Landsbanki Føroya
GOVERNMENTAL BANK

ECONOMIC ASSESSMENT

24. FEB 2010

ECONOMIC OUTLOOK 2010 AND 2011

CONTENTS

INTRODUCTION

In connection with the drawing of the Faroese Budget for 2011, the Faroese Governmental Bank (Landsbanki Føroya) has made an assessment of the economy and the economic outlook for the Faroese economy in 2009, 2010 and 2011. The report is as usual limited to an account of the economic trends as well as a projection of the key figures in the national accounts of 2009, 2010 and 2011 based on the economic model of the Governmental Bank.

The Governmental Bank of the Faroes issued its latest economic assessment in October 2009 and, due to the short period of time that has passed, the main conclusions will tend to be similar and the description of sectors and industry conditions will not have changed substantially. However, all economic indicators have been updated and the projection of GDP for 2009 and 2010 has been reassessed and updated. Furthermore, this assessment also contains the first GDP estimates for the year 2011.

The primary basis of the Governmental Bank's projection is the Faroese national accounts, managed by Statistics Faroe Islands (Hagstovan). The previous projections by the Governmental Bank were made on the basis of the final statement of national accounts for 2006, the preliminary statement for 2007, and the provisional statement for 2008 – which meant that the Governmental Bank projected GDP for 2009 and 2010. Other important key figures used in the economic analysis, e.g. the operations concerning the balance of payments, are not available for the years after 2006. Therefore, it is important to keep in mind that assessments of some particulars are uncertain as such.

The report starts with a general assessment of the Faroese economy, a global economic outlook, as well as a description of the key assumptions behind the economic projection of the Governmental Bank. Finally, the different sectors of the economy will be described, i.e. the business, financial and public sector, households, as well as the balance of payment. Appendices with figures corresponding to the description of the different sectors are to be found at the back of the report.

GENERAL ASSESSMENT

Similarly to what has happened globally, the Faroese economy experienced a downturn as the international financial crisis turned into an economic crisis in the fall of 2008 – directly affecting production in nearly all economies.

The Faroese economic situation

The financial crisis affected the Faroese financial sector directly as financing costs of Faroese banks increased considerably due to higher interest rates on borrowings from other financial institutions as well as expenses for bank bailouts. Overall, it seems as though the world of finance has weathered the storm and the worst winds have died down; yet, permanent changes are to be expected, such as stricter capital requirements in the financial sector.

The financial crisis – and subsequent economic crisis – also affected households, as they reduced consumption and increased their savings. This is a result of increasingly uncertain future outlooks, a drop in the value and equity of real properties and worse credit facilities for consumer loans and investments compared to previous years. This also affected the revenues of the Faroese Treasury, which experienced comparatively large budget deficits in 2008 and 2009 – and expectations are of similar budget deficits this year and in 2011.

In addition, a combination of external blows and structural difficulties have meant that industry production, in particular local production, has gone down dramatically these last 2-3 years and is now historically low. Fish prices are low and this puts a strain on operations, and while oil prices are lower than in 2008, they are still high compared to previous years. The conditions for growth in fish stocks in Faroese waters have been below average these past years. Structural problems such as excess industry capacity and too high fishing pressure on stocks surrounding the Faroe Islands, contribute to the fact that profitability in the domestic fishing industry is not at the same level as it could have been with lower fishing pressure and better fish stock management.

In general, the Faroese economy is quite sound. In 2006, the Faroe Islands had net assets abroad worth DKK 3.7 billion, according to Statistics Faroe Islands. Estimates in this economic assessment indicate that ever since there has been a surplus on the total balance of payments. Therefore one might conclude that the Faroese balance towards foreign countries is very acceptable. Faroese households seem to be quite well off in global comparison. By the end of 2008, the net liabilities of the Government, municipalities and social funds were in total modest (see figure F-49 and F-50 in the appendix). Financial institutions and households own the majority of the net assets in foreign countries.

Currently, one of the biggest challenges in the Faroese economy is in the administration of the country and municipalities, which are running large deficits, and the administration of the fishing industry, where companies are experiencing significant problems in operations, due to reduced catches, low selling prices and high oil prices.

Ensuring long-term economic growth could also be said to pose a challenge; partly on account of the fact that private sector investments have for many years only constituted a modest percentage of GDP (see figure F-6 in the appendix), but also because excess capacity in the fishing industry makes it hard to turn a profit and to ensure future industry growth.

Global outlook

A small economy like the Faroese, where imports and exports constitute a large part of the economy, is very much affected by global economic trends and especially developments in those countries with which we trade goods and services. The Faroese economy is particularly affected by external developments when it comes to the price of imported goods and exported products, but also the households and their tendency to spend and save are affected by the foreign economic trends. Global economic trends will therefore be significant in determining when productivity again will increase in the Faroese economy.

Following the downturn from around mid 2007 to mid 2009 – with a real reduction in the global economy of 1 percent in 2009 – estimates from acclaimed international organizations point to the fact that most economies should soon start to experience economic growth. Total growth for 2010 and 2011 is expected to be app. 4 percent[1], in real terms.

Recent projections by the OECD indicate that the lost grounds in terms of growth, however, will at the earliest be regained in 2013. For the OECD member countries the reduction was in real terms 4 percent. Growth is furthermore expected to be relatively low in 2010 and 2011. Estimates by other international organizations indicate that it will take years before the global economy reached its previous levels. Yet, estimates differ on how long this will take. Table 2 shows the latest economic growth outlook from the IMF.

Real GDP-growth, 2008-2011				TABLE 1
	2008	2009	2010	2011
World Economy	3,0	-0,8	3,9	4,3
USA	0,4	-2,5	2,7	2,4
Germany	1,2	-4,8	1,5	1,9
Great britain	0,5	-4,8	1,3	2,7
The Euro-zone	0,6	-3,9	1,0	1,6

Comment: 2009 og 2010 are IMF forecasts
Source: IMF World Economic Outlook Update, July 8, 2009

The table points to a growth in the global economy as a whole, primarily driven by growth in Asia and, in addition, the massive stimulation of the US economy seems to have had an effect.

Loan-funded spending, which was very apparent before the crisis, has all but disappeared – also in the Faroes – and people are now starting to save up. It is especially countries where property prices dropped and, consequently, equity was reduced that have experience an increase in savings and decrease in private consumption. Seeing as private consumption has a great effect on the overall economy, this may imply lower economic growth over the next couple of years. Several governments have made efforts to boost demand for goods and services by increasing government spending with different stimulus packages. These measures are time limited and it is not clear what effect a drop in public expenditure will have on economic developments.

[1] Source: IMF World Economic Outlook Update, January 26, 2010

ECONOMIC OUTLOOK

The projections of the Governmental Bank

There are indications of a fall in GDP in current prices by app. 3 percent in 2009, and the Governmental Bank's projections point to an increase of app. 3 percent in 2010. If prices increase by 2 percent, it would mean that the Faroese economy in grew in real terms, albeit a small growth. Thus, the economic downturn seems to have passed its peak and while indicators point in different directions2, our estimate is that we will see economic growth already this years.

Governmental Bank Forecast of GDP and wages for 2009, 2010 and 2011 FIG. 1

Source: Governmental Bank

Private consumption, which grew considerably from 2004 to 2007, was unusually high in 2007 and by autumn the same year it was slowing down, i.e. before the global financial crisis was full blown. Since then consumption has dropped significantly and rapidly. Imports for direct household consumption fell significantly in 2009 and consumption relative to disposable income has probably not been this low since 1998, i.e. a time when the effects of the Faroese economic crisis of the 1990ies were still being felt. It is difficult to estimate whether consumption has reached its lowest level under the current economic conditions. However, according to the Governmental Bank's assessment it is not likely that consumption will go further down. Surveys concerning people's economic outlooks for 2010 show that the households now are less pessimistic than they were 6 months ago and key indicators point in the same direction, e.g. the VAT-revenue to wage-payments ratio (cf. graph 3). Consumption is expected to increase on aggregate in 2010 and 2011.

Key economic indicators TABLE 2

Annual nominel growth	2003	2004	2005	2006	2007	2008	2009	2010	2011
GDP	-2,2	3,2	3,0	12,9	5,7	0,5	-1,9	3,4	3,8
Private consumption	4,1	8,1	9,1	9,5	10,2	-8,4	-8,5	3,9	4
Public consumption	5,4	6,2	5,2	3,6	8,2	10,8	1,5	3,1	1,4
Private Investment	61,8	-62,4	68,8	-2,7	2,1	-17,8	-23,7	10,8	17,6
Public Investment	1,9	16,5	-7,7	15,5	12,7	7,2	-0,8	1,4	2,5
Exports	-6,8	-4,3	4,6	12,0	4,3	5,6	-6,0	2,0	4,0

Source: Governmental Bank

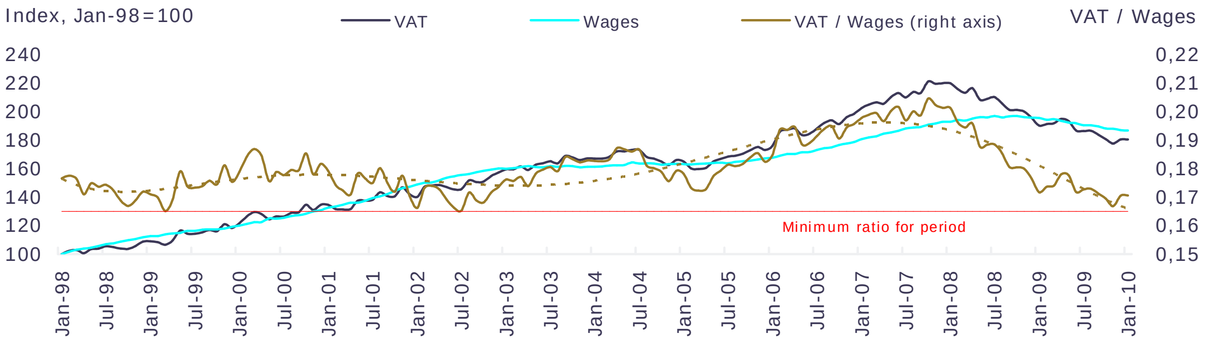
Public consumption is easier to estimate, especially since the Faroese Budget bill for 2010 was presented and municipal budgets have been set. It seems widely accepted that the expenditure limit must be kept and based on known government and municipal plans, public consumption is estimated to increase app. 3 percent in 2010 – of which, the government increases consumption by 4 percent and the municipalities by 1 percent. The assumptions used in the projections for 2011 put the growth in total public consumption at 1.5 percent.

[2] Please refer to the section "Economic developments and the projections of the Governmental Bank"

Private investments have fluctuated quite significantly during the past years and are more difficult to predict. Access to financing, the interest rate level and the bleak economic outlook of businesses influences the willingness of private companies to invest. It is estimated that private investments decreased significantly in both 2008 and 2009, but an increase is expected in 2010 and 2011.

Public investments decreased by app. 1 percent in 2009 and will grow between 1 percent and 2 percent in 2010 – municipalities seem to invest less, while the government increases its investments. The growth in total public investments is expected to be app. 2.5 percent in 2011.

Wages and VAT-revenues, Jan-98 to Jan-10 FIG. 2



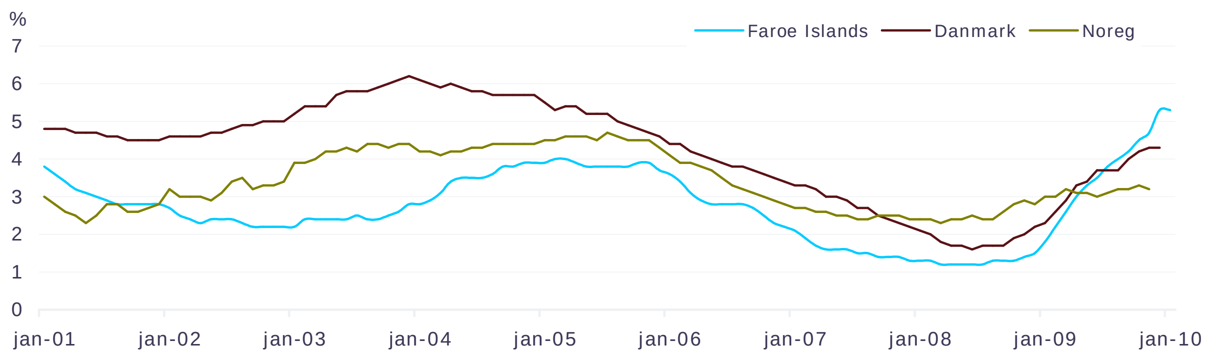
Source: Statistics Faroe Islands and TAKS

Total exports of goods and services fell by 6 percent in 2009[3] and while it is difficult to assess exports in general, export value is not expected to decrease further given current outlooks. Exports are expected to increase by 2 per cent in 2010 and 4 percent in 2011.

Economic developments and the projectioins og the Governmental bank

Payment of wages, which with some reservations can be interpreted as a measure for the overall productivity in the economy, have been on the decline since February 2009, as measured in continuous annual sums. The latest figures are from January this year and show an annual change of -4.5 percent. Apart for certain minor industries only public services and the fish farming industry experienced an increase in wage payments.

Seasonally adjusted unemployment as % of workforce, Jan-98 to Jan-10 FIG. 3



Source: Faroese Statistics and OECD

The unemployment rate has continued to rise during 2009 and at the end of January 2010 was measured at 5.6 percent[4]. With a 3 per cent growth in GDP in current prices and perhaps a 1 per

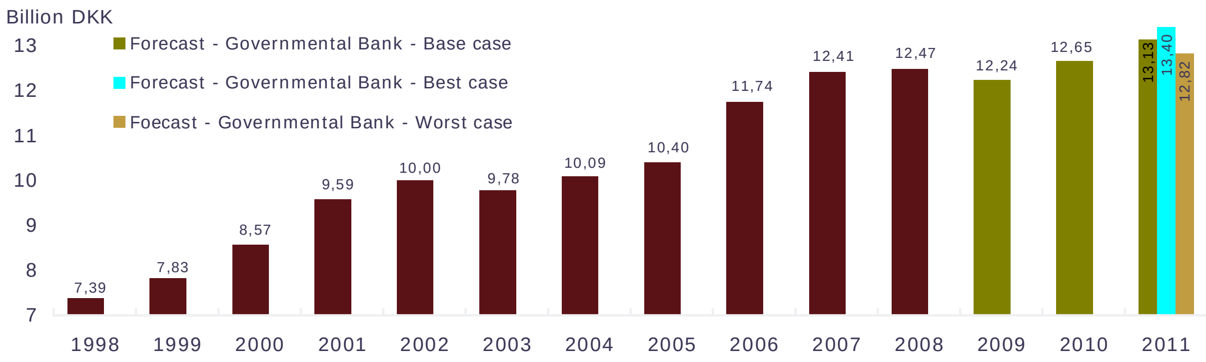
[3] No public accounts trace the development in exports in services after the 2006. Therefore, the projection of the Governmental Bank are comparatively uncertain with regards this issue.

cent growth in real terms, it is not unlikely to see certain reluctance from companies at hiring people. Therefore, the unemployment rate may increase further to app. 6-7 percent on average in 2010.

Increases in unemployment can be traced in most sectors, excluding the fish farming industry, the financial sector and the public sector. Following changes to legislation in 2009, the Faroese Employment Office (ALS) has significantly increased the size of all grants to unemployed persons. This may well be keeping emigration down, coupled with the fact that neighbouring country are also experiencing rising unemployment, and therefore may also contribute to a slightly higher rate of unemployment. On the other hand, the increases in unemployment benefits should mean that the reduction in the level of income due to unemployment should be less. Less emigration, which increases the number of persons in the system, and the higher individual grant rates both act in ways as to counter the reduction in consumption.

In our view the main reasons for the increase in domestic demand is the sizeable Treasury deficit, coupled with positive developments in the fish farming industry and improved outlooks in the fishing industry. The Governmental Bank expects that the increase in unemployment benefits will cause households to stop reducing their spending and possibly induce household to increase demand. These circumstances should to a degree hold back further growth in unemployment. This has also contributed to the Governmental Bank's estimates for 2010 of an average yearly unemployment rate of app. 6-7 percent, which is a bit than in 2009.

Faroese GDP 1998 - 2011, current prices FIG. 4



Source: Statistics Faroe Islands (1998 - 2008) and the Governmental Bank (2009 - 2011)

[4] The Faroese Employment Office informs that the processing time for granting persons unemployment benefits has gone up, therefore, these latest figures on unemployment may be underestimated by 1 to 2 percent.

THE DIFFERENT SECTORS IN THE ECONOMY

This section of the report will deal with the different sectors in the economy, which are important to the overall developments and future prospects.

The public sector

The Central Government

Up to 2008 the Faroese Government has had a stimulating effect on the economy by means of tax reductions and of a significant rise in public spending, even during the times of economic growth. The enormous increase in public revenue expenditure in 2008 has meant that the Government has directly stimulated business activity in 2008 and has counteracted a decline in business activity.

In 2009, the activities of the government were less stimulating, due to the fact that public revenue expenditures (especially the purchase of goods and services) are reduced in the 2009 Budget compared to the 2008 accounts, while the deficit increases, due to declining revenues.

In 2010 the Treasury's deficit is expected to be just below DKK 800 million. This can also be traced in the total growth of the economy, which is considerably stimulated by the deficit. The budget deficits in 2008 and 2009 were on average DKK 650 million. Particularly revenues from VAT and other charges have declined substantially since 2007.

Public pay-roll expenses have increased in 2009 and 2010 and this growth in expenses is greater than the increase in tax revenues; despite cuts in income tax and taxes on capital gains.

In the draft Budget for 2010, the Faroese Government envisions a deficit of DKK 778 million. Public revenue expenditure for institutions will increase by app. 1 per cent, likewise grants for households, and investments will increase a little bit more, while revenues will decrease.

The municipalities

There are bound to be differences in the municipalities' abilities to meet their operational and investments objectives in the years to come. Tórshavn municipality will probably not be hit hard by the reduction in tax receipts, while other municipalities might experience a reduced tax base. Tórshavn municipality is not burdened by debt in the same way as other municipalities and is therefore in a position to initiate a number of large projects, which may have a stimulating effect on the economy.

According to preliminary figures from the budgets, the municipalities' net expenditures (revenue and investment expenditures minus all the non-tax receipts) will be app. DKK 1,370 million and tax receipts will be app. DKK 1,280 million in 2009.

The municipalities combined have most likely had a slight curbing to almost neutral influence on the economic trends in 2010 and possibly even more curbing in 2011. This is particularly true when Tórshavn municipality is left out. The financial situation in the majority of municipalities more or less forces them to tighten expenditures in order to lessen the deficit.

In these past few years, the municipalities have increased their revenue and investment expenditures, while they now reduce investments during the current recession.

Due to the different financial situations and debt burdens of the municipalities, it is a great challenge to create regulations, which will consider both the Government's overall needs as well as the needs of the individual municipalities.

The social funds

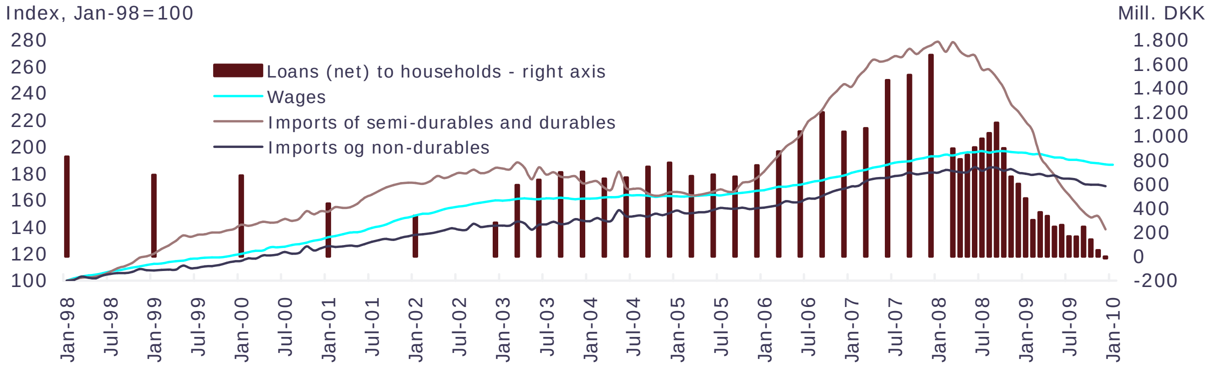
The social funds, the Faroese Employment Office (ALS) and the Faroese Labour Market Supplemental Pension Fund (AMEG), will be able to stick to their planned activities in 2010 and 2011. Especially ALS will most likely be able to stimulate the economy during the next two years. The ALS fund is in good condition to deal with the surge in unemployment. Yet, substantial changes have happened within a short period of time, and therefore it is difficult to offer any further indications or estimates of the condition of ALS, other than estimates of expected pay-out in the coming years.

Based on the amendments to the act concerning unemployment insurance and employment services, it is expected that ALS will increase their benefit pay-outs. Payments amounted to app. DKK 155 million in 2009. Outgoing payments are expected to reach app. DKK 250 million in 2010, which is about twice the size of ingoing payments. This will strengthen the spending power of the unemployed and at the same time lessen the fear of becoming unemployed. This will probably influence households so that they increase their savings to a lesser degree than they otherwise would.

The households

Different factors have had a negative impact on households in 2008 and 2009. Real property prices peaked in the autumn of 2007 and have dropped since then, see figure F-66 in the appendix. Together with increased borrowings, the fall in prices resulted in a drop in equity of app. DKK 4 billion or 20 per cent, although equity is still comparatively high. Shares owned by the Faroese people, of which households most likely own a small part, have depreciated by a total of 68 percent in market value (app. DKK 4 billion) during the same period of time. Uncertainties concerning the global economic outlook and our own fishing industry are still many. Moreover, the financial institutions have become more cautious in increasing lending operations.

Loans (net), wages and household consumption, Jan-98 to Jan-10 FIG. 5



Comment: Staistics from Mar-08 and onwards are from new records; therefore, there is a break in the series
Source: Governmental Bank and Statistics Faroe Islands

All these factors combined make it possible to understand why the households have become more cautious and reduced their spending as well as increased their savings. All these negative factors will hardly be permanent. Property prices will hardly improve any time soon, yet the equity is still excellent. Many of the Faroese listed businesses are financially sound, in spite of the low market value. There are indications that the market value again might increase a bit.

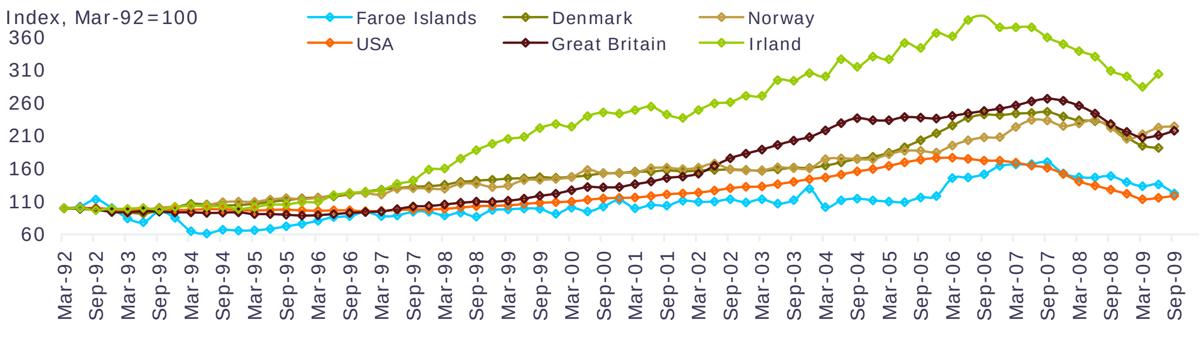
As seen in the VAT/wages ratio in figure F-61, the households have lowered their spending from the autumn of 2007 to the summer of 2009. What also can be seen is that the decline in consumer spending corresponds to the increase from 2005 to 2007. According to the developments in figure 5 households have decreased their consumption of both durable and semi-durable consumer goods in 2008 and 2009, while at the same time reducing net borrowing. The development in non-durable consumer goods seems to follow developments in earnings. As seen in figure F-37 in the appendix, borrowing has come to a standstill since October 2008, while deposits in banks made by the households have increased. This indicates that it is the households themselves that have taken initiatives towards lowering spending, rather than it being the lack of access to financing, which has prevented a growth in spending.

Surveys concerning public expectations made by The Faroese Ministry of Finance are shown in figures F-78 to F-82 in the appendix. Developments in household expectations correspond well to the developments in spending, as shown above. Therefore it is not meaningless to stress that pessimistic outlook of households seems to lessen in the recent surveys.

In global comparison, Faroese households are generally doing quite well. Property values appreciated significantly from 2005 to 2007 and later decreased in value. This does not seem have to been as overestimated as in other countries (see figure 8) and thus do not seem to be in further need of decreasing. Household debt is far less on the Faroe Islands (75 per cent of GDP) than e.g. in Denmark (111 per cent of GDP).

In conclusion, there is some reason to believe that households will be content with a level of consumption, which is no lower than the current level.

Real house prices in different countries FIG. 6



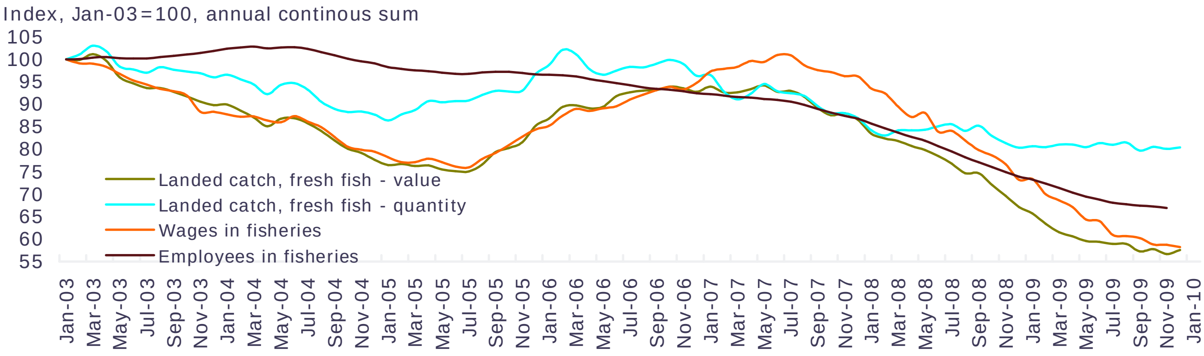
Source: Faroese Statistics, Eik Bank, OECD, Standard & Poor's, Central Statistics Office Ireland, Statistisk Sentralbyrå, Danmarks Statistik

The resource industries

The resource industries are categorized into four subgroups, which all operate under different conditions at different times. The subgroups are: demersal fishing in Faroese waters, demersal fishing in distant fishing grounds, pelagic fishing and fish farming.

Two of these groups – demersal fishing in Faroese waters and pelagic fishing – are currently in difficulties, because of outside blows and due to situations of a more structural nature. On the other hand, demersal fishing in distant fishing grounds and fish farming are currently making good and steady contributions to the Faroese economy.

Trends in fisheries, Jan-03 to Feb-09 FIG. 7



Source: Faroese Statistics

Demersal fishing in Faroese waters

The operations of the long line fishing fleet, door trawlers and pair trawlers fishing off the Faroe Islands are currently burdened by low fish prices coupled with poor catches, while in the preceding years it was especially high energy costs and poor catches that affected the operations.

Figure 9 shows that the catches have declined for many years, both in terms of quantity and value. There seem to be indication of a small change in conditions. It is still to early to assess the effects this could have, but on the whole prospects seem to be positive for the demersal fishing in Faroese waters. At the very least, prospects have now improved slightly.

Demersal fishing in distant fishing grounds

Currently, this part of the fishing industry, as indicated above, contributes to the Faroese economy consistently and well. According to ICES, fishing for cod and haddock in the Barents Sea seems to be at a sustainable level and outlooks are continuous for the future. Production is expected to improve in 2010 compared with the two preceding years. Low fish prices have burdened operations for one or two years, while on the other hand, oil prices have decreased and improved profitability. There are signs indicating that fish prices are on the rise again, although the increase is from a low level.

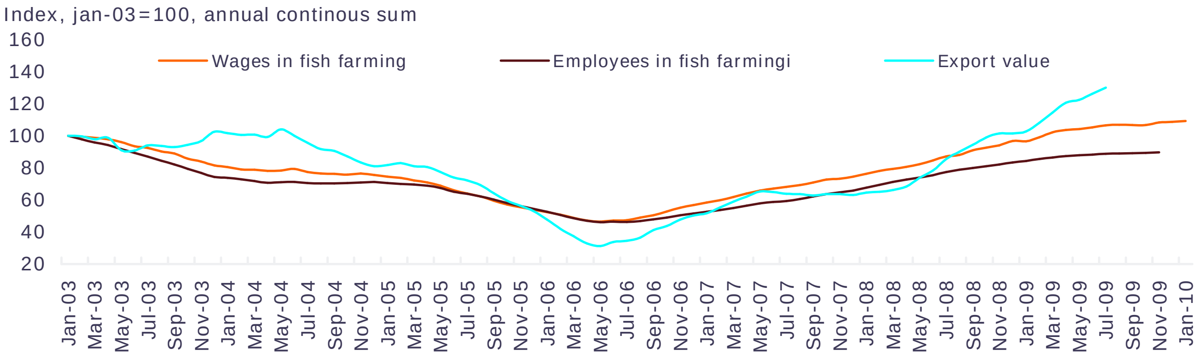
Pelagic fishing

Pelagic fish production has decreased significantly, especially due to the fact that the blue whiting quota was heavily reduced in 2009 and was set to decrease by 8.5 percent in 2010 according to the new fisheries agreement between the coastal states. Another difficulty facing the pelagic fishing industry is of a structural kind – as many years of excessive fishing has depleted the blue whiting stock to such an extent that it became necessary to slash quotas dramatically in order to protect the stocks.

Management of pelagic fish stocks can be somewhat difficult, due to the migratory nature of the stocks. This makes it difficult for countries to agree about a joint and enforceable fisheries policy over a longer period. Thus, the combined efforts of the involved countries means that fishing often is too intense compared to scientific advice.

The blue whiting quota was heavily reduced in 2009 (by 53 per cent) and a further 8.5 percent in 2010. In contrast, the quotas for Northerly Sea herring and mackerel increased by respectively 8 and 33 percent in 2009, and maybe it will be possible to add more value to these resources in the future. The capelin is an important part of pelagic fishing, however, it is difficult to say anything for certain about outlooks and stock volume is also expected to fluctuate.

Indicators for fish farming, Jan-03 to Jan-10 FIG. 8



Source: Faroese Statistics

The fish farming industry

The positive trends in the fish farming industry continue and, at the very least, we can conclude that since the summer of 2006 developments have only gone one way. The value of exports, in particular, has gone up and this reinforces the perception that the industry is close to reaching maximum capacity levels. Further growth may be difficult to ensure, yet, at the same time it is the fish farming industry that is driving Faroese economic growth in 2010 and 2011. Outlooks for the fish farming industry are on the whole quite good, particularly with regards to price as supply of salmon is on the decline – due to the state of the Chilean industry.

Harvests of farmed fish will go down slightly in 2010 compared with 2009. The reduction in quantity is app. 20 percent and export value is not expected to increase in 2010. Harvesting is likely to rise again in 2011 and 2012 as is the value of exports. Efforts have been directed at increasing production and tests made to see whether capacity can be expanded, e.g. through farming in less sheltered areas. This could potentially expand industry capacity, yet it is far from certain, given the current levels of knowledge.

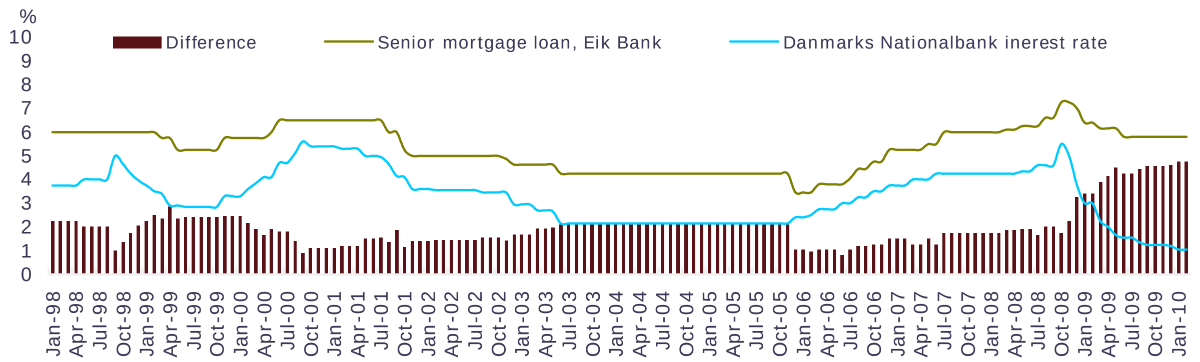
Summing up the resource industries

On the whole there are signs that, at best, production will stay at current level or go slightly up during the next year or two, compared with 2008 and 2009. Low fish prices are currently burdening operations and it remains unclear how long they will stay this low. Oil prices are still lower on average than in 2008, but have increased this year. Currently, it remains uncertain whether they will increase much further or start to decrease again.

The financial sector

Interest rate levels have of lately been record low in our neighbouring countries. Central banks around the world have cut short-term interest rates considerably and so far there has been no sign of an increase in 2010. Lending rates of Faroese banks have been somewhat higher than what we find on comparable loans in e.g. Denmark. This has had such an effect that the majority of the Faroese home loans are now mortgage financed. This sort of financial arrangement ensures a profit to the Faroese banks through administrative charges and improves liquidity, which can be used to pay off debt to other banks. The Danish Government's *Bank Packages* have reduced uncertainties and improved the position of Faroese banks. The banks currently have a net debt of DKK 4.1 bn to foreign financial institutions. Refinancing the debt is not expected to be difficult the first coming years, partly because of the banks' ability to obtain state warrants through the *Bank Packages*.

Interest rate margin on mortgage loans in FO and DNB`s interest rate FIG. 9



Source: Eik Bank and Danmarks Nationalbank

The size of the accounts the Faroese banks has been nearly unchanged in total from March 2008 to December 2009, as seen in e.g. F-39 in the appendix. Also observable is the fact that lending operations have decreased by app. DKK 1 billion, while bonds and other assets have increased by DKK 2 billion. On the liabilities side, deposits have increased by DKK 500 million, issued debt instruments have increased by DKK 2.5 billion and debt to foreign financial institutions has decreased by DKK 1.7 billion. Bank lending has decreased, on account of home loans being refinanced to mortgage loans.

Therefore, it seems that access to financing might not be any obstacle in financing the investments and operations of the business sector and households in the next couple of years.

Other industries

These are manufacturing and service industries, which are not mentioned above, but they combined account for a large part of the total added value in the Faroese economy.

The fish processing industry

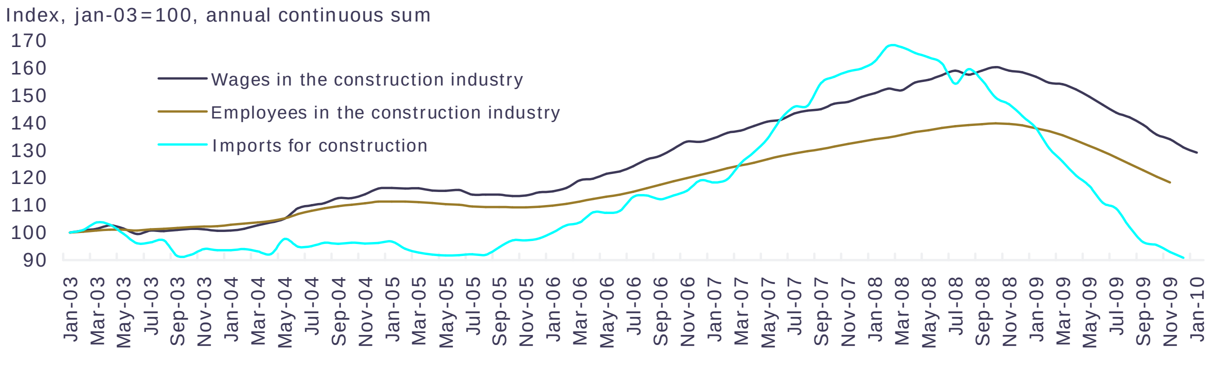
Changes have recently taken place in the fish processing industry and the number of processing plants has been reduced in order to boost the profitability of operations. There seems to be a great deal of uncertainty with regards to this sector of industry, as both access to financing and the difficulties in sequring raw materials for production still appears to limit production – although condition seem to have improved compared to last year.

In general, it is quite difficult to make estimates for the remainder of 2010 and 2011; however, indications are that a restructuring of production should be beneficial in the long run.

The construction industry

Not much has changed in the construction industry since the previous Economic Assessment. Expectations are roughly similar and the dramatic changes in conditions, compared with previous years, are still being felt. The levels of public investments in projects will to a great degree determine development in the building industry. Several projects have already been announced, e.g. the extension of the air strip at Vágar Airport, and Tórshavn municipality also plans to initiate a number of large construction projects.

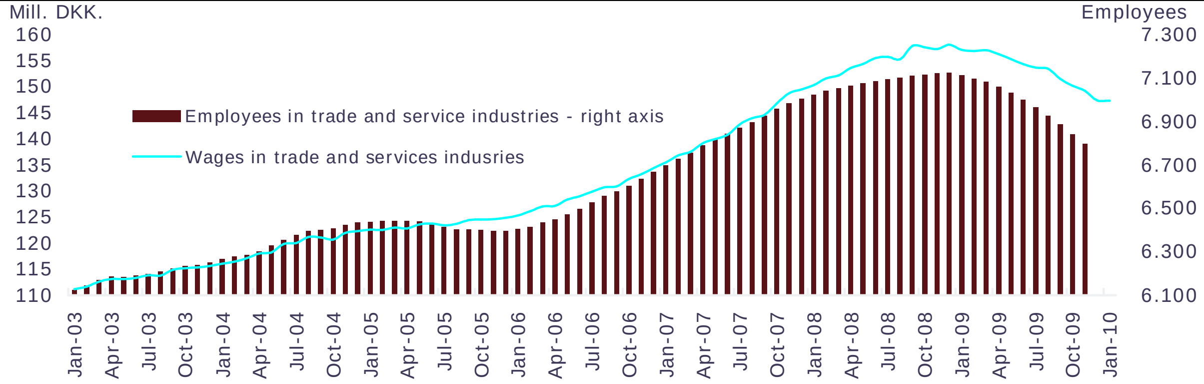
Trend developments in construction, Jan-03 to Jan-10 FIG. 10



Source: Faroese Statistics

The project management has not been satisfactory in the construction industry in recent years. So much work has been available that smaller businesses have taken upon themselves large projects. This has resulted in poor administration and low efficiency in the industry. The efficiency in the industry might improve in the years ahead, if construction companies increase in size and develop the necessary managerial skills. A consolidation is expected in the industry, as competition from foreign construction companies continues to increase.

Trend developments in trade and service industries, Jan-03 to Jan-10 FIG. 11



Source: Faroese Statistics

Trade and service industries

The reductions in private consumption have had a significant effect on the trade and service industries. Consumption fell dramatically in 2008 and 2009, following years of very high levels, and this still affects the industries. Indications are that inventories will not be reduced further and investments might go up slightly, however, not to the same levels as a few years ago.

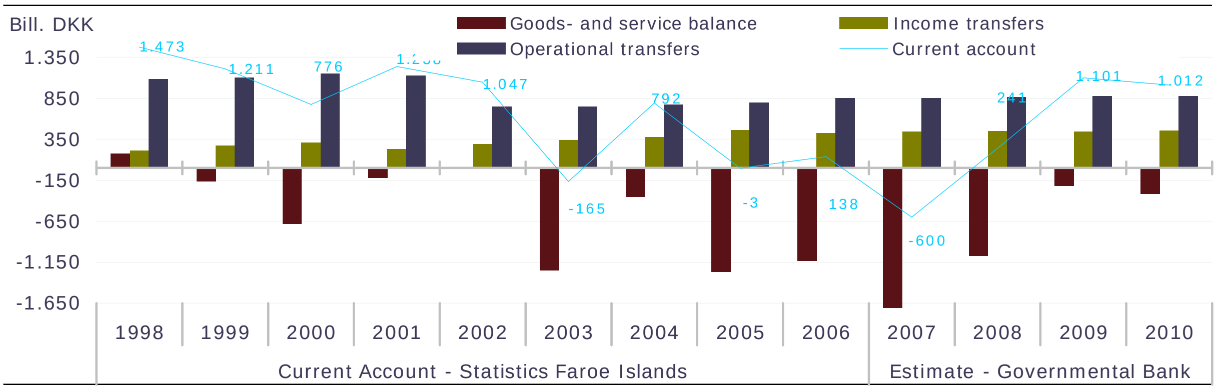
The trade barometer made by the Ministry of Finance indicates that prospects are not as dim as they were earlier. This supports the general assessment that the economy as a whole is at a turning point.

The balance of payments

The balance of payments includes the balance of trade, trade of services and transfers to and from abroad. The uncertainty is considerable regarding the statistics about the Faroese balance of payments, and the newest statement is from 2006. The figures are therefore to be read with some reservations.

According to the statements from Statistics Faroe Islands, the surplus on the balance of payments was on average substantial in the years 1998 to 2006, see Figure 12. The figures for 2003 and 2005 are greatly affected by the fact that two large ships were imported those two years, while 2006 is influenced by the fact that credit-funded spending really accelerated that year. There was a huge increase in imported goods, both durable and semi-durable consumer goods, and in materials for the construction industry that same year, which resulted in a large deficit on the balance of paymentsUmframt handilsjavnan fevnir gjaldsjavnin um handil av tænastum og um flytingar til og frá útlandinum. Óvissan er stór í hagtølunum um føroyska gjaldsjavnan, og eingin uppgerð er nýggjari enn fyri 2006. Tølini skulu tí lesast við ávísum fyrivarni.

Balance of payments 1998-2010 FIG. 12



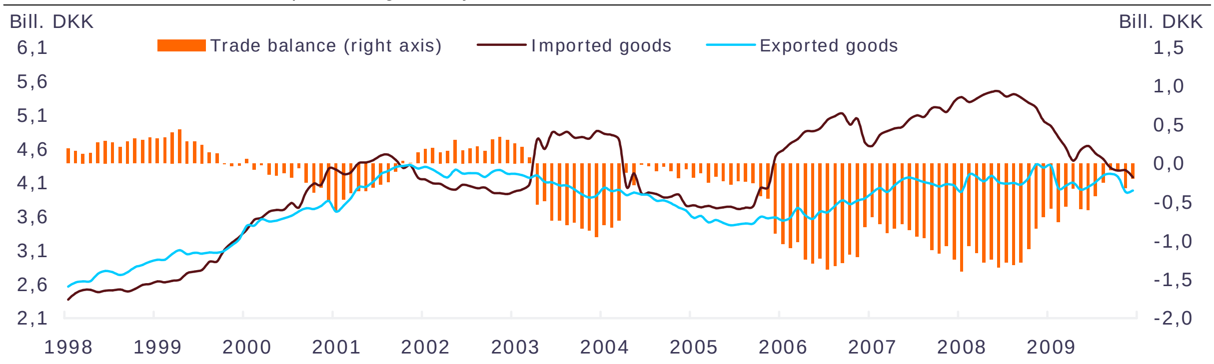
Source: Faroese Statistics (1998-2006) and the Governmental Bank (2007-2010)

Judging by the balance of trade, the deficit on the balance of payments in 2007 was most likely at the same level or higher than the deficit in 2003. In 2007, the deficit on the balance of trade reached DKK 1.5 billion, which is the largest ever recorded on the Faroe Islands. The deficit on the balance of trade was app. DKK 700 million in 2008. The surplus on the 2008 balance of payments was most likely at the same level as it was in 2006. The surplus in 2009 will probably be a bit higher, judging by the development in imports and exports, seeing as imports has decreased more than exports, see figure 6.

The surplus in 2010 is slightly lower, but the different is only minor. Trade in goods and services is nearly in balance, but has in total risen slightly compared to 2009. Developments have been quite extraordinary with regards to the balance of trade in goods and services, particularly since 2007. This is partly due to the presence of imports of large ships in certain years; however, private sector imports have also declined substantially in the last two years – and figures indicate that this reduction is sustained. It is, nonetheless, not likely that this will be the level for a longer period of time.

In other words, judging by the statistics, there is a surplus on the balance of payments, even though the public sector is currently experiencing huge deficits. Given that the statistics on the balance of payment are reliable, it means that the private sector combined, i.e. the industries and households, has huge surpluses and is increasing its savings significantly. The Governmental Bank has, in spite of great uncertainties, put figures on the trade operations of the balance of payments for the years 2007 to 2010, cf. figure 12.

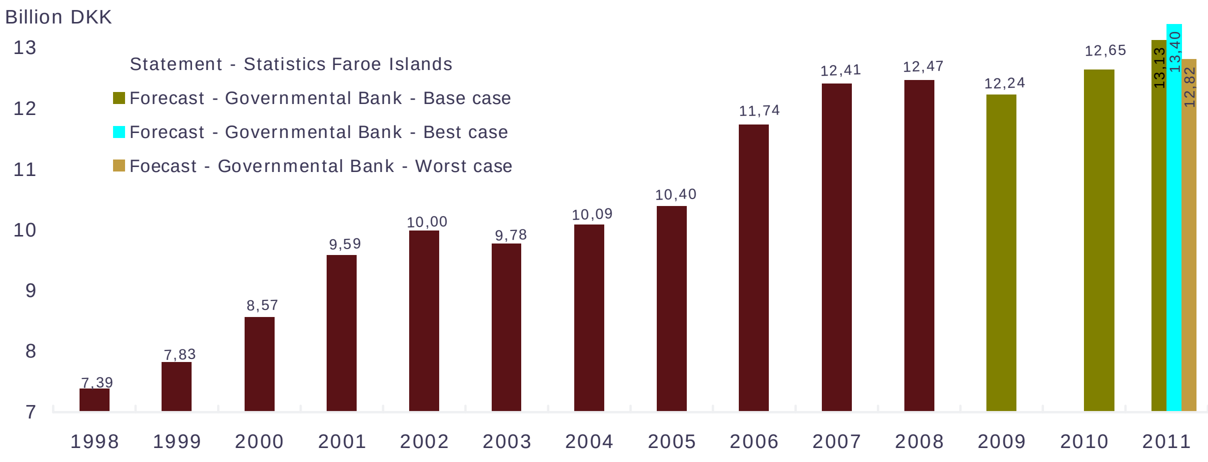
Trade balance: In- and exports of goods, jan-98 to dec-09 FIG. 13



Comment: Inports and exports are based on a 12 month moving average
Source: Statistics Faroe Islands

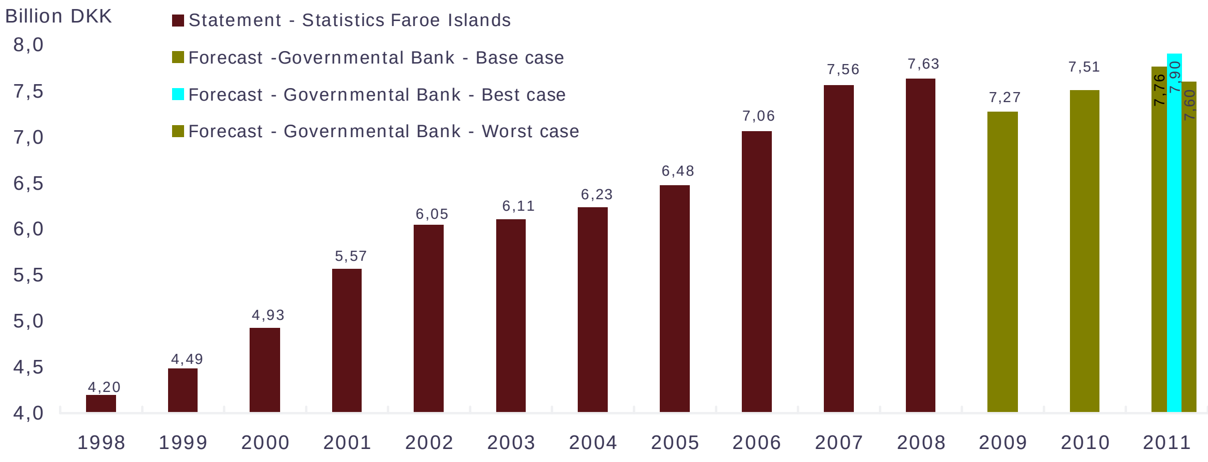
Appendix 1: GDP and other indicators

Faroese GDP 1998 - 2011, current prices F-1



Source: Statistics Faroe Islands (1998 - 2008) and the Governmental Bank (2009 - 2011)

Wages and associated payments, 1998 - 2011 F-2

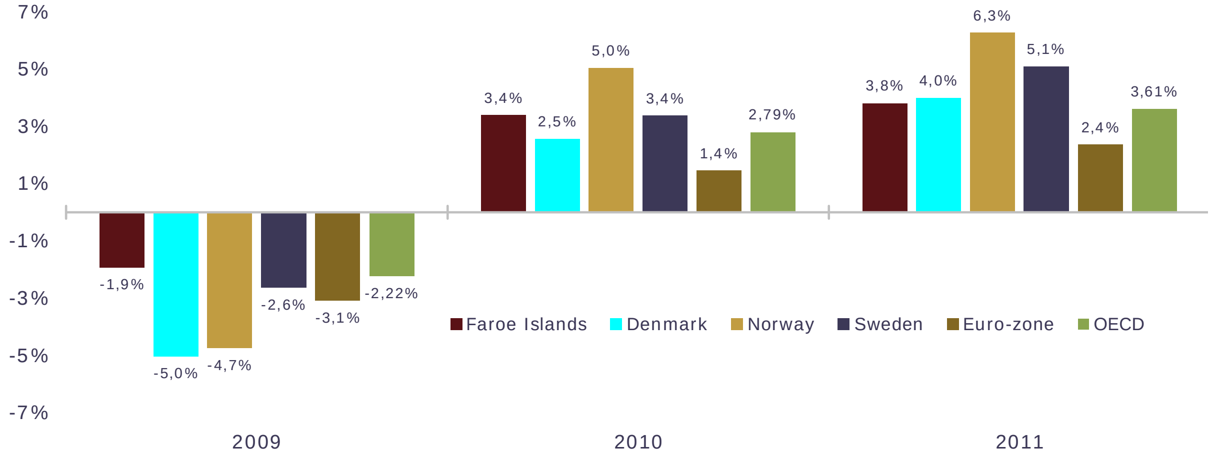


Source: Statistics Faroe Islands (1998 - 2008) and the Governmental Bank (2009 - 2011)

Governmental Bank Forecast of GDP and wages for 2009, 2010 and 2011 F-3

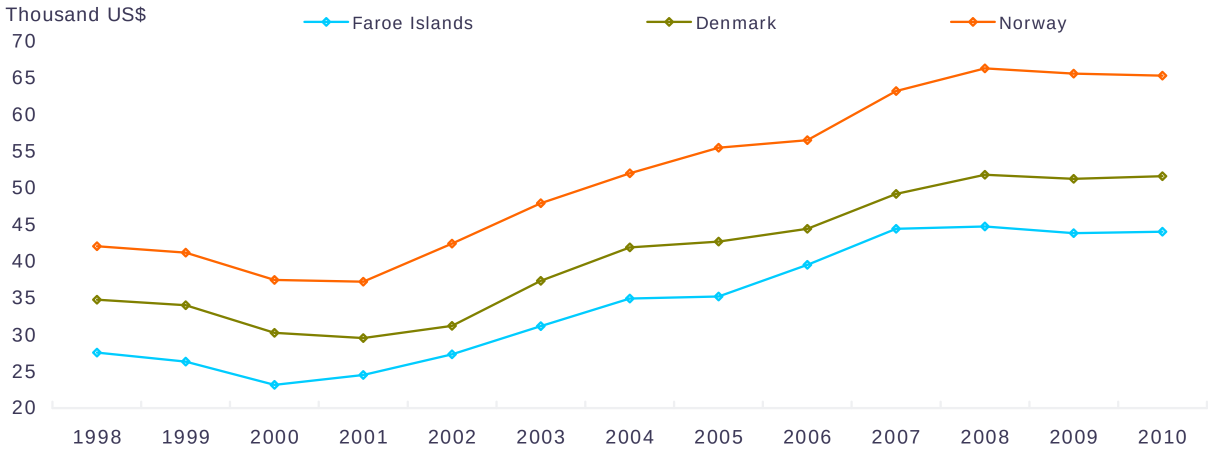
Source: Governmental Bank

GDP forecsts for selected countries/regions, 2009, 2010 and 2011 F-4



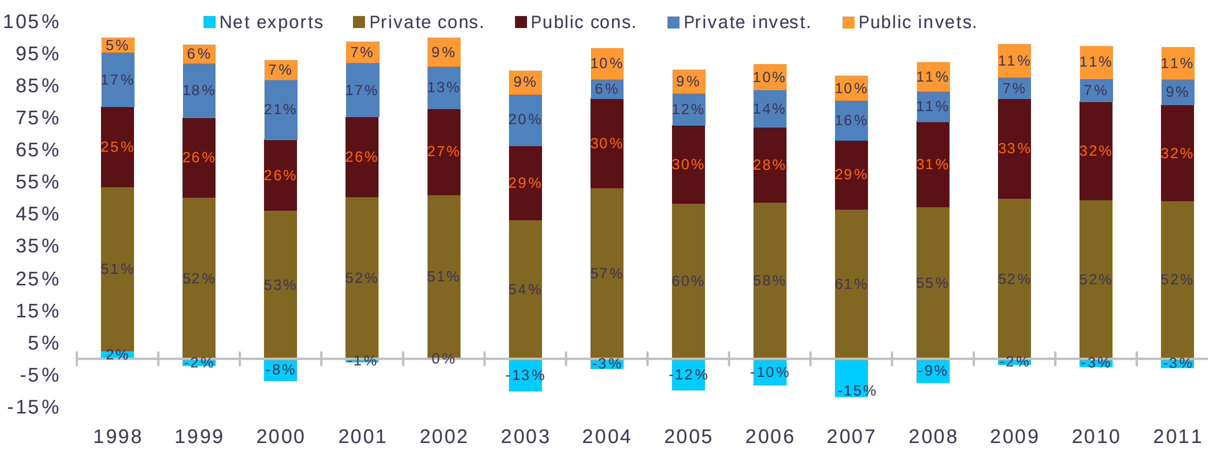
Source: Governmental Bank and OECD

GDP in fixed (2000) prices pr. capita in US$, 1998 - 2010 F-5



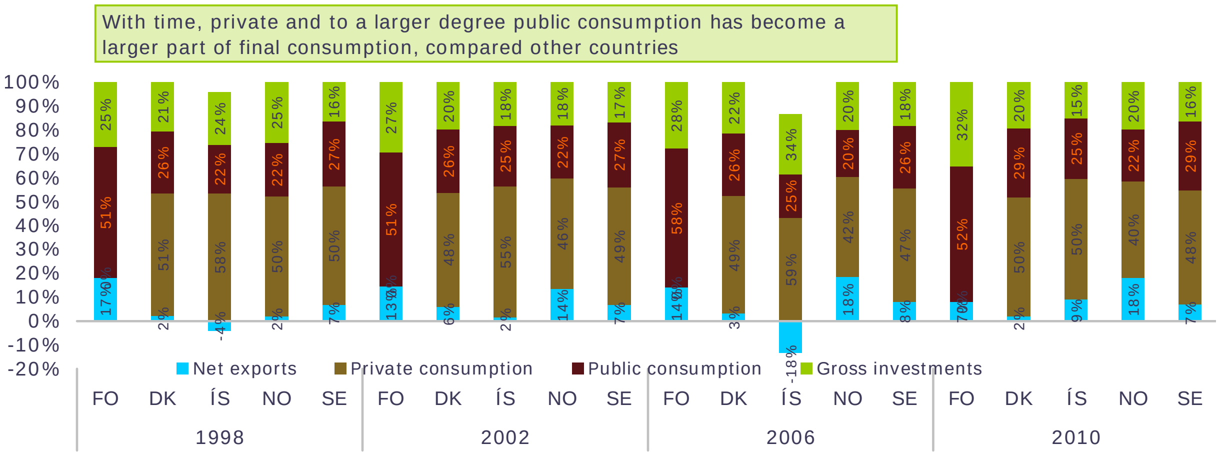
Comment: The Faroese GDP has been deflated using the General Price Index
Source: Faroese Satistics (1998-2008 statement), Governmental Bank(forecast 2009-2010) and statistical bureau´s in neighboring countries

Distribution of GDP-expenditure, 1998 - 2011 F-6



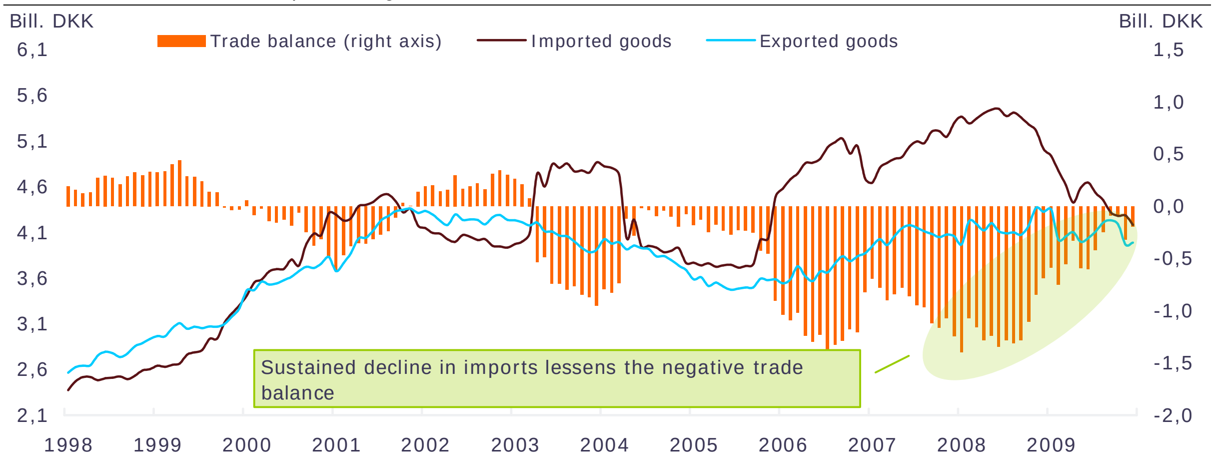
Source: Faroese Statistics (Statement 1998 - 2006) and Governmental Bank (Forecast 2007 - 2011)

GDP categorized by expence compared to neighboring countries, 1998 - 2010 F-7



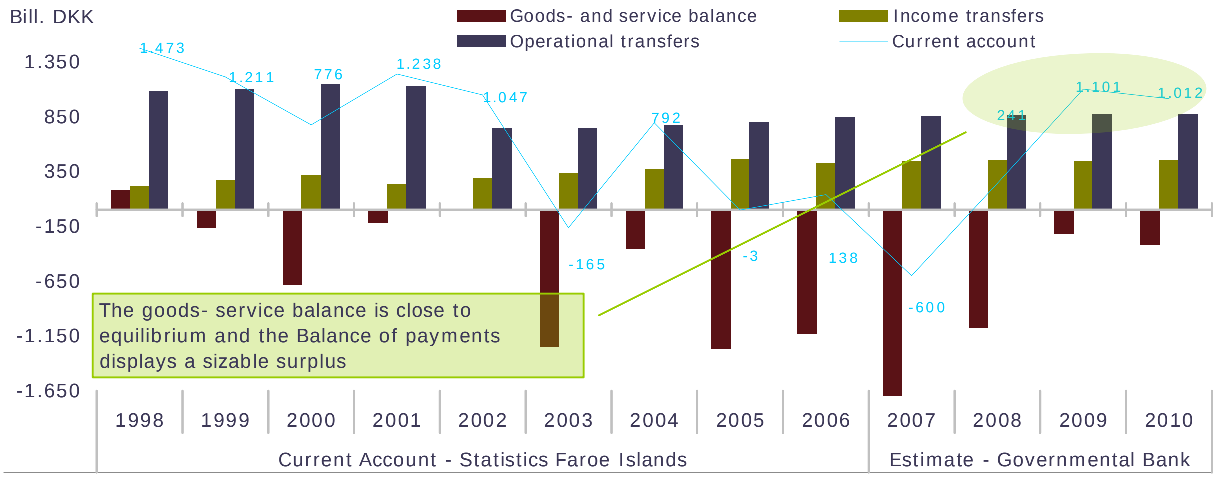
Source: Faroese Statistics (Satements from 1998, 2002 and 2006), Governmental Bank (Forecast 2010) and OECD for neighboring countries

Trade balance: In- and exports of goods, Jan-98 to Dec-09 F-8



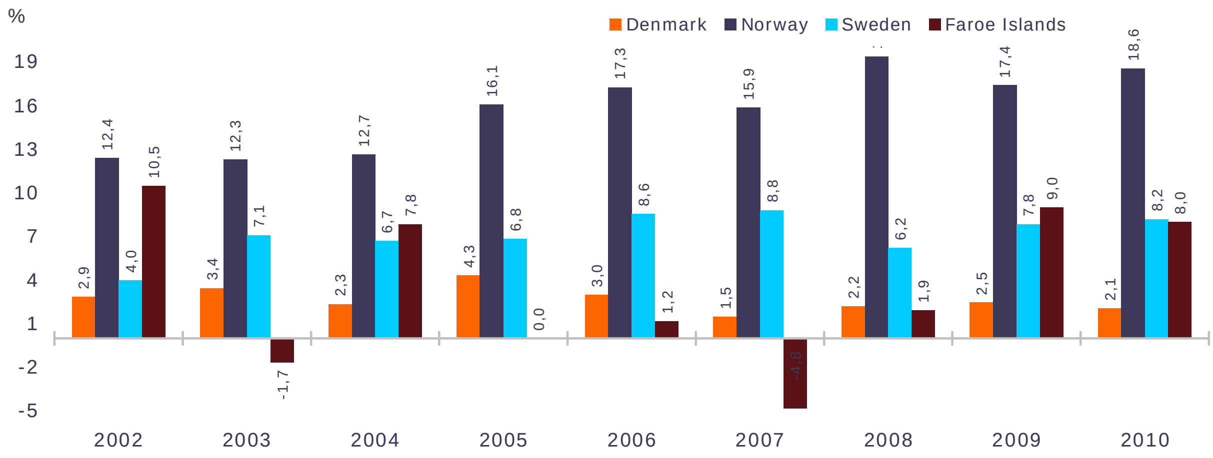
Comment: Inports and exports are based on a 12 month moving average
Source: Statistics Faroe Islands

Balance of payments 1998-2010 F-9



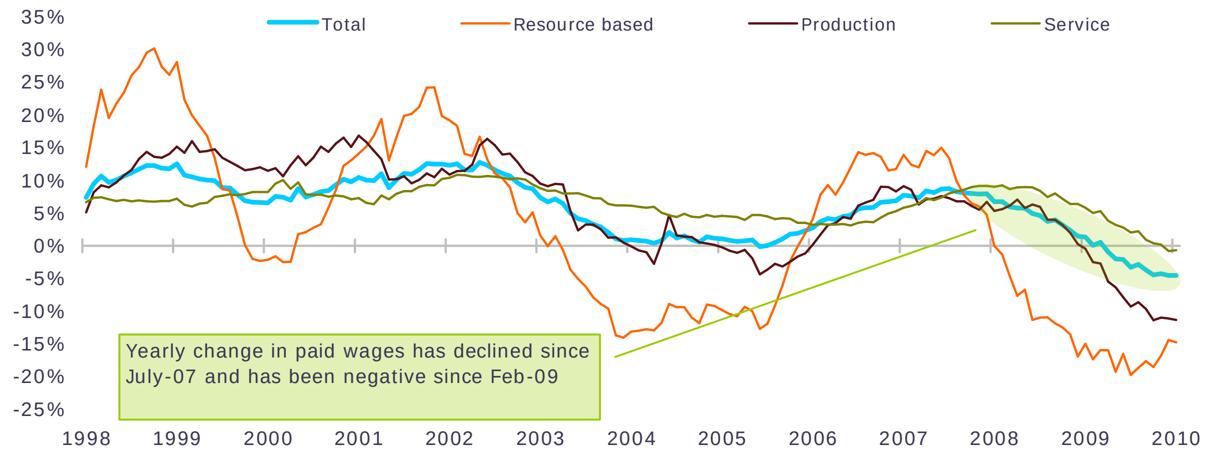
Source: Faroese Statistics (1998-2006) and the Governmental Bank (2007-2010)

Balance of payments as part of GDP F-10



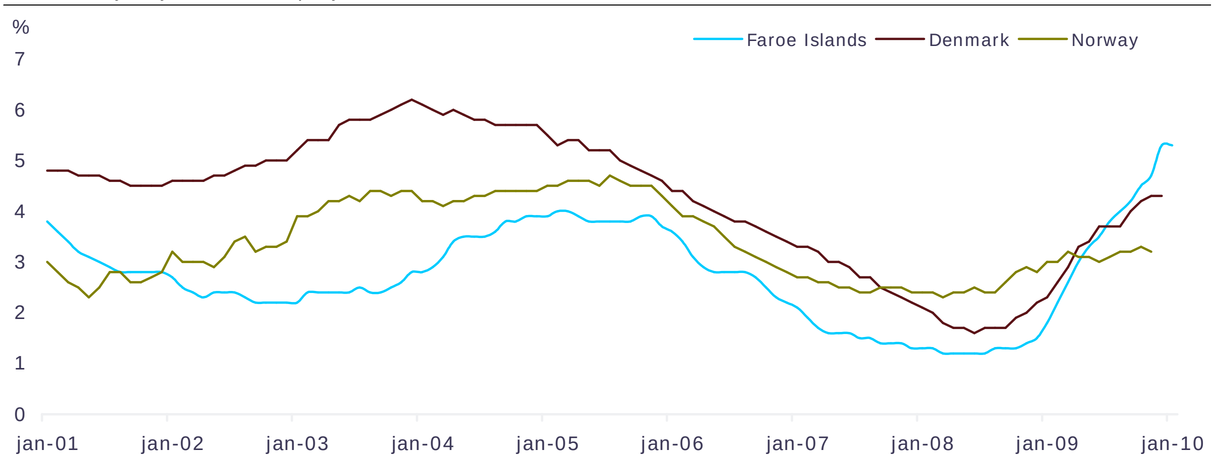
Source: Faroese Statistics (1998-2006) and the Governmental Bank (2007-2010), OECD for neighboring countries

Wage payments, year/year change, Jan-98 til Jan-10 F-11



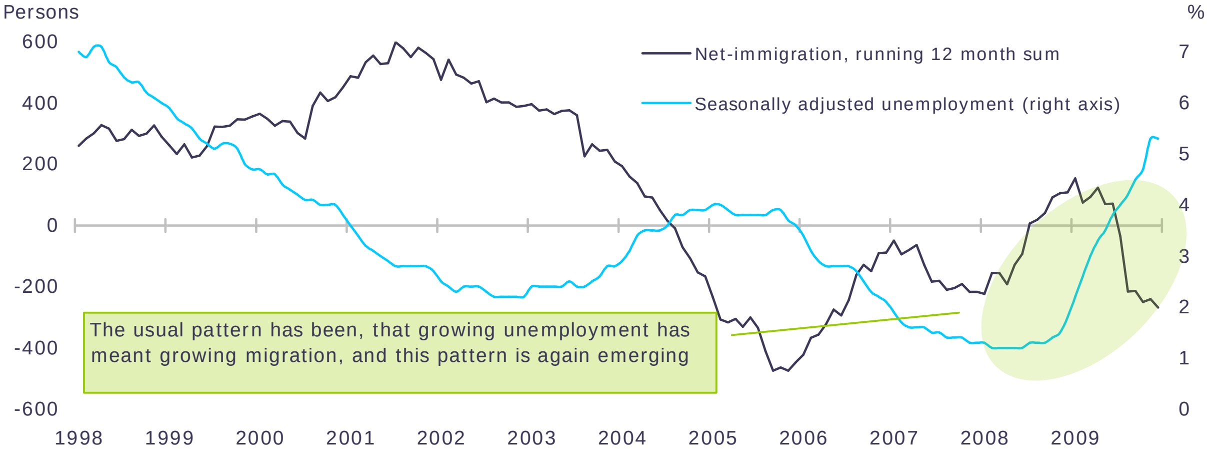
Source: Faroese Statistics, monthly data

Seasonally adjusted unemployment as % of workforce, Jan-98 to Jan-10 F-12



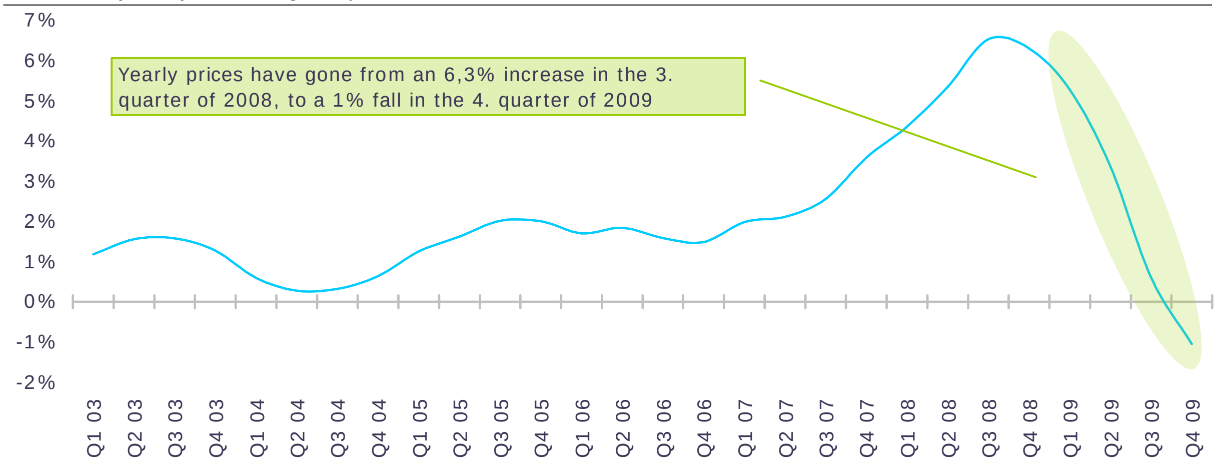
Source: Faroese Statistics and OECD

Unemployment and net-migration, Jan-98 to Jan-10 F-13



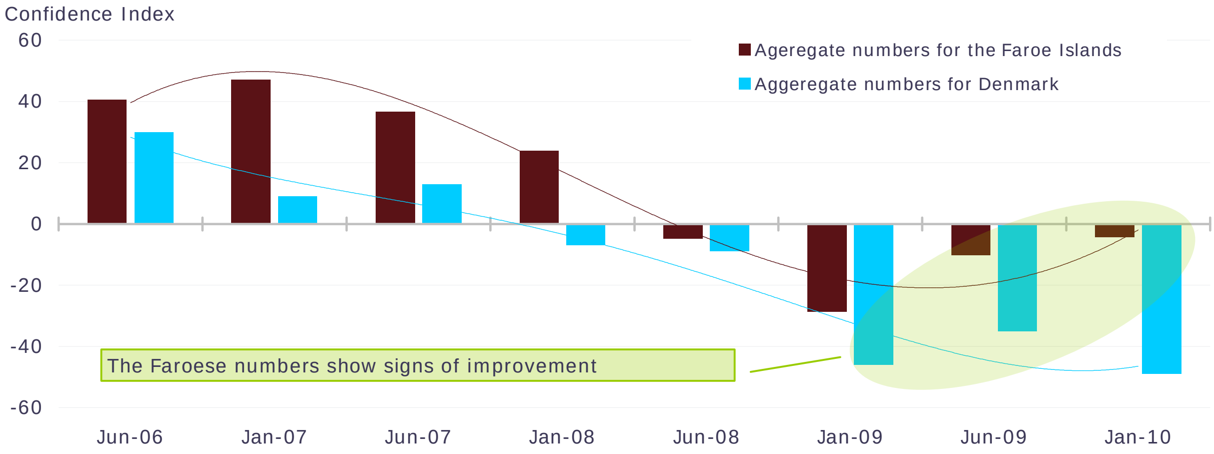
Source: Faroese Statistics and OECD

Inflation, year/year change in price index F-14



Source: Faroese Statistics

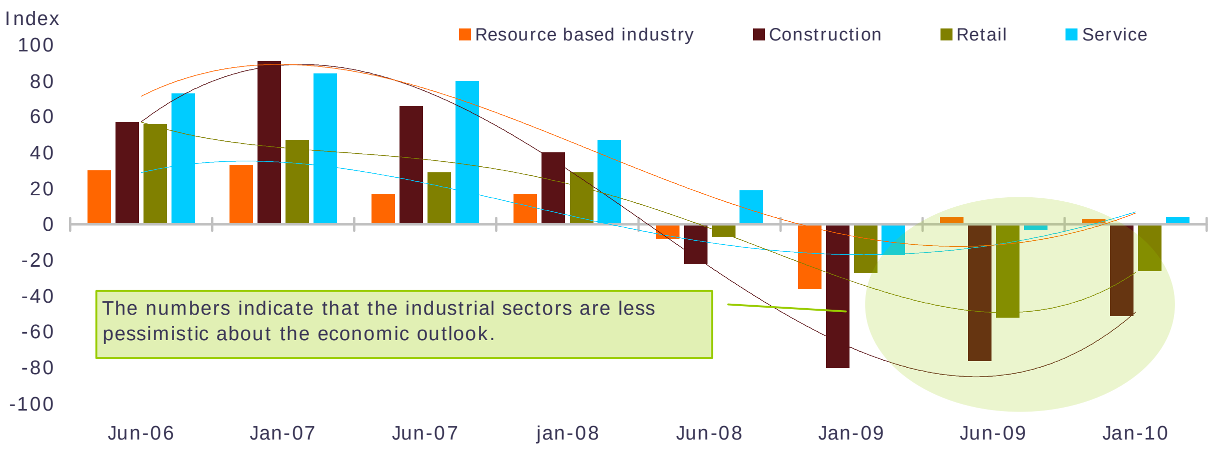
Industry- and consumer confidence - Aggregate numbers. F-15



Comment: The Faroese are asked about the situation 12 months ahead, while the Danes are asked about the same, only 3 months ahead
Source: Finance departement and Danish Statistics

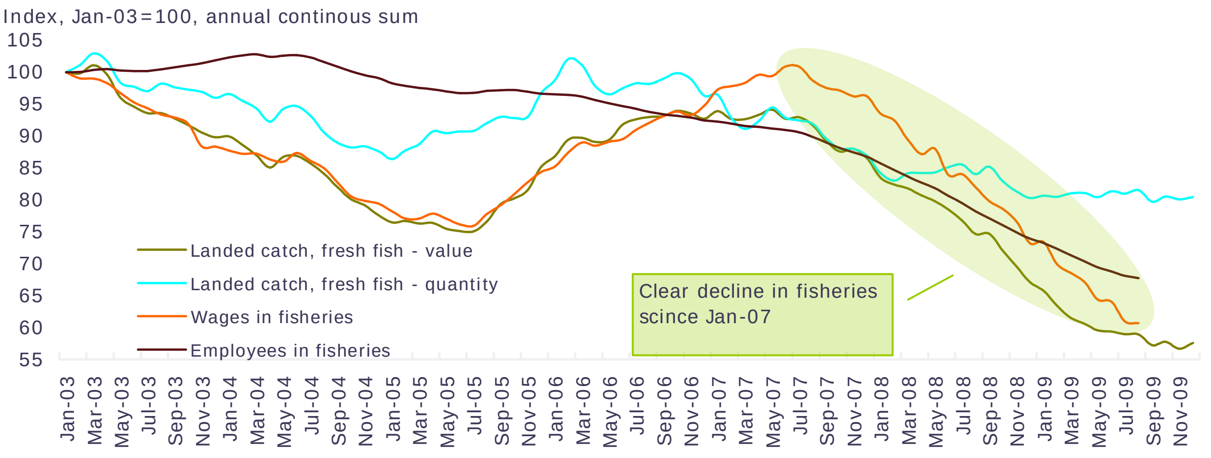
Appendix 2: The industrial sector

Confidence Index for different Industrial Sectors, Jun-06 til Jan-09 F-16



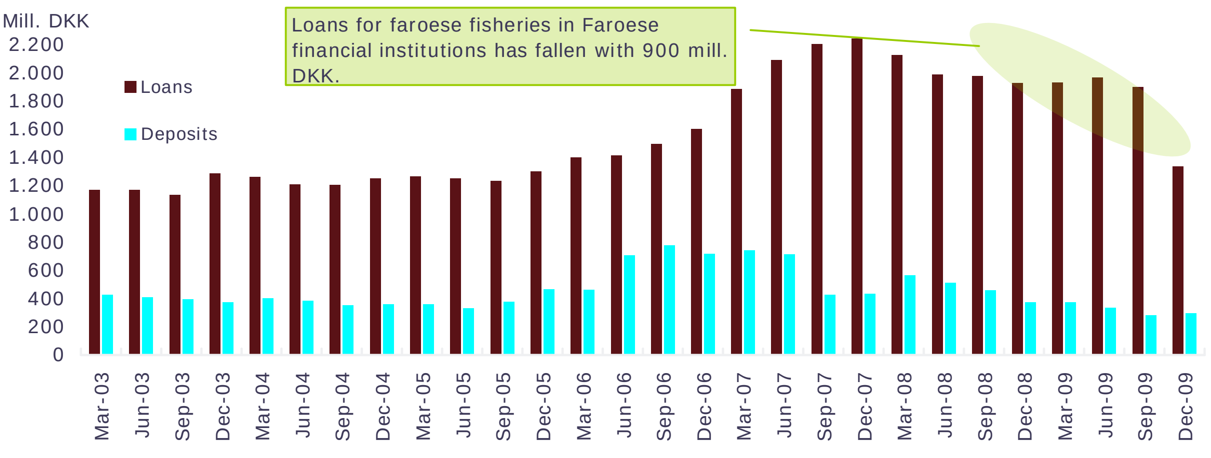
Source: Finance Ministry

Trends in fisheries, Jan-03 to Dec-09 F-17



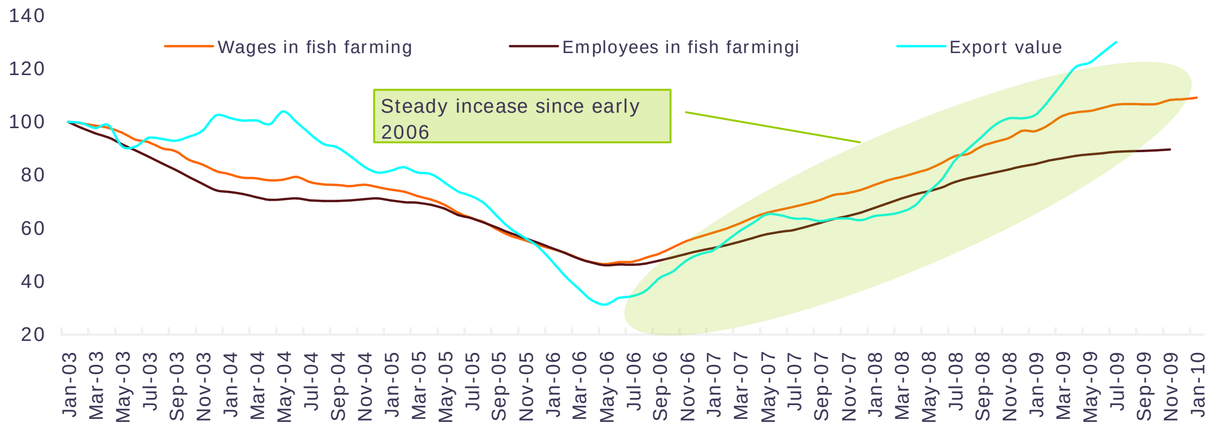
Source: Faroese Statistics

Loans and deposits for fisheries in financial institutions, Mar-03 to Dec-10 F-18



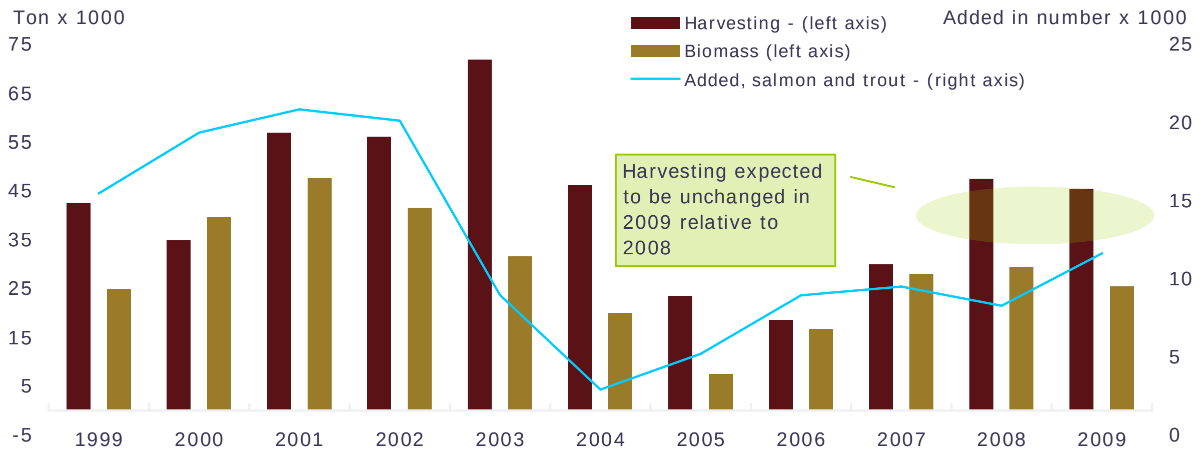
Source: Faroese Statistics

Indicators for fish farming, Jan-03 to Jan-10 F-19



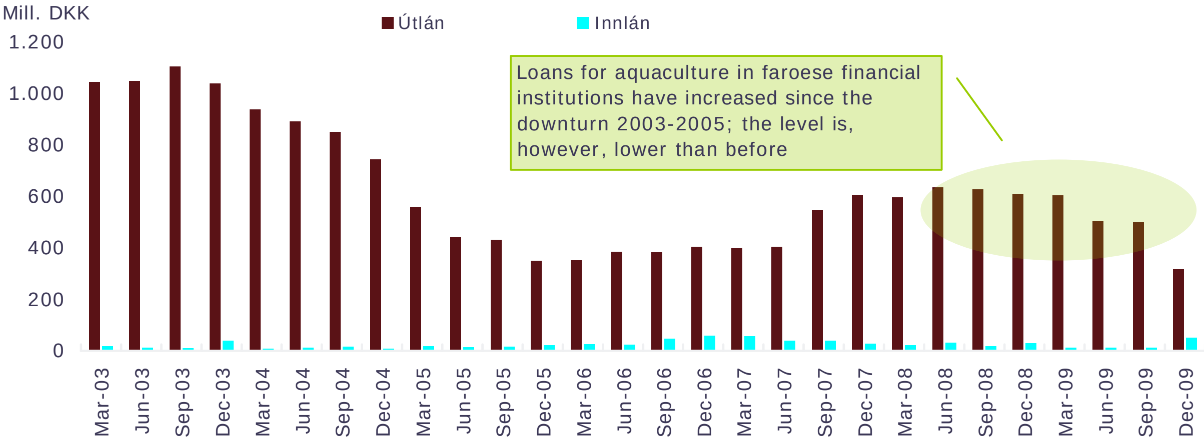
Source: Faroese Statistics

Harvesting and stocks of salmon and trout 1999 - 2009 F-20



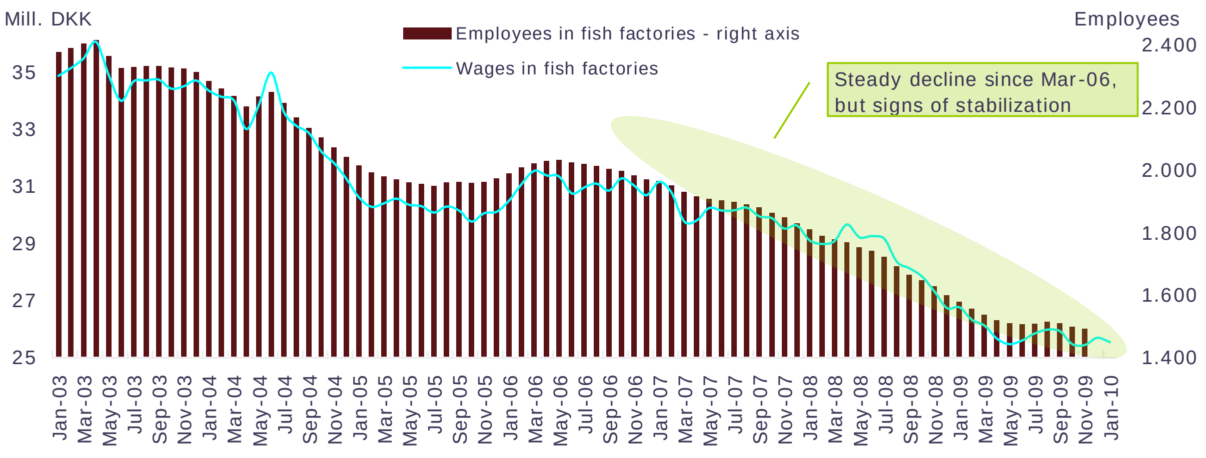
Source: Avrik sp/f

Loans and deposits for fish farming in financial institutions, Mar-03 to Dec-09 F-21



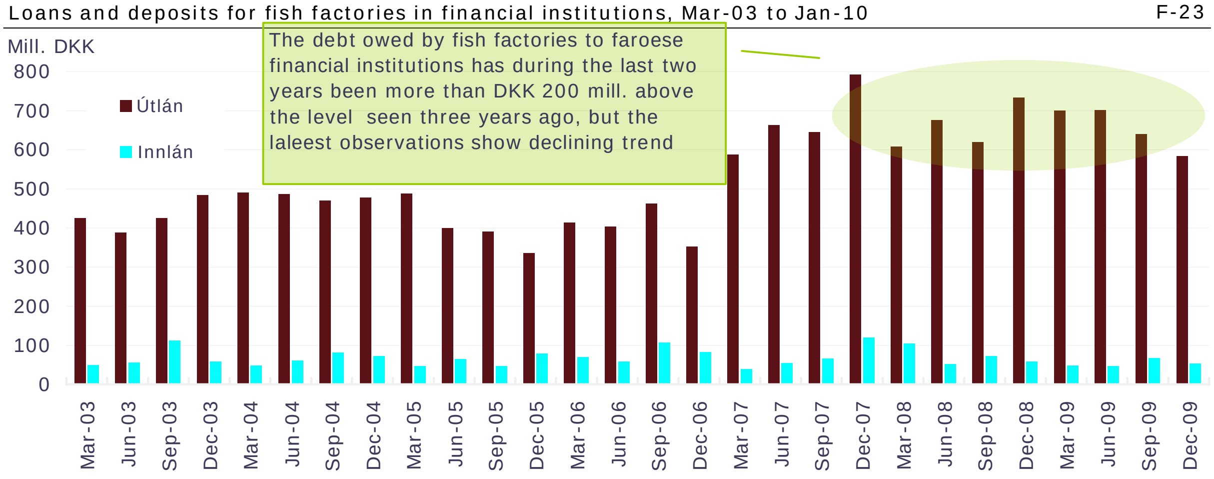
Source: Governmental Bank

Trend developments in fish factories, Jan-03 to Jan-10 F-22



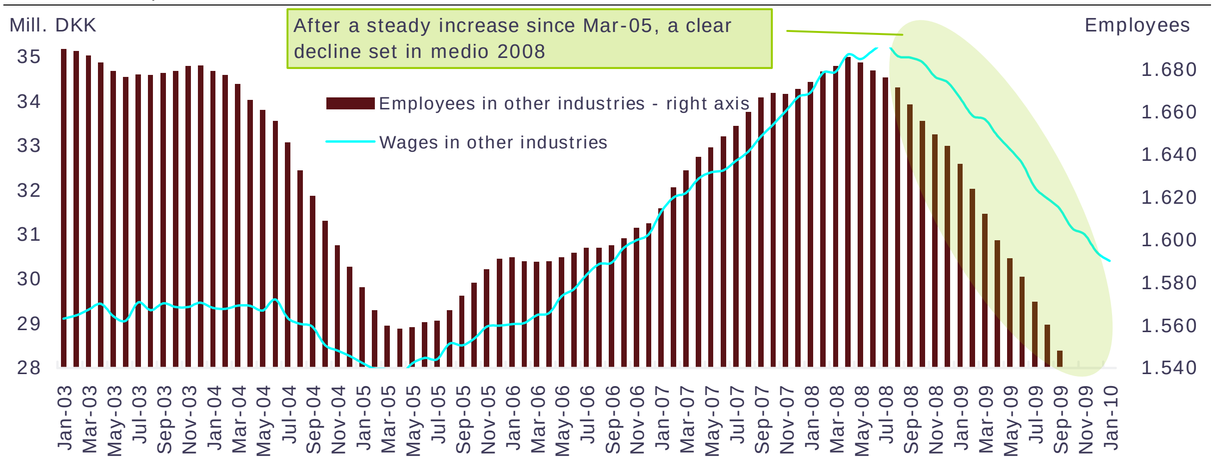
Source: Faroese Statistics

Loans and deposits for fish factories in financial institutions, Mar-03 to Jan-10 F-23



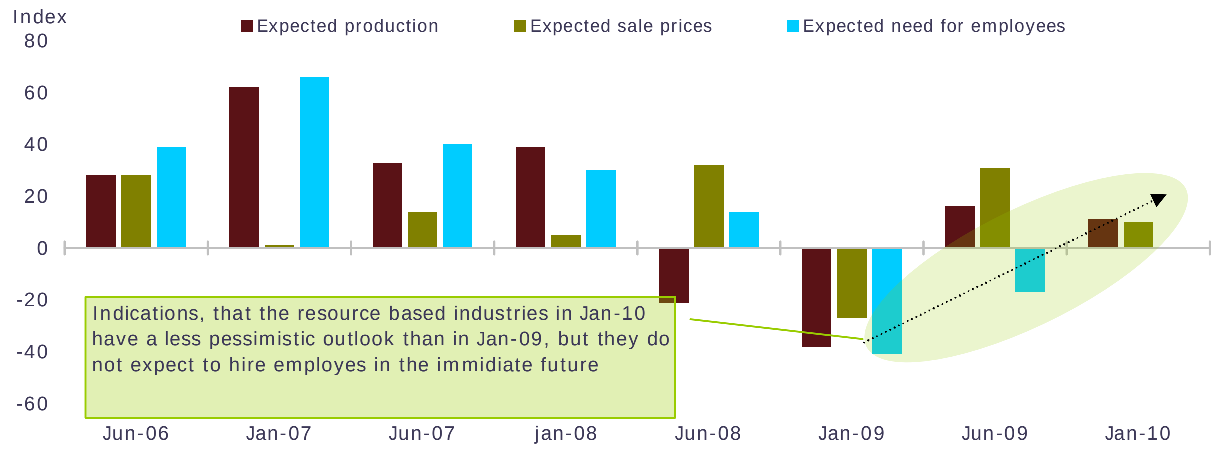
Source: Landsbanki Føroya

Trend developments for other industries, Jan-03 til Jan-10 F-24



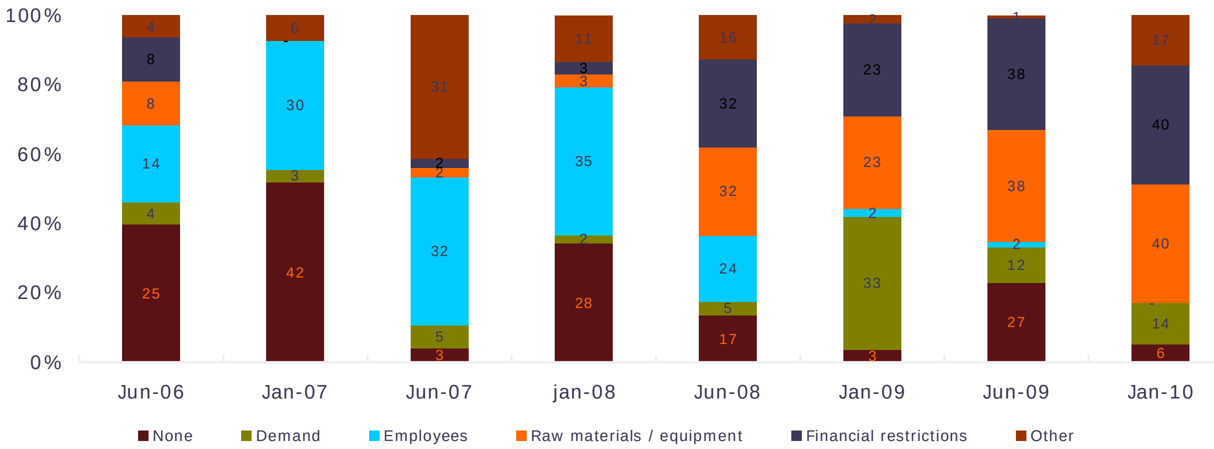
Source: Faroese Statistics

Confidence Index - resource based / other industries - their outlook concerning, prices, production and employees, Jun-06 til Jan-10 F-25



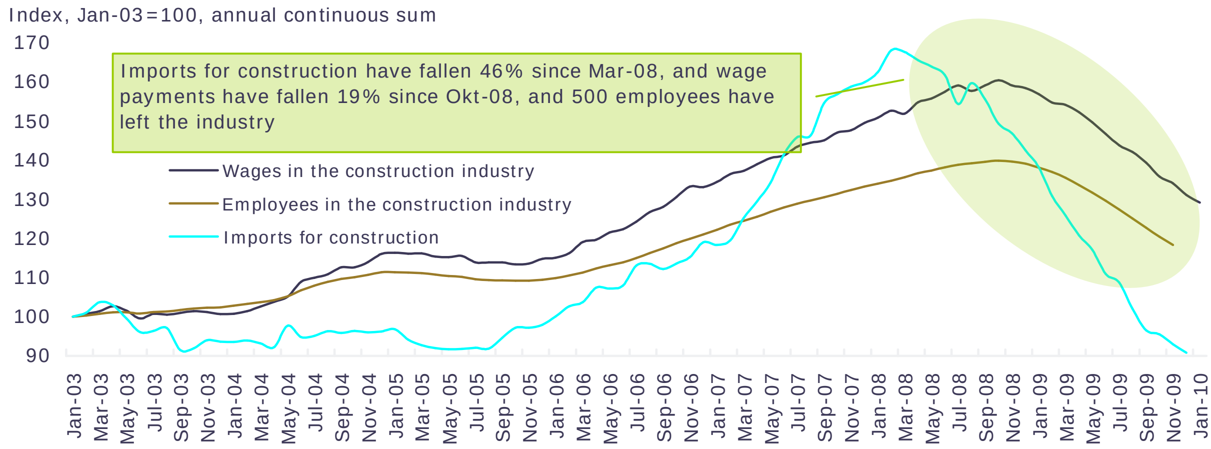
Source: Finance Ministry

Rescource based / other industries and their views on restrictions on production, jun-06 to Jan-10 F-26



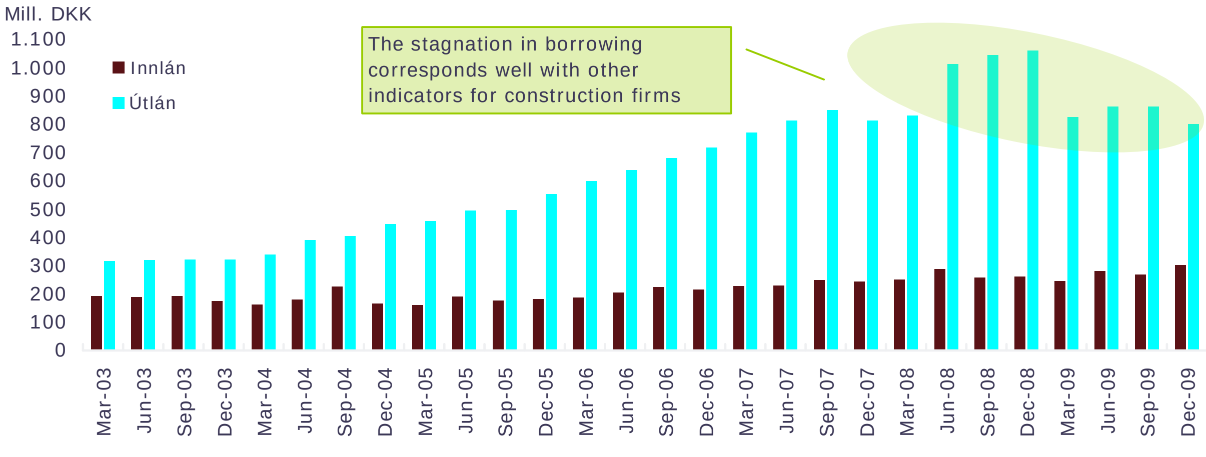
Source: Finance Ministry

Trend developments in construction, Jan-03 to Jan-10 F-27



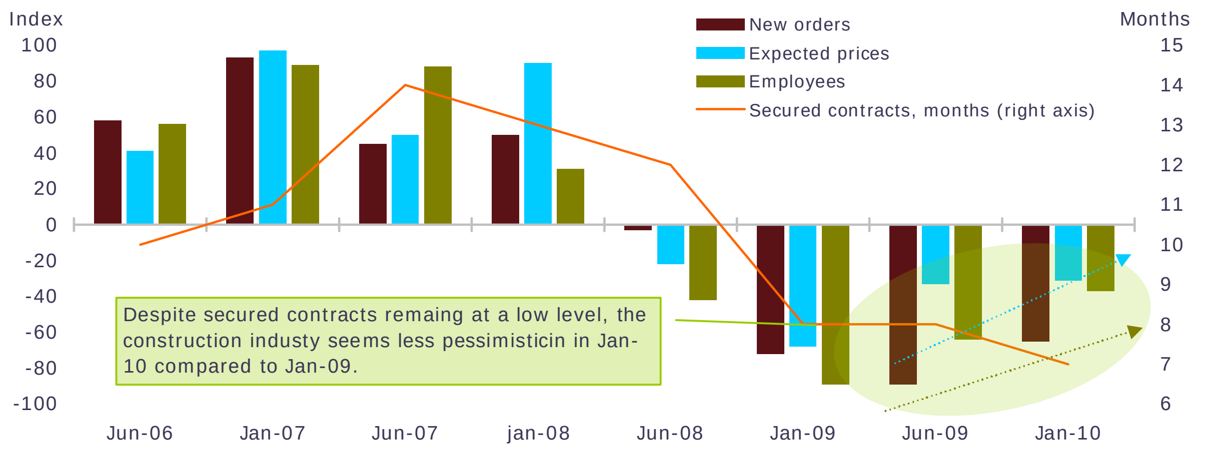
Source: Faroese Statistics

Loans and deposits for construction in financial institutions, Mar-03 to Dec-10 F-28



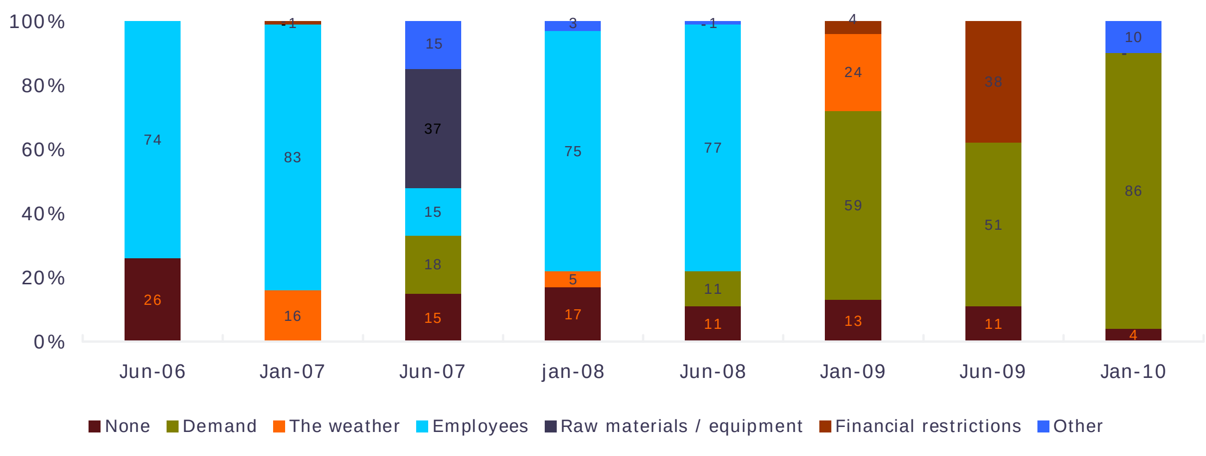
Source: Governmental Bank

Construction industry expectations about prices and employees, Jun-06 to Jan-10 F-29



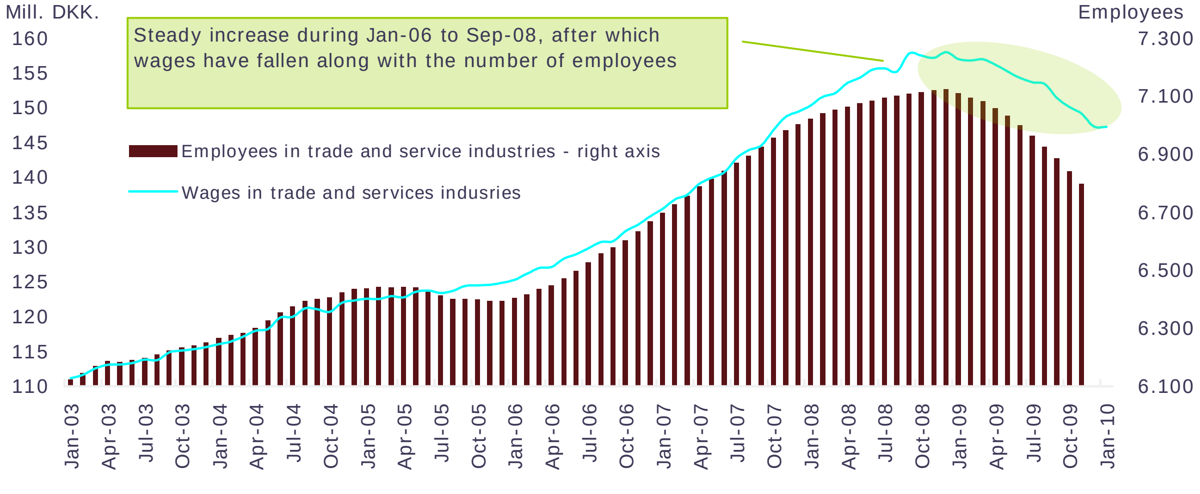
Source: Finance Ministry

Construction industry - its view on restrictions on production, Jun-06 to Jan-10 F-30



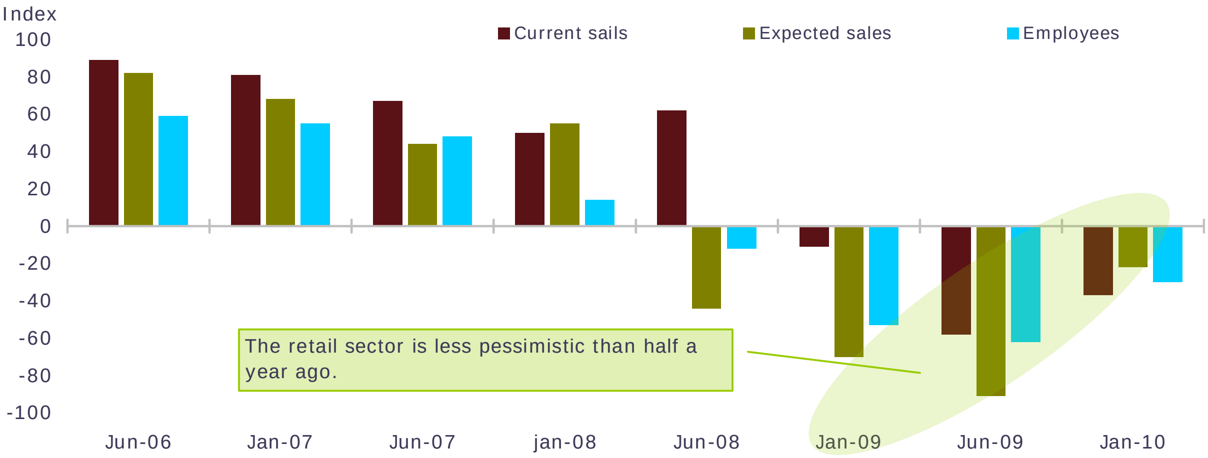
Source: Finance Ministry

Trend developments in trade and service industries, Jan-03 to Jan-10 F-31



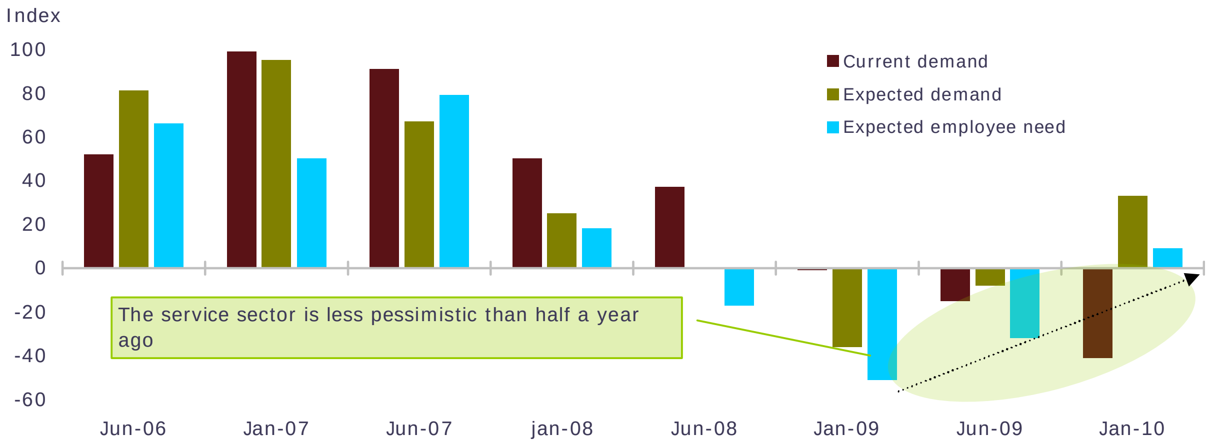
Source: Faroese Statistics

Confidence indicators - retail sector - estimates about current sails plus expectations about future sails and employee need, Jun-06 to Jan-10 F-32



Source: Finance Ministry

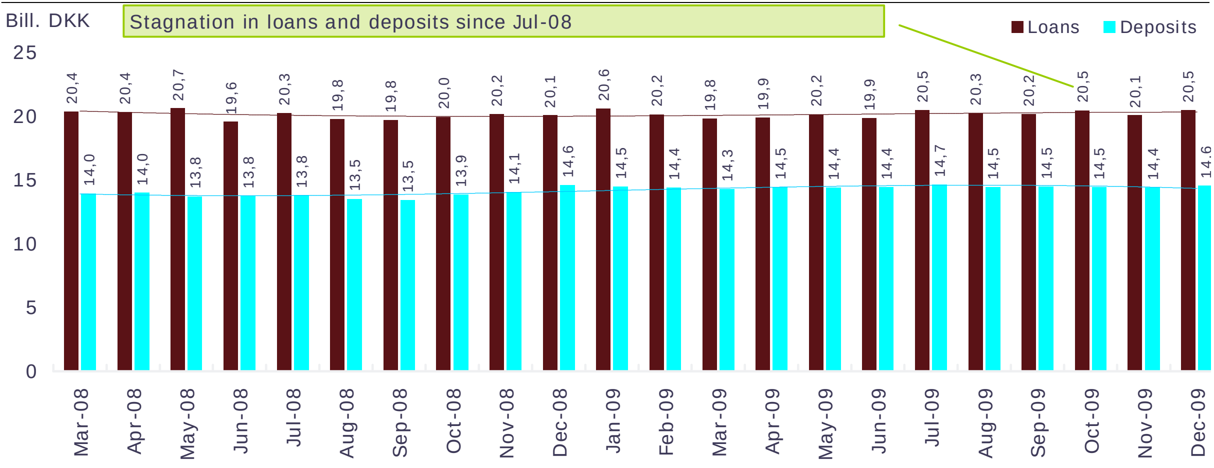
Confindence indicators - service sector - expectations Jun-06 to Jan-10 F-33



Source: Finance Ministry

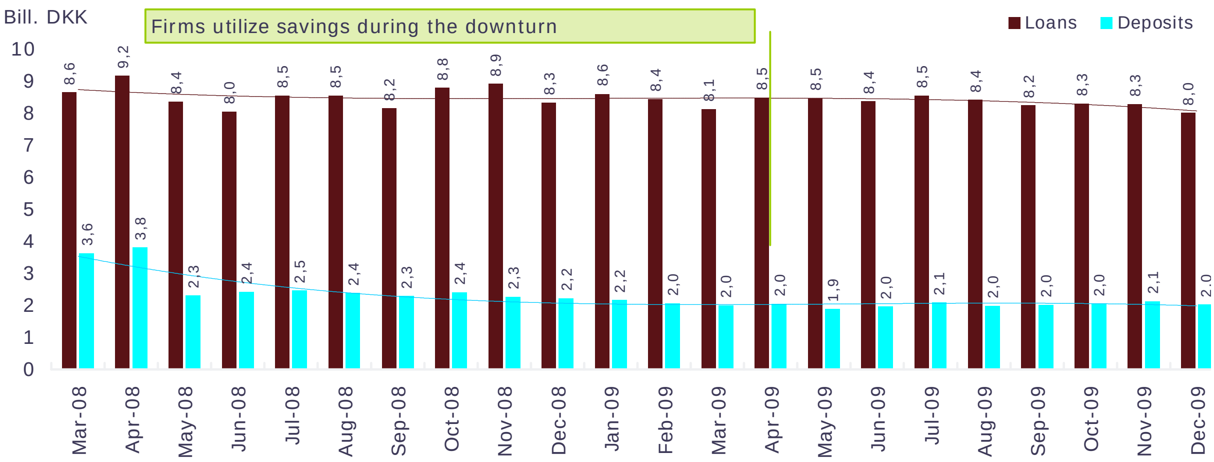
Appendix 3: The financial sector

Total loans and deposits in faroese banks, Mar-08 to Dec-10 F-34



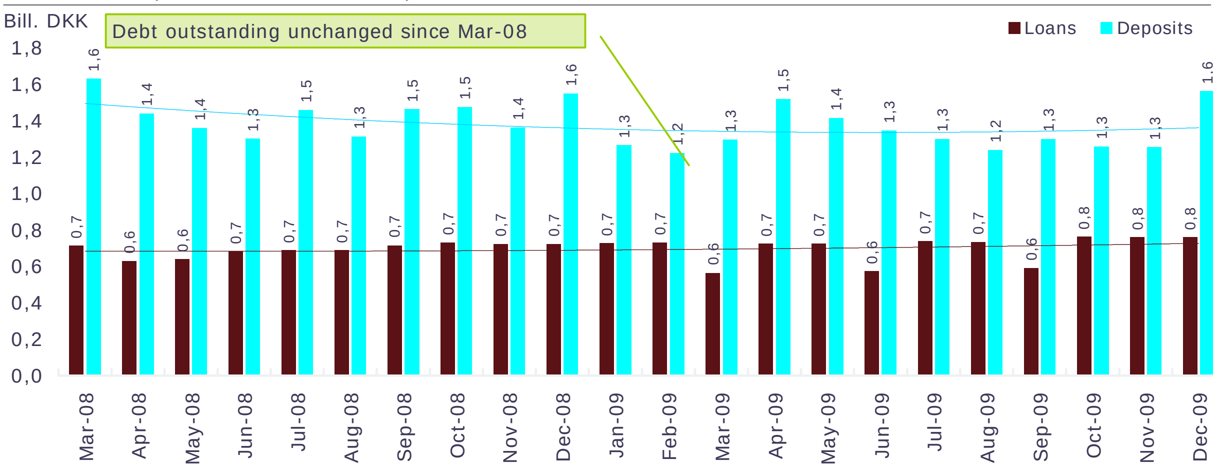
Source: Governmental Bank

Loans and deposits to and from firms, Mar-08 to Dec-09 F-35



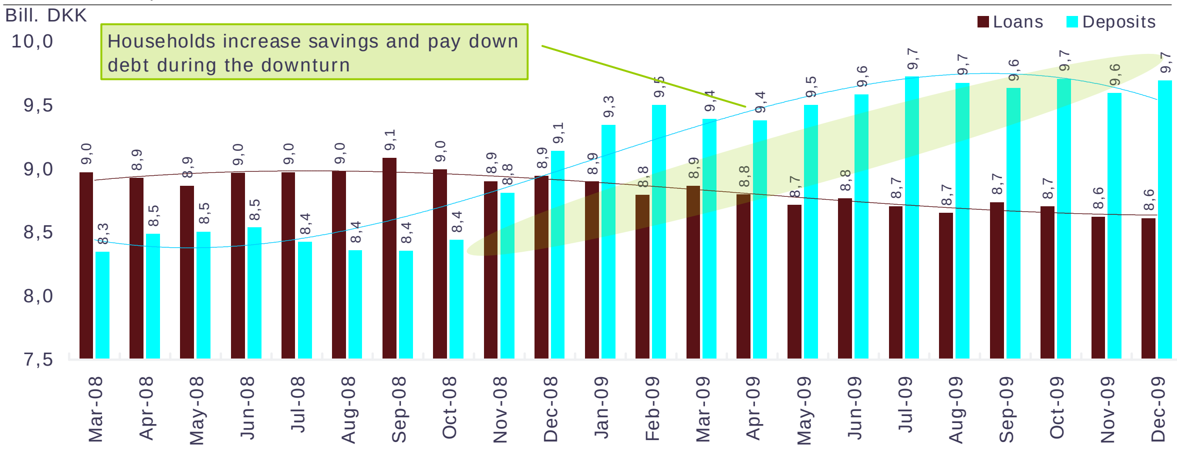
Source: Governmental Bank

Loans and deposits to and from the public sector, Mar-08 to Dec-09 F-36



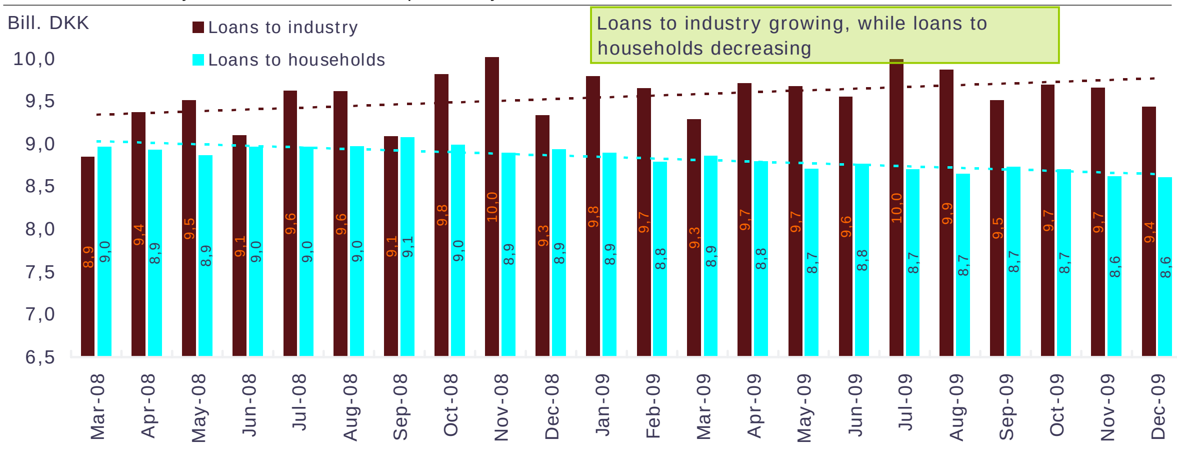
Source: Governmental Bank

Loans and deposits to and from households, Mar-08 to Dec-09 F-37



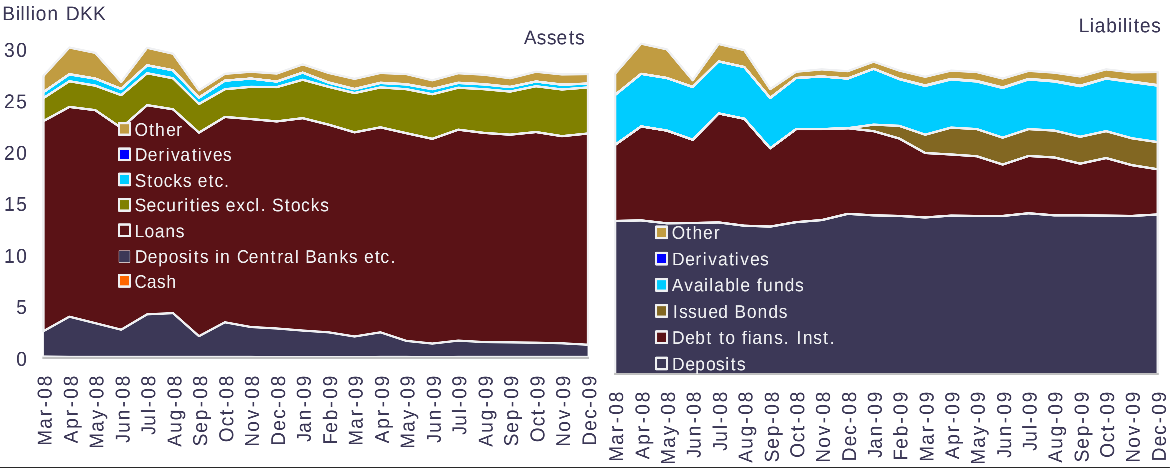
Source: Govermental Bank

Loans to industry and households respectively, Mar-08 to Dec-09 F-38



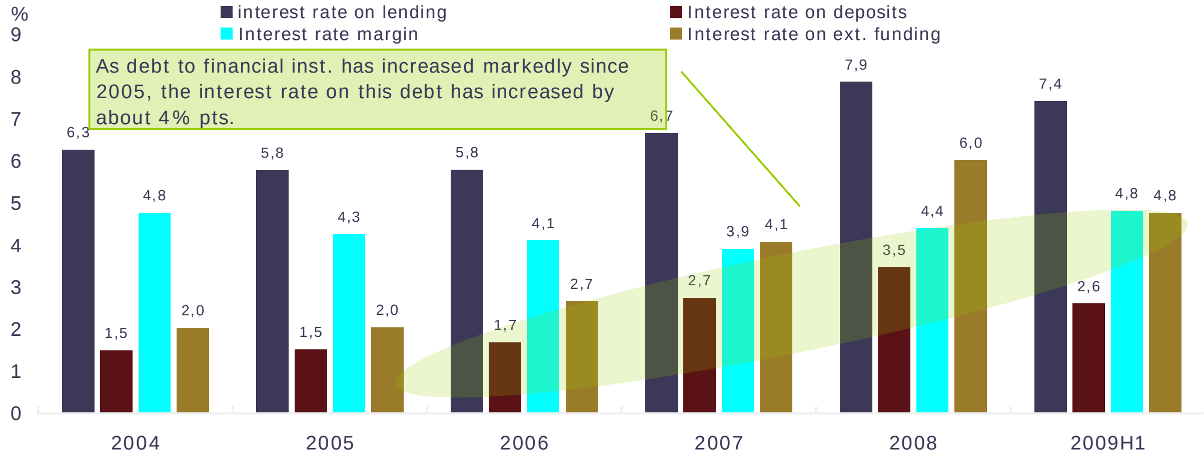
Source: Govermental Bank

Assets and liabilites in Faroese Financial institutions, Mar-08 to Dec-09 F-39



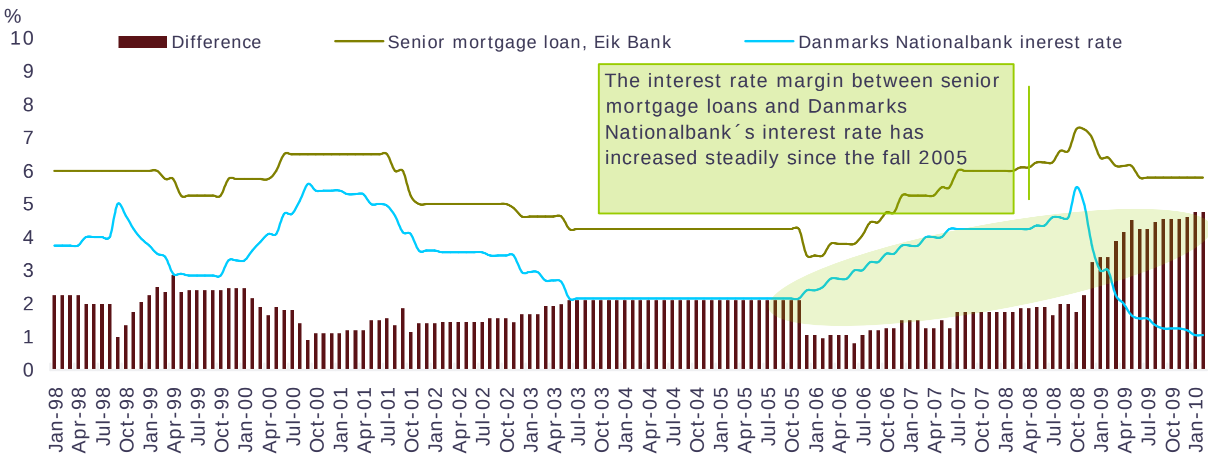
Source: Governmental Bank

Average interest rates on deposits and loans in faroese banks, 2004 to 2009 F-40



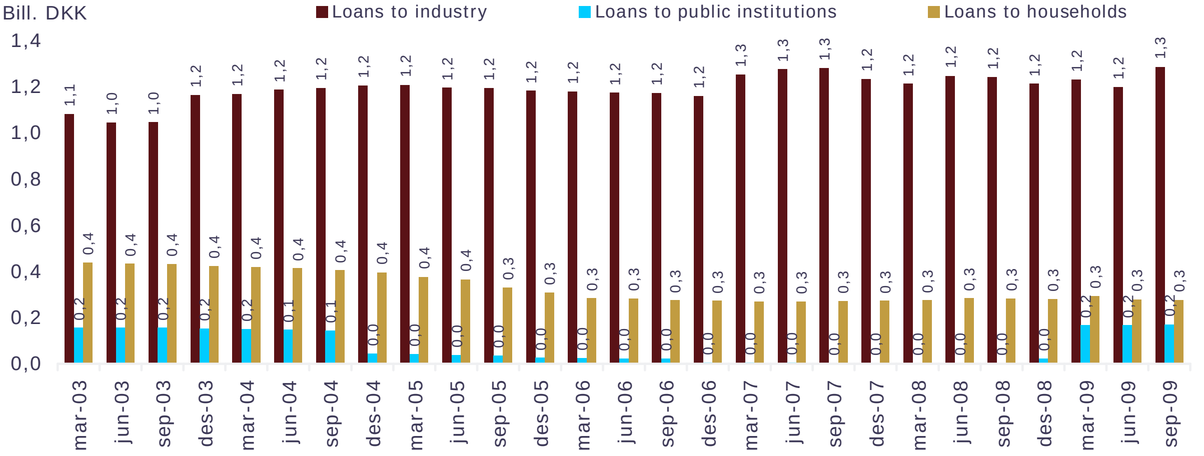
Source: Govermental Bank

Interest rate margin: Mortgage loans in FO and DNB`s interest rate F-41



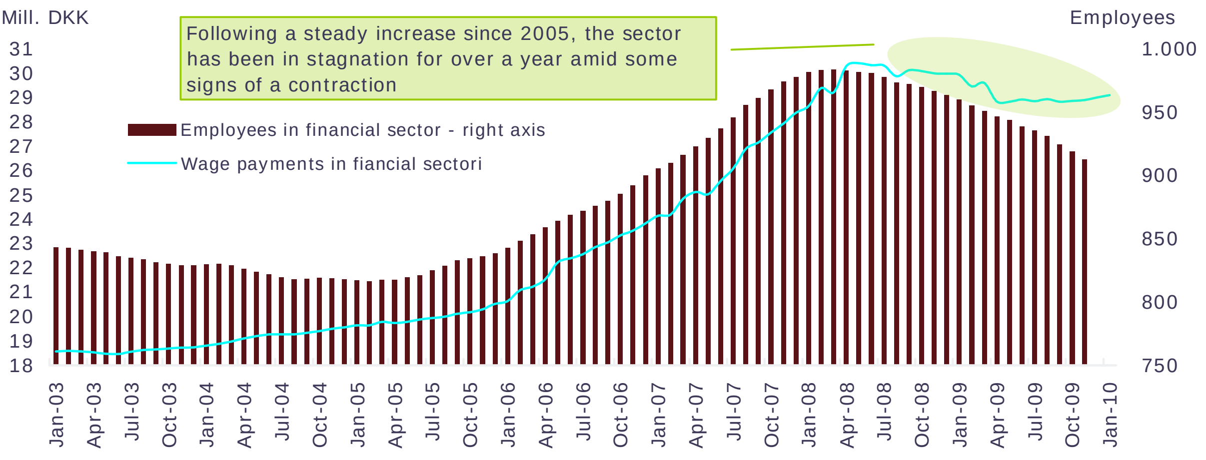
Source: Eik Bank and Danmarks Nationalbank

Loans and deposits - other financial instutions than banks, Mar-03 to Sep-09 F-42



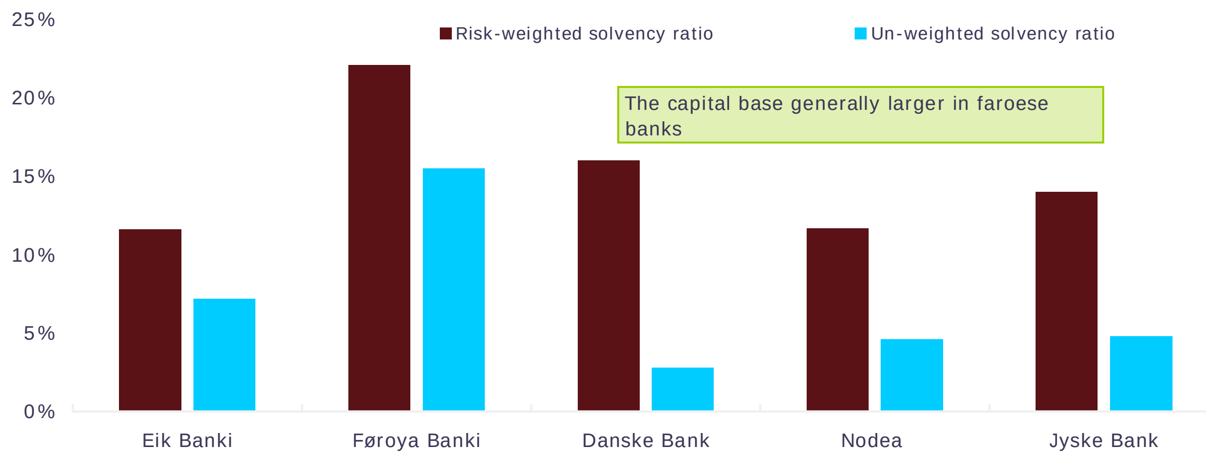
Source: Govermental Bank

Wage payments and employees in the financial sector, Jan-03 to Jan-10 F-43



Source: Faroese Statistics

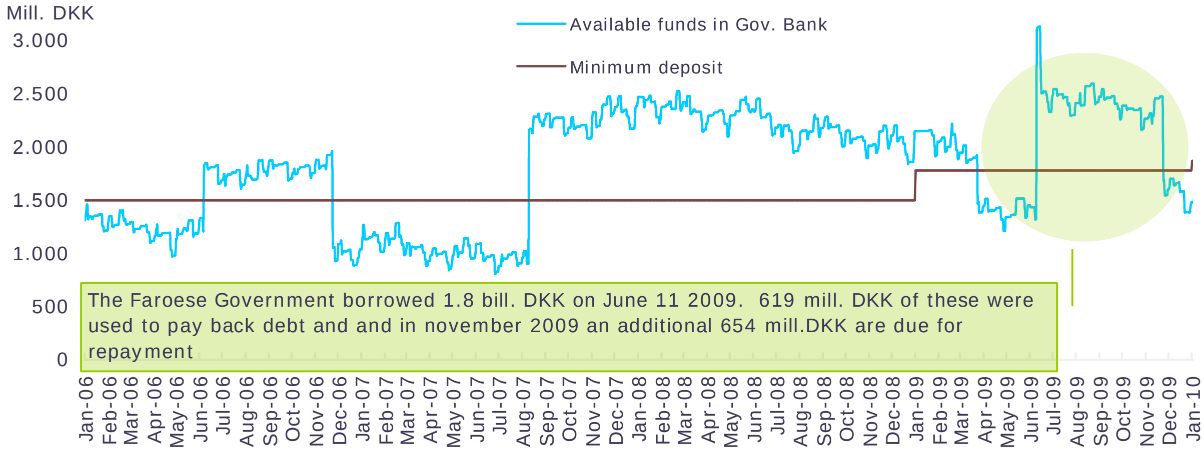
Solvency ratios, selected FO and DK banks, Medio 2009 F-44



Source: Govermental Bank

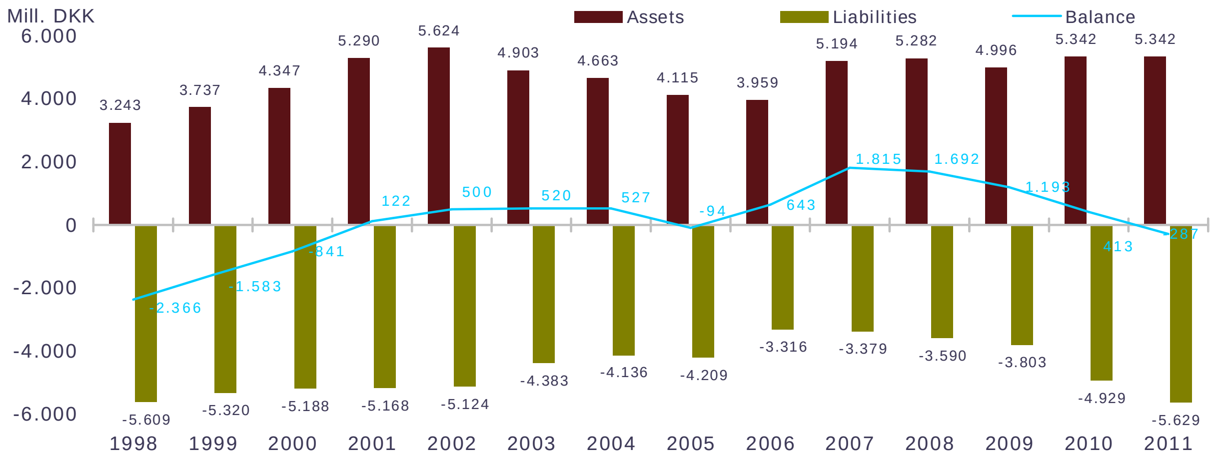
Appendix 4: The public sector

Available funds in Governmental Bank F-45



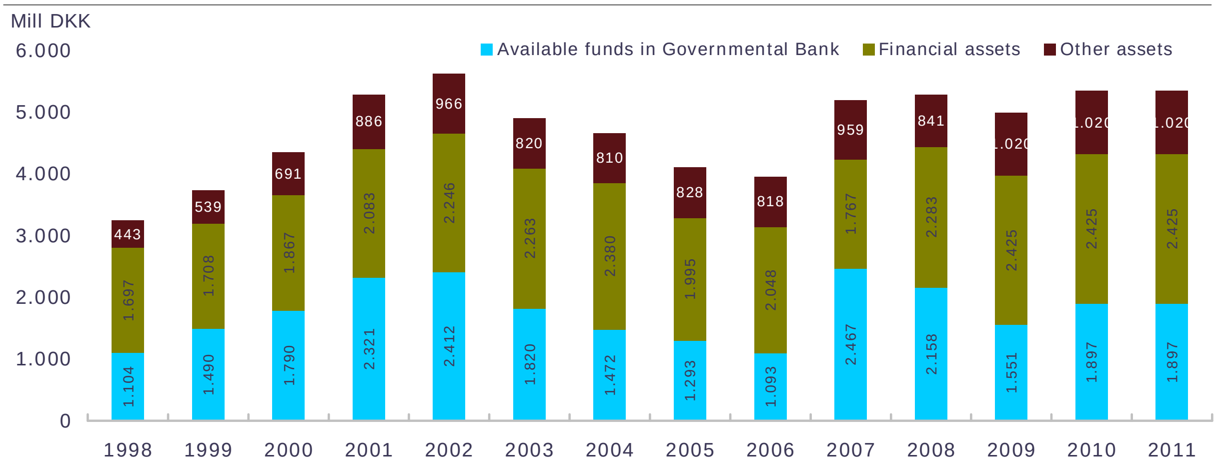
Source: Governmental Bank

Assets and liabilities of central government, 1998-2011 F-46



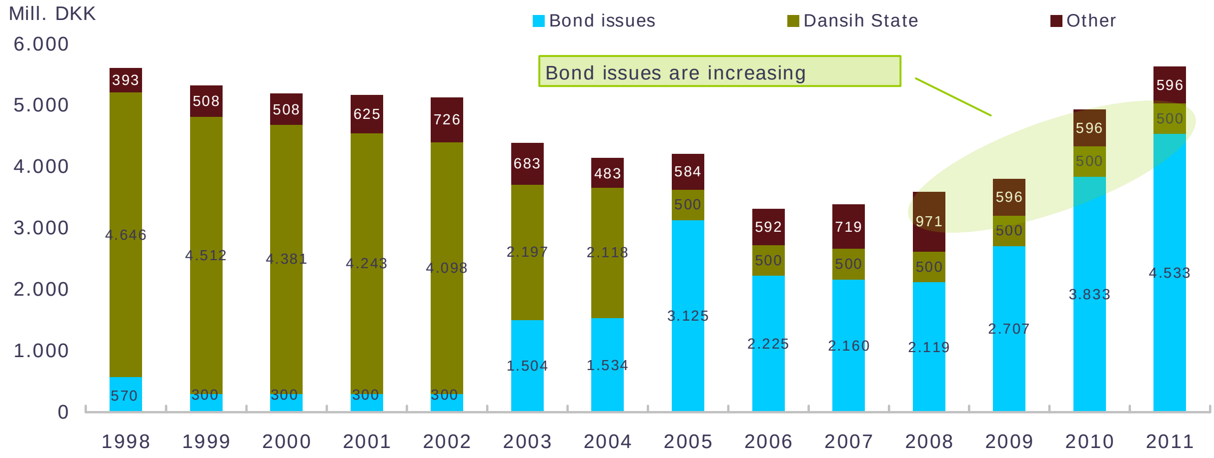
Source: Governmental Bank

Composition of government assets, 1998-2011 F-47



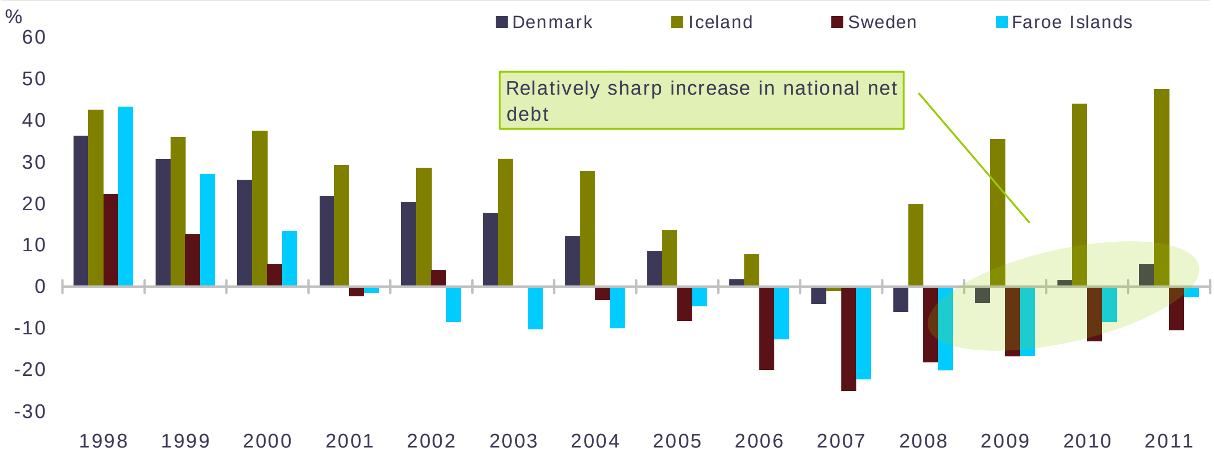
Source: Governmental Bank

Composition of government liabilities, 1998-2011 F-48



Source: Governmental Bank

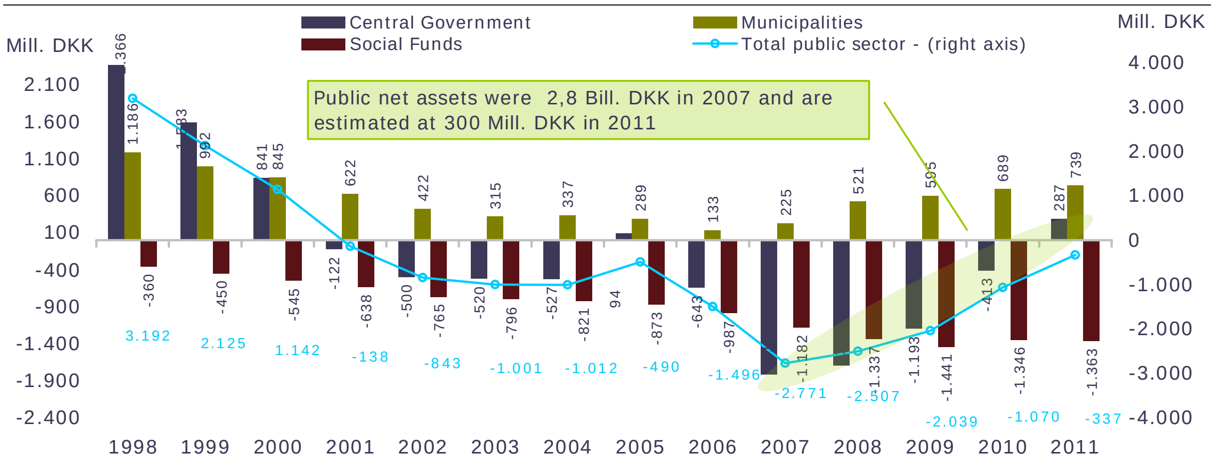
Net debt relative to national GDP in the Faraoes and neighbouring countries F-49



Comment: The numbers for 1998 and 1999 are not available for the Faroe Islands

Source: Governmental Bank and OECD

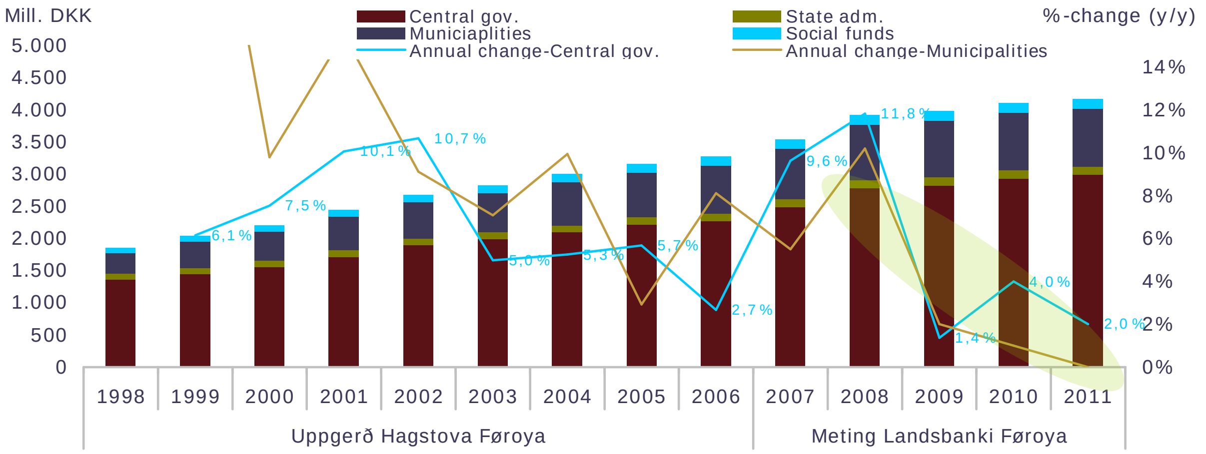
Public net debt, 1998-2011 F-50



Comment: Net debt statements are not available for 1998 and 1999

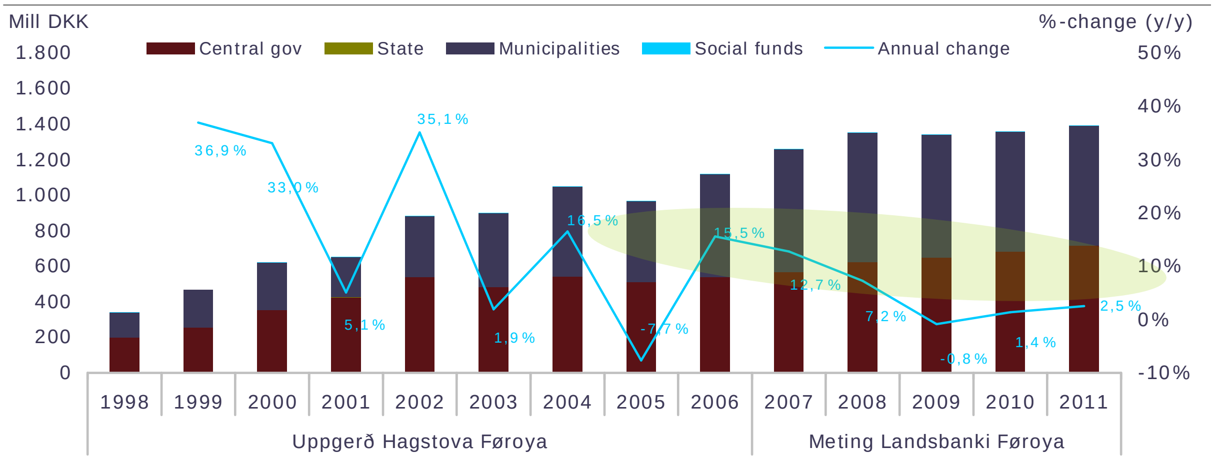
Source: Statistics Faroe Islands and Governmental Bank (estimate 2007-2011)

Public spending distribution, 1998-2011 F-51



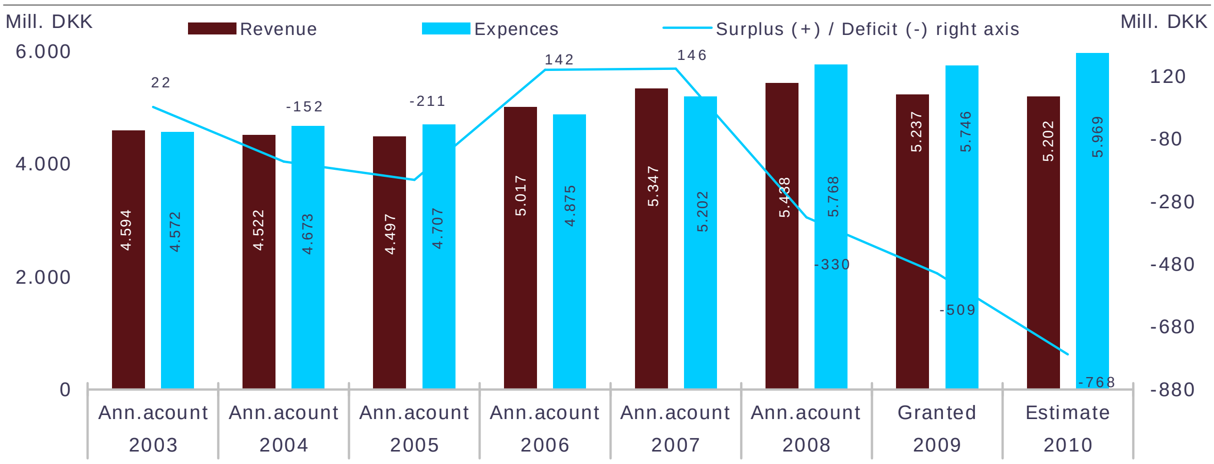
Source: Faroese Statistics (1998-2006) and Governmental Bank (2007-2011)

Public investment distribution F-52



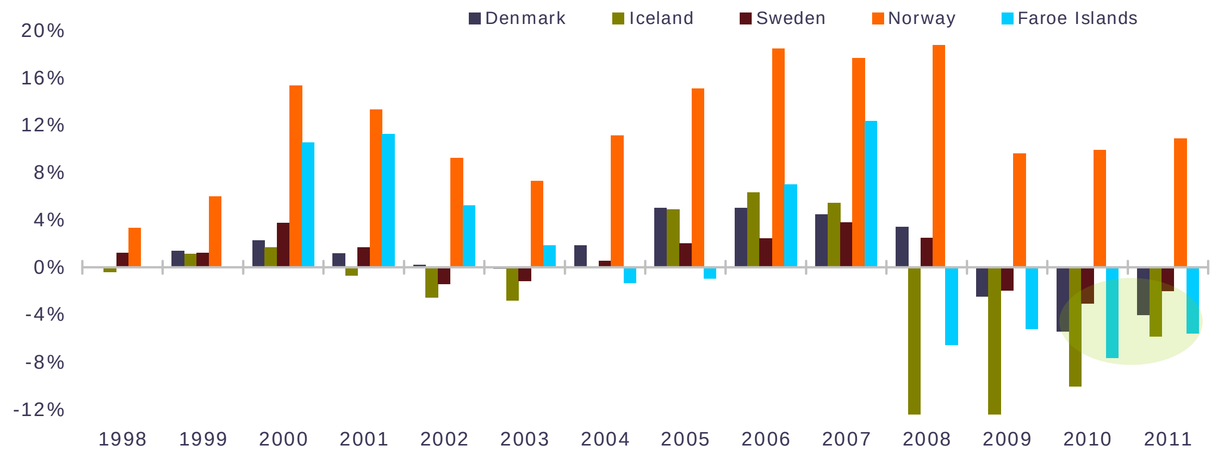
Source: Faroese Statistics (1998-2006) and Governmental Bank (2007-2010)

Government Budget F-53



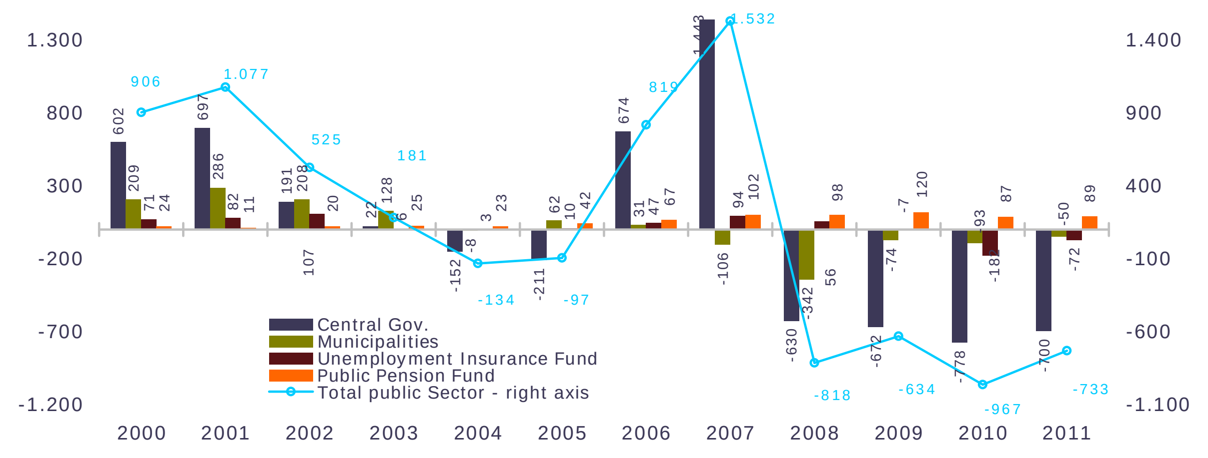
Faroese Budget Office and proposed budget for 2010

National surplus/defecit in the Faroes and neighbouring countries as % of GDP F-54



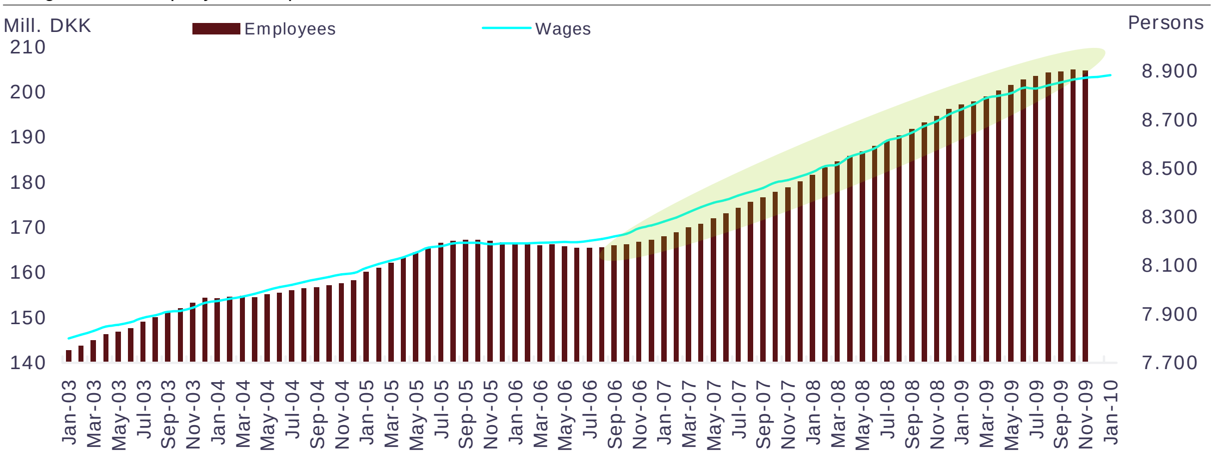
Source:Budget Office, Faroese Statistics, Finance Ministry, Governmental Bank and OECD

Performance in Faroese public sector, 2000-2011 F-55



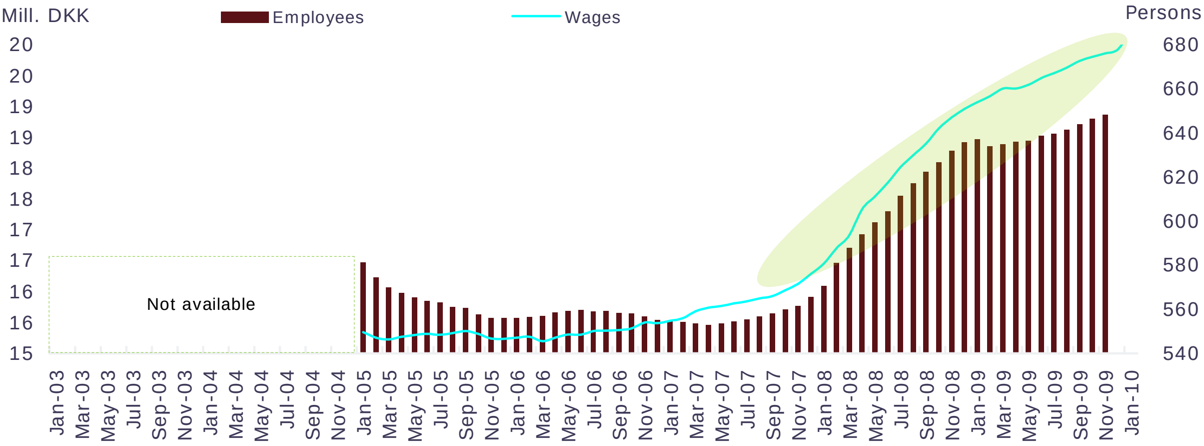
Kelda: Føroya Gjaldstova, Hagstova Føroya, Fíggjarmálaráðið, Landsbanki Føroya

Wages and employees in public administration and service, Jan-98 to Jan-10 F-56



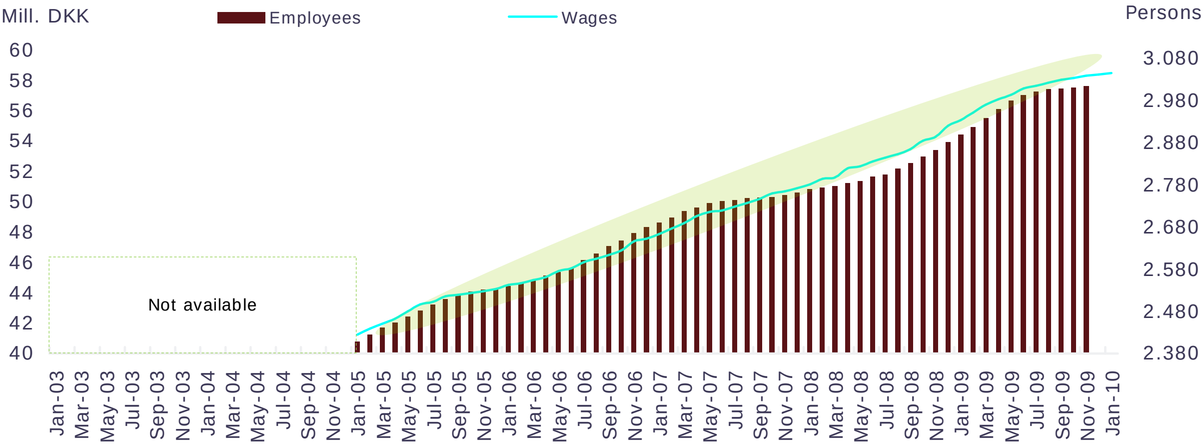
Source: Statistics Faroe Islands

Wages and employees in central administration, Jan-03 to Jan-10 F-57



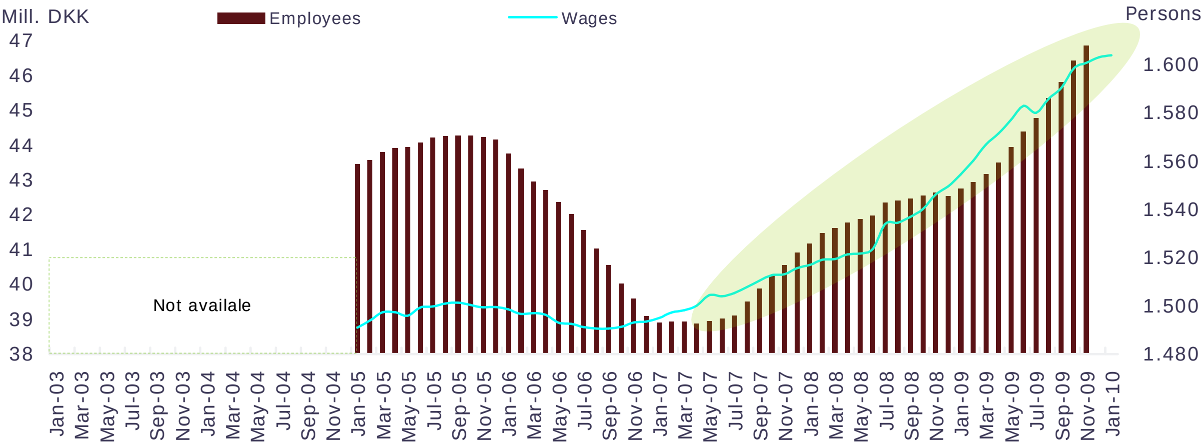
Source: Statistics Faroe Islands

Wages and employees in municipalities and state administration F-58



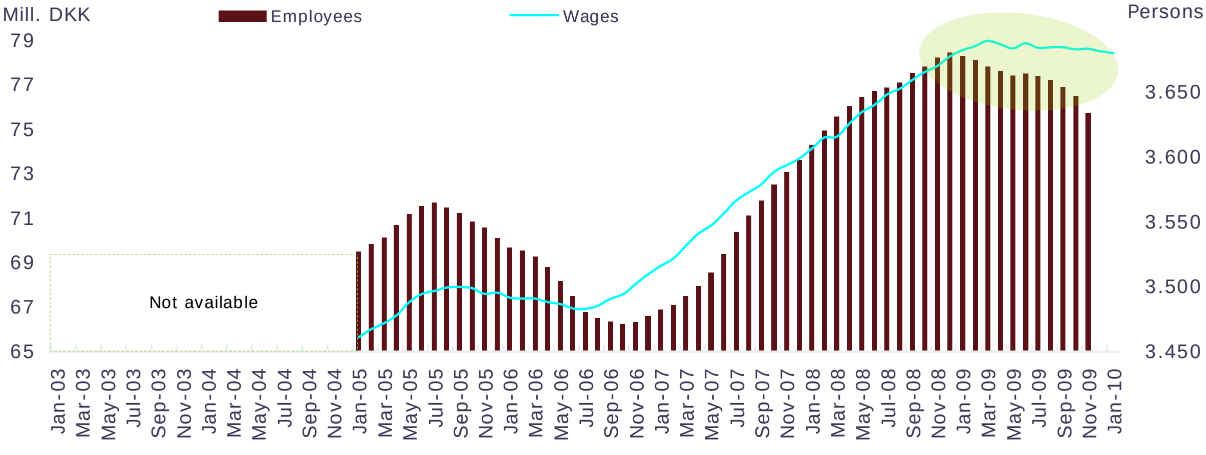
Source: Statistics Faroe Islands

Wages and employees in education, Jan-03 to Jan-10 F-59



Source: Statistics Faroe Islands

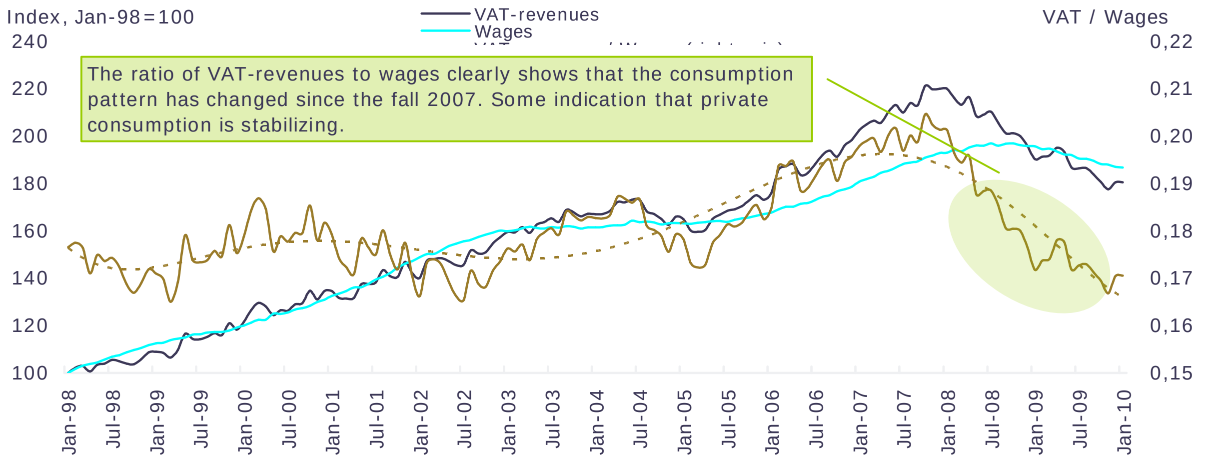
Wages and employees in health services, Jan-03 to Jan-10 F-60



Source: Statistics Faroe Islands

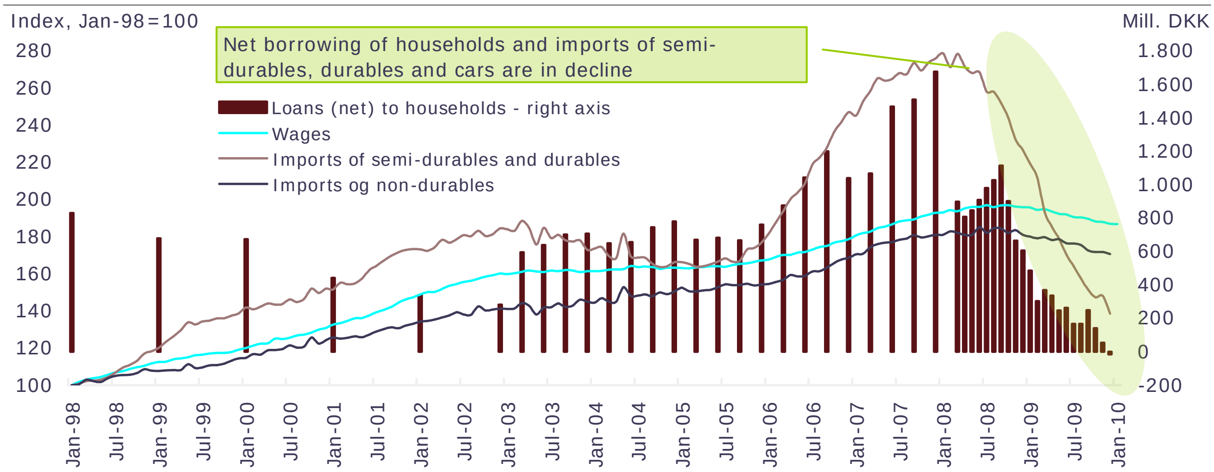
Appendix 5: Households

Wages and VAT-revenues, Jan-98 to Jan-10 F-61



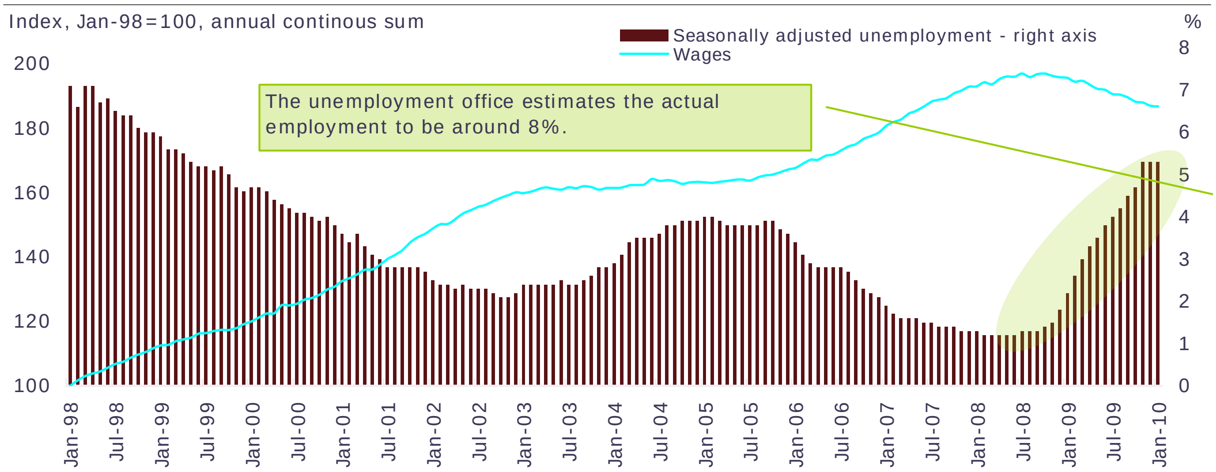
Source: Statistics Faroe Islands and TAKS

Loans (net), wages and household consumption, Jan-98 to Jan-10 F-62



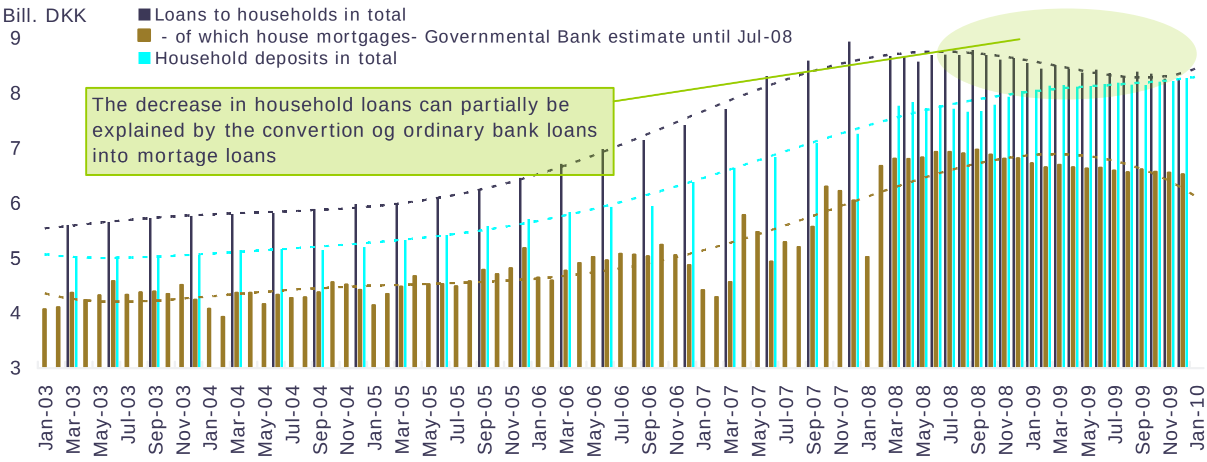
Comment: Statistics from Mar-08 and onwards are from new records; therefore, there is a break in the series
Source: Governmental Bank and Statistics Faroe Islands

Wages and unemployment, Jan-98 to Jan-10 F-63



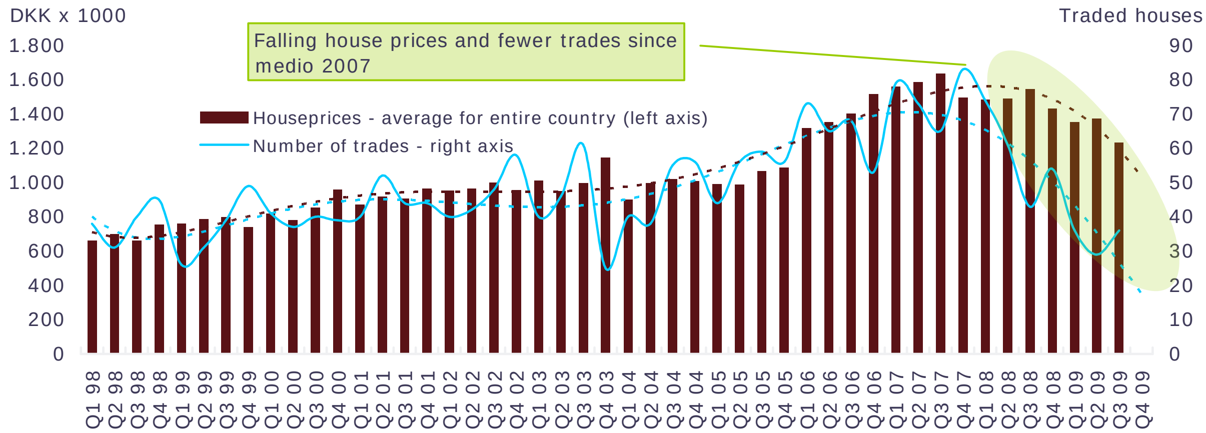
Source: Statistics Faroe Islands

Loans and deposits of households, Jan-03 to Jan-10 F-64



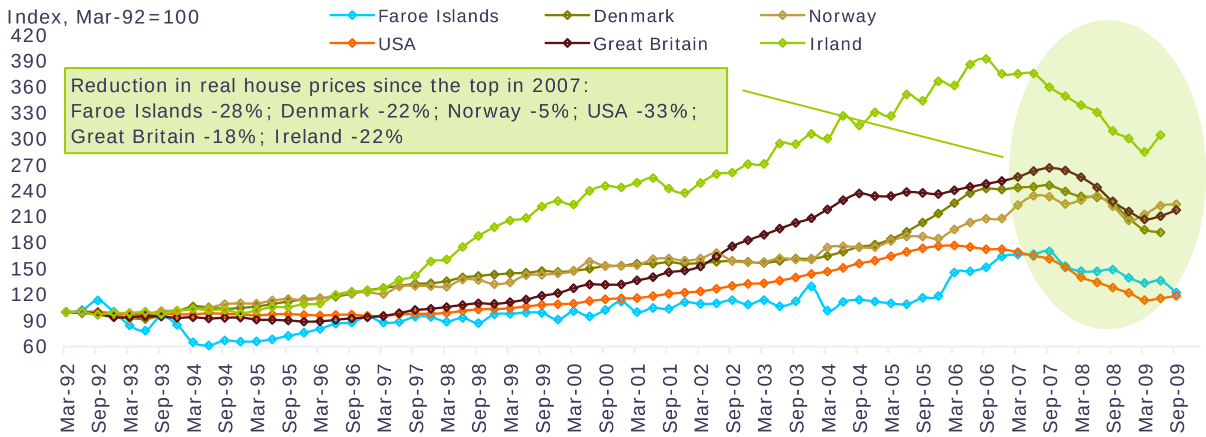
Comment: Staistics from Mar-08 and onwards are from new records; therefore, there is a break in the series
Source: Governmental Bank, TAKS and Eik Banki

House prices and traded houses, Q1-98 til Q4-09 F-65



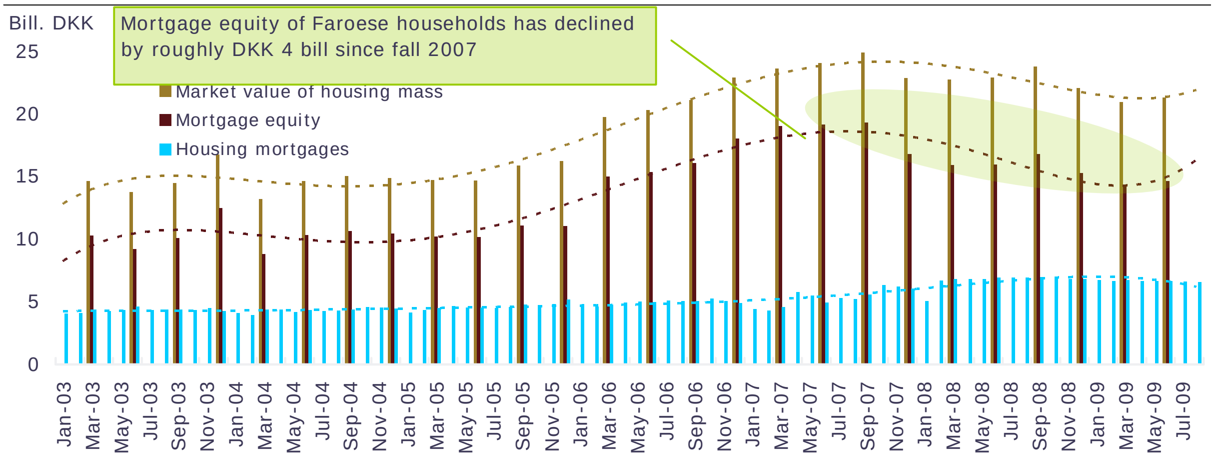
Source: Eik Bank and Statistics Faroe islands

Real house prices in different countries F-66



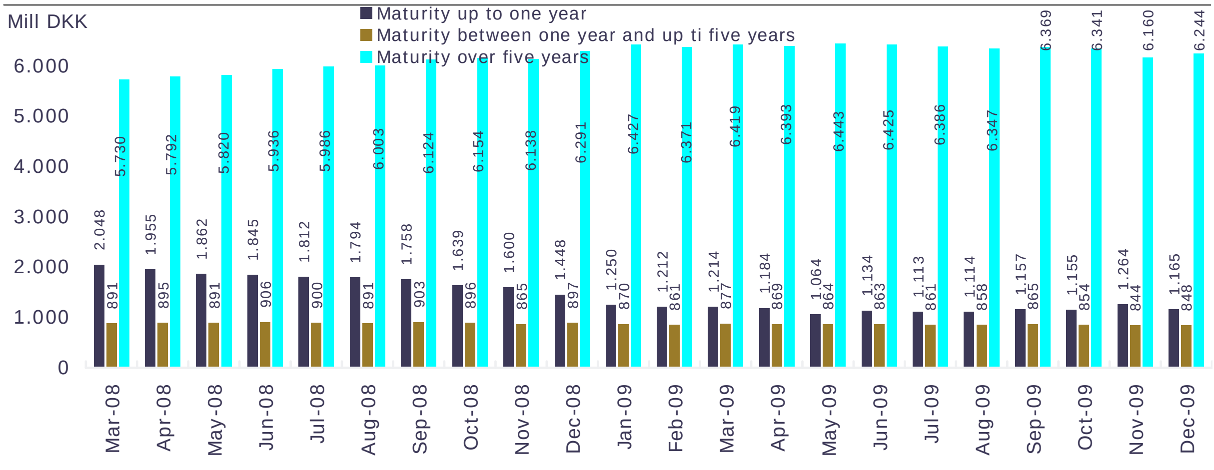
Source: Faroese Statistics, Eik Bank, OECD, Standard & Poor's, Central Statistics Office Ireland, Statistisk Sentralbyrå, Danmarks Statistik

Mortgage equity, Jan-03 til Okt-09 F-67



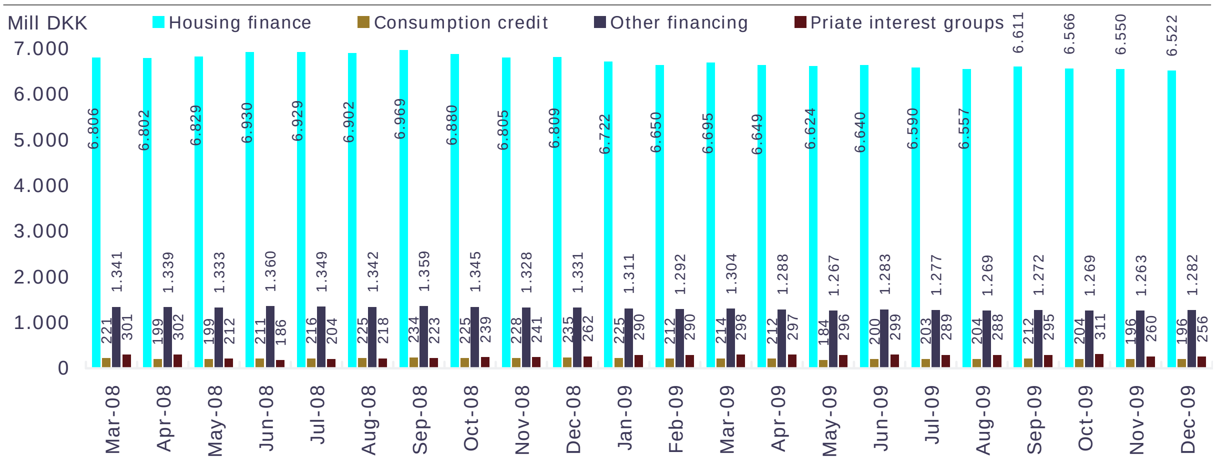
Comment: Statistics for mortgage loans are until Mar-08 the Governmental Bank´s calculations, while following statistics are from new
Source:Governmental Bank, Eik Bank, TAKS

Household borrowing in faroese banks, Mar-08 to Aug-09 F-68



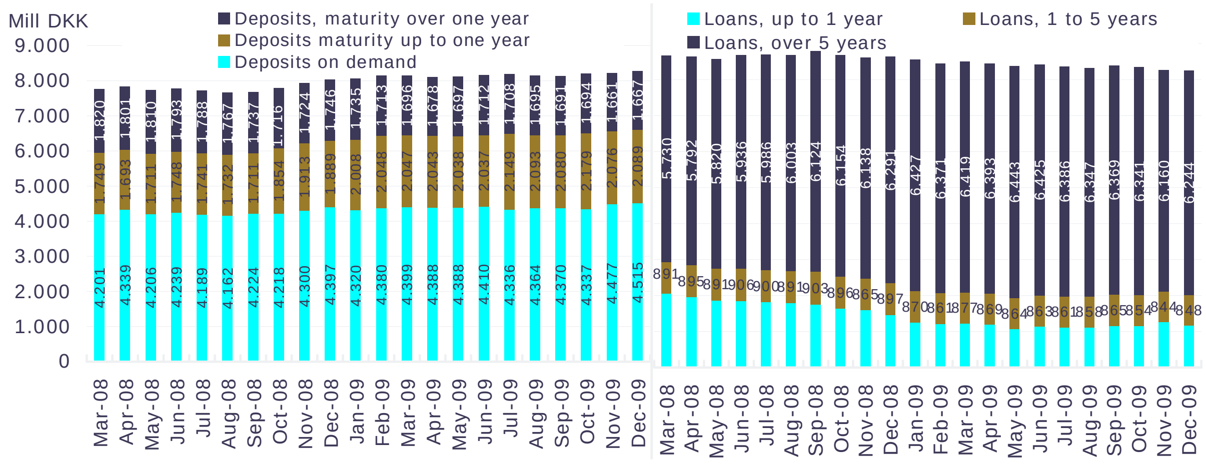
Source: Governmental Bank

Household borrowing in faroese banks, by purpose, Mar-08 to Dec-09 F-69



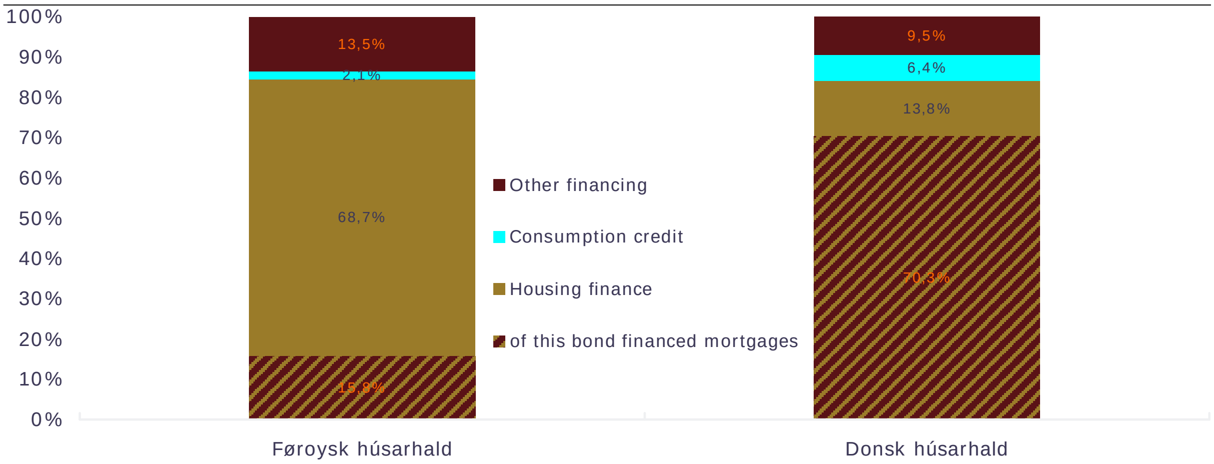
Source: Governmental Bank

Loans and deposits of households in faroese banks, Mar-08 to Dec-09 F-70



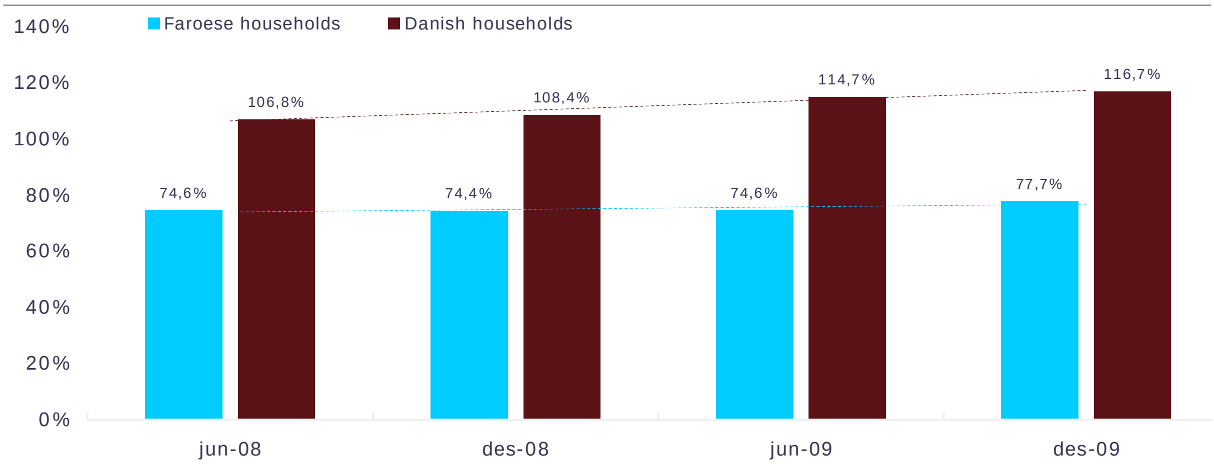
Source: Governmental Bank

Faroese household´s borrowing relative to Danish households, Dec-09 F-71



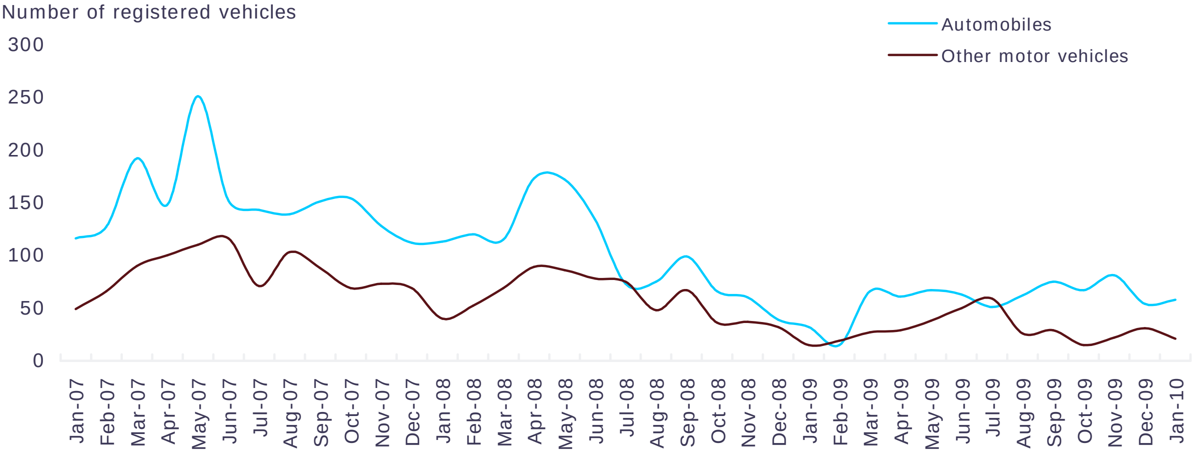
Comment: No satistics currently exist that meassure mortgage financing in the Faroes, but experts estimate it to currently be around 1 bill. D
Kelda: Governmental Bank and Danmarks Statistik

Bank- and mortgage debt relative to GDP in the Faroe Islands and Denmark F-72



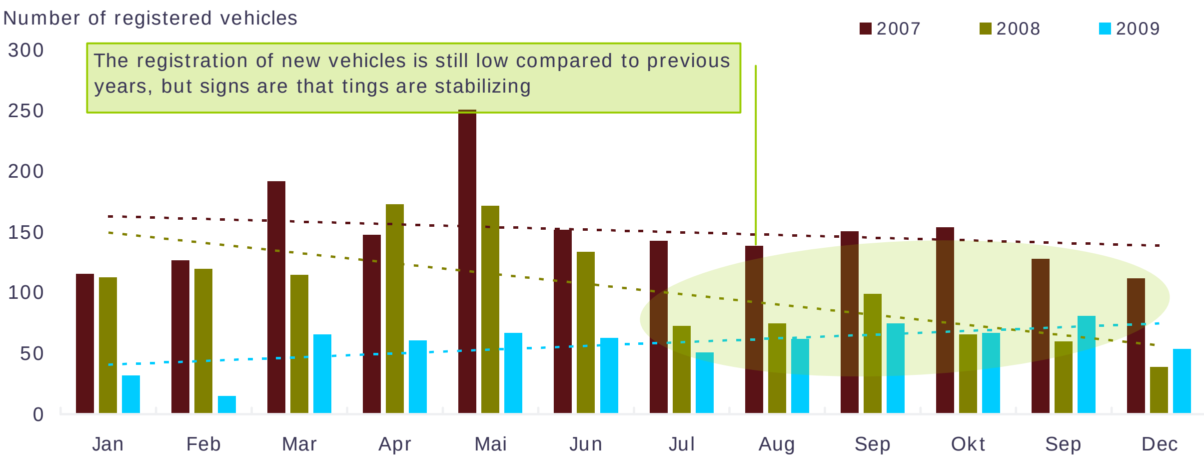
Comment: Debt in Mar-08 and Sep-08 is relative to GDPin 2008 and likewise for 2009-numbers
Source: Governmental Bank and Danmarks Statistik

Registration of new motor vehicles Jan-07 to Jan-10 F-73



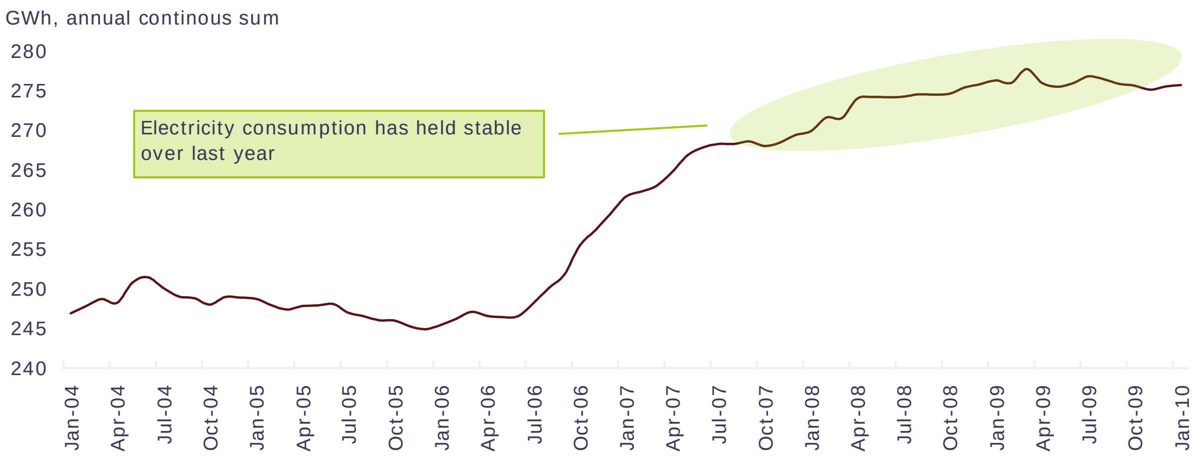
Source: Transportation Office

Registration of new motor vehicles in 2007, 2008 and 2009 F-74



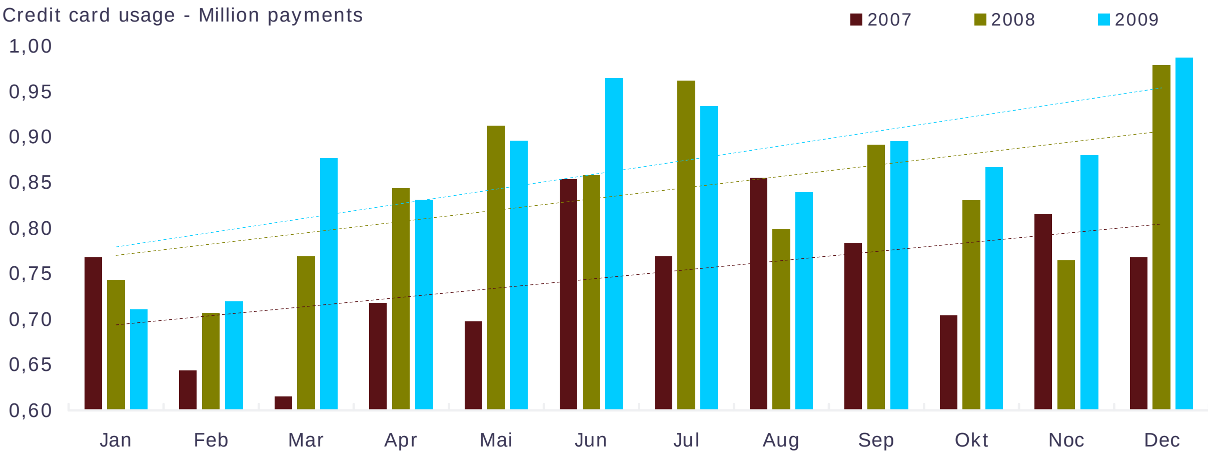
Source: Transportation Office

Electricity consumption, Jan-04 to Jan-10 F-75



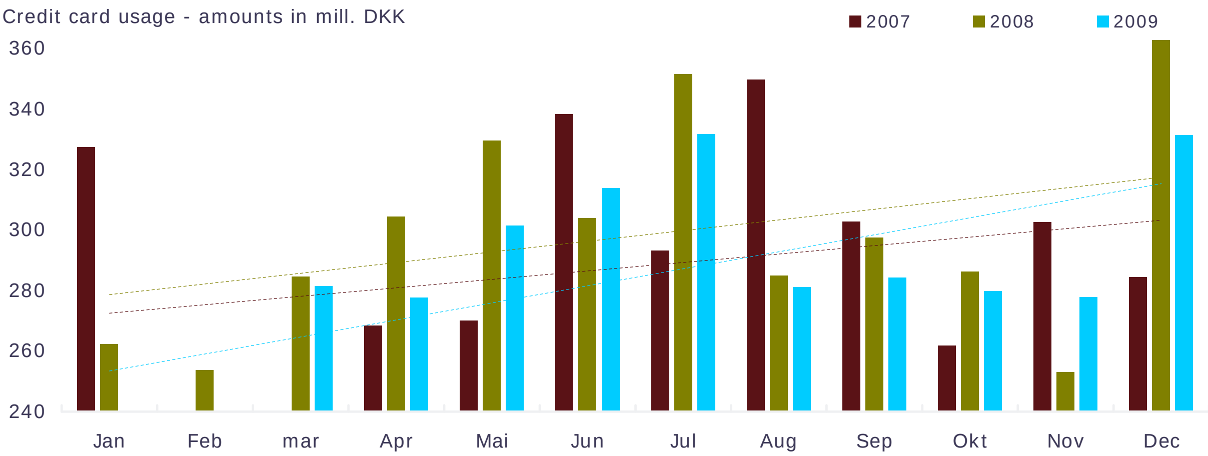
Source: SEV

Credit card usage - number of transactions, Jan-07 to Aug-09 F-76



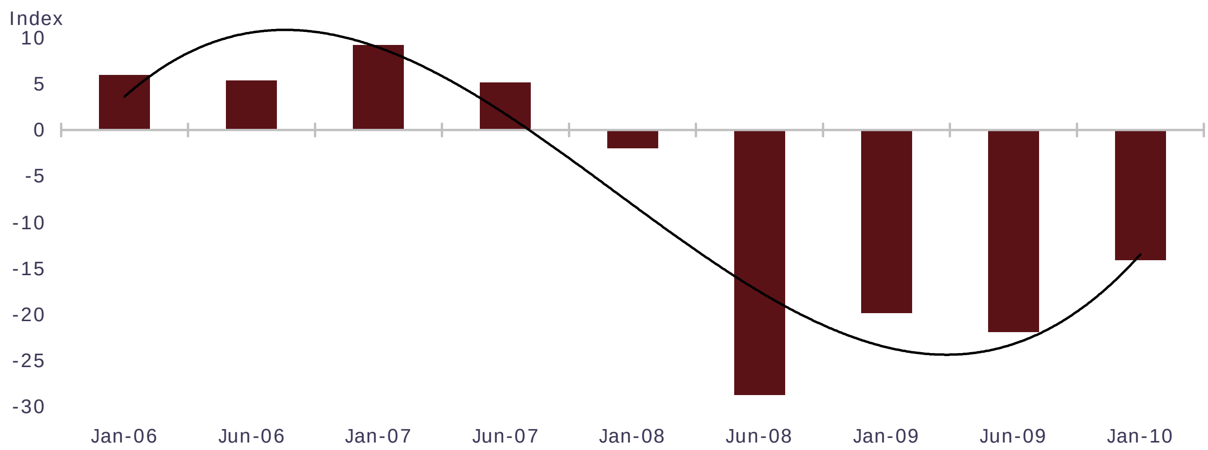
Source: Elektron

Credit card usage - amounts, Jan-07 to Aug-09 F-77



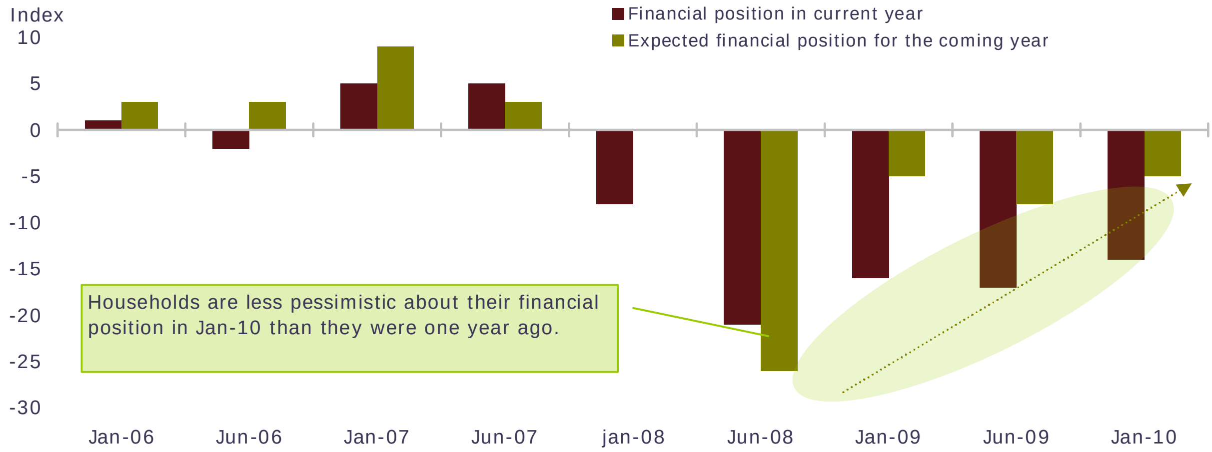
Source: Elektron

Confidence index - aggeregate number for Faroese households (according to themselves), Jan-06 to Jan-10 F-78



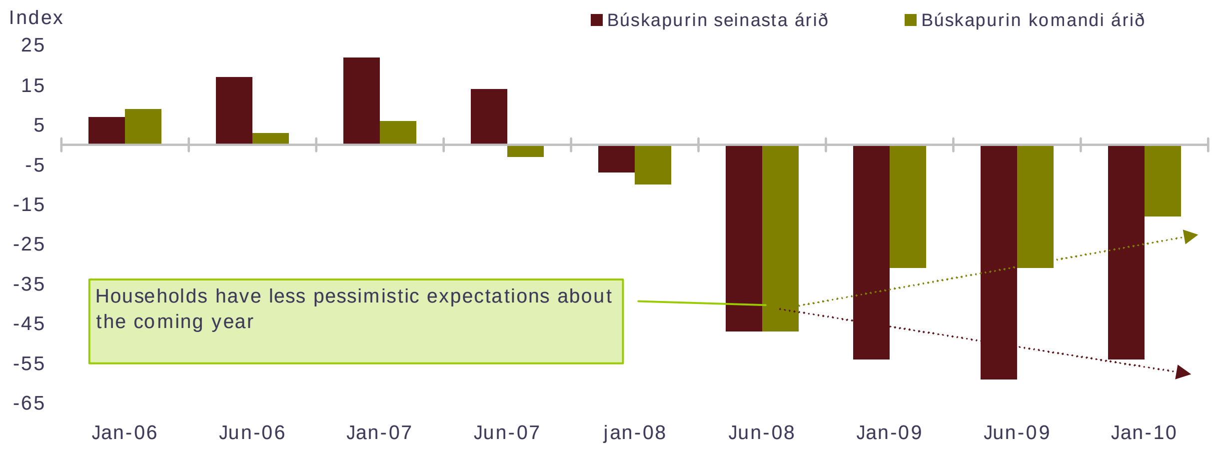
Source: Finance Ministry

Confidence Index - households and their financial position, Jan-06 to Jan-10 F-79



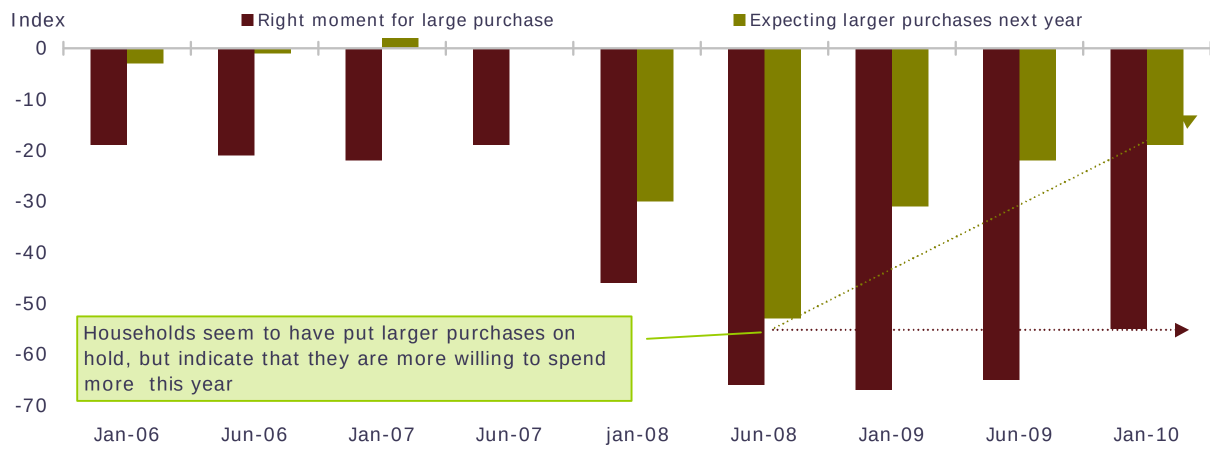
Source: Finance Ministry

Confidence Index - households and their expectations on the current state of economy and their expectations for the coming year, Jan-06 to Jun-10 F-80



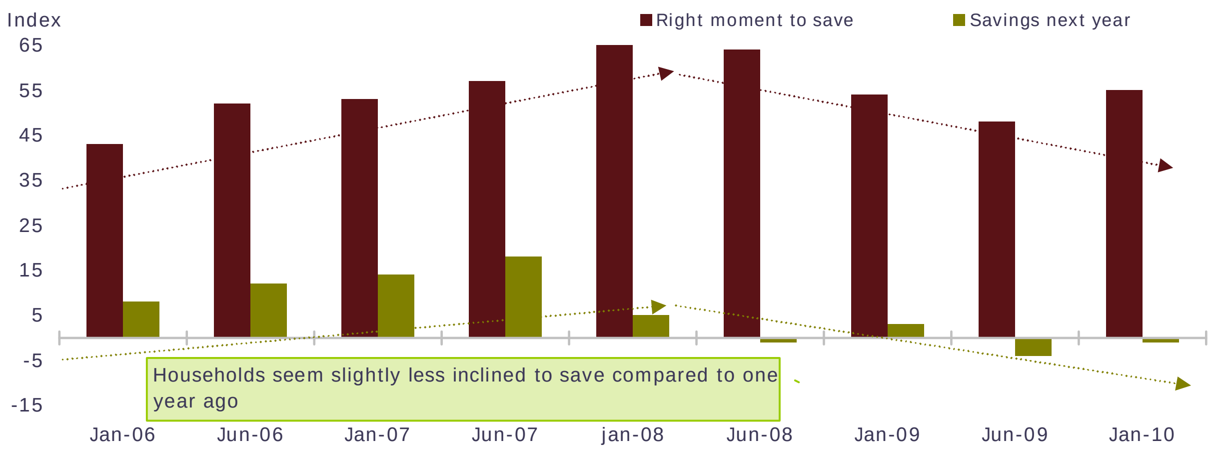
Source: Finance Ministry

Confidence Index - households and their expectations concerning large purchasees, Jan-06 to Jan-10 F-81



Source: Finance Ministry

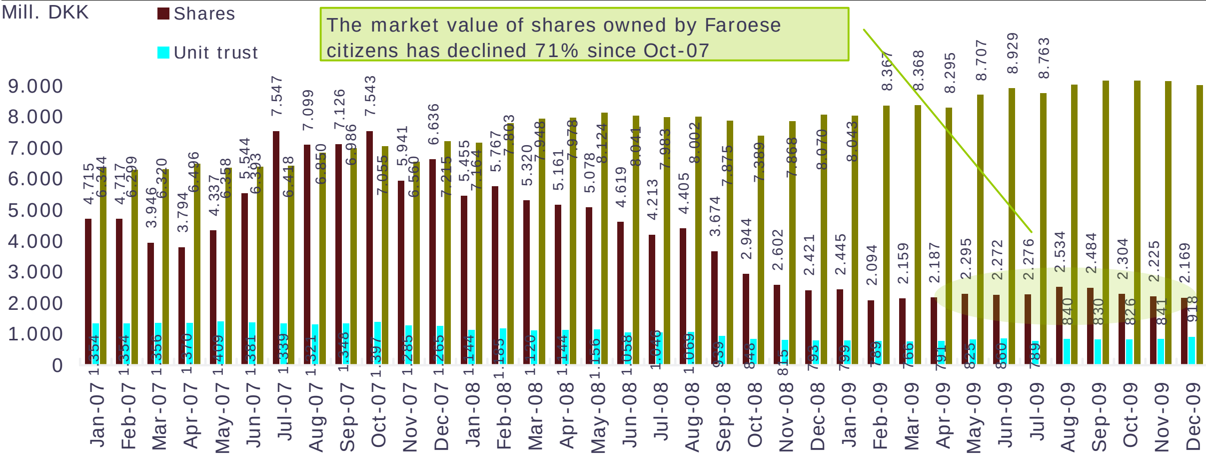
Confidence Index - expectations concerning savings, Jan-06 to Jan-09 F-82



Source: Finance Ministry

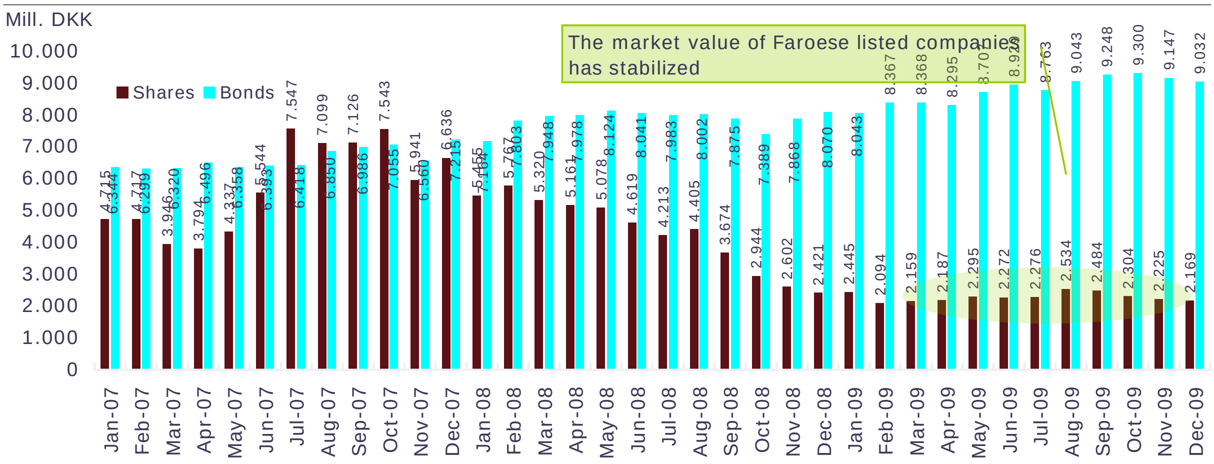
Appendix 6: Securities

Market value of securities owned by Faroese citizens, Jan-07 to Dec-09 F-83



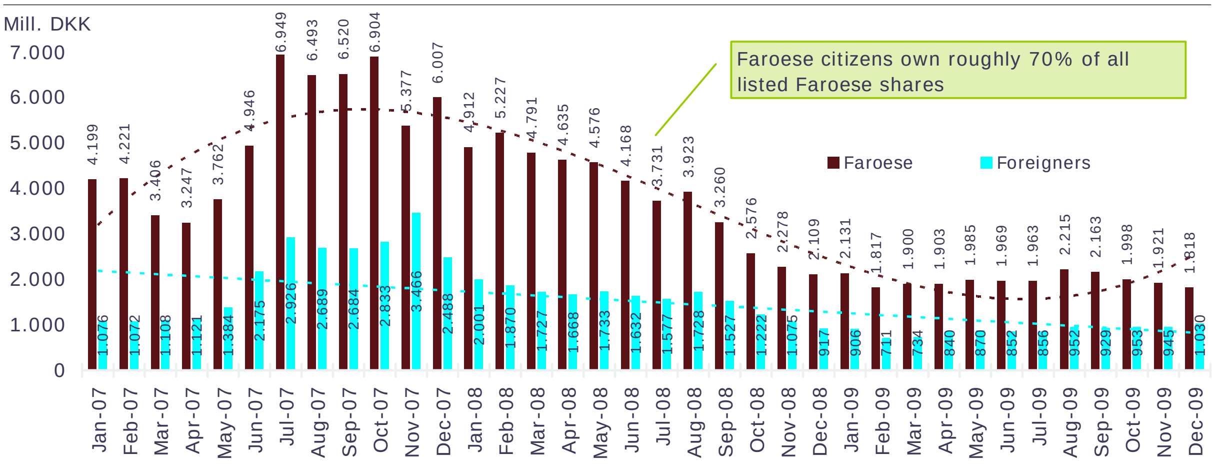
Source: Governmental Bank

Market value of listed Faroese secutities, Jan-07 to Dec-09 F-84



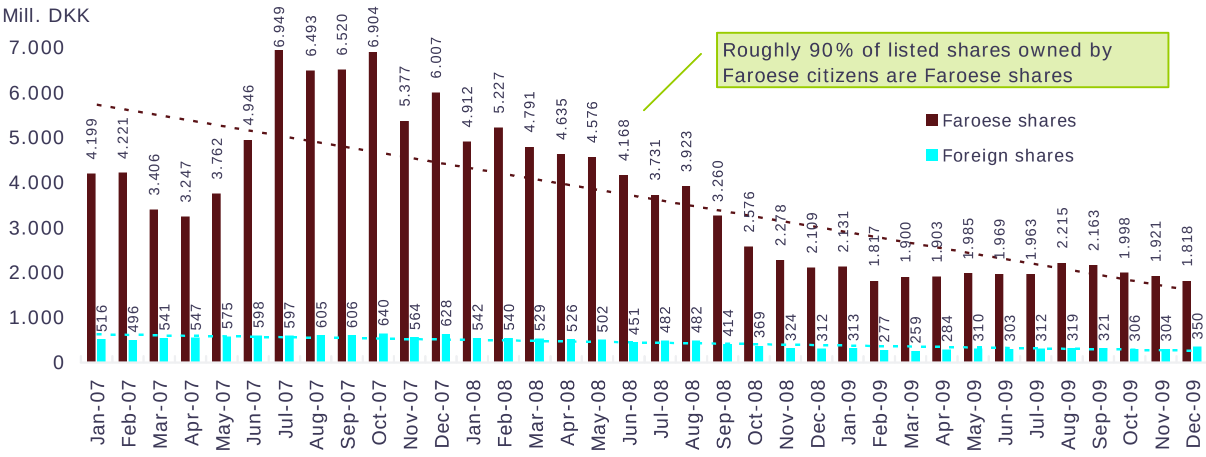
Source: Governmental Bank

Distribution of Faroese shares (market value) by owner, Jan-07 to Dec-09 F-85



Source: Governmental Bank

Dist. of shares owned by Far. cit, by issuer country, Jan-07 to Dec-09 F-86



Source: Governmental Bank

Landsbanki Føroya

GOVERNMENTAL BANK

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