

### Treasury finances, January-May 2001

Figures for Treasury finances in the first five months of 2001 are now available. They are on a cash basis and therefore not comparable to the Treasury accounts or the fiscal budget, both of which are presented on an accruals basis.

#### Summary

The cash deficit from operations amounted to a 5.1 billion krónur in the first five months of this year, compared to a surplus of 6.5 billion krónur last year. This result is about 4.5 billion krónur below budget projections. Revenue is close to projections for this period whereas expenditure exceeds projections by 4.5 billion krónur.

#### *Treasury finances in January-May (Millions of krónur, cash basis)*

|   | <u>1998</u>   | <u>1999</u>    | <u>2000</u>    | <u>2001</u>    |
|---|---------------|----------------|----------------|----------------|
| Revenue.....                            | 61,085        | 72,490         | 81,013         | 86,066         |
| Expenditure.....                        | 62,765        | 68,562         | 74,492         | 91,174         |
| <b>Cash from operations.....</b>        | <b>-1,679</b> | <b>3,928</b>   | <b>6,521</b>   | <b>-5,112</b>  |
| <b>Financial transactions.....</b>      | <b>2,198</b>  | <b>67</b>      | <b>1,625</b>   | <b>-2,109</b>  |
| <b>Net financial balance.....</b>       | <b>520</b>    | <b>3,996</b>   | <b>8,146</b>   | <b>-7,222</b>  |
| <b>Debt redemption.....</b>             | <b>-7,197</b> | <b>-16,801</b> | <b>-19,319</b> | <b>-21,545</b> |
| Domestic.....                           | 0             | -7,149         | -10,529        | -6,792         |
| Foreign.....                            | 0             | -9,652         | -8,790         | -14,753        |
| <b>Pension fund prepayments.....</b>    | <b>0</b>      | <b>-767</b>    | <b>-2,500</b>  | <b>-6,250</b>  |
| <b>Gross borrowing requirement.....</b> | <b>-6,678</b> | <b>-13,573</b> | <b>-13,671</b> | <b>-35,018</b> |
| <b>New borrowing.....</b>               | <b>7,888</b>  | <b>8,107</b>   | <b>12,704</b>  | <b>34,047</b>  |
| Domestic.....                           | 0             | -1,126         | 5,371          | 9,532          |
| Foreign.....                            | 0             | 9,233          | 7,333          | 24,515         |
| <b>Overall cash balance.....</b>        | <b>1,211</b>  | <b>-5,465</b>  | <b>-968</b>    | <b>-971</b>    |

Revenues are 5 billion higher than in the same period last year primarily due an increase in taxes on wages and profits. Expenditures are 16.7 billion higher than last year, half of which is due to special circumstances. Interest payments increase by 3.3 billion krónur; special payments to the disabled amount to 1.3 billion krónur; 1.1 billion is due to a contribution to improve the cash flow status of the Social Security Administration because of health insurance; government purchases of farm production quotas amount to 0.8 billion and a special increase in contributions to the Municipal Equalisation Fund amounts to 0.9 billion. Excluding these special transactions, expenditures increased by 9.3 billion, a part of which will not affect the accounts on an accruals basis.

The net financial deficit amounted to 7.2 billion krónur, about 4.2 billion above projections and 15.4 billion less than a year ago. This result is due to the increase in expenditures mentioned above in addition to the fact that in 2000 the Treasury received a one-time payment of 5.5 billion for the sales of shares in the two state-owned commercial banks. These sales actually took place late in 1999 with payment in early 2000.

A total of 6.3 billion krónur were paid to the Government Employees Pension Fund in the first five months of this year. This is being done to reduce the future commitments of the Treasury to the Fund. A total of 15 billion is allocated for this purpose in the 2001 fiscal budget.

The overall cash deficit amounted to just under 1 billion krónur for the first five months of the year, an amount similar to the deficit a year ago.

### Revenue

Total revenue of the Treasury amounted to 86.1 billion krónur in the first five months of the year, exceeding projections by 150 million krónur. Revenue exceeded the level of last year by 6.1 per cent. Tax revenues increased by 4.9 per cent, compared to 12.9 per cent a year ago and 18.5 per cent two years ago. This trends reconfirms the trend of declining growth in domestic demand.

Taxes on income and profit are still increasing at a good pace, by 16.4 per cent between the years. The increase stems mainly from proceeds from the corporate income tax and the capital income tax. Revenue from the personal income tax rises by just over 13 per cent. The increase in personal income tax revenue is largely due to the wage increases stemming from wage agreements in 2000 plus an additional increase in 2001. The rise in the social security tax is due to the same factors.

### **Treasury revenue in January-May** (Millions of krónur, cash basis)

|   |               |               |               |               | Increase in per cent |             |             |
|---|---------------|---------------|---------------|---------------|----------------------|-------------|-------------|
|   | 1998          | 1999          | 2000          | 2001          | 1999                 | 2000        | 2001        |
| <b>Total tax revenue.....</b>           | <b>56,761</b> | <b>67,259</b> | <b>75,931</b> | <b>79,680</b> | <b>18.5</b>          | <b>12.9</b> | <b>4.9</b>  |
| <b>Taxes on income and profit.</b>      | <b>17,169</b> | <b>19,925</b> | <b>24,255</b> | <b>28,224</b> | <b>16.1</b>          | <b>21.7</b> | <b>16.4</b> |
| Personal income tax.....                | 13,218        | 15,123        | 17,375        | 19,707        | 14.4                 | 14.9        | 13.4        |
| Corporate income tax.....               | 1,926         | 2,371         | 3,078         | 3,674         | 23.1                 | 29.8        | 19.4        |
| Other taxes on income and Profit.....   | 2,025         | 2,431         | 3,802         | 4,843         | 20.0                 | 56.4        | 27.4        |
| <b>Social security taxes.....</b>       | <b>6,292</b>  | <b>7,175</b>  | <b>7,699</b>  | <b>8,324</b>  | <b>14.0</b>          | <b>7.3</b>  | <b>8.1</b>  |
| <b>Net wealth taxes.....</b>            | <b>2,968</b>  | <b>3,299</b>  | <b>3,729</b>  | <b>4,278</b>  | <b>11.2</b>          | <b>13.0</b> | <b>14.7</b> |
| <b>Taxes on goods and services.....</b> | <b>30,237</b> | <b>36,784</b> | <b>40,118</b> | <b>38,684</b> | <b>21.7</b>          | <b>9.1</b>  | <b>-3.6</b> |
| Value added tax .....                   | 18,117        | 22,536        | 25,145        | 24,372        | 24.4                 | 11.6        | -3.1        |
| Other indirect taxes.....               | 12,117        | 14,247        | 14,969        | 14,314        | 17.6                 | 5.1         | -4.4        |
| Of which:                               |               |               |               |               |                      |             |             |
| Excise tax on motor vehicles.....       | 1,632         | 2,372         | 2,101         | 1,372         | 45.3                 | -11.4       | -34.7       |
| Excise tax on petrol.....               | 2,694         | 2,587         | 3,177         | 2,956         | -4.0                 | 22.8        | -7.0        |
| Diesel weight tax.....                  | 1,244         | 1,493         | 1,765         | 1,939         | 20.0                 | 18.2        | 9.9         |
| Tobacco and liquor taxes.....           | 2,957         | 3,187         | 3,375         | 3,100         | 7.8                  | 5.9         | -8.1        |
| Other indirect taxes.....               | 3,590         | 4,608         | 4,551         | 4,947         | 28.4                 | -1.2        | 8.7         |
| <b>Other taxes.....</b>                 | <b>95</b>     | <b>76</b>     | <b>130</b>    | <b>170</b>    | <b>-20.0</b>         | <b>71.1</b> | <b>30.8</b> |
| <b>Other revenue.....</b>               | <b>4,968</b>  | <b>5,591</b>  | <b>5,133</b>  | <b>6,380</b>  | <b>12.5</b>          | <b>-8.2</b> | <b>24.3</b> |
| <b>Total revenue.....</b>               | <b>61,734</b> | <b>72,866</b> | <b>81,092</b> | <b>86,063</b> | <b>18.0</b>          | <b>11.3</b> | <b>6.1</b>  |

The slowdown in the economy is clearly reflected in the development of indirect taxes. They declined by 3.6 per cent in the first five months of this year from the level a year earlier, falling short of projections by 3½ billion krónur. This development actually reflects a considerable contraction in real terms, as inflation has been close to 5½ per cent in this period. This is partly explained by a decline in vehicle imports by around 40 per cent in the first five months of this year from last year's level.

The value-added tax, the single largest revenue item, declined by 3.1 per cent from last year and is at the end of May short of projections by 2½ billion. Proceeds from the value added tax from imports increased by 7.9 per cent. Such a change causes a commensurate deduction from gross tax proceeds through a rise in the in-tax, thus causing a temporary fluctuation in tax collection, as was also the case in 1997-1999.

### Expenditure

Total expenditure of the Treasury amounted to 91.2 billion krónur in the first five months of the year, 4½ billion krónur in excess of projections, largely because of a one-time payment of 1.3 billion krónur in disability pensions following a Supreme Court verdict, and 1.3 billion in interest payments due to the early redemption of domestic government bonds. Expenditure increased by 16.7 billion krónur from the first five months of last year, which is primarily explained by the four items observed above and by increased interest payments of 3.3 billion krónur.

**Treasury expenditure in January-May**  
(Millions of krónur, cash basis)

|                                     | <u>1999</u>   | <u>2000</u>   | <u>2001</u>   | Increase in per cent |                  |
|-------------------------------------|---------------|---------------|---------------|----------------------|------------------|
|                                     |               |               |               | <u>1999-2000</u>     | <u>2000-2001</u> |
| <b>Administration.....</b>          | <b>7,621</b>  | <b>8,919</b>  | <b>9,159</b>  | <b>17.0</b>          | <b>2.7</b>       |
| General administration.....         | 4,356         | 5,104         | 5,029         | 17.2                 | -1.5             |
| Justice and law enforcement.....    | 3,265         | 3,816         | 4,132         | 16.9                 | 8.3              |
| <b>Social affairs.....</b>          | <b>41,443</b> | <b>43,570</b> | <b>52,243</b> | <b>5.1</b>           | <b>19.9</b>      |
| Of which: Education and culture.... | 9,258         | 10,040        | 11,575        | 8.4                  | 15.3             |
| Health.....                         | 17,002        | 18,161        | 21,333        | 6.8                  | 17.5             |
| Social security.....                | 12,871        | 12,853        | 16,442        | -0.1                 | 27.9             |
| <b>Economic affairs.....</b>        | <b>10,542</b> | <b>10,670</b> | <b>13,594</b> | <b>1.2</b>           | <b>27.4</b>      |
| Of which: Agriculture.. ..          | 3,769         | 3,866         | 5,010         | 2.6                  | 29.6             |
| Communications.....                 | 3,933         | 3,957         | 5,105         | 0.6                  | 29.0             |
| <b>Interest expenditure.....</b>    | <b>6,716</b>  | <b>8,392</b>  | <b>11,690</b> | <b>25.0</b>          | <b>39.3</b>      |
| <b>Other expenditure.....</b>       | <b>2,240</b>  | <b>2,938</b>  | <b>4,486</b>  | <b>31.2</b>          | <b>52.7</b>      |
| <b>Total expenditure.....</b>       | <b>68,562</b> | <b>74,492</b> | <b>91,174</b> | <b>8.6</b>           | <b>22.4</b>      |

**Administrative expenditures**, which include the Presidency, the Cabinet, the Althingi, the courts and law enforcement, increased by 200 million krónur from the previous year. Increases in salary payments and general non-salary expenditures are offset by lower outlays for the operation of real property and non-recurring expenditures of 150 million krónur connected with the millenium celebrations last year. The rise in law enforcement and civil security expenditures by close to 300 million krónur is largely due to avalanche prevention investments.

**Social affairs.** More than half of total expenditures in the first five months went to social affairs including education, culture, health and social security. Expenditures in this category rose by 8.7 billion krónur between the years. Expenditures for education rose by just over 1,150 million krónur, half of which is due to higher education and speciality schools and is in part explained by overtime payments to teachers following the teachers' strike at the secondary school level this past winter. Health expenditures increased by 3.2 billion krónur between the years, of which 1.1 billion krónur is explained by payments to the Social Security Administration to improve its cash balance. Last year the outlays of the Social Security Administrations increased faster than the Treasury appropriations it received, thus creating a cash deficit which is being offset this year. Operational expenditures of hospitals and nursing homes increased by 1.6 billion krónur and social security outlays increased by 3.6 billion krónur or 28 per cent, 1.3 billion of which, as noted earlier, is due to the Supreme Court verdict. Pensions for senior citizens rose also by 240 million krónur. Social welfare expenditures increased by 800 million krónur, mostly due to a shift in outlays between individual months. Outlays to the Unemployment Insurance Fund increase much less, only by 60 million krónur, since the unemployment rate is virtually unchanged from last year. Parental leave benefits in pursuance of the new Parental Leave Benefit Act have led to a 420 million krónur expenditure so far this year.

**Economic affairs.** Expenditures on economic affairs increased by close to 2.9 billion or 27.4 per cent, primarily due to government purchases of farm production quotas, a one-time payment of 780 million krónur in January. Expenditures on communications increased by just over 1.1 billion of which 600 million went to roadbuilding and maintenance and 371 million to harbours. Contributions to the Institute of Regional Development increased by 300 million krónur.

**Interest expenditures** increased by 39 per cent or 3.3 billion krónur, 1.8 billion of which is due to the redemption of a large government bond issue in February and 1.4 billion krónur due to interest payments on foreign debt

**Other expenditures** increase by 1.5 billion krónur between the years, primarily due to a 1.1 billion krónur special increase in the contribution to the Municipal Equalisation Fund.

#### **Capital transactions**

The outflow on financial transactions amounted to 2.1 billion in the first five months of this year as against an inflow of 1.6 billion last year. The difference is mostly explained by an in-payment of 5.5 billion early in 2000 due to the above-mentioned sales of shares in state-owned commercial banks.

Repayments of Treasury debt amounted to 21.5 billion krónur, nearly all due to the repayment of a foreign government loan. A large domestic bond issue from 1990 matured in February and the redemption amounted to 8.8 billion krónur, of which 4.8 billion were repayments of principal, the remainder being accumulated interest..

Furthermore, three domestic government bond issues were redeemed before maturity through a purchase auction for 3.1 billion, of which 1.8 billion were repayments of principal. Auctions of this kind are directed toward government bond issues that lack liquidity in the secondary market.

The Treasury remitted 6.3 billion krónur to the Government Employees Pension Fund, as noted above, as against 2.5 billion in the same period a year ago.

Treasury borrowing amounted to 34 billion krónur, 20.7 billion of which was borrowed abroad. This represents the proceeds from a bond issue of 250 million Euros that was used to refinance earlier foreign debt. Short-term borrowing, due in June 2001, amounted to 3.8 billion. Domestic Treasury bills outstanding increased by 6 billion in the first five months of the year. In addition, new government bonds with a 6-year maturity were sold for close to 3.4 billion krónur.