MONETARY BULLETIN

2020•1

Contents

5 February 2020

The objective of the Central Bank of Iceland's monetary policy is to contribute to general economic well-being in Iceland. The Central Bank does so by promoting price stability, which is its main objective. In the joint declaration made by the Government of Iceland and Central Bank of Iceland on 27 March 2001, this is defined as aiming at an average rate of inflation, measured as the twelve-month increase in the CPI, of as close to 2½% as possible.

Professional analysis and transparency are prerequisites for credible monetary policy. In publishing *Monetary Bulletin* four times a year, the Central Bank aims to fulfil these principles.

Monetary Bulletin includes a detailed analysis of economic developments and prospects, on which the Monetary Policy Committee's interest rate decisions are based. It also represents a vehicle for the Bank's accountability towards Government authorities and the public.

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Vol. 22 no. 1, 5 February 2020

ISSN 1607-6680, print
ISSN 1670-438X, online

This is a translation of a document originally written in Icelandic. In case of discrepancy or difference in interpretation, the Icelandic original prevails. Both versions are available at www.cb.is.

Icelandic letters:

ð/Ð (pronounced like th in English this)
þ/Þ (pronounced like th in English think)
In *Monetary Bulletin*, ð is transliterated as d and þ as th in personal names, for consistency with international references, but otherwise the Icelandic letters are retained.

Statement of the Monetary Policy Committee 5 February 2020

The Monetary Policy Committee (MPC) of the Central Bank of Iceland has decided to lower the Bank's interest rates by 0.25 percentage points. The Bank's key interest rate – the rate on seven-day term deposits – will therefore be 2.75%.

Leading indicators suggest that GDP growth was stronger in 2019 than previously assumed, while the outlook for 2020 and 2021 has deteriorated, according to the Bank's new macroeconomic forecast, published in the February *Monetary Bulletin*. According to the new forecast, GDP growth will measure only 0.8% this year, compared to 1.6% in the November forecast. The poorer outlook is due primarily to headwinds facing the export sector and tighter financing conditions for domestic firms.

Inflation declined rapidly over the course of 2019 and aligned with the target in Q4. It continued to fall in January, measuring 1.7%, the lowest observed inflation rate since autumn 2017. Underlying inflation has also fallen and is now at target, as are most measures of inflation expectations. According to the Bank's new forecast, inflation will be lower than was projected in November and below the target for most of the forecast horizon.

The monetary stance as measured in terms of the Bank's real rate has therefore tightened somewhat since the MPC's last meeting. The rise in corporate credit spreads has tightened the monetary stance even further.

Because inflation expectations are more firmly anchored to the target than before, monetary policy has had the scope to respond to the deteriorating economic outlook. The task of monetary policy is to secure medium-term price stability, but also to use the scope that it has to support a normal level of capacity utilisation.

Near-term monetary policy decisions will depend on the interaction between developments in economic activity, on the one hand, and inflation and inflation expectations, on the other.

Monetary Bulletin 2020/1[1]

The global GDP growth outlook is broadly unchanged from the forecast in the November *Monetary Bulletin*. Despite rising concerns about the impact of a new virus originating in China, global uncertainty has receded since November and the risk of a further softening of global GDP growth has eased. A key factor in this is the recent agreement reached by the US and China in partial resolution of their trade dispute, which reduces the likelihood of further escalation and even more severe repercussions for the global economy.

The Icelandic economy experienced a major setback in 2019, with the collapse of airline WOW Air and further shocks to the airline industry, coupled with the failure of the capelin catch and a deterioration in terms of trade. GDP growth slowed markedly, measuring only 0.2% for the first three quarters of the year. It outpaced the November forecast, however, which assumed a 0.1% contraction. Owing to more rapid growth in economic activity in the first three quarters, together with signs of stronger growth in private consumption and more favourable external trade in Q4, the GDP growth outlook for the year as a whole has improved since November. GDP is now projected to have grown by 0.6% in 2019 instead of contracting by 0.2%.

The outlook for 2020 and 2021 has deteriorated, however. Goods and services exports now appear set to contract this year instead of growing marginally, and if they do, it will be the first time since the early 1990s that exports have contracted two years in a row. A slower recovery of tourism, production difficulties in the aluminium industry, and the second consecutive capelin catch failure play a major role in explaining the deteriorating outlook. Furthermore, corporate interest rate spreads rose sharply in late 2019, leading to a downward revision of business investment in 2020 and 2021 relative to the November forecast. Year-2020 GDP growth is assumed to measure only 0.8%, compared to 1.6% in the November forecast. Although growth is projected to increase to 2.4% in 2021, it remains 0.5 percentage points below what was expected in November. The forecast for 2022, however, is broadly unchanged.

Unemployment has risen markedly in the past twelve months and is expected to keep increasing through this year, averaging just over 4% in 2020 and 2021. It will therefore be higher and take longer to subside than was projected in November. Thus the outlook is for the slack in the economy to persist longer than previously anticipated.

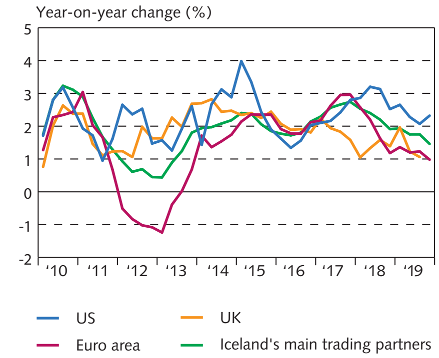
As was forecast in November, inflation continued to ease in late 2019, measuring 2.5% in Q4. It declined further in January, to 1.7%, and is expected to remain below the inflation target over the forecast horizon, before inching back up to the target towards the end of the period. Inflation will therefore be below the November forecast for much of the forecast horizon, as the slack in the economy is expected to be more persistent than was assumed in November.

1. The analysis appearing here is based on the Bank's assessment of economic developments since the publication of *Monetary Bulletin* 2019/4 in November 2019, and on the updated forecast presented here. It is based on data available at the end of January. The risk assessment in the updated forecast is based on the risk assessment in the November forecast.

The global economy and terms of trade

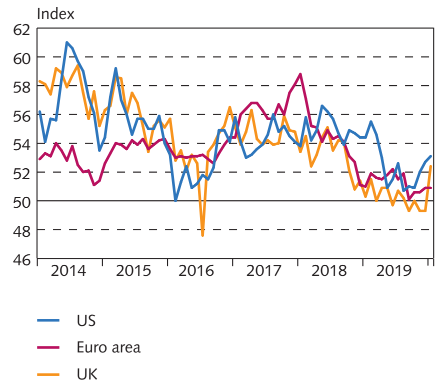
- In the US, GDP growth increased slightly in Q4/2019, as was forecast in the November *Monetary Bulletin*. In the euro area, however, growth slipped further, falling to its weakest in six years. The UK followed a similar pattern, with PMIs indicating a contraction between Q3 and Q4. The UK formally left the European Union (EU) at the end of January, but a permanent agreement outlining the trade relationship between the two parties has yet to be negotiated. The UK government aims to finalise such an agreement by the end of this year.
- Among Iceland's main trading partners, GDP growth is estimated to have measured 1.7% in 2019, its lowest in six years. Growth lost pace in nearly all trading partner economies, with the most pronounced slowdown in the eurozone, the US, and Sweden. Nevertheless, trading partner growth for the year turned out stronger than the 1.5% forecast in the November *Monetary Bulletin*.
- As before, leading indicators and international forecasts suggest that trading partners' output growth will be weak in the coming term. Despite rising concerns about the impact of a new virus originating in China, global uncertainty has receded since November and the risk of a further softening of global GDP growth has eased. This reduced risk is due largely to the partial trade agreement between the US and China, signed in mid-January. Under the agreement, the tariff hikes scheduled for December 2019 will not be implemented, and tariffs imposed last autumn have been scaled back. The agreement also obliges China to purchase more American goods. It does not apply to the tariff hikes introduced in 2018 and H1/2019, however. As a result, tariffs on imports from China to the US are still markedly higher than before the trade dispute began.
- Trading partners' GDP growth is projected to measure 1.6% this year, broadly in line with the Bank's November forecast. As in November, growth is expected to remain around 1.6% in 2021 and 2022.
- Trading partner inflation has picked up again, concurrent with a slowdown in the year-on-year decline in oil prices and an increase in global food prices. Inflation rose in nearly all trading partner countries, measuring 1.4% in Q4/2019, largely in line with the November forecast. The global inflation outlook has changed little since November. Among Iceland's main trading partners, inflation is projected to average 1.6% this year and rise to 1.8% by 2022.
- The US Federal Reserve has kept interest rates unchanged at its last two meetings, after lowering them three times in 2019. The Fed has signalled as well that it would hold rates steady in 2020. The European Central Bank (ECB) has also kept its key interest rate unchanged, as have central banks in most other advanced economies. Sweden's Riksbank, however, raised its key rate by

Chart 1
Global GDP growth[1]
Q1/2010 - Q4/2019



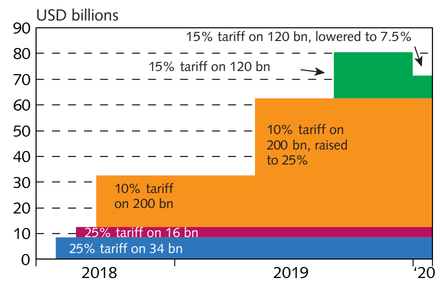
1. Central Bank baseline forecast Q4/2019 for main trading partners.
Sources: Thomson Reuters, Central Bank of Iceland.

Chart 2
Composite PMI[1]
January 2014 - January 2020



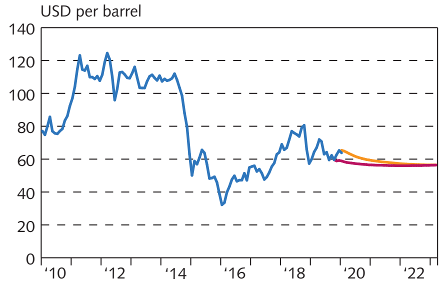
1. Markit composite output purchasing managers' index. The index is published monthly and is seasonally adjusted. An index value above 50 indicates month-on-month growth, and a value below 50 indicates a contraction.
Source: Thomson Reuters.

Chart 3
US tariffs on China[1]
June 2018 - January 2020



1. New US tariffs on goods imported from China. The amounts in the chart refer to the import value of goods affected by the tariffs.
Source: Office of the US Trade Representative.

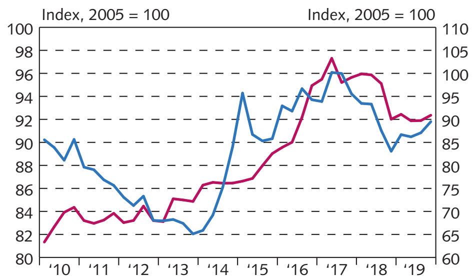
Chart 4
Global oil prices[1]
January 2010 - March 2023



Brent crude prices
Futures MB 2019/4
Futures MB 2020/1

1. Brent crude prices based on data through January 2020.
Sources: Thomson Reuters, Central Bank of Iceland.

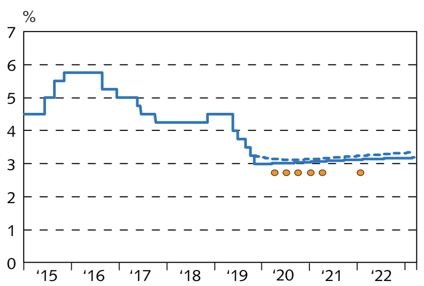
Chart 5
Terms of trade and real exchange rate[1]
Q1/2010 - Q4/2019



Terms of trade (left)
Real exchange rate (right)

1. Real exchange rate in terms of relative consumer prices. Q4/2019 terms of trade based on Central Bank baseline forecast.
Sources: Statistics Iceland, Central Bank of Iceland.

Chart 6
Central Bank of Iceland key interest rate and expected developments[1]
1 January 2015 - 31 March 2023



CBI key interest rate (seven-day term deposit rate)
Market agents' expectations[2]

1. The Central Bank's key interest rate and Treasury bond yields were used to estimate the yield curve. Broken lines show forward market interest rates prior to MB 2019/4. 2. Estimated from the median response in the Central Bank's survey of market agents' expectations concerning the collateralised lending rate. The survey was carried out during the period 20-22 January 2020.
Source: Central Bank of Iceland.

0.25 percentage points, to 0%, although it has signalled that no further rate hikes are planned for the next few years.

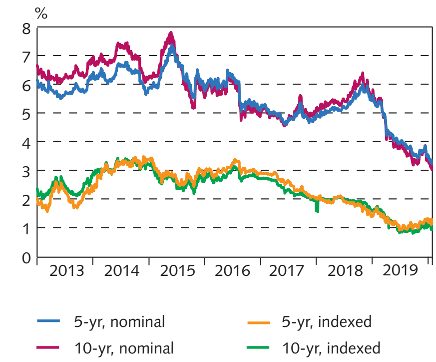
- Receding uncertainty about the global economy is reflected in developments in global financial markets. Although global equity prices declined somewhat at the end of January, owing to mounting concerns about the new coronavirus in China, they have risen since last autumn. Long-term interest rates in major advanced economies have also risen somewhat and corporate bond spreads have narrowed.
- After having held relatively stable in November, global oil prices rose in December, following the decision by OPEC and other oil-producing countries to slash production. Prices also rose following news of developments in the US-China trade dispute. They climbed still further early in 2020, due to growing tension between the US and Iran, although that uptick proved short-lived. Prices fell in late January, however, spurred by fears that the coronavirus outbreak will weaken demand for oil. Oil prices averaged 64 US dollars per barrel in January, and the outlook is for a decline of about 3½% between the 2019 and 2020 averages. Oil futures suggest that prices will be just under 60 dollars per barrel in the next few years. This is similar to the assumption underlying the November forecast.
- Global aluminium prices rose marginally in late 2019, after a nearly continuous slide lasting most of the year. They are now expected to be about 3% higher this year than in 2019 instead of remaining unchanged, as was forecast in November. Prices of marine products and non-oil commodities have risen in line with the November forecast, and the outlook is broadly unchanged.
- Terms of trade for goods and services are estimated to have deteriorated slightly more in 2019 than was forecast in November, owing mainly to a larger-than-expected increase in imported goods prices. As in November, terms of trade are expected to improve by over 2% this year, and the outlook for 2021 and 2022 is more or less unchanged.
- The real exchange rate in terms of relative consumer prices was broadly stable in 2019, after having fallen markedly in Q4/2018. The average was down 6.7% year-on-year in 2019, broadly as was forecast in November. The real exchange rate is expected to fall marginally this year and in 2021, to nearly 2% below the November forecast by the end of the forecast horizon.

Monetary policy and domestic financial markets

- The Central Bank Monetary Policy Committee (MPC) decided at its November meeting to lower the Bank's key interest rate by 0.25 percentage points, to 3%, but kept it unchanged in December. The key rate has therefore fallen by 1.5 percentage points since May 2019, although the decline in the real rate is less pronounced. The real rate in terms of the average of various measures of inflation and one-year inflation expectations is now 0.7% and has fallen by about 0.3 percentage points since May 2019. It has changed very little since November, but in terms of current twelve-month inflation it has risen by 0.8 percentage points, to 1.3%.

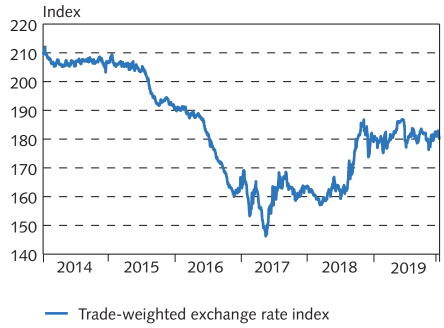
- According to the Central Bank's late-January survey, market agents expect the Bank's key rate to be lowered by a further 0.25 percentage points this quarter and then remain unchanged at 2.75% for the next two years. Forward interest rates suggest, however, that market agents believe the monetary easing cycle has come to an end.
- Yields on nominal ten-year Treasury bonds are currently 3% and have fallen by 0.2 percentage points since just before the November *Monetary Bulletin*. Shorter bond yields have developed in a similar manner, and as before, the yield curve is more or less flat. At the same time, yields on indexed ten-year Treasury bonds have risen slightly, to 0.9%.
- The interest rate differential versus Iceland's main trading partners narrowed significantly in 2019, alongside the decline in domestic interest rates, but has been broadly unchanged since November. Risk premia on Treasury foreign obligations have also changed very little.
- Capital inflows for new investment were limited in the final months of 2019, after a surge in inflows for investment in equity securities in H1. Outflows were also limited in Q4.
- The króna was relatively stable last year, after depreciating in autumn 2018, and is now at a level similar to that seen just before the November *Monetary Bulletin*. Turnover in the foreign exchange market totalled 188 b.kr. in 2019, about the same as in 2018 but much less than in the previous years. By and large, the commercial banks have been successful in pairing buyers and sellers internally and have not needed to go to the foreign exchange market. As a result, market turnover has been limited in comparison with the scope of external trade. The Central Bank has not intervened in the foreign exchange market since September 2019.
- In Q4/2019, the trade-weighted exchange rate index averaged just under 181 points; therefore, the króna was 0.5% weaker than according to the November forecast. The Bank's baseline forecast assumes that the exchange rate index will average just under 183 points this year and that the króna will depreciate slightly in 2021. It is projected to be about 1½% weaker than in the November forecast by the end of the forecast horizon.
- Year-on-year growth in broad money (M3) eased over the course of last year, from 8% in Q1/2019 to 4.3% in Q4. Growth in household deposits has begun to lose pace after several strong years, as has growth in corporate deposits.

Chart 7
Government-guaranteed bond yields[1]
2 January 2013 - 31 January 2020



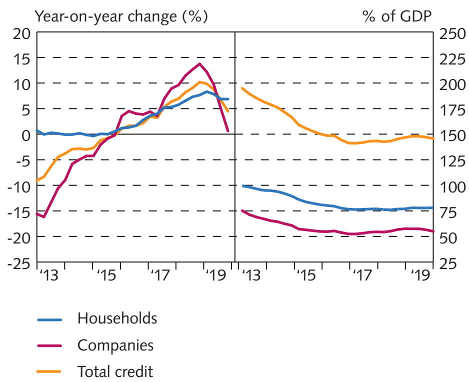
1. Based on the zero-coupon yield curve, estimated with the Nelson-Siegel method, using money market interest rates and Government-guaranteed bonds.
Source: Central Bank of Iceland.

Chart 8
Exchange rate of the króna[1]
2 January 2014 - 31 January 2020



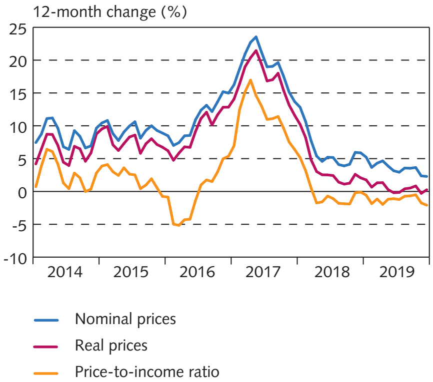
1. Price of foreign currency in krónur (narrow trade index).
Source: Central Bank of Iceland.

Chart 9
Credit system lending[1]
Q1/2013 - Q4/2019



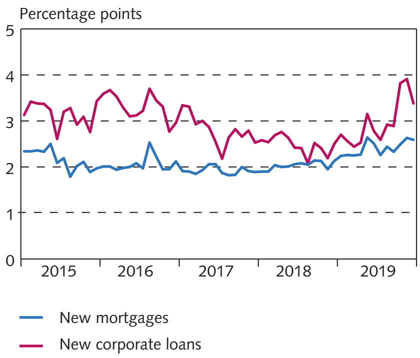
1. Credit stock adjusted for reclassification and effect of Government debt relief measures. Excluding loans to deposit institutions, failed financial institutions, and the public sector. Companies include non-financial companies and non-profit institutions serving households. Q4/2019 figures are Central Bank estimates.
Sources: Statistics Iceland, Central Bank of Iceland.

Chart 10
Capital area house prices
January 2014 - December 2019



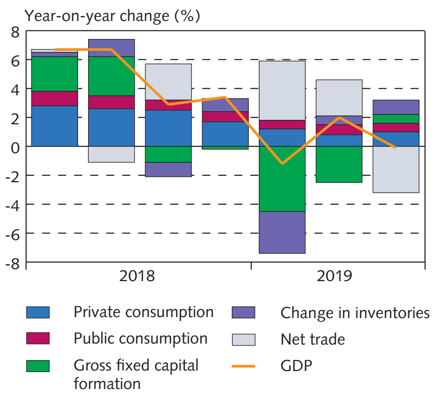
Sources: Statistics Iceland, Registers Iceland.

Chart 11
Interest rate spreads on lending[1]
January 2015 - December 2019



1. The difference between a weighted average of the large commercial banks' non-indexed lending rates and the Central Bank's key rate. The most recent figures are preliminary.
Source: Central Bank of Iceland.

Chart 12
GDP growth and contribution of underlying components[1]
Q1/2018 - Q3/2019



1. Because of chain-volume linking, the sum of contributions from components may not equal GDP growth.
Sources: Statistics Iceland, Central Bank of Iceland.

- Credit system lending growth began to taper off over the course of 2019. Year-on-year credit growth in Q4/2019 is estimated at 4.5%, down from 10% at the beginning of the year. Household lending increased by nearly 7% year-on-year in Q4, slightly less than at the beginning of 2019.

- The slowdown in corporate lending growth has been more pronounced. Loans to corporate borrowers increased by only 0.6% year-on-year in Q4/2019, down from the peak of 13.7% in late 2018. Loans to services firms and companies in retail and wholesale trade have contracted, whereas lending to the construction sector remains broadly unchanged. There are signs, however, that institutional investment funds' share in lending has begun to increase. These funds' stock of corporate loans grew by 20½ b.kr. in 2019, compared to just under 12 b.kr. for the entire credit system over the same period. To some extent, slower credit growth reflects weaker growth in economic activity, but in addition to this, one of the commercial banks has announced that it is slimming down its corporate loan portfolio.

- Capital area house prices rose by 2.4% year-on-year in December and rent prices by 4.3%. The year-on-year rise in house prices has eased almost uninterrupted since May 2017, and in December, real prices were broadly unchanged between years. Real estate market activity has declined, with purchase agreements down 4.6% year-on-year in 2019 and contracts for new construction down 2.9%. Furthermore, the average time-to-sale in the greater Reykjavík area has lengthened slightly in the recent term, to 2.6 months in December.

- Share prices increased steeply in 2019, with the OMXI10 index rising nearly one-third over the course of the year, and turnover was up 23% between years. The surge in share prices started to ease late in the year, however, and the Main List is up 0.7% since the November *Monetary Bulletin*.

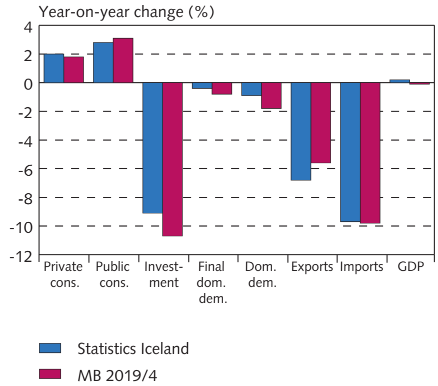
- Non-performing loan ratios contracted slightly in 2019, and the number of households and businesses on the default register has fallen. The number of corporate insolvencies also fell between years in 2019.

- Household mortgage rates have fallen broadly in line with the decline in the Bank's policy rate, although there are signs that interest rate spreads against the Bank's policy rate began to rise towards the end of 2019. Furthermore, several pension funds have tightened their lending rules in recent months. After a decline last summer, interest rates on the commercial banks' new corporate loans began to rise again, and spreads vis-à-vis the policy rate widened late in the year. In part, wider spreads probably reflect a revaluation of risk at a time when corporate lending has slowed significantly, owing to changes in domestic activity and the supply of corporate loans.

Demand and GDP growth

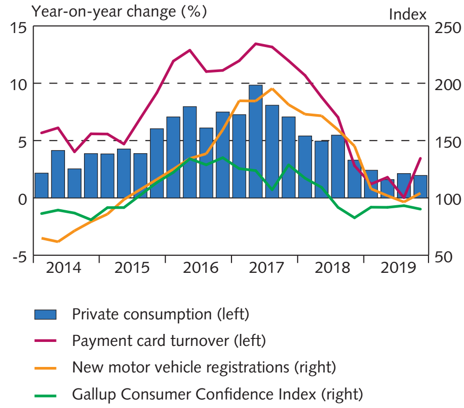
- According to preliminary figures published by Statistics Iceland, GDP contracted by 0.1% year-on-year in Q3/2019. This reflects the offsetting impact of 3.2% growth in domestic demand and a commensurably negative contribution from net trade. Statistics Iceland also published revised figures for H1, which indicate that GDP grew by 0.4% during the half instead of 0.9%, as previous figures had indicated. GDP growth for the first three quarters therefore measured 0.2%, as a positive contribution from net trade offset a 0.9% contraction in domestic demand.
- The Bank's November forecast assumed a contraction of 0.1% for the first three quarters; therefore, GDP growth measured 0.3 percentage points stronger than expected. Domestic demand contracted less, owing to stronger-than-expected growth in residential investment and a more favourable contribution from inventories. This was offset by less favourable external trade, which is attributable in large part to intellectual property-related services exports in the pharmaceuticals industry, which were expected to show in Q3 but are now likely to show up in the Q4 figures.
- Private consumption increased by 2.1% year-on-year in Q3, somewhat outpacing the November forecast. On the other hand, H1 private consumption was revised downwards, and growth in the first three quarters combined was therefore broadly in line with the November forecast. Key indicators of private consumption developed more positively in Q4 than they did earlier in the year; for example, payment card turnover grew by almost 6% year-on-year in December. As a result, private consumption growth for Q4 is projected at 2%, or 0.5 percentage points above the November forecast. If this forecast materialises, year-2019 private consumption growth will measure 2%, as compared with the November forecast of 1.7%. Consumption growth is expected to pick up over the course of the forecast horizon, in line with increased growth in real disposable income.
- Investment grew by nearly 3% year-on-year in Q3. Owing to a sharp contraction in H1, however, it shrank by more than 9% over the first nine months of the year. Business investment fell by just over 23%, in line with the Bank's November forecast, but public investment was somewhat weaker than projected. Offsetting this is strong investment in the construction sector, as figures from Statistics Iceland indicate that residential investment picked up even further in Q3 and grew by nearly 40% year-on-year over the first nine months as a whole. The Bank's November forecast assumed, however, that growth would slow over the course of the year, in line with indicators from the construction sector. This strong growth in residential investment according to Statistics Iceland figures weighs heavily in the updated forecast of developments in 2019 as a whole: total investment is now estimated to have contracted by 6.9% instead of the 8.4% projected in November. The forecast for 2020 has deteriorated,

Chart 13
National accounts Q1/2019 - Q3/2019



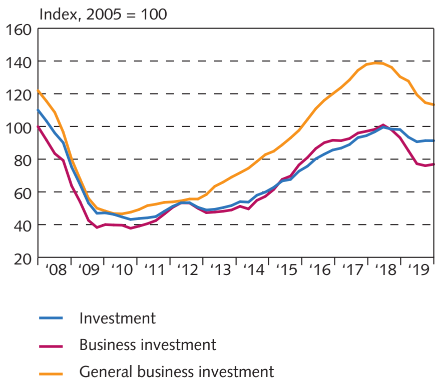
Sources: Statistics Iceland, Central Bank of Iceland.

Chart 14
Private consumption and its indicators[1]
Q1/2014 - Q4/2019



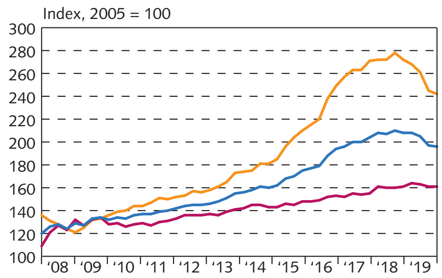
1. Private consumption and payment card turnover are year-on-year changes, while the figure for new motor vehicle registrations is a seasonally adjusted index with a mean of 100. New motor vehicle registrations net of car rental agencies' applications for new registrations in each quarter, with Q4/2019 figures based on data for October and November. Central Bank baseline forecast Q4/2019 for private consumption.
Sources: Gallup, Statistics Iceland, Central Bank of Iceland.

Chart 15
Investment[1]
Q1/2008 - Q4/2019



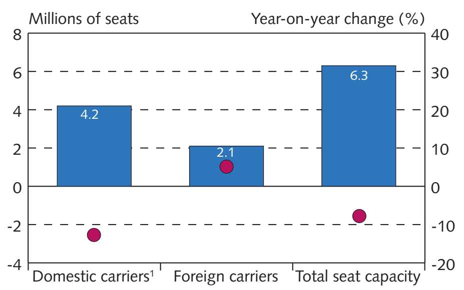
1. Four-quarter moving average. General business investment excluding energy-intensive industry, ships, and aircraft. Central Bank baseline forecast Q4/2019.
Sources: Statistics Iceland, Central Bank of Iceland.

Chart 16
Exports of goods and services[1]
Q1/2008 - Q4/2019



1. Four-quarter moving average. Central Bank baseline forecast Q4/2019.
Sources: Statistics Iceland, Central Bank of Iceland.

Chart 17
Airline seat capacity to and from Keflavík
1 January 2020 – 30 September 2020



1. WOW Air became insolvent on 28 March 2019.
Sources: Isavia, Central Bank of Iceland.

however, not least because of a more sluggish recovery of business investment, which in turn is affected by the above-mentioned widening of corporate borrowing spreads. Investment is forecast to grow by 0.3% this year, significantly below the 7.4% increase projected in November. The outlook for 2021 and 2022 has also deteriorated.

- The National Budget for 2020 was passed with a deficit equalling 0.3% of GDP, the first deficit budget passed since 2013. The deficit is 0.3 percentage points larger than was assumed in the November forecast, which was based on the 2020 fiscal budget proposal introduced in September 2019 and the fiscal plan approved by Parliament the previous spring. Primary expenditures increase by just under 0.1% of GDP relative to the 2019 National Budget, while the decline in primary income measures nearly 1.4% of GDP.

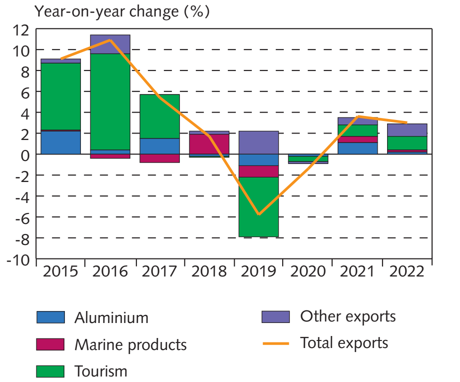
- Public consumption grew by 2.8% year-on-year in the first three quarters of 2019, and public investment contracted by 6%. Public consumption and investment expenditures are estimated to have increased by a combined 4.1% in 2019, after adjusting for the transfer of the Hvalfjarðargöng tunnel from private to public ownership. The growth rate is similar to that in 2018 but slightly below the November forecast. The outlook for the forecast horizon overall is broadly unchanged, however.

- Goods and services exports contracted by 6.8% year-on-year in the first three quarters of 2019, owing mainly to the contraction in tourism, although exports of aluminium and marine products declined as well. Production difficulties in the aluminium industry have turned out more protracted than previously anticipated, and poorer fish catches caused marine product exports to contract more than expected. Preliminary figures show that goods exports grew more slowly than projected in Q4, although this was offset in part by a smaller-than-expected decrease in tourist arrivals. As a consequence, goods and services exports are projected to have contracted by 5.8% in 2019 as a whole, as was forecast in November.

- The outlook for services exports in 2020 has deteriorated since November. Airline seat capacity to and from Iceland looks set to decline markedly, and tourist arrivals are expected to increase less than was forecast in November. According to Isavia's recently published flight schedule for Keflavík Airport, the outlook is for a contraction in air transport in 2020. This reflects the impact of WOW Air's insolvency in late March 2019, as well as the grounding of Icelandair's Boeing Max jets, which were to account for over one-third of the airline's fleet this year. Seat capacity on flights to and from Keflavík Airport is projected to decline by 8% year-on-year in the first three quarters of 2020. The decline is offset by increased offerings from foreign airlines. Seat capacity to North America is scheduled to decline by a fifth, and the number of transit passengers is therefore expected to drop markedly for the second year in a row.

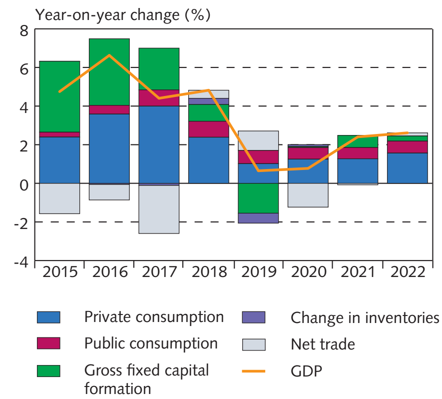
- The outlook for goods exports has also worsened, as it is now expected that aluminium smelters will not return to full capacity until 2021; furthermore, marine product exports are projected to be weaker than was forecast in November. A major factor in marine product exports is the prospect of a second consecutive year with no capelin quota issued. Based on issued quotas for other pelagic species and haddock, marine product exports are expected to contract by 2.6% this year, or 1.6 percentage points more than was forecast in November. On the whole, goods and services exports are projected to contract by 1.4% this year, whereas the November forecast assumed a growth rate of 0.4%. If the forecast materialises, this will be the second consecutive year to see a contraction in exports — the first time this has happened since the early 1990s. Exports are expected to begin recovering in 2021, when the aluminium smelters return to full capacity and marine production for export starts to pick up again.
- As was assumed in November, goods and services imports contracted by 9.7% in the first three quarters of 2019. However, preliminary figures from Statistics Iceland indicate a larger contraction in Q4 than was provided for in the November forecast. This is due in particular to a contraction in aluminium-related imports, as well as in imports of investment inputs and consumer durables. As a result, imports are estimated to have contracted by 8.5% in 2019, or 0.7 percentage points more than was forecast in November. Because investment is expected to slow down this year and export sector activity to decline, the outlook is for imports to increase by only 1.5% in 2020 – a marked decline from the November forecast. The outlook for the next two years is broadly unchanged, however.
- Because of a stronger contraction in imports in 2019 and 2020, the outlook is for the contribution from net trade to GDP growth to be somewhat stronger over the period than was forecast in November. The surplus on combined goods and services trade will increase commensurably. The trade surplus for 2019 is now estimated at 3.7% of GDP, and the surplus for the forecast horizon as a whole is projected at 3½%, nearly 1 percentage point above the November forecast. By the same token, the current account surplus is expected to narrow from 4.7% of GDP in 2019 to 3.8% of GDP in 2020.
- Consumption and investment spending is assumed to have increased by 1.8% in Q4/2019, but because of a negative contribution from inventories during the quarter, the increase in domestic demand is assumed to have been smaller, or 1%. Added to this is a positive contribution from net trade, which can be traced in part to the aforementioned transfer of intellectual property exports from Q3 to Q4. As a consequence, GDP growth appears to have been stronger in Q4 than was forecast in November, in addition to having been stronger in the first three quarters of the year. GDP is therefore projected to have grown by 0.6% in 2019 instead of contracting by 0.2%. The outlook for 2020 has deteriorated, however, and GDP growth is now projected at only 0.8%,

Chart 18
Exports and contribution of subcomponents 2015-2022[1]



1. Because of chain-volume linking, the sum of components may not equal total exports. Aluminium exports as defined in the national accounts. Tourism is the sum of "travel" and "passenger transport by air". Central Bank baseline forecast 2019-2022.
Sources: Statistics Iceland, Central Bank of Iceland.

Chart 19
GDP growth and contribution of subcomponents 2015-2022[1]

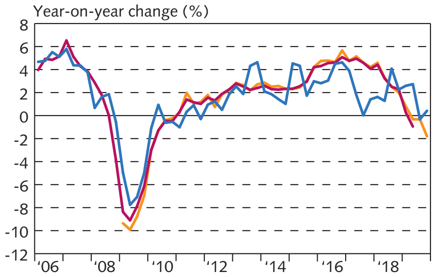


1. Central Bank baseline forecast 2019-2022.
Sources: Statistics Iceland, Central Bank of Iceland.

Chart 20

Number of employed persons[1]

Q1/2006 - Q4/2019



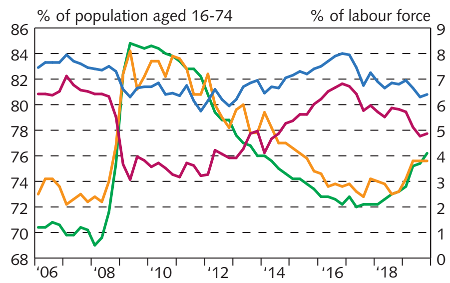
- Employed persons
- Wage-earners aged 16-74
- All wage-earners

1. Employed persons according to Statistics Iceland's labour force survey and wage-earners according to the Directorate of Internal Revenue's PAYE register. Wage-earners aged 16-74 includes individuals on childbirth leave and self-employed persons. All wage-earners excludes these groups but covers all age groups and bases the Q4/2019 figure on October values.
Sources: Statistics Iceland, Central Bank of Iceland.

Chart 21

Unemployment, employment, and labour participation[1]

Q1/2006 - Q4/2019



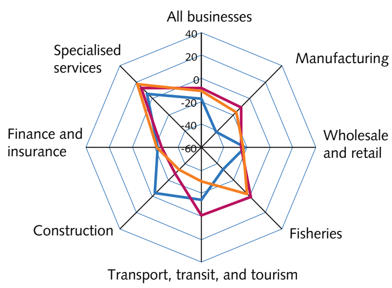
- Participation rate (left)
- Employment rate (left)
- Unemployment rate (right)
- Registered unemployment rate (right)

1. Seasonally adjusted figures. The registered unemployment rate is seasonally adjusted by the Central Bank.
Sources: Directorate of labour, Statistics Iceland, Central Bank of Iceland.

Chart 22

Firms planning recruitment net of firms planning redundancies within 6 months[1]

Share of businesses (%)



- December 2018
- September 2019
- December 2019

1. Seasonally adjusted figures.
Sources: Gallup, Central Bank of Iceland.

well below the November forecast of 1.6%. As is discussed above, the main factors in the revised projection are the poorer outlook for exports and the negative effects of rising corporate borrowing spreads on investment. Widening spreads will also affect the outlook for 2021 output growth, which is now estimated at 2.4%, some 0.5 percentage points below the November forecast.

Labour market and factor utilisation

- According to the Statistics Iceland labour force survey (LFS), total hours worked increased by 1.2% year-on-year in Q4/2019. However, the November forecast assumed that total hours would decline, as the year-on-year increase had slowed from Q3/2018 onwards, and there was no change between then and Q3/2019. The rise in total hours is due to a 0.4% increase in the number of employed persons and a 0.8% lengthening of the average work week. Data from the pay-as-you-earn (PAYE) register give a different impression, however. According to PAYE data, job numbers began to decline between years in Q2/2019 and, by October, were down 1.8% year-on-year.
- According to seasonally adjusted LFS figures, the labour participation rate rose and the employment rate increased marginally between Q3 and Q4/2019. Seasonally adjusted unemployment was therefore unchanged between quarters, measuring 3.8% in Q4. Registered unemployment rose by 0.4 percentage points over the same period, however, to a seasonally adjusted 4.1%. The year-on-year increase measured 1.6 percentage points, with the number of unemployed persons rising most in tourism-related sectors, construction, retail and wholesale trade, and industry and raw materials processing. The share of foreign workers is high in most of these sectors, and according to estimates from the Directorate of Labour, unemployment among foreign nationals rose by 3.8 percentage points during the period. In late 2019, two of every five individuals on the unemployment register were foreign nationals, compared to one in five in late 2014.
- Although unemployment among foreign nationals has risen, inward migration has slowed only marginally. In Q4/2019, year-on-year population growth measured 2%, including 1.4 percentage points due to immigration of foreign nationals. Growth in the foreign population is therefore still close to the level in the first half of 2017, the year that saw the largest single-year increase recorded to date. The number of active employees of employment agencies and foreign services firms has fallen, however. There were almost 950 such workers at the end of 2019, or about 300 fewer than at the end of Q3. This group is now at its smallest since mid-2016. The number of temporary work permits also fell slightly in 2019.
- According to the seasonally adjusted results of the Gallup survey carried out this winter among Iceland's 400 largest firms, the balance of opinion on staffing plans (i.e., firms planning to recruit as

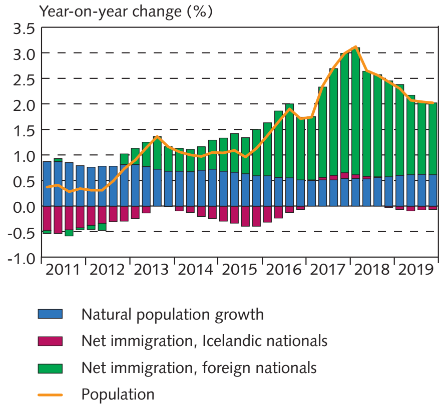
compared with those planning redundancies) was negative by 11 percentage points. The number of executives planning redundancies has risen slightly since last autumn, when the balance of opinion was negative by 7 percentage points. Prospects are bleakest in the construction sector, where the outlook is for a marked drop in job numbers in the coming term, and once again there is considerable pessimism in the transport, transit, and tourism sector. The only sector expecting an increase in staffing levels is miscellaneous specialised services, where the balance of opinion was positive by 18 percentage points. In this sector, which includes education and miscellaneous public institutions, the balance of opinion improved by 5 percentage points between surveys. As is discussed in the last *Monetary Bulletin*, job numbers in public services have risen steeply, partially offsetting the decline in most other sectors. The results of the winter survey therefore indicate that this trend will continue in H1/2020.

- After adjusting for seasonality, 16% of executives who responded to Gallup's winter survey considered themselves short-staffed. This is similar to the share reporting staff shortages in the autumn survey and therefore somewhat below the historical average. At the same time, the share of executives who reported that their firms would have difficulty responding to unexpected demand fell from 40% to 36%. On the whole, capacity pressures appear greatest in miscellaneous specialised services, while they are least pronounced in construction and utilities, finance and insurance, and transport, transit, and tourism. The resource utilisation (RU) indicator, which combines various indicators of factor utilisation, fell slightly in Q4/2019, after having risen over the course of the year.
- Total hours worked are forecast to increase by 0.7% this year and by an average of 1¾% per year in 2021 and 2022. Unemployment is projected to average 4.2% this year, 0.4 percentage points above the November forecast. It is also forecast to average over 4% in 2021 before tapering off gradually as the forecast horizon advances. Although the output gap is estimated to have been larger in 2019 than was forecast in November, the slack that opens up this year is expected to be more persistent than was anticipated then.

Inflation

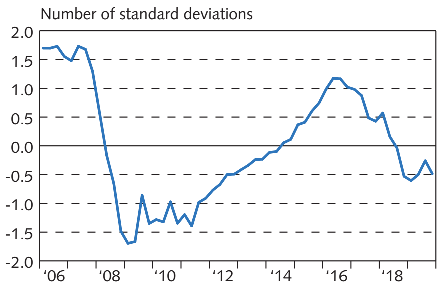
- Headline inflation has subsided rapidly in recent months. It measured 2.5% in Q4/2019, in line with the forecast in the November *Monetary Bulletin*. House price inflation slowed in the first three quarters of 2019. Even so, the housing component was the major determinant of developments in the CPI in Q4, mainly because of price hikes in regional Iceland. Price increases for various imported goods, particularly furniture and housewares, also made an impact.
- The CPI declined by 0.74% month-on-month in January, and twelve-month inflation measured 1.7%. Inflation has been below

Chart 23
Population
Q1/2011 - Q4/2019



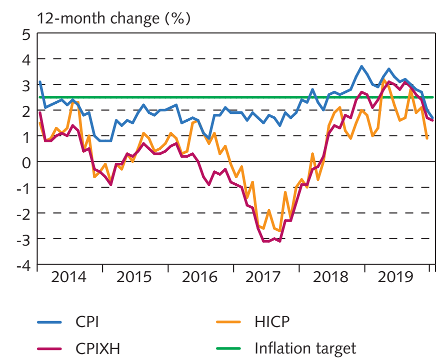
Source: Statistics Iceland.

Chart 24
RU indicator[1]
Q1/2006 - Q4/2019



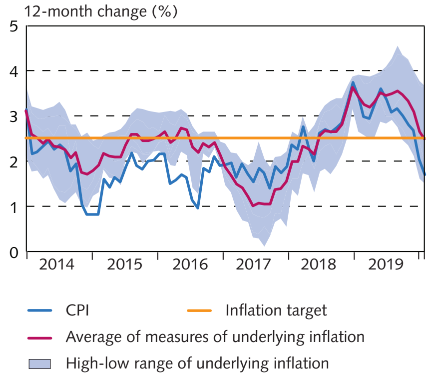
1. The resource utilisation (RU) indicator is the first principal component of selected indicators of factor utilisation; it is scaled so that its mean value is 0 and the standard deviation is 1. A more detailed description can be found in Box 3 in MB 2018/2.
Source: Central Bank of Iceland.

Chart 25
Various measures of inflation
January 2014 - January 2020



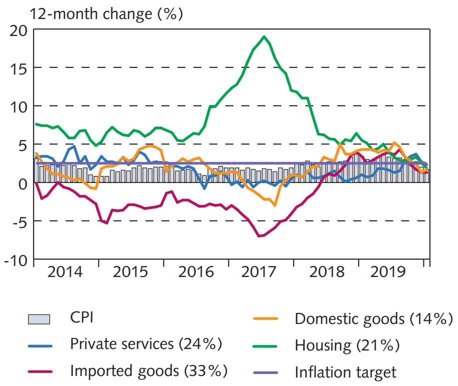
Sources: Statistics Iceland, Central Bank of Iceland.

Chart 26
Headline and underlying inflation[1]
January 2014 - January 2020



1. Underlying inflation measured using a core index (which excludes the effects of indirect taxes, volatile food items, petrol, public services, and real mortgage interest expense) and statistical measures (weighted median, trimmed mean, a dynamic factor model, and a common component of the CPI).
Sources: Statistics Iceland, Central Bank of Iceland.

Chart 27
Imported and domestic inflation[1]
January 2014 - January 2020



1. Imported inflation is estimated using the price of imported food and beverages, new motor vehicles and spare parts, petrol, and other imported goods. The figures in parentheses show the current weight of these items in the CPI.
Sources: Statistics Iceland, Central Bank of Iceland.

target since December and is now at its lowest since autumn 2017. It has fallen by just over 1 percentage point since the last *Monetary Bulletin* and by 1.7 percentage points since January 2019. Winter sales and a decline in owner-occupied housing costs were the strongest factors in January price measurements. Inflation excluding housing measured 1.6% in January and has also fallen markedly in recent months. Inflation according to the HICP, which also excludes owner-occupied housing costs, was even lower, measuring 0.9% in December. HICP inflation fell abruptly between months, in part due to base effects, as airfares, which account for a larger share in the HICP than in the CPI, rose considerably less in December 2019 than in the same month a year earlier.

- The average of various measures of underlying inflation was 2.5% in January, down by nearly 1 percentage point since January 2019. Underlying inflation headline has exceeded CPI inflation since last August. One reason for this is that some of the measures of underlying inflation exclude real mortgage interest expense, which has fallen with the decline in the Bank's policy rate and has therefore lowered inflation in the recent past. Headline twelve-month inflation is estimated to have been approximately 0.4 percentage points lower as a result.

- The contribution from imported goods to headline inflation has declined in recent months, as the króna has been relatively stable. In January, imported goods prices had risen by 1.3% in the previous twelve months, the smallest year-on-year rise since summer 2018. The year-on-year rise in domestic goods prices has also lost pace, measuring 1.7% in January, as producer prices of goods sold domestically have fallen since last autumn. Private services prices have risen by 2.3% since January 2019, and the twelve-month rise has lost momentum since last October.

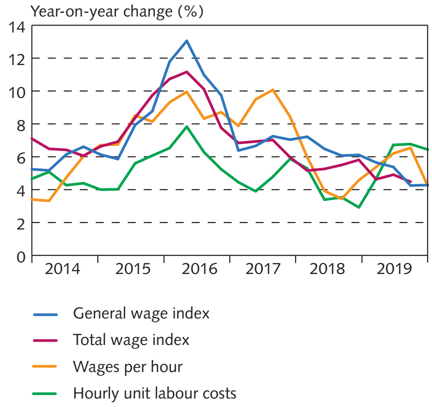
- Although the contribution of the rise in house prices to inflation has eased since October, over a fourth of headline inflation is attributable to the housing component. This is roughly equal to its weight in the CPI. The housing component rose by 1.8% year-on-year in January, as opposed to 5.5% in January 2019.

- The general wage index rose by 0.9% between quarters in Q4/2019, and by 4.3% year-on-year, in line with the November forecast. The November forecast assumed that comprehensive public sector wage agreements would be signed late in 2019, but a settlement has yet to be reached. A conclusion is expected before the end of Q1/2020, however. The wage settlements finalised between the State and selected public sector labour unions last autumn entailed more retroactivity and a more front-loaded payment schedule for 2020 than was assumed in the Bank's forecast. It is likely that the remaining public sector agreements will be along similar lines, and forecasted wage developments have been revised slightly as a result. Wages per hour are now projected to rise by 5.6% this year, or 0.6 percentage points more than according to the November forecast.

Because of base effects and the delays in the aforementioned public sector wage agreements, however, wages rose slightly less in 2019 than had been projected and are expected to rise less in 2021; therefore, wage developments over the horizon as a whole are broadly unchanged from the November forecast.

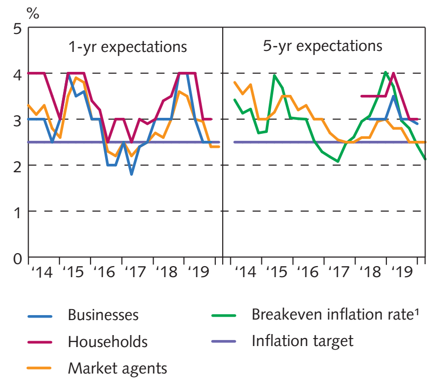
- Labour productivity is estimated to have contracted slightly in 2019, the first contraction since 2010. It is expected to remain flat this year and then increase by just under 1% per year in 2021 and 2022. Owing to larger wage hikes and weaker productivity growth, unit labour costs are expected to rise more this year than was forecast in November, or 5.4% instead of 4%. In 2021 and 2022, however, they are expected to rise less, averaging 3¾% per year instead of 4%.
- According to Gallup's winter survey, households' and businesses' one-year inflation expectations were unchanged between surveys, at 2.5-3%. Households' two-year inflation expectations fell by 0.2 percentage points, however, to 3%. The Bank's most recent market expectations survey suggests that, as in the October survey, market agents expect inflation to be at target in both one and two years' time.
- Most measures of long-term inflation expectations are also at or near the target. Market agents expect inflation to be at target, on average, in the next five and ten years, as they did in the previous survey. The five- and ten-year breakeven inflation rate has averaged 2.1% in Q1 to date, or 0.3 percentage points lower than in Q4/2019. Households' and corporate executives' long-term inflation expectations are about 3%. Executives' expectations fell marginally from the autumn survey.
- The outlook over the forecast horizon is for lower inflation than was projected in November, owing to a more pronounced and more persistent slack in the economy. Inflation is forecast at 1.9% in H1/2020, some 0.5 percentage points below the last forecast. The revision is also due to a more favourable initial position, as inflation turned out somewhat lower in December and January than was assumed in the November forecast. Inflation is expected to increase at the start of 2021 and measure 2.1% for the year as a whole, which is similar to the previous forecast. It will remain below the inflation target over the forecast horizon but will inch up to it towards the end of the period.
- The inflation outlook is subject to numerous uncertainties, and changes in important assumptions about domestic and global economic developments could cause inflation to diverge from the path presented here. As is the custom with the Bank's updated forecasts, the risk assessment of the baseline scenario is unchanged from the previous forecast. Therefore, the probability distribution of the forecast is also unchanged since November. As a result, there is a roughly 50% probability that inflation will be in the 1-3% range in one year and in the 1-3½% range by the end of the forecast horizon.

Chart 28
Different measures of wages[1]
Q1/2014 - Q4/2019



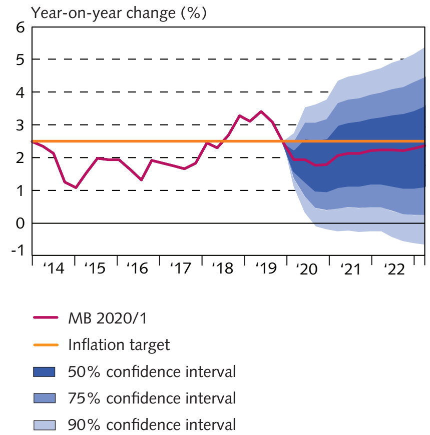
1. Wages per hour are based on annual figures for the wage portion of wages and related expenses according to the production accounts, as a share of total hours worked according to the Statistics Iceland labour force survey. Wages per hour and a four-quarter moving average for unit labour costs are based on Central Bank estimates for the year 2019.
Sources: Statistics Iceland, Central Bank of Iceland.

Chart 29
Inflation expectations
Q1/2014 - Q1/2020



1. The most recent value is the average of daily values from 2 January through 31 January 2020.
Sources: Gallup, Central Bank of Iceland.

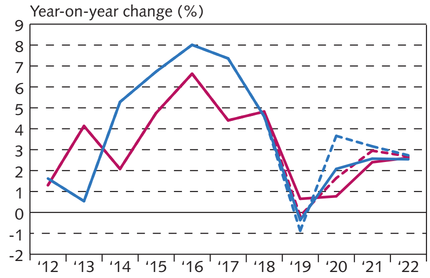
Chart 30
Inflation forecast and confidence intervals
Q1/2014 - Q1/2023



Sources: Statistics Iceland, Central Bank of Iceland.

Chart 31

Domestic demand and GDP growth 2012-2022[1]

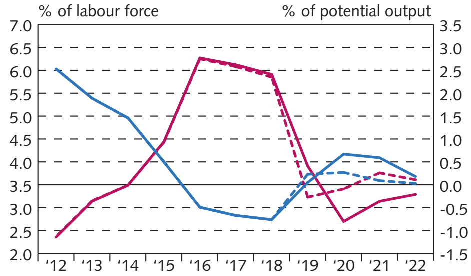


Domestic demand
GDP growth

1. Central Bank baseline forecast 2019-2022. Broken lines show forecast from MB 2019/4.
Sources: Statistics Iceland, Central Bank of Iceland.

Chart 32

Unemployment and output gap 2012-2022[1]

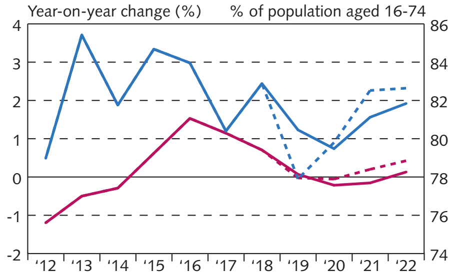


Unemployment (left)
Output gap (right)

1. Central Bank baseline forecast 2019-2022. Broken lines show forecast from MB 2019/4.
Sources: Statistics Iceland, Central Bank of Iceland.

Chart 33

Total hours worked and employment rate 2012-2022[1]

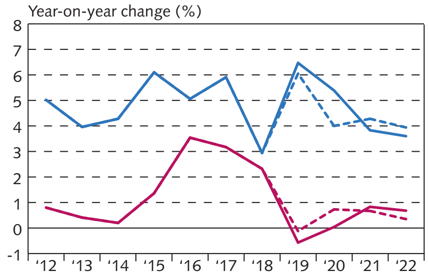


Total hours worked (left)
Employment rate (right)

1. Central Bank baseline forecast 2019-2022. Broken lines show forecast from MB 2019/4.
Sources: Statistics Iceland, Central Bank of Iceland.

Chart 34

Unit labour costs and productivity 2012-2022[1]

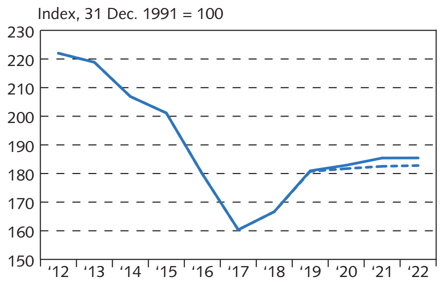


Unit labour costs
Productivity

1. Productivity measured as the ratio of GDP to total hours worked. Central Bank baseline forecast 2019-2022. Broken lines show forecast from MB 2019/4.
Sources: Statistics Iceland, Central Bank of Iceland.

Chart 35

Exchange rate 2012-2022[1]



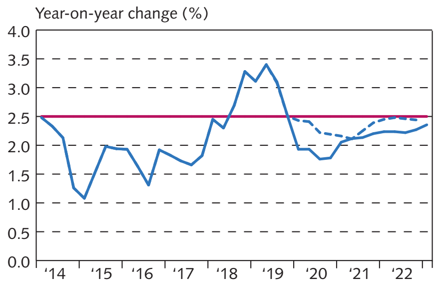
TWI

1. Narrow trade basket. Central Bank baseline forecast 2019-2022. Broken lines show forecast from MB 2019/4.
Source: Central Bank of Iceland.

Chart 36

Inflation[1]

Q1/2013 - Q1/2023



Inflation
Inflation target

1. Central Bank baseline forecast Q1/2020-Q1/2023. Broken line shows forecast from MB 2019/4.
Sources: Statistics Iceland, Central Bank of Iceland.

Appendix 1

Forecast tables

Table 1 GDP and its main components[1]

	2018	2019	2020	2021	2022
Private consumption	4.7 (4.7)	2.0 (1.7)	2.4 (2.2)	2.5 (3.3)	3.1 (2.8)
Public consumption	3.5 (3.5)	2.9 (3.2)	2.5 (2.6)	2.4 (2.4)	2.5 (2.5)
Gross capital formation	4.0 (4.0)	-6.9 (-8.4)	0.3 (7.4)	3.0 (3.6)	1.3 (2.7)
Business investment	-4.1 (-4.1)	-17.4 (-16.1)	1.2 (10.2)	-0.3 (1.2)	1.7 (3.5)
Residential investment	16.2 (16.2)	30.1 (13.0)	-4.6 (7.5)	5.3 (5.9)	4.5 (5.1)
Public investment	28.3 (28.3)	-9.7 (-3.7)	4.7 (-1.8)	10.7 (8.7)	-4.6 (-3.6)
Domestic demand	4.6 (4.6)	-0.4 (-0.9)	2.1 (3.7)	2.6 (3.2)	2.5 (2.7)
Exports of goods and services	1.7 (1.7)	-5.8 (-5.8)	-1.4 (0.4)	3.6 (3.6)	3.0 (2.8)
Imports of goods and services	0.8 (0.8)	-8.5 (-7.8)	1.5 (5.0)	4.0 (4.1)	2.8 (2.9)
Gross domestic product (GDP)	4.8 (4.8)	0.6 (-0.2)	0.8 (1.6)	2.4 (2.9)	2.6 (2.7)
GDP at current prices (ISK billions)	2,812 (2,812)	2,961 (2,929)	3,111 (3,078)	3,276 (3,268)	3,450 (3,447)
GDP at current prices (growth rate)	7.6 (7.6)	5.3 (4.1)	5.1 (5.1)	5.3 (6.2)	5.3 (5.5)
Total investment (% of GDP)	22.3 (22.3)	21.1 (20.9)	20.8 (21.8)	20.9 (21.9)	20.6 (21.9)
Business investment (% of GDP)	14.2 (14.2)	12.0 (12.2)	11.9 (12.9)	11.6 (12.7)	11.5 (12.8)
Gross national saving (% of GDP)[2]	25.5 (25.5)	25.7 (24.4)	24.6 (24.4)	24.5 (24.6)	24.3 (24.7)
Contribution of net trade to GDP growth (percentage points)	0.4 (0.4)	1.0 (0.7)	-1.2 (-1.9)	-0.1 (-0.1)	0.2 (0.0)

1. Year-on-year change (%) unless otherwise specified (figures in parentheses are from the forecast in MB 2019/4). 2. The sum of investment, inventory changes, and the current account balance.

Sources: Statistics Iceland, Central Bank of Iceland.

Table 2 Global economy, external conditions, and exports[1]

	2018	2019	2020	2021	2022
Marine production for export	11.5 (11.5)	-5.9 (-4.5)	-2.6 (-1.0)	3.0 (1.0)	1.0 (1.0)
Aluminium production for export[2]	-1.2 (-1.2)	-6.2 (-2.5)	-1.0 (4.0)	7.0 (1.0)	1.0 (1.0)
Foreign currency prices of marine products	4.7 (4.7)	6.6 (7.0)	3.0 (3.0)	3.0 (3.0)	1.5 (1.5)
Aluminium prices in USD[3]	13.3 (13.3)	-13.1 (-13.0)	3.0 (0.0)	4.0 (4.0)	4.0 (4.0)
Fuel prices in USD[4]	30.4 (30.4)	-10.3 (-11.5)	-3.3 (-9.2)	-6.2 (-2.1)	-2.4 (-0.2)
Terms of trade for goods and services	-3.6 (-3.6)	-0.8 (-0.4)	2.1 (2.2)	0.5 (0.7)	0.2 (0.2)
Inflation in main trading partners[5]	2.0 (2.0)	1.5 (1.5)	1.6 (1.6)	1.7 (1.7)	1.8 (1.8)
GDP growth in main trading partners[5]	2.3 (2.2)	1.7 (1.5)	1.6 (1.5)	1.6 (1.6)	1.6 (1.6)
Main trading partners' imports[5]	2.8 (3.0)	2.2 (1.9)	2.3 (2.8)	2.7 (3.2)	2.7 (3.0)
Policy rates in main trading partners (%)[6]	0.5 (0.5)	0.6 (0.6)	0.5 (0.5)	0.5 (0.5)	0.7 (0.6)

1. Year-on-year change (%) unless otherwise specified (figures in parentheses are from the forecast in MB 2019/4). 2. According to Statistics Iceland's external trade data. 3. Forecast based on aluminium futures and analysts' forecasts. 4. Based on average price of Brent crude oil futures during the period 16-22 January 2020. 5. Forecast based on Consensus Forecast, Global Insight, IMF, and OECD. 6. Forecast based on overnight index swap rates in main trading partner countries during the period 20 December 2019 - 8 January 2020.

Sources: Bloomberg, Consensus Forecasts, Global Insight, IMF, New York Mercantile Exchange, OECD, Statistics Iceland, Thomson Reuters, Central Bank of Iceland.

Table 3 Current account balance and its subcomponents[1]

	2018	2019	2020	2021	2022
Trade balance	3.0 (3.0)	3.7 (3.6)	3.3 (2.6)	3.4 (2.7)	3.6 (2.7)
Balance on primary income[2]	-0.2 (-0.2)	1.0 (0.2)	0.4 (0.0)	0.2 (0.0)	0.1 (0.1)
Current account balance	2.8 (2.8)	4.7 (3.7)	3.8 (2.6)	3.6 (2.7)	3.6 (2.8)

1. % of GDP (figures in parentheses are from the forecast in MB 2019/4). 2. The sum of primary and secondary income.

Sources: Statistics Iceland, Central Bank of Iceland.

Table 4 Labour market and factor utilisation[1]

	2018	2019	2020	2021	2022
Unemployment (% of labour force)	2.7 (2.7)	3.6 (3.7)	4.2 (3.8)	4.1 (3.6)	3.7 (3.5)
Employment rate (% of population aged 16-74)	79.4 (79.4)	78.1 (78.0)	77.6 (77.9)	77.7 (78.4)	78.3 (78.8)
Total hours worked	2.4 (2.4)	1.2 (-0.1)	0.7 (0.9)	1.6 (2.3)	1.9 (2.3)
Labour productivity[2]	2.3 (2.3)	-0.6 (-0.1)	0.0 (0.7)	0.8 (0.7)	0.7 (0.4)
Unit labour costs[3]	2.9 (2.9)	6.5 (6.1)	5.4 (4.0)	3.8 (4.3)	3.6 (3.9)
Wage share (% of gross factor income)	63.7 (63.7)	64.8 (64.7)	65.5 (65.1)	66.1 (65.8)	66.7 (66.6)
Real disposable income	4.5 (4.5)	2.6 (2.6)	2.8 (2.5)	3.4 (4.0)	4.0 (4.1)
Output gap (% of potential output)	2.4 (2.3)	0.4 (-0.3)	-0.8 (-0.1)	-0.4 (0.3)	-0.2 (0.1)

1. Year-on-year change (%) unless otherwise specified (figures in parentheses are from the forecast in MB 2019/4). 2. GDP per total hours worked. 3. Wage costs divided by productivity.

Sources: Statistics Iceland, Central Bank of Iceland.

Table 5 Exchange rate and inflation[1]

	2018	2019	2020	2021	2022
Trade-weighted exchange rate index[2]	166.7 (166.7)	181.0 (180.7)	182.9 (181.7)	185.4 (182.5)	185.4 (182.8)
Real exchange rate (relative consumer prices)[3]	96.8 (96.8)	90.4 (90.4)	90.1 (90.6)	89.1 (90.7)	89.5 (91.1)
Real exchange rate (relative unit labour costs)[3]	98.0 (97.8)	93.7 (93.4)	96.0 (94.8)	96.5 (96.3)	97.6 (97.4)
Inflation (consumer price index, CPI)	2.7 (2.7)	3.0 (3.0)	1.9 (2.3)	2.1 (2.2)	2.2 (2.5)
Inflation (CPI excluding effects of indirect taxes)	2.6 (2.6)	2.9 (2.9)	1.8 (2.2)	2.1 (2.2)	2.2 (2.4)

1. Year-on-year change (%) unless otherwise specified (figures in parentheses are from the forecast in MB 2019/4). 2. Narrow trade-weighted basket. The index has been recalculated so that on 2 January 2009 it was assigned a value equivalent to that of the now-discontinued Exchange Rate Index. 3. Average 2005 = 100.

Sources: Statistics Iceland, Central Bank of Iceland.

Table 6 Quarterly inflation forecast (%)[1]

Quarter	Inflation (year-on-year change)	Inflation excluding effects of indirect taxes (year-on-year change)	Inflation (annualised quarter-on-quarter change)
		Measured value	
2019:1	3.1 (3.1)	3.0 (3.0)	1.9 (1.9)
2019:2	3.4 (3.4)	3.3 (3.3)	4.3 (4.3)
2019:3	3.1 (3.1)	3.0 (3.0)	1.3 (1.3)
2019:4	2.5 (2.5)	2.4 (2.4)	2.5 (2.6)
		Forecasted value	
2020:1	1.9 (2.4)	1.8 (2.3)	-0.4 (1.6)
2020:2	1.9 (2.4)	1.8 (2.3)	4.3 (4.2)
2020:3	1.8 (2.2)	1.7 (2.1)	0.6 (0.6)
2020:4	1.8 (2.2)	1.7 (2.1)	2.6 (2.4)
2021:1	2.1 (2.2)	2.1 (2.1)	0.7 (1.5)
2021:2	2.1 (2.1)	2.1 (2.0)	4.5 (4.0)
2021:3	2.1 (2.2)	2.1 (2.2)	0.7 (1.1)
2021:4	2.2 (2.4)	2.1 (2.3)	2.9 (3.0)
2022:1	2.2 (2.4)	2.2 (2.4)	0.9 (1.7)
2022:2	2.2 (2.5)	2.2 (2.4)	4.5 (4.1)
2022:3	2.2 (2.5)	2.1 (2.4)	0.6 (1.1)
2022:4	2.3 (2.4)	2.2 (2.4)	3.1 (2.9)
2023:1	2.4	2.4	1.2

1. Figures in parentheses are from the forecast in MB 2019/4.

Sources: Statistics Iceland, Central Bank of Iceland.