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Productivity Growth in the Swedish Business Sector

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Summary

Since the Industrial Revolution, productivity growth among the developed nations has lifted millions of individuals out of poverty to prosperity. That is why it is worrying that productivity growth has tapered off in many countries over the past decade. Sweden is no exception. During the 2010s, Swedish productivity growth slowed down significantly, only achieving a third of the growth reached during the decade leading up to the global financial crisis of 2007–2010.

The so-called secular stagnation in terms of productivity growth we are currently witnessing is largely driven by factors shared by many OECD countries and which are difficult for individual countries to control. However, research also shows that there is a great deal of variation in productivity both between and within countries, not least in the business sector, which accounts for a significant portion of productivity growth. Hence, it is important to study productivity growth in the Swedish business sector over the past decades in more detail and not least which policy factors have played an important role in these developments. This is the purpose of this report.

The report begins by presenting a brief analysis comparing Swedish productivity growth with the OECD and Eurozone countries. Detailed administrative data on Swedish companies and employees are then used to study productivity growth in the Swedish business sector. There is a particular focus on the process of creative destruction, in which efficient companies grow and outcompete less efficient ones, and where the workforce subsequently moves to the growing companies. The report concludes with a policy analysis based on its empirical results and the research literature in the field.

Our overall assessment is cautiously positive. Compared to other OECD countries, the Swedish business sector exhibited relatively good productivity growth from the turn of the century until the financial crisis, after which several years of weak productivity growth followed. It has since improved in recent years, even though it is not as strong as before the financial crisis.

The creative destruction process has been less dynamic over the last two decades compared to the 1990s. During the 1990s, productivity in the business sector was largely driven by the entry of new productive companies and the exit of less productive ones, but this process has been weaker in the past decade. Since the financial crisis, productivity growth is instead driven by incumbent firms increasing their productivity. This so-called within-firm effect has been particularly noticeable in the manufacturing industry. Furthermore, the bulk of the within-firm effect comes from productivity growth in companies changing ownership (i.e., being acquired). In fact, roughly half of the total productivity increase in the Swedish business sector during the period 2000–2021 was created in such companies.

There are significant differences in productivity growth between different industries and over time. For example, in the finance and insurance industry, as well as the education industry, productivity growth is weak, while the real estate industry exhibits very weak growth. At the same time, the construction and information and communication industries have achieved very high productivity growth. The difference in productivity between the most and least productive companies has also increased during the period 1998–2021.

The workforce overall tends to move from less productive to more productive companies. It is more common that individuals having recently studied or changed profession move from less to more productive companies compared to individuals not having done so. This pattern is the most prominent among younger employees but is also visible among older ones. The most productive companies have a higher proportion of highly educated workers, but also high proportions of employees with upper secondary school degrees.

The Swedish business sector has become increasingly intangible. The share of intangible investments has in recent decades increased from about 12 percent of the value added to just over 16 percent, while

tangible investments as a share of value added have remained stable at about 13 percent.

Based on the empirical analysis and the relevant research literature, the report highlights five possible areas in which to implement policy reforms.

Protect the creative destruction process: improve competition, flexibility, and neutrality in the product market

The Swedish productivity-generating creative destruction process was enhanced when a series of micro-based policy reforms were implemented in the late 1980s and early 1990s. Up until the financial crisis, this enabled Sweden to exhibit very strong productivity growth from an international perspective. In an increasingly geopolitically uncertain, complex, and technology-based business world, with high demands regarding the ability to flexibly adapt production, the importance of well-functioning competitive conditions in the product markets becomes even more crucial with regard to efficient productivity growth in the business sector.

Based on this, we argue that it will be increasingly important to ensure that the Swedish Competition Authority has sufficient resources to uphold competition in the business sector. Sweden should also seek to ensure that competition rules are effectively applied in the international arena. This is to prevent Swedish companies from being disadvantaged by global super companies or companies with strong ties to the state in non-democratic countries abusing their dominant position in the world market.

Improve efficiency in institutions that stimulate research, development, and commercialization in the innovation market

The main market failure characterizing the innovation market is that research and development (R&D) and commercialization are associated with strong positive externalities on consumers and other companies. A well-functioning intellectual property system in the form of patent and trademark protection, which ensures that companies get

a return on their investments, may increase the incentives to invest in R&D and is thus crucial for high productivity growth in the business sector.

Industrial policy is sometimes associated with regulatory failures. That is why the risk of such regulatory failures should be taken into account, especially in the case of large industrial policy initiatives. Hence, we propose that Sweden mainly advocates an innovation system with more general tax reliefs in connection with R&D rather than more targeted industrial policy R&D initiatives in Sweden and the EU. That said, targeted support may be appropriate in order to support broader technology initiatives where there is an obvious market failure, such as in the case of carbon dioxide emissions.

Improve and adapt the financial market to a more intangible business sector

In the market for corporate financing, investors commonly know less than owners and management when it comes to a company's operations and viability. Well-functioning financial markets in which regulations are designed to reduce such asymmetric information problems are crucial for productivity growth in the business sector.

The empirical analysis in the report shows that the Swedish business sector has become increasingly intangible and that most investments in the business sector are now intangible. This likely means that venture capital and stock markets will play a larger role in corporate financing in the future.

Furthermore, it is likely that access to large capital markets will become more important in terms of financing large companies with a high proportion of intangible assets. The competitiveness of Swedish companies would thus benefit from having access to a more extensive stock market and venture capital market.

Possible reforms to address this development include increased neutrality between loan and equity-based financing or reducing the tax on long-term savings in the stock market. Furthermore, Sweden should work toward continued integration and efficiency in the EU's capital market.

Advocate a regulatory system more oriented toward productivity and commercialization

Regulations represent means for the state to mitigate various market failures and are intended to protect employees, consumers, owners, and the public. However, regulations also increase the costs for companies, both in terms of increased direct operating costs associated with adapting their operations and costs for increased uncertainty associated with investments.

Regulations in the business sector are associated with regulatory failures in the form of coordination failures between the areas of responsibility and objectives of various government agencies and between government agencies and companies. An increasingly geopolitically uncertain world and the emergence of a more complex, digitalized, and AI-based business sector means that regulatory coordination and management of asymmetric information problems in the regulatory system are expected to play a greater role in the business sector.

Therefore, we propose policy measures focused on reducing asymmetric information problems in the regulatory system and reducing coordination problems between different government agencies. Another possible approach is to introduce productivity as an objective for government agencies so that they internalize socio-economic efficiency in their operations. Furthermore, so-called regulatory sandboxes, where companies can test new services and products on a small scale under a reduced regulatory burden, could reduce asymmetric information problems in the regulatory system, especially in times of technological breakthroughs such as AI. This is also likely a suitable policy measure in this environment.

Increase opportunities for continuous further training throughout the entire career of workers

The increasing geopolitical instability and rapid technological developments increase the need for flexibility among companies and the workforce. We advocate for measures aimed at facilitating the process of updating human capital throughout life in order to improve the workforce's ability to adapt to the changing needs in the business sector.

Part of this training may take the form of on-the-job training and education. However, in order to make sure that sufficient levels of training are provided in skills that are not company-specific, as well as to those not currently employed, we believe that the regular university system may play a role by increasing the availability of shorter supplementary education programs focusing on skills in high demand in the business sector. In order to ensure that the courses meet the needs of the business sector, it may be appropriate to give this sector some influence over the program content (e.g., by consulting industry organizations).

In order to limit the total cost of education for society – and individuals – it may in some cases be appropriate that the increase in human capital throughout working life takes the form of a redistribution of the total amount of education over the lifecycle rather than increasing the total number of years spent in education.

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