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The Good Society

A Comparative Study of Denmark
and Switzerland

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Preface

This book is a result of cooperation between economists and political scientists from Switzerland and Denmark. In some respects the two countries have much in common, but in matters of economic and political institutions they are very different. Still we describe both countries as “good societies” characterized by wealth and happiness. This has made a comparative study of the two countries very relevant as well as challenging and fascinating for the researchers.

The book project originated from the Danish association, The Good Society, which is an association set up by interested private sponsors. This association generously financed the project.

The Institute for Political Studies, Cepos, in Copenhagen, has been responsible for the administration of the project.

The responsibility for the book’s contents and the points of view expressed as well as the responsibility for any errors of fact or interpretation lies naturally exclusively with the authors. The book has been realized in a close cooperation between the researchers, and all the researchers have contributed to all parts of the book. However, the main authors responsible for each chapter are:

Henrik Christoffersen: Chaps. 1 and 12

Michelle Beyeler: Chaps. 6, 7 and 8

Reiner Eichenberger, with help from Marco Portmann and David Stadelmann:
Chaps. 3, 4 and 11

Peter Nannestad: Chaps. 1, 5, 6, 7, 9 and 10

Martin Paldam: Chaps. 1, 2, 5, 9 and 10

Finally, it should be mentioned that the first author has done most of the editing.

Copenhagen
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Henrik Christoffersen

Contents

1	Two Good Societies: Switzerland and Denmark	1
1.1	Similar Outcomes: High Income and Happiness	1
1.2	Different Economic and Political Systems	4
1.3	Structural Differences	5
1.4	How Do Small Countries Succeed?	5
1.5	The Puzzle: Different Systems and Similar Outcomes	6
1.6	The Perspective of This Book	7
	References	8

Part I The Quality of Life in Two Different Good Societies: Denmark and Switzerland

2	Two Wealthy Economies and Their Development	13
2.1	Comparing GDP per Capita	13
2.2	The Convergence Within the Developed World	15
2.2.1	A First Look	15
2.2.2	Sigma Convergence in the West	16
2.2.3	Denmark and Switzerland in the Pattern	18
2.2.4	The Relative Development Path	19
2.3	Globalization: Two Measures	21
2.4	Exchange Rates: The Exceptional Swiss Case	23
2.4.1	The Nominal Exchange Rate of the Swiss Franc	23
2.4.2	Inflation and Real Exchange Rates	25
2.4.3	The Northern and the Southern Inflation Regime	25
2.4.4	The Position of Denmark and Switzerland in the Pattern	27
2.5	Summing Up	28
	Appendix: Data Definitions and Sources	28
	References	29

3	Are the Standards of Living Similar or Dissimilar? An Extended Comparison	31
3.1	Introduction	31
3.2	A Refined Traditional Comparison	32
3.2.1	Gross Domestic Product	32
3.2.2	Income Distribution	38
3.2.3	Consumption Patterns in Denmark and Switzerland	42
3.3	Comparisons Based on Real Life Impressions	45
3.3.1	Work Life and Unemployment	46
3.3.2	Education	49
3.3.3	Life Expectancy and Human Development Index	50
3.4	Comparisons Based on Citizens' Behavior	52
3.4.1	Shadow Economy	53
3.4.2	Crime	54
3.4.3	Alcohol Consumption and Addictive Behavior	58
3.4.4	Suicides: A Permanent Form of Exit	58
3.4.5	Tourism: A Form of Temporary Exit	60
3.5	Conclusion	62
	References	63
4	Happiness in Denmark and Switzerland	65
4.1	Introduction	65
4.1.1	Happiness as an "Ideal Measure" for Comparisons	65
4.1.2	Comparing Denmark and Switzerland with Happiness Data	66
4.2	Description and Discussion of Subjective Life Satisfaction as Measure for Comparisons	68
4.2.1	Objective Versus Subjective Measures of Comparisons	68
4.2.2	The Strengths of Subjective Life Satisfaction as a Measure for Comparisons	69
4.2.3	Explaining Subjective Life Satisfaction and the Influence of Aspirations	71
4.3	Capturing Happiness in the Field	72
4.3.1	Comparing First Results Across Countries	73
4.3.2	The Happiness of Danes Is More Than Words: Danes and Swiss Living Abroad	74
4.4	Explaining Happiness in Denmark and Switzerland	75
4.4.1	Variables Influencing Happiness: An Overview	75
4.4.2	Determinants of Danish and Swiss Happiness	76
4.4.3	Happiness Schedules for Danes and Swiss	95
4.4.4	Comparing Denmark and Switzerland to Western Europe	97
4.5	Conclusions	104
	Appendix	105
	References	112

Part II Two Models of Good Societies

5 Two Stylized Models 117

5.1 The Model of the Capitalist Welfare State 117

5.1.1 The Big Compromise: As Big a Welfare State as Possible, Given a Healthy Private Sector 118

5.1.2 The Three Big Parts in the Corporative Tradition 119

5.1.3 The EFO-Model: The Scandinavian Economic Model of Competitiveness 120

5.1.4 Steering by the Model 121

5.1.5 The Two Sides in the Big Compromise 122

5.1.6 Potential Strains in the Model (1): Will Foreign and Domestic Debt Stay Under Control? 123

5.1.7 Potential Strains in the Model (2): The Upward Drift of the Public Sector 123

5.2 The Safe Haven Model 124

5.2.1 The Setup of the Safe Haven Model 124

5.2.2 The Safe Haven Package and the Good Cycle of Implementation 126

5.2.3 National Accounting and the Autonomous Posts of the Balance of Payments 127

5.2.4 Awash with Liquidity: The Case of a Floating Exchange Rate 128

5.2.5 Gray and Black Funds and the Gates of Whitewash 129

5.2.6 The Long-Run Stability of a Safe Haven 131

5.2.7 The Next Few Decades 132

5.3 Work Ethics: Why Do the Danes and the Swiss Still Work? 132

5.3.1 The Theoretical Problem Creator: Low Incentives and Real Revaluations 133

5.3.2 Labor Market Participation 133

5.4 Different Models: Common Prerequisites 135

References 136

6 Political Institutions and Politics 139

6.1 Introduction: Two Old and Stable Democracies 139

6.2 Power Sharing in Government, Executive-Legislative Relations, and Corporatism 141

6.2.1 Electoral Strength of Major Parties in Switzerland and Denmark 142

6.2.2 Swiss Government: Institutionalized Consociationalism 144

6.2.3 Denmark: Minority Governments and De Facto Consociationalism 144

6.2.4 Two Types of Executive-Legislative Balance 145

6.2.5 Corporatism 146

6.2.6 Swiss and Danish Consociationalism in International Comparison 147

6.3	Autonomous Regions Versus Centralized Decisions	147
6.3.1	Swiss Federalism	149
6.3.2	Danish Centralism?	153
6.4	Direct Democracy	156
6.4.1	Swiss Direct Democracy	157
6.4.2	Referenda in Denmark	159
6.5	Two Versions of Good Democracies	161
6.6	Conclusions	163
	References	164
7	Civil Society: Associational Involvement, Norms and Values	167
7.1	Involvement in Voluntary Associations	168
7.1.1	Comparing Associational Membership in Switzerland and Denmark	168
7.1.2	Trends in Associational Membership	172
7.2	Trust	174
7.2.1	Generalized Trust	174
7.2.2	Trust in Institutions	176
7.3	Value Orientations	179
7.4	Gender and Family Roles	184
7.5	Conclusions	185
	References	186
8	Two Variants of the Welfare State	189
8.1	Two Welfare Systems	190
8.1.1	A View from Social Expenditures	191
8.1.2	Welfare State Sectors and Welfare Generosity	193
8.1.3	Care Services	195
8.1.4	Comparing Standard Household Budgets	197
8.2	Distributional Consequences	199
8.2.1	Redistribution, Social Inequality and Poverty	200
8.2.2	The Distribution of Employment Among Different Age Groups	203
8.2.3	The Distribution of Paid and Unpaid Work Among Women and Men	204
8.3	Explaining Differences in Welfare State Development	208
8.3.1	The Demand Side: Industrialization and Post-industrialization	209
8.3.2	Politics, Institutions and the Development of the Danish Welfare State	210
8.3.3	Politics, Institutions and the Development of the Swiss Welfare State	211
8.3.4	Recent Reforms: Are the Differences Diminishing?	212
8.4	Conclusions	214
	References	214

9 Immigration 217

9.1 Immigrant Populations in Switzerland and Denmark 218

9.1.1 Ethnic Composition of the Immigration into the Two Countries 218

9.1.2 Educational Attainment Levels 219

9.2 The Absorption of Immigrants into the Labor Market 222

9.2.1 The Swiss Case 222

9.2.2 The Danish Case 222

9.2.3 Summing Up 225

9.3 The Economic Impact of Immigration 226

9.3.1 A Model: The Net Present Value of the Immigration 226

9.3.2 Impact on the Wealth of the Host Country 228

9.3.3 Immigration and Income Distribution 231

9.3.4 Immigration and Public Finances 232

9.3.5 Summing Up 234

9.4 Immigration Policy Regimes 234

9.4.1 Swiss Immigration Policies 235

9.4.2 Danish Immigration Policies 237

9.4.3 Differences and Similarities 243

9.5 Conclusion 244

Appendix: Cross-Flows of Immigration Between Denmark and Switzerland 245

References 247

Part III Challenges for the Two Good Societies

10 The Future of the Danish Welfare State 253

10.1 The Expansion of Public Employment in Denmark 254

10.2 Baumol’s Mechanism and the Productivity Growth Claim 256

10.2.1 Blue Policy: Fix the Tax Share 256

10.2.2 Red Policy: Fix the Real Share of the Welfare State 258

10.2.3 How High Can the Tax Pressure Get? 259

10.2.4 Comparing Productivity in Public and Private Production 259

10.2.5 Summing Up 260

10.3 The Welfare Coalition and Bureaucratic Growth 261

10.3.1 The Median Voter and the Welfare Coalition 261

10.3.2 Alternative Median Voter Models 261

10.3.3 One or Several Dimensions? 262

10.3.4 Some Empirics 263

10.3.5 Bureaucratic Growth 263

10.3.6 Observations of Bureaucratic Growth 264

10.4 Demography: An Aging Population 266

10.5 Good Luck and Good Policies 268

- 10.6 Globalization and the Welfare State 269
 - 10.6.1 State Convergence and “Race to the Bottom”? 270
 - 10.6.2 Convergence of Welfare Systems? 271
- 10.7 The Welfare State and International Labor Flows 272
 - 10.7.1 Immigration to Denmark 274
 - 10.7.2 Ethnic Heterogeneity and the Welfare State 275
 - 10.7.3 Heterogeneity of Skills and the Welfare State 276
 - 10.7.4 Emigration from Denmark 278
- 10.8 Concluding Remarks 278
- Appendix: The Mechanics of Baumol’s Law 279
- References 280
- 11 The Future of Switzerland 283**
 - 11.1 Introduction 283
 - 11.2 Switzerland’s Puzzling Performance 284
 - 11.3 Simple Traditional Explanations Fail 285
 - 11.4 The Puzzle Becomes Even More Puzzling 287
 - 11.5 Explaining the Puzzle 289
 - 11.5.1 Institutions Matter 289
 - 11.5.2 Rich Midsize Country: High Prices 294
 - 11.5.3 Low Productivity and Low Growth 295
 - 11.6 Future Developments 297
 - 11.6.1 Globalization 297
 - 11.6.2 Sustainability of Social Insurance 298
 - 11.6.3 Migration 299
 - 11.6.4 Mirages and Traps 302
 - 11.7 Effective Reforms 304
 - 11.7.1 Preserving and Perfecting Institutions 304
 - 11.7.2 Prevent Rent-Skimming 306
 - 11.7.3 More Effective Use of Scarce Resources 306
 - 11.8 Conclusions 307
 - References 309
- 12 The Good Society: Conclusion 313**
- Subject Index 321**
- Author Index 325**

Chapter 1

Two Good Societies: Switzerland and Denmark

What makes a good society? This question is one of the oldest in political economy. While widely different answers have been suggested over time,¹ the answer given by Aristotle still seems to us to have a strong intuitive appeal: “A good society is a society that enables its members to lead a good life”. This definition begets the next question: What makes a good life? The next section gives a first look at two answers:

A basic condition for having a good life is a ‘good’ income, and Switzerland and Denmark do have relatively high incomes. Income is a mean to the goal of happiness: Many polls have been taken throughout the world asking people if they are happy with their life. They show that Denmark and Switzerland are unusually ‘happy’ countries.

1.1 Similar Outcomes: High Income and Happiness

The most widely used objective measure for the possibility of having a good life is income, defined as (the logarithm to) GDP per capita.² The data are discussed in Chaps. 2 and 3.

Figure 1.1 shows the development of income in Switzerland and Denmark in the postwar period up to 2008, compared to GDP per capita in the EU-15 countries (without Denmark) – and at the end EU-27. Through most of the period GDP per capita has been higher in Switzerland than in Denmark and both countries have been higher than the average EU-country. During the last part of the period the gap has decreased substantially.

¹ In economics the original question has developed into the field of welfare theory where the answers given are very abstract.

² The reason to take the logarithm is that welfare theory claims that relative differences count more than absolute differences. If you are poor, it matters a lot to get an income raise of € 100 per month, but if you are rich, such a raise is less important, but it may increase welfare the same if you get a 10 % increase in the wage.

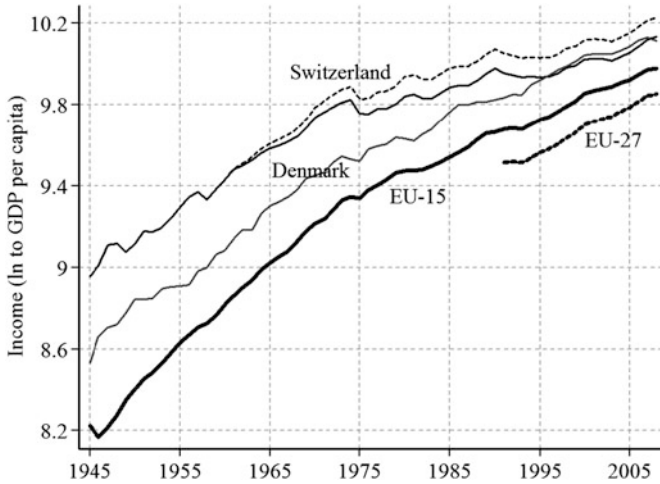


Fig. 1.1 Development of the average income since World War II (Note: The data used are from Maddison (2003); see also Appendix to Chap. 2. The two EU-lines do not imply that all countries in the sample were members all years. The *dotted line* for Switzerland is an attempt to assess the upper range for the Swiss income. Switzerland has had strong movements in its real exchange rate, giving large movements in relative prices. This makes it difficult to calculate the real GDP, and as discussed in Chap. 2 a range of estimates exists – hence the two series for the Swiss income)

The three lines on Fig. 1.1 move closer together throughout the period considered. At the start the range is 0.8–0.9. It means that Switzerland is twice as wealthy as EU-15. At the end the range is only 0.2–0.3. Here Switzerland is ‘only’ 25–30 % ahead. The reduction in the gap is part of the convergence process that has happened throughout the West due to increased integration. It will be discussed in Chap. 2.

The European Social Survey (ESS)³ asks the respondents: “How happy are you with your life?” The respondents are given a scale of possible answers from 0 (“extremely unhappy”) to 10 (“extremely happy”). This measure of happiness is further discussed in Chap. 4 below.

Figure 1.2 shows the average happiness levels for all countries that participated in the five ESS-rounds between 2002 and 2010⁴. The Danes stand out as the happiest people, and Switzerland is number 6. The difference is significant but rather small. Individuals may be happy or unhappy for many reasons, but the average happiness in a country must reflect ‘the society’ which all citizens have in common.

³ A similar question is used in both the World Values Surveys (WVS) and the European Social Survey (ESS). The pattern in the results is the same: Denmark and Switzerland always stand out as very happy countries. This is also the case when the sample of countries is extended to other Western countries and to the rest of the world.

⁴ The pattern is stable across the five surveys, so we just report the aggregate for all polls for each country.

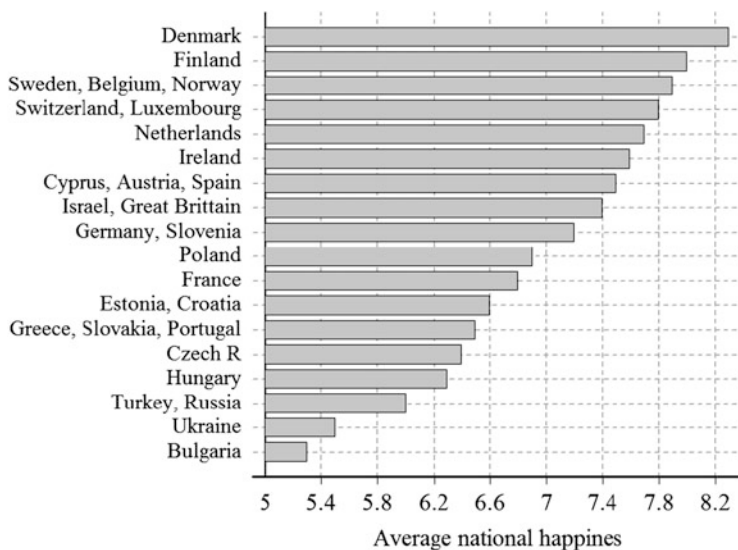


Fig. 1.2 Average national happiness scores 2002–2010 (Note: Calculated from the 223,255 valid answers to the European Social Survey. Only 1,732 respondents failed or refused to answer this item. Though large efforts are made to translate the question to mean the same across countries, some strange observations still emerge; i.e. notably the low score of the French)

Judged by our two criteria, Switzerland and Denmark thus stand out as two remarkable success stories, both absolutely and relative to comparable European countries. The countries are approximately equally rich per capita, and the populations are found to be almost equally happy. From that perspective both countries certainly deserve the label “good society”.

In many ways the two countries are similar: They are small Western countries, they are economically open capitalist market economies, and both countries are economically and politically stable. At the same time most observers looking at the two countries agree that both the economic and political *systems* in the two countries are different.

It is a recurrent theme in the book that the two countries *differ* from the rest of the West, but that a strong *convergence* pulls them toward the other countries, and hence each other. As the two countries have been relatively successful we shall concentrate on the differences. An important pattern is that the institutions have not converged, see Chaps. 4 and 5, but the outcomes have converged: This not only applies to income, but also to the welfare states and the immigration policies; see Chaps. 8 and 9 respectively.

1.2 Different Economic and Political Systems

Due to the strong convergence in the West much is similar in the two economies. We concentrate on the unusual traits in the economic model of the two countries in Chap. 3:

The unusual trait in the Danish economic model is that Denmark is the most developed *welfare state* in the world. Both taxes and general government expenditures are higher than everywhere else.⁵ What is less well known is that in order to remain competitive Denmark has been forced to be a more ‘market oriented’ capitalist country in other fields. Denmark has few state owned enterprises, very free trade, and the Danish labor markets are relatively flexible.⁶ It is obvious that the policy of being a capitalist welfare state has worked very well till now. The welfare systems in the two countries are compared in Chap. 8.

The unusual trait in the Swiss economic model is that the country is the largest offshore banking center in Europe, and many large multinational companies have their headquarters in Switzerland. International investors consider Switzerland to be a *safe haven*, and it is one of the few countries that have maintained the top triple A rating by the international credit rating companies throughout the periods during which such data have been published. This is due to low taxes and a stable economy. When a financial crisis occurs that causes exchange rates to devalue in other countries the Swiss Franc revalues, and it has actually revalued substantially relative to all other currencies.

Both countries are old and stable democracies. However, the political systems are very different, as discussed in Chap. 6.

Denmark is a representative parliamentary democracy with a unicameral parliament. In principle the 97 Danish municipalities are quite powerful: They have the right to tax and they administrate about 60 % expenditures. However, in practice the Danish state is rapidly limiting the space of municipal decisions, making the country increasingly centralized. Voters influence politics at the national parliamentary elections, where participation is high.

Switzerland, on the other hand, is a decentralized federal state with extensive direct democracy at all levels, a bicameral legislature and a convent-type central government with limited competences. Strong constitutional safeguards and traditions have kept the local governments rather independent. Voters influence policies via the many referenda, and much less at elections, where participation is comparatively low.

⁵ Denmark is now ahead of Sweden that has a rather similar welfare system. The difference to other EU-countries and Switzerland seems large at first, but it is smaller than it appears: Expenditures that are public programs in Denmark are often parts of (more or less compulsory) insurance schemes in other western countries.

⁶ One aspect of the market orientation in Denmark is well known. It is the Danish flexicurity model. The discussion of the model started on the political plan, and Wilthagen (1998) is as the first academic paper; see also Jørgensen and Madsen (2007).

Table 1.1 Ethnolinguistic and cultural divisions in Switzerland and Denmark

Groups	Denmark	Switzerland
Ethnic/linguistic	90 % Nordic, Western 5 %, others 5 %	German 65 %, French 18 %, Italian 10 %, Romansch 1 %, other 6 %
First language	Danish 90 %, others 10 %	German 63.7 %, French 20.4 %, Italian 6.5 %, Romansch 0.5 %, others 10.7 %
Religion	Lutheran 85 %, other, Christian 1 %, Muslim 4 %, none 10 %	Roman Catholic 41.8 %, Protestant 35.3 %, Muslim 4.3 %, Orthodox 1.8 %, other Christian 0.4 %, other 1 %, unspecified 4.3 %, none 11.1 %

Source: [CIA Factbook](#); [Statistics Denmark](#)

Civil societies also differ in the two countries. Compared to many other European countries, both Switzerland and Denmark have a rich associational life as well as high levels of institutional and general trust. However, in all three respects Denmark seems to (slightly) outperform Switzerland. Also, Swiss and Danes seem to rank some basic values differently, with the Swiss in general exhibiting a more conservative value orientation than the Danes, for instance with respect to attitudes towards work and to gender and family roles. These aspects of the civil societies in both countries are analyzed in Chap. 7.

1.3 Structural Differences

At the basic societal level Switzerland is a multicultural society with several religions, confessions and languages, while the Danish society is quite homogeneous; cf. Table 1.1. Thus the social fabric is fundamentally different in the two countries.

Immigration plays a much greater role in Switzerland than in Denmark. Immigrants make up about 10 % of the Danish population, but about 25 % of the Swiss population. The immigration to Switzerland has been dominated by immigrants from developed Western countries, while more than half of the Danish immigrants originate from less developed countries. These differences reflect immigration policies in both countries: Swiss immigration policy was for long driven mainly by labor market needs, while the rationale behind Danish immigration policies has been rather unclear; see Chap. 9.

1.4 How Do Small Countries Succeed?

The West has about 770 million inhabitants of which Western Europe has slightly above 400 million and the 4 overseas western countries are almost as big. Switzerland has 8 million and Denmark 5.5 million inhabitants, so both countries are rather small. They have a narrow resource base and hence they have to trade. Both economics and political science have seen large discussions of the consequences of the size of nations.

For the economist the concept of economics of scale suggests that large countries should do better. However the data does not support that notion. Alesina et al. (2005) survey the literature on the economic effect of the size of nations: It is quite clear that small countries tend to do as well as large ones provided that they are open.⁷

The political science discussion of the size of nations has been dominated by Katzenstein (1985), who presents data showing that the average small Western state is economically more successful than larger ones. It is argued (Katzenstein, 1985: 30–37) that the economic successes of small states are due to *corporatism*. Thus the successful outcomes in the two countries should be similar because both countries are corporatist. Chapters 5, 6, 7, 8 and 9 below compare the institutions in the two countries. They are found to be very different. Hence, for Katzenstein's conclusion to hold the term 'corporatist' has to be defined differently in the two countries.

In a broader sense political scientists and many economists argue that 'institutions' are crucial for development. This leads to the hypothesis that small states may do relatively well as it is easier to build good institutions in small states.

We shall argue that the only sense in which the institutions are similar is that they seem to work relatively well: They are handling internal and external imbalances relatively well. The key to success is thus that countries may manage to generate high levels of mutual trust and solidarity that allow them to be relatively flexible when problems occur. Small countries may be better at building such institutions. The causal links are thus from small to better steering to success.

1.5 The Puzzle: Different Systems and Similar Outcomes

This puzzle can be looked at from different angles. We believe that it is puzzling to the average Dane that the Swiss system with much smaller public welfare payments does not cause a big and seriously deprived underclass. It is probably similarly puzzling to the average Swiss that a country can collect well over 50 % of GDP in taxes without collapsing.

We think that the solution to this double puzzle is that the different institutions in the two countries perform much the same functions. In many ways the different institutions are *functionally equivalent* as regards the outcome they produce.

An example is the way the two different sets of institutions deal with the problem of differences in preference intensity. Imagine an issue where a majority with low preference intensity votes down a minority with high preference intensity, so that the result is an aggregate welfare loss of the majority. Thus under certain circumstances majority decisions may be inefficient (in the economic sense).

The Danish version of corporatism is to give privileged access to the political decision making process for organized interests in policy areas that are salient to

⁷ A special part of the literature looks at microstates. They normally do significantly better than their neighbors as they specialize in safe haven activities; see Paldam (2013).

them. This can be seen as an institutional recipe for dealing with the problem of differences in preference intensity.

The Swiss institutions of federalism and of direct democracy can perform the same function. If preference intensity varies over groups that are spatially separated, the institution of federalism can insure that differences in preference intensity are taken into account in the decision making process. The institutions of direct democracy can achieve the same thing by endowing groups with a credible threat of demanding a plebiscite if their (strong) preferences on a certain matter are not taken into account.

From that perspective, (Danish) corporatism and (Swiss) federalism and direct democracy perform the same function – to integrate differences in preference intensity into the democratic decision making process.

1.6 The Perspective of This Book

Our analysis of Switzerland and Denmark as “good societies” does not proceed from the expectation that there is one common institutional recipe for creating income and happiness that both countries have discovered and successfully followed in the past, and hence it cannot be our ambition to find and describe this recipe. Rather it is our ambition to argue that Switzerland and Denmark have in fact developed and followed different institutional recipes that both turned out to be successful in terms of bringing about high levels of average income and happiness. In short we are going to describe and analyze two different institutional pathways to the “good society”.

This does not imply that we think institutions do not matter for outcomes. Most likely neither Switzerland nor Denmark would have become rich and happy with the institutional setup of, say, North Korea. We are, however, keenly aware of the point stated forcefully by Rodrik (2007: 15): “There is no unique correspondence between the *functions* that good institutions perform and the *form* that such institutions take” (emphasis in the original).⁸ Thus, our analyses corroborate Rodrik’s point: Institutions count, but they need not be decisive.

In keeping with our reasoning above, we do not pretend that our analysis of Switzerland and Denmark provides a recipe for achieving high levels of income and happiness ready for use by those countries that have not quite made it there yet. We do not think that this is possible for two reasons. In the first place, as argued already, we do not believe there is a one-to-one correspondence between a particular institutional set-up and its outcomes. In the second place, even if there were, institutions are

⁸The idea that different institutions can fulfill the same function(s) is, of course, not novel in economics. Just consider two famous contributions: Coase (1960) and Ostrom (1990).

time-, country- and culture-specific. They are the product of particular choices made at particular points in time under particular circumstances.⁹ That means that one country's institutional set-up cannot simply be grafted onto another country. Thus, we do not concur with the prophecy offered by the Swiss writer Friedrich Dürrenmatt (which in any case most likely should be read as ironic at some level, cf. Barkhoff (2010: 200–202)): “Die Welt wird entweder untergehen oder verschweizern” (The world will either perish or become Swiss-like). Nor do we believe that the Danish system is a promising export article. When it comes to how to achieve income and happiness – the good society by our definition – our analyses have convinced us that one has to be very circumspect when proclaiming that “big lessons” can be learned from the two countries under scrutiny here.

What can be gained from a comparative study of Switzerland and Denmark is a healthy skepticism towards some cheap generalizations and truisms in political economy and the politics of the welfare state. Yes, it is possible to have a society with a huge public sector, imposing what some would consider an excessive tax pressure on its members, and still have high levels of wealth and happiness. Yes, it is possible to have a rich and happy society with a relatively minor public sector and low taxes, relying more heavily on private but state regulated and subsidized services as well as on the family (women) for welfare production, without having the old, the sick or the disabled dying in the streets. And no, it is not necessarily true that the growth performance of a country with a huge public sector and high taxes is worse than the growth performance of a country with a lean public sector and low taxes! What these and other examples tell us is that the palette of choices of how to achieve a good society is considerably broader than is often envisaged. That is the basic message in this book, and we consider it an optimistic one.

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⁹For a broad introduction to the institutional development of the Danish model see for instance Campbell et al. (2006).

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Part I
The Quality of Life in Two Different Good
Societies: Denmark and Switzerland

Chapter 2

Two Wealthy Economies and Their Development

As mentioned in the introduction both Denmark and Switzerland have managed to stay wealthier than most countries in Western Europe,¹ but the process of convergence in the West has reduced the gap. The West has experienced a strong economic integration in the twentieth century – notably in the second half. This process has led to convergence within the West – and as more countries have joined the process, it has become a true globalization.

The present chapter has four sections: Section 2.1 looks at the thorny problem of comparing the GDP per capita of Switzerland and Denmark. Section 2.2 concentrates on the convergence of the GDPs per capita within the West, notably Western Europe. Section 2.3 considers the perspective of globalization. Section 2.4 deals with the nominal and real exchange rates of the two countries.

2.1 Comparing GDP per Capita

The countries included and the data used in this section are listed in the [Appendix](#). The GDP-data are in constant prices, reached by dividing by a price index. We prefer a PPP-index made to make countries as comparable as possible – this is done in the Maddison-data set, see [Appendix](#). However, the index uses PPP weights for 1995.

A price index measures the average price increases from period 0 to period 1. It uses the quantities consumed in either period 0 (Laspeyre's index) or period 1 (Paasche's index) as weights – in principle both formulas are equally 'right'. The difference between the two calculations is the index problem. It is due to the reaction of people to the change in the relative prices from period 0 to 1. Normally

¹ During the last two decades the only European countries that are consistently richer than the two countries are Luxembourg and some micro-countries such as Liechtenstein, the Channel Islands and Monaco. However, Norway became richer in the last decade.

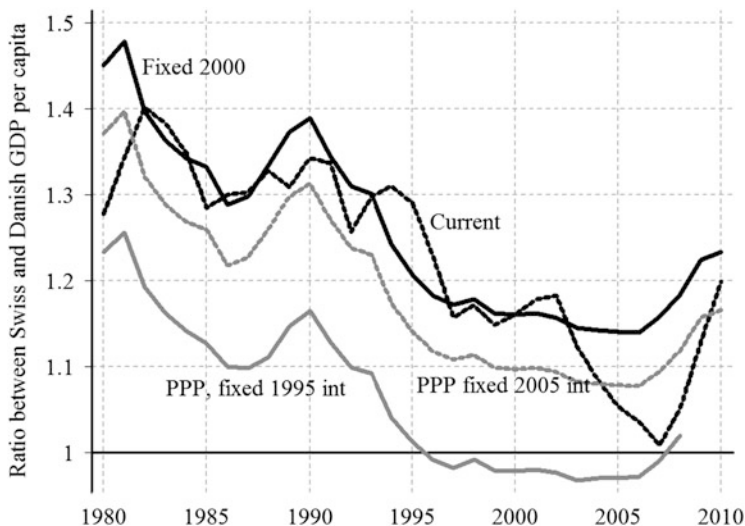


Fig. 2.1 Four series comparing Swiss and Danish GDP per capita (Note: The four series are: (1) is in fixed 2000 US\$, source WDI, (2) current US\$, source WDI, (3) PPP, fixed 2005 international US \$, source WDI. (4) PPP, fixed 1995 US\$, source Maddison (2003))

the shifts in relative prices are small and barely noted by people, so the index problem is small. However, for visible systematic movements, such as the ones caused by exchange rate movements, the index problem becomes substantial.

Figure 2.1 shows four comparisons. WDI (the World Bank databank) gives few Swiss data before 1980, so the comparison is restricted to the period from 1980 to 2010. The comparison based on current US\$ and the index with the oldest weight (1995-weights) should differ most. The two middle indices are have newer weights. The four curves show three main features: (1) They have a range of about 18 %. This reflects the size of the index problem. (2) The three curves in fixed prices have almost the same path – just shifted by a fairly constant factor. (3) All four curves have a clear downward trend, so that over the 30 years the difference in GDP between the two countries falls by about 30 percentage points.

The trend in the Swiss income relative to the Danish (and the West in general) is similar for all indices. It is due to the *downward* convergence of Switzerland as shown in the next section – notably Figure 2.2. From being about 35 % (± 10 %) richer than Denmark only 30 years ago, the difference is now only 10 % (± 10 %). The difference bottomed out at about 7 % (± 10 %) about 7 years ago, but the financial crisis after 2008 has once again increased the difference.

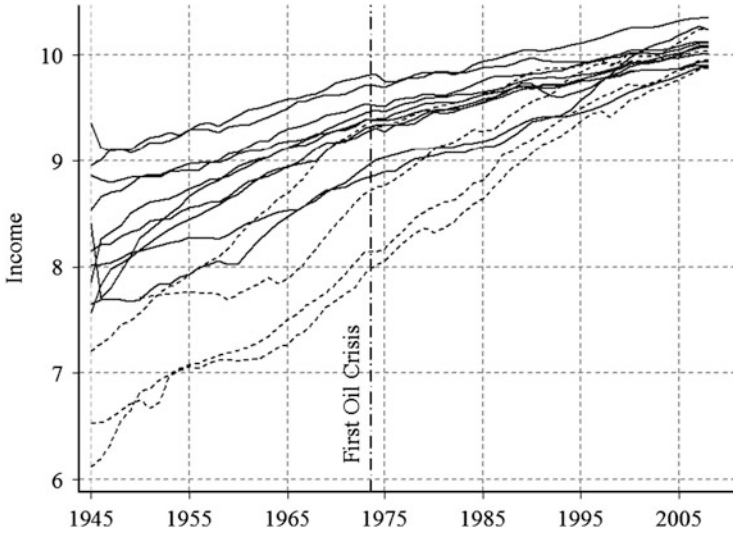


Fig. 2.2 The convergence of the OECD countries (Note: The 13 countries are chosen to be reasonably well spread out at the start. If all OECD-countries were included, the same pattern would appear, but it would be cluttered at the upper half. The countries with dashed lines are East Asiatic, see Table 2.3 of the Appendix)

2.2 The Convergence Within the Developed World

The main pattern is a *convergence upward*, where countries that are behind ‘catch up’. The following discussion refers to standard textbooks such as Jones (2002) and Barro and Sala-i-Martin (2004).

2.2.1 A First Look

The convergence among the developed countries is shown in Fig. 2.2. The horizontal axis is in years. The vertical axis is income defined as the natural logarithm to GDP per capita.

The figure shows that the countries differed by 3 lp (logarithmic points) at the start. This is no less than 20 times. If the East Asian countries are disregarded, the difference is about $1\frac{1}{2}$ lp, which is only $4\frac{1}{2}$ times. At the end the difference has fallen to less than $\frac{1}{2}$ lp, which is about $1\frac{1}{2}$ times, whether or not the East Asiatic countries are included. The fall in inequality within this country-group is thus substantial. Note that the speed of convergence slowed down a little after the first oil crisis in 1973, at least among the countries of the West.

2.2.2 *Sigma Convergence in the West*

The standard way to analyze convergence is to calculate the sigma-measure, where, as before, income is $y_{it} = \ln gdp_{it}$ and gdp is GDP per capita:

$$\sigma_G(t) = STD_{i \in G}(y_{it}), \text{ where } STD_{i \in G}(y_{it}) \approx STD_{i \in G}(gdp_{it})/AVR_{i \in G}(gdp_{it}) \quad (1)$$

The STD is the standard deviation and AVR is the average. G is a country group – at present it consists of the 20 countries of the West. The measure gives the cross-country income distribution so that the distribution becomes more skew when the measure rises. The long-run pattern thus shows a strong trend towards a more equal cross-country wealth distribution, precisely as convergence implies.²

Figure 2.3 shows the path of σ from 1921 to 2008 for the West. It shows the same pattern as Fig. 2.2, and it goes back to 1920. Therefore, a few additional observations can be made: The long-run trend was clearly interrupted by World War II. It made some countries – notably Germany and its allies – much poorer. But then the ‘Wirtschaftswunder’ caused Germany and its prewar allies to return to their long-run income path. The figure also shows that the Oil Crisis of 1973 caused the fast convergence to return to its long-run path.

The convergence will also be disturbed by the crisis of 2009–2011 as some of the countries that have been hit hardest are among the poorest in the group.

Economic theory considers long-run economic growth to be due to real factors – notably technology. The main theoretical insight of convergence rests on three conditions:

- (a) *Globalization*. The more countries are connected by trade, factor and information flows, the more similar will the economies become.
- (b) *Catch-up growth* where countries that produce at a low level of technology learn the technology of those ahead. It may be difficult if the technology gap is large, but at a certain moderate gap-level catch-up can be fast, as shown on Fig. 2.2.
- (c) *Steady state growth* at the ‘modern level’. It depends upon the development of new technologies at the margin. It is thus an international phenomenon.

The ‘modern level’ is determined by the international technological level and the state of the art techniques as regards management and economic policies. Obviously no country is doing everything right, so there is always some margin of inefficiency. Some inefficiencies are due to political constraints and some are due to business monopolies and lack of innovation. The ‘modern level’ is a zone where all countries are rich, but some differences remain. The poorest country is still 50 % below the richest.

²The 50 states of the USA have converged rather much, but there are still differences between the states, and with the σ -measure used below it appears that the smallest value that can be reached is above 0.1, and the countries of the West are surely more different than the US states.

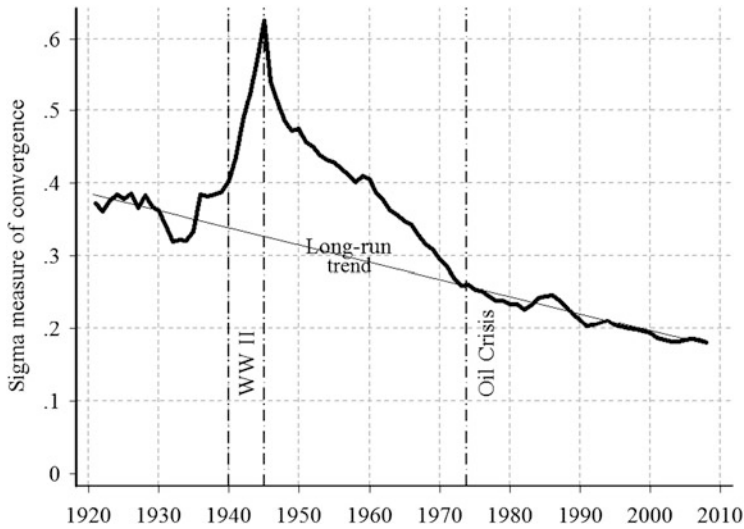


Fig. 2.3 Sigma convergence for the 20 countries of the West since 1920

- (d) *Differences remaining*. The more institutions and policies differ and the more protected the economies are, the more different can they remain.
- (e) *Flexible and 'clever' policies*. The main condition for staying ahead of the other countries once you are at the modern level is fast adjustment to new technologies and changes in the world economy.
- (f) *Transfers* between countries, such as the ones to safe havens and to foreign debt and resource rents obtained from export, may shift income between countries.

Conditions (a)–(c) describe a process of convergence towards the zone that constitutes the modern level, much as seen in Figs. 2.2 and 2.3. Both Denmark and Switzerland are at the modern level and have institutions that differ considerable from the rest – and from each other. Both have also managed to do relatively well, though they have converged considerably towards the average.

The 50 states of the USA form a strong convergence area, where goods and factors are free to flow, and policies and institutions are almost the same. Still the σ -measure of convergence is not zero, but it seems to have stabilized a little below 0.1.

The countries of the West (where the USA is one country) have many regulations and historical barriers to trade and factor flows, and institutions and policies are likewise different in many ways. International organizations such as the EU and the WTO have been rather successful in curbing obvious barriers to trade, but there are many more subtle trade hindrances at play.

Thus, it appears the West will not converge as much as the US states, and the process shown at Fig. 2.3 may stop well before 0.1. However, the curve in the figure does not show a clear leveling off. While the convergence is rather strong at the top where the world technology frontier is the joint attractor, there is no other attractor

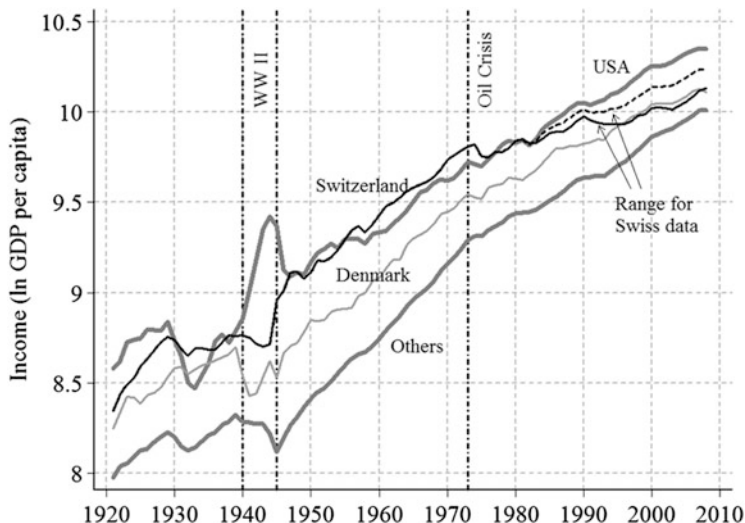


Fig. 2.4 The position of Denmark and Switzerland in the convergence pattern in the West (Note: Data from Maddison (2003). The lowest of the two Swiss curves is the Maddison estimate. The highest (*dotted*) curve is probably exaggerated. Others are the remaining 16 countries of the West in Table 2.3)

in the world today. And indeed, when modern economic growth starts in an area, it will typically lead to divergence in the first few decades. This, e.g., is the case for the African countries, the Chinese provinces and the Indian states. They all experience rather strong divergence.

2.2.3 Denmark and Switzerland in the Pattern

Figure 2.4 shows the development of the USA, Denmark, Switzerland and the *other* western countries. The strong convergence before the Oil crisis is shown as a reduction in the gap between others and the USA. It is also clearly visible that the convergence has been slower after the Oil crisis.

From the difference observed we conclude that the other western countries still have a substantial productivity gap to the USA, which in average amounts to about 40 %. This suggests the size of the potential efficiency gap that can be reduced by further integration.

The second point to note is the position of the countries of interest: Denmark is close to the middle of the interval between the USA and others throughout. Switzerland has a much more interesting path: It did experience problems during the Second World War. However, as soon as the war was over Switzerland had a prolonged boom lasting until about 1980, during which the country was richer than the USA most of the time, but since then it has gone to the middle of the interval as

well. This implies that Switzerland has had relatively low growth in the period. This is normally ascribed to low productivity increases.

2.2.4 *The Relative Development Path*

The development shown in Fig. 2.4 is shown relatively on Fig. 2.5a, b. The figures indicate that Denmark did rather well during the big crisis in the 1930s, but has otherwise followed the general western development. Switzerland has had a radically different path. From the First World War and only interrupted by the Second World War, Switzerland has been extraordinarily successful in producing a high standard of living. From 1947 to the Oil crisis in 1973, Switzerland was on average about 40 % wealthier than the rest of the West.

When the two countries are compared with Western Europe in Fig. 2.5a the Swiss exceptionalism is even more striking. Switzerland was 2.4 times richer than other Western European countries just after the Second World War, but the excess standard of living has declined ever since.

Figure 2.5a shows that Switzerland gained great advantages at the end of the War in 1944 and till 1949 by being a safe and well organized island surrounded by countries in chaos: Germany-Austria and Italy lost the war, and France was torn between losers and winners. It was only after 1950 that Europe gradually ‘normalized’. This history certainly gave the Swiss safe haven policies a jump start.

Switzerland differs from the other safe havens in two ways.³ In the first place it is much larger and consequently a large part of the economy is ‘normal’. Secondly, in most of the period since World War II, it has operated a floating exchange rate that has steadily revalued. This implies that some of the funds floating into Switzerland have remained in the country, giving a combination of a low interest rate and a steadily revaluing real exchange rate. It has also given an unusual housing market. So the Swiss economy is highly unusual in a number of ways.

Table 2.1 compares the trends in GDP (calculated as explained in the note to the table) and deviations trend the average for the countries of the West. Table 2.1 shows that five countries have the same long-run growth rate as the average one: They are Germany, France, Denmark, Canada, and Switzerland.

However, countries may have periods where they *deviate* from the long-run growth rate. Switzerland certainly did by having a truly enormous jump in incomes in 1944–47 and a slow return to the trend since then. This is a very unusual path of income. In fact, the Swiss development deviates more from the trend than that of any other western country.

³The OECD and IMF have had committees to study offshore banking centers. In Europe 11 countries are classified by both committees as financial safe havens. The other 10 countries are all micro-states see Paldam (2013).