

Midterm Exam:

The Swedish Model – A Great Success or a Failed Experiment?

1. Introduction

“Support for [...] high-quality public services and high taxes seems part of the Nordic identity. The region’s people expect free schooling and university education, high-quality health care, generous unemployment and sickness benefits, state-funded maternity and paternity leave, universal pensions and more.” (Economist p. 10)

Sweden is told to be the most generous welfare state in the world. More than half of its GDP consists of tax revenues – compared to about 30 percent in the US. Through “solidaristic wage policy” and redistribution the Swedish national wealth is more equally shared than anywhere else in the world. But what for? Is Sweden the perfect society where everybody cares for each other? Or is it just an unaffordable bubble that will explode soon? Don’t the Swedes need higher wage differences to create an incentive to be more competitive? That might sound provoking to the average Swede – but won’t it be necessary to sustain in a globalized economic system?

In this home exam I will try to weigh the pros and contras of the Swedish Model. Since I’m not that familiar with the liberal welfare state version of the United States I’ll mainly use effects resulting from the Swedish Model as contra-arguments against itself. Additionally I’ll try to judge the Swedish system through a German viewpoint, which is in Esping-Andersen’s terms a conservative welfare state.

2. Short History of the Swedish Model

“Equality has always been the central goal” (Esping-Andersen, p. 38) of the Swedish Social Democrats. It does already have a centenary tradition: They where not into the Marxian “class-struggle” and didn’t want to have a revolution but understood themselves as a “people’s party” especially for the “little people” as early as 1895. The 1928 introduced folkhem model (“people’s home”) showed where the long travel should go to: The whole State should be and act like a family: solidarity should be

natural and a day-to-day business. Even in terms of politics it favored grand coalitions – the other parties were not seen as “enemies” like in most of the other countries. Furthermore the folkhem especially meant Keynesianism (an anti-cyclical policy where you save budget surpluses in the good years and increase demand with that money in the bad years), agricultural subsidies and a social reform that included universal pensions, universal unified health insurance, and unemployment insurance. Its architect Gustav Möller focused on a symbiosis of equality and efficiency. Thus full employment and progressive taxation were other main targets. Still the system only provided a basic minimum of income security and many social rights were subject to needs testing. As Esping-Andersen (p. 47) puts it, “its real focus was to redress poverty”. So the Swedish Model had a lot of liberal welfare elements in the first run. It didn’t appeal the middle class. This finally changed in the 1950s: The middle class was being solidarized and thereby weakened the bourgeois opposition parties. The famous Rehn-Meidner-Model of solidaristic wage policy came up which should “eliminate unproductive jobs and, via retraining and mobility, shift workers to dynamic sectors” (Esping-Andersen, p. 51) came up. So instead of a basic equalization on a low level it should now be done on the top. The greatest expansion of the welfare state happened in the 1960s and 1970s: The “Million Program” urbanized Sweden when one Million housing units were built. There was generally more attention to the quantity and quality of social service delivery. Health, education and social services exploded (see Esping-Andersen, p. 60). But due to its enormous expansion and the solidaristic wage policy the welfare state got more and more expensive and caused serious economic trouble. So after some devaluations finally hard cuts were made into the system in the 1990s.

3. Arguments in favor of the Swedish Welfare State

A high living standard for everyone from “cradle-to-grave” is a great goal – and Sweden somehow achieved it during the years. Today Sweden is not only ahead in relatively even household income distribution. It also plays a leading role in gender mainstreaming and integration of immigrants. Fair play: Universal systems like daycare, education, health care and pensions take care that everybody has the same chances – not depending on social background, ethnicity, gender or whatever. Unlike in the US or in Germany it is quite frequent that kids with lower educated parents will go to university, have a great education and later on find themselves in high-skilled jobs. So social ascent

is a daily business in Sweden. This does not only favor the people itself: Since everybody should be treated equal and should have the same opportunities there is not much greed or jealousy around. Furthermore it also effects the economy positively: “Free” education even on university level and expenditure in health care shouldn’t be seen as burdens upon production, “but as investments in human capital. Society’s greatest asset is its human resources” (Tilton, p. 413). And thereby the main resource of every enterprise and any innovation. Especially for a nation which cannot just rely on raw materials like oil, gold mines or whatever this is its greatest aid. Therefore Sweden does not have any tuition fee at all at university. Contrary every Swedish student gets financial support to study. You receive about 2000 Kronor per month as a donation plus an optional loan of 5500 Kronor, e.g. to pay your rent, food or books. Surely that wouldn’t be possible in the US. And in the German welfare state this is one of the best ways to show why Esping-Andersen calls it conservative: First the family is responsible to give its children the financial aid to study. Only if they don’t earn enough then you can receive support from the state. So this way different to the universal Swedish approach which encourages everybody to study.

The “Nanny State” also increases security and freedom for common people: “Health insurance freed them from the high costs of medical care and their attendant anxieties; pensions from the risk of an impoverished old age; housing policy from the squalor and potential for illness found in slum condition; full employment policy, from the risk of unemployment”, quotes Tilton (p. 419) Tage Erlander. The full employment strategy of the Swedish Model is quite exemplary: It does not only satisfy the people and thereby minimize social struggle. It also “generates tax revenues rather than requiring their expenditure” (Tilton p. 423) or, in other words, “as unemployment rises, more people draw on the social welfare system and fewer contribute to it” (Stephens, p. 33). In that way it should help to have a healthy economy so that the result would be “competitive advantages” (Stephens, p. 33).

The cradle-to-grave idea helps women getting into the workforce: Parental leave in the first year and afterwards full daycare encourage women to work. On the one hand this is a great deal for the woman’s social standing since she is independent from male support. Otherwise there’d usually be unequal power within the family. On the other hand the daycare is a great tool for the whole economy: A high percentage of working women means that there are more people who contribute to the social security system and tax system. As pointed out in the “OECD manifesto to raise employment” (see

Economist 09-20-03) raising employment e.g. by getting women out of home into a job is really important to increase the number of people contributing to the public pension schemes. Even the daycare as itself works as a “job machine”: Since the women don’t have to raise their children at home anymore but take them to dagis, a huge number of jobs are created in this branch. So a lot of women work in the daycare business and thereby might even earn money for raising their own children within dagis and the children of others as well. So the dagis story is a great tool to raise national wealth: First it gets more attractive to get children since they won’t be a great financial burden. Boosting the fertility rate is necessary to fight the ageing of the population that would otherwise mean that social services/benefits became unaffordable. On the other hand more children mean more human capital that is important to stay innovative and competitive even on the global scale. Secondly it works like an upward spiral which increases the GDP by paying the job that would otherwise be done unpaid at home: Raising children. “One of the reasons for this extraordinary female bias is that services for women become jobs for women”, states Esping-Andersen (p. 61). And if almost everybody works fulltime this might create even more service jobs: People might tend to hire other people as “helping hands” for your own household.

Active labor market policy is another important tool not just to get the people away from unemployment but also to support the national wealth and the welfare system. Even if it just means to create a lot of “dig-a-ditch-jobs” it helps to increase private consumption. And once you have more consumption at least the theory says that this will create “real jobs” once again. This is a story which Germany right now starts to try with its so-called “Hartz IV-Reform”: At least a part of the four million unemployed people will be forced to take low-skilled-jobs like cleaning parks, helping old people or working in museums. They just earn one up to two Euros (nine up to 18 Kronor) per hour. But this is added to the unemployment benefits they already receive. So they’ll have a monthly extra of about 200 Euros (1800 Kronor) to spend. Surely this is not a big amount but that’s not the only idea of the active labor market policy: It shall especially help long-term unemployed people to find a new regular job since they can hereby prove to possible employers that they are still willing to work. Also active manpower policy means to move people to “good jobs” by retraining them and thereby supporting not only the people but also the domestic companies.

And finally another great thing about the redistributive state: You won’t find many poor people living here. There is no age-poverty at all in Sweden; at least there was none in

the 1980s (Esping-Andersen p. 51). This is due to the great pension scheme that guarantees that no retiree gets less than 50 percent of the median income.

4. Arguments against the Swedish Welfare State

The Swedish Model seems not to be affordable anymore. It's the little things that indicate it. Just go to a dentist and then you'll see that the State can't act like a nanny even in important fields anymore. Today people have to spend their 450 Kronor just to be examined. And serious treatments cost thousands of Crowns in these days. So the high taxes and insurances in Sweden don't cover to become healthy – is it just a bad Nanny nowadays? To a German that looks quite strange –dental examinations are fully covered by the mandatory insurance to prevent serious health problems. But after a long struggle my home country finally introduced a treatment fee – but it is just 10 Euro and thereby a fifth of the Swedish basic fee. So if you focus on Germany seems to be the better Nanny on this issue right now.

But why did it come that far? Some arguments against the Swedish Model are following: First I want to point out the Rehn-Meidner-Model of solidaristic wage policy. This policy (developed by trade union economists) might have sounded like a nice idea to push Sweden's economy further and further: Through "equal pay for equal work" within one branch the efficient companies should gain "excess profits" and use them to expand by hiring more employees. At the same time the inefficient companies would either be forced to get more productive or they'd die. So this model can create huge problems: It clearly favors big companies while it doesn't bear the entrepreneur in mind. What about small business startups that can't pay the full wage level but have to? This might not attract a lot of investors cause there are no incentives to start a company at all! Entrepreneurs would be attracted if the market barriers where not that high: Flexible wage schemes (see Stephens, p. 58) would be one step to support startups. Another incentive would be indirect subsidies like lowering the owner taxation or even direct subsidies.

While the original idea of the model was to enforce competition the contrary might occur not only in terms of startups: If the solidaristic wage level is set to high it will drive out a lot of inefficient companies who will close down. So high wages can favor oligopoly or even monopoly. What happens then? These companies might get lazy and raise prices due to the lack of competition at their front door. Even if the model does

have global competition in mind: The idea that the big companies would get bigger and bigger and create more and more jobs was maybe up-to-date in the 1950s. But due to mobile capital, floating exchange rates, shrinking/fading tariffs et cetera Rehn-Meidner is outdated: Gaining size for a company does not mean to hire people anymore but to lay them off – today you earn more money by enhancing computers and robots or to move production capacities to countries with lower wages and lower taxation, e.g. to Eastern Europe, Asia or South America. So the shareholders might profit from this expansion but not certainly the Swedish employees – it sometimes seems that Swedish Politics has lost contact to the real world.

Hugely connected to the Rehn-Meidner-Model might be the decrease in private sector employment vs. the increase in the public sector. It's hardly understandable that a national economy is healthy when the jobs in the private sector fall by 20 percent while they are tripled in the public sector within 35 years (between 1960 and 1995, see Lindbeck, p. 1279). A third of the employees were working either in public service or administration in 1995. Even compared to Germany, which is famous for its huge public administration, it is an astounding ratio: 5.9 million out of the 38.6 million working people are employed in public administration/services (statistics for 2002, see www.destatis.de). This means that there has to be some correlation between the shrinking market-financed employees and the rising public-financed workers: My speculation is that the solidaristic wage levels were set way too high. So the Rehn-Meidner-model might have not worked as well as it should. Thus a lot of inefficient companies could gain more efficiency but died during the years. Esping-Andersen (p. 55) notices that it came to wildcat strikes in the 1960s motivated by plant closures. So the growing companies on the top couldn't hire all of the laid-off people. Hundreds of thousands of jobs in the public sector were created to fight unemployment since high unemployment rates would have meant less tax revenues and thereby would have caused a lot of trouble to the mechanisms of the Welfare State. "Upgrading of welfare state services came to serve as the principal employment policy from the late 1960s onward", writes Esping-Andersen (p. 60). Although he connects this development mainly to the improvement of the women's position in society and greater attention to social service delivery and doesn't want to ascribe it to the lack of alternative economic growth due to male full employment it supports Lindbeck's numbers if you read further on: "Given the sluggish state of the Swedish economy throughout the 1970s, this would

clearly would have been difficult to attain otherwise. The welfare state has, In effect, provided the only significant source of job growth over a long era“ (p. 61).

Even more amazing than the relation between tax- and market paid employees is the comparison between all tax-financed and market-financed individuals in Sweden: It's 4.1 million tax-financed people compared to 2.2 million market-financed people (Ratio 1.83). Surely this is only affordable through incredible high taxation. Unfortunately I couldn't retrieve exact comparative numbers for this issue. But the ratio in Germany is distinctively lower and should be a little below 1.0 (own calculation based on total population, juvenile population, senior citizens and employment rates).

The wage explosions caused by the Rehn-Meidner-Model surely caused economic trouble: “The 1975 wage increases seemed to price Sweden out of international competition” (Esping-Andersen, p. 57). Inflation rose seriously and forced Sweden to a lot of currency devaluations to get more competitive with its exports, so to say the engine of its economy. But this also meant that the real wages fell as well. So Sweden was driven into a cycle: Since the unions anticipated the next devaluations and knew that the real wages already had went down they pushed high wage increases through every year. But since the economy wasn't that healthy anymore the national bank carried on its devaluation policy from the 1970s to the 1990s where the Krona finally dropped by 30 percent. Today this policy fortunately doesn't work any more since the Krona is in a free float against the US-Dollar. High wages and inflation also lead to high interest rates, in the early 1990s even up to 200 percent! This discouraged investments and thereby weakened the economy – another downward cycle was created. To the top of all this unemployment still rose and the public debts rose as well: In 1993 there was a public deficit of 12 percent! Fortunately the economy cured after the final devaluation in 1993 so the situation isn't that bad anymore, the unemployment rate fell again and thereby the replacement transfers the state had to pay before.

Additionally taxation has to be pointed out. On the one hand it is said that Swedes like to pay high taxes since they get a high payback through public services and universal benefits. Some days ago a discussion came up to get “free” (that means tax paid) public transportation instead of buying your subway-ticket since already half of it is covered by subsidies. This shows why Sweden is sometimes nick-named “The Nanny-State”: The people give a lot of money to the state by paying taxes and the state shall in exchange care for almost everything. As Tilton (p. 419) puts it, the democratic Swedish state acts on behalf of its citizens' interests, so taxes do not abuse citizen's freedom but

are simply a way of paying a price for the public services the people want. Nevertheless on the public transport issue a poll finally showed that there should still be a fee instead of a full tax-covered service since not everybody needs to use the public transportation. So maybe Sweden isn't solidaristic in any issue anymore? The high taxation teases the people already to act contradictory: Black-market labor is rising up, e.g. in construction work, childcare and even in franchise businesses. Did you ever wonder why so many people whisper "Taxi" in your ear while you are walking through Stockholm or Gothenburg by night? It's illicit work. A lot of Swedes move their money offshore to avoid taxation (see Economist, p. 12) or even leave the country. A famous example is IKEA: The headquarters and its founder/owner have moved to Switzerland. The national alcohol policy is also not supported that broadly: Since there is a 200 percent liquor tax and no competitive market at all through the state alcohol monopoly "Systembolaget", Swedes tend to buy their beer, wine and spirits abroad and thereby avoid domestic taxation: One in three bottles of beer is already being bought abroad (see Economist, p. 13). But this also means that it might influence the services you want to receive from the State.

Finally, one of the main arguments against the Swedish Model is surely a libertarian one: Do we need this massive redistribution at all? Should not just anybody care for himself? Wouldn't that be the best incentive to work hard and thereby get a strong economy?

5. Conclusion

In my opinion the Swedish Model is a great approach towards a good society without greed and jealousy but with lots of happy people all over the place. The Swedes have broadly understood that you won't have to be a millionaire to feel comfortable – they just have a good Nanny that cares for many things. So the largest GDP in the world is not the ultimate goal to achieve for them – it's only the guys at the Timbro think-tank who want that. The relatively even distribution is quite important to have satisfied people. The interesting thing in the Swedish case is that almost every party seems to agree with it – Sweden therefore is often called a social-democratic hegemony. So why should politics act against the majority if almost everybody likes the Nanny-State? Critics often use the freedom of choice as their main argument against the Nanny-State. But it was a voluntary decision of the Swedish people to get such a welfare state!

Still some doubts about the Swedish Model remain – even if its idea is great it might have been expanded to far. In their idealism Swedish politicians sometimes seem to oversleep serious problems: E.g. they stuck to long to the Rehn-Meidner-Model and didn't realize that it not just have positive effects but can drive out more companies and employees than it should. So if you compare the rising numbers of tax- and market-financed employees/individuals you'll soon find an explanation why Sweden has huge taxation: The people have to pay for the Rehn-Meidner-Model and other policies. Once again looking at the provocative Timbro-report EU vs. USA it shows that the Swedish tax burden rose by 12 percentage units between 1970 and 1999. In 1999, it was at 52 percent of the GDP. The 20-years-lasting devaluation-strategy and the rising public debt until the mid of the 1990s were other convincing indicators that something went seriously wrong. So finally reforms were initiated to get the system more sustainable by downsizing its generosity.

Today the Swedish Model seems to be cured at least a bit since some punitive elements for unemployed people and some fees in the health care system were introduced. Still the reforms have to move onward constantly, but for a student it's surely hard to say what exactly has to be done. My main idea would be getting a more effective administration and creating more incentives for business startups e.g. by lowering taxes because you already see what happens with the super-size-strategy of Rehn-Meidner: After serious trouble the car industries today belongs to American companies. Ericsson had to lay-off many people and today has a joint venture together with the Japanese company Sony. Nevertheless Sweden is surely ahead of reshaping its welfare system compared to my home country Germany. Through its cradle-to-grave idea it's still more attractive to get children than it is in Germany or in the US were the kids remain a harder financial burden: Free dagis, free school lunch and free university education combined with financial aid for students are really important tools to let the economy roar. But a high fertility rate is one of the main tools to stay sustainable and affordable: You'll always need more people contributing to the pension schemes and the state budget than people receiving replacements. So hopefully the new "Baby Boom", proclaimed by the free newspaper "Stockholm City" last week, is for real.