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The Myth of Nordic Socialism

By Rainer Zitelmann April 3, 2019 9:00 a.m. ET

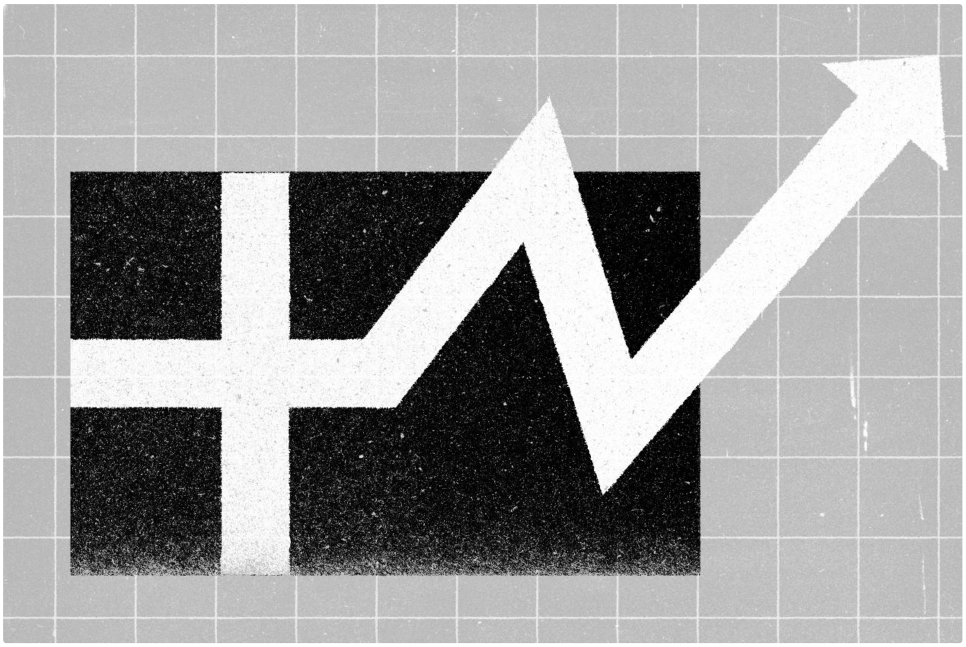

Illustration by Robert A. Di Ieso

Polls tell us that 20-somethings today feel better about socialism then they do about capitalism. Among those reclaiming the term are supporters of Jeremy Corbyn in the U.K. and Bernie Sanders in the U.S. To them, socialism doesn't mean a state-controlled system like the one we saw in the old Soviet Union, but the dream of a "democratic socialism" based on the Nordic model. But their dream is based on a big misunderstanding.

Although there are areas—especially in taxes and labor market regulation—where socialist elements still exist in the Nordics, the region is by no means socialist today. In fact, according to the Heritage Foundation's index of economic freedom, Sweden, Norway, Finland, Iceland, and Denmark rank among the 30 most capitalist countries in the world.

The image of the Nordic countries as strongholds of socialism is outdated, harking back to the 1970s and 1980s. To see how things have changed, let's take a closer look at one: Sweden.

In the late 1960s, Sweden's government spending was in the same ballpark as other OECD states. This changed starting in the late 1960s. Between 1965 and 1975, the number of civil servants grew from 700,000 to 1.2 million, alongside increasing government intervention in economic affairs and the creation of a number of new regulatory authorities. Between 1970 and 1984, the public sector absorbed the entire growth of the Swedish workforce, with the largest number of new jobs created in social services.

In 1960, for every 100 "market-financed" Swedes (i.e. those who derived their income predominantly from private enterprise), there were 38 who were "tax-financed" (i.e. dependent on the public sector for their income, whether as civil servants or as recipients of payments from the state). Thirty years later, that number had risen to 151—in other words, there were significantly more people living off of the state than paying into the system. This reflects Sweden's move away from a capitalist free-market economy to a socialist model.

This damaged the Swedish economy and resulted in prominent entrepreneurs leaving the country in frustration. IKEA founder Ingvar Kamprad, for example, moved to Denmark in 1974 and later to Switzerland. The economic situation in Sweden deteriorated as a direct result of extreme labor market regulation and the constant expansion of the role of the state, which led to massive dissatisfaction among the population.

Pushback against these socialist ideas gathered momentum, and by the 1990s there was a comprehensive counter-movement that—without fundamentally questioning the Swedish model of high taxes and comprehensive welfare benefits—nevertheless eliminated many of its excesses. A major tax reform in 1990/91 slashed corporate taxes from 57% to 30%. Income from shares was exempted from taxation, while capital gains from shares were taxed at only 12.5%.

The top marginal income-tax rate was set at around 50%, a reduction by 24 to 27 percentage points for the majority of the workforce. The proportion of earners taxed at a marginal rate of over 50% dropped from over half to only 17% paying income tax to the central government.

The reforms continued over the following years: in 2004, the estate tax of up to 30% was scrapped. Today, there is no estate tax in Sweden. The abolition of the wealth tax, which had already been cut, came into effect retroactively as of 1 January 2007. The corporate tax rate continued to decline, getting cut from 30% to 26.3% in 2009 and to 22% in 2013. Property tax rates were also cut substantially.

Between 1993 and 2000, social spending dropped from 22.2% to 16.9% of GDP, economic subsidies from 8.7% to 1.8% and public-sector payroll costs from 18.2% to 15.6%.

These changes have resulted in a drastic decline in equality. Sweden's Gini coefficient, which measures income distribution, grew by around 30% between the mid-1980s and the late 2000s. Only New Zealand recorded a similar growth in inequality during the same period.

Although contemporary Sweden remains a traditional welfare state in some respects (e.g. it has comparatively high tax rates), successive governments since the early 1990s have consistently chosen more freedom over more equality, more market over more state. Following the obvious failure of the socialist experiment, the balance between capitalism and socialism has shifted toward capitalism.

The conclusion: Why should countries like the United Kingdom or the U.S. make the same mistake as the Swedes did in the 1970s? Sweden's "democratic socialism" with high taxes, redistribution and high state regulation has failed, and the young people who are today enthusiastic about the ideas of Bernie Sanders should draw lessons from the experiences of Sweden and other Nordic countries.

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