



OECD Economic Surveys

SWEDEN

Executive Summary

March 2019



- **Economic growth is broad-based**
- **Inequality is low and well-being high**
- **Environmental policies are ambitious**
- **Macroeconomic policy is supportive**
- **The housing market has cooled**
- **The school system needs strengthening**

Main findings

Macroeconomic policies

- Inflation is close to the 2% target and capacity utilisation is high after several years of strong growth.
- Public finances are healthy, supported by a strong fiscal framework. Fiscal policy has supported the recovery, but is becoming less expansionary.

Environmental and green finance policies

- Implicit carbon taxes on fossil fuels are much higher in household than in industrial use.
- Climate change and climate change mitigation policies generate new financial risks and opportunities for investors.

Housing policy

- Housing prices have stabilised, but structural weaknesses remain, with potential adverse effects on financial and economic stability, as well as on mobility and well-being. The 2015 22-point government housing plan is a step in the right direction, but broader reforms are needed.
- Inefficient land-use planning and low incentives for municipalities to encourage construction contribute to housing shortages, which reduce affordability and labour mobility, despite useful recent measures to release land for development and speed up planning processes.
- Strict rental regulations tend to discourage mobility, notably for low-income households, and may contribute to spatial segregation.

Business regulations and competition policies

- Business regulations and administrative procedures are generally lean, but further streamlining could raise productivity.

Labour market and adult skills policy

- The integration of immigrants has improved, thanks to enhanced integration policies and strong demand for labour. Technological developments increase re-skilling needs for a large share of workers.

Education policy

- School segregation has intensified while compensatory funding has remained relatively constant. Schools with weaker pupil backgrounds lack qualified, experienced teachers and material resources.
- The central government lacks a regional structure to steer and develop schools, while many municipalities lack the necessary scale.
- No objective benchmark of school performance exists. Entry to upper secondary and tertiary education depend on grades, but grading practices differ between schools. The grading- and upper secondary entry systems put heavy weight on fail grades, notably in the core subjects Swedish, mathematics and English.
- School segregation has intensified and municipalities assign school places based on a strictly interpreted proximity principle, while private schools mostly assign places based on queuing time.
- Teacher quality affects pupil outcomes, but teacher education is fragmented and of relatively low status in Sweden.
- Mentoring and peer-to-peer learning improves teacher quality and job satisfaction, but are applied in a patchy manner across Sweden.

Key recommendations

Macroeconomic policies

- Continue to raise interest rates gradually, taking inflation and output developments into account.
- Continue to run budget surpluses while the economy remains solid.
In the case of a downturn, use the space provided by the fiscal framework.

Environmental and green finance policies

- Raise taxes on industrial energy use.
- Strengthen and further harmonise climate-related disclosure requirements, especially for financial intermediaries, including banks.

Housing policy

- Reform the recurrent property tax to better align tax charges with property values.
Phase out the deductibility of mortgage interest rate payments.
- Enhance co-operation between central and local government in land-use planning and increase incentives for municipalities to facilitate the timely release of development land.
- Simplify land-use planning procedures, balancing economic, environmental and social considerations.
- Ease rental regulations to incentivise rental housing supply, mobility and better utilisation of the housing stock, while maintaining tenant protection against abuse.

Business regulations and competition policies

- Continue to use digital tools to improve services, simplify procedures and shorten licences and permits processing times.

Labour market and adult skills policy

- Develop adult education, in cooperation with the social partners, including for people in unconventional forms of work.

Education policy

- Introduce a non-binding minimum norm of school financing, integrated with the national income equalisation system, to better target funding towards disadvantaged groups, including immigrants.
- Develop a regional arm of the central government school governance structure tasked with systematic quality improvement, inducing local cooperation, continuous teacher training and inspections.
- Remove sources of bias in national test grading to create an objective benchmark for school performance, and use it to remove differences in grading leniency.
- Weigh high and low grades symmetrically and suppress the requirement to pass in certain subjects to enter upper secondary education.
- Take the socio-economic mix into account when investing in new schools and in school entry.
- Strengthen teacher education with more instruction time, teacher practice and research.
- Improve continuous learning and development through a regional school governance structure, systematic peer learning and continued mutually beneficial cooperation with universities.

Economic growth is broad-based

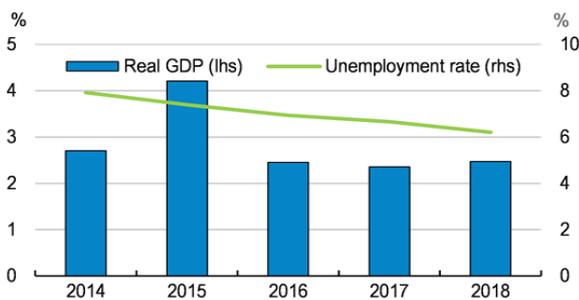
The expansion is strong. GDP has expanded at an average rate of close to 3% over the past five years (Figure A). The upswing has been broad-based, with robust consumption, investment and exports.

Unemployment has receded. Employment has grown steadily and the unemployment rate has fallen (Figure A). But jobseekers are increasingly low-skilled and immigrants, who struggle to find jobs.

Economic growth will moderate as capacity constraints tighten. Growth will slow, as the economy now operates around full capacity and labour shortages appear in many sectors (Table A). Shrinking residential investment following housing price falls is a further drag on the economy. Exports are expected to remain solid as long as the global economy keeps expanding.

Global uncertainties weigh on the outlook. The global economic environment is laden with uncertainties. As a small open economy highly dependent on exports, Sweden is vulnerable to potential global shocks, such as further intensification in global trade tensions, a disorderly Brexit, stress in European sovereign bond markets, as well as domestic events such as a severe drop of the housing market.

Figure A. Robust growth reduces unemployment



Source: OECD Economic Outlook database.

Table A. Economic growth is projected to remain robust

	2018	2019	2020
Gross domestic product	2.4	1.6	1.7
Private consumption	1.2	1.6	2.0
Gross fixed capital formation	3.5	-0.7	1.4
Exports	3.7	3.4	3.2
Imports	3.1	2.5	3.2
Unemployment rate	6.3	6.2	6.1
Consumer prices	2.0	2.0	2.1
CPI with fixed mortgage rate (CPIF)	2.1	2.0	2.0
Current account (% of GDP)	2.5	3.4	3.5
General government fiscal balance (% of GDP)	0.7	0.4	0.5

Source: OECD Economic Outlook 104 database, updated based on available information as of 28/02/2019.

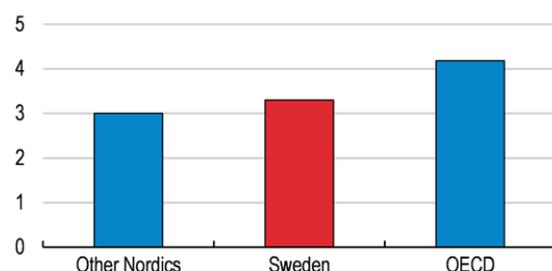
Inequality is low and well-being high

Rising employment has contributed to enhancing well-being and reducing poverty. However, robust capital income growth has pushed up inequality over the past few years.

Nevertheless, inequality remains low, albeit higher than in the other Nordic countries (Figure B).

Amending tax rules for unlisted companies and property, without increasing the overall tax burden, could help hold back inequality.

Figure B. Income inequality remains low
Ratio of ninth to first disposable income decile, 2016 or latest



Source: OECD Income Distribution Database (IDD).

Environmental policies are ambitious

Sweden is a frontrunner in the fight against climate change and in greening the economy. CO₂ emissions per unit of GDP are well below the OECD average and falling. Air quality is good and environment-related patenting strong.

The government has stepped up efforts, increasing investments in environmental protection and nature conservation. It has set clear objectives and policies to reduce carbon emissions and put in place an independent climate council to monitor progress. In addition to the carbon tax, the EU Emissions Trading Scheme and blending obligation for biofuels, there are measures such as subsidising solar cells, electric vehicles and charging points and supporting company and municipal investments reducing climate impact.



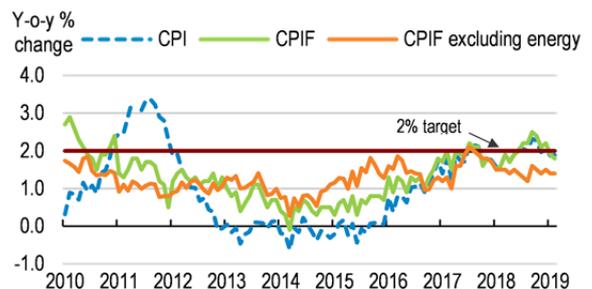
The macroeconomic policy stance is appropriately turning slightly counter-cyclical

Fiscal policy has supported the recovery. Two decades of prudent policy had created the fiscal space for Sweden to use fiscal expansion to dampen recessions.

In recent years, additional resources have been channelled to key areas such as education, immigrant integration, health, defence and environment protection, providing some stimulus despite high capacity utilisation. The 2019 budget is slightly expansionary, which is appropriate, especially as reduced margins for monetary policy will require fiscal policy to play a greater stabilising role in the next downturn.

Monetary policy has started to tighten, but remains supportive. With inflation close to the 2% target, albeit with some help from rising energy prices, the time has come to begin withdrawing stimulus (Figure C). Inflation expectations are close to the target. The Riksbank has started withdrawing monetary support, with a 25 basis points repo rate hike to -0.25% in December 2018. The gradual normalisation of policy rates should continue, to balance the risks of inflation undershooting against those of excess inflation and debt.

Figure C. Inflation is close to the target



Note: CPIF is CPI with fixed mortgage rate.

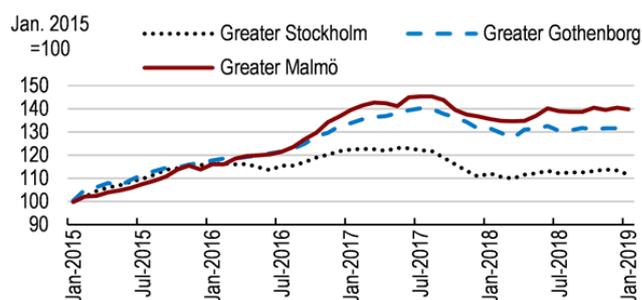
Source: OECD Economic Outlook database and Riksbank.

The housing market has cooled

Housing prices have fallen slightly. Housing prices have fallen since mid-2017, largely as a result of increased supply of tenant-owned apartments in big cities (Figure D), but seem to be stabilising.

Macroprudential measures, notably the introduction of a mortgage amortisation requirement, have also contributed to contain household indebtedness and housing price increases. Nevertheless, the housing price-to-income ratio remains about 30% above its long-term average and household debt continues to rise. Structural reforms are needed for the housing market to become more responsive to people's needs.

Figure D. Housing prices have fallen in big cities



Source: Valueguard.

Reducing regulation could lift productivity and well-being

The housing market suffers from excessive regulation that hinders the supply of new homes.

The government is implementing a 22-point plan including measures to release more land for development, accelerate planning processes and subsidise the construction of affordable housing.

While this is going in the right direction, broader reforms will be needed to achieve a well-functioning housing system, in particular moving towards more tenure-neutral taxation, further streamlining land-use planning procedures and easing rental regulations. Greater competition could help lower construction costs.

There is room for further progress on regulations and administrative procedures. Sweden is among the most business-friendly countries in the OECD. Nevertheless, some regulations and administrative procedures could be streamlined, taking advantage of the new opportunities offered by digitalisation.



Evolving work patterns create challenges

Automation increases re-skilling needs.

Digitalisation offers great opportunities to raise productivity, but puts nearly a third of jobs at risk of automation or significant change. Hence investment in re-skilling and up-skilling will be crucial to inclusive growth. This requires strengthening the foundation skills of the workforce and developing adult education, in cooperation with the social partners.

Labour legislation should adapt to evolving work patterns.

As unconventional forms of work gain ground, labour legislation will need to evolve to ensure the right balance between flexibility and protection for all workers. New rules should be designed in close cooperation with the social partners.

Improving primary and lower secondary school results is crucial

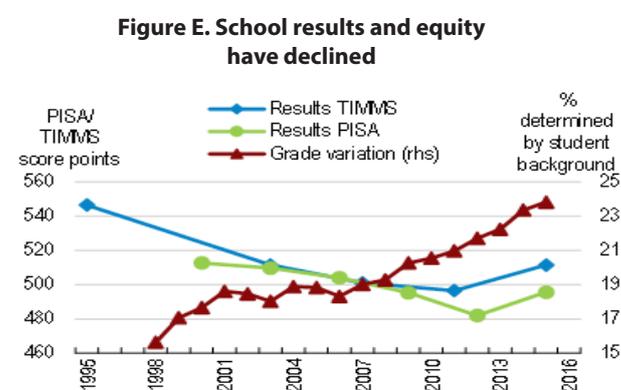
Swedish school results have declined for two decades. Issues with design and implementation of a series of reforms in the early 1990s, coinciding with a deep economic crisis, likely contributed (Figure E). School inequalities, driven by residential segregation and school choice, likely reduce equality of opportunity. A reform programme for primary and lower secondary schools should coordinate funding better and strengthen governance, combine school choice and competition with greater attention to socio-economic diversity, and increase the attractiveness of teaching.

The institutional set-up of the school system needs strengthening. School funding has to better target needs related to pupils' different socio-economic backgrounds. Developing a regional arm of the central government governance structure would enhance local cooperation, improve skills development, promote continuous quality improvements, and instil accountability at every level of the school system.

Competition and school choice must be steered to deliver for the public good. Municipalities need to take the socio-economic mix of pupils into account in municipal school entry and when investing in new schools. A liberal regime for the establishment and expansion of private schools needs to internalise a broader set of criteria, notably to counteract segregation. Municipalities should have a stronger say in such decisions. Pupils should be assigned to over-subscribed private compulsory schools by lottery, possibly with quotas reserved for pupils with unfavourable socio-economic backgrounds.

Teaching needs to become more attractive to address current teacher shortages, which are most acute in remote locations and set to intensify as the number of school-age children increases.

Improving teacher education with a stronger research base, more instruction time and teaching practice, strengthened continuous learning and development, as well as feedback and support mechanisms to foster more cooperation between colleagues, would help. Furthermore, principals and education personnel should be shielded from unnecessary administrative procedures.



Source: OECD (2016), Mullis et al. (2016), Martin et al. (2016), and Swedish National Agency for Education (2018).

SWEDEN

The Swedish economy is growing steadily, but the expansion has peaked and global uncertainties weigh on the outlook. Monetary and fiscal stimulus has supported the recovery, but is being gradually withdrawn as the economy operates close to full capacity. Strong public finances provide space for fiscal loosening in the case of a downturn, especially as low interest rates reduce monetary policy margins. Beyond a strong economy, Sweden enjoys high well-being, low inequality and strong environmental performance. Nevertheless, some structural issues need to be addressed, notably alleviating obstacles to housing affordability and enhancing the efficiency of public services by seizing the opportunities offered by digitalisation. Maintaining a high level of workforce skills is essential to sustain growth, competitiveness and social cohesion, calling for action to lift educational performance and promote lifelong learning. Against a background of lacklustre school results and increasing segregation, this Survey proposes a coherent set of reforms to strengthen education institutions, better target funding to pupils' needs, enhance the steering of competition and school choice, increase the attractiveness of the teaching profession and reinforce teacher education.

SPECIAL FEATURE: EDUCATION