Denmark

GDP is already above potential, but growth is set to continue at 3% in 2006 and 2½ per cent in 2007, with all demand components growing solidly. However, with capacity constraints already visible and wage and price inflation set to pick up in due course, domestic firms are likely to lose market share.

Expansionary monetary conditions are currently adding stimulus to the already buoyant economy. Hence, fiscal policy should be tighter and it is urgent to increase labour supply both by strengthening work incentives and by making it easier for foreigners to enter sectors like construction.

The expansion is strong and broadly based

The economy accelerated strongly in the summer of 2005, with GDP increasing by 3% for the year as a whole – much faster than estimated potential GDP growth of 1½ to 2%. The expansion has become broadly based with buoyant consumption and residential construction being re-enforced by growing business investments and exports, as order books have filled up rapidly since mid 2005. However, with strong domestic demand, imports have grown more briskly than exports. Housing investment expanded by 13% in 2005 on the back of exceptionally strong house prices increases. The output gap is estimated to have closed in late 2005, and labour shortages are appearing, notably in construction. So far, wage growth has been modest, and while consumer price inflation has increased from its 2004 trough, it has not gone much above 2%. In a recent survey, however, 44% of firms reported rising wage pressures *versus* only 2% reporting declining wage pressures.

Monetary conditions are excessively stimulative

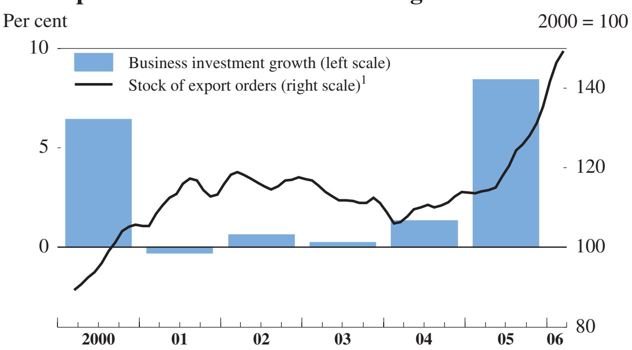
With continued slack in the euro area, monetary conditions received *via* the fixed exchange rate regime will add excessive stimulus. At 2½ per cent, short-term interest rates are currently well below estimates of a neutral rate. Over the projection period, short rates should be expected to rise gradually in line with the European Central Bank's policy rate, reaching 3¾ per cent at the end of 2007. Nevertheless, with an increasing positive output gap and growing wage and inflationary pressures, the difference between actual interest rates and those appropriate for domestic stabilisation is likely to remain.

Capacity constraints lead to loss of market share

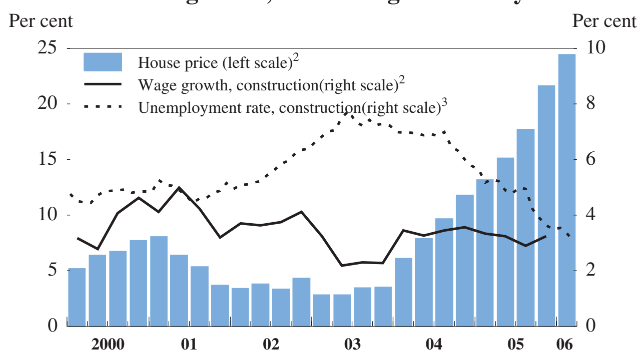
Capacity constraints are likely to limit the ability of domestic firms to meet growing demand in both home and export markets, as it has been the case in periods like the mid 1990s when the business cycle was desynchronised from that of the country's trad-

Denmark

Export and business investments gain momentum



Housing boom, but no wage reaction yet



1. Manufacturing, 3 months moving average, current prices.
2. Year-on-year percentage change.
3. Among persons with unemployment insurance. This tends to be higher than the Labour Force Survey concept used for the aggregate economy.
Source: Statistics Denmark.

StatLink: *http://dx.doi.org/10.1787/456308554210*

Denmark: **Demand, output and prices**

	2002	2003	2004	2005	2006	2007
	Current prices DKK billion	Percentage changes, volume (2000 prices)				
Private consumption	652.3	1.6	3.4	3.8	2.3	2.7
Government consumption	360.2	0.2	1.5	1.3	1.3	0.8
Gross fixed capital formation	270.8	2.0	4.5	9.0	8.7	5.8
Final domestic demand	1 283.3	1.3	3.1	4.2	3.4	2.9
Stockbuilding[1]	9.3	-0.6	0.2	-0.1	0.1	0.0
Total domestic demand	1 292.6	0.6	3.3	4.0	3.4	2.9
Exports of goods and services	648.9	-1.2	2.7	7.9	6.2	4.9
Imports of goods and services	568.7	-1.7	6.4	10.8	8.1	6.1
Net exports[1]	80.1	0.1	-1.3	-0.8	-0.5	-0.4
GDP at market prices	1 372.7	0.7	1.9	3.1	3.0	2.4
GDP deflator	_	1.9	2.2	2.6	2.0	2.9
Memorandum items						
Consumer price index	_	2.1	1.2	1.8	1.7	2.6
Private consumption deflator	_	2.0	1.7	2.0	2.0	2.6
Unemployment rate[2]	_	5.3	5.5	4.8	4.2	3.9
Household saving ratio[3]	_	3.3	3.0	-0.8	-1.0	-1.8
General government financial balance[4]	_	-0.1	1.7	4.0	3.3	3.8
Current account balance[4]	_	3.2	2.3	3.2	2.7	2.5

Note: National accounts are based on official chain-linked data. This introduces a discrepancy in the identity between real demand components and GDP. For further details see OECD Economic Outlook Sources and Methods, *(http://www.oecd.org/eco/sources-and-methods).*

1. Contributions to changes in real GDP (percentage of real GDP in previous year), actual amount in the first column.
2. Based on the Labour Force Survey, being ½-1 percentage point below the claimant-count unemployment rate.
3. As a percentage of disposable income, net of household consumption of fixed capital.
4. As a percentage of GDP.

Source: OECD Economic Outlook 79 database.

StatLink: *http://dx.doi.org/10.1787/356118422342*

ing partners. With an output gap moving from -2% of GDP in 2004 to a projected +1½ per cent of GDP in 2007, while growth abroad is around potential, negative net exports are likely to continue even though external demand is strong. The aggregate effect of the trade boycott following newspaper cartoons of the prophet Muhammad, is likely to be negligible, as only 2% of Danish exports go to the Middle East.

GDP growth remains well above potential

GDP is projected to continue growing at 3% in 2006 before slowing to around 2½ per cent in 2007. Consequently, private sector employment is set to expand and unemployment to fall further below its structural level. Wage and price inflation is expected to pick up, although with a lag. Imports should be growing somewhat faster than exports, and the trade balance should deteriorate. If oil prices remain at their current high level, revenues from corporate taxation of North Sea oil exploration will continue to boost the fiscal balance with the surplus remaining not far below the 2005 record of 4% of GDP. The effect of fiscal policy on economic activity is estimated to be broadly neutral, although tightening would be warranted.

House prices could pose risks

Gradually rising short- and long-term interest rates will help dampen the housing boom. A soft landing is still the central scenario, but if house prices continue going up at the exceptional pace seen lately, then a subsequent downward correction cannot be excluded. However, continued growth in employment and earnings should cushion household spending even if wealth effects from house price increases dissipate or reverse modestly. Large-scale mortgage equity withdrawals during 2005 are waiting to be spent. Meanwhile, even if falling a bit, house prices are so much above construction costs that residential investment should remain attractive.

Special chapters in recent issues of *OECD Economic Outlook*

No. 78, December 2005

Recent house price developments: the role of fundamentals

No. 77, June 2005

Measuring and assessing underlying inflation

No. 76, December 2004

Oil price developments: drivers, economic consequences and policy responses

Saving behaviour and the effectiveness of fiscal policy

No. 75, June 2004

Housing markets, wealth and the business cycle

The challenges of narrowing the US current account deficit

Asset price cycles, "one-off" factors and structural budget balances

Enhancing income convergence in central Europe after EU accession

No. 74, December 2003

Fiscal stance over the cycle: the role of debt, institutions, and budget constraints

Fiscal relations across levels of government

Enhancing the cost effectiveness of public spending

No. 73, June 2003

After the telecommunication bubble

Structural policies and growth

Trends in foreign direct investment in OECD countries

Foreign direct investment restrictions in OECD countries

Policy influences on foreign direct investment

No. 72, December 2002

Fiscal sustainability: the contribution of fiscal rules

Increasing employment: the role of later retirement

Product market competition and economic performance

Inflation persistence in the euro area

No. 71, June 2002

Economic consequences of terrorism

Ongoing changes in the business cycle

Intra-industry and intra-firm trade and the internationalisation of production

Productivity and innovation: the impact of product and labour market policies

OECD ECONOMICS DEPARTMENT

A wide range of news and information about recent Economics Department studies and publications on a variety of topics is now regularly available via Internet on the OECD Web site at the following address: ***www.oecd.org/eco***. This includes links to the *Economics Department Working Papers* series (***www.oecd.org/eco/Working_Papers***), which can be downloaded free of charge, as well as summaries of recent editions in the *OECD Economic Surveys* (***www.oecd.org/eco/surveys***) series and the *OECD Economic Outlook* (***www.oecd.org/OECDEconomicOutlook***).

OECD ECONOMIC OUTLOOK

The *OECD Economic Outlook* Flashfile, containing a summary of the *Economic Outlook* forecasts is now available on Internet at the time of its preliminary publication (a month to six weeks before the final publication date) at the following address: ***www.oecd.org/eco/statistics***. This includes key macroeconomic variables for all OECD countries and regions in Excel™ format, which can be input directly into most statistical and analytical software. The *Economic Outlook* Flashfile is available free of charge.

Subscribers to the *OECD Economic Outlook*, in addition to the two print editions, also have access to an online (PDF) edition, published on Internet six to eight weeks prior to the release of the print edition:

http://new.SourceOECD.org/periodical/oecdeconomicoutlook

The full set of historical time series data and projections underlying the *OECD Economic Outlook* is now available online as a statistical database *via* SourceOECD and on CD-ROM. It contains approximately 4 000 macroeconomic time series for OECD countries and non-OECD zones, beginning in 1960 and extending to the end of the published forecast horizon. Subscriptions to the database editions can be combined in sets with the subscriptions to the Print and PDF editions and can be made at any time of the year.

For more information, visit the OECD bookshop at ***www.oecd.org/bookshop***, or contact your nearest OECD supplier: ***www.oecd.org/publishing/distributors***.

TABLE OF CONTENTS

Tables

Figures

This book has...

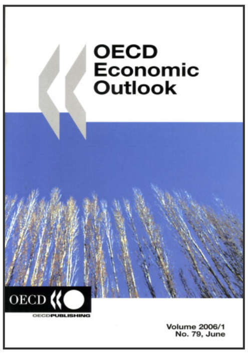
StatLinks

A service from OECD Publishing that delivers Excel™ files from the printed page!

Look for the StatLinks at the bottom right-hand corner of the tables or graphs in this book. To download the matching Excel™ spreadsheet, just type the link into your internet browser, starting with the ***http://dx.doi.org*** prefix.
If you're reading the PDF e-book edition, and your pc is connected to the Internet, simply click on the link. You'll find StatLinks appearing in more OECD books.

Conventional signs

$	US dollar	.	Decimal point
¥	Japanese yen	I, II	Calendar half-years
£	Pound sterling	Q1, Q4	Calendar quarters
€	Euro	Billion	Thousand million
mb/d	Million barrels per day	Trillion	Thousand billion
. .	Data not available	s.a.a.r.	Seasonally adjusted at annual rates
0	Nil or negligible	n.s.a.	Not seasonally adjusted
–	Irrelevant		



From:
OECD Economic Outlook, Volume 2006 Issue 1

Access the complete publication at:
https://doi.org/10.1787/eco_outlook-v2006-1-en

Please cite this chapter as:

OECD (2006), “Denmark”, in *OECD Economic Outlook, Volume 2006 Issue 1*, OECD Publishing, Paris.

DOI: https://doi.org/10.1787/eco_outlook-v2006-1-16-en