



# NORDIC & SWISS ECONOMIC OUTLOOK

## Nordics set for shallowest recessions in Europe

- The Nordic economies have weathered the Covid crisis comparatively well, and if our above-consensus forecasts for GDP growth this year prove accurate, the region will see some of the smallest falls in output in the whole of Europe. We forecast output in Denmark and Norway to fall by about 3% this year, and while Sweden has not been unscathed, despite its light-touch lockdown, the fact that the economy grew in Q1 sets the stage for an even smaller contraction. Switzerland has been hit harder, but it is facing a comparatively modest downturn by European standards, more akin to that in Germany than the worst-affected countries.
- That said, while the Nordic region has got off lightly, the legacy of Covid will persist and activity everywhere is likely to remain below its pre-virus trend throughout our forecast horizon. Accordingly, price pressures will remain too low for comfort across the board and central banks will be in no rush to tighten policy. We doubt that the Norges Bank will hike its key policy rate during our forecast horizon, and the SNB is set to stay on hold well beyond that. And in contrast to the market, we think that the Riksbank will cut its repo rate to -0.25% later this year or in early-2021.
- **Markets Overview** – Recovery in sentiment to benefit Nordic currencies.
- **Economic Overview** – Comparatively resilient, but still plenty for policymakers to do.
- **Switzerland** – On a similar trajectory to Germany.
- **Sweden** – Best of a bad bunch in Europe.
- **Norway** – Bouncing back, but energy shake-out to constrain growth.
- **Denmark** – Quick lockdown exit helps to limit slump.

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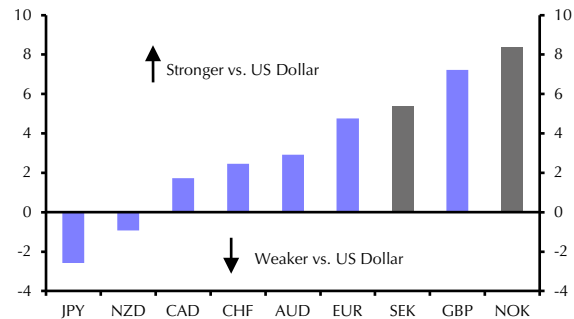


## Markets Overview

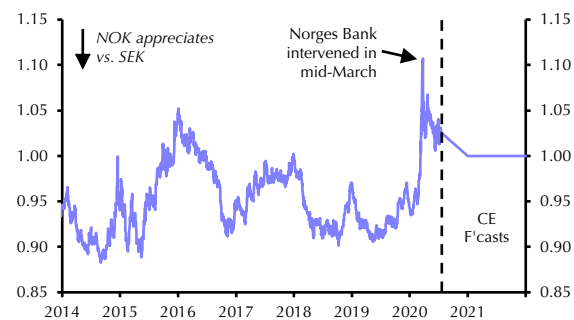
### Recovery in sentiment to benefit Nordic currencies

- We think that market sentiment will improve further during the rest of the year, which should support the Swedish krona and Norwegian krone and further reduce upward pressure on the Swiss franc.
- Global risk sentiment has been the main driver of the Nordic currencies in recent months, and we expect a continued recovery in risk appetite to result in them being amongst the best performing G10 currencies by year-end. (See Chart 1.) If our forecasts for the Riksbank to cut its repo rate again, and oil prices to edge up to \$45pb by year-end prove accurate, the NOK would benefit more than its Swedish cousin, and we forecast it to recover back to parity with the SEK in H2. (See Chart 2.)
- Meanwhile, the steps towards fiscal union in the EU have relieved upward pressure on the Swiss franc and allowed the SNB to dial down its interventions in the FX market. (See Chart 3.) If the franc edges lower over the next 18 months, as we expect, policymakers should largely be able to keep their powder dry.
- The spread between Swiss 10-year bonds and their German equivalents has collapsed to zero as Bunds have benefited more than their Swiss counterparts from safe-haven demand. We expect Swiss bonds to trade in line with Bunds in H2, but the spread is likely to widen again next year. Meanwhile, long-term yields are set to stay at zero in Sweden, and at very low, albeit positive, levels in Norway.

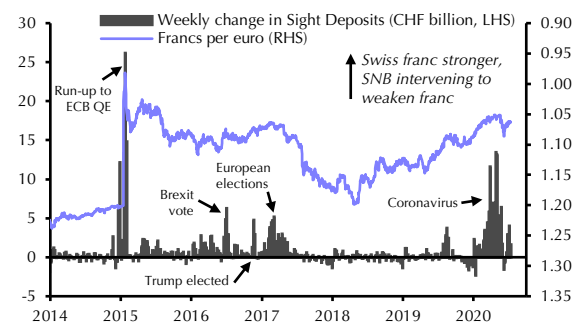
**Chart 1: G10 Currencies Vs. US Dollar**  
(CE Forecast Chg. Between 20<sup>th</sup> July & End-2020, %)



**Chart 2: Norwegian Krone per Swedish Krona**



**Chart 3: Swiss Francs per Euro & SNB Interventions**



Sources: Refinitiv, Capital Economics

**Table 1: Key Market Forecasts**

End of Period	Currencies (per Euro)					Ten-Year Bond Yields (%)				
	2019	Latest*	2020	2021	2022	2019	Latest*	2020	2021	2022
Switzerland	1.05	1.07	1.10	1.10	1.12	-0.47	-0.44	-0.25	-0.50	-0.50
Sweden	10.80	10.25	10.25	10.00	10.00	0.15	-0.09	0.00	0.00	0.00
Norway	11.20	10.52	10.25	10.00	9.75	1.58	0.66	0.75	0.75	1.00
Denmark	7.46	7.45	7.46	7.46	7.46	-0.15	-0.34	-0.25	-0.25	-0.25

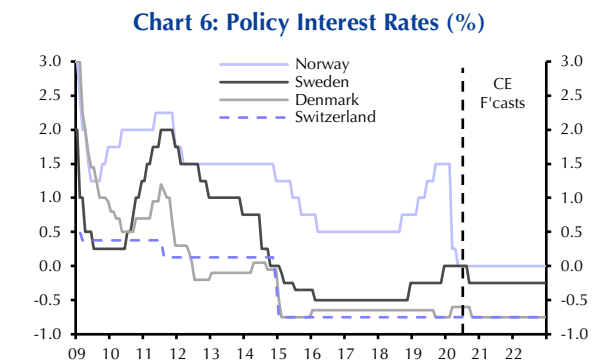
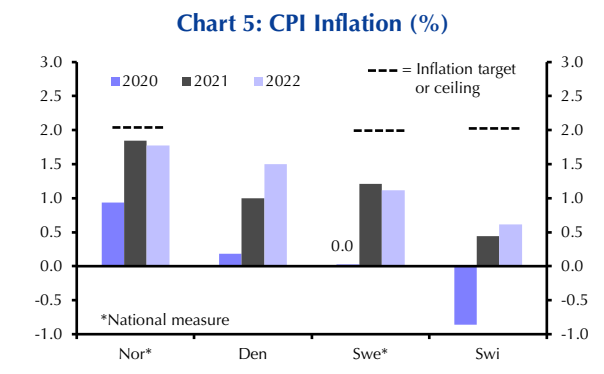
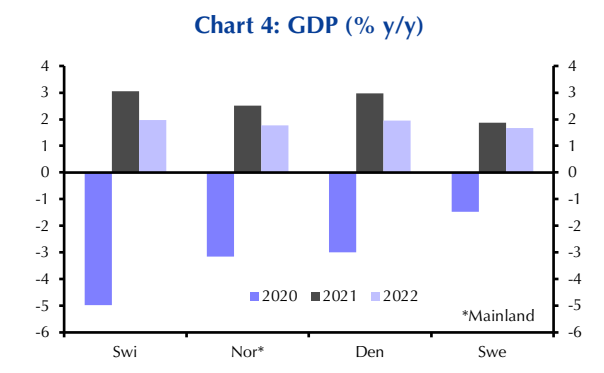
Sources: Refinitiv, Capital Economics. \*21<sup>st</sup> July



## Economic Overview

Comparatively resilient, but still plenty for policymakers to do

- A combination of decisive policy responses and structural factors will limit the damage wreaked by Covid in the Nordic economies – particularly relative to the euro-zone. Nonetheless, policymakers will not rest on their laurels and tighter policy is years away.
- The Nordic economies have bounced back quickly, and our 2020 GDP forecasts are now above consensus. We expect output in Denmark and Norway to contract by 3% this year, and Sweden is likely to fare even better. (See Chart 4.) Switzerland has been hit harder, but it is better placed than the worst-affected countries in Europe.
- That said, output everywhere is likely to remain below its pre-Covid trend throughout our forecast horizon. Previous falls in the value of the krone are boosting inflation in Norway, price pressures will remain too low for comfort across the board. (See Chart 5.)
- Against this backdrop, the SNB is set to keep its policy rate on hold at -0.75% until later this decade at least. And having slashed its key interest rate from 1.50% to zero this year, we doubt that the Norges Bank will hike rates during our forecast horizon. Meanwhile, although the Riksbank has done everything but touch interest rates so far, we think that it will cut its repo rate back into negative territory later this year, or in early 2021. (See Chart 6.)



Sources: Refinitiv, Capital Economics

Table 2: Key Economic Forecasts

	GDP (% y/y)				Inflation (%)				Policy Rates (%)			
	2019	2020	2021	2022	2019	2020	2021	2022	2019	2020	2021	2022
Switzerland	0.9	-5.0	3.0	2.0	0.4	-0.9	0.4	0.6	-0.75	-0.75	-0.75	-0.75
Sweden	1.3	-1.5	2.0	1.7	1.7	0.5	1.5	1.5	0.00	-0.25	-0.25	-0.25
Norway*	2.4	-3.0	2.5	1.8	2.3	1.0	2.0	2.0	1.50	0.00	0.00	0.00
Denmark	2.3	-3.0	3.0	2.0	0.7	0.2	1.0	1.5	-0.75	-0.75	-0.75	-0.75
Euro-zone	1.2	-7.5	5.0	1.5	1.2	0.4	1.0	1.3	-0.50	-0.50	-0.50	-0.50

Sources: Refinitiv, Capital Economics. \*Mainland GDP



## Switzerland

### On a similar trajectory to Germany

- **The Swiss economy has been hit harder than the Nordics, but the contraction in output this year is still likely to be comparatively modest by the standards of the euro-zone, and on par with Germany. In any case, the SNB will remain poised to resist bouts of upward pressure on the franc over the coming years.**
- Swiss GDP contracted by 2.6% q/q in Q1, driven, unsurprisingly, by a sharp fall in services following the virus-related lockdown. (See Chart 7.) Activity in the retail sector has bounced back since restrictions started to be eased (see Chart 8) and the fact that the services PMI rebounded in June suggests that activity gathered momentum going into the third quarter. (See Chart 9.)
- That said, other parts of the economy will take much longer to recover, not least the beleaguered tourism and hospitality sectors; while flight numbers have increased since European borders reopened, they are still less than half their year-ago levels. (See Chart 10.)
- Moreover, as in Germany, the downturn in manufacturing will prove harder to shake off. (Again, see Chart 9.) While the pharmaceutical sector may allow Swiss industry to outperform its German counterpart in the near term, as it did between 2018 and 2020 (see Chart 11), the bulk of firms in the industrial sector, which are more dependent on regional supply chains and demand, will struggle.
- On a positive note, officials' efficient policy response should help to reduce scarring effects. This includes the effective manner in which loans have been channelled to companies, and the extensive short-time working scheme, whose eligibility period will be extended to 18 months later this year, and will avoid as steep a

rise in the jobless rate as seems likely in other countries.

- Previous increases in the value of the franc drove core inflation to a 54-month low of -0.8% in June. While downward pressure on inflation from imported prices will soon start to fade (see Chart 12), underlying inflation will remain below zero into mid-2021 and will keep the SNB in vigilant mode.
- The baby steps towards EU fiscal union have taken the pressure off the franc since mid-May and have allowed the SNB to dial back its FX interventions. (See Chart 13.) If our forecast for the currency to edge lower against the euro in H2 proves accurate, policymakers should be able to remain largely on the sidelines of the FX market. (See Chart 14.)

**Table 3: Key Forecasts (% y/y, unless stated)**

	Ave.		Forecasts		
	09-18	2019	2020	2021	2022
GDP	1.5	0.9	-5.0	3.0	2.0
Private cons'ptn	1.5	1.1	-6.5	3.7	1.6
Total fixed invest.	1.8	0.7	-5.8	4.0	2.1
Gov't cons'ptn	1.6	1.3	5.8	3.2	1.0
Dom'stic demand	1.6	1.2	-4.8	3.7	1.7
Exports	3.0	0.6	-6.0	5.1	1.7
Imports	2.6	-1.4	-8.1	7.2	1.3
Current account <sup>1</sup>	9.8	10.4	5.0	5.0	7.5
HICP	0.0	0.4	-0.9	0.4	0.6
CPI	0.1	0.4	-0.9	0.4	0.6
Core CPI	0.1	0.4	-0.5	0.1	0.3
Employment	1.5	0.8	0.2	0.1	1.3
Unemp. Rate <sup>2</sup>	3.1	2.5	3.3	3.7	3.0
Gen'l gov't bal. <sup>1</sup>	0.5	0.9	-7.5	-3.0	0.0
Gen'l gov't debt <sup>1</sup>	43	39	48	50	50
10-yr bond yields <sup>3,4</sup>	0.54	-0.51	-0.25	-0.50	-0.50
Policy Rate <sup>3,4</sup>	-0.18	-0.75	-0.75	-0.75	-0.75
Francs per euro <sup>4</sup>	1.20	1.09	1.10	1.10	1.12

Sources: Refinitiv, Capital Economics

1) % of GDP, 2) % yr avg, 3) %, 4) end year.



# Switzerland Charts

Chart 7: Contributions to GDP Growth (% pts)

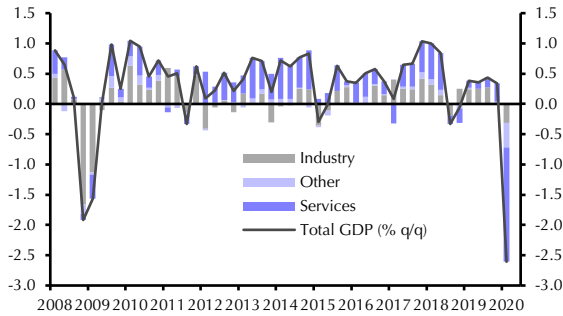


Chart 8: Retail Sales Volumes (SA, Feb. 2000 = 100)

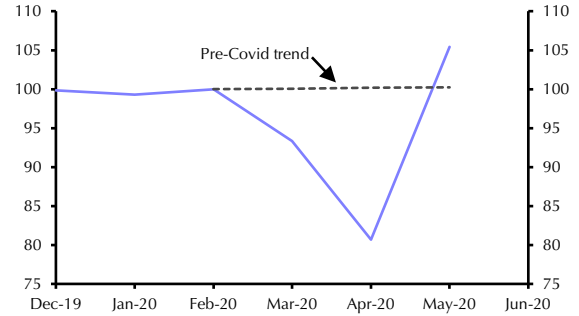


Chart 9: Switzerland PMIs

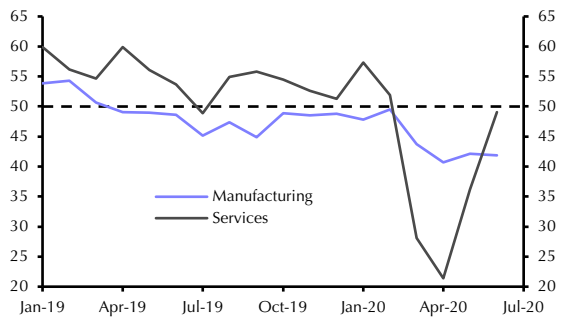


Chart 10: Total Flights Operated in Switzerland (7-day Moving Average, % y/y)

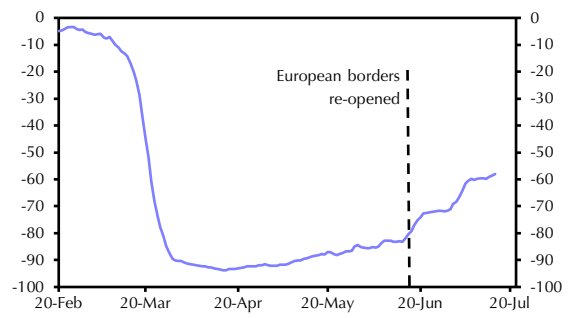


Chart 11: Manufacturing GVA (Jan. 2015 = 100)

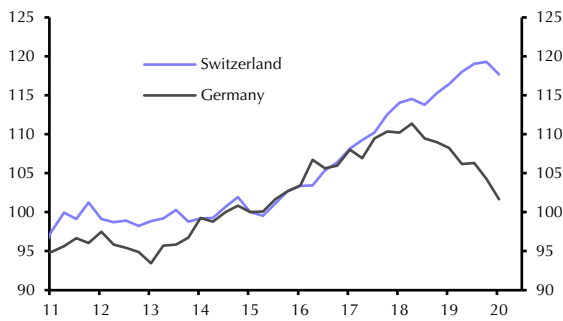


Chart 12: Imported Products Prices & Swiss Francs per Euro (% y/y)

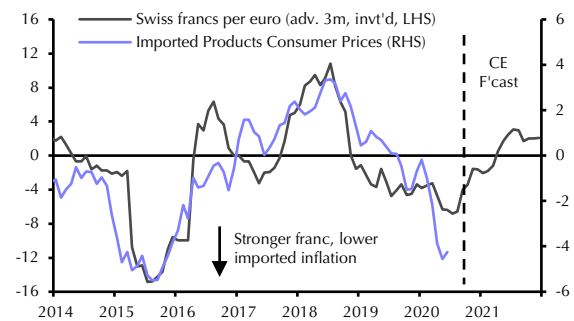


Chart 13: Swiss Francs per Euro & SNB Interventions

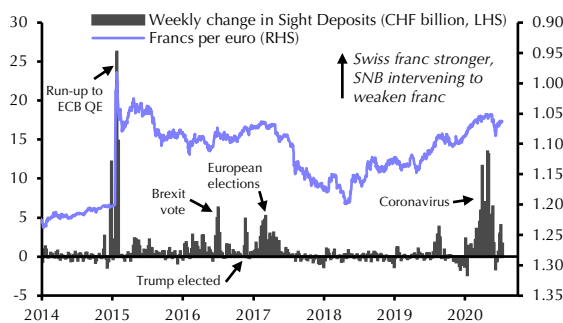
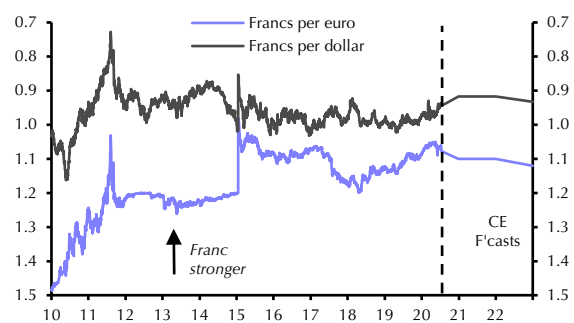


Chart 14: Swiss Franc Exchange Rates



Sources: Bloomberg, Refinitiv, Capital Economics



## Sweden

### Best of a bad bunch in Europe

- **The Swedish economy has weathered Covid well, thanks in part to the government's light-touch lockdown, and our forecast of a 1.5% drop in GDP this year is well above consensus. Nonetheless, with inflation set to remain stubbornly low, we think that the Riksbank will cut its repo rate back below zero before long and will probably expand its balance sheet even further.**
- Sweden's economy has not been immune to Covid, with consumers cutting discretionary spending even as many shops and restaurants have remained open. That said, the fact that Sweden was the only major economy to grow in Q1 (see Chart 15) does wonders for the economic arithmetic.
- Moreover, although activity did not bounce back in May in the same way as it did for countries that imposed lockdowns, the overall decline in private sector output is consistent on past form with a comparatively modest 4% contraction in GDP in Q2 – about one-third of the drop that we forecast in the euro-zone. (See Chart 16.) The fact that schools remained open throughout the pandemic has helped to reduce the amount of lost working time because of the virus. (See Chart 17.)
- Of course, the outlook is not without its challenges, particularly because the high prevalence of Covid in Sweden raises the possibility of the limited restrictions being tightened. (See Chart 18.) The fact that neighbouring countries have so far kept borders closed to Swedes will exacerbate pressure on the hospitality sector and adds to headwinds for exports, which are already impaired by weakness in key markets. (See Chart 19.) Meanwhile, although the government may use some of its fiscal space to cut income taxes,

consumer spending growth will be constrained if low wage rises are locked in during the delayed round of wage negotiations, scheduled for the autumn, as appears likely.

- In any case, while the economy has dodged a bullet, the sharp drop in resource utilisation still suggests that core price pressures will remain stubbornly low for a prolonged period. (See Chart 20.)
- Against this backdrop, we suspect that the Riksbank will extend its asset purchases beyond mid-2021 (see Chart 21), and also cut the repo rate back below zero later this year. And while the krona is likely to grind a bit higher if global sentiment continues to improve, we think that it will underperform the Norwegian krone in H2. (See Chart 22.)

**Table 4: Key Forecasts (% y/y, unless stated)**

	Ave.		Forecasts		
	09-18	2019	2020	2021	2022
GDP	2.0	1.3	-1.5	2.0	1.7
Private cons'ptn	2.2	1.2	-2.7	2.5	1.8
Total fixed invest.	2.5	-1.1	-2.2	2.9	2.4
Gov't cons'ptn	1.5	0.5	0.6	1.3	0.9
Dom'stic demand	2.2	0.2	-2.5	2.3	1.7
Exports	0.3	-1.0	-4.8	0.8	1.7
Imports	2.9	1.9	-7.3	1.7	1.9
Current account <sup>1</sup>	4.5	4.5	2.5	2.5	3.0
CPIF	1.4	1.7	0.5	1.5	1.5
CPIF ex. energy	1.4	1.6	1.3	1.5	1.5
Employment	1.0	0.6	-1.0	0.7	1.2
Unemp. Rate <sup>2</sup>	7.6	6.8	8.3	8.3	7.9
Gen'l gov't bal. <sup>1</sup>	-0.2	0.4	-7.5	-2.5	0.0
Gen'l gov't debt <sup>1</sup>	40	37	45	45	44
10-yr bond yields <sup>3,4</sup>	1.59	0.15	0.00	0.00	0.00
Repo Rate <sup>3,4</sup>	0.32	0.00	-0.25	-0.25	-0.25
Krona per euro <sup>4</sup>	9.38	10.51	10.25	10.00	10.00

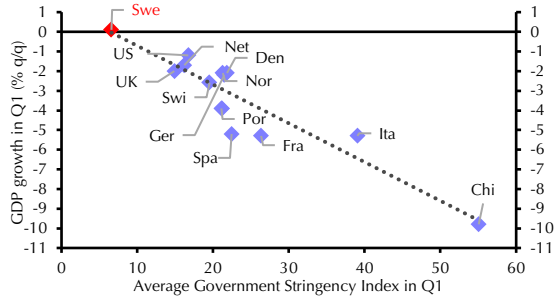
Sources: Refinitiv, Capital Economics

1) % of GDP, 2) % yr avg, 3) %, 4) end year.

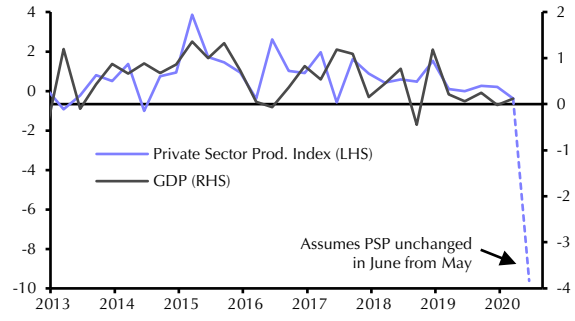


# Sweden Charts

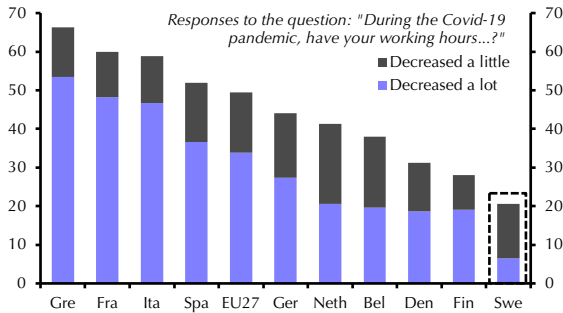
### Chart 15: Q1 GDP & Oxford University Stringency Indicator



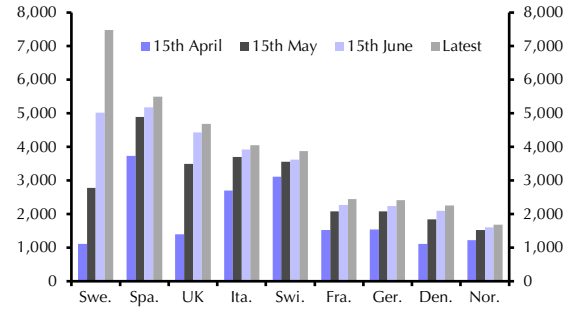
### Chart 16: Private Sector Production & GDP (% q/q)



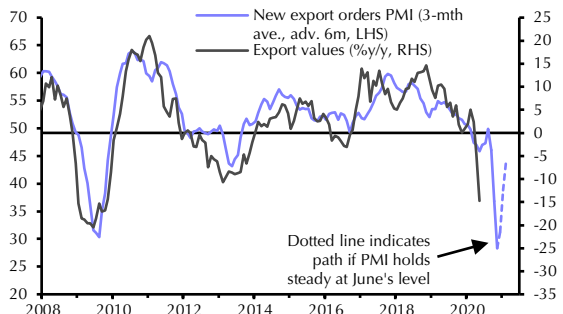
### Chart 17: Changes In Working Time Due to Covid-19 (% Share of Survey Respondents)



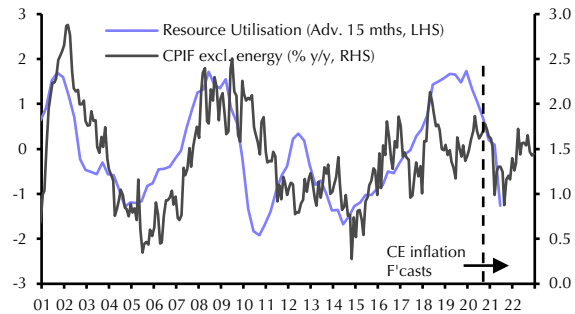
### Chart 18: Confirmed Virus Cases (Per Million Population)



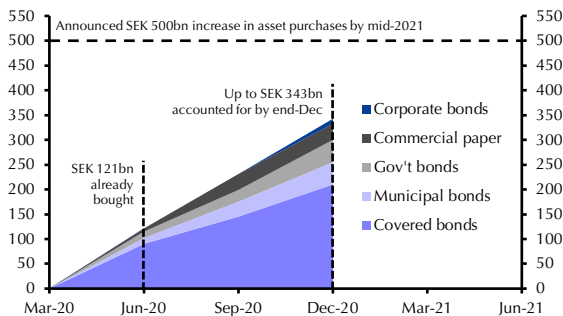
### Chart 19: Goods Exports & New Export Orders



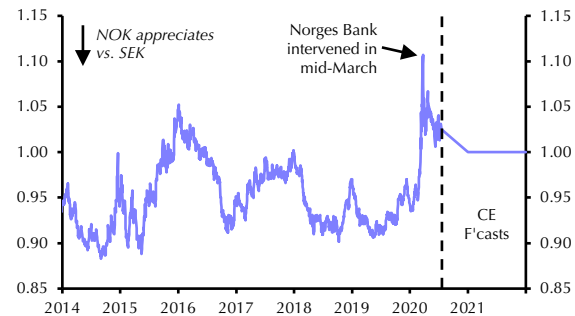
### Chart 20: Resource Utilisation & Core Inflation



### Chart 21: Riksbank Net Asset Purchases (SEK Billion)



### Chart 22: Norwegian Krone per Swedish Krona



Sources: Refinitiv, Riksbank, Eurofound, University of Oxford, CE



# Norway

## Bouncing back, but energy shake-out to constrain growth

- **The downturn in the Norwegian economy has been cushioned by the chunky official policy response, although planned cuts to investment in the energy sector will pose a headwind next year. The Norges Bank has a tendency of going against the grain, but we doubt that it will be able to raise its key interest rate during our forecast horizon.**
- The economy is operating in “two-speed” mode, with ‘everyday’ activity appearing to have gathered pace in June as restrictions continued to be eased. Having fallen by 11% over the course of March and April, we expect mainland GDP to have recovered to about 3% of its January peak in June. (See Chart 24.)
- That said, other parts of the economy, including tourism and firms exposed to weakness in the energy sector, face a longer path back to normality. The sharp cuts to oil production in June as part of OPEC+ package and the prospect of big reductions in energy investment will continue to pose headwinds for these companies in H2 and 2021. (See Chart 24.)
- All told, while a chunky fiscal stimulus has helped to prevent an even deeper downturn, the rebound next year is likely to lag behind that in Denmark, say. Moreover, although the unemployment rate has dropped back sharply since its March peak, we think progress from here will slow and it will remain above its pre-crisis level over the coming years.
- Previous declines in the krone will continue to put upward pressure on inflation in H2. (See Chart 25.) Nonetheless, the Norges Bank will look through this, and we expect policymakers to leave the deposit rate on hold at zero throughout our forecast horizon.

Chart 23: Monthly GDP (Jan. 2020 = 100)

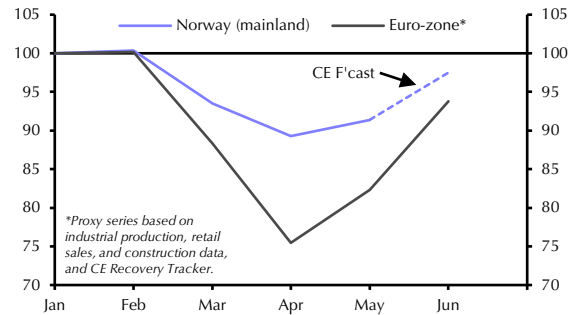


Chart 24: Oil Investment (% y/y)

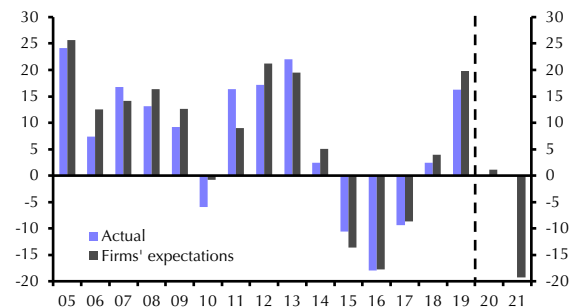
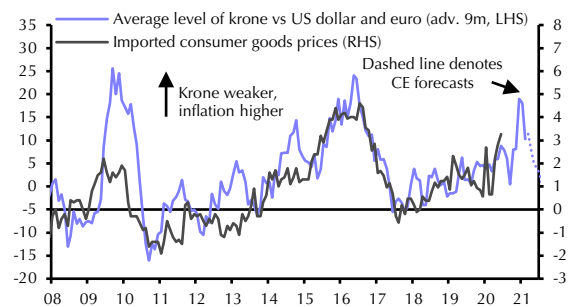


Chart 25: Krone Exch. Rate & Imported Goods Prices



Sources: Refinitiv, Google, Apple, Moovit, Capital Economics.

Table 5: Key Forecasts (% y/y, unless stated)

	Ave. 09-18	2019	Forecasts		
			2020	2021	2022
Mainland GDP	1.7	2.4	-3.0	2.5	1.8
Private cons'ptn	2.3	1.8	-8.1	2.3	1.6
Total fixed invest.	1.7	4.3	-5.0	1.6	2.3
Net trade effect	-0.3	-0.7	3.3	0.3	-0.1
Unemp. rate <sup>1</sup>	3.8	3.7	5.4	5.0	4.5
CPI-ATE	2.1	2.2	2.7	2.0	2.0
Gen'l gov't bal. <sup>2</sup>	9.1	8.8	2.5	3.0	5.0
Gen'l gov't debt <sup>2</sup>	35	41	45	37	36
Current account <sup>2</sup>	9.2	4.2	0.0	1.5	3.0
10-yr bond yield <sup>3</sup>	2.34	1.58	0.75	0.75	1.00
Key Policy Rate <sup>3</sup>	1.23	1.50	0.00	0.00	0.00

Sources: Refinitiv, CE. 1) % year avg., 2) % of GDP. 3) %-year end





# Denmark

## Quick lockdown exit helps to limit slump

- **The Danish economy has bounced back since restrictions were eased, but continued weakness in key export markets will weigh on its recovery over the coming years.**
- Having been one of the first countries to impose and to lift virus-related restrictions, Denmark is likely to see a comparatively small decline in GDP in Q2. Indeed, high frequency data suggest that the domestic economy troughed in April but has rebounded quickly since. (See Chart 26.)
- Exports will continue to face headwinds from the deeper recessions in key trading partners, and, as elsewhere, there is a risk that unemployment will rise next year as short-time work schemes begin to expire.
- That said, the comparatively small share of workers on temporary contracts in Denmark (see Chart 27) suggests that the risk of a sizeable delayed jump in unemployment is lower than in the euro-zone. All told, we expect GDP in Denmark to contract by about 3% this year, as in Norway.
- Denmark’s Nationalbank (DNB) raised its Certificates of Deposit rate from -0.75% to the heady heights of -0.60% earlier this year to support the krone. The currency has appreciated since then (see Chart 28) and is likely to remain above the centre-point of its trading band with the euro if investor risk sentiment continues to improve over the rest of the year, as we expect. Against this backdrop, we would not be surprised to see the DNB cut rates again before long. We have pencilled in a 15bp rate cut, probably in Q4, which would reverse the hike earlier this year and reinstate the 25bp interest rate differential with the ECB.

Chart 26: CE Recovery Tracker

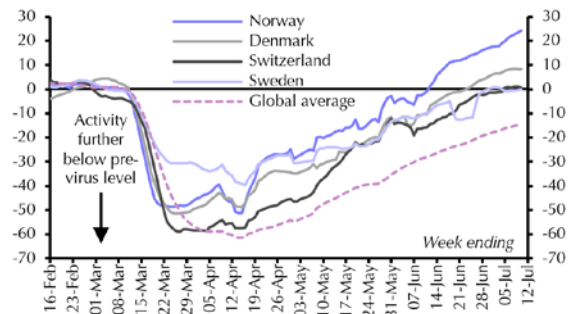


Chart 27: Temp. Contracts (% of Employed, 2019)

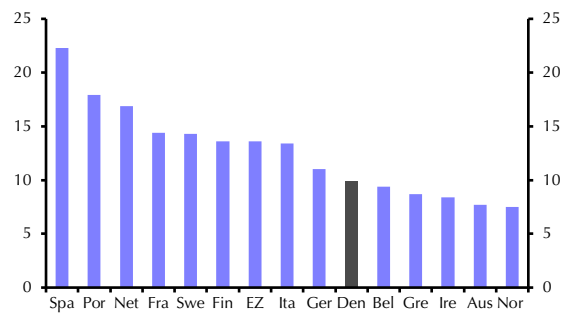
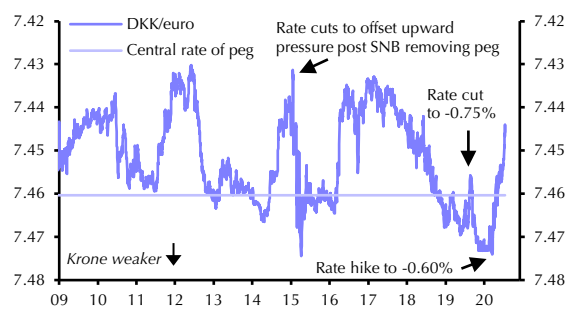


Chart 28: Danish Krone per Euro



Sources: Refinitiv, Eurostat, Moovit, Google, Apple, CE.

Table 6: Key Forecasts (% y/y, unless stated)

	Ave.	Forecasts			
	09-18	2019	2020	2021	2022
GDP	1.1	2.3	-3.0	3.0	2.0
Private cons'ptn	0.8	2.2	-3.1	2.8	2.0
Total fixed invest.	1.3	2.4	-5.1	3.1	1.0
Net trade effect	0.2	0.8	-0.3	0.8	0.8
Unemp. rate <sup>1</sup>	6.7	5.0	5.0	6.0	5.5
HICP	1.1	0.7	0.2	1.0	1.5
Gen'l gov't bal. <sup>2</sup>	-1.0	3.7	-7.5	-2.5	-2.0
Gen'l gov't debt <sup>2</sup>	41	33	42	43	43
Current account <sup>2</sup>	7.0	7.7	-1.0	3.5	4.0
10-yr bond yield <sup>3</sup>	1.39	-0.15	-0.25	-0.25	-0.25
Key Policy Rate <sup>3</sup>	-0.11	-0.75	-0.75	-0.75	-0.75

Sources: Refinitiv, CE. 1) % year avg., 2) % of GDP. 3) %-year end



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