

DANMARKS NATIONALBANK'S COMMENT ON THE DANISH ECONOMIC COUNCIL'S DISCUSSION PAPER, AUTUMN 2017

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Overall, Danmarks Nationalbank shares the Chairmanship's view of the economic situation. The Danish economy is in a broadly balanced cyclical position and heading towards a boom. The Chairmanship's assessment of how strong growth will be in the coming years remains a little higher than Danmarks Nationalbank's. This reflects a more optimistic view of how strong structural productivity growth will be.

It is essential to tackle the boom in such a way that large imbalances do not build up. Historically, things have gone wrong on a number of occasions. So far, the current upswing has been more balanced than the one we saw in the mid-2000s. Growth in employment rests on a more solid foundation as it is to a larger extent supported by an increasing structural labour force, reflecting factors such as the retirement reforms introduced some years ago. Furthermore, there are no signs of overheating of the housing market overall, credit growth remains low and wage inflation is moderate. However, there are still clearer signs of mounting labour market pressures, and parts of the housing market are heated.

At 8-9 per cent of GDP, the current account surplus is very large. So there is room to let imports cover part of the growth in demand and for a slightly higher rate of wage increase, which will ease the pressure on the labour market. The large current account surplus is presumably to some extent of a temporary nature and attributable to households exercising restraint and continuing to consolidate.

Danmarks Nationalbank agrees with the Chairmanship that it is important not to ease the fiscal policy stance in connection with the negotiations on the 2018 Finance Act and Job Reform II etc. In the current cyclical position, fiscal policy should not fuel demand further. Instead, it should help to prevent demand from rising too much above the level that capacity can sustain. Danmarks Nationalbank's recommendation is that the government should be prepared to step in and tighten fiscal policy with a view to dampening growth in demand.

The Chairmanship underscores that there is a risk that rising demand in the housing market will push prices up to a higher level than warranted by underlying factors such as interest rates and incomes. Danmarks Nationalbank's analyses show that housing prices in Copenhagen have reached a level

that cannot be explained by developments in interest rates and disposable income. The sustained high rate of increase in Copenhagen and Aarhus gives cause for concern.

The report includes an interesting analysis of how shifts between industries can affect long-term growth. That will be the case if industries with low productivity growth begin to play a larger role in the economy. The conclusion is that Denmark has not seen such shifts yet, but that they will presumably occur. If we also take into account the demographic headwinds awaiting us in the coming decades, there are strong indications that underlying GDP growth can be expected to be lower than in the preceding decades.

The report also concludes that shifts between industries made a positive contribution to productivity growth in the overall market-related economy in the period 1966-2013. This conclusion entails that the lower productivity growth seen in Denmark in recent decades is mainly attributable to a fall in productivity growth *within* sectors of the economy. It is found that there is a tendency for the contribution to productivity growth from shifts between industries to have become smaller over time and even marginally negative in the last few years. This is in tune with analyses performed by Danmarks Nationalbank. Growth in productivity in Denmark is broad-based and is not driven by a small group of high-productivity firms. However, substantial differences can be found within the same industry.