DENMARK

The Danish economy was hit hard, if belatedly, by the global economic crisis but is projected to recover gradually as world trade regains momentum and as support is provided by the large automatic stabilisers, substantial fiscal easing and low interest rates.

Despite some withdrawal of the fiscal stimulus imparted in response to the crisis, the budget deficit is expected to remain large in 2011. Additional consolidation measures will be needed in due course to bring the fiscal position back on track with the long-term targets, and these measures should be spelled out sooner rather than later.

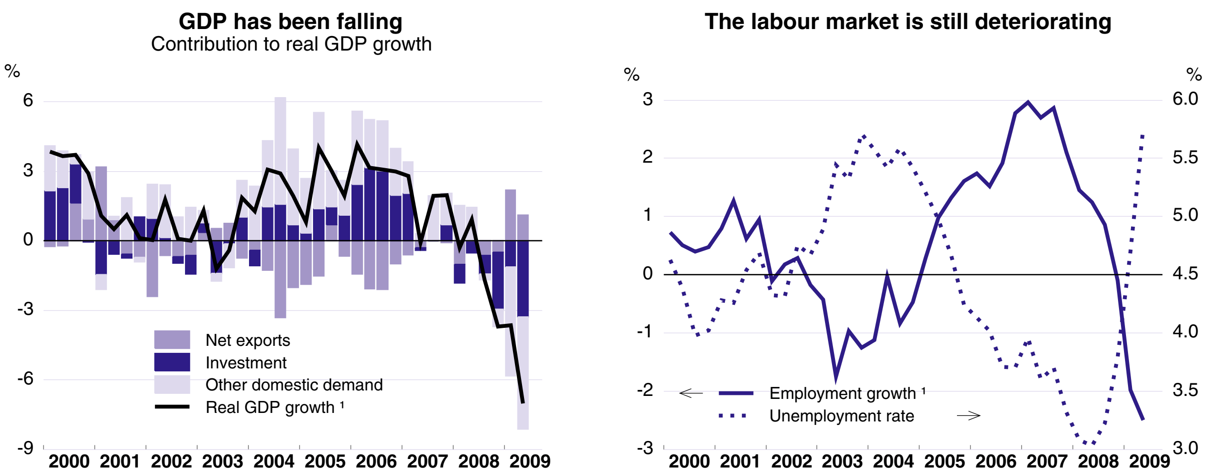
The economy has contracted sharply

Output fell sharply in the first half of 2009, with GDP in the second quarter down by 7% over a year earlier. The contraction was driven mainly by plunging business and housing investment as well as by the continuing decline in exports. Private consumption fell very steeply in late 2008 and early 2009 but less so subsequently, as it is being supported by tax cuts, withdrawals from the special pension scheme and less depressed equity prices. High-frequency indicators point to an improvement in the third quarter of 2009. Sentiment is up in manufacturing and industrial production seems to have stabilised at a low level, while the number of new bankruptcies is coming down. The outlook is more uncertain, however, for the construction sector.

Unemployment will increase further

Employment dropped in three consecutive quarters and unemployment has increased steeply, though from a very low level. Further declines in employment and increases in unemployment are projected even as the economy recovers. Wage inflation, which was fairly high until recently, eroding international competitiveness, has moderated.

Denmark



1. Year-on-year percentage change.

Source: OECD, OECD Economic Outlook 86 database.

StatLink http://dx.doi.org/10.1787/751207645883

Denmark: **Demand, output and prices**

	2006	2007	2008	2009	2010	2011
	Current prices DKK billion	Percentage changes, volume (2000 prices)				
Private consumption	792.8	2.4	-0.2	-4.8	1.6	2.4
Government consumption	422.5	1.3	1.5	2.2	1.8	1.5
Gross fixed capital formation	347.4	3.1	-5.1	-12.4	-4.9	3.2
Final domestic demand	1 562.7	2.2	-0.9	-4.5	0.4	2.3
Stockbuilding[1]	16.4	-0.3	0.2	-1.3	0.9	0.0
Total domestic demand	1 579.2	1.9	-0.7	-6.2	1.4	2.3
Exports of goods and services	846.5	2.2	2.2	-9.7	1.8	4.4
Imports of goods and services	797.0	2.8	3.4	-13.0	2.0	5.4
Net exports[1]	49.5	-0.2	-0.5	1.6	0.0	-0.4
GDP at market prices	1 628.6	1.6	-1.2	-4.5	1.3	1.8
GDP deflator	_	2.0	4.0	-0.5	1.2	2.1
Memorandum items						
Consumer price index	_	1.7	3.4	1.3	1.4	1.6
Private consumption deflator	_	1.8	3.1	1.4	1.2	1.4
Unemployment rate[2]	_	3.6	3.3	5.9	6.9	6.2
Household saving ratio[3]	_	-1.0	-0.3	8.1	9.0	8.1
General government financial balance[4]	_	4.5	3.4	-2.5	-5.4	-4.0
Current account balance[4]	_	1.5	2.2	2.5	2.1	2.1

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 86 database.

StatLink http://dx.doi.org/10.1787/753542825268

Financial and housing markets are still under pressure

Lending by banks and mortgage credit institutions has continued to slow, reflecting lower demand for loans but probably also caution on the part of financial institutions. They are exposed to significant credit risk as rising unemployment reduces the ability of households to service their debt and falling house prices lower the collateral value of loans. In the third quarter of 2009, financial institutions have continued to tighten credit standards for households and firms but were contemplating easing them somewhat by end-year. As yet, the housing market shows few signs of stabilisation: prices were still falling in the second and third quarters of 2009, albeit at a decreasing pace, and forced sales of real estate rose steeply in the third quarter. However, the number of construction permits has been rising since May.

Policy stimulus is substantial

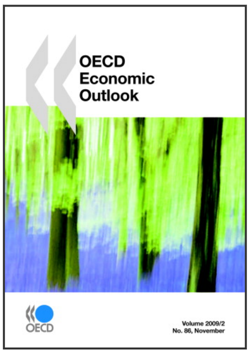
The central bank has continued to lower policy interest rates, thereby reducing the spread *vis-à-vis* the European Central Bank's official interest rates. In addition to the support coming from low interest rates, aggregate demand will be boosted in the second half of 2009 and in 2010 by the effects of tax reform and withdrawals of savings from the special pension scheme. In 2011, some of the temporary stimulatory measures will expire and measures to finance the tax reform are to be introduced. Nonetheless, the government deficit is expected to remain substantial in the near term.

The recovery will also be helped by external demand

After the worst recession since the 1960s, a relatively subdued recovery is projected. Exports are set to be one of its main drivers, against the backdrop of an acceleration in world trade and a further deceleration in wages coupled with a pick-up in productivity. Business investment is also projected to gain momentum in the latter part of 2010 as financial conditions normalise and the uncertainty surrounding the recovery fades. Sustained by the 2010 fiscal stimulus, the fall in unemployment and a turnaround in house prices, private consumption can be expected to regain strength throughout the projection period. Inflation is set to remain subdued as economic slack is worked off only slowly and the output gap remains large in 2011.

There are downside and upside risks

The recovery could be weaker if the housing market fails to stabilise soon despite low interest rates or if financial market conditions normalise more slowly than expected notwithstanding the government's measures to support the banking system. However, an upside surprise cannot be ruled out if monetary and fiscal stimulus were to translate into more robust consumer spending than projected.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