

# Danish reform policy

Reykjavik  
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# Denmark, an economic success story?



- GNI per capita USD 80.491 (2022). No. 5 in the world
- Fiscal sustainability 1½ per cent of GDP
- Net government debt eliminated
- Unemployment 2.9 per cent (April 2024)
- Current account 11.1 per cent of GDP (2023)
- Inflation 2.2 per cent (May 2024)

# Questions



- Is Denmark proof that socialism can work, or that welfare-statism is a superior economic system?
- Has Denmark always been an economic success story, or what did it take?
- Did the welfare state make Denmark rich?

# Some answers

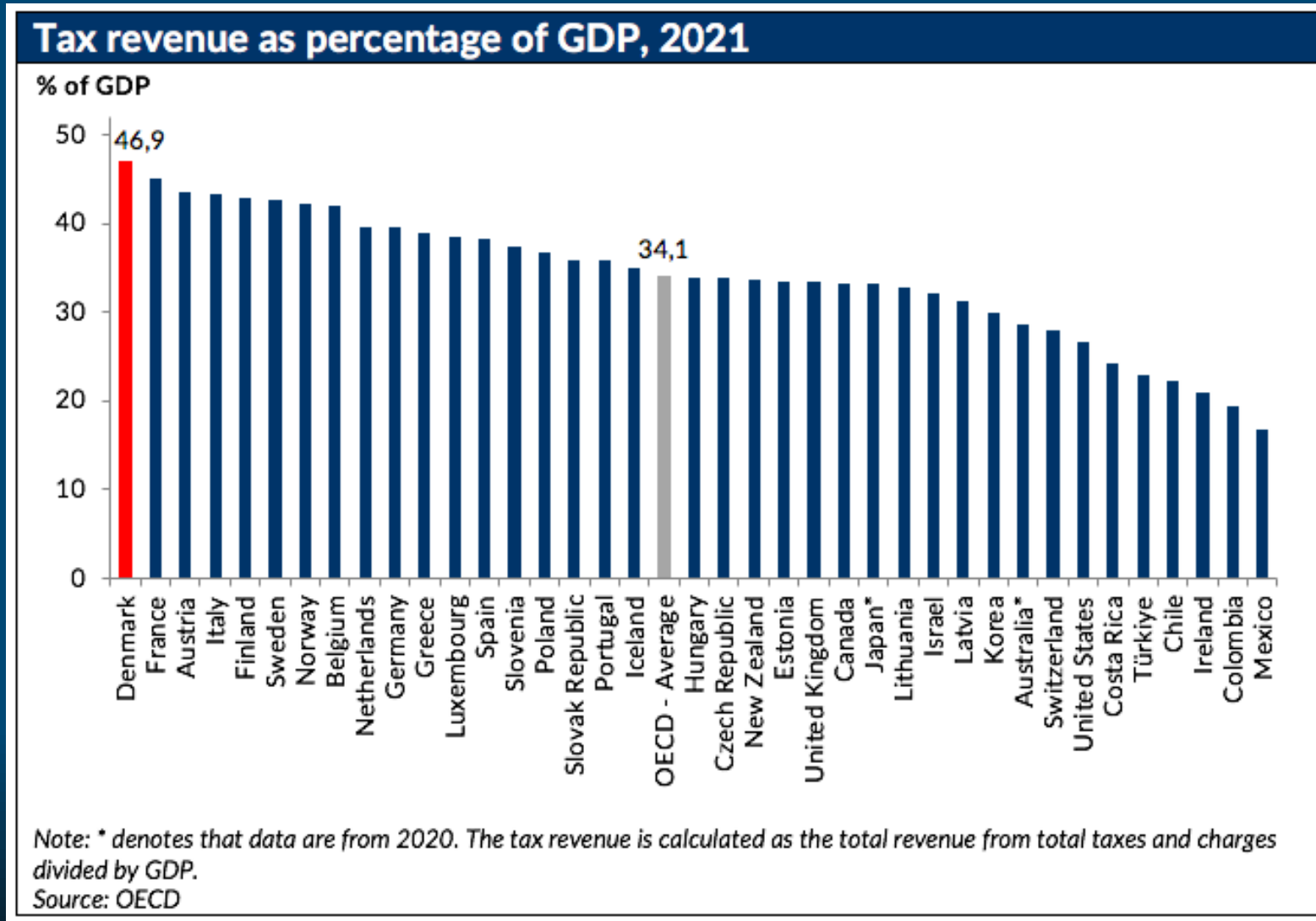
- Denmark is not socialist
- Denmark was rich long before the welfare state was introduced
- The introduction of the welfare state created huge economic imbalances
- Denmark had to undertake decades of economic reforms to deal with them

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# Taxes are high



# High economic freedom ranking

- Denmark is no. 7 on the Economic Freedom of the World Index (Fraser Institute et al).
- Denmark is no. 7 on the Heritage Economic Freedom Index
- Denmark is no. 3 on the CATO Institute Human Freedom Index

# Danish score on the EFI (rank)

<b>Overall score</b>	<b>8.1</b>	<b>(5)</b>
Size of government	5.2	(143)
Legal system and property rights	9.1	(2)
Sound money	9.6	(7)
Freedom to trade internationally	8.3	(31)
Regulation	8.4	(4)
<i>Credit market regulation</i>	<i>10.0</i>	
<i>Labor market regulation</i>	<i>7.3</i>	
<i>Business regulation</i>	<i>7.1</i>	
<i>Freedom to compete</i>	<i>9.1</i>	

(Max. score: 10.0)



# Nordic countries on EFI

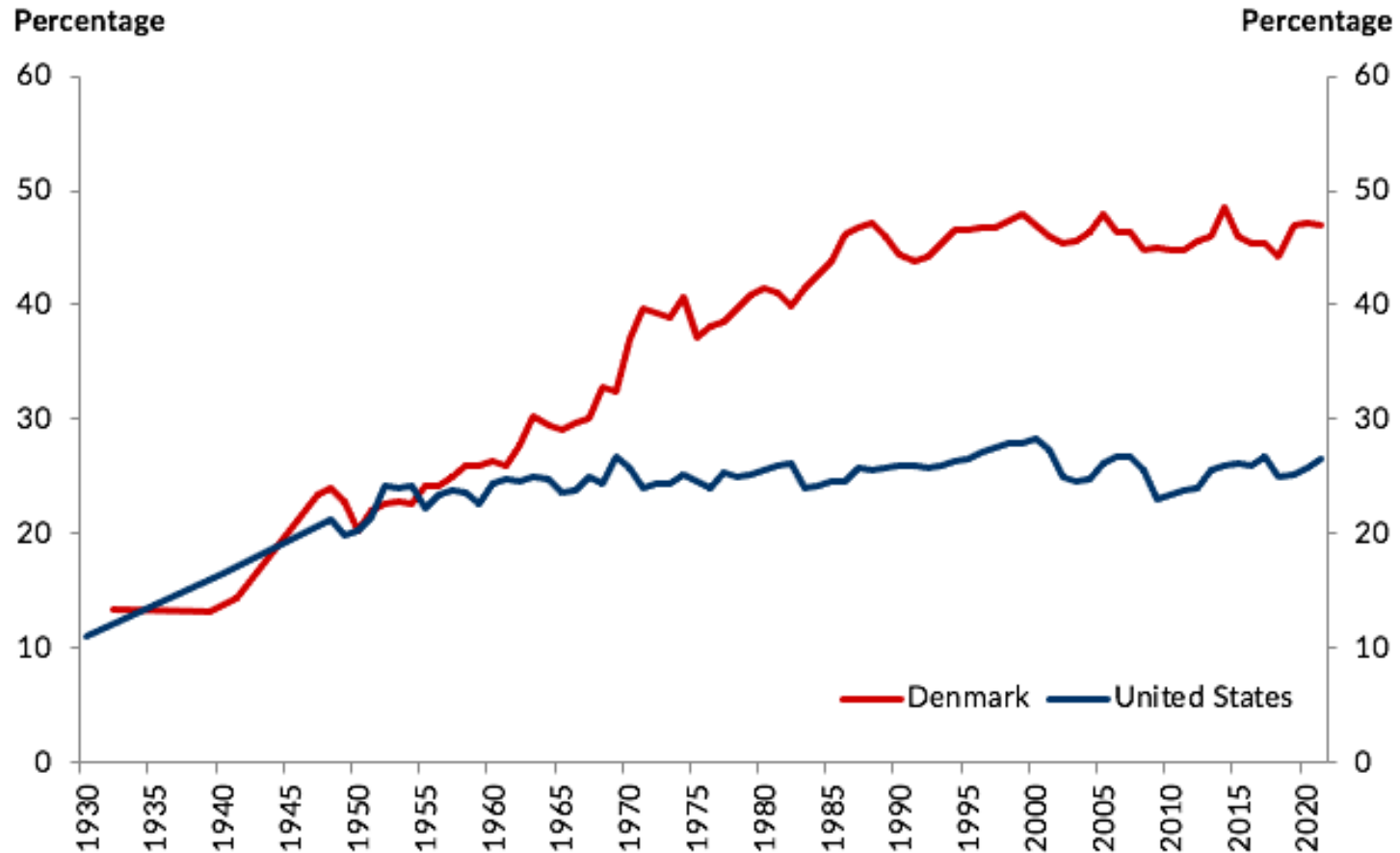
- Finland no. 17
  - Denmark no. 5
  - Norway no. 29
  - Sweden no. 17
  - Iceland no. 14
- 
- Freest parts combined no. 1.

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# Denmark used to have low taxes

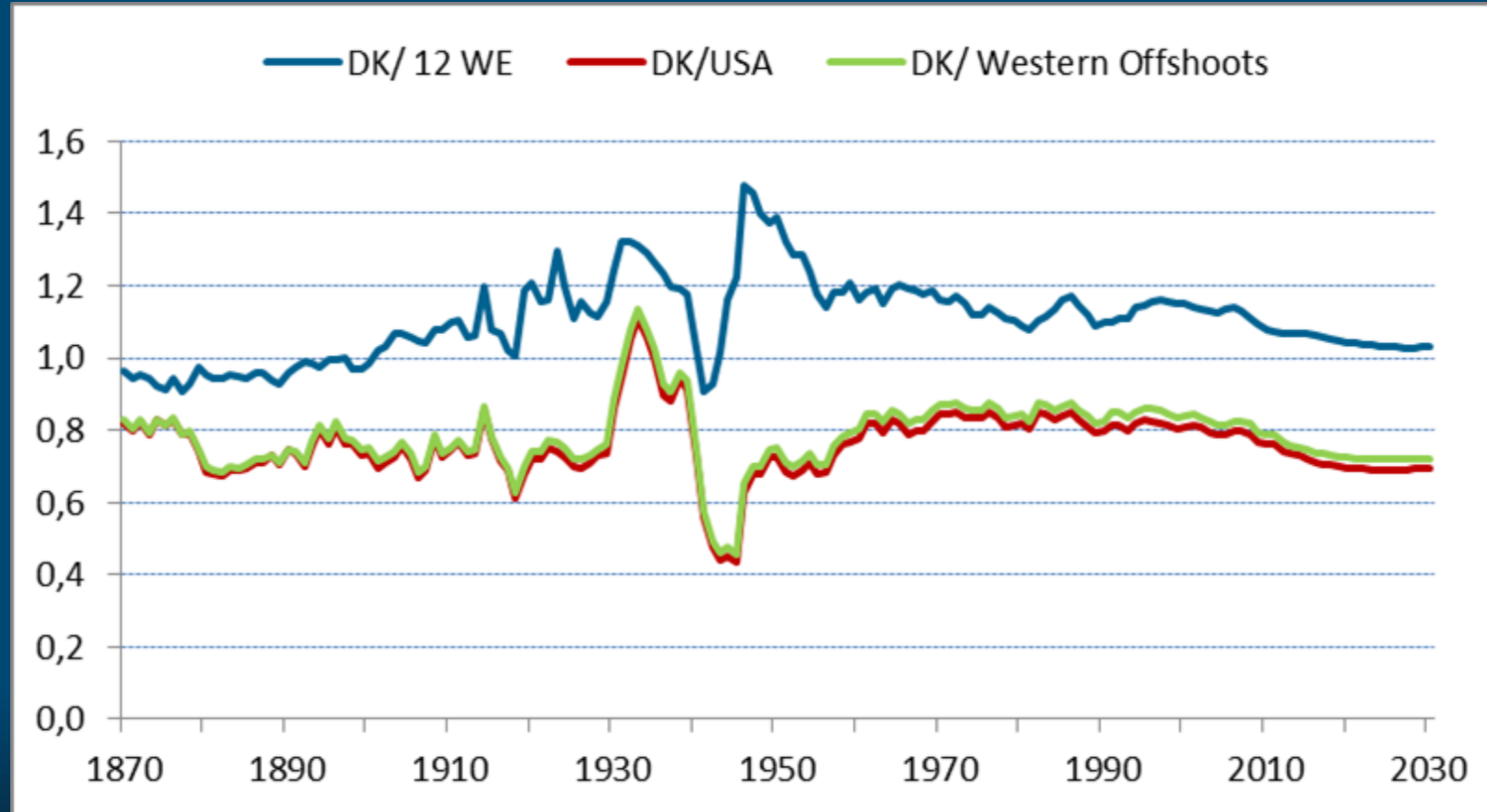
## Historical Tax Burden in Denmark and the US, 1930-2021



Remark: The Danish series has data break in 1947 and 1965, the American in 1948 and 1965

Source: Martin Ågerup - "Velfærd i det 21. århundrede", 2017 and OECD Tax Database

# When did Denmark become rich?



# Some answers

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# The political evolution of the welfare state



- 1956: “Folkepensionen”. Universal pay-go old age pension
- 1959: The Venstre-Konservative liberal economic plan
- 1966-67: “The red cabinet” (S): Tax base and welfare spending expanded
- 1967-71: VKR-government (V,K,R): Do.
- 1971-82: Mostly S gvts: Unsuccessful crisis management
- 1982-92: Schlüter gvts (V,K,Q,M,R): Economic reconstruction and reform
- 1992-present: Continuing reforms

# The Danish economy anno 1982



- Unemployment: 9.8 per cent
- Inflation 10.4 per cent
- Balance of payment deficit 4.4 per cent of GDP
- Gross government debt 67.0 per cent of GDP
- Government deficit 9.1 per cent of GDP

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# Public finances of successive gvts

Government	Chg Spending	Chg Reciepts	Chg Balance
Krag (S) 66-67	3.2	2.7	-0.5
Baunsgaard (RV) 67-71	6.2	9.0	0.7
Jørgensen/Hartling (S/V) 71-82	14.8	1.7	-13.1
Schlüter (K) 82-92	-0.8	6.1	7.0
Nyrup Rasmussen (S) 92-01	-3.5	0.2	3.7
Fogh Rasmussen (V) 01-09, Løkke Rasmussen (V) 09-11, 15-19, Thorning Schmidt 11-15 (S)	-2.4	-2.0	-0.6

# Elements of economic reform since 1982

- Fixed exchange rate (ERM) 1982-present
- Fiscal consolidation through tax increases and welfare reform
- EU fiscal rules and the budget law
- Tax reforms
- Welfare reform (indexing pension age)
- “Active” labour market reform and “flexicurity”
- Private pension savings
- Easing rent control
- Privatisation and utility deregulation
- Internal Market of EU
- Financial deregulation and reregulation
- The tax stop

# The prominence of tax and welfare reforms



Average economic growth p.a. 1986-2018	1.6
- Of which	
- underlying growth	1.1
- reforms	0.5
- of which	
- tax reforms	0.3
- other	0.2

# Growth is more important than redistribution



- Average income in the bottom 40 pct. of income distribution grew by a factor of eight from 1919-2019

- Taxes grew from 10 to 47.5 per cent of GDP

- Composition of income growth in the bottom 40 per cent:

• Economic growth, direct effect	54.4 per cent
• Redistribution	9.2 per cent
• Combined effect	<u>36.4 per cent</u>
•	100 per cent

# Challenges and the need for further reform



- Taxes and spending very high
- Fiscal super sustainability is turning into spending
- EU fiscal discipline crisis and “common” debt
- High marginal taxation of labour income
- High and uneven level of taxation of savings
- Corporate tax rate reductions have dried out
- Increasing level of regulation (factor 3 since 1989), including EU regulation
- Underlying growth is low
- Baumol disease in public sector spending
- Need for further welfare state privatization (a la pensions)