

## ENGLISH SUMMARY

### Chapter I: The Danish Economy

The Danish economy seems rather robust. After an economic slowdown in 2001 with GDP growing at 1 per cent, growth increased in the first half of this year, mainly due to higher private consumption and exports. Hence the economy is expected to grow at 1.7 per cent in 2002. Employment has decreased in 2002 for the first time since 1994. However, this is not seen as the start of a long period with low growth rates. Instead, a slight increase in the growth rate to nearly 2 per cent annually is expected from 2003 until 2005, and this will also lead to higher employment. However, the level of unemployment will only be slightly reduced, as the size of the labour force will also increase.

Even though this scenario involves only moderate growth, it can be considered a relatively favourable outcome of the current situation, since the Danish economy faces the risk of shifts in either direction. On the one hand, if demand grows more than expected, wage increases and inflation could be considerably higher than predicted, since the Danish labour market is very tight. Higher demand could thus eventually be harmful to production and competitiveness. On the other hand, factors such as falls in stock market prices, oil price uncertainty and a delayed global upswing could provoke a negative shift in confidence and thereby dampen consumption and investment.

The global economy has still not recovered from the slowdown in 2001. The economic outlook is now assessed more negatively than it was in the summer, and there are no indications of an early improvement; both real economic data and consumer and business confidence have disappointed over the last several months. Germany in particular is experiencing low growth and seems to have profound structural problems. Growth for Denmark's trading partners is expected to be around 1¼ per cent this year and about 2 per cent next year. However, there is substantial uncertainty concerning the timing and strength of

the expected upswing.

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

	Current prices	Per cent of GDP	Percentage change, volume				
	DKK bn. <sup>d</sup>		2001	2002	2003	2004	2005
Private consumption	631.3	47.0	0.8	2.0	2.7	1.9	2.0
Public consumption	343.0	25.5	1.2	1.3	1.0	1.0	1.0
Gross fixed capital formation	284.2	21.1	-0.1	1.7	1.3	2.5	1.5
consisting of:							
Residential investments	52.8	3.9	-13.5	-2.5	3.3	3.9	3.8
Business fixed investments	207.9	15.5	3.2	2.2	0.8	2.2	1.0
Public investments	23.5	1.7	3.5	6.0	2.0	2.0	2.0
Stockbuilding <sup>a</sup>	-0.2	-0.0	0.4	-0.3	0.3	-0.0	-0.0
Total domestic demand	1,258.3	93.6	1.1	1.4	2.2	1.8	1.6
Exports of goods and services	613.0	45.6	3.7	3.6	3.6	4.2	4.1
Imports of goods and services	526.8	39.2	4.3	3.0	4.5	4.2	3.6
GDP	1,344.5	100.0	1.0	1.7	1.9	1.9	1.9
<b>Key indicators</b>							
Consumer prices, percentage change <sup>b</sup>			2.1	2.3	1.9	1.7	1.7
Unemployment, per cent <sup>c</sup>			5.1	5.1	5.0	5.0	4.9
Current account, DKK bn.			34	29	32	39	51
Current account, per cent of GDP			2.5	2.1	2.2	2.6	3.2
General government financial balance, DKK bn.			38	28	29	34	40
General government fin. balance, per cent of GDP			2.8	2.0	2.0	2.2	2.5
Hourly wage costs, percentage change			4.6	4.2	4.0	3.8	3.8
Terms of trade, percentage change			1.4	-1.2	0.5	0.3	0.4

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. National definition.

d) The DKK/USD exchange rate is taken as 8.36 in 2001, 7.87 in 2002 and 7.42 in 2003-2005.

Sources: Statistics Denmark, *National Accounts* and own estimates.

Despite the low international GDP growth, Danish exports of industrial goods in particular have improved in the first half of 2002. The growth rate for imports is also expected to be quite large in 2002, reflecting the increase in domestic demand. Hence, net exports will only contribute slightly to GDP growth, which will thus be primarily driven by domestic demand. The same pattern is expected to continue until 2005. After three years of low growth, private consumption has increased in 2002, supported by an increase in vehicle purchases. In the coming years, private consumption is projected to grow almost in parallel with the expected increase in disposable income.

The current account surpluses will decrease in 2002, due to a worsening in the balance of services and to larger transfers to the EU. The current account is expected to improve in the years to come due to a moderate increase in investment and a larger increase in savings by both households and the public sector. The current account surpluses will ensure a significant reduction in foreign debt in the forecast period.

The public budget surplus is expected to decline from around 2<sup>3</sup>/<sub>4</sub> per cent of GDP in 2001 to around 2 per cent this year. The fall is primarily explained by the fact that supplementary pension payments have been converted to a mandatory private savings scheme. These pension savings are therefore no longer counted as part of public income. The budget surplus is projected to rise in 2004-05 as a result of higher revenue from taxation of returns on pension funds following the low revenue this year and next year as a consequence of the recent drop in stock market prices.

Future demographic changes, which will result in a smaller labour force and a larger number of elderly people in the population during the first half of the 21st century, will affect the sustainability of public finances. Under the assumption of some improvement in labour force participation rates because of a higher effective retirement rate, better integration of immigrants and their descendants, a higher female participation rate and fewer people receiving special early retirement pensions, calculations indicate that the basic income tax rate

should be raised by about 2½ percentage points to ensure a sustainable fiscal policy from 2005. Naturally, these results are highly sensitive to changes in the underlying assumptions, not least the changes in the labour force and the projected spending on public consumption. Because of relatively large future tax payments from the pension funds, among other things, the Danish sustainability problem is smaller than in many other OECD countries.

### **Policy recommendations**

The Danish economy is close to its capacity limit, and there is neither need nor room for further fiscal expansion in the form of unfinanced tax cuts or increased public spending. Even if the Danish economy develops less well than this forecast suggests, fiscal policy should not be expanded. Some tightening is needed in order to ensure a sustainable fiscal policy in the long run, even with relatively optimistic assumptions about the growth of labour supply.

There are strong arguments in favour of a change in the tax structure to a system with less weight placed on mobile tax sources such as capital returns and labour income, and greater weight – first and foremost – on land and property. Further, a reduction in personal income taxes in 2004 can only be recommended if it is financed by reductions in outlays or increases in other taxes.

Developments in the labour supply are of key importance to the long-run growth rate and to the sustainability of fiscal policy. A reduction in the tax on labour income will increase the labour supply. But the tax on labour income can be reduced in different ways, and the choice depends on the weighting between a decrease in income equality and an increase in labour supply.

The demographic developments that will mean a greater proportion of the population being elderly and a smaller proportion being in the labour force are not a threat to the standard of living in absolute terms; but it is an important question as to which generations are going to pay for the

increased public outlays. The distributional problems cannot be solved by an increase in economic growth, because the outlays to public transfers and consumption are expected to follow the growth in average income.

In Denmark, municipalities and counties impose income taxes at the local level. They have made an agreement with the government not to raise the average local tax rate in 2003. The counties have failed to keep this agreement. Therefore the government has proposed the imposition of a general penalty on all counties, and a specific penalty on the counties that have raised the level of local income tax. But these rules are too rigid, because they fix the tax differences between counties and without taking into account differences in growth in income and changes in fiscal needs. A system that allows trading with increases and decreases of tax rates between counties would make all better off, while at the same time ensuring exact observance of the overall budget objectives.

The government and the opposition have agreed to increase public grants for house building. One element in the proposal is grants to homes for students and disabled. This is a reasonable initiative. Another element is a tax reduction for new rental housing. But general subsidising of rental housing cannot be recommended, because it is an expensive and inappropriate way to remedy the problems in the market for rental housing. A third element is the exemption from rent control for lofts that are converted into flats. This is a good initiative if it is the beginning of the abolition of rent control for rental housing in general. In isolation, the initiative will have hardly any effect on the functioning of the housing market.

## **Chapter II-VIII: Danish Labour Market Policies – Trends and Needs for Changes**

### **Introduction**

Unemployment in Denmark has declined significantly since 1993. Part of this development may reflect a shift in labour market policies, starting with the 1994 labour market reform. An important element in this reform was the abolition of the rule allowing the unemployed to renew their eligibility for benefit periods by participating in active labour market programmes. The maximum period for receiving benefits was reduced to seven years. Another element of the reform was the introduction of individual action plans in order to target efforts to the needs of the unemployed and of the local labour market.

Subsequent changes have aimed at strengthening active labour market measures, on the principle that benefit entitlements should be conditional on participation in active labour market programmes (the “rights and obligations” principle). The benefit period has gradually been shortened to four years, and participation in activation measures has been advanced correspondingly. Furthermore, availability and eligibility criteria have been tightened. A special youth programme was introduced in 1996, resulting in earlier activation and cuts in benefits. The latest reform, entitled *Flere i arbejde* (More people in work) was adopted this year.

In the beginning of the reform process, access to different leave schemes and early retirement was widespread, and was even expanded. It was thought that these measures would open up temporary jobs for the unemployed, but in practice many participants in the schemes came from unemployment. As labour market conditions improved, access to these schemes was made stricter or less favourable, and some schemes were abolished.

## **The institutional framework for labour market policies**

Labour market organizations play an important role in implementing labour market policies in Denmark. As a consequence, many labour market reforms are the outcome of tripartite agreements between labour market organizations and the government (social pacts). The “Danish Model” is characterized by labour market regulation through institutions which have been created and developed by the labour market organizations over the past 100 years. There is an obvious contrast between the regulation tradition based on individual rights in other EU countries and the Danish Model practice of negotiating collective agreements. The Model has survived changing labour market conditions over the decades, but it is not necessarily indestructible.

The collective bargaining system has begun to change over the last 10-15 years. Negotiations have become partly decentralized, so that today pay is to some extent determined at the industry or company level. Previously, negotiations between the central organizations on the employers’ side and the employees’ side, namely the Danish Employers’ Confederation and the Danish Confederation of Trade Unions, played a bigger role than today—although these negotiations did also contain elements of a more decentralized character. The core labour market players, however, still have a decisive role to play in negotiations about working hours, the collective labour market, pension schemes, etc. Another important change in this period has been the increased awareness of the significance of wage competitiveness for employment. In 1987, the Danish Employers’ Confederation and the Danish Confederation of Trade Unions agreed on a common declaration stating that wage increases in Denmark should be lower than abroad. This declaration set the norms for wage formation until at least the mid-1990s.

## **Unemployment and wage formation**

The unemployment rate has declined from 12 to 5 per cent since its peak in 1993. A considerable part of this reduction, between 2 and 3 percentage points, is due to the strong economic expansion throughout the last part of the 1990s. In the same period, a larger number of people on voluntary schemes of withdrawal from the labour market comprising early retirement, transitional early withdrawal benefits and paid leave schemes, reduced unemployment by 1-1½ percentage points. The remaining part of the reduction in unemployment, corresponding to 2-3 percentage points, can presumably be ascribed to changes in the framework for the labour market. Changes in labour market policy have without doubt contributed to this improvement, but more decentralised wage negotiations are also likely to have been a factor behind the fall in structural unemployment.

One sign of structural improvements on the labour market is the historically low unemployment rate combined with relatively modest wage growth. The historic relationship between wage growth and unemployment, on which many wage models are built, seems to have changed in recent years. At the end of 1990s, wage relationships incorporated into macroeconomic models such as ADAM and SMEC were consistently overestimating wage growth rates. This breakdown in established relationships between wages and other factors is an indication of improved labour market conditions.

The active labour market and social policies have seemingly been responsible for a considerable part of the decrease in the structural unemployment, although it is not possible to put exact figures on the contribution of specific policies. This is due to the fact that policy changes have been implemented as coherent packages that have underpinned and reinforced each other. Therefore, it is very difficult to imagine suitable methods of estimating the contributions of different policies to the decrease in unemployment.



Although there is considerable uncertainty involved in determining the level of structural unemployment, it seems likely that the current level of unemployment is close to the structural level. Consequently, a demand-driven decrease in unemployment will result in increased inflationary pressure. It is therefore necessary to improve labour market structures in order to achieve a sustainable fall in unemployment from the present level.

Wage formation has become more decentralized as a consequence of the ongoing implementation of new wage negotiation procedures. Because of these new systems, a greater part of the change in the wage rate is now determined at the firm level. A number of studies indicate that wage formation now reflects individual productivity and firm-specific conditions to a greater degree than was previously the case. An analysis of the return to firm-specific qualifications indicates that wage formation was more individualised in the 1990s compared to the 1980s. Furthermore, there are indications of increased wage dispersion through the 1990s in areas where wage negotiations were formally more decentralized.

### **Active labour market policies**

The favourable employment effects of the active labour market and social policies in the 1990s are remarkable because they have not been followed by increasing income inequality. This is primarily due to the maintenance of a high rate of replacement of unemployment benefits. Active labour market programmes (ALMPs) have been effective in testing whether the unemployed are actually available for work and thus have made it less attractive for the unemployed to receive benefits. This is in line with empirical evidence showing that job search by unemployed persons is intensified just prior to the time of enrollment in the ALMPs. In addition, people who receive benefits but have little or no interest in being available for work typically leave the unemployment insurance system when they are required to participate in ALMPs.

However, the actual objective of the active labour market policies – to improve the job prospects of the unemployed – has not been achieved. Analyses in this report show that some programmes in fact have negative effects on the probability of leaving unemployment. These negative effects are often due to the locking-in effect; that is, while participating in active labour market programmes, the unemployed reduce their efforts to find regular jobs. Furthermore, there is sometimes a negative post-programme effect, which can arise because the people who have been “activated” overestimate the value of the qualifications obtained in the programmes, leading to a higher reservation wage and a more narrow search.

On-the-job training in the private sector is the only programme with a positive effect on employment prospects, but this applies only to those who get a regular job immediately after the programme. Public sector on-the-job training, on the other hand, reduces the chances of the unemployed finding jobs for all subgroups in the analysis. Classroom training has a positive post-programme effect for some groups, but there is always a negative locking-in effect as well, so that the net effect is negative for all groups.

Though the active labour market policy in Denmark appears to improve the job market qualifications of some groups of unemployed people, a comprehensive evaluation of the policy must also take the costs of the policy into account. In this report an attempt is made to calculate the economic value of some of the effects of the active labour market policy. A tentative estimate of the net economic value of the policy indicates that it costs Danish society about DKK 6 billion per year in total. Table 2 shows the results of a cost benefit analysis of Danish active labour market programmes. Only private sector on-the-job-training gives rise to a net economic surplus – the remainder of the programmes are shown to give rise to deficits.

*Table 2 Economic benefits and costs of various active labour market programmes for those entering a programme in 1998. Net 2002 values, DKK billions.*

	<b>Private sector on-the-job- training</b>	<b>Public sector on-the-job- training</b>	<b>Classroom training</b>	<b>Other programmes</b>	<b>Total</b>
Benefits	1.23	-0.77	-2.61	-2.03	-4.18
Costs	0.01	0.04	1.65	0.03	1.73
Net benefits	1.22	-0.81	-4.26	-2.06	-5.91

Note: All amounts are stated in net current values as of the fourth quarter of 2002 using the corresponding general level of prices. A real discount rate of 6 per cent is used. The effects can be negative if a programme – contrary to intentions – decreases the participants’ chances of finding a job.

Source: Own estimates.

The importance of some of the effects of the labour market programmes has not been quantified. For instance, the requirement that unemployed persons participate in such programmes can serve to test whether the unemployed are willing to accept employment and therefore also whether they are eligible for unemployment benefits. Furthermore, the prospect of participation in a programme may produce an increased incentive to search for a job prior to the programme start. Both these effects would make the active labour market policy appear more beneficial if they were taken into account. However, even if these effects were relatively large, it would not change the conclusion that active labour market programmes reduce the chances of employment for the participants. If the most important purpose of active labour market policy were to improve the self-confidence and work-related networks of the unemployed, then the policy might be evaluated differently.

## **Unemployment insurance**

Those who are unemployed can receive financial support, either in the form of unemployment insurance or social security payments. The receipt of unemployment insurance payments – unemployment benefits – is conditional on membership of an

unemployment fund. Once a member has been unemployed for more than four years, the right to receive unemployment benefits is suspended until the member has been in employment for a period. Similarly, individuals who join an unemployment fund have to be employed for a period before they earn the right to receive unemployment benefits. The unemployment funds are financed by membership fees, contributions from the state and, to a small degree, contributions from employers who lay off members of an unemployment fund. As membership fees do not depend on the economy-wide unemployment levels, and the contributions from employers are small, the state bears the marginal cost associated with rises in unemployment.

The receipt of social security payments is conditional on recipients not being able to provide for themselves and their dependents. A person's legal dependents are his or her spouse and children. The amount of social security benefit that individuals or families can receive is related to their ability to provide for themselves. This means that if the spouse of a recipient of social security benefit experiences an increase in labour income, then the amount of social security benefit decreases. Social security benefit is financed in equal proportions by the state and the municipalities.

The unemployment insurance system is not optimally designed to induce job search and job acceptance on the part of the unemployed. Current levels of unemployment insurance compensation result in only small financial gains for individuals who change from unemployment to low-wage jobs. In recent years, however, labour market policy has improved the financial incentives to work. In the late 1990s, the length of the period for which unemployed persons could receive unemployment benefit was significantly shortened. The most remarkable adjustments have been made in the social security system. The action plan for employment which is due to take effect in the middle of 2003 will give rise to a marked improvement of the incentives to work for recipients of social security benefits.

A problem which relates to both the unemployment insurance system and the social security system is that tax payers bear the full increase in the costs of financing compensation to the

unemployed when the level of unemployment rises. This means that labour unions and employer organizations do not fully take into account the costs of unemployment to society. They may therefore agree on wage levels that lead to unacceptably high levels of unemployment.

## **Labour force mobility**

The lack of incentive to search for vacant jobs is illustrated by the fact that the geographical mobility of both employed and unemployed workers is very low. Analyses in the report show that regional migration rates have been in decline in recent years, and that the migration rate is relatively low compared to other countries. However, the low cost of dismissing workers in Denmark leads to a high job turnover rate.

The unemployed rarely move to get a job, and contrary to expectations, the propensity to move declines with the increasing duration of the period of unemployment. One explanation for this is the relatively high replacement rate of unemployment benefits. A higher replacement rate reduces the incentives to find a job in another region more than it reduces the incentives to find employment locally.

## **Labour force participation**

During the 1990s, the Danish labour market shifted from a situation with high unemployment to a situation with a shortage of labour. For the years ahead, a projection of changes in the size of the labour force shows that it may grow by 22,000 during the period 2001-10 and by a further 28,000 people from 2010 to 2020. A number of assumptions were made, so that the projection differs from a purely demographic one: fewer people will make use of early retirement programmes, the labour market integration of first and second generation immigrants will be improved, the fall in participation rates for persons aged 60-66 years will be halted, and the average number of hours worked will stop declining even though there has been a steady decline over recent decades. These assumptions – which to some extent can be said to be

optimistic – are the explanation for why the projection shows a modest increase in the size of the labour force even though the demographic developments in the Danish population would otherwise lead to a fall. This is due mainly to the fact that immigrants have labour force participation rates which are significantly below those of native Danes. In total it must be concluded that the government's goal of an increase in the labour force of 66,000 persons between 2000 and 2010 cannot be accomplished given the present policies.

### **Labour market policy recommendations**

One way of improving the financial incentives to work is to let unemployment benefits decrease as the spell of unemployment lengthens. Thus, the long-term unemployed would receive less benefit than the short-term unemployed. The concrete design of the decreasing profile of benefits should, however, await further analysis of the likely effects on employment and the effects on the distribution of income. It is worth noting that the suggested policy measure would not affect the income of the short term unemployed but would improve the incentives to work for everybody.

In recent years, wage negotiations in Denmark have become increasingly decentralized. This aggravates the problem that the parties to the labour market do not take into account the cost to society of financing unemployment insurance. A reform should be considered in the way unemployment insurance is financed so that employers and workers bear a greater part of the marginal cost of increases in levels of unemployment. Part of such a reform could be the suspension of unemployment benefits for the first few days of a period of unemployment.

In the current Danish system, employers pay unemployment benefits for the first two days of unemployment of laid-off workers who happen to be members of an unemployment fund. Employers have no costs in laying off workers who are not members of an unemployment fund. Extending employers' payments of benefits to laid-off employees could also be expected to reduce the number of temporary lay-offs.

The recent labour market reform *Flere i arbejde* reduces the extent of active labour market programmes. The unemployed are no longer required to participate in programmes for 75 percent of the time after the first year of unemployment. Instead, they are required to participate in a programme every time they have had six consecutive months of unemployment after the first year of unemployment. Hence, the principle of “rights and obligations” to participate in active labour market programmes in order to receive benefits has not been changed, and the content of the programmes has not changed either.

On the basis of the analyses in the report, a thorough revision of the content and extent of the different active labour market programmes is recommended. This revision should be even more extensive than that involved in the policy reform *Flere i arbejde*. Focus should be shifted to a much higher degree to supporting the unemployed in their search for work and also to placing them under an obligation to search. Evidence from other European countries shows that even simple job search courses have positive effects. In particular, systems where the unemployed are monitored, and sanctions are taken if they fail to meet certain minimum requirements regarding job search, are successful in achieving the desired effects. The sanctions could be a reduction in benefits for a limited period if the unemployed person does not apply for a certain number of vacant jobs each month. Such systems do not lock the unemployed into programmes, and they may carry little additional cost, since there is already a system for employment service and benefit administration in place. In addition, they have no serious implications for the income distribution.

There are no positive effects of public sector on-the-job training on employment prospects for the unemployed participants in such programmes. On the contrary, there is a strong negative locking-in effect during participation, and there is also a negative post-programme effect. Furthermore, those participants who subsequently manage to get a job are employed for a shorter period than if they had not participated in the programme. Thus, it is necessary to consider how public sector on-the-job training can be improved and to what extent there are some elements of the programme that can be built on. The

net loss involved in public sector on-the-job training is almost DKK 1 billion (see table 2).

Classroom training is by far the most widely used active labour market programme, but the post-programme effect is positive only for women, unemployed skilled workers and older unemployed workers. However, there is always a strong negative locking-in effect, so that all groups experience a negative net effect on the transition rate from unemployment to employment. Hence, the extent of classroom training should be reduced, and it should be better targeted toward groups whose labour market position can be improved by such programmes. This probably means that the programmes should be of longer duration and be more vocationally orientated. In particular, the unemployed with the lowest qualifications may have a need for vocational and classroom training of longer duration if their employment prospects are to be improved.

The results of the analyses of the effects of active labour market programmes in Denmark are disappointing, but they are in line with experience from several other European countries. A new international study concludes that many programmes have been introduced by politicians without any prior knowledge of their effects, and that study calls for better communication between policy-makers and the scientific community, so that independent evaluations play a more important role in the implementation of the programmes.<sup>1</sup> Sweden, for instance, has established an institute for labour market policy evaluation (IFAU). In light of the fact that Denmark is among the countries that spend most money on their active labour market policy as a proportion of GDP, it is highly relevant to have independent evaluations and cost benefit analyses carried out continuously, so that the active labour market policy can be designed in the best possible way.

Efforts aimed at increasing the labour force should take as their starting point the fact that the number of persons aged 60

1) See Kluge, J. and C.M. Schmidt (2002): Can Training and Employment Subsidies Combat European Unemployment? *Economic Policy*, 35, pp. 411-448.



years or more in the population will increase during the next few years. Further, the number of first and second generation immigrants will also increase. As these two groups are precisely those for whom labour force participation rates are significantly below average, it is natural to target efforts at them.

There exist two early retirement schemes in Denmark. The traditional early retirement system is for persons of working age who have completely or partially lost their ability to work (*førtidspension*). The other system is the “post-employment wage” for persons aged 60-64 years (*efterløn*). Entering this scheme is not contingent on any disabilities, but only on age and payment of contributions over a certain minimum number of years. Persons of working age who have full capacity for work should not in general be entitled to receive government transfers. Therefore, the post-employment wage scheme should be abolished. The original goal of the post-employment wage was to ensure that employees who had become exhausted after many years of work, primarily those in low-skilled jobs, should have an opportunity to leave the labour force at the age of 60 rather than through the old age pension scheme. However, the scheme no longer fulfils its original goal. People aged 60-64 who are worn out after many years of work should of course be able to leave the labour market – as should everybody else of working age whose capacity to work has been lowered.

The purpose of the traditional early retirement system is to provide people who have lost the ability to work with an acceptable standard of living. The present administration of this system has most probably been affected by the existence of the post-employment wage scheme. Hence, the criteria for awarding persons early retirement benefits should be reconsidered in connection with the abolition of the post-employment wage. It is important that politicians announce the future rules for early retirement within a relatively short period of time, thereby making it possible for persons who currently are in the labour force to plan ahead. The abolition of the post-employment wage scheme should take place over a limited period of time. Younger people who have contributed to the scheme and who will not be able to receive a post-employment wage due to

the abolition of the scheme should naturally have their contributions repaid.

The demographic developments predicted in the Danish population for the coming years mean that there exists a great potential for growth in the labour force by improving the labour market integration of first and second generation immigrants. Analyses show that the employment and labour market participation rates of these groups, which are generally below average, can be mainly attributed to the fact that immigrants have a significantly lower level of education as well as fewer years of labour market experience compared to ethnic Danes. Further, a much larger proportion of the immigrant population receive government transfer incomes than is the case for native Danes. This means that the immigrant group on average has greater incentive problems in connection with the labour market, due to the automatic reduction in government transfers as labour income increases. An increase of the labour market participation of immigrants therefore mainly requires an improvement of the overall characteristics of this group with respect to the above factors. This improvement should include further education which significantly enhances opportunities in the labour market. In addition, new initiatives may help immigrants to overcome the entry barrier into the labour market, and may thus have a positive effect. Such initiatives can be job training, practical experience with firms, or the like.