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COMMISSION OPINION

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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 2015 submitted on 2 October 2014 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 Stability and Growth Pact and should preserve a sound fiscal position which ensures compliance with the medium-term budgetary objective (MTO). On 8 July 2014 the Council recommended that Finland should limit the emerging gap relative to the MTO in 2014, ensure to return to it in 2015 and respect it thereafter as planned, also to ensure that the debt criterion is fulfilled, while pursuing a growth-friendly fiscal policy.

5. After lower-than-expected real GDP growth in the first half of 2014, Finland's economic outlook has worsened since the Stability Programme was presented. The macroeconomic scenario underlying the Draft Budgetary Plan appears somewhat optimistic for 2014 and 2015. It forecasts economic activity to stay flat in 2014 and grow by 1.2% in 2015, while the Commission forecasts a 0.4% real GDP decline in 2014 and growth of 0.6% for 2015.

6. Regulation (EU) No 473/2013 requires the draft budget to be based on independently endorsed or produced macroeconomic forecasts. The macroeconomic forecasts underlying the Draft Budgetary Plan have been produced by the Economics department of the Ministry of Finance. Legal provisions to ensure the independence of this department for the forecasting activities are still under preparation.

7. The Draft Budgetary Plan forecasts the nominal deficit at 2.7% of GDP in 2014, up from 2.0% in the Stability Programme. Around half of the increase is explained by the switch to ESA 2010, while the rest is explained by lower than previously expected GDP growth and revenues that are forecast to grow by less than the standard revenue elasticity would suggest. For 2015, the difference in the general government balance between the Draft Budgetary Plan and the Stability Programme is markedly larger. The Draft Budgetary Plan forecasts the deficit to decline only to 2.4% in 2015, while the Stability Programme had forecast the deficit to decline to 1.2% of GDP. Besides the higher base from 2014, most of the difference is explained

by substantially lower revenue in every category. Expenditure as a share of GDP is maintained at nearly the same level as in the Stability Programme.

8. According to the Commission 2014 autumn forecast, the deficit is expected to reach 2.9% of GDP in 2014 and to decline to 2.6% in 2015. The difference stems from the lower underlying growth forecast and a somewhat higher forecast of expenditure.

9. Finland's general government debt reached 56.0% of GDP by the end of 2013. The Draft Budgetary Plan forecasts the debt ratio to reach almost 60% in 2014 and exceed 61% in 2015. This implies a 1.6pp increase in the debt ratio in 2015 whereas the Stability Programme planned a lower increase, 1.3pp of GDP. According to the Commission autumn forecast, the debt would reach almost 60% in 2014 and 62% in 2015.

10. The Draft Budgetary Plan includes expenditure cuts and revenue increases amounting to 1.2% of GDP. These measures are either already legislated or about to be finally adopted. They include an increase in indirect taxes, an increased progressiveness of capital income taxes, higher inheritance and gift taxes and an increase in social security contributions. The expenditure cuts concern a wide range of spending items.

11. In 2013, Finland reached its MTO of a structural deficit of 0.5% of GDP, but in 2014 it is expected to deviate from that position both according to the Draft Budgetary Plan and the Commission 2014 autumn forecast. Both the Draft Budgetary Plan and the Commission forecast estimate the deviation based on the structural balance pillar at close to 0.5 pp. of GDP. By contrast, the expenditure benchmark is comfortably met, both in the Member State and the Commission forecast. An overall assessment shows that the structural balance pillar is more relevant for 2014, and therefore points to some deviation from the MTO in 2014. For 2015, taking into account that a large negative output gap indicates difficult economic times, the required adjustment would be limited to 0.1 pp. The Commission forecast projects that the structural balance will not change in 2015 compared to 2014. This implies some deviation from the required adjustment, based on the structural balance pillar. While this deviation would not be regarded as significant over one year, the average deviation over 2014-2015 is 0.3%, exceeding the 0.25% threshold. Based on the Draft Budgetary Plan projection, the deviation is even higher. On the other hand, Finland still meets the requirements of the expenditure benchmark in 2015, both based on the Draft Budgetary Plan and the Commission forecast. An overall assessment based on the Commission forecast shows that the structural balance pillar is more relevant over 2014 and 2015 taken together, but that the significant deviation under this pillar is explained by statistical factors.

12. General government gross debt is planned to reach 61.2% of GDP in 2015, above the 60% of GDP reference value. The planned breach is fully explained by Finland's financial support to safeguard financial stability in the euro area. Additionally, the debt level has been influenced by large purchases of financial assets by the social security funds, resulting in the build-up of assets in parallel to the increase of debt. The debt ratio also reflects the effects of Finland's current cyclical position.

13. As part of the fiscal country-specific recommendation, Finland was to implement rapidly the reforms set out in its structural policy programme of August 2013, as well as the government spending limits and fiscal plan for 2015-2018 in order to reduce the medium and long term fiscal sustainability gap and strengthen conditions for growth. In particular, the government foresees measures to balance local government

finances, to increase the efficiency of the public sector, extend working careers by two years and to improve competition and competitiveness. More specific steps have been announced, most recently in August 2014. A pension reform was agreed by the social partners in late September 2014. The reform links retirement age to life expectancy as recommended by the Council in 2014. The target is to implement the reform from 2017 onwards. Finally, there is political consensus regarding the direction of the healthcare and social care reforms, aimed at the reduction of costs through the integration of service delivery by five regional providers. However, the details of the reform are still under discussion. If fully implemented, these measures could have a strong positive impact on public finances in the medium term through increased growth and reduced expenditure.

14. Overall, the Commission is of the opinion that the Draft Budgetary Plan of Finland, which is currently under the preventive arm, is broadly compliant with the provisions of the Stability and Growth Pact. The Commission invites the authorities to take the necessary measures within the national budgetary process to ensure that the 2015 budget will be compliant with the Stability and Growth Pact.

Furthermore, Finland should put in place appropriate safeguards to guarantee the functional autonomy of the body in charge of producing the macroeconomic forecasts.

The Commission is also of the opinion that Finland has made some progress with regard to the structural part of the fiscal recommendations issued by the Council in the context of the 2014 European Semester and invites the authorities to make further progress.

Done at Brussels, 28.11.2014

For the Commission
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Member of the Commission