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Recommendation for a

COUNCIL RECOMMENDATION

on the 2017 National Reform Programme of Sweden

and delivering a Council opinion on the 2017 Convergence Programme of Sweden

Recommendation for a

COUNCIL RECOMMENDATION

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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(2) thereof,

Having regard to Regulation (EU) No 1176/2011 of the European Parliament and of the Council of 16 November 2011 on the prevention and correction of macroeconomic imbalances,[2] and in particular Article 6(1) thereof,

Having regard to the recommendation of the European Commission,[3]

Having regard to the resolutions of the European Parliament,[4]

Having regard to the conclusions of the European Council,

Having regard to the opinion of the Employment Committee,

Having regard to the opinion of the Economic and Financial Committee,

Having regard to the opinion of the Social Protection Committee,

Having regard to the opinion of the Economic Policy Committee,

Whereas:

(1) On 16 November 2016, the Commission adopted the Annual Growth Survey,[5] marking the start of the 2017 European Semester of economic policy coordination. The priorities of the Annual Growth Survey were endorsed by the European Council on 9-10 March 2017. On 16 November 2016, on the basis of Regulation (EU) No 1176/2011, the Commission adopted the Alert Mechanism Report,[6] in which it identified Sweden as one of the Member States for which an in-depth review would be carried out.

[1] OJ L 209, 2.8.1997, p. 1.
[2] OJ L 306, 23.11.2011, p. 25.
[3] COM(2017) 526 final.
[4] P8_ TA(2017)0038, P8_ TA(2017)0039, and P8_ TA(2017)0040.
[5] COM(2016) 725 final.
[6] COM(2016) 728 final.

(2) The 2017 country report for Sweden[7] was published on 22 February 2017. It assessed Sweden's progress in addressing the country-specific recommendation adopted by the Council on 12 July 2016, the follow-up given to the recommendations adopted in previous years and Sweden's progress towards its national Europe 2020 targets. It also included an in-depth review under Article 5 of Regulation (EU) No 1176/2011, the results of which were also published on 22 February 2017.[8] The Commission's analysis leads it to conclude that Sweden is experiencing macroeconomic imbalances. In particular, persistent house price growth from already overvalued levels coupled with a continued rise in household debt poses risks of a disorderly correction. Although banks appear adequately capitalised, a disorderly correction could also affect the financial sector as banks have a growing exposure to household mortgages. In such a case, there could be spill-overs to neighbouring countries since Swedish banking groups are of systemic importance in the Nordic-Baltic region. Awareness of mounting risks among the Swedish authorities is high, and in recent years measures have been taken to rein in mortgage debt growth and increase housing construction. However, policy steps implemented so far have not been sufficient to address overheating in the housing sector. Overall, policy gaps remain in the area of housing-related taxation, the macroprudential framework, and in addressing bottlenecks for new housing supply as well as barriers to efficient usage of the existing housing stock.

(3) On 28 April 2017, Sweden submitted its 2017 National Reform Programme and its 2017 Convergence Programme. To take account of their interlinkages, the two programmes have been assessed at the same time.

(4) The relevant country-specific recommendations have been taken into account in the Member States' programmes for the European Structural and Investment Funds (ESI Funds) covering the 2014-2020 period. As foreseen in the legislation governing the ESI Funds,[9] where it is necessary to support the implementation of relevant country-specific recommendations, the Commission may request a Member State to review and amend its relevant ESI Funds programmes. The Commission has provided further guidelines on the application of those rules.[10]

(5) Sweden is currently in the preventive arm of the Stability and Growth Pact. In its 2017 Convergence Programme, the government plans to achieve a surplus of 0.3% of GDP in 2017 and to continue to meet the medium-term budgetary objective — a structural deficit of 1 % of GDP — throughout the programme period. According to the Convergence Programme, the general government debt-to-GDP ratio is expected to fall to 39.5% in 2017 and to continue declining to 31.4% in 2020. Robust economic growth and sound public finances are set to be the main drivers behind the declining general government debt-to-GDP ratio. The macroeconomic scenario

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7 SWD(2017) 92 final.

8 COM(2017) 90 final.

9 Article 23 of Regulation (EU) No 1303/2013 of the European Parliament and of the Council of 17 December 2013 laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund and laying down general provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund and the European Maritime and Fisheries Fund and repealing Council Regulation (EC) No 1083/2006, OJ L 347, 20.12.2013, p. 320.

10 COM(2014) 494 final.

underpinning these budgetary projections is plausible. Based on the Commission 2017 spring forecast, the structural balance is forecast to show a surplus of 0.4% of GDP in 2017 and a surplus of 0.8% of GDP in 2018, above the medium-term budgetary objective. Based on its assessment of the Convergence Programme and taking into account the Commission 2017 spring forecast, the Council is of the opinion that Sweden is projected to comply with the provisions of the Stability and Growth Pact in 2017 and 2018.

(6) Household debt has continued to rise from already high levels. Household debt grew by 7.1 % in 2016, approaching 86 % of GDP and about 180 % of disposable income, driven mainly by higher mortgage borrowing linked to continued house price rises. The distribution of debt levels has become increasingly uneven, with an elevated fraction of newly mortgaged households (16.4 % in 2016) borrowing as much as 600 % of their disposable income. The government has taken some relevant macroprudential measures — including the introduction of a new mortgage amortisation requirement in 2016 — but it remains unclear whether these will have sufficient impact over the medium term. In February 2017, the government launched a legislative process to enhance the legal mandate of the macroprudential authority, to ensure that in the future the authority can introduce potential macroprudential measures in a timely manner and use a wider range of tools. The legislative amendments are expected to be in force by February 2018. Adjusting fiscal incentives, for example by gradually limiting the tax deductibility of mortgage interest payments or by increasing recurrent property taxes, would help curb household debt growth, but the government has made no progress on this.

(7) Sweden has experienced rapid and persistent house price growth since the mid-1990s. House prices have continued to grow rapidly and persistently, especially in the main urban areas. Key drivers include generous tax treatment of home ownership and mortgage debt, accommodative credit conditions coupled with relatively low mortgage amortisation rates, and an ongoing housing supply shortage. This shortage is linked to structural inefficiencies in the housing market. Housing construction has continued to increase, but remains well below new construction needs. The government's 22-point housing market plan addresses some underlying factors for housing shortage, including measures to increase the amount of available land for construction, reduce construction costs and shorten planning process lead times. However, some other structural inefficiencies, including weak competition in the construction sector, do not receive appropriate attention. The housing shortage is exacerbated by barriers hindering the efficient use of the existing housing stock. Sweden's tightly regulated rental market creates lock-in and 'insider/outsider' effects, but no significant policy action has been taken to introduce more flexibility in setting rents. In the owner-occupancy market, relatively high capital gains taxes reduce homeowner mobility. A temporary reform of the deferral rules for capital gains taxes on property transaction was introduced, but this will probably have limited effect. Lack of available and affordable housing can also limit labour market mobility and the effective integration of migrants into the labour market, and contribute to intergenerational inequality.

(8) In 2016 Sweden had one of the highest employment rates in the EU (81.2 %), while recording one of the lowest long-term unemployment rates. However, challenges remain, such as integrating low-skilled people and non-EU migrants into the labour market and reducing the substantial employment gap for non-EU-born women. Sweden has made considerable efforts in the reception of asylum seekers and in the

integration of refugees and other immigrants. Further improvements appear possible as in 2016 only one third of participants to the introduction programme were in work or education 90 days after having completed the programme, and a comprehensive approach and governance on the corresponding recognition of qualifications are still missing.

(9) Basic skills proficiency of 15 year olds has improved after years of deteriorating performance, according to OECD's PISA 2015 survey. However, the proportion of low achievers is still around the EU average and the performance gap linked to the socioeconomic background of students has widened. The measures launched by the government to improve school outcomes and equity warrant close monitoring, together with the initiatives aimed at integrating newly-arrived migrant pupils into the school system.

(10) In the context of the European Semester the Commission has carried out a comprehensive analysis of Sweden's economic policy and published it in the 2017 country report. It has also assessed the Convergence Programme and the National Reform Programme and the follow-up given to the recommendations addressed to Sweden in previous years. It has taken into account not only their relevance for sustainable fiscal and socioeconomic policy in Sweden, but also their compliance with EU rules and guidance, given the need to strengthen the EU's overall economic governance by providing EU-level input into future national decisions.

(11) In the light of this assessment, the Council has examined the Convergence Programme and is of the opinion[11] that Sweden is expected to comply with the Stability and Growth Pact.

(12) In the light of the Commission's in-depth review and this assessment, the Council has examined the National Reform Programme and the Convergence Programme. Its recommendations made under Article 6 of Regulation (EU) No 1176/2011 are reflected in recommendation 1 below,

HEREBY RECOMMENDS that Sweden take action in 2017 and 2018 to:

1. Address risks related to household debt, in particular by gradually limiting the tax deductibility of mortgage interest payments or by increasing recurrent property taxes, while constraining lending at excessive debt-to-income levels. Foster investment in housing and improve the efficiency of the housing market, including by introducing more flexibility in setting rental prices and revising the design of the capital gains tax.

Done at Brussels,

For the Council
The President

[11] Under Article 9(2) of Council Regulation (EC) No 1466/97.