

# Swedish Productivity: How Well Are Our Productive Resources Used?

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# Summary

Over the past two decades, productivity growth in many EU countries has slowed and fallen behind that of the United States and China. This slowdown constrains increases in real incomes and, according to some observers, may undermine Europe's ability to sustain its social model, characterized by strong welfare systems, individual freedoms, and environmental protection. The Draghi Report<sup>1</sup> states that unless Europe becomes better at translating its skilled workforce and innovative ideas into higher productivity, its economic foundations will weaken.

Sweden has also experienced this trend. GDP per capita has grown more slowly since the early 2000s than during the 1990s, a decade marked by the emergence of new firms and rapid innovation that led to major economic successes. In the 1990s, a large share of Sweden's productivity growth was driven by creative destruction: new, efficient firms entered the market while less productive firms shrank or exited. In recent years, growth has instead been driven mainly by improvements within existing firms rather than by the emergence of new ones.

## Declining firm dynamism

Our analysis, based on detailed Swedish firm-level data, reveals signs that the Swedish economy has become less dynamic. The share of new firms has fallen from around 7 percent in the early 2000s to approximately 3.5 percent by the late 2010s, and the share of firms exiting the

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1. Draghi (2024). The Future of European Competitiveness. European Commission report.

market has also declined. Fewer new firms grow rapidly in their early years—so-called “gazelles” or “unicorns,” which were previously more important for job creation and innovation. Worker mobility between employers has also decreased, particularly in manufacturing, which still accounts for a substantial share of the Swedish economy.

This pattern mirrors findings from other advanced economies: fewer firms are entering and exiting, fewer workers are changing jobs, and the economy is reallocating resources—capital and labor—more slowly. This slowdown in firm dynamism matters because it weakens the process by which resources move from less productive to more productive firms, thereby dampening aggregate growth.

## Understanding barriers to growth

Economists use the concept of “distortions” to describe factors that prevent firms from achieving a productivity-maximizing allocation of resources. These distortions can arise from many sources—regulation, taxation, market power, or uncertainty—and they constrain the growth of high-performing firms. Research on the French labor market, for example, shows that strict employment protection rules for firms with more than 50 employees discourage expansion, while similar studies from Sweden suggest that dismissal regulations affect hiring and worker mobility.

We use a well-established economic model to:

- a. measure the magnitude of the distortions faced by firms in Sweden
- b. estimate how much of productivity growth comes from improved resource allocation across firms
- c. assess how much productivity could increase if these barriers were removed.

Put simply, we compare firms’ actual size with the size they would have in a perfectly efficient market. When a firm that should be large remains small, or when an inefficient firm remains large, we infer the presence of barriers or distortions.

## Main findings

We find that improvements in how Swedish markets allocate resources—what economists refer to as allocative efficiency—have contributed less and less to productivity growth over time. In the early 2000s, improved allocation accounted for around 2.5 percentage points of annual productivity growth; by the late 2010s, this figure had fallen to about 1.5 percentage points. In manufacturing, improved allocation explains roughly one quarter of productivity growth, and in services nearly all of it—yet in both sectors this contribution has steadily declined.

This weakened reallocation is consistent with the broader decline in firm dynamism. It implies that high-performing firms face greater difficulties in expanding, while low-performing firms survive for longer. In industries such as hotels and restaurants, where productivity growth relies heavily on the entry of new and more efficient firms, this trend may be particularly concerning.

## Potential productivity gains

To assess the potential benefits of more efficient allocation, we simulate how much Swedish productivity would increase if all distortions to resource allocation were eliminated. Our estimates suggest that aggregate productivity could, in principle, rise by 30–60 percent, with the largest potential gains in manufacturing and knowledge-intensive service industries (20–60 percent and 20–35 percent, respectively). In sectors such as construction and tourism, the potential gains are smaller, at around 5–15 percent.<sup>2</sup>

Our results also indicate that Sweden’s most productive firms—those that pay higher wages, export, and employ highly skilled labor—are often held back by greater growth barriers. Despite being more efficient, they are not much larger in terms of employment than less productive firms. In other words, Sweden’s best firms are too small. This helps explain why fast-growing young firms (gazelles and unicorns) have become less common. Industries in which distortions have increased show a sharper decline in such firms.

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2. These estimates should be viewed as indicative, given the inherent uncertainty in such simulations.

## Who bears the cost?

Distortions affect many groups. Workers and owners of highly productive firms miss out on opportunities for wage growth and innovation. Consumers may face higher prices and fewer choices, as the most efficient producers are unable to expand and exploit economies of scale. Cities, where many of these firms are located, may also lose part of their growth potential.

## What might the measured barriers reflect?

The productivity trends we observe are present in many countries, suggesting that their causes are not uniquely Swedish.

Nor does our report aim to single out specific regulations as the source of these distortions. Many regulations exist for good reasons—to protect workers, the environment, or fair competition—even if they sometimes reduce productivity. The central policy challenge is instead to better understand where regulations may unintentionally hold back high-performing firms without delivering corresponding social benefits.

Possible areas for review include regulations in the construction and housing sectors that limit labor mobility, barriers to scaling up innovative firms, or labor-market rules that hinder expansion. Addressing such frictions could help revive the forces of creative destruction that once drove Swedish growth.

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Sweden's productivity slowdown reflects a weakening of the economy's ability to reallocate resources from less productive to more productive firms. Our results show that the economy has become less dynamic: fewer new firms are created, fewer old ones exit, and fewer workers change jobs. As a result, the most productive firms struggle to expand.

The potential gains from achieving efficient reallocation are substantial—up to 60 percent higher productivity in some industries. Realizing these gains requires careful policy design: removing unnecessary barriers while preserving the social and environmental objectives that are central to Swedish and European values.

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