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Recommendation for a

COUNCIL RECOMMENDATION

on the National Reform Programme 2011 of Sweden

and delivering a Council opinion

on the updated Convergence Programme of Sweden, 2011-2014

{SEC(2011) 735 final}

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THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Articles 121(2) and 148(4) thereof,

Having regard to Council Regulation (EC) No 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies[1], and in particular Article 9(3) thereof,

Having regard to the recommendation of the European Commission[2],

Having regard to the conclusions of the European Council,

Having regard to the opinion of the Employment Committee,

After consulting the Economic and Financial Committee,

Whereas:

(1) On 26 March 2010, the European Council agreed to the European Commission's proposal to launch a new strategy for jobs and growth, Europe 2020, based on enhanced coordination of economic policies, which will focus on the key areas where action is needed to boost Europe's potential for sustainable growth and competitiveness.

(2) On 13 July 2010, the Council adopted a recommendation on the broad guidelines for the economic policies of the Member States and the Union (2010 to 2014) and on 21 October 2010, adopted a decision on guidelines for the employment policies of the Member States[3], which together form the "integrated guidelines". Member States were invited to take the integrated guidelines into account in their national economic and employment policies.

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1 OJ L 209, 2.8.1997, p. 1.
2 OJ C , p. .
3 Maintained for 2011 by Council Decision 2011/308/EU of 19 May 2011.

(3) On 12 January 2011, the Commission adopted the first Annual Growth Survey, marking the start of a new cycle of economic governance in the EU and the first European semester of ex-ante and integrated policy coordination, which is anchored in the Europe 2020 strategy.

(4) On 25 March 2011, the European Council endorsed the priorities for fiscal consolidation and structural reform (in line with the Council's conclusions of 15 February and 7 March 2011 and further to the Commission's Annual Growth Survey). It underscored the need to give priority to restoring sound budgets and fiscal sustainability, reducing unemployment through labour market reforms and making new efforts to enhance growth. It requested Member States to translate these priorities into concrete measures to be included in their Stability or Convergence Programmes and National Reform Programmes.

(5) On 29 April 2011, Sweden submitted its updated 2011 Convergence Programme covering the period 2011-2014 and its 2011 National Reform Programme. The two programmes have been assessed at the same time.

(6) Before the economic crisis of 2008-2009, the Swedish economy enjoyed more than a decade of strong growth driven by both domestic demand and net exports. Being an export-oriented economy with a sizeable financial sector, it was strongly affected by the slump in external demand and the freezing of financial markets in 2008, causing GDP to contract by 5.1% in 2009 and the unemployment rate to increase from around 6% to above 9%. Thanks to a sound starting position without large adjustment needs in the household, banking and public sectors, as well as an adequate monetary and fiscal policy response, the recession was rather short-lived and affected mainly the export-oriented manufacturing sector. As world trade revived, the Swedish economy experienced a very strong and broad-based recovery, with real GDP rebounding by 5.5% in 2010. Due to the combined effect of automatic stabilisers and discretionary measures, the fiscal balance went from a surplus of 3.7% of GDP in 2007 to a deficit of 0.9% in 2009, before returning to balance in 2010.

(7) Based on the assessment of the updated Convergence Programme pursuant to Council Regulation (EC) No 1466/97, the Council is of the opinion that the macroeconomic scenario underpinning the budgetary projections is broadly plausible, except for 2012 when it is too favourable. The budgetary strategy, as outlined in the updated Convergence Programme, is appropriate, as it would contribute to meeting Sweden's medium-term objective (MTO) of 1% GDP surplus over a cycle. This would provide some margin against breaches of the 3% of GDP reference value in any future downturn. The programme projects the general government surplus to widen from 0.6% of GDP in 2011 to 3.7% of GDP in 2014, the last year of the programme. This improvement would result from assumed strong economic growth, as the programme does not envisage any consolidation efforts in these years. Risks to the budgetary targets are broadly balanced. As the revenue forecast presented in the programme is somewhat cautious for 2011, budgetary outcomes could turn out slightly better this year, whereas certain downside risks to budgetary projections from 2012 onwards are linked to favourable macroeconomic assumptions. As the government has indicated that further expansionary fiscal measures envisaged in the 2011 Budget Bill (including a fifth step in the in-work tax credit for wage-earners, a further rise in the threshold for paying state income tax, lower VAT on restaurant services, and lower taxes on pensions) could be implemented as from 2012, if there is sufficient fiscal space, there

is a risk of a pro-cyclical fiscal policy stance. Given the demographic outlook, it is important that Sweden continues to meet its MTO.

(8) The current situation in the housing and mortgage markets is a source of potential instability. After a short-lived and mild correction at the height of the financial crisis, house prices in Sweden - in contrast to other countries - resumed the strong upward trend observed since the second half of the 1990s and are now at a record high. The strong increase in house prices has gone hand in hand with rising household indebtedness which represented around 170% of disposable income by mid-2010, a historical high. Moreover, a large share of mortgage debt is at variable rates with little amortisation. This makes Swedish households particularly vulnerable to interest rate hikes or set-backs in employment. A marked correction in the housing market could have negative repercussions for macro-economic stability by making households rein in consumption to balance their budgets and by increasing financing costs for Swedish banks.

(9) As regards the Swedish labour market, non-EU nationals and youth have a relatively weak position compared with the EU average. Further improvement of their position on the labour market is essential to raise the overall employment rate and to improve the labour supply in the long term so as to meet the demographic challenge of an ageing population. The Swedish government is currently implementing several reforms in order to improve the employment situation of both groups such as increased funds for coaching, work-experience positions, vocational adult education, apprenticeship training coaching, targeted wage subsidies and streamlined Swedish language courses. The latest statistics show clear signs that the Swedish labour market is improving across the board, except for foreign-born women.

(10) The Commission has assessed the Convergence Programme and National Reform Programme[4]. It has taken into account not only their relevance for sustainable fiscal and socio-economic policy in Sweden but also their conformity with EU rules and guidance, given the need to reinforce the overall economic governance of the European Union by providing EU-level input into future national decisions. It considers that the programmes are adequately addressing the main challenges for Sweden. However, while the government's fiscal strategy to continue meeting the MTO is appropriate, care needs to be taken from 2012 onwards to avoid an excessively loose fiscal policy in times of favourable growth. The risks of macro-economic imbalances should be assessed, notably those stemming from rising house prices and household indebtedness. In addition, the labour market participation of vulnerable groups needs to be monitored and improved, notably for youth and foreign-born women.

(11) In light of this assessment, the Council has examined the 2011 update of the Convergence Programme of Sweden and its opinion[5] is reflected in particular in its recommendation under (1) set out below. Taking into account the European Council conclusions of 25 March 2011, the Council has examined the National Reform Programme of Sweden,

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[4] SEC(2011) 735.

[5] Foreseen in Article 9(3) of Council Regulation (EC) No 1466/97.

HEREBY RECOMMENDS that Sweden should take action within the period 2011-2012 to

(1) Keep fiscal policy on a path that ensures that the medium-term objective continues to be met and avoid a pro-cyclical fiscal policy stance in the current economic upturn.

(2) Take preventive action to deal with the macro-economic risks associated with rising house prices and household indebtedness, including reforms to the mortgage system, rent regulation, property taxation and construction permits.

(3) Monitor and improve the labour market participation of young people and other vulnerable groups.

Done at Brussels,

For the Council
The President