



SAMTÖKFJÁRMÁLAFYRIRTÆKJA

Icelandic Financial Services Association

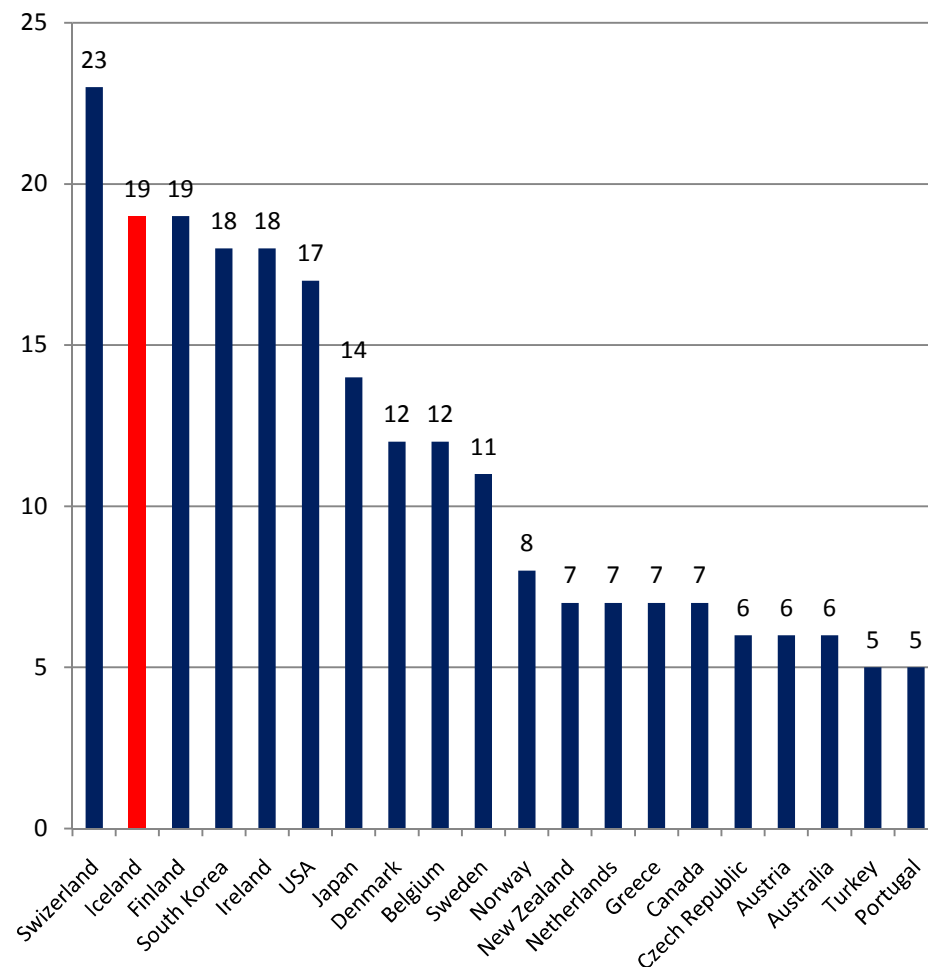
# Icelandic economy

AUGUST 2008

## International comparison

- Iceland is frequently ranked amongst the top 10 economies in the world in multiple categories by respected international institutions.
- Iceland ranks 2nd in the Global Benchmark Report 2007 which is an annual Danish assessment of 86 benchmarks of the development in the business environment and performances of OECD countries.
- Iceland ranked 1st out of 177 countries according to the UN Human Development Index 2007, measuring achievements in terms of life expectancy, educational attainment and adjusted real income.
- Further rankings for Iceland in 2007 include 14th for global economic freedom, 6th for corruption and 7th for world competitiveness in 2006.

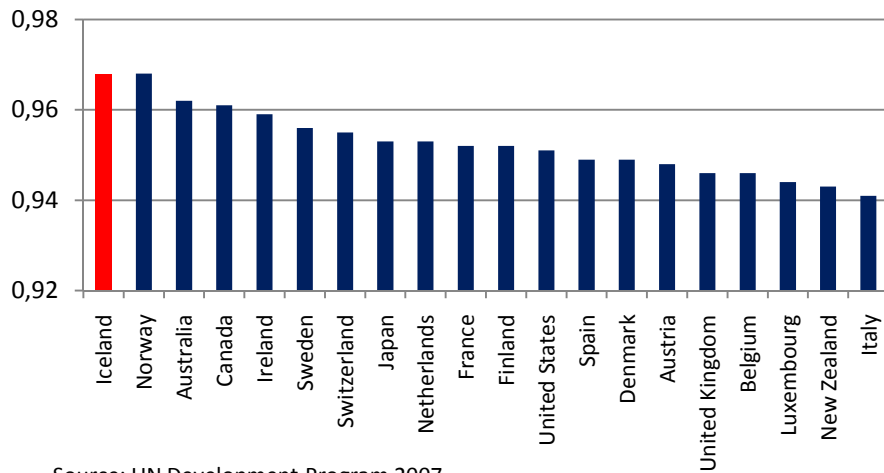
Number of top 3 positions in 86 international benchmarks



Source: Dansk Industri 2007

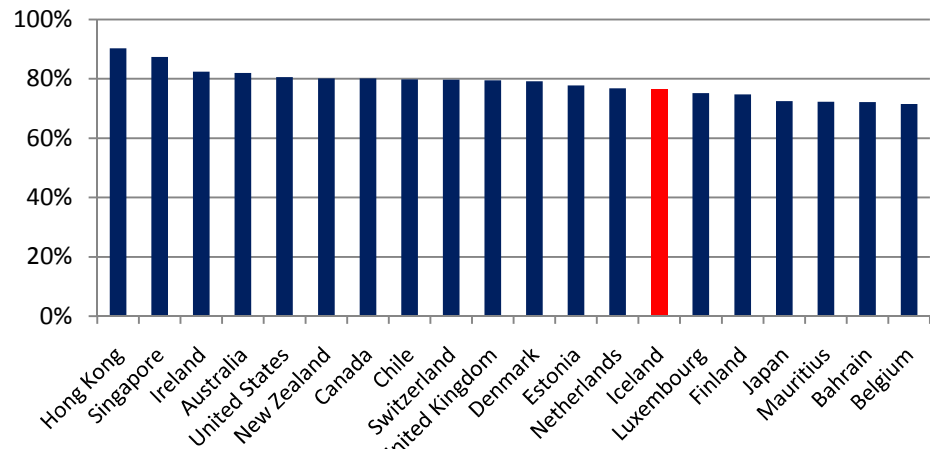
## International comparison

### UN human development index 2007



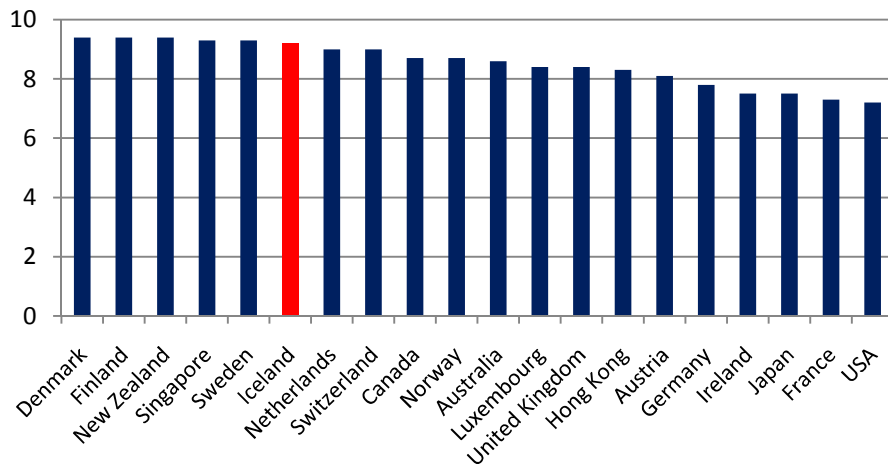
Source: UN Development Program 2007

### Global economic freedom 2007



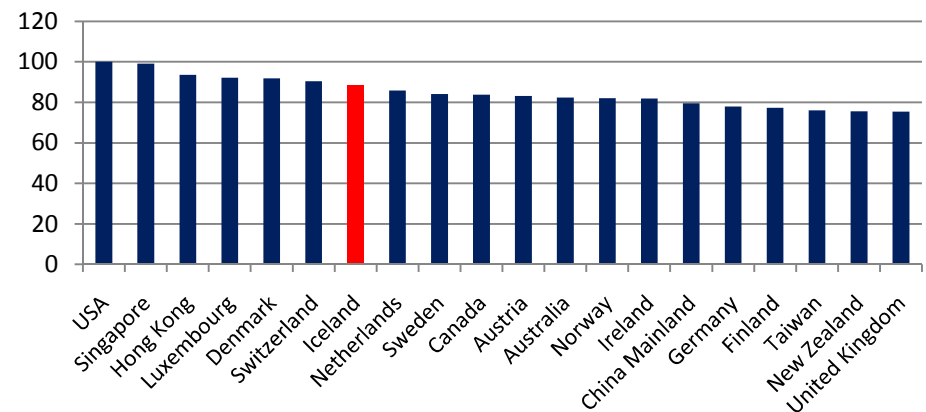
Source: Heritage Foundation 2008

### Corruption 2007



Source: Transparency International 2008

### World competitiveness 2006

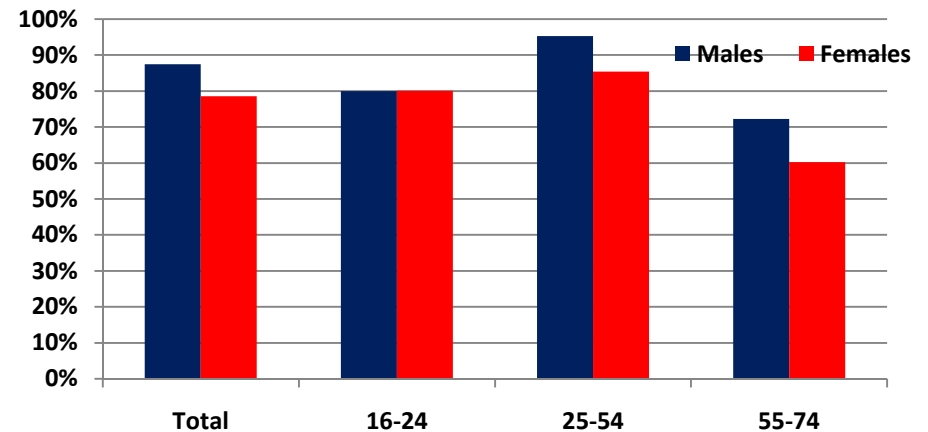


Source: IMD 2007

## Labour market

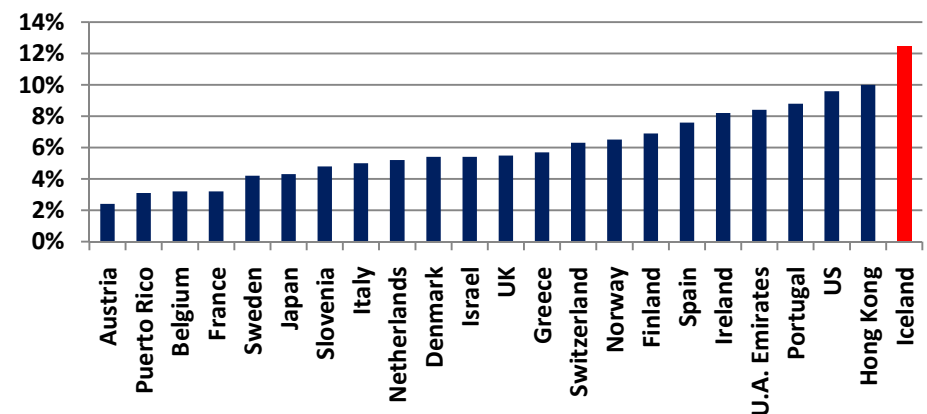
- Iceland's population is young with an average age of 34.5 and has the highest fertility rate in Europe with 2.08 children per woman.
- Labour market highly educated, open and flexible.
- Unemployment has ranged between 2%-5.3% since 1991.
- Migrant foreign workers meet labour demand in upswings and cushion labour market shocks in downswings.
- Labour participation rate is one of the highest in OECD countries, especially for women and workers aged 55-74.
- Iceland's labour force is among the most entrepreneurial in the world with a high frequency of early-stage entrepreneurial activity for people ages 18-64 (Global Entrepreneurship Monitor 2007 Report).

### Labour activity rate 2007



Source: Statistics Iceland 2008

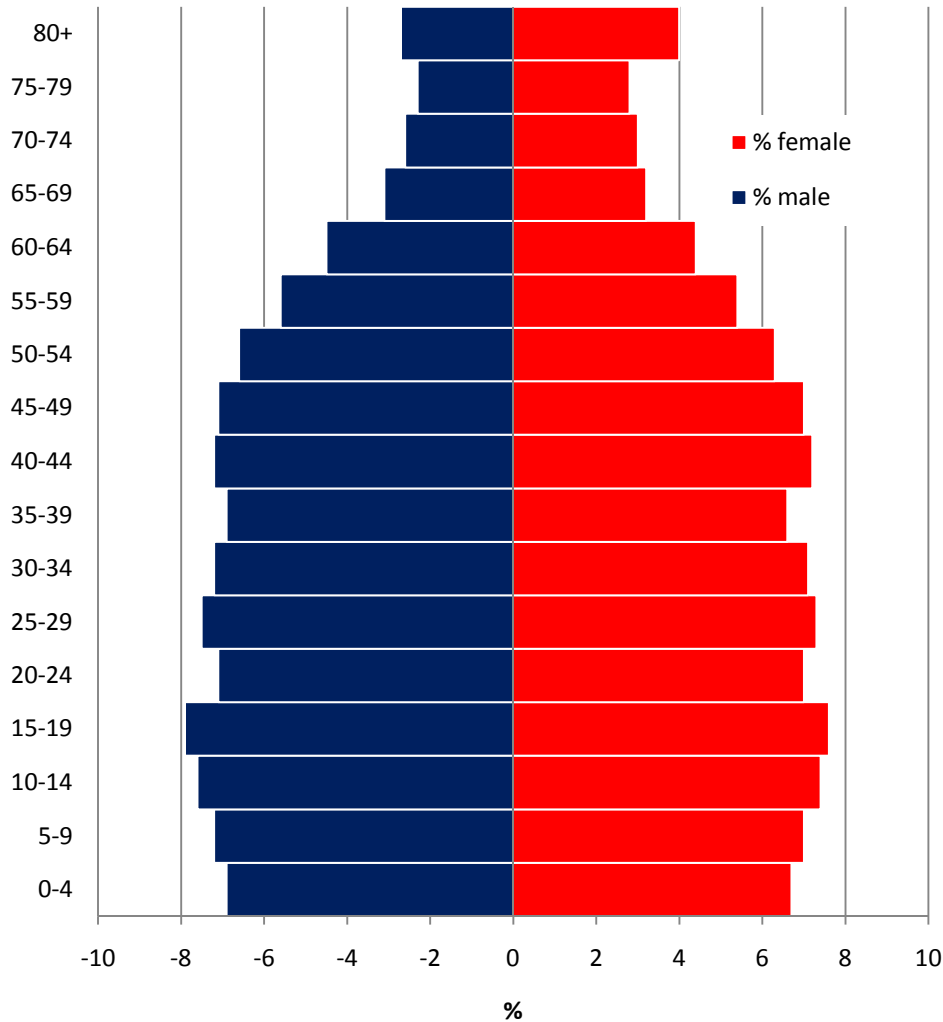
### Early-stage entrepreneurial activity 2007



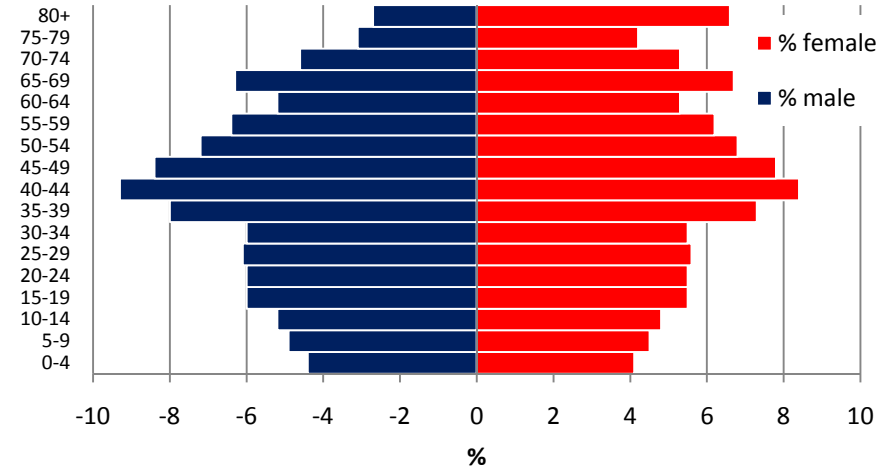
Source: Global Entrepreneurship Monitor 2007 Report

## Demographics

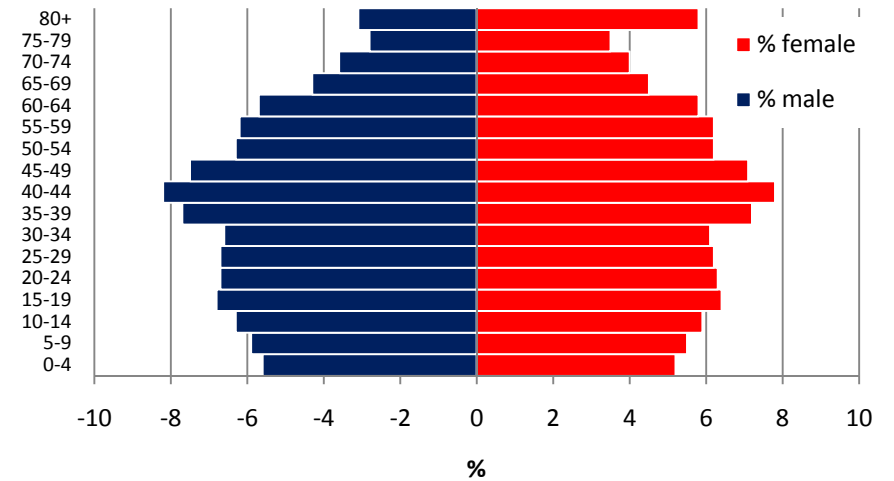
### Iceland 2007 - Population pyramid



### Germany 2007 - Population pyramid



### UK 2007 - Population pyramid

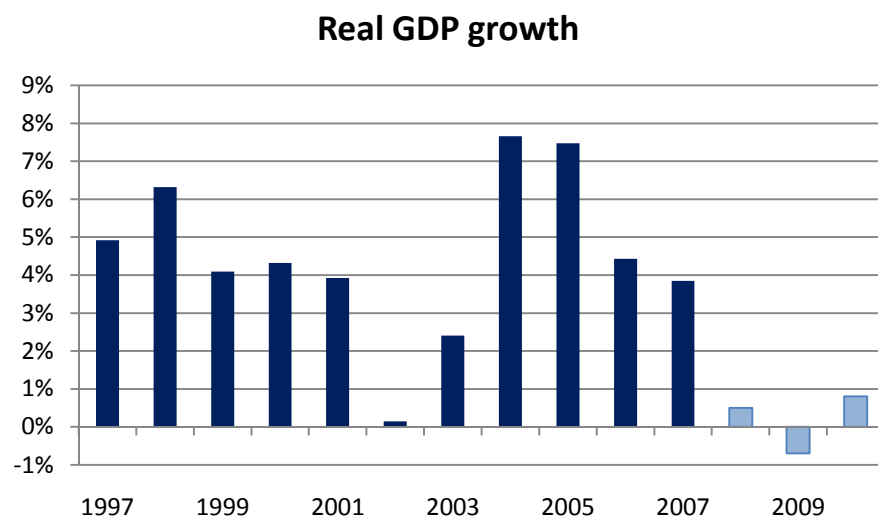


Source: U.S. Census Bureau 2008

## Structural reforms

- Icelandic economy prosperous and flexible.
- Per-capita income growth double the OECD rate since the mid-1990s.
- 5th highest GDP per capita among OECD member countries in 2007.

Source: OECD 2008



Source: Icelandic Ministry of Finance 2008

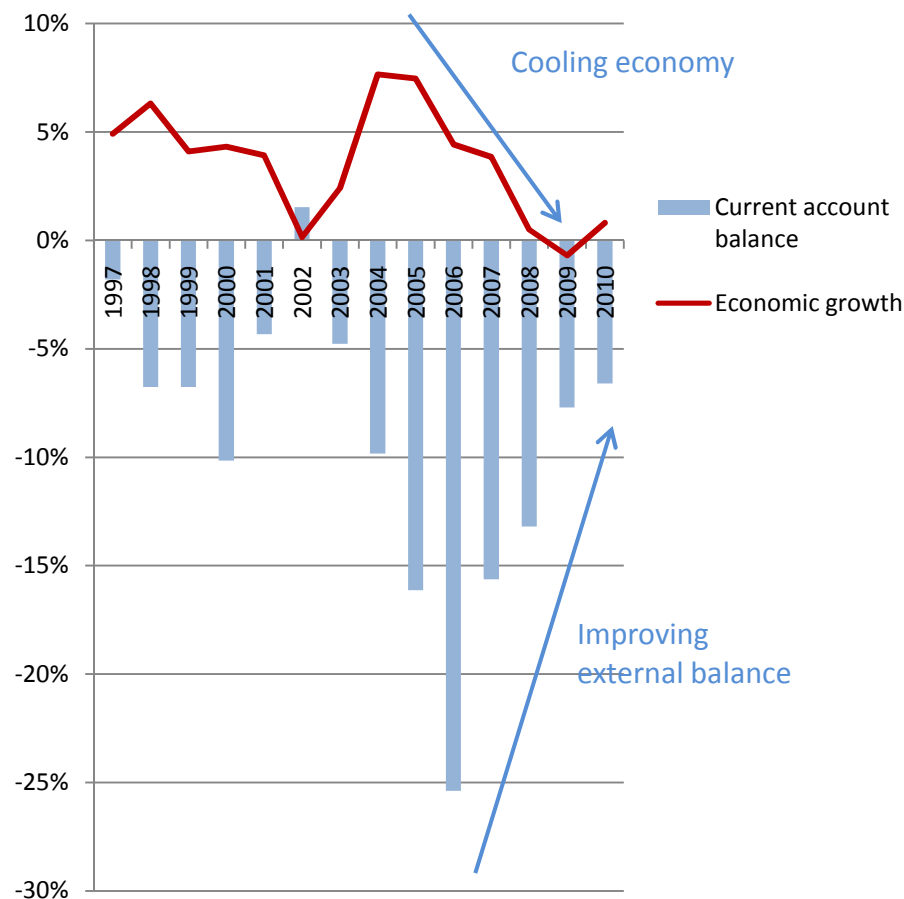
Prosperity achieved through extensive structural reforms since the mid 1990s:

- Liberalisation: In 1994 Iceland was a founding member of the EEA (European Economic Area) free-trade agreement between the EU and the EFTA nations. Agreement created a single market for capital goods, services and labour.
- Privatisation: Since the early 1990s public enterprises, including banks and telecom, have been privatised unleashing entrepreneurial dynamism.
- Globalisation: Icelandic companies strengthened by market reforms and entrepreneurialism have expanded into foreign markets (OECD 2008). Banking system becomes international.
- Personal and corporate taxes have been systematically lowered with current corporate income tax at 15% and tax on capital gains and financial income at 10%.

## Current account balance and GDP

- Icelandic economy has shown flexibility and resilience in correcting macroeconomic imbalances.
- A recent current account deficit was quickly reversed from -10.2% of GDP in 2000 to a surplus of 1.5% in 2002.
- Large current account deficit in 2003-2007 largely driven by foreign direct investment in Icelandic energy intensive industries, large-scale energy projects and booming housing market.
- Current account balance expected to improve 2008-2009 with a cooling economy and increased exports from aluminum production.

Growth in GDP and the current account

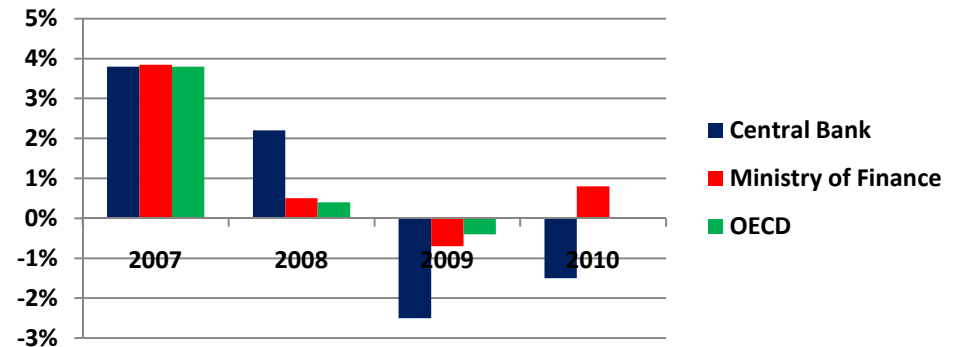


Source: Icelandic Ministry of Finance 2008

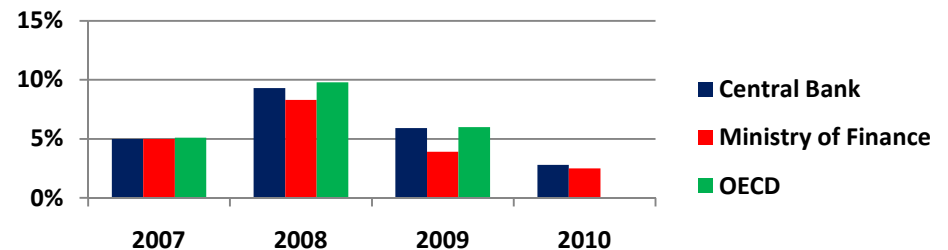
## GPD, inflation and unemployment

- Central Bank of Iceland has an inflation target of 2.5% with an upper and lower limit of 1-4%.
- Booming economy because of energy and aluminum projects and housing market fuelled domestic demand giving rise to persistent inflationary pressures 2003-2008.
- Tight monetary policy has raised Central Bank interest rates to 15.5%. Cooling economy and housing market expected to reduce inflation which will create conditions for a Central Bank rate cuts in late 2008.
- Inflation expected to decrease and employment condition to ease as the economy cools 2008-2010.

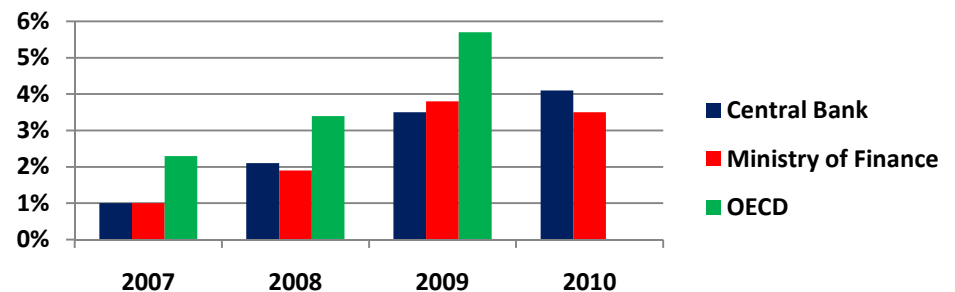
### GDP growth 2007-2010



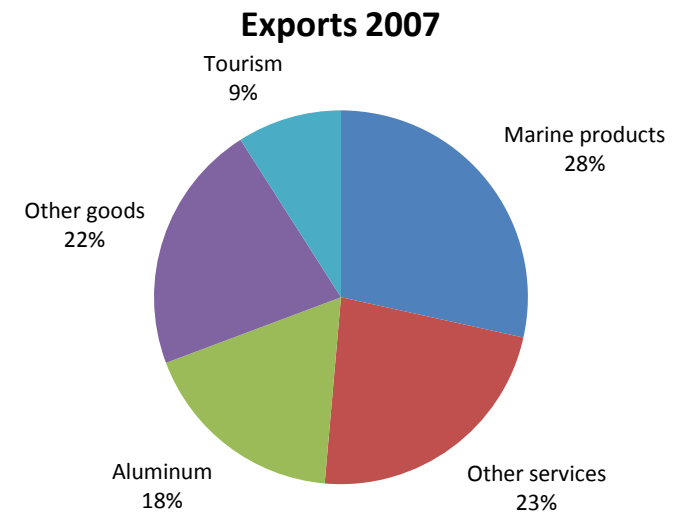
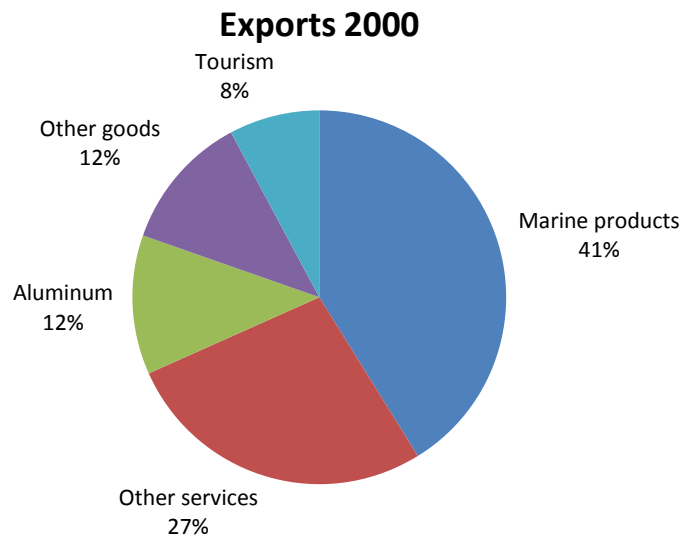
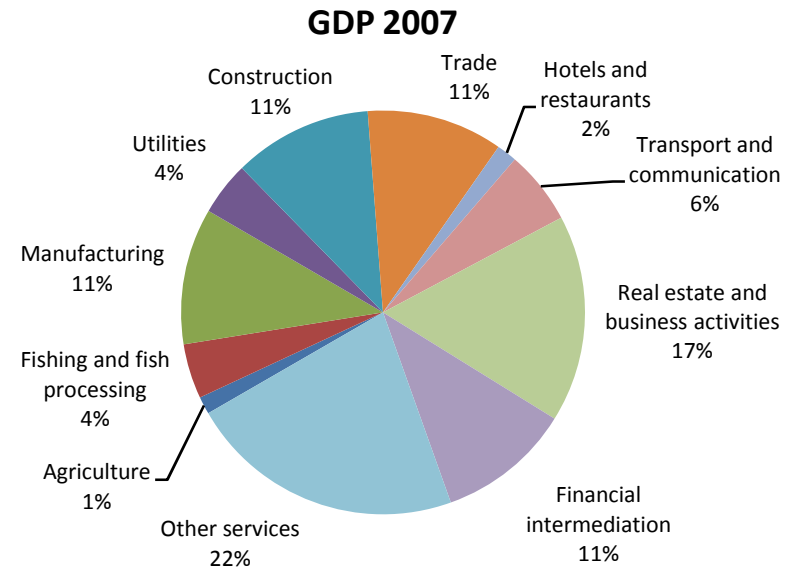
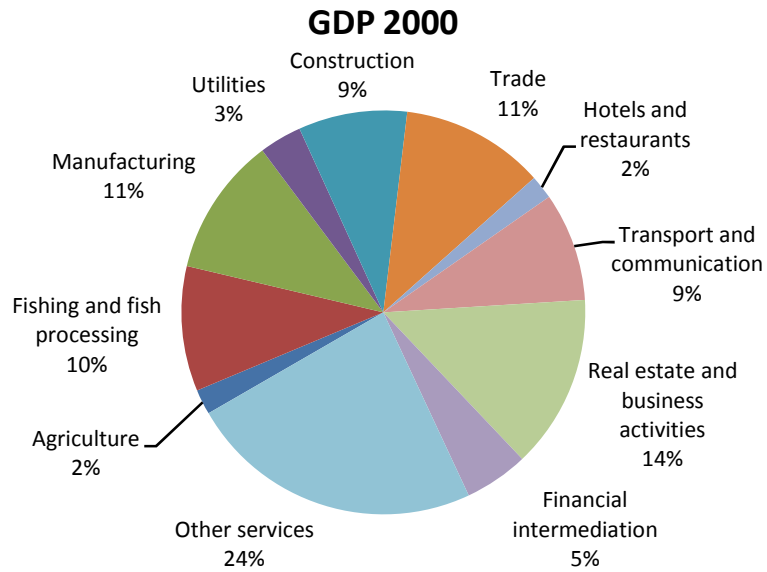
### Inflation 2007-2010



### Unemployment 2007-2010



## GDP and export diversity



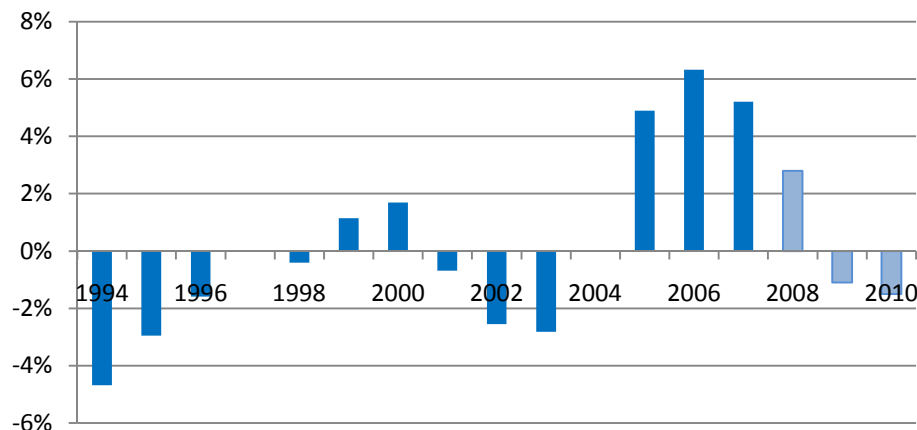
Source: Statistics Iceland 2008

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## Fiscal position

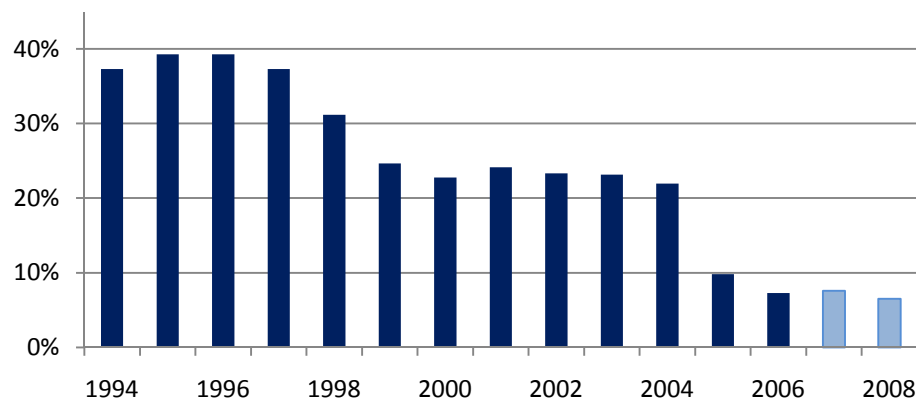
- Strong counter-cyclical fiscal structure established in the last decade.
- Economic prosperity allowed public sector debt to decrease considerably since 1996.
- Public sector net debt is expected to decrease further and reach 6.5% of GDP in 2008.
- Gives the Icelandic economy sufficient strength and ample breathing space to weather turmoils in international markets.
- “Moody’s believe there is a high degree of sovereign willingness to support the banking system because of the inherent importance of financial intermediation to the economy...”  
“...The government, central bank, or any other public or private institution so designated can mobilise whatever financial assets are necessary to handle a severe problem.” (Moody’s 2008)

Public sector financial balance - % of GDP



Source: Icelandic Ministry of Finance 2008

Public sector net debt - % of GDP



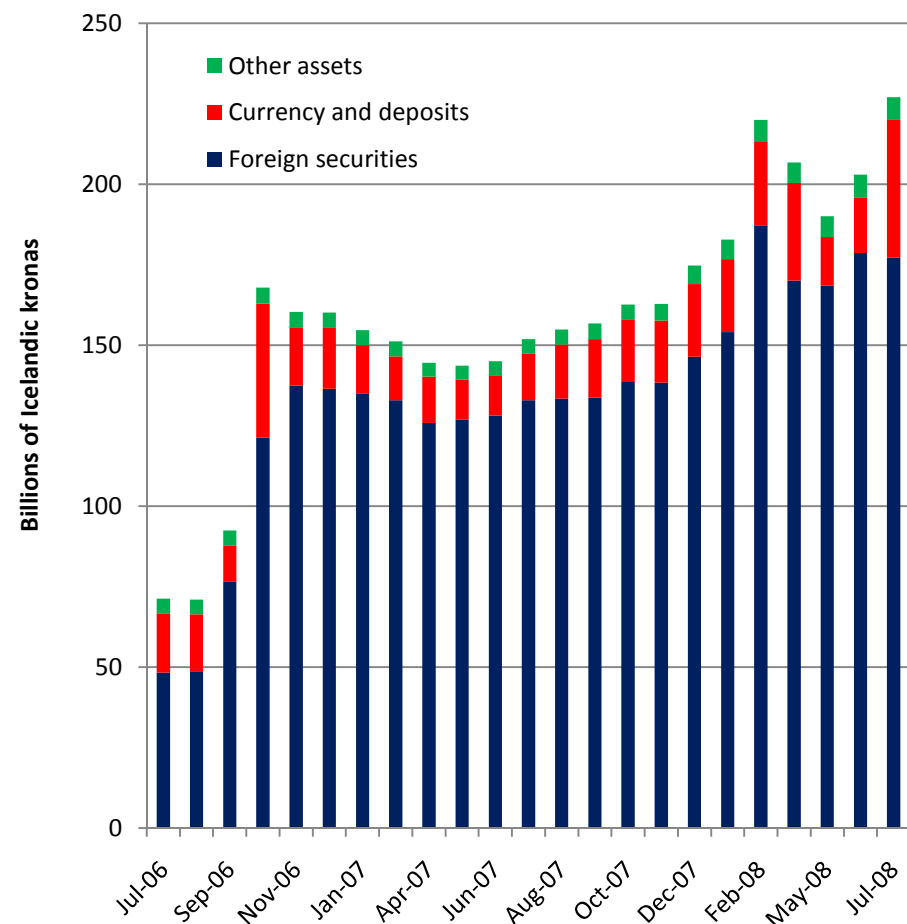
Source: Icelandic Ministry of Finance 2008

## Foreign currency reserves

- Foreign currency (FX) reserves of the Central Bank of Iceland have more than doubled since 2006.
- In May 2008 the Central Bank of Iceland entered into a euro/Icelandic krona bilateral swap facility agreement with the Central Banks of Sweden, Norway and Denmark, securing access to 1.5 billion euros in total.
- Government of Iceland to borrow up to 500 bn ISK in 2008 to strengthen current FX-reserves of the Central Bank.

### Foreign currency reserves

(positions at the end of each month)

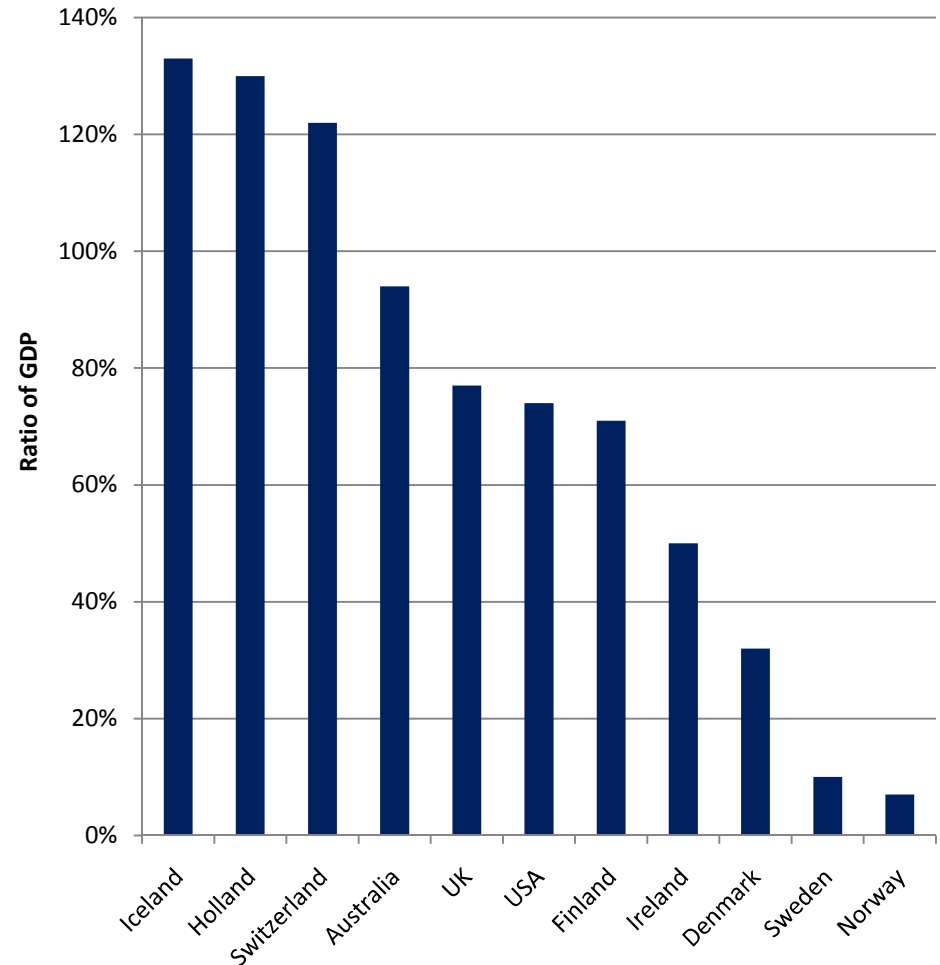


Source: Central Bank of Iceland  
2008

## Icelandic pension system

- Iceland has an almost fully funded pension system. (Moody's Mar 2008)
- Assets of the Icelandic pension system 133% of GDP in 2006, highest ratio in OECD countries. (OECD 2007)
- "Mandatory employer contribution rate was increased by two percentage points in early 2007, which will further stimulate pension asset accumulation in Iceland." (OECD 2007)
- Young population and strong workforce will further strengthen the Icelandic pension system.

Assets of the pension system as % of GDP

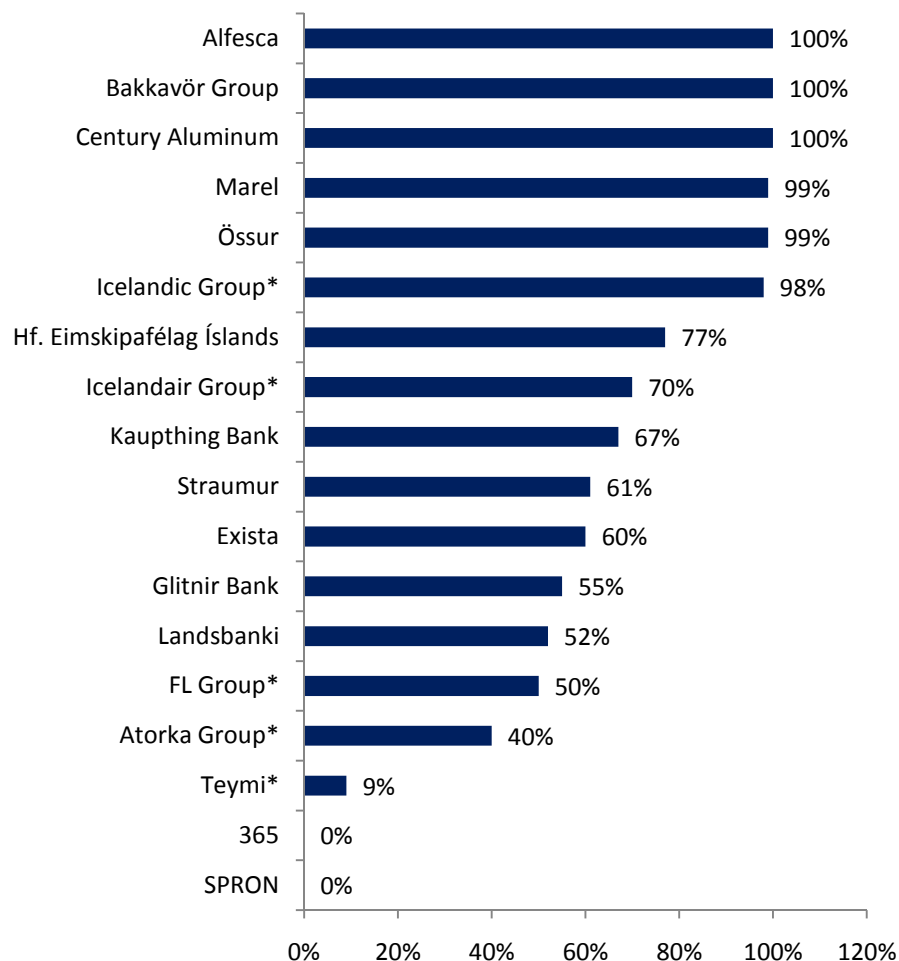


Source: OECD 2007

## Where does the money come from?

- Iceland is endowed with ample renewable resources with fertile fishing grounds laying the basis for GDP growth in the 20th century.
- Establishing private property rights for all fishing resources in 1990 (individual transferable quota system) released large amounts of capital.
- In 2007 Iceland had untapped over 75% of its renewable energy potential in hydro- and geothermal power attracting foreign direct investment in energy intensive industries.
- Strong pension funds provided capital for foreign investments.
- Privatisation of the banking system made new sources of financing available for companies wishing to expand their operations.
- Icelandic companies used international credit markets to fund further expansion abroad.

**Foreign earnings in 2007 as % of total income of largest OMXI15 corporates**



Source: Year-end reports 2007, \*Estimates by Landsbanki Research Jan 2008

## Summary

- Icelandic ranks high in an international perspective with first-rate living standards, competitiveness, low corruption and high economic freedom.
- Structural reforms in the 1990s laid the foundations for higher levels of economic prosperity.
- Iceland's ample green and renewable energy reserves will continue to attract foreign investments in energy intensive industries.
- Economy continued to diversify 2000-2007 with growth in energy intensive industries and financial services.
- Tight monetary policy, cooling economy and growing export revenues will restore macroeconomic balances.
- A fully funded pension system
- Sound fiscal position and low public sector indebtedness give Iceland ample breathing space to weather current market turmoils.

## Selected websites

Prime Minister's Office – [www.forsaetisraduneyti.is](http://www.forsaetisraduneyti.is)

Ministry of Finance - [www.fjarmalaraduneyti.is](http://www.fjarmalaraduneyti.is)

Central Bank of Iceland - [www.sedlabanki.is](http://www.sedlabanki.is)

Statistics Iceland - [www.hagstofa.is](http://www.hagstofa.is)

Financial Supervisory Authority (FME) - [www.fme.is](http://www.fme.is)

Icelandic Financial Services Association - [www.sff.is](http://www.sff.is)

Iceland Chamber of Commerce - [www.chamber.is](http://www.chamber.is)

Trade Council of Iceland - [www.icetrade.is](http://www.icetrade.is)

Invest in Iceland Agency - [www.invest.is](http://www.invest.is)