

On 19 September, Statistics Iceland published the national accounts for Q2/2014, together with revisions of figures extending back to 1997. The revision was due in part to the new national accounts standards implemented under the European System of National and Regional Accounts, commonly referred to as ESA 2010. The ESA 2010 standards provide for a number of changes in accounts preparation, the most important of which are discussed in this Box. First, research and development costs are now classified as investment and are added to the capital stock. Second, purchases of fixed military assets such as military ships and aircraft are no longer recorded directly under public consumption for the year but are recorded as investment and included in the capital stock. Third, goods sent abroad for processing are no longer included with goods imports and exports; instead, the contribution from the foreign company is classified as an imported service (and an exported service in the foreign company's home country). And fourth, accrued pension obligations are recognised as expenses in the payer's accounts and as households' assets, irrespective of whether the obligation in question has been paid. The ESA 2010 standards contain various other provisions as well, including provisions on data sources and processing and those pertaining to publication and revision of national accounts statistics. Statistics Iceland has extended its revisions to other items in addition to those that are new features of ESA 2010, as statistical offices in other European countries have done. Illegal activities such as prostitution, smuggling, and drug sales are now included for the first time, and items such as financial intermediation services indirectly measured (FISIM) and housing costs have been changed significantly.¹

For the period 1997-2007, measured nominal GDP increased upon revision by an average of 3.1% in comparison with the national accounts published in March. For the period 2008-2013, it increased by an average of 4.9%. The increase in GDP at constant prices is larger, at 3.6% for 1997-2007 and 8.5% for 2008-2013. The increase in Iceland's nominal GDP is similar to that in many other countries. In the UK, measured nominal GDP increased by an average of 3.6% for the period 1997-2009; in France, it rose by 3.2% in 2010 (including 2.4% due to ESA 2010); in the Netherlands, it increased by 7.6% in 2010 (including 3% due to ESA 2010); and in Denmark, where the national accounts have been revised back to 1966, measured GDP rose by between 1.6% and 3.1%.

Principal changes in methodology

The items that cause the greatest changes in the expenditures side of the national accounts are as follows:

Research and development expense (R&D) is now classified as investment, whereas it was previously included with intermediary goods. This change increases measured GDP by 1.4%. It increases investment by 14-16% for the past five years, and as a substantial portion of R&D was previously classified as public consumption, public consumption declines by 2½% over the same period. The change increases end-2012 capital stock by 5.3%.

Financial intermediation services indirectly measured (FISIM) – that is, the portion of financial services that customers pay for through interest rate spreads rather than through explicit service charges – have been re-evaluated. The re-evaluation results in a 2.5% increase in year-2007 GDP and a 1% increase in 2013. It shows as an increase in private and public consumption, as well as

Box 1

New national accounts standards

1. For further information, see *Statistical Series* 2014:10, Statistics Iceland, 19 September 2014.

Chart 1
Contribution to increase in nominal
GDP 2007-2013

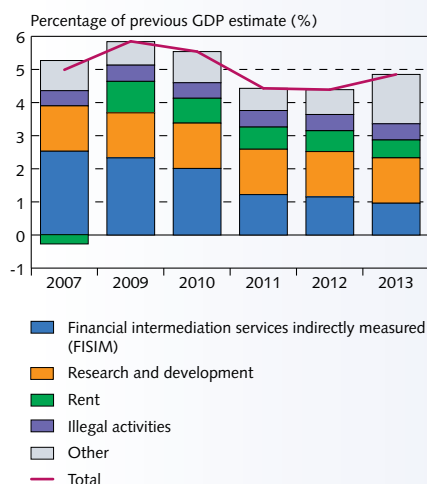


Chart 2
GDP at constant prices and GDP growth
1997-2013

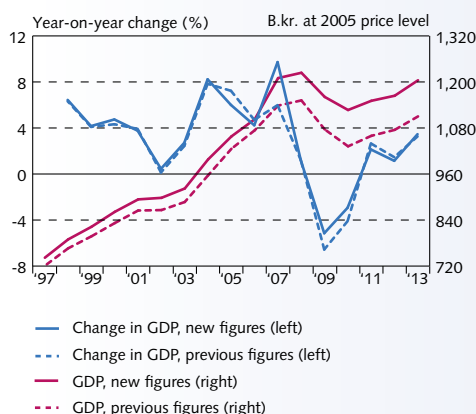


Chart 3
Seasonally adjusted GDP
Q1/2005 - Q2/2014



improving the trade balance and eroding the primary income balance by equal amounts.

Rent has been re-evaluated, causing GDP to rise by ½-1% over the past five years but to decline by 0.3% in 2007.

Illegal activities such as prostitution and drug sales are now included for the first time with GDP in Iceland. According to the national accounts standards, GDP should measure all legal and illegal economic activities involving the sale of goods and services in the market. This item increases GDP by 0.5% and private consumption by just under 1%.

Chart 1 illustrates the contribution of these four items to the changes in GDP estimates from 2007 onwards. As the chart shows, FISIM weighs heaviest early on, although the reclassification of R&D as investment has a strong effect as well.

The ESA 2010 provision classifying the purchase of military assets such as ships and aircraft as investment rather than immediate public consumption has significant effects in many countries but has little impact in Iceland. The provision excluding goods imported for processing and re-exported to their foreign owners from imports and exports has a significant impact on imports and exports of goods and services but does not affect GDP or the trade balance. The rules on treatment of pension savings will have a substantial impact on household net worth but will have no effect on measured GDP and GDP growth.

Revision of developments in GDP growth

As a result of these changes, GDP growth in Iceland is now considered to be somewhat stronger than previously estimated for the period 1997-2008, or 4.7% per year on average instead of the previous 4.4%. This is due primarily to the substantial revision of year-2007 GDP growth, which is now estimated at 9.7% instead of the previous 6% (Chart 2). This is Iceland's highest GDP growth figure since 1971, when it measured 13.1%.

The economic contraction of 2008-2010 is now considered smaller than before: GDP is estimated to have contracted by 5.1% in 2009 and another 2.9% in 2010, as opposed to Statistics Iceland's previous figures of 6.6% and 4.1%, respectively. According to the new figures, GDP growth during the period 2011-2013 is slightly weaker than previously projected, averaging 2.3% per year instead of the previous 2.4%.

Revision of quarterly figures

As in the previous figures, seasonally adjusted GDP peaks in Q4/2007 and bottoms out in Q1/2010 (Chart 3). The timing of the turnaround in the domestic economy is therefore unchanged. The contraction is smaller, however, at 10.9% instead of the previous 12.2%.² Since the economic recovery began in 2010, GDP is now estimated to have increased by 9.3%, or 1.8 percentage points less than previously projected.

Revisions of individual expenditure items

Upon revision, nominal private consumption rises by an average of 4.3% in 2009-2013, with the largest increase in 2009 (6.2%). Nominal public consumption declines by 2.4% for 1998 and is virtually unchanged for 2009-2013. The most pronounced change is in investment, which rises in nominal terms by 17.3% in 2010 and by

2. Based on direct seasonal adjustment of GDP, not Statistics Iceland's seasonally adjusted figures. The difference between the Central Bank and Statistics Iceland's methods for seasonal adjustment is discussed in Box IV-1 in *Monetary Bulletin* 2012/4.

an average of 15.8% in 2009-2013. Total imports and exports are broadly unchanged, but there are significant changes in which imports and exports are classified as imports and exports of goods, on the one hand, and services, on the other, due to the aforementioned change in the treatment of transactions with goods without transfer of ownership.

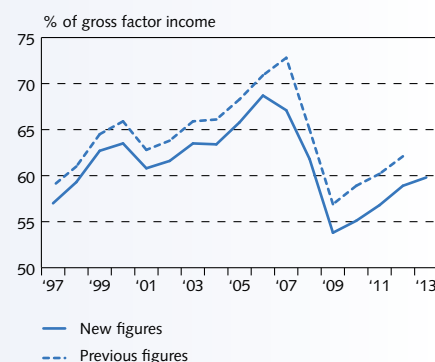
Measured growth in individual expenditure items changes as well. The contraction in private consumption from 2008 to 2010 now measures 10.1% instead of the previous 14.9%, with the change due primarily to the effects of FISIM, particularly in 2009. Private consumption growth during the period 2010-2013 is now estimated at 5.4% instead of the previous 6.3%. Measured growth in investment and public consumption has changed less markedly.

Changes in key ratios

The above-described changes in the national accounts have caused changes in a number of key ratios. For example, the ratio of investment to GDP has increased by 1.4 percentage points, both in terms of the average over the last five years and for the entire period since 1997. The ratio of private consumption to GDP has declined by an average of 0.4 percentage points over the past five years, and the public consumption-to-GDP ratio by 1.2 percentage points. Exports as a share of GDP have fallen by 2.7 percentage points and imports as a share of GDP by 3 percentage points, on average, over the past five years, owing primarily to the increase in GDP. The trade balance improves by 1.9 percentage points for 2007 and by 0.3 percentage points, on average, for the period 2009-2013, due mainly to a re-evaluation of FISIM. Debt-to-GDP ratios decline with the increase in nominal GDP.

The changes in the expenditure accounts also appear in Statistics Iceland's production and income accounts. In the production accounts, revenues from the additional activities now included are entered with gross operating revenues, while wages are broadly unchanged. In the production accounts, income earned by sole proprietors, including many farmers, small-scale fishermen, and tradesmen, is recorded with operating surpluses. This causes the wage share to decline. The estimated ratio for 2007 declines from 72.8% to 67.1%, or by 5.7 percentage points, and the ratio for 2008-2012 declines by an average of 3.2 percentage points. It is now estimated at an average of 58.9% over the 2008-2012 period and 59.8% in 2013 (Chart 4).

Chart 4
Wage share 1997-2013



Source: Statistics Iceland.