

13 September 2011

Screening report

Iceland

Chapter 20 – Enterprise and industrial policy

Date of screening meetings:

Explanatory meeting: 12-13 April 2011

Bilateral meeting: 25 May 2011

I. CHAPTER CONTENT

The *acquis* under the enterprise and industrial policy chapter consists of **policy principles and instruments** which are mainly reflected in communications, recommendations, and Council conclusions and are mostly implemented at EU level through the Competitiveness and Innovation Programme. They are also the subject of EU-wide consultation fora or structured exchanges of good practice. Enterprise and industrial policy also comprises **sectoral policies**. Overall, EU enterprise and industrial policy is strongly driven by the Europe 2020 strategy.

By establishing general **policy principles**, the EU seeks to promote the formulation of competitiveness enhancing enterprise policies and industrial strategies. These are geared towards speeding up structural adjustments, encouraging an environment favourable to business creation, domestic and inward foreign investments, promotion of small and medium-sized enterprises (SME), and entrepreneurship and innovation. More specifically, EU SME policy is characterised by policy recommendations and joint policy review mechanisms comprised in the Small Business Act as well as a common SME definition.

Enterprise and industrial **policy instruments** are developed in an EU programme Competitiveness and Innovation (CIP) 2007-2013. Its 1st pillar, called Entrepreneurship and Innovation Programme (EIP), provides financial support to enterprises and policymakers and is focused on actions which promote access to finance, business services such as the Enterprise Europe Network, European and national innovation policy and policies in support of SMEs. An important policy instrument is Directive 2011/7/EU combating late payments in commercial transactions.

Through enterprise and industrial **sectoral policies**, the EU promotes a more targeted analysis of competitiveness of specific sectors and the launch of sector specific initiatives such as high-level groups, policy forums, studies and expert panels as well as networking initiatives.

The formulation and implementation of enterprise and industrial policy require adequate administrative capacity at national, regional and local level, including efficient consultation processes and cooperation mechanisms.

Policy principles and policy instruments covered under this chapter are not incorporated in the EEA with the exception of Directive on late payments.

II. COUNTRY ALIGNMENT AND IMPLEMENTATION CAPACITY

This part summarises the information provided by Iceland and the discussion at the bilateral screening meeting. Iceland indicated that it accepted the *acquis* regarding enterprise and industrial policy. Iceland indicated that it did not expect any difficulties in implementing the *acquis* by accession.

II.a. Enterprise and industrial policy principles

Iceland is a service-based economy. Industry contributes 21% of its GDP. This share has been steadily increasing in the last three years at the expense of construction and financial services, which were heavily affected by the collapse of the banking sector in 2008 and the ensuing economic crisis. The role of industry is more prominent in Iceland's export structure. Industrial products contribute 48% of export value with metals (aluminium) taking the largest share.

Marine products contribute another 42%. The remaining 10% consist of agriculture, services and other industrial products.

According to Icelandic authorities, the country has been traditionally perceived as a business friendly environment attracting foreign investors. The stock of Foreign Direct Investments (FDI) is above 70% of GDP. According to Iceland, its main competitive advantages lies in strategic location, good infrastructure, availability of skilled labour and natural resources, including cheap renewable energy and clean environment, an entrepreneurial culture and a good innovation system. However, the economic and financial crisis has significantly affected the business environment. Macroeconomic instability, capital controls, and the still relatively poor functioning of financial markets, are currently the main obstacles for foreign and domestic investors.

Following the economic crisis, Iceland started developing a new economic strategy. Its initial phase was the “Moving Iceland Forward” initiative. Nationwide consultations were held in which people from all regions contributed to the process, including representatives from civil society, businesses, trade unions, local councils and the Parliament. The initiative resulted in a set of proposals which were translated into a more concrete framework policy entitled the Iceland 2020 policy statement. This now forms the basis for the Icelandic economic policy in selected areas over the coming years. Work has already started on these area specific policies such as the Economic Activity Plan, which covers main aspects of what is considered industrial policy.

The main emphasis of the government’s economic policy shall be on establishing a stable general macro-economic environment for the economy as well as a reliable economic policy framework and market rules. In order to create an environment for growth, the government intends to ensure the competitiveness and sustainability of the financial and tax environment, access to both domestic and foreign credit, and support more diversified foreign investment.

According to the policy documents, the main growth sectors are likely to be linked to industry and primary production and services, including the high-tech and knowledge industry, innovative sectors and tourism. As the Moving Iceland Forward Initiatives was prepared in country wide consultation, it devotes attention also to sectors, which were identified by people as desirable for stronger public involvement. They are, as follows: tourism, health, knowledge creation and renewable energy. Iceland 2020 includes plans for investment in human resources and the necessary infrastructures for the economy, as well as policies for strengthening of education, innovation and the environment and social infrastructure. Iceland 2020 defines 20 measurable objectives under the headings: Welfare, Knowledge, Sustainability, Economic and Development. Each area will be benchmarked on an annual basis.

SMEs account for close to 45% of employment in Iceland. However, entrepreneurship seems to be gaining significant political focus since the crisis. It is seen as a way to employ people that are entering the labour market or leaving construction and financial services. The OECD has assessed the Icelandic regulatory framework and culture as one of the most conducive to entrepreneurship among all OECD members.

Development of the SME sector is supported by a strategy launched in 2007. The strategy is part of legislation establishing public measures to support technological development and innovation, and is also embedded in the regional development policy. Implementation of the strategy lies with the Innovation Centre Iceland, a government agency responsible for delivering support services and providing subsidies for innovation-related activities.

Iceland is familiar with the Small Business Act (SBA) of the EU and participates in the SME Performance Review, which is the main review and monitoring mechanism of the SBA.

II.b. Enterprise and industrial policy instruments

Iceland participates in the EU Competitiveness and Innovation programme and its predecessor framework programmes since 1994. Iceland has had a positive experience with this participation. In particular, it believes that the Enterprise Europe Network (EEN) helps its small businesses take opportunities arising from the Single market. Iceland's EEN network is composed of three public agencies, which have links with local SMEs – Innovation Centre Iceland, Rannis and Islandsstofa. Iceland is particularly active in the Women Entrepreneurship Ambassadors programme. On the other hand, Iceland had not used of the Entrepreneurship and Innovation Programme (EIP) financial instruments to facilitate access to finance to Icelandic SMEs. However, it is currently re-assessing these options with the European Commission and the European Investment Fund.

Regarding national instruments, the Innovation Centre Iceland, a government agency, is responsible for delivering support services and providing subsidies for innovation and entrepreneurship related activities. It employs 90 people in 8 different regional locations. It provides on average 7,000 free counselling interviews per year.

The late payment Directive (2000/35/EC) has been transposed by Iceland through the EEA agreement. The new amending Directive (2011/7/EU) has not yet been incorporated into the EEA. It is expected that it will be incorporated by the end of 2011. Iceland commits that it will then transpose it.

II.c. Sectoral policies

Conservation and utilisation of energy resources is one of the main sectoral policies which defines industrial policy in general. As mentioned above, metals extracted through energy intensive processes are the second most important Icelandic export item after fish and other marine products. Aluminium production consumes 75% of all electricity generated in Iceland. The Icelandic Master Plan for Hydro and Geothermal Energy Resources is a framework for evaluation of power development proposals. About 100 hydropower and geothermal projects are currently being evaluated and ranked. Policy objectives regarding energy production feature also in Iceland 2020. They aim to reach a 20% share of renewable energy sources in all fuel used in transportation and fishing by 2020 and to have 75% of new cars registered in 2020 run on renewable fuels.

Tourism is the third biggest sector in Iceland, generating about 17% of foreign currency revenues. Tourism and tourism-related sectors employ around 10.000 people or 5% of total employment. In the last decade, the annual number of foreign tourists doubled from 300.000 to 600.000. 82% of visitors to Iceland claim that nature is the most important factor determining their visit. Nature protection is therefore the guiding principle of the national tourism strategy. The main problem of the sector is seasonality, which particularly affects the winter months, so prolongation of the tourist season beyond July and August stands as the second priority. An important measure taken so far is introduction of a quality control system for tourist sites, which is based on the principles first introduced in New Zealand. Iceland would like to strengthen statistical reporting in the tourism sector, therefore, it is investing in better monitoring and research.

The pharmaceutical and health industry represents only 1% of GDP. However, the government considers it to be strategically important, as this is a cutting-edge industry in which Iceland possesses world-class expertise (measured in the number of scientific citations).

One of the priority sectors for Iceland is creative industries, a rapidly growing sector consisting mainly of SMEs and considered to have high further growth potential. The government calculates that these industries currently contribute around 4% of GDP, 5% of employment and more than 3% of exports. The largest share in exports is held by video games. The government has commissioned a study which will form the base for a new strategy on creative industries.

The construction sector was significantly hit by the crisis. The government has adopted some measures, mainly tax incentives, to cushion the effect of the crisis, and plans to continue supporting the sector, particularly through stimulating R&D and to help focus it towards eco-design.

Iceland does not have a national space policy. However, it has participated, and still participates in several EU programmes in relation to space related technology such as the European Earth Monitoring Programme (GMES) or the European Geostationary Navigation Overlay Service (EGNOS). Two EGNOS stations are located in Iceland; one in Reykjavík and the other in Egilsstaðir. Iceland intends to continue its participation in future EU space activities such as GMES and EGNOS. It also intends to participate in the Galileo satellite programme.

III. ASSESSMENT OF THE DEGREE OF ALIGNMENT AND IMPLEMENTING CAPACITY

Overall, Iceland is already highly aligned to the *acquis* in the area of enterprise and industrial policy. It has been cooperating with EU Member States and with the European Commission since 1994 when it joined the EU framework programmes for competitiveness and innovation. In 2008, its business environment was severely affected by the crisis. The country reacted by designing a new comprehensive policy of economic development, which put industrial and sustainable development, innovation and entrepreneurship high on the agenda. Full implementation of these newly planned measures can only go ahead once macroeconomic stability is achieved.

Within the EEA Agreement, Iceland has a good track record fulfilling the obligations of Directive 2000/35/EC on combating late payment in commercial transactions.

Good track record of participation in the EU framework programmes for entrepreneurship and innovation points to Iceland having a satisfactory level of administrative capacity in this field.

III.a. Enterprise and industrial policy principles

Iceland has a good track record of cooperation with the EU in enterprise and industry policy formulation. The new policy currently being put in place reflects well the main EU principles in this area. Iceland is committed to the environmental sustainability aspects of its industrial policy and is consulting a wide range of stakeholders throughout the process.

Iceland has developed mechanisms to monitor the performance of its industrial and enterprise policy. The monitoring mechanisms proposed under the Iceland 2020 strategy are in line with the monitoring mechanism under the Europe 2020 strategy and its flagship initiatives.

The SME sector employs on average a lower share of the total labour pool than the EU average. However, all indicators evaluating Icelandic SMEs and entrepreneurship policy point that

effective measures to support the sector are in place. The low numbers are a result of the small size of the population combined with concentration of labour force in few big energy companies. The SME definition applied by the authorities is in line with the EU definition. Icelandic SME policy is regularly evaluated in the SME performance review of the European Commission, which checks all key aspects of the Small Business Act. Iceland scores high in these reviews.

III.b. Enterprise and industrial policy instruments

Iceland has a successful track record of participation in the EU Competitiveness and Innovation programme (CIP). It had participated in the predecessors of the CIP since 1994.

The performance of the Icelandic members of the Enterprise Europe Network has steadily improved over the period of last three years and has now reached satisfactory levels in comparison with other members of the network in the EU. Further improvements could be achieved notably by stimulating enterprises to utilise more fully the services offered in relation to the internationalisation of SMEs.

Iceland has developed a set of national instruments and established implementation agencies to provide financial support and services to local businesses. It has particular strengths in supporting women entrepreneurship.

In the EEA framework, Iceland transposed Directive 2000/35/EC on combating late payments in commercial transactions including on the level of interest and the provisions related to retention of title for creditors and recovery procedures. Iceland encountered no problems with transposition but needs to transpose the new upcoming Directive 2011/7/EU.

III.c. Sectoral policies

Iceland has few sectoral policies. The main one concerns energy resources which define performance of its metals industry. Iceland has developed a framework for assessments of new projects in the energy intensive sectors, and is putting sustainability high on the agenda. Among other sectors, a tourism strategy is designed and is in line with comparable strategies in the EU. Other sector specific policies emphasise the importance of research, innovation, clustering, niche markets, etc., which put them at comparable level with EU policies in those sectors. Overall, Iceland has the capacity to contribute to EU sectoral policies in many areas, as its industries are often niche and highly knowledge-intensive.