



Crisis, Miracles, and Beyond

Negotiated Adaptation of
the Danish Welfare State

Edited by Erik Albeek, Leslie C. Eliason, Asbjørn Sonne Nørgaard and Herman M. Schwartz

Aarhus University Press

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Dedicated to the memory of Leslie C. Eliason

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PREFACE

Like the crisis of the welfare state, this book has been underway for a long time! But, unlike the welfare state, and particularly the Danish welfare state, this book has finally come to an end! The papers in this collection of essays first saw the light of day in 1995, at a time when the Danish economy had just found its feet after a decade of turmoil and adjustment. At that time the authors of this book came together to explain how it was that Denmark, widely proclaimed to be riding a fast train to a macroeconomic hell (albeit in the first class coach), had somehow not only avoided going over the brink but had also reversed direction.

More than ten years later the Danish economy is one of the strongest in Europe. Unemployment is low, the budget is in surplus, foreign debt is at manageable levels, and people are generally happy with the economy and the welfare state. We hope that this book will provide some insight into why this came to be so. We found there was no magic policy or miracle that cured Denmark's ills. Indeed, one major point is that a changing external environment helped a Denmark that simultaneously changed domestic public policy in incremental but ultimately positive ways. These deliberate changes were specific to discrete policy areas, which is why the collection surveys health, education, and daycare in addition to the usual macroeconomic policy issues. But the collection also looks at the actual operation of and politics around local government, as well as relations between central and local government, because in Denmark local government funds and delivers the bulk of welfare state services. We argue that the cost efficiency and political legitimacy of these services is what makes or breaks a welfare state, not the generic external economic environment.

We also hope this collection sheds some light on the differences among the Scandinavian political economies and welfare states and also those between Scandinavia and the other advanced economies. As Lars Mjøset argued back in the 1980s, there were really five Scandinavian models, not one. The Danish model, despite a flurry of articles in the late 1990s and early 2000s, remains relatively unknown in English language publications. While the OECD routinely lauds the Danish mortgage finance system as a model for the rest of Europe, and also recommends Danish active labor market practices, much of the Danish welfare state remains *terra incognita* outside of Scandinavia. While we hope that there is something to be learned from the Danish experience, one

major point that emerges from our analyses is how much the working of these successful policies is tied up with a set of attitudes that is hard to transport across borders, and with a specific set of environmental conditions that will not necessarily be encountered again.

This is not to say that there are no transferable lessons, though. The central problems of the Danish welfare state in the 1980s and 1990s were political problems – enduring problems of governance and governability that transcend any specific polity. Could political actors shift the welfare state’s funding priorities if and when the demand for services changed or as social demographics changed? Could political actors prevent welfare state producers from putting their own interests ahead of their clients’ interests? Could political actors structure transfers in ways that maintained social solidarity and a willingness to work; or to put it in terms of the foregoing question, in ways that prevented rent seeking not by producers but by concentrated groups of clients? We think the chapters here speak to these core political questions in ways that matter for the durability of other welfare states.

We wish to extend our gratitude to Aarhus University Research Foundation for providing funding for the initial conference in 1995, and to the Danish Social Science Council for providing financial support for the publication of the book. Special thanks to the contributors and the publisher for their patience with the editing of the book, and to Annette Andersen for her efficient secretarial assistance in the preparation of the manuscript. And finally, Herman Schwartz would like to thank Eve Schwartz for understanding that the US Customs Department would not have allowed him to take an entire cake from her favorite Danish confectioner back to the USA after the 1995 conference!

Our great pleasure in seeing this project finally in print is overshadowed however by the untimely death of our co-editor Leslie Carol Eliason in 2004. Leslie received her BA from the University of Virginia and her PhD from Stanford. She taught at the Department of Scandinavian Studies and at the Evans School of Public Policy at the University of Washington, and then at the Monterey Institute for International Studies. Her love for Denmark started when she was a high school Rotary exchange student in Holstebro, and her impeccable command of the Danish language was fortified by a Marshall Fund Fellowship to study at the University of Aarhus, and a return visit as a Fulbright scholar. Her academic work focused on public policy and in particular the comparison of welfare states. But she clearly cared much, much more for her students, who remember her as an inspiring and committed teacher and trainer. We remember Leslie as a spirited and loyal colleague, who cared deeply about her

students and inspired other women in her field. While on a Fulbright Fellowship to Hungary and Bosnia she was diagnosed with melanoma and passed away shortly after. Leslie played a key role in motivating this project and we dedicate this book to her memory.

Erik Albæk, Asbjørn Sonne Nørgaard, Herman M. Schwartz

August, 2008

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INTRODUCTION

*Erik Albæk, Leslie C. Eliason, Asbjørn Sonne Nørgaard
and Herman M. Schwartz*

What explains the remarkable resilience of the Danish welfare state, and what does this tell us about the future of the welfare state in general? How did this welfare state survive a quarter century that saw the collapse of its economic foundations in Keynesian demand management and full employment, and the erosion of its political foundations in the face of a fairly successful and OECD-wide ideological challenge to the whole idea of the welfare state from the political right? In order to answer these important questions, this volume presents a comprehensive account and analysis of the institutional structure of the Danish welfare state.

The focus of the book

The book focuses on four narrower sets of questions. The first is simply an empirical question: what is the institutional and political structure of the Danish welfare state? Surprisingly, there has been no comprehensive survey of the Danish welfare state since Lars Nørby Johansen's chapter in Peter Flora's path-breaking *Growth to Limits*. But Johansen presented a dry, empirical, and quite brief survey of changes in spending levels, programs, and clientele. His analysis suffered from a lack of attention to the actual bureaucratic structures that delivered services, the economic sustainability of rapidly rising spending, and the political basis of welfare state support. Although Gøsta Esping-Andersen presented a roughly contemporaneous analysis of the political basis for the Danish welfare state in *Politics Against Markets*, this too suffered from a marked defect. Esping-Andersen more or less elevated Sweden as the exemplar of the Scandinavian social democratic welfare state. Denmark thus appeared to be a lesser or defective version of the Swedish model; the preeminence of the Swedish model obscured the details of the Danish system. The first task this book takes up is thus a comprehensive survey of the Danish welfare state. Naturally we examine some of the core social services and transfers: on the service side, health, and daycare; on the transfer side, pensions, unemployment insurance and some smaller programs.

Second, we ask how these various pieces fit together with each other, with the broad macroeconomy and with political dynamics. Rather than simply surveying the core social services and cash transfers, we also show how these services and transfers are governed by central and local decision-makers, how they interact with labor markets, and what their macroeconomic consequences are.

The third question turns from empirics to dynamics: given its foundation in a small, open economy, how is it that the Danish welfare state is economically sustainable and that spending does not spiral out of control? This involves us in an exploration of both the supply of and demand for cash: how was the macroeconomy and budget regulated so as to prevent an erosion of the state's capacity to tax, and why is it that citizen demands for services and transfers has not spiraled out of control?

Finally, the fourth question similarly turns to political dynamics: given a polity characterized by highly organized economic interests, corporatist control over most institutions, and producer control over welfare state services, how is it that the welfare state remains governable and retains public support? Why don't producers abuse their position of control within state institutions that deliver services? Why do citizens willingly accept some of the highest average and marginal tax rates in the OECD? Why do they tolerate substantial state intrusion into their lives? The briefest possible answer to all these questions is that the Danish institutional structure and moral economy permits a "negotiated adaptation" by Denmark's welfare society to a large number of internal and external stresses. The very institutional structures, which theories of welfare state crisis see as the causes of decay, are also the sources of resilience in the face of internal and external challenges.

What the studies in this book reveal is a much more varied and complex picture of the predicaments and problems of the welfare state than most generic theories suggest. Our research on the Danish welfare state demonstrates a need to reexamine the theoretical underpinnings of contemporary welfare state research. From the point of view of those who see the welfare state as perpetually mired in self-destructive tendencies, or from the point of view of those mired in Esping-Andersen's triad of ideal types, Denmark remains an inexplicable phenomenon. Thus, we consider Denmark a critical test case for, rather than an exception to, these arguments.

Over the years Denmark has been struck by most alleged symptoms of welfare state crisis. As a small country with an open economy, Denmark was severely affected by changes in the international economy and the recessions of the 1970s. EC/EU harmonization policies have been part of the Danish political landscape for more than 35 years. Minority governments and corporatism are dominant features in Danish policy making; and Denmark was one of the very few countries where a protest party managed to capitalize on a tax-welfare backlash. And yet Danish policy makers managed to overcome or contain such "crisis" tendencies.

Similarly, viewed from the perspective of comparative welfare state research, the Danish welfare state has been presented as institutionally less developed and more compromised by its relatively stronger element of Liberalism than

other Scandinavian social democratic welfare states. Our approach has been to subject these assumptions to empirical analysis. Rather than hypothesizing on the inherent weaknesses that drive the politics of welfare state change, we have redirected our attention to the questions of whether and how welfare states have the capacity to adapt institutionally to changes in their international and domestic environments.

The problem?

We ask the above questions because the Danish welfare state resembles the bumblebee: theoretically neither should fly, yet both seem to do pretty well despite the predictions of theories of the welfare state and aerodynamics respectively. Three decades of welfare state research and theorizing beginning in the 1970s suggest that the extensive – and expensive – Scandinavian service-heavy social democratic welfare states should encounter economic and political difficulties.

The Danish welfare state in particular should have had the hardest time surviving, compared to its Scandinavian neighbors. Not only is the generous, universal Danish welfare state expensive, absorbing roughly 45 pct. of GDP, it is also largely financed by highly visible progressive personal income taxes. The Danish public sector therefore should be the most likely candidate for a tax and welfare backlash (Wilensky, 1984). Second, the political basis for the welfare state is weaker than in the rest of Scandinavia. The Danish Social Democratic Party has always had a smaller vote share than its Scandinavian counterparts, and its share has eroded more rapidly than theirs (Esping-Andersen, 1985; Svensson, 1989). Weakness in the traditional working class vote was not offset by new white-collar middle adherents. On both the left and the right the Danish Social Democrats face well organized parties that attract considerable white collar support, and various tax protest and anti-immigrant parties have sometimes attracted more working class voters than the Social Democrats themselves. In turn this created minority coalition governments whose ability to steer the economy and polity should have been quite limited.

Externally, changes in the global economy as well as in supranational political institutions such as the European Union seem to have curtailed policy makers' opportunities to develop or even sustain their national welfare states (Keohane & Milner, 1996). The European Exchange Rate Mechanism (ERM), the European Central Bank, and the Euro all constrain or curtail local monetary policy autonomy, while calling into question the utility of local corporatist arrangements. Some research suggests that corporatist bargaining is more difficult to sustain in a deregulated economy. Kitschelt (1994), Piven (1991), and Pontusson (1992) each argue that the strength and solidarity of organized

labor, a critically important component of the corporatist bargaining structure, have been undermined by increasing market integration and exposure to more intense international competition. This means that national corporatist arrangements may be less effective as mechanisms to negotiate public sector expenditure control and reorganization.

All these tendencies can be seen in Denmark's unfolding economic crisis during the 1970s and 1980s. Like other Western countries, these years confronted Denmark with serious problems and challenges: persistently high unemployment, slow rates of growth in public sector efficiency, and what appeared to be a very low capacity to change policy and spending priorities. All of these might well have cumulated into a serious welfare state crisis. Thus, for example, in the so-called "landslide election" of 1973, Denmark became the first Western democracy to experience a tax revolt and a corresponding reaction against welfare spending. But intense voter concern with taxes was short-lived, and twenty years later popular support for the welfare state is as strong as ever (cf. Goul Andersen, below).

Similarly, the first international oil crisis provoked a serious recession that then turned into the devastating combination of high inflation, growing unemployment, and stagnating economic growth. These problems ramified into spiraling budget and balance of payment deficits. However, since the beginning of the 1990's the Danish economy has improved substantially. Indeed, by the end of the 1990's, observers were speaking of a "Danish Miracle" paralleling the "Dutch Miracle."

Meanwhile, neither tax revolt nor economic stagnation did much initially to inhibit the growth of the Danish welfare state. Indeed, after the 1973 election, Danish public expenditures grew faster than all but one other OECD welfare state in the 1970s. However, in the 1980s public expenditure growth was brought under control and the Danish rate was significantly below the 1970s rates and significantly below rates in other OECD countries. From 1986 to 1991 the share of national income consumed by the public sector actually decreased, and then remained stable through the 1990s. Remarkably, politicians achieved macroeconomic stabilization and reductions in public expenditure growth without major cuts in the levels or content of social welfare services and transfers. The same occurred in most countries where welfare state expenditures continued to grow parallel to, or faster than, GDP. According to Alber (1988: 463), "[t]his suggests an interpretation of the recent period as a phase of consolidation rather than of welfare state dismantling." So the much-heralded "fiscal crisis of the state" (O'Connor, 1973), while not an illusion, proved to be a manageable problem.

Similarly, Denmark's membership in the EU and ERM has not led to welfare state downsizing or affected the level, content, organization and financing