

# The Global Financial Crisis and the Return of the Nordic Model?

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# Topics

1. The global economic crisis
2. Globalisation in general
3. The demographic challenges

# Unclear terminology

- Nordic model
- Scandinavian model
- Swedish model

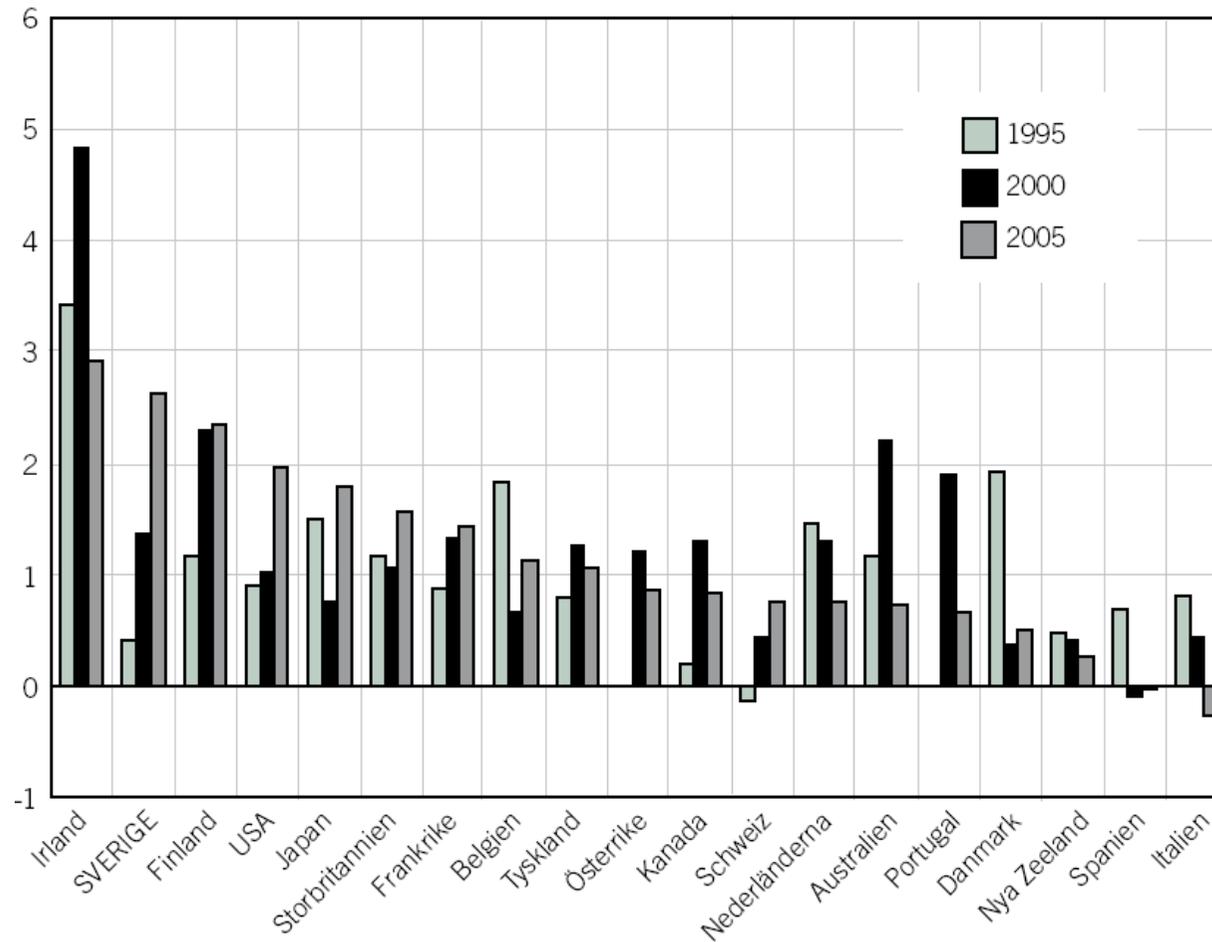
# Characterisation of the Swedish/Nordic model

- Macroeconomic outcomes
- Means to achieve these outcomes
- Broad mindsets

# The Swedish/Nordic model in terms of macroeconomic outcomes

- High employment
- High growth by Western European standards
- Even income distribution
- Large trade dependence

# Total factor productivity, contribution to GDP over five years



## Contributions to differences in total employment rates relative to the euro area average from differences in employment rates for various gender and age groups

	Total 15-64	Men 15-64	Women 15-64	Total 15-24	Total 25-54	Total 55-64
Denmark	12.1	4.2	7.8	4.1	4.3	3.7
Finland	4.6	-1.2	5.7	0.3	2.4	1.9
Sweden	10.1	1.7	8.3	1.0	3.5	5.6
Average	9.2	1.6	7.5	1.7	3.5	4.0

# The Swedish/Nordic model in terms of systems/institutions

- A generous welfare state with generous social insurance and a large public sector
- High taxes
- Co-ordinated wage bargaining and labour market regulations through collective agreements
- Active labour market policies
- A well-educated work force
- High R&D expenditures
- Deregulated goods markets but more regulated markets for services (including the building sector)
- Fairly little of selective industry support
- A sustainable pension system
- A fiscal framework promoting fiscal discipline

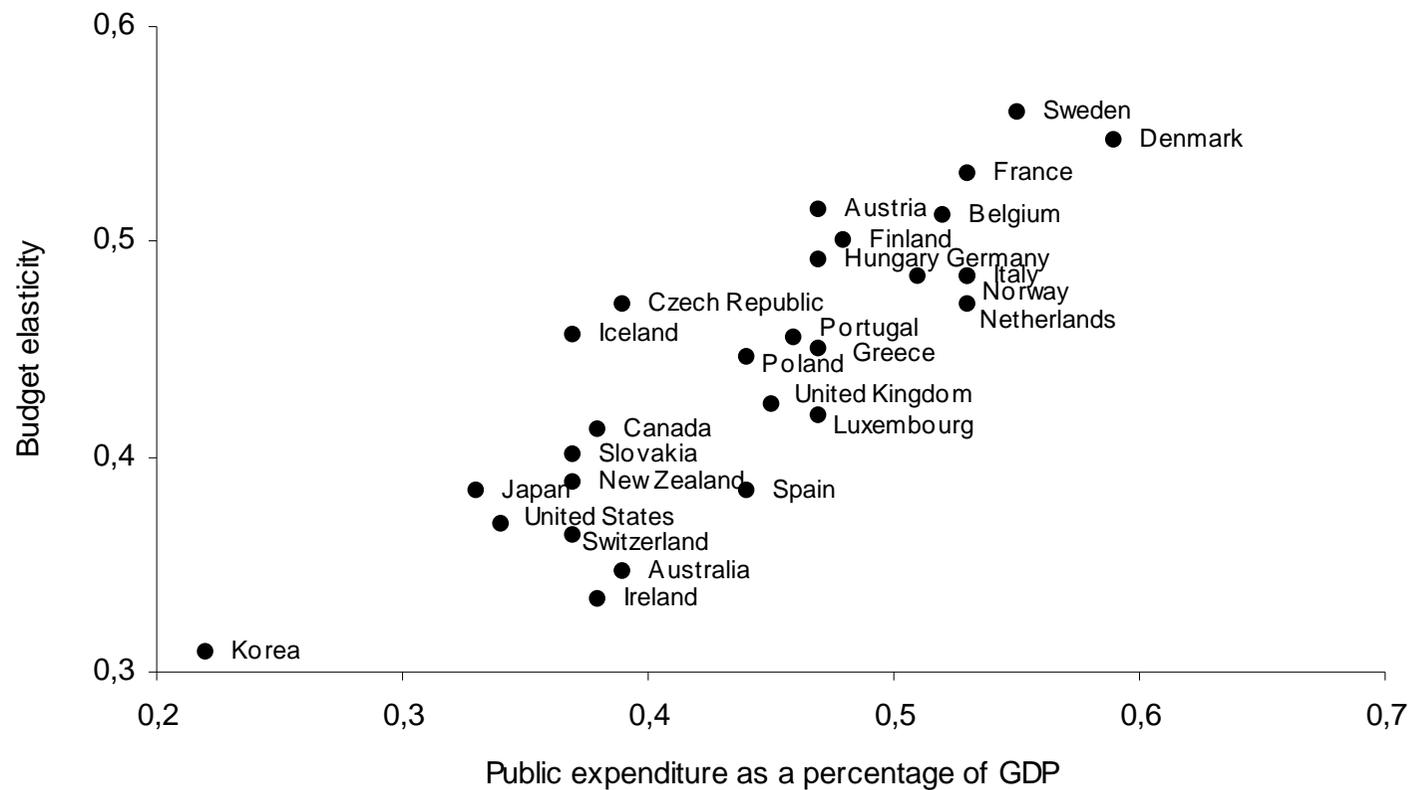
# The Swedish/Nordic model in terms of mindsets

- Rational approach to problem-solving?
  - but excessive marginal tax rates in the 1970s and early 1980s
  - tax reform, pension reform, new fiscal framework
- Consensus culture?
  - polarisation regarding unemployment benefits, earned income tax credits, top marginal income tax rates
  - consensus on R&D, product market deregulations, no selective subsidies, trade openness, the pension system, fiscal discipline

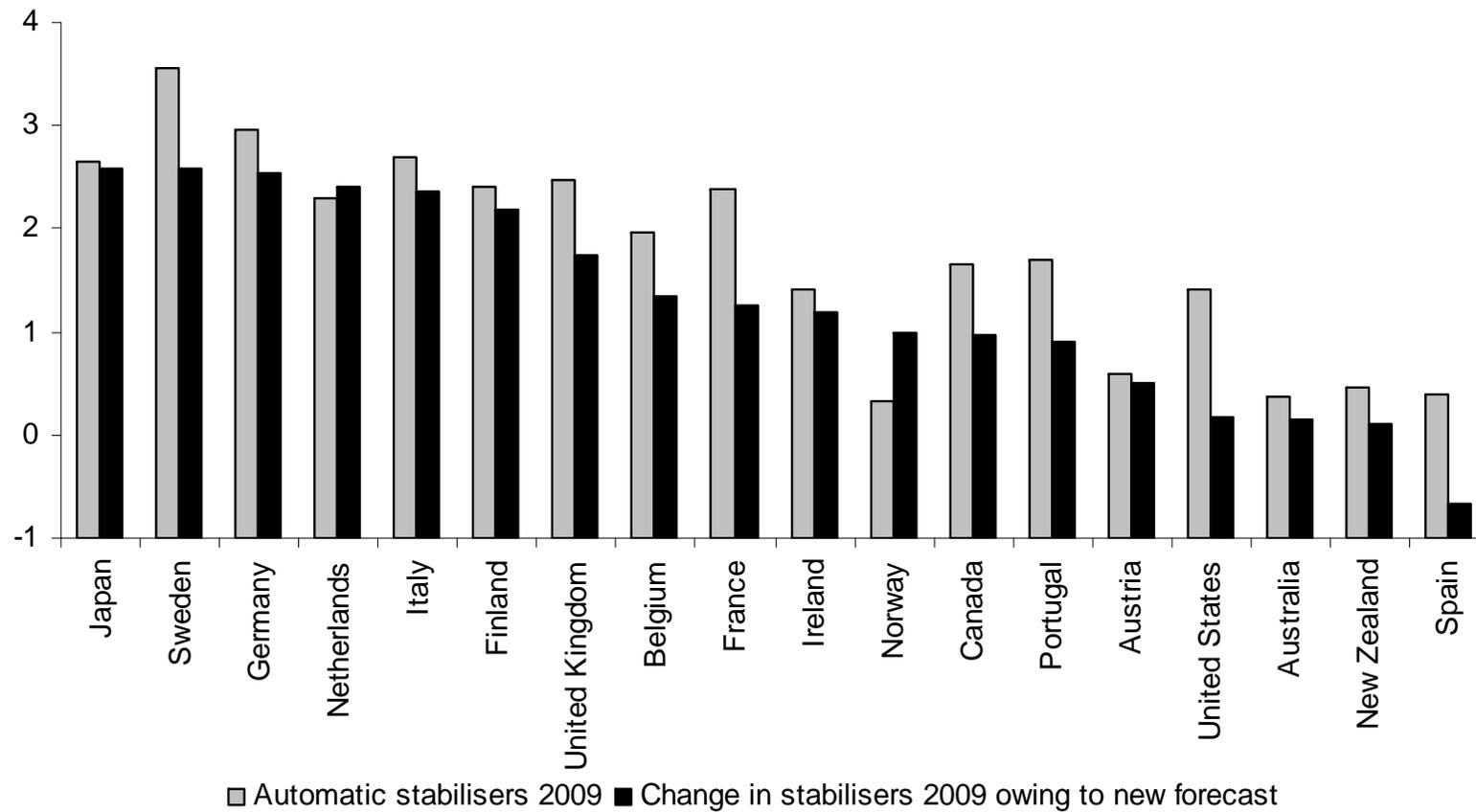
# Sweden and the global economic crisis

- Not so much direct consequences of the financial crisis
- Instead consequences of the fall in world demand
  - dependence on exports
  - investment and consumer capital goods
- Big government has meant strong automatic stabilisers
- Strong public finances have given room for expansionary fiscal policy
- The government's labour market reforms
  - less income protection for the unemployed
  - smaller risk that unemployment becomes persistent
  - they may (together with the absence of selective subsidies) have opened up for the work-sharing agreements in manufacturing

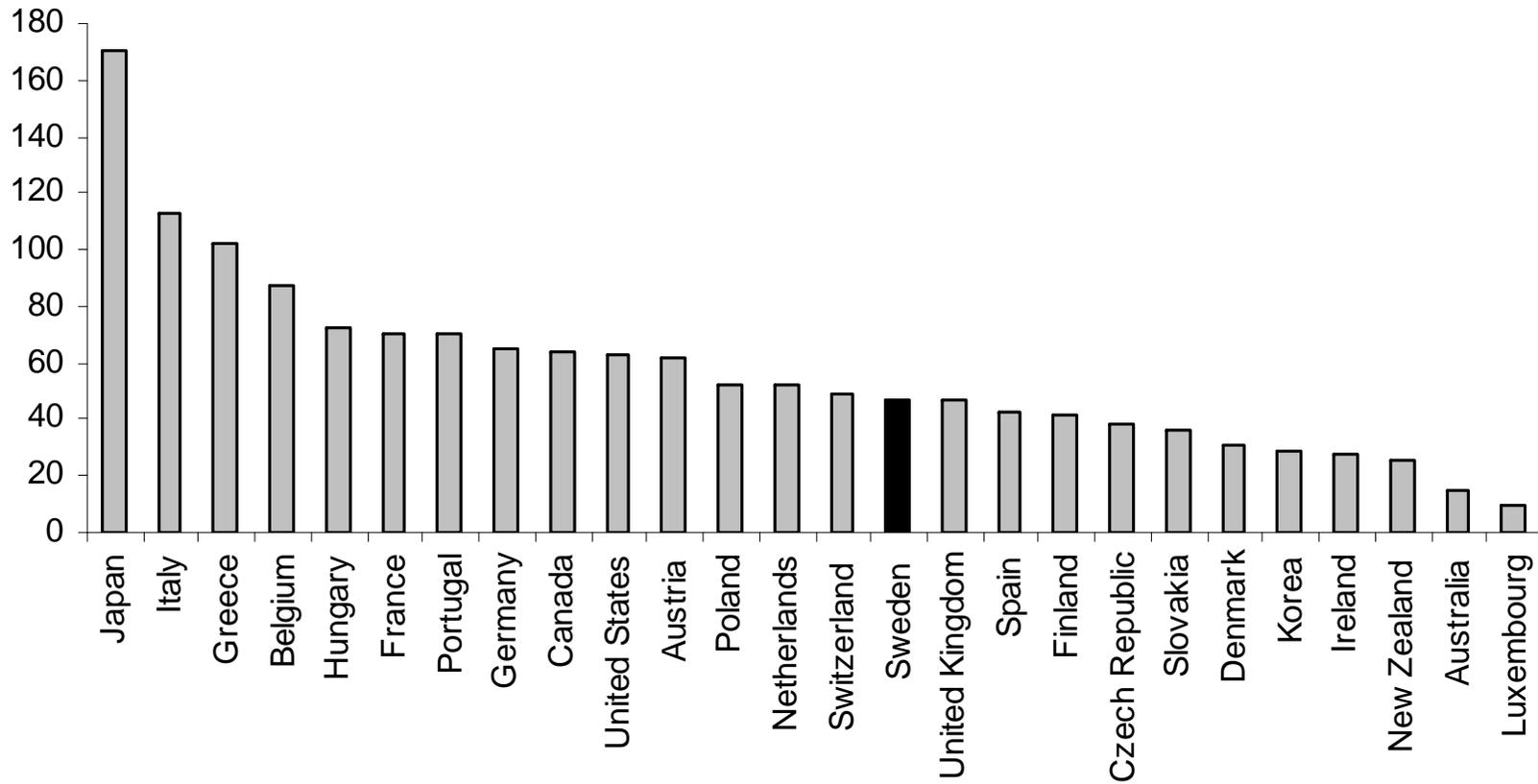
# Budget elasticity and the size of the public sector



# Automatic stimulus measures



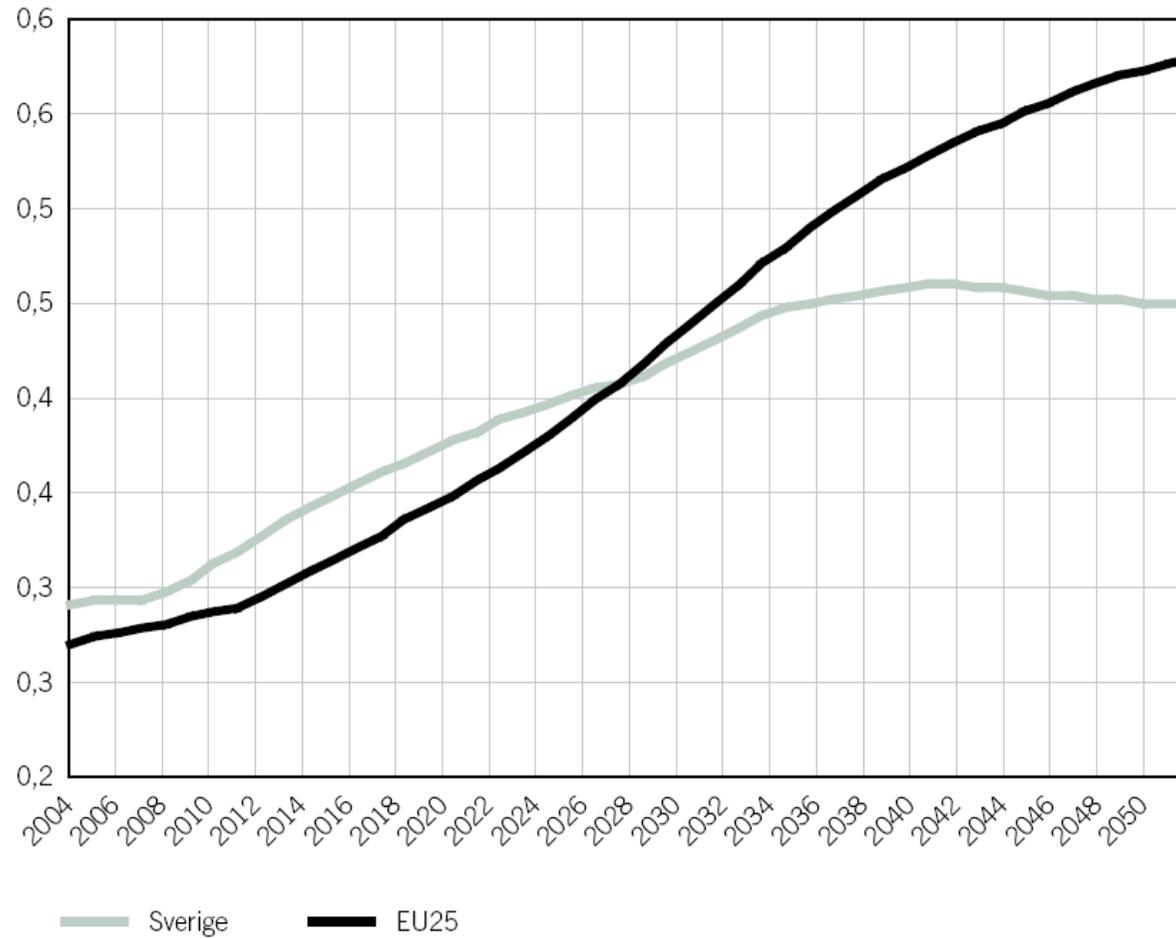
# General government gross debt in per cent of GDP



# The demographic challenges

- A smaller problem in Sweden than elsewhere but still a formidable problem
- The pension system has been reformed
  - defined contributions instead of defined benefits
- Public finances sustainability calculations are more favourable for Sweden than for other countries
  - but all such calculations are too favourable
  - spontaneous rises of retirement age will not be enough
- Measures to deal with the situation
  - changes in pension rules
  - increased reliance on user fees
  - labour market reforms to increase employment in general
- All measures are politically highly controversial

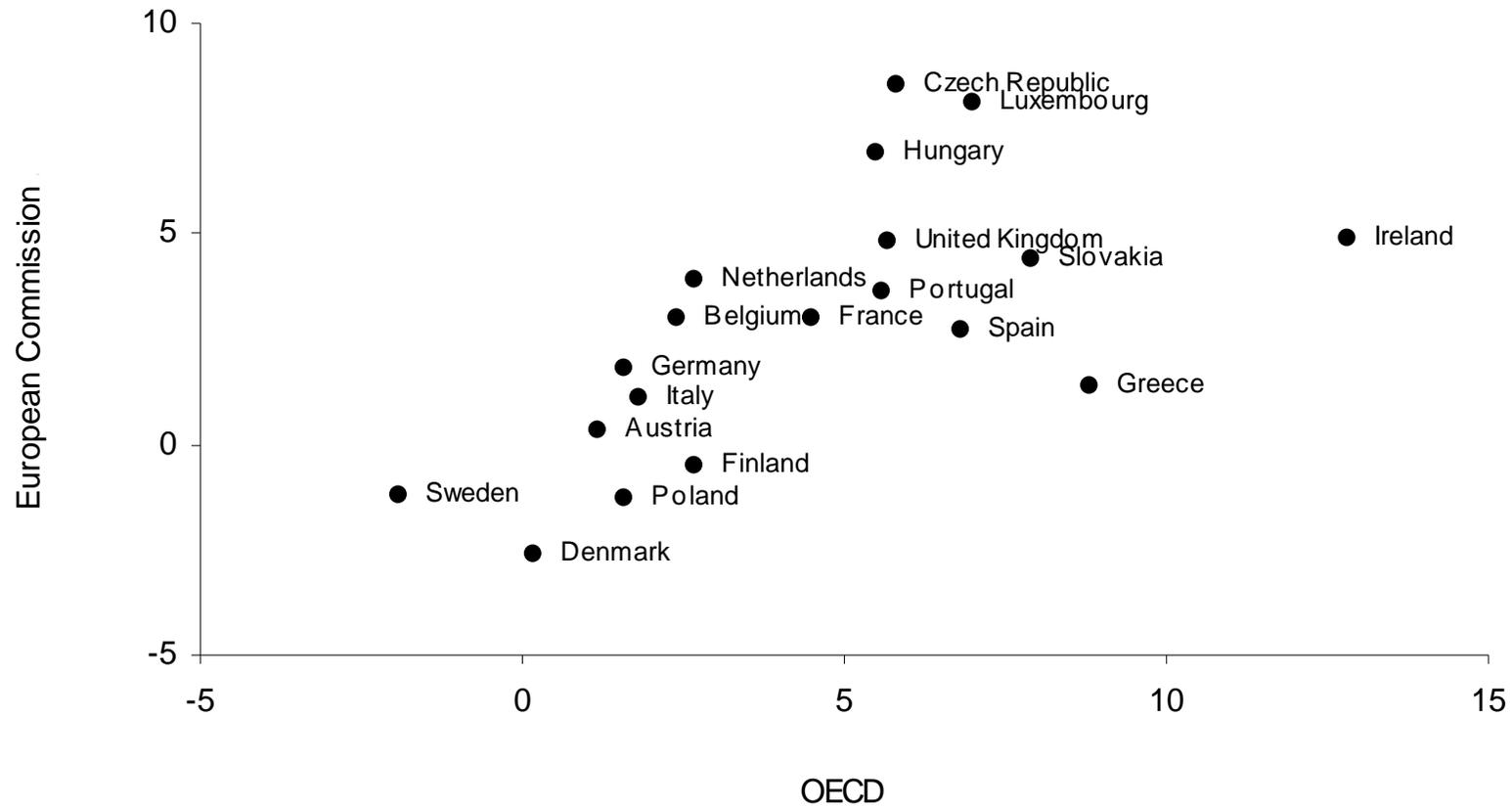
# Old-age Dependency Ratio (65+/20–64), Sweden and EU25



# Average labour market exit age



# Long-term sustainability of public finances (S2 indicator)



# The S2 indicator and intertemporal financial net worth, per cent of GDP

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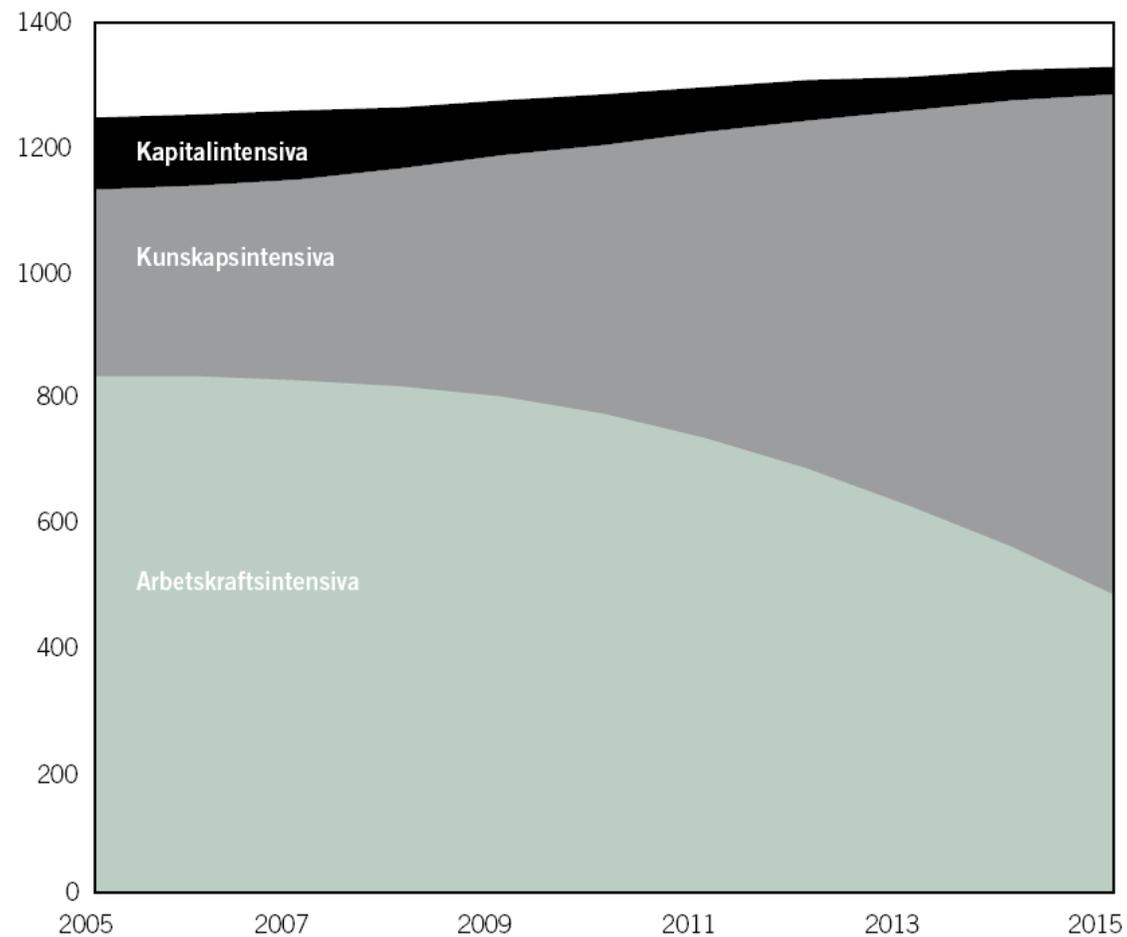
	S2	Intertemporal financial net worth
Base scenario	0.5	-52.5
Higher exit age	-0.8	84.0
Higher health care costs	8.2	-861.0

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# The challenges from globalisation

- Increase in trade between low-wage and high-wage economies
- Low-wage economies with relative abundance of low-skilled labour should specialise in labour-intensive production
- High-wage economies with relative abundance of high-skilled labour should specialise in skill-intensive production
- Potential aggregate wage gains for all countries

# Employment developments (1000s) in sectors exposed to international competition, Sweden



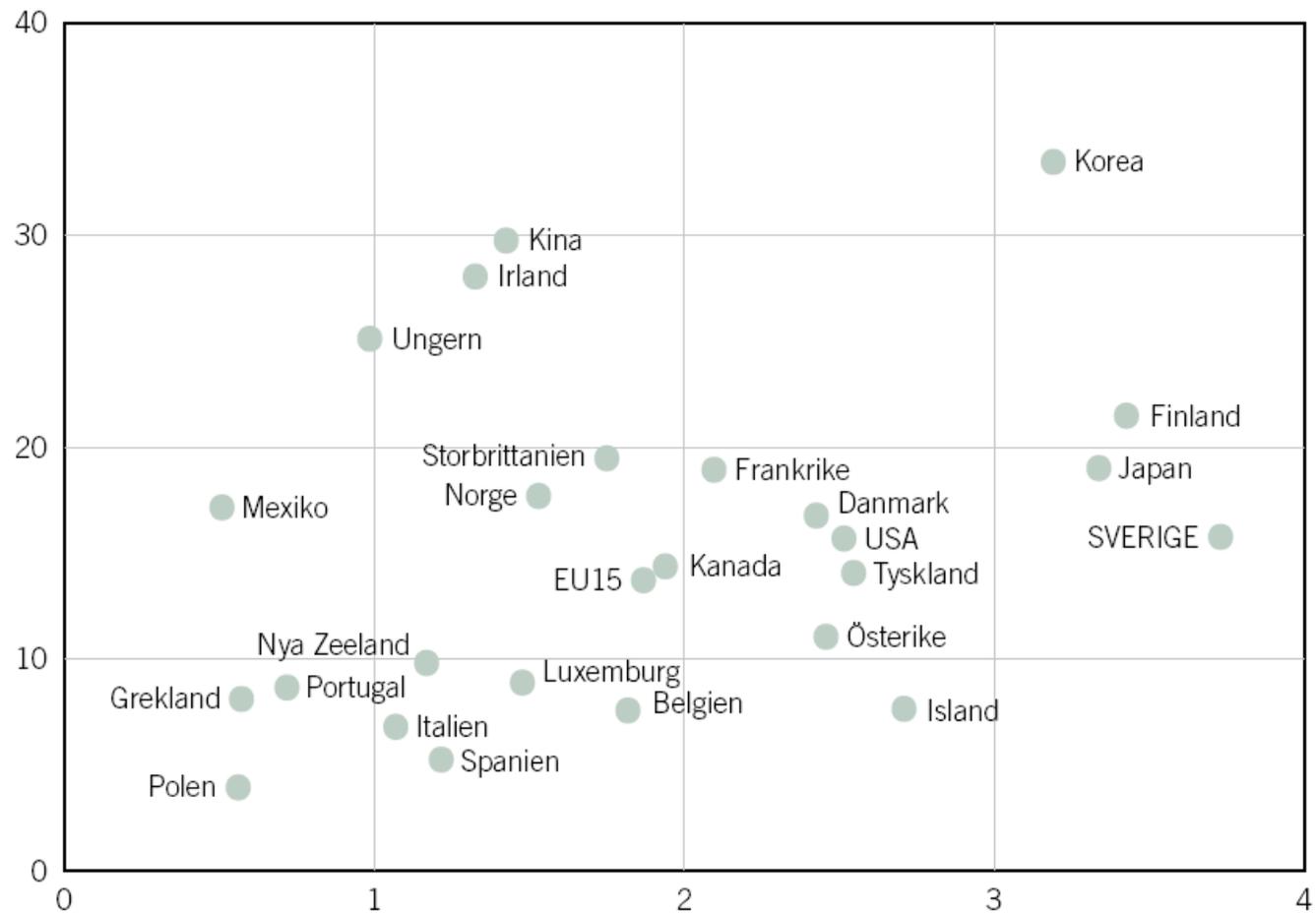
# Preconditions for the aggregate welfare gains to be realised

- Sufficient wage flexibility
  - relative wages of unskilled labour must fall
  - otherwise unemployment and too large contraction of labour-intensive sectors
- Trade potential in service sector should be used
  - allow low-wage imports of services
  - near-monopoly of public sector in health care and education is a likely obstacle to successful exports

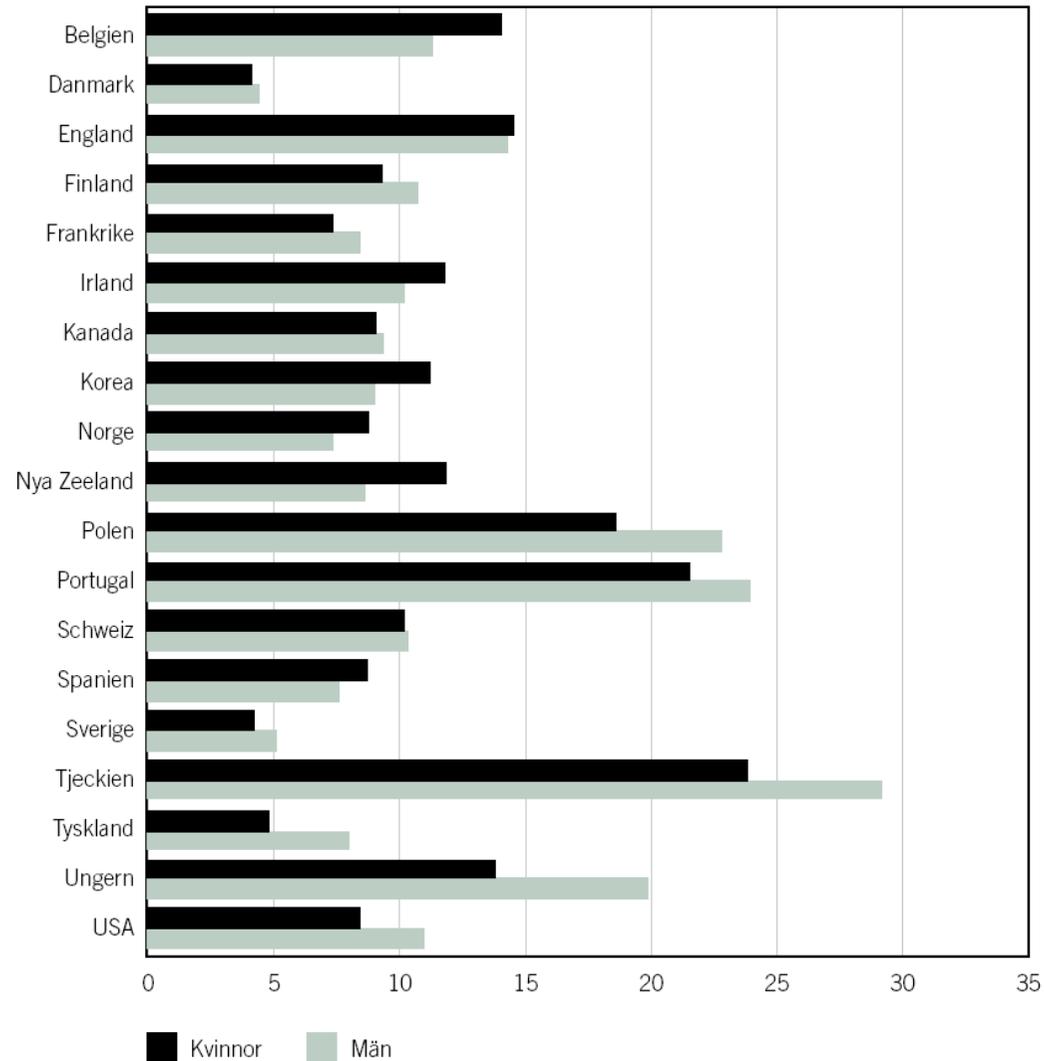
# Can we upgrade our production?

- High R&D expenditures but low returns
- Low return to higher education
  - volume of higher education
  - allocation of higher education
- Retraining policies in a state of flux
  - traditional labour-market retraining
  - retraining in the regular education system
  - the role of the parties in the labour market
  - basic youth education

# R&D expenditures in percent of GDP and the share of high-technology exports in total exports 2006/07



# Returns on higher education 2004, per cent



# How well designed is the Swedish model to deal with the challenges?

- Well-designed to cope with the economic crisis
- Better designed than most other models to deal with the demographic challenges
  - but still very large challenges
- Coping with globalisation likely requires large changes in the model
- Key question: Can we reach a consensus on the future equity-efficiency trade-off?