

## Press Release

25 August 2009

### Economic survey, August 2009 - The outlook

Generally the economic outlook has not changed considerably since the May edition of the Economic Survey. The fall in output and demand in the aftermath of the financial crisis is projected to lead to a fall in **real GDP** by 3 per cent in 2009, a bit more than expected in May, mainly due to a weaker than expected development in private consumption in the beginning of the year.

The fall in output was especially large in the 4th quarter of 2008, while the fall slowed down in the 1st and 2nd quarter 2009. The economy is projected to grow in the second half of 2009 and in 2010, due to the significant easing of the fiscal policy setting, the sharp drop in interest rates, a gradual recovery in the international economy, and a significant reduction in inventories. Economic policy is extraordinary expansionary in 2009 and 2010, also compared to other countries, despite relatively low unemployment in Denmark.

GDP is forecast to grow by 1 per cent in 2010. The expected increase in private consumption in the 2nd half of 2009 is set to sustain and moderately expand in 2010. Together with a historical high growth in public investments and a gradual increase in exports, these are the expected driving forces behind the increase in demand and in GDP-growth. The output gap is estimated to have closed in late autumn 2008 and is projected to be negative in 2009 and in 2010, estimated at -2¼ per cent of GDP in 2010. The household savings ratio is assumed to remain very high in both 2009 and 2010.

**Employment** is expected to fall by up to 75,000 persons in both 2009 and 2010 due to the fall in output that has already taken place. In 2010 employment will be at approximately the same level as in 2005. A relatively rapid rise in productivity is expected in 2010 after a fall in 2007-2008. The **labour force** is projected to fall by 20,000 persons in 2009 and 28,000 persons in 2010, one reason being that impaired job opportunities leads more young people into the education system. In addition the number of elderly is increasing due to the demographic development and the number of foreign workers is expected to fall. The labour force is reduced by approximately 1/3 of the fall in employment.

**Unemployment** has risen up until June, from an extraordinary low level. Unemployment is projected to rise further until the end of 2010, but eventually at a significantly lower pace. Unemployment is expected at 105,000 persons (annual average) in 2009 or 3½ per cent of the labour force, rising from 52,000 persons in 2008. In 2010 unemployment is expected at 150,000, or 5¼ per cent of the labour force. This is a bit lower than the unemployment in 2003/2004 and well below the average over the last three decades.

In 2009 and 2010 **wage growth** in private sector is set to slow to 3½ and just over 3 per cent respectively, compared to slightly more than 4½ per cent in 2008, due to severe labour market pressures. Wage growth is still expected to be higher than abroad, which is amplified by a strengthened effective exchange rate in 2009, so that wage competitiveness continues to deteriorate in 2009 and 2010. Wage competitiveness has been deteriorating since the millennial change, mainly due to relatively high Danish wage growth, a weak development in productivity, and a strengthening of the effective exchange rate.

The growth in **consumer prices** is forecast to fall to 1.4 per cent in 2009, compared to 3.4 per cent in 2008, mainly due to lower oil and energy prices and falling food price inflation since last summer, one reason being the financial crisis. In 2010 inflation is expected at 2.0 pct. partly due to higher indirect taxes imposed by the tax reform and a moderate rise in oil prices. Inflation in Denmark has been higher than in the euro area since June 2008.

Households' real disposable **income** is expected to rise significantly in 2009 by slightly more than 3 per cent, despite the fall in labour force and employment. The rise is due to tax reliefs, lower interest rates, growth in real wages and a relatively high automatic regulation of public income transfers. When including the disbursement of the Special Pension savings (SP) income growth is expected at 6½ per cent in 2009. This is a historically high level. In 2010 incomes are expected to continue growing at 4½ per cent (excluding the effects of SP-disbursement in 2009) as a result of further tax reliefs, growth in real wages and continued high automatic regulation of public income transfers.

**Private consumption** fell significantly in the second half of 2008 and in the first quarter of 2009 reflecting a jump in the savings rate. Even though private consumption is expected to grow markedly in the second half of 2009 due to the disbursement of SP-savings and tax reliefs, the annual growth rate is expected at -3¾ per cent in 2009 because of the low level in the beginning of the year. Consumption is expected to rise by 2¾ per cent in 2010 due to the high growth in incomes in 2009 and 2010. Households' savings rate is very high in both years.

**Prices of single-family houses** are expected to fall by 14 per cent in 2009, following a fall of 3¼ per cent in 2008, primarily reflecting significant price falls at the end of last year and the beginning of this year. In the course of 2009 prices are expected to stop falling due to the extraordinarily low interest rate and significant growth in incomes. In 2010 prices are expected to be fairly stable, so that prices of owner-occupied houses will be unchanged in 2010 compared to 2009 (annual averages), corresponding to house prices falling slowly in real terms.

In 2007 **residential investments** reached a historical high level of 7 per cent of GDP. Since then investments have fallen, but are still on a relatively high level. In 2009 residential investments are expected to fall by 10½ per cent, approximately the same pace as in 2008. The fall is moderated by the repair and maintenance scheme included in the Spring Package 2.0. In 2010 the fall is expected to slow to

3½ per cent following the expected stabilisation of the market for owner-occupied dwellings. This implies that residential investments in 2010 will be 5½ per cent of GDP, higher than in all years in the period 1981 to 2004.

The deteriorated international market potential and the fall in output is expected to lead to a reduction in the **fixed business investments** of slightly more than 9 per cent in 2009 after a fall of 4 per cent in 2008. In 2010 business investments are expected to fall further by 1 per cent. The expected turnaround and the assumed improvement in the international economy and low interest rates will support the business investments in 2010. Tighter credit conditions since last summer may on the other hand dampen investments both this year and next.

The financial crisis is expected to cause a fall in **global output** by 1½ per cent in 2009, following 3 per cent growth in 2008. In 2010, when the cycle is expected to improve in part due to the expansionary economic policies, the global economy is set to recover to 2¾ per cent. In 2007 global growth was 5 per cent.

Over the last year GDP has fallen rapidly in key Danish export markets like Germany and Sweden. **Market growth for Danish manufactures** is therefore expected at -11½ per cent in 2009, compared to 2 per cent in 2008 and 7½ per cent in 2007. In 2010 the market growth is expected to recover to 2 per cent.

In light of the market growth and the continued deterioration of Danish wage competitiveness, **manufacturing exports** is expected to fall by 13 per cent in real terms in 2009. A gradual improvement in the international economy in 2010 is expected to lead to growth in manufacturing exports of 1½ per cent. **Total export** of goods and services is expected to fall by 7½ per cent in 2009, while a modest growth of ½ per cent is expected in 2010.

The significant fall in total demand in 2009 is expected to lead to a fall in **imports** of goods and services of 9¼ per cent in real terms. In 2010 imports are expected to rise by 2¼ per cent. This follows a total growth of 40 per cent during the upswing from 2003 until 2007.

The **current account surplus** is expected to fall from just under 40 bn. DKK in 2008 to 20 bn. DKK in 2009 and 14 bn. DKK in 2010, which corresponds to ¾ per cent of GDP. The deterioration of the current account is – apart from an expected downward revision of the surplus in 2008 – to be seen on the back of a change in composition of demand, with a sizable fall in exports in 2009 due to the financial crisis and relatively weak growth in exports in 2010, while the growth in domestic demand is boosted by extensive expansionary measures.

Due to the weak demand, the rise in unemployment and the expansionary fiscal policy a **public finance** deficit of just less than 34 bn. DKK is expected in 2009, following a surplus of almost 60 bn. DKK in 2008. Public finances are sensitive to the changes in the business cycle, the development in the financial markets and in the oil price. Given the assumptions on the fiscal policy setting – including the

Spring Package 2.0, infrastructure investments and the agreement on local government finances – the deficit is expected to rise to just over 86 bn. DKK in 2010, almost 5 per cent of GDP. Breaching the EU reference value of 3 per cent of GDP in the Stability and Growth Pact.

The fiscal position is deteriorating by 8.3 per cent of GDP from 2008 to 2010. Around one third of the deterioration reflects expansionary fiscal measures (measured by direct revenue measures used in fiscal policy effect calculations), including higher expenditures for public consumption and investments, and lower personal tax burden in 2010 due to the tax reform in the Spring Package 2.0. The considerable weakening of the budgetary position also reflects the powerful automatic stabilisers, supporting the households' incomes during a cyclical setback.

The **structural surplus** in the public finances is estimated at 2¼ per cent of GDP in 2008 and just over ¼ per cent of GDP in 2009. In 2010 the surplus is expected to turn into a deficit of 1¼ per cent of GDP. The deficit in 2010 indicates a considerable need for consolidating the public finances towards 2015 in order to meet the central objective of at least balance in public finances in 2015. A status for the 2015-plan will be prepared for the Convergence Programme to the EU.

The **gross debt** (EU harmonised definition) is expected to rise from just less than 27 per cent of GDP by the end of 2007 to just over 42 per cent of GDP by the end of 2010, primarily due to the fiscal deficits and the increased borrowing necessary to finance initiatives in connection with the financial crisis. The public net assets, including both assets and liabilities, will be reduced to around balance in 2010.

On the basis of the agreements on infrastructure investments and the Spring Package 2.0 – including higher municipal investments, the repair and maintenance scheme, and disbursements of SP – the **fiscal policy effect** (the increase in GDP) from active fiscal policies in Denmark is estimated to 1.2 per cent of GDP in 2009. In 2010 activity is further supported by around 1 per cent of GDP, partly due to the agreement on higher municipal investments and the underfinancing of the tax reform in the first years. The fiscal policy measures in 2009 and 2010 are therefore estimated to increase GDP by just over 2 per cent of GDP in 2010.

For further comments on the forecast, please contact:

Jakob Hald, Deputy Permanent Secretary. Direct line: +45 33 92 40 63

Martin Jørgensen, Head of Division. Direct line: +45 33 92 41 38

The development in public finances is explained in more detail in the *Budget Outlook 2*, August 2009.

## Appendix

Table 1. Key figures for the Danish economy

Table 2. Key figures compared with the *Economic Survey*, May 2009.

<b>Table 1</b>						
<b>Key figures for the Danish economy</b>						
	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>
<b>Percentage change from previous year</b>						
Real GDP	2.4	3.3	1.6	-1.2	-3.0	1.0
Trade-weighted GDP abroad	2.2	3.1	2.8	1.3	-4.3	0.7
Export markets for Danish manufactures	5.9	8.9	7.6	2.0	-11.6	2.0
International competitiveness	-1.3	-1.1	-3.1	-4.0	-3.3	-1.6
Export of manufactures, volume <sup>1)</sup>	7.8	6.1	1.1	3.0	-13.0	1.4
Hourly wages	3.6	3.6	4.1	4.6	3.5	3.1
Consumer price index	1.8	1.9	1.7	3.4	1.4	2.0
Price index for single-family houses	17.4	21.6	4.8	-3.2	-14.0	0.0
Merchandise export prices	5.0	3.7	1.8	6.9	-6.1	1.9
Merchandise import prices	3.6	3.1	2.9	6.3	-5.2	1.1
Merchandise terms of trade	1.4	0.6	-1.1	0.6	-1.0	0.8
Productivity in private non-agricultural sector	1.3	1.9	-2.3	-3.7	1.5	5.9
Real disposable income of households	1.2	3.0	0.3	-0.6	3.1 <sup>2)</sup>	4.4
<b>Labour market</b>						
Labour force (thousands)	2,868	2,891	2,935	2,927	2,907	2,879
Employment (thousands)	2,727	2,781	2,857	2,875	2,802	2,729
Of which in private sector	1,902	1,956	2,035	2,062	1,978	1,900
in public sector	825	826	822	813	824	829
Percentage change in total employment	1.1	2.0	2.7	0.6	-2.6	-2.6
Unemployment (thousands)	141	109	78	52	105	150
Unemployment rate (per cent)	4.9	3.8	2.7	1.8	3.6	5.2
Unemployment rate, EU-def. (per cent)	4.8	3.9	3.8	3.3	5.5	6.6
<b>Long term bond yields and exchange rate</b>						
10-year government bonds	3.4	3.8	4.3	4.3	3.6	3.9
30-year mortgage credit bond	4.4	5.1	5.4	6.1	5.4	5.6
The effective krone rate (1980=100)	102.3	102.0	103.2	105.9	107.6	107.7
<b>Balance of payments</b>						
Goods and services (bill. DKK)	75.8	49.5	36.2	39.9	38.2	30.6
Current account (bill. DKK)	67.1	47.0	12.0	39.8	20.6	13.7
Current account (per cent of GDP)	4.3	2.9	0.7	2.2	1.2	0.8
Net foreign assets, ultimo (bill. DKK)	51.2	-26.9	-111.6	-152.6	-165.8	-151.7
Net foreign assets (per cent of GDP)	3.3	-1.7	-6.6	-8.8	-9.7	-8.6
<b>Public finances</b>						
Government net lending (bill. DKK)	77.1	81.5	75.1	59.5	-33.5	-86.3
Government net lending (per cent of GDP)	5.0	5.0	4.5	3.4	-2.0	-4.9
General government gross debt, year-end, (bill. DKK)	572.8	509.5	453.1	580.3	652.7	745.4
General government gross debt, year-end, (per cent of GDP)	37.1	31.3	26.8	33.5	38.3	42.3
Tax burden (per cent of GDP)	51.0	49.8	48.8	48.4	47.4	45.9
Expenditures (per cent of GDP)	51.9	50.7	50.0	50.9	55.1	56.5
1)	Excluding ships and planes.					
2)	Including the disbursement of SP-savings, real disposable income would rise by 6.5 per cent in 2009.					

	2009		2010	
	May	Aug.	May	Aug.
<b>Percentage change from previous year</b>				
Private consumption <sup>1)</sup>	-1.3	-3.7	2.5	2.8
Total public demand	2.4	2.3	1.1	2.1
- public consumption <sup>1)</sup>	1.5	1.4	1.0	1.0
- public investment	14.2	14.8	2.0	15.3
Residential construction	-8.4	-10.6	-3.6	-3.6
Fixed business investments	-8.2	-9.2	1.5	-1.0
Final domestic demand	-1.7	-3.2	1.6	1.7
Stock building (per cent of GDP)	-0.2	-0.7	0.1	0.2
<b>Total domestic demand</b>	<b>-1.8</b>	<b>-3.8</b>	<b>1.7</b>	<b>1.8</b>
Exports of goods and services	-7.3	-7.4	1.3	0.4
- of which manufactures	-12.0	-13.0	1.3	1.4
<b>Total demand</b>	<b>-3.8</b>	<b>-5.1</b>	<b>1.6</b>	<b>1.4</b>
Imports of goods and services	-6.3	-9.2	2.7	2.2
- of which goods	-7.4	-12.1	3.2	3.0
<b>GDP</b>	<b>-2.5</b>	<b>-3.0</b>	<b>1.0</b>	<b>1.0</b>
Gross value added	-2.5	-2.4	0.9	0.8
- of which private sector <sup>2)</sup>	-3.5	-3.5	0.8	0.9

1) Real growth of public consumption reflects growth in inputs, not improvements of output and is therefore not readily comparable to private consumption growth.

2) Excluding agriculture, housing and sea transport.

*(continued on next page)*

<b>Table 2 (continued)</b>				
<b>Key figures compared to the May Survey</b>				
	2009		2010	
	May	Aug.	May	Aug.
<b>Change in 1,000 persons</b>				
Labour force	-20	-20	-28	-28
Employment	-74	-74	-68	-73
Of which in private sector	-84	-84	-73	-78
in public sector	11	11	5	5
Unemployment	53	53	40	45
<b>Growth, per cent</b>				
Merchandise export prices	-2.3	-6.1	1.2	1.9
Merchandise import prices	-3.2	-5.2	0.7	1.1
Merchandise terms of trade	0.9	-1.0	0.5	0.8
House prices, single-family house	-7.0	-14.0	0.0	0.0
Consumer prices	1.4	1.4	2.1	2.0
Hourly compensation, private sector	3.2	3.5	3.2	3.1
Real disposable income, private sector	3.7	0.8	3.4	4.7
Real disposable income of households <sup>3)</sup>	2.6 <sup>4)</sup>	3.1 <sup>5)</sup>	4.0	4.4
Productivity in private non-agricultural sector <sup>6)</sup>	1.4	1.5	5.4	5.9
<b>Per cent per year</b>				
Interest rate 1-year flex loan	2.8	2.6	2.7	2.7
10-year government bonds	3.7	3.6	4.1	3.9
30-year mortgage credit bond	5.5	5.4	5.6	5.6
<b>Balances</b>				
Current account (bn. DKK)	19.9	20.6	14.9	13.7
Government net lending (bn. DKK)	-22.5	-33.5	-60.1	-86.3
Unemployment (thousands)	105	105	145	150
<b>External assumptions</b>				
Trade-weighted GDP abroad, per cent	-3.5	-4.3	0.6	0.7
Markets for Danish manufactures, per cent	-9.4	-11.6	1.6	2.0
Exchange rate, DKK per \$	5.6	5.4	5.6	5.2
Oil price, \$ per barrel	53.2	60.7	63.8	71.4
Oil price, DKK per barrel	299.5	329.1	357.3	374.5
3)	Adjusted.			
4)	Including the SP-disbursement, the rise in income in 2009 was 4.6 per cent in May.			
5)	Including the SP-disbursement, the rise in income in 2009 is now 6.5 per cent.			
6)	Excluding home utilisation and shipping.			