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Author: Otto Kyyrönen

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The Political Economy of Debt Sustainability Analysis: A Case Study of the Finnish Debt Brake

Otto Kyyrönen

The Finnish Centre for New Economic Analysis (UTAK)

Abstract: This paper critically examines the debt sustainability analysis (DSA) calculations underpinning Finland’s new national fiscal rule, the “debt brake.” The rule requires the public debt-to-GDP ratio, currently around 90 percent, to decline by at least 0.75 percentage points annually until it reaches 40 percent. Its implementation will rely on DSA calculations by the Finnish Ministry of Finance (MoF), which estimates that the next government must undertake fiscal adjustment amounting to more than 10 percent of this year’s central government appropriations. Drawing on the European Commission’s DSA framework, the paper reconstructs a model analogous to the MoF’s unpublished model and analyses how assumptions about fiscal multipliers, automatic stabilisers, and hysteresis effects shape projected debt dynamics. It then compares expenditure-based consolidation with revenue- and investment-based alternatives under different multiplier assumptions. The results suggest that the MoF’s calculations may underestimate the adverse effects of spending cuts on growth and debt dynamics. Alternative scenarios based on revenue measures and public investment can produce comparable or better debt outcomes while sustaining higher output. The paper shows how technical modelling choices, which often escape sufficient critical scrutiny, shape perceived fiscal policy space.

Keywords: debt sustainability analysis; fiscal rules; debt brake; political economy; Finland.

JEL: E17; E62; H20; H50; H63; H68.

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Contact: otto.kyyronen@utak.fi.

1 Introduction

In December 2025, Finland adopted a new national fiscal rule (hereafter the “debt brake”). The debt brake requires:

- that the public debt ratio¹ – currently around 90 percent – fall by at least 0.75 percentage points annually until it is below 40 percent of gross domestic product (GDP); and
- that the headline deficit² no longer exceed 2.5 percent of GDP.

The implementation of the debt brake will rely heavily on debt sustainability analysis (DSA) calculations produced by the Finnish Ministry of Finance (MoF). Unlike the European Commission (EC), for example, the MoF does not make its DSA calculations publicly available for scrutiny. This lack of transparency turns the MoF’s calculations into a black box that shapes the boundaries of public debate on fiscal policy.

In this article, I critically examine the DSA calculations underpinning the debt brake and assess the fiscal rule’s potential macroeconomic effects on the Finnish economy over the period 2028–39.³ The analysis is based on macroeconomic simulations created with the EC’s DSA model.⁴ The simulations consider different fiscal policy scenarios in which the debt target required by the debt brake is pursued through spending cuts alone, tax increases alone, or a combination of tax increases and public investment.

First, using the assumptions of the MoF, I simulate how much fiscal consolidation is needed over 2028–31 for the public debt ratio to decline – as required by the debt brake – by an average of 0.75 percentage points per year over 2032–39. According to my calculations, this condition is met under the MoF’s assumptions if fiscal consolidation over the next four-year parliamentary term strengthens the structural primary balance⁵ by €9.7 billion on an annual basis by 2031.⁶ This estimate is equivalent to more than 10 percent of this year’s central government appropriations and is consistent with the official consolidation recommendation

¹The public debt ratio is the ratio of gross public debt to GDP.

²The headline deficit is the unadjusted difference between total public revenue and total public expenditure.

³Finland is also subject to the EU fiscal rules, which by themselves will require significant fiscal consolidation in the coming years (Darvas, Welslau and Zettelmeyer 2024; Kyörönen, Holappa and Lainà 2025). This article nevertheless abstracts from the EU fiscal framework and focuses solely on the debt brake.

⁴I have further developed the EC’s DSA model to account for hysteresis effects. This is explained in Section 4.

⁵The primary balance is the headline budget balance excluding interest expenditure. The structural primary balance is derived by excluding cyclical effects and one-off or other temporary measures from the primary balance. It therefore provides a measure of the underlying fiscal position adjusted for temporary economic and fiscal factors.

⁶Importantly, this is a *net* figure. In other words, if the government were to cut taxes by €1 billion, it would need to offset this by implementing €10.7 billion in total consolidation measures.

issued by the parliamentary working group on fiscal policy in February 2026 (FinGov 2026, p. 83).⁷

Second, I simulate how a €9.7 billion consolidation package may affect the Finnish economy if implemented mainly through spending cuts during a recession or under conditions of weak growth. This question is particularly relevant because Finland’s real GDP per capita has not risen above its 2008 level since the financial crisis, and the economy has suffered from weak domestic demand since the end of 2022 (Kyyrönen 2025). The alternative simulations show that, under such conditions, a consolidation package of this scale may weaken growth so substantially that the public debt ratio does not turn onto a declining path after all.

Third, I simulate how much fiscal adjustment would be required in 2028–31 through tax increases alone, or through a combination of tax increases and public investment, for the public debt ratio to decline by an average of 0.75 percentage points per year in 2032–39. In these simulations, I again assume that the Finnish economy is operating below potential when the adjustment is implemented. According to my calculations, the debt target is met if taxation is tightened by a nominal €8.4 billion during the next parliamentary term, or if taxes are increased by €8.1 billion while public investment is raised by €5.1 billion. In the latter scenario, the positive multiplier effects of public investment accelerate growth, leaving real GDP €21.9 billion – or 7.5 percent – higher in 2039.

To my knowledge, this article is the first study to apply DSA modelling to the Finnish debt brake. It contributes to a growing literature showing that fiscal consolidation implemented under conditions of weak economic growth, especially when based primarily on spending cuts, may produce substantially weaker macroeconomic outcomes than anticipated and may even increase the public debt ratio (Albuquerque and Green 2023; Auerbach and Gorodnichenko 2017; Ciaffi, Deleidi and Capriati 2024; Fatás and Summers 2018; Gechert, Horn and Paetz 2019; Gechert and Rannenberg 2018; Goemans 2023; Heimberger *et al.* 2024; Holter and Ferreira 2024; Kyyrönen, Holappa and Lainà 2025; Lainà 2025). The analysis further suggests that these risks can be mitigated by calibrating DSA calculations more carefully according to the type of fiscal policy measure and the cyclical position of the economy. Under conditions of weak growth, tax increases may therefore be preferable to spending cuts, while the most favourable outcomes may be achieved by combining revenue measures with higher public investment.

The remainder of the article is structured as follows. Section 2 presents stylised facts on the Finnish economy. Section 3 reviews the relevant literature on fiscal multipliers and hysteresis. Section 4 introduces the EC’s DSA model, the assumptions used in the simulations, and the data sources. Section 5 presents the simulation results for different fiscal policy scenarios. Section 6 discusses the implications of the findings. Section 7 summarises the article’s main conclusions.

⁷Relative to total consolidated general government expenditure in 2024, €9.7 billion amounts to more than 6 percent. Here, consolidated means that property expenditure, income transfers and capital transfers between general government sub-sectors are excluded from general government expenditure.

2 Stylised facts: A brief post-war history of the Finnish economy

Table 1 reports key indicators for the Finnish economy from 1961 onwards. The periods are separated by major economic disruptions: the oil crisis of the 1970s, the depression of the early 1990s, the global financial crisis, and the COVID-19 pandemic. Following the literature on demand and growth models (Hein and Martschin 2021; Hein, Meloni and Tridico 2021), the table reports the growth contributions of each GDP component for each period, alongside selected additional indicators.

Table 1: Key indicators, Finland, 1961–2025.

Variables	1961–75	1978–89	1994–2008	2010–19	2021–25
Growth contributions (pp)					
Domestic demand	5.4	4.2	3.3	1.3	0.3
– Private consumption	2.6	2.1	1.7	0.6	0.3
– Public consumption	1.0	0.7	0.4	0.2	0.5
– GFCF	1.5	1.3	1.1	0.4	-0.4
– Changes in stocks	0.2	0.2	0.2	0.2	-0.1
Net exports	-0.3	-0.1	0.7	-0.1	0.4
– Exports	1.0	1.2	3.1	1.1	1.1
– Imports	-1.3	-1.4	-2.5	-1.2	-0.7
Other variables					
Real GDP growth (%)	4.8	3.9	3.8	1.2	0.5
Net exports (% of GDP)	-1.5	0.6	6.7	-0.4	-0.1
Real wage growth (%)	3.9	2.1	2.1	0.5	-0.3
Unemployment (% of LF)	1.9	5.1	10.5	8.3	8.0
Public debt (% of GDP)	8.6	14.1	45.6	62.0	79.0

Notes: Each variable is expressed as the average value for the respective period. Growth contributions indicate how much each GDP component contributes to the overall growth rate of real GDP, expressed in percentage points. GFCF denotes gross fixed capital formation, that is, investment in fixed assets. Real wages are proxied here by the CPI-adjusted index of wage and salary earnings, which is constructed by Statistics Finland (StatFin) to measure average regular earnings among full-time employees, including performance-related bonuses and collectively agreed one-off payments. The unemployment rate is the number of unemployed persons aged 15–74 who are without work, available to start within two weeks, and have actively sought work in the previous four weeks, expressed as a share of the labour force (LF). Data on the public debt ratio begin in 1970.

Sources: EC (2026b); StatFin (2026); own calculations.

As shown in Table 1, real GDP growth was rapid from the early 1960s until the late 2000s. Average annual growth was close to 5 percent in 1961–75 and close to 4 percent in both 1978–89 and 1994–2008. In the 1960s, 1970s, and 1980s, growth was driven mainly by domestic demand, supported by strong real wage growth, especially in the 1960s and 1970s, and by strategically timed cycles of currency devaluation before Finland joined the euro area in 1999.⁸ By contrast, the contribution of net exports of goods and services was close to zero in the pre-1990s period, while exports contributed around one percentage point per year.

⁸For Finnish cycles of currency devaluation, see Sauramo (2016).

Economic growth, full employment, and high inflation kept the public debt ratio extremely low, at around 10 percent of GDP.

After the depression of the early 1990s, real GDP growth remained at a broadly similar level, but Finland’s demand and growth model shifted from domestic demand-led to export-led. In particular, the rise of Nokia helped drive a historically exceptional increase in net exports, which averaged 6.7 percent of GDP in 1994–2008, while the growth contribution of exports rose to 3.1 percentage points per year. The large current account surplus provided sufficient external demand to sustain growth, even as real wages lagged behind labour productivity and unemployment settled at a structurally higher level, averaging 10.5 percent in 1994–2008. The public debt ratio rose sharply during the depression years, from 13.8 percent in 1990 to 56.2 percent in 1994, but rapid real GDP growth caused it to decline again, to 34.7 percent by 2008.

The global financial crisis hit the Finnish economy in 2009, when real GDP contracted by 8.1 percent. The shock coincided with strategic mistakes by Nokia’s management,⁹ as a result of which Finland lost its key export engine. The growth contribution of exports then returned to its historical level in 2010–19, at 1.1 percentage points per year.

After the financial crisis, employer organisations increasingly advanced the view that Finland still had an export-led growth model and that the main problem was the weak price and cost competitiveness of exports (Etna 2014; Kaitila 2019). This view, together with the traditional idea that real wages should follow labour productivity, helps explain why the policy response was to engineer real wage stagnation through coordinated wage-setting until economic growth recovered. As shown in Table 1, real wage growth fell to an average of 0.5 percent per year in 2010–19, compared with 2.1 percent per year in 1994–2008.

At the same time, every post-2010 government – with the exception of the Marin government in 2019–23 – implemented repeated consolidation packages.¹⁰ Wage stagnation and recurrent consolidation weakened domestic demand when external demand was already insufficient. This reduced firms’ inducement to invest,¹¹ further weakening both growth prospects and the non-price, or quality-based, competitiveness of exports.¹² This dynamic helps explain why real GDP per capita in Finland failed to regain its 2008 level during the 2010s and remains below that level even today (see Figure 1).

When the negative shock caused by the COVID-19 pandemic reached Finland, the Marin

⁹According to Vuori and Huy (2016), internal fears among Nokia’s middle managers discouraged them from passing negative information to top management. As a result, senior managers formed an excessively favourable view of the organisation’s technological capabilities and paid insufficient attention to long-term investments in innovation. This contributed to Nokia’s rapid loss of its position as a globally dominant and innovative technology company.

¹⁰The MoF’s economic surveys report the estimated budgetary impact of each government’s fiscal stance. For the Katainen government, see MoF (2014, pp. 75–77); for the Sipilä government, see MoF (2019, pp. 57–59); for the Marin government, see MoF (2023, pp. 68–71); and for the Orpo government, see MoF (2026, pp. 79–82).

¹¹According to the Confederation of Finnish Industries’ (EK) quarterly Business Tendency Survey, Finnish firms have repeatedly reported that insufficient demand has been the main constraint on growth since the financial crisis (EK 2026).

¹²For an analysis of non-price competitiveness in the euro area, see Gräbner *et al.* (2020).

government responded with countercyclical fiscal policy. Higher public expenditure, together with a 2.5 percent contraction in real GDP, pushed the public debt ratio above 70 percent for the first time in Finland’s post-war history. The stimulus nevertheless supported a rapid rebound: output grew by 2.7 percent in 2021, while the debt ratio fell by 1.3 percentage points. In 2022, labour-market performance also improved markedly, with the employment rate among 15–64-year-olds reaching its highest level since the 1980s, at 74.2 percent in October–November.¹³

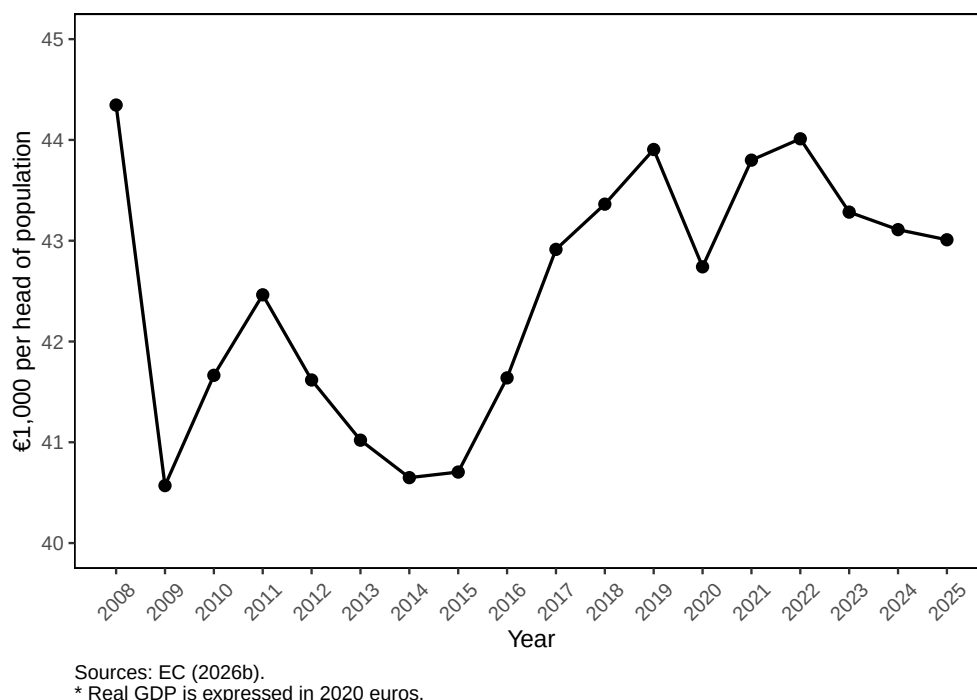


Figure 1: Real GDP per capita, Finland, 2008–25.

Inflation began to accelerate in Finland in 2021, with the year-on-year rate reaching a high of 9.1 percent in November–December 2022. As nominal wages failed to keep pace with prices, real wages declined by 6.3 percent in 2021–23, returning to roughly their level a decade earlier. At the same time, the European Central Bank (ECB) began raising its policy rate in July 2022 to contain inflation. The tightening was transmitted almost immediately to Finland, where most loans have floating interest rates (Core *et al.* 2025, p. 36). Higher interest rates significantly curbed domestic demand, and the economy entered a recession in late 2022.

The Orpo government took office in 2023 and pledged to improve the budget balance by cutting annual public spending by €4 billion by 2027, mainly from social security and health-care. It also argued that cuts to social security and other reforms would raise employment by

¹³For an estimate of the positive hysteresis effects of the Marin government’s stimulus package, see Lainà (2021).

100,000 persons, generating a further €2 billion in annual savings.¹⁴ However, implementing spending cuts during a recession and in a tight monetary-policy environment – especially cuts targeted at low-income households with a high propensity to consume – further weakened domestic demand.¹⁵ Economic difficulties therefore accumulated: real GDP growth was weaker than expected, the public debt ratio rose faster than projected, and unemployment began to increase. As shown in Figure 2, Finland’s unemployment rate started to rise in 2023 against the broader European trend and became the highest in the European Union (EU) in late 2025. In response, the Orpo government doubled down on its commitment to balance the budget and lower the public debt ratio, announcing a further €5–6 billion in spending cuts and tax increases. At the same time, however, it decided to reduce taxes on high-income earners and corporations by around €1.5 billion per year, further undermining its own stated objective of balancing the budget.¹⁶

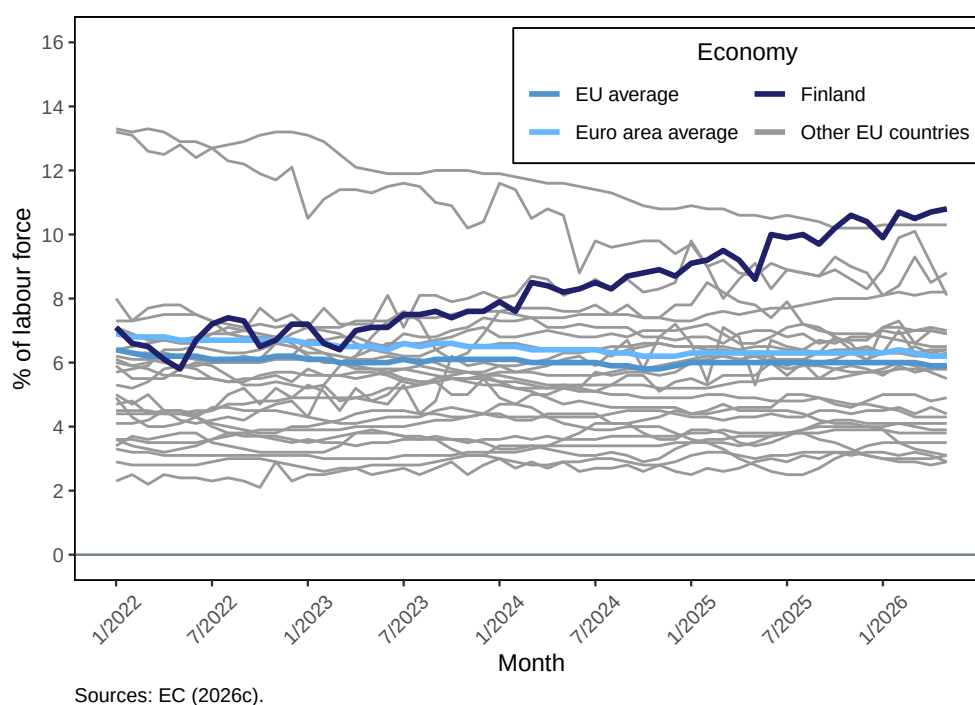


Figure 2: Unemployment rate (seasonally adjusted), EU, January 2022–May 2026.

In June 2025, the Orpo government unexpectedly held a press conference at which Prime Minister Petteri Orpo and Finance Minister Riikka Purra announced a proposal for a national debt brake for Finland. Other parliamentary parties subsequently entered into negotiations with the government, and the debt brake was signed into law in December 2025. As part of

¹⁴For a critical analysis of the MoF’s employment impact assessments of the Orpo government’s reforms, see Kyyrönen and Sund (2024).

¹⁵For an estimate of the negative hysteresis effects of the Orpo government’s consolidation package, see Lainà (2025).

¹⁶For a more comprehensive analysis of monetary and fiscal policy in Finland in the 2020s, see Kyyrönen (2025).

the new fiscal rule, a parliamentary working group on fiscal policy was established, bringing together politicians and MoF officials to discuss the scale of consolidation required in the near future. (Kyyrönen 2026, pp. 6–7.) In February 2026, the working group recommended that the next government, taking office in 2027, implement a net consolidation package of €8–11 billion over 2027–31 (FinGov 2026, p. 83). For context, although the Orpo government has announced spending cuts and tax increases worth €9–10 billion, the net consolidation amounts to only around €3 billion once spending increases and tax cuts are taken into account (NAOF 2025). The next government is therefore expected to consolidate roughly three times as much as the Orpo government.

3 Literature review on fiscal multipliers and hysteresis

The DSA calculations rely on assumptions about the size and persistence of fiscal multiplier effects. In short, a fiscal multiplier measures the impact of fiscal policy changes on GDP. For example, if the multiplier is 1.5, a €1 billion cut (raise) in public expenditure reduces (increases) GDP by €1.5 billion. Fiscal multipliers can be expressed as impact multipliers, which capture the immediate effect; peak multipliers, which indicate the highest value reached over a given period; average multipliers over a longer period; or cumulative multipliers, which capture the total effect over a specified time horizon.

Fiscal multipliers have typically been found to be smaller during expansions and larger during recessions or periods of weak economic growth (Auerbach and Gorodnichenko 2012; Gechert and Rannenberg 2018). Their size also varies across fiscal instruments. For example, tax multipliers are, on average, smaller than expenditure and public investment multipliers (EC 2026b, p. 56; Gechert and Rannenberg 2018). Institutional and structural features of the economy also matter. Multipliers tend to be larger in countries with fixed exchange rates than in countries with flexible exchange rates (Banerjee and Zampolli 2019; Ilzetzi, Mendoza and Végh 2013), and smaller in economies with high import-to-GDP ratios, as part of the demand effect leaks abroad (Gechert and Rannenberg 2018). Some evidence also suggests that multipliers are smaller in ageing economies, where labour supply is more constrained (Honda and Miyamoto 2020; Morita 2022). Other determinants, such as the public debt ratio and the tax rate, have also been studied, although the findings remain mixed (Boitani, Perdichizzi and Punzo 2022; Cho and Lee 2024; Ciaffi, Deleidi and Capriati 2024; Gunter *et al.* 2021; Ilzetzi, Mendoza and Végh 2013).

Fiscal multipliers are estimated using a wide range of research designs and methods, which helps explain why multiplier estimates vary across studies. The meta-study by Gechert and Rannenberg (2018), however, provides a comprehensive overview of the literature. They conduct a meta-regression of more than 1,800 fiscal multipliers estimated for various measures implemented under different cyclical conditions. Under conditions of weak economic growth, they find that the average two-year cumulative multiplier is 0.6 for tax measures, 1.8 for public expenditure, and 2.3 for public investment.

Public investment multipliers are generally found to be relatively large and persistent. For example, Goemans (2023) estimates that, under conditions of significant economic uncertainty, the public investment multiplier is approximately 2.1 in the first year. Part of this

effect reflects the ability of public investment to crowd in private investment: Matvejevs and Tkačevs (2023), for instance, find that one euro of public investment increases private investment by an average of two euros seven years later. Public investment has also been found to raise output, reduce the public debt ratio, increase employment, and lower unemployment (Abiad, Furceri and Topalova 2016; Gechert and Rannenberg 2018; Heimberger and Dabrowski 2025).

Public investment may also raise potential GDP. Fournier (2016, pp. 12–13) finds that a one-percentage-point increase in the public investment-to-GDP ratio raises the following year’s potential growth rate by around 0.1 percentage points. The effect is substantially larger for research and development (R&D): a one-percentage-point increase in the share of public R&D expenditure in primary expenditure raises the potential growth rate by as much as 1.4 percentage points, while a corresponding increase in public basic research expenditure raises it by up to 3.0 percentage points. Ciaffi, Deleidi and Mazzucato (2024) also find large multiplier effects for public R&D expenditure, estimating that each additional euro of public R&D raises GDP by €10–15 within five years.

Another key concept in analysing the macroeconomic effects of fiscal policy is hysteresis. Hysteresis refers to situations in which short-term demand shocks have persistent effects on either the level or the growth rate of real GDP (Fatás and Summers 2018; Gechert, Horn and Paetz 2019; Lainà 2021, 2025). These effects are often explained through labour-market dynamics: fiscal consolidation raises unemployment, some of which becomes structural, thereby weakening long-term economic performance, while fiscal stimulus can operate in the opposite direction. Hysteresis may also arise through investment channels, if consolidation directly reduces public investment and/or indirectly weakens firms’ inducement to invest, thereby weakening capital accumulation (Ball 2014; Fatás and Summers 2018; Heimberger and Dabrowski 2025; IMF 2015).

Hysteresis may leave the economy with either a permanent level loss or a permanent growth loss (Anzoategui and Kim 2023; Ball 2014; Fatás and Summers 2018; Furlanetto *et al.* 2025; Gechert, Horn and Paetz 2019; Lainà 2021, 2025; Roa-Rozo 2024). For example, the recession of the 1990s left the Finnish economy with a permanent level loss: economic growth eventually returned to its pre-crisis rate, but real GDP never caught up with its previous trend. By contrast, the financial crisis caused a persistent decline in Finland’s real GDP growth, resulting in substantially larger cumulative economic losses. (Kyyrönen and Sund 2024, pp. 31–34.)

4 Methodology and data

4.1 The debt sustainability model

The calculations in this study are based on the EC’s DSA model (EC 2024b; see also Darvas, Welslau and Zettelmeyer 2024). I use the deterministic part of the model, meaning that the calculations do not incorporate the so-called stochastic component. I have also extended the EC’s DSA model in certain respects to account for hysteresis effects.

As Finland's general government debt is denominated entirely in euros, the public debt ratio in year t can be calculated as follows:

$$D_t = D_{t-1} \cdot \frac{1 + r_t}{1 + g_t} - PB_t + SFA_t \quad (1)$$

where D is the public debt ratio, r is the implicit interest rate on public debt, g is the growth rate of nominal GDP, PB is the primary balance relative to GDP, and SFA is the stock-flow adjustment relative to GDP. The implicit interest rate on public debt is calculated by dividing interest expenditure paid during the year by the debt stock at the end of the previous year, while the primary balance refers to the difference between general government revenue and expenditure excluding interest expenditure.

The change in the debt ratio is obtained by subtracting the previous year's debt ratio from both sides of the equation. Rearranging terms gives:

$$\Delta D_t = D_{t-1} \cdot \frac{r_t - g_t}{1 + g_t} - PB_t + SFA_t \quad (2)$$

The implicit interest rate on public debt, the primary deficit, and the stock-flow adjustment increase the public debt ratio. By contrast, real GDP growth, inflation, and the primary surplus reduce the public debt ratio. In general, fiscal space is greater the smaller the difference between the interest rate and the growth rate ($r - g$).

The primary balance relative to GDP is calculated as follows:

$$PB_t = SPB_t + CYC_t + \Delta PROP_t - \Delta CoA_t \quad (3)$$

where SPB is the structural primary balance relative to GDP, CYC is the cyclical component relative to GDP, $PROP$ is property income relative to GDP, and CoA is ageing costs relative to GDP. The structural primary balance is an estimate of the public primary balance when actual GDP is at its potential level.

The cyclical component is obtained by multiplying the output gap by the semi-elasticity of the budget balance with respect to output:

$$CYC_t = OG_t \cdot \varepsilon \quad (4)$$

where OG is the output gap and ε is the semi-elasticity of the budget balance with respect to output. In its DSA calculations for Finland, the EC (2024b, 2025b) applies a semi-elasticity of 0.582, based on Mourre, Poissonnier and Lausegger (2019). By contrast, the MoF does not account for changes in the cyclical component in its national calculations.

Public expenditure is a component of GDP and indirectly affects other components of GDP, which is why fiscal consolidation has multiplier effects on GDP. Assuming that consolidation begins in year t , the multiplier effect (M) in year t is calculated as follows:

$$M_t = m \cdot (\Delta SPB_{AC,t} - \Delta SPB_{BL,t}) \quad (5)$$

where m is the fiscal multiplier, SPB_{AC} is the structural primary balance after consolidation (AC), and SPB_{BL} is the structural primary balance in the absence of fiscal policy changes, that is, in the baseline scenario (BL). The difference between the change in the post-consolidation structural primary balance and the change in the baseline structural primary balance ($\Delta SPB_{AC} - \Delta SPB_{BL}$) equals the size of fiscal consolidation.

The EC assumes that the multiplier effect directly affects the output gap:

$$OG_{AC,t} = OG_{BL,t} - M_t \quad (6)$$

where OG_{AC} is the output gap after consolidation and OG_{BL} is the output gap in the baseline scenario. The level and growth rate of real GDP after consolidation are calculated through the post-consolidation output gap. The EC assumes that the multiplier effect lasts for another two years after the consolidation period has ended.

By contrast, the MoF (2025a, p. 86) assumes that consolidation immediately weakens real GDP growth in the consolidation year t :

$$y_{AC,t} = y_{BL,t} - M_t \quad (7)$$

where y_{AC} is real GDP growth after consolidation and y_{BL} is real GDP growth in the baseline scenario. Once consolidation ends, real GDP growth returns to its baseline path, leaving a permanent level loss in real GDP.

This year, the EC (2026b, pp. 54–56) lowered the fiscal multiplier used in its DSA model from 0.75 to 0.6. In its national calculations, by contrast, the MoF (2025a, p. 86) assumes a fiscal multiplier of 0.5.

4.2 Simulation scenarios

Finland’s consolidation requirements should be determined solely by EU fiscal rules until 2033, while the debt target set by the debt brake should become binding for the first time in 2034–41 (FinGov 2026, p. 19). However, calculating the consolidation path first on the basis of EU rules for 2027–33 and then on the basis of the debt brake for 2034–41 would involve so much uncertainty that the results would not be particularly informative. Moreover, the debt brake already appears to be influencing actual consolidation recommendations: in February 2026, the new parliamentary working group on fiscal policy recommended consolidation of €8–11 billion for the next parliamentary term, exceeding what is required under EU rules (EC 2026b, p. 112; FinGov 2026, p. 83). For these reasons, this article assumes a hypothetical scenario in which fiscal policy is calibrated during the next parliamentary term so that the debt target set by the debt brake must be met in 2032–39.

The MoF consolidation scenario applies the same assumptions as the MoF uses in its national calculations. The fiscal multiplier is set at 0.5. Consolidation reduces real GDP growth only

once, in the year in which it is implemented, thereby leaving a permanent level loss in real GDP. Changes in the cyclical component, such as unemployment benefit payments, are not taken into account.

The first alternative scenario (A1) examines how the consolidation recommendation derived from the MoF scenario may affect the Finnish economy if consolidation is implemented mainly through spending cuts during a recession or under conditions of weak growth.¹⁷ In this scenario, the multiplier effect is expressed as a range: at the lower bound, the multiplier is 1.15 and the effect fades out within three years; at the upper bound, the multiplier is 1.69 and the effect fades out linearly over seven years. On average, the fiscal multiplier is 1.42 and consolidation affects the economy for five years.

The lower and upper bounds are based on Holter and Ferreira (2024), who estimate Finland's fiscal multiplier to lie between 1.15 and 1.69. The duration of the multiplier effect is based on the EC's DSA and medium-term forecasts, where the output gap is assumed to close in three years at the earliest, typically in five years, and at most in seven years (Heimberger *et al.* 2024; Mc Morrow, Röger and Vandermeulen 2017). In this scenario, the multiplier effect in year t is calculated as follows:

$$M_{A1,t} = m \cdot \sum_{i=0}^{P-1} \left[(\Delta SPB_{AC,t-i} - \Delta SPB_{BL,t-i}) \cdot \frac{P-i}{P} \right] \quad (8)$$

where i is the distance of the consolidation year from year t and P is the duration of the multiplier effect in years.¹⁸ The multiplier effect affects the output gap directly and real GDP growth indirectly, as in Equation (6). In addition, changes in the cyclical component are taken into account in this and all subsequent alternative scenarios, as in Equation (4).

In the second alternative scenario (A2), spending cuts are assumed to have a hysteresis effect on the level of real GDP. Consolidation affects the output gap only in the year in which it is implemented – that is, $P = 1$ in Equation (8) – and reduces potential real GDP growth only in the first post-consolidation year ($t + 1$ when t is the consolidation year):

$$y_{P,A2,t+1} = y_{P,BL,t+1} - M_t \cdot \varphi \quad (9)$$

where $y_{P,A2}$ is potential real GDP growth after consolidation, $y_{P,BL}$ is potential real GDP growth in the baseline scenario, and φ is the hysteresis parameter.

¹⁷Although the MoF has stated that it does not favour spending cuts over tax increases (Toivonen and Lindholm 2026), it has repeatedly framed future consolidation primarily in terms of expenditure cuts. For example, Mika Niemelä, Director General of the Budget Department, attracted considerable attention this spring by posing with a chainsaw while calling for cuts to public spending (Lyytinen and Salminen 2026). Similarly, Permanent Secretary Juha Majanen suggested in early 2025 that the current government cut taxes on high earners and corporations by around €2.5 billion, while at the same time advocating spending cuts to reduce the deficit (Luukka 2025, pp. 149–150).

¹⁸For example, when $i = 0$, the consolidation measure is implemented in year t , so $\frac{P-i}{P} = 1$ and the full amount of the measure is included in the multiplier effect. When $i = 1$, the measure was implemented in year $t - 1$, so only $\frac{P-1}{P}$ of that measure is included in the multiplier effect in year t .

Rawdanowicz *et al.* (2014) estimate Finland’s hysteresis parameter at 50 percent. Lainà (2021, 2025) operationalises this estimate such that a -1.0 percent output gap in a given year reduces potential growth by 0.5 percentage points in the following year. In his sensitivity analysis, Lainà (2021, 2025) assumes a hysteresis-parameter range of 30–60 percent, also based on the findings of Rawdanowicz *et al.* (2014).

I use the same values for the hysteresis parameter and operationalise it in the same way as Lainà (2021, 2025). Hysteresis is calculated only for the direct effect of consolidation on the output gap. An alternative approach would also account for the output gap inherited from the years preceding the consolidation period, in which case the negative hysteresis effect of consolidation would be larger. In this scenario, I use an average fiscal multiplier of 1.42 and an average hysteresis parameter of 50 percent. At the lower bound of the range, the fiscal multiplier is 1.15 and the hysteresis parameter is 30 percent; at the upper bound, the multiplier is 1.69 and the hysteresis parameter is 60 percent.

In the third alternative scenario (A3), spending cuts are assumed to reduce the level of potential real GDP in every year after consolidation. As a result, consolidation weakens potential growth over a prolonged period. Such a hysteresis effect may extend to real GDP growth especially if structural unemployment rises significantly, or if firms’ expectations deteriorate persistently and private investment falls relative to its pre-shock level. In this scenario, potential real GDP after consolidation in year t is calculated as follows:

$$\forall n \in \mathbb{Z}_+ : \quad Y_{P,A3new,t+n} = Y_{P,t+n} - M_t \cdot \tilde{Y}_{P,t} \cdot \varphi \quad (10)$$

where $Y_{P,A3new}$ is potential real GDP after consolidation and:

$$\tilde{Y}_P = \begin{cases} Y_{P,BL}, & \text{if } t \text{ is the first consolidation year of the adjustment period,} \\ Y_{P,A3}, & \text{otherwise.} \end{cases} \quad (11)$$

where $Y_{P,BL}$ is potential real GDP in the baseline scenario and $Y_{P,A3}$ is potential real GDP in the A3 scenario before the consolidation measure implemented in year t , but after any previous consolidation measures.

By studying forecast errors, Fatás and Summers (2018, p. 245; see also Blanchard and Leigh 2013) estimate that fiscal consolidation implemented in the euro area in 2010–11, which reduced real GDP by one percent in the consolidation year, reduced real GDP by 1.3 percent in 2015 and by 2.1 percent in 2021. Gechert, Horn and Paetz (2019, p. 11) find the same hysteresis effect in the euro area over the period 2010–15. When the hysteresis observed in these studies is converted into annual effects, the result is that, in the years following consolidation, the hysteresis effect averaged approximately 17.5 percent of the first-year negative effect. In addition, a 95 percent confidence interval can be calculated for the annual effect derived from Fatás and Summers (2018), amounting to approximately 8.4–26.6 percent.

I construct the range for the fiscal multiplier effect based on the findings of Holter and Ferreira (2024), Fatás and Summers (2018), and Gechert, Horn and Paetz (2019). The lower

bound combines a fiscal multiplier of 1.15 with a hysteresis parameter of 8.4 percent, while the upper bound combines a multiplier of 1.69 with a hysteresis parameter of 26.6 percent. On average, the fiscal multiplier is 1.42 and the hysteresis parameter is 17.5 percent.

In the tax scenario (A4), the fiscal multiplier for tax changes is 0.75 and the multiplier effect fades out over three years, that is, $P = 3$ in Equation (8). The multiplier effect of tax increases is roughly equal to the multiplier effect of all fiscal policy measures in the EC’s earlier DSA calculations (see Heimberger *et al.* 2024).

In addition, I assume that tax measures do not affect potential GDP. This assumption is plausible especially if tax increases are targeted at tax bases that minimise adverse effects on economic growth. On the other hand, the two-year cumulative tax multiplier used here is approximately twice as large as the tax multiplier found in the meta-study by Gechert and Rannenberg (2018), meaning that the demand effect of taxation is taken into account as larger than average.

In the tax and investment scenario (A5), the multiplier effect of tax measures is the same as in the previous scenario. For public investment, I use a fiscal multiplier of 2.0 and a hysteresis parameter of 26.6 percent. A multiplier of 2.0 is realistic under conditions of weak growth and economic uncertainty, especially if part of public investment is channelled into R&D expenditure (Ciaffi, Deleidi and Mazzucato 2024; Fournier 2016; Goemans 2023). Lainà (2021, 2025) also uses a multiplier of 2.0 in his calculations for Finland.

The hysteresis parameter of 26.6 percent, in turn, corresponds to the upper bound of the 95 percent confidence interval derived from the hysteresis effect estimated by Fatás and Summers (2018). This assumption can be considered plausible because public investment tends to have larger and more persistent effects than other types of fiscal policy measures. In other words, I assume that public investment has a positive hysteresis effect on potential real GDP growth in every year following the stimulus.

Table 2: Assumptions underlying each simulation scenario.

Scenario	Cyclical component	Impact multiplier	Multiplier persistence	Hysteresis parameter	Hysteresis affects
MoF consolidation	No	0.5	–	100%	Level of potential GDP
Higher multiplier (A1)	Yes	1.15–1.69	3–7 years	–	–
Level hysteresis (A2)	Yes	1.15–1.69	–	30–60%	Level of potential GDP
Growth hysteresis (A3)	Yes	1.15–1.69	–	8.4–26.6%	Potential GDP growth
Tax (A4)	Yes	0.75	3 years	–	–
Tax and investment (A5)	Yes	0.75 for T ; 2.0 for I	3 years for T	26.6% for I	Potential GDP growth for I

Notes: T denotes taxes and I denotes investment.

A fiscal multiplier of 2.0 combined with a hysteresis parameter of 26.6 percent corresponds to

a two-year cumulative multiplier of 2.5. This assumption is broadly consistent with the meta-study by Gechert and Rannenberg (2018), which estimates the average two-year cumulative multiplier for public investment under conditions of weak growth at 2.3.

Table 2 summarises the assumptions underlying the different scenarios.

4.3 Data

Most statistical data up to 2027 are taken from the EC’s (2025a) AMECO database, retrieved on 26 November 2025. From 2028 onwards, the endogenous variables are projected within the model.

Until 2027, data on the public debt ratio, real GDP, potential GDP, the output gap, the primary balance, the structural primary balance, the GDP deflator at 2020 prices, the implicit interest rate on public debt, and the stock-flow adjustment are obtained from the AMECO database.

From 2028 onwards, the structural primary balance is assumed to remain at its 2027 level without changes in fiscal policy. This constitutes the baseline scenario.

Inflation is assumed to settle at 2 percent from 2028 onwards. The implicit interest rate on public debt is assumed to increase over 2028–39 at the same pace as in the EC’s (2025b) DSA calculations.

Over 2028–39, potential GDP growth, property income, and ageing costs are based on the projections in the EC’s (2023, 2024a) Ageing Report.

From 2028 onwards, the stock-flow adjustment is assumed to equal the financial balance of the pension system, projected in the EC’s (2023, 2024a) Ageing Report. The effect of pension surpluses on the public debt ratio is fully offset through the stock-flow adjustment for the first ten years, after which the stock-flow adjustment is phased out linearly over the following ten years.

5 Simulation results

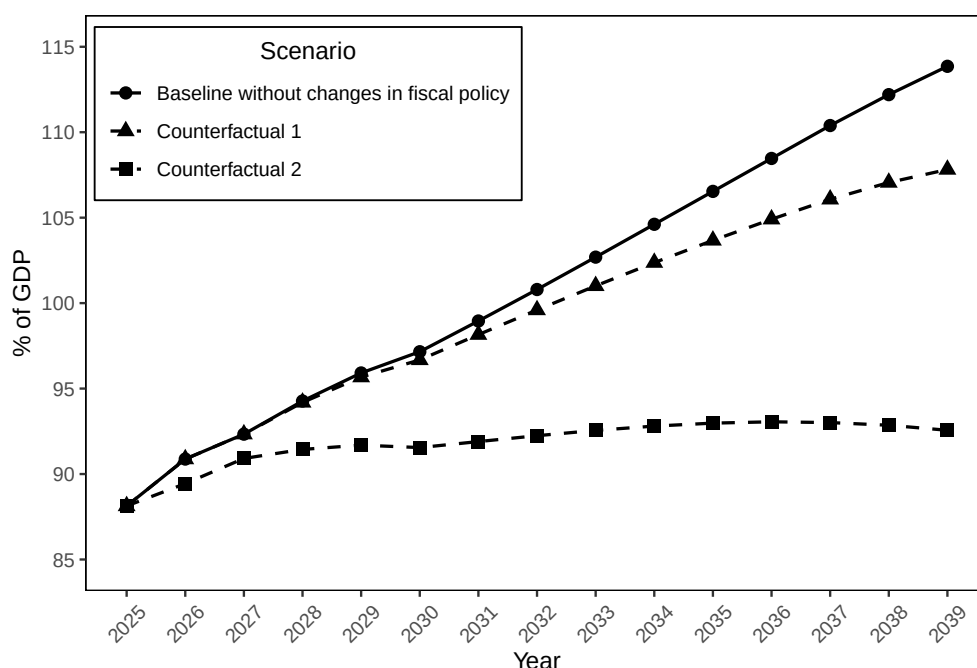
5.1 Baseline scenario

Figure 3 presents a projection of Finland’s public debt ratio for 2025–39. According to the projection, the public debt ratio rises from 88 percent to 114 percent by 2039, assuming no changes in fiscal policy. This is shown by the line labelled “Baseline without changes in fiscal policy.”

Finland’s public debt ratio rises in the projection for two reasons (Kyörönen 2025, pp. 139–141). First, the interest rate increases initiated by the ECB in 2022 raise the implicit interest rate on Finland’s public debt, as low-interest bonds are gradually replaced by bonds with higher interest rates. In Figure 3, the line labelled “Counterfactual 1” shows how Finland’s debt ratio would evolve if the implicit interest rate were to remain at its 2027 level over

2028–39. Under this assumption, the debt ratio would be about 7 percentage points lower in 2039.

Second, in 2024 the EC changed its methodology for projecting Finland’s public debt ratio. Following this change, the EC no longer treats the surpluses of public pension funds as revenue that can be used to reduce public debt. In Figure 3, the line labelled “Counterfactual 2” shows how the debt ratio would evolve if these surpluses were treated according to the previous methodology and if the implicit interest rate on public debt remained at its 2027 level. Under these assumptions, Finland’s public debt ratio would not increase over 2028–39, and the fiscal adjustment required by EU fiscal rules would be considerably smaller. In other words, the technical change concerning the treatment of public pension funds’ surpluses is the single most important reason why the EC projects Finland’s debt ratio to rise and requires substantial consolidation measures.



Sources: EC (2023; 2024a; 2024b; 2025a; 2025b); own calculations.

Figure 3: Public debt ratio, Finland, 2025–39.

5.2 MoF consolidation scenario

Using the MoF’s assumptions, the adjustment required by the debt brake amounts to a nominal €9.7 billion over 2028–31 for the public debt ratio to decline by an average of 0.75 percentage points per year over 2032–39. At 2020 prices, the adjustment amounts to €7.8 billion. For comparison, Finland’s central government appropriations are estimated at a nominal €90.8 billion in 2026 (MoF 2025b).

In Figure 4, the line labelled “MoF consolidation scenario” shows how the public debt ratio and real GDP respond to consolidation under the MoF’s assumptions. Consolidation puts the

debt ratio on a declining path from 2030 onwards. Although the level of real GDP declines and remains €4.3 billion lower in 2039, the effect on real GDP growth is only temporary. In other words, once consolidation has ended, the actual growth rate converges to the potential growth rate.

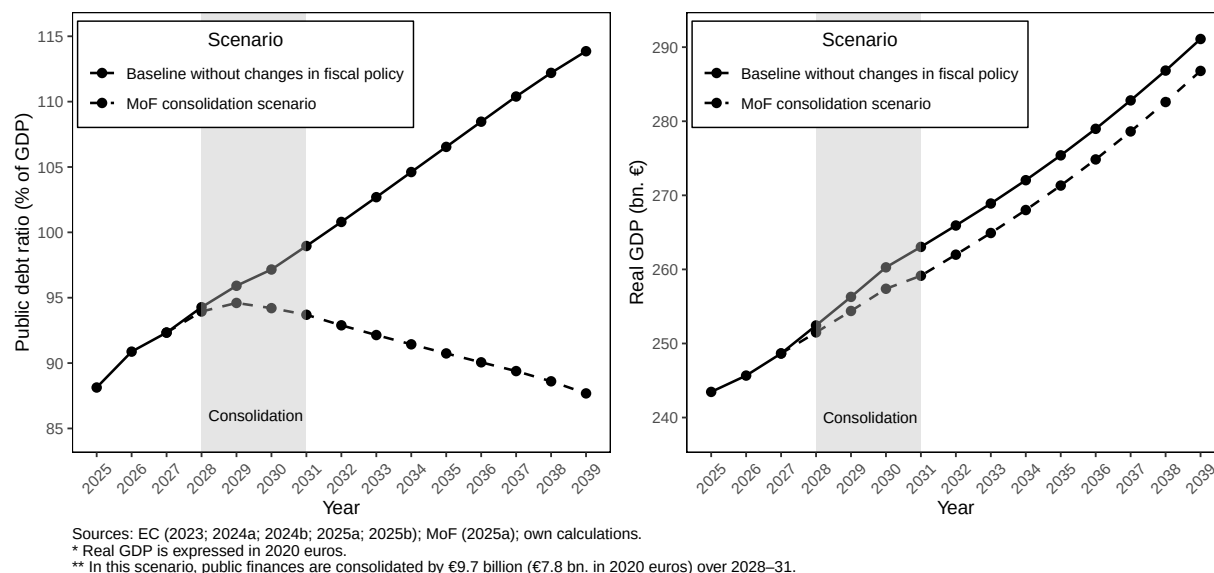


Figure 4: Public debt ratio and real GDP, MoF consolidation scenario, Finland, 2025–39.

5.3 Alternative multiplier and hysteresis scenarios

I next examine the effects of the consolidation recommendation derived from the MoF's assumptions (€9.7 bn.) on the public debt ratio and real GDP. In these calculations, changes in the cyclical component are taken into account, and consolidation is assumed to consist mainly of spending cuts implemented under conditions of weak economic growth.

In the A1 scenario, shown in Figure 5, the multiplier for spending cuts is assumed to be larger (1.15–1.69), and the multiplier effect is assumed to be more persistent (3–7 years). Spending cuts increase the public debt ratio substantially until the end of the consolidation period and put it on a declining path only with a considerable delay. At the upper bound of the range, the debt ratio in 2034 is no lower than it would have been without consolidation.

The right-hand panel of Figure 5 shows that consolidation reduces real GDP until the end of the next parliamentary term. In the worst case scenario, real GDP barely grows over 2028–31. Eventually, however, growth resumes and the debt ratio turns onto a declining path, because spending cuts are assumed to have no hysteresis effect on potential output.

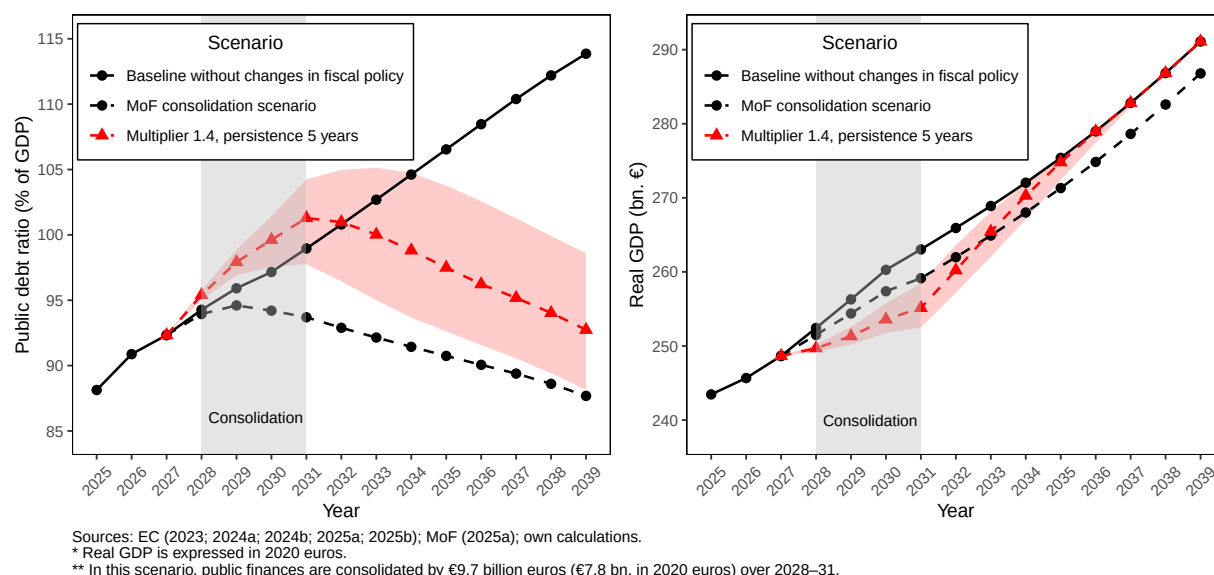


Figure 5: Public debt ratio and real GDP, consolidation scenario with a larger multiplier effect and a changing cyclical component, Finland, 2025–39.

Figure 6 shows the effects of spending cuts in the A2 scenario, in which consolidation is assumed to have a hysteresis effect on the level of real GDP. The public debt ratio rises until the end of the next parliamentary term before turning onto a declining path. The level of real GDP is permanently reduced by €3.0 billion in the best case scenario and by €8.8 billion in the worst case scenario, at 2020 prices.

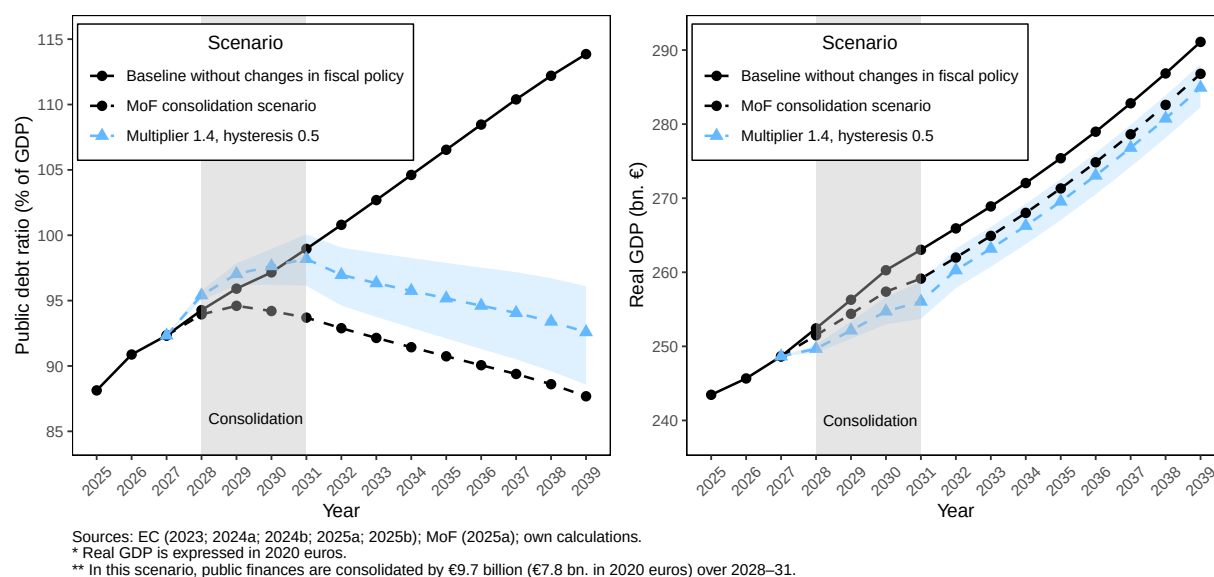


Figure 6: Public debt ratio and real GDP, consolidation scenario with a larger multiplier effect, a changing cyclical component and a level hysteresis effect, Finland, 2025–39.

In the A2 scenario, the debt ratio evolves more favourably during the consolidation period than in the A1 scenario. This difference is largely explained by the cyclical component. The larger the output gap, the higher the cyclical component. When hysteresis is taken into account in the A2 scenario, consolidation reduces potential GDP, thereby narrowing the output gap and lowering the cyclical component. At the same time, however, the economic losses are larger and more persistent.

In other words, the A1 scenario, shown in Figure 5, mainly captures short- and medium-term effects, whereas the A2 scenario, shown in Figure 6, mainly captures long-term effects. Neither scenario necessarily provides a fully realistic picture of both the short- and medium-term effects and the long-term effects.

Figure 7 shows the effects of consolidation in the A3 scenario, in which spending cuts are assumed to reduce the level of potential GDP in every year following consolidation, thereby weakening potential growth over a prolonged period. At the lower bound of the range, the public debt ratio and real GDP evolve slightly less favourably than in the scenario based on the MoF's assumptions. At the upper bound, by contrast, the debt ratio rises to 115.3 percent by 2039, while real GDP stops growing. On average, the debt ratio is 100.9 percent in 2039 and does not turn onto a declining path even in the long run. In addition, consolidation reduces real GDP by €19.6 billion – or 6.7 percent – by 2039.

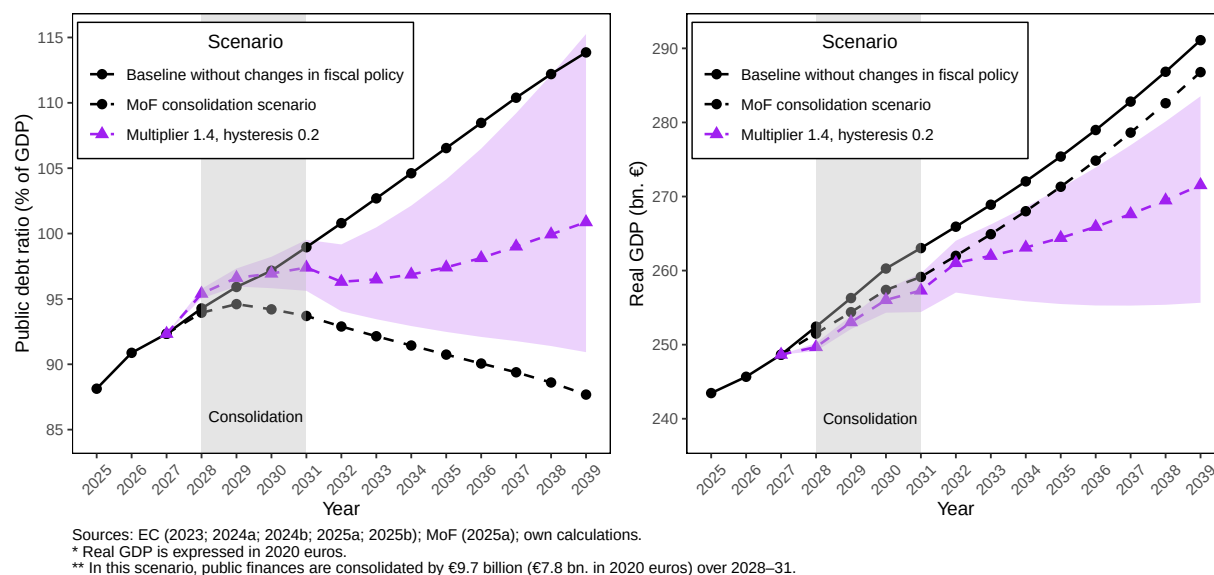


Figure 7: Public debt ratio and real GDP, consolidation scenario with a larger multiplier effect, a changing cyclical component and a growth hysteresis effect, Finland, 2025–39.

5.4 Alternative tax and investment scenarios

In the A4 scenario, the public debt ratio declines by an average of 0.75 percentage points per year over 2032–39 if taxation is tightened by a nominal €8.4 billion (€6.8 billion at 2020

prices) over 2028–31. The left-hand panel of Figure 8 shows that public finances begin to strengthen from 2031 onwards. By 2039, the debt ratio has fallen to 90.0 percent, after declining by an average of 0.75 percentage points per year over 2032–39.

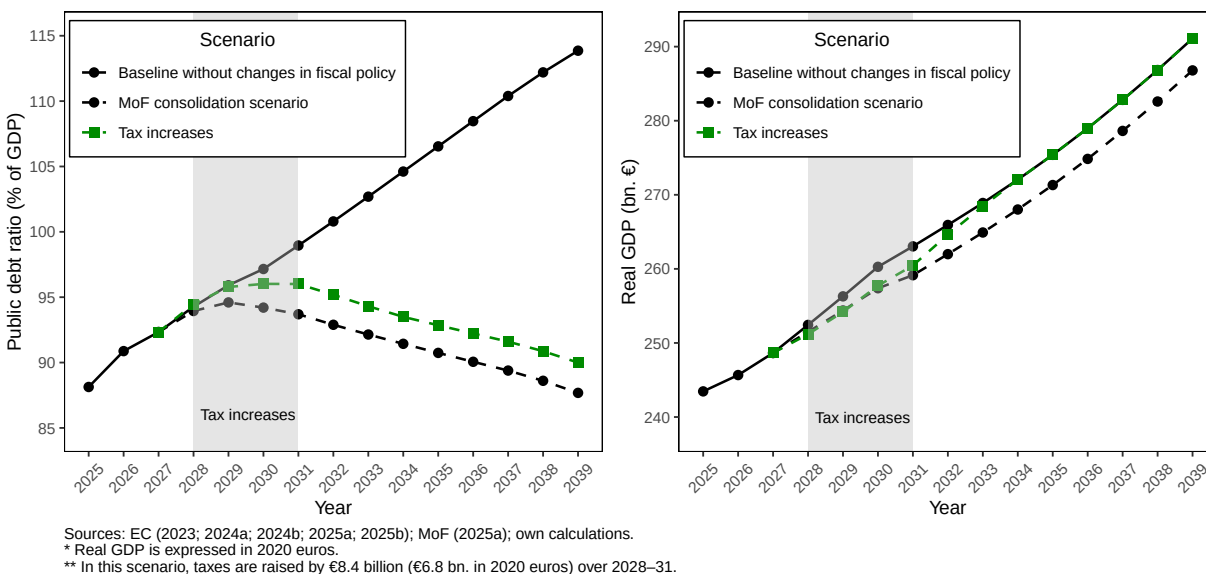


Figure 8: Public debt ratio and real GDP, tax scenario, Finland, 2025–39.

The right-hand panel of Figure 8 shows that tax increases reduce real GDP over 2028–33. Until 2030, GDP evolves almost identically to the MoF consolidation scenario, but by 2034 it has returned to its potential level.

I next estimate how much taxation would need to be tightened and public investment increased in the A5 scenario for the public debt ratio to decline by an average of 0.75 percentage points per year over 2032–39. According to my calculations, several combinations of tax increases and higher public investment would reduce the public debt ratio by the amount required by the debt brake. One realistic option is to tighten taxation by a nominal €8.1 billion and increase public investment by €5.1 billion over 2028–31. At 2020 prices, these amounts correspond to €6.5 billion in tax increases and €4.1 billion in higher public investment.

The effects of this proposal are shown in Figure 9. The left-hand panel shows that tax increases and higher public investment put the public debt ratio on a declining path from 2033 onwards. Over 2032–39, the debt ratio declines by an average of 0.75 percentage points per year, reaching 89.1 percent by 2039.

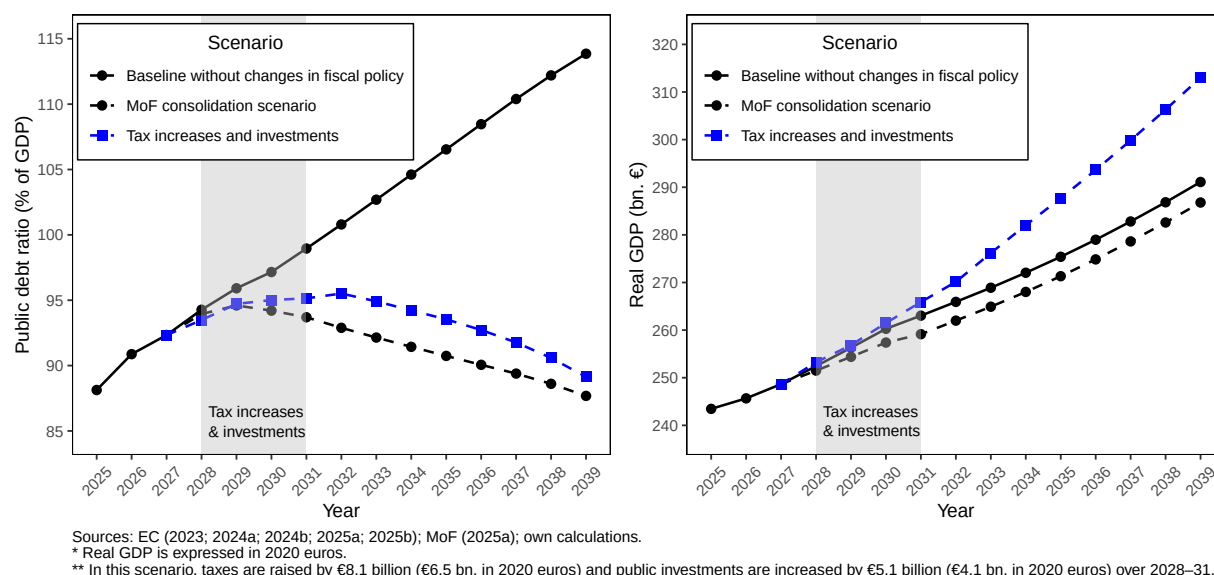


Figure 9: Public debt ratio and real GDP, tax and investment scenario, Finland, 2025–39.

The right-hand panel of Figure 9 shows that, as a result of higher public investment, real GDP grows faster than in the absence of fiscal policy measures. Economic growth accelerates to an average of 2.1 percent per year over 2032–39, leaving real GDP €21.9 billion – or 7.5 percent – higher in 2039, at 2020 prices. Thus, the debt ratio declines while the economy expands and real incomes rise.

6 Discussion

With the exception of the treatment of the cyclical component, the assumptions underlying the MoF’s consolidation calculations can be regarded as broadly consistent with the research literature when consolidation is implemented during an upswing or under conditions of strong economic growth. By contrast, when consolidation consists primarily of spending cuts and is implemented under conditions of weak growth, recommendations derived from the MoF’s assumptions may generate unexpectedly large negative multiplier effects on both economic activity and public finances. As discussed in Section 2, Finland’s weak economic performance and repeated consolidation measures after the financial crisis provide historical evidence that this risk can materialise.

As shown in Section 5, in each alternative scenario, spending cuts raise the public debt ratio considerably above the level implied by the MoF consolidation scenario during the consolidation period. In the worst case, this may have highly adverse consequences for Finland’s public finances. If the MoF assumes that consolidation affects the public debt ratio in line with its calculations, it may recommend further consolidation measures whenever the debt ratio develops less favourably than projected. As a result of these additional spending cuts, the debt ratio may again rise more than the MoF expects, prompting further recommenda-

tions for consolidation. This may give rise to a vicious circle of consolidation, weak economic growth, and a higher debt ratio.

Even if such a vicious circle does not emerge, the MoF’s consolidation recommendations may, through growth hysteresis, weaken economic growth to such an extent that the public debt ratio does not turn onto a declining path by 2039. When the calculations apply the hysteresis parameter derived from Fatás and Summers (2018), the economy grows by an average of only 0.7 percent per year over 2032–39. In this case, the 2030s would become Finland’s third consecutive lost decade.

These risks could be avoided if the MoF were to calibrate the parameters of its consolidation calculations more carefully according to, among other things, the type of fiscal policy measure, the cyclical position of the economy, and the structure of aggregate demand. EU rules do not prevent the MoF from using alternative parameters, as noted in the EC’s (2026b, p. 55) latest debt sustainability report.

A key question is what kinds of tax measures could produce the results shown in Figure 8. The purpose of this article is not to propose a concrete tax reform, but one possible example is the tax package proposed by Lainà (2024), which would raise a nominal €8.8 billion – €0.4 billion more than in the calculation shown in Figure 8. Only around €7 billion of the tax measures proposed by Lainà (2024) would need to be implemented if the tax cuts adopted by the Orpo government in 2025 were reversed. At the 2025 mid-term policy session, the government decided to reduce the top marginal tax rates from around 60 percent to 52 percent in 2026 and the statutory corporate tax rate from 20 percent to 18 percent in 2027. Neither measure is likely to increase economic growth in Finland: reducing the top marginal tax rates affects only a few percent of wage earners (see Finér and Systä 2025), while the research literature suggests that changes in the corporate tax rate have no significant effect on economic growth (Gechert and Heimberger 2022; Harju, Koivisto and Matikka 2022, 2024). Moreover, these tax cuts mainly increase the net incomes of high-income earners (Finér and Systä 2025; Heino 2024), which does little to stimulate aggregate demand, since the marginal propensity to consume is typically relatively low among high-income households (Albuquerque and Green 2023; Fisher *et al.* 2020).

Is an annual increase in public investment of €4.1 billion, measured at 2020 prices, a realistic scenario for Finland? Figure 10 shows that real investment in Finland has barely grown since the financial crisis. If real investment had continued to follow its trend from the 1990s and 2000s during the 2010s and 2020s, real investment would have been approximately €34.7 billion higher in 2024. From this perspective, a €4.1 billion increase in real public investment does not appear excessive.

In 2024, former ECB President Mario Draghi (2024) prepared a report for the EC on the future of European competitiveness. According to the report, the EU needs an additional €750–800 billion in annual investment to remain competitive, corresponding to around 4.4–4.7 percent of EU GDP in 2023. An increase in public investment of €4.1 billion, at 2020 prices, corresponds to around 1.7 percent of Finland’s real GDP in 2023. If, following Matvejevs and Tkačevs (2023), public investment is assumed to crowd in private investment by a factor of two, a €4.1 billion increase in public investment would raise total investment in Finland by around 5.1 percent relative to 2023 GDP. Thus, the investment increase consid-

ered here would be broadly in line with the scale of additional investment called for in the Draghi report.¹⁹

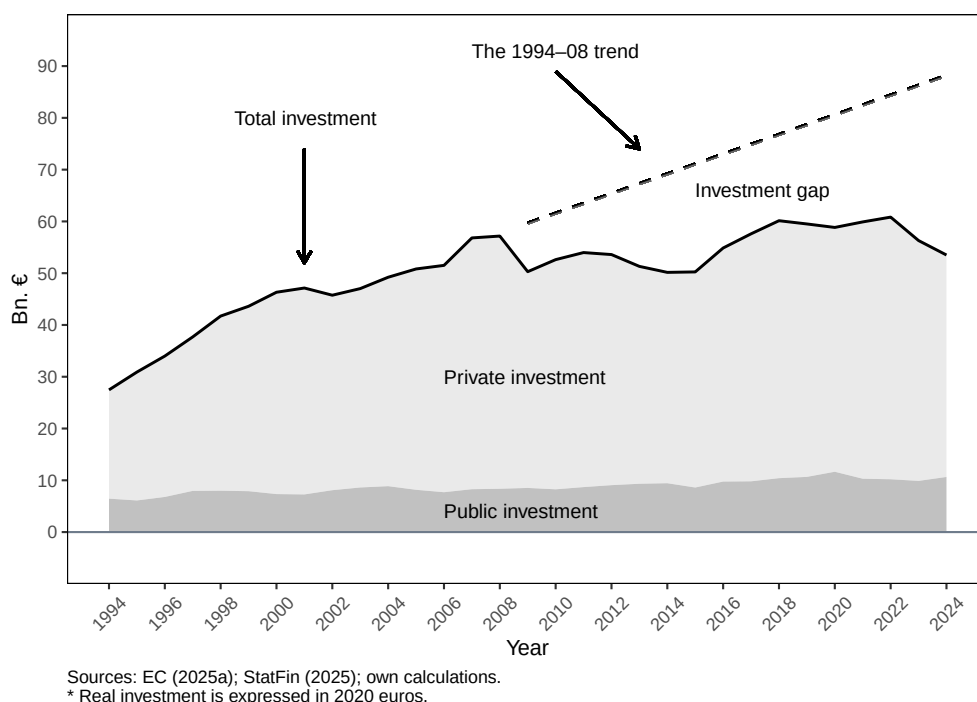


Figure 10: Real investment, Finland, 1994–24.

Finally, I emphasise that this article does not claim that spending cuts, tax increases, and public investment would affect Finland’s economic growth and public finances exactly as in the simulations presented above. The parameters used in the calculations are drawn from specific studies, and the results would change if different parameter values were applied. Rather, the simulations illustrate how the public debt ratio and real GDP would be likely to evolve if fiscal multiplier and hysteresis effects were, on average, consistent with the studies used in this article.

7 Conclusion

The new debt brake requires Finland to undertake significant consolidation measures in the future. This involves risks, in particular because the DSA calculations on which the debt brake’s implementation is based do not realistically account for the negative multiplier effects that cuts to public expenditure may have under conditions of weak economic growth.

¹⁹A recent Sitra memorandum by Alaja *et al.* (2026) applies complexity economics to examine which industries are most promising for Finnish goods exports. Alaja *et al.* (2026) find that Finland’s most promising growth sectors are in chemicals, metal products, mechanical engineering, optical instruments, and measurement technologies. These industries could plausibly be supported through public investment in Finland.

As shown above in Figures 5, 6 and 7, spending cuts may raise the public debt ratio during the next parliamentary term above the level implied by the MoF's consolidation calculations. This may in turn give rise to a vicious circle of consolidation, weak economic growth, and a higher debt ratio in Finland, undermining the conditions for growth and weakening public finances further. A similar dynamic has been observable during the parliamentary term that began in 2023.

Even if no such vicious circle emerges, the consolidation recommendation for the next parliamentary term derived from the MoF's assumptions – estimated at €9.7 billion – may weaken economic growth in Finland so substantially that economic stagnation continues and the public debt ratio remains on an upward path. This risk is credible, given that economic growth in Finland has been weak since the financial crisis.

Instead of relying on spending cuts, Finland could strengthen its public finances sustainably by increasing taxes and public investment. Even under conditions of weak growth, the targets set by the debt brake could be achieved over 2032–39 if taxation were tightened by a nominal €8.4 billion during the next parliamentary term. Tax increases should be targeted in ways that weaken aggregate demand as little as possible.

If fiscal rules are also interpreted as allowing public finances to be strengthened through public investment, the debt ratio could be put on a declining path by tightening taxation by €8.1 billion and increasing public investment by €5.1 billion. This would be the best option for the Finnish economy, as public investment would accelerate economic growth and increase employment, thereby improving real incomes and living standards.

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