

Why higher growth in Sweden than in the eurozone and the United States?

In an international perspective Sweden is experiencing strong growth. The rate of growth is currently higher in Sweden than in the eurozone and the United States, and the Riksbank's forecast is that this will continue next year. This article aims to highlight some of the factors that explain Sweden's relatively high growth now and over the coming period. These factors relate to global trade and Sweden's exports, the high level of household saving in combination with Sweden's strong public finances and the development of the housing market.

Background: GDP development in Sweden, the eurozone and the United States

In the 1970s and 1980s, Sweden's economy grew slowly in relation to the economies of Sweden's largest trading partners. However, in the 10 years preceding the start of the financial crisis, GDP growth in Sweden was higher than in both the eurozone and the United States (see Figure B1). This difference was particularly evident in comparison with the eurozone. This meant that for a considerable period of time growth was significantly higher in Sweden than in its largest trading partners (measured using TCW weights).¹² In connection with the financial crisis, GDP fell more in Sweden than in the eurozone and the United States, but has recovered strongly recently.

At present, the rate of growth is more rapid in Sweden than in the eurozone and the United States. This more rapid rate of growth is also expected to continue in 2011 (see Figure 1:2). This article will not attempt to provide a comprehensive description of the differences between the preconditions for growth in these countries and regions; the aim instead is to highlight a number of central factors. These factors relate to global trade and Sweden's exports, the high level of household saving in combination with Sweden's strong public finances and the development of the housing market.

It should be pointed out that the factors discussed in this article will decline in importance in the longer term, which is also reflected in the more similar rate of growth in Sweden, the eurozone and the United States towards the end of the forecast horizon (see Figure 1:2).

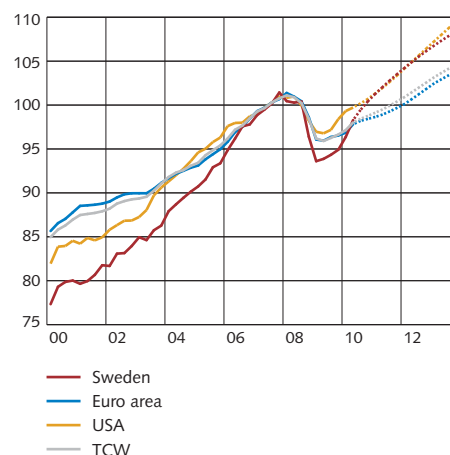
The upturn in global trade will benefit Sweden in the recovery phase

A very dramatic fall in global trade occurred in connection with the financial crisis (see Figure B2). This had a major impact on a small, open economy such as Sweden. Sweden's export market, which reflects imports in those countries that Sweden trades most with, took a heavy fall. This had an immediate impact on Swedish exports, which fell by over 15 per cent (see Figure B2).

The major fall in global trade in connection with the financial crisis also hit exports in the eurozone and the United States; exports in these areas fell by approximately the same amount as in Sweden (see Figure B3).

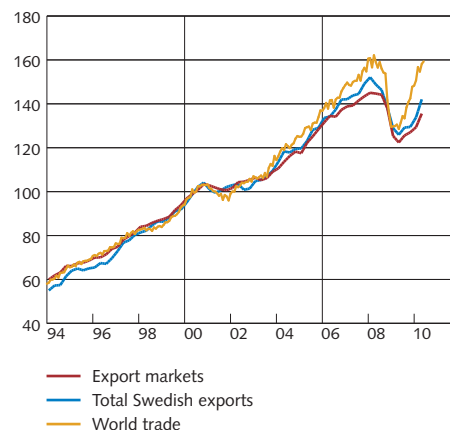
¹² The eurozone's share constitutes over 50 per cent, which explains the similarities between TCW-weighted GDP and the eurozone's GDP

Figure B1. GDP in Sweden and the world
Logarithmised index, 2007 = 100



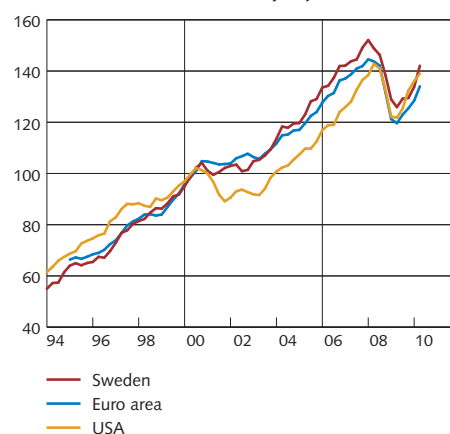
Note. Broken lines represent the Riksbank's forecast.
Sources: Bureau of Economic Analysis, Eurostat and the Riksbank

Figure B2. Volume of world trade, export markets and Swedish exports
Index 2000 = 100, seasonally adjusted data



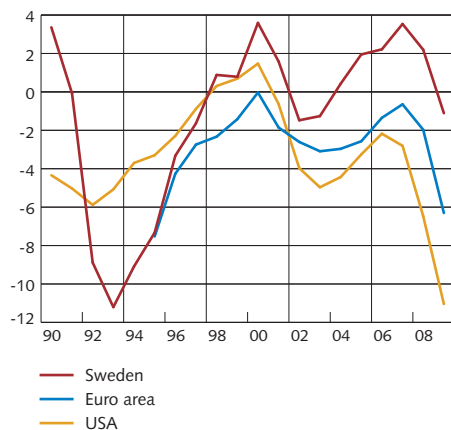
Sources: Netherlands Bureau of Economic Analysis, Statistics Sweden and the Riksbank

Figure B3. Export volumes in Sweden, the euro area and the USA
Index 2000 = 100, seasonally adjusted data



Sources: Bureau of Economic Analysis, Eurostat and Statistics Sweden

Figure B4. General government net lending in Sweden, the euro area and the USA
Percentage of GDP



Source: OECD

However, the higher export share meant that a small, open economy like Sweden was hit particularly hard.

In addition, a significant part of the fall in global trade consisted of reduced trading in investment goods and non-durables such as cars. It was easy to postpone the purchase of these goods when the financial crisis began.¹³ Such goods represent a large share of Sweden's exports. One could therefore say that Sweden suffered an extra adverse effect during the crisis due to the mix of goods in its exports.

Similarly, the strong upturn in global trade is now benefiting Sweden more than many other countries due to its high export share. Furthermore, the composition of Sweden's exports is no longer a disadvantage but rather an advantage. The current upturn in global trade is largely driven by the demand for exactly the types of products for which demand fell most during the crisis. As it was easy to postpone the purchase of these products it is also easy to take up these purchases again. However, Swedish exports have not grown at the same rate as global trade as it is mostly the emerging economies in Asia that account for the greatest increase in imports and the predominant regions for Sweden's export market are still Europe and the United States.

All-in-all, the development of global trade and the export markets has led to a strong recovery in Swedish exports and it is expected that growth will be particularly strong this year and next year. To some extent, the recovery of Swedish exports has also benefited from the tangible weakening of the Swedish krona in connection with the crisis (see Figure 1:17).

The significance of exports for Sweden's higher growth in relation to the United States and the eurozone is most relevant in explaining the differences in GDP recently and in the short-term forecast. The krona has strengthened significantly over the last 12 months and is now back to the levels that prevailed before the financial crisis. The Riksbank's assessment is that the krona will continue to strengthen. In the long term, the assessment is therefore that exports will increase in line with or somewhat more slowly than Sweden's export market (see Figure 1:19).

Very strong public finances in Sweden...

In contrast to the situation in the eurozone and the United States, there was a significant surplus in public finances in Sweden when the financial crisis began. In both the eurozone and the United States, public finances were in deficit by an average of 2 per cent of GDP during the 10 years leading up to the crisis. The corresponding figure for Sweden was a surplus of over 1 per cent; in line with the so-called surplus target.¹⁴ In other words, the initial position for public finances differed considerably.

¹³ For this reason these goods are sometimes referred to as "postponables".

¹⁴ The surplus target is that the public sector financial balance should be on average plus one per cent over an economic cycle.

Despite the severe downturn, the public sector financial balance fell to only -1 per cent of GDP in Sweden in 2009, which is a much smaller fall than in the eurozone and the United States (see Figure B4). The substantial deterioration in the public sector financial balance in the eurozone and the United States was the result of automatic stabilisers linked to the downturn and of extensive fiscal policy stimulation measures.

At the end of the 1990s, central government debt in the eurozone was at approximately the same level as in Sweden. After this, partly as a result of the surplus target for public finances, there was a trend decrease of the debt in Sweden that was not matched by a similar decrease in the eurozone or in the United States. When the crisis broke out, the level of central government debt began to increase dramatically in both the eurozone and the United States (see Figure B5).

It should be pointed out that, in turn, there are major differences between the countries in the eurozone with regard to the state of public finances. It was above all in countries such as Greece, Ireland, Italy, Portugal and Spain that major sovereign-debt problems arose during the crisis. During 2010, there was a lot of concern about how these countries would deal with their fiscal policy problems, which among other things has resulted in substantial increases in government bond rates (see Figure 3:13). These high bond rates are adding to the problems relating to sovereign debt in that they entail increased interest expenditure.

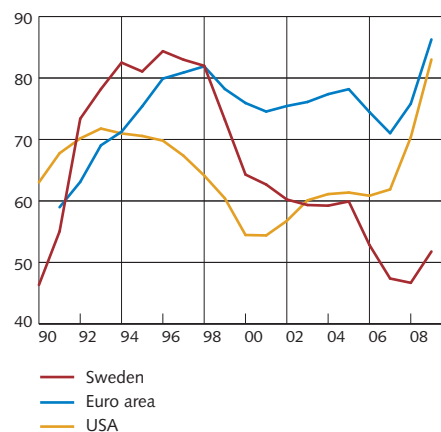
All-in-all, the factors mentioned above mean that the need for fiscal policy restraint is much more limited in Sweden than in the eurozone and the United States. The Riksbank, like the Ministry of Finance and the National Institute of Economic Research, sees no need for fiscal policy restraint in Sweden in the years immediately ahead.

...in combination with a high level of household saving

One of the strengths of the Swedish economy compared to the eurozone and the United States is the combination of a high level of household saving and strong public finances. In Sweden, there has been a strong trend increase in saving over the last 10 years, which is in contrast with the situation in many other countries. This has not been the case in Germany, for example, a country where household saving has traditionally been high but which today has a saving ratio in the same range as Sweden. In Germany, total private consumption has not increased at all over the last 10 years, which together with moderate increases in disposable incomes has led to a marginally increasing saving ratio (see Figure B6). Household saving in the United States declined more or less continuously over the 15 years leading up to the financial crisis, when it began to increase. In the countries in the eurozone where public finances have weakened most, such as Spain and Ireland, there has been a dramatic increase in household saving in a short time (see Figure B6).

An important question in this context is: What is a high level of household saving really due to? The Riksbank's assessment is that a large part of the increase in saving in Sweden in connection with the financial

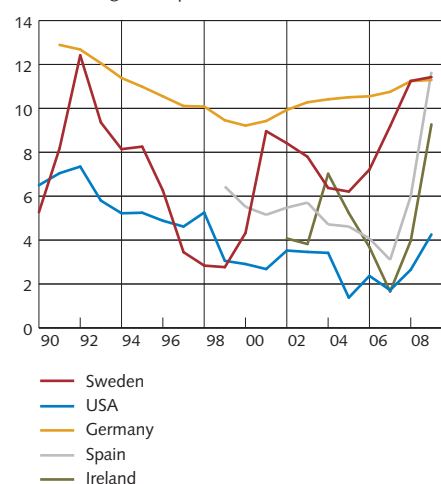
Figure B5. Development of central government debt in Sweden, the euro area and the USA
Percentage of GDP



Note. Public gross debt.

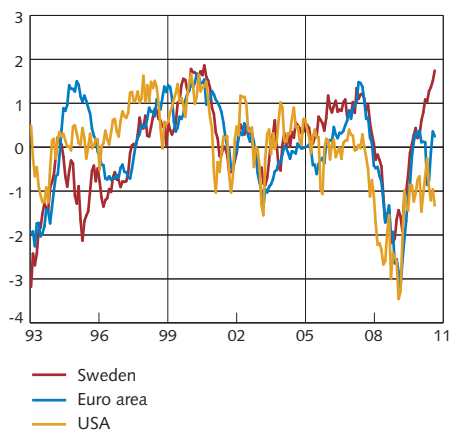
Source: OECD

Figure B6. Households' saving ratio in various countries
Percentage of disposable income



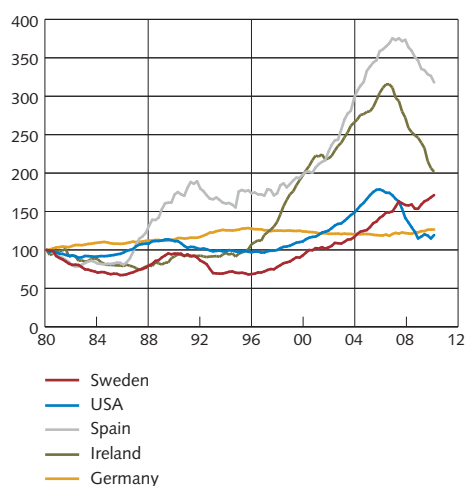
Sources: National statistical authorities and the OECD

Figure B7. Consumer confidence in Sweden, the euro area and the USA
Number of standard deviations from mean value



Sources: The Conference Board, DG ECFIN and National Institute of Economic Research

Figure B8. Real house prices in various countries
Index, 1980 = 100



Sources: BIS, Reuters EcoWin and the Riksbank

crisis is so-called precautionary saving. Greater uncertainty about future incomes has led the households to increase their saving. Over the last 12 months, there has been a significant increase in consumer confidence in Sweden, even in comparison with the eurozone and the United States, which is a sign that uncertainty is declining among the households (see Figure B7). The major deficits in public finances in many countries are generating further uncertainty about future incomes, which will probably push up precautionary saving among the households in these countries. In this respect, Sweden differs from, for example, the eurozone and the United States. This is an additional factor that indicates that the preconditions for a reduction in saving appear to be better in Sweden than in the eurozone and the United States.

It is thus the combination of sound central government finances and a high level of household saving that represents a strength of the Swedish economy in an international comparison. Relatively high increases in disposable incomes in combination with goods scope to reduce saving enable a high rate of growth in private consumption. The preconditions for this are weaker in the eurozone and the United States, which means that private consumption has the potential to grow more rapidly in Sweden than in these regions this year and next year.

Developments on the housing market – a low level of housing construction in Sweden means that major price falls are unlikely

House prices in Sweden have recovered following a slight downturn in connection with the financial crisis and are now at a higher level than before the crisis began. In this respect the situation in Sweden differs radically from that in the United States and some countries in the eurozone, such as Spain and Ireland (see Figure B8). This is also reflected in the figures for housing investment, which increased substantially before the crisis but then fell back in these countries (see Figure B9). Following the dramatic fall in the early 1990s, housing investment recovered slowly in Sweden but declined somewhat in connection with the financial crisis. Recently, however, investment has increased once again.

Major structural problems have arisen in the economies of those countries hit by a "boom-bust" cycle on the housing market, such as Spain, Ireland and the United States, and this has been reflected in a substantial weakening of public finances. Although countries such as Germany have not experienced this development of the housing market, it has still had an impact on the development of the eurozone as a whole.

In the United States, there are still very clear traces of the weak development of the housing market. Housing investment has fallen substantially, which has led to structural problems, for example when there is a need to move production factors in the form of capital and labour from the housing sector. This has probably restricted the development of the labour market, which has been surprisingly weak given the development of GDP.

The relatively stable development of the housing market in Sweden is thus one of the reasons why it has been possible to avoid structural problems in the Swedish economy. The "boom-bust" cycles that have been observed in other parts of the world have been characterised by an increased demand for housing that has been met by a dramatic increase in housing investment. The subsequent decline in demand has led to a surplus of housing and substantial falls in housing prices. A substantial increase in housing investment to high levels could therefore pose a risk to the Swedish economy. In international and historical terms, however, housing investment is at a low level in Sweden.

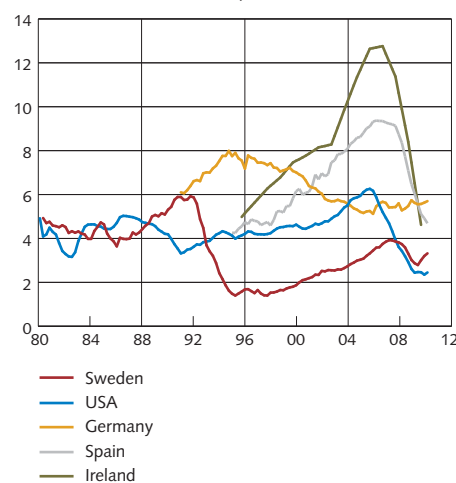
All-in-all, the fact that Sweden has not been hit by a declining housing market, and the accompanying structural problems, means that the situation looks much more stable than in many other countries in the eurozone and in the United States. This is an additional factor that indicates that economic growth will be higher in Sweden over the next few years than in the eurozone and the United States.

Summary

The forecast in this Monetary Policy Report is that GDP growth will be higher in Sweden this year and next year than in the eurozone and the United States. This article has aimed to highlight some of the explanatory factors that. These factors relate to global trade and Sweden's exports, the high level of household saving in combination with Sweden's strong public finances and the development of the housing market. There are, however, other factors that may be highlighted. One such factor is the stability of the Swedish banking sector. In contrast to the situation in the eurozone and the United States, the Swedish banks have been able to avoid major loan losses, which makes it easier for the banks to lend to households and companies, and therefore facilitates the recovery from the crisis.

In the longer term, the assessment is that the US housing market will improve and that public finances in the eurozone will stabilise. It is also expected that differences in the growth of consumption in Sweden on the one hand and the eurozone and the United States on the other will even out. Sweden's exports will grow in line with, or somewhat more slowly than, the export market. It is therefore primarily in the short term that GDP growth in Sweden is higher than that in euro area and the United States (see Tables A4 and A5).

Figure B9. Housing investments
Per cent of GDP, current prices



Sources: National statistical authorities and the Riksbank