EUROPEAN
COMMISSION

Brussels, 22.11.2017
C(2017) 8016 final

# COMMISSION OPINION

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## on the Draft Budgetary Plan of Finland

{SWD(2017) 516 final}

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GENERAL CONSIDERATIONS

1. Regulation (EU) No 473/2013 sets out provisions for enhanced monitoring of budgetary policies in the euro area for ensuring that national budgets are consistent with the economic policy guidance issued in the context of the Stability and Growth Pact (SGP) and the European Semester for economic policy coordination.

2. Article 6 of Regulation (EU) No 473/2013 requires Member States to submit annually to the Commission and to the Eurogroup a Draft Budgetary Plan presenting by 15 October the main aspects of the budgetary situation of the general government and its subsectors for the forthcoming year.

CONSIDERATIONS CONCERNING FINLAND

3. On the basis of the Draft Budgetary Plan for 2018 submitted on 5 October 2017 by Finland, the Commission has adopted the following opinion in accordance with Article 7 of Regulation (EU) No 473/2013.

4. Finland is subject to the preventive arm of the SGP and should ensure sufficient progress towards its medium term budgetary objective (MTO) of a structural balance of -0.5% of GDP. On 11 July 2017, the Council recommended Finland to achieve its medium term budgetary objective taking into account the allowances linked to unusual events, to the implementation of the structural reforms and to investments. . As its public debt exceeds the 60% of GDP reference value of the Treaty, Finland also needs to comply with the debt reduction benchmark.

5. The macroeconomic scenario underlying the Draft Budgetary Plan is plausible. While the Stability Programme submitted in April 2017 had forecast growth to reach 1.2% in 2017 and to accelerate to 1.8% in 2018, the Draft Budgetary Plan has revised growth expectations upwards to 2.9% in 2017 and to 2.1% in 2018. According to the Commission 2017 autumn forecast, the Finnish economy is expected to grow by 3.3% in 2017 and by 2.7% in 2018. In the Commission forecast the key drivers for the projected growth in both 2017 and 2018 are the same as in the Draft Budgetary Plan forecast, i.e. investment and net exports, but the Commission expects somewhat stronger growth from both. In light of the Commission forecast, the national projections are to some extent cautious.

6. Finland complies with the requirement of Regulation EU No 473/2013 which stipulates that the draft budget has to be based on independently produced or endorsed macroeconomic forecasts. The macroeconomic forecasts underlying the Draft Budgetary Plan have been produced by the Economics department of the Ministry of Finance, which is by law independent in its forecast functions.

7. The Draft Budgetary Plan projects a headline deficit of 1.2% of GDP in 2017 and 1.4% of GDP in 2018. The structural balance[1] is estimated at -0.7% of GDP in 2017 and -1.2% of GDP in 2018. Government debt is projected at 62.5% of GDP and 61.9% of GDP in 2018. These projections point to a somewhat improved state of Finland's public finances in comparison to those presented in the 2017 Stability Programme as the macroeconomic developments and outlook have strengthened.

8. In its 2017 Stability Programme, Finland indicated that the budgetary impact of the exceptional inflow of refugees is significant and should be considered as an unusual event outside the control of the government, as defined in Article 5.1 and Article 6.3 of Regulation (EC) No 1466/97. In the 2017 Stability Programme, Finland stated that the expenditure was 0.34% of GDP in 2016 and would decline to 0.19% of GDP in 2017. The provisions set out in Article 5(1) and Article 6(3) of Regulation (EC) No 1466/97 cater for this additional expenditure, in that the inflows of refugees are exceptional events, their impact on the country's public finances is significant and sustainability would not be compromised by allowing for a deviation from the adjustment path towards the MTO.Finland’s Draft Budgetary Plan for 2018 does not present any information on expenditure related to the inflow of refugees. In the absence of up-to-date information regarding the evolution of these costs in the Draft Budgetary Plan, the Commission's assessment is based on the figures reported in the 2017 Stability Programme. The Commission will make a final assessment, including on the eligible amounts, in spring 2018 on the basis of observed data as provided by the authorities.

9. The Draft Budgetary Plan for 2018 contains a few fiscal measures at a very aggregate level. Households' earned income taxes and contributions to social security will be reduced while expenditure cuts continue in central government. The Commission 2017 autumn forecast broadly confirms the projections for deficit and debt presented in the Draft Budgetary Plan for 2018. Generally, the projections for debt reduction are very similar, but the drivers for the debt ratio differ. Regarding 2018, the Commission expects higher nominal growth than the Draft Budgetary Plan, resulting in a lower debt-to-GDP ratio, but this is offset by a somewhat larger assumption on debt increasing stock-flow adjustment. If the stock-flow adjustment remains at exceptionally low levels, the debt ratio could surprise positively in 2018.

10. On 22 May 2017, the Commission issued a report under Article 126(3) TFEU, as Finland's debt-to-GDP ratio was 63.1% of GDP in 2016. The report concluded that, after the assessment of all relevant factors, the debt criterion should be considered as complied with.

11. Based on the Draft Budgetary Plan for 2018 and the Commission 2017 autumn forecast, the debt reduction benchmark is projected to be met in 2017 and 2018

12. In 2017, for Finland to comply with the requirements of the preventive arm, the structural balance should not worsen more than by 1% of GDP. This allowed deterioration takes into account the temporary allowances linked to the structural reform clause (0.5% of GDP) and to the investment clause (0.1% of GDP), as well as the previously granted allowance on the basis of an unusual event (inflow of

[1] Cyclically adjusted balance net of one-off and temporary measures, recalculated by the Commission using the commonly agreed methodology.

refugees), which are carried forward for a period of three years (0.2% of GDP)[2], and an estimated structural balance in the previous year that was slightly above the MTO. According to the information provided in the Draft Budgetary Plan, the expenditure benchmark of 1.9% (in real terms) will be complied with. The structural balance pillar on the basis of a recalculated output gap also points to compliance. The Commission forecast confirms these projections, as both pillars similarly point to compliance. This conclusion would not change in the case that the expected drop in refugee related costs, as reported in the Stability Programme, was to be taken into account in the assessment.

In 2018, Finland is required to respect its MTO taking into account the above-mentioned temporary deviations. This is consistent with a maximum nominal growth rate of net primary government expenditure of 2.1% (in nominal terms), corresponding to an annual structural adjustment of -0.2% of GDP. According to the information provided in the Draft Budgetary Plan, the nominal growth rate of government expenditure in 2018, net of discretionary revenue measures and one-offs, will not exceed the applicable expenditure benchmark rate. The recalculated structural balance is projected to deviate by 0.3% of GDP from the required adjustment. The Commission 2017 autumn forecast confirms these projections. The growth rate of government expenditure in 2018, net of discretionary revenue measures, will not exceed the applicable expenditure benchmark rate, while the change in the structural balance would deviate by 0.1% of GDP from the required adjustment. It appears that the change in the structural balance pillar is negatively impacted by significant revenue shortfalls, worth about 0.6% of GDP, driven by less tax-rich growth than suggested by standard elasticities. Taking this factor into account, the Commission 2017 autumn forecast and the Draft Budgetary Plan point to compliance with the required adjustment in 2018. This conclusion would not change in the case that the expected drop in refugee related costs, as reported in the Stability Programme, was to be taken into account in the assessment.

13. Since 2016, Finland has consolidated public finances mainly by reducing central government expenditure by cutting appropriations and reducing and freezing social transfers. At the same time, taxes on earned income have been reduced, and indirect taxes and excise duties have been increased. For 2018, Finland's Draft Budgetary Plan contains a small unfinanced reduction of labour taxes and social security contributions, thereby continuing the gradual shift away from taxation of earned income (favouring small income earners) towards indirect taxation. As for the recommendations contained in the Council Recommendation of 11 July 2017[3] on healthcare and social services, the implementation of the reform has been postponed by one year to 2020. The reforms to raise employment rate are advancing while the decision to open passenger railway services to competition has been taken. According to the Draft Budgetary Plan, these measures would address directly the country-specific recommendations given to Finland by the Council.

14. Overall, the Commission is of the opinion that the Draft Budgetary Plan of Finland, which is currently under the preventive arm and subject to the debt reduction

[2] Member States at the MTO are allowed to depart from it for up to three years to ensure equal treatment with those on the adjustment path towards the MTO.

[3] Council Recommendation of 11 July 2017 on the 2017 National Reform Programme of Finland and delivering a Council opinion on the 2017 Stability Programme of Finland (OJ C 261, p.114-118, 9.8.2017)

benchmark, is compliant with the provisions of the Stability and Growth Pact. The Commission invites the authorities to implement the 2018 budget.

The Commission is also of the opinion that Finland has made some progress with regard to the structural part of the fiscal recommendations contained in the Council Recommendation of 11 July 2017 in the context of the 2017 European Semester and invites the authorities to make further progress. A comprehensive assessment of progress made with the implementation of the country-specific recommendations will be made in the 2018 Country Reports and in the context of the country-specific recommendations to be proposed by the Commission in May 2018.

Done at Brussels, 22.11.2017

*For the Commission*
*Pierre MOSCOVICI*
*Member of the Commission*