Fiscal policy monitoring assessment on the management of general government finances

D/153/04.04.01/2023

This memorandum includes the spring 2023 assessment of the National Audit Office of Finland (NAOF) on the development and management of general government finances. It is a statutory task of the National Audit Office to monitor that central government finances are managed in compliance with the Fiscal Policy Act (869/2012) and the Decree on the General Government Fiscal Plan (120/2014), issued thereunder. The assessment takes into account the 'technical' General Government Fiscal Plan for 2024–2027. The assessment is based on the calculations by the fiscal policy monitoring function, the independent economic forecast issued by the Ministry of Finance in March by the Ministry of Finance in March 2023, and other economic forecasts.

As the General Government Fiscal Plan of the spring of an election year is technical, this report is concise and does not cover all assessment areas of fiscal policy monitoring. The fiscal policy monitoring function presented its previous assessment in the fiscal policy monitoring and audit report published on 16 December 2022[1]. The report presented key observations on the different fiscal policy areas for the entire parliamentary term ended. In addition, fiscal issues that will be topical during the new parliamentary term have been highlighted in the publication *National Audit Office's viewpoints for the 2023–2027 parliamentary term*.[2] The fiscal policy monitoring function will publish a broader fiscal policy report again in December 2023. The assessment will then deal with, for example, the Government Programme and the Government's first General Government Fiscal Plan.

The following members of the fiscal policy monitoring function have participated in the production of the contents of the assessment: Arto Kokkinen, Simo Pesola, Mika Sainio, Sini Salmi, Leena Savolainen, and Matthias Strifler.

Helsinki, 31 May 2023

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[1] The NAOF's separate report to Parliament: Fiscal policy monitoring report, R 25/2022 vp.
[2] National Audit Office's viewpoints for the 2023–2027 parliamentary term, April 2023. https://www.vtv.fi/app/uploads/2023/04/vtv-evastyksia-vaalikaudelle-2023-2027.pdf (in full in Finnish only, summary in English: https://www.vtv.fi/en/publications/national-audit-offices-viewpoints-for-the-parliamentary-term-2023-2027/)

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Summary of the assessment

The business cycle has been changing rapidly since the macroeconomic picture began to deteriorate following the Russian invasion of Ukraine in early 2022. However, the economic decline that began last summer seems to have ended in spring 2023. The mild winter and the largely unrealized energy shortage in Europe have probably protected the economy against stronger contraction. Despite this, the economic picture is very blurred and uncertain. The growth prospects of the global economy are exceptionally weak at the moment. In addition, there are a large number of economic risk factors that may lead to weakening of the business cycle. For example, the stability of the financial markets has been questioned in spring 2023.

The weak business cycle would justify expansionary fiscal policy in 2023. On the other hand, to avoid problems caused by inflation, fiscal policy should support monetary policy that curbs inflation, and such support would have been already needed in 2022. The use of fiscal stimulus in 2023 is also restricted by the growth of general government debt, which has continued since the Covid spring of 2020. A neutral fiscal impulse, which neither contracts nor stimulates the economy, may therefore prove justified in 2023 because of the contradiction between the weakening business cycle and the simultaneous high inflation.

The Government approved the last General Government Fiscal Plan of the parliamentary term on 23 March 2023. Due to the turn of the parliamentary term, the plan is ‘technical’, i.e. it does not contain any new political decisions. According to the fiscal policy monitoring assessment, the General Government Fiscal Plan of spring 2023 meets the requirements of the Decree on the General Government Fiscal Plan. The readability of the plan has been improved in spring 2023, which makes the plan more usable and supports the discussion based on it.

The General Government Fiscal Plan contains a lot of useful information on factors affecting the development of public finances. However, the impact of the F-35 fighter project on general government deficit and debt should be described more transparently in the plan. It should also be examined how the plan readers could be informed as well as possible about the uncertainty of the projections of general government finances. The uncertainty of the projections is illustrated by the fiscal position of 2022, which still in spring 2022 was expected to show a deficit of more than 2% in relation to GDP. However, spring 2023 data showed that the general government fiscal position in 2022 was close to the target set at the beginning of the 2019–2023 parliamentary term, despite the crises that took place during the parliamentary term.

According to the fiscal policy monitoring assessment, the spring forecast of the Ministry of Finance can be considered realistic within the meaning of the EU framework. The forecasts of the Ministry are in line with those of other forecasters because, as regards the variables examined, they fall within the prediction bounds formed.

The EU is currently considering the Commission's proposal to reform the fiscal framework. The aim is to reach agreement on the proposal during 2023. According to the Commission's proposal, the framework would focus on Member States’ debt sustainability and four-year fiscal-structural plans to support it. Nevertheless, the reference values for deficit and debt will probably remain unchanged. The Commission proposes amendments and specifications to the tasks of Independent Fiscal Institutions (IFIs). The extension of the tasks aims to strengthen compliance with the fiscal framework and the national ownership of it.

According to the spring 2023 forecasts, the development of Finland's public finances is worrying. There is a risk that Finland will not comply with the EU’s fiscal rules in the coming years. The general government deficit is projected to rise to and temporarily exceed the 3% limit defined in the EU rules. Finland's government debt-to-GDP ratio is also forecast to continue to show an upward trend. The Commission has urged Member States to seek a decreasing or moderate debt ratio in the medium term.

The central government spending limits for 2023 were exceptionally exceeded by EUR 0.3 million when the first supplementary budget for 2023 was processed in Parliament. The budget expenditure for 2023 exceeded the ceiling by EUR 0.3 million when three different legislative proposals were amended during their processing in Parliament. The government proposal for the supplementary budget for 2023 was in practice of the same amount as the ceiling for budget expenditure. Thus, no margin of manoeuvre was left in the spending limits to make it possible to prepare for changes during the processing of legislative proposals in Parliament.

The exceptions related to fiscal planning will expire at the end of 2023

The Government approved the last General Government Fiscal Plan of the 2019–2023 parliamentary term on 23 March 2023. Due to the turn of the parliamentary term, the plan was not submitted to Parliament as a report. In addition, the plan is ‘technical’, i.e. it does not contain any new political decisions. The content of the plan is regulated by the Decree on the General Government Fiscal Plan (120/2014), issued under the Fiscal Policy Act (869/2012). The information content of the last plan of the parliamentary term is subject to narrower requirements than normal. According to the fiscal policy monitoring assessment, the General Government Fiscal Plan of spring 2023 meets the requirements of the Decree on the General Government Fiscal Plan. Appendix 1 contains detailed observations on the extent to which the content of the plan corresponds to the requirements set by the Decree on the General Government Fiscal Plan.

The Ministry of Finance has added summary sections to the spring 2023 plan. This kind of development improves the readability and usability of the plan and supports the discussion based on it.

An important foundation for fiscal policy-making is the projections of general government finances, which extend over the next four years. The estimates are used, for example, during the preparation of the Government Programme. According to the findings of the National Audit Office, the processes for the preparation of projections in the Ministry of Finance are appropriate[3], but the uncertainty contained in the projections should be taken into account in the planning of general government finances[4]. This uncertainty does not only mean that details will be revised later, but the picture and outlook of public finances may change considerably in a short period of time. It would therefore be necessary to consider new ways of describing the uncertainty contained in the projections of public finances in the General Government Fiscal Plan in order to ensure that it is conveyed to the forecast users as well as possible.[5]

The uncertainty of the forecasts and the rapid change in the situation are illustrated well, for example, by the development of the forecasts and statistics on general government deficit in 2022 (see Figure 1). At the beginning of the parliamentary term, in 2019, the general government fiscal position was expected to fall short of the Government's target path by around one percentage point. In spring 2021, the forecast for 2022 had already declined to –2.9 per cent in relation to GDP, for example due to the impacts of the Covid-19 pandemic. After that, the outlook for public finances brightened, and the forecast improved slightly in spring 2022. In spring 2023, actual statistics showed that the general government deficit was eventually moderate, around –0.9% in relation to GDP. Despite the severe crises during the parliamentary term, the general government fiscal position in the last statistical year of the parliamentary term was thus almost in line with the target set at the beginning of the parliamentary term.

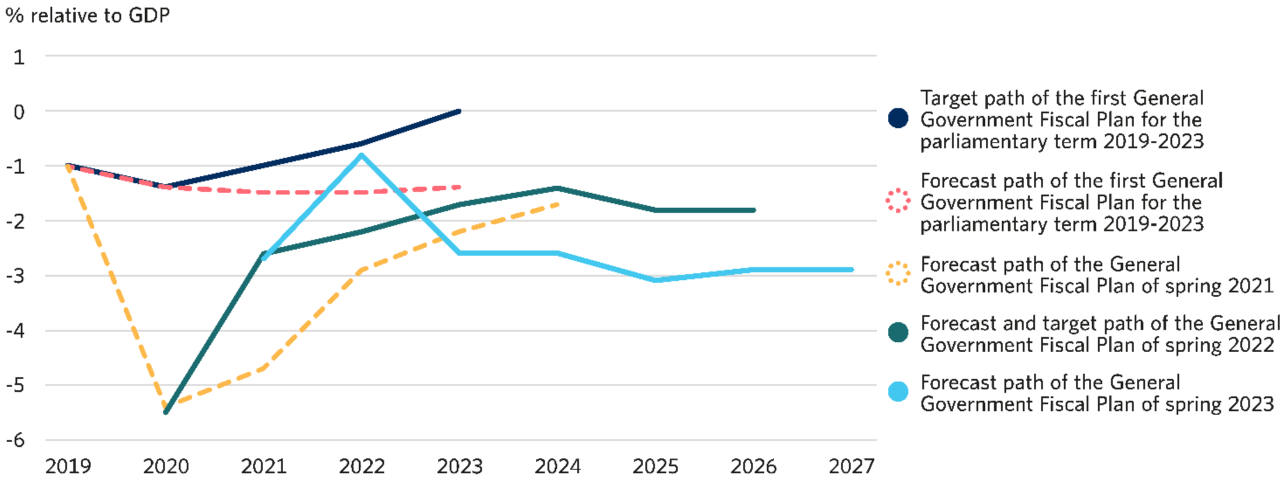

Figure 1: Target and forecast paths of the general government fiscal position in the 2019–2022 parliamentary term.
Source: Ministry of Finance.

[3] See the NAOF's audit report 17/2019: Medium-term projections in the planning of general government finances.
[4] See the NAOF's Annual Report 2020 and National Audit Office's viewpoints for the 2023–2027 parliamentary term, April 2023.
[5] Cf. the fan-like pattern by which the Ministry of Finance illustrates the uncertainty of the economic growth forecast: Economic Survey, Spring 2023, p. 19. Ministry of Finance 2023.

The General Government Fiscal Plan describes well the phenomena affecting the development of public finances. However, the presentation of factors affecting debt and deficit development should be supplemented further. The Finnish F-35 fighter project will impact the development of government debt and deficit in the coming years. The impact on public debt will arise when the central government takes on debt to cover the payments in the project. According to statistical rules, impacts on deficit will arise later when the fighters are delivered. The debt and deficit impacts of the project are not clearly described in the General Government Fiscal Plan. It is necessary to examine these impacts separately as the project's impacts are temporary on this scale.

The impacts of the fighter project can be examined by comparing the deficit and debt development set out in the General Government Fiscal Plan with the development paths excluding the impacts of the F-35 project (Figure 2). The debt paths diverge starting from 2023, when the payments start, whereas the deficit paths diverge starting from 2025, when the fighter deliveries are estimated to begin. If the F-35 project is excluded, government deficit in relation to GDP will be slightly more than 0.5 percentage points lower annually from 2025 onwards than in the baseline calculation. In 2027, the impact of the fighter procurement excluded, government debt in relation to GDP will be 2.4 percentage points lower than in the baseline calculation. Although the impacts can be considered substantial, they do not significantly change the overall picture of the development of general government finances.

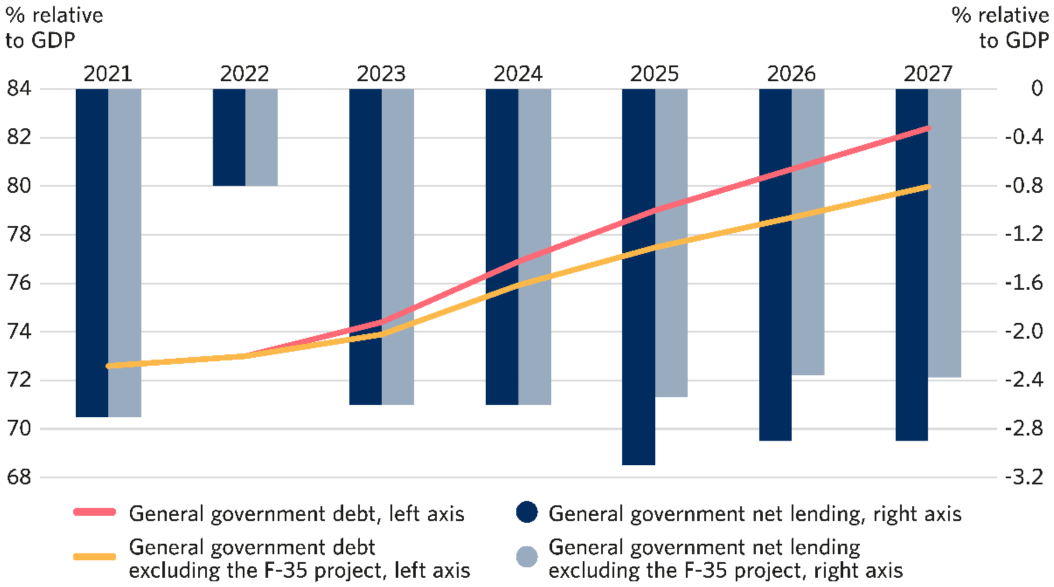

Figure 2: Impact of the F-35 fighter project on government deficit and debt. Source: The Ministry of Finance, the General Government Fiscal Plan, calculations by the NAOF's fiscal policy monitoring function.

The general escape clause of the Stability and Growth Pact related to the fiscal rules was activated in spring 2020. This means that Member States are allowed to deviate from the requirements concerning public finances, provided that the deviation does not jeopardize the sustainability of public finances over the medium term. In national legislation, the validity of the escape clause means that the targets set in the General Government Fiscal Plan need not lead to the achievement of the medium-term objective set for the general government fiscal position. According to the objective, the structural balance should be –0.5% in relation to GDP, which in practice means almost balanced general government finances. As the escape clause will be deactivated at the end of 2023, the fiscal targets set in the General Government Fiscal Plan of spring 2024 at the latest must be so tight that their achievement will lead to the achievement of the above-mentioned medium-term objective.

However, it should also be noted that the requirements concerning the setting of fiscal targets in Finland are strongly based on the ‘Fiscal Compact’, to which Finland is also committed. However, the concept of structural balance will probably no longer be used in the EU fiscal framework. In its conclusions of 14 March 2023, the EU Council has also stated that it is necessary to ensure the consistency of the Fiscal Compact with the new economic governance framework. If the EU legislation and the Fiscal Compact are amended, the Government must then ensure that the national fiscal legislation is updated without delay to avoid even temporary vagueness in the legislative requirements for fiscal target-setting.

The business cycle outlook is weak

At the end of 2022, the colour code of the business cycle heatmap produced by the fiscal policy monitoring function turned to pale blue, which illustrates a weak business cycle.[6] According to the heatmap, the business cycle has been changing rapidly since the macroeconomic picture began to deteriorate fast following the Russian invasion of Ukraine in early 2022. The macroeconomic deterioration was at first reflected in consumer confidence, which fell as soon as the war started in March 2022. In the summer of 2022, the decline was also reflected in other indicators, whose colour turned blue or at least faded (see Figure 3). Since then, the consumer price index has developed in a different direction than the other variables in the heatmap. Such divergent development of consumer prices was already anticipated in the fiscal policy monitoring assessment of spring 2022.

In Finland, inflation had already exceeded the European Central Bank's 2% target since August 2021 and reached 4.4% in January 2022, before the beginning of the Russian invasion in Ukraine. The inflation was partly due to the fact that demand recovered faster than supply. In 2021, national economies, including Finland, continued to suffer from supply disruptions caused by the Covid-19 crisis, while the lifting of restrictions on human mobility and the continued global fiscal stimulus seem to have contributed to the rapid recovery and even overheating of Finland and other national economies. Since then, Russia's war of aggression, the sanctions against Russia following the war, and the energy crisis have led to even higher inflation. High inflation, in itself, has a negative impact on consumer confidence, consumption, and the economic outlook. It is likely that consumer prices will, at least for some time, continue to develop differently from the other indicators in the heatmap. It may also be considered likely that consumer confidence will begin to increase when inflation decreases, and this has already started to happen in spring 2023.

Year	Vacancies, change	Capacity utili-zation	Consu-mer price index, change	Consumer confi-dence	Wages and salaries, change	Services confi-dence	Construc-tion confi-dence	Industrial confi-dence	Employ-ment rate, change	Un-employ-ment rate, change	Retail trade confidence	Composite indicator (weighted)
2023												
4		-0,48		-1,02		-0,43	-1,01	-0,84			-0,11	
3	-1,59	-0,55	2,99	-1,57		-0,35	-0,54	-0,81	0,09	0,07	0,00	-0,21
2	-1,32	-0,17	3,43	-1,69	1,08	-0,54	-0,80	-0,41	-0,11	0,23	-1,16	0,01
1	-1,04	-0,32	3,23	-1,81	0,72	-0,73	-0,90	-0,22	0,03	0,41	-1,35	-0,01
2022												
12	1,53	0,01	3,58	2,80	0,52	0,58	0,50	0,50	0,18	0,36	1,95	0,15
11	1,56	0,09	3,58	2,62	1,44	0,60	0,33	0,53	0,92	0,53	1,22	0,10
10	-0,54	0,12	3,18	-2,76	0,55	-0,57	-0,09	-0,28	1,12	0,69	-1,34	0,14
9	-0,18	0,87	3,08	-3,01	1,48	-0,63	0,07	0,00	0,93	0,82	-1,86	0,35
8	0,27	0,54	2,84	-2,26	1,38	-0,64	-0,39	0,19	0,29	0,88	-1,89	0,35
7	0,65	0,58	2,94	-2,32	0,72	-0,18	-0,58	0,43	0,28	0,91	-0,25	0,45
6	1,30	1,09	2,94	-2,05	1,05	0,11	-0,37	0,74	0,47	1,01	-0,16	0,74
5	1,44	1,44	2,54	-1,67	1,11	-0.08	-0,21	1,05	0,91	1,16	-0.43	0,87
4	2,17	1,56	1,89	-1,71	1,74	-0,11	0,46	1,18	1,59	1,39	-0,51	1,07
3	2,73	1,52	1,94	-1,35	1,67	0,28	0,68	1,24	1,01	1,36	-0,59	1,15
2	2,21	1,65	1,29	0,62	1,31	0,57	1,07	1,69	1,67	1,09	-0,29	1,33
1	1,84	0,98	1,24	0,37	1,41	0,56	0,98	1,42	1,47	1,05	0,26	1,15
2021												
12	3,31	1,60	0,79	0,15	0,95	0,63	1,14	1,38	2,09	1,38	0,19	1,35
11	3,03	1,13	0,89	0,80	0,65	0,64	1,11	1,76	0,80	1,12	0,86	1,23
10	3,39	1,27	0,65	1,16	0,55	0,70	0,93	1,82	0,73	0,98	0,66	1,26
9	2,73	0,85	0,30	1,79	0,92	0,50	0,84	1,69	0,03	0,88	0,76	1,08
8	2,37	1,14	0,15	1,45	0,82	0,44	0,89	1,77	2,09	0,92	0,94	1,24
7	2,34	0,78	0,00	1,53	1,08	0,69	0,55	1,34	1,32	1,04	0,30	1,09
6	2,48	0,88	0,05	1,63	2,10	0,49	0,26	1,47	1,80	1,46	0,82	1,32
5	1,98	0,62	0,15	1,37	2,13	0,13	0,09	1,13	2,55	1,77	0,51	1,24
4	1,63	0,32	0,10	1,37	0,88	-0,47	0,22	0,80	0,11	1,51	0,18	0,64
3	0,64	0,21	-0,30	0,09	-0,66	-1,02	-0,39	0,44	0,10	-0,20	-0,16	-0,08
2	-0,53	-0,08	-0,50	0,54	-0,50	-0,95	-0,97	-0,06	-0,25	-1,44	0,38	-0,43
1	-0,75	0,59	-0,50	0,50	-1,68	-0,93	-0,66	0,13	-1,78	-1,63	-0,12	-0,64

Figure 3: Heatmap produced by the fiscal policy monitoring function (28 April 2023). Source: Statistics Finland, Ministry of Economic Affairs and Employment, European Commission, Confederation of Finnish Industries, and calculations by the fiscal policy monitoring function.[7]

[6] The business cycle heatmap is a tool that describes the business cycle in Finland by means of colour codes and is based on indicators illustrating the state of the Finnish economy. The higher the share of red or blue indicators at the same time, the more likely it is that the economy is experiencing either good times or bad times. Further information on the business cycle heatmap is available on the heatmap web page, the NAOF's fiscal policy monitoring report of December 2021, the fiscal policy monitoring assessment of June 2021, and Strifler, M. and Kokkinen, A. 2021a.

[7] Strifler, M. and Kokkinen, A. 2021a.

The business cycle should be examined by means of both the monthly and the annual composite indicator of the heatmap (Figure 4). Monitoring the business cycle based on monthly and quarterly data is useful as it provides an accurate picture of cyclical changes (see, for example, the NBER's Business Cycle Dating Committee). Information on the annual-level business cycle is particularly important for fiscal policy-makers. The monthly composite indicator illustrates cyclical changes more sensitively than the annual indicator. For example, the monthly composite indicator reacted extremely rapidly and accurately to the sudden drop in economic activity in April 2020 following the outbreak of the Covid-19 pandemic and, correspondingly, to the rapid positive turn in the business cycle in spring 2021. The monthly composite indicator also shows the rapid deterioration of the business cycle in 2022 due to Russia's war of aggression.

Since December 2022, the monthly composite indicator has been below zero, i.e. the business cycle is negative. However, the long decline that has continued since summer 2022 seems to have stopped. The mild winter and the sufficient supply of energy in Europe have probably protected the economy against stronger contraction. Despite this, the economic picture is blurred and uncertain at the moment. In spring 2023, as a result of the high inflation and the rapid interest rate increases that central banks have made to combat it, there have again been suspicions that the financial stability may be weakening. It remains to be seen whether the central banks, now that banks are facing problems, will still be able to raise interest rates in order to halt inflation. In this respect, the central banks are between a rock and a hard place.

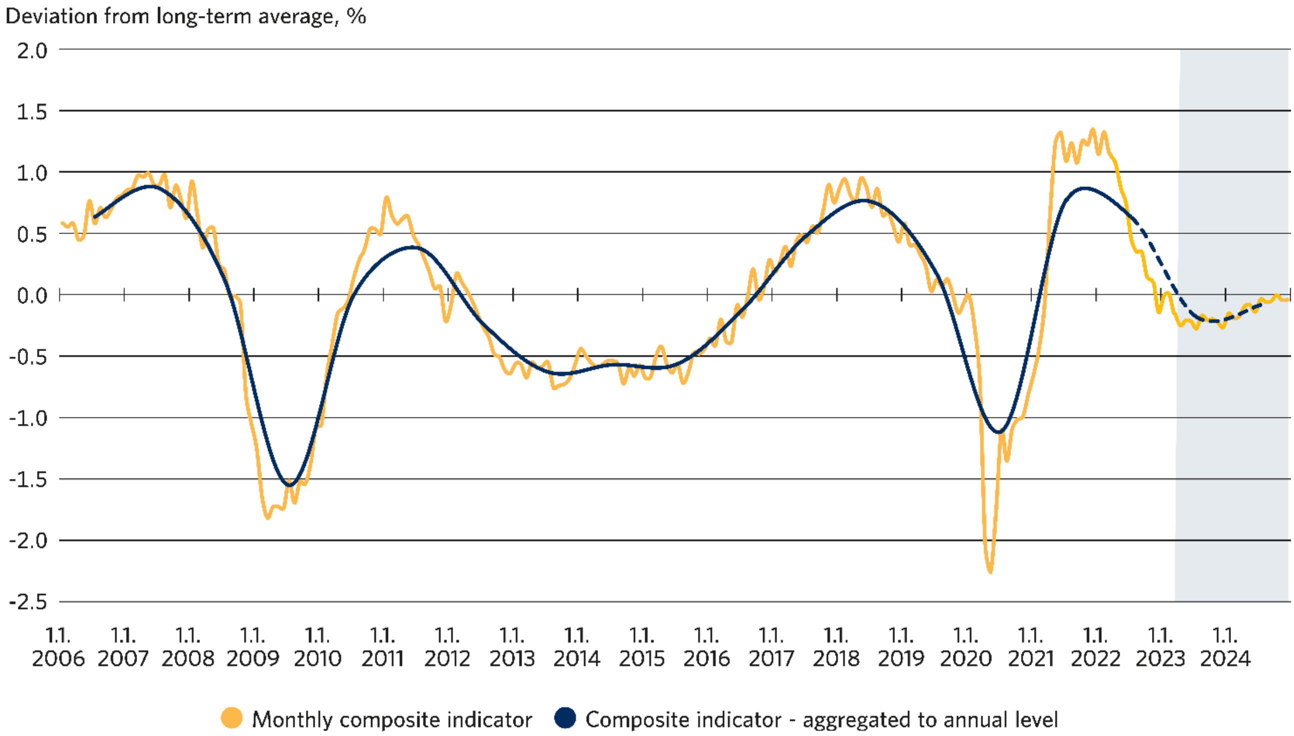

Figure 4: Monthly (yellow line) and annual (blue line) composite indicator, and forecast for the next year (grey background). The forecast is based on the heatmap data and other statistics available by 28 April 2023. Source: Statistics Finland, Ministry of Economic Affairs and Employment, Confederation of Finnish Industries, European Commission. Calculations and forecasts: fiscal policy monitoring function.[8]

[8] Strifler, M. and Kokkinen, A. 2021b: Forecast for the Finnish business cycle heatmap. Unpublished manuscript, fiscal policy monitoring function.

According to the current and next year's composite indicator forecast, the economy will adapt to the negative impacts of the war, economic sanctions, energy crisis, and high inflation, and the rapid deterioration of the business cycle will not continue in the near future (see Figure 4)[9]. In 2023, the development of the business cycle is forecast to be weak, and the indicator is forecast to remain below zero. According to the forecast, the recovery in 2024 will be slow and fragile, and the composite indicator will rise slowly towards zero. It should be noted that the forecast of the business cycle indicator of the heatmap currently involves a high level of uncertainty.

Unlike after the Covid-19 crisis, the key macroeconomic conditions are currently weaker, which prevents a rapid recovery. First, the high prices following the inflation, the decreased purchasing power, and the higher interest expenses have burdened the economy more permanently. Second, the spirit in global markets has shifted from cooperation towards confrontation and strategic competition. Should this remain permanent, it may slow down international trade and investments. This would be detrimental especially to a small open economy such as Finland. The growth prospects of the global economy are exceptionally weak at the moment.[10]

In addition, there are plenty of risk factors that may weaken the business cycle. Since spring, the United States and Europe have feared the emergence of a new crisis on the financial markets or possibly the property market. There has also been discussion as to whether the governments in EU countries with a high debt ratio can continue to borrow at a reasonable interest rate. There are also concerns about the geopolitical stability and the possibility of energy shortage next winter. Finland's membership in NATO stabilizes Finland's investment environment and presents a positive risk. If wages and prices develop more slowly in Finland than in the other key competitor countries, this may strengthen Finland's cost competitiveness.

The heatmap and its composite indicator aim to measure the business cycle directly based on observations. The output gap, in turn, is calculated as the difference between the observed GDP and the estimated trend or potential output. The trend or potential output are initially unobservable components and can be calculated in countless different ways. The traditional Hodrick–Prescott filter can be used to produce a trend for quarterly GDP. In addition to looking at trends or potential, it is natural to calculate when GDP returned to the pre-Covid crisis level (Figure 5). On the basis of both of these examinations, Finland's economy recovered rapidly after the Covid spring of 2020.

The calculation illustrates (a) how the output level of the second quarter of 2019 was achieved in the second quarter of 2021 and (b) how the GDP trend according to the Hodrick–Prescott filter (HP trend) was achieved between the second and third quarter of 2021. The output gap of the HP filter, calculated as the difference between the observed GDP and the HP filter trend, remained negative from the Covid spring until spring 2021. After that, the output gap based on the HP filter has been positive. The results support the picture of cyclical fluctuations in 2021 and 2022 produced by the composite indicator of the heatmap. Similar results have been presented in recent studies (see Sariola and Pönka 2021, and Orjasniemi and Kuusela 2021). In these studies, calculations have been made quarterly or biannually, which makes it possible to observe cyclical fluctuations and cyclical changes more accurately than on an annual level, in the same way as in the composite indicator of the heatmap.

[9] Strifler, M. and Kokkinen, A. 2021b.
Further information on the heatmap forecast is also available from the fiscal policy monitoring report of December 2021 and the fiscal policy monitoring assessment of June 2021. The forecast is based on the heatmap data and other specified statistics available by 28 April 2023. The monthly forecast was prepared from April 2023 to December 2024. For one of the variables, a forecast was also prepared for March.

[10] See IMF WEO, April 2023.

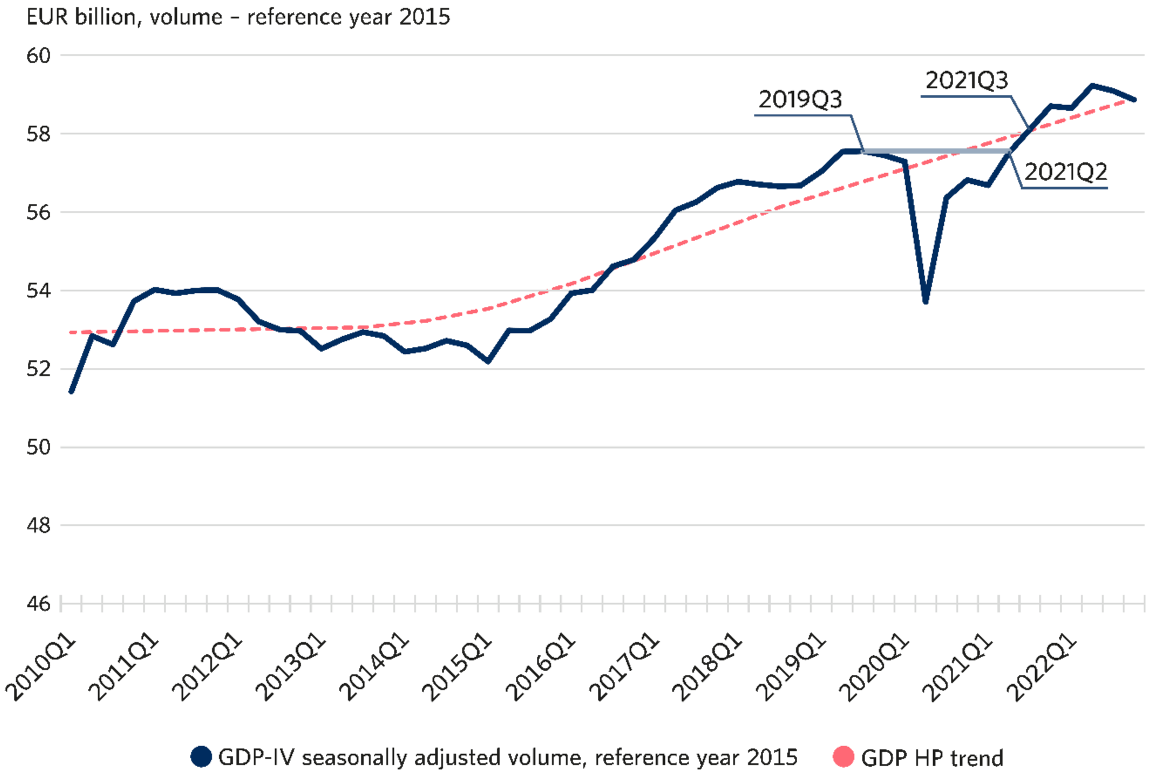

Figure 5: The seasonally adjusted quarterly volume of GDP and the Hodrick–Prescott trend (λ=1600). Sources: Statistics Finland, National Accounts, calculations of the fiscal policy monitoring function.

The general government structural balance is examined on an annual level. The balance relative to GDP has been cyclically adjusted using the annual output gap. One known method of calculating the output gap is to use the production function method jointly agreed by the European Commission and Member States (EU-CAM, PF method). When aggregated to annual level, the composite indicator of the heatmap with its forecast complements the picture of the business cycle provided by the annual output gap produced using the EU's common method. In addition to the Commission and the Ministry of Finance (MoF), the Bank of Finland (BoF), the International Monetary Fund (IMF), and the Organisation for Economic Co-operation and Development (OECD) regularly calculate and publish their own output gap estimates. The Ministry of Finance naturally uses the same production function method as the Commission. To get a broader picture of the annual business cycle, it is possible to compare the annual composite indicator and the results of the annual HP filter with the output gap estimates calculated by the above-mentioned organizations (Figure 6).

The composite indicator of the heatmap aggregated to annual level and the annual output gap estimates develop largely in line with each other (Figure 6). However, especially in cyclical changes, such as the financial crisis or the Covid-19 crisis, the dispersion is greater even on annual level.

As regards recovery from the Covid-19 crisis, it can be seen that the estimates produced by the Ministry of Finance and the EU Commission using the production function method differ from the other estimates in that, according to them, the output gap would have been negative since 2020, i.e. the economy would have remained continuously below the potential output. The same applies to the OECD's estimate, which differs even otherwise from all the other estimates: according to it, the economy would have been continuously in recession since 2012. In 2022, the Bank of Finland and the IMF revised their own output gap estimates upwards in such a manner that they both turned positive but remained nevertheless close to zero in 2022. According to the composite indicator and the HP filter,[11] the recovery would have been even faster. Inflation started to increase already in the second half of 2021. According to economic theory, a positive output gap cannot be maintained without inflationary pressures on wages and prices (see Forecast for the Finnish Economy by the Bank of Finland, 16 December 2022). The composite indicator was the only output gap estimate that indicated a positive output gap before the end of 2021.

[11] Other calculations also indicated a more rapid recovery. See the separate report of the fiscal policy monitoring function to Parliament in December 2022.

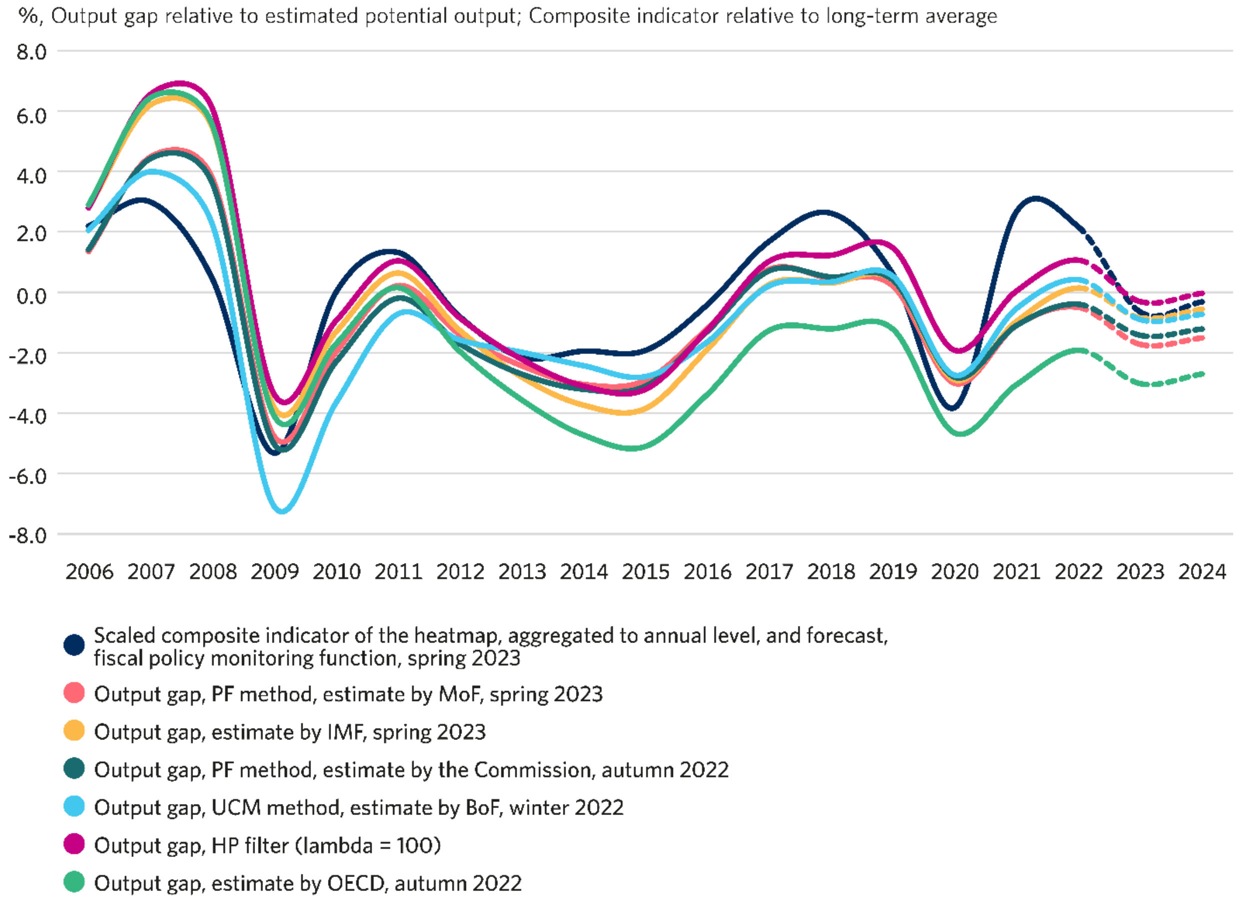

Figure 6: Composite indicator of the heatmap aggregated to annual level and its forecast, the HP filter (λ=100), and the annual output gap estimates of the following organizations: Ministry of Finance (MoF), Bank of Finland (BoF), EU Commission, International Monetary Fund (IMF), Organisation for Economic Co-operation and Development (OECD). Forecast for 2023 and 2024 (dashed line). The variation (standard deviation) of the business cycle indicator of the heatmap has been scaled to be comparable with the variation (standard deviation) of the output gap. Sources: MoF, BoF, EU Commission, IMF, OECD and the fiscal policy monitoring function.[12]

When examining the annual output gap forecasts, it can be seen that, unlike before, the different estimates now seem to develop in line with each other. According to all forecasts, the post-Covid upturn in 2021–2022 will be over, and the business cycle will deteriorate in 2023 as a result of the high inflation, the Russian war of aggression, and the energy crisis. According to the forecasts, the weak development will continue in 2024, and recovery will be very slow.

[12] Sources of the composite indicator of the heatmap: Statistics Finland, Ministry of Economic Affairs and Employment, Ministry of Finance, European Commission, Confederation of Finnish Industries. Calculations of the fiscal policy monitoring function. See Strifler, M. and Kokkinen, A. 2021b.

The weak business cycle, high inflation, and weakening debt sustainability hamper fiscal stance planning

According to the business cycle heatmap compiled by the fiscal policy monitoring function, the business cycle turned positive in 2021 and remained positive in 2022. However, according to the method based on the EU Commission's production function, GDP has remained below the potential output in 2021–2022. The differing estimates of the business cycle and of the economic recovery after the Covid crisis lead to different conclusions on the appropriateness of the fiscal stance for the business cycle in 2021–2022.

In 2023 and 2024, the estimates of the business cycle converge again and are in line with each other as before the above-mentioned years. According to the forecast of the composite indicator of the heatmap, the business cycle will be below the long-term average in 2023 and 2024. According to the forecast prepared by the Ministry of Finance and the potential output produced using the EU Commission's production function method, GDP will be below the potential output in 2023 and 2024.

It should be noted that the heatmap estimate of the business cycle will hardly be revised afterwards, while the output gap estimate may be significantly revised afterwards. The output gap estimate for 2022 also depends on the underlying potential output forecast, which involves an exceptionally high level of uncertainty due to the Russian war of aggression and the following blurred global economic outlook. The picture painted of the business cycle in 2022 by the composite indicator is currently based solely on outturn data.

The output gap, composite indicator, and primary balance forecasts all involve a lot of uncertainty due to the Russian war of aggression and a rather blurred global economic outlook. Corresponding uncertainty is associated with the assessment of the fiscal stance for 2023 and 2024.

A weak business cycle would justify expansionary fiscal policy in 2023. On the other hand, the European Central Bank aims to curb inflation, which has remained high since 2021 and 2022. In order to avoid problems caused by long-term inflation, fiscal policy should support monetary policy. Such support would already have been needed in the second half of 2021 and in 2022. The use of additional fiscal stimulation in 2023 is also restricted by the growth of general government debt, which has continued since the Covid spring 2020.

The discretionary fiscal stance in 2019–2024 is examined based on structural primary balance (Figure 7). Nominal primary balance has been cyclically adjusted by means of both the output gap and the composite indicator of the heatmap. According to the data available in spring 2023, the structural primary balance has been primarily negative in 2019–2024 based on both methods of cyclical adjustment. An exception to this is that the structural primary balance cyclically adjusted by the output gap is zero in 2022. If structural primary balance is interpreted to refer to long-term fiscal balance, there is no need to adjust the long-term fiscal balance according to the point estimate of the structural primary balance of the statistical year 2022. The result can be considered surprising.

When the business cycle estimates based on the output gap and the composite indicator of the heatmap are compared, it can be seen that after the exceptional years 2021–2022, they converge in forecast years 2023–2024. According to the estimates of both methods, the business cycle is negative (see Figure 7, dots along the horizontal axis).

When the estimates of structural primary balance are examined in relation to the estimates of the business cycle, it can be seen whether the discretionary fiscal policy is counter-cyclical or pro-cyclical relative to the business cycle (Figure 7). Due to the differing estimates of the business cycle, the difference between the estimates based on the output gap and the heatmap was also particularly great in the case of fiscal policy stance in 2021–2022. In forecast years 2023 and 2024, the estimates of the business cycle converge and, consequently, based on both methods, fiscal policy is countercyclical in a negative business cycle.

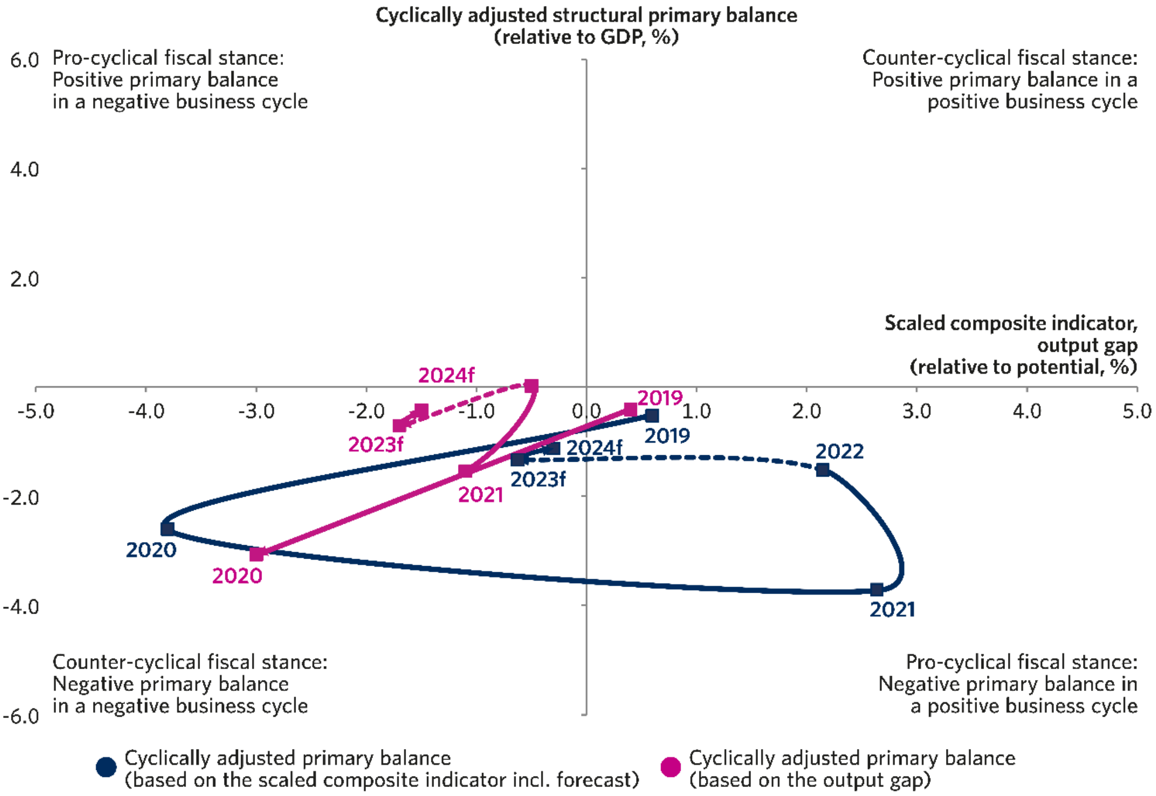

Figure 7: Fiscal stance in relation to the business cycle: structural primary balance based on the output gap and the cyclical heatmap indicator in relation to the business cycle based on the output gap and the cyclical heatmap indicator in 2019–2024. The primary balance has been cyclically adjusted by means of both the output gap (purple dots) and the composite indicator of the heatmap (blue dots). When the estimates of structural primary balance shown in the figure are examined in relation to the estimates of the business cycle illustrated on the horizontal axis, it can be seen whether the discretionary fiscal policy is counter-cyclical or pro-cyclical relative to the business cycle. The output gap values for 2023 and 2024 and the structural balance estimates calculated by means of them are based on the Ministry of Finance's primary balance forecast and the results of the jointly agreed production function method. The composite indicator values and the structural balance estimates calculated by means of them are based on the heatmap forecast and the Ministry of Finance’s primary balance forecast. The variation (standard deviation) of the business cycle indicator of the heatmap has been scaled to be comparable with the variation (standard deviation) of the output gap. (See Strifler, M. and Kokkinen, A. 2021c[13]) The estimates based on the output gap method of both the business cycle and the cyclically adjusted structural primary balance may be revised later even to a significant extent. Source: Ministry of Finance and NAOF's fiscal policy monitoring.

When the situation is examined by means of the fiscal impulse, i.e. the indicator describing the change and direction of fiscal policy compared with the previous year[14], the impulse of 2023 appears to be neutral based on the heatmap composite indicator, i.e. the change in structural balance is zero in a weakening business cycle (see Figure 8). In spring 2023, prior to the forthcoming Government's fiscal decisions, the impulse of 2024 looks roughly neutral based on the composite indicator. According to the estimate based on the output gap, the impulse provides counter-cyclical stimulus in 2023 and is roughly neutral in relation to the business cycle in 2024.

[13] Strifler, M. and Kokkinen, A. 2021c. Capturing uncertainty in measuring Finland’s fiscal stance. Unpublished manuscript, fiscal policy monitoring function, NAOF.
[14] The fiscal impulse is illustrated by examining the change in structural primary balance in relation to the change in the business cycle indicator. For more details on how to assess the fiscal stance, see: the NAOF's fiscal policy monitoring report 2021.

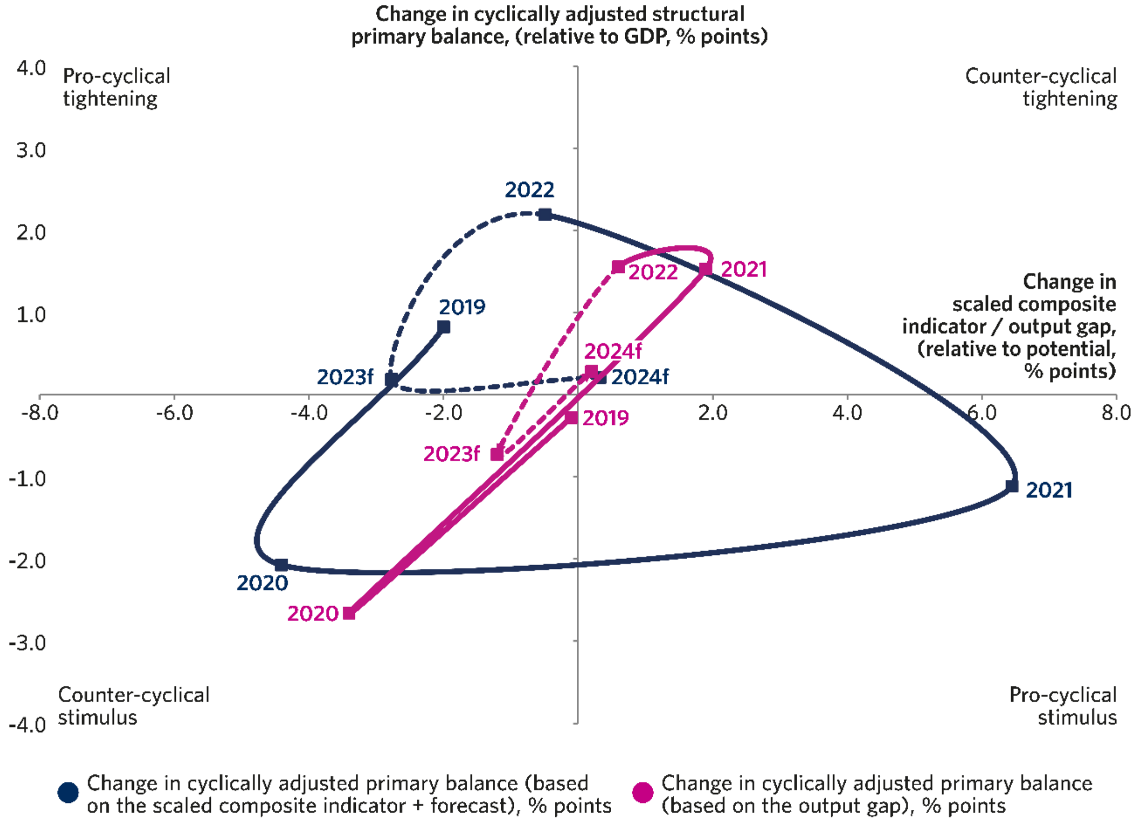

Figure 8: Fiscal impulse in relation to the change in business cycle: the change in structural primary balance (cyclical adjustment based on the output gap and the composite indicator) in relation to the change in both the output gap and the composite indicator produced by the NAOF's fiscal policy monitoring. The estimates for 2023 and 2024 are based on forecasts. Source: Ministry of Finance and NAOF's fiscal policy monitoring.

According to the estimate based on the composite indicator of the heatmap, the fiscal stance was pro-cyclically expansionary in a positive business cycle. For 2023, the forecasters forecast slightly negative economic growth. At the same time, at the beginning of 2023, inflation has not eased, and the European Central Bank is curbing it with interest increases to prevent it from dragging on for years. It is difficult to find a fiscal stance appropriate for these circumstances.

Counter-cyclically expansionary fiscal policy would be appropriate for the weakening business cycle, and this is what the fiscal stance still is in 2023. However, achieving an expansionary fiscal impulse would require an increase in expenditure or tax reductions. This is difficult to justify in view of the fact that general government debt has continued to grow since the outbreak of the Covid-19 pandemic and from the perspective of curbing inflation. A neutral fiscal impulse may therefore prove to be justified in 2023 because of the contradiction between the weakening business cycle and the simultaneous inflation. The fiscal impulse of 2024, which in spring 2023 is estimated to be neutral, does not yet include the discretionary measures of the new Government.

The spending limits were exceeded when Parliament decided on the first supplementary budget for 2023

During the processing of the first supplementary budget for 2023, Parliament decided on expenditure exceeding the central government spending limits. The government proposal for the supplementary budget for 2023 was in practice of the same amount as the ceiling for budget expenditure, i.e. of the total of EUR 70,310,487,200 reserved for the spending limits of 2023, EUR 70,310,437,000 was budgeted. When the supplementary budget was discussed in Parliament, the budgetary impacts of two unprocessed legislative proposals (HE 132/2022 vp and HE 133/2022 vp), EUR 4.676 million in total, were removed from it, while the impact of changes made in the processing of the approved government proposal (HE 175/2022 vp), EUR 5 million in total, was added to it. The combined impacts of these changes exceeded the spending limits by EUR 273,800.

The fiscal policy monitoring function is not aware of a similar situation in the history of the spending limits system where the budgeted amount would have exceeded the spending limits. The core idea of the spending limits system is that the expenditure ceiling limits and steers budgeting. In order for the central government spending limits to strictly limit budgeting, the Government should ensure that they are adhered to throughout the budgeting process.

A report of the Finance Committee (VaVL 46/2022 vp, adopted in the plenary session on 1 March 2023) states that the spending limits have been exceeded and describes the reasons for it. When discussing the supplementary budget, Parliament was thus aware of the fact that the spending limits had been exceeded. However, from the documents related to the processing of the supplementary budget in Parliament, it does not appear that the exceeding of the spending limits would have been discussed or that experts would have been heard regarding it. It is a normal and necessary part of the parliamentary processing of a supplementary budget to also take into account the budgetary impacts of the decisions taken by Parliament during the processing. During the 2019–2023 parliamentary term, the government proposals for six supplementary budgets were changed during the parliamentary processing, mainly due to legislative proposals.

Although the exceeding of the spending limits was due to changes made in the parliamentary processing of legislative proposals, which were difficult to foresee, it would have been possible to prevent it either by reducing a discretionary appropriation in the supplementary budget by an equal amount or by ensuring in advance that there was a margin of manoeuvre in the spending limits for unexpected situations. Changes made to budget proposals during the parliamentary processing have not previously led to exceeding the spending limits, as there has been a margin of manoeuvre for them. There was no longer a similar margin of manoeuvre in the 2023 supplementary budget, as the government proposal had been in practice of the same amount as the expenditure ceiling, even though several legislative proposals were still pending.

It has been customary for the outgoing Government to leave at least part of the supplementary budget provision in the spending limits of an election year, usually around EUR 300 million, to the incoming Government. However, the outgoing Government decided on a supplementary budget provision of only EUR 100 million in the spending limits for 2023, and the amount was budgeted in full in the government proposal for the first supplementary budget. Thus, no spending limits provision was left for the incoming Government for expenditure during the remainder of the year.

During the parliamentary term that ended, commitment to the central government spending limits weakened in an unprecedented manner. The Government violated the spending limits rule set in the Government Programme in all the years of the parliamentary term. The use of the entire margin of manoeuvre within the spending limits and the resulting exceeding of the spending limits in the 2023 budgeting can also be interpreted as an indication of the Government's weak commitment to the spending limits system. The outgoing Government thus left even the current year's expenditure pressures to be solved by the new Government.

Table 1: Final spending limits calculation and budgeting of the 2019–2023 Parliamentary term, updated in connection with the first supplementary budget for 2023 (EUR million). Source: Based on the MoF’s data, the NAOF's calculation.

Calculation of the spending limits during the government term	2020	2021	2022	2023
Technical spending limits	**44,853**	**46,417**	**46,582**	**46,716**
Spending limits expenditure according to the Government Programme, total	2,058	2,884	2,518	1,400
— permanent additional expenditure within the spending limits	1,078	1,375	1,318	1,370
— permanent reallocations of spending limits expenditure	-50	-50	-125	-100
— one-off future-oriented investments (spending limits expenditure)	730	419	175	–
— provision for the financing of future-oriented investments	–	840	850	–
— supplementary budget provision	300	300	300	100
Transfer of compensations for tax revenue losses incurred by municipalities during the previous parliamentary term to the spending limits	1,012	1,012	1,012	1,012
Provision for unforeseen expenditure needs in 2020–2022	150	244	135	
Spending limits of the parliamentary term (incl. the supplementary budget provision)	**48,073**	**50,557**	**50,247**	**49,128**
Structural adjustments, total	-1,341	2,112	2,758	16,664
Changes in justifications	-1,213	-266	-105	-192
Technical adjustments (timing change, re-budgeting, pass-through item, technical change)	-159	27	-1,844	391
Funding of the wellbeing services counties	–	–	1,956	12,525
Mechanism for exceptional circumstances	–	500	500	–
Expenses arising from the Covid-19 situation (within the spending limits)	–	1,850	351	–
Transfer to the spending limits due to the security policy situation	–	–	1,779	2,703
Transfer of the funding of Veikkaus' beneficiaries to the spending limits	–	–	–	990
Use of the unallocated reserve carried over from the previous year	31	–	121	247
Price adjustments, total	-34	602	1,495	4,069
Changes to the spending limits (+/–)	–	–	900	450
Spending limits of the parliamentary term, supplementary budget proposal 2023	**46,697**	**53,271**	**55,400**	**70,310**
Budgeted within the spending limits in the budget proposal	55,148	53,149	55,153	70,311
Not budgeted within the spending limits	**-8,451**	**2**	**0**	**-0.3**
Budgeted outside the spending limits in the budget proposal	13,601	14,690	22,757	13,151
Total amount budgeted in the budget proposal	**68,750**	**67,839**	**77,910**	**83,462**
Final accounts	67,074	66,002	76,261	–

In this spring's technical General Government Fiscal Plan for 2024–2027, the outgoing Government informs the next Government of the development of budget expenditure at the turn of the government term. This technical General Government Fiscal Plan provides information on how revenue and expenditure would develop during the next government term without new political decisions. The technical spending limits of the previous Government forms the basis on which the new Government will take decisions in the government negotiations on the level of spending limits expenditure during the government term and on the allocation of expenditure.

According to the technical General Government Fiscal Plan, budget expenditure would be around EUR 8 billion higher during the current parliamentary term compared with the spending limits decision of spring 2022. The increase in expenditure compared with the budget for 2023 is explained by statutory and contractual index adjustments (about EUR 2 billion), growth in the funding of the wellbeing services counties (EUR 2.8 billion, index and ex-post adjustment), additional expenditure caused by the exceptional security policy situation (EUR 2.1 billion), NATO expenditure (EUR 50–65 million), and the TE Services reform (EUR 48 million). Interest expenditure outside the spending limits is estimated to amount to EUR 3.4 billion in 2024 and EUR 3.8 billion in 2027.

The figure below presents an estimate in accordance with the technical General Government Fiscal Plan of budget expenditure and revenue excluding borrowing for 2024–2027 and the budgeting for 2023. The expenditure for 2024–2027 is presented at the price level of 2024, whereas the revenue estimates are presented at current prices; therefore, the revenue development is not fully comparable to the expenditure development. The figure shows the essential expenditure items at the turn of the parliamentary term.

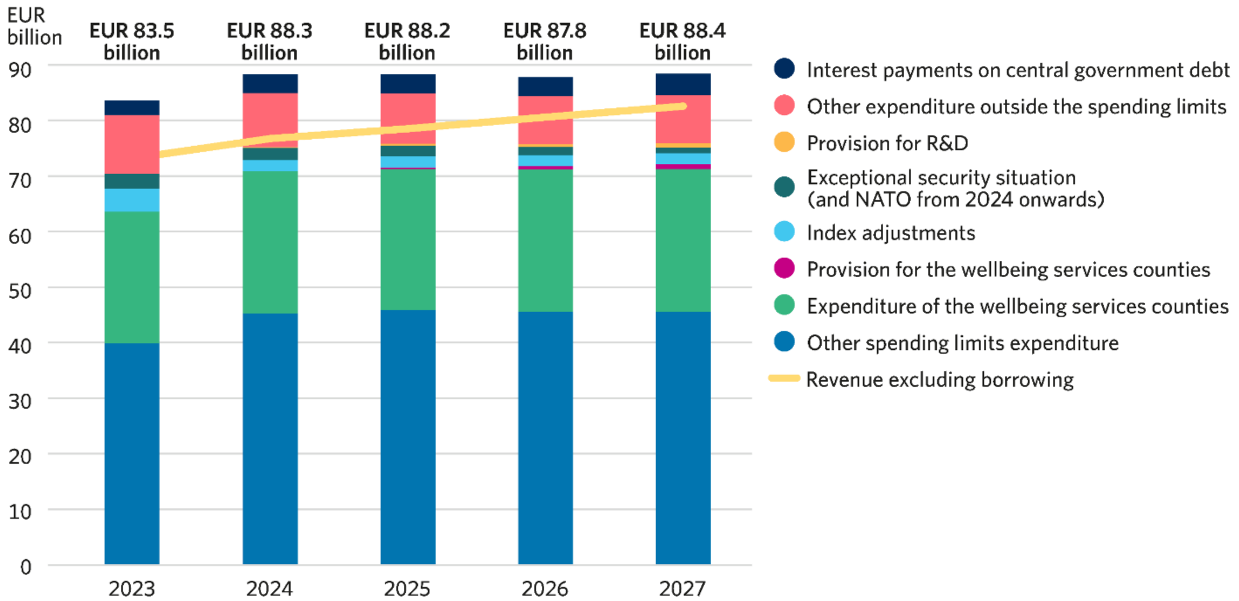

Figure 9: Estimates according to the technical General Government Fiscal Plan 2024–2027 of budget expenditure and revenue in the upcoming parliamentary term, excluding borrowing.

The EU fiscal rules are being reformed – Finland's indebtedness outlook is worrying

The fiscal policy monitoring task of the National Audit Office includes assessing Finland's compliance with the EU fiscal framework. The fiscal framework is based on the EU Treaty and the Stability and Growth Pact, and it is implemented as part of the European Semester. The general escape clause of the Stability and Growth Pact related to the fiscal rules was activated in spring 2020. This means that Member States are allowed to deviate from the requirements concerning public finances, provided that the deviation does not jeopardize the sustainability of public finances over the medium term. The general escape clause of the Stability and Growth Pact will remain in force until the end of 2023.

In spring 2020, before the crisis resulting from the Covid-19 pandemic, the Commission opened a discussion on the assessment of the EU fiscal rules and framework. Based on expert discussions, public debates, and discussions between Member States, the Commission published a communication on orientations for a reform of the EU economic governance framework in November 2022 and legislative proposals based on the communication in April 2023. The Commission proposes replacing the preventive arm of the Stability and Growth Pact (Regulation 1466/97) and amending the corrective arm (Regulation 1467/97) and the so-called Budgetary Frameworks Directive (2011/85/EU). The aim is to reach agreement on the proposal during 2023.

According to the Commission's proposal, the reformed framework would focus on Member States' debt sustainability and four-year fiscal-structural plans. The country-specific plans would present fiscal objectives as well as key investments and reforms for a period of at least four years. In addition, the plan would set an adjustment path limiting the growth of general government net expenditure. This multiannual expenditure target would be the only operational indicator in the common EU fiscal framework.

According to the Commission's proposal, the objective set for structural fiscal position, which has played a key role in the current rules, would be abandoned. It is an objective that is difficult to understand and based on a computational estimate of the output gap. The output gap estimate may be revised afterwards to a significant extent, especially when there are cyclical changes. Thus, the conclusion about the achievement of the structural fiscal position objective and about compliance with the related rule may therefore also be revised to a significant extent.

The 3% reference value for general government deficit and the 60% reference value for government debt relative to GDP, as specified in the Treaty, remain unchanged in the Commission's proposal. However, the Commission proposes to abandon the 1/20 adjustment rule applied to debt exceeding the reference value, i.e. the requirement for an approximately 5% annual adjustment. The Commission has assessed that a strong front-loaded adjustment required by the rule could jeopardize the conditions for growth.

On the basis of the Commission's proposal, a debt-to-GDP ratio exceeding the 60% reference value should be brought credibly to a downward path during the four-year plan or a stable level should be maintained. In addition, it would be possible to apply for an extension on the grounds of investments and structural reforms driving economic growth. The adjustment would be steered by a debt sustainability analysis, on the basis of which the expenditure adjustment path would be set. The plan would involve monitoring the general government net expenditure, i.e. a concept of expenditure that is unaffected by interest payments and cyclical unemployment expenditure but that takes into account the impact of discretionary changes in revenue.

Exceeding the reference values may lead to the initiation of an excessive deficit procedure (EDP). In the Commission's proposal, the deficit-based EDP procedure remains similar to the present one. However, according to the proposal, the debt-based EDP procedure would be strengthened, and deviation from the agreed net expenditure path would be a key criterion for opening it. Substantial public debt challenges would play a key role in opening the procedure.

The Commission also proposes amendments and specifications to the tasks of national Independent Fiscal Institutions (IFIs). The extension of the tasks aims to strengthen compliance with and national ownership of the framework. The new tasks proposed include assessment of compliance with the net expenditure path, production or approval of debt sustainability analyses, assessment or approval of measures related to the sustainability of public finances and sustainable growth, regular assessment of fiscal frameworks, and assessment of the progress of the measures required under the EDP procedure. The fiscal policy monitoring function considers the Commission's ultimate objectives to strengthen the national monitoring of the framework to be justified. If implemented in this form, the proposed tasks would require significant additional investment in the monitoring resources.

According to Statistics Finland's statistics and the Ministry of Finance's spring forecast, general government deficit will remain within the 3% reference value in 2022–2024 (Table 2). The deficit criterion was therefore complied with in 2022 and would be complied with in 2023–2024. According to the forecast, however, the reference value will be exceeded in 2025, and even thereafter the deficit is forecast to be only slightly below the reference value. The general government debt-to-GDP ratio exceeded the 60% reference value already in 2013. The Ministry of Finance forecasts that the general government debt ratio will be on the rise in the coming years.

Table 2: General government deficit and debt in 2021–2027. Sources: Statistics Finland and the Ministry of Finance (spring 2023 forecast).

Deficit/debt	2021	2022	2023*	2024*	2025*	2026*	2027*
General government deficit	-2.8	-0.9	-2.6	-2.6	-3.1	-2.9	-2.9
General government debt	72.6	73.0	74.4	76.9	79.0	80.7	82.4

According to the Commission's March 2023 communication on fiscal policy guidance, fiscal targets should be set in such a way that in the Member States where the debt ratio has exceeded the 60% reference value, the debt ratio is put on a downward path or stays at a prudent level over the medium term. The targets of all Member States should also maintain or bring their deficit ratio below the 3% reference value within the period covered by the Stability Programme (by 2026) and ensure that it is credibly maintained below the reference value over the medium term.

In addition, in May 2023, the Commission issued recommendations for the Council's country-specific recommendations. According to them, Finland should, for example, pursue such a fiscal policy in 2024 that limits the nominal increase in nationally funded net expenditure to 2.2%. For the period after 2024, the Commission proposes a gradual and sustainable economic adjustment, taking into account growth-enhancing investments and reforms.

Due to the change of the parliamentary term, Finland's stability programme of spring 2023 has been drawn up according to the unchanged policy scenario so that it only contains the measures decided by Marin's Government and does not set fiscal targets for the coming years. In autumn 2023, the next Government will adopt a new stability programme as part of the General Government Fiscal Plan.

In May 2023, the Commission also published a report under Article 126 (3), stating that Finland's general government debt will exceed the 60% reference value in 2022 and that the debt reduction criterion is not respected. Nevertheless, the Commission does not propose opening the EDP procedure in spring 2023. During the validity of the general escape clause, the Commission has not initiated a new EDP procedure for any Member State although the reference values have been exceeded. The Commission has expressed that it will propose to the Council possible opening of deficit-based EDP procedures in spring 2024 based on the actual data of 2023.

Contrary to the Commission's guidance, Finland's debt-to-GDP ratio will increase throughout the forecast period. The deficit ratio will remain close to the reference value. The fiscal policy monitoring function is concerned about the projected development of the debt and deficit ratio.

The forecast of the Ministry of Finance is in line with those of other forecasters

The high inflation, slowdown in exports, and reduced consumer purchasing power are reflected in the outlook of the Finnish economy. Economic uncertainty is expected to continue, GDP development is expected to decline in the current year, and growth is expected to remain very moderate in the next few years. In its forecast, the Ministry of Finance projects Finland's GDP to shrink by 0.2% in 2023, while in the following years it is expected to grow: by 1.3% in 2024 and by 1.6% in 2025.

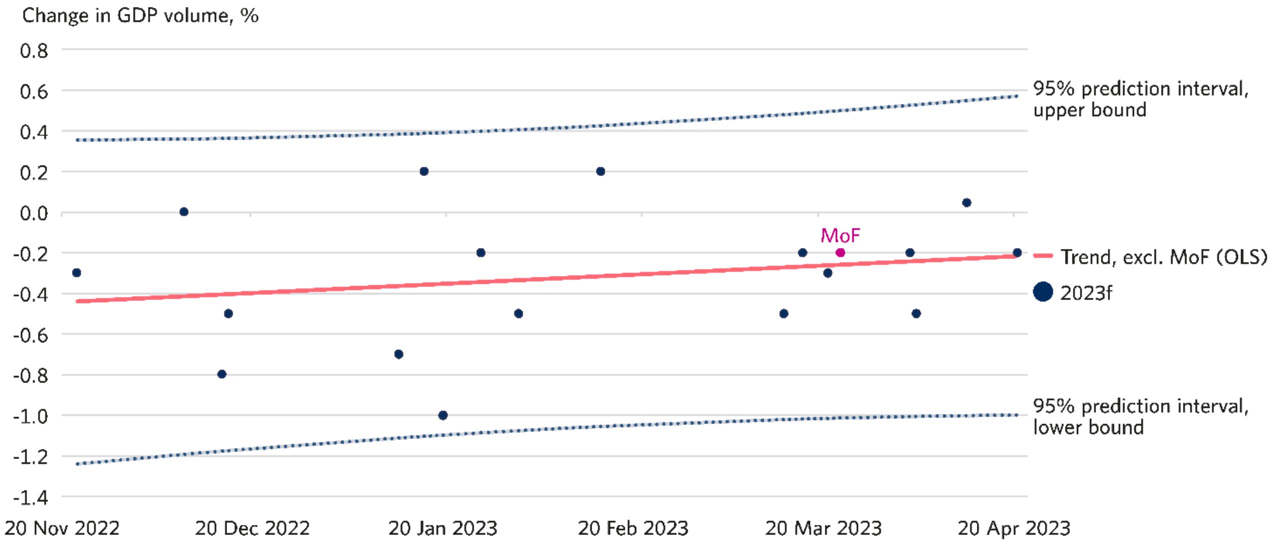

Figure 10: GDP forecasts for 2023, consensus forecast, and upper and lower bounds of the 95% prediction interval. The forecasts have been prepared between 22 November 2022 and 20 April 2023. Source: Forecasters, fiscal policy monitoring function.

When assessing the realism of the forecast by the Ministry of Finance, the fiscal policy monitoring function has reviewed the forecasts on the change in[15] GDP for 2023. The majority of forecasters expect Finland's economic growth to remain negative in 2023 (Figure 10). The Ministry of Finance's 2023 forecast of the change in GDP is in line with those of other forecasters and clearly within the prediction bounds. There are more differences between the forecasts made at the beginning of the year, whereas after the development in early 2023, the forecasts made after March converge more clearly around –0.2%. However, the forecasters expect the recession to remain short and inflation to fall towards the 2% target level in 2024–2025. Despite the economic recovery, the Ministry estimates general government gross debt relative to GDP to be 74.4% in 2023 and to grow to 76.9% in 2024 and to 79% in 2025. The development of gross debt will be influenced by possible fiscal consolidation measures taken by the new Government, which could not be anticipated in the forecasts.

Table 3 compares the forecasts of the Ministry of Finance with the 95% prediction interval which is formed of other economic forecasts and which aims to illustrate the bounds within which 95% of the forecasts are estimated to fall. The forecasts are examined by assessing whether the forecasts produced by the Ministry fall within the prediction bounds that take into account the dates of the forecasts. In the assessment, it should be noted that both the most optimistic and the most pessimistic forecast may prove to be closest to the actual development. It should also be taken into consideration that, although deviations as such do not reflect the realism of the forecasts, they can be used to assess whether the forecasters' thoughts about the economic development are in line with each other.

[15]The prediction interval has been formed on the basis of the forecasts of 17 forecasters other than the Ministry of Finance and the statistical T-test variable. These forecasters are Akava Works, Danske Bank, the Research Institute of the Finnish Economy (ETLA), the Finnish Centre for Pensions, the European Commission, Handelsbanken, the International Monetary Fund (IMF), MuniFin, Labore, Nordea, the OECD, OP Group, Pellervo Economic Research (PTT), POP Bank, the Mortgage Society of Finland (Hypo), the Bank of Finland, and Savings Bank. All forecasters do not produce forecasters in the same scope as the Ministry of Finance, and the set of forecasts for 2025 remains partly small.

Table 2: Comparison between the forecasts of the Ministry of Finance and those of the other economic forecasters. The forecast of the Ministry of Finance is compared with the 95% prediction interval formed of the other forecasts. The scale in the table: 1 = The MoF forecast falls within the 95% prediction interval that takes into account the publication dates of the forecasts. 0 = The MoF forecast falls outside the 95% prediction interval that takes into account the publication dates of the forecasts.

Forecast variable	2023f	2024f	2025f
GDP, change in volume, %	1	1	1
Imports, change in volume, %	1	1	1
Private consumption, change in volume, %	1	1	1
Public consumption, change in volume, %	1	1	1
Exports, change in volume, %	1	1	1
Investments, change in volume, %	1	1	1
Unemployment rate, % of labour force	1	1	1
Employment rate, % of population	1	1	1
Inflation, %	1	1	1
Current account, % of GDP	1	1	1
Government fiscal balance, % of GDP	1	1	1
Government gross debt, % of GDP	1	1	1

It should be noted that most of the forecasters only forecast the development of the current and the following year, whereby the group of forecasts for 2025 remains relatively small. This has an effect on the prediction intervals formed. However, the forecasts of the Ministry of Finance fall within the prediction interval in the case of all variables and, on the basis of the examination, are in line with those of the other forecasters. On the basis of the examination, the spring forecast of the Ministry of Finance can be considered realistic within the meaning of the EU framework. However, the forecasts also involve uncertainties, which are highlighted in the Ministry's forecast. The uncertain financial market situation, interest rate developments, geopolitical situation, and the measures possibly taken by the new Government to balance public finances, in particular, may change the upcoming economic development.

Appendix 1: Observations on compliance of the General Government Fiscal Plan for 2024–2027 with the requirements set by the Decree on the General Government Fiscal Plan (120/2014)

Requirement set by the Decree	Estimate of compliance
The General Government Fiscal Plan is reviewed annually by the end of April.	In 2022, the Plan was approved and published on 23 March 2023, which is in compliance with the requirement set by the Decree.
The General Government Fiscal Plan shall cover all parts of general government finances. The plan contains sections on central government finances, finances of the wellbeing services counties, municipal finances, and statutory earnings-related pension funds and other social security funds.	The coverage and structure of the plan comply with the requirements.
The General Government Fiscal Plan sets multiannual targets for general government as a whole regarding the ratio of fiscal position to GDP and, in addition, separate targets for the different subsectors of general government. The fiscal position objectives shall be set in such a manner that, based on the forecast of the Ministry of Finance, they lead at least to the achievement of the objective set for the general government's structural fiscal position. This can be deviated from if exceptional circumstances as referred to in the Fiscal Compact are prevailing in Finland, and they correspond to the exceptional circumstances under the EU Stability and Growth Pact. The General Government Fiscal Plan sets multiannual targets for general government debt and general government expenditure relative to GDP at market prices. These targets are in line with the targets set for the fiscal position of general government as a whole. The General Government Fiscal Plan presents estimates of the key revenue and expenditure items of general government and its subsectors (as referred to in section 3, item 1). The estimates are drawn up on the assumption that the legislation affecting revenue and expenditure is not amended and on the assumption that the legislation affecting revenue and expenditure is amended as specified by the Government. The plan describes the impact of both options on the medium-term structural fiscal position and long-term sustainability of general government finances. The General Government Fiscal Plan specifies the measures required for achieving the fiscal position targets and their estimated financial impact.	The requirements related to target setting are not applied as such to the last General Government Fiscal Plan for the parliamentary term. The information on the fiscal position of the general government and its subsectors is presented in the plan in accordance with section 3, item 7, of the Regulation.

Requirement set by the Decree	Estimate of compliance
The General Government Fiscal Plan presents a comparison between the most recent macroeconomic forecasts of the Ministry of Finance and the European Commission and the budgetary forecast, and explains any significant differences between the assumptions on which the forecasts are based.	Appendix 5 of the plan presents a comparison between the latest forecasts of the Ministry of Finance and the European Commission for six variables.
The General Government Fiscal Plan presents the impact of various growth and interest rate assumptions on the macroeconomic forecast and the budgetary forecast, as well as on the key figures related to general government finances.	Appendix 4 of the plan presents sensitivity analyses on the effects of different growth and interest rate assumptions.
The general government units that are not part of regular budgets at the subsector level shall be listed and published in connection with the General Government Fiscal Plan. The plan describes the combined impact of these units on general government fiscal position and debt.	The plan includes a list of the units classified in the national accounts as part of the central government. The plan also states that “For a list of units in the general government subsectors, see Statistics Finland’s website”, but a link to the list is not provided. The combined impact of these units on the financial position and debt has been presented in the plan. Thus, the requirement of the decree is met although the presentation of information at this highly aggregated level does not significantly increase transparency.
When preparing its economic forecasts, the Ministry of Finance shall take into consideration the National Audit Office’s conclusions on the macroeconomic forecast and the budgetary forecast. If, according to the conclusions, the macroeconomic forecasts have included a bias that has had a major impact on the forecasts during four consecutive years, the Ministry of Finance shall publish the actions it has taken to correct the bias or issue a public statement insofar as it does not concur with the National Audit Office’s conclusions.	The National Audit Office has not detected a bias as referred to in the Decree in the Ministry of Finance's macroeconomic forecasts.