

**INSTITUTIONAL COMPETITIVENESS:
A BROAD PERSPECTIVE ON THE DANISH CASE**

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EXECUTIVE SUMMARY

The ability of countries to achieve socioeconomic success depends not just on the macroeconomic policies that their governments pursue but also on the institutions within which their firms operate. In other words, national socioeconomic performance depends in part on the nation's institutional competitiveness, by which I mean its capacity to achieve socioeconomic success as a result of its political, economic, and cultural institutions.

This paper examines a few of the ways in which Denmark has achieved institutional competitiveness in the global economy during the last fifteen years or so. It argues that Denmark's impressive socioeconomic performance stemmed in part from its institutional capacities to generate strong economic growth and distribute the benefits of that growth rather equitably among the population. It also raises questions for the future that are intended to stimulate debate about how best to manage Danish institutions to ensure Denmark's institutional competitiveness in the future. In brief, the paper argues that Danish institutional competitiveness has stemmed from a combination of liberal and coordinated types of advanced capitalism, which have (1) increased the exposure of actors to market forces and (2) decentralized collective learning and decision-making institutions in ways that have enhanced the capacity of decision makers in the public and private sectors to collectively learn and flexibly adapt to their increasingly volatile and global environment. The flexicurity system and other labor market institutions are noted as examples. Other important points made in the paper include the following:

1. There is no one best institutional practice. Today the most successful countries—including Denmark—may have very different institutional profiles from each other.
2. High taxes and high levels of government spending have had positive rather than negative effects on Denmark's performance insofar as they have supported the other institutions that have provided for her institutional competitiveness.
3. Welfare spending should not be reduced significantly if social equality and, in turn, social cohesion are a national priority. This is important because social cohesion has contributed to Denmark's ability to adapt flexibly to globalization.
4. Institutions are tightly coupled. Changing one institution can have unintended consequences for the performance of other institutions. Hence, when things are going well, as they are in Denmark, decision makers ought to consider staying the course rather than pursuing major institutional changes.

INSTITUTIONAL COMPETITIVENESS: A BROAD PERSPECTIVE ON THE DANISH CASE¹

The ability of countries to achieve socioeconomic success depends not just on the macroeconomic policies that their governments pursue but also on the institutions within which their firms operate. In other words, national socioeconomic performance depends in part on the nation's institutional competitiveness, by which I mean its capacity to achieve socioeconomic success as a result of its political, economic, and cultural institutions.

Institutional competitiveness stems from the benefits that firms derive from operating within a particular set of institutions—benefits that afford them advantages over their competitors. For example, if firms operate where training and educational systems offer nationally coordinated apprenticeship programs rather than just general education, then their employees may be better trained to begin with and may have greater opportunities for upgrading their skills throughout their careers (Thelen 2004). If firms operate where finance capital tends to come from banks rather than stock markets, then they are often less pressured to maximize profit in the short term and more likely to take a more patient view that emphasizes increased market share, investment in research and development, and long-term growth (Dore 2000; Zysman 1983). If firms operate where labor unions are well organized rather than weak, where centralized corporatist rather than firm-level wage bargaining is the norm, and where works councils exist, then firms are more likely to experience cooperative relations with their employees, take part in subsidized job creation and training programs for the long term unemployed, and participate in active labor market programs that further improve the skills of workers (Martin and Swank 2004; Molina and Rhodes 2002; Streeck 1997, 1991)

In turn, if a highly skilled labor force, patient investment capital, cooperative labor-management relations, and the like enable firms to produce high quality goods, pursue long-term investment and productivity growth strategies, and use teams of workers and managers to collectively solve production and other problems—all in ways that enhance their international competitiveness—then these firms are institutionally competitive. That is, their competitive advantage stems from the institutions within which they operate. This is not to say that institutions are the only basis by which firms compete. But they are an important aspect of competitive advantage.

This paper examines a few of the ways in which Denmark has achieved institutional competitiveness in the global economy during the last fifteen years or so. It argues that Denmark's impressive socioeconomic performance stemmed in part from its institutional capacities to generate strong economic growth and distribute the benefits of that growth rather equitably among the population. It also raises questions for the future that are intended to stimulate debate about how best to manage Danish institutions to ensure Denmark's institutional competitiveness in the future. In brief, the paper argues that Danish institutional competitiveness has stemmed from a combination of liberal and

¹ The ideas in this paper are developed at length in several other places: Campbell (2004), Campbell and Hall (2006), Campbell et al. (2006), Campbell and Pedersen (2006, 2007).

coordinated types of advanced capitalism, which have (1) increased the exposure of actors to market forces and (2) decentralized collective learning and decision-making institutions in ways that have enhanced the capacity of decision makers in the public and private sectors to collectively learn and flexibly adapt to their increasingly volatile and global environment.

I begin by explaining how institutions affect national socioeconomic performance and that there is no one best practice when it comes to institutional arrangements that facilitate socioeconomic success. Second, I provide aggregate data demonstrating that there are multiple institutional routes by which national political economies can achieve success. Third, I explore some of the ways in which Danish institutions have contributed to success over the last fifteen years or so. Here I pay particular attention to labor market institutions, notably the so-called flexicurity system. Fourth, I raise some issues requiring careful thought with regard to how Denmark's institutions might (or might not) be changed in order to ensure the country's continued success. Specifically, I discuss the need to avoid overhauling the Danish taxation and welfare systems, particularly as they contribute to social cohesion, and the unseen dangers of major institutional changes.

MULTIPLE ROUTES TO SUCCESS: INSTITUTIONAL COMPLEMENTARITY

It is important to recognize that there is no one best practice when it comes to national socioeconomic performance. Different institutional types of capitalism each possess different institutional capacities for coping with market challenges. And each set of capacities may have unique advantages and disadvantages when it comes to competing in the global economy. So, institutional competitiveness can be achieved in different ways. In the broadest sense, this argument has been made for two very different types of capitalism: liberal market economies (LME), such as the United States, and coordinated market economies (CME), such as Germany and Sweden (e.g., Hall and Soskice 2001a).

Both LMEs and CMEs have institutional capacities—albeit different capacities—for being successful. For instance, firms in LMEs tend to compete on the basis of low cost and radical product innovation because they have institutions like weakly regulated labor markets as well as financial systems that impose short-term investment horizons but allow high risk taking. These enable firms to keep labor costs down, shed labor and close plants quickly, shift capital rapidly from one industry to another, and invest in risky but potentially revolutionary and lucrative research and development projects (e.g., breakthrough pharmaceuticals and software in the United States). Conversely, firms in CMEs compete more on the basis of quality and incremental innovation, such as adopting breakthrough technologies developed elsewhere or by improving production processes (e.g., numerically controlled machine tools in Germany; robotic auto assembly in Japan). This is because CMEs have institutions like cooperative industrial relations systems within firms, coordinated wage bargaining across firms, nationally coordinated vocational training programs, and financial systems that allow for long-term investment horizons. These produce highly skilled managers and workers who tend to cooperate in planning, trouble shooting, and the introduction of the latest technologies in ways that enhance product quality and improve production processes. Furthermore, LMEs tend to

promulgate neoliberal policies that sharpen market competition, such as economic deregulation, privatization, decentralization of government authority, and rolling back taxes and the welfare state. CMEs tend to eschew neoliberalism and instead promulgate policies that reinforce the capacities of actors for non-market coordination, such as by supporting corporatist bargaining and co-determination (Hall and Soskice 2001b; Soskice 1999).

The point is not just that there is more than one way to achieve success in the global economy and that these routes are to a degree institutionally determined, but that success depends on how well these institutions are integrated with each other. Specifically, the capacity of any country to perform well depends in part on its institutional complementarities. By institutional complementarity I mean that a country's institutions fit together such that the functioning of one depends on and enhances the functioning of the others. For instance, the returns from a stock market trading in corporate securities are likely increased by regulations requiring a fuller exchange of information about companies than by regulations that require less corporate transparency (Hall and Soskice 2001b, pp. 17-18). Institutional complementarities can exist within and across many areas of economic activity, including labor markets and industrial relations systems, vocational training and education systems, corporate governance systems, inter-firm relations, and relations with employees. The greater the complementarity among institutions governing the economy, the more successful the economy will be (Hall and Soskice 2001b, p. 45; see also Hall and Gingerich 2004).

Complementarity is often defined in terms of institutional similarities. That is, a set of institutions that coordinate economic activity either by market-based or non-market-based means, but not both, will yield socioeconomic results that are better than hybrid sets of institutions (e.g., Hall and Soskice 2001b). I accept that this form of complementarity may contribute to strong socioeconomic performance. But I also recognize that functional complementarity may arise from situations in which very different types of institutions coexist in a heterogeneous or hybrid mix such that they compensate for each other's shortcomings and deficiencies (e.g., Crouch 2005, chap. 3). Complementarities based on institutional heterogeneity may broaden the repertoire, knowledge base, and range of choices available to decision makers. In turn, this can afford decision makers high levels of flexibility and innovative capacity that can enhance socioeconomic performance—especially when markets are volatile and product life cycles are short as is increasingly the case under conditions of economic globalization (e.g., Whitley 1999).²

COMPARING DENMARK WITH OTHER COUNTRIES

A case that different institutional configurations can produce complementarities that facilitate socioeconomic success and that there are different ways to achieve institutional competitiveness (i.e., that there is no one best practice) is apparent if we compare some of the advanced capitalist countries over the last fifteen years.

² For further discussion of these issues, see the symposium on “Institutional Complementarity and Political Economy” in Socio-Economic Review 3(2), 2005.

Socioeconomic performance has many dimensions. I focus on several using standard measures that are generally accepted by researchers working in the area of comparative political economy. When taken together these give a good overall picture of a country's socioeconomic performance. Denmark's performance was much less impressive from the mid-1970s through the early 1990s than it has been since then—both in its own right and in comparison to other OECD countries. Indeed, until the late 1980s and early 1990s Denmark's performance was lackluster in terms of things like average GDP and productivity growth rates, unemployment, inflation, budget deficits, and national debt (e.g., Campbell and Hall 2006, tables 2-6). Since then, however, her performance has improved considerably and matched or exceeded most other advanced capitalist countries—including some with very different institutional arrangements.

Table 1 compares Denmark's performance on several social, economic, and fiscal measures during the 1990s and early twenty-first century with the performance of three other countries with much different institutional profiles: the United States, Germany, and Sweden. Germany and Sweden are good examples of CMEs whereas the United States is a good example of a LME (e.g., Hall and Gingerich 2004; Kenworthy 2006). Denmark is more of a hybrid with significant elements of both CME, such as a very generous welfare state and corporatist bargaining, and LME, such as few state owned enterprises and limited employment protection (Campbell and Pedersen 2007; Pedersen 2006). The comparison between Denmark and the United States is especially interesting insofar as the United States has been among the strongest economies in the OECD during the last decade or so.

Table 1 about here

Among the social indicators in table 1, GDP per capita in Denmark, while a few thousand dollars less than in the United States, was still among the very highest in the world. It was also a few thousand dollars more than it was in either Sweden or Germany. All four countries were extremely prosperous, particularly in view of their very high scores on the U.N. Human Development Index. However, Denmark outperformed the United States in terms of income and gender inequality, poverty rates, and illiteracy rates, all of which were lower in Denmark than in America. It also outperformed Germany on all of these indicators, except poverty, where there was less than one percentage point difference. Sweden performed a bit better than Denmark on the gender inequality, poverty, and illiteracy measures, which is not surprising since Sweden has a reputation for being among the most egalitarian countries in the world. Still, by all accounts Denmark is also among the most egalitarian countries (World Economic Forum 2003, p. 42)—a point to which I will return later.

Among the economic indicators, table 1 reveals that Denmark's performance was again impressive. Danish growth in GDP was roughly the same as in Sweden and better than in Germany. The United States performed the best although its growth rate was surely inflated due to the dot-com bubble during the late 1990s that eventually burst and reduced growth rates after that. Productivity growth rates were virtually identical for

Denmark, Sweden, and the United States whereas Germany experienced a slower growth rate. Similarly, unemployment was about the same in Denmark, Sweden, and the United States, but higher in Germany.³ Inflation was about the same in Denmark and the United States and somewhat higher than in either Sweden or Germany. However, at 2.3 percent annually, Danish inflation was well under control.

Finally, among the fiscal indicators in table 1, Denmark had the largest government budget surplus of the four countries although it had more national debt as a percentage of GDP than either Germany or the United States. Nevertheless, Denmark began to pay down its debt, which had ballooned during the 1970s and 1980s due to profligate fiscal policies. She also began to post annual budget surpluses of about 1 percent of GDP through 2004. In notable contrast, the United States, largely through a combination of income tax reductions and expansive military spending, managed to replace its budget surpluses of the 1990s with deficits running as high as 4.4 percent of GDP by 2004—deficits that have contributed to a skyrocketing national debt somewhere in the vicinity of 7 trillion dollars (*The Economist* 2005, p. 97). Similarly, in 2004 and 2005, as a result of sluggish economic performance and the continuing costs associated with reunification, Germany's fiscal performance deteriorated and exceeded the budget deficit limit of 3.0 percent of GDP required of members of the European Monetary Union to which it belongs.

Note that Denmark achieved strong socioeconomic performance with very high levels of central government spending and taxation. Table 2 shows that the level of central government spending as a percentage of GDP was higher in Denmark than it was in the United States and Germany. Of these four countries, only Sweden spent more as a percentage of GDP. But in terms of social expenditures (i.e., welfare state spending), Denmark spent roughly the same as a percentage of GDP as Sweden, but considerably more than Germany and especially the United States. Indeed, the Danish welfare state is among the most generous in the world. Moreover, the level of taxation, including the tax burden on capital, was virtually the same for Denmark and Sweden and considerably higher than it was in either Germany or the United States. Over all, the level of taxation and state spending in Denmark was very high by OECD standards and had been for many years (Abrahamson 2006; Campbell 2004, tables 5.1-5.3; Goul Andersen 2005; Swank 2002, pp. 142-47).

Table 2 about here

This is important because some scholars have argued that in advanced capitalist countries, high taxes, large state budgets, and generous welfare states will drive away the investment capital that is needed for developing new technologies, products, and industries, improving labor productivity, stimulating economic growth, controlling inflation, and otherwise enhancing socioeconomic performance (e.g., Cerny 1997; Genschel 2002; McKenzie and Lee 1991; Ohmae 1995, 1990). Following this logic, calls

³ Some argue that U.S. unemployment would have been 1-2 percent higher if its high rate of incarceration was considered. In that case, Danish and Swedish unemployment would have been lower than America's (Western and Beckett 1999).

for deep cuts in taxes and spending have become the political mantra for neoliberal politicians in Europe and North America since the late 1970s. Yet the Danish case suggests that countries can have both high taxes and generous spending and still achieve impressive socioeconomic performance. Indeed, Denmark's performance as represented in table 1 is comparable to that of the United States—a country with much lower levels of taxation and spending. This is another point to which I will return later.

Over all, then, the performances of Denmark, Sweden, and the United States were all strong and largely similar to each other, except for inequality where the United States lagged behind. Germany's performance was less impressive. Indeed, the World Economic Forum (2005) ranked Denmark, Sweden, and the United States among the top five most competitive economies in the world in 2004. Germany was ranked thirteenth. This is consistent with the findings in table 1. What all of this tells us is that countries with very different institutional profiles can achieve remarkably similar and successful socioeconomic performance. In short, there is no one best practice.

Although quantitative comparisons of aggregate data across countries are useful for establishing associations between institutions and socioeconomic performance, they are less helpful for teasing out the causal mechanisms that link institutions to performance. One way to address this problem is to examine the relationship between institutions and socioeconomic performance through more qualitative data. I do this now for Denmark and focus on one important area where the benefits of institutional complementarity have been especially evident.

DANISH LABOR MARKET INSTITUTIONS

In Denmark, almost all workers belong to unions and are covered by collective bargaining agreements reached through corporatist institutions (Hicks and Kenworthy 1998). In this regard, Denmark clearly exhibits traits associated with CMEs. However, the Danish approach to unemployment and labor market policy has recently involved some significant elements of the LME model as well. Indeed, Denmark has become more of a hybrid located somewhere between the purer LME and CME types.

To begin with, Danish labor market policy during the 1990s has been described as a system of “flexicurity,” which consisted of three basic elements (Madsen 2006). First, Danish employees in the private sector have long had rather limited levels of employment protection (e.g., regulations governing firing, severance pay, etc). Hence, employers had much latitude to hire and fire workers in response to market signals as is typical of LMEs. In this regard, Denmark had one of the most flexible labor markets in the European Union (World Bank 2004, p. 36). Among the advanced capitalist economies the over all level of employment protection in Denmark was well below that of the classic CMEs, Sweden and Germany, and much closer to the LMEs, Britain, Canada, New Zealand, and Australia (Estevez-Abe et al. 2001, p. 165). As a result, job mobility was quite high in Denmark compared to many other countries. During the early 1990s the median job tenure in Denmark was a relatively short 4.4 years—virtually the same as

it was in the United States and Britain and about half of what it was in Germany (10.7 years) and Sweden (7.8 years) (Estevez-Abe et al. 2001, p. 170).

Second, however, workers were not left alone to manage such employment uncertainties. Denmark offered generous unemployment policies, health insurance, and other welfare benefits on a universal basis, as is typical in CMEs, to ensure that when workers became unemployed they would have a social safety net that was substantial enough to protect them and their families from some of the worst problems associated with unemployment. Unemployment policies were generous in Denmark compared to most other EU and OECD countries, including those with large welfare states, such as Sweden, Germany, and the Netherlands (Hansen 2000, p. 33). Indeed, during the early 1990s Denmark's level of unemployment protection was greater than any other advanced capitalist country (Estevez-Abe et al. 2001, p. 168). That said, during the early 1990s these policies were reformed insofar as unemployment benefits were tied much more closely to requirements for employment seeking. Moreover, policy makers tightened eligibility rules for recipients and some benefit levels were reduced (Abrahamson 2006; Goul Andersen 2002). These so-called "activation" policies are typical of LMEs like the United States where, for example, during the 1980s and 1990s welfare benefits were tied more tightly to job hunting (i.e., workfare), eligibility for benefits was restricted, and benefit levels were reduced (e.g., Weir 1998). Activation has also become an important part of neoliberal welfare reform in various west European countries besides Denmark (Streeck and Thelen 2004, p. 24).

Third, and reminiscent of CMEs, Denmark developed in the early 1990s an extensive set of active labor market policies established in law that helped unemployed workers obtain new skills and training so that they could return to work. Workers also received assistance and encouragement in locating job opportunities for which they could apply. As a percentage of GDP, Denmark spent more on active labor market programs since 1993 than any other OECD country except Sweden (OECD 2004). And by the late 1990s workers spent more time in training and skill formation programs than did workers in any other member of the European Union (Eurostat 2003). Although Denmark has long had a national vocational training system with curricular and other issues worked out through corporatist negotiations between unions and employers with the state shouldering many of the costs involved, several important changes occurred in the late 1980s and early 1990s that improved the functioning of the system. (1) Negotiations over the organization of curriculum and some other aspects of that system were decentralized (Martin 2005, 2006). (2) Unions and employers negotiated training agreements through which they collaborated in upgrading the skills of blue collar workers, such as by letting workers spend more time away from work in academic courses and training programs, often with state subsidies for tuition, wage supplements, and the like. (3) Vocational training was made available to the unemployed on a widespread basis so that they could upgrade their skills while they were out of work (Kristensen 1996, 2006; Martin 2005, 2006)

Insofar as today's global economy requires greater reliance on skills, learning, and labor market flexibility, the flexicurity system was especially well equipped to help

Denmark perform successfully in the global economy. Studies show that the flexicurity system helped to reduce Denmark's unemployment rate during the 1990s (Goul Andersen 2002, p. 149; Madsen 2006).⁴ It allowed employers flexibility in hiring and firing; it cushioned the blow incurred by workers through job loss; it encouraged and helped the unemployed to find new jobs; and it helped retrain workers toward these ends. Furthermore, because workers were highly skilled, they could move with relative ease among different jobs across and within firms further enhancing labor market flexibility as well as their own job opportunities. Better training also enabled firms to introduce new and more flexible types of work organization, such as project teams and lean production techniques, which enabled them not only to introduce and adapt quickly to new information technologies, but also to search for continuous improvements in production processes themselves without enlarging cumbersome administrative hierarchies (Dobbin and Boychuk 1999; Goul Andersen 2003; Kristensen 1996).⁵ And, by paying more attention to training the unemployed, when workers eventually returned to work they were equipped with new skills and a better understanding of the new flexible forms of work organization that they were likely to encounter on the job (Kristensen and Zeitlin 2005, chap. 3; Martin 2006). Even skeptics of the flexicurity system agree that the system prepared the labor force for economic upturns and prolonged these upturns by avoiding situations where there were acute shortages of certain types of labor (Green-Pedersen and Lindbom 2005, p. 81). Finally, because the Danish vocational training system enabled workers to acquire new skills faster and more broadly than in many other countries, it created incentives for firms to modernize technologically and to constantly improve their production processes and strategies—especially if they wanted to prevent their most skilled workers from leaving for more interesting and promising jobs (Kristensen 1996).

The Danish labor market benefited from additional sources of flexibility—many having to do with institutional decentralization. To begin with, in recent years, as a result of labor market reforms and corporatist bargaining, important elements of the welfare programs, active labor market policies, and some aspects of collective bargaining agreements were decentralized to the regional level and sometimes to the level of individual firms. For example, as a result of legislation passed in 1993, job retraining programs and other aspects of active labor market policy were tailored at the regional and local levels to fit the needs of local employers. This was accomplished through decentralized negotiations among unions, employer groups, municipal authorities,

⁴ There is debate about exactly how much credit should be given to the flexicurity system for improving Danish socioeconomic performance as opposed, for example, to the pursuit of stable exchange rates, tighter monetary policy, an undervalued currency, deficit reduction, increased debt-driven consumer demand, more generous educational, parental, sabbatical and early retirement leave-schemes, and swings in the business cycle (Green-Pedersen 2003; Green-Pedersen and Lindbom 2005; Marcussen 2000; Schwartz 2001). However, most analysts accept that the flexicurity system was a contributing factor and that it is difficult to determine exactly how much each of these things contributed to Denmark's declining unemployment and rising employment rates during the 1990s (e.g., Green-Pedersen and Lindbom 2005).

⁵ For instance, shop stewards in the metalworking industry invented new payment, training, and job classification systems to increase the flexibility of production and increase the general skill level among workers (Sabel 1994, p. 136).

educators, and other relevant actors at the regional and local levels over curricular and other issues (Madsen 2006, p. 336; Martin 2005, 2006; Torfing 1999, p. 388).

In addition, provisions in general labor agreements for flexible working hours (i.e., flextime) were expanded after 1995. This made it easier for workers to negotiate work schedules with employers at the firm level. It also made it easier for families to juggle the demands of work and family, which enabled more people, especially women with young children, to enter the labor force. On the one hand, this provided employers with a larger pool of workers from which to choose. On the other hand, it gave workers more opportunities for employment. As a result, the Danish labor market was among the most flexible in Europe in terms of work scheduling (EIRO 1998).

Finally, wage bargaining, which had been managed through centralized corporatist arrangements at the national level, was decentralized in the late 1980s. Industrial-level associations of trade union and employer's organizations took over wage bargaining within limits set by the general organizations. This was done in the belief that excessive wage increases during the 1980s had damaged Denmark's international competitiveness and fueled recession. The new decentralized system delivered wage moderation at the end of the 1980s and beginning of the 1990s that helped lift Denmark out of recession (Green-Pedersen and Lindbom 2005, p. 73).

The important point here is that although Danish union density ratios remained among the highest in the world, employers remained well organized through business associations compared to many other countries, and the vast majority of workers were still covered by collective bargaining agreements—conditions that were typical of CMEs—decentralization of bargaining regarding job training, work scheduling, wages, and the like, especially to the level of individual firms, represented another move in the direction of LMEs (e.g., Lash and Urry, 1987, chap. 8). To be sure, decentralization did not signal the complete abandonment of coordinated decision making. But it was a step in the direction of the LME model. Indeed, Danish decision makers viewed decentralization of this sort as a way to translate a piece of the neoliberal model into the Danish context (Kjær and Pedersen 2001). Moreover, decentralization infused the system with an additional element of institutional flexibility that better fit the needs of employers trying to adjust to the global economy (Wilthagen and Tros 2004).

Over all, then, changes in Danish labor market institutions worked insofar as they helped reduce unemployment and afford firms the flexibility required to respond to market signals in ways that can improve socioeconomic performance. Corporatist bargaining, generous welfare programs, and active labor market policies—all typical of CMEs—were part of the story. But so too was the coupling of already low levels of employment protection with more stringent activation requirements and decentralized bargaining over issues like work schedules, vocational training programs, and wage bargaining—features more closely related to LMEs, particularly insofar as they occurred at the industry, local, or firm level. Rather than undermining labor market performance, the institutions involved complemented each other in ways that enhanced it.

DISCUSSION AND ISSUES FOR FURTHER CONSIDERATION

To summarize briefly, increasing institutional flexibility emerged in Denmark and helped to improve socioeconomic performance in the labor market. This was accomplished in two complementary ways. First, following the LME model, actors were increasingly exposed to market forces (e.g., activation policies; low employment protection; etc.). This increased the sensitivity of firms, workers, and others to new production and employment opportunities and enabled them to pursue these opportunities. Second, following the CME model, collective decision making and learning were preserved; but they were also decentralized in ways that were reminiscent of the LME model (e.g., local negotiations over worker training and work schedules; industry-level wage bargaining; etc.). This helped firms, workers, and other actors better identify problems and opportunities, such as by tailoring vocational training programs to the needs of local firms and workers, including the unemployed, and increasing the skill levels of workers, which facilitated a variety of technological and organizational innovations in firms and further enhanced their flexibility in responding to market forces. Thus, increased market exposure combined with decentralized collective learning and decision making increased the institutional heterogeneity and flexibility of the Danish political economy in ways that helped improve its performance over all. In other words, (1) greater exposure to market forces coupled with (2) decentralized, but still coordinated learning and decision making provided significant institutional complementarities. As I have argued elsewhere, the move toward increased market exposure, decentralization, and institutional heterogeneity also enhanced Denmark's institutional complementarities and competitiveness in other areas (Campbell and Pedersen 2007).

All of this raises several issues for further consideration. All have been subject to political debate in the past and I suspect will continue to be subject to more debate in the future. I do not claim to have the final word on any of them. My purpose is only to present a point of view that might help sharpen the terms of debate in ways that decision makers might find useful.

Fiscal Regimes and Institutional Complementarity

I noted earlier that taxation and state spending are considerably higher in Denmark than in most other advanced capitalist countries. This is one area where Denmark very closely fits the CME profile. Some people have argued that high taxes and government spending are a recipe for socioeconomic disaster, especially for countries with very open economies. This does not seem to have happened in Denmark. In fact, one could argue that high levels of taxation and state spending have actually contributed to Denmark's success insofar as they helped finance the development and maintenance of flexicurity labor market institutions, vocational training and skill formation institutions, and other institutions that have contributed to Denmark's recent success. As a result, the existing taxation and state spending systems, including Denmark's generous welfare programs, can actually be viewed as positive contributions to socioeconomic performance. Why?

The Danish fiscal regime interacts with these other institutions in ways that provide another source of institutional complementarity within the Danish system. After all, by supporting flexicurity, training, and these other institutions, the fiscal system has helped Denmark achieve considerable socioeconomic success, including low unemployment, high GDP per capita, and a very affluent society. In turn, this has provided a strong tax base from which the state can extract revenues and finance its spending.⁶ Indeed, the interaction between the fiscal regime and these other institutions is such that each one benefits from the other in symbiotic fashion. Although scholars have long recognized that small, economically open, advanced capitalist countries seem to require high levels of taxation and spending in order to compensate for the fact that they are often buffeted by the currents of the global economy (e.g., Cameron 1978; Garrett 1998; Swank 2002), proponents of lower taxes and less government spending often ignore the importance of fiscal systems in this regard.

Business seems to understand this in Denmark. High taxes are not a deterrent for business, at least insofar as business recognizes that high taxes underwrite a variety of infrastructures and other institutional benefits that they enjoy. For instance, according to the head of the European division of a large U.S. software firm, the company recently picked Copenhagen for its headquarters in part because of these sorts of public infrastructures; high taxes were neither a serious consideration, nor a deterrent.⁷ Further, as I understand it, promises of tax breaks were not made to encourage firms to move into the new science park near Roskilde University. Instead, what mattered was its proximity via improved public transportation (i.e., a new rail station) to Copenhagen with its cultural benefits, the availability of child care for workers, well-trained workers, and synergies between the university and the firms in the park. These attitudes are consistent with recent scholarship, which suggests that taxation is often not as important when it comes to business investment decisions as others have assumed and that businesses may not resist high taxes as long as they recognize that they will reap infrastructural, cultural, social service, and other benefits from them (Campbell 2004, chap 5; Jensen 2006; Kiser and Laing 2001; Swank 2002).

Evidence also suggests that the Danish population appreciates the institutional complementarities associated with their fiscal regime. Surveys suggest that about 85 percent of Danes are now content with their taxes—even though they are among the highest in the world. More important, roughly two thirds of the population would prefer improved public services rather than lower taxes. The population seems to realize that cuts in taxes could undermine some of the other institutions that have contributed to Denmark's high standard of living and socioeconomic performance (Goul Andersen 2005). Certainly there has been no groundswell of support for reforms of either the tax system or state spending. The same is true of other European countries that are

⁶ Additionally, this system of taxation and spending has paid for the public transportation, telecommunication, information technology, research and development, and other infrastructures upon which firms operating in Denmark depend so heavily. The Danish national health care system is a good example. Other more recent examples include such projects as the Øresund regional development project south of Copenhagen, the Øresund bridge to Sweden, new renovations to Copenhagen airport, the Great Belt Link bridge that connects eastern and western Denmark, and the new Copenhagen metro system.

⁷ Personal communication with Ove K. Pedersen.

preserving their high corporate and other tax rates in order to continue funding social welfare programs (e.g., International Herald Tribune 2005, p. 14; Kenworthy 2004, pp. 134-36).

That Denmark's socioeconomic performance was so similar to that of the United States is worth further comment in this context. The United States has been on the forefront of neoliberal tax, welfare, and regulatory policy reforms since the early 1980s (Campbell 1998; Pierson 1994; Vogel 1996). From a neoliberal perspective, which advocates lower taxes, government spending, and state regulation of economic activity, one would expect the United States to considerably outperform Denmark because Danish taxes and government expenditures are much higher than they are in the United States and because Denmark is a much more open economy than the United States.⁸ The fact that Denmark has performed so well vis-à-vis America despite of her much higher levels of taxation and government spending is surprising from a neoliberal perspective, but makes sense from the point of view of the institutional complementarities involved.⁹

Welfare Spending and Social Cohesion

I have provided evidence that supports the argument that there is no one best way to organize a country's political economic institutions in order to be successful in today's global economy. We have seen that countries with very different institutional profiles performed quite well during the 1990s and early twenty-first century. However, there seems to be one exception to this rule. To return to a second point made earlier, recall that Denmark has less income and social inequality than most other advanced capitalist countries in the world—particularly the United States where, despite moderate growth in average real wages during the 1990s, income inequality persisted. Sweden and Germany also had less inequality than the United States. In the Danish case, this is due in part to the effectiveness of Denmark's welfare, educational, labor market, and other institutions as well as the fiscal system that helps to finance them. While there may be more than one route to economic success as measured by things like productivity growth rates, unemployment, and inflation, the same may not be so true when it comes to the issues of income equality, gender equality, and poverty. In this case, the CMEs—and the hybrids that have the right CME and LME elements—may be better than the LMEs at reducing

⁸ In 1999, trade in goods was 67.8 percent of GDP in Denmark compared with only 19.8 percent in the United States. Gross foreign direct investment was 13.3 percent of GDP in Denmark and only 5.2 percent of GDP in the United States. And gross private capital flows across its borders were 25.4 percent of GDP in Denmark and only 13.6 percent in the United States (World Bank 2001, Table 6.1).

⁹ Denmark's performance vis-à-vis the United States is all the more impressive when we recognize some of the other advantages the United States enjoyed. The United States is a large state and world power. It has the capacity to shape the rules of global commerce. It did so at the Bretton Woods conference after the Second World War; it did so in 1971 when it abandoned the Bretton Woods fixed exchange agreement; and it has done so at other times since then. Denmark does not have the capacity to shape these rules. Furthermore, the United States enjoys the benefits of seigniorage: the dollar has been the principle reserve and transaction currency for much of the world since the Second World War. This has enhanced America's global economic and political position because, unlike other countries, it could print dollars for all sorts of economic purposes; go deeply into debt without fearing negative consequences, at least in the short term; and enjoy fewer economic restraints. Indeed, even after the Cold War, the role of the dollar as the world's key currency allowed the United States to live well beyond its means (Gilpin 2000, pp. 60-61, 120-21).

inequality, as others have maintained (e.g., Hicks and Kenworthy 1998). It is often suggested that there is a trade off between economic growth and social equality. The evidence presented here and elsewhere supports those who have argued that this is not the case (e.g., Kenworthy 2004). Denmark seems to have accomplished both wealth creation and a comparatively equitable distribution of that wealth.

This is important especially insofar as it bears on social cohesion. If it is the case, as some have argued (Katzenstein 2000; Zak and Knack 2001), that one important ingredient for socioeconomic success is social trust and cohesion—that is, a collective commitment to national goals that often underlies the more individualistic goals of interest groups, political parties, social classes, and the like—then maintaining high levels of social equality is important economically. After all, why would workers, for example, continue to moderate their demands of employers in the interest of improved economic productivity and growth if they believed that they were not getting a fair share of the benefits from such improvements? Indeed, cross-national research shows that higher levels of economic equality and opportunity lead to more social trust and cohesion (Rothstein 2005).

Denmark has been able to establish high levels of social cohesion and trust (Katzenstein 2000; Rothstein 2005). How? Among other things, these things have been based historically on a national commitment to social programs and equality.¹⁰ To be sure, social programs are not the entire story. For instance, the repeated loss of wars and in turn territory, most notably in 1864 when Denmark lost to Prussia a portion of southern Jutland and the German speaking duchies of Holstein and Schleswig, helped Denmark develop a unified and politically stable nation with a strong national identity (Korsgaard 2006). But one of the most important mechanisms through which a cohesive identity was forged involved passage of a series of acts, beginning in 1891, that laid the foundation for various state supported social programs that were intended explicitly to reduce inequality and class differences and, therefore, further unite the Danish people—programs that have been extended since then and to which the Danish people have become very attached (Kaspersen 2006).

The point is that efforts to shrink or restrict eligibility to the welfare state—and by implication the flexicurity system of which it is a part—may have the unintended consequence of undermining the very social cohesion that has helped Denmark survive as a nation historically and that has likely contributed to her ability to engage in the sorts of collective learning, cooperation, and negotiation discussed above that have been important elements in the Danish route to socioeconomic success in the globalization era.

Along these same lines, the recent influx of immigrants into Denmark, which actually remains quite small as a percentage of the population compared to other countries like France, Germany, and the United States (OECD 2005), and that has produced considerably less ethnic, linguistic, or religious fractionalization (Alesina et al.

¹⁰ Social programs and the welfare state have often been used in other advanced capitalist countries to reinforce solidarity and social cohesion at both the national and sub-national levels (Béland and Lecours 2005a, 2005b).

2003), poses a potential problem for social cohesion. If Denmark insists that immigrants must be fully incorporated into its society with the intention of permitting immigration but preserving a high level of social cohesion, then efforts must be made to make this work. Specifically, resources must be dedicated to help immigrants assimilate and feel that they are truly a part of Danish society. For instance, if learning the Danish language is required of immigrants in order for them to achieve citizenship, then sufficient resources must be made available to them for learning the language. In other words, social programs, vocational training, and other resources must be mobilized toward that end, if maintaining social cohesion is a national priority.

Similarly, maintaining universal social programs is important in this regard. Universal programs are those that serve all citizens regardless of their income as opposed to means-tested programs that are intended only for low-income people. Evidence suggests that countries, such as the United States, that rely more on means-tested programs have higher levels of economic inequality and, in turn, lower levels of social trust and cohesion than countries, such as Denmark and Sweden, that rely more on universal programs (Rothstein 2005).

Tight Coupling, Ripple Effects, and the Desirability of Institutional Change

Finally, institutions often come in tightly-coupled sets; they are interlocked with each other. So changing one institution—especially radically—can have unintended consequences for other institutions in ways that affect socioeconomic performance. For instance, tighter eligibility for various welfare benefits may have helped push people back into the labor market thereby reducing unemployment, but it has also contributed to an increase in the poverty rate in Denmark and the increasing marginalization of certain segments of the population. Notably, the implementation of the so-called “start allowance” for people having lived in Denmark for less than eight years, and which provides claimants with somewhere between 45 and 64 percent of traditional social assistance, has raised income poverty to a level not seen before in Denmark (Abramson 2006, pp. 370-71). In turn, if the marginalization of certain immigrant groups in society becomes more widespread, it may begin to undermine the kind of social cohesion discussed above that arguably has contributed to Denmark’s continued socioeconomic prosperity.

As it happens, institutional change is generally incremental when it occurs (Campbell 2004; Pierson 1994; Streeck and Thelen 2004). So the tendencies for decision makers to unintentionally set off ripple effects that reverberate with unanticipated consequences throughout the political economy are slim. The lesson here is twofold. First, attempts to import models that appear to have worked well in other countries may not yield similar benefits in the recipient country because the changes involved may conflict with or otherwise undermine the positive institutional complementarities already at work. In other words, imposing new institutional practices and overhauling policies in one area may conflict with those already in place in other areas thereby wrecking whatever positive synergies there may have been among them. Second, given the quite positive institutional complementarities that seem to be operating in Denmark at the

moment, decision makers should proceed with great caution before changing the institutions and policies in question. Americans are fond of saying, “If it isn’t broken, don’t try to fix it.” In light of her recent impressive socioeconomic success, this advice may be especially apropos for Denmark today.

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Table 1. Socioeconomic Performance

	Denmark	Sweden	Germany	USA
<i>Social Indicators</i>				
GDP per capita 1998 (1990 US\$)	\$22,123	\$18,685	\$17,799	\$27,331
U.N. Human Development Index ^a 2002	.932	.946	.925	.939
Income inequality 2000 (gini)	.247	.252	.252	.368
Gender inequality 2002 (ratio of female to male income)	72%	83%	52%	62%
Poverty rate 2002 (% population below 50% of median income)	9.2%	6.5%	8.3%	17.0%
Illiteracy rate 1994-1998 (% ages 16-65 lacking functional literacy)	9.6%	7.5%	14.4%	20.7%
<i>Economic Indicators</i>				
Average GDP growth 1996-2000	2.7%	3.0%	1.8%	4.0%
Average productivity growth 1996-2000	2.3%	2.2%	1.1%	2.2%
Average unemployment 1996-2000	5.1%	4.6%	8.3%	4.6%
Average inflation 1996-2000	2.3%	0.5%	1.2%	2.5%
<i>Fiscal Indicators</i>				
Government budget surplus/deficit 1998 (% GDP)	+1.7	-0.5	-0.9	+0.8
Government debt 1998 (% GDP)	64.0	----	38.6	42.8

^aThe Human Development Index is a compilation of measures of life expectancy at birth, adult literacy rate, gross school enrollment, and GDP per capita.

Sources: GDP per capita are from Maddison (2001, Table A-1c); gini coefficients for USA, Sweden, and Germany are from Mischel et al. (2005, p. 401); gini coefficient for Denmark is for the mid-1990s and is from the World Bank (1998, Table 2.8); human development index, poverty rates, literacy rates, and gender inequality data are from the United Nations (2004, pp. 139, 150, 221); all economic indicators are from OECD (2002, Tables 1, 13, 14, 19); all fiscal indicators are from World Bank (2001, Table 4.11).

Table 2. Government Expenditures and Taxes

	Denmark	Sweden	Germany	USA
<i>Expenditures</i>				
Total central government expenditures 1998 (% GDP)	37.3%	41.6%	32.6%	19.9%
Government social expenditures 1998 (% GDP)	30.8%	30.4%	27.4%	14.5%
<i>Taxation</i>				
Total central government revenues 1998 (% GDP)	38.5%	38.2%	31.3%	20.7%
Effective tax rate on capital ^a 1996	52.0%	53.0%	24.0%	37.0%

^aThe effective tax rate on capital represents the total tax burden on capital income. This consists of taxes on property income and immovable property plus taxes on unincorporated and corporate enterprise profits plus taxes on capital and financial transactions all as a percentage of operating surplus.

Sources: Central government revenues and expenditures are from World Bank (2001, Table 4.11); social expenditures are from OECD (2005); effective tax rate on capital is from Swank (2004).