1. Introduction

In the mid-2000s, my colleague Harald Niklasson and I published an article, ‘The Swedish Model in Turbulent Times’, retracing the main developments of the Swedish model since its inception in the early 1950s up to the early 2000s (Anxo and Niklasson 2006). Our main conclusion was that, at the turn of the century, the Swedish model appeared more in line with the core components of the original Swedish model than during the decades 1970–1980, which constituted, in our views, a clear deviation. During the 1990s, the economic policy modifications towards more restrictive and anti-inflationary macroeconomic policies, the re-orientation of active labour market policies towards supply-oriented measures and the structural reforms undertaken in wage formation, tax and social protection systems suggested a revival of the Swedish model. After a period of turbulence related to the early 1990s economic crisis, the Swedish economy underwent particularly favourable economic development. Up to the current global recession, unemployment oscillated between 5 and 6 per cent, inflation was curbed and current account and public finances were restored.

1. Namely, a macroeconomic policy combining full employment and price stability, a centralised and coordinated wage bargaining system and the application of a wage norm, the so-called ‘solidaristic’ wage policy based on fairness (same wage for the same job independently of the profitability of the firm/industry) and efficiency (that is, fostering rationalisation at the company level and promoting productivity-enhancing structural changes through closure of unproductive plants). Last but not least the implementation of an ambitious countercyclical Active Labour Market Policy (ALMP) favouring occupational and geographical mobility. Low unemployment and full employment are to be secured mainly by supply-oriented ALMP programmes favouring a reallocation of the labour force from the declining parts of the economy to the expanding ones.
Although the re-orientation of macroeconomic and employment policy during this period might explain the ‘Swedish success story’, the modifications in Swedish industrial relations – in particular, the clear tendency to re-coordinate wage bargaining – without doubt played a vital role in the Swedish recovery. These new developments reflected a desire on both sides of industry to re-coordinate collective bargaining at industry level and restore the leading role of the traded good sectors in wage formation. The tendency towards a re-coordination of collective bargaining co-existed with a marked tendency to the decentralisation and individualisation of wage setting and working conditions.

We also claimed that strong trade union organisations and high union density at company level ensured the implementation of negotiated forms of individualisation and differentiation (negotiated flexibility). In our view, these tendencies should not be interpreted as a weakening of the Swedish collective bargaining tradition, but rather as a recomposition and adaptation of the Swedish model of industrial relations in the face of the major transformations of work organisation and production processes over recent decades. In our view, these developments did not call into question the basis of the Swedish model, namely a strong contractual tradition based on the existence of powerful social partners who enjoy considerable autonomy from the public authorities, but instead reflected a transition and adjustment of the Swedish model to the new challenges posed by post-industrial societies.

Also during this period, the various reforms of the Swedish social protection system essentially took the form of a temporary reduction of income compensation and, perhaps with the exception of the fundamental restructuring of the pension system, left the architecture of the Swedish welfare state system almost intact. The Swedish social protection system remained, by international standards, clearly universal and inclusive in nature and still enjoyed a high level of across-the-board political and public support. The structural reforms undertaken in the tax and benefit system – in particular, the reshaping of the pension system and the tax reform initiated in the early 1990s aimed at strengthening work incentives and fostering investment in human capital – was also clearly in line with the general philosophy of the original Swedish model favouring the ‘work first line’, integrative transitions across the life course instead of passive support and social exclusion.
Last but not least, the third main element of the Swedish model, the extensive use of active labour market policy (ALMP) – that is, the overall policy of activation – still occupied a central role in Swedish stabilisation policy. Its re-orientation towards a supply-oriented policy (occupational and geographical mobility, active search programmes, labour market training and so on) in many respects appears to be in accordance with the strategy initiated in the 1950s.

Since the publication of the article in question, two major events have occurred in Sweden that could cast doubt on our optimistic view of a renaissance of the Swedish model. First, the Social Democratic Party lost power and a conservative-liberal coalition government took office in September 2006. The same political coalition was re-elected at the last parliamentary election in September 2010. During its first term of office, the new government conducted several neoliberal policy reforms, concerning among other things the tax and social protection systems, as well as reforms aimed at opening up public welfare services (health care, elderly care, social services and education) to competition. Second, in early autumn 2008, the global economic recession hit Sweden severely and some aspects of the macroeconomic policy implemented might also be interpreted as a departure from the original model.

The present chapter is structured as follows: after a description of the major policy developments since 2006 and their potential impacts during the current crisis we analyse the policy strategy adopted, and identify the groups particularly affected by the crisis. Finally, Section 4 reflects on the potential impact of the Great Recession on the Swedish model and economy.

2. Development of the Swedish model prior to the crisis

The several structural reforms undertaken by the current government during its first term of office (2006–2010) were aimed principally at increasing labour utilisation in the long run, through essentially supply-oriented measures, such as tax cuts and reforms of the social protection system (unemployment benefit and sickness insurance). Several tax reforms were conducted aimed at reducing the tax wedge and increasing labour supply at both the extensive and intensive margins. The
inheritance and wealth taxes were abolished in 2005 and 2007, respectively. The corporate tax rate was reduced,2 as was the total levy of social security contributions. Reforms of income tax have also been implemented gradually over the past five years. The most important tax reform in this context was the introduction of a system of in-work tax credits aimed at strengthening work incentives for low-income earners and a reduction of marginal tax for high income earners, both reforms entailing a reduction of marginal tax of around 2–3 percentage points.

Other important structural reforms concern the social protection system, namely unemployment insurance (stricter eligibility rules and lowering of benefits), as well as sickness insurance (more stringent rules, increased supervision and monitoring of a person’s capacity to work). A new unemployment insurance system took effect in 2007. Eligibility for unemployment benefits after the reform was based on the past 12 months’ earnings instead of the past six months. The reform also implied a significant diminution in the generosity of the Swedish unemployment insurance system, the income replacement rate being reduced from 80 per cent to 70 per cent after 200 days of unemployment. Furthermore, the maximum duration for receiving unemployment benefit was reduced to 300 days (450 days for unemployed people with children). The maximum daily benefit was lowered from SEK 730 to SEK 680.3 Altogether, this implies that the benefit level decreased by around 3 percentage points.

Furthermore, the right for a job seeker to restrict their search during the first 100 days to jobs according to their formal qualifications and vicinity was abolished. While these structural reforms might have increased ‘work incentives’ and job search intensity4 and might have reduced unemployment duration it should be stressed that this reform in itself does not improve the employability of vulnerable groups in the labour market and is also critically dependent on the development of labour demand for these groups. We may also contest that such a

\[2. \quad \text{From 28 per cent to 26.3 per cent.}\]
\[3. \quad 1 \text{ SEK} = 0.11 \text{ euro.}\]
\[4. \quad \text{A study conducted by the National Institute for Economic Research, NIER (2010), shows that the gradual introduction of income tax credits and the various reforms of the social protection system (unemployment and sickness insurance) between 2006 and 2010 decreased the total marginal tax effect by almost 5 percentage points. According to the same study, the so-called threshold effect (that is, the net increase in income due to taking a job) has also increased significantly.}\]
reform – in particular the abolition of the right of job seekers to restrict their search to jobs in accordance with their formal qualifications and vicinity – may lead to more efficient resource allocation in the economy, in particular in a period of reduced labour demand.

The second major reform concerns modifications in the financing of the unemployment insurance system: the contributions of the various Unemployment Funds administered by the trade unions (the Ghent system) were, after this reform, differentiated according to the unemployment level in the sector/industry concerned. In other words, a system of experience rating was introduced, individual unemployment insurance contributions being raised or lowered depending on whether unemployment increases or decreases in an industry. This reform entailed a large increase in individual contributions; in some cases, individual unemployment insurance fees tripled. The consequence was both a large decrease in union membership and a dramatic decline in the number of dependent employees covered by the unemployment insurance system: around 500,000 employees left the unemployment insurance system between 2007 and 2008. The most frequent reason for leaving the unemployment insurance funds was financial strain due to the rise in individual fees. The drop in membership was particularly severe in hotels and restaurants, retail and transport, as well as among municipal workers (see Eliasson 2008). Between 2006 and 2009, union density declined by 7 percentage points for blue-collar workers and by 7 percentage for white-collar workers (see Kjellberg 2010).

Obviously, the main objective of the government with this reform was to indirectly influence the outcome of wage bargaining by weakening the bargaining power of trade unions and therefore to induce wage restraint. The modification of the financing of unemployment insurance and the corresponding diminution of the number of persons covered by it meant that a large number of wage-earners, in particular low-paid/low-skilled employees with unstable employment conditions, lacked sufficient protection in case of unemployment – a potentially major problem.

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5. The Swedish public unemployment insurance system is regulated and subsidised by the state, but is administered by the trade unions’ unemployment insurance funds (Ghent system).

6. From 77 to 70 per cent for blue-collar workers and from 77 to 72 per cent for white-collars.
during the current recession. In other words, there are strong reasons to believe that the 2008 recession increased the number of social benefit recipients among individuals not covered or entitled to unemployment insurance, increased income inequalities (see next section) and amplified the risk of social exclusion for vulnerable groups. On the other hand, the increase of unemployment risk in connection to the global crisis has partly reversed the negative trends in unemployment insurance fund membership and also in union density. It should also be stressed that, despite the decline of union membership, Swedish union density remains high by international standards (70 per cent) and the coverage rate of collective bargaining is still around 90 per cent. In this sense it can be said that the Swedish model of industrial relations to date has been only marginally affected by these reforms, implying that the bulk of labour market regulations, working conditions and wage setting in Sweden will continue to be determined and regulated by collective agreements.

The Swedish model has been based on a strong political commitment to the goal of full employment. Despite the current political rhetoric, we argue that the policy developments testify to a weakening of this commitment with a clear re-orientation of macroeconomic policy towards price stability and budget balance. Employment rates are still clearly below their early 1990s level and unemployment rates are also significantly above the rates prevailing during the 1970s–1980s. True, the decline of employment rates since the early 1990s also reflects major investment in education and a general trend toward a postponement of entry into the labour market. However, compared to other EU Member States, such as Austria and Germany, part of the transition from school to work remains problematic in Sweden, with comparatively high youth unemployment. If Sweden might be classified as 'no country for young men/women' (to modify Yeats), on the other hand it is a relatively good country for old men (women), with the highest employment rates among senior workers in the EU.

3. Impact of the crisis on the Swedish economy and model

In the wake of the global financial crisis, the Swedish economy started to deteriorate rapidly in the second half of 2008. In 2009, Sweden's
GDP decreased by 5.1 per cent, the worst deterioration since the Second World War. With the severe drop in output and aggregate demand, employment declined sharply. Between 2007 and 2009, employment decreased by more than 100,000, while the unemployment rate increased from 5.9 per cent to 8.4 per cent. The fall in output and employment was particularly marked in manufacturing, with decreases of 25 and 20 per cent, respectively, while employment increased by almost 10 per cent in the private service sector and in construction. Employment also declined significantly in the female-dominated public sector, in particular at the municipality and county level, which are responsible for social services, health and education. The recession led to a reduction of tax revenues for local authorities due to the sharp increase of unemployment, local plant closures and the overall reduction of economic growth. In a first phase, this situation led to severe budget cuts at the local level and a decline in employment, in particular among public employees on short-term contracts. With regard to Swedish manufacturing, the fall in employment was particularly marked in export-oriented industries.

3.1 Policy responses: macroeconomic and labour market policy

In the face of the drastic worsening of the economic situation, as well as the growing awareness that Sweden will experience a much more dramatic drop in output and employment, the government took financial and fiscal stimuli measures at the end of 2008. In particular, extensive investments in the maintenance and operation of the road and rail networks were decided on. As far as the crisis of the financial system is concerned, the government launched a guarantee programme, aimed at securing the medium-term borrowing of banks and mortgage institutions and lowering the cost of borrowing for households and companies. In order to stimulate activity and maintain labour demand in the construction sector, work in the form of repairs, maintenance and improvement of one-family houses and tenant housing were made tax deductible. During 2009–2010, the government announced further countercyclical expansive fiscal measures to combat the crisis. These new fiscal measures covered mainly two areas: increased government grants to municipalities and county councils and more resources for active labour market policy. In September 2009, the government decided on a further increase of SEK 10 billion in the central government
grant to municipalities and county councils in 2010, as well as further investment in infrastructure (SEK 1 billion) in order to maintain and secure employment in the public sector.

As far as tax policy is concerned, the government introduced a fourth step in the abovementioned in-work tax credit (SEK 10 billion), a reduction in social security contributions for the self-employed, a further reduction in income taxes for low income pensioners and an increase in housing benefit for the long-term sick and the long-term unemployed. In order to limit the negative impact on poverty and social exclusion of the 2007 unemployment insurance reform in July 2009 the government decided on a reduction in individual unemployment contributions. The government also amended membership requirements temporarily so that members of an unemployment insurance fund in 2009 would be able to count one month extra for each month of membership in 2009. Another change introduced was that unemployment contributions were again tax deductible for employed members.

Since the late 1950s, active labour market policy (ALMP) has played a vital role in Swedish stabilisation policies. The preference for the principle of employment promotion (work-first principle) has always predominated over benefit options for the unemployed. In contrast to the 1990s crisis, when the bulk of counter-cyclical measures essentially took the form of an increase in the number of participants in various active labour market policy programmes, the Swedish government relied to a greater extent on expansionary fiscal and monetary policy to counteract the current economic recession. It is also clear that, in comparison to the 1990s crisis, the room for manoeuvre in which to conduct a more expansive macroeconomic policy was greater than previously, due to healthier public finances at the start of the economic downturn. Regarding active labour market policy measures, the volume of participants in the various ALMP programmes was gradually increased, but never attained the number of participants enrolled during the last severe recession in the early 1990s. The difference concerns not only the number of participants, but also the composition of ALMP measures. Compared to the previous crisis, the current government has focused more on labour supply-oriented and matching measures (job search assistance, coaching) and/or work experience and trainee schemes. The number of participants in traditional labour market training has also slightly increased, but much
less than in the previous recession. All in all, the number of participants in labour market policy programmes has increased but, as already mentioned, less than during the previous economic crisis. It should also be noted that public sector job creation has not been used in connection with the crisis, but the increase of central government grants to local governments has certainly had an effect in limiting the fall of employment in the female-dominated public sector.

3.2 Employment adjustment, wage setting and income inequalities

Traditionally and in line with the core elements of the Swedish model, economic downturns and structural changes have seldom been accompanied by measures aimed at maintaining the level of employment. In contrast to other European Member States, such as France or Germany, public policies aimed at reducing working time (work sharing) or facilitating temporary layoffs have not been favoured in Sweden. In the early phase of the recession, employment adjustments therefore essentially took the form of external numerical flexibility, in particular a large reduction in the number of agency workers and temporary contracts. The employment decline was also particularly dramatic among low educated and low skilled workers, while employment among employees with a high level of education was only slightly affected (employment even increased among high skilled employees). Youth unemployment, as well as unemployment among non-natives, is more sensitive to fluctuations in the business cycle and the employment prospects of young people and foreign born people have worsened significantly since the end of 2008. In the fourth quarter of 2009, youth unemployment rates reached a maximum of 30 per cent and those for foreign-born people 16.4 per cent (compared to 7.8 per cent for natives). The dramatic increase in youth unemployment might be ascribed to several factors: first, a significant increase in the youth labour supply, in other words, a relatively larger cohort of young people entering the labour market when the recession started; second, the incidence of temporary contracts is high among young people; and third, the Swedish Employment Protection Act, more specifically, the application of the seniority principle (last in, first out) favours workers with long seniority in the redundancy process. While the labour supply of people with an immigrant background was unchanged, the increase
of unemployment among non-natives is also related to their weak attachment in the Swedish labour market (higher incidence of temporary contracts, lower work experience and concentration in the low skilled segment of manufacturing industry and the service sector).

As far as gender is concerned, the relatively stronger impact of the crisis on male unemployment is related to the abovementioned decline of employment in the male-dominated export-oriented manufacturing sector, but compared to the previous crisis (1993), the gender gap in unemployment has remained much lower. There are strong reasons to believe that this is related to the more rapid decline in employment in the public sector at the local and regional levels due to severe budget cuts, despite the additional appropriations to local government by the Swedish government. Regarding older workers, Swedish companies seem to have used early retirement to accommodate the recession much less than in previous economic downturns. The employment rate of senior workers (55–64 years of age) has, to date, remained almost unchanged, while the unemployment rate increased only slightly, from 3.2 per cent in 2008 to 5.2 per cent in 2009.

As far as wage setting and wage developments are concerned, experience from the deep economic crisis of the early 1990s shows that wage moderation characterised wage developments during the second half of the 1990s and early 2000s. There were therefore strong reasons to expect that, in the wake of the current severe economic and financial crisis, wage agreements would also be concluded to preserve employment stability and limit further increases in unemployment. The outcome of the 2009–2011 bargaining round indicates that wage moderation has prevailed in Sweden. The resulting slowdown in the rate of increase in labour costs helped to alleviate the negative effects of the recession on output and employment and partly explain the increase in exports during the recovery.

Looking now at the development of the earnings distribution, the dispersion of disposable income has also increased in Sweden in the long run. Although Sweden belongs to the set of countries with the lowest earnings inequalities, the Gini coefficient increased by 26 per cent between 1991 and 2008, although it fell slightly between 2007 and 2009. During the current recession the reduction in disposable income has been particularly marked at the two ends of the income
distribution. Low and high earners both experienced a significant decline in disposable income between 2007 and 2009. Among high earners, the decline of income might be ascribed principally to the fall in capital income related to the global financial crisis. There are good reasons to believe that the deterioration among low earners might be ascribed to the conjunction of several factors: the increase in unemployment, particularly among low skilled and low paid workers, the dramatic increase in youth unemployment (new entrants into the labour market not covered by the unemployment insurance system), and the abovementioned unemployment insurance reform initiated in 2007. Although the government, as already mentioned, changed the qualification rules in 2009 and introduced a ceiling on individual contributions, there is reason to believe that a significant part of the decline in average disposable income in the first decile was a consequence of this reform.

4. Lessons and prospects three years after the Great Recession

In an international perspective, Sweden seems to have managed to overcome the current economic crisis better than many other Member States. In early 2011, the Swedish economy was in strong recovery with rapid growth (5.7% per cent in 2010), increasing employment and declining unemployment. Part of the recent improvement in the Swedish economy might be ascribed to the strong expansionary fiscal and monetary policies. Compared to previous economic downturns, Swedish economic growth during the past two years has been driven less by increases in exports than by an increase in public and private consumption, due both to increases in disposable household income\(^7\) and the additional appropriations to local government decided on in 2009 and 2010. Due to healthier public finances at the start of the economic downturn the room for manoeuvre for conducting a more expansionary macroeconomic policy was greater than during the previous recession (1993). Overall, the Swedish experience shows that

\(^7\) The increase in disposable income can be ascribed to the cuts in income tax and also the increase in some transfers, such as housing benefit for low earners.
strong public finances are essential for handling the challenges confronting fiscal policy, especially in a deep recession. While Swedish public finances have been somewhat weakened, deficits have also been limited. Against this background and in light of the recent economic recovery the needs of fiscal consolidation and excessive deficit procedure will be limited, implying that the negative impact of restrictive fiscal policy on employment in the public sector will also be limited in Sweden compared to other EU Member States. In contrast to countries with weaker industrial relations systems and unbalanced bargaining power between the two sides of industry, the specificity of the Swedish industrial relations system has also entailed a more balanced sharing of the cost of the crisis (see Anxo 2011). All in all, previous developments tend to show that the change of political majority and the economic reforms undertaken have up to now only marginally modified the core components of the Swedish model. The structural reforms of the tax and benefit systems aimed at strengthening work incentives are still clearly in line with the general philosophy of the original Swedish model favouring the ‘work-first line’ instead of passive support. Even if the volume of participants in ALMP programmes was lower during the current recession overall the policy of activation still plays a major role in Swedish stabilisation policy. Last but not least and despite the above-described decline of union density, the two sides of industry remain the two main actors regarding both labour market regulations and wage setting: the bargaining system remains centralised and coordinated.

Although the reforms undertaken by the current government have only marginally affected the Swedish model and if the government’s macroeconomic policy has helped to absorb and limit the negative impacts of the crisis on employment and income inequalities in the short run, we cannot rule out that the long-term consequences of the crisis might be significant. Despite the abovementioned signs of recovery and a tendency for employment to increase, the overall unemployment rate remains high, at 8 per cent in the first half of 2011, a level much higher than in previous periods (1960–1991), when unemployment rates oscillated between 2 and 3 per cent. The long-term consequences of high youth unemployment and the deterioration of the labour market for people with an immigrant background also remain worrying. As shown by previous empirical evidence (See Nordstöm-Skans 2004) the potential scarring effects of an early period of unemployment may have a long-lasting negative influence on
subsequent employment performance and income development across the life course. Furthermore, an early period of unemployment may affect the timing of other critical transitions and events, such as the transition from school to work and the constitution of an independent household, as well as access to housing, parenthood and fertility patterns, career opportunities and wage development (see Anxo et al. 2010). Some recent empirical evidence (see Anxo 2011) tends also to show that we may not rule out either that the current crisis, like the deep recession of the early 1990s, implies that, in future, a growing share of Swedish companies will rely increasingly on external numerical flexibility, with a rise in the use of short-term contracts and agency workers. If this is the case, this development may worsen the duality in the labour market between insiders and outsiders, alter the conditions of entry into the labour market and delay the acquisition of a permanent and stable job. It is also clear that if Sweden fails to re-establish the conditions for a return to full employment, in particular to reduce unemployment and increase employment rates for some of the abovementioned vulnerable groups, we cannot exclude a progressive decline of the Swedish model, its coherence and the robustness of its social cohesion.

References


