensing and permitting processes; addressing skills shortages through education reform, vocational training, and improved reskilling; reforming wage-setting arrangements to better align wage growth with productivity and the inflation target; closing infrastructure gaps; and improving the efficiency of R&D support while strengthening the broader innovation ecosystem. The authorities' recent Growth Plan to 2035 is well aligned with these priorities, and successful implementation will require strong cross-ministerial coordination, prioritization, monitoring and reporting.

**47. EU accession and euro adoption are ultimately political choices that involve balancing deeper integration and potential credibility gains against reduced macroeconomic policy autonomy.**

While EU membership and euro adoption could deepen integration and potentially enhance policy credibility, it would result in the loss of independent monetary policy and exchange rate flexibility. Should the process move forward, maintaining low inflation, sound public finances, and an exchange rate aligned with fundamentals, while advancing structural reforms to increase productivity and aligning wages with productivity, will be critical to safeguard stability and competitiveness.

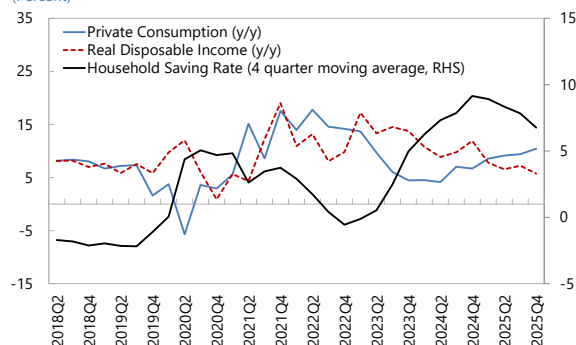
**48. It is proposed that the next Article IV consultation with Iceland take place on the standard 12-month cycle.**

# Figure 1. Iceland: Real Sector Developments

Consumer spending growth picked up in 2025 despite slowing real income growth as the savings rate declined.

## Private Consumption, Income and Savings

(Percent)

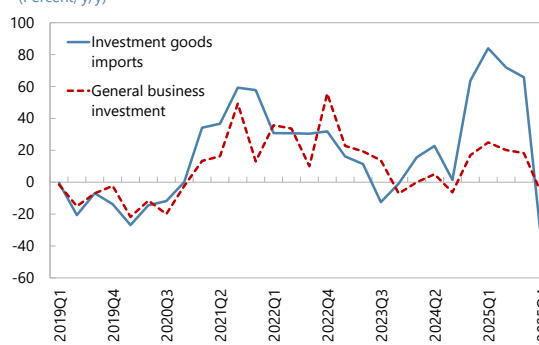


Source: Statistics Iceland.

Investment goods imports fell sharply, in tandem with slower business investment, following a data center surge.

## Investment Goods Imports and Investment

(Percent, y/y)

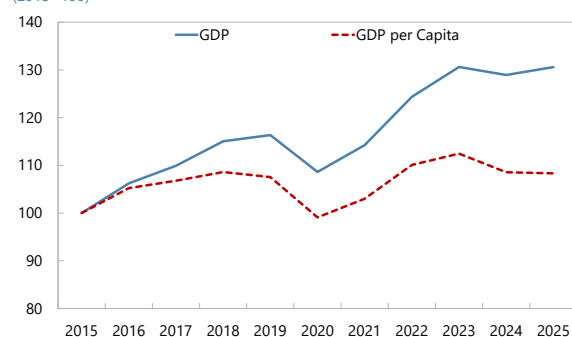


Sources: Statistics Iceland, Central Bank of Iceland.

Real GDP growth has outpaced per capita growth over the last decade.

## GDP and GDP per Capita

(2015=100)

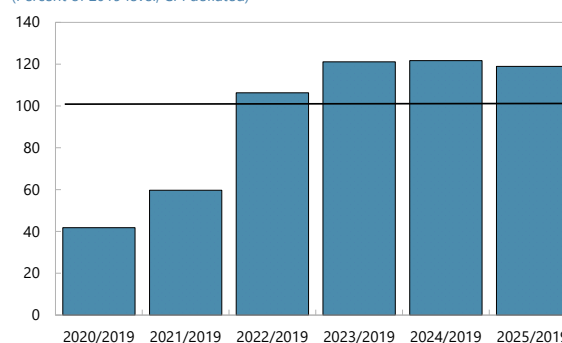


Sources: Haver Analytics; and IMF staff calculations

Real turnover in the tourism sector declined slightly in 2025 but remains around 20 percent above 2019 levels.

## Real Turnover in Tourism, 2020-2024

(Percent of 2019 level, CPI deflated)

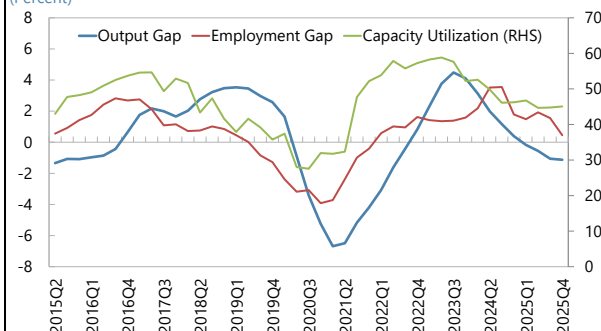


Sources: Statistics of Iceland and IMF staff calculation.

Indicators point to increasing slack, with capacity utilization drifting lower and negative output gap.

## Measures of Economic Slack

(Percent)



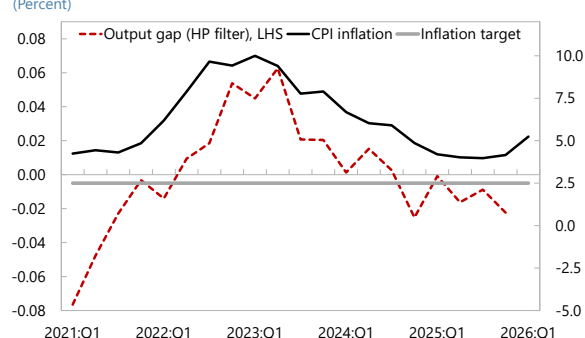
Sources: Haver Analytics; Statistics of Iceland; IMF staff calculations.

Note: The employment gap is defined as the deviation of employment from its trend.

CPI inflation has remained above the 2.5 percent target even as the output gap is negative.

## Output Gap and Inflation

(Percent)



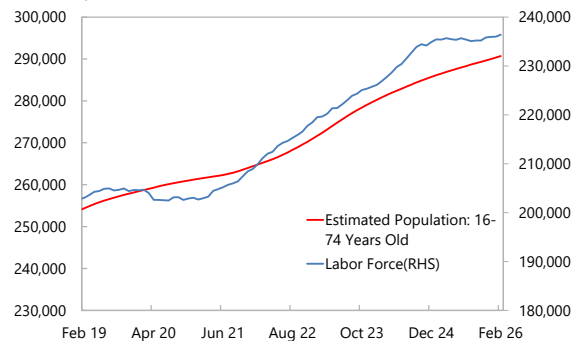
Sources: Statistics Iceland; Haver Analytics; and IMF staff calculations.

## Figure 2. Iceland: Labor Market Developments

Labor force growth has slowed despite continued population growth...

### Working Population and Labor Force, 2019-2025

(Number of persons)



...reflecting a decline in the activity rate.

### Activity Rate, 2019-2025

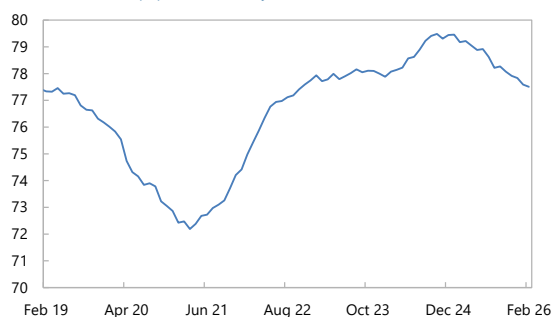
(Percent of estimated population, 16-74 years old)



The employment rate has fallen to its lowest level since October 2022.

### Employment Rate, 2019-2025

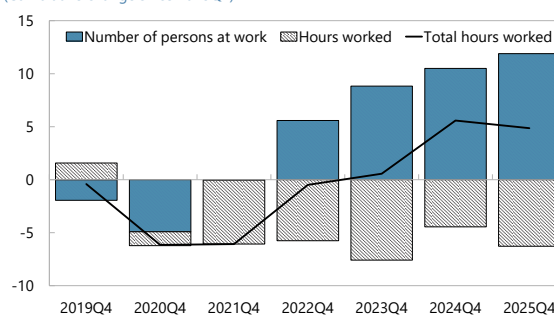
(Percent of estimated population, 16-74 years old)



Growth in total hours worked was driven primarily by higher employment.

### Employment and Hours Worked

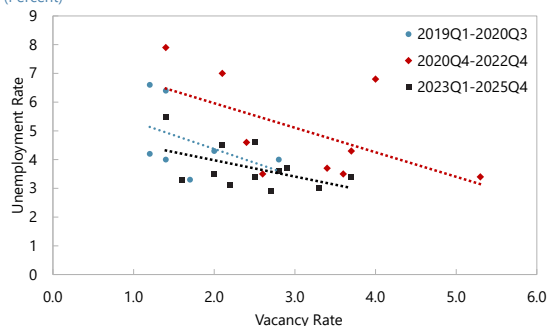
(Cumulative change since 2018Q4)



The Beveridge curve has flattened since the onset of Covid, as immigration flows are linked to the business cycle.

### Beveridge Curve

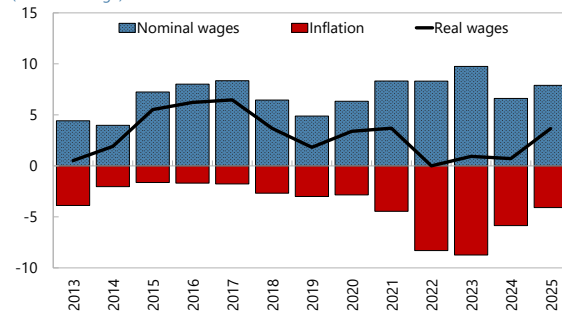
(Percent)



Real wages strengthened in 2025 with nominal wage growth outpacing declining inflation

### Real and Nominal Wage

(Percent change)

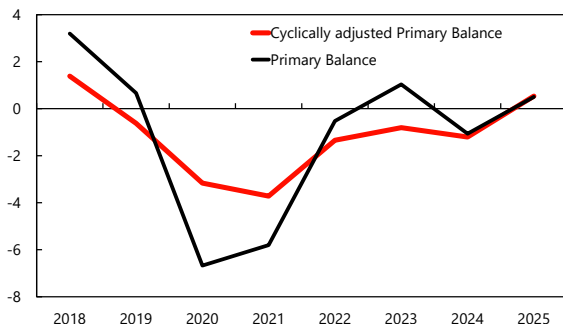


**Figure 3. Iceland: Fiscal Developments and Issues**

The fiscal position has been gradually improving since the pandemic...

#### Primary Balances: 2018-2025

(Percent of GDP)

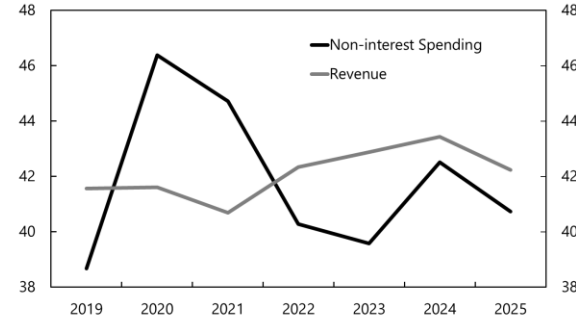


Source: Statistics Iceland.

...supported by robust revenues and a decline in non-interest spending since the pandemic.

#### General Government Revenue and Spending, 2019-2025

(Percent of GDP)

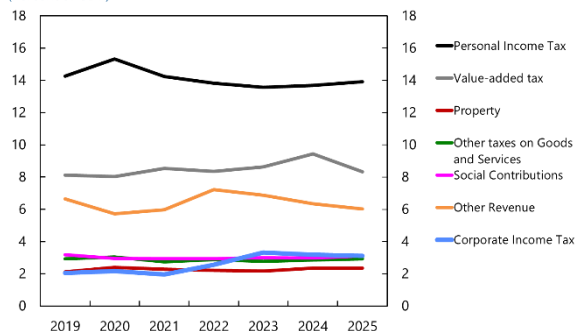


Source: Statistics Iceland.

The revenue composition was broadly stable through 2025...

#### General Government Revenue, 2019-2025

(Percent of GDP)

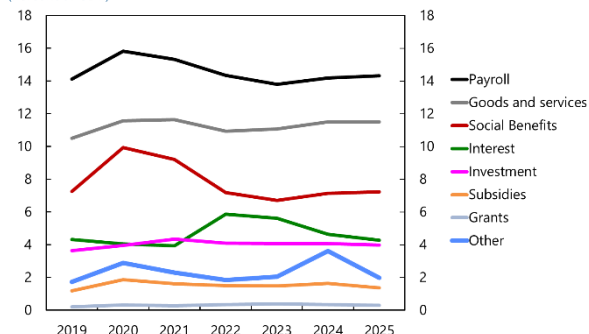


Source: Statistics Iceland.

An increase in payrolls was offset by a decline in interest and other spending following Grindavik purchases in 2024.

#### General Government Spending, 2019-2025

(Percent of GDP)

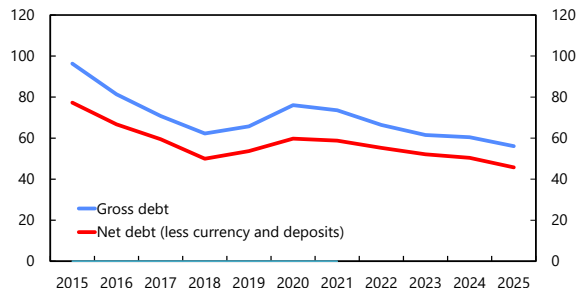


Source: Statistics Iceland.

Debt declined further in 2025, aided by the settlement of the IL Fund (previously HFF).

#### General Government Debt: 2015-2021

(Percent of GDP)



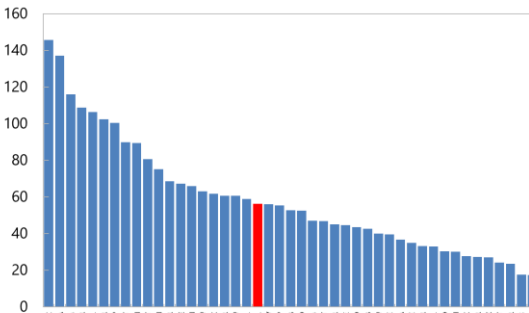
Source: Statistics Iceland.

Note: The settlement of the IL Fund (previously HFF) reduced government debt by around 5 percent of GDP in 2025.

Debt levels are below the average of advanced economies, but higher than most other Nordic countries.

#### General Government Debt, 2025

(Percent of GDP)



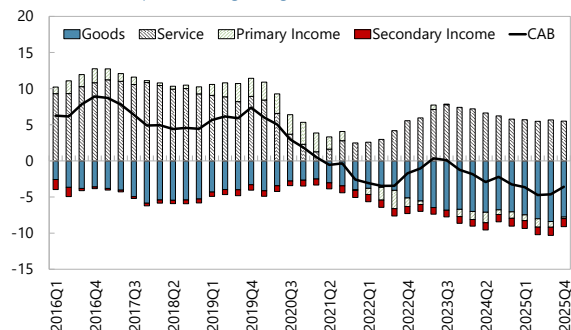
Sources: WEO, IMF staff calculations.

**Figure 4. Iceland: External Sector Developments**

The current account deterioration in 2024 and 2025 was driven by imported capital goods and idiosyncratic shocks.

#### Current Account Balance

(Percent of GDP; 4-quarter moving average)

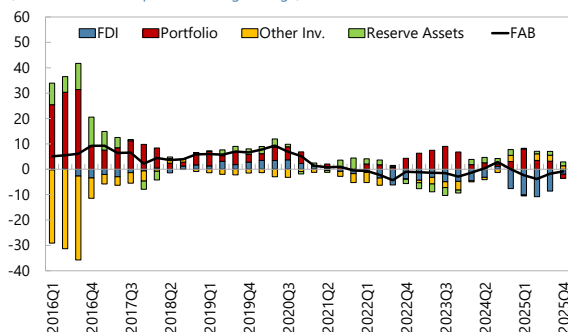


Source: Central Bank of Iceland.

Improvement in the financial account was driven by increasing FDI inflows.

#### Financial Account Balance

(Percent of GDP; 4-quarter moving average)

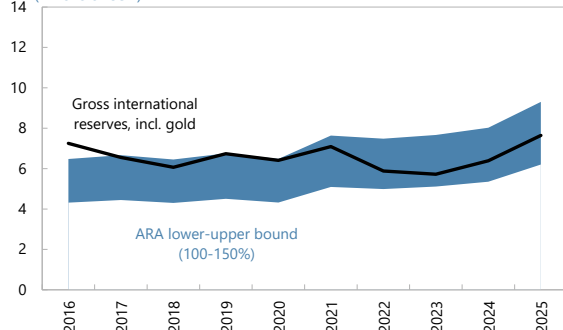


Sources: Haver Analytics, Central Bank of Iceland, IMF staff calculations.

Reserves increased in 2025 and moved toward the mid-point of the ARA metric.

#### Reserve Adequacy Level

(Billions of USD)

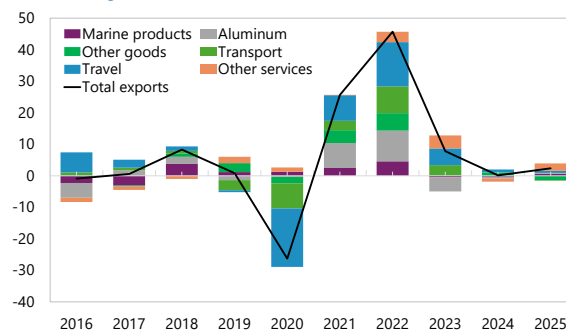


Sources: Central Bank of Iceland; and IMF staff calculations.

Export growth in 2025 was subdued

#### Nominal Exports (FOB) & Contributions of Subcomponents

(Percent change)

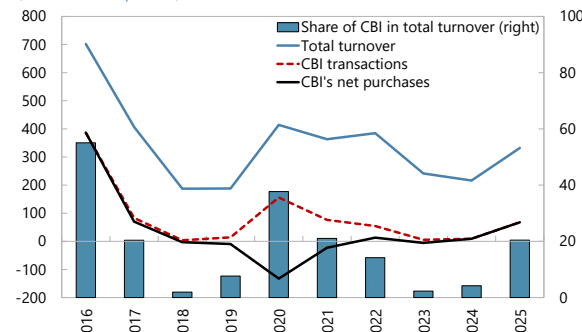


Sources: Statice and IMF staff calculations.

FX interbank market turnover increased in 2025 with CBI's temporary FX purchase program.

#### FX Market Turnover and Interventions

(Billion ISK, and percent)

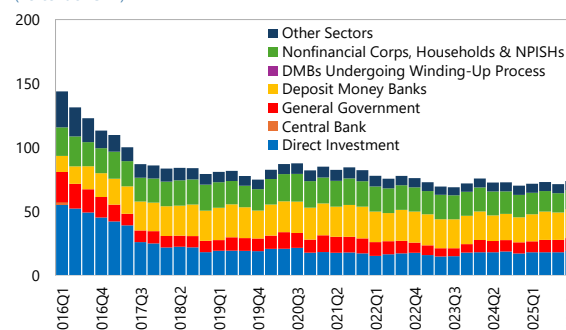


Source: Central Bank of Iceland.

External debt has been broadly stable.

#### External Debt, 2016-25

(Percent of GDP)



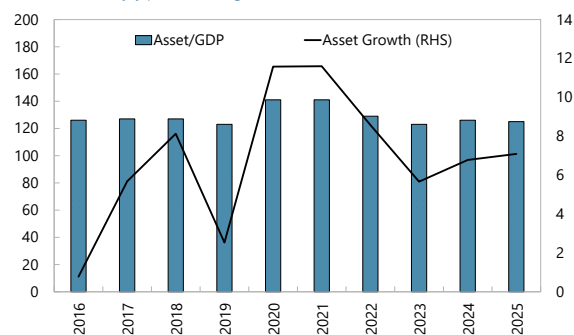
Sources: Haver Analytics, Central Bank of Iceland, and Statistics Iceland.

# Figure 5. Iceland: Banking Sector Developments

*Banks' assets are growing broadly in line with GDP.*

## Banking System Assets

(Percent of GDP, y/y percent change)

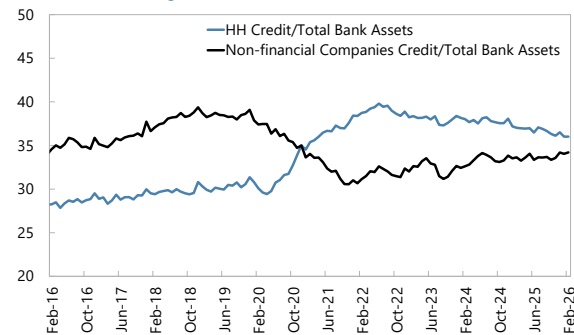


Source: Central Bank of Iceland.

*Banks' relative exposure to households is gradually declining in line with household deleveraging.*

## Exposure to Households and Non-Financial Corporations

(Percent of total banking sector assets)

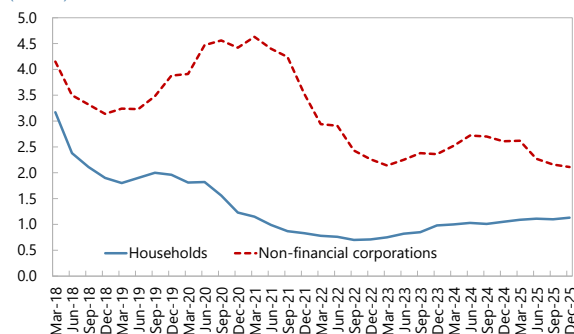


Source: Central Bank of Iceland.

*Non-performing loans remained broadly stable at a low level.*

## Non-Performing Loan Ratios

(Percent)

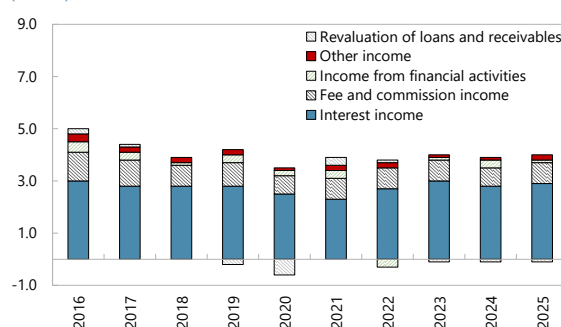


Source: Central Bank of Iceland.

*Bank profitability is sound, aided by robust net interest income.*

## Banks' Operating Income to Total Assets

(Percent)

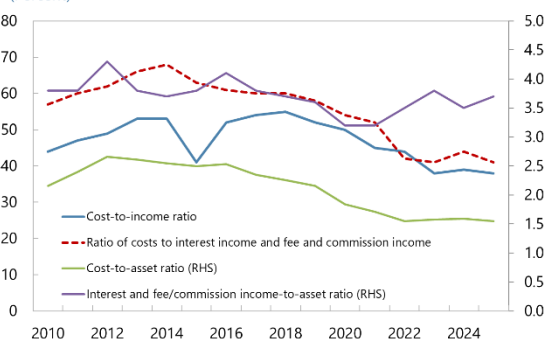


Source: Central Bank of Iceland.

*While net interest income has gone up, banks are managing their overall costs.*

## Cost Indicators of Icelandic Banks

(Percent)

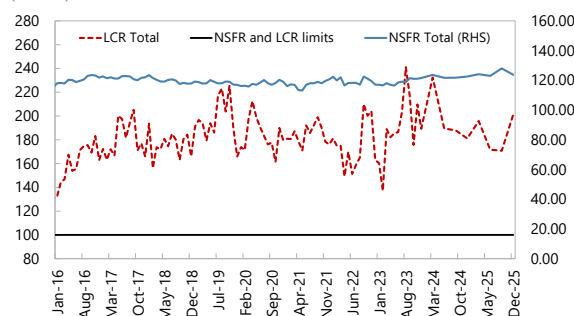


Sources: Central Bank of Iceland.

*Liquidity buffers remain ample.*

## Liquidity Requirement

(Percent)



Source: Central Bank of Iceland.

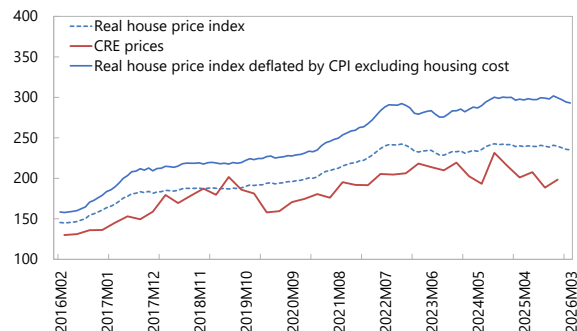
Note: LCR limit is for all currencies combined.

**Figure 6. Iceland: Housing Market Developments**

*Real house price growth slowed through 2025, while CRE prices declined...*

#### Real Estate Indices

(Index, 2000M3=100)

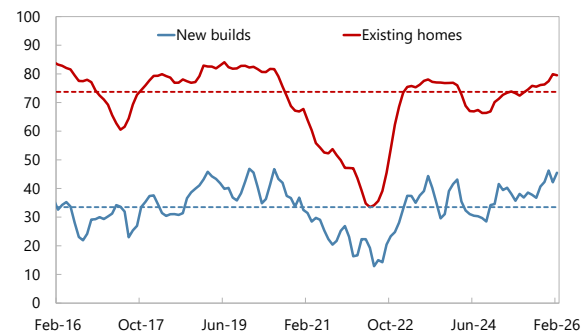


Sources: Statistics Iceland; CBI; and IMF staff calculations.

*...and the share of properties selling for below the asking price has risen.*

#### Share of Homes Selling below Asking Price

(Percent, 3-month moving average)

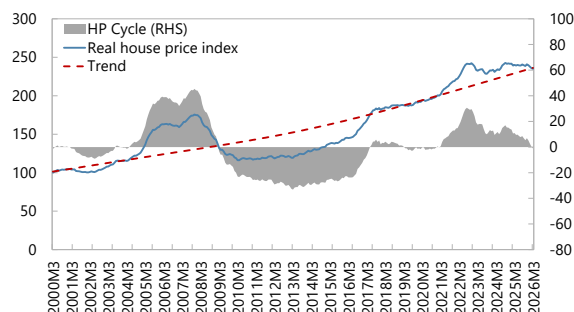


Source: Central Bank of Iceland.

*House prices are broadly in line with fundamentals.*

#### Real House Price: Trend and Cycle

(Index, 2000M3=100)

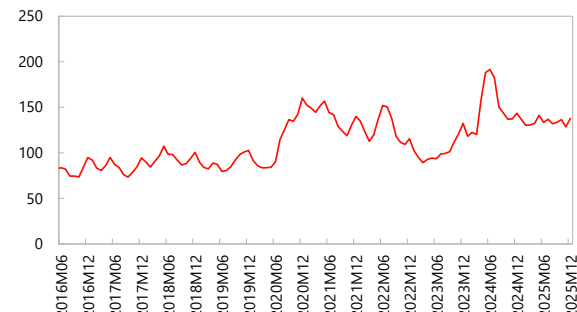


Sources: Statistics Iceland; Central Bank of Iceland; and IMF staff calculations.  
Note: Trend and cycle are constructed using Hodrick-Prescott (HP) filters.

*...while real estate turnover has moderated.*

#### Real Estate Turnover

(Index, December 2019 = 100)

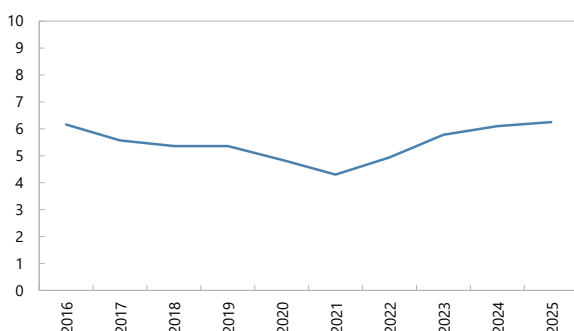


Sources: Registers Iceland and IMF staff calculations.  
Notes: Three-month moving average and deflated by the CPI.

*Higher interest rates have increased the debt service burden on households' mortgage loans.*

#### Household Interest Payment to Disposable Income

(Percent)

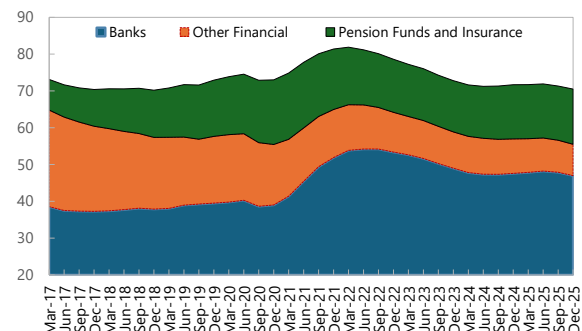


Source: Central Bank of Iceland

*Tighter financial conditions have triggered a decline in household indebtedness.*

#### Household Loans by Source

(Percent of GDP)



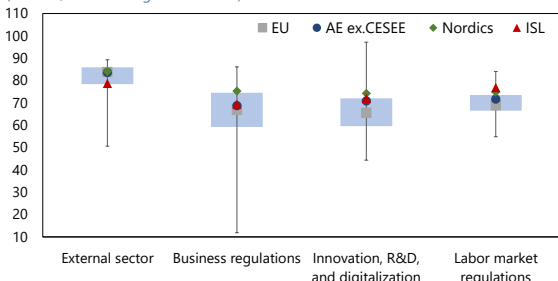
Sources: Statistics Iceland, Central Bank of Iceland and IMF staff calculations

Figure 7. Iceland: Structural Developments

Iceland lags peers in the strictness of business regulations, innovation and digitalization, and (services) trade...

#### Closeness to Frontier in Macrostructural Areas, 2022

(Percent, Relative to global frontier)

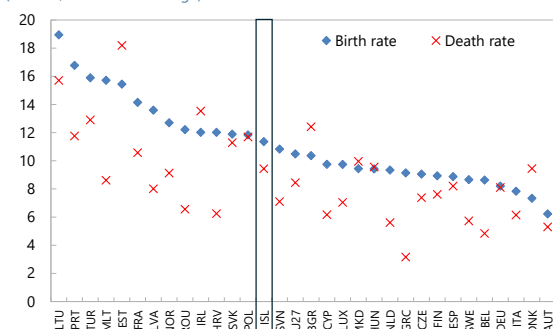


Sources: Fraser Institute; OECD; GTA; Eurostat; Berkley; IMF, World Bank; and IMF staff calculations.  
Note: Global frontier is defined as the average of top 3. Frontier = 100; all other values are normalized to this reference. The whiskers represent the range between the minimum and maximum values, while the bars indicate the interquartile range, spanning from the 25th to the 75th quartile. Regional numbers are simple average.

Firm entry and exit rates compare relatively favorably, but there is still room for improvement.

#### Enterprise Birth Rate and Death Rate

(Percent, 2022–2023 Average)

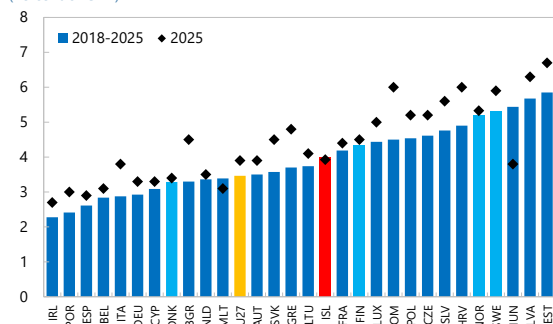


Sources: Eurostat, IMF staff calculations.

Public investment as share of GDP lags Nordic peers.

#### Gross Public Fixed Investment

(Percent of GDP)

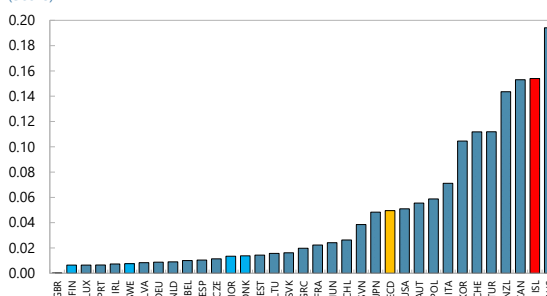


Sources: OECD, IMF staff calculations.

...while FDI regulations are also stricter than the OECD average and most advanced economies.

#### FDI Regulatory Restrictiveness (2024)

(Score)



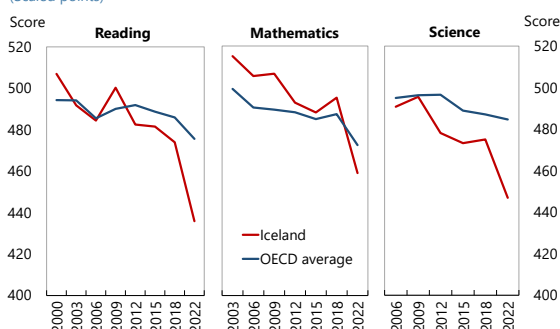
Sources: OECD FDI Regulatory Restrictiveness Index

Note: The index measures statutory restrictions FDI across 22 sectors. The score ranges from 0 (open) to 1 (closed).

Iceland's PISA scores have fallen sharply over the last decade.

#### Relative PISA Scores

(Scaled points)

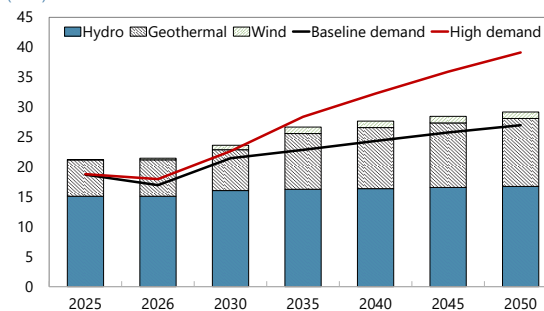


Sources: OECD, PISA 2022 database.

Energy demand set to outpace supply over time, suggesting need for expanded supply/entry into energy sector.

#### Energy Demand and Supply

(TWh)



Sources: Iceland Energy Forecast 2025–2050 (Landsnet, National Energy Authority, Power Regulatory Authority)

Table 1. Iceland: Selected Economic Indicators, 2021–31

|                                                | 2021                                           | 2022   | 2023   | 2024   | 2025   | 2026   | 2027   | 2028   | 2029   | 2030   | 2031   |
|------------------------------------------------|------------------------------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
|                                                | Projections                                    |        |        |        |        |        |        |        |        |        |        |
|                                                | (Percentage change unless otherwise indicated) |        |        |        |        |        |        |        |        |        |        |
| National Accounts (constant prices)            |                                                |        |        |        |        |        |        |        |        |        |        |
| Gross domestic product                         | 5.2                                            | 8.9    | 5.0    | -1.3   | 1.3    | 1.8    | 2.1    | 2.4    | 2.4    | 2.4    | 2.4    |
| Total domestic demand                          | 7.9                                            | 8.0    | 2.5    | 1.4    | 3.9    | 0.4    | 2.1    | 2.4    | 2.5    | 2.5    | 2.5    |
| Private consumption                            | 8.1                                            | 7.6    | 0.4    | 0.9    | 4.3    | 1.7    | 2.1    | 2.5    | 2.5    | 2.5    | 2.5    |
| Public consumption                             | 2.5                                            | 1.7    | 2.4    | 1.8    | 1.2    | 1.5    | 1.5    | 1.5    | 1.5    | 1.5    | 1.5    |
| Gross fixed investment                         | 13.5                                           | 15.3   | 6.2    | 6.5    | 4.0    | -2.9   | 2.7    | 3.2    | 3.6    | 3.6    | 3.6    |
| Net exports (contribution to growth)           | -2.8                                           | 0.6    | 2.5    | -2.6   | -2.7   | 1.4    | -0.1   | -0.1   | -0.2   | -0.2   | -0.3   |
| Exports of goods and services                  | 12.4                                           | 26.1   | 3.9    | -2.2   | 1.0    | 0.5    | 4.0    | 3.5    | 3.2    | 3.1    | 3.1    |
| Imports of goods and services                  | 20.3                                           | 22.6   | -1.9   | 4.2    | 7.2    | -2.4   | 3.8    | 3.5    | 3.4    | 3.4    | 3.4    |
| Output gap (percent of potential output)       | -3.8                                           | 1.6    | 3.6    | 0.3    | -0.1   | -0.3   | -0.3   | -0.1   | 0.0    | 0.0    | 0.0    |
| Selected Indicators                            |                                                |        |        |        |        |        |        |        |        |        |        |
| Gross domestic product (ISK bn.)               | 3,332                                          | 3,947  | 4,373  | 4,578  | 4,956  | 5,351  | 5,645  | 5,937  | 6,259  | 6,590  | 6,937  |
| Gross domestic product (\$ Mn.)                | 26,235                                         | 29,176 | 31,702 | 33,187 | 38,583 | 43,664 | 46,316 | 48,777 | 51,189 | 53,619 | 56,153 |
| GDP per capita (\$ thousands)                  | 73.2                                           | 80.0   | 84.5   | 86.5   | 99.1   | 109.7  | 114.0  | 117.6  | 121.0  | 124.2  | 127.5  |
| Private consumption (percent of GDP)           | 51.2                                           | 49.8   | 48.7   | 49.1   | 49.6   | 49.2   | 49.1   | 49.1   | 48.9   | 48.9   | 48.8   |
| Public consumption (percent of GDP)            | 27.4                                           | 25.5   | 25.2   | 25.9   | 26.1   | 26.0   | 26.0   | 26.0   | 25.9   | 25.8   | 25.7   |
| Gross fixed investment (percent of GDP)        | 22.5                                           | 23.8   | 24.9   | 26.8   | 26.7   | 24.6   | 24.8   | 25.0   | 25.2   | 25.4   | 25.6   |
| Gross national saving (percent of GDP)         | 20.2                                           | 22.5   | 24.2   | 23.0   | 23.0   | 23.3   | 24.0   | 24.5   | 25.0   | 25.5   | 25.8   |
| Unemployment rate (percent of labor force)     | 5.8                                            | 3.6    | 3.4    | 3.4    | 4.3    | 4.3    | 4.2    | 4.0    | 4.0    | 4.0    | 4.0    |
| Employment                                     | 3.4                                            | 7.0    | 3.6    | 4.1    | -0.6   | -0.4   | 0.6    | 1.1    | 1.1    | 1.1    | 0.0    |
| Labor productivity                             | 1.7                                            | 1.7    | 1.4    | -5.1   | 1.9    | 2.2    | 1.5    | 1.3    | 1.3    | 1.3    | 1.3    |
| Real wages                                     | 3.7                                            | 0.0    | 0.9    | 0.7    | 3.7    | 1.2    | 1.2    | 1.4    | 1.3    | 1.3    | 1.3    |
| Nominal wages                                  | 8.3                                            | 8.3    | 9.8    | 6.6    | 7.9    | 6.5    | 4.5    | 3.9    | 3.9    | 3.8    | 3.8    |
| Consumer price index (average)                 | 4.5                                            | 8.3    | 8.7    | 5.9    | 4.1    | 5.2    | 3.2    | 2.5    | 2.5    | 2.5    | 2.5    |
| Consumer price index (end period)              | 5.1                                            | 9.6    | 7.7    | 4.7    | 4.5    | 5.1    | 2.6    | 2.5    | 2.5    | 2.5    | 2.5    |
| Core CPI (average)                             | 4.3                                            | 7.6    | 8.6    | 6.1    | 4.2    | 6.1    | 2.7    | 2.5    | 2.5    | ...    | ...    |
| ISK/€ (average)                                | 148                                            | 159    | 163    | 164    | 152    | ...    | ...    | ...    | ...    | ...    | ...    |
| ISK/\$ (average)                               | 127                                            | 135    | 138    | 138    | 128    | ...    | ...    | ...    | ...    | ...    | ...    |
| Terms of trade (average)                       | 4.0                                            | 2.1    | -4.9   | 1.7    | 3.4    | 3.1    | -0.7   | -0.3   | 0.4    | 0.1    | 0.1    |
| Money and Credit (end period)                  |                                                |        |        |        |        |        |        |        |        |        |        |
| Base money (M0)                                | 9.0                                            | 1.5    | -21.5  | 16.7   | 2.9    | 13.5   | 11.8   | 10.9   | 9.9    | 9.2    | 8.7    |
| Broad money (M3)                               | 10.9                                           | 8.9    | 8.3    | 11.7   | 5.6    | 10.9   | 9.5    | 7.6    | 6.7    | 6.2    | 5.9    |
| Credit to nonfinancial private sector          | 10.5                                           | 11.3   | 5.2    | 8.1    | 5.3    | 5.9    | 7.0    | 6.3    | 5.7    | 5.3    | 5.2    |
| Central bank 7 day term deposit rate 1/        | 2.00                                           | 6.00   | 9.25   | 8.50   | 7.25   | 7.75   | ...    | ...    | ...    | ...    | ...    |
| (Percent of GDP unless otherwise indicated)    |                                                |        |        |        |        |        |        |        |        |        |        |
| General Government Finances 2/3/               |                                                |        |        |        |        |        |        |        |        |        |        |
| Revenue                                        | 40.7                                           | 42.3   | 43.1   | 42.9   | 42.6   | 43.2   | 43.3   | 43.1   | 43.2   | 43.2   | 43.2   |
| Expenditure                                    | 48.7                                           | 46.2   | 45.2   | 47.1   | 45.0   | 44.6   | 43.9   | 43.5   | 43.3   | 43.2   | 43.1   |
| Overall balance                                | -8.0                                           | -3.8   | -2.1   | -4.2   | -2.4   | -1.5   | -0.6   | -0.4   | -0.2   | -0.1   | 0.0    |
| Cyclically-adjusted primary balance            | -3.7                                           | -1.3   | -0.8   | -1.2   | 0.5    | 1.5    | 1.7    | 1.9    | 2.0    | 2.2    | 2.3    |
| Structural primary balance 4/                  | -0.3                                           | 0.1    | -0.2   | 0.9    | 0.9    | 1.7    | 1.8    | 1.9    | 2.0    | 2.2    | 2.3    |
| Gross debt                                     | 73.6                                           | 66.4   | 61.5   | 60.4   | 56.1   | 54.6   | 52.9   | 51.6   | 50.0   | 48.6   | 47.5   |
| Net debt                                       | 58.8                                           | 55.3   | 52.1   | 50.4   | 45.8   | 45.1   | 43.8   | 43.0   | 41.8   | 40.8   | 40.1   |
| Balance of Payments                            |                                                |        |        |        |        |        |        |        |        |        |        |
| Current account balance                        | -2.6                                           | -1.7   | -1.2   | -3.2   | -3.6   | -1.3   | -0.8   | -0.5   | -0.1   | 0.1    | 0.2    |
| of which: services balance                     | 2.5                                            | 5.6    | 7.4    | 5.8    | 5.5    | 5.2    | 5.3    | 5.8    | 6.4    | 6.8    | 7.2    |
| Capital and financial account (+ = outflow)    | -0.5                                           | -1.0   | -3.0   | 0.0    | 2.4    | -1.3   | -0.8   | -0.5   | -0.1   | 0.1    | 0.2    |
| of which: direct investment, net (+ = outflow) | -1.7                                           | -3.9   | -4.8   | -7.6   | -1.9   | -3.2   | -3.2   | -3.2   | -3.2   | -3.0   | -3.0   |
| Gross external debt                            | 83.1                                           | 74.3   | 73.7   | 67.9   | 61.7   | 56.0   | 54.2   | 52.8   | 51.5   | 50.4   | 49.3   |
| Central bank reserves (\$ Mn.)                 | 7,091                                          | 5,879  | 5,720  | 6,387  | 7,643  | 7,916  | 8,248  | 8,565  | 8,978  | 9,308  | 9,642  |

Sources: Central Bank of Iceland; Ministry of Finance; Statistics Iceland; and IMF staff projections.

1/ For 2026, policy rate as of the May MPC meeting.

2/ In April 2025, an agreement was reached on the settlement of remaining outstanding liabilities in the IL Fund (HFF).

3/ There is large uncertainty on the 2025 fiscal outcome, and numbers may be revised.

4/ Cyclically-adjusted primary balance excluding one offs.

**Table 2. Iceland: Money and Banking, 2021–31**  
(Billions of krónur unless otherwise indicated)

|                                                        | 2021        | 2022   | 2023   | 2024   | 2025  | 2026   | 2027   | 2028   | 2029   | 2030   | 2031   |
|--------------------------------------------------------|-------------|--------|--------|--------|-------|--------|--------|--------|--------|--------|--------|
|                                                        | Projections |        |        |        |       |        |        |        |        |        |        |
| <b>Central Bank</b>                                    |             |        |        |        |       |        |        |        |        |        |        |
| Net foreign assets                                     | 828         | 755    | 711    | 807    | 894   | 867    | 911    | 954    | 1,010  | 1,056  | 1,103  |
| Assets                                                 | 923         | 837    | 790    | 885    | 968   | 940    | 983    | 1,026  | 1,082  | 1,128  | 1,175  |
| Liabilities                                            | 95          | 82     | 79     | 78     | 74    | 72     | 72     | 72     | 72     | 72     | 72     |
| Net domestic assets                                    | -668        | -592   | -583   | -658   | -741  | -730   | -716   | -738   | -773   | -796   | -821   |
| Central government, net                                | -350        | -300   | -264   | -321   | -378  | -361   | -361   | -361   | -361   | -361   | -362   |
| Assets                                                 | 22          | 19     | 22     | 23     | 19    | 19     | 19     | 19     | 19     | 19     | 20     |
| of which: recapitalization bond                        | 0           | 0      | 8      | 4      | 13    | 0      | 0      | 0      | 0      | 0      | 1      |
| Liabilities                                            | 372         | 318    | 287    | 344    | 397   | 380    | 380    | 380    | 380    | 380    | 382    |
| of which: central government foreign currency deposits | 305         | 228    | 197    | 260    | 295   | 289    | 289    | 289    | 289    | 289    | 291    |
| Credit institutions (incl. nonbanks), net              | -189        | -183   | -228   | -258   | -296  | -315   | -354   | -377   | -411   | -435   | -460   |
| Assets                                                 | 8           | 6      | 1      | 0      | 0     | 0      | 0      | 0      | 0      | 0      | 0      |
| Liabilities                                            | 197         | 189    | 229    | 258    | 296   | 315    | 354    | 377    | 411    | 435    | 460    |
| of which: term deposits and CDs                        | 196         | 189    | 229    | 258    | 296   | 315    | 358    | 401    | 458    | 503    | 548    |
| Other items, net                                       | -128        | -109   | -91    | -79    | -66   | -54    | -87    | -73    | -57    | -39    | -18    |
| ESI (asset management company)                         | 1           | 2      | 2      | 1      | 1     | 1      | 0      | 0      | 0      | 0      | 1      |
| Total Expenditure                                      | 134         | 116    | 101    | 90     | 77    | 59     | 47     | 33     | 17     | -2     | -22    |
| Current Expenses                                       | 161         | 163    | 128    | 149    | 154   | 174    | 195    | 216    | 238    | 259    | 282    |
| Currency issued                                        | 82          | 81     | 76     | 71     | 69    | 68     | 118    | 134    | 150    | 166    | 183    |
| Deposit money banks' deposits at the central bank      | 79          | 82     | 52     | 78     | 84    | 71     | 77     | 82     | 88     | 93     | 99     |
| <b>Deposit Money Banks</b>                             |             |        |        |        |       |        |        |        |        |        |        |
| Net foreign assets                                     | -397        | -462   | -376   | -439   | -497  | -519   | -517   | -515   | -512   | -509   | -507   |
| Assets                                                 | 428         | 489    | 604    | 492    | 657   | 636    | 637    | 640    | 643    | 645    | 647    |
| Liabilities                                            | 825         | 952    | 981    | 931    | 1,154 | 1,154  | 1,154  | 1,154  | 1,154  | 1,154  | 1,154  |
| of which: bonds                                        | 710         | 748    | 773    | 743    | 960   | 960    | 960    | 960    | 960    | 960    | 960    |
| Nonfinancial Assets                                    | 2,666       | 2,940  | 3,071  | 3,459  | 3,419 | 4,062  | 4,354  | 4,636  | 4,904  | 5,166  | 5,433  |
| Central bank, net                                      | 279         | 278    | 289    | 343    | 318   | 322    | 372    | 421    | 482    | 533    | 584    |
| Assets                                                 | 282         | 280    | 290    | 344    | 318   | 323    | 372    | 421    | 483    | 534    | 584    |
| Liabilities                                            | 2           | 2      | 1      | 1      | 1     | 1      | 1      | 1      | 1      | 1      | 1      |
| Net Lending/Borrowing                                  | 235         | 250    | 266    | 343    | 303   | 318    | 326    | 334    | 342    | 351    | 363    |
| of which: bonds                                        | 202         | 212    | 215    | 285    | 246   | 262    | 269    | 278    | 285    | 294    | 307    |
| Financial Assets, Transactions                         | 3,507       | 3,870  | 4,036  | 4,389  | 4,634 | 4,912  | 5,255  | 5,585  | 5,903  | 6,214  | 6,540  |
| Nonfinancial                                           | 3,277       | 3,648  | 3,840  | 4,151  | 4,373 | 4,630  | 4,956  | 5,268  | 5,568  | 5,861  | 6,169  |
| Corporations                                           | 1,462       | 1,655  | 1,761  | 1,952  | 2,116 | 2,240  | 2,398  | 2,549  | 2,694  | 2,836  | 2,985  |
| Households                                             | 1,815       | 1,993  | 2,078  | 2,199  | 2,257 | 2,389  | 2,558  | 2,719  | 2,874  | 3,025  | 3,184  |
| Financial                                              | 231         | 221    | 197    | 238    | 261   | 283    | 300    | 318    | 335    | 353    | 371    |
| Other items, net                                       | -1,356      | -1,457 | -1,520 | -1,616 | -959  | -1,491 | -1,599 | -1,704 | -1,823 | -1,932 | -2,054 |
| Liabilities, Transactions                              | 2,268       | 2,478  | 2,695  | 3,021  | 3,187 | 3,543  | 3,836  | 4,121  | 4,392  | 4,657  | 4,926  |
| Krona deposits                                         | 2,002       | 2,181  | 2,387  | 2,720  | 2,868 | 3,188  | 3,452  | 3,709  | 3,952  | 4,191  | 4,433  |
| Foreign currency deposits                              | 266         | 296    | 308    | 301    | 319   | 355    | 384    | 413    | 440    | 466    | 493    |
| <b>Consolidated Banking System</b>                     |             |        |        |        |       |        |        |        |        |        |        |
| Net foreign assets                                     | 431         | 293    | 335    | 368    | 397   | 348    | 393    | 440    | 499    | 547    | 596    |
| Net domestic assets                                    | 1,912       | 2,257  | 2,427  | 2,716  | 2,860 | 3,263  | 3,561  | 3,816  | 4,043  | 4,277  | 4,514  |
| Broad money                                            | 2,343       | 2,550  | 2,763  | 3,085  | 3,257 | 3,611  | 3,955  | 4,255  | 4,542  | 4,823  | 5,109  |
| Net Debt                                               | 74          | 73     | 68     | 63     | 69    | 68     | 118    | 134    | 150    | 166    | 183    |

Sources: Central Bank of Iceland; and IMF staff projections.

**Table 3. Iceland: General Government Operations, 2021–31<sup>1/</sup>**  
(Percent of GDP)

|                                       | 2021        | 2022        | 2023        | 2024        | 2025        | 2026        | 2027        | 2028        | 2029        | 2030        | 2031        |
|---------------------------------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|
|                                       | Projections |             |             |             |             |             |             |             |             |             |             |
| <b>Total Revenue</b>                  | <b>40.7</b> | <b>42.3</b> | <b>43.1</b> | <b>42.9</b> | <b>42.6</b> | <b>43.2</b> | <b>43.3</b> | <b>43.1</b> | <b>43.2</b> | <b>43.2</b> | <b>43.2</b> |
| <b>Taxes</b>                          | <b>31.5</b> | <b>32.0</b> | <b>33.1</b> | <b>33.5</b> | <b>33.3</b> | <b>33.9</b> | <b>33.8</b> | <b>33.8</b> | <b>33.8</b> | <b>33.8</b> | <b>33.8</b> |
| Taxes on income and profits           | 17.2        | 17.8        | 18.6        | 18.6        | 18.5        | 18.4        | 18.4        | 18.4        | 18.5        | 18.5        | 18.5        |
| Personal income tax                   | 14.2        | 13.8        | 13.6        | 13.7        | 14.0        | 13.7        | 13.7        | 13.7        | 13.7        | 13.7        | 13.7        |
| Corporate income tax                  | 2.0         | 2.6         | 3.3         | 3.2         | 3.0         | 3.1         | 3.1         | 3.1         | 3.1         | 3.1         | 3.1         |
| Capital gains tax and rental income   | 1.0         | 1.4         | 1.7         | 1.7         | 1.5         | 1.6         | 1.6         | 1.6         | 1.6         | 1.6         | 1.6         |
| Taxes on payroll and workforce        | 0.3         | 0.3         | 0.3         | 0.3         | 0.2         | 0.3         | 0.3         | 0.3         | 0.3         | 0.2         | 0.2         |
| Taxes on property                     | 2.3         | 2.2         | 2.2         | 2.3         | 2.3         | 2.3         | 2.3         | 2.3         | 2.3         | 2.3         | 2.3         |
| Taxes on goods and services           | 11.3        | 11.2        | 11.6        | 11.8        | 11.8        | 12.3        | 12.4        | 12.3        | 12.3        | 12.3        | 12.2        |
| Value added tax                       | 8.5         | 8.3         | 8.8         | 8.9         | 8.8         | 9.1         | 9.1         | 9.0         | 9.0         | 9.0         | 9.0         |
| Other taxes on goods and services     | 2.7         | 2.9         | 2.8         | 2.9         | 3.0         | 3.3         | 3.3         | 3.3         | 3.3         | 3.3         | 3.3         |
| Taxes on international trade          | 0.1         | 0.2         | 0.1         | 0.1         | 0.2         | 0.1         | 0.1         | 0.1         | 0.1         | 0.1         | 0.1         |
| Other taxes                           | 0.4         | 0.4         | 0.3         | 0.4         | 0.4         | 0.4         | 0.4         | 0.4         | 0.4         | 0.4         | 0.4         |
| <b>Social contributions</b>           | <b>2.9</b>  | <b>2.9</b>  | <b>3.0</b>  | <b>3.0</b>  | <b>3.1</b>  | <b>3.0</b>  | <b>3.1</b>  | <b>3.2</b>  | <b>3.3</b>  | <b>3.3</b>  | <b>3.3</b>  |
| <b>Grants</b>                         | <b>0.2</b>  | <b>0.2</b>  | <b>0.1</b>  | <b>0.2</b>  | <b>0.2</b>  | <b>0.1</b>  | <b>0.1</b>  | <b>0.1</b>  | <b>0.1</b>  | <b>0.1</b>  | <b>0.1</b>  |
| <b>Other revenues</b>                 | <b>6.0</b>  | <b>7.2</b>  | <b>6.9</b>  | <b>6.3</b>  | <b>6.0</b>  | <b>6.2</b>  | <b>6.3</b>  | <b>6.0</b>  | <b>6.0</b>  | <b>6.0</b>  | <b>6.0</b>  |
| Property income                       | 2.9         | 4.3         | 4.0         | 3.3         | 3.1         | 3.2         | 3.4         | 3.1         | 3.1         | 3.1         | 3.1         |
| of which: interest income             | 1.8         | 2.6         | 2.5         | 1.5         | 1.3         | 1.4         | 1.5         | 1.2         | 1.2         | 1.2         | 1.2         |
| <b>Total Expenditure</b>              | <b>48.7</b> | <b>46.2</b> | <b>45.2</b> | <b>47.1</b> | <b>45.0</b> | <b>44.6</b> | <b>43.9</b> | <b>43.5</b> | <b>43.3</b> | <b>43.2</b> | <b>43.1</b> |
| <b>Current Expenses</b>               | <b>47.3</b> | <b>44.8</b> | <b>43.9</b> | <b>45.9</b> | <b>43.8</b> | <b>43.5</b> | <b>42.8</b> | <b>42.4</b> | <b>42.2</b> | <b>42.1</b> | <b>42.0</b> |
| Compensation of employees             | 15.3        | 14.4        | 13.8        | 14.2        | 14.3        | 14.3        | 14.2        | 14.1        | 14.0        | 13.9        | 13.9        |
| Use of goods and services             | 11.6        | 10.9        | 11.1        | 11.5        | 11.5        | 11.4        | 11.3        | 11.2        | 11.2        | 11.1        | 11.1        |
| Consumption of fixed capital          | 3.0         | 2.7         | 2.7         | 2.8         | 2.8         | 2.7         | 2.7         | 2.7         | 2.7         | 2.7         | 2.7         |
| Interest                              | 3.9         | 5.9         | 5.6         | 4.6         | 4.3         | 4.1         | 3.6         | 3.4         | 3.4         | 3.4         | 3.4         |
| Subsidies                             | 1.6         | 1.5         | 1.5         | 1.6         | 1.4         | 1.4         | 1.4         | 1.4         | 1.4         | 1.4         | 1.4         |
| Grants                                | 0.3         | 0.3         | 0.4         | 0.3         | 0.3         | 0.4         | 0.4         | 0.4         | 0.4         | 0.4         | 0.4         |
| Social benefits                       | 9.2         | 7.2         | 6.7         | 7.1         | 7.2         | 7.2         | 7.2         | 7.2         | 7.2         | 7.2         | 7.2         |
| Other expense                         | 2.3         | 1.9         | 2.0         | 3.6         | 2.0         | 2.0         | 2.0         | 2.0         | 2.0         | 2.0         | 2.0         |
| <b>Nonfinancial Assets</b>            | <b>1.4</b>  | <b>1.3</b>  | <b>1.3</b>  | <b>1.2</b>  | <b>1.2</b>  | <b>1.1</b>  | <b>1.1</b>  | <b>1.1</b>  | <b>1.1</b>  | <b>1.1</b>  | <b>1.1</b>  |
| Nonfinancial assets, acquisition      | 4.4         | 4.1         | 4.1         | 4.1         | 4.0         | 3.8         | 3.8         | 3.8         | 3.8         | 3.8         | 3.8         |
| Consumption of fixed capital (-)      | -3.0        | -2.7        | -2.7        | -2.8        | -2.8        | -2.7        | -2.7        | -2.7        | -2.7        | -2.7        | -2.7        |
| <b>Overall Balance</b>                | <b>-8.0</b> | <b>-3.8</b> | <b>-2.1</b> | <b>-4.2</b> | <b>-2.4</b> | <b>-1.5</b> | <b>-0.6</b> | <b>-0.4</b> | <b>-0.2</b> | <b>-0.1</b> | <b>0.0</b>  |
| <b>Financial Assets, Transactions</b> | <b>-2.4</b> | <b>1.8</b>  | <b>1.5</b>  | <b>-3.6</b> | <b>-0.2</b> | <b>1.5</b>  | <b>1.5</b>  | <b>1.5</b>  | <b>1.5</b>  | <b>1.5</b>  | <b>1.5</b>  |
| Currency and deposits                 | 0.3         | -1.4        | -0.5        | 1.0         | 1.1         | 0.0         | 0.0         | 0.0         | 0.0         | 0.0         | 0.0         |
| Securities other than shares          | 0.1         | -0.4        | -0.3        | -0.8        | -1.0        | 0.0         | 0.0         | 0.0         | 0.0         | 0.0         | 0.0         |
| Loans                                 | -1.4        | 0.5         | -2.3        | -0.2        | 1.4         | 1.5         | 1.5         | 1.5         | 1.5         | 1.5         | 1.5         |
| Shares and other equities             | -1.7        | 2.9         | 0.5         | 0.5         | -0.1        | 0.0         | 0.0         | 0.0         | 0.0         | 0.0         | 0.0         |
| Other accounts receivable             | 0.3         | 0.1         | 4.1         | -4.0        | -1.4        | 0.0         | 0.0         | 0.0         | 0.0         | 0.0         | 0.0         |
| <b>Liabilities, Transactions</b>      | <b>5.5</b>  | <b>5.6</b>  | <b>3.6</b>  | <b>0.6</b>  | <b>2.2</b>  | <b>2.9</b>  | <b>2.1</b>  | <b>1.9</b>  | <b>1.7</b>  | <b>1.6</b>  | <b>1.5</b>  |
| Securities other than shares          | 1.9         | 3.5         | 1.7         | -0.8        | -3.5        | 2.8         | 2.3         | 1.9         | 1.7         | 2.4         | 1.6         |
| Loans                                 | 3.6         | 0.7         | 0.7         | 2.4         | 4.7         | 0.1         | -0.3        | 0.0         | 0.0         | -0.8        | 0.0         |
| Krona denominated                     | 0.6         | 2.6         | 1.6         | 0.1         | 3.4         | 0.0         | 0.0         | 0.0         | 0.0         | 0.0         | 0.0         |
| Foreign currency denominated          | 3.0         | -1.9        | -0.9        | 2.3         | 1.3         | 0.1         | -0.3        | 0.0         | 0.0         | -0.8        | 0.0         |
| Insurance technical reserves          | 0.1         | 0.4         | 0.7         | -0.4        | 1.5         | 0.0         | 0.1         | 0.0         | 0.0         | 0.0         | -0.1        |
| Other accounts payable                | -0.1        | 0.9         | 0.6         | -0.5        | -0.4        | 0.0         | 0.0         | 0.0         | 0.0         | 0.0         | 0.0         |
| <b>Gross Debt 2/</b>                  | <b>73.6</b> | <b>66.4</b> | <b>61.5</b> | <b>60.4</b> | <b>56.1</b> | <b>54.6</b> | <b>52.9</b> | <b>51.6</b> | <b>50.0</b> | <b>48.6</b> | <b>47.5</b> |
| Krona denominated                     | 63.2        | 59.7        | 56.3        | 53.2        | 48.2        | 47.1        | 46.1        | 45.1        | 43.8        | 43.6        | 41.8        |
| Foreign currency denominated          | 10.4        | 6.8         | 5.2         | 7.2         | 8.0         | 7.5         | 6.8         | 6.5         | 6.1         | 5.0         | 5.7         |
| <b>Net Debt 3/</b>                    | <b>58.8</b> | <b>55.3</b> | <b>52.1</b> | <b>50.4</b> | <b>45.8</b> | <b>45.1</b> | <b>43.8</b> | <b>43.0</b> | <b>41.8</b> | <b>40.8</b> | <b>40.1</b> |
| <b>Memorandum Items:</b>              |             |             |             |             |             |             |             |             |             |             |             |
| Primary revenue                       | 38.9        | 39.8        | 40.6        | 41.4        | 41.2        | 41.8        | 41.9        | 41.9        | 42.0        | 42.0        | 42.0        |
| Primary expenditure                   | 44.7        | 40.3        | 39.6        | 42.5        | 40.7        | 40.5        | 40.3        | 40.1        | 39.9        | 39.8        | 39.7        |
| Primary balance                       | -5.8        | -0.5        | 1.0         | -1.1        | 0.5         | 1.3         | 1.6         | 1.9         | 2.1         | 2.2         | 2.3         |
| Structural balance 4/                 | -2.5        | -3.2        | -3.4        | -2.2        | -2.0        | -1.1        | -0.3        | -0.3        | -0.2        | -0.1        | 0.0         |
| Structural primary balance 4/         | -0.3        | 0.1         | -0.2        | 0.9         | 0.9         | 1.7         | 1.8         | 1.9         | 2.0         | 2.2         | 2.3         |
| Gross domestic product (ISK bn)       | 3,332       | 3,947       | 4,373       | 4,578       | 4,956       | 5,351       | 5,645       | 5,937       | 6,259       | 6,590       | 6,937       |

Sources: Ministry of Finance; Statistics Iceland; and IMF staff projections.

1/ There is large uncertainty on the 2025 fiscal outcome, and numbers may be revised.

2/ In April 2025, an agreement was reached on the settlement of remaining outstanding liabilities in the IL Fund (HFF).

3/ Gross debt less currency and deposits.

4/ Cyclically-adjusted balance excluding one-offs.

**Table 4. Iceland: General Government Financial Balance Sheet, 2021–31**  
(Percent of GDP)

|                               | 2021         | 2022         | 2023         | 2024         | 2025         | 2026         | 2027         | 2028         | 2029         | 2030         | 2031         |
|-------------------------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
|                               | Projections  |              |              |              |              |              |              |              |              |              |              |
| <b>Financial assets</b>       | <b>73.1</b>  | <b>63.4</b>  | <b>57.8</b>  | <b>55.6</b>  | <b>52.4</b>  | <b>50.0</b>  | <b>48.9</b>  | <b>48.0</b>  | <b>47.0</b>  | <b>46.1</b>  | <b>45.3</b>  |
| Currency and deposits         | 14.8         | 11.2         | 9.4          | 10.0         | 10.3         | 9.6          | 9.1          | 8.6          | 8.2          | 7.8          | 7.4          |
| Other assets                  | 58.2         | 52.2         | 48.4         | 45.6         | 42.1         | 40.5         | 39.8         | 39.4         | 38.8         | 38.4         | 37.9         |
| Securities other than shares  | 4.3          | 3.2          | 2.7          | 1.7          | 0.6          | 0.5          | 0.5          | 0.5          | 0.4          | 0.4          | 0.4          |
| Loans                         | 16.8         | 14.8         | 10.8         | 10.2         | 11.4         | 12.1         | 13.0         | 13.8         | 14.6         | 15.4         | 16.1         |
| Shares and other equities     | 31.1         | 27.8         | 25.5         | 24.9         | 22.9         | 21.2         | 20.0         | 19.0         | 18.0         | 17.1         | 16.3         |
| Other accounts receivable 1/  | 6.1          | 6.4          | 9.4          | 8.8          | 7.2          | 6.7          | 6.4          | 6.0          | 5.7          | 5.4          | 5.2          |
| <b>Liabilities</b>            | <b>107.6</b> | <b>98.3</b>  | <b>93.3</b>  | <b>89.8</b>  | <b>84.2</b>  | <b>80.7</b>  | <b>77.7</b>  | <b>75.2</b>  | <b>72.4</b>  | <b>69.8</b>  | <b>67.7</b>  |
| Gross debt                    | 73.6         | 66.4         | 61.5         | 60.4         | 56.1         | 54.6         | 52.9         | 51.6         | 50.0         | 48.6         | 47.5         |
| Securities other than shares  | 51.4         | 46.9         | 44.0         | 41.2         | 34.2         | 33.3         | 32.2         | 31.5         | 30.5         | 29.6         | 29.0         |
| Loans                         | 22.2         | 19.5         | 17.5         | 19.2         | 21.9         | 21.3         | 20.6         | 20.1         | 19.5         | 19.0         | 18.5         |
| Krona denominated             | 11.4         | 12.4         | 12.0         | 11.6         | 13.8         | 13.7         | 13.7         | 13.6         | 13.3         | 13.9         | 13.7         |
| Foreign currency denominated  | 10.7         | 7.1          | 5.5          | 7.6          | 8.1          | 7.6          | 6.9          | 6.6          | 6.2          | 5.1          | 4.8          |
| Other liabilities             | 34.0         | 31.9         | 31.8         | 29.3         | 28.1         | 26.0         | 24.8         | 23.6         | 22.4         | 21.3         | 20.1         |
| Insurance technical reserves  | 27.1         | 25.1         | 24.7         | 23.1         | 22.8         | 21.1         | 20.2         | 19.2         | 18.2         | 17.3         | 16.3         |
| Other accounts payable        | 6.9          | 6.8          | 7.0          | 6.2          | 5.3          | 4.9          | 4.7          | 4.4          | 4.2          | 4.0          | 3.8          |
| <b>Net financial worth 1/</b> | <b>-34.5</b> | <b>-34.9</b> | <b>-35.5</b> | <b>-34.1</b> | <b>-31.8</b> | <b>-30.6</b> | <b>-28.8</b> | <b>-27.2</b> | <b>-25.4</b> | <b>-23.7</b> | <b>-22.3</b> |
| <b>Memorandum item:</b>       |              |              |              |              |              |              |              |              |              |              |              |
| Net debt 2/                   | 58.8         | 55.3         | 52.1         | 50.4         | 45.8         | 45.1         | 43.8         | 43.0         | 41.8         | 40.8         | 40.1         |

Sources: Ministry of Finance; Statistics Iceland; and IMF staff projections.

1/ Assumes all assets of the institutions reclassified into the general government are financial.

2/ Gross debt less currency and deposits.

Table 5. Iceland: Balance of Payments, 2021–31

|                                                    | 2021                  | 2022         | 2023         | 2024          | 2025          | 2026         | 2027         | 2028         | 2029         | 2030         | 2031         |
|----------------------------------------------------|-----------------------|--------------|--------------|---------------|---------------|--------------|--------------|--------------|--------------|--------------|--------------|
|                                                    | Projections           |              |              |               |               |              |              |              |              |              |              |
|                                                    | (Millions of dollars) |              |              |               |               |              |              |              |              |              |              |
| <b>Current account</b>                             | <b>-677</b>           | <b>-501</b>  | <b>-389</b>  | <b>-1,077</b> | <b>-1,383</b> | <b>-560</b>  | <b>-382</b>  | <b>-238</b>  | <b>-75</b>   | <b>30</b>    | <b>112</b>   |
| Trade balance                                      | -394                  | 127          | 225          | -421          | -872          | -118         | -138         | -11          | 99           | 131          | 167          |
| Balance on goods                                   | -1,045                | -1,497       | -2,125       | -2,340        | -2,998        | -2,373       | -2,591       | -2,864       | -3,167       | -3,519       | -3,901       |
| Merchandise exports f.o.b.                         | 6,120                 | 7,531        | 6,815        | 6,966         | 7,400         | 8,796        | 9,066        | 8,692        | 8,504        | 8,768        | 9,041        |
| Merchandise imports f.o.b.                         | 7,165                 | 9,028        | 8,940        | 9,306         | 10,398        | 11,169       | 11,657       | 11,556       | 11,670       | 12,287       | 12,941       |
| Balance on services                                | 651                   | 1,624        | 2,350        | 1,920         | 2,126         | 2,255        | 2,453        | 2,853        | 3,266        | 3,650        | 4,068        |
| Exports of services, total                         | 3,682                 | 6,102        | 7,126        | 7,124         | 8,077         | 8,334        | 8,720        | 9,427        | 10,154       | 10,873       | 11,640       |
| Imports of services, total                         | 3,031                 | 4,478        | 4,776        | 5,204         | 5,951         | 6,079        | 6,267        | 6,575        | 6,888        | 7,223        | 7,572        |
| Primary income balance                             | -27                   | -344         | -319         | -296          | -85           | -49          | 122          | 159          | 201          | 261          | 324          |
| Receipts                                           | 763                   | 730          | 1,167        | 1,118         | 961           | 1,058        | 1,153        | 1,289        | 1,444        | 1,623        | 1,826        |
| of which: interest receipts                        | 45                    | 92           | 283          | 303           | 303           | 329          | 357          | 408          | 466          | 532          | 606          |
| Expenditures                                       | 790                   | 1,074        | 1,486        | 1,413         | 1,046         | 1,108        | 1,031        | 1,130        | 1,244        | 1,362        | 1,501        |
| of which: interest payments                        | 291                   | 378          | 765          | 927           | 858           | 841          | 685          | 695          | 707          | 709          | 717          |
| Secondary income balance                           | -256                  | -284         | -296         | -360          | -426          | -392         | -366         | -386         | -375         | -362         | -380         |
| <b>Capital and financial account (+ = outflow)</b> | <b>-122</b>           | <b>-306</b>  | <b>-951</b>  | <b>-7</b>     | <b>910</b>    | <b>-560</b>  | <b>-382</b>  | <b>-238</b>  | <b>-75</b>   | <b>30</b>    | <b>112</b>   |
| Capital account balance (+ = inflow)               | 8                     | -16          | -34          | -23           | 1,226         | 0            | 0            | 0            | 0            | 0            | 0            |
| Financial account (+ = outflow)                    | -130                  | -290         | -917         | 16            | -316          | -560         | -382         | -238         | -75          | 30           | 112          |
| Direct investment (+ = outflow)                    | -454                  | -1,136       | -1,515       | -2,527        | -738          | -1,397       | -1,476       | -1,550       | -1,622       | -1,615       | -1,691       |
| Portfolio investment ("+" = outflow)               | 20                    | 1,257        | 2,164        | 1,009         | -660          | 537          | 659          | 881          | 1,084        | 1,282        | 1,471        |
| Assets (+ = outflow)                               | 1,431                 | 1,005        | 2,036        | 2,033         | 1,613         | 1,176        | 1,330        | 1,440        | 1,525        | 1,597        | 1,658        |
| Liabilities (+ = inflow)                           | 1,411                 | -252         | -127         | 1,023         | 2,273         | 640          | 671          | 559          | 440          | 316          | 186          |
| Other investment (+ = outflow)                     | -924                  | -17          | -1,083       | 810           | 524           | 27           | 103          | 114          | 50           | 33           | -1           |
| Assets (+ = outflow)                               | 81                    | 882          | -238         | 910           | 560           | 392          | 274          | 192          | 134          | 94           | 66           |
| Liabilities (+ = inflow)                           | 1,005                 | 899          | 846          | 100           | 36            | 365          | 171          | 78           | 84           | 61           | 67           |
| Change in reserve assets (+ = increase/outflow)    | 1,143                 | -495         | -367         | 759           | 594           | 273          | 332          | 317          | 414          | 330          | 334          |
| <b>Net errors and omissions (+ = inflow)</b>       | <b>539</b>            | <b>226</b>   | <b>-494</b>  | <b>1,115</b>  | <b>-159</b>   | <b>0</b>     | <b>0</b>     | <b>0</b>     | <b>0</b>     | <b>0</b>     | <b>0</b>     |
|                                                    | (Percent of GDP)      |              |              |               |               |              |              |              |              |              |              |
| <b>Current account</b>                             | <b>-2.6</b>           | <b>-1.7</b>  | <b>-1.2</b>  | <b>-3.2</b>   | <b>-3.6</b>   | <b>-1.3</b>  | <b>-0.8</b>  | <b>-0.5</b>  | <b>-0.1</b>  | <b>0.1</b>   | <b>0.2</b>   |
| Trade balance                                      | -1.5                  | 0.4          | 0.7          | -1.3          | -2.3          | -0.3         | -0.3         | 0.0          | 0.2          | 0.2          | 0.3          |
| Balance on goods                                   | -4.0                  | -5.1         | -6.7         | -7.1          | -7.8          | -5.4         | -5.6         | -5.9         | -6.2         | -6.6         | -6.9         |
| Merchandise exports f.o.b.                         | 23.3                  | 25.8         | 21.5         | 21.0          | 19.2          | 20.1         | 19.6         | 17.8         | 16.6         | 16.4         | 16.1         |
| Merchandise imports f.o.b.                         | 27.3                  | 30.9         | 28.2         | 28.0          | 27.0          | 25.6         | 25.2         | 23.7         | 22.8         | 22.9         | 23.0         |
| Balance on services                                | 2.5                   | 5.6          | 7.4          | 5.8           | 5.5           | 5.2          | 5.3          | 5.8          | 6.4          | 6.8          | 7.2          |
| Exports of services, total                         | 14.0                  | 20.9         | 22.5         | 21.5          | 20.9          | 19.1         | 18.8         | 19.3         | 19.8         | 20.3         | 20.7         |
| Imports of services, total                         | 11.6                  | 15.3         | 15.1         | 15.7          | 15.4          | 13.9         | 13.5         | 13.5         | 13.5         | 13.5         | 13.5         |
| Primary income balance                             | -0.1                  | -1.2         | -1.0         | -0.9          | -0.2          | -0.1         | 0.3          | 0.3          | 0.4          | 0.5          | 0.6          |
| Receipts                                           | 2.9                   | 2.5          | 3.7          | 3.4           | 2.5           | 2.4          | 2.5          | 2.6          | 2.8          | 3.0          | 3.3          |
| of which: interest receipts                        | 0.2                   | 0.3          | 0.9          | 0.9           | 0.8           | 0.8          | 0.8          | 0.8          | 0.9          | 1.0          | 1.1          |
| Expenditures                                       | 3.0                   | 3.7          | 4.7          | 4.3           | 2.7           | 2.5          | 2.2          | 2.3          | 2.4          | 2.5          | 2.7          |
| of which: interest payments                        | 1.1                   | 1.3          | 2.4          | 2.8           | 2.2           | 1.9          | 1.5          | 1.4          | 1.4          | 1.3          | 1.3          |
| Secondary income balance                           | -1.0                  | -1.0         | -0.9         | -1.1          | -1.1          | -0.9         | -0.8         | -0.8         | -0.7         | -0.7         | -0.7         |
| <b>Capital and financial account (+ = outflow)</b> | <b>-0.5</b>           | <b>-1.0</b>  | <b>-3.0</b>  | <b>0.0</b>    | <b>2.4</b>    | <b>-1.3</b>  | <b>-0.8</b>  | <b>-0.5</b>  | <b>-0.1</b>  | <b>0.1</b>   | <b>0.2</b>   |
| Capital account balance (+ = inflow)               | 0.0                   | -0.1         | -0.1         | -0.1          | 3.2           | 0.0          | 0.0          | 0.0          | 0.0          | 0.0          | 0.0          |
| Financial account (+ = outflow)                    | -0.5                  | -1.0         | -2.9         | 0.0           | -0.8          | -1.3         | -0.8         | -0.5         | -0.1         | 0.1          | 0.2          |
| Direct investment (+ = outflow)                    | -1.7                  | -3.9         | -4.8         | -7.6          | -1.9          | -3.2         | -3.2         | -3.2         | -3.2         | -3.0         | -3.0         |
| Portfolio investment ("+" = outflow)               | 0.1                   | 4.3          | 6.8          | 3.0           | -1.7          | 1.2          | 1.4          | 1.8          | 2.1          | 2.4          | 2.6          |
| Assets (+ = outflow)                               | 5.5                   | 3.4          | 6.4          | 6.1           | 4.2           | 2.7          | 2.9          | 3.0          | 3.0          | 3.0          | 3.0          |
| Liabilities (+ = inflow)                           | 5.4                   | -0.9         | -0.4         | 3.1           | 5.9           | 1.5          | 1.4          | 1.1          | 0.9          | 0.6          | 0.3          |
| of which: net borrowing (+ = inflow)               | 5.7                   | -1.0         | -0.2         | 2.1           | 5.7           | 1.3          | 1.3          | 1.0          | 0.7          | 0.5          | 0.2          |
| Other investment (+ = outflow)                     | -3.5                  | -0.1         | -3.4         | 2.4           | 1.4           | 0.1          | 0.2          | 0.2          | 0.1          | 0.1          | 0.0          |
| Assets (+ = outflow)                               | 0.3                   | 3.0          | -0.7         | 2.7           | 1.5           | 0.9          | 0.6          | 0.4          | 0.3          | 0.2          | 0.1          |
| Liabilities (+ = inflow)                           | 3.8                   | 3.1          | 2.7          | 0.3           | 0.1           | 0.8          | 0.4          | 0.2          | 0.2          | 0.1          | 0.1          |
| Change in reserve assets (+ = increase/outflow)    | 4.4                   | -1.7         | -1.2         | 2.3           | 1.5           | 0.6          | 0.7          | 0.7          | 0.8          | 0.6          | 0.6          |
| <b>Net errors and omissions (+ = inflow)</b>       | <b>2.1</b>            | <b>0.8</b>   | <b>-1.6</b>  | <b>3.4</b>    | <b>-0.4</b>   | <b>0.0</b>   | <b>0.0</b>   | <b>0.0</b>   | <b>0.0</b>   | <b>0.0</b>   | <b>0.0</b>   |
| <b>Central bank reserves (\$ mn)</b>               | <b>7,091</b>          | <b>5,879</b> | <b>5,720</b> | <b>6,387</b>  | <b>7,643</b>  | <b>7,916</b> | <b>8,248</b> | <b>8,565</b> | <b>8,978</b> | <b>9,308</b> | <b>9,642</b> |
| (Percent of GDP)                                   | 27.0                  | 20.2         | 18.0         | 19.2          | 19.8          | 18.1         | 17.8         | 17.6         | 17.5         | 17.4         | 17.2         |
| (Percent of reserve adequacy metric)               | 139.3                 | 117.8        | 111.9        | 119.4         | 123.2         | 123.3        | 122.1        | 124.8        | 124.6        | 124.7        | 124.2        |
| <b>Memorandum item:</b>                            |                       |              |              |               |               |              |              |              |              |              |              |
| Gross domestic product (\$ mn)                     | 26,235                | 29,176       | 31,702       | 33,187        | 38,583        | 43,664       | 46,316       | 48,777       | 51,189       | 53,619       | 56,153       |

Sources: Central Bank of Iceland; and IMF staff projections.

**Table 6. Iceland: International Investment Position, 2015–25**  
(Percent of GDP)

|                                              | 2015         | 2016         | 2017         | 2018         | 2019         | 2020         | 2021         | 2022         | 2023         | 2024         | 2025         |
|----------------------------------------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|
| <b>Assets</b>                                | <b>211.2</b> | <b>156.0</b> | <b>115.3</b> | <b>118.9</b> | <b>128.9</b> | <b>152.4</b> | <b>168.7</b> | <b>133.6</b> | <b>134.0</b> | <b>147.9</b> | <b>141.7</b> |
| Direct investment                            | 90.2         | 62.8         | 25.5         | 25.8         | 26.2         | 29.0         | 32.3         | 23.3         | 21.9         | 22.0         | 17.4         |
| Portfolio investment                         | 39.2         | 36.7         | 43.1         | 45.4         | 57.3         | 74.5         | 89.9         | 69.3         | 76.8         | 88.0         | 87.3         |
| Equity and investment fund shares            | 34.4         | 34.2         | 39.6         | 39.9         | 51.4         | 68.3         | 83.2         | 63.5         | 68.5         | 82.9         | 81.5         |
| Debt securities                              | 4.8          | 2.5          | 3.5          | 5.5          | 5.9          | 6.2          | 6.6          | 5.8          | 8.2          | 5.1          | 5.8          |
| Financial derivatives                        | 0.5          | 0.3          | 0.5          | 0.4          | 0.4          | 0.6          | 0.2          | 0.4          | 0.4          | 0.4          | 0.3          |
| Other investment                             | 53.4         | 24.2         | 20.6         | 21.7         | 18.1         | 21.0         | 18.6         | 19.4         | 16.9         | 18.2         | 17.2         |
| Reserve assets                               | 28.0         | 32.0         | 25.6         | 25.5         | 26.8         | 27.4         | 27.7         | 21.2         | 18.1         | 19.3         | 19.5         |
| <b>Liabilities</b>                           | <b>215.8</b> | <b>153.1</b> | <b>112.1</b> | <b>108.5</b> | <b>107.2</b> | <b>117.3</b> | <b>124.1</b> | <b>108.3</b> | <b>99.4</b>  | <b>99.2</b>  | <b>97.6</b>  |
| Direct investment                            | 91.4         | 79.6         | 44.4         | 40.0         | 38.5         | 38.8         | 43.9         | 39.7         | 37.7         | 40.3         | 37.4         |
| Portfolio investment                         | 41.4         | 48.3         | 42.3         | 41.9         | 44.0         | 49.4         | 49.0         | 38.2         | 32.7         | 30.8         | 35.0         |
| Equity and investment fund shares            | 4.0          | 3.6          | 4.8          | 5.6          | 10.5         | 12.5         | 11.9         | 7.4          | 5.5          | 3.9          | 3.9          |
| Debt securities                              | 37.4         | 44.7         | 37.5         | 36.3         | 33.5         | 36.9         | 37.1         | 30.8         | 27.2         | 26.9         | 31.1         |
| Financial derivatives                        | 0.6          | 0.4          | 0.4          | 0.2          | 0.1          | 0.2          | 0.5          | 0.8          | 0.3          | 0.3          | 0.2          |
| Other investment                             | 82.5         | 24.9         | 24.9         | 26.3         | 24.5         | 28.9         | 30.8         | 29.6         | 28.7         | 27.8         | 24.9         |
| <b>Net international investment position</b> | <b>-4.6</b>  | <b>2.9</b>   | <b>3.2</b>   | <b>10.4</b>  | <b>21.7</b>  | <b>35.1</b>  | <b>44.6</b>  | <b>25.4</b>  | <b>34.7</b>  | <b>48.7</b>  | <b>44.2</b>  |

Sources: Central Bank of Iceland; and IMF staff calculations.

Note: The large reductions in external assets and liabilities in 2017 were primarily due to changes in direct investment, driven mainly by adjustments within consolidated entities in the pharmaceuticals sector (Central Bank of Iceland, Financial Stability Report, Vol.22, April 2018).

**Table 7. Iceland: Financial Soundness Indicators 1/, 2016–25**  
(Percent)

|                                                      | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 | 2025 |
|------------------------------------------------------|------|------|------|------|------|------|------|------|------|------|
| Regulatory capital to risk-weighted assets 2/        | 27.7 | 25.1 | 23.2 | 24.2 | 24.9 | 25.4 | 23.7 | 24.3 | 23.5 | 23.9 |
| Regulatory tier 1 capital to risk-weighted assets 2/ | 27.2 | 24.3 | 21.8 | 21.8 | 22.4 | 23.1 | 21.1 | 21.9 | 21.0 | 21.3 |
| Net interest margin 2/                               | 3.0  | 2.9  | 2.9  | 2.7  | 2.5  | 2.4  | 2.8  | 3.0  | 2.8  | 2.9  |
| Return on assets 2/                                  | 2.4  | 1.9  | 1.6  | 1.2  | 0.9  | 2.3  | 2.1  | 2.3  | 2.3  | 2.4  |
| Return on equity 2/                                  | 11.5 | 10.0 | 9.2  | 7.2  | 5.9  | 12.4 | 10.1 | 12.0 | 12.0 | 12.6 |
| Net interest income to total income 2/ 3/            | 51.5 | 53.7 | 64.5 | 66.8 | 69.5 | 60.0 | 70.9 | 69.1 | 66.2 | 63.3 |
| Noninterest expense to total income 2/ 3/            | 60.0 | 64.2 | 65.2 | 65.9 | 56.3 | 49.3 | 49.6 | 44.6 | 46.0 | 46.7 |
| Liquid assets to total assets 2/ 4/                  | 24.0 | 21.9 | 11.0 | 12.2 | 13.2 | 15.3 | 12.9 | 14.4 | 13.9 | 14.2 |
| High-quality liquid assets to total assets           | 17.3 | 13.2 | 10.8 | 12.0 | 12.8 | 14.5 | 12.6 | 14.2 | 13.6 |      |
| Net open foreign exchange position to capital 2/     | 1.2  | 0.5  | 0.3  | 2.1  | 0.3  | -0.7 | 0.5  | 1.8  | 0.7  | 0.7  |
| Total nonperforming loans (NPLs), facility level 5/  | 2.0  | 2.7  | 2.2  | 2.6  | 2.9  | 2.1  | 1.5  | 1.6  | 1.8  | 1.6  |
| Household NPLs, cross default basis 6/               | 4.8  | 3.0  | 2.1  | 2.1  | 2.9  | 1.8  | 1.4  | 1.0  | 1.1  | 1.1  |
| Corporate NPLs, cross default basis 6/               | 5.8  | 6.6  | 6.7  | 4.8  | 18.0 | 14.2 | 7.9  | 2.4  | 2.6  | 2.1  |
| Household and corporate NPLs, cross default basis 6/ | 5.2  | 4.9  | 4.7  | 3.6  | 10.9 | 7.8  | 4.6  | 3.3  | 3.2  |      |
| Loan loss provisions to household loans in default   | 41.7 | 32.3 | 22.4 | 17.5 | 17.7 | 16.3 | 16.2 | 13.9 | 14.2 | 14.2 |
| Loan loss provisions to corporate loans in default   | 50.4 | 44.2 | 31.4 | 31.5 | 34.1 | 27.9 | 24.8 | 25.1 | 21.9 | 25.8 |
| Loan loss provisions to total loans in default       | 47.5 | 40.9 | 28.6 | 27.6 | 29.7 | 25.4 | 22.6 | 21.6 | 19.6 | 21.8 |

Sources: Central Bank of Iceland; IMF FSI database; and IMF staff calculations.

1/ Three largest deposit money banks unless otherwise indicated.

2/ Data for 2017 through 2020, and 2025, are IMF staff estimates.

3/ Total income is total gross income.

4/ Liquid assets comprise cash and balances with the central bank, claims on credit institutions, and bonds and debt instruments.

5/ Over 90 days in default. From 2017Q4 EBA definition for non-performing loans is used, i.e. facility level, over 90 days in default or unlikely to pay.

6/ Over 90 days in default or deemed unlikely to be paid.

## Annex I. External Sector Assessment

**Overall Assessment:** The external position of Iceland in 2025 was moderately weaker than the level implied by fundamentals and desirable policies. The current account balance deteriorated to a deficit of 3.6 percent of GDP in 2025 from 3.2 percent in 2024. The current account was significantly impacted by transitory shocks that adversely affected the trade balance that more than offset a strengthening of the primary income balance and an improvement in the terms of trade. A positive net international investment position and adequate foreign exchange reserve buffers support external sustainability and mitigate potential adverse risks, including from higher energy prices.

**Potential Policy Responses:** The current account is expected to improve significantly in 2026 as the impact of transitory shocks in 2025 fades and gradually strengthen over the medium term supported by moderately tight macroeconomic policies. Sustained efforts to foster innovation are needed to facilitate the diversification of the economy toward higher value-added export-oriented sectors. The flexible exchange rate should act as the main shock absorber, supported by structural measures to enhance price and wage flexibility.

### Foreign Assets and Liabilities: Position and Trajectory

**Background.** The net international investment position (NIIP) declined to 44.2 percent of GDP in 2025, from 48.7 percent in 2024, though it has improved significantly over the past decade. The decline largely reflected a reduction in direct investment assets, which accounted for a 6.2 percentage points reduction in gross assets to 141.7 percent of GDP. Gross liabilities stood at 97.6 percent of GDP, reflecting only modest compositional changes, and are well diversified across FDI (37.4 percent of GDP), portfolio debt liabilities (31.1 percent of GDP), and other investments (24.9 percent of GDP).

**Assessment.** The NIIP is forecasted to remain at its current levels over the medium term, consistent with a recovery in the current account balance. However, fluctuations in valuation effects create uncertainties around the projections and pose a potential downside risk.

|                       |            |                     |                   |                   |                  |
|-----------------------|------------|---------------------|-------------------|-------------------|------------------|
| 2025 (Percent of GDP) | NIIP: 44.2 | Gross Assets: 141.7 | Debt Assets: 23.2 | Gross Liab.: 97.6 | Debt Liab.: 68.5 |
|-----------------------|------------|---------------------|-------------------|-------------------|------------------|

### Current Account

**Background.** The current account deficit widened to 3.6 percent of GDP in 2025, reflecting a series of transitory shocks including a disappointing fishing season, weak aluminum export growth, and a surge in imports of computer equipment. These pressures were partly offset by an improvement in the terms of trade—driven by higher marine and aluminum prices—and a strengthening of the primary income balance due to lower dividends and retained earnings outflows.

**Assessment.** The EBA-lite adjusted CA balance stood at 0.5 percent of GDP in 2025 after accounting for adjustors to capture the transitory effect of higher imports for data centers (3.1 percent of GDP), the disappointing fishing season (0.7 percent of GDP) and disruptions to aluminum production (0.3 percent of GDP). The EBA-lite CA regression estimates a norm of 2.1 percent of GDP, implying a staff-assessed CA gap

of -1.6 percent. There is a moderate positive contribution from policy gaps, primarily due to the difference between the fiscal deficit in 2025 and the fiscal balance required to stabilize debt over the medium-term.

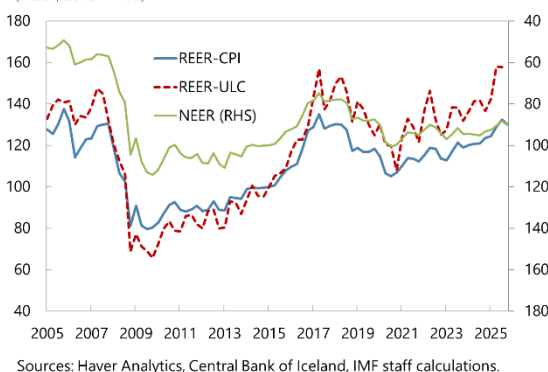
#### Iceland: Model Estimates for 2025 (in percent of GDP)

|                                                                                                                                                                                                                                                                                                                                  | CA model 1/<br>(in percent of GDP) | REER model 1/<br>(in percent of GDP) |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------|--------------------------------------|
| <b>CA-Actual</b>                                                                                                                                                                                                                                                                                                                 | <b>-3.6</b>                        |                                      |
| Cyclical contributions (from model) (-)                                                                                                                                                                                                                                                                                          | 0.0                                |                                      |
| Additional temporary/statistical factors (-) 2/                                                                                                                                                                                                                                                                                  | -4.1                               |                                      |
| Natural disasters and conflicts (-)                                                                                                                                                                                                                                                                                              | 0.0                                |                                      |
| <b>Adjusted CA</b>                                                                                                                                                                                                                                                                                                               | <b>0.5</b>                         |                                      |
| <b>CA Norm</b> (from model) 3/                                                                                                                                                                                                                                                                                                   | <b>2.1</b>                         |                                      |
| Adjustments to the norm (+)                                                                                                                                                                                                                                                                                                      | 0.0                                |                                      |
| <b>Adjusted CA Norm</b>                                                                                                                                                                                                                                                                                                          | <b>2.1</b>                         |                                      |
| <b>CA Gap</b>                                                                                                                                                                                                                                                                                                                    | <b>-1.6</b>                        | <b>-2.9</b>                          |
| o/w Relative policy gap                                                                                                                                                                                                                                                                                                          | 1.8                                |                                      |
| Elasticity                                                                                                                                                                                                                                                                                                                       | -0.3                               |                                      |
| <b>REER Gap</b> (in percent)                                                                                                                                                                                                                                                                                                     | <b>5.3</b>                         | <b>9.8</b>                           |
| 1/ Based on the EBA-lite 3.0 methodology                                                                                                                                                                                                                                                                                         |                                    |                                      |
| 2/ Additional adjustment to account for the temporary impact of shock to the import of capital goods for data centers (3.1 percent of GDP), loss of capelin catch (0.7 percent of GDP) and reduction in aluminum production due to a temporary shot-down of 2/3 production at a very large aluminum smelter (0.3 percent of GDP) |                                    |                                      |
| 3/ Cyclically adjusted, including multilateral consistency adjustments.                                                                                                                                                                                                                                                          |                                    |                                      |

### Real Exchange Rate

**Background.** Both the CPI- and ULC-based real effective exchange rate (REER) appreciated modestly in 2025, driven primarily by high inflation and wage growth in Iceland. The REER has appreciated significantly over the last decade, reflecting the emergence of tourism as a key export sector. While the appreciating REER has thus far not been associated with a deterioration in Iceland's external position, competitiveness pressures could emerge as growth in the tourism sector moderates and future growth increasingly depends on the development of higher value-added export sectors.

**Real and Nominal Effective Exchange Rates**  
(Index, 2015 = 100)



**Assessment.** Both the CA-based model and the REER model suggest minor overvaluation of the ISK.

### Capital and Financial Accounts: Flows and Policy Measures

**Background.** Net capital outflows from the capital and financial account increased to 2.4 percent of GDP in 2025, from near balance in 2024. This was driven primarily by a sizeable capital account inflow stemming from a large one-off transaction—the sale of intellectual property by an Icelandic biotechnology company to a foreign entity. Meanwhile, inward FDI moderated and net borrowing needs were satisfied by debt

portfolio investments. The large discrepancy between the financial account and the current account balance in 2024, leading to net errors and omissions, declined significantly to -0.4 percent of GDP. With the Exchange Rate Act of 2021, the remaining capital flow management measures (CFM) introduced in 2008 were removed, and no new CFMs have been introduced since then.

**Assessment.** Capital inflows to Iceland remain dependent on global market conditions. But vulnerabilities related to external financing are contained, given the positive stock position and adequate foreign exchange reserve buffers.

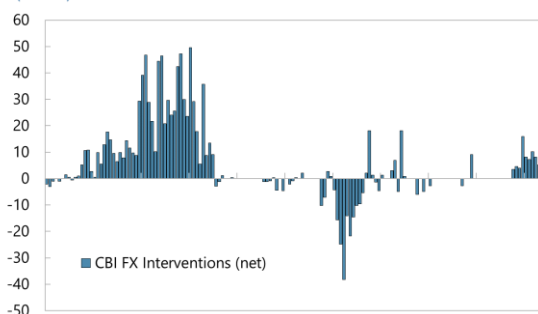
## FX Intervention and Reserves Level

**Background.** Under the free-floating exchange rate regime, the CBI uses interventions mainly to counter disorderly market conditions. However, the CBI commenced regular purchases of foreign exchange in April 2025 and continued doing so until year end to offset a projected decline in reserve coverage. As a result, the CBI's share of the foreign exchange interbank turnover in 2025 was unusually high at 20.5 percent. The level of foreign exchange reserves is equivalent to 19.8 percent of GDP and about 5 months of prospective goods and services imports.

**Assessment.** At 123.2 percent of the Fund's ARA metric, helped by the CBI's purchase program and €750 million Eurobond issuance in 2025, the level of reserves remains broadly adequate for precautionary purposes, but should gradually be increased towards the upper half of the adequacy range of 100-150 percent, given the exposure of Iceland's economy to external shocks.

**Central Bank FXI (net)**

(Bn. ISK)

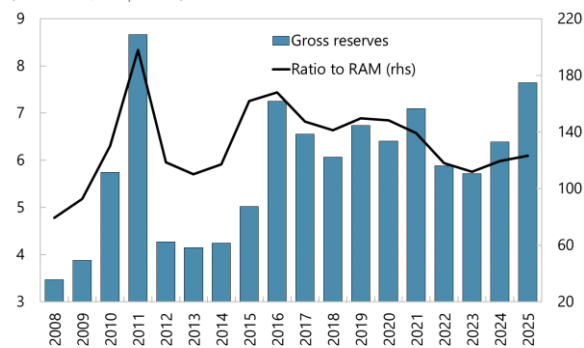


Jan-13 Apr-14 Jul-15 Oct-16 Jan-18 Apr-19 Jul-20 Oct-21 Jan-23 Apr-24 Jul-25

Sources: Haver Analytics, Central Bank of Iceland, IMF staff calculations.

**Gross Reserves**

(Billion USD, and percent)



Sources: CBI and IMF Staff Calculations.

## Annex II. Risk Assessment Matrix<sup>1</sup>

[illegible]

<sup>1</sup> The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly.

| Risks                                                                                                                                                                                                                                                                         | Relative Likelihood | Impact if Realized                                                                                                                                                                       | Policy Response                                                                                                                                                                                                                                                                                  |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| pressures, social unrest, and macro instability.                                                                                                                                                                                                                              |                     |                                                                                                                                                                                          |                                                                                                                                                                                                                                                                                                  |
| <b>Disorderly AI correction</b><br>An abrupt revision in expectations of strong AI-led productivity gains causes a sharp market correction, investment decline, and wealth loss, which suppress demand and tighten financial conditions globally.                             | High                | <b>High</b><br><ul style="list-style-type: none"> <li>A sharp re-pricing of risk could raise the cost of capital, lower confidence, and reduce investment.</li> </ul>                    | <ul style="list-style-type: none"> <li>Strengthen financial surveillance and stress testing.</li> <li>Use macroprudential tools and crisis plans to support the supply of credit.</li> </ul>                                                                                                     |
| <b>Fiscal Vulnerabilities and Higher Interest Rates.</b> Higher public debt and deficit levels put further upward pressure on long-term interest rates, sharply tightening global financial conditions and amplifying currency volatility.                                    | High                | <b>Medium</b><br><ul style="list-style-type: none"> <li>A tightening of global financial conditions could result in higher risk premia and increase exchange rate volatility.</li> </ul> | <ul style="list-style-type: none"> <li>Allow exchange rate to adjust while intervening to prevent disorderly market conditions.</li> <li>Adjust monetary policy to steer inflation and inflation expectations back to target</li> </ul>                                                          |
| <b>Structural Risks</b>                                                                                                                                                                                                                                                       |                     |                                                                                                                                                                                          |                                                                                                                                                                                                                                                                                                  |
| <b>Cyberthreats.</b> Cyberattacks on physical or digital infrastructure, technical failures, or misuse of AI technologies could trigger financial and economic instability.                                                                                                   | High                | <b>High</b><br><ul style="list-style-type: none"> <li>Damage to undersea cables disrupts connectivity.</li> <li>Disruption of cross-border payments and financial flows.</li> </ul>      | <ul style="list-style-type: none"> <li>Stand ready to provide support to critical infrastructure or institutions.</li> <li>Provide liquidity support to banks, if needed.</li> </ul>                                                                                                             |
| <b>Climate Change.</b> Extreme climate events and rising temperatures could cause loss of life, damage to infrastructure, food insecurity, supply disruptions, and heighten economic and financial instability.                                                               | Medium              | <b>Medium</b><br><ul style="list-style-type: none"> <li>Damage to infrastructure and wealth weakens economic activity.</li> </ul>                                                        | <ul style="list-style-type: none"> <li>Stand ready to provide targeted fiscal support to affected sectors.</li> <li>Increase investment in climate-resistant public infrastructure.</li> <li>Allow exchange rate to adjust while intervening to prevent disorderly market conditions.</li> </ul> |
| <b>AI Acceleration.</b> Rapid AI adoption significantly improves productivity, boosts growth, and revives business dynamism. Realizing these gains requires complementary policies to manage energy constraints, scale critical inputs, and support labor market transitions. | Medium              | <b>Medium</b><br><ul style="list-style-type: none"> <li>Faster-than-expected productivity and medium-term growth, though near-term gains may be uneven.</li> </ul>                       | <ul style="list-style-type: none"> <li>Increase investment in digital and energy infrastructure to support the AI transition</li> <li>Invest in training and education to upskill and reskill labor to facilitate adoption of AI</li> </ul>                                                      |

| Risks                                                                                                                                                     | Relative Likelihood | Impact if Realized                                                                                                                                                                                                                                                                       | Policy Response                                                                                                                                                                                                                                                                                                                                       |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Iceland-Specific Risks</b>                                                                                                                             |                     |                                                                                                                                                                                                                                                                                          |                                                                                                                                                                                                                                                                                                                                                       |
| <b>Increased wage pressures</b>                                                                                                                           | <b>High</b>         | <b>High</b><br>Higher real wage growth pushes up firms' costs, raises inflation and inflation expectations, and weakens competitiveness.                                                                                                                                                 | <ul style="list-style-type: none"> <li>• Adjust monetary policy to steer inflation and inflation expectations back to target.</li> <li>• Accelerate structural reforms to increase productivity.</li> </ul>                                                                                                                                           |
| <b>Idiosyncratic risks to exports.</b>                                                                                                                    | <b>Medium</b>       | <b>Medium</b><br>Disruption to exports from idiosyncratic risk in aluminum production, fish quotas, and patenting issues in the pharmaceutical sector could result in lower production and exports.                                                                                      | <ul style="list-style-type: none"> <li>• Diversify into high-value added sectors to broaden the export base, including but not limited to liberalizing services trade and reducing stringent FDI regulation.</li> </ul>                                                                                                                               |
| <b>Faster expansion in energy supply capacity.</b> Could boost investment in aquaculture and data centers.                                                | <b>Medium</b>       | <b>Medium</b> <ul style="list-style-type: none"> <li>• Stronger-than-expected growth in energy supply could boost latent investment in emerging energy-intensive sectors such as aquaculture and data centers, raise potential output and help diversify the economy further.</li> </ul> | <ul style="list-style-type: none"> <li>• Support expansion of energy supply and distribution through streamlined permitting, while safeguarding environmental concerns.</li> </ul>                                                                                                                                                                    |
| <b>Premature loosening of monetary policy.</b> Uncertainty about the state of the economy and the outlook for inflation could result in premature easing. | <b>Medium</b>       | <b>Medium</b><br>Increase in inflation and inflation expectations, damaging central bank credibility.                                                                                                                                                                                    | <ul style="list-style-type: none"> <li>• Adjust monetary policy to steer inflation and inflation expectations back to target.</li> </ul>                                                                                                                                                                                                              |
| <b>EU accession.</b> Uncertainty around the outcome could result in asset price volatility.                                                               | <b>Medium</b>       | <b>Medium</b><br>Increase in exchange rate volatility.<br>Sharp movements in domestic asset prices.                                                                                                                                                                                      | <ul style="list-style-type: none"> <li>• Allow exchange rate to adjust; if accompanied by a risk-off shock, consider the use of FXI to prevent disorderly market conditions and ease the burden on monetary policy.</li> <li>• Use macroprudential measures to strengthen resilience against excessive movements in domestic asset prices.</li> </ul> |

## Annex III. Sovereign Risk and Debt Sustainability Assessment

Annex III. Table 1. Iceland: Risk of Sovereign Stress

### Risk of Sovereign Stress

| Horizon                                   | Mechanical signal                       | Final assessment                        | Comments                                                                                                                                                                                                                                                                                                                                                |
|-------------------------------------------|-----------------------------------------|-----------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Overall</b>                            | ...                                     | <b>Low</b>                              | The overall risk of sovereign stress is low on a continued recovery and improved debt indicators. The government remains committed to its medium-term fiscal consolidation strategy. The re-introduction of fiscal rules in 2026 will help ensuring medium-term debt sustainability.                                                                    |
| <b>Near term 1/</b>                       |                                         |                                         |                                                                                                                                                                                                                                                                                                                                                         |
| <b>Medium term</b>                        | <b>Low</b>                              | <b>Low</b>                              | Medium-term risks are assessed as low. In the baseline interest rate risks are low, but can increase in an adverse high interest rate scenario. The wide fan chart is the result of the 2008 crisis, and thus the size of historical shocks to debt. The reintroduction of the fiscal rules in 2026 will help ensuring medium-term debt sustainability. |
| Fanchart                                  | <b>Moderate</b>                         | <b>Low</b>                              |                                                                                                                                                                                                                                                                                                                                                         |
| GFN                                       | <b>Low</b>                              | <b>Low</b>                              |                                                                                                                                                                                                                                                                                                                                                         |
| Stress test                               |                                         | ...                                     |                                                                                                                                                                                                                                                                                                                                                         |
| <b>Long term</b>                          | ...                                     | <b>Low</b>                              | Long-term risks are modest given the advanced pension system. Age related spending on health and social security will increase in the long-term. The fiscal rules, and the prudent long-term planning perspective of Icelandic policy making, will help ensuring debt sustainability.                                                                   |
| <b>Sustainability assessment 2/</b>       | Not required for surveillance countries | Not required for surveillance countries |                                                                                                                                                                                                                                                                                                                                                         |
| <b>Debt stabilization in the baseline</b> |                                         |                                         | Yes                                                                                                                                                                                                                                                                                                                                                     |

### DSA Summary Assessment

Commentary: Iceland is at a low overall risk of sovereign stress and debt is projected on a downward path in the baseline. Debt indicators have improved, and medium-term liquidity needs are low. In connection with the settlement of the IL Fund (HFF), the government increased maturities on its debt portfolio. The reintroduction of the revised fiscal rules in 2026 will help ensuring medium-term debt sustainability. Long-term spending pressures are mitigated by favorable demographics due to migration inflow. Government onlending and other below-the-line debt issuance should be monitored carefully.

Source: Fund staff.

Note: The risk of sovereign stress is a broader concept than debt sustainability. Unsustainable debt can only be resolved through exceptional measures (such as debt restructuring). In contrast, a sovereign can face stress without its debt necessarily being unsustainable, and there can be various measures—that do not involve a debt restructuring—to remedy such a situation, such as fiscal adjustment and new financing.

1/ The near-term assessment is not applicable in cases where there is a disbursing IMF arrangement. In surveillance-only cases or in cases with precautionary IMF arrangements, the near-term assessment is performed but not published.

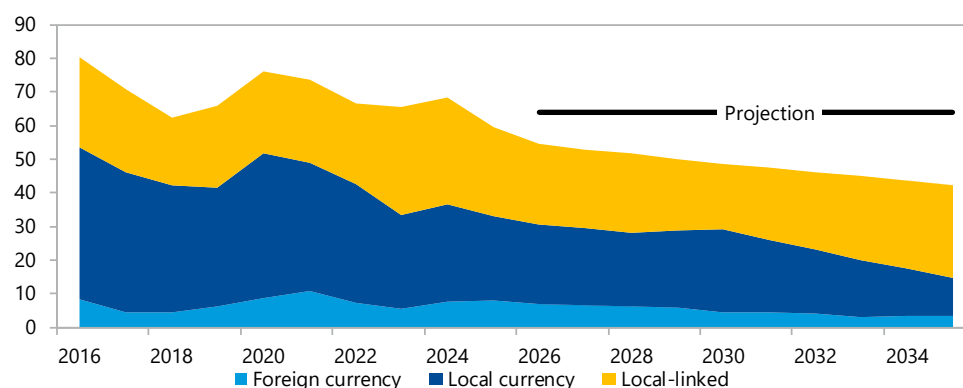
2/ A debt sustainability assessment is optional for surveillance-only cases and mandatory in cases where there is a Fund arrangement.

Annex III. Figure 1. Iceland: Debt Coverage and Disclosures

|                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |      |              |                  |        |                                     |                     |                       |             |             | Comments            |              |                         |                      |           |                                                                                                                                                                                                                                                                 |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------|--------------|------------------|--------|-------------------------------------|---------------------|-----------------------|-------------|-------------|---------------------|--------------|-------------------------|----------------------|-----------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1. Debt coverage in the DSA: 1/                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |      |              |                  |        |                                     |                     |                       |             |             | CG                  | GG           | NFPS                    | CPS                  | Other     |                                                                                                                                                                                                                                                                 |
| 1a. If central government, are non-central government entities insignificant?                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                        |      |              |                  |        |                                     |                     |                       |             |             |                     |              |                         |                      |           | n.a.                                                                                                                                                                                                                                                            |
| 2. Subsectors included in the chosen coverage in (1) above:                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                          |      |              |                  |        |                                     |                     |                       |             |             |                     |              |                         |                      |           |                                                                                                                                                                                                                                                                 |
| Subsectors captured in the baseline                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                  |      |              |                  |        |                                     |                     |                       |             |             | Inclusion           |              |                         |                      |           |                                                                                                                                                                                                                                                                 |
| CPS                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                  | NFPS | GG: expected | CG               | 1      | Budgetary central government        |                     |                       |             |             |                     | Yes          |                         |                      |           |                                                                                                                                                                                                                                                                 |
|                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |      |              |                  | 2      | Extra budgetary funds (EBFs)        |                     |                       |             |             |                     | Yes          |                         |                      |           |                                                                                                                                                                                                                                                                 |
|                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |      |              |                  | 3      | Social security funds (SSFs)        |                     |                       |             |             |                     | Yes          |                         |                      |           |                                                                                                                                                                                                                                                                 |
|                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |      |              |                  | 4      | State governments                   |                     |                       |             |             |                     | Yes          |                         |                      |           |                                                                                                                                                                                                                                                                 |
|                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |      |              |                  | 5      | Local governments                   |                     |                       |             |             |                     | Yes          |                         |                      |           |                                                                                                                                                                                                                                                                 |
|                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |      |              |                  | 6      | Public nonfinancial corporations    |                     |                       |             |             |                     | no           |                         |                      |           |                                                                                                                                                                                                                                                                 |
|                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |      |              |                  | 7      | Central bank                        |                     |                       |             |             |                     | no           |                         |                      |           |                                                                                                                                                                                                                                                                 |
|                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |      |              |                  | 8      | Other public financial corporations |                     |                       |             |             |                     | no           |                         |                      |           |                                                                                                                                                                                                                                                                 |
| 3. Instrument coverage:                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                              |      |              |                  |        |                                     |                     |                       |             |             | Currency & deposits | Loans        | Debt securities         | Oth acct. payable 2/ | IPSGSs 3/ | General government debt includes legacy debt from the former Housing Financing Fund, which are excluded from the definition of debt subject to fiscal rules but considered part of the central administration following a statistical reclassification in 2019. |
| 4. Accounting principles:                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                            |      |              |                  |        |                                     |                     |                       |             |             | Basis of recording  |              | Valuation of debt stock |                      |           |                                                                                                                                                                                                                                                                 |
| Non-cash basis 4/                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    |      | Cash basis   | Nominal value 5/ |        | Face value 6/                       | Market value 7/     |                       |             |             |                     |              |                         |                      |           |                                                                                                                                                                                                                                                                 |
| 5. Debt consolidation across sectors:                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                |      |              |                  |        |                                     |                     |                       |             |             | Consolidated        |              | Non-consolidated        |                      |           |                                                                                                                                                                                                                                                                 |
| Color code: <span style="background-color: #90EE90;"> </span> chosen coverage <span style="background-color: #FF0000;"> </span> Missing from recommended coverage <span style="background-color: #D3D3D3;"> </span> Not applicable                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                   |      |              |                  |        |                                     |                     |                       |             |             |                     |              |                         |                      |           |                                                                                                                                                                                                                                                                 |
| Reporting on Intra-Government Debt Holdings                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                          |      |              |                  |        |                                     |                     |                       |             |             |                     |              |                         |                      |           |                                                                                                                                                                                                                                                                 |
| Issuer                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                               |      |              |                  | Holder | Budget. central govt                | Extra-budget. funds | Social security funds | State govt. | Local govt. | Nonfin. pub. corp.  | Central bank | Oth. pub. fin corp      | Total                |           |                                                                                                                                                                                                                                                                 |
| CPS                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                  | NFPS | GG: expected | CG               | 1      | Budget. central govt                |                     |                       |             |             |                     |              |                         | 0                    |           |                                                                                                                                                                                                                                                                 |
|                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |      |              |                  | 2      | Extra-budget. funds                 |                     |                       |             |             |                     |              |                         | 0                    |           |                                                                                                                                                                                                                                                                 |
|                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |      |              |                  | 3      | Social security funds               |                     |                       |             |             |                     |              |                         | 0                    |           |                                                                                                                                                                                                                                                                 |
|                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |      |              |                  | 4      | State govt.                         |                     |                       |             |             |                     |              |                         | 0                    |           |                                                                                                                                                                                                                                                                 |
|                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |      |              |                  | 5      | Local govt.                         |                     |                       |             |             |                     |              |                         | 0                    |           |                                                                                                                                                                                                                                                                 |
|                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |      |              |                  | 6      | Nonfin pub. corp.                   |                     |                       |             |             |                     |              |                         | 0                    |           |                                                                                                                                                                                                                                                                 |
|                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |      |              |                  | 7      | Central bank                        |                     |                       |             |             |                     |              |                         | 0                    |           |                                                                                                                                                                                                                                                                 |
|                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |      |              |                  | 8      | Oth. pub. fin. corp                 |                     |                       |             |             |                     |              |                         | 0                    |           |                                                                                                                                                                                                                                                                 |
| Total                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                |      |              |                  |        | 0                                   | 0                   | 0                     | 0           | 0           | 0                   | 0            | 0                       | 0                    |           |                                                                                                                                                                                                                                                                 |
| 1/ CG=Central government; GG=General government; NFPS=Nonfinancial public sector; PS=Public sector.<br>2/ Stock of arrears could be used as a proxy in the absence of accrual data on other accounts payable.<br>3/ Insurance, Pension, and Standardized Guarantee Schemes, typically including government employee pension liabilities.<br>4/ Includes accrual recording, commitment basis, due for payment, etc.<br>5/ Nominal value at any moment in time is the amount the debtor owes to the creditor. It reflects the value of the instrument at creation and subsequent economic flows (such as transactions, exchange rate, and other valuation changes other than market price changes, and other volume changes).<br>6/ The face value of a debt instrument is the undiscounted amount of principal to be paid at (or before) maturity.<br>7/ Market value of debt instruments is the value as if they were acquired in market transactions on the balance sheet reporting date (reference date). Only traded debt securities have observed market values. |      |              |                  |        |                                     |                     |                       |             |             |                     |              |                         |                      |           |                                                                                                                                                                                                                                                                 |
| Comment: Debt coverage is general government debt in line with the publication of general government debt from Statistics Iceland. Pension liabilities and the guaranteed HFF bonds are included in the SRDSF.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       |      |              |                  |        |                                     |                     |                       |             |             |                     |              |                         |                      |           |                                                                                                                                                                                                                                                                 |

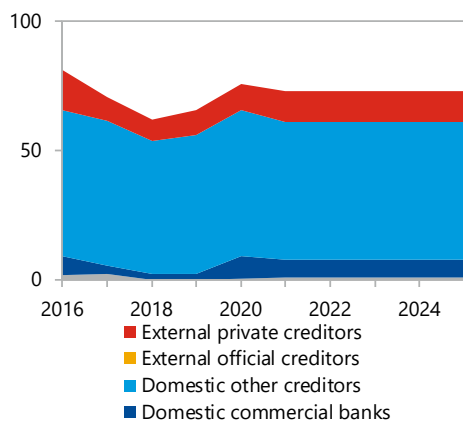
## Annex III. Figure 2. Iceland: Public Debt Structure Indicators

Debt by Currency (Percent of GDP)



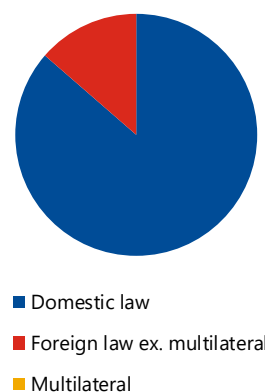
Note: The perimeter shown is general government.

Public Debt by Holder (Percent of GDP)



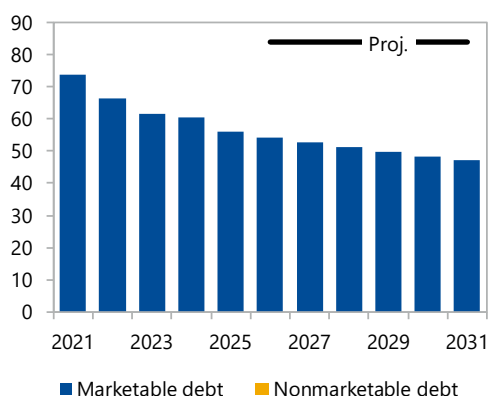
Note: The perimeter shown is general government.

Public Debt by Governing Law, 2025 (percent)



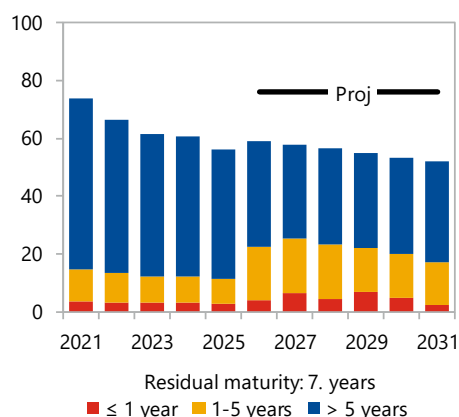
Note: The perimeter shown is general government.

Debt by Instruments (Percent of GDP)



Note: The perimeter shown is general government.

Public Debt by Maturity (Percent of GDP)



Note: The perimeter shown is general government.

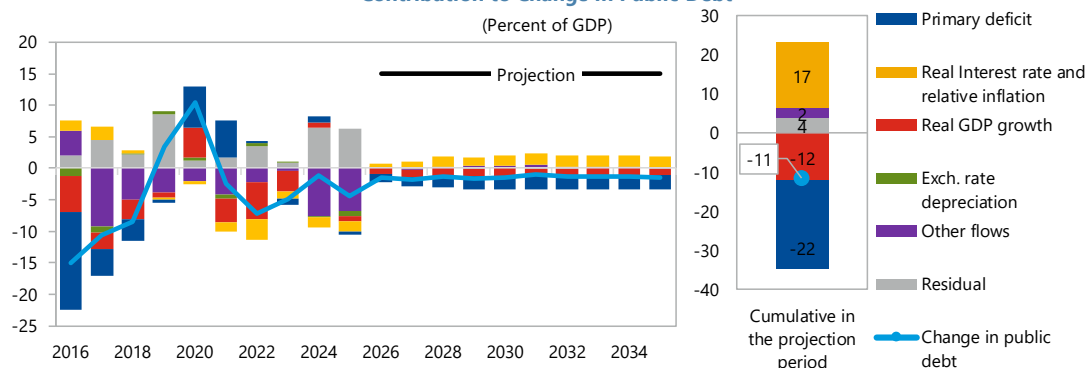
Commentary: Public debt is largely in domestic currency with a significant share linked to CPI. Iceland has a large institutional investor base, including pension funds. The government lengthened the average maturity in 2025.

Annex III. Table 2. Iceland: Baseline Scenario

(Percent of GDP unless indicated otherwise)

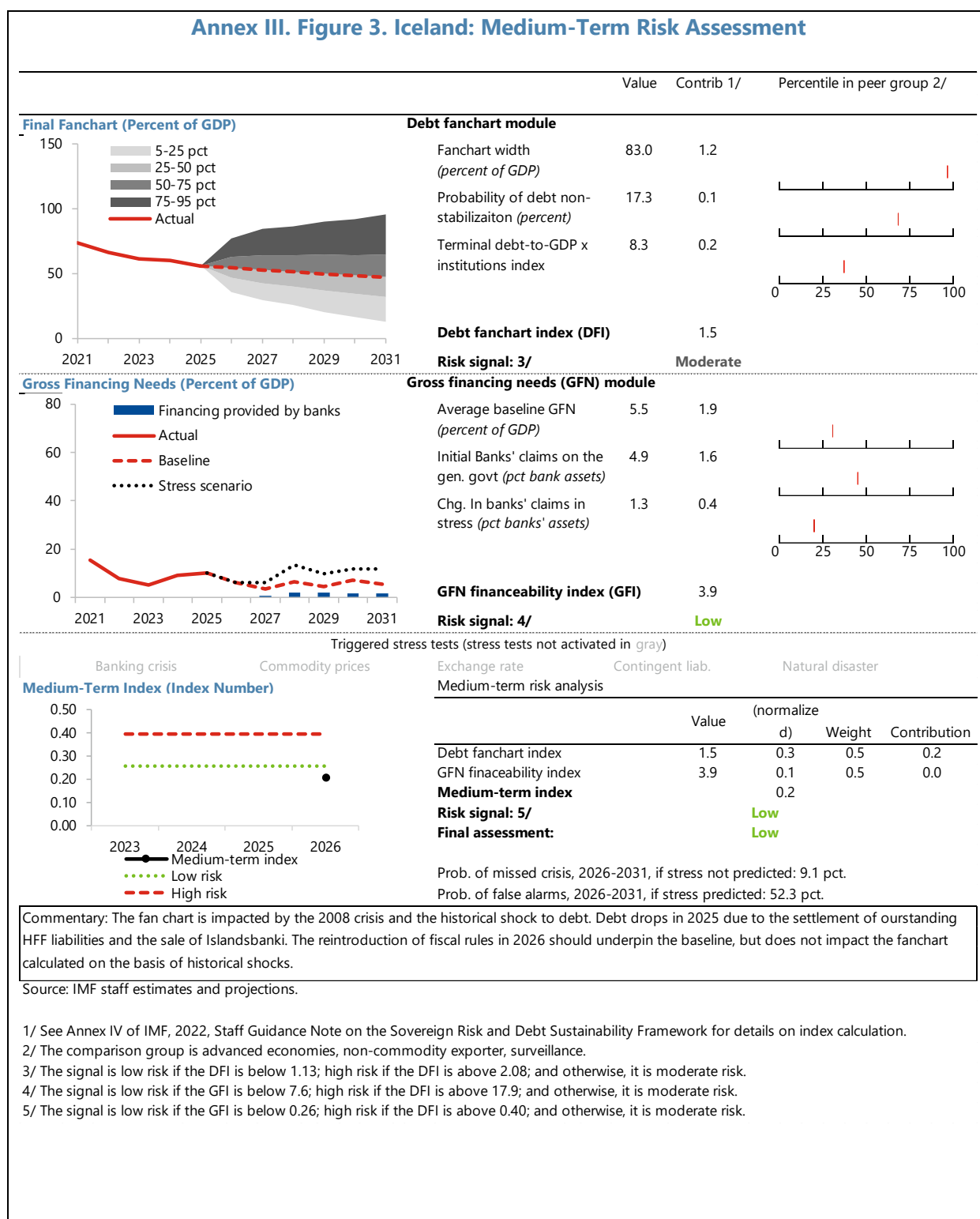
|                                           | Actual | Medium-term projection |      |      |      |      |      | Extended projection |      |      |      |
|-------------------------------------------|--------|------------------------|------|------|------|------|------|---------------------|------|------|------|
|                                           | 2025   | 2026                   | 2027 | 2028 | 2029 | 2030 | 2031 | 2032                | 2033 | 2034 | 2035 |
| Public debt                               | 56.1   | 54.6                   | 52.9 | 51.6 | 50.0 | 48.6 | 47.5 | 46.2                | 44.9 | 43.6 | 42.1 |
| Change in public debt                     | -4.3   | -1.5                   | -1.8 | -1.3 | -1.6 | -1.4 | -1.0 | -1.3                | -1.3 | -1.3 | -1.5 |
| Contribution of identified flows          | -10.6  | -1.5                   | -1.7 | -1.3 | -1.6 | -1.4 | -1.0 | -1.3                | -1.3 | -1.4 | -1.4 |
| Primary deficit                           | -0.5   | -1.2                   | -1.5 | -1.8 | -2.1 | -2.2 | -2.2 | -2.2                | -2.2 | -2.2 | -2.2 |
| Noninterest revenues                      | 41.2   | 41.8                   | 42.1 | 42.5 | 42.6 | 42.6 | 42.6 | 42.6                | 42.6 | 42.6 | 42.6 |
| Noninterest expenditures                  | 40.7   | 40.5                   | 40.6 | 40.6 | 40.5 | 40.4 | 40.4 | 40.4                | 40.4 | 40.4 | 40.4 |
| Automatic debt dynamics                   | -3.2   | -0.3                   | 0.0  | 0.3  | 0.2  | 0.5  | 0.6  | 0.7                 | 0.7  | 0.7  | 0.7  |
| Real interest rate and relative inflation | -1.6   | 0.7                    | 1.1  | 1.5  | 1.4  | 1.7  | 1.8  | 1.9                 | 1.8  | 1.8  | 1.7  |
| Real interest rate                        | -2.0   | 0.4                    | 1.0  | 1.4  | 1.4  | 1.6  | 1.7  | 1.8                 | 1.8  | 1.8  | 1.7  |
| Relative inflation                        | 0.3    | 0.3                    | 0.1  | 0.1  | 0.1  | 0.1  | 0.0  | 0.0                 | 0.0  | 0.0  | 0.0  |
| Real growth rate                          | -0.8   | -1.0                   | -1.1 | -1.2 | -1.2 | -1.2 | -1.1 | -1.1                | -1.1 | -1.1 | -1.0 |
| Real exchange rate                        | -0.8   | ...                    | ...  | ...  | ...  | ...  | ...  | ...                 | ...  | ...  | ...  |
| Other identified flows                    | -6.8   | 0.0                    | -0.2 | 0.3  | 0.3  | 0.4  | 0.6  | 0.2                 | 0.2  | 0.2  | 0.1  |
| Contingent liabilities                    | 0.0    | 0.0                    | 0.0  | 0.0  | 0.0  | 0.0  | 0.0  | 0.0                 | 0.0  | 0.0  | 0.0  |
| (minus) Interest Revenues                 | -1.3   | -1.4                   | -1.5 | -1.2 | -1.2 | -1.2 | -1.0 | -0.8                | -0.7 | -0.6 | -0.5 |
| Other transactions                        | -5.5   | 1.5                    | 1.4  | 1.5  | 1.5  | 1.5  | 1.6  | 1.1                 | 0.9  | 0.8  | 0.7  |
| Contribution of residual                  | 6.2    | 0.0                    | 0.0  | 0.0  | 0.0  | 0.0  | 0.0  | 0.0                 | 0.0  | 0.0  | 0.0  |
| Gross financing needs                     | 10.3   | 6.1                    | 3.4  | 6.6  | 4.4  | 7.0  | 5.4  | 3.0                 | 3.6  | 2.8  | 4.4  |
| of which: debt service                    | 12.1   | 8.8                    | 6.5  | 9.6  | 7.7  | 10.4 | 8.6  | 6.1                 | 6.6  | 5.7  | 7.2  |
| Local currency                            | 5.8    | 2.5                    | 3.3  | 5.5  | 3.5  | 3.8  | 5.6  | 3.7                 | 3.2  | 3.5  | 4.6  |
| Foreign currency                          | 0.0    | 0.8                    | 1.0  | 1.9  | 0.1  | 1.8  | 0.6  | 0.6                 | 1.6  | 0.2  | 0.4  |
| Memo:                                     |        |                        |      |      |      |      |      |                     |      |      |      |
| Real GDP growth (percent)                 | 1.3    | 1.8                    | 2.1  | 2.4  | 2.4  | 2.4  | 2.4  | 2.4                 | 2.4  | 2.4  | 2.4  |
| Inflation (GDP deflator; percent)         | 6.9    | 6.1                    | 3.3  | 2.7  | 2.9  | 2.8  | 2.7  | 2.6                 | 2.5  | 2.4  | 2.3  |
| Nominal GDP growth (percent)              | 8.2    | 8.0                    | 5.5  | 5.2  | 5.4  | 5.3  | 5.2  | 5.1                 | 5.0  | 4.9  | 4.8  |
| Effective interest rate (percent)         | 3.3    | 6.8                    | 5.3  | 5.6  | 5.7  | 6.2  | 6.5  | 6.6                 | 6.6  | 6.5  | 6.4  |

## Contribution to Change in Public Debt

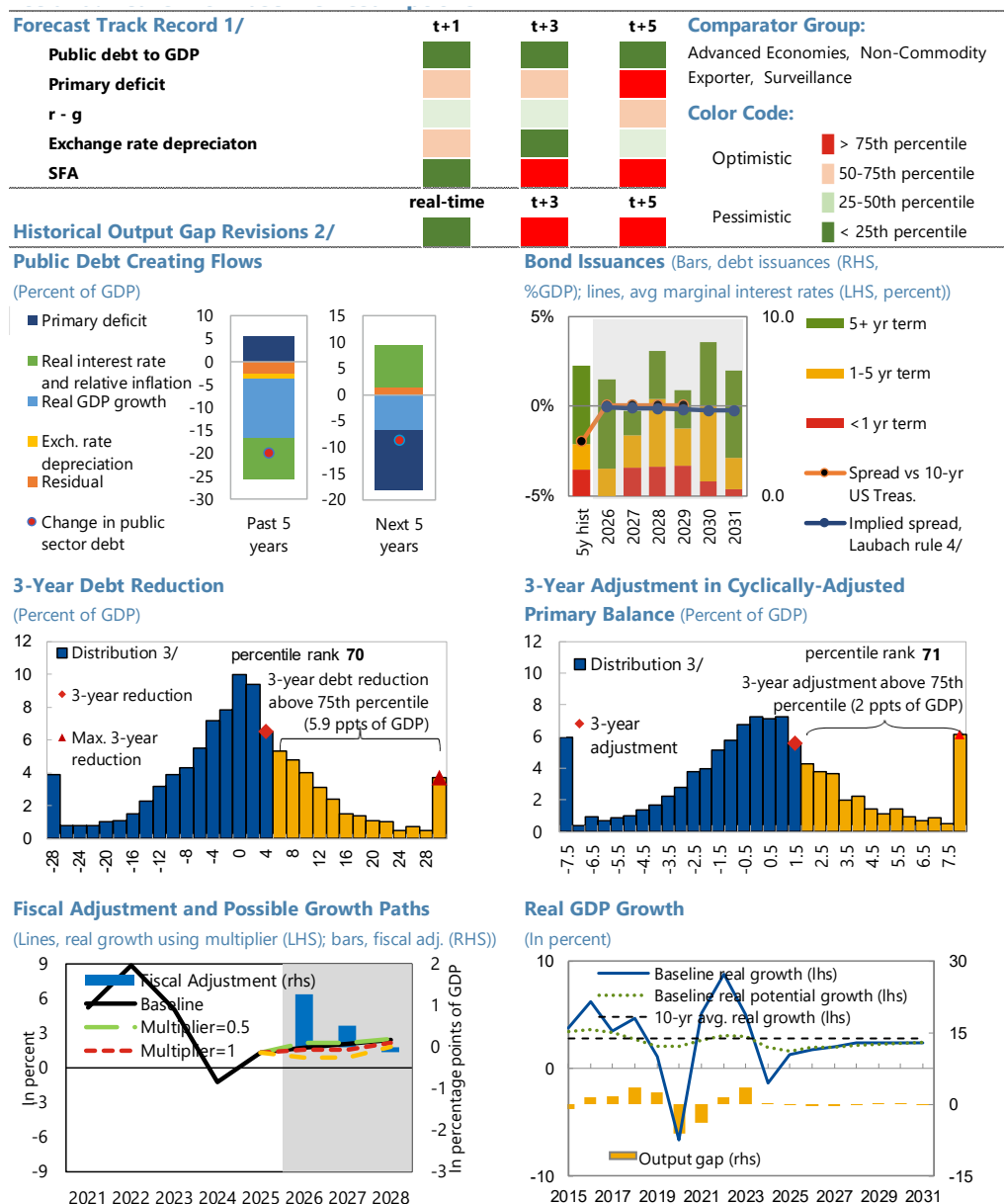


Commentary: Public debt is projected to gradually decline with fiscal consolidation and growth more than offset impact from real interest rates, supported by the reinstated fiscal rule from 2026. A settlement was reached in 2025 between the government and 18 pensions funds on outstanding liabilities in HFF. Public debt at end-2025 was significantly higher than projected in the 2025 Article IV consultation, mainly due to a smaller-than-anticipated impact of the settlement of securities issued by the Housing Finance Fund (HFF) of around 5 percent of GDP on general government debt. In addition the privatization of Islandsbanki reduced public debt below-the-line in 2025 (both recorded under 'other transactions'). There is statistical uncertainty on the 2025 outcome. Below-the-line issuance, especially in the form of government on-lending, but also other activities currently captured in other identified flows, are adding on average 1.5 percent of GDP annually to debt. These on-lending activities should be carefully monitored.

Annex III. Figure 3. Iceland: Medium-Term Risk Assessment



### Annex III. Figure 4. Iceland: Realism of Baseline Assumptions



Commentary: The realism assessment reveal potential optimism bias on the primary deficit and stock-flow adjustments at the t+5 horizon. The reduction in the primary deficit is supported by credible measures in the MTFS 2027-31 and the reintroduction of the amended fiscal rule from 2026. Historical stock-flow adjustments are impacted by HFF liabilities since 2019. A settlement agreement was reached in 2025 on outstanding liabilities and the government taking over the assets in HFF. The average issuance over the last 5 years is impacted by the pandemic period, with deficits close to the 2008 crisis, as well as the settlement of the IL Fund (HFF).

Source : IMF Staff.

1/ Projections made in the October and April WEO vintage.

2/ Calculated as the percentile rank of the country's output gap revisions (defined as the difference between real time/period ahead estimates

3/ Data cover annual observations from 1990 to 2019 for MAC advanced and emerging economies. Percent of sample on vertical axis.

4/ The Laubach (2009) rule is a linear rule assuming bond spreads increase by about 4 bps in response to a 1 ppt increase in the projected debt-to-GDP ratio.

## Annex III. Figure 5. Iceland: Triggered Modules

## Triggered Modules

Large amortizations

Pensions

Climate change: Adaptation

Natural Resources

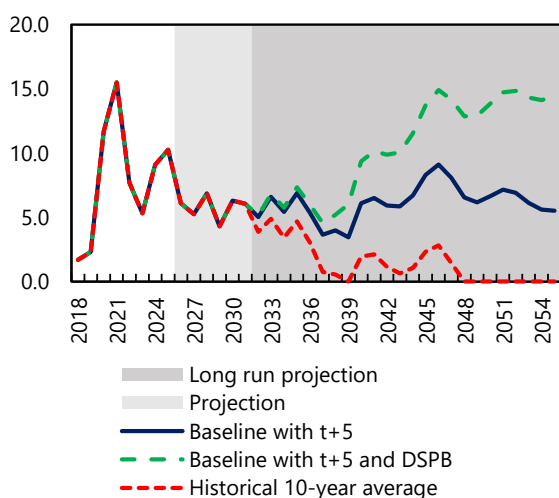
**Health**

Climate change: Mitigation

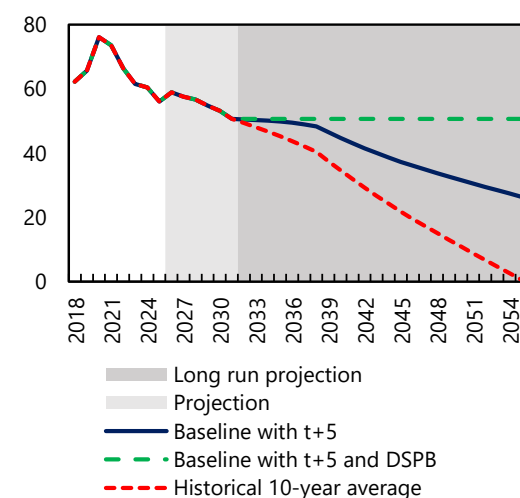
## Long-Term Risk Assessment: Large Amortization

| Projection                                                      | Variable                  | Risk Indication |
|-----------------------------------------------------------------|---------------------------|-----------------|
| Medium-term extrapolation                                       | GFN-to-GDP ratio          | <div></div>     |
|                                                                 | Amortization-to-GDP ratio | <div></div>     |
|                                                                 | Amortization              | <div></div>     |
| Medium-term extrapolation with debt stabilizing primary balance | GFN-to-GDP ratio          | <div></div>     |
|                                                                 | Amortization-to-GDP ratio | <div></div>     |
|                                                                 | Amortization              | <div></div>     |
| Historical average assumptions                                  | GFN-to-GDP ratio          | <div></div>     |
|                                                                 | Amortization-to-GDP ratio | <div></div>     |
|                                                                 | Amortization              | <div></div>     |
| Overall Risk Indication                                         |                           | <div></div>     |

## GFN-to-GDP Ratio



## Total Public Debt-to-GDP Ratio

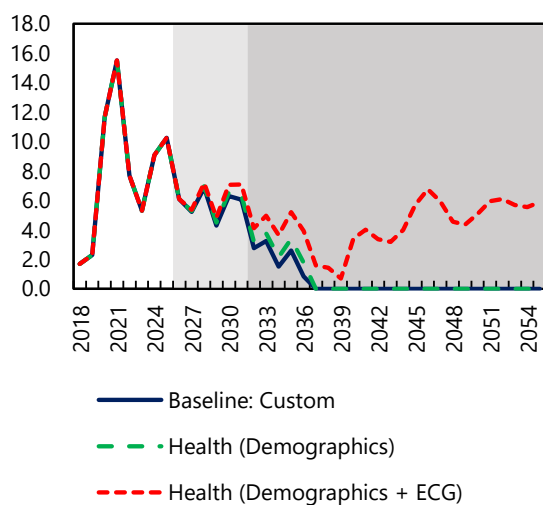


Commentary: The large amortization module indicates overall low funding/roll-over risks in the long-term, on staff's baseline assumptions. The risk indication is somewhat higher, but manageable, using an assumption of the debt-stabilizing primary balance in the projections.

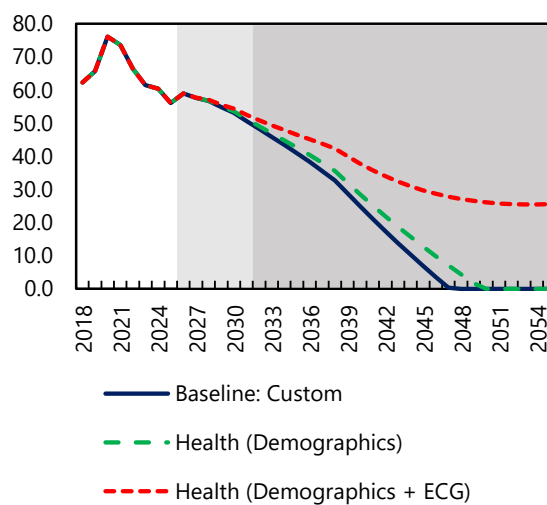
Annex III. Figure 6. Iceland: Demographics-Health

## Demographics: Health

## GFN-to-GDP Ratio



## Total Public Debt-to-GDP Ratio



Commentary: Demographic projections for Iceland suggest a lower trajectory of debt consolidation in some scenarios. Favorable demographics due to migration inflow is a mitigating factor. In particular Extra Cost Growth on health products and services can have an impact on the longer-term debt profile.

## Annex IV. Previous Article IV Recommendations

| Key Recommendations                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                          | Implementation Status                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                              |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Fiscal Policy</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                         |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    |
| <b>Support infrastructure spending</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    |
| <ul style="list-style-type: none"> <li>• Maintain at the minimum the current level of government investment as a share of GDP within the existing MTSF targets.</li> <li>• Encourage private participation in infrastructure projects, including through large Icelandic pension funds, multilateral investment banks, and international infrastructure funds, while containing fiscal risks.</li> <li>• Streamline permitting and licensing procedures to speed up infrastructure deployment.</li> </ul>                                                                                                                                                                                                                    | <ul style="list-style-type: none"> <li>• Government investments are planned to moderate as a share of GDP in the MTFS 2027-31, due to a lower rate of depreciation of existing assets.</li> <li>• The government is in the process of setting up a vehicle for public investments, which is in principle open to participation from private investors and pension funds.</li> <li>• The <i>Industrial Policy – Action Plan 2026–2027</i> includes several concrete measures to accelerate permitting and licensing, including simplifying and coordinating environmental and energy licensing, measures to prevent compensation and expropriation disputes from delaying electricity transmission and distribution projects; and creating a digital licensing platform for online applications and case tracking.</li> </ul>       |
| <b>Strengthen the Fiscal Framework</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    |
| <ul style="list-style-type: none"> <li>• Provide the Fiscal Council with additional capacity and resources to fulfil its expanded role in monitoring productivity developments and proposing reforms. Task the Fiscal Council with evaluating the macroeconomic and fiscal projections underpinning the MTFS.</li> <li>• Expand the coverage of the fiscal rules to better capture the entirety of the fiscal risks confronting the sovereign and to reduce the incentive to shift spending and borrowing to parts of the public sector not covered by the fiscal rules.</li> <li>• Publish fiscal data corresponding to the coverage of the fiscal rules on a quarterly basis rather than annually as currently.</li> </ul> | <ul style="list-style-type: none"> <li>• The fiscal council is in the process of recruiting additional staff within the existing resource envelope under a new chairmanship. The MOFEA started using the macroeconomic projections from the CBI as a basis for their fiscal projections, which will add greater policy consistency and strengthen efficiency.</li> <li>• No changes have been made since 2025, but the MOFEA is mindful of the risks of shifting spending – or below-the-line- operations – outside of the A1 sector.</li> <li>• No changes have been made since 2025. Government statistics is published by Statistics Iceland on a quarterly basis, but for central government as a whole. The fiscal council can request additional data from the MOFEA to assess the fiscal projections, as needed.</li> </ul> |
| <b>Monetary Policy</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    |
| <ul style="list-style-type: none"> <li>• Lower the policy rate as inflation declines toward the target. CBI should be vigilant to</li> </ul>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                 | <ul style="list-style-type: none"> <li>• Inflation surprised to the upside in 2026 Q1 and inflation expectations remain elevated. Higher global energy prices resulting from the war in the Middle East have</li> </ul>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                            |

| Key Recommendations                                                                                                                                                                                                                                                                                                                                                                                     | Implementation Status                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                  |
|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| risks on both sides, especially wage developments and imported inflation.                                                                                                                                                                                                                                                                                                                               | exerted upward pressure on inflation. CBI has responded by raising the policy rate by 25 basis points and signaled that further tightening is possible.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                |
| <b>Macprudential Policy</b>                                                                                                                                                                                                                                                                                                                                                                             |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                        |
| <ul style="list-style-type: none"> <li>Any easing of the CCyB should take care to safeguard the availability of capital that can be released if downside risks materialize. Borrower-based measures should remain on hold for now.</li> <li>Plans to reduce the prevalence of CPI-indexed mortgage loans should be carefully timed.</li> </ul>                                                          | <ul style="list-style-type: none"> <li>The CCyB remains at 2.5 percent. The CBI eased borrower-based measures for first-time borrowers as a response to the supreme court decision on variable rate mortgages in 2025 and given lower risks in the housing market.</li> <li>Detailed plans to reduce the prevalence of CPI indexed mortgages are yet to be made, while the government has stated some objectives, e.g., mandatory amortization requirements, as part of the housing package.</li> </ul>                                                                                                                                                                                                                                                                                                                                                                |
| <b>Foreign Exchange Reserves and FX Derivatives Market</b>                                                                                                                                                                                                                                                                                                                                              |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                        |
| <ul style="list-style-type: none"> <li>Build foreign exchange reserves to a level that is well above the lower end of the 100-150 percent Fund's Reserve Adequacy (ARA) range.</li> </ul>                                                                                                                                                                                                               | <ul style="list-style-type: none"> <li>The CBI started purchasing foreign currency on April 15, 2025. The stock of international reserves has increased by around 10 percent since then at 123% of the ARA metric. The CBI restarted a temporary regular FX purchase program in early 2026.</li> </ul>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                 |
| <ul style="list-style-type: none"> <li>Gradually deepen the foreign currency derivatives market to encourage greater participation of foreign investors in the domestic bond market and facilitate hedging of foreign currency risk.</li> </ul>                                                                                                                                                         | <ul style="list-style-type: none"> <li>The CBI assessed this in 2025 and determined that there was currently no need to change current regulation governing the derivatives market.</li> </ul>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                         |
| <b>Structural Policies</b>                                                                                                                                                                                                                                                                                                                                                                              |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                        |
| <b>Productivity</b>                                                                                                                                                                                                                                                                                                                                                                                     |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                        |
| <ul style="list-style-type: none"> <li>Improving infrastructure to facilitate access to domestic and international markets.</li> <li>Strengthen incentives for pursuing higher education and streamline professional licensing requirements for foreign nationals to address skills mismatches as well as to facilitate the movement of workers to more high-productivity firms and sectors.</li> </ul> | <p>The <i>Industrial Policy – Action Plan 2026–2027</i> puts energy and infrastructure transformation at the center of the growth strategy and includes measures to streamline licensing, facilitate large-scale investment, and strengthen infrastructure. The proposed investment vehicle (infrastructure company) will manage and facilitate large-scale projects.</p> <ul style="list-style-type: none"> <li>The <i>Industrial Policy – Action Plan 2026–2027</i> contains measure to strengthen STEM content in school curricula, expand STEM at university level, improve STEM teaching materials and facilities, and increase enrolment in vocational and technical education. The plan also contains measures to simplify and speed up work and residence permit applications for foreign experts, consolidating them under a single administrative</li> </ul> |

| Key Recommendations                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       | Implementation Status                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                   |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
|                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                           | channel and strengthening digital procedures and capacity to verify qualifications.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     |
| <b>Innovation and diversification</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                         |
| <ul style="list-style-type: none"> <li>Clarify R&amp;D eligibility criteria in the planned revision of R&amp;D legislation to improve predictability and stimulate private R&amp;D investment.</li> <li>Reassess the 2020 increase in R&amp;D expenditure ceilings.</li> <li>Consider allowing R&amp;D expenses to be offset against payroll taxes rather than corporate income taxes.</li> </ul>                                                                                                                                                         | <ul style="list-style-type: none"> <li>The authorities are reviewing the framework for public R&amp;D support. The <i>Industrial Policy – Action Plan 2026–2027</i> calls for a review of legislation governing support for innovation companies and public financing to increase efficiency, simplify processes, and improve performance evaluation.</li> <li>Revised legislation is under development and expected to be sent to parliament in 2026.</li> <li>Revised legislation is under development and expected to be sent to parliament in 2026.</li> </ul>                                                      |
| <b>Housing</b>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                            |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                         |
| <ul style="list-style-type: none"> <li>Develop a comprehensive housing strategy to improve affordability amid population growth, including tighter regulation of short-term rentals.</li> <li>Expand housing supply through land release, streamlined regulations, and incentives such as higher taxes on vacant urban lots.</li> <li>Use housing taxation and targeted support carefully, including higher capital gains taxes on secondary homes and investment properties, to curb speculative demand while limiting macro-financial risks.</li> </ul> | <p>The government has put in place a housing package, which aims to:</p> <ul style="list-style-type: none"> <li>expand housing supply by accelerating the development of a new residential complex in the City of Reykjavik, by simplifying building regulations, and by allowing municipalities to surcharge vacant urban lots.</li> <li>curb speculative demand by reducing capital-gains exemptions and rental-income credits for multiple-property owners, while expanding targeted equity-loan support for first-time buyers.</li> <li>to reduce the weight of index-linked loans in an orderly manner.</li> </ul> |

## Annex V. Update on the Implementation of FSAP Recommendations

| Recommendations                                                                                                                                                                                          | Horizon <sup>1</sup> | Status                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                               |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Cross-Cutting</b>                                                                                                                                                                                     |                      |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |
| Increase resources at the CBI for oversight of market risk, interest rate risk in the banking book (IRRBB), financial climate risks, and operational risks (ICT risk and cybersecurity); and for the RA. | NT                   | The CBI has enhanced its operations and resources. It merged the Banking Supervision and Insurance & Pension Divisions into a single Microprudential Supervision Division to optimize resources and strengthen supervision. Two positions are now dedicated to analyzing market risk and IRRBB. Operational risk monitoring resources, including ICT and cybersecurity, have more than doubled to 6 FTEs. Additionally, the CBI has increased resources for implementing the TIBER-IS framework for cybersecurity testing among critical financial system participants. A new cross-divisional team has been established to address financial climate risks and environmental issues, adding 2 FTEs. |
| <b>Regulation and Supervision: Banking and Pension Funds</b>                                                                                                                                             |                      |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |
| Develop and implement a streamlined and independent budgetary process for supervision.                                                                                                                   | NT                   | Supervisory fees are classified as a tax. Therefore, the MoFEA believes that allowing CBI to directly collect supervisory fees would be unconstitutional. The CBI has established a working group to examine potential options to the budgetary process to discuss with the MoFEA.                                                                                                                                                                                                                                                                                                                                                                                                                   |
| Update legislation to: a) ensure protection of supervisors; b) broaden the definition of related-party transactions; and c) broaden CBI's supervisory oversight over bank's external auditors.           | NT                   | The CBI previously proposed amendments to the Central Bank Act to enhance supervisors' legal protection post-merger with the FSA, but the PMO has not advanced this. The CBI submitted updated proposals to the PMO on potential amendments in late 2025. Further consultations among the PMO, MoFEA, and CBI are planned to determine next steps, potentially requiring a broader approach beyond financial supervisors.                                                                                                                                                                                                                                                                            |
| Remove MoFEA staff from CBI's FMEN (independence) and implement internal delegation of powers framework (accountability).                                                                                | NT                   | In January 2024, an external member replaced the MoFEA staff member on the CBI's FMEN. The June 2023 amendments to the Central Bank Act strengthened the delegation of powers within the CBI and clarified the FMEN's decision-making authority, including administrative fines, police referrals for violations, revocation of operating licenses for serious or repeated offenses, and dismissal of board members for misconduct. The CBI now handles all other decisions.                                                                                                                                                                                                                         |

| Recommendations                                                                                                                                                                                                                                      | Horizon <sup>1</sup> | Status                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                          |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
|                                                                                                                                                                                                                                                      |                      | The CBI has finalized an internal delegation framework that includes signature rules for the entire Bank and delegation from the Governor to the Deputy Governor for Financial Supervision, along with formal procedures for signature authorizations in the supervision divisions. Additional procedures for delegating power to other departments, such as foreign exchange interventions, have been put in place.                                                                                                                                                                            |
| Implement a comprehensive on-site inspection program for banks' risk management practices across all material risk domains incorporating an improved risk-based supervisory plan and ensure integration of climate-risks into supervisory processes. | NT                   | Each year, several aspects of risk management practices are evaluated as part of the SREP, including banks' risk management resources, risk appetite, and the roles of boards and employees. Climate risks are also included in the SREP process, which often involves on-site visits. The Microprudential Supervision Division has updated the on-site inspection program to conduct exams for category 1 and 2 entities on a 1–5 year cycle based on risk level. For category 3 and 4 entities, on-site inspections are performed as needed, following a risk-based approach.                 |
| Issue application regulations or supervisory guidance to banks for appropriate and proportionate implementation of EU rules (ensure compliance with Basel standards) and EBA guidelines.                                                             | MT                   | The CBI has contacted banking supervisory authorities in other Nordic countries to learn how to close the gap between EU rules and Basel standards. Following this consultation, no further action is foreseen.                                                                                                                                                                                                                                                                                                                                                                                 |
| Align rules on governance, internal controls, risk management with IORP II or Solvency II, and enact more stringent rules for outsourcing.                                                                                                           | NT                   | The CBI has revised outsourcing guidelines to establish stricter rules. A MoFEA-led working group is drafting a "green paper" to diagnose the current challenges facing the pension system. The green paper is expected to be published in 2026, followed by a white paper compiling of legislative amendments.                                                                                                                                                                                                                                                                                 |
| Perform regular on-site inspections for large pension funds and re-establish institutionalized supervisory dialogue.                                                                                                                                 | I                    | On-site inspections for larger pension funds (categories 1 and 2) will occur at least every five years. Inspections for smaller pension funds (categories 3 and 4) will be based on risk assessment results.<br><br>The CBI has established annual meetings with the four largest pension funds. These meetings include Deputy Governors for Financial Stability and Financial Supervision, along with directors and senior staff from the pension funds. Additionally, biannual meetings with the Icelandic Pension Fund Association will focus on supervisory priorities and relevant topics. |

| Recommendations                                                                                                                                                                                                                       | Horizon <sup>1</sup> | Status                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                 |
|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Define infringements and sanctions in the Pension Fund Act.                                                                                                                                                                           | NT                   | A MoFEA-led working group is drafting a “green paper” to diagnose the current challenges in the pension system to be published in 2026, followed by a white paper compiling legislative amendments.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    |
| <b>Systemic Risk Analysis</b>                                                                                                                                                                                                         |                      |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                        |
| Develop approaches to monitor funding risks from nonbank financial institutions (including pension funds) and foreign investors.                                                                                                      | NT                   | The CBI is enhancing its monitoring of funding risks from nonbank financial institutions by improving data collection on ownership of all ISK bonds from commercial banks and incorporating deposits from nonbank institutions and foreign investors into liquidity stress tests.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |
| Differentiate inflation indexed and non-indexed lending and funding instruments in the analysis of inflation impact on banks’ credit, interest rate, and market risks.                                                                | MT                   | The current models for default risk have been updated to better reflect the risks of indexed versus non-indexed loans at an aggregate level. Various analyses of indexation prevalence within sectors and associated risks have been conducted to complement these models. The next revision of default risk models will be based on the borrower level, allowing for improved differentiation between these loan types. Data collection for these revised models is underway, and they will be implemented once data requirements have been met and model validation can take place, which is expected in 2027. Borrower level models of loss given default, which comprehensively account for the effects of inflation indexation, have been rolled out for households and will be rolled out for corporate sectors. |
| Continue conducting liquidity stress tests with various runoff and haircut rates, enhance monitoring of LCR by currencies, and address outlier banks through Pillar 2 and supervisory actions.                                        | NT                   | The CBI has incorporated various scenarios for individual currencies, with different runoff and haircut rates, into liquidity stress tests. Results are included in monthly reports to the Financial Stability Committee. LCRs for all significant currencies are monitored at least monthly. Outlier banks are addressed through pillar 2 (SREP/ILAAP) and other supervisory measures. The CBI also has regulatory limits for euros and calculates the euro HQLA/FX net outflows, maintaining a minimum ratio of 100 percent.                                                                                                                                                                                                                                                                                         |
| Closely monitor the impact of higher inflation and interest rates on banks’ solvency condition and pension funds’ investment behavior, counterparty default risk, and (particularly for smaller pension funds) Pillar III cash flows. | NT                   | The CBI closely monitors changes in pension funds’ investments, influenced by both external and internal factors, including asset composition, risk profile, and arrears. Current monitoring focuses on the effects of interest rate and inflation developments on investment behavior and Pillar III cash flows.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |
| Perform data quality checks for pension funds’ supervisory reporting data, require pension funds to submit corrections and expand automated validation rules.                                                                         | NT                   | The CBI has enhanced automated validation rules for pension funds’ annual reports and asset lists. These rules now include SQL data quality checks, and a dashboard for warnings and reporting errors has been developed. Data quality checks are integrated into the ExMon monitoring tool, with alerts that can lead to automated                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    |

| Recommendations                                                                                                                                                                                                                  | Horizon <sup>1</sup> | Status                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                             |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
|                                                                                                                                                                                                                                  |                      | report rejections. Pension funds must submit corrections if their reports contain significant errors.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                              |
| <b>Cybersecurity Supervision and Oversight</b>                                                                                                                                                                                   |                      |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    |
| Investigate alternative domestic retail payment solutions in the event of a significant disruption to the credit and debit card system and refine playbooks to test how cash will be distributed and used in a crisis situation. | I/NT                 | Efforts are ongoing to introduce an account-to-account (A2A) domestic retail solution to enhance the resilience and efficiency of the domestic payment system. The CBI, in collaboration with the PMO and MoFEA, has drafted a bill that grants the CBI authority to issue rules for improving domestic payments, which Parliament adopted on June 22, 2024. In November 2024, the CBI invited proposals for a centralized domestic infrastructure for payment requests, with eight parties participating. Building on this the CBI is currently preparing a public procurement process for a domestic retail payment solution based on request to pay infrastructure. A working group within the Payments Council to assess commercial responses to significant disruptions in the debit and credit card systems. Furthermore, the CBI has re-established platform focused on operational security in the financial market infrastructures. The platform's mandate is to assess risks in financial market infrastructure, recommend mitigating actions and organize exercises to strengthen preparedness for potential crisis situations in the financial market. |
| Produce a financial sector specific cybersecurity strategy, clearly setting out the roles and responsibilities of each party.                                                                                                    | I                    | The Central Bank of Iceland prepared cybersecurity strategy, which was discussed with all relevant stakeholders in the financial sector. The strategy outlines the roles and responsibilities of the relevant parties and was subsequently refined in line with stakeholders' feedback and published in March.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     |
| <b>Macroprudential Policies</b>                                                                                                                                                                                                  |                      |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    |
| Further enhance transparency and accountability by developing a heatmap and regularly publishing reports on risk analysis.                                                                                                       | I                    | The Financial Stability Committee updates a non-published qualitative heat map quarterly to visually present risks. The CBI has traditionally used this heat map to illustrate key risk factors for financial stability. The Financial Stability Report is currently under review, incorporating best practices from financial stability reports of other Nordic countries.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                        |
| Further strengthen the analytical capacity by strengthening the analysis of tail risks, spillovers, systemic risks and calibration of macroprudential tools.                                                                     | NT                   | The CBI conducts regular monitoring through monthly and quarterly internal analyses and publishes a detailed assessment in the Financial Stability Report twice a year. The Financial Stability Committee meets quarterly, receiving comprehensive presentations and memos from the CBI that assess the financial cycle and systemic risk using various indicators. The Committee focuses on growth-at-risk and the distribution of LTV and DSTI ratios to monitor tail risks and makes decisions quarterly regarding the application of macroprudential tools.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    |

| Recommendations                                                                                                                                  | Horizon <sup>1</sup> | Status                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |
|--------------------------------------------------------------------------------------------------------------------------------------------------|----------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Continue closely monitoring cyclical risks in the real estate market and corporates, and take further macroprudential measures if risks persist. | I                    | The Financial Stability Committee monitors the RRE and CRE markets quarterly and is prepared to take macroprudential actions if risks continue. In addition to CBI semi-annual Financial Stability report, a special issue was published on Borrower-Based Measures (BBMs) on 3 December 2025. The special publication covers the legal framework for BBMs in Iceland, our experience of using these macro prudential tools, comparison with other European states and an overview of international research. The CBI also tracks developments in European CRE macroprudential measures, particularly from the ESRB, and is ready to implement them if necessary. With access to essential data on residential real estate transactions and leases from the Housing and Construction Authority, the CBI is developing a model to assess cyclical risks by creating quality-adjusted indexes of residential real estate and rental prices. The first paper was published in 2025 on this issue, <a href="#">see Working Paper no. 99: A Hedonic Housing Model for Macroprudential Policy</a> . Further research into this area is planned over coming years. |
| Close data gaps related to non-financial private sectors (households, non-financial corporates).                                                 | I                    | The CBI has gained access to tax reports from non-financial corporates to address data gaps. Non-financial corporate tax reports will also enhance data quality regarding domestic entities' foreign debt. Additionally, the CBI has intensified data collection on the CRE market by regularly purchasing data on available square meters for sale and rent, as well as tracking CRE rental price trends. The CBI also gathers detailed information on CRE under construction from the Housing and Construction Authority and monitors the quarterly and annual results of publicly listed CRE companies. Finally, a new index for CRE prices has been developed at the Central Bank. See Box 3 in our report on <a href="#">Financial Stability 2026/1</a> . The Central Bank is in contact with Statistics Iceland with the aim of gaining access to a database on household tax returns. Recently, the Central Bank has started gathering data from collection agencies to gain further insight into households and NFCs arrears on general claims.                                                                                                     |
| <b>Liquidity and Crisis Management</b>                                                                                                           |                      |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                             |
| Approve the crisis management handbook and test it in a simulation exercise, widening its scope to the resolution stage.                         | I                    | The crisis management handbook, titled Contingency Plan for Liquidity or Equity Shortfall at Credit Institutions, has been approved and operationalized. The RA conducts regular tests according to a predefined schedule and in the context of EBA guidelines.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                             |

| Recommendations                                                                                                                                                         | Horizon <sup>1</sup> | Status                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Establish a coordination body on resolution issues between the MoFEA and the CBI (RA).                                                                                  | I                    | Discussions are ongoing to formalize information sharing between the CBI and MoFEA on resolution issues, considering either a written MoU for a formal coordination body or a sub-group under the Financial Stability Council.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                              |
| Adopt a seven-day deadline for the Icelandic Depositors' and Investors' Guarantee Fund (TVF)'s disbursements and grant TVF access to adequate external funding sources. | NT                   | Efforts are underway to explore potential legislative amendments needed for implementing this recommendation. The MoFEA oversees the project, with preparatory work supported by the CBI. Work on amendments to law on deposit guarantee scheme continues within MoFEA. Details to be provided later in 2026, with legislative bill possibly introduced to parliament.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |
| Develop a repo market and operationalize the ELA, including the assessment of collateral eligibility.                                                                   | NT                   | The CBI has made efforts to develop an efficient money market, but challenges persist due to its small size and lack of liquidity. Banks have been hesitant to commit to two-way pricing for suggested tenors (one week to three months). While the CBI has revisited this issue multiple times, establishing a repo market requires significant commitment from banks, particularly the three D-SIBs. Additionally, the comfortable liquidity positions of individual banks diminish their need for an active cash market.                                                                                                                                                                                                                                                                                                                                                                 |
|                                                                                                                                                                         |                      | <p>The CBI maintains an ELA working group to ensure the operational effectiveness of ELA. The group analyzes practical and legal perspectives, including assessing collateral eligibility. The group assess loan debt portfolio data for these assessments</p> <p>The CBI assess the overall ELA collateral eligibility of Icelandic financial counterparties. Financial institutions must report their main assets, including loan portfolios, to the CBI's Loan Registry. Efforts are underway to utilize this Register for evaluating potential ELA collateral, thereby enhancing transparency and risk assessment.</p> <p>Furthermore, in line with Norwegian and Swedish law, the CBI is considering legislative measures to gain exclusive authority for the registration, mobilization, and monitoring of loan portfolios pledged as collateral by local financial institutions.</p> |
| Operationalize the application of all the resolution tools (not just bail-in).                                                                                          | NT                   | Resolution plans for Iceland's three D-SIBs are increasingly focused on developing transfer strategies (non bail-in), aligning with EEA developments. The current priority is to finalize bail-in playbooks, with Master playbooks (including transfer strategies) expected to be completed by 2026, in accordance with EBA Guidelines 2022/01 and the amended testing guidelines. The RA is focusing on operationalizing transfer strategies following progress in implementing the bail-in strategy.                                                                                                                                                                                                                                                                                                                                                                                      |

| Recommendations                                                                                                                                                                           | Horizon <sup>1</sup> | Status                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
|                                                                                                                                                                                           |                      | The first resolution plan utilizing a transfer tool as the preferred strategy has been approved. This drafting process allowed for a detailed examination of transfer strategies, including establishing a transfer perimeter and preparing for operational transfers. The RA has referenced both EBA GL 2022/01 and EBA GL 2022/11 (Transferability guidelines). Further tests with the banks are scheduled for 2026 and 2027 in accordance with a multiannual testing plan.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                             |
| <b>AML/CFT</b>                                                                                                                                                                            |                      |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                           |
| Improve collection and analysis of data; refine the risk assessment methodology; enhance AML/CFT supervision of banks; and continue to detect unlicensed virtual asset service providers. | NT                   | <p><i>Improve collection and analysis of data; refine the risk assessment methodology:</i> CBI is continuously reviewing and developing its methodology regarding risk assessments of individual obliged entities as well as sectoral risk assessment. In connection with technical assistance from the IMF, CBI has presented its methodology to the IMF, which provided CBI with valuable advice. It should be noted that this work was only explored at a preliminary level at this stage. Over the past year, CBI has also maintained productive cooperation with the Nordic and Baltic countries regarding their methodologies. Such collaboration provides CBI with valuable insight into how other FSA's are developing their approaches. With recent legal development in the EU it is clear that methodologies for risk assessments of individual reporting entities will be harmonized through e.g. the issuance of a regulatory technical standard (RTS). It can be expected that this RTS will be implemented domestically in the near future and will have a significant impact on data collection, calculations, and outcomes. CBI is currently working on a future vision for the overall framework of risk assessments. Although it is clear that major changes are forthcoming, the methodology as a whole has been reviewed annually, albeit with relatively minor changes, including increased data collection related to international sanctions and asset freezing.</p> <p><i>...and continue to detect unlicensed virtual asset service providers:</i> At CBI, checks are carried out regularly, at least annually, to determine whether there is any activity operating without registration or authorization, including VASPs.</p> <p><i>...enhance AML/CFT supervision of banks.</i> Risk-based inspections have been enhanced and conducted in previous years and will continue according to the risk assessment framework.</p> |
| Continue to improve bank's access to and maintenance of adequate, accurate and up-to-date information on the beneficial                                                                   | NT                   | The Business Registry is utilizing inputs from registered entities to address discrepancies in Business Registry certificates. This data supports monitoring and supervisory actions that correct the beneficial ownership registry. Efforts are enhanced through regular                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                 |

| Recommendations                         | Horizon <sup>1</sup> | Status                                                                                                                                                                                      |
|-----------------------------------------|----------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| ownership and control of legal persons. |                      | communication with registered companies. A steering group, including participation from the CBI and other agencies, serves as a forum for coordination and improvement of AML/CFT measures. |

## Annex VI. Data Issues

| Annex VI. Table 1. Iceland: Data Adequacy Assessment for Surveillance                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    |                                                                                                 |        |                               |                            |                                   |                           |               |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------|--------|-------------------------------|----------------------------|-----------------------------------|---------------------------|---------------|
| Data Adequacy Assessment Rating <sup>1</sup>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                             |                                                                                                 |        |                               |                            |                                   |                           |               |
| A                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                        |                                                                                                 |        |                               |                            |                                   |                           |               |
| Questionnaire Results <sup>2</sup>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       |                                                                                                 |        |                               |                            |                                   |                           |               |
| Assessment                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                               | National Accounts                                                                               | Prices | Government Finance Statistics | External Sector Statistics | Monetary and Financial Statistics | Intersectoral Consistency | Median Rating |
|                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                          | A                                                                                               | A      | B                             | A                          | B                                 | A                         | A             |
| Detailed Questionnaire Results                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                           |                                                                                                 |        |                               |                            |                                   |                           |               |
| Data Quality Characteristics                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                             |                                                                                                 |        |                               |                            |                                   |                           |               |
| Coverage                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                 | A                                                                                               | A      | B                             | A                          | B                                 |                           |               |
| Granularity <sup>3</sup>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                 | B                                                                                               |        | A                             | A                          | B                                 |                           |               |
|                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                          |                                                                                                 |        | A                             |                            | B                                 |                           |               |
| Consistency                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                              |                                                                                                 |        | B                             | A                          |                                   | A                         |               |
| Frequency and Timeliness                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                 | A                                                                                               | A      | B                             | B                          | A                                 |                           |               |
| Note: When the questionnaire does not include a question on a specific dimension of data quality for a sector, the corresponding cell is blank.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                          |                                                                                                 |        |                               |                            |                                   |                           |               |
| <sup>1</sup> The overall data adequacy assessment is based on staff's assessment of the adequacy of the country's data for conducting analysis and formulating policy advice, and takes into consideration country-specific characteristics.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                             |                                                                                                 |        |                               |                            |                                   |                           |               |
| <sup>2</sup> The overall questionnaire assessment and the assessments for individual sectors reported in the heatmap are based on a standardized questionnaire and scoring system (see <i>IMF Review of the Framework for Data Adequacy Assessment for Surveillance</i> , January 2024, Appendix I).                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     |                                                                                                 |        |                               |                            |                                   |                           |               |
| <sup>3</sup> The top cell for "Granularity" of Government Finance Statistics shows staff's assessment of the granularity of the reported government operations data, while the bottom cell shows that of public debt statistics. The top cell for "Granularity" of Monetary and Financial Statistics shows staff's assessment of the granularity of the reported Monetary and Financial Statistics data, while the bottom cell shows that of the Financial Soundness indicators.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                         |                                                                                                 |        |                               |                            |                                   |                           |               |
| A                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                        | The data provided to the Fund are adequate for surveillance.                                    |        |                               |                            |                                   |                           |               |
| B                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                        | The data provided to the Fund have some shortcomings but are broadly adequate for surveillance. |        |                               |                            |                                   |                           |               |
| C                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                        | The data provided to the Fund have some shortcomings that somewhat hamper surveillance.         |        |                               |                            |                                   |                           |               |
| D                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                        | The data provided to the Fund have serious shortcomings that significantly hamper surveillance. |        |                               |                            |                                   |                           |               |
| <b>Rationale for staff assessment.</b> Data provision to the Fund is adequate for surveillance purposes. Expenditure-based GDP data are available by component on a quarterly basis. Nonetheless, there is still scope for improvement for Income Accounts by sector that are not sufficiently detailed and available only on an annual basis; Production-based GDP or gross value added by industry are available only on an annual basis and only in nominal terms. Statistics Iceland is in the initial phase of developing quarterly GDP data using the production approach. Currently, there are no plans to compile GDP data using the income approach. At the same time, Statistics Iceland plans to start compiling annual data using a more micro-based approach, potentially allowing for more detailed statistics. Recent uncertainty surrounding the 2025 general government deficit underscores the importance of timely information sharing and institutional coordination. Data on Services Exports are often significantly revised given collection lags. There is scope to improve cooperation and data sharing between Statistics Iceland and other institutions involved in data production including the CBI and the Ministry of Finance, in order to strengthen the analysis of economic developments and to ensure methodological consistency of compiled data with international standards. The authorities could consider publishing general government asset and liabilities statistics on a quarterly frequency and general government expenditure and revenue statistics on a monthly frequency. The 2023 FSAP found remaining data gaps in the monetary and financial sector data, notably in the CRE sector, micro household and NFC balance sheet data, and climate risks. |                                                                                                 |        |                               |                            |                                   |                           |               |
| <b>Changes since the last Article IV consultation</b> The authorities have formed a high-level working group that will look at ways to strengthen the infrastructure for data collection, building on experiences in other countries, and assess the resource needs of Statistics Iceland. Statistics Iceland is reviewing the methodology used for seasonally adjusting national accounts data. The decision to lower the data adequacy assessment for Government Finance Statistics from A to B relates to large uncertainty created by the 2025 fiscal outcome. Statistics Iceland has begun to address these issues by reviewing its data needs and sources and establishing a formal coordination process with the Financial Management Authority and the Ministry of Finance and Economic Affairs.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                 |                                                                                                 |        |                               |                            |                                   |                           |               |
| <b>Corrective actions and capacity development priorities</b> None beyond the issues raised above. No capacity development priorities.                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                   |                                                                                                 |        |                               |                            |                                   |                           |               |

**Annex VI. Table 2. Iceland: Data Standards Initiatives**

Iceland subscribes to the Special Data Dissemination Standard (SDDS) since June 1996 and publishes the data on its National Summary Data Page. The latest SDDS Annual Observance Report is available on the Dissemination Standards Bulletin Board (<https://dsbb.imf.org/>).

**Annex VI. Table 3. Iceland: Table of Common Indicators Required for Surveillance**

*As of June 23, 2026*

|                                                                                                          | Data Provision to the Fund |               |                                |                                     | Publication under the Data Standards Initiatives through the National Summary Data Page |                                  |                                    |                                   |
|----------------------------------------------------------------------------------------------------------|----------------------------|---------------|--------------------------------|-------------------------------------|-----------------------------------------------------------------------------------------|----------------------------------|------------------------------------|-----------------------------------|
|                                                                                                          | Date of Latest Observation | Date Received | Frequency of Data <sup>7</sup> | Frequency of Reporting <sup>7</sup> | Expected Frequency <sup>7,8</sup>                                                       | Announced Frequency <sup>9</sup> | Expected Timeliness <sup>7,8</sup> | Announced Timeliness <sup>9</sup> |
| Exchange Rates                                                                                           | 2026-06-22                 | 2026-06-22    | D                              | D                                   | D                                                                                       | D                                | ...                                | D                                 |
| International Reserve Assets and Reserve Liabilities of the Monetary Authorities <sup>1</sup>            | 2026-05                    | 2026-06       | M                              | M                                   | M                                                                                       | M                                | 1M (1W encouraged)                 | NLT 21D                           |
| Reserve/Base Money                                                                                       | 2026-04                    | 2026-05       | M                              | M                                   | M (W encouraged )                                                                       | M                                | 2W (1W encouraged)                 | NLT 1W                            |
| Broad Money                                                                                              | 2026-04                    | 2026-05       | M                              | M                                   | M                                                                                       | M                                | 1M                                 | 1M                                |
| Central Bank Balance Sheet                                                                               | 2026-05                    | 2026-06       | M                              | M                                   | M (W encouraged )                                                                       | M                                | 2W (1W encouraged)                 | NLT 1W                            |
| Consolidated Balance Sheet of the Banking System                                                         | 2026-05                    | 2026-06       | M                              | M                                   | M                                                                                       | M                                | 1M                                 | 1M                                |
| Total assets of other depository corporations <sup>2</sup>                                               | 2026-04                    | 2026-06       | M                              | M                                   | M                                                                                       | M                                | 1M                                 | 1M                                |
| Total credit from other depository corporations <sup>2</sup>                                             | 2026-04                    | 2026-06       | M                              | M                                   | M                                                                                       | M                                | 1M                                 | 1M                                |
| Interest Rates <sup>3</sup>                                                                              | 2026-06-22                 | 2026-06-22    | D                              | D                                   | D                                                                                       | D                                | ...                                | D                                 |
| Consumer Price Index                                                                                     | 2026-05                    | 2026-05       | M                              | M                                   | M                                                                                       | M                                | 1M                                 | NLT 2W                            |
| Revenue, Expenditure, Balance and Composition of Financing <sup>4</sup> -General Government <sup>5</sup> | 2026-03                    | 2026-06       | Q                              | Q                                   | A                                                                                       | Q                                | 2Q                                 | 1Q                                |
| Revenue, Expenditure, Balance and Composition of Financing <sup>4</sup> -Central Government              | 2026-03                    | 2026-06       | Q                              | Q                                   | M                                                                                       | Q                                | 1M                                 | 1Q                                |
| Stocks of Central Government and Central Government-Guaranteed Debt <sup>6</sup>                         | 2026-05                    | 2026-06       | M                              | M                                   | Q                                                                                       | Q                                | 1Q                                 | 1Q                                |
| Total stock of General Government Debt <sup>5</sup>                                                      |                            | 2026-03       | A                              | A                                   | ...                                                                                     | ...                              | ...                                | ...                               |
| External Current Account Balance                                                                         | 2026-03                    | 2026-06       | Q                              | Q                                   | Q                                                                                       | Q                                | NLT 10W                            | NLT 10W                           |

**Annex VI. Table 3. Iceland: Table of Common Indicators Required for Surveillance (concluded)**

|                                           |         |         |   |   |   |   |                      |         |
|-------------------------------------------|---------|---------|---|---|---|---|----------------------|---------|
| Exports and Imports of Goods and Services | 2026-03 | 2026-06 | Q | Q | M | M | 8W (4-6W encouraged) | NLT 5W  |
| GDP/GNP                                   | 2026-03 | 2026-06 | Q | Q | Q | Q | 1Q                   | 75D     |
| Gross External Debt                       | 2026-03 | 2026-06 | Q | Q | Q | Q | 1Q                   | NLT 10W |
| International Investment Position         | 2026-03 | 2026-06 | Q | Q | Q | Q | 1Q                   | NLT 10W |

<sup>1</sup> Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.

<sup>2</sup> Other depository corporations include all deposit-taking corporations (except for the central bank) and money market funds.

<sup>3</sup> Both market-based and officially determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.

<sup>4</sup> Foreign, domestic bank, and domestic non-bank financing.

<sup>5</sup> The general government consists of the central government (budgetary funds, extra-budgetary funds, and social security funds) and state and local governments. The total stock of general government debt is required for SDDS Plus countries and encouraged for SDDS and e-GDDS countries.

<sup>6</sup> Including currency and maturity composition.

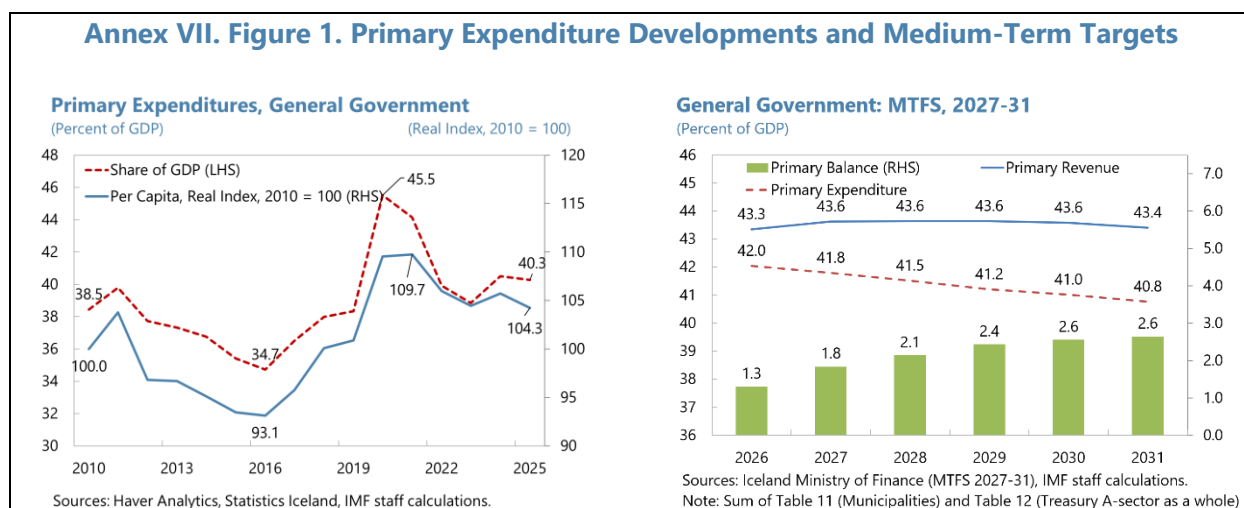
<sup>7</sup> Frequency and timeliness: ("D") daily; ("W") weekly or with a lag of no more than one week after the reference date; ("M") monthly or with lag of no more than one month after the reference date; ("Q") quarterly or with lag of no more than one quarter after the reference date; ("A") annual; ("SA") semi-annual; ("I") irregular; ("NA") not available or not applicable; and ("NLT") not later than.

<sup>8</sup> Encouraged frequency of data and timeliness of reporting under the e-GDDS and required frequency of data and timeliness of reporting under the SDDS and SDDS Plus. Any flexibility options or transition plans used under the SDDS or SDDS Plus are not reflected. For those countries that do not participate in the IMF Data Standards Initiatives, the required frequency and timeliness under the SDDS are shown for New Zealand, and the encouraged frequency and timeliness under the e-GDDS are shown for Eritrea, Nauru, South Sudan, and Turkmenistan. Indicators that are not in the IMF Data Standards Initiatives are shown as "...".

<sup>9</sup> Based on the information from the Summary of Observance for SDDS and SDDS Plus participants, and the Summary of Dissemination Practices for e-GDDS participants, available from the IMF Dissemination Standards Bulletin Board (<https://dsbb.imf.org/>). For those countries that do not participate in the Data Standards Initiatives, as well as those that do have a National Data Summary Page, the entries are shown as "...".

## Annex VII. Observations from Benchmarking of Public Spending<sup>1</sup>

**1. Ambitious fiscal consolidation plans and resilience objectives justify a closer examination of public spending efficiency.** The authorities' Medium-Term Fiscal Strategy targets a sizeable consolidation of about 1.2 percent of GDP in primary expenditure, supported by broad-based measures including staffing rationalization and efficiency gains. This reflects the need to rebuild buffers in an economy exposed to large shocks while accommodating moderate long-term spending pressures related to health and infrastructure, alongside emerging risks.



**2. Primary expenditure has increased significantly, and some spending categories stand out relative to peers.** Primary expenditures has risen significantly—by around 6 percent of GDP between 2016 and 2025, equivalent to a 12.5 percent increase in real per capita terms. In this context, some spending categories stand out as comparatively high. For instance, spending on health, education, recreation and culture, and the public sector wage bill exceed Nordic comparators by about 2.5 percent of GDP and euro-area peers by close to 5 percent of GDP. While part of this reflects structural features of a small economy with high fixed costs, the magnitude suggests scope for efficiency gains.

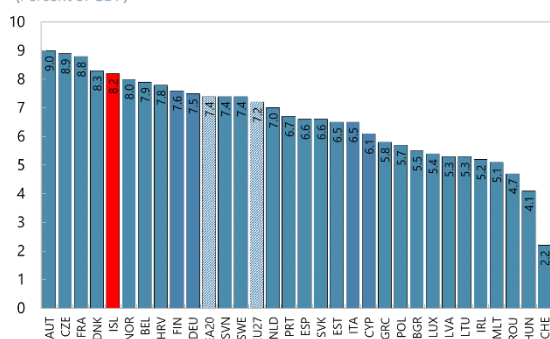
| Spending, 2023           | Iceland     | Nordics     | Euro Area   |
|--------------------------|-------------|-------------|-------------|
| Health                   | 8.2         | 7.8         | 7.4         |
| Recreation               | 3.0         | 1.5         | 1.1         |
| Education                | 6.7         | 6.0         | 4.6         |
| <b>Sum</b>               | <b>17.9</b> | <b>15.3</b> | <b>13.1</b> |
| Public sector wage bill* | 14.2        | 13.0        | 9.9         |

Source: Eurostat, IMF staff calculations.  
Note: \*2024

<sup>1</sup> Prepared by T. Gade (EUR).

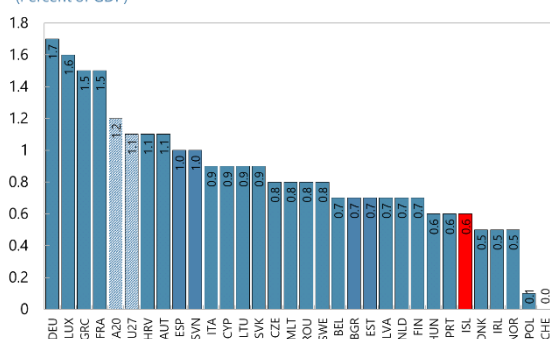
Annex VII. Figure 2. Health Spending Categories

### Health, 2023 (Percent of GDP)



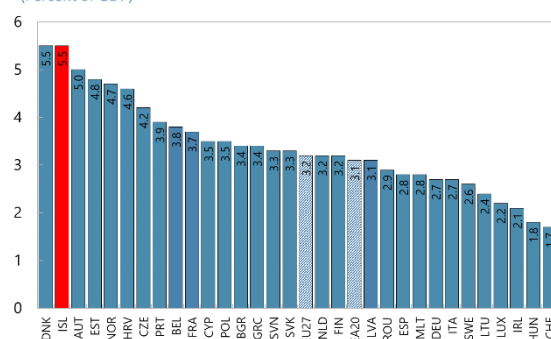
Sources: Eurostat, IMF staff calculations.

### Medical Products, Appliances, and Equipment, 2023 (Percent of GDP)



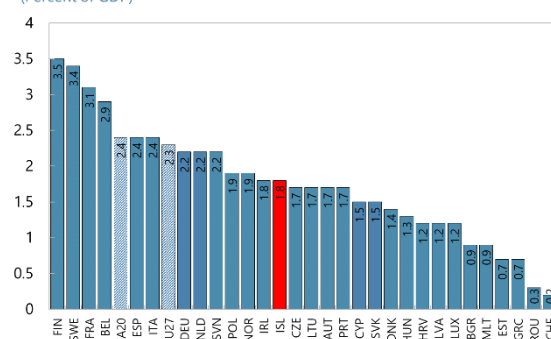
Sources: Eurostat, IMF staff calculations.

### Hospital Services, 2023 (Percent of GDP)



Sources: Eurostat, IMF staff calculations.

### Outpatient Services, 2023 (Percent of GDP)



Sources: Eurostat, IMF staff calculations.

**3. Health spending is driven by high hospital expenditures, although overall efficiency remains strong.** Spending is primarily concentrated in hospital services, while outlays on outpatient care and medical goods are comparatively lower. This may in part be explained by the construction of the new national hospital, which is a key investment in healthcare infrastructure and is expected to improve service delivery and efficiency through consolidation of fragmented facilities. For its income level, Iceland lies close to the efficiency frontier in terms of life expectancy outcomes, indicating broadly effective resource use, and only limited scope for efficiency gains.

Annex VII. Figure 3. Health Spending Efficiency

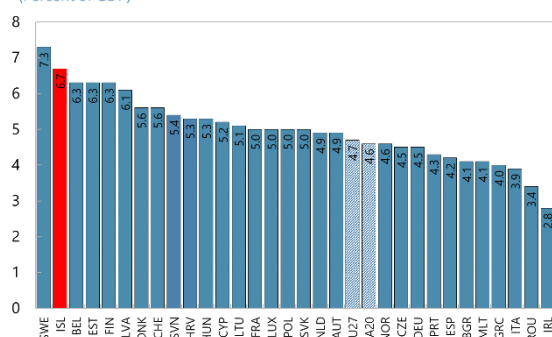


**4. Education spending is high across all levels, particularly in pre-primary and primary education.** Public spending on education exceeds EU and euro area averages by about 2 percent of GDP, with elevated spending broadly distributed across education levels but especially pronounced in early education. Structural and demographic factors partly explain this pattern, though the magnitude suggests scope for efficiency improvements.

**5. Education outcomes relative to level of spending point to scope for improved efficiency.** Benchmarking of outcomes, including PISA scores and tertiary attainment, indicates that Iceland could achieve stronger results for a given level of spending. Efficiency analysis highlights both input inefficiencies (excess resource use for given outcomes) and output inefficiencies (suboptimal outcomes given inputs), warranting deeper analysis at the program level.

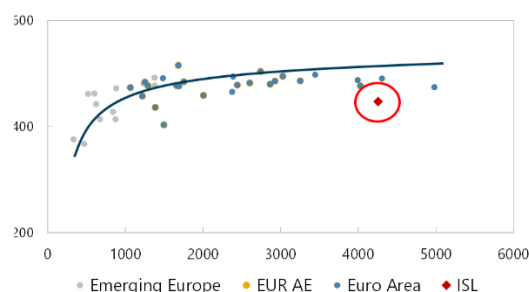
Annex VII. Figure 4. Education Spending Categories and Efficiency Indicators

### Education, 2023 (Percent of GDP)



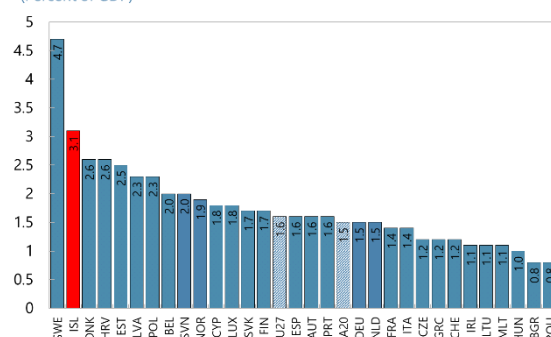
Sources: Eurostat, IMF staff calculations.

### Per Capita Spending and PISA Score

[Link to data](#)

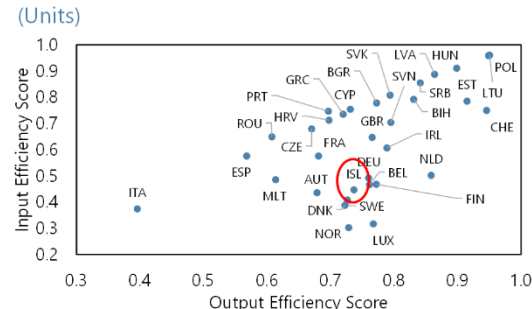
Sources: OECD and World Bank Education Statistics.

### Pre-Primary and Primary Education, 2023 (Percent of GDP)



Sources: Eurostat, IMF staff calculations.

### Input-Output Efficiency Score (Units)

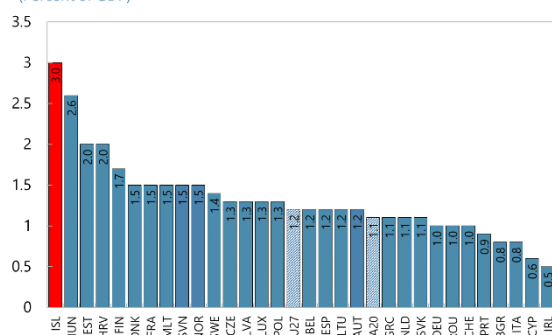
[Link to data](#)

Source: IMF staff calculations.

**6. Spending on recreation and culture is relatively high but reflects structural and social preferences.** Although these expenditures represent a relatively small share of total spending, they exceed comparator levels and could yield savings if gradually aligned with Nordic or EU averages. Cost drivers include low population density, small-scale effects, climate-related infrastructure needs (e.g., indoor facilities), social choice in public services, and possibly tourism-related services, which generate other revenues.

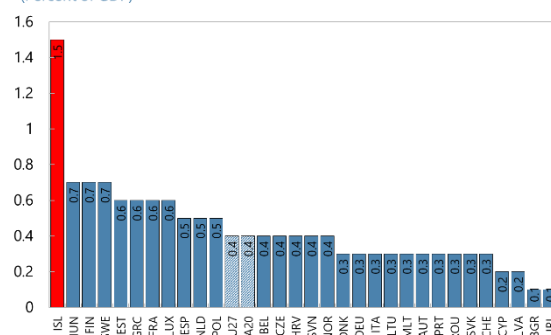
Annex VII. Figure 5. Recreation, Culture and Religion

### Recreation, Culture, and Religion, 2023 (Percent of GDP)



Sources: Eurostat, IMF staff calculations.

### Recreational and Sporting Services, 2023 (Percent of GDP)



Sources: Eurostat, IMF staff calculations.

**7. Assessing efficiency on recreational spending is challenging, but the spending category overall warrants further scrutiny.** Given the difficulty in quantifying output, particularly for cultural services, spending levels are partly a matter of social choice. Nonetheless, the magnitude of deviations suggests potential gains from targeted reviews of prioritization and delivery models.

**8. The public sector wage bill is high and has increased significantly over the past decade.** Iceland has the second-highest public wage bill in Europe, rising by about 1.5 percent of GDP since 2015 to around 14.5 percent of GDP. The increase has been driven primarily, but not exclusively, by municipalities.

**9. Public employment and wages have outpaced the private sector along both margins.** Public sector wages have grown faster than private sector wages, particularly at the municipal level, while the share of public employment has also increased. This expansion reflects both higher compensation per public employee and increases in the number of employees, contributing to structural spending pressures.

**10. There is scope to strengthen efficiency and contain spending growth while preserving outcomes.** The sustained increase in primary expenditure and elevated levels in selected categories point to potential efficiency gains. In particular, education and selected service sectors warrant detailed reviews of spending effectiveness, while in health, maintaining high outcomes at lower cost should remain a key objective.

**11. Containing the wage bill is central to fiscal adjustment.** Bringing the public wage bill closer to pre-pandemic levels—especially at the municipal level—through a combination of wage restraint and gradual staffing adjustments would support consolidation while preserving service delivery. Reducing the public sector employment share could also enhance labor market flexibility and medium-term growth.

## Annex VIII. Pros and Cons of the Choice of Exchange Rate Regime for Iceland in the Context of Possibly Restarting EU Accession Negotiations<sup>1</sup>

*In assessing euro adoption specifically, the main arguments in favor are: (i) lower transaction costs and elimination of króna–euro exchange-rate uncertainty for trade and investment; (ii) a more robust nominal anchor that could help durably reduce inflation and bring Icelandic interest rates closer to euro-area peers; and (iii) deeper integration into EU financial frameworks (including Banking Union and Capital Markets Union) that could strengthen supervision and crisis management and broaden market-based financing. The main arguments against are: (i) loss of independent monetary and exchange-rate policy that have historically helped absorb Iceland’s large, often idiosyncratic shocks; (ii) risk of “one-size-fits-all” ECB policy being poorly aligned with Iceland’s domestic cycle given the economy’s sectoral concentration and shock exposure; and (iii) greater exposure to euro-area-wide tail risks through shared backstops and crisis mechanisms. These considerations imply that—if Iceland were to choose the euro—strengthening domestic adjustment capacity (wage-setting, fiscal buffers, and resilience of the financial system), and reviewing the prevalence of indexation, would become even more important in the absence of an independent monetary policy and the exchange rate as an adjustment mechanism.*

### A. Context

**1. The Icelandic Government plans a national referendum on resuming accession negotiations for Iceland’s membership in the EU on August 29.** A second referendum (at a later stage) would determine whether Iceland would join the EU. If Iceland were to join the EU, the country would be expected to become a member of the Economic and Monetary Union (EMU), Banking Union and Capital Markets Union, all of which could have important implications for Iceland’s economic stability and development. To support public discussion on the matter, ahead of the upcoming referendum, a committee of independent foreign experts was tasked with preparing a report on Iceland’s currency and exchange rate policy options, in particular on the benefits and costs of joining the EMU, published in June 2026.<sup>2,3</sup>

**2. Iceland’s relationship with the EU has been evolving for decades.** As a member of the European Free Trade Association (EFTA) since 1970 and the European Economic Area (EEA) since 1994, Iceland already implements a large portion of the EU single market legislation and enjoys free movement of goods, services, capital, and people with the EU. It also participates in Schengen, various EU programs, and aligns closely with EU standards in many areas (e.g. consumer protection, environment, financial regulation) as part of EEA obligations. Iceland is not part of the EU’s Customs Union, Common Agricultural Policy, and Common Fisheries Policy, or the Economic and Monetary

<sup>1</sup> Prepared by T. Gade (EUR).

<sup>2</sup> See the Report on [Currency Matters](#), May 13, 2026.

<sup>3</sup> See also Central Bank of Iceland, 2012, [Iceland’s currency and exchange rate options](#), for an earlier and detailed assessment of the pros and cons of euro adoption and the 2017 Central Bank of Iceland report documenting the post-crisis policy reforms and improved policy outcomes.

Union (euro area). Iceland's EU membership bid in 2009–2013 progressed considerably before domestic politics led to a freeze.

**3. Joining the EU implies a commitment to join the Economic and Monetary Union, meaning Iceland would be expected to adopt the euro once it meets the Maastricht convergence criteria.** In practice, the timing of euro adoption is de facto flexible – some EU members have delayed joining the euro for years by not immediately entering ERM II. Nevertheless, if Iceland were to decide on joining the EU, it would eventually be on a path toward euro area membership, entry into the Banking Union, and participation in broader EU financial structures like the Capital Markets Union (CMU) and the Savings and Investment Union (SIU).

## B. Economic and Financial Trade-Offs

**4. A comprehensive assessment of a country's macroeconomic initial conditions, structural characteristics, and exposure to economic shocks is essential for determining the most appropriate exchange rate arrangement.**<sup>4</sup> Initial conditions—such as inflation, fiscal position, and reserve adequacy—affect a country's capacity to maintain stability under different exchange rate regimes. The economic structure, including factors like size, openness, extent of trade integration, economic and financial cycle synchronization, and labor market flexibility, influence how much the economy is in sync with the economy of the anchor currency, and how effectively an economy can adjust to changes without relying on exchange rate movements. Meanwhile, the nature and frequency of external and domestic shocks determine the usefulness of exchange rate flexibility as a shock absorber. Annex Figure 5 (end of note) presents a summary of these considerations for Iceland, while the sections below provide a more detailed assessment.

### *Initial conditions*

**5. Choosing an appropriate exchange rate arrangement requires a careful assessment of a country's initial macroeconomic conditions.** As outlined in the IMF's MCM Technical Assistance Handbook, factors such as inflation dynamics, external imbalances, fiscal space, reserve adequacy, and financial vulnerabilities are critical in determining whether a fixed or flexible exchange rate regime is preferable, or which reform measures would be needed to create adequate conditions. These conditions influence the capacity of a country to maintain external and internal stability under different regimes and help identify the policy trade-offs involved in the choice.

**6. Iceland has had higher and more volatile inflation than the euro area.** Under a float, the ISK can depreciate when domestic inflation outpaces partners', helping limit real overvaluation and loss of competitiveness. Euro adoption would potentially strengthen monetary credibility by importing the ECB's track record and could – over time – provide a more robust nominal anchor for inflation expectations than Iceland has historically achieved, potentially facilitating downward convergence of market interest rates toward euro-area levels over time. These gains would, however, come at the cost of removing independent monetary policy and the exchange-rate instrument, leaving Iceland with a one-size-fits-all interest rate that may not match domestic cyclical

<sup>4</sup> See IMF Monetary and Capital Markets Department, Technical Assistance Handbook, [Choice of Exchange Rate Arrangement](#), December 2022.

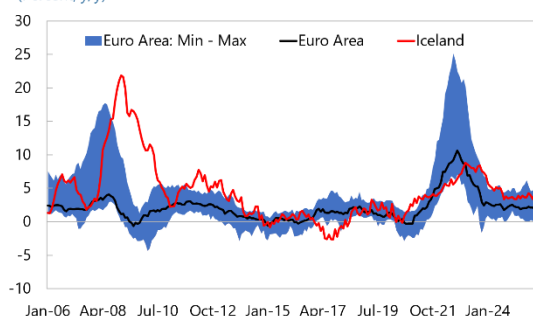
conditions. Historically, inflation in Iceland has been higher and not well correlated with inflation in the euro area, resulting in part in trend appreciation of the real exchange rate, and the CBI consistently having a higher monetary policy rate than the ECB over the last two decades (See Figure 1). Sustaining low inflation under the euro would depend critically on complementary domestic reforms — most importantly productivity-aligned wage setting, but likely also reforms of the prevalence of indexed-linked lending in Iceland, which may dampen the transmission of monetary policy.

**7. Iceland currently shows no major external imbalances.** With a floating ISK, small misalignments can correct through market movements; under a peg/euro, adjustment would rely more on wages and prices (“internal devaluation”). FX reserves are around 20 percent of GDP (over 120 percent of the IMF adequacy metric), sufficient under a float and gaining access to possible Eurosystem intervention in the interim is a mitigating factor. Once in the euro, reserve needs would fall—lowering the CBI’s “insurance” cost of having large reserves—and access to Eurosystem liquidity could strengthen crisis backstops. Overall, today’s external position supports either regime and would ease a transition to a tighter peg or the euro.

**Annex VIII. Figure 1. Indicators of Initial Conditions**

**Inflation Rate Across the Euro Area and Iceland**

(Percent, y/y)

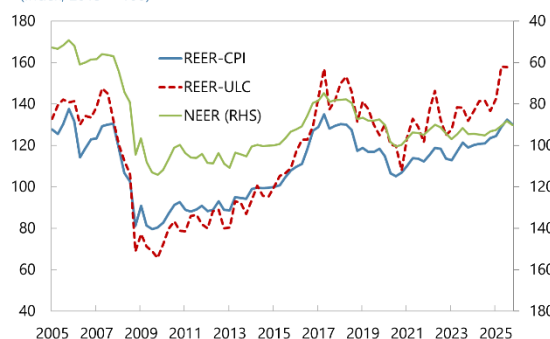


Sources: Haver Analytics and IMF staff calculations.

Note: The chart shows HICP for all countries, while Iceland targets national CPI.

**Real and Nominal Effective Exchange Rates**

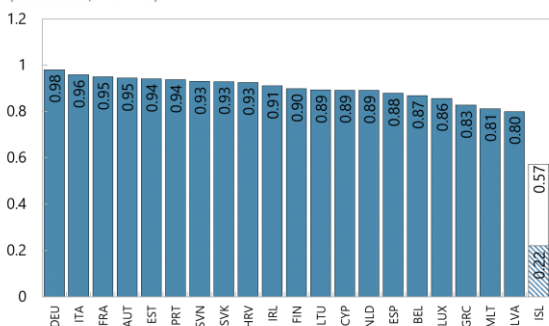
(Index, 2015 = 100)



Sources: Haver Analytics, Central Bank of Iceland, IMF staff calculations.

**Y/Y Inflation Correlation, 2005-25**

(Correlation, -1.0 : 1.0)

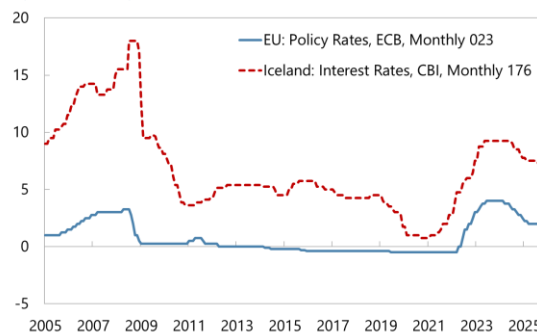


Sources: Haver Analytics, IMF staff calculations.

Note: Shaded bar is 2005-25, while the added non-shaded bar is 2010-25.

**Iceland and Euro Area Monetary Policy Rates**

(Percent Annual)



Sources: Haver Analytics.

**8. Iceland has limited economy-wide FX mismatches.** IMF analysis under the Integrated Policy Framework finds no significant aggregate balance-sheet mismatches; banks' foreign liabilities largely fund exporters with FX income, and regulation limits open FX positions.<sup>5</sup> The 2023 FSAP notes FX funding reliance, but views risks as mitigated and FX reserves as a likely backstop in severe stress.<sup>6</sup> This reduces the case for a fixed rate on financial stability grounds and leaves room for a float. However, given the size of the Icelandic occupational pension system and their large foreign currency assets, adopting the euro would reduce trading costs and exchange rate risks for a large part of these assets. Euro membership would further reduce residual currency risk and improve funding stability via the ECB's lender-of-last-resort role.

**9. Strong public finances are essential under any regime.** Iceland's fiscal position has improved after the large deficits during the pandemic, with consolidation aimed at restoring overall balance by 2027 and keeping debt on a declining, sustainable path. A key vulnerability is its history of pro-cyclical fiscal policy. However, the net expenditure rule and debt anchor are intended to strengthen discipline and are broadly in line with the revised fiscal rules in the EU. Under a float, monetary policy and the exchange rate can partly offset fiscal slippage, while under the euro, fiscal policy becomes the primary stabilization tool when domestic conditions diverge from the euro area. The recently amended fiscal stability rule with its net expenditure rule limits procyclical fiscal policy going forward, and with Iceland's relatively favorable debt/deficit metrics, they support feasibility of euro adoption.

**10. Overall, Iceland's initial conditions present a mixed picture for the choice of exchange rate regime.** Given Iceland's history of higher and more volatile inflation, euro adoption could—in principle—provide further monetary credibility, while it would also eliminate the exchange rate as a stabilizer. Meanwhile, the elimination of króna–euro currency risk, and prospects for lower borrowing costs are clear advantages of euro-area membership. Adequate reserves and sustainable public debt provide Iceland the option to consider euro adoption from a position of strength, but the balance of costs and benefits would ultimately hinge on whether domestic institutions—especially wage-setting and fiscal frameworks—can deliver internal adjustment when shocks hit and domestic conditions diverge from the euro area.

### ***Structure and Flexibility of the Economy***

**11. The structural characteristics of an economy—its size, openness, trade integration and export diversification, economic and financial cycles, labor market flexibility, and financial development—play a central role in shaping the suitability of an exchange rate regime.**

Beyond macro indicators, structural features of Iceland's economy influence the exchange rate cost-benefit analysis. Classic Optimal Currency Area (OCA) theory suggests that the suitability of a fixed vs. flexible currency depends on traits like economic size, openness, diversification, integration with potential partner countries, and labor market flexibility and ability to adjust internally.

<sup>5</sup> See IMF Iceland Selected Issues Paper '[Integrated Policy Framework – Iceland Pilot Study](#)', 2024.

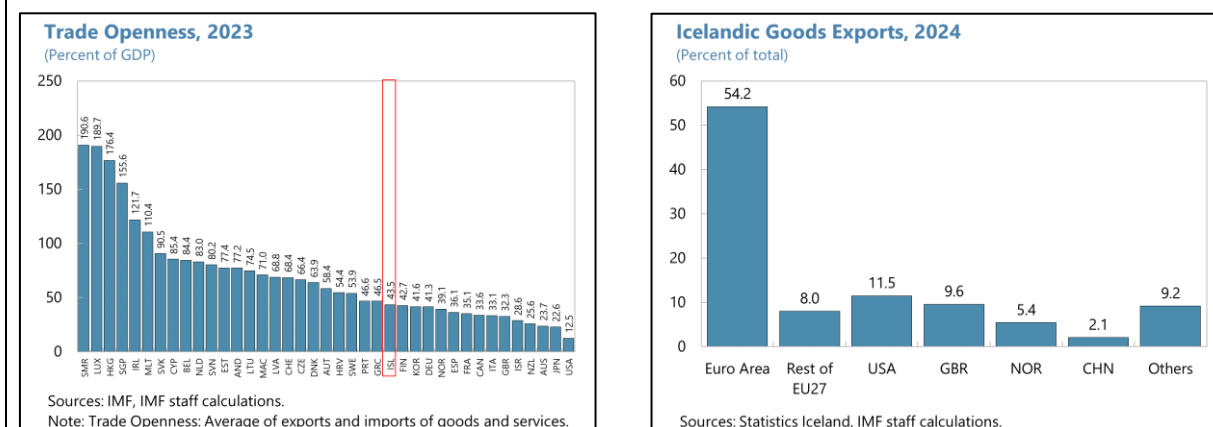
<sup>6</sup> See IMF Iceland: [Financial System Stability Assessment](#), June 2023.

**12. Small economic size makes the euro's stability attractive.** Very small economies often struggle to run independent monetary policy and therefore adopt hard pegs or foreign currencies. Iceland is a small open economy with strong institutions, and experience with inflation targeting under a floating króna. The trade-off is between importing credibility and lower premia via a large currency area versus retaining exchange-rate adjustment for asymmetric shocks vis-à-vis the euro area. If Iceland keeps the króna, sustaining credibility requires continued fiscal discipline and flexible markets; if it adopts the euro, it gains scale benefits (lower transaction costs and potentially lower interest rate premia) at the expense of policy autonomy.

**13. High openness and deep EU trade links strengthen the case for a tighter euro link.**

Trade is about 100 percent of GDP, and the EU is Iceland's main partner with roughly 55 percent+ of goods exports (and over half of imports) sent to the euro area (see Figure 2). Under the OCA logic, this raises the potential benefits of euro adoption via lower transaction costs, elimination of króna-euro exchange-rate uncertainty, and reduced frictions for investment with Europe. The flip side is reduced flexibility: if competitiveness shifts, a float can adjust quickly, whereas euro/peg adjustment would rely on prices and wages ("internal devaluation"). Euro adoption would remove króna-euro risk but not eliminate exposure to other exchange rates—most importantly the US dollar—given global pricing of key exports (e.g., seafood and aluminum) and significant pensions sector foreign assets.

**Annex VIII. Figure 2. Openness and Trading Partners**



**14. A flexible labor market improves feasibility of euro membership by enabling internal adjustment.** Iceland's flexicurity model, relatively adaptable hiring/firing, and labor mobility support adjustment when shocks hit. This matters most under the euro or a hard peg, where devaluation is unavailable and competitiveness must be restored through wages, productivity, and resource reallocation. Alignment of wage growth with productivity would be especially critical in a post-euro-adoption scenario, since misalignments could no longer be corrected by exchange-rate moves. Overall, labor-market flexibility is a structural point in favor of a currency union, provided it remains effective in practice.

**15. With an open capital account, regime choice is shaped by the monetary-policy**

**trilemma.** Iceland has largely free capital flows with broad-based capital controls imposed after the financial crisis lifted in 2017, and remaining restrictions subsequently lifted by 2021, implying that a fixed rate would eliminate independent monetary policy. The current float preserves monetary autonomy and lets the exchange rate absorb capital-flow shocks, as well as aids the adjustment of real shocks. Euro adoption would remove intra-EU currency risk and may attract investment, but Iceland would forgo national interest-rate policy and face tighter constraints on crisis measures such as unilateral capital controls. Adjustment would rely more on fiscal buffers, macroprudential policy, and euro-area institutions.

**16. Shallow ISK capital markets raise the cost of a small currency area, while euro adoption would deepen financing—but also shift key levers to EU institutions.**

Iceland's bond market and hedging instruments are relatively limited, which can amplify currency-risk premia and deter some foreign investors. A float creates ongoing demand for hedging and risk pricing; a hard fix or euro adoption would reduce króna risk (at least vs the euro) and facilitate firm's access to deeper European capital markets.

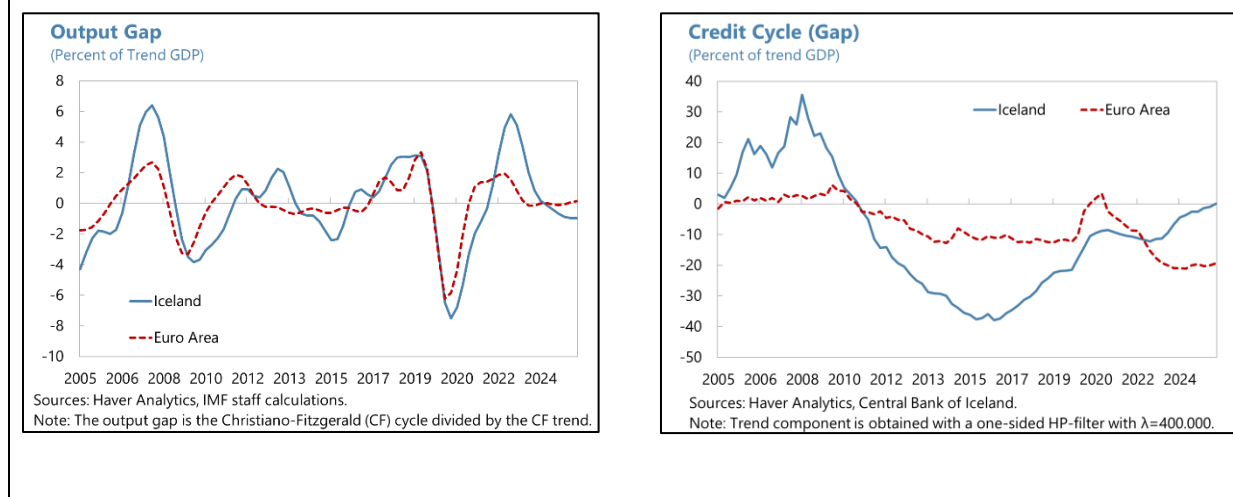
**17. In summary, Iceland's economic structure and flexibility offer both pros and cons of euro adoption.**

Iceland's high integration with the EU, flexible labor market, and solid institutions strengthen the case that internal adjustment could work under a currency union. Euro adoption could also lower financing costs over time by reducing currency and country risk premia and by improving access to deeper European capital markets. At the same time, Iceland's reliance on volatile sectors and exposure to country-specific shocks increases the insurance value of an independent monetary policy and a shock-absorbing exchange rate, while ECB policy—set for average euro-area conditions—could at times be poorly aligned with Iceland's domestic cycle.

***Shocks and Economic Resilience*****18. The nature, frequency, and symmetry of shocks that affect an economy are pivotal in determining the optimal exchange rate arrangement.**

Economies subject to large, frequent, or asymmetric external shocks—such as terms-of-trade fluctuations or volatile capital flows—may benefit from greater exchange rate flexibility to absorb these disturbances. Conversely, economies experiencing more symmetric shocks with their trading partners may find fixed regimes or currency unions more manageable. Analyzing the types of shocks, in conjunction with initial conditions, provides a comprehensive view of the adjustment mechanisms available under different regimes.

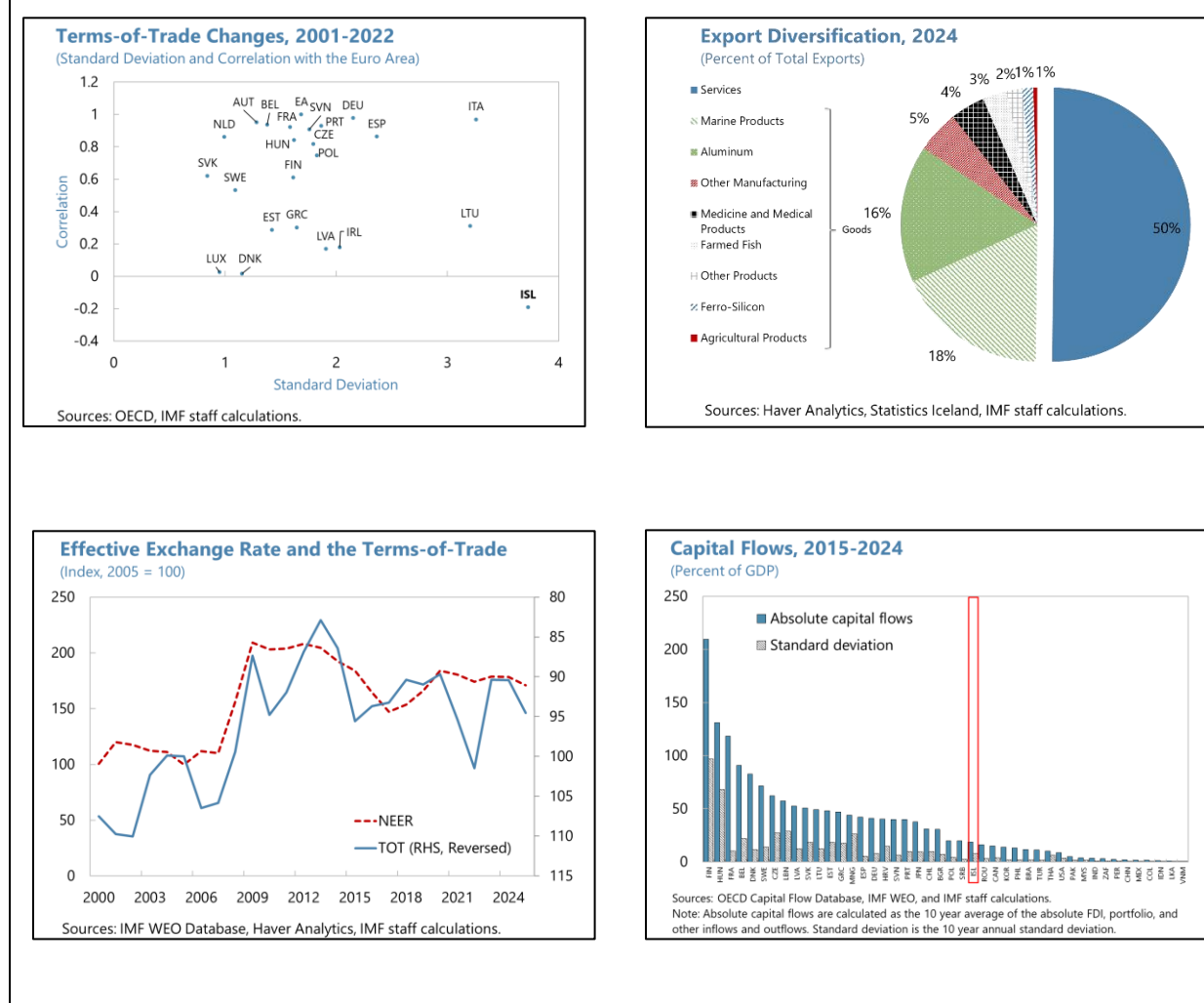
Annex VIII. Figure 3. Economic and Credit Cycles



**19. The greater economic and financial cycles are broadly in sync with the euro area.** The broad economic cycle is fairly well in sync with the euro area economic cycle, indicating that some shocks are global and shared with the euro area. However, there have been periods of divergence, e.g., in 2012–2015, a period when Iceland was hit by volatile fish and aluminum prices, as well as in 2022–2024, with the surge in tourism following the pandemic (see Figure 3). Meanwhile, the credit cycle in Iceland—while sharing some of the dynamics of the credit cycle of the euro area—has historically had a much larger amplitude. This is to a large part due to the credit boom leading up to the 2008 crisis and the years of balance sheet repair that followed. This could suggest that greater monetary policy movement is needed to curb the credit cycle, or/and underscore the importance of vigilant use of macroprudential tools.

**20. Iceland is exposed to large idiosyncratic shocks, especially through volatile terms of trade and tourism demand.** Iceland is more diversified than many small economies (sizeable services and public sectors; exports split between goods and services), yet output and external earnings still hinge on fisheries, aluminum, and tourism, and are thus exposed to large external and natural-resource shocks, as reflected in Iceland's large terms-of-trade shocks, which are both larger and less correlated relative to other European Union countries with the terms-of-trade shocks hitting the euro area (see Figure 4). Under the floating króna, depreciation after adverse terms-of-trade shocks helps cushion the economy by supporting competitiveness and compressing imports (as in 2008 and during COVID-19). Under the euro, this automatic buffer would be absent, and adjustment would rely on wages/prices ("internal devaluation"), labor reallocation, and fiscal support.

Annex VIII. Figure 4. Indicators of Economic Shocks



**21. Capital-flow shocks have mattered historically (notably around the 2000s boom-bust and banking crisis), though today flows are more moderate under stronger regulation and oversight.** With free capital mobility, a flexible exchange rate helps absorb shifts in global risk sentiment, while a fixed rate can be vulnerable to pressure if reserves are tested. While the króna is not assessed to be more volatile as other peer currencies, in part historically because of capital controls, adopting the euro would remove króna volatility and currency-crisis risk and could strengthen backstops through Eurosystem facilities, but it would not eliminate capital cycles and may amplify credit booms if currency risk premia fall.

**22. In summary, the broader economic and financial cycles are broadly in sync with the euro area, but Iceland is subject to significant, often country-specific shocks – a fact that underlines the value of a flexible exchange rate as a shock absorber.** If Iceland opts for the euro, it will need to rely on other mechanisms (fiscal, labor, and macroprudential policies, as well as European backstops) to manage those shocks—accepting some exposure to euro-area-wide tail risks through shared crisis mechanisms. The decision, then, hinges on whether the benefits of

stability and integration (including lower transaction and financing costs) outweigh the costs of losing the exchange-rate tool in the face of volatility.

## C. European Institutional Membership: Pros and Cons

**23. Euro area membership brings automatic participation in the EU Banking Union: the Single Supervisory Mechanism (SSM) led by the ECB, and the Single Resolution Mechanism (SRM).<sup>7</sup>** While supervision in Iceland is already strong, membership of the Banking Union would place major Icelandic banks under a well-known rigorous, harmonized supervisory framework, potentially strengthening confidence and increasing the likelihood that risks are detected early. In stress, access to ECB liquidity facilities and EU-wide resolution arrangements would improve crisis backstops, potentially lowering banks' funding costs. The main trade-off is reduced national discretion over supervision and crisis management, plus contributions to shared funds and some exposure to cross-border risk sharing. Overall, the Banking Union would anchor Iceland's financial system in a larger stability framework, at the cost of sovereignty over key financial decisions.

**24. The initiatives under the Capital Markets Union (CMU) and Savings & Investment Union (SIU) aim to deepen and integrate Europe's capital markets, reduce barriers to cross-border investment, and broaden financing beyond bank credit.** The key benefits would be access to a much larger pool of funding for firms, infrastructure, and innovation; more diversified investment opportunities for long-term savers (including pension funds); and, over time, lower costs of capital as country- and currency-risk premia decline in a more integrated market. EU membership would also give Iceland a voice in shaping these rules rather than passively adopting them via the EEA. The main caveats are that the CMU/SIU remain incomplete and benefits may take time; regulatory and legal reforms could impose adjustment costs; and deeper financial integration can increase exposure to pan-European credit and asset-price cycles—raising the importance of macroprudential and fiscal tools.

**25. EU/euro membership would embed Iceland in broader European frameworks (including the European Stability Mechanism, euro-area economic coordination and fiscal rules, and EU budget programs).** A core benefit is stronger investor confidence: membership in a larger and more recognizable policy framework signals stable, rules-based policymaking and can lower perceived country risk, supporting FDI and more resilient market access in stress periods. While Iceland already implements much of the *acquis* via the EEA, EU membership would add additional representation and provide voting rights where rules are set. The main cost is reduced ability to opt out: Iceland would be bound by majority decisions and would face sensitive issues beyond the monetary union (notably the Common Fisheries Policy). In finance, Iceland may need to align any "stricter-than-EU" safeguards with EU law.

---

<sup>7</sup> Participation in the Banking Union is mandatory for members of the euro area. Non-euro-area EU members can, however, voluntarily join the Banking Union under a close collaboration arrangement.

## D. Preparing for the Euro: Key Structural Reforms

**26. Euro or not, key reforms are essential.** If Iceland chooses to move toward euro adoption, reforms that strengthen internal adjustment and policy credibility would become more binding because the exchange rate and independent monetary policy would no longer cushion shocks. Priorities include wage-setting arrangements that align pay with productivity, continue implementing a fiscal framework that rebuilds buffers and supports countercyclical policy, and continued strengthening of financial-sector resilience. Entry conditions would also matter: adopting the euro at an overvalued exchange rate would risk locking in competitiveness losses and forcing costly internal devaluation. Many of these reforms are prudent even if Iceland retains the króna, but they become even more important under a fixed exchange-rate regime.

**27. Wage setting and labor flexibility:** Without the exchange rate as an adjustment valve, euro membership increases the premium on productivity-linked wage growth and rapid “internal” adjustment following asymmetric shocks. Building on Iceland’s social dialogue, wage bargaining frameworks should strengthen mechanisms that anchor pay outcomes to productivity and the low-inflation environment (consistent with ECB’s price stability objective), and allow agreements to be revisited when large shocks hit. Preserving flexicurity, labor mobility, and openness to foreign workers would help reallocate labor across sectors and reduce the output costs of adjustment.

**28. Prevalence of indexation in the economy.** Many contracts in Iceland are linked to the inflation rate. This includes e.g. rents, utilities, public procurement, many benefits, collective wage agreements with specific inflation trigger clauses, as well as mortgages. This could create greater inflation persistence and potentially dampen monetary policy transmission. Reviewing and possibly reforming the degree of indexation might be important with the current setup, but especially in case of euro adoption.

**29. Fiscal governance and buffers:** In a currency union, fiscal policy must do more stabilization work, making credible rules and buffers essential. Consistent with the IMF’s 2024 and 2025 Article IV advice, Iceland should continue to implement the planned fiscal-rule framework and materially strengthen the Fiscal Council’s mandate, resources, and access to timely data.<sup>8</sup> Medium-term consolidation should rebuild space in good times, while allowing room for public investment.

**30. Financial sector and prudential policies:** Iceland should preserve strong supervision and high resilience through the potential transition to ERM II/euro and keep macroprudential policy tight enough to contain housing/credit risks, especially during a transition towards the euro. Ample FX reserves should be maintained in this period. Safeguarding supervisory independence, strengthening pension-fund governance and risk management, advancing AML/CFT, and improving operational resilience (cyber, payments) and crisis tools (ELA and resolution readiness) is key.

**31. Legal and institutional readiness:** Euro adoption requires legal alignment, including a mandate consistent with euro-area price stability, and preparing the operational/legal framework for participation in the Eurosystem. Any constitutional implications of giving up the legal tender should

---

<sup>8</sup> See Iceland IMF staff reports [2024](#) and [2025](#) Article IV.

be assessed early to avoid delays. Finally, higher productivity and diversification reduce the costs of losing the exchange-rate tool: initiatives such as the Productivity Commission, reforms that raise competition and ease regulation, and investments in skills and innovation (including in energy-based and tech sectors) would strengthen resilience under either regime.

**32. In summary, Iceland has already made strides in many of the areas (fiscal prudence, labor flexibility, financial oversight, and macroprudential policy) that are key for potential euro adoption.** The experience of some euro area countries shows that inadequate preparation—e.g., entering the euro with weak fiscal discipline or rigid markets—can lead to significant costs later. Iceland can avoid that by front-loading reforms. Even if the decision is ultimately to retain the króna, these reforms are largely “no-regret” moves that will strengthen the economy.

**Annex VIII. Figure 5. Summary Table of Initial Conditions, Economic Structure and Shocks**

| Criteria                            | General Issue                                                                                                                                          | Iceland Characteristics                                                                                                                                                                                                       | Conclusion                                                                                                                                                                                                                                                              |
|-------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Inflation</b>                    | <i>The more domestic inflation deviates from trading partners, the greater the need for exchange rate adjustments</i>                                  | <ul style="list-style-type: none"> <li>Historically higher than EA.</li> <li>Not highly correlated (varies) with EA</li> <li>Both business cycle and inflation.</li> </ul>                                                    | <ul style="list-style-type: none"> <li>High, variable and out-of-sync inflation suggests benefits of flexible ER</li> <li>Policy credibility can be imported</li> <li>Mitigated by economic flexibility.</li> </ul>                                                     |
| <b>External shocks</b>              | <i>If there are large and more frequent foreign shocks, greater exchange rate flexibility is needed.</i>                                               | <ul style="list-style-type: none"> <li>Small open economy</li> <li>Relatively large TOT shocks</li> <li>Less diversified economy</li> </ul>                                                                                   | <ul style="list-style-type: none"> <li>Large shocks and less diversified economy suggest flexible ER</li> <li>Small open economy could suggest both</li> </ul>                                                                                                          |
| <b>Fiscal position/policy</b>       | <i>Fiscal policy would need to be sustainable and be able to act as counter-cyclical policy instrument</i>                                             | <ul style="list-style-type: none"> <li>Sustainable fiscal policy</li> <li>Fiscal rules in line with EU framework</li> <li>Ability to act as counter-cyclical tool</li> </ul>                                                  | <ul style="list-style-type: none"> <li>Conditions are in place but benefits of both regimes.</li> <li>The more out of sync the business cycle is, the more important this is.</li> </ul>                                                                                |
| <b>Trade/political integration</b>  | <i>The higher the extent of trade and political integration with partner countries, the stronger the case for a currency peg or a common currency.</i> | <ul style="list-style-type: none"> <li>High proportion of trade with the EU</li> <li>Regulatory integration through EEA</li> <li>National supervision/liquidity/capital markets</li> <li>Vulnerable to geopolitics</li> </ul> | <ul style="list-style-type: none"> <li>The large trade and political integration with the EU/EA suggest euro adoption.</li> <li>Membership of the banking union, ECB liquidity facilities, and capital markets union.</li> <li>Stronger geopolitical anchor.</li> </ul> |
| <b>Flexibility of labor markets</b> | <i>The less flexible the labor market, the stronger the case for a more flexible exchange rate.</i>                                                    | <ul style="list-style-type: none"> <li>Labor markets are relatively flexible</li> <li>High degree of collective wage bargaining</li> <li>History of above-productivity wage growth and elevated inflation</li> </ul>          | <ul style="list-style-type: none"> <li>Labor markets are sufficiently flexible</li> <li>Collective wage bargaining could work well within each regime.</li> <li>Wage growth aligned with productivity even more important under fixed exchange rate</li> </ul>          |
| <b>External balance</b>             | <i>Imbalances, if present, can have a variety of causes. Absent adequate policy measures, greater exchange rate flexibility is needed.</i>             | <ul style="list-style-type: none"> <li>No major misalignments (REER/CA)</li> <li>No FX balance sheet mismatches</li> <li>Large foreign assets in pension sector.</li> <li>Reserves are adequate.</li> </ul>                   | <ul style="list-style-type: none"> <li>Absence of FX balance sheet mismatches and exchange rate misalignments reduce the benefits of fixing the exchange rate.</li> <li>Euro adoption would reduce exchange rate risk related to pension fund FX assets.</li> </ul>     |

IMF, 2022, Technical Assistance Handbook, [Choice of Exchange Rate Arrangement](#), December 2022.

**Conditions mainly favor flexible exchange rate**

**Conditions in place but benefits of both regimes**

**Conditions mainly favor euro adoption**



# ICELAND

July 10, 2026

## STAFF REPORT FOR THE 2026 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

Prepared By

The European Department  
(in consultation with other departments)

### CONTENTS

FUND RELATIONS \_\_\_\_\_ 2

## FUND RELATIONS

(As of May 31, 2026)

Membership Status: Joined December 27, 1945

|                            |             |                       |
|----------------------------|-------------|-----------------------|
| General Resources Account: | SDR Million | Percent of Quota      |
| Quota                      | 321.80      | 100.00                |
| Fund holdings of currency  | 252.00      | 78.31                 |
| Reserve tranche position   | 69.80       | 21.69                 |
| SDR Department:            | SDR Million | Percent of Allocation |
| Net cumulative allocation  | 420.62      | 100.00                |
| Holdings                   | 430.73      | 102.41                |

Outstanding Purchases and Loans: None

Latest Financial Arrangements:

| Type     | Approval Date | Expiration Date | Amount Approved (SDR Million) | Amount Drawn (SDR Million) |
|----------|---------------|-----------------|-------------------------------|----------------------------|
| Stand-By | Nov. 19, 2008 | Aug. 31, 2011   | 1,400.00                      | 1,400.00                   |
| Stand-By | Mar. 22, 1962 | Mar. 21, 1963   | 1.63                          | 0.00                       |
| Stand-By | Feb. 16, 1961 | Dec. 31, 1961   | 1.63                          | 0.00                       |

Projected Payments to the Fund<sup>1</sup>

(SDR million; based on existing use of resources and present holdings of SDRs):

|                  | 2026 | 2027 | 2028 | 2029 | 2030 |
|------------------|------|------|------|------|------|
| Principal        | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Charges/Interest | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Total            | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |

Implementation of HIPC Initiative: Not applicable

Implementation of Multilateral Debt Relief Initiative (MDRI): Not applicable

Implementation of Catastrophe Containment and Relief (CCR): Not applicable

<sup>1</sup> When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

### Exchange Rate Arrangements:

The *de jure* exchange rate arrangement is free floating, and the *de facto* exchange rate arrangement under the IMF classification system is floating. The CBI publishes daily data on its foreign exchange intervention with a lag.

Iceland has accepted the obligations under Article VIII, Sections 2, 3, and 4 of the IMF's Articles of Agreement and maintains an exchange system free of multiple currency practices and restrictions on payments and transfers for current international transactions, with the exception of restrictions imposed for security reasons, which have been notified to the Fund in accordance with the Executive Board Decision No. 144-(52/51).

### Last Article IV Consultation:

Discussions for the 2025 Article IV Consultation were held during April 7–11 (virtually) and April 28–May 6, 2025 (in Reykjavik). The staff report (IMF Country Report No. 25/141 available at <https://www.imf.org/iceland>) was considered by the Executive Board on June 16, 2025. Article IV consultations with Iceland are currently held on a 12-month cycle.

### Financial Sector Assessment Program (FSAP) Participation and ROSC:

The Financial System Stability Assessment (FSSA) for the last financial stability assessment was discussed by the Board on June 23, 2023. The FSSA and accompanying Reports on the Observation of Standards and Codes (ROSCs) are available at <https://www.imf.org/iceland>.

### Technical Assistance:

| Department | Purpose                                                | Date          |
|------------|--------------------------------------------------------|---------------|
| MCM        | Capital account liberalization                         | March 2010    |
| MCM        | Reserves building and liquidity management             | June 2010     |
| MCM        | Public debt management                                 | July 2010     |
| FAD        | Fiscal framework issues                                | August 2010   |
| MCM        | Capital controls liberalization                        | November 2010 |
| MCM        | Converging to EU regulations-credit bureaus            | January 2011  |
| MCM        | Liquidity management                                   | March 2011    |
| FAD        | Tax policy                                             | March 2011    |
| STA        | External Sector Statistics                             | April 2011    |
| FAD        | Organic Budget Law                                     | October 2011  |
| FAD        | Follow up on Organic Budget Law                        | May 2012      |
| MCM        | Capital account liberalization                         | March 2013    |
| FAD        | IPSAS in Iceland: Towards Enhanced Fiscal Transparency | December 2013 |
| FAD        | VAT reform                                             | February 2014 |
| MCM        | Capital controls liberalization                        | May 2014      |
| MCM        | Banking supervision                                    | February 2015 |
| MCM        | Banking supervision                                    | March 2015    |

## ICELAND

|     |                                                        |                |
|-----|--------------------------------------------------------|----------------|
| MCM | Stress testing                                         | April 2015     |
| FAD | Distributional Effects of Tax Reforms and Expenditures | April 2015     |
| MCM | Banking supervision                                    | September 2015 |
| MCM | Banking supervision                                    | March 2016     |
| FAD | Organic Budget Law implementation                      | April 2016     |
| LEG | AML/CFT Risk-Based Supervision                         | 2025–27        |