

Erkki Liikanen: Major structural change in the Finnish economy

Speech by Mr Erkki Liikanen, Governor of the Bank of Finland, at the 70th anniversary of Oras (a Finnish company), Helsinki, 7 May 2015.

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1949s and 1950s

After the Second World War the Finnish economy and society was in front of huge challenges: 10 % of the population had to be relocated from Karelia which we lost to Soviet Union. The war reparations paid to Soviet Union in 1945–1951 accounted for 2–6 % of the GDP annually. In the first post-war years, the reparation costs constituted almost a quarter of all government expenditure.

Still, Finns had a lot of confidence on the future. The most striking example was the baby boom. Over 100 000 babies were born in 1945–1949 and still in 1950 close to 100 000. The baby boom had a deep impact on the society and economy then and still has. The high birth rate further boosted the need for new homes. In addition to residential construction, also public construction was booming, as new schools were needed.

Encouraged by the favorable domestic demand conditions, new entrepreneurs entered the market during the years of the baby boom. Erkki Paasikivi was one of them and in 1945 founded Oras in Rauma.

The Finnish economy was growing rapidly also in the 1950s. But the export-led growth was more volatile reflecting the international business cycle. The Korean boom in 1950 and 1951 and recession in 1952 had a deep impact on the forest industry and its supply chain.

Oras instead grew from 15 employees in 1950 to 20 in 1952. It was still a small company, but it already went actively abroad and especially to Germany to get the best available technologies.

A fundamental problem for Finland at the time was the choice between savings and consumption. To improve long-term growth prospects, more investment was needed. The new investment were mainly funded by domestic savings by postponing consumption. Many Finnish people seemed to be more interested to improve their standard of living here and now.

Obviously Erkki Paasikivi realized early the importance of postponing consumption. The profits from their business was retained in the company and invested for growth. Investments in R&D were made and productivity was improved.

1960s and 1970s

Major structural changes in the Finnish economy accelerated in the 1960s and early 1970s. Finland transformed from an economy dominated by agriculture to an industrial country. Migration from countryside to cities increased, as the baby boomers were entering the labor markets.

As many as 30 000 new homes were built every year in the 1960s. A third of them were government subsidized ARAVA homes. People all over the country were building their own houses. Living standards of the Finnish people were growing rapidly. One sign were modern bath rooms and saunas with showers built in the new homes.

My family was a typical case. I was in a primary school, when my parents built our own Arava house in Mikkeli in 1959. We got the running water and sewerage only in 1963. Then came the first products from Rauma into our home in Mikkeli.

The world economy grew steadily in the 1960s and still in early 1970s. Finland had already joined the IMF and World Bank in 1948, and GATT in 1949. In 1961 Finland was accepted as an associate member in EFTA. Thus Finland was able to guarantee that her industry had access to export markets equal with Sweden. So the Finnish economy was able to integrate with the Western world at the same time when the bilateral trade with the Soviet Union was important for our exports.

Deeper integration to international trade not only helped Finnish companies to enter new export markets but also facilitated technological spillovers from abroad to help Finland in catching up the technology gap with the more advanced economies.

International competition also posed new challenges for the Finnish economy, as low cost countries entered the markets for low-end products. Competing only or mainly with price would mean decreasing the wages and the living standards. The other option was to use more advanced technologies and to introduce products with higher quality. This was the policy Oras followed.

1980s

In 1988, as a young minister of finance I visited Oras in Rauma for the first time. I learned a lot then and even more last weekend when I had a chance to read the new excellent history of the company written by Timo Herranen. Many investments were taking place at the time in Rauma and atmosphere was positive.

Pekka Paasikivi was running the company during my visit. Jukka and Jari Paasikivi had also important responsibilities in the firm. What impressed me most in the factory? Actually, there were four things.

The first was how complex a product a faucet actually was. And this was well before the ICT revolution.

The second were the casual industrial relations in the factory at the time. There was a very low hierarchy.

Thirdly, I remember, how big a role was given to design. I am happy to hear that Jorma Vennola, the designer whose style we all know, is here with us.

And fourthly, an important focus of Oras was on internationalization.

All in all, it was also important to learn that a family company can grow fast when it is growth- and innovation -oriented and profits are retained in the company to finance growth.

Generally, the sentiment in Finland was gradually turning more international in the 1980s. The Finnish companies started to go international not only by establishing new sales units, also by making acquisitions to enlarge their market shares. A number of family-owned companies followed this path. Oras was among them. It was not possible to maintain the high pace of growth by a company mainly based in Finnish markets. They had to seek growth from abroad.

Also the drivers for economic growth were changing in the 1980s: According to professor Matti Pohjola, up until the mid-seventies investment of physical capital was the main driver of productivity and growth in Finland. It was only from the end of 1970s onwards, when human capital, like investments in education and R&D started to dominate.

One of the trends of the late 1970s and the early 1980s was that the baby boomers were increasingly entering the top positions in business and politics. In Oras, the new generation was also taking the lead, as Pekka Paasikivi was nominated as the new CEO of ORAS in 1979.

1990s

In summer 1990 I moved with my family moved to Brussels. When we arrived at Zaventem airport, we were welcome by Oras faucets in the toilets. Later I went to see a football match in Anderlecht. In the stadium we saw a small billboard of Oras: the red color and a faucet was easy to recognize. Later we understood that to win market shares was not as easy.

When we left Brussels in 2004, the faucets were in the news. The cartel case on faucet market had just been opened. Oras was not part of the cartel of a number of European companies. They were severely fined by the European Commission a few years later.

The domestic depression of the 1990s was deep in Finland. High interest rates and the later devaluations of markka hit many companies and bankruptcies went up. The collapse of trade with the Soviet Union had its important role. GDP fell steeply and unemployment grew fast.

Unlike many other Finnish companies, Oras had not taken major risks in its foreign operations. So it avoided exchange rate losses but benefited from improved competitiveness. Trade to the Soviet Union had a smaller role for the company than for many others. So in the difficult conditions of depression, Oras did relatively well.

The depression of the 1990 was deep but not very long. The pre-recession level of the GDP was reached in 1995, and the era of Nokia-Finland was about to start. Also the integration process of Finland with the Western Europe was completed, when Finland joined the European Union in 1995.

The early 1990's were a turning point not only to the ICT industry but to the Finnish economy as a whole. Up until the depression, the Finnish companies typically adapted more advanced technologies from abroad. In the early 1990s, this catching up process, was largely completed. Thus, instead of catching up the technological frontier, the Finnish manufacturers themselves had to push that frontier forward.

In its own industry, Oras has been pushing that frontier forward in the 1990s and at the same time it came more and more international. After acquisitions the personnel grew above one thousand.

2000's

At the turn of the millennium, the growth paths of Oras and the Finnish population started to diverge. Whereas Finland started to grey, Oras continued to grow. And in a new way.

Major investments were made in public companies while staying firmly as an industrial enterprise. Also brothers Pekka, Jukka and Jari Paasikivi reorganized their division of work.

The baby boomers started to reach retirement age so that in the end of the decade, the working age population turned to gradual decline.

New history of Oras gives also an interesting window to labor relations in different times. According to the history also the management says that it has made some misjudgments. Early retirement schemes were not successful, because a lot of silent senior knowledge left the company.

Relations with the unions have mostly worked but there have also been occasional tensions between the employer and the trade union. In the 1970's, one reason was internal political struggle within the union.

I am happy to see here Keijo Huunonen and Esko Sillanpää whom I learned to know well also from the book. Recently the company has responded to the aging problem and the looming shortage of work force with its own way. Oras has created a program that aims to support the work ability and transfer of skills from senior workers to younger cohorts. Interesting and positive innovations, not always without problems.

Thus, in 2014, the average retirement age in Oras was over 63 years, which is two years more than the national average.

The way forward?

The global economic outlook is challenging. According to the IMF outlook from two weeks ago, the recovery of the world economy continues, but it is happening slowly. In the short term, the decline in the price of oil, along with the adjustment of exchange rates are boosting the recovery.

The emerging economies grow slower this year than in the last year. Russia is falling and also Brazil has difficulties. China continues to grow, but not as fast as before. India is keeping the pace, because it is benefiting from lower oil prices and its population growth.

USA grows, in spite of recent signs of softness. Euro area is improving, too. The lower oil prices and ECB's monetary policy, along with the exchange rate movements, support growth. Also fiscal consolidation has proceeded and is not the same sort of drag in the future as before.

The question today is: Will Finland be able to benefit from the recovery of euro area?

We are facing four major challenges.

1. The economic crisis has hit us hard, but it was not the financial crisis. Our banks and financial markets have continued to function properly. Instead, our economy has entered a phase of major structural change, due to the recent fall in the share of the ICT sector and the decreasing consumption of certain important categories of paper.
2. Finland has lost part of its competitiveness since 2007. Our unit labor costs have grown more than 10 % higher than those of our competitors.
3. Retirement of baby boomers means that our labor force is shrinking 0.5 % a year for still one decade ahead.
4. Due to the fall of the GDP, our public sector is bigger than our national economy can well finance in the medium and long term.

And in addition to this, a geopolitical crisis has taken a toll of our growth.

What can we do? What do we have to do?

In June 2011 I invited with Timo Kalli, the chairman of the Parliamentary Supervisory Council two businessmen and a new M.P. who was a former businessman to Bank of Finland to discuss the economic situation. One of the businessmen was Jari Paasikivi from Oras, who is having its 70th anniversary today and the new M.P. was Juha Sipilä, who forming a new government today. The agenda has developed but not fundamentally changed.

We have three major tasks.

1. We need to restore cost competitiveness of our economy. This is the pre-condition to create growth and jobs. Social partners.
2. We need to make structural reforms to promote growth and improve possibilities to create jobs. Here the new government needs to move fast with decisions and their implementation.
3. We need to consolidate our public finances. We cannot move a growing debt burden to our children and grand-children.

Here we need a strong government and functioning relations between social partners.

Today I want to congratulate Oras for its 70-year history. I want to extend my congratulations to all in the company, the employees, the management, and the owners. The success has required major efforts for a long time from all of them. Thank you!