



MINISTRY
OF FINANCE

Economic Survey

Winter 2021

Economic Prospects

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Economic Survey

Winter 2021

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Abstract

Finland's gross domestic product is expected to grow by 3.4% in 2021. The deterioration of the COVID-19 pandemic in late 2021 increases uncertainty for economic decision-makers and will temporarily slow down economic growth around the turn of the year. Finland's GDP growth will remain at 3.0 per cent in 2022, as production in many sectors is still below the pre-pandemic level. However, economic growth will slow down and Finland's GDP is expected to grow by 1.5% in 2023 and by 1.4% in 2024.

In the forecast, the deterioration of the pandemic is expected to slow down the recovery of the economy temporarily. Uncertainties related to the manner in which the disease develops, virus mutations and vaccination coverage have again increased.

Energy prices will sustain inflation around the turn of the year and will gradually turn to a decline during 2022. The underlying factors behind the high inflation are related to both supply and demand. The rise in inflation is expected to be temporary as the disturbances in demand and supply are gradually eased.

The general government deficit will decrease substantially in 2021–2023. However, the deficit will not be fully eliminated during the period of rapid economic growth. Debt relative to GDP will also decrease temporarily as the economy recovers and the deficit is reduced. The debt ratio will again turn to growth as economic growth slows down.

Keywords economic prospects, public finance, economic development

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Taloudellinen katsaus, syksy 2021

Valtiovarainministeriön julkaisuja 2021:71**Julkaisija** Valtiovarainministeriö**Teema**

Talousnäkömät

Yhteisötekijä Kansantalouselosasto**Kieli** Englanti**Sivumäärä** 78**Tiivistelmä**

BKT:n arvioidaan kasvavan 3,4 % v. 2021. Covid-19-pandemian pahentuminen vuoden 2021 lopulla lisää taloudenpitäjien epävarmuutta ja hidastaa talouskasvua tilapäisesti vuodenvaihteen ympärillä. BKT:n kasvu pysyy 3,0 prosentissa v. 2022, sillä usealla toimialalla tuotanto on edelleen pandemiaa edeltävän tason alapuolella. Talouden kasvu kuitenkin hidastuu ja BKT:n arvioidaan kasvavan 1,5 % v. 2023 ja 1,4 % v. 2024.

Ennusteessa oletetaan, että tautitilanteen heikentyminen hidastaa talouden toipumista vain hetkellisesti. Taudinkehitykseen, virusmuunnoksiin sekä rokotekattavuuteen liittyvä epävarmuus on uudelleen lisääntynyt.

Energian hinta pitää inflaatiota yllä vuodenvaihteen ympärillä ja kääntyy vähitellen alenevaksi vuoden 2022 aikana. Nopean inflaation taustalla on sekä kysyntä- että tarjontapuolen tekijöitä. Inflaation nousun oletetaan jäävän tilapäiseksi kysyntä- ja tarjontahäiriöiden vähitellen helpottaessa.

Julksen talouden alijäämä pienenee voimakkaasti vuosina 2021-2023. Alijäämä ei kuitenkaan poistu kokonaan ripeän talouskasvun aikana. Myös velka suhteessa bruttokansantuotteeseen laskee väliaikaisesti talouden elpessä ja alijäämän pienentyessä. Talouskasvun hidastuessa velkasuhde kääntyy kuitenkin uudelleen kasvuun.

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Referat

Bruttonationalprodukten beräknas öka med 3,4 procent 2021. Den förvärrade covid-19-pandemin i slutet av 2021 ökar de ekonomiska aktörernas osäkerhet och bromsar upp den ekonomiska tillväxten tillfälligt kring årsskiftet. BNP-tillväxten stannar på 3,0 procent 2022, eftersom produktionen inom flera branscher fortfarande är på en lägre nivå än före pandemin. Den ekonomiska tillväxten dämpas dock och BNP beräknas öka med 1,5 procent 2023 och 1,4 procent 2024.

I prognosen förväntas försämringen av pandemin tillfälligt bromsa återhämtningen av ekonomin. Den osäkerhet som är förknippad med sjukdomens utveckling, virusvarianter och vaccinationstäckning har dock ökat igen.

Energipriset håller inflationen uppe kring årsskiftet, men den börjar så småningom avta under 2022. Den snabba inflationen beror på faktorer som gäller både tillgång och efterfrågan. Inflationssökningen uppskattas bli tillfällig i och med att de störningar som gäller tillgång och efterfrågan så småningom minskar.

Underskottet i de offentliga finanserna minskar kraftigt 2021–2023. Underskottet försvinner likväl inte helt under den snabba ekonomiska tillväxten. Skulden i förhållande till bruttonationalprodukten sjunker också tillfälligt när ekonomin återhämtar sig och underskottet minskar. När den ekonomiska tillväxten mattas av börjar skuldkvoten emellertid öka igen.

Nyckelord

ekonomiska utsikter, offentlig ekonomi, ekonomisk utveckling

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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
MEAE	Ministry of Economic Affairs and Employment
MoF	Ministry of Finance
MSAH	Ministry of Social Affairs and Health

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

ECONOMIC SURVEY WINTER 2021

This Economic Survey offers projections of economic developments in 2021–2024. In addition to short-term prospects, it includes a medium-term economic outlook extending to 2026.

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 quarterly national accounts data published by Statistics Finland in November 2021 and on other public statistical sources available by 13 December 2021.

Helsinki December 2021

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Preface

The overall view of the economy has remained fairly stable during the autumn in spite of the new acceleration of the COVID-19 pandemic and the increase in uncertainty caused by virus mutations.

The global economy is continuing its rapid recovery and pulling the Finnish economy along with it, although the quickest growth phase has already passed. The slowing down of growth is reflected in the Finnish economy in industrial orders, for example. While they continue to grow at a good rate, growth is substantially slower than in the preceding months. In spite of the slowing down of growth, the economic outlook of the business sector has remained good and confidence in the future is strong. Employment is improving rapidly and the unemployment rate is declining. At the same time, the number of job vacancies is higher than ever before and long-term unemployment has settled at a high level. It appears that the increase in uncertainty has begun to erode household confidence in the Finnish economy, but consumers' confidence in their own economy has remained strong.

With inflation having accelerated globally and in Finland, it is now subject to close scrutiny. Prolonged inflation and a cost spiral that would lead to a rapid tightening of monetary policy is not considered likely in the euro area. Inflation expectations have become anchored to the European Central Bank's inflation target. Financing conditions are expected to remain light. The situation is different in the United States, where the risk of tighter financing conditions is higher.

This Ministry of Finance forecast can be summarised as follows.

In 2021 and 2022, the economy will continue its rapid recovery from the slump and employment will continue to grow, although growth around the turn of the year will be slower than previously predicted due to the acceleration of the pandemic and the related restriction measures. The phase of rapid growth will level off in 2022 globally and in Finland. From 2023 onwards, the economy will grow at a rate of 1–1.5 per cent.

Rapid growth and the end of spending related to managing the pandemic will quickly reduce the general government deficit in 2021–2023. The growth of the general government debt ratio will level off temporarily, but the growth of debt will continue when economic growth slows down.

Successful management of the pandemic may stimulate faster-than-expected growth in the global economy, corporate investment and household consumption. Failure in managing the pandemic would have the opposite effect. If the existing vaccines were to be ineffective against virus mutations, the economic outlook would look completely different.

Provided that the pandemic will gradually abate and life will return closer to normal, international economic organisations have recommended that countries resume policy geared towards maintaining public debt in alignment with their long-term debt sustainability. At the same time, public resources should be increasingly allocated towards supporting the economic transition to carbon-neutral production and consumption.

This advice is also relevant to Finland, especially as the ageing of the Finnish population will increase public expenditures and weaken debt sustainability far into the future.

Solving this equation will require competencies, new technological solutions, significant private investments and an efficient public sector; in other words, front-line competitiveness that both creates and attracts companies and highly competent professionals to Finland as well as careful management of public sector finances.

The public sector can support the competitiveness of the economy directly by allocating funds to education, research, infrastructure and promoting health, for example. Due to the framework for public spending being tight, it is at least equally important for the public sector to regulate the conditions for economic activity in a manner that supports private labour supply, product development, innovation and investment. When this is achieved, the framework for public spending will be expanded.

When public debt grows relative to the economy's capacity to generate income, the risks of the public sector's financial management increase. Debt is not a free lunch, even in this time of zero interest rates. Therefore, it is important to keep a close eye on debt and carefully assess risks. In general government finances, the aim should be to observe rules that support carefully planned spending with a long-term view.

The international economic organisations have repeatedly emphasised this in the recommendations they issue to countries. This recommendation is especially topical in the context of economies moving on from a period of pandemic-related spending and in the midst of the ongoing structural transformation of the economy.

Summary

Economic outlook for the period 2021 – 2024

Finland's gross domestic product is expected to grow by 3.4% in 2021. The deterioration of the COVID-19 pandemic in late 2021 increases uncertainty for economic decision-makers and will temporarily slow down economic growth around the turn of the year. Finland's GDP growth will remain at 3.0 per cent in 2022, as production in many sectors is still below the pre-pandemic level. However, economic growth will slow down and Finland's GDP is expected to grow by 1.5% in 2023 and by 1.4% in 2024.

In the forecast, the deterioration of the pandemic is expected to slow down the recovery of the economy temporarily. Uncertainties related to the manner in which the disease develops, virus mutations and vaccination coverage have again increased.

The general government deficit will decrease substantially in 2021–2023. However, the deficit will not be fully eliminated during the period of rapid economic growth, as public expenditures are structurally higher than revenues. Debt relative to GDP will also decrease temporarily as the economy recovers and the deficit is reduced. The debt ratio will again turn to growth as economic growth slows down.

The growth prospects of the global economy are overshadowed by accelerating inflation

The global economy will grow by 6.1% in 2021 and the rate of growth will level off to 4.6% in 2022 and then slow down further to 3.4% in 2023 and 3.0% in 2024. The growth prospects of the global economy are overshadowed by the prolongation of the pandemic, supply chain disturbances and quickly accelerating inflation. In late 2021, the pandemic has put especially Europe to a test. Global supply chains have been disturbed for various reasons, such as the difficulties in the availability of semiconductors, disturbances in container transport and the shortage of labour and machinery in ports.

Consumer price inflation has accelerated quickly globally. The underlying factors include, for example, supply chain disturbances and the increase in energy prices. Electricity prices are extremely high in Europe due to the increase in natural gas prices, among other things. It is forecast that inflation pressures will ease to a large extent during 2022 but the risk of longer-term inflation and the resulting more extensive price pressure in economies has increased.

Global trade will grow by 4.8% in 2022 and by 4.4% in 2023. In 2024, trade will recover and reach 4.6% growth. The growth prospects are weakened by supply chain disturbances resulting from various reasons as well as by the slowing down of the growth of the global economy. In the euro area, the goods trade outlook is weaker than in the United States or emerging economies.

Economic recovery continues, driven by domestic demand

Finland's GDP growth will accelerate to 3.4% in 2021. The deterioration of the COVID-19 pandemic in late 2021 increases uncertainty for economic decision-makers and will slow down economic growth in the fourth quarter. A high savings rate and optimism among consumers have created a basis for rapid growth in private consumption. Private investments already increased during the first half of 2021 and the trend in housing construction in particular has been positive. Global economic recovery, stimulus measures and the demand for Finnish exports in important trade areas increased both exports and imports.

The number of employed persons has increased significantly in 2021. Employed persons numbered 65,000 more in October than a year earlier, and their number increased by 2.1% year-to-date. However, the number of employed persons is only higher among fixed-term and part-time employees. The number of permanent full-time employees is still lower than the previous year. In fact, the number of hours worked only increased by 0.4%.

The annual change in the consumer price index has accelerated to a level in excess of 3 per cent in late 2021, although inflation for 2021 will be 2.2 per cent. The increase in prices is primarily the result of rising energy prices. The prices of liquid fuels remain high and the increase in electricity prices has continued to accelerate. Increasing prices of goods have also begun to be visible as a factor accelerating inflation after the prolonged decrease in prices.

Finland's gross domestic product is expected to grow by 3.0% in 2022. Economic growth is expected to remain slow in the first quarter of the new year. As uncertainties related to the COVID-19 pandemic diminish, economic growth will accelerate again. Growth in private consumption continues as the balance between saving and consumption tilts more towards consumption. The growth of purchasing power will continue to accelerate in 2022 as hours worked and average earnings increase, although the price of consumption will grow by 2.5% in 2022.

Private investments will grow at an average rate of 2.9% during the forecast period, which means that their ratio to GDP will reach nearly 20% in 2024. Funding from the Recovery and Resilience Facility of the EU (RRF) will boost private investments particularly in 2022 and 2023. R&D investments are expected to benefit from RRF funding. The investment outlook for Finnish industries is good. Machinery and equipment investments will increase rapidly as the business environment stabilises after 2021.

Housing investments will turn to a slight decline of 2.2% in 2022 while housing starts will remain at a high level, at approximately 38,000 new housing units. Towards the end of the outlook period, housing starts will gradually approach the long-term average and investments in housing construction will contract further. Strong export growth will continue in 2022, driven by the growth of the global economy. The recovery of service exports will also accelerate growth compared to 2021.

The forecast assumes that the pay increases specified in the agreements in 2022 will follow the trend of the past two decades and that the pay increases will be higher than in 2021. This year, the pay increases specified in the agreements are slightly under 2% on average, and they are estimated to accelerate to slightly over 2% on average next year. Moreover, wage drifts are expected to increase in 2022. Nominal earnings would thus increase by 2.3% in 2021 and approximately 3% in 2022.

In 2023, GDP growth will slow down to 1.5%, which is still above the medium-term average. The short period of strong growth driven by global stimulus and the recovery from the COVID-19 pandemic will be over and the economy is again facing the growth constraints identified before the crisis. Finland's GDP is expected to grow by 1.4% in 2024.

The demand for labour is sustained by economic growth and in the short term, the demand can be met by the large number of unemployed persons and the government measures to increase the supply of labour. Economic recovery will increase the number of employed persons in 2022 and 2023, especially in the service sectors. The number of employed persons is expected to increase by 1.5% in 2022. As the economy loses strength, the growth will slow down but the employment rate will exceed 74% in 2024. The increase in earnings in 2023 and 2024 will be linked to the slower growth in productivity. At the same time, an increase in the level of economic activity and the resulting rise in employment as well as labour shortages in some sectors are expected to boost wage drifts.

Inflation will accelerate by 2.6% in 2022, as measured by the national consumer price index. Energy prices will sustain inflation around the turn of the year and will gradually turn to a decline during 2022. The underlying factors behind the high inflation are related to both supply and demand. A key demand-related factor is the fact that the savings that consumers have accumulated during the COVID-19 pandemic are being channelled to the consumption of durables. The growth of demand and increase in prices have been particularly rapid for goods related to construction and renovation. Supply side factors include, for example, disturbances in international trade, labour shortages and the shortage of components that especially affects the automotive and electronics industries. The rise in inflation is expected to be temporary as the disturbances in demand and supply are gradually eased. Inflation in Finland is expected to slow down to 1.8% in 2023 and 2024.

Public finances are recovering from the crisis but debt will continue to grow

The general government deficit will be reduced significantly in 2021 compared to the substantial deficit seen in the previous year. Public finances have been strengthened particularly by the rapid growth of revenue from taxes and social security contributions following higher economic growth and employment. In addition, the end of the economic slowdown has reduced the need for stimulus and support measures. At the same time, the COVID-19 pandemic continues to create a burden on health and social services, for example.

For the next few years, the general government deficit will still be higher than before the pandemic. Public sector expenditures are structurally higher than revenues, and the deficit will not be fully eliminated during the period of brisk

economic growth. A general government deficit-to-GDP ratio of approximately 1% is projected for the mid-2020s.

The ratio of public debt to GDP is sensitive to changes in economic growth. Brisk GDP growth and the reduced deficit will lead to a reduction in the debt ratio in 2021. However, as economic growth slows down, deficits at the central government, local government and wellbeing services county levels will see the debt ratio turn back to growth starting from 2023. The debt ratio in 2026 is estimated to be approximately 69%, or about 10 percentage points higher than before the pandemic.

Rapid deterioration of pandemic the main threat to economic growth

The main risks in the forecast are still related to the COVID-19 pandemic and the restrictions introduced to manage it. Virus mutations lead to more uncertainty in the prospects of managing the pandemic and the situation may rapidly change for the worse despite the progress in vaccinations. There is a risk that by failing to contain the pandemic, emerging countries will face a period of slow growth, and this would be a significant blow to global economic growth.

By slowing down the recovery, a prolonged pandemic would have a strong impact on private consumption and, in particular, on the demand for services. Deterioration of the COVID-19 situation is also reflected in growing uncertainty in the investment environment, which may postpone investments or prevent them altogether.

The acceleration of inflation is estimated to be a temporary phenomenon and inflation will again slow down starting from the second half of next year. However, it is possible that inflation will remain high for a longer time. Both market-based and survey-based inflationary expectations rose during the autumn but are still in line with the inflation targets. Concern about inflation-boosted wage and salary costs is also closely associated with the increase of inflationary expectations. A price-salary spiral in economy would be a self-feeding longer-term phenomenon, which would probably slow down economic growth.

A situation in which the Recovery and Resilience Facility would encourage more private investments than forecast can be seen as a positive risk for such investments.

The uncertainty of the economic forecast can be illustrated with the confidence intervals based on previous forecasting errors and built around the forecast. According to them, there is an 80% probability that GDP growth will be between 2% and 5% in 2021. There is also an 80% probability that GDP growth will be between 0% and 6% in 2022. The economic growth rate may also fall outside the confidence interval, especially because the growth estimates are associated with an exceptionally high degree of uncertainty.

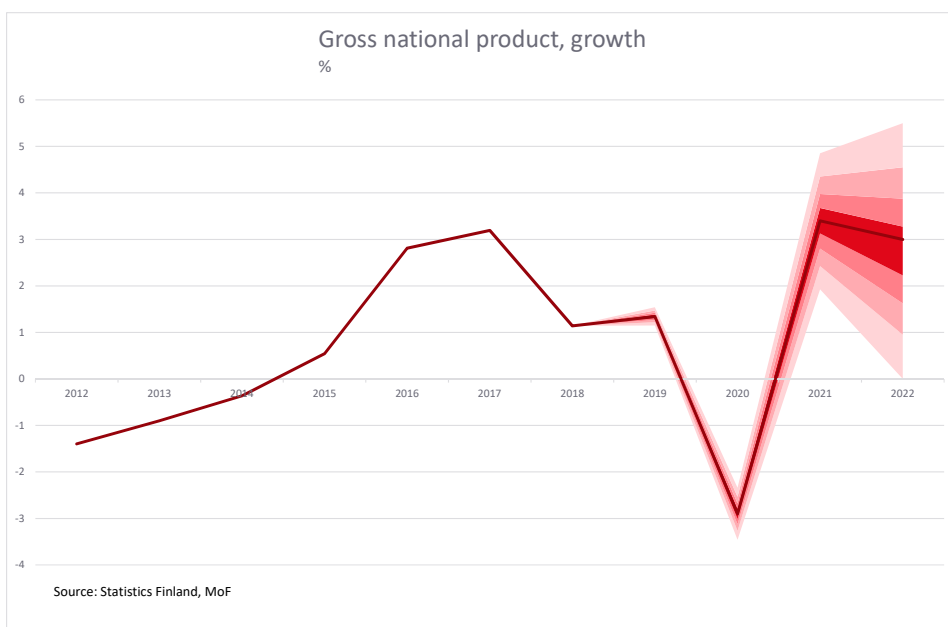


Table 1. Key forecast figures

	2020	2019	2020	2021**	2022**	2023**	2024**
	EUR bn	change in volume, %					
GDP at market prices	236	1.3	-2.9	3.4	3.0	1.5	1.4
Imports	85	2.3	-6.5	3.7	4.9	3.5	4.6
Total supply	321	2.5	1.5	3.4	3.6	2.1	2.4
Exports	85	6.8	-6.8	4.2	5.6	3.7	4.5
Consumption	178	1.1	-3.1	3.1	2.8	1.1	1.3
private	121	0.7	-4.7	3.0	3.8	2.1	1.7
public	58	2.0	0.5	3.3	0.7	-1.2	0.4
Investment	57	-1.6	-0.7	1.4	2.8	2.3	2.1
private	45	-2.4	-3.4	3.6	3.0	2.6	2.5
public	12	2.4	11.0	-7.4	1.7	1.2	0.3
Total demand	321	2.4	1.7	3.4	3.6	2.1	2.3
domestic demand	236	-0.4	-2.7	3.2	2.8	1.4	1.4

Table 2. Other key forecast figures

	2019	2020	2021**	2022**	2023**	2024**
GDP, EUR bn	240	236	249	262	271	281
Services, change in volume, %	1.7	-3.6	3.9	2.6	1.4	1.3
Industry, change in volume, %	2.6	-0.4	3.4	3.7	2.5	2.0
Labour productivity, change, %	0.3	-0.0	3.2	0.8	1.0	1.1
Employed labour force, change, %	1.0	-1.5	2.2	1.5	0.6	0.3
Employment rate, %	71.6	70.7	72.4	73.5	74.0	74.2
Unemployment rate, %	6.7	7.7	7.6	6.7	6.5	6.4
Consumer price index, change, %	1.0	0.3	2.2	2.6	1.8	1.8
Index of wage and salary earnings, change, %	2.1	1.9	2.3	3.0	2.5	2.6
Current account, EUR bn	-0.7	2.0	2.0	2.4	2.6	2.6
Current account, relative to GDP, %	-0.3	0.8	0.8	0.9	1.0	0.9
Short-term interest rates (3-month Euribor), %	-0.4	-0.4	-0.5	-0.5	-0.5	-0.4
Long-term interest rates (10-year govt. bonds), %	0.1	-0.2	-0.1	0.0	0.0	0.1
General government expenditure, relative to GDP, %	53.2	57.3	55.9	53.7	53.1	52.5
Tax ratio, relative to GDP, %	42.2	42.1	43.5	42.0	41.9	41.7
General government net lending, relative to GDP, %	-0.9	-5.5	-2.8	-2.1	-1.3	-1.1
Central government net lending, relative to GDP, %	-1.1	-5.5	-3.3	-2.5	-1.4	-1.4
General government gross debt, relative to GDP, %	59.5	69.5	67.7	67.1	67.5	67.9
Central government debt, relative to GDP, %	44.3	52.9	51.8	51.3	51.6	51.7

Medium-term outlook for the period 2025-2026

The Finnish economy will grow rapidly in 2021 and 2022 and as a result, economic output will approach the estimated potential output and the output gap will be almost closed in 2023. In its medium-term projection, the Ministry of Finance expects the output gap to remain closed after the current economic cycle, in other words, the Finnish economy will grow at its potential rate in 2025 and 2026¹. Thus, annual economic growth is expected to slow down to just over one per cent.²

The change in labour input will only have a minor impact on potential output in the period 2021–2024 and the impact may even be negative in the period 2025–2026. Before the middle of the decade, labour input will start declining as the working-age population shrinks and there is no longer any growth in the participation rate. The approach of the structural unemployment rate will also slow down growth in labour input.

In addition to labour input, the production conditions of the economy are also influenced by the capital stock. Last year, as a result of the downturn and uncertain economic outlook, the investment rate fell, which temporarily slowed down potential output growth. Growth in capital stock will boost potential output growth by about 0.5% each year between 2021 and 2026.

1 The Ministry of Finance bases its medium-term projection on an estimate of potential output growth, which is considered to determine the medium-term and long-term growth potential of the Finnish economy. In this projection, economic growth for the years $t+3$ and $t+4$ is estimated so that the output gap will close by the year $t+4$. However, during exceptional economic cycles, deviations from this basic assumption can be made if no credible results can be produced by adhering to the rule. In that case, depending on the situation, the output gap might be positive or negative in the year $t+4$.

2 In its assessments of potential output and the output gap, the Ministry of Finance uses the production function method jointly developed by the European Commission and EU Member States, in which potential output growth is divided into projections of potential labour input, capital and total factor productivity. Potential output and output gap are latent variables, the assessment of which involves uncertainties, especially during a strong economic cycle and under conditions of rapid changes in the production structure.

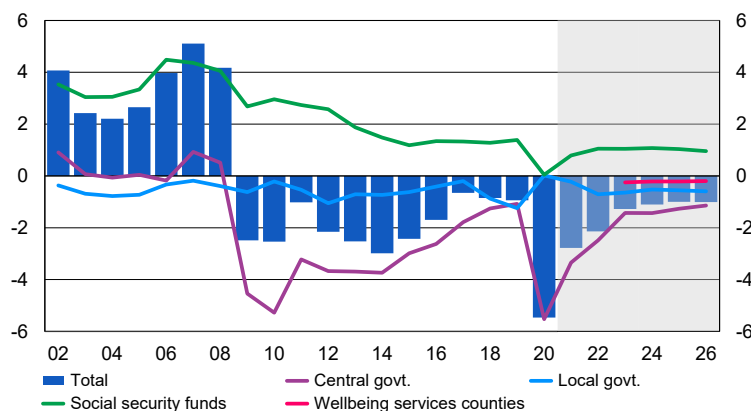
Total factor productivity is the third source of potential output growth. It has grown more rapidly in recent years, compared to the early 2010s. However, productivity growth remains weak compared to the early 2000s. Structural changes in the Finnish economy are one factor explaining the weak growth. The output of high-productivity sectors has declined and services have become more predominant in the overall structure of the economy. Annual total factor productivity is expected to grow by slightly under one per cent in the period 2021–2026, which can be compared with an average annual growth of more than two per cent in the early years of the 2000s.

Table 3. Key forecast figures for the medium term

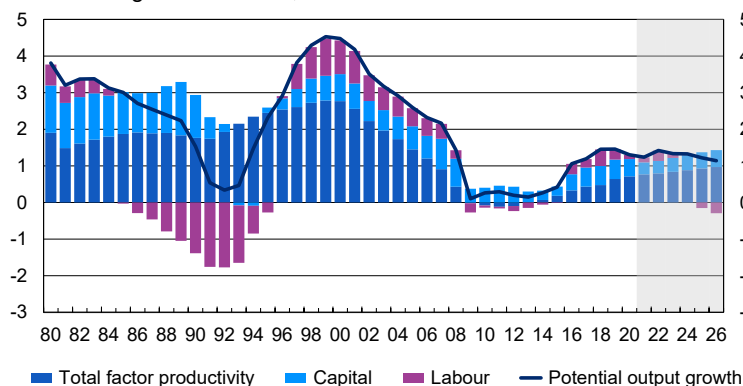
	2020	2021	2022**	2023**	2024**	2025**	2026**
GDP at market prices, change in volume, %	-2.9	3.4	3.0	1.5	1.4	1.2	1.2
GDP, EUR bn	236	249	262	271	281	289	299
Consumer price index, change, %	0.3	2.2	2.6	1.8	1.8	1.9	1.9
Unemployment rate, %	7.7	7.6	6.7	6.5	6.4	6.3	6.2
Employment rate, %	70.7	72.4	73.5	74.0	74.2	74.4	74.5
General government net lending, relative to GDP, %	-5.5	-2.8	-2.1	-1.3	-1.1	-1.0	-1.0
Central government	-5.5	-3.3	-2.5	-1.4	-1.4	-1.3	-1.1
Local government	0.0	-0.2	-0.7	-0.6	-0.5	-0.6	-0.6
Wellbeing services counties					-0.2	-0.2	-0.2
Social security funds	0.0	0.8	1.1	1.0	1.1	1.0	1.0
Structural balance, relative to GDP, %	-3.3	-1.7	-2.0	-1.2	-1.1	-1.0	-1.0
General government gross debt, relative to GDP, %	69.5	67.7	67.1	67.5	67.9	68.5	69.1
Central government debt, relative to GDP, %	52.9	51.8	51.3	51.6	51.7	52.1	52.3
Output gap, % of potential output ¹	-3.8	-1.8	-0.2	-0.1	0.0	-0.0	0.0

¹ Estimated according the method developed jointly by the EU Commission and Member States

General government financial balance relative to GDP, %



Contributions to potential output growth according to EU method, %



1 Economic outlook

1.1 Global economy

1.1.1 World economy

The world economy has recovered quickly from the downturn caused by the pandemic that broke out in 2019. However, growth prospects are overshadowed by the prolongation of the pandemic, supply chain disturbances and quickly accelerating inflation. In late 2021, the pandemic has put Europe in particular to the test. Global supply chains have been disturbed for various reasons, such as the difficulties related to the availability of semiconductors, disturbances in container transport and the shortage of labour and machinery in ports. The world economy grows by 6.1% in 2021, after which the rate of growth will level off to 4.6% in 2022 and then slow down further to 3.4% in 2023 and 3.0% in 2024.

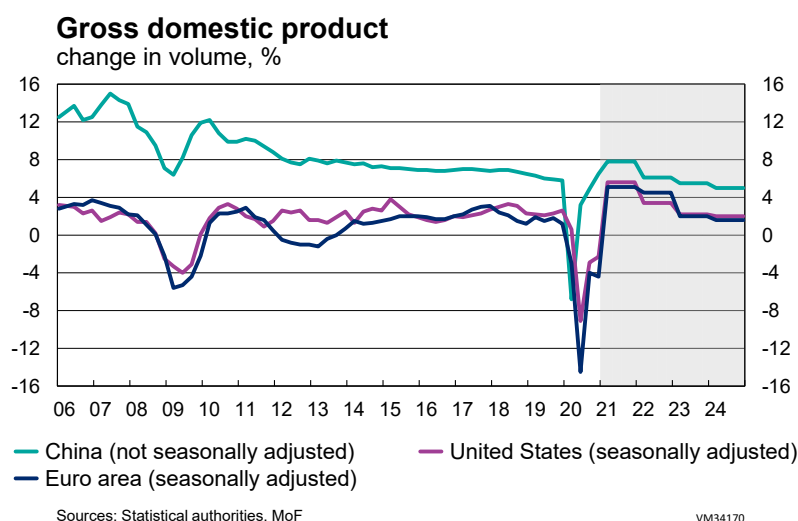
Consumer price inflation has accelerated quickly, especially in the United States, but also in Europe and emerging economies. Background factors include, for instance, supply chain disturbances and the increase in energy prices. Electricity prices are extremely high in Europe due to the increase in natural gas prices, among other things. It is predicted that inflation pressures will ease to a large extent during 2022 but the risk of longer-term inflation and the resulting more extensive cost pressure in economies has increased.

Economic growth slowed down in the United States in the third quarter of 2021 after the fast growth during the first half of the year. Consumer confidence has declined, particularly with regard to future economic development. In the future, fiscal stimulus will focus on infrastructure renewal and its influence on economic growth will be visible over a longer term. The economy will grow by 3.4% in 2022, after which the rate of growth will slow down to 2.2% in 2023 and to 2.0% in 2024.

Strict COVID-19 policy measures and the decline in car sales have slowed down retail trade in China in late 2021. Electricity shortage has hampered industrial growth. Problems in the real estate sector may have more extensive effects. Leading indicators

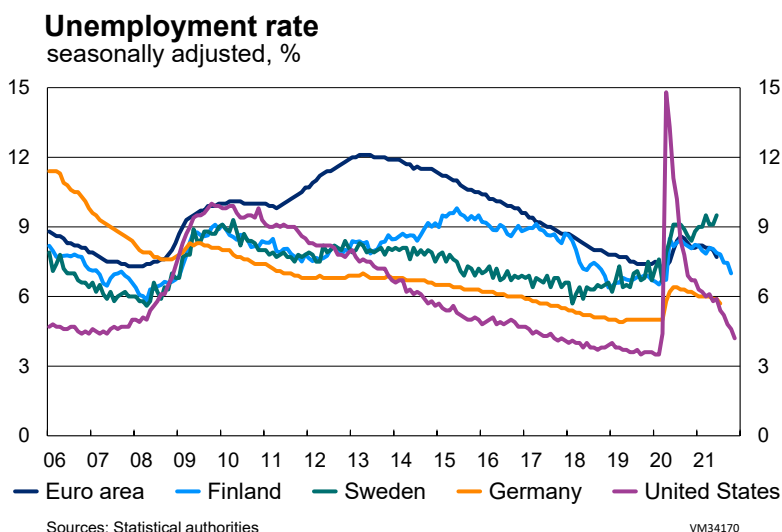
suggest fairly subdued development. The economy will grow by 6.1% in 2022, by 5.5% in 2023 and by 5.0% in 2024.

The prolonged COVID-19 pandemic overshadows the economic outlook of the euro area. Economic development will be weaker than estimated, especially in the final quarter of 2021 and the first quarter of 2022. The euro area economy will grow by 4.5% in 2022. Growth will slow down to 2.0% in 2023 as the economic cycle levels off and to 1.6% in 2024 as the economy is approaching its potential growth. The outlook for industries in Germany is subdued, largely due to the problems in the automotive industry. The French economy has recovered quickly in 2021, mainly thanks to the service sector, but its growth will slow down on a broad front during the outlook period.



Economic growth in the United Kingdom slowed down clearly in the third quarter of 2021. In addition to other challenges, Brexit has caused disturbances in the supply of certain commodities. Growth prospects are overshadowed by the acceleration of inflation and challenges in foreign trade. Growth will slow down from 4.6% in 2022 to 1.4% in 2023 and further to 1.3% in 2024.

Sweden has recovered from its difficult COVID-19 epidemic. The outlook for industries is relatively bright although the shortage of semiconductors hampered exports in summer 2021. The outlook for the service sector is likewise positive. However, the decline in consumer confidence in late 2021 seems to indicate the slowing down of growth. The economy will grow by 2.9% in 2022, by 2.2% in 2023 and by 1.9% in 2024.



The increase in households' real income has contributed to retail trade in Russia. The positive development in the extractive industry when energy prices are high also contributes to economic growth. On the other hand, the COVID-19 epidemic continues to be difficult and the resulting stricter restrictions overshadow the economic outlook. The economy will grow by 2.0% in 2022, after which the rate of growth will slow down to 1.2% in 2023 and further to 1.0% in 2024.

Although total output declined in Japan in the third quarter of 2021 in relation to the preceding quarter, leading indicators suggest cautiously positive development. The difficult COVID-19 epidemic situation experienced in the summer has eased and the state of emergency that was declared in 19 prefectures has been cancelled. Growth prospects will decline as fiscal stimulus decreases. The economy will grow by 1.1% in 2022 and by 0.5% in 2023 and 2024.

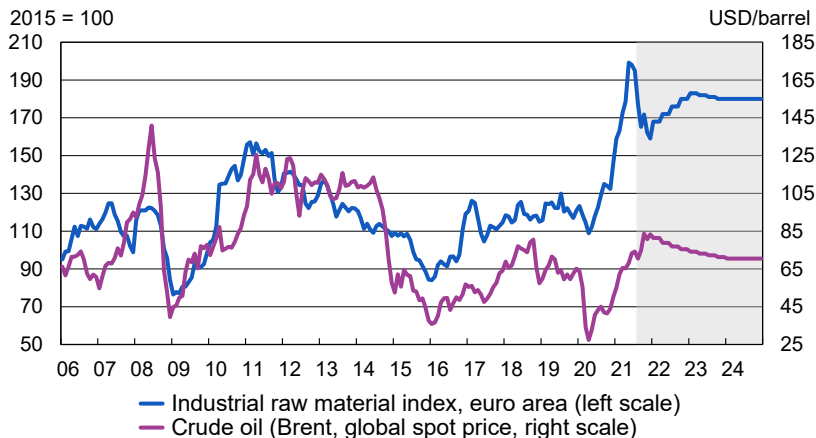
The situation in the financial markets is quite calm despite potential risks. New records have been made in the stock markets this year but the valuation levels do not seem, apart from some exceptions, to be generally unreasonable. On the basis of the reported results and balance sheet information, the situation of banks in Europe is still improving although there is uncertainty associated with the quality of balance sheets due to the COVID-19 crisis. The euro has weakened against the US dollar due to the different outlook of monetary policy and economy as well as the expected interest rate path. The omicron virus variant increased the VIX volatility index somewhat and,

on a more general level, it can be estimated that the COVID-19 pandemic, alongside inflation, will cause market volatility for quite some time to come. The realisation of risks in the Chinese real estate sector could also cause global repercussions.

Short-term market interest rates have been rather stable for a longer period of time. The interest rates of the key euro area countries' government bonds are again negative as expectations regarding a change of monetary policy have subsided. However, both short-term and long-term interest rates will rise moderately during the outlook period.

Crude oil prices have again been at a high level, reflecting the uncertain outlook of the global economy. However, supply is expected to increase as restrictions are gradually lifted and crude oil future prices are on their way down during the outlook period. Natural gas prices in Europe have decreased slightly from their historically high level. The prices of industrial raw materials have come down from the summer's peak level and will remain relatively high during the outlook period.

Raw material prices

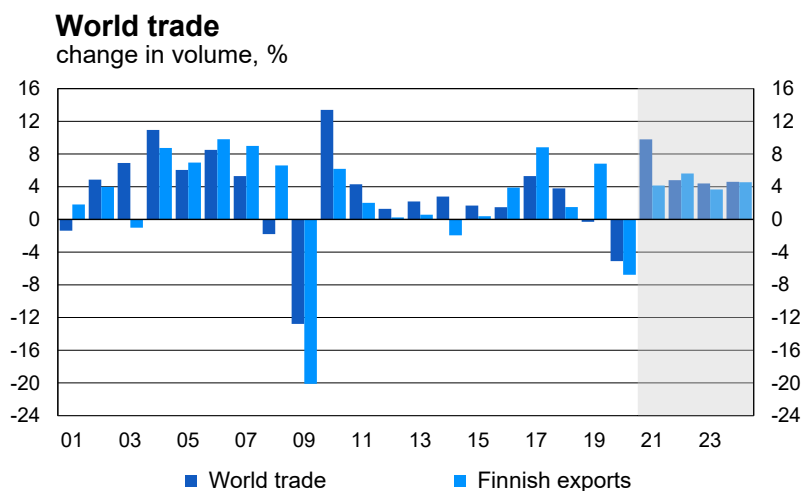


Sources: Hamburgisches WeltWirtschafts Institut, Macrobond, MoF

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1.1.2 World trade

World trade growth prospects are weakened by distribution chain disturbances resulting from various reasons as well as by the slowing down of the growth of the global economy. In the euro area, the goods trade outlook is weaker than in the United States or emerging economies. Goods trade will grow by 4.8% in 2022 and by 4.4% in 2023. In 2024, trade recovers and reaches 4.6% growth.



Sources: CPB Netherlands Bureau for Economic Policy Analysis, Statistics Finland, MoF VM34170

1.1.3 Risks

Risks associated with the development of the global economy are slightly more skewed to the downside than previously assessed. The omicron virus variant, detected in November, has quickly spread to all continents and may slow down economic growth on a broad front. Distribution chain disturbances may continue longer than predicted and further accelerate inflation. The prolongation of inflation may increase cost pressures more extensively in different economies. The tight situation on the energy markets may also become prolonged.

Upside risks include consumers' and companies' unexpectedly optimistic view of economic developments in industrialised countries and the faster progress of vaccination programmes also in developing countries.

Table 4. Gross domestic product

	2019	2020	2021	2022**	2023**	2024**
	change in volume, %					
World (PPP)	3.0	-3.2	6.1	4.6	3.4	3.0
Euro area	1.6	-6.5	5.1	4.5	2.0	1.6
EU	1.9	-6.0	4.8	4.1	2.0	1.6
Germany	1.1	-4.9	3.6	4.5	1.9	1.6
France	1.8	-8.0	6.0	4.4	2.0	1.5
Sweden	2.0	-2.9	4.3	2.9	2.2	1.9
United Kingdom	1.7	-9.7	6.7	4.6	1.4	1.3
United States	2.3	-3.4	5.6	3.4	2.2	2.0
Japan	-0.2	-4.7	2.4	1.1	0.5	0.5
China	6.0	2.3	7.8	6.1	5.5	5.0
India ¹	4.1	-7.4	7.5	6.5	7.1	5.5
Russia	2.0	-3.0	4.3	2.0	1.2	1.0

¹ Fiscal year

Sources: Statistical authorities, MoF

Table 5. Background assumptions

	2019	2020	2021	2022**	2023**	2024**
World trade growth, %	-0.3	-5.1	9.8	4.8	4.4	4.6
USD/EUR	1.12	1.14	1.19	1.15	1.13	1.11
Industrial raw material price index, EA, € (2015=100)	122.1	124.7	175.1	174.0	181.5	180.0
Crude oil (Brent), \$/barrel	64.1	43.4	71.4	78.1	72.7	70.5
3-month Euribor, %	-0.4	-0.4	-0.5	-0.5	-0.5	-0.4
Government bonds (10-year), %	0.1	-0.2	-0.1	0.0	0.0	0.1
Export market share (2010=100) ¹	99.8	98.1	93.0	93.7	93.1	93.0
Import prices, %	0.4	-5.0	8.7	6.6	1.7	2.2

¹ Ratio of export growth to world trade growth

Sources: CPB, Macrobond, HWWI, Statistics Finland, MoF

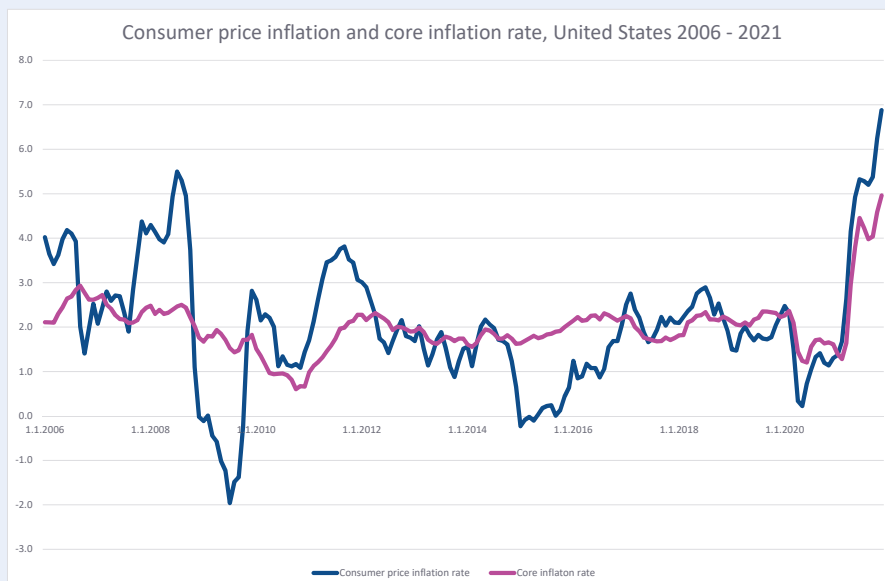
The acceleration of inflation is caused by factors related to supply and demand

Inflation measures the increase in the prices of goods and services in economy. Inflation occurs when prices increase due to an increase in production costs, such as raw material prices, wages and salaries. An increase in demand for products and services may cause inflation as consumers are ready to pay more for the product. Inflation may also accelerate as a consequence of intensive fiscal stimulus. Inflation can be regarded as income transfer from economic agents with assets to those with debt: the value of accumulated assets, on the one hand, and the real value of debt, on the other, decrease simultaneously.

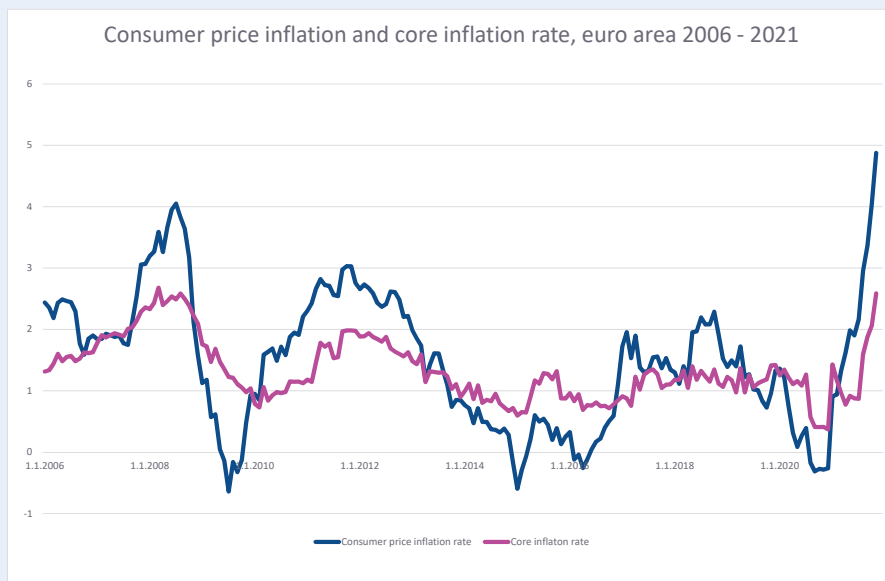
The prices of goods and services change constantly. Some prices increase, some decrease. Inflation is when the prices of goods and services increase on a broad front. In this case, the value of the euro decreases and the purchasing power of households declines. Every household has its own consumption habits. Some households drive a car while others solely use public transport. Some eat meat, others don't. When inflation is measured, the weight of different products and services is determined on the basis of the average consumption habits of all households. In the measurement of inflation, all goods and services consumed by households are taken into account.

Lately, inflation has been accelerating globally, which is caused by factors related to both supply and demand. A key demand-related factor is the fact that the savings that consumers have accumulated during the COVID-19 pandemic are being channelled to consumption. Supply-related factors include, for instance, disturbances in international trade, particularly in sea transport, due to various issues, such as temporary closures of some ports, weather conditions and the shortage of containers, machinery and labour in ports, and the shortage of components that affects the automotive and electronics industries in particular. The increase in key raw materials has also accelerated price increases, in particular in producer prices.

In the United States, inflation rose to 6.9 % in November 2021. Core inflation, or inflation excluding energy and food prices, which are highly volatile, has also increased rapidly. Massive fiscal stimulus, especially direct support to consumers, has increased consumption and, consequently, accelerated inflation.



In the euro area, inflation has accelerated rapidly over a short period of time. According to preliminary figures, in November 2021, inflation measured with the harmonised index of consumer prices was 4.9% and core inflation was 2.6%. Accelerated inflation is caused by development similar to that of the United States. Private consumption has increased rapidly after the COVID-19 crisis and led to price increases at the same time when supply constraints increase price pressures. Another factor influencing the price development in the euro area is the rapid rise in energy, especially electricity, prices; indeed, this has dominated inflation development in recent months. Wages and salaries in the euro area have not reacted to accelerating inflation and real earnings are declining in 2021. In the euro area, inflation was at its slowest at the end of 2020, when prices decreased by 0.3%. Deflation lasted for five months. Currently, prices in the euro area are increasing rapidly precisely due to the low level in the comparison period, but according to the Commission's estimate, the price level trend has exceeded the level of the pre-pandemic period.



In Finland, inflation has picked up during the current year and, according to the flash estimate of the harmonised index of consumer prices, inflation reached 3.4% in November 2021. When measured with domestic consumer prices, inflation development has been faster. The harmonised consumer price excludes prices of dwellings, which have recently risen rapidly. In November, the energy price component was the factor that accelerated inflation most. The increasing amount of savings accumulated in Finland during the COVID-19 pandemic has been channelled to trade in durable goods starting from late 2020. In particular, demand for goods related to construction and renovation has increased rapidly. The prices of these products have risen clearly. In Finland, inflation was at its slowest in April 2020, when prices decreased by 0.4%.

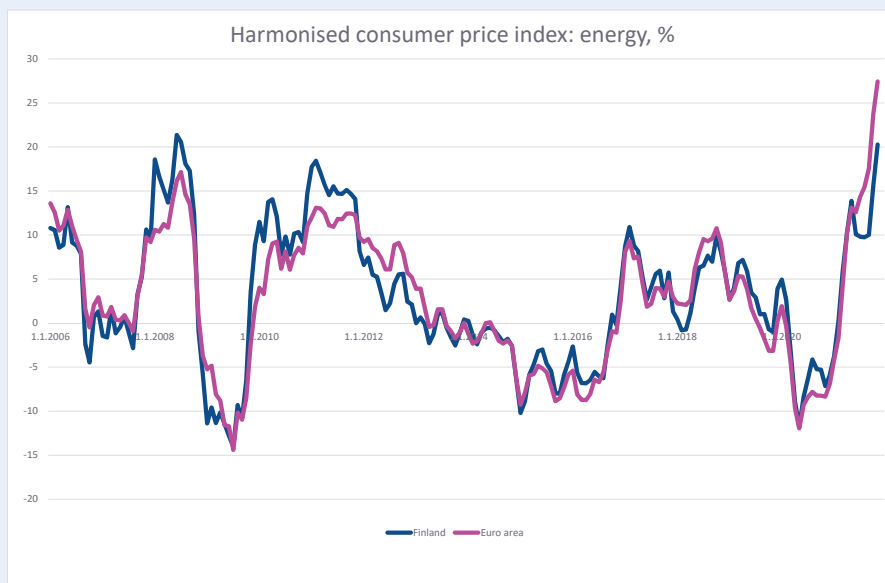
Inflation has increased slightly more slowly in Finland than in the euro area. In Finland, the measured increase in the prices of goods is lower than that of the euro area. The prices of goods have declined in Finland starting from 2015 whereas in the euro area, they have continued to rise steadily.

The COVID-19 crisis treated countries differently and the speed of demand recovery has also varied. In the euro area, the release of demand has been harder and more comprehensive than in Finland, which has led to more extensive price pressures.

Rising energy prices are a key factor

Perhaps the most important factor behind the acceleration of inflation during the past few months has been the increase in energy prices. In the third quarter of the current year, it explained approximately half of the increase in prices in the euro area. Energy price increases influence consumers directly (through electricity and petrol prices, for instance) but also indirectly as a result of rising costs in companies.

Households in the euro area use a larger share of their income for electricity and energy. As a result, an increase in electricity and energy prices has a stronger impact on inflation in the euro area than in Finland. Energy prices, especially electricity, have risen earlier and faster in the euro area than in Finland. Service prices rose in Finland already early in the year whereas in the euro area, they have risen only in recent months. Consequently, core inflation in the euro area became slightly higher than in Finland.



Crude oil prices have risen quite steadily since spring 2020. The OPEC+ countries (including Russia) have maintained crude oil prices at a high level by restricting production but they are now in the process of gradually lifting these restrictions. Starting from January 2022, oil future prices are on their way down. Natural gas prices have risen due to various factors, such as declining storages, the decrease in natural gas supply from Russia to Europe and the strong demand for gas (especially liquefied natural gas) in Asia. The International

Energy Agency (IEA) has estimated that Russia has capacity to increase gas exports to Europe by approximately 15%. The coming winter season will be challenging but starting from spring 2022, gas future prices are falling.

Electricity prices have also risen in recent months and the cold weather has further increased the price. In the electricity market, price fluctuations even within a single day have been very strong in the past few weeks, which is explained by the temporary deployment of more expensive production plants due to the increased demand. In many European countries, electricity is generated with natural gas, especially as countries are seeking to abandon the use of coal. Unfavourable weather conditions have limited the generation of renewable energy (particularly wind and solar power) in some European countries. The lower-than-usual water reserves in the Nordic countries have limited hy-dropower generation.

The acceleration of inflation is still considered a temporary phenomenon

The acceleration of inflation is estimated to be a temporary phenomenon and inflation will again slow down starting from the second half of next year. According to the IMF's forecast, inflation will return to the pre-pandemic level roughly in mid-2022 in both industrialised countries and emerging economies. The latest forecasts by the European Commission and the OECD also show that inflation is expected to slow down significantly towards the end of 2022.

In the Commission's autumn forecast, the reaction of wages and salaries to inflation remains minor as the European labour market is not tight. However, the increase in nominal earnings in the euro area is expected to exceed the overall inflation rate in 2022 and 2023, which means that the increase in real earnings will accelerate. However, the increase in wages and salaries is expected to remain subdued as the labour market shows no signs of becoming significantly tighter.

Thus far, inflationary expectations would seem to be based on solid macroeconomic factors¹. However, concerns have emerged quite recently regarding the continuation of inflationary expectations for a longer time in the medium term. Both market-based and survey-based inflationary expectations rose during the autumn but are still in line with the inflation targets. Concern about inflation-boosted wage and salary costs is also closely associated with the increase of inflationary expectations. A price-salary spiral in the economy would be a self-feeding longer-term phenomenon.

¹ According to the IMF, the anchoring of inflationary expectations means that expectations are stable for a longer term into the future, their dispersion is minor, they do not react to macroeconomic news and they are close to the central bank's target.



1.2 Foreign trade

1.2.1 Exports and imports

In 2021, world trade recovered from the COVID-19 pandemic. Strengthening of the global economy and stimulus measures will boost both exports and imports, especially in the early years of the outlook period. However, the shortage of components and other intermediate products is slowing down companies' ability to meet the growing demand globally. The strong growth of export and import prices will also mitigate the development of export and import volumes particularly in the early years of the outlook period. In sectors particularly hard hit by the crisis, such as tourism, recovery will be further delayed as the COVID-19 pandemic is discouraging travel.

In 2021, both exports and imports of goods are expected to grow rapidly and the growth will continue strongly into 2022. The growth of foreign trade in services is still delayed especially by the slow recovery of tourism combined with the slow recovery of transport. In 2022, rapid growth in foreign trade in services is expected as the

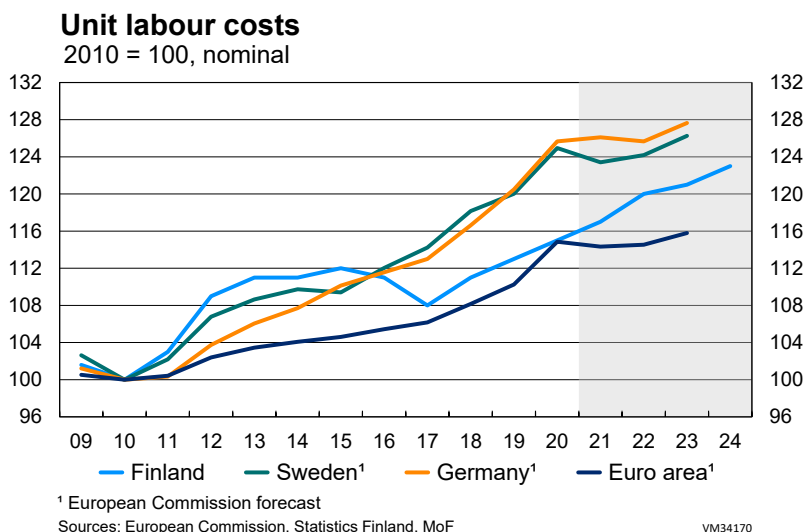
easing of restrictions and uncertainty will boost growth particularly in crisis sectors. In 2023, increase in foreign trade in goods and services will slow down but will continue on a growth path. Growth will accelerate again in 2024 driven by world trade.

Supported by strong export demand, export volumes are expected to increase by 4.2% in 2021 although recovery early in the year was slightly weaker than expected. Strong export growth will continue in 2022 and a growth rate of 5.6% is expected. Growth will be generated especially by the recovery of services. The rate of export growth will slow down in 2023, to 3.7%. In 2024, exports will accelerate to 4.5% driven by world trade.

The import recovery profile follows the export recovery profile. Import volume is estimated to increase by 3.7% in 2021, driven especially by goods. Uncertainty created by coronavirus variants will postpone the recovery of service imports until 2022 and, as a result, imports in 2022 are expected to increase by 4.9%. The rate of import growth will slow down in 2023, to 3.5%. In 2024, imports will accelerate to 4.6%.

Table 6. Foreign trade

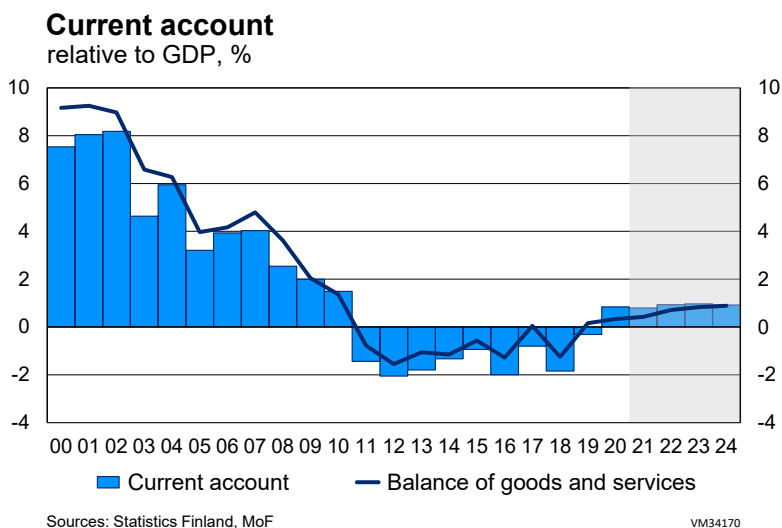
	2019	2020	2021	2022**	2023**	2024**
	change in volume, %					
Exports of goods and services	6.8	-6.8	4.2	5.6	3.7	4.5
Imports of goods and services	2.3	-6.5	3.7	4.9	3.5	4.6
	change in price, %					
Exports of goods and services	-0.3	-4.2	8.3	6.7	1.8	2.4
Imports of goods and services	0.4	-5.0	8.7	6.6	1.7	2.2



1.2.2 Prices and current account

The prices of industrial raw materials and capital goods have increased rapidly in 2021, which is reflected in the prices of exports and imports of goods. In 2021, export prices are expected to increase by 8.3% and import prices by 8.7%. While the prices are expected to grow more slowly in 2022, the upward trend in both export and import prices will continue towards the end of the outlook period. In 2022, export prices are expected to increase by 6.7% and import prices by 6.6%. After this, price increases will level off in both export and import prices but the upward trend will continue.

In 2020, current account started to show surplus as services account deficit decreased. Current account surplus was increased by the increase in foreign trade surplus generated by the moderate growth of imports and the improvement of the terms of trade. The ECB's profit distribution prohibition for banks ended at the end of September 2021, after which Finnish banks have distributed dividends. Factor incomes and income transfers account will show a surplus of 0.4% in relation to the GDP but became more balanced towards the end of the outlook period and in 2024 the account is in state of balance. The balance of goods and services will remain in surplus in 2021 and towards the end of the outlook period. The surplus will mainly result from an increase in goods exports while service imports will remain proportionally lower. The current account will show a surplus of 0.8% in relation to the GDP in 2021, driven by goods and services. In 2022, 2023 and 2024, surplus in relation to the GDP will remain nearly unchanged (0.9%, 1.0% and 0.9%).

**Table 7.** Current account

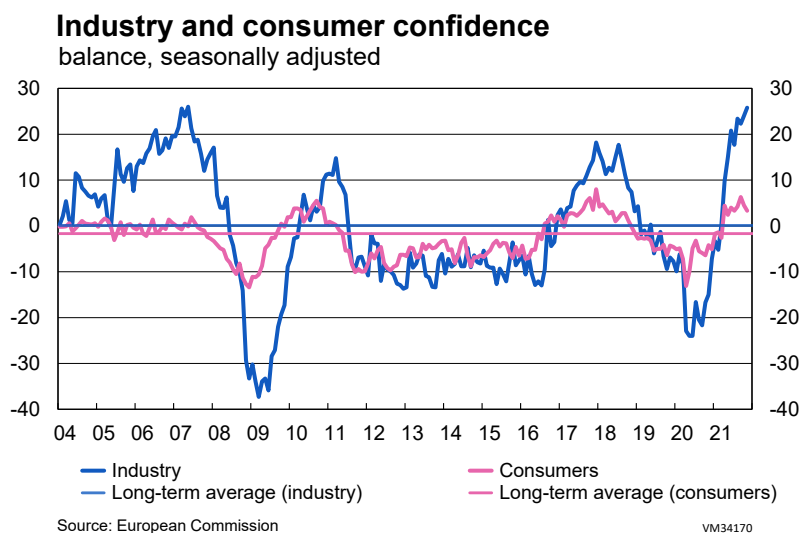
	2019	2020	2021	2022**	2023**	2024**
	EUR bn					
Balance of goods and services	0.4	0.8	1.0	1.9	2.2	2.4
Factor incomes and income transfers, net	-1.1	1.2	1.0	0.6	0.4	0.1
Current account	-0.7	2.0	2.0	2.4	2.6	2.6
Current account, relative to GDP, %	-0.3	0.8	0.8	0.9	1.0	0.9

1.3 Domestic demand

1.3.1 Private consumption

Private consumption increased by 2.7% in January–September 2021 year-on-year. Consumption increased slower than expected during the third quarter, but with the consumption figures for early 2021 adjusted upwards, private consumption has mainly developed in accordance with the September forecast.

The household debt ratio has continued to increase, exceeding 135% during the second quarter of 2021. The debt ratio is particularly increased by the rapid increase in households' housing loan base.



Consumers' confidence in their own economy remained very high in November as well. In particular, consumers' estimate of the current state in their own economy has strengthened substantially compared to the first half of 2021.

Boosted by an improvement in the employment situation, the wage bill continued to grow clearly in the third quarter.

The growth in retail trade and sales of motor vehicles came to a halt in the third quarter, but the sales volume was nevertheless clearly higher than a year earlier.

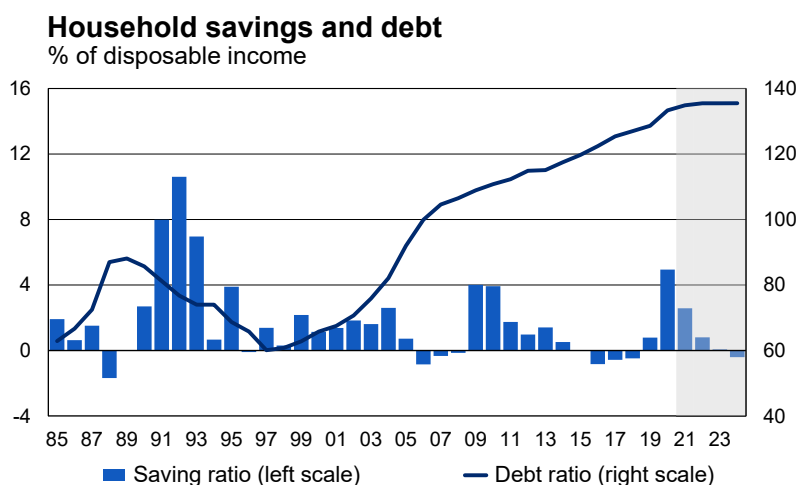
A high savings rate and solid confidence among consumers in their own economy create a basis for rapid growth in private consumption. Private consumption will increase by 3% in 2021, even though the deteriorated COVID-19 situation will slow down the growth in consumption during the fourth quarter.

In 2022, private consumption will grow by 3.8% and will exceed the pre-COVID-19 levels. Following a decreasing savings rate, growth in consumption will slow down to 2.1% in 2023.

Consumption of durables has already exceeded the 2019 levels, and as a result, the growth is expected to remain moderate during the outlook period. The consumption of semi-durables turned to growth in early 2021, and strong growth is expected to continue until the end of 2022.

The consumption of non-durables increased at an exceptionally high rate in 2020, as the consumption of food and electricity at home was boosted by remote work and a decrease in travel. The growth in the consumption of non-durables is estimated to slow down during 2022 as the COVID-19 pandemic wanes.

The consumption of services turned to growth during the second quarter of 2021, and the growth grew stronger in the third quarter. The growth is expected to slow down temporarily in the fourth quarter due to the pandemic growing stronger, but the consumption of services will strengthen again in early 2022 with the expanding use of the vaccination passport and increasing vaccination coverage. Foreign travel is expected to return to pre-crisis levels during 2022.

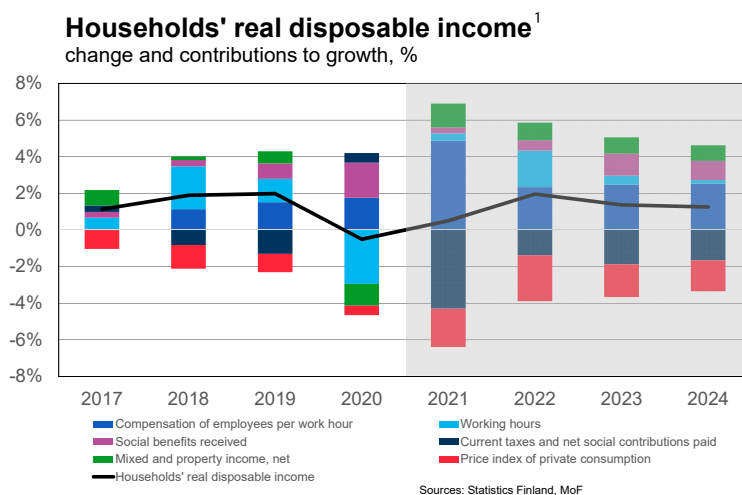


Sources: Statistics Finland, MoF

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A rapid decline in the savings rate is expected in the next few years as most of the savings will be released for consumption. Household consumption will catch up disposable income in 2023, as the savings rate closes zero.

The household debt ratio increased rapidly in 2020 as the disposable income did not increase at all and the debt stock increased by 2.9%. The growth rate of household's housing loan stock accelerated further in 2021, which will also increase the debt ratio in 2021.



Household real disposable income is expected to increase by 0.5% in 2021 as the employment situation improves and average earnings rise. The rise in average earnings will be boosted by the elimination of the reduction in employers' pension insurance contributions in 2021 and the increase in unemployment insurance contributions in 2021 and 2022.

An increase in hours worked and average earnings will give a further boost to purchasing power in 2022. Private consumption prices are estimated to rise by approximately 2% this year and by 2.5% in 2022. The sudden increase in energy prices in late 2021 lifts consumer prices with a delay, as most of the households' energy contracts are not tied to spot prices.

¹ The contribution from paid taxes and social security contributions as well as the price of private consumption are shown with negative sign, as any increase in these items reduces the real disposable income of households.

Table 8. Consumption

	2020	2019	2020	2021	2022**	2023**	2024**
	share, %	change in volume, %					
Private consumption	100.0	0.7	-4.7	3.0	3.8	2.1	1.7
Households	95.8	0.8	-4.8	3.0	3.8	2.1	1.7
Durables	8.1	3.2	2.4	6.1	2.3	2.0	4.0
Semi-durables	7.0	3.3	-10.7	9.2	5.0	2.0	2.5
Non-durable goods	28.8	-0.6	2.0	1.8	0.5	0.9	0.9
Services	51.9	1.3	-7.8	2.3	5.5	2.5	1.7
Consumption by non-profit institutions	4.2	-2.8	-2.4	2.5	3.0	2.0	1.8
Public consumption		2.0	0.5	3.3	0.7	-1.2	0.4
Total		1.1	-3.1	3.1	2.8	1.1	1.3
Households' disposable income		3.0	0.0	2.6	4.5	3.2	3.0
Private consumption deflator		1.0	0.5	2.1	2.5	1.8	1.7
Households' real disposable income		2.0	-0.5	0.5	2.0	1.4	1.3
		%					
Consumption in relation to GDP (at current prices)		75.6	75.5	75.4	75.4	75.1	75.0
Household savings ratio		0.8	4.9	2.6	0.8	0.1	-0.4
Household debt ratio ¹		128.6	133.3	134.9	135.5	135.5	135.5

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

1.3.2 Public consumption

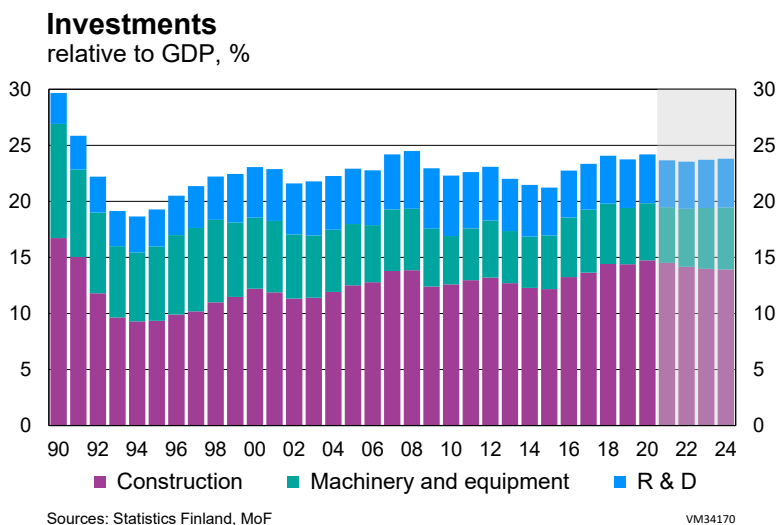
The largest items in public consumption expenditure are personnel expenses, and goods and services purchased. Local government consumption accounts for about two thirds and the central government for one quarter of public consumption, while consumption by social security funds makes up the remainder. In 2023, a significant proportion of municipal and joint municipal authorities' consumption will be transferred to wellbeing services counties.

Public consumption expenditure is expected to grow more rapidly this year than in 2020. The COVID-19 epidemic and its prevention by means of protective equipment, testing, tracing and vaccines have been significant expenditure items in general government finances. On the other hand, the crisis has generated simultaneous savings in some public functions due to restriction measures, for instance. In 2022, public consumption expenditure will grow more slowly as the additional spending prompted by the COVID-19 epidemic decreases, even though some of the appropriations budgeted for 2021 will be postponed to be used next year. However, the reduction of the service and care backlog generated during the epidemic causes increasing expenditure pressures.

The value of public consumption expenditure will continue to grow in 2022–2024, even though the volume of consumption will decline in 2023 with the end of the government term and the additional expenditure come to an end. Public sector collective agreements will expire at the end of February 2022. In the forecast, public sector earnings trends are expected to reflect the estimate of the overall earnings trends from 2022.

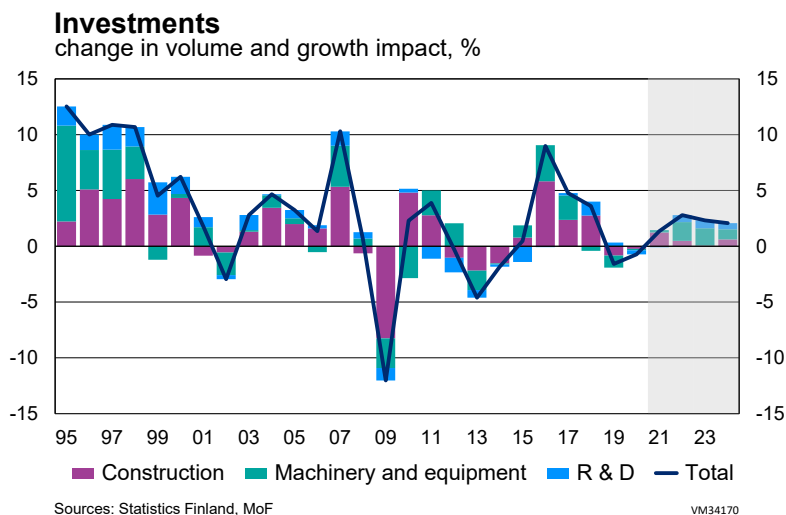
1.3.3 Private investment

Investments grew during the first three quarters of 2021, driven by investments in housing construction. In other investment sub-items, growth has been subdued or negative. However, private investments will grow by 3.6% in accordance with the forecast this year. The estimate of the growth in residential construction investments is now more optimistic than before. Other construction will also pick up starting in 2022, and there are signs of recovery in machinery and equipment investments as the growth prospects for the global economy are improving. The investment prospects for Finnish industries are good, and the funding from the Recovery and Resilience Facility of the EU (RRF) will boost private investments, especially in the period 2022–2023. During the subsequent outlook years, private investments will grow by 3.1% in 2022, 2.6% in 2023 and 2.5% in 2024. Private investments will grow at an average rate of 2.9% during the entire outlook period, which means that their ratio to GDP will reach nearly 20% in 2024.



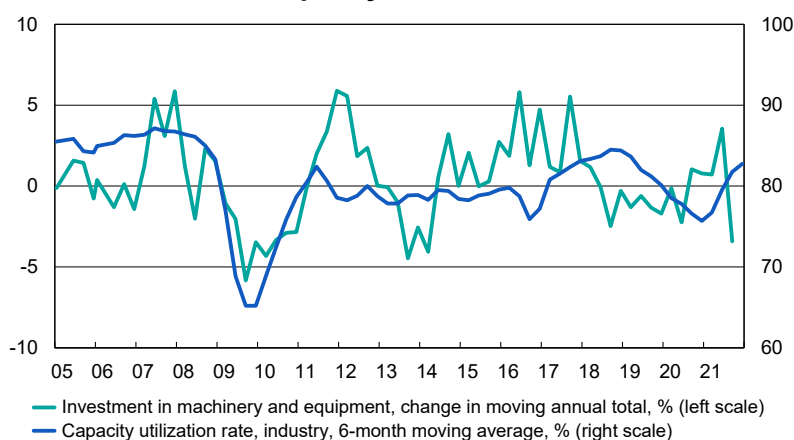
In 2021, the trend in housing construction in particular has been positive. There will be more housing starts in 2021 than previously anticipated. Housing starts will increase to more than 44,000, and renovation construction is also expected to grow at a slightly faster rate than last year. Overall, housing construction investments will grow by 6.5% in 2021. Housing construction will contract by one per cent in 2022 but housing starts will continue to be at a high level at about 38,000 new apartments. Towards the end of the outlook period, housing starts will gradually approach the long-term average and a decline of 2.2% is expected in 2023 and an increase of 1.0% in 2024. The demand for housing loans and housing construction will be sustained by low interest rates.

Non-residential building construction investments will grow by 4.5% in 2022. Commercial construction will turn to growth and industrial investments on the whole will increase. For example, Metsä Group has now launched its bioproduct mill project in Kemi. In non-residential building construction, positive development will continue in 2023. Non-residential building construction will grow by 2.5% in 2023 and 1.0% in 2024. As other construction, civil engineering construction will also grow throughout the outlook period, except for 2021. Boosted by the positive trend in building construction starts, civil engineering construction will grow by 2.2% in 2022. The growth will slow down towards the end of the outlook period.



Machinery, equipment and transport equipment investments recorded sluggish growth in the first three quarters of 2021. In part, this was due to export sales relating to transport equipment investments, recorded as negative investments, in the third quarter. Investments in machinery and equipment will grow by 8.0% in 2022 as the business environment becomes more stable. Machinery and equipment investments will be boosted by industrial investments. Substantial investments in machinery and equipment will be made at the Kemi bioproduct mill, for example, in the outlook period. This means that the positive trend in industrial investments will continue beyond 2022. Investments in machinery and equipment will grow by 7.0% in 2023 and by 4.0% in 2024. Other investments (including RD investments) will grow throughout the outlook period, except for 2021. During the outlook period, RDI investments will be supported from such instruments as the Recovery and Resilience Facility (RRF).

Investment and capacity utilization rate



Sources: Statistics Finland, Confederation of Finnish Industries

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Table 9. Fixed investment by type of capital asset

	2020	2019	2020	2021	2022**	2023**	2024**
	share, %	change in volume, %					
Buildings	51.5	-0.7	-2.3	2.6	0.5	-0.2	1.0
Residential buildings	29.3	-4.2	-2.5	6.5	-2.2	-2.2	1.0
Non-residential buildings	22.3	4.5	-2.0	-2.6	4.5	2.5	1.0
Civil engineering construction	9.4	-5.3	10.7	-1.0	2.2	1.8	1.2
Machinery and equipment	21.1	-4.9	-0.6	1.0	8.0	7.0	4.0
R&D-investments ¹	18.0	1.9	-2.0	-0.5	3.5	4.0	3.0
Total	100.0	-1.6	-0.7	1.4	2.8	2.3	2.1
Private	79.6	-2.4	-3.4	3.6	3.0	2.6	2.5
Public	20.4	2.4	11.0	-7.4	1.7	1.2	0.3
		%					
Investment to GDP ratio (at current prices)							
Fixed investment		23.7	24.2	23.7	23.5	23.7	23.8
Private		19.4	19.3	19.2	19.2	19.3	19.5
Public		4.4	4.9	4.4	4.4	4.4	4.3

¹ Includes cultivated assets and intellectual property products

1.3.4 Public investment

Public investments account for about 20% of all investments. Local government investments account for more than half of the total and central government a little less than a half. The proportion of social security funds is very small. From 2023 onwards, local government investments will be partially transferred to wellbeing services counties. These investments account for about 10% of all public investments. Almost 30% of all public investments are civil engineering investments, and other construction investments account for a same proportion of the total. Research and development investments account for slightly more than 25% and machinery and equipment investments for slightly over 10% of the total. Public investments have been high in recent years, accounting for over 4% of GDP. In Finland, public investments account for a considerable higher proportion of GDP than in EU countries on average.

The stimulus measures launched by Prime Minister Marin's Government and the measures set out in the Government Programme have raised public investments to a higher level than before. Central government investments have been boosted by transport infrastructure projects as well as research, development and innovation inputs. Public investments increased considerably in 2020, thereby evening out the economic cycle as the economy contracted and private investments decreased. Public investments increased by as much as 11%, particularly owing to considerable investments by the central government. Central government investments in buildings and weapons systems increased significantly. Local government investments also increased at a relatively rapid rate, albeit slower than in previous years. The growth in local government investments mainly concerned infrastructure investments.

Public investments will decrease in the current year, with coronavirus pandemic-related procurement by the central government decreasing compared to the year before. Local government capital expenditure remains at a high level, but after years of uninterrupted growth, investments will be on a par with the previous year. In spite of the considerable decrease in public investment, its share of GDP will continue to be clearly above the long-term average. Also, the share of public investment of all investment is high.

Public capital expenditure is estimated to turn to a slight growth in 2022 due to central government investments picking up. Local government investment is estimated to decrease slightly next year, although investment will continue to be at a high level.

Public investments are expected to grow moderately at the end of the outlook period. Investments in defence materiel will increase the central government's capital expenditure. Local government investment, on the other hand, will be decreased, particularly by the slowing down of the construction of hospitals. The investment peak in hospital construction is coming to an end, but new investments are still expected in several hospital districts.

1.4 Domestic production

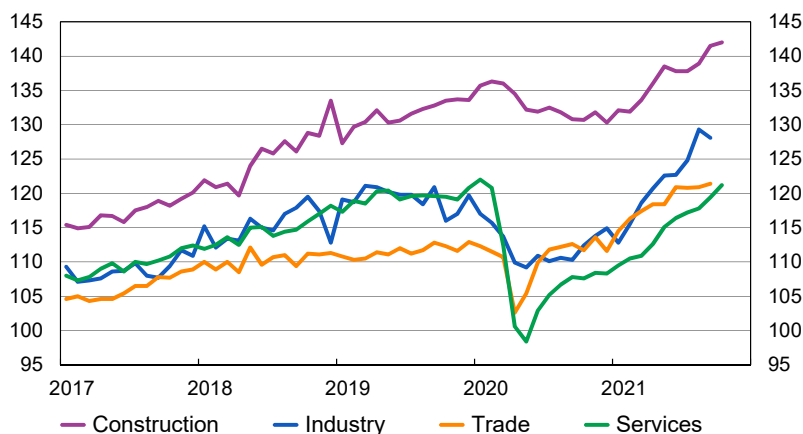
1.4.1 Total output

Good growth in the national economy continued during the third quarter of the year, even though the growth rate slowed down compared to the second quarter. Of the main sectors, services has developed the best during the current year. This is natural, as they also contracted the most in 2020. Construction and industries also grew during the all three quarters. Primary production, on the other hand, did not turn to growth until the second quarter, but its growth rate accelerated significantly in the third quarter due to strong demand in the forest industry, resulting in favourable overall development for the entire year.

The prices of production inputs, as well as the prices of finished products, developed at a fast rate in the current year. These trends are also visible in the development of the turnover of the main sectors. A rapid increase in producer prices and a shortage of components have been the main challenges facing companies, and the situation does not seem to alleviate in the short term in this respect. There is also a shortage of skilled labour, especially in the service sector.

Turnover trends in main sectors

2015 = 100, seasonally adjusted



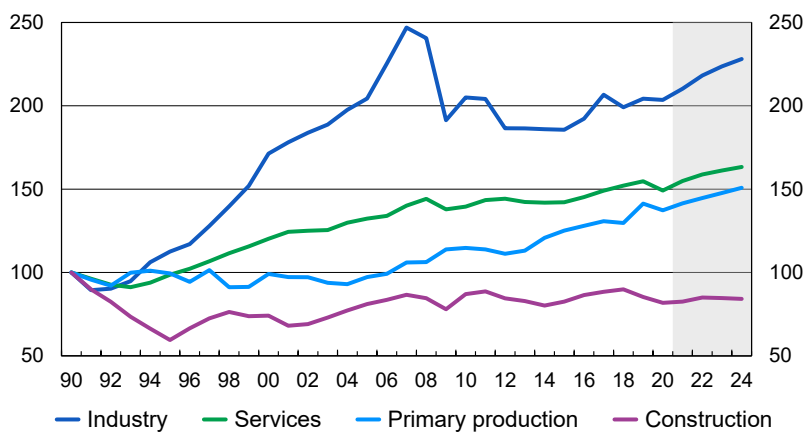
Source: Statistics Finland

Finland's gross domestic product will grow by 3.4% in 2021. In transportation and storage services and accommodation and food service activities in particular, production is far behind the pre-pandemic level. Due to these reasons, among others, economic growth is expected to increase to 3% in 2022. This will require quite brisk growth during the year, however so that the first quarter may grow slower than the other quarters as the worsening of the pandemic increases economic decision-makers' cautiousness. The volume of public services will also increase in 2022 due to the reduction of the service and care backlog generated during the COVID-19 crisis, among other things.

Economic growth will slow down substantially in 2023, with the production of private services having reached the pre-coronavirus crisis level and already growing clearly slower at that time. The volume of public services is also estimated to decrease in 2023. The GDP growth outlook for 2023 is 1.5% and 1.4% for 2024.

Production

1990 = 100



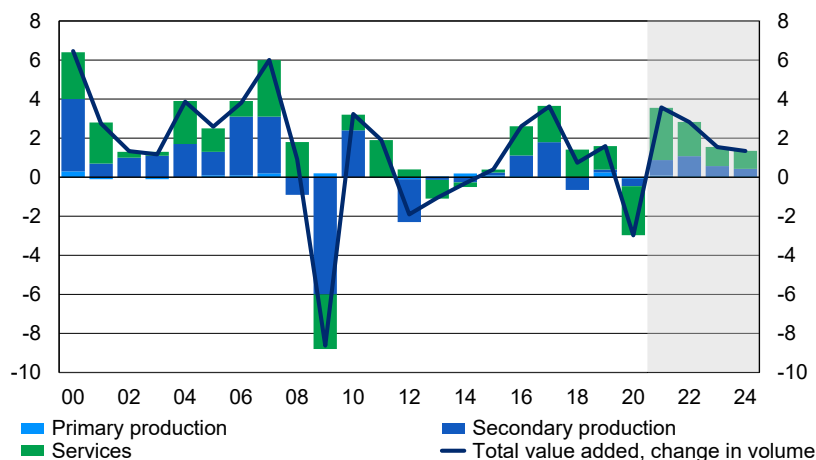
Sources: Statistics Finland, MoF

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Services account for about 70% of Finland's economic output. In the next few years, they will contribute to Finland's GDP growth more than the other main sectors.

Contribution to total production

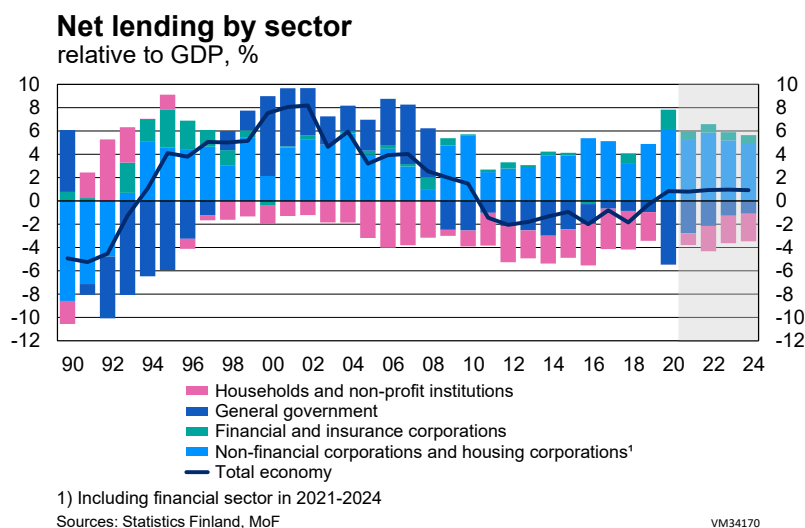
percentage points



Sources: Statistics Finland, MoF

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In 2021, productivity of the Finnish economy per working hour is estimated to increase by 3.2%, after which growth will slow down at an average annual rate of 1% in 2022–2024. The operating surplus is predicted to grow by 4.5% in 2021 and to accelerate further by 5.9% in 2022. After this, the growth in operating surplus will gradually slow down to about 5% in 2023–2024. Unit labour costs in Finland are estimated to increase at an average annual rate of 1.8 per cent between 2021 and 2024.



1.4.2 Secondary production

Total industrial orders have grown strongly and are at an almost unforeseen high level. It is likely that the increase in order prices has also contributed to this. According to the business tendency survey published by the Confederation of Finnish Industries in October 2021, industrial companies continued to expect growth both during the fourth quarter of 2021 and early next year, even though they estimated that the times of the biggest growth were already behind us.

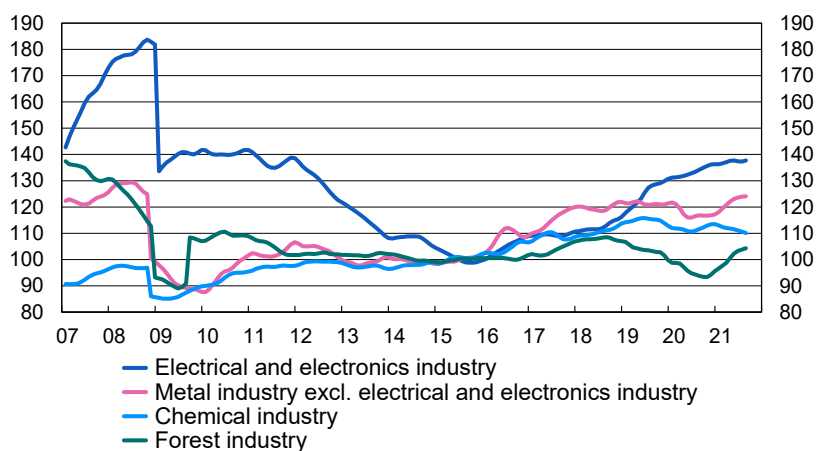
The forest industry's production grew strongly in terms of both volume and value in 2021. The selling prices of pulp and timber have increased strongly. The development in the next few years is also estimated to be positive, even though the growth rate will slow down considerably compared to the current year's very high level.

The development of the chemical industry's production has been poor in 2021. In particular, it has been affected by a major maintenance turnaround of an oil refinery postponed from 2020 to 2021. Order volumes have fluctuated considerably between months, but they have nevertheless been considerably high in 2021. In the next few years, the growth in the chemical industry's production is estimated to first accelerate clearly and then gradually normalize.

The electrical and electronics industry has also developed clearly weaker in 2021 year-on-year. Companies have faced challenges with the availability of components and raw materials. The shortage of skilled labour has quickly become an obstacle to growth. In the next few years, the availability of intermediate products is estimated to improve and facilitate clearly faster growth than in 2021.

Volume index for industrial production

2015 = 100, trend

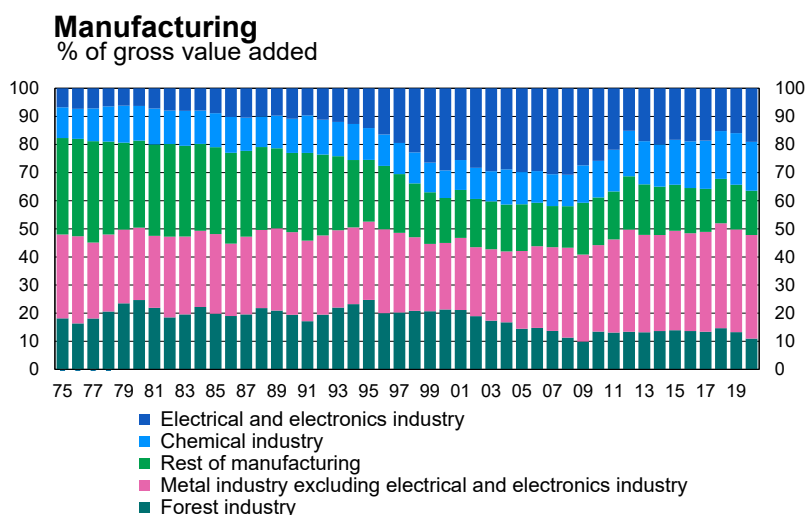


Source: Statistics Finland

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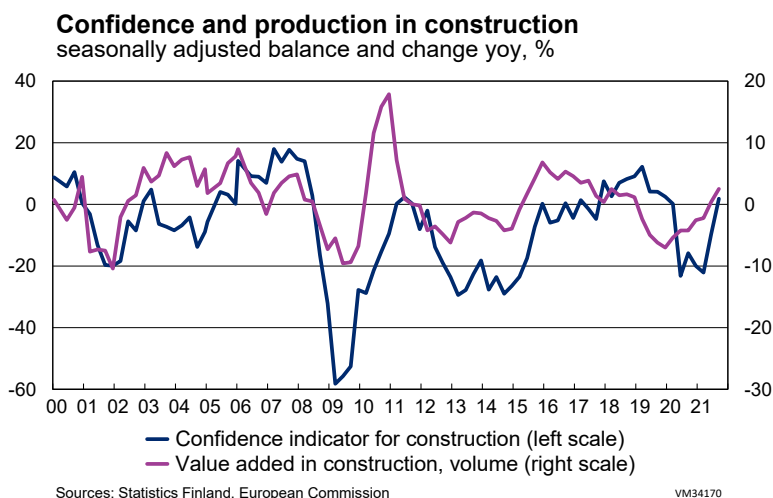
The metal industry thrived in 2021. There has been both domestic and international demand. In particular, the turnover of metal refining has grown strongly; the strong increase in the prices of metal products has contributed to this. Major industrial projects in the next few years and the growing global economy will keep up industrial demand also during the next few years. The metal industry accounts for most of the industrial value added. The chemical industry is the second-largest industrial sector and its size is about 50% of the metal industry.

A broad-based recovery of the global economy is expected to sustain growth in the manufacturing industry throughout the outlook period until 2024. Most of the industrial output is exported. In the last year of the forecast, industrial production will grow at a slower rate and growth will approach the long-term average.



Construction

Housing construction continued to grow strongly in 2021. The total number of starts for 2021 is expected to be about 44,000, which is an exceptionally high figure for Finland. Housing market and renovations have been boosted by an increase in household savings and rising employment. Moreover, investors' interest in housing has continued to be strong. However, it is expected that the number of housing starts will decrease clearly in the next few years, as the supply of housing has increased and there are already lots of vacant rental apartments offered in many places.



The development of the number of building permits granted for non-residential building construction has been quite weak in 2021, which in part conflicts with the good investment plans announced by companies. However, the occupancy rates of offices and commercial premises are still quite low, yet commercial construction continues to be active in the Helsinki Metropolitan Area. Commercial construction is estimated to become the driver of construction during 2022. The new Kemi bioproduct mill will give a significant boost to construction in northern Finland.

Similarly to other industries, the construction industry expects the phase of the strongest growth to be already behind. Construction activity is almost evenly divided between renovation and new construction. The growth rate of renovation is estimated to accelerate in 2021 and 2022 and slightly slow down towards the end of the outlook period in 2023–2024. Renovation construction is expected to grow by an average of about 2% each year during the outlook period.

The volume of civil engineering construction is still estimated to grow only slightly in 2021, even though turnover data at current prices indicate very strong growth. In the next few years, civil engineering construction will mainly develop guided by slowing public investments.

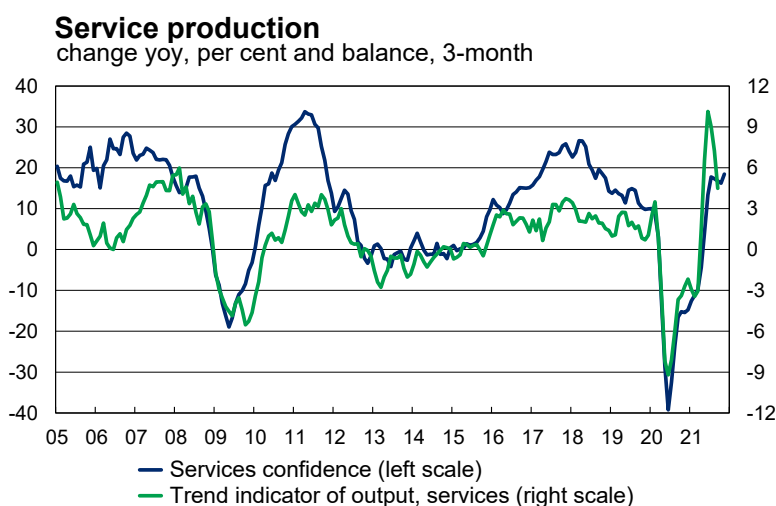
In 2022, the value added of construction will grow the fastest in the outlook period and slow down to a decrease in 2023–2024, primarily due to residential construction returning closer to the normal level.

1.4.3 Services

Service production grew favourably in 2021, and financial and insurance services have grown the fastest. The growth outlook of service production for 2021 is 3.9% which does not require much growth during the remainder of the year. Information and communications remain one of the cornerstones of Finland's service industries and it is also the only industrial sector in our country that has grown continuously for more than ten years. The projected growth in service exports will also increase demand in the information and communications sector. Trade and real estate services will also increase clearly in 2021.

Services are estimated to continue their good growth in 2022. The outlooks of many industries still suffering from the pandemic will brighten then, and the recovery of demand can be swift. The sectors that have suffered the most, such as air and water transport, travel agencies, accommodation and food service activities, arts, entertainment and recreation, will continue to be behind in late 2021 and early 2022. Booster vaccinations and increasingly pent-up demand will gradually increase their growth briskly during 2022. Public service activities will also support the growth in services in 2022.

The development of service confidence continues to be favourable, but according to the business tendency survey published in October, the phase of the fastest growth is behind us. Nevertheless, sales expectations are increasing cautiously.



Sources: Statistics Finland, European Commission

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Growth in services will slow down in 2022, but growth spillover and growth in public demand will keep annual growth at 2.6%. Public services, which include public administration, education, health and social services, make up the largest individual sector in services. The increase in industrial production and household consumption will also boost growth in services extensively in the coming years. Similarly, the strengthening of Finland's export demand in 2023–2024 will also be reflected in the growing demand for business services. In 2023–2024, growth will return close to its long-term average.

Table 10. Production by industry

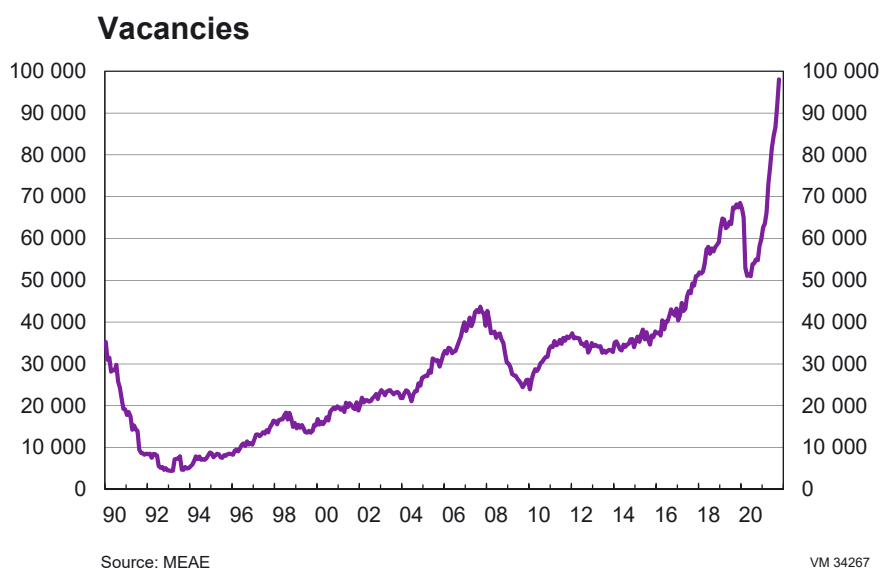
	2020	2019	2020	2021	2022**	2023**	2024**
	share, % ¹	change in volume, %					
Industry	20.3	2.6	-0.4	3.4	3.7	2.5	2.0
Construction	7.5	-5.1	-4.1	1.2	2.9	-0.4	-0.6
Agriculture and forestry	2.8	9.0	-2.8	2.8	2.2	2.1	2.1
Industry and construction	27.8	0.5	-1.4	2.8	3.5	1.7	1.3
Services	69.4	1.7	-3.6	3.9	2.6	1.4	1.3
Total production at basic prices	100.0	1.6	-3.0	3.6	2.8	1.5	1.3
GDP at market prices		1.3	-2.9	3.4	3.0	1.5	1.4
Labour productivity in the whole economy		0.3	-0.0	3.2	0.8	1.0	1.1

¹ Share of total value added at current prices

1.5 Labour force

The number of employed persons increased significantly in 2021. Employed persons numbered 65,000 more in October than a year earlier, and their number increased cumulatively by 2.1% year-to-date. However, the number of employed persons is only higher among fixed-term and part-time employees. The number of permanent full-time employees is still lower than the previous year. In fact, the number of hours worked only increased by 0.4%. Of the main industries, employment has only increased in service industries, with the exception of finance

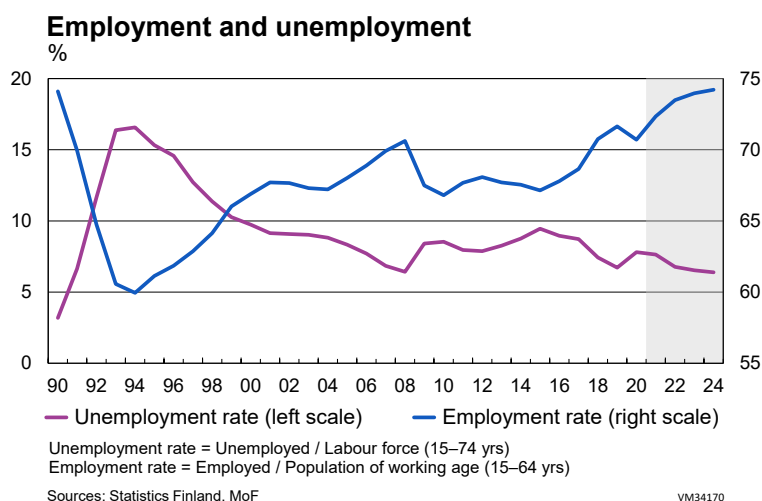
and insurance activities. In secondary production, the number of employed persons decreased. According to the employed persons trend, the number of employed persons has been increasing consistently for a little over a year, and the employment rate was 72.7% in October. The number of unemployed persons has contracted consistently according to the trend only for five years, and the unemployment rate was 7.1% in October. Long-term unemployment has also turned to a decline.



There is a strong demand for labour, and in a number of sectors, the potential is even higher. According to business confidence surveys, employment expectations have risen further in the main sectors during the autumn months. Especially in certain service and manufacturing sectors and construction, shortage of skilled workforce is gradually becoming a problem. In fact, there are plenty of job opportunities on offer, as employers have made a record number of vacancies available through labour administration. The more extensive survey-based statistics on vacancies produced by Statistics Finland also indicate that the number of job vacancies is now high. Jobs with particularly hard recruiting difficulties are found in secondary production industries and information and communications services, and regionally in Western Finland.

Last year, companies adjusted their labour costs through redundancies and lay-offs. In autumn 2021, the number of lay-offs decreased to one-third year-on-year, to the pre-coronavirus level.

Demand for labour is increased by growth in domestic demand, by the strong global economy, and the change in economic structures following a decrease in face-to-face services and increase in digital services. Nevertheless, the fact that the disease will not fully disappear will put the lifting of restrictions on business operations on an uncertain basis and the growth in employment will slow down at the turn of the year. Due to the very rapid increase in employment in the first half of 2021, employment growth will exceed 2% this year, even though the rate of growth has slowed down towards the end of the year. The employment rate will reach 72.4%, partially due to a fall in the number of working-age people.



The demand for labour is sustained by economic growth and in the short term, the demand can be met by the large number of unemployed persons and the government measures to increase the supply of labour. Economic recovery will boost the number of employed persons in 2022–2024, especially in the service sectors. The number of employed persons is expected to increase by 1.5% in 2022. As the economy loses strength, the growth will slow down in 2023 and 2024 but the employment rate will exceed 74% in 2024.

Strong employment growth usually leads to a rapid fall in unemployment. However, this has not happened during the first half of the year as growth in employment has come from outside the labour force. As a result, labour market participation has reached record levels, while at the same time, the number of unemployed has increased. The unusual situation is partly due to a sharp increase in lay-offs last year as many of the laid-off people were entered in the statistics as coming from outside the labour force. This year, laid-off people have been re-employed, which means that there has been no simultaneous fall in unemployment. Over the last few months, unemployment among young males has continued to be more common than a year earlier.

According to Statistics Finland, unemployment was 3.5% higher in the first half of 2021 than in the same period last year. Towards the end of the year, the unemployment trend has turned to a decline, with the continuous increase in employment also contracting the number of unemployed persons. However, the unemployment rate will decrease only slightly to 7.6%, due to the increase during the first half of the year. In particular, the recovery of the service sector next year will speed up the downward trend in unemployment and the jobless rate will fall below 7%. Provided that the labour market mismatches and region-specific or occupation-specific availability of labour does not become an obstacle to the functioning of the labour market (as is assumed in the forecast), the unemployment rate will fall to below 6.5% in 2024. This is still slightly above the level of structural unemployment in Finland estimated using the method jointly prepared by the European Commission.

Table 11. Labour market

	2019	2020	2021	2022**	2023**	2024**
	annual average, 1,000 persons					
Population of working age (15–74 yrs)	4128	4133	4123	4113	4100	4090
change	4	5	-10	-10	-13	-10
Population of working age (15–64 yrs)	3428	3421	3417	3413	3411	3409
change	-11	-7	-4	-4	-2	-2
Employed (15–74 yrs)	2533	2494	2549	2586	2602	2608
of which 15–64 yrs	2456	2419	2472	2508	2523	2530
Unemployed (15–74 yrs)	183	209	210	187	181	177
	%					
Employment rate (15–64 yrs)	71.6	70.7	72.3	73.5	74.0	74.2
Unemployment rate (15–74 yrs)	6.7	7.7	7.6	6.7	6.5	6.4
	1,000 persons per annum					
Immigration, net	15	18	21	21	21	21

1.6 Incomes, costs and prices

1.6.1 Wages and salaries

The rate of growth in nominal wages accelerated by half a percentage point to 2.3% in 2021 compared to the previous year. The acceleration was due to higher negotiated pay increases as wage drifts remained more or less at last year's levels (at about 0.5%). Nominal earnings grew faster in industries and in a number of private business services. At the same time, there was a substantial slowdown in the rate of increase in trade and especially in real estate services. The rate of growth in real earnings slowed down to 0.5% as inflation accelerated to slightly under 2%.

Some of the collective agreements for the previous period have already expired and negotiations on new agreements have commenced. Many of the collective agreements now in effect will also expire around the turn of the year and next spring. During the past two decades, the average duration of collective agreements has been nearly two years. The pay increases set for the first year of these

agreements have usually been higher than the increases set for the last year of the previous agreements. The forecast assumes that the pay increases specified in the agreements in 2022 will follow the trend of the past two decades and that the pay increases will be higher than in 2021. This year, the pay increases specified in the agreements are slightly under 2% on average, and they are estimated to accelerate to slightly over 2% on average next year. Moreover, wage drifts are expected to increase in 2022. Therefore, nominal wages would increase by 2.3% this year and approximately 3% next year.

The increase in earnings for 2023 and 2024 will be linked to the predicted slower growth in productivity. At the same time, an increase in the level of economic activity and the resulting rise in employment as well as labour shortages in some sectors are expected to boost wage drifts. Nominal earnings are expected to increase by about 2.5% in 2023 and 2024.

The wage bill increased by 4.9% year-to-date. The number of employed persons increased this year, especially among wage earners with above-average wages. Thus, the rate of wage bill growth was even faster than the steady rise in employment would have suggested, and especially more than suggested by the development of hours worked. In addition to nominal earnings, the wage bill is also affected by employment trends. As the rate of growth in employment and nominal earnings accelerates, the wage bill is expected to increase by 4.5% this year. Earnings are expected to rise more rapidly next year but employment will probably grow more slowly and thus, the wage bill will increase by about 4.5% in 2022. A slower rise in earnings and growth in employment will also slow down the increase in the wage bill in 2023 and 2024, and that year, the wage bill is expected to increase by about 3%.

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

	2019	2020	2021	2022**	2023**	2024**
	change, %					
Index of negotiated wage rates	2.0	1.3	1.8	2.3	1.8	1.7
Wage drift, etc.	0.1	0.7	0.5	0.7	0.7	0.9
Index of wage and salary earnings	2.1	1.9	2.3	3.0	2.5	2.6
Real earnings ¹	1.1	1.6	0.1	0.4	0.7	0.8
Average earnings ²	2.0	2.4	4.1	2.5	2.6	2.7
Labour costs per unit of output whole economy ³	1.8	1.8	1.7	2.6	0.8	1.7

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.

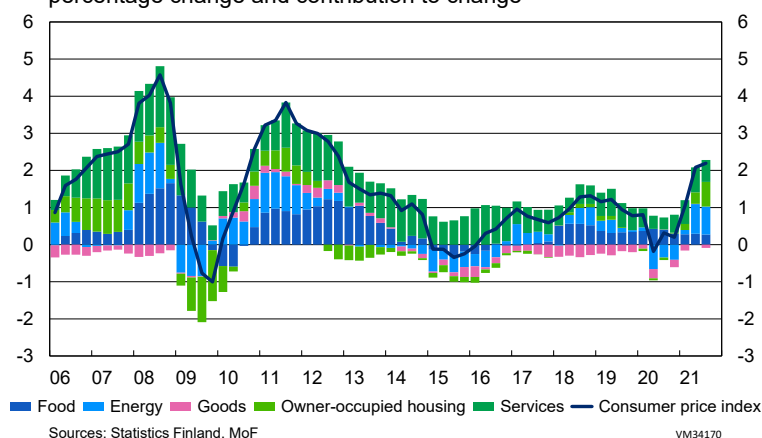
³ Compensation of employees divided by gross value added in volume at basic prices.

1.6.2 Consumer prices

The consumer price index rose by over three per cent during the second half of 2021 year on year. The increase in prices is primarily the result of increasing energy prices. The increase in the price liquid fuels accelerated further in November and increase in electricity prices has been continued. Increasing prices of goods have also begun to be visible as a factor accelerating inflation after the prolonged decrease in prices. Underlying the increasing prices of goods are factors related to both supply and demand. A key demand-related factor is the fact that the savings that consumers have accumulated during the COVID-19 pandemic are being channelled to consumption. In Finland, pent-up household demand has resulted in increasing prices for home renovations and related supplies.

Consumer price index

percentage change and contribution to change



Measured with the national consumer price index, an inflation rate of 2.2% is forecast for 2021. Energy prices will sustain inflation around the turn of the year and will gradually turn to a decline during 2022. In 2022, however, the inflation rate will accelerate to 2.6%.

Increase in service prices is the biggest single factor sustaining inflation in the coming years. Also, food prices are estimated to continue to increase at a rapid rate in the next few years, as the world market prices of food have been rising. The national consumer price index is expected to rise by 1.8% in 2023 and 2024. Core inflation will accelerate moderate, but it will remain under two per cent throughout the outlook period.

Consumer price index and index of wage and salary earnings

change yoy, %

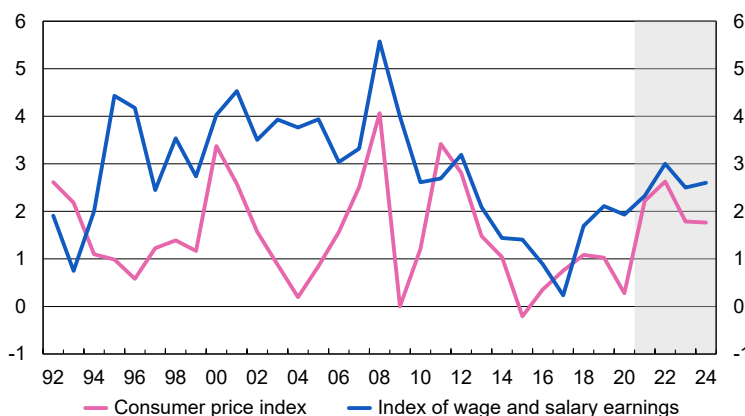


Table 13. Price indices

	2019	2020	2021	2022**	2023**	2024**
	change, %					
Export prices ¹	-0.3	-4.2	8.3	6.7	1.8	2.4
Import prices ¹	0.4	-5.0	8.7	6.6	1.7	2.2
Consumer price index	1.0	0.3	2.2	2.6	1.8	1.8
Harmonised index of consumer prices	1.1	0.4	2.1	2.4	1.9	1.9
Basic price index for domestic supply, including taxes	1.0	-3.3	9.4	6.3	2.2	2.2
Building cost index	1.0	-0.3	5.4	5.6	2.1	2.1

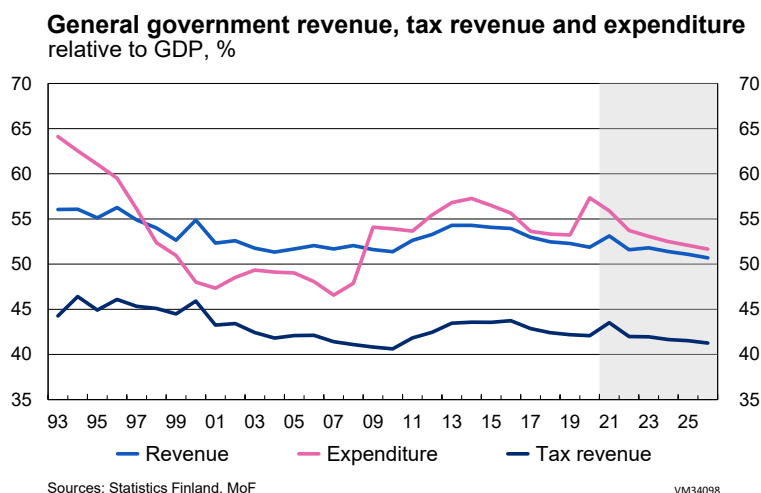
¹ As calculated in the National Accounts

2 General government finances

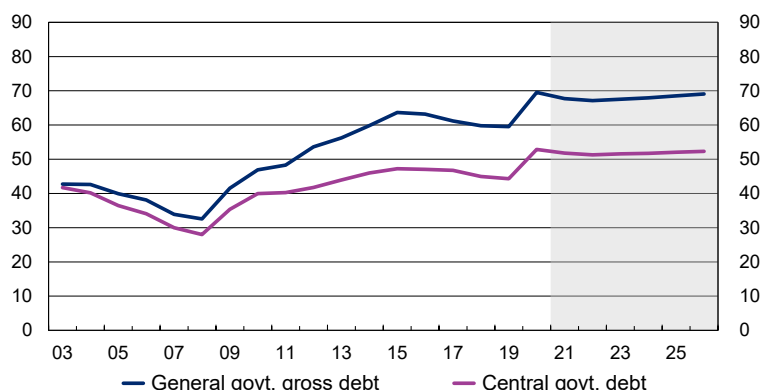
2.1 General government

The general government deficit, which has grown significantly during the COVID-19 pandemic, will decrease rapidly in the next few years. Brisk economic growth and the end of the support measures prompted by the COVID-19 pandemic will strengthen general government finances. However, general government finances will still remain in deficit after a short period of economic upturn. There is a structural imbalance between expenditure and revenue in general government finances.

Last year, the general government debt-to-GDP ratio increased due to the COVID-19 pandemic, reaching a level that was 10 percentage points higher than before the crisis. The increase in the debt ratio will turn to a decline this year, and that decline will continue next year. Strong GDP growth will have a favourable effect on the development of the debt ratio. Updated assessments of the financing of the jet fighter project are also taken into account in general government debt. Under the updated assessment, the need to take on new debt in 2021 and 2022 will be smaller than previously estimated. In the medium term, the debt ratio will start to increase again. The general government debt ratio will remain at a significantly higher level than before the COVID-19 pandemic, which increases the risks related to public finances.



General government debt relative to GDP, %



Sources: Statistics Finland, MoF

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Central government has borne most of the expenses of the support measures prompted by the COVID-19 pandemic. In fact, the central government is the general government sector with the highest deficit. Driven by economic growth and helped by the end of the support measures, the central government deficit will decrease during the outlook period.

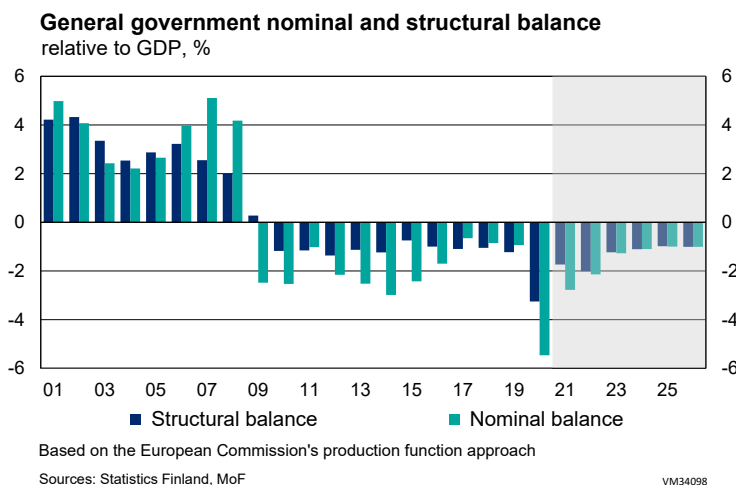
The financial balance in local government will return to a deficit after being in balance temporarily. In 2023, the structure of Finland's general government will change as the responsibility for health and social services and rescue services will be transferred from municipalities to counties. This will ease the structural spending pressures facing municipalities resulting from the ageing population. The counties will start with a slight deficit, which is caused by sizeable investments.

The financial position of employment pension institutions will improve as a result of a strong growth in contributions accompanying a rise in employment as well as the increase in private sector contributions to compensate for the reduced contributions implemented in 2020. The surpluses will, however, remain fairly moderate in the coming years as pension expenditure continues to grow and very low interest rates slow down growth in the institutions' property income. Decreasing unemployment will ease the situation of the other social security funds.

Table 14. General government finances¹

	2019	2020	2021	2022**	2023**	2024**
	EUR billion					
Current taxes	38.4	37.9	41.7	41.4	43.2	44.7
Taxes on production and imports	33.6	33.1	35.1	36.2	36.8	37.3
Social security contributions	28.6	27.6	30.5	31.7	33.0	34.0
Taxes and contributions, total ²	101.3	99.4	108.2	110.2	113.9	116.9
Other revenue ³	25.0	23.9	24.7	26.1	27.6	28.2
of which interest receipts	1.6	1.3	1.3	1.4	1.5	1.6
Total revenue	125.6	122.5	132.1	135.4	140.6	144.2
Consumption expenditure	55.6	57.7	60.7	62.8	63.5	65.3
Subsidies	2.6	4.2	4.3	2.8	2.9	2.9
Social security benefits and allowances	43.8	46.4	46.8	47.5	49.0	50.4
Other current transfers	5.8	6.7	6.6	6.7	6.6	6.5
Subsidies and current transfers, total	52.1	57.3	57.7	57.0	58.6	59.9
Capital expenditure ⁴	10.9	11.8	12.0	12.6	12.6	12.8
Other expenditure	9.1	8.6	8.5	8.6	9.4	9.3
of which interest expenses	2.0	1.6	1.3	1.2	1.0	0.9
Total expenditure	127.8	135.4	139.0	141.0	144.1	147.2
Net lending (+) / net borrowing (-)	-2.3	-12.9	-6.9	-5.6	-3.5	-3.1
Central government	-2.6	-13.1	-8.3	-6.5	-3.9	-4.0
Local government	-3.0	0.0	-0.5	-1.9	-1.7	-1.5
Wellbeing services counties						-0.6
Employment pension schemes	2.7	0.3	2.0	2.5	2.4	2.5
Other social security funds	0.6	-0.2	-0.0	0.2	0.5	0.5
Primary balance ⁵	-0.3	-11.3	-5.6	-4.4	-2.5	-2.2

¹ As calculated in the National Accounts² Incl. capital taxes³ Incl. capital transfers and consumption of fixed capital⁴ Gross fixed capital formation and capital transfers⁵ Net lending excluding gross interest expenses

**Table 15.** Main economic indicators in general government

	2019	2020	2021	2022**	2023**	2024**
	relative to GDP, %					
Taxes and social security contributions	42.2	42.1	43.5	42.0	41.9	41.7
General government expenditure ¹	53.2	57.3	55.9	53.7	53.1	52.5
Net lending	-0.9	-5.5	-2.8	-2.1	-1.3	-1.1
Central government	-1.1	-5.5	-3.3	-2.5	-1.4	-1.4
Local government	-1.2	0.0	-0.2	-0.7	-0.6	-0.5
Wellbeing services counties						-0.2
Employment pension institutions	1.1	0.1	0.8	1.0	0.9	0.9
Other social security funds	0.3	-0.1	-0.0	0.1	0.2	0.2
Primary balance ²	-0.1	-4.8	-2.2	-1.7	-0.9	-0.8
General government debt	59.5	69.5	67.7	67.1	67.5	67.9
Central government debt	44.3	52.9	51.8	51.3	51.6	51.7
General government employment, 1,000 persons	653	658	675	681	673	674
Central government	138	143	146	146	146	146
Local government	502	502	516	522	266	266
Wellbeing services counties						248
Social security funds	13	13	13	13	13	13

¹ EU-harmonized definition² Net lending excluding gross interest expenses

2.2 Central government

There was a sharp deterioration in central government budgetary position in 2020 as a result of the COVID-19 pandemic. According to the national accounts, the budgetary position in 2020 was as much as EUR 13.1 billion in deficit (5.5% of GDP). The sharp contraction of the Finnish economy weakened central government finances as the automatic stabilisers led to higher expenditure and lower revenue. Discretionary spending increases have also substantially weakened the central government budgetary position.

Central government expenditures in 2021 are estimated to be at the previous year's level, but the budgetary position will improve year-on-year due to rapid growth in revenues. The central government budgetary position is estimated to be over EUR 8.3 billion in deficit in 2021, which represents 3.3% of GDP. As the economy recovers and employment increases, the direct central government tax revenue will increase year-on-year to an exceptional degree. The growth in household purchasing power is also reflected in the rapid growth of indirect tax revenue.

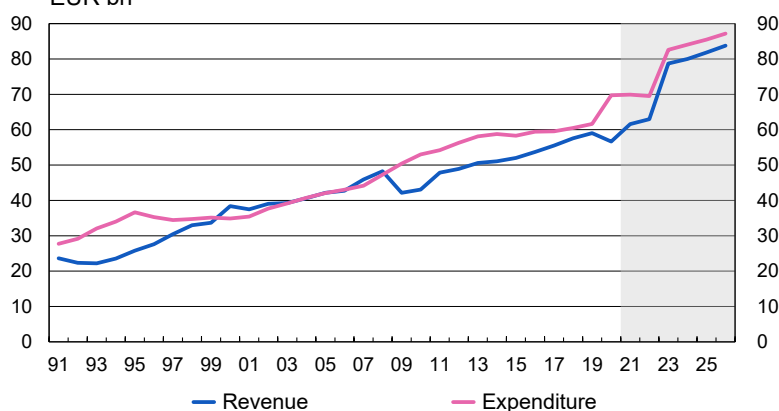
Active financial policy will keep discretionary expenditures at a high level. Prime Minister Marin's Government has issued four supplementary budgets in 2021. New discretionary measures introduced in 2021 include additional purchases of COVID-19 vaccines as well as subsidies for cargo and passenger shipping companies. The Recovery and Resilience Facility of the EU (RRF) will also increase expenditure, especially in 2022 and 2023. RRF spending will be channelled to investment grants, subsidies, public consumption and public investments. In the first stage, RRF spending increases will be covered from the current transfers granted by the EU, which means that they will not have an effect on the central government's budgetary position. Finland will have to pay its RRF funding contribution between 2028 and 2058.

The central government deficit is expected to decrease in 2022 as moderate growth in revenues continues. Expenditures will remain high. The additional expenditures caused by the COVID-19 pandemic will decrease but, at the same time, expenditures will be increased by a focus on investments. It is estimated that budgetary position will show a deficit of approximately EUR 6.5 billion.

The deficit is expected to decrease further to EUR 3.9 billion in 2023. The deficit is not expected to change significantly in the final years of the forecast period. In 2023–2026, the deficit-to-GDP ratio is expected to be between 1.1% and 1.4%. The brisk growth in revenues is expected to slow down after 2023. Starting from 2023, central government expenditures will be increased by defence materiel purchases that will create a substantial increase in investments.

Central government revenue and expenditure

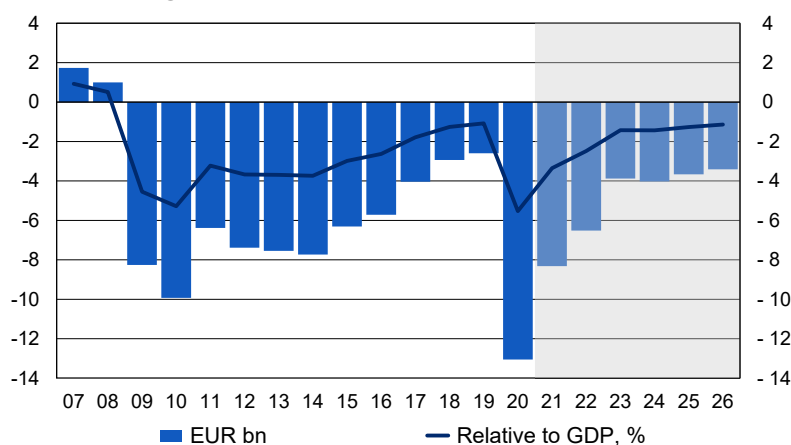
EUR bn



Sources: Statistics Finland, MoF

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Central government financial balance



Sources: Statistics Finland, MoF

VM34098

Table 16. Central government¹

	2019	2020	2021	2022**	2023**	2024**
	EUR billion					
Current taxes	15.2	13.3	16.1	15.9	30.8	31.6
Taxes on production and imports	33.6	33.1	35.1	36.2	36.8	37.3
Social security contributions	0.0	0.0	0.0	0.0	0.0	0.0
Taxes and social security contributions, total ²	49.6	47.2	52.1	53.0	68.4	69.8
Other revenue ³	9.5	9.4	9.4	9.8	9.8	9.7
of which interest receipts	0.2	0.1	0.1	0.1	0.1	0.1
Total revenue	59.1	56.7	61.4	62.8	78.2	79.5
Consumption expenditure	14.4	15.1	16.0	16.6	16.6	17.0
Subsidies and current transfers, total	40.6	47.7	47.2	45.7	58.9	60.0
to general government	28.7	33.2	32.7	32.7	45.8	46.9
Interest expenses	1.8	1.5	1.2	1.1	0.9	0.7
Capital expenditure ⁴	4.9	5.4	5.3	5.9	5.7	5.8
Total expenditure	61.7	69.7	69.8	69.3	82.1	83.5
Net lending (+) / net borrowing (-)	-2.6	-13.1	-8.3	-6.5	-3.9	-4.0
Primary balance ⁵	-0.8	-11.5	-7.1	-5.4	-3.0	-3.3

¹ As calculated in the National Accounts² Incl. capital taxes³ Incl. capital transfers (excl. capital taxes) and consumption of fixed capital⁴ Gross fixed capital formation and capital transfers⁵ Net lending excluding gross interest expenses

2.3 Local government

According to national accounts, the local government budgetary position was slightly in surplus in 2020. The local government budgetary position improving by over EUR 3 billion from the previous year is attributable to the significant support measures allocated to the local government sector due to the COVID-19 pandemic, which exceeded the costs created for the local government sector by COVID-19 in 2020.

In 2021, the local government budgetary position is expected to decline to a deficit of approximately EUR 550 million. The central government's COVID-19 support measures allocated to the local government sector will remain substantial while being smaller than in 2020. However, the growth of consumption expenditure has increased in 2021, resulting from the increase in expenditure on protective equipment and COVID-19 testing, changes in the tasks envisaged in the Government Programme and local government pay rises. A service and care backlog has also accumulated during the pandemic, and reducing the backlog has caused additional expenditure pressures. The Government has pledged to finance all new and expanding local government tasks and compensate the municipalities for costs directly linked to COVID-19.

The economic projection of local government finances for 2023–2026 is a pressure calculation that, in addition to general economic and population trends, only takes into account the measures impacting local government finances that are already included in the Budget proposals and the General Government Fiscal Plan. The projection does not include municipalities' and joint municipal authorities' own measures for the period 2023–2026. They will only be included in the projection after the budgets have been finalised. Municipal tax rates have been kept at 2022 levels. The pressure calculation takes into account the Government proposal to reform health and social services and rescue services approved by Parliament, which will transfer the responsibility for these tasks from municipalities to wellbeing services counties in 2023. The temporary administration of the counties is included in the local government forecast until the end of 2022. The transfer of employment and economic development services to municipalities in 2024, which is planned by the Government, has not yet been taken into account in the estimate.

Even though the increase in local government expenditure will slow down in 2022 as the COVID-19 crisis eases, local government budgetary position will deteriorate sharply as the temporary support measures end or their impact is reduced. In addition, more people will see their municipal taxes reduced than increased, but the average municipal tax rate weighted by taxable income will be close to the previous year's level at 20.01%. One-off subsidies prompted by the COVID-19 crisis have relieved the financial situation in local government and alleviated the worst of the adjustment pressures, but they have not solved the structural imbalance between revenue and expenditure in local government finances, a result of health and social services expenditure pressures arising from an ageing population and a decline in the working-age population. Growth in consumption expenditure is also sustained by the new tasks introduced by the Government, the reduction of the care and service backlog and price increases. At the same time, however, the health and social services reform may encourage municipalities to curb the rise in health and social services spending. Permanent adjustment measures by municipalities and joint municipal authorities have been included in the forecast on a technical basis at a level of EUR 100 million in 2022.

Local government collective agreements will expire at the end of February 2022. Personnel expenses are the largest cost item in local government and for this reason, pay agreements in the municipal sector have a significant impact on cost trends in the sector. In the pressure calculation, trends in local government earnings are expected to reflect the projected earnings trends at national level between 2022 and 2026. The tightness of the labour market is particularly visible in the municipal sector, as according to the employment outlook by occupation of the Ministry of Economic Affairs and Employment, there is a particularly severe shortage of health and social services professionals. There have also been difficulties in recruiting teachers in early childhood education and care and special needs teachers.

In 2023, the responsibility for health and social services and rescue services will be transferred to wellbeing services counties and the funding for them will become a central government responsibility. Local government revenue and expenditure will

be almost halved as a result of the reform.¹³ The health and social services reform will ease the cost pressures in local government arising from the growing need for care services for the ageing population. After the reform, local government will increasingly focus on services for young age groups, such as early childhood education and care, other education and training, which will lead to a decrease in the overall need for services. The impact of the decrease in the need for services has been slightly softened in the projection, as the capacity to adapt service production rapidly varies in different municipalities.

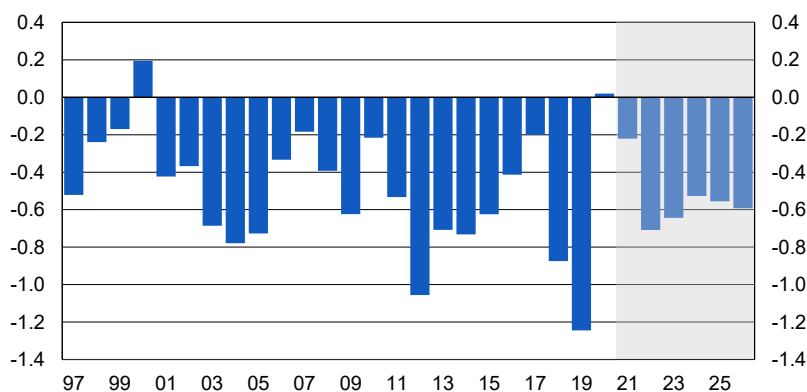
Local government investments have grown for the past 15 years, and the growth has been particularly rapid in recent years. The network of central hospitals in Finland, for example, has been updated at a brisk rate, and the peak of these investments is now beginning to have passed. A total of EUR 1.2 billion in investments will be transferred from local government to the wellbeing services counties. Although the fastest growth phase of investments is estimated to be behind us, it is assumed that investments will remain at a high level throughout the outlook period. The investment pressures will remain substantial because of the age of the building stock and migration.

The structural imbalance of local government revenue and expenditure means that local government will accumulate additional debts until 2023. With the health and social services reform, about EUR 4.6 billion in debts will be transferred from local government to wellbeing services counties in 2023. According to pressure projections, local government deficits will persist after the introduction of the health and social services reform but the growth of the deficit will become more moderate, which will also be reflected in slower growth of the local government debt ratio.

1 The calculations related to the health and social services reform are still preliminary by nature and they will become more specific when the general government fiscal plan for 2023–2026 is drafted. The Ministry of Finance has noticed an error in the calculations of central government transfers to local government for basic public services. Correcting this error would lead to the central government transfers to local government being approximately EUR 340 million higher than shown in the forecast starting from 2023. The error does not have any impact on the health and social services transfer calculation between municipalities and wellbeing services counties.

Local government financial balance

relative to GDP, %

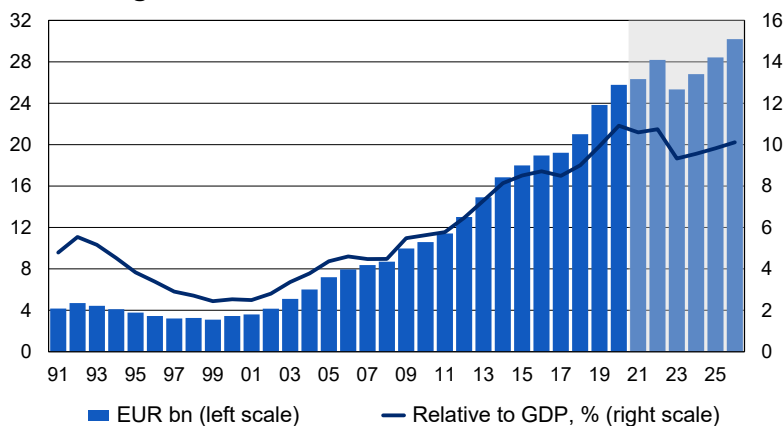


Incl. health and social services reform as of 2023

Sources: Statistics Finland, MoF

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Local government debt



Incl. health and social services reform as of 2023

Sources: Statistics Finland, MoF

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Table 17. Local government¹

	2019	2020	2021	2022**	2023**	2024**
	EUR billion					
Taxes and social security contributions	23.2	24.5	25.6	25.5	12.5	13.1
of which municipal tax	19.4	20.5	20.8	21.6	9.0	9.6
corporate tax	1.9	2.1	2.9	1.8	1.4	1.5
real estate tax	1.9	2.0	2.0	2.0	2.0	2.1
Other revenue ²	20.0	23.5	24.0	24.2	13.3	13.6
of which interest receipts	0.3	0.2	0.2	0.2	0.2	0.2
transfers from central government	14.4	17.7	17.9	17.9	7.2	7.4
Total revenue	43.2	48.0	49.6	49.7	25.8	26.7
Consumption expenditure	37.5	38.8	40.6	42.0	19.7	20.3
of which compensation of employees	22.1	22.4	23.4	24.2	12.5	12.8
Income transfers	2.5	2.6	2.7	2.7	2.0	2.0
of which social security benefits and allowances	0.8	0.8	0.8	0.8	0.2	0.2
subsidies and other transfers	1.6	1.8	1.8	1.8	1.7	1.7
interest expenses	0.1	0.1	0.1	0.1	0.1	0.1
Capital expenditure ³	6.2	6.6	6.8	6.9	5.8	5.9
Total expenditure	46.2	48.0	50.2	51.6	27.5	28.2
Net lending (+) / net borrowing (-)	-3.0	0.0	-0.5	-1.9	-1.7	-1.5
Primary balance ⁴	-2.9	0.1	-0.5	-1.8	-1.6	-1.4

¹ As calculated in the National Accounts² Incl. capital transfers and consumption of fixed capital³ Gross capital formation and capital transfers⁴ Net lending excluding gross interest expenses

2.4 Wellbeing services counties

In the projection for general government finances, counties will be treated as a separate local government sub-sector from 2023 onwards. In the projection, the counties comprise the activities of the counties (established as part of the health and social services reform), the HUS Group and the health and social services tasks of the City of Helsinki.

Initially, the counties will be slightly in deficit (about 0.2% of GDP). The deficit is due to the high level of health and social services investments.

Most of the funding for the counties will come from central government. In the two first years of operations, central government funding will be provided on the following basis: estimated increase in service needs plus 0.2 percentage points and in accordance with the county-specific price index and changes in tasks. The counties will also receive a small amount of payment income. In 2023, the sector will receive EUR 26.5 billion in revenue and 90% of this total will come from the central government.

Expenditure trends of the counties will be based on increases in service needs and anticipated price trends. Investment estimates are based on the financial plans of hospital districts. The cost of providing health and social services accounts for most of the expenditure of the counties. Personnel expenses or costs of purchasing goods and services will account for EUR 25.3 billion of the total in 2023.

Initially, the counties will also incur costs as they launch and organise their activities. It is assumed in the projection that the change costs arising from ICT changes, administrative expenses and the harmonisation of wages and salaries will be as estimated in the Government proposal for the health and social services reform. Scale of the change costs involves uncertainties.

Table 18. Welfare services counties

	2023**	2024**
	EUR billion	
Total revenue	26.5	27.4
Total expenditure	27.2	28.0
Net lending (+) / net borrowing (-)	-0.7	-0.6
Debt	5.3	5.9

2.5 Social security funds

In 2020, the surplus of employment pension institutions fell sharply to 0.1% of GDP. In 2021, the surplus will return to 0.9%. Employment pension contributions have been improved by the end of the temporary reduction in private sector employers' employment pension contributions and the higher total wage amount. Property income will also grow at a good rate. During the period 2022–2025, contributions will be increased by an increase in employment pension contributions to compensate for the reduction in contributions in 2020. The employment pension sector's surplus will remain at just under one per cent of GDP.

The other social security funds had a deficit of 0.1% relative to GDP in 2020. The sector will return close to balance in 2021. Unemployment costs are already decreasing to some degree and unemployment insurance contributions were increased at the beginning of 2021. The contributions will be increased further in 2022 and unemployment costs are expected to decline substantially when the improved employment situation is in effect for the full year. The sector will have a surplus of approximately 0.2% of GDP starting from 2022. The Employment Fund's cyclical buffer will start to grow and, towards the end of the forecast period, there will be pressure to reduce contributions due to the upper boundary of the cyclical buffer being approached.

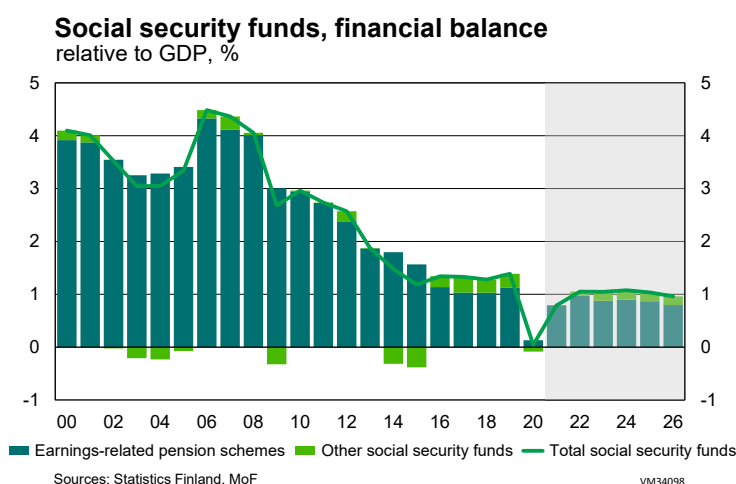


Table 19. Finances of social security funds¹

	2019	2020	2021	2022**	2023**	2024**
	EUR billion					
Investment income	4.3	3.5	3.9	4.4	4.7	5.2
Social security contributions	28.5	27.6	30.5	31.7	32.9	33.9
of which contributions paid by employers	17.8	16.7	18.8	19.8	20.6	21.2
contributions paid by insured	10.8	10.8	11.7	11.9	12.4	12.8
Transfer from general government	15.7	17.2	16.4	16.2	16.2	16.4
Other revenue	0.4	0.4	0.3	0.3	0.3	0.3
Total revenue	48.9	48.7	51.2	52.6	54.2	55.9
Consumption expenditure	3.8	3.8	4.0	4.2	4.2	4.3
Social security benefits and allowances	38.5	41.2	41.5	42.1	43.6	44.8
Other outlays	3.2	3.6	3.7	3.5	3.6	3.7
Total expenditure	45.5	48.6	49.2	49.9	51.4	52.9
Net lending (+) / net borrowing (-)	3.3	0.1	2.0	2.8	2.8	3.0
Earnings-related pension schemes	2.7	0.3	2.0	2.5	2.4	2.5
Other social security funds	0.6	-0.2	-0.0	0.2	0.5	0.5
Primary balance ²	3.4	0.1	2.0	2.8	2.9	3.0

¹ As calculated in the National Accounts² Net lending excluding gross interest expenses



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