SUMMARY

1. Since the last Trade Policy Review of Iceland in 2012, a number of significant changes to its trade policy have been introduced. Tariffs on non-agricultural goods were fully eliminated and tariffs on some agricultural goods were also reduced. In addition, a number of measures were undertaken and projects are currently under way to improve customs procedures and new free trade agreements have been signed. On the other hand, although new regulations for the agriculture sector took effect in 2017 for the period 2017-2026, the sector continues to be protected by high tariffs and supported by subsidies. In addition, foreign investment restrictions remain in some sectors, notably fishing and energy.

2. Since 2012, the country has continued to recover from the severe economic crisis that started in 2008. GDP growth averaged 3.8% for 2012-16, while GDP per capita reached nearly US$60,000 in 2016. Growth during this period was driven by tourism-related services while the contribution to GDP from the traditional fishing, fish processing, and aluminium sectors declined.

3. With a small open economy and limited range of natural resources, trade is critically important to Iceland’s economy and exports and imports of goods and services were the equivalent of over 90% of GDP in 2016. The main goods exported were fish and fish products, and aluminium and products thereof which together accounted for over three-quarters of the value of goods exports in 2016. However, a surplus in trade-in-goods in 2012 became a deficit in 2014 as imports increased while exports declined due to lower aluminium prices and lower quantities of fish exports. The EU is the main destination for exports (nearly three-quarters) and source of imports (nearly half). The deficit in trade-in-goods was more than compensated by the rising surplus in trade-in-services, primarily due to increased tourism. Tourism is now Iceland’s largest export sector, and tourism services (transport and travel) were responsible for nearly 80% of Iceland’s services receipts in 2016, which resulted in a tourism-services-related surplus of ISK 300 billion.

4. Practically, all the temporary restrictions on certain types of cross-border capital transfers and foreign exchange transactions that were introduced following the collapse of the banking sector have been removed. A capital account liberalization strategy was introduced in 2015 and controls were progressively reduced. In March 2017, the restrictions on foreign exchange transactions and cross-border movement of domestic and foreign currency were largely lifted.

5. Iceland is an active Member of the WTO but has a mixed record for notifications with no TBT, import licensing or preferential rules of origin notifications and only two SPS notifications were made in the period 2012 to 2016. On the other hand, several notifications from Iceland were distributed in the first half of 2017, including on domestic support for agriculture for the years 2013-15, new public procurement rules, and state trading enterprises.

6. As a member of the European Free Trade Association (EFTA) and the European Economic Area (EEA), many of Iceland’s trade and trade-related policies and laws are closely related to those of the European Union and Iceland is part of the Internal Market with free movement of goods, services, capital and workers. However, some issues such as trade policy and taxation, are not incorporated into the EEA and agriculture is covered by bilateral arrangements. In 2015, a new bilateral agreement on trade in agricultural goods between Iceland and the EU was concluded which eliminated or reduced tariffs on a range of products, increased the quantities in some existing tariff quotas, and created new tariff quotas. As part of the agreement, Iceland is to apply the same level of protection as the EU for GI products registered in the EU.

7. Iceland is a party to 32 reciprocal preferential agreements, mostly through the EFTA, with three new agreements having entered into force during the review period (Bosnia and Herzegovina, certain Central American states (Costa Rica and Panama), and the GCC). In addition, during the review period, Iceland concluded an FTA on its own behalf with China.

8. Since 2012, several projects have been implemented to improve customs procedures, including the introduction of a risk management system, and the introduction of a quality control system. In addition, work is under way on the establishment of an authorized economic operator programme, a single window system, implementation of the revised single administrative document, and an electronic system for the clearance of vessels. The instrument of ratification of the Trade Facilitation Agreement was submitted to the WTO on 31 October 2016.
In a significant development, Iceland eliminated tariffs on all non-agricultural products, with tariffs on clothing and footwear eliminated on 1 January 2016 and tariffs on remaining products eliminated on 1 January 2017. As a result, nearly 90% of tariff lines are now duty-free compared to 70% in 2012. In addition, tariffs on some agricultural products were also reduced. As a result, the overall average tariff fell from 8.3% in 2012 to 4.6% in 2017. However, tariffs on several agricultural product groups, particularly meat, dairy, plants, and flowers, remain high and often take the form of complex non-ad valorem duties. Nevertheless, the average applied tariff on agricultural products declined to 20% in 2017 compared to 29% in 2012 although tariffs are much higher on some products, such as dairy products. About 95% of tariff lines are bound and the unbound tariffs apply to a wide variety of products including some fuels, fertilizers, and machinery products all of which now have duty free applied rates. It was not possible to calculate the ad valorem equivalents for bound tariffs given the complex nature of some of them. However, there were no cases of applied rates exceeding bound rates.

Tariff quotas are used for a number of agricultural products either under the WTO Agreement on Agriculture, FTAs, or autonomously. In many cases, the current applied tariff for tariff lines subject to WTO tariff quotas is the same as, or lower than, the bound in-quota tariff and, therefore, the quota is not used.

Iceland has never used or initiated investigations for anti-dumping or countervailing duties, nor has it ever used the special agricultural safeguard although its customs legislation does provide for them and Iceland reserved the right to use the SSG on 390 tariff lines. There is no legislation on global safeguards although safeguard provisions are generally included in the free trade agreements to which Iceland is a party. According to Iceland’s notifications to the WTO, export subsidies for agricultural products have not been used since 31 August 1998.

Although a number of amendments have been made during the review period to the laws relating to SPS measures they remain strict and are justified on the grounds that Iceland’s domestic animals are highly susceptible to exotic pests and diseases. Imports of some products are prohibited and others are subject to controls and licensing requirements. In general, Iceland applies the EU's rules on food and imported food must comply with requirements that are at least equivalent to those applicable in the EU.

Incentives for regional investment are provided for under new legislation; the previous legislation expired at the end of 2013. Some of the projects approved under the expired legislation had been found by the EFTA Surveillance Authority to be incompatible with the EEA Agreement. Under the new legislation, tax incentives apply for investments outside the Reykjavik area which are limited to 15-35% of the initial investment depending on the size of the enterprise with the higher limits applying to smaller enterprises. In addition, there are incentives for research and investment through tax credits and grants.

Although there have been no substantive changes to the legislation on competition policy during the review period, the Icelandic Competition Authority (ICA) has been actively implementing the law and, in the 2012-2017 period, has prevented one merger, imposed conditions on a further 25 mergers, and has fined 17 companies a total of over €22 million for collusion or abuse of dominant position. In addition, in an opinion issued in 2015, the ICA found that due to the slot allocation arrangements at Keflavik Airport Icelandair has enjoyed a de facto priority for the most important slot times.

The legal framework for public procurement was significantly revised during the review period with a new Act on Public Procurement and other laws and regulations (including new thresholds) introduced to bring legislation into line with EEA rules. The new Act, which applies to the State, local authorities, their institutions and other public entities, sets out to ensure equal treatment of economic operators, encourage efficiency in public sector operations through active competition and to promote innovation and development in public procurement of supplies, works and services. Iceland has been a party to the WTO Agreement on Government Procurement (GPA) since 2001 and has completed the procedures for becoming a party to the revised GPA, which entered into force for Iceland on 6 April 2014.

In addition to changes in legislation on various aspects of intellectual property (IP), including on geographical indications (GIs), the trademark law, and a new fee structure, more changes are
foreseen to bring national laws into line with the EEA. Furthermore, the Intellectual Property Policy, 2016-2022, issued in 2016, put forward a number of proposals to review laws, promote the role of IP in the economy, and improve procedures for registration and enforcement of IP rights. The new act and regulation on GIs apply to food, wine, spirit drinks, and some other products. The product name may be protected if the product originates from a specific area, has qualities or characteristics of the area, and the production, processing and preparation of the product takes place in the area. The name must be registered by the Icelandic Food and Veterinary Authority (MAST). In addition, as part of the agreement with the EU on trade in agricultural products, Iceland is to provide protection for a list of 1,150 EU GIs.

17. Agriculture represents a small part of GDP and employment but remains historically, socially, and culturally important for Iceland, as well as being relatively highly protected and subsidized. Imports (at US$ 492 million in 2016) exceeded exports (US$95 million). Domestic policies were revised under new agreements between the Government and the farmers' association for the period 2017-2026. For dairy and beef, the production quota system remains but is to be reviewed in 2019 to consider the feasibility of abolishing it; headage payments continue and milk payments are to be increased; and support entitlements (basic payments to all active dairy and cattle farmers) are to be phased out. For sheep, support entitlements are also to be phased out while quality assurance payments are to be increased and headage payments introduced. Under these and other changes, the total support to agriculture is to decrease slightly over the duration of the agreements. During 2012 to 2016, support to agriculture in ISK terms increased under the Green, Blue, and Amber Boxes of the WTO and for the 2012 to 2015 period under the OECD's total and producer support estimates (TSE and PSE). The dairy sector is the most heavily supported; in 2016, it accounted for ISK 18.5 billion out of a total of ISK 21.3 billion in Amber Box support and, together with beef, ISK 0.7 billion in the Blue Box. Overall, the PSE was nearly ISK 26 billion in 2015 or 56% of gross farm receipts, the third highest among OECD countries.

18. Although the contributions of fishing and fish processing to GDP have declined, they remain relatively very important and represented 4.6% and 2.7% respectively in 2016. Total exports of fish and fish products were US$ 1,925 million in 2016, representing 43% of exports of goods, while imports were US$ 134 million. Fisheries policy has not changed significantly over the past few years. Based on stock assessments by the Marine and Freshwater Research Institute (MRFI), total allowable catches (TACs) are established which are allocated to individual vessels under the individual transferable quota (ITQ) systems. In addition, a number of effort and gear restrictions apply, discards of commercial species are prohibited, and a vessel owner may not leave port without an adequate quota for the trip. According to the OECD, the Fisheries Support Estimates (FSE) for 2012 to 2014 was negative indicating a net average annual contribution of ISK 4.4 billion from the fisheries sector as fees were greater than the estimates of support. The FSE was positive for 2015 when general services support was greater than cost recovery charges. Foreign ownership of fishing operations and fish processing is limited to 25% direct and 49% direct plus indirect ownership although up to 33% direct foreign ownership may be permitted in some cases.

19. Hydro and thermal power sources are abundant in Iceland and electricity prices for industrial consumers are the lowest in the EEA. As a result, energy intensive industries, such as aluminium production, have been established and aluminium and alloys thereof represent over one-third of total exports of goods (US$1.5 billion). Investment and ownership of energy exploitation rights and the production and distribution of energy are limited to EEA and EFTA residents, while Landsnet, a private company, has the exclusive right to provide transmission services.

20. Since the financial crisis, the banking system has stabilized and recovered. Currently there are four commercial and four savings banks (compared with nine in 2012). Two of the commercial banks are wholly state-owned, while a third has a minority government stake. The restructuring of the banks has also resulted in the ratio of non-performing loans to total loans declining from a peak of 20% in 2010 to 2.1% in 2016. In June 2015, the authorities announced a plan to unwind the estates of the failed banks and the remaining offshore ISK holdings (mainly bank deposits, treasury securities and equity interests). In June 2016, the Central Bank held the first of three voluntary euro auctions for offshore ISK holders with the exchange rate based on a sliding scale related to the size of the bid. Direct state assistance to the financial sector was the equivalent of about 34% of GDP. However, recoveries were estimated to be about 43% of GDP (mainly bank equity and subordinated debt, and stability contributions from the estates of the failed banks). Thus, the State is estimated to have made a net gain in excess of 9% of GDP. During the review
period, several regulatory changes were introduced including the establishment of new bodies to assess the financial system, systemic risk, and financial stability and formulate policies. In addition, several other measures, including new liquidity rules, funding ratios, capital buffers, and rules relating to consumer mortgage credit were introduced.

21. Tourism has increased considerably since 2010 and, in 2016, represented about 10% of GDP and nearly 40% of export receipts for goods and services. Total spending on tourism-related activities increased from ISK 93 billion in 2009 to ISK 222 billion in 2015. Apart from Iceland's unique landscape and other attractions, the increase can also be attributed to the depreciation in the ISK after the financial crisis, better and more frequent flight connections, and better marketing. Tourism also accounts for the increase in air passengers, as well as Icelandic airlines becoming a more financially viable option for transatlantic passengers and the promotion of Iceland as a transatlantic hub. The total number of passengers through Keflavik airport in 2017 is estimated to be in the region of 9 million.

22. Iceland has improved trading and investment conditions since 2012 and partly as a result of this the economy has recovered and is expanding rapidly. With a small population and limited natural resources, apart from energy and fish, trade remains important but the range of exports is limited to tourism, fish and fish products, and aluminium and products thereof. Therefore, the country remains vulnerable to shocks, including the appreciation of the ISK, overheating of the economy, and Brexit. However, short term exposure to external factors has been reduced: at end-2016, total external debt was US$23.4 billion compared to US$105.8 billion in 2012 and international reserves were over US$7 trillion (partly due to the unwinding of the estates of the failed banks). Furthermore, despite uncertainties relating to Brexit, as growth picks up in the EU, Iceland's main trading partner, opportunities for trade in goods and services should continue to improve.