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FINLAND: MACRO FISCAL ASSESSMENT
AN ANALYSIS OF THE FEBRUARY 2010 UPDATE OF THE STABILITY
PROGRAMME

The Stability and Growth Pact requires each EU Member State to present an annual update of its medium-term fiscal programme, called 'stability programme' for countries that have adopted the euro as their currency and 'convergence programme' for those that have not. The most recent update of Finland's stability programme was submitted on 4 February.

The attached technical analysis of the programme prepared by the staff and under the responsibility of the Directorate-General for Economic and Financial Affairs (DG ECFIN) of the European Commission, was finalised on 17 March 2010. Comments should be sent to Mart Maiväli (mart.maivali@ec.europa.eu). The main aim of the analysis is to assess the realism of the budgetary strategy presented in the programme as well as its compliance with the requirements of the Stability and Growth Pact. However, the analysis also looks at the overall macro-economic performance of the country and highlights relevant policy challenges.

The analysis takes into account (i) the Commission services' autumn 2009 forecast, (ii) the code of conduct ("Specifications on the implementation of the Stability and Growth Pact and guidelines on the format and content of stability and convergence programmes", endorsed by the ECOFIN Council of 10 November 2009) and (iii) the commonly agreed methodology for the estimation of potential output and cyclically-adjusted balances.

Based on this analysis, the European Commission adopted a recommendation for a Council opinion on the programme on 17 March 2010. The ECOFIN Council is expected to discuss its opinion on the programme on 16 April 2010.

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All these documents, as well as the provisions of the Stability and Growth Pact, can be found on the following website:

http://ec.europa.eu/economy_finance/sgp/index_en.htm

TABLE OF CONTENTS

1. INTRODUCTION.....	4
2. KEY CHALLENGES IN THE ECONOMIC DOWNTURN AND THE POLICY RESPONSE.....	5
3. MACROECONOMIC OUTLOOK.....	7
4. GENERAL GOVERNMENT BALANCE	9
4.1. Budgetary implementation in 2009	9
4.2. The programme’s budgetary strategy for 2010	11
4.3. The programme’s medium-term budgetary strategy	12
4.4. Risk assessment.....	14
5. GOVERNMENT DEBT AND LONG-TERM SUSTAINABILITY	16
5.1. Recent debt developments and medium-term prospects	16
5.1.1. Debt projections in the programme	16
5.1.2. Assessment	18
5.2. Long-term debt projections and the sustainability of public finances.....	18
5.2.1. Sustainability indicators and long-term debt projections	18
5.2.2. Additional factors	21
5.2.3. Assessment	22
6. INSTITUTIONAL FEATURES OF PUBLIC FINANCES	22
6.1. Fiscal framework.....	22
6.2. Quality of public finances	23
7. OVERALL ASSESSMENT.....	23
ANNEX. COMPLIANCE WITH THE FORMAT AND CONTENT REQUIREMENTS FOR STABILITY AND CONVERGENCE PROGRAMMES	25

1. INTRODUCTION

This document assesses the February 2010 update of Finland's stability programme, which was submitted on 4 February 2010 and covers the period 2009-2013. The programme builds on the 2010 budget, the 2010-2013 central government spending limits decision and the macro-economic forecast published by the Ministry of Finance in December 2009. It was approved by the government in a plenary session and presented to the national parliament without a vote during the drafting stage of the document. This assessment is structured as follows. Section 2 discusses the key challenges for public finances in Finland. Section 3 assesses the plausibility of the macroeconomic scenario underpinning the public finance projections of the stability programme against the background of the Commission services' economic forecasts¹. Section 4 analyses budgetary implementation in the year 2009, the budgetary plans for 2010 and the medium-term budgetary strategy. Taking into account risks attached to the budgetary targets, it also assesses the appropriateness of the fiscal strategy in relation to the provisions of the Stability and Growth Pact. Section 5. reviews recent debt developments and medium-term prospects, as well as the long-term sustainability of public finances. Section 6 discusses institutional features of public finances. Finally, Section 7 concludes with an overall assessment of the programme. The annex provides a detailed assessment of compliance with the code of conduct, including an overview of the summary tables from the programme.

¹ This assessment uses the Commission services' 2009 autumn forecast, as published on 3 November 2009, as a benchmark. However, more recent information that has become available has also been taken into account to assess the risks to the programme scenarios.

Table 1. Comparison of key macroeconomic and budgetary projections

		2008	2009	2010	2011	2012	2013
Real GDP (% change)	SP Feb 2010	1.0	-7.6	0.7	2.4	3.5	3.0
	COM Nov 2009	1.0	-6.9	0.9	1.6	n.a.	n.a.
	<i>SP Oct 2008</i>	2.6	0.6	1.8	2.4	2.2	n.a.
HICP inflation (%)	SP Feb 2010	3.9	1.7	1.8	1.7	2.0	2.0
	COM Nov 2009	3.9	1.8	1.6	1.5	n.a.	n.a.
	<i>SP Oct 2008</i>	4.0	2.3	1.9	2.0	2.0	n.a.
Output gap ¹ (% of potential GDP)	SP Feb 2010	3.7	-5.0	-5.0	-4.0	-2.2	-1.2
	COM Nov 2009 ²	3.5	-4.5	-4.3	-3.8	n.a.	n.a.
	<i>SP Oct 2008</i>	1.3	-0.6	-1.0	-1.2	n.a.	n.a.
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	SP Feb 2010	2.7	0.8	1.2	1.5	1.8	2.0
	COM Nov 2009	3.0	1.1	1.2	1.3	n.a.	n.a.
	<i>SP Oct 2008</i>	4.0	3.6	3.7	3.9	3.9	n.a.
General government revenue (% of GDP)	SP Feb 2010	53.4	53.1	52.6	53.4	53.2	52.8
	COM Nov 2009	53.4	51.5	50.5	50.6	n.a.	n.a.
	<i>SP Oct 2008</i>	51.4	50.3	49.7	49.4	49.4	n.a.
General government expenditure (% of GDP)	SP Feb 2010	49.0	55.3	56.2	56.4	55.5	54.7
	COM Nov 2009	48.9	54.3	55.0	55.0	n.a.	n.a.
	<i>SP Oct 2008</i>	47.0	48.2	48.6	48.4	48.5	n.a.
General government balance (% of GDP)	SP Feb 2010	4.4	-2.2	-3.6	-3.0	-2.3	-1.9
	COM Nov 2009	4.5	-2.8	-4.5	-4.3	n.a.	n.a.
	<i>SP Oct 2008</i>	4.4	2.1	1.1	1.0	0.9	n.a.
Primary balance (% of GDP)	SP Feb 2010	5.9	-0.8	-2.3	-1.2	-0.2	0.4
	COM Nov 2009	5.9	-1.4	-3.1	-2.9	n.a.	n.a.
	<i>SP Oct 2008</i>	5.4	4.0	3.3	2.8	2.4	n.a.
Cyclically-adjusted balance ¹ (% of GDP)	SP Feb 2010	2.6	0.3	-1.1	-1.0	-1.2	-1.3
	COM Nov 2009	2.7	-0.5	-2.3	-2.4	n.a.	n.a.
	<i>SP Oct 2008</i>	3.7	2.4	1.7	1.6	n.a.	n.a.
Structural balance ³ (% of GDP)	SP Feb 2010	2.6	0.3	-0.9	-1.0	-1.2	-1.3
	COM Nov 2009	2.7	-0.5	-2.2	-2.4	n.a.	n.a.
	<i>SP Oct 2008</i>	3.7	2.4	1.7	1.6	n.a.	n.a.
Government gross debt (% of GDP)	SP Feb 2010	34.2	41.8	48.3	52.2	54.4	56.4
	COM Nov 2009	34.1	41.3	47.4	52.7	n.a.	n.a.
	<i>SP Oct 2008</i>	32.4	33.0	33.7	34.1	34.6	n.a.

Notes:

¹Output gaps and cyclically-adjusted balances from the programmes as recalculated by Commission services on the basis of the information in the programmes.

²Based on estimated potential growth of 2.1%, 1.0%, 0.7% and 1.1% respectively in the period 2008-2011.

³Cyclically-adjusted balance excluding one-off and other temporary measures. One-off and other temporary measures concern only 2010 when they amount to 0.2% of GDP and are deficit-increasing according to both the most recent programme and the Commission services' November 2009 forecast.

Source:

Stability programme (SP); Commission services' autumn 2009 forecasts (COM); Commission services' calculations.

2. KEY CHALLENGES IN THE ECONOMIC DOWNTURN AND THE POLICY RESPONSE

This section describes recent economic and budgetary developments for Finland, which form the background against which the current programme assessment should be viewed, and outlines the key challenges to be addressed by future economic policies.

After a decade of rapid export-driven growth, Finland entered the global crisis in 2008 from a relatively strong position, having built up a substantial surplus in the current account and in the government finances. Nevertheless, the global crisis has had a strong impact on the export-dominated Finnish industry as well as on the domestic sectors through negative confidence effects. The programme forecasts GDP to decline by 7.6% in 2009, which is close to the preliminary GDP data published by the national statistics office on 1 March 2010, showing a 7.8% contraction in 2009. Finnish industry structure has traditionally been highly concentrated, with 70% of exports generated by metal engineering, electronics, and forestry sectors. With the global economic cycle turning to bust, demand for investment goods plummeted. Over 2009, Finnish exports dropped by the most in the euro area. Apart from the unfavourable composition effect, the sudden appreciation of the euro exchange rate against the currencies of Finland's main trading partners had a relatively strong impact on external trade, given that almost 70% of Finnish exports go outside the euro area, which is the highest share among euro area countries. The weakening of price competitiveness was further accentuated by the previous round of multiannual wage agreements, settled at the height of the economic cycle in 2007, providing exceptionally generous wage rises over the following 2-3 years. At the outset, the global crisis had a sharply negative impact on consumer confidence, even though the expected robust wage growth implied a solid rise in consumer purchasing power in 2008 and 2009. In contrast, over the course of 2009, consumer confidence has quickly rebounded to close to pre-crisis levels. Industry confidence indicators have also rebounded, albeit more moderately. However, the overall marked improvements in economic confidence seem to be only gradually reflected in actual output recovery. The labour market reaction to the crisis has so far been more subdued than could have been expected from the steep fall in output. Unemployment has increased from an average of 6.4% of the labour force recorded in 2008 to 8.2% in 2009. Additionally, temporary lay-offs and various schemes to reduce working time have been commonly used, amounting to almost 3% of the labour force, which to a large extent are not reflected in unemployment statistics. In the medium term, the key challenge relates to the imminent population ageing, which will lead to a gradual reduction of the working age population and further expenditure pressures.

Given the sizeable surplus in public finances recorded in 2008, Finland allowed a full operation of automatic stabilisers and in addition provided for a relatively large discretionary fiscal stimulus amounting to slightly below 2% of GDP in 2009 and a further above 1% of GDP in 2010. The aggregate weakening of general government finances was therefore particularly rapid in 2009, swinging from a surplus of 4.5% of GDP recorded in 2008 to a deficit above 2% of GDP in 2009, as projected in the programme. The government's stimulus measures were announced in several waves over 2008 and 2009. Judging by the budgetary impact, the stimulus is concentrated on revenue-side measures, largely implying permanent tax cuts, also motivated by the government's long term tax policy objectives. Notably, a significant cut was made to personal income tax, a measure that was already part of a longer-term strategy aiming to reduce the relatively high tax burden on labour and thus increase work incentives. It would also provide substantial support for households' purchasing power. The expenditure side measures were less costly from their budgetary impact, but were often designed with a view to provide incentives to kick-start larger investment projects. The majority of the labour market measures relate to training, targeted particularly to youth. The corporate sector- which is most heavily hit by the collapse of global demand- is primarily supported through easing the cost of financing by significantly increasing the funding capacity of various state support schemes for corporate financing (export credit, venture capital, participation in companies' own capital).

3. MACROECONOMIC OUTLOOK

Against the background of the current macroeconomic situation and the main policy challenges set out in the previous section, this section makes an assessment of the plausibility of the macroeconomic scenario underpinning the public finance projections of the programme.

As presented in Table 2, the programme projects economic activity to gradually recover, with GDP expected to grow by 0.7% in 2010, accelerating to 2.4% and 3.5% in 2011 and 2012 respectively, and moderating to 3% in 2013. The programme expects the recovery in 2010 to be export-led, with domestic demand still contributing negatively to growth on account of a continued contraction in investments, even though private consumption is already assumed to turn to modest growth. The recovery is seen to be on firmer ground in 2011 with all the main demand components contributing to growth and the labour market recovering somewhat.

Overall, the programme expects the economic recovery to be slow since the main industrial branches, heavily specialised in investment goods and vulnerable to global production shifts, do not appear to be well placed for rapid expansion once global markets recover. Nevertheless, the programme projects a temporary acceleration of economic activity in 2012, above the estimated GDP growth potential, explained in the programme by exports and investments rebounding to some extent from the present exceptional lows. The programme also assumes employment and wage growth to gather strength in 2012 and 2013, which is in turn reflected in solid private consumption growth and a modest rise in the inflation rate to about 2%. As the programme states, the medium term growth prospects for 2012-2013 are estimated using the production function method commonly adopted by the EU and the Member States. Given that after the severe economic crisis the estimated output gap appears notably large, and the medium term growth estimates assume a closing of the output gap by 2015, the method used results in a GDP growth forecast substantially exceeding the potential growth estimates.

The programme's GDP, inflation and labour market outlook for 2010 and 2011 is broadly in line with the Commission's autumn forecast, which covers the period until 2011². Compared with the Commission forecast, the GDP growth forecast of the programme for 2011 is somewhat higher, primarily on account of a projected stronger recovery in private consumption. This is also reflected in a somewhat higher inflation outlook and a stronger assumed recovery of the labour market. In light of the recently observed continuation of gains in consumer confidence, and labour market stress remaining within forecasted bounds, the more favourable outlook for private consumption could be justified. Given that private consumption forms the tax base for VAT, this discrepancy proportionately carries over to the revenue forecast, assessed in detail in Section 4. The other more minor differences in the composition of GDP growth should in themselves not entail additional risks to public finance projections³. However, the GDP growth forecast beyond 2011, even though derived under a commonly used methodology, can be considered markedly favourable since it is substantially higher than the estimated medium term growth potential. Additionally, given the consolidation needs, fiscal policy will likely not assume an expansionary stance adding to GDP growth over those years and the external competitiveness of many export sectors might

² The external outlook behind the programme's macroeconomic scenario is in line with that of the Commission services' autumn 2009 forecast.

³ The notable discrepancy on forecast for compensation of employees per head regarding 2009 and 2010 should in practice not lead to differences in tax bases in 2010 since the discrepancies work in opposite directions and balance each other out.

still be hampered in the medium term by industry specific competitiveness challenges and the recent relatively sharp wage hikes. Overall, the programme's macroeconomic assumptions are plausible until 2011, but appear markedly favourable thereafter.

The output gap estimates as recalculated by Commission services based on the information in the programme, following the commonly agreed methodology, indicate that the projected improvement in cyclical conditions would lead to a consistent narrowing of the output gap over the programme period. However, since the severe recession has already led to an exceptionally large output gap, estimated in the programme at 5% of GDP in 2009-2010, even the relatively robust recovery projected in the programme would not entirely close the output gap by the end of the programme period.

Although much of the observed decline in actual GDP in the context of the crisis is cyclical, growth in potential output will resume from a lower starting point. In addition, the crisis may also affect potential growth in the medium term through lower investment, constraints in credit availability and increasing structural unemployment. Moreover, the impact of the economic crisis will coincide with the negative effects of demographic ageing on potential output and the sustainability of public finances. Against this background it will be essential to accelerate the pace of structural reforms with the aim of supporting potential growth. In particular, for Finland it is important to undertake reforms to increase labour supply in the longer term in order to counter the negative effects on the labour market from the ageing of the population.

Table 2: Comparison of macroeconomic developments and forecasts

	2009		2010		2011		2012	2013
	COM	SP	COM	SP	COM	SP	SP	SP
Real GDP (% change)	-6.9	-7.6	0.9	0.7	1.6	2.4	3.5	3.0
Private consumption (% change)	-2.8	-2.2	1.0	1.2	1.4	2.5	3.0	2.5
Gross fixed capital formation (% change)	-11.0	-11.6	-2.4	-4.5	1.9	1.8	3.4	3.4
Exports of goods and services (% change)	-25.3	-25.7	4.6	5.0	4.8	5.6	6.5	5.5
Imports of goods and services (% change)	-22.1	-22.5	3.8	3.7	4.2	4.4	4.5	4.0
<i>Contributions to real GDP growth:</i>								
- Final domestic demand	-3.3	-3.3	0.2	-0.2	1.3	1.8	2.4	2.1
- Change in inventories	-1.2	-1.9	0.3	0.3	0.0	0.0	0.2	0.2
- Net exports	-2.4	-2.4	0.3	0.5	0.3	0.5	0.9	0.7
Output gap ¹	-4.5	-5.0	-4.3	-5.0	-3.8	-4.0	-2.2	-1.2
Employment (% change)	-2.9	-3.2	-2.5	-3.1	0.1	0.6	1.2	0.9
Unemployment rate (%)	8.5	8.5	10.2	10.5	9.9	9.6	8.7	8.1
Labour productivity (% change)	-4.1	-4.5	3.4	3.8	1.5	1.8	2.3	2.1
HICP inflation (%)	1.8	1.7	1.6	1.8	1.5	1.7	2.0	2.0
GDP deflator (% change)	2.1	1.1	1.5	1.2	1.5	1.5	2.2	2.1
Comp. of employees (per head, % change)	3.4	2.3	2.7	4.2	1.9	1.9	3.0	3.7
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	1.1	0.8	1.2	1.2	1.3	1.5	1.8	2.0
<u>Note:</u>								
¹ In percent of potential GDP, with potential GDP growth according to the programme as recalculated by Commission services.								
<u>Source:</u>								
Commission services' autumn 2009 forecasts (COM); Stability programme (SP).								

4. GENERAL GOVERNMENT BALANCE

This section consists of four parts. The first three parts discuss the budgetary implementation in the year 2009, the budgetary plans for 2010 and the medium-term budgetary strategy in the programme. The final part analyses the risks attached to the budgetary targets.

4.1. Budgetary implementation in 2009

The programme projects a general government deficit of 2.2% of GDP in 2009. Given the unexpectedly sharp decline in GDP and the repercussions particularly on tax revenues, the expected outcome in 2009 is over 4 p.p. weaker than the surplus of 2.1% of GDP targeted in the previous update of the stability programme. In line with the EERP and the large fiscal space that existed in 2008, Finland provided for a relatively strong and timely fiscal stimulus programme, amounting to almost 2% of GDP in 2009 and above 1% in 2010. The budgetary effects of the economic stimulus packages were for the most part already included into the projections of the 2008 programme and play only a minor role in explaining the difference in 2009 from previous targets. The additional stimulus measures taken during 2009 and thus not included in the programme update of 2008 amount to about ½ % of GDP, divided between both revenue and expenditure measures.

Table 3 compares the projected outcome for the general government balance, revenue and expenditure (as a percentage of GDP) in 2009 as presented in the new stability programme with the targets from the previous update of the programme. Differences between outcome and targets (excluding the impact of unanticipated GDP developments which may have affected the ratio, referred to as the ‘denominator effect’) are decomposed in the impact of a different starting position (i.e. the outcome of 2008 may also have been different from what was anticipated in the previous programme update) and the impact of differences in the revenue / expenditure growth rate from the planned growth rates⁴.

As visible from the table, in 2008 both revenue and expenditures were equally higher than previously projected and thus did not have a carry-over impact on the aggregate general government balance outcome in 2009. The weaker than projected outcome in 2009 arises from a large shortfall in revenue accrual. Given the unexpectedly sharp drop in economic activity, revenue is now assessed to have declined by 7% in 2009 instead of the 0.4% growth expected in the 2008 programme. A more detailed comparison by revenue categories shows that the main shortfalls were due to a sharp drop in income tax accrual, particularly corporate income tax. The other main tax categories (VAT and social security taxes) recorded a more modest shortfall from previous projections. The impact from the expenditure side was minor as expenditure growth in 2009 was only marginally higher than planned in the 2008 stability programme. Given that the labour market has remained relatively resilient in spite of the deep fall in GDP, the effect of the automatic stabilisers on expenditure has been somewhat contained.

⁴ Mathematically, the difference in the revenue ratio in Table 3 can be expressed as:

$$\rho^o - \rho^p = \underbrace{\frac{1+r^p}{1+g^p} \Delta \rho_{-1}}_{\text{Base effect}} + \underbrace{\frac{\rho_{-1}^o}{(1+g^o)(1+g^p)} \Delta r}_{\text{Revenue growth effect}} - \underbrace{\frac{\rho_{-1}^o}{(1+g^o)(1+g^p)} \Delta g}_{\text{Denominator effect}} + \underbrace{\frac{\rho_{-1}^o (r^o g^p - r^p g^o)}{(1+g^o)(1+g^p)}}_{\text{Residual}}$$

where r is the growth rate of revenue and g is the growth rate of GDP. The subscript -1 refers to the previous year's value. Superscripts o and p refer to the outcome and the planned value respectively. Similar for the expenditure ratio.

Compared with the Commission services' autumn 2009 forecast, the programme projections, finalised at a later date and therefore likely based on more recent budgetary information, foresee about ½ % of GDP better outcome in general government net lending in 2009. The discrepancy arises from the revenue side, as the programme expects somewhat stronger revenue accrual in 2009 in all the major tax categories, adding up to ½ % of GDP. This difference would also technically carry over for the following years. Additionally, compared with the Commission services' forecast, the programme's tax projections are also marginally higher in 2010 on all major tax components. The Finnish Statistical Office publication on 1 March 2010 on preliminary non-official data of general government finances indicates that the deficit in 2009 amounted to 2.2% of GDP, thus exactly matching the expectations in the programme⁵.

Table 3: Budgetary implementation in 2009

	2008		2009	
	Planned	Outcome	Planned	Outcome
	SP Dec 2008	SP Feb 2010	SP Dec 2008	SP Feb 2010
Government balance (% of GDP)	4.4	4.4	2.1	-2.2
Difference compared to target ¹	0.0		-4.3	
Difference excluding denominator effect ^{1,2}			-4.8	
<i>Of which:</i> due to a different starting position end 2008			-0.1	
due to different revenue / expenditure growth in 2009			-4.4	
p.m. Residual ³			-0.3	
<i>p.m. Nominal GDP growth (planned and outcome)</i>			2.5	-6.5
Revenue (% of GDP)	51.4	53.4	50.3	53.1
Revenue surprise compared to target ¹	2.0		2.8	
Revenue surprise excluding denominator effect ^{1,2}			-2.2	
<i>Of which:</i> due to a different starting position end 2008			2.0	
due to different revenue growth in 2009			-4.1	
p.m. Residual ³			-0.1	
<i>p.m. Revenue growth rate (planned and outcome)</i>			0.4	-7.0
Expenditure (% of GDP)	47.0	49.0	48.2	55.3
Expenditure surprise compared to target ¹	-2.0		-7.1	
Expenditure surprise excluding denominator effect ^{1,2}			-2.5	
<i>Of which:</i> due to different starting position end 2008			-2.0	
due to different expenditure growth rate in 2009			-0.3	
p.m. Residual ³			-0.2	
<i>p.m. Expenditure growth rate (planned and outcome)</i>			5.1	5.6
Notes:				
¹ A positive number implies that the outcome was better (in terms of government balance) than planned.				
² The denominator effect captures the mechanical effect that, if GDP turns out higher than planned, the ratio of revenue or expenditure to GDP will fall because of a higher denominator. Although the denominator effect can be very significant for revenue and expenditure separately, on the balance they usually largely cancel against each other.				
³ The decomposition leaves a small residual that cannot be assigned to the previous components. The residual is generally small, except in some cases where planned and actual growth rates of revenue, expenditure and GDP differ significantly.				
<i>Source: Commission services</i>				

⁵ While the deficit outcome matches exactly the programme figure, the statistics publication suggests that both nominal revenue and expenditure turned out somewhat lower than projected in the programme.

4.2. The programme's budgetary strategy for 2010

The programme plans for the general government deficit to temporarily breach the 3% of GDP threshold set in the Pact as the deficit is projected to widen to 3.6% of GDP in 2010. The projected increase in the deficit is driven by both a fall in the revenue ratio to GDP and a rise of the expenditure ratio. The decline in the revenue ratio is notably driven by income tax projections, reflecting also the discretionary tax cuts as part of the stimulus programme. The increase in the expenditure ratio arises mainly from social payments, with their ratio to GDP growing by 0.9 p.p. from the previous year, reflecting the operation of automatic stabilisers. The projections included in the programme take account of the 2010 budget bill adopted by the Parliament in December 2009. The central government budget for 2010 plans for budget revenue to fall by 1 p.p. and expenditure to rise by over 5 p.p. compared with 2009. Apart from cyclical factors, this results also from the planned stimulus measures in 2010, estimated to amount to over 1 % of GDP in relation to the previous year. The stimulus measures also constitute the largest discretionary measures of the central government budget for 2010, presented in Table 4.

Table 4. Main budgetary measures for 2010

Revenue measures ¹	Expenditure measures ²
<ul style="list-style-type: none"> • Personal income tax cuts (-0.6% of GDP) • Reducing employer's social security taxation (-0.3% of GDP) • Cuts on VAT on food (-0.2% of GDP) • General VAT rate increase by 1 p.p. (0.2% of GDP) 	<ul style="list-style-type: none"> • Increasing funding for various employment measures (-0.1% of GDP) • Increasing funding for various investments (-0.2% of GDP)
<p><u>Notes:</u></p> <p>¹ Estimated impact on general government revenue</p> <p>² Estimated impact on general government expenditure</p> <p><i>Source: Commission services and Finnish Ministry of Finance 2010 Budget Review</i></p>	

The structural balance, i.e. cyclically adjusted balance net of one-off measures⁶ as recalculated by the Commission services on the basis of the information in the programme, is set to decline by over 1% in 2010 from the previous year (see Table 5), indicating an expansionary fiscal stance in that year. This estimate broadly matches the size of the stimulus measures announced in the programme.

The fiscal performance of different government sectors varies greatly. The deficit is overwhelmingly driven by central government finances, which also includes the more cyclically sensitive revenue and expenditure items. As presented in the programme, the deficit in the central government is projected to approach 6% of GDP in 2010 and will still amount to 4½ % of GDP in 2013. This is however somewhat balanced by a surplus in social security

⁶ The differences between the Commission and the programme presentation of one-off measures are minor, related to the Commission including certain technical changes affecting the Finnish contribution to the EU budget.

funds, consistently exceeding 2½ % of GDP over the programme period, reflecting a steady accumulation of pension funds. Local government finances are seen to remain consistently in a deficit of slightly less than ½ % of GDP.

4.3. The programme's medium-term budgetary strategy

This section describes the medium-term budgetary strategy outlined in the programme - and how it compares with the one in the previous update - as well as the composition of the budgetary adjustment, including the broad measures envisaged.

The main aim of the programme's medium-term budgetary strategy is to support economic activity and the labour market over the economic crisis, at the same time taking account of the fiscal constraints set by long term sustainability needs. While the programme emphasises the importance of achieving a fiscal position safeguarding the long-term sustainability of public finances (estimated by the programme to correspond to a general government surplus of 4% of GDP), it also states that the current fiscal projections based on existing policies do not fulfil this aim. The programme ascertains that the government will decide on budgetary consolidation measures later, specified in the upcoming 2011 budget and in the next stability programme update. The current programme update has revised its medium-term objective (MTO) for the budgetary position, setting it at a structural surplus of 0.5% of GDP (see Box 2). This is lower than the MTO of 2% of GDP set in the previous programme update from 2008. Nevertheless, as the programme states, under current policies the target will not be achieved in the programme period without new, significant measures. The programme does not mention a target year for achieving the MTO. Additionally, the programme mentions the objective set out in the Government Programme of securing by means of employment-enhancing reforms a structural surplus in central government finances of 1% of GDP by the end of the parliamentary term. However, given the exceptional economic recession, the government has declared to show temporary flexibility as regards this particular target.

Box 1: The medium-term objective (MTO) for Finland

As noted in the Code of Conduct⁷, the MTO aims to (a) provide a safety margin with respect to the 3% of GDP deficit limit; (b) ensure rapid progress towards fiscal sustainability; and (c) allow room for budgetary manoeuvre, in particular taking into account the needs for public investment. The MTO is defined in cyclically adjusted terms, net of one-off and other temporary measures. On 7 July 2009, the ECOFIN Council took note of a new methodology for setting MTOs, ensuring that implicit liabilities (costs related to ageing populations, in particular projected healthcare and pension expenditure) are also accounted for.

Specifically, the country-specific MTOs should take into account three components: (i) the debt-stabilising balance for a debt ratio equal to the (60% of GDP) reference value (dependent on long-term potential growth), implying room for budgetary manoeuvre for Member States with relatively low debt; (ii) a supplementary debt-reduction effort for Member States with a debt ratio in excess of the (60% of GDP) reference value, implying rapid progress towards it; and (iii) a fraction of the adjustment needed to cover the present value of the future increase in age-related government expenditure. This implies a partial frontloading of the budgetary cost of ageing irrespective of the current level of debt. In addition to these criteria, MTOs should provide a safety margin with respect

⁷ "Specifications on the implementation of the Stability and Growth Pact and guidelines on the format and content of stability and convergence programmes", endorsed by the ECOFIN Council on 10 November 2009, available at: http://ec.europa.eu/economy_finance/sgp/legal_texts/index_en.htm

to the 3% of GDP deficit reference value and, for euro area and ERM II Member States, in any case not exceed a deficit of 1% of GDP.

As reported in the programme update, the MTO of Finland is a structural surplus of 0.5% of GDP. In view of the new methodology and given the most recent projections and debt level, the MTO appears to reflect the objectives of the Pact.

Table 5: Composition of the budgetary adjustment

(% of GDP)	2008	2009		2010		2011		2012	2013	Change: 2009-2013
	COM	COM	SP	COM	SP	COM ¹	SP	SP	SP	SP
Revenue	53.4	51.5	53.1	50.5	52.6	50.6	53.4	53.2	52.8	-0.3
<i>of which:</i>										
- Taxes on production and imports	12.9	13.1	13.4	12.7	13.3	12.8	14.1	13.8	13.6	0.2
- Current taxes on income, wealth, etc.	17.5	15.7	16.2	15.2	15.8	15.1	15.9	16.0	16.1	-0.2
- Social contributions	12.2	12.4	12.8	12.2	12.9	12.2	12.9	13.0	13.1	0.2
- Other (residual)	10.7	10.3	10.6	10.4	10.5	10.5	10.5	10.4	10.0	-0.6
Expenditure	48.9	54.3	55.3	55.0	56.2	55.0	56.4	55.5	54.7	-0.6
<i>of which:</i>										
- Primary expenditure	47.5	53.0	53.9	53.6	54.8	53.5	54.6	53.4	52.4	-1.5
<i>of which:</i>										
Compensation of employees	13.4	14.7	14.7	14.8	14.7	14.7	14.5	14.1	13.8	-0.9
Intermediate consumption	9.5	10.5	10.9	10.8	11.2	10.9	11.4	11.1	10.7	-0.2
Social payments	17.7	20.0	20.5	20.4	21.3	20.3	21.3	20.8	20.6	0.1
Subsidies	1.3	1.5	1.5	1.5	1.5	1.5	1.5	1.5	1.5	0.0
Gross fixed capital formation	2.6	2.8	2.8	2.8	2.7	2.7	2.7	2.6	2.5	-0.3
Other (residual)	3.1	3.4	3.5	3.4	3.4	3.4	3.3	3.3	3.3	-0.2
- Interest expenditure	1.4	1.4	1.4	1.4	1.4	1.5	1.7	2.1	2.3	0.9
General government balance (GGB)	4.5	-2.8	-2.2	-4.5	-3.6	-4.3	-3.0	-2.3	-1.9	0.3
Primary balance	5.9	-1.4	-0.8	-3.1	-2.3	-2.9	-1.2	-0.2	0.4	1.2
One-off and other temporary measures	0.0	-0.1	0.0	-0.1	-0.2	0.0	0.0	0.0	0.0	0.0
GGB excl. one-offs	4.5	-2.7	-2.2	-4.4	-3.4	-4.3	-3.0	-2.3	-1.9	0.3
Output gap ²	3.5	-4.5	-5.0	-4.3	-5.0	-3.8	-4.0	-2.2	-1.2	3.8
Cyclically-adjusted balance ²	2.7	-0.5	0.3	-2.3	-1.1	-2.4	-1.0	-1.2	-1.3	-1.6
Structural balance³	2.7	-0.5	0.3	-2.2	-0.9	-2.4	-1.0	-1.2	-1.3	-1.6
<i>Change in structural balance</i>		<i>-3.1</i>	<i>-2.4</i>	<i>-1.8</i>	<i>-1.2</i>	<i>-0.2</i>	<i>-0.1</i>	<i>-0.2</i>	<i>-0.1</i>	
Structural primary balance ³	4.1	0.9	1.7	-0.8	0.5	-0.9	0.7	0.9	1.0	-0.7
<i>Change in structural primary balance</i>		<i>-3.2</i>	<i>-2.4</i>	<i>-1.7</i>	<i>-1.2</i>	<i>-0.1</i>	<i>0.3</i>	<i>0.1</i>	<i>0.1</i>	
Notes:										
¹ On a no-policy-change basis.										
² Output gap (in % of potential GDP) and cyclically-adjusted balance according to the programme as recalculated by Commission services on the basis of the information in the programme.										
³ Structural (primary) balance = cyclically-adjusted (primary) balance excluding one-off and other temporary measures.										
Source:										
Stability programme (SP); Commission services' autumn 2009 forecasts (COM); Commission services' calculations										

As presented in Table 5, the headline and primary deficits are expected by the programme to gradually narrow from 2011 onwards, with the headline deficit reaching about 2% of GDP in 2013. The corresponding structural balance projection shows a deficit below 1½ % of GDP in 2013, which is short of the government's MTO target of a structural surplus of ½ % of GDP. The change in structural balance (as recalculated by the Commission services' on the basis of the information in the programme), indicates that the fiscal policy stance turns neutral starting from 2011. This is in line with the programme scenario built on a no-policy change assumption and given that the government has not yet announced any major measures beyond 2010.

The gradual reduction of the deficit ratio over 2011-2013 is largely driven by relative expenditure restraint. While the expenditure ratio to GDP is still set to increase in 2010, on account of both a relatively stagnant growth in nominal GDP and a relatively rapid nominal expenditure growth (reflecting the stimulus measures and robust growth in public sector wages), expenditure ratio to GDP is subsequently projected to turn to a steady decline. It is expected in the programme that the central government mid-term expenditure ceilings and ongoing productivity programmes at both the central- and local government levels would prove effective in curbing expenditure growth below nominal GDP growth.

The change in the revenue to GDP ratio over 2011-2013 is relatively flat. Comparing the revenue subcategories between the programme update and the Commission services' forecast, the only notable difference in both nominal terms and as a ratio to GDP relates to the projected "taxes on production and imports" accrual in 2011, where the programme projects a stronger rise. As discussed in section 3, this largely reflects the programme's assumption of a stronger rebound in private consumption, forming the tax base for VAT. Additionally, the planned rise in energy taxation by €750 million or 0.4% of GDP in 2011 was not included into the Commission services' autumn forecast done under a strictly no-policy change assumption since the government's announcement to raise energy taxation was not yet passed into legislation. The decision to raise the general VAT rate by 1 p.p. in July 2010 is taken account of in a similar magnitude in both forecasts. Beyond 2011, the VAT ratio to GDP is set to stabilise in the programme projections. The role of one-off measures in the projected consolidation path is insignificant.

4.4. Risk assessment

This section discusses the plausibility of the programme's budgetary projections by analysing various risk factors. For the period until 2011, Table 5 compares the detailed revenue and expenditure projections in the Commission services' autumn 2009 forecast, which are derived under a no-policy change scenario, with those in the updated programme. However, although the assessment uses the Commission services' forecast as a benchmark, it also takes explicitly into account all available information about more recent developments.

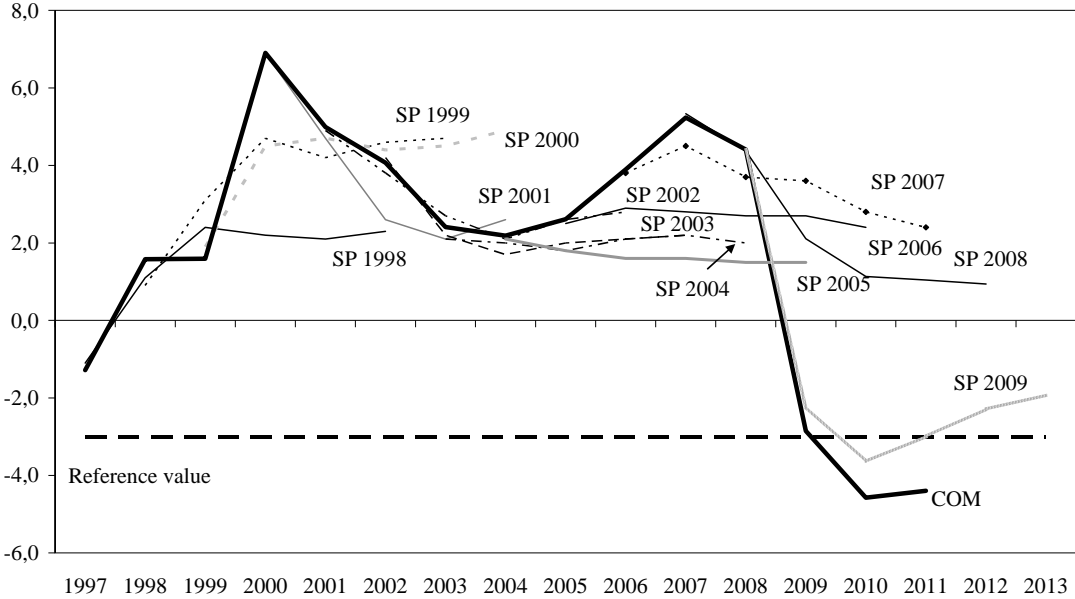
As discussed in Section 3, the programme projects growth to be more buoyant in 2011 than the Commission services' forecast. This arises mainly from the programme assuming a sharper recovery of private consumption, which is in turn reflected in projected higher VAT revenue in 2011. The risks arising from the more favourable growth outlook for 2011 are somewhat mitigated by the latest trends in consumer confidence and business outlook indicators indeed anticipating a continued recovery in economic activity. For 2012-2013, the programme assumes a gradual closure of the output gap over the medium term (by 2015) and thus projects growth rates well above the potential GDP estimate. The programme update includes a sensitivity analysis, modelling also the impact to budgetary targets from a 1% lower GDP growth scenario than the baseline. In case of a lower growth scenario, the programme projects the general government deficit to settle at around 4% of GDP and debt ratio to approach, but not exceed 60% of GDP by 2013.

While the Commission services' forecast the general government deficit ratio to be almost 1½ p.p. higher by 2011 than projected in the programme, ½ p.p. of it is explained by the programme expecting a better outcome in 2009, which would carry over to the following years (see the discussion in Section 4.1). Also, the programme projections include the planned rise of energy taxation by 0.4% of GDP in 2011, which is not yet included into legislation and not reflected in the Commission services' autumn 2009 forecast. However, it will likely not

give rise to major risks to the budgetary targets. Past track record has shown strong commitment to fulfil planned tax measures in due course. For the outer years, the programme projects the VAT ratio to GDP to remain constant, which should not give rise to any significant risks.

Somewhat offsetting the potentially optimistic revenue projections in 2011, also expenditure growth is assumed in the programme to be higher in that year than in the Commission services' forecast, primarily on account of social costs. Given that the two forecasts have broadly similar labour market projections, the programmes expenditure projection can be considered cautious for that year. The foreseen gradual reduction of the expenditure ratio to GDP in the outer years of the programme might be undermined by expenditure pressures in the local governments, especially given the projected increase in costs related to population ageing. While central government expenditure ceilings have a good track record in containing expenditure and reaching the budgetary targets, aside from for the exceptional year 2009 (see Figure 1), local government expenditures are not bound by similar restrictions. Past experience has shown that local governments are able to compensate for expenditure pressures by increasing local tax rates and some other measures⁸, thus containing the rise of municipal net lending by pushing up the tax burden. However, in view of national fiscal policy these solutions are often not the most optimal ones (a more detailed discussion in Section 6).

Figure 1: Government balance projections in successive programmes (% of GDP)



Source: Commission services' autumn 2009 forecast (COM) and successive stability programmes

Even though the programme projections are built on a no policy change assumption, the programme ascertains that the government will decide at a later date on a comprehensive fiscal consolidation strategy, also in view of the population ageing challenge. Some work for this end appears to be already undergoing in the form of government initiated working groups

⁸ See the discussion on local government finances presented in the Annex 1 of the previous Stability Programme assessment

examining reform options for social security, taxation and structural measures to boost economic growth.

The overall balance of risks indicates that the budgetary outcomes projected in the programme are subject to downside risks. While the risks to the more immediate growth outlook are limited as the latest forward-looking indicators confirm a relatively robust and continuous recovery of consumer confidence and albeit less so, of business confidence, the budgetary outcome in the outer years may be worse than projected given the markedly favourable growth assumptions underlying the budgetary projections. The risks to the targets are somewhat counterbalanced by the commitment of the government to specify exit measures in the 2011 budget and the next stability programme update.

5. GOVERNMENT DEBT AND LONG-TERM SUSTAINABILITY

This section is in two parts. A first part describes recent debt developments and medium-term prospects, including risks to the outlook presented in the programme. A second part takes a longer-term perspective with the aim of assessing the long-term sustainability of public finances.

5.1. Recent debt developments and medium-term prospects

5.1.1. Debt projections in the programme

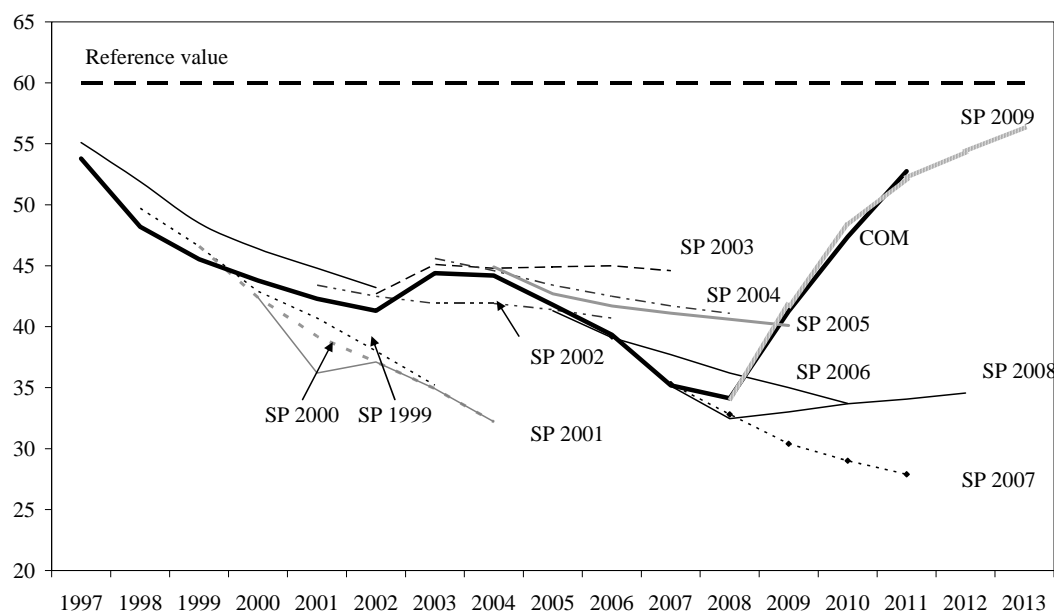
After years of steady decline, the gross debt ratio to GDP turned to a relatively rapid rise in 2009, reflecting the sharp weakening of the budgetary position and the rapid fall in nominal GDP impacting on the denominator of the calculated ratio to GDP. As an additional but relatively minor factor, some of the stimulus measures related to financial investments impact on the debt level even if they are not counted into the government deficit in ESA95 terms. The gross debt ratio in 2009 is projected in the programme update to have increased sharply from the preceding year, up by almost 8 p.p., reaching 41.8% of GDP (see Table 6). The upward trend is projected to continue, but at a decelerating pace as GDP returns on a growth path and the primary deficit is set to narrow in the outer years of the programme period. The gross debt ratio is projected in the programme to reach 56.4% of GDP by 2013.

Compared with the previous Stability programme update from 2008, which projected only a modest rise in the gross debt ratio to 34.6% of GDP by 2012, the new outlook for debt developments is markedly weaker (see Figure 2). This arises in the main from the unforeseen rapid weakening in primary balances, largely reflecting the deficit and borrowing need in central government finances. Local government deficits and borrowing have increased to a much lesser degree given that the major cyclically sensitive budgetary items are included in the central government sector and that local governments can offset expenditure pressures by rising municipal taxes and benefiting from higher central government transfers. The social security funds continue to show a surplus, reflecting the accumulation of assets to pension schemes, which does however not impact general government gross debt⁹. In Table 6, the stock flow adjustment largely corresponds to the accumulation of these financial assets. The crash in the global financial markets at the end of 2008 reduced the value of the pension fund assets by over 10% of GDP in that year. However, the pension schemes' consolidated

⁹ Under the assumption that these assets are invested outside the general government sector.

financial assets, amounting to about 52.4% of GDP in 2008, still exceeded government gross debt.

Figure 2: Debt projections in successive programmes (% of GDP)



Source: Commission services' autumn 2009 forecast (COM) and successive stability programmes

Table 6: Debt dynamics

(% of GDP)	average 2003-07	2008	2009		2010		2011		2012	2013
			COM	SP	COM	SP	COM	SP	SP	SP
Gross debt ratio¹	41.0	34.1	41.3	41.8	47.4	48.3	52.7	52.2	54.4	56.4
Change in the ratio	-1.2	-1.1	7.2	7.7	6.1	6.5	5.4	3.9	2.2	2.0
<i>Contributions²:</i>										
1. Primary balance	-4.9	-5.9	1.4	0.8	3.1	2.3	2.9	1.2	0.2	-0.4
2. "Snow-ball" effect	-0.3	0.5	3.1	3.8	0.5	0.6	0.1	-0.1	-0.7	-0.4
<i>Of which:</i>										
Interest expenditure	1.5	1.4	1.4	1.4	1.4	1.4	1.5	1.7	2.1	2.3
Growth effect	-1.4	-0.4	2.5	2.8	-0.4	-0.3	-0.7	-1.1	-1.7	-1.5
Inflation effect	-0.4	-0.6	-0.8	-0.4	-0.6	-0.5	-0.7	-0.7	-1.1	-1.1
3. Stock-flow adjustment	4.0	4.3	2.6	3.0	2.6	3.6	2.5	2.8	2.7	2.8
<i>Of which:</i>										
Cash/accruals diff.	-0.2	0.0		n.a.		n.a.		n.a.	n.a.	n.a.
Acc. financial assets	4.2	4.4		3.3		3.0		2.9	3.0	3.0
<i>Privatisation</i>	-0.8	0.0		-0.2		-0.2		-0.2	-0.2	-0.2
Val. effect & residual	-0.1	-0.1		2.1		-0.2		-2.0	-3.1	-2.9

Notes:

¹End of period.

²The snow-ball effect captures the impact of interest expenditure on accumulated debt, as well as the impact of real GDP growth and inflation on the debt ratio (through the denominator). The stock-flow adjustment includes differences in cash and accrual accounting, accumulation of financial assets and valuation and other residual effects.

Source:

Stability programme (SP); Commission services' autumn 2009 forecasts (COM); Commission services' calculations

5.1.2. Assessment

The gross debt projections presented in the programme are broadly in line with the Commission services' autumn forecast over 2009-2011. As visible in Table 6, while the Commission forecast the general government deficit (reflected under "primary balance") to remain higher over the years 2009-2011, the discrepancies regarding the forecast of the stock flow adjustment compensate for this. However, a more notable difference relates to the growth rate of the debt ratio in 2011, when the discrepancy between the two forecasts on general government deficit is also widening. This points to a risk that the expected recovery in GDP and fiscal balances should turn out weaker than expected in the programme's baseline scenario, the increase in the gross debt ratio would be correspondingly faster. As suggested by the sensitivity analysis carried out in the programme, the debt ratio is nevertheless not projected to exceed the 60% of GDP ceiling stipulated by the Stability and Growth Pact.

As mentioned already in section 4.1., the Finnish Statistics Office published on 1 March 2010 preliminary data on general government finances, showing the debt ratio to have reached 44% of GDP in 2009. This is more than 2 pp. higher than projected in the programme and the discrepancy would also carry over to the following years.

5.2. Long-term debt projections and the sustainability of public finances

5.2.1. Sustainability indicators and long-term debt projections

This section presents sustainability indicators based on the long-term age-related government spending as projected by the Member States and the EPC in 2009 according to an agreed methodology¹⁰.

Table 7 shows that age-related spending is projected to rise by 5.9 percentage points of GDP between 2010 and 2060, above the EU average (4.6 pps.). Sustainability indicators for two scenarios are presented in Table 8. 'The 2009 scenario' is based on a no-policy-change assumption and the 2009 structural primary balance as a starting year, while 'the programme scenario' takes into account the consolidation planned in the programme up to 2013 and is based on the projected 2013 structural primary balance as a starting position. Assuming that the structural primary balance remained at its 2009 level, the sustainability gap (S2)¹¹ would amount 4.3% of GDP, about 4½ percentage points more than in last years assessment, which is due to both a lower estimated structural primary balance in the starting year and a higher rise in age-related expenditure in the 2009 projections than in the previous ones.

The "programme scenario" projects a lower structural primary balance situation at the end of the programme period. Risks to long-term sustainability of public finances would increase, as shown by the sustainability gap (S2) reaching 7.0% of GDP.

¹⁰ Economic Policy Committee and the European Commission (2009), '2009 Ageing Report: Economic and budgetary projections for the EU-27 Member States (2008-60)', *European Economy* No. 2/2009. European Commission (2009), 'Sustainability Report 2009', *European Economy* No. 9/2009. European Commission (2008), 'Public finances in EMU – 2008', *European Economy* No. 4/2008..

¹¹ The S2 indicator is defined as the change in the current level of the structural primary balance required to make sure that the discounted value of future structural primary balances (including the path of property income) covers the current level of debt.

Table 7: Long-term age-related expenditure: main projections

(% of GDP)	2007	2010	2020	2030	2040	2060	
	Change 2010- 60						
Total age-related spending	24.2	24.7	27.2	29.7	30.4	30.5	5.9
- Pensions	10.0	10.7	12.6	13.9	13.6	13.4	2.6
- Healthcare	5.5	5.6	6.0	6.3	6.5	6.5	0.8
- Long-term care	1.8	1.9	2.4	3.1	3.9	4.4	2.5
- Education and unemployment benefits	6.9	6.4	6.2	6.4	6.4	6.4	0.0
Property income received	4.4	4.1	3.8	3.3	3.0	2.7	-1.5

Source: Economic Policy Committee and Commission services.

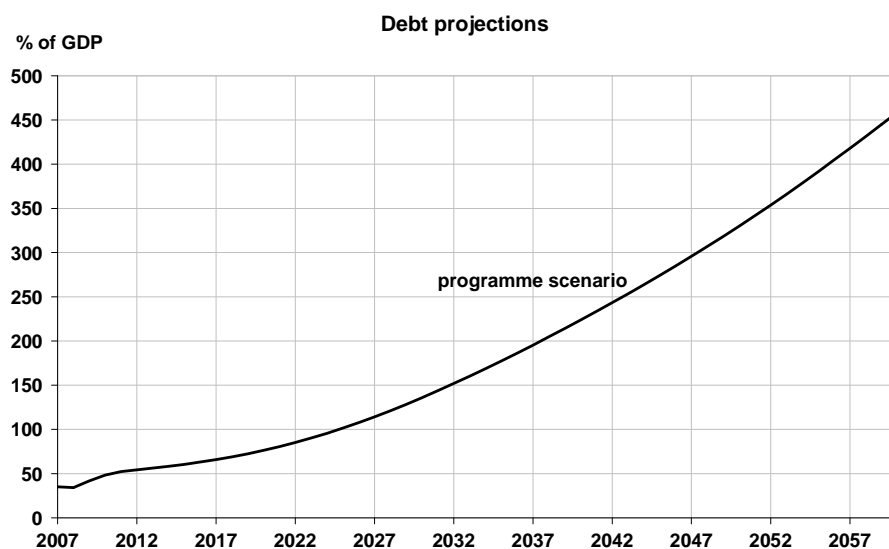
Table 8: Sustainability indicators and the required primary balance

Value	2009 scenario			Programme scenario		
	S1	S2	RPB	S1	S2	RPB
Value	3.1	4.3	5.1	6.0	7.0	5.2
<i>of which:</i>						
Initial budgetary position (IBP)	-0.1	0.2	-	2.7	3.0	-
Debt requirement in 2060 (DR)	-0.2	-	-	-0.1	-	-
Long-term change in the primary balance (LTC)	3.3	4.1	-	3.3	4.1	-

Source: Commission services.

Based on the assumptions used in the projection of the age-related expenditure and the calculation of the sustainability indicators, Figure 3 displays the projected debt-to-GDP ratio over the long-term.

Figure 3: Long-term projections for the government debt ratio



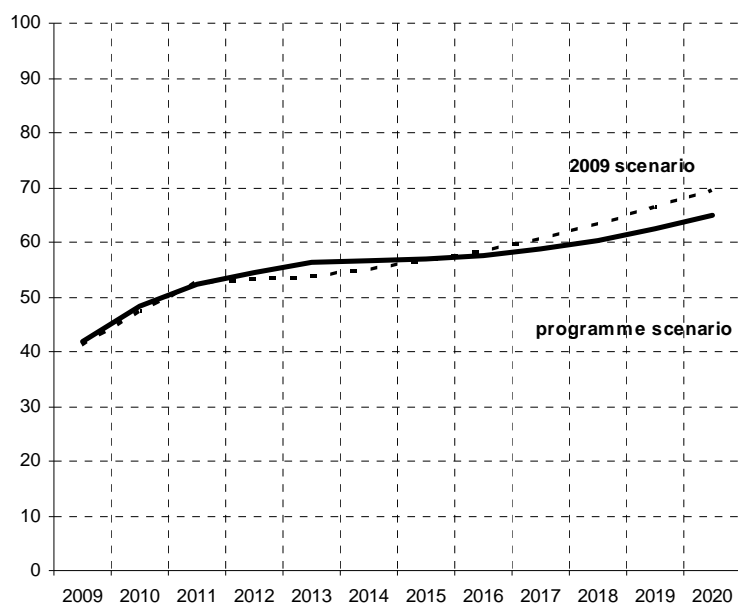
Note: Being a mechanical, partial-equilibrium analysis, the long-term debt projections are bound to show highly accentuated profiles. As a consequence, the projected evolution of debt levels should not be seen as a forecast similar to the Commission services' short-term forecasts, but as an indication of the risks faced by Member States.

Source: Commission services.

Based on the alternative assumptions of economic developments presented in Commission services' autumn 2009 forecast publication¹², Figure 4 shows projected medium-term trajectory of the debt-to-GDP ratio.

Figure 4: Medium-term projections for the government debt ratio

¹² Section 3.5 in European Commission (2009), 'European Economic Forecast – autumn 2009', European Economy No. 10/2009. This economic scenario assumes that the output gap caused by the crisis will be closed by 2017.



Source: Commission services' calculations

5.2.2. Additional factors

For an overall assessment of the sustainability of public finances, other relevant factors are taken into account, as shown in Table 9. Large assets accumulated in the public pension schemes, over 50% of GDP in 2008, will help to finance a part of the future increase in the pension expenditure. On the other hand, among the factors that weigh on the sustainability risk are the decline in the structural primary balance and the alternative national projections on age-related expenditure presented in the programme. The latter leads to a somewhat higher rise in age-related expenditure compared to the common EPC projections. Taken together, additional factor do not change the overall assessment of the long-term sustainability.

Table 9: Additional factors for the assessment of long-term sustainability risks.

	Impact on risk
Debt and pension assets	+
Decline in structural balance until 2011 in COM Autumn 2009 forecast	--
Alternative projection of cost of ageing	-
Strong decline in benefit ratio	na
High tax burden	na
Difference between S1 and S2	na

*Note: '-' : factor tends to increase the risk to sustainability, '+' : factor tends to decrease the risk to sustainability.
'na': not applicable.*

Alternative projections are often presented in the programmes, whose assumptions often diverge from the common method. Projections currently discussed in the Economic Policy Committee but not yet published, are for the time being also considered "unofficial".

An explanation on these factors can be found in chapter V of: European Commission (2009), Sustainability Report 2009, European Economy No. 9/2009.

Source: Commission services.

5.2.3. Assessment

While the long-term budgetary impact of ageing is slightly higher than on average in the EU, enacted pension reforms have helped to contain the projected increase in pension expenditure over the coming decades. Moreover, the large assets accumulated by the public pension funds will help finance a part of the future increase in pension expenditure. The budgetary position in 2009, as estimated in the programme, compounds the budgetary impact of population ageing on the sustainability gap. Ensuring high primary surpluses over the medium term and implementing appropriate structural reforms would contribute to limiting the medium¹³ risks to the sustainability of public finances. Medium-term debt projections that assume GDP growth rates to only gradually recover to the values projected before the crisis and tax ratios to return to pre-crisis levels show that the budgetary strategy envisaged in the programme, taken at face-value, would not be sufficient to stabilise the debt by 2020.

6. INSTITUTIONAL FEATURES OF PUBLIC FINANCES

This section is subdivided into two elements: the fiscal framework and the quality of public finances in a broader sense.

6.1. Fiscal framework

The main tool in controlling central government budget expenditure continues to be the multiannual spending limits procedure, whereby expenditure items are revised only for changes in the price and cost levels. The spending limits exclude cyclically sensitive expenditure items, making up about ¼ of total central government budget. It has therefore allowed the full operation of automatic stabilisers, supporting economic activity and social cohesion over the crisis period, but providing no mechanism to counter the relatively sharp downward swing in public finances driven by revenue shortfalls. Given that the post recession recovery is usually a slower process than the initial downturn into an economic crisis, the expected cyclical recovery will regenerate fiscal gains with a long lag. Additional measures might thus be needed to rebalance the fiscal position even with the economic recovery expected to take hold.

Given its good track record, the spending ceilings can be expected to remain an effective tool in containing non-cyclical central government expenditure. As noted in the programme, its institutional setup will likely remain broadly stable over the programme period, with some relatively minor development initiatives foreseen to further increase the clarity and transparency of the present framework. The programme recognises that more emphasis should be given to formulating a post-crisis exit strategy and developing fiscal policy rules with a view of long-term sustainability of public finances.

Local governments, having large constitutionally granted self-governance rights, are not bound by centrally imposed expenditure limits. Growth in local government expenditure has therefore exceeded central government performance in the past years. To compensate for the high expenditure growth, local governments can relatively easily increase their revenues, notably by raising local taxes, also central government transfers have been increased over past

¹³ In the Commission's 2009 Sustainability Report the risks to the sustainability of public finances were assessed as low

years (for a more detailed discussion see Annex 1 of the previous stability programme assessment). However, the tax increases at the local government level might go against the national tax policy strategy. Overall, a credible framework to contain expenditure rises at the local government level would be highly desirable.

6.2. Quality of public finances

The programme update has not altered the government's reform strategy concerning the reorganisation of service provision both at the central and local government level. These reforms have already in the main been under implementation over several past years. The central government has defined ambitious targets to reduce its personnel over the medium term as part of a productivity programme, with the double aim of increasing productivity and adjusting to a shrinking workforce in the face of population ageing. It is planned to reduce central government staff by about 12% over 2007-2015 mainly through natural attrition.

The central government attempts to bring about municipal service reforms through guidance, soft enforcement and incentives, leaving the local governments a high degree of self-determination. The aim is to achieve productivity increases in municipally provided services, which would in turn contain expenditure pressures. To this end, a framework law promoting the reform of local governments' structure and their service provision was passed by the parliament in the beginning of 2007. The reform aims to achieve an increase in productivity and efficiency through both economies of scale (forming larger municipalities) and innovations in service provision. An important facet of the reform is redesigning the state transfer system, with a view of enhancing transparency, productivity and cost efficiency¹⁴. Currently, most progress has been made in forming larger municipal entities. In the main the service provision reforms will yet have to shift to an implementation phase. In practice this means various innovations in service provision, more effective use of ICT, possibly a greater involvement of the private and non-profit sectors, identification and dissemination of best practices, etc. Overall, the hoped-for productivity gains at the local government level would materialise only in the medium- to long run.

7. OVERALL ASSESSMENT

Taking into account risks attached to the budgetary targets discussed above, this section assesses the appropriateness of the fiscal strategy in relation to the budgetary objectives of the Stability and Growth Pact, against the background of the current economic situation, the debt and long-term sustainability position of the country, and the institutional features of its public finances.

Overall, taking into account the risks to the budgetary targets mentioned above, the strategy to maintain supportive fiscal policies also in 2010 can be considered in line with the EERP. Following the negative effects of the economic crisis, the general government deficit limit of 3% of GDP is projected to be temporarily breached in 2010, gradually abating below the reference value thereafter. However, in view of the risks to the growth projections in the outer years of the programme, even the planned moderate reduction in the deficit may not be achieved. The projected fiscal stance, as measured by the change in structural balances, does not indicate fiscal consolidation to take hold in the medium term and the programme does not envisage progress towards its MTO within the programme period. While the programme

¹⁴ Finnish Ministry of Finance (2008) Talouspolitiikan strategia 2008, Kuntatalouden haastet (Economic Policy Strategy 2008, Challenges for Municipal Finances)

states that a consolidation strategy is being planned, it does not specify its precise objectives or main elements. A timely implementation of a comprehensive strategy aiming at a structural fiscal consolidation would be necessary to bring the budgetary strategy in line with the requirements of the Pact.

* * *

ANNEX. COMPLIANCE WITH THE FORMAT AND CONTENT REQUIREMENTS FOR STABILITY AND CONVERGENCE PROGRAMMES

This annex provides an assessment of whether the programme respects the requirements of Section II of the code of conduct (guidelines on the format and content), notably as far as (i) the model structure (Annex 1 of the code of conduct); (ii) the formal data provisions (Annex 2 of the code of conduct); and (iii) other information requirements is concerned.

(i) Model structure

The programme broadly follows the model structure for stability and convergence programmes specified in Annex 1 of the code of conduct.

(ii) Data requirements

With regard to data requirements, the programme has gaps in the compulsory and optional data prescribed by the new code of conduct. The external assumptions are not provided for the outer years of the programme period. Optional data “liquid financial assets” specified in the Code of conduct Annex 2 Table 4 point 6 is not given for 2009-2013 in the stability programme.

Beyond the requirements of the code of conduct, the stability programme includes a breakdown of pension fund assets in Finland.

The tables on the following pages show the data presented in the February 2010 update of stability programme, following the structure of the tables in Annex 2 of the code of conduct. Compulsory data are in bold, missing data are indicated with grey-shading.

(iii) Other information requirements

The table below provides a summary assessment of the adherence to the other information requirements in the code of conduct.

The SCP...	Yes	No	Comments
<i>a. Involvement of parliament</i>			
... mentions status vis-à-vis national parliament.	x		
... indicates whether Council opinion on previous programme has been presented to national parliament.	x		
<i>b. Economic outlook</i>			
... (for euro area and ERM II Member States) uses “common external assumptions” on main extra-EU variables.	x		
... explains significant divergences with Commission services’ forecasts ¹ .		x	
... bears out possible upside/downside risks to economic outlook.	x		
... analyses outlook for sectoral balances and, especially for countries with high external deficit, external balance.	x		
<i>c. Monetary/exchange rate policy</i>			
... (CP only) presents medium-term monetary policy objectives and their relationship to price and exchange rate stability.			<i>not applicable</i>
<i>d. Budgetary strategy</i>			
... presents budgetary targets for general government balance in relation to MTO and projected path for debt ratio.	x		
... (in case new government has taken office) shows continuity with respect to budgetary targets endorsed by Council.			<i>not applicable</i>
... (when applicable) explains reasons for deviations from previous targets and, in case of substantial deviations, whether measures are taken to rectify situation (+ provides information on them).	x		
... backs budgetary targets by indication of broad measures necessary to achieve them and analyses their quantitative effects on balance.	x		

The SCP...	Yes	No	Comments
... specifies state of implementation of measures.	x		
<i>e. "Major structural reforms"</i>			
... (if MTO not yet reached or temporary deviation is planned from MTO) includes comprehensive information on economic and budgetary effects of possible 'major structural reforms' over time.			<i>not applicable</i>
... includes quantitative cost-benefit analysis of short-term costs and long-term benefits of reforms.			<i>not applicable</i>
<i>f. Sensitivity analysis</i>			
... includes comprehensive sensitivity analyses and/or develops alternative scenarios showing impact on balance and debt of: a) changes in main economic assumptions b) different interest rate assumptions c) (for CP only) different exchange rate assumptions d) if common external assumptions are not used, changes in assumptions for main extra-EU variables.	x		
... (in case of "major structural reforms") analyses how changes in assumptions would affect budget and potential growth.			<i>not applicable</i>
<i>g. Broad economic policy guidelines</i>			
... provides information on consistency with broad economic policy guidelines of budgetary objectives and measures to achieve them.	x		
<i>h. Quality of public finances</i>			
... describes measures to improve quality of public finances, both revenue and expenditure sides.	x		
<i>i. Long-term sustainability</i>			
... outlines strategies to ensure sustainability.	x		
... includes common budgetary projections by the AWG and all necessary additional information (esp. new relevant information).	x		
<i>j. Other information (optional)</i>			
... includes information on implementation of existing national budgetary rules and on other institutional features of public finances.	x		
<p><u>Notes:</u> SCP = stability/convergence programme; CP = convergence programme ¹To the extent possible, bearing in mind the typically short time period between the publication of the Commission services' autumn forecast and the submission of the programme.</p> <p><u>Source:</u> <i>Commission services</i></p>			

Tables from Annex 2 of the code of conduct

Table 1a. Macroeconomic prospects

	ESA Code	2008	2008	2009	2010	2011	2012	2013
		Level	rate of change	rate of change	rate of change	rate of change	rate of change	rate of change
1. Real GDP	B1*g	165.294	1.0	-7.6	0.7	2.4	3.5	3.0
2. Nominal GDP	B1*g	184.728	2.8	-6.5	1.9	4.0	5.7	5.2
Components of real GDP								
3. Private consumption expenditure	P.3	95.574	1.9	-2.2	1.2	2.5	3.0	2.5
4. Government consumption expenditure	P.3	41.273	2.0	1.2	0.2	0.5	0.5	0.5
5. Gross fixed capital formation	P.51	38.098	0.3	-11.6	-4.5	1.8	3.4	3.4
6. Changes in inventories and net acquisition of valuables (% of GDP)	P.52 + P.53	2.0	1.1	-1.3	-0.9	-0.6	-0.1	0.4
7. Exports of goods and services	P.6	86.761	7.3	-25.7	5.0	5.6	6.5	5.5
8. Imports of goods and services	P.7	79.582	7.0	-22.5	3.7	4.4	4.5	4.0
Contributions to real GDP growth								
9. Final domestic demand		-	1.5	-3.3	-0.2	1.8	2.4	2.1
10. Changes in inventories and net acquisition of valuables	P.52 + P.53	-	-0.9	-1.9	0.3	0.0	0.2	0.2
11. External balance of goods and services	B.11	-	0.5	-2.4	0.5	0.5	0.9	0.7

Table 1b. Price developments

	ESA Code	2008	2008	2009	2010	2011	2012	2013
		Level	rate of change	rate of change	rate of change	rate of change	rate of change	rate of change
1. GDP deflator		<i>n.a.</i>	1.8	1.1	1.2	1.5	2.2	2.1
2. Private consumption deflator		<i>n.a.</i>	3.4	1.0	1.5	1.7	2.0	2.0
3. HICP¹		<i>n.a.</i>	3.9	1.7	1.8	1.7	2.0	2.0
4. Public consumption deflator		<i>n.a.</i>	5.3	3.2	2.6	2.8	3.0	3.0
5. Investment deflator		<i>n.a.</i>	3.9	-1.5	-1.3	-0.6	2.0	2.0
6. Export price deflator (goods and services)		<i>n.a.</i>	-1.6	-5.1	1.5	1.6	0.5	0.0
7. Import price deflator (goods and services)		<i>n.a.</i>	1.8	-6.6	2.0	2.4	1.5	1.0

¹ Optional for stability programmes.

Table 1c. Labour market developments

	ESA Code	2008	2008	2009	2010	2011	2012	2013
		Level	rate of change	rate of change	rate of change	rate of change	rate of change	rate of change
1. Employment, persons¹		2531	1.6	-3.2	-3.1	0.6	1.2	0.9
2. Employment, hours worked ²		4321	1.3	-6.6	-2.0	0.3	1.0	0.7
3. Unemployment rate (%)³		172	6.4	8.5	10.5	9.6	8.7	8.1
4. Labour productivity, persons⁴		65.30778	-0.5	-4.5	3.8	1.8	2.3	2.1
5. Labour productivity, hours worked ⁵		38.25364	-0.3	-1.1	2.7	2.1	2.5	2.3
6. Compensation of employees	D.1	73.136	6.8	-1.0	1.0	2.5	4.2	4.6
7. Compensation per employee		28.89609	5.2	2.3	4.2	1.9	3.0	3.7

¹Occupied population, domestic concept national accounts definition.

²National accounts definition.

³Harmonised definition, Eurostat; levels.

⁴Real GDP per person employed.

⁵Real GDP per hour worked.

Table 1d. Sectoral balances

% of GDP	ESA Code	2008	2009	2010	2011	2012	2013
1. Net lending/borrowing vis-à-vis the rest of the world	B.9	2.7	0.8	1.2	1.5	1.8	2.0
<i>of which :</i>							
- Balance on goods and services		3.9	2.1	2.5	2.7	3.1	3.3
- Balance of primary incomes and transfers		-1.3	-1.4	-1.4	-1.3	-1.4	-1.4
- Capital account		0.1	0.1	0.1	0.1	0.1	0.1
2. Net lending/borrowing of the private sector	B.9	-1.2	3.5	5.4	5.0	4.6	4.4
3. Net lending/borrowing of general government	EDP B.9	4.4	-2.2	-3.6	-3.0	-2.3	-1.9
4. Statistical discrepancy		-0.5	-0.5	-0.5	-0.5	-0.5	-0.5

Table 2. General government budgetary prospects

	ESA Code	2008	2008	2009	2010	2011	2012	2013
		Level	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP
Net lending (EDP B.9) by sub-sector								
1. General government	S.13	8145	4.4	-2.2	-3.6	-3.0	-2.3	-1.9
2. Central government	S.1311	1635	0.9	-4.5	-5.8	-5.2	-4.7	-4.5
3. State government	S.1312	<i>n.a.</i>	<i>n.a.</i>	<i>n.a.</i>	<i>n.a.</i>	<i>n.a.</i>	<i>n.a.</i>	<i>n.a.</i>
4. Local government	S.1313	-351	-0.2	-0.5	-0.4	-0.3	-0.4	-0.3
5. Social security funds	S.1314	6861	3.7	2.7	2.5	2.6	2.8	2.8
General government (S13)								
6. Total revenue	TR	98576	53.4	53.1	52.6	53.4	53.2	52.8
7. Total expenditure	TE ¹	90431	49.0	55.3	56.2	56.4	55.5	54.7
8. Net lending/borrowing	EDP B.9	8145	4.4	-2.2	-3.6	-3.0	-2.3	-1.9
9. Interest expenditure	EDP D.41	2719	1.5	1.4	1.4	1.7	2.1	2.3
10. Primary balance²		10864	5.9	-0.8	-2.3	-1.2	-0.2	0.4
11. One-off and other temporary measures³		0	0.0	0.0	-0.2	0.0	0.0	0.0
Selected components of revenue								
12. Total taxes (12=12a+12b+12c)		57336	30.8	29.9	29.3	30.2	30.0	29.9
12a. Taxes on production and imports	D.2	24364	12.9	13.4	13.3	14.1	13.8	13.6
12b. Current taxes on income, wealth, etc	D.5	32321	17.5	16.2	15.8	15.9	16.0	16.1
12c. Capital taxes	D.91	651	0.4	0.2	0.2	0.2	0.2	0.2
13. Social contributions	D.61	22527	12.2	12.8	12.9	12.9	13.0	13.1
14. Property income	D.4	9338	5.1	4.3	4.1	4.2	4.2	4.3
15. Other⁴		9375	5.3	6.0	6.2	6.1	5.9	5.5
16=6. Total revenue	TR	98576	53.4	53.1	52.6	53.4	53.2	52.8
p.m.: Tax burden (D.2+D.5+D.61+D.91-D.995)⁵		79410.0	42.7	42.5	42.0	42.8	42.9	42.8
Selected components of expenditure								
17. Compensation of employees + intermediate consumption	D.1+P.2	42187	22.8	25.6	25.9	25.8	25.2	24.5
17a. Compensation of employees	D.1	24698	13.4	14.7	14.7	14.5	14.1	13.8
17b. Intermediate consumption	P.2	17489	9.5	10.9	11.2	11.4	11.1	10.7
18. Social payments (18=18a+18b)		32665	17.7	20.5	21.3	21.3	20.8	20.6
18a. Social transfers in kind supplied via market producers	D.6311, D.63121, D.63131	4233	2.3	2.6	2.6	2.7	2.6	2.6
18b. Social transfers other than in kind	D.62	28432	15.4	17.9	18.6	18.6	18.2	18.0
19=9. Interest expenditure	EDP D.41	2719	1.5	1.4	1.4	1.7	2.1	2.3
20. Subsidies	D.3	2451	1.3	1.5	1.5	1.5	1.5	1.5
21. Gross fixed capital formation	P.51	4771	2.6	2.8	2.7	2.7	2.6	2.5
22. Other⁶		5638	3.1	3.5	3.4	3.3	3.3	3.3
23=7. Total expenditure	TE ¹	90431	49.0	55.3	56.2	56.4	55.5	54.7
p.m.: Government consumption (nominal)	P.3	41273	22.3	25.0	25.2	25.1	24.6	24.2

¹Adjusted for the net flow of swap-related flows, so that TR-TE=EDP B.9.

²The primary balance is calculated as (EDP B.9, item 8) plus (EDP D.41, item 9).

³A plus sign means deficit-reducing one-off measures.

⁴P.11+P.12+P.131+D.39+D.7+D.9 (other than D.91).

⁵Including those collected by the EU and including an adjustment for uncollected taxes and social contributions (D.995), if appropriate.

⁶D.29+D4 (other than D.41)+ D.5+D.7+D.9+P.52+P.53+K.2+D.8.

Table 3. General government expenditure by function

% of GDP	COFOG Code	2007	2012
1. General public services	1	6.2	6.8
2. Defence	2	1.4	1.7
3. Public order and safety	3	1.2	1.3
4. Economic affairs	4	4.4	4.7
5. Environmental protection	5	0.3	0.6
6. Housing and community amenities	6	0.4	0.4
7. Health	7	6.6	7.8
8. Recreation, culture and religion	8	1.1	1.6
9. Education	9	5.8	6.7
10. Social protection	10	19.9	23.9
11. Total expenditure (=item 7=23 in Table 2)	TE ¹	47.3	55.5

¹Adjusted for the net flow of swap-related flows, so that TR-TE=EDP B.9.

Table 4. General government debt developments

% of GDP	ESA Code	2008	2009	2010	2011	2012	2013
1. Gross debt¹		34.2	41.8	48.3	52.2	54.4	56.4
2. Change in gross debt ratio		-1.0	7.6	6.5	3.9	2.2	2.0
Contributions to changes in gross debt							
3. Primary balance²		5.9	-0.8	-2.3	-1.2	-0.2	0.4
4. Interest expenditure³	EDP D.41	1.5	1.4	1.4	1.7	2.1	2.3
5. Stock-flow adjustment		3.4	5.4	2.9	0.9	-0.1	0.1
<i>of which:</i>							
- Differences between cash and accruals ⁴		n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
- Net accumulation of financial assets ⁵		3.9	3.3	3.0	2.9	3.0	3.0
<i>of which:</i>		-	-	-	-	-	-
- privatisation proceeds		-0.2	-0.2	-0.2	-0.2	-0.2	-0.2
- Valuation effects and other ⁶		-0.5	2.1	-0.2	-2.0	-3.1	-2.9
p.m.: Implicit interest rate on debt⁷		4.1	3.8	3.9	3.8	4.2	4.4
Other relevant variables							
6. Liquid financial assets ⁸		69.7	n.a.	n.a.	n.a.	n.a.	n.a.
7. Net financial debt (7=1-6)		-35.5	n.a.	n.a.	n.a.	n.a.	n.a.

¹As defined in Regulation 3605/93 (not an ESA concept).

²Cf. item 10 in Table 2.

³Cf. item 9 in Table 2.

⁴The differences concerning interest expenditure, other expenditure and revenue could be distinguished when relevant.

⁵Liquid assets, assets on third countries, government controlled enterprises and the difference between quoted and non-quoted assets could be distinguished when relevant.

⁶Changes due to exchange rate movements, and operation in secondary market could be distinguished when relevant.

⁷Proxied by interest expenditure divided by the debt level of the previous year.

⁸AF1, AF2, AF3 (consolidated at market value), AF5 (if quoted in stock exchange; including mutual fund shares).

Table 5. Cyclical developments

% of GDP	ESA Code	2008	2009	2010	2011	2012	2013
1. Real GDP growth (%)		1.0	-7.6	0.7	2.4	3.5	3.0
2. Net lending of general government	EDP B.9	4.4	-2.2	-3.6	-3.0	-2.3	-1.9
3. Interest expenditure	EDP D.41	1.5	1.4	1.4	1.7	2.1	2.3
4. One-off and other temporary measures¹		n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
5. Potential GDP growth (%)		2.0	0.9	0.8	1.6	1.5	1.7
contributions:							
- labour		0.2	-0.5	-0.4	0.2	0.0	0.1
- capital		0.7	0.3	0.2	0.2	0.2	0.2
- total factor productivity		1.1	1.1	1.1	1.2	1.2	1.3
6. Output gap		3.6	-5.0	-5.2	-4.3	-2.5	-1.2
7. Cyclical budgetary component		1.8	-2.5	-2.6	-2.2	-1.2	-0.6
8. Cyclically-adjusted balance (2 - 7)		2.6	0.3	-1.1	-0.8	-1.0	-1.3
9. Cyclically-adjusted primary balance (8 + 3)		4.1	1.7	0.3	0.9	1.0	1.0
10. Structural balance (8 - 4)		n.a.	n.a.	n.a.	n.a.	n.a.	n.a.

¹A plus sign means deficit-reducing one-off measures.

Table 6. Divergence from previous update

	ESA Code	2008	2009	2010	2011	2012	2013
Real GDP growth (%)							
Previous update		2.6	0.6	1.8	2.4	2.2	n.a.
Current update		1.0	-7.6	0.7	2.4	3.5	3.0
Difference		-1.6	-8.2	-1.1	0.0	1.3	n.a.
General government net lending (% of GDP)	EDP B.9						
Previous update		4.4	2.1	1.1	1.0	0.9	n.a.
Current update		4.4	-2.2	-3.6	-3.0	-2.3	-1.9
Difference		0.0	-4.3	-4.7	-4.0	-3.2	n.a.
General government gross debt (% of GDP)							
Previous update		32.4	33.0	33.7	34.1	34.6	n.a.
Current update		34.2	41.8	48.3	52.2	54.4	56.4
Difference		1.8	8.8	14.6	18.1	19.8	n.a.

Table 7. Long-term sustainability of public finances

% of GDP	2008	2015	2020	2030	2060	n.a.
Total expenditure	49.0	51.4	54.0	58.2	71.4	n.a.
Of which: age-related expenditures	24.6	26.4	28.0	30.2	31.5	n.a.
Pension expenditure	10.7	12.1	13.2	14.3	13.7	n.a.
Social security pension	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Old-age and early pensions	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Other pensions (disability, survivors)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Occupational pensions (if in general government)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Health care	5.1	5.3	5.5	5.8	6.3	n.a.
Long-term care (<i>this was earlier included in the</i>	1.9	2.2	2.5	3.3	4.9	n.a.
Education expenditure	5.6	5.5	5.5	5.6	5.4	n.a.
Other age-related expenditures	-	-	-	-	-	n.a.
Interest expenditure	1.8	2.5	3.5	5.4	17.4	n.a.
Total revenue	53.4	49.9	51.3	50.7	49.5	n.a.
Of which: property income	5.1	4.3	5.7	5.1	3.9	n.a.
<i>Of which</i> : from pensions contributions (or social contributions if appropriate)	8.1	8.8	9.1	9.7	9.7	n.a.
Pension reserve fund assets	54.8	63.1	67.5	67.8	63.2	n.a.
<i>Of which</i> : consolidated public pension fund assets (assets other than government liabilities)	42.4	50.7	55.1	55.4	50.8	n.a.
Assumptions						
Labour productivity growth	n.a.	1.8	1.7	1.7	1.7	n.a.
Real GDP growth	n.a.	2.0	1.6	1.7	1.7	n.a.
Participation rate males (aged 20-64)	n.a.	82.9	83.9	85.2	85.4	n.a.
Participation rates females (aged 20-64)	n.a.	79.3	80.3	81.6	81.9	n.a.
Total participation rates (aged 20-64)	n.a.	81.1	82.1	83.5	83.7	n.a.
Unemployment rate	n.a.	7.0	6.4	6.4	6.5	n.a.
Population aged 65+ over total population	n.a.	17.3	22.7	26.8	28.7	n.a.

Table 8. Basic assumptions

	2008	2009	2010	2011	2012	2013
Short-term interest rate¹ (annual average)	4.6	1.3	1.5	2.5	n.a.	n.a.
Long-term interest rate (annual average)	4.3	3.7	3.7	4.0	n.a.	n.a.
USD/€ exchange rate (annual average) (euro area and ERM II countries)	1.47	1.39	1.48	1.48	n.a.	n.a.
Nominal effective exchange rate	2.1	1.6	0.5	0.0	n.a.	n.a.
(for countries not in euro area or ERM II) exchange rate vis-à-vis the € (annual average)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
World excluding EU, GDP growth	3.8	-0.4	3.8	4.1	n.a.	n.a.
EU GDP growth	0.8	-4.1	0.7	1.6	n.a.	n.a.
Growth of relevant foreign markets	3.6	-13.8	2.2	4.4	n.a.	n.a.
World import volumes, excluding EU	4.6	-12.6	4.6	5.0	n.a.	n.a.
Oil prices (Brent, USD/barrel)	98.5	61.3	76.5	80.5	n.a.	n.a.