

DENMARK

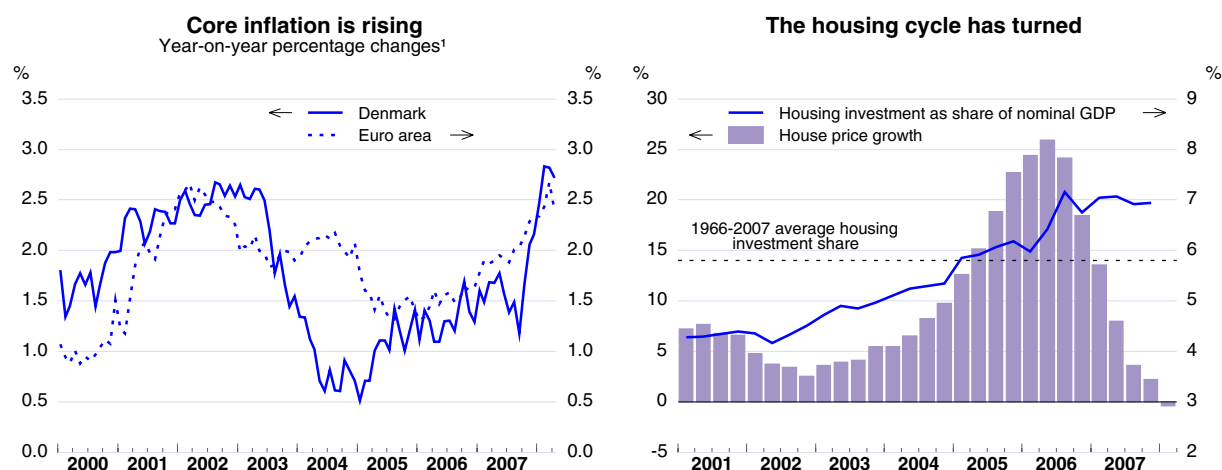
Following a marked slowdown, the economy has expanded at a rate close to potential and the pronounced labour and capacity shortages are easing only gradually. Going forward, construction activity is projected to contract and to drag down growth. Export demand is set to weaken, and households are likely to become more cautious when spending.

With wage and price inflation pressures, fiscal stimulus should be avoided. Rather, policies should continue to focus on expanding labour supply, via clearer incentives for benefit recipients to seek employment and financed reductions in marginal income tax rates.

Capacity pressures remain despite slower growth

Growth has slowed to around its potential rate of 1½ to 2%, leaving the positive output gap previously built up in place. Private consumption expanded rapidly late last year, along with business investment, but much of the additional demand was met by imports. Sentiment about the state of the economy weakened sharply in early 2008, but consumers are more optimistic about their own situation. Business profits are weighed down by rising raw material and labour costs, and sales expectations are weakening. Meanwhile, unemployment has continued to decline, and many firms indicate that they plan to continue hiring. For the private sector as a whole, hourly wage rises have gone up by 1½ percentage points to an annual rate of 4.6% in the final quarter of 2007, and similar rises have been agreed for most of the public sector for 2008-10. With private-sector productivity growth averaging 1½ per cent over the past fifteen years, these wage rises are indicative of some overheating, with a gradual erosion of competitiveness. Consumer price inflation was below 2% in most of 2007, but rose to well above 3% in early 2008, in tandem with the euro area.

Denmark



1. Core inflation excluding unprocessed food and energy.

Source: Eurostat database; OECD Economic Outlook 83 database and Association of Danish Mortgage Banks.

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Denmark: Demand, output and prices

	2004	2005	2006	2007	2008	2009
	Current prices DKK billion	Percentage changes, volume (2000 prices)				
Private consumption	707.2	5.2	3.8	2.5	2.9	1.0
Government consumption	389.0	0.9	2.0	1.7	1.9	1.3
Gross fixed capital formation	282.9	6.2	14.0	6.1	2.2	-1.9
Final domestic demand	1 379.2	4.2	5.4	3.1	2.5	0.4
Stockbuilding ¹	15.6	-0.7	0.6	-0.3	-0.4	0.0
Total domestic demand	1 394.8	3.4	6.0	2.7	2.2	0.4
Exports of goods and services	665.6	8.2	9.0	3.7	3.6	3.6
Imports of goods and services	594.1	11.2	14.1	5.6	5.6	3.2
Net exports ¹	71.4	-0.8	-1.8	-0.8	-1.0	0.2
GDP at market prices	1 466.2	2.5	3.9	1.8	1.2	0.6
GDP deflator	–	3.1	2.0	1.5	3.3	2.4
<i>Memorandum items</i>						
Consumer price index	–	1.8	1.9	1.7	3.3	2.6
Private consumption deflator	–	2.1	2.1	1.9	2.9	2.6
Unemployment rate ²	–	4.8	3.9	3.7	3.3	3.7
Household saving ratio ³	–	-4.0	-3.1	-2.7	-3.2	-2.6
General government financial balance ⁴	–	5.0	4.9	4.5	3.9	3.0
Current account balance ⁴	–	4.3	2.7	1.1	0.6	0.7

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 83 database.

StatLink  <http://dx.doi.org/10.1787/365132605888>

Financial turmoil or not, residential construction is set to contract

Following the spectacular house prices increases and high mortgage debt levels built up over recent years, Denmark would at first glance seem vulnerable to financial turmoil. Yet, so far, none of the major banks has reported significant losses related to bad loans. Mortgage lending standards have tightened and forced sales are becoming more frequent, but the latter still run at only a fifth of the rate observed on average in the 1980s. How much financial stress may yet surface is hard to predict, but in any case construction activity is projected to contract markedly. On the back of rising housing demand, residential investment has accounted for 7% of GDP since 2006, over one percentage point above its 40-year average. The granting of new permits halved during 2006, but with a backlog of dwellings under construction, completions have remained high until now. Residential investment is projected to ease to its historical average by the end of next year, implying a double-digit fall in the volume of residential construction.

With rising inflation fiscal stimulus is undesirable

Unlike many OECD economies, Denmark entered 2008 with a sizeable positive output gap, estimated at 2% of GDP. On top of higher energy and food prices, domestic inflationary pressures will therefore remain strong, even if the Danish economy slows further. A soft landing would require a

gradual increase of unemployment towards equilibrium levels which would be conducive to wage moderation and slow the erosion of cost competitiveness. Fiscal stimulus should be avoided in 2009, with the automatic stabilisers providing enough of a cushion. Public spending should be firmly controlled to avoid a repetition of the 2006-07 overruns, during which time public consumption rose by 2.0% and 1.7%, well above the 0.5% and 1.0% expected by government when presenting the fiscal bill in August of the preceding year. The problem concerns notably municipalities.

Growth is set to slow further but with rising cost pressures

With global financial turmoil lingering, weak export demand is projected to weigh on growth, both this year and next. Business investment is also set to weaken from high levels. Private consumption is expected to grow at a moderate pace, stimulated by wage growth, but tempered by more cautious saving behaviour as housing wealth contracts. Unemployment is projected to rise, but to remain below its estimated structural level, and inflationary pressures will persist. The fiscal surplus should remain large, not least thanks to buoyant revenues from North Sea oil and gas production.

Inflation surprises are a major risk

Global financial turmoil and its international reverberations are casting shadows over the near-term outlook, as are developments in the Danish housing market. Yet, inflation has recently jumped up and may become a major challenge as well.

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This book has...



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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		

Summary of projections

	2007	2008	2009	2009									Fourth quarter		
				2007	2008								2007	2008	2009
				Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2007	2008	2009
Per cent															
Real GDP growth															
United States	2.2	1.2	1.1	0.6	1.0	-0.5	0.7	0.2	1.0	1.4	2.2	3.0	2.5	0.3	1.9
Japan	2.1	1.7	1.5	2.6	3.3	1.1	1.0	1.3	1.6	1.6	1.7	1.7	1.5	1.7	1.6
Euro area	2.6	1.7	1.4	1.2	3.1	0.2	1.1	1.2	1.4	1.7	1.8	1.9	2.1	1.4	1.7
Total OECD	2.7	1.8	1.7	1.7	2.1	0.5	1.2	1.2	1.7	2.0	2.4	2.7	2.6	1.3	2.2
Inflation ¹															
United States	2.5	3.2	2.0	3.9	3.5	3.6	2.4	2.0	1.8	1.7	1.6	1.6	3.4	2.9	1.6
Japan	0.1	0.9	0.4	1.6	1.2	0.6	0.3	0.3	0.3	0.4	0.5	0.6	0.5	0.6	0.5
Euro area	2.1	3.4	2.4	4.8	4.2	3.3	2.6	2.4	2.3	2.2	2.1	2.0	2.9	3.1	2.1
Total OECD	2.2	3.0	2.1	3.5	3.4	3.2	2.5	2.3	2.0	1.9	1.8	1.8	2.8	2.8	1.9
Unemployment rate ²															
United States	4.6	5.4	6.1	4.8	4.9	5.2	5.5	5.8	6.0	6.2	6.2	6.1	4.8	5.8	6.1
Japan	3.9	3.8	3.8	3.9	3.8	3.8	3.8	3.9	3.9	3.8	3.7	3.7	3.9	3.9	3.7
Euro area	7.4	7.2	7.4	7.1	7.1	7.2	7.2	7.3	7.4	7.4	7.5	7.5	7.1	7.3	7.5
Total OECD	5.6	5.7	6.0	5.5	5.6	5.7	5.7	5.9	6.0	6.0	6.0	6.0	5.5	5.9	6.0
World trade growth															
	7.1	6.3	6.6	4.8	6.5	6.1	6.1	6.3	6.6	6.9	7.0	7.1	7.2	6.2	6.9
Current account balance ³															
United States	-5.3	-5.0	-4.4												
Japan	4.8	4.4	4.4												
Euro area	0.2	0.1	0.0												
Total OECD	-1.4	-1.3	-1.1												
Cyclically-adjusted fiscal balance ⁴															
United States	-3.2	-5.2	-4.4												
Japan	-2.6	-1.6	-2.5												
Euro area	-0.7	-1.0	-0.8												
Total OECD	-2.0	-2.8	-2.5												
Short-term interest rate															
United States	5.3	2.7	3.1	5.0	3.2	2.6	2.6	2.5	2.3	2.6	3.4	4.0			
Japan	0.7	0.8	0.7	0.8	0.8	0.9	0.9	0.8	0.7	0.7	0.8	0.8			
Euro area	4.3	4.5	4.1	4.7	4.5	4.5	4.5	4.4	4.2	4.1	4.1	4.1			

Note: Real GDP growth, inflation (measured by the increase in the consumer price index or private consumption deflator for total OECD) and world trade growth (the arithmetic average of world merchandise import and export volumes) are seasonally and working-day-adjusted annual rates. The "fourth quarter" columns are expressed in year-on-year growth rates where appropriate and in levels otherwise. Interest rates are for the United States: 3-month eurodollar deposit; Japan: 3-month certificate of deposits; euro area: 3-month interbank rate.

Assumptions underlying the projections include:

- no change in actual and announced fiscal policies;

- unchanged exchange rates as from 13 May 2008; in particular 1\$ = 104.44 yen and 0.64 € ;

The cut-off date for other information used in the compilation of the projections is 23 May 2008.

1. USA; price index for personal consumption expenditure, Japan; consumer price index and the euro area; harmonised index of consumer prices.

2. Per cent of the labour force.

3. Per cent of GDP.

4. Per cent of potential GDP.

Source: OECD Economic Outlook 83 database.



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