

News release

The Icelandic Government, acting on a proposal from the Minister of Social Affairs, has resolved to submit to the Icelandic parliament *Althingi* a bill of legislation amending the Act on Housing Affairs, No. 44/1998, as subsequently amended

The objective of the bill is to ensure more favourable housing mortgages for Icelanders through the Housing Finance Fund (HFF), by obtaining less expensive financing on the general loan market. This objective is to be achieved by restructuring HFF's bond issuance, replacing housing bonds and housing authority bonds with new HFF bonds. This restructuring will make financing more cost-efficient, remove the main disadvantages of the current issuance and create the basis for reliable price formation on the securities market.

The changes are aimed at improving the situation for HFF borrowers, both by lowering the cost of financing and by reducing risk in connection with real estate transactions. The system changes proposed in this bill will lead to payment of cash mortgages, thus eliminating the impact of discounts when selling securities. The bill proposes to link the interest rates on mortgages to currently market yields.

It is aimed at increasing the liquidity of HFF bonds on the securities market, which will likely result in lowering investors' yield demands. If this proves to be the case, HFF will be able to lower its mortgage rates to borrowers. The expectation is thus that the above-mentioned changes will result in lower financing costs for borrowers and reduce HFF's handling costs.

The Bill's main innovations include:

- Instead of HFF providing borrowers with market securities in return for a real estate mortgage, as is the case under the current housing bond system, HFF bonds will be auctioned on the market and the borrowers paid the value of the mortgage in cash. The terms of the mortgage will be based on HFF's total financing cost, i.e. interest terms will be determined by the outcome of auctions of HFF bonds and financing terms resulting from prepayment of HFF mortgages. The interest rate will be based on a weighted mean of these two factors. HFF will add a premium to this, as is currently the case for mortgages granted by HFF and sales of housing authority bonds. Under the new arrangements, interest rates on HFF mortgages will be adjusted following each auction and may as a result vary through time.
- The Bill proposes that instead of issuing two types of securities, as has been the case for just over a decade now, i.e. housing bonds and housing authority bonds, HFF will only issue one type of security, *HFF bonds*.
- HFF bonds are envisaged as inflation-linked annuity bonds with four instalments annually. Annuity mortgages are a common form of bond everywhere in the world, which should thus be compatible with all systems used today in securities transactions.

HFF bonds are to be issued in only a few series, which will be open for their entire period of maturity; they will thus be large series, marketable on the international market.

- A new *ÍLS mortgage* will replace the current real estate mortgage exchanged for housing bonds.
- To accelerate the introduction and marketability of HFF bonds on the market, owners of housing bonds and housing authority bonds will be offered to switch them for HFF bonds and switch auctions will be held. Work is currently underway on the arrangements for these switch auctions, which will be announced later. These switches will be based on market terms, with regard to the issuer's risk. HFF's Board of Directors intends to enlist the services of a specialist to assist in implementing the switches.
- HFF will no longer hold a call option for housing bonds, in response to mortgage pre-payments, as part of the policy of making the HFF bonds more attractive to investors.

The changes in loans are expected to take place from July the 1st 2004 and that the HFF bonds will be issued after April the 15th 2004.

The objective of the Bill is to strengthen and further the purpose of the Act on Housing Affairs. This Act is intended to contribute, through provision of mortgages and emphases in housing affairs, to ensuring security and equality in housing matters, and to make use of funding especially to increase the possibility for individuals to acquire or rent housing on manageable terms.

The Icelandic Bill of Legislation is included, together with an English translation.

Ministry of Social Affairs
Mars the 9th 2004