Talousennuste

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Economic forecast 2012–2013

Slowest phase of growth is over

Additional information

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LABOUR INSTITUTE FOR ECONOMIC RESEARCH

Economic forecast 2012–2013

Slowest phase of growth is over

The Labour Institute for Economic Research forecasts that Finland's GDP will grow this year by 1.9 per cent and 2.6 per cent next year. Like our forecast published last August, these projections are based on our view that the worsening of the European debt crisis since the summer of 2011 will not lead to a recession in developed countries like that experienced in 2009 and that Finnish GDP will not contract this year. Partly due to the strong money and financial market interventions by the U.S. and European central banks, the debt crisis began to subside at the beginning of this year. The turn-around is also attributable to the improvement in the economic situation especially the U.S.

Trends in Europe are very divergent in nature. After tightening their fiscal policies drastically, the crisis countries will still be in recession at least this year. Economic development is clearly better in central and northern European countries. The relatively low dependence of Finnish exports on the southern European crisis countries makes it possible for our total production to expand in 2012 and 2013 faster than in the rest of Europe.

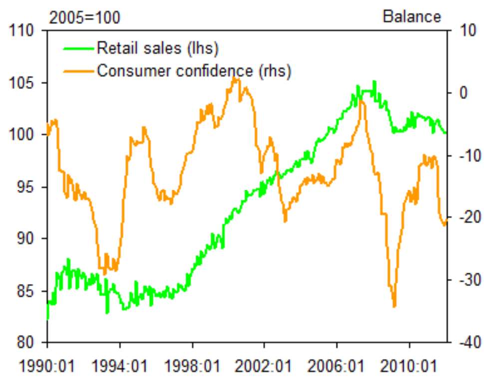
The relatively unstable situation in the European financial markets and the excessive tightening of fiscal policy by the debt crisis countries along with the ensuing consequences constitute a risk to Finland's economic growth in the next few years. The difficulties of the forest industry and electronics industry have also weakened our exports and thus more widely the Finnish economy. The fear, however, that the Finnish industry is structurally so weak that the current account would slip into a permanent deficit, seems premature. The expected trendwise improvement in the services account will limit the deterioration of the current account, so that it will already be in balance in 2013.

Relatively strong domestic demand and sluggish public sector growth almost completely eliminated the deficit of the overall Finnish public sector last year. The central government's budget deficit was also considerably smaller than expected. The expected moderate economic growth in the years 2013-2015 and the government's stabilization measures will generate a substantial fiscal surplus, which means that Finland's sustainability gap is deemed to be much smaller than, for example, the Ministry of Finance has so far estimated.

Euro area debt crisis is easing

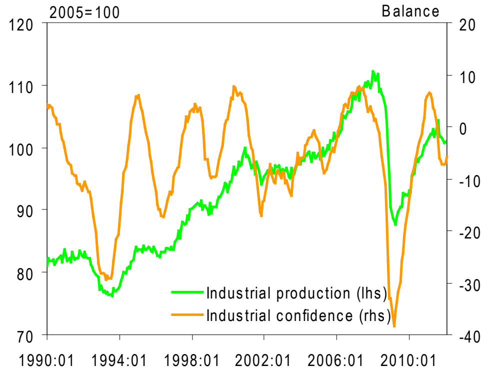
The European debt crisis has its roots in the 2009 recession. When the public sector began to weaken after the collapse of the private sector, private sector debt began to change into public debt. In countries where the current account was in deficit before the crisis of 2008-2009 and where the public finances were weak to begin with, the public sector's financial deficit also grew the most. As a result, the capital markets' confidence in the central governments' ability to cope with their debt weakened profoundly. This impact was compounded by the fact that

Consumer confidence and retail sales in euro area 1990:01–2012:02



Source: Eurostat

Industrial confidence and industrial production in euro area 1990:01–2012:02



Source: Eurostat

in some countries the collapse of the private sector stemmed from the housing loan bubble. The countries afflicted by the central government debt crisis are Spain, Ireland, Italy, Greece and Portugal. It is known that the Greek crisis is the deepest and its resolution has required the most support from other euro countries, the EU and the IMF.

Fiscal policy has been tightened considerably in all the crisis countries, which has also weakened the labour market by dampening domestic demand. As a result of the stringent fiscal policy the trade and current balances have strengthened considerably in almost all the crisis countries. In Greece, for example, the central government's deficit declined significantly in January-February of this year compared to that of a year ago. The public finances of Italy, Spain and Ireland are also getting stronger. In Portugal, on the other hand, public finances are at least so far still weakening. Balancing the crisis countries' public finances in addition to the ECB's actions - in particular its decision of December to begin granting three-year funding to banks - has restored confidence in the capital markets, in particular in the Italian and Spanish government's ability to cope with their debts.

Euro area government decisions to raise the lending capacity of the temporary stabilization fund (EFSF) to 440 billion euros to support the crisis countries have also in part contributed to the alleviation of the debt crisis. The measures decided on led by the German government to increase fiscal discipline in the euro area may have had a similar effect. However, the regulatory mechanism agreed upon in this connection including controlling the structural deficit of the public sector may prove to be difficult to implement, interfering too much with prudent fiscal policies aimed at smoothing cyclical development.

The timetable for the transition to a permanent stability mechanism (ESM) was moved up to next summer. The original lending capacity of the permanent fund is 500 billion euros. The current plan is to include credit already issued to the crisis countries through the temporary mechanism (EFSF) so that its notional lending capacity reaches about 800 billion euros. Unused credit facilities of the EFSF will not become part of the permanent mechanism, so the real resources of the permanent fund will be smaller than the EU Commission and the IMF would have hoped for.

European growth still slowing down this year

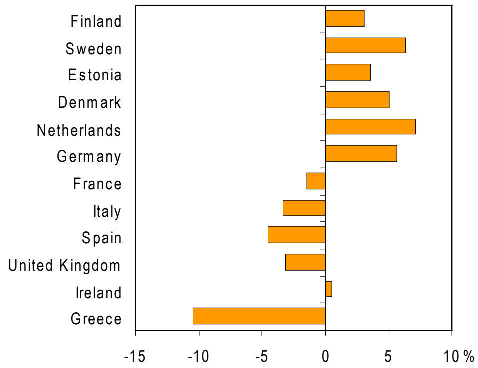
The tightening fiscal policy will spur a decline in the GDP of the crisis countries in the euro area this year, and next year their GDP will

Table 1. International economy

GDP growth (%)	2011	2012f	2013f
United States	1,7	2,3	3,0
Eur-17	1,5	0,4	1,4
Germany	3,0	1,2	2,0
France	1,7	0,8	1,5
Italy	0,2	-0,8	0,5
EU27	1,5	0,6	1,6
Sweden	3,9	1,4	2,8
United Kingdom	0,8	0,8	1,5
Japan	-0,9	2,0	2,5
Russia	4,3	4,5	5,0
China	9,2	8,3	8,7

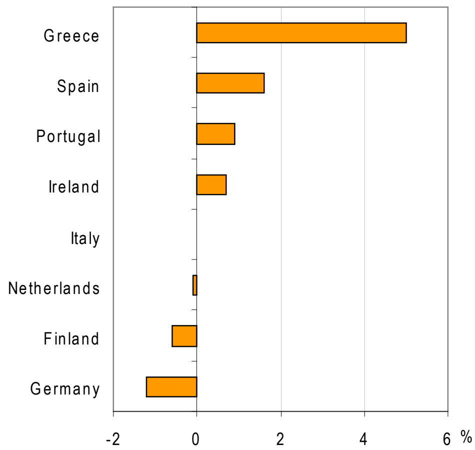
Source: BEA, BOFIT, Eurostat, Labour Institute for Economic Research

Current account deficit relative to GDP in 2010



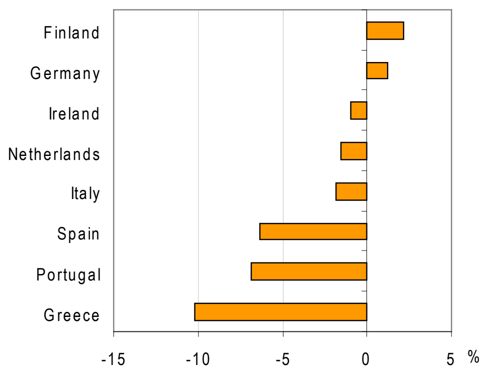
Source: IMF

Change in unemployment rate in euro countries during 2011, %-points



Source: Eurostat

Change in retail trade volume in euro countries during 2011, %



Source: Eurostat

increase much more slowly than that of the rest of Europe. It should be noted that fiscal policy has also been tightened considerably, for example, in France and the Netherlands. Savings in public finances and tax increases will inevitably bring about a more extensive slow-down of economic growth in Europe. However, the immediate impacts of trade flows, e.g. from crisis countries to other countries, are determined largely based on the location of different countries. Thus, a significant contraction in domestic demand in the crisis countries has a far greater negative impact on French and British exports than, for example, the exports of Finland and Sweden.

Europe's growth is affected this year by divergent forces: growth in the rest of the world, alleviation of the debt crisis as well as the relatively positive employment situation of some countries such as Germany combine to bolster private demand. The fiscal belt-tightening in the crisis countries and also, for example, in France and the Netherlands, threatens to put a damper on the budding upswing. The crisis countries' real GDP will contract this year under the conflicting pressures of these forces while other countries will achieve modest growth. The escalation of the debt crisis to such proportions that could drive also countries with strong credit ratings into a deep recession seems unlikely. Such a crisis would already extend to the entire world.

Euro area GDP shrank in the last quarter of last year by 0.3 per cent from the previous quarter but increased by 0.7 per cent on a year-on-year basis. According to confidence indicators, the euro area's economic situation is no longer weakening just now, but on the other hand a quick recovery is not on its way either. The first data on economic development from the early months of this year suggest that euro area GDP will decline even further. The Labour Institute for Economic Research forecasts that euro area GDP will grow 0.4 per cent this year and 1.4 per cent next year. According to this estimate, euro area GDP will already begin to grow again this year from the second quarter onwards. We base the estimate on positive economic development occurring outside Europe and the clear alleviation of the debt crisis, which is reflected, for instance, in a significant decline of the interest rates of Italian and Spanish long-term government bonds. The whole EU region's GDP will grow this year and next year by 0.2 percentage points faster than in the euro area.

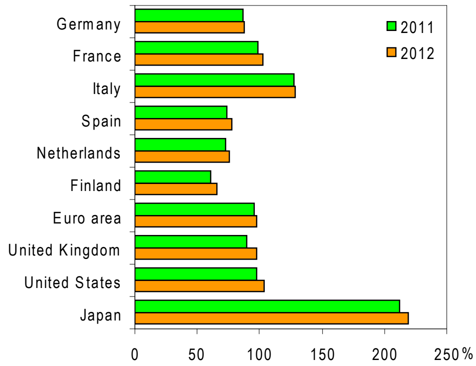
Public finances are curbing growth in the euro area, especially this year. Other components of domestic demand - private consumption and investment - will grow this year at an average rate of 0.5-1 per cent. However, next year its growth will speed up by about one percentage point from this year. Foreign trade will boost economic growth in the euro area in both years.

Divided Europe's south in midst of a crisis

European economic development is marked by two divergent trends this year and next. A substantial tightening of fiscal policy will curb growth in the crisis countries. Through the export market this will also put a damper on the growth of the rest of Europe, but despite this differences in growth rates will be significant. In Spain, Italy, Greece and Portugal overall output will contract this year. Next year only Greek GDP will be decreasing.

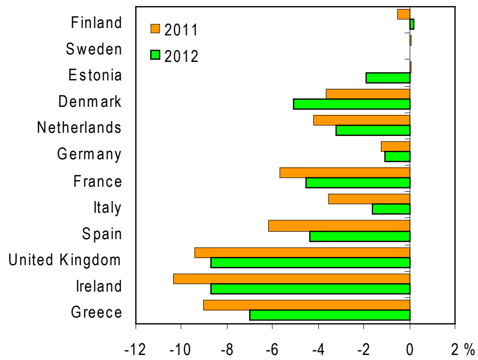
In Germany, stringent tightening of fiscal policy will be avoided. Employment remaining at a fa-vourable level and a rise of wages even

Debt-to-GDP ratio in 2011 and 2012



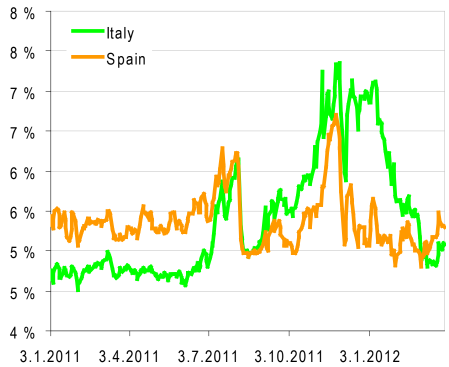
Source: OECD

Public sector deficit-to-GDP ratio in 2011 and 2012



Source: OECD

Italian and Spanish 10-year bond rates



Source: Nordea

faster than the rest of Europe will fuel a recovery in private consumption. A partly investor-driven pick-up in construction will increase investment. We forecast that the Germany's GDP will increase by 1.2 per cent this year and 2.0 per cent next year. In this forecast, the growth is faster than a number of German research institutions have projected so far. The difference in views stems from our perception that foreign trade will continue to support Ger-man growth in the coming years. To offset the decline of southern European export markets, Ger-many's industry will be able to expand exports outside this area, where growth will remain moder-ate..

Growth slower in Sweden than in Finland

Sweden's GDP growth rate fell sharply late last year when its export performance faltered due to the impact of the euro crisis. Despite this, Sweden's GDP grew last year by nearly 4 per cent. The weakening economic situation in recent months has already been reflected in the Swedish labour market, in such a way that the unemployment rate was already above the level of Finland in Janu-ary-February. We predict that the Swedish economy will also stage an upturn already in the second quarter of this year. Its GDP will grow 1.4 per cent this year and already 2.8 per cent next year.

The economic growth of Baltic countries will be 2-3 per cent this year and already significantly swifter next year. Growth is also relatively rapid in Denmark and Poland. In addition to euro area crisis countries, growth will be relatively slow this year in the Netherlands, the Czech Republic and Hungary.

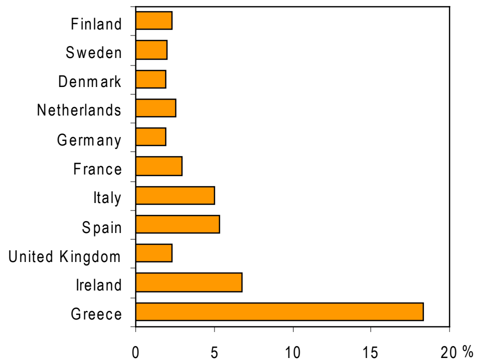
A turn for the better in the U.S. already late last year

U.S. economic growth subsided last year from 3 per cent to 1.7 per cent. GDP growth was driven by private consumption, business investment and exports. Housing investment was still frozen. After the housing bubble burst a few years ago, housing prices have declined to the 2004 level, and a lot of foreclosed houses are still coming to the market. This will slow down the recovery of residential construction.

Around the turn of last year the U.S. economy began to show signs of a slight increase in the rate of growth. Household debt and interest rates have dropped so that debt servicing expenditures in rela-tion to income have already fallen to normal levels. Household loans have indeed again begun to grow while confidence indicators have improved. Housing construction has already grown by a third from a year ago, and there is much room for growth since the level is still low. The outlook for industry has also improved, and investments are well under way, but export growth has slowed distinctly. Growth of the number of employed persons has accelerated, albeit so far only at the same pace as the relatively swift growth of the population. Thus, the vast majority of the observed decrease in the unemployment rate is explained by the decline in the labour force participation rate. We forecast U.S. economic growth will accelerate modestly this year to 2.3 per cent and to 3 per cent next year.

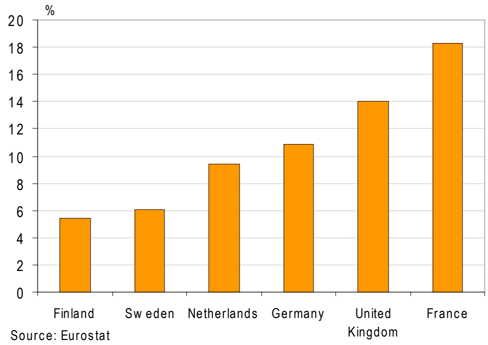
U.S. economic growth is fuelled significantly by the fact that the Federal Reserve has expressed that it will maintain its key interest rate close to zero until the end of 2014. The reduction in employers' contributions and the extension of the payment of unemployment benefits

10-year government bonds yields in March 26, 2012



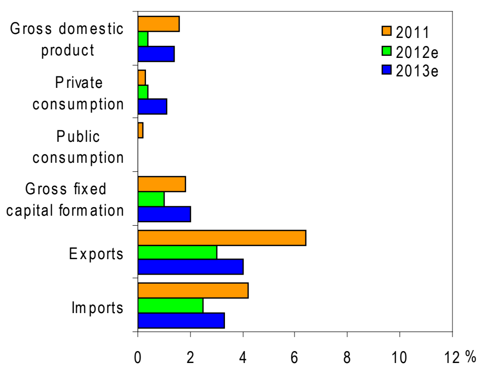
Source: Nordea

Share of goods exports to GIPSI countries (Greece, Italy, Portugal, Spain; Ireland) in 2010, %



Source: Eurostat

Economic development of euro area 2011–2013



Lähde: Eurostat, PT

until the end of this year are also significant stimuli. In the forecast they are presumed to remain in force also in 2013. There is likewise a continuation of most of the previous tax cuts in the central government's 2013 budget. The outcome of presidential and congressional elections in November may change the economic outlook for next year considerably..

China changing its growth strategy

In terms of purchasing power-adjusted GDP figures China became a larger economy than the euro area last year. The country's economic growth slowed throughout last year and ended up at 9.2 per cent. China has decided to change its growth strategy so that the target is slightly lower than previously, 7.5 per cent, simultaneously shifting the focus from investments to consumption, the GDP share of which has recently sunk to an exceptionally low level, to only about one third. This calls for a significant increase of salaries and social security, reducing the competitiveness of the country's export industries. The production structure cannot be reformed on a very tight schedule. There-fore the growth strategy change might bring about at least temporary difficulties.

The risk that China's growth will slow down dramatically cannot be ruled out, but it can be considered relatively unlikely. Partly autonomous provinces will help sustain rapid growth. In many of these provinces the growth targets are still around 12-14 per cent. On the other hand, if economic growth were indeed threatening to weaken too much, the country's leadership would be able to resort to very strong stimulus measures. Public expenditure is easy to increase. The central bank controls the exchange rate, and it has a great deal of flexibility regarding its key interest rate, the banks' reserve requirements and other means of control. China's economic growth is forecast to subside this year to 8.3 per cent, from which it will accelerate to 8.7 per cent in 2013

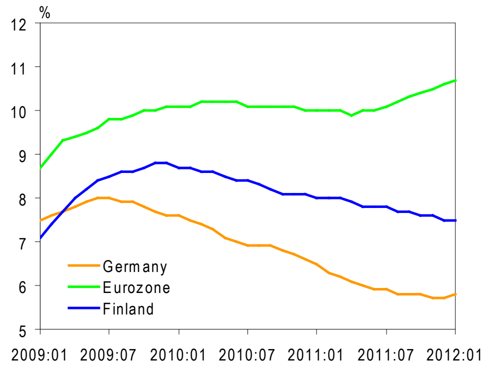
Light at the end of the tunnel in Japan

The earthquake, tsunami and nuclear disaster that occurred one year ago pushed Japan into a recession: GDP fell by 0.7 per cent. The country's nuclear power stations are awaiting security checks, and this means that one third of its electricity needs must be replaced with imported energy and savings. Reconstruction is being slow down by the huge amount of debris and a shortage of labour. Clear signs of improvement, are however already visible: consumer and business confidence has been increasing for more than half a year and employment is also improving. The decline of exports is coming to a halt. Japan's GDP growth is forecast to achieve 2 per cent this year and 2.5 per cent next year.

Growth will accelerate slightly in developing countries

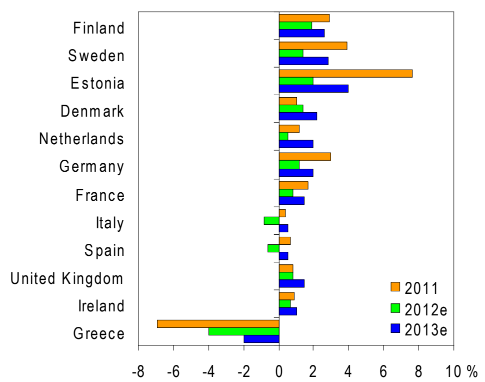
This year, the developed countries' share of the global economy measured in terms of purchasing power-adjusted GDP will already fall to less than half. Growth is appreciably quicker in certain developing countries, the largest of which – along with China – includes India, having already reached the same size as Japan, as well as equally large Brazil and Russia.

Unemployment rate in assorted countries 2009:01–2012:01



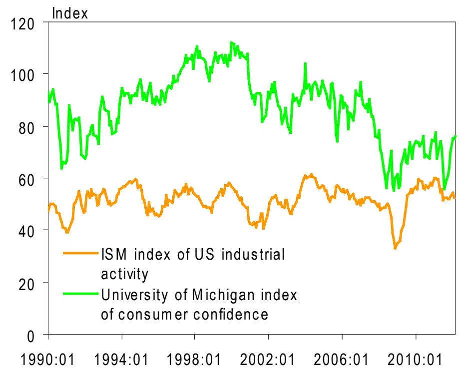
Source: Eurostat

GDP growth rates 2011, 2012 ja 2013



Source: Eurostat, Labour Institute for Economic Research

US economic indicators 1990:01–2012:03



Source: ISM, University of Michigan

Like so many other countries, India's growth slowed significantly towards the end of last year and remained at 7.3 per cent for the year as a whole. The trend stems from the weakness of exports and the fight against inflation with interest rate hikes. Growth is estimated to have continued to slow down since the beginning of the year, after which it will pick up as exports recover and the situation in the financial market improves. Growth is forecast to accelerate from this year's 7 per cent to 8 per cent next year.

Russia's growth accelerated to an almost 5 per cent pace in the second half of last year due to rising oil prices, consumer confidence and an exceptionally good agricultural harvest. Early in the year growth appears to have slowed slightly, and the country will indeed need new impetuses to growth in the future. As inflation subsided from a 10 per cent level to less than 4 per cent, the central bank can afford to lower interest rates. Newly elected President Putin gave rather large-scale election promises which are to be implemented gradually in the near future. The national debt is very small, and tax cuts, public sector pay and pension increases as well as investment projects are expected. The growth of domestic demand will boost imports strongly, but the current account and foreign currency reserves provide room for this. The country's growth will accelerate slightly in the future, this year to 4.5 per cent and 5 per cent next year.

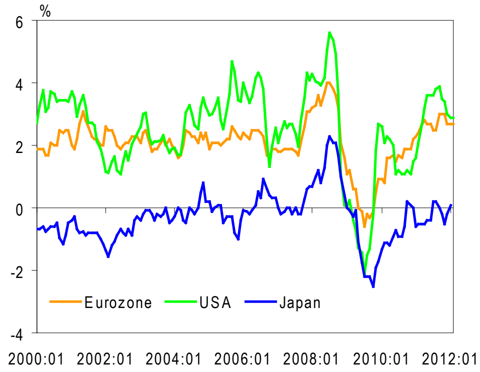
Last year, a clear slowdown in growth was seen in Brazil, and it remained at a 3.8 per cent annual rate. After the inflation rate reached its target zone of less than 6 per cent, interest rates have been lowered, which in collaboration with foreign exchange market interventions will slow down the appreciation of the country's currency. Growth indeed seems to be picking up slightly this year, reaching 3.5 per cent. It is projected to accelerate along with the global economy to 4.5 per cent in 2013.

Overall, the growth of emerging and developing economies will remain strong. The Middle East, Africa and most of Latin America are still relatively small in terms of economic clout, but Mexico, South Korea, Indonesia and Turkey are reaching the same scale as for example Australia and Canada - and they are growing substantially faster.

Raw material prices rising

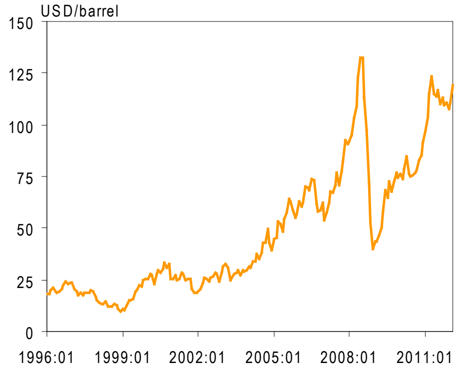
Over the past year, prices of many key raw materials have fallen significantly. Now, as the global economic growth outlook is somewhat brighter, prices have already started to climb slowly, which will also continue over the longer term. The price of oil (Brent-quality) rose already in the first half of the year by over 10 per cent from last year's average 111 dollar level. When calculated in euros the increase has been slightly higher, but overall the price shock has been much smaller than last year. The increase has been brought about in particular by sanctions against Iran and preparation for them by increased stockpiling. Significant risk factors include the escalation of the situation in Iran and other disruptions of the oil supply in different countries. We expect that oil prices will remain at an average level of just over 120 dollars. Next year it may decrease slightly if the effects of the current exceptional factors fade.

Inflation in assorted countries 2000:01–2012:02



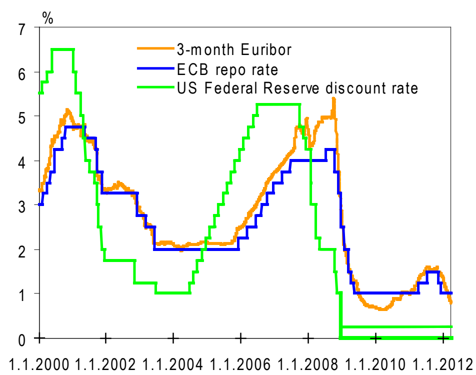
Source: Eurostat, OECD

World market price of crude oil (Brent) 1996:01–2012:02



Source: Energy Information Administration

Short-term interest rates 3.1.2000–26.3.2012



Source: ECB, Bank of Finland

Interest rates remain low

The euro area consumer price increase will decelerate this year by 0.4 percentage points to 2.3 per cent and to 2.0 per cent next year. Slowing inflation is attributable above all to the expected development of oil prices. Thus there does not seem to be a need for the Europe Central Bank to change its key interest rate, although it must be noted that its slightly less than two per cent inflation target concerns an 18-24 month range, which will soon already refer to the years 2014-2015. The ECB's monetary policy is in any case light during the forecast period, although beginning already next year exceptional measures are being discontinued. This is reflected in interest rates in such a way that they will rise to a more "normal" level. Longer interest rates will also be increased by the prospect of a possible hiking of key interest rates from 2014 onwards. As the economy strengthens, the fear of inflation getting out of hand also becomes stronger. This fear has raised its head already in Germany. If the euro area economy is develops better than forecast, the ECB's interest rate rises may indeed begin as early as next year.

The value of the euro against the dollars weakened between the period of September and January by more than 10 per cent, but after that the price has risen a few percentage points and remained at slightly more than a 1.30 level for some time. The forecast does not expect the exchange rate to change from its present level, as the crisis in the euro area is expected to remain under control. On behalf of other foreign exchange rates, it is particularly significant that China seems to have brought the strengthening of its currency to a halt at a time when its foreign trade surplus has evaporated. The Swedish krona has remained fairly strong in relation to the euro, and in the most recent months the Russian rouble has strengthened considerably.

Table 2. Demand and supply

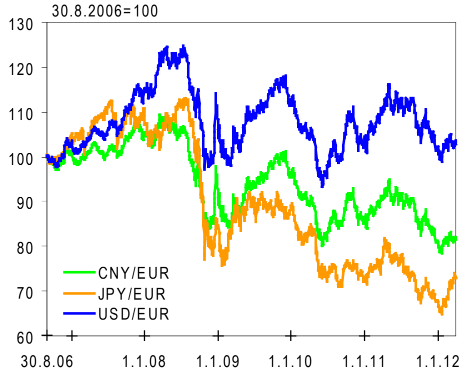
	2011 Bill. €	2011	2012f	2013f
		Change in volume (%)		
Gross Domestic Product	191,6	2,9	1,9	2,6
Imports	75,9	0,1	3,0	5,4
Total supply	267,5	2,0	2,2	3,4
Exports	74,9	-0,8	4,3	7,1
Consumption	151,0	2,6	1,7	1,0
private	105,3	3,3	2,2	1,3
public	45,7	0,8	0,5	0,4
Investment	36,7	4,6	1,8	3,6
private	31,9	5,0	2,5	4,5
public	4,8	2,4	-2,4	-2,6
Change in stocks (ml. tilastollinen ero)[1]	4,9	0,3	-0,3	0,4
Total demand	267,5	2,0	2,2	3,4

[1] *Volume change is in percentage points of GDP.*
Source: Statistics Finland, Labour Institute for Economic Research

Surplus of services offsetting trade deficit

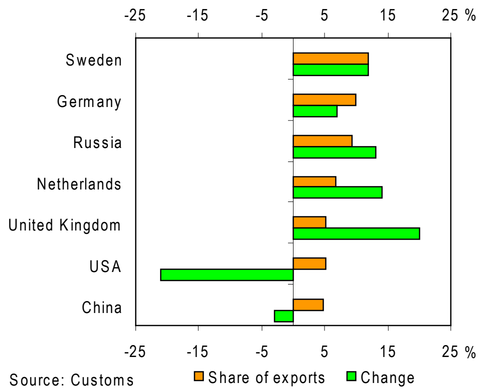
Last year, Finnish exports of goods and services fell by 0.8 per cent. Correspondingly, imports re-mained virtually unchanged. Imports of goods increased 4 percentage points faster than exports. This as well

Exchange rates 30.8.2006–26.03.2012



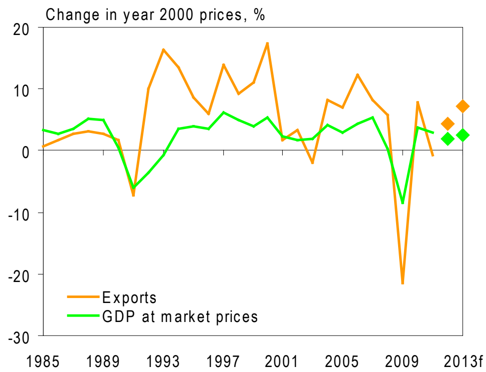
Source: ECB

Finnish merchandise exports in January-December 2011



Source: Customs

Changes in total production and exports in 1985–2013



Source: Statistics Finland, PT

as import prices' 3.5 percentage points faster increase than export prices created a deficit of about one million euro in the trade balance. According to the preliminary figures of Statistics Finland, the services account was only 25 million euro in surplus, but according to the Bank of Finland's more recent statistics, the surplus was 926 million euros. According to the Bank of Finland, the goods and services account deficit was only 189 million euros last year.

The growth rate of total exports and imports was decreased in any case by a significant drop in the foreign trade of services. However, in light of the Bank of Finland's figures, the estimate of Statis-tics Finland according to which the exports of services fell 8.6 per cent last year should be revised upwards to about -4 per cent. According to the Bank of Finland the current account ran a deficit of slightly less than 1.3 billion euros. In addition to the trade balance it was weakened by the significant deficit of income transfers.

The stabilization and mild pick up of global economic growth this year will strengthen our exports. Imports of goods however, continue to grow faster than exports of goods, and our terms of trade will continue to deteriorate. Thus, the trade deficit will grow by over a billion euro to 2.3 billion euro. To offset this, the surplus on services will increase to almost 1.5 billion euro, as the impact of exceptional factors which curbed service exports last year fades way. The strengthening of the services balance and the weakening of the trade balance reflects the higher service-intensity of the export trade. This stems from the fact that an increasing proportion of industrial enterprises' export can be classified as export of new knowledge. In addition to this the share of non-industrial export-oriented service firms is clearly on the rise in terms of overall production.

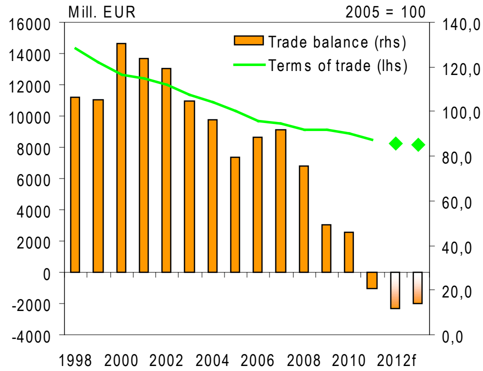
Next year, the substantial recovery in our export markets will strengthen our foreign trade in almost all respects. Exports of both goods and services will grow faster than imports, and the price of the export of goods will rise nearly as much as the price of the import of goods. Thus, the trade deficit will decline to just under 2 billion euros, and the balance of services will already exceed 2 billion euros. Next year the current account will already run a scarce surplus of about 200 million euros.

Manufacturing industries recovering next year

Finnish manufacturing sector will grow 2 per cent this year and by about 4 per cent next year. Industrial growth is, above all, slowed down by the downward trend of the paper industry, although the sector's output will already recover during this year from the low figures of the early year. Industrial growth will be bolstered by the food industry, which is being driven by exports to Russia, and metal processing, which will gather momentum from the international economic recovery. The cautiousness brought about by the euro crisis and financial bottlenecks have reduced industrial investment especially in Europe, and this is in turn slowing down the rather fast growth of its machin-ery and equipment industry and technical services. In the electronics industry output growth will not gain momentum until later this year as Nokia introduces new phones to the market. The chemical industry and electrical equipment manufacturing will grow somewhat more quickly than other industry.

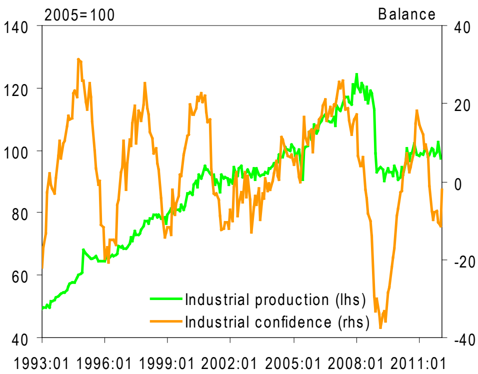
Electricity and heat production will pick up this year when

Terms of trade and trade balance 1998–2013



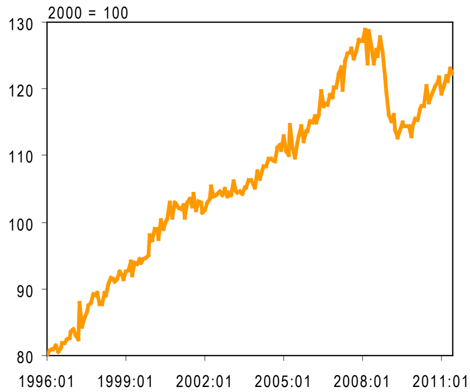
Source: Statistics Finland, PT

Industrial confidence and industrial production in Finland 1993:01–2012:02



Source: Eurostat

Trend indicator of output 1996:01–2012:12



Source: Statistics Finland

heavy industry recovers as the influence of exceptional factors associated with weather conditions passes. Construction is decelerating, but it will nevertheless grow this year by just under 2 per cent and already 4 per cent next year. Of the service industries, real estate and business services are growing relatively fast, nearly 3 per cent this year and already 5 per cent next year. Trade and transport growth will slow down significantly, and public services will not grow at all next year.

Housing construction subsiding - other construction continues to grow

Total investments increased by approximately 4.6 per cent last year. Quarterly growth nevertheless slowed towards the end of the year. Weakening economic expectations will also affect the current year's investment, but in 2013 they will experience a mild pick-up in growth.

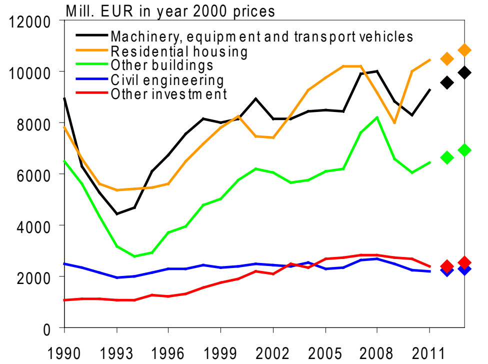
Table 3. Key forecasts

	2011	2012f	2013f
Unemployment rate (%)	7,8	7,8	7,2
Unemployed (1 000)	209	209	194
Employed (1 000)	2474	2486	2510
Employment rate (%)	68,6	69,3	70,3
Inflation, consumer price index (%)	3,4	2,9	3,2
Wages, index of wage and salary earnings,%	2,7	3,2	2,7
Real disposable income of households (%)	1,5	1,8	1,1
Current account surplus (Bill. €)	-0,8	-0,8	0,2
Trade surplus (Bill. €)	-1,0	-2,3	-2,0
Central governement surplus			
Bill. €	-5,4	-4,5	-1,4
% / GDP	-2,8	-2,0	-0,6
General governement financial surplus			
Bill. €	-0,9	0,5	3,8
% / GDP	-0,5	0,2	1,8
Emu debt			
% / GDP	48,6	49,0	47,4
Tax rate (%)	42,8	43,5	44,0
Short-term interest rates (3 month Euribor)	1,4	0,8	1,1
Long-term interest rates (10-year gov't bonds)	3,0	2,4	2,8

Source: Bank of Finland, Statistics Finland, Labour Institute for Economic Research

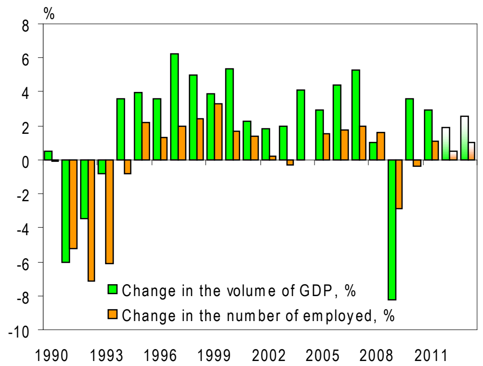
Residential construction continued to increase in early 2011, but the growth rate slowed down and in the last quarter of the year the volume of residential construction already fell a little in compari-son to the previous year's last quarter. The level of residential construction will remain almost unchanged this year: volume is sustained by renovation, although new construction is likely to decline. Non-residential construction continued to grow in the

Investments 1990–2013



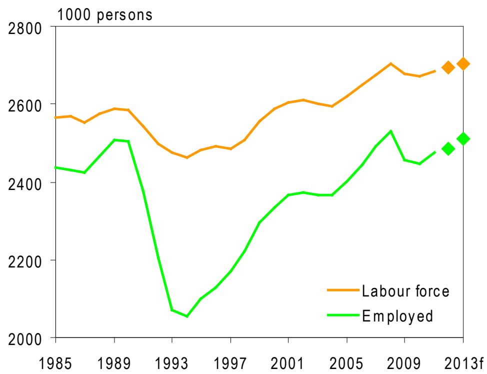
Source: Statistics Finland, PT

GDP and employment 1990–2013



Source: Statistics Finland, PT

Supply of labour and employment 1985–2013



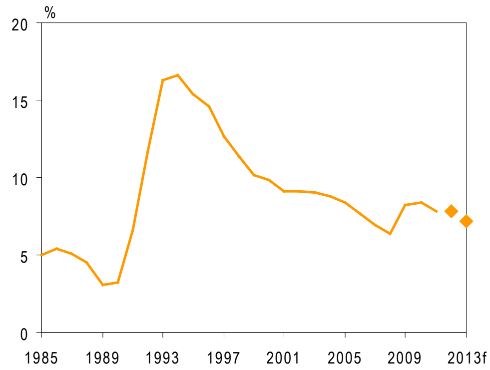
Source: Statistics Finland, PT

last quarter of last year, and it will continue its modest growth this year. Both housing and non-residential construction will grow more rapidly next year, housing construction by about 3 per cent and non-residential construction at an annual rate of approximately 4.5 per cent. Civil engineering construction experienced a decline last year. We forecast, however, about 2.5 per cent growth this year and next.

Machinery and equipment investment grew 12 per cent last year. During the year, growth strengthened towards the end of the year. The uncertain economic outlook, however, will weaken the strong growth of these investments this year: we predict 3 per cent real growth. Next year, improving prospects will boost real growth to 4 per cent.

Overall, private investment is projected to grow by 2.5 per cent this year and 4.5 per cent next year. Public investment will decline this year to 2.4 per cent and 2.6 per cent next year, mainly due to the tight financial situation of the municipalities.

Unemployment rate 1985–2013



Source: Statistics Finland, PT

Employment growth stalling this year but picking up next year

Employment increased by an average of 1.1 per cent last year. In January this year, employment remained more or less unchanged, and increased by 1.3 per cent in February. During the end of this year and next year employment growth will be slower than last year due to economic growth slow-ing down. We forecast that this year employment will increase at an average pace of 0.5 per cent. In 2013, growth will pick up somewhat to an average of 1 per cent. As regards job creation, this year the number of jobs will rise by 12,000 and next year by 24,000.

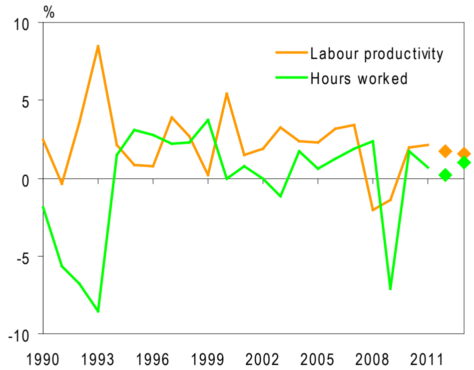
During a recession, the population's labour force participation rate typically declines because those left without work exit the labour force as active job seeking comes to an end. As the employment situation improves, the participation rate usually begins to rise again. The relative aging of the Fin-nish population also contributes to the reduction of the participation rate, because it is lower in the expanding older age groups. Last year, the labour force participation rate remained unchanged. Thanks to the slow recovery of the employment situation and the aging of the population, major changes in the labour force participation rate are not expected in the near future either. Thus, the participation rate will increase this year and next year by 0.1 percentage points.

Due to the combined effects of changes in the amount of employment and labour, the number of the unemployed will remain unchanged this year and will decrease next year by 15,000 people. The unemployment rate this year will average 7.8 per cent, remaining unchanged from last year, and will decrease next year to 7.2 per cent.

The youth unemployment rate, concerning 15-24 year olds, has been a specific matter of concern after the 2009 economic crisis. Youth unemployment rose sharply according to the Labour Force Survey in 2009 and still in the early months of 2010, but it has since levelled off and turned to a slight decline. Last year, the number of young people employed increased by 3.6 per cent and the youth unemployment rate decreased 1.3 percentage points in comparison to the previous year. However, youth unemployment is still distinctly higher than before the 2009 recession. The unem-ployment rate rose slightly in January from the previous year and declined in February.

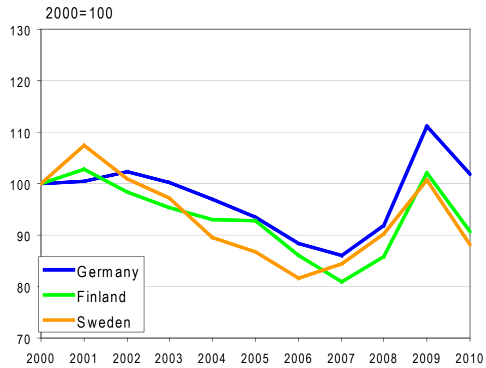
The interpretation of the youth unemployment rates of the Labour

Change in labour productivity and hours worked 1990–2013



Source: Statistics Finland, PT

Nominal unit labour costs (manufacturing industry) 2000–2010



Source: AMECO

Force Survey is problematic since some of the employed and unemployed young people are students at the same time. The slow employment growth, however, is also likely to affect young people's employment opportunities this year and next and campaigns targeted at young people, such as implementing a social guarantee, are a step in the right direction.

Adaption of the amount of work within the economy occurs not only through employment, but also through hours worked. Typically, the number of hours worked adapts to turning points in the econ-omy more than jobs, because hours are more easily adjusted than the number of people employed. Thus, hours worked also begin to rise before employment figures as output starts to grow once again. As a boom continues, the development turns around so that employment increases slightly more than the number of hours worked. In 2011, the number of hours worked rose only slightly less than employment, by 0.9 per cent. The growth of the number of hours worked will be reduced this year by layoffs and reduction of overtime. This year, the number of hours worked will increase by 0.2 per cent, i.e. at a slightly slower rate than employment. Next year they will increase by one per cent, i.e. at the same pace as employment.

Economic expansion and contraction also take place partly through productivity growth. Productivity increased by 2 per cent last year. This year, productivity will improve by 1.7 per cent as GDP grows by 1.9 per cent and the number of hours worked by 0.2 per cent. In 2013 correspondingly, productivity growth will be 1.6 per cent.

Table 4. EMMA-model forecasts for the years 2012 and 2013

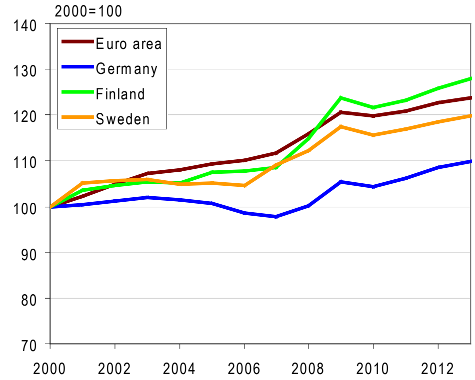
	2012 (%)	2013 (%)
Private consumption	+1,8	+1,7
Private investment	+2,4	+1,8
Exports	+3,4	+8,5
Imports	+2,6	+7,1
GDP¹	+1,9	+2,6

Public sector development in our institute's forecast.
Source: Labour Institute for Economic Research

Tax hikes fuel inflation

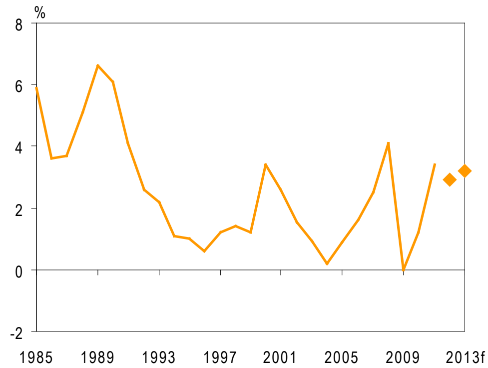
Consumer prices rose last year at a slightly decelerating pace, and the rise for the year as a whole remained at 3.4 per cent. Hikes in taxes on alcohol, tobacco, vehicles, lotteries, sweets, newspapers, hairdressing services and fuel as well as housing and food becoming more expensive will still sus-tain inflation in the beginning of this year, but the inflation rate for 2012 as a whole is going to be about half a percentage point lower than last year. The price increases of food, housing, transport and certain other types of products have clearly slowed down despite the tax increases. Next year, the one percentage point increase of the value-added tax will increase consumer prices by a total of more than half a percentage point, which will again spawn an increase in the rate of inflation to 3.2 per cent.

Nominal unit labour costs (total economy) 2000–2011



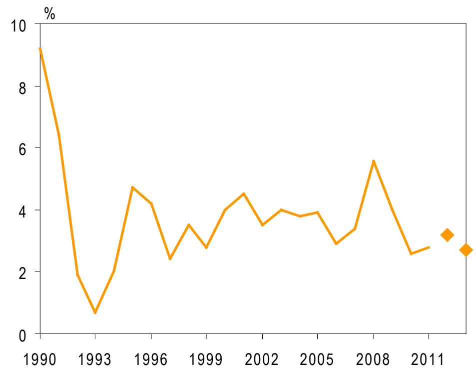
Source: AMECO

Change in consumer prices 1985–2013



Source: Statistics Finland, PT

Change in level of earnings index 1990–2013



Source: Statistics Finland, PT

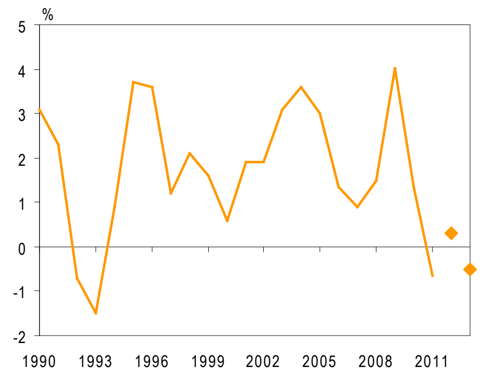
Growth of real earnings might subside next year

Last year, workers' real wages fell by 0.6 per cent when the rate of price increases exceeded income development. The year was exceptional, because nearly 20 years had elapsed since the previous decline in real wages. On the basis of contract wage increases, average wages climbed by an aver-age of 2 per cent and total wages increased an average of 2.7 per cent.

The two-year collective agreement signed by labour market organizations in autumn of 2011is the most important factor regarding the current and next year's wage development. The settlement which emerged following negotiations between the confederations was taken as a comprehensive basis for union-level agreements, and more than 90 per cent of wage receivers are included within the collective agreement. The government as participated in the outcome, which included e.g. an extraordinary adjustment to the central government income tax scales and an additional decrease to the corporate tax. An equal cost effect for wage increases is defined in the agreement for different sectors, but the union-level agreements differ from each other for instance in the emphasis of general increases and items to be agreed locally. The framework agreement's cost increase for the first 13-month period is 2.4 per cent, and 1.9 per cent the following year. In addition to the effects of wage increases these figures include the cost impacts of possible changes in other working condi-tions. Wage development is also affected by a 150 euro one-off payment to be made in 2012.

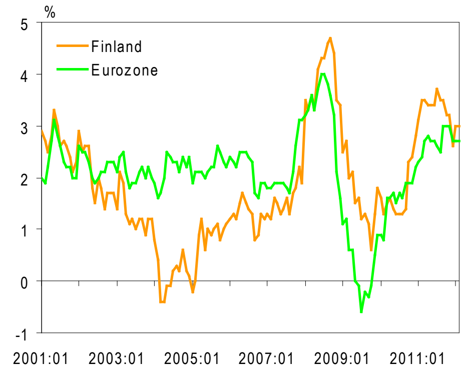
This year, wages will increase by 3.2 per cent and 2.7 per cent next year. As inflation remains at nearly 3 per cent in both years, real wage development remains roughly unchanged. Average in-comes are growing somewhat faster, however, than the index of wage and salary earnings. A structural factor behind this trend is the growth of the share of tasks requiring higher education.

Annual changes in real wages 1990–2013



Source: Statistics Finland, PT

Harmonized index of consumer prices 2001:01–2012:02



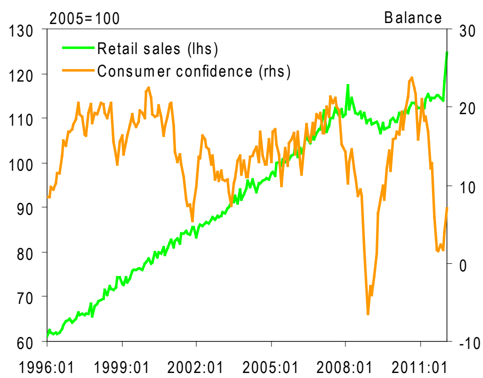
Source: Eurostat

Household disposable income continues to grow

The disposable real income of households grew by 1.4 per cent last year. The wage bill grew by nearly 5 per cent in nominal terms, while property and entrepreneurial income rose by a total of nearly 10 per cent and social benefits by about 3 per cent. The taxes of households increased slightly faster than their income, and accelerated inflation also slowed down the increase of purchasing power.

This year, the wage bill will grow by 3.9 per cent, which is somewhat slower than last year. Earnings growth will speed up somewhat, but employees' increase of labour input is still far below last year's. The social benefit growth is driven by, among other things, the development of the number of pensioners and social security index adjustments, which will exceed earnings growth this year. Property and entrepreneurial income will grow slightly more quickly than labour income in the future. The nominal growth of household's income will thus continue to be almost as strong as last year. Changes in direct taxation will not yet affect the deve lopment of purchasing power this year and inflation will slow

Consumer confidence and retail sales in Finland 1996:01–2012:02



Source: Eurostat

down slightly. Households' real purchasing power is growing roughly at the same pace as last year, by 1.7 per cent.

Year 2013 brings with it a slow-down in wage increases and tightening of taxation. Income taxation will be tighter both on the central government and municipal levels and the pension contributions of insured persons will continue to rise. On the other hand, the employment rate will improve more than during this year and the wage bill will increase at the same pace as this year. However, tax hikes in combination with accelerating inflation will reduce the increase of purchasing power. Real disposable income will grow more slowly next year than this year, by just over one per cent.

Private consumption still driven by pent-up demand

Private consumption grew quickly last year, by 3.3 per cent. Consumption growth was distinctly swifter than the growth of households' disposable income. The savings rate did indeed fall substan-tially at the same time, from slightly over 4 per cent to 1.5 per cent.

Pent-up consumer demand continues reflect upon private consumption. Households' purchasing power even increased during the crisis year of 2009 and has since risen relatively steadily. Con-sumption declined significantly during the economic crisis, but a positive and steady household income development has made it possible to restore the relationship between income and consump-tion to its previous level.

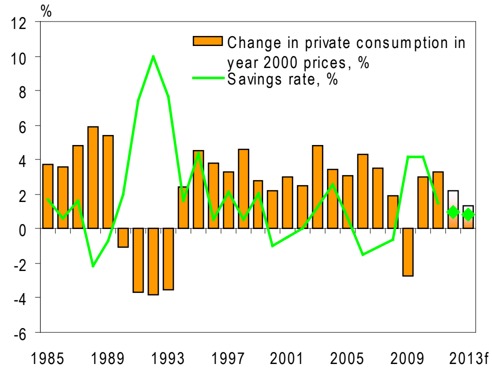
Last year, growth was fastest in consumption of durable consumer goods. The consumption of semi-durable consumer goods and services also increased significantly, but the consumption of non-durable goods increased only slightly. Consumption demand was therefore focussed primarily on consumption of those commodities that declined the most during the recession of 2009.

During the forecast period the purchasing power of households is expected to continue growing, reaching an average of one and a half per cent annual growth. This enables households to continue to increase their consumption. Data on improving consumer confidence and the economic outlook of the wholesale and retail trade and the services sector regarding the ongoing year are in line with this analysis. Private consumption is projected to grow by 2.2 per cent this year and by 1.3 per cent next year. Tax hikes are contributing to the slowdown in consumption growth. The savings rate will continue to decline somewhat

Central government tax revenues growing.

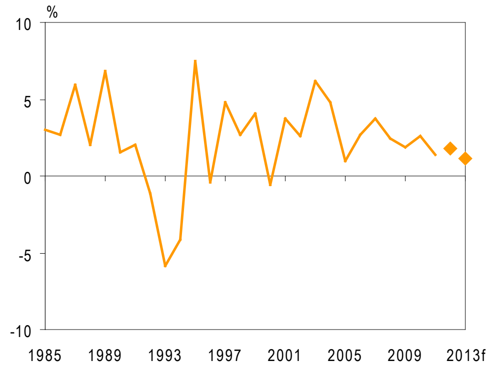
Indirect taxes were increased this year on a broad front: magazine subscriptions are now subject to VAT, while excise, car and vehicle taxes were raised. Excise taxes were increased for tobacco, al-cohol, sweets, ice cream, soft drinks, fuel, and lotteries. The rise in the car tax, which is also de-signed to steer consumption in a more environmentally friendly direction, came into effect in early April. As a result of tightening taxation and broadening its base, indirect tax revenues will grow 7.8 per cent this year, which means more than a 2 billion euro increase in

Private consumption and savings rate 1985–2013



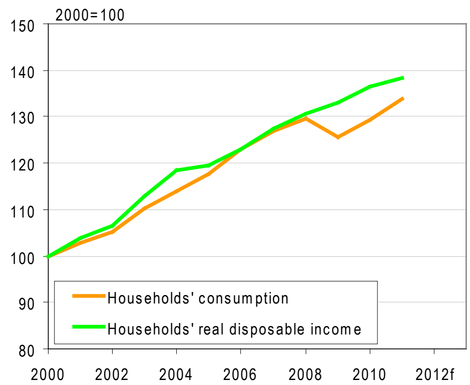
Source: Statistics Finland, PT

Change in household's real disposable income 1985–2013



Source: Statistics Finland, PT

Households' real disposable income and consumption 2000–2013



Source: Statistics Finland

central government revenues.

Indirect tax revenues will continue to increase next year. This stems partially from the fact that the government decided in its framework negotiations to increase the general VAT rate by a percentage point from the beginning of next year. The in-crease of the VAT rate will increase indirect tax reve-nues by about 750 million euros. With a simultaneous increase in the value of private consumption the central government's indirect tax revenues are forecast to increase by a total of 8 per cent over the next year

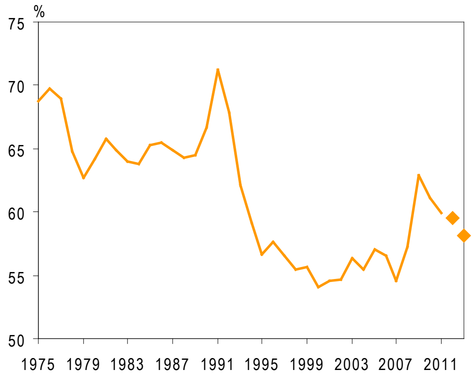
Last year direct taxes collected by the central government in-creased at a rate of more than 16 per cent. Wage bill growth will sustain income tax revenues this year, as the central government's tax base is adjusted for inflation and rising income levels. In ad-dition, the two percentage point increase of capital income taxa-tion, differentiation of the tax rate for amounts exceeding 50,000 euros to-gether with tightening dividend taxation for non-listed companies will increase the direct tax reve-nues of the cent-ral government by some 230 million euros this year. Reducing mortgage interest deductions and the cutting of domestic labour deductions will increase the governments' tax reve-nue by about 140 million euos. The central government's corporate tax reve-nue, in turn, is increased by lowering the share of corporate tax incomes diverted to the municipalities by five percentage points this year. A one percentage point decline in the corporate tax rate has the opposite effect. All in all, the central government's corporate tax revenues will increase, and its direct tax revenue will increase by 4.7 per cent this year.

In 2013 and 2014, the taxation of earned income will be tightened, because the earned income tax scales will not be adjusted for inflation. The fiscal impact of the tightening is a total of 800 million euros. In addition, next year the government will tighten the earned income taxation of those earning more than 100,000 euros per year, by creating a new category in the earned income tax scales, while the taxation of inheritances of more than one million euros is raised and the taxation of large pensions is increased to correspond to earned income taxation. These solidarity taxes will increase central government tax re-venue by a total of 115 million euros.

Tax revenues will also be increased by the increase in trans-fer tax and tightening of reimbursements for mileage driven. On the other hand, there will also be tax relief regarding the tax deductibility of R & D expenses and fixed-term growth incenti-ves will be increased, e.g. through raising imputed acquisition costs of investments in non-listed SMEs. The aforementioned decisions, together with a growing wage bill will increase the central government's direct tax revenue by a total of 8 per cent next year.

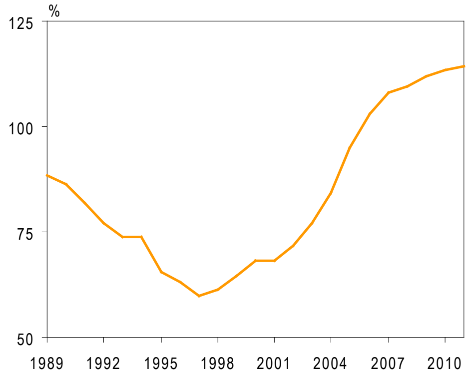
Central government transfers to municipalities will increase by 3 per cent this year. Next year the revenue sharing received by municipalities will be reduced so that they will grow by only 2.5 per cent from this year's level. All in all, the rapidly growing tax revenues and relatively slow-growing expenditure will imp-rove the central government's financial position significantly du-ring the fore-cast period. The central government's EDP deficit is projected to decline from last year's 5.4 billion euros to 4.0 billion euros this year and 1.4 billion euros next year.

Functional distribution of income in business activities 1975–2013



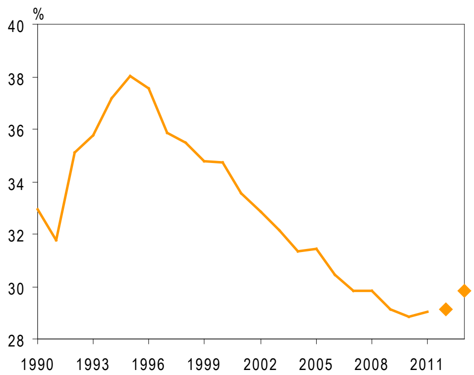
Source: Statistics Finland, PT

Household debt ratio 1989–2011



Source: Statistics Finland, PT

Wage earners' income tax rate 1990–2013



Source: GIER, LIER, Taxpayers' Association of Finland (TAF)

Municipalities in a challenging situation

Wage bill growth and tax hikes in several municipalities will increase municipalities' income tax revenue this year. On the other hand, the share of corporate taxes received by municipalities will decline by five percentage points in comparison to last year. Altogether, direct taxes received by the municipalities will increase 3.8 per cent this year. Government cost-cutting measures are tightening municipal finances this year and next: this year, revenue sharing received by municipalities will be cut by 631 million euro, while decisions made in the most recent framework negotiations will re-duce the revenue sharing further starting next year, so that their share will be 520 million euros lower in 2015. Many municipalities are indeed reacting to the policies by increasing taxation: the average municipal income tax rate is projected to increase by 0.15-0.20 percentage points next year. In addition, the municipalities seek to increase their revenues with property tax increases. Overall, growth in hours worked and tax increases will bolster the direct taxes received by municipalities by 5.1 per cent next year.

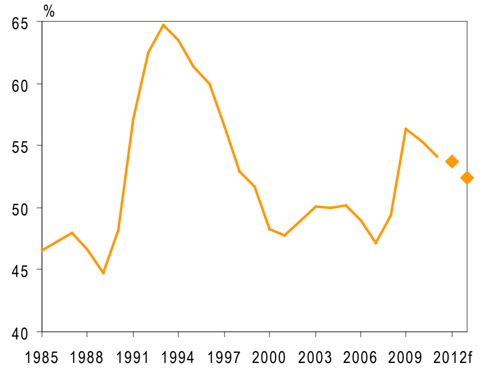
Social security payments received by employment pension institutions and social security funds will increase this year by 5.5 per cent and 5.6 per cent next year. Contributions will be increased by the favourable development of the wage bill and the 0.4 per cent pension contribution increases for both years agreed upon in the so-called social incomes policy agreement. On the other hand, in-creases in the basic daily allowance of unemployment insurance and labour market support will raise expenditures this year. In addition, the high index-linked pension increases due to inflationary adjustments will raise the employment pension institutions' expenditure significantly both this year and next. Thus the surplus of employment pension institutions and social security funds will remain almost unchanged in relation to the GDP in both forecast years.

General government in surplus already this year

The tax-to-GDP ratio will rise this year by 0.6 percentage points as a result of hikes in indirect taxa-tion and social security contributions. Next year the tax-to-GDP ratio will rise further since indirect and direct taxation is being raised. Next year the tax-to-GDP ratio will already be 44.0 per cent, which is almost a percentage point higher than that of last year. On the other hand, the ratio of gov-ernment expenditure to GDP will fall in both years, while nominal GDP will grow significantly faster than public spending. The ratio of public spending to GDP will fall from 54.1 per cent to 53.7 per cent this year and to 52.6 per cent next year.

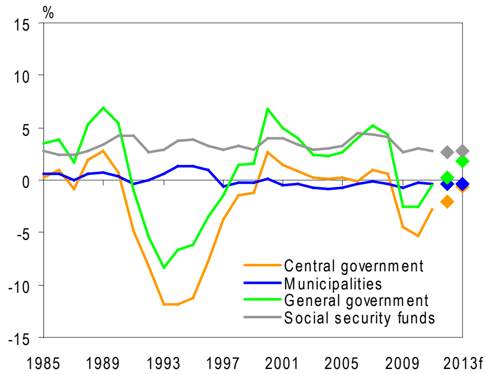
The total public sector's financial position will improve and start to run a small surplus this year. Next year, the public sector's financial position will continue to improve, above all, as a result of the improvement in the central government's financial position. Next year the deficit of the central government will decline to less than one per cent in relation to GDP, while the total public sector's surplus will be 1.8 per cent of GDP.

Public expenditures as percentage of GDP 1985–2013



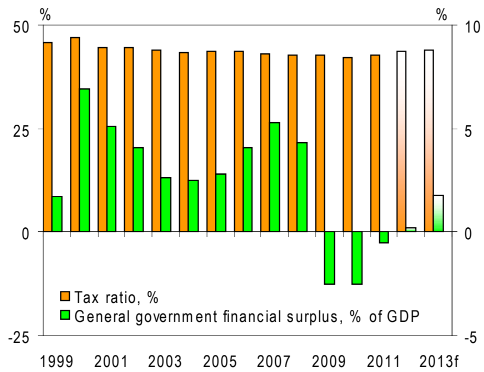
Source: Statistics Finland, PT

General government financial surplus as percentage of GDP 1985–2013



Source: Statistics Finland, PT

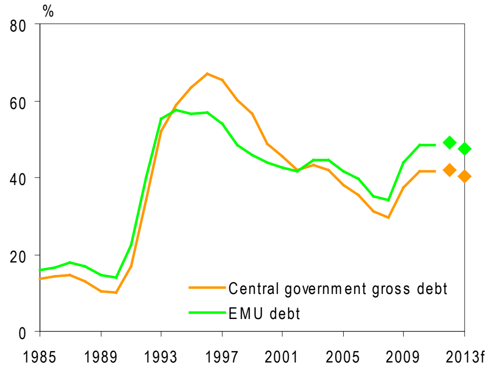
Public finances 1999–2013



Source: Statistics Finland, PT

The economic forecast of the Labour Institute for Economic Research is based on the projections of the EMMA model. The model's GDP forecast is consistent with that of the Institute.

Central government gross debt and general government EMU debt as percentage of GDP 1985–2013



Source: Statistics Finland, Ministry of Finance, PT

Government's fiscal policy

The Finnish government's fiscal policy is becoming pro-cyclical, which is attributable to the central government deficit and debt targets set in the government's programme and the implementation of a stringent budget stance spearheaded by Germany, where the public sector's structural deficit is also controlled. The exaggerated fear that the Finnish government's credit rating might be lowered also affects fiscal policy.

In its recent framework for spending and tax decisions the government has preliminarily decided to raise taxes by 1.5 billion euros and to cut expenditures by 1.2 billion euros. The most important decisions are the lifting of value added tax by one percentage point at the beginning of next year, as well as the decision to refrain from adjusting earned income taxes for inflation in 2013 and 2014. Because the tightening of taxation will reduce the tax base at least temporarily, mputed tax revenues by 1.8 billion euros. On the other hand, the tax deductions for R & D expenditures as well as fixed-term growth incentives will ease taxation by just under 300 million euros. The income tax deductions of low-income persons and increases in the basic allowance will cut taxation by 65 million euros. Thus, changes in the tax base will boost tax revenue by almost 1.5 billion euros.

According to preliminary analysis, the distributional impacts of the tax solution appear to be neu-tral, which is positive from the standpoint of public approval. The tightening of central government earned income taxation for high incomes also increases the progressivity of taxation. Over the years it has been substantially weakened when the share of municipal income tax has increased and the share of central government income taxes correspondingly decreased. Without simultaneously increasing the progressivity of capital income taxation, however, the solution increases the difference in taxation between persons with high incomes and those with corresponding capital gains.

The most extensive tax hikes will be carried out in the budget planning period beginning in 2013, when the combined effect of the tax hikes is more than one billion euros. The government perhaps wishes to demonstrate its decision-making ability to the credit rating agencies and that it will stick to the targets stipulated in the government's programme. The front-loaded implementation of tax hikes nevertheless means cuts in household purchasing power in 2013, when the development of real income otherwise appears to be flat. The risk in this case is that domestic demand might remain stagnant in a situation where the demand from international economies is still undermined by con-siderable uncertainty.

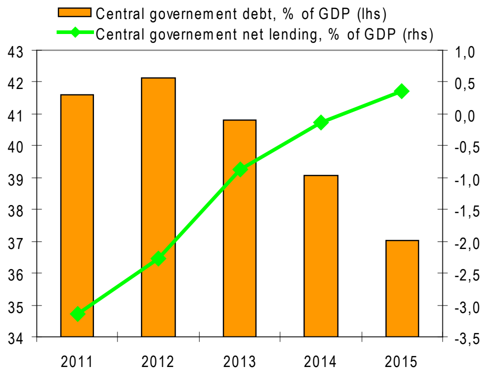
The government has also decided to continue in 2014 and 2015 the practice whereby the munici-palities' share of corporate tax revenues is raised to 27.87 per cent from the previous 22.87 per cent. This decision reduces central government tax revenue by more than 260 million euros. In this re-spect, the decline in central government tax revenues does not stem from changes in enterprises' or households' tax bases, but rather current transfers between central government and municipalities. These decisions will increase central government spending by just under 300 million euros, so that the reported 1.2 billion euros of expenditure cuts are reduced to just over 900 million euros. According to preliminary information, it appears that most of the spending cuts are scheduled to take place in 2015, a significant part also in the year 2014, but hardly any at all next year.

Since the government cannot be expected in the future to turn a blind eye to how the government finances and employment develop, it can be assumed that spending cuts slated for 2014 and 2015 are conditional. It appears that the central government's deficit will be shrinking, and the central government's debt as a percentage of GDP will be following a downward trend to such an extent that in the years 2014 and 2015 there will be no need for spending cuts to be implemented on the basis of the government programme. In this programme, it is assumed that the government debt relative to GDP will start to fall and the government deficit will narrow to less than one per cent of GDP during its term in office. The government programme also includes a clause stipulating that no more than 30 per cent of an improved fiscal position can be used for spending increases in line with the government's strategic goals if the central government's debt-to-GDP ratio turns to a clear decline before 2015.

The adjacent forecasts extending up to the year 2015 for the general government net lending and central government debt take into account the government's decisions reached in its March framework negotiations. In addition, it has been assumed that the GDP will grow by 2.8 per cent in 2014 and 2.5 per cent in 2015. A tight lid on expenditure together with favourable development of tax revenues will spawn a surplus in the total public sector next year. The central government's deficit will decline rapidly and the central government's gross-debt-to-GDP ratio will fall steadily.

If the central government's net lending were 3 billion euros less than the forecast presented in the adjacent table, the central government's deficit relative to GDP would improve to one per cent. Even at that time, the central government deficit would barely meet the targets set in the govern-ment's programme. The central government's debt-to-GDP ratio would still exhibit a declining trend. Calculated in this way the central government's need to adjust would be 3 billion euros, of which 30 per cent or 900 million euros could be used to increase central government expenditures according to the government programme. This suggests that government's decision in its framework negotiations to tighten spending by a further 900 million euros could be overturned.

Central government gross debt and net lending 2011-2015



Source: Statistics Finland

It should be noted that despite the apparent tightness of the spending framework, they have previously been modified if needed. Thus, in its March framework decision the government decided to raise previously agreed spending limits by 0.5 billion euros. Depending on the interpretation, the spending cuts are estimated to range from zero to over 900 million euros. Only if the international economy is hit by a deep new crisis will there be a need (under the government programme) for larger spending cuts.

At its best, fiscal policy should smoothen out cyclical fluctuations. In this respect austerity measures may become a problem. If economic development is much weaker than PT forecasts, the government may have to resort to means that exacerbate the recession further. However, if economic growth is much more favourable than expected, there is a risk that the government will unnecessarily refrain from implementing spending cuts (or alternatively new tax hikes) and thusnot take ad-vantage of the opportunity to strengthen public finances and reduce its long-term sustainability gap without weakening the labour market. But in the most likely scenario, it would be wise for the government to compromise on spending cuts and boost employment because a strong financial position gives the central government the leeway to do so.

Table 5. General Government Net Lending 2011-2015

Net lending	2011	2012	2013	2014	2015
Central government	-6004	-4526	-1856	-300	805
Municipalities	-833	-892	-754	-731	-723
Pension institutions and social security funds	5301	5407	5894	6374	6373
Total general government	-1536	-11	3283	5343	6455

Figures are millions of euros, without swap corrections

Source: Statistics Finland, PT

Reforms span lengthening of working careers "from the middle"

The central government's budget framework agreement and the working career agreement of the key labour market organizations have recognized the need for reforms in unemployment security and the pension system to be implemented in the next few years.

Public debate on working careers is typically focussed on the period toward the end of a person's career and the minimum age of eligibility for retirement. Nevertheless, reforms related to structural unemployment and work incentives also affect the length of working careers. Their impact is felt in the "middle" of careers and they reflect on the amount and duration of spells of unemployment as well as the number of hours worked. With the exception of youth unemployment, the means to lower unemployment have received little attention in recent years.

Economic theory suggests that job seekers should weigh all the benefits and costs of work accepted: higher unemployment benefits reduce the incentives to take a job, and the duration of benefits affects the duration of unemployment. A job seeker also takes into account the fact that taking a job improves future social security and employment opportunities. The dependence of unemployment benefit on other household income also affects work incentives: the additional income from taking a job will be reduced if the spouse's unemployment benefits decrease as a result.

The government has proposed that the needs testing of labour market support with respect to the spouse's income will stop, thus eliminating the incentive problems described above. According to the working career agreement the working history required for receiving the earnings related unemployment allowances will be reduced by two months to six months. A shorter requirement for the work history increases the incentive to seek and accept shorter job assignments, because they improve future unemployment benefits. Earning the eligibility for benefits after a shorter employment period may nevertheless increase and prolong periods of unemployment for those who under the old system would not have been eligible for earnings-related unemployment benefits exceeding the basic security.

After the reforms the length of unemployment benefits will also depends on the job seeker's activity. In the future, the duration of unemployment benefits will be shortened to 400 days if the unem-ployed person refuses to participate in activation measures. This will shorten the duration of unem-ployment, particularly after long spells of unemployment. In any case the duration of unemployment benefits for those with less than three years of work history will be shortened to 400 days or to 300 days if the person refuses to participate in activation measures. This will also shorten the average duration of unemployment.

The reforms also call for increased activation measures geared toward the unemployed and further obligations for labour administration. This is also important for the reduction of structural unemployment. Especially the elderly long-term unemployed have been left out of the scope of these measures almost completely. Successful reform will ultimately require development of unemployment benefits and active labour market policy as a whole.

From the standpoint of reforms aimed toward the end of the working career, previous studies indicate that the greatest impact has come from lifting of the lower limit of the so-called unemployment tunnel to 59 years of age. The unemployment tunnel has encouraged the focussing of lay-offs on older workers. Kyyrä's (2010) results show that lifting the lower limit of the unemployment tunnel by one year increased the average time spent in employment by only 0.8 months. Apparently new increases in the age limit for the start of the unemployment tunnel have a smaller impact on working careers than previously. Although the importance of an individual increase is relatively small, the hikes in the age limits over time are of significance as a whole (Jauhiainen and Rantala, 2011). Reforms of the unemployment tunnel include an increase in the employer's experience rating.

In addition, in accordance with the working career agreement the early old-age retirement pension will be discontinued and the age limit for part-time pension lifted to 61 years. Last year, only a few thousand people opted for early old-age retirement and therefore their working until the age of 63 would have had relatively little impact on the average length of working careers. The studies have not provided strong evidence of a prolonging effect on part-time retirement careers, and from a cost point of view, it has proven to be an expensive means of extending working life. The impacts of postponing the retirement age limit on the expected retirement age are probably minimal, but the reform does, however, have a positive impact on the labour input of older workers.

As a consequence of age limit changes the expected remaining length of the working lives of 50-year-olds has increased significantly. This change has, at least over time, a positive effect on the employment opportunities for older people, because from the standpoint of the hiring firm the length of the remaining career is a key factor in the recruitment decision (Ilmakunnas and Ilmakunnas 2011). This recruitment effect contributes to the lengthening of the working careers, but not very quickly.

The labour market organizations have estimated that the solutions prolong the working careers by about a year. To achieve this, the activation measures already decided upon and the qualitative improvement in working life will have to very effective.

Sources

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