MINISTRY OF FINANCE

Economic Survey

Summer 2018

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Economic Prospects

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Abstract

The strong growth of the Finnish economy will continue in 2018, after which economic growth will slow to below 2%. In the next few years, the economy will be supported by both foreign trade and domestic demand. Growth in exports will level off in line with trends in world trade, and economic growth will no longer be supported by net exports as strongly as before. Household demand will be limited by slower growth in real disposable income. Finland's GDP will grow by 2.9% in 2018. Strongly sustained economic growth and increased demand for labour will increase the number of employed in 2018 by 1.9% compared with the previous year, and the employment rate will rise to 71.2%.

In 2019, GDP growth will slow to 1.8%, while investment growth is projected to slow significantly. This is due, in particular, to a decline in the number of start-ups for new construction projects. In addition, investment decisions for major forest industry projects have been moved forward. Finland's GDP will grow by 1.7% in 2020.

The reasonably rapid continuing growth in GDP and the moderate development of real wages will maintain demand for labour in the forecast period. Due to the large number of unemployed and hidden unemployed as well as measures to increase the supply of labour, labour supply will not yet constrain growth in employment and production at the level of the whole economy. In individual sectors, a shortage of skilled labour may already become a barrier to growth. The number of people in employment will grow by nearly 1% per year in 2019–2020. The employment rate will rise to 72.6% in 2020.

Good economic conditions will reduce the general government deficit and debt ratio. The general government budgetary position will be almost in balance by 2020 and the public debt to GDP ratio will fall below 60% next year.

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Tiivistelmä

Suomen talouden suhdannenousu jatkuu vielä vuonna 2018, minkä jälkeen talouskasvu hidastuu ja jää alle kahteen prosenttiin. Lähivuosina taloutta tukevat sekä ulkomaankauppa että kotimainen kysyntä. Viennin kasvu tasoittuu maailmankaupan kasvun mukaiseksi ja nettoviennin kasvua tukeva vaikutus pienenee. Kotitalouksien kulutuskysyntää rajoittaa reaalisten käytettävissä olevien tulojen hidastuva kasvu. Vuonna 2018 BKT kasvaa 2,9 %. Vahvana jatkuva talouskasvu ja voimistunut työvoiman kysyntä nostavat v. 2018 työllisten määrän 1,9 % edellisvuotta korkeammaksi ja työllisyysasteen 71,2 prosenttiin.
Vuonna 2019 BKT:n kasvu hidastuu 1,8 prosenttiin. Investointien kasvun ennustetaan hidastuvan selvästi v. 2019. Tämä johtuu erityisesti uusien rakennushankkeiden aloitusmäärien kääntymisestä laskuun. Lisäksi suurten metsäteollisuushankkeiden investointipäätöksiä on siirretty eteenpäin. Vuonna 2020 BKT kasvaa 1,7 %.
Bruttokansantuotteen kohtuullisen nopeana jatkuva kasvu ja reaalipalkkojen maltillinen kehitys ylläpitävät työvoiman kysyntää ennustejaksolla. Työttömien ja piilotyöttömien suuresta määrästä sekä työvoiman tarjontaa lisäävistä toimenpiteistä johtuen työvoiman tarjonta ei koko talouden tasolla vielä rajoita työllisyyden ja tuotannon kasvua. Yksittäisillä toimialoilla pula osaavasta työvoimasta voi jo muodostua kasvun esteeksi. Työllisten määrä kasvaa lähes 1 % vuodessa vuosina 2019–2020. Työllisyysaste nousee 72,6 prosenttiin v. 2020.
Hyvä suhdannetilanne pienentää julkisen talouden alijäämää ja velkasuhdetta. Julkisen talouden rahoitusasema lähes tasapainottuu vuoteen 2020 mennessä ja julkinen velka suhteessa bruttokansantuotteeseen painuu alle 60 prosentin ensi vuonna.

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Referat

Konjunkturuppgången i den Finländska ekonomin fortsätter även under år 2018, varefter den ekonomiska tillväxten förblir under två procent. Den ekonomiska utvecklingen stöds under de närmaste åren av såväl utrikeshandel som inhemsk efterfrågan. Tillväxten i exporten stabiliseras i likhet med utvecklingen i världshandeln och tillväxtkontributionen av nettoexporten minskar. Hushållens konsumtionsefterfrågan begränsas av den långsamma ökningen i de disponibla inkomsterna i reala termer. Bruttonationalprodukten växer år 2018 med 2,9 %. Fortsatt stark ekonomisk tillväxt samt tilltagande efterfrågan på arbetskraft höjer år 2018 antalet sysselsatta med 1,9 % jämfört med fjolåret. Sysselsättningsgraden stiger till 71,2 %.
BNP-tillväxten mattas år 2019 av till 1,8 %. Tillväxten i investeringar förutspås minska tydligt år 2019. Detta beror i synnerhet på att antalet nya påbörjade byggnadsprojekt minskar. Dessutom har investeringsbeslut gällande stora projekt inom skogsindustrin flyttats framåt. BNP växer 1,7 % år 2020.
Efterfrågan på arbetskraft upprätthålls under prognosperioden av den fortsatt tämligen snabba tillväxten i BNP samt av den måttliga utvecklingen i reallönerna. På grund av det stora antalet arbetslösa och dold arbetslöshet samt åtgärder för att öka arbetskraftsutbudet, begränsar utbudet på arbetskraft inte ännu sysselsättnings- och produktionstillväxten i ekonomin som helhet. Inom enskilda branscher kan dock brist på kunnig arbetskraft redan utgöra en begränsning för tillväxten. Antalet sysselsatta ökar med nästan 1 % per år under åren 2019–2020. Sysselsättningsgraden stigen till 72,6 % år 2020.
Det goda konjunkturläget minskar underskottet och skuldsättningsgraden hos den offentliga ekonomin. De offentliga finanserna kommer nästan att balansera år 2020 och den offentliga skulden i förhållande till bruttonationalprodukten sjunker nästa år till under 60 %.

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PREFACE

This Economic Survey offers projections of economic developments in 2018–2020. The forecast and trend projections in the survey are prepared independently by the Ministry of Finance Economics Department based on the Act on the implementation of the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union and on multi-annual budgetary frameworks (869/2012).

The forecasts are based on national accounts data for 2017 published by Statistics Finland in May 2018 and on other public statistical sources available by 12 June 2018.

Helsinki June 2018
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The source for all data on materialised developments is Statistics Finland unless otherwise indicated.

SYMBOLS AND CONVENTIONS USED

-	nil
0	less than half the final digit shown
..	not available
.	not pertinent
**	forecast
CPB	CPB Netherlands Bureau for Economic Policy Analysis
HWWI	Hamburgisches WeltWirtschafts Institut
IMF	International Monetary Fund
MoF	Ministry of Finance

Each of the figures presented in the tables has been rounded separately.

Contents

Summary

Economic outlook for 2018–2020

The strong growth of the Finnish economy will continue in 2018, after which economic growth will slow to below 2%. In the next few years, the economy will be supported by foreign trade and domestic demand. Investments will remain supportive of economic growth, even though construction investment will decline next year. Growth in exports will level off in line with trends in world trade, and economic growth will no longer be supported by net exports as strongly as before. Household demand will be limited by slower growth in real disposable income.

Good economic conditions will reduce the general government deficit and debt ratio. The consolidation measures decided by the Government will strengthen public finances. The general government budgetary position will be almost in balance by 2020 and the public debt to GDP ratio will fall below 60% next year.

Positive development of the global economy will continue

Growth of global GDP will be at its most rapid during the current year. The robust economic conditions will continue in the next few years, but many predictive indicators suggest a slight slowdown in global economic growth. Growth in world trade will also be at its highest level during the current year. Growth will continue to be rapid, driven by the United States and the emerging economies. In the next few years, growth in world trade will slow to some extent, but will remain quite fast. The role of the emerging economies will be particularly significant. The ratio of growth in world trade to economic growth will decline slightly.

Construction investment set to decline

Finnish GDP is expect to grow by 2.9% in 2018. Strong economic growth will continue this year because the order books of industrial enterprises are strong and major construction projects are still ongoing.

Private investment, in both machinery and equipment and housing construction, will grow rapidly in 2018. There is an underlying shortage of capacity, which is reflected in industry and construction surveys. Growth of private consumption will be supported by rising earnings as well as by an improvement in employment.

Export growth is expected to continue in 2018. Machinery and equipment exports are developing favourably and investments in the forest industry will be fully reflected in exports in 2018. Exports of means of transport will grow significantly in 2018. Imports of goods were boosted in the first quarter of the year by, among other things, imports of durable goods and investment goods, and imports of services grew faster than imports of goods. In the forecast period, imports of goods will be strengthened by imports of intermediate goods used by the export industry.

Strongly sustained economic growth and increased demand for labour will increase the number of employed in 2018 by 1.9% compared with the previous year, and the employment rate will rise to 71.2%. The inflation forecast for the current year is 1.1%, as measured by the national Consumer Price Index. This year, inflation will rise mainly due to increased prices for services, food and energy. Changes in the prices of goods will also slow inflation this year. Changes in indirect taxation, on the other hand, will boost inflation by an estimated 0.3–0.4 percentage points.

In 2019, GDP growth will slow to 1.8%, while investment growth is projected to slow significantly. This is due, in particular, to a decline in the number of start-ups for new construction projects. In addition, investment decisions for major forest industry projects have been moved forward.

Growth of private consumption will be supported by rising earnings and an improvement in employment in 2019. The sum of wages and salaries will rise by 3.5% and keep growth of household disposable income above the level of recent years. In real terms, however, growth of household disposable income will slow as inflation picks up, which will curb growth in private consumption.

Although the favourable rapid growth in world trade will create a better outlook for Finnish exports in the forecast period, Finland's notional export demand will increase more slowly than growth in world trade, in line with the more moderate growth of the euro area, and exports will also grow more slowly than world trade in 2019. Although exports of services are constantly growing, exports will also continue to be mainly goods-driven in the future.

The reasonably rapid continuing growth in GDP and the moderate development of real wages will maintain demand for labour in the forecast period. Due to the large number of unemployed and hidden unemployed as well as measures to increase the supply of labour, labour supply will not yet constrain growth in employment and production at the level of the whole economy. In individual sectors, a shortage of skilled labour may already become a barrier to growth. The number of people in employment will grow by 1.0% in 2019 and by 0.7% in 2020. The employment rate will rise to 72% in 2019 and further to 72.6% in 2020.

Finland's GDP will grow by 1.7% in 2020. The slowdown in growth will be largely due to private consumption demand, as growth in household disposable income levels off. A pick-up in inflation will curb growth in real disposal income, although improving employment will simultaneously support it. Growth in private investment will continue to be good, as production investment is increased by major projects planned for the forest industry. Employment will continue to improve, but slightly slower than before.

Inflationary pressures will remain moderate in the forecast period, even though the economy will have fewer free resources as the output gap closes and production gradually exceeds its estimated potential level. In 2019 and 2020, the national Consumer Price Index is expected to rise by 1.4% and 1.6% respectively.

Economic growth strengthens public finances

The general government deficit will fall and the debt to GDP ratio will decline in the coming years, boosted by good economic growth. General government finances, after a prolonged period of weak economic development, will continue to be in a more vulnerable state than in the period before the financial crisis. The buffers for future expenditure pressures and downturns remain very thin. Population ageing will exert pressure on general government finances in the next decade, particularly as care expenditure will continue to grow rapidly.

Of the subsectors of general government finances, central government will be most in deficit. Local government will also continue to run a slight deficit. County government, which will begin in 2020, will also be in deficit. The county government deficit will be largely due to the hospital districts' many premises investments decided on earlier, which will be transferred to the Counties' Service Centre for Facilities and Real Estate Management. The surplus of the social security funds will decrease slightly in the next few years.

Risks inherent in economic growth

Most of the risks inherent in the global economy are still skewed to the downside. The main negative risk is protectionism and the threat of a trade war. The United States' trade policy measures have resulted in a tense situation among key trading partners. Trade-restricting measures would hamper business activity and undermine benefits to consumers.

The steel and aluminium tariffs imposed by the United States will have a relatively minor direct impact on Finnish exports, however, because Finland's exports of steel products to the United States are quite low. According to customs statistics, aluminium and steel goods subject to the import tariffs accounted for 1.8% of Finland's total exports to the United States in 2017. Should it spread further, the erection of trade barriers may, however, lead to a slowdown in growth of demand across the globe. The indirect effects of intensifying protectionism would naturally also be reflected more strongly in Finnish exports.

The uncertainty surrounding the Italian economy may increase. Very high public indebtedness, the fragility of the banking sector and the many structural problems of the economy are causing concern, which may weaken the outlook for the euro area. On the other hand, the capacity of euro area institutions to withstand and resolve crises is stronger than before the debt crisis of recent years.

The most significant of the positive risks is the faster than expected economic growth in the industrialised countries, especially in Europe, and particularly if countries continue to implement structural reforms supporting growth.

In the Finnish economy, the risks are in balance. An acceleration of investment in 2020 is partly based on the timing of major projects, with which there are associated risks. The large-scale implementation of major projects would increase the level of investment significantly higher than now forecast.

Households' growing indebtedness has risen to a very high level. Debt is concentrated in a relatively small group of households that are particularly vulnerable to the negative development of the economy or the housing market. Should risks relating to the development of household debt and the housing market materialise, household consumption opportunities may be reduced.

Table 1. Key forecast figures

	2017	2015	2016	2017	2018**	2019**	2020**
	EUR bn	change in volume, %					
GDP at market prices	224	0.1	2.3	2.7	2.9	1.8	1.7
Imports	85	3.2	5.4	3.7	3.4	3.0	2.6
Total supply	309	1.0	3.1	3.0	3.1	2.1	1.9
Exports	86	0.9	3.5	7.8	4.9	4.0	3.2
Consumption	174	1.3	1.7	1.6	1.6	1.2	1.2
private	122	1.7	1.7	1.7	2.0	1.6	1.4
public	52	0.2	1.5	1.6	0.7	0.4	0.9
Investment	51	0.7	8.0	5.8	4.5	1.9	2.1
private	42	2.2	8.2	8.1	4.8	1.9	2.9
public	9	-5.2	7.4	-4.3	3.2	1.8	-1.8
Total demand	311	1.2	2.9	3.5	3.2	2.2	2.0
domestic demand	225	1.3	2.7	2.0	2.5	1.5	1.5

Table 2. Other key forecast figures

	2015	2016	2017	2018**	2019**	2020**
GDP, EUR bn	210	216	224	234	242	251
Services, change in volume, %	0.4	1.5	2.9	2.7	1.9	1.7
Industry, change in volume, %	-1.7	1.9	3.9	5.9	2.6	2.0
Labour productivity, change, %	0.2	1.7	2.5	1.3	1.0	1.0
Employed labour force, change, %	-0.4	0.5	1.0	1.9	1.0	0.7
Employment rate, %	68.1	68.7	69.6	71.2	72.0	72.6
Unemployment rate, %	9.4	8.8	8.6	8.0	7.5	7.0
Consumer price index, change, %	-0.2	0.4	0.7	1.1	1.4	1.6
Index of wage and salary earnings, change, %	1.4	0.9	0.3	1.8	2.6	2.8
Current account, EUR bn	-1.5	-0.7	1.6	1.4	1.9	2.0
Current account, relative to GDP, %	-0.7	-0.3	0.7	0.6	0.8	0.8
Short-term interest rates (3-month Euribor), %	-0.0	-0.3	-0.3	-0.3	-0.1	0.1
Long-term interest rates (10-year govt. bonds), %	0.7	0.4	0.6	1.0	1.3	1.7
General government expenditure, relative to GDP, %	57.1	55.9	53.6	52.4	51.9	51.7
Tax ratio, relative to GDP, %	43.9	44.0	43.3	42.2	42.1	41.8
General government net lending, relative to GDP, %	-2.8	-1.8	-0.6	-0.7	-0.3	-0.1
Central government net lending, relative to GDP, %	-3.0	-2.7	-1.7	-1.7	-0.9	-0.6
General government gross debt, relative to GDP, %	63.5	62.9	61.3	60.0	59.4	58.4
Central government debt, relative to GDP, %	47.6	47.4	47.2	46.3	45.8	45.0

CALCULATION OF THE EFFECTS OF A WEAKENING IN THE EXPORT DEMAND

As economic growth continues in Finland, it is appropriate to examine the impact on growth of possible negative shocks. In this box, the macroeconomic effects of a temporary weakening of export demand are examined using the macro model (Kooma model) of the Ministry of Finance Economics Department. During the last two years, Finland's economic growth has been partly based on growth of exports, which has resulted from the strong growth path of the global economy and trade. Despite the favourable development, there are also risks perceptible in the global economy, of which an increase in protectionist measures and political uncertainty can be mentioned as examples. In addition, the upswing has continued in many export countries for several years now and the growth outlook for the euro area has deteriorated slightly.

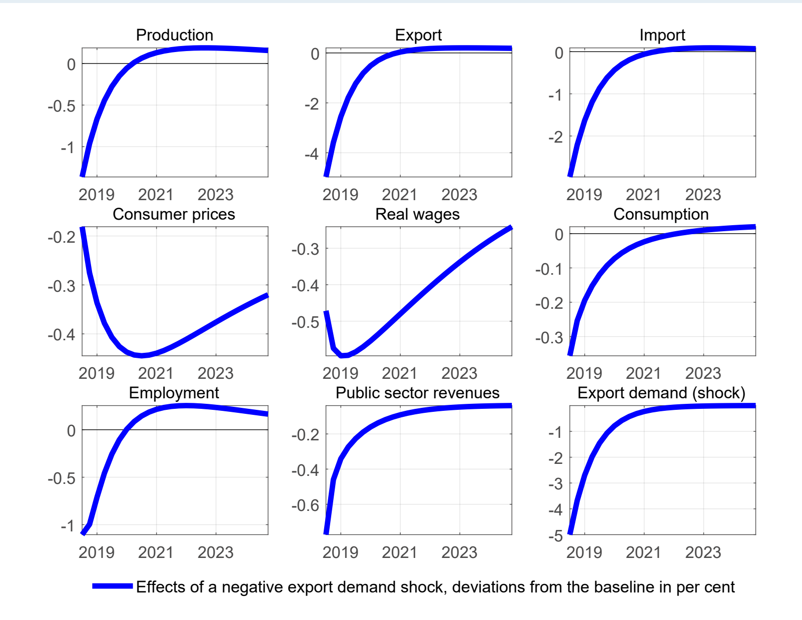
A natural way of modelling the effects of foreign shocks using the Kooma model is through export demand. The results below are reported in relation to a steady-state path, such as the assessment of Finland's economic outlook presented by the Ministry of Finance Economics Department in this publication. In the calculations, a shock has been used that weakens Finland's export demand by five per cent in the second quarter of 2018. In addition, the shock itself is assumed to weaken over time, so that its impact on export demand is only around two per cent in 2019.

The negative demand shock weakens the economy. GDP declines by just over one per cent due to a decrease in net exports. Exports fall immediately as a result of the shock by five per cent. Imports also fall because some of them are used for manufacturing export products. Imports, however, fall less than exports as some of the imports are sold directly to consumers.

The negative demand shock also adversely affects the outlook for export enterprises and domestic production. When export demand falls, excessive supply is generated in the national economy, thereby creating negative pressure on prices and wages. Consumer prices fall slightly less than wages, meaning a negative real wage development temporarily weakens private consumption. Enterprises' impaired earnings expectations result in fewer job vacancies and increased unemployment. This is reflected particularly in central government tax revenue, i.e. tax revenue falls and the deficit grows.

As a result of the decline in export demand, the Finnish GDP grows in two years more slowly than in the steady-state path. Through a reduction of real wages and Finland's relative export prices, the outlook for export enterprises and domestic production begins to improve, however, in the third year. Enterprises increase their production and hire new labour, which leads to improved employment. As the calculation assumes that wages are rigid also upwards, a rise of earnings more slowly than the steady-state path is reflected in an employment trend better than the steady-state path. This results in a slightly higher employment than on the steady-state path and thereby a higher production. As the impact of the shock subsides, exports begin to return to the steady-state path. Also the imports follow the development of exports and private consumption.

In summary, it can be stated that an export demand shock will have significant effects on a small and open economy like that of Finland. In addition to foreign trade, the impact of the shock is also rapidly reflected in household consumption and general government finances, such that consumption declines and central government debt grows. In the medium term, private consumption and central government debt return to their steady-state paths. The rate of adjustment, however, is affected by the assumptions of the model, such as wage inflexibility, and also, in practice, consumer and business confidence, for example.



1 Economic outlook

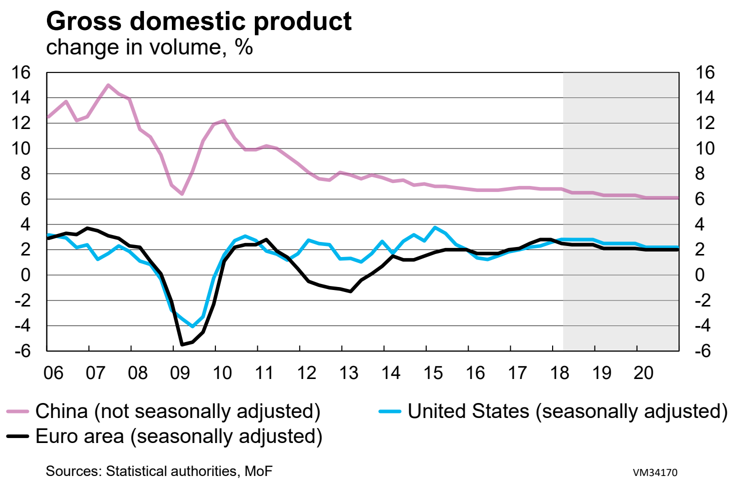
1.1 Global economy

Fastest stage of global economic growth this year

The positive development of the global economy will continue in the forecast period. GDP growth will be at its most rapid in the current year, as many large economies are close to or even above their output potential. The strong economic conditions will continue in the next few years, but many leading indicators suggest a slight slowdown in global economic growth. Growth in world trade will also be at its highest level during the current year.

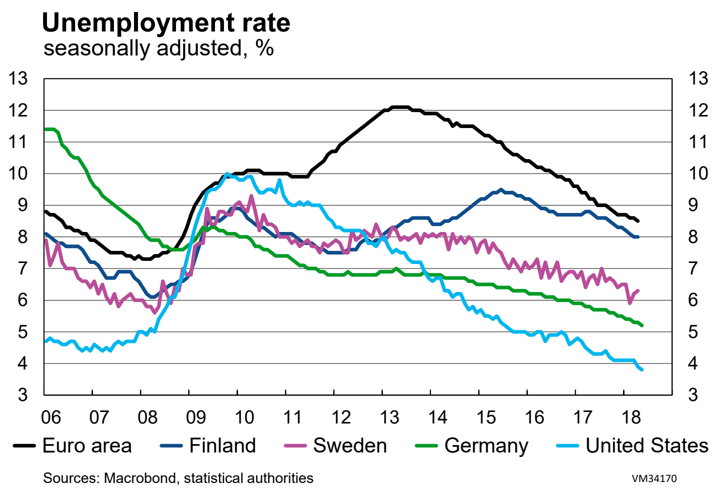
The United States' economic growth will be boosted this year by an expansive fiscal policy. In particular, the tax policy changes announced at the end of last year will accelerate growth. Unemployment is at a very low level, consumer confidence is high and inflation is picking up. The Federal Reserve will continue its policy of raising interest rates. The outlook for the near future is slightly more subdued, however: the manufacturing purchasing managers' index and new orders have started to decline in the early part of this year. Economic growth will also slow down somewhat in the forecast period.

The euro area is also experiencing strong economic growth. This year, growth will match the previous year's level, but preliminary data clearly indicate a slowing of growth in many countries in the first quarter of this year. Leading indicators have noticeably begun to decline in the early part of the year, although they are still at a relatively high level. Particularly in Germany, manufacturing confidence has started to fall. Inflation remains low.



In Britain, the outlook is to a large extent subdued due to uncertainty caused by Brexit. Economic growth will slow to an annual rate of less than 1% in the forecast period. Economic growth in Sweden is also slowing after a long period of rapid growth. The outlook is overshadowed by the housing market situation.

According to preliminary data, economic growth turned negative in Japan in the first quarter of this year. Consumer confidence is high, but the threat of deflation has not yet completely disappeared. Economic dynamism is constrained by an ageing population and a decline in the working age population.



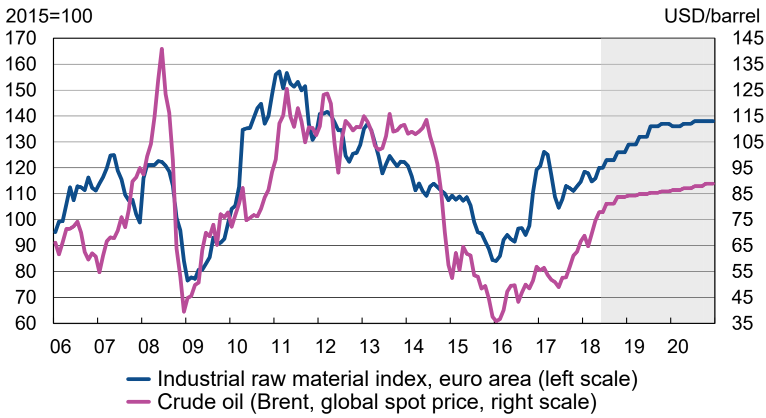
Fast, but slowing, growth is continuing in China. Preliminary data for the early part of the year suggest relatively rapid growth, and predictive indicators provide a cautiously positive picture of prospects for the near future. Exports and investments are slowing somewhat. The current account surplus will continue to decline as the focus of growth shifts from exports to consumption.

Economic growth in Russia continues to be quite subdued, although the recent increase in the oil price will boost consumption and investment. A sustainable improvement of the economy is constrained by an unbalanced production structure, weak productivity and many other structural factors.

The outlook for other emerging economies is largely positive. The Indian economy is continuing to enjoy rapid growth. Economic growth is recovering in Brazil after an extensive period of difficulty. The outlook for South Africa is improving as the political situation settles, although GDP contracted sharply in the first quarter of this year.

The rapid rise in crude oil prices in recent months reflects OPEC and Russian production restrictions, tensions in the Middle East and the prolongation of the crisis in Venezuela. The rise is therefore largely due to supply factors, although the rapid growth of the global economy is also increasing demand for crude oil. Prices of industrial raw materials are rising, driven by strong economic growth.

Raw materials prices



Sources: Hamburgisches WeltWirtschafts Institut, Macrobond, MoF

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Interest rates have risen in the United States as inflation accelerates. In the euro area, the development of interest rates has been moderate, with the recent exception of Italy. In the next few years, both short- and long-term interest rates will rise in Europe.

Rapid growth in world trade is levelling off

Growth in world trade accelerated at the end of last year. Growth will continue to be rapid this year, driven mainly by the United States and the emerging economies. In the case of the euro area, trade has developed more modestly. In the next few years, growth in world trade will slow to some extent, but will remain quite fast. The role of the emerging economies will be particularly significant. The ratio of world trade to economic growth will decline slightly.

Risks are skewed more to the downside

Recent developments in the global economy mean that risks are, to some extent, skewed more to the downside than estimated previously.

The main negative risk is protectionism and the threat of a trade war. The United States' trade policy measures have resulted in a tense situation among key trading partners. Trade-restricting measures would hamper business activity and undermine benefits to consumers. Should it intensify, protectionism could slow down growth in world trade and the global economy

The uncertainty surrounding the Italian economy may increase. Very high public indebtedness, the fragility of the banking sector and the many structural problems of the economy are causing concern, which may weaken the outlook for the euro area. On the other hand, euro area institutions are stronger than before the debt crisis of recent years.

Geopolitical tensions have risen, particularly with respect to the Middle East. An escalation of the situation would be quickly translated into an even higher increase in the price of crude oil.

A significant positive risk is the more favourable than expected economic development in industrialised countries, particularly in the United States and in Europe. The positive employment trend may support consumer confidence more than expected. Lower than expected interest rates may lead to stronger private consumption.

Table 3. Gross domestic product

	2015	2016	2017	2018**	2019**	2020**
	change in volume, %					
World (PPP)	3.3	3.2	3.7	3.9	3.7	3.6
Euro area	2.2	1.8	2.4	2.4	2.1	2.0
EU	1.6	1.7	2.3	2.2	1.9	1.8
Germany	1.5	1.9	2.2	2.5	2.3	2.1
France	1.2	1.2	1.8	2.1	1.9	1.8
Sweden	3.9	3.3	2.4	2.7	2.1	1.9
United Kingdom	2.2	1.8	1.8	1.3	1.0	0.8
United States	2.6	1.5	2.3	2.8	2.5	2.2
Japan	1.1	1.0	1.7	1.1	0.9	0.8
China	6.9	6.7	6.9	6.5	6.3	6.1
India				7.5	7.6	7.4
Russia	-3.7	-0.2	1.5	1.5	1.4	1.3

Sources: Eurostat, statistical authorities, IMF, MoF

Table 4. Background assumptions

	2015	2016	2017	2018**	2019**	2020**
World trade growth, %	2.0	1.6	4.7	4.9	4.7	4.4
USD/EUR	1.10	1.10	1.15	1.17	1.09	1.07
Industrial raw material price index, EA, € (2015=100)	100.1	96.3	114.5	121.5	133.5	137.3
Crude oil (Brent), $/barrel	53.5	45.1	54.8	77.5	85.1	87.6
3-month Euribor, %	-0.0	-0.3	-0.3	-0.3	-0.1	0.1
Government bonds (10-year), %	0.7	0.4	0.6	1.0	1.3	1.7
Export market share (2000=100)[1]	90.3	92.2	95.0	95.0	94.3	93.2
Import prices, %	-4.3	-2.8	3.5	2.6	2.4	2.1

1) Ratio of export growth to world trade growth
Sources: Statistical authorities, CPB, HWWI, Reuters, MoF

1.2 Foreign trade

Finland's foreign trade grew strongly in 2017. Growth in exports was boosted by the brisk growth in world trade, which will continue to be buoyant, particularly at the beginning of the forecast period. In 2019 and 2020, world trade will grow more slowly than this year. In addition, the euro area's economic development will be more moderate, which will slow growth in Finland's export demand.

1.2.1 Exports and imports

Exports and imports will continue to grow

According to current data, export volume grew in the first quarter of this year by only 0.3% compared with the corresponding period last year. Service exports grew in the first quarter by 2.9%, while goods exports declined slightly, by -0.3%. Deliveries of ships in the first quarter of last year are reflected in a high reference level for goods exports. This year, exports are expected to continue to grow at a rate of slightly less than 5%.

The rapid growth in world trade contributed to the brisk growth in exports in 2017. Goods exports to the euro area grew rapidly, but exports to outside the euro area also grew steadily. The outlook for the euro area has deteriorated slightly this year, however. This means that Finland's notional export demand will develop more weakly than the development of world trade. The euro area's share of exports is high, but the more favourable outlook for the United States and the emerging economies will be reflected in higher export demand. Exports, moreover, are currently still growing relatively quickly.

In goods exports, exports of means of transport have grown significantly in the early part of 2018 and export growth is expected to continue. Machinery and equipment exports are also developing favourably. In addition, investments already made in the forest industry will be fully reflected in exports during 2018. As with exports of goods, exports of services are continuing to grow – also to some extent more slowly compared with the previous year. Overall, services exports account for just under one third of exports, and this share is expected to remain unchanged during the forecast period.

According to the national accounts, the volume of imports grew more quickly than exports in the first quarter, 2.7%. Imports of goods were boosted by, among other things, imports of durable consumer goods and investment goods. Goods imports grew by 2.2% and service imports by 3.7%. In the forecast period, imports of goods will be boosted by imports of intermediate goods used by the export industry. On the other hand, growth of consumer goods imports in particular is steady.

Table 5. Foreign trade

	2015	2016	2017	2018**	2019**	2020**
	change in volume, %					
Exports of goods and services	0.9	3.5	7.8	4.9	4.0	3.2
Imports of goods and services	3.2	5.4	3.7	3.4	3.0	2.6
	change in price, %					
Exports of goods and services	-0.9	-1.8	2.9	2.1	1.9	1.5
Imports of goods and services	-4.3	-2.8	3.5	2.6	2.4	2.1

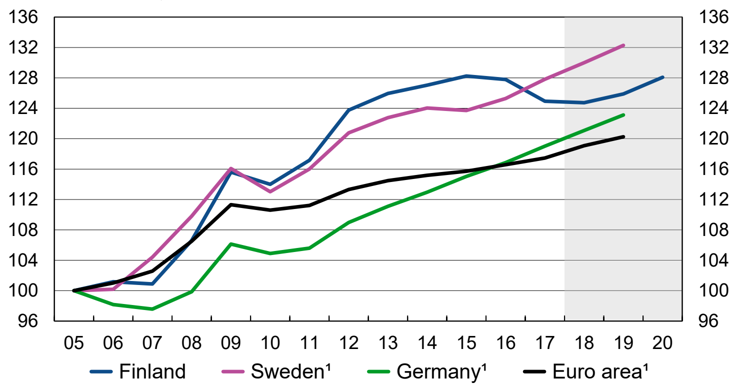
1.2.2 Prices and current account

Current account will remain in surplus

The price development of raw materials and oil used by industry will be reflected more strongly in increasing import prices in 2018. In the early part of 2018, the exchange rate of the US dollar exerted downward pressure on import prices, but as the forecast period progresses the dollar exchange rate will strengthen, which will again increase import prices. Both import and export prices will rise most quickly in 2018 and then more moderately in the coming years. Throughout the forecast period, the value of imports and exports will increase as a result of both volume growth and rising prices.

The terms of trade improved slightly in 2017, but in the forecast period the terms of trade will weaken because import prices will rise more than export prices. The weakening of the terms of trade will be moderate, however, because the price rise in raw materials imports will also be reflected in a rise in export prices. In the early part of the forecast period, conditions for exports will be further improved by trends in unit labour costs, which will be moderate compared with competitor countries, even though wages will rise. At the end of the forecast period, conditions for exports will improve due to the weakening euro.

Unit labour costs
2005=100, nominal



¹ European Commission forecast
Sources: European Commission, Statistics Finland, MoF
VM34170

Although the favourable rapid growth in world trade will create a better outlook for Finnish exports in the forecast period, Finland's notional export demand will increase more slowly than growth in world trade, in line with the more moderate growth of the euro area. Exports will grow in line with growth in world trade in 2018, but in 2019 export growth will be slower than growth in world trade. Exports will continue to be mainly goods-driven.

According to the latest data, the current account turned into a surplus of EUR 1.6 billion in 2017, driven by the trade balance, but the services balance remained in deficit. The current account will remain steadily in surplus throughout the forecast period, mainly due to the favourable development in the volume of net exports. In the forecast period, the deficit on the services balance is expected to narrow due to growth in services exports. The current account surplus, in turn, will be slightly reduced by export prices rising more quickly than import prices and by a deficit in factor incomes and income transfers.

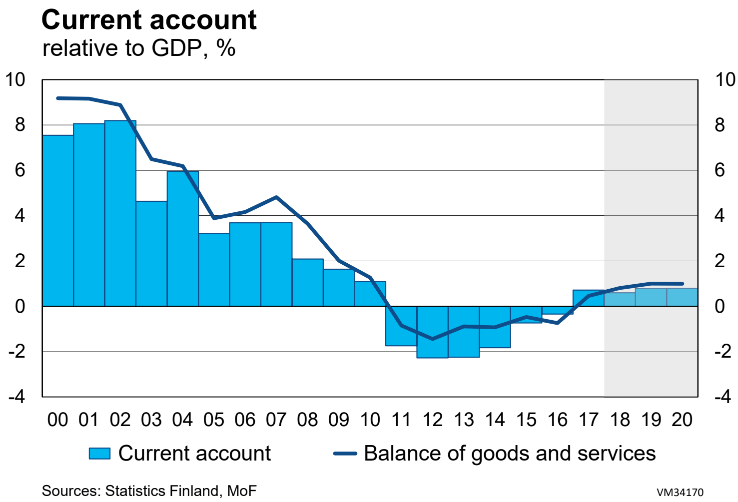


Table 6. Current account

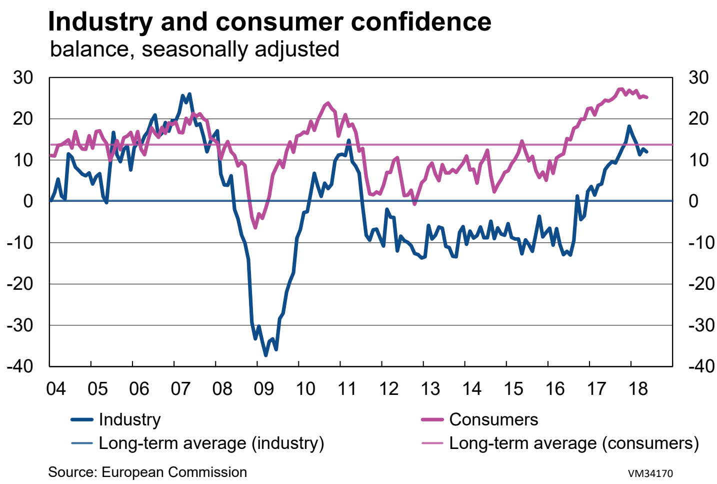
	2015	2016	2017	2018**	2019**	2020**
	EUR bn					
Balance of goods and services	-1.0	-1.6	1.0	1.9	2.4	2.5
Factor incomes and income transfers, net	-0.5	0.9	0.6	-0.5	-0.5	-0.5
Current account	-1.5	-0.7	1.6	1.4	1.9	2.0
Current account, relative to GDP, %	-0.7	-0.3	0.7	0.6	0.8	0.8

1.3 Domestic demand

1.3.1 Private consumption

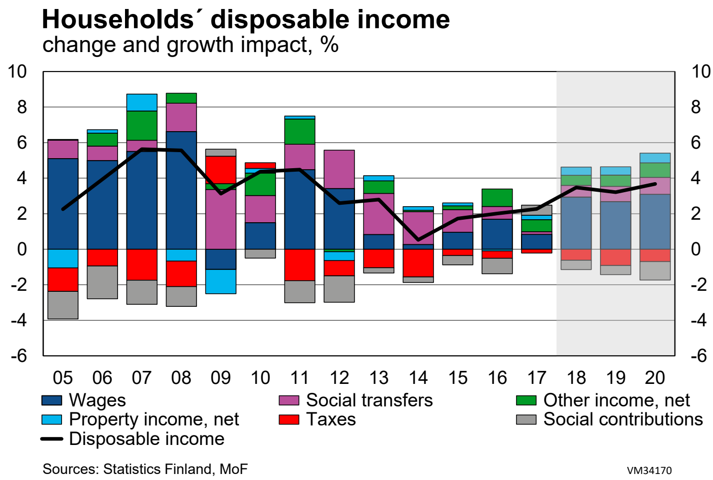
Employment will support consumption growth

Growth of private consumption will be supported by rising employment and earnings in 2018. Growth of the sum of wages and salaries will accelerate to 4%. Household disposable income will rise, but real income growth will be more moderate as inflation picks up. Growth of durable goods accelerated in the early part of the year and this growth remains the fastest of all the consumption categories. Consumption growth in all other categories will also accelerate year on year in 2018.

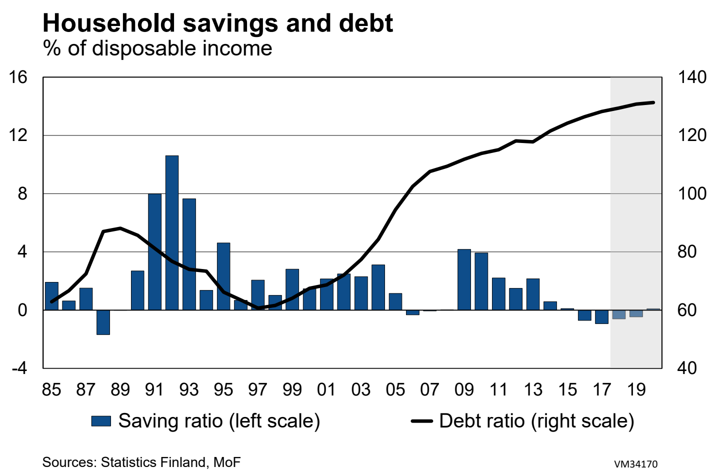


Growth of household disposable income will also be supported by growth of income transfers. Growth of pension income will support growth in disposable income as the improving employment situation slows growth of social transfers. Changes in taxation will continue to increase employees' purchasing power. The household savings rate will improve compared with 2017, but will still remain exceptionally low.

In 2019, growth of private consumption will be supported by rising earnings as well as an improvement in employment. The sum of wages and salaries will rise by 3.5% and keep growth of household disposable income above the level of recent years. In real terms, however, growth of household disposable income will slow as inflation picks up, which will curb growth of private consumption. The supporting impact of taxation on purchasing power will turn negative in 2019. Consumption growth will therefore slow, further improving the household savings rate.



In 2020, growth in the sum of wages and salaries will be most affected by the accelerating rise in the earnings level. The improvement in employment, although slowing, will also support growth of household purchasing power. Real income growth will be sluggish due to rising inflation, which will further slow down the increase in private consumption. The restoration of the savings rate closer to its historical average levels will also continue in 2020. Household indebtedness in ratio to disposable income will continue to grow. This trend will be supported by the low level of interest rates, the positive development of the labour market, easing of terms on new housing loans, a pick-up in the housing market and strong growth in residential construction. The problems of indebtedness will be heightened, however, when the level of interest rates rises in due course and households have to make hard choices about their other consumption.



1.3.2 Public consumption

The largest items of public consumption consist of personnel expenses and purchased goods and services. The public consumption to GDP ratio will fall slightly during the forecast period as public consumption expenditure grows more moderately than the value of GDP. Growth in the amount of public consumption will remain relatively slow in the coming years. Growth will be curbed in particular by the Competitiveness Pact and consolidation measures. The contribution of public consumption to growth in GDP volume will also fall from 0.4 percentage points in 2017 to 0.2 percentage points during the forecast period.

The price of public consumption will be impacted in 2018 and 2019 by, among other things, pay increases and a one-time productivity-based payment. In addition, the price will be raised in 2019 by the ending of the Competitiveness Pact holiday bonus cut.

Table 7. Consumption

	2017	2015	2016	2017	2018**	2019**	2020**
	share, %	change in volume, %					
Private consumption	100.0	1.7	1.7	1.7	2.0	1.6	1.4
Households	95.4	1.9	1.8	1.8	2.1	1.7	1.4
Durables	8.0	2.9	5.0	4.7	5.3	2.3	2.1
Semi-durables	7.7	1.0	1.2	2.3	3.1	1.1	0.9
Non-durable goods	25.7	0.7	0.9	1.0	1.1	1.4	1.2
Services	53.1	1.4	1.6	1.6	1.8	1.6	1.4
Consumption by non-profit institutions	4.6	-2.0	1.5	-1.0	0.0	0.5	0.5
Public consumption	100.0	0.2	1.5	1.6	0.7	0.4	0.9
Total		**1.3**	**1.7**	**1.6**	**1.6**	**1.2**	**1.2**
Individual consumption expendture in general government		0.9	1.0	1.6	0.9	0.4	0.7
Total individual consumption expenditure		1.5	1.6	1.7	1.2	1.1	1.4
Households´ disposable income		1.7	2.0	2.3	3.5	3.2	3.7
Private consumption deflator		0.3	0.9	0.9	1.1	1.4	1.7
Households´ real disposable income		1.4	1.1	1.4	2.4	1.8	2.0
		%					
Consumption as proportion of GDP (at current prices)		79.7	78.9	77.5	76.3	75.9	75.6
Household savings ratio		0.1	-0.7	-0.9	-0.6	-0.5	0.1
Household debt ratio[1]		124.2	126.4	128.2	129.4	130.7	131.3

1) Household debt at end-year in relation to disposable income.

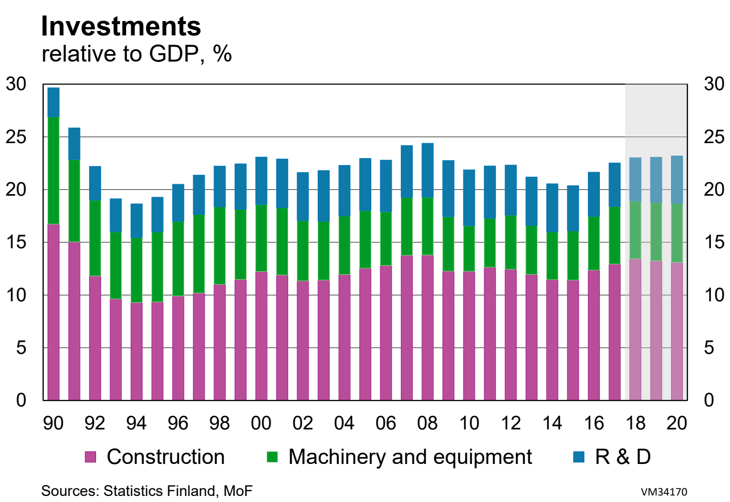
1.3.3 Private investment

Pace of investment will slow down

Private investment grew very strongly in the first quarter of the current year; both machinery and equipment investment and housing investment recorded up to double-digit growth figures. This year the level of investment will be high. There is an underlying shortage of capacity, which is reflected in industry and construction surveys. Investment growth is projected to slow significantly, however, in 2019. This is due, in particular, to a decline in the number of start-ups for new construction projects. In addition, investment decisions for major forest industry projects have been moved forward. The growth impact of investment on GDP will therefore fall short of the previous forecast.

Private investment is projected to grow by nearly 5% this year, by around 2% in 2019 and by around 3% in 2020. Growth in 2020 will be boosted by the start-up of already planned major projects. In 2020, the ratio of private investment to GDP will rise to around 19½%. The rate of investment will climb quickly, but as matters stand it would still, at the end of the forecast period, fall short of the corresponding rate in 2008.

Investment in housing has grown continuously for over three years. This year, growth will continue to be strong because the good employment trend and low interest rates are supporting household housing demand. The indicator of the sup-

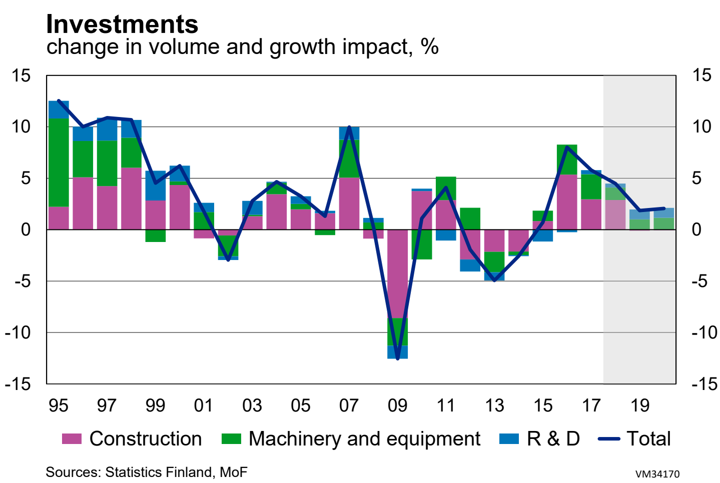


ply of new housing has also declined further. Investor demand, on the other hand, is becoming more uncertain, and particularly in smaller localities rapid changes in demand are possible.

This year and next, housing starts, which have risen to a high level, will decline by a few thousand per year and this will be reflected fairly quickly in investment figures. There is wide regional variation in construction, however. In the Helsinki Metropolitan Area, housing starts are expected to remain at a high level throughout the forecast period.

The number of building permits for non-residential building construction projects has fallen in the early part of the year by over 20%. Due to long construction times, it is expected that the coming decline in the start-up of business, warehouse, hospital and retail premises projects will not, however, be reflected in investment until next year. The outlook for 2020 is already better due to several already planned major projects. The probability of these major projects being implemented has risen because a number of the projects have already been granted environmental and building permits.

Investment in repair construction is projected to remain quite stable and to grow during the forecast period at an annual rate of around 2%. Repair construction in housing is expected to be livelier than in non-residential buildings.

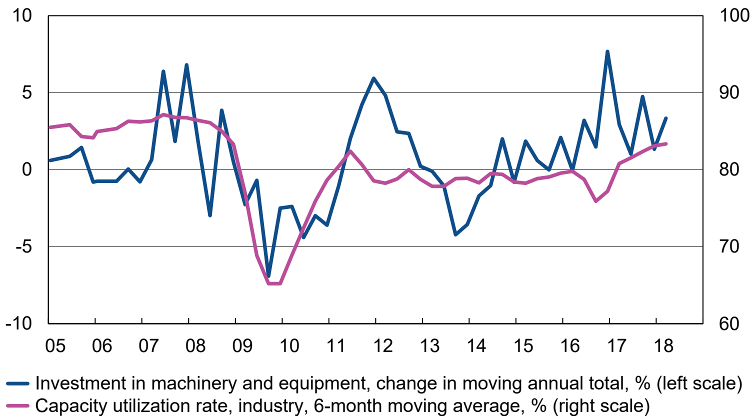


Civil engineering investment is expected to grow by 2½% this year and next. Growth is projected to slow down to just under 2% in 2020. Only around one third of structures and land improvements constitutes private-sector investment.

Investment in machinery, equipment and transport equipment is expected to continue to grow, because economic growth is good, there is a shortage of capacity, and growth expectations in the service sector, in particular, have strengthened. The service sector will account for more than half of this investment. According to industry estimates, industry's investment in equipment will fall this year because many large projects were completed last year. Next year, economic growth will continue to support investment in equipment, but at a level lower than now. Major projects planned in the longer term may increase Finland's machinery and equipment investment significantly.

Investment in research and development fell slightly in the early part of the year, and growth for this year is expected to remain at a few per cent. Next and the following year, however, investment in research and development is projected to strengthen in line with earlier expectations and to grow at an annual rate of around 5%.

Investment and capacity utilization rate



Source: Statistics Finland, Confederation of Finnish Industries VM34170

Table 8. Fixed investment by type of capital asset

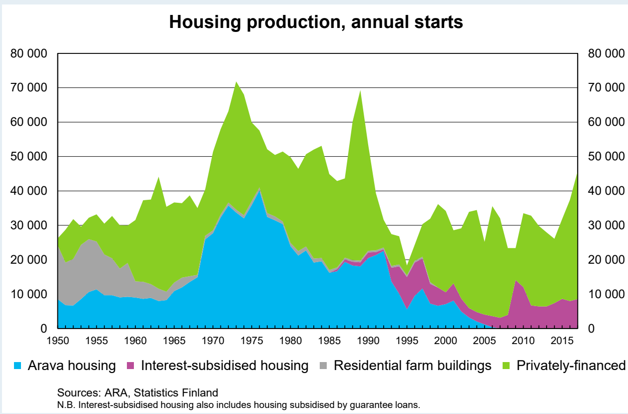
	2017	2015	2016	2017	2018**	2019**	2020**
	share, %	change in volume, %					
Buildings	47.8	2.0	9.7	5.8	5.5	-0.7	-0.5
Residential buildings	28.6	2.0	10.3	5.5	7.1	-0.5	-2.5
Non-residential buildings	19.2	2.1	8.8	6.4	3.2	-1.0	2.8
Civil engineering construction	9.6	-0.8	9.1	2.0	2.5	2.5	1.7
Machinery and equipment	24.2	4.6	12.7	10.4	5.0	4.2	4.8
R&D-investments1	18.4	-5.2	-1.2	2.0	2.1	5.4	5.2
Total	**100.0**	**0.7**	**8.0**	**5.8**	**4.5**	**1.9**	**2.1**
Private	82.8	2.2	8.2	8.1	4.8	1.9	2.9
Public	17.2	-5.2	7.4	-4.3	3.2	1.8	-1.8
		%					
Investment to GDP ratio (at current prices)							
Fixed investment		20.4	21.6	22.5	23.0	23.1	23.2
Private		16.5	17.6	18.7	19.1	19.2	19.4
Public		3.9	4.1	3.9	3.9	3.9	3.8

1) Includes cultivated assets and intellectual property products

SUBSIDISED HOUSING PRODUCTION NOW INCREASING THE PRICE OF CONSTRUCTION

The government subsidises housing production in many different ways. The main forms of subsidy are interest subsidies and guarantees granted for the construction of rental housing and right-of-occupancy housing. The government also subsidises the construction of privately-financed rental and owner-occupied housing through guarantees. The government's housing-related liabilities have increased to about EUR 18 billion.

Since 2011, an average of 7,000 government-subsidised dwellings (so-called ARA housing) have been built annually. ARA production has been increased even though privately-financed housing production has also grown in recent years at a rather rapid pace. The increase in housing production has been a long-term target, because housing has been scarce in the Helsinki Metropolitan Area and also to some extent in other growth centres.

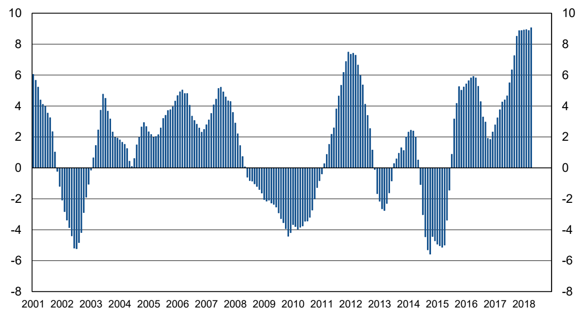


The economic cycle in construction is strong and the construction companies' capacity is almost fully utilised. This is evident, for example, in the fact that the recruitment problems of construction companies have increased (e.g. Confederation of Finnish Industries, May 2018). The tender prices for new construction have increased by an annual growth rate of almost 10% since the end of last year. This has also been evident in the low interest of construction firms in ARA production and in strongly increasing project costs. In April 2018, the annual change in the price of ARA production in the Helsinki Metropolitan Area was already more than 12%.

Keeping ARA production at a high level now will at the same time strengthen the boom because ARA production competes for the same production factors as other construction, thus increasing the prices of new construction. On the other hand, ARA production will probably also displace privately-financed housing production. According to an empirical study by Elias Oikarinen (VN TEAS 9/2018), ARA production displaces privately-financed housing production by 40%. The effect of this displacement means that, when the government grants funding to ten ARA dwellings, four privately-financed dwellings do not get built. Although the study did not investigate how great the displacement effect is in a different cyclical situation, it is logical to assume that it will be greater during a period of economic upswing because of limited resources and greater demand than in an economic downturn.

The ARA projects approved during favourable economic conditions will also increase the government guarantees relatively more than production carried out in a downturn because, when capacity is released during a downturn, prices tend to fall. Correspondingly, the starting rents of ARA housing will increase to a relatively

Residential construction tender price index sliding annual change, %



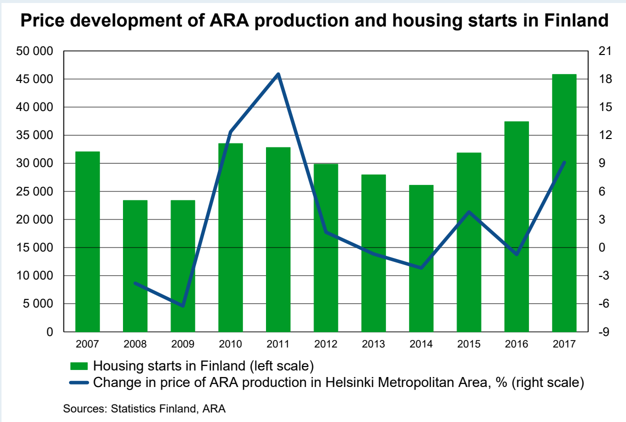
Source: Rapal; index concerns projects in the Helsinki Metropolitan Area

high level. In addition to growth in costs and risks to central government finances, in extreme situations ARA production may also even disturb the stability of the housing market. There is also reason to note that the government guarantees that enable ARA production are not evident in traditional fiscal policy indicators.

One reason for the increase in state-subsidised production has been the MAL (land use, housing and transport) agreements concluded by the state and the largest urban regions. In these, it has been agreed that part of the housing production planned by the municipalities will be built as state-subsidised housing production. Implementation of MAL agreements irrespective of the economic cycle increases pressure on the prices of subsidised housing production. The Housing Finance and Development Centre of Finland (ARA), however, does not accept all offers, so it does try to stabilise the situation.

In possible future MAL agreements, it might be sensible to adjust production requirements according to the economic cycle. The agreements could take into account the general economic situation, so that the state would not increase the price level of housing production by its own actions. The figure below illustrates that the price of ARA construction rises in favourable economic conditions and with housing production increasing.

ARA production is more influential if it is carried out counter-cyclically, in other words when market production is otherwise low. ARA production then balances the economic cycles. Although adjusting production completely to the cyclical situation is impossible, evaluation of the situation and direction of economic development is already an adequate way of avoiding the most violent peaks and troughs in prices. Furthermore, the government guarantees granted to non-regulated rental housing production in particular could be adjusted according to the economic cycle.



Moreover, the results of the VN TEAS project should be applied in the resident selection of A-Kruunu, a company that is wholly state-owned and will probably in the near future receive further capitalisation of EUR 50 million. According to research, the better the housing is targeted at the less wealthy and those on low incomes, the less the impact of displacement, because the less wealthy and lower earners naturally have poorer opportunities than the well-off to purchase a privately-financed rental or owner-occupied dwelling.

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1.3.4 Public investment

Local government investment accounts for more than half and central government investment for less than half of public investment. Social security funds represent a very small share of the total. Due to the counties to be established in 2020, the rate of local government investment among total public investment will fall back to below 50%.

The largest items of public investment will be civil engineering investment (30%), other construction investment (30%) as well as research and development investment (25%). The GDP share of public investment will remain close to the long-term average of approximately 4%, although the shares of subsectors will vary. The level of public investment will remain high due to such factors as a brisk rate of hospital construction, investments in the government's key projects and transport route repairs as well as the counties' ICT system development.

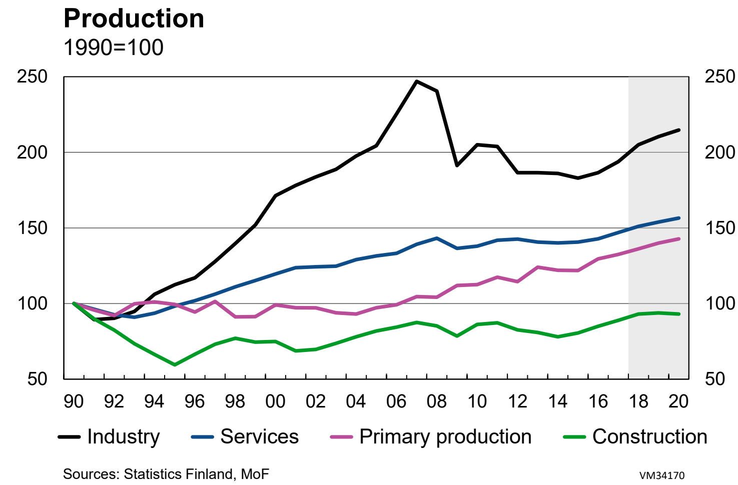
1.4 Domestic production

1.4.1 Total output

Economic growth will continue at a gradually slowing rate

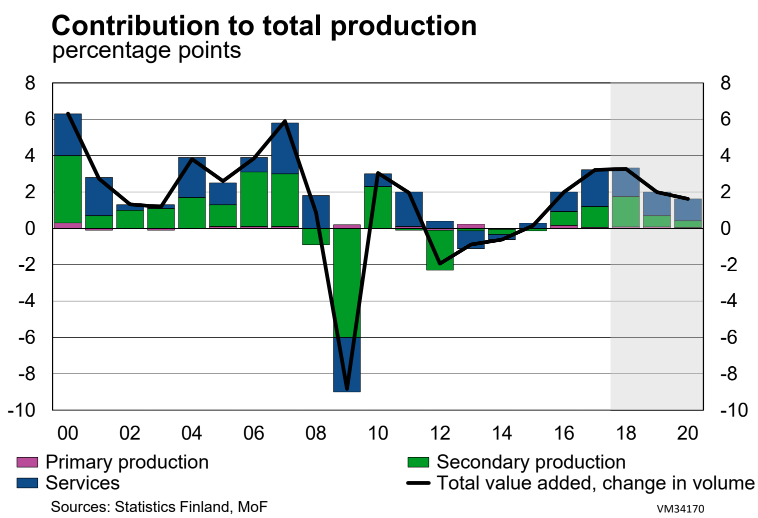
Growth in production accelerated at the beginning of the year. Gross value added for the economy was 2.8% greater in January–March than a year earlier. The level of gross value added is still 1½% lower, however, than before the financial crisis as industrial output still remains at a clearly lower level. Production in all the main sectors was greater in the early part of this year than a year earlier. The greatest increase was in the output of secondary production, i.e. industry and construction. Value added in primary production – agriculture and forestry – was just 0.1% greater than last year. Value added in the forest industry and the financial and insurance sectors was less than a year earlier.

The upturn in the economy is expected to continue this year, as the order book of industrial companies is strong, investment in major construction projects is continuing and sales expectations in the service sector have risen. On the other hand, there are signs of constraints on growth, as the value of new orders in manufacturing decreased in January–March compared with the end of last year, many workplaces are



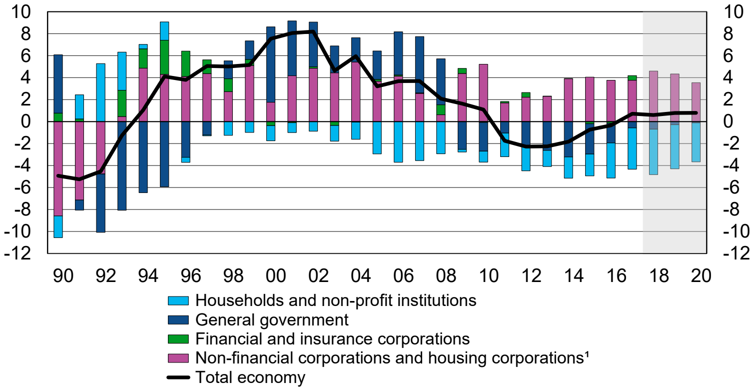
suffering from a lack of skilled labour and some also of capacity and, in many private business sectors, obstacles to growth are more common than at the end of last year.

Despite obstacles to output growth, economic activity will remain strong across the board. Growth is being driven by a large order book illustrating strong international demand in manufacturing, progress made in numerous private and public construction projects already started, and strong demand for services. Although the period of fastest growth seen in early 2018 appears to be over, the business tendency surveys of the Confederation of Finnish Industries (EK) indicate that the positive trend will still continue, at least for the next six months. In addition, the outlook's back-



ground assumptions concerning the continuation of the growth of world trade and the global economy support export-oriented industrial production and therefore, indirectly, business services. The growth in imports of Finland's most important trading area, Europe, is good news for Finnish industries manufacturing investment and intermediate products. Due to broad-based growth and strong momentum, gross value added for the economy will grow by more than 3% this year. The growth rate will slow down in 2019 and 2020, but total output will still increase by around 2% per year during those years.

Net lending by sector
relative to GDP, %



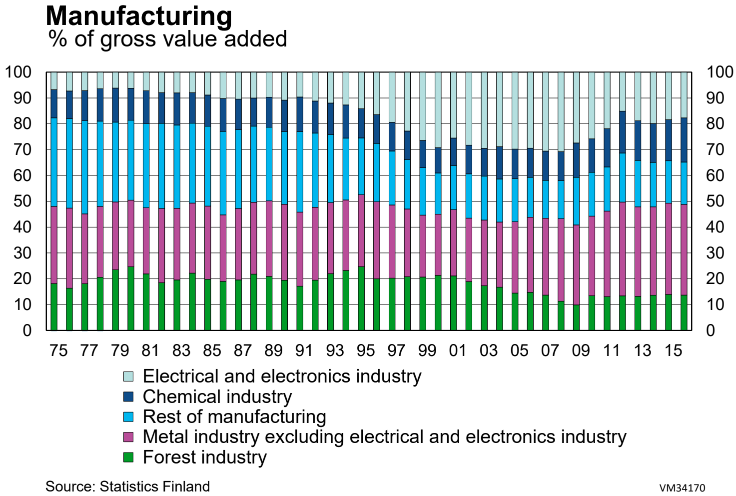
1) Including financial sector in 2018-2020
Sources: Statistics Finland, MoF

1.4.2 Secondary production

Manufacturing output undergoing broad-based growth

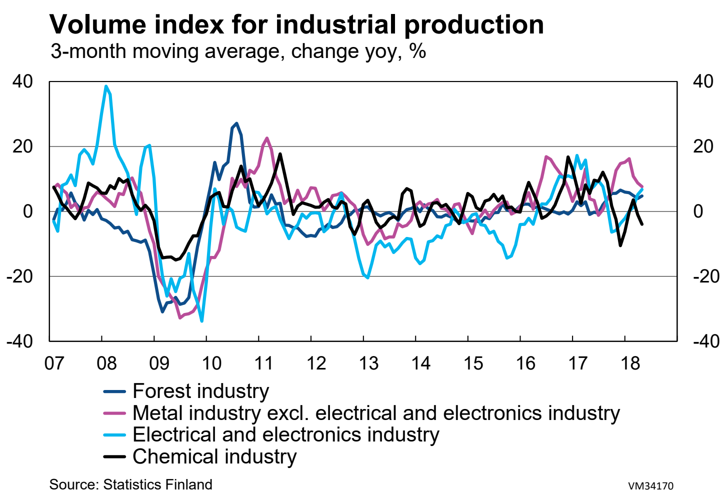
The upturn in manufacturing output continued in the early part of the year and value added in the sector increased by 4.3% from a year ago. The upswing was broad-based, even though forest industry output decreased partly as a result of challenges related to production factors. By contrast, growth in the output of technology manufacturing accelerated, boosted by increased demand over last year. Cold weather in the early part of the year also increased energy industry output.

Most of Finland's industrial production comprises raw materials and investment goods for export, the demand for which has improved as the global economy and trade have picked up and capacity utilisation has been increased by economic growth. In addition, the unit labour cost competitiveness of Finnish businesses improved last year as



the nominal cost of labour per unit of output in the economy as a whole decreased by more than 2% last year. The order book of manufacturing companies is also very strong, particularly in the forest and construction sectors, and guarantees average production for months ahead.

Business tendency surveys indicate that the best potential for growth in the coming months lies in the technology, building product, forest and food industries. The weakest expectations for output are in the textile and clothing, printing and chemical industries. In the forest industry, output is being pushed up by increased demand for pulp, paperboard and sawn timber. Increases in capacity are also supporting growth in the forest industry. Overall, industrial output will increase by around 6% this year due to the positive economic outlook and strong order book.



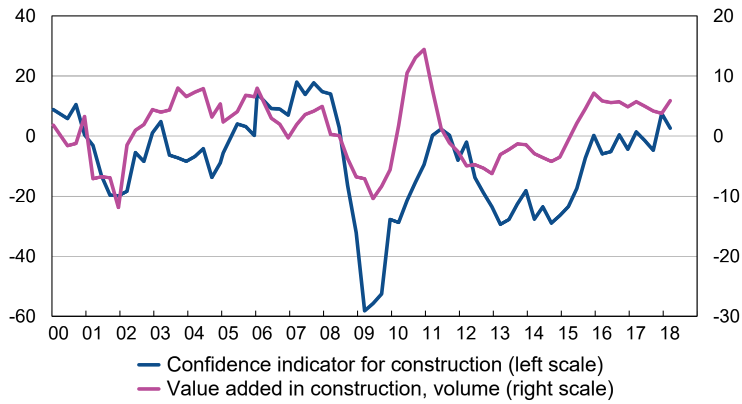
In the coming years, export demand will increase as global trade grows, albeit at a slowing rate. Imports are expected to increase in 2019 and 2020, particularly in the European market important to Finnish companies. Increased production capacity and efforts made by enterprises to improve the competitiveness of their products will boost industrial output in the years ahead. The growth of value added in manufacturing will be around 2½% next year but will slow to 2% in 2020. Despite this growth, the volume of industrial output will still remain almost one-sixth lower in 2020 than in the peak year of 2007.

End of the growth of construction looming

The growth rate of value added in construction accelerated to 6.6% in the early part of the year. Growth was supported by strong housebuilding, while civil engineering construction contracted in the winter. Housebuilding was strong, particularly in residential, commercial and office construction projects. This was influenced by increased housing demand in growth centres, municipal investments in health care and educational facilities and projects to expand and replace the capacity of enterprises. Growth is regionally unbalanced, however, because levels of new construction are higher in growth centres than outside them. The need for repair construction is high, particularly as regards residential and office buildings.

According to surveys, the economic prospects for construction have not risen during the early part of the year, as the growth in output has continued strongly for more than three years. The number of building permits has also taken a downturn. Many

Confidence and production in construction
seasonally adjusted balance and change yoy, %



Sources: Statistics Finland, European Commission

VM34170

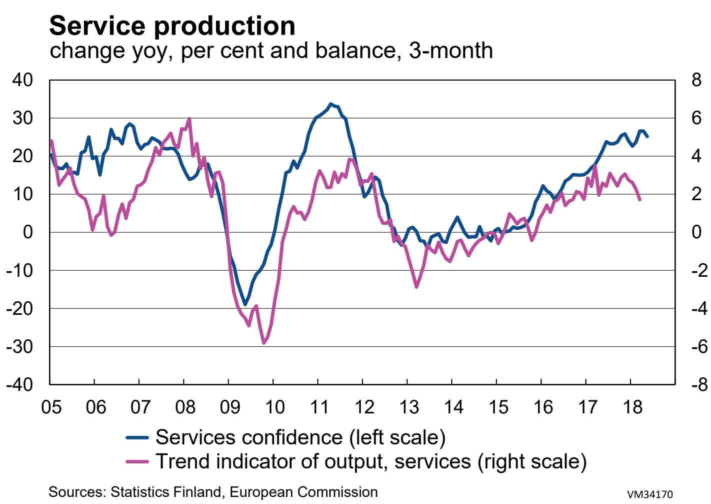
major construction projects are being completed this year, some of which are one-off in nature, so no similar new construction will immediately emerge to take their place. The level of production is high and capacity is almost in full usage. In addition, construction is the main industry suffering from the greatest shortage of skilled labour. Supported by ongoing construction projects, output in the construction sector will continue to increase this year by almost 5%, but construction will no longer be the fastest growing sector in the economy.

Construction will remain buoyant in growth centres in both 2018 and 2019, but the number of new starts will no longer increase as much as in recent years, further slowing down the pace of construction. In the 2019–2020 period, the focus will be on a few major new construction projects and on repair construction, so next year construction value added will increase by less than 1%, and will start to fall in 2020.

1.4.3 Services

Broad-based growth in services

Service production has increased constantly for three years and growth in the early part of the year still exceeded 2%. Value added for services increased rapidly in the private sector but hardly at all in the public. Business services increased most strongly, with the exception of the financial and insurance sectors. Sales of consumer services also increased as purchasing power improved.



The cyclical position of private services is strong. Sales are on the increase and are generally expected to continue to grow in the coming months. Lack of demand is troubling companies in the service sector less than before. Instead, the supply of skilled labour is a greater obstacle to growth than before in the service sector, particularly in ICT and property service companies. Nevertheless, companies in these sectors still expect growth to accelerate over the summer. The increase in value added in services this year will exceed 2½% year on year.

In future, service production will be supported by demand in other sectors and the positive development of income, so there is still good potential for growth in service sectors. International demand will increase service production serving foreign demand and, through intermediate products, also domestic service production. Limits on growth will, however, begin to be encountered more clearly, and economic development will slow after a long period of growth. Next year and the year after will see only a slight slowdown in service production growth from this year, with the coming annual growth rate averaging just under 2%.

Table 9. Production by industry

	2017	2015	2016	2017	2018**	2019**	2020**	Average
	share, %1)	change in volume, %						2017/2007
Industry	20.7	-1.7	1.9	3.9	5.9	2.6	2.0	-2.4
Construction	7.1	3.3	5.5	4.6	4.8	0.8	-0.8	0.2
Agriculture and forestry	2.8	-0.1	6.3	2.3	2.9	2.8	1.9	2.4
Industry and construction	27.8	-0.5	2.8	4.1	5.8	2.2	1.3	-1.9
Services	69.4	0.4	1.5	2.9	2.7	1.9	1.7	0.5
Total production at basic prices	**100.0**	**0.1**	**2.0**	**3.2**	**3.3**	**2.0**	**1.6**	**-0.2**
GDP at market prices		0.1	2.3	2.7	2.9	1.8	1.7	-0.0
Labour productivity in the whole economy		0.2	1.7	2.5	1.3	1.0	1.0	0.1

1) Share of total value added at current prices.

1.5 Labour force

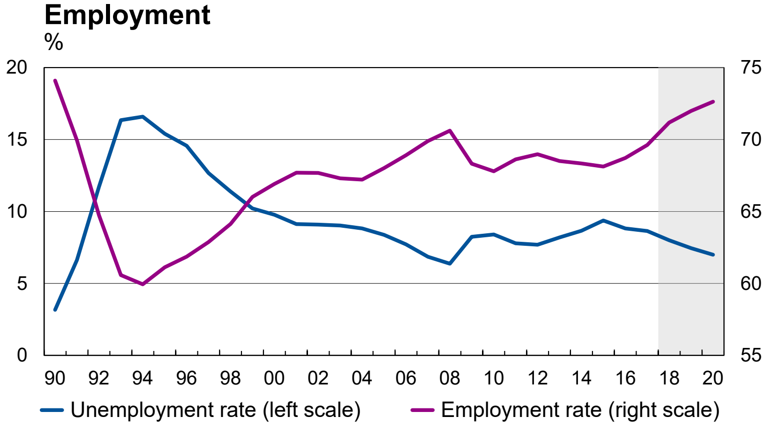
Unemployment to fall on all indicators

The good trend in economic activity has maintained growth in employment since the beginning of 2018. According to Labour force survey, the number of employed people increased in the period January–April by 2.4% in comparison with the previous year. Working hours have increased in the same proportion. Since the beginning of the year, the trend employment rate has remained at around 71%.

The demand for labour has continued to improve. According to Statistics Finland, the number of job vacancies increased by 4% in the first quarter of the year. New job vacancies reported to Employment and Economic Development Offices in the early part of the year were more than 20% higher than a year earlier. According to the European Commission's confidence indicators, in April Finnish enterprises' employment expectations were at their highest since 2011. Measured by the job vacancy rate, however, demand for labour in Finland was only at the medium level among EU Member States.

Strongly sustained economic growth and increased demand for labour will increase the number of employed in 2018 by 1.9% compared with the previous year, and the employment rate will rise to 71.2%.

Employment



Unemployment rate = Unemployed / Labour force (15-74 yrs)
Employment rate = Employed / Population of working age (15-64 yrs)

Sources: Statistics Finland, MoF VM34170

Since the beginning of the year, unemployment has clearly fallen according to both Labour force survey by Statistics Finland and Employment service statistics from the Ministry of Employment and the Economy. The trend unemployment rate fell in April to 8.0%. Powered by the rapid growth in employment, the number of unemployed people will decrease this year by more than last year. The projected unemployment rate for 2018 is 8.0%.

The reasonably fast continuous growth in GDP and a low to moderate growth in real incomes will maintain demand for labour during the forecast period. Due to a large number of the unemployed and disguised unemployed together with recent policy measures increasing the supply of labour, the supply of labour in the economy as a whole is not yet limiting growth in employment and the economy. The number of employed people will increase by 1.0% in 2019 and 0.7% in 2020. The employment rate will increase to 72% in 2019 and 72.6% in 2020.

Large numbers of the disguised unemployed and the structurally unemployed are still slowing the decrease in unemployment. The number of unemployed people is therefore anticipated to remain quite high for the entire forecast period, in spite of stronger economic growth. The unemployment rate will fall to 7.5% in 2019 and further to 7% in 2020.

According to the Employment Service Statistics compiled by the Ministry of Economic Affairs and Employment, the number of unemployed and long-term unemployed has decreased swiftly since 2017 in all age groups. Part of this decrease, however, is simply due to register information being corrected. As a result of strong economic growth and good demand for labour, the number of long-term and structurally unemployed can be expected to decrease further in the coming years.

Although the supply of labour in the Finnish economy on the whole is sufficient, sectoral labour shortages can already be detected in certain occupational groups. According to the Business Tendency Survey of the Confederation of Finnish Industries (EK) and the Employment Outlook by Occupation published by the Ministry of Economic Affairs and Employment, there is a particular shortage of construction and real estate service professionals as well as information, health and social services experts.

Elimination of sectoral labour shortages can be promoted by investing in skills, education and training, improving incentives for employment and increasing labour immigration. Ultimately, sectoral labour shortages will lead to higher pay levels in the affected industries.

Table 10. Labour market

	2015	2016	2017	2018**	2019**	2020**
	annual average, 1.000 persons					
Population of working age (15-74 yrs)	4102	4109	4114	4127	4138	4140
change	6	7	5	14	11	2
Population of working age (15-64 yrs)	3476	3463	3451	3441	3436	3429
change	-15	-13	-12	-10	-5	-7
Employed (15-74 yrs)	2437	2448	2473	2521	2546	2564
of which 15-64 yrs	2368	2379	2403	2449	2473	2491
Unemployed (15-74 yrs)	252	237	234	220	205	193
	%					
Employment rate (15-64 yrs)	68.1	68.7	69.6	71.2	72.0	72.6
Unemployment rate (15-74 yrs)	9.4	8.8	8.6	8.0	7.5	7.0
	1.000 persons per annum					
Immigration, net	12	16	17	17	17	17

1.6 Incomes, costs and prices

1.6.1 Wages and salaries

In 2017, earnings development was predominantly determined by the Competitiveness Pact concluded by the social partners. According to preliminary data, the index of wage and salary earnings increased by 0.3%. In the economy as a whole, the sum of wages and salaries increased by 2.6% in 2017.

Negotiations on pay rises for 2018 and 2019 have taken place on industry level. Negotiated pay increases have mainly followed the line set by the technology industry. Nominal earnings are expected to increase by 1.8% in 2018 and by 2.6% in 2019. Wage drifts are forecast to remain slightly below average because of increased local bargaining possibilities and company-specific items.

The sum of wages and salaries in the economy is projected to grow by 4.0% in 2018 and 3.5% in 2019.

In 2020, nominal earnings are projected to increase by 2.8% and the sum of wages and salaries by 3.5%. Rises in earnings will be boosted by the expiry of public-sector holiday bonus cuts.

In the years ahead, the rise in the level of earnings will continue to be slower than the average rise seen in the 2000s, which is in line with the high rate of unemployment.

Table 11. Disposable income

	2017	2015	2016	2017	2018**	2019**	2020**	Average
	share, %	change, %						2017/2007
Compensation of employees	56.7	1.1	1.6	0.9	3.2	2.9	3.4	2.0
Wages and salaries	46.6	1.0	1.4	2.6	4.0	3.5	3.5	2.2
Employers' contributions to social security schemes	10.1	1.4	2.5	-6.1	-0.5	0.2	2.8	0.9
Property and entrepreneurial income, net	27.8	7.2	8.8	11.4	6.2	5.3	4.4	0.9
Taxes on production and imports minus subsidies	15.5	-0.1	5.7	1.6	3.3	2.9	2.1	3.1
National income	100.0	2.3	4.2	3.7	4.1	3.6	3.5	1.8
Disposable income		2.4	4.3	4.0	4.1	3.7	3.5	1.8
Gross national income, EUR bn		211.5	219.2	226.8	235.8	244.1	252.4	

Table 12. Index of wage and salary earnings and labour costs per unit of output

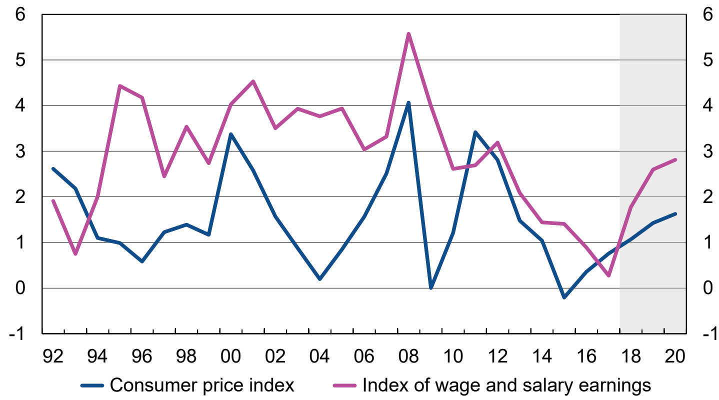
	2015	2016	2017	2018**	2019**	2020**	Average
	change, %						2017/2007
Index of negotiated wage rates	0.7	0.6	-0.3	1.2	2.0	2.1	1.8
Wage drift, etc.	0.7	0.3	0.6	0.6	0.6	0.7	0.7
Index of wage and salary earnings	**1.4**	**0.9**	**0.3**	**1.8**	**2.6**	**2.8**	**2.5**
Real earnings[1]	1.6	0.5	-0.5	0.7	1.2	1.2	1.1
Average earnings[2]	1.4	0.8	0.6	2.1	2.5	2.9	2.2
Labour costs per unit of output whole economy[3]	0.9	-0.4	-2.2	-0.1	0.9	1.7	2.3

1) The index of wage and salary earnings divided by the consumer price index.
2) Computed by dividing the national wage bill by the number of hours worked by wage and salary earners. The figures are affected by structural changes in the economy.
3) Compensation of employees divided by gross value added in volume at basic prices.

1.6.2 Consumer prices

Consumer prices are continuing to increase slowly. In the first quarter of 2018, the national Consumer Price Index rose by 0.7% compared with the previous year. Inflation was therefore as high as in 2017. Since the beginning of the year, rises in the prices of sub-items of services and foodstuffs has caused the inflation. The energy sub-item hardly affected inflation in the early part of 2018, but its effects will be felt more clearly later in 2018. Inflation is also expected to increase slightly towards the end of 2018 and in 2019. This is because the economy has fewer and fewer free resources, among other reasons.

Consumer price index and index of wage and salary earnings
change yoy, %



Sources: Statistics Finland, MoF VM34170

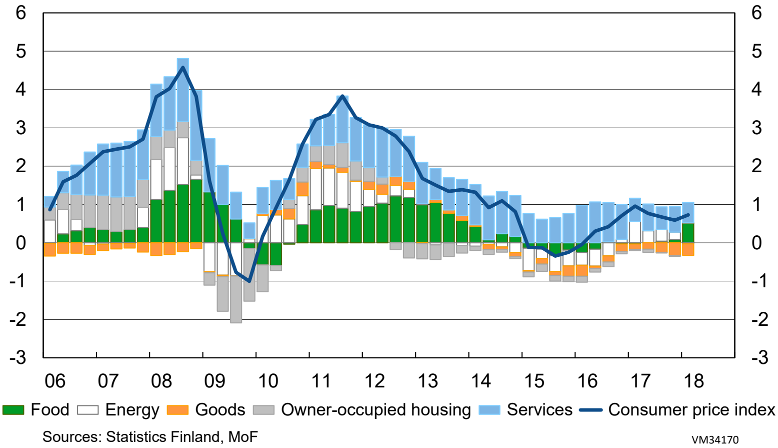
The inflation forecast for the current year is 1.1% as measured by the national Consumer Price Index. This year rises in prices of services, food and energy will be the chief causes of rising inflation. The effect on inflation of the prices of goods will remain negative this year. Changes in indirect taxes in 2018 will drive inflation by an estimated 0.3–0.4 percentage points.

The price of crude oil has risen significantly since last summer. Energy prices are expected to rise compared with last year, particularly in summer 2018. The weakening of the dollar clearly held back the rise in the price of oil up to the beginning of 2018, but the dollar's strengthening in recent months is now contributing to its advance. Import prices are continuing to increase, but the rise is steadier than before. This year, this will particularly affect the prices of goods, which are expected to fall less than last year.

As the level of earnings rises, the prices of services are expected to gradually increase. The increase will, however, remain moderate this year – this year, the prices of services are expected to increase by 1.1%, which is even slower than last year. This is due to factors including lowered day care charges. In 2018, falling prices have also been evident, in bus and particularly in train transport. On the other hand, increases in excise duties on alcoholic beverages and tobacco products will have a significant accelerating impact on inflation this year. Food prices are also projected to take an upturn during the current year.

Consumer price index

percentage change and contribution to change



Sources: Statistics Finland, MoF

Inflation pressure will remain moderate, but will rise slightly in the coming years of the forecast period, because the economy will have fewer free resources as the output gap closes and becomes positive. The national Consumer Price Index is forecast to increase by 1.4% in 2019 and 1.6% in 2020. The increase in service prices is projected to accelerate gradually during the forecast period as the earnings level rises. The oil price that is assumed to rise slowly during the forecast period and assumptions of the dollar's continued strengthening will also support inflation in 2019 and 2020.

Inflation in the euro area has slowed slightly, despite stable economic growth in the area. In the first quarter of 2018, euro area inflation was 1.2%. This is lower than in the corresponding period last year when it was 1.5%. Based on expert assessments in March by the European Central Bank, inflation in the euro area is expected to be 1.4% this year, 1.4% in 2019 and 1.7% in 2020. Comparable growth figures from the Harmonised Consumer Price Index in a forecast for Finland by the Ministry of Finance are 1.1% to 2018, 1.4% to 2019 and 1.6% to 2020. Finnish inflation in 2017 was clearly lower than the rate seen in the euro area, but it is projected to accelerate this and next year to a level closer to the average for the euro area.

Table 13. **Price indices**

	2015	2016	2017	2018**	2019**	2020**	Average
	change, %						2017/2007
Export prices[1]	-0.9	-1.8	2.9	2.1	1.9	1.5	0.3
Import prices[1]	-4.3	-2.8	3.5	2.6	2.4	2.1	0.3
Consumer price index	-0.2	0.4	0.7	1.1	1.4	1.6	1.6
Harmonised index of consumer prices	-0.2	0.4	0.8	1.1	1.4	1.6	1.8
Basic price index for domestic supply, including taxes	-2.7	-1.2	4.9	3.5	2.5	2.3	1.6
Building cost index	0.5	0.5	0.3	1.9	2.0	2.1	1.7

1) As calculated in the National Accounts

2 Public finances

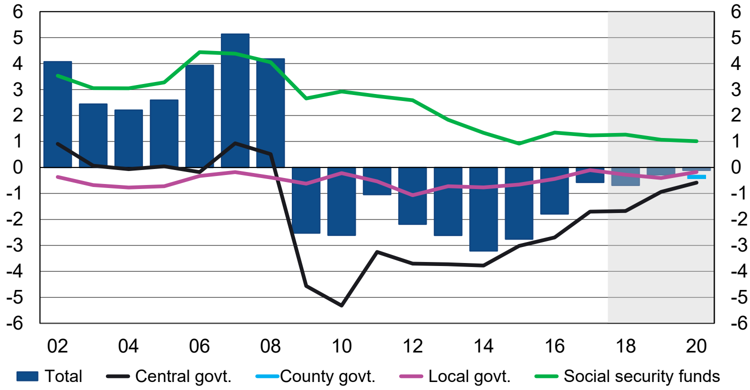
2.1 General government finances

The Finnish economy has clearly returned to a positive stance, and the deficit in general government finances has decreased in recent years as a result of economic growth. Consolidation measures decided on by the Government have also strengthened the financial position. As the good economic cycle continue, the development of the financial balance will continue in similar way in the coming years, and public finances will almost be balanced towards the end of the forecast period. Public debt in ratio to GDP will continue to fall. This year it stands at 60%.

As the next decade approaches, public finances are nonetheless in a fragile state. This is because indebtedness will continue in nominal terms despite the economic upswing, and the level of debt will still be at a high level as the next downturn dawns. Structural factors encumbering public finances will continue to create pressure on public finances in the 2020s. In the coming decade, the greatest growth pressure will be on health care and long-term care expenditure as the population ages.

Of the subsectors of general government finances, central government will be most in deficit. Local government will also continue to run a slight deficit. County government, which will begin in 2020, will also be in deficit. The county government deficit will be largely due to the hospital districts' many premises investments decided on earlier, which will be transferred to the Counties' Service Centre for Facilities and Real Estate Management. The total deficit of central government, county government and local government will be almost EUR 3 billion by the end of the forecast period. The surplus of employment pension institutions will remain a little under 1% in relation to GDP. The good economic conditions will strengthen the development of income from contributions and financial position of employment pension institutions, but the increase in pension expenditure stemming from structural causes will have an opposite effect.

The financial balance of general government
relative to GDP, %



Sources: Statistics Finland, MoF
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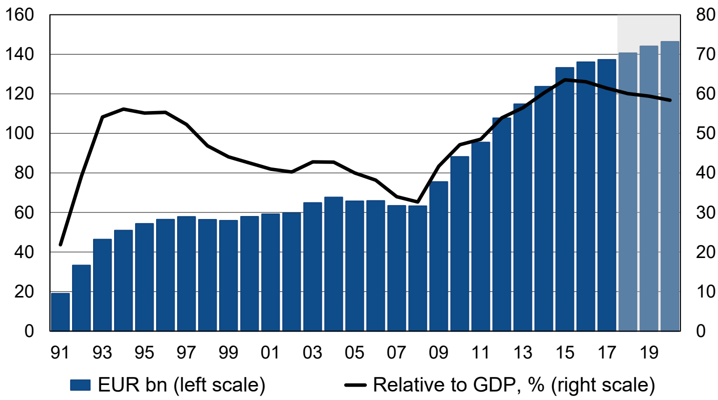
General government debt



Sources: Statistics Finland, MoF
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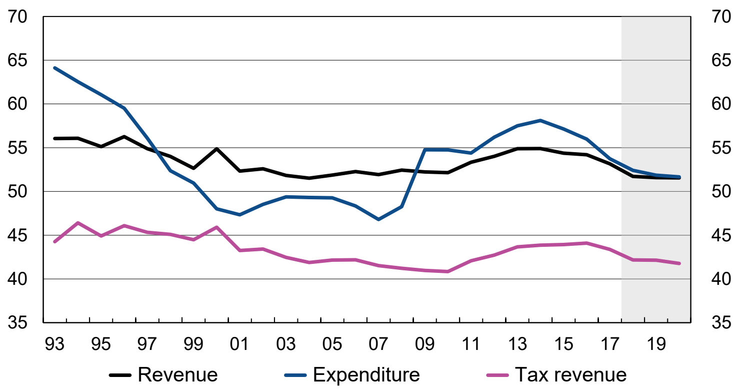
General government revenue, tax revenue and expenditure
relative to GDP, %



Sources: Statistics Finland, MoF
VM34098

The expenditure rate, i.e. the ratio of expenditure to GDP, is set to fall in the forecast period. A moderate rise in expenditure in the state budget will keep growth in expenditure slow. The tax rate, i.e. the ratio of taxes and tax-like payments to GDP, fell last year. The most significant reason for this was the Competitiveness Pact and related tax cuts. At the beginning of this year, the taxation of labour was further reduced, as was the unemployment insurance contribution. The tax rate will fall this year and remain more or less at the same level in the coming years.

Table 14. General government finance[1)]

	2015	2016	2017	2018**	2019**	2020**
	EUR billion					
Current taxes	34.8	35.6	37.2	37.7	39.6	40.5
Taxes on production and imports	29.7	31.1	31.5	32.4	33.2	33.7
Social security contributions	27.0	27.9	27.3	28.0	28.6	29.9
Taxes and contributions, total[2]	92.1	95.2	97.0	98.8	102.2	104.8
Other revenue[3]	22.5	22.3	22.8	23.1	23.6	25.3
of which interest receipts	2.1	1.9	1.6	1.8	1.9	2.0
Total revenue	**114.0**	**116.9**	**118.8**	**121.1**	**125.1**	**129.3**
Consumption expenditure	51.1	51.7	51.5	52.8	54.4	55.9
Subsidies	2.8	2.7	2.7	2.7	2.7	2.6
Social security benefits and allowances	41.6	42.3	42.5	43.2	44.2	45.3
Other current transfers	5.8	5.7	5.3	5.4	5.6	5.7
Subsidies and current transfers, total	50.2	50.7	50.4	51.3	52.4	53.6
Capital expenditure[4]	8.9	9.1	8.9	9.7	10.0	10.0
Other expenditure	9.5	9.3	9.2	9.0	9.0	10.1
of which interest expenses	2.4	2.3	2.2	2.0	2.0	2.1
Total expenditure	**119.8**	**120.8**	**120.1**	**122.7**	**125.8**	**129.6**
Net lending (+) / net borrowing (-)	**-5.8**	**-3.9**	**-1.3**	**-1.6**	**-0.7**	**-0.3**
Central government	-6.3	-5.8	-3.8	-3.9	-2.3	-1.5
County government						-0.9
Local government	-1.4	-1.0	-0.2	-0.6	-1.0	-0.4
Employment pension schemes	2.7	2.4	2.1	2.3	2.2	2.0
Other social security funds	-0.8	0.5	0.7	0.7	0.4	0.5
Primary balance[5]	-5.4	-3.4	-0.7	-1.3	-0.5	-0.2

1) As calculated in the National Accounts
2) Incl. capital taxes
3) Incl. capital transfers and consumption of fixed capital
4) Gross fixed capital formation and capital transfers
5) Net lending before net interest expenses

Table 15. Main economic indicators in general government

	2015	2016	2017	2018**	2019**	2020**
	% of GDP					
Taxes and social security contributions	43.9	44.0	43.3	42.2	42.1	41.8
General government expenditure[1]	57.1	55.9	53.6	52.4	51.9	51.7
Net lending	-2.8	-1.8	-0.6	-0.7	-0.3	-0.1
Central government	-3.0	-2.7	-1.7	-1.7	-0.9	-0.6
County government						-0.4
Local government	-0.7	-0.4	-0.1	-0.3	-0.4	-0.2
Työeläkelaitokset	1.3	1.1	0.9	1.0	0.9	0.8
Other social security funds	-0.4	0.2	0.3	0.3	0.2	0.2
Primary balance[2]	-2.6	-1.6	-0.3	-0.6	-0.2	-0.1
General government debt	63.5	62.9	61.3	60.0	59.4	58.4
Central government debt	47.6	47.4	47.2	46.3	45.8	45.0
General government employment, 1000 person	619	614	610	609	605	604
Central governmnet	133	131	130	128	127	121
County government						228
Local government	475	473	469	469	467	245
Social security funds	11	11	11	11	11	11

1) EU-harmonized definition
2) Net lending before net intrest expenses

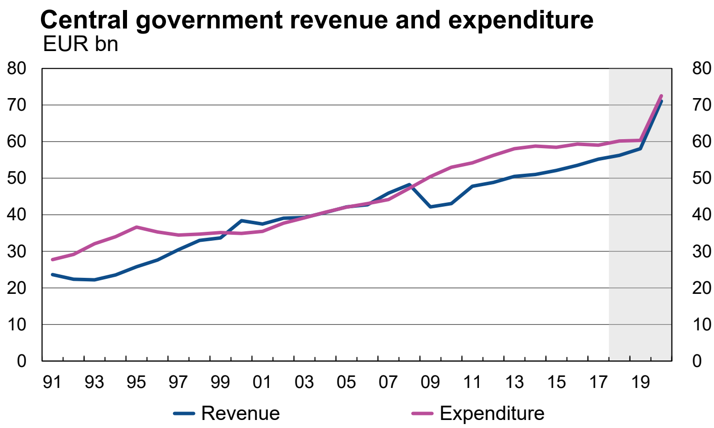
2.2 Central government

Government expenditure is expected to increase moderately in the coming years. Growth in expenditure will be mitigated by the gradually increasing consolidation measures of the Government Programme and the expiry of additional expenditure from key projects in 2019. Reductions in employer contributions contained in the Competitiveness Pact and temporary cuts in holiday pay have reduced employee contributions payable by the government in recent years. Correspondingly, the expiry of the temporary cut in holiday bonus will increase employee contributions in 2019. Expenditure in 2018 will be increased by government investments in key projects and transport infrastructure maintenance, the impact of which will be greatest this year. The expiry of the additional investments of previous years will be evident as a slowdown in investment growth. Because of the low interest rate, government interest expenditure will remain low during the forecast period.

The structure of government expenditure will begin to change in 2020, when the counties begin their operations. The counties will mainly finance their activities through income transfers obtained from central government, which will increase total government spending. Development of the counties' ICT systems has increased government expenditure in a front-loaded manner, even before the counties start to operate.

Government tax income will increase at a fast pace during the forecast period. Strong growth in employment will increase taxes collected from earned income. Household consumption expenditure, which will remain at a high level, will also support growth in VAT revenue.

The general government deficit will decrease towards the end of the forecast period, as a result of moderate growth in expenditure and an increase in tax revenues from the good economic situation. Despite the upturn in the economy, however, the deficit will remain substantial even up to the end of the forecast period.



Incl. health, social services and regional government reform in 2020
Sources: Statistics Finland, MoF
VM34098

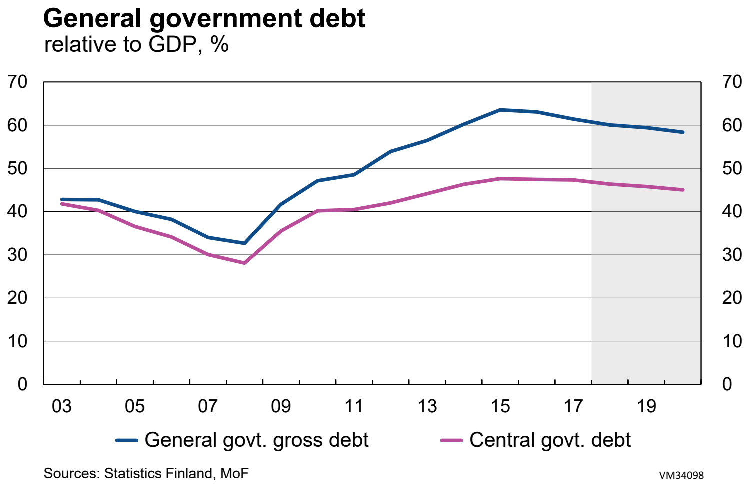


Table 16. Central government[1]

	2015	2016	2017	2018**	2019**	2020**
	EUR billion					
Current taxes	13.0	13.7	14.4	14.6	15.5	28.0
Taxes on production and imports	29.7	31.1	31.5	32.4	33.2	33.7
Social security contributions	0.0	0.0	0.0	0.0	0.0	0.0
Taxes and social security contributions, total[2]	43.3	45.3	46.8	47.7	49.5	62.4
Other revenue[3]	9.2	8.7	8.8	9.0	9.2	9.2
of which interest receipts	0.4	0.3	0.3	0.3	0.3	0.4
Total revenue	**52.5**	**54.0**	**55.7**	**56.7**	**58.6**	**71.7**
Consumption expenditure	13.7	14.1	13.9	14.2	14.6	14.5
Subsidies and current transfers, total	38.2	38.8	39.3	39.5	39.4	51.8
to general government	26.2	27.1	27.9	28.1	27.7	40.2
Interest expenses	2.3	2.2	2.1	1.9	1.9	2.0
Capital expenditure[4]	4.7	4.7	4.3	5.0	5.0	4.9
Total expenditure	**58.8**	**59.8**	**59.5**	**60.6**	**60.9**	**73.1**
Net lending (+) / net borrowing (-)	**-6.3**	**-5.8**	**-3.8**	**-3.9**	**-2.3**	**-1.5**
Primary balance[5]	-4.4	-3.9	-2.0	-2.3	-0.7	0.1

1) As calculated in the National Accounts
2) Incl. capital taxes
3) Incl. capital transfers (excl. capital taxes) and consumption of fixed capital
4) Gross fixed capital formation and capital transfers
5) Net lending before net interest expenses

2.3 County government

The responsibility for organising social and healthcare services, as well as several other municipal and central government functions, are being transferred to the counties. The new authorities will begin operating in 2020. The county sector will include both counties and the national service centres that they own.

Of the counties' expenditure, the lion's share will go to social and healthcare services. The total level of expenditure will be approximately EUR 24.2 billion in 2020. Most of the counties' revenue will come from central government funding. The counties will also receive sales income from service users. County revenues are expected to total approximately EUR 23.3 billion in 2020.

The financial position of the county sector will be in deficit. This will be largely due to the hospital districts' many premises investments planned or decided on earlier, which will be transferred to the Counties' Service Centre for Facilities and Real Estate Management. Investment expenditure will not directly affect the financial position of individual counties, as the counties will lease their premises from the Service Centre for Facilities and Real Estate Management. The Service Centre for Facilities and Real Estate Management may finance investments by borrowing. A significant amount of debt will be transferred from hospital districts to the county sector in addition to real estate and other property, and the amount of debt will also increase during 2020. An estimate of the amount of debt in the county sector by the end of 2020 is EUR 4.4 billion.

The counties will initially incur additional expenses from the start-up and organisation of operations. The forecast has not yet been able to take into account transition costs, because of their uncertainty and quantitative inaccuracy. Transition costs entail an expenditure risk for the forecast. The forecast has also not made any assumption on the increasing efficiency of county operations or consolidation measures or on the behavioural effects of the reform. Expenditure and revenue will follow their own development paths.

Table 17. **County finances**

	2020**
Transfers from central government	20.0
Other revenue	3.2
Total revenue	**23.3**
Consumption expenditure	19.6
Current transfers and othe expenditure	1.0
Capital expenditure	0.9
Total expenditure	**24.2**
Net lending (+) / net borrowing (-)	**-0.9**
Debt	4.4

2.4 Local government

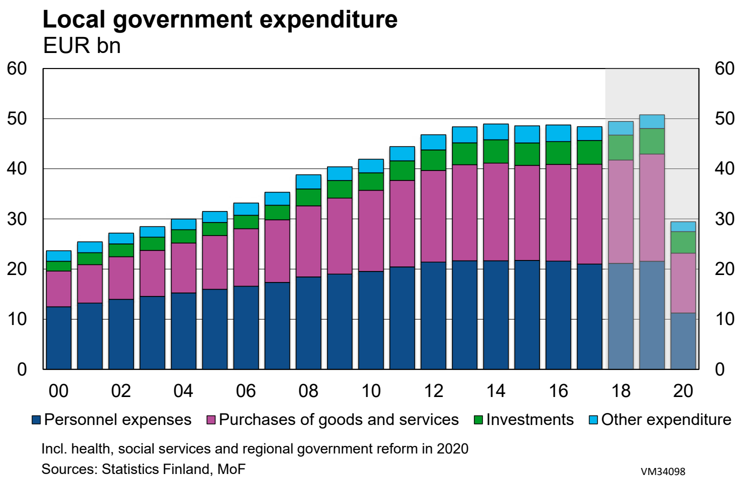
The financial position of local government will deteriorate this year in comparison with last year. Consumption expenditure will increase as a result of, for example, an increase in treatment and care expenditure from the ageing of the population, a reduction in daycare fees for families on low- and middle-level incomes, and a rise in earnings level in the municipal sector. The earnings level will increase as a result of, among other things, a general increase paid in May 2018 and a one-time productivity-based payment payable in January 2019. The productivity payment will be entered in the national accounts on an accrual basis in 2018, as the obligation to pay it will already arise in that year.

Local government revenue will increase only slightly this year. The growth in tax revenues will slow down, for example as a result of a fall in corporate tax revenues, which can be mainly explained by last year's exceptionally high corporate tax take. Furthermore, the average municipal tax percentage for 2018 fell, largely caused by a tax reduction by Helsinki.

The financial position of local government will continue to deteriorate in 2019. The growth in expenditure will be accelerated not only by growth in the need for social and healthcare services, but also by salary and wage increases in the municipal sector and the expiry of the holiday bonus cut prescribed in the Competitiveness Pact, the effect of which will mostly be evident in 2019. Investment expenditure will also continue to increase, as investments by hospital districts rise to a record level in 2019.

The growth in local government revenues will remain moderate in 2019. Revenue growth will be slowed down, for example, by a contraction in central governments transfers to local government resulting from a revised distribution of costs. The development assessment of local government for the period 2019–2020 contains only measures affecting expenditure and revenue that have already been decided upon. Measures by municipalities and joint municipal authorities will be taken into account in the outlook after the completion of the budgets.

Growth pressure on local government consumption expenditure will ease from 2020 because, as a result of the reform of social services and health care , the functions of local government will increasingly be focused on education. The financial position of local government will be slightly in deficit in 2020. Local government debt will increase slightly in 2018–2019, but in 2020 it will fall when the hospital districts' debt of approximately EUR 3.5 billion is transferred to county government.



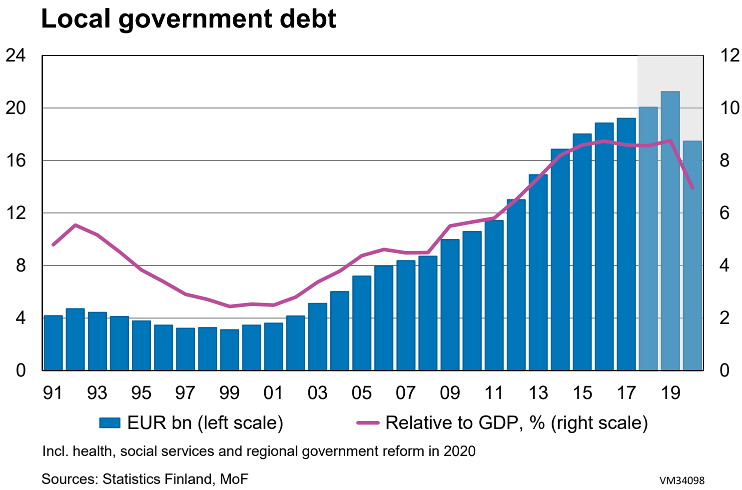


Table 18. Local government[1]

	2015	2016	2017	2018**	2019**	2020**
	EUR billion					
Taxes and social security contributions	21.9	22.0	22.8	23.1	24.1	12.5
of which municipal tax	18.6	18.7	19.1	19.5	20.4	9.2
corporate tax	1.7	1.5	1.9	1.9	2.1	1.5
real estate tax	1.6	1.7	1.8	1.8	1.9	1.9
Other revenue[2]	18.5	18.9	18.5	18.9	18.7	11.2
of which interest receipts	0.3	0.3	0.3	0.3	0.3	0.3
transfers from central government	13.7	14.3	13.7	14.0	13.6	6.4
Total revenue	**40.3**	**40.9**	**41.3**	**41.9**	**42.8**	**23.7**
Consumption expenditure	33.8	34.0	34.0	34.9	36.0	17.9
of which compensation of employees	21.7	21.6	21.0	21.1	21.6	11.2
Income transfers	3.3	3.3	2.7	2.7	2.7	2.0
of which social security benefits and allowances	1.3	1.4	0.8	0.7	0.7	0.1
subsidies and other transfers	1.8	1.8	1.9	1.8	1.9	1.8
interest expenses	0.1	0.1	0.1	0.1	0.1	0.1
Capital expenditure[3]	4.6	4.6	4.7	5.0	5.1	4.3
Total expenditure	**41.7**	**41.9**	**41.5**	**42.6**	**43.8**	**24.1**
Net lending (+) / net borrowing (-)	**-1.4**	**-1.0**	**-0.2**	**-0.6**	**-1.0**	**-0.4**
Primary balance[4]	-1.5	-1.1	-0.4	-0.8	-1.1	-0.6

1) As calculated in National Accounts
2) Incl. capital transfers and consumption of fixed capital
3) Gross capital formation and capital transfers
4) Net lending before net interest expenses

2.5 Social security funds

The surplus of earnings-related pension funds fell to 0.9% of GDP in 2017, compared with an average of just over 3% in the first decade of the 2000s. The surplus of earnings-related pension funds is expected to remain approximately at the level of last year throughout the forecast period. Positive economic conditions will increase income from pension contributions, but not enough to improve the financial position of pension funds. The rapid growth in pension expenditure will continue, as the number of pensioners is increasing along with the average level of pensions. Pension funds' property income will return to moderate growth during the forecast period, but will remain low due to the low interest rate. It has been agreed that private sector earnings-related pension contribution will remain at the present level of 24.4% throughout the forecast period.

Other social security funds consist mainly of the Social Insurance Institution (Kela) and the Unemployment Insurance Fund, which are responsible for the provision of basic security and for earnings-related unemployment security, respectively. The surplus of other social security funds rose to 0.3 per cent of GDP last year. Other social security funds are forecast to remain in slight surplus over the forecast horizon. The fall in unemployment expenditure will continue, as the employment situation continues to improve. The accelerating growth of total wages and salaries will increase income from social security contributions. On the other hand, a fall in unemployment insurance and sickness insurance contributions at the beginning of this year will lower revenues. Based on the Unemployment Insurance Fund's own estimate, it has been assumed that unemployment insurance contributions will be reduced at the beginning of next year by 0.4%. A larger reduction in contributions might also be possible, as the good economic situation has put the fund's finances clearly in surplus.

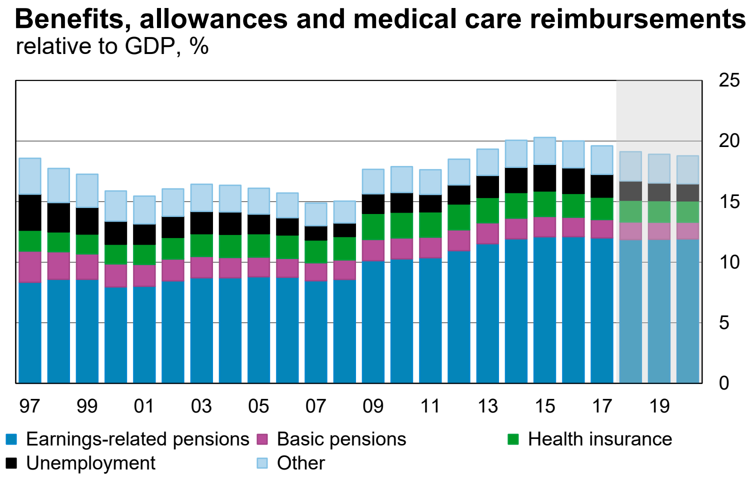


Table 19. Finances of social security funds[1]

	2015	2016	2017	2018**	2019**	2020**
	EUR billion					
Investment income	3.4	3.6	3.5	3.7	4.0	4.2
Social security contributions	26.9	27.9	27.3	28.0	28.6	29.8
of which contibutions paid by employers	18.2	18.8	17.6	17.5	17.6	18.1
contributions paid by insured	8.7	9.2	9.7	10.4	11.0	11.7
Transfer from general government	14.3	14.6	15.8	15.6	15.6	15.2
Other revenue	0.5	0.5	0.4	0.5	0.5	0.5
Total revenue	**45.2**	**46.5**	**47.1**	**47.8**	**48.6**	**49.8**
Consumption expenditure	3.7	3.6	3.6	3.7	3.8	3.9
Social security benefits and allowances	35.9	36.6	37.4	38.0	38.9	40.0
Other outlays	3.7	3.4	3.3	3.1	3.3	3.4
Total expenditure	**43.3**	**43.6**	**44.3**	**44.8**	**46.0**	**47.3**
Net lending (+) / net borrowing (-)	**1.9**	**2.9**	**2.8**	**3.0**	**2.6**	**2.5**
Earnings-related pension schemes	2.7	2.4	2.1	2.3	2.2	2.0
Other social security funds	-0.8	0.5	0.7	0.7	0.4	0.5
Primary balance[2]	0.5	1.6	1.7	1.8	1.3	1.2

1) Corporations classified under local government but not included in statistics on municipal finances as well as Government of Åland, Association of Finnish Local and Regional Authorities, Local Government Employers and Municipal Guarantee Board
2) E.g. differences in capital transfers and investment grants

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