Lloyds TSB | Corporate Markets

Country Review

July 2008

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Finland

Commentary

■ **Political outlook** - Following Parliamentary elections last year, Prime Minister Matti Vanhanen took charge of the four-party coalition government for a second term. However, recent scandals over campaign funding as several prominent party members failed to declare several substantial donations, has undermined the government's integrity. President Halonen was narrowly re-elected in January 2006 for a further 6 year term. The fiscal balance is likely to remain in surplus, despite tax cuts and slower gdp growth, as consumer spending remains strong, although the government is aware of the need to maintain a budget surplus in the face of a rapidly growing and aging population.

■ **Economic growth** - Industrial production is set to slow sharply this year, following a strong performance last year, although this was mainly due to output rebounding following the strikes in the paper industry in 2006. The trade balance will fall as the strong euro reduces demand for exports, although we still expect it to stay in surplus. We expect Finnish economic growth to slow in 2008 to 2.8%, down from 4.8% last year but consumer spending is expected to remain fairly resilient as employment and earnings growth remain strong, aided by government led tax incentives aimed at creating more jobs.

■ **Inflation and prices** - Inflation last year hit 2.5% on the back of higher housing costs and increased energy prices, and is set to rise further in 2008 to 3.5% as oil and food prices continue to remain elevated. While household inflation expectations have also risen substantially since the start of the year, inflation is likely to peak at over 4% this year before gradually falling back to target. However, with the ECB's tough monetary policy stance over inflation, we expect CPI to fall back towards 2%, although this may not happen until 2010.

■ **Interest rates and Forex** - Our current forecast has eurozone interest rates reaching 4.5% by end of 2008 before falling back next year as inflationary pressures subside. Slower economic growth and tight monetary policy will allow inflation to fall back towards a more comfortable level, although there is a risk that further rises in commodity prices could see inflation remain more stubborn than anticipated. The euro rose to a record against the dollar earlier this year and has remained resilient since then. However, we forecast that US$/€ could depreciate to 1.47 by the end of the year and £/€ to 1.27.

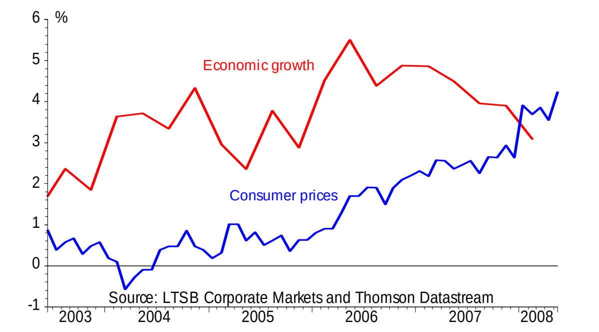
Country profile

- Prime Minister: Matti Vanhanen
- Parliament: Centre Party, National Coalition Party, Green League and Swedish People's Party coalition
- Next election: March 2011 / 2012 (General/Presidential)
- Nominal GDP: US$ 260.9bn (2007)
- Population: 5.27m (2006)
- Exchange rate: €/US$ 1.57, €/UK£ 0.79 (July 2008)
- Interest rates: ECB repo rate - 4.25% (July 2008) 10-year government bond yield – 4.79% (July 2008)
- Investment grade rating: Aaa (Moodys), AAA (S&P)

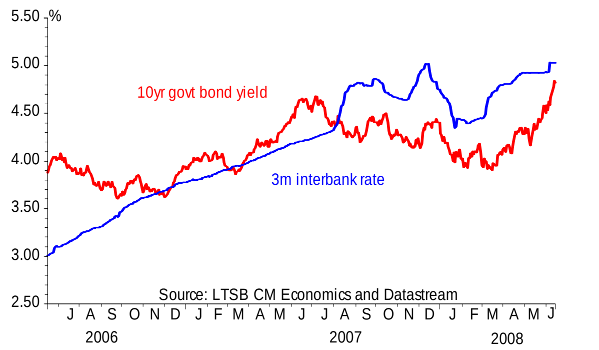
Trade statistics (2004)

Main export markets		Main suppliers	
Sweden	10.8%	Germany	14.6%
Germany	10.3%	Russia	12.9%
Russia	8.7%	Sweden	10.7%
Key country exports		**Key imports**	
Telecom related	17.7%	Electric machinery	10.0%
Paper	17.4%	Petroleum	8.6%

Growth and inflation



Short and long term interest rates



Key economic and market indicators

Annual % change	2007e	2008f	2009f	2010f
Gdp growth	4.3	2.6	2.3	2.5
Industrial production	4.3	3.3	2.4	2.3
Consumer spending	3.6	3.4	2.6	2.5
Consumer price inflation	2.5	3.8	3.0	2.0
Average earnings (whole economy)	3.1	4.1	4.1	3.3
Unemployment rate (% average)	6.9	6.2	5.9	5.9
Current account balance (% gdp)	4.6	4.3	3.6	3.7
Budget balance (% gdp)	3.9	4.2	4.1	3.9
Short-term interest rate (3m interbank, % average)	4.3	4.7	4.5	4.5
Bond yield (10-year government bond, % average)	4.3	4.4	4.7	5.0
Exchange rate (US$/€, end year)	1.46	1.47	1.30	1.24

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