Economic Survey Winter 2023

Economic Prospects

PUBLICATIONS OF THE MINISTRY OF FINANCE – 2023:96

MINISTRY
OF FINANCE

Publications of the Ministry of Finance 2023:96

Economic Survey

Winter 2023

Economics Department

Ministry of Finance Helsinki 2023

Publication distribution

Institutional Repository for the Government of Finland Valto

julkaisut.valtioneuvosto.fi

Ministry of Finance

ISBN pdf: 978-952-367-456-1
ISSN pdf: 1797-9714

Layout: Government Administration Department, Publications

Helsinki 2023 Finland

Description sheet
19 December 2023

Economic Survey, Winter 2023

Publications of the Ministry of Finance 2023:96		**Subject**	Economic Prospects
Publisher	Ministry of Finance		
Group Author	Economics Department		
Language	English	**Pages**	95

Abstract

The increase in prices and interest rates has reduced household consumption and investment. The Finnish economy will contract by 0.5% in 2023. In 2024, slowing inflation and a downward turn in interest rates, combined with moderately strong household income growth, will increase household disposable income. GDP will grow by 0.7% in 2024. Growth in consumption and investments will pick up in 2025 and the economy will grow by 2.0%. In 2026, growth will be 1.6%. Employment will fall slightly in 2024, but will increase from 2025 onwards. In 2026, the employment rate for people aged 15-64 will be close to 75% and the unemployment rate 6.6%.

The general government deficit will be 2.5% of GDP in 2023. The deficit will grow to 3.5% in 2024, driven by weak economic and employment growth and slow growth in tax revenue. The general government deficit will improve to around 3.0% of GDP in the following years as the Government's adjustment measures start to have an effect and the economy and employment begin to grow towards the end of the outlook period. The central government deficit will remain substantial throughout the outlook period, and local government deficits are not expected to improve. Due to the central government and local government deficits as well as slow economic growth, the debt ratio will continue to increase, and it is not on track to decline given the foreseeable economic development.

Keywords	economic prospects, public finance, economic development.		
ISBN PDF	978-952-367-456-1	**ISSN PDF**	1797-9714
URN address	https://urn.fi/URN:ISBN:978-952-367-456-1		

Kuvailulehti
19.12.2023

Taloudellinen katsaus, talvi 2023

Valtiovarainministeriön julkaisuja 2023:96		**Teema**	Talousnäkymät
Julkaisija	Valtiovarainministeriö		
Yhteisötekijä	Kansantalousosasto		
Kieli	englanti	**Sivumäärä**	95

Tiivistelmä

Hintojen ja korkojen nousu on vähentänyt investointeja ja kotitalouksien kulutusta. Suomen talous supistuu 0,5 prosenttia vuonna 2023. Vuonna 2024 inflaation hidastuminen ja korkojen kääntyminen laskuun yhdessä kotitalouksien kohtuullisen hyvän tulokehityksen kanssa lisäävät kotitalouksien käytettävissä olevia tuloja. BKT kasvaa 0,7 prosenttia vuonna 2024. Kulutuksen ja investointien kasvu voimistuu vuonna 2025 ja talous kasvaa 2,0 prosenttia. Vuonna 2026 kasvu on 1,6 prosenttia. Työllisyys laskee hieman vuonna 2024, mutta kasvaa vuodesta 2025 lähtien. Vuonna 2026 15–64-vuotiaiden työllisyysaste on lähes 75 prosenttia ja työttömyysaste 6,6 prosenttia.

Julkisyhteisöjen alijäämä on 2,5 prosenttia suhteessa BKT:hen vuonna 2023. Alijäämä kasvaa vuonna 2024 3,5 prosenttiin heikon talous- ja työllisyyskasvun sekä hitaan verotulojen kasvun vetämänä. Julkisyhteisöjen alijäämä kohenee jatkovuosina noin 3,0 prosenttiin suhteessa BKT:sta, kun hallituksen sopeutustoimet alkavat purra sekä talous ja työllisyys alkavat kasvaa ennustejakson lopulla. Valtionhallinnon alijäämä pysyy mittavana läpi koko ennustejakson, eikä paikallishallinnossakaan ole odotettavissa alijäämien oikenemista. Valtion ja paikallishallinnon alijäämien sekä hitaan talouskasvun seurauksena velkasuhde jatkaa kasvuaan, eikä se ole kääntymässä laskuun näköpiirissä olevalla talouden kehityksellä.

Asiasanat	talousnäkymät, julkinen talous, taloudellinen kehitys.		
ISBN PDF	978-952-367-456-1	**ISSN PDF**	1797-9714
Julkaisun osoite	https://urn.fi/URN:ISBN:978-952-367-456-1		

Presentationsblad
19.12.2023

Ekonomisk översikt, vinter 2023

Finansministeriets publikationer 2023:96		**Tema**	Ekonomiska utsikter
Utgivare	Finansministeriet		
Utarbetad av	Ekonomiska avdelningen		
Språk	engelska	**Sidantal**	95

Referat

De stigande priserna och räntorna har minskat investeringarna och hushållens konsumtion. Finlands ekonomi krymper med 0,5 procent 2023. År 2024 kommer den avtagande inflationen och det faktum att räntorna börjar sjunka i kombination med hushållens relativt goda inkomstutveckling att öka hushållens disponibla inkomster. Bruttonationalprodukten (BNP) ökar med 0,7 procent 2024. År 2025 stärks konsumtions- och investeringstillväxten och ekonomin växer med 2,0 procent. År 2026 uppgår tillväxten till 1,6 procent. Sysselsättningen minskar något 2024, men ökar igen från och med 2025. År 2026 var sysselsättningsgraden för 15–64-åringar inemot 75 procent och arbetslöshetsgraden 6,6 procent.

År 2023 är underskottet i den offentliga sektorns finanser 2,5 procent i förhållande till BNP. Underskottet ökar 2024 till 3,5 procent till följd av den svaga ekonomiska tillväxten och sysselsättningstillväxten samt den långsamma ökningen av skatteinkomster. Underskott i den offentliga sektorns finanser stiger under de följande åren till cirka 3,0 procent i förhållande till BNP i och med att regeringens anpassningsåtgärder börjar ge effekt och ekonomin och sysselsättningen börjar öka i slutet av prognosperioden. Underskottet i statsförvaltningen blir fortsatt kraftigt under hela prognosperioden, och inte heller inom lokalförvaltningen förväntas underskotten börja minska. Till följd av statens och lokalförvaltningens underskott och den långsamma ekonomiska tillväxten fortsätter skuldkvoten att öka, och det finns inga utsikter att den skulle börja minska med den ekonomiska utveckling som är inom synhåll.

Nyckelord ekonomiska utsikter, offentlig ekonomi, ekonomisk utveckling.

ISBN PDF	978-952-367-456-1	**ISSN PDF**	1797-9714
URN-adress	https://urn.fi/URN:ISBN:978-952-367-456-1		

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

SYMBOLS AND CONVENTIONS USED

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

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

ECONOMIC SURVEY WINTER 2023

This Economic Survey offers projections of economic developments in 2023–2026. In addition to short-term prospects, it includes a medium-term economic outlook extending to 2028.

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

The forecasts are based on quarterly national accounts data published by Statistics Finland in November 2023 and on other public statistical sources available by 13 December 2023.

Helsinki December 2023

Ministry of Finance Economics Department

Mikko Spolander
Director General

Janne Huovari
Senior Financial Advisor
Head of Macro Forecasting

Jenni Pääkkönen
Senior Financial Advisor
Head of Public Finance

Contents

Preface

The Finnish economy has been expected to drift into a recession towards the end of this year, and expectations have been fulfilled. Finland is in recession.

The recession will be deeper and longer than expected. As a result, the picture for 2024 has also deteriorated.

Early 2023 turned out to be weaker than forecast. Indeed, demand for services no longer supported private consumption in the second quarter of the year. Investments also decreased more than expected.

A turn for the worse was expected to take place in the third quarter of the year. This indeed happened, but according to preliminary data, the third quarter was even worse than expected.

Although wages are rising and inflation has slowed rapidly, interest rates are now biting into consumption and investment with full force, employment is weakening and households' financial gloom has started to intensify once again.

There will be a sticky start to 2024. However, growing purchasing power and falling interest rates will gradually turn the economy into a new upswing during 2024. When the brakes restraining growth are released, demand and output will recover and employment will start to grow. At the same time, work-incentivising reforms will increase labour supply. We estimate that in 2025 and 2026, demand and output will close quite quickly the gap that had opened.

Even if the economic conditions turn more favourable next year, the Finnish economy will enter the coming years in less than good shape. The COVID-19 pandemic, Russia's invasion of Ukraine, rising prices, costs and interest rates as well as the recession have blocked the circulation of the economy in a situation where the Finnish economy was already in need of an angioplasty.

The outlook for general government finances has been bleak for a long time, and even now there is no light to be seen.

Population ageing is putting the brakes on the economy's revenue generation and increasing the need for services. At the same time, the unit costs of services are rising. The restructuring of the economy is eroding taxation. More money will inevitably be sunk into interest on public debt as the central government, the wellbeing services counties and the municipalities will remain in deficit and debt will continue to grow. The imminent turn towards lower interest rates will likely be sufficient only to slow down growth in debt servicing expenditure.

The general government deficit will narrow more slowly as the turnaround to a new upswing is delayed.

In addition, even more problems threaten to accumulate in central government finances. As estimates of the 2023 deficit in the wellbeing services counties have deteriorated, and completed tax data have revised the transfer calculations for the health and social services reform, the wellbeing services counties and the municipalities are demanding more money from central government to cover their operating expenses.

The savings and work-incentivising reforms outlined in the Government Programme will reduce the general government deficit, but even implementation of the programme in full and on time will not be enough to reduce the deficit to the target of 1% of GDP in 2027 or to reverse the increase in public debt relative to GDP by 2027.

Strengthening the revenue generation capacity of the economy would be the best way to strengthen general government finances in the desired way.

The ongoing technological revolution, the energy transition and the associated reindustrialisation of the economy are creating concrete opportunities that, through their utilisation, new production and new jobs can be created in Finland. The change in the production structure requires vast investment and will succeed when the ability of Finnish companies and Finnish society to compete for investments is in good shape. The public authorities build the investment environment through their own decisions.

Without underestimating the opportunities related to technological change, energy transition and re-industrialisation, they are hardly sufficient to correct the structural imbalance in general government funding – at least not during one parliamentary term.

Economic restructuring takes time. The employment and productivity leap needed to strengthen revenue-generation capacity must be so large and implemented so rapidly that further plans to strengthen general government finances as desired cannot be based on them alone.

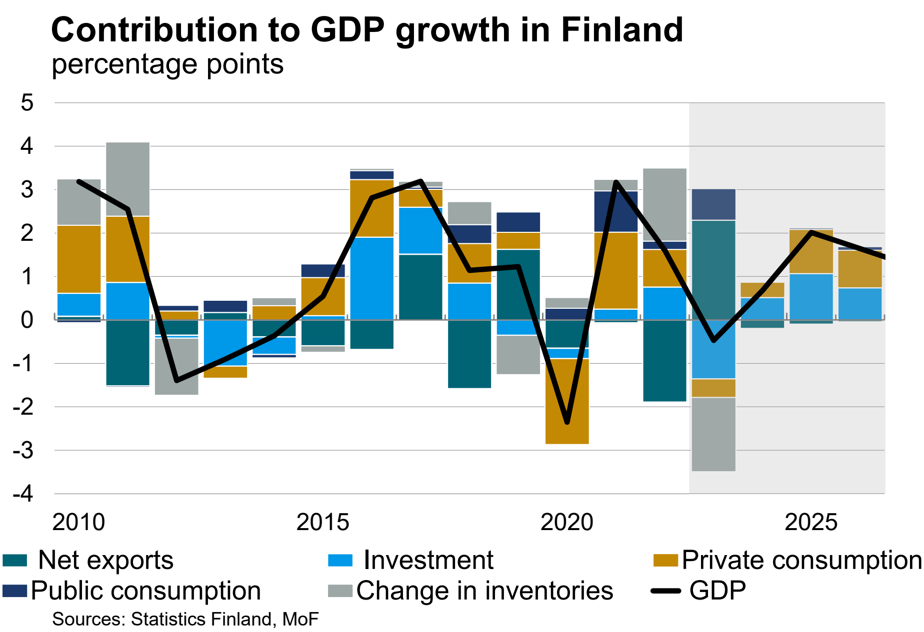
In addition to measures to support growth in employment and productivity, achieving the targets would require further savings as well as measures to maintain total tax revenue. These are currently being screened by a working group established by the Ministry of Finance to identify additional measures to strengthen general government finances.

Summary

Economic outlook for the period 2023 – 2026

At the beginning of the year, the Finnish economy was weaker than previous estimates, and in the third quarter output clearly decreased. The economic situation at end of the year remains weak, and Finland's GDP will contract by 0.5% this year. Construction is in the weakest situation, but good growth in services has also stalled.

The economy is expected to return to growth, however. Slowing inflation and a fall in interest rates, combined with moderately strong household income growth, will increase the purchasing power of households. Private consumption is set to return to subdued growth next year, and growth will strengthen in 2025. The fall in interest rates will also support investment, which will be underpinned by the energy transition and defence investment. In 2024, GDP will grow by 0.7%, and growth will strengthen in 2025 and 2026 to 2.0% and 1.6% respectively.



Boost from growth in world trade

Global economic growth has been slowed by inflation and rising interest rates as well as geopolitical tensions. However, the rapid slowdown in inflation and the good employment situation support future growth prospects. Interest rates are also expected to fall faster than previously expected. The mood in the financial markets has been quite optimistic recently. The global economy is expected to grow by 2.7% in 2024 and 3.0% in 2025.

Economic growth in the United States has been significantly faster than in the euro area in the recovery from the coronavirus crisis. In the euro area, economic growth has been held back by high energy prices, while in the United States the economy has been boosted by a stimulative fiscal policy. In the outlook period, however, the growth gap will be narrowed by the recovery of the euro area economy.

World trade has contracted this year, despite the growth of the global economy. This contraction is due both to geopolitical tensions and high inventory levels. In the future, however, world trade is expected to recover and also to provide a boost to Finnish exports. In 2023, exports from Finland will decline, but significantly less than imports. Net exports will therefore make a noticeably positive contribution to the economy this year. In 2024, exports are already expected to grow. Finland's cost-competitiveness is in good shape, and exports will grow as world trade recovers.

Slowing inflation and falling interest rates will boost consumption

Inflation has slowed rapidly during 2023. Inflation will be 2% on average in 2024, and will fall below 2% in 2025 and 2026. The main reason for the slowdown in inflation has been the fall in energy prices but, from the latter part of 2023, the slowdown has been broad-based. Price pressures remain highest in services but, even there, price increases have clearly slowed. As inflation slows, interest rates will also start to fall. Expectations for a fall in key interest rates next year have been brought forward and market interest rates have already decreased. The biggest positive impact from lower interest rates will be seen in 2025.

Real earnings will take an upturn in 2024, but the growth of household purchasing power will still remain subdued, as the deterioration of employment and social benefit cuts will curb growth of household disposable income. From 2025 onwards, household purchasing power and consumption growth will accelerate.

Residential construction decreasing and energy transition boosting investment

The construction of new housing is in sharp decline and this will continue in 2024. However, there is demand for housing due to immigration and domestic internal migration. A downturn in interest rates will stimulate the housing market and new production will increase from 2025 onwards. Non-residential construction is also in decline, but will recover faster than residential construction.

Despite the challenging short-term outlook, expectations for production investments are positive, and companies have a strong need to invest in the next few years. In addition to climate change and the energy transition, ever-advancing digitalisation and the use of artificial intelligence will increase investment. Indeed, there are a record number of plans for productive investments.

The volume of public investment will increase in the next few years, even though the tight situation in general government finances will reduce investment opportunities. Central government investment will be sustained by the strengthening of cyber security, border control and national defence as well as RRF investment funding. In local government, investment pressure will continue due to population migration and the repair backlog of the building stock.

Employment will fall, but remain high

With the decline in production, the demand for labour will decrease and the number of employed people start to fall. In 2024, employment will decline temporarily and the employment rate will fall. However, companies will respond to weak demand for labour mainly by adopting temporary layoffs and other labour flexibilities rather than redundancies. Indeed, the number of hours worked will decline more than employment. The contraction of construction activity, in particular, will increase unemployment in 2023 and 2024. The unemployment rate will rise to 7.5% in 2024.

In 2025 and 2026, economic growth will be quite strong, with employment increasing by nearly 1% per year. Employment growth will be broad-based and underpinned by the Government's measures to increase labour supply, the first of which will take effect in 2024. The employment rate for people aged 15–64 will reach nearly 75% in 2026.

Medium-term outlook 2027–2028

Over the medium term, economic output is projected to grow moderately. In 2027, GDP is projected to grow by around 1.3%, and growth of around 1.1% is expected in 2028. The factors supporting GDP growth include the growth of private investment, which is expected to recover due to decreasing market interest rates as well as green transition investments. The Finnish economy is projected to be still below potential output in 2027. Potential output growth will be around 1% per year.

Weak economic development will keep general government deficits deep

The general government deficit will be 2.5% of GDP in 2023. The deficit will deepen to 3.5% in 2024, driven by weak economic and employment growth and slow growth in tax revenue. The general government deficit will improve to around 3.0% of GDP in the following years as the Government's adjustment measures start to take effect and the economy and employment begin to grow towards the end of the outlook period. Despite all this, the general government deficit will be deep.

The central government deficit will remain substantial throughout the outlook period. Tax revenue will grow moderately and, despite the adjustment measures, expenditure growth will remain brisk. The rapid rise in prices and wages, the large investments made in preparedness and security, and the increasing debt servicing costs will keep central government expenditure growing throughout the outlook period.

The wellbeing services counties are planning adjustment measures, which are taken into account in the forecast to an amount of EUR 0.3 billion for 2024. Nevertheless, the deficit for 2024 is projected to remain at the 2023 level of around 0.5% of GDP. The deficit, moreover, is not on track to be corrected during the outlook period. In addition, local government is projected to be in deficit throughout the outlook period. On the other hand, employment pension schemes will remain significantly in surplus, and the other social security funds will remain close to balance during the outlook period.

As a result of the central government and local government deficits as well as slow economic growth, the debt ratio will continue to increase, and it is not on track to decline given the foreseeable economic development. In 2023, the debt ratio will be just over 75% of GDP and in 2026 it will be over 83%.

Risks

The decline of residential construction may be larger and last longer than projected. If construction and real estate companies were to run into financial difficulties on a large scale, the functioning of whole economy would be adversely affected. A slower-than-projected fall in interest rates would deepen the recession in the construction industry and weaken investment prospects in general compared with the forecast.

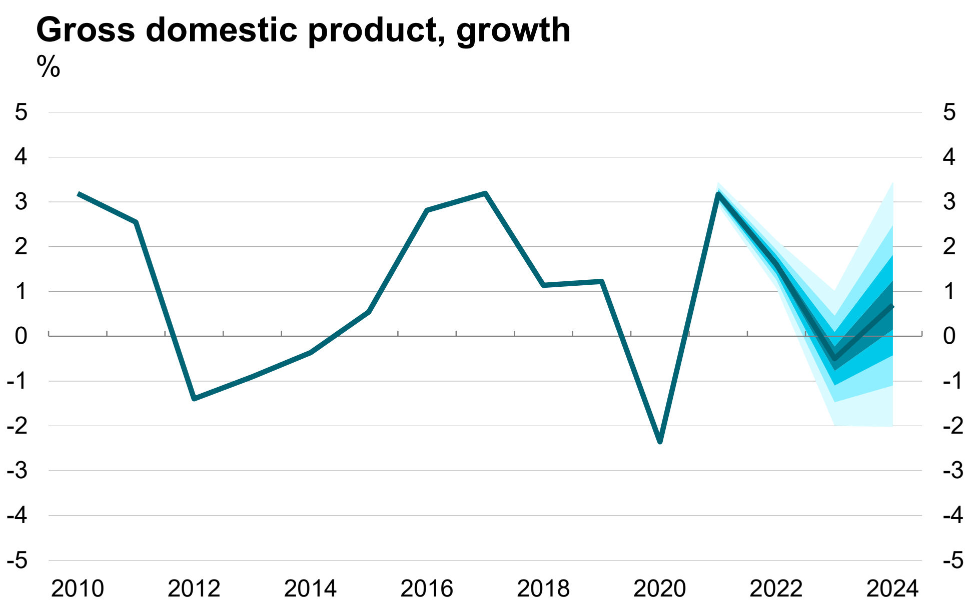
The outlook for the global economy is also rather bleak. Recent years have seen major crises, to which the response has been exceptional policy measures. The economy has not yet adjusted to all these changes and there is much uncertainty about the ultimate impacts. In addition, negative risks related to geopolitics and the environment may, if realised, increase uncertainty and disrupt the economy.

Furthermore, the economy is undergoing an energy transition and rapid technological development, which are likely to have major impacts. Positive surprises would probably be reflected first in investments.

Household consumption may also surprise positively if the economy otherwise develops in line with the forecast. In the forecast, the saving rate still remains reasonably high, so the development of household income would provide an opportunity for greater growth in private consumption. A faster-than-projected fall in interest rates would boost consumption more than forecast and accelerate the recovery in the housing market.

The real economy risks described above will inevitably be reflected in general government finances. Weaker (stronger) than forecast employment and economic growth will weaken (strengthen) general government finances. If, on the other hand, interest rates fall faster than projected, the central government deficit and the general government debt ratio will develop more moderately. The impact on the general government deficit will be limited, however, because the general government entities also has significant property income. A labour shortage, on the other hand, may have unpredictable effects on both the municipal sector and the wellbeing services counties. In addition, there is uncertainty associated with wellbeing services counties' savings measures, as it is possible that the wellbeing services counties will take more measures than has been assumed in this forecast.

The uncertainty of the economic growth forecast can be illustrated by confidence intervals around the forecast based on past forecast errors. Confidence intervals describe the range within which actual figures have fallen in previous forecasts with an 80% probability. However, these confidence intervals only reflect the normal uncertainty involved in forecasts, and they do not take into account the special risk factors present in each instance of forecasting.



Source: Statistics Finland, MoF

Table 1. Key forecast figures

	2022	2021	2022	2023**	2024**	2025**	2026**
	EUR bn	change in volume, %					
GDP at market prices	269	3.2	1.6	-0.5	0.7	2.0	1.6
Imports	128	6.0	8.5	-6.1	2.4	4.0	3.0
Total supply	**397**	**3.9**	**3.5**	**-2.3**	**1.2**	**2.6**	**2.0**
Exports	122	5.8	3.7	-1.3	2.0	3.8	3.0
Consumption	203	3.6	1.4	0.4	0.5	1.4	1.2
private	138	3.5	1.7	-0.8	0.7	2.0	1.7
public	65	3.9	0.8	3.0	0.0	0.1	0.3
Investment	65	1.0	3.2	-5.6	2.2	4.6	3.1
private	54	4.3	4.0	-5.4	0.9	2.9	4.2
public	11	-11.8	-0.2	-6.6	9.0	12.5	-1.3
Total demand	**395**	**3.7**	**3.3**	**-2.3**	**1.2**	**2.6**	**2.1**
domestic demand	274	3.0	3.2	-2.7	0.9	2.1	1.7

Table 2. Other key forecast figures

	2021	2022	2023**	2024**	2025**	2026**
GDP, EUR bn	251	269	282	289	301	313
Services, change in volume, %	4.3	3.2	0.9	0.7	1.5	0.9
Industry, change in volume, %	2.0	-1.3	0.2	1.8	2.8	1.9
Labour productivity, change, %	1.4	0.0	0.0	1.7	1.3	0.7
Employed labour force, change, %	2.4	2.5	0.1	-0.2	0.8	0.9
Employment rate (15–64 yrs), %	72.3	73.8	73.6	73.5	74.1	74.8
Employment rate (20–64 yrs), %	76.6	78.1	77.9	77.9	78.7	79.5
Unemployment rate, %	7.7	6.8	7.2	7.5	7.1	6.6
Consumer price index, change, %	2.2	7.1	6.3	2.0	1.4	1.7
Index of wage and salary earnings, change, %	2.4	2.4	4.2	3.5	3.3	3.1
Current account, EUR bn	1.0	-6.8	-2.2	-2.3	-2.7	-2.8
Current account, relative to GDP, %	0.4	-2.5	-0.8	-0.8	-0.9	-0.9
Short-term interest rates (3-month Euribor), %	-0.5	0.3	3.4	3.4	2.4	2.1
Long-term interest rates (10-year govt. bonds), %	-0.1	1.7	3.1	3.2	3.1	3.1
General government expenditure, relative to GDP, %	55.7	53.3	54.5	54.9	54.7	53.9
Tax ratio, relative to GDP, %	43.1	42.9	41.5	40.5	40.5	40.3
General government net lending, relative to GDP, %	-2.8	-0.8	-2.5	-3.5	-3.4	-3.0
Central government net lending, relative to GDP, %	-3.3	-1.6	-3.2	-3.7	-4.2	-3.8
General government gross debt, relative to GDP, %	72.5	73.3	75.5	79.1	81.4	83.3

1 Economic outlook

1.1 International economy

1.1.1 Global economy

The outlook for the global economy is uncertain at the end of 2023. The outlook is weakened by the transmission of high interest rates to private consumption and the associated weak consumer confidence as well as the modest development of world trade. In addition, geopolitical tensions remain high due to the continuation of Russia's war of aggression and the conflict in the Middle East. On the other hand, the rapid slowdown in inflation and the continued high level of employment in many economies support growth prospects. The global economy will grow by 2.7% in 2024, accelerating to 3% in 2025.

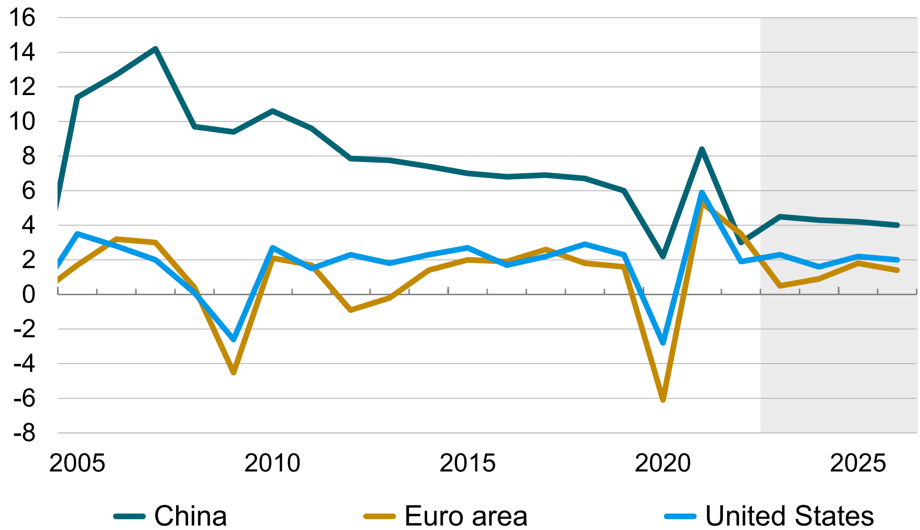
Economic growth in the euro area has stalled at the end of 2023. Total output contracted in the third quarter of the year. The outlook for German industry, in particular, is difficult. Leading indicators for both industry and services in the euro area remain on a low level. Inflation has slowed rapidly, resulting in expectations of an earlier easing of monetary policy. Construction is in deep crisis in a number of countries. Fiscal policy is expected to be mildly tightening in the next few years. Economic growth will recover from 0.5% in 2023 to 0.9% in 2024 as real incomes rise. Growth will accelerate further to 1.8% in 2025 as the global economy recovers. The Swedish economy is in recession at the end of 2023, and the situation is difficult due to the crisis in the construction industry, among other things. Total output will contract by 0.5% in 2023, but growth will recover to 0.8% in 2024 and to 1.8% in 2025.

Despite the uncertainties in the global economy, the economic outlook for the United States is quite favourable. Growth was strong in the third quarter of 2023, largely driven by private consumption. It is generally expected that the economy will experience a soft landing, with economic growth slowing in 2024, but will not go into recession despite tight monetary policy. In addition, inflation has slowed rapidly, which will support real incomes. Leading indicators have remained relatively strong. Fiscal policy is expected to be mildly tightening in the next few years. Economic growth will slow from 2.3% in 2023 to 1.6% in 2024, before recovering to 2.2% in 2025.

The economic outlook for China is challenging. The economic model based on public investments appears to have reached the end of the road, and the real estate sector is in deep crisis. Exports have been struggling in 2023, although they have picked up slightly towards the end of the year. At the same time, retail trade has recovered to some extent, but the outlook for private consumption remains uncertain. Inflation has slowed rapidly during 2023, and turned negative for a couple of months during the second half of the year due to exceptional factors. Economic growth will slow to 4.3% in 2024 and further to 4.2% in 2025.

The relatively favourable development of the Japanese economy in 2023 was halted by a contraction in total output in the third quarter. The near-term outlook is fairly positive, however, supported by exports. The UK economy has improved slightly as inflation slows, but the outlook for industry remains difficult. In the short term, economic growth in Russia appears to be supported by war-related industry. Isolation from the Western global economy is darkening the longer-term outlook. India's economic outlook is favourable as consumer confidence and the outlook for industry remain strong.

Gross domestic product
change in volume, %

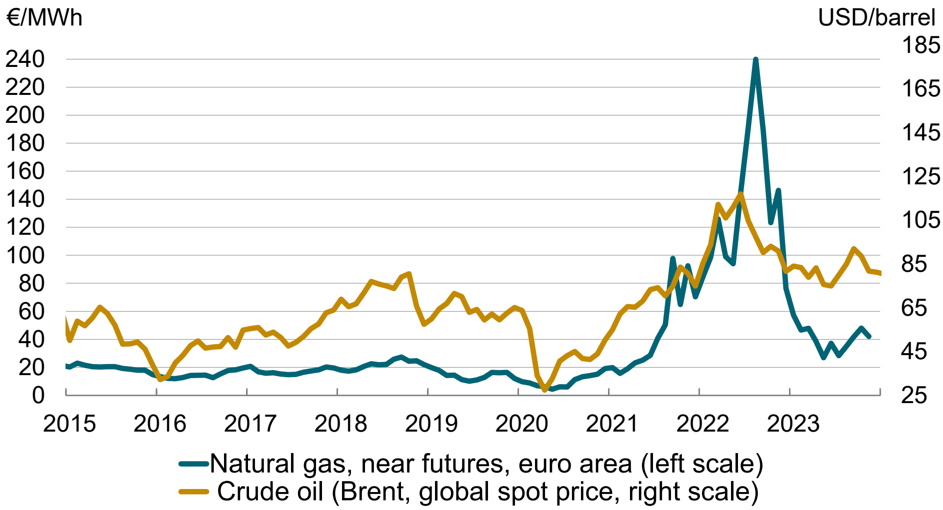


Sources: Statistical authorities, MoF

The mood in international financial markets has been quite optimistic recently. Market interest rates have taken a downward turn, as expectations grow of an earlier easing of monetary policy. Long-term interest rates have declined sharply, although they are also influenced by other factors. European stock indices have been rising modestly in the latter part of the year. The outlook for banks, in particular, is positive, whereas in spring 2023 there were still fears of an exacerbation of banks' problems in the United States and to some extent in Europe. Government bond spreads remained quite stable, indicating the situation to be calm. Potential risks include inflation accelerating once again above the central banks' target levels as well as unexpected market disturbances that could lead to chain reactions and broader impacts. Geopolitical turns of events, in particular, could trigger such reactions.

The price of crude oil has been on a downward path despite the production cuts announced by the OPEC+ countries. Oil production in the United States is at peak levels. The price of crude oil will fall during the outlook period. After a slight increase in the second half of 2023, the price of natural gas has started to fall again. Futures point to a downward trend in prices during 2024. Electricity prices are expected to rise slightly during the winter and heating season, but to fall again in spring 2024. Prices of industrial raw materials will continue to fall, although demand for some metals will remain strong as the battery industry grows.

Raw material prices



Sources: Intercontinental Exchange (ICE), Macrobond

1.1.2 World trade

World trade in goods has been very modest during 2023. In addition to the subdued general economic outlook, this seems to have been influenced, at least to some extent, by the restructuring of world trade. Many countries have deepened their trade relations with countries located nearby or perceived as friendly. The positive development of China's exports in October, however, points to a recovery in goods trade in the latter part of 2023. This outlook is also supported by strong growth in container traffic and rising freight rates towards the end of the year. After contracting by 1.9% in 2023, world trade will recover to 4.4% growth, largely due to developing countries and the United States. Growth will level off at 4.1% in 2025, also as the European economic outlook improves and foreign trade recovers.

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

1.1.3 Risks

Risks associated with the outlook for the global economy are rather strongly skewed to the downside. The conflict in the Middle East that broke out in October 2023 may affect sensitive energy markets, although fears of an escalation of the crisis have gradually subsided. The prolongation of Russia's war of aggression is maintaining geopolitical tensions. A renewed acceleration of inflation would lead to a continuation of tight monetary policy, weakening growth prospects globally. Further geo-economic fragmentation would deepen dividing lines in the global economy and world trade. An escalation of China's economic problems could weaken the outlook for the entire global economy. The impact of climate change may cause even greater adverse economic effects than expected.

A faster-than-expected slowdown in inflation would increase real incomes and broadly strengthen consumption demand. This outlook would be supported by an employment situation advancing more strongly than expected in many economies. An easing of geopolitical tensions would boost confidence worldwide.

Table 3. Gross domestic product

	2021	2022	2023**	2024**	2025**	2026**
	change in volume, %					
World (PPP)	6.7	3.3	2.9	2.7	3.0	2.8
Euro area	5.9	3.4	0.5	0.9	1.8	1.4
EU	5.7	3.2	0.5	0.9	1.8	1.4
Germany	3.1	1.9	-0.3	0.9	1.5	1.0
France	6.4	2.5	0.7	1.7	1.8	1.6
Sweden	5.9	2.9	-0.5	0.8	1.8	1.7
United Kingdom[1]	8.7	4.3	0.3	0.8	1.3	1.2
United States	5.8	1.9	2.3	1.6	2.2	2.0
Japan	2.3	0.9	1.7	1.4	0.7	0.4
China	8.4	3.0	4.5	4.3	4.2	4.0
India[2]	9.1	7.2	6.3	6.5	6.3	6.0
Russia	5.6	-2.1	1.5	0.5	1.0	0.8

[1] The United Kingdom withdrew from the European Union on January 1st 2021

[2] Fiscal year (April 1st to March 31st)

Sources: Statistical authorities, MoF

Table 4. Background assumptions

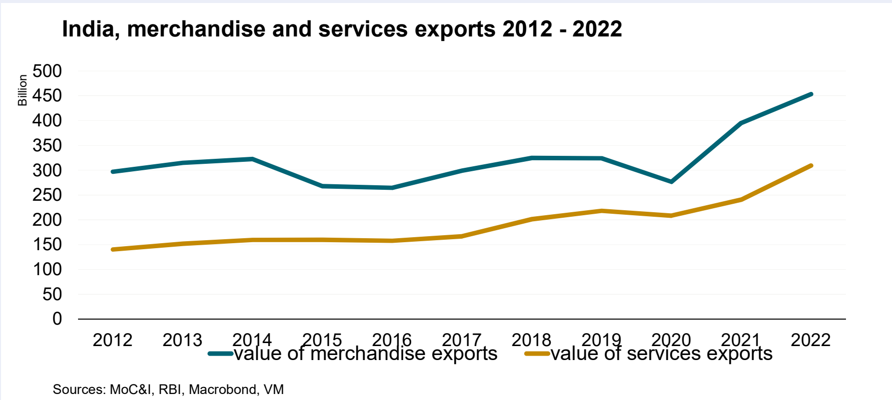
	2021	2022	2023**	2024**	2025**	2026**
World trade growth, %	10.9	3.7	-1.9	4.4	4.1	3.3
USD/EUR	1.18	1.05	1.08	1.07	1.07	1.07
Industrial raw material price index, EA, € (2015=100)	169.0	185.1	154.8	150.0	147.0	144.0
Crude oil (Brent), $/barrel	70.7	98.7	82.3	79.6	76.3	73.5
3-month Euribor, %	-0.5	0.3	3.4	3.4	2.4	2.1
Government bonds (10-year), %	-0.1	1.7	3.1	3.2	3.1	3.1
Export market share (2010=100)[1]	92.5	92.5	93.0	90.9	90.7	90.4
Import prices, %	9.7	19.4	-3.7	-1.6	1.7	1.7

[1] Ratio of export growth to world trade growth

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

Outlook and challenges for the Indian economy

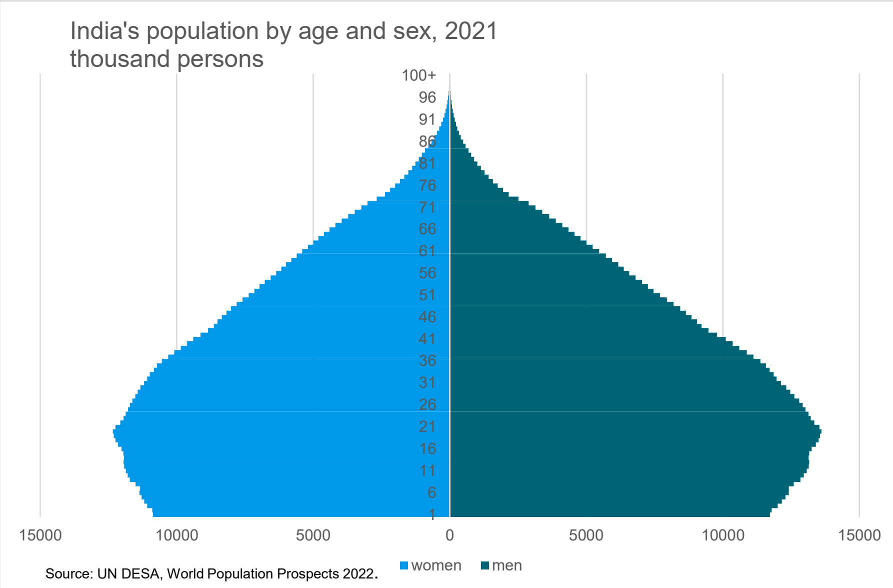
India's significance in the global economy is growing. According to UN estimates, the country's population overtook China's in April 2023 and accounts for one sixth of the world's population. Economic growth has been the fastest among the G20 countries in recent years, at around 6-7% per year, and it is expected to maintain this pace. According to a recent estimate, India's contribution to world economic growth is already approaching that of China, as measured by purchasing power parity.



India is particularly known for exports of IT services. Indeed, services exports have grown rapidly in recent years (see figure). There are many IT experts in the country who speak fluent English. In addition, labour is inexpensive. IT services are mainly exports of insurance sector, software and business services as well as financial services. Software activities account for around half of this. The main software and IT export destinations are the United States (62%), the UK (17%) and the EU countries (11%).

India's significance in the global economy may be considered, indeed, to be related to this growth in IT services exports. In contrast to growth in world trade in goods, growth in trade in services remains strong. Exports are expected to grow, in particular, to other than those industrialised countries mentioned above. As digitalisation progresses in emerging and developing economies, IT services may be expected to grow, and in this India has an advantageous position.

India has a young population and the country may benefit from the demographic dividend, i.e. the transition into the labour market of age cohorts that are coming of age and the resultant rapid economic growth. This is a phenomenon that will happen in the next few years, because in India, as in many other economies, the youngest age cohorts are already shrinking.



The challenges facing India are enormous. A key structural challenge is the caste system, which limits, in particular, the professional and social mobility of non-caste people, and thereby opportunities to make life choices. In economic terms, the caste system may be seen as a massive underutilisation of human capital. Caste-based discrimination was officially prohibited in the Indian Constitution in 1950, but the caste system still exists, particularly in rural areas. e challenges facing India are enormous. A key structural challenge is the caste system, which limits, in particular, the professional and social mobility of non-caste people, and thereby opportunities to make life choices. In economic terms, the caste system may be seen as a massive underutilisation of human capital. Caste-based discrimination was officially prohibited in the Indian Constitution in 1950, but the caste system still exists, particularly in rural areas.

Widespread poverty is a key societal challenge. According to a UN estimate (2016), India has 80 million people living in absolute poverty (6.7% of the population, definition: income level below USD 1.25 per day). In addition, the World Bank estimated in 2019 that 84% of the population live on less than USD

6.85 per day. On the other hand, according to a UN estimate, the number of people in extreme poverty decreased by 271 million between 2005–2006 and 2015–2016.

Poverty is linked to large-scale informal work. According to estimates, 85–90% of India's labour force works in the informal labour market. The overwhelming majority of these people are self-employed or work occasionally. Others work for an official employer, i.e. belong to so-called organised informal labour. Informal work is a key factor in maintaining poverty. Workers are out of the reach of services and social networks.

India's middle class is large and it is projected to continue to grow over the next decade. This group constitutes a considerable societal force that may be expected to have consumption potential even on a global economic scale.

Sources:

https://news.un.org/en/story/2023/04/1135967

https://www.ft.com/content/85c4bd8d-84a2-4008-b86a-946c14706b2e

https://www.indiantradeportal.in/vs.jsp?lang=0&id=0,31,24100,29404

https://en.wikipedia.org/wiki/Poverty_in_India

Ramana Murthy, S V, Measuring Informal Economy in India _ Indian Experience, Session II: Traditional Estimation Practices: Determining the Level and Growth of the Informal Economy, www.imf.org

1.2 Foreign trade

1.2.1 Exports and imports

2023 has been marked by an economic slowdown both in Finland and internationally. In Finland, both export and import volumes have fallen, as have foreign trade prices, resulting in a rather sharp decline in the value of exports and imports. From the standpoint of growth of the Finnish economy, however, foreign trade has supported GDP growth, as net exports have been positive. This is due to the fact that imports have declined more sharply than exports in 2023. In the previous year, net exports had the opposite effect; despite economic growth, net exports weakened GDP.

In 2023, imports of goods have fallen sharply both in Finland and across Europe. The previous year's growth was quite strong, partly because companies prepared for the uncertainty caused by Russia's war of aggression by increasing their inventories. The strong recovery in tourism was also reflected in Finland's services imports during 2022. In 2023, companies are making use of inventories accumulated in the previous year, and the slowdown in the economy will further reduce the need for goods imports. Imports are forecast to decrease by 6.1% in 2023.

In 2024, the outlook for imports will improve, but the recovery will be delayed until the second half of the year. Growing exports will also require an increase in production inputs imported from abroad, and a rise in real incomes will also increase demand for both imported goods and services. Imports are projected grow by 2.4% in 2024. In 2025, imports will grow quickly, as the amount of domestic investments increases. For the end of the outlook period, up to 2026, defence procurements have been made, which will maintain the level of imports. Imports are projected to grow by 4% in 2025 and 3% in 2026.

Finland's goods exports declined sharply in the third quarter of 2023. Weakness in Finland's key European export markets has been more clearly evident towards the end of the year, as the order book, which still supported exports at the beginning of the year, has diminished. In the last quarter, however, a large ship delivery will boost exports. Growth in services exports was also slow in the early part of the year. Exports are expected to contract by 1.3% in 2023.

Domestically, economic activity has declined and order books have fallen in several sectors, leading to expectations of slow development in early 2024. Sector-specific differences are large, however, and in some sectors the outlook for foreign trade has remained good or is improving. Exports will turn to growth in 2024, but faster growth will be delayed until the end of the year. Towards the end of 2024, the trend in exports will be reversed by recovering world trade, and exports are projected to increase by 2% percent in 2024. In addition, Finland's cost competitiveness will remain favourable over the outlook period. From 2025 onwards, the outlook for exports is good, as the effects of the recovery of the global economy are reflected in strong growth of Finnish exports. Exports are projected grow by 3.8% in 2025 and 3% in 2026.

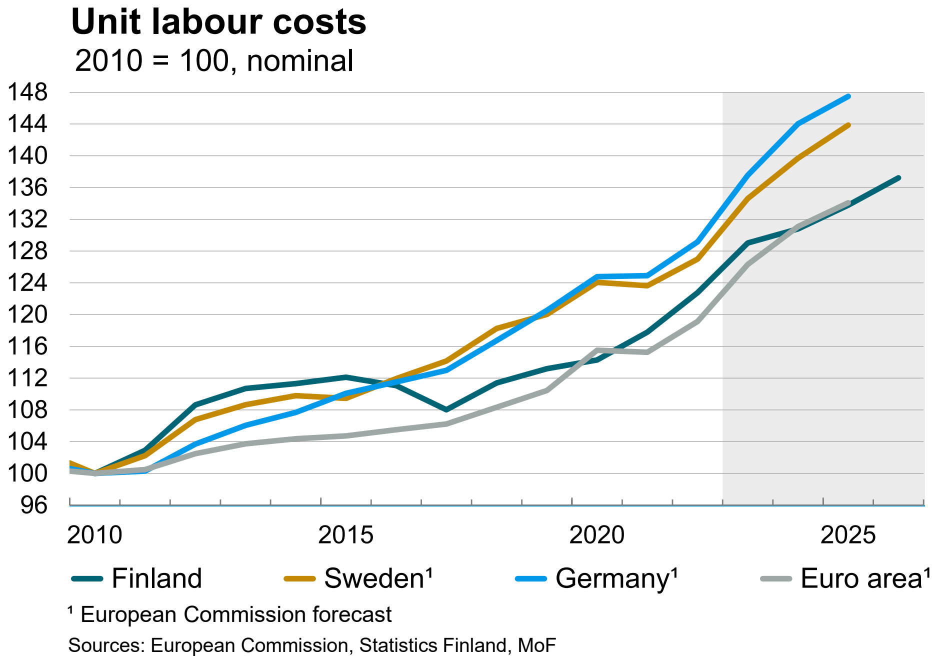


Table 5. Foreign trade

	2021	2022	2023**	2024**	2025**	2026**
	change in volume, %					
Exports of goods and services	5.8	3.7	-1.3	2.0	3.8	3.0
Imports of goods and services	6.0	8.5	-6.1	2.4	4.0	3.0
	change in price, %					
Exports of goods and services	9.8	18.6	-4.3	-1.3	1.6	1.7
Imports of goods and services	9.7	19.4	-3.7	-1.6	1.7	1.7

1.2.2 Prices and current account

Prices in foreign trade of goods rose by an exceptional amount in 2022 after export and import prices of energy and raw materials became significantly more expensive. In 2023, prices in foreign trade of goods fell sharply in the early part of the year, but in the third quarter import prices rose slightly, impacted by the rise seen in energy prices. Prices in foreign trade of services have been more stable and prices have continued to rise in 2023. Import prices will fall by 3.7% and export prices by 4.3% in 2023.

In 2024, the decline in prices will slow and prices will slowly start to rise but, on an annual basis, import prices will fall by 1.6% and the export prices by 1.3%. Prices in foreign trade of services will continue to rise in 2024. In 2025, prices in foreign trade of both goods and services will rise as the global economy and the Finnish economy grow.

In 2023, the trade balance will be in surplus due to a stronger contraction in goods imports than in goods exports. This will also significantly reduce the current account deficit accrued during the previous year. The services account has typically been in deficit, but in 2022 the deficit was higher than in previous years due, among other things, to strong development of tourism imports. From 2023 onwards, this deficit will narrow but will still remain high.

In 2024 and towards the end of the outlook period, the balance of goods and services will remain in deficit. Growth in defence spending and an increase in investments towards the end of the outlook period as well as the persistent deficit in the services account will particularly contribute to this. Primary income, such as investment income, will flow to Finland in net terms in excess of the amount paid abroad, resulting in a primary income account surplus. As in previous years, however, more income transfers will be paid abroad in net terms, as a result of which the factor incomes and income transfers account will remain in deficit. The development of these sub-items impacts the current account in such a way that in 2023 the current account deficit will narrow significantly, to EUR 2.2 billion, having been EUR 6.8 billion in deficit in 2022. In the following years, the deficit will widen again slightly to EUR 2.3 billion in 2024, EUR 2.7 billion in 2025 and EUR 2.8 billion in 2026. The current account to GDP ratio is projected to be -0.8% in 2023 and 2024 and -0.9% in 2025 and 2026.

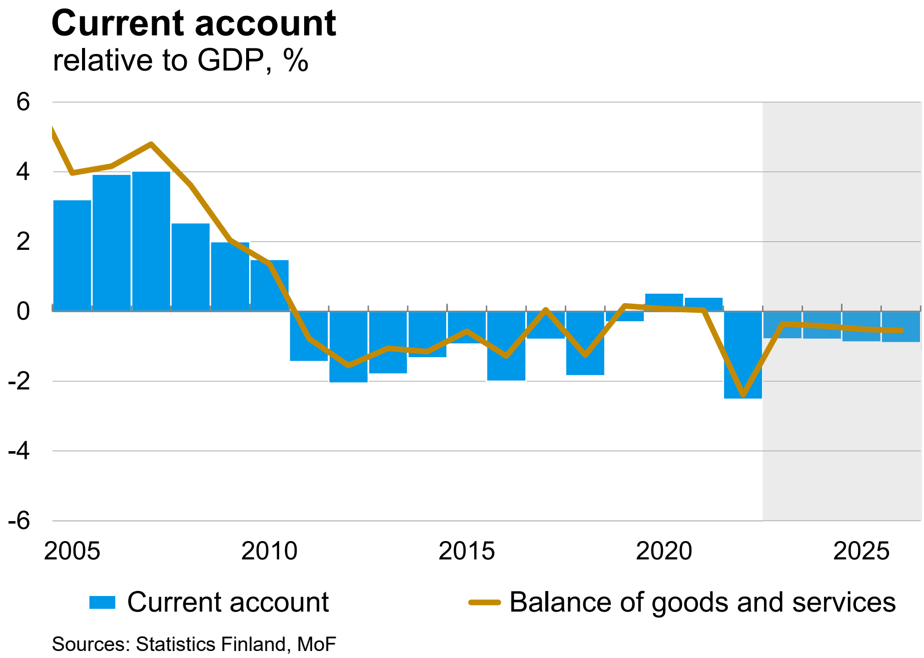


Table 6. Current account

	2021	2022	2023**	2024**	2025**	2026**
	EUR bn					
Balance of goods and services	0.1	-6.4	-1.0	-1.2	-1.5	-1.7
Factor incomes and income transfers, net	1.0	-0.3	-1.2	-1.1	-1.1	-1.1
Current account	1.0	-6.8	-2.2	-2.3	-2.7	-2.8
Current account, relative to GDP, %	0.4	-2.5	-0.8	-0.8	-0.9	-0.9

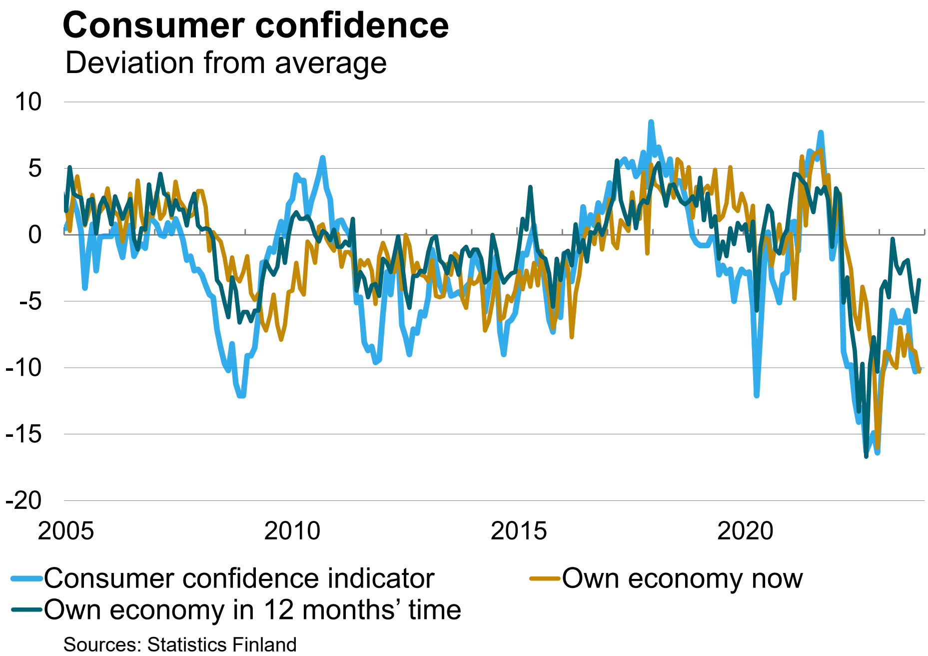
1.3 Domestic demand

1.3.1 Private consumption

In the third quarter of 2023, private consumption fell significantly compared with the previous quarter, and was 1.6% lower than in the corresponding period last year. In addition to the very weak development of the third quarter, Statistics Finland revised consumption for the first and secondquarters of the current year sharply downwards. As a result, the moderate growth in private consumption seen in the national accounts data published at the end of August has turned into a steep decline.

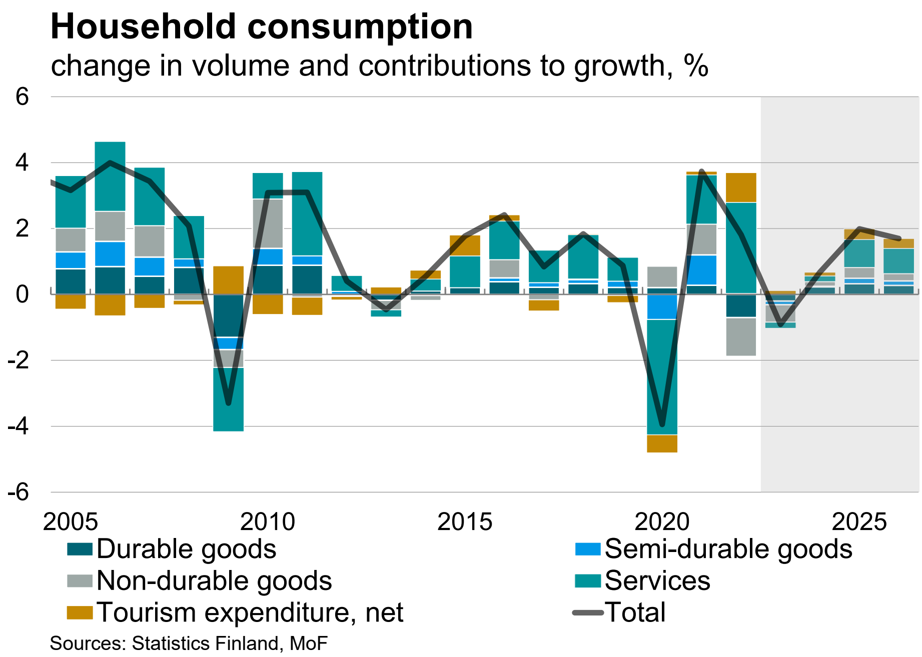
The fall in real household wages has come to a halt in the autumn as inflation has slowed and the lowest income households have benefited from large increases in index-linked income transfers. Despite the rise in the level of interest rates, household incomes exceeded consumption in the early part of the year, which has returned the net savings ratio to positive. Indeed, the sharp drop in household consumption currently seems to be based above all on an exceptionally high level of caution and a lack of confidence, which in turn may be due to anticipation of a deteriorating employment situation. Part of the growth in household incomes has also apparently been directed to, instead of consumption, extra repayments of housing loans, through which households have tried to reduce their interest expenditure.

Total private consumption will decrease by 0.8% in 2023. Low consumption at the end of the year has also negatively impacted the forecast for 2024. Due to a deterioration in the employment situation, growth in real wages will remain at around 1% in 2024. Reductions in the wage tax rate will increase the income of employed persons, but these are partly offset by cuts in social benefits, which will decrease disposable income in low-income households. Private consumption will grow by 0.7% in 2024, but in 2025 private consumption growth will accelerate significantly as interest rates fall and purchasing power increases.



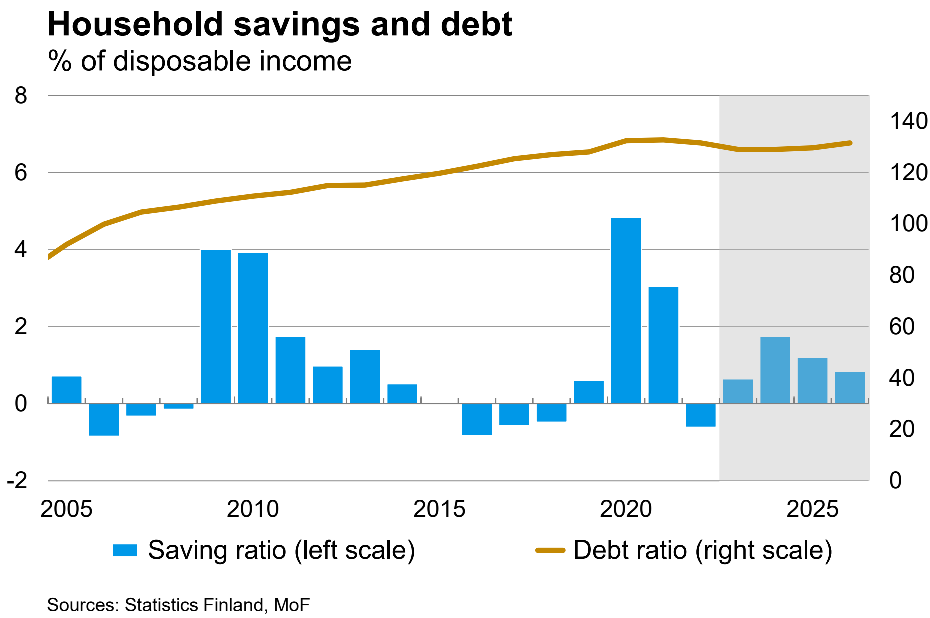
Consumer confidence took a downturn again in October–November. Consumers view Finland's economic situation as particularly gloomy, but the majority of respondents, however, still expect their own financial situation to improve in the next 12 months.

The decline in durables consumption has come to a halt, but consumption will remain at a very low level in 2023, even significantly below the level of 2019. First registrations of cars have remained at a low level. Durables purchasing intentions in the consumer confidence survey were still highly negative in November, which is why growth in durables consumption is not expected to accelerate until later, during 2024.



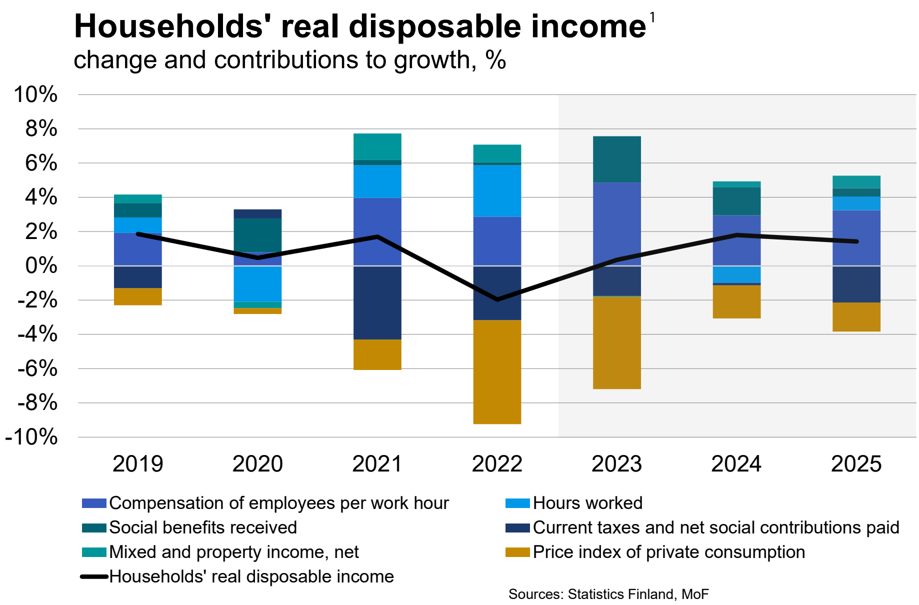
Due to the high price level and negative carry-over effect, non-durables consumption will decline by around 2% in 2023, despite the market price of electricity and fuel prices having now returned to normal levels. As the prices of food and current electricity contracts level off, non-durables consumption will return to growth in 2024.

Services consumption will decline slightly in 2023. Sharp price increases, for example in restaurant services, may have contributed to the slowdown in consumption. In 2024, services consumption will return to growth as purchasing power improves.



The household savings ratio has turned positive in 2023 as disposable income grows faster than consumption. The savings ratio is projected to remain positive also in 2024 as consumer caution curbs consumption growth.

The household debt ratio will fall in 2023 and is not expected to rise in 2024. As employment and confidence improve in 2025, the debt ratio will start to rise again slowly.



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

Real disposable income, which measures the combined purchasing power of households, will turn to growth in 2023 as the rise in private consumption prices slows, average earnings increase and social benefits received grow substantially due to indexation. Interest paid by households is growing strongly but, at the same time, interest income from mutual funds and savings accounts is also rising, resulting in only a slight decline in net property income.

The growth in household purchasing power is projected to accelerate in 2024 and 2025 as inflation slows further. Taxation of wages will decrease in 2024 due to reduction in unemployment insurance contribution. The increase in private consumption prices is projected to slow to around 2% in 2024 and 1.7% in 2025.

Table 7. Consumption

	2022	2021	2022	2023**	2024**	2025**	2026**
	share, %	change in volume, %					
Private consumption	100.0	3.5	1.7	-0.8	0.7	2.0	1.7
Households	95.2	3.7	1.8	-0.9	0.7	2.0	1.7
Durables	7.2	3.1	-7.9	-2.7	3.2	4.6	3.8
Semi-durables	7.2	12.0	0.4	-1.4	0.3	2.4	2.0
Non-durable goods	29.0	3.3	-4.2	-2.1	0.6	1.4	1.0
Services	51.7	2.9	5.6	-0.4	0.4	1.9	1.7
Consumption by non-profit institutions	4.1	-2.7	-1.2	1.0	1.0	1.7	1.7
Public consumption		3.9	0.8	3.0	0.0	0.1	0.3
Total		**3.6**	**1.4**	**0.4**	**0.5**	**1.4**	**1.2**
Private consumption deflator		1.8	6.1	5.4	1.9	1.7	1.9
Public consumption deflator		2.8	4.0	5.6	2.8	3.7	3.4
Households´ disposable income		3.5	4.0	5.8	3.8	3.2	3.2
Households´ real disposable income		1.7	-2.0	0.4	1.8	1.4	1.3
		%					
Consumption in relation to GDP (at current prices)		75.7	75.5	76.1	76.3	75.9	75.7
Household savings ratio		3.0	-0.6	0.6	1.7	1.2	0.8
Household debt ratio[1]		132.7	131.5	129.0	129.0	129.6	131.5

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

1.3.2 Public consumption

The growth rate of public consumption has been relatively brisk in the first three quarters of the year, and is expected to accelerate to 3% in 2023. Consumption expenditure will be increased by, among other things, an increase in age-related expenditure, increased costs of the wellbeing services counties and the rise in defence materiel purchases and immigration-related expenses caused by Russian's war of aggression.

Public consumption growth is projected to remain close to zero in 2024–2026. Growth in consumption expenditure will be curbed by, among other things, the Government's operating expenditure savings, which will continue throughout the parliamentary term. In addition, growth in consumption expenditure will be slowed by permanent adjustment measures of the municipalities and joint municipal authorities as well as the wellbeing services counties, which have been included in the forecast for a total of EUR 400 million from 2024 onwards.

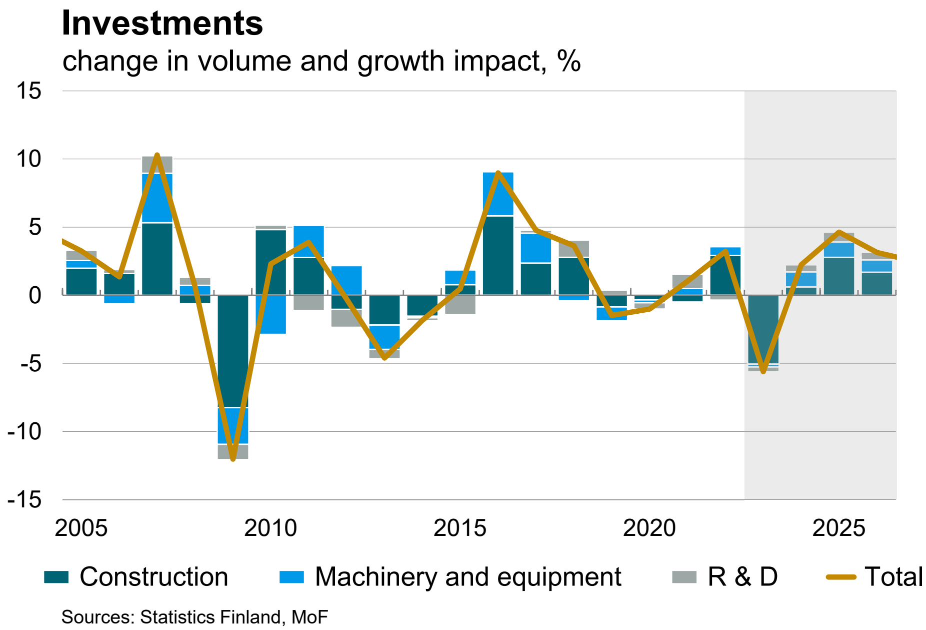
The value of public consumption will be increased during the outlook period particularly by rapidly rising prices. Although inflation is already slowing, the impact of already increased inflation will pass into the price of public consumption in the outlook period, partly due to long-term outsourcing agreements. The development of earnings in the public sector will also be accelerated by the remuneration system development programmes agreed upon for the municipal and wellbeing sectors and the wage harmonisation agreement of the wellbeing services counties.

1.3.3 Investments

Investments will decline by 5.6% in 2023, but will turn to 2.2% growth in 2024. In 2025, investments are projected to return to a stronger growth rate of 4.6%. The overall ratio of investments to GDP will be 23.1% in 2023. The ratio of private investment to GDP will be 19.2% and public investment 3.9%. In 2023, private investment will decline by 5.4% and public investment by 6.6%.

Around half of the investments will be in construction, of which more than half will be residential construction. The decline in investments is mainly due to a decrease in residential construction. For this year, the decrease in residential construction investment will be 9.1% and0.2% next year. The turning point to recovery in construction will be delayed until 2025, even though construction is expected to revive more broadly already in 2024, at least in office construction.

In other investment items, too, volumes will be lower in 2023 than in the previous year.

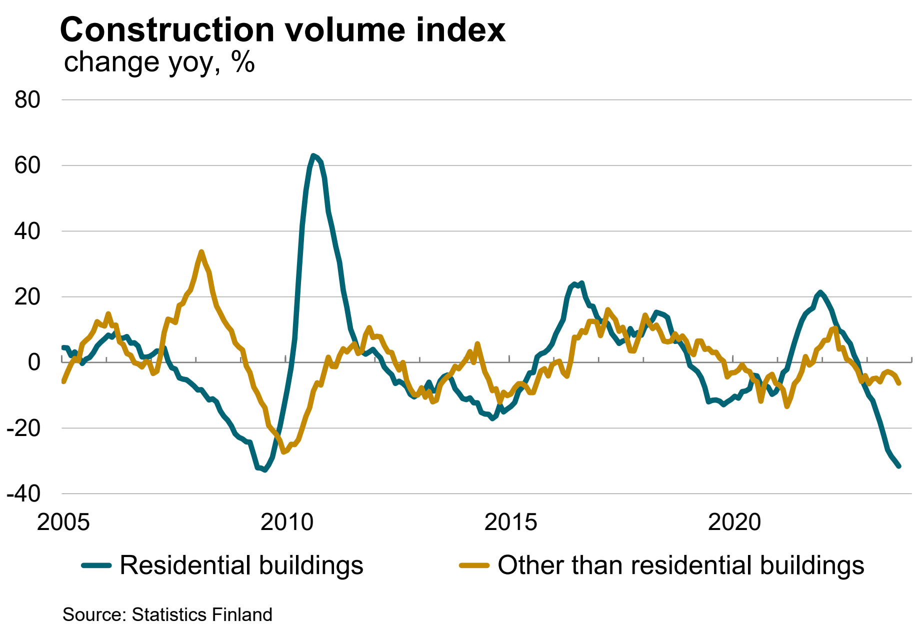


Construction

Residential construction investments will decline in 2023 and 2024. Construction is expected to recover in 2025. A decline of 12% is projected for 2023 and 4% for 2024. The picture of a downturn in residential construction has become clearer during the year, but the previous year's starts have kept construction going. Construction is not expected to remain at a low level once demand returns. Interest rates are expected to start falling, which would boost housing sales, raise house prices and gradually kick-start residential construction. So far, there has not yet been a fall in construction costs that might be assumed from the current market situation. Urbanisation and immigration both sustain the need for housing production. At the end of the outlook period, the number of housing starts will return to a level closer to the long-term average. In 2025 and 2026, residential construction is expected to recover at annual growth rates of 5% and 3% respectively.

In 2022, a start was made on the construction of around 37,000 homes. By September this year, construction of around 20,000 homes had started. Although the statistics on housing starts are likely to be revised downwards, the figure can be used to estimate the number of housing starts for the year as a whole, if starts in the latter part of the year are taken into account. Housing completions are still quite high, with a further 31,000 homes being completed this year. The collapse in demand for new housing sales has increased the number of construction companies' empty new homes.

Measured by cubic volume, the number of permits in July–September 2023 has decreased by 39% in comparison with 2022. In residential construction, the decline has been 50% and in non-residential construction 35%. According to Statistics Finland, the number of building permits has varied from region to region. Most building permits are granted in Uusimaa, Central Finland and North Ostrobothnia, and with regard to the regions, more building permits have been granted to six regions than a year earlier. The slow but steady growth in repair construction will dampen the decline in construction investments and, in the long run, replace new construction. Last year's rise in costs has also adversely affected housing companies' repair construction projects and, exceptionally, the volume of renovation construction is also projected to decrease.



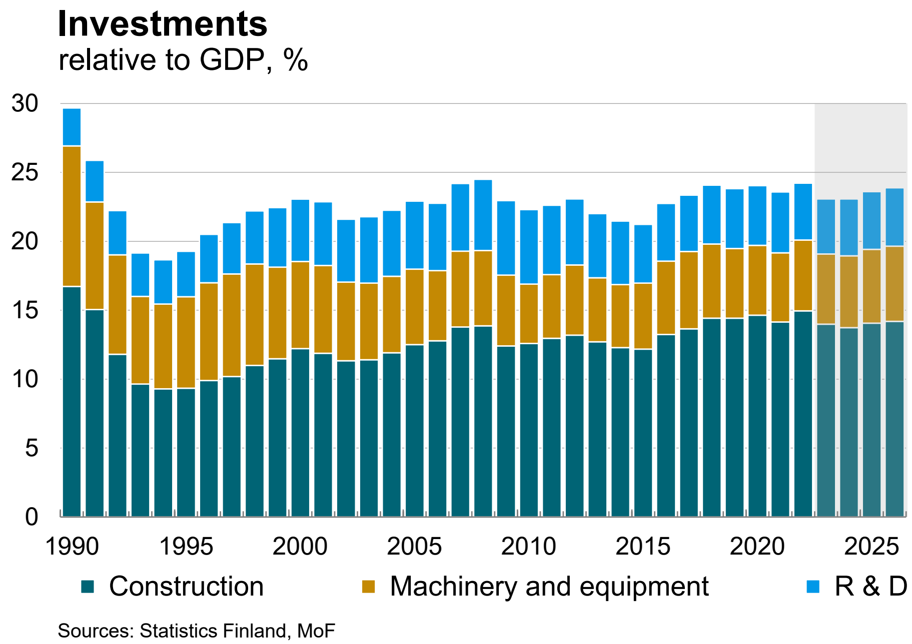
Non-residential building investments will also decline in 2023, but not as much as residential buildings. Non-residential building investments include industrial properties, warehouses and commercial properties. Expectations concerning facilities construction remain more positive than for residential construction, and facilities construction is expected to grow significantly already in 2024. Non-residential building investments are expected to decline by 5% this year and to turn to growth of around 5% in 2024. The growth rates in 2025 and 2026 are projected to be 3% and 2% respectively.

The decline in civil engineering follows other construction, such as foundations for residential areas. In 2022, a significant increase in civil engineering still came from the construction of wind power plants. The construction of wind power plants is continuing, but those areas of civil engineering that are based on residential construction are being postponed. Civil engineering is projected to decline by 4% in 2023 and subsequently recover to annual growth of 6–7% starting from 2024. In the longer term, growth is expected to be around 4%.

Public investments

Although the deficit limits the investment opportunities of general government, the investment ratio is projected to grow. Central government investment will be sustained by the strengthening of cyber security, border control and national defence as well as RRF investment funding. In addition, the Act on Research and Development Funding will substantially increase central government investment from 2024 to 2030. The first deliveries of the Finnish Air Force's multirole fighter aircraft are expected in 2025. This will substantially increase public investment over the previous level.

In local government, investment pressure will continue due to population migration and the repair backlog of the building stock. Investment pressures for healthcare and social welfare investment projects are considerable, but increased costs and financing costs will slow down investment. The finances of the municipalities and wellbeing services counties are tighter than expected. Decisions of the new Government may have a significant impact on the development of public investment in the coming years.



Machinery and equipment investments have held up well, even though production has fallen, the utilisation rate is quite low and the rise in interest rates has increased investment costs. Despite the challenging short-term outlook, expectations for production investments are positive. Finland's cost competitiveness is good, and investment is supported, in particular, by lower energy costs than the rest of Europe. Companies also have large investment needs in the next few years. In addition to climate change and the energy transition, ever-advancing digitalisation and the use of artificial intelligence will increase machinery and equipment investments.

According to the Confederation of Finnish Industries' monitoring of green transition investment plans, there are plans amounting to more than EUR 200 billion in inland. While it is likely that most of these plans will not be realised, the volume of investment plans is at a substantially higher level than usual. If implemented, most of the investments would take place towards the end of the decade, but wind power, battery, hydrogen and biorefinery investments, in particular, are coming and are planned for the next few years.

R&D investments as well as software and database investments will decline for the second year in a row in 2023 after very rapid growth in 2021. Nevertheless, the growth of R&D investments in the coming years is supported by the parliamentary target of raising Finnish R&D funding to 4% of GDP by 2030. Investments will be increased by the measures related to this target, including the tax deduction for R&D expenditure that entered into effect at the beginning of 2023 as well as financial support and loans under the EU's Recovery and Resilience Facility. R&D activity is also increased by the development of technology, which is changing production methods in many fields and requires investment in R&D.

Table 8. Fixed investment by type of capital asset

	2022	2021	2022	2023**	2024**	2025**	2026**
	share, %	change in volume, %					
Buildings	50.5	-0.5	2.0	-9.1	-0.2	4.1	2.6
Residential buildings	29.6	2.8	1.7	-12.0	-4.0	5.0	3.0
Non-residential buildings	20.9	-4.8	2.5	-5.0	5.0	3.0	2.0
Civil engineering construction	11.2	-2.4	20.1	-4.0	6.0	7.0	4.0
Machinery and equipment	21.2	2.4	3.0	-1.0	5.0	5.0	4.0
R&D-investments[1]	17.1	5.7	-1.8	-2.0	3.0	4.0	3.0
Total	**100.0**	**1.0**	**3.2**	**-5.6**	**2.2**	**4.6**	**3.1**
Private	83.0	4.3	4.0	-5.4	0.9	2.9	4.2
Public	17.0	-11.8	-0.2	-6.6	9.0	12.5	-1.3
Investment deflator	6.5	2.3	6.5	5.9	0.2	2.0	2.0
		%					
Investment to GDP ratio (at current prices)							
Fixed investment		23.6	24.2	23.1	23.1	23.6	23.9
Private		19.4	20.1	19.2	19.0	19.1	19.5
Public		4.2	4.1	3.9	4.1	4.5	4.4

[1] Includes cultivated assets and intellectual property products

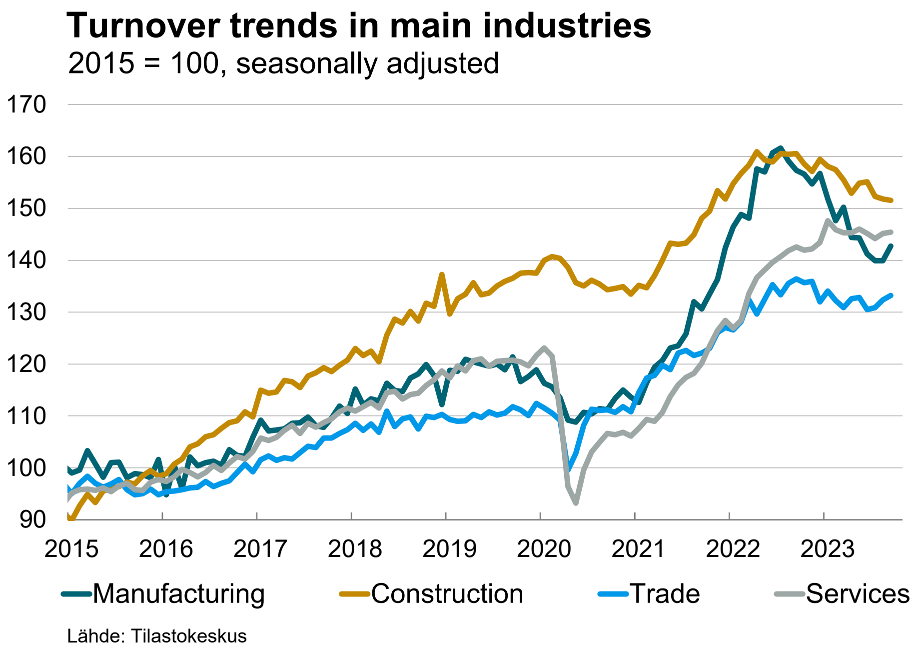
1.4 Domestic production

1.4.1 Total output

The value added generated by the industries will not increase this year, and growth in 2024 will continue to be subdued. For 2023, however, the development of value added has been more positive than when measured in terms of GDP, as product taxes relative to the size of the economy have decreased, which is reflected in the fact that in 2023 the development of value added will be close to zero, while GDP will fall by 0.5%.

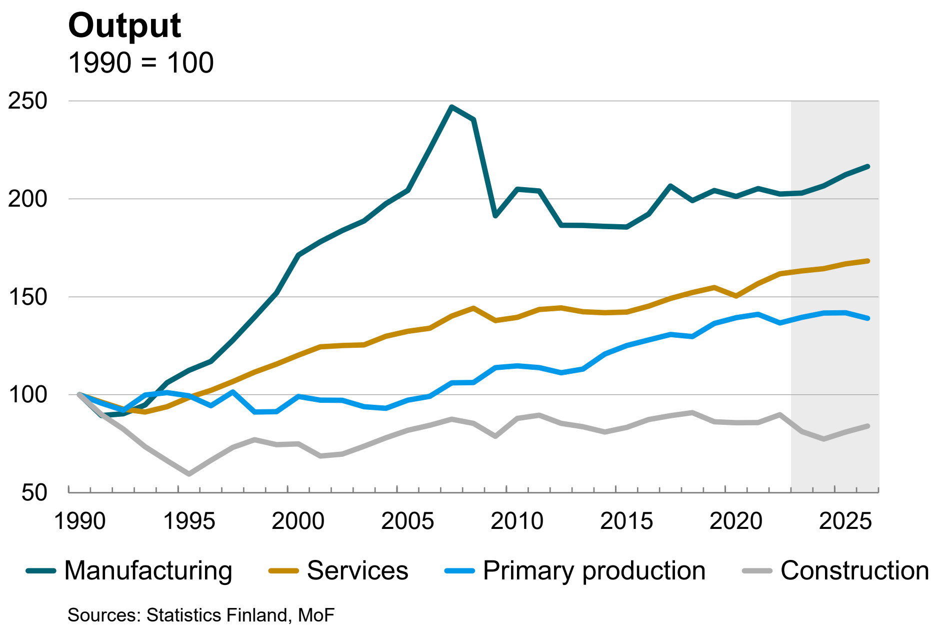
In the first two quarters of 2023, the value added grew by 0.3% and 0.6% compared with the previous quarters, according to revised figures from Statistics Finland. The 0.9% decline in the third quarter brought value added volume back to the level of the end of last year, and a further drop is expected in the fourth quarter, which means a recession for the latter part of the year.

In 2024, growth is expected to revive slowly and export demand to recover. For 2024, value added is projected to grow by 0.6%, slightly behind growth of total output. Product taxes are expected to increase again in real terms. The recovery in demand from 2025 will boost output not only in exports but also in construction and supporting services and in domestic production. For 2025, value added is expected to grow at a rate of around 2%, and in 2026 it will approach its longer-term potential of around 1.5%.



Most industries have seen a turnaround in both expectations and production volumes in 2023. The exception to this has been construction, where production levels have been falling since last year. In the first two quarters of the year, growth was seen in a number of industrial sectors, and in the second quarter production increased in nearly all service sectors. The start of the year was also promising for primary production in agriculture.

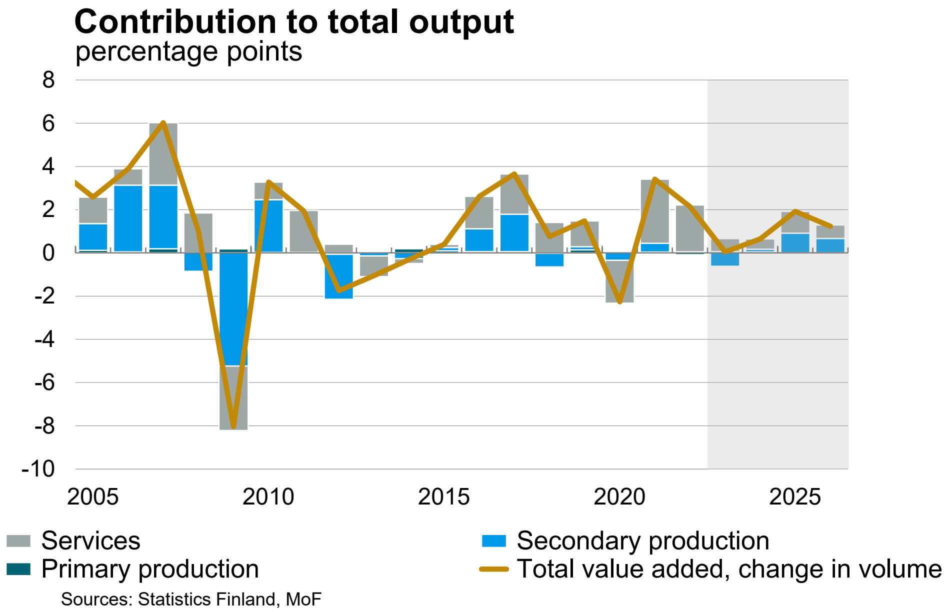
In the latter half of 2023, the decline in service production has been largely due to the decline in construction. In a number of service sectors, such as information and communication services as well as financial services, output has fallen. The same trend is expected to continue for the rest of the year.



In primary production, forestry production will decline as the use of wood in construction and the forest industry decreases. Climate policy targets are also expected to affect the amount of felling in the forestry sector, although there is still uncertainty about the timing of the turnaround. The reduction in wood imports from Russia has maintained the need for felling. In agriculture, data on production values vary significantly and is subject to considerable uncertainty.

Industry is project to grow by 2.8% and 1.9% in 2025 and 2026. Construction is expected to recover to 4.5% in 2025 and 3.8% in 2026. Service production will grow by 1.5% in 2025 and 0.9% in 2026. Although there are signs of a contraction in primary production, the figures for the early part of the year have been so promising that they point to growth for the year as a whole. Primary production is projected to grow by 1.6% in 2024, 0.1% in 2025 and decline by 2% in 2026.

Service production continues to support the creation of value added in the economy. It has grown in significance in exports, and around 70% of the value added of the entire economy is generated in services. The decline in construction is also reflected in service production, particularly in information and communication services, the financial sector and other business services. Continued uncertainty in Finland's main export markets, especially Germany and Sweden, has an impact, particularly on energy-intensive sectors such as the chemical industry and the energy supply industry. In the export industry, the outlook is stabilising with regard to price levels, and raw material prices are expected to take a downturn.



1.4.2 Secondary production

Secondary production includes mining and construction in addition to industry. In addition to manufacturing, industry also includes heat and electricity supply and other energy production as well as waste management. In manufacturing, the largest export industries are the forest industry, the chemical industry, the metal industry, and the electrical and electronics industry, which according to the Standard Industrial Classification TOL include several sub-industries, but together they account for more than 60% of Finnish exports.

The declining economic conditions have been reflected in the order books of manufacturing, i.e. export industries. Order volumes have declined since late 2022 if changes are measured by moving averages, which would be predictive of a decline in output. Production volume indices also show a decline, but rapid changes in orders and volume are typical of monthly observations. The economic situation for industry is also negative in terms of expectations, although a small recovery of output is also perceptible. The decline from last year's peak expectations has been rapid and steep.

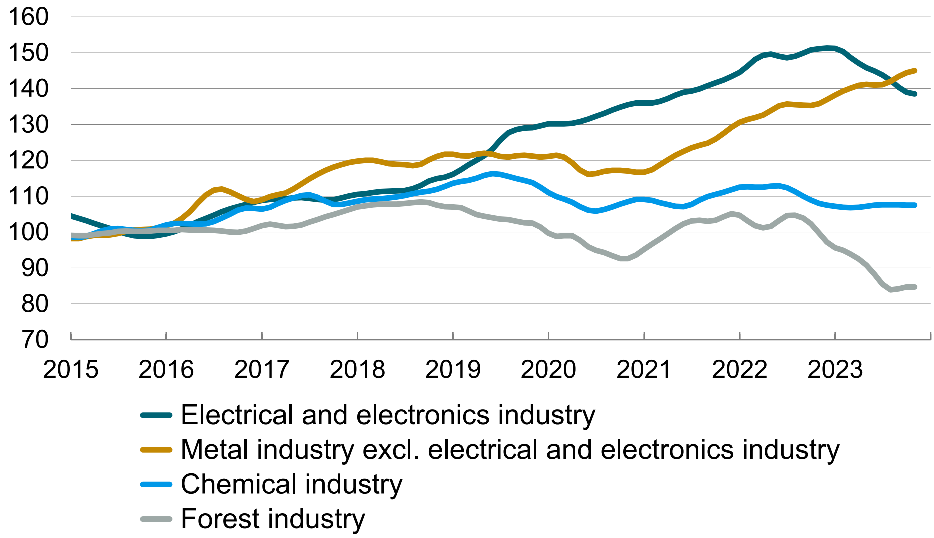
The forest industry is suffering from a weak export outlook and high costs. On the other hand, capacity has been increased at Kemi and Äänekoski, and production is expected to grow next year. The operations of sawmills are also affected by the decline in construction. The main export market for the forest industry is Europe, and Germany in particular. China is also an important export market for pulp. The price level of pulp has fallen sharply, but has already taken an upward turn again. Moreover, the export price for pulp remains at a high level.

Order books in the chemical industry have returned closer to normal levels after several peak years, which explains the falls in production levels in recent quarters. The outlook for the chemical industry follows, on the one hand, the outlook for exports and, on the other, the outlook for the domestic forest industry. Export prices rose until late last year but turned to a decline this year. Higher energy prices affect the chemical industry due to its energy-intensive nature, and expectations in other industries have a direct impact on the industry. The economic expectations in the industry are negative for this year.

In the metal industry, including metal refining and the machinery and metal products industry, production growth has levelled off and order volumes have begun to decline. The electrical and electronics industry is also an important export sector. Last year, the industry was still growing well, but this year the industry has seen a decline in the value added of production throughout the early part of the year.

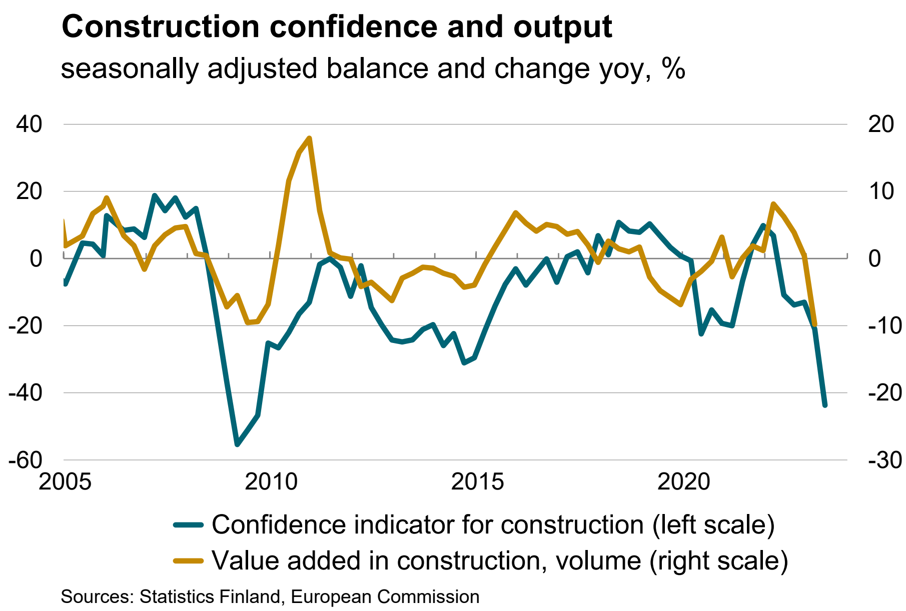
Volume index for industrial production

2015 = 100, trend



Source: Statistics Finland

Construction has been declining since the end of last year. In 2023, production will still reflect starts made in 2022, and the decline in production is expected to continue into 2024. Business Tendency Survey indicators in the construction industry have fallen sharply and confidence indicators are at financial crisis levels.



1.4.3 Services

In 2023, production in most service industries has contracted after the second quarter. According to the quarterly national accounts, service production grew by 0.8% and 0.4% in the first two quarters and declined by 1.1% in the third quarter. This is strongly driving the development of value-added as a whole.

For a long time, the level of service production has kept production at a reasonable level. It is only at the end of this year that expectations in service production have also deteriorated. The trade sector has been growing in the second quarter and transport has also seen growth for two consecutive quarters. Growth is evident in the retail sector, and services are expected to grow at wide range, albeit low rate in the next few years. In the transport sector, the level of production has clearly fallen since the pandemic. Production in the tourism and restaurant sector is still recovering from the decline caused by COVID-19.

According to the Business Tendency Survey, the service sectors expect sales to remain at the current level for the next six months. Demand has also declined in the service sectors, which adds to the previous factors constraining growth i.e production bottlenecks through the lack of skilled labour.

In 2023, service production is expected to grow by 0.9%, which is clearly less than previous estimates, but still cautiously positive. In 2024, services are expected to grow by 0.7%, which is less than normal. In 2024 and 2025, growth is projected to be 1.5% and 0.9% respectively.

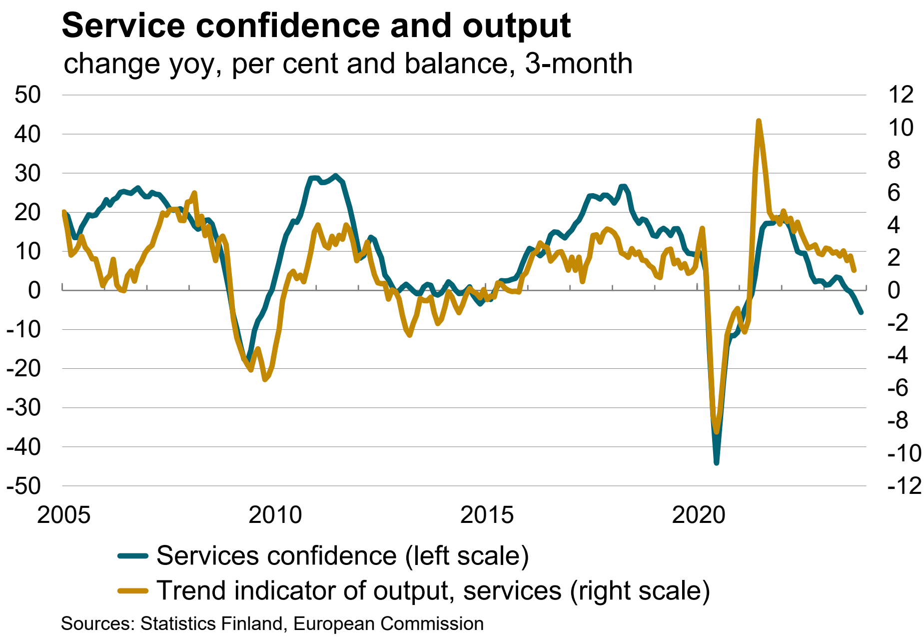


Table 9. Production by industry

	2022	2021	2022	2023**	2024**	2025**	2026**
	share, %[1]	change in volume, %					
Industry	22.4	2.0	-1.3	0.2	1.8	2.8	1.9
Construction	7.0	0.1	4.6	-9.6	-4.7	4.6	3.8
Agriculture and forestry	2.6	1.2	-3.1	2.1	1.6	0.1	-2.0
Industry and construction	29.4	1.5	0.2	-2.1	0.4	3.2	2.3
Services	68.0	4.3	3.2	0.9	0.7	1.5	0.9
Total production at basic prices	**100.0**	**3.4**	**2.2**	**0.0**	**0.6**	**2.1**	**1.5**
GDP at market prices		3.2	1.6	-0.5	0.7	2.0	1.6
Labour productivity in the whole economy		1.4	0.0	0.0	1.7	1.3	0.7

[1] Share of total value added at current prices

Emissions on a downward path due to technology

Finland's Climate Act targets net zero by 2035. This means that anthropogenic greenhouse gas emissions decrease and removals by sinks increase so that, at the latest by 2035, Finland has reached a situation where its greenhouse gas emissions are at most equal to the removals. Greenhouse gases include for instance carbon dioxide, methane and hydrofluorocarbons.

Greenhouse gases are generated in many economic activities. For example, carbon dioxide is produced from the use of fossil fuels in industry, and methane from animals in agricultural production. To reach the climate targets, the economy needs to undergo structural change. This will require industries of the economy to change their activities towards lower emissions, or industries to disappear and new ones to emerge. In economic production, emissions decrease for two reasons: 1) as greenhouse gas emission intensity decreases, for example through lower-emission technology, and 2) as economic activity decreases in emission-intensive sectors. Emission intensity is the amount of emissions generated per unit of value added produced.

This box examines how Finland's production-based emissions will change in 2022-2026. The analysis therefore includes emissions other than direct emissions from households, which are generated particularly in transport and in building-specific heating.

Methodology

The Ministry of Finance's domestic production forecast as well as Statistics Finland's air emission accounts[1] and the national accounts are used in the analysis.

For each industry in the forecast, the emission intensity for 2010–2021 is calculated by dividing the sector's emissions by the sector's gross value added at constant prices. Emission intensity is projected for 2022–2026 using an approximation based on linear regression. Once the emission intensity has been estimated, it can be multiplied by economic activity, i.e. the volume of value added in the forecast period. This gives an estimate of how emissions will develop in the future.

The calculation does not address the reasons for the decrease in emission intensity in each industry. Technological development, however, may shed some light on this. Many industrial sectors have invested in lower-emission technology and improved their energy efficiency. This means they can continue to produce the same amount of products with lower emissions. This analysis therefore assumes that technological development will be similar to that between 2010 and 2021. If the forecast were to be extended to Finland's net zero target for 2035, the development of various technologies would have to be evaluated more precisely.

On the other hand, if emission intensity does not decrease fast enough, emissions may rise due to increased activity in an industry. During the transition, economic activity in some industries may also decline as consumers shift their consumption habits towards lower-emission products and demand moves from one industry to another. For more details on the industry forecast, see section 1.4.

The review also does not take a position on future policy changes that could accelerate or slow down the decrease in emission intensity or the green transition more generally.

Results

Emission intensities for the main industries are on a downward path in the period 2010–2021 and therefore the forecast for emission intensity also shows a downward trend. The change in the value added of production is projected to be zero or positive in 2023–2026.

Production emissions are projected to decrease over the review period (Chart 1). Total production emissions in 2026 are expected to be around 33 million tonnes carbon dioxide equivalent.[2]

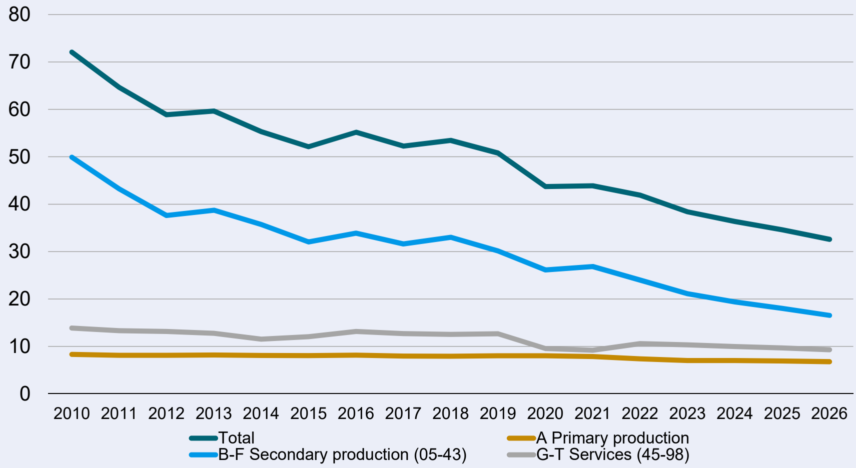
Examining the change by industry, the largest decrease in emissions is from secondary production (industries B-F). Industrial emissions reductions have been driven, in particular, by EU emissions trading system, which has set a price for emissions and thus encouraged sectors to develop lower-emission solutions. In industry, emission reductions come particularly from the reduction in energy supply emissions. In addition to industry, secondary production also includes construction, whose emission intensity has remained nearly constant.

Emissions from services (industries G-T) are on a slightly downward path. Historically, changes in emissions from services have been driven, in particular, by the transport industry. For example, in the coronavirus years 2020 and 2021, emissions from services decreased as emissions from transport services declined. The emission intensity of services is low (Chart 2).

Emissions from primary production (industry A) are on a slightly downward path. Emissions from primary production did not decrease significantly in 2010–2021, and therefore a similarly cautious trend over the review period is assumed in this analysis. Of the main industries, primary production has the highest emission intensity (Chart 2).

Chart 1. Production emissions forecast

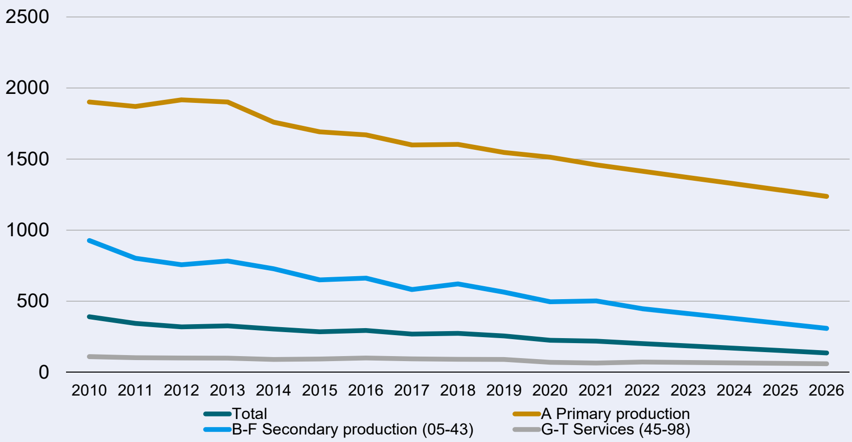
Greenhouse gases, CO2 eq., million tonnes



Sources: Statistics Finland, MoF

Chart 2. Emission intensities

Amount of emissions generated per unit of value added produced, CO2 eq., tonnes/million euros

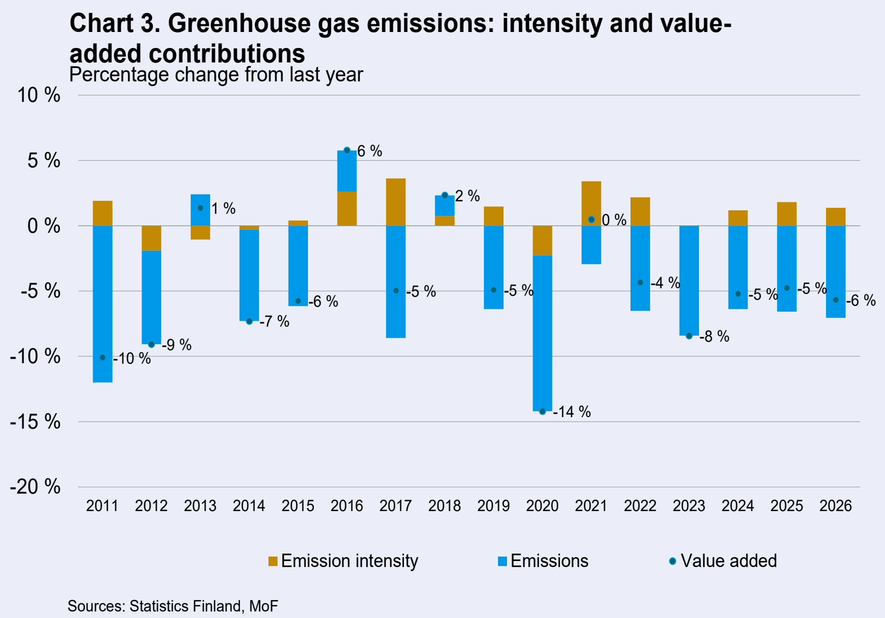


Sources: Statistics Finland, MoF

The value added of production was on an upward path in the period 2010–2021. At the same time, however, greenhouse gas emissions from production have fallen.[3] Chart 3 breaks down the emission changes into two components: 1) value added and 2) emission intensity of production.

The chart shows that the emissions forecast is driven mainly by a decline in emission intensity. This is particularly pronounced in industry. In primary production, the amount of value added is, in contrast, more significant than the change in emission intensity, as the emission intensity of primary production did not decline significantly in 2010–2021.

The decline in emission intensity may be assumed to be longer-term, as investments in new technology will be made for years to come. There is uncertainty about this, however: whether the current technological development will continue, slow down or accelerate. On the other hand, in the short term, the amount of value added of production has an impact. If production experiences a boom, this may increase Finland's emissions, at least in the short term.



Only emissions from production are taken into account in this analysis. Direct emissions from households, such as transport and building-specific heating, are not included in the results. The total emissions of households were 5.3 million tonnes carbon dioxide equivalent and of production 44 million tonnes carbon dioxide equivalent in 2021. The larger part of household emissions, 4.2 million tonnes, came from transport. Between 2010 and 2021, household emissions fell by 2.5 million tonnes, while the population grew by over 3%.

Closing words

Finland’s greenhouse gas emissions are on a downward path. Finland's emission reductions are driven mainly by a decrease in emission intensity. Economic activity is significant, however, particularly in the short term. Shifting production to low-emission-intensity industries, such as services and high-technology products, would help achieve emissions targets. Shifting towards high value-added sectors also supports the Finnish economy.

[1] The total emissions correspond to the emissions included in Finland’s greenhouse gas inventory to which the emissions of Finnish economic units abroad have been added and from which the emissions of foreign economic units in the Finnish territory have been subtracted (https://stat.fi/tilasto/dokumentaatio/tilma)

[2] Carbon dioxide equivalent describes the combined global warming effect of various greenhouse gas emissions.

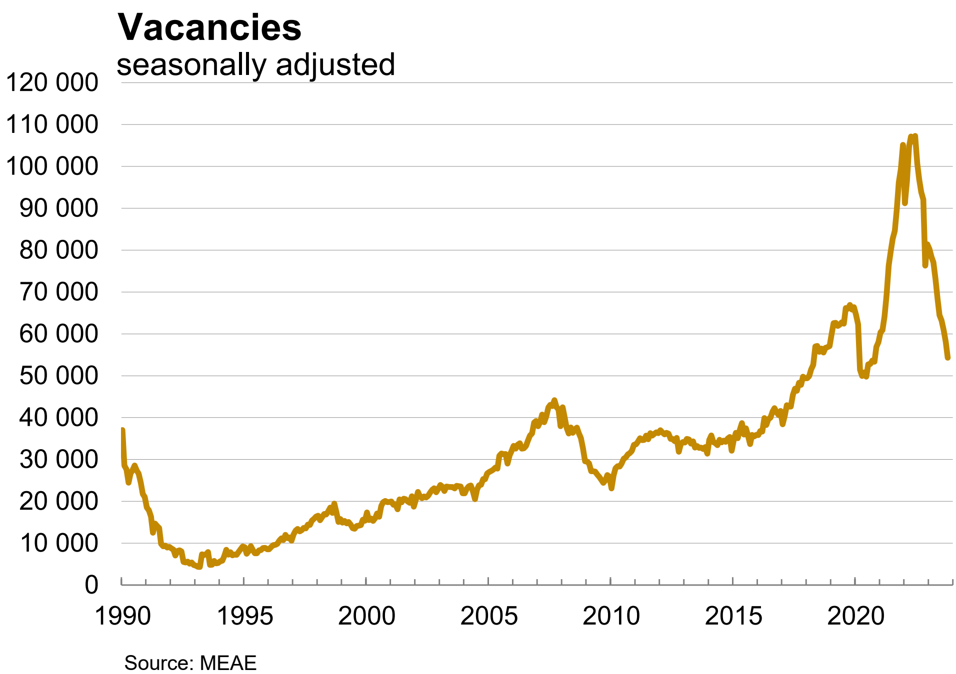
[3] There has been a “decoupling”, in which emissions decrease even as production increases.

1.5 Labour force

Employment will fall temporarily from its peak level. The number of employed people will level off in 2023 and the employment rate will fall slightly. The turnaround in the labour market took place in the summer and autumn. There have been fewer employed people than last year, particularly in the private sector, as the number of vacancies has decreased. In addition, many people, particularly men, have exited the workforce. Due to the positive trend in the early part of the year, the number of employed people in 2023 will still be 0.1% higher on average than in the previous year, but the number of hours worked will no longer increase. In addition, the employment rate will fall from 2022, as the increase in the number of people of working age in 2023 will be the most for 13 years due to substantial immigration.

In 2024, the number of employed people will temporarily decline as demand for labour will be weak due to the economic downturn. Businesses plan to employ significantly fewer people around the turn of the year, particularly in construction and industry. The general shortage of skilled labour motivates companies to hold on to their employees, as the recession is expected to be short-lived, and it is likely that employers will elect to use temporary lay-offs and other labour flexibility solutions instead of redundancies. The economy is expected to recover towards the end of the year, while employment, particularly in services, will also recover. In 2024, the number of employed people will therefore be only 0.2% fewer than in 2023 and the employment rate will remain at the same level. In construction, the number of employed people will still be lower than in 2023. The fall in employment and the high number of temporary lay-offs will result in a clear reduction in the number of hours worked across the economy as a whole.

In 2025 and 2026, economic growth will be quite strong, with employment increasing by nearly 1% per year. Employment growth will be broad-based and underpinned by the Government's measures to increase labour supply, the first of which will take effect in 2024. The forecast includes measures that will be decided in the parliament during 2023. The employment rate for people aged 15–64 will reach nearly 75%, the highest in decades.



The number of unemployed people already started to increase in spring 2023, with unemployment among men, in particular, increasing more than among women. The rise in unemployment will continue in the latter part of 2023 and to some extent in 2024. The contraction of construction activity, in particular, will increase unemployment in 2023 and 2024. The unemployment rate will rise to 7.5% in 2024.

The turnaround in the economy and employment in 2025 and 2026 will reduce unemployment, but the competence requirements of a skilled labour force will slow the fall in unemployment. In 2026, the unemployment rate will remain at around 6.5%, which 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.

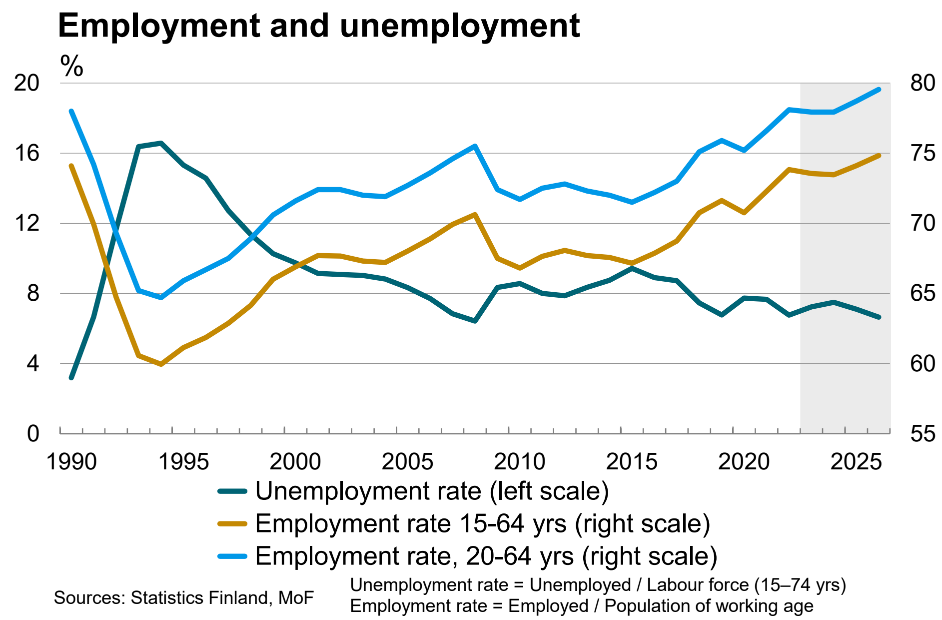


Table 10. Labour market

	2021	2022	2023**	2024**	2025**	2026**
	annual average, 1,000 persons					
Population of working age (15–74 yrs)	4123	4120	4129	4119	4112	4107
Population of working age (15–64 yrs)	3417	3421	3439	3438	3437	3435
Labour force (15–74 yrs)	2765	2808	2827	2831	2843	2855
Employed (15–74 yrs)	2555	2619	2623	2619	2641	2665
of which 15–64 yrs	2470	2526	2530	2526	2547	2571
Unemployed (15–74 yrs)	212	190	205	212	202	190
	change in volume, 1,000 persons					
Population of working age (15–64 yrs)	-3	4	18	-1	-1	-2
Employed (15–64 yrs)	50	56	4	-4	21	23
	%					
Employment rate (15–64 yrs)	72.3	73.8	73.6	73.5	74.1	74.8
Employment rate (20–64 yrs)	76.6	78.1	77.9	77.9	78.7	79.5
Unemployment rate (15–74 yrs)	7.7	6.8	7.2	7.5	7.1	6.6
	1,000 persons per annum					
Immigration, net	23	34	55	50	25	25

1.6 Income, costs and prices

1.6.1 Wages and salaries

The decline in real incomes is starting to be over. The rate of increase in nominal wages will accelerate to just over 4% in 2023. The acceleration was due to higher negotiated wages, as wage drifts decreased. The rise in negotiated wages accelerated substantially in the municipal sector in particular, but negotiated wages were also higher than in the previous year in other public and private sector industries. The rate of increase in earnings accelerated to a significant degree particularly in real estate services, insurance services and healthcare services, while the rate of increase in earnings in secondary production accelerated only slightly. Real wages decline in 2023 by around 2% year-on-year as inflation still substantially exceeded the rate of increase of nominal wages. The level of real earnings, however, no longer declined in the third quarter compared to the early part of the year.

Many two-year collective agreements have been signed in the private sector and the public sector in 2023. The negotiated increases this year have been generally around 4.5% at the annual level, making them substantially higher than in the previous year and the highest in 14 years. The negotiated increases in the municipal and wellbeing sector exceed that level because, in addition to wage increases in line with the general wage increases across the economy, theosts associated with the wage structure programme and wage harmonisation. This makes the local government sector the pay leader of this round of negotiations. Wage drifts are projected to be approximately half a percentage point across the entire economy.

In 2024, the annual effect of the negotiated increases will be approximately 1.5%, as the one-off payments made the previous year will no longer be included in the agreements. In addition, earnings will be increased by wage drift. In many sectors, the timing of negotiated increases will be earlier than in 2023. In the local government sector, the increases will also be substantially higher in 2024. Due to the weakness of the economy, wage drifts are not projected to be larger than average. The combined effect of negotiated increases, wage drifts and earnings carry-over effect will be to raise nominal earnings in 2024 by 3.5% on average across the economy.

As there are not yet many collective agreements in effect for 2025 and 2026, the assumption of increased real earnings across the entire economy is linked to the projected modest growth in productivity. Significant wage increases will continue in the local government sector in 2025. Nominal earnings are projected to increase by just over 3% annually in 2025 and 2026.

The sum of wages and salaries will increase by 5% in 2023. The sum of wages and salaries will be increased by higher earnings, higher performance bonuses and higher employment. The sum of wages and salaries will rise fastest in the public sector, also reflecting growth of employment there. In the private sector, the sum of wages and salaries will also increase quickly particularly in sectors that were previously hard-hit by the pandemic and in industries that serve the business sector. In the construction industry, the sum of wages and salaries will decrease due to the declining number of employed people.

In addition to nominal earnings, the sum of wages and salaries is also affected by the overall development of employment and its reallocation between industries. With employment contracting, the sum of wages and salaries is projected to increase by around 3% in 2024, and it is assumed that the rate of increase in nominal earnings will slow. In the 2025 and 2025, the rate of earnings growth is projected to slow while employment growth accelerates, which would mean that the sum of wages and salaries will increase by just over 4% annually in 2024 and 2025.

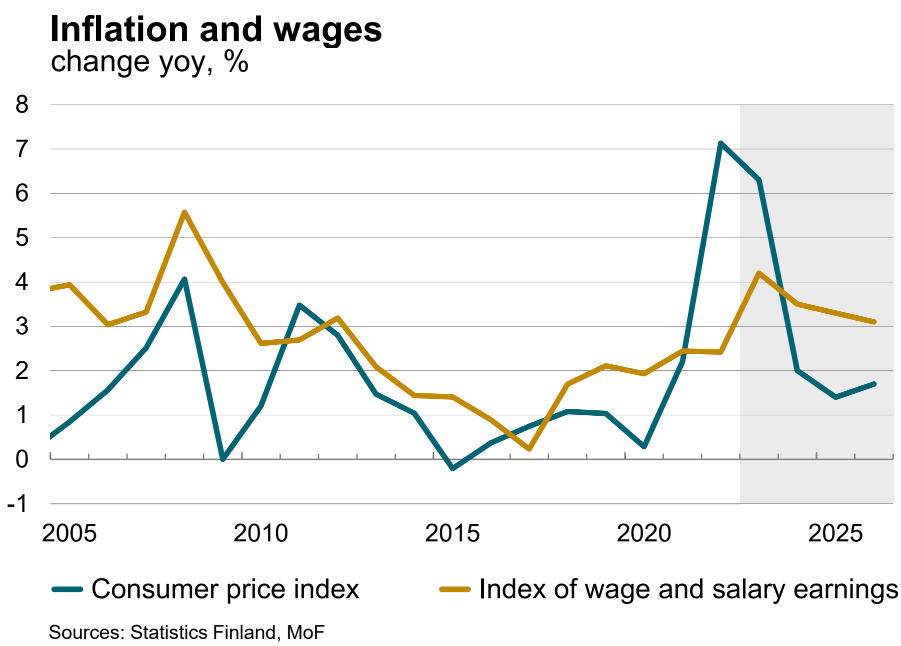
Table 11. Index of wage and salary earnings and labour costs per unit of output

	2021	2022	2023**	2024**	2025**	2026**
	change, %					
Index of negotiated wage rates	1.8	1.8	3.9	2.8	2.6	2.4
Wage drift, etc.	0.7	0.6	0.3	0.7	0.7	0.7
Index of wage and salary earnings	**2.4**	**2.4**	**4.2**	**3.5**	**3.3**	**3.1**
Real earnings[1]	0.2	-4.7	-2.1	1.5	1.9	1.4
Sum of wages and salaries	5.5	6.4	5.0	3.0	4.2	4.1
Average earnings[2]	3.5	3.3	5.0	4.1	3.4	3.3
Labour costs per unit of output whole economy[3]	3.1	4.2	5.1	1.4	2.3	2.6

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.

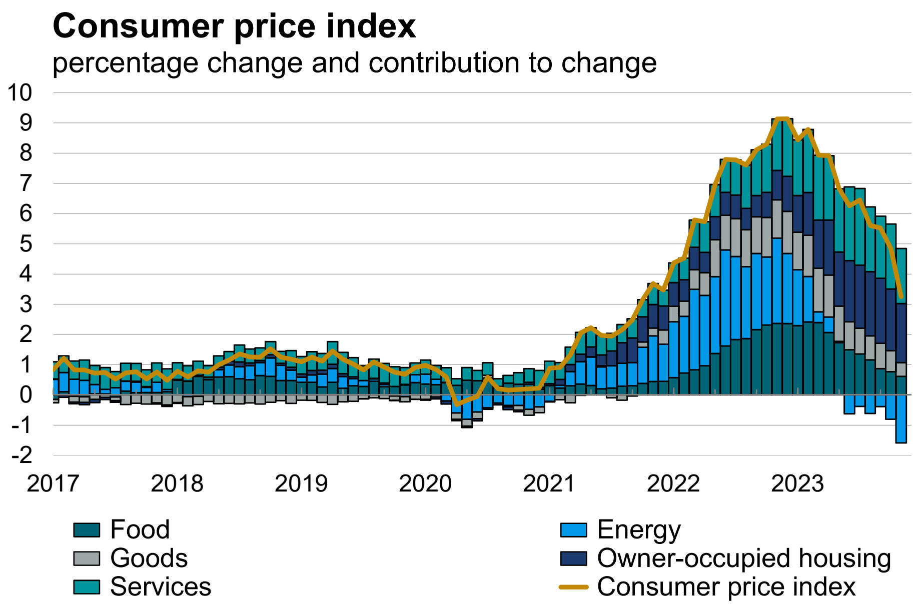
3 Compensation of employees divided by gross value added in volume at basic prices.



1.6.2 Consumer prices

Inflation has slowed rapidly in 2023. In November, inflation as measured by the Harmonised Index of Consumer Prices (HICP) was below 1%, i.e. the slowest since early 2021, even though it was still around 8% at the beginning of the year. Inflation measured by the national Consumer Price Index (CPI) has also slowed down considerably. The CPI, however, also includes interest rates on housing loans and consumer credit, which is why its deceleration has been slower than the HICP as interest rates have risen. In other words, the cost of living has risen more in the current year for those who have a housing loan.

The main reason for the slowing of inflation has been the fall in energy prices. However, the slowing is broad-based, which is also reflected in a easing of core inflation. Nevertheless, prices will remain above the pre-energy crisis level.



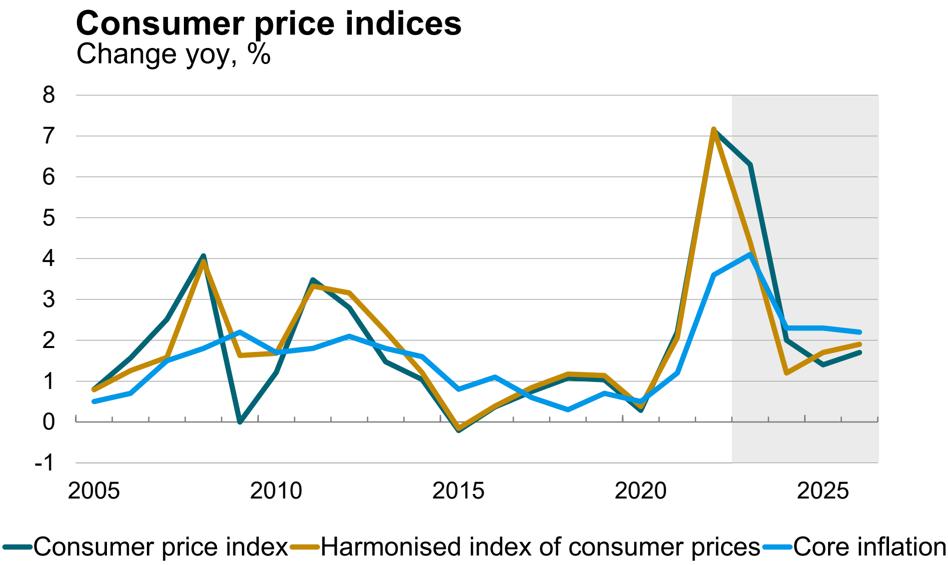
Sources: Statistics Finland

The effect of energy on inflation will remain negative for the next few years. This is mainly due to a fall in the consumer price of electricity, but the market also expects oil prices to fall over the outlook period. In addition to market developments, the energy price forecast is influenced by the level adjustment made to the price index of electricity by Statistics Finland in August, which technically reduces inflation until July 2024. In all, energy prices will decline by around 7% on average in 2024, with a further decline of around 2% expected in 2025.

The annual change in food prices has slowed rapidly, and the rise is the slowest in the entire euro area. Moreover, the slowing of the rise in producer prices is also being reflected to an increasing extent in the prices of processed food products, and the overall rise in food prices will slow further during the first half of 2024. According to companies' sales price expectations, a higher proportion of companies in food industry intend to cut prices over the next 3 months than to raise them.

The demand for goods has remained low and the import prices of consumer goods and domestic producer prices have remained stable. Seasonal fluctuations in prices have gradually normalised, and companies' sales price expectations also anticipate a slowdown in the rise in prices of consumer goods in the future. On the other hand, the most price pressure remains in services, even though the rise in prices has also slowed down there. Sales price expectations still point to a rise in prices and, for example, rent increases have been quite moderate so far. The projected development of wages and salaries will keep service inflation at around 3.3% in 2024 and around 3% in 2025 and 2026.

The impact of rising interest rates on housing loans and consumer credit has been highlighted in the CPI this year. Their contribution to inflation is still almost 3 percentage points, while the combined impact of other commodities is less than 1 percentage point. The impact will diminish over the outlook period, however, first as the rise in interest rates slows and later as they start to fall. Due to interest rates, inflation measured by the CPI will be higher than the HICP this year and next. On the other hand, in 2025 and 2026, when interest rates fall, the impact will be the opposite; inflation measured by the HICP will be faster than that measured by the CPI.



Sources: Statistics Finland, MoF

In 2023, inflation will be 6.3% measured by the CPI. Inflation will be significantly lower than this at the end of the year. Core inflation is faster than in 2022, as the rise in prices of services and goods still accelerated in the first half of the year. Inflation will be 2% on average in 2024, and will fall below 2% in 2025 and 2026. This means that inflation will slow substantially from the 2022 and 2023 figures during the outlook period. The rise in the prices of services will contribute most to sustaining inflation in the coming years.

The biggest negative risks remain the impact of rising wages on inflation and the development of energy prices. For example, an escalation of the Middle East crisis could push energy prices up again, although concerns about escalation have eased slightly recently. On the other hand, high prices and the rise in interest rates have reduced demand, and as a result price pressures might also ease faster than expected. Indeed, market inflation expectations in the euro area have fallen rapidly. In addition, China's ongoing low inflation, even deflation, may further slow the rise in goods prices. In the longer term, it is also possible that a further slowing of globalisation, improving the resilience of production chains, mitigating and adapting to climate change, and trade disputes could also push prices higher in the coming years than has been the case.

Table 12. Price indices

	2021	2022	2023**	2024**	2025**	2026**
	change, %					
Export prices[1]	9.8	18.6	-4.3	-1.3	1.6	1.7
Import prices[1]	9.7	19.4	-3.7	-1.6	1.7	1.7
Consumer price index	2.2	7.1	6.3	2.0	1.4	1.7
Harmonised index of consumer prices	2.1	7.2	4.4	1.2	1.7	1.9
Core inflation[2]	1.2	3.6	4.1	2.3	2.3	2.2
Basic price index for domestic supply, including taxes	10.1	20.3	-2.3	-1.3	1.1	1.3
Building cost index	5.4	8.2	3.0	-0.5	0.9	0.8

[1] As calculated in the National Accounts

[2] Harmonised index of consumer prices, excluding energy and food

1.7 Medium-term outlook 2027 – 2028

Over the medium term, economic output is projected to grow moderately. In 2027, GDP is projected to grow by around 1.3%, and growth of around 1.1% is expected in 2028. The factors supporting GDP growth include the growth of private investment, which is expected to recover due to decreasing market interest rates as well as green transition investments. The Finnish economy is projected to be still below its normal capacity in 2027. However, economic output will approach the estimated potential output level, and the output gap will be closed at the end of the outlook period in 2028.

The positive development of the labour market is expected to continue in the medium term. The employment rate (ages 15–64) is projected to increase moderately in 2027 and 2028. The employment rate will rise to 75.5% in 2027 and to 75.9% in 2028. In addition to the economic conditions, the positive development of employment will be influenced by the employment measures of the Government's structural policy. The unemployment rate is projected to fall and the unemployment gap is expected to close in 2028.[1] In 2028, the unemployment rate is expected to be 6.1%.

Consumer prices are expected to rise steadily over the medium term. In 2027 and 2028, the change in consumer prices is expected to be 2% annually, which is in line with the European Central Bank's inflation target.

The medium-term projection is based on an estimate of potential output growth, which is considered to determine the medium-term and long-term growth potential of the Finnish economy.[2] Potential output refers to the economy's long-term growth path or a sustainable level of output that ensures stable inflation, which is achievable when economic capacity is in normal use. During the period 2023–2028, potential output is expected to grow on average by around 1% per year.

The development of potential output depends on the development of labour input, capital stock and total factor productivity. The impact of the change in labour input on the growth of potential output will be minor until 2026, after which labour

1 The unemployment gap refers to the difference between the unemployment rate and the NAWRU unemployment rate. The NAWRU unemployment rate refers to the level of unemployment where the labour market is in equilibrium and (wage) inflationary pressures remain stable.

2 In this projection, economic growth for years t+3 and t+4 (years t+4 and t+5 in the winter forecast) is estimated so that the output gap will close by year t+4. The output gap indicates the difference between the economy's actual output and potential output at a given point in time. During exceptional economic conditions, however, deviations from this basic assumption may 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. 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 decomposed into projections of potential labour input, potential capital stock and potential total factor productivity. Potential output and output gap are latent unobserved variables, the assessment of which involves uncertainties, particularly during a strong economic cycle and under conditions of rapid changes in the production structure.

input will stop growing and it will begin to reduce potential output. The weak growth contribution of labour input is due to the negative development of hours worked. 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 around 0.5% each year between 2023 and 2028.

Total factor productivity is the third source of potential output growth, and it has shown slightly higher 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. For the period 2023–2028, annual total factor productivity is expected to grow on average by around 0.5%, down from an annual average of more than 2% in the early 2000s.

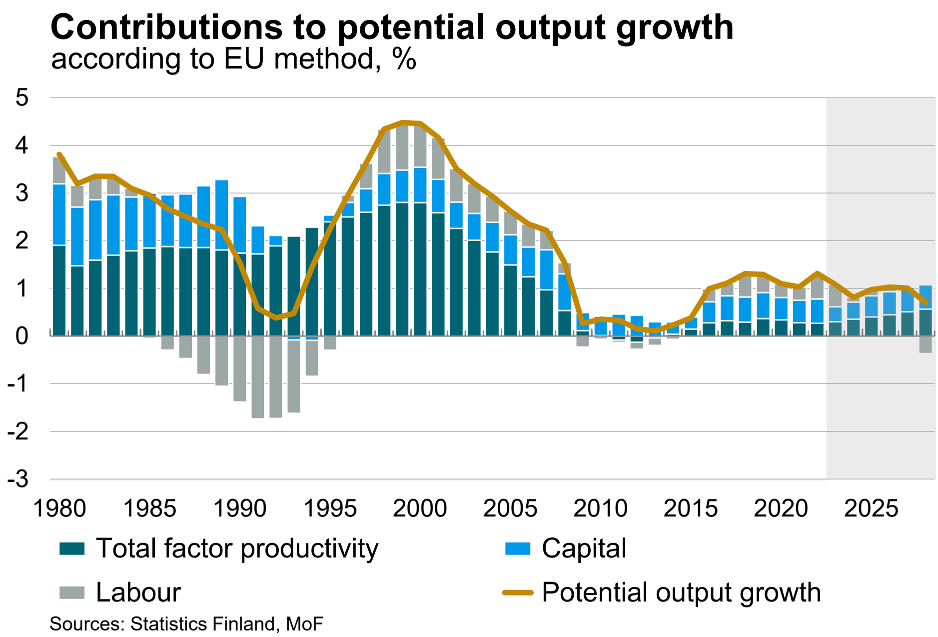


Table 13. Key forecast figures for the medium term

	2022	2023**	2024**	2025**	2026**	2027**	2028**
GDP at market prices, change in volume, %	1.6	-0.5	0.7	2.0	1.6	1.3	1.1
GDP, EUR bn	269	282	289	301	313	325	336
Consumer price index, change, %	7.1	6.3	2.0	1.4	1.7	2.0	2.0
Unemployment rate, %	6.8	7.2	7.5	7.1	6.6	6.4	6.1
Employment rate, %	73.8	73.6	73.5	74.1	74.8	75.5	75.9
General government net lending, relative to GDP, %	-0.8	-2.5	-3.5	-3.4	-3.0	-3.0	-2.9
Central government	-1.6	-3.2	-3.7	-4.2	-3.8	-3.7	-3.7
Municipal finances[1]	-0.2	-0.1	-0.1	-0.3	-0.3	-0.4	-0.3
Wellbeing services counties			-0.5	-0.3	-0.4	-0.4	-0.5
Social security funds	1.0	1.3	0.7	1.4	1.5	1.6	1.5
Structural balance, relative to GDP, %	-0.5	-1.3	-2.3	-2.7	-2.7	-2.8	-2.9
General government gross debt, relative to GDP, %	73.3	75.5	79.1	81.4	83.3	84.8	85.7
Central government debt, relative to GDP, %	52.7	55.4	58.5	60.6	62.2	63.5	64.6
Output gap, % of potential output[2]	-0.6	-2.0	-2.2	-1.2	-0.6	-0.3	0.0
Potential output growth, %[2]	1.3	1.1	0.8	1.0	1.0	1.0	0.7

[1] Local government until 2022

[2] Estimated according the method developed jointly by the EU Commission and Member States

2 General government finances

2.1 General government

General government finances will be persistently in deficit throughout the outlook period. Economic growth turned to a slight decline and will also remain subdued in 2024. Inflation-driven growth in expenditure will weaken the general government budgetary position. Tax revenue growth will be sluggish, with the deficit will deteriorate to well above 3% of GDP in 2024. In the following years, the deficit will slowly improve due to the Government's measures and economic growth. General government expenditure will be increased, however, by a number of previously decided measures, rising interest expenditure and substantial defence procurement.

General government debt will rise to over 75% of GDP in 2023 and to over 85% by 2028. Despite adjustment measures, the debt ratio will continue to rise. The central government, the municipalities and wellbeing services counties are all in deficit and will accrue debt every year.

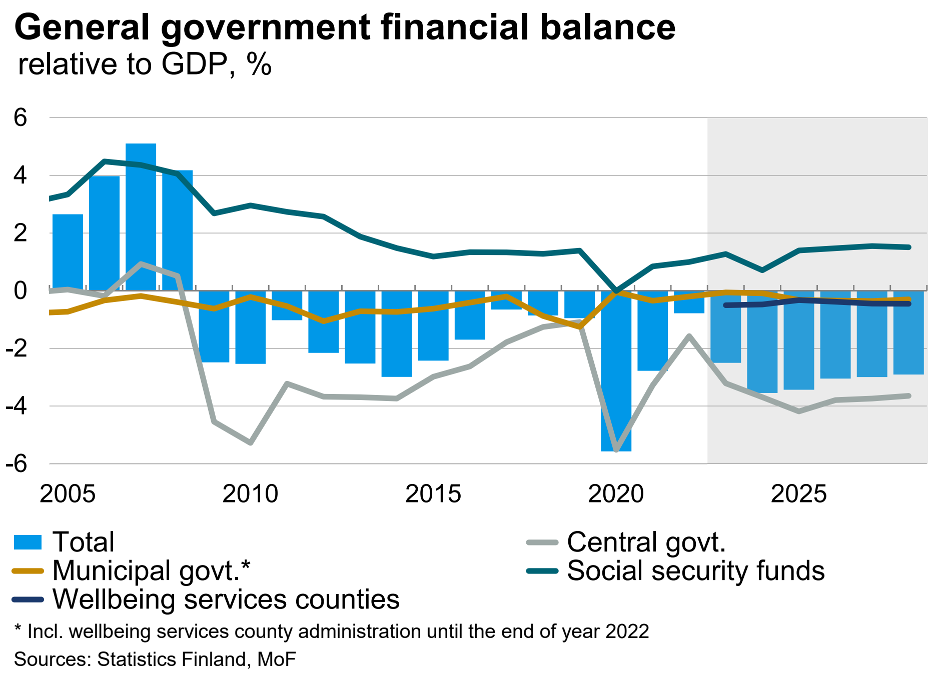
The central government budgetary position is the weakest of the sectors. The deficit will deteriorate to over 3% of GDP in 2023 and further to over 4% in 2025. Expenditure will be increased by previously agreed investments in, for example, preparedness, R&D expenditure and fighter aircraft procurement. The adjustment measures decided on by the Government will decrease central government expenditure. Tax revenue growth will be anaemic as the economy slows.

Of the local government subsectors, the municipal administration will remain in deficit, and the deficit will deepen as a result of investments and rapid price rises. Municipal investment expenditure will be kept high by the ageing building stock, migration and infrastructure construction.

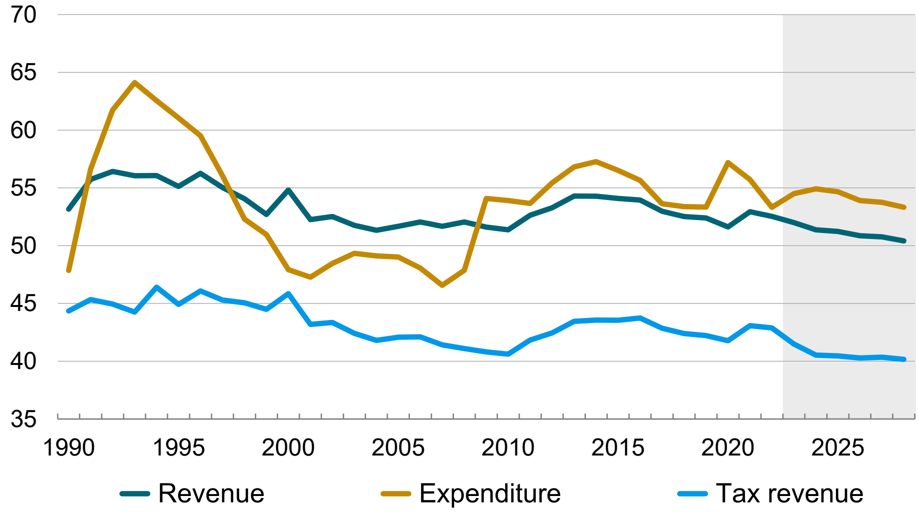
In 2023, the wellbeing services counties are projected to be in deficit in 2023 due to rapid increases in prices and wages as well as high investment expenditure. Wage settlements in the wellbeing services counties will increase personnel expenses faster than overall earnings growth, as a result of which the counties will have to make annual adjustments. The situation in the wellbeing services counties will also be exacerbated by labour shortages. Measures in the Government Programme will reduce expenditure pressures on the counties. In addition, the counties will have to adjust their activities in the coming years, which will slow expenditure growth.

The budgetary position of employment pension schemes will remain relatively unchanged in 2023–2024. The sector's property income and pension contribution income will grow rapidly, but pension expenditure will also rise sharply due to index increases. As the growth of pension expenditure slows in 2025, the budgetary position will improve to around 1.5% of GDP.

The budgetary position of the other social security funds will be 0.4% of GDP in 2023. The budgetary position of the sector will narrow in 2024, when unemployment insurance contributions will be sharply reduced. The other social security funds will be close to balance over the outlook period.

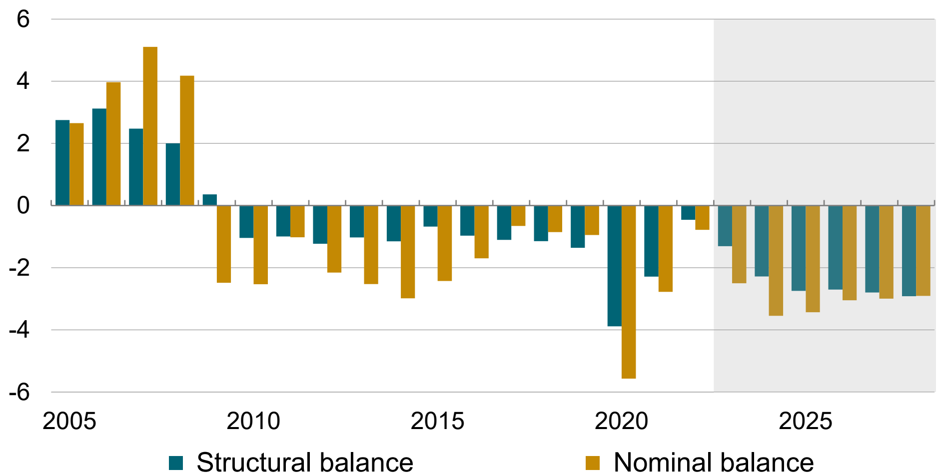


General government revenue, tax revenue and expenditure
relative to GDP, %



Sources: Statistics Finland, MoF

General government nominal and structural balance
relative to GDP, %



Based on the European Commission's production function approach
Sources: Statistics Finland, MoF

Table 14. General government finances[1]

	2021	2022	2023**	2024**	2025**	2026**
	EUR billion					
Current taxes	42.1	45.7	45.6	47.4	48.6	51.1
Taxes on production and imports	34.7	36.4	36.1	36.0	37.6	38.3
Social security contributions	30.5	32.2	34.2	32.9	34.8	35.8
Taxes and contributions, total[2]	108.1	115.2	117.0	117.2	122.0	126.2
Property income	7.2	7.0	9.3	10.8	11.9	12.5
Sales and fee income	16.5	17.5	18.7	19.1	19.3	19.6
Other revenue	1.0	1.4	1.6	1.5	1.3	1.1
Total revenue	**132.9**	**141.2**	**146.7**	**148.5**	**154.5**	**159.4**
Compensation of employees and intermediate consumption	61.0	64.0	69.9	71.3	73.4	75.6
Subsidies	4.0	3.0	2.6	2.7	2.6	2.7
Social security benefits and allowances	54.8	55.6	59.5	62.2	63.4	64.7
Other current transfers	6.8	6.8	6.8	6.5	6.9	6.9
Property expenditure	1.3	1.5	2.6	3.5	4.2	4.8
Gross capital formation	10.6	11.1	11.1	12.0	13.8	13.8
Other expenditure	1.3	1.3	1.4	0.6	0.6	0.5
Total expenditure	**139.8**	**143.2**	**153.8**	**158.8**	**164.8**	**169.0**
Consumption expenditure	61.7	64.6	70.3	72.2	75.1	77.9
Net lending (+) / net borrowing (-)	**-7.0**	**-2.1**	**-7.0**	**-10.3**	**-10.3**	**-9.5**
Central government	-8.2	-4.2	-9.1	-10.7	-12.6	-11.9
Municipal administration[3]	-0.9	-0.5	-0.2	-0.3	-1.0	-1.1
Wellbeing services counties			-1.4	-1.4	-1.0	-1.2
Employment pension schemes	2.3	2.3	2.6	2.8	3.9	4.3
Other social security funds	-0.1	0.3	1.0	-0.8	0.4	0.3
Primary balance[4]	-5.7	-0.6	-4.5	-6.8	-6.2	-4.8

[1] As calculated in the National Accounts

[2] Incl. capital taxes

[3] Local government until 2022

[4] Net lending excluding gross interest expenses

Table 15. Main economic indicators in general government

	2021	2022	2023**	2024**	2025**	2026**
	relative to GDP, %					
Taxes and social security contributions	43.1	42.9	41.5	40.5	40.5	40.3
General government expenditure	55.7	53.3	54.5	54.9	54.7	53.9
Net lending	-2.8	-0.8	-2.5	-3.5	-3.4	-3.0
Central government	-3.3	-1.6	-3.2	-3.7	-4.2	-3.8
Municipal administration[1]	-0.3	-0.2	-0.1	-0.1	-0.3	-0.3
Wellbeing services counties			-0.5	-0.5	-0.3	-0.4
Employment pension institutions	0.9	0.9	0.9	1.0	1.3	1.4
Other social security funds	-0.1	0.1	0.4	-0.3	0.1	0.1
Primary balance[2]	-2.3	-0.2	-1.6	-2.4	-2.1	-1.5
General government debt	72.5	73.3	75.5	79.1	81.4	83.3
Central government debt	51.3	52.7	55.4	58.5	60.6	62.2
General government employment, 1,000 persons	667	682	679	678	675	674
Central government	146	150	151	151	147	147
Municipal administration[1]	508	519	263	259	261	262
Wellbeing services counties			252	255	254	253
Social security funds	13	13	13	13	13	13

[1] Local government until the end of 2022.

[2] Net lending excluding gross interest expenses

Development of the tax ratio

The tax ratio is expected to fall in the medium term. The most significant factors explaining the fall in the tax ratio are the decrease in indirect taxes and unemployment insurance contributions relative to GDP. On the other hand, the impact of the Government's tax decisions on tax revenue will be roughly fiscally neutral in the 2024–2027 parliamentary term. The Government's tax decisions include both revenue-raising and revenue-reducing measures.

The structural factor, which lowers the tax ratio in the Ministry of Finance forecast, can be explained by examining indirect taxes. Excise duties and transport taxes are mainly unit taxes, i.e. the tax levels are determined in euros, for example per litre or kilogramme. As prices rise, their real level falls, which lowers real tax revenue and therefore also the ratio of tax revenue to (nominal) GDP. When the unit tax levels lag behind the price (or income) level, this can be considered to be a reduction of taxation.

In addition to this, the revenue from excise duties and transport taxes decreases as taxable consumption decreases and shifts to lower taxed products, thereby also decreasing the ratio of tax revenues to GDP. In addition to tax steering, this transition also occurs as a result of other regulations such as the Tobacco Act, renewable fuel distribution obligations and CO2 limit values for cars.

A decrease in tax revenues that occurs as a result of steering does not necessarily mean, however, that the private sector's non-tax costs would correspondingly decrease. In some cases, the private sector's costs may rise as a result of steering, despite a decline in tax revenues. For example, an increase in the renewable fuel distribution obligation will raise the price of fuels and still reduce tax revenues.

In direct taxation, corporate tax and capital income tax revenues are sensitive to cyclical developments. Changes in economic growth and corporate earnings may lead to an accumulation of significant changes. Earned income and capital income tax receipts grew significantly faster than GDP in 2021 and 2022, resulting in a higher tax ratio without any actual tax increases.

General government tax revenues by sector and tax category, % GDP

	2022	2023*	2024*	2025*	2026*	2027*	2028*
Total taxes and social security contributions	42.9	41.5	40.5	40.5	40.3	40.4	40.2
Central government	21.0	24.7	24.4	24.2	24.1	24.2	24.0
Municipalities	9.9	4.7	4.8	4.7	4.7	4.8	4.8
Social security funds	12.0	12.1	11.4	11.5	11.4	11.4	11.4
Total taxes and social security contributions	42.9	41.5	40.5	40.5	40.3	40.4	40.2
Current taxes[1]	17.4	16.6	16.7	16.4	16.6	16.7	16.7
Taxes on production and imports	13.5	12.8	12.5	12.5	12.2	12.2	12.0
Social security contributions	12.0	12.1	11.4	11.5	11.4	11.4	11.4

[1] incl. inheritance and gift tax

Value-added tax in ratio to GDP will remain stable during the review period. The biggest part of the transfer tax base consists of housing share and real estate sales. Of housing share sales, sales of first homes will still be exempt from transfer tax to the end of this year. In addition, transfer tax is received from other kinds of share trading, but securities trading on the stock market does not fall within the scope of the tax. In the period 2019–2022, an average of around EUR 900 million per year of transfer tax was accrued. In the transfer tax forecast, the Economics Department's assessment of the development of the housing and real estate market is used. In the outlook period 2023–2027, real estate and housing share sales are expected to remain slightly lower than before.

An estimate of municipal tax receipts is prepared as part of the earned income and capital income tax forecast. The forecast takes into account not only the development of the tax base but also known changes in the tax criteria. The forecast includes the assumption that an index adjustment will be made annually to earned income tax criteria. In the forecast, the average municipal tax percentage of the last adopted budget year is used as the average municipal tax percentage for the coming years.

Of the social security contributions, the most important are earnings-related pension contributions, which will develop quite steadily. On the other hand, unemployment insurance contributions will be reduced for 2024, which will lead to a significant reduction in social security contribution revenue. In 2024, health insurance contributions will also be reduced.

2.2 Central government

The central government budgetary position has remained weak in 2023. Despite the cost-saving measures taken by Prime Minister Orpo's Government, the budgetary position of central government will remain deeply in deficit throughout the outlook period. The factors contributing to the weakening of the budgetary position include previous measures that increase expenditure, slow economic growth, a slowing of tax revenue growth, and rising interest expenditure. Central government expenditure is increased by additional expenditure on national defence, immigration and the security of supply due to Russia's war of aggression.

In 2023, central government tax revenue will grow by an exceptional amount, 23.4% compared with 2022. This is due to the reform of the organisation of health, social and rescue services, in connection with which a significant amount of earned income tax and corporate tax revenue will be transferred from the municipalities to central government. In 2024, central government tax revenue will grow by only 1.1% due to sluggish economic growth. In 2025, tax revenue growth will accelerate to 3.6%, driven by economic growth and rising employment, and will remain the same in 2026.

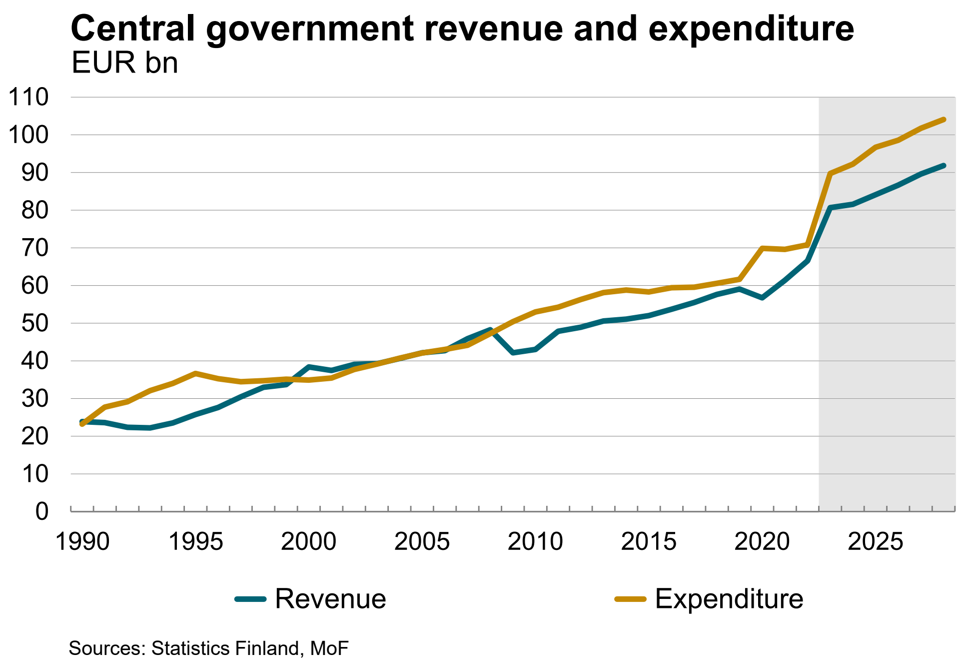
Central government consumption expenditure will grow rapidly in 2023. Rising prices and wages as well as higher expenditure on immigration reception and increased procurement of defence materiel will increase consumption expenditure. In 2024, growth in consumption expenditure will moderate significantly. Cost-saving measures allocated to nearly all administrative branches will curb expenditure growth. In 2025, the responsibility for organising employment and economic development services (TE services) will be transferred from the central government to municipalities. This is a cost-neutral reform for the central government, as the costs incurred due to the responsibility for organising the services will be compensated for by increased income transfers to municipalities.

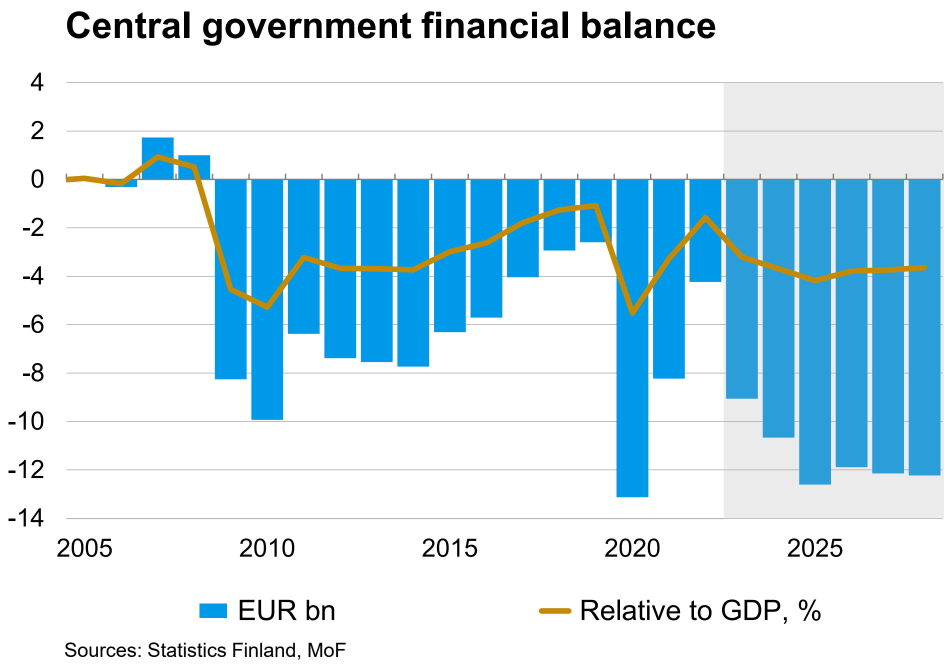
In 2023, investments will remain at the previous year's level. Investments in 2023 will be reduced by the defence materiel assistance to Ukraine being recognised as negative investments and capital transfers abroad in the national accounts. In 2024, investments will grow by an exceptional amount, when deliveries begin of purchases to replace previously transferred defence materiel, and as measures are launched to reduce the repair backlog of infrastructure . In addition, the Act on

Research and Development Funding will increase investment from 2024 onwards. Deliveries of F-35 aircraft starting in 2025 will raise investments to a high level for an extended period. New acquisitions for border surveillance will materialise, when patrol vessels are delivered to the Border Guard in 2025 and 2026. In the final years of the outlook period, investments will be boosted by vessel deliveries of the Navy's Squadron 2020 project.

Central government interest expenditure has been growing rapidly and will continue to grow throughout the outlook period. In 2023, interest expenditure according to the national accounts will be around EUR 1.9 billion. In 2026, interest expenditure is projected to be EUR 3.8 billion, namely 1.2% of GDP.

The central government budgetary position will deteriorate in the forecast period, initially as a result of weak revenue development due to slow economic growth, and in 2025 as investment spending and the financing needs of the wellbeing services counties increase. Rising interest expenditure will weigh on the budgetary position during the outlook period.




Central government financial balance
4
2
0
-2
-4
-6
-8
-10
-12
-14
2005
2010
2015
2020
2025
EUR bn
Relative to GDP, %
Sources: Statistics Finland, MoF

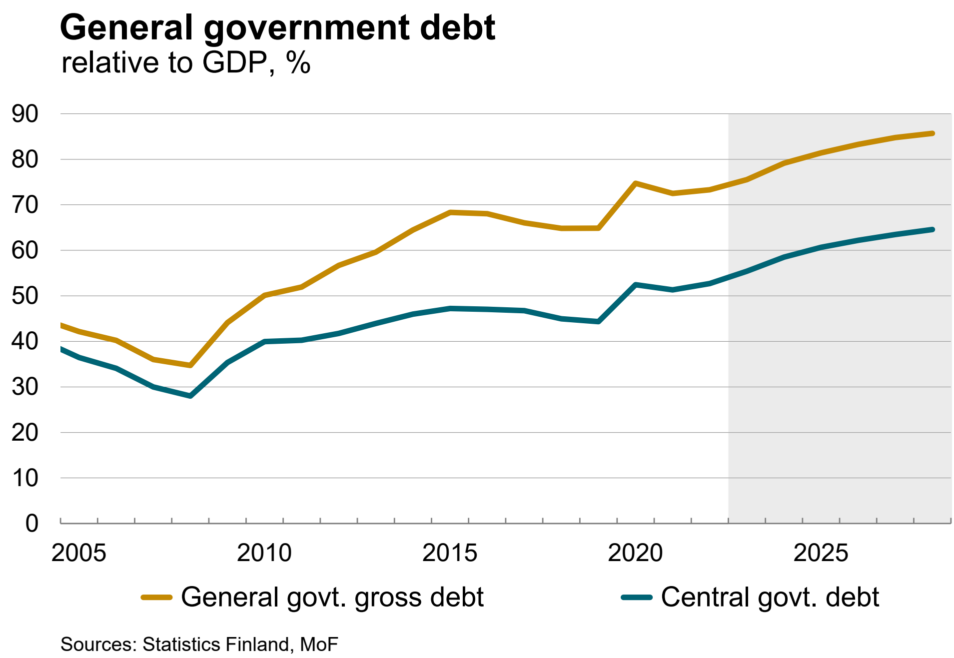

General government debt
relative to GDP, %
90
80
70
60
50
40
30
20
10
0
2005
2010
2015
2020
2025
General govt. gross debt
Central govt. debt
Sources: Statistics Finland, MoF

Table 16. Central government[1]

	2021	2022	2023**	2024**	2025**	2026**
	EUR billion					
Current taxes	16.3	19.1	32.3	33.5	34.3	36.2
Taxes on production and imports	34.7	36.4	36.1	36.0	37.6	38.3
Social security contributions	0.0	0.0	0.0	0.0	0.0	0.0
Taxes and social security contributions, total[2]	51.8	56.4	69.6	70.4	72.9	75.5
Sales and fee income	4.3	4.4	4.6	4.6	4.7	4.7
Property income	1.9	2.0	2.4	2.4	2.5	2.5
Other revenue	3.4	3.7	4.1	4.1	4.0	3.9
Total revenue	**61.4**	**66.6**	**80.7**	**81.6**	**84.1**	**86.7**
Compensation of employees and intermediate consumption	15.6	16.7	19.0	19.5	19.6	20.0
Property expenditure	1.2	1.3	1.9	2.8	3.4	3.8
Subsidies	3.5	2.5	2.2	2.2	2.2	2.2
Social security benefits and allowances	4.8	4.9	5.4	5.5	5.5	5.6
Other current transfers	38.7	39.2	55.2	56.3	58.6	59.6
to general government	32.6	33.1	49.2	50.5	52.7	53.6
Gross capital formation	4.1	4.5	4.5	5.3	6.8	6.7
Other expenditure	1.7	1.6	1.6	0.7	0.7	0.6
Total expenditure	**69.6**	**70.8**	**89.7**	**92.2**	**96.7**	**98.6**
Consumption expenditure	16.0	17.3	19.4	20.0	20.2	20.8
Net lending (+) / net borrowing (-)	**-8.2**	**-4.2**	**-9.1**	**-10.7**	**-12.6**	**-11.9**
Primary balance[3]	-7.1	-2.9	-7.1	-7.9	-9.2	-8.0

[1] As calculated in the National Accounts

[2] Includes gift and inheritance taxes

[3] Net lending excluding gross interest expenses

2.3 Municipal administration

Year 2023 appears reasonably good in the municipal administration, although consumption expenditure growth has been faster than previously estimated. On the other hand, investment expenditure has been clearly lower than last year. The budgetary position of the municipal administration[1] is projected to be close to balance in 2023 and 2024. The deficits will deepen to around 0.3–0.4% of GDP between 2025 and 2028, due to, among other things, rapidly rising costs and the reconciliation and timing of central government transfers related to the reform of health and social services. The deficits will increase municipal administration debt, but growth in debt ratio to GDP will remain very moderate.

Consumption expenditure in the municipal sector will increase during the outlook period mainly driven by rising prices, as the need for services in education (including early childhood education) decreases across the forecast period in the pressure projection due to the declining birth rate and smaller age cohorts. An exception to consumption expenditure growth driven by rising prices is the TE services reform, scheduled for 2025, when responsibility for the organisation of employment and economic development services will be transferred to municipalities, and their liability for financing unemployment benefits will be simultaneously expanded. The municipal sector's largest expenditure item is personnel expenses, which negotiated increases will increase by around 3% in 2024. At the same time, the increase in personnel expenses will be curbed by a reduction in unemployment insurance contributions, which will also have a positive impact on tax revenue. From 2025 to 2027, earnings in the municipal sector are expected to improve at a somewhat higher rate than in the economy in general due to the development programme for remuneration systems agreed for the municipal sector.

Current transfers to municipalities from central government will decrease in 2024 as central government transfers are reduced as a result of the further specification of the transfer calculation related to the health and social services reform. In addition, the one percentage point index brake decided on by the Government will curb growth in central government transfers to municipalities in 2024–2027. After

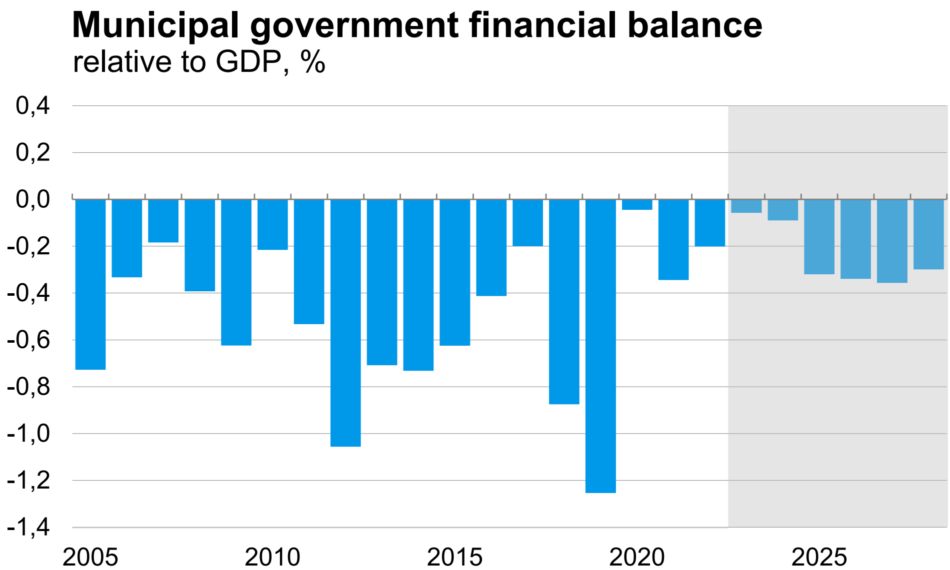
1 In the forecast, Helsinki's health, social and rescue services have been included in the wellbeing services counties subsector.

the completion of 2022 taxation at the end of 2023, it became apparent that the estimated cut in central government transfers related to the transfer calculation for the health and social services reform was not sufficient. In order to ensure cost neutrality between municipalities, wellbeing services counties and central government, which is a principle of the reform, an additional transfer will be made to central government from the municipalities' central government transfers. The Government decided, however, to phase the new additional cut over the period 2025–2027 in order to avoid a large unforeseen cut in central government transfers in 2024, at a time when a large number of municipalities had already decided on their 2024 budget. This gave municipalities more time to adjust to the lower than expected central government transfers.

The average municipal tax rate will rise in Finland by 0.07 percentage points to 7.51% in 2024, which is estimated to increase municipal tax revenue by around EUR 80 million annually. In addition, real estate tax revenues will be boosted by the Government's decision to separate land from buildings within the general real estate tax rate and to raise the lower limit of their tax band. The change will increase the real estate tax revenue of municipalities by just over EUR 100 million from 2024. Tax revenues remain the most important source of revenue for the municipal sector, although they have almost halved as a result of the health and social services reform. Although tax revenue growth in the outlook period will remain close to the long-term average, it will mean significantly lower additional revenue for municipalities than in the past. The health and social services reform significantly reduced municipalities' financial room for manoeuvre, which further underlines the importance of risk management in municipal financial planning.

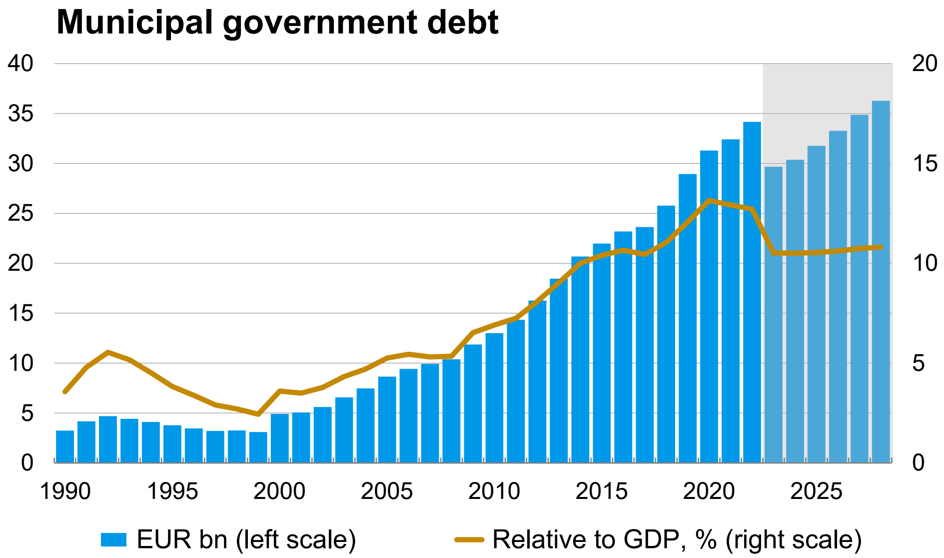
Investment pressures in the municipal sector have not disappeared despite the momentary downturn in investment, but they still remain considerable due to, among other things, the age of the building stock, migration and the changes required by the green transition. However, the uncertain outlook of the investment environment, increased interest rates and the deteriorating financial situation of the municipalities may push back investments or prevent their implementation. Investments are projected to return to the normal growth trend in the coming years.

Growing deficits will exert adjustment pressures in the municipal sector and will require careful consideration of the need for investments. To date, the projection has only taken into account the municipalities' and joint municipal authorities' own technical EUR 50 million saving in consumption expenditure from budget year 2024 onwards and the changes in tax rates decided by municipalities for 2024. Municipal administration expenditure may prove to be lower than the pressure projection, if municipalities are able to adjust both their service networks and their operations to meet the declining need for services. On the other hand, pruning the service network may prove to be a politically difficult issue in municipalities of all sizes.



Incl. wellbeing services county administration until the end of year 2022

Sources: Statistics Finland, MoF



Incl. wellbeing services county administration until the end of year 2022

Sources: Statistics Finland, MoF

Table 17. Municipal administration[1]

	2021	2022	2023**	2024**	2025**	2026**
	EUR billion					
Taxes and social security contributions, total	25.8	26.6	13.2	13.9	14.3	14.9
of which municipal tax	20.8	21.8	9.1	9.7	10.0	10.5
corporate tax	3.0	2.8	1.9	1.8	1.9	1.9
real estate tax	2.0	2.0	2.2	2.3	2.4	2.4
Sales and fee income	11.4	12.3	9.6	9.8	9.9	10.0
Transfers from the central government	17.6	18.3	8.1	7.8	8.4	8.5
Other revenue	1.7	1.7	1.9	1.9	2.0	2.0
Total revenue	**56.5**	**58.9**	**32.8**	**33.4**	**34.5**	**35.4**
Compensation of employees and intermediate consumption	43.5	45.3	24.8	25.1	25.9	26.6
Social assistance and benefits in kind	5.6	5.9	0.7	0.8	1.1	1.1
Other current transfers	1.9	1.8	1.7	1.7	2.1	2.1
Property expenditure	0.1	0.2	0.5	0.6	0.6	0.7
Gross capital formation	6.4	6.5	5.4	5.5	5.8	6.0
Other expenditure	-0.2	-0.2	-0.1	-0.1	-0.1	-0.1
Total expenditure	**57.4**	**59.5**	**33.0**	**33.7**	**35.4**	**36.5**
Consumption expenditure	41.6	43.2	20.8	21.3	22.5	23.4
Net lending (+) / net borrowing (-)	**-0.9**	**-0.5**	**-0.2**	**-0.3**	**-1.0**	**-1.1**
Primary balance[2]	-0.7	-0.4	0.3	0.3	-0.4	-0.4

[1] As calculated in the National Accounts excl. Helsinki's social welfare and health care services and rescue services

[2] Net lending excluding gross interest expenses

2.4 Wellbeing services counties

In the first year of operation, the budgetary position of the wellbeing services counties will be clearly in deficit at around 0.5% of GDP. The state of deficit will continue throughout the outlook period. The counties' expenditure has increased rapidly due to wage agreements, staff shortages and a general rise in prices. Investments in the sector are also at a high level. The deficit of the counties in counties accounting terms will be substantial in the current year and will require adjustment measures from the counties. In the coming years, the sector is projected to remain in deficit, but the counties' own adjustment measures could improve the sector's budgetary position to a better level than forecast.

The forecast for the wellbeing services counties assumes, on the basis of preliminary budget data of counties, that in 2024 the counties will be able to adjust their activities. Prudently, only some of the adjustment measures have been taken into account in the forecast. This estimate will be refined as budgets are adopted and more precise data on activities become available.

In 2023, the expenditure of the wellbeing services counties has been increased by the rapid rise of wages and prices. Although personnel availability problems have curbed the growth in wage expenditure, the prices of services have increased sharply. In 2024, expenditure growth in the sector will be slowed by adjustment measures, estimated at around EUR 0.35 billion, planned by the counties. Measures planned for later years have not yet been taken into account in the forecast, as more uncertainty is associated with them. Expenditure growth will also be slowed by the decisions made by Prime Minister Orpo's Government regarding changes to the tasks of the counties up to 2027. Investments are at a high level and will remain there, as large investment projects are under way or about to start in many counties in the next few years.

Wage growth is of particular importance for the development of the expenditure of the wellbeing services counties. The negotiated wage increases of the wellbeing services counties are considerable for the next few years, and negotiated pay programmes will further increase expenditure. The growth in wage costs will be constrained by personnel shortages, which in turn will cause wage competition, result in the use of more expensive purchased services or impair the availability of services. All of these will have an impact on cost growth, either in other ways or possibly at a later date.

Most of the financing for the wellbeing services counties comes from central government. Central government funding increases in accordance with the growth of service needs, the price level and changes to the responsibilities of the wellbeing services counties. In terms of prices, the wellbeing services counties' central government funding is linked to the increase in the general level of wage and salary earnings, which will inevitably weaken the wellbeing services counties' budgetary position annually. The projection takes into account the provision for a retrospective review of the wellbeing services counties' in amounts corresponding to the spending limits provision presented General Government Fiscal Plan, not at the level of the projected deficit. It is possible that, despite the wellbeing services counties' own measures, the spending limits provision made in autumn 2023 will not be sufficient for the retrospective review.

Table 18. Welfare services counties[1]

	2023**	2024**	2025**	2026**
	EUR billion			
Sales and fee income	3.7	3.8	3.9	4.0
Transfers from the central government	25.7	26.5	28.3	29.1
Other revenue	0.2	0.2	0.2	0.2
Total revenue	**29.6**	**30.5**	**32.5**	**33.4**
Compensation of employees and intermediate consumption	24.0	24.5	25.7	26.7
Social assistance and benefits in kind	5.7	6.0	6.3	6.5
Property expenditure	0.1	0.1	0.2	0.2
Gross capital formation	1.2	1.2	1.2	1.1
Other expenditure	0.1	0.1	0.1	0.1
Total expenditure	**31.0**	**31.9**	**33.4**	**34.6**
Consumption expenditure	25.8	26.5	27.9	29.0
Net lending (+) / net borrowing (-)	**-1.4**	**-1.4**	**-1.0**	**-1.2**
Primary balance[2]	-1.3	-1.2	-0.8	-1.0
Index of welfare services counties, change, %	3.52	2.53	2.83	2.87
Index of wage and salary earnings of welfare services counties, change, %	6.0	4.7	6.6	4.7

[1] As calculated in the National Accounts incl. Helsinki's social welfare and health care services and rescue services

[2] Net lending excluding gross interest expenses

2.5 Social security funds

2.5.1 Employment pension schemes

In 2023, the surplus of employment pension schemes will remain at the previous year's level of 0.9% of GDP. The surplus of employment pension schemes is projected to continue to grow in 2024–2026, reaching 1.4% of GDP in 2026.

Earnings-related pension expenditure will increase significantly in 2023, by over 9%. In 2024, earnings-related pension expenditure is projected to continue to grow relatively rapidly, by around 7%. Expenditure is expected to continue to grow in the coming years, albeit at a much slower pace of just over 3% per year.

Despite the rapid increase in expenditure, the surplus of employment pension schemes is expected to improve in the coming years. The revenue of employment pension schemes will be increased, in particular, by property income, which is projected to further due the higher level of interest rates. In addition, revenue from earnings-related pension contributions will rise throughout the outlook period as the sum of wages and salaries grows.

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. The surplus of the other social security funds will increase to around 0.4% of GDP in 2023. In 2024, the other social security funds are projected to remain slightly in deficit, particularly due to a significant reduction in unemployment insurance contributions. In addition, health insurance contributions will be temporarily reduced to equalise the surplus accrued in previous years. In the following years, the sector will return to a surplus of 0.1% of GDP.

In 2023, expenditure in the sector will grow by 2.5%. In 2024, expenditure will be reduced by the Government's measures, but total expenditure will still increase by 1.7%. In 2025, total expenditure is projected to decline. Total expenditure will be reduced by, among other things, lower unemployment benefits and housing allowance expenditure. The impact of the Government's measures will also be evident in the following years.

In 2023, the sector's revenue will increase by 6.8% compared with the previous year, driven by growth in received social security contributions. In 2024, the sector's revenue is projected to decrease. The decrease in revenue will be mainly due to a reduction in received social security contributions, in particular due to a decrease in unemployment insurance contributions. Unemployment insurance contributions will be nearly halved as a result of the favourable state of the Employment Fund's cyclical buffer and the measures outlined in the Government Programme.

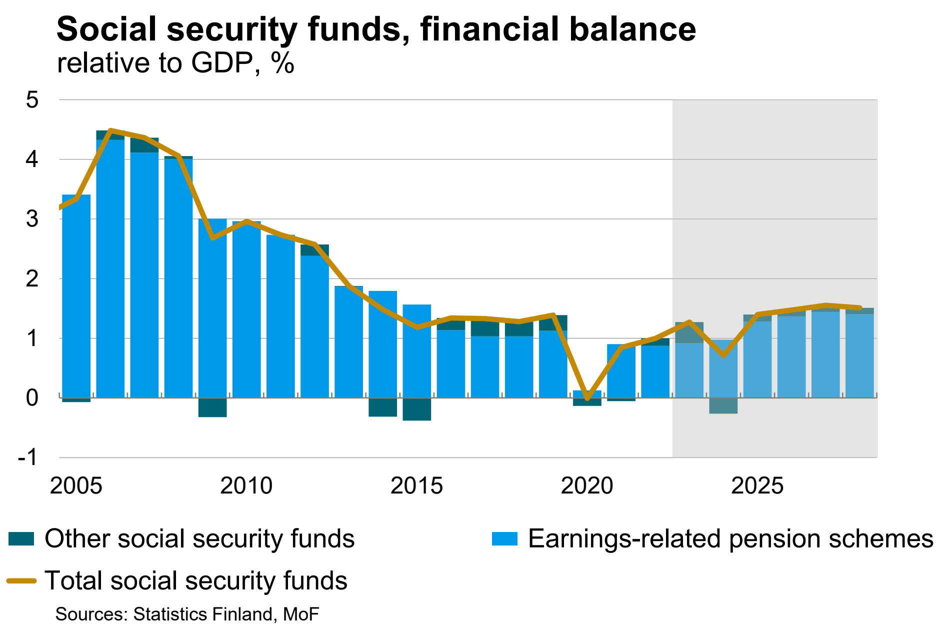


Table 19. Finances of social security funds[1]

	2021	2022	2023**	2024**	2025**	2026**
	EUR billion					
Property income	4.0	3.6	5.1	6.6	7.6	8.1
Social security contributions	30.4	32.2	34.2	32.9	34.8	35.8
of which contibutions paid by employers	18.9	20.3	21.4	20.9	22.0	22.9
contributions paid by insured	11.5	11.9	12.8	12.0	12.8	12.9
Transfer from general government	16.8	16.2	16.8	17.7	17.7	17.7
Other revenue	0.8	0.9	0.9	0.9	0.9	0.9
Total revenue	**52.0**	**52.9**	**57.0**	**58.0**	**60.9**	**62.5**
Compensation of employees and intermediate consumption	1.9	1.9	2.1	2.1	2.2	2.2
Social benefits and social benefits in kind	44.4	44.8	47.7	49.9	50.6	51.6
Other expenditure	3.6	3.5	3.6	3.9	3.9	4.1
Total expenditure	**49.9**	**50.2**	**53.4**	**55.9**	**56.7**	**57.9**
Consumption expenditure	4.1	4.2	4.2	4.4	4.5	4.6
Net lending (+) / net borrowing (-)	**2.1**	**2.7**	**3.6**	**2.1**	**4.2**	**4.6**
Earnings-related pension schemes	2.3	2.3	2.6	2.8	3.9	4.3
Other social security funds	0.0	0.3	1.0	-0.8	0.4	0.3
Primary balance[2]	2.1	2.7	3.6	2.1	4.2	4.6

[1] As calculated in the National Accounts

[2] Net lending excluding gross interest expenses

Appendix 1.

Table 1. Local government (Municipal administration + Welfare services counties)[1]

	2021	2022	2023**	2024**	2025**	2026**
	EUR billion					
Sales and fee income	11.4	12.3	13.3	13.5	13.8	14.0
Taxes and social security contributions, total	25.8	26.6	13.2	13.9	14.3	14.9
Transfers from the central government	17.6	18.3	33.8	34.4	36.7	37.6
Other transfers	0.2	0.2	0.2	0.2	0.3	0.3
Other revenue	1.5	1.5	1.9	1.9	2.0	2.0
Total revenue	**56.5**	**58.9**	**62.5**	**63.9**	**66.9**	**68.8**
Compensation of employees and intermediate consumption	43.5	45.3	48.8	49.7	51.7	53.3
Social assistance and benefits in kind	5.6	5.9	6.5	6.8	7.3	7.6
Other current transfers	1.9	1.8	1.7	1.8	2.2	2.2
Property expenditure	0.1	0.2	0.6	0.7	0.8	0.9
Gross capital formation	6.4	6.5	6.5	6.7	7.0	7.1
Other expenditure	-0.2	-0.2	-0.1	-0.1	-0.1	-0.1
Total expenditure	**57.4**	**59.5**	**64.0**	**65.6**	**68.9**	**71.0**
Consumption expenditure	41.6	43.2	46.7	47.8	50.4	52.4
Net lending (+) / net borrowing (-)	**-0.9**	**-0.5**	**-1.6**	**-1.6**	**-1.9**	**-2.3**
Primary balance[2]	-0.7	-0.4	-1.0	-0.9	-1.2	-1.4

[1] As calculated in the National Accounts

[2] Net lending excluding gross interest expenses.

MINISTRY
OF FINANCE

MINISTRY OF FINANCE
Snellmaninkatu 1 A
PO BOX 28, 00023 GOVERNMENT
Tel. +358 295 160 01
financeministry.fi

ISSN 1797-9714 (pdf)
ISBN 978-952-367-xxx-x (pdf)

December 2023