

THE NORDIC RECIPE FOR GLOBAL SUCCESS

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The Nordic recipe for global success



July 2005

Preface

The international business environment is rapidly changing. Therefore, companies must make sure that they are at all times able to meet the increasing international competition. Also, they must exploit new market opportunities in order to survive in the global market.

The Nordic economies will gain more from the globalisation than larger economies. As small countries we are affected more heavily by international competition than large countries. Small countries also depend more on foreign investments and on export, and therefore international trade is of vital importance to survive in the global market.

International division of labour has increased tremendously over the past years. Distance has become less important because of the technological development, easier access to transportation, and improved ways of communication.

The opening of Eastern and Central Europe, China, and India brings about new opportunities, but also increased competition. The low labour costs and the striking growth rates of these countries are a concrete threat. The Nordic Countries will by no law of nature keep their leading positions in the future.

The challenge for Nordic companies is to ensure and maintain their excellence in a global perspective. They must be leading in all fields. The manufacturing sector is becoming increasingly capital intensive, and there is an obvious need to improve the opportunities for growth for the labour intensive service sector. Therefore, it is vital to improve the incentives for both sectors to operate in our part of the world.

The Nordic countries must continue to strengthen their position in the global market. This will give them a chance to prosper from the opportunities offered by globalisation—and this way they will generate growth and prosperity.

This publication gives an overview of the major challenges for the Nordic countries and presents a common recipe for global success.

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Executive Summary

Globalisation presents a number of opportunities and challenges for Nordic countries. Easy access to information, fast and cheap transportation, technological development and easy communication widen the companies' liberty of action tremendously. However, Nordic companies now have to compete directly with companies from distant corners of the world.

Until now Nordic countries have managed to meet this challenge and take advantage of the global opportunities. The relatively small and open Nordic economies play an increasing role in the international division of labour. However, to keep their leading positions in the global arena, Nordic countries must continuously evaluate and adjust policies in order to create the best possible conditions for companies and citizens—and hereby create the best basis for growth and prosperity.

CHANGE IN PRODUCTION PATTERNS

Today, many companies find it attractive, and often necessary to locate labour-intensive and standardised production in countries where labour costs are below Nordic levels.

Improvements in international transport and logistics have played a major role in enabling companies to locate all or parts of production around the world, while advances within communications technol-

ogy enable companies to keep control of production.

The gains from outsourcing are largely connected with the rate of reemployment for employees whose jobs are moved, which is to a large extent affected by the degree of mobility and flexibility of the labour market. Calculations show that Denmark, like the US, gains positive returns from outsourcing whilst Sweden does not. The positive Danish returns from outsourcing can mainly be explained by Denmark's flexible labour market and a large reemployment rate. Nevertheless, US gains bigger net returns from outsourcing than Denmark and Germany loses more than Sweden. This underlines the need for flexibility in the Nordic labour markets.

NORDIC COUNTRIES CANNOT COMPETE ON WAGES

Increased global competition increases the need for Nordic companies to have good conditions in order to sustain economic growth and prosperity. With the emergence of a great number of new open market economies with lower labour costs it is obvious that Nordic companies cannot compete on wages alone. They must be leading in investing in highly productive equipment, in research and innovation and in developing a highly educated workforce. However, this does not mean that annual

wage increases are not significant to competitiveness. Competitiveness is always a fragile balance between costs and quality and product capability. In the future, the Nordic countries must be more committed to efficient and knowledge-intensive production higher up the value chain.

EDUCATION AND ADAPTABILITY

A well-educated workforce is a prerequisite for Nordic companies to maintain their competitiveness in the future through increased commitment to research and development and highly productive, knowledge-intensive production higher up the value chain. The Nordic workforce needs to be among the world's most productive and best educated. Furthermore, education is the most important pillar in a strategy for ensuring jobs for people with weak qualifications.

FLEXIBLE LABOUR MARKETS

The Nordic countries need to be among the world's leading regions as regards the adaptability of the labour markets. This requires flexible labour markets with flexible hiring and termination conditions, strong incentives to work and to educate oneself, and attractive personal and business tax conditions.

Moving some jobs out of the country does not solve the problem of the shortage of qualified labour. In the future there will be fewer young people to support more and more old people. Unless we manage to increase employment or productivity it will lead to a decline in growth and prosperity. This requires a two-pronged strategy: on the one hand, attractive framework

terms must be created for investment in highly productive Nordic jobs. On the other hand, the available workforce must have the range and composition to fill the jobs in a flexible way.

NORDIC COUNTRIES NEED TO ALTER THEIR TAX SYSTEMS

However, the strategy to make Nordic countries the home of knowledge-intensive and highly productive development and production is being hindered by high income taxes. Nordic countries have some of the world's highest tax burdens and this limits incentives to work, particularly as regards mobile, well-educated and well-paid employees. This makes it more attractive for companies to locate knowledge-intensive activities such as research and development in countries where income taxes, and consequently company labour costs, are lower. If the strategy of commitment to highly qualified labour and highly productive jobs is to succeed, it is crucial to alter the tax system to make it more attractive for highly qualified staff to work and live in these countries.

Finally, there should be a larger income difference between work and social security. The system of taxes and transfer incomes must be aligned so as not to hinder individual work incentives.

MORE RESEARCH AND DEVELOPMENT

It is of high importance that companies have access to public research centres which underpin the long-term accumulation of knowledge. Therefore, Nordic countries must build up research centres with enough critical mass to match the

USA and the Far East, and with strong public-private partnership.

It is crucial for all Nordic countries to ensure sufficient motivation for private investment in research and development. The Nordic countries would benefit by increasing incentives and opportunities for an increased private effort in the research and development area.

Nordic countries must be leading in understanding customers' needs in order to create high value for consumers. A combination of research-driven and user-driven technological innovation creates the most efficient research, by creating added value for the customer. These two kinds of innovation should not be viewed as "either-or" activities. Both types of research should prevail. Besides, the exchange of knowledge between knowledge institutions and companies should be enhanced.

STRENGTHENED FINANCIAL INFRASTRUCTURE

The capital markets of the Nordic countries and Europe have still not been fully liberalized and the capital markets of the individual countries are still not fully integrated. There are still differences in legislation, administrative regulations, tax and accounting rules and consumer protection regulations standing in the way of full integration. According to the OECD, there is a continued need for reforms throughout Europe in order to achieve a fully integrated European financial market as efficient as the American.

DECOUPLING PUBLIC SPENDING FROM PRIVATE SPENDING

Growth leads to increased prosperity and opportunities for more welfare, but the Nordic countries have designed the welfare systems such that public spending both on transfer incomes and public services grows at the same rate as growth in incomes, and thus will continue to exceed public revenues by the lack of reforms. Growth should be the solution to our economic balance problems but this mechanism is hindered by a welfare system fault. Public spending should be decoupled from private sector growth, and there ought to be a greater role for the private sector in producing welfare services even if the services are tax financed.

The task is to create attractive growth conditions for companies in a global economy where knowledge is the most important raw material and where highly productive investments are an essential catalyst.

The creation of prosperity by the business sector is the base upon which society can finance the welfare distributed by the public sector.

PROMOTE NEW MARKET OPPORTUNITIES

As new countries become increasingly important growth markets, it becomes ever more important for Nordic companies also to enter these markets, not just to sell their goods but increasingly also to insource or outsource, produce, acquire knowledge and to research and develop locally.

It is crucial to the success of Nordic companies in a climate of cut-throat competition that they can rely on the support

of a set of efficient international business instruments to support their participation in the global markets.

Furthermore, it is important that organisations such as the WTO and the EU continue to provide free market access to companies and a free and secure framework for investment and other business activities in markets around the world. And a strong and decisive EU must fight for and safeguard common interests of the European business community throughout the world.

HOW TO MEET THE GLOBAL CHALLENGE

Global development is rapid and our competitors are eager to establish themselves in a good position. Consequently, we urgently need to reform a number of structural growth conditions for company growth and value creation if Nordic countries are to stay competitive and become global winners. The Nordic economies must be geared to support high productivity, adequate num-

bers of competent employees and successful participation in the international division of labour in all its facets. This is the foundation of growth and prosperity in global competition. As stated by the former chief economic advisor of President Clinton, Dr. Martin Neil Baily: "The recipe for long-term growth is simple: increase the number of people in the workforce and create conditions that make them more productive".

Nordic countries have so far been relatively good at using the opportunities offered by globalisation. However, as the international division of labour increases rapidly—Nordic countries are lagging behind in adapting to flexible, global knowledge-based economies compared to a number of other developed countries.

If globalisation is met with the right attitude and if conditions for running business are optimised to the new international market situation—then Nordic companies can make use of the new opportunities offered by globalisation and become global winners.

The Nordic recipe for global success

The Confederation of Danish Industries, The Confederation of Finnish Industries, The Confederation of Swedish Enterprise, The Confederation of Norwegian Business and Industries and The Confederation

of Icelandic Employers strongly urge the following actions in order to give Nordic companies and hence Nordic countries the best foundation for becoming winners in the global knowledge based economy.

The Nordic recipe for global success

Growth, development and prosperity in the Nordic countries depend on offering good conditions for doing business

- Create/maintain flexible labour markets to ensure smooth and efficient job turnover.
- Create strong incentives for work and education.
- This requires attractive personal and business tax conditions. Nordic countries have some of the world's highest tax burdens. This limits incentives to work, particularly as regards mobile, well-educated and well-paid employees. This makes it more attractive for companies to locate knowledge-intensive activities elsewhere. Therefore, it is crucial to alter the tax system to make it more attractive for highly qualified staff to work and live in these countries. The high marginal taxes, combined with generous transfer systems, are to blame for diminishing the incentive to work.
- Shape a prioritised commitment to research, development and innovation. Enhance the focus on business oriented research and development.
- Keep the rise in labour costs at a sustainably low level. As a result of the historically rapid rise in wage costs, Nordic salaries are among the highest in the world, thereby deteriorating our competitive position compared to our closest rivals.
- Enlarge the gap between the level of transfer incomes and net income from work.
- Improve the climate for investments—in order to improve the conditions for new entrepreneurs and to make the Nordic countries attractive for foreign investments and for investing in new productivity enhancing technology. The Nordic countries should stress capital import neutrality, in particular by abolishing net wealth taxes reducing the capital income tax rate, which would promote investments and the supply of capital.



- Globalisation and technological development imply that new jobs being created require higher qualifications than jobs being phased out. In the future, the Nordic countries must be more committed to efficient and knowledge-intensive production higher up the value chain. This requires a highly educated and productive workforce.
- Globalisation gives access to the world market, but the EU continues to be a key-market for Nordic companies. At the same time, Europe should be used as a bridge to the rest of the world and a strong decisive EU should safeguard the interests of European business in WTO and throughout the world. Europe faces a risk of becoming a minor player in the global economy in decades to come. Therefore, there is a need to unite behind the Lisbon agenda: to make Europe the most dynamic and competitive knowledge-based economy in the world.

Introduction

Within the last few years, Nordic countries have attracted international attention regarding how to create wealth and prosperity.

The Confederation of Danish Industries, The Confederation of Finnish Industries, The Confederation of Swedish Enterprise, The Confederation of Norwegian Business and Industries and The Confederation of Icelandic Employers wish to present some facts and guidelines for how Nordic countries can embrace the opportunities of globalisation in order to stay competitive and keep up the high level of wealth and prosperity.

Firstly, we will take a general glance on the overall conditions with regard to keeping high levels of prosperity and competitiveness in the Nordic countries.

Secondly, we will discuss how the Nordic countries can keep their strong international positions and stay among the richest countries in the world with high levels of wealth.

Thirdly, we will look closer into how Nordic companies can take advantage of the increased international division of labour. Moreover, we analyse the national consequences of globalisation, e.g. how the Nordic workforce adapts to globalisation.

Finally, we will look deeper into which political conditions Nordic companies must have, in order to stay competitive and sustain our economic growth and prosperity. This comprises the Nordic recipe for global success.





Globalisation creates basis for Nordic prosperity

The welfare of the Nordic countries is dependent on globalisation. Nordic goods are today sold everywhere in the world. Nordic exports are important for the prosperity and consumption opportunities of the Nordic people, and export and prosperity depend on high and growing productivity in Nordic companies.

Today, Nordic companies are active players in the global division of labour. As a result, more and more companies are moving their production facilities to countries outside the Nordic countries. The international division of labour is creating new opportunities. Thus, today it is far easier to share knowledge with collaborative partners from all over the world. However, globalisation presents a number of challenges. Now, Nordic companies have to compete directly with companies from distant corners of the world.

Up until now, the Nordic countries have managed to meet these challenges. The Nordic countries are relatively small and open economies, playing a considerable role in the international division of labour. The whole world is our market and it might be said that Europe is our domestic market—not just for exports but also for investment, outsourcing and exchange of labour and knowledge.

However, increased global sales do not benefit Nordic citizens unless business ac-

tivities also take place in the Nordic countries and can be converted to increased exports and employment. Fortunately, there is a tendency for those Nordic companies, which are successful around the world also to be productive and competitive enough to manage well in their domestic markets.

Productivity is crucial to prosperity

Industries with rising productivity experience an increasing demand from abroad. However, domestic demand is increasingly moving towards sectors with low productivity growth, and therefore exports are also important to prevent a decline in overall productivity in the Nordic countries.

The value of produced goods and services is determined by the number of people who work, the number of hours they work, the amount of value created per working hour and how good they are at marketing the result. Thus, our prosperity depends on our ability to produce and sell, which is why boosting productivity is so important.

Productivity growth is mainly related to technological progress, liberalisation, privatisation and outsourcing.

Competitive exports through innovation and knowledge

In recent years a number of new growth countries—principally in Eastern and

Central Europe and Asia—have taken market shares in the international market. These countries enjoy considerably lower levels of costs than Nordic countries. Thus, if Nordic companies are to remain competitive, it is crucial that our companies are highly productive; otherwise Nordic produced goods will be much too expensive. But the competitiveness of Northern companies is not just a question of how much can be produced at a certain price. Competitiveness has also a quality aspect, not only with regard to the product durability but also with regard to enhanced product capabilities. The high cost level in the Nordic countries makes it necessary for companies to be committed to high quality products capable of achieving high prices in the world market compared to those of the competitors.

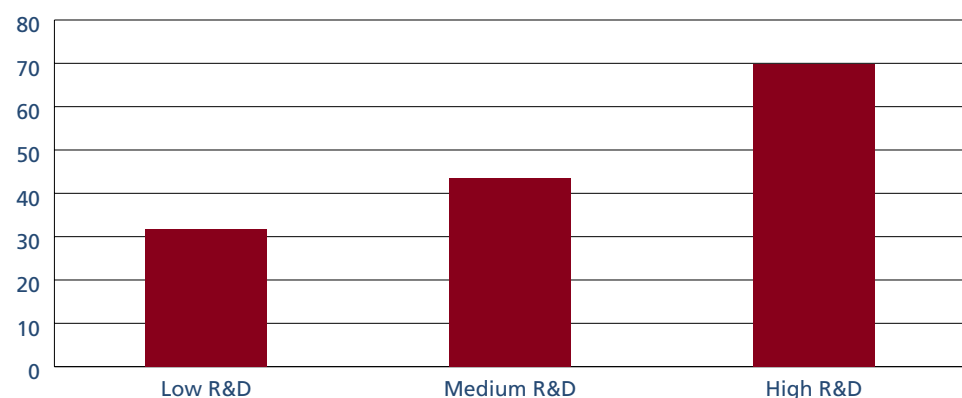
To do this, we must integrate more knowledge into our products through high

quality, a commitment to design, branding, service, customisation and constant innovation and renewal of products in order to satisfy customers' needs best possible. Products which can be sold at high prices are referred to as upmarket products¹. They are aimed at customers who are willing to pay a higher price for a quality product or a product with extra features and capabilities rather than purchasing a lower quality rival product. Innovation and new knowledge are decisive factors in developing upmarket products. It is therefore necessary to invest in R&D of products and their applications and to have employees with the right expertise.

The ability of companies to develop upmarket products depends also on competences and skills of employees. Industries, where a large number of employees have a high education, also tend to have a high proportion of upmarket products.

R&D BOOSTS UPMARKET SHARE

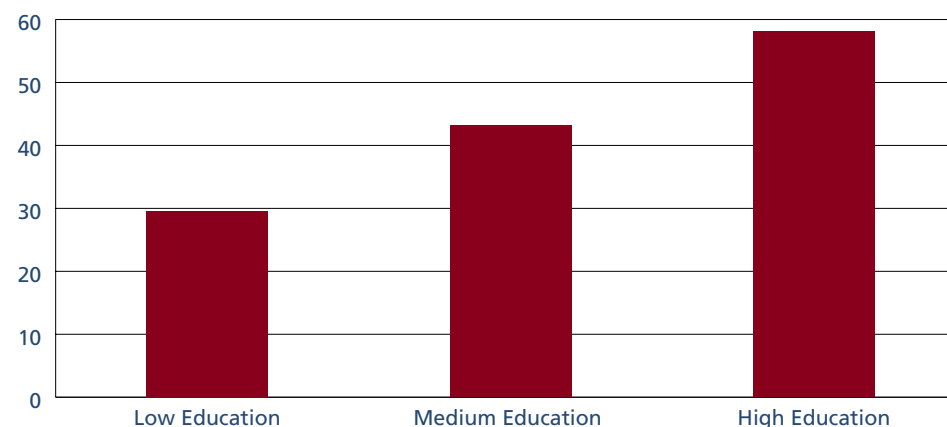
Upmarket share for industries classified according to research level²
Per cent



Source: Eurostat (Comtext) and DI estimates

EDUCATION INCREASES UPMARKET SHARE

Upmarket share for industries according to educational level²
Per cent



Source: Eurostat (Comtext) and DI estimates

A glance at the Nordic countries' upmarket share of export to EU15 imply some differences in the Nordic countries' export patterns with regard to upmarket share in exports. Around 40 per cent of the Danish, Finnish and Swedish export consists of upmarket products whilst the share for Iceland and Norway is much smaller.

When excluding oil, fuels and energy export, the picture, especially for Norway, is somewhat different. This more than doubles the Norwegian upmarket export share.

However, commitment to upmarket products is not the only opportunity available to Nordic companies to thrive. Nordic

UPMARKET SHARE OF EXPORT TO EU15

Per cent

	1999	2000	2001	2002	2003	(1999-2003)	M.euro, 2003
Denmark	41.0	45.0	43.9	43.8	46.9	44.1	30,934
Iceland	13.8	14.0	14.0	22.2	23.7	17.6	1,649
Norway	18.8	18.0	14.2	13.3	14.1	15.7	39,081
Sweden	49.0	42.1	50.7	42.3	48.1	46.5	46,674
Finland	42.2	30.4	30.4	40.8	39.8	36.7	22,993

Source: DI

UPMARKET SHARE OF EXPORT TO EU15

Export excl. oil, fuels and energi (per cent)

	1999	2000	2001	2002	2003	(1999-2003)	M.euro, 2003
Denmark	42.9	49.9	47.4	48.2	50.9	47.9	27,937
Iceland	13.8	14.0	14.0	22.2	23.8	17.6	1,646
Norway	34.8	30.9	33.2	32.7	36.0	33.5	15,206
Sweden	50.0	43.6	52.0	43.6	49.1	47.7	45,165
Finland	42.8	31.5	31.5	42.1	41.8	37.9	21,801

Source: DI

downmarket and middle-market products can also be exported and be profitable, but only provided there is a competitive relation between price and quality. This requires constant focus on reducing costs and maintaining competitive prices, e.g. by investing in automation production processes, or by outsourcing parts of the production process.

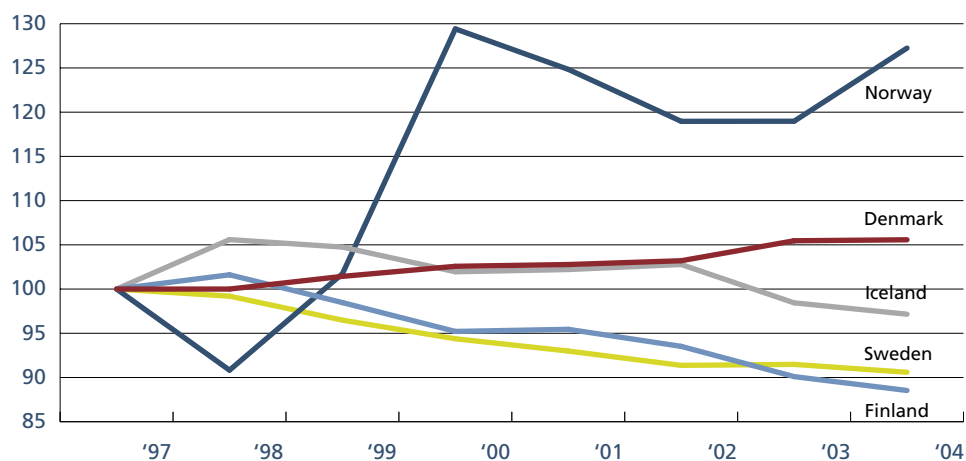
China is low in the quality hierarchy with an upmarket share of export of only 14 per cent. The rapid growth in China's exports is primarily explained by the country's low wage costs.

Development in terms of trade

As mentioned earlier, our prosperity depends on our ability to produce and sell. If

TERMS OF TRADE

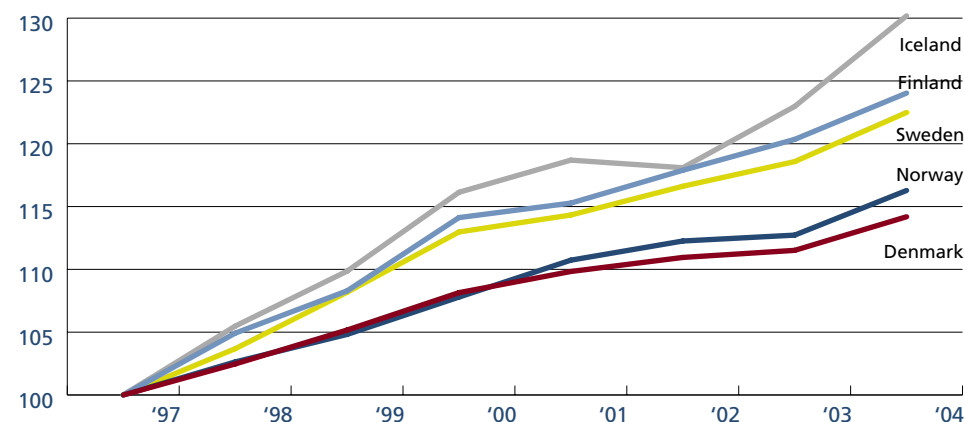
Index 1997 = 100



Source: Ecwin

GROSS DOMESTIC PRODUCT, VOLUME

Index 1997 = 100



Source: Ecwin

we manage to produce a high degree of upmarket products, we ought to be able to sell our products at ever increasing prices without risking to lose market shares. An important aspect of a country's economic development is the development of its terms of trade, i.e. the ratio of export prices over import prices. A fall in the terms of trade illustrates a slower development of the export prices in relation to the import prices. During the past decade there has been a widely differing development among the Nordic countries in this area.

The sharp fall in the Swedish and Finnish terms of trade since the late 1990's can to some extent be explained by the two countries' intense share of highly technological production, in particular telecommunication but also transport equipment and chemicals, where there is a serious price pressure on the global market. The increase in the Norwegian terms of trade can, at least partly, be explained by the

positive development of energy prices as well as process of raw materials and intermediate goods, which are important in the Norwegian business structure.

Paradoxically, a fall in the terms of trade tends to be combined with an increase in GDP growth, measured in volume and at the same time, a more modest development of GDP measured in value. On the other hand, it is important to recall that falling export prices, ceteris paribus, eventually will result in a weaker development of the private sector profit levels. In other words, if a country experiences a fall in the terms of trade, seemingly large production increases will not necessarily result in correspondingly large increases of living standards.

The differing development in terms of trade among the Nordic countries can serve as one explanation to why countries such as Sweden and Iceland since 1997 have not advanced in comparison to the

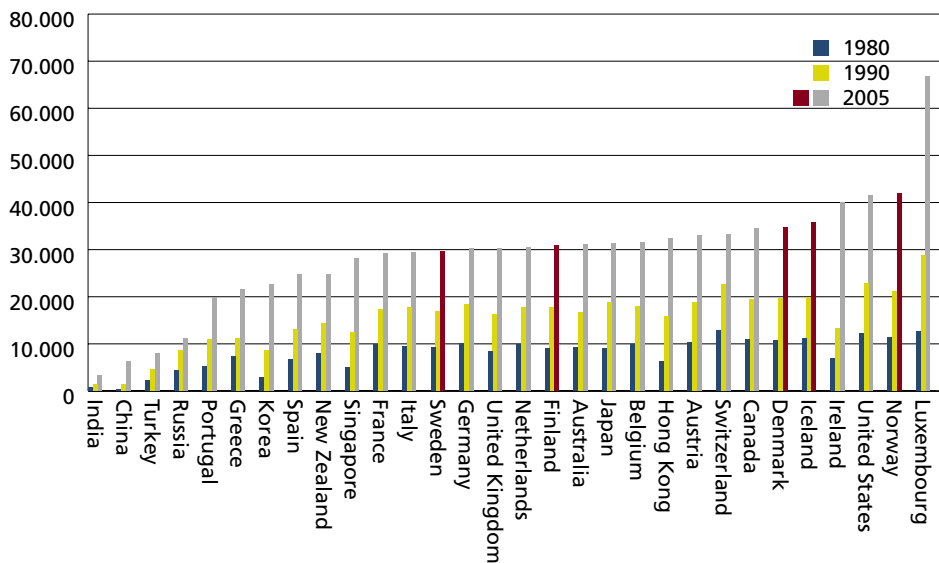
other Nordic countries with regards to GDP per capita, adjusted for purchasing power, despite the two countries' relatively strong GDP growth. It can also explain why countries such as Denmark and Norway have been able to maintain their high positions during the same period.

As a conclusion, it is advisable for economic observers, as well as for govern-

ments, not to put all attention on the volume growth of a national economy without considering the potential effects of the terms of trade. The GDP per capita measurement, with a purchasing power adjustment, is in many cases a more accurate measurement when comparing the wellbeing and development of different countries' national economies.

GDP PER CAPITA

Adjusted for purchasing power (USD)



Source: OECD, main economic indicators and Economic Outlook 2004

International division of labour

Globalisation has given the Nordic business community access to far corners of the world, but Europe continues to be the key-market for Nordic export companies, both as suppliers and as a region for investment and marketing. However, Europe faces a risk of becoming a minor player in the global economy in decades to come, unless we show forethought and strength. Therefore, there is a need to unite behind the common goal of the 2000 Lisbon summit: to make Europe—and the Nordic region—the world's most dynamic and competitive knowledge-based economy by 2010. This requires significant structural reforms.

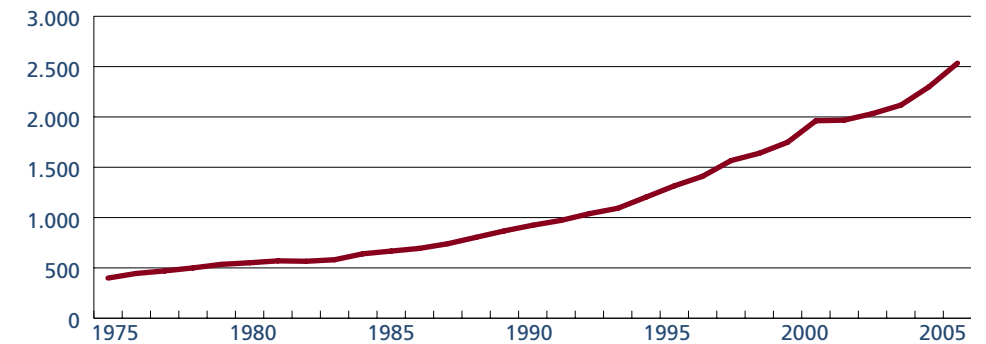
The international division of labour implies that goods and services, capital,

labour and knowledge move increasingly across borders to the benefit of companies and society as a whole. The benefits of globalisation are especially visible within the EU single market³. The European Commission assesses that in its first ten years since internal borders were removed in 1993 the single market has created 2.5 million more jobs and has brought added prosperity to the tune of EUR 877 billion.

Moreover, not only European companies and citizens derive great benefit from the economic gains associated with increased division of labour. The international economy as a whole has become far more open. Progress has largely been driven by market liberalisation and technological progress.

RAPID GROWTH IN INTERNATIONAL TRADE

USD bn (1995 prices)



Source: OECD, main economic indicators and Economic Outlook 2004

International trade is constantly increasing in importance

International trade is becoming ever more important to the world economy. Since 1975, world trade has increased by just over 6 per cent per annum. This is more than twice as high as the growth in global production.

Global markets are becoming increasingly important for the Nordic economies and a growing part of Northern production originates from demand abroad. Most of Nordic foreign trade still involves the rich countries, i.e. the European countries, the US and Japan.

Bringing down trade barriers

More than 90 per cent of the world's economies is today subject to the free trade agreements of WTO. These agreements have resulted in a considerable reduction in international trade tariffs first

through negotiations in GATT and then in the WTO.

At the global level, there is a major need to bring down barriers to international trade. Calculations made for the Copenhagen Consensus Conference 2004 show that the creation of prosperity in the world would be considerably greater if trade barriers and subsidies were reduced. Economists estimate that reducing subsidies and trade barriers by 50 per cent could result in a doubling of annual global GDP growth.

Thus, the WTO has an ever more important role to play, but the EU can also assist Nordic companies in gaining access to new markets. The enlargement in 2004 of the EU with 10 new members, mainly from East and Central Europe, and the future development of the EU towards Eastern Europe will remove barriers and obstacles to trade. Moreover, future EU policies to-

wards neighbouring countries, especially Russia and other former Soviet republics, can contribute to breaking down barriers to trade and investment.

More cross-border investment

Many Nordic companies take active part in globalisation. Subsidiaries of Nordic companies employ a number of people abroad. This does not say whether jobs have been moved from the Nordic countries, but it does show that Nordic companies take an active part in globali-

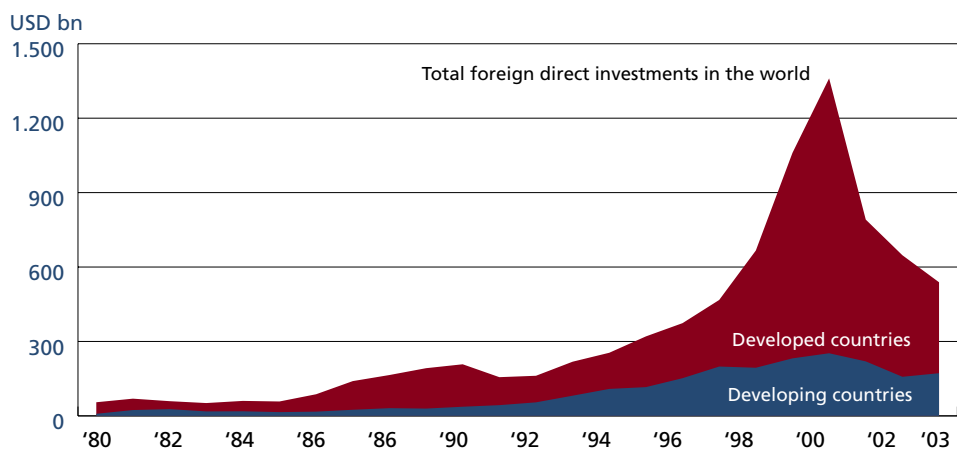
sation and are integrated into the world economy.

The vast majority of the world's direct investments are made in developed countries. In matters of investment, the attraction of the rich countries is largely attributed to sound structural conditions, i.e. stable growth, good infrastructure, good education system, stable political conditions and favourable business (e.g. tax) conditions.

In a world where companies invest increasingly across national boundaries, it

RICH COUNTRIES RECIEVE MOST INVESTMENT

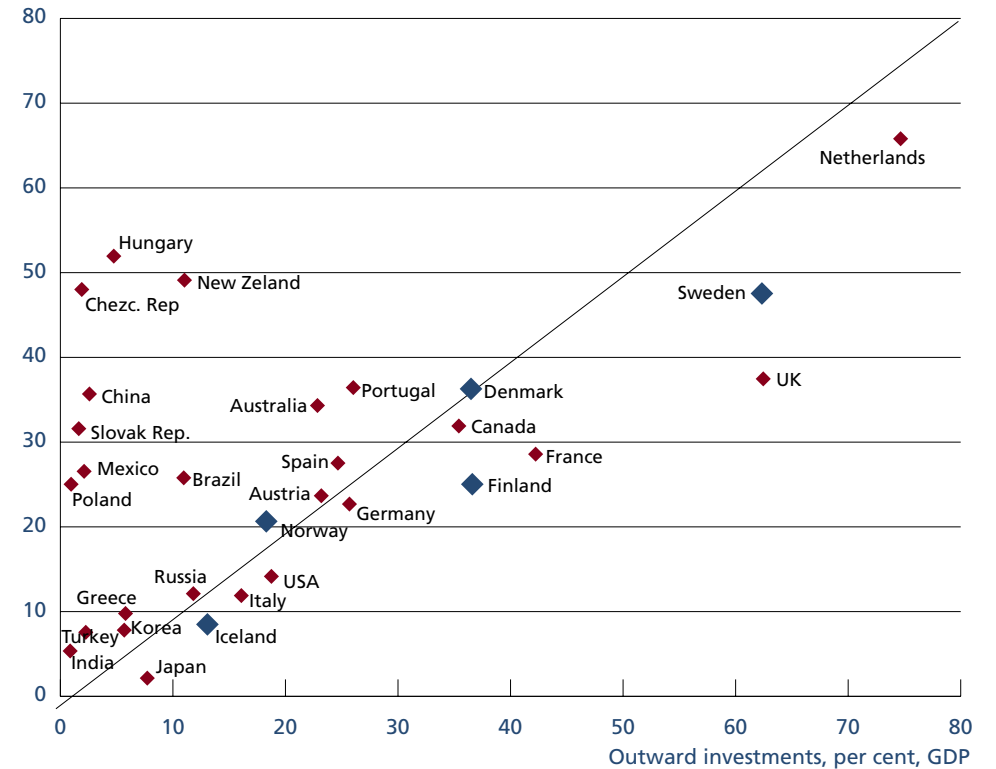
Total foreign direct investment in the world



Source: Unctad

OUTWARD AND INWARD INVESTMENTS

Inward investments (cumulative), per cent, GDP



Source: Unctad, OECD and DI calculations

is crucial to balance inflow and outflow investments. The figures show that foreign companies to a large extent have invested as much in Nordic countries as Nordic companies have invested abroad.

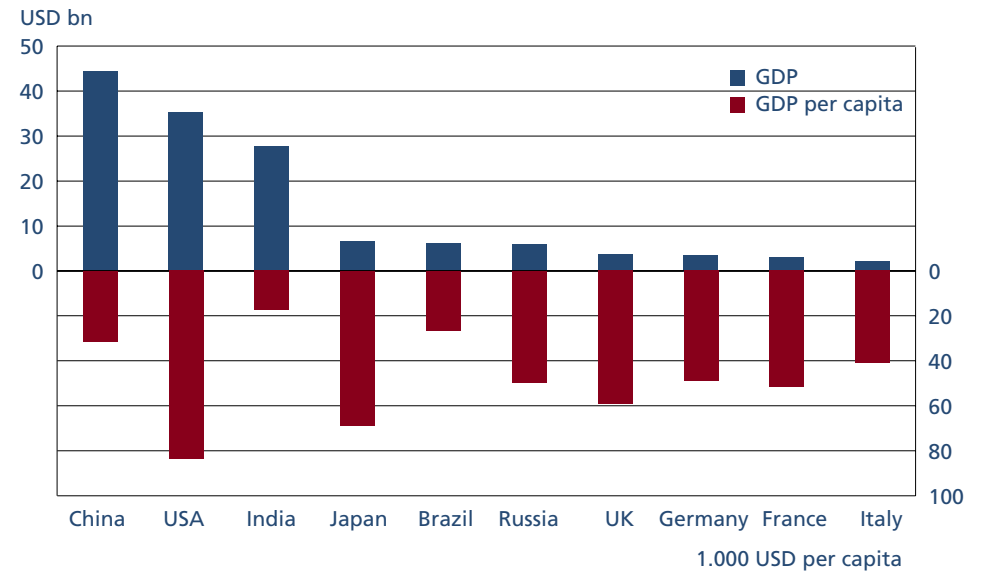
The European and Nordic challenge

The competitiveness and economic growth of Europe are important for Nordic companies, since Europe is still our most important market both in terms of supplies, marketing and investment. Following the expansion of the EU, opportunities for export, outsourcing and investment in Central and Eastern Europe have grown

considerably. The new countries offer high growth and low labour costs as well as easy access due to the common EU rules.

However, economic growth rates paint a somewhat gloomy picture of the European situation. With growth of around 2 per cent per annum, Europe is currently not in a position to win the prize as the world's most competitive economy. Countries such as the US, Japan, China and Russia currently enjoy economic growth rates significantly higher than the European countries. In the long term we must accept the fact that countries such as China, India, Russia and Brazil will play a much larger role in the world economy. A projection

THE WORLD'S LARGEST ECONOMIES IN 2050

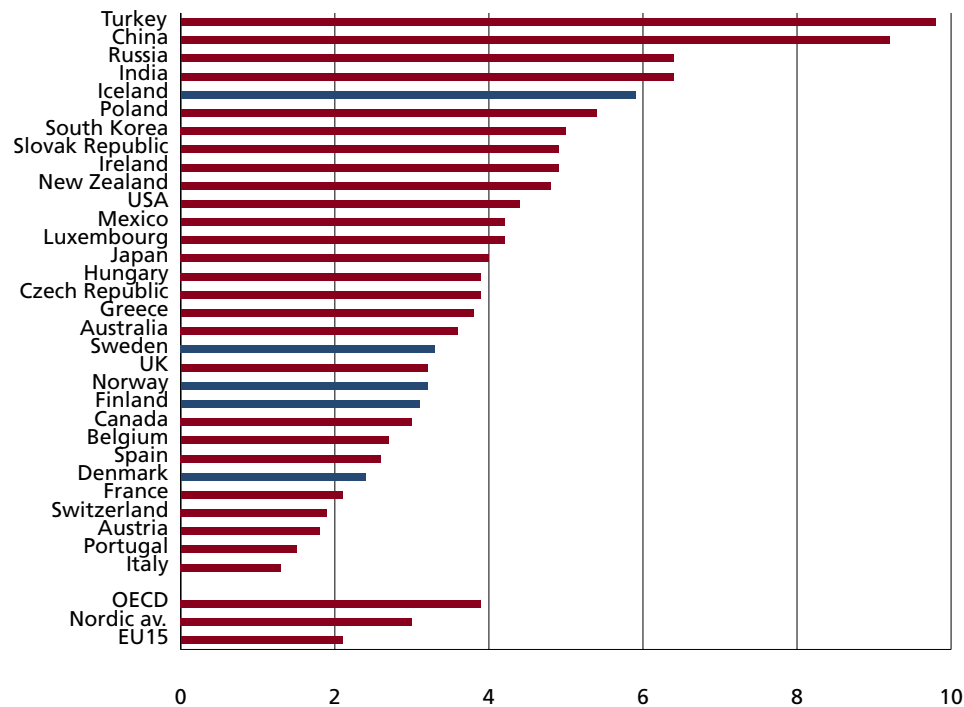


Source: Goldman Sachs, Global Economics Paper no. 99, October 2003

of current development trends made by the American investment bank Goldman Sachs, shows that in less than 40 years these four economies will take up more of the global economy than the G6 countries—the US, Germany, Japan, the UK, Italy and France—do today.

China is in a class of its own. The value of China's production output is expected to exceed the UK and Germany already in 2010, while China is expected to overtake Japan around 2015 and the US by 2040. By that time China, the US and India will dominate the world economy.

REAL GROWTH IN GDP PER CAPITA, 2004



Source: OECD, Economic Outlook no. 76, IMF World Economic Outlook Sep. 2004



New ways of running companies

Many Nordic companies change from being international to global. Company focus is moving from international sales to global optimisation of the value chain. The individual parts of the value chain are located where it is most profitable. Companies take advantage of globalisation through investment, outsourcing and working together with customers, suppliers and knowledge centres anywhere in the world. This is not something companies can merely take or leave. They must take full advantage of the global opportunities. Otherwise, they will not be able

to increase productivity and continue to sharpen their competitive edge.

Nordic companies have always been active in the international markets. Small domestic markets have forced companies to seek international marketing opportunities, which is why Nordic companies today have large export shares compared to companies in many other parts of the world. The large volume of Nordic exports creates basis for Nordic imports.

However, in recent years Nordic countries which have mainly focused on exports up till now, are to an increasing extent set-

GLOBALISATION OF NORDIC COMPANIES

Scope of global activities

Low		High		
<p>1 Sales in new markets</p> <p>Companies export to new markets to expand their customer bases.</p> <p>Production model from home market transferred to export market.</p>	<p>2 Relocation of production</p> <p>Finished goods production relocated to exploit cost differences.</p> <p>Finished goods exported globally.</p>	<p>3 A thinning of the value chain</p> <p>Parts of the value chain relocated to exploit cost differences or obtain access to new skills.</p>	<p>4 Reconstruction of the value chain</p> <p>Relocated functions restructured to exploit new opportunities, e.g. "Around the clock R&D".</p>	<p>5 Creation of new markets</p> <p>Global specialisation provides new products at considerably lower prices and thus gives access to new markets or customer segments.</p>

Source: McKinsey

ting up production facilities abroad where production costs are lower. Moreover, advances in transport and communications technology have enabled Nordic companies to offshore parts of the value chain to other parts of the world, to sharpen their competitive edge or to obtain access to special skills and competences.

Physical borders and distances are becoming less and less important to global production networks. However, the division of labour is growing not just across national boundaries but also across industries. For example, today the outsourcing and offshoring of service tasks are a natural part of company activities. Thus, the constant work of optimising the value chain to strengthen competitiveness also breaks down industrial and service industry barriers.

Labour-intensive production relocated abroad

One of the areas of major change has been in production. Today, many companies find it attractive to locate wage-intensive and standardised production in countries where labour costs are below Nordic levels. Improvements in international transport and logistics have played a major role in enabling companies to locate all or parts of the production around the world, while major advances within communication technology enable companies to keep control of the production anywhere it is being carried out.

Many companies choose to locate production in Eastern Europe, but South East Asia is also attracting Nordic companies by virtue of the low wage costs and highly qualified staff available there. However, it



is not just the prospect of lower production costs that is encouraging companies to relocate but also improved access to some of the fastest growing markets in the world.

Setting up production abroad present many challenges. Despite this, many companies find that the gains outweigh the difficulties.

Many companies decide to maintain part of production in the Nordic countries in order to make development of new products more flexible. This is especially the case for companies where development and production are closely integrated.

For many companies global optimisation of the value chain also implies a change in supplier strategy. Many companies are in the process of reducing the number of suppliers, especially due to the opportunities for purchasing from all parts of the world.

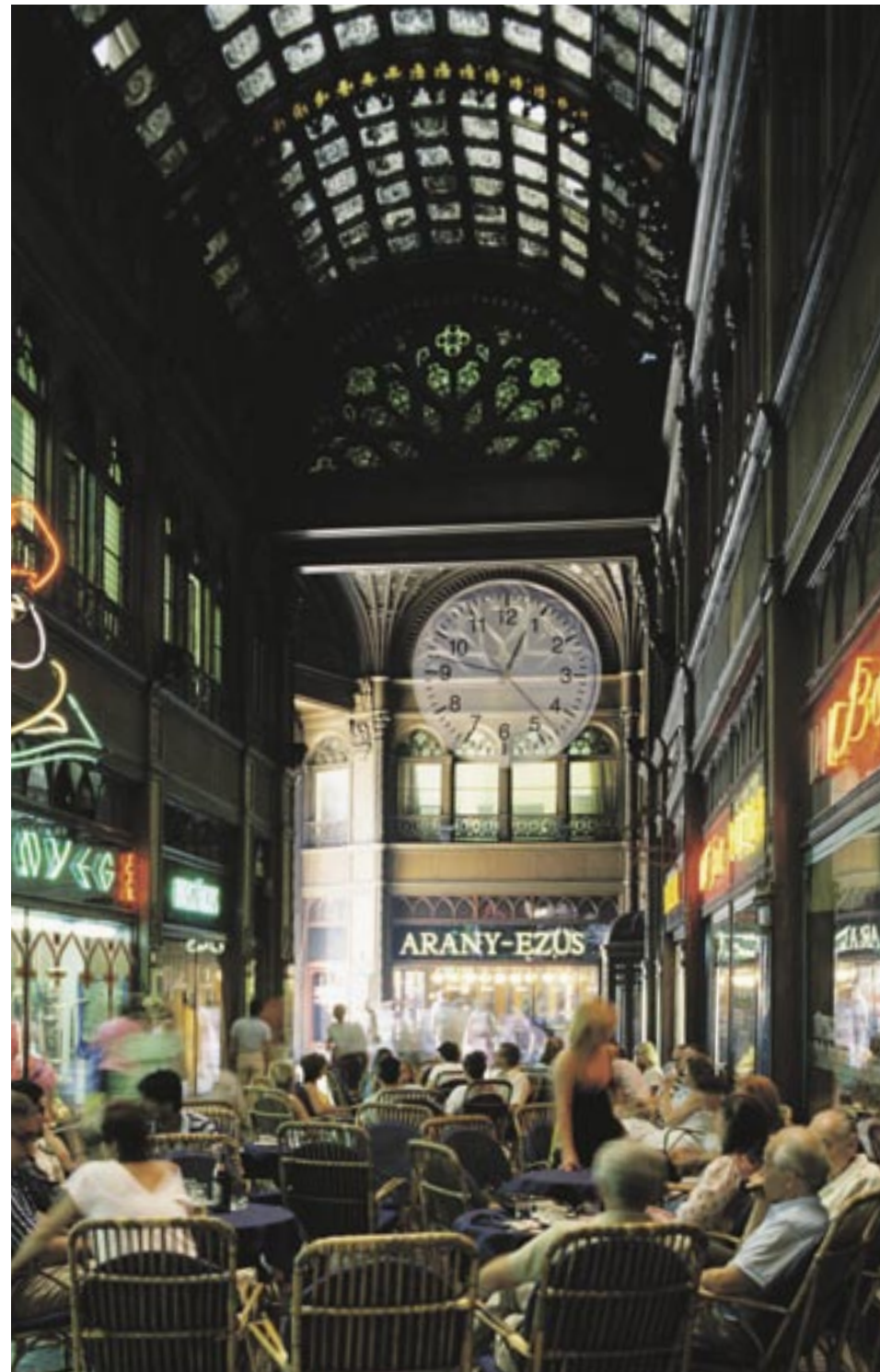
Product development in a global perspective

It is not just in purchasing and production where major changes have taken place. When it comes to product development

Nordic companies are increasingly aware that it is not possible to survive the ever more cut-throat global competition without taking advantage of the best available knowledge, whether this is located with customers, suppliers or in international knowledge centres.

When product development is not something that takes place behind closed doors but rather in cooperation with the best international knowledge centres, Nordic companies are far better able to face global competition where the requirement is for rapid development, sometimes as little as 2-3 weeks in some industries.

In this regard, Nordic countries must be leading in understanding the needs of customers. Knowledge-sharing between business and research institutions promotes combinations of user-driven research with research-driven innovation. This creates the highest potential added value for customers, e.g. by combining the latest technologies with customers' demands. This gives the biggest potential pay-off from research and can thus improve the Nordic countries' share of upmarket product manufacturing.



Job creation and job destruction

The activities of Nordic companies abroad are of economic benefit for the Nordic countries. Exports create far more jobs than we lose due to imports, and our participation in the global division of labour provides cheaper goods for consumers, thus boosting our purchasing power and prosperity. However, if this situation is to endure we need flexible labour markets to ensure smooth and efficient job turnover. We need to secure a situation where more jobs are being created than lost. Consequently the Nordic workforce must have the right skills to attract new jobs.

Large volume of exports is a crucial prerequisite for Nordic companies to maintain high employment in the Nordic countries. The returns from offshoring primarily come from three sources.

Firstly, offshoring to low-wage countries results in cost savings for companies.

Secondly, increased offshoring involves increased purchasing power for the recipient countries, and thus increased import of goods and services from western countries. China's participation in the international division of labour since the late 1970's has created tremendous prosperity in China as well as in the rest of the world. The rise in prosperity in the rest of the world is most obvious when the increase in purchasing power as a result of cheap Chinese prod-

ucts is measured. The biggest savings for customers and companies are obtained from imports of computer hardware and industrial production machinery. By importing these products from China—the European cost price is halved compared to a situation where the same products should be bought at average OECD-prices. For Denmark, calculations show that the total hypothetical saving for the Danish population is 13 bn DKK. This illustrates that consumer prices are reduced as a consequence of increasing international trade. Thus, consumer purchasing power has been boosted markedly when it comes to imported goods.

Thirdly, there can be gains if the supplier abroad is owned by a company from a Nordic country and returns the profits to the same Nordic country.

In addition, there are significant potential indirect returns attributable to freed-up Nordic labour being relocated to new jobs.

Economic return from outsourcing

Calculations carried out by McKinsey Global Institute show that American companies taking advantage of the global division of labour through outsourcing represent an economic benefit—both for the country that is outsourcing and for

BENEFITS FROM OFFSHORING

Net return to 1 euro outsourced to India

	USA	Denmark	Sweden	Germany
Cost savings	0.58	0.52	0.52	0.48
Import of US/GE/DK goods, services by providers in India	0.05	0.03-0.05	0.05	0.03
Transfer of profits by US/DK/S/GE owned providers in India	0.04	N/A	0.04	N/A
Direct return	0.67	0.55-0.57	0.61	0.51
Value of relocated labour	0.45-0.47	0.48	0.34	0.29
Potential net return	1.12-1.14	1.03-1.05	0.95	0.8

Note: Calculations for Germany include outsourcing to Eastern Europe

Source: McKinsey Global Institute 2003, 2004; Future Growth Think Tank 2004 and own calculations

the recipient country. The same applies to Denmark according to DI estimates.

However, for Sweden and Germany the picture is somewhat different. Calculations carried out by the Confederation of Swedish Enterprise indicate that the return to Sweden of 1 euro outsourced is only 0.95 euro. This is mainly explained by a low reemployment rate—which in turn is caused by low mobility and low flexibility on the Swedish labour market⁴. Therefore, it is not a law of nature that outsourcing leads to positive economic returns. The negative return from outsourcing from Swedish companies underlines the need for flexible labour markets and constant adaptation of economic policies as to create conditions that enable Nordic companies to take advantage of the international division of labour and thus at the same time create prosperity.

Furthermore, the rise in labour costs must be kept on sustainable levels and incentives to work should be strengthened by enlarging the gap between the level of transfer incomes and net income from work. Finally, the climate for investments should continuously be improved—in order to improve the conditions for new entrepreneurs and to make the Nordic countries attractive for foreign investments.

Does globalisation increase employment?

One crucial issue is what happens to the level of employment in the Nordic countries when production is relocated outside the Nordic countries as a consequence of globalisation.

In general, we find that overall Nordic employment over the last 20 years of growing international division of labour

has been on the rise. However, there have been fluctuations due to changes in the global economic climate and the business cycle; e.g. the 30 per cent decline in the value of the dollar between 2002 and 2005. Thus, the decline in employment of recent years is only to a small extent explained by structural changes.

However, in some Nordic countries, the growth of public employment, high tax rates, and regulated labour markets, have resulted in private employment growing slower than the population at large. This situation is not sustainable in the long run. With tightened competition from low-wage countries we can expect the Nordic manufacturing sector to become more and more capital intensive. With this in mind, it is important to open up the opportunities of growth for the more labour intensive private sector as well.

Nordic companies expanding their foreign employment improve their competitiveness, in general to the benefit of employment in the Nordic countries. A Danish study⁵ from 2003 showed that Danish companies with international operations increasing their employment abroad increased their employment in their home countries compared to the rest of the industry. Finnish studies also show that companies with international outsourcing operations have increased their domestic employment in Finland more than those companies operating only in Finland. Equally, studies from Rambøll Management (2005) show that 41 per cent of the Scandinavian and Finnish⁶ companies that have outsourced within the last two years have increased their numbers of employment. This compares to that 47 per cent of companies that did not outsource increased



employment. Moreover, 51 per cent of companies which are currently outsourcing expects to employ more people over the next two years whilst 53 per cent of the companies that have not outsourced expect to employ more people in the future. This compares to that 22 per cent of the companies which are currently outsourcing expect to employ fewer people in the home country over the next two years. However, for companies that are currently not outsourcing, only 19 per cent have reduced employment and 10 per cent expects to reduce employment.

The study indicates that a Nordic company establishing itself and growing abroad generally does not reduce employment in its home country. However, in Sweden and Norway recent experiences show that a slight majority of outsourcing companies reduced employment in their home country. In general however, successful participation in the global division of labour is a prerequisite for companies remaining competitive and thus preserving and expanding the number of jobs in their home country.

The extent to which Nordic companies move jobs to other countries differs remarkably. 10.7 per cent of Swedish com-

panies and 10 per cent of Finnish companies have moved parts of their production to other countries whilst 14 per cent of Norwegian and Danish companies have currently moved jobs to other countries.

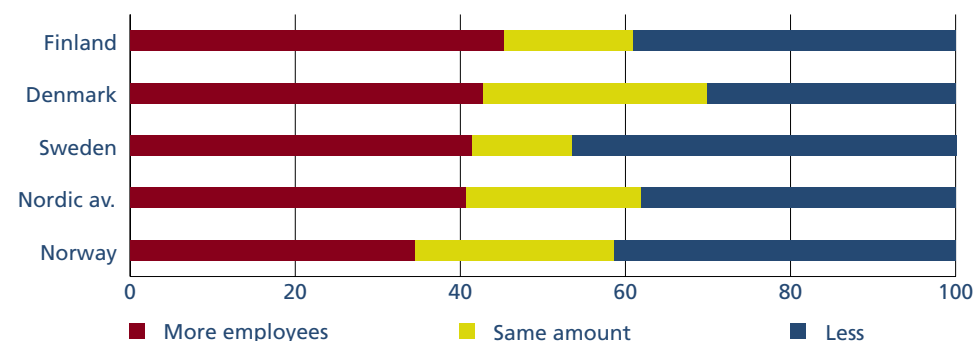
Nordic countries do not outsource to the same countries. 40 per cent of Danish companies which are outsourcing focus on Asia, whilst Sweden, Norway, Finland and Iceland concentrate more on outsourcing to European countries.

Until now, outsourcing is concentrated within few sectors. First of all, companies within manufacturing, wholesale trading and agency trade are leading when it comes to outsourcing. Currently, Danish manufacturers outsource twice as much as Swedish manufacturers. On the contrary, the Swedish and Norwegian transportation sectors are outsourcing twice as much as the Danish transportation sector. Outsourcing is least widespread within the retail trade sector and the building and construction sector.

Job turnover and relocation of jobs

There are no overall statistics of the number of jobs annually relocated from Nordic countries abroad as a result of out-

OUTSOURCING: CONSEQUENCES FOR EMPLOYMENT IN HOME COUNTRY



Note: The companies asked have outsourced within the last two years.

Source: Rambøll Management 2005

sourcing. However, several Danish studies indicate an annual figure for Denmark in the area of 5,000 jobs, representing only 2 per cent of total job creation and job destruction. And Swedish studies estimate an annual relocation of 23,000 jobs abroad in the past five years, representing around 9 per cent of total job creation and job destruction.

However, these analyses do not allow for the fact that those Nordic companies

outsourcing become more competitive, thereby enabling them to increase employment in the Nordic countries. Nor do they allow for the fact that foreign companies are creating new jobs in the Nordic countries.

The annual job turnover in Sweden is around 300,000 jobs, whilst the annual job turnover in Denmark is 250,000 (i.e. 250,000 jobs are closed down whilst another 250,000 jobs are created every year).

DIFFERENCES IN OUTSOURCING PATTERNS, PER CENT

	Asia	Eastern Europe	Western Europe
Finland	16.4	41.8	37.3
Norway	17.9	31.6	52.6
Sweden	20.3	25.4	50.8
Denmark	39.4	33.7	35.6
Nordic average	24.9	33.2	43.7

Source: OECD, Economic Outlook Database

CHANGES IN POPULATION AND PRIVATE EMPLOYMENT, 1983-2003

Total percentage change

	Denmark	Finland	Iceland	Norway	Sweden
Employment of the business sector	13.1	-8.2	21.8	6.1	3.7
Population change	5.3	7.4	22.1	10.6	7.6

Source: OECD, Economic Outlook Database

When compared to the overall job turnover in the labour market—5,000 Danish and 23,000 Swedish jobs respectively—the numbers are not alarming. However, Swedish estimates indicate that the relocation process is accelerating. This puts a pressure on the labour market to create more jobs in the coming years. The differences between the Danish and Swedish experiences regarding job relocation and expectations to future employment are mainly due to structural differences in the two countries; e.g. Denmark's higher concentration of the service sector and Sweden's more strictly regulated labour market and higher concentration of the manufacturing sector. This underpins the importance of flexible labour markets, company adaptability and continued adjustment of Nordic business conditions

as to take best advantage of the rapidly changing global opportunities.

One consequence of globalisation and the introduction of new technology is the constant increase of educational and qualification requirements resulting in a change in the content of existing jobs.

The new jobs being created require higher qualifications than the jobs being phased out. In recent years, there has been a considerable decline in unskilled labour employed. On the other hand, employment of skilled labour and highly educated staff is growing.

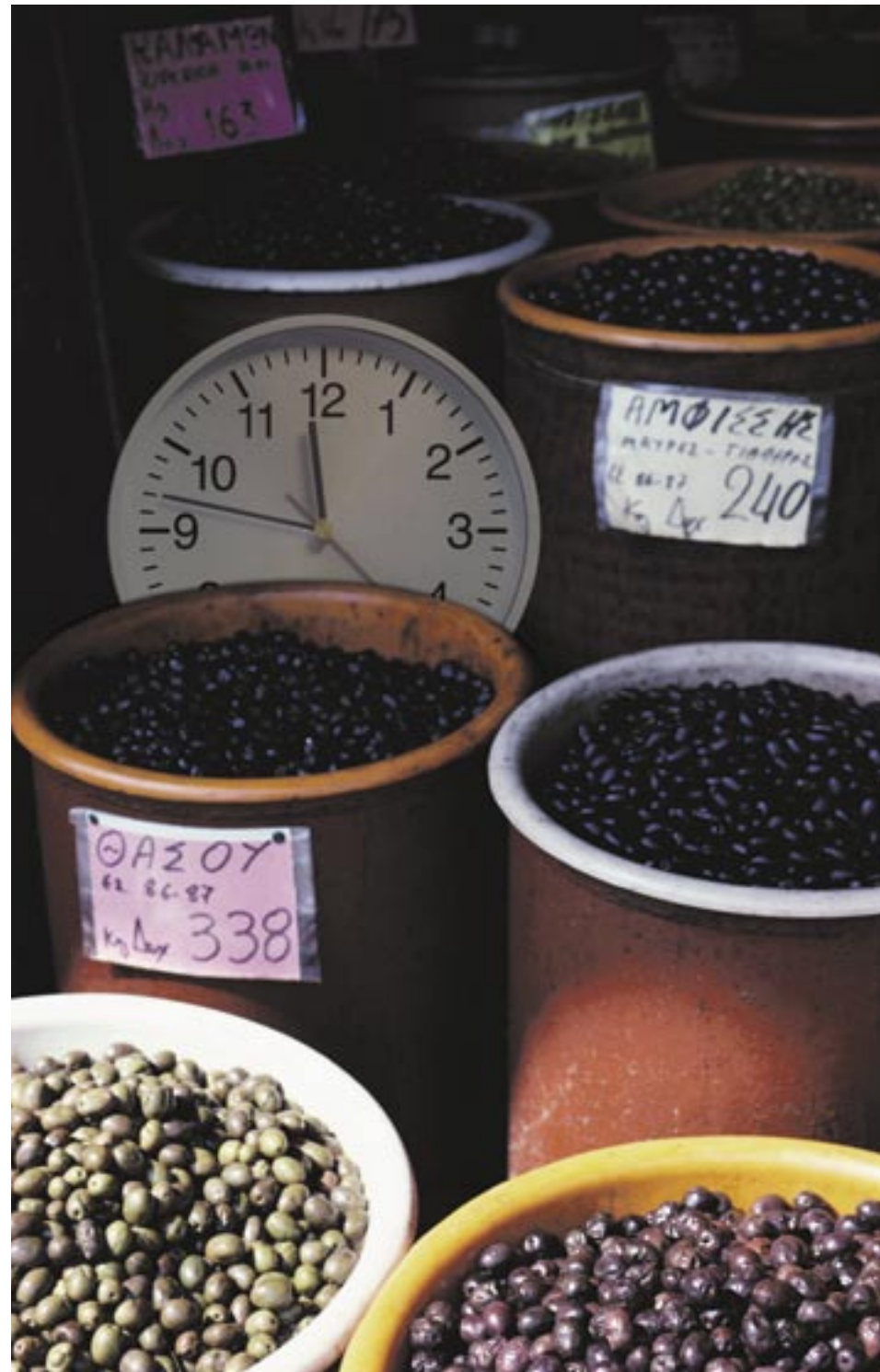
Research has shown, that the transition to ever more highly qualified staff apparently has not hit unskilled labour as hard in Denmark as it has in many other countries. This is due to the fact that the overall qualifications of the workforce are rather high

and rising whilst the proportion of people in the labour market without educational qualifications is declining.

Nevertheless, there are no signs that the least educated people have suffered as a consequence of globalisation and technological development. There are signs that the rise in the general level of education

and the flexibility and dynamism of the labour market has broadly been able to cope with the change. However, for some Nordic countries, e.g. Sweden and Finland, which are heavier reliant on the manufacturing sector, the tendency is not as obvious as for instance in Denmark.





The recipe —How to seize the global opportunities

Rise in global competition increases the need for Nordic companies to have good conditions in order to sustain economic growth and prosperity. Nordic companies cannot compete on wages alone and Nordic countries need to offer competitive terms for businesses to thrive. They must be leading in investing in highly productive equipment, in research and innovation and in developing a highly educated workforce.

The increasing international division of labour is creating new opportunities for growth and prosperity, but there is also increasing competition between companies both in the domestic and the international markets.

However, it is not only companies that are facing increased competition. Today, we are experiencing an increasing competition between the nations of the world in terms of creating favourable growth conditions for companies. Companies are increasingly choosing to locate at places where access to a well-educated workforce and favourable conditions for investment and business opportunities is prevalent. Good growth conditions for companies attract jobs, productive investment and create increased prosperity for citizens.

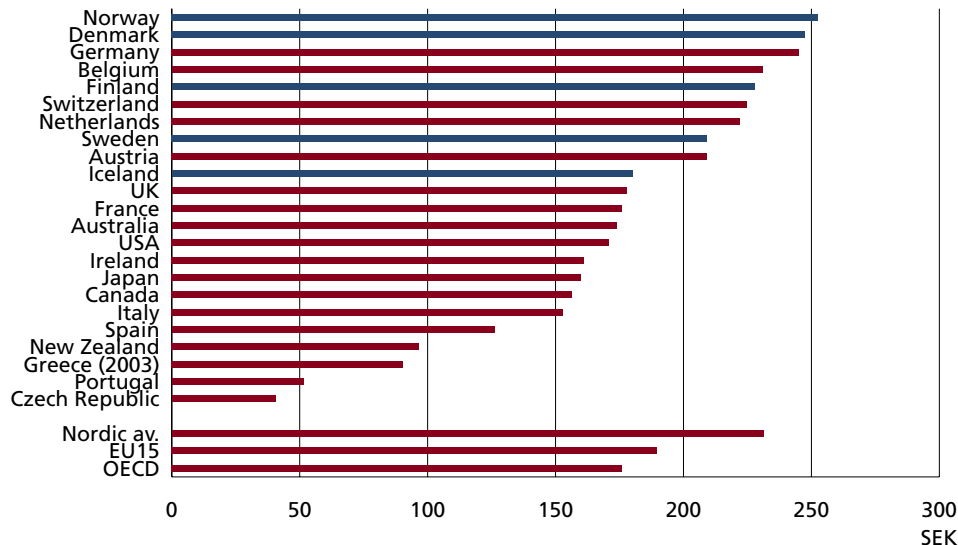
Therefore, the Nordic countries need to be among the most attractive regions

in the world to invest and do business in. It is necessary to create a competitive framework for Nordic and foreign company investments in the Nordic countries. Otherwise, we risk growth and prosperity completely bypassing a high cost region such as the Nordic countries. We can learn from countries such as Ireland, which during a decade has managed to attract foreign and highly productive investment, especially from companies wishing to export from Ireland. Ireland's success has been stimulated by such factors as the attractively low corporation tax, a low tax pressure of 30 per cent of GDP⁷, a well-educated workforce and easy access to export markets.

High labour costs rely on high productivity, expertise and adaptability

Nordic countries are today amongst the countries with the highest wage costs in the world, and are thus unable to compete with low wage countries for individual wage intensive production processes. Thus, the Nordic countries' role in the global division of labour is to attract and hold onto highly productive jobs whose value created during the hours of work matches the high wage costs. The Nordic countries need to be among the world's leading re-

LABOUR COST PER HOUR, INDUSTRIAL WORKERS, 2004



Source: Svenskt Näringsliv 2003, DA 2004

gions as regards the level of technological expertise, the general level of education of its population and adaptability of the labour market.

This requires a flexible labour market with strong incentives to work and to educate oneself, attractive personal and business tax conditions, expertise at international top levels and a prioritised commitment to research, development and innovation.

For a number of years, pay rises in the Nordic countries have exceeded many of the western countries with whom we compete. As a result of the rapid rise in wage costs, Nordic salaries are among the highest in the world, thereby reducing our competitive advantage compared to our closest rivals. With Eastern Europe and the Far East in mind it is obvious that the

Nordic countries are unable to compete on wage costs alone.

The high annual gross income of a skilled industrial worker in the Nordic countries must be viewed in the light of the relatively short annual working hours in most Nordic countries, which mean that Nordic wage earners are only available at work for a very short time compared to workers in other countries.

Although Nordic countries cannot compete on wage levels with low wage countries this does not mean that annual wage increases are not significant to competitiveness. On the contrary!

But it would not accord with the Nordic countries' level of welfare to attempt to implement large wage reductions to compete with low-wage countries. Instead we are forced to acknowledge that some la-

bour intensive production, which does not require a high skill level, will either be relocated to other parts of the world where costs are lower or must be automated. In the future, the Nordic countries must be more committed to efficient and knowledge intensive production higher up the value chain. However, such a commitment depends on the Nordic workforce being highly educated and productive.

Furthermore, moving some jobs out of the country does not solve the problem of the shortage of qualified labour. In the future there will be fewer young people to support more and more old people. Unless we manage to increase employment or productivity, it will lead to a decline in growth and prosperity.

This requires a two pronged strategy: on the one hand attractive framework terms must be created for investment in highly productive Nordic jobs. On the other hand we must ensure that there are sufficient numbers of competent employees available to fill these jobs.

WHAT TO DO!

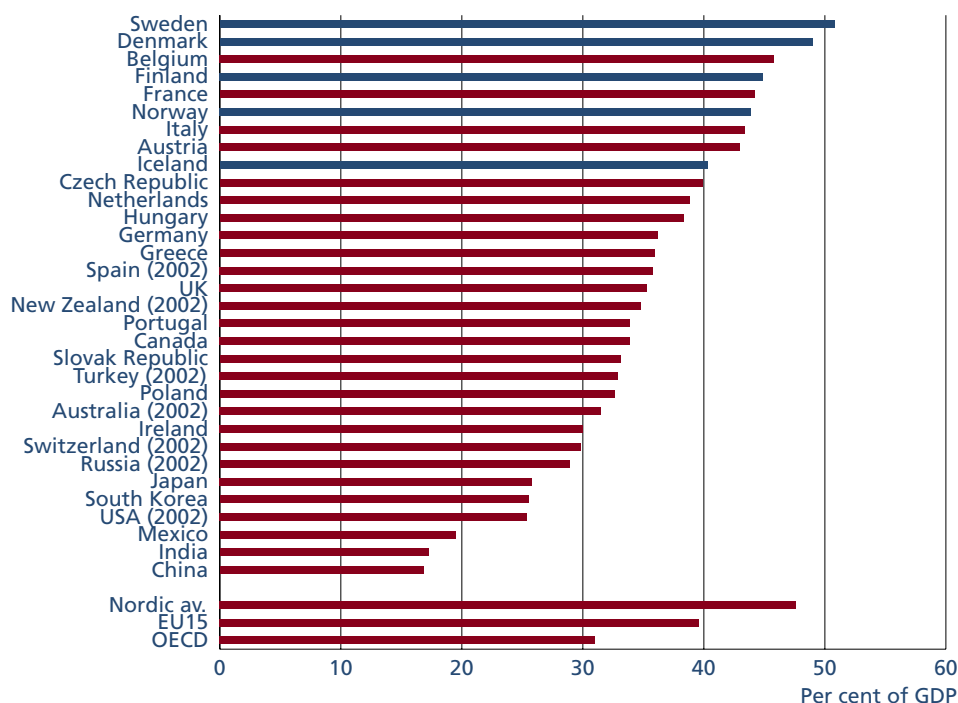
- Keep/establish a flexible labour market with strong incentives to work and to educate oneself
- Establish attractive personal and business tax conditions
- Keep increase in wage costs at a sustainable low level.
- Improve education at all levels
- Establish a prioritised commitment to research and innovation

High taxes frighten off talent and hamper business development

However, the strategy to make Nordic countries the home of knowledge-intensive and highly productive development and production is being hindered by high income taxes. Nordic countries have some of the world's highest tax burdens and this limits incentives to work, particularly as regards mobile, well educated and well paid employees. This makes it more attractive for companies to locate knowledge



TOTAL TAX REVENUE AS A SHARE OF GDP, 2003



Source: OECD – Revenue Statistics 2004, IMD 2004

intensive activities, such as research and development, in countries where income taxes, and consequently company wage costs, are lower.

Personal income taxation

It will be necessary to improve tax system to promote labour force participation better, particularly by increasing the difference in levels of labour income and transfer income. Currently, the incentives to work are too weak in particular among low skilled labour. At the same time, the problems of the shadow economy are increasing. The legitimacy of the tax system may be in danger if this problem is not addressed properly.

If the strategy of commitment to highly qualified labour and highly productive jobs is to succeed, it is crucial to alter the tax system to make it more attractive for highly qualified staff to work and live in these countries. The high marginal taxes on work are to blame for diminishing the incentive to work. Also, the incentives to educate oneself are reduced due to the high marginal tax levels.

Lower marginal tax rates should not be financed by increasing other rates and dues but through larger restraints on public spending on services—first of all on transfer payments. Within few years, there will be a very large group of old people

in the Nordic countries. This will gradually increase the pressure on the tax systems. This underlines the need for adjusting the tax system to stimulate work performance and growth. Higher age of retirement and a reduced growth rate in transfer payments could contribute considerably to meet this challenge.

Business taxation

It is important that tax systems do not distort investment decisions—either by distorting decisions about what type of investment to undertake or where to locate it—or who is making the decision and financing it. From a national perspective, there is a considerable risk of double taxation and misplacement of investments. We therefore think it is important to underline the desire to generally apply Capital Import Neutrality.

Moreover, differences in the taxation of owners will impact the ownership structure. Here, the different tax levels play a role as well as imputation systems or partial inclusion systems. The tax treatment of capital gains is also important. So far, most of the academic literature on Capital Ownership Neutrality has focused on the “quality” of owners. With different tax burdens, the most efficient owners may not be the actual owners and therefore the overall efficiency and growth of the economy will suffer. There is also a revenue implication when ownership structure is affected. Countries with high tax burden on capital income will tend to have a reduced ownership share (which could lead to reduced overall investment level in the EU since the most productive own-

ers are suppressed) and they will collect less in taxes as well. The existence of net wealth taxes, still existing in Sweden and Norway, run counter to effective ownership and growth and should therefore be abolished. A removal would make more entrepreneurial capital available to small and medium sized businesses, enhancing investment and job creation.

It is important to eliminate the remaining tax obstacles to cross-border economic activity and thereby create a true common market in the area of company taxation, which is indispensable if the Lisbon goals are to be achieved.

We would like to strongly encourage the government of all nations to speed up the process of removing tax barriers to investments in general and to cross-border investments in particular. It is important to find an early resolution to cross-border loss relief.

The small business taxation also needs improvements. Special regulation in several Nordic countries are at present too rigid and ought to better take into account the risk aspects of running small businesses.

WHAT TO DO!

High tax burdens limit incentives to work, particularly as regards mobile, well educated and well paid employees. This makes it more attractive for companies to locate knowledge-intensive activities in countries where income taxes, and consequently company labour costs are lower.

- Alter the tax system to make it more attractive for highly qualified staff to work and live in the Nordic countries.
- This should be done mainly by reducing the marginal tax on extra work as to increase the incentives to work and educate oneself.
- In the area of business taxation there is a need to remove tax barriers and enhance economic efficiency. We underline the desire to generally apply capital neutrality. In particular, it is important to abolish net wealth taxes and to reduce the capital income tax rate to promote investments and the supply of capital.

Erosion of the educational advantage

A well educated workforce is a prerequisite for Nordic companies to maintain their competitiveness in the future through increased commitment to research and development and highly productive, knowledge intensive production higher up the value chain. The Nordic workforce needs to be among the world's most productive and well educated. We cannot expect to earn top class wages with only a mediocre education.

JOB STRATEGY FOR THE UNSKILLED

It is crucial to ensure that there are jobs in the future for major parts of the Nordic workforce which today have a weak educational background. And there is no easy solution.

However, there appear to be four focus areas which combined could make a considerable contribution to boosting employment for this group:

- > Training and education
- > Investment in highly productive capital equipment
- > Highly qualified personnel who create jobs for less qualified personnel
- > Work incentives

Education is the most important pillar in a strategy for ensuring jobs for people with the lowest qualifications. This does not just apply to the basic education of the young, but also to supplementary training and further education. Technology is developing at a pace so rapid that in the future it will be unrealistic to imagine employees being able to preserve their skills if they do not improve these during their working life. Nordic companies are already among the leading in the world as regards company financed supplementary training. But there is also a need for a considerable financial commitment both on the part of individuals and the state. By lowering the marginal tax rates the hard efforts of

education could become more profitable, which means that the incentives to get an education in the first place would be strengthened.

Nevertheless, an educational strategy of this kind will not be enough. Even an extremely successful and focused commitment to educate more people will only make a serious contribution to improving companies' competency levels in the very long term.

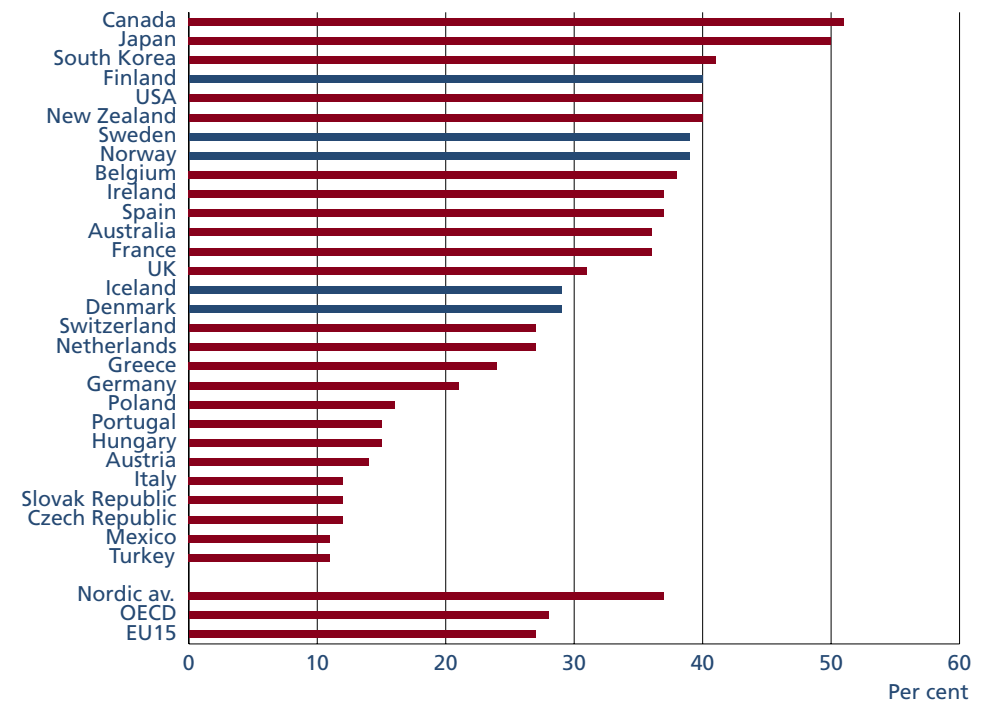
The individual's productivity must also be increased by making it attractive for companies to invest in hi-tech capital equipment in the Nordic countries.

An often ignored strategy of providing jobs for poorly educated people is actually to create more attractive conditions for the highly educated—and for the knowledge-intensive companies that employ highly qualified personnel. If companies set up production and development and create jobs for highly educated people, experience has shown that this will result in more jobs both for the skilled and unskilled.

Finally, there should be a larger income difference between work and social security. The system of taxes and transfer incomes must be so as not to hinder individual work incentives aligned⁸.

TERTIARY EDUCATION, 2002

Share of 25-34 year old population that has attained tertiary education



Source: OECD, Education at a glance 2004

EDUCATION ENHANCES DEVELOPMENT AND JOB CREATION

There is a need for more people to get a higher education. However, during periods of economic downturn one often hears the objection that many highly educated people cannot find employment.

However, it is clear that higher education leads to better employment opportunities. This has to do with the greater professional ballast which companies are demanding. People with higher education contribute with greater knowledge and more skills to help companies develop. In addition, people with higher educations are better able to adapt to fluctuating market conditions, and consequently enjoy better job opportunities.

High spending on education is not necessarily synonymous with a high educational level. Nordic countries are amongst those countries that spend most financial resources on education. However, the level of education especially in Denmark and Iceland is not high compared with many other OECD-countries. Therefore, there is a need for improved quality in the educational systems.

WHAT TO DO!

- Create better interaction between the educational system and industry.
- Strengthen educations at all levels (from basic education of the young, to supplementary training and further education for older employees).
- Make it attractive for companies to invest in hi-tech capital equipment to increase the individual's productivity.

- Make education more profitable. By lowering the marginal tax rates, the incentives for education would be strengthened.
- Create larger income difference between work and social security. The system of taxes and transfer incomes must be so as not to hinder individual work incentives aligned. This can be done by reducing the rate of increase in transfer payments.

Research, innovation and dissemination of knowledge

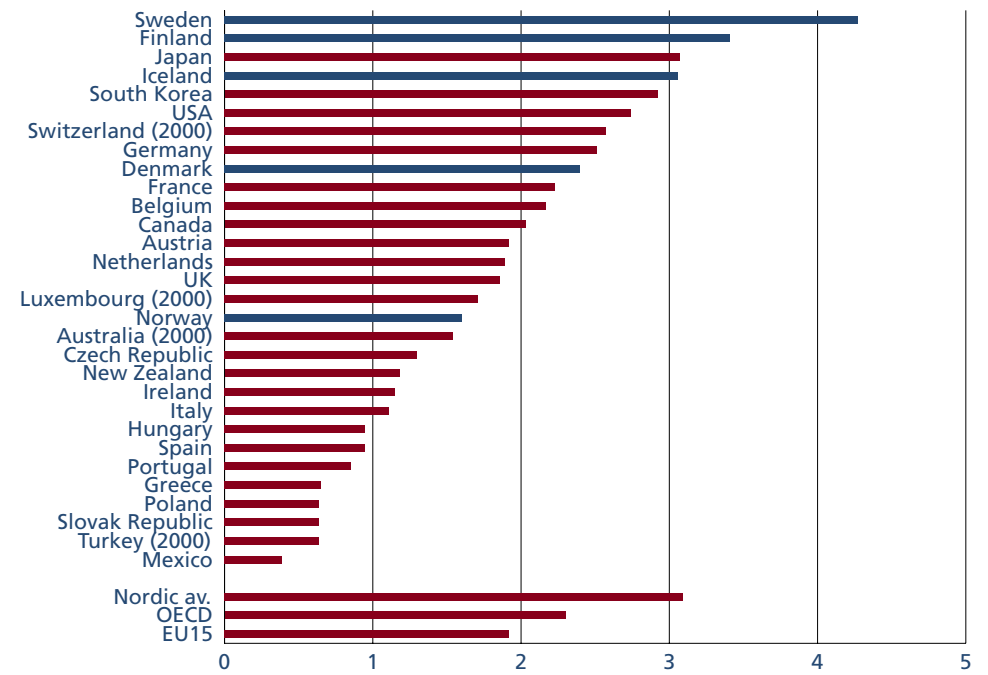
Maintaining and building up the Nordic countries' position as a rich and highly productive region requires investment in people acquiring qualifications. Moreover, investment in research and development enable us to create new knowledge which can be converted into new products, service solutions or production processes. As high cost countries we need to be on the forefront when it comes to creating new knowledge. After all, companies decide to invest in research and development where they find the highest expertise.

Whilst Sweden and Finland have long ago passed the EU 2010 Barcelona target of investing 3 per cent of GDP in research, Iceland has just reached it, Denmark is close, but Norway still seems to have a long way to go.

Nevertheless, it is not just the level of investment, which is important. How research money is invested is equally important.

Companies are increasingly competing in the conversion of new technologies into new products and business areas.

TOTAL INVESTMENTS IN RESEARCH AND DEVELOPMENT AS A SHARE OF GDP, 2001



Source: OECD, Education at a glance 2004

Per cent of GDP

Today, the universities research activities are rather sparsely connected with companies' opportunities to make use of their research. Even though Nordic countries are relatively well off with regard to research and development input, at least when looking at research and development as a share of GDP we do not seem to be very good at commercialising our research and development. Public research and development is—in other words—too rarely commercialised. Therefore, there should be established stronger strategic partnerships between knowledge institutions and companies. It is therefore of high importance that companies have access to public research centres, which underpin the long-term accumulation of knowledge. Nordic

countries must build up research centres with enough critical mass to match the US and the Far East and with strong public/private partnership.

It is crucial for all Nordic countries to ensure sufficient motivation for private investment in research and development here. Moreover, the Nordic countries could benefit by increasing incentives and opportunities for an increased private effort in the research and development area. Positive attitude towards entrepreneurship is an important precondition in this regard. This requires good conditions for entrepreneurs, e.g. easy access to money and more gentle rules with regard to rescheduling of debts. Also, there is a need for enhanced focus on entrepreneurship at the educational level.

At the same time, Nordic countries must be leading in understanding customers' needs, to best create high value for consumers. A combination of research driven and market-driven technological innovation creates the most efficient research, by creating added value for the customer.

Research driven and market driven innovation should not be looked at as complete separate activities. Companies do not develop new products out of the blue. They focus both on new technology and market demands. Therefore it is not a question of "either-or".

WHAT TO DO

- Strengthened education, qualitatively and quantitatively at all levels through better incentives.
- Invest at least 3 per cent of GDP in research and development.
- Focus more on business oriented research and development, e.g. by prioritising specific research areas that can put Nordic countries on the international research map.
- Improve conditions for industrial and public research and development agreements.
- Create stronger strategic partnerships between knowledge institutions and companies. It is therefore of high importance that companies have access to public research centres, which underpin the long term accumulation of knowledge.
- Build up research centres with enough critical mass to match the US and the Far East and with strong public/private partnership.
- Create better conditions for entrepreneurs by easier access to venture capital, relaxed rules for rescheduling of debts and strengthened focus on entrepreneurship in educations.
- Promote coordination of research driven and market driven technological innovation as to meet the needs of customers with the most sophisticated technology. This will optimise the gains from research and create the highest value for customers and researchers as well as lead to higher up-market export shares.
- Ensure sufficient motivation for private investment in research and development.
- Improve commercialization possibilities of research and development by lowering the taxes on capital and labour

An efficient capital market

Access to competitive financing is crucial to economic development in both existing and new companies. The European capital market should be just as efficient as in the US. But there is still some way to go be-

fore Europe has an efficient single capital market of American standards.

The capital markets of the Nordic countries and of Europe have still not been fully liberalised and the capital markets of the individual countries are still not fully inte-

grated. There are still differences in legislation, administrative regulations, tax and accounting rules and consumer protection regulations standing in the way of full integration. According to the OECD, there is a continued need for reforms in Europe and in the Nordic countries.

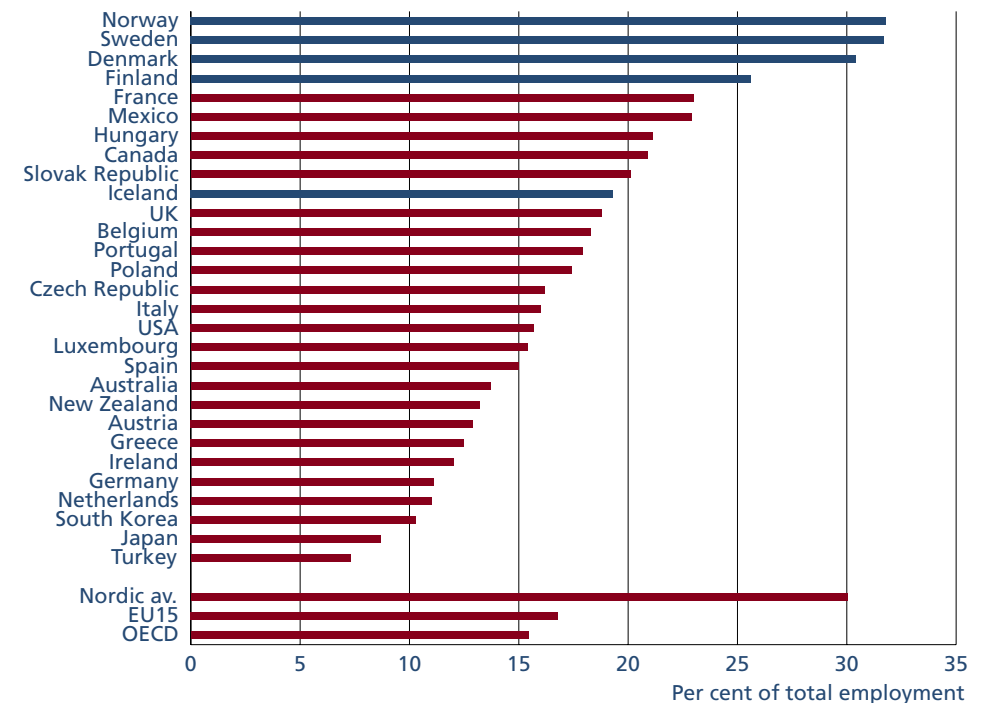
WHAT TO DO

- Improve financial infrastructure.
- Coordinate national policies relevant to financial markets, focusing on common needs and in line with the rapid development in this sector.

Efficient competition-oriented public administration and service

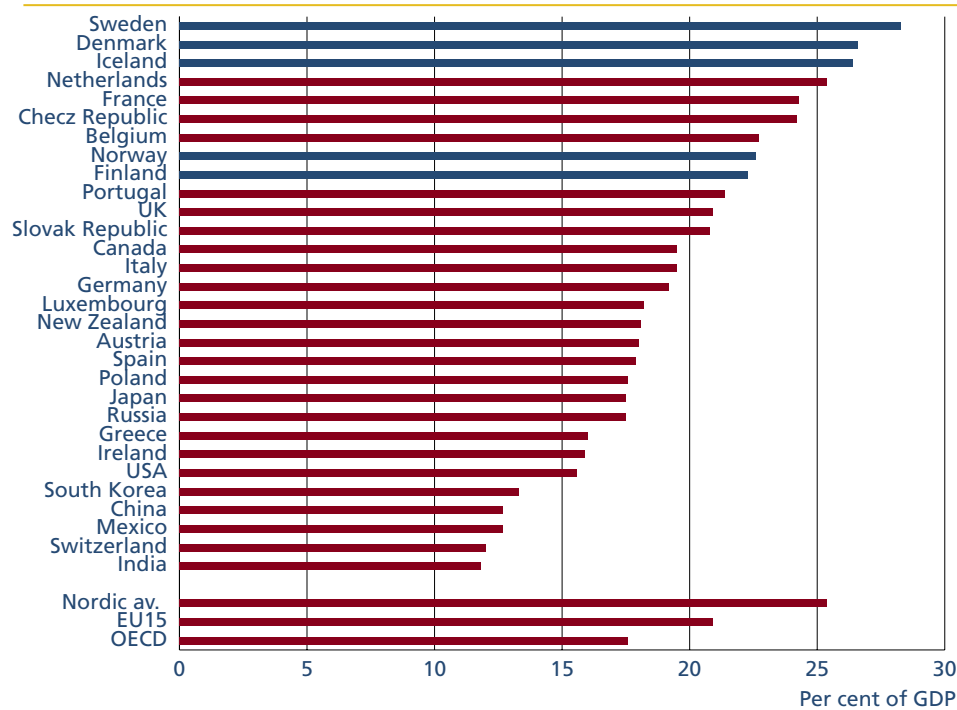
Welfare of our citizens is depending on the creation of prosperity in the business sector. Thus, it is important also from an international standpoint that there are attractive regional and local business environment conditions, since production, skill development and recruitment are largely local and regional in nature. Also, it is crucial to give the highest priority to growth and the creation of prosperity through highly productive and competitive value creation in the business sector.

EMPLOYMENT IN THE PUBLIC SECTOR AS A SHARE OF TOTAL EMPLOYMENT, 2003



Source: OECD

PUBLIC CONSUMPTION, 2003



Source: OECD and World Bank

Public authorities and institutions in the Nordic countries must have adequate focus on matching the needs of companies. In addition, the public sectors must be run efficiently so as to tie up the least possible resources both in the form of labour and taxation of the private sector.

Today, Nordic countries have some of the world's largest public sectors. Measured by share of total employment, it accounts of between 19 per cent (Iceland) and 32 per cent (Norway and Sweden) of total employment and is financed by collecting high percentages of GDP in taxes and duties.

Measured by total public consumption (share of GDP), Iceland, among Nordic

countries, stands out as the only country to have experienced a trend rise in the ratio of public consumption to GDP over the past two decades. Today, Sweden, Denmark and Iceland are the OECD-countries with the highest levels of public consumption relative to GDP. The upward trend in Iceland is attributable mainly to wage payments to civil servants.

The ratio of the government wage bill to GDP can be seen as the product of three separate terms: the share of government employment in total; compensation per employee relative to the economy-wide average; and the share of economy-wide compensation in overall GDP.

It is crucial to give the highest priority to growth and the creation of prosperity through highly productive and competitive business value creation. An efficient public sector administration and service should support this. The creation of prosperity by the business sector is the base upon which society can finance the welfare distributed by the public sector. When deciding whether to invest and thus create jobs, the existence of a stable economic framework is crucial for companies. Demographic changes which have resulted in more old people and fewer young people combined with the way in which we have arranged our welfare societies is likely to create significant problems in the future such as increased public borrowing.

The challenge is the way we have designed our welfare arrangement meaning that neither more citizens nor economic growth can remedy the financing problems. Thus, we need to alter our systems. Growth leads to increased prosperity and opportunities for more welfare, but we have arranged matters in such a way that public spending both on transfer incomes and public services grows roughly at the same rate as growth in incomes and thus will continue to exceed public revenues. Therefore, growth is only the solution to our economic balance problems if reforms are carried through.

The challenges facing society mean that the present situation is not economically sustainable in the long term. If we do not correct the structural imbalances, we will run an unsustainable deficit in public finances, since under the current rules and given the present trends spending will outweigh revenues.

Public spending should be decoupled from private sector growth, and there ought to be a larger role for the private sector in producing traditional welfare services even if the services are still tax financed. By introducing a greater deal of competition into the welfare sector, investment and productivity increases will follow, which in turn will relieve some of the financial burden. Further, in the future we need to move a larger share of the financial responsibility of welfare services from the state to the individual.

WHAT TO DO!

- Create attractive regional and local business environment conditions, since production, skills development and recruitment are largely local and regional in nature.
- Give the highest priority to growth and the creation of prosperity through highly productive and competitive business value creation.
- Design welfare system so that public spending is decoupled from private sector growth.
- Introduce a greater deal of competition in the traditional welfare sectors.

Tools for corporate globalisation

As new countries become increasingly important growth markets, it becomes ever more important for Nordic companies also to enter these markets, not just to sell their goods but also increasingly to insource or outsource, produce, acquire knowledge and to research and develop locally.

It is crucial to the success of Nordic companies in the climate of cut-throat competition that they can rely on the support of a set of efficient international business instruments to support their participation in the global markets.

Relations between suppliers and customers have grown ever closer. Today, suppliers often work together with customers in developing and producing highly specialised or upmarket products. These strategic partnerships for developing upmarket products can often open up entirely new markets.

Furthermore, it is important that organisations such as the WTO and the EU continue to provide free market access to companies and a free and secure framework for investment and other business activities in markets around the world. But companies only increase their international activities if they also have access to the necessary information, expertise, financing, etc., and therefore the international business instruments must have adequate resources and be capable of collaborating based on good commercial understanding and awareness.

WHAT TO DO!

- Create conditions so that companies can rely on the support of a set of efficient international business instruments to support their participation in the global markets.
- Involve actively and support the EU and WTO in bringing down barriers for trade and investments.

The global competition for prosperity

Globalisation is intensifying the global competition for prosperity. Both Nordic and European politicians face an enormous challenge to adapt their economies to the new global conditions. The task is to create attractive growth conditions for companies in a global economy where knowledge is the most important raw material and where highly productive investments are an essential catalyst.

The question is which countries are best able to organise themselves, so as to provide companies with the best possible preconditions for the creation of growth and prosperity.

The countries, companies and citizens that are able to adapt to the new circumstances and best at taking advantage of the new opportunities offered by globalisation will become winners in globalisation.

The Nordic region is rich, but in recent decades Nordic countries have gradually moved down the global prosperity rankings. As an exception, Iceland though has had the second highest growth in GDP per capita out of the 29 OECD-countries.

Nordic countries are also lagging behind in adapting to flexible, global knowledge-based economies compared to a number of other developed countries. Global development is rapid and our competitors are eager to establish themselves in a good position. Consequently, we urgently need to reform a number of structural growth conditions for company growth and value creation. The Northern economies must be geared to support high productivity, adequate numbers of competent employees

and successful participation in the international division of labour in all its facets. This

is the foundation of growth and prosperity in global competition.

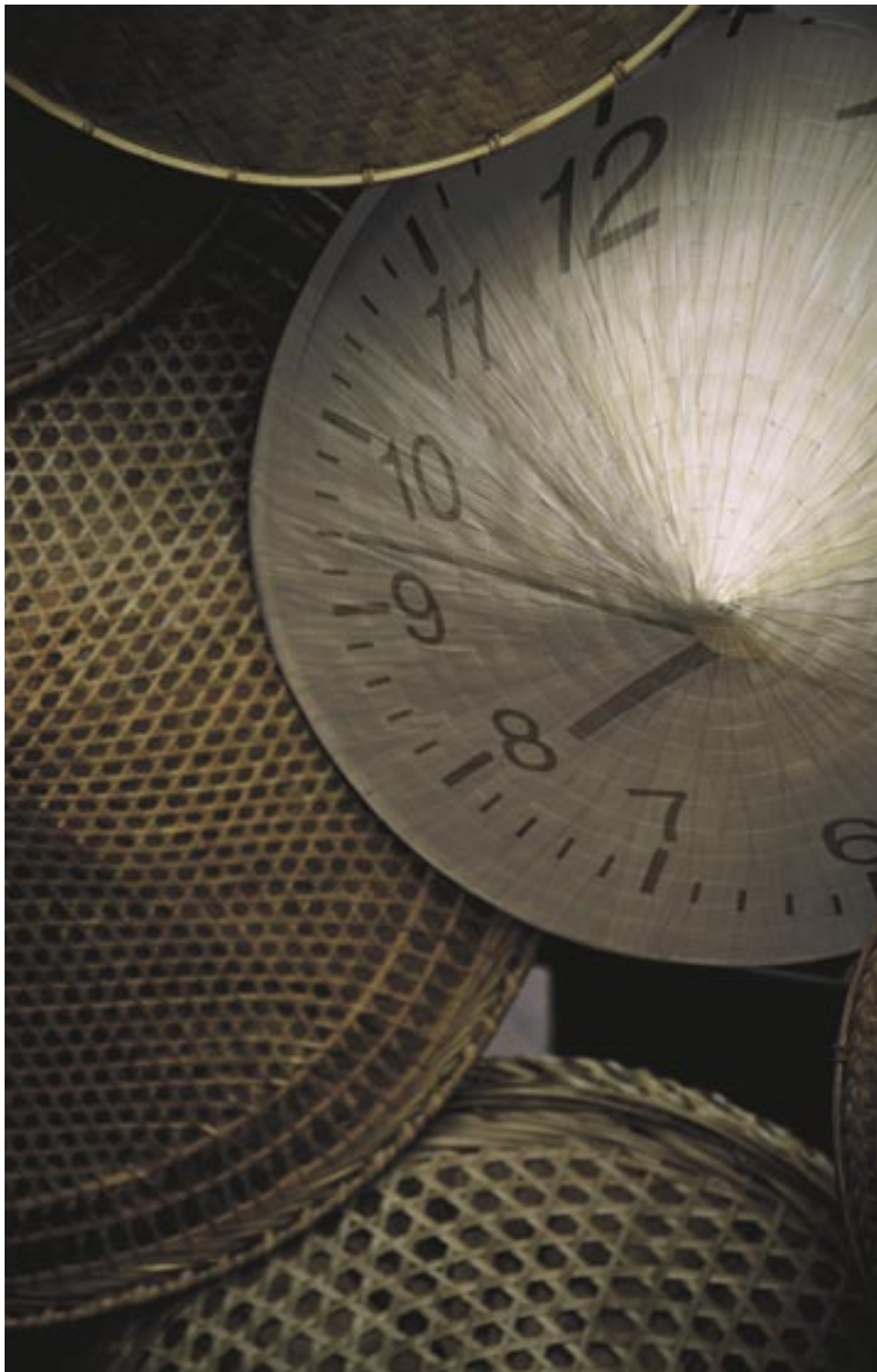
Definitions: Outsourcing and offshoring

OUTSOURCING

To let a contractor, collaborator or partly owned company (less than 10 per cent ownership) take over all or parts of a company's tasks; production, administration, development etc. that were previously performed in-house. Outsourcing can be of domestic character as well as international character.

OFFSHORING

Offshoring, can be defined as a company's relocation of business processes (including production/manufacturing) to a lower cost location.



Notes

- ¹ An export product is assumed to be of high quality if the export price is higher than the average price for the same product type exported from the rest of the world to the old EU15 countries. Based on this approach, all export products can in principle be divided into a quality hierarchy. 1) Upmarket products, whose export price from the country in question is 15 per cent above the median price from the rest of the world. 2) Middle-market products, whose export price from the country in question is within 15 per cent plus or minus the median price for the rest of the world. 3) Downmarket products, whose export price from the country in question is 15 per cent below the median price for the rest of the world.
- ² Graphs referring to Danish upmarket share.
- ³ Apart from EU25 the internal market is also accessible for Norway, Iceland and Lichtenstein.
- ⁴ The Danish Ministry of Economic and Business Affairs has calculated that the reemployment rate in Denmark is approximately 70 per cent. $\frac{2}{3}$ of dismissed textile workers found a new job within one year and 80 per cent of dismissed employees (in general terms) got reemployed within five years. Furthermore, calculations shows that between 77 and 85 per cent of the Danish workers who took an additional education after their dismissal found new jobs (relatively) shortly after their dismissal. For Sweden the picture is somewhat different. The Confederation of Swedish Enterprise estimates that the Swedish reemployment rate is only 50 per cent.
- ⁵ Source: DI's 2003 Establishment Study.
- ⁶ The study did not include Iceland but covered only Denmark, Norway, Sweden and Finland.
- ⁷ The tax revenue as share of GDP for Denmark and Sweden is close to 50 per cent, for Norway and Finland around 45 per cent and for Iceland 40 per cent of GDP
- ⁸ In Iceland, unemployment benefits are not related to previous income, but are fixed amounts for all. The amount is lower than the minimum wage. But this system is now under revision and some form of income relation is explored.

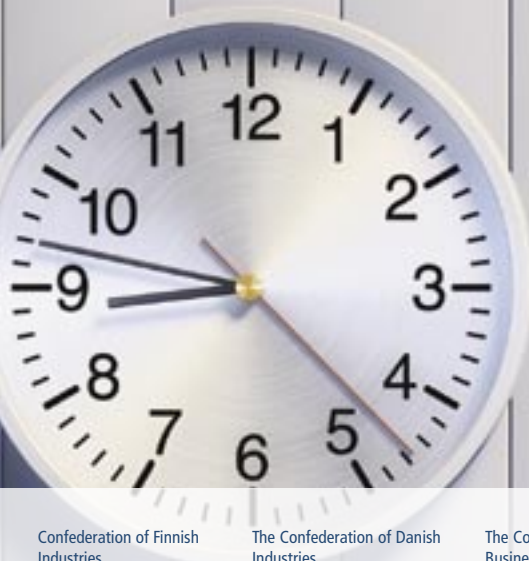




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