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Crisis and chance
How Sweden managed to saved its welfare system
and possible lessons for Germany

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Mr von Bredow, Ladies and Gentlemen,

I am very grateful for the kind words of introduction. In particular, however, I would like to thank the German Council on Foreign Relations for the invitation to speak to you here today.

First of all, I am naturally always pleased to be back in Berlin. But more than that, the topic I shall be initially speaking about and on which, I hope, we will have a lively discussion, is a matter of pressing concern. I am not a politician, you have learnt that from my curriculum vitae. I lead an international energy company - and for us, as I will be explaining in more detail - growth, ability to plan, prosperity and security are hardly any less significant than for companies in general.

My speech is concerned with crises, how to overcome the crisis, it is concerned with Germany, and it is concerned with my homeland, Sweden. All this is already there in the title. But I am concerned with something else again, and this is something that soon comes up if you continue thinking about the topic: Europe.

Ladies and Gentlemen,
Germany, once the country of the economic miracle, has become the sick man of Europe – a role played by the United Kingdom a few decades ago. Today this has long ceased to be a German problem. The intermeshing of our national economies has turned it into a European problem.

Sweden is currently involved in a heated debate on the introduction of the euro. Next weekend a referendum will resolve the matter, and it is a question

of how far it is still possible and permissible to go in Europe, in the European Union indeed, in going your own way.

This is Vattenfall

However, allow me first to present my company to you, at least in broad outline.

We are here in Berlin, and Berlin has been the headquarters of the German Vattenfall companies for a little more than a year. This is the location of Vattenfall Europe AG as the holding company for our German operations and this is naturally also the location of Bewag, which today is a wholly-owned subsidiary of our Group. So there is no lack of local involvement. And yet I know that there is still work to be done in this country to make our company better known.

Vattenfall is, quite simply, the Swedish word for waterfall.

The more than 90-year history of our company is based on hydro power. It goes back to the Kungliga Vattenfallstyrelsen, the “Royal Waterfall Board”, founded in 1909. In 1992 this became the public limited company Vattenfall AB – a fateful year for the Swedish economy and even more so for Swedish social systems.

With the opening of the Nordic energy markets in the mid-1990s, Vattenfall grew from a Swedish to a European energy company. In Germany, Vattenfall acquired the majority shareholding in Hamburgische Electricitäts-Werke AG in several steps, leading to the present-day Vattenfall Europe AG; in Poland, Vattenfall is the major shareholder in the energy companies EW in Warsaw and GZE in Silesia.

The Vattenfall Group is one of the largest energy companies in Europe and is the largest power generator in the Nordic countries. In the past year, we sold more than 188 Terawatt-hours, that is to say 188 billion Kilowatt-hours, of power and in doing so attained turnover of around 11 billion euro. We are the fifth-largest power generator in Europe and today employ more than 35,000 people.

Vattenfall was founded in Sweden. Today the market-place is Europe, and we regard our home market as being Germany, Poland and Finland, as well as Sweden.

Our vision

We at Vattenfall have a vision. It reads: Vattenfall – a leading European energy company.

What do we mean by that?

We naturally need a certain size to be able to be leaders. We have been working hard on that over the last few years. But leadership to me also means setting standards in the all-important areas of our industry. Whether it is in environmental protection, in service to the customer or in the social and economic service we provide, so to speak as a catalyst.

And we want to be a European business. That is more than just a geographical term. We are working intensively in a multinational group to establish a common identity with common values.

The strategy of growing outside the traditional market is by no means unique in our sector. The two large German competitors are also growing internationally. I can say with some pride that we have come a long way along this road and count ourselves among the front-runners.

Part of this success can also be seen in Germany, today the largest market for the Vattenfall Group. We have merged and restructured the companies we have acquired, under the name of Vattenfall Europe. This has led to a competitive energy business which today is the third-largest in the largest energy market in Germany - because that is what Germany is. And we are, as a survey conducted by the newspaper "Die Welt" showed last week, the largest industrial enterprise in eastern Germany and therefore a major factor for stability and employment in the Länder of the former GDR.

Energy and society

Ladies and Gentlemen, I owe you the explanation I promised earlier as to why the question of the restructuring of economic and welfare systems concerns me as the CEO of an energy corporation, whether here in Germany or in my homeland Sweden.

For me, the answer is actually quite simple: both, efficient welfare systems and efficient energy supply are signs of stability and sustainability. If they work and if they withstand stress, they are a manifestations of highly developed societies.

If they fall out of line, the welfare of everyone is at stake. Electricity, the precious noble form of energy, does not just enable us to use all kinds of comforts from toasters to air conditioning – electric power and its cheap and reliable availability are basic requirements for our societies to work.

This was recently made dramatically apparent to people in the north-east of the USA. Anyone can easily withstand an evening without television, but social life also suffered an involuntary outage. It was necessary to switch from "normal operation" to "disaster", and Bill Clinton's former energy adviser Bill Richardson made a stark judgement of the situation: "We're the world's greatest superpower but we have a third-world electricity grid".

Energy companies today are no longer simply "providers", but are in keen competition with the power product. It's good that that is the case. In Europe we have decided in favour of open energy markets. We believe that services can be provided better in a competitive setting. At the same time, however, the energy system has to look to the future.

As an energy company we bear long-term responsibility - even competition has done nothing to alter that. We already have to work on the solutions today so that the day after tomorrow we can offer our customers environmentally sound, but at the same time – and that tends to be overlooked – more reliable and low-cost energy supply. Only when we can harmonise these three aims will we really act sustainably, in my view.

But investments in power generating plants are costly, and they have a long time frame. In the past this was far easier for energy companies to calculate, because the costs (under the supervision of the authorities, of course), were passed on to the customers. Today, however, the price of the power product is formed on the basis of supply and demand. If demand declines, the price drops on the power commodity market.

In a competitive environment, recession and economic decline are also a problem for energy companies. This was shown, among others, by the example of VEAG, one of the predecessors of Vattenfall Europe. With a huge investment effort, the company modernised power generation in eastern Germany. When economic development fell substantially short of expectations in the Länder of the former GDR and the market was simultaneously opened up in 1998, the enterprise found itself under threat for a short time.

I hope you will forgive me this somewhat extensive preface. But I consider it important to emphasise this initial thesis: to the same extent that modern civilisation is dependent on efficient power supply, it is in the vital interests of the energy companies themselves that social and economic stability prevail. And that includes appropriate growth and sustainable social systems.

Do you know Sweden?

I assume there are a considerable number of frequent travellers in the room. Many of you will probably have been in Stockholm or Gothenburg at some time, you may even have had an opportunity to spend a few days out in the countryside.

If I do not ask you, my honoured audience, but the average German, I am convinced that the image of Sweden here in Germany is a good 10 to 20 years behind the reality.

Sweden, that's forests and lakes, elks and reindeer, and lots of other nature besides. Everyone knows ABBA and IKEA, the people are friendly, environmentally aware and mostly blond. Beer and wine are sold by the State itself and at such ludicrously high prices that even Germans lose their thirst for beer. And IKEA advertising would have people in Germany believe that we throw our Christmas trees out of the window on 6 January.

Obviously everyone thinks of the welfare state, which was invented in Scandinavia and which the German social democrats would like to have copied piecemeal in the 1970s. The State sees citizens throughout their lives with all the blessings social planners could think up, regardless whether they are desirable or sensible or not. All financed by horrific levels of taxation, in particular on anything that creates the impression of luxury. Astrid Lindgren, people know, once even had to pay 102 per cent tax.

So much for the clichés.

Not everything about the clichés is incorrect. Although the myth about Astrid Lindgren's taxation comes from the fable world of Pomperipossa in Monismania, a short story she wrote for a newspaper in 1976, Swedes really have long had to bear a higher tax burden than most of their European neighbours. In return, however, the State has much to offer. The consequence is that tax morality is better than in many countries with lower rates of taxation.

Sweden was not involved in the two devastating wars that laid waste the continent in the last century. So in the post-war period there emerged a country with a high level of prosperity, with prosperity fairly distributed among everyone. Sweden – a country with good quality of life. At the same time, a country which in the Cold War did not join any of the major blocks, is not a member of NATO and did not become a member of the European Union until 1995.

And naturally Sweden still has a functioning social system today. Again today!

Because at the start of the 1990s the “folkhem”, the all-embracing social state which Sweden had created had reached its limits.

In the autumn of 1992 the crisis peaked and the country was in danger of collapse. "94 days that shook Sweden" was the heading in the newspaper Dagens Nyheter in a historical retrospective last year.

What had happened?

The road to crisis

Imagine that the base rate was raised tomorrow to, let us say, 20 per cent. That sounds good for savers, but for anyone who has to finance investments it would be pure horror. But at the beginning of September 1992 that actually was the interest rate in Sweden.

And it became far worse than that.

The storm clouds had been gathering since the 1970s. However, reforms were delayed, too much tinkering went on. Since the early 1970s, the Swedish krona had lost an astonishing 90 per cent of its value in comparison with the rest of Europe.

The recession worsened in the early nineties. Between 1991 and 1994 alone, 450,000 people lost their jobs, in a country which, it should be noted, only has a population just over a tenth that of Germany. The government budget showed a deficit of up to 13 per cent. The Swedish economy was sliding into bankruptcy.

It was finally 16 September 1992 that entered Swedish economic history as “Black Wednesday”.

In the days leading up to that Wednesday, billions had been flowing out of the country, and when Bengt Dennis, head of the Swedish central bank, began morning discussions at 7 a.m., it was clear that something dramatic had to be done that very day. And so the bank base rate was set at an incredible 75 per cent.

The interest-rate shock

75 per cent!

And yet no success was achieved! Capital continued to flow out of Sweden unabated. In the afternoon the head of the central bank had to act, and used his authority to raise the interest rate once more.

At 3.20 p.m. on 16 September 1992, the base rate stood at 500 per cent.

Five hundred per cent. This crazy figure, the ultimate sheet anchor of monetary policy, perhaps demonstrates most clearly that Sweden not only faced problems but faced the severe economic crisis since the 1930s.

Something had to change, and quickly.

Crisis pact

Something did happen, and it happened the same day. The prime minister Carl Bildt, who at that time was leading a centre-right coalition, promptly asked the Social Democrat Ingvar Carlsson to return from his trip abroad at once.

Consensus is regarded as very important in Sweden. And so it was characteristic that in the country's hour of crisis the government and opposition turned overcoming the crisis into a national issue. Much of what was fundamentally changed in Sweden could only be imagined in this special constellation.

As little as four days later, on 20 September, the centre-right government presented crisis package 1 together with the Social Democrats. The base rate was brought back down from 500 to 50 per cent. The crisis package envisaged spending cuts of around 18.9 bn kronor, and additional revenue of 8.7 bn, but at the same time relief amounting to 6.5 bn kronor. The bottom line figure was savings of 30 bn kronor.

At the same time, the central bank carried on with its interventions on a large scale. Capital nevertheless continued to flow out of Sweden.

On 30 September a new crisis package was adopted. On 1 January 1993, employers' contributions were reduced by 4.3 per cent, two public holidays were done away with and value-added tax on foods was increased. At the same time, income tax allowances were decreased by 2500 kronor. Altogether, the package brought about cost reductions of around 4 per cent in the economy and in so doing made a considerable contribution to increasing competitiveness. The base rate was lowered to 24 per cent.

Slowly capital came back into the country as well. However, when the interest rate was reduced to 11.5 per cent again in November, the outflow of

capital started afresh. After a few vain attempts by the central bank to defend it, the Swedish krona finally became freely convertible on 19 November and was no longer supported. This meant a sea change in Swedish monetary policy: the interest-rate target was replaced by an inflation target.

Reconstruction and reform

A first step had been taken with the crisis packages. Under the still fresh impression of the crisis, however, Sweden tackled the extensive reconstruction of its economic and social system. Many measures could be enumerated, but the following appear to me to be most important:

- * Consolidation of government finances: The budget was improved half by savings measures and half by higher taxes and charges. Many subsidies were abolished. Since 1998 the state budget has been in balance again and is even showing a surplus.

- * Reconstruction of the pensions system: Since 1999 there have been two parallel pensions systems in Sweden. The old system is based on a general basic pension plus an income-linked additional pension; the new one contains a pension calculated from life-time income, plus a compulsory premium pension with individual accounts. Everyone can decide here about their investment risk for themselves. The relationship between contributions paid in and pension paid out has a greater impact than in the past. Someone who wishes to retire at the age of 61 is free to do so, but he only receives 71 per cent. Someone who works until the age of 67 can increase his pension by up to 120 per cent.

- * Adjustment of social-security benefits: Occupational health insurance benefits were reduced from 100 to 75 per cent. And in unemployment insurance, which is the responsibility of the trade-union unemployment schemes, contributions were slightly raised and benefits slightly reduced.

At the same time as government finances were being reorganised, the Swedish economy underwent a fundamental structural change. Although Sweden is still an industrial nation, its international competitiveness today is largely based on its leading position in information technology. Sweden leads the world in use of the Internet and mobile phones.

Knowledge transfer from science to industry works thanks to close co-operation between universities and businesses. And education policy has created the necessary conditions for that to be possible. The proportion of students completing upper secondary education is now 95 per cent, and Sweden comes near the top in the Pisa study.

Sweden today

How is Sweden placed today?

I would like to illustrate with some outline data how Sweden in recent years – in a world economic climate that is not exactly rosy - has developed strongly.

For 2003 we currently anticipate economic growth of 1.3 per cent, and for the coming year we expect the economy to grow by 2.5 per cent. That is not too spectacular, and entails a danger of a possible rise in unemployment. But, please note, all this in an environment in which other national economies are contracting or stagnating.

Unemployment in Sweden stood at 5 per cent in July. It is uncertain, however, whether the government will attain the employment target of 80 per cent of the working population in the coming year.

It also seems to me to be worth noting that labour costs in the period 1991 to 2001 rose considerably less in Sweden than, for example, in Germany. This is obviously largely due to the dramatic devaluation of the krona in the first half of the 1990s. Nevertheless, while costs for one hour of work in Sweden between 1991 and 2001 rose from 134 to 192 kronor, Germany recorded a rise over the same period, expressed in terms of Swedish currency, from 137 to 245 kronor.

And Germany....?

How are things in Germany, Ladies and Gentlemen? The answer to that question is perhaps the most delicate part of my speech. Because despite all the affirmations of European co-operation, a foreigner coming along with advice on reform and economic development is still regarded with suspicion.

That is in no way my intention. Nor does it appear necessary to me to speak at length about the current crisis in Germany in this room. Everyone, I imagine, is aware of that.

Instead, here are some thoughts from someone who is completely beyond suspicion of being a foreign know-all. I quote from an interview with a newspaper:

Quote: "Modern policy on fairness means a first-class educational policy, and that means at the same time and with full emphasis the best possible support for everyone, including support of top-level performance, without obstacles. We - Germany is meant here - always spend too little money on education and research." And again: "If we want to maintain the present standard of

living in Germany, we must be guided by Sweden. The structures of the education system and the organisation of science there are exemplary."

The person handing out those compliments is none other than the German minister of economic affairs, Wolfgang Clement, just over three weeks ago in an interview with *Wirtschaftswoche*. His compliments were not just directed at Sweden.

In response to the follow-up question whether the continuing theme of the German reform agenda should be looked up in Stockholm, the minister replied: "Not only there. Where the labour market is concerned I look towards the United Kingdom. For more than two years this country has been showing us what good employment finding should be like and what it will soon will be like here. When it comes to flexibility in the labour market, the Netherlands has the best practice. We can learn from many different countries."

Lessons learned

I must say, I am very pleased with this. Wolfgang Clement does not just think as a German minister of economic affairs – he thinks as a European.

Because it can only be about that: joint learning. Anyone who understands Europe knows that it cannot be a case of everyone doing the same thing. Germany is too different from Sweden to simply take over solutions piecemeal. Nor can that be done with the Dutch neighbours, and even less so with the United Kingdom. But it should not, in either direction, stop us from learning from one another.

What can be learned from the way in which Sweden has overcome its crisis?

Three lessons occur to me:

Openness: By that day of 16 September 1992, the glossing-over of problems in Sweden had come to an end. It was now clear to everyone how drastic the economic situation was. That it was not a dip in the economic cycle. That the fault lines ran far deeper. This sober assessment was necessary in order to bring about fundamental changes. Only in such a situation, where it is clear to everyone that things cannot continue the way they are, it is possible to set about slaughtering sacred cows. That is the real opportunity in the crisis: to tackle all those problems which were all too willingly allowed to continue to exist in times of pleasure. If necessary, to be cruel as well.

In Germany, Ladies and Gentlemen, despite the writing on the wall, I do not yet see this awareness of crisis. All the camps are continuing to do their own

thing, senseless strikes are suddenly called as a trial of strength and there continues to be a lack of appreciation of the real need for reform.

Fairness: The reconstruction of the economic and social system will only succeed if it is done in a fair and comprehensible way. That was particularly important to us in Sweden. Anyone who can contribute more must also contribute more. But even someone who can contribute little has to provide his part. In Sweden the situation was roughly that the 20 per cent of households with the highest income had to bear 40 per cent of the additional household burden, while the 20 per cent of households with the lowest income still contributed 10 per cent. However, fairness can also mean generational fairness and mean that spending on education is actually increased - so that the young generation have their fair chance and society preserves its capability to manage the future.

The harmonious agenda: Tackling the taxation system today, the pensions system tomorrow and the healthcare system in a year does little to help. The reconstruction can only succeed if it is guided by an overall concept. It must be clear to everyone that it is not possible to take out one part of the reform agenda and put it off until some vague date in the future.

And Europe...?

Ladies and Gentlemen, as I mentioned at the beginning, I do not actually wish to speak to you just about Germany and Sweden, but rather about Europe.

In five days, Swedes will be voting on whether to introduce the common European currency, the euro. The public debate has been going on for weeks, and the arguments on both sides have been sufficiently exchanged. And let me say that many of the arguments of the No camp are eerily reminiscent of the debate on whether Sweden should join the common Europe at all.

What we see in particular, however, is that the economic situation in Germany – and in France and Italy too - has a direct impact on the debate in Sweden. Those who speak out against the euro in Sweden like to draw attention to the situation in Germany to say: "Look, that's what's they've got for giving up the deutschmark." As easy to see through, as foolish as these arguments are, they do have an impact. This is the background to why the Swedish prime minister Göran Persson in the past week scolded Germany, Italy and France, creating headlines here in Germany.

If we declare ourselves for a common Europe, Ladies and Gentlemen, we also have to understand that the mistakes a country makes have to be ironed out by everyone. That is the idea of this self-elected community.

There are opportunities to learn from one another, Ladies and Gentlemen, in both directions. I would like to take an example from the energy sector of how Sweden is currently taking Germany as a model. As far as I know, this is not realised at all in this country. I am talking of the abandonment of nuclear energy.

Even earlier than Germany, Sweden took a political decision in the early 1980s to abandon nuclear power, but implementation of this political decision has not yet been completed between the government and the nuclear power operators. Negotiations begin in the autumn, and it is hoped that a result according to the "German model", according to the model of the German nuclear consensus, will be found.

I do not wish to be misunderstood: as the largest Swedish energy business we consider the premature shutdown of nuclear power plants to be a wrong decision. But in Germany the nuclear consensus has achieved at least two things: firstly certainty of planning for the operators, which at present is lacking in Sweden, and secondly de-emotionalisation of the debate, so that here, as I read with great interest, the future option of nuclear energy can at least be openly considered again.

One last point: Europe means common learning! And I therefore hope that my speech has provided you some new insights, and I look forward to your comments and questions and to an interesting discussion with you. Thank you very much.