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The Structure of the Retail Sector in Iceland

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Biography of the author

Professor Einarsson is the former dean of the Faculty of Economics and Business Administration at the University of Iceland. He obtained his PhD in Germany. He is the author of 6 books on microeconomics, business administration and cultural economics and over 50 journal articles and conference papers and over 400 shorter articles on economics, fisheries and politics in magazines, newspapers, and on websites. Professor Einarsson is a former Member of the Icelandic Parliament and Chairman of the Board of the Central Bank of Iceland and served as a delegate for Iceland at the General Assembly of the United Nations in New York.

Abstract

The paper discusses the structure of the retail sector in Iceland. Although there was considerable trade in Iceland in the first century of settlement, retailing did not become a significant economic sector until the 20th century, at a time when the Icelandic economy was undergoing extensive transformation. A relatively small number of retail chains dominate most of the market at the current time, but competition is nevertheless quite active, even though the distance of the country from other countries makes foreign competition difficult. The retail sector is now a prominent feature of the Icelandic economy, and the contribution of the retail sector to Gross Domestic Product is discussed in the paper, as well as its role in the labour market. Also, the creative industries now represent a prominent factor of the Icelandic economy and the paper ventures the opinion that framework of these industries is well suited to the description of the retail sector.

Significant changes have occurred in consumption patterns in recent decades, and in many ways Icelandic trends have been different from those of the other Nordic countries. , altough he structure of the retail trade in the Nordic countries varies. Very large shops are common in Iceland, Finland and Denmark, while smaller shops are prominent in Norway and, to some extent, in Sweden. Hypermarkets have gained increasing prominence over the last 20 years in Europe, and in Iceland, one company, Hagar, has a 46% market share in the food retail trade with three different types of stores catering to different consumer needs. One peculiarity which is worth noting as well is that in the retail market in Iceland 70% of the volume of all merchandise is imported. On the other hand, there have not been extensive changes in Iceland's principal trading partners in recent decades.

Iceland is extremely sparsely populated in comparison with other countries, which makes the retail sector more difficult than in more densely populated countries. However, urbanisation, particularly in the metropolitan area of the capital, has been extensive in the last 100 years, and Iceland is among the countries of the world where the largest part of the population lives in the area of the capital city, which in turn reduces retailing costs. Logistic costs are a major factor in all trade, including retail. The paper gives an account of the impact of logistics costs on trading in Iceland and compares the conclusions with other studies. These costs are extremely dependent on the organization of transport and the competitive environment of trade and services.

1. The retail sector and economic development

Iceland is 103,000 square km in area, with a population of 290,000. Iceland is an independent country, an island in the North Atlantic, with Greenland and the Faeroe Islands as its closest neighbours. The country achieved independence from Denmark in 1944 and enjoys a very high standard of living. In 2003, Iceland's GDP in PPP in US $ per head was 29,800, putting the country in the 8th place in the world (*OECD in Figures* 2004). Iceland is one of the Nordic countries and cooperates closely and extensively with the other Nordic countries, Denmark, Finland, Norway and Sweden. The distance from the capital, Reykjavik, to the mainland of Europe is about 2.000 km. Figure 1 shows the geographic location of Iceland.

Fig. 1: The Atlantic Ocean and Iceland

The retail sector in Iceland has undergone extensive development in recent decades. The independence of the country in 1944 and the post-war years had an impact on Iceland's adaptation to the economies and economic policies of neighbouring countries, as the Icelandic community changed gradually from a primary production society into a service society.

Iceland has been settled since the second half of the ninth century, and was an independent nation until 1262, with active domestic and foreign trade in the first centuries of settlement (Björnsson 2004). From 1626 until 1944, however, Iceland was a colony, first of Norway and then Denmark. In the 15th century England engaged in extensive trade with Iceland, and in the 16th century the Englishmen were joined by the Germans. The King of Denmark, or his agents, controlled all commerce in Iceland, both imports and exports, in the 17th and 18th centuries, but in the 19th century trade was taken over by Icelanders. The 20th century was a time of rapid progress, both in commerce and in farming methods. Figure 2 shows the population trends and economic growth in Iceland over a 100 years' period from the start of the 20th century (*Icelandic Historical Statistics* 1997, *Statistical Yearbook of Iceland* 2004).

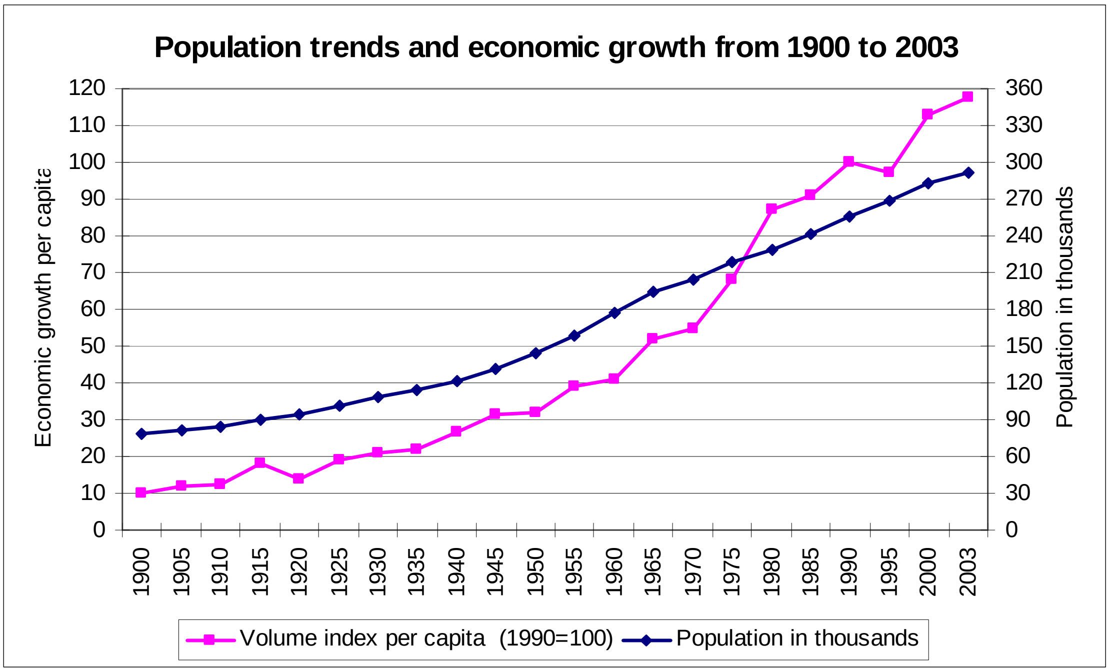

Fig. 2: Population trends and economic growth from 1900 to 2003

As Figure 2 shows, the population of Iceland has grown almost fourfold over the last hundred years, while economic growth per capita has multiplied by a factor of 12 over the same period. Although retail trade was taken over entirely by Icelanders in the period from 1870 to 1903, wholesale remained in foreign hands for the duration of that time. After 1903, however, wholesale was also transferred gradually into Icelandic hands. Figure 3 shows the share of the labour market in agriculture, the fishing industry and trade from 1900.

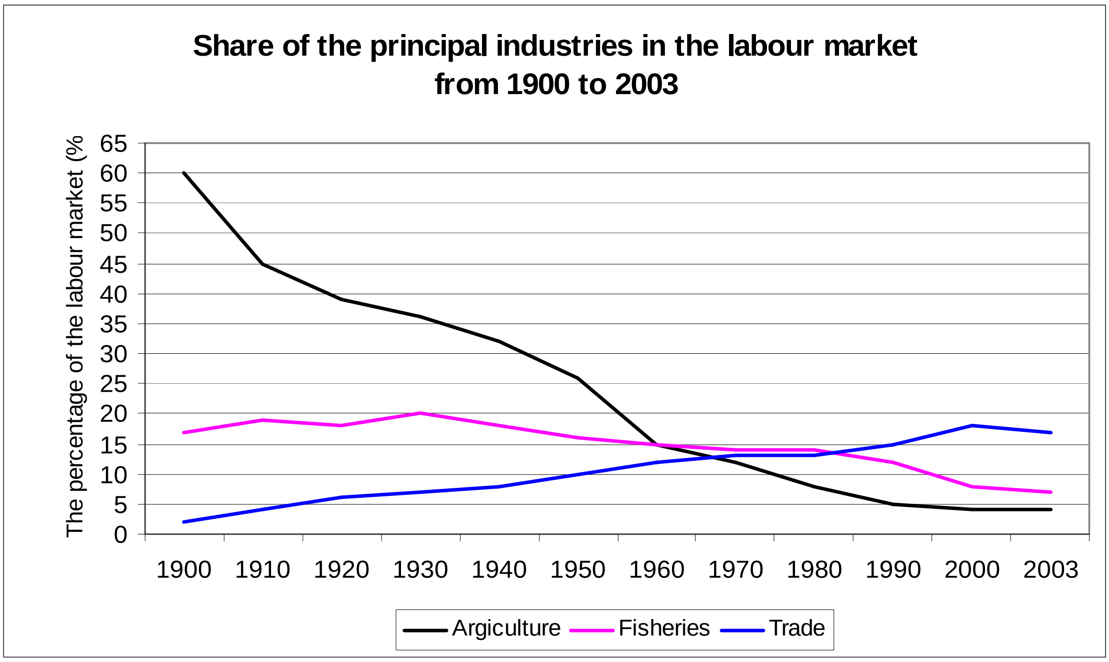

Fig. 3: Share of the principal industries in the labour market from 1900 to 2003

As shown in Figure 3, the industries in Iceland have undergone a transformation over the past 100 years. The share of agriculture in the labour market has fallen from 60% in 1900 to 4% in 2003. Fisheries have fallen from 17% to 7% in 2003, while trade has increased its share in the labour market from 2% in 1900 to 17% in 2003. The retail trade was subject to extensive government interference until 1960, but since that time retail has been governed by a market economy.

One part of the transformation of the Icelandic industries involves the rise of the creative industries and their role in the development of the economy. This is worth brief scrutiny. Research into creative activities was first conducted principally within the social sciences and psychology, which centred on the creative individuals themselves or their creative work. Now, however, growing attention is being focused on the environment of creative work and the creative industries. Creation normally refers to innovation, so that the definition of "creative industries" relates not only to artistic creation, but to a much wider concept.

In the United States, where studies in this field are most advanced, investigations are conducted on the basis of sectors or professions. In the discussion of the creative industries there are two different viewpoints. On the one hand, there is the approach of looking at the creative industries that produce goods and services which have a cultural and artistic value, or recreational value. Here it is the goods and services produced that are at the centre of gravity. From this point of view, sectors such as the film sector, music sector and publishing sector belong to the creative industries (Caves 2000). On the other hand one can look at the individuals in the separate sectors and classify their work into the four following categories: primary production, manufacturing, services and creative industries (Florida 2002). The discussion of the creative industries in this paper uses this method. The industries that constitute creative industries are science, education, arts, design, journalism, sports, computer sciences, engineering, technology, architecture and management.

Management is regarded as a part of the creative industries, as well as high technology, as these are fields where new ideas are shaped. Management in the retail sector and some other elements within that sector therefore belong to the concept of creative industries. Based on the definition of the creative industries above, figures over a longer period in Iceland can be compared with comparable figures for the United States. Figure 4 shows the division of jobs in Iceland by primary production, manufacturing, services and creative industries in the years 1990 and 2002, and a comparison with the United States in 1999 (Florida 2002).

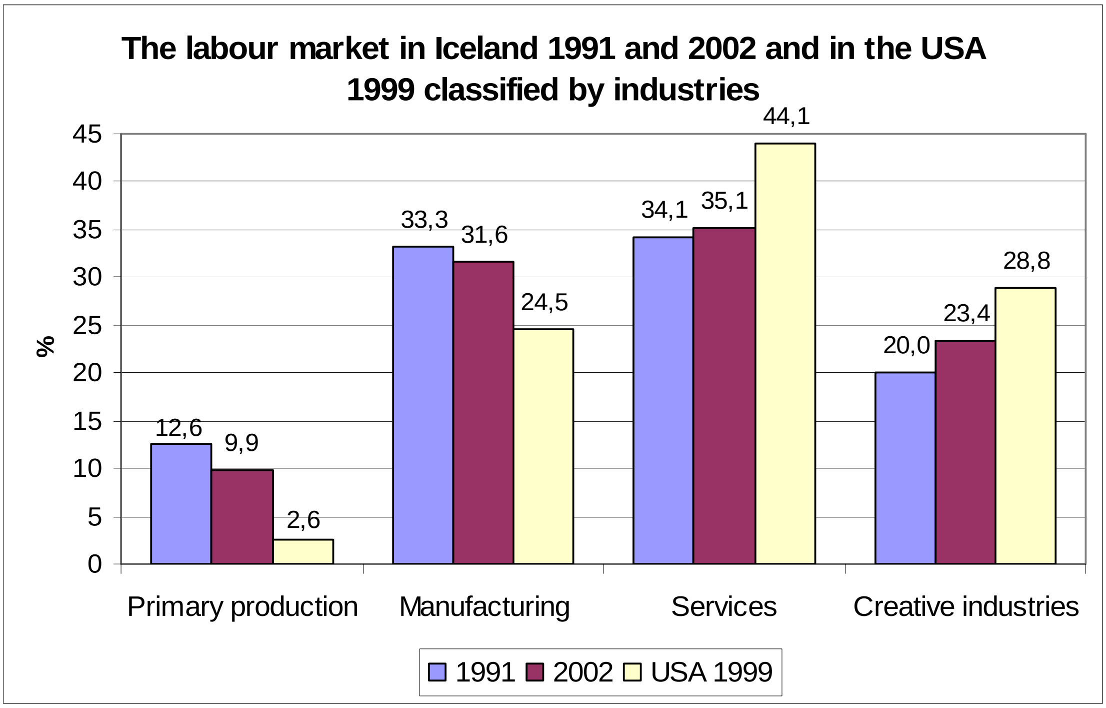

Fig. 4: The labour market in Iceland 1991 and 2002 and in the USA 1999 classified by industries

Figure 4 shows that primary production in Iceland fell from approximately 13% in 1990 to just under 10% in 2002. Manufacturing went from a 33% share to 32% in these 12 years and services from 34% to 35%. The creative industries went from a 20% share in 1990 to 23% in 2002. The corresponding share for the United States was 29%. By 1999, primary production had become a small segment of the labour market in the USA at slightly less than 3%. The creative industries in Iceland account for slightly less than a quarter of the total jobs, or approximately 40,000, and their share is growing. This approach to the analysis of the labour market provides a good indication of the division of labour in modern societies and illustrates the substantial changes that have occurred in the economies of individual countries in recent years. The framework for creative industries is well suited for explaining and describing the increasingly important and complicated role of the retail sector in the developed countries.

2. Changes in consumer behavior

Figure 5 shows changes in consumer patterns in recent decades (*Statistical Yearbook of Iceland* 2004) with private consumption dominating the retail sector.

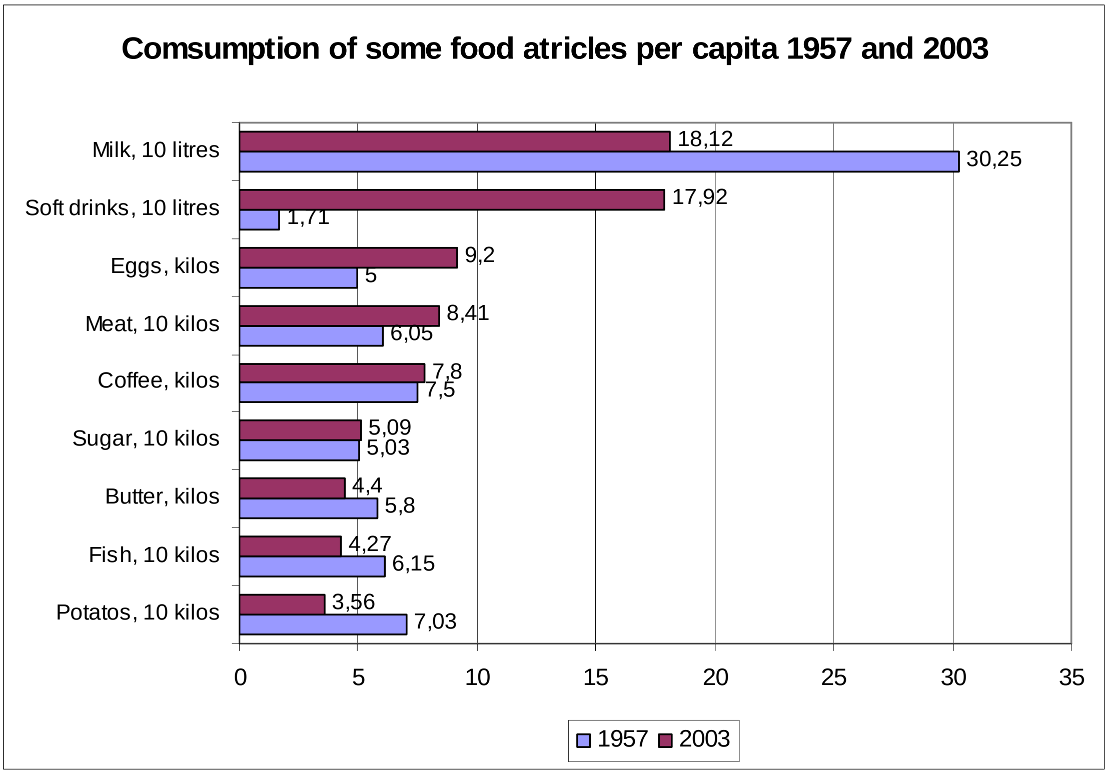

Fig. 5: Consumption of some food articles per capita 1957 and 2003

As Figure 5 shows, changes in food consumption have been extensive over the last 50 years or so. The consumption of milk, which remains substantial in Iceland, has fallen by almost a half. Consumption of soft drinks has grown tenfold. The consumption of eggs and milk has also grown significantly. The consumption of potatoes and fish has fallen considerably, while there has been little change in the consumption of coffee and sugar as a separate product, although it must be kept in mind that the increase in the consumption of soft drinks has greatly increased the consumption of sugar.

Changes in consumption patterns in recent decades are clearly revealed by examination of private consumption over a longer period in Iceland, as shown in Figure 6.

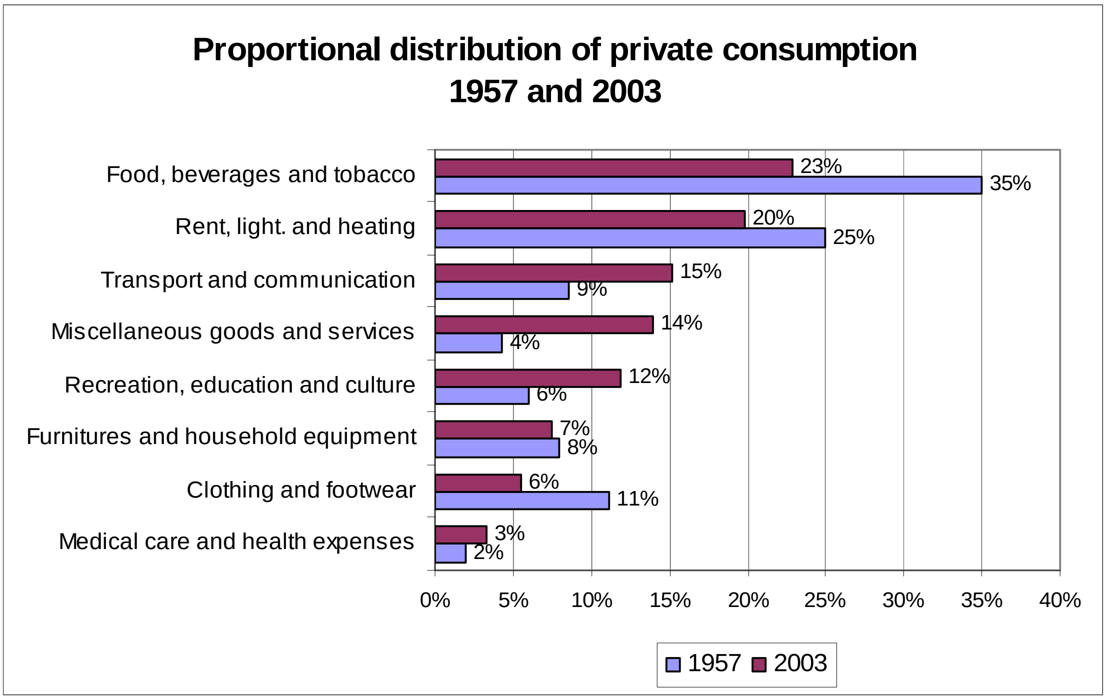

Fig. 6: Proportional distribution of private consumption 1957 and 2003

As shown in Figure 6, purchases of food, housing and clothing have declined proportionally over the last 50 years or so. The increases have occurred in transportation and telecommunications, education and recreation. This change in consumption patterns reflects the social changes occurring over the period. Table 1 shows private consumption in the Nordic countries (*Statistical Yearbook of Iceland* 2004).

	Iceland	**Denmark**	**Finland**	**Norway**	**Sweden**
Registered passenger cars per 10,000 inhabitants	57	35	43	43	45
Sales of alcohol, litres per capita	6.5	11.3	9.2	5.9	6.9
Vegetable fresh, kg per capita	50.7	…	64.1	…	67.4
Milk, 10 litres per capita	14.8	10.4	14.5	11.9	11.5
Beef and veal, kg per capita	13.6	27.5	18.4	20.0	21.4
Pork, kg per capita	20.1	55.6	33.0	24.1	34.4
Sheep and lamb, kg per capita	23.4	1.3	0.4	5.5	1.0
Poultry, kg per capita	15.2	22.0	15.8	11.0	13.8
Fish and shellfish, kg per capita	45.8	…	38.7	55.5	28.5
Sugar, kg per capita	50.9	40.8	33.4	41.2	44.7

Table 1: Consumption in the Nordic countries per capita 2002 /2003

Table 1 shows that car ownership is greatest in Iceland, the consumption of alcohol is greatest in Denmark and Iceland has the lowest consumption of vegetables and the highest of milk. Icelandic consumption of beef and veal is low in comparison with all of the other Nordic countries, but, conversely, the consumption of lamb is highest. Iceland is in about mid-group in the consumption of poultry and at the top in the consumption of fish.

The retail sector has grown significantly in Iceland in comparison with other sectors, with retail growing by approximately 70% in 1990 to 2002 at the same time that the increase has been about 40-45% in Denmark and Sweden and 30% in Finland, but only 20% in Norway (*Nordic Statistical Yearbook* 2004).

3. Size of the retail sector in the economy

One measure of changes in the scope of the retail sector is the retail volume based on fixed prices and as a ratio of GDP, as shown in Figure 7.

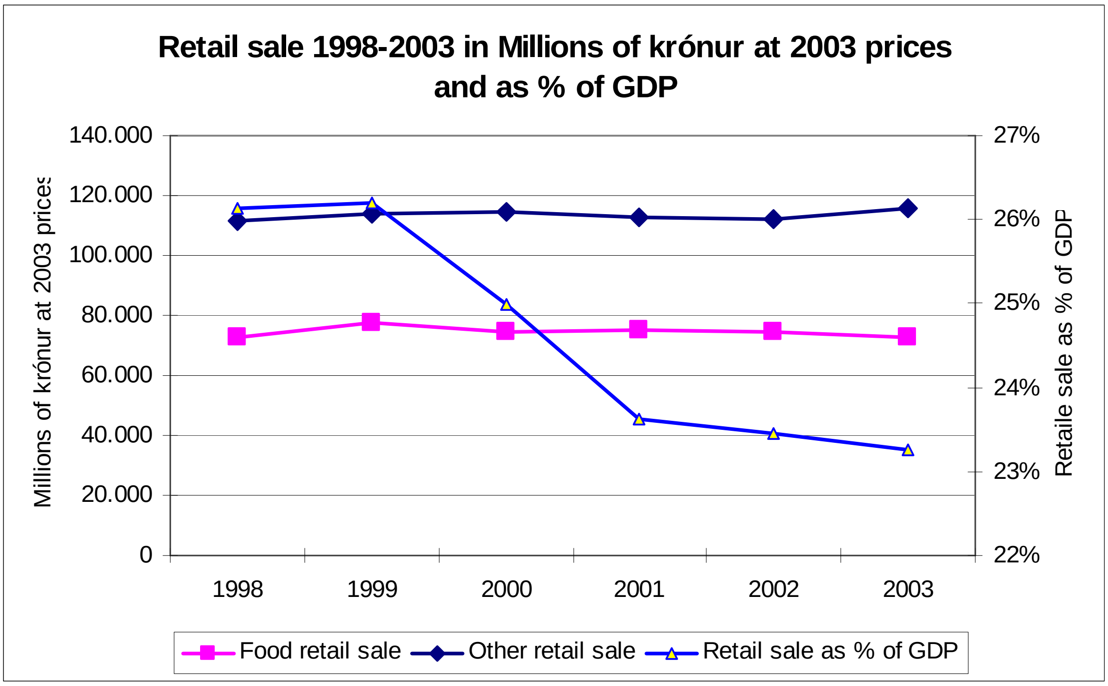

Fig 7: Retail sale 1998-2003 in Millions of krónur at 2003 prices and as % of GDP

As shown in Figure 7, retail has been stagnant over the last 5 years. Food retail is the single largest retail sector, with a turnover of ISK 77 billion this year. Other retail had a volume of ISK 177 billion over the last 5 years. Retail as a ratio of GDP fell over the last 5 years from just over a 26% share to just over 23%, as shown in Figure 7.

Figure 8 shows retail sales divided by sector for the year 2003.

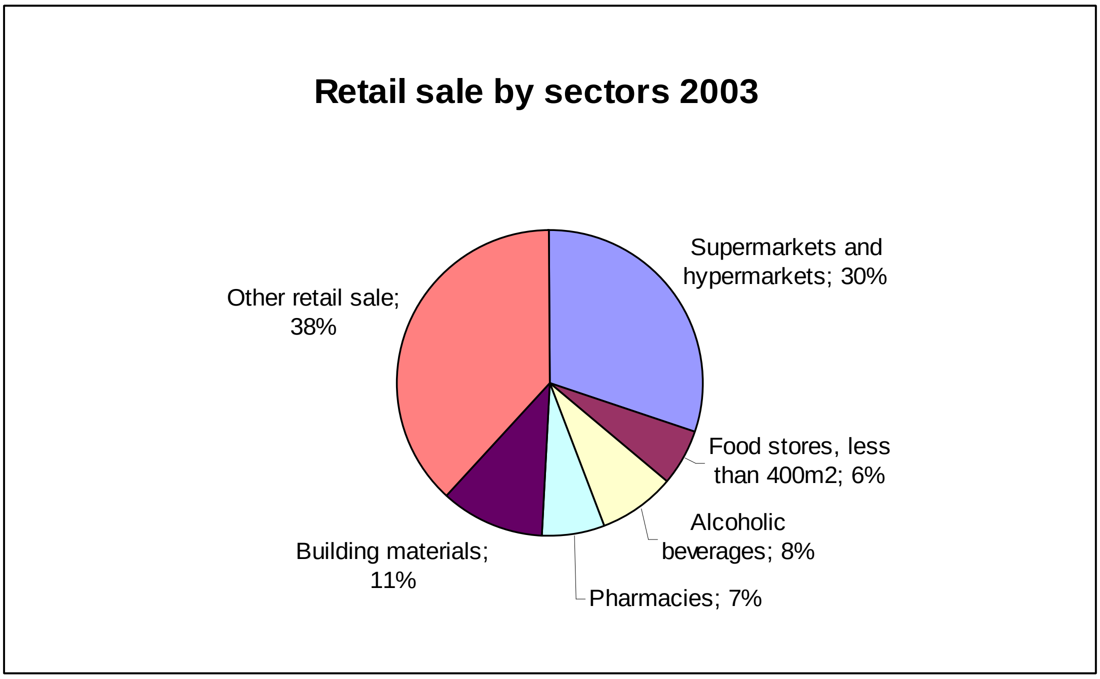

Fig. 8: Retail sale by sector 2003

The retail volume is accounted for to a considerable extent by food sales. This is clearly shown in Figure 8, where supermarkets and hypermarkets, where food is sold in the greatest quantities, account for 30% of total retail. Traditional food retailers with shopping space under 400 square metres only account for an approximately 6% share of total retail. Sales of alcohol are special in Iceland, as the state runs a monopoly, which is responsible for all retailing of spirits, wine and beer. Pharmaceuticals are almost exclusively sold in specialist shops which, however, are frequently owned by the larger retail chains.

Supermarkets and Hypermarkets have been gaining a steadily growing market share, and in 2004 there were three companies in Iceland with 88% of all retail sales of fast moving consumer goods, where the capital area, of course, dominates.[1] Imports to Iceland have originated primarily in Europe, as shown in Figure 9, which describes Iceland's principal import countries in 1983 and 2003 (*Statistical Yearbook of Iceland* 2004).

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[1] The three companies are Hagar, with a 46% share, Kaupas, with 26%, and Samkaup with 16% (Björnsson 2004).

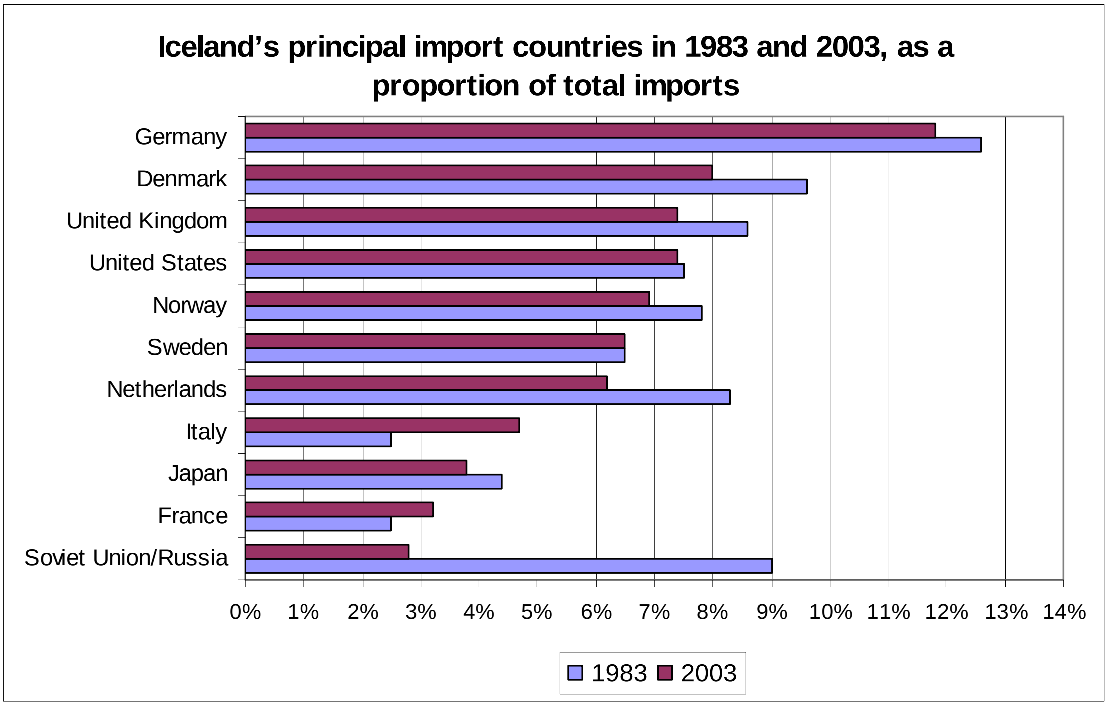

Figure 9: Iceland's principal import countries in 1983 and 2003, as a proportion of total imports

As Figure 9 shows, changes in import countries and the proportional division of trade with them have not been significant over the last 20 years. The same 11 countries accounted for the greatest proportion of imports both in 1983 and 2003, and in both cases Germany is the principal source of imports. In 1983 these countries accounted for 79% of total imports and in 2003 the proportion was the same. It is interesting to note the substantial trade with the former Soviet Union; in fact, Iceland was the European country with the greatest proportion of trade with the Soviet Union. Iceland exported mostly ocean perch to the Soviet Union, but imported almost all of its oil and gasoline from the Soviet Union.

The share of the trade sector and related industries in Gross Domestic Product has grown significantly in recent years, as shown in Figure 10.

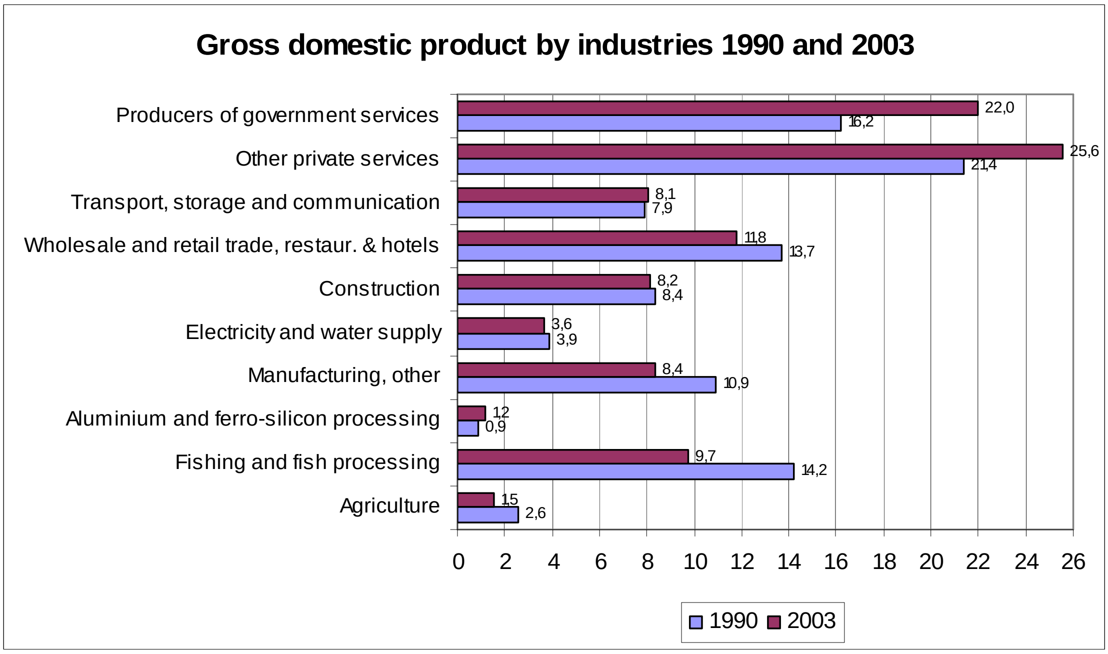

Fig. 10: Gross Domestic Product by industries 1990 and 2003

The share of trade and related industries in GDP amounts to approximately 12%, as shown in Figure 10. Investments in connection with trade and related sectors have accounted for 3% to 4% of the total investment in Iceland in recent years, and although these investments have fallen by 25% over the last six years it must be borne in mind that prior to that time there was a significant increase in investments in commercial premises, especially in retail. Thus, investment in this sector amounted to 11% of total investment in 1987 (*Icelandic Historical Statistics* 1997). Figure 11 shows the share of the retail sector in Gross Domestic Primary Income.

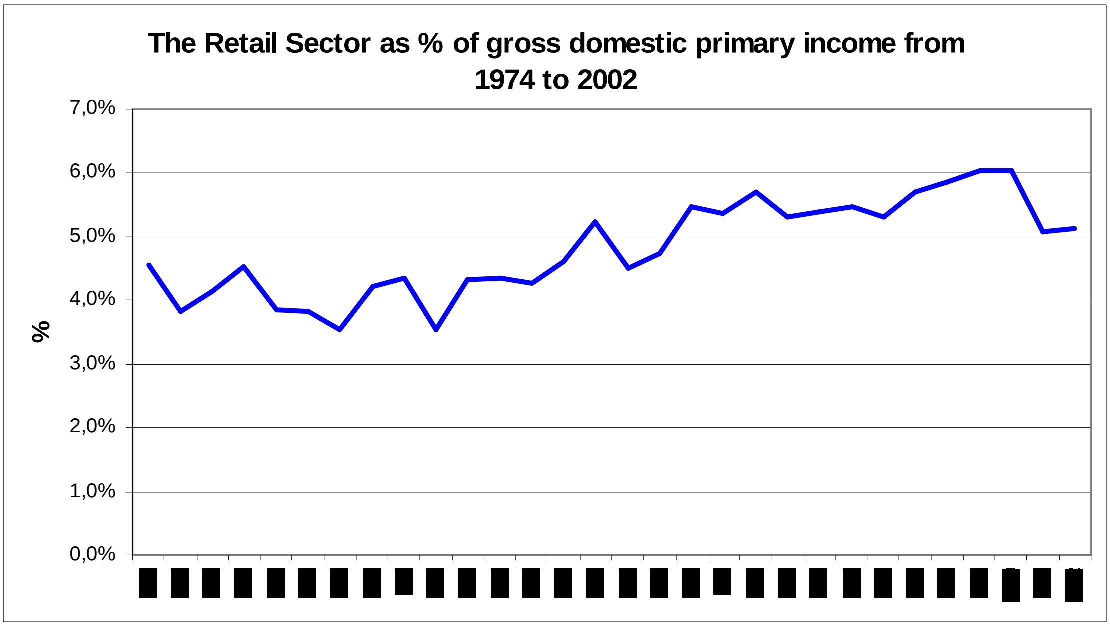

Fig. 11: The tettail sector as % of gross domestic primary income 1973-2002

Figure 11 shows that the share of the retail sector over the last three decades has fluctuated considerably. The share was lowest in 1982, at 3.5%, and highest in 1999 and 2000, at 6.0%. The share has been increasing in recent decades, although it has fallen slightly in the last few years.

4. Logistics cost and trade areas

Iceland is a relatively large country in comparison with its population, with the result that logistics weights significantly in retail prices. Figure 12 shows the population distribution in 162 countries in the world in 2003. The combined population of these countries, which includes most of the countries in the world and all the world's largest countries, is 6.3 billion. Iceland, with 3 inhabitants per square kilometre, is among the most sparsely populated countries in the world, six places from the bottom.

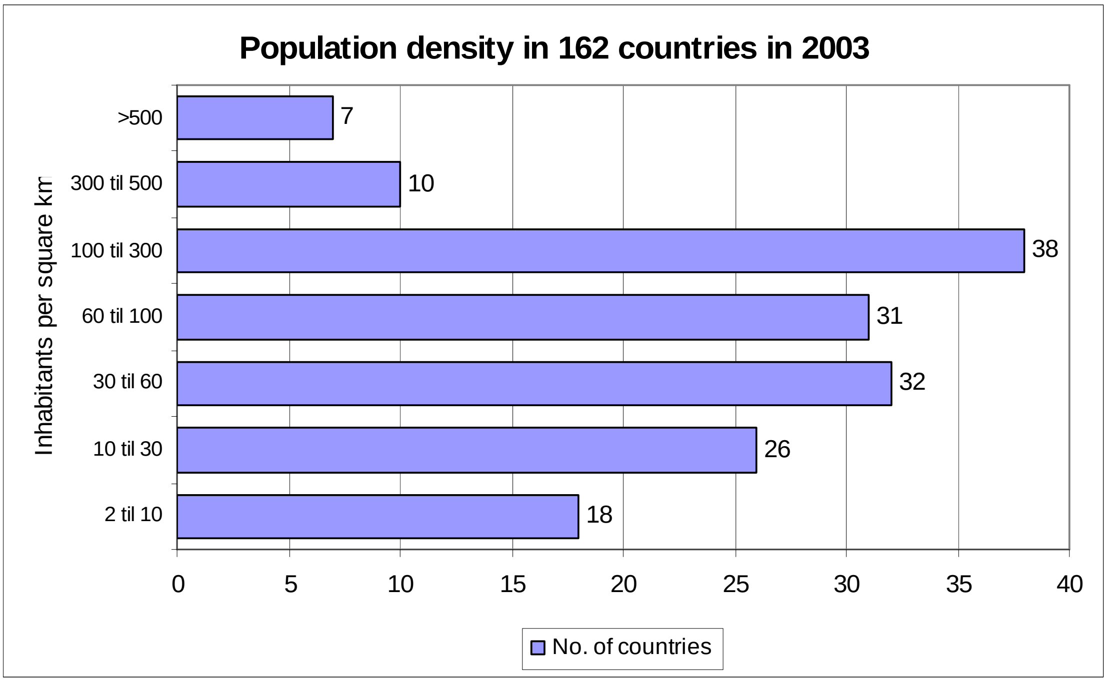

Figure 12: Population density in 162 countries in 2003

The most densely populated country in the world is Singapore, followed by Malta. The ten most sparsely populated countries in the world are Mongolia, Namibia, Australia, Botswana, Surinam, Iceland, Mauritania, Libya, Canada and Guyana. However, the sparseness of the population in Iceland is offset by the fact that a very large proportion of the population lives in the capital area. Figure 13 shows the migration trends between urban and rural areas from 1901 to 1997.

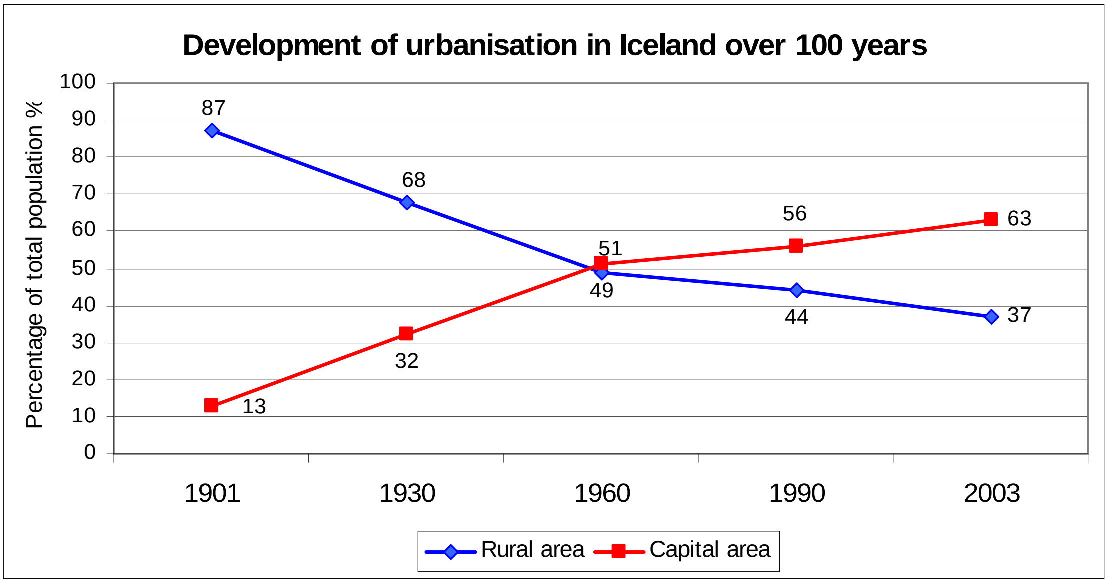

Figure 13: Development of urbanisation in Iceland over 100 years

Figure 13 shows that in 1901 87% of Icelanders lived in rural areas, as compared to 37% at present. This trend has had a significant impact on retail.

Looking at urbanisation in capitals around the world, Figure 14 shows what proportion of the populations of 162 countries lived in the capital area of their respective countries in 2003 (*World Capitals* 2004, *Area and Population of Countries* 2004).

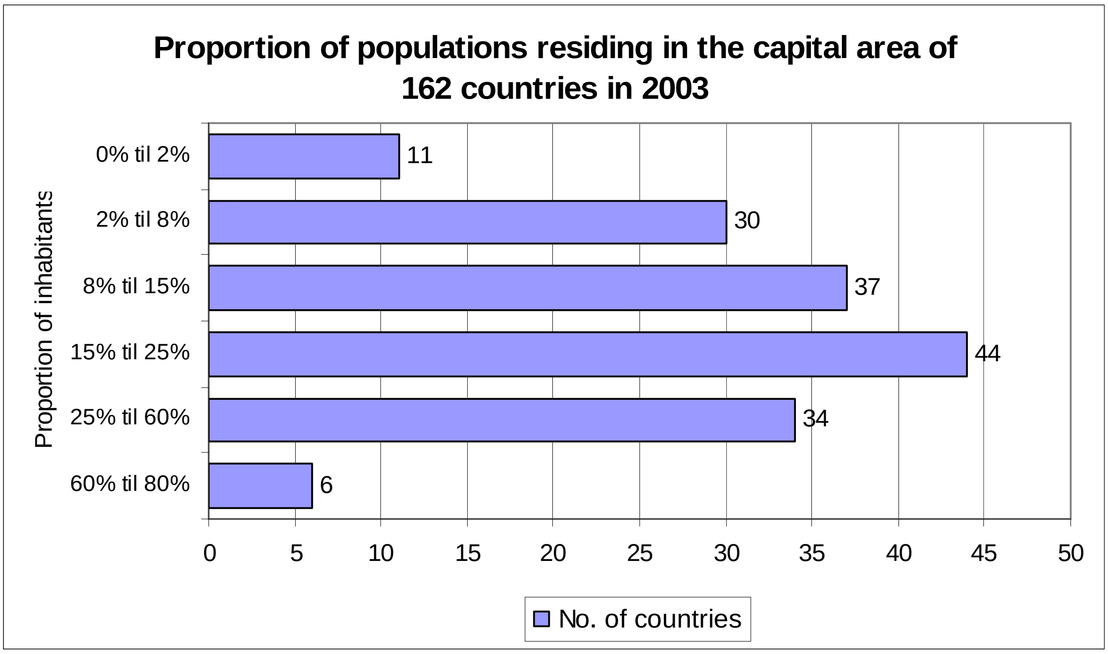

Figure 14: Proportion of populations residing in the capital area of 162 countries in 2003

The case in Iceland is that 63% of the population live in the metropolitan area of the capital, making Iceland virtually into a city state. In only five countries in the world is the ratio of people living in the capital area higher than in Iceland. The ten countries where most of the population lives in the capital area are Singapore, Bahrain, Kuwait, the Bahamas, Qatar, Iceland, Uruguay, the Lebanon, Surinam, and Malta. Although retail is generally difficult in very sparsely populated countries such as Iceland, this is offset by the fact that the large proportion of the population living in the capital reduces distribution costs.

Logistics form a significant part of retail costs. Logistic costs have been investigated for certain factors, i.e. trade in food and non-alcoholic beverages (*Logistics Costs in Iceland* 2003) in both the wholesale sector and the retail sector. The logistic costs in the year 2003 amounted to 8% of turnover. Of that figure, transportation costs were 3%, inventory costs were 4.4% and management costs were 0.5%.

Table 2 shows logistics costs as a percentage of turnover in some European studies (Einarsson 2004).

Research, Year and Country	**Manage-ment costs**	**Inven-tory costs**	**Transpor-tation costs**	**Total costs as % of turnover**
Iceland 2002, food/n-a beverages, manufacturing, trade	0.5%	4.4%	3.0%	8.0%
Norway 1997, manufacturing industry	1.0%	2.8%	7.9%	11.7%
Norway 2001, manufacturing industry	0.9%	2.6%	5.6%	9.1%
Norway 1997, wholesale sector				14.3%
Norway 1999, wholesale sector	1.0%	4.1%	4.1%	9.2%
Finland 1990, manufacturing, trade, construction (m/t/c)	0.7%	5.5%	4.8%	11.0%
Finland 1995, m/t/c	0.8%	4.9%	4.7%	10.3%
Finland 1999, m/t/c	0.6%	5.0%	4.6%	10.2%
Europe 1987, Kearney				14.3%
Europe 1993, Kearney				10.1%
Europe 1998, Kearney, 200 companies	1.2%	3.4%	3.1%	7.7%

Table 2: Logistics costs in some studies in Europe

Table 2 shows the three parts of logistics costs, i.e. management costs, inventory costs and transportation costs. The first row in Table 2 shows Icelandic data. The next two show data from Norway in the manufacturing industry, indicating great improvements in reducing logistics costs over 4 years. The same trend appears in the next two rows, which are based on data concerningthe wholesale sector in Norway. The next three rows show research data from Finland which indicate relatively high logistics costs. There are not many significant differences between the three studies represented in the table. The last three studies were carried out by the company A.T. Kearney for the European Logistics Association (ELA) and show great improvements in 11 years. The ELA surveys extended to the 2.000 members of the ELA and about 200 companies responded to the last survey. One has to be careful in interpreting and comparing these results. The studies have different backgrounds and the data are not always comparable. Nevertheless, it is safe to say that the logistics costs in Iceland are similar to those in Norway. Although Iceland is far more distant from other countries the market in the capital region is more concentrated than elsewhere even though the country is rather large.

The structure of the retail trade in the Nordic countries varies (Næss, 2003). Very large shops are common in Iceland, Finland and Denmark but smaller shops are common in Norway and to some extent in Sweden. In all the five Nordic countries the big companies control the retail trade and these big companies regard the entire world as their home market. The biggest retail company in the world, Wal-Mart, has a turnover of 200 billion euros in 2002, which is 500 times the size of the Iceland's GDP, to give an example. In Iceland one company, Hagar, has a 46% market share in food retail trade with three different types of stores. The same company has a 28% market share of the pharmaceutical market. The reason for its success is that strategic investments have been made in location, information technology and logistics. This company also has extensive operations in Sweden and Britain (Björnsson, 2003).

5. Conclusions and discussion

The position of Iceland is in many ways special as regards the retail trade. The country is large but sparsely populated, although a large proportion of the population lives in the capital area. Retail is an important economic factor, and it would be interesting to analyse the retail sector in further detail in the context of the creative industries, which form a significant part of the economy. Regional trends can have a significant impact on the retail sector, as migration, increased urbanisation and the concentration of markets into larger units result in a completely different situation for retail enterprises than in the past. Private consumption patterns are somewhat different from other countries, especially as regards food products, but it is not clear whether the difference has any particular significance. Supermarkets and hypermarkets dominate the retail sector in Iceland, as they do in neighbouring countries. Studies of logistic costs indicate that these costs are similar in Iceland as in Norway, but it would be interesting to make a more detailed multilateral comparison in this area. Population density and proportion of inhabitants living in the capital area of different countries varies greatly from one country to the next. This is an interesting subject for investigation, not only in relation to the retail sector but other sectors as well.

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