UNOFFICIAL TRANSLATION

Ministry of Finance

STABILITY PROGRAMME FOR FINLAND

September 2000 update

1 Economic policy premises

The Finnish economy has experienced a sustained period of rapid economic growth since 1994. Employment has improved fast over this period, but unemployment remains high. As a result of the deep recession of the early 1990s, also state debt is still at a high level. The Finnish public finances are still not adequately equipped for the pressure of an ageing population and of tougher tax competition.

The primary objectives of Finland's economic policy in the second half of the 1990s were to foster growth by strengthening the economic fundamentals and to stabilise public finances. This policy proved successful. Economic policy should now focus more clearly on structural issues, instrumental in securing stable economic growth.

Owing to policies aimed at economic stability and wage moderation and due to increased competition brought about by EU accession, inflation has remained slow in recent years. Nonetheless, inflation as measured in terms of the consumer price index accelerated in the second quarter of 1999, reaching a rate of 3 per cent in the summer of 2000, becoming one of the fastest in the euro area. To date, the increase in inflation has been largely due to price developments in import prices, notably the price hike in crude oil.

With economic growth prevalent only in some sectors and regions, capacity utilisation rates have risen to high levels in some sectors of the economy, and the risk of production bottlenecks and subsequent overheating of the economy has become significant.

A spread in price pressure and the creation of a price-wage-price spiral would bring stable economic growth and favourable employment prospects to an end at the latest in the medium term. For this reason, the key task in economic policy is to avert these risks.

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The primary goal of the second multiparty government of Prime Minister Paavo Lipponen, nominated in spring 1999, is to improve employment. This calls for sound economic growth and moderate wage developments, among other things. The Government is committed to enhancing the preconditions for economic growth by means of reforms in the product, capital and labour markets as well as in the tax and social benefit systems, designed to boost employment and encourage independent initiative.

The sizeable state debt, along with a heavy tax burden, constitutes the most serious problems in public finances. The Government Programme, published in spring 1999, sets out the following goals for central government expenditure:

- With a view to preparing for both cyclical fluctuations and expenditure pressures caused by the ageing of the population, the government aims to reduce the central government debt-to-GDP ratio below 50 per cent during the election period ending in 2003.

- To this end, a structural surplus (national accounts definition) is to be created in central government finances by means of tight fiscal policy.

- Central government expenditure will be kept constant in real terms, at the 1999 Budget level or lower, over the whole term of office.

The principles outlined in the Government Programme have since been specified:

- Since the adoption of the Government Programme, economic prospects have improved, making fiscal restraint even more essential in order to ensure stability. The expenditure ceilings, adopted in March 2000 and constraining the drafting of the 2001 Budget Proposal, reduce budgetary expenditure in central government by a good percentage point in real terms as of the year 2000. Thereafter budgetary expenditure adjusted for costs incurred by active debt redemption is to be maintained unchanged in real terms. The expenditure ceilings are explained in more detail in section 2.1 of this Programme.

- The Government statement to Parliament on the expenditure ceilings for 2001-2004 sets out a central government surplus ratio of almost 1½ per cent as a minimum target in order that the tax cuts outlined in the Government Programme can be carried out without jeopardising the target set for fiscal balance.

- A Government decision-in-principle reached in May 2000 allocates the bulk of state privatisation proceeds to the redemption of state debt.

- The Government decided in the same connection that central government indebtedness will be monitored using debt figures that exclude the effect of property sales proceeds.

Furthermore, the parliamentary factions of the ruling parties have agreed to refrain from using any automatic savings generated by a decrease in unemployment and reduced debt servicing to cover new spending items or levels, should the economic cycle so require.

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The Stability and Growth Pact, specifying the Treaty, establishes that Member States shall adhere to a medium-term objective of budgetary positions close to balance or in surplus. In line with the Government Programme for central government debt reduction, the Finnish government comfortably meets the requirement of a balanced general government budgetary position as set out in the Stability and Growth Pact. Owing to the partly funded employment pension system, which is included in the public sector, the social security funds continue to register a surplus of approximately 3 per cent in relation to total output. Local government finances are close to balance.

The Government aims to maintain a general government surplus ratio of at least 4½ per cent over the election period. This goal is in line with the surplus target of almost 1½ per cent in central government finances.

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While the comprehensive incomes policy agreement pursued by the Government was not reached in autumn 1999, the settlements made at the branch level generally proved to be fairly uniform. Most wage settlements are for one year, with a labour cost impact of 3.1 per cent as estimated by the contracting parties. However, contract wage increases in some sectors eventually exceeded this benchmark as a result of strikes and threats of strikes.

The government deems it important that the main labour market organisations remain committed to a target of low inflation and is willing to encourage the contracting of multi-year wage settlements to foster strong competitiveness in the Finnish economy.

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The government is committed in its Programme to implementing a FIM 10-11 billion reduction in income taxes and social security contributions (1½ per cent of GDP) over the election period. However, the tax cuts presuppose robust economic growth, moderate wage settlements and reforms in the tax structures. In line with the Government Programme, the tax concessions will be partly offset by higher energy and environmental taxes. Capital and corporate tax rates have already been raised. As outlined in the Programme, the timing of the tax cuts is influenced by the cyclical position of the economy, and the aim is to ensure that the changes in the tax rates in all tax brackets is equal and that the overall effect of the cuts is job-conducive for those in the lowest income brackets.

The Government reduced income tax rates and social security contributions for the tax year of 2000 for a sum equivalent to approximately 0.4 per cent of GDP. Moreover, a 1 per cent inflation adjustment was made in the brackets in income taxation and the sickness insurance payments of pensioners were lowered.

Given the current conditions of strong economic growth, the risk of wage inflation has become evident. Consequently, the government has considered tax cuts with exceptional caution. The government's proposed cuts in income taxes and social security contributions in the 2001 Budget Proposal amount to around 0.8 per cent of GDP. This involves a calculatory inflation adjustment of less than 0.2 per cent of GDP. Should the government be convinced that labour cost developments can remain moderate in the coming years, the question of labour taxation can be addressed again at a later date.

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Broad Economic Policy Guidelines (BEPGs) for the economic policies of the Member States and the Community are adopted every year. The government presented Parliament with a summary of the Broad Economic Policy Guidelines, approved by the ECOFIN Council in June 2000. The BEPGs advocate, among other things, Member States caution in order to avert fiscal policy from turning pro-cyclical, given the current conditions of fast growth, and consequently recommends accelerating the process of consolidation in public finances. A report on the implementation of the BEPG recommendations will be drawn up at the EU level in the course of the autumn.

The document presents the following fiscal policy guidelines for Finland:

- maintain a tight fiscal stance, and stand ready, already in 2000, to tighten further if the risks of overheating materialise more clearly;

- continue to increase the government surplus through a reduction in government expenditure relative to GDP; to this end, respect firmly the central government expenditure guidelines; and

- continue the reductions in taxation on labour as part of the restructuring of the tax system.

The labour market measures advocated in the Guidelines for Finland are especially to review the incomes transfers system and to pursue recent policy orientations to reduce the tax burden, particularly rates on low wages. In order to improve the functioning of the product markets, Finland should strengthen competition especially in the distribution sector and to further open up to competition the markets for public procurement and public services as well as to consider reforming the competition law as outlined in the white paper of the Commission.

The government notes that its economic policy is in line with the recommendations for economic policies of the Broad Economic Policy Guidelines.

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By its structural policy measures, the government is pursuing faster economic growth towards the end of the projection period than is presented in this Stability Programme. However, the public finance estimates presented in this Programme are based on cautious growth assumptions. Government structural policy measures are described in more detail in section 4 of this Programme.

The Government assesses that the surplus figures in this Programme meet the target of a structural surplus in state finances as outlined in the Government Programme. In accordance with the resolution issued by ECOFIN on 1 May 1998, any room for manoeuvre arising from better-than-expected economic developments will be used to consolidate public finances.

Should budgetary developments prove weaker than estimated in this Programme, the fiscal policy targets will nonetheless be met on condition that public expenditure conforms with the decisions already taken and in line with the state expenditure ceilings.

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Council Regulation 1466/97 stipulates that all euro area Member States shall submit information necessary for the purpose of multilateral surveillance, as laid down in Article 99 (ex Article 103) of the Treaty, by annually drafting a Stability Programme. The content of the Programme at hand adheres to the said Regulation as well as the opinion adopted by the Monetary Committee on 16 September 1998. This Programme has been prepared in conjunction with the Budget Proposal for 2000, and as laid down in the Government Rules of Procedure, is adopted by the Government plenary session. This Programme, like its predecessors, will be handed over to the Parliament for information.

This Programme is based on the Government Programme adopted last year, on the state expenditure ceilings adopted in March this year and on the Budget Proposal for 2001. The Programme was drawn up taking into consideration the Government decision-in-principle made in May on 2000 on the allocation of state sales proceeds throughout 2000-2003, the supplementary budget for 2000 and other government decisions.

The Programme is non-binding for 2004, as general elections will be held in Finland in spring 2003, followed by the appointment of a new government.

The general government deficit and debt ratios presented in this Programme are now based on ESA95 concepts for the first time instead of the earlier ESA79 definitions. The statistical reform had little impact on Finland's deficit and debt ratios.

2 General government consolidation measures

2.1 Central government finances

Owing to spending cuts made in both central and local government finances, average annual public expenditure grew at a rate of only half a per cent in real terms between 1994-1999, while total output increased by an average of 4½ per cent annually over the same period.

The Government is committed to continuing with a fiscal policy that restricts expenditure growth. The government announced in its Programme that central government real expenditure would be kept constant at the 1999 Budget level or lower over the government's whole term in office.

In March 2000, the Government adopted the expenditure ceilings for the ministries for 2001-2004 and presented them to Parliament for handling. Following parliamentary handling, the government gained a two-thirds majority vote of confidence in Parliament in May 2000.

The expenditure ceilings ensure that state budgetary finances at fixed prices will remain at the 1999 Budget level over 2001-2004. In comparison with the 2000 Budget, however, spending is set to decrease by FIM 2½ billion, in other words over one per cent.

The expenditure ceilings are defined by the ministries and bind their budget preparations. Should the economy develop as envisaged, the spending pressure for the coming year can be anticipated quite well. The expenditure ceilings for the latter years take into account foreseen events and existing decisions only. Meeting the medium-term fiscal policy targets demands constant readjustment of priorities between government projects and expenditures.

Income estimates and tax yield estimates for state property sales proceeds were raised by altogether FIM 19½ billion (2½ per cent of GDP) in the supplementary budget for 2000 adopted in May and revised in June, of which over one half is to be allocated to state debt redemption. Spending for the ministries was increased by almost FIM 3 billion, partly owing to this spring's pay rises, which had not been budgeted for in the ordinary Budget.

In May, the government reached a decision-in-principle on the use of state sales proceeds between 2000-2003. The government will boost basic funding for universities and will commit to certain projects aimed to bolster longer-term growth prospects. The decision gives rise to spending amounting to FIM 1 million over 2000-2003. The rest of privatisation proceeds already received and forthcoming will be allocated to debt redemption. In addition, the government intends to accumulate funds in the State Pension Fund faster than originally planned and is prepared to introduce a specific counter-cyclical fund.

The sum total for the 2001 Budget Proposal adopted in September 2000 proved to be about one per cent higher than the guidelines. As the difference is mainly due to an increase in the inflation estimates, the Budget Proposal meets the Government Programme target of keeping expenditure constant in real terms.

The government decided to lower income tax rates and social security contributions in 2000 for a sum roughly equivalent to 0.4 per cent of GDP. Reductions in payroll taxes amount to about one half of the total. Moreover, a one percentage point inflation adjustment was made in the brackets for income taxes, and the sickness insurance contributions of pensioners were lowered. The inflation adjustment in the tax scales is lower than the change in earned income, implying that the income tax rate of wage earners will remain virtually unchanged on 1999.

In connection with the 2001 Budget Proposal, the government introduced income tax cuts for a sum corresponding to 0.6 per cent of GDP. Moreover, a 3 per cent inflation adjustment in line with consumer price developments in 2000 is to be made in the income tax scales. Should the government be convinced that labour cost developments will remain moderate in the coming years, the question of labour taxation can be addressed again at a later date.

A technical assumption is made in the calculations of this Programme such that income taxes and social security contributions will be reduced altogether by about ½ per cent of GDP in 2002 and 2003.

In line with a market-oriented industrial policy, the government has reduced state ownership in a number of enterprises and still holds a number of privatisation authorisations from Parliament. In June 2000, the government was granted authority by Parliament to sell the government's remaining stake of slightly over one half of the Sonera plc equity stock.

The supplementary budget proposal for 2000 raises state sales proceeds estimates to around FIM 13 billion, and the 2001 Budget Proposal makes provision for privatisation proceeds amounting to FIM 2.5 billion. No assumptions for sales proceeds have been made in the indebtedness calculations in this Programme for later years.

2.2 Local government and social security funds

In the national accounts, the Finnish public sector is classed into central government, local government and social security funds. Local government mainly consists of municipalities. Employment pension funds, while mainly private enterprises, are included in the social security funds of general government finances because of their statutory nature.

The financial position in local government has on the whole been satisfactory in recent years. Overall, the fiscal stance in local government is expected to be close to balance over the whole of this government, with the debt-to-GDP ratio in local government predicted to slightly decrease by 2004.

Social security contributions need not be raised in the next few years and unemployment contributions can even be lowered. Notwithstanding, the financial surplus in the social security funds promises to remain unchanged at above 3 per cent of GDP. The bulk of the surplus lies in the employment pension funds, which are making provision for the future pensions of the large babyboom generations. The market value of the employment pension funds amounted to 53 per cent of GDP at the end of 1999.

In the context of social security financing, 2001-2004 forms a period of taking stock for the future, as the financial situation forebodes deterioration after the projection period with the ageing of the population. Indirect labour costs in relation to wages are anticipated to increase by several percentage points towards the end of this decade if the effective retirement age for the baby-boom generations remains at its current level; the present average retirement age is 59. The government aims to increase the ratio of employed people to the population of working age for instance by deferring exit from the labour market by an average of 2 to 3 years in the long run, closer to the normal old-age retirement age (generally 63-65 years).

3 Medium-term projection for 2000-2004

3.1 Economic projections for 2000-2004

The current fast growth in the EU economy is expected to slacken to an annual rate of 2½ per cent towards the end of the projection period.

Although brisk GDP growth has continued already for many years in Finland and though there are signs of bottlenecks, preconditions for further growth are still good: there is still potential for employment to improve, the rapidly growing information technology branches are well represented in Finland and there is still broad growth potential for service production. Should economic policy succeed as planned, cost developments will not curb economic growth in the medium term, allowing the Finnish economy to grow slightly faster than the rest of the EU.

Though the fundamentals for growth are favourable, prudent growth estimates are justified as a basis for fiscal policy. The estimates in this Programme for 2000 and 2001 draw on the economic forecasts appended to the Budget. Succeeding projections are based on the following assumptions:

- economic growth in Finland slows down to 2.7 per cent a year by 2004;

- export demand grows faster than domestic demand as world trade growth picks up again;

- the interest rate assumption is based on market expectations and the exchange rate assumption on the situation prevailing in August 2000;

- wage developments remain moderate; and

- central government expenditure and incomes develop as described in sections 2.1 and 2.2 of this Programme.

Table 1: Main economic indicators for 1999-2004

	1999	2000*	2001*	2002**	2003**	2004**	2000-2004
	change, %						
GDP	4,0	5,2	4,2	3,2	2,7	2,7	3,6
Imports	3,2	6,7	6,0	5,2	5,2	5,2	5,7
Exports	6,3	10,8	8,3	5,5	5,0	5,0	6,9
Private consumption	3,6	3,0	2,9	2,9	2,7	2,7	2,8
Public consumption	2,0	0,6	0,8	0,5	0,5	0,5	0,6
Private investment	6,2	8,1	5,8	4,0	3,5	3,5	5,0
Public investment	-3,8	-2,8	-0,8	0,0	0,0	0,0	-0,7
Price of private consumption	1,7	2,8	1,8	1,8	1,8	1,8	2,0
Price of GDP	0,7	1,8	1,2	1,7	1,8	1,8	1,7
Employment	3,3	1,7	1,6	0,8	0,6	0,5	1,0
Labour productivity	1,8	3,4	2,5	2,4	2,1	2,2	2,5
	level						
Unemployment rate	10,2	9,6	8,6	8,0	7,8	7,5	
Employment rate (15-64 years)	66,0	66,8	67,7	68,0	68,2	68,3	

* forecast ** medium-term projection

Average annual growth over 2000-2004 is expected to amount to 3½ per cent, which is slightly faster than in the 1980s. Average growth between 1995-1999 was as high as 4½ per cent.

Productivity growth is estimated to decelerate to a little over 2 per cent over the projection period as growth focuses on the service sector, where labour productivity grows slower than in the economy as a whole. Labour supply is set to increase faster than the working age population as labour demand augments. If the above assumptions hold, the employment rate for those aged 15-64 years can be estimated to rise to 68½ per cent and the unemployment rate to decline to 7½ per cent in 2004.

3.2 Developments in the general government balance between 1999-2004

The surplus in general government finances in 1999 proved to be slightly smaller than anticipated in the September 1999 update to the Stability Programme, as indicated in the tables appended to this Programme. The surplus projected for 2000 has nonetheless been kept virtually unchanged.

The development path for general government finances presented in Table 2 is based on economic policy decisions and on the macro-economic projection presented in Table 1, the underlying assumptions being discussed in detail in section 3.1

The surplus in general government finances is projected at around 4½ per cent of GDP between 2001-2004. General government is expected to remain in surplus over the whole of the projection period, and finances in local government are anticipated to be more or less in balance. The surplus in the social security funds is estimated at approximately 3 per cent of GDP.

Finnish public sector investments were financed without exception by current income until the recession in the early 1990s, but between 1992-1996 the deficit exceeded investment. The situation started improving in 1993 and the problem has since been settled.

Table 2: General government financial balance and debt as a percentage of GDP

	1999	2000*	2001*	2002**	2003**	2004**
Financial balance						
Central government	-0,8	1,3	1,4	1,3	1,4	1,9
Local government	-0,2	0,1	0,1	0,0	0,0	0,0
Social security funds	2,9	3,1	3,2	3,1	3,1	3,0
General government total	**1,9**	**4,5**	**4,7**	**4,4**	**4,5**	**4,9**
Debt						
Central government	44,0	39,9	36,9	34,8	32,7	30,1
Local government	2,7	2,5	2,3	2,3	2,2	2,1
Social security funds	0,0	0,0	0,0	0,0	0,0	0,0
General government total	**46,6**	**42,4**	**39,2**	**37,1**	**34,9**	**32,2**

* forecast ** medium-term projection

3.3 Sensitivity analysis of public finances

A base scenario as well as fast and slow growth alternatives are illustrated in the diagrams at the end of this Programme. In these alternative scenarios, total output growth is assumed to differ by an average of one percentage point from the growth path in the base scenario during 2001-2003.

In the slow growth scenario annual growth would decelerate to below 2 per cent at the end of the projection period and unemployment would remain at roughly the present level. The general government would register a surplus over the forecast range also in this scenario.

In the more favourable scenario, economic growth would continue at a rate of almost 4 per cent and unemployment would decrease rapidly. In this alternative, the surplus in general government would continue to grow, fuelled by ever-stronger central government finances.

The analysis of interest rate sensitivity in general government finances is based on a projection in which interest rates differ by one percentage point either upwards or downwards from the base scenario from the beginning of 2001. In the high interest rate scenario, total output as well as employment, essential for balance in public finances, would deviate from the base scenario less than in the slow growth alternative, and the general government deficit would develop more favourably than in the slow growth scenario, despite the impact of higher interest rates on debt servicing expenses. Conversely, in the low interest rate scenario, general government developments would not be quite as favourable as in the fast growth alternative, with growth in total output and employment both remaining weaker.

3.4 Estimates on structural deficit developments

The instructions approved by the Monetary Committee on 16 September 1998 stipulate that stability programmes provide sufficient information on GDP developments to allow an analysis of the cyclical position of the economy. An undisputed method of estimating the so-called structural deficit does not exist, however, and it is difficult to interpret the results obtained.

The assessment methods applied by the Commission and the OECD indicate that total output in Finland is set to exceed the long-term growth profile by 1½ to 3 per cent in the medium term. This implies a government structural balance (adjusted for cyclical influences) 1 to 2 percentage points weaker than estimated in this Programme.

The assumption in the base scenario in this Programme is that unemployment will not decline below the structural level over the projection period. This means that price and wage pressure does not take place, implying that the developments can be construed as sustainable.

Growth rates higher than those in the base scenario, instead, call for further structural reforms aiming at lower structural unemployment. This would provide better growth potential in the economy and fiscal pressure would thus be less severe. This is a further argument for continuing structural reforms.

4 Structural policy

The Finnish economy faces two major challenges. First, owing to the developments in the global economy, the competition the Finnish economy is facing is clearly increasing and spreading to new sectors, narrowing down the traditional sheltered economy. The adoption of the euro and a deepening Single Market play a key role in spurring these changes. Second, with the ageing of the population, labour supply is set to decline in the next decade, correspondingly weakening the financial base in social security and pensions. A contracting labour force hampers economic growth potential as well as increases pressure on the financing of public expenditure.

These two challenges highlight the importance of fiscal restraint and structural reforms. There is a growing need in general government finances to concentrate on relieving the expenditure pressure caused by the ageing of the population and on reducing the central government debt ratio. The key task in structural policy is to secure prerequisites for employment-oriented stable economic growth. Crucial structural policy measures consist of:

1. Securing adequate labour supply and enhancing the operation of the labour markets. The government aims to increase the employment rate (ratio of employed to population of working age) close to 70 per cent. One of the main medium-term challenges is to keep ageing workers employed. At present, only 45 per cent of those aged 55-64 remain in work. An agreement was struck between the labour market organisations and the employment pension funds last year on some measures aiming at higher retirement ages. Having viewed the initiative positively, the government has encouraged its materialisation. Moreover, the government is monitoring the implementation of the agreement and the adequacy of the measures will be assessed in collaboration with the labour market organisations. The need for further measures will be evaluated on the basis of this assessment.

With a view to further reducing unemployment, social benefits and taxes will be better co-ordinated so that work is always rewarding. Active labour market measures will be targeted particularly at reducing long-term unemployment, and job brokerage will be enhanced. The government's employment policy measures are described in detail in the National Action Plan adopted in April 2000.

Measures to improve working life are carried out by the government within the framework of an established tripartite principle, built on collaboration with the labour market organisations. Changes in labour legislation aim to strike the right balance between the security of employees and the flexibility required in company operations. Efforts will be made to make wages and terms of employment more flexible in different economic cycles, different industrial sectors and at more local levels. The government endorses greater flexibility in working hours. A report was published on the reform of labour legislation and the government will present Parliament with a government proposal in the course of autumn 2000.

2. Enhancing operation of product and capital markets. By bolstering the operation of the markets, the risk of overheating caused by fast economic growth can be reduced and boosting the operation of the markets can create the preconditions for profitable production in a new economic environment. Eliminating barriers to competition promotes the introduction of new entrepreneurs and innovations on the markets, while the flexibility of the economy helps adapt to changes in global demand.

The government reform policies in the functioning of the product and capital markets in Finland are presented in the "Cardiff report" adopted in November 1999. Following the adoption of the report, actions to boost competition in the telecommunications markets, among others, were launched.

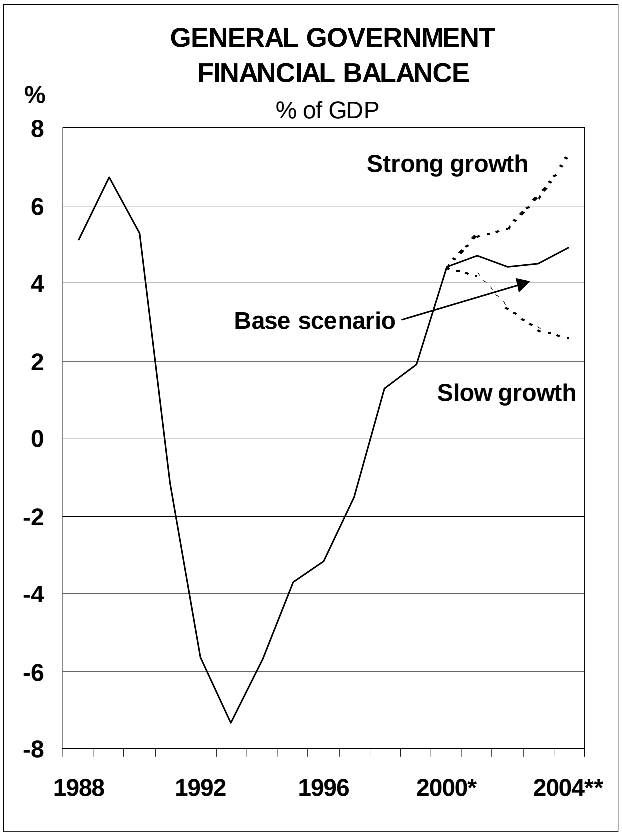
In June, the government introduced reforms aimed to improve the functioning of the housing markets. Within a broader package, measures will be taken to bear upon house prices by stepping up housing construction in the capital city region and other centres of growth. The supply of skilled construction workers will be enhanced, the availability of suitable housing lots will be increased and competition will be encouraged. In the same context, an assessment is to be made on whether new actions need to be taken in stabilising the market for rented housing by reforms in legislation, for instance. The system of housing allowances will be revised and the economic efficiency of the system will be improved.

A lack of funding is currently no obstacle to the expansion of business activities, so measures to enhance the capital markets will continue to focus on securing a neutral treatment of all investment instruments.

3. Further advancing the educational level of the population and enhancing research and development activities. Educational levels are rapidly rising in the newly industrialised economies and growth in the international economy is fastest in highly processed products and services. These developments create a constant challenge for the Finnish educational system and educational policy therefore gains an important economic dimension. With a view to raising the overall educational level, free pre-school education for all 6-year-olds was introduced in autumn 2000. Moreover, efficiency in education will be increased, particularly at the university level, by shortening the length of studies. The main emphasis in vocational training lies in improving the quality of the training.

Increasing the quality and effectiveness of education and research creates a base for innovations, for developing high-technology products and services as well as for ensuring a growth strategy aiming at an overall rise in value-added in production.

Thanks to the privatisation proceeds of state property, among other things, the ratio of R&D expenditure to GDP is anticipated to reach 3.3 per cent by 2003. The bulk of R&D activities and funding still takes place in the private sector, however, and indeed, the share of private-sector funding is expected to increase. The quality and the effectiveness of public funds allocated to R&D is set to continue gaining in weight.


GENERAL GOVERNMENT
FINANCIAL BALANCE
% of GDP
%
8
6
4
2
0
-2
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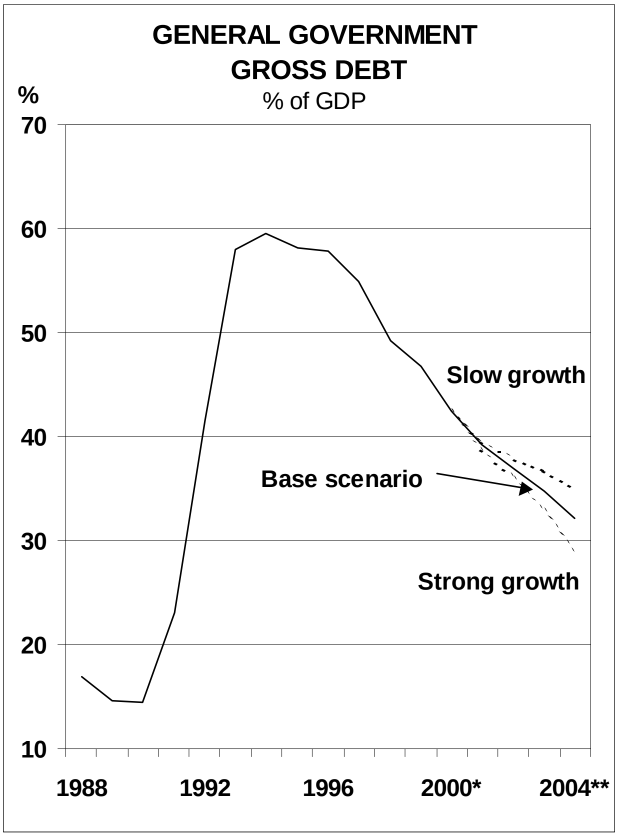
1988
1992
1996
2000*
2004**
Strong growth
Base scenario
Slow growth


GENERAL GOVERNMENT
GROSS DEBT
% of GDP
%
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50
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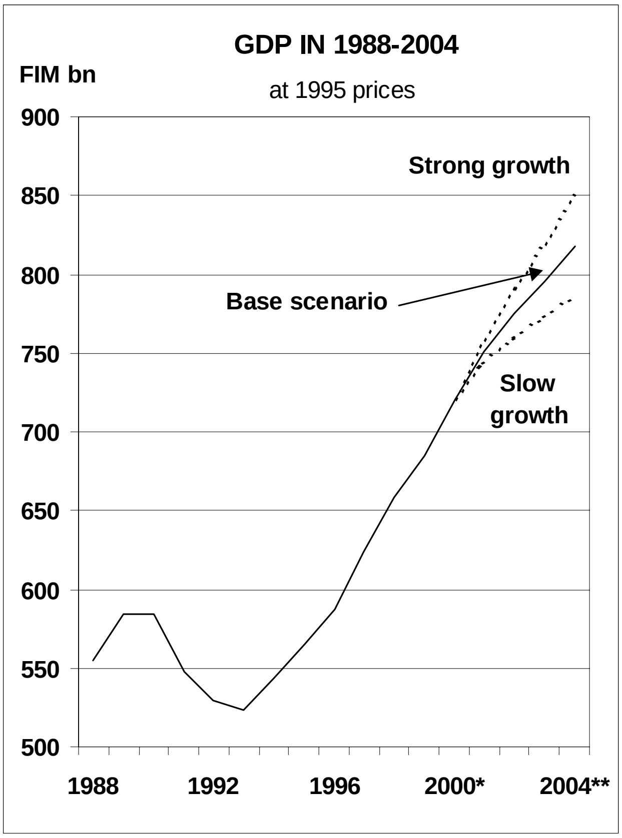
1988
1992
1996
2000*
2004**
Slow growth
Base scenario
Strong growth


GDP IN 1988-2004
at 1995 prices
FIM bn
900
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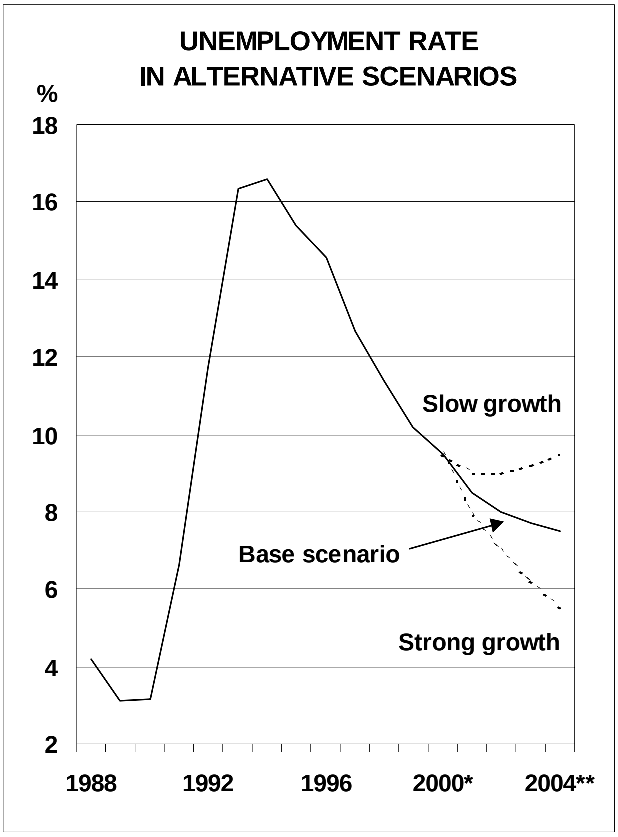
800
750
700
650
600
550
500
1988
1992
1996
2000*
2004**
Strong growth
Base scenario
Slow
growth


UNEMPLOYMENT RATE
IN ALTERNATIVE SCENARIOS
%
18
16
14
12
10
8
6
4
2
1988
1992
1996
2000*
2004**
Slow growth
Base scenario
Strong growth

A1. General government finances as a percentage of GDP

	1999	2000*	2001*	2002**	2003**	2004**
Taxes	32,5	33,2	32,4	31,5	31,0	30,7
Social security contributions	12,9	12,5	12,4	12,3	12,2	12,2
Other revenue	3,5	3,8	3,6	3,5	3,5	3,4
Total revenue	**49,0**	**49,5**	**48,4**	**47,3**	**46,7**	**46,3**
Consumption expenditure	21,5	20,8	20,5	20,2	20,1	19,9
Subsidies	1,6	1,6	1,6	1,5	1,5	1,5
Social income transfers	17,8	16,8	16,4	16,1	15,9	15,7
Interest outlays	3,5	3,3	2,8	2,7	2,5	2,2
Other expenditure	2,3	2,1	2,1	2,0	2,0	1,9
Total expenditure	**46,6**	**44,7**	**43,4**	**42,7**	**42,0**	**41,2**
Saving	2,4	4,8	5,0	4,7	4,7	5,2
Depreciation and net capital transfers	2,3	2,3	2,3	2,2	2,2	2,2
Gross capital formation	2,8	2,6	2,5	2,5	2,5	2,4
Financial surplus, net lending	**1,9**	**4,5**	**4,7**	**4,4**	**4,5**	**4,9**
Total expenditure (1)	49,7	47,6	46,2	45,4	44,7	43,9

1) Including capital formation.

A2. General government interest outlays and primary balance as a percentage of GDP

	1999	2000*	2001*	2002**	2003**	2004**
Gross interest payments	3,5	3,3	2,8	2,7	2,5	2,2
Primary balance	5,4	7,8	7,6	7,1	7,0	7,1
Net lending	1,9	4,5	4,7	4,4	4,5	4,9

A3. General government financial balance and debt as a percentage of GDP

	1999	2000*	2001*	2002**	2003**	2004**
Financial balance, net lending (-), %	**1,9**	**4,5**	**4,7**	**4,4**	**4,5**	**4,9**
Stock flow adjustments	2,1	3,6	3,8	4,3	4,0	3,7
-Public sector consolidation (1)	1,8	0,6	0,6	0,6	0,6	0,5
-Impact of exchange rates (2)	1,4	0,3	0,0	0,0	0,0	0,0
-Net accumulation of financial assets	-1,1	2,6	3,2	3,7	3,4	3,2
Impact of nominal increase in GDP	-2,3	-3,3	-2,3	-1,9	-1,7	-1,6
Change in gross debt	-2,1	-4,3	-3,2	-2,1	-2,2	-2,7
Level of gross debt, %	**46,6**	**42,4**	**39,2**	**37,1**	**34,9**	**32,2**

1) The employment pension funds are assumed to decrease their investments in central government assets by FIM 5 billion per annum between 2000 - 2004

2) Exchange rates estimated to remain at August 2000 level between 2000-2004.

A4. General government financial balance, debt and main economic indicators between 1995-2004, according to the Convergence Programmes of 1995-1997 and the Stability Programmes of 1998, 1999 and 2000, as a percentage of GDP, 1)

	1995	1996	1997	1998	1999	2000*	2001*	2002**	2003**	2004**
Financial balance										
CP-95	-5,3	-0,7	0,5	1,4	2,3					
CP-96	-5,2	-2,9	-1,4	-0,5	0,3	1,1				
CP-97	-5,0	-3,1	-1,3	-0,1	0,3	1,0	1,9			
SP-98			-1,1	1,1	2,4	2,2	2,1	2,3		
SP-99				1,0	3,1	4,7	4,2	4,6	4,7	
SP-2000	**-3,7**	**-3,2**	**-1,5**	**1,3**	**1,9**	**4,5**	**4,7**	**4,4**	**4,5**	**4,9**
Debt										
CP-95	64,9	64,8	64,8	61,8	59,2					
CP-96	59,4	61,8	61,0	59,9	58,3	56,5				
CP-97	58,1	58,0	59,1	57,5	56,3	54,8	52,0			
SP-98			55,1	51,9	48,5	46,4	44,8	43,2		
SP-99				49,2	46,3	42,9	40,7	38,0	35,2	
SP-2000	**57,2**	**57,1**	**54,1**	**48,7**	**46,6**	**42,4**	**39,2**	**37,1**	**34,9**	**32,2**
GDP, % change										
CP-95	5,0	4,5	4,0	3,0	2,5					
CP-96	4,3	2,8	3,9	4,0	3,5	3,0				
CP-97		3,3	4,5	3,5	3,5	3,0	2,8			
SP-98			6,0	5,5	4,0	2,7	2,6	2,6		
SP-99				5,6	3,8	3,9	3,0	2,6	2,6	
SP-2000	**3,8**	**4,0**	**6,3**	**5,5**	**4,0**	**5,2**	**4,2**	**3,2**	**2,7**	**2,7**
Employment, % change										
CP-95	2,9	2,8	2,0	1,1	0,7					
CP-96	2,2	1,5	1,7	1,9	2,3	1,4				
CP-97		1,0	1,7	1,4	1,5	1,4	1,3			
SP-98			2,5	2,6	1,9	1,0	0,8	0,7		
SP-99				2,4	2,8	1,7	0,8	0,4	0,4	
SP-2000	**2,2**	**1,3**	**2,0**	**2,4**	**3,3**	**1,7**	**1,6**	**0,8**	**0,6**	**0,5**
General government revenue										
CP-95	52,1	53,0	53,1	53,1	53,1					
CP-96	53,0	54,9	53,8	53,3	52,7	52,3				
CP-97		54,6	54,2	53,2	52,1	51,5	51,4			
SP-98			52,7	52,1	50,7	49,8	49,3	48,7		
SP-99				51,2	51,2	51,4	50,4	49,9	49,3	
SP-2000	**50,6**	**51,0**	**50,0**	**49,5**	**49,0**	**49,5**	**48,4**	**47,3**	**46,7**	**46,3**
General government expenditure (2)										
CP-95	56,1	52,8	51,6	50,8	49,9					
CP-96	56,3	56,4	53,7	52,2	50,8	49,8				
CP-97		56,4	53,9	52,0	50,6	49,3	48,2			
SP-98			52,9	50,0	47,5	46,7	46,1	45,4		
SP-99				49,2	47,6	46,1	45,7	45,1	44,6	
SP-2000	**53,7**	**53,0**	**50,7**	**47,6**	**46,6**	**44,7**	**43,4**	**42,7**	**42,0**	**41,2**

CP-95 Convergence Programme, September 1995

CP-96 Convergence Programme update, September 1996

CP-97 Convergence Programme update, September 1997

SP-98 Stability Programme, September 1998

SP-99 Stability Programme, September 1999

SP-2000 Actual figures and Stability Programme update, September 2000

1) Due to the National Accounts reform the consolidation of revenue and expenditure in central government budgeting, the figures given in the September 2000 update of the Stability Programme are not fully compatible with the previous figures.

2) Excluding capital expenditure.