

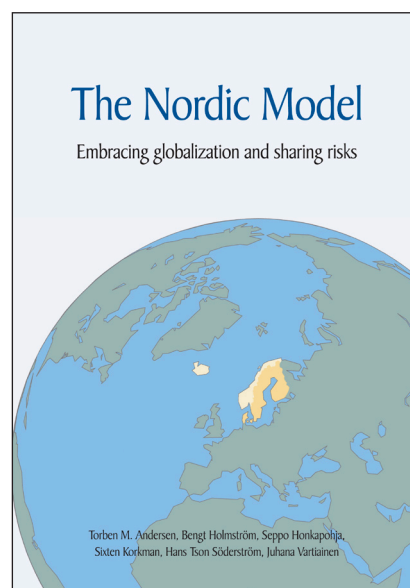
The Nordic Model

The Nordic model is widely regarded as a benchmark. A number of comparative studies of economic and social performance have ranked the Nordics high. A common finding of cross-country comparisons is that the Nordics succeed better than other countries in combining economic efficiency and growth with a peaceful labour market, a fair distribution of income and social cohesion. The model is pointed to as a source of inspiration for other people in their search for a better social and economic system.

On the other hand, many observers around the world are amazed that “the bumble-bee can fly” – that the Nordic economies can prosper and grow in spite of the presumably weak economic incentives associated with high tax wedges, a generous social security system and an egalitarian distribution of income. Critics have been looking for inner contradictions in the model and they have questioned its sustainability. Some argue that the economic performance of the Nordic countries is simply a result of exceptional and temporary advantages, bound to disappear over time.

This report deals with the Nordic model, the reasons why it has worked in the past, and the challenges it is being subjected to in the future. Present economic and social trends, including globalization and demographic change, pose significant challenges to the model as we know it. The model will remain viable and successful only if the challenges and the need for reform are understood – and if action is taken.

Globalization is primarily an opportunity and not a threat. It has been the very basis of the growth in productivity and living standards that the



Nordics have achieved. However, the continued trend of globalization will put the model under pressure. The emerging economic giants in Asia and Latin America will force us to restructure our economies at a rapid pace; relocation of production and job losses need to be compensated for through innovations and growth in new activities. Simultaneously, globalization may undermine the financial viability of the welfare state by increasing international factor mobility and tax competition between nations as well as by opening up the possibility of “social tourism” for eligible groups.

Demographic change – in the form of an ageing population – increases the size of the passive population (retirees), while tending to decrease the size of the active population (workers). The result is a dramatic rise in the dependency ratio and a strong pressure towards increased social spending and higher tax rates. The combination of ageing populations and high ambitions

for welfare services will strain public finances, even more so if globalization increases the mobility of jobs and labour. The sustainability of present tax-transfer systems and public systems of care for the elderly are being seriously put into question.

In responding to these challenges we regard a number of proposed “solutions” as basically non-workable. For instance, the financial dilemma of the welfare state cannot be resolved through more rapid economic growth, higher taxes, increased fertility or more immigration.

On the other hand, we believe it is essential to preserve one central feature of the Nordic Model. The Nordics have been embracing both globalization and the welfare state, and we argue that the security offered by collective mechanisms for sharing risks has been instrumental in enhancing a favourable attitude to globalization and competition. This key characteristic of the model must be preserved – in order to maintain an economic and social climate which is conducive to future welfare and growth. Collective risk sharing should continue to offer a safety net which helps workers and their families to cope with risks and to adapt to new requirements in times of change.

In addition, we emphasize that a high rate of labour force participation is an indispensable ingredient of the model. There must be sufficient incentives – in the form of financial rewards and/or workfare elements – to participate in the labour force and to work. Lengthening working careers must go hand in hand with increasing longevity. The “social contract”, including the public pension system, should not be based on the assumption that the tax burden can be passed on to future generations in the form of rising tax rates.

There is also a need to define the core tasks of the welfare state and to clarify the scope of the services that citizens are entitled to and should be able to expect. Higher productivity in the provision of welfare services is imperative and can be enhanced by, inter alia, privatization and outsourcing of public services, though only in cases where difficult and important issues of governance can be dealt with satisfactorily.

Finally, investment in human capital should not be the victim of increasingly tight budget constraints; what is good for the young is good for the future of society.

Our findings and conclusions are summarized in the sections that follow. The reasoning behind them is then developed in the ensuing chapters.

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