

Erkki Liikanen  
Bank of Finland

## **Growth potential and public finances need further strengthening**

18 December 2017





# **Euro area monetary policy remains accommodative and conducive to higher inflation**



# Euro area growth and price outlook

Eurosystem's December projection (cf. ECB's September projection)

- **GDP**
  - **2017: 2.4% (+0.2)**
  - **2018: 2.3% (+0.5)**
  - **2019: 1.9% (+0.2)**
  - **2020: 1.7%**
  
- **Inflation**
  - **2017: 1.5% (unchanged)**
  - **2018: 1.4% (+0.2)**
  - **2019: 1.5% (unchanged)**
  - **2020: 1.7%**

***Economic growth and the price outlook are based on the assumption of a continuation of the strongly accommodative monetary policy throughout the forecast horizon.***



## Monetary policy still accommodative

- **Monetary policy will remain accommodative until the Governing Council sees a sustained adjustment in the path of inflation consistent with its inflation aim.**
  - **Net asset purchases will be made at a monthly pace of EUR 30 billion from January 2018 until the end of September 2018.**
  - **The net asset purchases may be continued beyond September 2018 if the Governing Council does not see a sustained adjustment in the path of inflation consistent with its aim without the support of monetary policy.**
  - **After the end of the net asset purchases, the Eurosystem will reinvest the principal payments from maturing securities purchased under the APP which contributes to the accommodative monetary policy stance.**
  - **The ECB Governing Council continues to expect key ECB interest rates to remain at their present levels for an extended period of time and well past the horizon of the net asset purchases.**



# **Finnish economy: Growth potential and public finances need further strengthening**



## The current news on the Finnish economy is positive, and the outlook has improved

- *Growth has continued and is now more broadly based than before*
- *Exports and corporate investment are both growing, in addition to household demand*
- *The employment rate has gradually risen and the general government deficit shrunk*
- *Cost-competitiveness has taken a turn for the better*



## The objective should be ambitious

- *The economy is still struggling to rise from a level weakened by many years of sluggish developments*
- *Need to strengthen*
  - *Growth potential*
  - *Outlook for public finances*

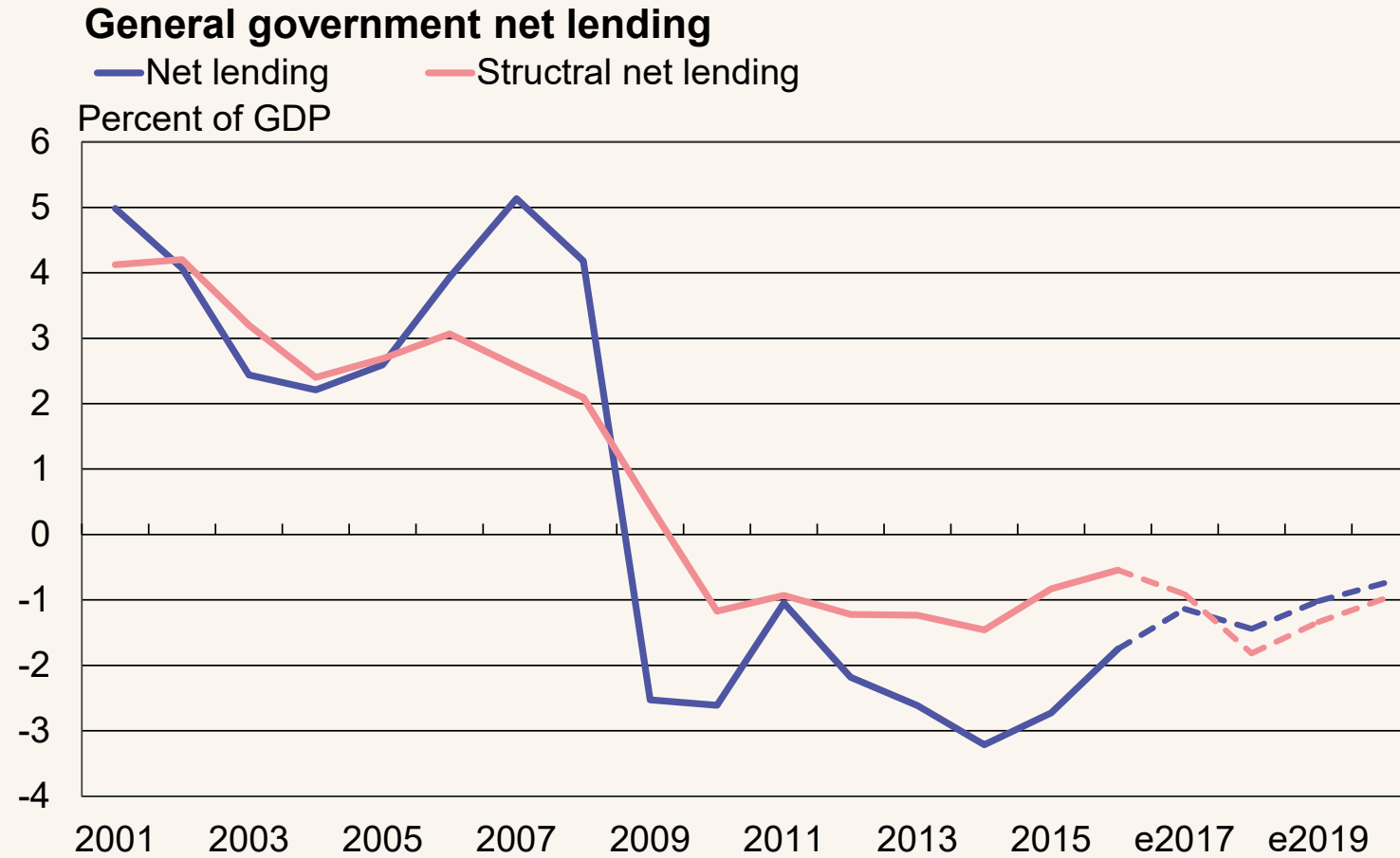


# Fiscal deficit has diminished, but sustainability is still not ensured





# Public finances remain in deficit



Sources: Statistics Finland, European Commission, and Bank of Finland (forecasts).

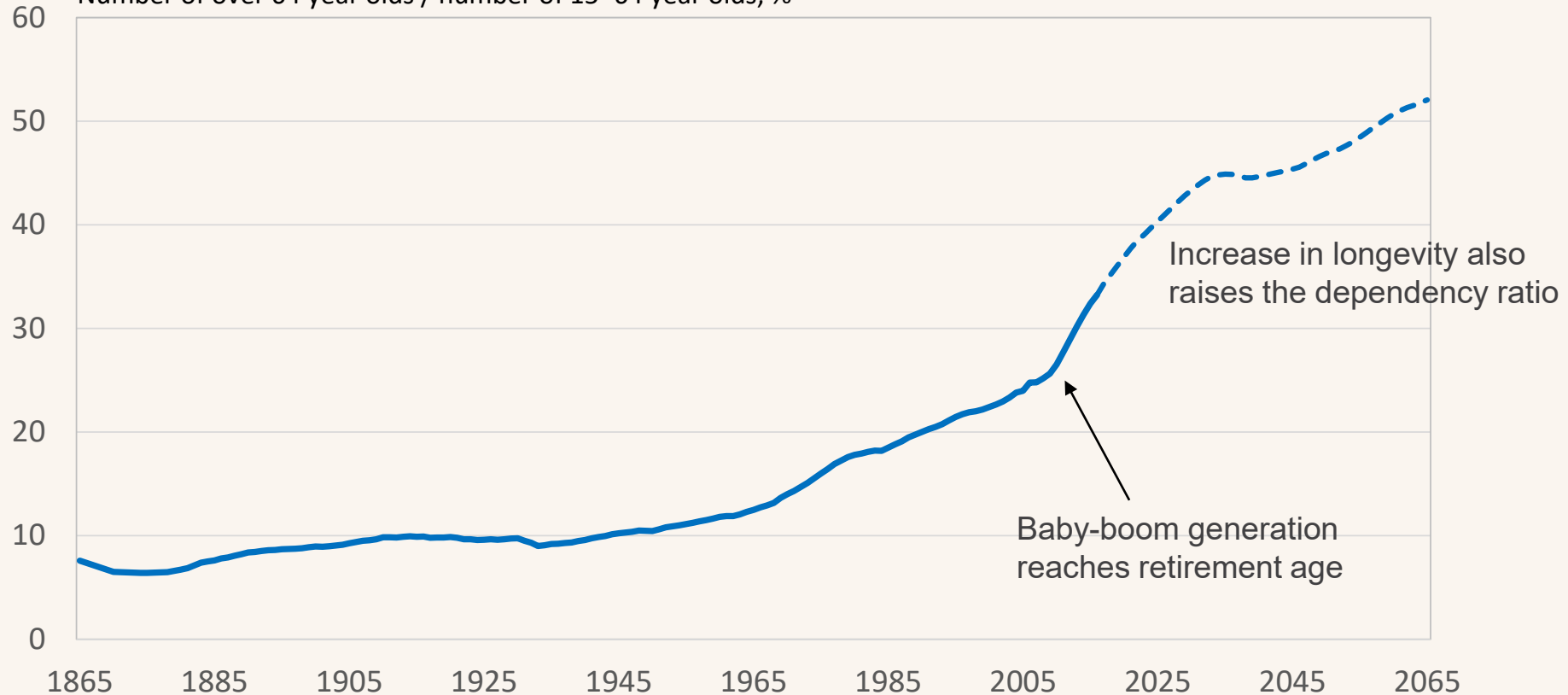
34003



# Fiscal sustainability gap still 3% of GDP, as the ratio of the elderly to working-age population grows

## Old-age dependency ratio

Number of over 64 year olds / number of 15–64 year olds, %



Source: Statistics Finland.

27747



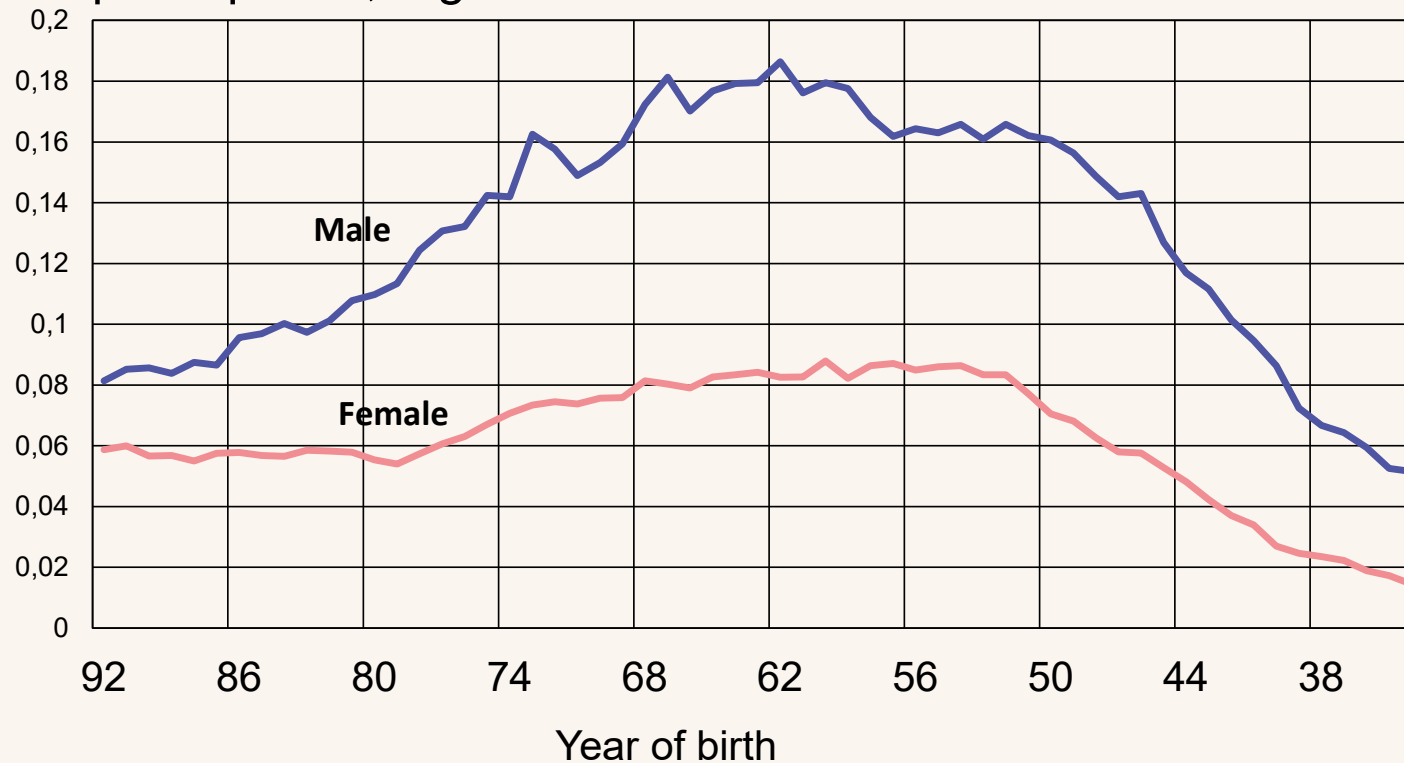
## Structural reforms can improve fiscal sustainability

- *Pension reform of 2015 improved fiscal sustainability*
- *Reform of social and health care services can significantly affect the outlook for public expenditure growth*
- *Raising the employment rate*
  - *Employment rate plays a central role in improving fiscal sustainability*



## Males born in the 1980s may have lower labour force participation than those born earlier

Estimated effect of year of birth on labour force participation, regression coefficient



Helvi Kinnunen and Petri Mäki-Fränti:  
"The influence of age, gender, and  
education on labour supply in Finland"  
(in Finnish).  
[www.eurojatalous.fi](http://www.eurojatalous.fi)

Sources: Statistics Finland and Bank of Finland calculations.

35437

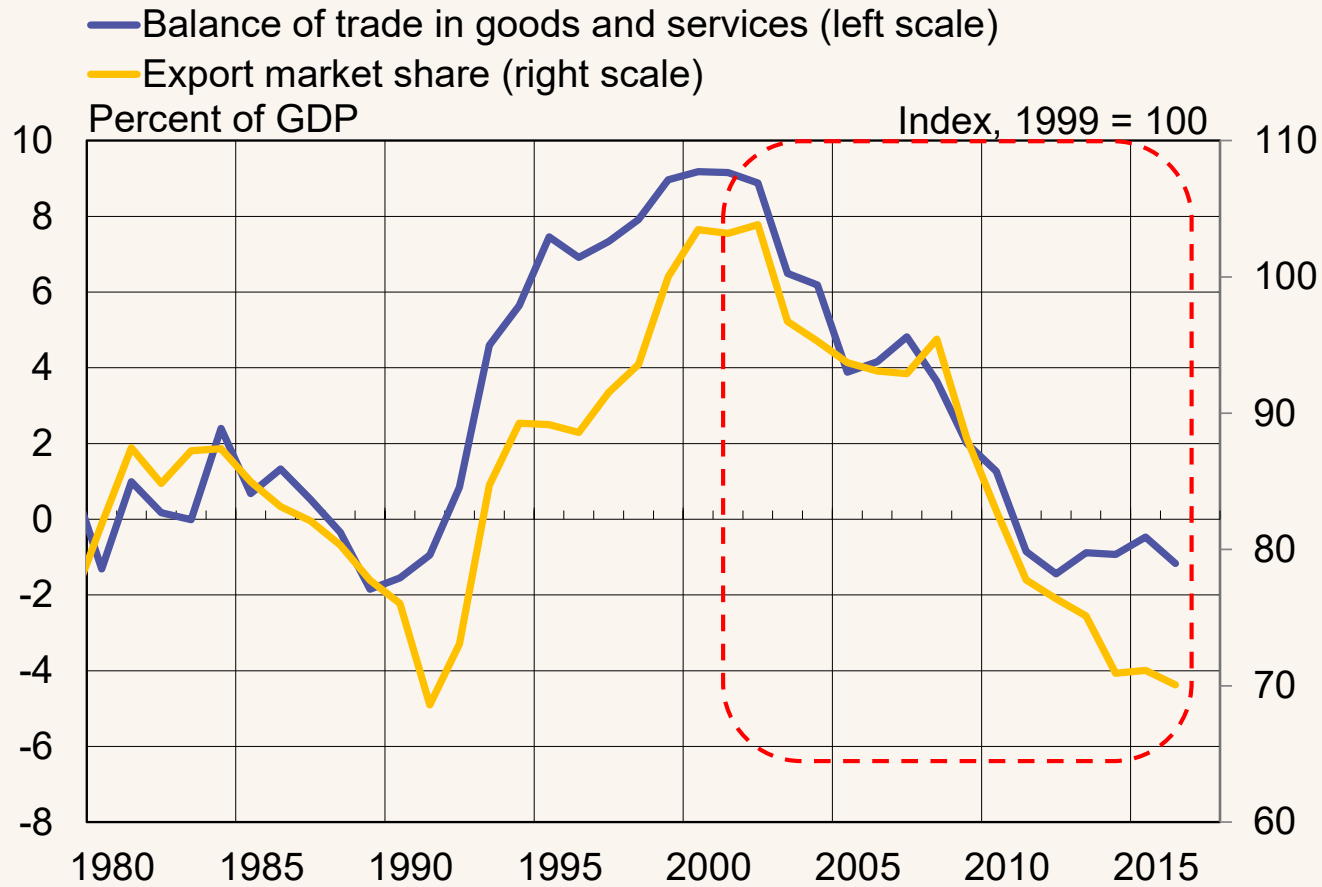


**Cost-competitiveness has taken a turn for the better**

**Agreements during the next few months and years will  
affect the outlook for growth and employment**



# Developments in the open sector of the economy were subdued until 2016



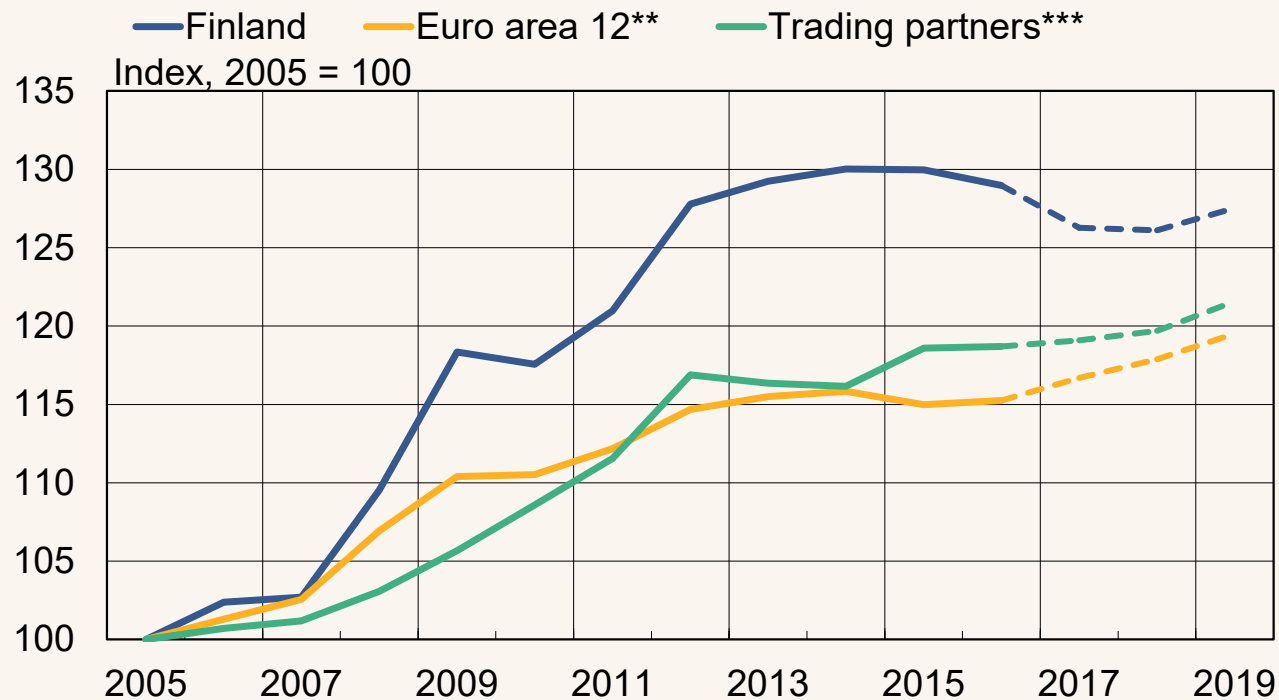
Sources: Statistics Finland, European Commission, and OECD.

34093



# Wage agreements for 2018 and 2019 have important effects

Unit labour costs adjusted for changes in terms of trade\*



\*) Labour compensation relative to real national income.

\*\*\*) First 12 euro area member states. \*\*\*) 14 traditional industrial countries.

Forecasts: Bank of Finland (Finland) and European Commission (other countries).

Sources: Statistics Finland, Bank of Finland and European Commission.

34093



# Economics provides knowledge of means, not ends





## Knowledge derived from research can be utilised when planning structural and cyclical policies

- ***Broad goals for society rest in part on value judgements. Decisions made by elected officials***
- ***Economic research can help us***
  - ***know how to reach goals set for society with maximal efficiency and minimal costs***
  - ***understand past developments in the economy and analyse current problems***
- ***An important plan to found a new economics institute in Finland***



## Jean Tirole: “Economics for the Common Good”

- *Jean Tirole was awarded the Nobel price in economics in 2014*
- *Tirole told he had to reply to questions such as: What is economics, and how can it improve welfare? His reflections resulted in a book (2016, 2017)*
- *Tirole describes areas where economics has created tools that can be used to solve common problems*
  - *What are the weights of the state and the market? What is the role of independent institutions? What are the most effective tools in the battle against climate change? What kind of incentives can support reaching common goals, and when can they turn against them? Inequality: how to measure it, analyse reasons for it, and propose ways to deal with it?*
- *Tirole also writes about restrictions in the role of a research economist*
  - *The media is not a natural place for a researcher. Their perceived uncertainty supports their interest in making research. Arguments in favour and against, “two-handed economist”.*
  - *Unfortunately, reseachers sometimes present in public such arguments that they would never dare to defend in a scientific seminar, or would correct them soon.*



## Conclusions

- ***Near-term outlook brighter than last summer***
- ***Now essential to improve the longer-term outlook for growth and public finances***
  - *Raising the employment rate*
  - *Improving the conditions for productivity growth*
- ***Important that the young are able to enter the labour market***



**Thank you!**