

Stapi Pension Fund

Financial statement 2019

Stapi lífeyrissjóður
Strandgötu 3
600 Akureyri
kt. 601092-2559

Independent auditors report

To the Board of Directors and members of Stapi Pension Fund

Opinion

We have audited the enclosed annual accounts of Stapi Pension Fund for the year 2019. The annual accounts contain an overview of developments in net assets regarding pension payments, a balance sheet, a cash flow statement, a statement of actuarial position, information on main accounting policies and other explanatory notes.

In our opinion, the accompanying financial statements give a true and fair view of the financial position of Stapi Pension Fund as at 31 December 2019, and its financial performance and its cash flows for the year then ended in accordance with the Icelandic Financial Statement Act and the Regulation on the Annual Financial Statements of Pension Funds.

Basis for the opinion

The audit was carried out in accordance with international auditing standards. Our responsibilities according to those standards are outlined in further detail in the section below on auditors' responsibilities. We are independent of Stapi Pension Fund as stipulated by the code of practice applicable to auditors in Iceland and we have complied with the provisions of the code. We feel that we have, during the auditing process, acquired sufficient and relevant documentation on which to base our opinion.

Other sources of information

The fund's Board of Directors and Managing Director are responsible for other sources of information which include the Report by the Board of Directors and Declaration on Management Practices.

Our opinion with regards to the annual accounts does not extend to other sources of information and we neither draw conclusions nor provide confirmation as to the content of these, with the exception of the confirmation presented below, regarding the Board of Directors' Report.

In relation to our auditing, we are responsible for the reading of other sources of information indicated above and examining whether these significantly disagree with the annual accounts or the knowledge we have acquired during the auditing process or contain significant errors in other respects. If we conclude, on the basis of work we have carried out, that other sources of information contain significant errors, we are obliged to report such knowledge. In this respect, we have nothing to report.

In accordance with the provisions of Paragraph 2, Article 104 of Act No. 3/2006 on Annual Accounts we confirm that, to the best of our knowledge, the Report by the Board of Directors enclosed with these annual accounts provides the information required according to the Act on Annual Accounts, in addition to explanations presented in the notes section of the accounts.

Responsibilities of the Board of Directors and MD regarding annual accounts

The Board of Directors and Managing Director are responsible for the implementation and presentation of the annual accounts in accordance with the Act on Annual Accounts. Furthermore, the Board of Directors and MD assume responsibility for the necessary internal controls in relation to the implementation and presentation of the annual accounts, in such a manner that they contain no significant flaws, whether through fraud or error.

During the compilation of the annual accounts, the Board of Directors and MD are responsible for assessing the situation of Stapi Pension Fund as a going concern. If applicable, the Board of Directors and MD shall present relevant comments as to operational feasibility and as to why the decision was taken to apply the criterion of operational feasibility in the compilation and presentation of the annual accounts, unless the Board of Directors and MD have decided to dissolve the fund and wind up its operation or have no other realistic options.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objective is to give reasonable assurance that the annual accounts are free of significant flaws, whether due to fraud or error and to issue an endorsement comprising our opinion.

Reasonable assurance, however, is no guarantee that an audit carried out in accordance with international auditing standards will reveal all significant errors which may exist. Flaws or errors may be caused inadvertently or through fraudulence and are regarded as significant if they can, separately or collectively, influence the financial decision-making of the users of the annual accounts,

Our auditing complies with international auditing standards and is based on professional judgment and an approach of professional scepticism in the auditing process. In addition, we carry out the following operations:

- We analyse and assess the risk of a significant flaw in the annual accounts, whether this be by mistake or fraud; we design and implement auditing measures to respond to such risks and acquire sufficient and relevant auditing evidence on which to base our opinion. The risk of failing to spot a significant flaw due to fraud is greater than that of not spotting an error by mistake, since fraud may involve conspiracy, forgery, obfuscated presentation of annual accounts, items being deliberately omitted or internal controls bypassed.
- We familiarise ourselves with internal controls relating to auditing, for the purpose of designing suitable auditing methods, but not for the purpose of presenting an opinion on the effectiveness of internal controls.
- We assess whether the accounting methods used, and related notes, are appropriate and whether management's assessment of accounting practices is realistic.
- We draw conclusions regarding management's use of the criterion of "going concern" and we assess, on the basis of our auditing, whether there is any significant doubt as to operational feasibility and whether conditions exist which could cause serious reservations with regard to the fund's ability to continue as a going concern. If we feel there is serious uncertainty as to operational feasibility it is our duty to draw special attention to relevant notes in our endorsement of the annual accounts. Should such notes be unsatisfactory, we must withhold unreserved endorsement. Nevertheless, future events or circumstances may cause uncertainty as to the fund's situation as a going concern.
- We assess whether the annual accounts provide a clear picture of underlying business transactions and events; we assess the presentation, structure and content of the annual accounts, including attached notes, with regard to clarity and coherence.

We are obliged to inform the Board of Directors and the auditing committee on the estimated scope and timing of the audit, among other things, as well as important points brought up during the auditing process, including serious shortcomings with regard to internal controls revealed by the audit, if applicable.

We have, furthermore, declared to the Board of Directors and the auditing committee that we have complied with the code of practice regarding independence and we have provided them with information on connections or other matters which could possibly affect our independence and, where applicable, what precautions we have taken to ensure our independence.

Akureyri, 26 March 2020

Deloitte ehf.

Aðalsteinn Sigurðsson
State Authorized Public Accountant

Hólmgrímur Bjarnason
State Authorized Public Accountant

Report by the Board of Directors

Stapi Pension Fund operates in accordance with the Pension Act, No. 129/1997, on mandatory insurance of pension rights and on activities of pension funds. The fund's operation is authorised by the Ministry of Finance in compliance with Article 52 of the aforementioned Act. The objective of the fund is to guarantee its members, as well as their surviving spouses and children, a pension according to the fund's Articles of Association. The fund comprises three separate sections, a mandatory division, a voluntary division and a specially designated voluntary division.

Main items of information relating to operating year, anticipated evolution of the fund and a declaration on management practice

Return on Stapi fund's assets in 2019 was the best in the fund's history in its current form, or a real return of 10%. All asset classes generated a positive return contribution during the year. The fund's target is a real return of 3.5%, whereas average real return of the past 10 years comes to 4.1%.

The fund's actuarial position strengthened during the year and is currently negative by 0.4%, having been negative by 1.8% at the end of 2018. The assessment of the fund's liabilities is now based on life expectancies during the period 2014-2018, whereas the previous assessment was based on the years 2010-2014. Altered mathematical postulates exercise a negative impact of 0.6% on the Fund's actuarial position.

The Board of Directors anticipates that the fund's operation will be along similar lines in the next few years. Since the end of the financial year, share prices in Stapi's portfolios have fallen significantly in the wake of the Covid-19 virus. The fund's low risk profile, however, and a wide distribution of assets has reduced this impact on the portfolio as a whole. Unresolved entitlements within Stapi's entitlement system have for the most part moved in step with changes in the fund's asset index. Thus altered asset prices will affect the fund's ability to match its liabilities to a lesser extent than otherwise would have been the case. The fund's return on investments is anticipated to cover future growth of liabilities and the fund's system of entitlements is expected to ensure a balanced outcome in this respect.

The fund's Board of Directors has passed a special declaration, published with this Annual Account, with regard to administrative practice. According to the Law on Annual Accounts, entities relating to public interest shall supply the necessary information to assess development, scope and impact with regard to matters relating to the environment, social aspects and human resources, human rights policies, and the prevention of corruption and bribery. In addition, a brief business model description is to be supplied etc. The company's strategy and success in these matters is outlined in Appendix I to the annual account.

Fund membership and contributions

In the year 2019 a total of 21,939 fund members working for 3,287 employers paid contributions to the fund's mandatory division. The year's total contributions amounted to ISK 12,572 million. Contributions to the mandatory division were ISK 12,162 million, increasing by 7.5% from the previous year and contributions to the voluntary division grew by 8.3% compared to the previous year, totalling ISK 301 million. Finally, the year's contributions to the specially designed voluntary division were ISK 1.9 million. The number of active members who generally make regular monthly contributions to the fund was 15,086 in the mandatory division, 784 in the voluntary division and 346 in the specially designated voluntary division.

Pension disbursements

The mandatory division's total pension disbursements during the year amounted to ISK 6,408 million, rising by 12.9% from the previous year. Individual retirement pension plans were ISK 4,540 million, disability benefits amounted to ISK 1,566 million, spouse pensions were ISK 254 million and child benefits were ISK 48 million. Disbursements from the voluntary division amounted to a total of ISK 174 million, and ISK 1 million from the specially designated voluntary division. The total number of pensioners at end of year was 10,261

Operating expenses

The fund's operating expenses in 2019 amounted to ISK 429 million. Operating expenses as a proportion of assets came to 0.2%. Full-time equivalent units were 18.5 during the year, and total payroll expenses were ISK 217 million.

Assets and return on investments

The mandatory division's net assets available for benefits were ISK 249,521 million, increasing by 16% compared to the previous year. The division's nominal return on investments was positive by 12.9% and real return amounted to 10%. The net assets of the voluntary division amounted to ISK 6,422 million, increasing by 16.8% from the previous year. The voluntary division offers three investment options: the deposit portfolio, the conservative portfolio and the dynamic portfolio; the net real return of those portfolios, respectively, totalled 0.2%, 11.3% and 14.9% during the year. The net assets of the specially designated voluntary division were ISK 190 million at the end of year.

Actuarial position

An actuarial audit has been carried out with respect to the fund's mandatory division at end of year 2019. The year's actuarial performance was positive by ISK 5,169 million, and the fund's actuarial position at end of year was negative by ISK 1,636 million, or 0.4% of the fund's liabilities.

The Board of Directors and the CEO of Stapi Pension Fund hereby ratify and endorse with their signatures the fund's annual accounts for the year 2019.

Akureyri, 26 March 2020

Board of Directors

CEO of Stapi Pension Fund

Statement of changes in net assets for pension payments in 2019

	Expl.	2019	2018
Contributions			
Fund members' contributions		3,295,740	3,268,743
Employers' contributions		9,276,608	8,401,548
Transfer of entitlements and repayments		(100,045)	(140,596)
		<u>12,472,303</u>	<u>11,529,695</u>
Special additional contributions	3	614,699	524,392
		<u>13,087,002</u>	<u>12,054,086</u>
Pensions			
Total pensions	4	6,583,981	5,888,456
Contribution to vocational rehabilitation fund		78,753	74,932
Direct costs relating to disability pensions	5	4,401	4,623
Retirement pensions from Institute of Social Security		(1,005)	(1,120)
		<u>6,666,131</u>	<u>5,966,891</u>
Net investment income			
Net income from holdings in companies and funds	6	19,249,834	2,677,495
Net income from bonds	7	10,402,323	7,218,579
Net income from investments in residential housing		(760)	64,239
Interest income from tied bank deposits		45,211	61,011
Interest income from cash in hand		215,459	271,848
Interest income from contributions and other claims		77,117	33,874
Other investment income		31,340	9,712
Cost of investments	8	(98,817)	(94,337)
		<u>29,921,706</u>	<u>10,242,421</u>
Operating expenses			
Office and administration expenses	9	428,662	456,349
Other income (expenses)	12	(487,364)	(17,085)
Change in net assets for pension payments		<u>35,426,552</u>	<u>15,856,183</u>
Net assets from previous year		220,706,669	204,850,486
Net assets for pension payments at end of year		<u><u>256,133,221</u></u>	<u><u>220,706,669</u></u>

Balance sheet 31 December 2019

	Expl.	31.12.2019	31.12.2018
Assets			
Investments			
Holdings in companies and funds	10	121,710,528	99,202,253
Bonds	11	127,804,622	116,151,923
Tied bank deposits		806,862	970,887
Investments in residential housing		0	24,714
		<u>250,322,011</u>	<u>216,349,776</u>
Claims			
Claims against employers		1,351,675	1,368,235
Other claims		31,856	164,860
		<u>1,383,531</u>	<u>1,533,095</u>
Various assets			
Property, plant and equipment	14	289,884	180,920
Cash in hand		<u>4,457,132</u>	<u>2,795,776</u>
Total assets		<u>256,452,559</u>	<u>220,859,567</u>
Liabilities			
Trade payables			
Other liabilities		319,338	152,898
Total liabilities		<u>319,338</u>	<u>152,898</u>
Net assets for pension payments		<u>256,133,221</u>	<u>220,706,669</u>
Off-balance sheet liabilities	16		

Cash flow 2019

	2019	2018
Incoming payments		
Contributions	12,488,862	11,344,531
Paid-in interest on cash in hand and claims	159,497	166,491
Other pay-ins	614,699	524,392
	13,263,058	12,035,414
Payouts		
Pensions	6,583,981	5,888,456
Operating expenses	424,426	452,113
Investment í tangible assets	113,200	0
Other payouts	110,613	145,484
	7,232,220	6,486,053
Increase in disposable cash for investment	6,030,838	5,549,360
Investing activities		
Proceeds from holdings in companies and funds	815,827	671,432
Purchased holdings in companies and funds	(33,112,587)	(34,964,029)
Proceeds from sold holdings in companies and funds	29,030,400	26,897,684
Principal and interest instalments on bonds	14,866,594	8,299,398
Purchased bonds	(24,304,105)	(35,950,305)
Proceeds from sale of bonds	7,961,414	27,392,177
Reimbursed tied deposits	212,756	238,856
Purchased residential housing	(34,500)	(42,112)
Proceeds from sold residential housing	62,400	1,139,297
Paid income from residential housing operations	3,186	89,033
Cost of residential housing	(3,947)	(24,794)
	(4,502,561)	(6,253,363)
Increase (decrease) of cash and cash equivalents	1,528,277	(704,003)
Exchange difference of cash and cash equivalents	133,079	139,231
Cash in hand at beginning of year	2,795,776	3,360,549
Cash in hand at end of year	4,457,132	2,795,776

Financial ratios

	2019	2018	2017	2016	2015
Mandatory division:					
Net assets in excess of liabilities	-0.39%	-1.79%	-0.92%	-1.54%	0.42%
Net assets in excess of accruing liabilities	-0.07%	-0.18%	-1.05%	-3.18%	-0.62%
Net real return *).....	9.98%	1.46%	5.21%	-0.13%	9.18%
Average of net real return during the past 5 years *).....	5.06%	4.13%	3.99%	3.76%	4.00%
Average of net real return during the past 10 years *).....	4.14%	2.73%	1.22%	0.62%	1.35%
Proportional allocation of investments:					
Listed ownership interests in companies and funds	37.9%	35.4%	34.2%	34.8%	35.1%
Listed bonds	45.1%	49.3%	50.5%	51.1%	49.4%
Listed ownership interests in companies and funds	11.1%	10.5%	10.7%	10.3%	12.1%
Unlisted bonds	6.3%	4.4%	3.6%	3.0%	2.1%
Tied bank deposits	0.3%	0.4%	0.6%	0.8%	1.3%
Investments in residential housing	0.0%	0.0%	0.5%	0.0%	0.0%
Proportional division of investments according to currencies					
Assets in Icelandic kronur ISK	68%	71%	74%	76%	75%
Assets in foreign currencies	32%	29%	26%	24%	25%
Number of active fund members:	15,200	15,086	14,486	13,903	13,348
Number of fund members at end of year:	91,086	89,433	87,292	85,711	87,446
Number of pensioners:	10,261	9,620	9,059	8,559	8,094
Proportional division of pensions:					
Retirement pensions	70.8%	70.6%	68.9%	67.4%	65.6%
Disability pensions	24.4%	24.4%	25.7%	26.9%	28.4%
Spouse pensions	4.0%	4.3%	4.6%	4.7%	4.9%
Child benefits	0.7%	0.7%	0.8%	0.9%	1.0%
Full position equivalents:	18.3	18.3	15.0	14.0	13.5
Total contributions (at constant prices)	12,767,235	11,831,750	10,269,519	9,129,960	8,335,233
Total pensions (at constant prices)	6,490,615	5,754,823	5,400,054	5,094,579	4,876,149
Total net investment income (at constant prices) *)	28,518,417	10,056,488	13,760,819	3,950,163	19,381,995
Office and administrative costs (at constant prices)	397,833	428,923	378,772	318,479	280,499
Increase (decrease) of net assets (at constant prices)	34,397,203	15,704,491	18,251,512	7,667,066	22,560,581
Pension burden	50.8%	48.6%	52.6%	55.8%	58.5%
Office and administrative costs (total) as a % of contributions	3.1%	3.6%	3.7%	3.5%	3.4%
Net investment income as a % of mean asset position *)	13.1%	5.0%	6.9%	2.1%	10.9%
Office and administrative costs as a % of mean asset position	0.17%	0.20%	0.19%	0.17%	0.16%

*) Financial ratios, investment income and asset position have been recalculated in accordance with new auditing practice. Net real return is calculated from net investment income less operating costs and other expenses. When calculating net investment income as a percentage of mean asset position, other expenses have been subtracted from investment income. Constant prices are based on changes in the consumer price index.

Financial ratios

	2019	2018	2017	2016	2015
Voluntary division:					
Net real return - Deposit portfolio.....	0.20%	-0.35%	2.44%	2.55%	2.69%
Net real return - Conservative portfolio.....	11.27%	-0.19%	6.15%	1.33%	7.87%
Net real return - Dynamic portfolio.....	14.93%	-0.72%	5.34%	-0.20%	8.05%
Mean net real return of past 5 years - Deposit portfolio.....	1.50%	2.03%	2.67%	2.68%	2.75%
Mean net real return of past 5 years - Conservative portfolio.....	5.20%	3.93%	4.85%	4.44%	5.07%
Mean net real return of past 5 years - Dynamic portfolio.....	5.33%	3.81%	4.80%	4.95%	4.95%
Mean net real return of past 10 years - Conservative portfolio.....	5.71%	5.68%	6.56%	6.61%	7.71%
Mean net real return of past 10 years - Dynamic portfolio.....	5.32%	5.00%	5.99%	5.99%	7.42%
Voluntary division, all portfolios:					
Proportional allocation of investments					
Listed ownership interests in companies and funds	56.3%	55.4%	48.9%	45.1%	33.2%
Listed bonds	43.7%	44.6%	47.9%	51.3%	62.6%
Tied bank deposits	0.0%	0.0%	3.2%	3.6%	4.2%
Proportional division of investments according to currencies					
Assets in Icelandic kronur (ISK)	78.4%	78.7%	73.1%	84.2%	78.3%
Assets in foreign currencies	21.6%	21.3%	26.9%	15.8%	21.7%
Net investment income as a % of mean asset position	15.2%	3.1%	7.4%	3.0%	9.7%
Office and administrative costs as a % of mean asset position	0.5%	0.5%	0.5%	0.5%	0.5%