



MINISTRY
OF FINANCE

Economic Survey

Autumn 2022

Economic Prospects

Publications of the Ministry of Finance – 2022:60

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Economic Survey

Autumn 2022

Economics Department

Ministry of Finance, Helsinki 2022

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Abstract

Gross domestic product (GDP) in Finland is projected to grow by 1.7% in 2022. Economic output developed favourably in the first half of the year, and employment has continued to grow rapidly. Economic growth is projected to slow more during the second half of the year than previously forecast in the summer. GDP growth will slow to 0.5% in 2023. The prices of goods and services, as well as energy, have also continued to rise faster than previously projected in the summer. GDP growth in 2024–2026 is projected to be faster than the potential economic growth rate at approximately 1.4% per year.

The general government deficit will contract in 2022 due to brisk economic growth and employment growth as well as the end of COVID-19 measures. The deficit will begin to increase again in 2023, and public finances will remain in a deep deficit in the coming years. The ratio of general government debt to GDP will decrease this year but turn to growth next year.

Debt servicing costs are projected to grow during the outlook period. Continuously rising debt servicing costs come out of the rest of public spending and reduce the already tight buffers of general government finances.

Keywords economic prospects, public finance, economic development, draft budget

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Taloudellinen katsaus, syksy 2022

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Yhteisötekijä	Kansantalousosasto		
Kieli	Englanti	Sivumäärä	112

Tiivistelmä

BKT:n arvioidaan kasvavan Suomessa 1,7 % v. 2022. Alkuvuonna talouden tuotanto on kehittynyt suotuisasti ja työllisyys on jatkanut nopeaa kasvua. Talouskasvun ennustetaan hidastuvan loppuvuonna enemmän kuin vielä kesällä ennakoitiin. BKT:n kasvu hidastuu 0,5 prosenttiin v. 2023. Myös hyödykkeiden ja energian hintojen nousu on jatkunut kesällä arvioitua nopeampana. Vuosina 2024–2026 BKT:n kasvun arvioidaan olevan talouden potentiaalista kasvua nopeampaa, noin 1,4 % vuosittain.

Julkisyhteisöjen alijäämä supistuu v. 2022 ripeän talous- ja työllisyyskasvun sekä koronatoimien päättymisen johdosta. Vuonna 2023 alijäämä kääntyy uudelleen kasvuun ja julkinen talous pysyy syvästi alijäämäisenä tulevina vuosina. Julkisen velan suhde BKT:hen alenee tänä vuonna, mutta kääntyy nousevalle uralle ensi vuonna.

Velanhoidokustannusten arvioidaan kasvavan ennustejaksolla. Alati kasvavat velanhoidokulut ovat pois muusta julkisesta rahankäytöstä ja kaventavat julkisen talouden ennestäänkin niukkoja puskureita.

Asiasanat talousnäymät, julkinen talous, taloudellinen kehitys, budjettiesitys

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Referat

Bruttonationalprodukten (BNP) beräknas öka med 1,7 procent 2022 i Finland. Under början av året utvecklades produktionen gynnsamt, och sysselsättningen fortsatte att öka snabbt. Den ekonomiska tillväxten väntas avta mer i slutet av året än vad som förutsågs under sommaren. BNP-tillväxten avtar till 0,5 procent 2023. Ökningen av priset på nyttigheter och energi fortsatte också snabbare än vad som förutsågs under sommaren. BNP-tillväxten 2024–2026 förutses vara snabbare än den potentiella ekonomiska tillväxten, cirka 1,4 procent per år.

Den offentliga sektorns underskott minskar 2022 tack vare snabb ekonomisk tillväxt, positiv sysselsättningsutveckling och avslutade coronaåtgärder. Underskottet börjar åter öka 2023, och de offentliga finanserna uppvisar ett fortsatt stort underskott de kommande åren. Den offentliga skulden i förhållande till BNP minskar i år, men vänder uppåt igen nästa år.

Skuldhanteringskostnaderna väntas öka under prognosperioden. De ökande skuldhanterings-kostnaderna påverkar den övriga offentliga penninganvändningen och minskar de redan från tidigare knappa buffertarna inom den offentliga ekonomin.

Nyckelord ekonomiska utsikter, offentlig ekonomi, ekonomisk utveckling, budgetförslag

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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
HWI	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 AUTUMN 2022

This Economic Survey offers projections of economic developments in 2022–2024. 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 national accounts data for the year 2021 published by Statistics Finland in July 2022, on other public statistical sources available by 22 August 2022 and the decisions taken by the Government in its budget negotiations on 1 September 2022.

Helsinki September 2022

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Preface

Compared to the expectations outlined in public discussion, the Ministry of Finance's forecast paints a moderate picture of the direction of the economy over the next 6–18 months.

The first half of 2022 was substantially stronger than anticipated with regard to the economy, output and employment. Households have consumed. They have particularly used services that they were unable to use during the restrictions imposed in response to the COVID-19 pandemic.

According to the forecast, economic growth will slow significantly towards next year. A period of stagnant growth is ahead, and the economy drifting into recession is a scenario that cannot be excluded. Uncertainty, energy shortages, high inflation, eroding purchasing power and rising interest rates are curbing the growth of consumption and investment across the board.

Nevertheless, the situation is expected to improve in 2023.

The forecast does not anticipate an escalation of Russia's war of aggression. Nor does it anticipate a deterioration of the COVID-19 pandemic or restrictions that would have a substantial impact on output, demand or employment. Nor an out-of-control price-wage spiral. Nor a collapse of the electricity market or other energy markets. Nor a change in the ECB's mandate to ensure the stability of the financial markets and anchor inflation expectations in the medium term. Nor a change in the confidence that creditors have in the Finnish government's capacity to service its debt and other liabilities.

There are probably surprises on the horizon, either involving the events mentioned above or something else. Those surprises may come one at a time or in bunches. It is important to prepare for them.

Compared to the previous forecast published in June, the risks associated with the multiplier effects of inflation, the prolongation of the period of rapid inflation, the energy crisis and the complete and longer-term stagnation of economic growth

have increased. The autumn round of negotiations on pay is also a source of uncertainty.

Consumer prices are driven higher by the energy shortage. Furthermore, in an overstimulated market, even small changes in the supply or demand of energy are reflected in dramatic changes in the price of energy. Higher energy prices have already increased the price of food, for example.

Demand inflation is not yet a key driver of rapid inflation, and wage inflation has not started yet.

The uncertain and volatile situation is cause for concern for the monetary authority of the euro area. Monetary policy in the euro area may be a balancing act between the risk of broader inflation and the risk of a recession, but the era of near-zero interest rates is over in any case.

After the COVID-19 pandemic eased, confidence in the future quickly returned and households have been spending their accumulated savings on goods and services. Since then, households have suffered another big scare. War broke out in Europe. Interest rates on housing loans are rising. The prices of new electricity agreements are many times higher than those of expiring agreements. The framework of daily life, which was thought to be stable, is now changing rapidly.

Having suffered a new scare, households may start to save money for a rainy day – at least those households that have the capacity to do so and, at the latest, if a downturn in the labour market were to happen. An increase in saving would reduce consumption, total demand in the economy, and growth. Confidence in the future among businesses has shown more signs of hope for the time being, although there is considerable deviation in their views.

The rapid growth of employment and consumption has increased tax revenue and boosted general government finances in 2021–2022. When economic growth slows and debt servicing costs increase, the general government deficit and debt will start to grow again. Further factors that increase the deficit include the start-up costs of the wellbeing services counties, decisions to support security, the security of supply, research, product development and the green transition of the economy, measures to compensate households for the exorbitant increase in the price of electricity, and the continuously growing expenditure arising from the ageing of the population.

The Ministry of Finance estimates that the structural imbalance of revenue and expenditure in general government finances amounts to approximately EUR 9 billion. Public finances are not on a sustainable foundation in the long term.

The starting point for the management of public finances is to adjust revenue and expenditure to fit the framework established by economic performance. It is also necessary to maintain room to manoeuvre in public finances to prepare for more unfavourable scenarios. The framework of managing public finances is tight, with continuously growing debt and increases in other liabilities eating up the room to manoeuvre within the framework.

The root cause behind the sustainability problem in the management of public finances is that Finland's economic performance is not sufficient in relation to the needs of the public sector – both statutory needs and other needs. We want to provide public services and benefits at the same level as our Nordic peers despite our economic performance being weaker compared to our peers. This root cause is inescapable and it will not fix itself.

Inflation will not rectify the situation – on the contrary. Inflation prevents the economic resources from being efficiently allocated, and curbing inflation requires higher interest rates and weaker employment. Inflation undermines the conditions for growing the framework of managing public finances.

There are two sides to the reconciliation of public sector needs with economic performance.

By changing the rules that define the economic operating environment and ensuring that public funds are used smartly, it is possible to increase the efficiency of resource use in the economy, support growth and income formation, and create space in the framework in which the management of public finances needs to happen. In any scenario, climate change and the excessive consumption of natural capital force us to seek more efficient and sustainable solutions for production, consumption and the creation of economic growth.

At the same time, we must prepare to evaluate the needs of the public sector as a whole and with a critical perspective. A spending review, for example, would be an appropriate tool for such an evaluation, and the change in the government term would be an opportune time for it.

Summary

Economic outlook for the period 2022 – 2024

Gross domestic product (GDP) in Finland is projected to grow by 1.7% in 2022. Economic output developed favourably in the first half of the year, and employment has continued to grow rapidly. Economic growth is projected to slow more during the second half of the year than previously forecast in the summer. GDP growth will slow to 0.5% in 2023. The prices of goods and services, as well as energy, have also continued to rise faster than previously projected in the summer. Rising consumer prices will substantially erode household purchasing power, consumption and economic growth during the rest of the year and in early 2023. GDP growth in 2024–2026 is projected to be faster than the potential economic growth rate at approximately 1.4% per year.

The outlook of foreign trade is overshadowed particularly by the significant contraction of trade with Russia, although exports to Russia are still continuing to some extent. As the economic outlook for Europe has deteriorated since the summer, export growth in the coming years will be subdued.

The forecast assumes that the sanctions against Russia in force in early August 2022 will remain in place throughout the outlook period. However, the direct impacts of the restrictions are outweighed by the indirect impacts, such as the extensive disruption of the energy markets and rising prices.

The impacts of the COVID-19 pandemic and Russia's war of aggression on economic growth have weakened Finland's public finances. The general government deficit will contract this year due to brisk economic growth and employment growth as well as the end of COVID-19 measures. The deficit will begin to increase again next year, and public finances will remain in a deep deficit in the coming years. The ratio of general government debt to GDP will decrease this year but turn to growth next year. There is a considerable structural imbalance between general government expenditure and revenue, and the sustainability gap is now estimated to be 3.0% of GDP, or approximately EUR 9 billion at the level of 2026.

Debt servicing costs are projected to grow during the outlook period. Continuously rising debt servicing costs come out of the rest of public spending and reduce the already tight buffers of general government finances.

The threat of an energy crisis is slowing economic growth in Europe

The outlook of the global economy has been clouded by rapid inflation, the European energy crisis and Russia's continued war of aggression. Geopolitical tensions between the world's superpowers have increased, while emerging economies are still at risk of food shortages. After rapid growth last year, global economic growth will slow to 2.7% in 2022 and further to 2.5% in 2023.

The outlook for the euro area has been clouded by Russia's continued war of aggression and energy shortages. Inflation has accelerated further, and consumer confidence is low. The economic outlook of Germany is particularly weak. The US economy contracted in the first and second quarter of this year. Nevertheless, the US economy is not considered to be in a recession, as the growth of employment and wages is still very strong. Economic growth in China has slowed considerably this year, with ongoing COVID-19 shutdowns and problems in the real estate sector weakening the growth outlook.

Monetary policy has been tightened in the United States and the euro area, and interest rates have been rising. While there are already signs of inflation slowing in the United States, inflation has yet to slow permanently. The forecast assumes that long-term and short-term market interest rates will keep rising until the end of 2024.

The difficult situation in the European energy market is continuing, and it may be necessary to regulate energy consumption during the coming winter. The price of natural gas is very high in Europe. However, the price of crude oil, for example, has fallen from the highs seen in the late spring of 2022. The prices of industrial raw materials also declined sharply during the summer, which reflects the uncertain outlook in the industrial sector. Raw material prices are projected to decrease moderately during the outlook period.

World trade in goods has been characterised by a high level of activity since the late spring. Some signs have emerged to suggest that the component shortages that have disrupted world trade are starting to ease. World trade will grow by 4.2% in 2022 and subsequently slow to 4.0% in 2023, reflecting the situation in the global economy.

Rising prices put the brakes on economic growth

Finland's GDP will grow by 1.7% in 2022, although GDP growth will slow substantially towards the end of the year. Consumer price inflation has already accelerated to nearly 8%, and inflation will rise to an average of 6.5% this year, as measured in terms of national consumer prices. Although the rising consumer prices are still mainly a consequence of increasing energy prices, the number of rising prices in the consumer price index is 10 times higher than the number of falling prices. Consumer price inflation is very broad-based, with prices rising quickly in all consumption categories.

Private consumption – and trade in durables, in particular – saw weak development in the first quarter of the year. The uncertainty caused by Russia's war of aggression and the ensuing sanctions has also weakened consumer confidence substantially, which appears to be delaying consumption particularly with regard to durables. Rising prices will erode household purchasing power and keep consumption growth subdued during the rest of the year. The real incomes of households are contracting in spite of the growth of employment, and the household savings ratio will approach zero.

Due to the substantial contraction of Finnish exports to Russia, the growth of exports of goods and services will be considerably slower than the growth of the export markets this year. At the same time, the weakened economic outlook of the euro area and the United States has emerged as a factor that casts a shadow over foreign trade. The sharp increases in export and import prices will also curb the development of foreign trade.

The continued strong housing construction will support investment this year. Other private investment will contract as diminishing confidence leads to the postponement of investments.

Employment growth will slow after rapid growth seen in the first half of the year. Nevertheless, employment will grow by approximately 2% this year. Labour market mismatches appear to have increased further, and shortages of skilled labour are weakening the conditions for increasing output. Pay increases in the collective agreements concluded this year have most commonly been around 2%, which is slightly higher than last year. Wage drifts are projected to increase in 2022 due to the high demand for competent personnel.

GDP growth will slow to 0.5% in Finland in 2023. Growth will be stagnant in the early part of the year. However, domestic demand will begin to recover towards the end of the year due to the rise in prices slowing substantially and real wages turning to slight growth.

The high price level will continue to slow the growth of household purchasing power in 2023, which leads to a subdued growth outlook for private consumption. In 2023, private consumption growth will slow to 0.8% as employment growth comes to a halt and the real incomes of households grow only slightly.

Export growth in 2023 will approach the growth of the world market, although companies will not yet fully find other markets to replace exports to Russia. Weak growth in the euro area will restrict export growth in particular.

The impacts of the war are reflected in imports through sanctions, trade disruptions and reduced exports. However, import products can be substituted more quickly than new export markets can be found, in addition to which investment will support imports in the early part of the outlook period.

In 2023, the global economic outlook will be weaker than this year, which will curb domestic investment. The investment outlook for Finnish manufacturing industries was bright after the COVID-19 pandemic, but uncertainty may lead to the postponement or suspension of investment projects in the future. Financing from the EU's Recovery and Resilience Facility (RRF) will for its part boost private investment during the outlook period. Over the entire outlook period, private investment will grow at an average rate of 1.9% and the ratio of private investment to GDP will remain at around 19%.

The volume of public consumption will contract in 2023 as the parliamentary term ends and the once-off additional expenditure comes to an end. The growth in consumption expenditure will be fairly moderate in 2024 when the transition costs arising from the start-up and organisation of the wellbeing services counties decrease. The value of public consumption will, however, rise faster than in recent years as prices increase rapidly.

The most typical duration of collective agreements has been two years, but agreements on next year's increases are due to be made during this autumn or early 2023. In addition, the agreement in the municipal sector guarantees an increase of at least 1.9% on top of the pay programme. This forecast assumes that the pay increases specified in the 2023 agreements will be higher than in 2022. The assumption is based on strong demand for labour and a significantly accelerated rise in consumer prices. Furthermore, wage drifts are projected to be higher than average next year due to the high demand for competent personnel. This would increase nominal earnings by 3.5% next year.

Economic growth is expected to be minimal and labour demand is projected to decline, leading to a slight contraction in the number of employed people in 2023. Employment turning to a decline will increase unemployment, particularly in secondary production, and the unemployment rate is projected to increase slightly compared to this year.

The recovery of economic growth will increase the number of employed persons in 2024, particularly in the service sectors. The employment rate will rise to 74.1% in 2024, partly due to the contraction of the size of the working-age population. If, as assumed by the forecast, labour market mismatches and region-specific and occupation-specific availability of labour do not become an obstacle to the functioning of the labour market, the unemployment rate will fall to around 6.5% in 2024.

Inflation will peak in the latter part of 2022 and remain high in the early part of 2023. Inflation will slow to an average of 3.2% in 2023. In particular, based on the development of market prices, electricity prices are projected to continue to increase and to remain high until the early part of 2023. Energy prices are even expected to decline moderately starting from the second half of 2023.

The increase in the prices of food, especially fresh food, will accelerate towards the end of this year. Increased costs are pushing producer prices higher, which is ultimately reflected in consumer prices. High prices and rising interest rates will gradually reduce total demand, and price pressures will ease. Inflation will fall to 1.8% in 2024.

Economic growth is projected to be 1.4% in 2024. The recovery of export volume will be the strongest in 2024. As the rise in prices slows, household purchasing power will increase and private consumption growth will accelerate.

The rise in earnings growth in 2024 is linked to projected, subdued productivity growth. On the other hand, economic growth and the resulting rise in employment as well as labour shortages in some sectors are expected to keep wage drifts high. Nominal earnings are projected to increase by approximately 3% in 2024.

General government finances are not on a sustainable foundation

General government finances will continue to strengthen this year, boosted by the rapid growth of tax revenue and the reduction in support measures related to the COVID-19 pandemic. The deficit will start to increase again next year as economic growth slows and employment weakens. General government finances will remain in a structural deficit for the years to come, and there is a longer-term sustainability gap in general government finances. The sustainability gap is estimated to be approximately 3.0% of GDP, or roughly EUR 9 billion at the level of 2026.

Among the subsectors of general government finances, the central government's deficit will improve slightly this year, only to subsequently weaken as economic growth slows. The structure of local government will change next year when the wellbeing services counties become operational. Local government will remain in deficit even after the reforms as expenditures grow slightly faster than revenues due to factors including personnel costs and investment pressures. Initially, the wellbeing services counties will be in deficit due to extensive investments. The rapid increase in personnel costs will exacerbate the wellbeing services counties' deficit in the subsequent years. Social security funds will remain in surplus due to increasing property income despite the projected rapid growth of benefits next year due to substantial cost-of-living index adjustments.

General government debt in ratio to GDP will contract temporarily this year. Decreasing deficits and the particularly favourable growth of nominal GDP are factors that contribute to the contraction of the debt ratio. Starting from next year, nominal GDP growth will slow and the combined deficit of central government, local government and wellbeing services counties will remain substantial, which will make the debt ratio start to increase again.

Debt servicing costs are projected to grow during the outlook period due to the rising yields on the government's benchmark bonds. Continuously rising debt servicing costs come out of the rest of public spending and reduce the already tight buffers of general government finances.

Energy shortage in Europe and cost-wage spiral are risks to the outlook

The measures taken to slow down inflation may further weaken economic growth in Europe and elsewhere in the international economy. In the forecast, the levelling off of domestic consumption growth will also slow down inflation towards the end of next year. Should inflation be faster than projected or longer in duration, interest rates will be higher than assumed in this forecast. Increases in interest rates are not dependent on the realisation of domestic risks, as monetary policy in the euro area responds to inflation in the euro area.

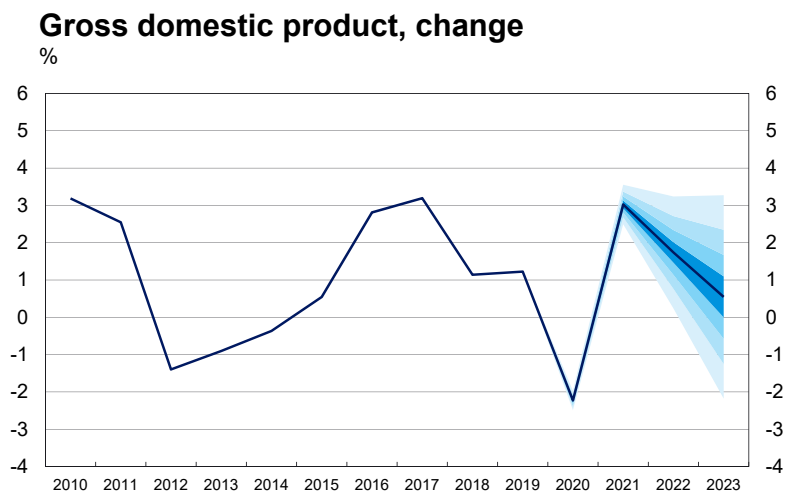
A wage-price spiral in the euro area would lead to tightening monetary policy and higher interest rates, which would weaken economic growth in export markets as well as Finland. A domestic wage-price spiral that is more intense than in the competing countries would weaken cost competitiveness and slow the recovery of economic growth in Finland.

The uncertain outlook of the investment environment may push back investments even further or prevent their implementation. An above-forecast level of private investments potentially catalysed by the Recovery and Resilience Facility (RRF) are a positive risk for private investments. There is a positive risk involved in the energy sector's green investment projects when the goal is to fast-track independence of Russian fossil fuels.

The most significant risks to general government finances are related to general economic development. Russia's invasion of Ukraine and the impacts of the resulting market disruptions may be reflected in general government finances more heavily than projected through general economic development, the preparations required by the changed situation and compensation paid out to citizens. Potential new waves of the COVID-19 pandemic and the ensuing care backlog may increase general government spending.

A faster-than-assumed increase in the interest rate level would increase the risk of general government indebtedness. A higher level of debt means a greater negative impact of rising interest rates on general government finances over the longer term. In addition, general government contingent liabilities and especially the rapid rise in guarantees will pose a risk for general government finances. The current parliamentary term will end next year, and the forecast for general government finances beyond the current parliamentary term is based on the assumption of unchanged policy. Decisions made by the next government may move general government finances in either direction.

The uncertainty of the economic forecast can be illustrated with 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 0.2% and 3.2% in 2022. Correspondingly, there is an 80% probability that GDP growth will be between -2.2% and 3.3% in 2023. The economic growth rate may of course also fall outside the confidence interval, especially when the growth estimates involve an exceptionally high degree of uncertainty.



Source: Statistics Finland, MoF

Table 1. Key forecast figures

	2021	2019	2020	2021	2022**	2023**	2024**
	EUR bn	change in volume, %					
GDP at market prices	251	1.2	-2.2	3.0	1.7	0.5	1.4
Imports	98	2.4	-5.8	5.6	1.8	2.6	3.2
Total supply	350	1.5	-3.3	3.7	1.8	1.2	2.0
Exports	99	6.7	-6.8	5.6	1.1	2.7	4.0
Consumption	189	1.1	-2.6	3.3	1.4	0.5	1.0
private	128	0.7	-4.1	3.6	1.1	0.8	1.4
public	61	2.0	0.5	2.7	1.8	-0.2	0.1
Investment	59	-1.5	-0.5	1.1	3.6	1.2	1.7
private	49	-2.3	-3.1	4.6	2.8	0.1	2.9
public	11	2.4	11.1	-12.8	7.3	5.9	-3.3
Total demand	349	1.5	-3.4	3.5	1.8	1.2	2.0
domestic demand	250	-0.4	-2.1	2.8	2.0	0.6	1.1

Table 2. Other key forecast figures

	2019	2020	2021	2022**	2023**	2024**
GDP, EUR bn	240	238	251	269	279	289
Services, change in volume, %	1.7	-3.1	3.6	1.5	0.8	1.5
Industry, change in volume, %	2.6	-1.3	0.7	2.7	1.3	1.7
Labour productivity, change, %	0.2	0.2	0.1	0.3	0.7	1.3
Employed labour force, change, %	1.0	-1.5	2.4	2.3	-0.2	0.3
Employment rate, %	71.6	70.7	72.3	73.9	73.8	74.1
Unemployment rate, %	6.7	7.7	7.7	6.6	6.7	6.5
Consumer price index, change, %	1.0	0.3	2.2	6.5	3.2	1.8
Index of wage and salary earnings, change, %	2.1	1.9	2.4	2.6	3.5	3.0
Current account, EUR bn	-0.7	1.5	2.3	-1.3	-1.8	-1.1
Current account, relative to GDP, %	-0.3	0.6	0.9	-0.5	-0.7	-0.4
Short-term interest rates (3-month Euribor), %	-0.4	-0.4	-0.5	-0.1	1.3	1.5
Long-term interest rates (10-year govt. bonds), %	0.1	-0.2	-0.1	1.4	1.8	2.0
General government expenditure, relative to GDP, %	53.3	57.2	55.5	53.9	54.7	54.1
Tax ratio, relative to GDP, %	42.3	41.9	43.0	42.5	42.0	41.5
General government net lending, relative to GDP, %	-0.9	-5.5	-2.7	-1.4	-2.2	-2.2
Central government net lending, relative to GDP, %	-1.1	-5.5	-3.3	-2.3	-3.0	-2.9
General government gross debt, relative to GDP, %	64.9	74.8	72.3	71.2	72.7	74.1
Central government debt, relative to GDP, %	44.3	52.5	51.2	50.8	52.0	53.1

Medium-term outlook for the period 2025-2026

Subdued growth is in sight in the medium term, with economic growth of approximately 1.5% projected for 2025–2026. The Finnish economy is projected to still remain below its normal capacity in 2024. Economic output will approach the estimated potential output level ¹ and the output gap will be closed in 2026².

The change in labour input will increase potential output until 2023, after which labour input will stop growing and it will begin to reduce potential output, as the working-age population continues to shrink and there is no longer any growth in the participation rate. The unemployment rate approaching the structural level will also begin to limit the growth of labour input.

In addition to labour input, the production conditions of the economy are influenced by capital stock. Growth in capital stock will boost potential output growth by just over 0.5% each year between 2021 and 2026.

Total factor productivity is the third source of potential output growth and has shown more rapid growth in recent years than in the early 2010s. However, productivity growth remains weak compared to the early 2000s. Structural changes in the Finnish economy are one factor explaining the weaker growth. The output of high-productivity sectors has declined and services have become more predominant in the overall structure of the economy. Slow productivity growth has also been common in other developed economies. Annual total factor productivity is expected to grow by around 0.5% in 2021–2026, down from an annual average of more than 2% in the early 2000s.

1 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, particularly during a strong economic cycle and under conditions of rapid changes in the production structure.

2 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 years $t+3$ and $t+4$ is estimated so that the output gap will close by 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 year $t+4$.

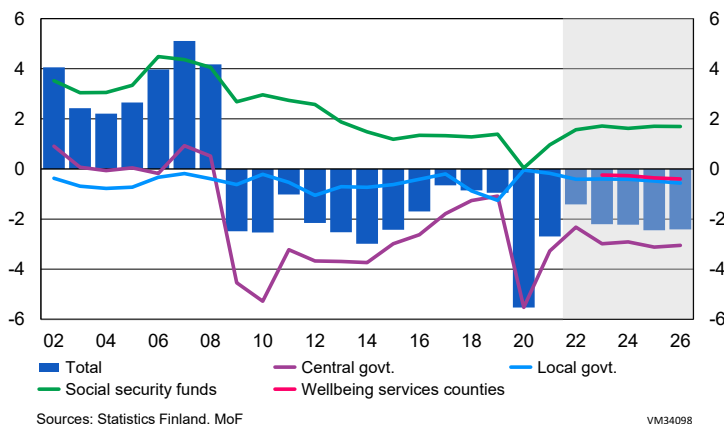
Table 3. Key forecast figures for the medium term

	2020	2021	2022**	2023**	2024**	2025**	2026**
GDP at market prices, change in volume, %	-2.2	3.0	1.7	0.5	1.4	1.5	1.4
GDP, EUR bn	238	251	269	279	289	299	310
Consumer price index, change, %	0.3	2.2	6.5	3.2	1.8	1.9	2.0
Unemployment rate, %	7.7	7.7	6.6	6.7	6.5	6.4	6.3
Employment rate, %	70.7	72.3	73.9	73.8	74.1	74.4	74.7
General government net lending, relative to GDP, %	-5.5	-2.7	-1.4	-2.2	-2.2	-2.4	-2.4
Central government	-5.5	-3.3	-2.3	-3.0	-2.9	-3.1	-3.1
Local government ¹	-0.0	-0.2	-0.4	-0.4	-0.4	-0.5	-0.6
Wellbeing services counties				-0.2	-0.3	-0.4	-0.4
Social security funds	0.0	0.8	1.3	1.4	1.4	1.5	1.6
Structural balance, relative to GDP, %	-3.8	-2.0	-1.0	-1.5	-1.7	-2.2	-2.4
General government gross debt, relative to GDP, %	74.8	72.3	71.2	72.7	74.1	75.2	76.0
Central government debt, relative to GDP, %	52.5	51.2	50.8	52.0	53.1	53.7	54.1
Output gap, % of potential output ²	-3.0	-1.2	-0.7	-1.2	-0.9	-0.4	0.0

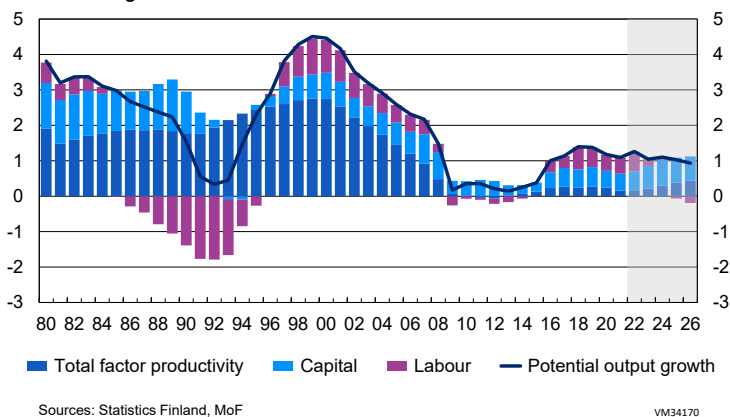
¹ Excl. wellbeing services county administration as of 2023

² 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 International economy

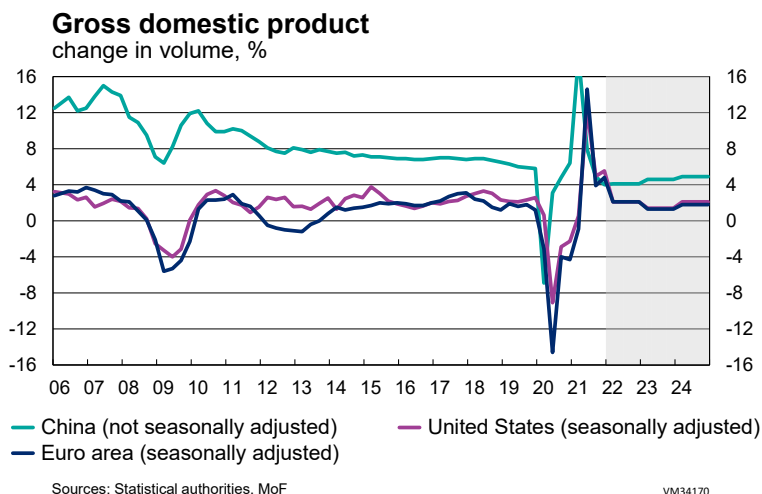
1.1.1 Global economy

The outlook of the global economy has been clouded by rapid inflation, the energy crisis in Europe and Russia's continued war of aggression. Geopolitical tensions between the world's superpowers have increased. Emerging economies are still at risk of food shortages. After rapid growth last year, global economic growth will slow to 2.7% in 2022 and further to 2.5% in 2023.

The US economy contracted in the first and second quarter of this year, but the employment rate remains very high. The prevailing view is that the economy is not in a recession. Monetary policy has been tightened very rapidly and inflation is starting to show signs of slowing. Total output will grow by 2.1% this year and by 1.4% in 2023.

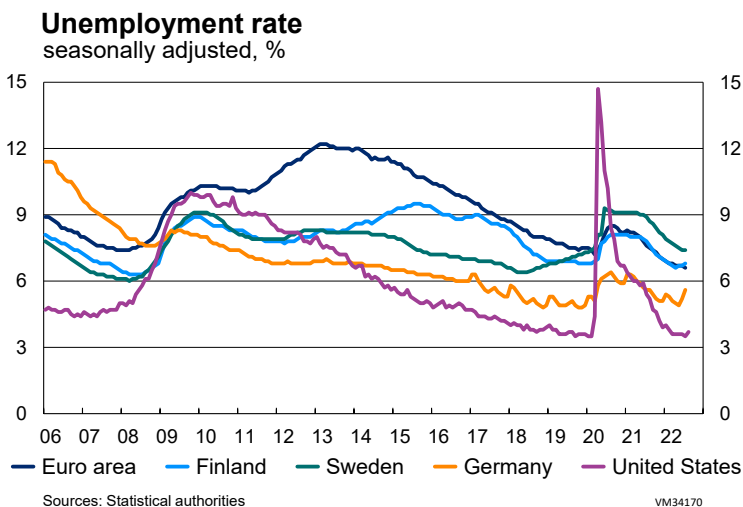
Economic growth in China has slowed considerably this year. China's GDP contracted significantly in the second quarter compared to the preceding quarter. The outlook is weakened by the ongoing COVID-19 shutdowns and problems in the real estate sector. The growth of retail sales and industrial production fell short of expectations in July. In August, the central bank unexpectedly lowered a key interest rate. Economic growth will slow to 4.1% this year. Next year, the economy will recover with projected growth of 4.6%.

The outlook for the euro area has been clouded by Russia's continued war of aggression and the energy crisis. Inflation has continued to accelerate, and consumer confidence is low. The outlook is particularly challenging in Germany. Southern Europe, on the other hand, has benefited from the lifting of COVID-19 restrictions. The coming winter is expected to be very difficult with regard to the availability of energy. Total output growth will slow to 2.1% in 2022 and further to 1.3% in 2023.



The UK economy contracted slightly in the second quarter of 2022 compared to the preceding quarter. Very rapid inflation is limiting consumers' real incomes and private consumption. Brexit-related problems are having an adverse impact on export companies in particular, and the foreign trade deficit has reached an unprecedented level. Total output will grow by 2.7% in 2022 and by 1.8% in 2023.

In Sweden, total output recovered in the second quarter after a weak first quarter, but the outlook remains challenging. Consumer confidence in economic development is at its lowest point since the turn of the century. Inflation has been further accelerated by the Swedish krona depreciating against the euro and the US dollar. Total output will grow by 1.8% in 2022 and by 1.6% in 2023.



The Russian economy will contract in 2022 due to the invasion of Ukraine, but less sharply than previously projected. Production in the mining industry increased in June due to the recovery of oil production. Secondary production continued to contract at the same time, however. Households have responded to the economic conditions by increasing their savings. Total output will contract by 7% in 2022 and by 2% in 2023 due to the continued uncertainty.

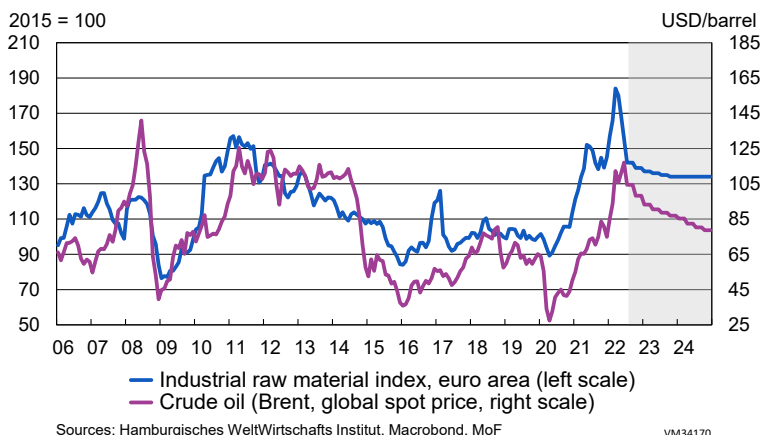
The Japanese economy is gradually recovering after the lifting of long-standing COVID-19 restrictions. The increase in inflation has been fairly moderate compared to other developed economies. The central bank has not tightened its monetary policy, choosing instead to pursue a yield curve control policy. Total output will grow by 0.7% in 2022, with growth slowing to 0.3% in 2023.

Uncertainty is continuing in the international financial markets. There is pessimism in Europe in particular, with risk appetite having decreased and capital flowing into safe havens. While there has been positive development in the stock markets during the summer, key indices in the euro area and the US are still lower than they were at the beginning of the year. Both short-term and long-term interest rates have been volatile, reflecting the nervousness in the markets. In the euro area, the government bond spreads between the southern Member States and Germany have widened, and the ECB has adopted a new monetary policy tool to keep the spreads under control. The US dollar has appreciated against other major currencies, reflecting the rapid tightening of monetary policy and higher interest rates.

Inflation remains high almost worldwide. The energy crisis is maintaining high inflation particularly in Europe. Inflation has also become broader, which is reflected in the acceleration of core inflation in many economies. Nevertheless, some signs of lower inflation expectations have emerged not only in the United States but also in Europe. Inflation is widely expected to slow in 2023.

The situation in the European energy market remains difficult. It may be necessary to regulate energy consumption during the coming winter. At the same time, however, the price of crude oil has fallen from the highs seen in the late spring of 2022. The price of natural gas is very high in Europe due to Russia's war of aggression and the resulting uncertainty. The prices of industrial raw materials, on the other hand, have declined sharply since the spring, perhaps reflecting the uncertain outlook in the industrial sector. Raw material prices are projected to decrease moderately during the outlook period.

Raw material prices

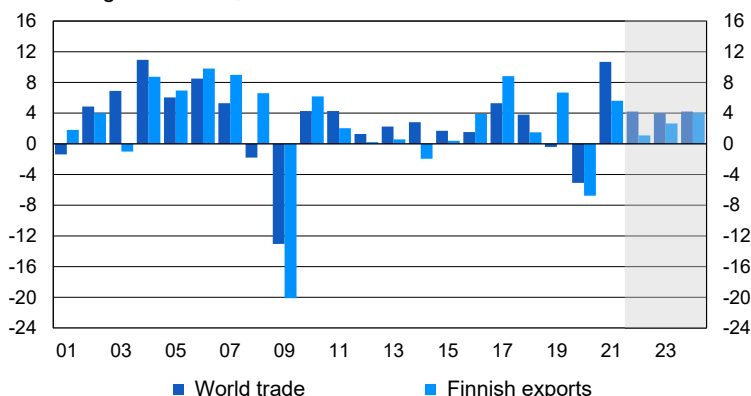


1.1.2 World trade

World trade in goods has been characterised by a high level of activity since the late spring. The carry-over effect of robust trade in late 2021 is also contributing to the fairly high rate of trade growth in 2022. Some signs have emerged to suggest that the component shortages that have disrupted world trade are starting to ease. However, increased tensions in East Asia may have an adverse impact on the busy shipping traffic in the South China Sea. World trade will grow by 4.2% in 2022 and subsequently slow to 4.0% in 2023, reflecting the situation in the global economy.

World trade

change in volume, %



1.1.3 Risks

Risks associated with the outlook of the global economy are heavily skewed to the downside. A key risk in Europe and the United States is the economy drifting into a recession in late 2022 and early 2023. Rapid inflation continuing for longer than expected, and the consequent decline in the real incomes of households, would be a significant recessionary factor. If Russia's war of aggression were to be prolonged, it would be reflected in the continuation of economic uncertainty in Europe in particular. The difficult situation in the energy markets may lead to a crisis in Europe in the coming heating season. The potential escalation of geopolitical tensions between China and the United States would cast a shadow over the economic outlook globally.

Upside risks include the broader-than-expected easing of the logistics problems that have afflicted world trade in goods. Furthermore, inflation may decline faster than expected in many economies due to the weakened outlook of the world economy.

Table 4. Gross domestic product

	2019	2020	2021	2022**	2023**	2024**
	change in volume, %					
World (PPP)	3.0	-3.1	6.3	2.7	2.5	3.0
Euro area	1.6	-6.5	5.6	2.1	1.3	1.8
EU	1.9	-5.9	5.3	2.1	1.3	1.8
Germany	1.1	-4.9	2.9	1.6	0.9	1.8
France	1.9	-7.9	6.8	2.0	1.2	1.7
Sweden	2.0	-2.3	4.9	1.8	1.6	2.1
United Kingdom	1.7	-9.3	7.4	2.7	1.8	1.4
United States	2.3	-3.4	5.8	2.1	1.4	2.1
Japan	-0.2	-4.6	1.8	0.7	0.3	0.6
China	6.0	2.2	8.1	4.1	4.6	4.9
India ¹	3.7	-6.8	9.5	6.0	6.7	5.5
Russia	2.2	-2.7	4.7	-7.0	-2.0	0.0

¹ Fiscal year

Sources: Statistical authorities, MoF

Table 5. Background assumptions

	2019	2020	2021	2022**	2023**	2024**
World trade growth, %	-0.4	-5.1	10.7	4.2	4.0	4.2
USD/EUR	1.12	1.14	1.18	1.06	1.00	0.98
Industrial raw material price index, EA, € (2015=100)	100.9	100.0	140.1	154.4	135.5	134.0
Crude oil (Brent), \$/barrel	64.1	43.4	70.7	102.9	89.8	81.7
3-month Euribor, %	-0.4	-0.4	-0.5	-0.1	1.3	1.5
Government bonds (10-year), %	0.1	-0.2	-0.1	1.4	1.8	2.0
Export market share (2010=100) ¹	99.9	98.1	93.7	90.9	89.8	89.6
Import prices, %	0.4	-5.1	9.5	20.8	2.5	0.5

¹ Ratio of export growth to world trade growth

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

1.2 Foreign trade

1.2.1 Exports and imports

Russia's invasion of Ukraine has significantly weakened the outlook for Finland's foreign trade. Russia's share of Finland's exports and imports has been halved since the invasion began, but trade has not yet come to a complete halt. At the same time, the economic outlook of the euro area and the United States has emerged as a factor that casts a shadow over foreign trade. The economic outlook of Germany, which is an important trading partner for Finland, has deteriorated since the spring. At the same time, rapid inflation is eroding consumer purchasing power in Europe as well as the United States. The sharp increases in export and import prices will also curb the development of export and import volumes, particularly in the early years of the outlook period. China's rigorous COVID-19 shutdowns are also causing uncertainty in world trade, which is reflected in a risk to Finland.

The volume of exports will grow by 1.1% in 2022. The slowdown in export growth is projected to come mainly from goods exports, while services exports will remain strong, driven by, among other things, tourism as well as telecommunications, information technology and information services. Export growth will pick up in 2023 as companies manage to find substitutes for the lost Russian market. At the same time, however, the weakened economic outlook of the euro area will limit growth

from the other direction. The volume of exports is projected to grow by 2.7% in 2023. The recovery in export volume will be stronger in 2024, with projected growth of 4.0% driven by trade in goods picking up in particular.

The volume of imports will grow by 1.8% in 2022. In imports, the impacts of the war arise from sanctions, trade disruptions and declining exports. However, import products can be substituted more quickly than new export markets can be found, in addition to which public investment will support imports in the early part of the outlook period. Imports of goods and services are expected to grow by 2.6% in 2023 and by 3.2% in 2024.

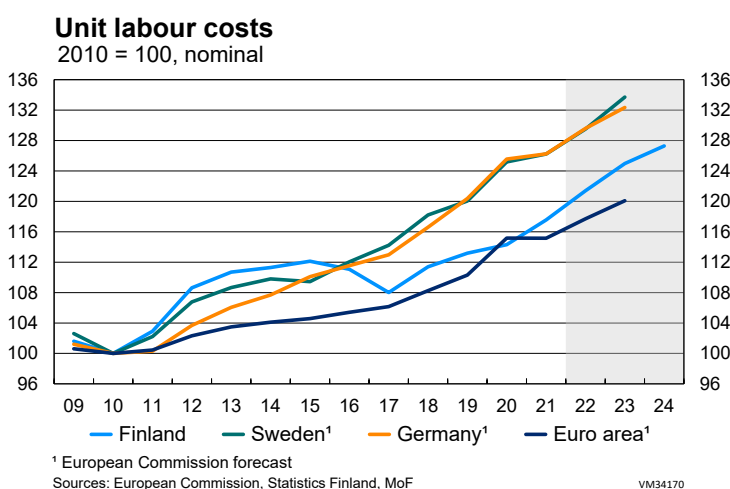


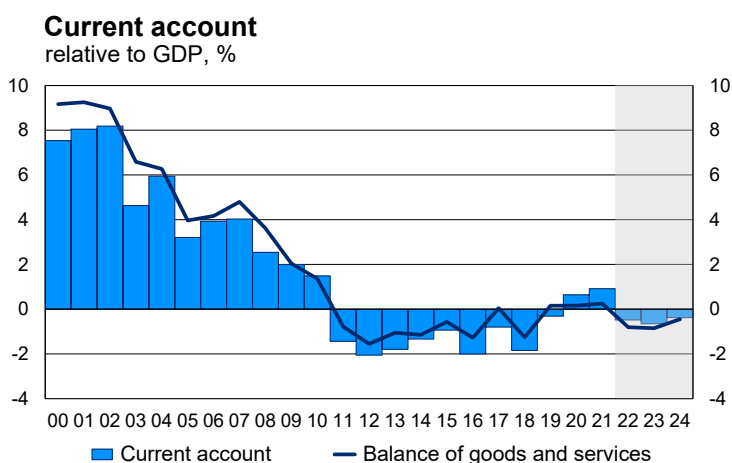
Table 6. Foreign trade

	2019	2020	2021	2022**	2023**	2024**
	change in volume, %					
Exports of goods and services	6.7	-6.8	5.6	1.1	2.7	4.0
Imports of goods and services	2.4	-5.8	5.6	1.8	2.6	3.2
	change in price, %					
Exports of goods and services	-0.2	-4.1	9.7	18.7	2.4	0.6
Imports of goods and services	0.4	-5.1	9.5	20.8	2.5	0.5

1.2.2 Prices and current account

Prices have increased rapidly in 2022. Due to structural differences between exports and imports, import prices are increasing faster than export prices in 2022. This will temporarily weaken Finland's terms of trade. Upward pressure on prices is driven particularly by goods, in terms of both import and export prices. Import prices are projected to increase by 20.8% in 2022, with export prices increasing by 18.7%. The increase in prices is expected to level off to a significant degree in 2023. Import prices are still increasing faster than export prices, but the difference is no longer substantial. Import prices are projected to increase by 2.5% in 2023, with export prices increasing by 2.4%. The slowing of the rise in prices will continue in 2024, with import prices projected to increase by 0.5% and export prices by 0.6%. The difference between the price increases of goods and service will diminish towards the end of the outlook period.

The current account showed a surplus of EUR 2.3 billion in 2021 after revisions to the statistics. The current account is projected to turn to a deficit of EUR 1.3 billion in 2022, particularly due to exports growing less than imports. Primary income is also projected to weaken in 2022, reducing the surplus of factor incomes and income transfers. Exports will not recover during the outlook period to the level seen before Russia's invasion of Ukraine, which will keep the current account at a deficit in 2023 and 2024. The factor incomes and income transfers account will continue to decline towards the end of the outlook period, but it is projected to remain at a surplus. The current account in ratio to GDP was 0.9% in 2021 and is projected to be -0.5% in 2022.



Sources: Statistics Finland, MoF

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Table 7. Current account

	2019	2020	2021	2022**	2023**	2024**
	EUR bn					
Balance of goods and services	0.4	0.4	0.6	-2.2	-2.4	-1.3
Factor incomes and income transfers, net	-1.1	1.2	1.7	0.9	0.6	0.2
Current account	-0.7	1.5	2.3	-1.3	-1.8	-1.1
Current account, relative to GDP, %	-0.3	0.6	0.9	-0.5	-0.7	-0.4

1.3 Domestic demand

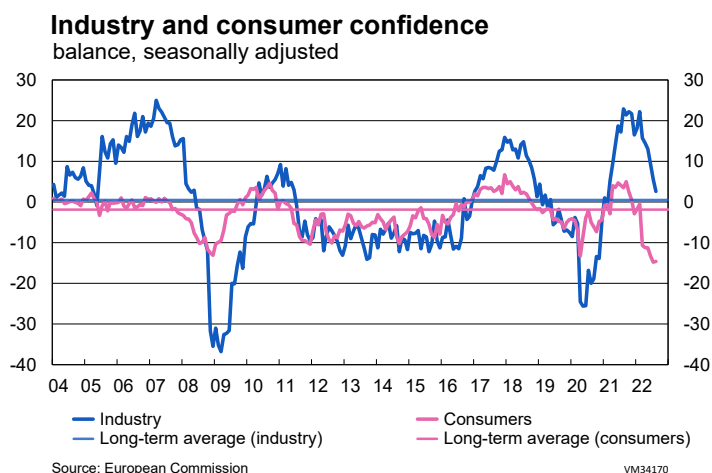
1.3.1 Private consumption

Household consumption decreased in the first quarter of 2022, mainly as consumption of durables declined markedly. According to a flash estimate by Statistics Finland, GDP growth was 0.6% in the second quarter, but no statistical data was available on the development of private consumption in the second quarter at the time of preparing the forecast.

The rapid increase in prices is eroding households' purchasing power, which in turn is worsening the potential for private consumption growth, particularly this year and next. The uncertainty caused by Russia's war of aggression and the ensuing sanctions has also undermined consumer confidence, which appears to be delaying consumption particularly with regard to durables.

Total private consumption will increase by 1.1% in 2022 as, regardless of the price hikes, service consumption will increase as the COVID-19 pandemic recedes.

In 2023, private consumption growth will slow to 0.8% as employment growth comes to a halt and the real incomes of households grow only slightly. As the rise in prices slows, household purchasing power will increase more rapidly in 2024, with private consumption growth accelerating to 1.4%.



Consumers' confidence in their own finances deteriorated further in July: consumers' assessments of the current state of their own finances and of their own financial situation after 12 months both turned negative, which is highly exceptional. Nevertheless, it should be noted that still only 31% of consumers expect their finances to deteriorate over the next 12 months.

The sum of wages and salaries has continued to show strong growth: in March–May, the sum of wages and salaries of the whole economy was up by almost 6% year on year. However, the growth of the sum of real wages and salaries levelled off in the spring as inflation accelerated to approximately 7%.

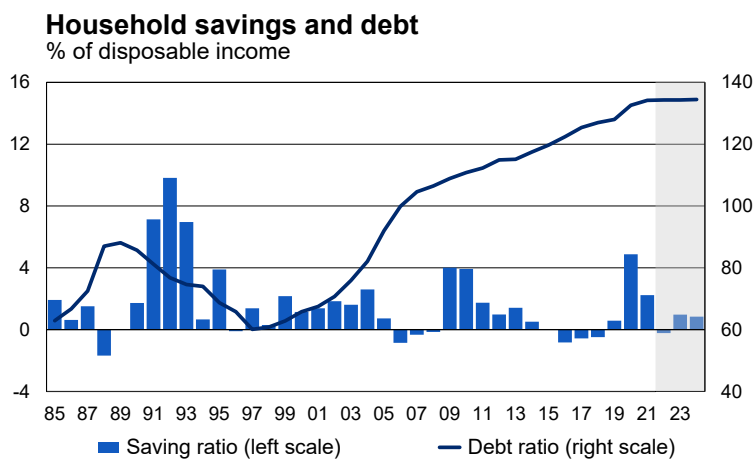
The volume of retail sales in the second quarter was almost 4% lower than a year earlier. Payment card data from banks also indicates that the consumption of goods declined during the first half of the year. At the same time, the turnover trend chart for services and payment card data both indicate that service consumption grew during the first half of the year.

Consumption of durables began to decline in late 2021 compared to the very high level seen during the COVID-19 pandemic. First registrations of cars in the first half of 2022 have been over 20% lower than in the previous year, but the lengthening of delivery times caused by component shortages is also contributing to this. As a result of the weak start to the year and exceptionally low consumer confidence, durables consumption is projected to decline by just under 9% in 2022. Next year, moderate growth of 1.5% is projected for durables consumption.

The consumption of semi-durables also turned to a decline in the first half of the year, and their consumption in 2022 as a whole is projected to increase by less than 1%. Next year's growth will also be very slow.

The surge in energy, fuel and food prices will result in a downturn in non-durables consumption in 2022, even though the price elasticity of non-durables consumption is typically relatively low due to weak substitutability. Non-durables consumption is not projected to grow next year due to the high prices.

Service consumption continued to grow during the first half of the year. Consumption is projected to grow by 4% in 2022, as service consumption is still below the pre-pandemic level. However, the war in Ukraine is expected to slow the recovery of international travel to some extent due to the rerouting of flights to Asia, for example. As household purchasing power declines, service consumption growth will slow to 1% in 2023.

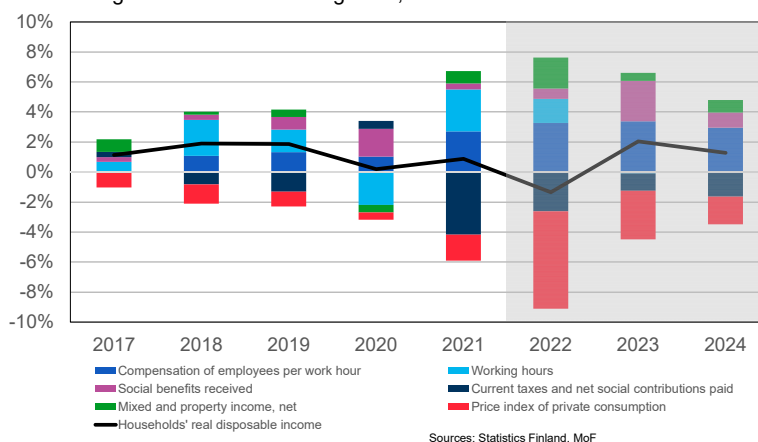


Sources: Statistics Finland, MoF

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The savings ratio is projected to approach zero already this year as the price of private consumption rises faster than incomes. The rate of increase in the debt ratio is projected to slow down this year due to higher interest rates.

Households' real disposable income¹ change and contributions to growth, %



Households' real disposable income, which approximates the combined purchasing power of households, increased almost 1% in 2021, mainly due to growth in the compensation of employees.

Household purchasing power is projected to decline by approximately 1% in 2022, as the exceptionally rapid increase in consumer prices will fully eat up the increase in disposable income. Purchasing power is also cut by the slow growth of social benefits received, as the high inflation of 2022 will increase index-based benefits mostly in 2023. The rise in average earnings will be slightly boosted in 2022 by the temporary increase in employers' pension insurance contributions.

Households' real disposable income is projected to rebound in 2023 as inflation slows and social benefits received increase substantially due to cost-of-living index increases. The growth of the price of private consumption is projected to slow to approximately 3% in 2023 and less than 2% in 2024.

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

Table 8. Consumption

	2021	2019	2020	2021	2022**	2023**	2024**
	share, %	change in volume, %					
Private consumption	100.0	0.7	-4.1	3.6	1.1	0.8	1.4
Households	95.8	0.9	-4.3	3.7	1.1	0.8	1.4
Durables	8.1	2.5	3.3	4.5	-8.6	1.5	3.2
Semi-durables	7.5	2.4	-9.5	11.6	0.7	0.6	1.1
Non-durable goods	28.5	-0.1	1.5	2.0	-1.4	0.1	0.7
Services	51.7	1.4	-6.9	3.5	4.0	1.0	1.4
Consumption by non-profit institutions	4.2	-2.5	1.9	1.6	1.1	0.8	1.4
Public consumption		2.0	0.5	2.7	1.8	-0.2	0.1
Total		1.1	-2.6	3.3	1.4	0.5	1.0
Households' disposable income		2.9	0.7	2.6	5.1	5.3	3.1
Private consumption deflator		1.0	0.5	1.7	6.5	3.2	1.8
Households' real disposable income		1.9	0.2	0.9	-1.4	2.0	1.3
		%					
Consumption in relation to GDP (at current prices)		75.8	75.4	75.4	75.5	75.6	75.4
Household savings ratio		0.6	4.9	2.2	-0.2	1.0	0.8
Household debt ratio ¹		128.0	132.6	134.2	134.3	134.3	134.5

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

1.3.2 Public consumption

Public consumption expenditure grew exceptionally quickly last year. Consumption expenditure was increased, in particular, by the significant growth of the costs of treating and combating the COVID-19 pandemic and, moreover, by the gradual normalisation of public services compared with spring 2020, when many functions were underused due to restrictions related to COVID-19.

The growth in public consumption expenditure is projected to slow to 1.8% in 2022, as the additional spending prompted by the COVID-19 pandemic decreases,

even though some of the appropriations budgeted for 2021 were pushed back to the current year. Growth in consumption expenditure is being sustained by factors including growing demand for services due to population ageing, preparedness required due to Russia's invasion of Ukraine and increases in immigration, and the extended tasks introduced by the Government Programme, with the related costs increasing annually.

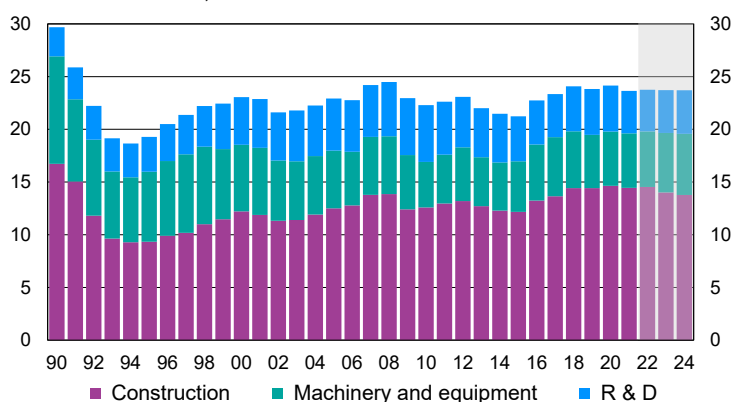
The volume of public consumption will contract in 2023 as the parliamentary term ends and certain once-off additional expenditure items come to an end. In 2024, the rising demand for services will increase the growth of health and social services expenditure, but with some of the expenditure financed with the Recovery and Resilience Facility being eliminated and the transition costs arising from the start-up and organisation of the wellbeing services counties decreasing, the growth in consumption expenditure will be fairly moderate at just 0.1%. The value of public consumption will, however, rise faster than in recent years as prices rise throughout the outlook period. The earnings development of the entire local government sector (including the administration of the wellbeing services counties) is assumed to be in line with the pay increases agreed upon this past summer and the five-year pay programme, which will increase local government sector pay by a total of approximately 5.1% over five years in addition to agreement increases. The forecast includes the risk of consumption prices rising more rapidly due to the nurse unions' wage increases.

1.3.3 Private investment

Growth in private investment during the outlook period is a little slower than average due to the prevailing uncertainty. The continued strong housing construction, however, will support investment this year, and private investment will grow by 2.8%. Investments in housing construction will develop favourably as there was a high level of housing starts in late 2021. As uncertainty continues, other construction will not pick up significantly. In 2023, the global economic outlook is weaker than this year, which will be reflected in investment. The investment outlook for Finnish manufacturing industries was bright after the COVID-19 pandemic, and the outlook for 2022 remains positive, but uncertainty may lead to the postponement or suspension of investment projects in the future. Financing from the EU's Recovery and Resilience Facility (RRF) will again boost private investment during the outlook period. Private investment will grow by 0.1% in 2023 and by 2.9% in 2024. Over the entire outlook period, private investment will grow at an average rate of 1.9% and the ratio of private investment to GDP will remain at around 19%.

Investments

relative to GDP, %



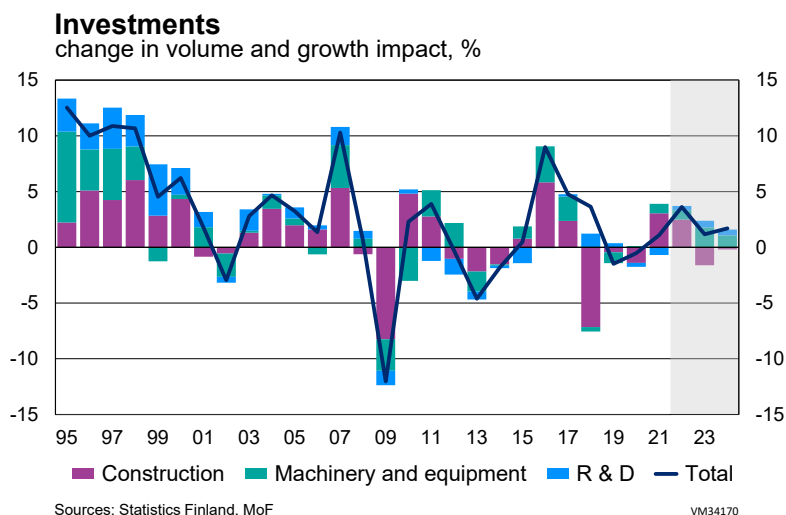
Sources: Statistics Finland, MoF

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The trend in housing construction will remain strong in 2022. As a result of last year's positive development in housing starts, housing investments will grow by 6.0% this year. The trend in housing construction permits was unfavourable in the first half of the year, so housing starts will fall from their 2021 level, which will be reflected next year in declining housing investments. At the end of the outlook period, the number of housing starts will decline to a level that is closer to the long-term average. Repair construction will have a positive effect on housing construction investments during the outlook period. The change in housing investment will be -4.2% in 2023 and -1.5% in 2024. The demand for housing loans is showing signs of slowing. The uncertainty will also be reflected in housing construction during the outlook period.

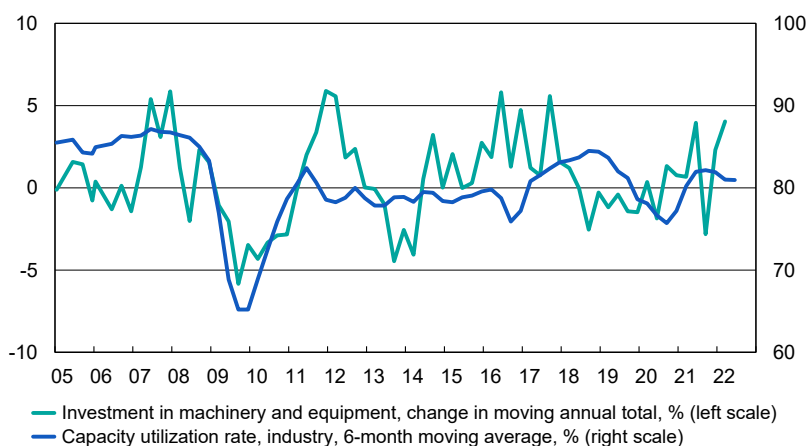
Non-residential building construction investments will grow by 1.5% in 2022. The growth rate will be moderate, as the prevailing economic uncertainty affects investment projects in facilities construction in spite of the favourable industrial outlook for 2022. Progress will be made in projects already under way, but most new investment plans are likely to be postponed. The development of non-residential building construction will be only slightly more positive towards the end of the outlook period as uncertainty is reduced. Investment growth will be -0.5% in 2023 and 1.2% in 2024. Civil engineering investments will show moderate growth in 2022 due to factors including the high price of oil, and investments will decline in

2023 in line with the trend in other construction activity. At the end of the outlook period, as uncertainty is reduced, growth will again return closer to average.



Machinery, equipment and transport equipment investments will grow in 2022, driven by industrial activity. Projects such as those in the energy sector to implement the green transition will see rapid progress this year and the next. Overall, the level of investment in machinery and equipment will be reasonably high during the outlook period. Machinery and equipment investments will grow by 4.0% in 2022, by 8.8% in 2023 and by 5.0% in 2024. Other investments, including research and development investments, will grow throughout the outlook period, but the uncertainty will weaken this growth in the early part of the outlook period. RDI investments will be supported during the outlook period with financing from sources including the Recovery and Resilience Facility (RRF) and changes in taxation, which will accelerate investments as the outlook period progresses.

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

	2021	2019	2020	2021	2022**	2023**	2024**
	share, %	change in volume, %					
Buildings	53.1	-0.7	-2.3	5.0	4.1	-2.6	-0.3
Residential buildings	30.3	-4.2	-3.2	5.8	6.0	-4.2	-1.5
Non-residential buildings	22.9	4.3	-1.2	4.1	1.5	-0.5	1.2
Civil engineering construction	8.0	-5.3	10.7	-17.3	2.0	-0.5	1.0
Machinery and equipment	21.9	-4.4	0.5	4.1	4.0	8.8	5.0
R&D-investments ¹	17.0	2.1	-2.0	-4.1	2.5	4.0	3.5
Total	100.0	-1.5	-0.5	1.1	3.6	1.2	1.7
Private	82.3	-2.3	-3.1	4.6	2.8	0.1	2.9
Public	17.7	2.4	11.1	-12.8	7.3	5.9	-3.3
		%					
Investment to GDP ratio (at current prices)							
Fixed investment		23.8	24.1	23.6	23.8	23.7	23.7
Private		19.4	19.2	19.5	19.4	19.2	19.4
Public		4.4	4.9	4.2	4.4	4.6	4.3

¹ Includes cultivated assets and intellectual property products

1.3.4 Public investment

Public investment has been high in recent years, accounting for more than 4% of GDP. In Finland, the ratio of public investment to GDP is considerably higher than in the EU countries on average. Last year, public investment declined significantly in both central and local government. This was attributable to a reduction in weapons system investments and construction-related expenditure. Although public investment contracted by as much as 12% year-on-year, the ratio of public investment to GDP was still above the longer-term average. The share of total investment accounted for by public investment was also high.

In 2022, public investment will be increased by efforts to improve Finland's security and security of supply in response to changes in the security environment. The EU's Recovery and Recovery Facility (RRF) will increase financing for investments promoting the green transition and digitalisation. In addition, there are investment costs associated with the establishment of the wellbeing services counties.

In 2022, public investment will account for approximately 18% of total investment, corresponding to EUR 9.8 billion. Local government investments account for just over half of public investment, while central government investments account for just under half. Social security funds represent a very small share of the total. From 2023 onwards, local government investments will be partially transferred to the wellbeing services counties. These investments account for around 10% of all general government investments. Civil engineering investments and other construction investments both account for close to 30% of public investment. Research and development investments account for just over 25% and machinery and equipment investments for just over 10% of the total.

Next year, public investment growth is projected to continue at around 6%, driven by central government measures to strengthen cybersecurity, national defence and border control. The Government's discretionary increases in transport infrastructure investments will cease in 2023. Some local government investments will be transferred to the wellbeing services counties in connection with the health and social services reform, but the slowdown in hospital construction will also reduce investments.

At the end of the outlook period in 2024, investments will decrease as the one-off investment increases of the previous years come to an end. Central government will

increase investments in R&D activity and the Border Guard's vessel procurement. In local government, investment pressure will continue due to population migration and the age of the building stock. In recent years, many new hospitals have been built and old ones renovated. The investment peak in hospital construction has now been passed, but significant new investments are still expected in many areas. There are uncertainties related to the start dates of individual projects.

The forecast takes into account the decisions made by Prime Minister Sanna Marin's government regarding the General Government Fiscal Plan, central government spending limits, the budget and the supplementary budgets. Discretionary measures during the upcoming parliamentary term and by the next government may have a significant impact on public investment in the final years of the outlook period.

1.4 Domestic production

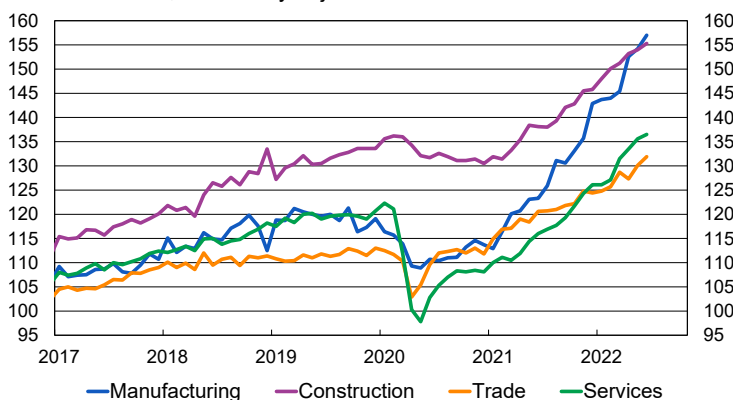
1.4.1 Total output

The value added of the Finnish economy increased by 3.9% year-on-year in the first quarter. Manufacturing industry grew very strongly, by more than 7% year-on-year. The highest growth came from the metal industry. At the same time, the largest sector of the national economy, i.e. services, remained close to the level seen at the end of last year. Year-on-year growth was still 3.8%, however. Trade contracted by almost 4% year-on-year, as the sharp rise in prices kept the change in volume in check, even though the value of trade increased. The reduction in private consumption, among other things, contributed to this.

The rise in prices has been the sharpest since 1989–1990. Among other things, this has been brought about firstly by the strong increase in demand after the COVID-19 pandemic as well as the war of aggression started by Russia in Ukraine in spring 2022. Raw material prices are fluctuating sharply and this reflects significant uncertainty about the direction of future international economic development. It is projected that the price changes will continue to have the effect of slowing demand and thereby also output. However, based on the operating surplus and the interim financial results of companies, businesses have also been able to pass their increased costs on to the prices of their products.

Turnover trends in main industries

2015 = 100, seasonally adjusted

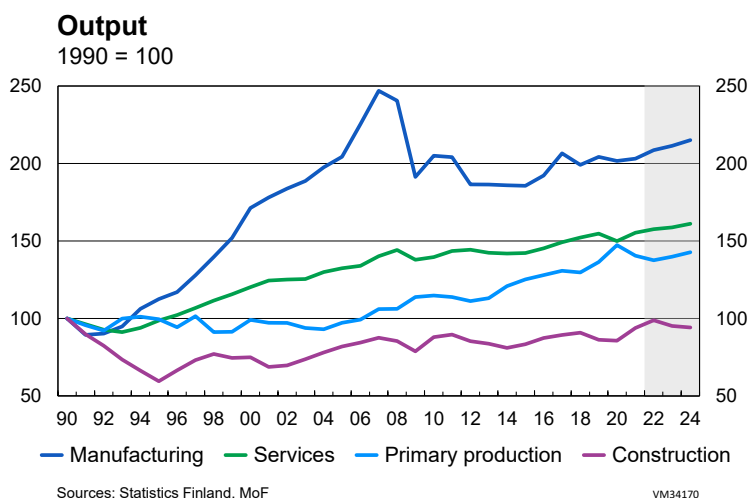


Lähde: Tilastokeskus

The early part of the year was characterised by major changes in the operating environment, but the order books of companies were still at a good level, ensuring their ability to increase production. The prolongation of Russia's war of aggression contributes to ongoing uncertainty and high costs for raw materials. The impacts have also been particularly evident in the deterioration of household confidence and the collapse in construction sector expectations. The adverse impacts of the war are expected to become progressively more visible in manufacturing, in services more broadly than trade as well as in construction and primary production.

Furthermore, the pursuit of substitute markets will intensify competition globally and, at the same time, there has been a shift to tightening monetary policy, while financial policy – which was highly stimulus-oriented during the years of the COVID-19 pandemic – will not increase total demand to the same extent as during the pandemic. Global economic growth will slow in the autumn and next year, reducing export demand in Finland.

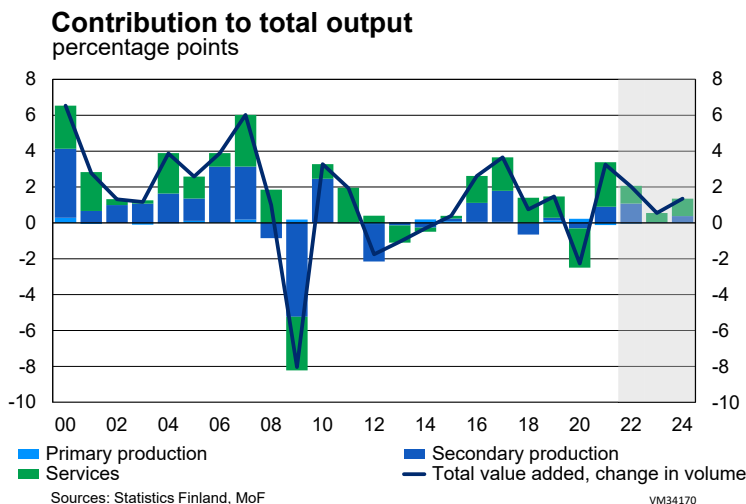
In 2022, the growth of total output is projected to slow to 1.9%. Manufacturing and construction will grow by 3.5%, while services will grow by 1.5%. In primary production, the grain harvest is projected to normalise from last year's exceptionally poor level. Forestry, on the other hand, suffered from a strike in the paper industry in the early part of the year. Last year's record high housing starts will maintain construction production well this year.



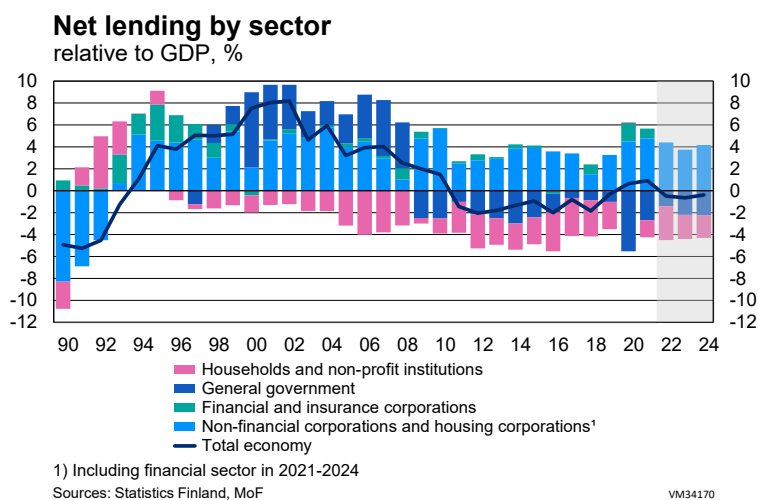
The erosion of purchasing power caused by the rapid increase in prices will reduce household consumption and investment demand throughout the outlook period. Public sector demand for war industry products is growing in Finland and elsewhere due to the war of aggression started by Russia. Investments related to the green transition are also gradually increasing total demand. Examples of these include investments related to clean energy production and new technology adoption financed under the Recovery and Resilience Plan.

Growth of only just over 0.5% is projected for 2023, as global economic growth and demand for international trade are expected to be subdued. Finland's export demand will be adversely affected, particularly by the slowing EU economy. Construction will decline sharply next year as housing starts are expected to continue to decrease in line with the current trend in building permits.

Economic growth is projected to be 1.3% in 2024. The economy is projected to recover over the course of the year as inflation slows and the tightening of monetary policy diminishes. The growth rates of the main sectors will exceed their average level except in the case of construction, where production will continue to settle at a more normal level after the highs seen after the COVID-19 pandemic. The output gap is projected to still be slightly open at the end of the outlook period.



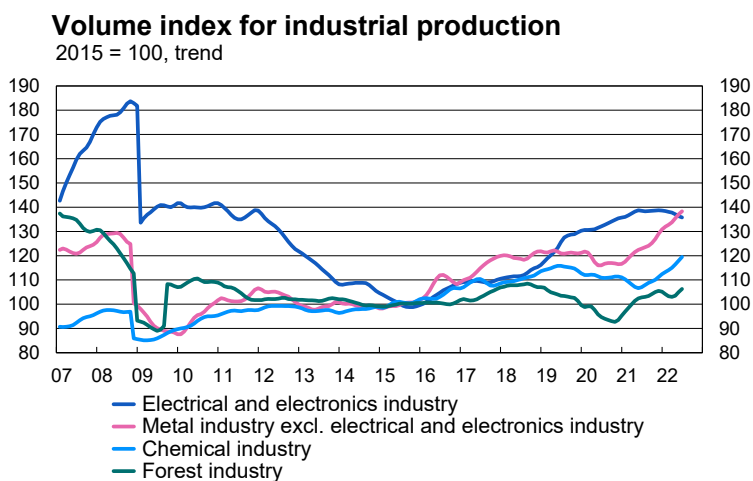
This year, the productivity of the Finnish economy per employed person will decline by approximately 0.5%, after which the annual growth rate will increase to just under 1% on average in 2023–2024. The operating surplus is projected to grow by slightly more than 9% in 2022 and to decrease gradually due to slower economic growth so that the increase in the operating surplus would be approximately 4% in 2024. Nominal unit labour costs in Finland are projected to increase by just over 3% in 2022 and to subsequently slow to an average annual rate of about 2% in 2023 and further to approximately 1% in 2024 as productivity improves.



1.4.2 Secondary production

Manufacturing

The economic situation in manufacturing remains quite good, as manufacturing order books are higher than average. Nevertheless, the stream of new orders is already diminishing, and the value of orders has been increased by higher prices, which means that the number of orders has not increased in line with their value. Output growth in the first half of the year was still faster than last year, but the sector's economic outlook is already substantially weaker than last year according to the Business Tendency Survey. There are large differences in demand between the sectors and also within them.

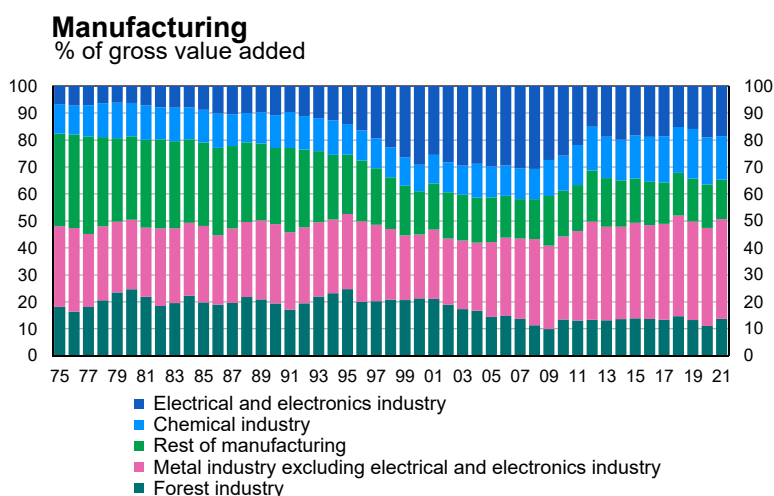


In the forest industry, new orders have declined, output has turned to a decline and development for the whole year is expected to remain weak. The long strike in the paper industry, in particular, will reduce the sector's value added this year. Next year, substantial growth is projected for the forest industry, particularly due to a significant increase in the industry's capacity.

In the chemical industry, order volumes vary significantly from month to month. Orders turned to growth in the summer, brightening the situation. At the same time, however, the outlook continued to weaken due to declining order books and diminishing demand. Capacity constraints and material shortages will limit output growth in the short term.

The metal industry, excluding the electrical and electronics industry, saw very strong growth in the early part of the year. A large number of new export orders were received by the electrical and electronics industry in the spring, and the outlook for the rest of the year is positive. The metal industry accounts for most of the manufacturing value added. The chemical industry is the second-largest manufacturing industry and around half the size of the metal industry. Most of the manufacturing output is exported.

Manufacturing value added is projected to grow by slightly under 3% this year. Next year, growth is projected to slow to just over 1% due to weaker export demand. Output growth is projected to accelerate to slightly under 2% in 2024, driven by increasing exports.



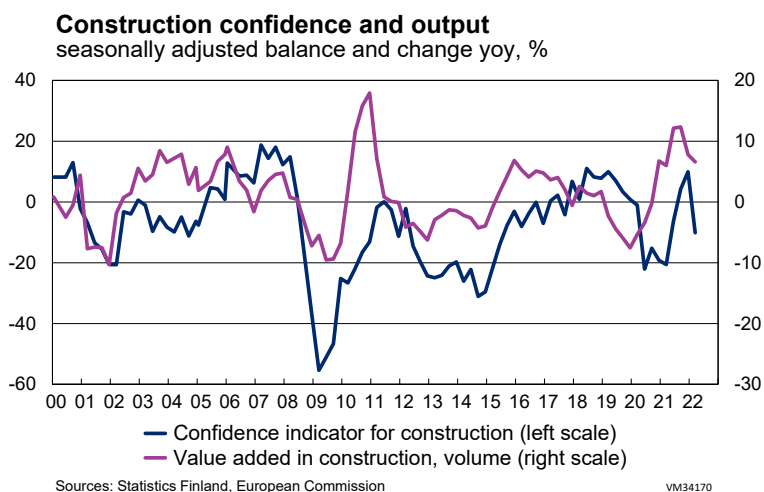
Source: Statistics Finland

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Construction

Construction grew in the first quarter of this year. This was due to last year's exceptionally high rate of housing starts. However, construction began on just over 17,000 homes in January–May 2022, which was less than in the corresponding period last year. The number of non-residential starts also decreased year-on-year. The biggest change was seen in building permits, where the cubic volume of granted permits in the first half of the year was approximately 25% lower than in the previous year. The cubic volume of granted permits for apartment buildings decreased by around 16% year-on-year in January–May. The cubic volume of granted permits for non-residential buildings decreased by 27% year-on-year during the first half of the year.

Uncertainty, rising prices and the expected rise in interest rates are reducing interest in borrowing and will therefore reduce housing production volumes in the coming years. On the other hand, the continuing relatively good employment trend is maintaining housing demand. Construction of approximately 40,000 homes is projected to start this year. Next year, the number is expected to decline by several thousand. Other construction projects are also being adversely impacted by rising prices and uncertainty, with the possibility of projects being postponed and partly cancelled.



Repair construction accounts for around half and new construction work for the other half of construction output. Repair construction is projected to develop favourably this year and next, but the increasing prices of renovations may

temporarily slow the rate of growth. Repair construction is projected to grow by an average of 2% each year over the outlook period.

The volume of civil engineering construction is estimated to grow to some extent this year. Civil engineering construction will decline slightly next year due to factors including the weak financial situation of municipalities and the slowing progress of rail projects.

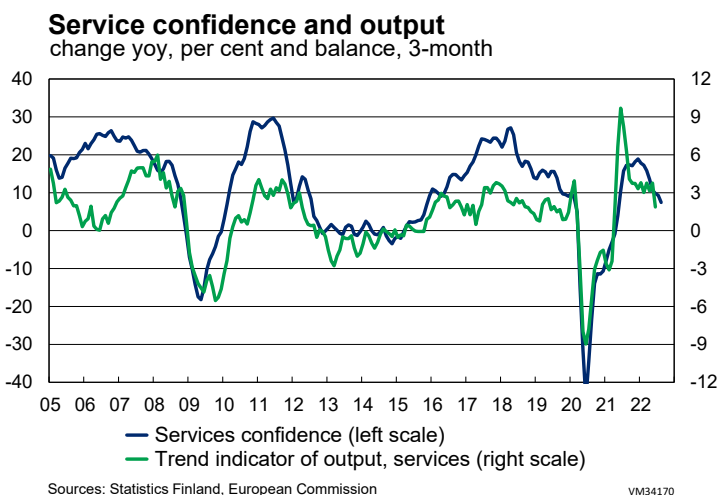
The value added of construction will increase by 5.3% in 2022 and decrease by nearly 4% next year. In 2024, the value added of construction will decline by a further 1%.

1.4.3 Services

There was a broad-based increase in service production in the first half of the year. Sales volumes increased in several service sectors, albeit not as quickly as the value of turnover. Growth was particularly strong in the accommodation and restaurant sector, which is recovering from the COVID-19 pandemic, but double-digit growth was also seen in business services. The most substantial contraction was seen in the sales volume of the trade sector, which was weighed down by the weak development of the wholesale trade.

According to the Business Tendency Survey, the service sectors estimate that sales will continue to grow, but at a slower rate. Constraints to growth in the service sectors are particularly due to a lack of skilled labour. The Business Tendency Survey suggests further substantial growth in the accommodation and restaurant sector, with growth most commonly expected in the information and communication services sector. In the transport sector, growth is constrained by rising costs.

Service sales will grow by approximately 1.5% in 2022, with services accounting for a majority of the change in combined value added. In particular, business services and information and communication services are expected to continue to develop favourably. Service growth will be restricted this year by the erosion of household purchasing power, the weakening of the international economy and the cessation of trade with Russia. The erosion of household purchasing power will also slow the recovery this year of sectors adversely affected by the pandemic, such as other services and the arts, entertainment and recreation. Service growth will be supported by public services activities in 2022.



In 2023, production is projected to generally grow in all service sectors, although the real estate sector will suffer from the decline in construction and public service production will also decline slightly next year. Public services, which include public administration, education, health and social services, make up the largest individual sector in services. The strongest growth is again expected to be in the information and communications sector. In 2024, the rate of service growth will be average at 1.5%.

Table 10. Production by industry

	2021	2019	2020	2021	2022**	2023**	2024**
	share, % ¹	change in volume, %					
Industry	20.6	2.6	-1.3	0.7	2.7	1.3	1.7
Construction	7.7	-5.1	-0.7	9.6	5.3	-3.8	-1.0
Agriculture and forestry	2.6	5.2	8.0	-4.6	-2.1	1.6	2.1
Industry and construction	28.4	0.5	-1.1	3.2	3.5	0.0	1.1
Services	69.0	1.7	-3.1	3.6	1.5	0.8	1.5
Total production at basic prices	100.0	1.5	-2.3	3.2	1.9	0.6	1.3
GDP at market prices		1.2	-2.2	3.0	1.7	0.5	1.4
Labour productivity in the whole economy		0.2	0.2	0.1	0.3	0.7	1.3

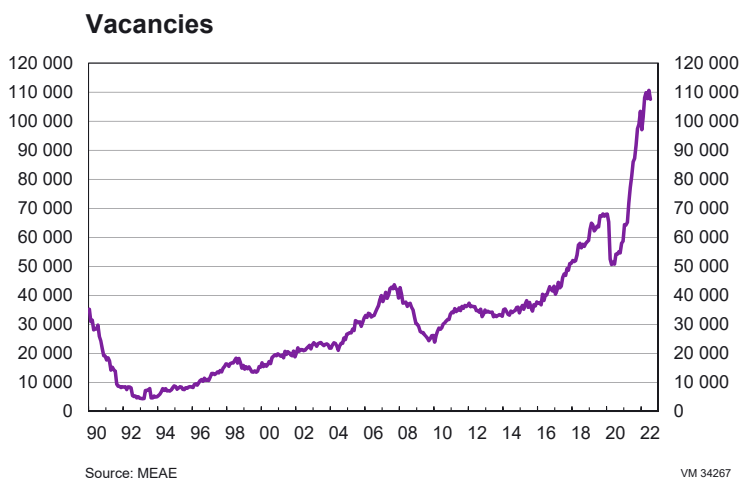
¹ Share of total value added at current prices

1.5 Labour force

The situation in the labour market was exceptional in the summer. While the number of employed persons has continued to grow and there is a record number of job vacancies – also in relation to the number of unemployed jobseekers – the decline in unemployment has levelled off. Consequently, there is a lot of labour in the labour market, as the pull of the labour market draws new people into working life.

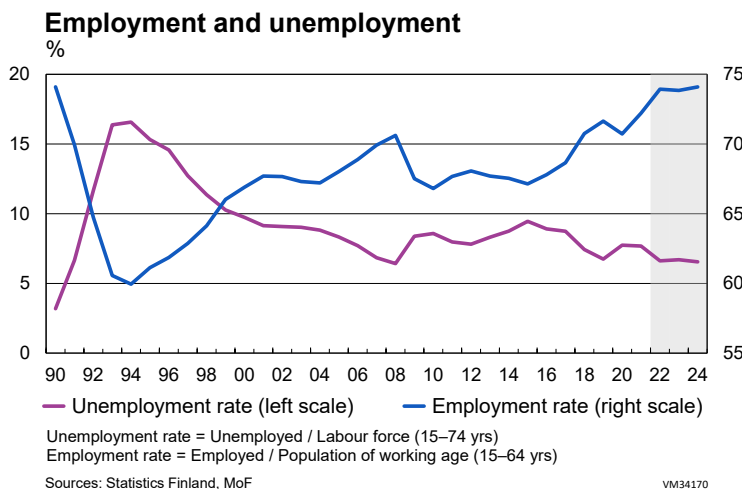
In the first half of the year, the number of employed people increased by 3.2%. The number of entrepreneurs has decreased slightly, but the number of wage and salary earners has increased. There are more people employed than last year in industry and particularly in the service sectors. The number of people employed in business, accommodation and restaurant services, in particular, has seen double-digit growth, as has been the case in social services. The number of people employed in the forest and chemical industries has increased more sharply than in the economy as a whole. The number of people employed in the public sector has also risen faster than in the private sector, so there are significant sector-specific differences in development. Full-time wage and salary earners represent a substantially larger proportion of employed people than last year, although the number of part-time employees has also grown. Consequently, the increase in work

performed, i.e. number of hours worked, was only about half of the increase seen in the number of employed people, i.e. 1.8%. The trend employment rate reached 74% in June, the highest level ever recorded as currently measured. The number of working hours has not yet reached its pre-COVID-19 pandemic level.



Labour market mismatches appear to have increased further, and competence gaps are weakening the conditions for economic growth. The number of job vacancies is high while the decrease in the number of unemployed people has levelled off. Business surveys show that it is challenging for companies to find the employees they need, particularly due to shortages of experience, special competence and education and training. According to the Confederation of Finnish Industries' Business Tendency Survey, companies' employment expectations were still positive in early 2022, with the exception of construction and the retail trade.

Employment growth will slow in the second half of the year. Economic growth is projected to diminish significantly, particularly in construction, trade and the chemical industry, which will lead to weaker demand for labour. Due to the strong first half of the year, the number of employed people for the full year will exceed last year's average by just over 2%. The employment rate will increase by 1.5%, nearly reaching 74%.



Economic growth is projected to be minimal next year, and labour demand is projected to decline, leading to a slight contraction in the number of employed people. Economic recovery will increase the number of employed persons in 2024, particularly in the service sectors. The employment rate will exceed 74% in 2024, partly due to the contraction of the size of the working-age population.

Strong growth in employment led to a clear fall in unemployment in the early part of 2022, but the decline levelled off in the summer. Furthermore, the number of long-term unemployed increased slightly in the early summer in the 25–49 age group, which is a key demographic in the labour market. The decline in unemployment was broad-based until the spring, with overall unemployment in the 20–69 age group being lower than in the previous year for both men and women. Unemployment was higher than in the previous year only in the 55–64 age group for men and the 45–54 age group for women.

The slowdown in economic growth is projected to increase unemployment during the remainder of the year. Nevertheless, due to the decline seen in the first half of the year, the unemployment rate will still be lower than last year by one percentage point at 6.6% of the labour force. Employment turning to a decline in 2023 will increase unemployment next year, particularly in secondary production, and the unemployment rate is projected to increase slightly compared to this year.

If, as assumed by the forecast, labour market mismatches and region-specific and occupation-specific availability of labour do not become an obstacle to the functioning of the labour market, the unemployment rate will fall to around 6.5% in 2024. This is still around one half of one percentage point above the level of structural unemployment in Finland estimated using the common methodology of 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	4101	4091
change	3	5	-10	-10	-12	-10
Population of working age (15–64 yrs)	3428	3421	3417	3414	3411	3410
change	-11	-7	-3	-4	-3	-1
Employed (15–74 yrs)	2533	2495	2555	2611	2606	2613
of which 15–64 yrs	2455	2420	2470	2524	2519	2526
Unemployed (15–74 yrs)	183	209	212	185	187	183
	%					
Employment rate (15–64 yrs)	71.6	70.7	72.3	73.9	73.8	74.1
Unemployment rate (15–74 yrs)	6.8	7.7	7.7	6.6	6.7	6.5
	1,000 persons per annum					
Immigration, net	15	18	23	23	23	23

1.6 Incomes, costs and prices

1.6.1 Wages and salaries

The rate of increase in nominal wages slowed in the first half of the year to 2.1% from last year's average of 2.4%. The slowdown was particularly due to a decrease in wage drifts, but the level of negotiated increases was also slightly lower than a year ago. The rate of increase in private sector earnings slowed due to lower negotiated increases, but in the public sector negotiated increases were higher, which also accelerated the rate of increase in earnings. Of the sectors, the rate of increase in earnings in secondary production slowed year-on-year, but in services the rate of increase accelerated, particularly in the real estate sector. Real wages fell by just under 3%, as inflation significantly exceeded the rate of increase in nominal earnings. Real earnings are projected to fall by nearly 4% on average this year.

A large number of new collective agreements have been concluded in many private and public sectors this year. Pay increases in the collective agreements concluded this year have most commonly been around 2%, which is slightly higher than last year. Furthermore, the municipal sector reached an agreement on a multi-year pay programme that will increase pay by approximately 1% per year for the next five years. Wage drifts are anticipated to be significant in the private sector in 2022 due to the high demand for competent personnel. This would mean a 2.6% increase in nominal earnings this year.

The most typical duration of collective agreements has been two years, but agreements on next year's increases are due to be made during this autumn or early 2023. In addition, the agreement in the municipal sector guarantees an increase of at least 1.9% in addition to the pay programme. This forecast assumes that the pay increases specified in the 2023 agreements will be higher than this year in the economy as a whole, which would deviate from the average practice of this millennium, where the pay increases specified in two-year agreements have been lower for the second year. The assumption is based on strong demand for labour and a significantly accelerated rise in consumer prices. Furthermore, wage drifts are projected to be higher than average next year due to the high demand for competent personnel. This would increase nominal earnings by 3.5% next year.

The rise in earnings growth in 2024 is linked to projected, subdued productivity growth. On the other hand, economic growth and the resulting rise in employment as well as labour shortages in some sectors are expected to keep wage drifts high. Nominal earnings are projected to increase by approximately 3% in 2024.

The sum of wages and salaries increased by 6.5% in the first half of the year. Towards the end of the year, the growth rate will slow down due to the high reference level and the waning of employment, resulting in the sum of wages and salaries growing by an average of nearly 5% for the entire year. In addition to nominal earnings, the sum of wages and salaries is also affected by employment trends. With employment contracting, the sum of wages and salaries is projected to increase by just over 3% next year, although it is assumed that the rate of increase in nominal earnings will accelerate. Next year, the rate of earnings growth is projected to slow while employment growth will accelerate, which would mean that the sum of wages and salaries will still increase by just over 3% in 2024.

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	1.9	2.5	2.0
Wage drift, etc.	0.1	0.7	0.6	0.7	1.0	1.0
Index of wage and salary earnings	2.1	1.9	2.4	2.6	3.5	3.0
Real earnings ¹	1.1	1.6	0.2	-3.9	0.3	1.2
Average earnings ²	2.0	1.9	2.2	3.1	3.4	3.3
Labour costs per unit of output whole economy ³	1.6	1.0	2.8	3.3	2.9	1.9

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

Inflation has continued to accelerate, emerging as a factor that slows down economic growth. Increased prices erode consumers' purchasing power and force households to think about their consumption behaviour.

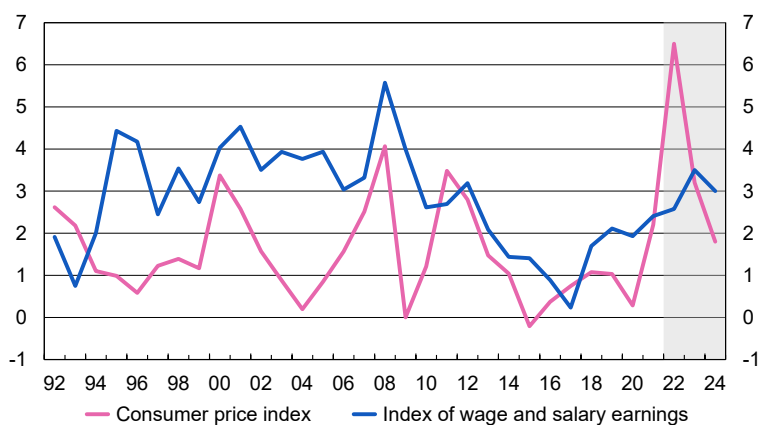
Inflation reached an annual rate of nearly 8% in July 2022. Although the acceleration of inflation is still mainly a consequence of rising energy prices, the number of rising prices in the consumer price index is 10 times higher than the number of falling prices. Inflation is very broad-based, with prices rising quickly in all consumption categories.

Average inflation of 6.5% is projected for 2022. However, inflation will be faster than average in the second half of 2022. In particular, based on the development of market prices, electricity prices are projected to continue to increase and to remain high until the early part of 2023. Energy prices will increase by over 31% in 2022 and further by nearly 8% in 2023. It is expected that the peak in energy prices will have been passed by the latter half of 2023. Energy prices are even expected to decline moderately starting from the second half of 2023.

Inflation is also projected to accelerate in the latter part of this year with regard to food prices, particularly in the case of fresh food. Increased costs are pushing producer prices higher, which is ultimately reflected in consumer prices. The increase in the price of energy and raw materials has also begun to be reflected in the prices of goods and services. Rising wages are increasingly reflected in the prices of services, which will maintain inflation the most in the coming years. The projected development of wages and salaries will push service inflation to around 2.6% in 2023 and 2024.

High prices and rising interest rates will gradually reduce demand, and price pressures will ease. Inflation will slow to 3.2% in 2023 and further to 1.8% by 2024.

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



Sources: Statistics Finland, MoF

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Table 13. Price indices

	2019	2020	2021	2022**	2023**	2024**
	change, %					
Export prices ¹	-0.2	-4.1	9.7	18.7	2.4	0.6
Import prices ¹	0.4	-5.1	9.5	20.8	2.5	0.5
Consumer price index	1.0	0.3	2.2	6.5	3.2	1.8
Harmonised index of consumer prices	1.1	0.4	2.1	6.7	3.4	1.9
Basic price index for domestic supply, including taxes	1.0	-3.3	9.0	20.5	4.5	2.3
Building cost index	1.0	-0.2	5.4	8.6	3.3	2.3

¹ As calculated in the National Accounts

2 General government finances

2.1 General government

The large imbalance in general government finances caused by the COVID-19 pandemic has been reduced by the strong economic and employment growth. Economic growth will slow this year, but employment growth will remain strong and general government finances will improve, boosted by the strong growth of tax revenue. The reduction in the deficit will also be supported by a decrease in the support measures due to the COVID-19 pandemic.

Economic growth will slow significantly next year, and the deficit will again start to increase. The many preparatory measures taken in response to Russia's war of aggression will also weaken general government finances in the years to come. The projected subdued economic growth will not be sufficient to rectify the imbalance in general government finances, and the deficit will remain large in the near future.

General government debt in ratio to GDP rose to a high level due to the COVID-19 pandemic and has not recovered to the pre-crisis level. However, the increase in the debt ratio was temporarily reversed last year. Particularly favourable nominal GDP growth is contributing to the temporary decrease in the government debt ratio. As the combined deficit of central government, local government and wellbeing services counties remains substantial, the debt ratio will start to increase again starting from next year. There is a longer-term structural imbalance between general government expenditure and revenue due to factors including population ageing and, consequently, general government finances are not on a sustainable foundation.

Central government finances will be strengthened this year by reductions in COVID-19 support measures and next year by the ending of the temporary measures of the government term. Preparedness-related measures are reflected particularly in the budgetary position of central government. The fiscal stance is discussed in more detail in the box on page 64. The deficit will grow starting from next year as tax revenue growth slows and, later, also as a result of the procurement

of fighter aircraft¹. Temporary measures will also be implemented next year to support the purchasing power of citizens in response to the exceptionally rapid rise in consumer prices, as well as measures aimed at mitigating the impacts of high electricity prices. The central government's debt servicing costs will also start to grow during the outlook period.

From next year onwards, the structure of Finland's general government will change when responsibility for the organisation of health, social and rescue services is transferred from the municipalities to the wellbeing services counties. This will alleviate the municipalities' structural expenditure pressures due to population ageing but, even so, local government finances will remain in deficit in the pressure projection. Initially, the wellbeing services counties will be in deficit. The deficit is due, among other things, to the high level of investments.

The surplus of earnings-related pension funds will be just over 1% in the next few years. Pension expenditure will continue to increase, but contributions, on the other hand, will again grow strongly this year, and rising interest rates will also increase growth of the pension funds' property income. The financial position of other social security funds will be strengthened during the outlook period by the improvement of the unemployment situation but, at the same time, pensions and social benefits will grow particularly sharply next year as inflation affects the cost-of-living index increases of the benefits. Social security funds will be in a slight surplus during the outlook period.

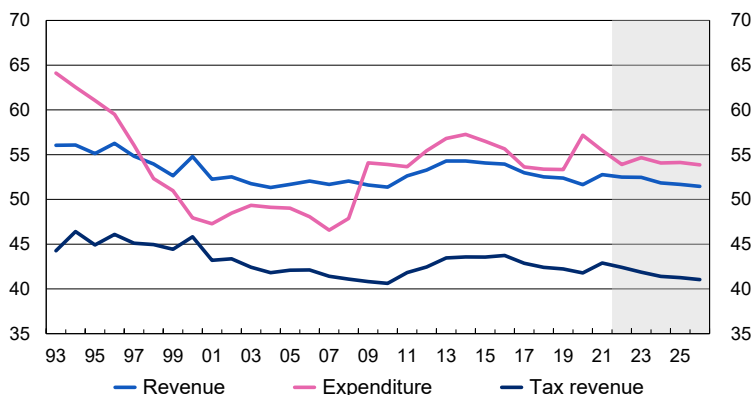
The most significant risks to general government finances are related to general economic development. Russia's invasion of Ukraine and the impacts of the resulting price pressures may be reflected in general government finances through general economic development, the preparations required by the changed situation and compensation paid out to citizens. Potential new waves of the COVID-19 pandemic and the accumulated care backlog may also have an adverse impact on general government finances. At the same time, however, significant appropriations were budgeted for various purposes related to the COVID-19 pandemic. Not all of these appropriations will necessarily be used, which may improve general government finances this year in particular. The current

¹ The forecast assumes that the new aircraft will be delivered to Finland from 2025 onwards. In the national accounts, the fighter project will be recognised in the budgetary position on an accrual basis

parliamentary term will end next year, and the forecast for general government finances beyond the current parliamentary term is based on the assumption of unchanged policy . Decisions made by the next government may move general government finances in either direction.

General government contingent liabilities and especially the rapid rise in guarantees will pose a risk for general government finances. Concentration of the guarantee liabilities in a small number of sectors and enterprises is increasing the risks arising from the liabilities. Extensive realisation of the liabilities would lead to higher public spending and speed up the increase in the debt-to-GDP ratio. Furthermore, the higher the debt ratio accumulated during low interest rates, the faster the increase in debt servicing costs arising from higher interest rates over the longer term.

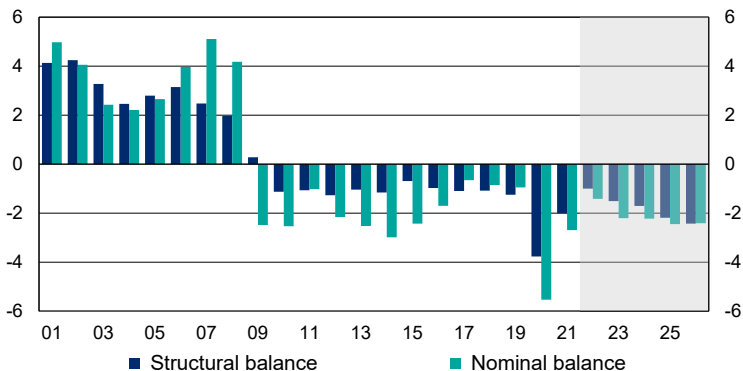
General government revenue, tax revenue and expenditure
relative to GDP, %



Sources: Statistics Finland, MoF

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General government nominal and structural balance
relative to GDP, %



Based on the European Commission's production function approach

Sources: Statistics Finland, MoF

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Table 14. General government finances¹

	2019	2020	2021	2022**	2023**	2024**
	EUR billion					
Current taxes	38.4	38.0	42.0	45.0	45.0	46.6
Taxes on production and imports	33.6	33.1	34.7	36.3	37.3	37.7
Social security contributions	28.6	27.6	30.3	31.8	33.4	34.3
Taxes and contributions, total ²	101.3	99.4	107.9	114.0	116.6	119.5
Other revenue ³	25.1	24.3	25.6	28.0	30.4	31.1
of which interest receipts	1.7	1.4	1.4	1.8	2.1	2.3
Total revenue	125.7	122.9	132.7	141.2	146.1	149.6
Consumption expenditure	55.6	57.8	61.4	64.9	67.0	69.2
Subsidies	2.6	4.4	4.0	3.1	2.6	2.8
Social security benefits and allowances	43.8	46.4	46.9	47.7	51.2	52.5
Other current transfers	5.8	6.6	6.9	6.8	6.7	6.9
Subsidies and current transfers, total	52.1	57.4	57.7	57.6	60.5	62.2
Capital expenditure ⁴	10.9	12.1	11.7	13.2	14.0	13.5
Other expenditure	9.3	8.8	8.6	9.3	10.8	11.2
of which interest expenses	2.1	1.7	1.3	1.6	2.1	2.4
Total expenditure	127.9	136.1	139.5	145.0	152.3	156.0
Net lending (+) / net borrowing (-)	-2.3	-13.2	-6.8	-3.8	-6.1	-6.4
Central government	-2.6	-13.1	-8.2	-6.2	-8.3	-8.4
Local government ⁵	-3.0	-0.1	-0.4	-1.1	-1.1	-1.2
Wellbeing services counties					-0.7	-0.8
Employment pension schemes	2.7	0.3	2.1	3.7	3.6	3.7
Other social security funds	0.6	-0.2	-0.2	-0.2	0.4	0.2
Primary balance ⁶	-0.2	-11.5	-5.4	-2.2	-4.1	-4.0

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 expenses⁵ Excl. wellbeing services county administration as of 2023⁶ 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	41.8	42.9	42.4	41.9	41.4
General government expenditure ¹	53.3	57.2	55.5	53.9	54.7	54.1
Net lending	-0.9	-5.5	-2.7	-1.4	-2.2	-2.2
Central government	-1.1	-5.5	-3.3	-2.3	-3.0	-2.9
Local government ²	-1.3	-0.0	-0.2	-0.4	-0.4	-0.4
Wellbeing services counties					-0.2	-0.3
Employment pension institutions	1.1	0.1	0.8	1.4	1.3	1.3
Other social security funds	0.3	-0.1	-0.1	-0.1	0.1	0.1
Primary balance ³	-0.1	-4.8	-2.2	-0.8	-1.5	-1.4
General government debt	64.9	74.8	72.3	71.2	72.7	74.1
Central government debt	44.3	52.5	51.2	50.8	52.0	53.1
General government employment, 1,000 persons	653	661	692	696	696	695
Central government	138	143	146	150	150	150
Local government ²	502	505	533	534	283	282
Wellbeing services counties					250	250
Social security funds	13	13	13	13	13	13

¹ EU-harmonized definition

² Excl. wellbeing services county administration as of 2023

³ Net lending excluding gross interest expenses

Table 16. Fiscal balance and debt ratios in some EU economies

	2020	2021	2022**	2020	2021	2022**
	Fiscal balance			Debt		
	relative to GDP, %					
*Finland	-5.5	-2.7	-1.4	74.8	72.3	71.2
Finland	-5.5	-2.6	-2.2	69.0	65.8	65.9
United Kingdom	-12.8	-8.3	-3.9	102.5	102.8	100.2
Sweden	-2.7	-0.2	-0.5	39.6	36.7	33.8
Denmark	-0.2	2.3	0.9	42.1	36.7	34.9
Ireland	-5.1	-1.9	-0.5	58.4	56.0	50.3
Spain	-10.3	-6.9	-4.9	120.0	118.4	115.1
The Neatherlands	-3.7	-2.5	-2.7	54.3	52.1	51.4
Luxembourg	-3.4	0.9	-0.1	24.8	24.4	24.7
Portugal	-5.8	-2.8	-1.9	135.2	127.4	119.9
Austria	-8.0	-5.9	-3.1	83.3	82.8	80.0
Germany	-4.3	-3.7	-2.5	68.7	69.3	66.4
France	-8.9	-6.5	-4.6	114.6	112.9	111.2
Belgium	-9.0	-5.5	-5.0	112.8	108.2	107.5
Italy	-9.6	-7.2	-5.5	155.3	150.8	147.9
Greece	-10.2	-7.4	-4.3	206.3	193.3	185.7

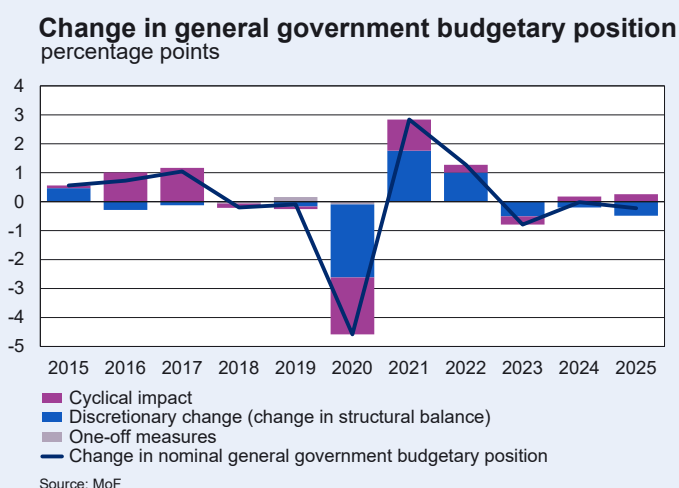
Sources: EU Commission Spring Forecast 2022; *Finland: Ministry of Finance, Autumn 2022

Fiscal stance

Expressed by the change in the structural balance (budget balance corrected for the impact of the economic cycle), the fiscal stance will turn from tightening to slightly stimulating next year. Expenditure will be temporarily increased by preparedness-related expenditure arising from Russia's invasion of Ukraine as well as measures to support citizens' purchasing power and compensate for the high price of electricity. At the same time, however, fiscal policy will be automatically tightened by the end of the temporary measures implemented in response to the COVID-19 pandemic and the temporary measures stipulated by the Government Programme for the years 2020–2022.

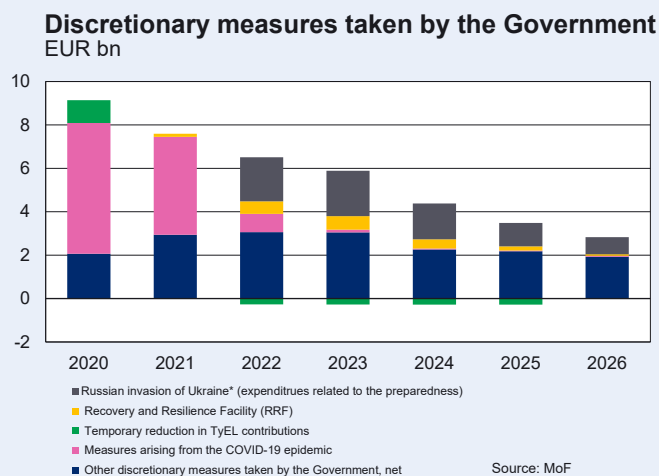
Comparing the structural balance with the spring of 2019, before the COVID-19 pandemic, the Government Programme and Russia's war of aggression, the stance appears slightly stimulating too.

After next year, i.e. during the period 2024–2026, the structural balance will weaken due to factors including the growth of age-related expenditure arising from the ageing of the population. The economic cycle is not projected to provide much support for improving the general government budgetary position. The period in question falls in the term of the next government, and the projections do not include any new potential decisions that affect general government finances.



The figure below illustrates the cumulative size of the measures introduced by the Government that impact general government revenue and expenditure each budget year. The Technical General Government Fiscal Plan of spring 2019 is used

as the baseline. Measures related to COVID-19 impacting the budgetary position recognised in the national accounts¹ at the general government level totalled around EUR 11½ billion, with most of these being allocated to 2020 and 2021.



Starting from 2022, the level of discretionary measures is increased by measures associated with preparedness related to Russia's war of aggression, which amount to approximately EUR 7.6 billion in total. Most of these expenditures are allocated to 2022 and 2023.

In the longer term, the combined effect of all of the measures on the general government budgetary position is approximately EUR 3 billion higher than before the current parliamentary term.

According to current estimates, Finland will receive around EUR 2.1 billion in grants from the Recovery and Resilience Facility (RRF). RRF will not have any impact on the general government budgetary position as the assumption in the forecast is that revenue matches the expenditure. The assumption is based on the Eurostat² guidance note on the statistical recording of the RRF.

1 There are measures impacting general government finances in which the timing cannot be directly derived from annual budgeted revenue and expenditure, as multiannual appropriations can also be used after the budget year. This particularly applies to 2021 and 2022, as a significant amount of budgeted appropriations were carried over from 2020 and 2021 to the subsequent years. The use of deferrable appropriations and its estimated impact on the budgetary position recognised in the national accounts have been taken into account in the forecast for general government finances.

2 Section 27 at <https://ec.europa.eu/eurostat/documents/1015035/12618762/GFS-guidance-note-statistical-recording-recovery-resilience-facility.pdf/ae773e09-1537-8c13-c71c-56d2e7d6958a?t=1633595971082>

2.1.1 General government debt

Last year, the general government debt ratio contracted by approximately 2.5 percentage points to 72.3% of GDP. The debt totalled EUR 181.7 billion at the end of 2021. Although the amount of debt is increasing, the debt ratio will contract slightly this year. The debt ratio will turn to growth in 2023 and is projected to amount to 76 % in 2026. There is a risk of general government debt being higher in 2022-2024 if the financing granted in the third supplementary budget to companies operating in the electricity market is paid out directly from the central government rather than in the form of guarantees.

A methodological change was made to the general government debt statistics in summer 2022, which increased the recorded amount of debt starting from the year 2000. The effect of the change at the level of 2021 was approximately six percentage points, or EUR 15 billion. The change concerned interest rate subsidy loans for social housing production. The change in methodology is described in more detail in the box on page 71.

Factors affecting the change in the debt ratio are itemised in Table 17. In the next few years, the debt ratio will be increased by a growing primary deficit in central and local government finances as well as by interest expenditure. At the same time, nominal economic growth will reduce the debt ratio. This year, in particular, rapid inflation also increases nominal GDP, which reduces the debt ratio. The impact of growth will be dampened in the subsequent years while the primary deficit and interest expenditure increase. The debt ratio will consequently start to increase faster.

Other factors illustrate the expenditure and revenue that do not impact the deficit recognised in the national accounts (stock-flow adjustment). In 2021, the debt ratio contracted more than would have been required for the deficit. Borrowing was reduced by factors including a decrease in central government cash assets. The financing of the fighter aircraft project will add to the borrowing needs from this year onwards. The impact on deficit of the fighter aircraft procurements will not be seen until the estimated commencement of the deliveries in 2025. The growth of the amount of interest rate subsidy loans will increase debt by approximately EUR 1.4 billion in 2023 and by about EUR 1 billion in 2024–2026.

In addition to on-budget debt, a number of other items are also included in general government debt. For example, central government debt includes the debts of a number of off-budget units and companies, interest rate subsidy loans granted

for rental and right-of-occupancy dwellings (see box) as well as the collateral on the derivative contracts used in the management of the central government debt portfolio. Local government debt also includes the debt of many municipality-owned companies and an amount of debt corresponding to the interest rate subsidy loans related to municipality-owned rental housing companies. The debt of the social security funds comprises the debts of the Employment Fund and the cash collateral on the derivatives of pension providers.

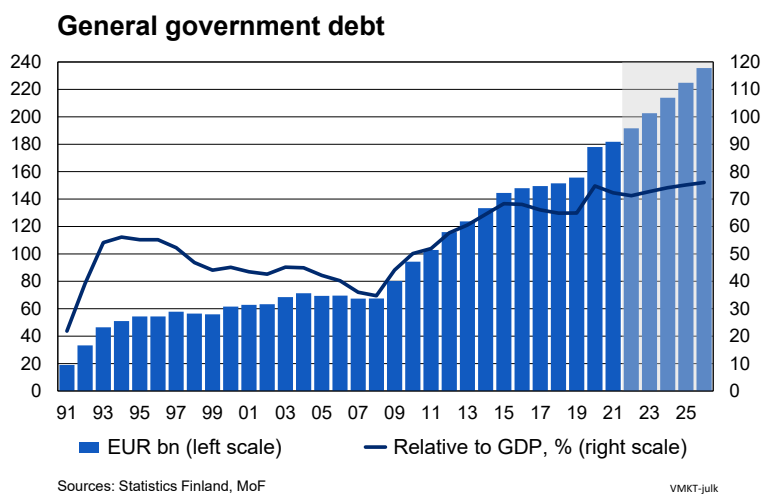


Table 17. Change in general government debt ratio and related factors

	2020	2021	2022**	2023**	2024**	2025**	2026**
Debt ratio, relative to GDP, %	74.8	72.3	71.2	72.7	74.1	75.2	76.0
Change in debt ratio	9.9	-2.5	-1.1	1.5	1.4	1.0	0.9
Factors impacting change in debt ratio							
Primary budgetary position (excluding employment pension funds)	4.9	3.0	2.2	2.7	2.7	3.0	2.9
Interest expenditure	0.7	0.5	0.6	0.7	0.8	0.9	1.0
Other factors ¹	3.7	-2.0	0.8	0.5	0.4	-0.2	-0.4
Change in GDP	0.5	-4.0	-4.7	-2.5	-2.5	-2.6	-2.6
Surplus of employment pension funds	0.1	0.8	1.4	1.3	1.3	1.4	1.5

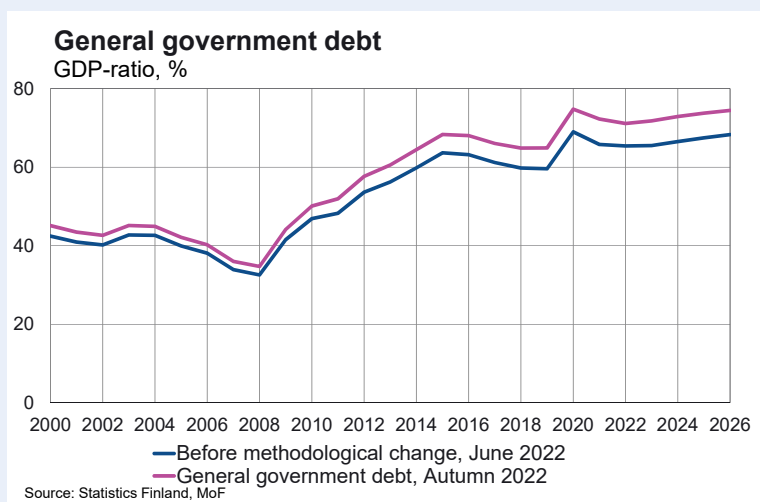
¹ Includes privatization proceeds, lending and factors related to the valuation and timing of revenue and expenditure.

Plus indicates increasing effect on debt ratio, minus a lowering effect on debt ratio."

General government debt increased significantly due to a change in methodology

The general government debt ratio increased by about 6 percentage points (approximately EUR 15 billion) from 66% to roughly 72% at the level of 2021 due to Statistics Finland implementing a change in methodology pertaining to the compilation of statistics concerning ARA interest subsidy loans granted for social housing production. The change was also retrospectively applied to time series data on debt dating back to 2000.

Figure 1. General government debt before and after the change in methodology



The change was related to the interest subsidy loan system for rental and right-of-occupancy dwellings. Under the system, the government grants an interest rate subsidy and a guarantee to the rental housing developer, and the developer secures loans from financial institutions. Statistics Finland reviewed the classification in connection with the regular examination related to the EU reporting of information on deficits and debt. As a result of the review, Statistics Finland decided to start recording the interest subsidy loans on general government accounts due to the restrictions applied to the renting of the subsidised dwellings. The assets and liabilities of general government increased by an equal amount as a result of the change in methodology. Interest expenses and interest income also increased by an equal amount. Among the subsectors of general government, the loans in question are allocated to central government and local government. The loans of municipally owned rental housing companies are allocated to local government and the loans of other non-profit institutions are allocated to central government.

Due to this change in methodology, changes in the loan portfolio under the interest subsidy system will influence general government debt going forward. Over the past few years, the total amount of interest subsidy loans has grown by approximately EUR 1 billion per year. In the 2023–2026 forecast of the Ministry of Finance’s Economics Department, the growth of the amount of interest subsidy loans is projected to increase general government debt by about EUR 1.4 billion in 2023 and approximately EUR 1 billion per year thereafter. These estimates are based on anticipated authorisations to grant interest rate subsidies and the amount of maturing interest subsidy loans.

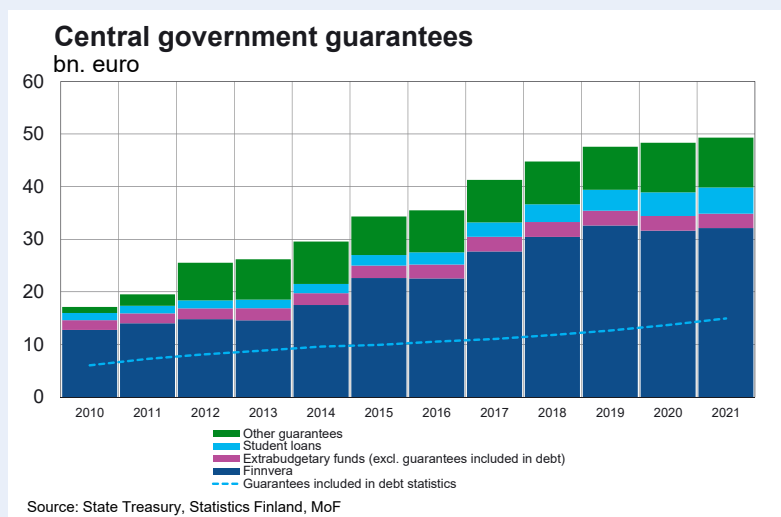
The change in methodology underscores the significance of contingent liabilities to general government finances. The interest subsidy loan system has been a significant policy programme for regulating the housing market, by which the central government has supported the construction of social housing in the form of rental dwellings and right-of-occupancy dwellings. The subsidies have not had much effect on general government expenditures or debt during low interest rates. Nevertheless, the total amount of interest subsidy loans has been substantial (EUR 15 billion in 2021) and it has already previously constituted a significant risk to general government finances that could materialise if interest rates were to rise. The liabilities associated with the system were previously reported in connection with state guarantees, for example. The change in the statistical methodology improves the visibility of the risks related to the system.

Contingent liabilities can materialise

The increase in the debt ratio related to interest subsidy loans was due to a change in statistical classification, with no actual expenses arising from it. As interest rates rise, interest subsidy expenditure may also begin to increase, with guarantee losses being a further risk. However, the system is not the only contingent liability that burdens general government finances that has not been visible in the general government deficit or debt statistics. The Ministry of Finance examines these liabilities in its overview of central government risks and liabilities, which is published annually.

The central government and municipalities have a significant amount of guarantees, with those related to interest subsidy loans representing only part of the total. In particular, liabilities related to export financing have increased substantially in the past few years. The total amount of guarantees related to export financing is EUR 32 billion. As regards housing production, the central government also has guarantees and interest subsidy loans relating to owner-occupied dwellings of private individuals. At the end of 2021, central government guarantees totalled EUR 64 billion. Municipalities’ guarantees amounted to EUR 32 billion.

Figure 2. Central government guarantees, EUR billion Source: State Treasury and Ministry of Finance



There have been two major unexpected events during the past couple of years, namely the COVID-19 pandemic and the war in Europe, along with the rapid escalation of tensions in international relations. Both of these events have also had an impact on the central government's contingent liabilities. State-owned enterprises have needed financial support and capitalisation (Finnair, Finavia). The difficulties of Uniper, a subsidiary of the majority state-owned enterprise Fortum, may also cause problems through a reduction in the central government's dividend income, for example.

Finnvera has had to recognise significant loss provisions on its export guarantees. These loss provisions already amount to nearly EUR 1.5 billion. The provisions have not materialised to date. Nevertheless, the loss provisions have resulted in the depletion of Finnvera's buffer reserves, and the central government has transferred funds of EUR 400 million to the State Guarantee Fund. A significant proportion of Finnvera's guarantees are related to the shipping industry, which has been particularly hard-hit by the pandemic and suffers from continued uncertainty.

During the COVID-19 pandemic, commitments have also been made to new liabilities to support business activities. These have included guarantees and various types of direct financial support, for example. Some of the costs incurred have arisen from implicit liabilities, where the central government has not had a legally binding obligation to support the activities in question but, in practice, it has been unavoidable for the central government to

support companies to ensure the continuation of air or sea traffic, for example. The central government has also provided significant financial support to municipalities.

Measures implemented by means of guarantees, interest subsidies or other contingent liabilities are easier to carry out because they do not result in expenditure when granted. Nevertheless, the liabilities involve a risk of subsequent losses. They also increase the vulnerability of general government finances to crises, as contingent liabilities tend to be realised in a recession or in other crises in which general government finances become drastically weaker. The development of liabilities should be evaluated regularly in the future, and efforts should be made to minimise the risks arising from them.

2.2 Central government

The central government deficit will decrease this year as support expenditure due to the COVID-19 pandemic declines and revenue rises sharply. The positive trend in employment is reflected particularly in taxes collected on wages. At the same time, investment expenditure will grow substantially this year.

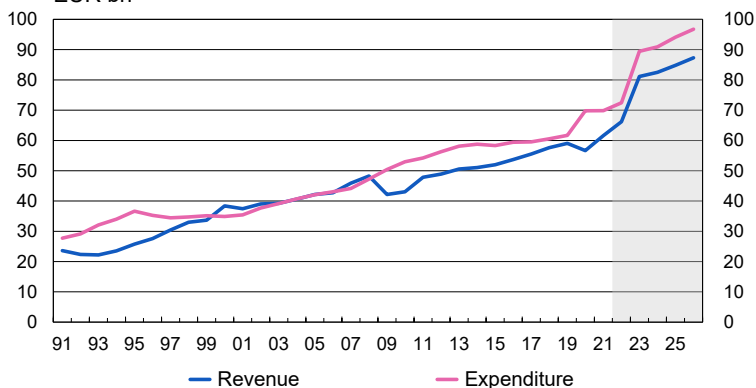
Russia's invasion of Ukraine will increase discretionary spending in 2022. During 2022, Prime Minister Marin's Government has adopted three supplementary budgets, whose expenditure increases are allocated to, among other things, national defence, reception of refugees, safeguarding security of supply, and cost support for companies in the tourism, restaurant and event sectors. In addition, the EU's Recovery and Resilience Facility (RRF) will increase expenditure, particularly in the period 2022–2023, with the related financing continuing until 2026. RRF financing will support the green transition, employment and skills, health and social services, and digitalisation. RRF spending will be channelled to investment grants, subsidies, public consumption and, to some degree, public investments. In 2022, the central government's RRF spending will amount to nearly EUR 500 million, of which more than EUR 110 million in new investment support will be allocated to the development of energy infrastructure and new energy technology. In the first stage, RRF spending increases will be covered from the current transfers granted by the EU. Finland will have to pay its RRF financing contribution in 2028–2058. Central government revenue will be boosted by the positive trend in employment.

Finland's target is to increase research and development expenditure to 4% of GDP by 2030. In 2023, central government expenditure will be increased by investments in accordance with the General Government Fiscal Plan to promote research, development and innovation (RDI). In addition, the funding of the Defence Forces has been increased, particularly for 2023, and immigration expenditure is expected to remain at a higher level than in previous years. Expenditure growth will be slowed by the elimination of spending prompted by the COVID-19 pandemic and the end of the future-oriented investments agreed upon in the early stages of the government term. As economic growth slows, the increase in tax revenue will decelerate. In 2023, the deficit will increase from the previous year and amount to approximately EUR 8.3 billion, or 3% of GDP.

Interest expenditure paid by the central government will rise to a level that exceeds previous expectations. In 2023, interest expenditure according to the accounts will exceed EUR 1.6 billion. Interest expenditure is projected to exceed EUR 2.2 billion in 2026. Rising interest expenditure comes out of the rest of public spending.

Economic growth in 2024 will not be sufficient to generate adequate revenue to cover expenditure, and the deficit is likely to be large. For 2024, expenditures will be increased by Border Guard investments, and funding for RDI activities will also be increased. The deficit is projected to further deteriorate in the medium-term outlook for 2025–2026. From 2025, investment expenditure will be increased by the expenditure on the Defence Forces' F35 fighter project as well as additional funding for RDI activities in 2025–2026. At the end of the outlook period, investments will also be increased by the procurement of Navy vessels. The amount of investment will increase in 2025 by as much as 29% compared to the preceding year.

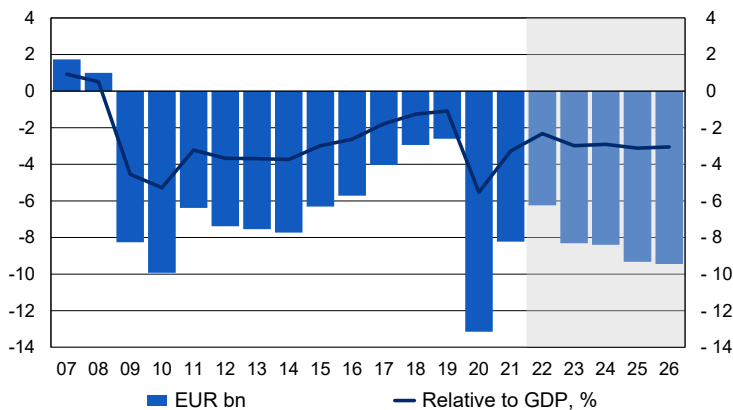
Central government revenue and expenditure EUR bn



Sources: Statistics Finland, MoF

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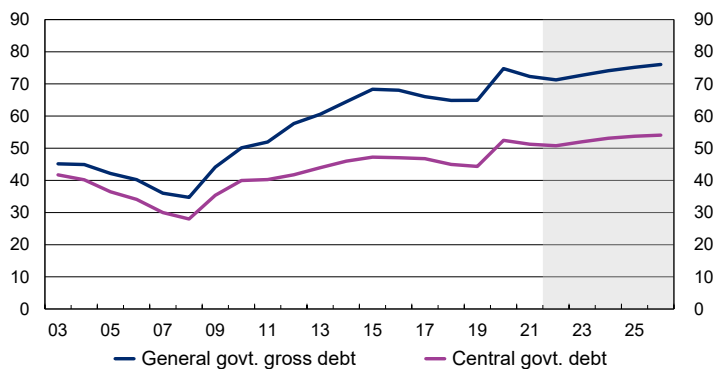
Central government financial balance



Sources: Statistics Finland, MoF

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General government debt relative to GDP, %



Sources: Statistics Finland, MoF

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Table 18. Central government¹

	2019	2020	2021	2022**	2023**	2024**
	EUR billion					
Current taxes	15.2	13.4	16.2	18.5	32.3	33.3
Taxes on production and imports	33.6	33.1	34.7	36.3	37.3	37.7
Social security contributions	0.0	0.0	0.0	0.0	0.0	0.0
Taxes and social security contributions, total ²	49.6	47.3	51.8	55.7	70.5	71.9
Other revenue ³	9.6	9.5	9.9	10.1	10.0	9.9
of which interest receipts	0.3	0.2	0.2	0.2	0.3	0.3
Total revenue	59.2	56.8	61.6	65.9	80.5	81.8
Consumption expenditure	14.4	15.3	15.9	17.7	18.3	18.5
Subsidies and current transfers, total	40.6	47.7	47.0	46.2	61.6	63.0
to general government	28.7	33.2	32.6	32.9	48.6	49.7
Interest expenses	1.9	1.6	1.2	1.4	1.7	2.0
Capital expenditure ⁴	4.9	5.4	5.8	6.8	7.2	6.7
Total expenditure	61.8	69.9	69.9	72.1	88.8	90.2
Net lending (+) / net borrowing (-)	-2.6	-13.1	-8.2	-6.2	-8.3	-8.4
Primary balance ⁵	-0.7	-11.6	-7.0	-4.9	-6.6	-6.4

¹ As calculated in the National Accounts

² Incl. capital taxes

³ Incl. capital transfers (excl. capital taxes) and consumption of fixed capital

⁴ Gross fixed capital formation and capital transfers

⁵ Net lending excluding gross interest expenses

The 2023 budget and central government spending limits

The Budget proposal for 2023 is based on the General Government Fiscal Plan published in April 2022 and the Programme of Prime Minister Marin's Government. On-budget expenditure will total about EUR 80.5 billion in 2023. Compared with the 2022 Budget, spending will be about EUR 15.6 billion higher.

The increase in spending is mainly due to the health and social services reform, which will change the structure of general government expenditure. The reform will increase the level of on-budget expenditure by approximately EUR 14 billion per year.¹ However, this figure does not take into account that approximately EUR 1.9 billion of the 2023 funding of the wellbeing services counties will be paid already in December 2022. In addition, the 2022 Budget did not include the measures decided upon in response to Russia's invasion of Ukraine. These amounts to approximately EUR 2 billion in both 2022 and 2023.

Taking into account the factors mentioned above, the increase in spending in 2023 is approximately EUR 2.5 billion compared to the 2022 Budget. The expenditure level for 2023 will rise, among other things, due to statutory and contractual index increases. In addition, interest expenditure is projected to grow by approximately EUR 1 billion compared to the 2022 budget due to the general increase in interest rates. On the other hand, on-budget expenditure will decrease in 2023, among other things, because expenditure related to the COVID-19 pandemic will diminish and because part of the temporary spending increases decided by the Government (including future-oriented investments) will come to an end.

Taking into account the change in the price level and the structural change caused by the social and health care reform, the appropriations of the administrative sectors (all other expenses excluding interest expenses) will increase by about half a percent compared to the 2022 Budget. However, the expenses budgeted for 2022 (including the first and second supplementary budgets) will decrease by more than 3.5% in this review, because it was decided on measures of about EUR 2 billion in the second supplementary budget of 2022 due the Russia's invasion of Ukraine.

¹ The estimate has been made according to a transfer calculation prepared on the basis of the cost level in 2022. In addition, with the reform, the central government's cost will increase fully by the increases due to the need for social and health care services and the index increase. These increases will increase government spending by approximately EUR 750 million in 2023. In the past, about a quarter of the increases has been compensated to the municipalities in accordance with the central government transfer percentage.

The spending limits for 2023 amount to approximately EUR 69.3 billion, of which about EUR 380 million will be set aside as an unallocated reserve after the 2023 Budget proposal. In the 2023 spending limits, a total of EUR 100 million has also been set aside for supplementary budgets.

The budget proposal includes a total of EUR 2.1 billion in appropriations for 2023 for expenditure arising from Russia's invasion of Ukraine, similarly to 2022. The Government decided on most of these appropriations already in April 2022 in connection with the government spending limits discussion, making an exception to the spending limits for them. The expenditure under the exception clause will be covered as expenditure outside the spending limits. On that basis, total appropriations of approximately EUR 1.0 billion are proposed for the Ministry of Defence's administrative branch and the Border Guard. Approximately EUR 59 million is proposed to improve cyber security preparedness. An appropriation of approximately EUR 241 million is proposed for a package concerning security of supply, energy self-sufficiency and the green transition. Appropriations of about EUR 791 million are proposed for helping Ukrainians fleeing the war and promoting the integration of migrants. In addition, appropriations of EUR 30 million are proposed for aid to Ukraine.

Expenditure outside the spending limits

Expenditure that varies according to the economic cycle and automatic fiscal stabilisers – such as unemployment security, housing allowances, basic social assistance and pay security – are outside the central government spending limits. However, expenditure effects generated by changes in the criteria for these items are included within the spending limits. Debt interest payments, value added tax expenditure, financial investment expenditure and expenditure corresponding to technically transmitted payments by central government are also excluded from the spending limits.

Proposed expenditure outside the spending limits amount to approximately EUR 11.7 billion, which is EUR 0.4 billion less than in the 2022 budget. Expenditure outside the spending limits will decrease significantly due to two technical factors. Firstly, due to a structural change, expenditure of approximately EUR 700 million that was previously financed by revenue from gambling will be brought within the scope of the spending limits. Secondly, tax compensation to municipalities outside the spending limits will be decreased by about EUR 450 million due to funding transfers related to the health and social services reform.

Expenditure outside the spending limits will be significantly increased by the rising interest expenses on central government debt. Interest expenditure is projected to grow by approximately EUR 1 billion compared to the 2022 budget due to the general increase in interest rates. Among expenditure outside the

spending limits, expenditure related to the COVID-19 pandemic and financial investment expenditure will decline substantially.

The EU's Recovery and Resilience Facility

A total of EUR 574 million for the investments paid from the Recovery and Resilience Facility (RRF) of the EU will be budgeted for 2023. At the same time, a total of EUR 391 million in revenue is expected from RRF in 2023. The payments are based on the progress in national plans and will be carried out when it has been checked that the objectives set out in the plans have been implemented as described in them.

On-budget revenue

In 2023, on-budget revenue (excluding borrowing) is estimated to be about EUR 72.5 billion, with tax revenue accounting for about EUR 64.5 billion of the total. On-budget tax revenue will increase by 33% from the 2022 Budget. The strong growth is particularly attributable to the health and social services reform, which will lead to a significant increase in the central government's earned income tax revenue, capital gains tax revenue and corporate income tax revenue. Excluding the impact of the health and social services reform, tax revenue will increase by an estimated 5% from the previous year.

Tax criteria changes set out in the Budget proposal lowering taxation will reduce the accumulated cash balance by about EUR 1.7 billion in 2023. The most important of the reductions is the index adjustment made in the earned income tax criteria, which will reduce tax revenue by approximately EUR 0.6 billion. In addition, the reduction in earned income taxes connected to the health and social services reform will reduce tax revenue by approximately EUR 0.6 billion. At the same time, tax revenue will be increased, among other things, by the increase in excise taxes on tobacco and the elimination of tax subsidies for paraffinic diesel.

In addition, compared to the General Government Fiscal Plan in spring, some new tax criteria changes have been decided. The measures taken to support the purchasing power of households and compensate for the rising electricity price are estimated to reduce the central government's tax revenue by a total of approximately EUR 0.5 billion. In addition, compensating municipalities for the reduction of day care fees will reduce the central government's tax revenues by EUR 90 million.

Based on the updated macroeconomic forecast and accrual data, on-budget tax revenue was risen by about EUR 1.3 billion compared to the General Government Fiscal Plan in spring (estimate without the effect of new tax criteria changes). The change was particularly attributable to the revenue estimate for value-added tax rising by EUR 0.6 billion and the revenue estimate for corporate income tax rising by EUR 0.5 billion. The increase in the revenue estimate for value-added tax was primarily due to better-than-anticipated employment growth and the subsequent growth of private consumption. The increase in the revenue estimate for corporate income tax, in turn, was due to the more accurate data on taxes for 2021 as well as the better-than-anticipated trend in the operating surplus.

Other on-budget revenue will decline by approximately 14% in 2023 due to the projection of the central government's revenue from dividends and the sale of shares declining from the EUR 2.4 billion budgeted for 2022 to approximately EUR 1 billion. This decrease is entirely due to a reduction in the estimated revenue from the sale of shares, as no revenue from the sale of shares has been budgeted for 2023. Compared to the General Government Fiscal Plan published in spring, the central government's projection of revenue from dividends and the sale of shares will decline by EUR 0.4 billion for the aforementioned reason.

The budget deficit projection and updating the projection from the spring

The Budget proposal is about EUR 8 billion in deficit, which will be covered with additional borrowing. The deficit will increase by approximately EUR 1 billion compared to the 2022 Budget. Central government debt is estimated to total about EUR 156 billion at the end of 2023. With the third supplementary budget proposal for 2022, the debt estimate has increased by EUR 10 billion due to preparations for significant lending needs, but there is considerable uncertainty in the amount of loans granted by the central government to electricity companies and repaid by them in this exceptional situation.

The on-budget deficit in 2023 has increased by about EUR 0.6 billion compared to the General Government Fiscal Plan presented in spring 2022. Due to the factors discussed above, the revenue forecast is EUR 0.3 billion higher than what was anticipated in spring. At the same time, however, on-budget expenditure is about EUR 0.9 billion higher.

Factors affecting changes in on-budget balance compared with the General Government Fiscal Plan of spring 2022, EUR billion

	2023
Estimated balance, General Government Fiscal Plan of Spring 2022	-7.5
Revision of expenditure estimate	-0.9
New expenditure measures (net)	-0.5
Procurement of defence materiel	-0.3
Value-added tax expenditure	-0.1
Government aid to municipalities and joint municipal authorities	-0.4
Financing of wellbeing services counties	0.7
Contributions to the European Union	0.0
Change in debt interest payment estimate	-0.4
Unemployment security, housing allowance and pay security (excl. refugees from Ukraine)	0.0
Other changes in expenditure (net), including more accurate index adjustments	0.2
Revision of revenue estimate	0.3
New tax criteria changes (net)	-0.6
Changes to estimates of interest, dividend and sales of shares income	-0.4
Changes to the estimate of miscellaneous revenue	0.0
Other factors affecting projected revenue (including accrual data and new economic forecast)	1.3
Total change	-0.6
Balance projection, Budget proposal 2023	-8.0

Table 19. Forecasts for certain revenue and demand items impacting taxable income and the tax base

	2022	2023**	2024**	2025**	2026/2022**
	change, % per year				annual change, %
Taxable earned income and capital income	2.7	3.5	3.3	3.2	3.2
Wage and salary earnings and other income	4.8	3.3	3.3	3.4	3.6
Pensions and other social security benefits	1.6	7.0	3.5	3.1	3.6
Capital income	-7.2	-4.4	2.7	2.7	-0.7
Index of wage and salary earnings	2.6	3.5	3.0	3.0	3.0
Operating surplus	9.4	4.7	4.6	4.1	5.3
Value of household taxable consumption expenditure	8.4	4.2	2.5	3.5	3.4
VAT base	9.0	4.6	2.5	4.0	3.6
Petrol consumption	-3.2	-1.7	-3.7	-4.9	-3.9
Diesel consumption	-0.6	-0.9	-2.1	-2.7	-1.9
Electricity consumption	-1.5	3.3	0.8	0.9	0.8
Duty-paid alcohol consumption	-3.8	1.1	0.2	-0.7	-0.8
New passenger cars	-9.7	29.4	4.5	1.6	5.5
Consumer price index	6.5	3.2	1.8	1.9	3.1

Table 20. Impact of change in selected tax base items on tax revenue

Tax category	Tax base	Change	Change in tax revenue, EUR million
Taxes on earned income	Wage and salary earnings	1%	470, of which central govt. 139 and local govt. 221
	Pension incomes	1%	146, of which central govt. 38 and local govt. 94
Capital income tax	Investment income	1%	46
Corporate tax	Operating surplus	1%	55, of which central govt. 36 and local govt. 19
VAT	Value of private consumption	1%	141
Car tax	Sales of new cars	thousands	3
Energy tax	Electricity consumption ¹	1%	9
	Petrol consumption	1%	13
	Diesel consumption	1%	15
Duty on alcoholic beverages	Alcohol consumption	1%	15
Duty on cigarettes	Cigarette consumption	1%	10

¹ Excl. manufacturing industries, datacenters and greenhouses

Table 21. Central government on-budget revenue

	2021	2022**	2023**	2024**	2025**	2026**	2026/2022**
	provisional financial accounts	budget incl. supplementary budget					annual change, %
EUR billion							
Total tax revenue estimates	46.8	49.7	64.5	67.3	69.4	71.7	9.4
Income and wealth taxes	15.9	16.8	30.9	33.1	34.5	36.2	21.1
Taxes based on turnover	21.2	22.6	23.5	24.2	25.2	26.0	4.2
Excise duties	6.8	7.5	7.4	7.2	7.0	6.8	0.2
Other taxes	2.9	2.9	2.8	2.8	2.7	2.7	-1.4
Miscellaneous revenue	7.2	6.4	6.5	6.2	6.4	6.5	-1.9
Interest income and profit entered as income	2.4	2.6	1.3	1.3	1.3	1.3	-8.0
Total revenue estimates	56.4	58.9	72.5	74.9	77.3	79.6	7.4

Table 22. Impact of discretionary tax measures on general government tax revenue

	2021	2022	2023**	2024**	2025**	2026**
	EUR million					
Earned income taxes	-434	-612	-1347	-664	-584	-518
Average increase in municipal tax rate	60	0	0	0	0	0
Investment income tax	26	-18	-29	-7	5	0
Corporate tax	-100	33	14	7	28	201
Other direct taxes	-108	-107	-9	0	0	25
Value-added tax	44	-21	-0	1	0	0
Energy taxes	96	178	64	24	8	15
Other indirect taxes	93	62	62	45	0	0
Social security contributions	1375	-49	508	-172	11	-347

On-budget accounts and national accounts

As the definition of central government differs between on-budget accounts and national accounts, no direct conclusions on the central government budgetary position recognised in the national accounts can be made on the basis of the central government budgetary position.

Central government on-budget entities showed a deficit of EUR 9.6 billion in 2021. According to the national accounts, the central government deficit was EUR 8.2 billion, or around EUR 1.4 billion lower. The difference in 2021 between the national accounts and the Budget is mainly explained by an increase in deferrable appropriations, which are entered in the on-budget deficit for the budget year but in the national accounts only when the money is spent. The total of deferrable appropriations carried over to following years was around EUR 2.7 billion higher in 2021 than in the previous year. Other differences between entry practices, in turn, weakened the accounts in relation to the Budget.

This year, the budget balance is weaker than the budgetary position in the national accounts. The difference is due to the share of the funding of the wellbeing services counties for January 2023, which has been budgeted for 2022, not being recognised as an expense in the accounts until 2023. The difference between the

budget and the national accounts is increased by tax timing adjustments being higher than usual due to the health and social services reform. On the other hand, the budgetary balance will be improved by planned share disposals, which in turn do not affect revenue recognised in the national accounts.

In 2023, the deficit recognised in the national accounts will be close to the budget deficit. The budget will again be burdened by the financing of the fighter project, which will begin to be reflected in expenditure recognised in the national accounts starting from 2025. The national accounts in 2023 will be weakened by the funding of the wellbeing services counties for the early part of 2023, which is recognised in the budget in 2022. The deficit recognised in the national accounts in 2025–2026 will be substantially higher than the on-budget deficit as the financing of the fighter project starts to be reflected in expenditure recognised in the national accounts.

It is not always possible to make conclusions about the central government borrowing requirement on the basis of the on-budget deficit or the deficit recognised in the annual accounts. In 2021, central government borrowed an additional EUR 3.7 billion. On the basis of the on-budget deficit, central government should have borrowed a total of EUR 9.5 billion, which means that the borrowing was as much as EUR 5.8 billion lower than the on-budget deficit would have required, and EUR 4.4 billion lower than the deficit recognised in the national accounts would have required. Generally speaking, there are several reasons for the difference between the deficit and the movement in debt. The reasons why borrowing could be decreased in 2021 included central government reducing its cash reserves by EUR 2.5 billion. In addition, deferrable appropriations reduced the need for borrowing in relation to the budget deficit by EUR 2.7 billion. Due to a change in the compilation of statistics on general government debt, EDP debt will be affected by changes in the interest subsidy loan portfolio in the future.

There are several reasons for the difference between the central government budgetary position and the central government budgetary position recognised in the national accounts. The most important of these is the fact that the national accounts concept of central government is broader than the on-budget entities, which mainly comprise central government agencies. In addition to on-budget entities, the central government sector in the national accounts also includes, for example, government funds (excluding the State Pension Fund), universities

and their real estate companies, and Senate Properties. The decisions on the classification of public sector units are regularly reviewed. A list of all units of central government and, more broadly, general government can be found on the website of Statistics Finland.

In addition to classification, differences also arise because the criteria for recognising expenditure in the national accounts and in on-budget entities differ from each other. The national accounts are accrual based, whereas on-budget activities are based partly on the cash-basis principle. Due to the different recognition principles, deferrable appropriations in the Budget in particular result in differences between on-budget and national accounts expenditure. Deferrable appropriations are multi-year appropriations that are entered in the Budget for one year only. In the national accounts, deferrable appropriations are recognised on accrual basis according to their year of use in the same way as other expenditure. The net effect of deferrable appropriations can vary substantially from year to year. Additionally, in the national accounts, taxes, subsidies and EU contributions are translated into accrual-based items by means of timing adjustments. The differences arising from the timing adjustments can only be determined afterwards.

Such financial investments as loans granted and repaid by central government and disposals and acquisitions of equities that in the national accounts are primarily treated as financial transactions are also included as revenue and expenditure in the on-budget budgetary position. Financial transactions do not have any effect on the central government budgetary position recognised in the national accounts. Also recorded as financial transactions are derivatives, which the State Treasury has successfully used to achieve significant reductions in interest expenditure from the Budget. Because the downward effect of derivative instruments on interest expenditure is not taken into account in the national accounts, interest expenditure in the national accounts is clearly higher than on-budget interest expenditure.

Table 23. On-budget balance and central government net lending¹

	2020	2021	2022**	2023**	2024**
	EUR billion				
On-budget surplus (+) / deficit (-) ²	-17.4	-9.6	-7.7	-8.4	-8.4
Privatization proceeds (net proceeds from equity sales)	0.4	-0.2	-0.8	0.2	0.2
Financial investment, net	-0.4	-0.2	-0.3	0.1	-0.0
Revenue surplus in off-budget units	-0.2	-0.3	-0.3	-0.3	-0.3
Cash / accrual basis adjustment	0.8	0.3	2.0	1.2	1.6
Other adjustment items ³	3.6	1.8	0.9	-1.0	-1.4
Central government net lending (+) / borrowing (-)	-13.1	-8.2	-6.2	-8.3	-8.4

¹ In National Accounts terms.

² Incl. government debt servicing.

³ Incl. debt cancellations, profit on reinvested foreign direct investments, impact of the difference in the recording of deferrable budgetary appropriations, superdividends

2.3 Local government

Although the growth of local government consumption expenditure will slow in 2022 due to COVID-19 expenses declining year-on-year, the local government budgetary position will weaken to show a deficit in excess of EUR 1 billion (0.4% of GDP) due to the end of the increased corporate tax apportionment and support measures such as higher central government transfers to local government. Growth in consumption expenditure will be sustained in 2022 not only by the increase in the need for services but also by the reduction of the service and care backlog and the expansion of municipalities' duties in accordance with Prime Minister Marin's Government Programme, with related expenses increasing each year. Additional expenditure is also arising from the immigration of those fleeing the war in Ukraine. The Government is committed to compensating municipalities for related additional expenditure in, for example, education and integration.

The pay decision reached in the local government sector in summer 2022 applies to all local government employees. In addition to agreement increases linked to the general line, pay in the local government sector will be reformed through a

separate development programme in 2023–2027. According to the programme, local government sector pay will increase by a total of approximately 5.1% over five years in addition to agreement increases. Pay agreements in the municipal sector have a significant impact on the development of costs in local government, as personnel expenses are the largest cost item. There are also risks of further industrial action, with the care-worker unions having made threats to that effect.

In 2023, health, social and rescue services duties will be transferred to wellbeing services counties and the corresponding financing to central government¹. Municipal revenue and expenditure will nearly halve as a result of the reform. With the reform of health and social services, this unpredictable and rapidly growing expenditure will be transferred to the responsibility of wellbeing services counties. After the reform, the duties included in municipal finances (local government excluding wellbeing services counties) will be even more focused on early childhood education and general education, the combined need for which is declining due to the fall in the birth rate throughout the 2010s. In the projection, the decline in the need for services has been slightly dampened as usual, as there are limited opportunities for adjustments to the school network in small municipalities. The number of children in early childhood education and care is also influenced by the participation rate, which has been increasing in the past few years.

In 2023, the health and social services reform will take effect and the parliamentary term will come to an end. Many of the government's temporary measures will end and certain items will be eliminated from local government finances, including COVID-19 grants as well as quality and equality projects in early childhood education and care, basic education and upper secondary education.

An estimated total of EUR 1.2 billion in investments will be transferred from municipal finances to the wellbeing services counties. Nevertheless, investment pressures in municipal finances will remain substantial because of the age of the building stock and migration, among other factors. Climate change mitigation and preparing for the impacts of climate change also require municipalities to adopt

¹ In the forecast, Helsinki's health, social and rescue services have been included in the wellbeing services counties subsector.

new operating practices and invest in the green transition, for example. However, it is possible that investments will be postponed due to the uncertain economic outlook, resource bottlenecks and increasing costs.

The deficit in municipal finances is projected to remain at approximately 0.4% of GDP in 2023. The structural imbalance between revenue and expenditure in municipal finances will increase the nominal debt of the municipal sector until 2023. Approximately EUR 5.1 billion in debt will be transferred from municipal finances to the wellbeing services counties in 2023 as a result of the health and social services reform. Municipal finances will be over EUR 1 billion in deficit in the pressure projection even after the reform of health and social services in 2023. Although the spending pressures arising from the ageing of the population will ease as a result of the reform of health and social services, there will still be a slightly growing imbalance between revenue and expenditure. The deficit in municipal finances will grow to 0.6% of GDP towards the end of the outlook period in 2026. However, the growth of the deficit will level off, which will be reflected in slower growth of the debt ratio compared to the average rate seen over the past decade.

Table 24. Local government excl. wellbeing services counties as of 2023¹

	2019	2020	2021	2022**	2023**	2024**
	EUR billion					
Taxes and social security contributions	23.2	24.6	25.8	26.5	12.7	13.2
of which municipal tax	19.4	20.5	20.8	21.7	8.6	9.2
corporate tax	1.9	2.2	3.0	2.7	2.0	1.9
real estate tax	1.9	2.0	2.0	2.1	2.1	2.1
Other revenue ²	20.1	23.7	23.9	24.7	14.5	14.9
of which interest receipts	0.3	0.3	0.3	0.3	0.3	0.3
transfers from central government	14.4	17.7	17.6	18.1	8.1	8.3
Total revenue	43.2	48.3	49.7	51.2	27.2	28.1
Consumption expenditure	37.5	38.8	41.4	43.0	20.5	21.3
of which compensation of employees	22.1	22.4	23.4	23.9	12.6	13.0
Income transfers	2.6	2.7	2.7	2.8	2.1	2.2
of which social security benefits and allowances	0.8	0.7	0.7	0.7	0.0	0.0
subsidies and other transfers	1.6	1.9	1.9	1.9	1.8	1.8
interest expenses	0.2	0.1	0.1	0.2	0.3	0.3
Capital expenditure ³	6.2	6.9	6.1	6.5	5.7	5.8
Total expenditure	46.3	48.4	50.2	52.3	28.3	29.3
Net lending (+) / net borrowing (-)	-3.0	-0.1	-0.4	-1.1	-1.1	-1.2
Primary balance ⁴	-2.8	0.0	-0.3	-0.9	-0.9	-0.9

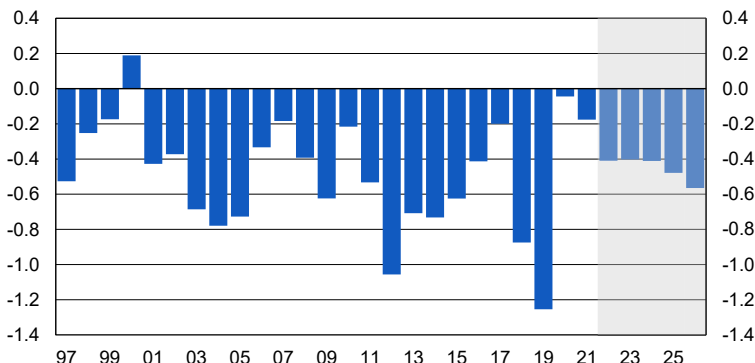
¹ As calculated in the National Accounts

² Incl. capital transfers and consumption of fixed capital

³ Gross capital formation and capital transfers

⁴ Net lending excluding gross interest expenses

Local government financial balance relative to GDP, %

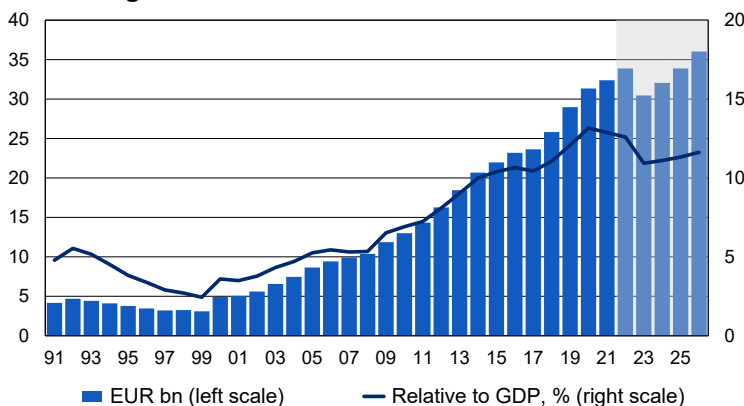


Excl. wellbeing services county administration as of 2023

Sources: Statistics Finland, MoF

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Local government debt



Excl. wellbeing services county administration as of 2023

Sources: Statistics Finland, MoF

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2.4 Wellbeing services counties

The wellbeing services counties will start their actual operations at the beginning of 2023. Starting from that time, they will be treated as a separate subsector in the projection for general government finances. In the projection, the wellbeing services counties comprise the activities of the new wellbeing services counties (established as part of the health and social services reform), the Hospital District of Helsinki and Uusimaa (HUS), and the health, social and rescue services of the City of Helsinki.

Initially, the wellbeing services counties will be slightly in deficit. The deficit will be about 0.2% of GDP and is mainly due to the high level of health and social services investments, which will decrease slightly in the subsequent years. The budgetary

position of the sector will be weakened by the rapid rise in costs, particularly personnel costs. In the projection for the wellbeing services counties, it is assumed that the earnings trend of the sector will be in line with the pay increases agreed at the beginning of June and the five-year pay programme, although no agreements have been concluded with the care-worker unions.

Most of the financing for the wellbeing services counties will come from central government. Central government funding will increase according to the estimated need for services plus 0.2 percentage points. From 2025 onwards, only 80% of the increase in the need for services will be taken into account. Funding will also change in accordance with the county-specific price index and changes in duties. The wellbeing services counties will also receive a small amount of fee income from customers. In 2023, the sector will receive EUR 27.4 billion in revenue and 90% of this total will come from central government.

Expenditure trends of the wellbeing services counties are based on estimated increases in service needs and anticipated price trends. Investment estimates are based on budget data and separate surveys concerning investments. The cost of providing health and social services accounts for most of the expenditure of the wellbeing services counties. Personnel expenses or costs of purchasing goods and services will account for EUR 26.1 billion of the total in 2023.

Initially, the wellbeing services counties will also incur change-related 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. The scale of the change costs involves uncertainties. In addition, pay increases for the care-worker unions involve a cost risk as the negotiations are still under way.

Table 25. Welfare services counties

	2023**	2024**
	EUR billion	
Total revenue	27.4	28.4
Total expenditure	28.1	29.1
Net lending (+) / net borrowing (-)	-0.7	-0.8
Debt	5.8	6.6

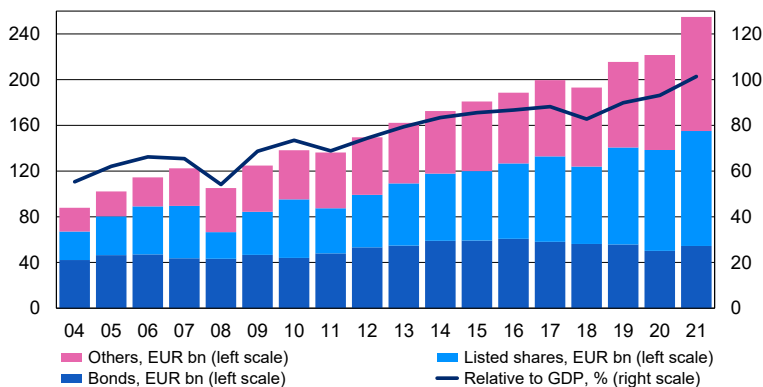
2.5 Social security funds

2.5.1 Employment pension schemes

Last year, the surplus of employment pension schemes returned close to the pre-pandemic level, amounting to 0.8% of GDP. This year, the surplus of employment pension schemes will increase to 1.4% of GDP. The surplus will be strengthened by the temporary increase in the pension contribution of private sector employers for the period 2022–2025. Growth in the pension funds’ property income has a considerable impact in particular. Earnings-related pension assets grew to EUR 256 billion at the end of 2021, but the amount decreased slightly in the first half of this year.

Earnings-related pension expenditure will grow sharply in 2023 as the rapid increase in prices affects the cost-of-living index adjustments for pensions. At the same time, the sector’s financial position will stop improving, although the rising interest rates will also increase property income. Property income received by employment pension schemes (interest and dividends) increased by 14% last year. Property income is projected to continue to grow rapidly this year as interest rates rise.

Investment portfolio of pension funds
all members



Sources: The Finnish Pension Alliance TELA, Statistics Finland, MoF

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Social security funds, financial balance relative to GDP, %

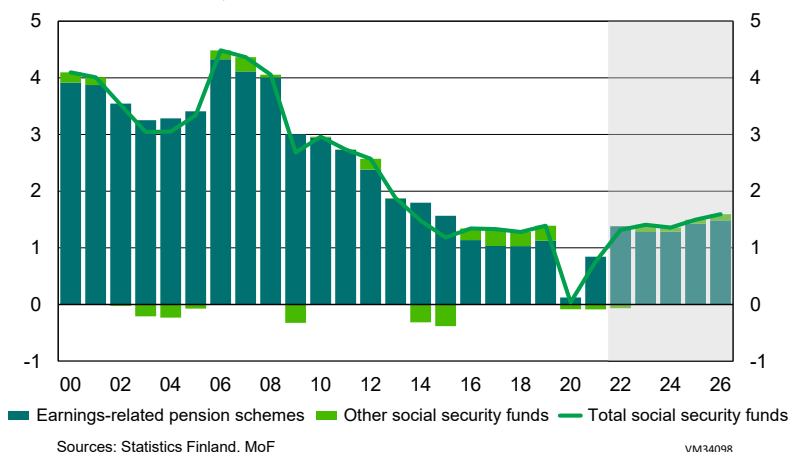


Table 26. Finances of social security funds¹

	2019	2020	2021	2022**	2023**	2024**
	EUR billion					
Investment income	4.3	3.5	4.0	5.4	6.7	7.3
Social security contributions	28.5	27.6	30.3	31.8	33.4	34.3
of which contributions paid by employers	17.8	16.7	18.8	19.9	20.9	21.4
contributions paid by insured	10.8	10.8	11.5	11.9	12.5	12.8
Transfer from general government	15.7	17.2	16.8	16.3	17.2	17.3
Other revenue	0.4	0.4	0.3	0.3	0.3	0.3
Total revenue	48.9	48.7	51.4	53.8	57.6	59.1
Consumption expenditure	3.8	3.8	4.1	4.2	4.2	4.3
Social security benefits and allowances	38.5	41.2	41.7	42.4	45.6	46.9
Other outlays	3.2	3.6	3.7	3.6	3.8	3.9
Total expenditure	45.5	48.6	49.5	50.2	53.6	55.1
Net lending (+) / net borrowing (-)	3.3	0.1	1.9	3.5	4.0	3.9
Earnings-related pension schemes	2.7	0.3	2.1	3.7	3.6	3.7
Other social security funds	0.6	-0.2	-0.2	-0.2	0.4	0.2
Primary balance ²	3.4	0.1	1.9	3.6	4.0	4.0

¹ As calculated in the National Accounts

² Net lending excluding gross interest expenses

Table 27. Social security contributions rates and pension indices

	2019	2020	2021	2022	2023**	2024**
Social insurance contributions ¹						
Employers						
Sickness insurance	0.77	1.34	1.53	1.34	1.58	1.48
Unemployment insurance	1.50	1.26	1.43	1.51	1.54	1.54
Earnings-related pension insurance	17.35	15.22	16.95	17.40	17.40	17.40
Local government pension insurance	21.17	20.78	20.60	20.34	20.34	20.34
Employees						
Sickness insurance	1.54	1.86	2.04	1.71	1.95	1.88
Unemployment insurance	1.50	1.25	1.40	1.50	1.50	1.50
Earnings-related pension insurance	7.05	7.45	7.45	7.45	7.45	7.45
Benefit recipients						
Sickness insurance	1.61	1.65	1.65	1.50	1.51	1.53
Pension indices						
Earnings-related index (over 65)	2585	2617	2631	2691	2864	2935
National pension index	1617	1633	1639	1674	1798	1837

¹ Annual averages. The contributions of employers and the unemployment and employment pension contributions of beneficiaries as percentages of wages and salaries. The figures are weighted averages.

2.5.2 Other social security funds

The other social security funds are the Social Insurance Institution of Finland, which is primarily responsible for basic security, and the Employment Fund, which is responsible for earnings-related unemployment security. This year, the other social security funds have a slight deficit of 0.1% in relation to GDP. The financial position of the other social security funds will turn to a surplus next year and remain close to balance for the remainder of the outlook period.

Increases in unemployment insurance contributions this year are boosting the sector's revenue. In addition, unemployment expenditure will decrease further year-on-year before turning to slight growth. The Employment Fund's cyclical buffer will nevertheless start to grow and, towards the end of the outlook period, there will be pressure to reduce contributions due to the upper boundary of the cyclical buffer being approached. The expenditure of the Social Insurance Institution of Finland

(Kela) will be increased this year by factors including infectious disease allowance, the amount of which is projected to remain at a high level even in the coming years. The growth of benefits is also accelerated by cost-of-living index increases being higher due to rapid inflation. Next year's expenditure will also be increased by financial support for electricity, the amount of which is tentatively estimated to be EUR 300 million. To compensate for rising prices, improvements have also been made to many other benefits in addition to the usual cost-of-living index increases

2.6 Long-term sustainability of general government finances

The ageing of the population has already increased pension expenditure over the past 10 years and is creating major pressures on the long-term sustainability of Finland's general government finances. An increase in older population is the main factor increasing the health and long-term care expenditure in the coming decades, and the current total tax rate will be inadequate to finance these increases in the future. At the same time, the working-age population, which pays the taxes needed to finance the public services and social security, is shrinking.

There is a long-term imbalance (sustainability gap) between general government revenue and expenditure. The sustainability gap calculation shows how much general government finances should be consolidated in the near future in order to ensure that the finances are in balance in the long-term. In other words, after the adjustment, there would no longer be any need to increase the tax rate, cut spending, introduce structural reforms consolidating general government finances or increase general government debt. However, the sustainability gap calculation does not address the question of how the general government debt ratio should be stabilised or set the timetable for this process. Furthermore, the harmful impacts of

the adjustment or positive impacts of structural reforms on economic growth are not taken into account¹.

The purpose of the sustainability gap calculations is to estimate how the ageing of the population impacts the outlook for general government finances in the coming decades. In addition to the ageing of the population, there are also many other factors that put further pressure on general government finances, which arise from such issues as preparations for the new, weaker security environment, climate change and the need to overhaul and repair public infrastructure, but which are not included in the calculation of the sustainability gap.

The Ministry of Finance estimates that the sustainability gap will be approximately 3% of GDP (some EUR 9 billion) at the 2026 level. The estimated level of the sustainability gap has remained more or less unchanged since last spring. The findings can be interpreted so that the ageing of the population poses a significant challenge to the sustainability of general government finances. The projected growth of the general government debt ratio also increases the risks to general government finances.

In the sustainability gap calculation, general government debt is not expected to converge to any specific level. Thus, the debt balance produced by the calculation may also be relatively high or low, depending on the level of the debt ratio at the time of the calculation and the estimated impact of the ageing of the population on public spending trends in the coming decades. For this reason, the debt sustainability of general government finances should also be examined in other ways. These methods include the reviews presented in the Ministry of Finance report on the sustainability of Finland's public finances².

1 As the sustainability gap (S2 indicator) does not take into account the potential adverse effects of direct adjustment measures on economic growth, it should not be used as the sole instrument to assess the required adjustment. There are other methods in which more consideration is given to the negative growth impacts of direct adjustment measures. Technically, the results given by the S2 indicator correspond to a situation in which the fiscal policy coefficient would be zero (the adjustment measures do not slow down economic growth). It is generally assumed that direct adjustment measures will slow down economic growth. At the same time, however, many of the structural reforms do not have such adverse effects and they can also strengthen the basis for economic growth.

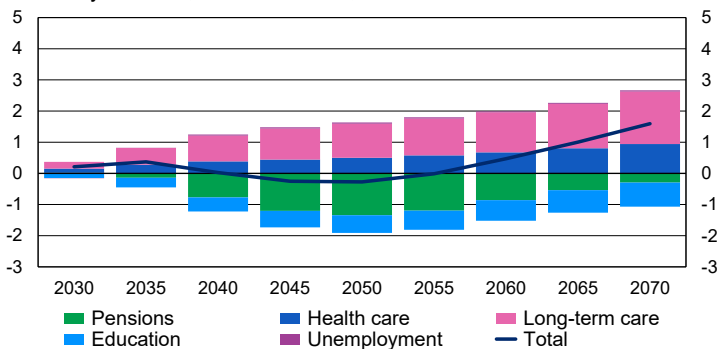
2 <https://julkaisut.valtioneuvosto.fi/handle/10024/162357> (in Finnish, with English abstract)

The Ministry of Finance estimate of the long-term sustainability of general government finances is based on the methods and calculation principles jointly agreed in the European Union Working Group on Ageing Populations and Sustainability (AWG). The sustainability gap calculation is a pressure calculation, not the most probable future scenario. The calculation is based on the assumption of unchanged policy, which means that it projects trends under current legislation and practices to the future with the help of population projections, spending decompositions by age groups, and estimates of long-term economic growth trends. Only the decisions whose impacts on general government finances can be estimated with sufficient accuracy are considered in the sustainability gap estimate. The methods used in the sustainability gap calculations are detailed on the Ministry of Finance website³.

The aim is to use realistic assumptions as a basis for the sustainability gap estimate. As any indicator, the estimate changes slightly as the data and forecasts used are updated. The table below presents key calculation assumptions used in the sustainability gap calculation and examines the sensitivity of the calculation to changes in the assumptions. The results of these sensitivity assessments are presented in more detail in the last chapter of the description of sustainability gap calculation methods referred to above. The sustainability gap calculation and its sensitivity assessments provide a useful and logical way to analyse the size of the challenge arising from the ageing of the population and how this challenge can be addressed.

3 <https://vm.fi/menetelmakuvaukset>

Change in age-related expenditure from year 2026, relative to GDP, %

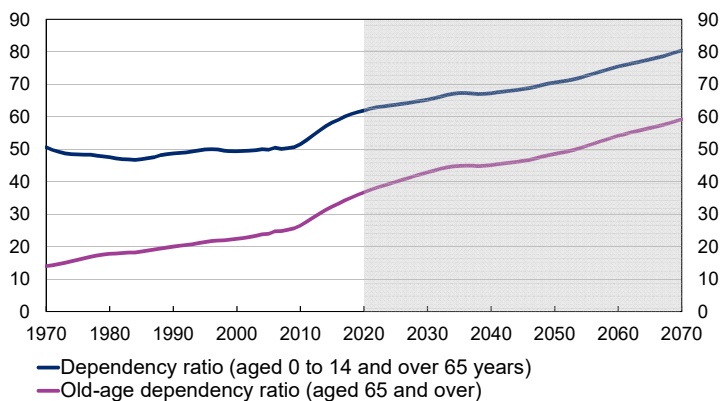


The figure is compiled using the model developed by the Ministry of Social Affairs and Health for social expenditure analysis

Source: MoF

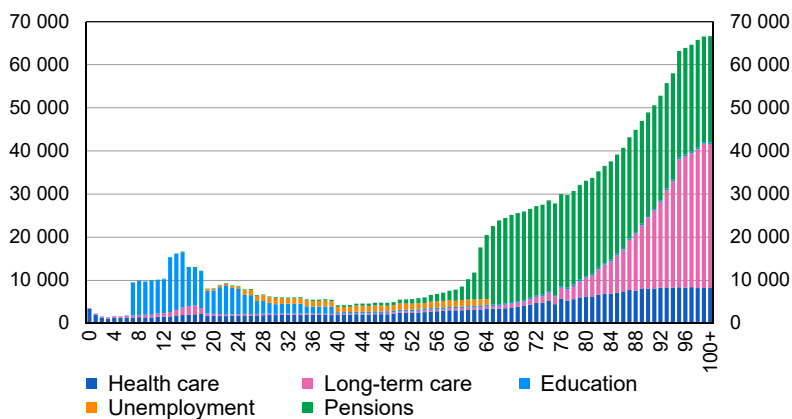
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Dependency ratio persons per hundred persons of working age



Sources: Statistics Finland, MoF

Age-related expenditure by age category in 2019 EUR per capita, average



Sources: SOME model developed by the Ministry of Social Affairs and Health, MoF

Table 28. Impact of various factors on the sustainability gap

	Baseline scenario (fall 2022)	Change	Impact on sustainability gap, pp. ¹
Growth in general productivity (and real earnings) in 2026-2070	on average 1.5%	+0.5 pp.	-0.3
Employment rate (15-64 yrs) in 2026-2070	74.5% in 2026 and 76.5% in 2070	+1.0 pp.	-0.2
Annual productivity growth of public health and social services in 2026-2070	0%	+0.5 pp.	-1.7
General government structural primary balance ² / GDP in 2026	-1.10%	+1.0 pp.	-1.0
Total fertility rate	1.45	+0.25 (= 1.70)	approx. 0.0
Annual net immigration (impact if employment rate remains unchanged)	15000,0	+7,500 (= 22,500)	-0.3
Life expectancy at the age of 50 (33.7 years in 2021)	Will be increased by approximately 7 years by 2070	-1.4 years (= 5.4 years)	-0.6
Postponement of the need for health and social services as life expectancy increases	Will be postponed by half of the life expectancy increase (people aged over 50)	Will be postponed at the rate of life expectancy increase	-1.1
		No postponement as life expectancy increases	1.1
Inflation (change in GDP deflator and consumer prices) in 2026-2070	2%	-0.5 pp.	approx. 0.0
Real interest rate on central and local government debt (+ impact on the discount rates of the two sectors)	Real interest rate on central and local government debt and	-0.5 pp.	-0.2
Real interest rate on central and local government debt and impact on the real rate of return on central and local government and employment pension schemes' investments in bonds (+ impact on all sectors' discount rates)	interest income 2%, real rate of return on central and local government's investments in shares 4% and real rate of return on employment pension schemes' investments 3.5%	-0.5 pp.	0.1
Real interest rate on central and local government debt and real rate of return on all general government investments (+ impact on all sectors' discount rates)	(from 2040s onwards)	-0.5 pp.	0.7

¹The calculations are based on summer 2020 MoF sustainability gap calculations (impact of assumption changes are stable over different calculation rounds)

² Deficit excl. interest payments

Supplementary statistics

2. **Outturn data and forecasts used in budget process for 2017–2021**
3. **National balance of supply and demand**
4. **Financial balance of the Finnish economy**

Appendix table 1. Outturn data and forecasts used in budget process for 2017-2021

	Years 2017-2021		Average forecast accuracy	
	Forecast averages, % ch.	Outcome averages, % ch.	Forecast under-/over-estimation ¹ , pp.	Magnitude of forecast accuracy ² , pp.
GDP (volume)	1.5	1.1	0.4	1.6
GDP (value)	3.2	2.8	0.4	1.9
Private consumption (value)	3.0	1.7	1.3	2.1
Current account, relative to GDP, %	-0.6	0.1	-0.6	1.3
Inflation	1.3	1.1	0.3	0.7
Wage bill	2.6	2.8	-0.2	2.0
Unemployment rate	7.7	7.6	0.1	0.7
Central government debt, relative to GDP, %	48.7	48.2	0.5	4.2
Central government net lending, relative to GDP, %	-2.0	-2.6	0.6	1.5
General government net lending, relative to GDP, %	-1.9	-2.1	0.2	2.0

Forecasts are compared with March/June preliminary national accounts data.

Averages for the past five years are calculated on the basis of spring and autumn forecasts concerning the budget year.

¹ Over- or underestimation is indicated by average forecast accuracy.

² The average of absolute accuracy values indicates the average magnitude of forecast accuracy, regardless of the direction of deviation.

Appendix table 2. National balance of supply and demand, EUR million

	Current prices					
	2019	2020	2021	2022**	2023**	2024**
GDP at market prices	240 097	237 987	251 431	268 902	278 564	288 587
Imports of goods and services	95 283	85 131	98 432	121 054	127 356	132 114
Total supply	335 141	323 118	349 863	389 956	405 920	420 701
Exports of goods and services	95 657	85 512	99 064	118 885	124 982	130 819
Consumption	181 700	179 391	189 489	202 892	210 650	217 524
private	126 081	121 548	128 136	138 008	143 644	148 367
public	55 619	57 843	61 353	64 884	67 007	69 157
Investment	57 149	57 463	59 450	63 874	66 059	68 405
private	46 636	45 767	48 924	52 177	53 370	55 858
public	10 513	11 696	10 526	11 697	12 837	12 517
Total demand	335 146	323 150	348 789	389 969	404 846	419 627
	At reference year 2015 prices; not additive					
	2019	2020	2021	2022**	2023**	2024**
GDP at market prices	229 599	224 486	231 272	235 291	236 575	239 930
Imports of goods and services	90 769	85 476	90 262	91 876	94 305	97 344
Total supply	320 372	309 953	321 427	327 058	330 974	337 540
Exports of goods and services	91 624	85 435	90 224	91 211	93 638	97 404
Consumption	175 912	171 251	176 939	179 334	180 254	182 061
private	121 753	116 810	121 052	122 432	123 444	125 196
public	54 167	54 462	55 917	56 924	56 835	56 897
Investment	52 317	52 043	52 607	54 511	55 147	56 080
private	42 528	41 195	43 098	44 312	44 357	45 631
public	9 794	10 878	9 491	10 189	10 792	10 438
Total demand	320 373	309 447	320 401	326 032	329 945	336 509

Appendix table 3. Financial balance of the Finnish economy

	2017	2018	2019	2020	2021
	relative to GDP, %				
Gross investment	23.3	24.1	23.8	24.2	23.4
households and non-profit institutions	6.9	7.1	7.0	7.0	7.1
non-financial corporations and financial and insurance corporations	12.4	12.6	12.4	12.2	12.1
general government	4.1	4.3	4.4	4.9	4.1
Gross saving ¹	23.3	23.5	23.8	25.2	25.9
households and non-profit institutions	3.6	3.9	4.7	7.2	4.9
non-financial corporations and financial and insurance corporations	16.3	16.2	15.7	18.7	19.4
general government	3.3	3.4	3.4	-0.7	1.6
Financial surplus	-0.7	-1.8	-0.2	0.8	0.8
households and non-profit institutions	-3.5	-3.3	-2.5	0.0	-2.4
non-financial corporations and financial and insurance corporations	3.4	2.4	3.2	6.2	6.6
general government	-0.7	-0.9	-0.9	-5.5	-2.6
Statistical discrepancy	0.0	-0.0	0.0	-0.1	0.8

¹ Incl. capital transfers (net)



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