



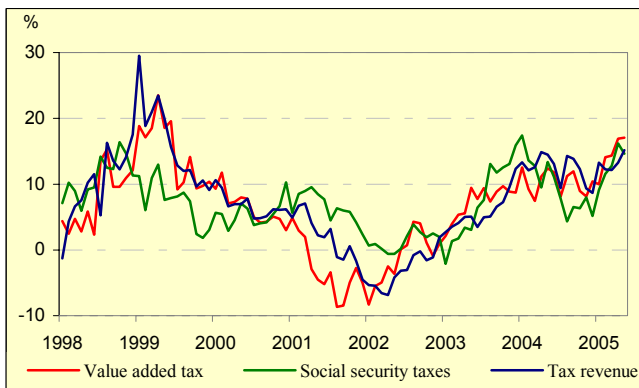
June 30, 2005

Treasury finances, January-May 2005

The surplus of cash at hand from [Treasury operations](#) amounted to 11.2 billion krónur in the first five months of the year, which is 14.2 billion more than a year ago and 25.1 billion better than projections had indicated. Revenue turned out to be 27.4 billion higher than a year ago whereas expenditure increased by 13.5 billion. The net financial surplus amounted to 17.8 billion compared with a deficit of 2.4 billion last year.

Treasury revenue

12-month change, 6-mov.avg., constant prices



Total Treasury revenue amounted to 136.6 billion, an increase of 27.4 billion or 25.1 per cent. Total tax revenue amounted to 121.2 billion, increasing by 19.5 per cent projected exceeding revenue by a small margin to compare general prices increased by 4.1 per cent during the same period resulting in a real increase of 14.8 per cent. Taxes on income and profits amounted to 42.2 billion krónur, an increase of 17.5 per cent over last year. The personal income tax increased by 10.1 per cent and the corporate tax by 6.5 per cent, whereas the capital income tax rose substantially more, by 54.4 per cent, equivalent to 48.3 per cent in real terms. The social security tax amounted to 12.8 billion, increasing by 13.1 per cent in real terms from the previous year. By comparison, the wage index of Statistics Iceland rose by 6.5 per cent in the same period. Taxes on assets and net wealth rose considerably, by 53 per cent, mostly on account of rising revenue from the stamp duty. Other current revenue amounted to 15.1 billion, exceeding projections by 7.8 billion. The increase is due to a 6.3 billion krónur dividend payment from Iceland Telecom in April and a payment in May of 1.5 billion in fines paid by oil distribution companies for their cartel co-operation.

Indirect taxes rose as well by 18 per cent in nominal terms and 13.4 per cent in real terms. The bulk of the increase comes from the value added tax which rose by 19.9 per cent and from import excise duties on motor vehicles rose by 74.9 per cent due to an 85 per cent increase in the value of motor vehicle imports. These developments reflect a stronger exchange rate and increased economic activity.

Total expenditure amounted to 126.8 billion and increased by 13.5 billion from the previous year. Of this amount, 5.7 billion were interest payments, since a large issue of government savings bonds, along with accrued interest, matured last April. Excluding interest, total expenditure increased by 7.5 per cent. Social expenditure i.e. social security, education and health, amounted to 79.2 billion or 62 per cent of the total. This expenditure group rose by 7 billion or 10 per cent. Of this increase, 3.6 billion went for health and 1.5 billion to social security and the same

amount to education. These increases are slightly offset by declines in other expenditure categories, such as for communications and fisheries.

The growth of productivity in the Nordic countries

It is well known that the rate of productivity is important for the economy as it is an important measure of economic wellbeing, since it is broadly congruent with real GDP growth per capita. In order to explain this concept more fully, the factors of production, i.e. labour and capital, must be viewed in conjunction with technology and know-how. All these factors work together to increase production of goods and services and income derived from it. Increased productivity of labour is achieved through increased utilization, which entails increased output both in quantity and quality. Such an increase in productivity is of increasing importance, partly because of constraints on labour supply. It should also be kept in mind that labour productivity is dependent upon fixed investment, human resources and management organisation. Information technology has also been an important contributor in this respect in recent years.

A recent [report](#) from the Nordic Council of Ministers shows the development of per capita labour productivity in the Nordic countries in recent decades.

Labour productivity in the Nordic countries 1981-2003

Average growth rates	1981-1990	1991-2000	2001-2003
Norway	2.9%	3.7%	3.5%
Iceland	1.5%	2.0%	3.2%
Finland	3.3%	3.6%	1.4%
Denmark	1.2%	1.8%	1.4%
Sweden	2.3%	3.2%	1.1%

Productivity per employee.

Labour productivity growth in Iceland was on the low side in the eighties and in the first half of the nineties. Since then it has increased sharply, and in recent years it has exceeded that of Finland, Denmark and Sweden by a half. These figures also indicate that in Iceland there is an increased scope for economic growth that is compatible with low inflation. A substantial structural change in the business environment along with the globalisation of the economy are an important part of this development and have together led to increased competition and economic adjustment. In the above report it is noted that the growth in productivity per hour worked is generally somewhat higher than on a per capita basis. This is due to a shortening work week over this period.

Double-taxation developments

On May 24th to 26th, representatives of Iceland and Romania met for the first time in Reykjavik to discuss a double-taxation agreement between the countries. The drafting of an agreement is well under way, and only a few matters remain to be finalised. The next meeting is expected to take place in the first half of next year at which time the drafting of the agreement is expected to be completed.

Representatives from Iceland and Germany will be meeting in the beginning of July in order to review the existing double-taxation agreement between the two countries. The review is expected to be completed at that meeting. A meeting with representatives from Greece will take place at the end of November this year, following a long interlude but the agreement is almost completed. Negotiations with Croatia are expected to begin this year, but a date has so far not been set.

Treasury revenue, January-May		
12-month changes %	2003-2004	2004-2005
Total tax revenue	15.5	19.5
Income taxes	17.5	17.5
Social security taxes	14.9	17.7
Asset taxes	16.1	59.2
Indirect taxes	14.4	18.0
Total revenue	0.5	25.1

Treasury expenditure, January-May			
12-month changes %	2003-2004	2004-2005	2004-2005
Administration	7.1	2.2	
Social affairs	10.9	9.8	
Economic affairs	7.5	-1.1	
Interest	-16.8	67.1	
Other	-6.2	14.3	
Total expenditure	8.5	12.0	

Treasury finances, January-May		
Million krónur	2004	2005
Cash from operations	-2,947	11,243
Net financial balance	481	17,780
Debt redemption	-28,389	-29,994
Gross borrowing required	-31,033	-13,764
New borrowing	40,861	9,273
Overall cash balance	9,828	-4,490

Economic indicators		
12-month changes, %	2004	2005
Inflation - June	3.9	2.8
Core inflation - June	3.6	3.5
Wage index - May	4.6	6.6
Tot.turnov.Jan-February	7.3	11.9
Ret.turnov.Jan-February	4.9	6.1
Unemploy.in % May	3.3	2.2