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Subject:	Recommendation for a COUNCIL RECOMMENDATION on the 2016 national reform programme of Finland and delivering a Council opinion on the 2016 stability programme of Finland

Delegations will find attached the above mentioned draft Council Recommendation, as revised and agreed by various Council committees, based on the Commission proposal COM(2016) 346 final.

COUNCIL RECOMMENDATION

of…

on the 2016 National Reform Programme of Finland

and delivering a Council opinion on the 2016 Stability Programme of Finland

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Articles 121(2) and 148(4) thereof,

Having regard to Council Regulation (EC) No 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies[1], and in particular Article 5(2) thereof,

Having regard to Regulation (EU) No 1176/2011 of the European Parliament and of the Council of 16 November 2011 on the prevention and correction of macroeconomic imbalances[2], and in particular Article 6(1) thereof,

Having regard to the recommendation of the European Commission,

Having regard to the resolutions of the European Parliament,

Having regard to the conclusions of the European Council,

Having regard to the opinion of the Employment Committee,

Having regard to the opinion of the Economic and Financial Committee,

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1 OJ L 209, 2.8.1997, p. 1.
2 OJ L 306, 23.11.2011, p. 25.

Having regard to the opinion of the Social Protection Committee,

Having regard to the opinion of the Economic Policy Committee,

Whereas:

(1) On 26 November 2015, the Commission adopted the Annual Growth Survey, marking the start of the 2016 European Semester for economic policy coordination. The priorities of the Annual Growth Survey were endorsed by the European Council on 17-18 March 2016. On 26 November 2015, on the basis of Regulation (EU) No 1176/2011, the Commission adopted the Alert Mechanism Report, in which it identified Finland as one of the Member States for which an in-depth review would be carried out. On the same day, the Commission also adopted a recommendation for a Council Recommendation on the economic policy of the euro area. This Recommendation was endorsed by the European Council on 18-19 February 2016 and adopted by the Council on 8 March 2016[3]. As a country whose currency is the euro and in view of the close interlinkages among the economies in the economic and monetary union, Finland should ensure the full and timely implementation of the Recommendation.

(2) The 2016 country report for Finland was published on 26 February 2016. It assessed Finland's progress in addressing the country-specific recommendations adopted by the Council on 14 July 2015, and Finland's progress towards its national Europe 2020 targets. It also included the in-depth review under Article 5 of Regulation (EU) No 1176/2011. On 8 March 2016, the Commission presented the results of the in-depth review. The Commission's analysis led it to conclude that Finland is experiencing macroeconomic imbalances. In particular, it is essential to tackle the loss of cost-competitiveness accumulated over several years, which is mainly due to wage growth having exceeded that of productivity for a protracted period, leading to a sharp deterioration in the current account between 2008 and 2012. The analysis also pointed to significant medium- and long-term risks to the sustainability of already strained public finances.

[3] OJ C 96, 11.3.2016, p. 1

(3) On 14 April 2016, Finland submitted its 2016 National Reform Programme and its 2016 Stability Programme. In order to take account of their interlinkages, the two programmes have been assessed at the same time.

(4) Relevant country-specific recommendations have been addressed in the programming of the European Structural and Investment Funds for the 2014-2020 period. As foreseen in Article 23 of Regulation (EU) No 1303/2013 of the European Parliament and of the Council[4], where it is necessary to support the implementation of relevant Council recommendations, the Commission may request a Member State to review and propose amendments to its Partnership Agreement and relevant programmes. The Commission has provided further details on how it would make use of this provision in guidelines on the application of the measures linking the effectiveness of the European Structural and Investment Funds to sound economic governance.

(5) The 2016 Stability Programme indicates that the budgetary impact of the exceptional inflow of refugees is significant and provides adequate evidence of the scope and nature of these additional budgetary costs. According to the Commission, the eligible additional expenditure amounted to 0,05 % of GDP in 2015 and is currently estimated at 0,2 % of GDP in 2016. The provisions set out in Article 5(1) and Article 6(3) of Regulation (EC) No 1466/97 cater for this additional expenditure, in that the inflow of refugees is an exceptional event, its impact on Finland's public finances is significant and sustainability would not be compromised by allowing for a temporary deviation from the adjustment path towards the medium-term budgetary objective. Therefore, the required adjustment towards the medium-term budgetary objective for 2015 has been reduced to take into account these costs. Regarding 2016, a final assessment, including on the eligible amounts, will be made in spring 2017 on the basis of observed data as provided by Finland's authorities.

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[4] Regulation (EU) No 1303/2013 of the European Parliament and of the Council of 17 December 2013 laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund and laying down general provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund and the European Maritime and Fisheries Fund and repealing Council Regulation (EC) No 1083/2006 (OJ L 347, 20.12.2013, p. 320).

(6) Finland is currently in the preventive arm of the Stability and Growth Pact. On 18 May 2016, the Commission issued a report under Article 126(3) of the TFEU, as Finland's general government debt exceeded the 60 % of GDP reference value in 2015. The analysis concluded that the debt criterion should be considered as complied with. In its 2016 Stability Programme, the Government plans an improvement in the headline balance to -2.5% of GDP in 2016 and further to -1.3 % in 2020. The Government plans to reach its medium-term budgetary objective — a deficit of 0.5 % of GDP in structural terms – by 2019. According to the Stability Programme, the government debt-to-GDP ratio is expected to peak at 67.4% in 2019 and to decline to 67,2 % in 2020. The macroeconomic scenario underpinning these budgetary projections is plausible. The measures needed to reach the medium-term budgetary objective by 2019 have not been sufficiently specified. Based on the Commission 2016 spring forecast, there is a risk of some deviation from the recommended adjustment in 2016. The conclusion for 2016 would not change in case the budgetary impact of the exceptional inflow of refugees was excluded from the assessment. Under unchanged policies, there is a risk of a significant deviation from the recommended adjustment in 2017. The debt-to-GDP ratio is projected to continue its upward trend, reaching 66,9 % in 2017. Based on its assessment of the Stability Programme and taking into account the Commission 2016 spring forecast, the Council is of the opinion that there is a risk that Finland will not comply with the provisions of the Stability and Growth Pact. Therefore, further measures will be needed to ensure compliance in 2016 and 2017.

(7) Due to ageing of the population and a declining workforce, expenditure on pensions, health and long-term care is set to increase from 23,1 % in 2013 to 26,9 % of GDP by 2030. In January 2016, Finland enacted a pension reform that will link the statutory retirement age to changes in life expectancy as of 2027. Social and healthcare services, provided by the municipalities, amount to 10 % of GDP. Without reform of the system, that expenditure is forecast to grow by 2,4 % annually in nominal terms and increase as a share of GDP. The main outline of a far-reaching administrative reform and restructuring of healthcare and social services has been agreed. The reform's main aims include the reduction of the sustainability gap in the long run by EUR 3 billion through better control of the costs. This will be achieved through integration of services, larger arrangers of services and digitalisation. All of the details still need to be worked out and change management plans put in place before the reform can be implemented from 2019 as planned. The Government has announced that measures to implement the reform will be presented at the end of 2016. The magnitude and tight timetable of the reform mean that implementation will be a challenge. Timely adoption of the legislative proposals is therefore important.

(8) To restore Finland's competitiveness, the functioning of the labour market must be improved in several ways. On an aggregate level, wage increases have been moderate since the centrally agreed wage deal was agreed in late 2013. Under the agreement, the year-on-year increase in negotiated wages slowed from 1,3 % in the last quarter of 2013 to 0,5 % in the fourth quarter of 2015. In June 2015, the social partners decided to extend the agreement into 2016. However, labour productivity growth has not yet recovered and therefore nominal unit labour costs are forecast to increase, albeit more slowly. Negotiations have been carried out to restore cost-competitiveness. A Competitiveness Pact was agreed between social partners on 29 February 2016. The agreement needs to be translated into sectoral agreements before it can be implemented. The Competitiveness Pact will be complemented with measures agreed between social partners to ensure more labour market flexibility and a new model for wage growth by anchoring wages of other sectors to those facing external competition. It is important to implement the labour market measures in a way that fully respects the role of social partners.

(9) Due to declining size of the working age population, improving the labour market participation rate is important. This requires continued efforts to integrate older workers, young people, the long-term unemployed and the low-skilled into the labour market. The employment rate has decreased by more than two percentage points, from a pre-crisis peak of 70,6 % in 2008 to 68,5 % in 2015, while unemployment has increased from 6,4 % to 9,4 %. The employment rate of the elderly has been gradually improving, but some early exit pathways remain in the form of extended unemployment benefits for older workers until retirement (the 'unemployment tunnel') which, if not reduced, could limit the positive impact of the pension reform enacted in 2016. The effects of the changes to the parameters of the unemployment tunnel in the previous pension reform will be assessed in 2019. Long-term unemployment increased considerably between 2008 and 2014 from 1,2 % to 1,9 % of the total labour force, despite many of the long term unemployed eventually moving out of the labour force. Youth unemployment increased to 22,4 % in 2015. The low-skilled are affected most by the poor performance of the labour market. Cutting the budget for active labour market policies at a time when there is an increasing demand for such measures could harm opportunities for the above-mentioned groups to return to work. In terms of activation, the complex benefits system with its different types of allowances can result in significant inactivity and low wage traps. Addressing these traps and introducing positive incentives to accept work, such as improving the possibility to combine work and benefits, is particularly important in view of the cuts to the budget for active labour market policies. The arrival of a comparatively large number of migrants and refugees in Finland in 2015 could serve to counter the effects of population ageing, but only if they are successfully integrated into the labour market and the education system. There are matching problems in the labour market, partly due to the structural change in the economy, as new jobs are created in geographical areas and industries other than those where jobs have been lost. Measures that increase affordable housing in the Helsinki area and effective policies to help people update their skills and find work are needed.

(10) The business environment in Finland is as good as or better than in other advanced economies. However, lack of competition, in particular in services aimed primarily at the domestic market, such as retail and transport services, affects the overall competitiveness of the Finnish economy. Businesses have identified excessive regulatory requirements as obstacles to entry to and growth in some markets. These excessive requirements need to be addressed to promote entrepreneurship and investment. In the retail sector, the reform of planning regulations will set more flexible rules on the size and location of stores. The tradable sector continues to restructure and would benefit from developing new markets, products and services, particularly those with high value added. Structural change could be facilitated by policies supporting company expansion, internationalisation and innovation. Legislative amendments were passed in autumn 2015, but most are expected to be implemented only between 2016 and 2018. The Government has announced that further structural reforms will be made to increase market competition.

(11) In the context of the European Semester, the Commission has carried out a comprehensive analysis of Finland's economic policy and published it in the 2016 country report. It has also assessed the Stability Programme and the National Reform Programme and the follow-up given to the recommendations addressed to Finland in previous years. It has taken into account not only their relevance for sustainable fiscal and socio-economic policy in Finland but also their compliance with EU rules and guidance, given the need to strengthen the EU's overall economic governance by providing EU-level input into future national decisions. The recommendations under the European Semester are reflected in recommendations (1) to (3) below.

(12) In the light of this assessment, the Council has examined the Stability Programme, and its opinion[5] is reflected in particular in recommendation (1) below.

(13) In the light of the Commission's in-depth review and this assessment, the Council has examined the National Reform Programme and the Stability Programme. Its recommendations under Article 6 of Regulation (EU) No 1176/2011 are reflected in recommendations (2) and (3) below,

[5] Under Article 5(2) of Regulation (EC) No 1466/97.

HEREBY RECOMMENDS that Finland take action in 2016 and 2017 to:

1. Achieve an annual fiscal adjustment of at least 0.5 % of GDP towards the medium-term budgetary objective in 2016 and 0.6 % in 2017. Use any windfall gains to accelerate the reduction of the general government debt ratio. Ensure timely adoption and implementation of the administrative reform with a view to better cost-effectiveness of social and healthcare services.

2. While respecting the role of social partners, ensure that the wage setting system enhances local wage bargaining and removes rigidities, contributing to competitiveness and a more export industry-led approach. Increase incentives to accept work and ensure targeted and sufficient active labour market measures, including for people with a migrant background. Take measures to reduce regional and skills mismatches.

3. Continue pursuing efforts to increase competition in services, including in retail. Promote entrepreneurship and investment, including by reducing administrative and regulatory burden, to foster growth of high value added production.

Done at Brussels,

For the Council
The President