

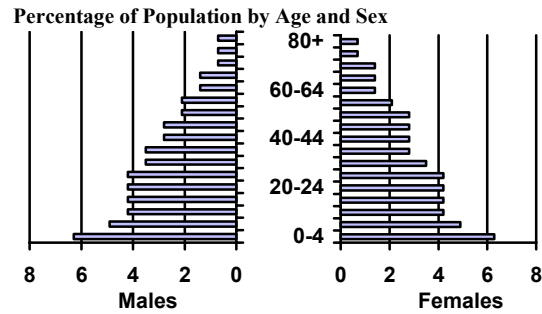
ICELAND

Iceland's population structure has changed considerably over the past 50 years. The figures at right show the percentage of Iceland's total population by five year age groups separately for males and females. In 1950, the structure of Iceland's population formed a pyramid, where each successively younger age cohort represents a larger portion of the total population.

Between 1950 and 2000, Iceland's birth rate fell from 3.70 to 1.90, and life expectancy rose 7 and 8 years for males and females respectively. These factors caused the population structure to diverge from a classic pyramid shape to a formation more representing a pillar, where the percentage of the population in each age cohort is more evenly distributed. Only the older age groups retained the pyramid form.

Looking to the future, the anticipated mix of fertility rates slightly below replacement with rising life expectancy will lead to a fulfillment of a pillar formation. The average age in Iceland will be nearly 41 years old by 2030 compared to today's average age of 35.

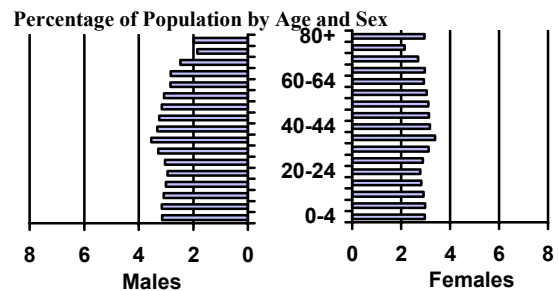
Iceland's Population Structure in 1950



Iceland's Population Structure in 2000



Iceland's Population Structure in 2030



Source: UN Population Division, World Population Prospects (The 2000 Revision).

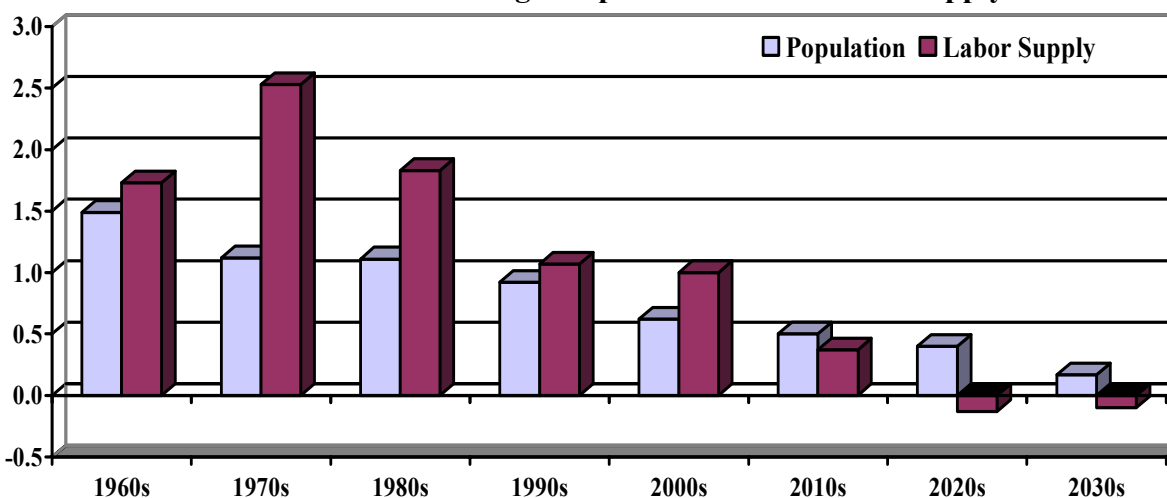
Demographic History

	1950	1960	1970	1980	1990	2000
Life Expectancy at Birth						
Males	70.00	70.80	71.40	73.94	76.25	77.10
Females	74.10	76.10	77.40	79.83	80.81	81.79
Life Expectancy at 65						
Males	-	-	-	80.52	81.35	81.77
Females	-	-	-	83.80	84.36	85.04
Fertility Rate	3.70	3.94	2.84	2.25	2.19	1.90
Net Migration Rate	-0.25	-0.75	-0.36	-0.02	-0.52	0.00

A critical component of a society's ability to expand its production of goods and services is the growth of its labor force. As Iceland's population aged over the past half-century, the growth of its labor force has undergone changes as well. Soon after the end of World War II, many industrialized societies, including Iceland for a period, experienced a spike in birth rates – better known as the baby boom. As a result, population growth rose at a decidedly faster rate in the 1960's. As the baby boom entered the labor force, including an unprecedented number of its female members, labor supply growth increased rapidly during the 1960's and 1970's. However, fertility rates have dropped considerably from those of the early post-war period - a trend that has persisted to the present. This created a period of high workforce participation in Iceland such that between 1970 and 2000, total dependency rates in Iceland dropped 47 percent, while youth dependency dropped 52 percent.

Iceland has enjoyed robust labor supply growth over the past 50 years; however, this trend will not last indefinitely. As a growing segment of Iceland's population moves into retirement over the next few decades, labor force growth is expected to slow considerably. This is caused by the combination of several factors – prolonged fertility below replacement, improving life expectancy and a greater proportion of the population in age groups that have lower propensities to work. In fact, by the 2020s, these forces will actually cause Iceland's labor force growth to shrink. As a result, Iceland will face a growing inactive portion of its population, reflected by a 7 percent increase in the total dependency ratio and a 73 percent rise in old age dependency rates between 2000 and 2030.

Annual Percent Change: Population versus Labor Supply



Source: World Bank, World Development Indicators database

Dependency Ratios

	1970	2000	2030	% change 1970-2000	% change 2000-2030
Youth- (Inactive pop 0-19)/ LF 15+	0.89	0.42	0.34	-52.33	-20.11
Aged- (Inactive pop 55+)/ LF 15+	0.24	0.18	0.31	-25.81	72.84
Total- (Inactive pop 0-19 and 55+)/ LF 15+	1.13	0.60	0.64	-46.72	7.27

Source: Sources: International Labor Office, LABORSTA database, current through 2001; UN, Population Division, World Population Prospect (The 2000 Revision); OECD, CDE database on labor statistics, current though 2002

Old Age Pension System

Iceland's old age pension system is a two-tiered system with a universal benefit and compulsory occupational scheme. As of 2002, the universal pension is worth IKr 19,900 per month and is gradually reduced if annual income exceeds IKr 1,296,060 and is completely eliminated when income exceeds IKr 2,095,660. There is a pension supplement of up to IKr 34,372 per month for a single person that is withdrawn when income exceeds IKr 1,332,480. Additionally there is a means-tested pension supplement of IKr 15,257 per month for a single person along with certain allowance for living expenses and dependent care.

To receive the maximum benefit, a retiree must be age 67 with at least 40 years' residency between ages 16 and 66. The benefit is reduced proportionally if residency years are below the cap, and no benefit is payable if residency is less than 3 years. This benefit is adjusted annually according to the current state budget for changes in wage trends and adjusted at least to the cost-of-living index.

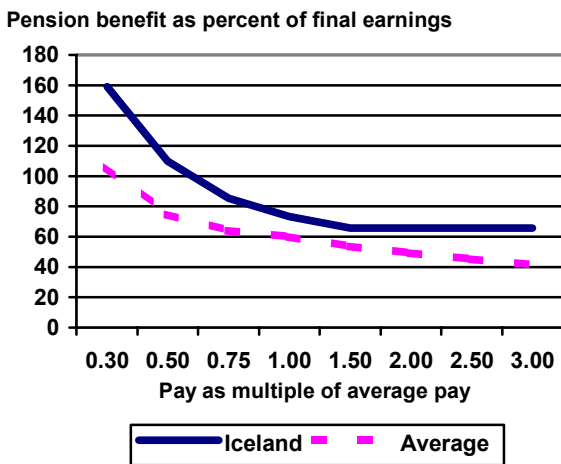
The mandatory occupational pension schemes are required to provide at least 56 percent of lifetime average earnings for a retiree, who meets the normal retirement age and has contributed to the plan for 40 years. This is equivalent to 1.4 percent of average lifetime salary per contribution year. The normal retirement age is 65 for public-sector employees and 67 for private sector employees. The benefit is payable as an annuity and is reduced if the retirement age and 40 years' contributions are not attained. Benefits in payment must be indexed, at minimum, to the consumer price index.

To finance the universal pension program, employees do not contribute to the plan, while employers put in 5.83 percent of payroll – a portion of which is used to finance unemployment benefits. For the occupational scheme, employees contribute 4 percent of wages and employers add 6 percent of payroll to fund the program.

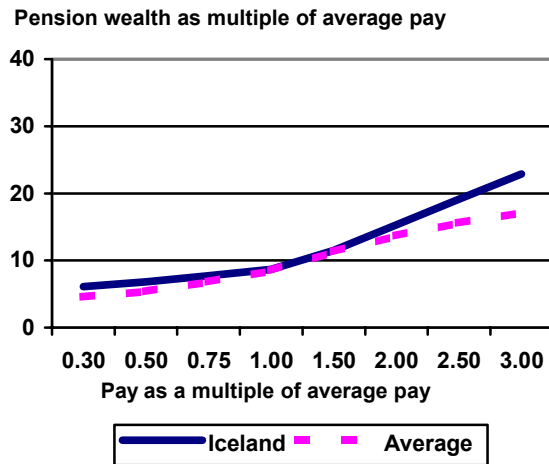
As the graphs indicate below, Iceland's old age pension system provides above average income replacement for all income groups compared to the other OECD nations. However, retirees from Iceland's pension scheme can accumulate pension wealth roughly in-line with the OECD average, although full career above average wage earners can generate slightly higher levels by retirement.

Source: Social Security Administration, Social Security Programs Throughout the World (2002).

Gross Replacement Rates
Iceland v OECD Average



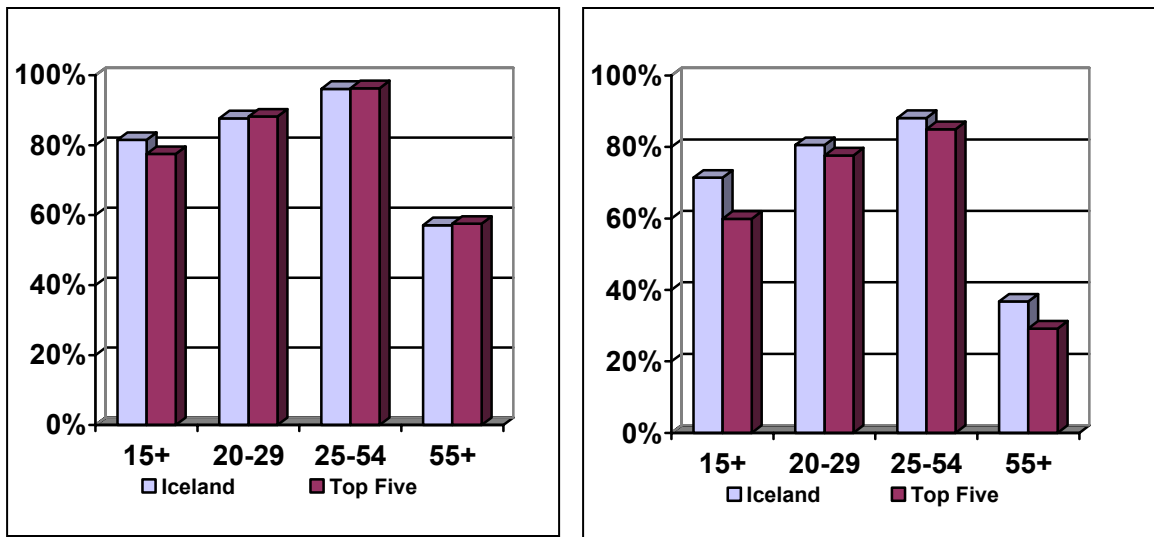
Gross Pension Wealth
Iceland v OECD Average



Source: Whitehouse, Edward (2003)

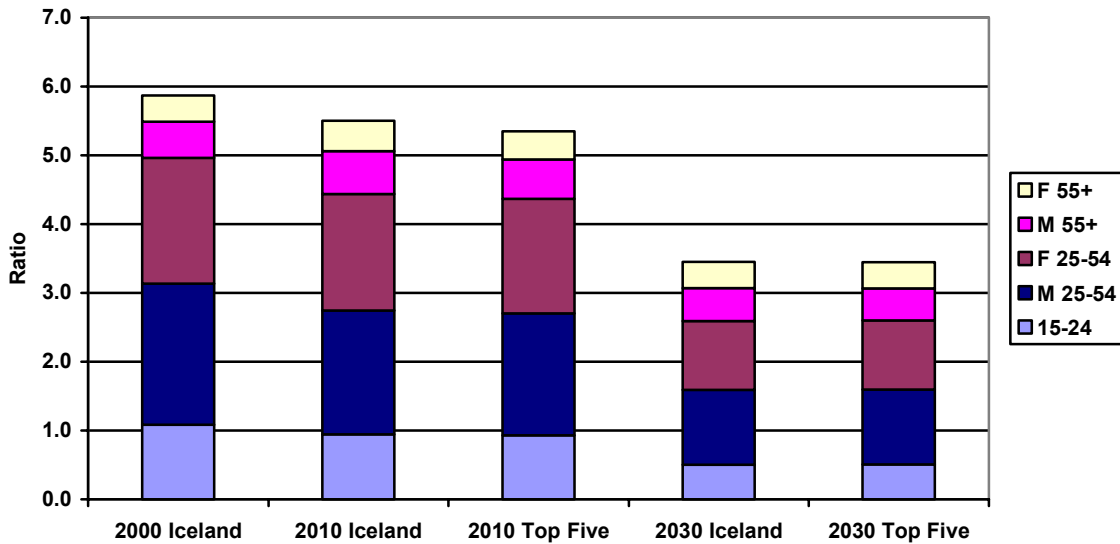
Notes: Pension wealth estimates are a multiple of economy-wide average.

Labor Force Participation Rates: Iceland v Top Five OECD Country Composite



Source: OECD, Corporate Data Environment database on labor statistics, current though 2002

Ratio of Workers in Iceland 15+ to Retirees 60+ in 2000, 2010 and 2030 and Under Alternative Assumptions of Old Age Participation Rates for the Top Five OECD Countries



Source: UN Population Division, World Population Prospects (The 2000 Revision); OECD, Corporate Data Environment database current though 2002

Much of the burden caused by demographic aging is due to rising dependency rates. In the coming decades, many industrialized nations will need to figure out how to support a growing inactive population with fewer workers. Iceland is in a unique position among the OECD countries; it excels at achieving high workforce participation. The figures above indicate that all age and gender sectors of Iceland's population are participating at levels virtually equivalent to the average of the Top-five OECD nations. However, even at the relatively high workforce participation rates, Iceland's ratio of workers to retirees is expected to fall from 5.9 to 3.5 between 2000 and 2030. Yet, unlike many other OECD nations, Iceland will continue to enjoy higher labor supply growth than population growth over the present decade, making the current period a good opportunity to adopt policies to address its old-age dependency burden that will build in coming periods.