

## DENMARK

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## UNCERTAINTY REMAINS

The Danish economy has quickly rebounded after the reopening of the borders but a complete catch-up will take time since the resurgence of the Coronavirus epidemic keeps the country's economic situation uncertain. Services exports were hard hit by the crisis in 2020, but are offset by a surge in Danish household consumption, supported by government measures. Fiscal policy should remain accommodative in 2021 and the Central Bank of Denmark will continue to defend its peg with the euro.

Danish GDP rebounded by 4.9% (q/q) in the third quarter of 2020, but failed to compensate the Q2 sharp fall of 7% (q/q). GDP is expected to contract by 3.9% over the year. In 2021, growth is expected to rebound by 3.5% according to the European Commission estimates. However, new measures to fight the Covid-19 pandemic and a weaker external environment could undermine the recovery.

## HOUSEHOLDS REGAIN CONFIDENCE

The Danish economy's recovery depends on the resumption of world trade. Since the beginning of the crisis, services exports have been hit hard, falling by 11.6% in Q2 2020, mainly due to the absence of foreign tourists. The rebound in Q3 (+5.6%) is far from sufficient to allow exports to return to their 2019 level. In addition, the prospect of a hard Brexit could add an additional drag, as the UK is the Denmark's fourth largest trading partner.

After falling by 6.38% (q/q) in Q2 2020 and despite a rebound of 3.3% (t/t) in Q3, business investment is unlikely to return to its pre-crisis level until a vaccine is widely spread in 2021. The second wave of the Covid-19 pandemic eroded the confidence of business leaders which remains low in Q4 (the manufacturing PMI in November reached 47.7) and is unlikely to improve in H1 2021. The housing market has rebounded strongly since the end of June, and real-estate prices have risen above pre-crisis levels<sup>1</sup>.

Household consumption has picked up rapidly since the end of the first lockdown in March 2020 and recovered to pre-crisis levels as of June 2020. It should therefore decline by only 2% in 2020 and increase by 4% in 2021. This optimism among households is expected to continue thanks to government support measures to consumption and labour market resilience<sup>2</sup>. Part of the special pension scheme was paid to households in October, which triggered an increase in their incomes amounting 2.6% of GDP. Moreover, the recovery of consumption would increase price volatility in 2021.

During lockdown in April and May 2020, inflation dropped to 0% before rising to 0.2% in October 2020. This sharp slowdown is due to a deep drop in oil prices. It would have been even more pronounced without the introduction of an additional tax on tobacco in April<sup>3</sup>. Inflation is expected to accelerate in 2021, to nearly 1%. The central bank's top priority is to protect the DKK peg to the euro, which was threatened as the Danish krone has regularly exceeded the peg (EUR 0.1340 against DKK 1). The central bank said it is open to massive selling of DKK to defend its value. The key policy rate was cut by 15bp to -0.6% in March 2020 and is unlikely to be lowered again in 2021.

<sup>1</sup> House prices rose 4.3% in Q3 2020, compared to 3.6% in Q4 2019.

<sup>2</sup> The labour market participation rate dropped 3% during the first lockdown, but half of it was recovered by August 2020.

<sup>3</sup> The price of a pack of cigarettes increased 24% in April following the introduction of a tobacco tax, rising from DKK41 to DKK55 a pack. The price will rise to DKK60 in January 2022.

## GROWTH AND INFLATION (%)

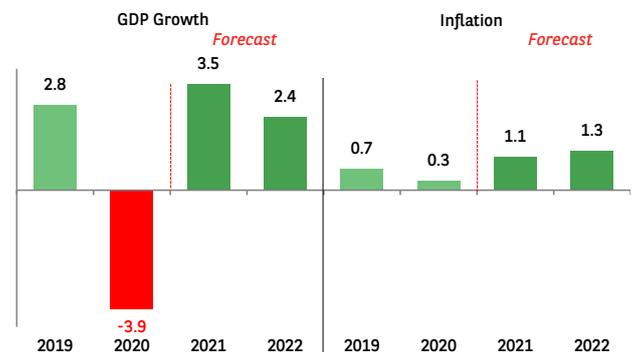


CHART 1

SOURCE: EUROPEAN COMMISSION, BNP PARIBAS

In H2 2020, the government rapidly replaced the broad subsidy programmes of the first lockdown with more targeted measures aiming at companies forced to shut down and their employees. Fiscal policy should still remain expansionist in 2021 and 2022 and will continue to widen the fiscal deficit, which will probably swell to 3.4% of GDP in 2020. Over the DKK 66 billion in government loans guarantees made available to companies in 2020, only DKK 4.8 billion were claimed. The remaining amounts could therefore still be granted to companies facing difficulties in 2021. Large training programmes will also be launched. The agenda for structural reforms, and for the ecological transition in particular, will be maintained in 2021 and 2022.

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