ENGLISH SUMMARY

Chapter I: The Danish Economy

In 2005 and 2006, annual GDP growth in Denmark exceeded 3 per cent. It is expected that in 2007 the economy will grow by only 1½ per cent. Demand remains solid, but demand growth rate is expected to slow down somewhat. The labour force is expected to shrink over the coming years; this is primarily attributable to demographics and to an expected normalization of the business cycle. In the coming years an even lower rate of growth in GDP is expected, due to the fall in the size of the labour force and to the return of the economy to a neutral position in its cycle. On this basis, employment is expected to decrease over the coming years, leading to lower GDP growth rates.

The current low level of unemployment means that the pressure on the labour market remains significant, and wage acceleration can consequently be expected. The present forecast indicates a "soft landing" for the economy, but a more abrupt ending of the economic upturn cannot be ruled out, since there are several risk factors present in the global economy. Furthermore, wages may accelerate faster than anticipated, constituting a risk to the Danish economy.

Chapter I presents a short-term forecast for the Danish economy as well as a medium-term projection up to the year 2015. In the long run, GDP growth is determined by the size of the structural labour force, structural unemployment, growth in productivity, and changes in hours worked. The size of the structural labour force is expected to remain almost constant, while structural unemployment is expected to slowly decrease. It is estimated that the trend growth in hourly productivity is of a little less than 1½ per cent a year, while hours worked are expected to decrease. Overall, this implies a trend growth rate in GDP of approximately 1¼ per cent a year.

Production is presently above trend and consequently the output gap is positive and amounts to around 2 per cent of structural GDP. Unemployment is substantially below its structural level, and the size of the labour force is far above its structural level. As a consequence, current employment is considerably above its structural level. Over the coming years a normalization of the cycle is expected, implying that unemployment will gradually increase and the labour force gradually decreases in size. Hence, GDP growth will be below trend for a number of years, and the average GDP growth rate as we approach 2015 is expected to be around only 1 per cent a year.

The level of employment is historically high, and unemployment is at its lowest level since the beginning of the 1970s. Unemployment has fallen by approximately 100,000 persons during the past 3½ years, and employment has increased by nearly 150,000 persons during the same period. The large increase in the size of the labour force is primarily due to the economic upturn and to the increasingly more open borders within the EU, leading to a significant inflow of foreign labour.

Labour productivity fell in 2007. This may be attributable to the economic boom that has allowed a number of people with low levels of productivity to move into employment. However, over the coming years they will increase their productivity – at maybe even a greater pace than settled workers are able to – and this promises faster productivity progress compared to this year.

Private consumption growth has been low over the last quarters, but various indicators point in the direction of a resurgence. Over the coming years, employment is expected to decrease slowly from its current high level. Nevertheless, disposable income will continue to grow significantly, due to the agreement enacted by Parliament on income tax cuts. The investment ratio (investments relative to GDP) has increased significantly but is expected gradually to level out. Despite a significant dampening of US growth, triggered by the housing market and the financial crisis, Danish export market growth is expected to remain above trend for the years to come. This should ensure a solid export growth rate despite the fact that Danish wage increases, and ultimately export prices, are expected to rise faster then import prices.

Over the coming years, the strong demand will continue to challenge the flexibility of the labour market. In the forecasts, it is assumed that a significant part of the demand growth will be met by foreign production, i.e. increases in imports. All in all, however, it is expected that increased import growth rates will dominate the effects of improved terms of trade and the expected bright export market performance. On this basis, the current account is expected to be negative in a couple of years.

The tight labour market is expected to lead to wage acceleration over the coming years – wage increases are expected to reach 5 per cent a year, which is significantly higher than among Denmark's closest trading partners. Import prices will still increase only modestly, while oil price inflation and higher wage increases will cause an upward trend in the overall rate of price increases. Inflation is expected to reach around 2½ per cent annually over the coming years.

Projected fiscal policy is clearly expansive in the coming years, partly because of high growth rates in public consumption and partly because of tax cuts. As a consequence – and with the normalization of the economic cycle – the very large public sector budget surplus from recent years is expected to be gradually reduced. It is expected that the public sector balance surplus will be approximately zero in 2015.

Table 1 Short-term outlook for the Danish economy

	Current prices DKK bn.	Per cent of GDP	Percentage change, volume				
	2006	**2006**	**2006**	**2007**	**2008**	**2009**	**2010**
Private consumption	793.5	48.3	3.1	2.2	2.6	2.5	2.2
Public consumption	419.6	25.6	1.5	1.8	1.7	1.0	1.0
Gross fixed capital formation	370.8	22.6	12.7	5.0	1.3	1.8	1.0
consisting of:							
Residential investments	108.5	6.6	12.0	8.9	-2.7	-1.1	-0.9
Business fixed investments	230.5	13.2	13.5	4.9	3.0	2.5	1.8
Public investments	31.8	1.9	13.1	-12.0	5.0	8.0	1.8
Stockbuilding [a)]	9.6	0.6	0.3	-0.2	0.0	0.0	0.0
Total domestic demand	1,593.6	97.0	5.2	2.4	2.0	1.9	1.6
Exports of goods and services	853.1	52.0	10.1	2.3	2.1	2.7	2.7
Imports of goods and services	804.5	49.0	14.4	4.2	2.9	3.8	4.1
GDP	1,642.2	100.0	3.5	1.5	1.6	1.4	0.9
Key indicators							
Consumer prices, percentage change [b)]			2.1	1.9	2.4	2.6	2.1
Unemployment, per cent [c)]			4.3	3.2	2.9	3.1	3.5
Current account, DKK bn.			39.5	21.5	17.2	11.7	-0.8
Current account, per cent of GDP			2.4	1.3	1.0	0.6	0.0
General government financial balance, DKK bn.			76.5	68.3	60.3	55.6	48.0
General government fin. balance, per cent of GDP			4.7	4.0	3.4	3.0	2.5
Hourly wage costs, percentage change			3.1	4.3	4.8	5.0	4.5
Terms of trade, percentage change			-0.5	-0.7	0.7	0.9	0.6

a) The percentage changes are calculated as 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.

Note: The DKK/USD exchange rate is taken as 5.94 in 2006, 5.44 in 2007 and 5.08 in 2008-10.

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

Policy recommendations

The current economic upturn has led to a significant shortage of labour, and it is necessary to increase the size of the effective labour force. The Danish parliament has introduced a welfare reform which includes a series of labour market policies aimed at contributing to a reduction in structural unemployment. In addition, the Government has indicated that it will initiate a string of measures which will increase the size of the labour force. Some of these measures are aimed at attracting more foreign labour to Denmark. In chapters III and IV several recommendations are presented on how to maintain or increase the foreign contribution to the Danish labour force.

To increase employment, the Government has proposed tax cuts for persons still working at the age of 64. This has previously been recommended by the chairmanship in *Danish Economy,* Spring 2007. If the tax cuts are given to those who turn 64 in 2010 or later, it is estimated that the initiative will be fully financed if just one third of those who would normally retire as 62-year-olds postpone their retirement from age 62 to 64. However, if the cut is given to all 64-year-olds in 2008, the initiative will be significantly more expensive in the short term and have only a limited additional effect on the labour supply.

In addition, the Government has announced that it will make it possible for persons on disability pension to work for a period and then return to the disability pension scheme later on. Potentially, this could contribute to increasing the effective labour supply, but at the same time there is a risk that it will increase the general inflow to the disability pension scheme. Another risk is that it may involve an unintended increase in the inflow to subsidised jobs, the so-called flexi-jobs, which are also designed for people with limited capacity to work. The inflow to flexi-jobs has been substantial in recent years, while at the same time the number of people entering the disability pension benefit scheme has not fallen correspondingly. There are therefore good reasons to consider the incentives structure in this arrangement.

Another element in the Government's efforts to increase the labour force is the tax cuts introduced in extension of the medium-term fiscal plan, the 2015 plan. The tax cuts will mean an increase in the earned income tax credit, combined with an extraordinary increase in income transfers in 2008 and an increase in the basic allowance for the middle tax bracket in 2009. Overall, income tax will be reduced by approximately DKK 10 billion, which is equivalent to 0.6 per cent of GDP. It is estimated that labour supply will be increased by around 5,000 people working full-time, which is equivalent to 0.2 per cent of the labour force. Had the tax cuts been given as reductions in the tax rate for the top tax bracket instead, the effects on labour supply would have been larger, but with very different distributional consequences.

Apart from a small contribution from indexing energy fees, the tax cuts will not be financed in the short term. At the same time, public expenditure on consumption and investment is expected to increase significantly. Public consumption is expected to increase by 1¾ per cent in 2008. One factor behind this high rate of growth in public expenditures is that municipal consumption expenditures are expected to increase by more than agreed upon between the municipalities and the central Government. The current system does not have any clear sanctions on the individual level. The agreement system should therefore be supplemented with clear sanctions known to each municipality before the budget is set, or be replaced by another system. One possibility is tradable municipal "expenditure rights" (see *Danish Economy,* Autumn 2006).

The projected fiscal policy will contribute to increasing total demand. During the current economic upturn it is inappropriate that fiscal policy should contribute to increasing the pressure on the labour market. It is estimated that fiscal policy will contribute to GDP growth by half a percentage point in 2008 and by a quarter of a percentage point in 2009. In other words, the projected fiscal policy will make a significant contribution to greater wage increases and to the substantial deterioration of the competitiveness which seems likely to occur during the coming years.

Even if substantial structural policy reforms that noticeably reduce the pressure on the labour market are carried out, there is no reason to put further pressure on the economy through fiscal policy. If pressure on the labour market were to be eliminated through structural policy reforms, structural employment would have to be increased by approximately 50,000 persons. It is hard to imagine that reforms could be made to influence the labour market on such a scale in the short term. And even if that were the case, a neutral fiscal policy would be appropriate.

If no labour market policy reforms are carried out, fiscal policy should not only be neutral, but should actually reduce GDP growth. On the basis of the analyses of fiscal policy in *Danish Economy,* Spring 2007, fiscal policy should dampen GDP growth by up to half a percentage point in 2008. However, that forecast, based on low growth rates and a risk of the international economy being affected by the financial crisis more severely than anticipated in our main scenario, implies that a smaller degree of tightening is suitable. In the absence of policy reforms, a dampening of the GDP growth of one quarter of a percentage point in 2008 and 2009 is recommended. This is three-quarters and half of a percentage point lower than in our present forecasts, respectively.

A reduction of GDP growth of one quarter of a percentage point can be obtained in many ways, but it can hardly be implemented without a significant reduction in the projected growth in public consumption (see the calculations in section I.8). A tighter fiscal policy will lead to a faster increase in unemployment, and thereby reduce the risk of untenable expectations for future wage rises. A tightening of fiscal policy will at the same time create a permanent improvement of the public finances of the magnitude of 1 per cent of GDP in comparison to the situation where the fiscal policy is expansive, as currently planned. The recommended tightening of fiscal policy would also contribute significantly to a reduction of the long-term fiscal sustainability problem.

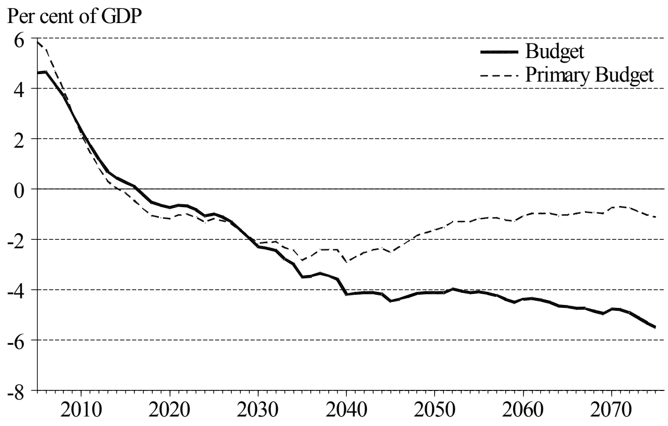
Chapter II: A Long-Term Projection of the Danish Economy

Chapter II presents a new long-term projection of the Danish economy which builds upon the medium-term projection to 2015 presented in Chapter I. The long-term projection period is the 21st century, although the decades up to 2040 are emphasized. The projection has been made using the computable general equilibrium model DREAM.

According to the projection, the labour force will be reduced by about 5 per cent during the next decade. Thereafter, the retirement rules of the welfare agreement from last year will result in renewed labour force growth. Because of the expected continued productivity growth, the material living standards of the population are expected to grow considerably. GDP per capita is expected to double before 2050. At the same time the consumption to GDP ratio increases permanently in the projection, accompanied by a decline in the ratio of private sector wealth to GDP.

The government budget worsens considerably during the projection, as shown in Figure A. This is partly due to demographic factors, but also to the fact that government revenues in the base year are considered to be extraordinarily large.

Figure A Government Budget in the projection



Note: The primary budget is equal to the actual budget minus net interest expenditures. When the actual budget deficit is larger than the primary budget deficit, net government debt – and consequently interest expenditure – is positive. In the projection, net government debt equals 38 per cent of GDP in 2040.

Compared to the medium-term "2015 Plan" which the government presented in August, the projection in the present chapter produces a more negative view of public finances in the long run. Consequently, the projection concludes that there are still problems concerning the long-run sustainability of Danish fiscal policy. However, long-term projections like the one presented here are inherently very uncertain, with uncertainty increasing the further into the future we look. Hence, it is not possible to answer with complete confidence the question of whether Danish fiscal policy is sustainable today, given the specific ambitions for the labour force stipulated in the 2015 Plan.

According to the assumptions underlying the Government's 2015 Plan, Danish fiscal policy is sustainable. According to the central assumptions decided upon in the projection presented in this report, the result is reversed and the budget must be permanently improved by an amount corresponding to about 1½ per cent of GDP in order to ensure sustainability. Under the condition that the specific requirements of the 2015 Plan regarding the size of the labour force and hours worked are fulfilled, the budget should still be permanently improved by around three quarters of a per cent of GDP to obtain sustainability. This corresponds to about DKK 12 billion at present price and wage levels.

As present fiscal policy is unsustainable according to the projection, the budget needs to be improved at some time. How this should be done depends on several independent choices. Basically, fiscal sustainability may be obtained by actions which increase revenues or decrease expenditures. Revenue-increasing actions may be tax reforms which result in a net surplus, or reforms which effectively increase the labour force, whereas expenditure reductions may be obtained by reducing government consumption or public transfers. The instruments chosen here affect the economic conditions of life for people alive at the time of the reform.

Another independent choice is *when* to improve the budget. The intertemporal distribution of the increased burden affects the economic conditions of life for the various generations alive at different points in time. Economic science does not provide any objective answers as to how this intergenerational distribution is optimally designed. Economists play a role by pointing out various costs and benefits of certain possible strategies, but the issue is fundamentally one of distributional policies, which the population and its elected representatives alone should decide upon.

It does seem natural, though, that a trade-off between the interests of the various generations should take into account the standards of living which otherwise affect them. Over time, consumption possibilities for different generations will be influenced by several different factors: exogenous phenomena such as business cycles, changes in economic policy, the varying size of the generations themselves and finally the general perpetual productivity growth which generally ensures that younger generations become richer than their older predecessors. Even though the last effect clearly dominates in the long run, all the factors mentioned may influence the rate of growth in the consumption possibilities of the generations. Apart from this, the various generations also differ regarding other conditions of life.

For instance, younger generations have a considerably higher life expectancy than do the present oldest Danish cohorts.

In any case, it is important that the consequences for different generations of different budget financing strategies are presented clearly so that the impact of various choices is made evident.

Given the uncertainty as to whether the present fiscal policy is considered sustainable, the tax cuts and the extraordinary increase in government expenditure in 2008 and 2009 which form part of the 2015 Plan are remarkable. According to the calculations presented here, the budget deterioration will not be financed, in the sense that it aggravates the existing sustainability problem. This is true even though the tax cuts are expected to increase labour supply.

Taking a closer look at the specific labour force requirements of the 2015 Plan, the ambition for longer hours worked on average for those in employment is relatively new. As it has not been thoroughly investigated how longer hours worked can be ensured without undesirable side effects, the decision to appoint a labour market commission to go into the question deeply seems like a good idea. However, it can be debated whether it is advantageous to decide in advance that the majority of the necessary fiscal sustainability improvements should come from this particular change, given the fact that it is not clear which instruments are best suited to influence hours worked, and which side effects these instruments may have.

In order for the general public to be able to judge how realistic the 2015 Plan actually is, it is important that all central assumptions behind the plan are made visible. This is true for the period up to 2015 as well as for the long-run projection after 2015.

It is worth discussing whether the specific goals of the 2015 Plan are sufficient for the objectives that such mid-term plans should fulfil. One overall ambition is that the plan should be compatible with a sustainable fiscal policy. In the operational time frame consisting of the period up until 2015, one of the overall goals of the 2015 Plan is to maintain a structural budget surplus of between ¾ and 1¾ per cent of GDP until 2010, and at least a balance in 2011-15.

Given the long-term projection of the plan, this is sufficient to ensure sustainability. However, the structural budget cannot be immediately observed, which makes it difficult to decide whether actual development will in fact be compatible with this goal. That is why it is relevant to supplement the overall aim of the structural budget with more specific benchmarks.

The plan contains further requirements for government consumption expenditures, which may not exceed 26½ per cent of GDP in 2015. However, focusing on a single element in the budget may lead to an undesirable change in the balance between this element and the other elements over time. Therefore, it seems desirable that a medium-term plan should specify the anticipated development for all main budget posts: direct and indirect tax revenues, transfers, government consumption and investment. In particular, investments have a clear intertemporal dimension which might mean that they deserve special attention in a medium-term context. Decreasing investment levels in order to improve the budget implies a smaller government capital stock in the long run and hence does not necessarily improve the total situation with respect to future government assets.

Chapter III: The role of immigration for the labour force

The flow of people migrating to or from Denmark has seen a steady increase since World War II, with a positive net migration into Denmark of 5-10,000 people per year over the last two decades. Migration is expected to increase in the coming years as the process of globalisation continues. Immigration will affect the Danish economy more than before as the number of immigrants in the labour force increases. In this context, the increased international mobility of labour poses major challenges for the Danish economy.

Over the coming decades, demographic changes will, on the one hand, reduce the size of the Danish labour force, while, on the other hand, they lead to a decrease in the migration potential in Eastern European countries. These changes will – combined with comparatively greater demographic shortfalls in a number of major neighbouring economies such as Germany and Sweden – presumably considerably increase competition for both permanent and temporary labour migration.

There has been a shift in the composition of migration into Denmark since 2002. Changes in immigration rules have prompted a decrease in the number of immigrants admitted for humanitarian reasons (encompassing mainly refugees and family reunification), and this has been partially offset by an increase in labour immigration. Targeted labour immigration regulations, such as the job card scheme and special rules regarding workers from the ten new EU countries in Eastern Europe (the so-called "Eastern Worker agreement"), have led to low but increasing immigration flows since their introductions in 2002 and 2004 respectively.

Strong labour demand in the Danish economy has led to a rapid influx of temporary migrants, cross-border commuters and foreign firms operating in Denmark. In particular, the construction and manufacturing sectors have benefited from this additional labour force.

Analyses reveal substantial differences in the average duration of stay across categories of immigrants. Humanitarian immigrations have a permanent character, and accordingly also exhibit by far the longest duration of stay in Denmark, while labour immigrations – and in particular educational stays – are typically temporary and shorter. The shift from humanitarian to labour immigration has therefore led to shorter average durations of stay.

Wages among recently arrived immigrants are more unevenly distributed than among ethnic Danes. Some have a low income, while others have a higher potential income. Some of the best qualified could be tempted to move to other countries with lower taxation. However, a statistical analysis rejects the hypothesis that more highly skilled immigrants have a higher propensity to emigrate.

Over the last two decades an increasing number of Danes have emigrated and stayed abroad for a longer period than previously. However, the propensity to emigrate is correlated with higher educational achievements, and the increased emigration rate over time seems to be driven mainly by increases in the average educational level of the Danish population.

The increased permanent immigration for work-related reasons as well as the greater influx of temporary workers have contributed considerably to the size of the Danish labour force over the past years. Permanent immigration in 2003-2005 increased the labour force in 2006 by approximately 15,000 persons, while the number of cross-border commuters rose by around 25,000 between 2005 and 2007. This inflow of workers and the increased number of foreign firms operating in Denmark can – given the low unemployment rate – to some extent account for the relatively modest wage increases over the last years. The recent developments in migration and wages indicate that migration has contributed to the flexibility of the labour force. This increased flexibility of the labour force could lead to a lower rate of structural unemployment in the Danish economy.

A dynamic computable general equilibrium analysis reveals that immigration with the current composition does not improve the long-term sustainability of the Danish fiscal policy and welfare system. Immigrants receive fewer welfare services over their full lifetime, but also pay less in taxes, since their average participation rate is lower than among ethnic Danes. However, immigration may contribute somewhat to the sustainability of the Danish welfare system if structural unemployment is reduced and more work-related immigration and a higher educational level among immigrants lead to higher participation rates and higher wage incomes among immigrants.

The chairmen of the Danish Economic Council recommend a considerable simplification of the Danish immigration policy. The regulations should stimulate immigration of highly-educated workers and support temporary immigration in times of strong labour demand in Denmark. Specifically, it is suggested that work-related immigration be governed by only two sets of rules for people from outside the EU and Nordic countries: a generalized job card scheme which would provide work permits to persons with a job offer in Denmark, and a simplified green card scheme that would provide work permits to highly qualified workers.

It is suggested with respect to the job card scheme that workers with a job offer that will lead to annual earnings of at least DKK 250,000 per year should be able to obtain work and residence permits for two years (with the possibility of extension) if the job in question meets the standard Danish wage and employment criteria and involves at least 30 working hours per week. This should facilitate the hiring of foreign workers under the standard Danish wage and employment regulations, while ensuring that immigration does not undermine unskilled residents' employment and wage conditions.

It is suggested that the duration of work permits based on the job card scheme be restricted to two years in order to signal that the role of that scheme is to alleviate short-term shortages of labour. The introduction of yearly quotas for this type of work permit could also be considered, letting the quota vary with the expected labour market conditions in Denmark. As long as the measured unemployment rate is below the structural rate of unemployment, a large quota is necessary, while the opposite is the case when the measured rate of unemployment is above the structural rate.

The qualifications of the Danish labour force need to rise hand in hand with those of the work forces in other developed countries if Denmark is still to benefit from globalisation and increased international trade. In order to attract workers with documented high qualifications, it is suggested that persons between the age of 18 and 59 with a documented degree at bachelor level or higher should be able to obtain residence and work permits in Denmark. This would constitute a simplification and liberalisation of the current regulations in the Danish immigration law, according to which highly-qualified workers can obtain a six-month residence permit to search for work in Denmark.

The Danish welfare system may make it less attractive for foreign specialists to work in Denmark, since they contribute in full to the system – through tax payments – but only enjoy a limited share of the welfare services. Under the current regulations, foreign specialists can therefore – during a transitional period of 3 years – be taxed less than others by paying labour market contributions and a gross income tax of only 25 per cent. It is suggested that the transitional period is extended by an additional two years, during which a gross tax rate of 33 per cent would apply. This would maintain a strong incentive to come to Denmark, while offering a gradual transition to the regular tax system for specialists who stay longer.

There is a considerable immigration to Denmark for educational purposes, but only very few people stay for several years in Denmark and use the education they obtain here. Students from outside the EU and Nordic countries pay tuition fees in Denmark. One way to make it more attractive for foreign students to use their skills in Denmark would be to introduce a tax credit system for graduates who have paid for their education (in Denmark or abroad) with respect to their subsequent labour income in Denmark.

The proposal could be extended to all Danish graduate students, as suggested earlier by both the Welfare Commission and the chairmanship of the Danish Economic Council (*Danish Economy*, Autumn 2003). The tuition fees for graduate students would be financed by individual state-backed loans, which should in principle be repaid after graduation. However, all graduates would receive a tax credit with respect to their subsequent labour income equal to the instalments and interest on the loan. This proposal would thus be fully neutral for students who stayed and worked in Denmark after graduation. Since the proposal would also encompass tuition fees for graduate studies outside Denmark, it would act as a tax reduction for highly educated immigrants who come to Denmark with a paid-for foreign education. Graduates who emigrate – and thus do not contribute to the financing of the Danish welfare system through tax payments – would however pay for their graduate studies themselves. The inclusion of Danish students in the combined proposal of a tuition fee and a subsequent tax credit would make the Danish welfare system less vulnerable to emigration of highly educated workers.

Chapter IV: Integration of immigrants and their offspring

It is important that foreigners are integrated into Danish society, since this will secure them a living standard comparable to that of native residents as well as improving long-term fiscal sustainability.

Education is an important way of integrating young immigrants into Danish society.

The Danish education system is divided into three parts: “folkeskolen” (primary and lower secondary school) for children aged 6-16 years, upper secondary school and vocational training for persons aged 15-20, and further or higher education for persons aged 18 years or above.

Denmark has nine years of compulsory schooling, and about 85 per cent of the pupils attend a state school. Educational programmes available at the upper secondary school and vocational training level include both vocational training courses and general academic courses preparing students for further studies. The courses of further and higher education last between 2 and 8 years. Enrolment in longer courses of higher education normally requires matriculation from upper secondary school.

The education level for immigrants and second-generation immigrants from non-Western countries is lower than for ethnic Danes. Furthermore, the proportion of young people who do not finish a course of upper secondary education or vocational training is far higher for immigrants and second generation immigrants than for native Danes. Analyses in the present report show that immigrants and second-generation immigrants from non-Western countries get lower marks than Danes at the final test from lower secondary school. A substantially higher proportion of immigrants and second-generation immigrants fail the tests, and a significantly smaller proportion gets high marks. One explanation for this is that the parents of these pupils have a lower level of education, but even after correcting for this, immigrants still get lower marks.

Analyses in the report also reveal that Danish pupils who attend a school with more than 50 per cent of the pupils being from non-Western countries get lower marks in written Danish than pupils who attend a school with less than 10 per cent of the pupils being from non-Western countries. The same applies for marks in written maths when the proportion of non-Western immigrants is above 10 per cent.

About 85 per cent of all young people start a course of education at upper secondary level after finishing lower secondary education. Young people with high marks typically attend general academic courses preparing students for further studies, and those with lower marks typically attend vocational training courses. Parents' educational background and employment also have a significant influence on the choice of education at the upper secondary and vocational training level, especially for Danish pupils. Immigrants and second-generation immigrants have, all else being equal, a greater tendency to choose a general academic course.

Immigrants and second-generation immigrants who finish a general academic course get lower marks than ethnic Danes, even after a correction for marks from the final test at the lower secondary school.

Marks from upper secondary school are very important for both the probability of starting and for the probability of completing a course of further or higher education, while parents' educational background has only a minor influence. Immigrants and second-generation immigrants have a lower probability of finishing a course of further or higher education, even after correcting for differences in marks from the matriculation examination.

In summary, the analyses in the report show that immigrants and second-generation immigrants from non-Western countries acquire fewer skills in the course of their primary and lower secondary education, and this influences their results further on in the educational system. It contributes to the fact that a smaller proportion of immigrants and second-generation immigrants finish a course of higher secondary education, a vocational training course or a course qualifying them for some particular type of work. Only immigrants from Western countries, Asia and Latin America finish courses of higher secondary education in the same proportions as Danes.

It is a goal that immigrants and their children should get the same qualifications in school as Danish children. In the report it is recommended that new educational methods should be introduced in order to improve the level of success of immigrants in primary and lower secondary school. These methods must be evaluated in a systematic way. Some measures have already been introduced, but the results of these initiatives have not been tested. Furthermore, it is recommended that homework assistance after school is offered to everybody who is assessed as having a special need for aid.

Also, it is recommended that non-Western immigrants are dispersed more equally across schools in both the public and the private sector. In Denmark about 85 per cent of private school costs are financed by the Government, and it is therefore recommended that public contributions to these schools are increased by the proportion of immigrants and second-generation immigrants in the school.

An important element of vocational education is practical experience in a firm. However, analyses in the report indicate that it is particularly difficult for immigrants and second-generation immigrants to find a training place in a firm. It is recommended that firms should be financially rewarded if they hire trainees who have difficulty in finding a training place despite having good qualifications.

Integration into the Danish labour market of migrants arriving through family reunification

Participation in the labour market is another way of integrating immigrants. It is especially important for adult immigrants, because they do not have the same opportunities as the young immigrants of taking a course of education. In the analysis, we focus on family-reunified migrants.

Since 1999, all immigrants coming from outside the EU and the northern part of Europe have been offered free teaching in Danish for three years. Furthermore, immigrants who are not self-supporting are offered employment-promoting opportunities that lead to an improvement in their skills as well as to inclusion in on-the-job training programmes. Family-reunified migrants who are supported by their spouses may receive offers regarding employment-promoting opportunities, though these offers are not mandatory.

Less than half of the family-reunified immigrants are found to be participating in Danish language courses six months after their arrival, and even fewer have taken up some employment-promoting offer after around one year. On-the-job training programmes in the private sector are the most effective employment-promoting opportunities, while classroom training actually appears to worsen the chances of moving into employment.

Two out of three of the family-reunified immigrants are women between 25 and 34 years old. The immigrants mostly come from the Middle East, Africa and Asia.

On average, family-reunified men move into employment faster than family-reunified women. After two years of stay in Denmark, the probability of having been employed on the labour market for persons who are family-reunified with Danes or non-refugees is 75 per cent for men and 30 per cent for women. The probability of getting a job for persons reunified with refugees is 35 per cent for men and 10 per cent for women. After five years the probability of having been employed is 90 per cent for all men, while for women the probability is around 50 per cent for those reunified with Danes or non-refugees and about 30 per cent for those women that are reunified with refugees.

Many of the immigrants who came to Denmark before 1999, and thus prior to the introduction of the current integration rules, have only a slight degree of attachment to the Danish labour market. People in this group have difficulty in getting a job, because they have been out of employment for a long period and because they are older. On top of this, some of them do not have any economic incentive for getting into employment.

Therefore, it is recommended that all persons above 35 years of age with a marginal income on the labour market in the period from 2005 to 2007 should be granted an earned income tax credit amounting to 25 per cent of all labour market income. This earned income tax credit should be given for the coming three years and should decrease thereafter.