8. Making up the Balance and Conclusion

8 – 1 Summary of Economic Effects

In the preceding chapters we have studied the effects EU membership would have in Iceland. Because of Iceland's membership in the European Economic Area, the effects are not as far reaching as for total outsiders. Our conclusions are that the most important factors that would change are the:

(1 State's budgetary expenses, where the Icelandic state would be a net contributor to the EU in line with other rich EU member states;

(2) Monetary union, where estimations on effects vary substantially, but almost all indicate positive effects;

(3) Agricultural policy, where the Icelandic society's benefits from the Common Agricultural Policy would be cheaper food and that the least efficient farmers will be pushed into more productive jobs;

(4) Fisheries policy, which is an unsolved problem where the EU Common Fisheries Policy in its current form could possibly lead to losses by damaging the long-term viability of fisheries.

As noted in chapter 4, the Customs Union, foreign direct investment and economic specialisation are not likely to have large effects[284].

Table 33 shown on next page summarises the macroeconomic changes in Iceland from EU membership and makes up the balance as a percentage of GDP. Table 33 (on next page) is based on the findings presented in preceding chapters and essentially answers the economic part of the central question raised in the introduction in chapter one, by providing a profit and loss calculation on the effects in Iceland if Iceland abandoned the EFTA-EEA arrangement for EU membership.

[284] If Iceland were not an EEA member, this could be different.

Table 33. Estimated total macroeconomic benefits and costs for Iceland from EU membership, as a percent of GDP

	Benefit	**Cost**
State finances: [285]		0.25% [286]
Customs Union: [287]	Negligible [288]	
Economic and Monetary Union: [289]	5% [290]	
Common Agricultural Policy: [291]	1.25% - 2.5% [292]	
Common Fisheries Policy: [293]	Minimal [294]	0.00% - 3% [295]
Other effects, foreign direct investment and specialisation: [296]	Negligible [297]	Negligible [298]
Total benefits and costs:	Benefits of between 6.25% and 7.5%	Costs of between 0.25% and 3.25%
Average theoretical benefits beyond costs:	(6.25% + 7.5%) / 2 - (0.25% + 3.25%) / 2 = 5.1%	
Likely benefits and costs based on political options: [299]	(6.25% + 7.5%) / 2 = 6.9%	0.25%
Grand total: [300]	6.9% benefits minus 0.25% costs = **Benefits of 6.6 % of GDP** [301]	

[285] Discussed in chapter 4. Payments to the EU minus payments received back from the Union.
[286] With an error of estimation of 0.15 percentage points up or down.
[287] Discussed in chapter 4.
[288] Because Iceland is already in the EEA.
[289] Discussed in chapter 5.
[290] When all of Europe has adopted the Euro. With the current size of the Euro-zone the effects would be about half, i.e. 2.5% of GDP.
[291] Discussed in chapter 6.
[292] Of this amount savings on food corresponds to 0.75% - 2% of GDP and a further estimated 0.5% of GDP comes from farmers moving to more productive jobs. Households' direct savings on cheaper food would be higher, i.e. 1.5% - 4% of their income.
[293] Discussed in chapter 7.
[294] Through total removal of customs duty on fish products and possibly some EFF support.
[295] Depending on the outcome of accession negotiations. As outlined in chapter 7, it should be possible to have zero losses on the CFP. The 3% figure refers to a scenario where overexploitation has caused a 50% reduction in fish stocks, as is the case with some fish stocks in EU waters. However, since this happened gradually in the EU, there should be ample time find alternative employment.
[296] Discussed in chapter 4.
[297] Because Iceland is already in the EEA.
[298] Idem.
[299] See text and comments in respective chapters, particularly chapter 7 on options to counter the CFP attitude of overexploitation.
[300] Based on that skilled negotiators carry out accession negotiations and Iceland's demands / political position be well defined. (*Footnote 301 printed on next page*).

8 – 2 Conclusion

Table 33 on the previous page shows that although the Icelandic state treasury would lose money equivalent to 0.25% of the GDP on EU membership, the macroeconomic gains for the economy and net welfare change could be substantially larger than the expenses. When full effects of EU membership have taken place, some 10-20 years after accession and after adopting the Euro, the Icelandic GDP could be approximately 6.6% higher than if the country stayed outside the Union.[302] However, an exception is the Common Fisheries Policy (CFP) where it appears not feasible for Iceland to accept the CFP without some safeguards that marine biological advice on fish catch quotas being rigorously followed. Under the current circumstances, the EU CFP could in the long-term lead to macroeconomic losses possibly outweighing many of the other gains from EU membership. Nevertheless, we believe that it would be possible in EU accession negotiations to negotiate safeguards for the fisheries, i.e. first priority to be exempt from the CFP; if that is not acceptable to the EU, then that scientific advise on maximum sustainable yield be followed rigorously; and as a last resort Iceland would simply not use its full TACs[303] given to it from the EU, thereby preventing overfishing.[304]

Trying to answer the question if the EEA provides Iceland with all the economic and political advantages of EU membership, it appears that the answer is no, - it does not. The question has to be modified, however, from asking not only about advantages, but also about possible disadvantages of EU membership. From an economic perspective, the Icelandic state will have increased expenses through contributions to the EU common budget, beyond what Iceland will get back in subsidies. This amounts to the previously mentioned 0.25% of GDP. These contributions would have to be financed through increased direct or indirect taxes, which in itself is a negative factor when trying to stimulate economic growth. However, the monetary union will likely have a large positive effect by stimulating increased trade, more efficient production and less

[301] This means that in a number of years, possibly two decades after accession, the Icelandic GDP would be approximately 6 ½ % higher than if Iceland stays outside the EU and EMU.

[302] Interestingly, Lejour et al. (2008) estimate that Croatia's GDP might increase by between 8% and 9% by joining the EU. We would like to add that Croatia's benefits from joining the EU would likely be larger than Iceland's benefits, because Croatia does not participate in the EEA and Croatia's current GDP per capita is substantially lower than Iceland's GDP.

[303] Total Allowable Catches.

[304] For a detailed discussion of the problems facing fisheries in Europe, see Chapter 7.

price discrimination. The Customs Union with a further removal of trade barriers would also produce net welfare gains, although the EEA already provides for a free movement of industrial goods. Notably the food and agricultural sector will be influenced deeply by opening the Icelandic market to the Common Agricultural Policy (CAP). There would be increased freedom in the trade of agricultural products from Europe, which would not only reduce food prices in Iceland, but also push many small farmers over to other more profitable occupations, which would increase net economic welfare. Since the average Icelandic farmer's productivity has for many decades been below society's average productivity, it is reasonable to expect that better paid jobs would be available. Iceland is a founding member of the World Trade Organisation (WTO) and the WTO will promote increased freedom in trade of agricultural products in the coming years. Joining the EU CAP will speed up the inevitable liberalisation process of the Icelandic agricultural sector, perhaps in a similar manner as happened in Finland when Finland joined the Union in 1995.

With the exception of the CFP in its current form, it appears that the macroeconomic benefit for the Icelandic society as a whole is considerably higher than the extra government expenses stemming from EU membership. The state would pay more to the EU than would come back from EU funds, but the net welfare increase and macroeconomic benefits in the form of lower food prices, reforming the agricultural sector, removing all intra-EU customs controls, and becoming a member of the European Economic and Monetary Union (EMU), appears to outweigh the state's extra expense by a considerable margin. EU membership would possibly influence ownership of fisheries companies, some of which might possibly be bought by foreign investors. However, new ownership is not likely to change much since all EEA (EU) citizens can invest and spend their profits wherever they want regardless of nationality. It should be reiterated that the main problem with the CFP is that EU fisheries ministers always decide to catch more fish from the ocean than nature can support in the long term. This has led to drastic reduction in catches in current EU waters, and the same might happen in Icelandic waters if fishing quotas are increased beyond sustainable yield. Considering that fisheries contribute to approximately 6% of Iceland's GDP, a damage to fisheries as an economic resource would have a very negative effect, at least until other jobs could be created. Fish has not disappeared from EU waters, but some stocks have been reduced to half of what they were a few decades ago. Unless the EU fisheries policy is changed, it can end with irreversible negative effects.

On the political front, it appears that membership of the EU would increase the influence on how EU legislation is formulated and voted for, as Iceland has to accept EU legislation anyway through the EEA treaty. The current situation, just to be consulted on new legislation and then having it imposed in the form of obligatory incorporation into national law is worse than participating fully in the formulation of new legislation as EU member states do. As a small member, Iceland could increase its bargaining power by aligning politics with other small members of a similar political and cultural background, notably the Nordic Countries (Finland, Denmark, Sweden and possibly in the future also Norway if Norway joins the EU). On the level of "high politics", meaning power and security, we find that at this early stage it is not clear how the EU Common Foreign and Security Policy (CFSP) will evolve. If the EU evolves into a giant superpower willing to throw its weight around in international politics, then some questions of political sovereignty and independence may arise, especially for smaller member states which have less influence and voting power than the big members.

We therefore conclude that there appears an economic advantage of Icelandic EU membership, with the possible exception of the CFP. But as mentioned in chapter 7, just to exclude EU membership without even trying to negotiate an acceptable deal, with emphasis on sustainable fisheries, would be a mistake. The requirement would be that scientific advice on fish catch quotas be closely followed regardless of contemporary economic or social demands. Alternatively, Iceland could pursue the option to sell its EU allocated catch quota on a gradually increasing price scale, thereby preventing catches from passing sustainable yield by simply putting the price too high on the part which exceeds sustainable yield. In that case, Iceland would in all probability substantially benefit from EU membership.

The outcome of EU accession negotiations is very important for an aspiring member state. Although the main rule is that new member states have to adjust themselves to the Union, it is possible to negotiate some exceptions, e.g. as Denmark did with foreign ownership of summerhouses, or agricultural support in the northernmost areas of the Union. It cannot be repeated too often that Icelandic negotiators and politicians will bear a huge responsibility in any accession negotiations[305].

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[305] Mistakes can lead to large losses. An example is the EEA agreement with free flow of capital. Using the liberty of free flow of capital, many Icelandic banks had very large operations outside Iceland. When the main Icelandic banks collapsed in 2008, the Icelandic government, being the guarantor of parts of the deposits in accordance with European rules, was left with a financial burden far outweighing its domestic economics. When the EEA agreement was signed, nobody could foresee this.

Last but not least, if EU membership does not turn out according to expectations, there is nothing that prevents members from following Greenland's footsteps and leave the Union. The EU will not use force to keep members in the Union if they decide to leave in accordance with the provisions of the Lisbon Treaty. However, in such an unusual case that a member leaves the Union, there is no automatic guarantee that the departing state could join or renew the EEA arrangement, although it is likely that some cooperation arrangement between the Union and a departing state would be made, in a similar manner as the Union has agreements with many non-member states.

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