

Faroese economy grows despite high global uncertainty

The Faroese economy continues to be characterised by pressure on the labour market and rising house prices. The high economic activity has also been reflected in increasing lending growth, with a particularly strong increase in lending corporates. However, the economy has slowed after a few years of strong growth, driven mainly by the development of the fishing and aquaculture industries. Exports are sensitive to global conditions, and lower fishing quotas are on the horizon. This creates a high level of uncertainty for a small, open and relatively undiversified economy like the Faroe Islands. Economic policy should focus on increasing the economy's resilience.

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The economic boom continues, but at a slower pace for the labour market

Several years of economic boom have led to high employment and virtually no unemployment. However, the pace of the labour market and the influx of foreign labour have slowed, and falling salmon prices have dampened exports. Going forward, trade policy uncertainty and lower fishing quotas create greater risks to growth.



High profits contribute to support bank resilience

Banks are generally doing well and have built up capital over a number of years. Profits are currently high, which increases banks' resilience. Through 2025, lending growth has picked up, with strong growth in lending to corporates.



Fiscal planning can increase the resilience of the economy

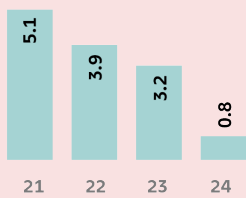
Fiscal policy pushes activity at a time when the economy is already under pressure. A solid fiscal planning framework for the entire public sector could support more appropriate expenditure management.

Why is it important?

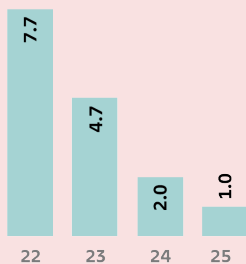
Danmarks Nationalbank is the central bank for the entire Danish Realm. We therefore continuously analyse the development in the Faroese and Greenlandic economies to live up to our purpose of ensuring stable prices and ensuring the best basis for assessing the possible emergence of socio-economic imbalances.

Main chart Facts about the Faroe Islands

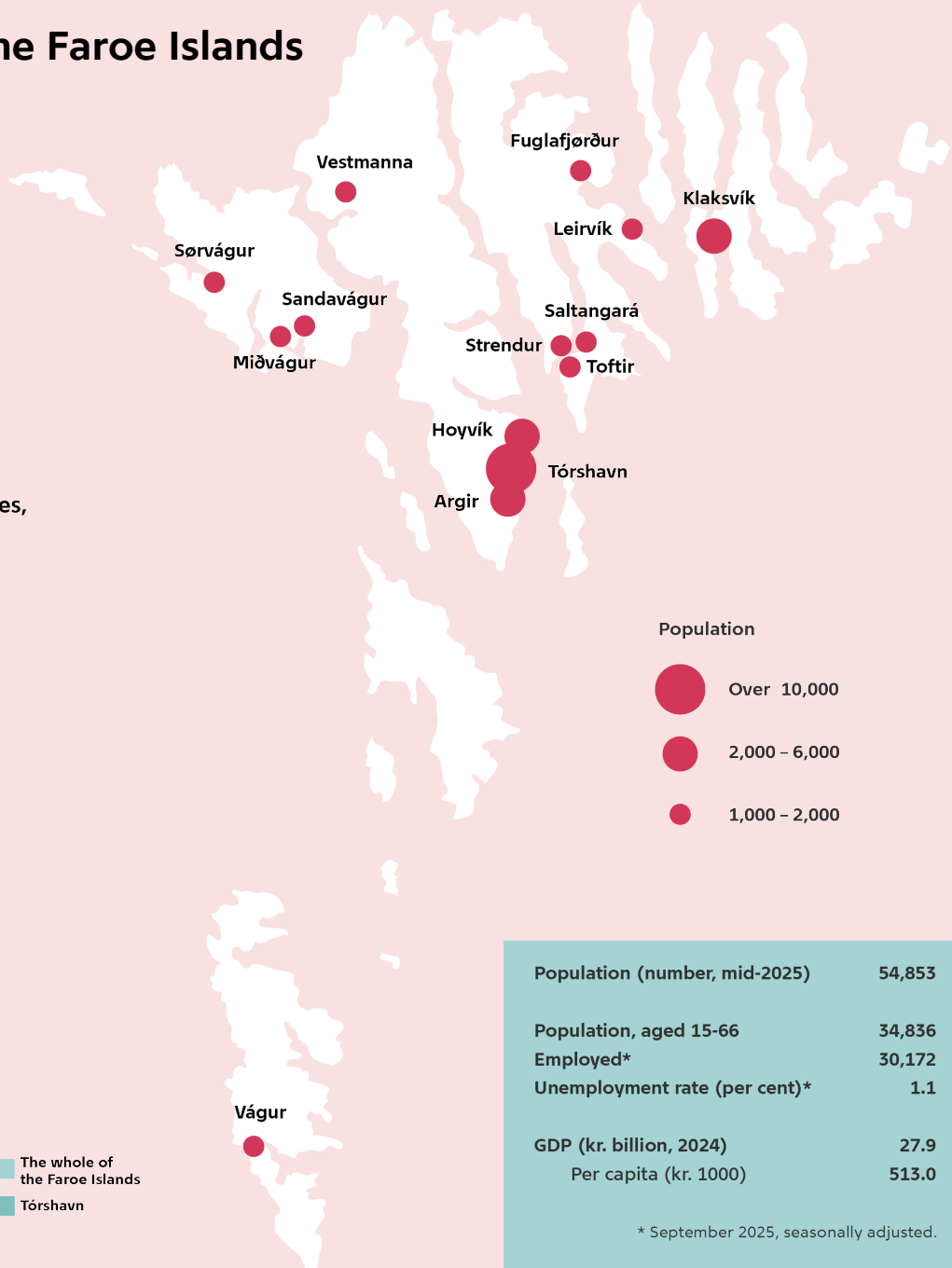
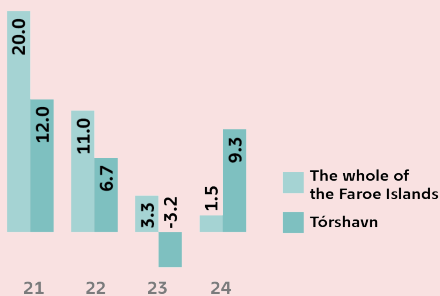
GDP growth, per cent.



Growth in consumer prices, per cent.



Growth in house prices, per cent.



Note: GDP growth is calculated in real terms.
Source: Hagstova Føroya (Statistics Faroe Islands).



Keywords

Faroese economy

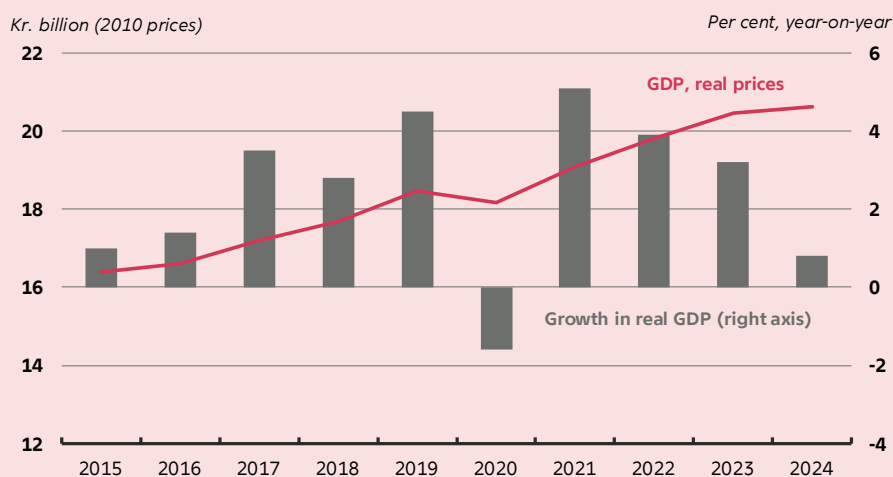
01 The economic boom continues, but at a slower pace than before

The Faroese economy continues to grow with intense pressure on the labour market. Growth in the Faroe Islands has been among the highest in Europe for several years, and the expansion has led to widespread pressure on production capacity. However, there are signs that the pace of the economy has slowed after some years of high growth. In 2024, the Faroese gross domestic product (GDP) increased by 0.8 per cent in real terms, while annual growth was over 3 per cent from 2021 to 2023, see chart 1. Economic growth is also expected to be positive in 2025 and 2026.¹

However, the outlook for the Faroese economy is currently surrounded by great uncertainty. This is mainly due to geopolitical developments, including greater uncertainty related to international trade conditions and tariffs, as well as the prospect of a significant reduction in some fishing quotas in 2026. Changes in global conditions can have a major impact on the growth of the Faroese economy and public finances. So, it is essential to focus on measures to increase the economy's resilience.

CHART 1

Growth in the Faroe Islands has slowed in recent years



Source: Hagstova Føroya.

¹ The Economic Council of the Faroe Islands expects Faroese GDP to increase by 2 per cent in 2025 and 6.1 per cent in 2026 in current prices, see the Faroese Economic Council Autumn Report 2025, *Føroyski Búskapurin, Heystið 2025* ([link](#)).

Limited export growth with large fluctuations in prices and volumes

The Faroe Islands is a small, open economy that relies heavily on trade with the outside world. The export sector is centred on fishing and aquaculture, which account for the majority of goods exports. Therefore, fluctuations in fish prices and the situation in export markets have a major impact on the overall development of the economy.

Exports of fish products include salmon farming, pelagic² and demersal fishing, among others, and their processing. Within the Faroese fishing industry, different sectors are dependent on the fishing method and area, which provides a degree of diversification. Fisheries also benefit from being able to fish in different waters: A number of international agreements have historically ensured that the Faroe Islands and neighbouring countries have been able to fish in each other's waters, thereby spreading risk and contributing to more efficient use of resources.³

In 2025, goods exports have increased slightly, with annual revenues of approximately kr. 13 billion, of which 93 per cent is attributable to exports of fish and fish products, see chart 2. Recently, however, export values have been characterised by large fluctuations in both prices and volumes. This reflects, among other things, that fishing quotas, which set the maximum allowable catch, have been reduced for several fish species.⁴ However, quota reductions and lower global supply have led to higher market prices, for example for cod and mackerel, contributing to higher export values.

The situation is different in the salmon-farming industry. There has been a significant increase in output, while the price of salmon has dropped significantly in 2025 due to increased global supply.⁵ The average export price of Faroese salmon fell by around 37 per cent from January to August 2025, but during the same period, the volume of salmon exported increased by around 23 per cent compared to the previous year. Salmon exports are expected to exceed 100,000 tonnes in 2025, more than doubling since 2011. This reflects the fact that over the past decade, significant investments have been made to expand production capacity.

Trade policy uncertainty and quota reductions create greater risks for exports

The Faroese salmon-farming industry consists of a few large companies that, in recent years, have become increasingly vital to the overall Faroese economy. Today, salmon exports account for almost half of all goods exports, a significant part of which is exported to the US. As a result, Faroese goods exports to the US have increased significantly in recent years and now account for around 12 per cent of total goods exports, see chart 3.

² Pelagic fishing is fishing for fish species that move in schools in the open water. These include herring, mackerel and blue whiting.

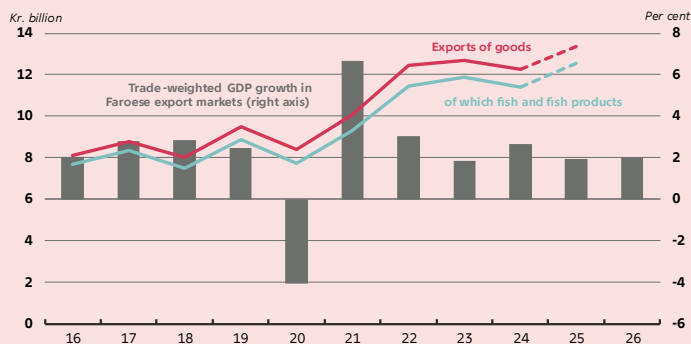
³ The Faroe Islands have fisheries agreements on quota exchange with Greenland, Iceland, Norway, Russia and the UK, among others.

⁴ In 2025, the quotas for mackerel and blue whiting catches were reduced compared to 2024.

⁵ The implicit price of Faroese salmon, calculated based on export value and volume, fell from around kr. 70/kg in January 2025 to around kr. 45/kg in August 2025.

CHART 2

Subdued development in goods exports and weaker growth in export markets

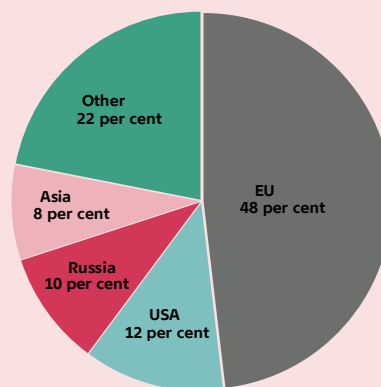


Note: Trade-weighted growth in export markets is based on the October 2025 *IMF World Economic Outlook*. The growth is calculated as trade-weighted GDP growth in the Faroe Islands' 12 largest trading partners, which account for almost 90 per cent of Faroese goods exports. Exports of goods for 2025 are projected based on the export value from January to September 2025.

Source: Hagstova Føroya, IMF and own calculations.

CHART 3

Geographical distribution of Faroese goods exports



Note: Export shares are calculated based on goods exports from October 2024 to September 2025.

Source: Hagstova Føroya and own calculations.

The US administration has so far imposed a 10 per cent tariff on Faroese goods. Higher tariffs could potentially pose a significant trade barrier for the Faroese export sector in the coming years. However, for the time being, the Faroe Islands have gained a competitive advantage as other fish exporting countries, including EU countries, Norway and Iceland, have had a higher tariff of 15 per cent imposed by the US. At the same time, the demand for salmon is increasing worldwide, which improves opportunities to increase exports to other countries if demand in the US drops.

US tariffs and increased geopolitical uncertainty are also dampening growth prospects in some of the Faroe Islands' largest export markets. Food exports are generally less sensitive to global economic fluctuations, and the Faroese export sector can therefore be expected to have a certain degree of resilience to lower growth in export markets.⁶ However, in the current geopolitical situation, the overall trading conditions can change quickly. Therefore, it's more beneficial than ever to have some flexibility to shift exports quickly if trading conditions in some markets deteriorate. This is especially true for a small, open and relatively undiversified economy like the Faroe Islands.

Increasing global demand for salmon means that the price of salmon is expected to rise again in 2026.⁷ This will have a positive impact on growth in the Faroe Islands. For pelagic fishing, however, there is the prospect of a significant reduction in some fishing quotas. In autumn 2025, the Faroe Islands, together with Iceland, Norway and the UK, agreed to follow the recommendations of the

⁶ For the cyclical sensitivity of food in Denmark, see Adrian Michael Bay Schmith and Helle Eis Christensen, *Stort fald i dansk eksport, men sammensætningen kan være en stødpude* (large drop in Danish exports, but the composition might ease the fall, in Danish only), *Danmarks Nationalbank Economic Memo*, No. 8, June 2020.

⁷ See the Economic Council of the Faroe Islands autumn report 2025, *Føroyski Búskapurin, Heystið 2025* ([link](#)).

International Council for the Exploration of the Sea, ICES, to reduce the blue whiting quota by 41 per cent and increase the herring quota by 33 per cent. A final agreement on the mackerel quota remains outstanding, with a 70 per cent reduction recommended.⁸ The reduced quotas are due to a decline in fish stocks, partly because catches have exceeded the recommendations for the total allowable catch in recent years.⁹ Mackerel exports account for more than 10 per cent of goods exports, so a significant reduction in quotas will generally harm fishing revenues.

The labour market remains very tight

The high level of activity in recent years is also reflected in the Faroese labour market, with high employment, low unemployment and labour shortages in several places. Employment has increased to over 30,000 people, while unemployment has remained relatively stable at around 1 per cent of the labour force for the past two years. There is full employment in the Faroe Islands, and the labour force participation rate is high compared to other European countries.¹⁰

In recent years, employment has increased due to a significant expansion of the labour force, with many foreigners entering the Faroese labour market. The share of foreign labour in total employment has thus increased from around 2 per cent to around 7 per cent over the last 10 years. However, this is still lower than the level in Denmark and Iceland, for example. The use of foreign labour in the Faroe Islands is particularly widespread in the manufacturing and hospitality industries and has helped to alleviate pressure on the labour market in recent years.

The Faroese labour market is generally characterised by a high degree of flexibility, with the ability to attract foreign labour during times of prosperity. Conversely, there has historically been an outflow of labour during economic downturns. In 2022 and 2023, employment growth was driven mainly by foreign labour due to high demand for labour, while the *fast track scheme* from 2021 made it easier for companies to recruit labour from abroad.¹¹ However, in the last few years, employment growth has slowed, and the contribution from foreign labour has become significantly smaller, see chart 4. This indicates that the pressure on the labour market is less than before.

⁸ See the Ombudsman of the Faroe Islands, *Orientering*, no. 20, 2025.

⁹ Catches have exceeded ICES recommendations when coastal states have not been able to agree on how the catch should be distributed between countries. This means that several countries have instead set their own quotas unilaterally, resulting in the total catch exceeding the recommendations.

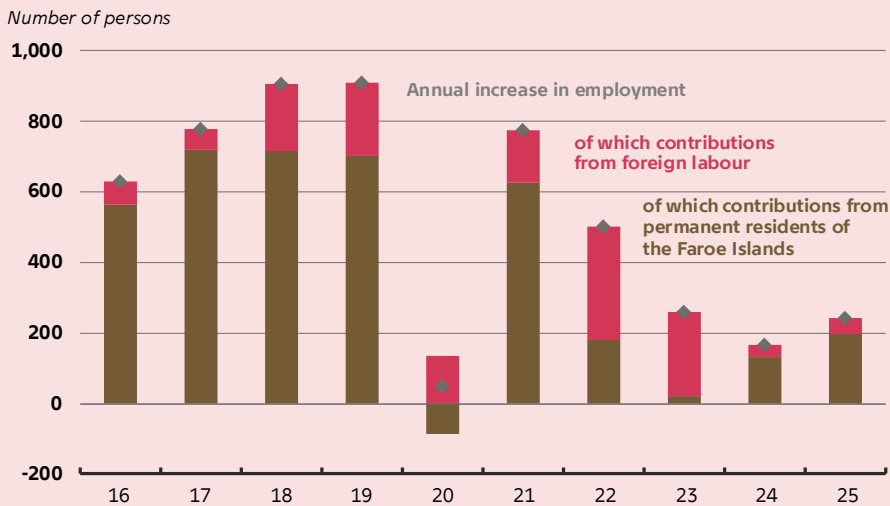
¹⁰ The labour force participation rate in the Faroe Islands in 2024 was 85 per cent for the 15-74 age group, the highest in Europe.

¹¹ Among other things, the fast track scheme made it possible to bring in labour from third countries.

CHART 4

The labour market has slowed

Annual growth in employment



Note: *Permanent residents of the Faroe Islands* are defined as people who have lived in the Faroe Islands for at least half of their lives or for 7 out of 10 consecutive years. Employment growth is based on average levels for the whole year. 2025 includes data from January to October.

Source: Hagstova Føroya and own calculations.

However, the pressure on the labour market is expected to remain high in the future, with limited labour market resources posing a structural challenge to the economy. This is particularly true in the healthcare and eldercare sectors, where the need for labour is increasing as the population lives longer. The Economic Council of the Faroe Islands estimates that there will be a need for 450 additional full-time positions in eldercare alone over the next ten years.¹² The labour shortage should also be seen in the light of the fact that around 40 per cent of each year group go abroad for education, but only half return to the Faroese labour market. This means that the Faroe Islands will lose around 20 per cent of each year group. The limited availability of resources in the labour market is a bottleneck for the economy and could be a barrier to future growth.

High wage increases support private consumption

The tight labour market of recent years and widespread employee demand for compensation for real wage losses in previous years have led to high wage increases. In the private labour market, the 2024 collective agreement for fish factory workers and port workers, among others, resulted in an agreed wage increase of 8.2 per cent in 2024 and 2025. The agreement also included a general wage increase for this group, which, together with the agreed wage increase, results in wage increases of up to 13 per cent over the two-year collective agreement period.¹³ Against this backdrop, the average annual wage growth in the Faroe Islands has increased to over 6 per cent in 2025, approximately twice as high as before the pandemic, see chart 5. For the average Faroese employee, real wages have caught up with their pre-inflation levels from 2022, see chart 6.

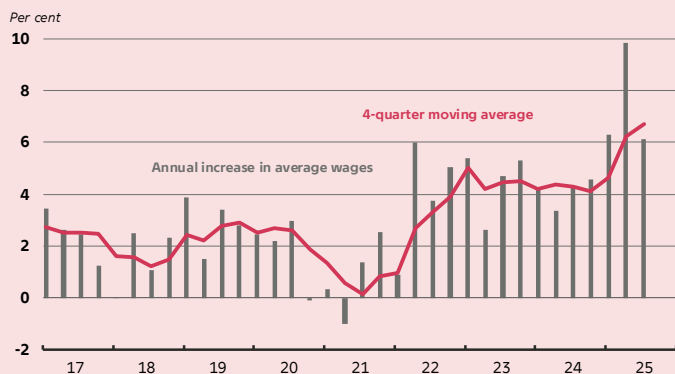
¹² See Economic Council of the Faroe Islands, *Kommunubúskapurin og eldraðkið, Heystið 2025 (link)*.

¹³ See Mikkel Bess, Sofie H. Friis and Tina S. Hvolbøl, *Fiscal planning can increase the resilience of the Faroese economy, Danmarks Nationalbank Analysis, no. 20, December 2024.*

CHART 5

High wage growth in recent years

Wages per employee



Note: Calculated as the actual wage per employee in the entire economy. The bars show quarterly annual growth. The red curve shows the 4-quarter moving average. Employees are not counted twice if employed in more than one job.

Source: Hagstova Føroya and own calculations.

CHART 6

Real wages for the average worker have recovered after the declines in 2022 and 2023



Note: The chart shows the development of the average wage in the Faroe Islands. Real wages are deflated with the consumer price index.

Source: Hagstova Føroya and own calculations.

High wage increases are currently helping to support private consumption, which is expected to make a positive contribution to GDP growth in 2025.¹⁴ In 2025, household consumption has also been further stimulated by lower interest rates and tax cuts. Consumer confidence in the Faroe Islands fell sharply in 2022 amid rising inflation and higher interest rates, and has since remained below the historical average.

Inflation is low despite higher food prices

Inflation in the Faroe Islands has fluctuated around 1 per cent over the past year, see chart 7. Consumer price developments in the Faroe Islands are generally in line with those in Denmark and the rest of Europe, where inflation has come under control after a very high level in 2022.

As in many other countries, food prices have risen significantly recently, helping push up inflation. However, subdued price developments for other goods have kept inflation low. Overall, food prices have increased by around 30 per cent over the past five years, which roughly corresponds to price increases in Denmark, see chart 8.¹⁵ In response to high food prices, the government has decided to remove VAT on vegetables from 2026, among other things.

Despite high wage growth and rising food prices, inflation is being kept down as the prices of fuel, transport, clothing and other items have fallen over the past year. The assessment of actual inflation in the Faroe Islands and the contribution of individual consumption groups to price developments is complicated by the fact that the weightings used to measure consumption in the Faroe Islands are not regularly updated. The weights are based on a 2007 consumption survey, so

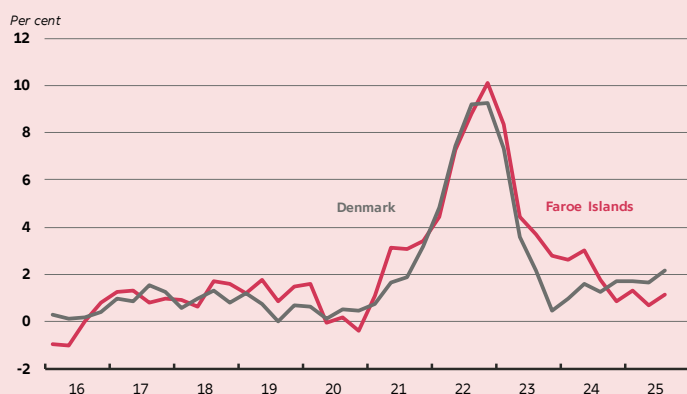
¹⁴ See the Economic Council of the Faroe Islands autumn report 2025, *Føroyski Búskapurin, Heystid 2025* ([link](#)).

¹⁵ One reason food prices have risen is that supply in commodity markets has not kept pace with demand. This has led to rising commodity prices globally, which ultimately affects food prices, see for example, Oliver H. Bentsen, Christoffer J. Weissert and Amy Y. Zhuang, Global conditions drive high food prices in Denmark and abroad, *Danmarks Nationalbank Analysis*, no. 20, September 2025.

the calculated inflation assumes that Faroese consumption patterns have not changed since then.¹⁶ As consumers tend to shift consumption towards relatively cheaper goods, fixed weights can overestimate the calculated inflation rate. It's crucial to have as accurate a picture of price development as possible, as this is important for wage negotiations and economic policy planning, among other things.

CHART 7
Inflation has been low for the past year

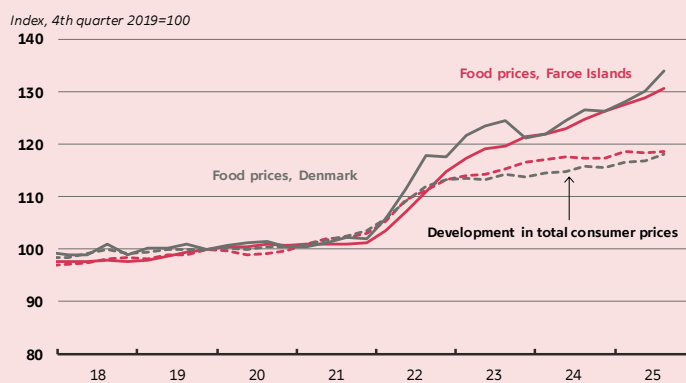
Annual change in the consumer price index, CPI



Note: The chart shows the annual change in the consumer price index based on quarterly data.
Source: Hagstova Føroya, Statistics Denmark and own calculations.

CHART 8
Food prices in the Faroe Islands have increased by the same amount as in Denmark

Development in food prices and total consumer prices



Note: The red and grey curves show the price development of food and non-alcoholic beverages in the Faroe Islands and Denmark, respectively. The dashed red and grey curves indicate the development of the total consumer price index in the Faroe Islands and Denmark, respectively.
Source: Hagstova Føroya, Statistics Denmark and own calculations.

¹⁶ Statistics Faroe Islands, Hagstova Føroya, adjusts the weights for individual items within the overall consumption categories as part of the regular maintenance of the consumer price index. Likewise, new products and services are continuously updated, and those that are no longer relevant are removed from the weight basis.

02 House prices continue to rise

Prices in the Faroese housing market have increased significantly across geographical areas, see chart 9. In 2024, house prices in Tórshavn increased by approximately 9 per cent compared to the previous year, and the data for 2025 points to annual price increases of over 10 per cent. The development should be seen in light of the positive trends in the economy, population growth, high wage increases and falling interest rates, among other things.

House prices reflect the relationship between supply and demand in the housing market. The supply of housing in this context is understood as the total number of homes, the housing stock, which develops slowly as it takes time to plan and build new houses. In the short term, it is therefore predominantly demand that determines the development of house prices.¹⁷

High economic activity has led to increased migration to the Faroe Islands over the past 10 years. From 2015 to 2024, the population grew by 5,820 people or 2,744 households.¹⁸ In the same period, almost 2,100 new homes were built. In the short term, house prices may reflect a delay in the construction of new houses relative to the number of new households. From 2015 to 2022, when house prices generally increased, there were more new households than homes, see chart 10. There has been a delay in housing construction, which has contributed to pushing up prices. However, this development came after a period where the number of new houses exceeded the number of new households. Other factors, such as the trend towards increased private rentals targeting tourists, may also have contributed to the increase in housing demand in recent years.

Several factors indicate that house prices may continue to rise in the future. For example, the prospect of continued rising incomes and high activity, including several large public construction projects, has led to rising prices in the construction industry. This could mean that the supply of housing will remain constrained in the future. House prices are also affected by the fact that there is no real estate taxation in the Faroe Islands and there are subsidies for interest expenses on housing loans.¹⁹ Both factors contribute to increased fluctuations in house prices.²⁰ The introduction of a housing tax in the Faroe Islands linked to prices in the housing market could dampen price fluctuations and the cyclicity of the economy in general.

¹⁷ See Henrik Yde Andersen, Cecilie Walsted Graaskær, Simon Juul Hvid, Asbjørn Klejn, Rikke Rohde Nielsen, Emil Toft Vestergaard, Twin speed housing market, *Danmarks Nationalbank Analysis*, no. 27, November 2025.

¹⁸ The calculation is based on data for the number of households from Hagstova Føroya from December 2015 to October 2025.

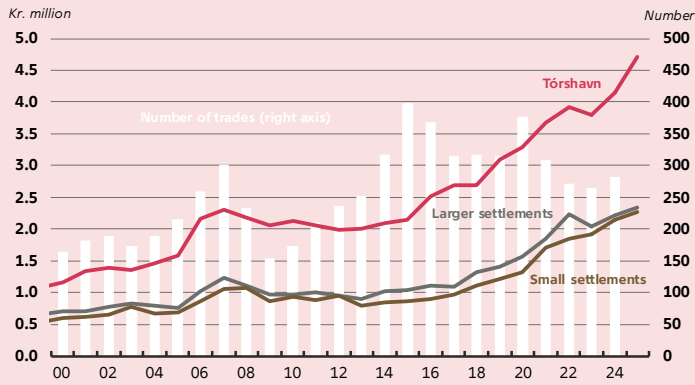
¹⁹ Homeowners can apply for a subsidy on their interest expenses related to housing loan instalments. The interest subsidy is 35 per cent of the interest expenses up to a ceiling of kr. 100,000, i.e. a maximum subsidy of kr. 35,000 can be obtained. The interest subsidy can only be granted to one person per property registration number, see www.taks.fo.

²⁰ See Danmarks Nationalbank, House price bubbles and the advantages of stabilising housing taxation, *Danmarks Nationalbank Monetary Review*, 3rd Quarter 2016.

CHART 9

House prices have increased

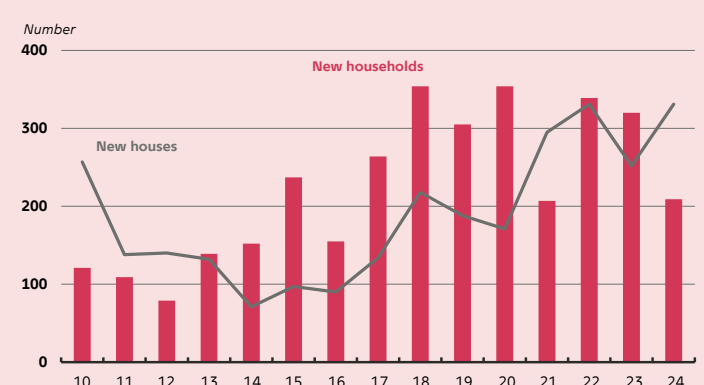
Development in average house prices



Note: The chart shows the average house prices for each year. Figures for 2025 are 2024 house prices projected using the growth in preliminary house prices for 2024 calculated by Føroya Banki.
Source: Hagstova Føroya, Føroya Banki and own calculations.

CHART 10

Increasing housing supply since 2016



Note: The chart shows the number of completed houses. The calculation is based on new connections to the electricity grid, as there is no actual calculation of completed residential construction. For 2010 to 2025, the number of new households is calculated as the difference in the number of households at year-end.
Source: Hagstova Føroya and own calculations.

Increasing growth in housing loans

Growth in housing loans to households has accelerated during 2025. Mortgage lending was 6.9 per cent higher in October 2025 compared to October 2024, see chart 11. This development is primarily driven by growth in lending from Faroese banks.

Home financing via bank loans is still most common among households. The housing loans are largely variable-rate, with interest rates that reset after one month. As a result, interest rate fluctuations quickly pass through to homeowners' costs. Interest rates on both outstanding and new housing loans have fallen, reducing household debt servicing costs, see chart 12.

Rising house prices have not led to a general increase in loan-to-value ratios among house buyers. However, in smaller segments, such as first-time buyers with the lowest loan-to-value ratios, there has been an increase.²¹ Almost two-thirds of all housing loans also have a debt-to-income ratio of less than 3. The majority of lending for home purchases is with amortisation, which helps increase homeowners' resilience to economic shocks.

In 2023, rules on lending for housing purposes were adopted, corresponding to the Danish provisions on minimum down-payment requirements and debt-to-income ratio found in the Executive Order on good practice for housing credit.²²

²¹ First-time buyers are defined here as home buyers who appear in the Credit Register for the first time in a given quarter with housing debt secured by real estate. Previous housing debt in both Denmark and the Faroe Islands is taken into account. Home buyers who last had a mortgage before the end of 2019 (when reporting to the Credit Register began) will also be categorised as first-time buyers.

²² See Executive Order No. 1582 of 6 December 2023 for the Faroe Islands on good practice for financial companies. The rules only apply to financial institutions and to the loans they grant. Mortgage loans are not covered by the Executive Order. This is because the Royal Decree is only authorised to lay down rules for financial institutions, as the mortgage credit area has been transferred to the Faroe Islands. The Executive Order, therefore, does not regulate Danish mortgage credit institutions, for example.

CHART 11

Rising house prices lead to increasing growth in housing loans

Annual growth in housing loans, per cent



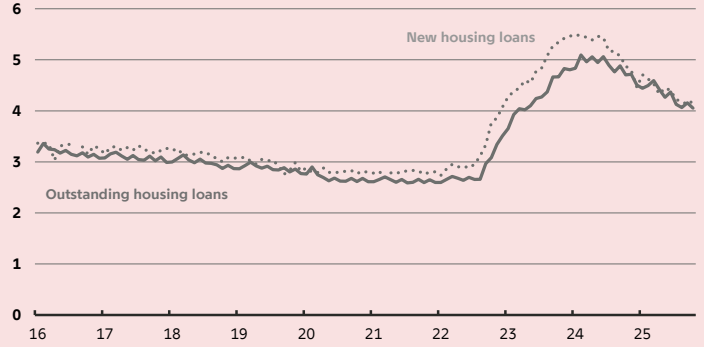
Note: The chart shows growth in lending to Faroese households for housing purposes from Faroese, Danish and Greenlandic institutions. Growth is calculated as a three-month moving average. The most recent observation is October 2025.

Source: Danmarks Nationalbank.

CHART 12

Interest rates on both new and outstanding housing loans have fallen

Interest rate, per cent



Note: The chart shows interest rates on new and outstanding housing loans from Faroese, Danish and Greenlandic credit institutions to Faroese borrowers. The most recent observation is October 2025.

Source: Danmarks Nationalbank.

03

Continued high profits support banks' resilience

The growth of the Faroese economy is also reflected in the banking sector, which is generally doing well. Banks have few losses and impairment charges, and through 2025, credit growth has picked up, with strong growth in lending to corporates. Banks have built up capital over a number of years, and profits are high, which increases banks' resilience.

Increase in lending driven by strong growth in lending to corporates

Credit in the Faroe Islands is mainly granted through the four Faroese banks.²³ They are also responsible for distributing mortgage loans, as cooperation agreements have been established with Danish mortgage credit institutions. The growth in lending in the Faroe Islands has accelerated during 2025 and was just over 9 per cent at the end of October, see chart 13.²⁴

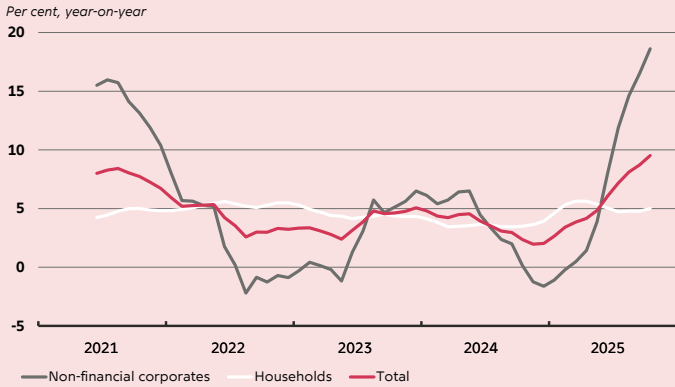
The annual growth in lending to households is moderate, at around 5 per cent, as of the end of October 2025. However, growth in lending to non-financial companies has accelerated sharply, and is almost 19 per cent year-on-year at the end of October 2025. The strong growth in lending to non-financial companies is primarily driven by growth in lending to the *fishing industry*, and the *transport and hotel industry*, see chart 14. The two industries together account for almost 35 per cent of the institutions' lending to non-financial companies.

²³ Furthermore, large companies in particular take out loans directly from foreign institutions.

²⁴ Lending covers loans from Faroese, Danish and Greenlandic credit institutions to Faroese residents, unless otherwise stated.

CHART 13

Strong growth in lending to non-financial companies

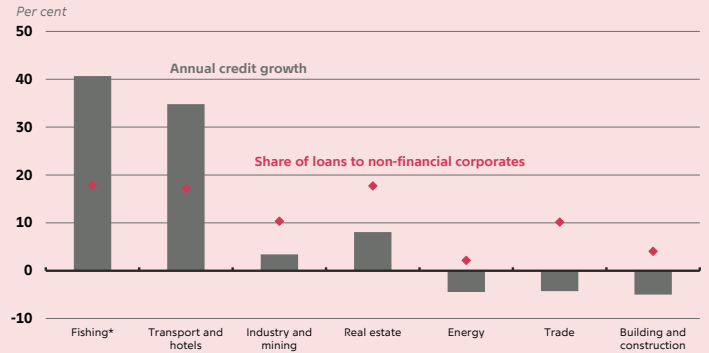


Note: The chart shows growth in nominal lending to Faroese non-financial companies and households from Faroese, Danish and Greenlandic credit institutions. *Non-financial companies* include private and public companies. Lending growth is calculated as the annual growth rate in lending, calculated as a three-month moving average. The most recent observations are from October 2025.

Source: Danmarks Nationalbank.

CHART 14

Particularly strong growth in lending to the fishing and transport and hotel industries



Note: Annual growth in nominal lending from Faroese, Danish and Greenlandic credit institutions to different industries and the industries' share of total lending to non-financial companies. *Non-financial companies* include private and public companies. Lending growth is calculated as the annual growth rate in lending, calculated as a three-month moving average. The most recent observations are from October 2025.

Source: Danmarks Nationalbank.

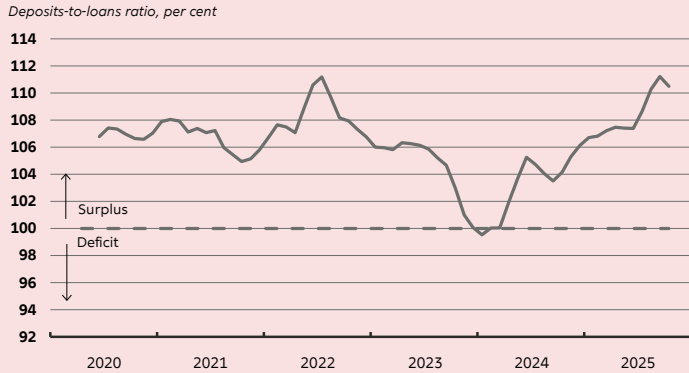
The banks fulfil the Liquidity Coverage Ratio, LCR, and Net Stable Funding Ratio, NSFR, requirements with good excess coverage. Banks continue to finance their lending activities predominantly through customer deposits. The deposit surplus has increased during 2025, see chart 15. At the end of October 2025, deposits amounted to approximately 110 per cent of loans. However, this covers some variation across the Faroese banks.

Continued high profits in H1 2025

Bank profits remain at a high level, see chart 16. Higher interest rates have driven higher profits since 2022. The institutions' net interest and fee income has decreased slightly from H1 2024 to H1 2025. At the same time, the banks reversed impairment charges in the first half of 2025, which contributed positively to the result. Impairment charge ratios for both companies and households remain low. The continued growth in the Faroese economy and high employment is therefore also reflected among the banks' customers.

CHART 15

Higher deposit surplus

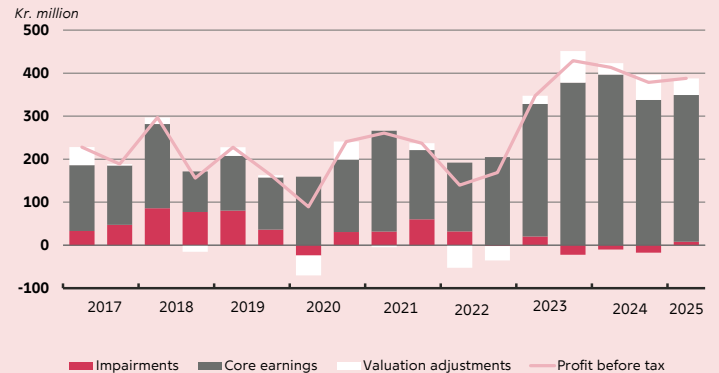


Note: The chart shows the total deposits of Faroese banks in relation to their lending to non-financial counterparties. Deposits and loans are calculated excluding repo transactions. The most recent observations are from September 2025.

Source: Danmarks Nationalbank.

CHART 16

Profits remain at a high level



Note: Half-year data for Faroese banks. Core earnings consist of net interest and net fee income, personnel and administrative expenses, amortisation and impairment charges of intangible and tangible assets, and other operating income and expenses. A positive value for impairment charges means that impairment charges are reversed.

Source: The Danish Financial Supervisory Authority and own calculations.

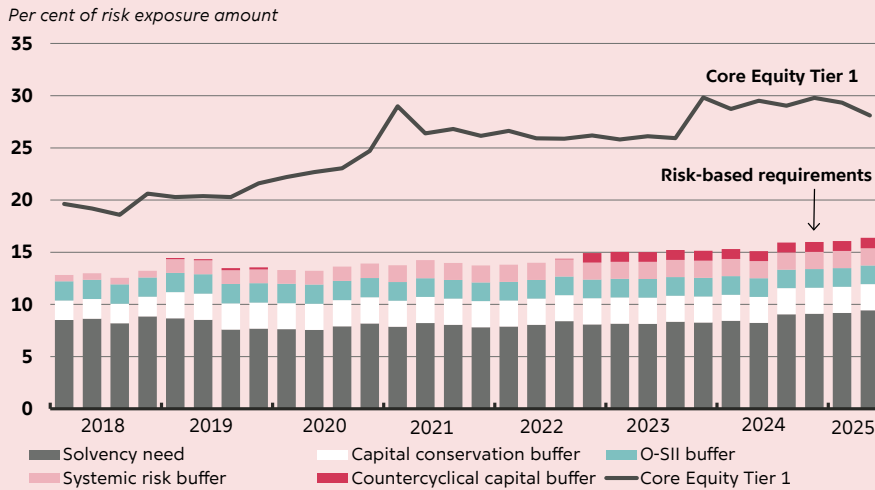
Bank capitalisation has been stable over the past two years

Banks' capitalisation, measured as Common Equity Tier 1 as a percentage of risk-weighted exposures, has remained largely unchanged since the end of 2023, with a slight decrease in the second half of 2025, see chart 17. Banks have been building up capital for a long time.

Since 1 July 2025, banks have had to meet an increased systemic risk buffer requirement from 2 per cent to 3 per cent. In addition, a countercyclical capital buffer of 1 per cent has been in place since 2023. Both capital buffers are intended to ensure that banks have sufficient room to bear losses and continue providing credit to households and companies in a systemic crisis.

CHART 17

Continued significant headroom to the risk-based capital requirements



Note: The chart shows the Faroese banks' capital requirements and Common Equity Tier 1 as a percentage of the risk exposure amount. The systemic risk buffer has been increased from 2 per cent to 3 per cent as of 1 July 2025. The level of the countercyclical capital buffer is the weighted average of the rates for the relevant jurisdictions in which the institutions have credit exposures (Denmark, the Faroe Islands and Greenland).

Source: The Danish Financial Supervisory Authority and own calculations.

From 1 January 2026, banks must calculate their capital requirements in accordance with the latest amendment to the Capital Requirements Regulation, CRR3. This is expected to result in lower risk-weighted exposures overall for banks, especially due to the lower weighting of residential mortgage exposures with a low loan-to-value ratio. At the same time, banks' minimum requirement for eligible own funds and liabilities, MREL, is being phased in towards 1 July 2026.²⁵ To fulfil MREL, banks predominantly use Common Equity Tier 1.

²⁵The MREL is designed to ensure that each bank has sufficient own funds and eligible liability instruments to absorb losses and capitalise the bank if its problems become so severe that it is in danger.

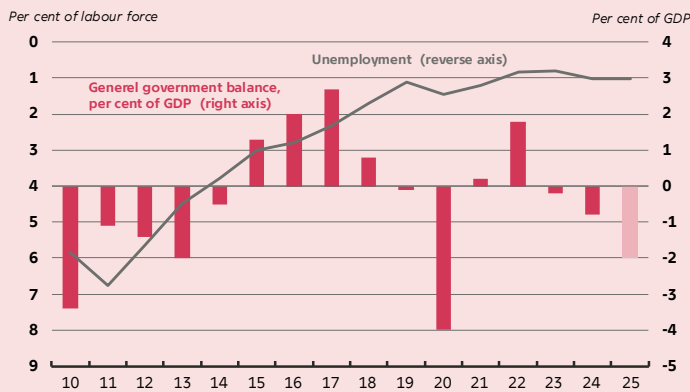
04 Fiscal planning can strengthen the Faroese economy

Despite several years of economic boom, there have been no significant surpluses in public finances in recent years, see chart 18. In 2025, the Economic Council of the Faroe Islands expects a total public deficit of around 2 per cent of GDP, and the 2026 budget proposal also foresees a deficit in the national treasury next year. Fiscal policy thus boosts economic activity in a period when the economy is already operating at maximum capacity.

When public finances are not strengthened in good times, austerity measures may be needed when the economy turns around, which can amplify an economic downturn. However, compared to other European countries, the gross public debt in the Faroe Islands is relatively low at around 30 per cent of GDP.²⁶

CHART 18

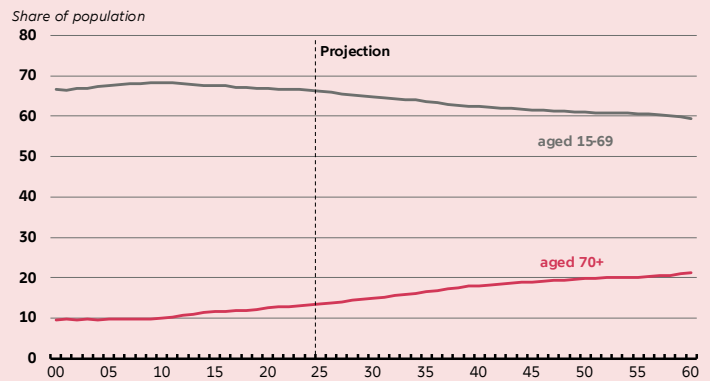
Public budget deficits despite favourable macroeconomic conditions



Source: Hagstova Føroya and the Faroe Islands Economic Council.

CHART 19

Demographic headwinds will increase in the coming years



Source: Hagstova Føroya and own calculations.

Lower fishing quotas can reduce income from fishing

A significant part of the Faroe Islands' public revenue comes from taxes on fishing and aquaculture, which fluctuate from year to year as they depend on several global factors, including developments in fish prices and quotas. If the Faroe Islands follow ICES' recommendations to significantly reduce fishing, this will lead to a decrease in the Faroe Islands' revenue from resource taxes, and thus the deficit may be larger than expected under the budget proposal.

²⁶ In September 2025, Moody's gave the Faroe Islands a credit rating of Aa2 with a stable outlook. The Danish government will likely provide financial assistance if the Faroe Islands face severe economic difficulties ([link](#)).

However, the Faroe Islands Economic Fund²⁷ helps smooth revenues from the fishing and aquaculture industries over time. This is done by paying out revenues from the fund to the Finance Act, totalling up to kr. 600 million, while additional revenues are paid out over a seven-year period.²⁸ This is generally an appropriate way to smooth public revenue over time and supports the stability of public finances and the levelling of the business cycle. In recent years, however, fiscal policy has been pro-cyclical as there has been no corresponding control on the expenditure side.

Sustainability challenge creates need for structural adjustments

The Economic Council of the Faroe Islands' latest sustainability calculation estimates that a permanent fiscal tightening of 9 per cent of GDP will be required to bring public finances into balance in the long term. This reflects, among other things, that the Faroe Islands' demographic composition will change significantly in the coming years. This should be seen in light of a higher average life expectancy, declining fertility rates and a relatively high number of young people leaving the Faroe Islands without returning. In the coming decades, the proportion of people of working age will make up a decreasing share of the Faroese population, and the share of older people will increase instead, see chart 19. This will increase the pressure on public finances in the coming years.

Fiscal sustainability can be improved by policies that support later retirement from the Faroese labour market, including a higher retirement age. The retirement age in the Faroe Islands is currently 67½ and will rise to 68 in 2030. However, it will only counteract the demographic development to a limited extent. The government has therefore previously proposed raising the retirement age to 70 by 2042, but the proposal was withdrawn for reconsideration and is still under discussion.²⁹

In addition, there are political considerations about building a tunnel to Suðuroy at an estimated cost of up to 20 per cent of GDP. Such a significant investment would greatly reinforce the need for a strong fiscal framework to support appropriate fiscal planning and improve the sustainability of public finances. This is also due to the fact that this project is assessed to be less user-financed than several other projects, which increases vulnerability.

The fiscal framework can increase the resilience of the Faroese economy

The challenge of fiscal sustainability emphasises the need for comprehensive management and long-term planning of public finances. This can support both addressing known challenges promptly and building fiscal buffers in good times, leaving room to manoeuvre to deal with unforeseen challenges. Over the past few years, it has become clear that countries with strong public finances have also had more room for political manoeuvre to deal with unexpected economic challenges, such as the pandemic and the current military build-up in Europe.

In the draft Finance Act for 2026, the Government of the Faroe Islands has proposed the introduction of a fiscal framework that creates an upper limit for annual expenditure growth in the country. However, the framework will only apply to the central government's expenses and thus not those of the municipalities, so that there will still be no central control of the municipalities' total expenses. According to the proposal, the budget's operating expenses may

²⁷ The Faroe Islands Economic Fund was established in 2011 and aims to support a self-sustaining economy and contribute to cyclical equalisation.

²⁸ Currently, up to kr. 350 million is paid out from the fishing industry and kr. 250 million from the aquaculture industry.

²⁹ This includes the possibility of earlier retirement for people who have been in the labour market for many years.

not exceed those of the previous year by more than 1 per cent, in addition to general wage and price increases.³⁰

It is positive that work is being done to establish a framework to support more appropriate cost management in the public sector. However, the spending cap can be extended and reinforced in several areas. Among other things, fiscal rules should ensure that known challenges that put pressure on sustainability in the longer term are also taken into account when designing the short-term fiscal policy. Therefore, fiscal policy should be tied to multi-year targets for the development of public spending, combined with an overall target for the general government balance. The fiscal framework should therefore also cover the entire public sector, especially since demographic trends will put increasing pressure on municipal spending. A solid framework for coordinating public finances across the central government and municipalities is crucial to strengthening the resilience of the Faroese economy going forward.

³⁰ The Economic Council of the Faroe Islands is tasked with calculating the amount of growth in operating expenses allowed each year and reporting whether the actual growth in expenses is within the ceiling. The proposal also includes capital appropriations, which must follow an annual investment plan adopted by the Lagtinget, and thus may not exceed the politically decided limits. See, for example, the Ombudsman of the Faroe Islands, *Orientering*, no. 18, 2025.

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