

Sweden: Achieving Results for Sustained Growth

What are the key challenges?

How does the governance framework contribute to high standards of social welfare?

How to face the challenge of ageing and public finances?

How can regulatory reform help to improve economic performance?

How can the local and European dimensions be integrated?

How can regulatory impacts be effectively assessed?

How to move reforms forward?

For further information

For further reading

Where to contact us?

Introduction

Regulatory reform contributes to promoting sustained economic growth, complementing sound macro-economic policies. While Sweden has made significant progress on regulatory reform since the early 1990s and enjoyed major productivity gains as a result, it should instil more competition in the public sector, cut red tape and liberalise labour markets if it is to meet the challenge of an ageing population and maintain its high standards of social welfare.

Sweden's gross domestic product (GDP) per capita is above the euro area average and its spending on research and development as a percentage of GDP is higher than any other OECD country. But further reforms are needed to build on this success. Despite strong economic growth, few new jobs have been created.

Competition should be improved in key sectors such as construction and food retailing. The Competition Authority should be made more independent and given stronger powers while the regulatory frameworks for the electricity and telecommunications sectors should be modernised. The rules for public procurement should be simplified. The public sector competes in many areas with the private sector, such as running bakeries, gyms and garden centres, which distorts the competitive playing field and hinders the creation of small firms. Firm action to tackle anti-competitive behaviour by state entities has not yet been taken. Co-ordination between national and local levels of government needs to be strengthened. A stronger focal point for regulatory reform within government is also needed. The complex agency structure and its impact on local government efficiency need to be addressed.

Sweden has been a pioneer in setting and meeting ambitious environmental goals, but it should continue to ensure transparency and consultation in a European context, as well as cut red tape further in relation to permits.

This *Policy Brief* looks at Sweden's regulatory reform efforts in recent years and at what further measures are needed. ■

What are the key challenges?

Sweden's strong economic performance and impressive productivity gains since the mid-1990s may not be sustainable over the long term, given the pressures of an ageing society. To fully reap the benefits of globalisation and reduce the risk of job flight, a comprehensive policy response is required. Reforms are necessary to support Sweden's ambitious public policy goals, including high standards of public welfare and social cohesion. Three issues require attention: boosting job creation, improving labour market flexibility and reducing the relatively high inactivity levels; improving the management and performance of public sector service provision; and developing a more resilient economy based on a stronger service sector and greater contribution by entrepreneurs. Local levels of government will need to play a key role in tackling some of these issues.

Sweden's high standards of environmental protection raise growing challenges, including how to take these forward in the EU context, and finding the best way to balance high standards and significant regulation with the cost to business. Although Sweden appears generally competent and innovative in this field, effective regulation of this complex sector has to be viewed as a continuous "work in progress".

Sweden's capacities for carrying out necessary reforms need to be enhanced. Its current regulatory framework shows areas for improvement. Three issues stand out. First, a process or structure is needed to promote a strategic reform vision. Second, there is a need to address issues arising from a complex and bureaucratic agency structure, notably its impact on local government efficiency. Third and not least, there is no framework or forum that systematically brings together the central and local levels of government to manage issues and build a common purpose.

Sweden's economy has made a remarkable recovery from the major crisis of the early 1990s. Regulatory reform was a significant factor behind the resurgence of the economy. Product market deregulation was tackled quite vigorously, and the competition law strengthened. Accession to the EU in 1995 was also a major step. The upswing has been sustained since then. This delivered a considerable "productivity dividend". It appears that deregulation since 1988 has directly added 0.45% to annual productivity growth, and more if indirect effects are taken into account. Another important area is market openness. Substantial efforts have been and continue to be made to minimise regulatory burdens related to international trade.

Policy reforms have also contributed to structural change in the economy including the emergence of high growth sectors such as telecommunications. A better quality labour force has also helped. The ICT industry has become the flagship of the Swedish corporate sector, but other specialist sectors such as car manufacturing and pharmaceuticals are also thriving. Sweden has also benefited from its open markets, linked to a high level of international trade and successful export industries. International commerce has grown significantly faster than the national economy, benefiting from low barriers to trade. Finally, a highly credible monetary policy has helped to underpin the economy.

While there is considerable potential for building on this success, not all factors affecting Swedish performance are so positive. The lack of flexibility in the labour market is an issue. Overall economic performance remains surpassed by a number of OECD countries, particularly outside Europe. Although Sweden now has a relatively robust competition agency, with a strong public presence, there are areas for improvement including the need for stronger powers and greater independence. Competition remains below average in some important parts of the economy, such as the construction sector and food retailing. The infrastructure sectors offer a mixed picture, with some sectors such as electricity in need of renewed attention, and others such as aviation and the railways which are still very much a “work in progress”. Public procurement is in need of reform, even if it is to a large extent governed by EC-Directives, with limited scope for reform in a single member state. Not least, Sweden has a relatively high level of labour market legislation, higher than the OECD average and the other Nordic countries. Efforts to promote competition in the public sector remain insufficient. The lack of an entrepreneurial culture is also a major issue. ■

How does the governance framework contribute to high standards of social welfare?

Economic success has enabled Sweden to develop and maintain high levels of social welfare and supports the achievement of social goals. These include economic security including full employment and equality through the reduction of income differences and the mitigation of poverty, as well as homogeneity of living conditions throughout the country.

Swedish governance has developed around a strong and pervasive role for the state as guardian of society, and a large tax-financed public sector, reflecting citizens' traditional willingness to pay for quality social services through taxation. Public ownership and production are substantial. Sweden is also distinguished by a political and societal culture which is particularly strong on transparency and integrity, reflected in the fact that consensus building is the cornerstone of decision making. Other important features of Swedish governance include a clear distinction between strategic policy-making and implementation, reflected in the institutional and rule-making structure which puts considerable responsibilities on a large number of implementing agencies, and a strong role for local government.

Some of these governance characteristics raise challenges for further reform, such as the consensus-building traditions which have an impact on the timing of decision making. The importance of local government needs to be taken into account in order to secure a shared understanding of common goals between the different levels of government. ■

How to face the challenge of ageing and public finances?

How can the current strong economic performance be sustained so that the ambitious social goals and welfare system can be maintained? This is a challenging task when facing increasing demand for higher standards, especially in public services. Although important steps have been taken to counter the impact of an ageing population, Sweden's own statistics show that over the next 35 years the proportion of the population aged over 65 will increase by almost 40%, and the ratio of those over 65 to the working age

population will peak at around 40%. The direct effect of these changes on labour supply can be expected to slow the rate of growth of GDP per capita.

The Swedish labour market faces certain challenges despite a generally high employment rate. Labour market constraints are already an important issue. Specific issues include a total labour supply which is only average in international comparison; a relatively high incidence of sick leave and disability benefits; limited job creation in response to economic growth; room for improvement in the employment rate; and low labour market flexibility.

Although public finances are in relatively good shape compared with most other OECD countries, ageing still represents a major challenge. Preparations to meet this challenge such as the 1999 pension reform and the fiscal surplus target need to be followed through. Complementary measures to meet possibly higher than expected public expenditure should be considered. One way to contain public expenditure is to make the provision of public services more efficient. ■

How can regulatory reform help to improve economic performance?

Regulatory reform can promote a more efficient public sector by introducing competition in the provision of public services. Outsourcing via public procurement is one way of introducing greater competition. Sweden has adopted the EC Directive on public procurement, but it has proved difficult to ensure full compliance with their requirements, notably the legal remedies prescribed. Progress in this area is hampered by several factors: rules in the legislative and institutional framework set by EC Directives that may prove burdensome for some companies; reluctance by some municipalities and state institutions to change the way they operate and put activities out to tender.

Public sector activities in competitive markets need to be rationalised. Public sector entities show a growing tendency to operate in areas where private companies already exist either at the national or at the local level. This distorts the competitive playing field and impedes the creation of new small firms. Policies to even out regional differences appear to be encouraging government agencies and municipalities into new ventures. A number of reports have challenged this practice, but firm action, such as addressing gaps in the Competition Act to tackle anti-competitive behaviour by state entities has not yet been taken.

Regulatory reform can also help improve the economy's dynamism and resilience, and lift job creation prospects. Entrepreneurial activity remains relatively muted, limiting the potential number of new jobs. SMEs have an important role as drivers of business development and as suppliers of new jobs, but an effective policy framework for the development of entrepreneurship is lacking. Broad policy issues that hold back progress include a lack of competition in the public sector, low venture capital availability, and employment protection legislation. Although Sweden is among the better OECD countries for its efforts at reducing administrative burdens, these burdens do not seem to be fully controlled, and a more systematic approach is needed. Lack of information about the extent and source of administrative burdens hampers progress, and makes it hard to

raise the political profile of the issue. The role of local government in burden reduction has also been overlooked. The setting up of a new body in charge of reducing administrative burdens in 2006 may help in the future.

Regulatory frameworks for important sectors need to be improved and updated. Sectors such as food retailing and housing need to operate within a regulatory framework that supports stronger competition, and in the case of housing, mobility. The infrastructure sectors are often subject to rapid change, and their regulatory frameworks need regular review to reflect this, particularly for telecommunications and electricity. ■

How can the local and European dimensions be integrated?

Swedish counties and municipalities have important delegated tasks across a wide range of public services, as well as a central role in planning and licensing. They are thus key actors in policies aimed at improving public sector efficiency and stimulating entrepreneurship. Important areas for attention at this level are procurement; the provision of services by local government entities in often competitive markets, or ones that should be competitive; and the promotion of entrepreneurship, not least through review of permit and planning processes which are often slow and may benefit from stronger competition.

Ensuring that these levels of government are helping the attainment of social and economic policy goals is an issue for urgent attention. The principle of local autonomy to tailor actions to local conditions needs to be reconciled with the expectation of homogeneity of living conditions across the country. Reaching a shared understanding of objectives at all levels of government remains a challenge and requires an effective management of corresponding trade-offs.

EU accession has also had a strong impact on the regulatory framework, boosting competition in some markets. Accession opened the EU's Single Market fully to Swedish companies, and has given Sweden the opportunity to influence EU-wide developments. Some EU legislation such as the transparency directive which addresses state subsidies has also been a positive addition to Swedish policy and regulation. EU accession has also, however, affected important Swedish traditions of consensus building and accountability. Time for consultation is limited, for example. Management of EU regulatory processes needs to be adequately resourced within the framework of an overall strategy which identifies the most important issues. Local government is often a key stakeholder but needs to be more involved in these processes. Special care is needed in the transposition of EU law to ensure that it does not add to existing regulatory burdens as it is estimated that 44% of such burdens stem from EU legislation. Finally, developing and applying specific tactics for issues that are especially important can be very effective, as Sweden has demonstrated, for example, in the area of acid rain. ■

How can regulatory impacts be effectively assessed?

Regulatory Impact Analysis (RIA) needs further development. The process shows a number of gaps, and responsibilities for its management are fragmented. This may result in a lack of commitment to the process. Benchmarking (regulatory practices, competition between firms, or

international benchmarking) is another potentially powerful tool, and opportunities to apply it should be pursued, especially at local level.

Regulatory tools could also contribute to the efficient attainment of environmental goals. Sweden already uses the creative design and application of effective tools such as the refunded emission payment to reduce NO_x emissions, and these efforts need to be sustained. Its Environmental Code and Environmental Quality Objectives have established an innovative regulatory framework which promotes collaboration across all policy areas and levels of government. However attachment to high standards of environmental protection raises some challenges. This includes how to take these forward in the EU context and finding a way to balance high standards and stringent regulation against business sector costs, whether this is the competitiveness of large firms in international markets, or the burdens of SMEs at home. The cost of environmental regulation is a particular issue for SMEs, which would be helped by the application of an effective RIA process for environmental policies. Meeting environmental goals usually affects a large range of other policies, placing a premium on policy co-ordination, and managing trade-offs is a delicate task. Although Sweden appears quite innovative from an international perspective, effective regulation of this complex sector remains a challenging task. ■

How to move reforms forward?

Although awareness of the need for action is high in Sweden, as illustrated through recent reports, consensus seems hard to establish on reform issues. This is the case for increasingly sensitive issues such as public procurement and health care delivery. The absence of a crisis also means there is no strong spur to action. A process or structure additional to traditional ones may be needed to boost reform, promoting a strategic reform vision and helping to establish consensus on important issues. Communication of this vision should not be neglected. Because of strongly rooted transparency and consensus making-traditions, reforms that are tackled through public debate in Sweden are more likely to gain support.

The following elements could also help to move reforms forward. First, tackling the issue of rule making in stovepipes, which impacts transparency, accountability and efficiency. Sweden has a strong tradition of autonomous action for the different parts of government. Co-ordinating mechanisms are important, but there is also a need for rationalisation. Agencies are responsible for the largest part of the Swedish regulatory system, and streamlining the large and growing number of agencies would reduce complexity, particularly co-ordinating their impact at the local level.

Second, developing a stronger focal point for regulatory policy within government. Although there has been a steady flow of technical developments in Swedish regulatory policies, and particular attention to the needs of SMEs, this does not yet amount to a comprehensive and coherent regulatory policy. Regulatory policy is dispersed across several institutions, including agencies, which makes it hard to manage major reforms that involve a large number of potentially powerful players.

Third, improving co-ordination between national and local levels of government. There is no framework or forum yet in place that systematically brings together the central and local levels of government to manage issues and build a common purpose. There may be a tendency to over regulate local governments, with a need to move further to agree on shared objectives.

Fourth, strengthening the contribution to pro-competitive reform that can be made by the competition authority. Experience with the current framework reveals the need for improvements. The Competition Authority appears to need enhanced skills and competencies, more independence, and stronger enforcement. This also applies to the independent regulators, which lack powers and independence. Although the agency model which has been adopted for Swedish regulators secures a certain independence from ministries, it falls short of international best practice in some respects, including the lack of sanctions, an unclear relationship with the Competition Authority, and a relative lack of transparency and independent status which would give regulators more clout in dealing with ex monopolies.

Beyond these points, it would also be important to capitalise on the role of the Parliament and the National Audit Office in promoting reform. Both institutions have played an important role in recent times drawing attention to reform issues such as competition between the public and private sector. ■

**For further
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For further reading

OECD (2007), **Sweden: Achieving Results for Sustained Growth – OECD Reviews of Regulatory Reform**, ISBN: 978-92-64-00851-9, € 30, 108 pages.

OECD (2005), **Guiding Principles for Regulatory Quality and Performance**. Available at: www.oecd.org/regreform.

OECD (2006), **Cutting Red Tape: National Strategies for Administrative Simplification**, ISBN: 978-92-64-02978-1, € 45, 141 pages.

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