Nordic Council of Ministers

Nordic Economic Outlook 2020

Annual report on the economic development in the Nordic countries in terms of growth, business cycles and public finance

Contents

1. Summary

This report of economic development in the Nordic countries has been prepared by the Nordic Group of Macro Analysts and describes the economic outlook in the five Nordic countries. The economic outlook is based on the budget bill forecast from the autumn 2020 for all the countries.

1.1 Global developments

The Covid-19 pandemic poses a serious threat to life and health. Disruption caused by the pandemic, extensive containments measures and voluntary social distancing have caused sharp declines in economic activity worldwide. Global growth, which already slowed down last two years, is projected at – 4.5 percent in 2020 according to IMF October outlook. The outlook is somewhat better that anticipated in the Funds last WEO update in June. The reason is better outcome for the second quarter 2020 than expected and stronger indicators for the third quarter. In 2021 global growth is projected at 5.2 percent a little lower than in June. The outcome is wider negative output gaps and elevated unemployment worldwide.

Forecasts are uncertain and downside risks are high both at the short and in the medium term. Risks are mostly related to the future development in the pandemic, but other downside risks also remain, particularly related to future trade relations.

1.2 Developments in the Nordic countries

All five countries are hard hit by the COVID-19 pandemic. Even though responses were different all the countries were hit by a severe shock during the first half of the year and they are all facing uncertainty in the short term. The Nordic countries have implemented extensive and targeted measures to mitigate the economic effects of the crisis. In the initial phase of the pandemic, fiscal policy focused on temporary measures to support badly affected businesses and households with the purpose of maintaining employment, securing household income and avoiding insolvency due to liquidity problems. These discretionary measures came on top of the already strong automatic stabilisers in the economies.

Without the prompt and strong fiscal and monetary policy response, the contraction in economic output would have been substantially larger. Most European economies, including the Nordic countries, are facing another wave of the pandemic causing tightening of containment measures again and raising uncertainty. An effective and widely available vaccine is believed to be prerequisite for the economy to regain full strength.

The Nordic countries experienced steep declines in export, consumption and investment in the first half of 2020. The GDP contraction from the first to the second quarter was historically large, at -4.5 to -9.1%. For 2020 as a whole, GDP is projected to fall by between -3.1 and -7.6% compared to 2019. The service sector has been particularly hard hit, with tourism at the forefront – a particularly large export sector in Iceland. Also sports and cultural sectors have been badly affected. Unemployment rates have risen significantly.

Discretionary measures employed by the Nordic countries have been considerable and are quite similar in many respects. The focus has been on liquidity measures (new and extended credit lines, and tax deferrals), VAT and tax cuts, household income protection as well as job retention, and support for businesses aimed at the most affected sectors and groups (export and import- oriented businesses and service sectors, in particular hospitality, aviation, sports and culture).

Monetary policy responses have been accommodative in the countries. In two of the Nordic countries, Central banks rapidly made steep cuts in policy rates.

The Danish economy is growing again following declines in GDP in the first and second quarter this year. A projected decline in GDP of 4.5 per cent this year is expected to be followed by an increase of 4.2 per cent next year. However, significant uncertainty surrounds the projection, which is based on the assumption that the recovery will continue without major disruptions, and that the outlook for the global economy does not deteriorate further

The Finnish economy has contracted in three consecutive quarters. The coronavirus (COVID-19) pandemic nevertheless caused less damage to the Finnish economy in the first half of the year than it did to most other European economies. Gross domestic product (GDP) is forecast to shrink 4.5% in 2020, to grow by 2.6% in 2021 and by 1.7% in 2022. This gradual recovery in the economy follows the standstill seen in the early part of 2020.

The Icelandic economy is forecast to contract by 7.6% this year. The Icelandic economy has been hard hit by the pandemic, not least because of the large share of the tourist sector in the exports, causing unemployment reach 7.8% of the labour force. Nevertheless, the country's economic fundamentals are strong. The current account has been in sustained surplus since 2013 and the net foreign asset position has turned positive (22% of GDP) as decades of current account deficits were turned around following the financial crisis. Both public and private entities have used the recent economic expansion to pay down debt and as a result balance sheets have improved dramatically, thereby increasing the economy's resilience to downturns. Both fiscal and monetary policy is accommodating.

The coronavirus pandemic has caused a setback in the Norwegian economy that is without precedent since the war. The GDP for Mainland Norway was in the national budget 2021 forecast to decline by 3.1 percent this year, followed by a 4.4 percent increase next year. This will bring the activity level next year above its pre-crisis level, but nonetheless below normal and lower than the levels forecast prior to the coronavirus outbreak. The strength of the rebound is uncertain and depends on how the pandemic develops.

Sweden's GDP fell sharply during the second quarter of 2020. The decline was the largest seen in a single quarter since measurements began in 1980 and was mainly driven by falls in exports and household consumption. Sweden's export-oriented economy was clearly affected by reduced demand and lockdowns in the rest of the world. The Swedish economy seems to have bottomed out in the spring 2020 and is expected to, like the global economy, recover in the second half of 2020. It is expected to take until the end of 2021 before GDP is on the same level as before the virus outbreak.

1.3 Public finances

The Nordic countries have strong automatic stabilizers that have done their work in light of the CORONA outbreak on top of that the countries have implemented discretionary measures to increase the economies resilience. Last years solid growth, strengthening labour markets and policy efforts have improved fiscal conditions giving fiscal space for expansionary fiscal policy response.

In Denmark the public finances in 2020 and 2021 reflect the economic setback following the coronavirus pandemic as well as the expansionary fiscal policies implemented in order to support the Danish economy. Therefore, the actual public surplus of 3.8 per cent of GDP in 2019 is expected to turn into a deficit of respectively 3.9 per cent of GDP in 2020 and 2.4 per cent of GDP in 2021. The Danish EMU-debt is projected to increase from approximately 33 per cent of GDP in 2019 to 46 per cent of GDP in 2020 after which it is expected to drop to approximately 42 per cent of GDP by the end of 2021.

Finland's general government deficit will reach 7.7% this year, while general government debt will increase to about 70% of the GDP. Even though the general government deficit will shrink in the next few years, it will still amount to 2.7% of the GDP (about EUR 7 billion) in 2024.

In Iceland, the fiscal space is being used both to allow strong automatic stabilisers to work in full and for targeted discretionary measures, with a focus on both short term measures and infrastructure projects to strengthen the growth potential. In total, the general government deficit is expected to reach -11.0% of GDP in 2020 and 10% in 2021. The government has announced that it will continue to use fiscal policy to support the economy as needed but that it intends to halt the growth in debt to GDP in 2025. The Central Bank has slashed interest rates by 175 bp to 1%, fully lowered the 2% counter cyclical buffer, announced a quantitative easing programme and intervened in the foreign exchange market.

In Norway the savings in the Government Pension Fund Global (GPFG) and the fiscal rule give space for considerable fiscal leeway to counter the negative impact of the pandemic. The objective has been to minimise the negative impact on the economy by limiting income shortfall for both businesses and individuals, and by averting bankruptcies among viable businesses. Petroleum revenue spending in 2020 is historically high. The structural non-oil fiscal deficit is calculated to correspond to 3.9% of the value of the GPFG at the beginning of 2020. The budget for 2021 aims to continue to support private sector activity and employment, but at the same time reduce Fund capital spending towards a more sustainable level.

The economic downturn in Sweden, combined with government's fiscal policy measures will substantially weaken public finances in 2020. The general government net lending is expected to increase as the economy recovers. Since the decline is judged to be temporary, the cyclically adjusted balance is less impacted. The cyclically adjusted balance is nevertheless believed to show deficits up to and including 2022. As a result of the deterioration, the general government gross debt ratio is looking to increase rapidly between 2019 and 2020, to thereafter fall as a share of GDP.

Table 1. Central macroeconomic variables

	2018	2019	2020	2021
GDP growth, %				
Denmark	2.2	2.9	-4.5	4.2
Finland	1.5	1.1	-4.5	2.6
Iceland	3.9	1.9	-7.6	3.9
Mainland Norway	-	2.3	-3.1	4.4
Sweden	2.0	1.2	-4.6	4.1
Inflation, %				
Denmark	0.8	0.8	0.3	1.2
Finland	1.1	1.0	0.4	1.2
Iceland	2.7	3.0	2.8	2.7
Norway	-	2.2	1.1	3.5
Sweden	2.0	1.8	0.3	1.1
Unemployment (LFS), %				
Denmark	3.5	3.6	4.8	4.4
Finland	7.4	6.7	8.0	8.2
Iceland	2.7	3.6	7.8	6.8
Norway	-	3.7	4.7	4.4
Sweden	6.3	6.8	9.0	9.5
Current account balance, percentage of GDP				
Denmark	7.0	8.9	5.6	5.7
Finland	-4.0	-1.1	-1.2	-2.7
Iceland	2.9	6.0	1.8	1.0
Norway	-	-	-	-
Sweden	2.3	4.1	4.6	4.0-

2. Denmark

2.1 Economic outlook

The corona pandemic continues to have a big impact on economic developments across countries. Denmark is among a number of countries that succeeded in getting the epidemic under control relatively early on, thereby enabling a reopening of the economy. This has lifted economic activity especially in the industries that have suffered most from the initial restrictions and changed consumer behaviour.

Against this background, the Danish economy is growing again following declines in GDP in the first and second quarter this year. A projected decline in GDP of 4.5 per cent this year is expected to be followed by an increase of 4.2 per cent next year. However, significant uncertainty surrounds the projection, which is based on the assumption that the recovery will continue without major disruptions, and that the outlook for the global economy does not deteriorate further.

The projected recovery is expected to be driven by a recovery in private consumption, while exports and private investments are set to deliver only a small positive contribution next year after a significant negative contribution to GDP growth this year. Thus, this recovery differs from the recovery following the financial crisis, which was especially driven by exports, while private consumption remained subdued for several years.

The expectations for a recovery driven by private consumption should be seen in light of clear signs of increasing spending. The volume of debit card transactions and retail sales show an increase in private consumption since the spring. Although consumer confidence remains rather subdued, the level of debit card transactions is close to the level from 2019.

The housing market has also shown positive signs, with housing sales rebounding from declines in March and April. The housing market is usually quite sensitive to the economic cycle and shifts in sentiment. The quick recovery should also be seen in the context of continued low interest rates. Furthermore, prior to the downturn the level of house prices was relatively balanced, and there were no signs of, for example, unsustainable increases in indebtedness as during the boom in 2005–2007.

The increase in domestic demand has occurred in line with the reopening of the economy and has been aided by the various support packages and compensation schemes that have helped underpin incomes and production capacity. In addition, there are other policy decisions that will strengthen demand, including the disbursement of three weeks of previously frozen holiday pay (equivalent to about 2 per cent of GDP, net of income tax), the green housing agreement, and the tax-free one-off subsidy of DKK 1,000 to all benefit recipients.

Domestic demand is also strengthened by increased public demand in the form of public consumption and public investment, which partly offsets the decline in private demand this year. Thus, economic policy dampens the decline in aggregate demand and supports the recovery.

The economic downturn abroad is affecting export market demand. Restrictions on travel and other restrictions that have been implemented as a result of the corona pandemic also affect some export industries, for example by limiting the opportunities for new sales promotions or the provision of services in other countries. These developments have led to a large decline in exports, although there are differences between industries. In particular, the important pharmaceutical industry has been relatively unscathed during the first half of the year.

The wage compensation scheme (in force until August 31) has helped to limit the setback in the labour market, which has not reacted to the extent that the drop in GDP would otherwise entail. A decline in employment of 50,000 persons this year is set to be followed by an increase of 17,000 persons next year. The rather moderate improvement from 2020 to 2021, measured by annual averages, reflects an expected increase in private employment of around 55,000 persons from the end of 2020 to the end of 2021. The improvement in employment is also reflected in unemployment, which is expected to decline by around 34,000 persons through 2021, reaching 127,000 persons at the end of the year.

The risks to the outlook are mainly on the downside (looking beyond the effects of upward revisions to historical data). These relate mainly to the evolution in the pandemic itself, in Denmark and abroad, as well as other external risks, including the risk of a disorderly Brexit.

2.2 Public finances

The public finances in 2020 and 2021 reflect the economic setback following the coronavirus pandemic as well as the expansionary fiscal policies implemented in order to support the Danish economy. Therefore, the actual public surplus of 3.8 per cent of GDP in 2019 is expected to turn into a deficit of respectively 3.9 per cent of GDP in 2020 and 2.4 per cent of GDP in 2021.

In the general government draft budget proposal for 2021, the fiscal policy is planned to be expansionary and the fiscal policy is planned with a structural deficit of 0.5 per cent of GDP in 2021 equivalent to the limit for structural deficits in the Danish Budget Law. Measured by the structural budget balance, the fiscal expansion amounts to approximately DKK 21 billion corresponding to 0.9 per cent of GDP compared to the policy assumptions underlying the previous Economic Survey.

In the general government draft budget proposal for 2021, funds are set aside to support the recovery of the Danish economy and handle the health care challenges effectively. Additional funds are allocated to improve public services, enhance safety and trust, prioritize climate initiatives and improve the conditions of Danish businesses etc. Based on the budget agreements with the municipalities and regions in 2021 and the general government draft budget proposal, real public consumption is estimated to grow by 0.6 per cent in 2021 from an elevated 2020-level which among other things reflect extraordinary expenses in 2020 related to the handling of COVID-19.

The objective of structural budget balance in 2025 remains unchanged. This implies, among other things, that new permanent spending initiatives must be financed responsibly. Towards 2025, the fiscal policy is planned based on an adjusted profile for the structural budget balance which supports the recovery of the economic activity in the intervening years. Within the fiscal policy frame, the highest possible growth in public consumption exceeds the growth in the demographic pressure in every year. Furthermore, the fiscal policy plans entail an increase in public investments and a reserve for additional fiscal stimulus.

The fiscal support of the economy in the current years is large from a historic perspective. The contribution from the planned expansionary fiscal policy is in the same order of magnitude as the fiscal stimulus in the years following the financial crisis in 2008. With the temporary compensation schemes and fiscal stimulus, the fiscal policy is estimated to increase demand by approximately 2.4 per cent of GDP in 2021 which contributes to reduce the output gap.

The Danish EMU-debt is projected to increase from approximately 33 per cent of GDP in 2019 to 46 per cent of GDP in 2020 after which it is expected to drop to approximately 42 per cent of GDP by the end of 2021. Thus, the EMU-debt is still expected to remain well below the limit of 60 per cent, and Denmark is still among the countries with the lowest debt in the EU. The public net worth is estimated to be reduced to 2.6 per cent of GDP at the end of 2020 and 0.1 per cent of GDP at the end of 2021. Hence, almost two years after the outbreak of the corona pandemic, the public sector is not expected to have a net public debt.

Table 2: Key figures for the Danish economy

	2019	2017	2018	2019	2020	2021
	DKK bn.					
Private consumption	1,076	2.3	2.7	1.4	-2.8	4.7
Public consumption[1]	557	0.9	0.3	1.2	2.2	0.6
Fixed business investments	322	5.2	6.2	3.3	-12.2	-0.5
Stock building (per cent of GDP)	14	0.1	0.3	-0.3	-0.9	0.8
Total domestic demand	2,163	2.4	2.9	1.3	-2.3	2.8
Exports	1,362	4.8	3.3	5.0	-10,2	6.2
Total demand	3,525	3.3	3.0	2.7	-5.8	4.6
Imports	1,190	4.2	4.8	2.4	-8.6	5.5
GDP	2,335	2.8	2.2	2.9	-4.5	4.2

	2017	2018	2019	2020	2021
Employment (1,000 persons)	2,919	2,965	3,003	2,948	2,965
Gross unemployment (per cent of labour force)	3.8	3.5	3.6	4.8	4.4
Consumer price index (per cent)	1.1	0.8	0.8	0.3	1.2
Hourly compensation (per cent)	2.2	2.3	2.5	2.1	2.4
Effective exchange rate (2015=100)	102.1	103.6	102.9	103.9	104.7
Terms of trade (goods)	-1.5	-2.3	0.1	0.2	0.0
Current account (per cent of GDP)	8.0	7.0	8.9	5.6	5.7

[1] *Measured by the output method incl. depreciations.*

Source: *Statistics Denmark and the Danish Ministry of Finance.*

3. Finland

3.1 Economic outlook

The Finnish economy has contracted in three consecutive quarters. The coronavirus (COVID-19) pandemic nevertheless caused less damage to the Finnish economy in the first half of the year than it did to most other European economies. During the summer, there was a quieter period in the virus situation, which prompted households in many countries to be more active and to consume more, which was also the case in Finland. However, the pace of economic recovery is slow due to the low level of confidence felt across the economy and the increase in uncertainty. The considerable increase in COVID-19 infections and the imposition of new restrictions cast a further shadow over the recovery, and the economy is once again at a turning point.

Gross domestic product (GDP) is forecast to shrink 4.5% in 2020, to grow by 2.6% in 2021 and by 1.7% in 2022. This gradual recovery in the economy follows the standstill seen in the early part of 2020. Private consumption will recover the fastest, but the growth in consumption of private sector services will continue to be slow. The reduced level of housing construction will weaken the recovery in investment. Exports and industrial production are suffering from the continuation of the pandemic and will not return to growth until next year.

The uncertainty caused by the pandemic is slowing the growth in foreign demand in many sectors that are important for Finland's exports, and as a consequence exports will continue to decrease further this year. The outlook for industry in the latter part of this year is therefore also subdued. In services, the outlook for ICT and business services is better than in sectors directly affected by restrictions in mobility and by reduced consumer confidence.

Growth in private investment will be weakest in the third quarter of this year and will continue to be weak at the end of the year. In construction, however, the first half of the year was more favourable than had been anticipated. The number of new housing starts for 2020 as a whole will be down only slightly. This will amount to a decrease of a few thousand units and will mark a clear reduction in the amount of investment in housing construction.

Growth in private investment will remain weak overall in the coming years. Investment in machinery and equipment will be boosted by stronger demand internationally and domestically towards the end of the forecast period. Expenditure on research and development will start to grow, supported by government funding for R&D activities. Private investment will decrease overall, reducing the ratio of private investment to GDP to around 19% in 2022.

Consumption of services has been hardest hit by the restrictions on mobility and business activities prompted by the virus pandemic. Consumer caution is expected to adversely affect the consumption of services next year as well. Consumption of consumer goods decreased moderately in the first half of 2020, while food consumption actually increased slightly compared to a year ago. It is estimated that the consumption of goods will return to its normal level in the first half of 2021.

The demand for labour has decreased, and the number of people employed will continue to decrease in 2020. In 2021 and 2022, growth in the economy will gradually push up the demand for labour. The unemployment rate in 2021 will rise to 8.2% at most. In 2022, despite an increase in employment, the employment rate will not exceed 71.5%.

Earnings will rise by about 2% a year from next year. The increase in consumer prices will remain moderate due to the low level of consumption growth.

The virus situation has remained good in Finland and the economic forecast assumes that this will also be the case in the future. Consumer confidence and the capacity of the economy to perform will remain weak until an effective treatment or vaccine is found for COVID-19. A clear deterioration in the virus situation during the autumn would increase uncertainty across the economy and weaken the level of economic growth even without any actual new restrictive measures.

A resurgence of the virus is the most significant risk factor in the forecast. The extent of the economic impact of a second wave would depend not only on the government measures taken to mitigate the epidemic and support the economy, but also on how these actions affect the multitude of economic decisions taken throughout the country. If the economy has not fully recovered before a second wave, the contraction in the economy could be smaller than seen in the spring this year. It is nevertheless likely that in this case the economic growth potential would be diminished and the effects of the crisis would be felt over a longer period.

Substantial measures by the European Union to stimulate output and demand have either been launched already or are under preparation. The implementation of these measures, and of Finland's economic recovery package decided by the Government in June, will have a positive effect on production both domestically and elsewhere in 2020 and 2021.

3.2 Public finances

Finland's general government deficit will reach 7.7% this year, while general government debt will increase to about 70% of the GDP. Public finances are weakened by the economic downturn triggered by the COVID-19 pandemic and the Government measures supporting companies, citizens and economic growth.

Even though the general government deficit will shrink in the next few years, it will still amount to 2.7% of the GDP (about EUR 7 billion) in 2024. The combined deficit of central and local government will be larger because the employment pension institutions, which are part of general government, will post slight surpluses.

Finland's general government finances already suffered from a structural deficit during the peak of the economic cycle preceding the downturn. Our general government finances have been substantially weakened by the ageing of the population for the last ten years as the number of ageing people using public services and benefits has been growing at a rapid rate. At the same time, the working-age population financing Finland's public services and social security with its taxes has started to shrink.

The ageing of the population will also cause expenditure pressures in general government finances in the future as the number of people aged over 75 (major users of health and social services) will grow. As a result, the general government debt-to-GDP ratio will probably grow throughout the 2020s. According to the current estimates, consolidating general government finances by EUR 5 billion by the year 2026 would stabilise the debt ratio to between 70 and 75 per cent during the next ten years. Restoring the debt ratio to 2019 levels (around 60%) during the 2020s would require consolidation measures totalling about EUR 10 billion.

Table 3: Key figures for the Finnish economy

	2019	2017	2018	2019	2020	2021	2022
	EUR bn.	**Percentage change unless stated otherwise**					
GDP at market prices	241	3,3	1,5	1,1	-4,5	2,6	1,7
Imports	95	4,2	5,5	2,4	-10,0	4,0	2,8
Total supply	336	3,5	2,6	1,5	-6,1	3,0	2,0
Exports	96	8,6	1,7	7,5	-12,5	5,3	3,8
Consumption	181	0,7	1,7	1,0	-1,5	3,1	0,8
private	126	1,0	1,8	0,9	-3,8	4,0	1,6
public	55	0,1	1,6	1,2	3,9	1,1	-1,1
Investment	57	4,8	3,9	-1,0	-4,7	0,0	2,9
private	47	5,7	3,7	-1,5	-7,6	0,2	4,2
public	10	0,5	5,0	1,3	8,7	-0,9	-2,6
EUR bn.							
GDP		226	234	241	233	242	250
Current account		-2.1	-4,0	-1,1	-1,2	-2,7	-1,5
Percentage change							
Services, change in volume		2,6	2,4	1,2	-3,6	2,7	1,4
Industry, change in volume		8,6	-2,0	3,7	-6,8	3,4	3,6
Labour productivity, change		3,0	-1,0	0,2	-0,6	1,8	1,5
Employed labour force, change		1,1	2,6	1,1	-2,0	-0,5	0,5
Employment rate		69,6	71,7	72,5	71,2	71,0	71,5
Unemployment rate		8,6	7,4	6,7	8,0	8,2	8,0
Consumer price index		0,7	1,1	1,0	0,4	1,2	1,4
Index of wage and salary earnings		0,2	1,7	2,1	1,7	2,5	2,0
Short-term interest rates (3-month Euribor)		-0.3	-0.3	-0,4	-0,4	-0.4	-0.3
Long-term interest rates (10-year govt. bonds)		0,5	0,7	0,1	-0,2	-0,1	-0,1

Percentage change						
Services, change in volume	2,6	2,4	1,2	-3,6	2,7	1,4
Industry, change in volume	8,6	-2,0	3,7	-6,8	3,4	3,6
Labour productivity, change	3,0	-1,0	0,2	-0,6	1,8	1,5
Employed labour force, change	1,1	2,6	1,1	-2,0	-0,5	0,5
Employment rate	69,6	71,7	72,5	71,2	71,0	71,5
Unemployment rate	8,6	7,4	6,7	8,0	8,2	8,0
Consumer price index	0,7	1,1	1,0	0,4	1,2	1,4
Index of wage and salary earnings	0,2	1,7	2,1	1,7	2,5	2,0
Short-term interest rates (3-month Euribor)	-0.3	-0.3	-0,4	-0,4	-0.4	-0.3
Long-term interest rates (10-year govt. bonds)	0,5	0,7	0,1	-0,2	-0,1	-0,1
Percentage of GDP						
Tax ratio	42,9	42,4	42,2	41,9	42,7	42,3
General government net lending	-0,7	-0,9	-1,0	-7,7	-5,0	-3,9
Central government net lending	-1,8	-1,2	-1,2	-7,2	-4,4	-3,2
General government gross debt	61,3	59,6	59,2	70,2	72,8	74,3
Central government debt	46,8	44,9	44,2	53,3	55,6	56,6
General government expenditure	53,7	53,4	53,3	59,8	57,6	56,0
Current account	-0,9	-1,7	-0,5	-0,5	-1,1	-0,6

Source: *Statistics Finland and the Finnish Ministry of Finance.*

4. Iceland

4.1 Economic outlook

The COVID-19 pandemic has severely affected the Icelandic economy. Gross domestic product is expected to contract by 8% in 2020. When the crisis hit, growth had already slowed in 2019 due to a slowdown in tourism, after growing by 34% since 2010, an average growth rate of 3.7% per year. In March of this year, Iceland had one of the steepest increases in COVID-19 cases in Northern Europe, prompting containment measures that led to a sharp decline in consumption and rise in unemployment. An effective containment response paved the way for a recovery in domestic demand over the summer. However, the country's large tourism sector is still severely affected by travel restrictions and a decreased willingness to travel internationally.

The COVID-19 epidemic in Iceland and the containment response have its particularities in comparison with peers. Unlike most European countries, the first wave of the epidemic was virtually eradicated by early May. This allowed economic activity to normalise more quickly than in most of Western Europe. Iceland has relied to a greater extent on extensive testing and contact-tracing, while lockdown measures have been less stringent than in many mainland European countries. Private consumption fell by 8% in the second quarter of 2020, but to a large degree due to a collapse in spending by Icelanders abroad as a result of less travel. A reorientation of consumption towards domestic goods and services has contributed positively to domestic demand.

A sharp decline in exports contributes the most to the contraction in GDP this year. Exports are expected to fall by 30%, mostly due to a 75% drop in tourist arrivals. Tourism led the recent economic expansion in Iceland; its share in GDP more than doubled between 2011 and 2018 to reach 8%. Tourist arrivals had already declined in 2019 as the country's second-biggest airline ceased operations early that year. The decline in tourist arrivals in 2019 along with cost pressures had already brought challenges to tourism before the pandemic hit. In March, international travel came to a halt and tourist arrivals collapsed completely. In June, travel restrictions were eased and tourist arrivals recovered somewhat, reaching about 20% of 2019 levels in July. Tourism has now been brought nearly to a halt yet again, as new rules regarding quarantine upon entry into Iceland entered into force on August 19 while the pandemic is widespread in our most important markets.

After growing by 34% since 2010, an average of growth rate of 3.7% per year, the country's economic fundamentals are strong. Both public and private entities have used the expansion to pay down debt and as a result balance sheets have improved dramatically, thereby increasing the economy's resilience to downturns and contributing to positive current account balance.

Despite the very large negative shock to Iceland's largest export sector, the current account balance was positive by 1.7% of GDP in the first half of 2020, as imports have also fallen and the country entered the recession with a sizeable current account surplus. The Icelandic króna depreciated by 13% in the first nine months of the year. The real exchange rate had approached historically high levels during the recent economic expansion but is now close to its historical average.

Despite the negative shock to domestic demand, inflation has risen recently due to the depreciation of the króna. It measured 1.7% in January but had risen to 3.5% in September. Both short-term and long-term inflation expectations are close to target, though, as the negative output gap that has formed is expected to weigh against the effect of the depreciation on inflation over the next months and the central bank has ample tools to keep inflation close to target going forward.

Rising unemployment is among the most serious macroeconomic repercussions of the pandemic. Unemployment in Iceland has been low in recent years but was already on the rise before the coronavirus crisis hit, reaching 5.0% in February. It is now expected to reach over 10% at the end of the year. It is also worrying that the share of people of working age who do not participate in the labour market has risen since the crisis hit. Tourism, a labour-intensive sector, has contributed the most to these developments. Over 40% of unemployed are foreign labour and among them the unemployment rate is 20%.

4.2 Fiscal policy space is being partially used to alleviate the downturn

Public finances have suffered a large hit due to the recession as a result of strong automatic stabilisers and discretionary measures in response to the pandemic. General government net lending was -2% in 2019 but is expected to reach -11% of GDP this year and to remain negative over the next years. Targets for government net lending for the next years have been revised downwards by a revision of the government's Fiscal Policy Statement and a draft 2021–2025 Fiscal Plan.

The government has implemented a broad range of economic policy measures in response to the pandemic. The aim of these measures has been: i) to safeguard to the extent possible the cash flow of firms and households, thus lessening the negative feedback loop between the supply-side shock directly due to the pandemic and the demand side of the economy, ii) to protect vulnerable groups, such as the low-income and marginalised workers most affected by containment measures and the hit to tourism, and iii) to set the ground for a fast, forceful and balanced recovery once the right conditions are in place.

On the fiscal side, strong automatic stabilisers and targeted discretionary measures have eased the hit to businesses and households. Among the main fiscal measures undertaken are part-time unemployment benefits, closure subsidies, government guaranteed loans to companies and a boost to public investment. A part of the fiscal response has been a revision of the Fiscal Policy Statement for 2018–2022, the document setting the frame for fiscal policy in this period, allowing for the increased government deficits that result from the pandemic and related policy measures.

The part-time unemployment scheme has been successful in sustaining businesses' cash position while providing generous income support to households and protecting employer-employee relationships. At its peak in April, around 15% of the workforce were registered in the scheme. It has been extended twice, first through August and then again until the end of the year.

Further measures for households include supplemental child benefits, payment of wages during government-stipulated quarantine, and a temporary allowance to withdraw from third-pillar pension funds. Further support to businesses includes support loans for those companies that have suffered a heavy revenue loss, direct subsidies for those that were made to close operations during the containment measures stipulated by the government, payment of wages during notice period for companies fulfilling certain criteria, deferral of tax payments and netting of income tax. The tourism sector is supported by two further measures: a voucher for Icelanders to travel domestically and a government-sponsored marketing campaign in key markets abroad. Public investment and support for innovation have also been boosted in response to the pandemic with an aim to unlock productivity gains. In total, the direct fiscal cost of COVID-19-related measures so far amounts to around 3% of GDP and the indirect cost is an additional 6.5% of GDP.

The Central Bank of Iceland's monetary and macroprudential policy response has also been wide-ranging. The policy rate was cut by 175 basis points between February and May. In March, the countercyclical capital buffer was cut from 2% to 0%, and further steps were taken to improve the liquidity position of banks and thus put them in a stronger position to support their customers. Finally, the Central Bank of Iceland has for the first time conducted quantitative easing (QE). Its announced envelope for the purchases of government bonds in the secondary market amounts to around 5% of GDP this year; it has only purchased a fraction of this amount so far.

The COVID-19 pandemic has put into clear focus the importance of strong macroeconomic buffers, economic diversification and international cooperation, not least on economic affairs. For a small, open economy such as Iceland, this is best ensured with strong trade ties, particularly with our neighbouring European economies. A marked decline in the share of external trade in GDP, mostly due to the decline in tourism, is worrying in this regard and must be reversed.

The macroeconomic outlook for the next years is heavily uncertain, mostly due to the pandemic and its repercussions. It seems likely that the crisis will leave permanent scars on some sectors and on production capacity in general. Macroeconomic policy must now accommodate and adapt to developments. While the policy stance should recognise that some of the damage on production capacity cannot be undone, it must also take into account that under these circumstances, macroeconomic policy has an especially important role in preventing long-term unemployment, supporting investment and thus, ultimately, contributing to potential growth.

Though an effective health and containment response has made the COVID-19 crisis less severe for most of Iceland's population and economy than in neighbouring countries, the country's large tourism sector is heavily hit. The sector faces a difficult and uncertain path to normality. Nonetheless, tourism will likely play a large role in supporting exports and employment when the pandemic ultimately wanes. The potential of tourism to bring a rapid recovery of jobs once the situation normalises is especially important in order to prevent elevated unemployment from becoming permanent.

A recovery in tourism will not be a panacea, though. While strong macroeconomic buffers have ameliorated the shock of a virtual collapse in Iceland's most important export sector, the crisis has highlighted the vulnerabilities associated with a lack of diversification of exports in a small, open economy. The government will aim to support diversification into other sectors with the potential to harvest long-term productivity growth. Government investment has increased in 2020, will be increased even further in 2021 and sustained at a high level in the medium term. There is a special focus on projects that are labour-intensive and support productivity. Government support for innovation has also been increased significantly.

Pivotal to the swift and bold policy response has been the accumulation of ample policy buffers on all fronts in recent years, including a steep decline in public debt, a significant improvement in the external balance, and the greater anchoring of inflation expectations. A medium-term objective of economic policy is the preservation and, if necessary, restoration of these buffers. This includes an eventual adjustment of fiscal policy to ensure that government debt remains at a level low enough to provide room to mitigate the economic shocks the future might hold. Therefore, while the government debt-to-GDP ratio is forecast to rise in the coming years, an aim is set in the draft 2021–2025 Fiscal Plan to stabilize it no later than in 2025.

Table 4. Key figures for the Icelandic economy (%)

	2018	2019	2020	2021	2022
Private consumption growth	4.7	1.3	-5.0	4.2	3.3
Public consumption growth	4.0	4.2	2.8	1.8	1.9
Gross fix capital formation	-1.0	-6.6	-8.9	5.5	2.4
Exports growth	1.7	-4.9	-30.0	17.1	8.6
Imports growth	0.8	-10.2	-23.2	17.4	8.6
GDP growth	3.9	1.9	-7.6	3.9	3.1
Consumer price inflation (annual rate)	2.7	3.0	2.8	2.7	2.6
Unemployment rate (annual average)	2.7	3.6	7.8	6.8	6.2
Current account balance (% of GDP)	2.9	6.0	1.8	1.0	1.3
General government net lending balance (% of GDP)[1]	0.8	-1.5	-10.6	-9.7	-7.3
General government primary balance (% of GDP)[1]	3.0	0,5	-8,5	-7,6	-5.0
General government gross Maastricht debt (% of GDP)	36.4	35.9	51.0	57.5	62.2

1) *Underlying balance, i.e. without large one-off revenues and expenditure*

Source: *Statistics Iceland, October 2020, Ministry of Finance and Economic Affairs*

5. Norway

5.1 Economic Outlook

The coronavirus pandemic has caused a setback in the Norwegian economy that is without precedent since the war. Economic activity has recovered in line with falling infection levels and easing of the strictest infection control measures. A higher oil price and strong consumption growth have also boosted economic activity. Late March saw the highest registered unemployment since World War II, but it has since declined rapidly. We estimate that GDP for Mainland Norway will decline by 3.1 percent this year, followed by a 4.4 percent increase next year. This will bring the activity level next year above its pre-crisis level, but nonetheless below normal and lower than the levels forecast prior to the coronavirus outbreak.

The strength of the rebound is uncertain and depends on how the pandemic develops. As several other European countries, Norway has recently had renewed outbreaks. New infection control measures have been introduced, primarily in areas with the largest outbreaks. That increases the risk of a new setback and of unemployment remaining high. The forecasts rest on assumptions that there will not be a renewed coronavirus outbreak as severe as witnessed earlier this year and that a vaccine most probably will be widely available sometime next year.

The contraction of the global economy has also been without precedent. The majority of our trading partners experienced steeper declines in GDP than Norway. Economic activity expanded in response to an easing of infection control measures, but several European countries have recently had renewed outbreaks and have tightened infection control measures, thereby slowing the economic recovery. Norwegian export firms are likely to be faced with weak demand for quite some time. On the other hand, the oil price has increased from the exceptionally low levels of March and April, and the temporary petroleum tax reductions adopted in June may also dampen the negative impact on the Norwegian offshore supply industry.

The oil price has bounced back somewhat and has recently been around 40 dollars a barrel, after having declined to below 20 dollars during the oil market collapse in late April. Production cuts from OPEC and other oil producers have served to reduce excess supply and increase the oil price. Norway has also decided to cut oil production in 2020. Recently, the gas price has also increased. Oil futures indicate that the oil price may increase further.

Unemployment in Norway has declined since the beginning of April, but a high number of workers remain furloughed. The number of people registered as fully unemployed has more than halved since its peak, from 10.7 percent of the workforce in March, to 3.8 percent on 22 September. That is about 0.9 percentage point higher than the average over the last twenty years and 1.5 percentage point higher than in February. The figures include those employees who are completely furloughed, and changes for this group of workers explain both the March increase and the subsequent decline. If we exclude furloughed employees, the number of people registered as fully unemployed in September was close to the historical average. Unemployment has declined more swiftly than projected in the Revised National Budget in May.

Wage growth looks set to be moderate this year. At the same time, depreciation of the Norwegian krone over several years has served to improve competitiveness. Exceptionally low electricity prices have reduced consumer price inflation. Consequently household purchasing power should increase this year in spite of low wage growth. Electricity prices are expected to normalise next year, thereby allowing for the prospect of negative real wage growth.

Developments in domestic private consumption have exceeded expectations. Consumption of goods increased markedly from April to July, before declining somewhat in August, but was still 5 percent higher in August than in February. Also more recent data from the BankAxept/Vipps payment service indicate that consumption has come somewhat down form the high level witnessed during the general summer vacation. Some of the upturn in the consumption of goods is mirrored by a drop in consumption of services. Restrictions on travel and cross-border shopping have also boosted domestic consumption. For 2020 as a whole, private consumption is expected to contract by 6 percent, mainly due to a decline in Norwegians' consumption abroad. Private consumption is projected to expand by close to 8 percent next year.

The overall effect of the pandemic on the housing market has been small. Sales volumes have remained at pre-crisis levels. After declining in March and April, housing prices returned to their February level in May and have continued to increase through the summer. The rapid housing market rebound must be viewed in light of historically low interest rates. The market for new homes has been more heavily impacted, with a reduction in both sales and housing starts during the spring. There are now indications of an upturn in the market for new homes, with fairly high sales of new homes through the summer months.

The setback in the Norwegian economy in 2020 is expected to be less severe than we projected in May. A less severe downturn than anticipated means a lower risk of employees permanently dropping out of the labour market and capital remaining unused. Parts of the business sector are nonetheless facing a particularly strong pressures to adjust. The significant rebound in GDP for mainland Norway observed in the last few months is expected to continue into next year, thus implying strong economic growth in 2021. GDP for mainland Norway is nevertheless expected to be below the levels forecast prior to the coronavirus outbreak, with lower employment and higher unemployment.

Although significantly lower than immediately after the coronavirus outbreak, uncertainty about future developments in the Norwegian economy remains higher than normal. Economic activity may fall again in the event of the authorities being forced to reinstate strict infection control measures.

Table 5. Key figures for the Norwegian economy. The National budget 2021

		2019	2019	2020	2021
		Billion NOK[1]			
Private consumption		1,591.3	1.5	-6.0	7.8
Public consumption		866.7	1.7	2.2	1.1
Gross fixed investment		926.5	6.1	-5.0	1.0
Of which:	Petroleum extraction and pipeline transp.	178.4	12.8	-2.2	-11.5
	Business sector Mainland Norway	335.8	5.6	-10.6	5.4
	Housing	196.2	-0.9	-6.9	4.9
	Public sector	212.7	7,5	4.5	1.1
Demand from Mainland Norway[2]		3,202.7	2.2	-4.2	5.7
Exports		1,311.5	1.5	-2.1	4.3
Of which:	Crude oil and natural gas	463.7	-4.3	9.0	6.3
	Goods from Mainland Norway	432.3	4.9	-4.4	3.5
	Services from Mainland Norway	272.4	6.2	-13.2	6.2
Imports		1,249.3	5.2	-10.6	4.7
Gross domestic product		3,549.4	1.2	-1.5	4.5
Of which:	Mainland Norway	3,038.6	2.3	-3.1	4.4
Other key figures:					
Employment, persons			1,6	-1.6	0.6
Unemployment rate, LFS (level)			3.7	4.7	4.4
Unemployment rate, registered (level)			2,2	4.9	3.1
Annual wage			3.5	1.7	2.2
Consumer price index (CPI)			2.2	1.1	3.5
Underlying inflation (CPI-ATE)			2.2	2.7	2.2
Crude oil price, NOK per barrel (level)			564	408	424
Three-month money market rates, pct.[3]			1,6	0.7	0.4
Import-weighted exchange rate (yearly change)[4]			2.9	5.7	-2.4

1 Preliminary national accounts in current prices

2 Excluding inventory changes

3 Technically calculated using forward prices in September

4 Positive number indicates a depreciation of the krone

Sources: *Statistics Norway, ICE, Norges Bank, Norwegian Labour and Welfare Administration, Reuters, Macrobond and Ministry of Finance*

5.2 Economic policy

The pandemic and the introduction of strict infection control measures have given rise to a need for extraordinary fiscal policy and monetary policy measures this year. Norges Bank lowered the key policy rate to zero pct., and the scale of the measures introduced via the fiscal budget is without precedent in modern Norwegian history.

Our savings in the Government Pension Fund Global (GPFG) and the fiscal rule give us considerable fiscal leeway to counter the negative impact of the pandemic. In accordance with the fiscal rule, we have temporarily increased the spending of Fund capital (beyond the long-term guideline of 3 pct.) to stimulate economic activity and employment, and to reduce unemployment. The objective has been to minimise the negative impact on the economy by limiting income shortfall for both businesses and individuals, and by averting bankruptcies among viable businesses. After scaling back the strictest infection control measures and the economy started to recover, the measures have focused more on growth and restructuring, as well as targeting those industries that continue to be directly affected by the infection control measures. Box 1 gives an overview of economic measures that have been introduced or proposed in response to the pandemic.

Petroleum revenue spending in 2020 is historically high. The structural non-oil fiscal deficit is forecasted to be NOK 395.0 billion; NOK 151.4 billion more than was adopted last autumn. The structural non-oil fiscal deficit is calculated to increase by 4.5% of Mainland Norway trend GDP from 2019 to 2020 (the fiscal policy indicator), and to correspond to 3.9% of the value of the GPFG at the beginning of 2020.

The budget for 2021 aims to continue to support private sector activity and employment, but at the same time reduce Fund capital spending towards a more sustainable level. Bringing the infection situation under control has, in combination with extensive economic measures, triggered an earlier start to the economic rebound than many had expected, and economic growth has picked up in recent months. Capacity utilisation in the Norwegian economy is nonetheless estimated to be below normal levels also in 2021. This means that fiscal stimulus also will be needed next year, although to a significantly lesser degree than in 2020.

The structural non-oil fiscal deficit is forecasted to be NOK 313.4 billion in 2021, which corresponds to 3.0 percent of the forecasted value of GPFG at the beginning of the year. The structural non-oil fiscal deficit is expected to decrease by 2.9% of Mainland Norway trend GDP from 2020 to 2021, as temporary Covid-19 measures are phased out. Spending will nonetheless be NOK 61 billion higher than in 2019, calculated at 2021 prices. Overall, the budgets for 2020 and 2021 have a strong expansionary effect on economic activity in mainland Norway.

Public sector expenditures were already at a high level before the crisis, and with the high spending this year, these expenditures are expected increased to 66 percent of mainland Norway GDP in 2020. This is historically high, both in terms of our own development and compared to other countries. In order for fiscal policy to be sustainable over time, we must ensure that a temporary expenditure increase does not turn into a permanently higher expenditure level. Larger fiscal deficits today will reduce fiscal sustainability in the longer run. Future generations will have to pay for current public spending through higher taxes or lower public spending. Still, in the absence of strong measures, the downturn would have been steeper with more bankruptcies and higher unemployment. The increased petroleum revenue spending has therefore been both appropriate and necessary. The budget-proposal for next year will reduce public expenditure to 61 percent of mainland Norway GDP in 2021, 5 percentage points lower than this year, but still higher than in the years before the crisis.

Table 6. Key figures for the central government. The national budget 2021

	2019	2020	2021
Non-oil deficit, NOK billion	227.6	433.2	371.2
Structural non-oil fiscal deficit, NOK billion	242.6	395.0	313.4
Per cent of capital in the Government Pension Fund Global[1]	2.9	3.9	3.0
Per cent of trend GDP mainland Norway	7.9	12.3	9.4
Fiscal impulse	0.4	4.5	-2.9
Real underlying expenditure growth, per cent.	1.7	10.1	-4.6

1 *At the beginning of the year*

Source: *Ministry of Finance.*

Box 1 Overview of economic measures introduced in 2020 in response to the coronavirus pandemic

The Government and the Storting has been launching economic measures in three phases in order to tailor necessary measures to the economic situation.

The *first phase* saw the introduction of emergency measures to stave off unnecessary bankruptcies and redundancies, along with extra income support for wage earners. These included a government loan guarantee scheme and temporary tax changes to improve the liquidity situation, a reduced countercyclical buffer requirement to prevent stricter bank lending practices from exacerbating the downturn, as well as temporary changes to the unemployment benefit and furloughing rules. The furloughing scheme was modified to make the State absorb a larger portion of furloughing costs. Employer's social security contributions were temporarily reduced, and a number of other tax reductions and deferrals were introduced. The State also took on a larger share of the cost of sickness absence and caring for children who were ill or otherwise unable to go to school.

The *second phase* saw the introduction of further specific measures to improve solvency in industries, firms and businesses that had been hit especially hard by the pandemic. This included, inter alia, the introduction of a compensation scheme for businesses suffering large sales reductions, a grant scheme for sports, charities and cultural events, as well as separate arrangements targeting the self-employed. The business compensation scheme was subsequently extended and expanded to include seasonal businesses.

The economy is now in the *third phase*, in which measures are intended to boost employment, restructuring and economic growth. The Government's roadmap for *Norway's Coronavirus Crisis Exit Strategy – Producing More and Making Working Life More Inclusive* included a number of measures to increase employment, strengthen the private sector, facilitate a green future, expand skills, boost inclusion and improve integration. The measures are intended to stimulate increased activity by being tailored to the economic situation. This implies that the introduction of new measures needs to be considered in relation to, and complement, existing measures. The wage support scheme is an example of such a measure, the purpose of which is to get furloughed employees back to work and prevent unemployment from being entrenched at a high level.

The financial emergency measures adopted or proposed come to a total of NOK 126 billion in 2020; see Table 3. These measures come in addition to the so called automatic stabilisers, which are the effects of income support schemes and tax schemes in place prior to the crisis. The automatic stabilisers are big in Norway due to the comprehensive welfare schemes that are mainly financed by taxes.

For some of the measures introduced earlier, the estimates have subsequently been modified in line with developments. Economic activity in Norway has rebounded more rapidly than had been expected, thus making the need for intervention less comprehensive than feared. The compensation scheme for businesses suffering large sales reductions will, in particular, cost less than the amount appropriated by the Storting. Moreover, it is estimated that the temporary changes to the national insurance income support schemes, such as the expansion of unemployment benefit and sickness benefit, will cost less than previously expected. This is primarily because the labour market has improved more quickly, sickness absence has been lower and care benefit spending has been less than originally anticipated.

The economic measures are temporary and shall be phased out as the economy reverts to a more normal situation. The compensation scheme for businesses suffering large sales reductions was discontinued at the end of August. Discontinuation of the temporary emergency measures is necessary to avoid supporting inactivity instead of innovation, and to chart a route back to sustainable and targeted economic policy.

In addition to the abovementioned measures, the spring of 2020 saw the adoption of temporary tax reductions for petroleum activities. The reductions are expected to provide the companies liquidity amounting to NOK 115 billion for the years 2020 and 2021. Over time, the changes are expected to inflict a public revenue loss of about NOK 8 billion, measured as net present value. The tax reductions increase oil companies' prospects for going ahead with planned investments. These tax reductions are not included in Table 3.

Table 7. Economic measures for 2020 adopted or proposed in response to the pandemic

	Appropriation 2020 *NOK billion*
Measures targeting businesses	66.1
Counter income shortfall for businesses, etc.[1]	34.8
Compensation scheme for businesses suffering large sales reductions	7.0
Aviation sector, incl. loss provision for guarantee scheme	14.3
Loss provision, government loan guarantee scheme via banks	10.0
Expansion of income support schemes for individuals	16.5
Other compensation schemes[2]	11.1
Measures for sectors with duties of critical importance to society[3]	25.4
Other measures	7.2
TOTAL Economic measures	**126.3**

1 *Includes, inter alia, a reduced obligation for employers to pay wages upon furloughing, reduced employer liability for care benefit and coronavirus-related sickness absence, temporary tax reductions and the support scheme for getting furloughed employees back to work.*

2 *Includes, inter alia, compensation for cultural events, charities and sports, and compensation for national road ferries, trail transport and other public transport.*

3 *Includes, inter alia, appropriations for the health sector, local government, the police and the Norwegian Labour and Welfare Administration.*

Source: *Ministry of Finance.*

6. Sweden

6.1 Economic Outlook

Sweden's GDP fell sharply during the second quarter of 2020. The decline was the largest seen in a single quarter since measurements began in 1980 and was mainly driven by falls in exports and household consumption. Sweden's export-oriented economy was clearly affected by reduced demand and lockdowns in the rest of the world.

The Swedish economy seems to have bottomed out in the spring 2020 and is expected to, like the global economy, recover in the second half of 2020. Confidence indicators have begun to rise again, but from low levels. It is however expected to take until the end of 2021 before GDP is on the same level as before the virus outbreak. The resource utilization is expected to be significantly lower than normal and the Swedish economy is expected to be in a deep recession both in 2020 and 2021.

The fall in household consumption in the first half of 2020 was larger than any previously measured fall. This sharp decline was mainly due to restrictions aimed at reducing the spread of infection and associated changes in behavioural patterns. Consumption of hotel, restaurant and travel services, as well as cultural and sporting events, were hit particularly hard. However, high frequency indicators such as card transaction data indicate a gradual recovery in household consumption. Increased unemployment and uncertainty about the development of the pandemic is expected to hold back the recovery somewhat.

Tax revenues in the municipal sector are expected to grow more slowly than normal during 2020, but since the government has provided additional funds in the spring, the public sector consumption is believed to continue unchanged. Additional funds are intended to be added in 2021. In 2020 and 2021, public consumption is expected to increase in line with the historical trajectory.

Gross fixed capital formation fell sharply during the first half of 2020. Increased uncertainty, mainly linked to how quickly the economy will recover, makes companies postpone investments. Indicators also point to low capacity utilization in industry, which indicates subdued investment prospects. To date, the construction industry has not been affected to the same extent by the recession as other industries, but a gradual decline is expected ahead. Housing investments are expected to decrease, but the decrease will be delayed compared to other business investments, as new construction is expected to decline more gradually. Overall, total investment is expected to fall sharply in 2020 and increase somewhat in 2021. However, it will take time to recover the large fall. Through 2021, investments are expected to remain at levels lower than in 2019.

Supply disruptions and falling demand in the rest of the world have affected Sweden's export sector hard. Several indicators, such as companies' export orders, have sunken to low levels. Both exports and imports are expected to decline significantly in 2020, to recover in 2021, when external demand rises.

The employment rate has fallen sharply during the first half of 2020. Since the labour force has decreased less than employment, the unemployment rate has increased. The unemployment rate has increased in all groups, but especially among young people.

When the demand in the economy rises and production gradually increases, the labour market is expected to recover as well. Several labour market indicators, for example companies' employment plans, have improved slightly after the extremely low levels that were noted in the spring. However, employment is expected to fall sharply in 2020. The fall is limited, since many companies invoke the option of short-time work scheme. Employment is expected to grow slightly in 2021, but the pace will likely be slow since many companies primarily increase production by increasing working hours among already employed when short-time work scheme are phased out. Unemployment is expected to increase in both 2020 and 2021.

Inflation (CPIF) was low during the first half of 2020. This trajectory is expected to continue in the nearest future and is primarily explained by low energy prices. Low resource utilization in Sweden and in the rest of the world is expected to curb inflation, mainly in 2020, but also in 2021. Central banks worldwide are expected to keep policy rates low for a long period of time, in order to stimulate demand and thereby inflation. The low policy rates and extensive purchases of assets, such as government bonds, contribute to a situation where interest rates remain low.

The economic downturn combined with government's fiscal policy measures will substantially weaken public finances in 2020. The general government net lending is expected to increase as the economy recovers. Since the decline is judged to be temporary, the cyclically adjusted balance is less impacted. The cyclically adjusted balance is nevertheless believed to show deficits up to and including 2022. As a result of the deterioration, the general government gross debt ratio is looking to increase rapidly between 2019 and 2020, to thereafter fall as a share of GDP.

Table 8. Key figures for the Swedish economy

	2019	2020	2021	2022	2023
GDP	1.2	-4.6	4.1	3.8	2.7
Private consumption	1.2	-4.7	4.3	4.3	3.2
Public consumption	0.3	1.2	0.8	-0.1	-1.4
Fixed capital formation	-1.3	-9.0	3.5	5.5	4.2
Stock building (contribution to growth)	-0.1	-1.0	1.0	0.0	0.0
Exports	3.2	-6.8	4.8	5.7	5.0
Imports	1.1	-8.3	5.0	4.8	4.2
Net exports (contribution to growth)	1.0	0.4	0.1	0.6	0.6
Productivity in private sector	2.0	-0.1	0.8	1.9	1.3
Hours worked	-0.3	-4.3	3.0	1.8	1.6
Employment, aged 15–74	0.7	-2.1	0.3	2.4	1.7
Unemployment, % of labour force aged 15–74	6.8	9.0	9.5	8.1	7.1
GDP gap	0.7	-5.9	-3.8	-1.8	-0.6
Wages	2,6	1,8	2,2	2,5	2,8
CPI	1.8	0.3	1.1	1.0	1.3

Table 9. Estimates from the Budget Bill for 2020

	2019	2020	2021	2022	2023
Fiscal position	0,3	-5,5	-3,5	-1,6	0,3
Structural balance	0,3	-2,6	-1,0	-0,3	0,8
Consolidated gross debt	35,2	42,6	42,3	41,4	39,5

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