



The Estonian Economy and Monetary Policy is an Eesti Pank review released four times a year that summarises the main recent events in the global and Estonian economies. Twice a year, in June and December, the review also contains a full forecast for the Estonian economy, while in March and September a brief forecast update is included.

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CONTENTS

INTRODUCTION	4
THE EXTERNAL ENVIRONMENT	5
THE GLOBAL ECONOMY	5
THE EURO AREA	7
Box 1. Economic activity in the euro area	8
Box 2: The euro area's monetary policy environment	9
ESTONIA'S MAIN TRADING PARTNERS	11
THE ESTONIAN ECONOMIC ENVIRONMENT	13
ECONOMIC ACTIVITY	13
DOMESTIC DEMAND	15
EXTERNAL BALANCE AND COMPETITIVENESS	16
Box 3: Changes in the structure of exports are contributing to strong growth	17
THE LABOUR MARKET	19
Box 4: Short-term employment in Estonia	21
PRICES	23
GOVERNMENT FINANCES	23
ECONOMIC FORECAST 2018-2021	25
THE INTERNATIONAL ECONOMIC ENVIRONMENT	25
ECONOMIC ACTIVITY	26
DOMESTIC DEMAND	26
EXTERNAL BALANCE AND COMPETITIVENESS	29
PRICES	31
Box 5: Estonia's equilibrium inflation rate	32
Box 6: The impact of the reference base effect on inflation	33
GOVERNMENT FINANCES	35

INTRODUCTION

The global economy has continued to soften in the first half of this year. Disputes around international trade and the introduction of trade barriers have reduced the options for exporting, making countries ever more dependent on domestic markets. In many cases this has left the options for growth more restricted. The uncertainty has also made companies more cautious about the future and more fearful of an unexpected worsening of trade conflicts. An increase in tensions in the Middle East is also considered very possible, with a consequent rise in the oil price. The postponement of Brexit has left unanswered the question of the departure of the United Kingdom from the European Union, and its future form and the economic impact it will have on the countries of Europe remains unclear.

More modest growth in the larger economic regions, which includes the weakness that has hit European countries, is one of the reasons why the deceleration in economic growth that started in Estonia in 2017 has continued. Together with this the labour market will calm down, as demand for the output of companies will in future increase at a slower rate in Estonia and in the main export markets, and the business sector will not want to employ as many workers as in previous years.

The expectations of companies for employment are already down, and it is probable that this will continue further.

Estonian resident employees will not feel the cooling of the labour market very sharply, because companies will first reduce their employment of temporary labour from abroad, which has grown strongly in recent years. Employment will remain almost unchanged for local residents in the coming years, but unemployment will increase a little because of more active participation in the labour market, one cause of which is the rise in the retirement age and the widening gap between pensions and wage income, which is also encouraging people to remain in work for longer.

Although the economy is not doing as well as in recent years, it will continue to do better than usual in the coming years. The average wage level will exceed its long-term trend, and unemployment will remain very low despite rising slightly. This is reflected in consumption and in the tax receipts of the state, both of which are inflated because of the favourable conditions. Running a budget deficit at this time will cause inflation to rise, reducing competitiveness and so harming the outlook for growth in the economy.

THE EXTERNAL ENVIRONMENT

THE GLOBAL ECONOMY

Growth in the global economy is being hindered by trade disputes. The trade disputes between the US and China culminated in the US imposing higher customs tariffs, rather than in the agreement that was expected¹. China responded with its own measures, after which the US promised to introduce higher tariffs on all other Chinese goods as well. Unfortunately there has been no improvement in recent months in several macroeconomic indicators such as industrial output growth or export orders. The weakening of the composite index for global economic activity² in May is not promising either. This means that global economic growth will in future be supported primarily by domestic demand within countries. Uncertainty and geopolitical tensions have again increased and the danger looms of a full-blown trade war.

Economic developments have been different in different countries in recent months, and economic activity has increased in several advanced countries. The economies in the US and the euro area grew rapidly in the first quarter, with support from generally strong labour markets, good domestic demand and growth in the service sector in the euro area. These developments partly reflect a calmer time in the global economy in spring when a trade agreement still seemed achievable. Furthermore, the fiscal stimulus to the US economy was only a temporary measure, and weaker foreign demand will start to limit the growth in the US. Growth in the econ-

omy of the United Kingdom picked up in the first quarter, partly because Brexit was postponed until the autumn, but also because of increased government spending and domestic consumption (see Table 1). In the shorter term the political uncertainty caused by national and European Parliament election results will deepen the tensions in Europe, as will the seemingly unending confusion about the final outcome of Brexit. The Japanese economy is also facing trade tensions that have reduced exports of machinery and equipment from Japan to China. Before the rise in VAT³ in October this year, there may be faster growth in domestic consumption, which would compensate a little for the negative impact on the Japanese economy of falling exports.

Slower growth in global trade will push governments to introduce various supportive measures. As trade disputes have become ever more serious, the demand environment has worsened for many countries, and export revenues have fallen. This has pushed countries in many parts of the world to increase their government spending ever further, increasing their already large debt burdens. Global trade tensions and internal imbalances have led several emerging Asian economies to cool down moderately, while internal political arguments and fights have weakened the economies in developing South American countries and also in Turkey for example. Although the Russian economy grew faster than expected at the end of last year on the back of the construction sector and commodities exports, growth has been hindered of late by the rise in VAT at the

Table 1. GDP growth in different regions in 2012 - 2018 (change, %)*

	2013	2014	2015	2016	2017	2018	2018 Q4	2019 Q1	2019
World	3.5	3.6	3.5	3.2	3.8	3.7			3.3
Advanced economies	1.3	2.1	2.3	1.7	2.4	2.4			1.8
Emerging markets and developing economies	5.1	4.7	4.3	4.4	4.7	4.6			4.4
Euro area	-0.2	1.4	1.9	1.8	2.5	1.8	1.2 (0.2)	1.2 (0.4)	1.3
United States	1.8	2.5	2.9	1.6	2.2	2.9	2.9 (0.5)	3.2 (0.8)	2.3
China	7.8	7.3	6.9	6.7	6.9	6.6	6.4 (1.5)	6.4 (1.4)	6.3
Japan	2.0	0.4	1.4	1.0	1.7	0.9	0.2 (0.4)	0.8 (0.5)	1.0
United Kingdom	2.0	2.9	2.3	1.8	1.7	1.3	1.2 (0.2)	1.8 (0.5)	1.2

* GDP at constant prices, quarterly growth over the previous quarter is in brackets, 2019 is WEO forecast
Source: IMF World Economic Outlook Update (April 2019), OECD, Eurostat, National Statistics

1 The justification given was that China had not kept its promises to follow rules protecting intellectual property and to stop devaluing the yuan.

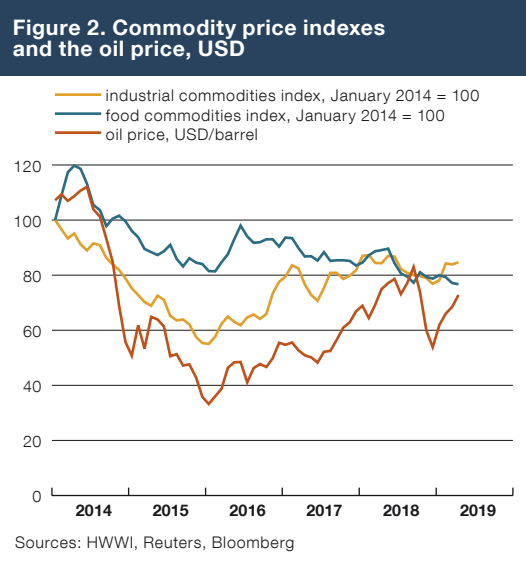
2 JP Morgan, Global Composite PMI.

3 From the current 8% to 10%.

start of the year, falling demand for commodities, and continuing sanctions. The Chinese government has already strongly increased public sector spending⁴ to support the economy, while the central bank has continued to inject liquidity into the market with special lending programmes and has eased credit requirements for banks. Although the Chinese economy still grew quite quickly in the first quarter, growth in investment, industrial output and exports has slowed steadily against the backdrop of more and more new US trade restrictions.

Several central banks have stopped or postponed their tightening of monetary policy. This gave investors a burst of optimism until early May and encouraged risk appetite in financial markets, with the result that US stock markets were up 20% between the start of the year and May (see Figure 1). Companies also surprisingly announced better financial results than expected. Interest rates on long-term sovereign bonds moved in different directions for different countries, but the general direction was upwards. After the decision by the United States on 10 May to raise customs tariffs on Chinese goods⁵, there was quite a sharp fall in financial markets, and volatility returned. Stock markets fell around the world and investors started to sell risky assets. There was a clear preference for safer asset classes, which brought down the interest rates on sovereign bonds and caused the Japanese yen to appreciate. The reaction of investors has so far been less exaggerated than it was in December last year, because it is still possible that China and the US will manage to reach agreement about their points of dispute at the G20 meeting in June. One positive point is that there was no very significant outflow of capital from developing country funds when risk assessments worsened in May.

The oil price has continued to rise on commodities markets. In the middle of May oil climbed to 71 dollars a barrel, though it fell back to 65 dollars a barrel by the end of May due to the rise in uncertainty in the world economy. Supply-side restrictions from OPEC will push the oil price in future, in the same way that re-escalated tensions



between the US and Iran have. The United States wants to close down oil exports from Iran entirely, and this has caused tension in the Persian Gulf region, where oil tankers from several countries have been attacked. The volatility in global financial markets has encouraged the price of gold upwards (see Figure 2). Despite rising fuel prices, inflation in advanced economies has not particularly increased, because it has been held back by low food commodity prices. The strong rise in the oil price has however led to higher inflation in several emerging economies. They also face food price inflation because the spread of swine flu in Africa has raised the price of pork.

⁴ Tax cuts and increased spending on infrastructure.

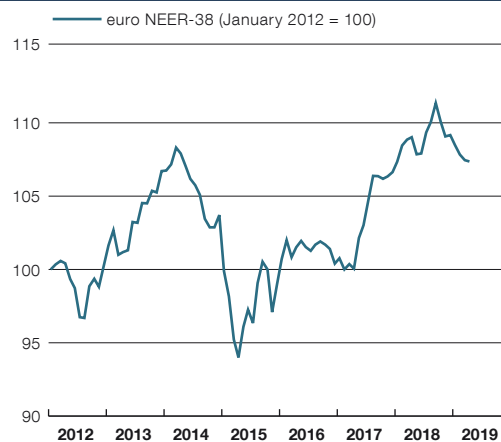
⁵ From 10% to 25% on 200 billion dollars of Chinese goods.

THE EURO AREA

Economic growth in the euro area has picked up. Quarterly growth increased to 0.4% in the first quarter, while yearly growth held steady at 1.2%, but optimism arises from the exit from recession of two of the euro area's larger countries, Germany and Italy⁶, faster growth in Spain, and increased economic activity in France (see Box 1 on economic activity in the euro area). Economic growth in Germany and in several other euro area countries is mainly supported by growth in corporate investment in fixed assets and household spending, while the impact from net exports remains negative. The sectors that are doing best at the moment in the euro area are services and construction, while growth in industrial output continues to struggle. Monthly growth has however accelerated in German industrial output in the past couple of months. This indicates that the German industrial sector might be recovering a little faster than was feared at the start of the year, and that car manufacturing has got over its major dip. Although the US postponed in May the introduction of higher customs rates for cars and parts from Europe for six months, there remains a lot of uncertainty about the longer term.

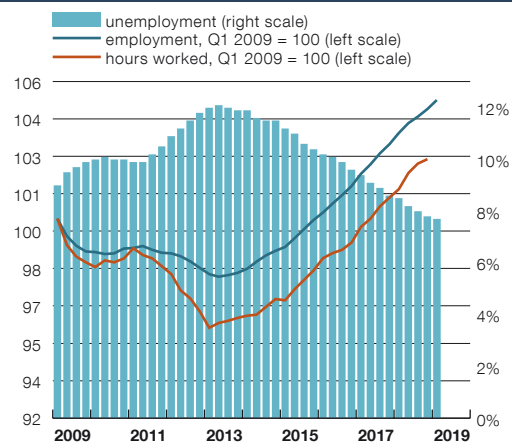
Financing conditions remain favourable in the euro area (see Box 2) and corporate investment is growing. Growth has also been supported by strong domestic demand, which is shown by the substantial increase in retail sales. Confidence at companies is most affected by worries about the risks from the external environment. The overall reduction in global trade caused by the trade conflict between the US and China may for example in future also reduce the incomes of European exporters. The euro exchange rate with main trading partners has depreciated however (see Figure 3), which should offer some alleviation for exporters. The postponement of Brexit is also causing uncertainty. All of this is also in line with the weakening of activity indexes⁷ for the industrial sector in the euro area in May.

Figure 3. Trade-weighted euro exchange rate



Source: European Central Bank

Figure 4. Employment and unemployment in the euro area



Source: Eurostat

The labour market in the euro area remained strong. It has not yet shown any effect from the fall in activity in the industrial sector, which forms around a quarter of the euro area economy. The unemployment rate fell to 7.6% in April, which is its lowest level of the past decade (see Figure 4). Wage growth remains quite fast at 2.3%. The strong labour market is helping to keep consumer confidence in the euro area above its long-term average level. Survey data⁸ in recent months have shown that consumers have become a little more concerned about the performance of the econ-

6 Technically speaking it was only the Italian economy that was in recession as it shrank for two quarters in a row at the end of 2018, while economic growth in Germany was only negative in the third quarter of 2018.

7 IHS Markit Eurozone Manufacturing PMI.

8 Business and Consumer Survey Results, European Commission, April 2019.

omy and their personal incomes, and have postponed large purchases.

In May inflation in the euro area slowed down.

Inflation was pushed up by 0.3 percentage point in April to 1.7% mainly by one-off factors⁹, but also because of the faster rise in energy prices (see Figure 5). In May inflation declined in the euro area to 1.2% as expected mainly because of the fall in prices for energy and services. Market-based inflation expectations¹⁰ also remain around 1.4%. Core inflation, without volatile food and energy prices, also declined from 1.3% to 0.8% in May.

Figure 5. Euro area inflation



9 The reference base effect of Easter.

10 Five-year inflation expectations for five years ahead derived from inflation swap transactions, the 5y/5y ILS rate (inflation linked swap rate).

Box 1. Economic activity in the euro area

The deceleration in economic growth last autumn was caused by the natural turn in the economic cycle and several temporary factors. These included problems in car manufacturing in adapting to new environmental standards, and short-term interruptions in other branches of manufacturing, and also issues such as the fall in confidence provoked by the gilet jaune protests and difficulties with deliveries. It became apparent at the end of the year however that some of these temporary factors would last longer than first expected, and for this reason the experts of the European Central Bank reduced their forecast in March for growth this year to 1.1% from the 1.7% forecast in December. It is forecast that growth will slow in the first half of the year, but it will start to pick up again in the second half. A risk that is repeatedly mentioned in recent forecasts is that economic growth may be slower than predicted because of global protectionism, populist governments and Brexit.

The March forecast by the experts of the European Central Bank expected that growth in the euro area economy would be a quarterly 0.2% in the first quarter, but the estimate from Eurostat put it at 0.4%. Total output in the euro area was up 1.2% over the year, which was the same rate of increase as in the fourth quarter of last year. The acceleration in growth in the first quarter was fairly even across countries. Most of the larger countries in the euro area saw signs of the economy expanding at the start of the year, especially those where growth was weak in the second half of last year. The estimate by Eurostat shows that total output in Germany started to grow again in quarterly terms, and at a rate that was last seen in the second quarter of 2018. The Italian economy also started to grow again having shrunk for two quarters. France came out of its dip of the end of last year and growth continues in Spain at more or less the rate that it has been at.

The decline in economic activity in the euro area in recent quarters has been eased by domestic demand remaining strong, which has supported growth in employment, and also because the global uncertainty has not particularly weakened the confidence of consumers. Retail sales volumes increased by around 2% over the year in the euro area in the first quarter of this year. The growth in domestic demand was supported by a more expansive fiscal policy in some coun-

tries in the euro area that will lead budget deficits to be twice what they were last year. Domestic demand has also been encouraged by the gradual recovery in car sales after the drop caused last autumn by the introduction of environmental standards. These environmental standards will continue to affect car production in future. Increased environmental awareness has led larger cities, especially in Germany, to start to introduce limits on vehicles with diesel engines. Domestic demand is also still supported by the construction sector, which is growing thanks to low interest rates. Construction work was boosted in the spring by relatively favourable weather conditions that allowed the building season to start as much as two months earlier than usual. It should be remembered though that a reduction in the impact of several one-off factors that have supported domestic demand could lead growth to slow in the second quarter. Favourable interest rates, and continuing rapid growth in wages and employment will continue to support private consumption though.

The situation in manufacturing improved only a little in the early part of the year. Growth in output volumes has been limited above all by the weak confidence that reflects the increasing uncertainty of companies about their ability to export. One company in four notes lack of demand as a factor limiting output volumes. Neither has confidence been increased by the postponement of Brexit, because the need to prepare for the exit of the United Kingdom from the European Union imposes large costs on companies, especially as the departure date becomes ever more uncertain. Survey data show that estimates about new orders in industry are a little more pessimistic than earlier, though still above their historical average. Supply-side limits continue to have an impact, as the use of production resources in manufacturing in the euro area remains close to its historical peak, while there are shortages of qualified labour in several countries, especially Germany. Low unemployment will boost the rise in labour costs, but the weak global demand environment means that end prices for products cannot be raised. For this reason estimates of the competitiveness of production companies have been downgraded a little. Financing conditions remain favourable for companies though, which makes it possible for investment to increase.

In general it can be said of recent quarters that 2019 started for the euro area close to the baseline scenario or a little better than it, meaning that no important risks were realised and the low point for growth in the current cycle was probably passed in autumn last year. Faster growth in the first quarter than was forecast is a consequence of several favourable factors coinciding, which is partly a one-off event. Further growth in the economy depends largely on how the global demand environment for euro area industrial output turns out.

BOX 2: THE EURO AREA'S MONETARY POLICY ENVIRONMENT

The objective of the Eurosystem monetary policy is to maintain price stability in the euro area. The European Central Bank defines price stability as inflation of below but close to 2% over the medium term. Although wage growth has accelerated in the euro area, inflation pressures have initially remained weak. The June 2019 forecast of the Eurosystem staff expects that the Harmonised Index of Consumer Prices (HICP) will rise annually by between 1.3% and 1.6% in 2019-2021. For this reason the Governing Council of the European Central Bank has decided to continue with its accommodative monetary policy for some time yet. The Eurosystem forecast shows though that core inflation will climb gradually in the coming years. This will be supported by the ongoing economic expansion and by increasing labour shortages and wage pressures in many euro area countries.

So that financing conditions would remain favourable and inflation, which has been below its target for many years, could build up some momentum, the Governing Council of the European Central Bank has held monetary policy interest rates at their current levels, with the minimum bid rate on main refinancing operations at 0.00%, the lending facility rate at 0.25%, and the deposit facility rate at -0.40% (see Figure B2.1). The Governing Council expects interest rates will remain at their present levels at least through the first half of 2020, and in any case for as long as necessary to ensure the continued sustained convergence of inflation to its target level.

Net asset purchases ended in December 2018, but due to reinvestments the ECB balance sheet will not decrease and the money created through the asset purchases will continue to boost the economy for as long as necessary. The Governing Council intends to continue reinvesting, in full, the principal payments from maturing securities purchased under the asset purchase programme for an extended period of time past the date when it starts raising the key ECB interest rates, and in any case for as long as necessary to maintain favourable liquidity conditions and an ample degree of monetary accommodation.

Monetary policy measures helped the consolidated balance of the Eurosystem to stand at 4.7 trillion euros by the end of April 2019, which is equal to 42% of the GDP of the euro area. During the reinvestment period, the size of cumulative net purchases under each constituent programme¹¹ will be kept at their levels as at the end of December 2018¹². At the end of April the total value of bonds purchased under the asset purchase programme stood at 2.6 trillion euros (see Figure B2.2). At 2.1 trillion euros, the largest part of the portfolio consists of public sector bonds, of which Eesti Pank's purchases accounted for 5.6 billion euros.

The Governing Council decided in March that from September this year until March 2021 it will again offer longer-term loans to banks on favourable conditions. The details of the new lending programme were announced in June¹³. Like the earlier targeted longer-term refinancing opera-

Figure B2.1. Eurosystem key interest rates and EONIA

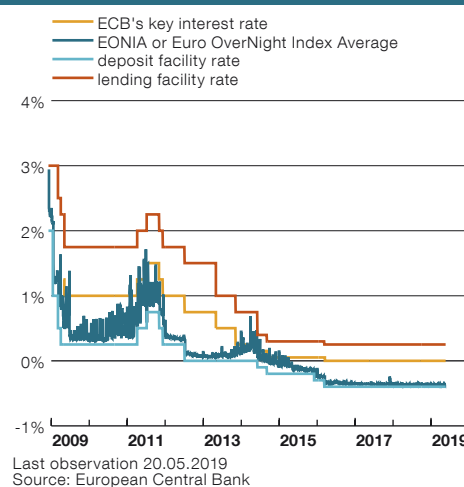
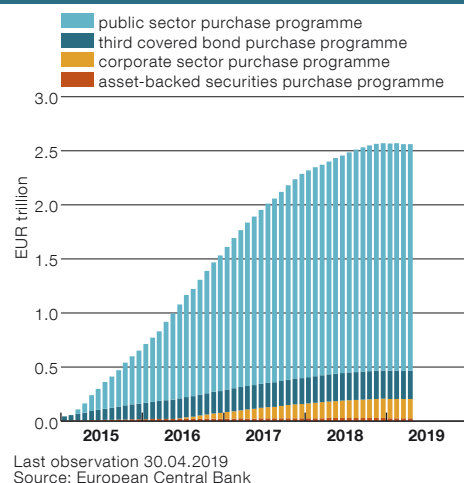


Figure B2.2. Eurosystem holdings under the asset purchase programme



11 The expanded asset purchase programme (APP) covers the public sector purchase programme (PSPP), the asset-backed securities purchase programme (ABSPP), the third covered bond purchase programme (CBPP3) and the corporate sector purchase programme (CSPP).

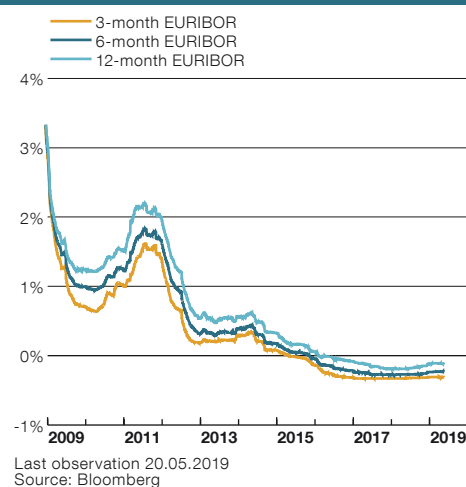
12 Limited temporary deviations may occur for operational reasons.

13 <https://www.ecb.europa.eu/press/pr/date/2019/html/ecb.mp190606-1876cad9a5.en.html>

tions (TLTRO)¹⁴ the new TLTRO-III loan series will help to preserve favourable bank lending conditions and the smooth transmission of monetary policy. The interest rate charged will depend on the percentage by which a bank exceeds its benchmark stock of eligible loans. The maturities of the new loans will be two years. The Eurosystem's standard lending operations will continue to be conducted as fixed rate tender procedures with full allotment for as long as necessary, and at least until the end of the reserve maintenance period starting in March 2021.

Money market interest rates remain negative in the euro area and at the end of May the three-month EURIBOR was at -0.32%, the six-month EURIBOR at -0.25%, and the 12-month EURIBOR was at -0.17% (see Figure B2.3). Yearly growth of the money supply in the euro area remains strong with support from the accommodative measures and credit creation of the Eurosystem, and in April the broad money indicator M3 was up 4.7% despite the asset purchase programme ending. The yearly growth in the stock of loans to non-financial companies has slowed a little in recent months and was 3.9% in April, reflecting the lagged reaction to weaker growth in the economy last year. The yearly growth in the stock of housing loans increased in April to 3.4%. Credit growth is supported by favourable lending conditions and rising demand for housing loans. Demand from companies for loans stabilised in early 2019 after rising for almost four years from the second quarter of 2015. The latest Bank Lending Survey for the euro area shows that lending conditions for companies in the euro area remained on average largely the same in the first quarter of 2019, while housing loan standards have tightened.

Figure B2.3. Euro area money market interest rates



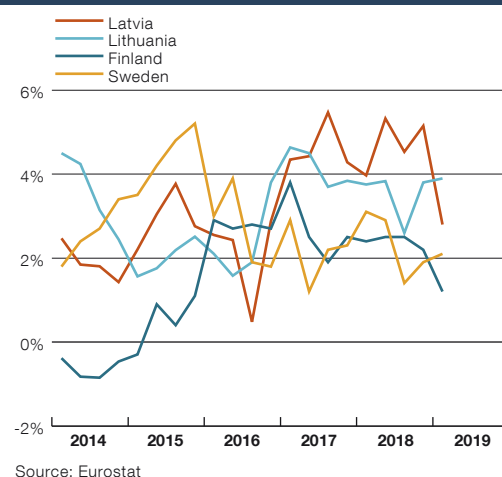
14 TLTRO-I loans were issued in September 2014 to June 2016, and TLTRO-II loans in June 2016 to March 2017. The first and second series of TLTRO loans had maturities of 2-4 years.

ESTONIA'S MAIN TRADING PARTNERS

The economies of Estonia's main trading partners were performing quite well in the first quarter, but there is a perceived weakening of economic activity. The economies of neighbouring countries advanced in both quarterly and yearly terms (see Figure 6), and only Latvian yearly economic growth was slower than expected in the first quarter, while its quarterly growth fell to -0.1%.

Growth slowed sharply in the Latvian construction sector, which was still very strong last year. The growth in Latvia and Lithuania is largely based on domestic demand, as private consumption is boosted by growth in household incomes and in employment, while the cost of financing is low. At the same time, the consumption of Finnish and Swedish households did not

Figure 6. Yearly growth in GDP of trading partners



Source: Eurostat

increase in the first quarter. Growth in investment in neighbouring countries is also slowing and this is particularly noticeable in construction. Despite the uncertainty in the external environment, foreign trade improved in the first quarter (see Figure 7). Swedish exports have grown very rapidly, as exports of goods have been supported by a sharp depreciation in the krona against the euro and the US dollar. Despite the downward trend in economic confidence in Estonia's export partners, manufacturing saw stable growth in the first quarter that was in line with foreign trading activity. Economic confidence in Finland has however fallen below its long-term average.

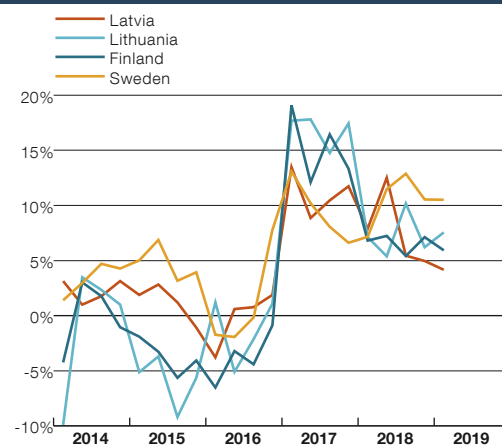
There are more people in employment in the labour markets of Estonia's trading partners than ever before.

Unemployment rates have fallen in the Nordic and Baltic countries to very low levels (see Figure 8). At the same time the employment rate has hit record peaks, making it harder for companies to find skilled employees. Rapid wage growth and increased participation in the labour market by those of retirement age have helped reduce the number of people inactive in Latvia and Lithuania. Fast economic growth will increase labour market tensions even further in the Baltic states, and will mean increased shortages of labour and continuing rapid growth in wages. Despite the tensions in the labour market and the shortage of workers, wage rises have been modest in Sweden and to a lesser extent in Finland.

The cost of the consumer basket rose in April in both monthly and yearly comparison (see Figure 9).

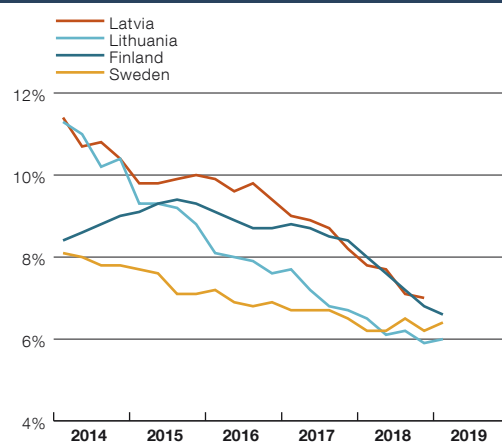
The inflation has mainly been higher due to the global price of oil, which has made motor fuel more expensive. Consumer prices have also been pushed up by rapid rises in the price of electricity, vegetables and package holiday tickets. Inflation climbed to 3.4% in Latvia in April, which is its highest rate for two years, partly because of rises in excise at the start of the year and because energy goods have a larger share in the consumer basket. Inflation in Lithuania was last as high in October last year, while in Finland and Sweden, inflation hit its peak of the past half year in April. Although the rise in inflation in Sweden may prove temporary, the central bank is hitting its inflation target of 2% for the time being and no rise in interest rates is expected soon.

Figure 7. Yearly growth in exports of trading partners



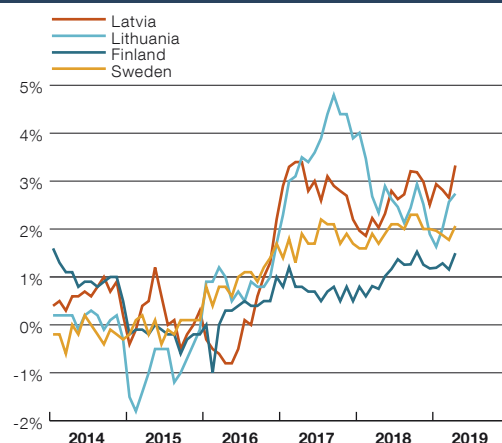
Source: Reuters

Figure 8. Unemployment in trading partners



Source: Eurostat

Figure 9. CPI inflation in trading partners



Source: Eurostat

THE ESTONIAN ECONOMIC ENVIRONMENT

ECONOMIC ACTIVITY

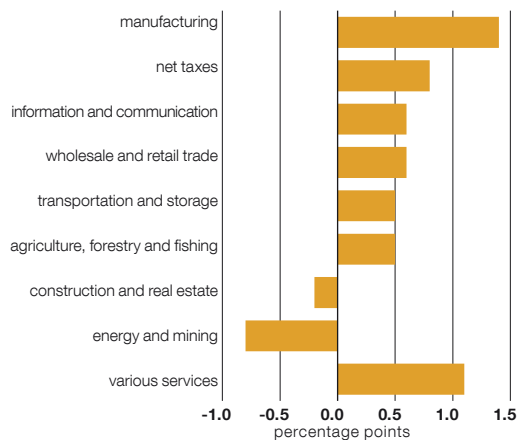
The Estonian economy was larger by 4.5% over the year in the first quarter of 2019, and by 0.5% over the fourth quarter of 2018. Exporting branches of the economy dominated. The largest share of the growth came from manufacturing (see Figure 10), but almost all parts of the economy contributed. The biggest change from the fourth quarter was the sharp slowdown in the growth in value added of the construction sector, as construction volumes remained at the same level as in the first quarter of the previous year, having grown by nearly 20% in the fourth quarter of last year. Alongside manufacturing, business services and IT also saw rapid growth in value added.

While output grew in most branches of manufacturing in the first months of the year, a fall in the energy industry reduced the rate of growth in the industrial sector as a whole, which covers manufacturing together with energy and mining (see Figure 11). The strong growth in manufacturing is something of an exception among countries in the Europe Union, where problems in the German car manufacturing industry have reduced growth in several other countries. The connections between Estonian industry and German car manufacturing are weak though, and so those problems have had much less of an impact in Estonia. The weakness in the energy sector that held back growth was mainly a consequence of a decline in the competitiveness of oil shale electricity as a result of European climate measures.

The good performance of manufacturing is reflected in the rapid growth in exports of electronic equipment, which may be partly a consequence of trade restrictions between China and the United States, as Chinese difficulties may improve the position of producers in other countries, including Estonia. However, the production of electronic equipment adds only a small part of the value added of industry.

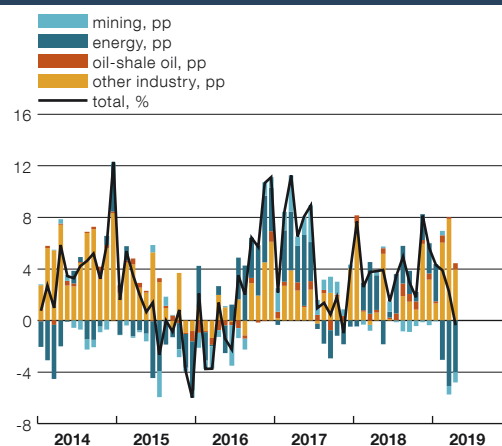
Although the output of manufacturing increased strongly in the first months of the year, the expectations of manufacturing companies for output indicate that growth may slow in the months ahead (see Figure 12). Expectations

Figure 10. Contributions of sectors to GDP growth in Q1 2019



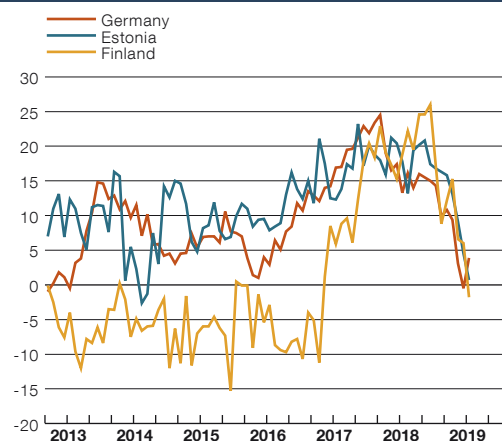
Source: Statistics Estonia

Figure 11. Yearly growth in industrial production



Sources: Statistics Estonia, Eesti Pank

Figure 12. Production expectations in manufacturing



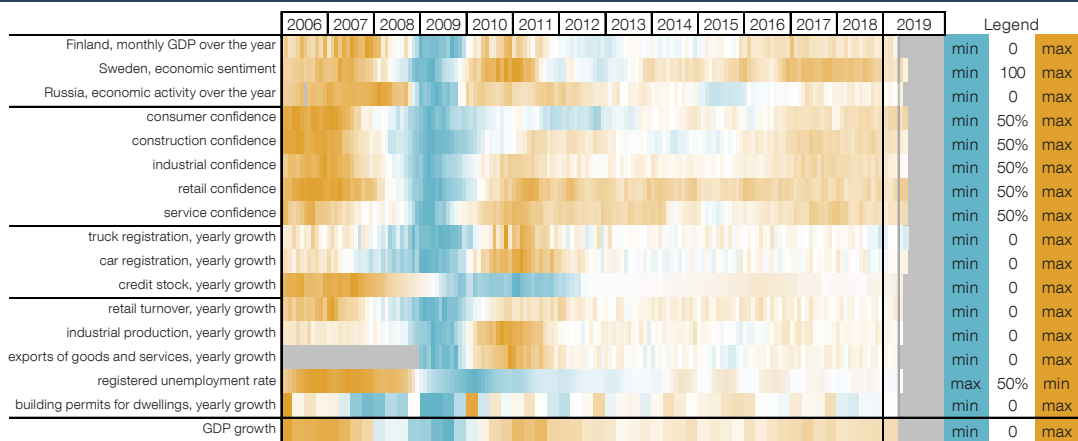
Source: European Commission

weakened in Germany at the start of the year, but the impact of this has reached Estonia and Finland with something of a lag. Falling expectations reflect the general slowdown in the growth in world trade, which is partly a consequence of trade conflicts. The general outlook of companies, as shown in the economic sentiment index, has softened by less than the expectations for production in manufacturing (see Figure 13). The expectations of service companies remain optimistic. The differences between the industrial and service sectors illustrate that the companies that are more dependent on foreign markets seem to feel a greater danger of weaker growth.

Figure 13. Forward looking economic confidence and sentiment indexes



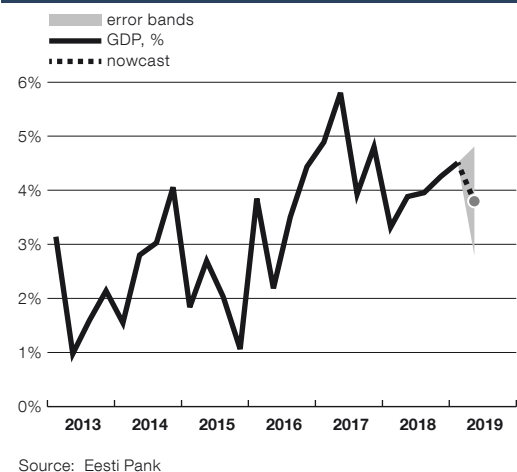
Figure 14. Heatmap of the Estonian economy



The economic activity heatmap only shows warmer colours, or an improvement in conditions from the previous quarter, for indicators related to consumers and retail sales. The rest of the variables have either not improved or have even worsened (see Figure 14). The nowcast model for economic growth used by Eesti Pank, which uses various short-term statistics as inputs, also currently indicates that growth will slow in the second quarter (see Figure 15).

Economic activity has been affected considerably by foreign labour in recent years. Without substantial immigration the economy would have grown more slowly. The increasing use of foreign labour makes it harder to estimate the cyclical position of the economy. The

Figure 15. GDP growth and current quarter nowcast



addition of short-term foreign labour increases the supply capacity in the economy temporarily, and so should ease upwards pressures on wages and prices. However, short-term foreign labour is dependent on the state of the economy, and if demand weakens, the foreign workers may promptly leave and so reduce the supply capacity in the economy. The long-term sustainable rate of growth for the Estonian economy is estimated at around 3% a year.

DOMESTIC DEMAND

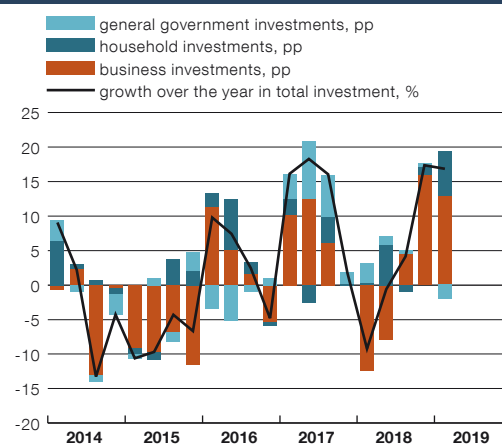
Yearly growth in Estonian domestic demand was 4.0% in the first quarter of 2019, and demand was driven by increased investment and private consumption. Gross fixed capital formation was 17.1% more than a year earlier because of the support from investment by companies and households (see Figure 16).

Investment by non-financial companies in fixed assets was up around 22% on the year at constant prices in the first quarter. Some two thirds of this growth came from investments in transport vehicles, where 177 million euros was invested rather than the more usual 70-80 million. The rest of the growth came largely from investments in other machinery and equipment, as investments by companies in construction were only 2.4% more than a year earlier and this made no significant contribution to the overall figure for growth. Investment was up in almost all areas, while the largest contributors were retail trade, and transportation and storage.

Companies in most sectors borrowed little from banks in the first quarter, and it was primarily energy companies that took out new long-term loans. The average interest rate on new long-term corporate loans was higher in the first months of 2019 than in 2018, which partly reflects a tightening of lending conditions in some loan segments. Interest rates are still low compared to what they were in the previous decade and companies have good access to domestic bank loans.

The general government invested less in fixed assets than it did a year earlier. Gross fixed capital formation at constant prices fell by 12% and this fall was due fairly equally to reduced invest-

Figure 16. Gross fixed capital formation



Sources: Statistics Estonia, Eesti Pank

ment in construction and in machinery and equipment. Gross fixed capital formation declined at the central government level, while local governments slightly increased the investments funded from their budgets.

Demand and supply for housing continued to be large in the first quarter. This is also reflected by the rapid growth in the investment by households in housing, which was 105 million euros larger in the first quarter than a year earlier, representing growth of 30% at constant prices. This is in line with the statistics for usage permits, which indicate strong growth in new space, and especially in reconstructed space. At the same time there are signs that indicate some calming in the housing market in the future. The number of transactions for residential property in the real estate market in the first quarter of 2019 was at around the same level as a year earlier (see Figure 17) and the number of new housing loans was lower than a year earlier. The conditions for housing loans did not change significantly and the average interest rate on new housing loans remained close to where it was in the second half of 2018 at around 2.5%.

Growth slowed in spending by households on consumption at the start of this year (see Figure 18). Consumption grew by 4.8% in 2018 overall, but in the first quarter of this year consumption growth was down to 2.8%. The growth in private consumption was notably slower than that in real wage income earned by households. The growth

Figure 17. Number of purchase and sale transactions with residential real estate and growth in new housing loans

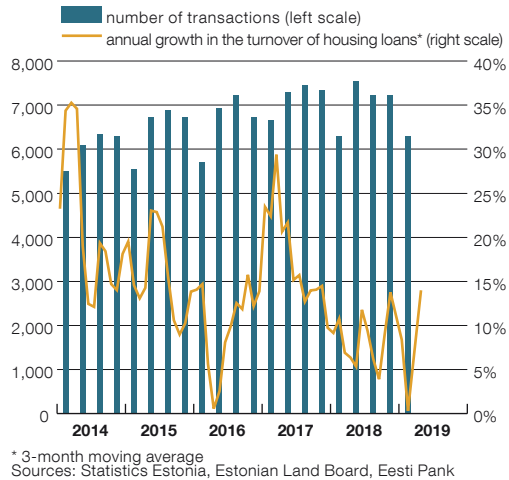
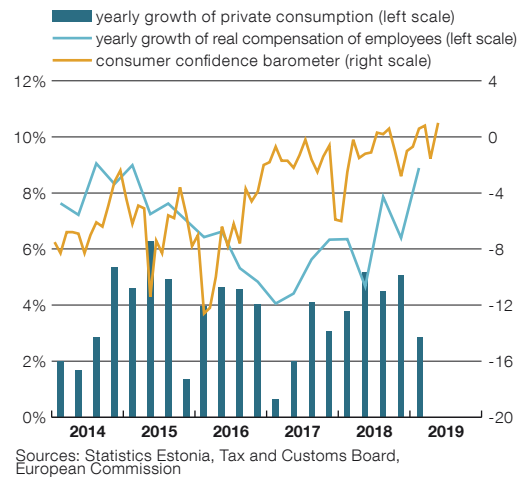


Figure 18. Private consumption



in real wages was accelerated by rises in the number of people in employment and in the average wage, and by lower inflation. Faster growth in incomes and slower growth in consumption indicate that the total savings of Estonian residents continue to increase. One contributing factor to the slower growth in consumption spending was that spending abroad by Estonian residents, which increased rapidly last year, was down in the first quarter of this year. The growth in consumer spending was also restrained because the growth in unavoidable spending related to residential property was down sharply on last year, which may be partly because the winter weather was warmer in the first quarter than a year earlier. At the same time, purchases of durable and semi-durable goods increased strongly in the first quarter, which is in line with the rapid growth in sales revenues at retail companies.

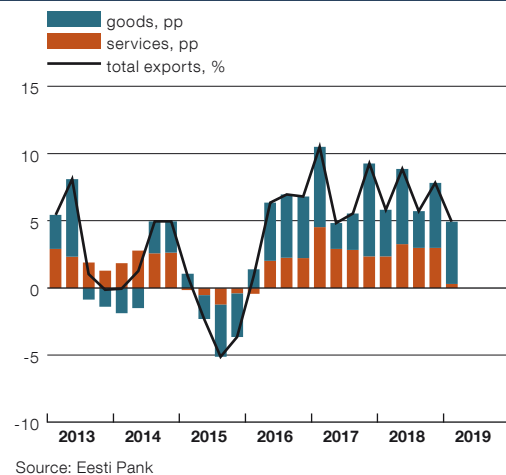
The growth in domestic demand in the first quarter was held back by corporate inventories growing more slowly than they did last year.

Growth in inventories slowed most in wholesale and retail, where goods purchased for sale increased by less than a year earlier, and in construction where there was slower growth in raw materials.

EXTERNAL BALANCE AND COMPETITIVENESS

The main target markets for Estonian exports were weaker than forecast, and their demand for imports grew more slowly. Reduced activ-

Figure 19. Decomposition of growth in exports

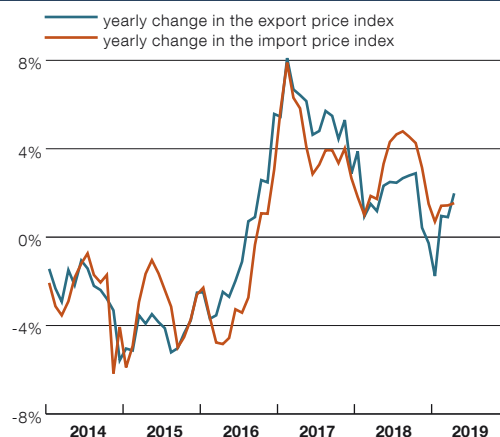


ity in foreign markets, increased uncertainty, and risk aversion have limited the capacity of Estonian exports to grow. The dynamics of foreign demand remained quite uneven across individual target markets, but overall the effect was to slow exports of Estonian goods and services. Despite the relatively strong economic growth in Estonia's main trading partners, foreign demand for Estonian goods and services grew more slowly in the first quarter. Statistics for GDP show that Estonian exports of goods and services grew by 4.9% at current prices in the first quarter (see Figure 19). This means that the value of Estonian exports grew a little faster than foreign demand due to the increase in volume, while the rise in relative prices was smaller.

The results for exports were affected a lot by changes in the structure of target markets and the composition of products exported. Alongside the weaker indicators for foreign demand are structural changes and their role in increasing the general capacity to export often goes relatively unnoticed. Initial estimates for recent months support the earlier forecast in that the growth in goods exports to euro area countries has faded in line with demand in those countries. As expected, the growth in goods exports to non-euro area countries was a little stronger, but it was also slower than in the previous quarter. Exports of services, which can usually cope better with cooler demand, did not grow in the first quarter. The decline in exports of construction services and rail transport services overshadowed the growth in sales of digital and other business services (see Box 3). Export prices rose by less than import prices in the first quarter, meaning that terms of trade had deteriorated slightly (see Figure 20).

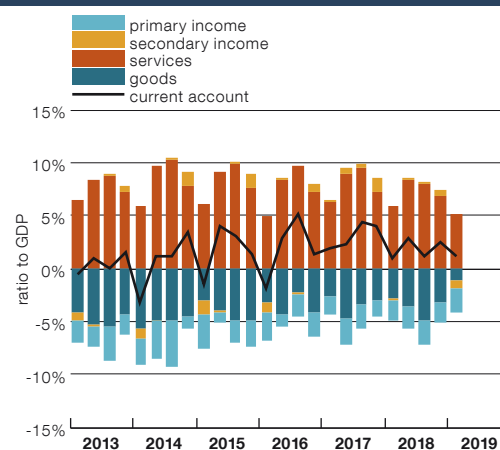
Slower growth in export revenues and continuing strong demand for imports worsened the trade balance of the Estonian economy a little (see Figure 21). The surplus on the current account shrank to 1.1% of GDP in the first quarter of 2019. The Estonian economy still remained a net lender to other countries, investing more abroad in financial assets than it took in from there.

Figure 20. Export and import price indexes



Source: Statistics Estonia

Figure 21. The current account



Sources: Statistics Estonia, Eesti Pank

Box 3: Changes in the structure of exports are contributing to strong growth

Exports of goods and services play a very important role for growth in the Estonian economy. The economy is very open and data for 2018 put the share of exports at 75% of gross domestic product.

Estonian prices and labour costs have risen quite fast in recent years, which has caused strong cost pressures in the economy as a whole and has reduced the competitiveness of exporting companies for several products in their target markets. Eurostat data show the share of Estonian exports in global exports of goods and services increased in 2018 by 2.3% with goods exports up 1.3% and services exports up 4.9% at current prices, though in December 2018 there was a reason to talk about a reduction in the market share of Estonian exports in target markets, as it had fallen in the preceding three quarters, especially in volume terms. The ability of exporting companies to compete in a globalised world and to adapt to changes depends on several factors. Gain or loss of market share may depend on the particular features of demand in target markets or on the combination of products exported, as demand for different goods and ser-

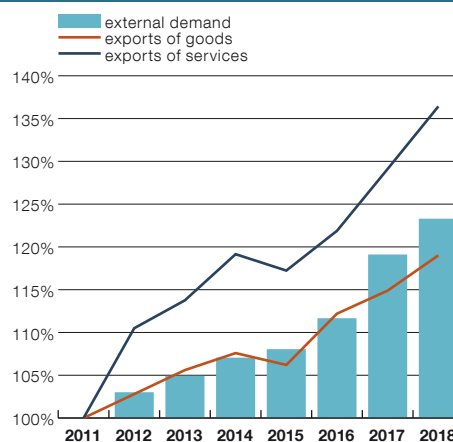
vices can change in different ways around the world. Changes in the structure of exports can also have an important impact on the indicators for Estonian competitiveness, and through that on the whole of productivity, employment, economic growth and public welfare.

Competing on price and cost remains very important, and costs rising higher than at competitors can reduce the ability of a company to earn profit, even forcing it to exit the market as Baltika and Sangar have recently had to do, but the key to maintaining competitiveness and increasing market share does not only lie in prices and costs. Companies in developed countries with high wage levels mainly compete not so much on price as on quality, seen in factors like better and more innovative products, brand popularity, taste, reputation or good marketing. Among these non-price factors that play an important role are the combination of exports and the difference in that combination for different target countries and groups of products; the design and quality of the products; the existence of particular niches; the position of a company in global production and value chains; innovation; efficiency; national economic policy; and consumer preferences.

National competitiveness can be considered as the ability of exporters to increase their income from international markets faster than competing countries do, and this can be affected by export volumes as well as by prices. In the past seven years since Estonia joined the euro area, the country's exports at current prices have grown by a little more than one third, meaning on average 1.1 times faster than demand has grown in Estonia's main target markets. This faster growth has come entirely because of exports of services, and the situation is more complicated for goods exports, as goods exports from Estonia have lost around 3% of market share by export volume over the seven years (see Figure B3.1). At nominal prices goods exports still grew at more or less the same speed as foreign demand (see Figure B3.2), as they did not entirely accompany the fall in prices in foreign markets in 2013-2016 that was mainly due to the appreciation of the euro exchange rate (see Figure B3.3). Services exports at nominal prices increased by some 63% over the past seven years though, and their share in the additional growth of total exports has increased. Services accounted for a third of total exports in 2018 by value, but they accounted for more than half of the additional growth in exports over seven years.

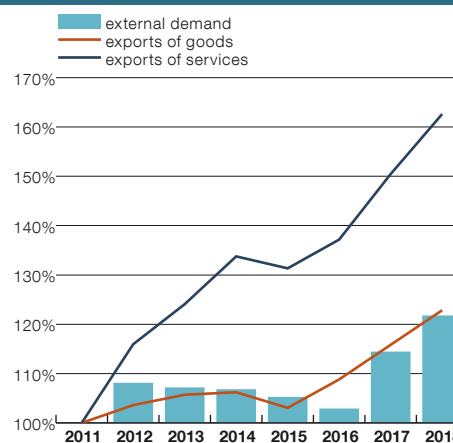
Estonia stands out from other countries by having a relatively efficient service sector. One third of the growth in the value of exports of Estonian services from 2011 was due to the increase in

Figure B3.1. Exports and external demand at constant prices



Sources: Statistics Estonia, Eesti Pank

Figure B3.2. Exports and external demand at current prices



Sources: Statistics Estonia, Eesti Pank

the volume exported, and two thirds came from the rise in the price of exports. Prices for services exported to target markets rose notably faster than average prices, increasing by 21% over seven years (see Figure B3.3).

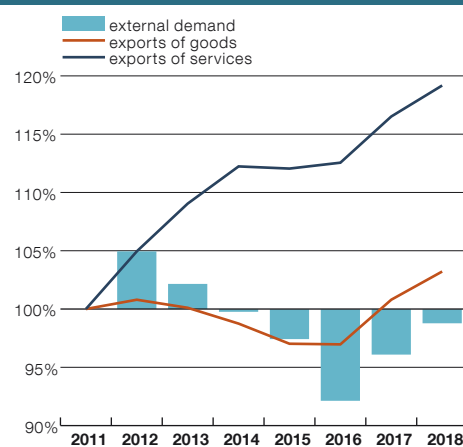
The faster rise in prices for services illustrates the rapid growth in unit labour costs, but at the same time the ability of exporters of services to raise market prices is also an illustration of the improved competitiveness of the Estonian services sector in international markets. A survey published by the European Commission in 2014¹⁵ found that if rising unit costs raise product prices, demand is only reduced under certain circumstances such as an equivalent alternative product being available. Prices also rise if exported products become more complex, knowledge intensive or higher quality, and if consumers recognise that products are of better quality, they will continue buying them and demand may even increase. In economic theory this is called shifting up the demand curve because of improved quality.

Prices and volumes have both increased substantially for Estonian exports of services, which strongly indicates that more complex services have performed well and the structure of services has changed as the share of more expensive services has increased. Exports of digital and other ICT services and of scientific and business services have increased much faster than the average. Changes in methodology mean that the distribution of types of service can only be compared from 2013 onwards, since when exports of more complex services have increased 1.7 times faster than those of other services have, and their share in total exports of services increased in five years from 13.7% in 2013 to 21.3% in 2018. Exports of transport and storage services have grown more slowly than the average, and in consequence their share in the total exports of services has fallen over the years.

Overall it is apparent that the ability of exporting companies to compete in global markets is not based only on low costs, but more and more on higher productivity and more complex products. Increasing market share rapidly still requires export products to become more complex and for this to be done faster. It is very hard to say whether in future non-price factors and an increase in the share of more complex types of services in the structure of exports will manage to replace entirely the reduction in the production of various goods with a price advantage, or whether the growth in the market share of Estonian exports will slow up in the near future.

¹⁵ Hylke Vandenbussche. Quality in Exports. European Commission, Economic Papers 528, September 2014.

Figure B3.3. Prices of exports and external demand, 2011 = 100%



Sources: Statistics Estonia, Eesti Pank

THE LABOUR MARKET

Rapid growth in the economy meant that demand for labour remained strong in the first quarter of 2019. Employment in Estonian companies and institutions increased by 1.9%, while unemployment remained low. Data from the Tax and Customs Board show the number of peo-

ple declared as receiving a wage grew by a further 2.6% in the first quarter of 2019, which is a similar rate to that of last year. This may have been boosted by the continued rise in the number of short-term workers from abroad coming to Estonia. The labour force survey shows that employment increased in the service sector and

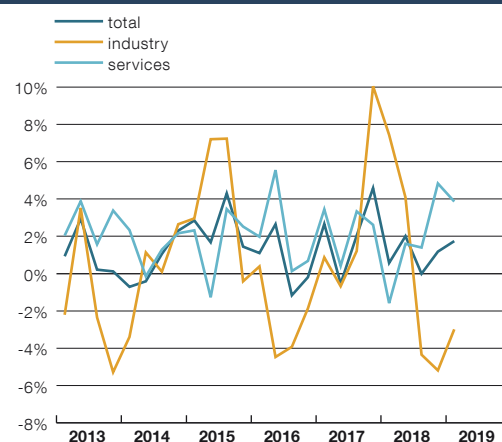
fell in the industrial sector (see Figure 22). As manufacturing and construction are the sectors where the majority of short-term foreign labour coming to Estonia works, it is probable that the growth in employment in those sectors has been underestimated (see Box 4 on labour from abroad).

Like in 2018, the number of people working part-time increased in the first quarter of 2019, while there were still the same number of full-time workers as a year earlier. The number of hours worked per employee fell by 0.6%, but the rate of fall was slower than in the previous year. This decrease is fully explained by the increase in the share of part-time workers.

The unemployment rate was at 4.7% in the first quarter of 2019, and seasonally adjusted unemployment fell in the first quarter from the previous one (see Figure 23). The fall in unemployment was due not only to increased employment but also to slightly lower labour force participation than a year earlier. The fall in unemployment in recent years has been driven by a reduction in the number of long-term unemployed, while the number of those out of work for under a year has remained relatively stable. Long-term unemployment is currently at a record low level, even including the economic boom years before the financial crisis. Registered unemployment has remained at around 4.7% since the start of 2018. The number of unemployed registered as having reduced capacity for work has stabilised at a little more than 10,000 people, and this accounts for a little under a third of all the registered unemployed.

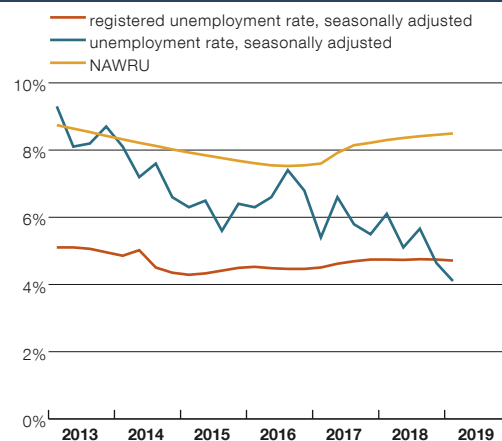
Rapid economic growth has increased demand for labour, and this has then boosted wage growth as the labour market is tight. The average gross monthly wage was up 7.9% in the first quarter of 2019, which is around one percentage point lower than in the previous quarter, but is still high. Wages rose faster in the general government sector, as they did in 2018, and by less at private companies (see Figure 24). General government wage growth was around 10% in public administration, education and health. The fastest wage growth in the private sector was in industry because of the rapid wage growth in construction, and it was more moderate in services.

Figure 22. Yearly growth in the employment of Estonian residents from the Labour Force Survey



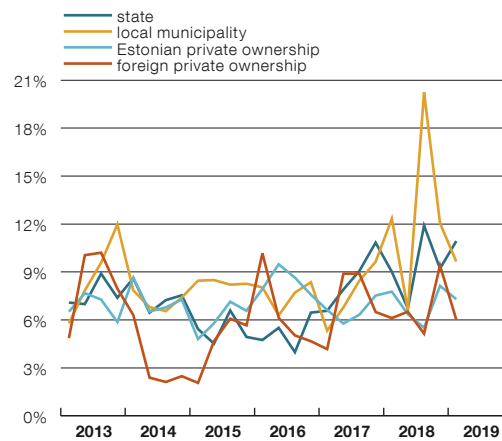
Source: Statistics Estonia

Figure 23. Unemployment



Sources: Statistics Estonia, Töötukassa, Eesti Pank

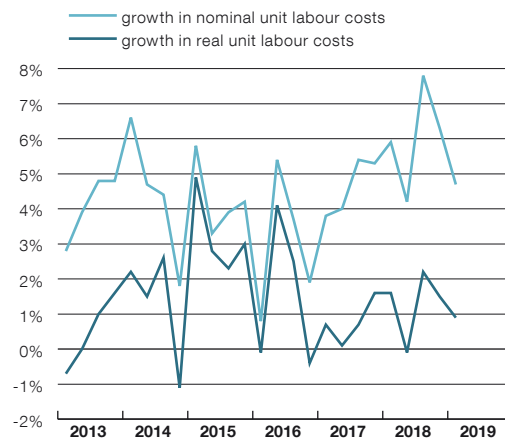
Figure 24. Yearly change in average wages by ownership status



Source: Statistics Estonia

The discrepancy between growth trends in labour costs and corporate profits narrowed in the first quarter of 2019 (see Figure 25). Although labour productivity growth was less than wage growth, the growth rates for the two indicators were better aligned than in previous quarters. The share of labour costs in value added in services and construction increased, while it declined in industry. This means that competitiveness in the industrial sector, which is the most exposed to foreign competition, was not harmed by labour cost pressures.

Figure 25. Growth in unit labour costs



Source: Statistics Estonia

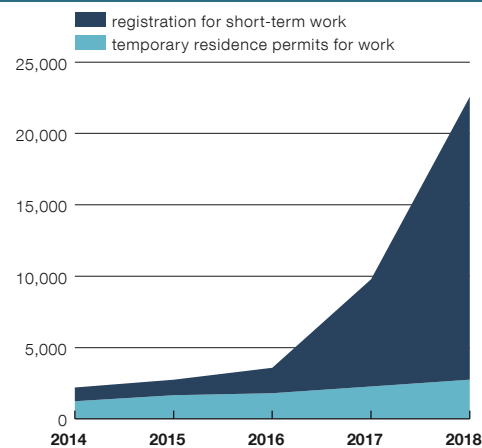
Box 4: Short-term employment in Estonia

Estonia's migration balance was negative from when independence was regained until 2014, meaning that every year more people left Estonia than moved there to live. The situation has been reversed since 2015, as more people move to Estonia than leave. Immigrants moving on a permanent basis have been accompanied by a large leap in the numbers of workers coming from other countries who will not remain permanently in Estonia. This has been facilitated partly by rapid rises in wages and labour shortages that have made Estonia more attractive as a place to go to work, and also by a loosening of the rules on people coming to work for a short time from countries that are not in the European Union. At the start of 2017 the maximum period permitted for short-term work was extended from six months to nine months, and in July 2018 it was extended further to 12 months. This box analyses how short-term workers from outside the European Union coming to work in Estonia have affected the economy.

The main indicators for the Estonian labour market are employment, unemployment and the labour force participation rate, and estimates of them are based on the Estonian Labour Force Survey. They describe the labour market behaviour of permanent residents of Estonia, including those who work abroad. The estimate of the number of people employed by companies and institutions operating in Estonia is based on the same survey, with the number of people working abroad subtracted. Although the number of residents of foreign countries working in Estonia has increased over recent years, they are not included in the estimate of employment.

Data from the Police and Border Guard Board show 7510 citizens from countries outside the European Union were registered as working short-term in Estonia in 2017 and 19,828 in 2018 (see Figure B4.1). How many of these

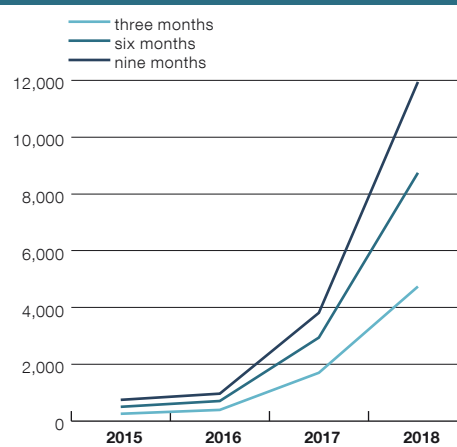
Figure B4.1. Inflow of foreign labour from non-EU countries



Sources: Police and Border Guard Board, Eesti Pank

people are on average working in Estonia at any given moment depends on how long they have come to work for. Registration for short-term employment increased rapidly in 2015-2018, and so it may be assumed that registration also increased within those years. There are no data on the duration of employment, but the time-limit suggests that in each month of 2018 the maximum number of workers in Estonia would be those who had registered within the previous nine months. It is very probable that the average duration of employment is still shorter than the maximum permitted period, and so three variations are used for the calculation, with the average duration of employment taken as three, six and nine months.

Figure B4.2. Yearly average number of non-EU resident workers in Estonia for different average durations of employment



Sources: Police and Border Guard Board, Eesti Pank

Under these assumptions, the share of citizens of countries outside the European Union who were working short-term in Estonia at Estonian companies and institutions was on average 0.7-1.8% of total employment in 2018 (see Figure B4.2). The situation was very different in different sectors, and the share of such workers in construction may have reached 3-8% in 2018. Short-term working also boosted the growth in employment. The employment of permanent residents of Estonia at Estonian companies and institutions grew by 1.2% in 2018, but if short-term workers from outside the European Union are also counted, employment increased by 1.7-2.5%.

This means that short-term foreign workers in Estonia contributed to the creation of value added alongside permanent residents of Estonia, and leaving them out of the calculation overestimates the growth in productivity per worker. Using only residents of Estonia in the calculation shows productivity per employee grew by 2.6% in 2018. If foreign short-term workers are added to this, the growth in labour productivity is more modest at between 1.3% and 2.1% (see Table B4.1). Assuming that the productivity of permanent residents and workers from other countries is equal, those workers coming from elsewhere contributed 0.5-1.3 percentage points of the GDP growth of 3.9% in 2018. It does not necessarily follow though that if temporary labour could not be hired from outside the European Union, growth in the economy would be smaller by the amount that short-term workers contribute. Stricter rules on immigration would though have made it harder for companies to hire labour, which would have increased wage pressures and through this affected the labour market behaviour of Estonian residents and the competitiveness of exporting companies.

Table B4.1. Impact of foreign workers on selected economic indicators for different durations of stay, 2018

	only residents employed in Estonia	residents and non-EU residents employed in Estonia by the average duration of employment of non-residents		
		three months	six months	nine months
employment growth, domestic concept	1.2%	1.7%	2.1%	2.5%
productivity growth	2.6%	2.1%	1.7%	1.3%
the contribution of non-resident workers to GDP growth	0 pp	0.5 pp	0.9 pp	1.3 pp

Sources: Police and Border Guard Board, Eesti Pank

PRICES

The rise in consumer prices slowed in the first months of 2019.

The main reason for this was the fall in the price of oil, which started in the fourth quarter of last year. Core inflation also slowed at the start of the year and came below 2%. The rise in the prices of imported consumer goods was held back by the low level of economic activity in the euro area. Favourable import prices eased the cost pressures that companies were facing because of rapid wage growth and the shortage of available labour. Inflation was also slower because it was lifted strongly last year by rises in excise rates, but the effect of taxes has been smaller this year. Prices have risen on average by 3.3% in the past two years, but without the impact of excise rises, inflation would have been 2.7%.

Inflation started accelerating again in the beginning of the second quarter and it exceeded 3% in April.

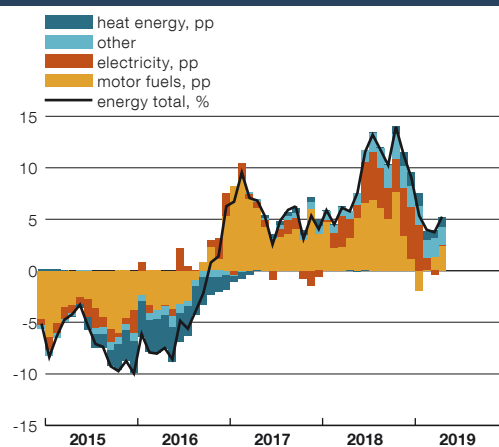
It was mainly the groups of goods with volatile prices that contributed to the rise in inflation. Vegetables, especially potatoes, were up in price by over 30% on the year, and air tickets were also up. The higher oil price also caused the price of motor fuels to start to rise (see Figure 26). The price of a barrel of crude oil rose back above 70 dollars in April. On top of the rise in the crude oil price, prices for imported fuels have also been driven up faster by a fall in the exchange rate for the euro. The recent information about the state of the economy in the euro area has not all been favourable, and this has contributed to the euro weakening. The rise in energy prices has been driven for a long time by increasing prices for solid fuels, especially wood.

The yearly rise in the price of food commodities remained slow in the first quarter.

Unfavourable weather for agriculture has caused prices of food commodities to start to rise on the European domestic market. Grain prices have been rising since last autumn. Higher prices on global markets for dairy products and meat had not yet passed substantially into the domestic markets of the European Union in the first quarter.

Consumer prices of consumption goods were up by less than 1% over the previous year in the first quarter, because import prices have

Figure 26. Energy price inflation



Source: Statistics Estonia

risen only slowly. The prices of industrial inputs were 4-5% lower on global markets in dollar terms in the first quarter than a year earlier. The volatility in services prices of late reflects the sharp rise in the price of air tickets.

GOVERNMENT FINANCES

The rise in tax revenues slowed considerably in the first months of 2019.

Yearly growth in tax revenues was almost 7% in the fourth quarter of last year, but the initial estimate for the first four months of 2019 shows that the general government received on average only 4.5% more than in the same period of 2018. The increase in tax revenue was very different in different months, which is to be expected.

The main reasons for the volatility and for slower growth than earlier were the numerous tax changes that came in last year, as their impact in reducing revenue only appears with a lag.

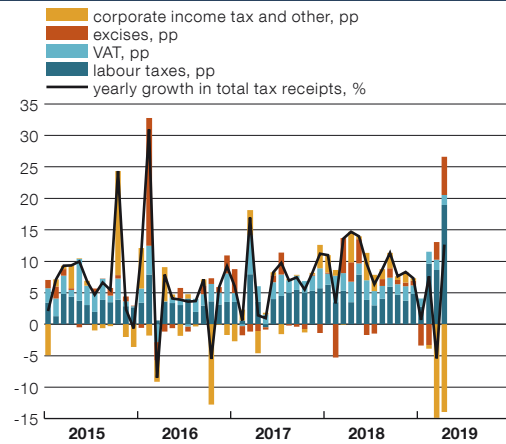
Several corporate income tax measures were introduced last year that increased receipts of corporate income tax by 0.6% of GDP. This year there will be a lower tax rate on legal entities that distribute profit regularly, and so the receipts from corporate income tax will be smaller. Indeed, less was received by the state treasury in corporate income tax from January to April than in the same months in 2018 (see Figure 27).

Another factor that significantly affected tax receipts in the first months of the year was that

after the reform of the tax-free threshold last year, many people made less use of the lower threshold than their actual income would have allowed. As a consequence the repayments following personal income tax declarations were twice as large this year as a year earlier, and from January to April the receipts of personal income tax were 10% smaller. This was a temporary reduction and overall receipts of labour taxes can still be considered very good.

Growth in government spending remained fast in the first months of the year. The state budget that has been passed suggests that growth of over 7% can be expected in general government spending this year. The yearly growth in general government spending was 11% in the first quarter of last year, and initial estimates suggest that it remained at about the same rate in the first months of 2019. Above all the rapid growth in

Figure 27. Tax receipts in the state budget



Source: Tax and Customs Board

general government spending on consumption and wages continued, while investments were smaller than a year ago.

ECONOMIC FORECAST 2018-2021

The Eesti Pank economic forecast is produced jointly by experts from the central bank's Economics and Research Department and Financial Stability Department. It is a part of the joint forecast for the euro area produced by the euro area central banks and the European Central Bank, which uses shared assumptions about interest rates in euro area money markets, the euro exchange rate and commodities prices. The outlook for demand and prices in Estonia's trading partners is based on forecasts prepared by other central banks in the euro area at the same time. The external assumptions used in the forecast and the Estonian economic indicators are based on data available as at 22 May 2019. The Eesti Pank forecasts are compiled using EMMA, the macro-model of the Estonian economy developed and regularly updated by Eesti Pank.

THE INTERNATIONAL ECONOMIC ENVIRONMENT

In the near term growth will slow further in the global economy, as it is restricted by trade and political tensions, and the slowing of the economic cycle in several countries around the world. This will then in turn slow the growth in global trade and industrial output. As the larger central banks have postponed tightening of monetary policy, funding conditions will remain favourable this year and next and will support domestic demand and activity in the service sector. Financial markets are however quite volatile and risk averse and a downgrading of risk assessments could again make funding conditions tighter for developing countries. These factors will mainly affect economic growth this year, and in the subsequent years the global economy should start to revive again.

The trade fight between the US and China became more intense when the US imposed higher customs tariffs of 25% on 200 billion dollars of Chinese goods, to which China responded with its own measures. The points of dispute in trade with the European Union have not been resolved either, although before summer the US decided to postpone for six months new customs tariffs of up to 25% on cars and car parts from Europe. The consequent reduction in trade could hold back growth in the economy in China and

several advanced economies, and also in emerging Asian economies for which Chinese demand is an important source of economic growth. Despite government support measures, the Chinese economy may grow more slowly this year than in the previous couple of years, as domestic demand weakens and growth slows in industrial output.

Foreign demand for exports from the euro area will be a little lower this year than was expected at the start of the year. This will reduce export income in the euro area and probably also the contribution of the industrial sector to economic growth. Employment remaining at high levels with wages growing and extremely low interest rates will help boost domestic demand though. Wage growth will pass into consumer prices unevenly across the euro area countries, but earlier rises in labour costs and the narrowing of the output gap will more and more start to push inflation up. The strong rise in the oil price at the start of the year will be another external factor lifting inflation.

The economic conditions of Estonia's main trading partners are good, but growth in the economies will still slow in the future. The decline in activity in the external environment has led the forecasts for GDP growth in Estonia's export partners to be revised downwards, but growth will still be faster there than in the euro area on average. Growth in the Swedish and Finnish economies will slow to around 1.5% in 2019, and the deceleration

Table 2. External assumptions in the forecast

	2018	2019	2020	2021	March 2019 projection		
					2019	2020	2021
Foreign demand growth (%)*	3.5	2.1	2.8	3.2	2.4	3.4	3.4
Oil price (USD/barrel)	71.1	68.1	65.8	62.7	61.7	61.3	60.6
Interest rate (3-month EURIBOR, %)	-0.32	-0.32	-0.32	-0.20	-0.29	-0.18	0.02
USD/EUR exchange rate	1.18	1.12	1.12	1.12	1.14	1.14	1.14

*Foreign demand growth is the weighted growth of imports of trading partners
Source: European Central Bank

tion in investment among other factors will keep it at the same level in the next year. The European Commission Spring Economic Forecast finds that the Latvian and Lithuanian economies will grow by 3% on the back of private consumption, but this rate will fall in 2020 because of weaker conditions in export markets and slower growth in domestic demand. There will also be a notable slowdown in Latvia in the use of European Union Structural Funds, but Lithuania will remain quite active in this at the same time. The estimates of export partners for the state of the economy in six months have worsened substantially.

ECONOMIC ACTIVITY

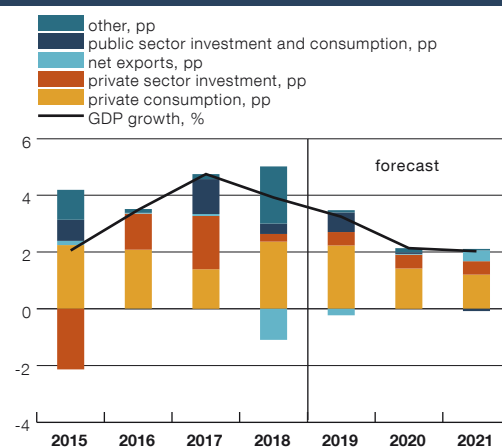
Growth in the economy is slowing. The second half of this year may see a much slower rate of growth in the economy than previous years.

Growth will remain above 3% this year, but in the next two years it will be closer to 2% (see Figure 28). The forecast assumes that the use of foreign labour will not increase and that shortages of available labour in the economy mean that growth will be restricted in future. Foreign labour has made a significant contribution to the rapid growth in the Estonian economy of recent years. The demand side will also weaken, as foreign demand will no longer grow as fast as it did some years ago and investments made with support from European Union Structural Funds are contributing less than they did in previous years.

Even with slower growth, the economy continues to do well. The strong economic growth of recent years has been notably above the potential level, and closing the output gap will take time. Stimulating the economy under such circumstances may push inflation up. The disappearance of the earlier economic growth and the loss of competitiveness will raise unemployment at the same time, especially in parts of the economy that are exposed to international competition. Branches of the economy that receive a fiscal stimulus will see continued wage pressures meanwhile, and this will then boost inflation further.

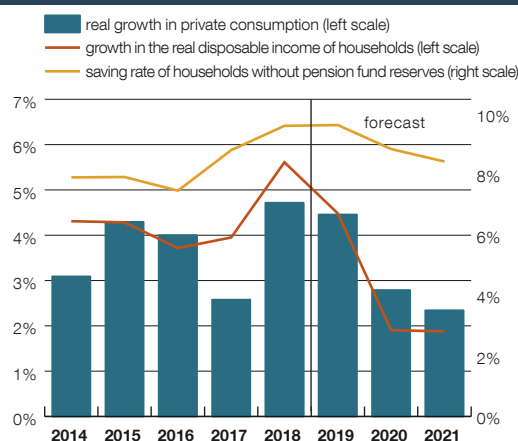
The risks to growth have increased. Growth in the economy may be restricted by risks from the domestic and external environments. A sharp

Figure 28. Contributions to GDP growth



Sources: Statistics Estonia, Eesti Pank

Figure 29. Private consumption and disposable income of households



Sources: Statistics Estonia, Eesti Pank

increase in restrictions on foreign labour would make life harder in many parts of the economy, and this could have a noticeable impact on growth in the Estonian economy. The introduction of tighter restrictions on trade between Europe and the USA would make things harder for the Estonian industrial sector. The main indicators for the economic forecast are shown in Table 3 and compared with the forecasts of other institutions in Table 4.

DOMESTIC DEMAND

Private consumption will grow at more or less the same rate this year as it did last year, though the growth in incomes will slow (see Figure 29). Household incomes will rise more slowly than they did last year, because both sala-

Table 3. Economic forecast by key indicators*

	2018	2019	2020	2021	Difference from December projection		
					2019	2020	2021
Nominal GDP (EUR billion)	25.68	27.52	29.06	30.52	0.09	0.06	0.07
GDP volume**	3.9	3.3	2.1	2.0	0.3	-0.2	0.0
Private consumption expenditures***	4.8	4.5	2.8	2.4	0.1	-0.2	0.1
Government consumption expenditures	0.3	0.9	0.7	-0.2	0.7	-0.3	-0.5
Fixed capital formation	3.3	4.1	1.6	1.8	-3.4	-1.1	0.8
Exports	4.6	3.8	2.8	3.2	1.8	-0.6	-0.2
Imports	6.2	4.3	2.9	2.8	0.9	-0.9	0.0
Output gap (% of potential GDP)	3.9	3.9	3.0	2.3	0.3	0.2	0.3
CPI	3.4	2.5	2.7	2.1	0.3	0.5	0.0
HICP	3.4	2.6	3.1	2.3	0.0	0.6	0.1
GDP deflator	4.7	3.9	3.4	2.9	0.0	0.0	0.0
Unemployment rate (% of the labour force)	5.4	4.6	5.5	6.1	-0.9	-0.1	0.0
Employment****	1.2	1.1	-0.1	-0.1	0.7	-0.2	0.3
Average gross wage (EUR)	1310	1415	1505	1584	7	20	20
Average gross wage growth	7.6	8.1	6.4	5.2	0.6	1.0	-0.2
GDP per employee	2.6	2.1	2.3	2.2	-0.5	0.1	-0.2
Current account (% of GDP)	1.8	1.4	1.3	1.4	0.6	0.9	1.0
Budget balance (% of GDP)*****	-0.6	-0.1	-0.2	-0.4	-0.3	-0.2	-0.3

* Numbers reported are annual rates of change in per cent unless noted otherwise, ** GDP and its components are chain-linked, *** including NPISH, **** employment by domestic production units; ***** the budget balance forecast considers only those measures on which sufficient information was available at the date of the forecast
Sources: Statistics Estonia, Eesti Pank

Table 4. Estonian economic forecasts by other institutions

	GDP real growth, %					CPI inflation, %				
	2017	2018	2019	2020	2021	2017	2018	2019	2020	2021
Eesti Pank	4.9	3.9	3.3	2.1	2.0	3.4 (3.7*)	3.4 (3.4*)	2.5 (2.6*)	2.7 (3.1*)	2.1 (2.3*)
Ministry of Finance	4.9	3.9	3.1	2.7	2.7	3.4 (3.7*)	3.4 (3.4*)	2.1 (2.2*)	2.2 (2.3*)	2.0 (2.1*)
European Commission	4.9	3.9	2.8	2.4		3.7*	3.4*	2.4*	2.2*	
IMF	4.9	3.9	3.0	2.9	2.8	3.7*	3.4*	3.0*	2.8*	2.6*
OECD	4.7	3.9	3.2	2.8		3.7*	3.4*	1.7*	2.3*	
Consensus Forecast	4.9	3.2	2.5			3.4	2.6	2.5		
SEB	4.9	3.9	2.8	2.5		3.4	3.4	2.3	2.2	
Swedbank	4.9	3.9	3.0	2.7		3.4	3.4	2.4	2.4	

* HICP

Source: Eesti Pank, June forecast 12.06.2019; MoF, Spring 2019 forecast 04.04.2019; European Commission. Economic Forecast. Spring 2019. 07.05.2019; IMF, WEO, April 2019, 23.04.2019; OECD, Economic Outlook, May 2018, 21.05.2019; Eastern Europe Consensus Forecasts, May 2019; SEB, Nordic Outlook, May 2019, 08.05.2019; Swedbank Economic Outlook 11.04.2019

ries and social transfers to households will grow more slowly. Growth in consumption will remain fast even so, because inflation will fall a little and households still feel confident about the future. The general expectation of households in the first months of the year was that their own economic circumstances would be very good in the coming year. A further boost to consumption growth is that the household saving rate will not rise any further for the year as a whole.

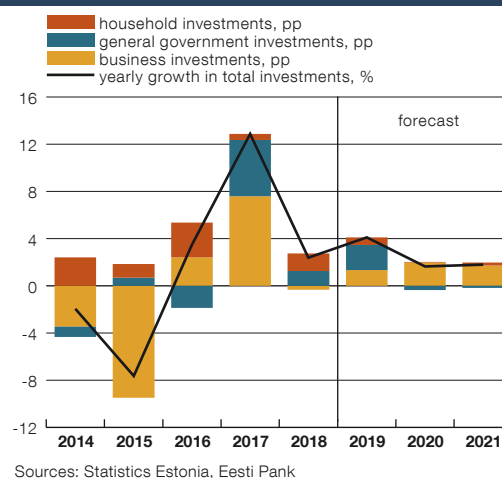
Private consumption will still grow notably more slowly in subsequent years however. Household incomes will continue to rise more slowly, because the number in employment will not rise and the growth in the average wage will slow. The rise in net household incomes will also be reined back by the income tax system, as wages will rise more and more employees will receive a gross monthly wage of more than 1200 euros, after which the monthly 500 euro

tax-free income threshold starts to be reduced. The growth in consumption will not slow as sharply as that in incomes, because the saving rate has climbed high and this gives households room to reduce it a little.

The increase in investment in residential property, which was very strong last year, will calm down in 2019 (see Figure 30). There are still several contradictory factors that affect demand and supply in the Estonian housing market. The amount of new residential space that received construction permits was down by a tenth last year, and the fall continued more gently in the first quarter of this year. This means that new living space is no longer being added as fast. The amount of space to be extended and renovated covered by permits is also down. The supply of housing is also limited by labour shortages in the construction industry. In April, data from the Estonian Institute of Economic Research showed the number of households planning to buy or build a home in the next 12 months continued its slide that has lasted for a couple of years now. Demographic factors are also not as supportive as before and suggest that demand for housing should decline, because the number of young people of the age to purchase housing will soon start to fall. Demand for housing will continue to be boosted in the short term by rising incomes and low interest rates, and it will remain quite strong and so it is probable that the supply of housing will also be large. Prices for housing will continue to grow moderately at a rate which, on average, should not exceed that of growth in incomes.

Corporate investment will grow faster in 2019 than it did in the previous year, but the outlook is more doubtful given the general uncertainty. The slower growth in foreign demand that is one of the main assumptions of the forecast is also recognised by companies in surveys by the Estonian Institute of Economic Research and this is reducing the appetite for investment. The utilisation rate of production capacity in the first half of 2019 was generally the same as last year, and this does not suggest any direct pressure to increase investment more quickly. Growth in corporate investment will be faster this year than last year because of the relatively low reference base. Despite the slight rise in interest margins, financ-

Figure 30. Gross fixed capital formation



ing options are generally good. As the economic circumstances of Estonia's main trading partners improve, it is expected that both demand and investment will grow faster.

Last year's growth in general government investment will not continue in the years ahead. Growth in general government investment in 2019 will still be supported by the use of resources from the European Union Structural Funds, but the use of structural funds will decline from 2020, and this will slow the growth in general government investment.

The capacity of the banks to lend will generally remain good in the forecast horizon, but the small competition and rising risk assessments have pushed interest margins a little higher than earlier in some loan segments. The capacity of the banks to lend is aided above all by their high levels of capitalisation and their low cost of funding. There have become fewer lenders for housing loans in the market in recent years and interest margins are relatively high, but those banks are able to meet the demand for housing loans. It is probable that the supply of consumption loans and loans aimed at small companies will increase. In contrast there are few suppliers in the segment of loans to large companies, and competition is weak. Equally, banks are being more cautious than previously in lending to some sectors like real estate. Very low base interest rates mean that loan interest rates overall still remain low. The options for companies to

access funds from the non-bank financial sector will probably also increase.

The risks related to the sources of funding of the banks are becoming harder to foresee. If the financial markets were to raise their estimates of the risks to the Nordic economies and banking groups, this would probably have an unfavourable impact on the price of funding of banks in Estonia and on the credit supply. Money laundering suspicions have so far had only a small impact on the funding of banking groups, but it is not inconceivable that this impact could increase. The banks operating in Estonia largely fund themselves from domestic deposits, and this reduces the risk to their funding. Following the changes in the banking market the role of bonds in funding the banks is also increasing. This will make the Estonian banking sector more sensitive to international bond markets and reputational risk.

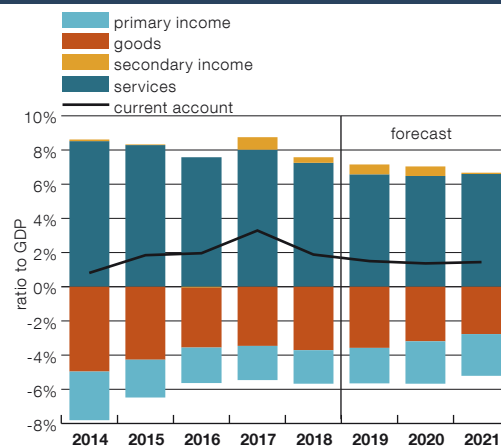
EXTERNAL BALANCE AND COMPETITIVENESS

Estonia's ability to increase its exports is more limited. Sluggish foreign demand, bottlenecks in key global issues, and stagnation about resolving them have led to rises in overall risk levels and in doubt. The forecast for exports assumes that foreign demand will continue to grow weakly in 2019 and will later start to recover gradually.

The market share of Estonian exports in foreign markets will be maintained, but it will not grow significantly. The current uncertainty and the worrying environment are not encouraging bold decisions and innovations. New markets are entered cautiously, while low levels of investment mean that the product ranges remain more or less the same and are not particularly refreshed.

The structure of Estonian export products will continue its shift towards an increase in more complex manufactured goods and services, but more slowly than before. The share in the structure of goods exports of those areas where rising labour costs have made companies like the clothes manufacturers Baltika and Sangar reduce or cease production will decline further. In contrast the share of products that compete more on

Figure 31. The current account



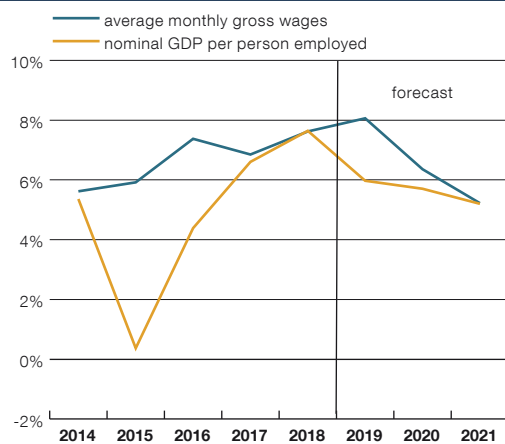
Sources: Statistics Estonia, Eesti Pank

non-price features such as taste, quality, design, or reputation, will slowly but steadily increase. Exports of services will cope better with the fall in demand and they show more stable growth, as exports of transport services increase with goods exports, while those of ICT and other business services will continue to follow the trends they have been on. In the longer term, demand for more complex industrial products and services will grow faster, as it is more dependent on rising incomes.

The position of the current account will decline a little, but it will still remain positive. Although exports will grow more slowly than imports, modest investment activity will keep growth in imports low. The nature of the economic cycle says that exports react to slowing foreign demand earlier than to domestic demand, meaning that growth in exports slows earlier than that in imports, reducing the current account position in the forecast horizon (see Figure 31).

Wages will rise more slowly throughout the forecast horizon, because the cooling of the economy will slow the growth in demand for labour (see Figure 32). The softening of demand for labour is indicated by the much weaker expectations of companies for employment in early 2019. At the start of the forecast period, wage growth will be driven by the same factors that led wages to rise fast in 2018, which are the small pool of available labour, the rise in the minimum wage, wage agreements in healthcare, and the

Figure 32. Wage and productivity growth



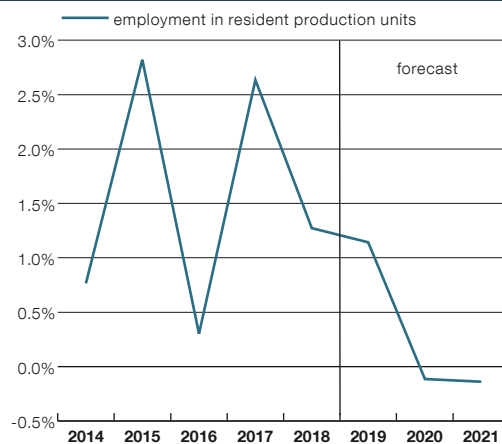
Sources: Statistics Estonia, Eesti Pank

ending of the impact of the income tax reform. In the longer term the difference between growth rates for wages and productivity will be reduced, and unit costs will rise more slowly (see Figure 33).

Much greater uncertainty than previously will be a feature of wage growth in education and public administration. The plan of the governing coalition to achieve balance in the structural fiscal position calls for wages to be frozen in those areas, but this has not been accounted for in the baseline scenario of the current forecast. Upwards pressure on wages will remain stronger in the public sector than in the private sector. The relative wage level in education remains lower in Estonia than in European Union countries with higher living standards.

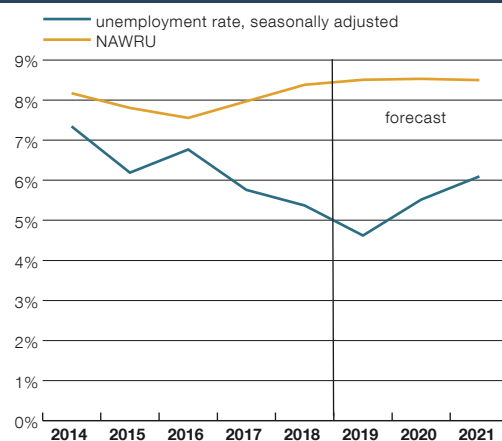
The growth in the labour supply will slow in the forecast horizon. Migration will offset the natural decline in the working age population in the forecast horizon, but the labour force participation rate will rise more slowly than earlier. The Work Ability Reform has by now been almost fully implemented and it cannot significantly increase labour force participation any further. The rise in the retirement age for both men and women, higher life expectancy, and an increase in the number of healthy life years will all have a positive impact on the participation rate. There has been an increase in the past two years in the hiring of labour from abroad alongside local labour, mainly in construction and manu-

Figure 33. Annual growth in employment



Sources: Statistics Estonia, Eesti Pank

Figure 34. Unemployment



Sources: Statistics Estonia, Eesti Pank

facturing, but also in agriculture. It is forecast that the amount of foreign labour in the economy will not increase in future.

The unemployment rate will rise during the forecast horizon, but it will still remain low in historical comparison and in comparison with the natural rate of unemployment (see Figure 34). The unemployment rate will rise because a cooling economy will put the brakes on the growth in employment, while the labour force increases a little in size. The unemployment rate will be affected in future by employment developments in the oil shale sector, where profitability has taken a hit from the rise in the price of emissions quotas and there is uncertainty about its recovery.

PRICES

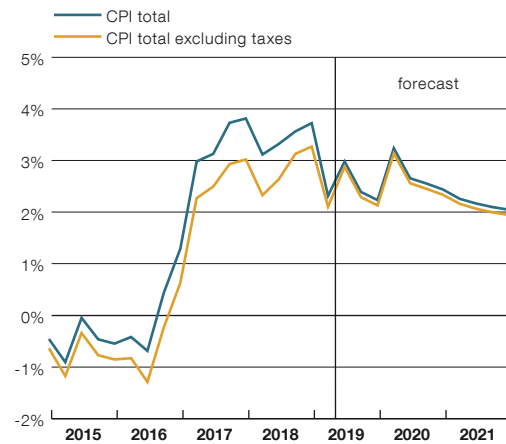
Prices are rising more slowly this year than in several previous years, at a rate of 2.5%. Inflation will accelerate at the start of next year, but the average rise in prices over the year will stay below 3% (see Figure 35). The equilibrium rate of inflation for Estonia over the next five year horizon is around 2.5% (see Box 5).

Inflation is being set by the volatility in energy prices and energy will remain the central driver of inflation over the forecast horizon. The oil price rose in the first months of the year, but futures contracts indicate that the price level of crude oil could be lower this year than last. Domestic inflation will be driven in the forecast horizon by strong growth in wages and the low rate of unemployment. Economic activity overall will be smaller throughout the forecast horizon in Estonia.

Estonian food prices depend strongly on prices in the internal market of the European Union, but also on circumstances in global markets. The higher price of meat products on global markets has emerged as a risk factor, because demand has increased in Asia. The prices of dairy products may also rise with a lag on European Union markets, as unfavourable weather has reduced output in countries in Oceania. The consumer food basket will rise in price by 3% on average this year.

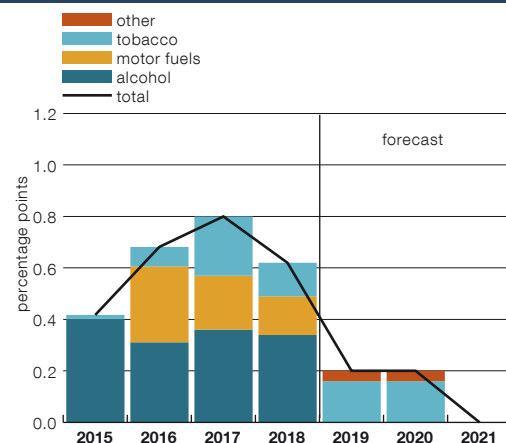
The domestic factor that will cause companies to face cost pressures during the forecast horizon will be wage growth, which most directly affect services prices. Relatively rapid rises in wages will particularly push up the prices of personal services among other services. Service price inflation slowed at the start of 2019 temporarily, probably because of the pass-through of lower oil prices. More expensive oil means that the prices of transport services could rise at a faster rate. The prices of consumer goods will continue to rise moderately throughout the forecast horizon. Price rises should be restrained by the popularity of online shopping

Figure 35. Inflation forecast



Source: Eesti Pank

Figure 36. Contribution of indirect taxes to inflation



Source: Eesti Pank

and by tighter competition. Inflation for consumer goods will be also impacted by the changes in the methodology for calculating prices of used cars¹⁶.

Inflation will also be reined back as tax rises will be smaller this year than those in several previous years (see Figure 36). At the start of last year excise rates rose for alcohol and motor fuels, and this lifted inflation by 0.6 percentage point. Tobacco excise rose at the start of this year, but the new government wants to cut excise rates for alcohol from July this year. The downward effect on inflation of the fall in alcohol excise would be of up to 0.2 percentage point this year.

¹⁶ The price level of used cars has stopped falling as the methodology for calculating the prices of used cars in the consumer price index changed this year. Cheaper prices for used cars reduced inflation for each year this decade by 0.18 percentage point, and the effect on the consumer basket of non-energy industrial goods was -0.6 percentage point.

Slower inflation rates this year will also partly be due to the high reference base of last year, as inflation this year reflects last year's price developments to a large extent. During the first half of the forecast horizon the reference base effect will restrain price rises, but it will start to

accelerate them towards the end of the year. In the coming months the effect of the sharp rise in electricity prices on the Nordic electricity exchange last year will pass out of the reference base. How the reference base affects inflation is discussed in more detail in Box 6.

Box 5: Estonia's equilibrium inflation rate

One of the many tasks of the central banks of the euro area countries is to monitor the national economies in order to identify possible economic imbalances and give warning of them. To do this job effectively, central banks use medium and long-term assessments of various parts of their economies, especially of real production and prices.

The medium and long-term inflation rate for Estonia can be estimated by finding the key explanatory factors for it using statistical data from the start of the 1990s up to 2017. These factors can be used to forecast the equilibrium inflation rate for Estonia for the next decade, which roughly equals the natural rate of price change in the economy without short-term pressures from the business cycle or any intervention from central bank monetary policy.

There are some theoretical and practical considerations that should be observed in finding the equilibrium inflation rate:

- the focus should be on the medium and long-term perspective;
- there may in theory be several explanatory factors for the medium and long-term inflation rate, such as economic growth and productivity, price flexibility, demography, state institutions, monetary policy, tax and fiscal policy, membership of economic unions, various economic forces that act over the long term such as price convergence, and others;
- it is hard to say in advance which explanatory factors will be important for the inflation rate and which will not, and the relative importance of different factors is highly likely to change over time, so that what was important in the 1960s and 1970s has no particular relevance in the 21st century;
- a central bank wanting to estimate inflation rates in the medium and long-term perspective needs to explain the relative contribution of all the potential explanatory factors to setting the equilibrium inflation rate for the country.

Analysts at Eesti Pank estimate the equilibrium inflation rate for Estonia using modern statistical methods that are based on the wide-ranging and unique database inside the bank that comprises 200 individual data collections from multiple sources. The data sources include Penn World Tables, the data set of development indicators of the World Bank, the international financial statistics of the International Monetary Fund, the International Monetary Fund's World Economic Outlook, the CIA World Factbook, the database of Freedom House, and data from many other scientific research papers and websites. The main goal of this work is to bring together the available statistical data on as many countries from around the world as possible, so that the explanatory factors for inflation rates in the medium and long-term perspective can be estimated from them on a global scale, and this can be used to estimate and forecast the equilibrium inflation rate for Estonia.

From among the factors explaining inflation rates at the global level, the Eesti Pank statistical models have shown that those that are most important in the medium and long-term perspective are the levels of incomes and prices, the exchange rate regime, the dependence of the economy on natural resources, the share of tax revenues in GDP, and the GDP growth rate and its volatility. Basing the forecast on those factors finds that the equilibrium inflation rate for Estonia is around 2.5% a year for the next five years, as the growth rate of GDP will still remain relatively fast and the price level in Estonia is below the average for the euro area. In the long term though, demographic factors become the most important. Current population forecasts together with high levels of income and a lack of price convergence with the euro area allow the assumption that the long-term equilibrium inflation rate for Estonia will be closer to 2.0%, which is also the monetary policy goal of the Eurosystem.

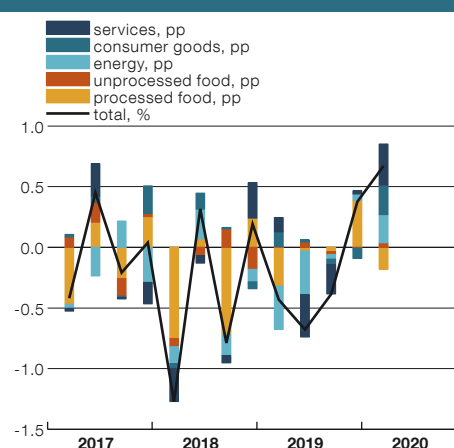
Box 6: The impact of the reference base effect on inflation

The growth in Estonian consumer prices was volatile in early 2019. The rise in prices was around 4.5% in October last year, but by March it had come down to 1.9%. A substantial part of the fall came from the high reference base of a year earlier. The reference base effect will also cause volatility in inflation rates during the forecast horizon. This box considers the concept and calculation of the reference base effect.

The reference base arises when the annual price growth of an item is strongly affected by an unusually sharp change in prices a year earlier. Inflation could have been accelerated by one-off tax changes or a sharp rise in energy prices for example. Twelve months later, when the impact of the high reference base passes out, the inflation rate can in consequence drop sharply. The opposite applies with a one-off sharp fall in prices a year earlier. This means that account must be taken both of recent price developments and of what was happening a year earlier when interpreting and forecasting the dynamics of inflation.

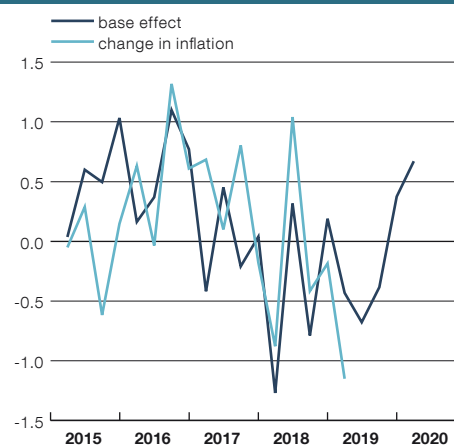
In recent years the reference base effect has mainly been caused by rises in excise, but also by the volatility in energy prices (see Figure B6.1). Food price inflation started to slow in the first half of 2018 because the rise in excise rates on alcohol and tobacco products in 2017 fell out of the comparison base. At the start of this year the reference base effect for energy prices

Figure B6.1. Contribution of components to the base effect



Source: Eesti Pank calculations

Figure B6.2. Base effect and inflation



Source: Eesti Pank

was negative, meaning it slowed inflation, because prices rose in the first months of last year for motor fuels and for electricity. The reference base will continue to hold inflation down in the coming months because the price of electricity rose on the Nordic electricity exchange in summer 2018 to the highest level seen for several years.

At the end of this year the reference base will again start to raise inflation (see Figure B6.2). This is mainly because of the wide volatility of inflation for food products and for services. The reference base effect will raise inflation by 0.4 percentage point in the fourth quarter of 2019 and by 0.6 percentage point in the first quarter of 2020.

Calculation

The percentage change in the yearly rise in consumer prices (π_t) is found by comparing the consumer price index (p_t) with the price level of 12 months earlier (p_{t-12}):

$$\pi_t = \frac{(p_t - p_{t-12})}{p_{t-12}} \times 100$$

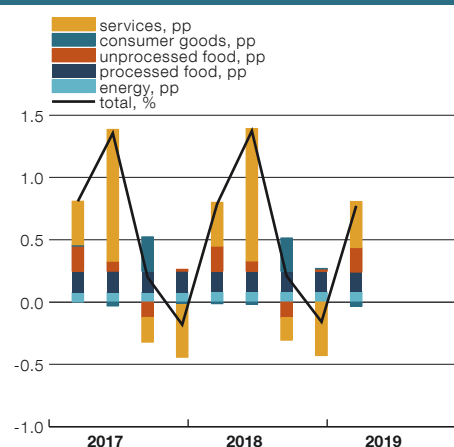
The change in the yearly rise in consumer prices is then observed as the difference between the monthly price changes this year and last¹⁷:

$$\pi_t - \pi_{t-1} = \left[\frac{(p_t - p_{t-1})}{p_{t-1}} - \frac{(p_{t-12} - p_{t-13})}{p_{t-13}} \right] \times 100$$

This equation shows the monthly price growth in the previous year plays a major part in the dynamics of inflation. Consumer prices in February 2019 were 0.17% higher than in January for example, while in 2018 prices were 0.91% higher in February than in January. This means that the yearly growth in the consumer price index was slowed in February 2019 by 0.74 percentage point ($-0.74 = 0.17 - 0.91$).

As the reference base effect comes from unusual price changes in the previous year, there arises the empirical question of how to measure them. This is done by removing the regular seasonal effects and long-term price trend from the monthly changes to the consumer price index (see Figure B6.3) to leave the irregular changes, which could be regarded as the base effect. As the prices of some CPI categories, such as energy and processed food, do not follow a regular seasonal pattern, only the long-term trend can be extracted. The seasonality of services prices is multiplicative, meaning it tends to increase gradually from year to year. The long-term trend is found in this box using the arithmetic average of the monthly price rises for 2010-2019, but alternatives such as the Hodrick-Prescott filter could also be used instead.

Figure B6.3. Regular price growth



Source: Eesti Pank calculations

¹⁷ Base effects and their impact on HICP inflation in early 2005, ECB monthly bulletin 1/2005.

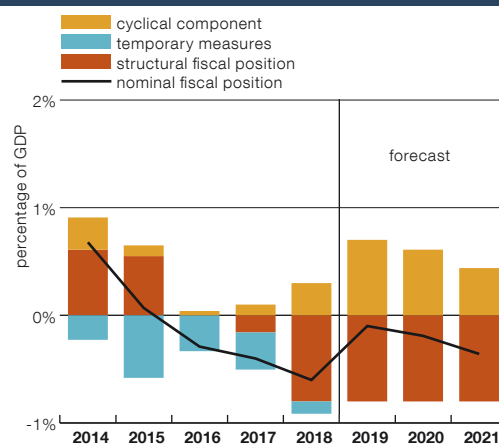
GOVERNMENT FINANCES

As economic growth slows, so will the growth in tax revenues. The general tax burden measured as a ratio to GDP will fall a little in future. The gradual transition to lower corporate income tax for companies paying regular dividends will continue, while the cut in excise on alcohol means growth in excise revenues will be minimal, and the growth in the economy will not be as tax-rich as it was. The decline in the tax burden will partly be offset by the increase in the effective personal income tax rate caused by rapid wage growth. It was also evident in 2018 and in the first months of this year that many taxpayers are making consistently less use of the tax-free income threshold than they have the right to. The overall tax burden will fall to 33% of GDP. A large number of tax changes came in last year and it cannot be argued decisively that the behaviour of taxpayers in the new tax environment has already become clearly fixed. This means the probability of forecast error is higher than usual.

Spending continues to rise fast. Wage growth remains strong, social transfers will increase because of indexes reflecting the good position of the economy in the recent past, and indicators for last year show the share of investment funded by the own funds of general government units to be larger than previously. Transfers from the European Union budget will also be at their peak level at the start of this forecast period. Overall spending by the general government will grow more slowly, but it will still be too fast given the position of the economic cycle and the forecast growth in revenues.

The fiscal position of the general government deteriorated last year. The growth in spending was faster than forecast in the final months of the year, tax measures did not increase revenues by as much as was hoped, and the growth in non-tax revenues was also below expectations. Continued relatively fast growth in spending and a declining tax burden will keep the general government budget in a small deficit throughout the forecast horizon. As growth in the economy

Figure 37. General government fiscal position



Sources: Statistics Estonia, Eesti Pank

exceeds its long-term sustainable level in future, there will be a persistent structural deficit. This means the economy is being stimulated at a time when the private sector does not need support (see Figure 37).

The structural fiscal deficit of the general government, which was larger than expected last year, will be repaired too little in future. The fiscal rules call for the general government structural fiscal position to be improved by at least 0.5% of GDP a year. The baseline scenario of the Eesti Pank forecast was prepared at a time when the new government coalition programme had not yet been finally fixed, and it was not known what steps the government intended to take to improve the fiscal position.

At the end of May the government passed its updated budget strategy for the next four years, which sets the goal of returning the general government budget to structural balance from 2021. The government plans to achieve this through several measures to increase revenues and limit spending in 2020-2023. Eesti Pank considers that the growth rates for spending are being cut too little to return the budget to structural balance, and fiscal policy will be too loose for the position of the economic cycle even after the measures to improve it have been taken.