## 3.2 Finland

### 3.2.1 Setting the scene: key traits of the country's political economy

Finland has been hard hit by the economic and financial crisis. Being an open, export-oriented economy, the worldwide recession and the collapse in trade entailed a huge decline in manufacturing exports. This situation has been further aggravated by more structural problems confronting key sectors such as electronics (notably Nokia) and forestry (Dølvik *et al*. 2014; Hopia and Metelinen 2013). Looking at GDP growth, the country has experienced a 'double dip': the recession in 2009 (–8.3 per cent of GDP) was followed first by a recovery in 2010, then by a second drop from 2012. According to a recent forecast (European Commission 2015c) the Finnish economy is expected to recover slowly from 2015. Both the general government gross debt and deficit were affected by the economic downturn. The debt almost doubled – from 32.7 per cent of GDP in 2007 to 59.3 per cent in 2014 – thus approaching the 60 per cent Maastricht threshold, and the country's budget moved from being in surplus in 2008 (4.2 per cent of GDP) to a persistent deficit in the following years (with a low-point of –3.2 per cent of GDP in 2014).

Social indicators, too – though less dramatically than in other EU countries – have deteriorated over the crisis years. The employment rate registered a decrease in 2009 (73.5 per cent, compared with 75.8 per cent in 2008) and then remained quite stable in the following years (Table 7). Similarly, the unemployment rate increased by about 2 percentage points between 2008 (6.4 per cent) and 2009 (8.2 per cent), then remaining fairly flat until 2014 (8.4 per cent). However, while the Finnish unemployment rate is still below the EU average, the 0.5 percentage points increase between 2013 and 2014 is particularly worrisome insofar as it represents the biggest increase in the EU over that period (Europe-

Table 7 **Finland: selected socio-economic indicators, 2007–2014**

| Indicators/years | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 |
|---|---|---|---|---|---|---|---|---|
| Real GDP growth | 5.2 | 0.7 | −8.3 | 3.0 | 2.6 | −1.4 | −1.3 | −0.1 |
| General government gross debt (EDP concept) (% of GDP) | 34.0 | 32.7 | 41.7 | 47.1 | 48.5 | 52.9 | 55.8 | 59.3 |
| General government deficit/surplus (% of GDP) | 5.1 | 4.2 | −2.5 | −2.6 | −1.0 | −2.1 | −2.5 | −3.2 |
| Employment rate (% 20-64) | 74.8 | 75.8 | 73.5 | 73.0 | 73.8 | 74.0 | 73.3 | 73.1 |
| Unemployment rate (%) | 6.9 | 6.4 | 8.2 | 8.4 | 7.8 | 7.7 | 8.2 | 8.7 |
| People at risk of poverty or social exclusion (% of total population) | 17.4 | 17.4 | 16.9 | 16.9 | 17.9 | 17.2 | 16.0 | 17.3 |

Source: Annex to Agostini and Natali (forthcoming).

an Commission 2015c: 46). The rate of people at risk of poverty or social xclusion remained fairly stable (around 17 per cent) over the crisis years and even declined slightly in some years.

Finland displays the key traits of 'national-coordinated market economies' (NCME), characterised by a comprehensive industrial relations system with a high-level of social partner density and a key coordination role played by national-level wage bargaining (Agostini and Natali forthcoming) (Table 8).

Table 8 **The Finnish social model**

| Labour market regime | Welfare regime | Varieties of capitalism |
|---|---|---|
| Nordic | Social democratic | National-coordinated market economy (NCME) |
| | | Peculiarities:<br>- Member of the euro zone since 1999 |

Source: Authors' elaboration of Agostini and Natali (forthcoming).

The presence of strong, centralised worker and employer organisations, the development of institutions facilitating tripartite cooperation and the emergence of stable party constellations or hegemonic parties are in fact strongly characteristic of Nordic countries (Dølvik *et al.* 2015: 20). Because their economies are highly reliant on international trade, collective agreements have been fundamental to enhancing export competitiveness by allowing for wage flexibility, technological change and investment (Vartiainen 2011b). In Finland, the role of the state in supporting centralised pay setting has been even more accentuated than in other Nordic countries: indeed, through the so-called 'incomes policy' developed since the 1950s, Finnish governments have facilitated wage bargains by linking these to economic policies and social reforms (ibid.). Looking more specifically at social policy, Finland can be included among the 'social democratic' welfare regimes, typically characterised by a comprehensive welfare state granting universal rights to income security and education, a high level of decommodification, high social spending and extensive provision of public services (Dølvik *et al.* 2014; Agostini and Natali forthcoming). The Finnish pension system is rather unusual by international standards, given the specific features of the employment pension[13] (which, together with the national pension, until 2011 represented one of the two schemes of the first pillar) and the fundamental decision-making role given to the social partners (Kautto forthcoming). In terms of labour market regime, Finland is part of the 'Nordic' cluster, characterised by a certain degree of internal flexibility and a relatively low degree of external flexibility, coupled with fairly generous unemployment benefits and high expenditure on ALMP (Sturn 2011). Legislation on collective dismissal associated with economic downturns has traditionally been flexible, while provisions on individual terminations are stricter (with the exception of Denmark) (Dølvik *et al.* 2015: 68).

Many observers describe the economic crisis that hit the Nordic countries at the beginning of the 1990s as a critical juncture that significantly shaped their socio-economic models (Dølvik *et al.* 2014; Dølvik *et al.* 2015; Jochem 2011): it was a sort of 'existential crisis' that called into question the viability of the Nordic social model (Dølvik *et al.* 2014: 249). Confronted with such economic turmoil, the Nordic countries re-

**13.** The employment pension can be described as a 'functional hybrid' incorporating many features that, in other countries, are generally attached to second pillar schemes (Kautto, forthcoming).

acted with a series of reforms of macroeconomic and fiscal policies, the financial sector, wage setting arrangements and labour market regulation (Dølvik *et al.* 2014).[14] In Finland (a member of the EU since 1995), the wage moderation and fiscal consolidation efforts pursued over the 1990s were also linked to the need to meet the Maastricht criteria, given the decision to join EMU among the first participants (Vartiainen 2011a). Although most social benefits were either cut or not adequately raised compared with living costs or wage developments (Jutila 2011), reforms undertaken over the 1990s and 2000s did not result in the dismantling of the traditional social model but rather in its 'consolidation' (Dølvik *et al.* 2014).[15] In particular, social and tax policies were reoriented towards labour supply, the education and skills formation systems were expanded, and social benefits were made more conditional and linked more closely to the 'activation' of the recipients. Moreover, public services were reinforced, more emphasis was put on programmes for the reconciliation of work and family life and a series of pension reforms were implemented (Dølvik *et al.* 2014; Dølvik *et al.* 2015). Finland, along with the other Nordic countries, introduced or reinforced many elements of what is currently labelled the 'social investment' approach.

Summing up, on the eve of the Great Recession Finland was characterised by good socio-economic conditions, with relatively high rates of GDP growth, a sound budgetary situation, a robust financial sector, comparatively good labour market performance and a fairly comprehensive and effective welfare state. That said, especially due to rapid population ageing and the shrinking working age population, doubts about the long-term sustainability of the Finnish welfare system persisted and were an important theme already in the pre-crisis public debate (Vartiainen 2011a). In particular, the sustainability of the pension and health-care systems were a matter of concern. Furthermore, the centralised wage setting system – which had played a pivotal role in the socio-economic development of the country – was seriously called into question in 2007, when employers refused to take part in nationally coordinated wage settlements (Vartiainen 2011a, 2011b).

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**14.** These measures were accompanied by huge currency depreciations in Finland and Sweden (ibid.: 264).

**15.** For more critical accounts, see Blomgren *et al.* (2012) and Jutila (2011). While stressing that the Finnish welfare state is still enviably effective, Blomgren *et al.* (2012) identify cuts/slow increase in social benefits and in tax rates (the latter since the 2000s) as key determinants of the rise in income inequality over the past twenty years. Jutila (2011) concludes that these changes have entailed a gradual but continuous retrenchment of the Finnish

Table 9 **Finnish governments, 2007–present**

| Years | Prime Minister | Position in the political spectrum | Coalition forces | Reform programme |
|---|---|---|---|---|
| 2007–2010 | Matti Vanhanen (II) | Centre-right | - Centre Party<br>- National Coalition Party<br>- Swedish People's Party<br>- Green League | Social standards improvement (2009–2010) |
| 2010–2011 | Mari Kiviniemi | Centre-right | - Centre Party<br>- National Coalition Party<br>- Swedish People's Party<br>- Green League | Social standards improvement (based on PM Vanhanen's government programme) |
| 2011–2014 | Jyrki Katainen | Grand coalition | - National Coalition Party<br>- Social Democratic Party<br>- Left Alliance<br>- Green League<br>- Swedish People's Party of Finland<br>- Christian Democrats | Social standards devaluation |
| 2014–2015 | Alexander Stubb | Grand coalition | - National Coalition Party<br>- Social Democratic Party<br>- Green League (until September 2014)<br>- Swedish People's Party<br>- Christian Democrats | Social standards devaluation (based on PM Katainen's government programme)<br>Some selective investment |
| 29 May 2015–present | Juha Sipilä | Centre-right | - Centre Party<br>- Finns Party<br>- National Coalition Party | Social standards devaluation (some selective investment) |

Source: Hopia H. and Metelinen S. (2013); Jokivuori P. (2011); Prime Minister's Office (2015).

The development of the crisis in the EU significantly influenced Finnish politics in terms of coalition composition, reform programmes and stability. Since 2007, five coalition governments have taken office in Finland as a result of the parliamentary elections held in 2007, 2011 and 2015 (Table 9).[16] With regard to the reform pattern of the crisis years,

**16.** The Kiviniemi and Stubb governments were both in office for one year and were formed because of the resignations of the Prime Ministers Vanhanen (for personal reasons) and Katainen (who joined the Juncker cabinet as Commissioner for Jobs, Growth, Investment and Competitiveness). These governments followed the path taken by previous cabinets, as the structure of the coalition remained more or less unchanged.

two broad trends can be identified. At the beginning of the crisis, Finnish governments supplemented the work of the automatic stabilisers by expansionary policy packages (social standards improvement). However, after a stimulus package of approximately 1 per cent of GDP implemented in 2009 by the Vanhanen government (Jochem 2011: 141), more restrictive budget choices were gradually implemented (Dølvik *et al.* 2015: 36). A clear trend reversal is visible after the 2011 parliamentary elections, marked by the historic success of the populist True Finns Party (nowadays the Finns Party) and the sharp decline in popularity of the Centre Party (Hopia and Metelinen 2013: 165). Indeed, fiscal consolidation was a priority for the coalition government formed by Prime Minister Katainen (in which the True Finns Party decided not to take part despite the election results). The common trend towards social standard devaluation in the EU and the increasing pressure from the European Union in this direction might have played a role in shaping the reform pattern towards fiscal consolidation. However, given the industry-specific shocks experienced and the stagnating labour force, the Grand Coalition government would probably have managed to implement such a programme even without pressure from European institutions in this regard (Dølvik *et al.* 2014: 271). A similar focus on the sustainability of public finances characterises the Strategic Programme of Prime Minister Juha Sipilä, which combines this priority with a clear will to implement structural reforms promoting employment, entrepreneurship and economic growth (Prime Minister's Office 2015: 10).

When it comes to 'EU pressure' coming from the European Semester, messages recommending Finland to continue its fiscal consolidation efforts and preserve a sound fiscal position have been a constant of CSRs received between 2011 and 2015. In 2010, an Excessive Deficit Procedure was launched, based on the expectation that – in 2011 – the public deficit would have exceeded 3 per cent of the GDP. Since the forecast proved to be wrong, the EDP was closed in 2011. Growing concerns about the trend of the public budget emerge, in particular, from the CSRs for 2014 and 2015. Other CSRs received by Finland between 2011 and 2015 concerned a number of sectors covered by the present research, including pensions, the labour market and the public administration.

## 3.2.2 Structural reforms sector by sector

**Pensions**
Confronted with a rapidly ageing population, the Finnish pension system has been reformed several times over the past 20 years. Reforms undertaken in the 1990s and the 2000s especially concerned the 'first pillar' of the system, with a view to ensuring both its sustainability and its adequacy (Kautto forthcoming). Raising the effective retirement age was a key goal of these reforms but, despite remarkable improvements, the progress achieved before the crisis was insufficient (Natali and Stamati 2013). Furthermore, the crisis has uncovered some shortcomings related to poverty protection, insofar as Finland's rate of people aged 65 or more at risk of poverty is higher than the EU average (ibid.).

Changes made over the crisis years have been characterised by continuity with the previous reform pattern. Most of them concerned the first pillar of the pension system and consisted of a mix of interventions aimed at reinforcing financial sustainability by promoting longer working careers and more expansive measures (Kautto forthcoming; Natali and Stamati 2013). In spring 2009, the social partners and the government agreed to discuss measures aimed at achieving a three-year increase in the effective pension age by 2025. However, due to trade union opposition, no agreement was reached on the government proposal to gradually raise the minimum retirement age by two years (Vartiainen 2011a). In the same year, taxes on pension income were lowered and the government intervened to prevent benefit indexation from turning negative in 2010 (Natali and Stamati 2013).[17] Furthermore, employer contributions to the Social Insurance Institution (responsible for the national pension) were gradually eliminated from 2010, while employee and employer contributions to the TyEL fund (for private employees) were raised by 0.4 percentage points a year between 2011 and 2014 (ibid.). In March 2011, the government introduced the 'guarantee pension', a scheme intended to top up the national pension for low-income pensioners and to cover people who do not qualify for the national pension due to insufficient years of residence (Kautto forthcoming). A further agreement concluded by the social partners in spring 2012 introduced additional measures such as the discontinuation of 'early old age retirement' (a scheme that

17. As reported by Natali and Zaidi (2015: 5), over the crisis years pension payments have been affected by the decision to decrease the indexation for both national and earnings-related benefits.

allowed retirement at the age of 62) from 2014, a one-year increase in the age limits to qualify for part-time pensions and the unemployment benefit system (from 60 to 61), and a 0.4 percentage point increase in contributions in 2014 and 2015 (ibid.).

An agreement on the new reform was reached by the social partners in autumn 2014 and was due to be discussed by Parliament in autumn 2015 with a view to entering into force in 2017. Among the main changes agreed are (Ministry of Finance 2015: 18–19): a two-year rise in the retirement age, abolition of the part-time pension (to be replaced by a ‘partial early old-age pension’) and the introduction of a new pension benefit (the ‘years-of-service pension’). The minimum age of eligibility for the old age pension will gradually increase until it reaches 65 years in 2025 and, from 2027, it will be linked to life expectancy. The new ‘partial early old-age pension’ will initially concern individuals aged 61. Then, by 2025, the minimum age for this benefit will be raised to 62 and, from 2027, it will be linked to life expectancy. Finally, the newly introduced ‘years-of-service pension’ will apply to individuals aged at least 63 (from 2027 the age limit will be linked to life expectancy) with a working career spanning at least 38 years in work that is either physically or mentally wearing, and with an impaired work capacity.

Overall, looking at pension reforms implemented in Finland over the crisis years, we can identify two sub-periods. At the beginning of the crisis, some expansive measures were enacted, especially aimed at ensuring the adequacy of pensions. Since late 2011, however, initiatives aimed at ensuring the financial sustainability of the system (notably, by extending working life) have prevailed. Generally speaking, these measures go in the direction suggested by the CSRs on pension policy addressed to Finland since 2011, which have repeatedly pointed to the need to increase the retirement age and to reduce early exits from work. That said, considering the remarkable degree of continuity between changes undertaken over the crisis years and the pre-crisis reform pattern (Kautto forthcoming), the impact of pressure coming from the European Semester should not be overestimated. Indeed, the latter seems to have simply been an additional stimulus to implement decisions already taken at the national level.

**Labour market**

After the employers’ decision to withdraw from nationally coordinated wage setting (in 2007), social partner negotiations took place at the sectoral level. However, already in 2011 there was a return to centralised wage bargaining and, in 2013, a traditional incomes policy settlement was concluded. The latter foresaw a very modest pay increase for the period 2014–2015[18] and was facilitated by the government, which linked inflation adjustments of income taxation to the success of the negotiations (Dølvik *et al*. 2014: 278). Though centralised wage agreements concluded over the crisis years did not include either wage freezes or wage cuts, such decisions were in many cases taken in the firms hardest hit by the crisis (Dølvik *et al*. 2014; Svalund *et al*. 2013). Local-level flexibility was important for coping with the crisis and to avoid, whenever possible, dismissals: a number of firms made extensive use of such solutions as flexible working time, internal redeployment and temporary lay-offs. The latter option was facilitated by the government which, in 2009, relaxed the access requirements for these schemes and extended to workers temporarily laid off the 'change security' activation programme, thus offering further retraining opportunities (Svalund *et al*. 2013).

The rate of unemployment benefits remained unchanged over the crisis years, although the duration of earnings-related unemployment insurance benefits was marginally reduced for some groups (Dølvik *et al*. 2014: 278). Conversely, at the beginning of the crisis replacement rates were raised moderately (OECD, 2012) and access criteria were eased in 2009 and 2010 (Svalund *et al*. 2013: 188). However, the conditionality attached to the benefits (notably, activation requirements) was tightened and sanctions for non-compliance were made more stringent.[19] Furthermore, in order to push municipalities to take more responsibilities towards the long-term unemployed, financing criteria for both the basic unemployment allowance and labour market subsidies were modified, introducing an earlier and more substantial participation of the municipalities in the co-financing of these schemes (Kangas and Kalliomaa-Puham 2015: 16).

Especially since 2013, the provision of ALMP has been extended (Dølvik *et al*. 2014; Jochem 2011), with a focus on specific target groups, such as the long-term unemployed, people with reduced work capacity, elderly workers and unemployed young people. Measures implemented since 2013 include (European Commission 2015c; Ministry of Finance 2015):

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**18.** 'Promoting wage development in line with productivity' was among the CSRs addressed to Finland under the European Semester.

**19.** In particular, legal requirements for the geographical and occupational mobility of the unemployed were tightened.

(i) the introduction of an income disregard (up to 300 euros) on earnings-related incomes for the beneficiaries of the labour market subsidy; (ii) a reorganisation of the wage subsidies system introducing subsidies for long-term unemployed, elderly workers and workers with disabilities (effective since 2015); and (iii) provisions targeted at young people, implemented mainly within the framework of the 'Youth Guarantee'. As for the latter, measures already existing since 1996 were amended in 2013 with a view to strengthening and better integrating the two components of the model (employment and education), broadening the target group, enhancing measures for reaching the most vulnerable (through vocational, medical and social rehabilitation services) and renewing financial investments (Ministry of Employment and the Economy n.d.).

Other changes concerned the governance of labour market policies, with a view to enhancing the coordination between the various measures and the actors involved and improving the provision of individualised assistance (especially for categories such as the long-term unemployed and young people). In 2013, in order to improve their efficiency and their capacity to offer customised services, the Public Employment Services were reformed: the 74 local Employment and Economic Development offices were merged into 15 regional offices (OECD 2014a).[20] The 'Act on multi-sectoral services cooperation' (2014) aims at facilitating the development of one-stop-shop arrangements by obliging the Social Insurance Institution (KELA), municipalities and public employment services to draft, in collaboration with the job seeker, multi-sectoral plans for employment (Kangas and Kalliomaa-Puha 2015: 16).

Overall, looking at labour market policy, one can conclude that measures adopted over the crisis years have further reinforced the 'social investment orientation' of the Finnish model. Most of these changes were in line with recommendations coming at EU level, emphasising the need to target labour market measures at the long-term unemployed, young people and older workers.

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**20.** As reported by the Finnish Ministry of Finance (2015: 17), since 2014 the Employment and Economic Development Centres have significantly increased job offers made to the unemployed, and employment plan monitoring and job-seeker reporting have been enhanced through the development of an electronic service. Probably, the reform of the PES also has budget saving objectives and, as reported by the European Commission (2015c: 48), the budget of the public employment services has indeed been cut.

**Education**
The Finnish education system has traditionally been highly effective by international standards. Public spending on education is higher than the EU average and general government expenditure on education as a percentage of GDP remained fairly stable in the first years of the crisis (European Commission 2014b: 3). Nevertheless, from 2011 several fiscal consolidation measures were introduced. Data on year-on-year changes in constant prices (Agostini and Natali forthcoming: Appendix) show that real government expenditure decreased both in 2011 and 2012. Additionally, the 'Structural Policy Programme' adopted in 2013 foresaw a further reduction of approximately 280 million euros (5 per cent of the education budget) over the period 2014–2017 (European Commission 2015c: 50–51). According to the European Commission (ibid.: 51), these cuts risk having an impact on the quality of educational outcomes.

Over the crisis years, the Finnish education system has been subject to a number of reforms, which have concerned early childhood education and care, tertiary education, and vocational and educational training.

With regard to early childhood education and care, a first change concerned the governance of the system, responsibility for which was transferred, in 2013, from the Ministry of Social Affairs and Health to the Ministry of Education and Culture. Therefore, early childhood education and care is now an integral part of the education system. Second, in order to facilitate early interventions in learning difficulties and ensure that every child has access to high quality pre-primary education, irrespective of their social background (Ministry of Finance, 2015), a mandatory school year for children aged 6 was introduced in 2013. As pointed out by Kangas and Kalliomaa-Puha (2015), both these interventions have reinforced the social investment orientation of the Finnish early childhood education and care system, whose effectiveness may, however, be reduced by recent fiscal consolidation measures. The latter have indeed affected municipalities' budgets, leading to an increase in the child-to-staff ratio and in the average number of pupils in classrooms and to the cutting of some support measures for children with specific needs (ibid.).

Finland has traditionally been characterised by a high rate of participation of upper secondary students in vocational education and training and a relatively low level of participation in apprenticeship training (European Commission 2014b: 4). The provision of vocational education and training and apprenticeships for young people has recently been increased, especially since 2013, within the framework of the Youth Guarantee (Ministry of Finance 2015: 23–24). As for vocational education, the reform of the selection criteria in upper secondary education is expected to give priority to people without a post-basic education qualification, while the reform of the vocational education qualification – aimed at improving the skill-base and the flexibility of the system – will come into force in August 2015. In 2014, the system of on-the-job learning and apprenticeship training (targeted at people under 25 without a post-basic education qualification) was reformed in order to increase the availability of apprenticeship training placements and to promote the development of training models combining institutional training and apprenticeship. As for adults, in spring 2014 the government decided to allocate 20 million euros for 2014–2015 for programmes aimed at strengthening the skill-base of adults without basic or post-basic education qualifications.

As for tertiary education, a comprehensive 'university reform' aimed at improving both the effectiveness and the efficiency of the system was enacted in 2009. The objectives of the reform were to improve universities' capacity to react to changes in the operational environment, to diversify their funding base, to better compete for international research funding and to enhance international cooperation (Aarrevaara *et al.* 2009: 93). In order to do so, the reform enlarged the financial and administrative autonomy of the universities (transformed into independent legal entities taking the form of either public corporations or foundations under private law) and increased the incentives to search for private funding (ibid.: 94). In order to further rationalise the university system, the reform was accompanied by a proposal to merge some universities. A common goal of the reforms implemented since then has been the attempt to shorten the duration of studies in order to accelerate the transition to working life. Such an objective is apparent in the reform of both the funding model of universities (2013) and students' financial aid (2014). The 2013 revision increased the importance attached to the number of qualifications attained by students and their progress in their studies in determining the amount of funding for the universities (Ministry of Finance 2014). The new funding model was extended to universities of applied sciences in 2014. The reform of the students' financial aid came into force in 2014 and aimed at supporting full-time studies and accelerating the completion of studies (among other things by introducing an 'incentivising study loan compensation for the efficient completion of studies) (Ministry of Finance 2015: 35).

Overall, reforms undertaken over the crisis years aimed at improving the effectiveness and efficiency of the Finnish education and training system, from early childhood education and care to tertiary education. However, the education budget has been cut since 2011 within the framework of fiscal consolidation policies.

**Public sector**

Over the crisis years, the Finnish public sector did not experience major structural reforms. This is also true of the central public administration,[21] in which little change has occurred since 2008. Specifically, no pay cuts were introduced for employees in the sector, nor were changes in working time agreed or implemented (EurWORK 2014b). By contrast, tripartite negotiations in 2011 led to a pay increase of 4.3 per cent for 94 per cent of the Finnish workforce (ibid.: 18). This trend is confirmed when looking at the general government public expenditure on compensation of employees (as a percentage of GDP), which even increased in the aftermath of the crisis, from 12.9 per cent in 2008 to 14.3 per cent in 2009, and then remained fairly stable in the following years (Annex to Agostini and Natali forthcoming).

However, although the crisis did not worsen public workers' conditions, it is worth mentioning that a reduction of about 6,400 has been reported in the number of employees in 'public administration, defence and social security'[22] from 2008 (116,300) to 2013 (109,900) (ibid.). The substantial downsizing of the sector, however, followed a path already started in 2003 with the adoption of the Finnish State Productivity Programme (planned to end in 2015), which by 2011 had reduced the central public administration by 8,000 jobs with the aim of reducing costs and improving the efficiency of the system. The effectiveness of the programme itself has been questioned as it has been shown to have brought about little (or no) productivity gains (EurWORK 2011).

21. In this case, following Eurofound (2015: 2), we understand by public administration 'those central government departments or ministries that carry out planning, management and coordination functions rather than public-service delivery functions'. Therefore, the definition excludes all the other sectors providing services of general interest, such as education and health care.
22. The 'public administration, defence and social security' classification refers to the Statistical Classification of economic activity in the European Community (NACE), Rev. 2 (2008).

Nonetheless, although major restructuring was implemented in the pre-crisis years, new adjustments are under way, especially at local level, also because of EU pressure coming from the Country-Specific Recommendations addressed to Finland with regard to the public sector. The Local Government Structure Act, which entered into force in summer 2013, is aimed at achieving productivity gains and cost savings in the provision of public services (Ministry of Finance 2014: 17) by means of mergers of municipalities and reductions of their tasks. Consequently, the reform will have a strong impact on Finnish administrative structure, which expresses the constitutional value of self-government with a high degree of decentralisation and a large share of local government spending as a percentage of GDP (OECD 2014a). According to an estimate of the Finnish government, the reform – when fully implemented between 2015 and 2017 (indicatively) – will result in a reduction of 1 billion euros in operating expenditure for local authority duties and obligations. Additionally, the new local administrative structure aims to generate 1 billion euros in savings through measures implemented by local authorities, for instance by improving productivity and through tax revenues (Ministry of Finance 2014: 17), although the effects of these measures will be visible mainly in the medium and long term.

Summing up, no restrictive reforms in the public sector have been implemented since 2008. The explanation is twofold. First, the role played by the social partners, especially the trade unions, which have managed to block unfavourable reform processes, such as (at least until 2014) the increase in the retirement age (EurWORK 2014b). Second, the reform of the sector already undertaken in the early 2000s, in common with other Northern European Member States, subsequent to the economic crisis experienced in the 1990s (Eurofound 2015).

### Research and development

Given the innovation-driven nature of the Finnish economy, gross domestic expenditure on R&D in Finland has been the highest in the EU since 2007. Specifically, it reached a peak of 3.8 per cent of GDP in 2009 and – despite a reduction – in 2013 the level of domestic expenditure on R&D was 3.3 per cent of GDP, an outstanding result in comparison with the 2 per cent EU average registered in the same year. Nevertheless, the country is not on track to reach the Europe 2020 national target on R&D (4 per cent of GDP). This is mainly due to the decline in business expenditure registered since 2011 (European Commission 2015c: 61), despite the internationally high figure when it comes to private spending on R&D[23] (Ministry of Finance 2014: 39). As for public spending on research and innovation, expenditure rose continuously from 2000 and declined for the first time in 2013, although it is still one of the highest values in the EU (1.01 per cent of GDP). However, consistent public spending on research and innovation did not directly translate into equivalent innovation outcomes (European Commission 2015c: 56).

Comprehensive reform of research institutions and research funding was launched in 2013, aimed at tackling this lack of efficiency by strengthening multidisciplinary and high-level research of significance for society, including research promoting renewal of the country's economic base and competitiveness, the development of working life and enhancement of the public sector (ibid.). Therefore, the reform addresses the specific recommendations issued by the European Commission with regard to innovation policies and attempts to find new solutions and fields of specialisation to increase the competitiveness of the Finnish economy (hard hit by the fall in productivity of the electronics and forestry industries). However, evaluation of the reform's outcome in this respect will be possible only in the long term. In particular, the measures implemented include the organisation of research institutes into larger and stronger entities and a new funding system for universities. The research activities of universities of applied sciences saw an increase in the allocation of resources of 10 million euros in 2013 and a new funding model implemented at the beginning of 2014 (Ministry of Finance 2014: 40).

Moreover, in order to reverse the declining trend in business R&D investment registered in the past few years, the Finnish government has put in place, for 2013–2014, a system of incentives including a tax incentive for research and development activity and a double depreciation allowance for industrial investments (ibid.). Additionally, with the attempt to promote research and development and enterprise growth, Finland has also resorted to a significant allocation of European Regional Development Funds for the budgeting period 2014–2020 (European Commission 2015c: 60).

To sum up, despite remarkable performances in comparison with other EU Member States, Finland is experiencing a reduction of its gross

**23.** In 2013, it accounted for 69 per cent of total spending.

domestic expenditure on R&D, mainly as a consequence of shrinking private investment. Following this development, the measures implemented in recent years have aimed at increasing private investments by means of tax incentives for conducting R&D activities. In 2013, additional emphasis was placed on the need to make the research environment more responsive to the needs of the Finnish economic model through the implementation of a comprehensive reform of research institutions and research funding.

### 3.2.3 Preliminary remarks on structural reforms in Finland and their determinants

Finland has traditionally been considered to be a country following a 'high-road' to economic growth and competitiveness, characterised by the desire to combine sound budgetary conditions, high quality production and innovation-driven growth, fairly high wages and social standards. This development model was consolidated over the 1990s and 2000s, when a series of reforms in various policy areas strengthened the 'social investment orientation' of the Finnish model, though at the cost of some cuts to social benefits, which contributed to an increase in income inequality.

Attempts to preserve the model while coping with the global crisis (as well as with more country-specific problems affecting the Finnish economy and society) are apparent from policy choices made over the crisis years. In fact, changes undertaken over the period generally display a significant degree of continuity with past reforms, although in a context characterised by deteriorating budgetary conditions and growing importance attached to the objective of fiscal consolidation. In more detail, while the initial reaction to the crisis consisted in the implementation of a series of measures aimed at preserving or improving social standards, since 2011 more restrictive measures (social standard devaluation) have been implemented, although they have sometimes been accompanied by investment-oriented initiatives. Particularly worrisome signals are coming from two key sectors of the Finnish development model: education and R&D. The former has been heavily hit by budget cuts undertaken since 2011, although public spending on education is still above the EU average and various measures aimed at improving the efficiency and effectiveness of the system have been implemented. Similarly, although it is still the highest in the EU, gross domestic expenditure on R&D as a

## Table 10 Summary table: drivers of reform and major reform trends in Finland, 2008–2014

| | 2008–2011 | 2011–2014 |
|---|---|---|
| **Drivers of reform** | | |
| Economic crisis | Economic recession (slight recovery in 2010);<br>Drop in exports;<br>Increase of public deficit and debt | Economic recession;<br>Increase of public deficit and debt |
| Coalition governments | Centre-right | Grand coalition |
| EU influence | EDP (2010–2011);<br>European Semester (2011) | European Semester |
| **Structural reforms** | | |
| Reform path (for the five policies under scrutiny) | Social standards improvement | Social standards devaluation/some selective investment |
| *Main reforms in each policy field* | | |
| Pensions | - Reduction of taxes on pension income and measures to ensure benefit indexation;<br>- Introduction of the 'Guarantee pension' | - Measures aimed at extending working life |
| Labour market | - Measures facilitating temporary lay-offs;<br>- Changes to unemployment benefits (replacement rates/ access conditions/activation requirements/ sanctions) | - Extension of ALMP (for specific target groups);<br>- Reform of PES |
| Education | - University reform | - Decrease of government expenditure;<br>- Reform of early childhood education and care;<br>- Reform of the on-the-job learning and apprenticeship training systems |
| Public sector | | - 4.3 per cent pay increase (2011);<br>- Local Government Structure Act (2013) |
| Research and development | | - Reform of research institutions and research funding;<br>- Tax incentives on R&D |

Source: Authors' elaboration.

percentage of GDP declined in 2012 and 2013, mainly as a consequence of a reduction in private expenditure.

Most of the reforms referred to in this report are consistent with the contents of CSRs received by Finland since 2011 within the framework of the European Semester. That said, the role of the EU in 'pushing' these changes should not be overestimated. Indeed, considering the remarkable continuity of changes implemented over the crisis years with the reform path of the past, messages coming from the EU level cannot be understood as 'strong pressure' on domestic policymakers. Probably, it would be more correct to interpret most of these recommendations as additional stimuli to implement decisions already taken at the national level. This holds true also for the fiscal consolidation measures implemented by the Finnish government since 2011. Although recommendations to continue fiscal consolidation efforts and preserve a sound fiscal position have been a constant of CSRs addressed to Finland, Dølvik *et al.* (2014: 271) suggest that the Finnish grand-coalition government would have probably managed to implement this sort of fiscal consolidation programme even in the absence of those recommendations. However, it is possible to expect that – in parallel with the deterioration of the budgetary situation – the degree of pressure from the EU level is likely to increase in the coming years, as such a trend is already apparent from the tenor of some of the CSRs received by Finland in 2014 and 2015.