DENMARK

After reaching 2.2% in 2017, GDP growth is projected to return to a pace of 2% in 2018 and 2019, supported by robust domestic demand. Wages and inflation are expected to rise as labour resources become increasingly scarce.

Monetary policy conditions will continue to support demand, especially private investment. A neutral fiscal stance over the projection period is appropriate, given intensifying capacity constraints. Tensions in the labour market should be eased by addressing barriers to employment for immigrants, older workers and those with reduced work capacity.

Financial vulnerabilities stem from very high gross household debt and continued house price increases. House price developments pose risks to future domestic demand, since sustained very low interest rates can fuel a housing bubble in the Copenhagen area. The recent strengthening of macro-prudential policies and reform of property valuation and taxation are welcome. However, the debt-bias in the tax system in favour of housing and credit needs to be lowered.

Domestic demand is broad-based and solid

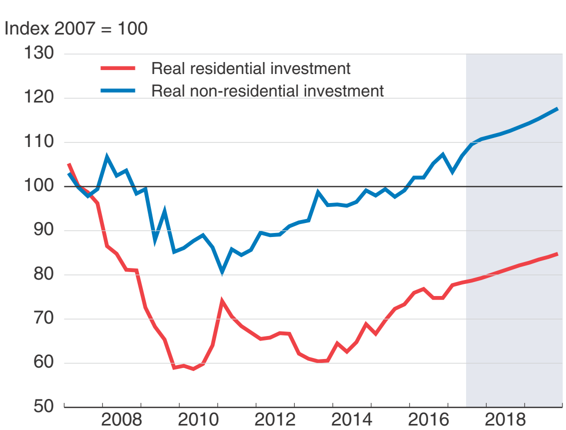
With solid growth over the past two years, the economy is reaching its full potential, sustained by strong household spending and public investment. The unemployment rate has fallen to its estimated structural level and labour shortages are spreading. Inflation has picked up, even though it remains close to that of the euro area. Both consumer and business confidence are relatively upbeat. In line with strengthening external demand, export performance has also improved, notably in services.

Policy needs to limit the risks of over-heating

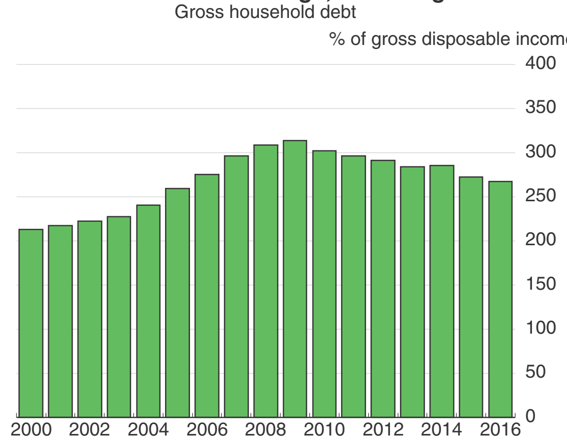
While the fiscal stance is projected to be broadly neutral in both 2018 and 2019, economic growth will be supported by continued expansionary monetary policy

Denmark

Investment continues to pick up



Household debt is high, but falling
Gross household debt



Source: OECD Economic Outlook 102 database.

StatLink http://dx.doi.org/10.1787/888933631437

Denmark: **Demand, output and prices**

	2014	2015	2016	2017	2018	2019
	Current prices DKK billion	Percentage changes, volume (2010 prices)				
GDP at market prices	1 981.2	1.6	2.0	2.2	2.0	2.0
Private consumption	934.3	1.6	2.1	2.3	2.4	2.7
Government consumption	510.9	1.1	0.3	0.5	0.8	0.7
Gross fixed capital formation	379.7	3.1	6.0	3.5	4.1	3.3
Final domestic demand	1 824.9	1.7	2.4	2.1	2.3	2.3
Stockbuilding[1]	18.3	-0.4	0.0	0.1	0.0	0.0
Total domestic demand	1 843.2	1.3	2.4	2.2	2.3	2.3
Exports of goods and services	1 082.0	2.3	2.8	4.5	3.5	3.7
Imports of goods and services	944.0	1.9	3.8	4.7	4.3	4.5
Net exports[1]	138.0	0.4	-0.3	0.1	-0.2	-0.1
Memorandum items						
GDP deflator	_	0.7	0.0	1.8	1.8	2.2
Consumer price index	_	0.5	0.2	1.2	1.6	1.8
Core inflation index[2]	_	1.3	0.7	1.1	1.7	1.8
Unemployment rate (% of labour force)	_	6.2	6.2	5.8	5.7	5.6
Household saving ratio, net (% of disposable income)	_	4.2	4.3	4.9	4.8	4.7
General government financial balance (% of GDP)	_	-1.5	-0.4	-1.3	-1.1	-0.8
General government gross debt (% of GDP)	_	54.2	52.8	53.9	54.8	55.3
General government debt, Maastricht definition (% of GDP)	_	39.5	37.7	38.8	39.7	40.2
Current account balance (% of GDP)	_	8.8	7.3	8.5	8.5	8.6

1. Contributions to changes in real GDP, actual amount in the first column.
2. Consumer price index excluding food and energy.
Source: OECD Economic Outlook 102 database.

StatLink http://dx.doi.org/10.1787/888933632501

conditions. Easy financial conditions could translate into excessive price increases of owner-occupied flats in Copenhagen. Following a recommendation by the Systemic Risk Council, credit conditions have been tightened for borrowers with liabilities above four times their annual income, which will help to stabilise the housing market.

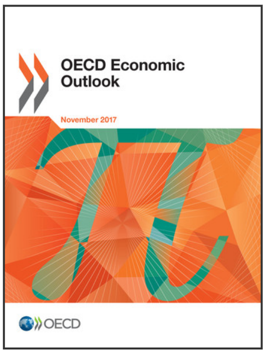
A long-awaited reform of property taxation was approved earlier this year. It should help to stabilise property prices, especially when it becomes fully effective in 2021. The possibility of reducing property taxation again in event of a sustained rise in the property tax revenue as a share of GDP should be abandoned, in order to allow the taxes to damp the housing cycle. Moreover, interest rate deductibility in the tax system could be reduced further.

Sustained employment growth has been helped by recent reforms improving work incentives. To ease tensions in the labour market, addressing barriers to low-wage jobs and disincentives to longer working hours are priorities. Policy action is needed to expand the employment potential of marginalised groups, such as migrants with low language skills or those with reduced work capacity. Enhancing their employability would also improve their inclusion and the distribution of the growth dividend.

Economic expansion will continue at a sustained pace

The economy is projected to maintain GDP growth of around 2% in both 2018 and 2019. Inflation will strengthen to 1.8% in 2019 and increased labour market tightness will translate into faster wage growth. Real disposable income growth will remain robust, sustaining household spending. Business investment is expected to pick up as economic slack disappears. While interest rates will start to rise over the projection period, monetary conditions will remain accommodative.

A tighter-than-projected labour market could stoke wage pressures that would increase household incomes but undermine the competitiveness of Danish exports. Frontloading of residential construction could happen before the recently approved property tax reform takes effect and that could result in temporarily higher economic activity, adding further to the labour shortages in the construction sector. Downside risks are related mainly to unfavourable developments in the main trading partners in Europe.



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