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FINLANDS BANK
EUROSYSTEMET

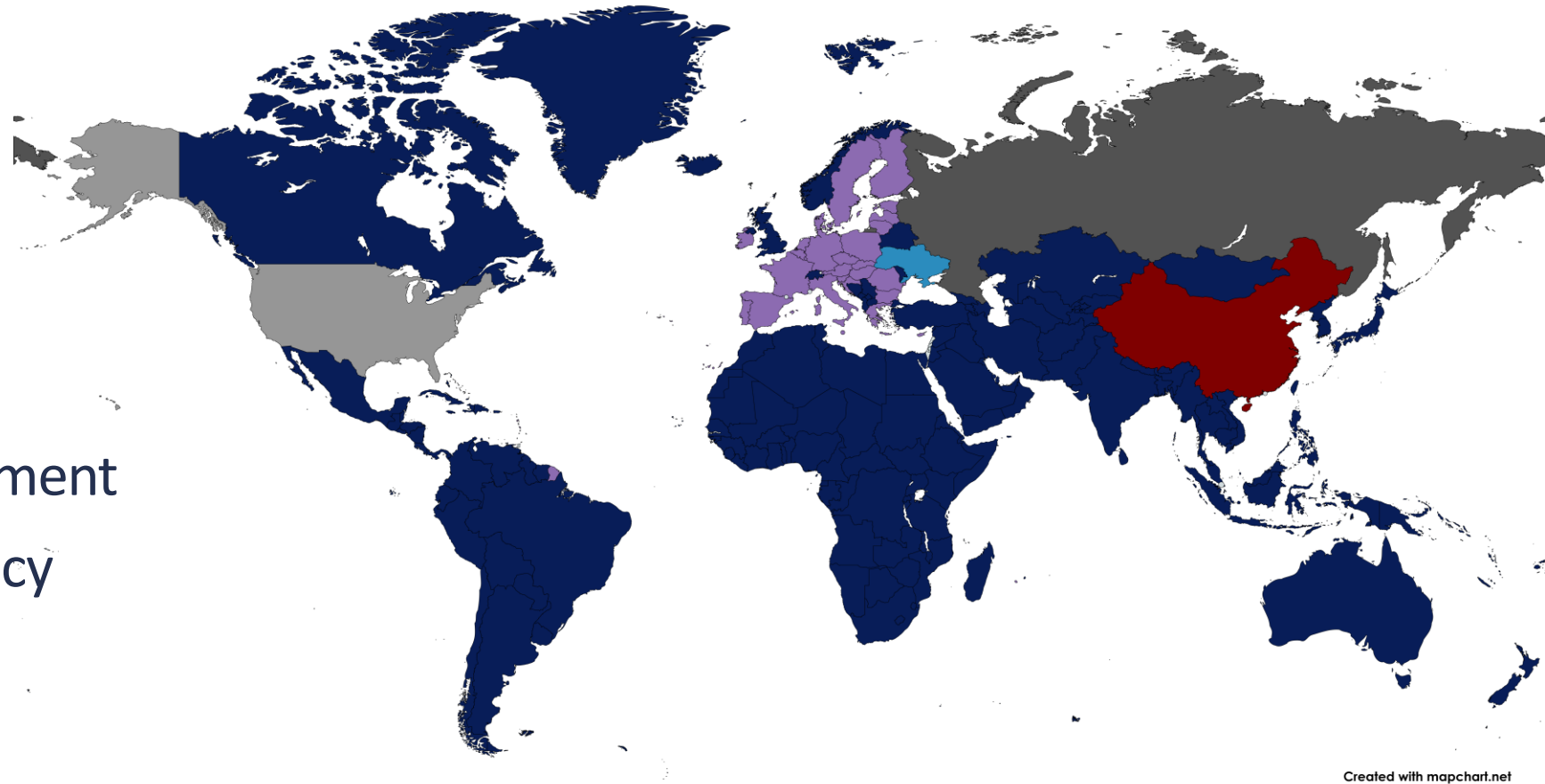
Europe's economy under the weight of power politics

The Bank of Finland's biannual lunch for EU Heads of Mission
2 June 2026

Governor Olli Rehn
Bank of Finland

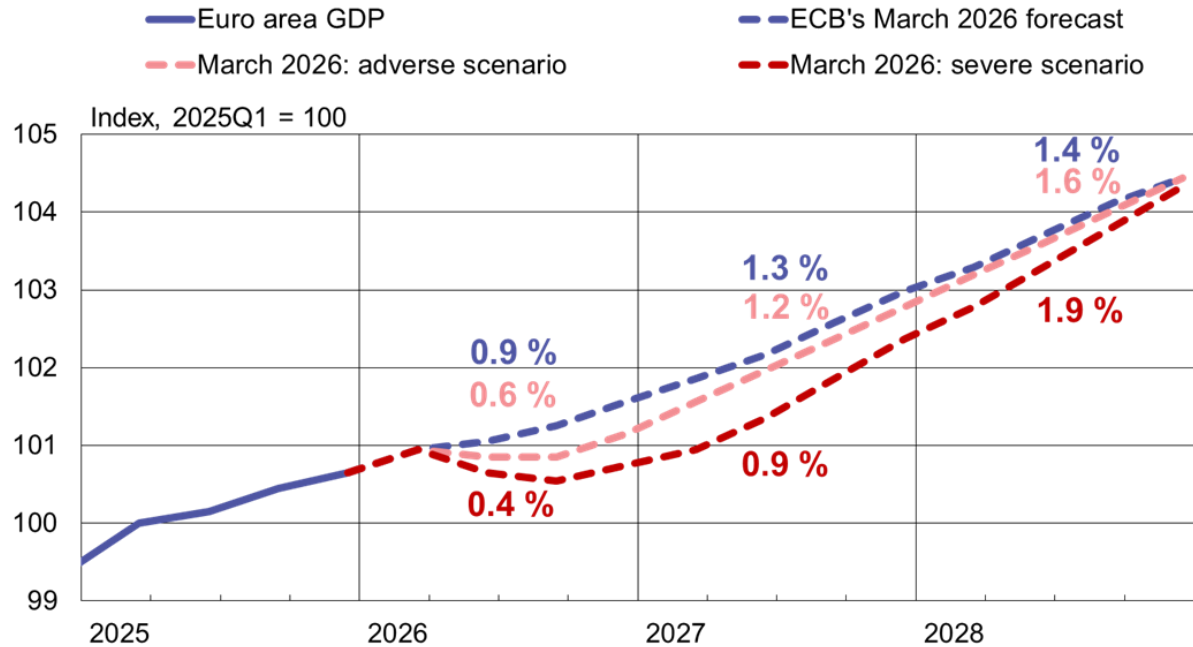
Geopolitics is casting a shadow over Europe's economic performance

- Middle East and global energy markets
- War in Ukraine
- Greenland
- European defense investment
- U.S. Tariffs and Trade Policy
- China and Taiwan



War in the Middle East slows euro area growth and accelerates inflation

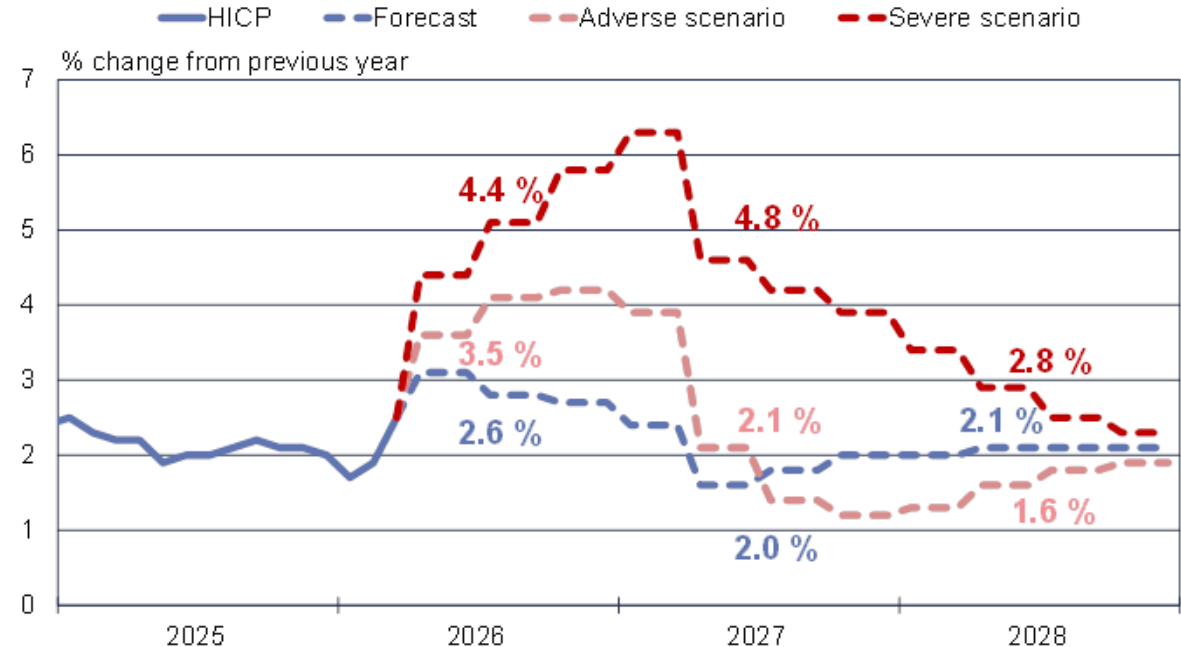
ECB's March 2026 macroeconomic projections



Figures next to the curve are annual growth rates, %.
Sources: Eurostat and ECB.

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Euro area inflation, ECB's March 2026 forecast



Sources: Eurostat and ECB.

Euro area medium-term inflation expectations derived from swaps remain anchored near 2%, while US expectations are slightly higher

Market-based inflation expectations* in the euro area

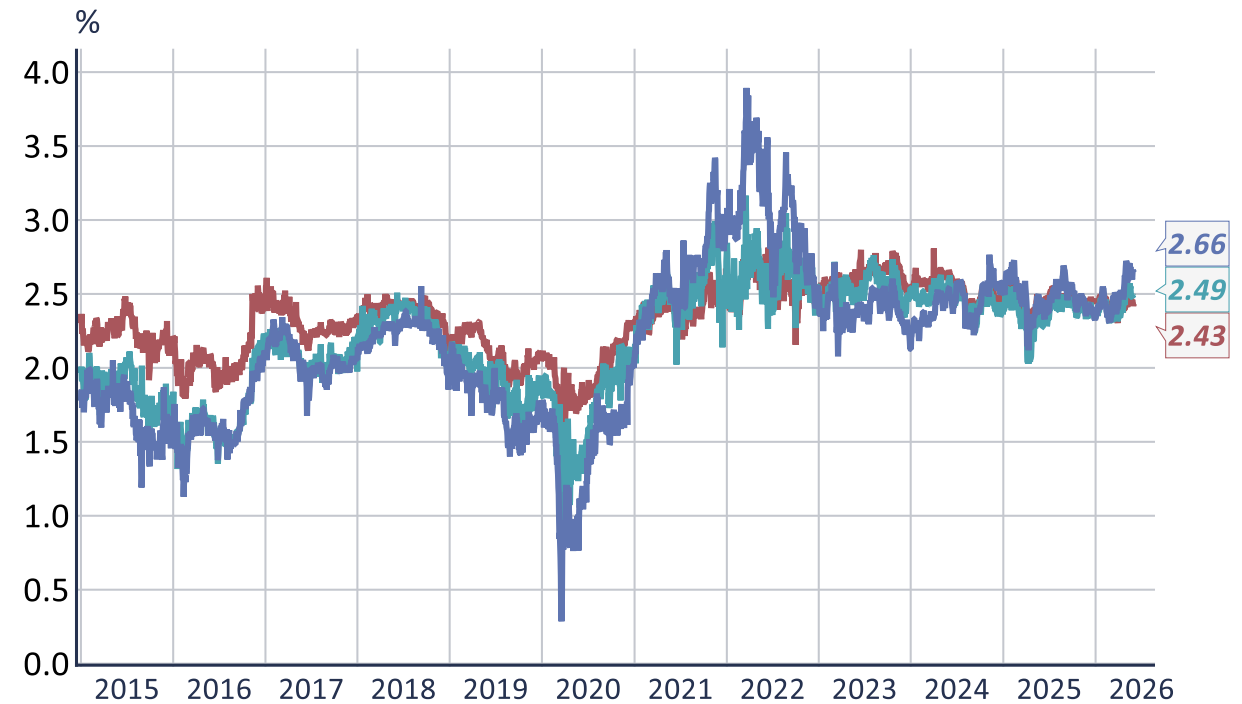
— 1y after 1y — 1y after 3y — 5y after 5y



Source: Bloomberg. *Expectations derived from inflation swap rates.
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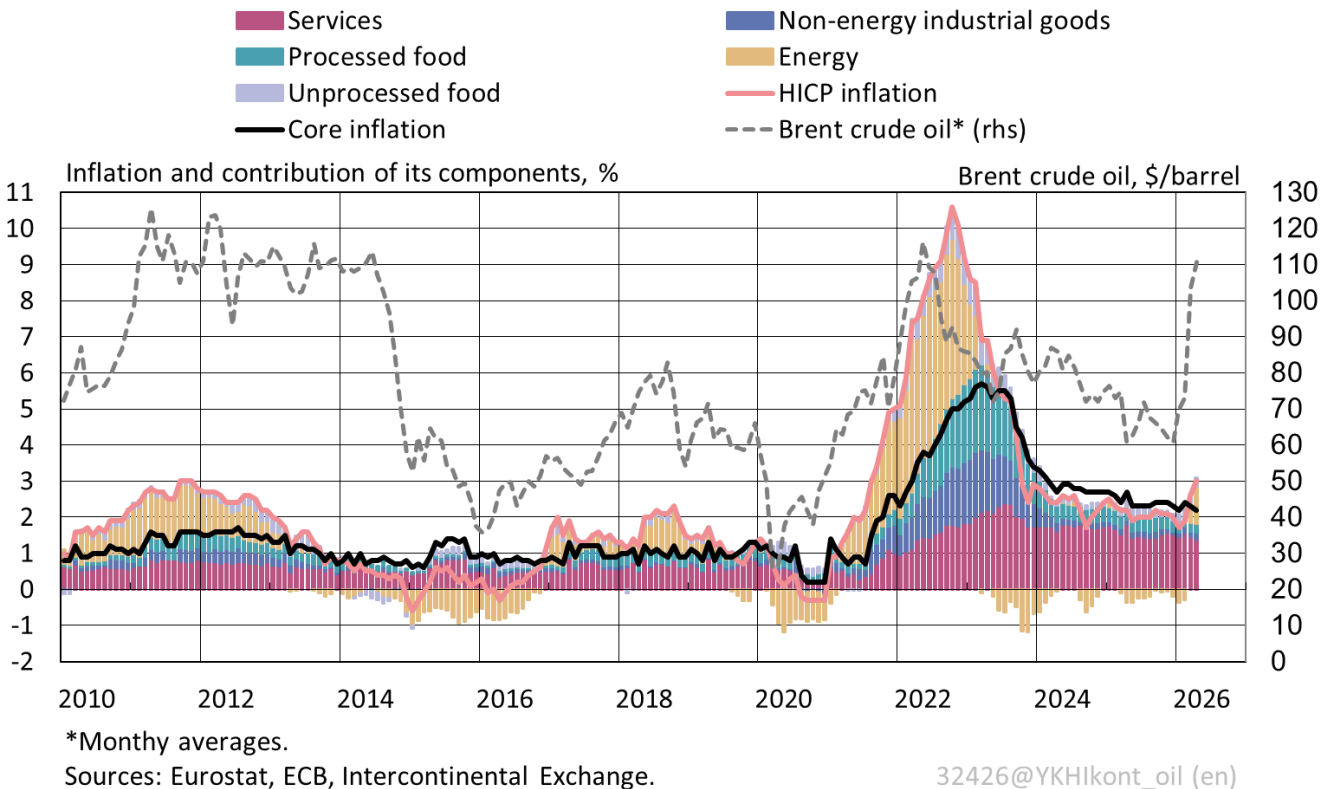
Market-based inflation expectations* in the US

— 1y after 1y — 1y after 3y — 5y after 5y



Source: Bloomberg. *Expectations derived from inflation swap rates.
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Every crisis is unique – no two crises are alike



- Geopolitical shocks are complex: they push up oil and gas prices, but also increase uncertainty, decrease demand and weaken economic growth.
- Whether the oil shock is now feeding longer term inflationary pressure depends partly on the overall economic and labour market situation.
- In line with its 2025 strategy, the ECB is analysing this uncertainty with the help of scenarios. Medium-term horizon.

More than four years of full-scale war have changed Ukraine's economy

- **The scale of the shock is hard to overstate.** Russian forces occupy a fifth of Ukraine's land area, around 15% of the population fled the country before the invasion, and the economy by end-2025 was roughly 20% smaller than in 2021.
- **Despite large-scale destruction of the energy system, the economy has kept growing.** GDP grew around 2% in 2025, and the IMF projects further 2% growth in 2026.
- **The war has reshaped the economy's structure.** Defence-related manufacturing has nearly tripled since 2021, while agriculture dominates exports. Ukraine has gone from a handful of arms manufacturers to a thriving drone industry in the space of three years.
- **What follows are four macroeconomic lessons from this experience** — relevant not just for Ukraine, but for how Europe thinks about economic resilience, defence industrial policy, and the role of international financial support in modern conflict.

Lessons from Ukraine



Gradual deregulation stabilises — not destabilises — a crisis economy



Crises catalyse innovation and speed up how things are done



The economy is the second frontline



Institutional reform under pressure is hard — but failure to deliver is costlier

Europe's strategic triple test

- **Common defence** → Europe must take more responsibility for its own defence and promote joint European investments and procurements.
- **Green transition** → The latest energy crisis again shows that Europe must further strengthen the resilience and competitiveness of its energy sector.
- **Productivity** → Investments in human capital, deepening of capital markets, removing regulatory barriers, promoting innovation.
- Measures taken by the EU and its Member States in these three areas will shape the economic future and strategic autonomy of Europe.
- Monetary policy will operate with a steady hand in an uncertain world.



” *Securing stability,
in science we trust.*

