Kingdom of Denmark
Rating Report

SCOPE AAA STABLE OUTLOOK

Credit strengths	Credit challenges
• Wealthy and competitive economy • Sound public finances and low public debt • Solid external position • Strong institutional framework and stable governance	• Vulnerabilities related to high property prices • High levels of household debt

Rating rationale:

Wealthy and competitive economy: Denmark has one of the highest GDP-per-capita ratios in Europe and ranks first in the 2022 IMD World Competitiveness Ranking. Economic output proved resilient during the Covid-19 pandemic and has been growing rapidly in subsequent years. Slower economic growth in 2023 should help return the economy to a more neutral cycle.

Public finances: Denmark benefits from strong public finances characterised by budget surpluses in the near term, broadly balanced budgets over the medium term and a moderate debt burden. Challenges of an ageing population and investment needs are being addressed.

Strong external position: Denmark has generated a current account surplus every year since 1998, and we expect continued high surpluses over the coming years. A credible commitment to maintaining its fixed exchange rate is backed by large official reserves.

Strong institutional framework: Denmark ranks among the top countries globally in terms of governance indicators. It has a strong record of implementing structural reforms, maintaining fiscal discipline and conducting appropriate monetary policy aligned with the ECB.

Rating challenges include: i) vulnerabilities in the Danish financial system, including from high household debt; and ii) banking sector vulnerabilities related to high property prices.

Denmark's sovereign rating drivers

Risk pillars		Quantitative		Reserve currency	Qualitative*	Final rating
		Weight	Indicative rating	Notches	Notches	
Domestic Economic Risk		35%	aaa	DKK [+0]	+1/3	AAA
Public Finance Risk		20%	aaa		+1/3	
External Economic Risk		10%	aaa		+1/3	
Financial Stability Risk		10%	aaa		-1/3	
ESG Risk	Environmental Factors	5%	aa+		+1/3	
	Social Factors	7.5%	bb		0	
	Governance Factors	12.5%	aaa		+1/3	
Indicative outcome			**aaa**		**+1**	
Additional considerations					**0**	

Note: *The qualitative scorecard adjustments, capped at one notch per rating pillar, are weighted equally with an aggregate adjustment rounded to the nearest integer. The reserve currency adjustment applies to currencies in the IMF's SDR basket. For details, please see Scope's 'Sovereign Ratings' methodology. Source: Scope Ratings

Outlook and rating triggers

The Stable Outlook reflects our view that risks to the ratings are balanced.

Positive rating-change drivers	Negative rating-change drivers
• Not applicable	• Increasing financial system risks, resulting in broader systemic risk • A severe economic shock, resulting in weaker medium-term growth prospects • A deteriorating fiscal outlook, resulting in an upward trend in government debt ratios

Ratings and Outlook

Foreign currency

Long-term issuer rating	AAA/Stable
Senior unsecured debt	AAA/Stable
Short-term issuer rating	S-1+/Stable

Local currency

Long-term issuer rating	AAA/Stable
Senior unsecured debt	AAA/Stable
Short-term issuer rating	S-1+/Stable

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Bloomberg: RESP SCOP

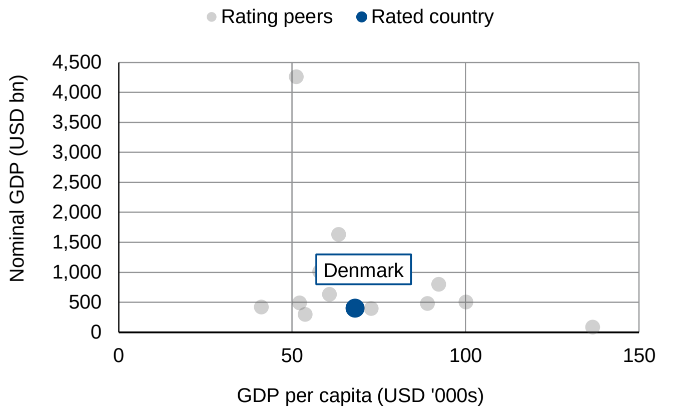
Domestic Economic Risks

- **Growth outlook:** Economic output proved resilient during the Covid-19 pandemic, rebounding strongly by 4.9% in 2021 and 3.8% in 2022 after a shallow decline of 2.1% in 2020. Following the economic upswing of the past two years, slower growth should help gradually return the Danish economy to a more neutral cycle. Consumption is likely to remain weak in early 2023 due to lower household purchasing power, low consumer confidence and declining house prices. Rising wages will support private spending during the second half of 2023, helping offset weaker export growth. We expect moderate growth in the Danish economy, with GDP increasing by 0.6% in 2023, supported by production growth in the pharmaceutical sector. For 2024 we expect economic output to grow by 1.1%, before returning to Denmark's medium-term growth potential of around 1.5% per year in 2025.
- **Inflation and monetary policy:** Energy, food and transport prices have been rising sharply over the past year. Inflation (CPI) fell to 6.7% in March 2023 compared with the same month in 2022, declining from its peak of 10.1% in October 2022. While headline inflation has started to fall, core inflation (CPI excluding energy and unprocessed food) remains elevated at 6.4% in March 2023. We expect core inflation to decline gradually over the next two years. Denmark's central bank pegs its exchange rate to the euro. As euro area monetary policy targets an inflation rate of 2% over the medium term, the fixed-exchange-rate policy provides a framework for returning inflation to a low and stable level. However, limited monetary policy and exchange rate flexibility restrict the central bank's ability to address financial imbalances, control money supply and take unconventional measures such as quantitative easing. Denmark's central bank increased its deposit rate to 2.60% in March 2023. This remains in line with the ECB's monetary policy, whose deposit facility rate increased to 3.00% in March.
- **Labour markets:** Denmark has a highly competitive and flexible labour market. The unemployment rate fell to 4.5% in 2022. We expect the unemployment rate to reach 4.7% in 2023 due to slowing economic growth then rise slightly to 4.8% in 2024. Several two-year collective wage agreements were concluded in February and March of this year. The increases are significantly higher than in past negotiations but are aligned with wage rises in major euro area economies.

Overview of Scope's qualitative assessments for Denmark's *Domestic Economic Risks*

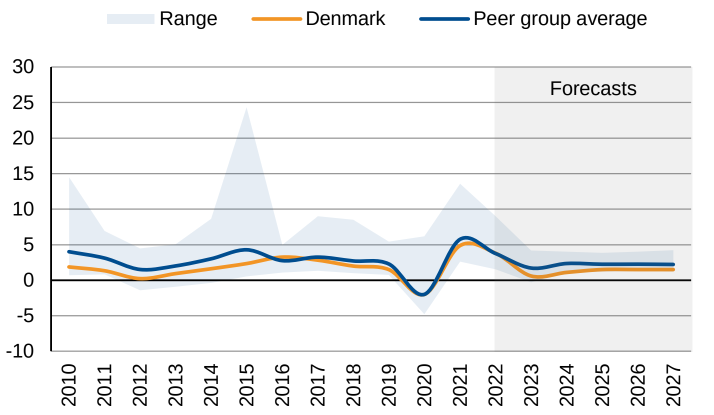
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aaa	Growth potential of the economy	Neutral	0	Robust growth potential and pre-crisis track record of sustained growth
	Monetary policy framework	Neutral	0	The fixed-exchange-rate policy helps anchor inflation and has supported external competitiveness, but it restricts the central bank's ability to control money supply.
	Macro-economic stability and sustainability	Strong	+1/3	Competitive economy, favourable business environment and highly skilled labour force support productivity growth; highly flexible labour market

Nominal GDP and GDP per capita, USD



Source: IMF World Economic Outlook (WEO), Scope Ratings

Real GDP growth, %



Source: IMF WEO, Scope Ratings forecasts

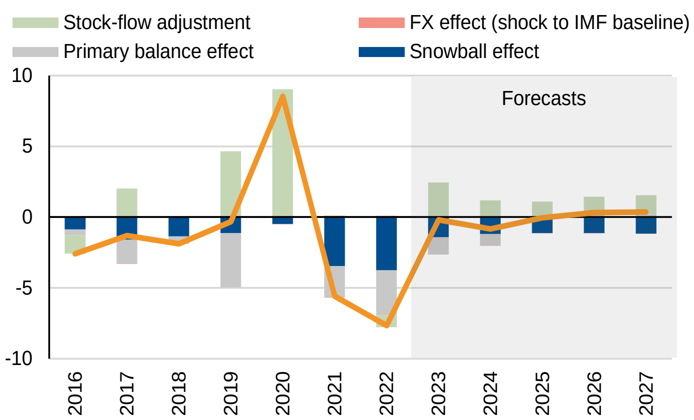
Public Finance Risks

- **Fiscal outlook:** The March 2023 budget proposals reflect a tightened fiscal policy with the aim of helping contain inflationary pressures by reducing economic activity. Policy measures announced include DKK 2.4bn (0.1% of GDP) to be spent on inflation support for the most vulnerable households and DKK 2bn to tackle hospital backlogs. In response to the escalation of the Russia-Ukraine war, the government also reaffirmed its intention to raise defence spending from 1.4% of GDP in 2020 to 2% of GDP by 2030 and establish a Ukraine fund of around DKK 7bn (0.3% of GDP) to fund military and operational support. We expect the fiscal balance to remain in surplus of around 1.5% in 2023 and 1% in 2024, down from 3.6% in 2022. Denmark's fiscal outlook is supported by its forward-looking pension policies given an ageing population. The retirement age is gradually being increased to 67 and is expected to rise to 68 by 2030, after which it will be linked to future increases in life expectancy.
- **Debt trajectory:** Denmark's general government debt ratio declined in the years before the pandemic, falling from 46.1% of GDP in 2011 to 33.7% in 2019. Fiscal support measures caused the ratio to increase to 42.2% in 2020, which compares favourably to an average of around 50% in peer countries with AAA ratings. The continued fiscal surpluses and fast economic recovery following the pandemic lowered the debt ratio to around 29% in 2022. Spending pressures due to an ageing population and continued investment needs are likely to result in a broadly stable public debt level over the next few years.
- **Debt profile and market access:** Denmark benefits from a stable debt structure and excellent market access. Financing costs have increased in line with other highly rated economies, with the 10-year yield rising from 0.1% at the beginning of 2022 to 2.6% in February 2023. The average maturity of government debt stood at nine years as of February 2023, longer than that of most peer countries. The government retains significant financing flexibility through a cash buffer of DKK 162bn (5.9% of GDP) held at the central bank, which increased in 2022 due to a significantly larger budget surplus than expected. The buffer remains well above the target range of DKK 50bn-75bn.

Overview of Scope's qualitative assessments for Denmark's *Public Finance Risks*

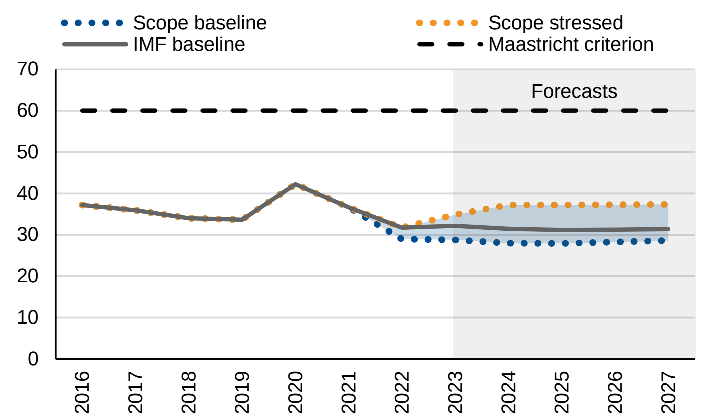
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aaa	Fiscal policy framework	Strong	+1/3	Appropriate response to Covid-19 and energy shock; pre-crisis track record of balanced budgets; progressive pension reform to adapt retirement age
	Debt sustainability	Neutral	0	Stable debt trajectory
	Debt profile and market access	Neutral	0	Excellent market access; low government financing costs in line with those of peers

Contributions to changes in debt levels, pp of GDP



Source: IMF WEO, Scope Ratings forecasts

Debt-to-GDP forecasts, % of GDP



Source: IMF WEO, Scope Ratings forecasts

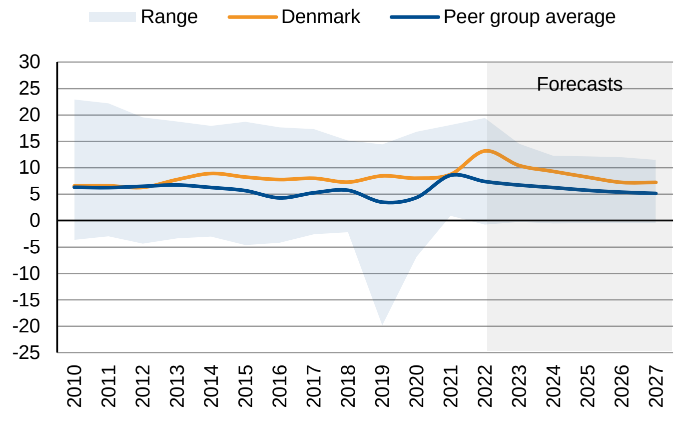
External Economic Risks

- **Current account:** Denmark has consistently run current account surpluses above the peer group average, reflecting its large financial sector, exceptionally high domestic savings and strong exports of high-value goods and services. In Q3 2022 Denmark's current account surplus reached a new high of 16.9% of GDP. This was driven by increased services exports and particularly high freight rates but also strong pharmaceutical exports and weaker domestic demand that resulted in lower imports. While the current account surplus fell in the final quarter of 2022, it was still exceptionally high at 13.2% of GDP for the full year and is likely to remain elevated. Although we expect the economic slowdown among key trading partners to slow export growth in 2023, Denmark has a highly competitive and less cyclically sensitive export sector. At the same time, the country's demand for imports is likely to decrease due to slowing economic growth. Denmark is still a net energy importer but the redevelopment of the Tyra gas field should be completed by next winter. This is expected to deliver 2.8 billion cubic metres of gas per year, which would exceed Denmark's annual gas consumption during 2020 and 2021.
- **External position:** Danish external debt declined from above 185% of GDP in 2010 to around 145% in 2019, before increasing again at the onset of the pandemic. It stood at 124% in 2022 and related mainly to debt in the financial institutions sector (71% of GDP) and intercompany lending (25% of GDP). Short-term debt relative to total gross external debt has remained stable over the past decade and stood at 46% in 2022. Reflecting Denmark's high level of domestic savings, the country's external position remains sound with a net international investment position of 74.5% of GDP as of Q3 2022, up from negative 5% in 2008.
- **Resilience to shocks:** Denmark's central bank has intervened repeatedly in foreign-exchange markets since October 2019 to support the krone's peg to the euro. It has succeeded in maintaining the peg in line with its primary mandate. Denmark's credible commitment to maintaining its fixed exchange rate is backed by its large official reserves totaling DKK 602.9bn (22% of 2022 GDP) as of February 2023. While the krone is not considered to be a reserve currency, it is seen as a regional safe-haven currency due to the longstanding exchange rate peg.

Overview of Scope's qualitative assessments for Denmark's *External Economic Risks*

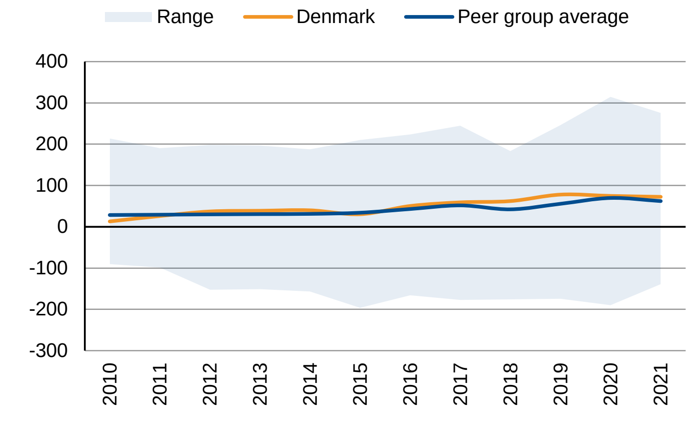
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aaa	Current account resilience	Neutral	0	Low cyclicality of export composition and external sector competitiveness support current account resilience.
	External debt structure	Neutral	0	Relatively high external debt, especially in the financial institutions sector
	Resilience to short-term external shocks	Strong	+1/3	Very large net external creditor position, regional safe-haven currency

Current account balance, % of GDP



Source: IMF WEO, Statistics Denmark, Scope Ratings

Net international investment position (NIIP), % of GDP



Source: IMF, Scope Ratings

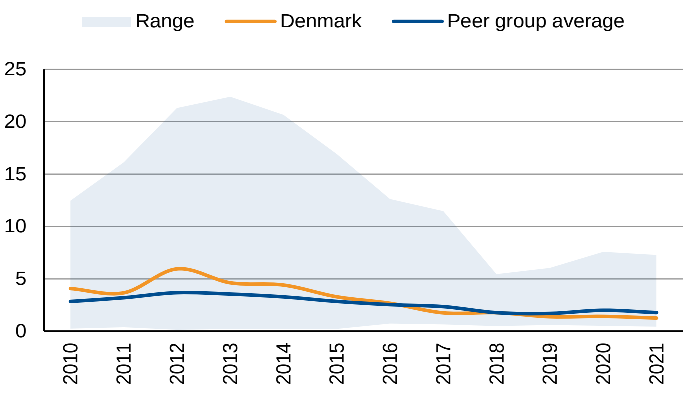
Financial Stability Risks

- **Banking sector:** The banking sector is entering the current period of slower growth and high inflation from a relatively strong position. Overall, the Systemic Risk Council has noted that the sector is in a good position to withstand the recent deterioration of financial market conditions. The share of non-performing loans stood at 1.4% in Q3 2022 (compared to a 1.8% euro area average), while regulatory Tier 1 capital to risk-weighted assets stood at 19.5% (compared to a 16.3% EU average). However, there are large differences across credit institutions, and the central bank's semi-annual stress test indicated that some systemic credit institutions come close to breaching capital buffer requirements in a severe recession scenario.
- **Private debt:** Household debt amounted to 255% of net disposable income in 2021, the highest among OECD countries. High levels of mortgage debt have increased vulnerability to rising interest rates, higher unemployment and sharp declines in house prices. However, these risks must be viewed in the context of very high levels of household assets, with Danish households' net worth at 989% of their net disposable income in 2021, the highest level in the OECD. This provides a strong safety net against short-term income shocks.
- **Financial imbalances:** House prices have decreased by around 10% from their peak in the second quarter of 2022 as the economic slowdown and rising interest rates drive a market correction. The government's planned tax reform in 2024, which would link housing taxes to house prices, should help reduce price fluctuations in future. The Systemic Risk Council previously noted risks associated with a rising number of variable-rate mortgage loans with deferred amortisation granted by credit institutions, even to homeowners with high loan-to-value ratios. The financial system is exposed to the domestic housing sector, with mortgage banks' real estate lending comprising around 44% of total Danish financial sector assets as of January 2023. Denmark's high level of household savings and assets held in the pension system facilitated the development of the world's largest mortgage-covered bond market. A sharper correction in the housing market could result in spillover effects in Denmark's highly interconnected financial system of mortgage credit institutions, pension funds and insurance companies. The Danish central bank has concluded that mortgage credit institutions have enough liquidity to withstand a 20% drop in property prices and still meet liquidity demands.

Overview of Scope's qualitative assessments for Denmark's *Financial Stability Risks*

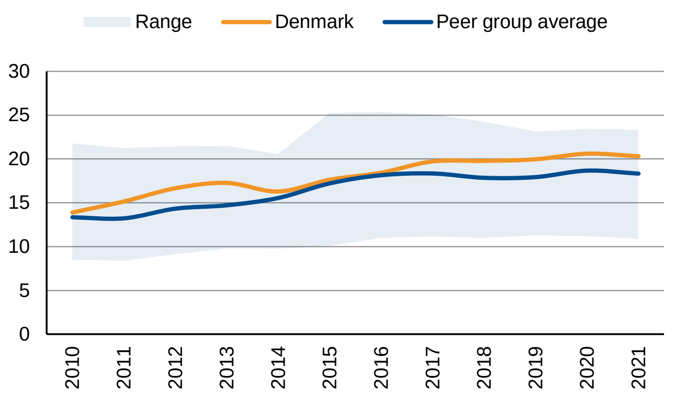
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aaa	Banking sector performance	Neutral	0	High capitalisation levels, stable levels of non-performing loans
	Banking sector oversight	Neutral	0	Prudent oversight under Denmark's central bank and financial supervisory authority; improvements in anti-money laundering/combating the financing of terrorism framework
	Financial imbalances	Weak	-1/3	High private-sector debt, large size of banking sector vis-à-vis the real economy and high interconnectedness in the Danish financial system

Non-performing loans, % of total loans



Source: IMF, Scope Ratings

Tier 1 ratio, % of risk-weighted assets



Source: IMF, Scope Ratings

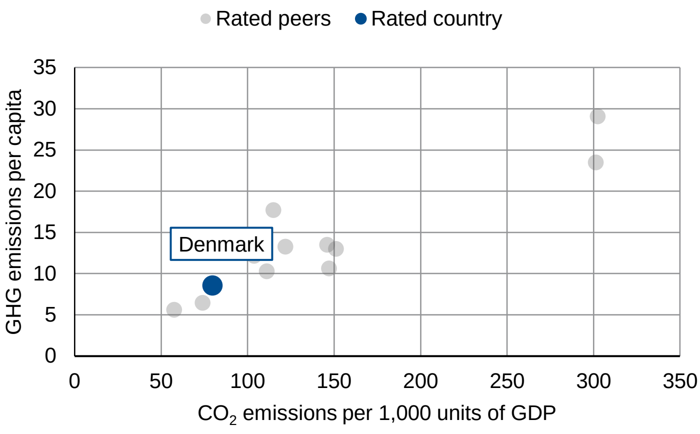
ESG Risks

- **Environment:** Denmark aims to reduce greenhouse gas emissions by 70% by 2030 (relative to 1990 levels) and reach carbon neutrality by 2045. To ensure independence from Russian gas, the government also aims to achieve 100% green gas in heating and quadruple green power production by 2030. The country has earmarked 60% of its share of the EU's Recovery and Resilience Facility for green initiatives, well above the EU's 37% target. Its first green bond was issued in January 2022 and a further 10-year green bond is planned for the second half of 2023. Around 33% of energy consumption came from renewable sources in 2021, and coal consumption has declined rapidly in recent years, from 20% in 2010 to just 8% in 2021. Around 84% of electricity production came from renewable sources, with more than half from wind energy. The Danish Council on Climate Change noted that while the Danish government has adopted significant mitigation measures and climate initiatives, there is still a reduction gap of 6m tonnes of CO_2 to reach the 70% emissions reduction target by 2030, and further policy initiatives will be required to fill this gap. The council suggested focusing on the implementation of already agreed measures and addressing emissions from the agricultural sector.
- **Social:** Denmark benefits from high GDP per capita and an advanced social safety net, which contributes to low income inequality. However, the elevated old-age dependency ratio places increasing demands on welfare services, particularly healthcare. Non-EU migrants experience a high jobless rate with persistent employment gaps relative to Danes due to insufficient job qualifications. Besides continued investment in education and digitalisation, the new government plans to raise productivity and increase labour supply by offering tax cuts that encourage people to work more and by abolishing a public holiday.
- **Governance:** Following the November 2022 general election, Denmark's Social Democratic leader Mette Frederiksen formed the first bipartisan government in four decades in coalition with the Liberals and the Moderates. While minority governments are common in Denmark since gaining representation in parliament requires only 2% of the vote, the new coalition holds a practical majority with 89 of 179 seats as four seats go to lawmakers from Greenland and the Faroe Islands, who do not tend to intervene in Danish domestic politics.

Overview of Scope's qualitative assessments for Denmark's *ESG Risks*

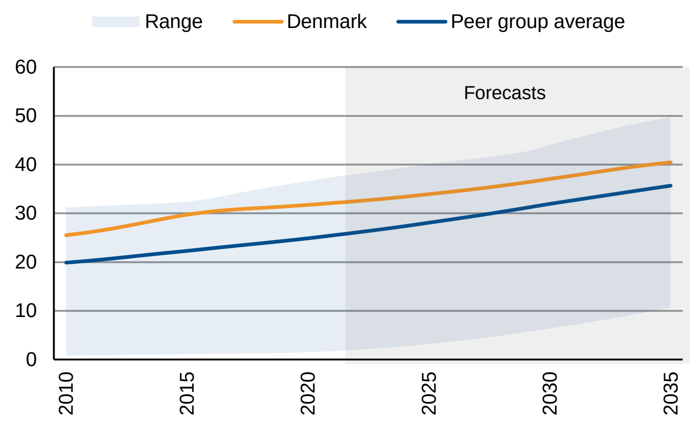
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aa+	Environmental factors	Strong	+1/3	Strong environmental standards, ongoing allocation of resources to achieve ambitious long-term targets for carbon neutrality and emissions reduction
	Social factors	Neutral	0	Relatively favourable demographics, well-established social safety nets, inclusive labour market
	Governance factors	Strong	+1/3	High-quality institutions, stable political environment

Emissions per GDP and per capita, $mtCO_2e$



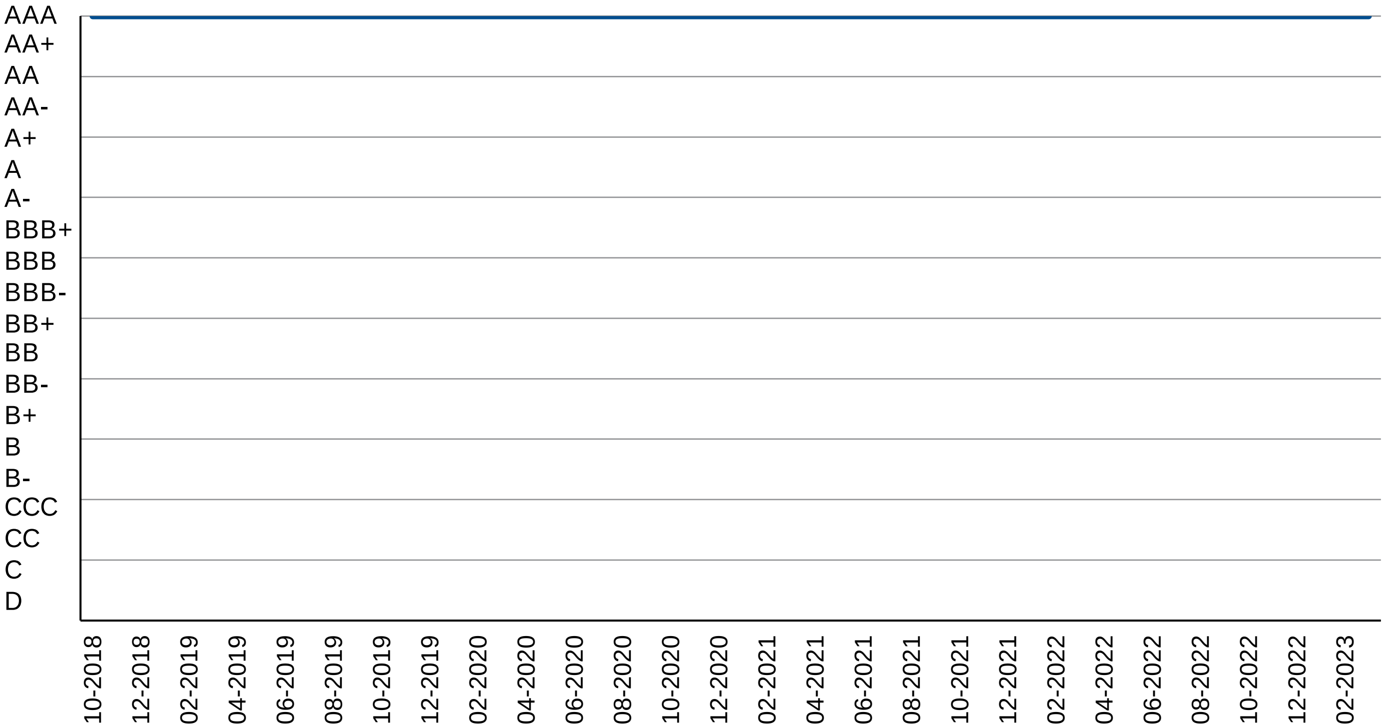
Source: European Commission, Scope Ratings

Old-age dependency ratio, %



Source: United Nations, Scope Ratings

Appendix I. Rating history



NB. Positive/Negative Outlooks are treated with a +/-0.33-notch adjustment. Credit Watch positive/negative with a +/-0.67-notch adjustment.

Appendix II. Rating peers

Rating peers are related to sovereigns with an indicative rating in the same rating category or in adjacent categories per Scope's Core Variable Scorecard, including a methodological reserve-currency adjustment.

Peer group*
Finland
Germany
Ireland
Luxembourg
Netherlands
Norway
Sweden
Switzerland

*Publicly rated sovereigns only; the full sample may be larger.

Appendix III. Statistical table for selected CVS indicators

This table presents a selection of the indicators (24 out of 30 – with the governance indicator reflecting a composite of six indicators) used in Scope's quantitative model, the Core Variable Scorecard, in line with Scope's Sovereign Rating Methodology. The metrics and sources for the data presented here ensure comparability across global peers and may therefore differ from national and other selective international statistics.

Pillar	Core variable	Source	2017	2018	2019	2020	2021	2022
Domestic Economic	**GDP per capita, USD '000s**	IMF	57,773	61,724	59,679	61,006	68,202	65,713
	Nominal GDP, USD bn	IMF	332.1	356.8	346.5	355.2	398.3	386.7
	Real growth, %	IMF	2.8	2.0	1.5	-2.0	4.9	2.6
	CPI inflation, %	IMF	1.1	0.7	0.7	0.3	1.9	7.2
	Unemployment rate, %	WB	5.8	5.1	5.0	5.6	4.8	-
Public Finance	**Public debt, % of GDP**	IMF	35.9	34.0	33.7	42.2	36.6	31.8
	Interest payment, % of revenue	IMF	-0.2	-0.7	-0.5	-0.6	-0.8	-0.8
	Primary balance, % of GDP	IMF	1.7	0.4	3.9	-0.1	2.2	0.8
External Economic	**Current account balance, % of GDP**	IMF	8.0	7.3	8.5	8.0	8.8	8.2
	Total reserves, months of imports	IMF	5.0	4.2	4.0	4.6	4.3	-
	NIIP, % of GDP	IMF	59.0	62.0	77.7	74.5	72.2	-
Financial Stability	**NPL ratio, % of total loans**	IMF	1.7	1.8	1.4	1.4	1.2	-
	Tier 1 ratio, % of risk-weighted assets	IMF	17.8	19.0	19.4	19.9	20.2	19.8
	Credit to private sector, % of GDP	WB	161.8	161.3	161.4	163.7	-	-
ESG	**CO_2 per EUR 1,000 of GDP, $mtCO_2e$**	EC	106.9	105.0	92.3	79.8	80.1	-
	Income share of bottom 50%, %	WID	21.7	21.6	21.5	21.4	21.4	-
	Labour force participation rate, %	WB	77.9	78.2	79.0	-	-	-
	Old-age dependency ratio, %	UN	30.1	30.6	31.0	31.5	31.9	32.3
	Composite governance indicators*	WB	1.6	1.7	1.7	1.7	1.8	-

* Average of the six World Bank Worldwide Governance Indicators

Appendix IV. Economic development and default indicators

IMF Development Classification	Advanced economy
5y USD CDS spread (bps) as of 13 April 2023	14.1

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