

English translation of the Weekly Web Release



MINISTRY OF FINANCE IN ICELAND

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Measuring fiscal restraint and the fiscal accounts

Each year, a discussion comes up on the comparison between the revenue surplus of the fiscal budget and the results of the Treasury accounts, where conclusions are drawn regarding the impact of fiscal finances upon the economy. In this respect, it is important to distinguish which revenues and expenditures have an actual impact in a given year under discussion and which items are imputed and originate in previous years or come up for payment in the future.

In comparing the fiscal budget and the fiscal accounts for the years 1998 to 2004 – i.e. from the time a new accounting method was adopted – one could jump to the conclusion that fiscal restraint did not live up to its goals. Upon closer inspection, the opposite turns out to be the case; the accounts show a better result than had been estimated in the fiscal budgets for those years. In assessing the economic impact of fiscal finances it is necessary to take account of irregular expenditures that are booked in a given year but are actually on account of previous years or occur because of a change in future expenditure commitments, such as pension commitments and tax claims written off. The same applies to irregular revenue, such as the difference between the sales price and the book value of privatised assets. Taking account of these entries, the revenue surplus, excluding irregular items, exceeded budget estimates for this period by more than 17 billion krónur.

In the assessment of the impact of fiscal finances upon the economy, the national accounts presentation, as dictated by international standards of accounting for government finances, is used, rather than the actual fiscal budgets or the fiscal accounts themselves. These accounting standards differ considerably. Under the national accounting standards for government finances, future pension fund commitments are not expensed but only those commitments that are incurred because of wage and salary costs arising in the accounting year. The profit from the sale of assets is not booked over the current account. The difference in the national accounting and the fiscal budget methods is discussed more closely in the [Ministry's October Economic Forecast](#)

According to national accounts standards, the Treasury has yielded a revenue surplus since 1997 except in 2002 and 2003. Real GDP declined in 2002. The surplus is estimated at 1 per cent of GDP in 2004 and at 2.8 per cent of GDP in 2005.

The restraint of fiscal finances has thus increased sharply in the past two years. Reviewing the financial balance is another method of assessing the impact of fiscal finances on the economy and the amount left over to repay debt. The financial surplus includes funds left over from the normal operations of the Treasury plus net lending by the Treasury and proceeds from the sale of assets. This year, the financial surplus is estimated at 98 billion krónur, most of which is being used to repay debt or to deposit with the Central Bank. Debt repayment is expected to amount to close to 58 billion and 36 billion will be deposited with the Central Bank. These funds will thus be withdrawn from the economy, an amount equivalent to 30 per cent of total Treasury tax revenue for the year.

What is the share of foreigners in Iceland?

The number of foreigners in Iceland has increased rapidly in recent decades. Some even maintain that the relative share of foreign nationals in Iceland is approaching or exceeding that of neighbouring countries. In this regard, it is important to use comparable definitions of who actually is a foreigner and who is not. At the end of 2003, a total of 290,570 persons lived in Iceland of which 280,390 were Icelandic citizens and foreigners totalled 10,180 or 3.5 per cent of the population. On the other hand, 19,530 were born abroad of which more than half were Icelandic citizens. The largest segment of this group were persons born of Icelandic parents abroad because the parents were either studying or working there. A total of 775 persons with foreign citizenship are born in this country, 7.6 per cent of all foreign citizens. Taking into account that about 4,000 foreign citizens have received Icelandic

citizenship in the past 15 years, it may be estimated that Icelanders of foreign origin are about 5 per cent of the population. From this account, it can be seen that it is not easy to define precisely who belongs to comparable category of foreigners. It is also not easy to get data that are based on an equivalent definition.

Regardless of definition, the question remains unanswered whether there are relatively more foreigners here than in neighbouring countries. Sweden has a population of 9 million of which 1.1 million or 12 per cent are born abroad, compared to 6.7 per cent here. Foreign citizens are close to half a million or 5.3 per cent of the total. This is because a large number of people have moved to Sweden seeking employment or as refugees. Many of those have become Swedish citizens and are no longer counted as foreigners in the statistics. These people have descendants that are both born in Sweden and have Swedish citizenship. About 7 per cent of foreign citizens received Icelandic citizenship last year, a ratio similar to that of Sweden.

Denmark has about 270,000 immigrants, including their descendants who do not have citizenship, about 4.9 per cent of the population. By comparison, about 190,000 persons along with their descendants have received citizenship, 3.5 per cent of the population. About 8.4 per cent of the total population is therefore of foreign descent.

In both these countries that are being used for comparison with Iceland, the proportion of foreigners rose earlier than it did here. A large part of immigrants has therefore acquired local citizenship by now. Denmark classifies people of foreign origin into immigrants on one hand and their descendants on the other. This is done so as to enable the authorities to follow their adjustment to the socio-economic environment of the country.

It may be concluded from the above discussion that people of foreign origin have increased in number in this country in recent years, although their proportion is still below that of neighbouring countries. There are also indications that the labour market participation of foreigners differs among these countries. This is an important prerequisite for the adjustment by foreigners to the local milieu. The experience of the other countries indicates that it is important that immigrants as well as their descendants participate in local life as much as possible.

The impact of ageing on public services

The Human Resources Working Party of the OECD is presently discussing the impact of the foreseeable ageing of populations in coming decades and its consequences for public sector (central and local government) services, i.e. what measures they should take. One of the issues under discussion is an increased emphasis upon the human resource management of the public sector. It will be necessary to direct the working population into those sectors where the demand for services will increase, such as into care for the ageing and away from sectors where the demand for services is declining, such as the care for and the primary education of children. Such a development demands a change in emphasis on personnel training. The emphasis on continuous education and adult retraining will be increased in this connection. The need will also arise to review the division of labour between the public and private sectors in respect of how and where such services will be provided. At a recent meeting of the OECD Human Resources Working Party, the discussion centred upon the need for meeting the rising average age of public sector employees in addition to the ageing of the total population. It is evident that a large number of experienced public servants will be pensioned in coming years and decades. This will create new problems at the same time as opportunities will arise that must be used.

The impact of ageing, both on society as a whole as well as within the public sector, emerge later in Iceland than, for example, in other European nations, partly because of a different age composition. This will give Iceland the opportunity to follow developments in other nations. This situation will continue to be under discussion in the OECD.

Treasury revenue. January-August		
12 month changes %	2003-2004	2004-2005
Total tax revenue	15.3	18.5
Income taxes	20.5	15.5
Social security taxes	10.3	16.6
Asset taxes	18.3	50.3
Indirect taxes	13.6	18.4
Total revenue	6.1	21.1

Treasury expenditure. January-August		
12 month changes %	2003-2004	2004-2005
Administration	8.7	2.4
Social affairs	9.8	6.7
Economic affairs	5.9	-3.4
Interest	-13.5	52.9
Other	-0.4	15.0
Total expenditure	7.0	7.6

Treasury finances. January-August		
Million krónur	2004	2005
Cash from operations	-6,761	16,298
Net financial balance	1,068	27,558
Debt redemption	-29,593	-33,363
Gross borrowing requirem	-33,525	-8,406
Net borrowing	40,177	15,832
Overall cash balance	6,652	7,426

Economic indicators		
12 month changes %	2004	2005
Inflation - October	3.7	4.6
Core inflation - October	3.1	4.8
Wage index - August	5.2	6.7
Tot.turnov. Jan-June	9.8	8.7
Ret.turnov. Jan-June	5.3	9.0
Unemploy.in % September	2.6	1.4