



Greenland's Economy

Autumn 2020

- Economic outlook
- Economic policy
- The public sector

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Summary

Within a short space of time, Greenland's economic situation has changed significantly. The economic progress achieved over a number of years has been disrupted by the COVID-19 pandemic. In response to the outbreak in Greenland, various lockdown initiatives and travel restrictions, etc. were implemented. This largely succeeded in containing the spread of infection in Greenland, and consequently made it possible to start reopening the country. However, Greenland still faces substantial risk as a result of the spread of infection in other countries. Citizens are very vulnerable to the spread of infection, and a high rate of infection would place great strain on Greenland's health service.

The global consequences of the COVID-19 pandemic are vast and in 2020 most countries will be in recession, with a decline in economic activity. Although some reversal is expected in 2021, at the present time it is difficult to predict developments owing to the many uncertainties, including public health trends.

Greenland's economy is adversely affected by the pandemic, but not to the same extent as in the majority of other countries. This is largely attributable to Greenland's special economic structure. The economic assessment presented in this report is for virtually zero growth in 2020, and hence a level of economic activity corresponding to 2019. This assessment is obviously subject to great uncertainty, but a number of indicators suggest that Greenland's economy is not as severely afflicted as it appeared to be when the crisis took hold.

However, that does not mean that the disruption caused by COVID-19 is without implications for Greenland. The tourism and transport sectors, especially, are severely disrupted and face major challenges. It is uncertain when the tourist inflows to Greenland will revert to normal. Other sectors, the fisheries in particular, are impacted by the global economic trend and the ensuing fall in prices. This follows several years of rising prices, and the price fluctuations are within the expected range given the sector's market exposure.

For some years, the employment rate has shown an encouraging trend, and although the COVID-19 crisis has caused an increase in unemployment, the rate remains low. There is still a shortage of skilled labour in a number of sectors, and the need for structural improvements in order to boost employment by means of education, increased mobility and stronger financial incentives to take up employment remains vital.

The Danish Government's financial support packages have been crucial in supporting businesses and wage earners directly affected by the lockdown in Greenland, travel restrictions, etc. However, this is an extraordinary set of economic instruments warranted only in special circumstances and for a limited period of time. The financial support packages should therefore be phased out as soon as possible. However, the tourism and transport sectors have a unique need for support since they are still severely impacted by COVID-19 restrictions. Fluctuations in prices and revenues as a result of altered market conditions ensuing from the global economic crisis cannot be properly resolved by financial support packages. These fluctuations are part of the market risks private-sector businesses have to expect to endure. The introduction of financial support packages in this type of situation overrides the prevailing market forces, and severely strains the process of achieving a self-sustaining economy and safeguarding the Greenlandic Treasury (Landskassen).

The Treasury is under strain from covering the cost of providing financial support packages, emergency flights, etc. and dwindling fisheries resource rent tax revenues, for example. Several years of surpluses in Greenland's public finances have consequently reverted to a substantial deficit in 2020, and a deficit is likewise expected for 2021. Current projections are for a deficit in 2020 at around the DKK 500 million mark, while the budget proposal anticipates a deficit in 2021 of just over DKK 180 million.

These deficits reflect that Greenland has economically and politically managed to support the sectors that bore the brunt of the imposed lockdowns and restrictions. These interventions were thus key in mitigating what might otherwise have been severe economic impacts. Since the fiscal policy for a number of years has focused on avoiding deficits and debt accumulation, there has been a certain room for implementing this mitigation approach.

However, the COVID-19 crisis has still come at a cost to Greenland that places great demands on Greenland's economic policy. Going forward, it will be necessary to direct economic policy at achieving a surplus target in order to avoid increased debt levels. This is compounded by the well-established challenge that an ageing population poses a severe financing problem. Without a realignment of Greenland's economic policy, expenditure will significantly exceed revenue; a situation which would be unsustainable. In this way, the COVID-19 crisis has stepped up the requirements for pursuing a stringent economic policy. There is no economic scope for realising new cost-intensive initiatives in the coming years, since these must be financed while achieving cutbacks in order to attain an economic surplus and ensure fiscal sustainability in relation to the advancing age of the population. There is consequently a great need to draw up a new mid-term economic plan and implement it in specific initiatives.

Meanwhile, the requirements for ensuring a progression towards a more self-sustaining economy are intensifying. This calls for the diversification of trade and industry, which is challenged by the COVID-19 crisis. The tourism sector is under pressure. The global economic crisis has also adversely affected the price on raw materials, which impacts mining operations in terms of both exploration activities, but also the commencement of scheduled mining projects.

However, certain other factors conducive to economic progress and the progression towards a more self-sustaining economy are possible to influence. One case in point is education and vocational training. The challenges and problems in this area are well-established and well understood. For Greenland, these problems cannot be addressed by institutional changes or reforms, but by a targeted and direct intervention to raise standards of education and training throughout the population. The challenge lies in tackling the problems and ensuring the collaboration between parents, teachers and policymakers that will be conducive to real improvements. An immediate step would be to set specific learning targets for secondary school pupils. Trends in this area should be monitored closely, and any non-attainment must result in action. There are also other problems within the education system, which can be tackled concurrently. These particularly concern the large group of school leavers who fail to progress to further education and vocational training. However, deliberations on the general institutional frameworks should in no way hinder the essential measures that can be put in place here and now.

The special-feature chapter in the present report examines the options for realising efficiency improvements and boosting productivity in the public sector; factors of crucial significance for solving the fiscal challenges faced by the Treasury. Greenland's public sector is relatively large owing, to some extent, to the special factors prevailing in a country with a small population scattered over a large land mass. However, the question of whether the right problems are being addressed, and whether they are being addressed effectively, is a central consideration given the size of the public sector.

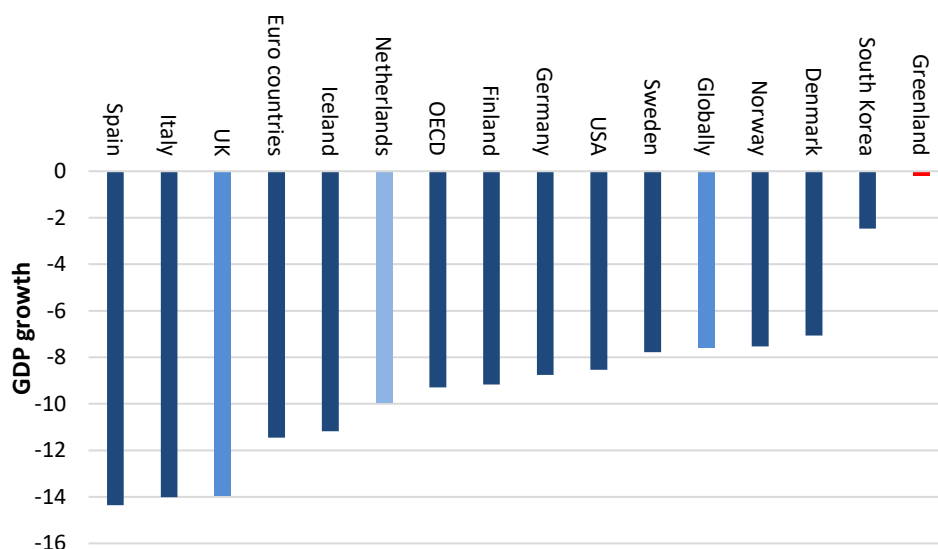
A number of public sector tasks holds potential for efficiency improvements, allowing the same tasks to be carried out with greater effect and more cost-effectively. In this way, citizens will either not perceive any changes or improvements, while the Government of Greenland and municipalities will save on expenditure. If substantial cutbacks or tax increases are to be avoided, while addressing the Treasury's fiscal challenges, it is a requirement to boost efficiency and productivity in the public sector. This will also free up labour, which will facilitate the diversification of trade and industry.

Chapter 1 Economic outlook

Greenland's economic situation has changed significantly as a result of the COVID-19 pandemic. National lockdowns, travel restrictions and other interventions to contain the spread of infection have had major economic impact globally. Uncertainty surrounding both future health implications and economic outcomes is affecting behaviour; households have curbed their spending, and businesses their investment plans. The economic backlash is exacerbated by the fact that this is a global crisis, with many countries affected simultaneously.

One consequence of this is that the economic outlook has changed significantly within a short space of time. Many countries are in recession, with a steep decline in economic activity and employment. International organisations such as the IMF, the OECD and the World Bank are forecasting a fall in global activity in 2020 of 5 percent, and a fall of 7-8 percent for countries in the west; see Figure 1.1. Although the national economies are expected to recover in 2021, the global outlook is subject to great uncertainty. After the initial wave of the pandemic was successfully contained, by late summer, a large number of countries were registering an increase in the infection rate. The continued flare-up of infection and the ensuing economic impacts reduce the likelihood of a rapid return to normal levels of activity. The uncertainty surrounding the future economic outlook is especially great at the present time.

Figure 1.1. Global economic crisis – forecasted decrease in activity, selected countries, 2020



Source: Forecast for Greenland; see Table 1.2; for other countries, OECD Economic Outlook, June 2020. Among the OECD countries, the greatest decline in activity is projected for Spain and the lowest for South Korea.

Greenland's economy was doing well when COVID-19 broke out in the country in March. Growth had been strong since 2015, powered especially by an upturn in the fisheries and in the building and construction sector. The number of registered job-seekers (discounting seasonal fluctuations) was decreasing month by month. Equally, public finances were showing a surplus, and both public and private debt were moderate. Essentially, Greenland's economic situation was encouraging before the COVID-19 pandemic struck.

COVID-19 has also disrupted Greenland. A range of lockdown initiatives were implemented, including travel restrictions. This largely succeeded in containing the spread of infection through the country, allowing domestic reopening to be initiated. However, Greenland still faces substantial risk as a result of the spread of infection in other countries. Citizens are very vulnerable to the spread of infection, and a high rate of infection would place great strain on Greenland's health service.

The COVID-19 crisis is impacting activity and employment, but less so than in other countries. The impacts have also been lesser than indicated at the start of the crisis¹. Greenland's transport and tourism sector is hard hit, but the fisheries are also affected by secondary price impacts. However, the secondary domestic impacts are still modest in Greenland. The current situation for the various sectors of Greenland's economy is summarised in Table 1.1.

Table 1.1. Direct and secondary impacts of the COVID-19 crisis on Greenland's trade and industry

Trade and industry	Percentage share of:			Direct and secondary impacts of the COVID-19 crisis
	jobs	payroll	production	
Fisheries and catches	8.5	10.8	18.6	● Risk of price drops as a result of significant global downturn and fall in demand. Limited volume impacts.
Raw materials extraction industry	0.3	0.5	0.1	● Exploration activity may decrease as a result of global recession and a fall in prices on raw materials.
Industry	6.7	3.6	4.6	● Limited volume impacts at the fish processing plants. But potential challenges with the non-domestic workforce.
Utilities and refuse collection . .	1.8	2.1	2.8	● No direct impacts.
Building and construction activities	6.9	8.0	10.8	● Limited direct impacts, but potential challenges with the non-domestic workforce recruited for construction projects.
Trade	11.5	8.7	9.4	● Decline within tourism especially. Other retail trade may be affected by reduced income growth.
Transport	6.7	8.7	8.5	● Air transport traffic restrictions and regulations. Decline in demand and sluggish adaptation in the tourism sector.
Hotel and restaurant sector . . .	3.1	2.0	2.0	● Significant decline in the number of overseas guests, especially at hotels. Sluggish adaptation in the tourism sector is to be expected.
Postal, telecoms, IT, radio and TV etc. sector.	2.3	2.9	3.7	● No direct impacts. Possibly secondary increased demand for digital solutions.
Financing and business services sector	6.4	7.6	12.0	● Limited direct impacts. Secondary impacts from the decline in tourism and falls in fish prices may affect business services.
General public services and personal services sector	45.8	45.2	27.4	● Limited or no direct impacts. Greenland's health sector may be strained by an increased rate of infection.

Note: Direct and secondary impacts are as assessed by the Economic Council based on currently available statistics and information procured concerning the sectoral impacts of the COVID-19 crisis. The sectoral breakdown conforms to that adopted by Statistics Greenland, which is why industry includes the processing of fish products.

The COVID-19 crisis – as was the case during the global financial crisis – is less disruptive to the economy of Greenland than that of the majority of other countries. This is due to a number of factors: Firstly, Greenland succeeded in rapidly containing and halting the outbreak across the country, and managed to lift a large proportion of domestic lockdowns relatively rapidly. Secondly, Greenland's unique production and industrial structure reduces its exposure to global developments. The activity level in the fishery sector is only to a limited extent affected by economic trends, whereas fish prices are much more sensitive to fluctuations in global market conditions. In addition, the public sector is large, and the block grant from Denmark helps to reduce the dependence of revenues on economic trends. Finally, the self-reinforcing

¹ See Economic Council, Policy Brief 2020-1, the implications of the COVID-19 crisis on Greenland's economy.

economic mechanisms are weaker in Greenland than in many other countries, since the import component of spending and investment is relatively high. The spillover effects of a downturn in tourism, for example, on other industries are lesser than in other countries where domestic inputs play a larger role.

Over the longer term, the COVID-19 crisis may, however, have major implications for Greenland. The tourism and transport sector is hard hit, and the problems of bringing the infection risk under control and the general concerns and hesitancy of consumers may affect the Greenland tourism sector for many years to come. The International Air Transport Association (IATA) predicts that air travel and hence a very large share of tourist traffic will not return to pre-COVID-19 levels until 2024². This will have major implications for Greenland's tourism industry and transport sector. The global economic crisis has also affected prices on raw materials, which impacts mining operations in terms of both exploration activities but also the commencement of scheduled mining projects. The crisis thus has indirect implications for developing a more diversified industry structure as the basis for a self-sustaining economy.

The following sections report in more detail on the economic trend, and the chapter also contains a new economic forecast. The economic policy is discussed in Chapter 2. The data on which this chapter relies are official statistical values. Lockdowns and other restrictions were imposed in the majority of countries in March-April 2020, which means that only limited statistical observations are available for the period after the outbreak of COVID-19. The Economic Report (2020) discusses the immediate effects of the lockdowns based on various indicators.

1.1. The fishery sector

The fishery sector have had several good years. Cod prices in 2019 were 80 percent higher than in 2010 and halibut prices were 50 percent higher, while prawn prices more than doubled; see Figure 1.2. For comparison, consumer prices rose in the same period by approx. 15 percent. With slight variation, the favourable price level was sustained until the end of 2019. Halibut prices fell slightly in the first quarter of 2020 relative to the previous quarter, but were still higher than the average price for 2019. Prawn prices fell in the first quarter of 2020 to a price approx. 6 percent below the average price for 2019. The price of cod, however, rose strongly to approx. 5 percent above the 2019 average price.

The global downturn in the wake of the COVID-19 crisis is tending in the direction of lower demand for fish products, for example, and hence lower fish prices. How far the prices will fall will depend on the severity and the duration of the COVID-19 crisis. The fishing companies are predicting a decrease in export prices of up to 20 percent for Greenlandic fish products depending on species and product for the duration of the pandemic. If this prediction holds true, the price decreases will have major implications for both resource rent tax revenues and for the other indirect fisheries tax revenues. The 2019 Economic Council report calculated that a 20 percent fall in fish prices would reduce public revenue directly by DKK 232m in that resource rent taxes would be down by DKK 113m, income taxes by DKK 92m and corporate taxes by DKK 27m.

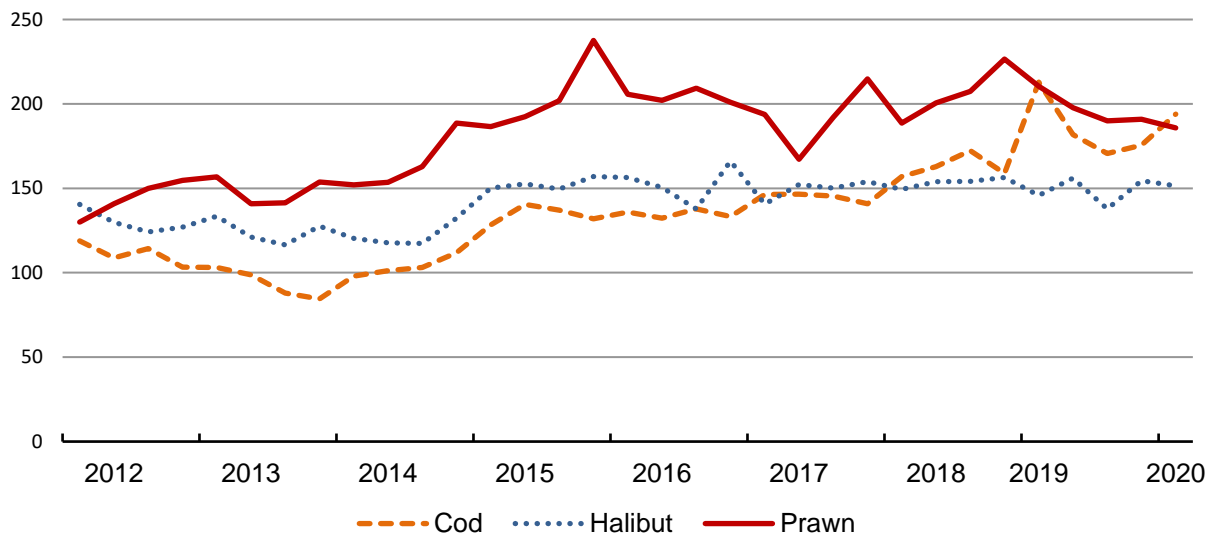
In terms of volume, the fishery in Greenland's territorial waters in 2019 was approx. 12 percent smaller than in 2018. Catches of cod were down for the third year running, and mackerel catches more than halved

² <https://www.iata.org/en/pressroom/pr/2020-07-28-02/>

in 2019 relative to the previous year. Against that, prawn and halibut catches were 9 percent and 2 percent higher, respectively, than in the previous year.

Figure 1.2. Average prices of fish and shellfish, 2012-2020

Index 2010 = 100



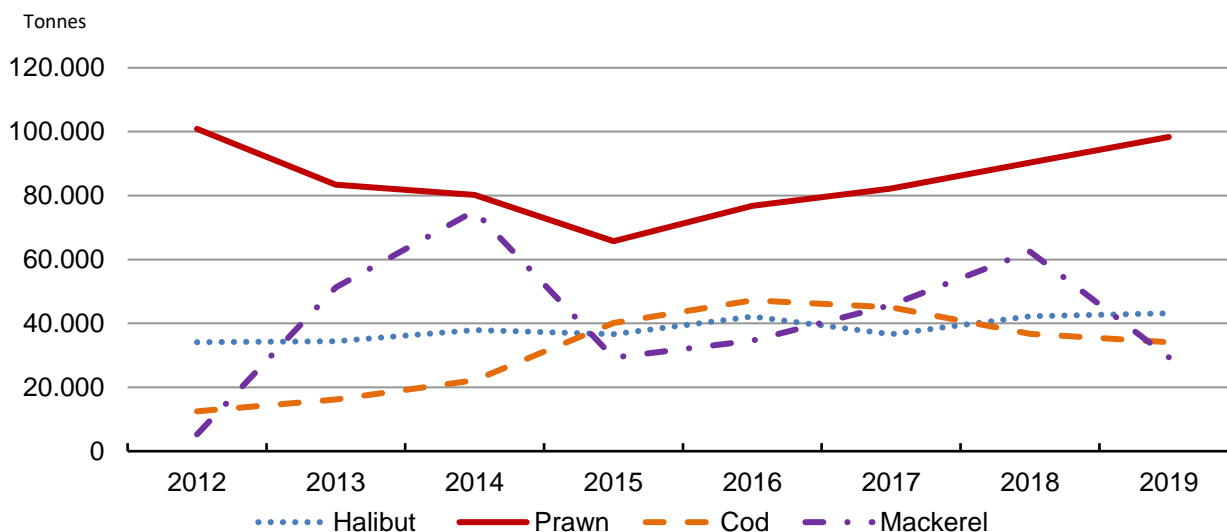
Note: The last observation was made in Q2 2020.
Source: Statistics Greenland.

Up until 2020, catches of prawn were 7-8 percent higher than in the same period in 2019, which may be due to the incorporation of new trawlers in the fleet. The options for flexible utilisation of the quotas may also have affected the timing of the catches. For the economy, the prawn fishery is the most important fishery in Greenland, and is MSC-certified as sustainable. The halibut catch from January to July 2020 was 6 percent lower than in the same period in 2019, while catches of cod were more or less level with the previous year.

The medium term³ OECD-FAO Agricultural Outlook 2020-2029 forecasts a general trend towards rising fish prices despite the immediate adverse impacts of the COVID-19 crisis.

³ OECD-FAO Agricultural Outlook 2020-2029, July 2020, https://stats.oecd.org/viewhtml.aspx?datasetcode=HIGH_AGLINK_2020&lang=en

Figure 1.3 Catches by Greenlandic fishers and vessels in Greenland's waters, 2012-2019



Note: The mackerel catches include the share of mackerel fished in ICES (International Council for the Exploration of the Sea) ecoregions/advisory areas.

Source: Statistics Greenland.

1.2. Tourism

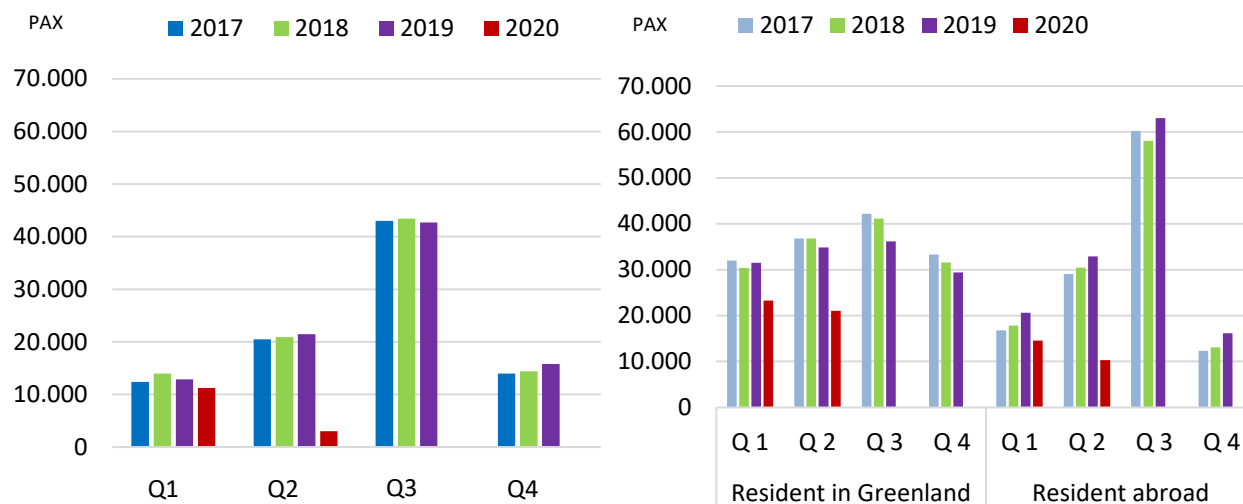
Greenland's tourism sector was also buoyant until 2020, with an upturn in tourism in the period 2015-2017 following several years of stagnation or downturn. This trend was interrupted in 2018, but then resumed in 2019 when the number of bednights spent by overseas guests in Greenland increased by 4 percent relative to the previous year; see Figure 1.4. For several years, the number of air passengers on international flights has remained fairly constant at around 80,000 PAX, rising to just under 90,000 in 2017, but increasing to almost 93,000 in 2018 and 2019.

Given its heavy reliance on overseas visitors, Greenland's tourism industry is particularly hard hit by the COVID-19 crisis. The number of air passengers on international flights fell by 86 percent in Q2 2020 relative to the same period in the previous year, and the number of bednights in Q2 2020 was 69 percent below the 2019 level. Most of the tourism season revenue based on overseas visitors this year must consequently be regarded as lost.

Besides the general financial support packages introduced in March 2020, two new packages introduced in June 2020 were targeted at businesses within the tourism sector, and were intended to boost activity in the sector. 'Activity package for the tourism industry' offers two components: 1) discount schemes to boost domestic tourism and 2) discount schemes for tour operators. The second financial support package, the 'Mobility Scheme' enables scheduled route operators to offer a discount on domestic fares within Greenland between towns and outlying settlements.

The financial support packages have helped prevent the tourism industry collapsing in parts of the country, especially in South Greenland. However, a new surge of COVID-19 infection in many countries has increased the uncertainty surrounding the tourism outlook. The International Air Transport Association (IATA) predicts that air travel and hence a very large share of tourist traffic will not return to pre-COVID-19 levels until 2024. It is to be expected that the same uncertainty is likely to impact tourism in Greenland also.

Figure 1.4 Air passengers and hotel bednights 2016-Q2 2020



The Government of Greenland's goal of boosting the tourism industry was demonstrated, for example, in the spring 2016 national sector plan for tourism, and the creation of what was originally a Greenland Government wholly-owned company, Kalaallit Airports A/S, to build, own and operate new or expanded airports in Qaqortoq, Nuuk and Ilulissat. The two international airports at Nuuk and Ilulissat have since then been hived off into Kalaallit Airports International A/S, in which the Danish Government now holds a one-third share and the Government of Greenland a two-thirds share. Increased uncertainty surrounding the tourism industry is also likely to affect the plans to build additional hotel capacity to serve the airport projects.

1.3. Extractive Industries

Developing extractive industries (raw materials, minerals, oil etc.) is still on the backburner in Greenland. Following the closure of the gold mine in South Greenland in 2013, no raw materials were mined in Greenland for some years until LNS Greenland Gems started mining ruby near the Qeqertarsuaat settlement in the summer of 2017. To date, this project, with around 30 employees, has only resulted in modest exports of untreated ruby. Hudson Greenland's anorthosite project at the Kangerlussuaq fjord employs more or less the same number of workers in the mining phase as the ruby project. The mine opened in September 2019, but production has since been suspended and is not expected to resume until refinancing has been secured.

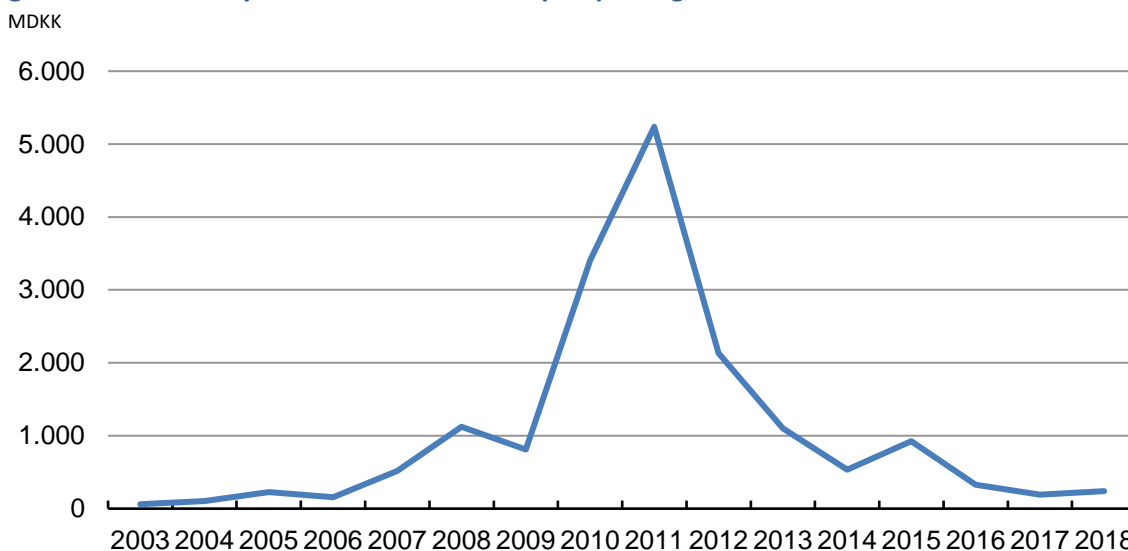
In August 2020, Tanbreez Mining Greenland was granted an extraction licence for mining rare minerals at Killavaat Alannguat in South Greenland. The construction phase is expected to take 2-3 years, and will provide around 80 local jobs during the production phase. Plans are now well-advanced for mining ilmenite at the abandoned settlement of Moriusaq, close to Thule Air Base under the Dundas Ilmenite Titanium Project run by a subsidiary of Blue Jay Titanium Mining Company. The company has filed an application for an extraction licence which will be undergoing public hearing until September 2020. This project is expected to employ 60-100 workers in its operational phase.

A mining permit was granted for zinc and lead at Citron fjorden in Northern Greenland in 2016. At the beginning of 2020, the company notified that it was working to raise the capital needed for the project. In its operations phase, this project will employ almost 500 workers, of which only a few are expected to come from Greenland. The mine will be very remote from any populated area in Greenland.

The Government of Greenland's aim to make Greenland more attractive for hydrocarbon extraction was implemented in a new strategy for the oil/gas sector for the period 2020-2024, approved by the Government of Greenland in January 2020. At the present time, an exploration company has applied for approval of up to 4 exploratory drillings on Jameson Land in East Greenland. If a permit for this is granted, this will be the first time since the Cairn Energy drilling programme in 2010/11 that a full drilling programme is carried out.

Exploration costs covered in Greenland have been decreasing since 2010/11 with slight variation; see Figure 1.5. The figure shows that Cairn Energy's drilling programme generated investments worth DKK 5bn in 2010/2011.

Figure 1.5. Costs of hydrocarbon and mineral prospecting, 2003-2018



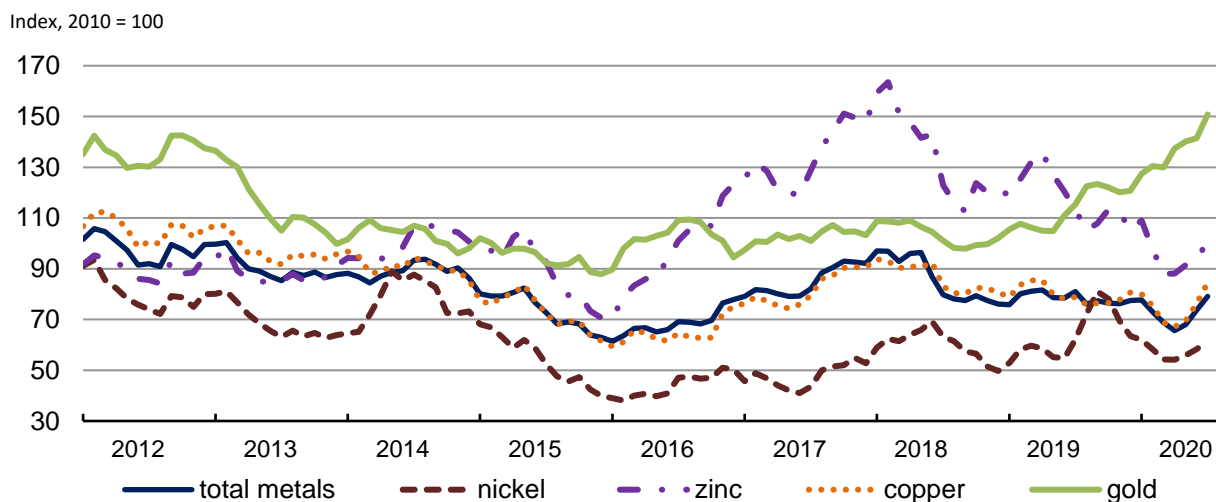
Note: The figures for 2004-2016 are final, whilst those for 2017-2018 are preliminary.

Source: Statistics Greenland.

The price indices for a number of raw materials fell in late 2019 and in early 2020. In Q2 2020, however, the prices showed a transient slight increase; see Figure 1.6. In its annual *Commodity Markets Outlook* from April 2020, the World Bank highlights the uniquely high uncertainty surrounding both demand and the price trend in the mineral commodities market in the wake of the global economic shock from the pandemic. The uncertainty solely concerns the scale of the negative impact on the commodities markets. More specifically, the World Bank estimates that the oil price will be just over 40 percent lower in 2020 than in 2019, while metals and minerals prices will average 13 percent lower. The forecast is for only partial recovery of the market prices in 2021, the exception being the price of gold which increases in times of crisis.

The prices on raw materials may dampen new investments in exploration and mining activities. Another limiting factor may be the extraction companies' perception of the regulatory conditions governing mining. A global survey of perceptions is available in, the private Canadian think-tank, Fraser Institute's annual survey of the attractiveness for companies to mine in different jurisdictions. This is a questionnaire-based survey conducted among industry respondents, so a reservation should be made due to the fact that only a limited number of companies were surveyed. However, it is still cause for concern that Greenland fell from its top-quarter ranking in 2014 in the companies' perception of the attractiveness of the different jurisdictions' mining policies (Fraser Institute's *Policy Perception Index*) to a ranking among the least attractive half in 2019.

Figure 1.6 World Bank metal prices index, 2012-2020



Note: Price index in USD. The latest observation was in July 2020.
 Source: World Bank Commodity Markets Outlook.

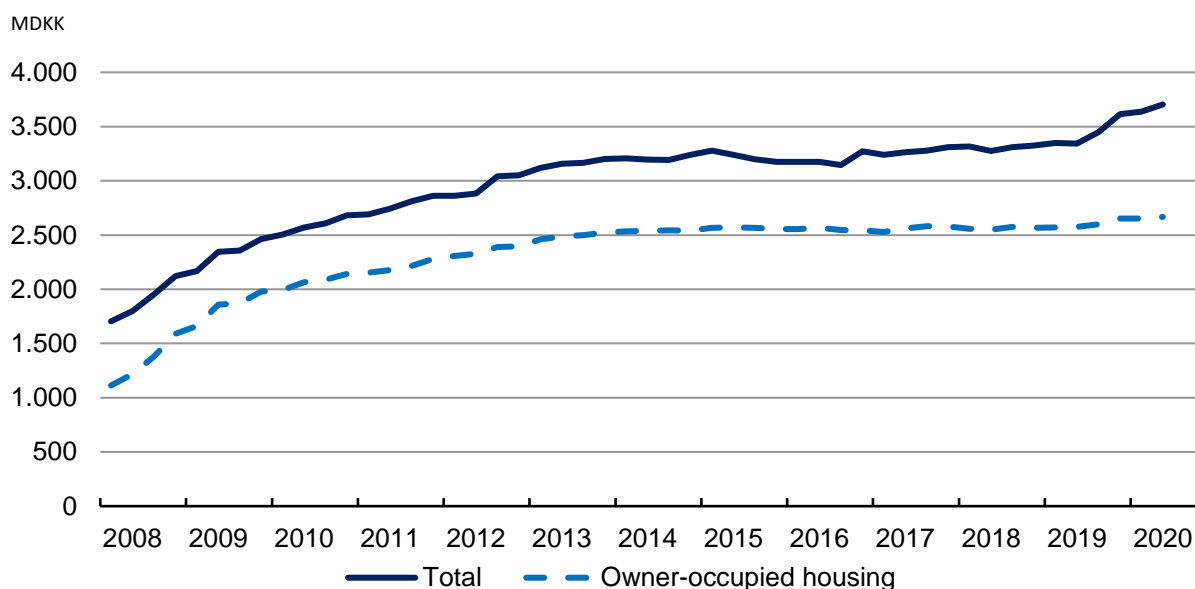
1.4. Investment

In the past, the Government of Greenland' capital expenditures by drawing on the Construction and Renovation Fund financed a large proportion of Greenland's building and construction investments. As other investors have surfaced, the Government of Greenland have increasingly invested through companies, and the significance of withdrawals from the Construction and Renovation Fund has lessened for investments as a whole. In 2018, withdrawals from the Fund accounted for only some 18 percent of total building and construction investment in the National Accounts, as against almost 40 percent in 2011 and 2012. Going forward, there is no prospect of the withdrawals from the Construction and Renovation Fund financing a substantial share of the aggregate investment, since the budget proposal provides for deferral of construction activities via reversal of funds from that Fund; see Chapter 2.

Potential developers are reporting problems getting projects started, and there are several indications that capacity utilisation in the building and construction sector is already high. The initiation of large-scale projects is thus currently at risk of rapidly causing bottlenecks, resulting in rising costs and deferral of other activities.

Based on mortgage credit institution lending in Greenland, the level of activity in construction of owner-occupier homes in recent years is deemed to be very modest; see Figure 1.7. Total lending for owner-occupied homes has been fairly constant, with the level of new mortgage loans equating to redemption of old ones, as the losses made on these are negligible.

Figure 1.7. Mortgage credit institution lending to Greenland, 2008-2020



Note: The latest observation was in Q2 2020.
Source: Statistics Greenland.

The buoyancy of the fishery sector has resulted in increased investment in all vessel types and in equipment. Over the course of 2019, several owners are expected to introduce newly-built trawlers in the offshore fishery. This presents an opportunity to rationalise the industry, thus helping to boost profitability in the future. A number of the vessels were built in Spain and investments in these vessels increased the total value of imports by approximately DKK 1.6 billion in 2019.

The period 2019-2024 will see the new international airports built in Ilulissat and Nuuk. While construction of the airports is in progress, in the region of DKK 700m will be invested annually. While labour for carrying out the airport projects is largely expected to be sourced from outside Greenland, the project will likely result in secondary effects in the form of support industries.

Construction of the airports at Nuuk and Ilulissat is under way. The original plan was for both airports to be commissioned in 2023, but adverse weather and the COVID-19 pandemic have so far delayed the project by up to 12 months. Efforts will initially be concentrated on the Nuuk site, where relocation of the workforce and equipment from Nuuk to Ilulissat is not expected to go ahead until 2022. The airport in Qaqortoq will likewise be delayed, as Kalaallit Airports has not yet succeeded in negotiating a public procurement within its financial constraints. Efforts are currently focused on a round of tenders next year for finalisation in 2024.

The total financing plan for the airports amounts to DKK 3.7bn. In its 2019 annual report, Kalaallit Airports stated that the 2020 investment budget was projected to amount to DKK 700m, but among the various effects of the delays, construction of the buildings in Nuuk cannot go ahead as originally scheduled, and the investment budget for 2020 must thus be expected to be lower than planned.

1.5. Consumption

Household final consumption expenditure is rising. Private spending can to some extent be illustrated by retail sales figures for the three largest retail chains; see Figure 1.8. Retail sales in 2019 were 4.3 percent higher than in 2018. In the same period, the consumer price index increased by 2.4 percent, and the volume increase is thus just under 2 percent. The growth in retail sales continued in Q2 2020 after stagnating in Q1 2020. Since a very large proportion of consumer goods are imported, fluctuations in private consumption have less impact on the economy than in the majority of other countries, while investment and exports have greater influence on economic fluctuations.

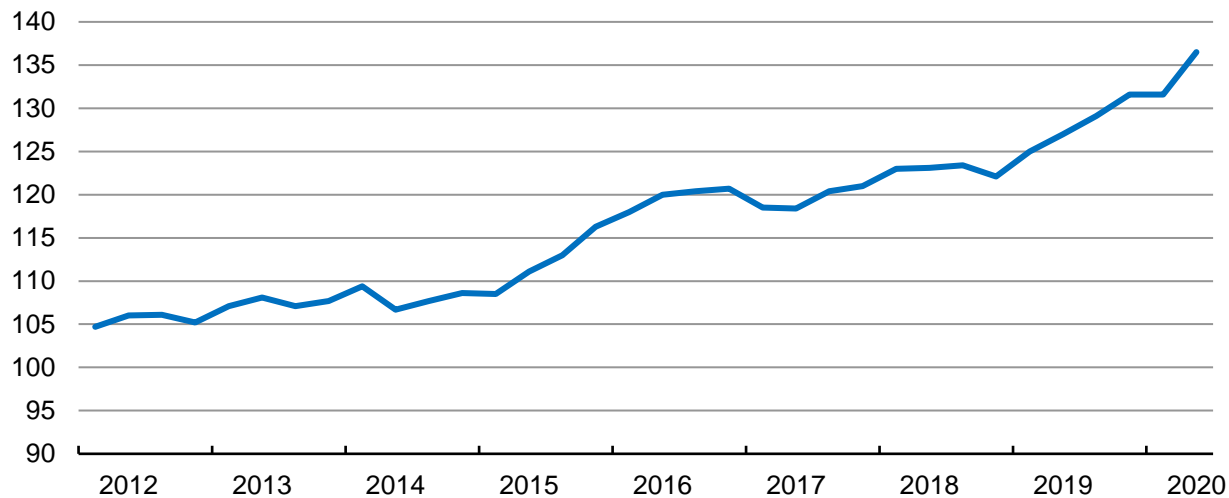
The value of imported motor vehicles and privately owned boats has risen steeply in recent years; see Figure 1.9. In 2019, vehicle imports were down, while imports for privately owned boats rose. This is yet another indicator of strong increases in consumption and disposable income.

As mentioned earlier under Section 1.2, June 2020 saw the introduction of two new financial support packages enabling tourism operators to offer discounts on accommodation, excursions and domestic travel fares within Greenland. These measures are likely to generate further increases in consumption in Q3 2020.

Finally, recent years have brought stagnation in bank lending to households; see Figure 1.10. In Q2 2020, lending to households was approx. 1 percent lower than in the preceding year. This is a sure sign that the growing consumption is generally not loan-financed.

Figure 1.8 Retail sales, seasonally adjusted, 2010-2020

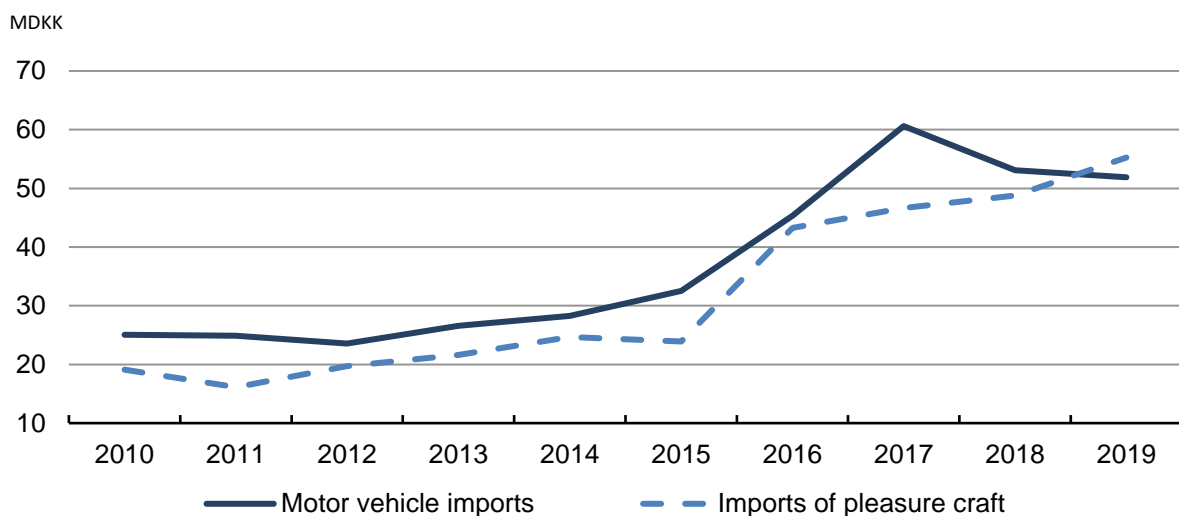
Index, 2010 = 100



Note: The last observation was made in Q2 2020.

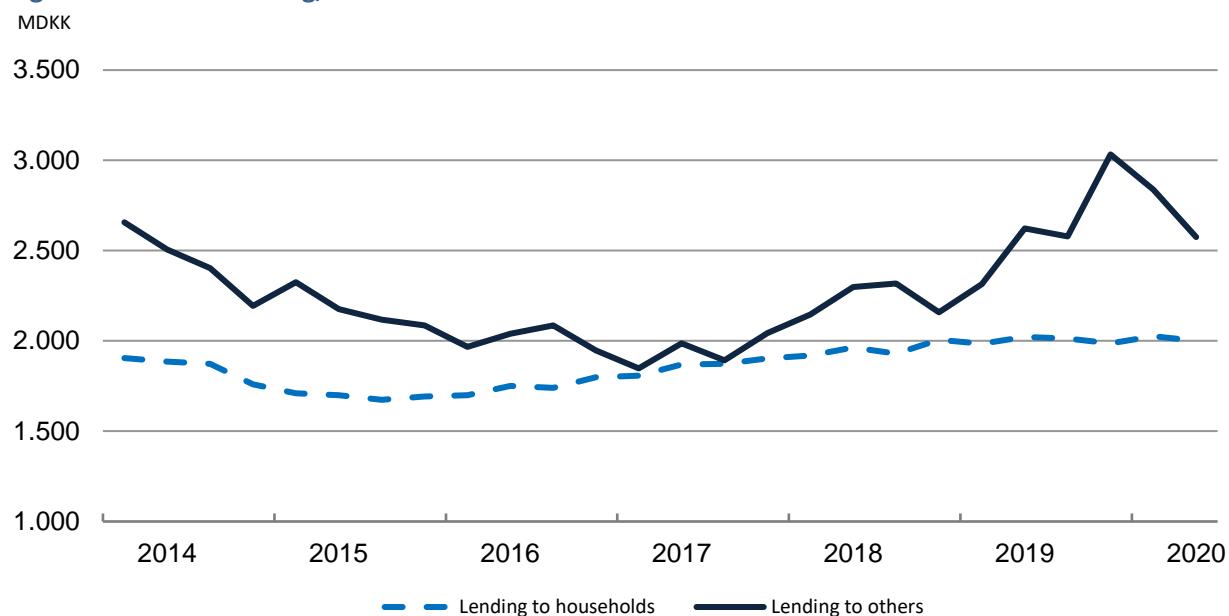
Source: Statistics Greenland.

Figure 1.9 Imports of motor vehicles and pleasure craft, 2010-2019



Source: Statistics Greenland.

Figure 1.10. Bank lending, 2014-2020



Note: The last observation was made in Q2 2020.

Source: Statistics Greenland.

1.6. The activity trend and employment

In the face of the global COVID-19 crisis, the outlook is virtually zero economic growth in 2020. Table 1.2 presents the key figures in the forecast. The trend for the individual demand components, i.e. private consumption, investment, exports and imports, is subject to great uncertainty. The substantial decline in exports is strongly linked to the decline in hotel and tourism activity, since far fewer foreigners will be visiting Greenland this year. Added to this is a moderate volume adjustment in the fishery sector, which also adversely impacts exports. Consumption appears to be sufficient to sustain the 2019 level in spite of a period of lockdowns and changes in consumption behaviours. This is one of the main reasons why the impacts of the COVID-19 crisis may be less severe than previously forecasted. Investments are relatively unchanged and high, supported by the building and construction investments in the new airports, and construction activity in Nuuk.

The growth outlook this year is more uncertain than usual. The severity and duration of the downturn is as yet unknown, and much may change over the autumn and winter. If domestic demand is unexpectedly favourable, the growth in Greenlandic production may be slightly higher than projected by this forecast. Conversely, however, the possibility still exists of a substantial fall in production if households curb their spending and businesses their investment plans.

Zero growth in 2020 means that Greenland, unlike many other countries, will not be plunged into full recession in the wake of the global pandemic. However, status quo in the level of activity from 2019 to 2020 must also take into account the projection in autumn 2019 for 3.8 percent growth in activity in 2020. In this way, Greenland's economy will suffer from the COVID-19 crisis, but not as severely as to mean a recession proper.

Growth in 2021 is to some extent characterised by recovery, in which an expected gradual normalisation in tourism, hotel and services might boost foreign consumption in Greenland (classified as exports in the National Accounts) and private consumption. Overall, growth could potentially reach 2 percent next year. The substantial international downturn, however, means that activity at year-end 2021 will be lower than anticipated before COVID-19 crisis.

Table 1.2 Supply balance, annual real growth in percent.

	Share of GDP in 2018	2013	2014	2015	2016	2017	2018	Forecast		
		2019	2020	2021						
Private spending	36.2	-1.1	0.7	0.2	1.5	1.3	1.1	2.7	0.7	3.4
Public spending	44.1	4.1	-0.2	-0.6	1.8	2.3	1.8	0.7	0.4	0.7
Gross investment	23.8	-20.7	-21.9	10.2	10.9	-0.7	12.3	31.9	-1.6	-0.1
Exports of goods and services	40.8	2.4	11.8	-9.9	15.2	-5.4	4.2	4.8	-5.0	1.0
Total final consumption	145.0	-3.9	-1.7	-0.6	5.9	-1.0	4.0	8.0	-1.3	1.3
Imports of goods and services	45.0	-6.6	-11.5	1.7	11.0	-3.1	5.7	20.4	-3.0	-0.1
Gross domestic product	100.0	-1.3	4.7	-2.5	4.7	0.5	3.2	1.3	-0.2	2.1

Note: 2015–2016 are final figures; 2017–18 are provisional figures; 2019–21 are Economic Council estimates.

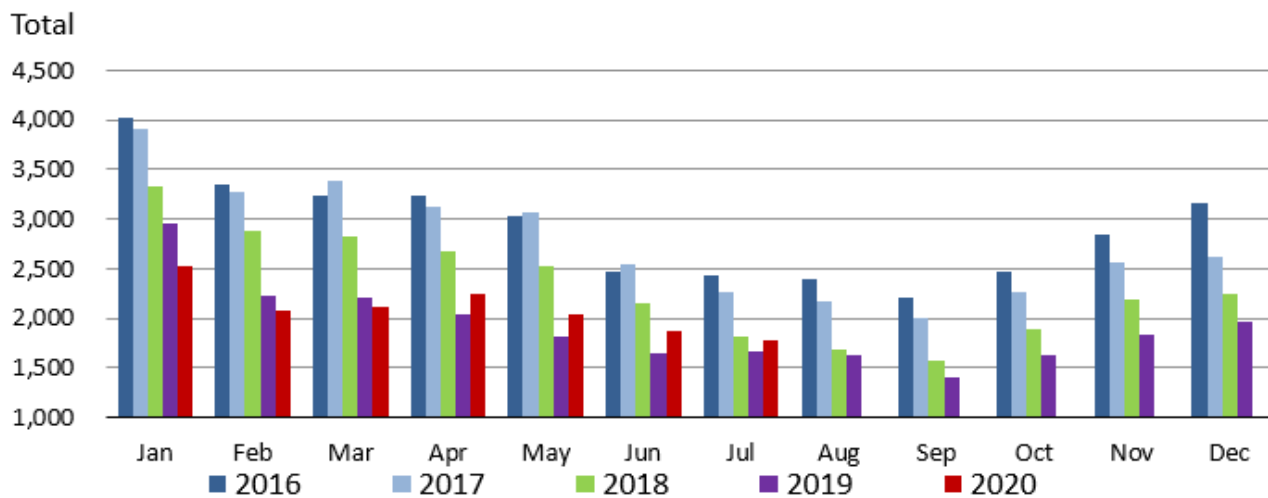
Source: Statistics Greenland and own calculations.

Zero growth this year will mean a fall in the employment rate. However, at baseline, pre-pandemic, there were widespread labour shortages and correspondingly high demand for foreign labour. An economic slowdown will reduce this demand, and the increase in the unemployment rate this year may consequently be limited. The financial support packages for industry and the labour market are also helping to minimise the impact of the COVID-19 crisis on the labour market.

Current labour market assessments are necessarily based on the number of registered job-seekers. This number has fallen steeply since 2016, *see Figure 1.11*. The decrease in the unemployment rate is most noticeable in cities and particularly affects those ready to take up employment. In July 2020, 1,777 individuals were registered as seeking employment, which is an increase of 117 job-seekers relative to the same month in the previous year. Persons furloughed with pay compensation for private-sector businesses are not registered as unemployed. The statistics show the total number of individuals who contacted their local authority in any single month because of unemployment. The statistics are therefore influenced by the administrative practice of each local authority and fluctuations in any one month should be interpreted with caution. So far, the figures do not, however, indicate any significant impact from the COVID-19 crisis on the labour market.

Statistics Greenland publishes annual registry-based statistics of unemployment amongst 18-64 year-olds ordinarily resident in Greenland. This data is the closest Greenland comes to anything comparable with other countries' unemployment statistics. The statistics do not include anyone who has been in paid employment and registered as a job-seeker in the same month. The number of unemployed persons in 2018 was 1,582, corresponding to an unemployment rate of 5.8 percent of the workforce, compared to 6.8 percent in 2017, and 7.3 percent back in 2016.

Figure 1.11 Registered job-seekers, 2016-2020

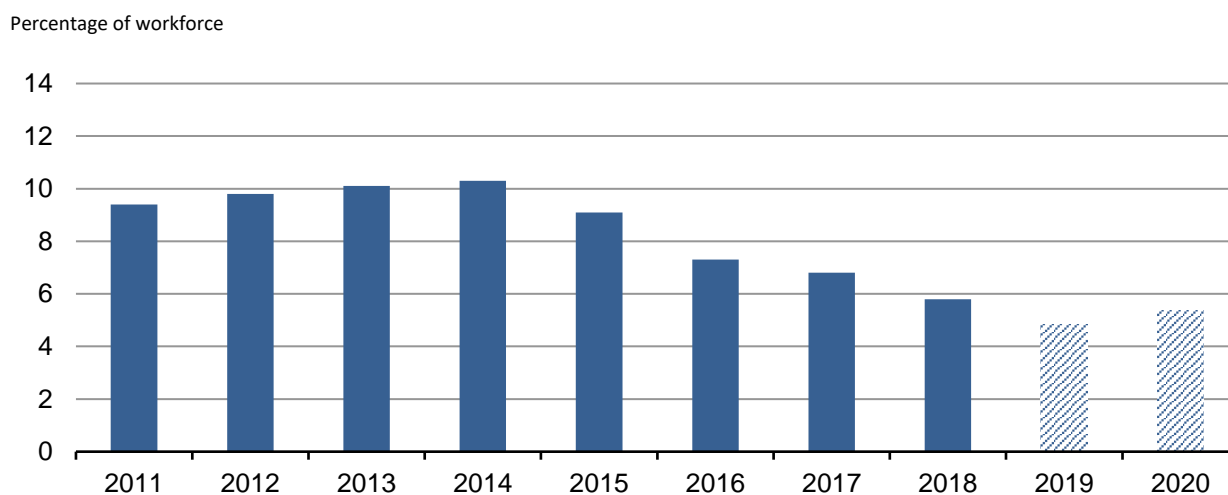


Note: The last observation was made in July 2020.

Source: Statistics Greenland.

The number of registered job-seekers has followed the average unemployment trend in the registry-based statistics very closely in recent years, as the monthly average for registered job-seekers has been 900-1,000 individuals higher than the average unemployment rate per month according to the unemployment statistics for all years from 2012 to 2018. If the workforce is assumed to be more or less unchanged, a mechanical projection puts the unemployment rate at 4.8 percent in 2019 and at 5.4 percent in 2020; see Figure 1.12.

Figure 1.12 Unemployment among permanently resident 18-65-year-olds, 2010-2020



Note: Figures for 2010-2018 are from Statistics Greenland, whilst those for 2019-2020 are the Economic Council's estimates.

Source: Statistics Greenland and own estimates.

In sum, the statistics and indicators show that employment has been rising and unemployment falling since 2014. This trend was temporarily halted in 2020, but the downturn in the labour market is significantly lesser than in other countries. Given the prospects of a bounce-back in 2021, pressure on the labour market could soon re-arise, and thereby also the need to increase the workforce or recruit more foreign labour.

The principal challenges facing Greenland's labour market are still primarily structural in nature. Unemployment is particularly high among individuals with no tertiary education. The registry tallies for 2017 show that unemployment in this group was 11.0 percent compared to 3.2 percent for those with a vocational qualification, and 0.5 percent for persons with higher education. It is also more difficult to reduce unemployment among those with no tertiary education.

Chapter 2 Current economic policies

In a short space of time, the COVID-19 crisis has substantially changed the conditions of economic policy. As infection spread and lockdowns were imposed in other countries, it also became necessary to impose a number of restrictions and suspend certain activities entirely or partially in Greenland. Meanwhile, financial support packages were introduced to mitigate the economic consequences of lockdowns for companies and wage-earners.

The epidemic in Greenland has been contained, although there is continuous risk of exposure to infection from outside Greenland, and the majority of lockdown regulations have now been revoked. However, great uncertainty persists concerning the pandemic and the risk of new infection, which might necessitate new regulations. In spite of the partial reopening of the economy, certain economic impacts will persist well into the future, and depend on both health and economic developments globally. The economic consequences derive from falling consumption and investments in a large number of countries simultaneously. Concerns about the risk of infection, lockdowns, quarantining, etc. may cause consumers to limit their spending. This in turn impacts general demand and halts corporate investment plans. Since this trend is present simultaneously in many countries, the impacts on the global economy may be vast, see Chapter 1, and may have substantial negative impact on specific sectors such as transport and tourism.

This trend influences Greenland's economic policy firstly via the direct economic consequences of the COVID-19 crisis as a result of financial support packages, etc. and secondly in that it reduces the capacity to achieve trade and industry diversification. Transport, tourism and mining may be significantly affected with the entailed adverse impacts on the capacity to grow these sectors. These challenges compound the already well-established challenges surrounding education and societal factors and a solution to the sustainability problem of public finances owing to the advancing age of the population of Greenland. The disruption caused by COVID-19 has thus in a number of areas stepped up the economic policy requirements.

2.1. Trends in Greenland's public finances

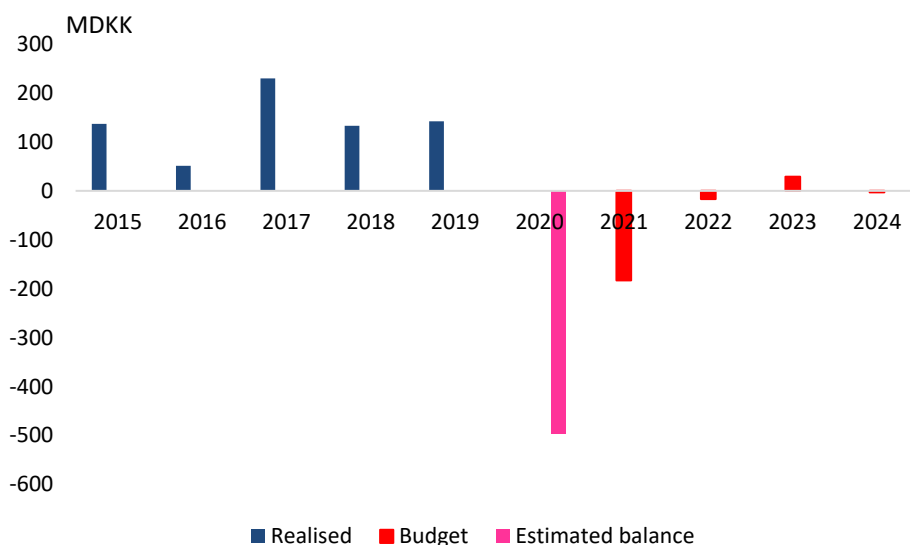
The reversal in economic trends affects the Treasury. Greenland now has rising expenditures on items such as financial support packages and health care. Economic decline and rising unemployment will also increase welfare benefit expenditures. However, savings may be obtained in other areas due to lower activity. On the revenue side, a fall in taxes and duties is to be expected, including a fall in the resource rent tax; see the discussion in Chapter 1. Public revenue is however safeguarded by the fact that the block grant from the Danish Government and EU subsidies are not affected by global economic trends.

In the years 2015-2019, the Treasury reported a surplus; see Figure 2.1. In 2019, the surplus was larger than projected owing to the buoyant economic cycle. Now, however, the COVID-19 crisis is causing a sharp reversal in Greenland's public finances. At the present time, estimates of the effects of the pandemic on the 2020 public finances are subject to significant uncertainty. However, a provisional and uncertain estimate indicates that the surplus for 2020 may be in the region of DKK 500m, but that direct expenditures incurred from the health service, financial support packages and emergency flights as a result of the COVID-19 crisis are estimated to total around DKK 265m. The emergency flights alone account for approx. 75 percent of that total expenditure. At the same time, there will be a fall in tax, duty and excise revenue, Greenland Airports revenues and dividends of some DKK 330m, with the fall in resource rent tax revenue accounting for around DKK 125m. These figures are subject to significant uncertainty at the present time, but the Treasury will inevitably be very severely impaired.

The 2020 budget proposal anticipates a fiscal deficit for 2021 and subsequent austerity measures. The years 2021-2024 are forecasted to result in a deficit of DKK 175m, but with fiscal balance achieved over the period 2022-2024 as a whole. In order to realise this, the budget proposal includes cutbacks and efficiency improvements in the public sector.

It is as yet unclear how the COVID-19 crisis is impacting municipal finances. The municipal tax revenues do not appear to be adversely affected to any great extent, which reflects that the crisis has not proved as severe as originally assumed. As the crisis will continue to have impacts beyond 2020, municipal finances may yet be challenged.

Figure 2.1. Greenland’s Treasury - CI balance, 2015-2024



Note: Positive figures indicate a surplus. 2020 is an estimate, 2021-2024 are budget years.
Source: 2021 Budget proposal.

The COVID-19 crisis adversely affects the Treasury. Although the budget proposal does not meet the requirement for public finances to either balance or show a surplus, there are good arguments for derogating from this principle in a crisis situation. This makes it possible to support Greenland's economy and operate with a less stringent fiscal policy. This makes the effects of the crisis less severe than would have been the case if expenditures and revenues had to be adjusted in order to balance the budget. The capacity for pursuing this less austere policy has been achieved by pursuing a responsible budgetary policy over a number of years and thereby avoiding the accumulation of debt. However, during the buoyant, pre-pandemic years, no substantial buffers were amassed, which is why the COVID-19 crisis has major implications for Greenland's economic policy.

It will be crucial to establish a plan for restoring balance to the public finances, and to avoid accumulating any sizeable debt. As stated, the budget proposal contains a plan for achieving budgetary balance over the years 2022-24. Given that the severity and duration of the crisis are not yet known, the fiscal adjustments needed may be more substantial than assumed for the purposes of the budget proposal.

The Government of Greenland also have substantial risk exposure through the government-owned companies, which must necessarily be factored into assessment of the freedom of scope for Greenland's economic policy. A negative financial trend in one or more of these companies could have severe implications for the Treasury. The total net interest-bearing debt – which includes debt in the companies held by the Government of Greenland – is projected to increase from DKK 3.6bn in 2020 to DKK 4.2bn in 2023.

The Finance Act holds a number of added expenditures on reform initiatives, including the introduction of the employment allowance and a reduction in the corporate tax rate from 30 to 25 percent. The bill also provides for economies as a result of, for example, the roll-out of the Ilangaassivik payment system. Furthermore, the budget proposal contains no price and wage adjustments to operating expenditure and subsidisation appropriations, which thus corresponds to an annual budgetary economy of approximately DKK 75m. Achieving this without detriment to the quality or scope of public-sector service provision will pose a major challenge. Equally, there is no scope for new cost-intensive initiatives or bills. The budget proposal makes no provision for any financial support packages targeted at businesses/employment.

Finally, the budget proposal also provides for deferral of construction activities via reversal of funds from the Construction and Renovation Fund and a reduced capital investment budget. Although these measures relieve the public finances in the short term, in effect, they amount to indirect borrowing, since the maintenance backlog for public sector housing and ports, etc. will only increase and hence reduce the value of Greenland's future capital stock. New initiatives such as hydropower plants (enlargement of Buksefjord hydroelectric power plant and construction of a plant at Qasigiannnguit) will be deferred. The COVID-19 crisis also has implications for the airport projects and the expenditure and revenue estimates on which these projects were originally based, may need to be revised in a negative direction. The project at Qaqortoq has proved impossible to realise within the original budget, and has therefore been deferred.

The liquidity of the Treasury is a concern in its own right. Given the great uncertainty surrounding the scale of the crisis, the liquidity draw has consequently been subject to great uncertainty. As the crisis has so far been less severe than originally feared, the liquidity draw has also been lower. The minimum liquidity requirement has not been challenged. Going forward, however, there will be a need to ensure the option of taking up loans to cover both the anticipated deficit and delays with implications for Greenland's liquidity. The budget proposal asserts that a credit facility of DKK 1bn would provide adequate security. The budget proposal also proposes authorisation for borrowing up to DKK 1.5bn. Ensuring access to a loan facility is important in ensuring that the Treasury avoids liquidity problems, which would reinforce the effects of the crisis.

2.2. The COVID-19 crisis and financial support packages

In response to the COVID-19 crisis, financial support packages have been introduced for businesses and employees. The objective of these measures was to support companies and employees in situations where the economic possibilities were impacted by the lockdowns imposed to limit the risk of spreading infection. Similar measures were introduced in many other countries.

The financial support packages for businesses include an 'emergency package' for private businesses within the hotels and restaurants sector and certain service industries and a 'general industry package' for businesses in other sectors including the fisheries sector, the construction sector and the transport sector, etc.

Businesses whose revenue has dropped by at least 30 percent are eligible for compensation for direct cancellations or for fixed overheads (overall maximum of DKK 1m per company per month). Originally, DKK 50m was earmarked for the emergency package and DKK 100m for the general industry package.

A loan option has also been set up for private companies. The Danish Government has proposed that small and medium-sized enterprises (SMEs) in Greenland be covered by Denmark's SME guarantee scheme, in the same way that Greenland is covered by the Danish Government's financial support package for large corporates. Under this measure, the Danish Government has established a guarantee scheme to cover 70 percent of bank loans to companies that can document loss of turnover in excess of 50 percent as a result of COVID-19. Deadlines for payment of taxes and duties, etc. have also been extended to improve corporate liquidity.

The *labour market package* comprises relief to support workers. When companies furlough permanent employees, they can receive compensation for wages. To be eligible, at least 30 percent of the applicant's employees or 25 employees must have been furloughed during the period of wage compensation. Compensation for 90 percent of the salary can be paid, up to a maximum of DKK 20,190 per 30-day wage compensation period per employee. The employee must take five days of annual leave/time off in lieu for each 30-day wage compensation period. DKK 107m has been set aside for this scheme.

Total uptake of the financial support packages (including loan facilities) amounted in mid-August to just over DKK 43m, of which half was granted to the tourism industry. By the end of July 2020, the financial support disbursed totalled just over DKK 7m for the wage compensation scheme, and loans worth approx. DKK 7m. Uptake of the schemes has been lower than expected, which reflects a smaller need than originally assumed. The subsidies have notably been granted to hotel and restaurant businesses, the transport sector, retailers, service providers (including travel agents, tour operators and other tourism enterprises) together with cultural, entertainment and sports enterprises.

The schemes originally covered the period 1 March 2020 to 30 June 2020, but were subsequently extended through to 30 September 2020; thereby extending the financial support period from 3 to 7 months. Meanwhile, compensation for overheads has switched to a linear model so that compensation is granted for estimated loss of turnover subject to an upper compensation limit. If a company's revenue has declined by 50 percent, the compensation covers 50 percent of overheads, and the compensation cannot exceed 80 percent. The transition to the linear model is an obvious improvement, as it provides a better incentive structure.

In addition, 'activity packages' have been introduced for the tourism industry to boost domestic tourism in a situation affected by travel restrictions and fewer overseas tourists, but also limited options for residents of Greenland to holiday abroad (staycation). This scheme contains discounts on accommodation and tourist excursions. The COVID-19 discount for overnight stays is reimbursable by up to DKK 500. The COVID-19 discount for tourist excursions is reimbursed by up to DKK 300; see also the discussion in Chapter 1.

As in the case of the financial support packages, businesses in especially hard-hit sectors have been granted deferred due dates for paying withheld PAYE (tax deducted from income at source) and labour market contributions for April, May, June and July. The payments are deferred by three months to July, August, September and October, respectively. Public-sector companies with activities in these sectors can apply for deferral of these payments. It is possible that the scheme could be extended to other industries.

Deferring tax and duties is the equivalent of a loan, and is a useful way of ensuring better liquidity for the relevant companies. However, the payment deferrals are relatively limited, and some companies can be expected to have difficulty making these payments in the latter part of the year alongside their normal taxes. It may be necessary to spread the payments over a longer period. In general, loans are preferable to direct support, since they do not distort the market mechanism to the same extent. The disadvantage of deferring tax and duties generally is that this occurs without credit-rating. This means there is also a risk of building up a tax debt which some companies would be unable to pay. The more wide-ranging the scheme is, the greater the problems that can arise from it. Guarantee schemes, e.g. for SMEs guaranteeing up to 70 percent of the loan amount, do not have this problem to the same extent, since a credit-rating is performed (by other lenders bearing 30 percent of the loan risk).

A preliminary analysis indicates that deferral of taxes for February until the end of June accounted for (post-application) just over DKK 20m, of which DKK 1.2m was still outstanding by the end of July.

The financial support packages have become necessary in the extraordinary situation that arose as a result of the lockdown restrictions. However, this is a very unusual type of economic policy, and there are problems associated with giving businesses support to cover overheads and support when employees are furloughed. Essentially, it puts the vital part of the market mechanism out of action.

The criteria for support are based either on a reduction in revenue or on furloughing of employees, and thus on a comparison between the situation now and before the start of the crisis. The longer the duration, the more problematic this balance becomes, since it has a tendency to 'freeze' a past situation. The economy, however, is in a continual flux of transitions and adjustments, and this dynamism is likely to become static if the financial support packages are maintained for an extended period. The Government of Greenland are not in a position to support businesses permanently, and an extended support period poses the risk that resources will be tied up in unprofitable business activities, thereby reducing the adaptability of the economy.

Conversely, certain longer term interventions are needed for the tourism sector due to its unique operating conditions and to prevent it from being plunged into a long-term crisis. These measures should be aimed at individual businesses to ensure that the requisite capacity and infrastructure are maintained, and the measures should be temporary with a fixed end date and a patent incentive for companies to develop new business areas.

It is important that the financial support packages are aimed only at those businesses whose operating conditions have been directly curtailed by COVID-19 regulations. A number of other industries may suffer under the general stagnation ensuing from the COVID-19 crisis. This applies to some extent to the fishery sector. However, these are secondary impacts that are not directly attributable to Greenlandic regulations, and are caused by changes in the global economic trend. These fluctuations are no different in nature or scope from the effects of conventional cyclical trends, and thus constitute ordinary commercial risks. It would set a major and problematical precedent if such fluctuations were to be remedied by financial support packages. It would as a minimum also entail that the affected industries would have to contribute more to the Treasury in good times. The situation in the fishery sector, however, underlines the problems that follows by permitting an excess influx into the industry in buoyant periods. This creates a situation in which a large portion of the population becomes dependent on income from the fishery sector, thereby creating a basis for political pressure for support in any downturn. If fishing is permitted above the sustainable level over the short term, it has another adverse impact on the economic sustainability of locking resources within the industry, and political pressure for support, thereby placing strain on the public finances.

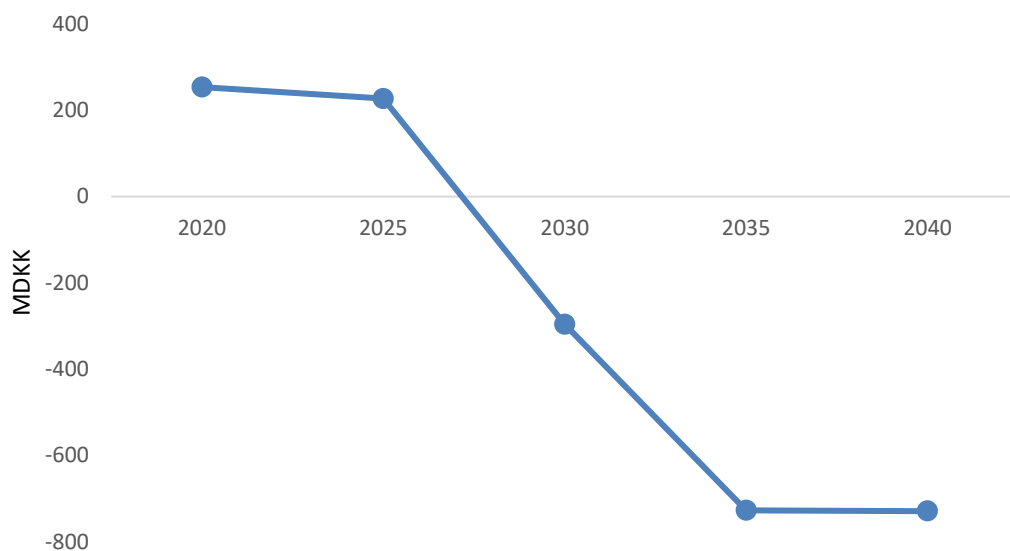
The financial support packages are an extraordinary economic policy instrument that is not normally used to support economic activity. They should therefore be phased out as quickly as possible, and any need to support activity must be effected via conventional fiscal policy instruments and labour market policies.

2.3. The advancing age of the population is driving up public spending

Public revenue was significantly strengthened during the economic upturn, which resulted in a fiscal surplus in recent years. Revenue will naturally also increase and decrease in response to the economic cycle going forward. Expenditure, however, will almost certainly trend in only one direction; meaning upwards, with the advancing age of the population. The number of elderly persons is set to increase, also relative to the population of working age, and this will radically increase public expenditure. The Economic Council's analyses of this trend indicate that the ageing population will increase public expenditure by between 5 and 6 percentage points of Gross Domestic Product. This means that public expenditure will exceed public revenue by around DKK 1bn by 2035. If Greenland's current economic policy remains unchanged, public expenditure will outstrip revenue and result in systematic fiscal deficits; see Figure 2.2.

This projection indicates the importance of fulfilling the reform requirements of the Sustainability and Growth Plan so that Greenland's public finances can be sustainably boosted by DKK 1bn by 2030. Accomplishing this is a question of making efficiency improvements in the public administration and of helping more citizens to progress from passive benefit to active self-sufficiency through labour market reforms. Every single public-sector employee that can be released into private-sector employment on the same pay will boost the public finances by an average of DKK 315,000. And each time citizens can be transitioned from receiving public benefits to becoming financially self-sufficient, with earned income corresponding to the union-determined minimum wage, the public finances will be boosted by just under DKK 120,000.

Figure 2.2. Projection of Greenland's public sector operating and capital balance, 2020-2040



Note: The figure shows public revenue and expenditure exclusive of interest and dividends projections for public services and public administration (the Government of Greenland, municipalities and Danish Government), presented in national accounts format; see Public Finances, Statistics Greenland. The balance has been adjusted for inflation. Positive figures are public surpluses and negative figures are deficits. Danish Government expenditure is offset by reimbursements (i.e. revenues) and thus does not affect the public balance.

Just how Greenland's economy is set to develop over the next decades will depend on many factors. More citizens gaining education and training, new infrastructure, new business opportunities and changes in the population composition are all factors that will influence Greenland's economic progress. The Economic Council and the Ministry of Finance in association with DREAM (Danish Institute for Economic Modelling and Forecasting) are devising a model for Greenland's long-term economic development and the public finances. This will be an important future-oriented reform tool for clarifying the impacts of educational policy, taxation policy, labour market and welfare policy, etc.

2.4 Economic policy requirements

Greenland's economic situation has changed radically as a result of the COVID-19 crisis. Both the short-term and longer-term requirements and needs impose tight constraints on the country's economic policy.

The crisis has spurred the need to restore the Treasury's finances. For a number of years to come this will require Greenland to achieve a fiscal surplus in order both to service debts and amass buffers to guard against any future crises. Meanwhile, there is a large unresolved sustainability problem linked to the public finances as a result of the advancing age of the population; see Section 2.3. The implications of the COVID-19 crisis compound this challenge, thus stepping up the requirements for controlling public finances. As discussed above, the challenge is in reality greater, since the maintenance backlog is not directly visible from the conventional analysis of public finances.

As such, the situation will require operating with a surplus for a period while carrying out reforms to resolve sustainability problems. For some years, Greenland's economic policy planning has been subject to the requirement for fiscal balance, which for the future needs to be replaced by a fiscal surplus. One milestone for addressing the sustainability problem has been the Sustainability and Growth Plan, but so far only a few of its initiatives have been implemented. Given the new situation, it is crucial to create a new, long-term plan, as soon as it becomes possible to get a perspective on the immediate impacts of the COVID-19 crisis.

The situation is worsened further by the setback to the strategy of developing a multi-faceted economy via tourism and extraction industries. The future of Greenland's tourism industry depends not only on travel restrictions but also on consumer reactions to the pandemic. Even if air travel restrictions were lifted, how tourism patterns would be affected is unclear. Among other things, tourism will depend on whether effective forms of treatment or a vaccine are found. Otherwise, the risk of infection and quarantine may suppress demand.

The extraction industries have also been directly impacted by Greenland's lockdown, as this has delayed exploration activities. There is also the impact of the global economic crisis on mineral prices, and a long-term global economic crisis could have major consequences for the capacity to develop the extraction industry. The crisis has thus increased the vulnerability of Greenland's economy, and so initiatives are necessary.

According to the budget proposal, the Government of Greenland will give special priority to reducing the number of young people in the youth target group (in neither employment nor education), general improvements in the education sector (including reduction in the drop-out rate, higher completion rates) and a more active labour market drive focusing on meeting demand for apprenticeships, creating increased mobility and more visible and explicit obligations for employment benefit recipients to be available for work.

These priorities are well-founded and will serve to create equal opportunities, reduce inequalities, improve public finances and boost Greenland's capacity for achieving a self-sustaining economy.

The need for special initiatives in the education sector has long been discussed. The 2019 budget proposal called for educational reform to create a more flexible and cohesive education system. The report "A Cohesive and Flexible Education System" has just recently undergone consultation, but actual political decisions are still a good way off. Any deferral of essential education sector reforms has major implications for both the generations of children and youth affected, but also for the national economy. Raising the level of educational attainment is imperative for achieving a more self-sustaining economy.

The education sector must also be given top political priority. The problems in the education sector, and not least secondary education are well-established and have been fully analysed. The most important limitation to progress in the education sector is not the institutional framework for the educational system. The problem is more with teaching standards, the failure of many pupils to acquire elementary academic skills, and thus the grades at graduation needed to progress in the educational system. The challenge lies in tackling the problems and ensuring the collaboration between parents, teachers and policy-makers that will be conducive to real improvements. An immediate step would be to set specific learning targets for

secondary school pupils. Trends in this area should be monitored closely, and any non-attainment must result in action. There are also other problems within the educational system, which can be tackled concurrently. They particularly concern the large group of youngsters that fail to progress to further education after lower secondary school. However, deliberations on the general institutional frameworks should in no way hinder the essential measures that can be put in place here and now.

The problems in the education sector and the social services sector are well-established and have been analysed in various contexts. There is a great need to progress from general deliberations to the creation of concrete action plans, with the involvement of relevant partners such as municipalities, the business community, teachers/educationists, etc.

Chapter 3 The public sector – efficiency improvements and productivity

Greenland's public sector is a major economic factor. Public sector spending accounts for 60 percent of gross domestic product, and 40 percent of Greenland's workforce is employed in the public sector. There is therefore due cause to evaluate the public sector continuously: are the right services being provided, and with maximum efficiency?

The relevance of these questions is reinforced by the radical change in the population's age composition that will occur over the coming years. The number of elderly persons is set to increase, including relative to the population of working age, and this will radically increase public expenditure; see Section 2.4. The Economic Council's analyses of this trend indicate that the ageing population will increase public expenditure by between 5 and 6 percentage points of Gross Domestic Product. Without a realignment of Greenland's economic policy, public expenditure will significantly outstrip revenue and result in systematic deficits. This situation would be unsustainable, and a solution must therefore be found to this financing problem. The 2016 Sustainability and Growth Plan presents the overall aim of solving the financing problem and making Greenland more economically self-sustaining, and cutting back public spending is a significant component of the strategy.

However, the public sector is not only under pressure from the advancing age of the population, but also public demand for improvements and further action in sectors such as education, healthcare and social services. The public sector is also a key driver for the development of infrastructure, utilities, etc.

The public sector also plays a major role in diversification of Greenland's trade and industry. Diversification can be achieved by increasing the general level of educational attainment or by investing in infrastructure, but also by freeing up labour for the private sector. If productivity and efficiency in the public sector can be increased, this would free up labour and support the scope for developing other industries.

The public sector is thus caught in a trap between, on the one hand, increased demand for welfare services and, on the other hand, the necessity of procuring financing for those services.

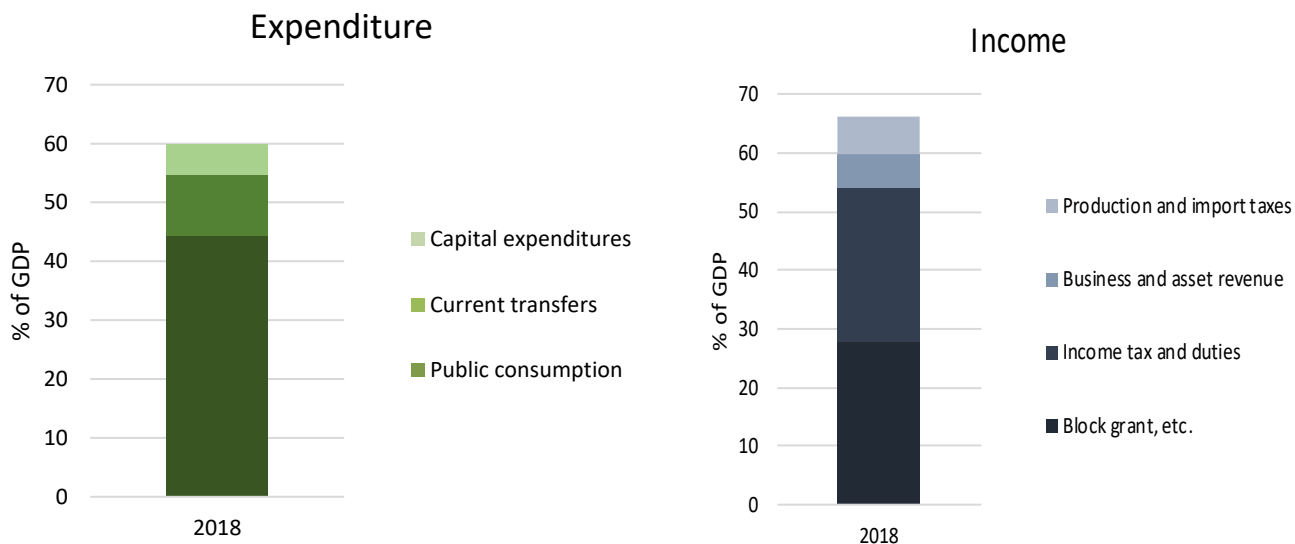
This chapter examines the public sector's size and structure as a basis for discussing the potential for realigning the sector by means of increased efficiency and productivity. This chapter concerns the public expenditure on payrolling, service procurement, etc. and not on the structure of the welfare safety net in the form of income support or the structure of the tax system. The chapter is introduced in Section 3.1 with a brief outline of the size of the sector and its expenditure composition, and Section 3.2 contains an international benchmarking. The question concerning public sector efficiency and productivity is addressed at length in Section 3.3.

3.1 The public sector – size and structure

Greenland's public sector performs many roles. The classic functions comprise the judiciary, police service, administration, etc. In a welfare society, the public sector is also responsible for education, health and care services and other welfare services provided free or at low cost to the public. This serves to ensure equal opportunities for citizens. The principle of distribution and welfare services is focal and is integral to the welfare safety net in the form of various services and benefits. Also focal are public-sector investments in infrastructure and utility companies.

Figure 3.1 shows the size and general composition of Greenland's public sector from the perspective of both expenditure and revenue. In terms of its share of national expenditure, the public sector claims 60 percent of gross domestic product. On the expenditure side of the budget, a crucial distinction is made between expenditure on current transfers in the form of benefits to replace wage-earner income (pensions, welfare benefit, unemployment benefit, etc.) and various subsidies (e.g. housing benefit), and on the other side, public-sector final consumption expenditure on activities within education, healthcare, administration, etc. A large share of public-sector final consumption expenditure payrolls employees of municipalities and the Government of Greenland and covers procurement of goods and services, such as consulting services or temporary staff in health care. The current transfers cover the cost of facilitating the welfare safety net and are not discussed any further in this chapter. In addition are capital expenditures covering public-sector investment and interest rates. Public-sector revenue breaks down into various types of tax revenue, business revenue and the block grant from the Danish Government, etc.

Figure 3.1. The size of the public sector and real economic percentage of GDP, 2018

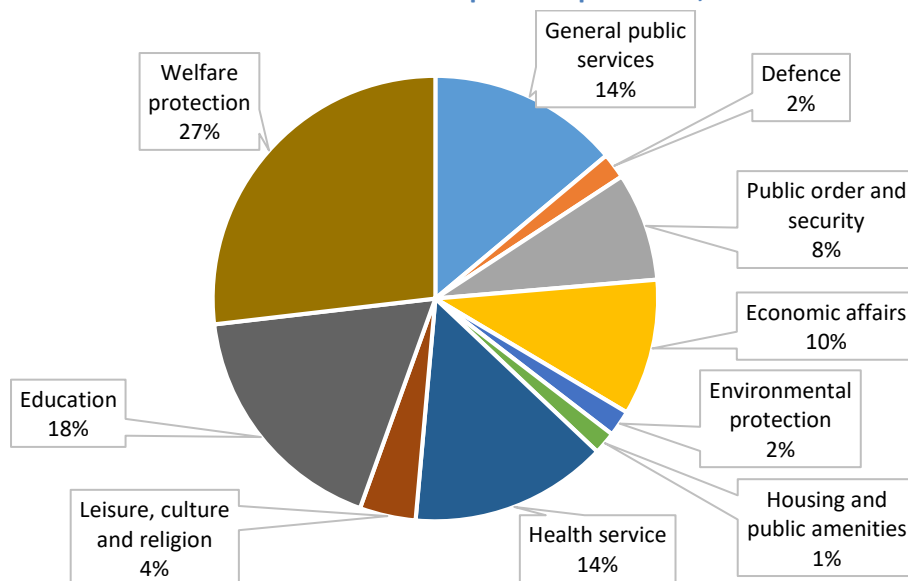


Note: Expenditure and revenue figures are for public services and public administration, and comprise the Government of Greenland, municipalities and the Danish Government). Danish Government expenditure on the police service, the judiciary and defence is covered in full by reimbursements on the revenue account, and in the revenue figure comes under "block grant, etc." Source: Public Finances 2018, Statistics Greenland.

The breakdown of public expenditure into various expenditure items is presented in Figure 3.2. The largest aggregate expenditure item is welfare protection followed by education and healthcare. An assessment of the level and breakdown of public expenditure must necessarily take into account that public services worth approx. DKK 1.2bn in 2018 are fulfilled by the Danish Government, including cost-intensive areas within the police service, judiciary and defence. Taken together with the expenditure on the administration of the Government of Greenland and municipalities, these expenditures constitute the *collective consumption of general government* and cover the traditional services fulfilled by the public sector for society as a whole. Collective consumption expenditure accounts for around 40 percent of public-sector spending. For comparison, in the Nordic countries, the share is approximately 30 percent.

In addition, public consumption consists of welfare services used individually by citizens. Greenland has a high degree of free and equal access to, e.g. education, healthcare and care services, which are made available as *individual consumption expenditure by general government*. Other public services are subject to payment of relatively modest user fees, which in some cases are means tested. This includes child day care, for example. Free and equal access to public services mean that Greenland provides equal opportunities for gaining an education and for obtaining healthcare. In this way, Greenland operates with substantial redistribution via public consumption, which serves to reduce social inequality. In many other countries, students co-finance their studies (by taking out student loans for example) and health and care services are to a greater extent financed by insurance and there is more emphasis on user fees for service. Around 60 percent of public consumption covers this type of individual consumption expenditure.

Figure 3.2. Functional distribution of total public expenditure, 2018



Note: General public services and public administration covers the Government of Greenland, municipalities and the Danish Government.

Source: Public Finances, Statistics Greenland.

In the economic policy debate, focus is directed at whether certain types of public spending support employment, production and productivity and in so doing are conducive to industrial diversification. In the theoretical literature, a distinction is made between active/productive and passive/non-productive expenditures. The active expenditure may have a positive effect on production and employment, for example, while passive expenditure has either no effect or a negative effect. A number of expenditures on education, research, infrastructure, healthcare and childcare, etc. are active expenditures supportive of the economy. Besides serving to foster trade and industry diversification, initiatives of this nature are self-financing in the sense that a higher level of employment and production increases the tax base and hence aggregate tax revenue, unlike in a situation where these expenditures are not incurred or are very low. The level of self-financing is obviously significant, but the burning issue in economic policy is the effect achieved from investing *additional* resources in these sectors or the effect of reprioritising resource consumption between the various public-sector domains. Many resources are already invested in public consumption in Greenland, and the dynamic effects of even heavier spending may therefore be limited in many public welfare domains.

Moreover, the socio-economic effects of public expenditures cannot be assessed in isolation from their financing. Some types of expenditure may, for example, have a positive effect on the employment rate, while tax-based financing has de-incentivising effects that reduce employment. Thus, in order to determine the net effect, it is necessary to take into account both the direct impacts of public spending and the secondary negative impacts of the financing. A large proportion of Greenland's public expenditure can be financed by external transfers such as the block grant from the Danish Government. This makes it possible, given the level of expenditure, to maintain a relatively low level of taxes and duties. However, when assessing further initiatives, it is necessary to take account of the consequences of the financing.

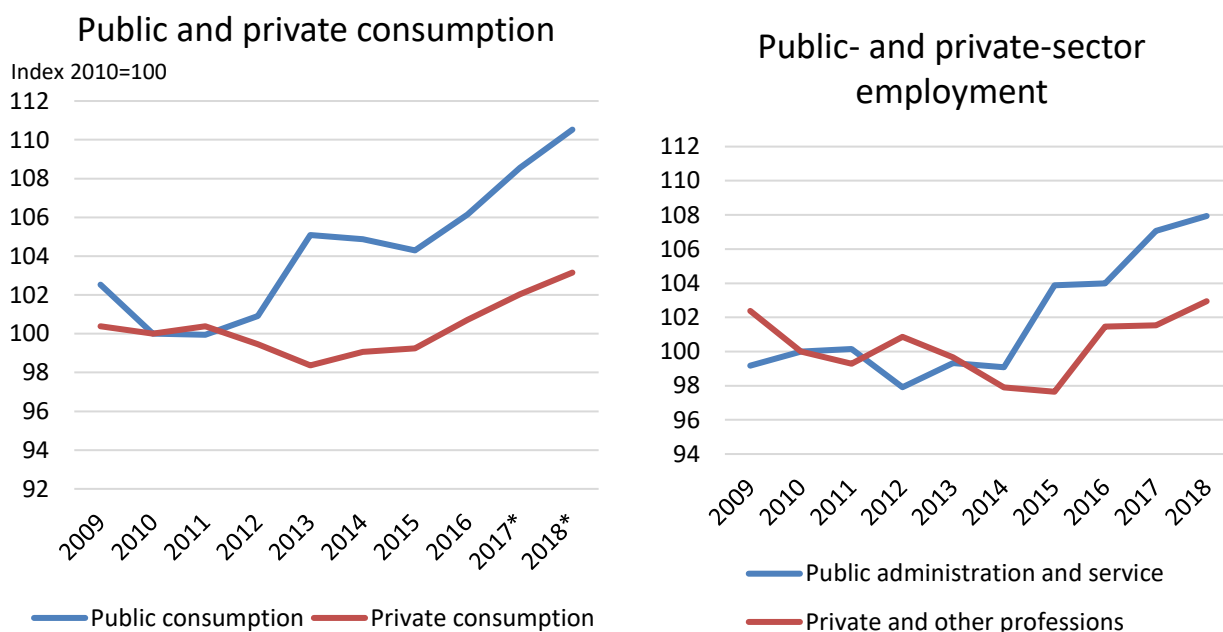
Even if public expenditures are well-founded, there is thus an upper limit to how much public expenditures and hence their financing can be increased without detriment to employment and production. There is an inverse "U-shaped" correlation between the scale of the economy and the productive elements of public expenditure. If public expenditure levels are low, any increase in productive expenditures tends to boost production as a result of their productive influence on the economy, while the negative effects of their financing remain modest. But in line with an increase in public spending, the socio-economic benefits gradually diminish. At the same time, the socio-economic costs will then increase as a result of the negative effects of financing of those expenditures.

In practice, it is not possible to say exactly where the break-even point lies between the productive effect of public expenditures and the negative effect of their financing. It all depends on what the expenditures are paying for and how they are paid for. As stated, the block grant from the Danish Government finances a large proportion of Greenland's public expenditure without the negative financing consequences, which may account for the higher level of public spending in Greenland compared to other countries. However, the public sector in Greenland has become very large, which increases the risk of any further public-sector enlargement being detrimental to the country's economic development.

Figure 3.3. shows the trend in public consumption and private consumption (discounting price and wage increases) for the period 2009-2018. Public consumption in this period followed a steadily increasing trajectory, and the increase exceeded that of private consumption. This means that public spending exceeds private spending (household final consumption expenditure) in Greenland, as one of very few places in the world. The public consumption expenditure level is approximately DKK 150,000 per capita versus household final consumption expenditure of approximately DKK 125,000 on average in 2018. More than 40 percent of full-time employees in Greenland work in the public sector. In 2019, there were 10,872 full-time employees in the public sector, of which 4,065 worked for the Government of Greenland. 6,806 for the municipalities along with a further 4,000 or so employed by companies wholly or partially owned by the Government of Greenland. It should be noted that public-sector tasks not yet devolved to Greenland from Denmark also account for a good deal of employment. Insofar as services are procured from foreign service providers owing, for example, to a shortage of skilled labour in Greenland, the resulting expenditures also hold secondary employment value.

The increase in public spending and employment is striking and cannot be explained by a change in the population's age composition, which otherwise accounts for multiple public expenditures. Since 2015, Greenland has seen an upturn in the economy and employment while public consumption expenditure has risen substantially. This underlines the above-mentioned expenditure trap between, on the one hand, the requirement for improvements or enlargements in public welfare benefits and, on the other hand, the need for expenditure reductions in the interests of future fiscal balance.

Figure 3.3. Public and private consumption and employment, 2009-2018



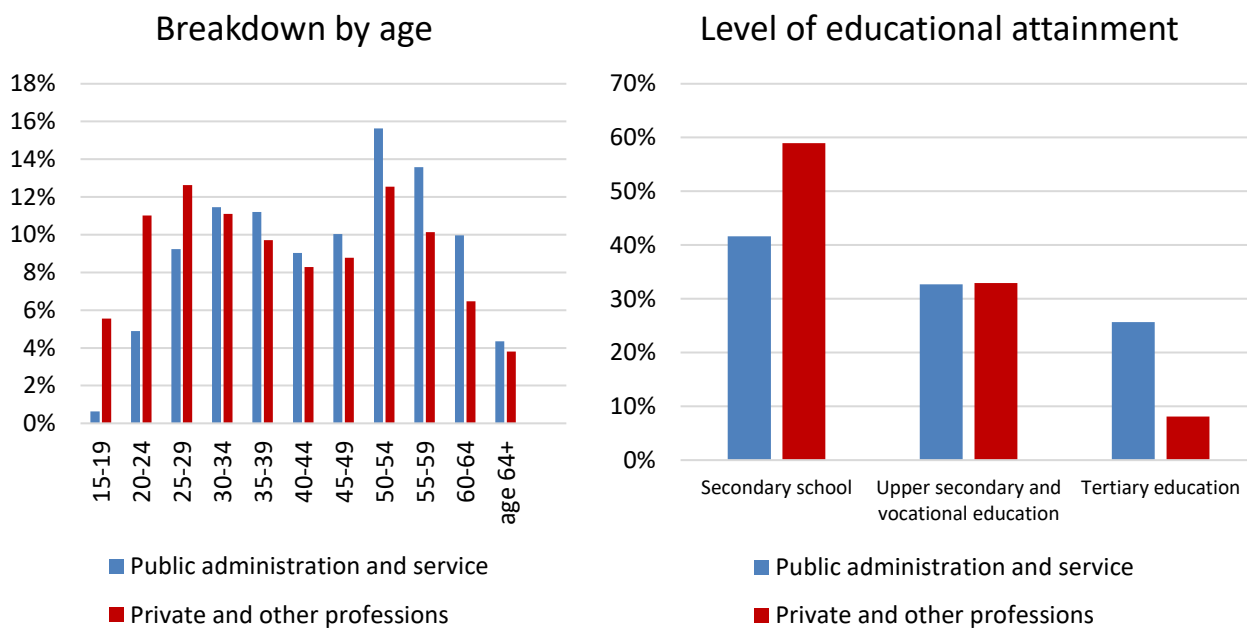
Note: The private and public consumption statistics are sourced from Greenland's National Accounts, while the employment trend is based on primary employment averaged per month within public service provision and public administration and all other occupations, which are primarily within the private-sector, including those within companies held by the Government of Greenland.

Source: Greenland's National Accounts and employment statistics, Statistics Greenland.

The goal of achieving increased efficiency and productivity in the public sector is predicated on freeing up labour for the private sector over a number of years. This is a process that must be undertaken gradually. There are already significantly more employees of senior age in the public sector compared with in the private sector; see Figure 3.4. By 2030, one in four public-sector employees in 2018 will have reached pensionable age. Freeing up labour will thus mean that young adults entering the labour market over the next decade will increasingly have to find employment in the private sector.

Naturally, there will also be cases in which efficiency improvements and digitisation will reduce demand for public-sector labour. In those cases, it will be important not to override the dynamics of the labour market in order to allow for both 'hiring and firing' in the public sector. In general, the level of educational attainment is fairly high among Greenland's public-sector employees, which gives them sound prospects for finding new positions if they are made redundant; see Figure 3.4.

Figure 3.4. Age and level of educational attainment of public and private-sector employees, 2018



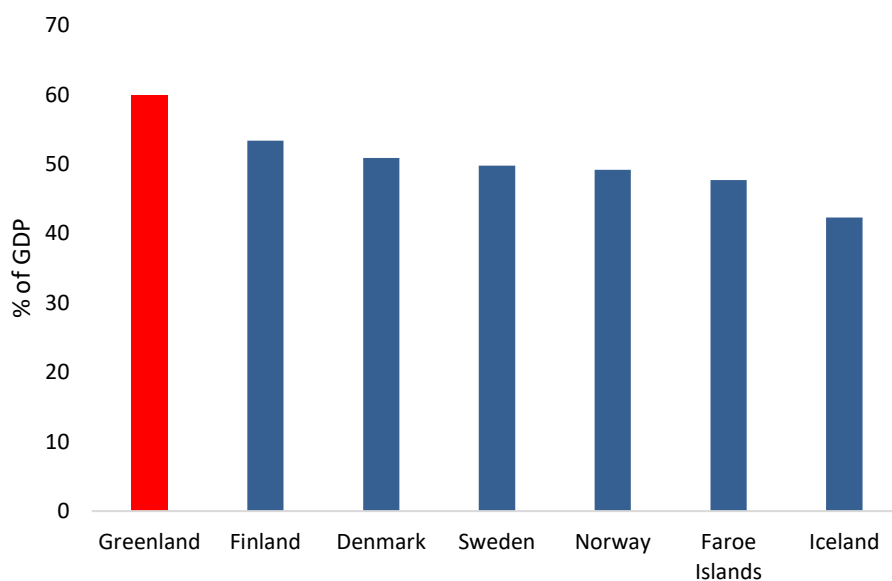
Note: The employment statistics are based on primary employment averaged per month within public service provision and public administration and all other occupations, which are primarily within the private-sector, including those within companies held by the Government of Greenland.

Source: Employment statistics, Statistics Greenland.

3.2. Greenland's public sector benchmarked internationally

The size and structure of Greenland's public sector is comparable with that of other countries. The usual comparators are the Nordic or OECD countries; Figure 3.5. The public sector is large in Greenland, including in comparison with the Nordic countries, which among OECD countries usually rank among the countries with the largest public sectors. Benchmarking the public sector across countries is not straightforward. The expenditure level tends to be influenced by whether welfare benefits are disbursed net or gross, and disparities in expenditure levels cannot be interpreted immediately as indicative of differences in quality, since if costs in a country are higher, this will result in high expenditure for a given level of quality.

Figure 3.5: Size of the public sector in the Nordic countries, 2018, measured by aggregate public expenditure as a percentage of GDP



Source: Nordic Council, Nordic Statistics, <https://www.nordicstatistics.org/public-finance/>. The data for the Faroe Islands refer to 2017.

It should be noted that benchmarking of the type presented in Figure 3.1 does not take into account the special circumstances of an economy such as Greenland's, especially a small and geographically dispersed population. The block grant means, for example, that income and consumption opportunities in society are greater than those yielded by purely domestic production. This has notably resulted in relatively high public consumption opportunities for the population.

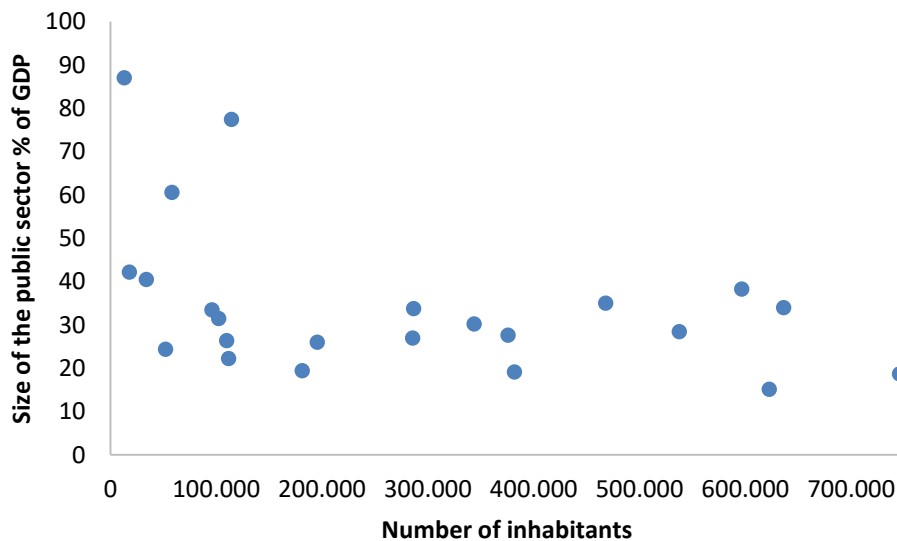
Comparisons of so-called "small states"⁴ show a certain tendency for the public sector to account for a larger share of the economy than in countries with a large population. Small states are not only characterised by the modest size of their population, but typically also long transport distances (many being islands) with small geographies, and a strongly specialised production structure. These economies are typically disadvantaged by diseconomies of small scale in their public service production, which tends in the direction of a larger public sector. The diseconomies of small scale are linked, for example, to the fact that

⁴ See, e.g. Cabezón, P. Tumbarello, & Y. Wu Strengthening Fiscal Frameworks and Improving the Spending Mix in Small States, IMF Working Paper WP/15/124, 2015.

the fixed costs of administration, parliament and many other activities must be distributed across relatively few citizens.

Small states also tend to have a high level of public debt and public expenditures that fluctuate in line with external economic trends. The last-named stems from the fact that these countries often have a more specialised trade and industry structure subject to greater fluctuation in economic activity, but also that they lack a fiscal policy instrument such as a budget act, for example. Figure 3.6 shows the correlation between the size of the public sector and population size for economies (for which data exist) with a population of fewer than 700,000 individuals.

Figure 3.6: Size of the public sector and population count for economies with fewer than 700,000 citizens.



Source: World Bank.

Figure 3.6 shows that the size of the public sector, measured by total public expenditure as a share of GDP, is fairly wide-ranging among economies with a population of fewer than 100,000 citizens. The share ranges between 20 percent and almost 90 percent. Many of these small states are small islands in the Indian Ocean, however, and are thus scarcely comparable with the arctic region.

For comparison, aggregate public expenditure in 2016 in Nunavut (not featured in Figure 3.6) accounted for 83 percent of GDP, and subsidies accounted for 78 percent of total revenue (population: just under 40,000 individuals). Nunavut thus has a relatively larger public sector and a greater dependency on subsidies than Greenland.

Greenland differs from other small states in several respects. Firstly, in its vast land mass and the scattered settlement pattern with large distances between towns and outlying settlements. So-called economic clusters linked to towns and suburban areas and close contact with other towns are thus not an option in Greenland. As such, the difficulty of benefiting from economies of scale is a fundamental term of trade. Secondly, strict control of public finances means that the public sector is not heavily indebted. However, the Government of Greenland have substantial commitments in a number of companies, and hence the ensuing risk exposure.

3.3. Efficiency and productivity in the public sector

Public sector activities are essentially predicated on the aim of fulfilling political priorities, including distribution interests, but also on so-called market failures. Distribution interests concern the commitment to giving all citizens equal access to, for example, education and healthcare and ensuring that everyone has a reasonable standard of living.

Public sector activities may also be predicated on the inefficiency of the market mechanism. The market mechanism has many advantages, but in certain domains, such as healthcare and education, it may be difficult to base services exclusively on market solutions. Private sector markets may fail to function efficiently due to information problems and transaction costs. The market mechanism advantages derive from efficient competition, which may be difficult to achieve in a country with a small, scattered population. The need for public sector commitment may thus be greater in Greenland than in other countries, but this has no bearing on the focal issue of efficiency and productivity in its public sector.

Greenland's public sector manages substantial economic resources, which makes it imperative to continuously consider two fundamental questions: are the right services being provided, and with maximum efficiency? And in the best possible way? The first question is largely a policy issue, even though it should be considered in the light of market failures, and is contingent on one priority: How important is it to expend resources in a given area, and what is the cost of achieving the set goals? These questions are crucial in the context of the distribution of resources to various purposes but also as regards the total size of the public sector. Given this distribution of resources, in specific areas it is imperative to examine continuously how services may best be provided in order to achieve maximum quality at the lowest possible expense.

The question of efficiency and productivity in the public sector is often controversial, but is a key socio-economic concern. Increased efficiency and productivity relate to whether a better standard of public sector service can be provided at no greater expense or at no detriment to quality at a lower expense. This is important in ensuring responsible management of public funds and is hence a key input in the political prioritisation process. From the citizen perspective, increased efficiency is either synonymous with service improvement or status quo and a reduced fiscal burden, and thereby reduced risk of cutbacks in other areas or tax increases.

No unequivocal answer exists as to how public spending influences efficiency and productivity in society: However, it is clear that the probability of a positive correlation likely when public institutions support competition and efficiency in the private sector through regulatory control, etc. Education, infrastructure and healthcare are commonly highlighted as public spending sectors that promote economic development. Investment in infrastructure must be socio-economically profitable and carried out as cost-efficiently as possible, which is also a fundamental requirement in Greenland's Debt and Investment Strategy of 2012. Public spending on education must facilitate higher standards all the way from secondary school to tertiary education so that young people do not drop out of the education system, and must do more to ensure that pupils gain good future employment and earning potentials. The economy of Greenland would be boosted

if public expenditures generally are given priority in order to ensure a high standard of key services within education, infrastructure and healthcare.

The great challenge in assessing public sector efficiency and productivity is that the value of public sector performance is not being quantified. In the private sector, undertakings are continuously subject to customer decisions on whether their product or service is value for money. This kind of test is not automatically in play for the public sector. Public sector services are generally made available free of charge to citizens of Greenland. This means that citizens are unaware of the price and do not consider whether the standard represents value for money. Costs are covered by public sector revenues, and policy-makers decide the scope and quality of service provision.

It is therefore imperative for Greenland's public sector to establish other methods of ensuring that public sector performances are efficient and productive. This could be achieved in many ways, for example, by evaluating specific areas, conducting surveys of citizen ratings and satisfaction with the services provided, various metrics for the scope and quality of public-sector undertakings. In many countries, many attempts have been made to establish means of assessing the efficiency and productivity of public-sector activities.

However, many of their methods are in themselves both administratively- and cost-intensive. It would thus be helpful to consider simpler, more viable approaches to raising efficiency in the public sector. Expenditure analyses are now planned and in certain domains have also been carried out. It is important to maintain the momentum of this process in order to achieve improved decision-support. However, it is equally important for these analyses to maintain a keen focus on identifying genuine cost-saving potentials and efficiency improvements that are viable in practice. All key expenditure items could be analysed at regular intervals with a view to economising, including in high-priority sectors such as education, healthcare and social services. In recent years, Greenland's budget proposals have proposed such expenditure analyses, with provisions made for efficiency improvement initiatives for subsequent implementation. However, experience shows that finding those economies is subsequently difficult. However, the 2021 budget proposal sets out a number of specific cost-reduction measures, which could be implemented immediately and contribute to boosting the public finances. These include administrative savings in the central administration as an example.

Another method is so-called 'green harvesting', where budgets are reduced by a certain percentage over a number of years. The advantage of this method is that it is very simple to implement. If, for some years, focus on efficiency and productivity has been lacking, this is an easy way of reaping some of the locked-up rewards. One of the drawbacks is that the same opportunities for efficiencies do not exist in all domains: it is not feasible, for example, to step up efficiency in activities where direct human contact and care-giving are the primary service. Conversely, in other domains, such as those that are more administratively intensive, the potential will be greater. The green harvesting method can consequently be applied to certain budget items in order to focus on reducing the administrative costs. In the 2021 budget proposal, one of the expenditure-reducing initiatives is to stall price and wage adjustment of the operating and grant appropriations in 2021. This would yield a budgetary improvement of around DKK 75m. The waiving of the price and wage adjustment item is an example of the green harvesting method mentioned above. Consideration must be given to suspending price and wage adjustments going forward, possibly for the

more administratively intensive items, in order to accomplish the necessary budgetary improvements laid down in the Sustainability and Growth Plan.

Case study: Effects of reduced public-sector employment

Greenland's Sustainability and Growth Plan proposes reductions in public-sector spending as a key solution to the public financing issue. The Bill proposes making economies by 2030 equating to approximately 9 percent of public expenditure (DKK 700m less than public consumption expenditure of around DKK 7,700m in 2016). If actual efficiency improvements are involved, service provision will be unchanged and hence have no direct effect on citizens. The aim is to achieve the same standard of public service output but with lower resource utilisation. A 9 percent shedding in the number of public-sector employees equates to almost 1,000 fewer full-time employees, who, over a number of years, can be freed up for employment in the sector (primarily service industries).

The order of magnitude of this increase in employment in the private sector may be illustrated by a calculated example.

The gross value added (GVA) in public-sector service sectors, i.e. administration, healthcare, education, culture, etc. is broken down by payroll expenditure and procurement of goods and services, and averaged approximately DKK 340,000 per public-sector employee in 2019. For comparison, the GVA in the primarily private service sectors – transport, retail, hotels, IT and financing – averaged DKK 678,000 per employee. A public-sector employee released for employment in a private-sector service industry will thus increase the value added by DKK 338,000 net.

The exact effect of this type of reassignment of labour from the public to the private sector is contingent on a number of factors, but the above example shows the potential major effects and therein the contribution to a more self-sustaining economy.

The Sustainability and Growth Plan proposes economies in public expenditures as a result of efficiency improvements and productivity increases as a pivotal element. This plan has so far only to a very limited extent been translated into specific initiatives. The spending increases of recent years are not consistent with the need for higher efficiency in the public sector in order to overcome the financing problems posed by the advancing age of the population. There is therefore an urgent need to follow up the Sustainability and Growth Plan with specific and viable initiatives together with a schedule of when the initiatives will be implemented. The COVID-19 crisis has major implications for Greenland's public finances and stepped up the need to follow up on the fiscal policy strategy; see Chapter 2.

The Economic Council

The Economic Council compiles independent analyses and appraisals of the economy of Greenland. The Council is appointed by the Government of Greenland and is led by an independent chairmanship. The Chairman of the Economic Council is Professor Torben M. Andersen.

The analyses serve as an independent contribution to decision-support for Greenland's economic policy. The assessment of economic trends and the sustainability of Greenland's economic policy are recurring topics in the Council's reports. The reports deal with current reform topics geared to making Greenland more economically self-sustaining. Such topics concern the education sector, fisheries management, taxation, the housing sector, labour market and welfare policy, the extraction industry and trade and industry policy.

The Economic Council's analyses are published in reports and concise policy-oriented briefings on the Council's website: <http://naalakkersuisut.gl/da/Naalakkersuisut/Departementer/Finans/Oekonomisk-raad>

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