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## ■ Risk of 'golden parenthesis' for the Swedish economy

Deputy Governor Villy Bergström today spoke in Gävle before the Chamber of Commerce of Central Sweden about growth conditions in Sweden.

"The Riksbank recently presented an assessment of inflation and also made a decision regarding interest rates. In this latest Inflation Report it was observed that we are currently in a favourable situation characterised by robust growth and low inflation. It was also noted that wage costs are being held back by low negotiated wage increases and high productivity growth, while import prices are being restrained by the stronger krona. In addition, the Report observed that the international economic recovery has taken firmer root, thus stimulating Swedish exports. But I do not intend to dwell on the present monetary policy situation or on developments in the Swedish economy in the years ahead. My intention instead is to look beyond the time horizon that is relevant to current monetary policy and to adopt a considerably longer-term perspective," began Mr Bergström.

"Naturally, the further into the future we try to look, the greater the uncertainty becomes. The internationalisation of the business sector is likely to continue and to affect output and prices over several decades. As always, however, productivity is difficult to estimate, especially in the long term. The cyclically-adjusted trend in productivity growth has gradually risen since the beginning of the 1990s. As current productivity is neither driven by large-scale investment per hour worked nor, as before, by the telecommunications industry, the most important remaining explanation is technological and organisational changes. It is possible that the extensive IT investment seen in the late 1990s is now bearing fruit in the shape of increased efficiency in the workplace. However, not even technology-driven improvements in productivity last forever. They may raise productivity for a number of years, perhaps a whole decade, but their effects eventually diminish over time," said Mr Bergström.

”The danger with today’s relatively benign situation is that we forget considerable, underlying growth problems in the Swedish economy. In the really long-term perspective, seen over the past three decades, Sweden has still lost ground in terms of GDP per capita. For example, in order to catch up with the United States in terms of GDP per capita over ten years, Sweden would need 2.5 percentage points higher productivity growth than that of the United States (with today’s figures more than 4 per cent productivity growth per year), which is an unattainably high figure. With a more realistic productivity advantage of a half percentage point per year compared with the US, it would take more than half a century to catch up,” said Mr Bergström.

”In the years ahead there are also dark clouds on the horizon. One such cloud is the labour supply. Despite high growth Swedish employment is low, not least due to the high frequency of sick leave. The problems will be aggravated when the population ages and the dependency burden for the economically active population rises sharply. Today, there are 0.29 persons over 65 years of age for every member of the economically active population ; by 2030 this is estimated to have risen to 0.42. If we are to be able to meet this challenge employment must increase, by way of reduced sick leave, perhaps also a higher retirement age and earlier entry to working life. Moreover, we have an unutilised labour reserve in the form of the unemployed and the immigrant population, for whom the employment rate averages 30 per cent lower than for native Swedes,” said Mr Bergström.

”Another source of concern is the weak capital formation in Sweden. The input of real capital per hour worked is crucial for productivity. Investment in new capital also brings with it new technology. At the same time as Sweden lost ground in terms of GDP per capita at the beginning of the 1970s, the proportion of our available resources that was invested in capital formation (net investment as a proportion of net domestic product) fell from around 15 per cent to 5 per cent. Capital formation has never recovered since. This means that the rate of technological renewal in the business sector and the rest of the economy is being held back, as are improvements in the country’s infrastructure. Weak capital formation, and thereby slow technological renewal, dampens long-term productivity growth. By the same token we can see that in industries and during periods where capital formation has been high, productivity growth has also held up. Examples of this are the IT investment at the end of the 1990s and the less publicised strong productivity growth and competitiveness of Swedish basic industries through increased capital intensity,” said Mr Bergström.

”If the foundations are not laid for boosting employment and long-term capital formation the currently favourable period for the Swedish economy risks becoming a ‘golden parenthesis’ between the stagnation of the 1970s and 1980s and the future problems of an ageing population and strained government finances,” concluded Mr Bergström.