

CHECK AGAINST DELIVERY

Introduction

December is a month of tradition – a month when predictability reigns with Christmas lights, Christmas trees and rituals.

For many years, we may have thought the same thing about globalisation – a stable and almost obvious tradition. However, we can no longer count on globalisation as a fixed backdrop. I would like to talk about that today.

When I stood here last year, inflation was the most important macroeconomic issue. Today, inflation is under control and the economy is well balanced.

But unforeseen shocks to the economy and our everyday lives can occur quickly, as we have experienced in recent years.

Think of the pandemic, when Denmark was locked down. From one day to the next we could not buy various goods because major international ports were closed or factory workers had been sent home. Or Russia's war in Ukraine, which caused the price of energy to rise rapidly and dramatically.

And I guess we are now in a situation where we are all unsure of what is going to happen in the coming years. As a result of wars, signs of disruption in international trade and other factors, we now face the risk of an increasingly polarised world.

What we also call geoeconomic fragmentation.

*****Geoeconomic fragmentation*****

Geopolitics is affecting your customers' everyday lives in a way we probably have not seen since the Cold War.

Trade barriers are on the rise, and many companies are considering moving production closer to their headquarters.

There are also clear signs that some countries are trading less with each other today due to conflicting political interests.

We can see this, for example, if we consider the world as two blocs centred around the EU and the US on one hand and China and Russia on the other. If we compare the period before the war in Ukraine with now, trade growth between the blocs has decreased significantly more than trade within the blocs.

Globalisation has also led to a marked specialisation of certain products. This means that in some cases production is concentrated in just a few countries.

While this has economic benefits, it also poses a significant risk. When we become dependent on specific countries for strategically important goods, we create vulnerability in our supply chains.

And we must not be blind to the fact that in a more unstable world, there may be good reasons from a security perspective why we in the EU, for example, should be able to produce more of the energy we need ourselves. Or reduce our dependence on individual countries for raw materials and products that are important in many sectors.

However, this must not become an excuse for classic protectionism and broad-based government subsidies. And our analyses show that small open economies are particularly vulnerable to such developments.

*****The single market, globalisation and the Danish economy *****

We must always be aware of the benefits that Denmark has gained from globalisation.

Many Danish companies have excelled at taking advantage of globalisation, and in several sectors they have become leaders in the world market.

At the same time, access to cheap imports has helped keep price increases down. It has also benefited employment, among other things.

Globalisation has helped increase productivity by allowing companies to locate their production where it is most efficient.

At the same time, technological advances and innovation have spread faster globally because countries and companies have had to adapt to global competition.

But if government subsidies and other trade barriers become more widespread it will reduce efficiency, increase costs and hinder innovation.

All in all, this will result in lower productivity and real economic growth, both here in Denmark and globally.

This is in a reality where productivity in the EU is challenged and where factors such as demographics and the green transition are already contributing to low structural growth in the coming years.

The so-called Draghi report contains many relevant proposals on what Europe needs to do to become more productive and competitive vis-à-vis the US and China.

I would like to emphasise one proposal in particular. It is not that extraordinary, but it has great potential.

The proposal is about improving the EU single market.

We must remember that every time a Member State has special rules in the EU, it has an economic cost. What we economists call negative externalities.

The International Monetary Fund, IMF, has found that trade costs within the EU are equivalent to an ad valorem tax of 44 per cent. The interstate trade costs in the US are equivalent to an ad valorem tax of 15 per cent.

But removing barriers in the single market is a long haul. It is not a quick and easy solution.

That is why it is crucial that the European Commission drives the agenda forward and that the Member States support it – even when things get difficult and national approaches need to be adjusted.

*****Cybersecurity*****

Geopolitical tensions have also increased the cyber threat to our society. Because the criminals are now more likely to be, or be supported by, state actors. They have far more sophisticated skills. And destructive goals in mind.

Denmark is among the most digitised countries in the world. And with digitalisation comes increased vulnerability to cyberattacks.

We can see this, for example, from the results of a survey by the European Banking Authority, EBA.

About a quarter of the European banks surveyed experienced cyberattacks in the second half of 2023 that led to a serious operational incident. The year before, it was about a tenth of the banks.

Recently, we have also seen a number of denial-of-service attacks against Nordic banks' websites. Attacks that, in strength and complexity, surpass anything we have seen before.

This is a disruptive element within individual banks and for their customers. However, what really concerns me are serious cyberattacks that cause significant damage to societally critical functions and can threaten financial stability.

I know you all have a sharp focus on cyber, and I am pleased to see that cyber maturity has improved over time. The Centre for Cyber Security also stresses that the financial sector is mature when it comes to cybersecurity.

At Danmarks Nationalbank, we are very pleased with our joint work on cyber risks in the FSOR collaboration, in which a number of you sitting here today are also active participants. And many of the rest of you are represented by your data centres.

This broad and close collaboration across authorities and private actors is also a source of inspiration for other countries and organisations.

But it is vital that we continuously work to increase cyber resilience. Not only in terms of preventive measures to counter cyberattacks, but also in terms of measures that ensure the ability to continue critical business activities after a serious cyberattack.

*****Payments infrastructure*****

The geopolitical situation means that we need to consider how citizens' daily payments can be maintained in situations such as during internet outages.

The members of the Danish Payments Council, including Finance Denmark, have therefore assumed responsibility for developing a digital payment contingency measure involving payment cards.

The aim is to ensure that citizens can use their Dankort and Visa and Mastercard payment cards to buy groceries and medicines among other things, even if the internet is down.

This has required close collaboration between several actors to make a number of necessary adjustments to systems and rules related to the use of payment cards.

The contingency measure is expected to be fully rolled out to the majority of grocery stores and pharmacies by early 2025.

But the Danish Payments Council is aware that the work on the card payment contingency measure does not end here.

The next step for the members of the Danish Payments Council will be to ensure that the contingency measure is tested regularly to ensure that it is robust and works effectively in the event of a crisis.

In four to five months we will join the pan-European payments infrastructure, TARGET Services. This means, among other things, joining forces with the euro countries in a common front against cyber threats.

This is a huge investment for both you in the sector and for Danmarks Nationalbank, and the collaboration has been very successful.

The other Nordic central banks also see TARGET Services as a future possibility. This means we can look forward to strong and increased Nordic and European collaboration on a common payments infrastructure with increased joint innovation in mind.

The TIPS cross-currency project is one such example. Here, Danmarks Nationalbank is working with the ECB and Sveriges Riksbank to enable instant cross-currency payments on the common TIPS platform. The project will allow banks to develop new and improved solutions for settling cross-border payments.

I therefore encourage the banks to actively participate in the project. Together, we must achieve a solution that offers easy and efficient settlement of these payments while meeting the EU requirements that banks face.

All with the aim of ensuring that Danish citizens continue to have access to secure and efficient payments in the future.

*****State of the financial sector*****

Let me say a few words about the state of the financial sector.

You still have high profits at the banks. Higher interest rates in 2022 and 2023 have contributed to a significant increase in net interest income, while you have experienced very few losses on your customers.

The limited losses are largely due to the fact that the soft landing in the economy has become a reality. For businesses, the financial statements generally reveal a moderate increase in profits. For the vast majority of homeowners, their economic situation has also proved robust during the period of high inflation and rising interest rates.

However, that does not mean that higher interest costs have not had an effect. And we are now seeing the beginnings of payment difficulties in the most challenged businesses and households.

Furthermore, there are still significant risks related to the commercial real estate market, which I spoke about last year. This summer, the Minister for Industry, Business and Financial Affairs therefore activated the sector-specific systemic risk buffer. It will be evaluated after next summer.

The market expects a period of lower interest rates ahead. And you are already seeing the beginnings of a decline in net interest income, which could be exacerbated by further interest rate cuts.

Earnings on lending, measured by the lending margin, are low and have been declining for an extended period. In addition, interest rates on housing loans have been reduced across the board during 2024.

The decline in the lending margin is mainly due to the slope of the yield curve making it cheaper to finance long-term loans. At the same time, the part of the lending margin that covers the risk of loss is at its lowest level in 20 years.

This may reflect strong competition for customers.

But it is important that you do not underestimate the risk of loss on your loans. Remember, it is in good times that bad loans are granted.

*****Climate change*****

Finally, a few words about climate change. It is a global problem and requires global solutions. That is why it is also worrying that we are seeing growing challenges with global collaboration in this area as well.

Climate change is already having a major impact in many countries. A global green transition is therefore necessary to maintain a robust economy in the long term – including in Denmark.

The transition may involve risks in the short term. We all need to learn more about those risks.

At Danmarks Nationalbank, we have made some calculations considering a risk scenario where challenges arise in achieving Denmark's climate goals. In the scenario, taxes on emissions must therefore be increased further compared to the already agreed taxes.

This will reduce the profits of your customers who emit the most. But our analysis also shows that the overall losses on your loans are limited.

However, the scenario highlights one of several risks of the transition. If multiple risks occur simultaneously or during an economic downturn, the situation could become more serious.

*****Concluding remarks*****

To sum up: The Danish economy and the financial sector are currently in a good place.

But we are facing many disruptions and we are having to deal with important issues such as geopolitical tensions, cyber threats, climate change and the green transition.

These challenges also mean we face major public investments over the coming years, such as for defence, transforming our energy systems and climate protection.

Compared to many other countries, the Danish economy is well equipped to finance this task.

But it is not just about funding.

And to keep one of the traditions of Danmarks Nationalbank, I would remind us that there must be room in the economy to absorb the major investments. Otherwise, prices and wages will rise, with the risk of renewed inflationary pressure.

And we do not want to go there.

Thank you for your attention.