

# Public finances - December 2015

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*Fiscal policy is planned within the framework given by the Danish Budget Law, EU-requirements and the medium-term 2020-plan. The overall goal is fiscal sustainability, i.e. a stable development in public debt in the longer term. Currently this requires structural budget balance in 2020. Furthermore, the annual structural deficit limit is ½ per cent of GDP due to the Budget Law. As the Danish economy gains additional momentum it is also key, that fiscal policy is gradually tightened from an accommodative starting point. This will support a sustainable recovery and reduce public deficits in order to reach structural balance in 2020.*

*For the forecast period 2015-17 the actual budget deficits comply with the 3 per cent of GDP limit given by the EU's Stability and Growth Pact. The estimated actual deficits amount to 2.0 per cent of GDP in 2015, 2.8 per cent of GDP in 2016 and 2.0 per cent of GDP in 2017, implying a close margin vis-à-vis the 3 per cent limit in 2016.*

*The budget bill for 2016 involves a strengthening of public finances since the structural deficit is being reduced to 0.4 per cent of GDP in 2016. This supports a credible adjustment towards a structurally balanced budget in 2020. Based on a set of technical assumptions concerning fiscal policy the structural budget balance is estimated at 0.4 per cent of GDP for 2017. Fiscal policy for 2017 will be planned in more detail during the course of 2016 including agreements on the economy of local governments and the central government budget bill for 2017.*

*The Budget Law introduces binding separate expenditure ceilings for central government, municipalities and regions. Based on information on expenditure developments so far in 2015 and budget figures for 2016 the expenditure ceilings are expected to be complied with.*

*Fiscal space will be quite tight in coming years in order to comply with the structural balance target in 2020 and to stabilize the recovering economy. Real public consumption is expected to increase by 0.8 per cent in 2016 and is assumed to remain unchanged in 2017. Furthermore, the high level of public investment during the recession is to be gradually normalized.*

*Both gross and net public debt are relatively moderate. Net debt is estimated at approx. 10 per cent of GDP in 2017, while gross debt (EMU) holds a broad margin against the 60 per cent of GDP limit given by the Stability and Growth Pact.*

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## 1.1 Actual budget balance

An actual budget deficit (general government) of 2.0 per cent of GDP is currently expected for 2015, *cf. table 1.1*. For the coming two year the actual budget deficits are estimated at 2.8 per cent of GDP in 2016 and 2.0 per cent of GDP in 2017, respectively. Thus, the actual budget balance is forecast to comply with the maximum deficit limit of 3 per cent of GDP given by the EU Stability and Growth Pact, although the margin is rather close for 2016.

**Table 1.1**  
Actual budget balance (general government), 2012-2017

	2012	2013	2014	2015	2016	2017
Actual balance, per cent of GDP	-3.5	-1.1	1.5	-2.0	-2.8	-2.0
Actual balance, DKK bn	-66.1	-20.4	28.5	-39.8	-56.6	-41.7

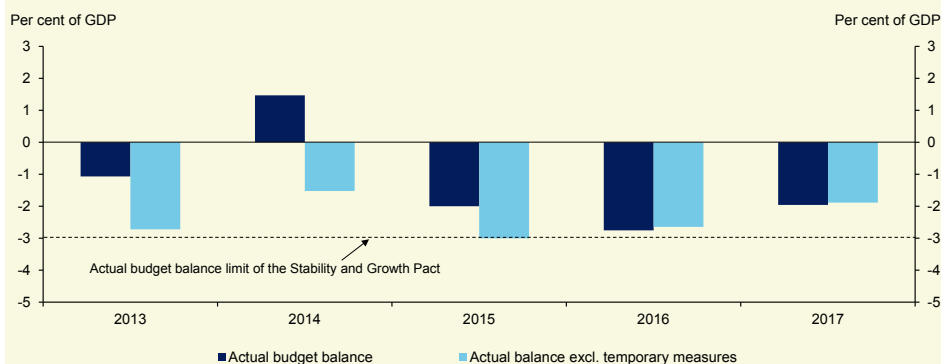
Source: Statistics Denmark and own calculations

Despite further growth in GDP and unemployment the actual budget deficit is expected to increase from 2015 to 2016. This namely reflects that the budget balance in 2015 is affected by significant temporary revenues. Thus, the so-called *Pension Package* (October 2014) is currently expected to give rise to revenues of DKK 28 bn corresponding to approx. 1.4 per cent of GDP in 2015. The Pension Package involves revenues from restructuring of capital pensions and LD-funds.

On the other hand, the current assessment also takes into account an extraordinary depreciation of arrears from tax and duties which affects the actual budget balance negatively by approx. DKK 6¼ bn (0.3 per cent of GDP) in 2015.

Excluding these temporary measures the budget deficit for 2015 is estimated at approx. 3 per cent of GDP, *cf. figure 1.1*.

**Figure 1.1**  
Actual budget balance with and without temporary measures 2013-2017



Source: Statistics Denmark and own calculations.

## Revised estimates for the actual budget balance in 2015-2016

Compared to September estimates the actual budget balance has improved by approx. 20 bn DKK in 2015 (1.0 per cent of GDP), while the expected deficit for 2016 is almost unchanged, cf. table 1.2.

The improvement of the actual budget balance for 2015 mainly reflects higher temporary revenues from the restructuring of capital pension schemes amounting to DKK 13.3 bn in 2015. Higher estimated revenues from the so-called pension yield tax of DKK 9.6 bn (0.5 per cent of GDP) in 2015 pulls in the same direction.

In addition, total expenditure on public consumption and investment in 2015 and 2016 are almost unchanged compared to the September estimates.

**Table 1.2**  
Revised actual budget balance estimates for 2015-2016 compared to September

DKK bn	2015	2016
<b>Change in estimates concerning the public balance, DKK bn</b>	<b>19.8</b>	<b>0.1</b>
Hereof:		
- Pension yield tax	9.6	-1.3
- Temporary tax revenues due to <i>Pension Package</i>	13.3	-
- Income tax etc. (incl. labour market contributions)	0.3	1.9
- North sea revenues (incl. North Sea fund)	-0.6	-1.9
- Corporation tax (excl. tax liability on hydrocarbon)	1.5	1.7
- VAT	0.0	-1.1
- Public consumption	2.0	0.1
- Public investment	-2.0	-0.3
- Other expenditure and revenue (residual)	-4.3	1.0

Note: Positive numbers indicate an improvement of budget balance due to higher revenue or lower expenditure. Negative numbers indicate a worsening of budget balance due to lower revenue or higher expenditure.

Source: Own calculations.

## 1.2 Structural budget balance

Fiscal policy is primarily planned on the basis of the structural balance, which is an estimated measure of the underlying position of public finances. With the Danish Budget Law a budget balance requirement was implemented. Thus, the annual structural balance may not exceed a deficit of ½ per cent of GDP at the time of the budget proposal unless extraordinary conditions are present. While the structural deficit limit essentially applies when presenting the budget proposal this does not imply that discretionary measures can be introduced afterwards if they weaken the structural balance beyond the deficit limit given by the Budget Law.

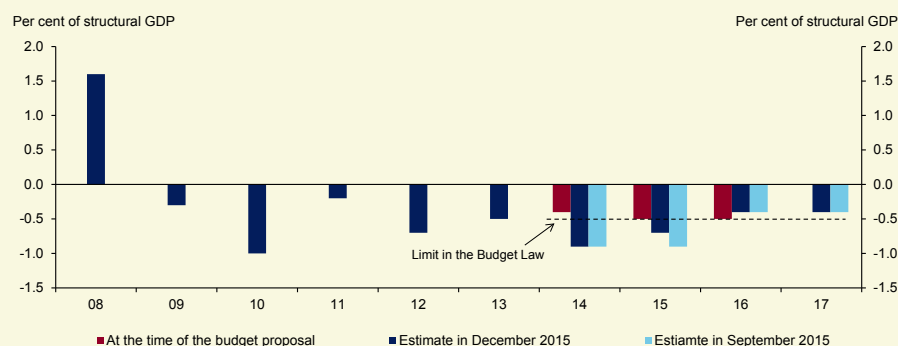
Fiscal policy in 2014 and 2015 was planned in accordance with the Budget law, i .e. with estimated structural deficits of maximum 0.5 per cent of GDP at the time of the budget proposal, cf. figure 1.2. However, in later surveys the structural balance weakened and is currently estimated at -0.9 per cent of GDP in 2014 and -0.7 per cent of GDP in 2015, respectively. This is primarily due to uncertainty surrounding the estimates of (structural) public revenues.

The structural deficit is currently estimated at 0.4 per cent of GDP in 2016. This is unchanged compared to the September estimate, which was based on the government's budget proposal for 2016. This reflects that the agreement on the budget bill for 2016 reached in November is fully financed and maintains the strengthening of public finances included in the budget proposal.

The gradual tightening of fiscal policy is aligned with the cyclical position of the economy and the need to make progress towards the goal of at least structural balance in 2020.

New information regarding the development of oil prices etc. has weakened the structural balance in 2017 compared to the September projection. In order to ensure a margin to the structural deficit limit public consumption expenditures has technically been reduced by DKK 2 bn (0.1 per cent of GDP), which implies a structural deficit of 0.4 per cent of GDP in 2017.

**Figure 1.2**  
**Structural balance estimates**



Source: Economic Survey, August 2013-15, Updated medium-term projection, September 2015 (only available in Danish as *Opdateret 2020-forløb: Grundlag for udgiftslofter 2019* at [www.fm.dk](http://www.fm.dk)) and own calculations.

### From actual to structural budget balance

The Danish Ministry of Finance calculate the structural budget balance by correcting the actual balance for cyclical effects and the impact of other temporary factors, including the often large fluctuations in the pension yield tax and North Sea revenues.

As an example, the calculation of the structural balance in 2016 starts with the estimated actual deficit of 2.8 per cent of GDP, cf. table 1.3 (row 1). The cyclical position of the econo-

my is estimated to be weaker than a normal situation (based on a weighted output and employment gap). Thus, the cyclical impact on the actual balance is estimated at approx. -1 per cent of GDP (row 2). Moreover the actual budget balance is corrected for a number of fluctuations in the revenues from North Sea activities, the pension yield tax, corporate taxes, vehicle registration tax etc. In total these items are estimated to be 1.3 per cent of GDP below the structural revenue levels in 2016 (row 3-8), *cf. figure 1.3-8*. The actual balance is also corrected for other factors (row 9) which primarily reflects that there in some years are large one-off measures with no impact on the structural balance.

**Table 1.3**  
**From actual to structural budget balance**

	2014	2015	2016	2017
<b>Per cent of GDP</b>				
1. Actual balance	1.5	-2.0	-2.8	-2.0
<i>Herof temporary impact on the actual balance from:</i>				
2. Cyclical component (gap-related)	-1.7	-1.4	-1.0	-0.7
3. Corporate taxes <sup>1)</sup>	-0.1	0.0	0.0	0.0
4. Vehicle registration	-0.1	0.0	0.0	0.0
5. Pension yield tax	1.7	-0.1	-0.4	-0.4
6. North Sea revenues	-0.3	-0.7	-0.7	-0.3
7. Net interest payments <sup>1)</sup>	0.2	-0.2	0.0	0.0
8. Special budget items <sup>2)</sup>	-0.5	-0.1	-0.2	0.0
9. Other factors <sup>3)</sup>	3.2	1.3	-0.1	-0.1
<b>10. Structural balance (1-2-3-4-5-6-7-8-9)<sup>4)</sup></b>	<b>-0.9</b>	<b>-0.7</b>	<b>-0.4</b>	<b>-0.4</b>
<i>Memo item: Weighted cyclical gap</i>	-2.2	-1.8	-1.4	-1.0

1) Excluding revenues regarding North Sea activities.

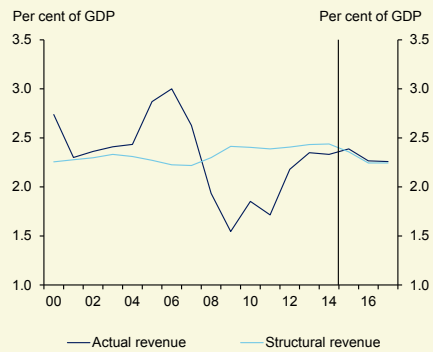
2) Includes a correction for extraordinary depreciations of tax arrears in 2015 amounting to approx. DKK 18 bn in 2015 distributed equally between 2013, 2014 and 2015.

3) Includes minor corrections including a conversion of the structural balance in per cent of actual GDP to per cent of structural GDP. Also includes a correction for the following one-off measures: One-off revenues of DKK 29¼ bn (1½ per cent of GDP) in 2013 and DKK 58¾ bn (approx. 3 per cent of GDP) in 2014 following from the restructuring of capital pensions. One-off revenues of DKK 28 bn. (1.4 per cent of GDP) in 2015 following from the pension package from October 2014. Advanced revenues from pension taxation of approx. DKK 5 bn in 2013 (¼ per cent of GDP) and DKK 2 bn (0.1 per cent of GDP) in 2014 assumed to take place uniformly from 2015-19.

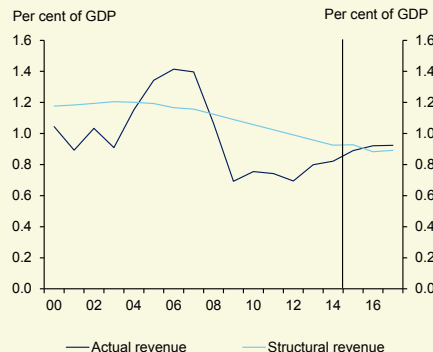
4) Structural balance in per cent of structural GDP.

Source: Statistics Denmark and own calculations.

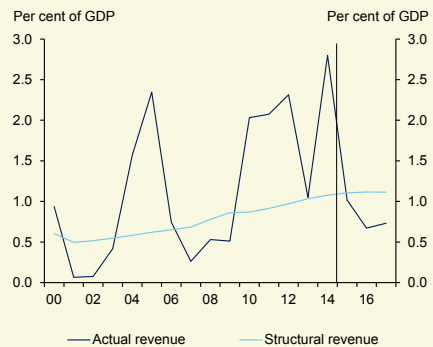
**Figure 1.3**  
**Corporate taxes (excl. hydrocarbon)**



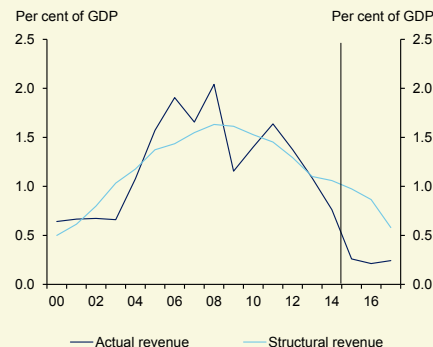
**Figure 1.4**  
**Vehicle registration tax**



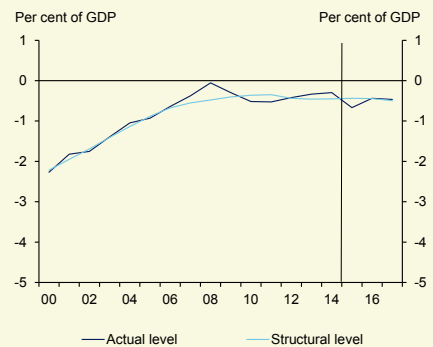
**Figure 1.5**  
**Pension yield tax**



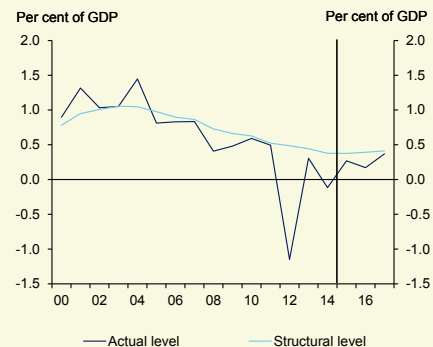
**Figure 1.6**  
**North Sea revenues**



**Figure 1.7**  
**Net interest payments**



**Figure 1.8**  
**Special budget items**

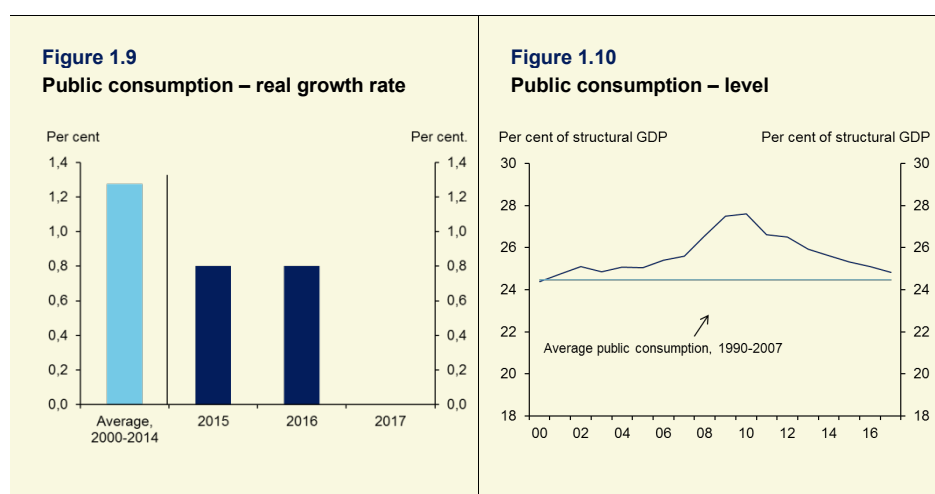


Source: Own calculations.

## 1.3 Public consumption and investment

### Moderate real growth in public consumption

Real growth in public consumption is expected at 0.8 per cent in both 2015 and 2016, *cf. figure 1.9*. In 2017 public consumption is assumed to remain unchanged in real terms. The estimated real growth rates for public consumption for the forecast period 2015-2017 is relatively moderate compared to the period 2000-2014, where the average annual growth rate amounted to 1¼ per cent. Nonetheless, the level of public consumption (as share of structural GDP) is still relatively high by historical standards, *cf. figure 1.10*.



Source: Statistics Denmark and own calculations.

Nominal public consumption expenditure is estimated at 520¼ bn DKK in 2015, which is 2 bn DKK lower than the September estimate, *cf. table 1.4*. This reflects central and local government account figures covering the first three quarters of 2015, which indicate lower consumption expenditures than previously assumed. Due to the lower level of public consumption in 2015 the projected real growth rate of public consumption has been reduced from 1.2 per cent to 0.8 per cent in 2015.

**Table 1.4**  
**Public consumption estimates**

	2015	2016	2017
<b>Real growth rate (per cent)</b>			
September survey	1.2	0.3	-
December survey	0.8	0.8	0.0
<i>Change since September (percentage points)</i>	<i>-0.4</i>	<i>0.5</i>	<i>-</i>
<b>DKK bn</b>			
September survey	522.2	531.1	-
December survey	520.2	530.9	541.1
<i>Change since September</i>	<i>-2.0</i>	<i>-0.2</i>	<i>-</i>

Source: Own calculations.

Based on the agreed central government budget bill for 2016 and preliminary budgets of the municipalities and regions for 2016 nominal public consumption expenditure is estimated at approx. 531 bn DKK next year.

The projected real growth rate of public consumption is increased from 0.3 per cent to 0.8 per cent in 2016. This mainly reflects the lower level of public consumption in 2015 and increased expenditures concerning asylum seekers in 2016.<sup>1</sup>

From 2016 to 2017 public consumption expenditure is projected to remain unchanged in real terms. Thus, the projected real growth rate of public consumption is lowered by 0.5 percentage points in 2017 compared to the *Updated medium-term projection, September 2015*. This primarily reflects a technical reduction of public consumption due to a weakening of the structural balance in 2017, cf. section 1.2 above.

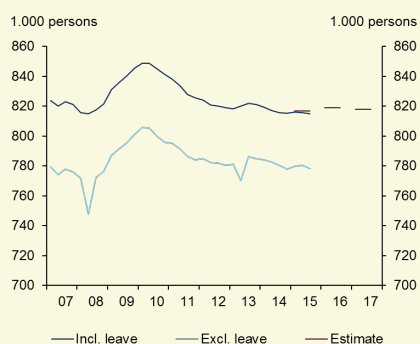
### Stable development in public employment

The level of public employment is currently estimated to remain unaltered from 2014 to 2015, and increase by some 2,000 persons in 2016, cf. figure 1.11 and table 1.5. In light of an unchanged level of real public consumption from 2016 to 2017 public employment is technically assumed to decrease by 1,000 persons in 2017.

<sup>1</sup> In 2016 the expenditures regarding asylum seekers is adjusted upwards compared to the central government budget proposal for 2016 presented in September. This implies – ceteris paribus – an increase of the real public consumption growth rate by 0.3 percentage points compared to the September estimate.



**Figure 1.11**  
Public employment (national accounts)



**Table 1.5**  
Public employment estimates

	2015	2016	2017
<b>Change compared to the previous year (1.000 persons)</b>			
September	1.0	1.0	-
December	0.0	2.0	-1.0
Change	-1.0	1.0	-
<b>Level in December</b>	<b>817</b>	<b>819</b>	<b>818</b>

Source: Statistics Denmark, Budget Outlook 3, September 2015 and own calculations.

## Public investment

Public investment expenditure has been historically high over the past years in order to stimulate economic activity during the recession. However, a normalization of the investment expenditure level is planned over the coming years as the recovery gains further momentum. Thus, the public investment (as share of GDP) is expected to decline from 3.8 per cent in 2015 to 3.4 per cent. in 2017, cf. table 1.6.

Based on current information concerning public investment projects etc. the estimated expenditure for 2017 exceed the level stipulated in the latest medium-term projection by DKK 5 bn, cf. *Updated medium-term projection, September 2015* (only available in Danish at [www.fm.dk](http://www.fm.dk)). Thus it will be necessary to adjust public investment when fiscal policy for 2017 is planned more concretely.

However, the estimated public investment expenditure level in 2017 based on projects etc. is uncertain partly due to time lags in construction activity between individual years e.g. with respect to major infrastructure projects and large hospital construction projects etc.

**Table 1.6**  
Public investment estimates

	2015	2016	2017
Public investment expenditure (DKK bn, current prices)	75.8	71.6	73.2
Real growth rate (per cent)	1.2	-6.9	-0.1
Share of GDP (per cent)	3.8	3.5	3.4

Source: Statistics Denmark and own calculations.

## 1.4 Expenditure ceilings

Starting in 2014 the Budget Law introduced separate binding expenditure ceilings for central government, municipalities and regions, respectively. The expenditure ceilings continuously cover a 4 year period and are determined in accordance with the medium-term projections.

As expenditure control took place in May and September 2015 the two central government sub-ceilings (operating expenditures and income transfers) were expected to be met concerning 2015. The subsequent and final expenditure control for central government expenditures in 2015 will be carried out at the end of the first quarter of 2016 based on final account figures.

Based on an updated status for central government spending in 2015 the operating expenditures are estimated to be DKK 6¼ bn lower than the relevant sub-ceiling, *cf. table 1.7*. In addition, central government spending on income transfers in 2015 is expected to remain approx. DKK 6¼ bn below the relevant subceiling.

Based on municipal and regional budgets for 2015 and current information on account figures covering the first three quarters of 2015, local government expenditures are also expected to comply with the relevant ceilings in 2015.

**Table 1.7**  
**Expenditure ceilings, 2015**

Bn DKK (2015-prices)	Central government sub-ceilings		Municipalities	Regional sub-ceilings	
	Operating expenditures	Income transfers	Operating expenditures	Health expenditures	Development expenditures
Expenditure ceiling	189.0	257.6	234.7	104.7	3.0
Budget	189.8	254.1	234.5	104.9	3.0
Updated status for central government spending in 2015	182.7	251.4	-	-	-

On the central government budget bill for 2016 the operating expenditures are planned in accordance with the relevant sub-ceiling, *cf. table 1.8*. Central government expenditure concerning income transfers are expected to be approx. DKK 3 bn lower than the ceiling set for 2016.

A preliminary evaluation of local government budgets for 2016 show operating expenditures which are DKK 0.2bn below the relevant sub-ceiling. Local government budgets are therefore within the limit of the expenditure ceiling in 2016. The same holds for the regional budgets.

**Table 1.8**  
**Expenditure ceilings, 2016**

Bn DKK (2016-prices)	Central government sub-ceilings		Municipalities	Regional sub-ceilings	
	Operating expenditures	Income transfers	Operating expenditures	Healthcare expenditures	Development expenditures
Expenditure ceiling	182.2	257.4	237.4	107.4	3.0
Budget bill and preliminary local gov. budgets for 2016	182.2	254.3	237.2	107.4	3.0

## 1.5 Fiscal stance

To measure the impact of fiscal policy changes on economic activity so-called *fiscal effects* (an indicator of the fiscal policy stance) are calculated. The fiscal multi-year fiscal effects are computed as the fiscal policy impact as of 2015 and onwards. Thus, the fiscal effects are calculated from a relative expansionary starting point in 2014 characterized by historically high levels of public consumption and investment. Overall, fiscal policy (from 2015 onwards) is estimated to contribute neutrally to growth in 2015, -0.3 per cent in 2016<sup>2</sup>, and -0.4 per cent in 2017, *cf. table 1.9*. Thus, the general assessment is that fiscal policy is aligned with the upswing in the Danish economy.

**Table 1.9**  
**Activity effects fiscal policy and other economic policy measures from 2015 onwards**

Per cent of GDP	2015	2016	2017
<i>GDP level</i>			
Fiscal policy as of 2015 (multi-year effects)	0.0	-0.2	-0.6
<i>Growth contribution</i>			
Fiscal policy (multi-year effects)	0.0	-0.3	-0.4
- hereof one-year fiscal effect	0.0	-0.1	-0.2

Note: Multi-year effects are computed as the activity effect of the fiscal policy from 2015 and onwards.  
Source: Own calculations.

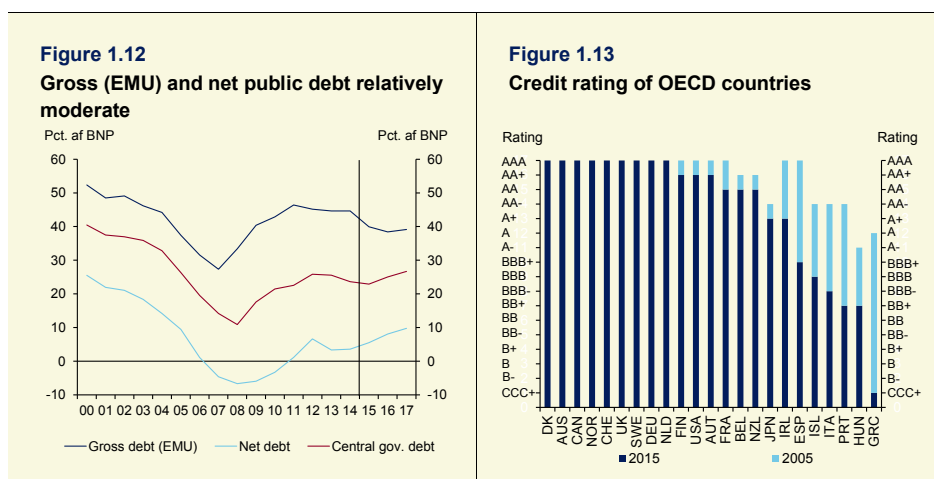
As GDP growth is expected to increase in the coming years, the higher economic activity is also expected to result in a further increase in private-sector employment. Therefore a gradual tightening of fiscal policy is crucial in the current juncture. In addition, the adjust-

<sup>2</sup> Besides the contribution from the one-year fiscal effect in 2016 the multi-year effect of the fiscal policy in 2016 reflects that both revenue and expenditure elements also have multi-year effects. These elements have a negative growth effects in 2016.

ment of fiscal policy should also be seen in light of the present very accommodative monetary policy.

## 1.6 Public debt

Central government debt (as share of GDP) is estimated to increase from 23¾ per cent in 2014 to 26¾ per cent in 2017, *cf. figure 1.12*. The gross public debt (EMU-definition) is estimated at approx. 38-40 per cent of GDP in the forecast period 2015-17, thus maintaining a broad safety margin against the 60 per cent of GDP limit of the Stability and Growth Pact. Gross debt is reduced quite markedly from 44½ per cent of GDP in 2014 to approx. 40 per cent of GDP mainly due to the stop in issuance of central government bonds for period 30 January to 7 October 2015, reducing central government holdings in Danmarks Nationalbank instead. Furthermore, net public debt – the key debt concept concerning fiscal sustainability – is estimated at a rather moderate level of approx. 10 per cent of GDP in 2017.



Source: Statistics Denmark and own calculations.

Sound public finances and moderate public debt supports that Denmark is one of relatively few countries in the world with the highest credit rating (AAA) in the three major rating agencies Moody's, Standard & Poor's and Fitch, *cf. figure 1.13*. While a number of OECD countries have experienced a downgrade of their credit ratings in wake of financial crises and the subsequent debt crisis, the assessment of Denmark has been maintained. The high credit rating reflects a high confidence in the Danish economy. It is an important objective for fiscal policy to support a high credit rating, as it supports low interest rates for the Danish government, Danish homeowners and other Danish borrowers.