

English translation of the Weekly Web Release



MINISTRY OF FINANCE IN ICELAND

August 24th 2006

Treasury accounts for 2005

The accounts of the Treasury for 2005 have now been published. Its main elements are as follows:

Treasury balance. Treasury surplus amounted to 113 billion krónur in 2005 compared with 2 billion the year before. Half of the increase is due to the sale of the Iceland Telecom, leaving a profit of 56 billion. The remainder of the surplus is due to the expansion in the economy, bringing in extra revenue, and to restraint in Treasury expenditure. Treasury revenue, other than from the sale, increased by 55 billion, whereas expenditure remained virtually unchanged between years. The Treasury surplus is a record, irrespective of the profit from the Iceland Telecom sale.

Financial balance. The financial surplus amounted to 77 billion, in addition to 32 billion from the sales proceeds of Iceland Telecom were deposited with the Central Bank under a special arrangement. The Treasury used the financial surplus to reduce debts and increase its liquid holdings at the Central Bank. Close to 50 billion krónur were used to reduce foreign debt, and liquid funds were increased by 27 billion. All told, the Treasury used 109 billion of its surplus to improve its balance with the Central Bank and for the repayment of foreign debt. The net debt of the Treasury, amounted to 60 billion at the end of the year instead of 156 billion at the beginning.

Treasury revenue. Total Treasury revenue amounted to 421 billion krónur, 42.3 per cent of GDP. Excluding revenue from the sale of Iceland Telecom, the revenue/GDP share was 36.0 per cent compared with 33.0 per cent the year before. Revenue from indirect taxes amounted to 165 billion, about half of revenue other than from the sale of Iceland Telecom. Direct taxes amounted to 132 billion, compared with 102 billion the years before. The largest element in the increase was 12 billion krónur from the corporate income tax, double that of the previous year.

Treasury expenditure. Treasury expenditure amounted to 308 billion krónur compared with 300 billion the year before. Excluding capital income tax that the Treasury pays to itself, the expenditure/GDP ratio was 30.3 per cent and 31 per cent including the tax. This compares with an expenditure/GDP ratio of 32.8 per cent in 2004, the ratio declining for two years in a row. As before, expenditure on health is the most important item on the expenditure side, amounting to 77 billion, followed by social security and other social expenditure of 70 billion. Together, these two items account for about half of total Treasury expenditure.

EU Directive on occupational retirement provision

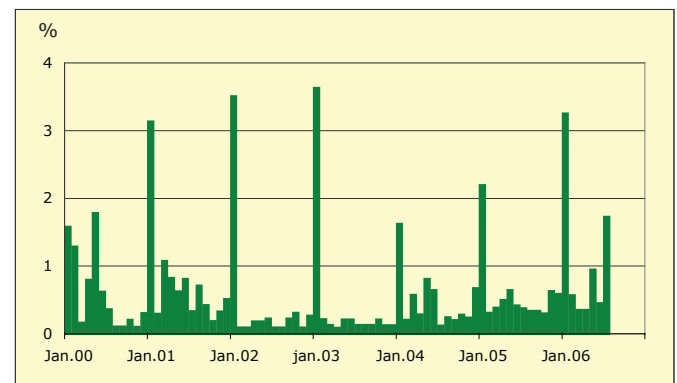
The Ministry of Finance drafting legislation for the introduction of Directive [EU 2003/41/EC](#), regarding occupational retirement provision. Preparations for implementing the Directive have been under way in EEA member countries at different speed, but the stage to which such preparations have progressed differs amongst member countries. As for Iceland, a bill will be presented to the Althingi in the upcoming session. The objective of the Directive is to make it possible for occupational retirement funds to offer defined services across borders within the EEA Area, support and promote efficient investments and a secure investment income, ensure the rights of pensioners and other holders of retirement claims, increase competition, introduce the mutual recognition of supervisory authorities within the EEA Area and create preconditions for a strong internal market for occupational retirement savings. The Directive will apply to institutions that accept non-compulsory occupational retirement savings for the formation and eventual payment of retirement pensions and operate on a funded basis and are separate from the business contributing thereto. The Directive excludes from its applicability those pension funds that according to definition come under Council Regulation 1408/71/EC, with subsequent amendments. This Regulation applies to the traditional Icelandic pension funds that have been defined as such since 1994. With the introduction of the Directive, it is being as-

sumed that the sovereignty of individual countries over their own retirement arrangements will not be impaired. Such sovereignty will, amongst others cover compulsory contributions to pension funds as well as compulsory membership.

The impact of wage agreements is beginning to show

Statistics Iceland has recently published the wage index for July, showing an increase of 1.7 per cent from the previous month. The bulk of the increase may be attributed to the agreement between employers and unions in the general labour market of July 1st. The following graph shows the monthly increases in the index in recent years. The index tends to show the largest increases when there are general wage increases. Such increases have generally taken place at the turn of the year. Increases in the index have also taken place when agreements are reached with smaller groups. Increases in excess thereof represent wage drift due to seniority increases or individual pay raises. In the Ministry's most recent [macroeconomic forecast](#), the total impact of the new wage agreement was estimated at 4 per cent. A provisional estimate of the wage increases in the general labour market at present is that wages have increased by 2.5 per cent. The wage index is expected to continue increasing over the next 1-2 months as the impact of the wage agreements becomes fully reflected in the index. Wage drift is expected to diminish.

The wage index of Statistics Iceland: Monthly increases in per cent



The graph below show the 12-month change in the wage index which has been increasing since the beginning of 2004 and is now as high as at the peak of the previous expansion. Due to the recent wage agreements, it is expected that the increase will level off. The Ministry's most recent estimate of wage increases this year is slightly over 9 per cent. The latest figures are in line with this estimate. A new macro-economic forecast will be published on October 2nd.

12-month increases in the wage index



Treasury revenue January-June		Treasury expenditure January-June		Treasury finances January-June		Economic indicators			
12 month changes (%)	2005	2006	12 month changes (%)	2005	2006	12 month changes (%)	2005	2006	
Total tax revenue	18.7	16.3	General public services	29.1	-20.0	Million krónur			
Taxes on income & profit	15.5	33.5	Health	10.5	6.3	Cash from operations	15,536	29,706	
Taxes on property	56.8	-27.3	Social security & welfare	-0.7	6.0	Net financial balance	25,915	27,498	
Taxes on goods & services	18.9	9.8	Economic affairs	0.5	-0.4	Debt redemption	-30,002	-38,873	
Social contributions	15.8	15.3	Education	17.7	9.7	Gross borr. requirement	-5,988	-13,355	
Total revenue	23.9	10.4	Total expenditure	9.7	0.8	Net borrowing	9,579	16,246	
						Overall cash balance	3,591	2,890	
						Inflation (August)		3.7	8.6
						Core inflation (August)		4.0	7.6
						Wage index (July)		6.6	10.2
						Total turnover (Jan. - April)		5.8	11.9
						Retail turnover (Jan. - April)		3.9	6.2
						Unemployment rate, sa (July)		2.0	1.4