

Research Denmark

Danish CPI vs euro area HICP inflation

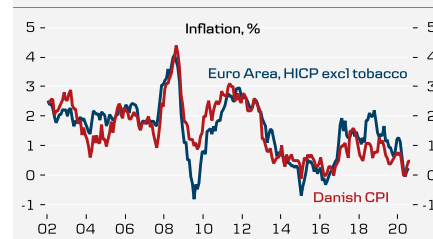
- Several specific events and technicalities regarding data collection drive Danish inflation on a monthly basis.
- Danish inflation has been well anchored in the euro area for years but it has been lower since 2018, with a key reason lower rent increases for housing, something that looks to be the new normal.
- As a rule of thumb, oil prices affect Danish inflation by half as much as the euro area.

In the short run, many idiosyncratic events affect Danish inflation and these can drive it above or below that of the euro area. Unlike in the euro area, such events do not even out among other noise. One example is book prices – measured as an index including the 20 most popular books. Over the years, these have fluctuated heavily. In several months in 2015, they were up 30-50% y/y, pulling up inflation by up to 0.25pp, after which there was a period with price declines. Currently, they stand at up 34% y/y. The new tobacco tax is also pulling CPI inflation up, by 0.4pp. As opposed to the euro area, tobacco is included in the index to which Danish inflation-linked government bonds link.

As a rule of thumb, the direct feed-through from oil prices to Danish CPI inflation is about half that of the euro area, as Danish people drive their car less and many heat their homes with district heating, the price of which is not particularly correlated with oil. The weight on fuel, natural gas and liquid fuels for heating in Denmark is slightly less than half of that for the euro area. On the one hand, this might underestimate the total effect on inflation, as it accounts only for the direct feed-through to prices. On the other, it does not take into account that natural gas prices do not always correlate with oil.

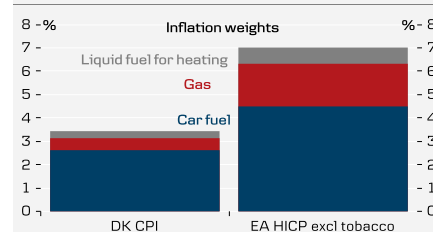
Until a few years ago, Danish inflation was well anchored in the euro area if you looked beyond the monthly noise. From the introduction of the euro in 1998 until 2017, the annual difference between Danish CPI and euro area HICP (excluding tobacco) inflation was just 0.05pp. However, since then it has increased somewhat. The key difference between the two measures (besides tobacco) is the weight of housing rent, as owner-occupied housing (approximated by rental) is also accounted for in the CPI. For this reason, housing rent weighs 20.7% in Danish CPI but only 6.7% in euro area HICP excluding tobacco. Since 2011, housing rent has gradually contributed less to inflation in Denmark and it no longer lifts Danish CPI significantly above that of the euro area. We know that the regulated part of the private rental market may not increase rents by more than the annual increase in the net price index from the previous summer. This was only 0.5% in July, so low inflation is self-reinforcing in this way. In the social housing sector, where rents are set according to costs, the low level of interest rates is helping to keep rents subdued. Hence, there is nothing to indicate that upcoming rent increases should be significantly higher than has been the case in recent years.

Inflation has been lower in Denmark in recent years



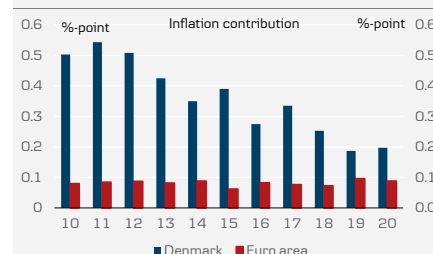
Source: Statistics Denmark, Eurostat, Macrobond Financial

Oil-related energy weights are twice as heavy in the euro area as in Denmark



Source: Statistics Denmark, Eurostat, Macrobond Financial

Danish rent increases have declined



Source: Statistics Denmark, Eurostat, Macrobond Financial

Analyst

Bjorn Tangaa Sillemann
+45 45 12 82 29
bjsi@danskebank.dk

Disclosures

This research report has been prepared by Danske Bank A/S ('Danske Bank'). The author of this research report is Bjørn Tangaa Sillemann, Analyst.

Analyst certification

Each research analyst responsible for the content of this research report certifies that the views expressed in the research report accurately reflect the research analyst's personal view about the financial instruments and issuers covered by the research report. Each responsible research analyst further certifies that no part of the compensation of the research analyst was, is or will be, directly or indirectly, related to the specific recommendations expressed in the research report.

Regulation

Danske Bank is authorised and subject to regulation by the Danish Financial Supervisory Authority and is subject to the rules and regulation of the relevant regulators in all other jurisdictions where it conducts business. Danske Bank is subject to limited regulation by the Financial Conduct Authority and the Prudential Regulation Authority (UK). Details on the extent of the regulation by the Financial Conduct Authority and the Prudential Regulation Authority are available from Danske Bank on request.

Danske Bank's research reports are prepared in accordance with the recommendations of the Danish Securities Dealers Association.

Conflicts of interest

Danske Bank has established procedures to prevent conflicts of interest and to ensure the provision of high-quality research based on research objectivity and independence. These procedures are documented in Danske Bank's research policies. Employees within Danske Bank's Research Departments have been instructed that any request that might impair the objectivity and independence of research shall be referred to Research Management and the Compliance Department. Danske Bank's Research Departments are organised independently from, and do not report to, other business areas within Danske Bank.

Research analysts are remunerated in part based on the overall profitability of Danske Bank, which includes investment banking revenues, but do not receive bonuses or other remuneration linked to specific corporate finance or debt capital transactions.

Financial models and/or methodology used in this research report

Calculations and presentations in this research report are based on standard econometric tools and methodology as well as publicly available statistics for each individual security, issuer and/or country. Documentation can be obtained from the authors on request.

Risk warning

Major risks connected with recommendations or opinions in this research report, including as sensitivity analysis of relevant assumptions, are stated throughout the text.

Expected updates

None.

Date of first publication

See the front page of this research report for the date of first publication.

General disclaimer

This research has been prepared by Danske Bank A/S. It is provided for informational purposes only and should not be considered investment, legal or tax advice. It does not constitute or form part of, and shall under no circumstances be considered as, an offer to sell or a solicitation of an offer to purchase or sell any relevant financial instruments (i.e. financial instruments mentioned herein or other financial instruments of any issuer mentioned herein and/or options, warrants, rights or other interests with respect to any such financial instruments) ('Relevant Financial Instruments').

This research report has been prepared independently and solely on the basis of publicly available information that Danske Bank A/S considers to be reliable but Danske Bank A/S has not independently verified the contents hereof. While reasonable care has been taken to ensure that its contents are not untrue or misleading, no representation or warranty, express or implied, is made as to, and no reliance should be placed on, the fairness, accuracy, completeness or reasonableness of the information, opinions and projections contained in this research report and Danske Bank A/S, its affiliates and subsidiaries accept no liability whatsoever for any direct or consequential loss, including without limitation any loss of profits, arising from reliance on this research report.

The opinions expressed herein are the opinions of the research analysts and reflect their opinion as of the date hereof. These opinions are subject to change and Danske Bank A/S does not undertake to notify any recipient of this research report of any such change nor of any other changes related to the information provided in this research report.

This research report is not intended for, and may not be redistributed to, retail customers in the United Kingdom (see separate disclaimer below) and retail customers in the European Economic Area as defined by Directive 2014/65/EU.

This research report is protected by copyright and is intended solely for the designated addressee. It may not be reproduced or distributed, in whole or in part, by any recipient for any purpose without Danske Bank A/S's prior written consent.

Disclaimer related to distribution in the United States

This research report was created by Danske Bank A/S and is distributed in the United States by Danske Markets Inc., a U.S. registered broker-dealer and subsidiary of Danske Bank A/S, pursuant to SEC Rule 15a-6 and related interpretations issued by the U.S. Securities and Exchange Commission. The research report is intended for distribution in the United States solely to 'U.S. institutional investors' as defined in SEC Rule 15a-6. Danske Markets Inc. accepts responsibility for this research report in connection with distribution in the United States solely to 'U.S. institutional investors'.

Danske Bank A/S is not subject to U.S. rules with regard to the preparation of research reports and the independence of research analysts. In addition, the research analysts of Danske Bank A/S who have prepared this research report are not registered or qualified as research analysts with the New York Stock Exchange or Financial Industry Regulatory Authority but satisfy the applicable requirements of a non-U.S. jurisdiction.

Any U.S. investor recipient of this research report who wishes to purchase or sell any Relevant Financial Instrument may do so only by contacting Danske Markets Inc. directly and should be aware that investing in non-U.S. financial instruments may entail certain risks. Financial instruments of non-U.S. issuers may not be registered with the U.S. Securities and Exchange Commission and may not be subject to the reporting and auditing standards of the U.S. Securities and Exchange Commission.

Disclaimer related to distribution in the United Kingdom

In the United Kingdom, this document is for distribution only to (I) persons who have professional experience in matters relating to investments falling within article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (the 'Order'); (II) high net worth entities falling within article 49(2)(a) to (d) of the Order; or (III) persons who are an elective professional client or a per se professional client under Chapter 3 of the FCA Conduct of Business Sourcebook (all such persons together being referred to as 'Relevant Persons'). In the United Kingdom, this document is directed only at Relevant Persons, and other persons should not act or rely on this document or any of its contents.

Disclaimer related to distribution in the European Economic Area

This document is being distributed to and is directed only at persons in member states of the European Economic Area ('EEA') who are 'Qualified Investors' within the meaning of Article 2(e) of the Prospectus Regulation (Regulation (EU) 2017/1129) ('Qualified Investors'). Any person in the EEA who receives this document will be deemed to have represented and agreed that it is a Qualified Investor. Any such recipient will also be deemed to have represented and agreed that it has not received this document on behalf of persons in the EEA other than Qualified Investors or persons in the UK and member states (where equivalent legislation exists) for whom the investor has authority to make decisions on a wholly discretionary basis. Danske Bank A/S will rely on the truth and accuracy of the foregoing representations and agreements. Any person in the EEA who is not a Qualified Investor should not act or rely on this document or any of its contents.

Report completed: 16 September 2020, 15:32 CEST

Report first disseminated: 17 September 2020, 06:30 CEST