Joining forces

Paige Perrin **explores the current trend of consolidation in the Icelandic pension sector and the wider impacts of a more concentrated market structure on competition, ownership and financial stability**

Over the past four decades, Iceland's pensions market has consolidated from around 96 funds to fewer than 20 today.

The latest wave of mergers suggests Iceland's pension system is entering a period of renewed consolidation, as funds grapple with growing regulatory burdens, compliance demands and pressure to achieve greater scale.

While consolidation promises stronger institutions and lower costs, it also raises questions about concentration risk, competition and pension funds' growing influence on the economy.

Íslenski Pension Fund managing director and Icelandic Pension Funds Association board member, Ólafur Páll Gunnarsson, points to economies of scale, stronger investment capabilities and growing governance, reporting and risk management requirements as the main drivers of consolidation.

"Pension funds today operate in a much more complex environment than they did in the past, and the demands placed on boards, management and internal controls have increased significantly," he says.

Furthermore, Icelandic Pension Funds Association legal advisor, Andrés Thorleifsson, argues that consolidation can strengthen operations, increase efficiency and create economies of scale for the benefit of fund members.

And for smaller schemes, rising regulatory and supervisory requirements have become increasingly costly, according to Frjálsi Pension Fund managing director, Arnaldur Loftsson.

"By merging with larger pension funds, the cost ratio of smaller funds declines," he says, noting that mergers can also reduce operational risk and improve long-term sustainability for schemes facing declining contributions and rising benefit payments.

Those pressures are already reflected in a series of recent mergers.

Brú Pension Fund merged with the Akureyri Employees' Pension Fund in 2025, while Lífsverk and Almenni combined in early 2026 to form the Almenni-Lífsverk pension fund.

Since then, the merged fund has begun merger talks with SL Pension Fund. Frjálsi Pension Fund has also completed a merger with the Pension Fund of the Icelandic Dental Association and has recently confirmed it will merge with the Farmers' Pension Fund, a move expected to be completed before the end of 2026. And, in June, Gildi Pension Fund and Festa Pension Fund entered discussions about a potential merger.

But not all merger discussions result in deals. Earlier this year, Lífeyrissjóður Verzlunarmanna and Birta Pension Fund began exploratory talks over a potential merger, but later confirmed they would not proceed to formal negotiations.

Gunnarsson describes this as "a new phase of consolidation" that may not yet have run its course.

"Depending on how recently approved and pending mergers are counted, the number of funds stands at around 17 and could fall further in the near term," he continues. "It is quite realistic that Iceland will have fewer than 10 pension funds within the next decade. That would allow for stronger institutions and lower unit costs while still preserving a degree of diversity and competition within the system."

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Structural limits and market risks

Despite the ability to improve efficiency, some experts warn that a shrinking number of increasingly powerful funds could deepen concerns about ownership concentration within Iceland.

Gunnarsson cautions that there are "clear limits to how far consolidation should go".

"Icelandic pension funds are already extremely large relative to the domestic capital market, so allowing the number of funds to fall too far would raise concerns about ownership concentration, market influence, and systemic risk," he stresses.

Gunnarsson emphasises that the challenge is to "find the right balance".

"Pension funds need enough consolidation to become stronger, more efficient and professionally managed, while still preserving diversity and competition. The goal should not simply be to have fewer and larger funds, but to build a system where funds are large enough to be resilient, yet not so dominant that they create risks for the wider economy," he adds.

Beyond these structural concerns, other experts highlight the implications for competition and ownership in the domestic market.

The University of Iceland School of Business professor, Gylfi Magnússon, warns that the downside of consolidation is a "concentration of power in fewer hands and clearer signs of horizontal ownership, where the same funds hold shares in competing firms".

"When you look at the largest owners of listed companies in Iceland, you almost always see the largest pension funds near the top. This is a concern for competition – and lack of competition is a chronic problem in a small and somewhat isolated market," he continues.

He adds that funds also hold the bulk of many bond classes, which affects market dynamics.

"Consolidation of the industry is likely to hamper price discovery and reduce liquidity in the stock and bond market, especially if large pension funds merge. This is not a concern for their foreign assets, where they are tiny players in large markets, but it can affect the market for the local currency," he says.

Magnússon warns that large funds must "tread very carefully" when rebalancing portfolios, unless they are selling one foreign asset for another.

Almenni-Lífsverk pension fund board member and University of Iceland associate professor, Már Wolfgang Mixa, stresses that consolidation is not only a financial stability issue but also a governance issue.

"When pension funds become dominant owners in many of the same companies, their views on board appointments, executive pay, strategy, mergers, financing, price mark-ups, and sustainability policies can have a broad impact on the economy," Wolfgang Mixa says.

"In such a small market, decisions made by a limited number of board representatives on behalf of pension funds may, therefore, affect not only fund members but also the wider public."

Loftsson argues that pension funds are not necessarily ideal owners of listed companies on their own, suggesting that shareholders with direct personal incentives for company success may be more suitable.

"As individual pension funds grow larger, the risk increases that their ownership stakes in listed companies will become even more significant," he adds.

Gunnarsson explains that Icelandic pension funds are very large investors in the domestic market, while the country has relatively few other large institutional or private investors.

However, in recent years, the rules on foreign investment have been liberalised in Iceland, and a large part of pension fund equity exposure is now in foreign assets, helping to reduce pressure on the domestic market.

Thorleifsson highlights that a "significant" portion of Icelandic pension funds' assets is abroad (about 41.5 per cent). He also notes that there is a set quantitative limit of 20 per cent on the share a pension fund can hold in each issuer, which should reduce the influence of each pension fund.

Member response and benefits

Member reaction to consolidation has generally been positive, with most mergers proceeding without significant opposition.

Gunnarsson points out that "in some cases, members of smaller funds have supported or called for mergers, because they recognise that a larger fund can provide a stronger operational foundation and better protection of rights".

"Smaller funds may be vulnerable if they lack scale or the resources needed to meet modern regulatory and investment requirements," he suggests.

Thorleifsson highlights the merger between Almenni Lífeyrissjóðurinn and Lífsverk as an example of member support for consolidation.

"The merger was put to a vote among fund members, with 87 per cent and 81 per cent of votes being in favour of a merger," he says.

Despite this acceptance, he acknowledges the importance of member representation, saying: "As funds become larger, it will be essential to ensure that members continue to have confidence in governance structures and that different member groups feel properly represented within the merged institutions."

Beyond member acceptance, consolidation also brings operational and investment advantages.

Loftsson argues that larger funds have greater capacity to uphold strong governance practices, for example, by implementing ownership policies and actively participating in annual general meetings of companies in which they invest. He also argues that larger funds have access to a broader range of investment opportunities and are better positioned to negotiate lower fees with external managers.

Cost efficiency is another major factor. In this context, Thorleifsson notes that Icelandic pension funds already operate with very low costs, with an average cost ratio of 0.6 per cent of total assets in 2024. He adds that lower ratios following mergers mean a larger share of investment returns accrues to members, increasing the likelihood that funds can meet long-term liabilities.

Outlook and future constraints

Thorleifsson says it is "hard to say" how many more mergers are realistic, noting that a key limiting factor is that Icelandic pension funds also provide disability benefits.

He explains that the disability burden remains "unevenly distributed" across funds due to members' differing occupational profiles.

Funds with a higher proportion of manual workers or predominantly female members tend to experience significantly higher disability rates than those funds serving office-based or male-dominated professions. Gunnarsson notes there is an ongoing discussion about separating disability pension rights from pension funds and placing them in a separate disability fund. He suggests that, if implemented, the reform "could open the door to a broader shift away from mandatory occupation-based membership", giving employees greater choice over their pension fund.

"This could lead to stronger competition between pension funds, even as the overall number of funds declines," he states.

Consolidation in Iceland's pension sector is expected to continue, driven by scale and regulatory pressures, though structural constraints will limit how far this can go.