

## Chapter 10

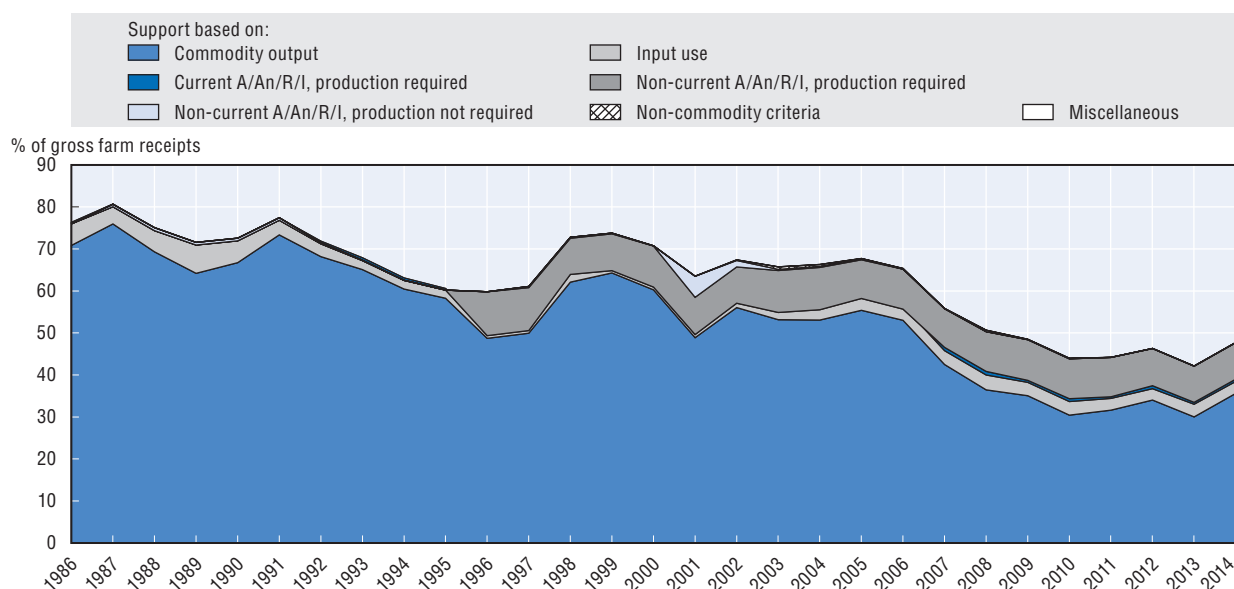
# Iceland

*The Iceland country chapter includes a brief evaluation of policy developments and related support to agriculture, contextual information on the framework in which agricultural policies are implemented and the main characteristics of the agricultural sector, an evaluation of support in 2013-14 and in the longer term perspective, and a brief description of the main policy developments in 2014-15.*

### Evaluation of policy developments

- Iceland's level of support remains well above that of most other OECD countries, although it has declined significantly between 2005 and 2010 due to higher world market prices and a strong devaluation of the Icelandic Króna. In contrast, reforms of the agricultural policies in Iceland have been limited. With unchanged market and trade policies, lower reference prices for dairy products in 2014 led to the highest level of support since 2009.
- Despite the shift towards more decoupled payments in the sheep meat sector in the mid-1990s and the establishment of a market for dairy quotas helping to reduce efficiency losses, agricultural support in Iceland remains dominated by market price support and other production and trade distorting measures. About three-quarters of farm support is provided in these most distorting forms, largely preventing agricultural producers from receiving market signals and responding to them.
- To sustainably reduce the level of support and its distortive effects, policies need to be changed away from border protection and in favour of measures less linked to production. Reforms need to efficiently target explicit policy objectives, including the protection of the environment and the conservation of natural resources, while reducing market distortions.

Figure 10.1. **Iceland: PSE level and composition by support categories, 1986-2014**



Source: OECD (2015), "Producer and Consumer Support Estimates", OECD Agriculture Statistics (database), <http://dx.doi.org/10.1787/agr-pcse-data-en>.

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## Contextual information

Iceland is a relatively small economy with a GDP per capita close to the OECD average. The economic downturn after 2007 resulted in a significant deterioration of the economy with lower per capita GDP and higher inflation and unemployment rates. Both GDP growth and inflation rates have come back closer to trend levels since 2011, while unemployment, albeit reduced and below average OECD rates, has remained higher than in much of the 1990s and 2000s. At about 8% and 4.5%, respectively, the shares of the agriculture (including fish) in both GDP and employment are relatively high, due to the importance of the fishing sector. Iceland has been a consistent net importer of agro-food products (excluding fishery), with a total agro-food trade balance of USD -132 million in 2013. Agriculture in Iceland mainly consists of livestock production, with milk and sheep meat being the most important products, together accounting for about half the agricultural production. Horticulture, much of which is under glass, is an important sector too, and together with a few other crops represented some 13% of total agricultural production in 2013.

Table 10.1. **Iceland: Contextual indicators, 1995, 2013<sup>1</sup>**

	1995	2013 <sup>1</sup>
<b>Economic context</b>		
GDP (billion USD)	7	15
Population (million)	0.27	0.32
Land area (thousand km <sup>2</sup> )	100	100
Population density (inhabitants/km <sup>2</sup> )	2.6	3.2
GDP per capita, PPP (USD)	23 195	41 860
Trade as % of GDP	25.3	32.7
<b>Agriculture in the economy</b>		
Agriculture in GDP (%)	11.6	8.0
Agriculture share in employment (%)	9.5	4.5
Agro-food exports (% of total exports)	6.8	6.4
Agro-food imports (% of total imports)	10.0	9.0
<b>Characteristics of the agricultural sector</b>		
Agro-food trade balance (million USD)	-53	-132
Crop in total agricultural production (%)	22	13
Livestock in total agricultural production (%)	78	87
Agricultural area (AA) (thousand ha)	2 280	1 872
Share of arable land in AA (%)	0.3	6.5
Share of irrigated land in AA (%)	..	..
Share of agriculture in water consumption (%)	42	42
Nitrogen balance, kg/ha	7	8

Note: Agriculture employment and GDP shares without fisheries are about half and one-sixth of the percentages shown, respectively.

1. Or latest available year.

Sources: OECD Statistical Databases, UN Comtrade Database, World Development Indicators and national data.


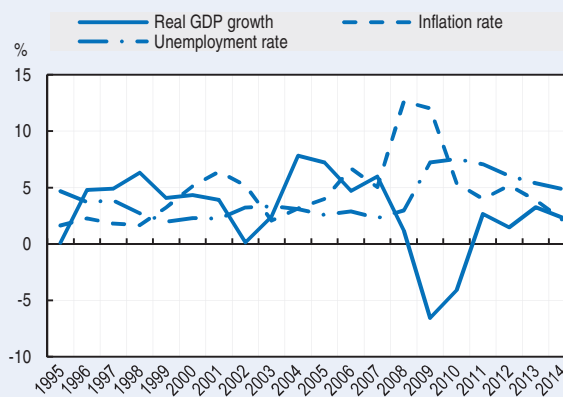
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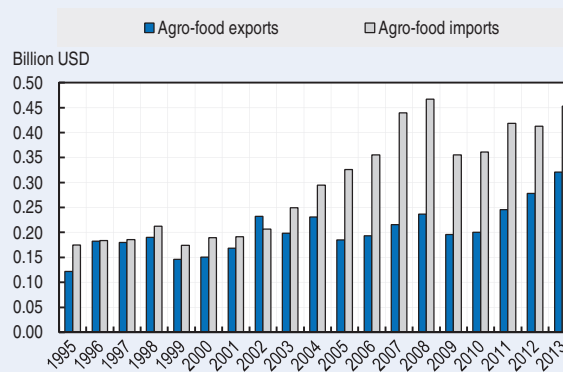
Figure 10.2. **Iceland: Main macroeconomic indicators, 1995-2014**



Source: OECD Factbook Statistics.

StatLink  <http://dx.doi.org/10.1787/888933234683>

Figure 10.3. **Iceland: Agro-food trade, 1995-2013**



Source: UN Comtrade Database.

StatLink  <http://dx.doi.org/10.1787/888933234694>

Note: Detailed definitions of contextual indicators and their sources are provided in the "Reader's guide".

## Development of support to agriculture

After a drop in 2013, support to agriculture has increased again in 2014 to reach its highest level in five years. Despite a significant decline in support levels and market distortions between 2005 and 2010, Iceland is still among the five OECD countries showing the highest support to farmers. Direct payments, largely based on historical livestock production, have replaced some of the former price support in the sheep meat sector, and together with movements of international prices and exchange rates have contributed to reductions in the level of price distortions as measured by the NPC.

### PSE as % of receipts (%PSE)

Between 1986-88 and 2012-14, support to farmers in Iceland has declined by 32 percentage points. But at 45%, it remains high compared to most other OECD countries. After having fallen to 42% in 2013, the %PSE jumped back to 48% in 2014 due to lower international dairy prices.

### Potentially most distorting support as % of PSE

The share of potentially most distorting support (based on output and variable input use – without input constraints) in total PSE has fallen over the past decades, due to higher international commodity prices, the devaluation of the Króna since 2007, and the change in sheep meat payments towards historical entitlements in the mid-1990s. Still, these forms of support represent about three-quarters of the total PSE.

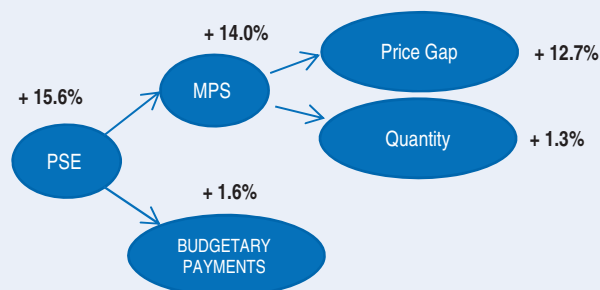
### Ratio of producer price to border price (NPC)

In the long term, the ratio of producer prices (including unit output payments) to border prices has been reduced substantially, from over 4 in 1986-88 to 1.6 in 2012-14. Poultry, eggs, wool and milk show the highest NPC. Again, much of this decline was due to changes in international prices and exchange rates.

### TSE as % of GDP

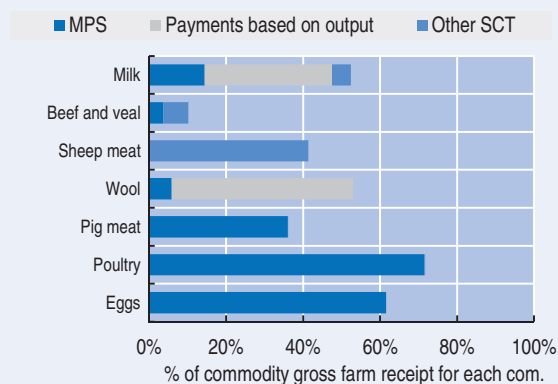
Total support was 1.1% of GDP in 2012-14, with the expenditure on general services representing some 5% of the Total Support Estimate.

### Decomposition of change in PSE, 2013 to 2014



The level of support increased in 2014 mainly due to a widened gap between higher domestic prices and lower border prices (MPS), in particular for dairy products.

### Transfer to specific commodities (SCT), 2012-14



Single Commodity Transfers (SCT) represented 98% of the total PSE. The share of the SCT in the commodity gross farm receipt is lowest for beef and veal (10%) and highest for poultry (72%).

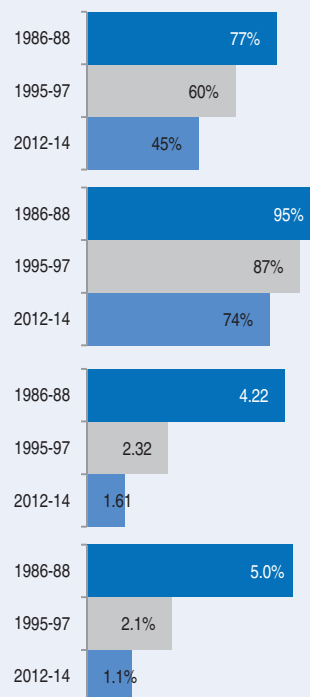


Table 10.2. Iceland: Estimates of support to agriculture

Million ISK	1986-88	1995-97	2012-14	2012	2013	2014p
<b>Total value of production (at farm gate)</b>	<b>9 644</b>	<b>10 326</b>	<b>31 686</b>	<b>30 447</b>	<b>32 004</b>	<b>32 606</b>
<i>of which: share of MPS commodities (%)</i>	80.3	73.5	80.4	79.7	79.9	81.7
<b>Total value of consumption (at farm gate)</b>	<b>8 388</b>	<b>9 706</b>	<b>27 496</b>	<b>26 317</b>	<b>28 125</b>	<b>28 047</b>
<b>Producer Support Estimate (PSE)</b>	<b>7 909</b>	<b>8 825</b>	<b>19 366</b>	<b>18 926</b>	<b>18 169</b>	<b>21 005</b>
Support based on commodity output	7 374	7 645	14 179	13 908	12 951	15 679
Market Price Support <sup>1</sup>	7 307	4 533	8 368	8 497	7 029	9 578
Payments based on output	66	3 112	5 811	5 411	5 922	6 100
Payments based on input use	536	337	1 221	1 108	1 301	1 254
Based on variable input use	129	0	241	224	228	271
with input constraints	0	0	0	0	0	0
Based on fixed capital formation	233	126	517	430	609	512
with input constraints	0	0	0	0	0	0
Based on on-farm services	174	210	463	454	464	470
with input constraints	0	0	0	0	0	0
Payments based on current A/An/R/I, production required	-49	-181	239	289	192	237
Based on Receipts / Income	-49	-181	-391	-327	-436	-410
Based on Area planted / Animal numbers	0	0	630	616	628	647
with input constraints	0	0	2	6	0	0
Payments based on non-current A/An/R/I, production required	0	1 011	3 727	3 621	3 724	3 836
Payments based on non-current A/An/R/I, production not required	48	14	0	0	0	0
With variable payment rates	0	0	0	0	0	0
with commodity exceptions	0	0	0	0	0	0
With fixed payment rates	48	14	0	0	0	0
with commodity exceptions	48	14	0	0	0	0
Payments based on non-commodity criteria	0	0	0	0	0	0
Based on long-term resource retirement	0	0	0	0	0	0
Based on a specific non-commodity output	0	0	0	0	0	0
Based on other non-commodity criteria	0	0	0	0	0	0
Miscellaneous payments	0	0	0	0	0	0
<b>Percentage PSE (%)</b>	<b>77.2</b>	<b>60.4</b>	<b>45.4</b>	<b>46.3</b>	<b>42.1</b>	<b>47.7</b>
<b>Producer NPC (coeff.)</b>	<b>4.22</b>	<b>2.32</b>	<b>1.61</b>	<b>1.63</b>	<b>1.52</b>	<b>1.68</b>
<b>Producer NAC (coeff.)</b>	<b>4.44</b>	<b>2.52</b>	<b>1.83</b>	<b>1.86</b>	<b>1.73</b>	<b>1.91</b>
<b>General Services Support Estimate (GSSE)<sup>2</sup></b>	<b>731</b>	<b>927</b>	<b>958</b>	<b>916</b>	<b>949</b>	<b>1 008</b>
Agricultural knowledge and innovation system	187	327	112	114	109	114
Inspection and control	37	88	391	374	384	416
Development and maintenance of infrastructure	91	187	22	15	23	28
Marketing and promotion	58	75	39	31	40	45
Cost of public stockholding	359	249	393	382	393	405
Miscellaneous	0	0	0	0	0	0
<b>Percentage GSSE (% of TSE)</b>	<b>6.8</b>	<b>9.1</b>	<b>4.7</b>	<b>4.5</b>	<b>4.9</b>	<b>4.6</b>
<b>Consumer Support Estimate (CSE)</b>	<b>-4 566</b>	<b>-4 012</b>	<b>-7 680</b>	<b>-7 563</b>	<b>-6 657</b>	<b>-8 820</b>
Transfers to producers from consumers	-6 421	-4 340	-7 860	-7 973	-6 720	-8 885
Other transfers from consumers	-51	-35	0	0	0	0
Transfers to consumers from taxpayers	1 906	363	180	410	63	65
Excess feed cost	0	0	0	0	0	0
<b>Percentage CSE (%)</b>	<b>-70.4</b>	<b>-42.9</b>	<b>-28.1</b>	<b>-29.2</b>	<b>-23.7</b>	<b>-31.5</b>
<b>Consumer NPC (coeff.)</b>	<b>4.44</b>	<b>1.82</b>	<b>1.40</b>	<b>1.43</b>	<b>1.31</b>	<b>1.46</b>
<b>Consumer NAC (coeff.)</b>	<b>3.50</b>	<b>1.75</b>	<b>1.39</b>	<b>1.41</b>	<b>1.31</b>	<b>1.46</b>
<b>Total Support Estimate (TSE)</b>	<b>10 546</b>	<b>10 115</b>	<b>20 504</b>	<b>20 251</b>	<b>19 181</b>	<b>22 078</b>
Transfers from consumers	6 472	4 375	7 860	7 973	6 720	8 885
Transfers from taxpayers	4 124	5 775	12 644	12 278	12 461	13 193
Budget revenues	-51	-35	0	0	0	0
<b>Percentage TSE (% of GDP)</b>	<b>5.0</b>	<b>2.1</b>	<b>1.1</b>	<b>1.1</b>	<b>1.0</b>	<b>1.1</b>
<b>GDP deflator (1986-88=100)</b>	<b>100</b>	<b>211</b>	<b>462</b>	<b>455</b>	<b>464</b>	<b>467</b>

Note: 1986-88, 1995-97 and 2012-14: unweighted averages. p: provisional. NPC: Nominal Protection Coefficient. NAC: Nominal Assistance Coefficient.

A/An/R/I: Area planted/Animal numbers/Receipts/Income.

1. Market Price Support (MPS) is net of producer levies and excess feed cost. MPS commodities for Iceland are: milk, beef and veal, sheep meat, wool, pig meat, poultry and eggs.

2. A revised GSSE definition with new categories was introduced in 2014. When possible, the revision was implemented for the whole time series. The GSSE series and the resulting TSE are not comparable with the series published previously. (For more details see the Annex 1.A1 to Chapter 1).

Source: OECD (2015), "Producer and Consumer Support Estimates", OECD Agriculture statistics (database). doi: dx.doi.org/10.1787/agr-pcse-data-en

StatLink  <http://dx.doi.org/10.1787/888933235291>

## Description of policy developments

### Main policy instruments

Agricultural policies in Iceland are based on two main legal acts: Act No. 99/1993 on the Production, Pricing and Sale of Agricultural Products lays down the policy framework as well as provisions for production control, provision on slaughter and processing, market measures and producer support, whereas Act No. 70/1998 on Agriculture lays down provisions for development projects, extension services and livestock improvements.

Within that framework, agricultural policies are determined by renewable multi-year agreements between the Government of Iceland and the Farmer's Association, which provide the general framework for support and production control for farmers in the covered sectors. The three agreements currently in force, all of which have been renewed in fall 2012, are the Agreement on Dairy Production (due to expire in 2016), the Agreement on Sheep Production (due to expire in 2017) and the Agreement on Horticultural Production (due to expire in 2015). Each of the agreements contains a precautionary clause allowing necessary changes to be made in case that Iceland might join the European Union during the term of the agreements. Since March 2015, however, an EU membership is no longer envisaged by the Government of Iceland.

Iceland's agricultural support continues to be provided through market price support, maintained by border measures, and through direct payments, which are based on payment entitlements, directly or indirectly coupled with production factors. Direct payments are provided to cattle (mainly dairy) and sheep producers and, on a smaller scale, to certain greenhouse producers, while market price support is provided for all livestock products and some horticultural products.

Wholesale prices continue to be managed for approximately half of the dairy products. A government-chaired committee, representing both the Farmers' Association and – on behalf of the consumer side – the labour union, annually determines guaranteed minimum prices for milk delivered within production quotas. Both production quotas and entitlements for support payments are tradable between farmers. While reference prices for sheep meat can be published by the Sheep Farmers' Association, these have no binding effect on slaughter companies' pricing policies.

Iceland maintains prices above world market levels for a range of livestock products, including the poultry and eggs sectors, milk products as well as, to a lesser extent, the pig meat sector. MFN tariffs for most meat and egg products are at 30%, and additional specific tariffs apply depending on the product. However, products originating in partner countries of the European Economic Area or in one of the more than 35 countries with which Iceland has free trade agreements may carry lower tariffs. According to the legislation on protection against animal diseases, imports of uncooked animal products require the permission of the Minister of Fisheries and Agriculture, based on recommendations by the Food and Veterinary Authority.

Payments based on historical entitlements have replaced output payments for sheep meat in the mid-1990s, and payment entitlements have become tradable among farmers. Keeping a minimum of winter-fed sheep on the farm is, however, required for being eligible to receive the payments. Additional payments to sheep farmers are related to a quality control scheme for lamb meat, based on animal welfare, product quality and traceability, and sustainability criteria.

Agricultural revenues are subject to a levy which is distributed within and between various agricultural bodies. Among these bodies is the Emergency Relief Fund: it grants compensation payments to farmers who suffer major financial losses after natural disasters or because of extreme weather conditions, animal diseases or accidents for which there are no insurances available on the

market. Agri-environmental policies particularly focus on soil conservation and forestry: related payments aim at the reduction of desertification and sand encroachment, the promotion of sustainable land use, the reclamation and restoration of degraded land and new afforestation.

### Domestic policy developments in 2014-15

Since the **reform of the support for domestic wool processing** in late 2012, with most of the support for the collection and processing of domestic sheep wool (84%) now being paid directly to the producers, the domestic price for raw wool has dropped significantly, erasing the market price support for this product.

Mainly in response to the increasing domestic consumption of dairy products in Iceland, the **milk production quota** was increased from 116 million litres in 2013 to 125 million litres in 2014. The quota has been further increased to 140 million litres for the year 2015.

From 1 January 2014, two **dairy-specific levies** were **abolished**. These include firstly the price transferral levy which used to be collected at delivery of milk to the dairy processor at a per litre basis to lower the price of certain dairy products. The price transferral levy amounted to ISK 313 million (USD 2.6 million) in 2013. Secondly, the price equalisation levy, also collected at delivery of milk to the dairy processor at a per litre basis, used to help cover production cost differences between individual dairy processors, in particular lowering transportation costs of milk to dairy processors and of dairy products to the market. The price equalisation levy amounted to ISK 92 million (USD 0.75 million) in 2013.

### Trade policy developments in 2014-15

Iceland is a member of the European Free Trade Association (EFTA) and of the European Economic Area (EEA). While the EEA Agreement does not apply to most trade in agricultural goods, it opens trade in a number of processed agricultural products and encourages bilateral agreements on primary commodities. Such a bilateral agreement between Iceland and the EU has been in force since 2007, extending the EU-Iceland Free Trade Agreement from 1972. It reduces or eliminates agricultural tariffs and establishes quotas in bilateral trade. Furthermore, EFTA has a number of Free Trade Agreements with countries in South-East Europe, North Africa and the Middle East, Latin America, and Asia, as well as with the South African Customs Union. A bilateral Free Trade Agreement between Iceland and China came into force on 1st July 2014. In addition, Iceland has a bilateral Free Trade Agreement with the Faroe Islands.

In March 2015, the Government of Iceland announced that Iceland should no longer be considered a candidate country to the European Union. In 2009, Iceland had applied to join the EU, and accession negotiations had started in July 2010, with a Screening Report on agriculture published in June 2011.\* In January 2013, the former Government decided to put the accession negotiations on hold, and in May 2013, the newly elected Icelandic Government decided to continue this policy. At that time, negotiations on 27 chapters had been opened, of which 11 provisionally closed. Other chapters, including agriculture and rural development and fisheries had not been opened yet.

\* Chapter 11 "Agriculture and Rural Development" can be found at [http://ec.europa.eu/enlargement/pdf/iceland/key-documents/screening\\_report\\_11\\_is\\_internet\\_en.pdf](http://ec.europa.eu/enlargement/pdf/iceland/key-documents/screening_report_11_is_internet_en.pdf).







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