



**SVERIGES
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TAX REFORM NECESSARY AND POSITIVE FOR THE SWEDISH ECONOMY

The tax reform was necessary for the Swedish economy and its effect has been positive, in the opinion of the Riksbank in its submission on the report from KUSK, the government committee set up to evaluate the tax reform. The Riksbank considers that the reform's benefits more than offset any occasional costs in a transitional period.

The Riksbank emphasizes that the tax reform's main principles must be safeguarded in order for the reform to yield its expected and intended positive effects in full. A sustainable and robust tax system provides a good planning environment and contributes to stable economic development.

When the reform was implemented the Swedish economy had long-standing structural problems of a serious nature, e.g. a lack of financial saving that had been manifested in persistent deficits on the current account. The tax system stimulated loan-financed consumption and contributed to overheating in the real estate market. The tax reform was therefore needed for a long-term improvement in the Swedish economy.

Economic effects of the tax reform not fully elucidated

The distributional effects of the tax reform should, in the Riksbank's opinion, be seen in a wider context than the evaluation has used. The standard chosen for comparison is namely the unstable situation that prevailed prior to the reform, with extensive structural imbalances and high inflation. The Riksbank considers that sooner or later, equilibrium mechanisms in the economy would have brought about corrections in these respects. The evaluation should therefore have chosen a more stable situation as its starting point, or at least discussed the consequences of using an unstable situation for comparisons.

The Riksbank also considers that desirable distributional effects must be weighed against impairments which they may entail in economic efficiency. A lack of efficiency leads to lower

growth, with the result that in the long run there is less to distribute. In that the tax reform has helped to enhance economic efficiency, in the Riksbank's opinion the reform should provide better conditions for future distribution policy.

Two of the conclusions from the evaluation are that the tax reform was under-financed by about SEK 35 billion and that it accounted for about 1 percentage point of GDP's fall at the beginning of the 1990s. The Riksbank finds that these conclusions are drawn from an approach that is unduly narrow.

In this respect the Riksbank underscores that government finance has had an underlying imbalance which is fundamentally ascribable to the high spending ratio. High expenditure creates a need of high taxes, which impair economic efficiency via tax wedges. Government finance also became highly sensitive to cyclical fluctuations, so that economic downturns resulted in large budget deficits. The Riksbank considers that in this context the tax reform, by reducing tax wedges, could help to mitigate the problem. As regards the under-financing of the reform, consideration should be paid to the underlying imbalance in government finance, which stemmed from the high spending ratio and the economy's prevailing structural problems.

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