Nordea

ECONOMIC OUTLOOK

MARCH 2015

Unconventional times

Cyclical recovery

The ailing world economy remains on the right track, well aided by extremely accommodative monetary policies and low oil prices. We now also see signs of the Euro-area economy gaining momentum.

Sub-zero rates and QE in the Nordics

Denmark and Sweden play along the larger economies with unconventional policies. Norway may have to follow suit soon.

Data overview

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Data sources:

Data sources are Macrobond, national statistical bureaus and own calculations unless otherwise noted.

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Global overview

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Unconventional times

The ailing world economy remains on the right track, well aided by extremely accommodative monetary policies and low oil prices. Especially the Anglo-Saxon economies, the US and the UK, got off to a good start to 2015, and we now also see signs of the Euro-area economy gaining momentum. But the Emerging Markets economies are struggling with lacklustre growth and many, including China and Russia, face a period of structural slowdown.

It is also becoming increasingly clear that despite the improved outlook global growth will have to be measured at a lower scale than before the Great Recession. Due to factors such as the demographic trends in the Western world, low investment activity and declining global trade growth, secular stagnation has re-emerged as a theme that all economic policy-makers will have to take into consideration.

Another concept entering economic theory and practice over the past few years is quantitative easing (QE). This is a non-conventional monetary policy tool. It means that a central bank allows its printing press to run at high speed and uses the new money to buy e.g. government and mortgage bonds. Thereby it can keep interest rates low and, as a positive side-effect, cause its currency to weaken. QE is a way of stimulating economic growth and boosting inflation – if so desired by central banks with inflation-targeting strategies. Over the past years this type of monetary policy has been relatively successful in the US, the UK and Japan, but quantitative easing programmes also present a significant risk to monetary and financial stability if they are not exited in time. The reason is that an overly long period of ultra-low interest rates and ample liquidity is bound to lead to high inflation and/or bubble-like conditions in e.g. the housing or equity markets.

Recently, the ECB launched a huge QE programme that took effect on March 9. Prior to that, the ECB had brought its deposit rate into negative territory to weaken the euro and stimulate lending activity in the Euro area.

The bank has announced that the QE programme will remain in place at least until September 2016; the precise timing of its exit depends on how inflation develops from the currently far too low level. This means that the Euro area is facing a long period of ultra-low interest rates – and an inherent risk of mispricing of financial and real assets. The fact that the individual Euro-area countries are at different stages in the economic cycle does not make the challenge any easier for the ECB.

Also the Nordic central banks have had to resort to non-traditional means. Despite high economic growth the Swedish Riksbank has slashed its policy rate to below zero and launched an admittedly limited QE programme in an effort to drive inflation back up near the 2% target.

After many years in the slow lane the Danish economy has finally returned to the growth track. The Danish central bank has had to realise that new monetary policy instruments are now needed to defend its fixed exchange rate regime when the reference country for its currency peg introduces negative interest rates and quantitative easing measures.

In none of these countries do real economic developments call for interest rates in negative territory, which illustrates the monetary policy challenges that small economies face in a globalised world no matter what their monetary policy regime is.

As a result of the slowdown of the Norwegian economy caused by the sharp drop in oil prices, even Norges Bank may be forced to cut its policy rate sharply. Norges Bank has an inflation-targeting strategy, and it is definitely possible that inflation in Norway will decline to a level where the bank will have to slash rates by more than seems justified by real economic developments.

Among the Nordic countries, it is actually only Finland that can be said to have a need for a highly expansionary monetary policy line. The fact that the rate of inflation in Finland is one of the highest in the Euro area merely goes to show that economic paradoxes are still not a thing of the past.

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The inflation game

- Sustained consumer spending
- More benign prospects for exports
- Riksbank to keep SEK weak near term
- Inflation up, but will not reach 2% target

Hopes of more broadly based recovery

The Swedish economy has performed well over the past couple of years. GDP growth has been around 2% annually and employment has risen sharply. Economic growth has been driven by domestic demand, while exports have shown a weak trend.

However, towards the end of 2014 exports showed signs of improving. And with the plunge in oil prices and the low level of interest rates, the foundation for a recovery of the global economy has improved. Hence, prospects for Swedish exports appear to brighten. Also the weak Swedish krona is a welcome relief for the hard-pressed exporters. But due to persistent structural problems in the Euro area and subdued growth in the neighbouring Nordic countries, exports will grow relatively slowly. Still, with these additional drivers GDP growth will accelerate this year and next year.

Households slightly cautious

In recent years households have been the key growth driver of the Swedish economy. All components relating to household demand, such as retail sales, car sales and residential construction have increased sharply.

Considering the current strong financial shape of households thanks to rising disposable incomes, high savings and sharply rising asset prices, consumer demand could have been even stronger. This shows through in the confidence readings, which reflect stronger pessimism than normally. The main reasons for this are probably the current geopolitical tensions and economic uncertainties globally.

Domestic growth engines

Going forward, several uncertainties will likely remain. But if the global economy improves in line with expectations and employment in Sweden continues to increase, they should provide a boost to overall sentiment.

The Swedish Financial Supervisory Authority's stricter amortisation requirements are not likely to have any significant dampening effect on home prices, credit growth or household consumption. And we do not assume there will be any further measures aimed at restricting household borrowing over the forecast period. Therefore, households should remain a key engine of growth over the forecast horizon.

Other growth engines include government consumption and mounting investment activity. However, the latter relies on a sustained strong trend in domestic construction, while the recovery of investment in the export sector will progress only slowly.

Modest pay rises despite improved labour market

The number of people with jobs rose 1.0% in 2013 and no less than 1.4% in 2014, and current indicators point to a sustained strong trend. Unemployment is down, but as a result of a sharp increase in labour supply, the unemployment rate is declining only slowly.
There are signs that structural unemployment has in-

Sweden: Macroeconomic indicators (% annual real changes unless otherwise stated)

	2011 (SEKbn)	2012	2013	2014	2015E	2016E
Private consumption	1,693	0.8	1.9	2.4	2.5	2.4
Government consumption	921	1.1	0.7	1.9	1.9	1.0
Fixed investment	830	-0.2	-0.4	6.5	4.1	4.0
- industrial investment	170	-3.1	-1.4	5.4	-0.4	4.7
- residential investment	141	-11.8	2.1	20.3	13.9	4.6
Stockbuilding*	41	-1.1	0.1	0.2	0.1	0.0
Exports	1,707	1.0	-0.2	3.3	5.6	5.1
Imports	1,535	0.5	-0.7	6.5	5.6	5.0
GDP		-0.3	1.3	2.1	2.9	2.6
GDP, calendar adjusted		0.1	1.3	2.3	2.7	2.4
Nominal GDP (SEKbn)	3,657	3,685	3,775	3,908	4,079	4,244
Unemployment rate, %		8.0	8.0	7.9	7.8	7.6
Employment, % y/y		0.7	1.0	1.4	1.5	0.9
Consumer prices, % y/y		0.9	0.0	-0.2	0.3	1.3
Underlying prices (CPIF), % y/y		1.0	0.9	0.5	1.0	1.4
Hourly earnings, % y/y		2.8	1.9	1.7	2.7	2.8
Current account balance (SEKbn)		204.8	229.0	221.5	246.2	264.8
- % of GDP		5.6	6.1	5.7	6.0	6.2
Trade balance, % of GDP		3.7	3.8	3.2	3.2	3.3
General government budget balance (SEKbn)		-34.1	-51.8	-80.7	-71.5	-44.8
- % of GDP		-0.9	-1.4	-2.1	-1.8	-1.1
General government gross debt, % of GDP		36.4	38.6	40.7	40.9	40.3

* Contribution to GDP growth, percentage points.

creased further in recent years. As a result, idle labour market resources should not be overestimated. The export industry still sets the benchmark for the coming round of pay talks, and the improved global economic outlook and the tighter labour market support higher wages. But we do not expect the coming pay rises to exceed those agreed during the latest round, which ended up at just over 2% points per year over a 3-year period.

The SEK – the Riksbank's most important tool

The upcoming pay talks must be completed within about a year, which makes it more important for the Riksbank to drive inflation and especially inflation expectations higher. This is the rationale behind the Riksbank's recent stimulus measures. The bank wants to make sure that inflation is back close to the 2% target in a not too distant future.

Against this backdrop, we expect the Riksbank to cut the repo rate to -0.2% during the spring. Moreover, the bank will most likely decide to continue its relatively modest SEK 10bn government bond buying programme in the coming quarter. But further stimulus measures should not be on the cards. We expect the first rate hike to be sanctioned in H2 2016.

We think that with its repo rate in negative territory and its printing press on stand-by the Riksbank seems to be aiming at weakening the SEK as a means to drive inflation higher. The SEK has indeed weakened over the past year and that has impacted inflation. We expect the weak SEK to give a further boost to consumer prices this year. However, we do not see core inflation as measured by the CPIF rising to 2%, at least not while energy prices remain relatively stable. Also, this pick-up is only temporary. We expect the SEK to strengthen and the uptrend in inflation to flatten towards the end of the forecast period.

Short term, we think the Riksbank will succeed in maintaining a weak SEK, although it will be a tough job. The ECB's major balance sheet expansion may boost market players' appetite for other currencies such as the SEK. Moreover, the Swedish economy in most respects is more robust than the Euro-area economy. This also points to SEK strengthening. But opposite forces drive the USD/SEK both short and long term. The US economy is growing and the first fed funds rate hike is getting closer, which support the USD.

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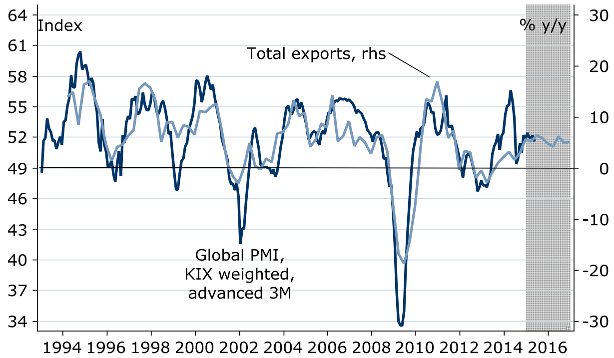
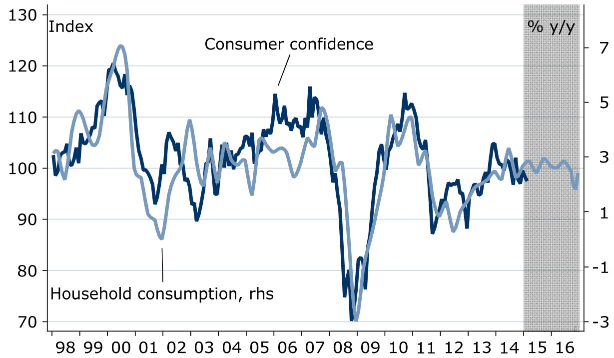
Finally brighter prospects for the export industry?



Source: Nordea Markets and Macrobond

Sustained consumer spending

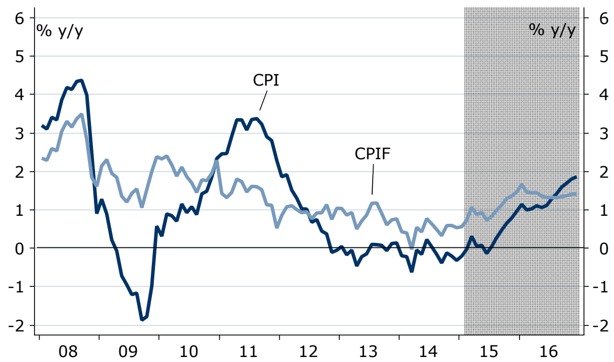


Source: Nordea Markets and Macrobond

Improved labour market

Source: Nordea Markets and Macrobond

Core inflation on the rise



Source: Nordea Markets and Macrobond

To battle low inflation as well?

- Oil-driven weakness in Norwegian economy
- Soft landing thanks to expansionary monetary and fiscal policies and gradually rising oil prices
- Low labour supply growth dampens uptrend in unemployment

Sustained low growth

In the December issue of *Economic Outlook* we revised down our growth forecast for the Norwegian economy due to the decline in oil prices. Since then oil prices have dropped even further. Although we now foresee a weaker performance by the oil-related industries and lower real wage growth than in December, we have only revised down our growth forecast marginally. Lower interest rates will at least this year to a large extent compensate for the lower real wage growth. Also, the NOK has weakened markedly, which will ease the readjustment of the Norwegian economy. Lastly, we expect oil prices to pick up over the next two years, thereby limiting the slowdown in oil-related industries.

Lower oil prices keep wage growth in check

The mainland economy will be affected by the decline in oil prices through lower demand from the oil companies. Especially oil sector investment will decline by an estimated 20% this year and by 10% next year. But equally important for both growth and inflation is the effect on wage growth. Rising oil prices and strong profitability in the oil-related industries coupled with a shortage of labour with relevant skills have been the key factors behind the past many years' high wage growth in Norway relative to other countries.

However, this is not likely to continue going forward. Already last year, wage growth started to slow markedly, ending the year slightly above 3%. This is a clear sign that the pressure on the labour market is abating. We look for wage growth of just under 3% over coming years. Oil-related industries will have to cut costs and trim activity. The scope for pay rises will decrease, and competition for qualified labour will fade. Some high-wage earners in the oil-related industries will shift to industries where wages are lower. The Norwegian Confederation of Trade Unions (LO) and The Confederation of Norwegian Enterprise (NHO) appear to agree that modest pay rises are necessary for the readjustment of the economy. Good profitability in some traditional industries as a result of the NOK depreciation pulls in the opposite direction, but probably not sufficiently to prevent modest wage growth by Norwegian standards.

No crisis in the pipeline

Despite lower activity in the oil-related industries and weak real wage growth we expect the mainland economy to grow by 1½-1¾% this year and next year. Declining interest rates will at least this year compensate for the reduced purchasing power caused by the lower real wage growth, thereby underpinning consumption growth. Another factor contributing to putting a floor under consumption growth is the boost given by the lower interest rates to the housing market and, in turn, residential construction.

Economic growth will be further underpinned by the significant depreciation of the NOK over the past years as Norwegian businesses gain market share at home and abroad. This will also lift investment activity in the mainland, as already suggested by the manufacturing industry's strong investment plans for 2015. Also strong public sector demand will support growth.
Despite all this, growth in production and employment

Norway: Macroeconomic indicators (% annual real changes unless otherwise noted)

	2011 (NOKbn)	2012	2013	2014	2015E	2016E
Private consumption	1,125	3.5	2.1	2.1	2.0	1.5
Government consumption	587	1.6	1.7	2.5	2.4	2.5
Fixed investment	596	7.6	6.8	1.2	-4.0	-0.7
- gross investment, mainland	431	7.4	2.9	1.8	2.5	2.2
- gross investment, oil	148	15.1	17.1	0.0	-20.0	-10.0
Stockbuilding*	126	-0.3	0.5	0.4	0.0	0.0
Exports	1,154	1.4	-3.0	1.7	2.0	2.1
- crude oil and natural gas	568	0.5	-7.6	0.9	0.8	0.6
- other goods	316	-0.2	1.0	2.7	3.8	4.1
Imports	796	3.1	4.3	1.6	-0.2	1.2
GDP	2,792	2.7	0.7	2.2	1.3	1.5
GDP, mainland	2,158	3.8	2.3	2.3	1.5	1.7
Unemployment rate, %		3.2	3.5	3.5	4.1	4.4
Consumer prices, % y/y		0.8	2.1	2.0	2.3	2.0
Core prices, % y/y		1.2	1.6	2.4	2.7	1.9
Annual w ages, % y/y		4.0	3.9	3.1	2.8	2.8
Current account balance (NOKbn)		368.6	307.7	266.7	176.0	276.0
- % of GDP		12.4	10.0	8.5	5.4	8.2
Trade balance, % of GDP		12.9	10.2	8.4	5.0	7.8
General government budget balance (NOKbn)		410.6	347.7	285.4	218.7	277.2
- % of GDP		13.8	11.4	9.1	6.7	8.2

* Contribution to GDP growth (% points)

will slow compared to previously. Unemployment will increase slightly, but the pick-up will be dampened by lower labour supply growth in the wake of the weakening of the labour market. Perhaps also labour supply growth will slow more than seen previously. Some oil-related industries have made extensive use of foreign labourers and they will now have to return home.

Low inflation

Core inflation currently runs at 2½%, up from 1% in early 2013. Part of the increase can be explained by the NOK weakening as it has made imported goods more expensive. But also domestic inflation has risen probably as a result of higher imported input costs.

The recent NOK weakening suggests that inflation could edge up further. But in 2016 after importers have raised their prices, imported inflation will abate. Price growth internationally is subdued and will by all accounts remain so. Also domestic inflation will likely decline sharply in 2016; with lower wage growth we expect domestic inflation to drop below 2%.

Norges Bank to cut rates; NOK to strengthen over time

Lower oil prices, clear signs of lower-than-expected wage growth and lower interest rates internationally suggest that Norges Bank will cut rates twice this year. But there is no guarantee that it will stop there. In 2016 we expect inflation to move well below both the inflation target and Norges Bank's recent forecasts. If so, Norges Bank may decide on a new round of rate cuts. However, by that time oil prices should have moved back up, interest rates internationally should be higher and the international outlook should have improved. Against this backdrop we think that Norges Bank will consider the below-target inflation rate as a temporary phenomenon and refrain from cutting rates further.

Once Norges Bank is done cutting rates and oil prices start to back up, the NOK will likely strengthen again. By how much is difficult to say due to the current scenario with money market rates at close to zero and quantitative easing measures being adopted in both Sweden and the Euro area. In this environment demand for the NOK may rise sharply, and the NOK could strengthen more than anticipated. In that case, inflation and growth will come out lower, which would once again put rate cuts on the agenda. Hence, how low Norwegian interest rates will go depends on the currency market.

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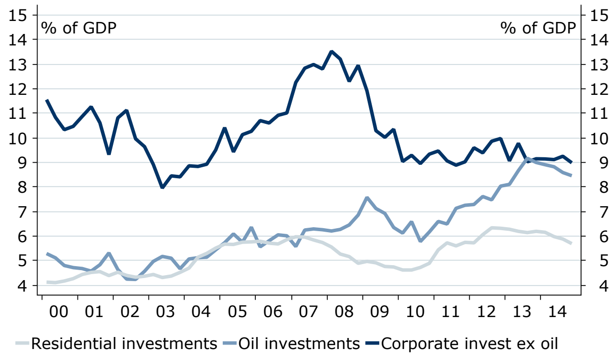
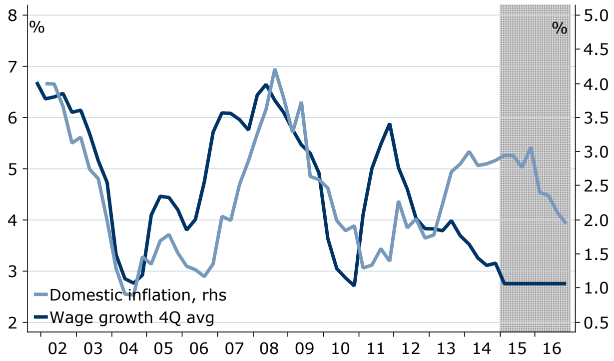
Lower oil Investment will hit the economy



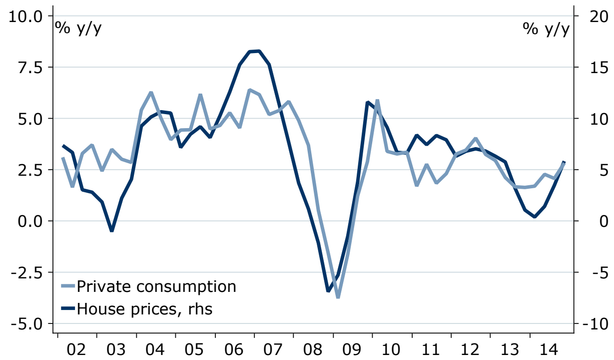
Source: Nordea Markets and Macrobond

Lower wages mean lower domestic inflation



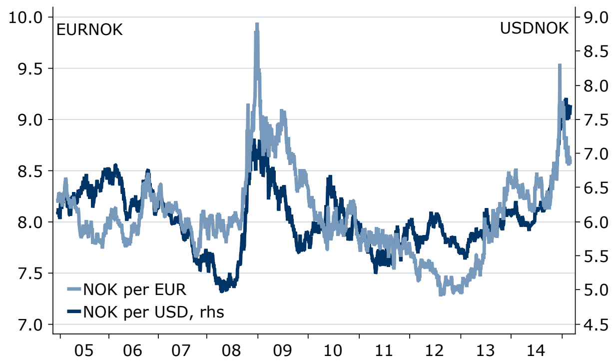
Source: Nordea Markets and Macrobond

Healthy household demand



Source: Nordea Markets and Macrobond

NOK not that weak against the euro anymore



Source: Nordea Markets and Macrobond

Times of change

- Economic growth to pick up
- Consumer spending breaks vicious circle
- Inflation briefly in negative territory
- Risk of new bubbles in two-tier housing market

These are times of change for the Danish economy. The signs of crisis appear to be fading. Growth has been in positive territory for six consecutive quarters and consumer spending is starting to rebound. We expect this positive trend to continue in coming years and now see growth at 1.5% this year, rising to 1.9% in 2016. This is marginally higher than our forecasts from December last year.

Consumer spending breaks vicious circle

Stagnant consumer spending has for several years been a major obstacle to a self-sustaining upswing in the Danish economy. But at last the tide now seems to be turning. Retail sales are rising steadily, consumer confidence has stabilised at a high level and households' purchasing power is supported by positive real wage growth, all-time low interest rates and rising employment. We expect this positive trend to accelerate in coming years. Consumer spending will therefore likely again become a key growth engine of the Danish economy.

Exports of services sharply up

Owing to the Ukraine crisis and the Russian boycott of, for instance, Danish agricultural products, Danish goods exports have been under considerable pressure since 2014. The reason why total exports still rose by almost 3% last year is a considerable increase in exports of services. In the course of 2015 we expect goods exports to start growing too, driven by a marked weakening of the effective krone rate and accelerating growth in the Euro area.

Investment activity on the rise

Business investment activity is slowly picking up. Supported by declining interest rates, easier credit standards and the improved economic outlook, business fixed investment has grown to the highest level since the autumn of 2010. Higher investment activity on Danish soil is very positive as it contributes to boosting the overall activity level and underpins the long-term growth potential. In step with the pick-up in private sector investment activity, public investment continues to grow. However, we look for a deceleration of public investment over the coming years, which once again highlights the need for further improvements of businesses' operating environment to prop up and promote private sector investment.

Negative inflation for the first time since 1954

In January a very rare phenomenon emerged in the Danish economy: inflation in negative territory. Consumer prices have not fallen on a year-over-year basis since 1954. Several factors triggered the slide into negative territory in January, but the most important one was the sharp drop in oil prices that caused transport and heating costs to decline sharply. This effect was further intensified by the abolition of the supply security tax on fossil fuels from 1 January. We expect inflation to remain around the current level over the coming months. Later in the year the effect of lower oil prices will begin to drop out of the index, which should prompt inflation to edge higher.

Growing private sector employment

Since mid-2013 employment has risen by nearly 32,000 persons. Notably, employment in private service industries has increased, while the number of public sector employees has declined. The pick-up in private sector employment is a key element of the ongoing recovery of

Denmark: Macroeconomic indicators (% annual real changes unless otherwise noted)

	2011 (DKKbn)	2012	2013	2014	2015E	2016E
Private consumption	872	0.4	0.0	0.3	1.5	1.9
Government consumption	491	-0.2	-0.5	1.4	0.8	0.5
Fixed investment	336	0.6	1.0	2.9	1.9	2.8
- government investment	40	9.8	0.3	4.5	-1.2	-3.2
- residential investment	80	-8.2	-5.0	4.5	1.3	3.8
- business investment	216	1.2	3.4	1.9	3.2	4.4
Stockbuilding*	18	-0.6	-0.2	0.3	0.0	0.0
Exports	971	0.1	0.8	2.9	3.2	3.9
Imports	869	0.9	1.5	4.0	3.3	4.0
GDP		-0.7	-0.5	1.0	1.5	1.9
Nominal GDP (DKKbn)	1,833	1,867	1,886	1,915	1,956	2,015
Unemployment rate, %		6.1	5.8	5.1	4.8	4.6
Gross unemployment level, '000 persons		162	153	134	128	122
Consumer prices, % y/y		2.4	0.8	0.6	0.3	1.2
Hourly earnings, % y/y		1.6	1.2	1.3	1.6	2.0
Nominal house prices, one-family, % y/y		-3.3	2.7	3.5	3.2	3.9
Current account balance (DKKbn)		105	136	120	113	106
- % of GDP		5.6	7.2	6.2	5.8	5.2
General government budget balance (DKKbn)		-68	-20	19	-20	-35
- % of GDP		-3.7	-1.1	1.0	-1.0	-1.7
General government gross debt, % of GDP		44.4	43.8	44.9	41.6	42.8

* Contribution to GDP growth (% points)

the Danish economy as it both boosts household purchasing power and reduces the pressure on the government budget. We expect employment to continue to increase in the years ahead driven by rising activity in the economy overall.

Fluctuating government budget balance

At first glance, the government budget balance appears to have improved markedly. According to preliminary estimates the 2014 budget surplus will amount to nearly DKK 20bn. However, the budget surplus is solely attributable to the government's one-off revenues from the optional bringing forward of capital pension tax in 2014.

This year the government budget balance will be supported by an extension of this scheme, but the expected one-off revenues will likely be considerably lower than in previous years. Short term, government revenues will also decline because of the sharp drop in oil prices. Given the combination of a relatively large deficit on the underlying government budget and the ongoing economic recovery, there is currently no room for further fiscal policy measures, we think.

Risk of local housing market bubbles

Financial market developments have been dominated by the Danish central bank's unequivocal defence of its fixed exchange rate regime. The currency reserves have swelled to a record-high level, the bank's policy rate is in negative territory and a temporary freeze has been imposed on new government bond issuance. At this juncture, it is difficult to predict when the central bank will be able to normalise its monetary policy line, especially as it is difficult to assess the effect of the ECB's QE programme on the demand for Danish kroner. However, we expect a gradual normalisation over the forecast horizon.

With growing employment and all-time low financing costs the scene is set for rising property prices. Particularly the prices of owner-occupied flats in major cities have risen. Elsewhere, the housing market recovery has not progressed at the same pace. If the current two-tier market persists for a long time, the situation could become critical as that would entail a significant risk of new local housing market bubbles that would be difficult to alleviate through government regulation.

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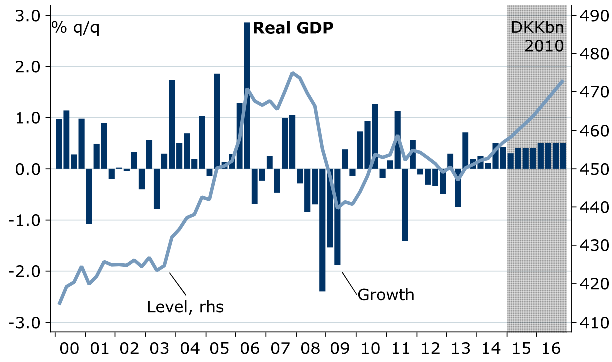
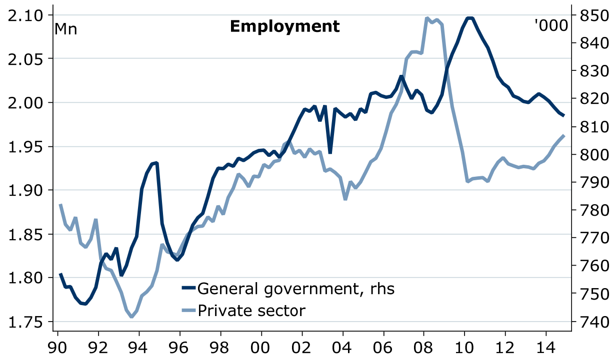
Prospects of higher growth in Danish economy



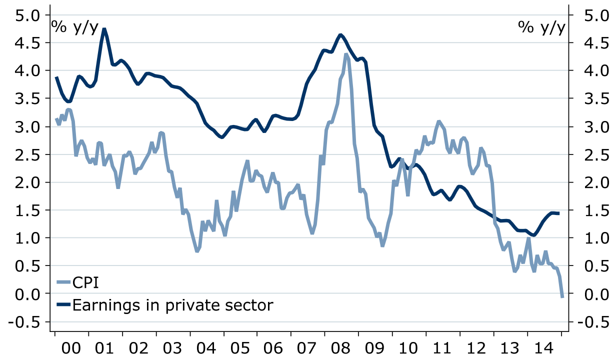
Source: Nordea Markets and Macrobond

Private sector employment rising



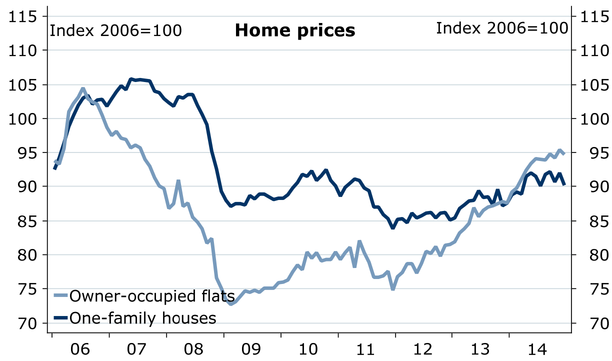
Source: Nordea Markets and Macrobond

Positive real wage trend thanks to negative inflation



Source: Nordea Markets and Macrobond

Rebound in home prices



Source: Nordea Markets and Macrobond

It's all in our own hands

- The Finnish economy has bottomed out
- Euro movements are benefitting Finland only in part
- Cheaper oil provides temporary support this year
- Private investment is at the same level as in 1999

The economy has bottomed out

We have raised our near-term growth estimates for the Finnish economy. We estimate overall production growth to be zero in 2015 and to accelerate to 1.5% in 2016 (the previous forecasts were -0.3% and 1.0%, respectively). We believe the economic downhill came to an end with the gentle drop in Q4 2014. Nevertheless, we do not expect a broad-based pick-up until 2016. This year, weak domestic demand will still weigh on economic growth as much as the foreign trade will boost it.

We have raised the forecasts primarily for two reasons: the pick-up of economic growth in the euro area in particular and cheaper oil. The fragile recovery of the euro area that has continued for eighteen months seems to finally gain strength, supported by the weaker euro, significantly cheaper crude oil and the exceptionally accommodating monetary policy, among other things. This will gradually begin to improve Finland's export demand.

Limited support to growth from euro and crude oil

In our baseline scenario, growth will initially be driven by exports. However, export growth will still be curbed by the limitations in the Russian trade, as their removal does not seem very likely at the moment. Domestic demand will not improve until 2016. This year, the labour market is weak and purchasing power is not improving at a great speed. These will continue to weigh on private consumption, which will nonetheless remain on the previous year's level thanks to the declining fuel prices. Investment will decrease for the fourth consecutive year.

The support offered by the weaker euro and cheaper oil to the Finnish economy will be limited and temporary. From Finland's point of view it is essential how the euro performs against the currencies of the most important export countries. Yes, the euro has depreciated against the US dollar, pound sterling and Chinese yuan, but against the Swedish krona and especially the Russian rouble it has appreciated. The effect of the euro movements on exports to Germany and the Netherlands is not immediate. In conclusion, the euro supports Finnish exports only in certain respects.

With the weaker euro, the euro price of crude oil has dropped clearly less than its dollar counterpart. Consequently, the Finnish consumer does not get to enjoy the drop in full either. Fuel prices consist to a significant extent of a fixed tax, which is why the cheaper oil does not translate directly to cheaper prices at petrol pumps.

Long-term growth is in Finland's own hands

In spite of these reservations, the surrounding world now offers the Finnish economy an important temporary boost. This will, however, not be enough in the long term. Finns must do the most important thing themselves, and that is to put the home turf in order. Structural reforms and a sustainable base to public sector financing would bolster long-term growth, but they are to a large extent still to be realised. What is positive, though, is that the success is purely in our own hands. Based on the numerous reports commissioned in the past few years, we know what must be done. Now it is just a question of

Finland: Macroeconomic indicators (% annual real changes unless otherwise noted)

	2011 (EURbn)	2012	2013	2014	2015E	2016E
Private consumption	106	0.3	-0.6	-0.2	0.0	0.7
Government consumption	47	0.5	0.6	0.2	0.1	-0.3
Fixed investment	44	-2.2	-5.3	-5.1	-1.5	3.4
Stockbuilding*	3	-1.1	-0.3	0.6	0.1	0.2
Exports	77	1.2	-0.7	-0.4	2.1	3.9
Imports	79	1.6	-1.6	-1.4	1.6	3.1
GDP		-1.4	-1.3	-0.1	0.0	1.5
Nominal GDP (EURbn)	197	200	202	204	206	211
Unemployment rate, %		7.7	8.4	8.7	9.0	9.0
Industrial production, % y/y		-8.5	-1.5	-1.3	1.0	3.0
Consumer prices, % y/y		2.8	1.5	1.0	0.1	1.0
Hourly earnings, % y/y		3.2	2.2	1.4	1.0	0.8
Current account balance (EURbn)		-3.8	-3.8	-3.7	-2.5	-2.3
- % of GDP		-1.9	-1.9	-1.8	-1.2	-1.1
Trade balance (EURbn)		-0.7	0.0	0.7	1.8	1.6
- % of GDP		-0.4	0.0	0.3	0.9	0.8
General government budget balance (EURbn)		-4.2	-4.9	-7.0	-6.5	-5.4
- % of GDP		-2.1	-2.4	-3.4	-3.2	-2.6
General government gross debt (EURbn)		105.7	112.7	121.1	128.8	136.0
- % of GDP		53.1	56.0	59.3	62.5	64.5

* Contribution to GDP growth (% points)

making the necessary decisions. We assume in our forecast that the government that will be formed after the parliamentary election in April will be able to complete the necessary reforms. If not, economic growth will be zero next year, as the recovery of oil prices will slow down private consumption. If the reforms are left in the air, investments would be postponed. In any case, there is a need to cut costs in the public sector.

Private investment at the same level as in 1999

The big picture of the economy has remained more or less the same since the forecast revision in December. Recent data from 2014 naturally complement the picture and serve as the basis for the current year.

The Finnish economy contracted for the third year in a row in 2014. Since 2007, economic growth has been -5% in aggregated terms. During the same period, the net national income (NNI), which measures how much we can consume if we maintain the productivity of our capital stock, has contracted, in real terms and per capita, about 13%, which equals almost 2% per year.

The reality is even harsher, as we have not taken care of the capital stock. Investment is the smallest since 2002, and private investment is even more subdued: it is the smallest since 1999.

This year, investments will decline further. There will be less investment in construction, machinery and equipment, and research and development. As long as the growth outlook remains non-existent, companies will not invest in expanding their business or create new jobs. As a result, employment will continue to weaken and the unemployment rate will rise to 9% on average in 2015 and 2016. The weak labour market points towards very moderate wage increases throughout the forecast period.

Public sector deficit larger than expected

For the last two years, the Finnish economy has consumed more than it has earned. Last year, this became considerably more pronounced. A similar period has not been seen in two decades. Private sector savings are in the green, but in the public sector, savings are clearly in the red, even before investment.

Recent statistics reveal that the official public sector deficit was considerably larger than forecasted in 2014: 3.4% of total production. This means that the Maastricht deficit criterion was exceeded for the first time since 1996. The central government deficit was EUR 8 billion. The corresponding figure for municipalities was EUR 2 billion. Without corrective measures, the debt burden of the public sector will continue to grow fast.

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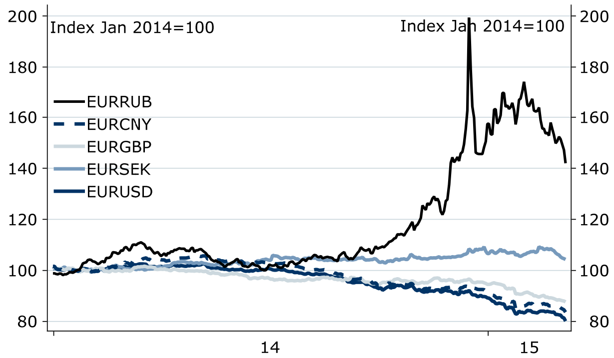
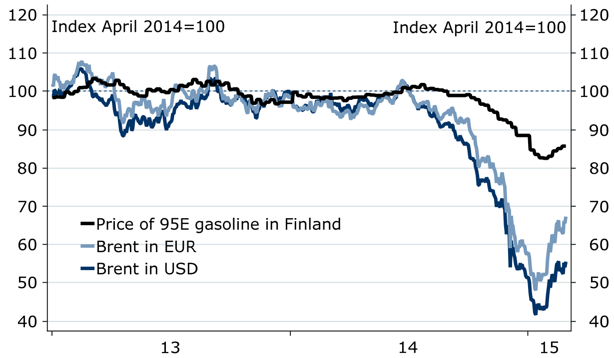
The support offered by euro is limited



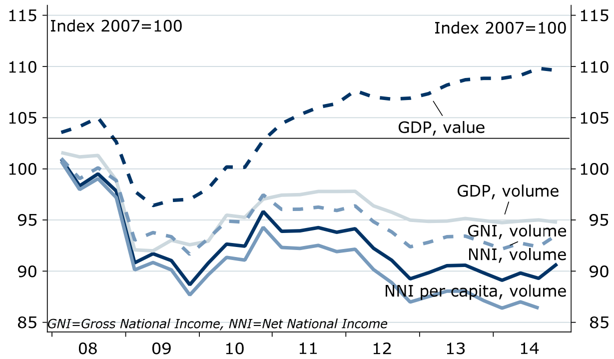
Source: Nordea Markets and Macrobond

Consumers enjoy only partial benefits of cheaper oil



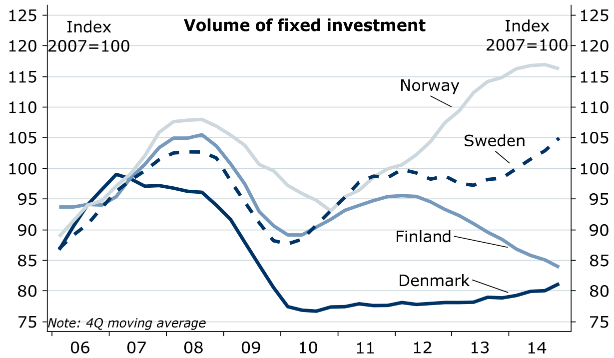
Source: Nordea Markets and Macrobond

National income has collapsed since 2007



Source: Nordea Markets and Macrobond

Investment is at the lowest level since 2002



Source: Nordea Markets and Macrobond

Temporary soft patch

Estonia continued with soft growth of 1.8% y/y in 2014, up from 1.6% in the previous year. Despite the Russia-related geopolitical risks and the weak Euro-area recovery, GDP growth accelerated in H2 to around 2.5% y/y on average. Consumption remained robust as expected, but exports surprised on the upside. The fall in exports to Russia was more than offset by exports to the EU.

Exports to Russia are expected to weaken further despite the RUB recently regaining some lost ground against the EUR. Furthermore, food and energy exports face low export prices and low demand. Overall, we expect a temporary soft patch in exports to be followed by a gradual pick-up in H2 as Euro-area demand recovers.

The ECB has launched QE to address deflationary risks and weak growth. We expect prices in Estonia to fall slightly for another year due to energy and, to a lesser extent, food prices. A subdued recovery in inflation will take hold in H2. The expected real wage growth around 5% will support consumption, which will remain the key growth engine. The drag on growth stems from state and private investment. Investment will recover in 2016 with a pick-up in exports and a rise in the share of EU co-financed state investments. The key sectors which have contributed to growth are manufacturing and retail trade. Manufacturing volume exceeded 5% y/y throughout H2 driven by exports.

Estonia will continue its economic convergence with slower growing, but higher GDP per capita Euro-area peers. The key future challenge lies in accelerating value-added growth with an ageing population and workforce. During the last ten years the total population has shrunk by 3.7%, with the number of elderly people (65 years and older) up 9%. Notably, the younger population (15-24 years) is down the most, by a quarter!

Overall, the economy is expected to remain in a soft patch as investment demand remains low and exports are slow to recover due to difficult geopolitical situation. Growth will accelerate in 2016 supported by exports and investment.

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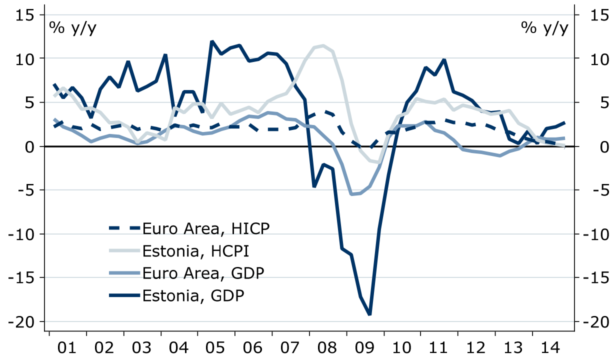
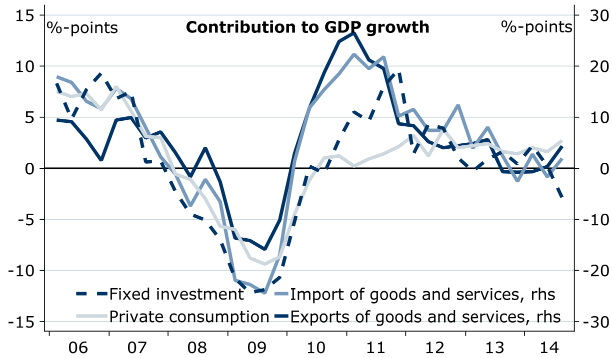
Inflation and growth



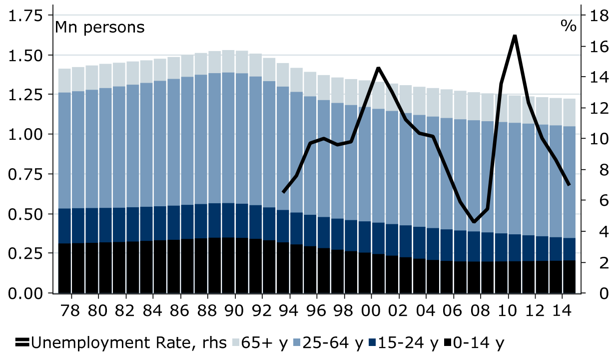
Source: Nordea Markets and Macrobond

Strong consumption, soft exports in sight



Source: Nordea Markets and Macrobond

Population and workforce ageing



Source: Nordea Markets and Macrobond

Estonia: Macroeconomic indicators (% annual real changes unless otherwise noted)

	2011 (EURbn)	2012	2013	2014	2015E	2016E
Private consumption	8.3	5.1	3.8	4.4	4.1	3.5
Government consumption	3.1	3.2	2.9	1.1	0.4	1.6
Fixed investment	4.2	10.4	2.5	-2.6	0.2	4.6
Exports	14.4	6.2	2.4	2.4	1.0	3.9
Imports	13.5	11.8	3.3	1.5	1.1	4.1
GDP		4.7	1.6	1.8	2.0	3.2
Nominal GDP (EURbn)	16.4	18	19	19	20	21
Unemployment rate, %		10.0	8.6	7.3	7.2	6.7
Consumer prices, % y/y		3.9	2.8	-0.1	-0.5	2.2
Current account balance, % of GDP		-1.8	-1.1	-0.5	-0.7	-0.8
General government budget balance, % of GDP		-0.2	-0.2	0.3	-0.4	-0.4

Creditless and consumerless recovery: how much longer?

Latvia's economic performance in 2014 was disappointing. Contrary to expectations, credit continued shrinking, consumers were reluctant to spend, the real estate market remained stagnant. On top of that the Russian economic crisis slowed down export growth. As a result, GDP growth slowed down to a mere 2.4% in 2014 versus our preliminary forecast of 5%.

But Latvia has huge untapped growth potential. Firstly, consumers may release pent-up demand, accumulated since mid-2013. Secondly, deleveraging is expected to end by 2016, especially as the credit-to-GDP ratio in Latvia is already the third lowest in the Euro area (after Lithuania and Slovakia). Thirdly, the Russian economic crisis will have only a limited negative impact on the Latvian economy (0.7% of GDP) and is likely to have some positive externalities as Latvia is apparently on the list of safe-haven countries for Russian citizens' money.

Re-commencement of activity by the largest exporter in Latvia, Liepajas Metalurgs, (4% of total exports in 2012) will give a boost to export growth, even though it is still unclear whether with the new management the company will reach pre-closure production volumes. Latvia holds the EU Council presidency for the first half of 2015, which will not only allow Latvia to set the agenda for discus-sions and potentially shape the decisions in a favourable way, but also increase tourism sector revenue. This should more than compensate for the decline in visitors from Russia, for whom travelling abroad has become much more expensive.

The Latvian economy is like a compressed spring waiting to be released by positive external factors. We expect the pent-up demand and investment potential to show through in 2016 and hence remain on the cautious side about 2015. However, the risks to our forecasts are tilted to the upside – just in case the spring pops up earlier than expected.

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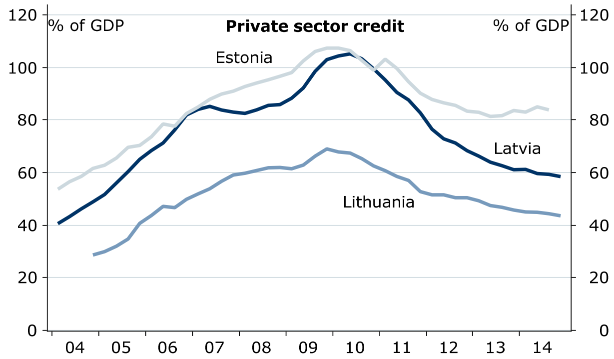
Deleveraging is coming to an end

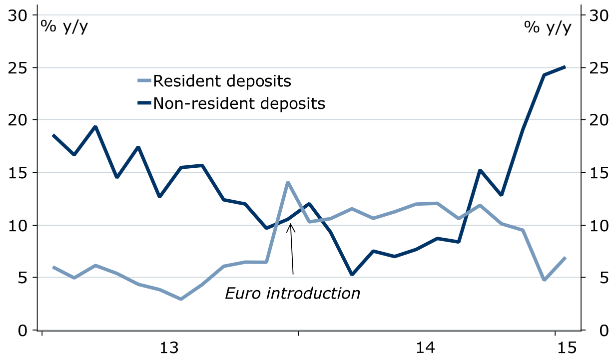


Source: Nordea Markets and Macrobond

Latvian consumers' pent-up demand

Source: Nordea Markets and Macrobond

Russian money flowing to Latvian safe haven



Source: Nordea Markets and Macrobond

Latvia: Macroeconomic indicators (% annual real changes unless otherwise noted)

	2011 (EURbn)	2012	2013	2014	2015E	2016E
Private consumption	12.6	3.0	6.2	2.3	4.0	4.5
Government consumption	3.7	0.4	2.9	3.6	1.5	2.5
Fixed investment	4.5	14.5	-5.2	1.6	2.0	6.0
Exports	11.7	9.8	1.4	1.9	2.8	4.0
Imports	12.7	5.4	-0.2	1.5	3.2	4.2
GDP		4.8	4.2	2.4	2.6	4.0
Nominal GDP (EURbn)	20.3	22.0	23.2	24.1	24.7	26.2
Unemployment rate, %		14.9	11.9	10.8	9.4	8.6
Consumer prices, % y/y		2.3	0.0	0.6	0.2	2.0
Current account balance, % of GDP		-2.5	-0.8	-2.9	-2.6	-3.0
General government budget balance, % of GDP		-1.4	-0.9	-1.0	-1.5	-1.5

Austerity is over – time to go shopping!

The Lithuanian economy surprised on the upside, with strong growth in Q4 2014 (2.4% y/y) despite economic turbulence in Russia and weak growth in the Euro area. Consumer confidence fell to a 2-year low in August 2014, but then rapidly recovered as fears of a Russian economic recession, "Euro-driven" inflation and "Grexit" subsided. Strong fundamentals (rising wages, falling unemployment rate and declining consumer prices) will continue to support domestic consumption, with both the retail trade and construction sectors forecasted to be the fastest growing sectors in 2015.

Lithuania changed over to the euro in January 2015 – one year after Latvia and four years after Estonia. The change-over marks the end of long-lasting austerity policies, with the state budget deficit for 2015 planned to remain at the 2014 level (1.2% of GDP). Having the fourth lowest public debt and deficit to GDP ratios in the Euro area, Lithuania can afford it, but the risks of "post-euro relief" still remain, especially given the rising defence spending and the potentially lower-than-expected budget revenues should the Russian economic crisis deepen.

It is estimated that exports to Russia may fall by as much as 30-50% in 2015 alone due to lower consumer purchasing power, a weakening rouble and outright trade restrictions. The overall negative effect is estimated to be 1.7% of GDP with the transport and logistics sector being hit hardest. However, since most exports to Russia are re-exports (89%), the effect on local producers will be limited (except for the dairy industry). The tourism sector may face challenges as well, since close to 50% of export revenues comes from the Belarus and Russia.

Lower oil prices, ECB stimulus, a weaker euro and active export re-orientation policies will to a large extent offset the negative spill-over effects from the Russian economic crisis; hence overall economic growth will remain positive both in 2015 and 2016.

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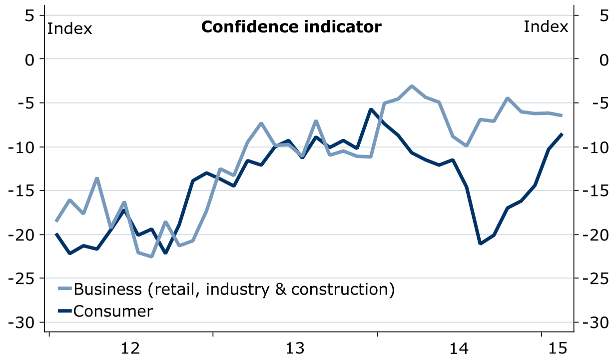
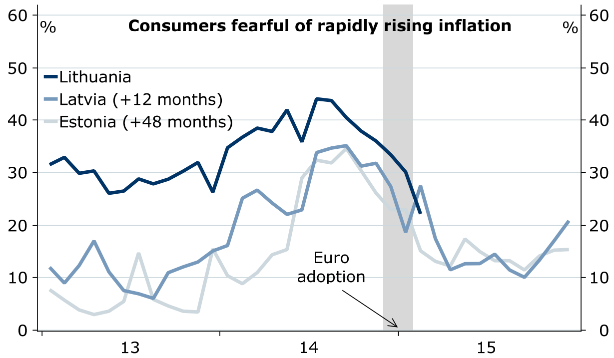
Consumers not scared anymore



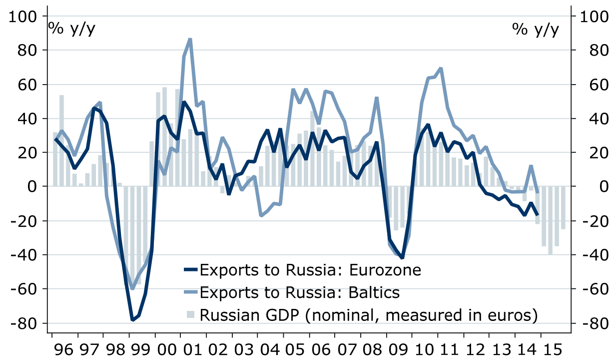
Source: Nordea Markets and Macrobond

Consumers no longer afraid of "euro-driven" inflation



Source: Nordea Markets and Macrobond

Exports to Russia may fall by as much as 40%



Source: Nordea Markets and Macrobond

Lithuania: Macroeconomic indicators (% annual real changes unless otherwise noted)

	2011 (EURbn)	2012	2013	2014	2015E	2016E
Private consumption	19.5	3.6	4.2	5.6	3.6	4.4
Government consumption	5.7	1.2	1.8	1.3	2.0	2.4
Fixed investment	5.8	-1.6	7.0	8.0	3.0	6.0
Exports	23.5	12.2	9.4	3.4	2.4	4.6
Imports	24.3	6.6	9.0	5.4	3.2	4.2
GDP		3.8	3.3	2.9	2.8	4.2
Nominal GDP (EURbn)	31.25	33.3	35.0	36.3	37.6	40.1
Unemployment rate, %		13.4	11.8	10.6	8.7	7.6
Consumer prices, % y/y		3.1	1.0	0.1	0.5	2.4
Current account balance, % of GDP		-0.2	1.5	-0.5	0.0	0.5
General government budget balance, % of GDP		-3.3	-2.2	-1.2	-1.4	-1.0

Economy and RUB will look for a new equilibrium

Following a slowdown in economic growth throughout 2014, Russia is moving into recession at the beginning of 2015. The Russian economy grew by 0.6% y/y in 2014 but in 2015 we expect GDP to shrink by 3.9%.

Contracting investment activity will be the biggest drag on the economy. Large Russian state-owned companies are demotivated by the volatile rouble, high interest rates, geopolitical uncertainty and sanctions resulting in limited access to financing in western capital markets. On the other hand state-owned companies will certainly be supported by budget money (read FX reserves) and they will become almost the only driver of investment activity in the country during 2015-16.

Inflation has also become one of the major negative factors for household consumption. Retail sales growth has been decelerating and reached 4.4% y/y in January, confirming a long-term weakening trend. Decreasing real wage growth, a negative spill-over effect from low oil prices and an increased savings rate will continue to weigh on household consumption.

However, we expect inflation to peak in Q2 2015 and start to decelerate as the effect of RUB weakness fades and due to a higher base. By the end of 2015 inflation may slide to 12-13%.

Thus we expect the central bank to have some room for gradual easing in 2015. Current level of the key rate does not reflect the expectations of lower inflation in H2 2015 and the need for monetary stimulus given the current recession. But we do not expect a quick return to pre-crisis levels on the monetary market.

The RUB is likely to continue to follow oil prices. The situation on the currency market may stay tense given the geopolitical situation and internal structural problems in the Russian economy. We neither expect a quick rebound in oil prices nor a significant improvement on the geopolitical side and thus the RUB may stay volatile at the beginning of 2015. On the positive side, oil market stabilization will support the rouble.

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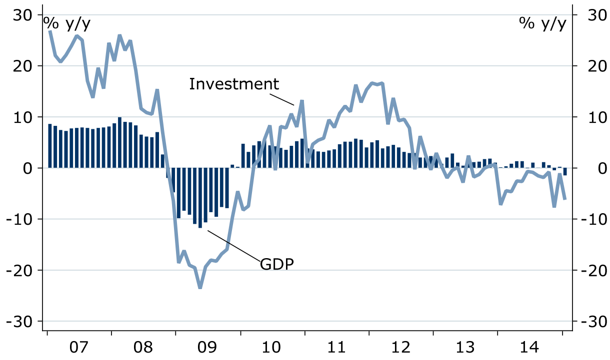
Weak investment activity – the major drag

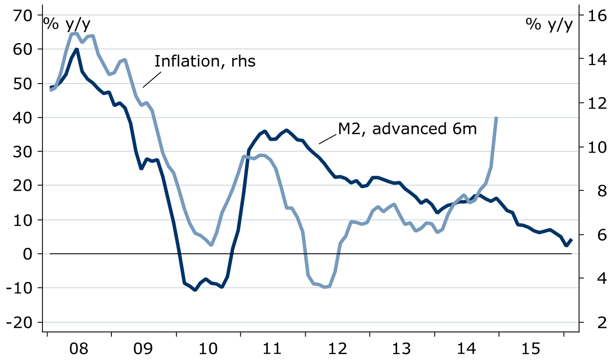


Source: Nordea Markets and Macrobond

Household consumption has been decreasing

Source: Nordea Markets and Macrobond

Inflation may peak in H2 2014



Source: Nordea Markets and Macrobond

Russia: Macroeconomic indicators (% annual real changes unless otherwise noted)

	2011 (RUBbn)	2012	2013	2014	2015E	2016E
Private consumption	27,193	7.9	4.7	2.5	-4.0	0.5
Government consumption	10,103	4.6	0.5	0.4	0.0	0.1
Fixed investment	11,950	6.4	-0.1	-2.5	-9.0	0.5
Exports	16,941	1.4	4.2	-0.6	-15.0	5.0
Imports	12,164	8.8	3.7	-8.6	20.0	2.0
GDP		3.4	1.3	0.6	-3.9	0.2
Nominal GDP (RUBbn)	55,967	62,147	66,194	70,975	73,010	77,723
Unemployment rate, %		5.7	5.5	5.2	6.9	6.3
Consumer prices, % y/y		6.5	6.5	11.4	13.0	9.0
Current account balance, % of GDP		3.6	1.6	2.5	1.9	1.2
General government budget balance, % of GDP		-0.2	-0.8	-0.5	-3.0	-2.0

Cyclical recovery in a structural slowdown

- Positive cyclical outlook for the global economy
- Good news from the Euro area
- But growth to remain modest by past norms

It might not feel that way, but the global economy entered 2015 on a slightly stronger footing as 2014 finished better than it began. Thus, we estimate that global growth picked up from 2.8% in the first half of 2014 to 3.4% in the second half, driven by the US economy and the global boost from the sharp drop in oil prices.

The moderate improvement in the global economy will likely continue in 2015 and 2016, but growth is still projected to remain modest by past norms and unemployment is set to stay much above pre-crisis levels in many economies. Global GDP growth is now projected to increase from 3.3% in 2014 to 3.4% in 2015 and 3.7% in 2016, slightly lower than our December projections.

Stimulative monetary policies have generated only sluggish growth so far in the expansion due to a combination of drags from fiscal tightening, private-sector deleveraging, increased financial regulation and general uncertainty (related to the psychological shadow of the recession, political uncertainty and geopolitical concerns). Going forward, however, these drags should gradually fade and with lagged support from low interest rates and low oil prices, the global economy should gradually gather steam. Global growth will receive a significant boost from lower oil prices. For 2015 we expect an average Brent oil price of USD 62 per barrel, down from an average USD 100 last year. This should lift global GDP growth this year by more than 0.5% point.

Diverging trends

Underneath the still fragile global economy sharply diverging trends remain, with large risks and vulnerabilities. The acceleration in global growth we are seeing in 2015 is largely driven by the mature economies, the US and the Euro area. But growth is set to remain significantly stronger in the US and the UK than in the Euro area and Japan. In Emerging Markets, China will continue to see a structural slowdown, while growth will remain weak in Russia and Brazil but continue to pick up in countries like India.

2014 was a good year for the **US** economy, and 2015 and 2016 should be even better. With fiscal tightening and household deleveraging now over, activity is gathering momentum and the labour market is fast approaching full employment. Because the US is still a net importer of oil, lower oil prices will provide a significant boost to US growth, despite some offsets from a weaker energy sector. In addition, stronger wage growth will support stronger consumer spending and given the wealth effects powered by record stock prices and higher home prices, household savings rates should, if anything, decline. As a consequence, also construction and business investment growth should pick up, while net exports will continue to act as a drag on activity, not least due to an appreciating USD. We continue to expect US GDP growth of around 3% in both 2015 and 2016.

Also in the **UK**, a self-sustaining recovery remains on track, mainly driven by private consumption. The labour market has improved significantly and continued tightening should gradually increase upward pressures on wages and give further support to the recovery. The parliamentary election on 7 May could cause political uncertainty, affecting both household and business confidence, but it will probably not jeopardise the recovery.

Maybe the best economic news over the past few months is that the **Euro-area** recovery gathered pace towards the end of 2014 and in early 2015. Thus, although growth remains unimpressive compared to the US as legacies from the financial crisis linger, Euro-area GDP growth exceeded the region's limited growth potential in Q4. Looking ahead, activity should accelerate somewhat further, supported by low interest rates, a further weakening of the EUR, low oil prices, smaller drags from fiscal tightening and corporate deleveraging and easing credit conditions. Moreover, the negative impact of the Russia/Ukraine conflict on business confidence is assumed to further abate in the Euro area.

Despite the firming of activity, very low **inflation** remains a serious concern in the Euro area. If low inflation expectations become entrenched, a rising real debt burden would intensify pressures to delever for both households and companies and could potentially trigger a deep recession. However, the ECB's decision in January to launch sovereign QE including monthly purchases of EUR 60bn from March this year through September

GDP growth forecast, % y/y

	World		G3		BRIC		US		Euro area		China		Japan		UK	
	New	Old	New	Old	New	Old	New	Old	New	Old	New	Old	New	Old	New	Old
2013	3.3	3.3	1.1	1.1	5.7	5.7	2.2	2.2	-0.4	-0.4	7.7	7.7	1.6	1.5	1.7	1.7
2014	3.3	3.3	1.5	1.5	5.4	5.4	2.4	2.3	0.9	0.8	7.4	7.4	0.0	0.3	2.6	3.0
2015	3.4	3.6	2.2	2.1	4.9	5.1	3.2	3.2	1.3	1.0	7.0	7.2	0.8	0.9	2.5	2.5
2016	3.7	3.9	2.2	2.1	5.5	5.7	2.9	2.8	1.6	1.5	6.8	7.0	1.3	1.5	2.2	2.2

Note: "Old" is the EO December 2014 forecast
Source: Nordea Markets and IMF

2016 should help contain such risks, especially through a weaker EUR.

Greece remains in deep trouble but no longer seems to pose a systemic threat to the Euro area as a whole. We attach a low probability to a Greek exit from the Euro area. But even in case of Grexit, we would expect no major impact on the growth outlook for the region as the ECB would use all measures at its disposal to defend the currency union. The risk that a Greek exit, if it happens, could undermine the broader credibility of the common currency should not be ignored, though.

Overall, Euro-area GDP growth is now projected at 1.3% in 2015 and 1.6% in 2016, up from 1.0% and 1.5%, respectively, in December.

In **China**, growth remains in a structural downtrend. Challenged by a slowdown in the growth of the labour force and excessive credit and investment growth, the Chinese authorities acknowledge the importance of achieving more sustainable growth, while at the same time avoiding an abrupt slowdown. Thus, each time headwinds from the property downturn or ongoing efforts to slow down investment have hit growth too hard, the authorities have eased up and provided monetary and fiscal stimuli. Most recently, the central bank cut rates in late February for the second time in three months and in early February reserve requirements were cut.

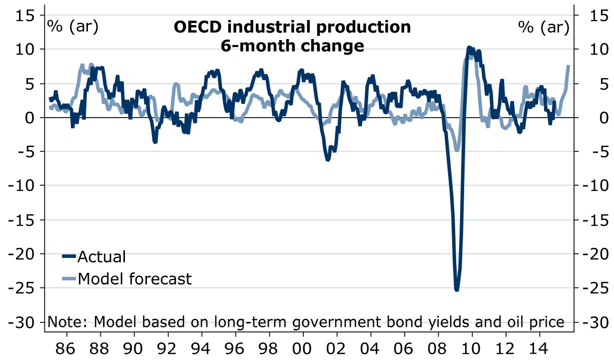
Looking forward, we expect China's growth slowdown to remain well-managed and hence project GDP growth to fall from 7.4% last year, a level not seen since 1990, to 7.0% in 2015 and 6.8% in 2016. However, due to a deteriorating property market amid high debt levels, overcapacity and weak profitability, a hard landing remains a significant risk. For more on China, see the box "China 3.0 – decades of structural slowdown".

After dipping into recession in Q3 2014, the fourth time since 2008, **Japan** is now back in positive growth territory. Going forward, the economy should benefit in the near term from the Bank of Japan's very aggressive open-ended quantitative easing, a weaker JPY, lower oil prices and the delay of the 2015 consumption tax hike. Overall, we expect GDP growth to strengthen to around trend in 2015 and above trend in 2016.

Secular stagnation

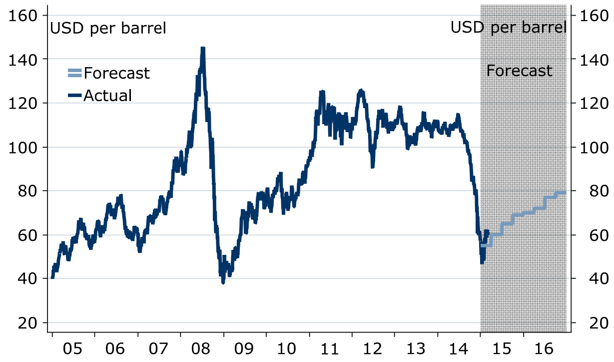
While there are reasons to be cautiously optimistic about the near-term cyclical outlook for the global economy, we believe it will be in the context of weaker structural/longer-term growth. Outside the US and the UK, much of the global economy is struggling with what might be **secular stagnation**. Thus, both in the Euro area and Japan, where trend growth rates have dropped below 1% annually, stagnation and deflation, that is, prolonged broad-based declines in prices and wages, are real concerns.

Indicators point to cyclical recovery



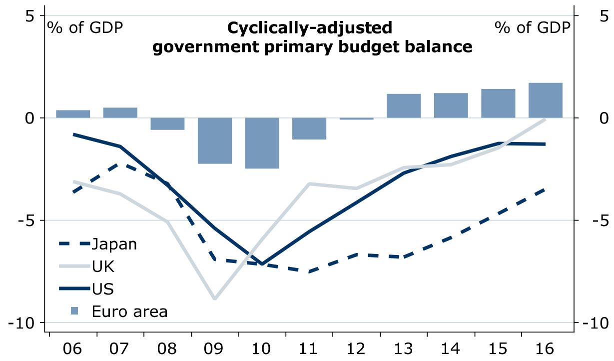
Source: Nordea Markets and Macrobond

Significant boost from lower oil prices



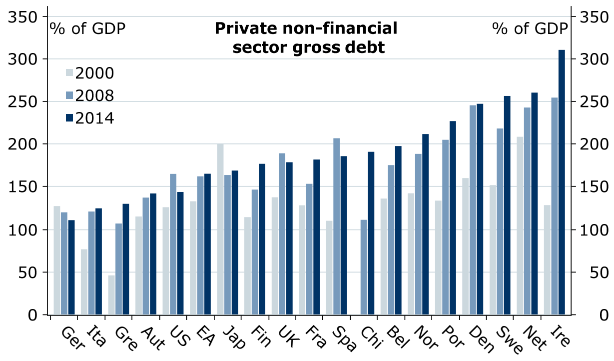
Source: Nordea Markets and Macrobond

Less drag from fiscal tightening



Source: Nordea Markets, IMF and Macrobond

Private-sector deleveraging has only just begun



Source: Nordea Markets, BIS and Macrobond

Even in the US, potential growth has fallen, to currently around 2% according to the OECD.

The slowdown in trend growth, which started in the early 1970s, reflects trend declines in both population growth and productivity growth. In Japan the population is now outright shrinking, while in Germany the same tendency was interrupted only last year by strong net immigration due to the euro crisis. As a result, averaged across the G7 countries, trend growth has been reduced from over 4% in 1970, to 3% in 1990, 2.5% in 2000 and 1.5% now.

Going forward, potential growth might revive somewhat from current levels as economies move closer to full employment. But the risk is that an ageing population might prove more of a brake on risk-taking than thought, with companies holding back investments due to diminished expectations regarding long-term growth prospects.

Another potential drag on long-term growth is that **global trade** might not be as significant a contributor to growth as it has been in the past. Since the financial crisis, global trade has slowed significantly, growing by less than 4% in both 2013 and 2014, well below the pre-crisis average growth of 7½% per year. The slowdown is partly cyclical and hence temporary, but a good deal of the weakness might be of a more permanent nature. Thus, a moderation of the decades-long trend in expanding global supply chains and the geographical fragmentation of production processes could imply that trade elasticities may not return to their highs of the late 1990s and early 2000s. Persistently weak global trade would be a major negative especially for small open economies like the Nordics.

Central banks at crossroads

The multi-speed economic performance implies divergent monetary policies across the globe. In the US, where growth and inflation expectations are not as uncomfortably low as in the Euro area and Japan, the Federal Reserve, having stopped its large-scale long-term asset purchases (QE), is likely to begin hiking interest rates around mid-year. Also the Bank of England is expected to start normalising monetary policy later this year. By contrast, the ECB has just started its own version of QE and the Bank of Japan maintains its aggressive approach to monetary stimulus.

A further general strengthening of the USD, as the result of the outperformance of the US economy and divergent monetary policies, is believed to be favourable for a rebalancing of global growth and inflation. However, the risk of a bumpy Fed exit should not be ignored. Thus, while the Fed's normalisation of monetary policy is a symptom of the strengthening US economy, it still poses a challenge for especially Emerging Markets.

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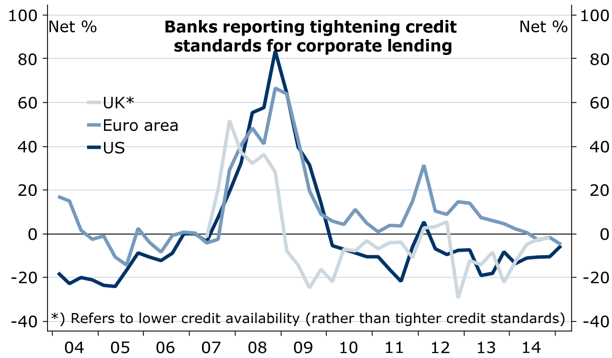
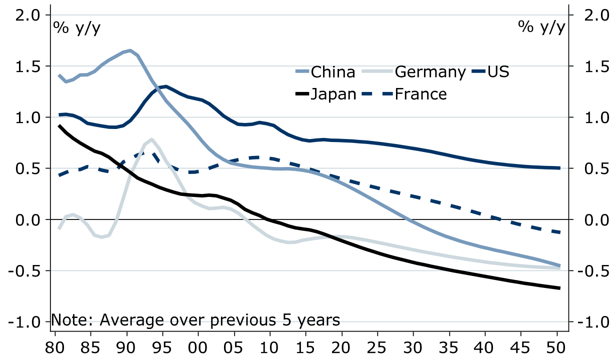
Easing of credit conditions



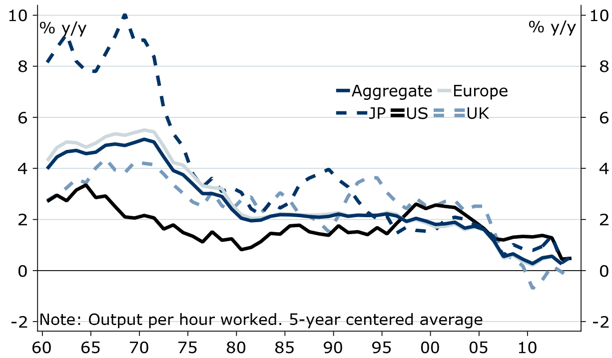
Source: Nordea Markets and Macrobond

Slowdown in population growth



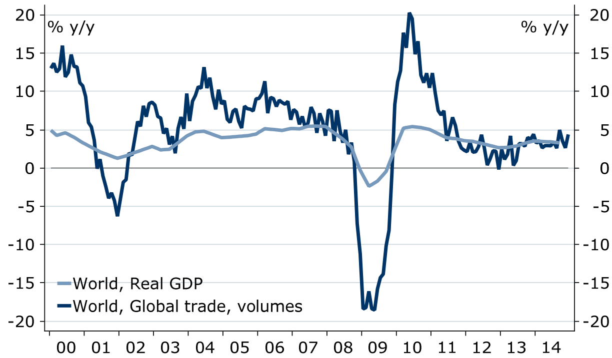
Source: Nordea Markets, US Census Bureau and Macrobond

Slowdown in productivity growth



Source: Nordea Markets and Macrobond

Global trade remains sluggish



Source: Nordea Markets and Macrobond

Risk scenarios

Our baseline scenario for the global economy is based on the assumption of continued highly accommodative monetary policies, moderating fiscal tightening, less drag from private-sector deleveraging, more supportive credit conditions and a fading impact on confidence from geopolitical tensions. However, several risks to our baseline could affect the global growth outlook in both a positive and negative direction.

All in all, at this juncture we see the risks to our baseline global growth scenario as balanced.

The table below shows a realistic upside and a realistic downside risk scenario based on a shock to the Euro-area economy, with derived consequences for the Nordic economies.

Upside risks:

- Stronger-than-expected lift to demand from the recent drop in oil prices.
- Stronger-than-expected boost to economic sentiment as geopolitical concerns fade.
- Stronger-than-expected recovery as pent-up demand is released.
- Less-than-expected tightening of Fed monetary policy.
- A much easier fiscal policy line is accepted in the Euro area, increasing aggregate demand.
- Structural reforms in France and Italy as well as in key Emerging Markets including India and Brazil.

Downside risks:

- Unexpectedly strong increase in oil prices.
- Financial market instability, potentially including capital flight from Emerging Markets, as the Fed normalises policy. Could potentially lead to increased protectionism and renewed currency war.
- More pronounced private sector deleveraging than expected, especially in Europe.
- The ECB's large-scale asset purchases fail to boost the economy, thereby increasing the risk of stagnation and deflation in the Euro area.
- Greece exits the Euro area and the credibility of the common currency is undermined. Reintroduction of the Euro-area breakup risk leads to financial market turmoil in the region and possibly beyond.
- Further escalation of geopolitical tensions (Russia-Ukraine, the Middle East, the South China Sea), with negative repercussions on confidence.
- Chinese credit bubble bursts, potentially triggered by housing market collapse.

Risk scenarios for real GDP growth, % y/y

	Strong		Baseline		Weak	
	2015	2016	2015	2016	2015	2016
Euro area	1.7	1.8	1.3	1.6	0.4	0.6
Sweden	3.0	2.8	2.7	2.4	1.7	1.5
Norway	1.7	2.2	1.3	1.5	0.9	1.1
Denmark	1.8	2.2	1.5	1.9	0.7	1.2
Finland	0.7	2.0	0.0	1.5	-0.4	0.8

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From cartel to market share

Oil prices dropped by 60% from June 2014 to mid-January. The two key explanations behind the unexpected sharp fall were a significant slowdown in oil demand growth and a complete change in OPEC's market strategy on the back of strong growth in US and Russian oil production. Defending market share and not price level is now the objective. The rebound in oil prices has been triggered by expectations that less rigs hired by the US shale industry and sharp cuts in oil companies' investments will reduce the supply overhang later in 2015 and 2016. Before we see signs that the supply/demand balance is tightening oil prices will remain volatile. In the medium term, oil prices will rebound as supply growth will be dampened and demand continues to increase.

Oil demand is expected to grow at a slower pace as a consequence of both cyclical and structural factors. Overcapacity in the energy-intensive industry in China and economic conditions of oil-importers such as Japan and the EU are expected to weigh on demand, despite the positive effects of lower oil prices on stock building and fuel consumption in the US. In the medium term, the ongoing structural changes and lower oil intensity are essential to the oil market outlook. The most important factor is the increasing competition in the transport sector, which accounts for 55% of oil demand. Mounting attention given to climate and a decade of rising oil prices have triggered the technological development of new and more efficient batteries and engines and a sharp fall in the production cost of green energy such as wind and solar power. We have only seen early evidence of the growth potential offered by natural gas, electric, hydrogen and dual-fuel vehicles, airplanes and ships. Therefore we expect that an accelerating rate of technological progress in the transport sector will curb the long-term growth momentum of oil demand markedly.

Until 27 November, the oil market was partly controlled by OPEC. With Saudi Arabia, the only country with a solid spare capacity buffer, OPEC was able to support a price at around USD 110/barrel, above the estimated marginal cost (MC) of USD 90/barrel. But the artificially high prices under the cartel regime had some undesirable side-effects: OPEC lost ground to the US and Russia. Saudi Arabia thus unexpectedly introduced a new oil order to defend market share. With a more competition-driven market, the new equilibrium price will move closer to the MC. We also expect a downscaling of OPEC's spare capacity to squeeze more expensive producers out of the market. This should lead to a rightward shift in the MC curve and drive the new equilibrium price towards USD 80/barrel depending on how faithful OPEC to its new market share strategy.

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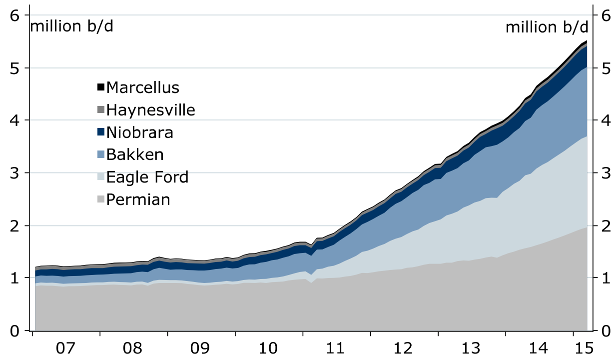
Oil price forecasts Brent – (USD/barrel)

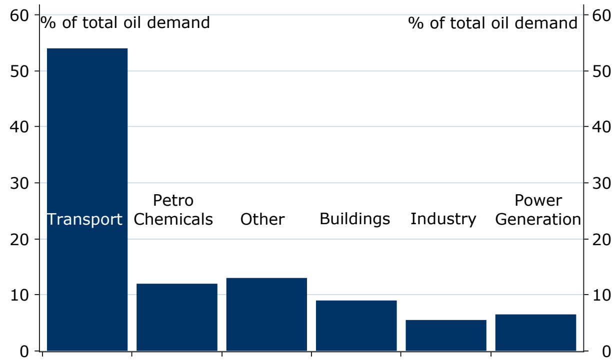
	Q1	Q2	Q3	Q4	Year
2012	118	109	109	110	112
2013	113	103	110	109	109
2014	108	110	103	77	100
2015E	55	60	65	69	62
2016E	70	72	77	79	75

No sign of a slowdown in the US shale production



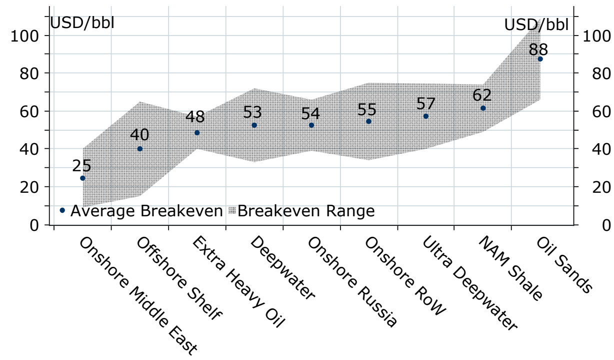
Source: Nordea Markets and Macrobond

Oil market's last stronghold transport about to fall



Source: IEA, Nordea Markets and Macrobond

Moving to a new equilibrium price level



Source:Rystad Energy, Nordea Markets and Macrobond

Blue-eyed monetary policy

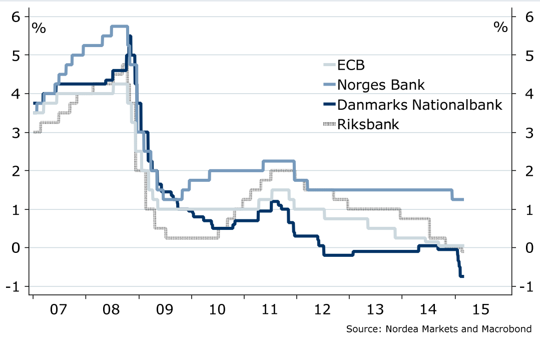
The pressure on the three monetary policy regimes in the Nordic countries intensified at the beginning of 2015.[1] *In Denmark, and possibly also in Sweden, the pressure is expected to ease during the forecast horizon. In Norway, however, challenges are waiting ahead.*

After the Swiss central bank in January left the peg with the euro and let its policy rate drop into negative territory, speculations mounted that Danmarks Nationalbank, the Danish central bank, would go the same way. Suddenly Denmark was perceived as a high-yield alternative for investors. Danmarks Nationalbank responded immediately with subsequent rate cuts and massive intervention in the FX market, which reduced the pressures on the currency.

Also in Sweden there's an ongoing struggle to reach the monetary policy target. Despite a strong economic performance, the Riksbank, the Swedish central bank, cut its policy rate to -0.10% in February 2015.

Besides negative policy rates, other unconventional measures have also been taken in both Denmark and Sweden. In March, the Riksbank started to buy government bonds, although the amount so far is negligible and the move should rather be seen as a symbolic act. Denmark chose to intervene by temporarily suspending issuance of government bonds, thus reducing supply.

Policy rates in the Nordics

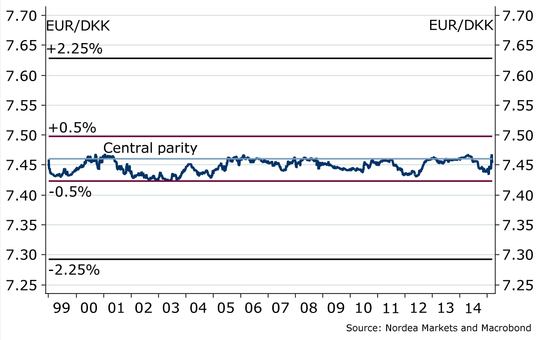


Denmark will manage ...

It is relatively easy to defend a currency that is under appreciation pressure, and Danmarks Nationalbank both has the capability and the willingness to maintain the fixed exchange rate regime. Denmark has a long tradition of maintaining a fixed rate policy towards its main trading partners, and since 1983 the fixed exchange rate policy has been a cornerstone of the economic policy pursued. By referendum Denmark has decided not to join the euro, but it participates as the currently only member in ERM2, with a central parity rate of 7.46038 against the euro.[2]

Economic history suggests that it is more difficult to defend a currency under depreciation pressure. It is also this situation which Danmarks Nationalbank has prepared for and clearly wants to avoid. A closer look at the trading range for the currency shows a clear asymmetry where the tolerance for a weaker krone is lower.

Trading range for the Danish krone



... while the Riksbank will struggle

The Riksbank's task seems more difficult to solve. Also in Sweden, the currency plays an integral role in monetary policy. By running an expansionary monetary policy the Riksbank tries to weaken the krona, or at least avoid appreciation, which should lead to higher import prices and with a lag also higher consumer prices. Deputy Governor Per Jansson recently exemplified this concern very well in an interview by stating that *"should we get a steep strengthening of the krona, well then it's more or less game over"*. The problem with this strategy is that once the currency depreciation ends, consumer inflation will fade. Thus, the currency effects should to a large extent be transitory.

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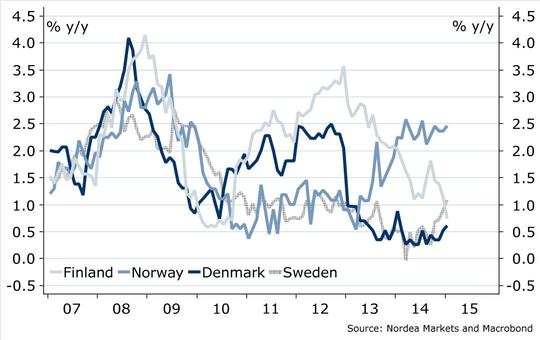
[1] Sweden and Norway have inflation target regimes. While the Riksbank specified its inflation target at 2%, Norges Bank is aiming for 2.5%. Denmark has chosen a fixed exchange rate regime vis-à-vis the euro. Finland has joined the Euro area and thereby lacks a national monetary policy.

[2] The normal fluctuation band in ERM2 is +/- 15%, but Denmark has chosen a narrow band of +/- 2.25%. The ERM2 agreement includes a provision on unlimited intervention credit between the ECB and Danmarks Nationalbank. Since the late 1990s, the Danish central bank has kept the krone stable at a level close to the central parity rate.

Our forecast is that core inflation will undershoot the target during the whole forecast period.

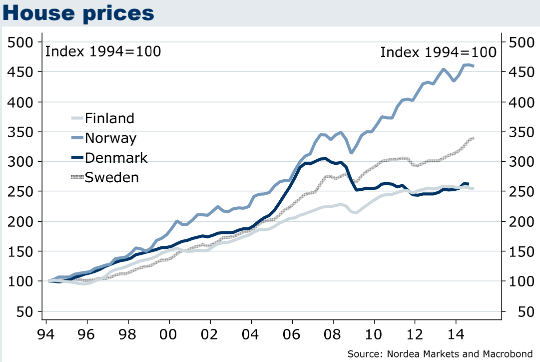
Inflation excluding energy



Norges bank – can't rule out unconventionals

Norges Bank, the Norwegian central bank, is one of very few central banks in the world that over the past year has seen inflation close to the target. In January, core inflation stood at 2.5%, which is spot on target. That is to a large degree a result of a weaker Norwegian krone. However, the effect of the weaker currency will fade, and the krone has strengthened somewhat again. The drop in oil investments will weigh on economic growth in 2015 and 2016. Wage growth has already declined, which suggests also significantly lower domestic cost pressure going forward. Our forecast of annual wage growth at just below 3% and imported inflation again returning to about zero, point in the direction of core inflation declining to 1¼-1½% in late 2016. The subdued inflation outlook, coupled with continued low inflation and rates abroad, will put pressure on Norges Bank in coming years. Our baseline scenario is that Norges Bank will settle with two more rate cuts this spring, but further steps cannot be ruled out. The challenge is particularly large as the Norwegian inflation target stands at 2.5%, which is above those of other countries at around 2%.

House prices



Monetary policy – it's complicated

The risks with the current expansionary monetary policy are well-known. Low interest rates, and signals that they will be low for long, will most likely continue to push up asset prices. On the housing markets, the stakes seem highest in Norway and Sweden where prices have risen sharply in recent years. The loose monetary policy also drives bond and stock prices further up. Unsurprisingly, the Nordic stock market indices have performed better than their global counterparts so far in 2015.

Somewhat paradoxically, there is actually a risk that the fight against too low consumer price inflation increases the likelihood of a deflationary economic situation, characterised as broad-based price declines and postponements of investments and consumption. In Norway, it would also be a paradox if Norges Bank by monetary measures should try to push annual wage increases well above those of its trading partners again at a time when a stabilisation and gradual decline in its petroleum sector requires more focus on cost competitiveness.

Monetary policy is complicated and a comparison of the inflation developments in the Nordics may serve as an illustration of the difficulties facing inflation target regimes. Over the past ten years inflation averaged 1.2% in Sweden.[3] The corresponding figure in Norway, Denmark and Finland is 1.9%. Isn't it ironic that the countries without explicit inflation targets managed to hover as close, or even closer, to 2% than those with such targets? Nor does inflation seem to be more stable in Norway or in Sweden. In fact, Danish inflation shows the lowest volatility, measured as standard deviations over the past ten years.

Another ironic fact is that Denmark and Finland, the countries with the weakest economic performance in recent years, actually lack means to conduct a monetary policy to stabilise the economy. At this juncture, however, it is probably not the absence of loose monetary policy that has prevented these economies from growing. After all, the similarly weak performance in the Euro area has been met by an expansionary monetary policy

[3] The inflation measure used here is overall CPI for all countries. The pattern is the same if we instead compared core inflation (HICP excl energy). Swedish inflation has also in this case averaged 1.2%, which is significantly lower than in all other Nordic countries.

in the whole region, Finland included. Real difficulties would only arise in case of an asymmetric shock that hits Denmark or Finland but not the Euro area at large.[4]

Summing up

Economic developments during the past years have differed across the Nordic countries. While developments in domestic demand in Norway and Sweden have been favourable, Denmark and Finland continue to struggle. In terms of policy, however, all countries face challenges. Due to different monetary policy regimes, as well as the diverse economic developments, the challenges also differ across the countries. While monetary policy in Denmark and Sweden has already tested new ground, the Norwegian central bank has so far stayed conventional. Given the subdued inflation outlook, however, one cannot rule out unconventional measures also in Norway by the end of the forecast horizon or in 2017. In Finland the challenges are not monetary but for real.

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[4] But then stabilisation policy never seems to have had any prominent role in Finnish policy-making. I previously worked at the Swedish Ministry of Finance and recall a visit at the Finnish finance ministry back in 2002. At the time a referendum on EMU-membership drew near in Sweden and the purpose of the visit was to learn more about our neighbour's experiences. The official from the Finnish ministry simply stated that "*You Swedes are so obsessed with stabilisation policy. In Finland we focus on structural issues*".

China 3.0 – decades of structural slowdown

In the past three decades China has gone through an incredible transformation from a small closed economy to the world's largest exporter and commodity consumer. The economy has witnessed incomparably high growth. Between 1991 and 2011, it grew by 10.4% on average per year and was labelled a growth miracle. But this is no longer the case. In the last three years Chinese demand has slowed and repeatedly been considered as a major risk to the global economy. The deceleration reflects structural changes as well as a different attitude regarding the growth model. China has entered phase three of its development and will face decades of structural slowdown.

Manufacturing: from driver to drag

China has been a true industrialised nation with the manufacturing sector as the main growth engine. Industrial activities were driven mainly by two factors: exports and construction. With abundant low-cost labour and the entry into the WTO in 2001, China has built its affluence by supplying the world with discount made-in-China products. Exports made up 40% of GDP at their peak in 2006. In comparison, Japan's exports have never accounted for more than 20% of GDP. The export-oriented growth model has boosted labour-intensive manufacturing on the east coast.

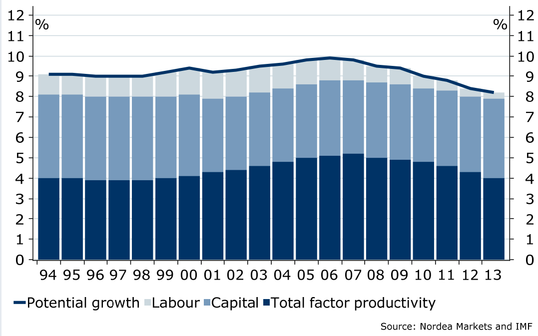
The construction boom, sparked by China's property market privatisation in the 1990s and supported by the ambitious ongoing urbanisation plan, led to a rapid expansion of the heavy industry in northern China, particularly mining. It was also a key factor behind China's endless thirst for natural resources. Real estate investment accounts for 15% of GDP. The share nearly doubles when other real estate-related sectors are taken into account. If the export-oriented light industry is labour-intensive, then heavy industry is capital-intensive. The mining boom has drawn a rush of investment into the sector funded by cheap state bank credit. Investment in manufacturing has accounted for 40% of total investment, twice as much as investment in infrastructure.

Given manufacturing's importance for China, it is not surprising that when the sector starts to struggle, it dampens the growth of the whole economy. Annual growth in industrial production declined from 13.1% between 1991 and 2011 to below 8% in 2014. The PMI index, among the most watched Chinese data, has been hovering around 50. The downturn in manufacturing has triggered disappointing growth in exports, investment and credit.

Potential growth has peaked

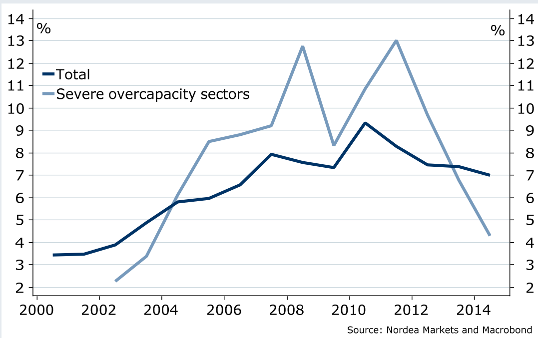
As explained above, abundant labour supply and rapid expansion of the capital stock have been the key ingredients in China's growth miracle. These advantages started to fade in recent years. According to the IMF, potential growth dropped from around 10% in the boom years to 8% today. The OECD expects potential growth of 2% in 30 years. The working-age population began to shrink in 2012. The decline will accelerate due to the one-child policy and go on for decades. Labour supply is set to be a drag on future growth.

Estimated contr. to China's potential growth



Labour shortage is not the only problem. Since 2011 China has witnessed diminishing returns on investment, particularly for the mining sector that suffers from severe excess capacity. Chinese officials recorded capacity utilisation in the mining sector of only 50% in 2014. Between 2008 and 2013, China's investment ratio rose by 6.5% points and its corporate debt ratio by 68% points. To avoid a debt crisis, Beijing has put a stop to the credit-fuelled investment mania that has driven the economy since 2008. Thus, the capital stock is expected to make a lower contribution to growth going forward. Finally, it is reasonable to assume continued falling productivity growth given the technology catch-up that has already taken place. To sum up, we can expect lower potential growth in China in the coming decades.

Return on assets of Chinese industrial firms



Willing to adopt a new growth policy

To understand China's structural slowdown, it is just as important to identify the structural factors as it is to recognise the authorities' attitude towards growth. As shown above, the IMF's estimates of potential growth began to decline already in 2006, but actual growth saw no remarkable drop until 2012. The explanation is obvious. The previous administration was not ready for a slowdown and chose to overstimulate the economy by pouring cheap credit into the state-owned enterprises (SOEs) that invested in heavy industrial sectors. Growth was kept artificially high as desired, but a number of unexpected problems have emerged subsequently.

Overcapacity in heavy industry and the resulting credit risk have already been mentioned above. Overreliance on manufacturing has left many provinces with serious air and water pollution. According to the World Bank's China 2030 report, environmental deprivation and resource depletion in China have costs of about 10% of GDP. Another study has shown that smog is likely to reduce the average life expectancy in northern China by 5.5 years. Income inequality is another unwanted outcome of industrial dominance. Households have for years been indirectly financing public investments in manufacturing through artificially low deposit rates. This has created unequal wealth distribution and tension between the households and the SOEs. The social stability-obsessed government cannot afford to ignore these tangible and intangible costs that cause dissatisfaction in the population. Thus, it will have to tolerate lower growth and continue pushing for transformation from industry to services and from investment to consumption.

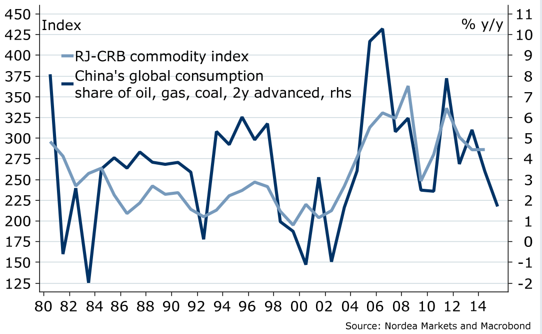
Implications for the world

As the world's second-largest economy and contributor to a third of global growth, China's structural slowdown will inevitably have universal implications. Global trade and commodity markets are expected to feel the largest impacts.

China is one of the largest export markets for most countries. This will slowly change in the future and is already reflected by falling import growth. Many observers have attributed this to murky domestic conditions in China, but it is in fact due to a structural downturn in exports. China has a large share of imported parts in its exports. Although the share has fallen from its peak of 60% in the 1990s to 35% today, it is still high by international comparison. The short-term reaction to lower export growth is to reduce import growth. In the longer term, China will likely import more consumer goods for domestic use. Consumption's share of the economy is expected to rise on continued urbanisation, more people joining the middle class and improved social security that reduces the need for precautionary saving. We see the falling export growth as structural because rising labour costs will cause more production to be shifted out of China and to lower-cost emerging countries. In some cases, it is economical to produce in developed markets.

China is the world's largest consumer of most commodities and uses about 50% of the world's coal and base metals and 12% of oil. A structural slowdown especially in energy-intensive industries such as steel and a move towards more consumption-driven growth in China have contributed to the drop in commodity prices in recent years. Because of this fundamental change of growth model, China's future commodity demand will slow down compared to the boom years. This will likely put downward pressure on prices. It is important to highlight that we do not expect a crash in commodity demand. Infrastructure is far from well-developed on a macro level. The average age of a building is around 25 years, a fact that is likely to support relatively steady construction growth.

China's importance for commodities



Source: Nordea Markets and Macrobond

The Chinese economy has doubled in size in the last five years so it is harder to grow by 7% today than 10% then. A slowdown is inevitable. China has entered phase three of its development. If it lasts 30 years like the previous two phases, then China faces decades of structural slowdown. On the surface, it is bad news for the world economy through trade and commodity channels. However, if the lower growth is accompanied by balanced and sustainable growth in the longer term, with much a smaller risk of a hard landing, then it should be desirable for everyone.

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Germany – structural challenges and growing Euro blues

The German economy is doing fine right now. Under the surface, however, there are several structural risks and challenges to longer-term growth. Politically, the battles about QE and with Greece indicate a growing unease in Germany about how things in Europe are developing.

According to Deutsche Bundesbank's estimate, potential output recently grew by 1.1%. The forecasts are 1.1% for 2014 to 2016 and 1.0% for 2017 to 2019. Growth is determined by the quantity of capital and labour and by how productively these factors are combined. The challenge for the future is to prevent the labour component from becoming too negative despite the adverse demographic trend, and to improve conditions for investment and productivity growth. There are many ways to do so. Here we concentrate on labour market issues, the still significant dependence on goods exports at the expense of services and on public investment.

Labour market and education

In Germany population ageing is setting in earlier than in most other OECD countries. The baby boomer generation will start retiring massively around 2020. Compensating factors could be increasing labour market participation, longer working hours and strong immigration. The grand coalition's decision to make early retirement at the age of 63 more attractive for certain groups of employees counteracts former efforts to increase labour force participation.

Germany now has one of the highest participation rates among OECD countries (77.5%), but there are also few countries where employees work fewer hours. The share of women working part-time is high, not least because the marginal tax and levy burden on second earners is high. Moreover, combining work and family responsibilities is still more difficult than in the Nordics or in France.

Net immigration of around 400k to 500k per year could be necessary to compensate for the adverse demographic trend. Germany had that in recent years, mostly from Eastern Europe. However, the pool of East Europeans moving abroad is not unlimited, and many moved to countries like the UK that had not imposed restrictions to the free movement of labour after the EU enlargement in 2004. Immigrants from Southern Europe may move back to their home countries once conditions there have improved. Therefore Germany has to become better at attracting highly skilled immigrants also from outside the EU.

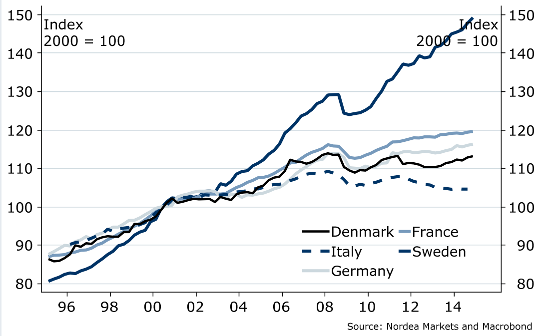
Concerning the quality of labour, there is ample room for improvement, too. More than in other countries, educational success depends on the socio-economic background of the parents. The German dual education system combining apprenticeship in a company with vocational training worked well in the past and contributed to low youth unemployment. The system may need adaptation, however, not least to improve IT knowledge. Germany also has a relatively low proportion of people attaining tertiary education.

Services count into GDP, too

Germany is mostly known for cars and machines finding buyers all over the world. In 2013, industry (including construction) accounted for 30.2% of gross value added – the highest share among all the non-eastern European EU members. The share of services was 69% compared to an EU average of 73.6% (Denmark: 77.2%; Sweden: 74.3%; Finland: 71.6%).

Many professional services, for example lawyers, architects and engineers, are highly regulated. Deregulation leading to lower entry barriers would create more competition and jobs. It would also make the economy less vulnerable to external shocks. Currently this is not on the government's agenda, but that might change if the trend in global goods trade growth remains as sluggish as it has been since 2012.

Services: Gross value added



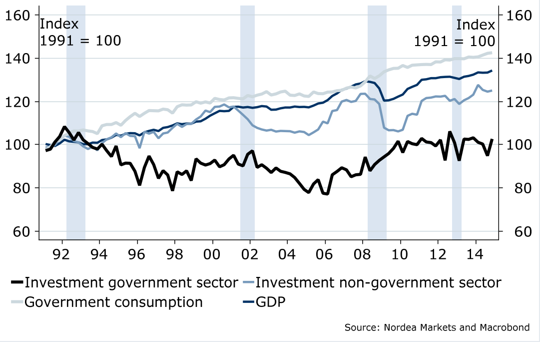
Some rebalancing of the economy is taking place, however. From a demand perspective, private consumption now is the main growth driver. Seen from a sector level, capital investment in the service sector grows faster than in industry. The logistics sector, for example, is growing fast, and the increase in house prices and construction activity can easily stimulate job growth in real estate-related services.

Neglect of public investment

For quite a while already, a lively debate about the declining quality of public infrastructure has been going on in Germany. Parents can tell frightening stories about the poor state of their children's schools and weekends spent painting walls, but it's much more than anecdotes. The network of roads and railways is aching under the increase of freight and passenger traffic. After all, Germany is a transit country bordering directly with nine other countries. Public infrastructure is an intermediate good for all companies. It is one important factor for companies deciding where to do business.

In recent years, public consumption has been favoured over public investment. Municipalities are responsible for about half of all public investment, such as building local streets and hospitals and maintaining schools. Many municipalities simply lacked the revenue to fund investment spending (which also indicates a need to reform the complicated system of financial relationships between the federal, the state and the local level, but that's a separate issue).

Government investment stagnating



Gross government investment today is not higher than it was in 1992 (see chart). Net public investment has even been negative since 2003: investment is too low to compensate for the depreciation of the capital stock. The public investment to GDP ratio is one of the lowest in the EU.

Several studies suggest a public investment gap of roughly EUR 80bn or almost 3% of GDP. German politicians are adamant about not putting too high a burden of public debt on future generations. Somewhat paradoxically, they are much less reluctant to pass on a capital stock in poor shape.

These are just a few of the areas where Germany has to reform. Berlin often calls for more growth-enhancing reforms in other European countries. This would sound more credible and less schoolmasterly homework was also done in Germany.

Politics: growing unease about Europe

As in other European countries, also Germans' trust in the European project has declined. At the same time, according to surveys Germans' distrust in the ECB has risen to an all-time high. QE is widely considered as a desperate attempt to buy over-indebted countries even more time for growth-enhancing reforms – time that probably will be wasted again.

The Bundesbank lost the QE battle against the ECB. This may partly explain the uncompromising attitude of the German Finance Ministry towards Greece during the recent negotiations about the bailout extension. It seems that Germany acted as the "spokes-country" of a coalition including Finland, Austria, the Netherlands, Slovakia, the Baltic countries, Spain and Portugal. New times maybe as Germany's traditional partner in European politics used to be France.

At home, the German government received large public support for its tough stance. This battle the government did not want to lose, not least to prevent the Euro-sceptic party Alternative für Deutschland (AfD) from rising further. The AfD won 6.1% in a recent regional election in Hamburg. It is far away from taking over political responsibility anywhere in the country. We consider the electoral potential for the AfD to be significantly higher. For now, however, it cannot be realised because of huge internal divisions and an unclear overall political message.

The overwhelming majority of the political class in Germany is still very much pro-Euro and wants no country to leave the Euro area – provided that the countries stick to the rules. Upcoming negotiations with Greece about a new bailout programme and possible debt relief will again put German politicians' patience and willingness to compromise to the test. As we see it, Germany has moved away from its traditional position that aimed at preserving the integrity of the Euro area *at any price*. It that sense, Germany has become a less compromising and therefore more difficult partner to deal with.

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Growth, %

	2012	2013	2014E	2015E	2016E
World[1)]	3.4	3.3	3.3	3.4	3.7
USA	2.3	2.2	2.4	3.2	2.9
Euro area	-0.7	-0.4	0.9	1.3	1.6
China	7.7	7.7	7.4	7.0	6.8
Japan	1.7	1.6	0.0	0.8	1.3
Denmark	-0.7	-0.5	1.0	1.5	1.9
Norway	3.8	2.3	2.3	1.5	1.7
Sweden	-0.3	1.3	2.1	2.9	2.6
UK	0.7	1.7	2.6	2.5	2.2
Germany	0.6	0.2	1.6	1.7	1.6
France	0.4	0.4	0.4	0.9	1.2
Italy	-2.3	-1.9	-0.4	0.5	1.1
Spain	-2.1	-1.2	1.4	2.2	2.3
Finland	-1.4	-1.3	-0.1	0.0	1.5
Estonia	4.7	1.6	1.8	2.0	3.2
Latvia	4.8	4.2	2.4	2.6	4.0
Lithuania	3.8	3.3	2.9	2.8	4.2
Poland	2.1	1.6	3.3	3.0	3.2
Russia	3.4	1.3	0.6	-3.9	0.2
India	4.8	4.7	5.3	5.9	6.3
Brazil	1.0	2.5	0.0	-0.5	0.7
Rest of World	4.0	3.5	3.2	3.5	4.0

Inflation, %

	2012	2013	2014E	2015E	2016E
World[1)]	4.4	4.0	4.0	3.5	4.0
USA	2.1	1.5	1.6	0.3	2.6
Euro area	2.5	1.4	0.4	0.2	1.2
China	2.7	2.6	2.0	1.4	3.0
Japan	0.0	0.4	2.7	0.6	0.6
Denmark	2.4	0.8	0.6	0.3	1.2
Norway	0.7	2.1	2.0	2.3	2.0
Sweden	0.9	0.0	-0.2	0.3	1.3
UK	2.8	2.6	1.5	0.5	1.5
Germany	2.1	1.6	0.8	0.4	1.7
France	2.2	1.0	0.6	0.0	1.0
Italy	3.3	1.3	0.2	0.1	1.1
Spain	2.4	1.5	-0.2	-0.7	1.3
Finland	2.8	1.5	1.0	0.1	1.1
Estonia	3.9	2.8	-0.1	-0.5	2.2
Latvia	2.3	0.0	0.6	0.2	2.0
Lithuania	3.1	1.0	0.1	0.5	2.4
Poland	3.7	1.2	0.2	0.3	2.2
Russia	6.5	6.5	11.4	13.0	9.0
India	9.7	10.1	7.3	6.1	6.0
Brazil	5.4	6.2	6.4	7.1	5.6
Rest of World	6.6	6.2	6.4	6.5	6.0

1) Weighted average of 186 countries. Weights for all countries and data for Rest of World are from the most recent World Economic Outlook, by the IMF. The weights are calculated from PPP-adjusted GDP-levels

Public finances, % of GDP

	2012	2013	2014E	2015E	2016E
USA	-6.8	-4.1	-3.4	-2.6	-2.8
Euro area	-3.6	-2.9	-2.6	-2.2	-1.9
China	0.2	-0.9	-1.0	-2.0	-2.5
Japan	-9.8	-10.1	-9.5	-9.0	-9.0
Denmark	-3.7	-1.1	1.0	-1.0	-1.7
Norway	13.8	11.3	9.1	6.7	8.2
Sweden	-0.9	-1.4	-2.1	-1.8	-1.1
UK	-6.1	-5.8	-5.4	-4.4	-3.5
Germany	0.1	0.1	0.6	0.2	0.2
France	-4.9	-4.1	-4.3	-4.1	3.8
Italy	-3.0	-2.8	-3.0	-2.6	-2.0
Spain	-10.3	-6.8	-5.6	-4.5	-3.7
Finland	-2.1	-2.4	-3.4	-3.2	-2.6
Estonia	-0.2	-0.2	0.3	-0.4	-0.4
Latvia	-1.4	-0.9	-1.0	-1.5	-1.5
Lithuania	-3.3	-2.2	-1.2	-1.4	-1.0
Poland	-3.9	-4.3	-3.2	-3.0	-2.5
Russia	-0.2	-0.8	-0.5	-3.0	-2.0
India	-7.4	-7.2	-7.0	-6.5	-6.0
Brazil	-2.8	-3.3	-4.0	-3.5	-3.1

Current account, % of GDP

	2012	2013	2014E	2015E	2016E
USA	-2.9	-2.4	-2.2	-1.9	-2.2
Euro area	1.8	2.6	2.9	2.9	2.7
China	2.6	1.9	1.8	2.0	1.5
Japan	1.0	0.7	1.0	1.2	1.5
Denmark	5.6	7.2	6.2	5.8	5.2
Norway	12.4	10.0	8.5	5.4	8.2
Sweden	5.6	6.1	5.7	6.0	6.2
UK	-3.7	-4.5	-5.2	-4.5	-4.1
Germany	7.2	6.9	7.5	8.0	7.7
France	-2.5	-2.0	-1.8	-1.3	-1.7
Italy	-0.5	0.9	1.8	2.6	2.6
Spain	-0.4	1.5	-0.1	0.6	0.5
Finland	-1.9	-1.9	-1.8	-1.2	-1.1
Estonia	-1.8	-1.1	-0.5	-0.7	-0.8
Latvia	-2.5	-0.8	-2.9	-2.6	-3.0
Lithuania	-0.2	1.5	-0.5	0.0	0.5
Poland	-3.5	-1.3	-1.0	-1.5	-1.8
Russia	3.6	1.6	2.5	1.9	1.2
India	-4.7	-1.7	-1.5	-2.0	-2.0
Brazil	-2.4	-3.6	-4.2	-3.9	-4.3

Monetary policy rates

	9.3.15	3M	31.12.15	30.06.16	31.12.16
US	0.25	0.25	0.75	1.25	2.00
Japan	0.10	0.10	0.10	0.10	0.10
Euro area	0.05	0.05	0.05	0.05	0.05
Denmark	0.05	0.05	0.05	0.05	0.05
Sweden	-0.10	-0.20	-0.20	-0.20	0.50
Norway	1.25	0.75	0.75	0.75	0.75
UK	0.50	0.50	0.75	1.25	1.75
Switzerland	-0.75	-0.75	-0.75	-0.75	-0.75
Poland	1.50	1.50	1.50	1.50	2.50
Russia	15.00	14.00	12.00	11.00	9.00
China	5.35	5.35	5.35	5.35	5.35
India	7.50	7.25	7.00	6.75	6.75
Brazil	12.75	13.25	13.25	12.75	12.00

Monetary policy rate spreads vs Euro area

	9.3.15	3M	31.12.15	30.06.16	31.12.16
US	0.20	0.20	0.70	1.20	1.95
Japan[1]	-0.15	-0.15	-0.65	-1.15	-1.90
Euro area	-	-	-	-	-
Denmark	0.00	0.00	0.00	0.00	0.00
Sweden	-0.15	-0.25	-0.25	-0.25	0.45
Norway	1.20	0.70	0.70	0.70	0.70
UK	0.45	0.45	0.70	1.20	1.70
Switzerland	-0.80	-0.80	-0.80	-0.80	-0.80
Poland	1.45	1.45	1.45	1.45	2.45
Russia	14.95	13.95	11.95	10.95	8.95
China	5.30	5.30	5.30	5.30	5.30
India	7.45	7.20	6.95	6.70	6.70
Brazil	12.70	13.20	13.20	12.70	11.95

1) Spread vs USA

3-month rates

	9.3.15	3M	31.12.15	30.06.16	31.12.16
US	0.26	0.25	0.85	1.35	2.15
Euro area	0.04	0.05	0.00	0.00	0.00
Denmark	-0.21	-0.20	-0.10	0.00	0.10
Sweden	0.06	-0.05	-0.05	-0.05	0.65
Norway	1.36	0.85	0.95	0.95	0.95
UK	0.56	0.60	0.85	1.40	1.90
Poland	1.65	1.60	1.60	1.75	2.75
Russia	16.89	16.30	14.20	13.00	11.00

3-month spreads vs Euro area

	9.3.15	3M	31.12.15	30.06.16	31.12.16
US	0.23	0.20	0.85	1.35	2.15
Euro area	-	-	-	-	-
Denmark	-0.25	-0.25	-0.10	0.00	0.10
Sweden	0.02	-0.10	-0.05	-0.05	0.65
Norway	1.33	0.80	0.95	0.95	0.95
UK	0.53	0.55	0.85	1.40	1.90
Poland	1.62	1.55	1.60	1.75	2.75
Russia	16.86	16.25	14.20	13.00	11.00

10-year government benchmark yields

	9.3.15	3M	31.12.15	30.06.16	31.12.16
US	2.23	2.20	2.40	2.80	3.20
Euro area	0.34	0.40	0.60	0.80	1.00
Denmark	0.39	0.40	0.65	1.00	1.25
Sweden	0.82	0.90	1.10	1.50	2.50
Norway	1.61	1.45	1.50	1.70	1.95
UK	1.94	1.90	2.20	2.60	3.00
Poland	2.52	2.40	2.75	3.00	3.25

10-year yield spreads vs Euro area

	9.3.15	3M	31.12.15	30.06.16	31.12.16
US	1.89	1.80	1.80	2.00	2.20
Euro area	-	-	-	-	-
Denmark	0.05	0.00	0.05	0.20	0.25
Sweden	0.48	0.50	0.50	0.70	1.50
Norway	1.27	1.05	0.90	0.90	0.95
UK	1.60	1.50	1.60	1.80	2.00
Poland	2.18	2.00	2.15	2.20	2.25

Exchange rates vs EUR

	9.3.15	3M	31.12.15	30.06.16	31.12.16
EUR/USD	1.09	1.08	1.05	1.03	1.00
EUR/JPY	131.4	135.0	136.5	136.5	135.0
EUR/DKK	7.45	7.45	7.45	7.45	7.45
EUR/SEK	9.19	9.30	9.10	9.00	8.90
EUR/NOK	8.59	8.50	8.30	8.15	8.00
EUR/GBP	0.72	0.70	0.69	0.68	0.66
EUR/CHF	1.07	1.05	1.05	1.08	1.10
EUR/PLN	4.12	4.30	4.20	4.10	4.00
EUR/RUB	66.0	65.9	65.1	57.7	51.0
EUR/CNY	6.80	6.75	6.53	6.33	6.10
EUR/INR	68.1	67.0	63.0	60.8	57.0
EUR/BRL	3.36	3.46	3.36	3.19	3.00

Exchange rates vs USD

	9.3.15	3M	31.12.15	30.06.16	31.12.16
-					
USD/JPY	120.9	125.0	130.0	132.5	135.0
USD/DKK	6.86	6.90	7.10	7.23	7.45
USD/SEK	8.46	8.61	8.67	8.74	8.90
USD/NOK	7.91	7.87	7.90	7.91	8.00
GBP/USD	1.51	1.54	1.52	1.51	1.52
USD/CHF	0.98	0.97	1.00	1.05	1.10
USD/PLN	3.79	4.0	4.0	4.0	4.0
USD/RUB	60.7	61.0	62.0	56.0	51.0
USD/CNY	6.26	6.25	6.22	6.15	6.10
USD/INR	62.7	62.0	60.0	59.0	57.0
USD/BRL	3.09	3.20	3.20	3.10	3.00

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