ICELANDIC POLICY ON COMPETITIVENESS for growth and jobs

Ministries of Industry and Commerce Ministry of Finance Iceland

September 1996

This report is mainly based on work done by the Ministries of Industry and Commerce to formulate more comprehensively the industrial competitiveness policy, in co-operation with the Ministry of Finance.

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Published by the Ministries of Industry and Commerce and the Ministry of Finance $\,$

Report 96-5

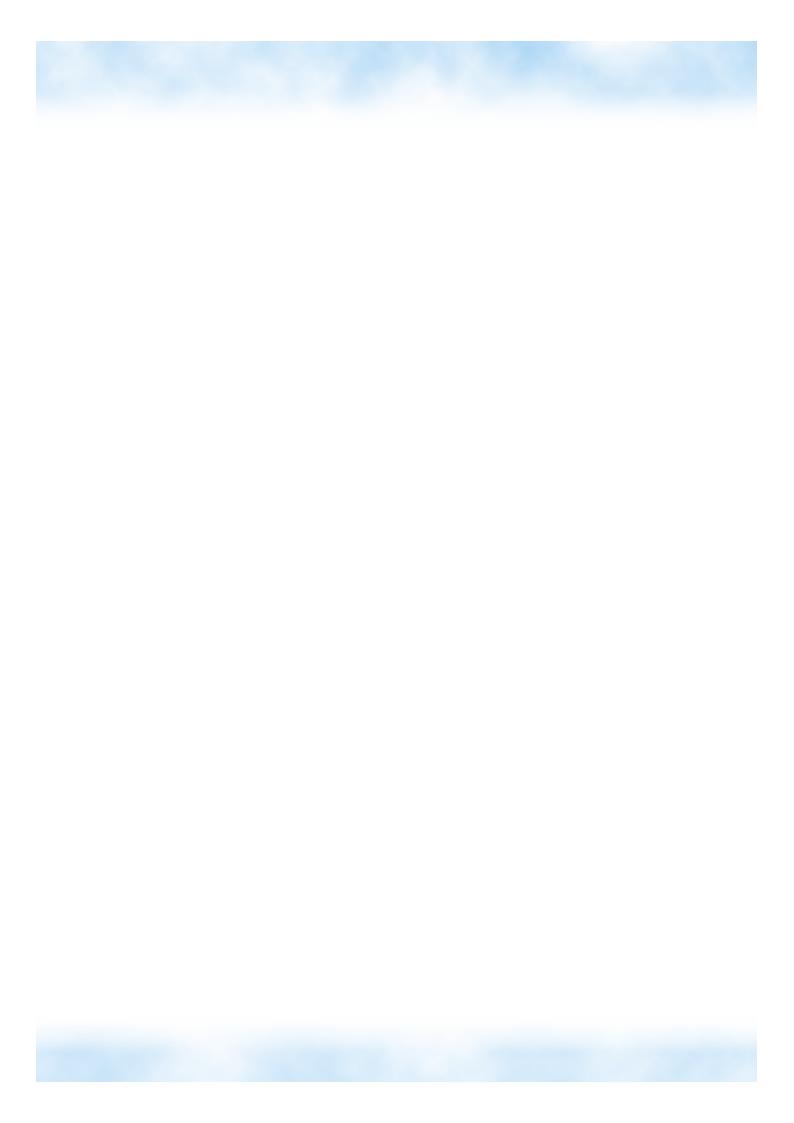
Printed in Ísafoldarprentsmiðja hf Designed by Auglýsingastofa E. Backman

ISBN 9979-871-10-5

September 1996

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Introduction

In April 1995, a coalition Government formed by the Independence Party and the Progressive Party took office. The core of the Government's economic policy is to enhance the macroeconomic environment in general and to ensure thereby growth and employment. Due to the size of the economy and other factors as well, the competitiveness and industrial policy are more or less incorporated into the overall macroeconomic policy.

However, there is a growing interest in giving higher priority to formulate a more comprehensive policy on industrial competitiveness and technological advancement than before. This can be seen in various actions taken by the Government and the Ministries, e.g., by the Ministries of Industry and Commerce and the Ministry of Finance and other Ministries as well.

This interest is demonstrated in various areas like the general economic policy, small and medium-sized enterprises (SMEs), financial market reform, institutional framework in R&D, international co-operation, general support for industry, investment and venture capital, policy on competition, regulatory reform, reform of the tax system,

diffusion of technology, research and development, information technology, energy policy measures, export-related support, trade and foreign investment, privatisation, labour-related measures and vocational training, as well as measures to protect the environment and regional development policy measures. These policies will be clarified in later sections.

Publication of this paper is just one step in the process of giving higher priority to competitiveness policies in general and to formulate a more comprehensive policy. Special attention will be on economic and industrial factors, as well as linking macroeconomic and microeconomics factors better than before.

This paper is mainly based on work done by the Ministries of Industry and Commerce to formulate more comprehensively the industrial competitiveness policy, in co-operation with the Ministry of Finance. The aim of this publication is to make a contribution to the formulation of the industrial competitiveness policy, stimulating growth and employment.

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Minister of Industry and Commerce

Friðrik Sophusson Minister of Finance Icelandic Policy on Competitiveness for growth and jobs

Ministries of Industry and Commerce

Ministry of Finance

I Competing in a Global Economy

I.1 The Economy

Iceland is the second largest island in Europe, located in the North Atlantic Ocean, measuring 103,000 km², or slightly larger than Ireland, with a population of 270,000. Because of the Gulf Stream, Iceland enjoys a warmer climate than its northerly location would indicate.

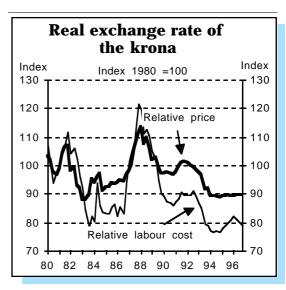
The Icelandic economy is largely based on the use of renewable natural resources, the most important of which are the coastal fishing stocks, hydro-electric and geothermal power and the grasslands which support the livestock. The economy, traditionally based on fisheries and agriculture, has during the last few decades, diversified into manufacturing, processing and service industries, while at the same time diversifying its marine sector.

I.2 Structural changes

Extensive structural changes have taken place in the Icelandic economy in the last decade, bringing stability to an economy ravaged by high inflation and unstable economic growth. In the early eighties, economic policy was loose, culminating in 1983 when inflation reached its peak of over 80% per annum. This was followed by a rapid unsustainable expansion in the economy especially in the period 1985-1987. Large wage increases, not supported by productivity increases, caused, inter alia a sharp rise in the real exchange rate of the króna.

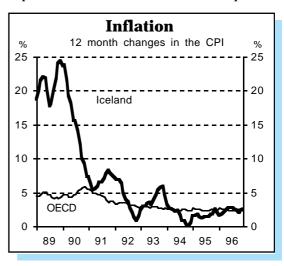
This led to heavy losses by many enterprises which consequently were forced into extensive restructuring, followed by a wave of mergers or, alternatively, the firms went under. In addition, real interest rates rose steeply, after having been negative for a long time, following a liberalisation of the financial market. Finally, in 1988 a period of economic

stagnation set in, led by falling fish prices and reduced fish catches.



In reaction to this development, the government helped pave the way in developing a strong ground for continued growth by stabilising the inflation rate as well as the economy through tight fiscal and monetary policy and market liberalisation.

Taxes on firms were lowered, the capital market was fully liberalised and government expenditure was curtailed. As a consequence,

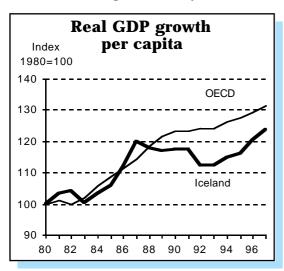


interest rates fell. Furthermore, the real exchange rate of the króna has been brought down, i.a., through a sharp lowering of inflation and wage restraint. Although unemployment has increased, it is still far below that of most industrialized countries.

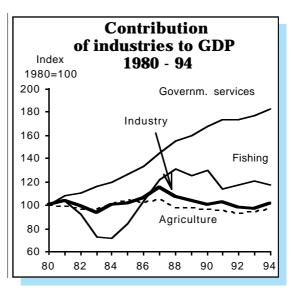
The structural adjustment continues and earlier this year two acts of law concerning the labour market took effect, which aim for greater flexibility on the labour market and hence for a more competitive and productive economic environment.

I.3 Current economic outlook

Following a period of stagnation from 1988 through 1992, partly due to restrictions on fish catches and a deterioration in the terms of trade, economic growth slowly resumed in



1993, when growth in the GDP measured nearly 1 per cent. The year 1994 was favourable for economic development, when GDP grew by $3\frac{1}{2}$ per cent, driven by a strong pickup in exports of goods and services, leaving a record surplus on the current account of 2 per cent of GDP. Economic growth slowed a little in 1995 and measured 2 per cent. The growth was largely led by a strong pick-up in domestic demand of $4\frac{1}{2}$ per cent. The current account continued to show a surplus of nearly 1 per cent of GDP.



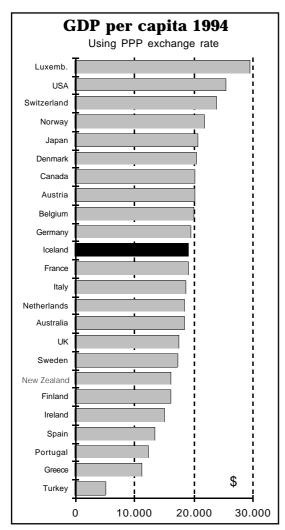
A strong growth is foreseen for 1996, led by a strong increase in private investment. Private consumption growth is also expected to remain robust at over 6 per cent. GDP growth in 1996 is currently estimated at 4½ per cent, with a growth in investment of 20 per cent. Economic growth is expected to continue in the coming year, although at a slightly slower pace.

Continued economic stability is foreseen in the medium term with stable economic growth, similar to that of the other OECD countries, low inflation and falling unemployment.

I.4 Gross domestic product per capita

In 1980 Iceland ranked fifth among the OECD countries in GDP per capita. Due to stagnating economic growth and high inflation, by 1990 Iceland had fallen to eighth place. From 1990 to 1994 Iceland's ranking continued to decline as the economy contracted, but now more aggressively than before, and had reached 11th place, with USD 19,270 per capita in 1994, based on the PPP exchange rate. In 1995 the status was more or less the same as in 1994.

Although economic stability with low inflation has now lasted for half a decade, this is not a long time in which to build up the com-



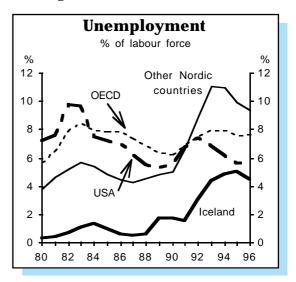
petitive advantage of companies, industries or the economy in general. Long-term economic stability is essential for strengthening the competitiveness of companies in Iceland, for the creation of growth and jobs.

I.5 Wages, prices and employment

In the past few years, inflation has been sharply reduced and is now in line with the inflation rates of other OECD countries. In 1994 and 1995, inflation was moderate with consumer prices rising by $1^{1/2}$ -2% with an estimated rise of $2^{1/2}$ % in 1996, in spite of considerable wage increases both in 1995 and in 1996. Food prices have risen far less, i.a., due to greater competition and lowering of the

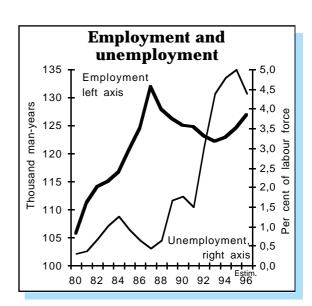
VAT on food products in the beginning of 1994.

The wage level has also remained relatively stable. General wage agreements stipulating moderate wage increases have been in effect in Iceland since 1990. To facilitate the signing of new agreements, the Government has at times agreed to certain fiscal concessions,



including lowering the VAT on food products.

The general wage agreements contribute to more stable production and stronger investment growth, without eroding the competitive position of industry, thus leading to increased employment.



After a continuous decline since 1987, employment started to grow in 1995. Consequently, the rise in unemployment has been halted and has fallen from a peak of 5 per cent in 1995 down to roughly 4 per cent.

For decades, unemployment was nearly nonexistent in Iceland. In the early nineties, however, unemployment crept up slowly, although still low in comparison to other countries.

As in other countries, the hardest hit are those with only elementary education and young people with little work experience. Also, there has been a marked increase in long-term unemployment.

Labour force participation rates in Iceland are relatively high compared to other countries, especially female participation rates. The total participation rate measures 80 per cent in Iceland, while it measures around 65 per cent in the EU and roughly 75 per cent in Japan and the U.S.A.

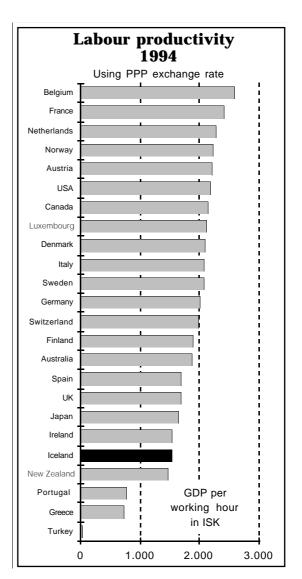
With both stable prices and wages, the real exchange rate has fallen markedly, both in terms of relative consumer prices and unit labour cost. This has improved the competitive position of domestic companies and stimulated growth, both for exporting companies and companies operating on the domestic market.

I.6 Labour productivity

Productivity - a key indicator of economic efficiency - is one of the basic factors for improving the standard of living.

However, problems connected with concepts and measurement of production, labour and capital make it difficult to obtain a quantitative indicator of productivity. Still, measures of productivity give important indications of the competitive position of companies, industries and the economy, as well as the standard of living.

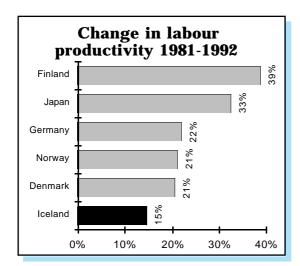
In international comparison, value added per working hour is generally used as a measure of productivity. A comparison of the



level of labour productivity across countries in 1994, indicates that labour productivity in Iceland is among the lowest within the OECD countries in 1994, with Iceland in 20th place. Belgium, which ranks highest, has a labour productivity which is 67% higher than Iceland's.

Furthermore, the productivity growth from 1981-1992 has not been favourable in Iceland in comparison to other countries.

Productivity trends are influenced by many factors both external and internal of companies. The slow productivity growth in Iceland in the past few years reflects mostly the economic situation, affected e.g. by changes in



reduced fish catches, in an economy operating in many cases within a set of strict rules and regulations.

However, productivity will be the basic factor for improving the standard of living in the coming years.

Increased productivity is therefore the challenge that has to be met to improve the standard of living.

I.7 Profitability of industry

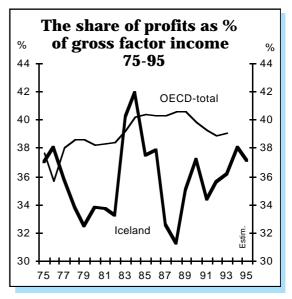
The profitability of industry in general has been rather poor since 1977 compared with other countries, although the profitability has improved somewhat in the last few years. The share of capital in gross factor income (the profit ratio) has on average been close to 35 per cent. It rose considerably in 1989 and 1990, declined in 1991, but rose again in 1992 and 1993 and reached 38 per cent in 1994, its highest level since the period 1983-1986.

The profit ratio is estimated at 37 per cent for 1995. The profit ratio is intended to provide an indication of the distribution of the value added created in the economy between labour and capital. The ratio for Iceland is considerably lower than that for the OECD as a whole, which averages close to 40 per cent.

The profit ratio differs from the profit concept that appears in the annual accounts of firms in that the profit ratio includes the wages

of the self-employed, real interest charges and depreciation. Of these, the real interest rates are the most significant as they fluctuate widely from one year to the next.

Real interest rates rose steeply from 1980 and became positive, after having been negative for a long time, as the financial market was gradually liberalised.



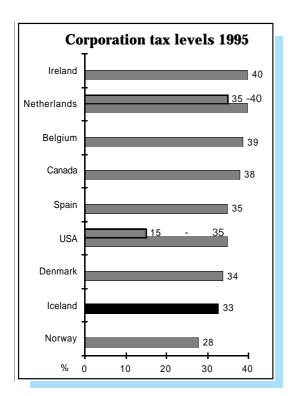
This resulted in even lower profit in firms after 1980 than the chart indicates.

I.8 Taxes on corporations

In the past few years, the tax system in Iceland has been subject to a complete overhaul. The main aim has been to bring the tax system in line with that of other European countries in light of the increased international co-operation and competition.

Corporations are subject to income tax, with a rate of 33%, which ranks among the lowest among OECD countries. Furthermore, dividends of up to 7% of the nominal value of capital stocks are deductible from taxable income. A tax on net assets less nominal value of equity, of 1.45% is also levied on corporations, while municipalities generally levy a real estate tax.

In 1991, five separate levies on wages, payable by the employer, were replaced with a single social security tax, which is currently levied on total wage cost. The social security tax is levied at two different rates, $3^{1/2}$ % on



agriculture, fisheries, manufacturing, hotels and restaurants and 7% on other sectors.

Iceland also levies a value added tax (VAT) with a general rate of 24½, with a lower rate of 14% levied on food, heating, books, magazines, newspapers, user fees for radio and television, and hotel services.

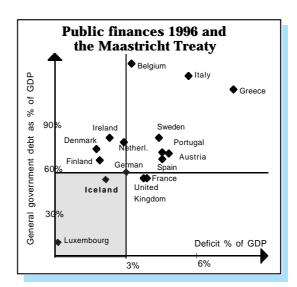
When Iceland entered the EEA, all import duties on industrial goods imported from countries within the EEA were abolished. At the same time, import duties levied on goods imported from countries outside the EEA were lowered. Excise duties are levied on a range of industrial goods at varying levels.

A 10 per cent withholding tax on capital income will be introduced in the beginning of 1997. All capital income, such as interest income, dividends, capital gains and rent will be subject to a uniform taxation of 10 per cent.

I.9 The public sector

General government expenditure amount to less than 40 per cent of GDP, while the general government accounts for over 60 per cent of GDP in Sweden and Denmark. Germany, France and Italy follow with a ratio of around 50 per cent of GDP.

As in most other OECD countries, the Treasury has been run with a persistent deficit, leading to a build-up of public debt. Since 1991, however, extensive structural changes have been implemented in the central government to improve its operation. The efficiency of the system of tax collection has been improved and special efforts have been made to reduce tax evasion. On the expenditure side framework budgeting has been introduced. Efforts have been made to



curtail automatic expenditure increases and emphasis has been laid on privatisation, corporatisation and contracting out. Furthermore, the personnel policy of the central government has been reviewed in order to bring it more in line with the situation on the private market. The current government declared in 1995, that the central government would be run with a balanced budget in 1997 and a budget proposal to that effect will be presented in October.

Until now, the operation of the elementary school system in Iceland has been divided between the central and local governments. Starting in the autumn of 1996, local governments will have sole responsibility for the operation of the elementary school system.

Of the eighteen member countries of the EU and EFTA, only four satisfy all of the four Maastricht criteria for entering the third phase of economic monetary union. These include relatively low inflation, low interest rates on government bonds as well as limited general government deficit and limited public debt. Iceland as well as the other EFTA countries satisfies the criteria, along with Luxembourg, the only EU country to fulfill all the criteria.

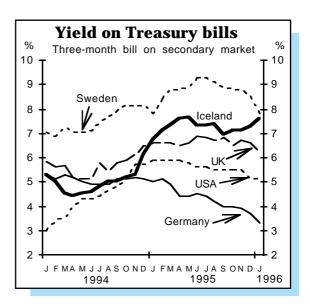
I.10 Monetary developments and structural changes

The financial market has developed very rapidly in recent years as it has been liberalised and restrictions on capital movements between Iceland and other countries have been removed.

In 1995 the last of the restrictions on crossborder financial asset transactions was abolished, thus concluding a gradual process of deregulation in the financial market.

In the middle of the 1980's, interest rates were liberalised; a securities exchange, the Icelandic Stock Exchange, was established; securities companies emerged; and mutual funds were established. At the end of the 1980's important mergers of financial institutions took place, when the number of commercial banks fell from seven to three. At the beginning of the 1990's the rules governing foreign direct investment were liberalised and the Government adopted a policy of a phased elimination of restrictions on foreign exchange.

Iceland's membership of the European Economic Area ensures open access to the markets of the European Union. It has also meant that Icelandic legislation has in many respects been adjusted to European Union legislation.



In the last few years, domestic interest rates have fallen. This is due to several factors, such as greater stability in the economy, lower inflation rates and structural reform of the financial markets.

Although extensive deregulation has taken place in the financial sector, a large part of the banking system is still in the hands of the central government. Of the four commercial banks operating in Iceland two are state-owned. However, the Government plans to incorporate the state-owned banks during it's term in office.

Investment credit funds play an important role in the Icelandic financial system. They are for the most part government owned institutions and are involved in providing long-term investment capital to enterprises. They finance their activity through either bond issues in the domestic market or through borrowing abroad. The Government plans to incorporate the most important state-owned investment credit funds.

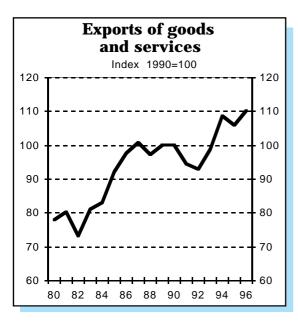
Pension funds are the single most important source of long-term capital in

Iceland. Membership in pension funds is mandatory for wage earners and self-employed people. The pension funds are independent non-governmental entities. They invest mainly in government guaranteed securities but have gradually begun to diversify into private bond issues, equity capital and foreign securities.

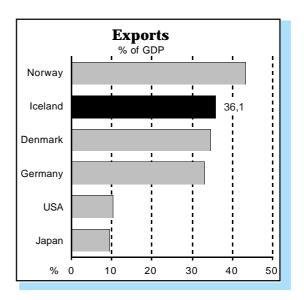
With the liberalisation of the financial markets there have been significant changes in new issue activity. For a long time the government was the only issuer of bonds in the market. As the market developed and was deregulated, other borrowers, such as local governments, financial institutions and private companies, began to enter the market.

I.11 Foreign trade

As a result of low inflation and subdued wage development in Iceland in the last few years, the real exchange rate of the króna has fallen. Consequently the competitive position of Icelandic industry has improved. Thus, following a period of falling export volume, exports started to increase in 1993 with even stronger growth in 1994.



Although fish products remain the main exports, the strongest growth has been experienced in exports of light industrial goods, especially pharmaceuticals, and various products used in the fisheries. Export volume fell slightly in 1995, but is picking up again this year and continued growth is foreseen in the coming year.

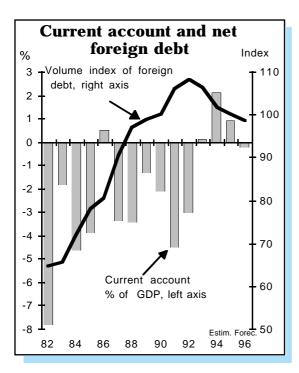


After a slack in 1992 and 1993, imports started to pick up in the middle of 1994, and have been growing ever since. This is mostly attributable to stronger growth in domestic demand. This year, imports of automobiles have grown extensively, as have imports of investment goods.

The growth in exports preceded the growth in imports, leaving a surplus on the current account in the period 1993-1995, up to 2% of GDP in 1994. With stronger domestic demand, however, the surplus has been diminished and is expected to be negative in 1996 and 1997, partly due to the enlargement of the aluminium smelter.

I.12 Foreign debt

In the years 1987-1993 net foreign debt rose from 40% of GDP to 55%. At the same time,



debt service payments doubled and culminated in 1994, when they reached 35% of export revenue.

Since then, as the result of a stronger external balance, foreign debt has been declining. The ratio of foreign debt to GDP (public and private) has fallen to 50% in 1995 and is expected to fall further this year. Debt service payments have also fallen and are currently estimated to amount to roughly 20% of export revenue in 1996.

Simultaneously, there have been extensive changes in the composition of foreign debt holdings. While corporations and financial institutions have been lowering their foreign debt, the central government debt has risen. This is mostly due to the Government's explicit policy of supporting the low level of domestic interest rates.

Thus, the central government has increasingly borrowed abroad, while the private sector has shifted its borrowing to the domestic market.

II The Economic and Fiscal Agenda

Following a general election in April 1995, a new government took office. It is a coalition between the Independence Party and the Progressive Party, led by Prime Minister Davíð Oddsson, the leader of the Independence Party.

The core of the Government's economic policy is to strengthen economic stability to ensure continued growth and increased employment without endangering the current price stability and to continue to lower the level of foreign debt.

In the past few years, inflation has been sharply reduced and is now in line with the inflation rates of other OECD countries. Interest rates have fallen as a result of tight fiscal and monetary policy and deregulation of the financial market. Although unemployment has increased, it is still far below that of most industrialized countries. It is imperative that this achievement be sustained. A credible fiscal policy is seen as a prerequisite for a further lowering of interest rates, encouraging private investment and thereby enhancing economic growth and increasing employment.

The Government aims to eliminate the central government budget deficit in 1997. A balanced budget would create the prerequisites for a decline in real interest rates and ensure the stability of the exchange rate of the króna. To reach this goal, expenditure restraints must be practised, as the tax incidence will not be raised.

The Government advocates a marketoriented policy. To implement this policy, further structural changes in the financial markets are proposed, most importantly to incorporate the state-owned commercial banks and investment credit funds. Efforts will be made to seek new opportunities for Icelandic products and services on foreign markets, to establish co-operation with foreign enterprises and nations, and to attract foreign investment in Iceland. In connection with this, efforts will be made to stimulate equity investment and further enhance the competitiveness of Icelandic enterprises. In the fishing industry, catch quotas will constitute the principal system. Efforts will be made to incorporate provisions into Iceland's constitution to the effect that marine resources shall constitute a communal asset of the nation, and that fisheries management and fishing rights shall be decided by law.

For future growth of the Icelandic economy, the Government propose to increase the role of education as well as the advancement of research and development and encouragement of supplying venture capital to growing enterprises.

The new information technology will be utilized for the benefit of economic progress, industrial development, scientific research, the arts and cultural affairs of all types. The Government also proposes to increase the efficiency of the public sector and enhance the competitiveness of the private sector.

The policy statement of the Government

The main economic policy objectives of the Government are as follows:

- ⇒ To maintain economic stability and improveconditions for economic growth.
- ⇒ A favourable exchange rate and interest rates comparable to those in the countries of our principal competitors form the basis of a strong economy and are the prerequisites for increased employment. Increased investment and new ventures will serve as measures to work against unemployment.
- ⇒ To attain a balanced budget during the Government's term in office. Emphasis will be put on thrift and putting welfare on a more secure base. For this purpose, it is imperative to halt automatic outlays from public funds.
- ⇒ Systematic changes will be initiated for the purpose of maximum utilization of funds appropriated for the health service and education, individual industries and public construction projects.
- ⇒ A study will be made of whether pension funds are able to take over certain aspects of the social security system.
- ⇒ Talks will be initiated with municipal authorities on their serious budget deficits and ways of dealing with this problem.
- ⇒ To ensure stable and solid operating conditions for exporting sectors and to promote new initiatives and progress in product development and marketing.
- ⇒ To initiate co-operation with the social partners on a review of the tax system with the aim of reducing tax evasion, lowering marginal tax rates, simplifying the tax system and promoting equality.
- ⇒ The tax environment of enterprises will be on a par with the best in the countries of our competitors. Thus no exceptional taxation arrangements will be required as incentives for increasing the number of foreign companies operating in Iceland.

III Policy on Industrial Competitiveness and Technology

III.1 The policy on industry and technology in general

The main element of the national economic policy is to enhance the macroeconomic environment in general. Due to the size of the economy and other factors as well, the policy on industry and technology is more or less incorporated into the macroeconomic policy. However, there is a growing interest in giving higher priority to industrial competitiveness and technological advancement and to formulate the policy more comprehensively than before. This can be seen in actions taken by the Government in recent years, e.g., by the Ministry of Industry and Commerce, Ministry of Education and Ministry of Finance.

In late 1992, the Minister of Education and Science appointed a committee to formulate an overall science and technology (S&T) policy. The Government issued a declaration on science policy in September 1993. This declaration is instrumental for the present policy and resulted, e.g., in new legislation reforming the S&T advisory council systems taking effect in 1994, and in several other measures to reinforce the country's S&T infrastructure.

Late in 1992 the Minister of Industry and Commerce appointed a committee to review the government support system for promoting innovation. The committee delivered its recommendations in late 1993. Some of the recommendations have already been implemented and others are under way.

There is also a growing interest within the public sector and the private sector as well, to formulate a more comprehensive competitiveness and industrial policy than before. For this purpose, the Minister of Industry and Commerce appointed a committee to analyse the framework conditions for manufacturing,

which presented its recommendations in 1994, and another committee to analyse the links between the fisheries and the manufacturing sector, which submitted its recommendations in October 1995. In 1995, the Minister of Industry and Commerce also appointed a special committee to analyse and provide recommendations to stimulate the growth of small and medium sized companies and the competitiveness of industry in general.

Various other actions have been taken, for example in the energy sector, by stimulating foreign investment and use of the country's hydropower resources, and appointing a committee to provide recommendations concerning the information society.

Various actions have been taken by the Ministry of Finance to improve competitiveness. A special emphasis has been laid on improving the efficiency of the public sector, through a privatisation programme and increased use of tenders in purchasing. The Minister of Finance also appointed two committees with representatives from the business community, which together presented their recommendations on how to improve Iceland's competitiveness.

The present coalition Government of the Independence Party and the Progressive Party, in office since April 1995, has announced its intention to implement an active policy on economic, technological, innovative and industrial competitiveness in general. These policies will be clarified in later sections. ¹

III.2 International co-operation

Iceland is an active participant in international and regional co-operation. International organisations and fora to which

¹ The Policy Statement of the Coalition Government of the Independence Party and the Progressive Party. The policy statements throughout the text are excernts from this document.

Iceland belongs include the OECD, GATT, WTO and the European Economic Area, (EEA) as well as such diverse organizations as the United Nations, NATO, the Nordic Council, the Nordic Investment Bank, the International Monetary Fund and the World Bank.

Iceland is one of the founding members of the Organization for Economic Co-operation and Development (OECD) and is a signatory to the OECD International Capital Codes. Iceland became a contracting party to the General Agreement on Tariffs and Trade (GATT) in 1964 and is a founding member of the World Trade Organization (WTO).

Iceland joined the European Free Trade Association (EFTA) in 1970 and entered into a free-trade agreement with the European Community (now the European Union, EU) in 1972. In May 1992 the member countries of EFTA and the EU signed an agreement to establish the European Economic Area (EEA). This free-trade zone, which now comprises eighteen countries, came into effect on January 1, 1994. The member countries of the EEA are Iceland, Denmark, Finland, Sweden, Norway, the UK, Ireland, France, Germany, Italy, Greece, Portugal, Spain, the Netherlands, Belgium, Luxembourg, Liechtenstein and Austria.

The EEA Agreement provides for wideranging economic co-operation and Iceland's membership assures foreign investors of the four basic EU freedoms regarding unrestricted movement of goods, persons, services, and capital. These principles, as well as EU rules of competition apply automatically in the entire EEA. Through the EEA, Iceland is therefore a member of the world's largest market area, which with 360 million people is a larger trading group than the North American Free Trade Association (NAFTA). Iceland is committed to participate in the ongoing development of the EEA and will thereby keep in step with all basic European policies regarding trade and investment in the future.

The policy statement of the Government

- ⇒ To strengthen Iceland's relations with the European Union on the basis of the Agreement on the European Economic Area, to follow closely developments within the Union during the coming years, and to explain Icelandic interests to its member states.
- ⇒ Emphasis will be put on ensuring trade cooperation and other relations with the United States. The ideas that have been put forward on a free-trade co-operation agreement between the United States and other Atlantic states will be studied as to whether it would provide additional scope for Icelandic companies to expand their market share.
- ⇒ Emphasis will be put on seeking new markets in all parts of the world, and opportunities sought to utilize Icelandic initiative for projects abroad.
- ⇒ The opportunities for international trade offered by Iceland's membership of the World Trade Organization will be utilised. Iceland's membership of NATO, and its defence co-operation with the United States, will continue to be the central point of its security policy, and emphasis will be put on increasing Iceland's participation in the overall political consultation fostered by the Alliance.
- ⇒ Emphasis will also be put on maintaining the important co-operation between the Nordic countries, and Iceland's participation in the activities of the United Nations and the Organization for Security and Co-operation in Europe.
- ⇒ Iceland will promote the establishment of an Arctic Council which will be the forum for co-operation and co-ordination of the states which have interests in the Arctic region, especially in the field of the environment and as regards the utilisation of its resources.
- ⇒ Iceland's interests concerning fisheries on the high seas must be secured through the promotion of its cause internationally and through international agreements.

III.3 General support for industry

Increased interest in the competitiveness of industry and the economy for creation of growth and jobs in recent years in Iceland has resulted in a higher priority given to formulate a more comprehensive policy than before.

General support for innovation in Iceland has in the past, however, lagged behind in many ways, in comparison to many other OECD countries, although substantial change has occurred in the area of science and research, as has already been described. This can be seen, e.g., from the OECD Review 1992, and from recommendations given by a committee appointed by the Minister of Industry and Commerce which reviewed the Government support system for promoting innovation in 1993, and in a draft report of a committee analysing the links between the fisheries sector and the manufacturing sector in November 1995.

There are many underlying causes for the shortcomings of the support system in this area in the past, e.g., economic instability in the period 1970-1990, as has been described in section I, dominance of the fisheries in the economic policy, and dominance of macrofactors in general in the economic policy, resulting in a lack of attention to the microeconomic and competitive factors in industry as well as in other branches of the economy. This is mainly the case in areas such as product development, networking, export, consulting, company start-ups, training and venture capital.

Various improvements have been made, e.g. in the field of framework conditions. Several changes have been made to the tax system, e.g., the corporate tax rate has been lowered to 33% and is now among the lowest in the OECD countries. New support programmes have been set up, while the EEA Agreement also provides for wide-ranging cooperation projects in industry as well as in

other areas. Improvements have also been carried out in the field of export and general services to industry. Special improvements will also be made in the fields of collecting upto-date statistical information on industrial activity.

The policy statement of the Government envisages improvements in industrial competitiveness and technology, as will be described in the relevant sections.

The policy statement of the Government

- ⇒ To ensure stable and solid operating conditions for export industries, and promote new initiatives and progress in product development and marketing.
- ⇒ Intensive research in the field of marine biology and productivity are prerequisites for rational fisheries management and development.
- ⇒ To promote new initiatives and progress in product development and marketing. Special emphasis will be put on improving the handling of marine resources.

III.4 Small and medium-sized enterprises (SMEs)

Most of the companies in Iceland are small or medium-sized, if such companies are classified with fewer than 250 employees, as is done in the EEA Agreement. The SME policy has therefore been included more or less in the general policy on economic and industrial competitiveness.

However, growing interest in this field results in a higher priority given to more comprehensive comprehensive policy and actions than before.

The Minister of Industry and Commerce appointed in 1995 a special committee to analyse and provide recommendations to stimulate the growth of small and medium-

sized companies and the competitiveness of the industry in general. The members of the committee are drawn from employees, employers, three ministries, the Regional Development Institute, the Venture Capital Company and a private business company. The committee has provided various recommendations to the Ministry concerning improvements in the framework for business to increase competitiveness, deregulation, etc., some of which have already been implemented.

The Minister of Industry and Commerce also launched another measure in this field in the beginning of 1996, when the programme Job Creation inititative for SMEs,was launched. The programme incorporated several older programmes and new ones as well, concerning cooperation, consulting and general support to small and medium-sized enterprises. Several other actions have taken place as well in the Ministry, e.g., on analysing and providing recommendations for sectors in industry.

The policy statement of the Government

- \Rightarrow To stimulate growth of small and mediumsized enterprises.
- ⇒ To increase the competitiveness of the industry in general through various measures.

III.5 Investment support and venture capital

No special investment support programmes are in place for industry, e.g., for investment in buildings and machinery, although there is R&D support for special investment in innovation systems. However, changes have been made in restructuring funds to stimulate innovation and venture capital. The venture capital market has also changed recently, both in a quantitative and a qualitative way,

resulting in a more advanced venture capital market. However, in spite of some increase in the last few years, the supply of venture capital is limited, especially for small and medium-sized companies.

An increased number of companies are now also registered as publicly quoted shareholding companies. Government tax deductions which allow new shareholders to deduct investment in publicly registered companies against their taxable income up to a limit are an important stimulus for increased venture capital and trade in shares.

In 1995 the Industrial Development Fund for Iceland, which was created in 1970 when Iceland entered EFTA, became totally owned by Iceland after the original capital had all been refunded in accordance with the original charter of the Fund.

During the last few years changes have been made in the laws which regulate foreign investment as well as the law concerning the capital market in general in Iceland. Financial market legislation is now more or less compatible with that in other EEA countries.

The government has therefore recently established the Invest in Iceland Bureau, which is responsible for the promotion of foreign investment in Iceland, in addition to earlier measures in place to encourage foreign investment, especially in the field of energy resources.

The policy statement of the Government

- ⇒ Through tax incentives, the public will be encouraged to put up risk capital for industry. Preparations for such amendments to the tax laws will be completed in 1996
- \Rightarrow Transformation and merging of funds.

III.6 Policy on competition

In participating in the European Economic Area, Iceland has agreed to adopt important legislation and regulations concerning the field of competition, originally passed by the European Union.

This affects the present competition policies and regulatory framework in which companies find themselves. The National Competition Board, which was set up in 1992, has made many significant rulings in matters of competition, both related to private companies as well as matters relating to competition between government bodies and the private sector.

All public purchases in Iceland above a certain limit must be offered for tender in all the EEA countries. A lower limit has been set by the Ministry of Finance for local tenders.

The policy statement of the Government

- ⇒ There will be a reduction of bureaucracy in the relations of citizens with the authorities, and unnecessary legal and regulatory provisions will be abolished.
- ⇒ To continue emphasis on improvements in the area of competition.
- ⇒ To work for restructuring in public enterprises, e.g., through increased tenders, the merger of institutions, service contracts, an amended pay system, and increased responsibility of administrators.
- ⇒ In industries in which the state competes with private enterprises, they will be placed on an equal footing.

III.7 Regulatory reform

Growing global attention is laid on regulatory reform and deregulation and in Iceland as well. Various structural reforms have been implemented in recent years in order to increase efficiency in the economy.

A new law on limited liability companies came into effect in 1995, providing clearer responsibility for the management and boards of such companies.

During the last few years some changes have been made in general concerning, e.g.,the financial market, foreign investment and competition.

As a party to the Agreement on the European Economic Area, Iceland has agreed to adopt important legislation and regulatory work originally passed by the European Union. This has far-reaching effects for competition policies and the regulatory framework in which companies find themselves. The legislation in this field is therefore more or less in harmony with the other EEA countries.

The policy statement of the Government

- ⇒ To establish rules which guarantee access by citizens to information possessed by the state.
- ⇒ There will be a reduction of bureaucracy in the relations of citizens with the authorities, and unnecessary legal and regulatory provisions will be abolished.
- ⇒ State services will be attuned to modern technology, e.g., through on-line connections of service institutions and paperless customs clearance.
- → Measures will be taken to ensure that the activities of supervisory bodies neither result in unnecessary burdens for enterprises nor in distorting competition.
- ⇒ Special emphasis will be put on the role of prevention and education in the health services, i.a. with the aim of reducing the consumption of intoxicants. A more goal-oriented co-operation and division of responsibilities will be established between the country's hospitals.
- ⇒ To promote effectiveness and increase variety in the operation of health-care facilities.

⇒ A new Social Security Act will be passed with the aim of better securing the rights of those who really need benefits. The Social Security Institute will be made more active in monitoring benefit payments and medical insurance, and the services purchased by the institute.

III.8 Reform of the tax system

In the past few years the tax system in Iceland has been subject to a comprehensive overhaul. The main aim has been to bring the tax system in line with that of other European countries. This must be seen in light of increased international co-operation and competition, especially as regards the corporate tax system in light of the integration in Europe.

The base for levying indirect taxes, which earlier accounted for three-fourths of central government revenue, had in many ways become inadequate for tax policy purposes. This was mainly due to various exemptions and deductions implemented over the years, whereby the tax base shrank. Therefore, the primary goal has been to broaden tax bases by eliminating various exemptions, together with lowering tax rates. The tax system also needed to become more responsive to economic developments by including some built-in stabilisers. This is especially important in a small, open economy such as the Icelandic one, where fluctuations are frequent.

The income tax system will be revised during the term of this Government to reduce the large marginal effects many groups face currently and, at the same time, improve work incentives. Furthermore, the Government will revise the tax system in order to encourage entrepreneurship and increase the supply of venture capital.

The policy statement of the Government

- ⇒ To initiate co-operation with the social partners on a review of the tax system with the aim of reducing tax evasion, lowering marginal tax rates, simplifying the tax system and promoting equality.
- ⇒ The tax environment of enterprises will be on a par with the best in the countries of our competitors.

III.9 Diffusion of technology

The main actors in promoting the difussion of technology are the applied research institutions, which also provide technical support services. However, this system needs further strengthening in light of the rapid technical change. In this context the Icelandic Research Council is using the Technology Fund and its international contact network to encourage companies to take part in European programmes with the aim of strengthening the base for the diffusion of technology in an international context.

The Icelandic Research Council is running an Innovation Relay Centre, an EU network, with its main objective easing the way for firms to acquire and transfer technology and to utilize R&D results. This is an important complement to domestic efforts.

The Industrial Loan Fund and the Technology Institute of Iceland have collaborated on programme for product development and enhancing productivity, offering advantages to small companies. Similar programme for export promotion are operated by the Icelandic Trade Council. The subject of the diffusion of technology is more or less incorporated in other industrial and research fields.

The policy statement of the Government

⇒ To strengthen the overall industrial, research and technological policy in general.

III.10 Institutional framework in R&D

The institutional framework within the area of science and technology has changed in recent years. The most significant change was made by the merger of the National Research Council of Iceland and the Science Council of Iceland into the Icelandic Research Council, on July 1, 1994.

The objectives of the Council include advising the parliament and government on science and technology issues; funding research projects in all fields of science and technology through two separate funds operated by the Council; stimulating efforts to participate in international co-operation including the EU's Framework Programme, and making proposals to the government for budget appropriations in science, research and development.

New guidelines were established, e.g., to stimulate increased co-operation with and participation of private companies in R&D.

Increased appropriations to the funds operated by the Icelandic Research Council do in fact result in increased support to all other research institutions through research and development co-operative projects which receive grants through competitive selection from the IRC's funds. The Ministry of Education and Science has the operative responsibility of and covers the expenses from international agreements which enable scientists in public and private research institutions to participate in, e.g., the EU Framework Programme.

Another change in the field of institutional framework within the area of science and

technology is the implementation of service contracts between the government and public laboratories. The Building Research Institute was one of the first to enter into such a service contract with the Ministry of Industry and Commerce. Contracts provide for public support at a certain level for services rendered. However, the institution is free to use its appropriation in any way it finds necessary to meet its objectives in accordance with the service contract. This reduces the previous detailed control of the institutions, personnel policies, etc., and transfers responsibility to the Board of the Building Research Institute.

The policy statement of the Government

- ⇒ To work for restructuring in public enterprises, e.g., through increased tenders, the merger of institutions, service contracts, an amended pay system, and increased responsibility of administrators.
- ⇒ Increased cost efficiency in public construction projects will be sought.
- ⇒ Efforts will be made to simplify public enterprises and at the same time make them more efficient.
- ⇒ In industries in which the state competes with private enterprises, they will be placed on an equal footing.
- ⇒ The demand will be made that state-owned enterprises yield a profit.

III.11 Research and development

In 1993, between eight and nine thousand Icelanders attended higher educational institutions, some three thousand of them in other countries — mostly in Europe or North America. This high percentage of Icelandic students studying abroad clearly adds a significant international dimension to the

somewhat homogenous Icelandic society. In a special report by the OECD, the following assessment is made: "Iceland appears...to combine an excellent general education level with a large number of students studying abroad. These features have important implications for a small economy like Iceland."²

The main forms of support for scientific research and innovation are direct government appropriation to relevant institutions. The main institutions in these fields are the Icelandic Research Council and research institutions in the fields of industry, construction, energy, fisheries and agriculture, one institution for each activity. Institutions in the field of Higher Education are also subject to public funding of R&D.

Significant project funding from the government goes through the R&D funds operated by the Icelandic Research Council. Recently the government's budget appropriations to the R&D funds have been increased as a part of the restructuring of the S&T policy and mechanisms, as mentioned earlier.

Recent statistics on R&D performance indicate an increased priority for technical change and innovation. Firms and public research institutions have increased their R&D activity recently and there is a significant shift towards a higher effort in the field of technology. The business enterprise sector is now spending more effort on R&D and should be able to meet increasing competitive pressures and add value to its operations, as mentioned in the Government policy statement. The share of R&D performed in the business enterprise sector has risen from about 10% in 1981 to nearly 31% in 1993.

Public support for sectoral research institutions, dealing with more applied research, has not increased but rather the opposite. These institutions report to the Ministries of Industry, Fisheries and Agri-

culture, respectively. These institutions have, on the other hand, come to play a more important role in R&D projects initiated by industry as BERD (business expenditure on research and development) has been increasing. The present policy emphasis competitive project funding upon application.

One of the most significant events in the EEA Agreement concerning industry, science and research, is Iceland's participation in the 4th Framework Programme of the European Union. During the 3rd Framework Pro-Icelandic researchers became gramme involved in some 15 projects. However, in response to the first call for proposals for the 4th Framework Programme, Iceland has already submitted nearly 100 applications in various fields. A significant number of these relate to information technologies and they are not particularly concerned with the traditional industries. These would indicate an emerging shift in orientation towards more diversified interests.

The policy statement of the Government

- ⇒ To ensure that everybody has the opportunity to seek education, irrespective of their place of residence or financial position.
- ⇒ Individual needs for re-training and adult education will be met.
- ⇒ The transfer of primary education to local governments will be completed in cooperation with them and teachers' unions.
- ⇒ Secondary education will be strengthened, not least vocational and practical training.
- ⇒ Intensive research and development are the prerequisites for progress in the Icelandic economy. Efforts must be made to utilize to the fullest the funds appropriated for this purpose, and ensure that both new and traditional branches of industry have equal access to research funds.

²OECD Science, Technology, and Innovation Policies, 1993

- ⇒ Continued efforts will be made for building up and developing the University of Iceland, the University in Akureyri, and arts education at the university level.
- ⇒ The Student Loan Act, and relevant regulations, will be reviewed. Assistance will be rendered to the Students' Innovation Fund, and students' participation in research projects will be increased.
- ⇒ Intensive research in the field of marine biology and productivity are prerequisites for rational fisheries management and its normal development.
- ⇒ Special emphasis will be put on improving the handling of marine resources.

III.12 Information technology

Computer networks using recent information technology are playing an ever greater role in the country's educational system, from primary schools to universities and research institutions and, of course, in economic life. This applies both within the country and in communicating with business associates, schools, libraries, etc., abroad. Country-wide high speed optical lines and technical infrastructure connect the whole country into one network with gateways to other countries using x.25, x.400, TCP/IP, etc. The users have access to tools like e-mail, WWW, gopher, ftp, telnet, nn (news), IRC, etc.

Today all major educational institutions are connected and some offer distance courses in several subjects, including a full-time B.Ed. programme using computer communication.

The establishment of ISMENNT (the Icelandic Educational Network) has been an important backbone to this development. Starting as an individual initiative for connecting primary schools in northern Iceland in the late 1980's, ISMENNT now connects more than 90 per cent of all educational institutions in the country, from primary schools to universities

and research institutions. This effort within the educational system has set an example for other sectors within society and important changes are taking place through the rapid diffusion of this technology. The Minister of Education and Science introduced information policies for education and culture, and a thorough review of the Ministry's in-house information policies has already taken place.

In Iceland there is no other direct support scheme or specifically promoted programmes for the development and the diffusion of information communications technologies. However, the National PTT service has made significant investments in satellite communications and optical fibre networks which now reach all parts of the country. Despite the lack of specific government incentives for IC technology the general computer literacy and penetration of computer technology into home and economic life seems to be relatively well advanced in Iceland. It has already started to have a significant influence on the structure and operation of companies, and on new job opportunities. The EEA Agreement provides also for wide-ranging co-operative projects in the field of information technology.

In 1995 the Minister of Industry and Commerce appointed a committee to formulate a comprehensive information and communication policy on the information society. The committee has now delivered its recommendations. The main object of the policy is to view to increase the productivity and competitiveness of Icelandic enterprises and the quality of live.

The policy statement of the Government

⇒ To formulate a comprehensive policy of cooperation with the representatives of industry on information technology and communications, with a view to increasing the productivity and competitiveness of Icelandic enterprises. ⇒ The new information technology will be utilized for the benefit of economic progress, industrial development, scientific research, the arts and cultural affairs of all types.

III.13 Energy policy measures

Iceland is the only country in western Europe that still has large resources of low-cost hydroelectric power and geothermal energy remaining to be harnessed. Although electricity consumption per capita is one of the highest in the world, only a fraction of the country's energy potential has been tapped. This plentiful supply of hydroelectric power and geothermal energy, together with suitable sites and a skilled labour force, makes Iceland an ideal location for power-intensive industries.

This situation has already attracted some foreign investors to Iceland, and export-oriented power industries now consume about half the country's electricity production. The main policy in this field has been utilisation of the large resources of low-cost hydroelectric power and geothermal energy remaining to be harnessed, with emphasis on foreign investment. Improvements will also be made in simplifying the regulatory framework in the field of electricity.

The policy statement of the Government

⇒ To work for further foreign investment in the Icelandic economy in this field.

III.14 Export-related support

Increased interest in competitiveness in industry in the last few years in Iceland has resulted in a higher priority given to a more comprehensive policy than before. Although

the support system is in general rather limited, including in the field of export, new programmes have been set up to service exports better.

In 1993 the Government launched the Reaching Out programme to encourage small and medium-sized companies to increase their marketing knowledge, with some emphasis on marketing information, promotion of innovation, value added and increase in employment. Various consulting programmes are also run by the Trade Council in co-operation with other institutions to encourage export knowledge and export in general, although these programmes have more or less no direct public financial support.

The policy statement of the Government

- ⇒ To ensure stable and solid operating conditions for export businesses.
- ⇒ To promote new initiatives and progress in product development and marketing.
- ⇒ To stimulate domestic investment abroad and consulting services.

III.15 Trade and foreign investment

Upon joining the EEA, Iceland removed all tariffs on industrial goods imported from the EEA countries. At the same time, tariffs on imports from countries outside the EEA area were lowered. Also, as a founding member of the WTO, Iceland is committed to lifting a ban on imports of agricultural goods in accordance with the agreement. Thus, there are few restrictions on the trade of goods in Iceland.

The basic principle of the Investment Act of 1991 is that non-residents are, with a few exceptions, permitted to invest freely in business enterprises in Iceland, as is shown in the above table. For foreign investors and corporations domiciled in other countries,

	Limitations on foreign investment 1995	Approved liberalisation
Fishing and primary fish processing:	Foreign investment not permitted.	25% foreign ownership permitted (indirect).
Energy development:	Foreign investment not permitted.	Hindrances abolished on January 1, 1996 in accordance with the EEA agreement.
Commercial banks:	25% foreign ownership permitted.	Foreign ownership permitted.
Airline operations: agreement.	49% foreign ownership permitted.	Permitted in accordance with the EEA
Single direct investment over the value of 250 million krónur:	Special permission needed	No special permission needed.

Icelandic legislation is aimed at creating a friendly investment environment based on national treatment, and the trend is towards full liberalisation.

Iceland's membership in the EEA represents a guarantee for foreign investors. The Agreement makes adherence to EU provisions and conditions the general norm in Iceland, thus providing for direct rights for non-national investors. A company domiciled in any of the other member countries of the EEA has the same right to operate in Iceland as an Icelandic registered company and needs only, with a few exceptions, to apply for the same permits and registration as a local company.

Companies registered in Iceland are likewise permitted to operate in all the EEA countries without any special permits or legislation. The same rules apply to the movement of labour. Citizens of the EEA countries do not need a work permit in Iceland.

Foreign investment in Iceland has remained at a very low level in recent years in spite of deregulation, but Icelandic investments overseas are on the rise. Icelandic companies involved in fisheries have set up operations or entered into joint ventures with partners in many parts of the world. They have started operations in Namibia, Mexico, Chile, Kamchatka, Vietnam, Mexico and China. Icelanders have also invested in European countries such as France, Belgium, the UK and in the former East Germany and

Lithuania. A particularly important consequence of these investments is the increased export of Icelandic technical know-how and technological products.

The policy statement of the Government

- \Rightarrow To work towards further foreign investment in Iceland.
- ⇒ Marketing efforts will be increased by strengthening the activities of the Trade Council of Iceland, the Iceland Tourist Board, and the Marketing Office of the Ministry of Industry and the National Power Company.
- ⇒ The foreign service will put increased emphasis on promoting the opportunities offered to foreign investors in Iceland.
- ⇒ Work will be continued on preparations for energy-intensive industry.
- ⇒ The Foreign Investment Act will be reviewed with a view to attracting foreign investment.

III.16 Privatisation

During the last few years, a program for privatisation has been in force in Iceland. Various state-owned companies have been sold and others have changed their operational form to limited liability companies. This has especially been the case when state-owned companies and institutions have competed in the private sector.

The privatised enterprises include a venture capital lending institution, an insurance company, a fish processing company, a fish meal company, a coastal shipping line, and a machinery and heavy equipment plant. The state also sold its 20 percent ownership in Icelandair to private investors. The state-owned tourist bureau was restructured into a limited liability company and sold. The state-owned and operated Motor Vehicle Inspectionhas been restructured into a limited liability company. In 1989 a state-owned commercial bank was sold to three private banks as the four banks merged into one.

The privatisation programme continues as the Government plans to incorporate the two state-owned commercial banks and the investment credit funds.

The policy statement of the Government

- ⇒ To submit a privatisation programme which will be implemented during the government's term in office.
- ⇒ Emphasis will be put on changing the operational form of the state-owned commercial banks and investment funds. This applies also to state-owned companies and institutions which now compete with the private sector.
- ⇒ During the government's term in office, work will proceed on the sale of state-owned companies in accordance with the decisions of the Althing.

III.17 Labour-related measures and vocational training

The Icelandic workforce is considered to be well educated and technically skilled. There is now a strong focus on vocational training, which takes place in comprehensive schools, industrial-vocational schools and specialised vocational schools. Students can choose cours-

es from different vocational fields, leading to full qualification in certified crafts and industrial trades. Strong emphasis is put on foreign languages in the Icelandic school system.

An important measure in this field is the Vocational Training Programme, started in 1992. The aim of the programme is to stimulate vocational training in the business sector with the intention of fostering increased productivity, raising the quality of goods and services and facilitating technical innovation and development in Icelandic business, fostering improved practical skills and increased ability on the part of workers to encounter new demands in a changing environment, and giving the workforce, and in particular those who have had little or no previous experience and education, equal access to vocational training. Basic training in particular skills is made readily available to those who lose their jobs due to technical improvements, for re-education and training for other jobs.

The aim of this programme shall be achieved by supporting systematic vocational training, preparatory work, the production of teaching and course material, teaching and practical training, and initiating and formulating an over-all policy for vocational training in the business sector in accordance with the decision of the Vocational Training Council. Those eligible for support are employers' and workers' organisations, individual business enterprises, private or public bodies that organise vocational training in the business sector, and the vocational training councils of the individual occupations.

In order to improve the efficiency of the labour market, certain structural changes were implemented earlier this year, when two laws concerning the labour market took effect.

The act on unions and work disputes replaces an act from 1938. The new act stipulates the process of each round of wage negotiations and ensures the timely initiation of talks and defines the role of the arbitrator in this process, while describing the possible ways of calling a strike. These changes aim for greater flexibility on the labour market and hence for a more competitive and productive economic environment.

The other act concerns central government employees and includes the abolishment of lifetime hiring in favour of five year contracts for higher ranked employees. Administrators are also given greater responsibility in the operation of the institution in question, while receiving a larger margin in which to determine employees' wages. The overall aim of these changes is to bring the situation in the public sector more in line with that already existing on the private market.

Furthermore, the pension fund system will be revaluated with the aim of strengthening its operating conditions and ensuring that everyone enjoys comparable pension rights. More choices will be offered in choosing a savings scheme, and competition between pension funds will be enhanced.

The policy statement of the Government

- ⇒ To review the labour laws with the aim of promoting stability, the responsibility of contracting parties and greater influence by individual members of trade unions.
- ⇒ To strengthen the economic base of the pension fund system so that all citizens may enjoy comparable pension rights. Increased choices in pension savings must be ensured and competition between the various pension funds will be promoted.
- ⇒ A general law will be passed on the activities of pension funds which will, amongst other things, ensure direct influence by individual fund members on the policy and administration of such funds.

- \Rightarrow A law will be passed on the status and role of privately-owned pension funds.
- ⇒ Agreements will be sought with the pension funds by which they will be encouraged to invest an increased proportion of their annual disposable funds in business enterprises.
- ⇒ To make the loan period of the housing loans of the State Housing Board flexible, establishing a loan period of 15 to 40 years instead of 25 years as is now applicable.
- ⇒ Special emphasis will be put on assisting young people to acquire ownership of their first home. Those who are paying off older mortgages shall be given the opportunity to extend their loans.
- ⇒ Efforts will be made to assist individuals who are having serious difficulties in meeting payments for the purpose of regaining control of their finances. The objective is to transfer the general housing loans system from the State Housing Board to the banking system.

III.18 Measures to protect the environment

Iceland is more dependent on the environment, like marine resources, than most other nations. Thus strong emphasis has been laid on preserving the environment and Iceland has sought to preserve its reputation for providing clean air and water. Several changes have been made in the last few especially concerning the adoption of the EEA legislation in this field. The law on EIA (Environmental Impact Assessment) came into force on May 1, 1994. Although a separate act, it is linked with other licensing acts for mandatory consultation with licence granting agencies. The adopted approach closely follows that of the 85/337/EU Directive. There are however, some subtle differences. For example, concerning the category of projects that require a mandatory EIA, Iceland goes a step further than the EU Directive, reflecting

the environmental and economic character of the country. The main aim of the act is to ensure that the impacts of projects likely to have a significant effect on the environment, natural resources and communities are assessed before the projects are initiated. Factors taken into account include a project's location, resulting activities, nature and size. The act shall also ensure that such an assessment is invariably a part of the planning process. Though the Ministry of the Environment is the principal authority for the EIA, the National Physical Planning Agency (NPPA) is responsible for its implementation.

The policy statement of the Government

- ⇒ To take an active part in international cooperation on pollution control and the protection of the marine ecology.
- ⇒ Efforts will be made to attain more systematic recycling and re-use of materials.
- ⇒ Efforts will be made to improve tourist services, taking strict account of environmental considerations.
- ⇒ Priority shall be attached to preserving Iceland's image of environmental purity and protection.

III.19 Regional development policy measures

The main policy in this field has been the promotion of regional development through secure and reliable communications so that the country's resources, on land and sea, can be utilised efficiently. This has been done, e.g., through improvements in the field of transport and communications.

It has also been done through the transfer of specific tasks from the state to local governments. This autumn, the operation of the primary school system has been transferred from the state to the local governments. Further actions include the reduction of the cost of heating buildings in regions where this cost is exceptionally high and the operation of the Regional Development Board. Regional development has also been promoted through special official assistance.

The policy statement of the Government

- ⇒ To promote regional development through secure and reliable communications so that the country's resources, on land and in the sea, can be utilized efficiently.
- ⇒ Through the transfer of specific tasks from the state to local governments, and the relocation of public institutions, efforts will be made to strengthen specific service centres.
- ⇒ Efforts will be made to reduce the cost of heating buildings in regions where this cost is extremely high.
- ⇒ The operations and organization of the Institute of Regional Development, the Unemployment Insurance Fund, and employment counsellors, will be reviewed with the aim of allowing these bodies to join in the promotion of progress and development of industry throughout the country.

Icelandic Policy on Competitiveness for growth and jobs

Ministries of Industry and Commerce
Ministry of Finance