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Center for Economic Policy Analysis

**Flexibility, Employment Development and Active  
Labour Market Policy in Denmark and Sweden in the 1990s**

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# **Flexibility, employment development and active labour market policy in Denmark and Sweden in the 1990s**

*By Peter Plougmann (Oxford Insight) and Per Kongshøj Madsen (University  
of Copenhagen)*

*Third draft, November 2001*

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## 1. Introduction

A first look at the economic development in Denmark and Sweden in the 1990s tells a story of two countries with somewhat different experiences. Denmark has been chosen as one of the "European Tiger Economies" to be included in a recent ILO study of successful small European economies together with Austria, Ireland and the Netherlands (Auer, 2000). At the same time, Sweden has been used by neo-liberal opponents of the Scandinavian Welfare State Model as the final evidence of the collapse of this model. However, a closer look reveals a somewhat more complex account. Sweden has actually done better than its reputation leads to believe and Denmark might be less of a success story. But taken together they represent some of the bolder and more promising political strategies in Europe in the late 1990s.

Both countries have a history of a well-developed welfare state system and a high level of social cohesion. Both countries have also suffered from serious unemployment problems and both have by 2001 regained an internationally low level of unemployment and high level of employment. Furthermore, both countries have embraced the possibilities offered by the so-called "New Economy" and are in the process of turning themselves into economies depending on knowledge-intensive industries and leaving traditional modes of production behind them. Lots of public and private attention has been and continues to be paid to the education and training of the labour force with an emphasis on life-long learning and focus on broad competences developed by all employed and jobseekers alike. Finally, both countries are well known for their very elaborated Active Labour Market Policy (ALMP).

The macro-economic environment in Denmark and Sweden in general is characterised by low inflation, low interest rates, moderate wage growth and consolidated government budgets. The improvements in labour market conditions have taken place without any increased wage and income differentials and without any reduction in the compensation rate (unemployment benefits and/or social security). In addition, the high utilization of the labour force has been achieved without any significant decline in the well being of the people. The general social security system, for which the Scandinavian model is so famous, has been maintained throughout the 1990s. It has been possible to combine low unemployment with a relatively high compensation rate. The resulting structural improvements are primarily attributable to the ALMP, which has been successively adjusted to meet the changing demands and focuses of the labour market in both countries. The Danish case even makes it possible to argue that the equilibrium rate of unemployment (or the NAIRU) has decreased significantly. This might be due to the effects of the ALMP.

It is important to note that these recent developments have taken place without changing the fundamental characteristics of the Scandinavian Model: high tax rates, a comprehensive social security system, a universal unemployment insurance benefit system and some of the lowest degrees of wage and income inequality in the world (Kvist, 2000). It is true that some changes have taken place. Thus the principles of new public management have been introduced in the large public sectors. One also observes some decline of corporatism and an extension of decentralised steering based on market mechanisms rather than on regulation by central authorities. These changes, however, can

just as easily be interpreted as rational political adjustments aimed at adapting the social institutions to the new global economic and social conditions of the 21<sup>st</sup> century. The governments of Denmark and Sweden have reflected on the recommendations of the OECD Job Study, but have far from applied them all. Politically, the modernization of the Scandinavian version of the welfare state has been given priority. This article does not advocate that what has happened is the realisation of the "Third Way", but it might be quite close.

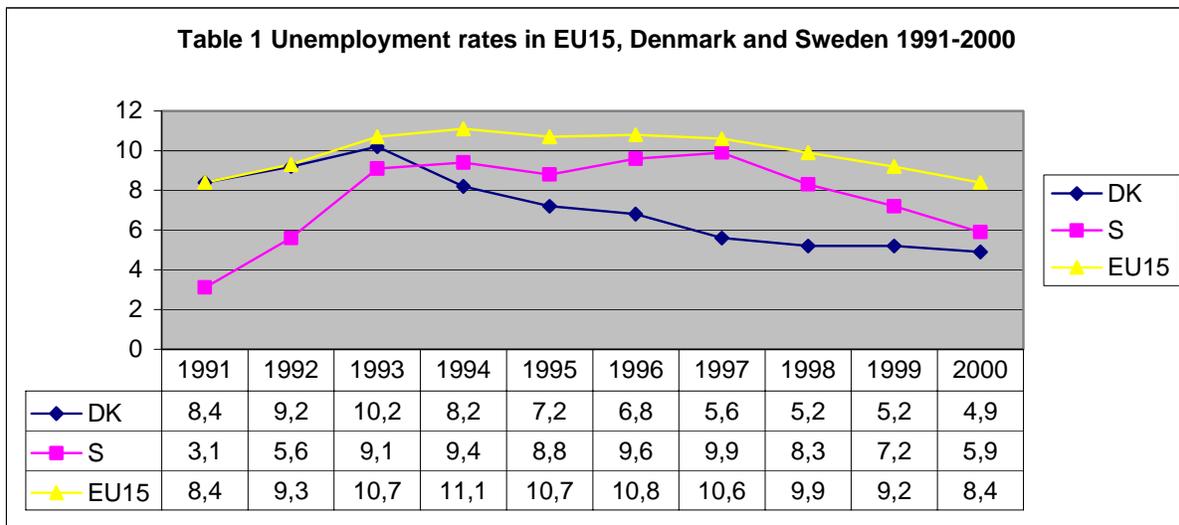
This article will describe the development of the labour market in the two countries and discuss to what extent the recommendations of the OECD Job Study have been applied in Denmark and Sweden. We will try to illustrate the significant national features of the ALMP in order to evaluate the potential impact of the policy on the functioning of the labour market. Then the dynamics behind the positive employment development will briefly be discussed. Finally, we will look ahead and pinpoint some future problems of the national labour markets that may have to be reflected in a modernized ALMP.

## 2. Main characteristics of the labour markets in the two countries

Both Denmark and Sweden experienced high levels of unemployment in the beginning of the 1990s. However, since 1993/94 Denmark has gone through a remarkable recovery. The same has been the case for Sweden since 1997. For both countries the outcome in recent years has been high levels of labour force participation rates and a low level of unemployment.

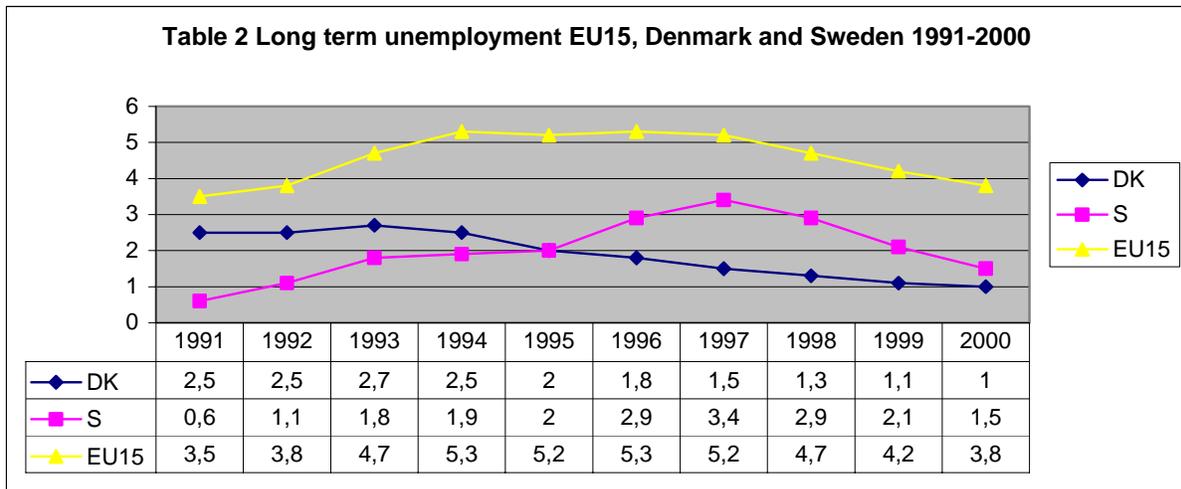
### Unemployment

As shown in table 1 below, unemployment in Denmark and Sweden is considerably lower than the average in EU15.



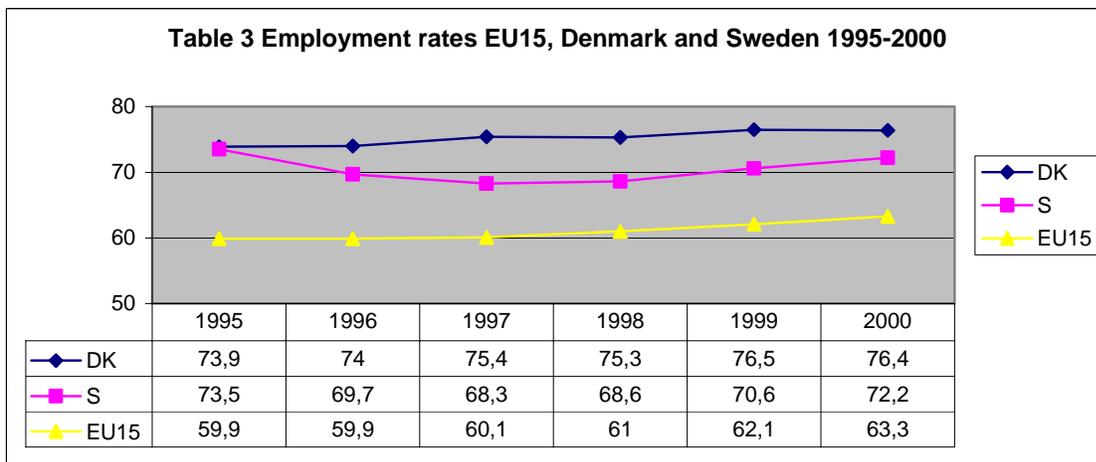
Unemployment in Denmark has more than halved in just five years and is currently among the lowest in Europe, coming close to the level of the US<sup>1</sup>. Especially the reduction of youth unemployment is impressive by international standards. The development of open unemployment in Sweden has been more turbulent, moving from 2.5-3 per cent before 1991 to a peak of approx. 10 per cent in 1997 and down to less than 4 per cent 2001. Concurrently with the decline in general unemployment, both countries have succeeded in reducing the level of long-term unemployment. Denmark succeeded earlier than Sweden, which had to go through a rough period of readjustments before being able to combat long-term unemployment very effectively in 1997.

<sup>1</sup> Benchmark report



## Employment

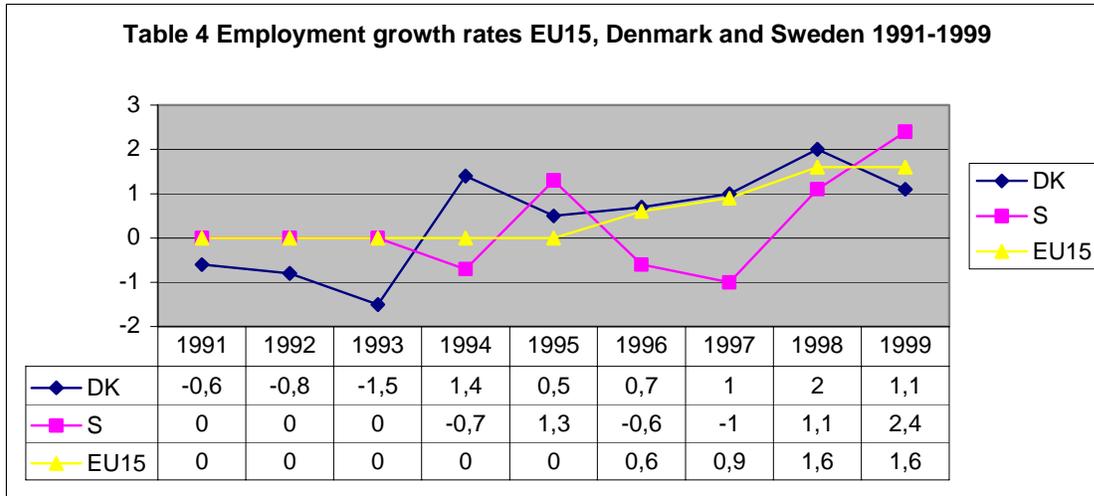
The employment rates of both Denmark and Sweden are currently some of the highest in the EU.



In Denmark the labour force participation rate and employment /population ratio are among the highest in the world indicating a strong utilization of the existing and the potential labour force. The comparatively high aggregate employment rate is due in particular to high employment among the young and prime age women.

Sweden did indeed lose some of its economic strengths during the 1990s. In the years following 1991 Sweden lost more than 600,000 jobs due to a dramatic setback in general demand. Labour force participation has traditionally been high in Sweden. But Sweden

no longer stands out internationally in this respect. Few hours worked and absenteeism have reduced the effective utilisation of labour by 17 per cent over the past three decades. The employment growth rates have fluctuated heavily in the 90s, especially in Sweden (table 4).



However, since 1997 Sweden has experienced strong growth rates in employment allowing Sweden to surpass Denmark and EU15 in 1999. Sweden has tended to stay strong in 2000 and 2001 although the recent downturn in 2001 of the ICT industry has resulted in massive job cuts.

Job growth in Denmark has been less than the OECD average. Even if the reduction in unemployment in Denmark has been impressive, it does not reflect an equally impressive growth in employment. The increase in new jobs has been lower than what is apparent in other OECD countries (International Employment Ranking 2000, *Bertelsmann*). On average, in the last five years there has been a net increase of 1.4 per cent more jobs p.a. in Denmark. The average for 21 OECD countries has been 1.5 per cent in the same period. Countries such as Holland, Ireland and Spain have had much larger increases, in Ireland approx. 5.5 per cent p.a.; in Holland and Spain 2.7 per cent and 2.8 per cent new jobs, respectively.

Sweden tends to have a more impressive job record than Denmark. According to the labour market authorities in Sweden the development on the labour market is exceptionally positive and jobs are being created more quickly than they have been since the end of the Second World War.

During 1998 and 1999 employment increased by a total of 146,000 jobs and for 2000 and 2001 the labour market authorities predict an increase of 86,000 and 77,000, respectively, which means a total increase of 309,000 jobs over 4 years. This means that almost 60 per cent of the jobs lost at the beginning of the 1990s have been regained.

Employment in Sweden has especially increased in the private service sector in recent years. This means that approx. 70 per cent of the total increase in jobs in the country has been provided by the private service sector. The same development can be seen in Denmark.

The low level of unemployment and the high level of employment in both countries imply that any additional growth in employment will have to be based on a net increase of people entering the labour force. Much of the net increase is, due to the demographic constraints of a negative reproduction rate and a general greying population, to come from immigration. This, however, is a highly politically controversial issue in both countries.

### **The flexibility of the labour market**

Labour market flexibility is essential to the long-term success of national economies.

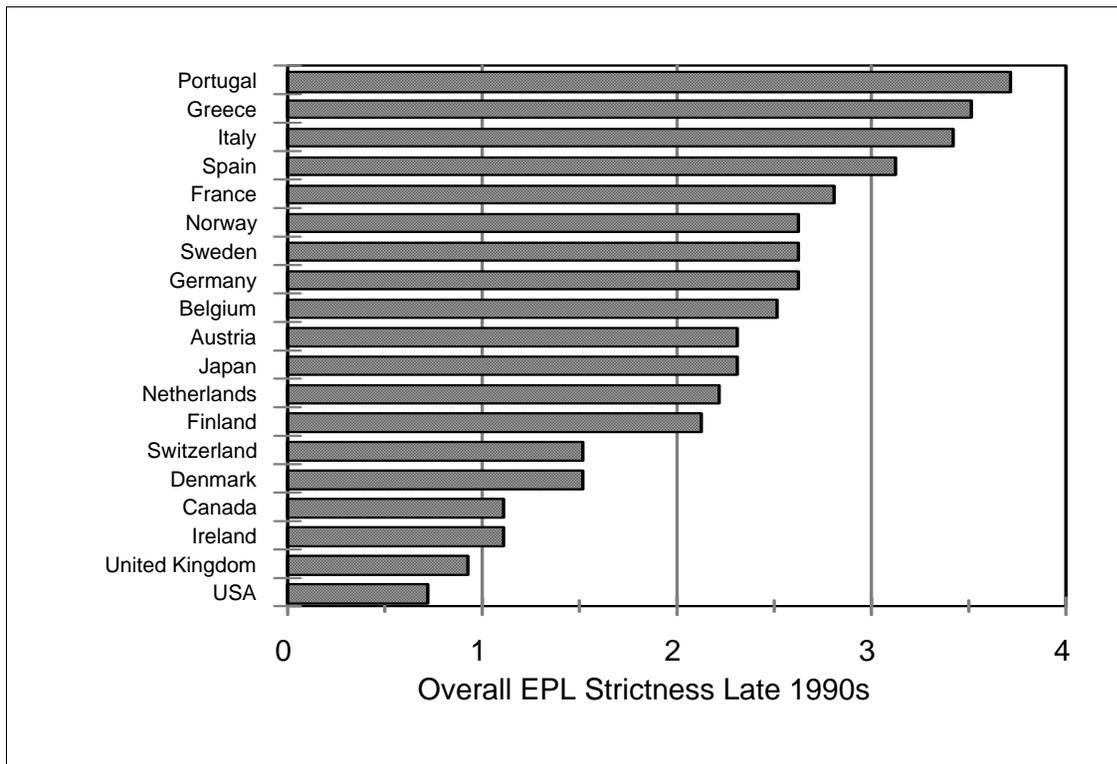
However, it is necessary to understand the concept of flexibility properly. All too often the demand for flexibility only takes the short-term interests of the employers in flexible labour costs into account, leaving out the long-term collective interest in a high level of both numerical and functional flexibility.

The level of labour market flexibility can be described using a number of indicators such as:

- the level of employment protection legislation and working time regulation
- the actual level of working time flexibility and level of labour turnover across sectors and industries
- the level of functional flexibility identified in studies of work organisation
- the level of long-term unemployment and mobility between different levels of attachment to the labour market

We have already proved that long-term unemployment has decreased significantly in both countries. If we turn to the other indicators, data from Denmark clearly give the impression of a very flexible labour market, while the picture for Sweden is more mixed.

First, when the level of employment protection legislation is examined, information can be gained from a recent OECD study (OECD, 1999), cf. figure 1. As it is evident from the indicator in figure 1, Denmark shows a low level of employment protection compared to most other industrialized countries - and much lower than the other Nordic countries including Sweden, with whom Denmark is commonly grouped as an example of the Scandinavian welfare model.



*Figure 1: Overall strictness of the employment protection legislation (EPL) in the late 1990s. Average indicator for regular contracts, temporary contracts and collective dismissals. Source OECD (1999), table 2.5.*

The low level of employment protection in Denmark is associated with a high level of numerical flexibility measured by labour turnover of more than 20 per cent p.a. International statistics on labour turnover are not available, but recent studies from OECD and ILO show that average job tenure in Denmark is among the lowest in Europe and is on the same level of that found in the UK and the US, cf. figure 2. Again, Sweden is located at the other end of the scale with a level of job tenure similar to Japan and Greece. More detailed studies show that the high level of labour mobility in Denmark seems to be a phenomenon that is widespread across sectors including the public sector (Bingley et al, 1999).

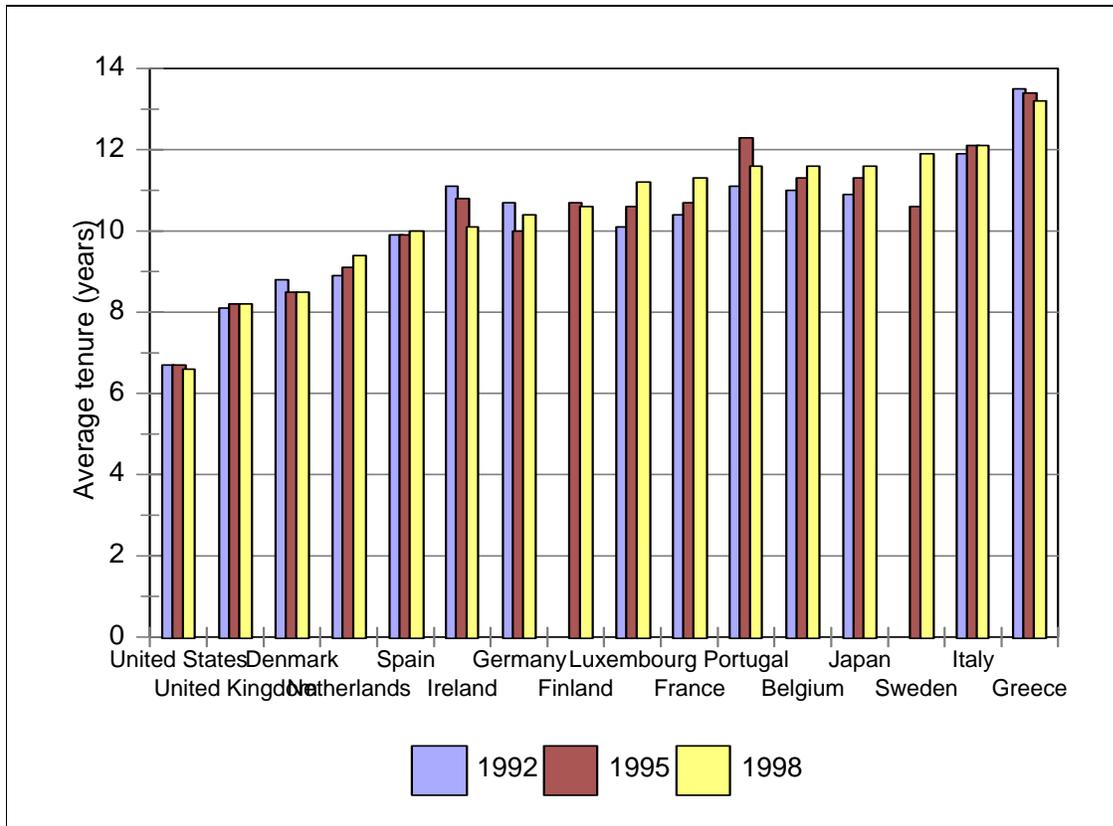
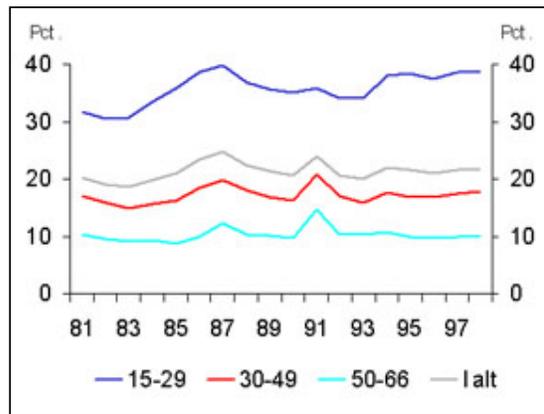


Figure 2: Average tenure in years for employees in a number of OECD countries, 1992-1998. Source: Auer and Casez (2000).

A high level of mobility of employees between different workplaces and industries is an indicator of an effective labour market where the labour force proves very adaptive towards changes in demand for qualified labour. High mobility can reduce the capacity problems of the industrial production by reducing mismatch problems. High mobility also tends to reduce the level of structural unemployment due to the many job openings giving unemployed persons the opportunity to find new jobs. It must be mentioned that some of the mobility can be seen as a forced, non-voluntary job change. However, the majority of all job turnovers have in recent years been voluntary, reflecting the wishes of the employees to pursue new opportunities in an expanding labour market.

Mobility differs from age group to age group and is - not surprisingly - highest for the younger cohorts, cf. figure 3.

**Figure 3: Per cent of employees who have changed jobs within a year 1980-1998, by age groups**



*Source: Danish Ministry of Finance, 2000*

### **Geographic mobility and unemployment**

OECD has criticised both the Danish and the Swedish unemployment insurance benefit systems for being too generous, thus creating rigidities in the labour market and damaging the process of job creation. Job seekers are not going to be eager enough when looking for a new job if the benefits are too close to the minimum wages of industries employing unskilled labour, it says. The modest income gains that the unemployed can achieve by finding a job is not sufficient for many jobseekers to commute great distances or accept jobs paying less than the job the unemployed person had earlier. When empirical data from Denmark is examined, this argument finds little support.

In the period from 1980 to 1998 the geographic mobility has gradually increased. People looking for work tend to commute greater distances in 1998 than in 1980 (an increase of 50 per cent). The effects of this are a potential better match between vacancies and the competence of job seekers. This changing behaviour also has an impact on reducing the structural unemployment. Statistics show that unemployed persons who find new employment are generally more mobile than persons coming from another job. Thus, even if the Danish unemployment system does leave little income gain for an unemployed, low-skilled person that finds a low-pay job, the attitude and the social values of the majority of the unemployed seem to be in favour of looking for new employment.

Unemployed with a degree of 0.5 or more of annual unemployment have increased the distance of commuting relatively more than other groups of unemployed and already employed persons. This kind of indicator seems to prove that the criticism of the generosity of the Danish unemployment benefit system lacks substantial empirical evidence.

### **Flexibility and perceived job security**

Another interesting aspect of labour market flexibility is the perceived job security among employees. Once more empirical evidence seems to go against conventional wisdom as shown by a new study from the European Foundation for the Improvement of Living and Working Conditions, (2000). Thus, less than one of ten employees in Denmark (9 per cent) are afraid of losing their current job. That is the lowest level in EU, where one out of three expresses concern about losing their present employment. Employees in countries such as Germany and Italy consider their job to be far less secure than Danish employees do.

There is a close relationship between a high level of concern and a high level of present unemployment, as it is the case in e.g. Greece and Spain, where two of three express doubts about their future employment opportunities. However, other societal factors seem to play a role when it comes to perceived job security. A country such as Austria with an unemployment level lower than Denmark has more employees who are concerned about job security, 23 per cent in total.

Employees living and working in Scandinavia generally express a high level of employment confidence. Sweden is ranked seven of the EU countries with 20 per cent of the employees feeling unsecured. Norway and Finland are placed between Denmark and Sweden in the ranking.

The high flexibility on the Danish labour market seems to be to the main reason for the high rating by the Danish employees. 68 per cent of all Danish employees think it will be easy for them to find another job, if they lost their present job. On average in the EU only 35 per cent believe it to be easy to find a suitable job, whereas 48 per cent expect it to be difficult. Only 25 per cent of the Danes think it might be difficult to find a new job matching their preferences.

This potential contradiction between a high labour turnover and a perception of easy employability among Danish employees might be explained in two ways that supplement each other. Firstly, the Danish industrial structure of many SMEs and almost no large, national dominating corporations creates a very open local labour market with many entry and exit opportunities. In contrast, labour markets dominated by large corporations that create an internal labour market only leaves relatively few job openings for outsiders to use. That explanation might be why the European Foundation study finds a difference between Denmark and Sweden on this indicator. Sweden is much more dependent on large corporations than Denmark. The second explanation is the flexible and generous unemployment benefit system, which makes high mobility and a perception of relative economic security possible at the same time.

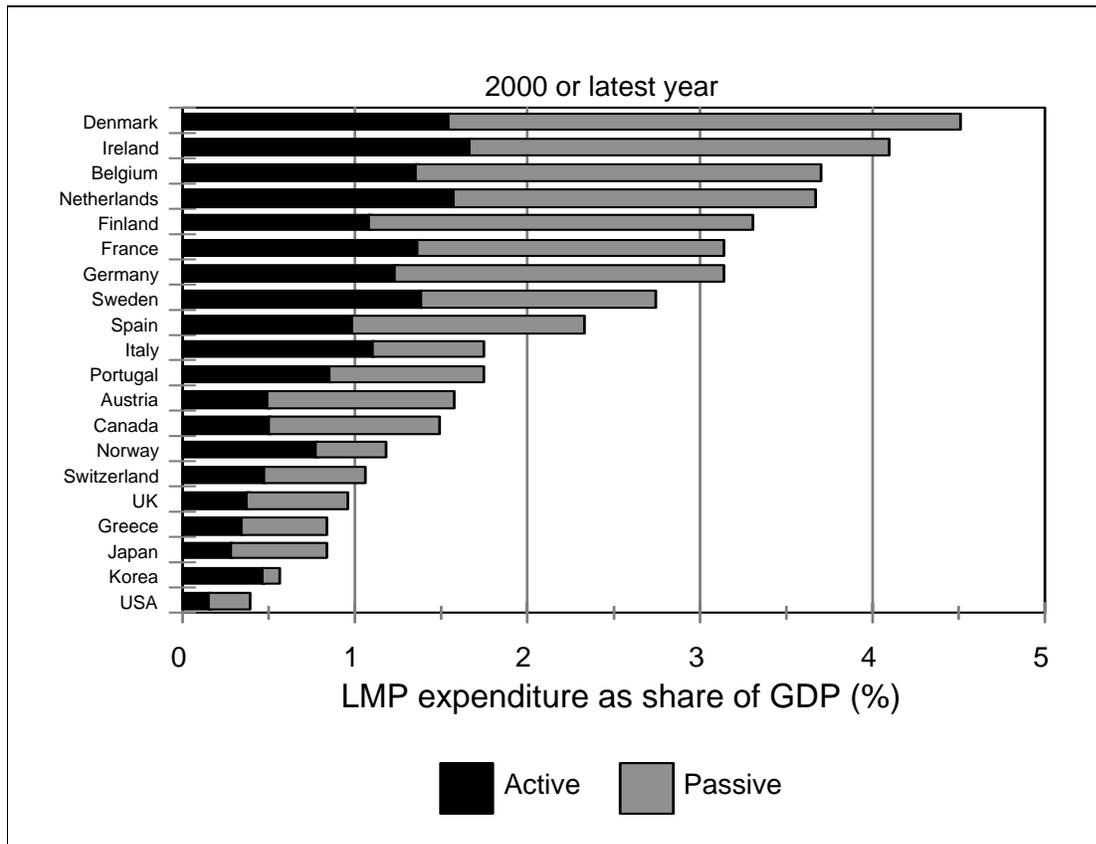
In conclusion, this section of the article has illustrated the very good performance of the Danish and the Swedish economy when it comes to the development of employment and unemployment in the 1990s. Especially in Denmark, labour market flexibility is very high. This goes hand in hand with a positive perception of employability among employees and adds to the impression of an effective and flexible labour market, not a labour market characterised by institutional rigidities as often claimed by critics.

We will now turn to the discussion of ALMP and its contribution to the status of the labour market described.

### 3. Labour market policy and welfare state models

Both Denmark and Sweden are high spenders when it comes to labour market policy, cf. figure 5.

Figure 5: Expenditure on labour market policy as share of GDP divided into active and passive measures. 2000 or latest year. Source: OECD (2000, 2001), table H.



As indicated by figure 5, in 2000 Denmark was the country in the OECD area with the highest share of GDP spent on labour market policy, while Sweden was ranked no. 8. When it comes to active measures, Denmark and Sweden are among the four most active spenders. Even if one takes into account the fact that the international statistics on public spending in this area may be somewhat flawed, there is no doubt that Denmark and Sweden are representative of countries where both active and passive labour market policy plays a massive role, compared to more liberal regimes such as the UK or the US.

Thus, both Denmark and Sweden still represent welfare state models that differ significantly from the models of the US, the UK and continental European countries by

maintaining a universal social coverage in case of unemployment based on an assumption of the individual rights and needs of the labour force.

Gallie and Paugam (2000) have developed an interesting taxonomy of different welfare state models, using three criteria for "unemployment welfare regimes": (i) the share of the unemployed entitled to receive unemployment insurance benefits, (ii) the level and duration of the benefits, (iii) the scope of ALMP. Based on these indicators it is possible to construct a taxonomy of four different welfare state regimes, cf. table 5.

*Table 5: Four different welfare state regimes as defined by the situation of the unemployed*

Regime	Part of unemployed covered by unemployment benefit system	Level of compensation and duration of unemployment benefits	Active Labour Market Policy (ALMP)	Country illustrations
Sub-protective	Very incomplete	Extremely limited	Generally not existing	Greece, Italy, Portugal, Spain
Liberal (minimum protection)	Few	Limited	Weakly developed	UK, Ireland
Employment-centred	Variable (depends heavily on the employability of the person in question)	Unequal	Extensive	France, Germany, Netherlands
<u>Universalistic</u>	Comprehensive coverage	High, generous	Very extensive	Denmark, Sweden

*Source: Adapted from Gallie & Pauham (2000), table 1.9 and pp. 9-11*

This taxonomy places Denmark and Sweden in the same category of welfare regime with a universal strategy to handle the structural labour market problems. It is important to have this taxonomy in mind when the recommendations of the OECD are discussed.

This article will argue that during the 1990s policy makers of Denmark and Sweden were locked into the universal welfare state regime and made no serious attempt to follow the OECD recommendations. However, some changes in policy strategy have taken place in both countries. And some may argue that the governments of Denmark and Sweden did take initiatives as part of their ALMP, thus questioning the existing functionality of the universal welfare state regime. When describing the policy changes in the 1990s, Casey and Gold (2000) underline that the Netherlands, Sweden and Ireland all performed better in the recent period and add:

*" Each of these countries displays neo-corporatist traits. However, each of them has been moving toward supply-side corporatism, which places a considerable premium upon decentralisation, ordered deregulation and a respect for the role of the market.*

*The first two countries have also taken substantial steps to modify and adapt their systems of social protection."(Casey and Gold, 2000, p. 99)*

Thus, one may see the trend in form of governance in Sweden as a decline of corporatism and an extension of a market approach. This has not happened in Denmark in the 90s, at least not as significantly as in Sweden although some critics claim that the trend toward a new regime is evident. In order to investigate such criticism the ALMP in Denmark and Sweden will be examined closely and the ALMP will be related to the recommendations of the OECD.

#### 4. ALMP and macro-economic developments

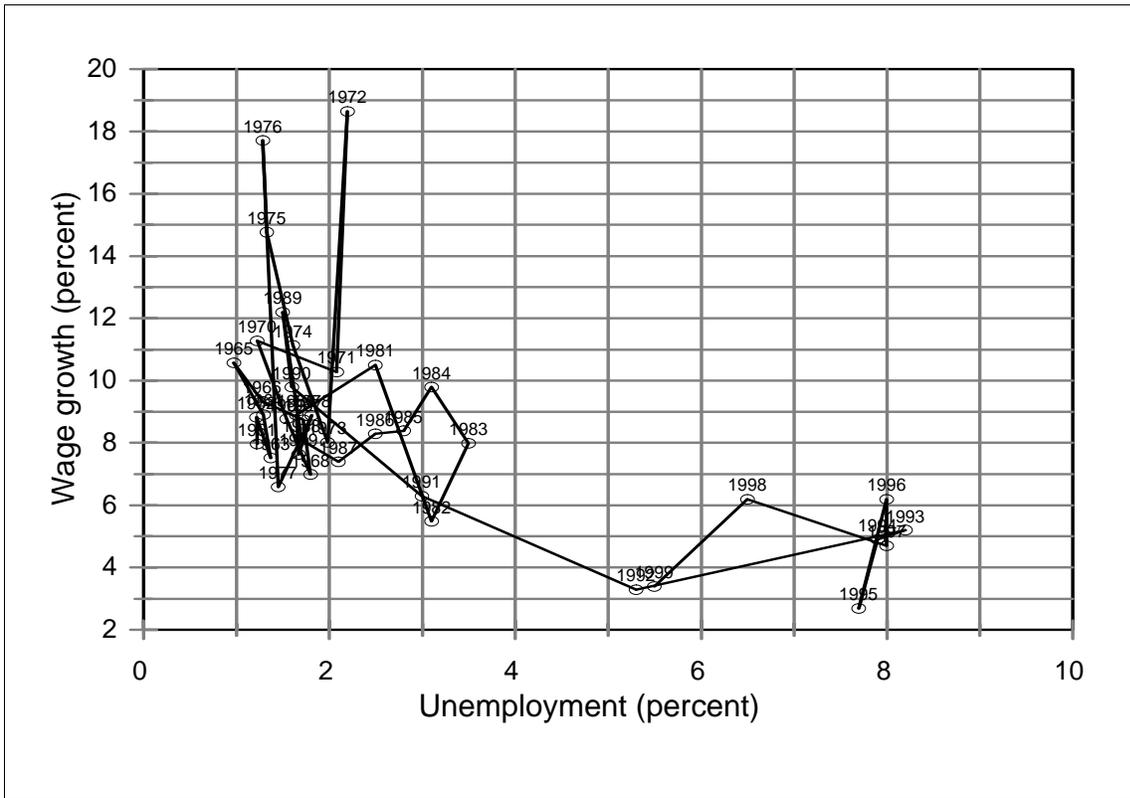
As shown above both Denmark and Sweden have made impressive recoveries in recent years. Unemployment has declined to half its former level in recent years and employment rates for both men and women are among the highest in Europe. Most astonishing is the sharp drop in open unemployment and the rise in employment that have taken place without the rise in wage inflation, which could be expected based on historical experience.

Figures 6 and 7 give an impression of the relationship between the unemployment and wage inflation in recent years in both Denmark and Sweden as represented by the traditional Phillips curve.

**Figure 6: Denmark: Unemployment and nominal wage growth, 1961-1999**



Figure 7: Sweden: Unemployment and nominal wage growth, 1961-1999



When Denmark is examined in figure 6, the pattern of wage inflation and unemployment in the years from 1961 to 1999 can be divided into four distinct sub-periods. Phase 1 from 1961-1970 is a period with a low level of unemployment and a tendency for wage inflation to increase slowly from the first to the second half of the decade, but still being below 15 per cent. During phase 2 from 1972-75, the level of wage increase rose to around 20 per cent per year, while the unemployment rate at the same time increases from 2 to 6 per cent.

An important institutional factor behind this development was the automatic indexation of wages based on price inflation, which was then part of the Danish wage-agreements. The outburst of inflation in relation to the first oil crisis automatically spilled over into rising nominal wages. This form of regulation was restricted somewhat in 1975 and finally suspended in 1983.

The third phase can be identified from 1975 to 1994. What may be interpreted as a new rather stable Phillips curve appears, where the wage increases during the upswing from 1984 to 1988 tend to reach the levels seen at the same level of unemployment around 1980.

Finally, the fourth phase is represented by the observations from 1993 to 1999. During this period open unemployment in Denmark was cut by half. This was mainly due to a

sharp increase in effective demand, while the level of wage inflation was still below 5 per cent. Literature in this field gives several explanations for this exceptional development. One explanation focuses on a changed climate in wage negotiation with organisations on both sides becoming increasingly aware of the potential damages for employment caused by high nominal wages in a situation where the Danish currency has been firmly linked first to the German Mark and then to the Euro. Another explanation points to the contribution of the Danish labour market reform of 1994 when it comes to reducing imbalances on the labour market during the upswing (Madsen, 1999). Finally, some researchers focus on the artificial reduction in registered unemployment caused by the rising number of persons in labour market programmes and leave schemes. However, even though there was an increase in the take up of such programmes in 1994-1995, the fall in unemployment since then cannot be attributed to so-called "book-keeping effects" (cf. Madsen, 1999, chapter 3).

Sweden also shows a configuration of unemployment and wage inflation, which during some sub-periods may be interpreted along the lines of a traditional Phillips curve, cf. figure 7. Most of the observations from the first 30 years are located in a cluster, where unemployment lies in the interval from 1 to 3 per cent and wages increase by between 7 and 11 per cent per year. The main exceptions are again found in the early 1970s where the inflationary push of the first oil crisis made Swedish wages increase by up to 19 per cent per year. Apart from that it is tempting to interpret these three decades as the golden years of the Swedish model, where low unemployment and moderate wage inflation went hand in hand. After this long first phase, a second period can be identified covering the 1990s. Here unemployment rapidly increased to 8 per cent. At the same time wage growth declined to a level of 3 to 6 per cent per year. It is especially notable that the recent Swedish recovery, which has lowered unemployment to around 6 per cent, has not yet been accompanied by a new rise in wage inflation. For Sweden – and also for Denmark as noted above – this presents a remarkable change in the pattern of nominal wage formation.

## **5. The importance of ALMP to recent success**

The political strategy behind this achievement is the combination of an effective macro-economic policy, a policy of wage moderation and a labour market reform carried out jointly by the social partners and the government. This balanced strategy is one of the main reasons for the Danish success. An active labour market and education and training policy supporting labour market mobility is an additional factor that explains the Danish labour market revival in the 1990s.

Allan Larsson, the former director of EU's DG5 (the directorate responsible for employment) has been a firm advocate of the Danish ALMP. He summarized why politicians should pay attention to what have happened in Denmark in this fashion,

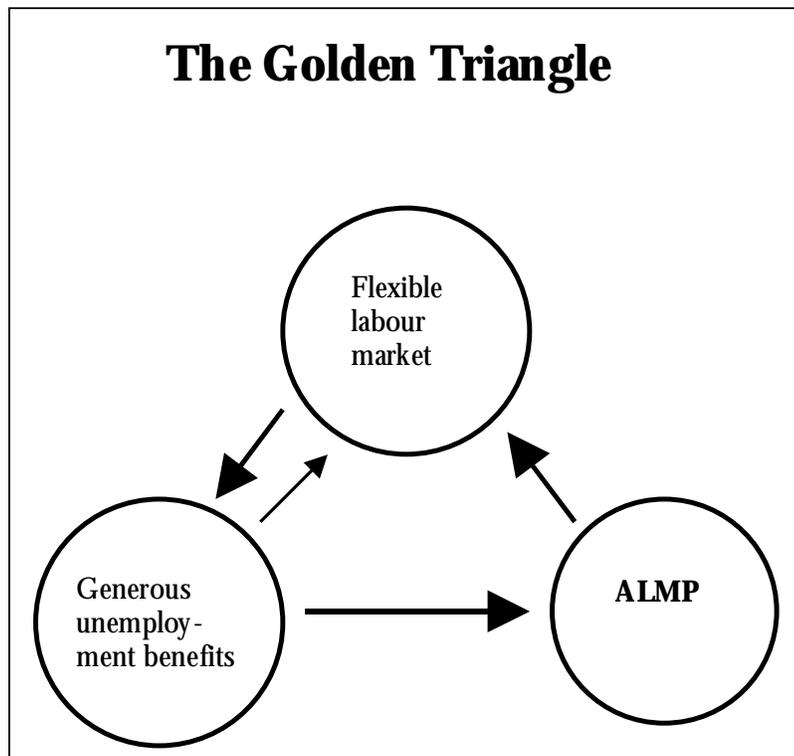
*"Over the past few years, Denmark has implemented many of the elements of what is now being pursued as the European Employment strategy: employability, entrepreneurship, adaptability and equal opportunities. Denmark has done this with impressive results. That is why policymakers in many Member States now look to Denmark as an inspiration for the development of labour market policies in the EU."*

### "The Golden Triangle"

One interpretation of particularly the success of the Danish employment system that has become popular in recent years has been that of the "Golden Triangle", which summarizes three important characteristics of the Danish labour market (Madsen, 2002):

- A high level mobility and flexibility combined with a low level of formal job protection
- The bulk of the social costs of high flexibility is soaked up by the generous public unemployment insurance benefit system
- ALMP with a strong emphasis on rights and obligations to activation

Figure 8: The Golden Triangle of the Danish Labour Market



These three elements of the ALMP act in a close cooperation and make it socially acceptable for companies to adjust the use of their staff very flexibly. Dismissed workers rely on the flexible labour market for a rapid entry to a new job and rely equally on the high level of compensation of the unemployment insurance benefit system in case of a short period of unemployment.

Unemployed persons with difficulties in finding new employment after a short period of unemployment are trained as part of the ALMP and in this way gain skills that enable them to exploit the opportunities arising from the high numbers of job openings on the flexible labour market.

The ALMP in one way facilitates the flexible labour market but also takes advantage of the same flexibility. Thus, a flexible labour market might be part of the solution and not just a problem.

This Danish model therefore is a total different employment system from the one found in e.g. Southern Europe, but it also differs from the system in Sweden. As described above, the job protection measures in Sweden place a great deal of restriction on the companies when it comes to dismissing labour. The price for this institutional set-up is obvious - low flexibility on the labour market and a high premium on hiring new staff. Managers of companies tend to think twice before hiring. This also creates an environment in which less competitive labour is easily bypassed thus increasing the risks of long-term unemployment. The fact that the Swedish labour market recovered so quickly under these institutional conditions makes the recovery so much more impressive. However, one should bear in mind that the imbalance of the Swedish labour market is still around 7 per cent and that Sweden still has to create 200,000 more jobs to reach the employment level from 1991.

### **The Danish ALMP 1994-2000**

So what happened in the 1990s with the Danish ALMP? First of all, the Danish labour market policy has undergone rather drastic changes in recent years:

- The share of active expenditures has increased
- The formation and implementation of policy have been decentralised (the steering reform).
- At the same time the use of instruments and programmes has been changed (the activation reform).
- For the unemployed who are insured the maximum duration of benefits and participation in activation programmes has been reduced from approx. 9 years to 5 years (from 1999).
- Emphasis is now put on an obligation to full-time activation after only two years of unemployment. For some groups activation takes place at an even earlier time.

One of the most important reforms has been a *steering reform* involving a decentralisation of policy implementation to regional labour-market authorities, which were empowered to design activation programmes in line with local needs. One has to bear in mind the smallness of Denmark, which is close to the size of a region in an EU perspective. Nevertheless, the decentralization process placed the responsibility for implementing the ALMP at the county level. The integration of the social partners at county level is essential to the success of this steering model. The outcome thus relies heavily on the existing social capital in the local area.

Another part of the reform contained an *activation reform* with the following elements:

- The creation of a two-period benefit system for the insured unemployed with strong emphasis on activation during the second period.

- A change in the assistance to the long-term unemployed from a rule-based system to a system based on a needs assessment of the individual unemployed and of the local labour market (introducing the so-called "individual action plan").
- The removal of the connection between job training and the unemployment benefit system, which meant that participating in job training would no longer extend the right to unemployment benefits if a person became unemployed after the training period.

These reforms may be seen as initiatives that comply with some of the key recommendations of the OECD Job Study, especially the recommendation that points to the need for strengthening the emphasis on active labour market policies and reinforcing their effectiveness.

Furthermore, the 1995 initiative to intensify the supervision of availability (and employability) might appear to comply with the OECD recommendations. However, these policy initiatives were taken in 1993/94 and have been adopted within the framework of the Danish welfare regime, a regime that aims at universal and generous social coverage. Thus, the social effects of the reforms did not have the same strategic aim as the OECD had in mind. It was still a policy that accepted a premium on social cohesion in general.

This cannot be said to apply to the new policy to combat youth unemployment. The youth unemployment programme that started in 1996 focused on activation of the young unemployed and included a reduced compensation to young unemployed. This new incentive structure increased the job search behaviour of the young people. Similarly, many young unemployed went into formal education. Both changes contributed to reducing the open youth unemployment. In 1999 the rights and obligations to activation were applied to young people with six months of unemployment, thereby increasing the effectiveness of the ALMP even further.

The ALMP reform of 1994 also changed the way ALMP is financed. From a system where unemployment insurance benefits, vocational training, etc. were financed by the state (taxes) and payment from insured members of the unions. The ALMP is now generally financed by a direct tax on all employed and self-employed persons (8 per cent of the gross income). The employers also contributed by paying a total of 0.6 per cent of the wage sum of all employed in a company, - a so-called labour market contribution. These changes in the financing model make all costs of ALMP more visible to both policy makers and the public in general.

Finally, a number of paid leave schemes were introduced, which were not in line with OECD thinking. In 1994 paid leave schemes encouraging both employed and unemployed people to take a leave of absence were introduced. These schemes served two aims. One was to increase the number of open vacancies for unemployed to fill and another was to provide the employed part of the labour force with a new welfare service. A third aim, which was only related to the job rotation scheme, was to enhance the competence of employed and at the same time provide the unemployed with job experiences which they could not obtain otherwise. These paid leave schemes were very successful, - actually too successful and the incentive structure was changed several times

the following years in order to reduce the number of people taking advantage of the schemes.

Evaluations of the reform demonstrate that the activation reforms in many respects have been successful, although not without problems. A study by the Danish National Institute of Social Research summarizes the findings of the large-scale evaluation programme of the 1994 labour market reforms (Larsen and Langager, 1998). The general question raised is whether the labour market reforms and the subsequent adjustments in labour market policy have had a positive impact on the functioning of the labour market. Not surprisingly, this question has to be answered with considerable care. However, the evaluation findings concerning the importance of the activation strategy may be summarized as follows (Larsen and Langager, 1998, pp.34-36):

- the employment goals specified in the individual action plans indicate that there is a *considerable planned mobility* among the unemployed;
- the labour market policy seems to function effectively in the sense that the planned mobility among the unemployed is *greater* in areas where the need for mobility is highest (due to threats of bottlenecks)
- there are *significant positive employment effects* of both vocational training and education for the unemployed, and
- the *effective supply of labour among the insured unemployed seems to have increased* between 1994 and 1997, probably due to the stricter demands made on the unemployed during the second phase of the reform (for instance, the increased demands on the young unemployed).

With regard to the measures directed at firms, there are indications that the reforms have contributed to the absence of bottlenecks since 1994:

- there is some indication that *the quality of the services provided by employment services to firms has improved* since the reform in terms of meeting the need for skilled labour (although there are also examples of short-term labour shortages),
- the introduction of new forms of placement services (in the form of *open* self-service placements), together with monitoring activities and regular contacts with employers, has led to *an increase in the transparency of the labour market*, thereby improving its functioning as a system for matching labour supply and demand.

Whether these effects of the reforms have led to an improvement in the general functioning of the labour market, measured by its ability to adapt to external shocks and to allocate labour efficiently, is hard to evaluate. The lack of significant shortages of labour since 1994, in spite of the fall in unemployment and the strong growth in employment, could indicate that the functioning of the labour market has improved. Whether this is solely due to the reforms, or also to other factors (including changes in wage-fixing practices) cannot be definitively determined on the basis of the evidence available.

## **Education and training**

A specific feature of the ALMP in both countries is the focus on competence development and training. The Danish system may serve as an illustration.

The most important aspects of the Danish education and training system are:

- The public system for both basic and adult vocational education and training operates under strong influence from the social partners (unions and employers associations).
- The training and education system is targeted at the workforce in general (based on the concept of life-long learning) and not solely at the unemployed.

In Denmark this system has functioned for more than 40 years. The 1994 labour market reform allows for a more flexible use of adult education and training. Also, another important part of the reform was the fact that the integration of the unemployed using training and education partly took place through job rotation and paid leave schemes. However, these schemes have been abandoned or severely reduced in effect in recent years.

The Danish government introduced a new reform of the adult and continuing education system in January 2000, which in many ways marks a change of strategy and incentive structure from a market-driven to a public-policy approach, leaving more responsibility for education and training to the social partners.

The goal of the reform is to give all adults access to life-long learning opportunities. The government intent is to focus education and training activities on adults with low educational and skill levels. Firms have been given a larger financial responsibility for improving the skills and education of higher-educated employees. Firms are in reality responsible for financing the continued education of their higher-skilled workers (e.g., via company-related vocational training courses).

The providers of the public educational programmes have been asked to develop programmes and training activities related to the participants' daily jobs and to provide knowledge about machines, materials and processes, as well as general qualifications such as communication, organisation and planning skills. The training also serves to improve personal qualifications such as responsibility, flexibility and even basic reading and writing skills.

A committee comprising of relevant labour market actors (e. g. unions and employers associations) has been formed and is in the process of defining the financial arrangements and deciding on the courses offered. The committee will receive EURO 383 million each year from the government (2001). This is also the maximum state investment in education and training. If activities go beyond this level of costs, the firms have to pay. Critics argue that the conditions for joining state-financed education (i.e. basic job-related education) exclude many employees.

## **The Swedish ALMP in the 1990s**

During the 1990s the ALMP reached a level of activity no one had ever expected. A total of 630 billion Skr. were spent and 2.9 million people were in contact with the Public

Labour Market Authorities in some way or other during the 1990s. Every year as many as 200,000 persons participated in the Public Employment Programmes (approx. 5 per cent of the labour force). This proves that it was not just a small minority but large segments of the Swedish population who were involved in the ALMP in the 1990s (Agell et al, 2000).

Table 6 shows that in 1996 employment programmes involved approx. 4.7 per cent of the labour force and the open unemployment was 8.1 per cent amounting to an imbalance of 12.7 per cent in 1996. This picture has changed since then. It is estimated that the number of persons in the employment policy programmes in Sweden amount to 113,000 in 2000 and 115,000 in 2001, representing approx. 2.6 per cent of the labour force. This means that the proportion of unemployed plus the programme participants amount to 7.3 per cent in 2000 and is expected to amount to 6.5 per cent in 2001.

**Table 6 Development of the labour market and number of participants in employment policy programmes in Sweden 1996-2001**

	Per thousand persons					
	Result				Prognosis	
	1996	1997	1998	1999	2000	2001
Labour	4310	4264	4255	4309	4358	4404
Employed	3963	3922	3979	4068	4154	4231
Unemployed	347	342	276	241	204	173
Percent of LF	8,1	8	6,5	5,6	4,7	3,9
Employment policy programs						
	202	191	173	142	113	115
Percent of LF	4,7	4,5	4,1	3,3	2,6	2,6
Imbalance in percent of LF	12,7	12,5	10,6	8,9	7,3	6,5

Counted as numbers of people, this represents a reduction from 383,000 persons in 1999 to 288,000 in 2001. In other words, there is still a large number of unemployed, but the situation has definitely changed for the better since 1996.

The same is true about Denmark. Among transfer recipients the reduction of involuntary unemployed has been particularly pronounced from 360,000 in 1994 to less than 150,000 in early 2000. An increase of 40,000 persons has taken place over the same period for people on voluntary schemes such as early retirement or leave. Long-term unemployment has dropped a great deal from 160,000 persons to less than 40,000 over that period. The number of long-term unemployed in activation schemes on top of that has been almost unvarying at 70-80,000 persons (The Danish Ministry of Finance, 2000).

This description of the ALMP in Denmark and Sweden shows how many different roads have been tried in order to keep the balance between learning from the past, increasing the effectiveness of the measures and still adhering to the fundamental concepts of the universal welfare state regime.

## 6. The role of the "new economy" in Denmark and Sweden

Even if the activities behind the ALMP are interesting, ALMP can only deliver respectable results if the economy in general is doing well. So what are the dynamics behind the positive employment development in both countries: in short, the dynamics can be identified as a robust "job creation machine".

Both Denmark and Sweden have traditionally relied on manufactured exports for most of their growth. Sweden has historically been dominated by large corporations operating on the global market to a higher extent than Denmark. In the 1990s the two countries have both deregulated industries such as telecommunications, airlines and banking. By doing so they have followed the recommendations of among others the OECD. The results have been strong growth in the ICT sector, many mega mergers and heavy lay-offs and major restructuring of whole industries, - adapting them to the demands of the global competition.

Both governments have focused on fostering a more entrepreneurial culture in order to help new companies and high technology flourish. This policy has been particularly successful in Sweden where much of the growth is currently coming from businesses that did not exist 10 years ago. This policy has also been pursued in Denmark but with less success than in Sweden.

In Sweden information technology and service companies are now the main source of new jobs, not the traditional manufacturers. Sweden has invested a large part of its gross domestic product in "knowledge" - research, development, training and education - than any other country in the world in recent years. An illustration of this development is the expansion of Kiska Science Park that started in the early 1970s outside Stockholm. Kiska is now a complex of more than 600 technology companies employing approx. 27,000 workers.

Denmark has been a bit slower to catch up with the possibilities presented by the global market and new technologies. However, the growth of the mobile telecommunication industries as well as new bio-tech businesses has taken root in the greater metropolitan area of Copenhagen.

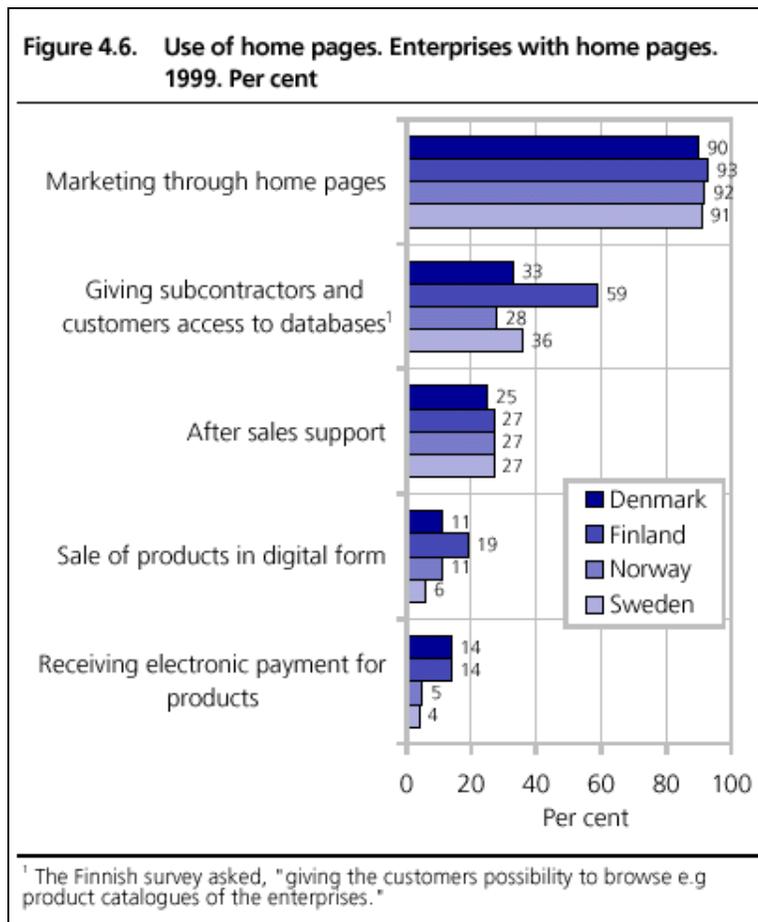
The different traditional industrial sectors of the national economies have been quick to adapt to the new circumstances and opportunities created by the 'new economy'.<sup>2</sup> An indicator of this is the widespread access to the Internet by companies of all sizes:

	Denmark	Finland	Norway	Sweden
All enterprises	85	94	77	88
Employees				
10-19	78	91	69	84
20-49	91	96	83	92
50-99	94	99	90	93
100+	97	100	93	98

<sup>2</sup> Use of ICT in Nordic enterprises 1999/2000

In 2000, close to 9 out of 10 enterprises had access to the Internet and even among small firms close to 80 per cent had access in Sweden and Denmark.

The pattern of Internet use also points to a broad acceptance of the new technology for many different purposes. This indicates that ICT is well integrated in the production process. General information search was the most common task (90 per cent) carried out with the help of Internet. In Denmark financial transactions via the Internet were more common than in Sweden. While only about 40 per cent of the Swedish enterprises conducted financial transactions via the Internet, about 60 per cent of the enterprises in Denmark had exploited this possibility. About one quarter of the enterprises in both countries reported that they used the Internet to recruit new personnel.



If different elements of e-business activities like marketing, sales and services as well as electronic payments for products are examined, you will find that they are used by a large segment of the Danish and Swedish companies. Together, the indicators of ICT usages show a business environment in both Sweden and Denmark that embarrasses the possibilities of the New Economy.

Another important indicator related to the integration of ICT in the economy at large is the long-term development of the productivity. According to an ILO study labour productivity in Sweden grew by 39 points and Denmark by 34 points in the years between 1980-1997 placing Sweden and Denmark among a group of high growth countries surpassing countries like France and Germany in the period. It is of course extremely difficult to make accurate estimates of the impact of ICT on the national economies of Denmark and Sweden, but a number of indicators point to some kind of positive effect in both countries.

Many of the companies in the old traditional industries have incorporated the best from the dot-com companies in terms of flexibility, innovations and a new work culture<sup>3</sup>. This has generated new international market opportunities and allowed for the utilization of new technologies. This also puts pressure on the HRM of the companies that spills over into the ALMP.

The cornerstone of this development is the focus on competence development and the realisation of new forms of work organization. The management of an increasing number of firms and organisations have acknowledged the effectiveness of mobilizing the tacit knowledge of the employees. Changes in management forms towards **high-skill** and **high-trust** organisational and management models are becoming still more widespread in order to generate efficiency in all parts of the production process. Different Danish studies have concluded that approx. 25 pct of all companies (particularly in the industrial sector) are experiencing a development in the direction of an increasingly comprehensive, flexible form of organisation. This development is endorsed by the trade unions that view this as a road to better, higher-paying and more qualified jobs.

The social partners (unions and employers associations) are in agreement with a strategy where competence development is achieved by close cooperation between local representatives of the social partners within the individual companies and within the framework of the national labour market policies. In this aspect the goals of the ALMP and the interests of the social partners are the same. It does, however, put forward the need for adjustments of the ALMP to place more emphasis on the needs of the already employed away from the long-term unemployed. This is of course a major change of perspective for the national ALMP.

## **7. The future of the Danish and Swedish labour market models**

Finally, we will discuss the future of the Danish and Swedish labour market models. The dangers are already becoming obvious. In the case of a continuous high-growth scenario the demand for qualified labour that meets the needs of the 'new economy' will increase faster than the supply. This is a problem already in Sweden. The Stockholm area has shortages of computer specialists, sales representatives and teachers, even caterers. The public employment service's most recent analysis shows shortages in several dozen job categories and acute shortages in many others, including car mechanics, taxi drivers and nurses.

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<sup>3</sup> "Danish Industry in the New Economy", Danish Technological Institute, October 2000. ("Dansk Industri i den ny økonomi", Teknologisk Institut, oktober 2000.)

At the same time, the labour force reserves are becoming scarce, especially in Denmark, and the demographics of both countries are threatening to become a major obstacle for the continuation of the 'job machine'.

The major challenge facing the ALMP in both Sweden and Denmark is the need to modernize the programmes and incentives once more. This time to a future where the problems of meeting the demands for skilled and specific qualified labour related to the new economy are a greater than long-term unemployment. The future focus of ALMP will not be on the long-term unemployed, but on increasing the size of the labour force and enhancing the qualifications of the labour force within the framework of the new economy. This includes (LO, 2001):

- Getting the non-active part of the population mobilized and motivated for entering the labour force
- Integrating immigrants into all parts of the labour market by fighting discrimination
- Establishing a structure on the labour market that will increase the possibilities for older workers to find flexible, part-time employment.
- Reducing the absentees and improving the quality of the working life
- Reforming the unemployment insurance benefit system in order to fit to a labour market with more free agents and more self-employed.

In the case of a new recession, both countries are in danger of encountering heavy 'mismatch' problems on the labour market; i.e. increasing long-term unemployment of low qualified labour co-existing with increasing demand for specialized qualified labour. This will also lead to a need for a modernization of the ALMP, much along the lines already discussed, but the ALMP must also take the problems related to the long-term unemployment into account. This will be a real challenge for the future ALMP in the welfare regimes of Denmark and Sweden.

## **8. Conclusion**

There is no doubt that flexibility on the labour market, numerical as well as functional, is essential to the future of the employment in countries like Sweden and Denmark. During the 1990s, the two countries have been through a difficult time changing from a period of high unemployment to the current situation with high employment and increasing mismatch problems on the labour market. Both have managed to reduce long-term unemployment and have focused on ALMP programmes where life-long learning is seen as an integrated part of the policy. Even if both countries currently experience bottleneck problems on the labour market, they have avoided major wage inflation. Both countries have integrated elements of the recommendations of the OECD Job study, however, it has been without having to abandon the universalistic welfare regime. In this way, Sweden and Denmark are both good examples of the necessity of staying very critical of a primitive interpretation of the neo-liberal economic theory. It is not necessary to embrace the US model of job creation - it is possible to modernize the Scandinavian model.

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Flexicurity, first developed as a labour market policy in the Nordic countries, has been endorsed by EU leaders and the European Commission as a way of solving the Union's employment problem. However, as a new Commission faces up to Europe's worst recession for many decades, doubts have emerged as to how committed member states are towards flexicurity and making it work across the EU. The secret behind the success of the Nordic models was found to be the 'flexicurity' approach, which was implemented in Denmark in the early 1990s, and - with some variations - in other Nordic countries, the Netherlands and Austria.