

# **Carnegie Council\DRT International Privatization Project**

**From “Confusion  
Economics” to a  
Market Economy:  
The Only Way for  
Sweden**



**Minister Per Westerberg**  
Minister of Industry and Commerce,  
Sweden



**No. 9**

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# From “Confusion Economics” to a Market Economy: The Only Way for Sweden

April 6, 1992

Minister Per Westerberg

**I**n the seventeenth century Sweden was one of the superpowers of Europe; in the last two centuries it has been fortunate to stay out of wars and thus has been able to build an industrial and welfare nation among the most advanced in the world. But this nation is now under severe attack from financial and economic realities. The problems are not only the recession, but are more profound structural ones in the whole of the economy. Almost exactly twenty years ago, Sweden’s standard of living was about 10 percent above the OECD average, but now we have fallen rapidly behind. Since the beginning of the 1970s Swedish wage-earners have had almost no increase in purchasing power, if one takes into account inflation and taxes. Also, there have never been so many people out of work in Sweden since the 1930s.

Between 1970 and 1990 the public sector absorbed a large majority of the labor force, and this was also used to artificially reduce the level of unemployment. This structure, with a dominant and monopolized public sector, created a steadily increasing demand for higher taxes, which finally led to the collapse of “the third way”—the name the Social Democrats had given their policy and a part of the so-called Swedish model.

In recent years, the proportion of Swedish direct investment abroad and foreign investment in Sweden has been running at 10 to 1. The reason is not only that Swedish companies have invested too much abroad, but that foreign enterprises and investors did not find it attractive enough to invest in Sweden. We have reached the stage where radical changes must be implemented. A primary objective of the new government is to revitalize Sweden as a growth-oriented country with a positive climate for doing business.

Each individual measure introduced by the present government will be justified on the basis of increased economic growth and greater productivity. We have already taken an important step in this direction in our first budget. Our proposals for savings in state expenditure exceed what many believed was politically possible. For

the calendar year as a whole, the impact on public saving will be 27 billion Swedish kroner, which amounts to \$5 billion. This is, in effect, the largest cut in public sector costs by a Swedish government in modern times. The savings achieved are of the type that stimulate productivity and increase growth. The measures include an increase of personal risk but also a high cost protection in the welfare system. What is good for the individual should also be good for companies and society as a whole.

The recession, the free market in the EC, the structural changes in Sweden, and the breakdown of the socialist regimes in Central and Eastern Europe are major challenges

that give opportunities to form Northern Europe into the fastest growing economic region of the world. There are three areas on which we have begun and will continue to focus our efforts within the Ministry of Industry and Commerce:

1. We will create more favorable conditions for small and medium-sized growth companies.

2. We will deregulate and increase the potential for effective competition throughout the economy and especially the public monopolies.

3. We will launch one of the most extensive programs for the privatization of state-owned companies.

Uneven corporate structure is one of Sweden’s most serious long-term problems; the structure of the industrial and business sector in Sweden resembles an hour-glass—wide on either end but narrow in the middle. In other words, we have a certain number of small companies and a certain number of large companies, but in between there is very little. Many industrial countries have provided special favorable treatment for small companies, but the opposite has been the case in Sweden. We are now changing this completely.

In Sweden we had one of the harshest taxations on capital invested in companies but almost nothing on farms and real estate. This has now been changed, and we have also started to reform labor market legislation. In Sweden

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such legislation is based on the demands and needs of the major central organizations in the labor market, but now new labor markets must shift the focus to small workplaces and the solutions they require. In addition, during the autumn we will submit proposals for special setting-up loans for new enterprises. I believe that this will strengthen the development potential of smaller companies. Increasing competition throughout the economy is the second main task of our efforts to improve the climate

for enterprise and investment in competition legislation. I regard competition legislation as being one of the elements of an economy that offers pluralism, efficiency and the ability to change. The new legislation will be built on the principles underlying EC competition rules. It will permit an increase in competition. This especially also applies to the public sector production of welfare services. The Swedish welfare system was built by public monopolies. New monopolies have to be effective when they are created, but tend to grow fat over the years. This is one explanation of our tax pressure. Municipalities and other public authorities will now simply be compelled to look for the very best offer for the procurement of any services they are expected to provide.

The program for the privatization of state-owned holdings is in 35 groups. The privatization program is a long-term one and stretches over several electoral periods and business cycles. It varies from big public utilities and ordinary competitive companies to, for example, the state dog training school. We will start with the steel company, SSAB, as the first privatization sale during this spring. SSAB is one of the most competitive and well structured steel companies in Europe, and is listed on the Stockholm stock exchange. We will subsequently continue our privatization program with the objective of attaining a sales

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volume of approximately \$1.5 billion annually. One approach which we will use in the sale of SSAB is to offer the public the opportunity to acquire state bonds with detachable options; offering the opportunity to buy shares at a later time. The fact that the process must be professional from a business point of view, and that the industrial solutions and timing are crucial, means that the preparatory work and method of sale are central aspects of our efforts.

**"Our proposals for savings in state expenditure exceed what many believed was politically possible. For the calendar year as a whole, the impact on public saving will be \$5 billion. This is the largest cut in public sector costs by a Swedish government in modern times ."**

Of utmost importance is our overall objective: to privatize and reduce the political interference in business and industry.

There are four primary reasons underlying this privatization program.

First, it involves a streamlining of the state's role in society and in relation to business and industry. No organization other than the state can establish, maintain and monitor the basic legislation that defines the market framework. Problems arise, however, when the state also operates as an actor on the market through the ownership of companies; this creates a major risk of an overlap in these roles. There are good examples of that in the Volvo-Procordia case and the Scandinavian Airlines (SAS).

The second reason is to spread ownership throughout society. A healthy market economy requires a spread of private ownership. There is also a goal to get more international ownership in certain companies. Thirdly, we believe that privatization will make the companies stronger and more competitive. The methods for the privatization of each individual company must be tailor-made in order to reach that goal. A fourth reason is that state revenue from the sales will release capital that can be used for infrastructure investments in roads, railroads, airports, telecommunications, science, and higher education, or to just decrease the national debt. In other words, through privatization the state switches from one form of asset to another, which strengthens the nation's overall competitive power.

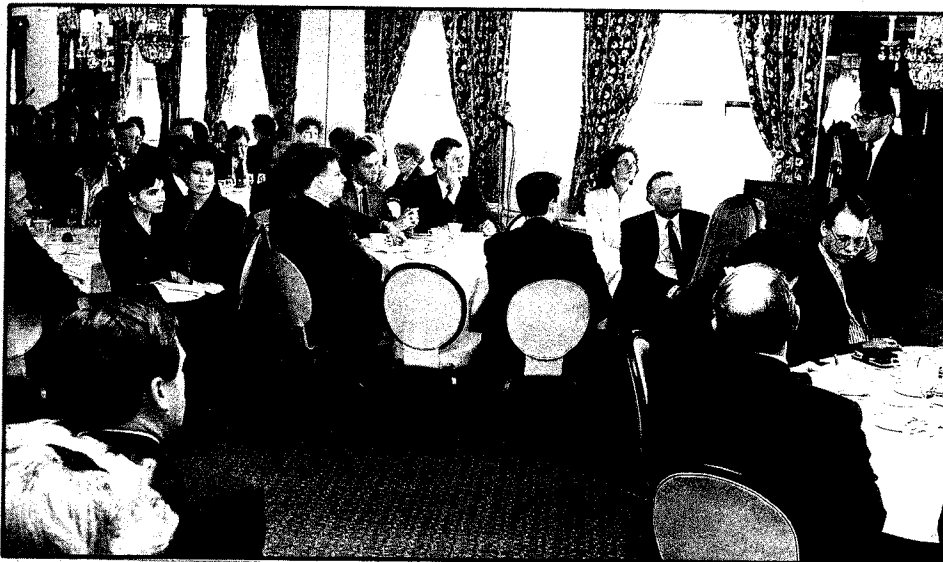
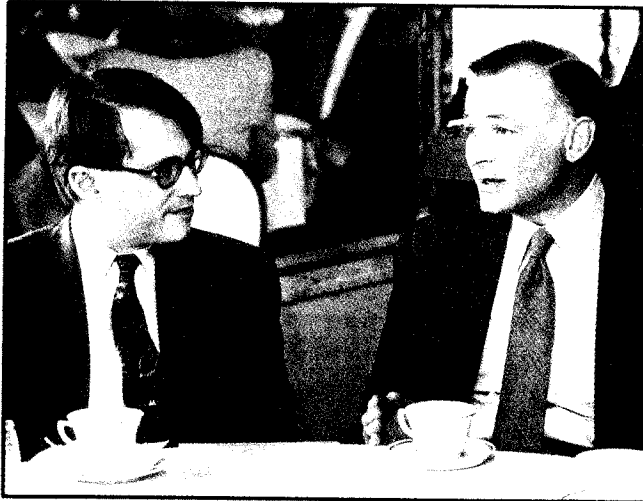
Naturally, there will be no restrictions on foreign investment in privatized companies. On my appointment as Minister of Industry and Commerce, one of the first measures I introduced was the removal of obstacles to foreign investment in Sweden. The Swedish economy will be an open one. And, as I have previously emphasized, we need greater foreign ownership and increased foreign investment in Sweden. Also, the removal by the government of the system of restricted shares is an additional factor that can facilitate foreign capital investment.

Ladies and Gentlemen, the government of which I am a member has now started the transition of Sweden from

"The government of which I am a member has now started the transition of Sweden from the era of 'confusion economics' to a market economy. We have a mandate from the Swedish people to fulfill our program from the election campaign and thus to change Sweden into a vigorous market economy. Surprisingly for some, we are going to use that mandate."

the era of "confusion economics" to a market economy. There will no longer be any doubt about what is and what is not the role of the state in the economy. Consequently, the excessively large public sector, government regulations, monopolies, negative discrimination of small companies, high taxes and state-owned companies are now being tackled systematically and in a target-oriented manner. We are now creating the basis for new structures which will hopefully provide increased welfare and open new opportunities for a new, strong growth-oriented period in Northern and Eastern Europe.

Already today we see signs of a turning point which include increased competitive strength, low inflation, and increased industrial production and export. We have a mandate from the Swedish people to fulfill our program from the election campaign and thus to change Sweden into a vigorous market economy. Surprisingly for some, we are going to use that mandate. ■



*ABOVE LEFT: Minister Per Westerberg and president Rick Dowden, president and CEO, Volvo North America Corp. ABOVE RIGHT: Gloria Gilbert Stoga, director, Privatization Project, Carnegie Council; and Johan Bjurstrom, executive director, Hoken North America. LEFT: Minister Westerberg addresses corporate executives at a Privatization Project breakfast. Photos by Larry Lettera.*

## Questions and Answers

**Q** How will you manage the problem that U.S. businesses have with provision of health care for employees? Will there be many changes in the health care delivery system in Sweden?

**A** There won't be any big changes in the health care system as a whole, but the production of health care in Sweden will be opened up for competition, so it will be possible to start private enterprises to provide the public sector with the production of health care. For example, it has been very difficult for medical doctors to start private practices in Sweden. We will change that: we will make it possible for dentists to go into private practice, and we will try to make it possible to have some small hospitals privatized. We hope that many of the people who have ideas within the public sector can use them to start new enterprises. Of course there will still be a public insurance program; everyone will be in the welfare system. Our welfare system will be especially good for the person who is sick for a long time.

**Q** Do you hope to reduce the percentage of the Gross National Product which goes into health care?

**A** I personally think that it is not possible to do that in Sweden. There are a lot of other areas where we can have cuts in public expenditure, but health care, we believe, is not one. But we can make the health care system much more effective and work absences for certain operations can be much shorter than they are today.

**Q** What is the status of Sweden's bid to enter the Common Market and is this one of the principal causes of the program you are introducing?

**A** The chairman of the European Community will be Britain, from the first of July. I would say Britain is heavily in favor of Sweden's membership; Germany is too. Our goal is that we will start negotiations with the EC this autumn for full membership. We will try to meet each commissioner and every minister of importance in every member state in the EC, in order to identify and eliminate problems in advance. We very much would like a fast negotiation with the EC. We believe negotiations have to start this autumn in order for Sweden to be a full member of the EC by 1 January 1995.

**Q** Can you specify some of the incentives you are offering, especially in taxation, to foreign investors?

**A** We have no special incentives for foreign investors in Sweden; we try to have a taxation system competitive with the EC. We have found that if we rely on opening the borders completely to the EC and the rest of the world, we can't have the highest tax rate. We have recognized, then, that we have to lower the most crucial taxes first; the ones that are damaging to the Swedish economy. So we have begun to lower taxation on companies; we have lowered the taxation on capital; and we will have lowered them even more in the upcoming year. We would even like to have lower taxes on energy; and I hope we do so as of 1 January 1993, in order to make Swedish industry more competitive than it is today. So there are no special incentives for foreign investors, but I would say it's necessary for Sweden to have competitive taxation on capital and investments, because otherwise it's impossible for us to compete. We are up in the far North of Europe, as you know, and I think we have to offer a little more favorable system than the central areas of Europe.

**Q** What is the position of your government on environmental regulations—specifically with water and air quality, and their impact on business?

**A** I think air and water pollution are not big problems for Swedish industry. Even the very angry groups, such as Greenpeace, and other environmental groups in Sweden, are telling us that Swedish industry has done a very, very good job in environmental terms. They have greatly reduced both air and water pollution. I think the pressure within the government and in parliament is very strong to have strict protection for the environment, but we also feel that we have to help the other countries around the Baltic Sea to improve water quality. For example, one river in Poland pollutes the Baltic Sea more than the whole of Sweden does—much more—and so it's a much better investment in environmental terms to work in Poland than it is in Sweden today. We have to have some sort of negotiation and perhaps we might even help to try to get better protection in Poland, in the Baltic States, and in St. Petersburg, for example. We are trying now to connect national grids for electricity in Sweden with ones in Central Europe and even with the ones in Eastern Europe. This is crucial because this is the only way of closing a bad nuclear reactor outside of St. Petersburg that doesn't work, or closing a very damaging coal-fire power plant in Poland, for example. Today, about 90% of Sweden's air pollution comes from Poland, Germany, and the former Soviet Union.

**Q** I believe your previous government's economic policy towards energy was to phase out the nuclear supply of electricity over the next decade or so. What is the current government's view on this?

**A** There was a treaty among three major parties last spring: the Social Democrats, the Liberals, and the Center Party. They formed a treaty about how to handle nuclear power stations and energy policies, and that treaty has been accepted by the present government. I personally voted against it in parliament because I am more in favor of nuclear power than the treaty is, but now I am responsible for Sweden's energy policy. The treaty states that we shall phase out nuclear power stations in Sweden if we can get new electricity from other sources in Sweden *and* if those sources are competitive in price for electricity. *Or*, we can close nuclear plants, if we can save enough electricity in Sweden to warrant that. Of course there are stipulations that we contribute a certain amount of money to help to get new power from alternative sources, such as wood. But when we've done that, it will be up to the market and the partners to show if it's possible to phase out nuclear power stations or not. As you can hear, I don't think it's possible. Of course we will fulfill the treaty; there's no doubt about it. Incidentally, my German counterpart recognized that Sweden's nuclear power stations are perhaps the safest in the world.

**Q** I wonder if you could speak a bit more about the system of education and what changes the country plans to make.

**A** There are two components to our education policy. First, the school check will follow the pupil, as of the first of January next year. That means it will be possible for a private school for the first time to receive grants; the municipalities' monies will follow the pupil to the school of his choice. That will create a more pluralistic education system in Sweden. Secondly, we will increase funding for science and research and development by about 50%. We would like to establish centers of excellence at some Swedish universities. We are going to double the number of people going to universities in Sweden within some years; right now the figure is much too low. Twenty years ago we were very competitive with the rest of Europe. Today I would say we are last, with only about 11% of our students going on to the universities. (I can tell you my British colleagues are very happy that they are not the last ones any more.) So, if we want to get up to the educational average in the OECD, we have to have about 22% of our students going to universities, and we will try to reach that figure within a few years.

**Q** Do you feel that once the Swedish people begin to feel the economic costs of your reform they will still be very strongly supportive of your programs?

**A** I must say that I am impressed by the opinion polls in Sweden. Even if we currently have the highest figure for unemployment in Sweden that we have had since the 1930s—it's an open figure of 4.5%, but if you take into account people in various work programs, it's about 9% unemployment—we still have a strong non-socialist majority in parliament. Of course we recognize that we will face big problems in Sweden, especially within a year I would say, when we will reach the top figure of unemployment in Sweden. But at the same time we feel there is no other choice. We have to make a very quick change in the economy because otherwise we will have a long stumbling period of further economic decline, which we have already had during the last ten years. The last three years in Sweden have been disastrous for the economy and I will say that some of my Social Democratic colleagues should be glad they lost the election campaign in 1988 instead of 1991, because it has been disastrous. Of course there will be problems when we implement our policies, but we feel that when we have a very deep recession in Sweden, a structural crisis, and a very costly welfare system, people understand there have to be some changes. We have been in an economic decline already and the people are looking for new policies; so there is much more chance to implement new ideas and make a very quick change in the economy and in policies. For example, the privatization program. I think it's commonly recognized that in good conscience the government can ask why it owns companies when we would like to use that money in other areas where we need it more. For example, we need to invest in roads, railroads, and infrastructure, which will be essential when we participate in the EC's free open market in just two years. I don't think all these reforms will be easy, but I think they are possible.

**Q** My question was, do you think people will buy it? You see the wisdom of your reforms, but will the Swedish people?

**A** We feel that there will be pressure put upon us, but there will be pressure whatever we do. Of course we will have to have a goal where we find there will be a turnaround in the economy, a recovery; and finally, it's much better to make the toughest decisions in the beginning than in the end. You make the changes in the policies now, just after the election campaigns, so they will work before the next elections.

**Q** You mentioned that you'd have to cut taxes to be more competitive. Which social programs would you cut since you have less money?

**A** We are not cutting social programs as a whole. We are trying to implement some sort of self-risk in the programs of the welfare system. For example, for the first two days when you're absent from work, you

won't be paid in Sweden in the future. This step alone will save a very large amount of money. We believe that our welfare system is very good, but we have to make it work in a much better way than it does today. Too many people take advantage of the welfare system and make it too costly and it's not always used by the people that really need it. We believe that we can reform those things. If we look, for example, at the cost of the welfare system when it was created as a monopoly, it was very cost-efficient but it has tended to become very fat over the years and we have to have some sort of competition so it will be more cost-efficient in the future. Of course there will be cuts in some of the programs, for example for subsidizing some parts of the Swedish industry, because we don't believe in subsidizing industries. And of course there will be cuts in different areas, but we believe there is not much choice. For example, a very big question is the taxation on liquor; a very Swedish question. When we open up to the Common Market, people will be able to import liquor and wines for personal use from Central Europe and there will be those countries' taxes on it, not Swedish taxes. Those taxes will be lower, so the Swedish government will get very little revenue out of its taxation on liquor and wine if it is much too high compared to Central Europe's. That's also the case with taxation on energy. We won't get the plants that consume a lot of energy in Sweden if our energy taxes are too high. Instead some companies will move to Poland or to the Baltic States and use the same amount or even more energy because it's cheap there. I think the goal for the Swedish economy is to reduce tax. It's not easy, but it's the only way. There is no other way to go.

**Q What are your plans for privatizing infrastructure and telecommunications?**

**A** First, perhaps, I should point out that we've used the French solution. We have had one parliamentary decision regarding privatization and then it is up to the government to decide how to sell the 35 companies we have targeted, so we don't have to go back to the parliament for approval of our privatization program anymore.

There are some infrastructure parts that we are going to sell, such as the big power-generating company. The first of January of this year we broke out the national grid from Vattenfall in order to create a competitive electricity market within Europe. We will be a front runner in this area, going ahead about two years earlier than the rest of the continent. We will try to have a third-party access system within the national grid so you could buy your electricity from any power plant you like and then you have to pay the national grid for the electricity for your plant or factory. When we establish such a market within electricity, then we are going to put Vattenfall into the market. Vattenfall is the fifth biggest power-generating company in Eu-

rope today.

We will go ahead with Swedish Telecom in the future, but it first has to have competition, which it will have within a few years. We haven't gotten a decision in parliament for Swedish Telecom yet; we will have a decision in parliament when we can foresee that there will be a competitive market for Swedish Telecom even inside Sweden. We won't do as the British did with British Telecom, selling off a monopoly, because I would like to sell companies working in competitive markets.

**Q Are you planning to have any advertising on television?**

**A** Not for the moment. The channels that have advertising in Sweden are all still small, so you don't get through to large audiences so much with advertising on television. Of course there will be advertising in newspapers in Sweden and when we have a market-based third television channel that would cover most of Sweden it will be possible to have some sort of advertising on TV. But right now the two main channels owned by the government can't have any advertising at all by law.

**Q What agency will be handling privatization in Sweden? Is there a structural form which foreign investors will approach?**

**A** We are using a special form, of course. We have a very small group of people working with the privatization program within the Ministry of Industry; it's just six people. In addition, we are using consultants and international advisors. For example, in the case of Swedish Steel, we have advisors from Sweden and a Swedish bank—Handelsbanken—that will monitor the privatization of Swedish Steel, and they will be assisted by international advisors. Different advisors and different banks will work with each company to be privatized so there will be some sort of solution that is tailored for each company. For about 10-15 other companies we have working committees which consist of representatives from the ministry, and from the company, and then they bring in consultants or advisors. They are buying the services of advisors and consultants which they believe will be the best for their company. We believe that's the best thing to do. Otherwise, I think, we would get into a very big debate in Sweden if you identified just one bank such as was done in France, for example, with Paribas. ■

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