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Assessment of the 2017 convergence programme for

Sweden

(Note prepared by DG ECFIN staff)

CONTENTS

1. INTRODUCTION

On 28 April 2017, Sweden submitted its April 2017 convergence programme (hereafter called convergence programme), covering the period 2016-2020. The government approved the programme on 27 April 2017 and the parliamentary committee on finance was informed about the convergence programme on 25 April 2017.

Sweden is currently subject to the preventive arm of the the Stability and Growth Pact (SGP) and should preserve a sound fiscal position which ensures compliance with the medium term objective (MTO).

This document complements the Country Report published on 22 February 2017 and updates it with the information included in the convergence programme.

Section 2 presents the macroeconomic outlook underlying the convergence programme and provides an assessment based on the Commission 2017 spring forecast. The following section presents the recent and planned budgetary developments, according to the convergence programme. In particular, it includes an overview on the medium term budgetary plans, an assessment of the measures underpinning the convergence programme and a risk analysis of the budgetary plans based on Commission forecast. Section 4 assesses compliance with the rules of the SGP, including on the basis of the Commission forecast. Section 5 provides an overview on long term sustainability risks and Section 6 on recent developments and plans regarding the fiscal framework. Section 7 provides a summary.

2. MACROECONOMIC DEVELOPMENTS

Real GDP in Sweden rose by 3.3 % in 2016. Domestic factors remained key growth drivers, notably housing investment along with private and public consumption. The programme forecasts real GDP growth to moderate to 2.6 % in 2017 before slowing to 2.1 % in 2018. In 2017, private consumption on the back of a strong labour market and dynamic exports are set to be the main growth engines, while in 2018 a decline in general government consumption dampens growth.

Table 1: Comparison of macroeconomic developments and forecasts

	2016		2017		2018		2019	2020
	COM	CP	COM	CP	COM	CP	CP	CP
Real GDP (% change)	3.3	3.3	2.6	2.6	2.2	2.1	2.0	2.5
Private consumption (% change)	2.2	2.2	2.1	2.3	2.4	2.6	2.9	3.1
Gross fixed capital formation (% change)	5.9	5.9	3.9	3.3	3.1	3.2	3.3	3.7
Exports of goods and services (% change)	3.4	3.4	3.9	4.4	3.8	3.9	3.6	4.0
Imports of goods and services (% change)	3.7	3.7	3.5	3.8	3.4	3.7	3.9	4.2
Contributions to real GDP growth:								
- Final domestic demand	3.2	3.2	2.3	2.3	1.9	1.8	2.0	2.3
- Change in inventories	0.1	0.1	-0.1	-0.1	0.0	0.0	0.0	0.0
- Net exports	0.0	0.0	0.4	0.5	0.4	0.2	0.0	0.1
Output gap[1]	0.2	0.3	0.0	0.1	-0.2	-0.2	-0.5	-0.3
Employment (% change)	1.7	1.7	1.5	1.7	1.2	1.0	0.7	0.7
Unemployment rate (%)	6.9	6.9	6.6	6.6	6.6	6.4	6.3	6.2
Labour productivity (% change)	1.6	1.4	1.1	1.0	1.0	1.1	1.3	1.7
HICP inflation (%)	1.1	1.1	1.4	1.6	1.4	1.4	1.7	1.8
GDP deflator (% change)	1.4	1.4	2.3	2.0	2.0	1.8	2.0	1.9
Comp. of employees (per head, % change)	2.5	3.0	2.5	3.2	2.6	3.2	3.5	3.4
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	4.9	4.5	5.1	4.7	5.3	4.4	4.3	4.2

Note:

[1] In % of potential GDP, with potential GDP growth recalculated by Commission services on the basis of the programme scenario using the commonly agreed methodology.

Source :

Commission 2017 spring forecast (COM); convergence programme (CP).

Last year's programme projected real GDP to grow at 2.2 % in 2017 and 1.8 % in 2018. The macroeconomic outlook has therefore improved. For both years, investment and export growth have been revised up taking into account the stronger external environment and the continued accommodative monetary policy in Sweden and the euro area.

The macroeconomic scenario of the convergence programme is in line with the Commission 2017 spring forecast. The programme projects GDP growth of 2.6 % in 2017 and 2.1 % in 2017, while the Commission forecasts 2.6 % and 2.2 %, respectively. The convergence programme expects a slightly stronger growth contribution from net exports in 2017 compared with the Commission spring forecast and some minor differences in the domestic demand components. For 2018, final domestic demand and net exports are slightly weaker than the Commission spring forecast. The convergence programme projection for investment in 2017 is lower than the Commission spring forecast on the account of different assumptions on the growth profiles in the construction sector including housing. In addition, the convergence programme projections for private consumption growth (the tax base for indirect taxes) are higher than the ones of the Commission spring forecast as it assumes a slightly better labour market and therefore stronger wage growth (the tax base for personal income tax and social contributions) in both 2017 and 2018.

Sweden's economy is performing at its potential. The output gap, as recalculated by the Commission based on the information in the programme following the commonly agreed methodology, is expected to close in 2017 before turning negative in 2018 and remaining negative until the end of the period covered by the programme[1]. The (recalculated) output gap in the programme differs from the one estimated in the Commission 2017 spring forecast, mainly due to differences in projected labour and total factor productivity growth.

Overall the macroeconomic scenario underpinning the budgetary projections of the convergence programme is plausible.

3. RECENT AND PLANNED BUDGETARY DEVELOPMENTS

3.1. DEFICIT DEVELOPMENTS IN 2016 AND 2017

The general government balance improved significantly to a surplus of 0.9 % of GDP in 2016 after a surplus of 0.2 % of GDP in 2015, while the target of the 2016 convergence programme was a deficit of 0.4 % of GDP. The strong improvement is explained by better than expected VAT receipts, strong corporate and income tax revenues and lower expenditure related to the integration of refugees. No extraordinary measures were taken in 2016, explaining the substantial improvement compared to the convergence programme target.

For 2017, the convergence programme foresees a slight deterioration of the general government balance from a surplus of 0.9 % of GDP in 2016 to 0.3 % of GDP in 2017. This is in line with the Commission 2017 spring forecast. The decline in the surplus is mainly due to an expenditure increase linked to the reception and integration of refugees. Over time these expenses are according to the programme expected to decline from the 2017 level. In addition, expenditure was lower in 2016 due to an EU rebate, which would not also benefit 2017. As the convergence programme expects revenues to decline as a share of GDP, the general government surplus is set to fall. Nevertheless, the projected figure for the general government balance for 2017 has significantly improved compared to the projection of the convergence programme for 2016 (from a deficit of 0.3 % of GDP to a surplus of 0.3 % of GDP), which was based on the assumption of a much higher inflow of asylum seekers and respective expenditure for migration and integration.

3.2. MEDIUM-TERM STRATEGY AND TARGETS

The purpose of the programme is to maintain and further increase the general government surplus until the end of the programme period. This would result in a recalculated structural balance of 2.3 % of GDP, significantly outperforming the MTO.

The MTO specified by Sweden in the convergence programme, a structural balance of -1 % of GDP, reflects the objectives of the Pact and is consistent with the minimum updated requirement as a member of the EU. In addition, Sweden has national budgetary policy goals,

[1] The recalculated output gaps differ from the ones presented in the programme mainly due to some differences in the methodology.

among which a 1 % surplus target and an expenditure ceiling setting limits for expenditure developments, which should ensure respect of the MTO.[2]

For 2018, the convergence programme expects under a no-policy change assumption a general government surplus of 0.6 % of GDP, similar to the Commission 2017 spring forecast (0.7 % of GDP). The main driver behind this improvement is a decline in general government consumption due to lower expenditure on migration, whereas revenues remain broadly unchanged as a share of GDP. These developments according to the programme are set to further improve the headline balance over the programme period.

The structural balance as recalculated by the Commission based on the information in the programme following the commonly agreed methodology is expected to stand at 0.4 % of GDP in 2017 and 0.7 % of GDP in 2018, respecting the MTO of a structural deficit of 1 % of GDP. The time profile of the programme expects a gradual improvement of the structural balance, so that it would reach 2.3 % of GDP in 2020. The structural balance forecast in the Commission 2017 spring forecast is 0.4 % of GDP in 2017 and 0.8 % in 2018 respectively.

[2] The government intends to change the structural surplus target to 0.33 % of GDP over the economic cycle and to introduce a debt anchor. Respective proposals are supposed to be submitted to the Riksdag together with the Budget Bill for 2018 and should come into force as of 2019.

Table 2: Composition of the budgetary adjustment

(% of GDP)	2016	2017		2018		2019	2020	Change: 2016-2020
	COM	COM	CP	COM	CP	CP	CP	CP
Revenue	**50.9**	**50.4**	**49.9**	**50.1**	**49.9**	**50.0**	**50.0**	**-0.9**
of which:								
- Taxes on production and imports	22.6	22.4	22.5	22.3	22.4	22.4	22.3	-0.3
- Current taxes on income, wealth, etc.	18.4	18.3	15.7	18.4	15.7	15.9	16.0	-2.4
- Social contributions	3.7	3.6	5.3	3.6	5.3	5.3	5.3	1.6
- Other (residual)	6.3	5.9	6.4	5.8	6.5	6.4	6.4	0.1
Expenditure	**50.0**	**50.0**	**49.6**	**49.4**	**49.3**	**48.6**	**47.9**	**-2.1**
of which:								
- Primary expenditure	49.6	49.5	49.2	48.8	48.8	48.1	47.4	-2.2
of which:								
Compensation of employees	12.6	12.6	12.6	12.5	12.5	12.4	12.3	-0.3
Intermediate consumption	8.1	7.9	8.0	7.6	7.8	7.6	7.4	-0.7
Social payments	17.0	17.0	16.9	16.8	16.7	16.4	16.2	-0.8
Subsidies	1.6	1.6	1.6	1.5	1.6	1.6	1.6	0.0
Gross fixed capital formation	4.4	4.5	4.5	4.5	4.5	4.5	4.5	0.1
Other (residual)	5.9	5.9	5.7	5.9	5.7	5.6	5.5	-0.4
- Interest expenditure	0.4	0.5	0.4	0.6	0.5	0.5	0.5	0.1
General government balance (GGB)	**0.9**	**0.4**	**0.3**	**0.7**	**0.6**	**1.4**	**2.1**	**1.2**
Primary balance	**1.3**	**0.9**	**0.7**	**1.3**	**1.1**	**1.9**	**2.7**	**1.4**
One-off and other temporary	0.0	0.0	-0.2	0.0	0.0	0.0	0.0	0.0
GGB excl. one-offs	**0.9**	**0.4**	**0.5**	**0.7**	**0.6**	**1.4**	**2.1**	**1.2**
Output gap[1]	0.2	0.0	0.1	-0.2	-0.2	-0.5	-0.3	-0.5
Cyclically-adjusted balance[1]	0.8	0.4	0.2	0.8	0.7	1.7	2.3	1.5
Structural balance[2]	**0.8**	**0.4**	**0.4**	**0.8**	**0.7**	**1.7**	**2.3**	**1.5**
Structural primary balance[2]	1.2	0.9	0.8	1.4	1.2	2.2	2.8	1.6

Notes:

[1]Output gap (in % of potential GDP) and cyclically-adjusted balance according to the programme as recalculated by Commission on the basis of the programme scenario using the commonly agreed methodology.

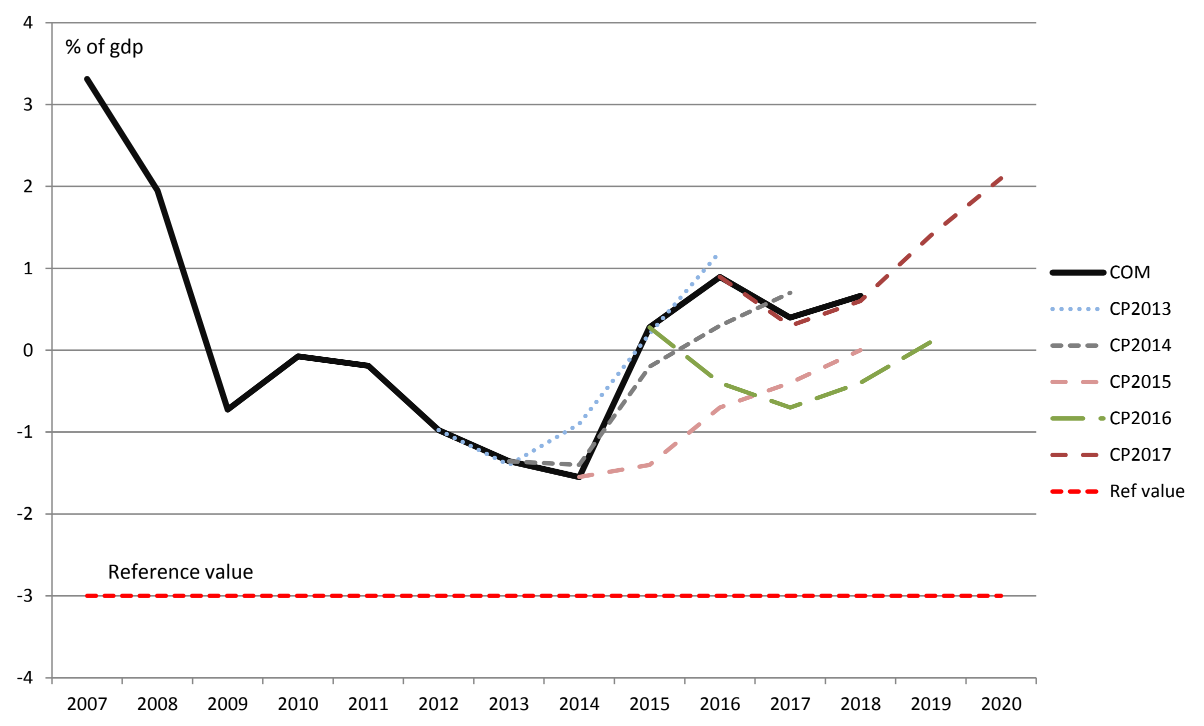
[2]Structural (primary) balance = cyclically-adjusted (primary) balance excluding one-off and other temporary measures.

Source:

Convergence programme (CP); Commission 2017 spring forecasts (COM); Commission calculations.

Previous convergence programmes have assumed a less positive outlook as regards the deficit projections. Notably, last year's projection rested on the assumption of a progressive development towards a balanced budget by 2019, while this year's convergence programme projects a faster adjustment path as outlined above (due, inter alia, to the lower expenditure linked to the reception and integration of migrants).

Figure 1: General government balance projections in successive programmes (% of GDP)



Source: Commission 2017 Spring Forecast. Stability and convergence programmes

3.3. MEASURES UNDERPINNING THE PROGRAMME

The convergence programme describes measures proposed and announced by the government in the Budget Bill for 2017. In total, these measures are estimated to have an effect on the general government finances of roughly -0.4 % of GDP in 2017 and of -0.1 % of GDP in 2018. Overall, the key priorities of the Swedish government, as reflected in expenditure increases resulting from recent and forthcoming reforms, remain and address challenges in the welfare sector and in support the local government sector. These policies areas are prioritised through the so-called "welfare billions" (around 0.25 % of GDP in both 2017 and 2018) that include measures to improve conditions for teaching, to promote reading and to introduce free health care for the elderly, among others. Other priorities are the labour market and tackling unemployment (roughly 0.15 % and 0.2 % of GDP in 2017 and 2018 respectively), and supporting a sustainable future through efficient transport and infrastructure, along with the challenge of becoming one of the first fossil-fuel free countries in the world (roughly 0.15 % and 0.2 % of GDP in 2017 and 2018 respectively).

On the revenue side, overall tax revenues are expected to increase in 2017 by around 0.15 % of GDP. According to the Budget Bill, these increases result mainly from a higher energy tax on electricity, abolished deductions for interest on certain loans, a new excise duty on chemicals and a limited adjustment of the lower and upper brackets for national income tax. As for 2018, the expected revenues increases would amount to roughly 0.25 % of GDP but the main source of financing would come in the form of expenditure reductions (approximately standing at 0.4 % of GDP). These reductions include measures for more effective labour market policy and, more importantly, reduced expenditure for migration and unaccompanied minors and young people.

The convergence programme refers to "one-off and other temporary measures" amounting to 0.2 % of GDP in 2017 that corresponds to the EU rebate received in 2016 and not in 2017. This item has not been classified as a one-off and other temporary measure in the Commission 2017 spring forecast as it does not result from government action.

3.4. DEBT DEVELOPMENTS

Sweden's government gross debt ratio was 41.6 % of GDP in 2016, below the 60 % of GDP reference value. While this is higher than the average over the time period 2011-2015, it is 2.4 pps. lower than in 2015.

The debt ratio is projected to decrease in 2017, as a proportion to GDP, on the back of strong growth and valuation effects. The foreseen sustained economic growth and general government balance improvement should imply a further gradual decrease of the debt ratio until the end of the programme period. In 2018, economic growth along with the inflation effect and the primary balance improvement are set more than compensate the interest expenditure, serving to reduce the debt ratio. The convergence programme forecast on government gross debt is trending in the same direction as the Commission's 2017 spring forecast, albeit with a slower pace.

Table 3: Debt developments

(% of GDP)	Average 2011-2015	2016	2017		2018		2019	2020
			COM	CP	COM	CP	CP	CP
Gross debt ratio[1]	**41.0**	**41.6**	**39.1**	**39.5**	**37.0**	**37.3**	**34.7**	**31.4**
Change in the ratio	1.1	-2.4	-2.5	-2.1	-2.2	-2.2	-2.6	-3.3
Contributions[2] *:*								
1. Primary balance	**-0.1**	**-1.3**	**-0.9**	**-0.7**	**-1.3**	**-1.1**	**-1.9**	**-2.7**
2. "Snow-ball" effect	**-0.6**	**-1.5**	**-1.5**	**-1.4**	**-1.0**	**-1.0**	**-0.9**	**-0.8**
Of which:								
Interest expenditure	0.8	0.4	0.5	0.4	0.6	0.5	0.5	0.6
Growth effect	-0.8	-1.4	-1.0	-1.0	-0.8	-0.8	-0.7	-0.8
Inflation effect	-0.6	-0.6	-0.9	-0.8	-0.7	-0.7	-0.7	-0.6
3. Stock-flow adjustment	**1.8**	**0.5**	**-0.1**	**0.1**	**0.1**	**-0.1**	**0.2**	**0.3**
Of which:								
Cash/accruals diff.				0.2		0.0	0.2	0.3
Acc. financial assets								
Privatisation				-0.1		-0.1	-0.1	-0.1
Val. effect & residual				0.0		-0.1	0.2	0.1

Notes:

[1] End of period.

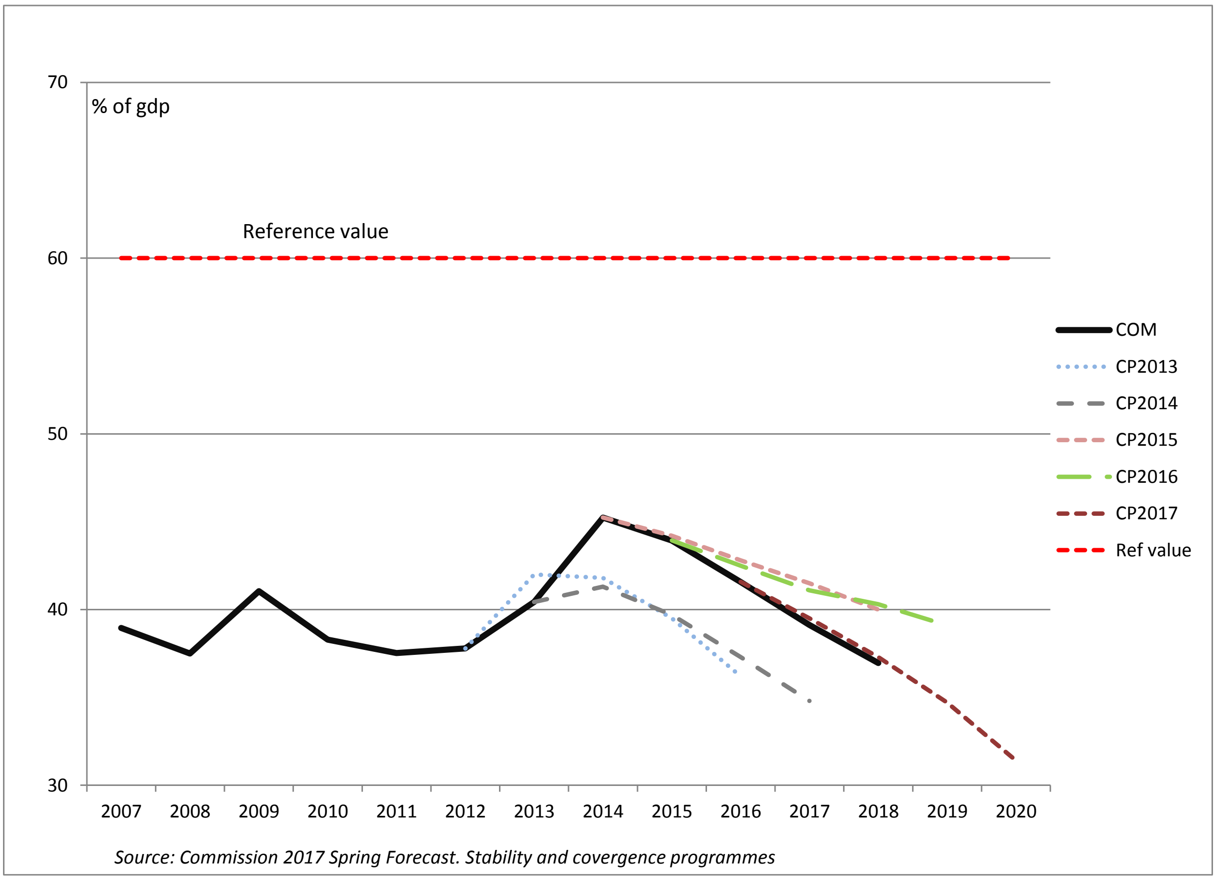
[2] The snow-ball effect captures the impact of interest expenditure on accumulated debt, as well as the impact of real GDP growth and inflation on the debt ratio (through the denominator). The stock-flow adjustment includes differences in cash and accrual accounting, accumulation of financial assets and valuation and other residual effects.

Source :

Commission 2017 spring forecast (COM); convergence programme (CP), Comission calculations.

Last year's convergence programme assumed also a declining debt ratio over time, although at a slower pace compared to this year's programme since the 2016 programme expected a general government deficit, while the 2017 programme forecasts an increasing surpluses. Previous programmes also assumed a declining trend, but from a lower level[3].

Figure 2: Government debt projections in successive programmes (% of GDP)



3.5. RISK ASSESSMENT

For 2017 and 2018, the convergence programme and the Commission 2017 spring forecast are almost fully aligned regarding the general government balances. The recalculated structural balance is expected to be 0.4 % of GDP in 2017 and 0.7 % of GDP in 2017 in the convergence programme. These figures are similar to those of the Commission 2017 spring forecast which expects 0.4 % of GDP in 2017 and 0.8 % of GDP in 2018. In both cases the MTO of a structural deficit of 1 % of GDP is thus expected to be respected.

There are a few risk factors that could affect the Swedish economy negatively. In 2015, Sweden welcomed a very large number of asylum seekers (163 000 persons). While it is a priority of the government that those individuals who are granted permanent residency get access to efficient training and quickly get integrated into the labour market, it is at this stage uncertain how fast a successful integration is possible. There are risks both on the expenditure and on the revenue side linked to the possibility of the large cohort of newcomers not successfully entering the labour market.

[3] This lower level was mainly caused by changing accounting standards. As of 2014, central government units besides the National Debt Office may old outstanding repos over the turn of the year, contrary to previous practice. If repos are not closed before the end of the year, both gross debt and assets increase according to National Accounts.

The current fiscal forecast is based on a continued, but moderate inflow of around 30 000 asylum seekers in the coming years. However, it remains difficult to assess international developments and, as a consequence, the likely number of asylum seekers in upcoming years.

Sweden is a small, open economy heavily dependent on its exports. Therefore, any weaker-than-expected economic growth in the rest of the world ultimately affects growth and employment through lower exports. Furthermore, currency fluctuations can have marked effects for Swedish exports and the Riksbank has repeatedly stated its readiness to intervene with further monetary policy stimulation in case of an abrupt Swedish krona appreciation. Finally, a potential correction in house prices, which rose to new historical highs in 2016, could dampen household consumption and construction investment. The convergence programme also acknowledges that increasing household indebtedness poses a risk to macroeconomic stability.

Considering Sweden's long track record of fiscal soundness respecting its obligations under the preventive arm of the SGP, its sound fiscal position and the relatively robust budgetary framework, the risks outlined above are assessed to be low.

4. COMPLIANCE WITH THE PROVISIONS OF THE STABILITY AND GROWTH PACT

Sweden is subject to the preventive arm of the Stability and Growth Pact. In 2016, the Council did not address a SGP-related recommendation to Sweden. Based on the outturn data and the Commission 2017 spring forecast, the ex-post assessment suggests compliance with the preventive arm requirements in 2016.

The 2017 convergence programme projects the recalculated structural balance to temporarily worsen from a surplus of 0.8 % of GDP in 2016 to a surplus of 0.4 % in 2017. In 2018, it is expected to revert to 0.8 % of GDP. According to the information provided in the convergence programme, Sweden is expected to remain above its MTO - a structural balance of -1 % of GDP. This is confirmed by the convergence programme and the Commission 2017 spring forecast, according to which the structural balance is projected to reach 0.4 % of GDP in 2017 and to improve to 0.8 % in 2018 under the no-policy-change assumption. Therefore, Sweden is projected to be in compliance with the requirements of the preventive arm of the Pact in both 2017 and 2018. Beyond 2018, the programme indicates that the structural balance is set to remain above the MTO over the programme period, with a positive margin to the limit value.

Table 4: Compliance with the requirements under the preventive arm

(% of GDP)	2016	2017		2018	
Initial position[1]					
Medium-term objective (MTO)	-1.0	-1.0		-1.0	
Structural balance[2] (COM)	0.8	0.4		0.8	
Structural balance based on freezing (COM)	0.8	0.4		-	
Position vis-a -vis the MTO[3]	At or above the MTO	At or above the MTO		At or above the MTO	
(% of GDP)	**2016**	**2017**		**2018**	
	COM	**CP**	**COM**	**CP**	**COM**
Structural balance pillar					
Required adjustment[4]	Compliant				
Required adjustment corrected[5]					
Change in structural balance[6]					
One-year deviation from the required adjustment [7]					
Two-year average deviation from the required adjustment [7]					
Expenditure benchmark pillar					
Applicable reference rate[8]					
One-year deviation adjusted for one-offs[9]					
Two-year deviation adjusted for one-offs[9]					
PER MEMORIAM: One-year deviation [10]					
PER MEMORIAM: Two-year average deviation [10]					
Conclusion					
Conclusion over one year					
Conclusion over two years					

Notes

[1] The most favourable level of the structural balance, measured as a percentage of GDP reached at the end of year t-1, between spring forecast (t-1) and the latest forecast, determines whether there is a need to adjust towards the MTO or not in year t. A margin of 0.25 percentage points (p.p.) is allowed in order to be evaluated as having reached the MTO.

[2] Structural balance = cyclically-adjusted government balance excluding one-off measures.

[3] Based on the relevant structural balance at year t-1.

[4] Based on the position vis-à-vis the MTO, the cyclical position and the debt level (See European Commission: Vade mecum on the Stability and Growth Pact, page 38.).

[5] Required adjustment corrected for the clauses, the possible margin to the MTO and the allowed deviation in case of overachievers.

[6] Change in the structural balance compared to year t-1. Ex post assessment (for 2014) is carried out on the basis of Commission 2015 spring forecast.

[7] The difference of the change in the structural balance and the corrected required adjustment.

[8] Reference medium-term rate of potential GDP growth. The (standard) reference rate applies from year t+1, if the country has reached its MTO in year t. A corrected rate applies as long as the country is adjusting towards its MTO, including in year t.

[9] Deviation of the growth rate of public expenditure net of discretionary revenue measures, revenue increases mandated by law and one-offs from the applicable reference rate in terms of the effect on the structural balance. The expenditure aggregate used for the expenditure benchmark is obtained following the commonly agreed methodology. A negative sign implies that expenditure growth exceeds the applicable reference rate.

[10] Deviation of the growth rate of public expenditure net of discretionary revenue measures and revenue increases mandated by law from the applicable reference rate in terms of the effect on the structural balance. The expenditure aggregate used for the expenditure benchmark is obtained following the commonly agreed methodology. A negative sign implies that expenditure growth exceeds the applicable reference rate.

Source :

Convergence programme (CP); Commission 2017 spring forecast (COM); Commission calculations.

5. LONG-TERM SUSTAINABILITY

Sweden does not appear to face fiscal sustainability risks in the short run according to the S0 indicator, which captures the short-term risks of fiscal stress stemming from the fiscal, as well as the macro-financial and competitiveness sides of the economy.

Based on Commission forecasts and a no-fiscal policy change scenario beyond forecasts, government debt, at 41.6 % of GDP in 2016, is expected to decrease (to 21.8 % in 2027), thus remaining below the 60 % of GDP Treaty threshold. This highlights low risks for the country from debt sustainability analysis in the medium term. The full implementation of the convergence programme would keep debt on a decreasing path until 2027.

The medium-term fiscal sustainability risk indicator S1 is at -4 pps. of GDP, primarily related to the initial budgetary position, as well as the low level of government debt contributing with -2.4 pps. and -1.8 pps. of GDP respectively, thus indicating low risks in the medium term. The full implementation of the convergence programme would put the sustainability risk indicator S1 at -6.8 pps. of GDP, leading to even lower medium-term risk. Overall, risks to fiscal sustainability over the medium-term are, therefore, low.

The long-term fiscal sustainability risk indicator S2 (which shows the adjustment effort needed to ensure that the debt-to-GDP ratio is not on an ever-increasing path) is at 0.1 pps of GDP. In the long-term, Sweden therefore appears to face low fiscal sustainability risks. Full implementation of the programme would bring the S2 indicator down to -1.3 pps. of GDP, leading to an even lower long-term risk.

Table 5: Sustainability indicators

Time horizon			No-policy Change Scenario		Stability / Convergence Programme Scenario	
Short Term			**LOW risk**			
S0 indicator [1]			0.1			
Fiscal subindex			0.0	LOW risk		
Financial & competitiveness subindex			0.2	LOW risk		
Medium Term			**LOW risk**			
DSA [2]			LOW risk			
S1 indicator [3]			-4.0	LOW risk	-6.8	LOW risk
of which						
	Initial Budgetary Position		-2.4		-4.5	
	Debt Requirement		-1.8		-2.6	
	Cost of Ageing		0.2		0.2	
	of which					
		Pensions	-0.3		-0.2	
		Health-care	0.1		0.1	
		Long-term care	0.3		0.3	
		Other	0.1		0.1	
Long Term			**LOW risk**		**LOW risk**	
S2 indicator [4]			0.1		-1.3	
of which						
	Initial Budgetary Position		-0.8		-2.2	
	Cost of Ageing		0.9		0.9	
	of which					
		Pensions	-0.7		-0.6	
		Health-care	0.3		0.3	
		Long-term care	1.1		1.0	
		Other	0.2		0.2	

Source: Commission services; 2017 stability/convergence programme.

Note: the 'no-policy-change' scenario depicts the sustainability gap under the assumption that the structural primary balance position evolves according to the Commissions' spring 2017 forecast covering until 2018 included. The 'stability/convergence programme' scenario depicts the sustainability gap under the assumption that the budgetary plans in the programme are fully implemented over the period covered by the programme. Age-related expenditure as given in the 2015 Ageing Report.

[1] The S0 indicator of short term fiscal challenges informs the early detection of fiscal stress associated to fiscal risks within a one-year horizon. To estimate these risks S0 uses a set of fiscal, financial and competitiveness indicators selected and weighted according to their signalling power. S0 is therefore a composite indicator whose methodology is fundamentally different from the S1 and S2 indicators, which quantify fiscal adjustment efforts. The critical threshold for the overall S0 indicator is 0.46. For the fiscal and the financial-competitiveness sub-indexes, thresholds are respectively at 0.36 and 0.49*.

[2] Debt Sustainability Analysis (DSA) is performed around the no fiscal policy change scenario in a manner that tests the response of this scenario to different shocks presented as sensitivity tests and stochastic projections*.

[3] The S1 indicator is a medium-term sustainability gap; it measures the upfront fiscal adjustment effort required to bring the debt-to-GDP ratio to 60 % by 2031. This adjustment effort corresponds to a cumulated improvement in the structural primary balance over the 5 years following the forecast horizon (i.e. from 2019 for No-policy Change scenario and from last available year for the SCP scenario); it must be then sustained, including financing for any additional expenditure until the target date, arising from an ageing population. The critical thresholds for S1 are 0 and 2.5, between which S1 indicates medium risk. If S1 is below 0 or above 2.5, it indicates low or high risk, respectively*.

[4] The S2 indicator is a long-term sustainability gap; it shows the upfront and permanent fiscal adjustment required to stabilise the debt-to-GDP ratio over the infinite horizon, including the costs of ageing. The critical thresholds for S2 are 2 and 6, between which S2 indicates medium risk. If S2 is below 2 or above 6, it indicates low or high risk, respectively*.

* For more information see Fiscal Sustainability Report 2015 and Debt Sustainability Monitor 2016.

6. FISCAL FRAMEWORK

The main Swedish numerical rule, the 1 % of GDP surplus target over the economic cycle encompasses the finances of the general government, i.e. including both central and local governments and the pension system. The fulfilment of the surplus target has traditionally been assessed against five indicators. A long-standing uncertainty regarding the monitoring of this rule is that the relative weight the government puts on each of the indicators is not defined.

Regarding ex post compliance, the authorities report in the convergence programme that the surplus target has not been attained, based on the measure of the backward-looking 10-year average of the general government balance (0.2 % of GDP in 2016). Also, the seven-year indicator stood at 0.1 % of GDP in 2016, i.e. almost a full percentage point below the target, but it is expected to improve to 0.6 % in 2017.

Looking forward, the envisaged budgetary balances laid down in the programme would lead Sweden in the direction of a gradual closing of the gap in the medium term, with a structural balance of 0.3 % of GDP in 2017, 0.6 % in 2018 and 1.4 % in 2018. At the same time, the national authorities are also in the process of revisiting the current national budgetary policy targets in a direction that will further facilitate goal achievement, including shifting the surplus target to 0.33 % of GDP (see the February Country Report for the details of the 2016 September reform proposal). The government announced in the convergence programme that they intend to introduce the corresponding amendment to the Riksdag together with the 2018 Budget Bill.

The Fiscal Policy Council is currently not involved in the endorsement or assessment of the macroeconomic scenario underpinning the convergence programme. However, in its annual reports, the Fiscal Policy Council has signalled the issue of non-compliance with the 1 % surplus target and the complexity of the rules that render evaluation difficult for several years. The Fiscal Policy Council has expressed its broad support of the planned reform package. However, the Council opposes the announced change to the nomination procedure, which it fears might in fact decrease the independence of its members since it would become more closely connected to the political sphere.

Based on the information provided in the convergence programme, the past fiscal performance in Sweden appears to comply only partially with the requirements of the applicable national numerical fiscal rules. However, the planned and forecast fiscal performance appears to broadly comply with the national requirements as adapted by the announced reform.

7. CONCLUSIONS

In 2016, Sweden achieved an improvement of the structural balance, which stood at 0.8 % of GDP, significantly outperforming the MTO. However, expenditure increases linked primarily to the reception and integration of migrants are expected to temporary affect the structural balance negatively in 2017. The consolidated gross debt stood at 41.6 % of GDP at the end of

2016, below the Treaty threshold of 60 % of GDP. The debt ratio is projected to decrease further in 2017, as a proportion to GDP.

Overall, Sweden's structural balance is expected to remain above the MTO in both 2017 and 2018 and is therefore foreseen to continue to meet the requirements under the preventive arm of the Pact.

8. ANNEX

Table I. Macroeconomic indicators

	1999-2003	2004-2008	2009-2013	2014	2015	2016	2017	2018
Core indicators								
GDP growth rate	3.1	2.9	0.9	2.6	4.1	3.3	2.6	2.2
Output gap [1]	0.1	1.4	-2.3	-2.0	-0.4	0.2	0.0	-0.2
HICP (annual % change)	1.8	1.7	1.3	0.2	0.7	1.1	1.4	1.4
Domestic demand (annual % change) [2]	2.3	2.8	1.1	2.9	4.0	3.5	2.3	2.0
Unemployment rate (% of labour force) [3]	6.1	6.9	8.1	7.9	7.4	6.9	6.6	6.6
Gross fixed capital formation (% of GDP)	21.8	23.0	22.4	23.1	23.6	24.2	24.5	24.7
Gross national saving (% of GDP)	27.4	31.1	28.4	28.2	28.9	29.7	30.2	30.6
General Government (% of GDP)								
Net lending (+) or net borrowing (-)	**0.5**	**1.9**	**-0.7**	**-1.5**	**0.3**	**0.9**	**0.4**	**0.7**
Gross debt	**52.8**	**43.5**	**39.0**	**45.2**	**43.9**	**41.6**	**39.1**	**37.0**
Net financial assets	**-9.2**	**5.7**	**18.7**	**19.7**	**19.1**	**21.0**	**n.a**	**n.a**
Total revenue	54.9	53.3	51.2	50.0	50.5	50.9	50.4	50.1
Total expenditure	54.4	51.4	51.8	51.5	50.2	50.0	50.0	49.4
of which: Interest	3.0	1.7	1.0	0.7	0.5	0.4	0.5	0.6
Corporations (% of GDP)								
Net lending (+) or net borrowing (-)	**2.1**	**3.1**	**0.3**	**-1.5**	**-3.3**	**-3.3**	**-2.4**	**-1.9**
Net financial assets; non-financial corporations	**-131.3**	**-154.7**	**-180.9**	**-197.4**	**-208.2**	**-206.7**	**n.a**	**n.a**
Net financial assets; financial corporations	**-1.5**	**-3.4**	**-5.0**	**-11.5**	**-6.9**	**-5.5**	**n.a**	**n.a**
Gross capital formation	15.6	15.9	15.2	16.4	17.2	17.6	17.7	17.8
Gross operating surplus	23.3	24.7	23.5	23.5	24.0	23.1	23.8	24.3
Households and NPISH (% of GDP)								
Net lending (+) or net borrowing (-)	**2.0**	**2.4**	**6.0**	**7.7**	**7.4**	**7.1**	**6.9**	**6.5**
Net financial assets	**110.9**	**134.4**	**155.0**	**190.2**	**198.7**	**203.9**	**n.a**	**n.a**
Gross wages and salaries	39.1	38.1	40.0	40.5	39.7	39.7	39.3	39.1
Net property income	3.1	3.4	5.2	5.9	6.4	5.9	5.8	5.9
Current transfers received	22.7	21.4	20.9	20.6	20.1	19.8	19.6	19.4
Gross saving	4.5	5.6	8.9	10.3	10.3	10.1	9.9	9.6
Rest of the world (% of GDP)								
Net lending (+) or net borrowing (-)	**5.0**	**7.7**	**5.7**	**4.7**	**4.5**	**4.9**	**5.1**	**5.3**
Net financial assets	**31.1**	**18.0**	**12.2**	**-1.1**	**-2.7**	**-12.7**	**n.a**	**n.a**
Net exports of goods and services	6.2	7.1	5.1	4.3	4.7	4.6	5.2	5.4
Net primary income from the rest of the world	0.4	2.4	2.5	2.2	1.5	1.6	1.5	1.5
Net capital transactions	-0.3	-0.2	-0.2	-0.1	-0.2	-0.1	-0.1	-0.1
Tradable sector	43.7	43.0	41.3	40.1	40.3	39.7	n.a	n.a
Non tradable sector	44.5	45.2	46.8	48.4	48.2	48.6	n.a	n.a
of which: Building and construction sector	4.4	5.1	5.0	4.9	5.2	5.4	n.a	n.a
Real effective exchange rate (index, 2000=100)	101.6	102.5	105.5	110.0	104.3	103.8	102.3	102.0
Terms of trade goods and services (index, 2000=100)	103.9	99.6	99.7	99.8	100.6	100.9	101.3	101.4
Market performance of exports (index, 2000=100)	101.2	101.9	99.2	99.1	100.4	100.8	101.3	101.2

Notes:

[1] The output gap constitutes the gap between the actual and potential gross domestic product at 2005 market prices.

[2] The indicator on domestic demand includes stocks.

[3] Unemployed persons are all persons who were not employed, had actively sought work and were ready to begin working immediately or within two weeks. The labour force is the total number of people employed and unemployed. The unemployment rate covers the age group 15-74.

Source :
AMECO data, Commission 2017 spring forecast