

“Iceland between Europe and the United States”
Seizing new opportunities in a changing world

**Utrikespolitiska Institutet
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Ladies and Gentlemen

Allow me to start with a few comments on the relationship between Iceland and Sweden, since it is very much in the Icelandic tradition to put things into a historical perspective. Most of you know that Sweden and Iceland share a long history together – which stretches all the way back to the settlement of Iceland.

It is generally believed that Iceland was first settled in the mid eighth century. The sagas tell of the Swedish explorer Garðar Svavarsson who in the year 870 is said to have sailed his ship from Sweden to Iceland. Garðar was the first person to sail around Iceland and thus confirm that we are indeed an island. He was also the first Viking to settle in Iceland, but only managed to stay for one winter.

The modern societies of Iceland and Sweden have much in common, which explains why Icelanders feel so much at home in Sweden. There are about 4000 Icelanders living here, half of them in the Stockholm area. Many come as students, both at undergraduate level and postgraduate level.

The Icelandic Embassy in Stockholm was one of the very first Icelandic embassies to open, having been established in July 1947, shortly after we received full

independence from Denmark. Lately, Icelandic investors have turned their eyes to Sweden looking for business opportunities, resulting in several sound and profitable investments.

Ladies and Gentlemen – the title of this talk is “Iceland between Europe and the United States”.

In 1948, Nordic Foreign Ministers told their Icelandic counterpart “how fortunate Iceland was to be situated out in the Atlantic”. Of course, the immediate reason for the sentiment was the communist coup in Prague and the feeling of insecurity among many smaller states in Europe in the face of Soviet expansionism. Iceland was seen as insulated from this threat by the wide ocean.

There was another aspect to Iceland’s position in the middle of the Atlantic. This was geostrategic and has had an important influence on the shaping of Iceland’s security and defence policy since the Second World War.

I will discuss these matters in further detail in a few minutes. But first let me indicate the wider thesis of my talk. “Iceland between Europe and the United States” is a particular way of positioning Iceland, not only geographically, but also culturally, politically and economically. I will argue that this is much too limited a way of analysing Iceland’s position in the contemporary world. We see it in a more multidimensional way than before – we are between Asia and Europe as well as between America and Europe. This theme I will return to. But first to continue on matters of security and defence.

Underpinning Iceland’s national security has been its Defence Agreement with the United States dating from 1951. In this context it is important to remember our special situation as a country without its own military. The US base at Keflavik

was, for many years, home to several thousand military personnel and their family members together with fighter planes, maritime patrol aircraft, search and rescue helicopters and later AWACS (Airborne Warning and Control System) planes. It thus guaranteed our security in a world where an expansionist Soviet Union was deemed to be a threat.

At the same time the Defence Agreement and our membership of NATO – Iceland is a founding member - gave the US and other NATO allies a valuable strategic asset in the Keflavik base guarding the air and sea lines of communication across the North Atlantic.

After the end of the Cold War the geostrategic role of Iceland diminished. The early nineties were a time to reflect, reform and reinvent roles, not only for countries but international and regional organisations as well. NATO was by many thought to be a Cold War relic and not an organisation for our time. This turned out to be far from the truth and NATO has proved that it has indeed an important role to play in the complicated security environment of today.

The end of the cold war, however, was just part of a complex series of developments which changed the ballgame in ways which could not have been anticipated. New opportunities came to light and globalisation greatly picked up speed. Iceland along with other EFTA countries, at the time including Sweden, negotiated the EEA Agreement, and started to seek ways to play a more international active role.

Iceland continues to look to the US and to NATO as the mainstays of its defence and security. Indeed, it is our strongly held view that the USA must remain engaged with Europe and that credible European defence will best be secured in cooperation with the US.

The prime venue for defence cooperation is NATO and Iceland has sought over recent years to increase its contribution to the Alliance. This has been a challenge as we have no military forces of our own. Instead, we have concentrated on building up civilian crisis response capacity and have contributed to NATO peacekeeping operations in Afghanistan, Bosnia-Herzegovina and Kosovo. We will continue with these projects along with participation in UN peacekeeping operations.

After the Cold War US forces in Iceland were reduced to a minimum. Negotiations are ongoing between the Icelandic and US governments on further adapting the defence relationship to a changed security environment. It is being emphasized on the part of Iceland in these talks that a minimum level of defence preparedness must be maintained in Iceland, as in all our Allied and neighbouring states. Meanwhile we are prepared to make a contribution by assuming costs related to search and rescue in support of US forces and the operation and maintenance of the airfield and certain associated facilities at the Keflavik base.

Any security and defence policy must also take account of new threats and challenges. The incidence of conventional wars has reduced markedly in the past 20 years. At the same time new threats have appeared. Indeed, this was the focus of the UN summit last September.

Iceland's geographical position is not a protection against the wide range of threats and challenges facing the world today. These include the proliferation of nuclear weapons, the scourge of terrorism, transnational crime and environmental degradation. As Kofi Annan has stated, "In a world of interconnected threats and challenges, it is in each country's self-interest that all of them are addressed effectively ... by broad, deep and sustained global cooperation." It is my view that

any nation assessing its defence and security needs must see them in the light of the global and multifarious nature of current security challenges.

While the end of the Cold War and growing globalisation have presented the international community with many pressing problems they have also offered multiple opportunities.

There has been a fair amount of coverage in the Nordic press about Icelandic investments in the Nordic countries and elsewhere. These are indeed massive and not only in relation to the small size of the Icelandic economy. Several factors have facilitated Icelandic operators in grasping the opportunities opened by globalisation most of which can be attributed to policies pursued by the Government of Iceland in recent years.

First, the authorities have since the early nineties worked effectively on liberalising, deregulating, and improving the environment in which economic entrepreneurs operate. Important structural reforms were made with privatisation and tax reform, and a successful fisheries management system, based on transferable quotas, was strengthened. The role of the state in the economy has been significantly decreased and is now mostly limited to making and enforcing the basic rules and guidelines by which all businesses must abide.

As a result, the economy has been performing extremely well in the last years. This is evident from Iceland's rating with agencies such as Moody's and Standard and Poors, on economic growth, competitiveness, creativity, level of corruption and unemployment - and not least on the quality of life. Last week Iceland was placed in third position, after Denmark and Finland, in Forbes Capital Hospitality Index on how friendly the country is to foreign investment.

Gone are the days when the State owned the three largest banks in Iceland, ran a shipping company and even produced fertilizer and cement. The Government has also greatly reduced corporate taxes, which has attracted foreign investors, encouraged local investment and discouraged our companies from moving abroad. Lower taxes and the Government's privatisation programme along with sound economic policies have created stable economic conditions for Icelandic – and foreign - businesses to operate in. We have also been able to reduce government debt by half in a period of just five years from 40% of GDP in 2001 to 20% in 2005. External debt has come down from over 26% to less than 9% in the same period. As Finance Minister for 7½ years I am very pleased with this result.

Another factor is Iceland's pension system which is stronger than in most comparable countries. Already, in the beginning of the 1970s a private pension fund scheme was established, which is now more or less fully funded. A few years ago, similar changes were made to the public pension system and as a result this system will in due course also be fully funded. Important changes have been implemented in order to strengthen the financial position of the funds and ensure similar pension rights for all pensioners. Increased freedom of choice, i.e. greater emphasis on voluntary pension savings, is also an important element. As a result, pension fund assets have grown dramatically as a percentage of GDP. At the end of 2004 pension fund assets, foreign and domestic, were equivalent to about 110% of GDP.

Furthermore, the Government has pursued an active policy of removing trade barriers and increasing market access for Icelandic businesses, both in our most important markets and in new ones.

The establishment of the European Economic Area in 1994 was a major step which we took together with Sweden and the other EFTA countries at the time.

The EEA provided access to the EU's Internal Market with freedom of movement of goods, services, labour and capital in the whole area. In addition we contribute generously with Norway and Liechtenstein to the solidarity funds for less developed parts of the EU. We consider the EEA to be a remarkable success and a durable arrangement for all parties. I, therefore, see no immediate reason for why Iceland should seek membership in the European Union. One can indeed be a good European without being a member of the EU.

Despite the key contributing factors I have just described, I must admit that we have been pleasantly surprised with the robust activity of Icelandic investors in European markets.

Having said all this, it is only reasonable to ask whether the Icelandic investment abroad is viable? I believe that it is - that this development is truly built on solid grounds. However, it is only to be expected that some mistakes will be made and not all investments will live up to expectations. Those who take risks will often profit, but some investments will inevitably also carry losses. That does not change the fact that the great expansion of Icelandic investments abroad is built on firm foundations. As long as our businesses can continue to rely on sound economic policies at home, an open and dynamic banking system, an attractive tax environment, and a highly qualified work force, the Icelandic economy will continue to flourish.

Ladies and Gentlemen,

I have taken a fairly wide ranging look at the international environment. My analysis has strayed somewhat from my title, "Iceland between Europe and the United States". It is, however, a useful place to start simply because this geographical fact contrasts with the complex picture of our relations with the

world. In matters of trade we are closer to Europe – certainly, the EU is by far our biggest trading partner. But at the same time we are pushing into markets in other parts of the world.

Globalisation has an impact on us all and Iceland is accordingly broadening its horizon. Increased focus is now given to new and interesting markets, such as India, China and Africa. In two weeks an Icelandic embassy will be opened in New Delhi and recently we opened an embassy in Pretoria, South-Africa. Iceland and China have also, on a bilateral basis, agreed on undertaking a feasibility study on establishing free trade between the two countries. Through EFTA we have a wide net of free trade agreements, the aim of which is to ensure that our operators enjoy equal terms of trade vis-à-vis major competitors in different markets.

We are also working hard to extend our network of air traffic agreements to ensure that the dynamic Icelandic air carrier sector, which by the way is totally privately owned, has a firm basis for operations around the world.

In its foreign policy the Government of Iceland has over recent years taken a determined course to become more active in international relations. For this reason we have taken on important duties in several international organisations to which we belong. We take part in peacekeeping operations, as I mentioned earlier, we held the presidency of the Arctic Council last year, and this year we are in the Chairmanship of the Council of Baltic Sea States. At present we also coordinate the Baltic-Nordic constituency in the World Bank. Moreover, Iceland has put forward its candidacy for a non-permanent seat on the UN Security Council for the period 2009-10 and is campaigning with the active assistance of our Nordic partners.

This brings me to one aspect of the way in which we relate to the world which remains more significant and more enduring than most others. This is our identity as one of the Nordic countries. The strength and influence of Nordic values over the past century has been remarkable. These include a strong commitment to peaceful international relations, development and democratic principles which sadly are often challenged by extremism, as we have witnessed in the past few weeks with regard to the dispute over the cartoons first published by Jyllandsposten in Denmark. The Nordic family is fundamental to Iceland at the official government level but even more so among ordinary people. It is important to further strengthen that relationship.

Låt mig till slut få tacka Utrikespolitiska institutet för att jag fick komma hit.

Det är onödigt att använda många ord på Islands och Sveriges goda relationer. Men låt oss komma ihåg att för att upprätthålla goda relationer måste man känna och förstå varandra. Just därför är det viktigt att få tillfälle att, som här, förmedla tankar om hur vi upplever vår situation, ett litet land mellan Europa och USA, och, inte minst, höra era reaktioner på det jag haft att framföra.

Jag skall göra mitt bästa för att svara på frågor. Tack för att ni tog er tid till att komma hit.

Ladies and Gentlemen – thank you for your attention. I will now be happy to try to answer any questions you may have.