

The Swedish model

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Summary

By international comparison, Sweden is a prosperous country whose wealth is evenly distributed. The Swedish model is a strategy for inclusive growth. The objective is to increase prosperity to the benefit of all, while safeguarding the autonomy and independence of citizens. The aim of this report is to describe the Swedish model as a strategy for inclusive growth.

The Swedish model can be said to consist of three fundamental pillars: a labour market that facilitates adjustment to change, a universal welfare policy and an economic policy that promotes openness and stability. A labour market that facilitates adjustment to change should comprise an active labour market policy, an effective unemployment insurance scheme and support for adjustment when structural changes make it necessary for workers to adapt to new tasks. The welfare policy is based on universal principles by which all citizens have access to high-quality welfare services. Moreover, the social security system must give the right to financial security to everyone who has fulfilled their obligations. The economic policy is characterised by openness and embraces international competition while promoting economic stability and creating the conditions for a dynamic business sector.

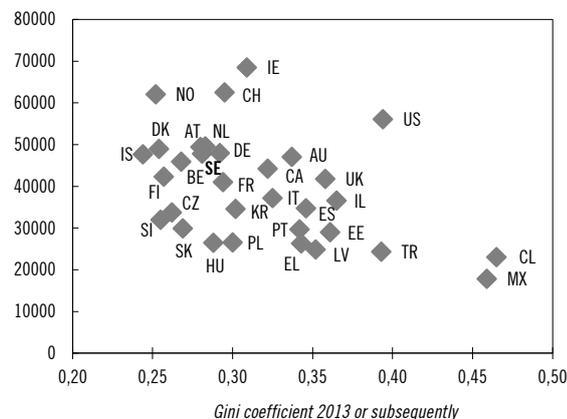
A number of prerequisites must be in place to ensure that the pillars and the interaction among them function effectively and that the objective is achieved. Sound public finances are required to safeguard the long-term sustainability of fiscal policy. The fiscal policy framework is an important tool for achieving this. A high level of trust in the system is another prerequisite. This is essential to ensuring that the system is perceived as legitimate and as something to which people should be willing to contribute by paying taxes. High employment is also essential. Many people must work in order to finance welfare that is available to all. Strong and equal social partners are another key prerequisite. The social partners are responsible for coordinating wage formation and facilitating adjustment to change in the labour market.

1 Introduction

GDP per capita rose by 50 per cent in Sweden during the period of 1995–2016. This growth is higher than in most other OECD countries. There was a temporary downturn in the trend during the financial crisis, but GDP per capita in Sweden has been growing again since mid-2013. After two decades of relatively high growth, Sweden has climbed to tenth place on the list of OECD countries with the highest GDP per capita and has thus overtaken countries including Germany and Canada. Income inequality also increased during the same period, in Sweden and elsewhere, and Sweden is among the OECD countries where the increase has been greatest. As income inequality was low at the base point, Swedish income inequalities are still small by international comparison.

Figure 1.1 GDP per capita and Gini coefficient

Purchasing power parity (PPP) based GDP per capita in 2015, USD



Note: AT=Austria, AU=Australia, BE=Belgium, CA=Canada, CH=Switzerland, CL=Chile, CZ=Czech Republic, DE=Germany, DK=Denmark, EE=Estonia, ES=Spain, FI=Finland, FR=France, UK=United Kingdom, EL=Greece, HU=Hungary, IE=Ireland, IL=Israel, IS=Iceland, IT=Italy, KR=South Korea, LV=Latvia, MX=Mexico, NL=Netherlands, NO=Norway, PL=Poland, PT=Portugal, SE=Sweden, SI=Slovenia, SK=Slovakia, TR=Turkey, US=United States. PPP-based GDP per capita for Luxembourg was USD 102 131 in 2015, a significant outlier from the other countries in the sample. Accordingly, Luxembourg has been omitted from the figure to improve readability. The Gini coefficient can have a value between 0 and 1. A coefficient of 0 expresses maximal economic equality (where everyone has the same income). A coefficient of 1 expresses maximal inequality (only one person has all the income). Source: OECD.

Figure 1.1 Illustrates the level of GDP per capita (as a measurement of prosperity) and the Gini coefficient (a commonly used measurement of income inequality) for a number of OECD countries. The countries that have the highest prosperity (measured in this way) and the lowest income inequality are found in the upper left-

hand corner of the figure. The field is dominated by the Nordic countries, including Sweden, which have over an extended period developed similar strategies for inclusive growth: a Nordic model for the labour market, welfare policy and economic policy.

The aim of this report is to describe the Swedish version of this model as a strategy for inclusive growth. The “Swedish model” is a term often used in public debate. The intention here is not to delve more deeply into the history of the model's development, nor the challenges the model is confronting. Closer analysis of how policies pursued in recent decades have affected the model is also outside the scope of this report.

There is no clear-cut definition of the Swedish model, but as regards the labour market, welfare policy and economic policy, the model can be said to be based on a number of overarching objectives, pillars and prerequisites.¹ Specifically, the model is aimed at mutually reinforcing interaction between equity and prosperity.

The overarching objective of the Swedish model is to ensure that prosperity both increases and is equitably distributed among citizens. Another central principle is that equitable distribution of prosperity must be combined with autonomy and independence for citizens. The overarching objective of combining increased prosperity and equality have informed Swedish economic policy for many years, but the model is continuously adapted in response to new circumstances and challenges.²

¹ This division was inspired by Andersen and Roine's description of the Nordic model (Introduction, Nordic Economic Policy Review No 2, 2015, pp. 8–9):

... the Nordic model should not be defined or assessed in terms of specific policy instruments, what matters is the overarching objectives. Goals — such as equal opportunities in life regardless of family background, the eradication of poverty, gender equality, the lowering of income inequality, etc. — as well as some principles — such as individually based universal rights to things such as health care and education, well-organized labour markets, etc. — have remained largely stable, while the specific policies and instruments to reach them differ across time and countries.

² In a similar way, Vartiainen has said that the underlying objectives must be differentiated from specific policies; policy can change, but the deeper objectives remain the same (To create and share — the remarkable success and contested future of the Nordic Social-Democratic Model, NordMod2030, 2014, p. 11):

The Nordic model is often described as a set of specific policies, such as high taxation, provision of public services, centralized

The fact that income inequality has increased relatively rapidly in Sweden in recent decades, albeit from a low level, can be partially explained by the weakening of certain components of the model. It may therefore be relevant to take a closer look at the mainstays of the model and clarify how they, when the model is working well, constitute a strategy for inclusive growth.

The main objectives of the model are described in greater detail in the next section (section 2). The relationship between efficiency and equity is also discussed (section 3). Thereafter, the three pillars of the model and the prerequisites for the smooth functioning of the model are presented (section 4). The report ends with concluding remarks (section 5).³

2 The main objectives of the model

2.1 Prosperity, equity and gender equality

The objective of the Swedish model is to ensure that prosperity increases and is equitably distributed among citizens. High and rising prosperity is dependent upon a dynamic business sector that contributes to high productivity growth and employment.

The equity goal is based on the fundamental belief in the equal value of all human beings and their equal rights to independent and autonomous lives. Attainment of the equity goal thus has inherent value. Gender equality is a matter of equality between women and men and is a central component of the equity goal. Women's opportunities for gainful employment are critical to their ability to lead independent lives. As well, women's participation in the

wage settlements and extensive social insurance. In my view, a deeper understanding of the model should interpret all such policies as contingent reflections of a deeper political objective: to create value and to share risks. The specific policies adopted have at different times reflected different circumstances and economic and political strategies.

³ When comparisons are made in the text between countries, the point of departure has been to cover the countries that, in addition to Sweden, were included in Sapir's analysis of European social models (Globalisation and the Reform of European Social Models, Background document for the presentation at ECOFIN Informal Meeting in Manchester, 2005): Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain and the United Kingdom. Japan, Canada, South Korea and the United States were also included as comparable non-EU countries. The sample has, however, sometimes been limited depending upon the availability of data.

labour market has substantially increased the labour force in the economy and thus contributed to both higher prosperity and the financing of comprehensive welfare.⁴

Joblessness is the most common cause of economic disadvantage. In general, lack of work also entails exclusion from many social contexts.

The effort to achieve equitable distribution of income thus begins in the labour market, where the education policy and the active labour market policy, along with coordinated wage formation, are intended to create the conditions for high and equally distributed real wages. This requires policy to be designed so that everyone is provided good opportunities for education and work, regardless of social background. In addition, the redistribution policy has impact through taxation and transfer systems that further equalise disposable incomes.

Need-based provision of publicly financed services, such as schools, elderly care and healthcare also contributes to more equitable distribution of total resources.

2.2 Autonomy and independence

One of the goals of the Swedish model is to safeguard citizens' autonomy and independence and prevent power imbalances. This is a matter of relationships between employees and employers, but also between individuals and their families. Through the welfare system and regulation of various power structures, the model aims to create a society in which individuals can maintain a good standard of living and favourable opportunities for development, independently of family and with a strong position in relation to their employers.⁵ Trägårdh and Berggren (2006) drew attention to this aspect of the Swedish model. They describe how the model is based on a direct alliance between the individual and the state as regards both rights and duties. The social safety net is there, regardless of the individual's relationship

to their family, their employer or charitable institutions. Thereby, the model minimises the immediate ties of dependency on family, neighbours, employers and civil society organisations.⁶

3 The relationship between efficiency and equity

That the Nordic countries have successfully delivered such good economic performance in spite of having such large public sectors is sometimes described in economics literature as a paradox.⁷ The reciprocal, reinforcing interaction between efficiency and equity is a key factor in the Swedish model. This stands in contrast to the classically simplified model wherein a high degree of equally distributed incomes by means of public interventions can only be achieved at the price of lower efficiency. Okun (1975) called this “the big tradeoff”, where any insistence on carving the pie into equal slices would shrink the size of the pie (total income).⁸ The argument is that the taxes that will finance the redistributive policy and increase economic equality also reduce the individual's incentives to work, study and invest, for example, because both immediate compensation and the reward after tax are lower. In this case, the individual is assumed to make the decision not to work more without regard to the benefit to the individual and society as a whole of that which is financed by taxes in the form of welfare services and the social safety net. The individual will thus work and invest less than what would be economically efficient.⁹

There are also studies that investigate the instance of “moral hazards” in policy design, particularly as regards the welfare policy. The focus here is on the individual's incentives to

⁴ Berglund and Esser, Modell i förändring landrapport om Sverige (Model in Change. Swedish Country Report) NordMod 2030 Sub-report 8, 2014.

⁵ See also Esping-Andersen, *The Three Worlds of Welfare Capitalism*, 1990.

⁶ Trägårdh and Berggren, *Är svensken människa? Gemenskap och oberoende i det moderna Sverige* [Is the Swede human? Community and independence in modern Sweden] 2006, p. 53.

⁷ See e.g., *The Economist*, Special Report: The Nordic Countries, 2013.

⁸ Okun, *Equality and Efficiency: The Big Tradeoff*, 1975.

⁹ See also Andersen, *The Welfare State and Economic Performance*, SOU 2015:53 Appendix 4 to the Long-Term Inquiry Report, 2015, pp. 45–46; Andersen and Maibom, *The big trade-off between efficiency and equity – Is it there?* 2016.

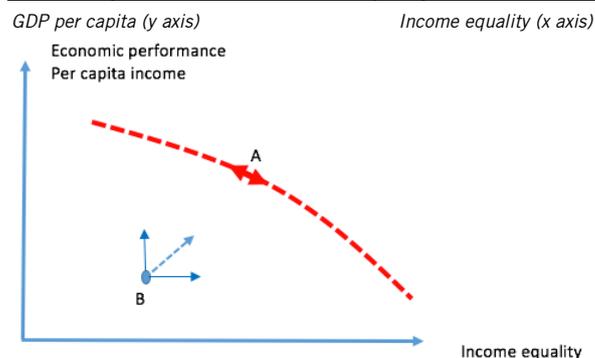
over-use the social security systems, such as sickness insurance.¹⁰ Lindbeck (2008) and Ljunge (2011) argue that the significance of this depends in part on the social norms that surround the social security systems, and that these norms have changed over time. They argue that as the welfare system has been expanded and more people have become beneficiaries, acceptance for being dependent upon the system for one's support has increased. Consequently, they also observe that the risk of over-use of the system has increased.¹¹

According to Andersen (2015), how systems are designed is important in relation to incentive problems and the risk of over-use of unemployment and social insurance, for example. Above all, Andersen emphasises the importance of making rights conditional upon duties. A good balance between rights and duties is thus central to the efficient functioning of the model. For example, the rights of unemployed people to unemployment benefits are conditional upon actively looking for work or participating in training to increase their employability.¹²

There are several empirical studies that examine the correlation between inequality and prosperity. The results diverge. Andersen (2015) and Andersen and Maibom (2016) attempt to explain the divergent results by defining a frontier where countries can theoretically be if institutions are well-designed and resources are used efficiently given the state of technological progress (see point A and the dashed red line in figure 3.1). Many countries, however, are inside, not at, the frontier for historical, institutional and political reasons. For countries inside the frontier, it is possible to increase efficiency and equity concurrently through well-designed reforms and thus move towards the frontier (see

point B and the dashed blue line in figure 3.1).¹³ Thus, for countries inside the frontier, the simple textbook view does not apply; there is an opportunity to increase both economic performance and equality by means of well-designed policies and institutions.

Figure 3.1 Schematic illustration of the trade-off between economic performance and income equality



Source: Andersen and Maibom, The trade-off between efficiency and equity, <http://voxeu.org/article/trade-between-efficiency-and-equity> [accessed 2017-01-10].

The relationship between efficiency and equity is also addressed in the literature on the consequences of globalisation and technological change in advanced economies. Sapir (2005), first categorises Western European countries in four groupings with different social models: the Nordic, the Continental, the Anglo-Saxon and the Mediterranean countries.¹⁴ He thereafter analyses how the various social models are meeting the challenges of globalisation and technological change and the consequences on employment and the risk of poverty. Sapir's underlying thesis is that social models that reduce barriers to structural transformation, encourages adjustment to change and provide sufficient incentive to work generate higher employment than the average. They are therefore considered more efficient. Social models that reduce the risk of poverty are considered more equitable. When the Western European countries are placed on a matrix

¹⁰ See e.g., Lindbeck, Sociala normer och socialförsäkringar – Teori och svenska erfarenheter [Social norms and social insurance - Theory and Swedish lessons learnt], Ekonomisk Debatt, 2008; and Ljunge, The Spirit of the Welfare State? Adaptation in the Demand for Social Insurance, 2011.

¹¹ Lindbeck, Sociala normer och socialförsäkringar – Teori och svenska erfarenheter [Social norms and social insurance - Theory and Swedish lessons learnt], Ekonomisk Debatt, 2008; Ljunge, The Spirit of the Welfare State? Adaptation in the Demand for Social Insurance, 2011.

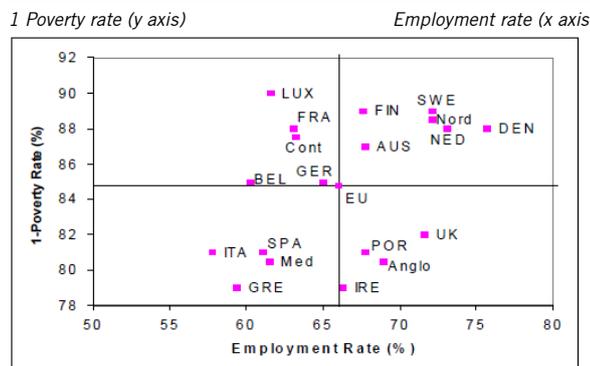
¹² Andersen, The Welfare State and Economic Performance, SOU 2015:53 Appendix 4 to the Long-Term Inquiry Report, 2015, p. 96.

¹³ Andersen, The Welfare State and Economic Performance, SOU 2015:53 Appendix 4 to the Long-Term Inquiry Report, 2015, pp. 45–46; Andersen and Maibom, The trade-off between efficiency and equity, <http://voxeu.org/article/trade-between-efficiency-and-equity> [accessed 2017-01-10].

¹⁴ Sapir, Globalisation and the Reform of European Social Models, Background document for the presentation at ECOFIN Informal Meeting in Manchester, 2005.

according to employment rates and the probability of escaping poverty, a clear pattern related to the social models emerges (see figure 3.2).

Figure 3.2 Employment rates and probability of escaping poverty in 15 EU countries and four country groupings



Note: Social models are designated as: Nord=Nordic, Cont=Continental, Anglo=Anglo-Saxon, Med=Mediterranean. Countries are designated as: SWE=Sweden, FIN=Finland, NED=Netherlands, DEN=Denmark, AUS=Austria, LUX=Luxembourg, FRA=France, GER=Germany, BEL=Belgium, UK=United Kingdom, POR=Portugal, IRE=Ireland, SPA=Spain, ITA=Italy, GRE=Greece. Source: Sapir, Globalisation and the Reform of European Social Models, Background document for the presentation at ECOFIN Informal Meeting in Manchester, 2005.

Based on this pattern, Sapir presents a typology of the social models for the country groupings according to how well they have generated both efficiency and equity (see table 3.1).

Table 3.1 Four European social models

		Efficiency	
		Low	High
Equity	High	Continental	Nordic
	Low	Mediterranean	Anglo-Saxon

Source: Sapir, Globalisation and the Reform of European Social Models, Background document for the presentation at ECOFIN Informal Meeting in Manchester, 2005.

Sapir then focuses on what in the various models might be significant to efficiency and equity, respectively. It proves that the Nordic social model delivers both efficiency and equity. Good opportunities for adjustment to change increase the employment rate and generous social security systems help mitigate the risk of poverty. However, the distribution of human capital proves to be a better explanation of the differences between the countries in this regard. The risk of poverty in the European countries seems to clearly decline in relation to the proportion of the population with at least upper secondary education. Sapir therefore concludes that social models that result in equitable

distribution of human capital also generate more equity in the outcome.

3.1 The relationship between welfare policy and long-term GDP level

Comprehensive public interventions are often needed to achieve more equitable distribution. The question of the correlation between the size of the public sector and the long-term GDP level is thus also closely related to the relationship between efficiency and equity. Again, empirical research has not found any strong and unambiguous correlation. In the discussion, scholars including Lindbeck (1997), Fölster and Henrekson (1999), and Håkansson and Lindbeck (2004) have argued that the public sector has negative impact on the long-term GDP level, while Agell, Lindh and Ohlsson (1999) and Korpi (2004) have contended that such a negative correlation cannot be proven.¹⁵ On the one hand, taxation (in particular) and social transfers generally have distortionary (negative) effects on incentives to work, for example, which impairs economic efficiency and, by extension, the long-term GDP level. On the other hand, the public sector is an important instrument for equalising conditions for individuals and reinforcing total productive capacity in the economy through, for example, providing childcare, education and healthcare.¹⁶ One conclusion that can be drawn from this is that looking only at the incentive effects of taxes and transfers does not result in an accurate description of reality. The size of taxes and spending is not the only thing; how taxation is designed and what the money is spent on also matter.

¹⁵ See Lindbeck, The Swedish Experiment, Journal of Economic Literature, 1997; Fölster and Henrekson, Growth and the Public Sector: A Critique of the Critics, European Journal of Political Economy, 1999; Håkansson and Lindbeck, Korpi vilseleder igen [Korpi misleads again], Ekonomisk Debatt, 2004; Agell, Lindh and Ohlsson, Growth and the public sector: A reply, European Journal of Political Economy, 1999; Korpi, Har den "svenska modellen" minskat vår ekonomiska tillväxt? [Has the "Swedish model" reduced our economic growth?], Ekonomisk Debatt, 2004.

¹⁶ Ekholm et al. Svensk välfärd och globala marknader [Swedish welfare and global markets], Report of the SNS Welfare Policy Council, 2007, pp. 11–12; Andersen, The Welfare State and Economic Performance, SOU 2015:53 Annex 4 to the Long-Term Inquiry Report, 2015, p. 8.

Empirical research has found evidence of a correlation between the type of expenditure and tax and economic performance. Productive expenditures are associated with better economic performance if financed by the least distortionary modes of taxation. Productive expenditures are such that have a direct impact on employment and income; examples may be spending on education and childcare. Table 3.2 shows how various combinations of different types of expenditures (productive or non-productive) and taxes (distortionary or non-distortionary) can be expected to affect GDP.¹⁷

Table 3.2 GDP growth effects of public expenditure and revenues

		Expenditures	
		Productive	Non-productive
Taxation	Distortionary	Ambiguous – possible non-linear effect	Growth retarding
	Non-distortionary	Growth enhancing	Growth neutral

Source: Andersen, The Welfare State and Economic Performance, SOU 2015:53 Appendix 4 to the Long-Term Inquiry Report, 2015.

3.2 Welfare “from the cradle to the grave”

Another central aspect of the Swedish model is that the publicly provided welfare services and the social security systems cover an individual's entire life course, i.e., from “the cradle to the grave”. Children and youth are the beneficiaries of childcare and education, older people of long-term care services and pensions, while the working-age population are contributors through income taxes. All age groups are beneficiaries of healthcare and transfers, but to various extents. The social contract across generations can be said to consist of a savings element and a borrowing element. In theory, this

shifting of resources across the life cycle could take place in a complete capital market, but the conditions for such markets are not found in practice. This function compensates for a market failure and thus increases economic efficiency.

Public investments in the forward part of the contract (borrowing), that is, early in life through investments in education, for instance, can generate relatively larger efficiency gains than investments in the backward part of the contract. This contract also makes it possible for talented young people to educate themselves, even if their families are financially disadvantaged. This contributes to better exploitation of human capital potential in the population and, by extension, to higher income and growth in the economy as a whole.¹⁸ Nevertheless, the backward element of the contract, including the right to elderly care services for instance, is an important part of the contract.

Obviously, economies with stronger social contracts across generations have relatively larger public sectors, but because the public sector partially overcomes market failures and results in higher investments in welfare in general and education in particular, it also generates higher prosperity (output).¹⁹

3.3 How is Sweden faring?

The empirical analyses carried out by Andersen (2015) and Andersen and Maibom (2016) show that Sweden is among the “best practice countries” that, with well-designed policies and well-designed institutions, are near the frontier and stand out by having achieved both high income and high equity.²⁰ There are countries, however, that have both higher GDP per capita and higher equity than Sweden. This indicates

¹⁷ Andersen, The Welfare State and Economic Performance, SOU 2015:53 Appendix 4 to the Long-Term Inquiry Report, 2015, pp. 8–10, 56–57; Ekholm et. al. Svensk välfärd och globala marknader [Swedish welfare and global markets], Report of the SNS Welfare Policy Council, 2007, pp. 17, 39–40. Non-productive expenditures, however, may be motivated on other grounds than economic performance (Andersen 2015, p. 17).

¹⁸ Andersen, The Welfare State and Economic Performance, SOU 2015:53 Appendix 4 to the Long-Term Inquiry Report, 2015, pp. 16–17, 49–55.

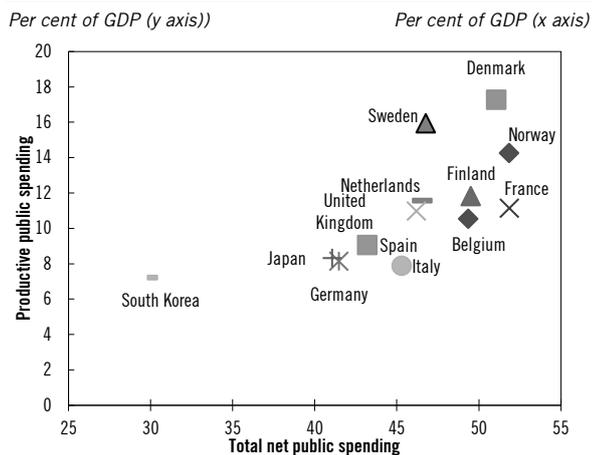
¹⁹ Andersen, The Welfare State and Economic Performance, SOU 2015:53 Appendix 4 to the Long-Term Inquiry Report, 2015, p. 52.

²⁰ Andersen, The Welfare State and Economic Performance, SOU 2015:53 Appendix 4 to the Long-Term Inquiry Report, 2015; Andersen and Maibom, The big trade-off between efficiency and equity – Is it there? 2016.

that it should also be possible to increase both GDP per capita and equity in Sweden by means of well-designed measures. There is also nothing to indicate that the frontier illustrated in figure 3.1 is constant over time. The frontier indicates where “best practice” is at present, but it is possible that research and policy development can lead to improvements to institutions and systems so that “best practice” is shifted outwards so that both higher GDP per capita and higher equity are made possible.

According to Andersen (2015), an important explanation for why Sweden and other Nordic countries have successfully combined efficiency and equity is that a high proportion of their relatively high public expenditure is productive (see figure 3.3); e.g., that a high proportion of public spending has direct impact on employment and income because they increase human productivity and employment.²¹

Figure 3.3 Total and productive (active) public spending



A Note: Productive (active) spending include education, health expenditure for persons below the age of 60, child and old age care and active labour market policies, 2011.
 Source: Andersen, The Welfare State and Economic Performance, SOU 2015:53 Appendix 4 to the Long-Term Inquiry Report, 2015, reproduced in Govt Bill 2015/16:1, Proposed Central Government Budget, Fiscal Plan, etc., section 1.6.

Sapir’s (2005) analysis also shows that the social model that characterises Sweden and other Nordic countries has successfully combined high efficiency and high equity (see table 3.1). In the analysis, Sapir points to arrangements in the Swedish labour market,, which facilitate

adjustment to change, and the relatively even distribution of human capital as critical factors.²²

The components of the Swedish model that have together contributed to successfully combining high equity and high GDP per capita are described in greater detail in section 4.

4 The model’s pillars and prerequisites

The Swedish model is based on three fundamental pillars: a labour market that facilitates adjustment to change (pillar 1), universal welfare policy (pillar 2) and economic policy that promotes openness and stability (pillar 3).

A labour market that facilitates adjustment to change (pillar 1) is based on coordinated wage formation, an active labour market policy and effective unemployment insurance.

Welfare policy (pillar 2) is based on universal principles by which all citizens have access to high-quality welfare services.

Economic policy (pillar 3) is characterised by openness and acceptance of international competition. The economic policy must also ensure economic stability.

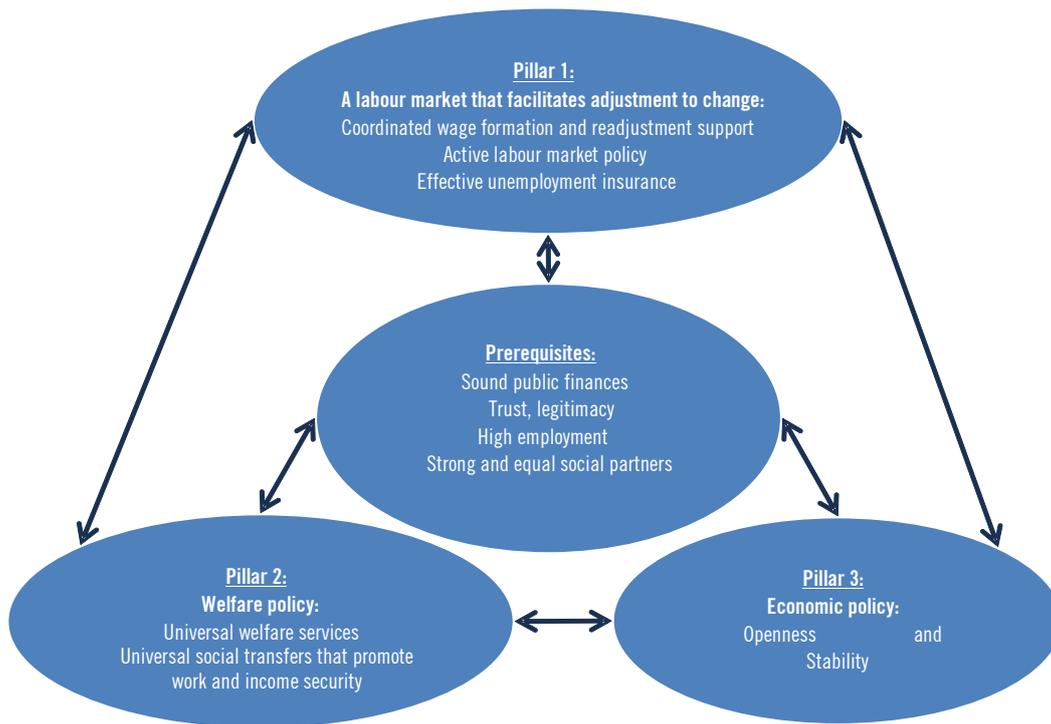
Certain prerequisites need to be in place for the three pillars and the interaction among them to work and the objective is achieved. These prerequisites are sound public finances; a high level of social trust and trust in the system, which is perceived as legitimate; high employment; and strong, equal and legitimate social partners. These three factors are fundamental prerequisites for the effective function of the models three pillars and are reinforced when the overall objectives are achieved.

Figure 4.1 provides a schematic illustration of the pillars and prerequisites of the model and how they interrelate. The components of the model and how they interact are described in greater detail below.

²¹ Andersen, The Welfare State and Economic Performance, SOU 2015:53 Appendix 4 to the Long-Term Inquiry Report, 2015.

²² Sapir, Globalisation and the Reform of European Social Models, Background document for the presentation at ECOFIN Informal Meeting in Manchester, 2005.

Figure 4.1 The pillars and prerequisites of the Swedish model and how Sweden, as a small economy, should achieve the objectives of higher prosperity and equity while safeguarding the autonomy and independence of citizens



Source: Own illustration based on Dølvik et al., *The Nordic model towards 2030. A new chapter? Nordmod2030*, 2014.

4.1 Prerequisites for the Swedish model

4.1.2 Trust and legitimacy

4.1.1 Sound public finances

Sound public finances are a fundamental prerequisite for the Swedish model to work. This is essential to ensuring that fiscal policy is sustainable over the long term and that there is fiscal space to pursue stabilisation policy (see also section 4.4.2). The fiscal policy framework, with surplus targets, expenditure ceilings, a municipal balanced budget requirement and rigorous budget process are important tools for achieving this aim. Other aspects of a sustainable fiscal policy include that it contributes to equitable distribution of resources over time.²³

Research shows that trust is the most fundamental factor in the successful establishment and upholding of common regulations that benefit most people.²⁴ The financing of the common welfare and the use of public resources must be perceived as fair and effective. If citizens do not trust that the resources they give up when they pay taxes or charges are used appropriately, there may be serious resistance to contributing to the common good.²⁵

²³ See also SOU 2016:67, section 3.

²⁴ Elinor Ostrom has emphasised this in her research (see e.g., *Governing the Commons: The Evolution of Institutions for Collective Action*, 1990).

²⁵ Bo Rothstein has unpacked this (see e.g., *Just institutions matter: the moral and political logic of the universal welfare state*, 1998); Wennemo, *Det gemensamma – om den svenska välfärdsmodellen*, [What we have in common: On the Swedish welfare model], 2014, pp. 76, 128, 141, 275.

Sweden and the other Nordic countries are distinguished by a high level of social trust.²⁶ Research has shown that this is a key explanation of why Sweden has managed to combine a universal welfare state, equitable income distribution and good economic performance.

Another important explanation for the widespread public trust in the welfare systems and for why they are perceived as legitimate is that that have been mainly universal and covered everyone, rather than being needs-based (selective) and covering only those with the greatest need. It is easier to build a universal welfare policy on simple and clear-cut rules. This creates legitimacy and reduces distrust in politics and the system. The universal policy also means that commonly shared welfare benefits everyone. Experience has shown that citizens are more willing to accept financial responsibility for various initiatives when they understand how the initiatives will benefit them. An efficient tax system with low risk of tax evasion and tax avoidance is another key factor.

The orientation of the model towards a high employment rate also helps reinforce trust in the system and its legitimacy.

Effective control and supervision of various systems, so that they are used as intended and not abused, is another important aspect of safeguarding trust and legitimacy. It is also important that the government agencies that administer the systems are audited and that risks of corruption, e.g., in connection with public procurements, are minimised.

4.1.3 High employment

High employment is a prerequisite for the three pillars of the model and has direct impact on the capacity to achieve its objectives. High employment for both men and women is essential to high and equitably distributed prosperity and to protect the autonomy and independence of citizens against unequal relationships of power.

Financing universal welfare is expensive. For this reason, the model requires as many people as possible to be able and allowed to work and as few people as possible who are dependent upon social transfers.²⁷ The duty of every individual to work according to their ability is a central component of the social contract among citizens for which the state is responsible, and which also gives every individual the right to welfare services. Accordingly, the model is strongly oriented towards creating high employment and sustainable working life for men and women.

High employment is a prerequisite for the effectiveness of the other components of the model, such as a labour market that facilitates adjustment to change and the welfare policy, as well as achievement of the objective of increased and equally distributed prosperity. At the same time, these two pillars contribute to achieving the goal of high employment, which is an example of the mutually reinforcing interaction that must exist between the different parts of the model.

Many policy areas have both welfare and employment policy aims. Large parts of the welfare policy, including an expansive childcare system and an effective education system, foster increased labour force participation and high employment, as well as high long-term productivity growth. Combined with equal distribution of human capital and coordinated wage formation, high employment also reduces the need for redistribution. Higher employment not only increases the tax base, spending on various social insurance systems is reduced when fewer people need benefits from the insurance system for their support.²⁸

By international comparison, Sweden is distinguished by high labour force participation and a high employment rate. The employment rate is the highest in the EU and, particularly high among women (see figure 4.2).

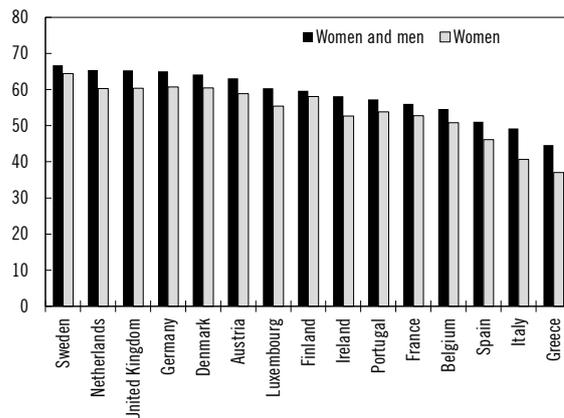
²⁶ Wennemo, *Det gemensamma – om den svenska välfärdsmodellen* [What we have in common: On the Swedish welfare model], 2014, pp. 272–273.

²⁷ Esping-Andersen, *The Three Worlds of Welfare Capitalism*, 1990, pp. 27–28.

²⁸ Berglund and Esser, *Modell i förändring – landrapport om Sverige, NordMod 2030 (Model in Change. Swedish Country Report)*, 2014 p. 17.

Figure 4.2 Employment rate, total and for women aged 15–74, 2015

Per cent of population



Source: Eurostat.

4.1.4 Strong and equal social partners

Another important prerequisite for effective interaction between the fundamental pillars is that the social partners, as key actors in the model, are strong, equal and perceived as legitimate. Conditions in the labour market, including wages, are regulated to a great extent by collective agreements negotiated and made directly between the social partners. This arrangement reduces the need for labour laws. It is essential that the social partners are strong and equal to ensure effective wage formation (see also section 4.2.1 on the role of the social partners in wage formation).²⁹

In the literature, Calmfors and Driffill (1988) have suggested in a theoretical model that both centralised and decentralised wage setting can contribute to real wage growth that is aligned with productivity growth and high employment. The condition is that wage setting is either highly centralised or highly decentralised. The Nordic countries and the United States are presented as concrete, empirical examples of how a high degree of centralisation or decentralisation can manage this.³⁰ Calmfors (1993) also argues that there is a long tradition of success with both of these models as regards

employment and productivity growth.³¹ There is later literature, however, such as Fitzenberger and Franz (2003), that instead suggests that industry-level wage bargaining can lead to higher employment than decentralised wage setting. Developments in the United States over recent decades, where real wage growth has been lower than productivity growth, also show that the conclusions in Calmfors and Driffill's theoretical model are not entirely unambiguous, but are rather dependent upon certain prerequisites. The changes that have occurred in the Swedish wage bargaining scheme since the mid 1990s have also been discussed in the literature. Proceeding from Calmfors and Driffill's original idea, Vartiainen (2010) analyses the consequences of a scheme in which the outcome of negotiations in the manufacturing sector sets a norm for collectively agreed pay increases for the rest of the economy. The conclusion is that wage norm observance can improve both productivity and the employment rate compared to the non-observance of the wage norm, provided that the wage norm binds.³²

Strong unions also foster more equal relationships between workers and employers and thus to making workers more autonomous and independent in relation to the employer. As well, the social partners often play a central role in the implementation of major reforms. In such cases, the required negotiations among political decision-makers, employers and unions help generate acceptance for the changes made, provided that the partners are perceived as legitimate.³³ In this way, strong social partners also reinforce social trust.

Sweden and the other Nordic countries have the highest union membership rates in the world.³⁴ The union membership rate has, however, declined sharply since 2007, partly due to the cutbacks in unemployment insurance

²⁹ Dølvik et al., *The Nordic model towards 2030. A new chapter?* NordMod 2030, 2014, pp. 21–22.

³⁰ Calmfors and Driffill, *Centralization and wage bargaining*, Economic Policy, 1988.

³¹ Calmfors, *Centralisation of wage bargaining and macroeconomic performance – a survey*, OECD Economic Studies, 1993.

³² Vartiainen, *Interpreting Wage Bargaining Norms*, Working Paper no 116, Swedish National Institute of Economic Research (NIER), 2010.

³³ Wennemo, *Det gemensamma – om den svenska välfärdsmodellen [What we have in common: On the Swedish welfare model]*, 2014, pp. 268–269.

³⁴ Wennemo, *Det gemensamma – om den svenska välfärdsmodellen [What we have in common: On the Swedish welfare model]*, 2014, p. 259.

implemented that year. Another result of the changes was that fewer people were covered by an unemployment insurance scheme.

Strong and equal social partners that negotiate wages and working conditions foster sound order in the labour market, competitive businesses and good real wage development for wide groups of people. This also provides opportunities for the Government to work with the social partners to devise constructive solutions to problems in the labour market.

That the social partners have such a prominent role in the labour market also means that they have a responsibility to create stable conditions and facilitate labour market entry for more people.³⁵ Critics, however, have argued that the model of negotiations among the social partners has contributed to high thresholds to labour market entry that have resulted in a high proportion of short-term contracts, particularly among groups that have recently entered the labour market.³⁶

4.2 Pillar 1 – A labour market that facilitates adjustment

The distinguishing characteristics of the Swedish labour market are coordinated wage formation, an active labour market policy and effective unemployment insurance. The fundamental premise is that individuals should contribute through work and be willing to adjust to new tasks. Provided that individuals perform this part of the social contract, they qualify for rights in the form of income-related social security, and, after needs assessment by the Public Employment Service, active initiatives to facilitate the return to work after having become unemployed. In addition, there is a certain level of financial security for people who do not qualify for income-related social security benefits. The social partners also provide a large portion of support in connection with unemployment through various career readjustment agreements.

4.2.1 Coordinated wage formation

Conditions in the labour market are regulated to a high degree through collective agreements negotiated and made directly between the social partners, rather than through law and state intervention. This is a key component of the Swedish model. For example, there are no statutory minimum wages, as there are in many other countries. The collective agreements cover a large proportion of workers. Collective agreements also enjoy special legal status, as legislative provisions in the labour market area are often not peremptory, but can be substituted or augmented with agreements between the social partners in collective agreements. This model has a long history, in which the Saltsjöbad Agreement of 1938 was an important milestone.³⁷

Contributing to good conditions for workers is not the only aim of coordinated collective agreements that cover a high proportion of workers and employers. They also limit firms' opportunities to compete in product markets by means of poorer wages and other terms of employment. Firms that fail to sufficiently increase their productivity are eliminated, while profitability and expansion are promoted in firms that are innovative and invest in new technology. By this means, coordinated wage formation can encourage faster productivity growth and stronger competitiveness in the overall economy. It also entails a continuous need for adjustment when workers in low-productivity firms are made redundant and need to be redirected to new jobs with more productive firms.

Uniquely to the Nordic countries, unions have in general constructively contributed to structural transformation, rather than opposing it, largely owing to the opportunities for good

³⁵ See also NIER, Wage Formation Report, 2016, p. 7.

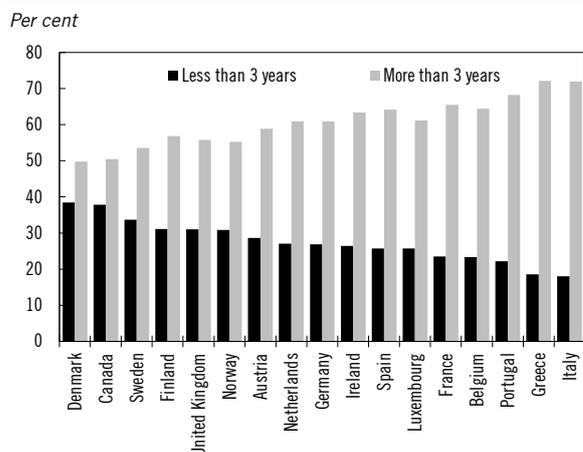
³⁶ See e.g., OECD, Economic Survey Sweden March 2015, p. 36.

³⁷ Karlson and Lindberg, En ny svensk modell – vägval på arbetsmarknaden: sönderfall, omreglering, avreglering eller modernisering [A new Swedish model – choice of path in the labour market: breakdown, re-regulation, de-regulation or modernisation], 2008, pp. 18, 19, 26. The definition of a collective agreement is an agreement between an employer or employers' organisation on terms of employment such as pay, working hours and annual leave or other conditions between employers and workers, such as labour conflict measures, bargaining procedures and no-strike rules..

income security and active career readjustment support provided.³⁸

That the social partners have such a prominent role fosters flexibility in the labour market and less need for preemptory laws. This flexibility is essential to effective adjustment, where it is important that necessary modifications of terms and contractual provisions can be made, depending on the industry affected. The job tenure interval is an indicator of flexibility and mobility in the labour market. A short interval indicates high mobility in the labour market. Figure 4.3 shows that Sweden is among the countries where a relatively high proportion of the total workforce has been in their current jobs for a relatively short time.

Figure 4.3 Percentage of workforce in current jobs for less than three years or more than five years



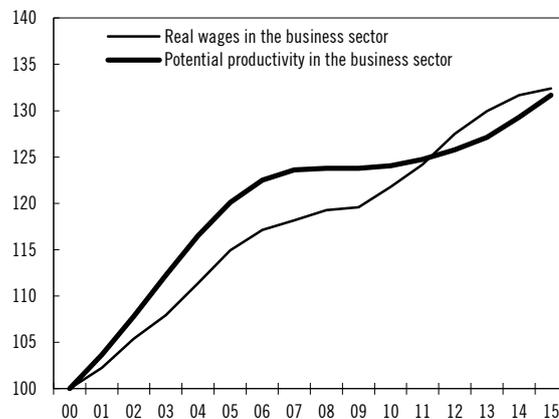
Note. Data is unavailable for Japan, the United States and South Korea. Source: OECD.

The social partners' responsibility for wage formation is a central component of the Swedish model. The state has overarching responsibility for the national economy, while the social partners have main responsibility for wage formation. In parallel, the system has been augmented with the option for central mediation through a third party, which reduces the risk of conflict and subsequent industrial action if the partners are unable to achieve compromise. The current wage formation model has contributed to persistent real wage growth that has been in line with productivity growth (see figure 4.4).

Nominal wages have also increased at a balanced pace. The model has also encouraged small wage differences (see figure 4.5).

Figure 4.4 Real wages and potential productivity in the business sector

Constant prices, index, 2000=100

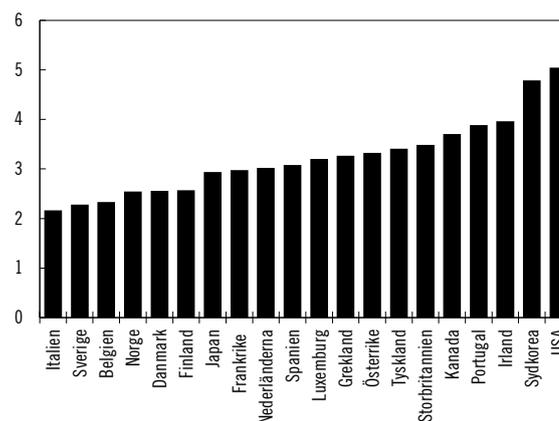


Note. Both productivity and real wages are deflated by the value added price, which makes them comparable.

Source: Statistics Sweden and own calculations.

Figure 4.5 Wage distribution 2012 or subsequently

Quotient between decile 9 and decile 1 in the wage distribution



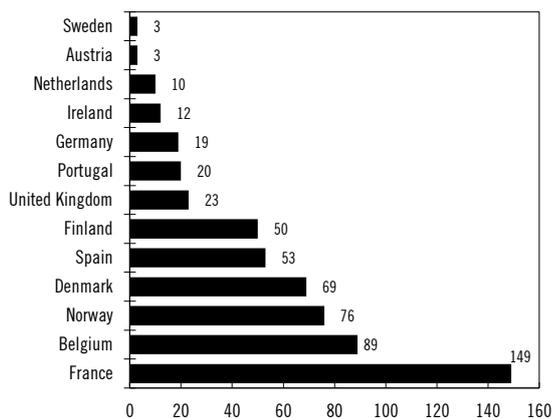
Source: OECD.

The likelihood of industrial action in the Swedish labour market, measured as the number of days not worked due to industrial action, has also been low compared to other countries (see figure 4.6).

³⁸ Wennemo, Det gemensamma – om den svenska välfärdsmodellen [What we have in common: On the Swedish welfare model], 2014, pp. 233–234.

Figure 4.6 Number of days not worked due to industrial action 2009–2015

Average days not worked per 1,000 employees



Note: Insufficient data for Greece, Italy and Luxembourg. Data only for European countries.

Source: European Trade Union Institute.

4.2.2 Active labour market policy

Another distinguishing characteristic of the labour market in the Swedish model is an active labour market policy which, combined with the career readjustment agreements between the social partners, supports mobility in the labour market and facilitates the return to work after a period of unemployment. The active labour market policy is also aimed at facilitating labour market entry for disadvantaged groups. It mainly consists of three types of initiatives:

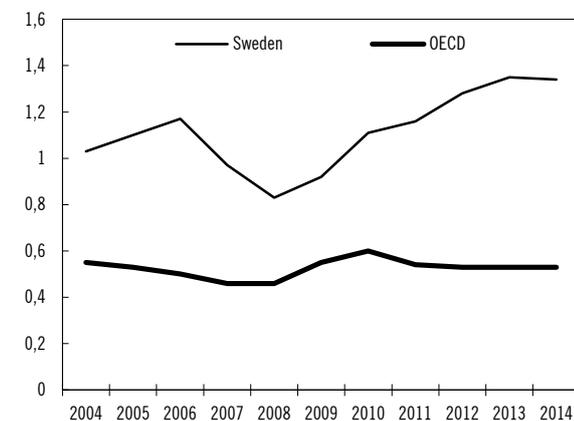
1. Labour market-related further training to improve unemployed people's human capital (preparatory initiatives, various forms of vocational training, work experience placements and labour market introductions);
2. Subsidised employment (employment support in the form of subsidies to employers to hire an unemployed person or a person with a disability) and;
3. Employment services (matching unemployed people to available jobs through arranging contacts and coaching).³⁹

³⁹ See also Forslund and Vikström, *Arbetsmarknadspolitikens effekter på sysselsättning och arbetslöshet – en översikt* [Labour market policy effects on employment and unemployment], Report 2011:7, IFAU, 2011, p. 7; Berglund and Esser, *Model in Change. Swedish Country Report*, NordMod 2030, 2014 p. 75.

Relatively speaking, Sweden has invested more in active labour market policy than the OECD average, measured by public expenditure on active labour market programmes as a percentage of GDP (see figure 4.7).

Figure 4.7 Public expenditure on active labour market programmes in Sweden and the OECD 2004–2014

Per cent av BNP



Source: OECD.

The purpose of the active labour market policy, combined with the career readjustment agreements, is to enable rapid structural transformation while maintaining high employment among both women and men. In order to maintain high employment, labour market measures should also strengthen the position of weak groups in the labour market and improve matching between labour supply and demand.⁴⁰ This is achieved mainly by equipping unemployed people, in various ways, with the skills that are in demand. Society is responsible for creating the conditions necessary for all men and women to be able to work. Individuals are responsible for making themselves available to the labour market and acquiring the skills that are in demand.

4.2.3 Effective unemployment insurance

Along with career readjustment insurance policies, unemployment insurance serves a key function for facilitating adjustment and creating acceptance of the need for continuous structural

⁴⁰ Fransson and Sundén, *Vad är arbetslinjen? [What is the work incentive strategy?]* Samtal om socialförsäkring, Nr 4, Socialförsäkringsutredningen, 2005, p. 42.

transformation in the economy. It also serves an important welfare policy function.⁴¹ In this regard, the employment policy and the welfare policy are clearly intertwined.

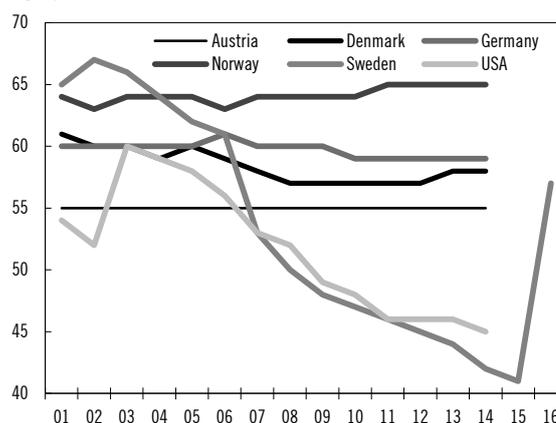
An effective unemployment insurance scheme provides income security and thus reinforces citizens' independence and capacity to adjust. Generous insurance benefits during temporary periods of unemployment can contribute to better matching by giving people the latitude to apply for jobs for which they have the right qualifications. Income-related unemployment insurance also works as an automatic stabiliser in recessionary periods.⁴²

An effective unemployment insurance scheme is also readjustment insurance that, combined with active initiatives, makes it possible for people to acquire new skills and adjust to a new job. At the same time, it is important that the insurance scheme provides clear incentives to work.⁴³ Consequently, the unemployment insurance scheme has been designed so that incentives to work are maintained even when the compensation provided is comparatively high. This is accomplished through making the right to benefits conditional upon active job search or participation in training to increase employability.

In an international comparison with Austria, Denmark, Germany, Norway and the United States, the NIER found that the income protection level of Swedish unemployment insurance in 2007 had fallen to lower levels than in the other European countries studied. Unemployment insurance benefits were increased in the autumn of 2015, which brought the net compensation rate in Sweden in line with the other European countries studied and above that in the United States (see figure 4.8).⁴⁴

Figure 4.8 Net compensation rate of unemployment insurance at the median wage

Single persons with no children



Note: The net compensation rate is stated as the quotient between unemployment insurance benefits after tax and wages after tax. The compensation levels reported apply to the initial period of unemployment (weeks 1–20 in most cases). The United States is represented by the state of Michigan. Sources: NIER, Wage Formation Report 2016 and OECD.

4.3 Pillar 2 – Welfare policy

The scope and orientation of Swedish welfare policy is largely determined by the overarching objectives of the Swedish model of high and equitably distributed prosperity and individual independence of unequal power relationships. The social rights make individuals less economically dependent upon family, employers and charities.⁴⁵ This applies to welfare services, such as childcare, schools and healthcare, as well as the social transfer systems, such as sickness insurance, parental leave insurance and unemployment insurance. They also promote gender equality by giving women and men equal opportunities for education and paid work that provides economic independence.

In addition to generally contributing to the prosperity of Swedish citizens, welfare services and the social transfer systems are designed with a view to promoting high labour force participation, high employment, strong productivity growth and competitiveness. In other words, the welfare services in particular are productive to a high extent (see also sections 3.1 and 3.3 and figure 3.3). Large parts of the welfare

⁴¹ SOU 2015:51, p. 237.

⁴² SOU 2015:21, pp. 235–237, 789.

⁴³ SOU 2015:21, pp. 235–237.

⁴⁴ NIER, Wage Formation Report, 2016, pp. 101–106.

⁴⁵ Trägårdh och Berggren, *Är svensken människa? Gemenskap och oberoende i det moderna Sverige*, 2006, s. 32, 53.

system are also designed to promote equality of both opportunities and outcomes. Expenditures for education and childcare are examples of this. Investments in education, for example, have helped make it possible for young people from less financially secure families to get an education, which has led to better exploitation of total human capital, higher income, increased equity and economic growth overall.

Swedish welfare policy is distinguished by a high degree of universality, i.e., public services and transfers are designed as social rights that cover the entire population in various life situations and not only economically disadvantaged groups. This is very different from a selective welfare policy under which public support is provided only after needs assessment to individuals who are unable to meet their basic needs through income earned in the market.⁴⁶ While need-tested services also exist in the Swedish welfare system, these are intended only to work as the last social safety net when rights-based social security systems are insufficient. As mentioned in section 4.1.1, a universal welfare policy has been shown to foster higher trust in the welfare systems. It is easier to build a universal welfare policy on simple and clear-cut rules without costly needs-testing. These characteristics enhance the efficiency of the system.

4.3.1 Welfare services

High-quality universal welfare services to promote equitable prosperity and individual autonomy...

Universally designed, high-quality welfare services in the form of healthcare, education, long-term care services for the elderly and childcare, etc., contribute to more equitable distribution of prosperity. Publicly financed healthcare and long-term care work like an

insurance policy that gives people equal access to health and social care when the need arises. Equitable distribution of knowledge in society is, by extension, important for equitable distribution of earned income. In order to achieve a high and equitably distributed level of knowledge in society, it is important that knowledge outcomes for school pupils are generally good and that there is a narrow spread in pupil performance.⁴⁷ Allowing all pupils the opportunity to develop in school based on their unique circumstances fosters personal growth and autonomy as well as the capacity to become established in the labour market and participate actively in society. Equal educational opportunities also depend upon giving everyone the opportunity to support themselves while they are studying. Financial aid for studies helps make this possible. In addition to equalising the financial circumstances of students and others, financial aid contributes to greater social justice by creating more equitable financial opportunities to pursue education.

...and higher employment and prosperity

Universal, high-quality welfare services do not only contribute to more equitable distribution of prosperity. They also contribute to higher GDP by enabling high labour force participation and more hours worked in the economy. This applies above all to childcare (and parental leave insurance, see section 4.3.2), but also elderly care services and services for people with disabilities. The system has created the conditions necessary for a very high employment rate among women and for Sweden to have the highest employment rate in the EU (see section 4.1.3).⁴⁸

Over the long term, economic productivity is crucial to material prosperity. In turn, total human capital is essential to productivity growth. By international comparison, Sweden is a highly qualified knowledge-based economy

⁴⁶ Rothstein, *What should the state do? On the moral and political logic of the welfare state* 3rd edition, 2010, pp. 30-32; Korpi and Palme, *The Paradox of Redistribution and Strategies of Equality: Welfare State Institutions, Inequality, and Poverty in the Western Countries*, *American Sociological Review*, 1998; Esping-Andersen, *The Three Worlds of Welfare Capitalism*, 1990.

⁴⁷ SOU 2015:104, s. 9.

⁴⁸ See also the report from the Expert Group on Public Economics (ESO) 2015:5, pp. 21–22, 35 on how Swedish childcare system (and parental leave insurance) stand out by so clearly supporting the opportunities of parents to work, and how such a family policy has proven significant to increasing the employment rate among women and increasing the participation of men in caring for the home and family.

with relatively high and equal distribution of knowledge. A high-quality education system that is accessible to all is necessary for Sweden to be an outstanding nation of knowledge and research. It is significant that the education system communicates with the business sector so that future workers can be educated in fields where Sweden can compete internationally, as well as to promote adjustment in the labour market.

4.3.2 Social security systems

The social security systems in the form of social insurance schemes and transfers is aimed at creating more equitable distribution of prosperity. In many cases, they are also designed to strengthen incentives to work. The latter applies to the social insurance schemes in particular.

The social insurance schemes are aimed at providing income security to the insured when they cannot work due to illness, parenthood, etc., and upon retirement.⁴⁹ The protection in the insurance schemes has thus been related to income so that more work and higher income result in better income protection.⁵⁰ By this means, the incentives to work are strengthened. That the insurance schemes are managed in such a way that the systems are not over-used (see section 3) is also a linchpin of the model. Another distinguishing characteristic of Swedish social insurance schemes is that they are universal and, to a great extent, obligatory. Korpi and Palme (1998) find support for the idea that social insurance schemes that cover high earners and not only the most disadvantaged are more successful at increasing equity. The advantage to making social insurance schemes obligatory to such a high extent is that the risks are then spread over a large number of individuals whose risks of income loss vary. As a result, people at higher risk of losing their earned income also gain access to insurance at a reasonable cost, which would not otherwise have been possible

(and people at low risk are covered by insurance that they would otherwise probably not have purchased, but which they will have a right to if they become unemployed). In this way, the insurance becomes redistributive and fosters more equitable distribution of social security.⁵¹

Parental leave insurance is the part of the social security that makes an especially clear contribution to the high employment rate in the population and increased equity. Along with childcare and the child allowance, it constitutes a central component of the economic family policy, whose goals include reducing economic disparities between households. It has been designed for aims including promoting high labour force participation and more hours worked in the economy. Combined with an expansive childcare system (see section 4.3.1), it has made it possible for parents to combine active parenthood with employment. Thereby, it has also contributed to greater financial equality between women and men. In 2015, Sweden had the third-lowest gender employment gap in the EU (see figure 4.9). The size of the parental allowance is also related to the parent's earned income, which provides an incentive to become established in the labour market before one becomes a parent. It has, however, been shown that wage development suffers during the parental leave period. This applies to both men and women, but since women have used more parental allowance days than men, women's wage development has suffered more than men's. Women do not subsequently catch up with men in terms of pay; the pay gap between them instead increases over time after having taken parental leave.⁵²

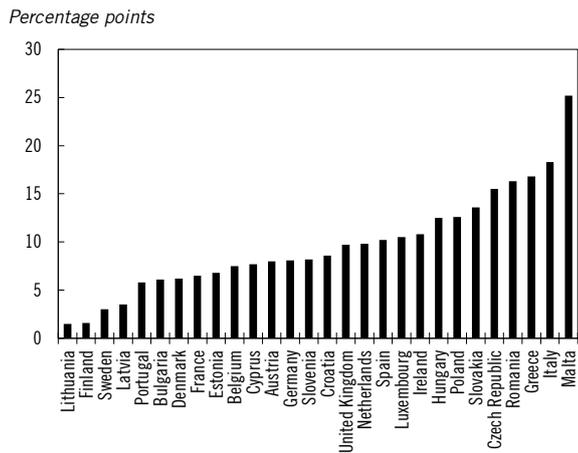
⁴⁹ And in connection with unemployment; unemployment insurance is addressed separately in section 4.2.3

⁵⁰ SOU 2015:21, pp. 235–236, 249–250; Rothstein, *Vad bör staten göra? Om välfärdsstatens moraliska och politiska logik*, third edition, 2010, p. 30.

⁵¹ SOU 2015:21, pp. 249–250; Berglund and Esser, *Model in Change*. Swedish Country Report, NordMod2030, 2014 p. 17.

⁵² SOU 2015:50, pp. 170–171.

Figure 4.9 Employment rate and gender employment gap in the EU, 2015



Note. The statistics refer to the 15–64 age group.
Source: Eurostat.

jobs. Together, this has created high transformation pressure, where less productive firms have been outcompeted while the more productive have been able to grow.⁵³

By international comparison, Sweden is relatively open to international competition, measured for example by the ease of starting and operating a local firm. Based on this measurement, Sweden is ranked as the ninth most open country in the world (out of a total of 190) (see table 4.1). Sweden is also ranked highly in international reviews of innovation and revitalisation (see table 4.1).

4.4 Pillar 3 – Economic policy

In relation to the Swedish model, the economic policy is, on the overarching level, oriented towards stabilising the economy and promoting openness and competitiveness. High and consistent demand pressure combined with responsible fiscal policy facilitates the structural transformation necessary to respond to international competition in a small, open economy and sustain a high employment rate.

4.4.1 Openness and competitiveness

In a small, open economy like Sweden's, the capacity of the business sector to continuously evolve and perform well in international competition is critical to economic growth and employment. Swedish prosperity is based to a great extent on the ability of Swedish companies to compete internationally.

Globalisation and its consequential demands for specialisation and continuous technical development entail great opportunities for higher prosperity, but also challenges and risks for firms and, especially, individuals. The overarching economic policy has been designed for a long time with a view to encouraging a dynamic business sector that delivers strong productivity growth and performs well in international competition. In parallel, active labour market policy measures and an effective unemployment insurance scheme have supported individuals as they transition to new

⁵³ Vartiainen, To create and share – the remarkable success and contested future of the Nordic Social-Democratic Model, NordMod2030, 2014, pp. 9, 23; Ekholm et al., Svensk välfärd och globala marknader [Swedish welfare and global markets], Report of the SNS Welfare Policy Council, 2007, pp. 14-15.

Table 4.1 Ranking of countries according to ease of doing business and innovation, 2016

	Ease of starting and operating a local firm	Innovation
Denmark	3	8
South Korea	5	11
Norway	6	22
United Kingdom	7	3
United States	8	4
Sweden	9	2
Finland	13	5
Germany	17	10
Ireland	18	7
Austria	19	20
Canada	22	15
Portugal	25	30
Netherlands	28	9
France	29	18
Spain	32	28
Japan	34	16
Belgium	42	23
Italy	50	29
Luxembourg	59	12
Greece	61	40

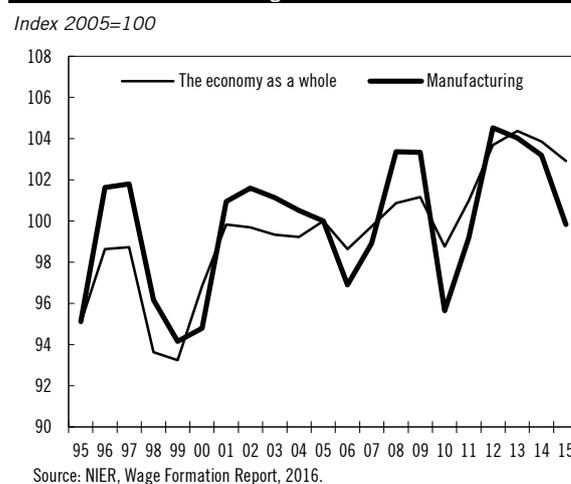
Note. Ease of doing business ranking: the country ranked 1 is the country where it is easiest to start and operate a local firm. A total of 190 countries are included in the sample. Global Innovation Index: ranking 1–100
 Source: World Bank World Economic Indicators, World Bank Economy Rankings; The Global Innovation Index.

As regards Sweden's international competitiveness, the NIER (2016) has determined that the labour cost share has increased more in the past 20 years in Sweden relative to the outside world, in terms of the economy as a whole (see figure 4.10).⁵⁴ The labour cost share is naturally affected by economic fluctuations, and as economic development in Sweden differs from development elsewhere, it is difficult to interpret the trend between two individual years. If one

⁵⁴ The labour cost share shows what portion of the added value in production consists of labour costs and can, expressed in relative terms vis-a-vis the outside world, be used as an indicator of international competitiveness. Unit labour costs show the labour cost per unit produced and if expressed in relative terms vis-a-vis the outside world can, like the labour cost share, be used as an indicator of international competitiveness. However, the advantage to the labour cost share is that it does not consider only the cost side and the price of labour, but also the income side and the value of production (see also Swedish National Institute for Economic Research, Wage Formation Report, 2016. p. 63–69.

looks at the period as a whole, however, an upward trend can be seen, which would indicate a decline in competitiveness. The relative upwards trend may, however, be explained to a significant extent by the change in the composition of the Swedish business sector towards industries that are more labour and knowledge intensive. Manufacturing is the sector of the economy that is particularly vulnerable to international competition. In this sector, fluctuations of the relative labour cost share have been greater than for the economy as a whole, which makes it very uncertain whether there is an upward trend in the data or not, and thus whether there is any clear indication of a loss in competitiveness. Taking into account tendencies in other macroeconomic indicators, with continued high foreign trade surpluses and a high ratio of business investment, the overall assessment is that there are no clear indications that the competitiveness of Swedish business as a whole, including the manufacturing sector has declined in the past 20 years, but rather that it is performing well in international competition.⁵⁵

Figure 4.10 Relative labour cost share in the economy as a whole and in manufacturing



Openness and international competition have, however, not brought only prosperity-increasing gains for the economy, but also greater uncertainty and risks for workers. Income inequality has increased over the past 20 years in Sweden and elsewhere, and Sweden is among the

⁵⁵ NIER, Wage Formation Report, 2016, pp. 61-70.

OECD countries where the increase has been greatest (see section 1). The welfare policy has evolved as a means of managing the risks and making it possible for the economy to reap the advantages of openness. Openness and the welfare policy reinforce each other by sharing the risks and the gains of openness. In so doing, political support for openness and technical progress has been strengthened.⁵⁶

4.4.2 Stabilisation policy

In Sweden, the task of stabilising economic fluctuations lies mainly with the monetary policy. According to the Sveriges Riksbank Act, the objective of monetary policy is to maintain a fixed monetary value. The Riksbank has specified this as an inflation target of an annual change in the consumer price index (CPI) of 2 per cent. At the same time as monetary policy is aimed at attaining the inflation target, it is also to support the objectives of general economic policy for the purpose of attaining sustainable growth and a high level of employment. This is achieved through the Riksbank, in addition to stabilising inflation around the inflation target, endeavouring to stabilise production and employment around paths that are sustainable in the long term.⁵⁷

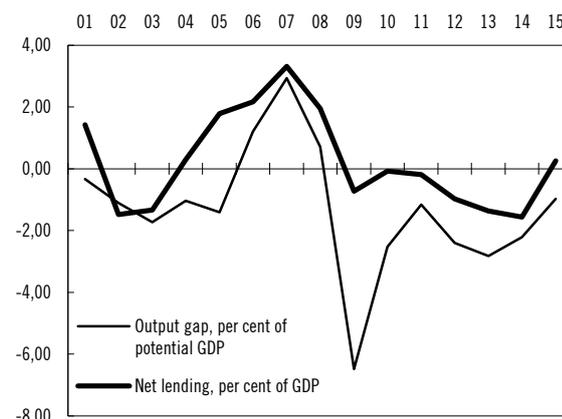
The primary task of fiscal policy in the Swedish model is to contribute to greater prosperity through a well-designed structural policy that promotes a dynamic and competitive business sector, sustainable growth and high employment. The fiscal policy should also promote the equitable distribution of prosperity gains. However, the fiscal policy also plays a role in pursuing the stabilisation policy. Comprehensive public operations have an inherently stabilising effect on the economy. Above all, income-related unemployment insurance functions as an automatic stabilisation mechanism that is reinforced by an active labour market policy. In certain situations, the fiscal

policy can be used more actively to stabilise the economic situation. This applies in particular when resource utilisation in the economy is low at the same time that the monetary policy rate is already so low that it is difficult for the Riksbank to further stimulate the economy. In such a situation, there may be reason to allow the fiscal policy to play a more active role in cyclical stabilisation. An important prerequisite for this is that the Government has sufficient scope for fiscal policy action, that is, that there are large enough buffers in the public finances (see also section 4.1.1). Maintaining such scope for fiscal policy action has been a central reason for the surplus target for the public finances.⁵⁸

Net lending is an indicator of the stabilisation policy direction of fiscal policy, including the effect of the automatic stabilisation mechanisms; that is, not only the active fiscal policy. In relation to how the economy has developed, it can be said that the fiscal policy has generally worked to stabilise the economy (see figure 4.11).

Figure 4.11 Net lending and output gap

Annual percentage change in volume and per cent of potential GDP



Source: Statistics Sweden and Govt Bill 2016/17:100.

5 Concluding remarks

The hallmark of the Swedish model is its overarching objective: prosperity should both grow and be equitably distributed. The interaction among the three pillars is essential, as is the capacity for constructive and pragmatic

⁵⁶ Vartiainen, To create and share – the remarkable success and contested future of the Nordic Social-Democratic Model, NordMod2030, 2014, pp. 9, 23; Ekholm et al., Svensk välfärd och globala marknader [Swedish welfare and global markets], Report of the SNS Welfare Policy Council, 2007, p. 15.

⁵⁷ See The Riksbank's Monetary Policy Report, February 2017.

⁵⁸ SOU 2016:67, p. 200.

cooperation among the social partners and between the partners and political leadership to evolve the model in response to changes in the outside world. The various components of the Swedish model have been continuously adjusted over time in order to manage various challenges and changes in circumstances. The model will have to do this in the future as well, but the objective of greater prosperity that benefits all will remain the fundamental premise of the model.