

Iceland's Recovery—Taking Stock

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Where we are:

The IMF Stand-By Arrangement ended in August...

...but the recovery program still has a few years to run

Fiscal consolidation through 2014

Lifting capital controls

Agenda for strengthening institutions

Strong ownership by the authorities contributed to success...

...and bodes well for implementation going forward

Stabilization and adjustment—2 phases

1 Stabilize: emergency measures to soften the impact

- A: mobilize exceptional financing (IMF, Nordics, Poland)
- B: impose capital controls
- C: allow a large budget deficit (fiscal automatic stabilizer)
- D: monetary policy to support exchange rate stabilization

2 Adjust and unwind: normalization

- A: replace exceptional financing with normal finance
- B: lift capital controls
- C: close the budget deficit over several years
- D: new monetary policy framework

Outlook

Projected five-year averages (2011-15)

Growth	2-3 percent
Trade surplus	7-9 percent of GDP
Current account surplus	0-2 percent of GDP
Inflation	2.5 percent

...and levels by 2015

Unemployment	3-4 percent (8 today)
External debt	180 percent of GDP (330 today)
Government debt	70 percent of GDP (96 today)

...but there are downside risks (“challenges”)

Challenges ahead

BOP/exchange rate/capital control:

- replace and repay exceptional finance
- support the exchange rate
- build sufficient reserve cover
- while gradually eliminating capital controls
- against background of unfavorable international climate

Investment/growth/employment:

- Resumption of sustained growth
- in the face of household deleveraging
 - and fiscal consolidation
 - and an unfavorable global climate

Meeting the challenges

A: Consistent policy frameworks

Consistent medium term fiscal framework

- Medium term fiscal plan

- Local government finances

- Medium term debt and liquidity management strategy

Capital control liberalization framework with flexible pacing

- Pace will be set by balance of payments developments

Household and corporate debt restructuring framework

- Return to normality for households and corporations and banks

Well capitalized banks and tough supervision

Meeting the challenges

B: Sustainable macroeconomic balances lower macro risks

Fiscal

- Consolidation measures 10 percent so far.
- Gross debt ratio projected to decline from 96 in 2010 to 70 by 2015
- Net debt ratio from 69 to about 50
- Improved structure of debt—maturity and diversification

External

- Current account turnaround
- Gross debt projected to decline from 330 to 180 by 2015
- Net debt significantly lower
- Increasing reserve cover

Price and exchange rate stability