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THE GREENLANDIC ECONOMY

Strong growth, but reforms are required



Strong labour market pressures

Good fishing opportunities at high prices are the main reasons for the strong economic growth. The potential for raw material extraction and tourism is still waiting to be fulfilled. Unemployment is very low and labour market pressures high.



Airport projects will increase pressures

Large-scale investments are being made in three airports. The aim is to improve the infrastructure and business opportunities. These construction projects will increase pressures in the economy, with a risk that other projects are postponed or become considerably more expensive than anticipated.



Independence and industrial policies

The wish for greater independence combined with a high standard of living is difficult to realise. Among other things, it requires a broader business sector and focus on efficiency and sustainability in both the public and private sectors. The latter entails that all fisheries become sustainable and that public finances take strong fluctuations in revenue from fisheries into account.

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The favourable trend in the Greenlandic economy continues, with rising incomes and employment. This is mainly attributable to larger catches of fish and shellfish that have sold at good prices, but consumption and investment have also picked up in both the private and public sectors.

Large-scale airport investments will be made in the coming years. That will increase the risk that the economy overheats. In 2014-17, real economic growth was just under 2.5 per cent p.a. In its report from October, the Economic Council in Greenland forecasts that growth in the gross domestic product, GDP, increased to 3.6 per cent in 2018 and will be around 2.2 per cent in 2019, rising to 3.8 per cent in 2020, see Table 1.

The booming economy has led to labour shortages in many sectors and geographical areas. Unemployment figures are compiled with a lag, but based on the indicators available, the Economic Council has calculated that unemployment – calculated in more or less the same way as in Denmark – has dropped from more than 10 per cent of the labour force in 2014 to less than 4 per cent in 2019. In many cases, it has been sought to counter the labour shortage by attracting foreign labour, including unskilled labour.

Public finances reflect the favourable cyclical position, with increased revenue from direct and indirect taxes. With 2014 as an exception, recent years have seen surpluses on the current and investment balance, even though budgets have generally operated with equilibrium.

The government of Greenland and its predecessor, the home rule, have for many years been careful not to accumulate too much government debt. Hence, the debt-to-GDP ratio has been shrinking. At end-2018, the government, local government and government-owned companies had interest-bearing gross debt totalling approximately 19 per cent of GDP, while interest-bearing net debt was approximately 5 per cent. By comparison, Denmark's EMU debt, which comprises more or less the same elements as the interest-bearing gross debt, was 34 per cent of GDP.

Facts about Greenland

Box 1

Currency	Danish kroner
Population (number of people, beginning of 2019)	55,992
of which in Nuuk (capital)	17,984
Population aged 18-65 years	36,584
Employment ¹ (2017)	24,922
Unemployment ² (2017)	1,858
GDP (kr. billion, 2017)	18.5
per capita ³ (kr. 1,000)	331.2

Source: Statistics Greenland, Statistics Denmark and own calculations.

1. Average of monthly data.
2. Approximated OECD definition, average of monthly data.
3. By comparison, GDP per capita in Denmark was approximately kr. 377,700 in 2017.

Outlook for further growth in the Greenlandic economy

Table 1

	2013	2014	2015	2016 ¹	2017 ¹	2018 ²	2019 ²	2020 ²
GDP	-1.3	4.7	-2.5	6.0	1.0	3.6	2.2	3.8
Imports of goods and services	-6.6	-11.5	1.7	8.2	-5.5	7.3	21.1	-2.6
Total utilities	-3.4	-1.2	-1.1	6.7	-1.0	4.8	8.6	1.4
Private consumption	-1.1	0.6	0.2	1.2	2.4	2.4	2.6	2.6
Public consumption	4.1	-0.2	-0.6	1.5	3.5	1.8	0.7	0.7
Gross investment	-20.7	-21.9	10.2	9.3	-2.9	5.9	37.7	0.6
of which exploration for raw materials	-49.2	-52.7	44.5	-46.8	-36.8	31.8	17.8	6.5
of which buildings and structures	-21.1	-11.0	19.7	9.8	-0.4	3.3	11.1	34.5
Exports of goods and services	2.4	11.8	-9.9	16.9	-7.6	11.3	4.5	1.6

Note: Demand and supply, annual real growth in per cent.

Source: Statistics Greenland and Economic Council.

¹ Preliminary data.

² The Economic Council's forecasts.

Good fishing opportunities at high prices

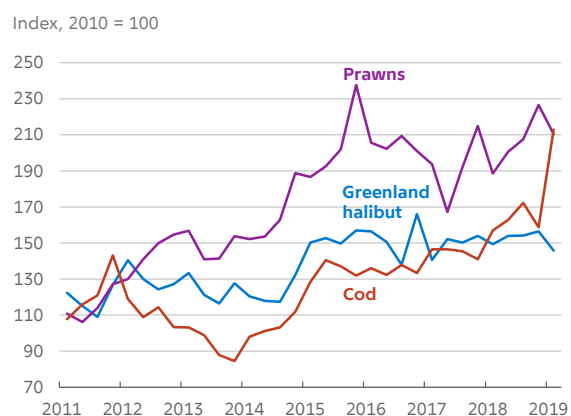
The current upswing has been generated by growth in catches and processing of fish and shellfish. Fisheries is the predominant Greenlandic export industry. Around 95 per cent of exports of goods stem from fisheries, of which almost half from prawns, making this the economically most important species in Greenlandic fisheries.

For some years, *prawn* prices have been relatively stable at a level which is twice as high as the price level in 2010, see Chart 1.

At the same time, catches of prawns have picked up since the trough in 2015, see Chart 2. In 2018, catches rose by 10 per cent compared with the 2017 level, and this trend continued unabated in the 1st half of 2019. Prawn fishing has been MSC certified as sustainable, which is a requirement for selling to many of the large purchasers of fish and shellfish. This certification means that, with small variations, the politically fixed quotas comply with biological advice and hence the latest knowledge about the level of fishing that is sustainable in the long run.

High fish prices

Chart 1



Note: The most recent observations are from the 1st quarter of 2019.

Source: Statistics Greenland.

Greenland halibut is the second most important species in Greenland. It is caught both in open seas and close to the coast. Like prawn fishing, fishing in open seas has been MSC certified. Coastal fishing, which is not MSC certified, takes place from small, open boats – and in the winter also from snow scooters and dog sledges. Coastal fishing is of great importance to many local communities, especially in the Disko Bay and areas further north. The size of the coastal quotas has a direct impact on many households and is consequently a matter of political sensitivity, presumably even more so after the number of licences issued has increased strongly.

In 2018, catches of Greenland halibut in Greenlandic waters rose by 15 per cent, following an equivalent decline in 2017. This was mainly attributable to a very severe winter that year. In the 1st half of 2019, catches were a little higher than in the corresponding period of 2018.

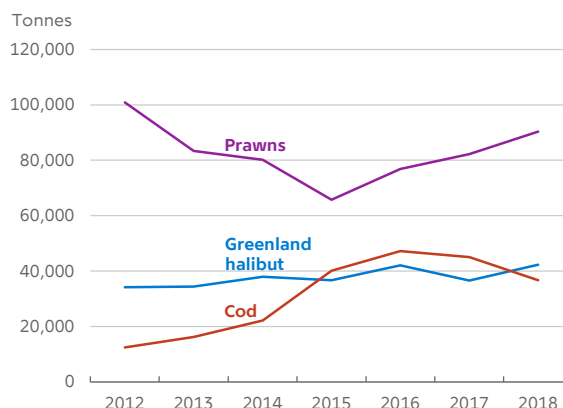
Stocks of Greenland halibut show diverging trends in open seas and coastal waters. Biological advice for 2019 concerning fishing in open seas in the Davis Strait and Baffin Bay increased by more than 10 per cent, while advice concerning coastal areas was reduced by 10-20 per cent, depending on the area. In most coastal areas, the fish caught are getting smaller year by year, which the biologists see as a sure sign that fishing intensity is too high. Naalakkersuisut, the government of Greenland, has expressed concerns about this development and announced that it will bring quotas closer to the advised levels over a number of years. However, in the short term it has taken another path. Since the 2019 quotas for the Disko Bay had almost been depleted in early September, quotas were increased to support employment.

Catches of *cod* fell by 19 per cent in 2018, having risen continuously for a number of years until 2016. Throughout the period, catches have exceeded the biological advice, which is aimed at ensuring the build-up of spawning stocks. Catches have continued to fall in 2019.

All in all, fisheries are increasing, and prices are good. The good earnings mean that the open-seas fleet is being modernised via imports in 2019, presumably of six new trawlers at prices exceeding hundreds of million kr. each. These trawlers are the main factor behind the large increases in investments and imports in 2019, see Table 1.

Catches are increasing

Chart 2



Source: Statistics Greenland.

There is a tendency to overfish in areas that are not MSC certified. As a result, the outlook for future fisheries is obviously mixed. If fishing is to be reduced in some geographical areas, employment in the sector will fall. However, the current labour shortage means that it will be possible for many people to find employment in other sectors if they stop fishing.

Fisheries commission and resource taxes

A large political majority has supported the establishment of a fisheries commission. This commission has been broadly composed, with a lawyer as its chairman, two independent members with insight into fisheries economy and management and nine members from industry and organisations. The terms of reference from March 2019 state, inter alia, that the commission's proposals must be aimed at achieving "the greatest possible long-term economic gain from fishing on a sustainable basis". This also means that fishing must be biologically sustainable in future, with a balance between the capacity of the fleet and its fishing opportunities in the longer term. The commission is expected to complete its work in June 2020 so that Naalakkersuisut can present a bill for reading in the autumn of 2020.

Greenland is a global pioneer when it comes to taxing catches of fish and shellfish. The resource taxes

are designed in such a way that the rate payable per kilo caught varies with the market price of the product. The higher the price, the higher the tax payable by all sector participants. The current rate, which is also the highest possible rate, is 17.9 per cent and applies so long as the export price for a product exceeds kr. 29 per kilo. If the export price falls below kr. 17 per kilo, the tax rate falls to 5 per cent. So if prices are high, the tax ensures that the whole society benefits from the higher-than-normal earnings, reflecting that society has granted a vessel permission to fish a certain volume of a limited natural resource. Besides the resource tax, participants pay ordinary taxes on the vessel's profit after deduction of the resource tax, and likewise employees are taxed in the same way as other wage earners.

The favourable trend in fisheries over the last few years means that revenue from resource taxes has risen from kr. 22 million in 2010 to kr. 425 million in 2018. Last year's resource taxes made up 18 per cent of the government's revenue from direct and indirect taxes – and 6 per cent of total revenue.

Hence, the resource taxes have become an extremely important source of revenue for Greenland. This means that public finances have become increasingly dependent on the prices of fish and shellfish remaining high. These prices are determined in the global market.

The Economic Council has calculated the impact on public finances in 2018, had prices been 20 per cent lower than they actually were and catch volumes unchanged. The result was that government revenue would have been kr. 232 million lower. This amount includes not only kr. 113 million less in resource taxes, but also the immediate fall in corporate and income taxes. However, the derived consequences of a weaker economy on consumption, investments and fisheries-related sectors have not been taken into account. Against that background, it is clear that the realised surplus of kr. 133 million on the current and investment account in 2018 would have made way for a sizeable deficit, had the price fall been a reality. In other words, the government finances are very vulnerable to catch volumes and prices for fish and shellfish. This dependence is simply a fundamental condition in the Greenlandic economy.

If developments in fisheries are unfavourable, there is a considerable risk that economic policy must

be tightened – either by raising direct and indirect taxes or by cutting down on some of the major expenditure items. This scenario can be countered by building up buffers while prices are high, as they are at present. Price falls of the – hypothetical – size mentioned above are by no means unprecedented, but right now there are no indications that prices will drop sharply.

The Economic Council has also calculated that it will be necessary permanently to strengthen public finances by around kr. 1 billion p.a. for the next 10-15 years in order to ensure their sustainability. This fiscal sustainability problem still needs to be tackled. It would be prudent to build up reserves in these years when fisheries are booming and employment is high.

Business development and increased independence

There is a widespread wish in Greenland for greater independence from Denmark without a marked decrease in the standard of living. Among other things, the Act on Greenland Self-Government describes the functions that are undertaken by the Danish government and can be transferred to the Greenlandic government. These are primarily police, justice and defence. The Danish government bears the costs in the areas which have not been taken over by Greenland, but which could be taken over – amounting to around kr. 1 billion p.a. If an area is transferred to the Greenlandic government, this will not affect the subsidy from Denmark to Greenland, the block grant. However, the grant will be reduced if revenue from raw material extraction at some point exceeds a certain threshold value.

Given that the block grant constitutes just over half of the Greenlandic government's total revenue, other revenue must increase considerably if the wish to become independent of the block grant is to come true. This can seem impossible. Without large revenues from raw materials, this will, as a minimum, require a broader business sector than at present and higher efficiency in both the public and private sectors. The public sector accounts for a very large share of the economy. In 2017, public consumption accounted for 43 per cent of GDP, compared with 25 per cent in Denmark. Obviously, this share must fall,

and so must public sector employment as a result. If a corresponding number of private sector jobs are to be created at the Greenlandic wage level, which is high by international standards, the labour force must be highly skilled. However, some steps have been taken towards creating a broader business sector.

After some years without raw material extraction, there are now two active mine projects, extracting rubies and aluminium oxide (anorthosite), respectively. Each project employs approximately 30 people. During 2020, the closed gold mine in South Greenland is also expected to reopen for a few years.

A number of other raw material projects are also approaching the extraction stage. They make valuable contributions to a more diversified business structure, but will not in themselves be able to replace the block grant.

Exploration for raw materials is also increasing, but remains at a far lower level than in the years around 2010, when especially one UK company spent billions of kroner on test drillings for oil in the sea west of Greenland.

The potential to increase tourism in Greenland is considerable, and large-scale private sector investments are being made in hotel capacity and other facilities with a view to exploiting the opportunities arising when the airports in Nuuk and Ilulissat are ready, presumably in 2023, see the section on airports below. The potential must be said to be large, but it has not been realised in recent years. In fact, growth in the numbers of foreign hotel guests, air passengers and cruise guests has been non-existent or modest.

Qualifications of the labour force

At any rate, there is a need to increase the supply of qualified labour so as to reduce the need for imported labour. This will increase productivity and income per permanent resident in Greenland.

If this need is to be met, it will require a large-scale educational effort right from the school or pre-school level, as well as an increase in the number of hours each person works per year.

As regards the latter, the Economic Council has pointed out that for many people the relationship between an increase in earned income and the resultant taxation and scaling down of social benefits means that, for a large income interval, disposable income hardly rises even though people work more.

High qualifications and adaptability are required for a number of existing jobs, and that will undoubtedly also apply to many future jobs. There is some way to go before Greenlandic labour can fill most of the expected jobs within mining and tourism.

The foundation for boosting the qualifications of the labour force must be laid in the schools. Greenland already spends many resources on its schools, so it is a question of ensuring a good return on the resources spent rather than increasing spending.

New airports and their funding

The transport structure to and from Greenland and domestically differs fundamentally from those seen in most other countries.

Today, all passenger transport to and from Greenland takes place by air, and flying is also the dominant form of domestic transport, except over short distances, where sailing also plays a role. No roads exist between the individual towns and settlements, and the considerable distances between the inhabited areas, combined with deep fjords, mountains and a cold climate, rule out the option of linking the country via roads. So it is evident that the location and size of the airports, as well as the flight schedules, are of great interest and can easily lead to conflicts between different regions.

Nearly all travellers to and from Greenland pass through the airport at Kangerlussuaq and transfer to smaller aircraft for their final destinations, in some cases with stops en route. Only few passengers have Kangerlussuaq as their final destination. The airport, which was constructed by the Americans for military purposes in 1941, has sufficiently long runways to cater for practically all aircraft. It is very seldom closed due to adverse weather conditions.

For a number of years, an expansion of the airport at Nuuk has been considered so as to allow non-stop

flights from Europe to Nuuk, where most passengers are heading. However, other regions of Greenland have had concerns about this solution.

Against that background, Inatsisartut, the parliament of Greenland, in 2015 made a decision in principle to modernise the infrastructure and strengthen business development in Greenland.

Following a lengthy process, it was decided to extend the runways at Nuuk (Central Greenland) and Ilulissat (North Greenland) to 2,200 metres and build a new airport of 1,500 metres at Qaqortoq (South Greenland). This will make it possible to fly from Europe to the first two destinations with most aircraft types, thereby bringing most business travellers directly to Nuuk and most tourists directly to Ilulissat. Total investments were forecast at approximately kr. 4 billion, which is more or less half of the Greenlandic government's total annual revenue.

The airports were to be funded via a capital injection of almost kr. 2.1 billion into a 100 per cent government-owned company, supplemented with government-guaranteed loans for another kr. 2 billion or so.

Hence, the project entailed a substantial financial risk for the Greenlandic government. The profitability of the overall project with three airports was doubtful and if the assumptions failed, the government would bear a large risk relative to both the size of the economy and government revenue.

Against that background, Naalakkersuisut and the Danish government in September 2018 concluded an agreement in principle to the effect that Denmark will help to boost business development in Greenland, inter alia via Danish contributions to the funding of the required airport structure.

To fund the airports at Nuuk and Ilulissat, the Danish government has agreed to contribute kr. 700 million in equity to the company Kalaallit Airports International A/S in addition to the kr. 1,400 million from the Greenlandic government. Furthermore, the Danish government will provide guarantees for loans of kr. 450 million to the company and grant the company on-lending for the same amount. The Danish government is not involved in the funding of the airport at Qaqortoq.

This agreement reduces the Greenlandic government's risk and borrowing requirement, as well as

Airport locations

Chart 3



Note: The red crosses indicate the airports mentioned in the text.

the interest payable on the loans to be raised.

In addition, the Greenlandic government is thinking of building small airports in seven towns now serviced by helicopters. The Finance Bill for 2020 includes funding for preliminary studies with a view to making a political decision in the autumn of 2020.

A special issue in relation to the discussion of the future international airports has been whether the airport at Kangerlussuaq is to be rebuilt as a heliport; as a 1,500 metre runway, entailing that the end of the runway where the problems with shrinking permafrost are most pronounced will be closed; or whether a longer runway should be preserved. In September 2019, the Danish government and Naalakkersuisut concluded an agreement in principle to the effect that the armed forces' need to use the airport at Kangerlussuaq is safeguarded, but at the same time it must still be possible to use the airport for civil traffic. The detailed terms and conditions are to be agreed between Naalakkersuisut and the Danish government.

Construction work in Nuuk and Ilulissat is scheduled to begin in the autumn of 2019. Labour will primarily come from abroad as spare capacity in the Greenlandic construction industry is insufficient at the moment. There is a considerable risk that the construction projects will lead to price increases for, or postponement of, other projects.

ABOUT ANALYSIS



As a consequence of Danmarks Nationalbank's role in society we conduct analyses of economic and financial conditions.

Analyses are published continuously and include e.g. assessments of the current cyclical position and the financial stability.

The analysis consists of a Danish, a Greenlandic and an English version. In case of doubt regarding the correctness of the translation the Danish version is considered to be binding.

DANMARKS NATIONALBANK
HAVNEGADE 5
DK-1093 COPENHAGEN K
WWW.NATIONALBANKEN.DK

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Anders Møller Christensen
Advisor

ECONOMICS AND MONETARY
POLICY



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