The Crisis in Europe

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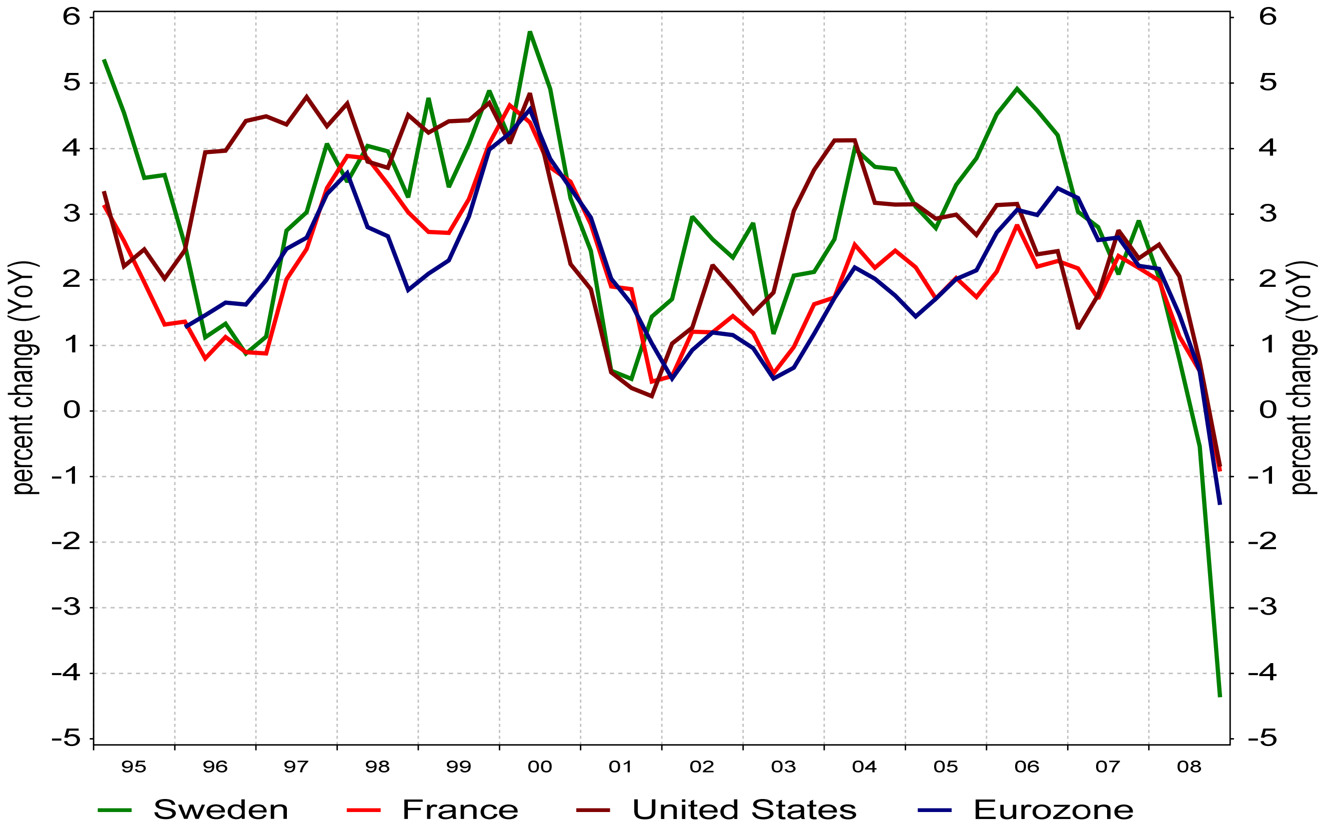
The economic crisis in Europe

- Financial sector problems
- GDP is falling during 2009
- Unemployment is increasing the coming years
- Public finances deteriorates

Gross domestic product

Percent change, 1995-2009, Source: Eurostat, U.S. Department of Commerce



Nordic-Baltic region hit hard

- Small open economies with high export levels
- Export based on raw materials and investment products
- Baltic and Icelandic economies overheated
- Close economic and financial links

The Government's aim

- Mitigate the financial crisis
- Meet the economical downturn
  - Automatic stabilizers
  - Expansionary economic policy
    - Measures should be in line with structural reform agenda
    - Temporary, targeted and timely measures
- Uphold the sustainability of public finances, the welfare system and employment rates

The Government’s measures to restore the financial system

- Secure liquidity and deposits
  - The Riksbank guarantees liquidity
  - Increased ”guarantee of deposits”
  - A state guarantee scheme
- Solutions for insolvent banks
  - Stability fund, authorities and legislation in place
- Capital injections to solvent banks
- Extended credits to enterprises
  - Guarantees to export credit authorities
  - Increased lending to enterprises
  - Support for the automotive industry
  - Deferment of taxes

Framework for state support to banks based on experiences from the 1990's

- Government Support to Credit Institutions Act gives the Government a broad mandate to take action
- Measures depend on status of the institution and the market:
  - Guarantee scheme and recapitalization scheme for fundamentally sound institutions to support lending
  - National Debt Office to intervene if a financial institution should get into serious difficulties, state capital provided through preferred shares with strong voting rights
  - Possibility to take over ownership of institution with less than ¼ of regulatory capital
- The measures that can be taken have been designed to safeguard taxpayers' interests and secure financial stability

State ownership a central resolution issue

- Brings efficiency in management and state control of restructuring
- Ensures confidence in state intervention and support measures
- Gives political advantages – safeguards taxpayers interests and public finance – the systemic stability to be saved, not individual banks

The Government's measures

- Reforms in budget in line with long term structural agenda and the business cycle
  - Tax cuts (for individuals and enterprises)
  - Investments in health care, infrastructure, education and R&D
- Temporary, targeted and timely measures
  - Active labour market policy
  - Support to the municipalities

Europe's challenges ahead

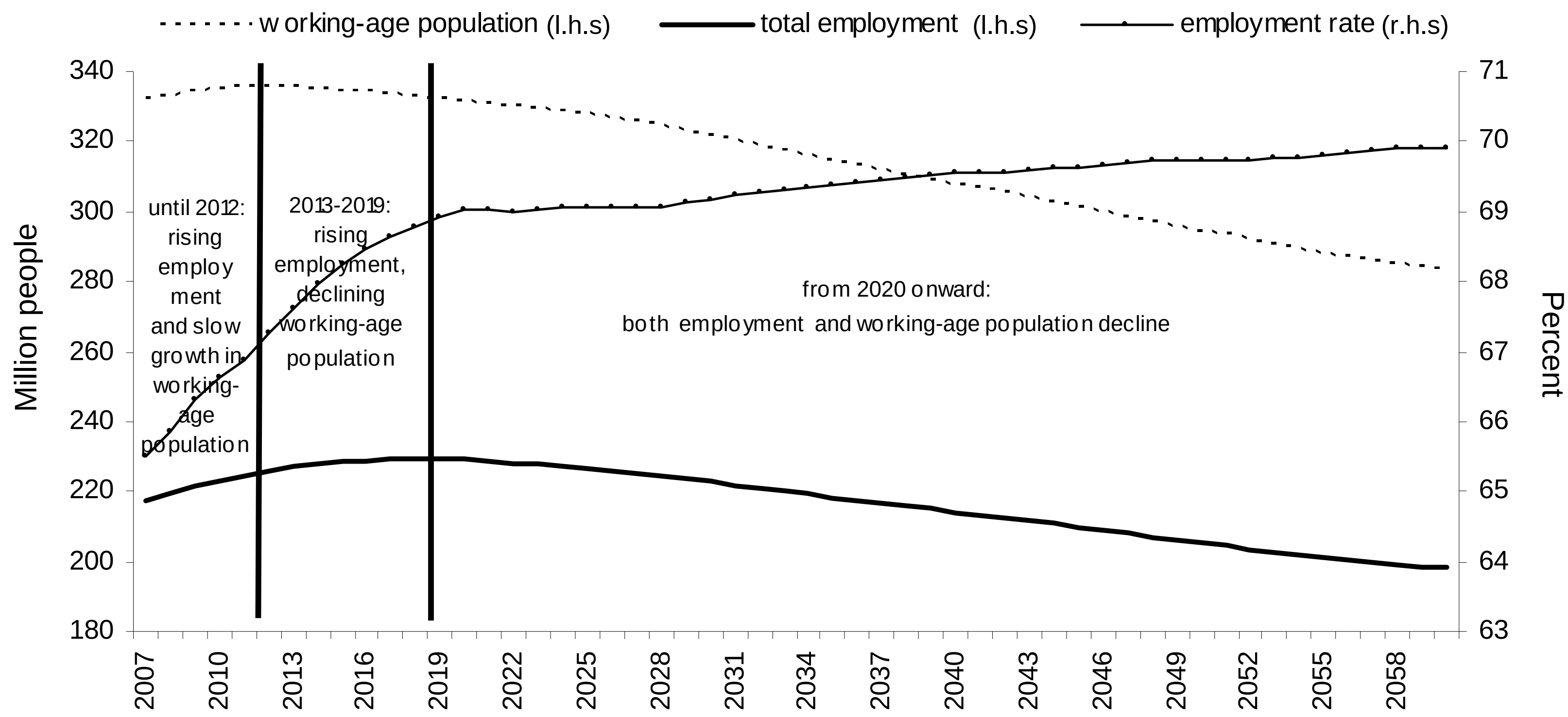
- Ageing society
- Deteriorating public finances with increasing debt levels
- Rising unemployment levels and risk of persistence

Europe’s demographic challenge

- Europe’s population is ageing…
  - The old-age dependency ratio in the EU is expected to rise from 25 percent today to 54 percent in 2060
  - According to *The 2009 ageing report* age-related government expenditures in the EU are set to rise by 4,7 percentage points of GDP 2007-2060 in the absence of further reforms
  - Around 1/2 of the increase is due to higher expenditures on pensions and 1/3 due to higher expenditures on health care
- …and our window of opportunity is closing
  - Delaying reforms imply that stronger measures are required further ahead

Employment growth remains possible for the next 10 years only

Employment rate in percent, 2007-2060, Source: European Commission

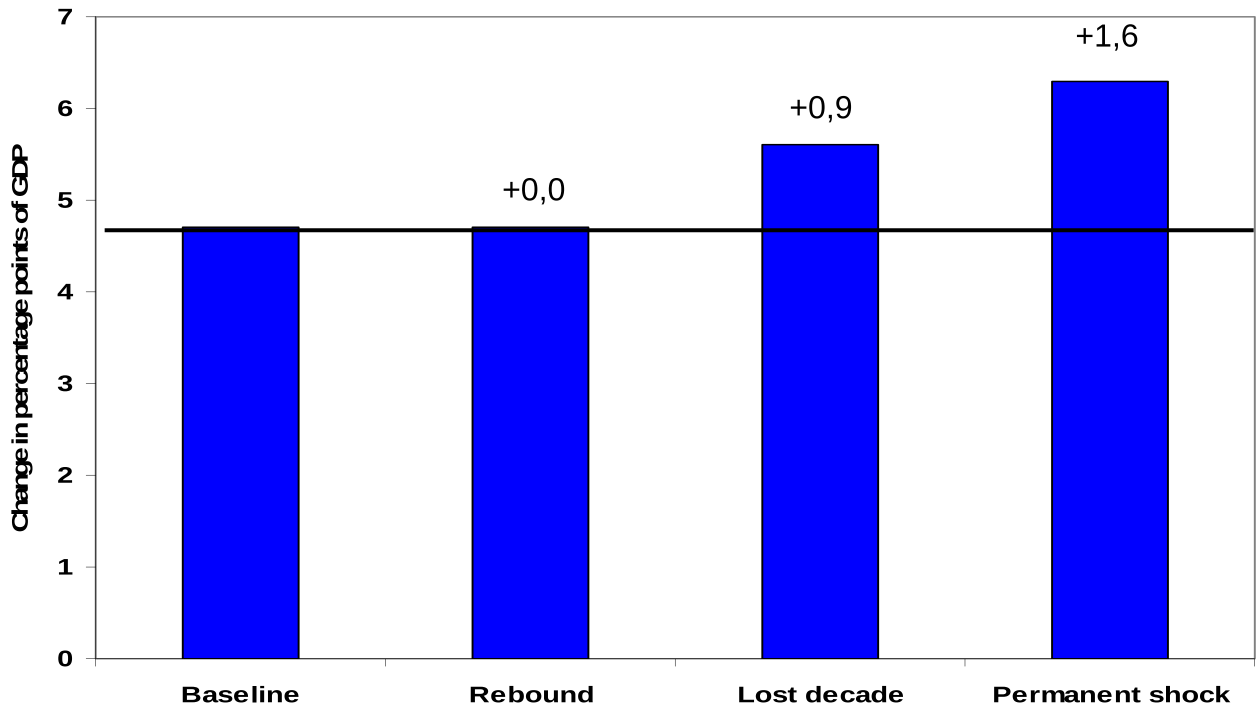


The current crisis could aggravate the demographic challenge

- If the crisis turns into a permanent shock to potential growth age-related costs could rise by 1,6 percentage points of GDP over the baseline
- Policy measures are required to ensure that the crisis does not turn into a permanent shock to employment and labour productivity

A permanent shock increases the long run costs of ageing

EU27, Cost of ageing, 2007-2060, Source: European Commission



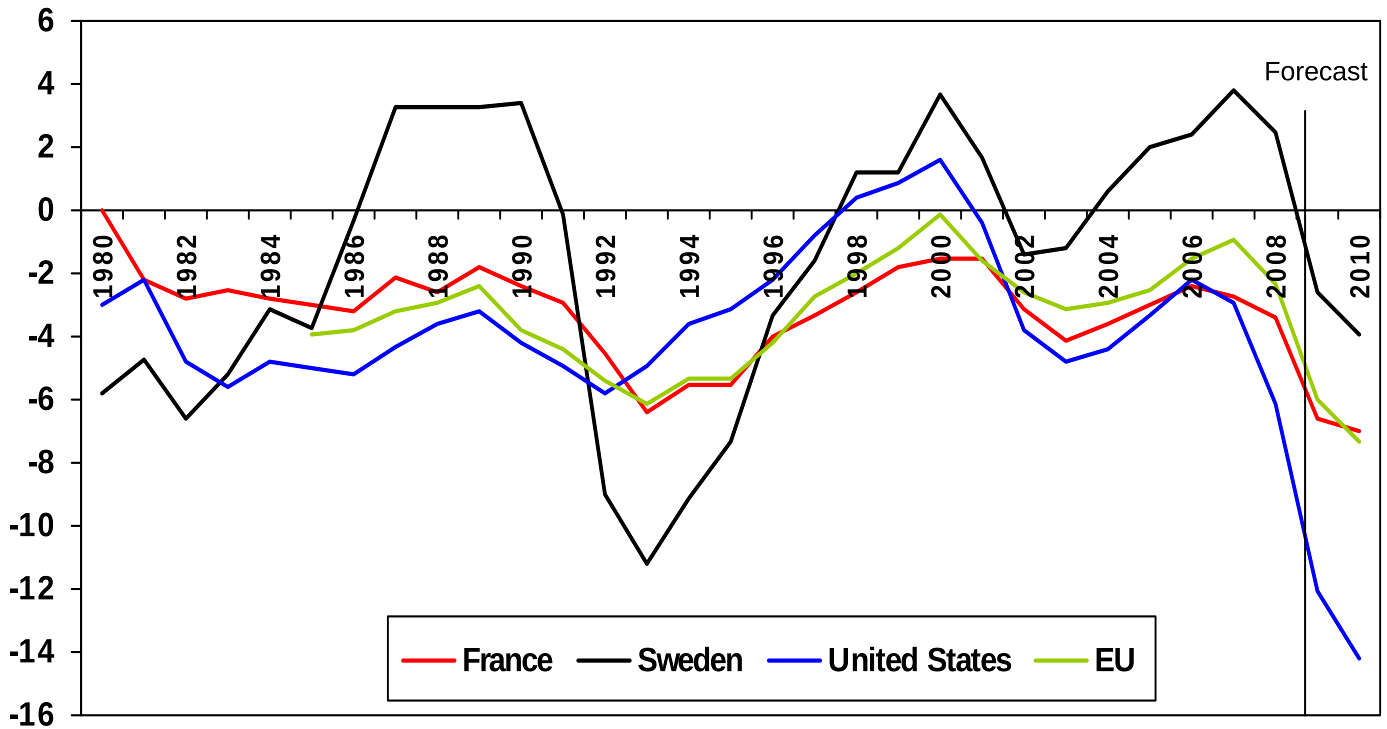
Public finances in EU have deteriorated substantially since last autumn

- The aggregate general government deficit in EU is in the new forecast expected to be -6.0 percent 2009 and -7.3 percent 2010. An increase of the deficit with 3.7 and 4.7 percentage points since the forecast in November

- The government debt is rising to 72.6 percent of GDP 2009 and 79.4 percent 2010 according to the new forecast. An increase with 11.7 respectively 17.6 percentage points since November

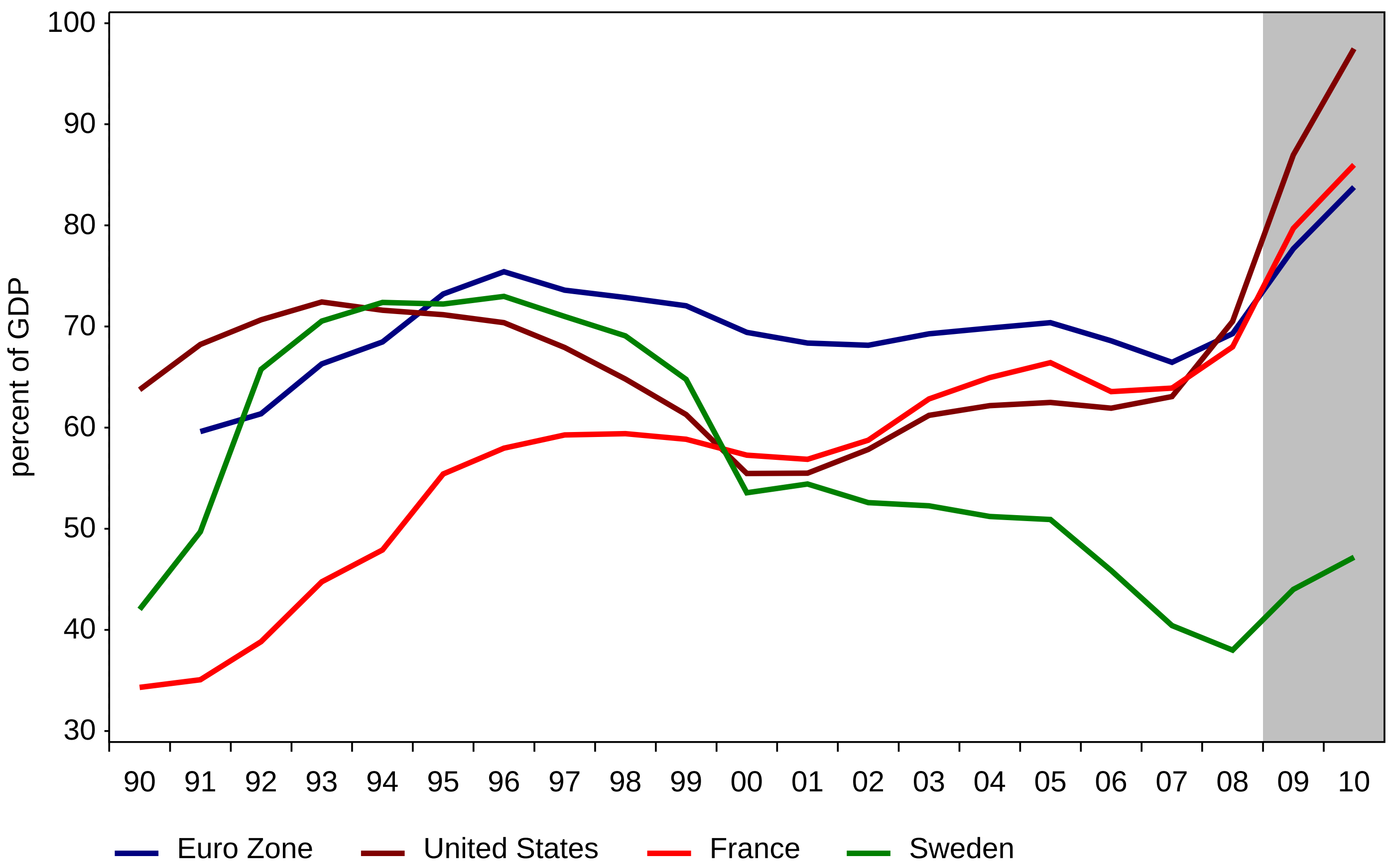
General government net lending

Percent of GDP, 1980-2010, Source: OECD, European Commission



General Government Gross Debt

Percent of GDP, 1990-2010, Sources: OECD, IMF, European Commission

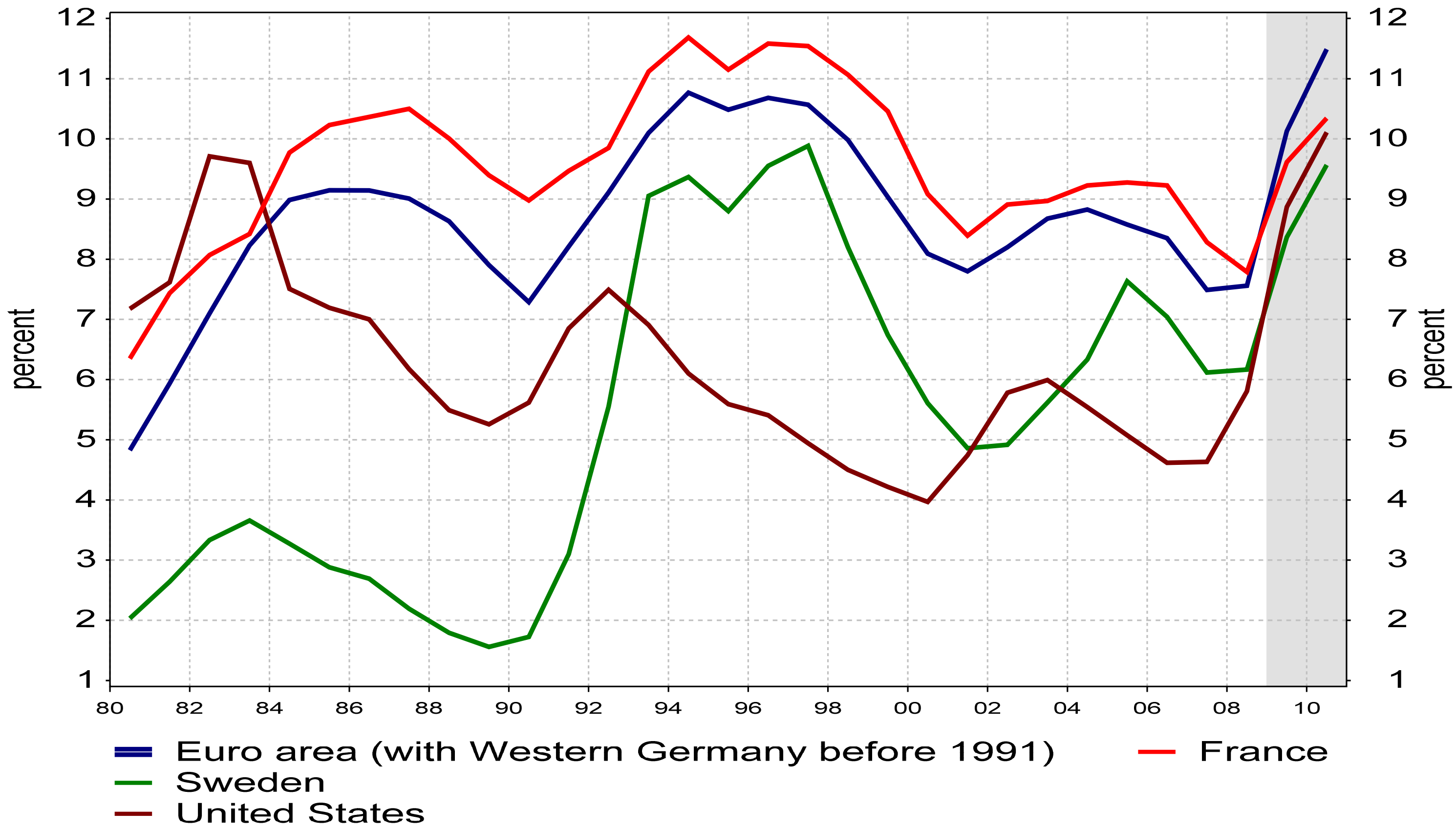


The unemployment rate risk getting stuck on a high level

- Changes in skills, motivation and search behaviour during an unemployment spell can trigger long-term unemployment
- “Insiders” demand wage-increases that reduces the demand for labour
- Increased economic turbulence in the presence of high unemployment benefits
- Some evidence suggests that unemployment persistence may be higher in Europe than in the US

Unemployment rates

Percent, 1980-2010, Sources: OECD, IMF WEO



Prohibit that the unemployment rate get stuck on a high level

- Safety during adaption
- Keep the motivation for applying for a work up
- Encourage professional and geographical flexibility
- Active labour market policy for the unemployed
  - Job search assistance
  - Practice
  - Training
  - Wage subsidies and guarantees

Conclusions

- Important that policy measures are taken to ensure that the crisis does not turn into a permanent shock to employment and labour productivity
- Important to secure sustainability in public finances in order to ensure stability
- Important that the unemployment rate is not stuck on a high level