



**COUNCIL OF  
THE EUROPEAN UNION**

**Brussels, 24 January 2006**

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**UEM 25**

**NOTE**

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from : General Secretariat of the Council  
to : Delegations

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Subject: Council Opinion on the updated Convergence Programme of Denmark

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Delegations will find attached the Council's opinion on the updated Convergence Programme presented by Denmark, as adopted by the ECOFIN Council on 24 January 2006.

Attachment

**COUNCIL OPINION**  
**of 24 January 2006**  
**on the updated convergence programme of Denmark, 2005-2010**

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community,

Having regard to Council Regulation (EC) No 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies<sup>1</sup>, and in particular Article 9(3) thereof,

Having regard to the recommendation of the Commission,

After consulting the Economic and Financial Committee,

HAS DELIVERED THIS OPINION:

- (1) On 24 January 2006 the Council examined the updated convergence programme of Denmark, which covers the period 2005 to 2010.
- (2) Over the last decade, GDP growth has averaged some 2 per cent, while inflation has broadly followed euro area inflation. Employment growth has picked up in recent years and unemployment is close to its lowest level in the last decade. The macroeconomic scenario underlying the programme envisages real GDP growth of 2.4% in 2006 and 1.6% on average over the rest of the programme period. Assessed against currently available information, this scenario appears to be cautious, in particular regarding the technically-assumed growth rates for 2007 and 2008. The programme's projections for inflation appear realistic.

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<sup>1</sup> OJ L 209, 2.8.1997, p. 1. Regulation as amended by Regulation (EC) No 1055/2005 (OJ L 174, 7.7.2005, p. 1). The documents referred to in this text can be found at the following website: [http://europa.eu.int/comm/economy\\_finance/about/activities/sgp/main\\_en.htm](http://europa.eu.int/comm/economy_finance/about/activities/sgp/main_en.htm)

- (3) On 17 February 2005, in its opinion the Council endorsed the budgetary strategy presented in the 2004 update of the convergence programme of Denmark. Regarding the 2005 budgetary implementation, the 2004 update targeted a 2.2% of GDP general government surplus for 2005 while the current update forecast a 3.6% surplus for a similar GDP growth outlook. Revenues have come in better than expected, including revenues from the pension fund yield tax as well as from oil and gas exploitation.
- (4) The programme broadly follows the model structure and data requirements for stability and convergence programmes specified in the new code of conduct<sup>1</sup>.
- (5) The budgetary strategy aims at maintaining structural surpluses between 1½% and 2½% on average over the programme period, implying a marked reduction in the general government debt ratio, in order to provide a sound basis for the ageing of the population. The strategy is based on expenditure restraint, with the objective of keeping the annual growth of real public consumption at 0.5%, and maintenance of the tax freeze and of a balanced budget requirement for local governments. The update foresees the general government surplus to narrow from 3.6% of GDP in 2005 to 3.1% in 2006 and 3.2% in 2007, then declining slightly to reach 2.9% of GDP at the end of the programme period. The estimated general government surpluses in the present update are markedly higher than in the previous update while projected GDP growth is similar.
- (6) As its MTO, the programme targets a structural balance (taking into account the use of the transition period of the Eurostat decision mentioned above) of between 1½% and 2½% of GDP over the programme period. In structural terms (i.e. in cyclically-adjusted terms net of one-off and other temporary measures), the surplus falls from a peak of 3.6% of GDP in 2005 to around 2¾% of GDP in 2006 before firming to 3¼% of GDP thereafter. However, the calculated easing in 2006 by 0.8 percentage point of GDP reflects a normalisation of expected tax receipts from pension funds, which were exceptionally high in 2005. Corrected for the temporary higher revenues in 2005 the structural surplus is broadly unchanged from 2005 to 2006.

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<sup>1</sup> The programme has gaps in the compulsory data and does not provide all optional data prescribed by the new code of conduct (especially projected world and EU GDP growth for certain years are missing).

- (7) As the MTO is more demanding than the minimum benchmark (estimated at a deficit of about 1/2% of GDP), its achievement should fulfil the aim of providing a safety margin against the occurrence of an excessive deficit. As regards appropriateness, the programme's MTO lies within the range indicated for euro area and ERM II Member States in the Stability and Growth Pact and the code of conduct and is significantly more demanding than implied by the debt ratio and average potential output growth in the long term. The programme explains that it is set at a more demanding level than required by the Pact to set a sound basis for long-term fiscal sustainability through a rapid debt reduction.
- (8) On balance, the risks to the budgetary projections in the update appear to be on the positive side, in particular as GDP growth may be higher than expected, mainly due to the technically-assumed low GDP growth in 2007 and 2008 stemming from a gradual closing of the output gap as estimated by the Danish authorities. Hence, GDP growth and the budgetary outcome in these years could be better than projected in the programme. A negative risk is the compliance with the target of limiting the growth of real public consumption, against the background of a mixed track record in this regard.
- (9) In view of this risk assessment, the budgetary stance in the programme seems sufficient to maintain the programme's MTO throughout the programme period. In addition, it provides a sufficient safety margin against breaching the 3% of GDP deficit threshold with normal macroeconomic fluctuations in each year. The fiscal policy stance implied by the programme is also in line with the Stability and Growth Pact in the sense that it is not pro-cyclical in good economic times – appropriate account taken of the exceptionally high revenues from pension yield tax and oil and gas extraction that boost the estimated surplus for 2005 – which is important given the cyclical position of the Danish economy. The reclassification of second-pillar funded pension schemes from spring 2007 (when the transition period for the implementation of the Eurostat decision of 2 March 2004 on the matter expires) will reduce the Danish surpluses by around 1% of GDP in each year but would not materially alter this assessment.
- (10) The debt ratio is estimated to have reached 36% of GDP in 2005, well below the 60% of GDP Treaty reference value. The programme projects the debt ratio to decline by around 14 percentage points over the programme period.

- (11) With regard to the sustainability of public finances, Denmark appears to be at low risk on grounds of the projected budgetary costs of an ageing population, due to its solid public finances and provided that the assumed employment increases and low government consumption growth are achieved, which requires further labour market reforms and spending restraint. The strategy of putting sustainability concerns at the heart of fiscal policy making, including containing pension expenditure and involving accumulation of assets, contributes positively to the long-term outlook for public finances. The currently favourable budgetary position contributes to the financing of the projected budgetary impact of an ageing population and the medium-term budgetary plans are consistent with sustainable public finances<sup>1</sup>.
- (12) The envisaged measures in the area of public finances are broadly consistent with the broad economic policy guidelines, included in the integrated guidelines for the period 2005-2010. In particular, Denmark respects its MTO. However, new measures have not been specified to achieve the assumed increase in employment of close to 2% of the labour force by 2010.
- (13) The National Reform Programme of Denmark, submitted on 26 October 2005 within the context of the renewed Lisbon strategy for growth and jobs, puts emphasis on improving labour supply to ensure the long-term sustainability of public finances and improving the efficiency of the public sector. The budgetary implications of the actions outlined in the National Reform Programme are fully reflected in the budgetary projections of the convergence programme. The measures in the area of public finances envisaged in the convergence programme are in line with the actions foreseen in the National Reform Programme.

The Council is of the opinion, that, overall, the budgetary position is sound and the budgetary strategy provides a good example of fiscal policies conducted in compliance with the pact.

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<sup>1</sup> Details on long-term sustainability are provided in the technical assessment of the programme by the Commission services, to be published at the website:  
[http://europa.eu.int/comm/economy\\_finance/about/activities/sgp/main\\_en.htm](http://europa.eu.int/comm/economy_finance/about/activities/sgp/main_en.htm)

### Comparison of key macroeconomic and budgetary projections<sup>1</sup>

		2004	2005	2006	2007	2008	2010
Real GDP (% change)	<b>CP Nov 2005</b>	<b>2.0</b>	<b>2.4</b>	<b>2.4</b>	<b>1.1</b>	<b>1.6</b>	<b>2.1</b>
	COM Nov 2005	2.1	2.7	2.3	2.1	n.a.	n.a.
	CP Nov 2004	2.2	2.5	1.3	1.9	1.8	1.8
HICP inflation (%)	<b>CP Nov 2005</b>	<b>0.9</b>	<b>1.6</b>	<b>2.0</b>	<b>1.3</b>	<b>1.9</b>	<b>1.8</b>
	COM Nov 2005	0.9	1.7	2.0	1.9	n.a.	n.a.
	CP Nov 2004	1.2	1.7	1.6	1.7	n.a.	1.6
Output gap (% of potential GDP)	<b>CP Nov 2005<sup>2</sup></b>	<b>-0.8</b>	<b>-0.3</b>	<b>0.1</b>	<b>-0.7</b>	<b>-0.9</b>	<b>-0.6</b>
	COM Nov 2005 <sup>6</sup>	-1.3	-0.6	-0.4	-0.4	n.a.	n.a.
	CP Nov 2004 <sup>2</sup>	-0.6	-0.1	-0.5	-0.4	n.a.	-0.4
General government balance (% of GDP)	<b>CP Nov 2005</b>	<b>2.3</b>	<b>3.6</b>	<b>3.1</b>	<b>3.2</b>	<b>2.7</b>	<b>2.9</b>
	COM Nov 2005	2.9	3.7	3.0	2.7	n.a.	n.a.
	CP Nov 2004	1.4	2.2	1.8	1.9	2.2	2.2
Primary balance (% of GDP)	<b>CP Nov 2005</b>	<b>4.7</b>	<b>5.6</b>	<b>4.7</b>	<b>4.1</b>	<b>3.5</b>	<b>3.7</b>
	COM Nov 2005	5.3	5.8	4.9	4.4	n.a.	n.a.
	CP Nov 2004	4.5	4.8	4.5	4.6	n.a.	4.4
Cyclically-adjusted balance (% of GDP)	<b>CP Nov 2005<sup>2</sup></b>	<b>2.8</b>	<b>3.8</b>	<b>3.0</b>	<b>3.6</b>	<b>3.3</b>	<b>3.3</b>
	COM Nov 2005	3.8	4.1	3.3	3.0	n.a.	n.a.
	CP Nov 2004 <sup>2</sup>	1.7	2.0	2.0	2.0	n.a.	2.3
Structural balance <sup>3</sup> (% of GDP)	<b>CP Nov 2005<sup>4</sup></b>	<b>2.6</b>	<b>3.6</b>	<b>2.7</b>	<b>3.3</b>	<b>3.3</b>	<b>3.3</b>
	COM Nov 2005 <sup>5</sup>	3.6	3.9	3.0	2.7	n.a.	n.a.
	CP Nov 2004	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Government gross debt (% of GDP)	<b>CP Nov 2005</b>	<b>42.3</b>	<b>35.6</b>	<b>31.7</b>	<b>28.9</b>	<b>26.5</b>	<b>21.5</b>
	COM Nov 2005	43.2	36.0	33.0	31.5	n.a.	n.a.
	CP Nov 2004	42.3	39.4	37.4	35.3	33.1	28.8

Notes:

<sup>1</sup>The budgetary projections exclude the impact of the Eurostat decision of 2 March 2004 on the classification of funded pension schemes, which needs to be implemented by the time of the spring 2007 notification. Including this impact, the general government balance would be 1.3% of GDP in 2004, 2.7% in 2005, 2.1% in 2006, 2.2% in 2007, 1.7% in 2008 and 1.9% in 2009, while government gross debt would be 43.5% of GDP in 2004, 36.8% in 2005, 32.9% in 2006, 30.1% in 2007, 27.7% in 2008 and 22.7% in 2010.

<sup>2</sup>Commission services calculations on the basis of the information in the programme.

<sup>3</sup>Cyclically-adjusted balance (as in the previous rows) excluding one-off and other temporary measures.

<sup>4</sup>One-off and other temporary measures taken from the programme (0.2% of GDP in 2004 and 2005 and 0.3% in 2006 and 2007; all deficit-reducing).

<sup>5</sup>One-off and other temporary measures taken from the Commission services' autumn 2005 forecast (0.2% of GDP in 2004 and 2005 and 0.3% in 2006 and 2007; all deficit-reducing).

<sup>6</sup>Based on estimated potential growth of 1.9%, 2.1%, 2.1% and 2.1% respectively in the period 2004-2007.

Source:

*Convergence programme (CP); Commission services' autumn 2005 economic forecasts (COM); Commission services' calculations*