Nordic-Baltic Business Report

Well prepared to take on the challenge

- The Nordic and Baltic economies will be hard hit by the Covid-19-induced shock due to their small size and relative openness.
- Strong economic fundamentals and a timely reaction to the health crisis ensure that the countries are in an advantageous position to take on the challenge.
- The crisis gives a chance to push for bolder and greener policies, as well as advance reforms aimed at streamlining the growing public sector and further tailoring the economy and human capital to the digital post-corona world.

Tackling an unprecedented challenge

The nature of the shock that Covid-19 has brought about is very different from previous crises. Tackling and surviving it requires extra-fast thinking, and an innovative government response, as well as digitally apt, creative, and flexible businesses and citizens. The Nordics and Baltics are rather well prepared to take on the challenge.

Virus containment strategies have differed. The Swedish strategy, while softening the blow to the economy, has put stress on the country’s already-pressured health care system. Nordic and Baltic countries overall, though, have so far been relatively successful at controlling the virus and ensuring that the health systems are able to cope with the inflow of patients. Timely action has allowed them to refrain from imposing even more suffocating measures on the economies. Risks, however, remain. While the Nordics boast well-developed and efficient health sectors, the health care system in the Baltics is weak, has been underfinanced and unreformed for many years, and can quickly become overwhelmed if the case count surges.

The abruptness and severity of the economic shock is unprecedented and far greater than that experienced during the global financial crisis. Economies all over the world are hurt via both the export channel and the dramatic fall in domestic demand.

The prospects for export markets seem gloomy – the recovery is projected to be slow all over the world. This paints a bleak background for the small and open economies of the Nordics and Baltics. Norway faces an additional hurdle due to its reliance on oil exports. Some other economies in the region count machinery among their key export products, which can also suffer more due to the long and complicated supply chains. Some respite is to come from such less-affected sectors as food exports and pharmaceuticals, which feature prominently in the export structure of Denmark and the Baltics.
Imbalances were a key feature of pre-2008 times, especially in the Baltics, but the Covid-19 crisis has come at a point when the economies are structurally sounder and, therefore, at a better starting position to weather the storm. Some differences emerge, though. The Baltics have seen a balanced development in the housing market and a lowering of private sector debt. However, in Norway, Sweden, and Denmark household debt levels remain high. The good news is that a credit crunch is unlikely—the region’s financial sector is well capitalised and able to support the economy in its fight against the virus.

Due to previously enacted sound fiscal policies and comparatively low public debt, the region’s economies can alleviate the economic crisis via a wide range of support measures. Even though the implementation of these support mechanisms often leaves much to be desired, the governments are learning fast.

**Don't waste a good crisis**

The post-corona world is one that is likely to see a much greater role of government, the corollary of which is a steep rise in public debt. It is important to use these funds wisely, as well as streamline the public sector in order to increase its efficiency. Strengthening the health care system will be a key priority in all countries. The massive fiscal stimulus should also be geared towards green investment, especially in Norway and Estonia, whose ecological footprint is larger than that of other economies in the region.

The crisis has turbocharged the previous trend of moving towards a more digitalised way of life. This is good news for the Nordics since they are top scorers on digital readiness, while Latvia and Lithuania have some catching up to do in this regard. Within the countries, the less-digitally-savvy individuals and the ones most affected by the crisis are also typically those who are already at the bottom of the income and wealth distribution. Governments, especially in the Baltics, that score low on social inclusion should implement policies to prevent a part of the population from falling even farther behind.

All the region’s economies score well on the World Bank’s *Doing Business*, therefore, they are in a good position to benefit from the shortening of supply chains and likely relocation of production. Attracting new investment is crucial, especially for the catching-up Baltics.

Except for Estonia and Finland, educational outcomes in the region’s economies, as measured by OECD’s PISA are not stellar. Further structural reforms are needed to address this challenge and upskill human capital more broadly to be fit for the future labour market.

The crisis gives the Nordic and Baltic economies a chance to push for bolder policies and reforms that have previously been postponed due to the lack of sense of urgency or political will. As a result, the Nordics and Baltics can emerge from this fight even stronger, more competitive, and more sustainable.

**About the Nordic-Baltic Business Report**

The Nordic-Baltic Business Report takes a broad perspective on the strength and appeal of the Nordic-Baltic region from the business and investor points of view. The Summary Sheet gives an insight into recent macroeconomic and financial sector developments, the long-term sustainability of current trends in environmental protection, social inclusion, governance, and medium-term growth aspects, and the competitiveness of the region’s economies. This report provides an overview of similarities and differences, strengths, and shortcomings for those doing business and considering investment decisions in Estonia, Latvia, Lithuania, Sweden, Denmark, Finland, and Norway.

**Nordic-Baltic Business Report is a product of Swedbank Macro Research**

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### Early Warning Indicators

**General macroeconomic and financial sector developments and internal and external imbalances (2019 or latest available).**

<table>
<thead>
<tr>
<th>Macro stability</th>
<th>Estonia</th>
<th>Latvia</th>
<th>Lithuania</th>
<th>Sweden</th>
<th>Denmark</th>
<th>Finland</th>
<th>Norway</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current account, % of GDP</td>
<td>2.2</td>
<td>-0.5</td>
<td>4.3</td>
<td>3.9</td>
<td>7.8</td>
<td>-0.8</td>
<td>3.9↑</td>
</tr>
<tr>
<td>Wage and productivity growth differential, pp</td>
<td>2.1</td>
<td>1.9</td>
<td>5.9↓</td>
<td>0.1</td>
<td>0.2</td>
<td>2.4</td>
<td>2.4</td>
</tr>
<tr>
<td>Inflation (annual CPI growth), %</td>
<td>2.3↑</td>
<td>2.8</td>
<td>2.3</td>
<td>1.8</td>
<td>0.8</td>
<td>1.0</td>
<td>2.2</td>
</tr>
<tr>
<td>Household consumption and GDP growth differential, pp</td>
<td>-1.2</td>
<td>-0.6</td>
<td>-0.6</td>
<td>0.4</td>
<td>0.0</td>
<td>0.5</td>
<td>0.3-</td>
</tr>
<tr>
<td>Real estate price and GDP growth differential, pp</td>
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<td>-0.2</td>
<td>-0.2</td>
<td>1.0</td>
<td>1.1</td>
<td>-1.7</td>
<td>4.5</td>
</tr>
<tr>
<td>Household lending and GDP growth differential, pp</td>
<td>-1.3</td>
<td>-4.1↑</td>
<td>0.8</td>
<td>1.2</td>
<td>-1.5</td>
<td>0.0</td>
<td>-3.3</td>
</tr>
<tr>
<td>Corporate lending and GDP growth differential, pp</td>
<td>-8.6↓</td>
<td>-8.2</td>
<td>-8.7↓</td>
<td>-0.1</td>
<td>1.5</td>
<td>3.9</td>
<td>7.3</td>
</tr>
<tr>
<td>Government budget balance, % of GDP</td>
<td>-0.3</td>
<td>-0.2</td>
<td>0.3</td>
<td>0.5</td>
<td>3.7</td>
<td>-1.1</td>
<td>2.6</td>
</tr>
<tr>
<td>Public debt, % of GDP</td>
<td>8.4</td>
<td>36.9</td>
<td>36.3</td>
<td>35.1</td>
<td>33.2</td>
<td>59.4</td>
<td>40.6</td>
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### Financial sector stability

<table>
<thead>
<tr>
<th>Estonia</th>
<th>Latvia</th>
<th>Lithuania</th>
<th>Sweden</th>
<th>Denmark</th>
<th>Finland</th>
<th>Norway</th>
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</thead>
<tbody>
<tr>
<td>Tier 1 capital ratio, %</td>
<td>25.5</td>
<td>20.6</td>
<td>18.8</td>
<td>18.6</td>
<td>19.0</td>
<td>18.6</td>
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<tr>
<td>Liquidity coverage ratio, %</td>
<td>152</td>
<td>306</td>
<td>259</td>
<td>179</td>
<td>187</td>
<td>183</td>
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<tr>
<td>Resident loan-to-deposits ratio, %</td>
<td>108</td>
<td>84</td>
<td>81</td>
<td>118</td>
<td>73</td>
<td>143</td>
</tr>
<tr>
<td>Loan overdues &gt; 90 days, % of portfolio</td>
<td>0.4</td>
<td>3.8</td>
<td>1.9</td>
<td>0.6</td>
<td>1.7</td>
<td>1.4</td>
</tr>
</tbody>
</table>

Traffic lights signal the degree of concern. Cut-off values for traffic lights are assigned based on existing regulations, research, historical analysis, and expert judgement. Traffic light interpretation: ![ - no problem, ] - cause for some concern, ![ - increased risk. Arrows indicate improvement ↑ or deterioration ↓ in the traffic light colour from the actual value a year ago.

### Sustained Economic Development Indicators

**Longer-term sustainable economic development (progress towards UN SDGs), % of benchmark**

<table>
<thead>
<tr>
<th>E: Environmental protection (SDGs # 2, 6, 7, 11-15)</th>
<th>Estonia</th>
<th>Latvia</th>
<th>Lithuania</th>
<th>Sweden</th>
<th>Denmark</th>
<th>Finland</th>
<th>Norway</th>
</tr>
</thead>
<tbody>
<tr>
<td>61</td>
<td>72</td>
<td>66</td>
<td>80</td>
<td>89</td>
<td>88</td>
<td>89</td>
<td>91</td>
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<td>72</td>
<td>66</td>
<td>66</td>
<td>89</td>
<td>88</td>
<td>89</td>
<td>92</td>
<td>94</td>
</tr>
</tbody>
</table>

*Benchmark is 90/10th percentile of EU28 in 2015. In total 43 indicators covering all 17 SDGs, aggregated to three pillars. For Nordics: ![ >90% ], ![ 70-90% ], ![ <70% ]. For Baltics: ![ >80% ], ![ 60-80% ], ![ <60% ].

### Competitiveness Indicators

**Country rank in competitiveness, business environment, education, digitalization, innovation, and well-being (number of countries/ regions)**

<table>
<thead>
<tr>
<th>Estonia</th>
<th>Latvia</th>
<th>Lithuania</th>
<th>Sweden</th>
<th>Denmark</th>
<th>Finland</th>
<th>Norway</th>
</tr>
</thead>
<tbody>
<tr>
<td>Global Competitiveness Index 4.0 2019 (out of 141)</td>
<td>31</td>
<td>41</td>
<td>39</td>
<td>8</td>
<td>10</td>
<td>11</td>
</tr>
<tr>
<td>Doing Business 2020 (out of 190)</td>
<td>18</td>
<td>19</td>
<td>11</td>
<td>10</td>
<td>4</td>
<td>20↓</td>
</tr>
<tr>
<td>Corruption Perceptions Index 2019 (out of 183)</td>
<td>18</td>
<td>44</td>
<td>35</td>
<td>4</td>
<td>1</td>
<td>3</td>
</tr>
<tr>
<td>PISA Reading, Mathematics, Science 2018 (out of 79)</td>
<td>5</td>
<td>29↑</td>
<td>33</td>
<td>16</td>
<td>18</td>
<td>10↓</td>
</tr>
<tr>
<td>Digital Economy and Society Index 2019 (out of 28)</td>
<td>8</td>
<td>17</td>
<td>14</td>
<td>2</td>
<td>4</td>
<td>1</td>
</tr>
<tr>
<td>Global Innovation Index 2019 (out of 129)</td>
<td>24</td>
<td>34</td>
<td>38</td>
<td>2</td>
<td>7</td>
<td>6</td>
</tr>
<tr>
<td>World Happiness Index 2020 (out of 156)</td>
<td>51</td>
<td>57</td>
<td>41</td>
<td>7</td>
<td>2</td>
<td>1</td>
</tr>
</tbody>
</table>

Traffic lights show the percentile rank of a country in a ranking: ![ >80% ], ![ 60-80% ], ![ <60% ]. Arrows indicate improvement ↑ or deterioration ↓ in the traffic light colour compared to the previous ranking.

All data recorded as of May 25, 2020.
Estonia: Crisis creates learning opportunities

Doing business in Estonia is easy and straightforward. The public sector is efficient and the tax system favourable. Still, many challenges remain. The economy needs streamlined policies that help companies through this crisis. The unprecedented fiscal stimulus should be used cautiously. Investment in green energy and infrastructure should be increased.

The Great Lockdown showed the importance of digital solutions

Estonia has good prerequisites to go through the corona crisis – empty spaces are plentiful, social distancing is part of the culture, digital solutions are widespread, and the health system is trustworthy. At the peak of the crisis, 60% of hospital beds and 17% of intensive-care beds were occupied. Still, learning points from the crisis are many. The communication by the authorities could have been clearer, restrictions fewer and better targeted, and the activities and messages by different parts of the state better streamlined.

Estonia is a world leader in human capital, digital capability, and ease of doing business. E-identity and other public and private e-systems have helped people working and studying from home. Although doing business in Estonia is relatively easy, the global competitiveness index is dragged down by the small size of the market and the relatively poor health of the society – a result of unhealthy habits, which are partly due to the Soviet past, and long waiting lists for doctor appointments.

Massive fiscal stimulus should be well targeted

The economic impact of this crisis is smaller than what we saw 12 years ago because economic and credit growth have been more balanced. The very low public debt enables the government to borrow and spend on a massive scale. The economy needs measures that help companies survive the short but severe hit, so wage subsidies and other direct support has been well received. At the same time, the demand for loan guarantees, the biggest item in the government support package, has been very modest as demand for credit has dropped in the current uncertain environment. Some of the crisis measures, like the suspension of payments in the 2nd pension pillar or the decrease in the diesel excise tax, do not really ease the pain in the economy right now. In the longer term, public investment in Rail Baltica or better roads, or an even more efficient government sector, would help the economy prosper.

Estonia’s ecological footprint is relatively large, as all its electricity and a large part of its heat energy are produced from local shale oil. Massive fiscal stimulus would be a good chance to invest in green energy and reduce the northeastern region’s dependence on shale oil. Surging unemployment calls for social and labour market policies that help people adapt and find new jobs. So far, jobs have been lost among the most vulnerable, in sectors where the average wage level is one of the lowest: tourism and entertainment. Also, immigration should not be restricted when suitable labour is not available locally.
Latvia: Going more digital

The Latvian economy has taken its lesson from the previous crisis, earning the right to use more flexibility in supporting the economy in the corona-world. The stumbling blocks are the previously insufficient investments in the digital economy and protracted reforms in health care and education.

Old homework done, but digital skills and health care overlooked

The measures to limit the spread of the coronavirus, combined with deteriorating economic sentiment, are projected to result in a sharp fall in GDP in 2020. The light private sector debt burden, an advantage during a downturn, exposes subdued investment over the past decade, especially in R&D, innovation, and digital solutions. Before the pandemic, there was a lack of political will to push the health care reform through. Now, the underfinanced sector could quickly become overwhelmed if the number of Covid-19 cases surged. Luckily, the government has acted swiftly and decisively to mitigate the coronavirus outbreak, reducing the risks to the health care system.

Latvia’s digital preparedness for the stay-at-home economy lags its regional peers. Businesses have been slower to take up digital technologies, while almost half of the population still lacks basic digital skills, undermining productivity. This makes the private sector less flexible and more vulnerable during the pandemic. The good news is that Latvia is scoring relatively well in digital public services and connectivity, making this a good stepping stone for further progress. Furthermore, the financial sector is robust, the economy is much more balanced than in 2008, and public debt is low, allowing ample fiscal stimulus.

Corona helps fight resistance to change

The digitalised are more resilient in corona times and will be quicker to flourish post-crisis. During these couple of months, we have seen even the most reluctant Latvian businesses going more digital at a turbo speed. This not only helps to weather the crisis but also increases competitiveness and boosts productivity in the longer term. However, growing digitalisation, in conjunction with the crisis hitting the least-well-off disproportionately hard, can add to the existing income inequality, as people with poorer digital skills and already lower incomes are left farther behind.

The pandemic has made a very strong case for speeding up the protracted health care reform and increasing the sector’s funding, especially given Latvia’s ageing society. Another lesson is the importance of investing in human capital, digitally apt and flexible, at both individual and government levels. The education reform, currently in progress, is badly needed as the OECD comparisons of educational outcomes show that Latvia is lagging its counterparts in the region. The reform foresees changing the Latvian curriculum away from passive listening to embracing creativity, problem-solving and self-directed learning.
Lithuania: An opportunity to emerge stronger

A balanced economy and comparatively mild health crisis put Lithuania in a good starting position on a path to recovery. A loosened fiscal regime provides an opportunity, if executed competently, to address the problem of underinvestment, to improve competitiveness, and to create a more IT-savvy, dynamic, and inclusive society.

Meeting the crisis on solid foundations

The great shutdown of the economy will make a big dent in economic performance in 2020. However, this time around the Lithuanian economy is in a much better position to weather the storm. Despite the long business cycle, the economy remained balanced, the financial sector is very healthy, and, probably for the first time since independence, the government has the fiscal firepower to enact a meaningful countercyclical policy. Despite the ill-preparedness of the health system to combat the infection, early action on social-distancing measures and the low population density meant that the health situation never got out of control. The benign health situation allows the economy to re-open and bounce back more quickly than Western Europe. While the government managed to deal with the health emergency rather successfully, economic support is more lacklustre and sometimes misguided. A quite wide array of measures was announced quickly, but, due to excessive red tape and lack of administrative capacity, the distribution of support in many cases has been somewhat disappointing. Luckily, the Lithuanian aversion to debt means that businesses and households have met the crisis with strong balance sheets; the solid IT infrastructure has also enabled a lot of people to continue with their jobs from the safety of their homes without much trouble.

An opportunity to fix old problems

The great lockdown, at least temporarily, introduced profound changes in lifestyle around the globe and likely will accelerate trends that were slowly brewing for a while. The shortening of supply chains is imminent, and, due to its favourable business environment and experience in attracting greenfield investment, Lithuania should be well positioned to benefit from a re-shoring of manufacturing. In addition, the reversal migration trends will help in improving the medium-to-long-term growth outlook. The pandemic highlighted the value of good policy and capable public administration, as well as the need to strengthen competences in most areas of the public sector. Hopefully, the massive experiment with digitalisation will not be forgotten once this is over and the best practices will stick. A wise implementation of digital technologies in the health sector could both reduce future risk of epidemics by expanding telemedicine and ease the burden on the health system, resulting in both more affordable and better health coverage. As most countries, Lithuania is planning a major medium-term recovery spending spree. It is an opportunity to improve both physical and digital infrastructure that could facilitate green and sustainable growth. Human capital is just as important. The education, health, and judicial systems should be propelled into the 21st century, not only to improve prospects of economic growth but also to create a more equitable society.
Sweden: Strong position but structural reforms lag

Sweden was well equipped for the crisis, with a highly digital society, strong public finances, and a solid financial sector. But the lack in investments in health and elderly care and the postponed structural reforms are now exposing vulnerable groups. To address these issues are a priority.

Time to pay the price of postponed structural reforms

Following the banking rescue in the 1990s, a fiscal policy framework was introduced. The public finances have since been kept in order, and not even the financial crisis has put a large mark on public debt. Throughout the last years, the issue has rather been that the debt level has been worrisomely low. Despite a strong starting position, both in relation to GDP and public finances, necessary structural reforms on, e.g., the housing market have not been conducted amidst low interest rates. The cost of this is now evident.

The real estate indicator (p. 3) is green, but other data reveal a dysfunctional housing market. Households’ debt level is high (almost 190% of aggregate disposable income), and over the years house prices have increased faster than disposable incomes. Measures that the Financial Supervisory Authority introduced have, on the one hand, increased households’ resilience but, on the other, worsened the possibility for some groups to enter the market, especially in larger metropolitan areas. The corona crisis, which hit hard those people with a weaker footing on the labour market, will raise the entry barriers to the housing market even higher. The Swedish unemployment rate started to increase in 2019 as the labour force grew on the back of more immigrants entering the job market. The job market continues to be polarised, with an employment rate for foreign-born people 10 percentage points below that of domestic-born people (15-74-year olds). Given Sweden’s weak PISA ranking and bad integration, there will continue to be great demand for both labour market, education and housing market reforms ahead. But all is not pitch dark. The financial sector is robust — crucial in times of a crisis when the credit channel must work. The economy is also highly digital, which has simplified the new ways of corona-working.

Ongoing trends likely to be amplified – a green, digital era in the years to come

In times of crises, ongoing trends tend to speed up. The economy was already very digital, but some sectors were lagging on e-commerce, e.g., groceries, and this sector, as well as pharmacy, has attracted new consumers in the crisis. Online shopping will likely increase its market share in less mature sectors. But digitalisation will also grow in importance beyond e-commerce, as many businesses now are up running with remote employees. This will keep demand high for energy and infrastructure investments, not least those of a green kind. The Swedish National Debt Office plans on issuing green bonds of at least SEK 10 billion, but the exact amount is not yet decided, and the overall borrowing requirement in coming years will be high. Fiscal policy will over the years continue to be greenly tilted, but it will also focus on elderly and health care and social inclusion, as inequality, integration, and people’s well-being likely have worsened in the crisis.

**Employment rate, 15-74 years**

<table>
<thead>
<tr>
<th>%, trend adjusted</th>
<th>2005</th>
<th>2010</th>
<th>2015</th>
<th>2020</th>
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<tbody>
<tr>
<td>Domestic born</td>
<td>65</td>
<td>65</td>
<td>65</td>
<td>65</td>
</tr>
<tr>
<td>Foreign born</td>
<td>55</td>
<td>55</td>
<td>55</td>
<td>55</td>
</tr>
<tr>
<td>Total</td>
<td>60</td>
<td>60</td>
<td>60</td>
<td>60</td>
</tr>
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</table>

Sources: Swedbank Research & Macrobond

**Public finances**

<table>
<thead>
<tr>
<th>% of GDP, incl. Swedbank’s forecasts</th>
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<th>98</th>
<th>00</th>
<th>02</th>
<th>04</th>
<th>06</th>
<th>08</th>
<th>10</th>
<th>12</th>
<th>14</th>
<th>16</th>
<th>18</th>
<th>20</th>
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<tbody>
<tr>
<td>Government budget balance</td>
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<td>4</td>
<td></td>
<td></td>
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<td></td>
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<td></td>
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<td></td>
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<tr>
<td>General government debt (Maastricht)</td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>65</td>
</tr>
</tbody>
</table>

Sources: Swedbank Research & Macrobond
**Denmark: In a good position to tackle a health crisis**

The Danish economy is in a better position to deal with the recent crisis than the financial crisis a decade ago. Public finances are sound, the housing market is more balanced, and the labour market has been doing well. In the long-term perspective, broadened domestic investments and upskilling targeted to the needs of digitalisation and automation are crucial.

**Entering the corona crisis from a good starting position**

Compared with the global financial crisis in 2008-2009, when the domestic housing market crash coincided with a collapse in global demand, the Danish economy is in a much better position to face the current crisis. Savings, especially among households, have risen over the recent decade, making households less vulnerable. Also, spending on health care is much higher than the EU average. Denmark’s public finances are sound, creating room for manoeuvre in economic policy. The labour market is functioning well, and Danish politicians have introduced extensive measures to limit the number of layoffs and business closures. We expect a considerable deficit in government finances and a sharp increase in government debt, but the level will continue to be low in an international context.

GDP is expected to contract by 4% this year, when both domestic and global demand drop significantly. The Danish economy relies heavily on international trade and global value chains, as the current account surplus shows. The surplus is to a large extent driven by exports of goods, an increasing proportion of which never crosses the Danish border because the goods are produced in foreign subsidiaries. Broken value chains in the aftermath of the corona crisis could thus have a big impact on the Danish economy. On the other hand, Denmark is more protected from the fall in external demand than more industry-driven countries, such as Finland and Sweden, due to its large pharmaceutical and food industries.

**High competitiveness, but extended investments and targeted education needed**

Overall, the Danish economy is solid and scores well on all relevant macroeconomic, competitiveness, and sustainability indicators. Financial stability is robust, social inequality is low, and Denmark has a strong and high-performing health care system. Denmark also has an ambitious target for reducing greenhouse gas emissions, requiring significant investments and reforms across the economy; this highlights the importance of a green recovery following the corona crisis.

Private investment in research and innovation has picked up since the financial crisis but is concentrated in a small number of large companies. Broadening this investment to a wider range of companies would be needed going forward. The speed-up of digitalisation and automation increase the need for individuals to continually maintain and upgrade their skills. Although the Danish economy scores high on the digital economy index, a relatively low PISA reading is worrisome. In addition, reforms are needed to ensure that the education and the upskilling are targeted to the needs of the future labour market.
Finland: What does not kill you makes you stronger

Finland has an innovative and robust economy and year after year continues to be ranked as one of the best places to live, go to school, and travel. However, before the pandemic Finland was already facing long-term challenges related to its ageing population and sustainability of its public finances. These problems will not magically disappear; instead, the sustainability problems of the public finances will increase massively.

Soaring public debt and price competitiveness issues dominate

Finland entered the pandemic with an already-deteriorating economy based on weak external demand and insufficient productivity growth. During the past few years, Finland has tackled its price competitiveness problems. With the contribution of the Competitiveness Pact, labour costs have been pulled down and the price competitiveness of exports has improved. Recent wage negotiations continue to support cost competitiveness, but not as aggressively as during previous years, and this situation could change fast if wages adjust following the coronavirus outbreak in other countries. Ensuring a competitive exporting sector will continue to be an issue for Finland, with its rigid wage-setting system.

Public finances had started to improve before the coronavirus outbreak but are now deteriorating fast. The public debt-to-GDP ratio is expected to increase to almost 70% in 2020 from levels of around 60% and will continue to worsen. This creates a very difficult situation for the Finnish public economy, which already is under a lot of pressure due to increased expenditures related to the rapidly ageing population. In order to balance its public finances, going forward Finland will need to solve several structural labour market issues and raise labour market participation or increase labour-demand-driven immigration.

Largest reforms usually done under pressure

Although Finland continues to be ranked well in global competitiveness, it has lately experienced a worrisome fall in the ease of doing businesses. The tax burden in Finland (42.4% of GDP in 2018) is among the heaviest in Europe and in the Nordic-Baltic region, but the corporate income tax has been gradually lowered over the long term and has been standing at 20% since 2014. It would be important for Finland to ensure that companies thrive in order to make sure innovations stay high and to return productivity to the growth rates seen before the financial crisis. The coronavirus outbreak challenges the political reform agenda of the Social Democrat-led government. Expanding the tax base might still be on the agenda, but during the coming years raising taxes will not be the first priority. However, it will regain importance once the post-pandemic stimulus phase is over. Finland is a reform-driven, innovative economy that usually manages to implement its largest reforms under heavy pressure and out of necessity. The corona crisis might just create the right environment for pushing through the politically difficult labour market reforms needed to boost long-term growth potential and achieve the ambitious environmental goals of the government.

<table>
<thead>
<tr>
<th>General government gross debt</th>
<th>Finland, Old-Age Dependency Ratio</th>
</tr>
</thead>
<tbody>
<tr>
<td>% of GDP</td>
<td>Ratio of Population Aged 65+ per 100 Population 20-64, Medium Fertility</td>
</tr>
<tr>
<td>80</td>
<td>70</td>
</tr>
<tr>
<td>60</td>
<td>60</td>
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<td>40</td>
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<td>20</td>
<td>40</td>
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<tr>
<td>0</td>
<td>30</td>
</tr>
<tr>
<td>Actual debt/GDP</td>
<td>20</td>
</tr>
<tr>
<td>Debt threshold in SGP</td>
<td>10</td>
</tr>
</tbody>
</table>

Sources: Swedbank Research & Macrobond

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**Norway: Strong economy at a structural level**

The Norwegian economy was well prepared to handle the corona crisis as the health care sector is well developed and government finances are solid. The additional hit delivered by the sharp oil price decline, however, reveals some challenges and will likely intensify discussions about the transition to greener investments. The current use of the Government Pension Fund will mean less welfare for future generations.

**Solid economic and political structures support Norway through the crisis**

With a well-developed health care sector, Norway seems to have been well prepared to handle the corona virus. The government acted quickly and forcefully; it also learned from experiences of other countries, as the disease hit Norway later than other countries. This has allowed the number of infected to stay relatively low and kept the hospitals from becoming overstrained. Additionally, this has allowed lockdown measures to be eased quite quickly.

In terms of the economy, Norway was not only hit by the direct consequences brought by the corona virus, the lockdown measures, and lowered global demand, but also by the sharp decline in the oil price, which will likely affect oil investments negatively for several years to come. We expect GDP to drop by 6% in 2020. However, the Norwegian economy is very strong at a structural level and thus well equipped to handle the crisis. This includes solid government finances, a large Government Pension Fund, robust public institutions, and a focus on political cooperation across political parties during challenging times. Politicians have also largely listened to employer organisations to make the right decisions. Additionally, Norway scores high on digitalisation, which has enabled many workplaces to keep productivity up despite the extensive use of home offices.

**The downturn reveals and reinforces challenges faced**

The Norwegian economy achieves high scores on most macroeconomic, financial stability, sustainability, and competitiveness indicators. We believe that many of the aspects of the economic, as well as social and political structures, will help Norway tackle the crisis well, as was also the case during the financial crisis.

On the other hand, the downturn also reveals and reinforces the challenges that are faced. The most important challenge is that the Golden Age for the oil sector is undoubtedly over. The crisis will likely amplify discussions about the transition to greener investments. The current use of the Oil Fund will mean less welfare for the future generations. If trend growth is to return to where it was before, innovation must be supported. This has been a fact for a long time, but it is being emphasised now. The current account balance, as a share of GDP, has been falling for a while. That trend will continue, unless the growth impulses are intensified in other industries.
Appendix

Early warning indicators
2019 full year data unless stated otherwise
Note: From 2018 to 2019 ABLV bank licence annulment weighed on Latvia’s credit portfolio growth.

A fall from 2017 to 2018 in Estonia and Latvia represents a one-off Luminor corporate portfolio transfer to the parent bank in Sweden.
Graph colours signal the degree of concern. **Green** stands for *no problem*, **yellow** – *cause for some concern*, **red** – *increased risk*.

Data recorded as of May 25, 2020.
Sources: Swedbank Research & Macrobond

**Sustainable economic development indicators**
Swedbank Sustainability Indicators, % of target (2015 or latest available)
Data recorded as of May 25, 2020.
Sources: Swedbank Research & Macrobond

For more information please see

- The latest Swedbank Economic Outlook, May 2020: In the midst of the Corona crisis – the bottom has likely been reached
- In-depth in Swedbank Economic Outlook, August 2019: Macro-ESG – A long-term growth diagnostic (p.24)
- Macro Focus, March 2019: What central banks can do to fight climate change
- In-depth in Swedbank Economic Outlook, January 2019: Clash of the titans – central banks and climate change (p.22-23)
- In-depth in Swedbank Economic Outlook, August 2018: Cost of inaction on climate change is rising (p.22-23)
- Macro Focus, June 2018: Swedbank’s Sustainability Indicators for the Nordics and the Baltics (updated tables, extended to the Nordics)
- Macro Focus, January 2018: Swedbank’s Sustainability Indicators: towards the 2030 Agenda
- In-depth in Baltic Sea Report, December 2017: Sustainable development in the Baltics and Sweden – where do we stand?
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