

## **Fitch Affirms Iceland's Kaupthing Bank at 'A'; Outlook Stable**

Fitch Ratings-London/Frankfurt-26 July 2007: Fitch Ratings has today affirmed Iceland's Kaupthing Bank's ("Kaupthing") ratings at Long-term Issuer Default ("IDR") 'A', Short-term IDR 'F1', Individual 'B/C' and Support '2'. The Outlook for the Long-term IDR is Stable. The Support Rating Floor was affirmed at 'BBB'.

The ratings of Kaupthing reflect its strong position in the Icelandic market, the improved diversification of its profits and assets, its good asset quality, its satisfactory capitalisation and underlying profitability. The ratings are also based on Kaupthing's exposure to the volatile Icelandic economy and the Nordic stock exchanges, the risks entailed by its rapid expansion and on its reliance on wholesale funding, which is gradually declining in light of the recent increase in customer deposits following the launch of several deposit-taking initiatives.

In 2006, Kaupthing took steps to strengthen its business and risk profile, including the reduction of its cross-shareholding with its main shareholder, the diversification of its assets and income streams, as well as its funding sources, the restructuring of its UK subsidiary, Kaupthing Singer & Friedlander, and the successful raising of fresh capital. Outside Iceland, the bank has now two strong lending platforms in the UK and in Denmark (through its subsidiary FIH Erhvervsbank), making it far less reliant on the Icelandic market than in the past. In addition, Kaupthing has been consolidating its positions in capital markets-driven activities in northern Europe, hiring teams in the investment banking and brokerage areas.

Recent performance has benefited from favourable capital markets and operating environment, leading to high business volumes and low credit costs. Retail and corporate banking should generate steady profits, in particular in the UK and the Nordic countries, where the economic outlook remains positive. Nevertheless, the strong focus on corporate and investment banking means that performance of the bank will, to some extent, remain reliant on developments in the capital markets. One of the key focuses of management is to increase cross-selling between the different divisions and markets to strengthen business flows and deliver satisfactory returns on the recent investments. "In Fitch's view, the bank's diversification and expansion strategy should help to offset the volatility of its domestic market and currency and also offset its strong focus on investment banking", says Olivia Perney Guillot, Senior Director at Fitch's Financial Institutions Group in Frankfurt.

In November 2006, Kaupthing successfully launched an ordinary share capital issue of ISK57bn (around EUR650m), reflecting the bank's growing focus on attracting foreign investors, a natural development in view of the internationalisation of its activities. Its good capital ratios are a pre-requisite given the bank's risk profile, the volatile situation experienced recently on the funding markets, and rapid expansion. The bank continues to invest in its corporate and investment banking franchise outside Iceland and remains open to acquisitions

Kaupthing is the largest bank in Iceland by equity and total assets, and one of the 10-largest banking groups in the Nordic region.

Fitch's credit analysis of Kaupthing can be found on the agency's website, [www.fitchratings.com](http://www.fitchratings.com).

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