Swedish Fiscal Policy Council
Background and organization

Meeting with Jean-Philippe COTIS

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Sweden during the Recent Crisis

- Despite a 5% drop in GDP in 2009 and previously high fiscal balance elasticity, Sweden:
  - Moderate drop in fiscal balance;
  - Modest maximum deficit of 0.7%. Now surplus;
  - Recovered to pre-crisis GDP in 2010.

- Very different from the crisis in early 1990s: similar amplitude in GDP fall, but then an extreme deterioration of public finances and rise in unemployment and long recovery.

- Key explanations for Sweden’s good performance:
  - Important reforms were undertaken during the 1990s;
  - No structural imbalances – no domestic amplification mechanisms;
  - Strong budget before crisis due to well-functioning fiscal framework;
  - A conservative Finance Minister determined not to repeat mistakes;
  - Luck…
Background to Reforms

- Sweden suffered a deep economic crisis in the 1990s:
  - Credit market deregulation in 1980s led to rapid credit expansion;
  - Rapidly increasing property prices, then collapse;
  - Banking crisis;
  - Large real appreciation leading up to crisis;
  - Exploding unemployment rates;
  - Very high interest rates;
  - Structural problems became apparent (tax system, pension system, wage formation, long run growth…).

- Similar to the current crisis in Spain.

- Crisis created a wide consensus on need for a major *makeover*. 
A Comprehensive Makeover

- A new tax system:
  - Corporate taxes cut in half;
  - Marginal top income taxes reduced from 70% to 50%;
  - VAT tax base broadened.

- Insolvent banks taken over and split into good and bad banks. Ultimately not bad deal for tax payers;

- EU membership in 1995;

- Election periods extended to 4 years;
A Comprehensive Makeover

- Stricter competition law; deregulation and privatizations of rail, telecom, taxi, schools, post, electricity;
- Tough fiscal consolidation (1993-1998, ~ 11% of GDP);
- Delegation of monetary policy to independent central bank with inflation target. Large initial depreciation. Then more stable development of prices and wages.
- New contributions-defined pension system, immune to variation in growth and demographics;
- New Fiscal Policy Framework. (FPC much later)
The Swedish Fiscal Framework

- Top-down budget process;
- A fiscal *surplus target* for general government net lending of 1% of GDP, on average, over the business-cycle. Involves judgment;
- Central government *expenditure ceiling* set 3 years in advance;
- Balanced budget requirement for local governments;
- Since 2007, a Fiscal Policy Council with a broad remit (to facilitate transparency and accountability);
- *Note: The strength of this framework depends on the political will to respect it…*
Lessons from the Crisis in the 1990s

- **Structural problems must be identified early**
  - Crisis often reveals structural problems;
  - Automatic stabilizers, fiscal policy and social safety nets work well for temporary shocks in countries with no structural problems but not when problems are structural.

- **All reasons for deficit bias need to be identified and addressed**
  - Common pool, information, time consistency.

- **Mandate for change**
  - Crisis creates a window of opportunity for change, but broad political *and* popular support for reform necessary. A political *story* is needed;
  - Institutional reform should be politically neutral.
  - Institutional reforms can peg down and enhance institutional memory.

- **Competitiveness is key for fiscal adjustment.**
  - Fisal adjustment largely after growth had resumed.
The set-up of the council

- Established in 2007, at first politically controversial.
- An agency under the Government;
- Six members:
  - Academics (typically well-known and resting on tradition of strong public standing);
  - Policy-making experience;
- Supplementary activities to ordinary jobs (mainly academic positions);
- Small secretariat: five persons;
- Annual budget 900 000 €;
- Some provisions to safeguard the Council’s independence, but more important is strong outside option of academics. Not a career path.
THE RIKSDAG (Parliament)  
349 members

GOVERNMENT  
24 Ministers

The Committee on Finance  
17 members

Ministry of Finance  
470 employees

The Swedish National Audit Office  
300 employees

The Riksbank (Central Bank)  
400 employees

Swedish Fiscal Policy Council

The Swedish National Financial Management Authority  
160 employees

The National Institute for Economic Research  
60 employees

The Council  
6 members  
Chairman: Lars Jonung

The agency  
5 employees

The Swedish National Audit Office

The Riksbank (Central Bank)

Swedish Fiscal Policy Council

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The tasks of the Fiscal Policy Council

1. Focus on *ex post* evaluation, with some *ex ante* evaluation;
2. Quite broad remit with substantial freedom to interpret.
3. Evaluate whether fiscal policy meets its objectives:
   - Long-run sustainability, surplus target, expenditure ceiling;
   - Fiscal stance wrt business cycle.
4. Evaluate if developments are in line with healthy sustainable growth and sustainable high employment;
5. Monitor transparency of government budget proposals and motivations for various policy measures;
6. Analyze effects of fiscal policy on distribution of welfare;
7. Contribute to better economic policy discussion in general:
   - Annual report in May (this year May, 14);
   - More information on [www.finanspolitiskaradet.se](http://www.finanspolitiskaradet.se).
Has the fiscal policy framework worked?

- Generally successful implementation:
  - Top-down approach is followed;
  - Spending ceilings have not been passed (albeit some minor, and politically costly, examples of creative bookkeeping);
  - Surplus target has been met – at least until now… (various indicators used);
  - Broad political support: opposition (and FPC!) wanted more spending during crisis, but less than 1% of GDP;
  - The Fiscal Policy Council has increased the transparency and facilitated a higher quality of the political discussion.
Growth and Unemployment 1985-2012

Note: Growth rate of GDP (percent) in Sweden and weighted average of 19 OECD countries.

Source: OECD Economic Outlook December 2011.
General Government Net Lending as % of GDP 1976-2011
General Government Net Lending as % of GDP 1976-2011

- Total (central/right govt.)
- Total (left govt.)
- Local
Swedish prices relative to French and German

![Graph showing Swedish prices relative to French and German over time. The graph includes two lines, one for SE/GE and one for SE/FR, with data points from 1970 to 2008.]
Average retirement age – state employees

Retirement age

1999 2000 2001 2002 2003 2004 2005 2006 2007 2008 2009

Females Males

FINANSPOLITISKA RÅDET
SWEDISH FISCAL POLICY COUNCIL
Themes in the reports

- Increase the clarity of the surplus target (net lending of 1% of GDP over a business cycle):
  - Underlying fundamental objectives
  - Too many indicators
- Criticism of circumventions of the expenditure ceiling;
- Critical evaluation of the fiscal sustainability calculations;
- Request for additional discretionary fiscal stimulus in the current recession (but less of permanent measures);
- Critical evaluation of the Government’s labor market reforms;
- The economic reporting of the Government.