Fitch Ratings
KNOW YOUR RISK

Fitch Affirms Ratings of Icelandic Banks on Revision of Iceland's Outlook to Negative

23 Feb 2006 4:00 AM (EST)

Fitch Ratings-London-23 February 2006: Fitch Ratings today affirmed the ratings of four Icelandic banks as follows:

Kaupthing Bank ("KB"): Long-term 'A', Short-term 'F1', Individual 'B/C' and Support '2'
Landsbanki Islands ("LBK"): Long-term 'A', Short-term 'F1', Individual 'B/C' and Support '2'
Islandsbanki ("ISB"): Long-term 'A', Short-term 'F1', Individual 'B/C' and Support '2'
Straumur-Burdaras ("Straumur"): Long-term 'BBB-' (BBB minus), Short-term 'F3', Individual 'C/D' and Support '3'

The banks' rating Outlooks remain Stable despite the revision of Iceland's sovereign Outlook to Negative on 21 February 2006; Iceland's Long-term foreign currency Issuer Default Rating was affirmed at 'AA-' (AA minus).

Ratings assigned to KB, LBK and ISB in November 2005 and to Straumur in January 2006 take into account Iceland's macro-prudential risks, including rising inflation, rapid credit growth, buoyant asset prices, a steep current account deficit and escalating external indebtedness. For KB, LBK and ISB, these risks are offset to some extent by the banks' large capital bases, with Tier 1 ratios of 9.4%, 11.9% and 9.9% respectively at end-2005, and by the significant geographic diversification of their loan portfolios, with foreign lending representing between around 35% and 70% of the banks' loan books at end-2005.

Positions in foreign currencies are subject to strict limits from the Central bank of Iceland, and stress-tests indicate that the banks are well-equipped to absorb shocks on this front. Foreign currency lending to Icelandic corporates is significant, and could represent an indirect FX risk for the banks. An estimate 75% of the cash flows of Icelandic listed corporates are in foreign currencies and, according to banks' information, a limited proportion of the foreign currency borrowers are not hedged against FX risk; however, a track record still has to be built in this respect to ascertain the quality of the hedges by some foreign currency borrowers. Stress-tests by the banks on interest rate risk also indicate that the overall impact on the banks' capitalisation of a 100bps shift in interest rates would be relatively limited. Straumur only acquired its investment banking licence in January 2004 and its ratings reflect its less established position compared with its peers and a lower degree of diversification of its activities, despite a substantial capital base, with a Tier 1 ratio of around 35% as at January 2006.

Fitch will continue to monitor the evolution of the Icelandic macro-imbalances and the management of these risks by the banks.

Contact: Alexandre Birry, London, Tel: +44 207 862 4150; Alison Leveridge, +44 207 417

4305

Media Relations: Jon Laycock, London, Tel: +44 20 7417 4327.

Fitch's rating definitions and the terms of use of such ratings are available on the agency's public site, www.fitchratings.com. Published ratings, criteria and methodologies are available from this site, at all times. Fitch's code of conduct, confidentiality, conflicts of interest, affiliate firewall, compliance and other relevant policies and procedures are also available from the 'Code of Conduct' section of this site.

Copyright © 2006 by Fitch, Inc., Fitch Ratings Ltd. and its subsidiaries.