

Regional Economic Development in Finland in the 1990s and the Outlook to 2005

Olavi Rantala

After the recession ten years ago, the Finnish economy began a period of exceptionally rapid growth, starting from the mid-1990s. In recent years, the growth of the economy has been significantly influenced by the vigorous expansion of the telecommunications equipment industry. The fact that manufacturing by this sector is concentrated in a few localities has, in the recent past, led to large regional differences in economic growth in Finland. These regional differences have in turn led to differentiation in the regional development of employment and population. The present downturn in the international economy is expected to slow the rate of industrial and economic growth in Finland over the next few years, which will consequently also slow the development of regional differentiation¹⁾.

The Growth of the Finnish Economy After the Recession of the Early 1990s

At the beginning of the 1990s, the Finnish economy entered a deep recession. The background to the crisis was the unbalanced economic development of the 1980s, above all a serious external imbalance arising from the gradual erosion of international cost-competitiveness.

The economic crisis was triggered by a sudden drop in exports in 1991, mainly due to the collapse of eastern exports related to the collapse of the Soviet Union. During 1991-1993, the recession led to a reduction of more than 10 percent in total output, a rise in the rate of unemployment to nearly 20 percent, a serious banking crisis, and a steep devaluation of the Finnish markka in 1991-1992.

The improvement in international cost-competitiveness deriving from the devaluation, along with the recovery in western export markets

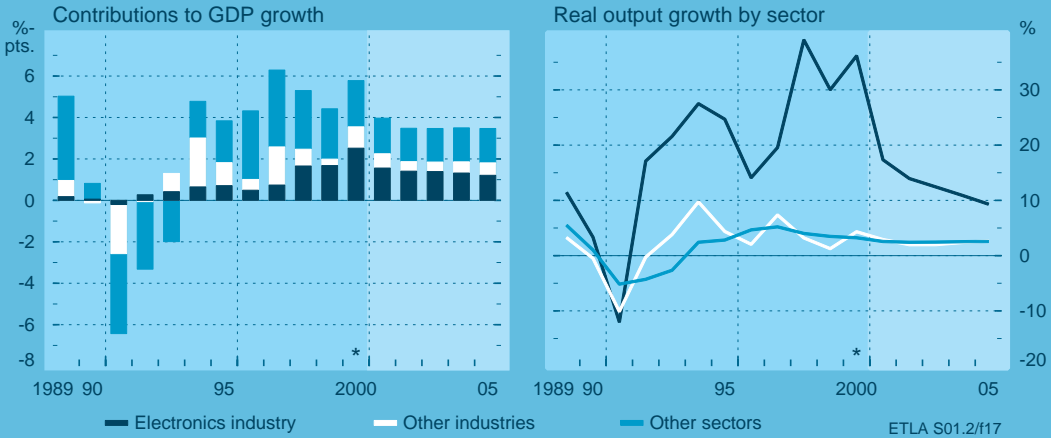
led to a rapid revival of Finnish industrial exports and output in 1993. Shortly afterwards, a new period of healthy growth began in the services and construction sectors too.

Since the mid 1990s, a major role in the rise of the Finnish economy has been played by the electronics industry, especially by intense growth in telecommunications equipment manufacturing. This is almost entirely thanks to a single company, i.e. Nokia (see *The Finnish Economy and Society 1/2001* p. 72-80).

The significance of the electronics industry peaked in the years 1998-2000, when output in the sector grew by 30-40 percent annually and represented more than one-third of the 5-6 percent annual growth of the GDP. Though the downturn in the international economy that began last year in the USA is forecast to slow the expansion of even the electronics industry, the sector is expected to continue growth at a rate clearly above that of traditional industry in the years 2001-2005.

¹⁾ The regional economic forecast was made at the beginning of 2001 and thus, in the case of the development of the whole Finnish economy, does not entirely correspond to the medium-term outlook presented above. The regional economic forecast was produced co-operatively by the Research Institute of the Finnish Economy, the Labour Institute for Economic Research, and the Pellervo Economic Research Institute.

Real Output Growth in Finland



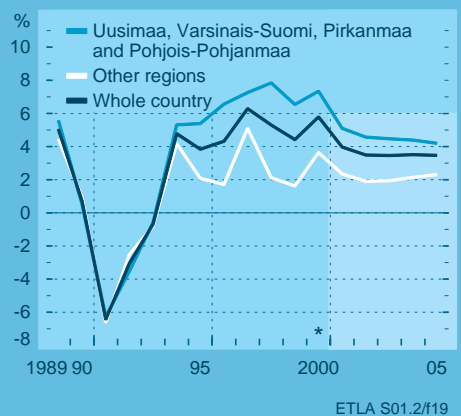
The Growth of the Electronics Industry has Affected Regional Economic Development

The rapid growth of the electronics industry, in particular Nokia's manufacture of telecommunications equipment, has, since the mid-1990s, led to a situation in which Finland has become divided into two 'camps' in terms of regional economic growth. In 1994-2000, the annual increase in Finland's GDP averaged about 5 percent. The annual increase in the total GDP of the four regions with the most rapid growth – Uusimaa, Varsinais-Suomi, Pirkanmaa and Pohjois-Pohjanmaa – averaged about 6.5 percent. Nokia's telecommunications equipment industry is concentrated in precisely those regions. The annual GDP growth of the rest of Finland averaged only about 3 percent. Regional differences in growth are expected to remain relatively large in 2001-2005 as well.

The Finnish GDP is expected to grow annually on average by about 3.5 percent in 2001-2005. Of the export sectors, the rate of growth of the output of the electronics industry, especially the manufacture of telecommunications equipment, will be clearly more rapid than that of total output, with the corresponding growth of telecommunications being the most rapid in all the domestic sectors. The success of the manufacture of telecommunications equipment is reflected in the forecasts for the growth of output, particularly in the Uusimaa, Varsinais-Suo-

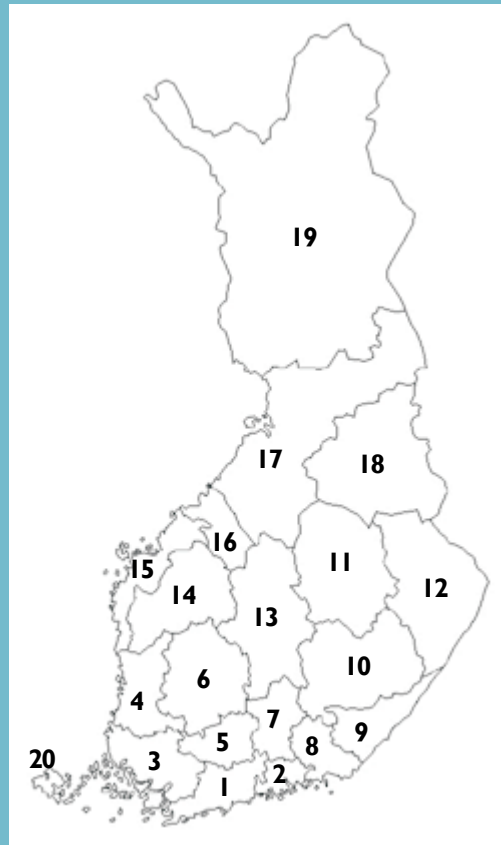
mi, Pirkanmaa and Pohjois-Pohjanmaa regions, where a significant share of the total output of this sector is located. In these regions, the annual growth of the GDP will be more than 4 percent in 2001-2005. In fact, the rapid growth in output is limited in Uusimaa to Helsinki and its contiguous city areas, in Varsinais-Suomi to the town of Salo, in Pirkanmaa to the city of Tampere, and in Pohjois-Pohjanmaa to the area around the city of Oulu.

GDP Growth in Finland



The Finnish Regions (NUTS3)

Region	Number
Uusimaa	1
Itä-Uusimaa	2
Varsinais-Suomi	3
Satakunta	4
Kanta-Häme	5
Pirkanmaa	6
Päijät-Häme	7
Kymenlaakso	8
Etelä-Karjala	9
Etelä-Savo	10
Pohjois-Savo	11
Pohjois-Karjala	12
Keski-Suomi	13
Etelä-Pohjanmaa	14
Pohjanmaa	15
Keski-Pohjanmaa	16
Pohjois-Pohjanmaa	17
Kainuu	18
Lappi	19
Åland	20

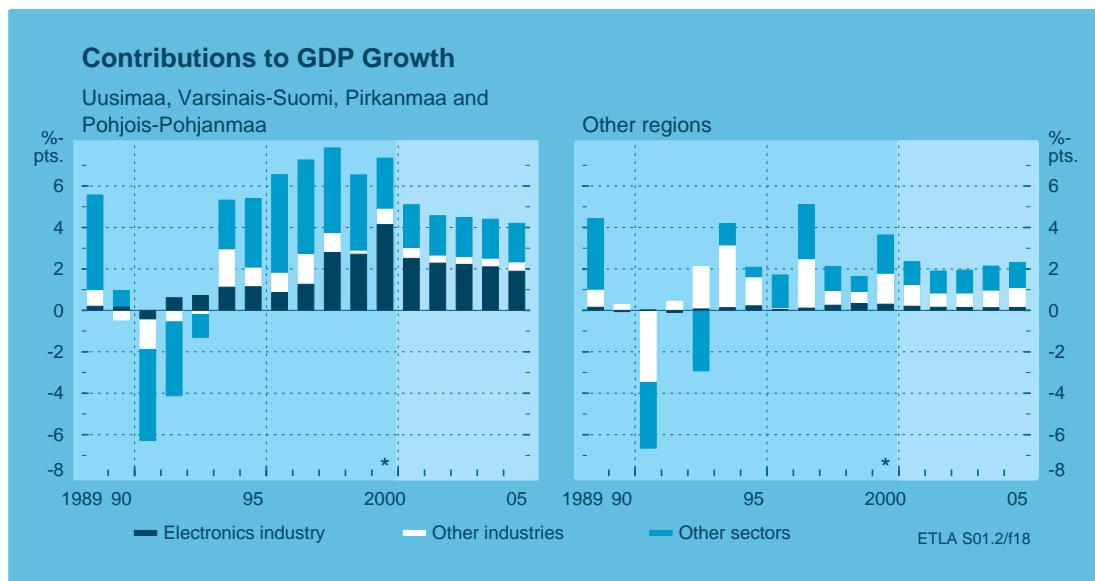


The other regions almost entirely lack the powerful growth effect of the electronics industry and the manufacture of telecommunications. In these areas, the annual growth of the GDP will remain on average at about 2 percent. The slowing of growth in the various regions will also be aggravated by the downturn in the international economy and the slackening of growth in traditional industry.

About half of the predicted 6 percent annual growth in the GDP in 2001-2005 in the regions of most rapid growth, i.e. Varsinais-Suomi and Pohjois-Pohjanmaa, will come from the expansion of the manufacture of telecommunications equipment. The powerful effect of the telecommunications sector in Varsinais-Suomi and Pohjois-Pohjanmaa is explained by the fact

that, on the one hand, the electronics industry accounts for about one-fifth of total output in these regions, and, on the other, that the manufacture of telecommunications equipment is forecast to grow at an annual rate of about 14 percent on average in 2001-2005. Growth in Uusimaa is significantly affected not only by the manufacture of telecommunications equipment, but also by the growth in telecommunications sector services. Uusimaa accounts for nearly one-half of the sector's output, which is forecast to grow at an average annual rate of about 7 percent over the next few years.

Rapid economic growth in a particular region is generally reflected in growth in trade and construction in the same area. It is forecast that this will also happen in the near future mainly



in Uusimaa, Varsinais-Suomi, Pirkanmaa and Pohjois-Pohjanmaa, where the rate of growth of the GDP will be clearly above that in the other regions. Thus, the expansion of the electronics industry has, besides its direct effect on output, indirect effects on economic growth in the growth regions by increasing the output of other sectors.

Outside of the most rapidly growing regions, the greatest part of industrial output comes from sectors other than the electronics industry. The forest industry is to a great extent concentrated in Kymenlaakso and Etelä-Karjala in southeast Finland. The effect of the traditional engineering industry is particularly apparent in the growth of output in Satakunta, Kanta-Häme, Pirkanmaa, Päijät-Häme and Keski-Pohjanmaa. Development in Itä-Uudenmaa is, on the other hand, dominated by the oil-refining and chemical industries. The growth effect of the chemical industry is also visible in Satakunta and Keski-Pohjanmaa, while that of the plastics industry can be seen in Pohjois-Karjala and Pirkanmaa. The growth effect of the food industry is most clearly apparent in output in Etelä-Pohjanmaa.

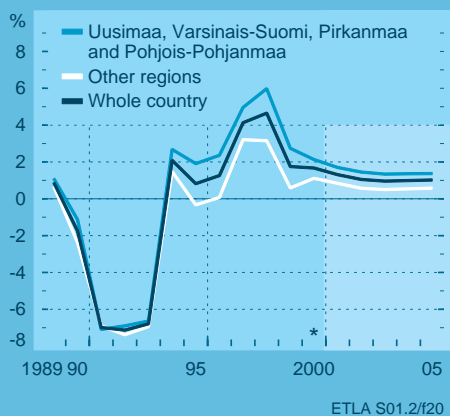
Of the major sectors of the economy, private services will considerably affect the growth of the GDP in 2001-2005. In this respect too, the regions have very individual economic struc-

tures. In Uusimaa and Åland, the growth of output in the service sectors has clearly a greater effect on the growth of the GDP than is the case in the other regions. The development of total output in Uusimaa reflects the growth of trade, transportation and business services in particular. Development trends in Åland are greatly affected by changes in the volume of shipping.

Employment and Population Development Reflect Regional Differences in Economic Development

The regional division of economic growth in Finland into two classes, which was referred to above, is also apparent in the regional development of employment and population after the mid-1990s. In regions with rapid economic growth, i.e. Uusimaa, Varsinais-Suomi, Pirkanmaa and Pohjois-Pohjanmaa, the annual increase in the demand for labour in the latter half of the 1990s was on average two percentage points faster than in areas of slow economic growth. Simultaneously, in regions of rapid economic growth, the rate of population increase has averaged nearly one percent, while areas of slow economic growth saw the start of a decrease in population in the mid-1990s, as a result of emigration.

Employment Growth in Finland



The success of the electronics industry is reflected not only in the development of total output, but also of employment in those regions in which the sector has significant output. Though labour productivity is increasing very rapidly in the electronics industry, the exceptionally vigorous growth of output in the sector will continue to lead to an increasing need for labour in the next few years. In addition, the electronics industry indirectly affects the improvement of employment in the growth regions by accelerating growth in labour-intensive sectors, such as construction and trade.

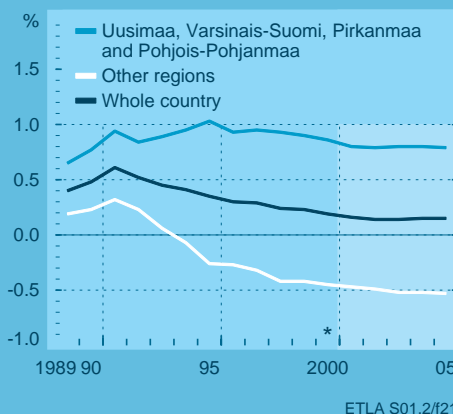
Services have a significant job-creating effect, both nationally and regionally, as they are labour-intensive sectors with a relatively low rate of growth in labour productivity. Thus, a greater than average share of services in total output will increase employment, especially in Uusimaa. In Uusimaa and other regions, new jobs are created particularly in trade and business services. Besides private services, the public sector – mainly the municipalities – also has a substantial effect on the growth of employment in all regions. In the next few years, construction, too, will have a positive effect on employment, though the clearest employment effect will be in those regions in which building output increases the most, in line with general economic activity.

Over the next few years, the population of the whole country will increase to only a relatively

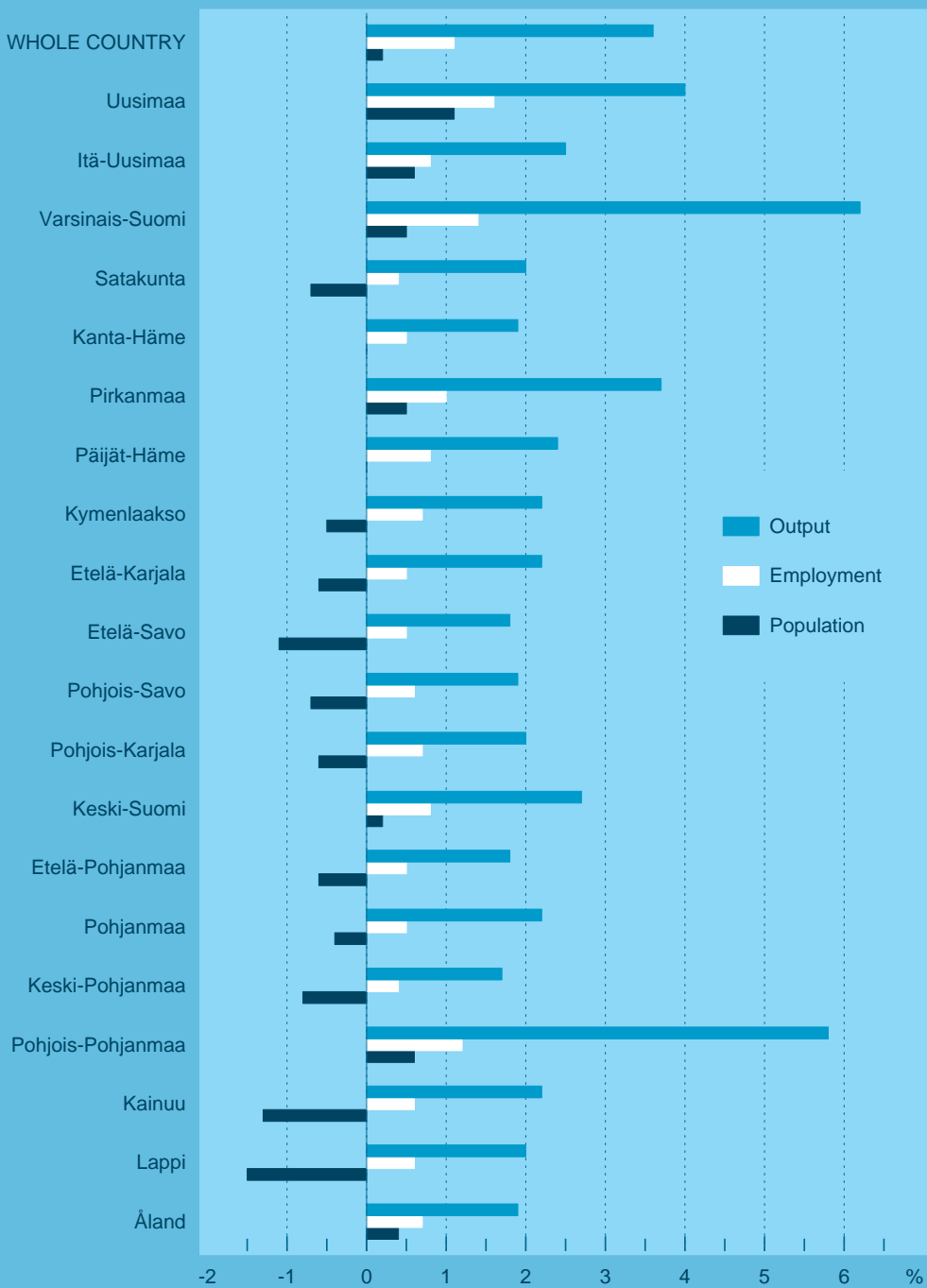
small extent. Some areas, however, will see a substantial increase in population, while others will experience a considerable drop. Good economic development will be reflected in a net increase in population through migration and a visible growth of population in regions such as Uusimaa, Varsinais-Suomi, Pirkanmaa and Pohjois-Pohjanmaa. Differences between regions in terms of population development will tend to be boosted by the acceleration in the natural growth of the population produced by increases from migration. On the other hand, in areas with a net loss of population through migration, the population structure will age, the birth rate drop, and natural population development will become unfavourable.

The supply of labour will reflect the trend of population development and will continue to decrease in some areas. As at the end of the 1990s, the supply of labour will develop negatively in certain areas in eastern and northern Finland, from which emigration will continue to be pronounced. The aging of the population will also reduce the supply of labour. It is forecast that the rate of unemployment in Finland will drop from last year's figure of nearly 10 percent to nearly 7 percent by 2005. The rate of unemployment will then remain clearly higher than average in many areas in eastern and northern Finland.

Population Growth in Finland



Average Annual Growth in Real Output, Employment and Population, 2001-2005



Regional Policy Evens Out Regional Differences in Standards of Living

Finland has traditionally made extensive use of regional policy to even out differences in regional economic developments. Support for the private enterprise sector was determined for a long time on the basis of regional policy. The provision of transport and communication services, in a sparsely populated country of great distances, has also had a considerable effect on regional developments. To this one should also add the provision of other infrastructure, the regional investments of state-owned companies and the establishment of regional institutes of higher learning.

Both national and common EU regional policy play a role in Finland's regional economic development. National regional policy can be divided into direct regional policy and indirect regional policy arising from taxation and other transfer payments. Indirect regional policy is an important tool in reducing regional income differentials – in terms of money it is even more extensive than direct regional policy.

The primary aim of taxation, social payments and other transfer payments in Finland is to guarantee equal living standards to all demographic groups regardless of where they live. This evens out regional differences indirectly as it is primarily manifest in the transfer of funds from richer areas to less developed ones.

A consequence of tax policy and social policy is that regional differences in disposable household incomes per capita are significantly more evenly distributed than GDP per capita. This means that, despite the vast differences in regional economic growth since the mid-1990s, the average standard of living in different parts of the country is more or less the same. In terms of household income per capita, only Uusimaa stands out from the rest as an area of higher living standards.

Regional policy proper aims to directly influence the factors affecting regional development and to create the prerequisites for economic growth and employment in less developed are-

as. The forms of regional development programmes and support currently vary to a great extent. Programme-based regional policy is conducted through regional EU programmes and government programmes for the development of cities, rural areas and centres of expertise. Special national measures are also taken on the basis of regional policy.

Finland's EU membership has had its effect on regional policy. EU regional policy is essentially programme-based, whereas Finland's regional policy was previously zonal in nature. In addition to general levels of development, EU regional policy aims to tackle specific regional developmental concerns. Financing through the so-called horizontal programmes is also often used, in connection with which one now often speaks of urban policy and rural policy. Finland's EU membership has also brought with it EU structural funds as well as new ways of doing things. The share of purely national actions has simultaneously decreased.

EU structural fund financing and related national regional assistance has increased during Finland's EU membership since 1995. For 1995-1999, this regional assistance amounted to about FIM 18 billion. The new EU structural fund programme will distribute about FIM 28 billion between 2000-2006.

A large portion of national regional policy financing is tied to EU programmes. In contrast to other EU countries, the focus of Finland's regional assistance for private enterprise has been on research and development. On the other hand, the share of regional assistance distributed on purely regional grounds has been relatively low in comparison with other EU countries.

EU expansion into Eastern Europe will limit the ability of Finland and other old member states to receive EU regional funding on the current scale after 2006. However, Finland is different from the old and the new members due to its sparsely distributed population, severe climate and remote location. It is for this reason that Finland will continue to require an efficient national regional policy to supplement EU regional policy in the future.