

## ENGLISH SUMMARY

### Chapter I: The Danish Economy

Economic activity in Denmark slowed down in 1999 after a long period with strong growth driven by domestic demand. The effects of the so-called “Whitsun” package, which contained measures explicitly aimed at dampening private consumption, were reinforced as interest rates began to rise during the second half of 1999. However, the fall in the rate of growth of private consumption coincided with a sharp rise in exports which helped maintain GDP growth. The rapid transition from domestic- to foreign-demand-driven growth and the rather fortunate timing of this change gave rise to a soft landing for the Danish economy. The growth in domestic demand is expected to increase in the projection period, but it is not anticipated that it will reach the same high level as in the period 1994-98. Continued high growth rates in exports and rising domestic demand are expected to mean that GDP will grow by more than 2 per cent in 2000. In 2001 and 2002 the GDP growth rate is expected to be 1½ per cent, and growth will again be predominately driven by domestic demand. Employment is expected to increase moderately in 2000, partly due to rising employment in the public sector. It is assumed that labour supply will remain constant during the projection period, and hence it is predicted that unemployment will continue to fall in 2000. Unemployment is expected to average 147,000 persons during the year. Employment will continue to rise slowly in 2001 and 2002, thus reducing the level of unemployment even further.

Domestic demand is expected to grow at a moderate pace in 2000, after a decline in 1999. The recovery of domestic demand will be mainly the result of a lower tax burden and higher disposable incomes. The hurricane that hit Denmark in December 1999 is also expected to increase domestic demand by casing investment-related activities to increase in 2000 and 2001.

The global economy in the spring of 2000 has been marked by rising optimism and increasing growth rates in GDP. In the United States, Western Europe and Japan the growth rates are expected to be higher in 2000 than in 1999, and Denmark's trading partners will have a combined growth rate of 3¼ per cent in 2000. Beyond 2000 the combined growth rate is projected to decline, primarily due to a modest weakening of economic activity in the United States.

Exports are expected to continue to grow very rapidly in 2000 due to the high GDP growth rates abroad and improved international competitiveness. A slowdown in the global economy and a strengthening of the Danish effective exchange rate is expected to reduce the growth rate in exports of manufactured goods from 6½ per cent in 2000 to 5¼ per cent in 2001 and 2002. Foreign trade developments will lead to a current account surplus of 2 per cent of GDP each year in the period 2000-02. The predicted current account surpluses are primarily the result of a lower level of investment. However, the expected current account surpluses are also the result of a higher propensity to save. In this respect it is worth noting that the saving to income ratios in the projection period are about 1 percentage point higher than in 1998, when the current account showed a deficit of 1 per cent of GDP.

The surplus on the general government financial balance is expected to be 2-2½ per cent of GDP. The main reasons for this are a continuing growth in the tax base and a slower rate of growth in expenditure as a result of the low unemployment rate.

The inflation rate has been growing significantly during 1999 and through the first half of 2000. However, the higher inflation rate is expected to be only temporary. The inflation rate is expected to fall again due to lower growth rates in import prices and energy prices and a strengthening of the Danish effective exchange rate in 2001 and 2002. Despite the low unemployment level, wages are expected to grow at a slower pace than in the past few years. The slower growth in wages will also mean lower inflation rates. However, if the

dollar does not depreciate within the next year – as it is assumed it will – and the Danish effective exchange rate is thus prevented from rising, this could lead to higher inflation rates than set out in the forecast.

*Table 1 Short-term prospects for the Danish economy*

	1999	1999	Percentage changes			
	Current prices DKK bn. <sup>d</sup>	Per cent of GDP	in volume terms			
			1999	2000	2001	2002
Private consumption	613.7	50.6	0.7	1.8	2.4	2.3
Public consumption	312.5	25.8	1.1	1.2	1.2	1.2
Gross fixed capital formation, consisting of:	237.9	19.6	-0.7	0.3	-1.5	1.5
Residential investments	51.3	4.2	0.0	0.3	-3.5	-4.5
Fixed business investments	167.7	13.8	-0.3	0.0	-1.4	3.3
Public investments	19.0	1.6	-6.3	4.0	2.0	2.0
Stock building <sup>a</sup>	-1.6	-0.1	-1.0	0.3	0.0	0.0
Total domestic demand	1162.5	95.8	-0.5	1.7	1.2	1.9
Exports of goods and services	444.0	36.6	7.0	5.1	3.9	3.6
Imports of goods and services	393.1	32.4	1.3	4.2	3.7	4.1
GDP	1213.3	100.0	1.6	2.1	1.4	1.7
<b>Key indicators</b>						
Consumer prices, percentage change <sup>b</sup>			2.5	2.7	1.8	1.5
Unemployment, per cent <sup>c</sup>			5.6	5.2	5.0	4.7
Current account, DKK bn. <sup>d</sup>			13.9	24.7	26.1	28.9
Current account, per cent of GDP			1.1	1.9	2.0	2.1
General government financial balance, DKK bn. <sup>d</sup>			35.9	32.4	29.8	33.2
Gen. government financial balance, per cent of GDP			3.0	2.5	2.2	2.4
Hourly wage costs, percentage change			3.3	3.9	3.8	3.8
Terms of trade, percentage change			1.1	0.3	0.0	0.2

- a) The percentage changes are calculated as the real changes in stock building relative to real GDP in the previous year.
- b) Implicit private consumption deflator.
- c) Percentage of the total labour force.
- d) The DKK/USD exchange rate is taken as 7.66 in 2000, 7.03 in 2001, and 6.90 in 2002.

## **Policy Recommendations**

A characteristic of the Danish economy at present is that it seems to be balanced on a narrow path, with moderate domestic demand on the one hand and a tight labour market on the other. The main concern is whether the path is consistent with wages continuing to grow at a relatively slow pace. One of the main aims of the “Whitsun” package was to reduce the rate of growth in private consumption through a reduction in the extent to which interest payments were tax deductible and an increase in green taxes. However, contrary to the widely held expectation the reduction in tax deductibility of interest payments did not produce any significant dampening of the rate of increase in prices on the housing market in 1999, primarily because homeowners took advantage of the large gap between short- and long-term interest rates by using floating-rate bonds for financing purposes. The slowing of the rapid growth in domestic demand in 1999 was thus primarily a result of the higher green taxes and the reduction in disposable income. The desired cooling of the Danish economy was achieved. However, if housing prices actually had gone down as a direct consequence of the “Whitsun” package, the result could have been a much stronger decline in domestic demand, perhaps even a more dramatic fall than intended. In the absence of the increased opportunities for obtaining relatively cheap financing of owner-occupied housing and the improvement in international competitiveness achieved thanks to a falling effective exchange rate, the fiscal tightening could have resulted in a much harder landing for the Danish economy in 1999.

The surplus on the general government financial balance is expected to be large in each year in the projection period. The surplus leaves room for an extended reduction of the public debt and thence greater opportunities in the future to pursue an active and stabilizing economic policy in the face of adverse impulses to the business cycle. Taking a longer term view, with the prospects of an ageing population and a resulting increase in the demand for government spending, it seems

sensible to use the current favourable conditions to bring down the public debt. Otherwise, either there will have to be significant rises in taxes to finance the future growth in government spending, or there will have to be severe changes in the pattern of government spending in order to keep it down to affordable levels. Faced with the long-term fiscal challenges of an ageing population, the current surpluses should not be reduced by cutting taxes or by using any other type of fiscal expansion. Under the current economic conditions with a low rate of unemployment, increasing demand as a result of a fiscal expansion would be very hazardous, since it could lead to an overheating of the Danish economy. Hence, unbalanced tax cuts cannot be recommended in the current economic conditions. On the other hand, neither is there any necessity for fiscal tightening in a situation where the Danish economy is growing at a moderate pace.

A degree of restraint with respect to wage demands has been exercised in the central wage negotiations, particularly viewed in the light of the low unemployment level. At present the outcome of the local wage negotiations is not known, and these may turn out to play a very important role in determining future wage levels. In this respect there is a risk that the new division between central and local wage settlements, together with the low and still falling rate of unemployment, may result in higher wage increases than expected. It is possible that the restraint in wage demands in the central wage negotiations may have been the result of the labour market not being as tight as the official unemployment figures indicate. The reason is that the active labour market policy through various schemes has re-categorised unemployed persons as employed, meaning that the actual number of job-seekers might be higher than the unemployment figures indicate.

An additional outcome of the wage settlements has been a reduction in the average number of hours worked through increases in the amount of standard holiday time. The consequences of this will be a diminishing labour supply and a reduction in taxable income, putting extra pressure on the tight labour market and potentially cutting the surplus on the general government financial balance. Maintaining or

increasing the labour supply in the context of an ageing population constitutes a great challenge for policy makers in the future, and greater concentration is needed on making the necessary structural improvements to deal with this situation. Increasing the size of the labour force by reversing the current tendency to exclude functional but less productive workers from the labour market could be a possible solution.

Increasing prices of energy and oil have contributed significantly to the currently high Danish inflation rate. However, domestic conditions are seen as the primary reason why the inflation rate in Denmark is higher than in most European countries. In particular, the inflation rate in Denmark has exceeded the EMU inflation criterion in the first months of 2000. However, this situation is expected to be only temporary, due to the modest growth rates in domestic demand and the increasing level of economic activity in the rest of EU. Furthermore, the level of inflation is not alarming, but it does indicate that greater attention should be paid to domestic factors that may cause higher inflation rates.

## **Chapter II: The EMU: Danish Exchange Rate Policy at a Crossroads**

On January 1, 1999, 11 out of the 15 EU member countries implemented the third and final phase of the Economic and Monetary Union (EMU). Denmark has so far chosen to opt out of the EMU, but will hold a referendum in September on the question of joining the monetary union.

The issue of Denmark's possible membership of the EMU is linked more to political considerations than to purely economic factors. Nonetheless, if Denmark does decide to join the EMU, this move will affect the future economic situation in Denmark. The report concentrates on some of the purely economic issues related to the decision to either enter the monetary union or stay outside more permanently. It does not discuss the possible indirect economic consequences of changes in the political position of Denmark which may occur if the country joins the EMU. Thus, it does not try to assess the economic importance

of being able to influence the decision-making processes in the monetary union, nor the consequences of giving up further sovereignty. The Chairmanship has not found it possible to analyse these issues on a sufficiently objective and scientific basis.

Because entry into the EMU will presumably have permanent consequences for the Danish exchange rate and monetary policy conditions, the long-term consequences and the possible future development prospects of the EMU should be taken into consideration at least as much as the short-term consequences. There will be various efficiency gains in the form of saved transaction costs, a probable reduction of the interest rate spread towards Germany, the ending of exchange rate fluctuations against the currencies of present EMU member countries, and probably beneficial effects from increased competition in some sectors. However, these gains are not expected to be very significant for the long-term development of the Danish economy.

In relation to stabilization policy, it is significant that empirical analyses show that Denmark deviates somewhat from the core countries of the EMU with respect to changes in GDP and other economic variables. Future Danish EMU membership might in itself change these differences, but the change could be in either direction. Hence it is not impossible that there would be a situation in the future where the Danish business cycle differed considerably from that of the other countries, and the option of exercising an independent Danish monetary policy reaction would be useful. The restrictions concerning fiscal policy in the Maastricht treaty seem somewhat arbitrary, but at present do not seem likely to restrict Denmark's stabilization options. However, because of demographic changes, these restrictions may cause problems in the future for several EMU member countries, and partly because of this, future pressure to change the fiscal policy rules of the EMU can be anticipated.

Whether it is advantageous from a purely economic viewpoint for Denmark to join the EMU depends on whether the efficiency gains outweigh the costs of definitively giving up the

possibility of an independent monetary and exchange rate policy. The value of an independent monetary policy depends on the extent to which a monetary policy based on the whole Euro area will also be suitable for Denmark, and if it is not suitable, on the willingness of Danish politicians to use other stabilization instruments. The fact that Denmark has been able to maintain a fixed exchange rate against the Deutschmark for several years shows that we may not necessarily need an independent monetary policy to be able to react to differences in the business cycle. The probability that Denmark will be affected by a major asymmetric shock is not very great. Summing up, the Chairmanship assesses the purely economic costs and benefits for Denmark of EMU membership as being small and uncertain. However, as stated earlier, there are a number of other aspects, not least those of a political nature, which may have an important role for Denmark's choice, but which are not considered in the report.

If Denmark decides to stay outside the EMU, one possibility is to continue the fixed exchange rate policy *vis-à-vis* the Euro within the ERM II agreement, possibly in an expanded fluctuation band. The fixed exchange rate policy has gained credibility and is today well incorporated into economic policy and expectations formation. This in itself speaks for continuing the fixed exchange rate policy in the event that Denmark decides not to join.

Persistent speculative pressure on the Danish Krone could force an abandonment of the fixed exchange rate arrangement. Normally, speculative attacks only occur when an unsustainable economic policy is incompatible with a fixed exchange rate. As regards Denmark, it is difficult to point to any real economic reasons why the Danish currency should be overvalued and thus be subject to speculation. This does not, however, exclude the possibility of unfounded speculative attacks in a situation where we decided to keep the fixed exchange rate arrangement. But it is not likely that periods of speculative pressure would be long-lasting, and experience from earlier crises shows that they quickly abate and that they only have real economic consequences for countries that already have structural problems.



If it turns out to be impossible or undesirable to continue the fixed exchange rate arrangement, an alternative would be to adopt a monetary policy based on inflation targeting, like the United Kingdom and Sweden. Such a policy means that the central bank should target price increases instead of the exchange rate. An advantage of inflation targeting is that monetary policy is conducted on the basis of domestic conditions. In this way, Denmark's Nationalbank would not necessarily have to automatically follow interest rate changes in Euroland regardless of whether they are appropriate in the prevailing economic situation. Another advantage is that the currency would be less vulnerable to speculative attacks and consequently the risk of having to raise the interest rate temporarily to defend the currency would be smaller. Among the disadvantages is that a monetary policy based on inflation targeting is less transparent than a fixed exchange rate policy. It also allows greater exchange rate swings. However, if the inflation target is the same in two areas, and economic policy is credible, the exchange rates will also move in parallel in the long run, and short term fluctuations in the exchange rate are unlikely to have any importance for foreign trade.

The introduction of the Euro went smoothly. However, the EMU has still not been in a situation where the common monetary policy has been put to a severe test, and it is therefore too early to definitively evaluate the success of the EMU construction. An assessment must therefore to a large extent rest on an evaluation of the institutional framework of the EMU and the political intentions behind the construction. Although it seems most likely that the EMU will be able to secure low and stable inflation, the possibility that the common monetary policy may cause tensions at some point in time cannot be ruled out. This could lead to a high and varying rate of inflation in Euroland. In such a situation, only an independent inflation target could prevent Denmark from importing inflation from Euroland.

### **Chapter III: On the Margin of the Labour Market**

The level of employment is higher than ever, and the number of persons unemployed has fallen dramatically during the past seven years of high growth. These developments must not be allowed to obscure the fact that a large number of people have not benefited from the economic upturn. However, the positive economic outlook and the current relatively small cohorts of young people offer a unique opportunity for reducing the number of people entering the category of the long-term unemployed and the groups excluded from the labour market.

The long-term unemployed are defined as those people of working age who have been unemployed for more than 80 per cent of the time over a period of three years. Their absence from employment may be due to unemployment, or participation in labour market activation programmes, to being on leave from normal unemployment job search, or to being on a rehabilitation scheme. Being employed for less than 20 per cent of the time, these people must be considered as being at the margin of the labour market. We estimate the number of the long-term unemployed to have been around 85,000 persons in 1998, which was equivalent to 2.5 per cent of the population aged between 20 and 64 years. In 1994 the number of long-term unemployed persons was approximately 145,000 (4.5 per cent).

Those excluded from the labour market are people who have left the labour market altogether, but against their will. A large proportion of these receive disability pensions. Some of those on early retirement schemes would have preferred to remain employed if possible. There are 270,000 persons (8.3 per cent of the population aged 20-64) on disability pensions and 175,000 persons (5.4 per cent) on early retirement schemes. In addition, some of those out of the labour force who are either receiving social assistance or without public income support are among those excluded from the labour market. The total membership of these groups accounts for more than 6 per cent of the population aged between 20 and 64 years, and even though there is a large flow of people in and out of these groups, some of the people there are on their way out of the labour market or have in practice been excluded from it.

Some of the long-term unemployed are regarded by firms as unsuitable for employment when considered in relation to current wage levels, due to bad health, substance abuse, high age or poor qualifications; and others make it difficult for themselves to obtain employment because they only want to accept favourable job conditions. Unskilled workers and immigrants are relatively often among the long-term unemployed.

There has been a shift in demand for labour towards people with education or training, at the expense of unskilled labour. The main reason for this is probably new technology, as it can be seen as a substitute for unskilled labour in sectors across the employment spectrum. Globalization has also led to a lower demand for unskilled labour to some extent, but the effects of globalization are much smaller than those of new technology.

Immigrants have particular difficulties in getting jobs. The problems are particularly severe for refugees and immigrants from countries with a low level of per capita income. In particular, immigrants coming to Denmark too late in life to attend primary school seldom get a job, as few manage to obtain an education and they have difficulties in learning the language and the culture. The higher level of unemployment among immigrants can only partly be explained by their level of education, though. Discrimination is also likely to be a factor.

Poor health can on the one hand be due to factors such as traffic accidents, lifestyle, or inherited predisposition to illness, and on the other hand be due to working conditions having caused accidents, sickness or other disorders induced by physical or psychological work-related strain. The type of working environment associated with the highest risk of becoming unemployed or excluded from the labour market has been found to be in jobs characterised by poor job security, low level of influence, physical strain and repetitive activities. These factors are most common in jobs done by unskilled workers. Poor working environments are costly to society, as they lead to expensive treatment in hospitals, etc. and to lower

production levels, because injured workers are unable to work for some time. Incentives for firms to improve the working environment should be increased in some way, as firms only pay the private costs of injuries to and reduced working ability of their employees, and these are small in comparison with the social costs related to sickness and accidents on the job. Incentives could be increased by imposing a tax on the premiums paid for industrial accident and sickness insurance.

The first category of people excluded from the labour market are those receiving disability pensions. This group is dominated by unskilled workers. Estimates have shown that unskilled workers who were in their mid-thirties in 1980 had a much greater likelihood of being in receipt of a disability pension by 1997 than people with a formal education. It is likely that the increased probability of being disabled is related to the characteristics of unskilled jobs, but at the same time unskilled workers have a lifestyle which helps to explain the increased risk of disability. This lifestyle is partly due to the lower income level related to unskilled jobs. However, those of the unskilled who did not have a job in 1980 had the greatest risk of becoming excluded. This indicates that the argument regarding poor working environment should not be carried too far.

The Government and a number of other political parties are planning a reform of the disability pension legislation. It is suggested that municipal authorities should be required to test a person's working capability and estimate their chances of returning to a job, possibly on special terms (fewer hours, special equipment provided, etc.), independent of the person's education and earlier career. This would demand a more flexible labour market, where firms created jobs for persons who had a limited ability to work. In order to meet these demands it is the ambition of the Government that 40,000 jobs should be created in the private and public sectors with wage subsidies to the employer. There is, however, a risk that the existence of these subsidised jobs would cause a reduction in the number of normal, non-subsidised jobs in existence. The Chairmanship thus recommends greater use of jobs created at the local level with special conditions of employment, but

without subsidies. To reduce the number of people becoming long-term unemployed, companies should be made responsible for setting up action programmes to ensure that people did return to their jobs after a period of sickness. This should be done in cooperation with trade unions, employers' organizations and regional authorities.

Labour market policy has changed since 1994 in that a more active strategy has been adopted. Now the unemployed are offered the opportunity and indeed required to engage in either job training or education at an earlier stage than previously. Several programmes have been launched to integrate the unemployed into the labour market. The most successful programme is job training in the private sector, but most of the other programmes also increase the participants' chances of returning to employment.

Rehabilitation is the name given to a special programme which is used both for rehabilitating disabled persons and for integrating persons who have not been on the labour market before and who experience severe difficulties in entering the labour market. The advantages of this programme are that participants are allowed to get public income support for up to five years and that they are even allowed to follow an academic course of education while receiving such support. One special case is that nearly one in ten single parents receive rehabilitation support. Our estimations show that the success of the programme depends on both the basic educational level before starting and the final educational level after rehabilitation. If the participant completes a course of education the probability of success increases significantly.

One basic problem is that the programmes to help the long-term unemployed and to prevent people from being excluded from the labour market are initiated and financed by different authorities. The institutions involved are the Employment Service, the municipalities and the unemployment funds. The Employment Service is a state institution, while the unemployment funds are closely connected to the trade unions. Both the Employment Service and the municipalities are engaged in active labour market policies, including education

and job training. Both the Employment Service and the unemployment funds register the fact when an insured person becomes unemployed. The municipality is the only authority which is allowed to start a rehabilitation process, and municipalities are also required to contact their residents who are in receipt of sickness benefit for more than eight weeks, even though a person's employer might be situated in another municipality.

The problems are that several authorities are involved in the same types of programme without there being any coordination between them, and that people who move between employment, unemployment, sickness benefit and rehabilitation are dealt with by several different institutions, these often having no knowledge of the case history of the people in question.

These problems are well known to the Employment Service, the municipalities and the unemployment funds, and they have been experimenting for some years with different forms of cooperation. The experiments have shown that there is a potential benefit from closer cooperation.

In the light of these problems and the experiments it is recommended to consider the advantages of amalgamating the Employment Service, the unemployment funds and the municipalities' labour market activities. A united authority would have better opportunities to initiate the necessary actions at an earlier stage, which could lead to there being fewer long-term unemployed and to reducing the number of persons who are excluded from the labour market.

## **Chapter IV: Health – A Task for the Welfare State**

Danish health care expenditure amounts to 6½ per cent of GDP, which is a little less than the OECD average. There are several economic reasons why the provision of a health service should be a task for the welfare state. For instance, it is very difficult for patients to assess the availability and quality of

treatment. Priority has been given in Denmark to providing free access for all to most health services, regardless of an individual's means.

Health care provision in Denmark is to a very great extent a public responsibility, as about 80 per cent of health care costs are financed through taxes. The responsibility for running the service is decentralised, and most of the services are run directly by the public regional authorities. The tasks of financing and running the services are thereby integrated.

The Danish health care service can be divided into two sectors: primary health care and the hospital sector. The primary health care sector deals with general health problems, and its services are available to all. The primary health care sector consists of general practitioners, practising specialists, practising dentists, physiotherapists, etc. The general practitioners act as "gate-keepers" with regard to hospital treatment and treatment by specialists. They are paid by the counties. The counties have the responsibility for financing and running the hospitals. 80 per cent of public health expenditure goes on the hospitals and 20 per cent on primary care.

The hospital budgets are determined by each county as global budgets. Use of global budgets for hospitals has kept the cost of running the hospitals within agreed limits. The drawbacks of global budgets are the limited possibilities in the short run to adjust the supply of services to changes in demand, and the lack of incentives to use resources efficiently. One way to strengthen incentives is to increase competition between hospitals. A separation of purchaser and provider is a necessary but not a sufficient condition for competition. Due to geographical distances there is often only a single provider, and therefore it is difficult to establish conditions for competition. However, it is a possibility in large cities.

General practitioners (GPs) are paid partly by fees-for-services payments and partly by capitation fees. Capitation fees are paid for all patients listed with the GP. The income from capitation fees amounts to approximately one-third of a GP's

total income. The GP's incentives to choose the most cost effective provision of health services could be strengthened if for selected treatments the GP had a budget per patient listed. The GP could then choose to treat any given patient or pay a specialist or a hospital for the treatment. Similarly, a GP could have a limited budget for medicines. This could strengthen incentives to choose the cheapest medicine in cases where several medicines would have the same effect on the patient.

There are income-related inequalities in the delivery of health care in Denmark. Low income groups have a relatively higher consumption of health care services than high income groups, and even if differences in age and sex across income groups are taken into account, some inequality remains. This is particularly noticeable for hospital bed days. It should be noted that the causality between these phenomena is not clear, since on the one hand illness can limit employment opportunities and thereby reduce income, while on the other hand low income is often associated with poor living conditions, which in turn can lead to higher morbidity rates.

One specific measure of the health status of the population is life expectancy, and the report shows that there are inequalities in life expectancy as well. For instance, highly educated men tend to live longer than less educated men, but this picture does not apply for women, where education seems to be a minor factor in the determination of expected lifetime. Other results show that the expected lifetime of skilled workers is longer than that of unskilled workers. Taken together, the analyses indicate that morbidity and mortality are unevenly distributed, so that people with high socioeconomic status tend to be better off in terms of health than those with low socioeconomic status.

The life expectancy of the Danish population has been rising and will continue to do so. Calculations in the report show that demographic developments alone will account for a significant rise in the future public expenditure on health care. In addition, the pattern of illnesses can be expected to change, so that illnesses demanding comparably more lengthy and complex treatment are likely to occur more frequently in the future. The



emergence of new methods to treat patients will also affect health care costs, but it is uncertain in which direction the effect will lie. On the one hand, the demand for new health care services may rise, and thus increase the pressure on expenses. On the other hand, new techniques may prove to be cost saving, as they are likely to be more effective.

Increased future expenditure on health care must be financed in some way. Today the health sector in Denmark is mainly financed through personal income taxes, but direct payments account for approximately 17 per cent of the financing, while payments from private insurance companies amount to 2 per cent.

One possible source for financing increased expenditure on health care is to raise the proportion of direct payments. There are, however, some side effects of direct payment that must be taken into account. First, direct payment can cut down on unnecessary consumption, but it can also reduce the utilisation of relevant health care services. Second, direct payment will tend to increase income inequality, because lower income groups have a relatively high level of consumption of health care services. The effect on income distribution from a specific scheme of direct payments is analysed in more detail in the report, and the revenue is derived. The scheme of direct payments considered has similarities to direct payment systems currently used in other Nordic countries. Calculations show that the finances of regional authorities could be improved by approximately 6 per cent by the direct payment scheme. However, the scheme would definitely increase income inequality which, taken together with the possible negative effects on the health status of the nation, means that increasing the proportion of direct payments in the health care sector cannot be recommended.

The existing user charges in Denmark are concentrated on a few areas, including dental care and medicines, while there generally are no direct payments for primary care, specialist care and in-patient care. This division is due to historical reasons, and there are no rational explanations **for it**.

The individual user of health care services can find the coverage from the public health sector to be restricted. Today there is only limited supplementary capacity for treatment outside the public health care sector, and the opportunities for buying supplementary private insurance are few. It is worth considering improvements in the scope and availability of private supplementary insurance. However, the private health care system must still supply basic services free of charge. Increased demand for hospital personnel in the private health care sector can imply shortages in the hospital personnel available to the public health care sector. It should be stressed that such shortages could have serious effects for the public health care sector.

The need for health care services is very great, and it is not possible to fulfill all needs for publicly financed health care services. Health economics methods are useful tools in priority decisions. It is, however, important to stress that health economics analyses cannot be used in isolation. A broader and highly recommendable approach is health technology assessment. The standing Committee for Health Technology Assessment in Denmark was established in 1996. The concept of health technology assessment is to clarify all relevant consequences of a decision to apply a given health technology. Health technology assessment includes clarification and assessment of a number of areas where the utilization of health technology may have consequences. These are summarised in four principle elements: technology, the patient, the organisation and the economy. It is recommended that health technology assessment should be used to a greater extent.