

DENMARK

The Danish economy is currently experiencing its worst recession in over four decades. The downturn, which started with the unwinding of the property boom, has now been compounded by the trade and financial effects of the global economic crisis.

The capacity pressures evident in recent years have disappeared and economic slack is widening. There would be scope for additional fiscal policy stimulus in 2010. Monetary policy should be eased in line with policy in the euro area and as foreign exchange market conditions allow.

GDP will continue to fall in the near term

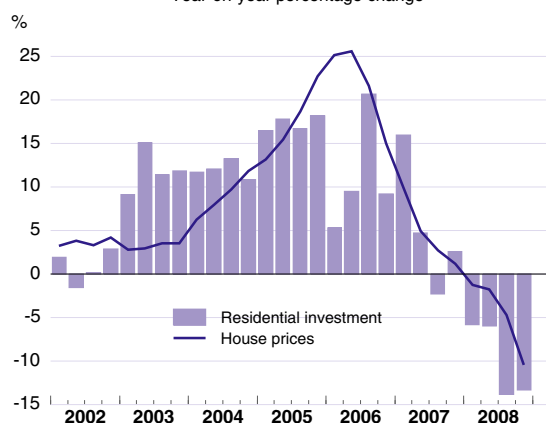
The Danish economy had already turned down before the global financial crisis intensified in late 2008, as the unwinding of the property boom reined in consumption and residential investment. GDP contracted during most of last year and, by end-2008, was 3.6% lower than a year earlier. Indicators suggest a further large fall in demand in early 2009. The pace of decline of industrial production has accelerated since the start of the year. Monthly goods trade data point to a sharp fall in both imports and exports. Business sentiment has deteriorated rapidly and the number of business bankruptcies has soared. On the other hand, interest rates faced by households have come down and business expectations and consumer confidence have improved.

Financial stress and weak property markets persist

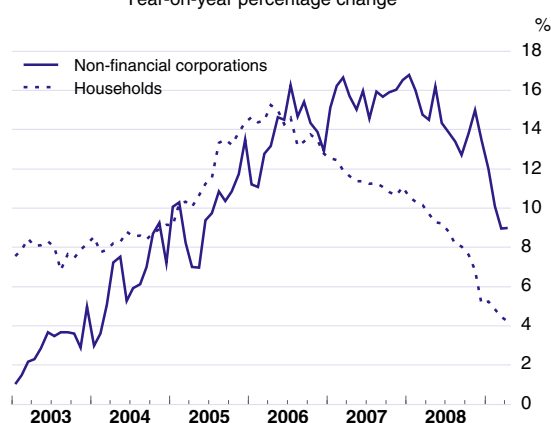
Growth in lending by banks and mortgage credit institutions has slowed from the rapid rates of a few years ago. Smaller institutions in particular have had difficulty raising funds to finance lending. Increasing loan losses will depress bank profitability, although the government's capital injection package should provide support for lending. Subdued lending growth may also reflect an easing of demand for mortgage loans. National average prices for one-family houses fell 7.7% in the last quarter of 2008, and were down 10.4% from a year earlier. Lower house prices and

Denmark

House prices have shaped residential investment growth
Year-on-year percentage change



Growth in lending has slowed
Year-on-year percentage change



Source: Statistics Denmark; OECD Economic Outlook 85 database; and Danmarks Nationalbank.

StatLink <http://dx.doi.org/10.1787/657402041755>

Denmark: Demand, output and prices

	2005	2006	2007	2008	2009	2010
	Current prices DKK billion	Percentage changes, volume (2000 prices)				
Private consumption	745.1	4.4	2.4	-0.1	-2.3	0.5
Government consumption	402.5	2.1	1.3	1.1	1.5	1.0
Gross fixed capital formation	301.6	13.5	3.1	-3.6	-8.3	-3.2
Final domestic demand	1 449.3	5.7	2.2	-0.6	-2.6	-0.1
Stockbuilding ¹	20.2	-0.3	-0.3	0.1	0.0	0.0
Total domestic demand	1 469.5	5.3	1.9	-0.5	-2.9	-0.1
Exports of goods and services	757.0	9.1	2.2	2.2	-12.8	0.5
Imports of goods and services	681.2	13.9	2.8	3.7	-11.1	0.0
Net exports ¹	75.8	-1.7	-0.2	-0.7	-1.1	0.2
GDP at market prices	1 545.3	3.3	1.6	-1.1	-4.0	0.1
GDP deflator	—	2.0	2.0	4.3	1.9	2.3
<i>Memorandum items</i>						
Consumer price index	—	1.9	1.7	3.4	1.3	1.5
Private consumption deflator	—	1.9	1.8	3.1	1.3	1.4
Unemployment rate ²	—	3.9	3.6	3.3	6.0	7.9
Household saving ratio ³	—	0.4	-1.0	0.6	5.0	5.0
General government financial balance ⁴	—	5.0	4.5	3.4	-2.4	-4.1
Current account balance ⁴	—	2.9	0.7	2.0	1.5	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 above the registered 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 85 database.

StatLink  <http://dx.doi.org/10.1787/660767780342>

rising unemployment should hold down residential investment, although renovations of existing buildings will be boosted by government subsidies for energy efficiency.

Policy stimulus is substantial but there would be scope to do more in 2010

The central bank has been gradually reducing the spread to European Central Bank (ECB) official interest rates which had opened up last October. Danish central bank foreign currency reserves have doubled in recent months and the currency has been stable. With the spread to euro area rates expected to be eliminated in coming months, Danish monetary policy will follow any further easing implemented by the ECB. Fiscal policy will be expansionary in 2009, due in part to tax cuts decided in 2007. The government's initiative to release funds from the compulsory private Special Pension saving scheme in mid-2009 should add to demand, although there is considerable uncertainty over how much. Further tax cuts commencing in 2010, as part of a tax reform to add to labour supply in the long run, will provide an additional boost. The need for additional stimulus is reduced by the large size of the automatic stabilisers, with the budget position set to decline by almost eight percentage points of GDP in total, but further fiscal measures could cushion activity.

**GDP will contract further
in 2009 before recovering
slowly in 2010**

GDP is projected to contract sharply in 2009. Exports will be weak in the near term and may lag somewhat behind the recovery in export markets due to the modest appreciation of the effective exchange rate. Consumption is set to be dampened by falls in household wealth and rising unemployment, but should get significant support from the boost to disposable income resulting from fiscal policy measures. Slowing lending growth, low share prices and low capacity utilisation will restrain capital formation. The economy should recover during 2010, but only enough to raise annual GDP growth barely above zero. Inflationary pressures are expected to ease due to the scale of economic slack, but indirect tax hikes will limit disinflation in 2010. The unemployment rate probably surpassed the estimated structural rate already in the first half of 2009 and will continue to rise into 2010.

**There are downside and
upside risks**

Economic developments in Denmark could be weaker still if the feedback effects of higher unemployment, lower house prices and rising loan losses lead financial institutions to cut back lending even more. This risk is mitigated somewhat by the government's offer to inject capital into banks and mortgage credit institutions. However, the economy could perform better than currently anticipated if the monetary and fiscal stimulus translate into more robust consumer spending than currently projected.



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