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Recommendation for a
COUNCIL RECOMMENDATION
on the National Reform Programme 2011 of Finland
and delivering a Council opinion
on the updated Stability Programme of Finland, 2011-2014
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COUNCIL RECOMMENDATION

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THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Articles 121(2) and 148(4) thereof,

Having regard to Council Regulation (EC) No 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies¹, and in particular Article 5(3) thereof,

Having regard to the recommendation of the European Commission²,

Having regard to the conclusions of the European Council,

Having regard to the opinion of the Employment Committee,

After consulting the Economic and Financial Committee,

Whereas:

- (1) On 26 March 2010, the European Council agreed to the European Commission's proposal to launch a new strategy for jobs and growth, Europe 2020, based on enhanced coordination of economic policies, which will focus on the key areas where action is needed to boost Europe's potential for sustainable growth and competitiveness.
- (2) On 13 July 2010, the Council adopted a recommendation on the broad guidelines for the economic policies of the Member States and the Union (2010 to 2014) and on 21 October 2010, adopted a decision on guidelines for the employment policies of the Member States,³ which together form the "integrated guidelines". Member States were invited to take the integrated guidelines into account in their national economic and employment policies.

¹ OJ L 209, 2.8.1997, p. 1.

² OJ C , p. .

³ Maintained for 2011 by Council Decision 2011/308/EU of 19 May 2011.

- (3) On 12 January 2011, the Commission adopted the first Annual Growth Survey, marking the start of a new cycle of economic governance in the EU and the first European semester of ex-ante and integrated policy coordination, which is anchored in the Europe 2020 strategy.
- (4) On 25 March 2011, the European Council endorsed the priorities for fiscal consolidation and structural reform (in line with the Council's conclusions of 15 February and 7 March 2011 and further to the Commission's Annual Growth Survey). It underscored the need to give priority to restoring sound budgets and fiscal sustainability, reducing unemployment through labour market reforms and making new efforts to enhance growth. It requested Member States to translate these priorities into concrete measures to be included in their Stability or Convergence Programmes and National Reform Programmes.
- (5) On 25 March 2011, the European Council also invited the Member States participating in the Euro Plus Pact to present their commitments in time to be included in their Stability or Convergence Programmes and their National Reform Programmes.
- (6) On 6 April 2011, Finland submitted its 2011-2014 Stability Programme update and its 2011 National Reform Programme. In order to take account of the interlinkages, the two programmes have been assessed at the same time.
- (7) At the trough of the global economic crisis, Finland experienced a very steep fall in GDP, given that the Finnish economy has traditionally been reliant on the export performance of its main industries. In 2009, GDP contracted by 8.2%, driven by an exceptionally steep fall in exports (20% fall in volume) and related adverse confidence effects on investment. The unemployment rate increased by about 2 percentage points, rising from 6.4% of the labour force in 2008 to 8.3% in 2010. The economic recovery has been strong, with GDP expanding by 3.1% in 2010, sustained by both domestic demand and a rebound in exports. After a brief dip in 2009, real-estate prices and housing construction volumes rebounded rapidly to above the pre-crisis levels, raising some concern about excessive expansion of the real-estate market. Finland emerged from the economic crisis with a general government deficit at 2.5% of GDP in 2010 and debt at 48.5% of GDP.
- (8) Based on the assessment of the updated Stability Programme pursuant to Council Regulation (EC) No 1466/97, the Council is of the opinion that the macroeconomic scenario underlying the programme is plausible for 2011-2012, but slightly too favourable thereafter. For 2011-2012, the macroeconomic scenario is in line with the Commission services' Spring forecast. For 2013-2015, the programme projects growth of about 2% of GDP, which is slightly above the potential growth estimate of 1.5% and could therefore be subject to some downside risks. The objective of the budgetary strategy is to bring the deficit down to 0.9% of GDP in 2011 and 0.7% in 2012, reflecting the cyclical improvement in the economy and some consolidation measures already decided by the previous government. However, the Stability Programme update does not plan any further fiscal consolidation over 2013-2015. Risks to the budgetary targets appear to be balanced. The most notable risk factor stems from the global macroeconomic environment, which has traditionally had a strong impact on the export-reliant Finnish economy.

- (9) The latest programme update does not envisage making use of the forecast improvement in economic conditions for budgetary consolidation in the medium term. While the medium-term objective (MTO), set by the Finnish authorities of a structural surplus of 0.5% of GDP, is projected to be achieved in 2011, in the following years, the structural balance is set to fall below the target.
- (10) Taking action to counter the effects of population ageing has been one of the priorities of successive Finnish governments. Reflecting these efforts, Finland appears to be at medium risk with regard to the long-term sustainability of public finances. Nevertheless, the country faces a strong and immediate demographic shift and a notable sustainability gap still exists in public finances. This challenge has implications for many policy areas. Population ageing will lead to a significant rise in demand for ageing-related services, which are mostly provided by local governments in Finland. Various studies have found that productivity improvement in public services has been poor over the past few years. The Finnish authorities have already implemented several reforms to restructure public services and boost productivity at both central and local government level. The relatively large investments in information technology in the public sector have not yet shown up in productivity improvements, implying that structural and administrative changes are needed to accompany investments. Overall, there is still room for additional measures to achieve productivity gains and cost savings in public service provision.
- (11) The current increase in long-term unemployment is a cause for concern. Between 2005 and 2008, long-term unemployment fell substantially, but it began to rise again in 2009. At the end of March 2011, the number of long-term unemployed stood at 57 400, up 12 400 on the previous year. Many of the long-term unemployed are currently in the 55–64 age group. Due to retirement patterns, the greatest increase in unemployment will be among 45–54 year-olds. Although the long-term unemployment rate in Finland is below the EU average, the issue should be looked at in the context of securing labour supply in the future and social inclusion. Experience shows that long-term unemployment, in particular, increases the risk of poverty and social exclusion. Although the Finnish authorities recognise the increase in long-term unemployment as a pressing issue, so far no comprehensive strategy has been designed to combat it. Finland expanded its active labour market policy (ALMP) measures efficiently during the crisis to fight youth unemployment. While this helped to reduce youth unemployment over 2010–2011, it still remains above the EU average, and may warrant new measures. In the same way, reinforcement and better targeting of ALMP measures would help to reverse the negative trend in long-term unemployment..
- (12) In view of demographic changes, raising the employment rate of older workers is important for public finances and crucial to meet the demand for labour in the future. The Finnish pension system was reformed in 2005 and pension benefits were linked to a life-expectancy coefficient in 2009. However, the statutory pension age is currently not linked to life expectancy. Given the continuing increase in life expectancy, such a link would not only contribute to labour supply but also help to ensure adequate pensions. Early retirement schemes have been reduced over the last few years, but there is still some room for further measures to enhance employment incentives among the elderly. For example, the extended unemployment benefit for the elderly functions broadly in the same way as the abolished unemployment pension. Despite improvements over the last decade, employment rates of older workers and the

effective exit age are low by Nordic standards. Disability is very often the cause of early retirement. Increasing the effective retirement age requires measures that also take into account the quality of working life, including the well-being and health of employees. This is important in particular in view of the high number of people on disability pensions. Since 2009, Finland has spent about EUR 14 million on projects to improve the working environment. The impact of these initiatives merits to be assessed. Participation in lifelong learning has traditionally been very high in Finland and will continue to be important given emerging new skills requirements and demographic changes.

- (13) Greater competition, particularly in the services sector, has become increasingly relevant for boosting productivity and enhancing potential economic growth. Finland's remote location and sparse population density weakens business competition, resulting in relatively low productivity growth in non-tradable sectors. Existing business structures are occasionally highly concentrated, particularly in the food industry or wholesale and retail trade. This might contribute to the relatively high consumer price level, although long transport distances could also play a role. Retail prices are among the highest in the EU. Competition in the retail trade continues to be partly hindered by regulations, despite some recent loosening, and by barriers to foreign and domestic enterprises entering and exiting the market.
- (14) Specific commitments under the Euro Plus Pact are not explicitly set out in Finland's Stability and National Reform Programmes but are expected to be submitted once the new government has been formed.
- (15) The Commission has assessed the Stability Programme and National Reform Programme⁴, taking into account not only their relevance for sustainable fiscal and socio-economic policy in Finland but also their conformity with EU rules and guidance, given the need to reinforce the overall economic governance of the European Union. It considers that consolidation measures should be specified for the medium term and that further action is needed to improve the sustainability of public finances, including by boosting public sector productivity. Further action is also needed to increase incentives to work and to raise the effective exit age from the labour market, as well as to enhance productivity and competition in the service sector markets.
- (16) In light of this assessment, also taking into account the Council Recommendation under Article 126(7) Treaty on the Functioning of the European Union of 2 June 2010, the Council has examined the 2011 update of the Stability Programme of Finland and its opinion⁵ is reflected in particular in its recommendations under (1) and (2) set out below. Taking into account the European Council conclusions of 25 March 2011, the Council has examined the National Reform Programme of Finland,

⁴ SEC(2011) 734.

⁵ Foreseen in Article 5(3) of Council Regulation (EC) No 1466/97.

HEREBY RECOMMENDS that Finland should take action within the period 2011-2012 to:

- (1) Continue the fiscal consolidation using any windfall revenue to reduce the deficit, while taking additional measures to maintain the fiscal position above the medium-term objective.
- (2) Take further measures to achieve productivity gains and cost savings in public service provision, including structural changes, in order to respond to the challenges arising from population ageing.
- (3) Target active labour market measures better on the long-term unemployed and young people.
- (4) Take measures to improve the employability of older workers and their participation in lifelong learning. Take further steps to discourage early exit from the labour market and further link the statutory retirement age limits to life expectancy.
- (5) Take further measures to open up further the service sector, by redesigning the regulatory framework and removing restrictions in order to facilitate new entry into service sector markets, especially in the retail sector.

Done at Brussels,

*For the Council
The President*