

Elli Heikkilä, et al.

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Economic Renewal and Demographic Change Evaluation of policies for well functioning local labour markets in the Nordic countries

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Economic Renewal and Demographic Change

*Evaluation of policies for well functioning
local labour markets in the Nordic countries*

by

Ingi Runar Edvardsson

*University of Akureyri
Akureyri - Iceland*

Elli Heikkilä

*Institute of Migration
Turku - Finland*

Mats Johansson

*Swedish Institute of Regional Research (SIR)
Östersund - Sweden*

Lars Olof Persson

*Nordregio, Nordic Centre for Spatial Development
Stockholm – Sweden*

Torben Dall Schmidt,

*Institute of Border Region Studies –
University of Southern Denmark,
Aabenraa, Denmark,*

Lasse Sigbjørn Stambøl

*Statistics Norway, Research Department
Oslo - Norway*

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Introduction

Although unemployment is a persistent problem in several countries, the issue of labour shortages is now emerging as an increasingly stubborn obstacle to growth across Europe (European Commission, 2001). The concurrence of relatively high levels of unemployment and labour shortages essentially reflects the highly differentiated nature of the labour market and the lack of coherence between the growth of demand for labour and the skills on offer among those looking for work. Recruitment difficulties tend to be reported in particular sectors even in periods of recession. In periods of recovery and as unemployment falls – or, more accurately, as the excess supply of labour diminishes – it is to be expected that skill bottlenecks will become more serious, the more so, naturally, in regions where unemployment is relatively low, but also in other areas where the skills of the unemployed do not match the demands of employers. If economic growth at present rates is sustained over the longer term, the problem of this “skills imbalance” is expected to be compounded by the projected slowdown in labour force growth over the next 10-15 years. In some regions we have already seen a decline.

In 2001 the employment rate was 63.9 percent on average for the European Union, but the objective has been set at 70 percent for 2010. At the Stockholm summit in 2001 agreement was reached on the overall goals required, which it was understood would require significant levels of commitment by the Union and by the Member States to the goal of full employment, as well as to the notion that a dynamic EU must consist of active welfare states. The EU heads of state and government were also unanimous in their belief that the path to such a goal requires investment in the areas of both employment and social policy (European Commission, 2004).

EU countries differ considerably in terms of their internal labour market structures and economic performance. Larger countries in particular display wide variations in the size of their Local Labour Markets (LLM). Some countries, e.g. Germany display a wide variation in industrial structure and income levels. Other countries such as Portugal and Greece show wide variations along the rural – urban scale. Countries with small populations and large territories, such as Scotland, Finland, and Sweden, also display a wide variation in LLM size.

In order to diminish economic and social inequalities the EU has put forward the cohesion policy. It is a specific policy involving a transfer of resources between Member States via the budget of the EU for the purpose of supporting economic growth and sustainable development through investment in people and in physical capital. Due to the cohesion policy, and the Structural Funds, differences in income and employment in the EU have narrowed over the past decade, especially since the mid-1990s. Large differences in prosperity and economic performance, however, remain, and these will widen much further when the new Member States join the EU in May 2004 (European Commission, 2004).

The concept of the Transitional labour market was launched by OECD in the mid 1990s (Schmid 1998, Schmid et al 2002). Transitional labour markets are defined as legitimate, negotiated and politically supported sets of mobility options for the individual. These transitions can take place in different time scales, day, week, month and year, but also under different phases of the life cycle. In the book on *The Dynamics of full Employment*, it is stated that the individuals’ increasingly frequent shifts of status from/to employment and education,

disability and sickness, retirement, household work, unemployment, etc., are becoming increasingly important to deal with in a successful employment policy.

The first hypothesis put forth by Schmidt et al (2002) is that the functioning and dysfunctions of labour markets could only be understood in a systemic framework. Employment systems are defined as the set of policies and institutions influencing interaction between the production systems and the labour market systems. The outcome of this interaction determines the quality and quantity of employment.

The second key hypothesis is that transitional labour (TLM) markets are beginning to emerge across Europe. TLMs are used as both a theoretical and a policy-oriented concept. They are based on observations that the border between the labour market and other social systems – the educational system, the private household economy, etc. are getting blurred. The important policy recommendation is that these boundaries should become more open for transitions between formal employment and productive non-market activities. Opening up of these boundaries should reduce the permanent insider/outsider problem which is so typical for modern labour markets.

In the transitional labour market theory, employment is getting a new meaning. Traditionally, employment is defined as the act of employing someone, the state of being employed or a persons regular occupation. In the emerging transitional labour market, employment is rather a temporary state or the current manifestation of long term employability. The prototype for this new employment concept, is the network labour market, with flexible entries and exits contingent on opportunities and individual expertise and continuous and flexible paths of accumulating work experience.

Thus, transitional labour markets are arenas for new forms of self-employment, where social integration is developed through the individuals' relation with others. In this form, social integration is taking place by productive social interaction not only within the field of paid work, but also in family work, cultural activities and voluntary work. Transition does not only mean movements between employment statuses, but also stands for flexible employment careers, including stages for preparation, encounter, adjustment, stabilization and renewed preparation for a new job or a new task.

This way of analyzing labour market performance makes it very obvious that simple, one-dimensional measures to achieve "full employment" such as minimum wages or negative income tax are not expected to be efficient. There is little doubt that the concept TLM provides a richer and realistic model for proactive and cooperative labor market policy.

Well functioning labour markets are those which secure high labour force participation for all groups on the labour market, where transition from unemployment, sickness or education to work is relatively easy, and opportunities to lifelong learning are present. Labour market performance has been closely related to labour market and welfare policies. Thus, labour legislation on hiring and firing workers, maximum working hour's regulation, work environment regulation etc. have a clear impact on labour market participation. Similarly, social security systems (unemployment benefits, parental leave, sickness benefits and so on) affect labour force participation as well, since extensive social welfare provides the labour force with opportunity to stay outside the labour market for some time (Edvardsson, 2003). In this paper we have chosen to analyse national policies on welfare and labour markets.

The purpose of this paper is to analyse cohesion regarding Local Labour Market (LLM) performance in Denmark, Sweden, Iceland, Norway and Finland. This is done, first, by looking the best and worst performing labour markets regarding activation of the labour force and transitions in respective countries. Second, employment policy implications for different types of LLM are considered.

The following hypotheses are put forward and tested in the paper:

H1: Given the extensive welfare and labour market policies the employment rates in the Nordic countries is relatively high on a European level.

H2: Given the extensive welfare and labour market policies there is a relatively small difference in the performance of LLM in the Nordic countries.

H3: The greatest differences in the performance of LLM will be found in the capital areas/metropolises on the one hand, and small labour markets on the other hand.

A Career Approach

This paper is based on a research project where labour markets in the Nordic countries have been analysed. In each country the most significant two year economic upswing period were chosen for analysis in the period 1995-2000. The chosen period differ therefore between countries depending on national economic development.

In this project, labour market performance is defined as a *dynamic* concept: the ability of the LLM

- to adapt to, and facilitate, structural change in the local economy by activating all educational segments of labour,
- to increase the input of human capital investments, and
- to reduce sick leave and increase reactivation rates.

The segmented structure of the labour markets according to formal qualification will be inherent in the analysis. By means of this *career approach* we are able to describe to what extent, and where, labour in different pools or status groups, and at different levels of education, is *activated or deactivated*. Activation rate is measured as a change in status to employment from year t to year $t+1$. Correspondingly, deactivation means changes in status from employment year t to year $t+1$.

Given that we have an empirical approach to describing and analysing the impact of knowledge and human capital input on a regional economy, we need an *operational definition of the knowledge* embodied in labour. Thus in the empirical analysis based on official register data we are left with a definition based on the level of formal education of each individual.

The following major *statuses* (year t and year $t+1$) are defined and dealt with in this analysis: Employed (wage labour or self employed), Pension/not employed, Studies, Unemployed and Sick leave.

Nordic employment policy

From a larger international perspective, there is a “Nordic model” as regards labour market policy, social policy and educational policy. A distinctive character of the Nordic model is the high public spending and strong public sector. There are, however, small but decisive differences between the Nordic countries. The purpose of the following sections is to analyse these similarities and differences.

The systems for *parental leave* are somewhat different in the Nordic countries. Thus, the longest parental leave is in Sweden where it is one year and four months, while it is shortest in Iceland and Finland, nine to ten months. There is also a difference between the countries in the possibility of mother and fathers to share the leave. The Icelandic system was recently appointed the first gender equal system, with three months each for the mother and the father, and three months that can be allocated freely. In all countries a large part of the leave time can be allocated freely between mother and father, but the tendency is still that the mother take the main part of the leave. The reasons for this are based in the system of gender relations as a whole and outside the scope of this study. A summary of the parental leave systems in the Nordic countries is given in table 1.1.

In the field of *sickness benefit* we find the greatest differences between the Nordic countries in labour market policy. First, the length of the sickness leave is one year in every country except Sweden, where there is no limit. This difference demands two comments. There might be that the fact that there is no limit in the Swedish system only is a statistical matter, and that the sick after one year are transferred to another category – the early retired for example. Another aspect is that a limited period for sick leave is an important push factor, pushing people back into employment, and that the Swedish system lacks this kind of push factor. Second, the amount of the benefit varies between the countries. Only in Norway is the benefit 100% of the salary up to a year, but the same is also the case for many groups on the Danish labour market. In Sweden the compensation is about 80% of previous salary. In Finland and Iceland, the amount varies dependent on collective bargained contracts. Third, only in Sweden is there a one day qualifying period fore sickness benefits. Finally, the responsibility of the employers varies. In Sweden employers have the responsibility to initiate activities for a healthy working life, rehabilitation etc. and pay sick pay for the first 21 days of sickness (apart from the 1 day without payment). In Iceland the employers pay sick pay for one to three months. The public sickness benefits are extremely low, resulting in private solutions to a high degree. In Denmark the employers pay for a longer period, but they get this reimbursed from the state/municipality. In Finland the employer pay until the 9th day of sickness. For a longer period the employer can pay salary or the employee get allowance. If the allowance is not paid to the employee it is paid to the employer, as a reimbursement for the paid salary. A summary of the sickness benefit system in the Nordic countries is given in table 1.1.

Table 1.1. The main characteristics of employment policy in the Nordic countries.

	Denmark	Finland	Iceland	Norway	Sweden
Parental leave length -	52 weeks. Possible to prolong with lower compensation	Parents are entitled to parental allowance either to the father or the mother for 158 weekdays (plus additionally 60 days for additional child)	3 months for each parent, not transferrable, plus 3 months with transferrable leave	42/52 weeks	Maximum 480 days
Parental leave payment level –	A public compensation paid to parents if they are not entitled to full wages from their employer. This differs from employers/sectors	Based on previous income. Basic subsidy common to all is 11.45€/per day	80% of salary in the previous 12 months. A child birth grant for students and those outside the labour market	Full pay, that is the same level as sick pay for 42 weeks or 80% of sick pay for 52 weeks	150 SEK a day is the guarantee level. Otherwise 80% of the income from the previous year/365, apart from 90 days when payment is 60/SEK per day
Sickness benefit length -	52 weeks within 18 months	52 weeks within two years	52 weeks within two years	52 weeks within three years	No time limit
Sickness payment level	Minimum for the employer to pay sickness benefit for 2-5 weeks. If the employer does not pay for the whole period, the municipality and the state pay	The employer pay full pay for the first 9 days for those who have worked longer than 1 month, otherwise 50% of the full pay	Employers pay full pay up to 1-3 months (up to a year for state employees). Thereafter the public social system pay sickness benefit which is a flat rate	The employers pay 100% of pension basing income for the first 16 days. Thereafter the benefit is paid by the National Social Insurance	Ca. 80% of full pay.
Unemployment benefit length -	4 years	500 days	5 years	?	300-450 days
Unemployment payment level	90% of full pay with a comparably low upper bound	50% of full pay	29 €a day	23.16€a day. Earning-related daily allowance: 45% until 2.084,40€ and 20% of the remainder	?
Pension age	60-67 years	65 years (62-68 from 2005)	65-67 years	67 years	From 61 years. The guarantee pension is from 65 years
Pension system	<i>Basic pension:</i> For Danish citizens 67 years and older (65 from July 1 st 2004). <i>Early retirement:</i> for those 60-65 years, members of unemployment insurance scheme and paid a pension scheme contribution for 25 years of the last 30 year of working life. <i>Condition early retirement:</i> for those	<i>Employment pension:</i> Depends on the amount of earnings and length of employment after the age of 23. Earnings are determined on the basis of the pay during the last 10 years in each employment. For self-employed or temporary	<i>Public basic pension with two components:</i> basic pension and income supplement. The supplement is income-tested and the basic amount is partly income-tested. The public pension is a modest sum but universal in nature. <i>Mandatory and</i>	<i>Basic pension:</i> the maximum level is 54,170 NOK, 80% if a married couple are both retired. <i>Additional pension:</i> The amount is based on working years, the maximum reach after 40 years of working. This pension is for	The pension is based on income (work, higher education, unemployment benefit, parental/sick benefits) from 16 years of age. <i>Income based pension:</i> the main part. <i>Premium pension:</i> 2.5% of the pension based income is placed

	with reduced ability to work (requirements: Danish citizenship, 18 years or older, resident in Denmark for minimum 3 years between 15-67).	employed the overall career earning are the basis. The total sum of pension is 60/66% of the highest previous earnings.	<i>fully funded occupational pension system</i> (60-80% of former salary). <i>Voluntary individual pension accounts.</i>	those with a yearly income above the basic income. <i>Special addition:</i> For those with only a small additional pension. The maximum amount reached after 40 years of membership in the National Social Insurance. The amount is ca. 80% of the basic amount.	in stocks and bonds. <i>Basic pension (guarantee pension):</i> for those with low or now income, immigrants etc. Different rules depending on years in Sweden, other social insurance etc.
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Formally, the Nordic systems regarding *unemployment support* are similar in structure, but different in detail. Unemployment benefits are given to unemployed individuals, who are registered as unemployed, of working age and that have been employed for a certain period prior to unemployment. There are also in most cases unemployment benefits for those with no prior employment. In all Nordic countries apart from Iceland, the unemployment allowance is based on previous income, the highest percentage in Denmark (70-80) and the lowest in Finland (50). The maximum period is different between the countries ranging from 300 days to five years.

The pension systems in the Nordic countries are rather similar in structure. There is a guarantee pension for those with no or low income and there is an income based pension which is the biggest part of the paid amount. In Denmark, Sweden, Iceland and in Finland there are also pension savings in funds and incentives for private pension savings. The retirement age is different in the countries, between 61 and 68 (from 2005). However, the tendency is towards more flexibility in the system, so that longer working period equals higher pension. In Sweden it is possible to retire from 61 years of age, in Finland 62 (from 2005), Denmark 65 (if entitled to early retirement then as of 60) and Norway and Iceland 67.

The public sector is in all Nordic countries except Iceland takes more responsibility for increasing competencies especially among the elderly on the labour market. There is also a tendency towards changing the pension system in order to increase the incentives for the elderly to stay longer on the labour market. In Norway there is a lower employer fee for older employees and in Sweden employers receive subsidies for hiring older employees. The Swedish pension system the one among the Nordic systems with the strongest incentives for employees to stay on the labour market in spite of that they have reached retirement age.

To summarize: the Nordic employment policy system is quite extensive on an international standard, and covers most aspects of the adult life, such as sickness, unemployment, childbirth, and retirement. Consequently, it encourages transition from sickness, unemployment and childbirth to work and vice versa. Also, the system supports senior workers to retire from work.

Performance of Nordic Labour Markets

In this paper we focus on labour market performance, as access to employment is of key significance for social cohesion since employment determinates in most cases whether people are able to enjoy a decent standard of living and contribute fully to the society in which they live (European Community, 2004). In this section we will examine the employment rate, and the unemployment rate, and transition in Europe in general, and in the Nordic countries in particular.

According to Figure 1.1 the employment rate in the Nordic countries is quite high, and around or above the Lisbon target of 70% in 2010. In 2002, Denmark had an employment rate of 75.9%, Finland 68.1%, Sweden 73.6% (European Commission, 2004), while the non-EU member countries Norway and Iceland had even higher employment rates. The employment rate in Iceland in 2001 was 86.6%, the highest in Europe, and the rate for Norway was 80.3% (Statistics Iceland, 2004).

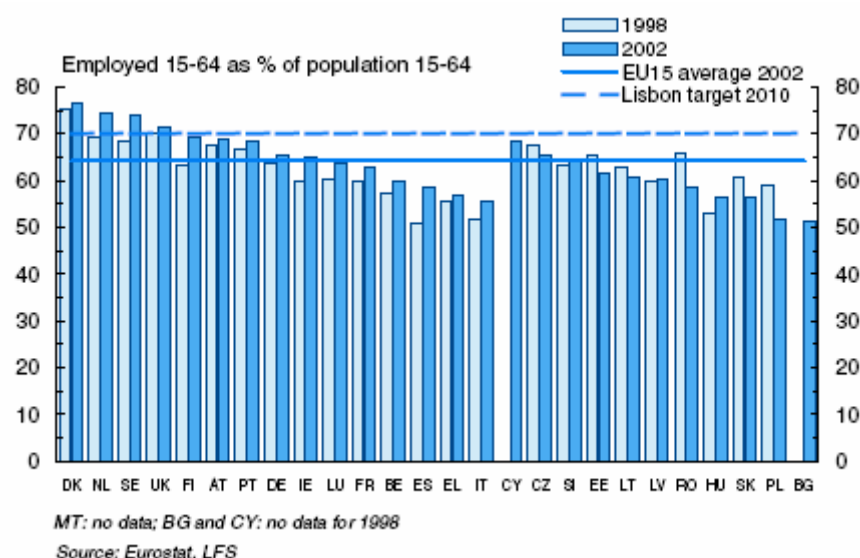


Figure 1.1. Employment rate in EU, 1998 and 2002.

Similarly, the unemployment rate is relatively low in the Nordic countries with the exception of Finland. Thus, the unemployment rates range between 2.3-5.1% (Finland excluded), while the average for the 27 EU member states was 9.1% in 2002.

Table 1.2. Unemployment rates in the Nordic countries in 2002.

Denmark	4.6
Finland	9.1
Iceland	2.3*
Norway	3.5*
Sweden	5.1
EU27	9.1

Notes: * 2001.

Sources: European Commission (2004) and Statistics Iceland (2004b)

Another indicator of the performance of the labour market, besides employment and unemployment rates, is the manner in which labour markets can activate students, sick people and parents to employment (transition rates). Given that the employment rate is quite high in Iceland, and most transitions are from job-to-job, we will below focus upon Denmark, Finland, Norway and Sweden.

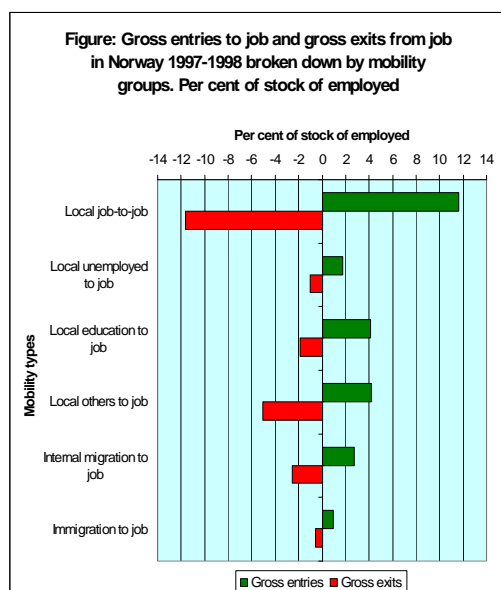


Figure 1.2. Gross entries to and from job, Norway 1997-1998

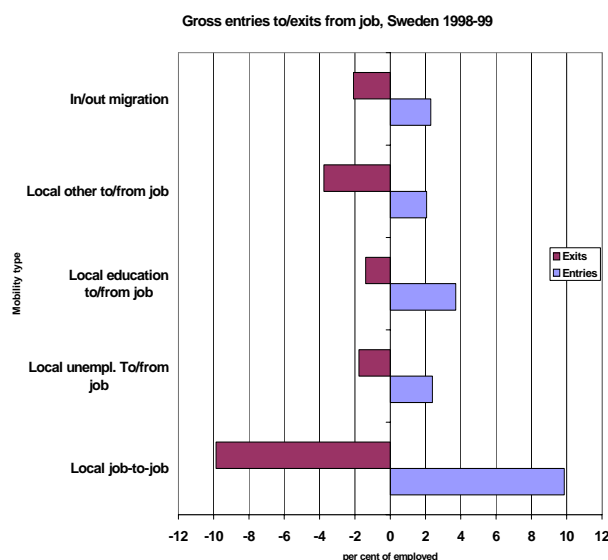


Figure 1.3. Gross entries to and from job, Sweden 1998-1999

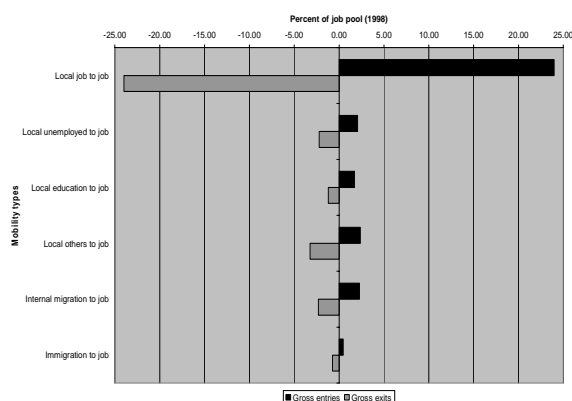


Figure 1.4. Gross entries to and from job, Denmark 1998-1999

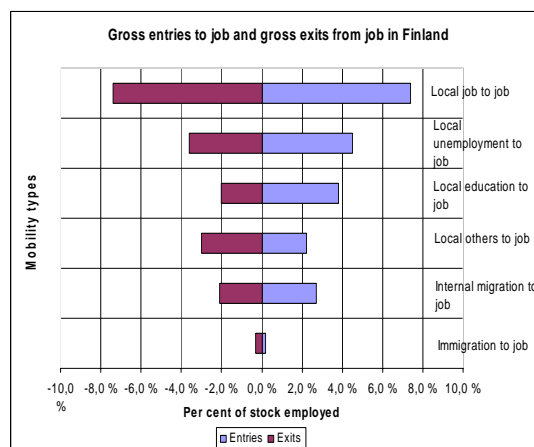


Figure 1.5. Gross entries to and from job, Finland 1999-2000.

Figures 1.2-1.5 show gross mobility rates by mobility types for Denmark, Finland, Norway and Sweden. All mobility rates are measured in per cent of the stock of employed in the first year of the period, which varies between the countries. By standardizing the rates is it possible to measure how much each type of mobility contributes to the total gross and net mobility in the nation as a whole and in each typology of regions.

Figure 1.2-1.5 clearly shows that the most important type of mobility is the change of jobs within the local labour markets. In the local job-to-job mobility each individual transition necessarily contributes to one exit and one entry within each local labour markets, thus making a balance between the exits and entries. In Norway as a whole the gross job-to-job mobility in 1997-1998 were almost 12% of the stock of employed and contributed to almost half of all gross mobility in the regional labour markets. In Sweden the job-to-job mobility was 10% in 1998-1999, as much as 24% in Denmark, and about 8% in Finland. Due to very strong economic growth in this period, an important part of the gross entries also derives from persons outside the labour force. However, the mobility from job to out of the labour force is even higher, mostly due to the age structure of employment in most of the countries. The mobility from local education to job is also important, albeit of minor importance compared to the effect of local job shifts. When experiencing low unemployment rates in most of the countries, the entries from unemployed to job represents a rather small part of the total gross entries to job, but as expected in an upswing period the entries from unemployment are significantly higher than the exits from job to unemployment. The gross effects of immigration to and emigration from job are also relatively small, though clearly positive in this upswing period.

From the above we can conclude that the performance of the Nordic labour markets is relatively good in a European perspective. The employment rate is high, and the labour markets manage to activate the labour force to a great extent. Hence, the employment policy seems to support high employment rates, and transition.

Local Labour Market performance

EU countries differ considerably in terms of their internal labour market structures and economic performance as already noted. That is also the case in the Nordic countries.

Table 1.3. The highest and lowest employment and unemployment rates in Nordic LLMs.

	Finland	Denmark	Iceland	Norway	Sweden
Highest employment rate	77.6	79,9	82.6	81.9	92.3
Unemployment	1.9	2,4	1.2		1,3
Lowest employment rate	49.2	59,8	82.0	63.9	86.5
Unemployment	18.9	6,2	1.4		6,6

From Table 1.3 we can see that the employment rate varies a lot between the best and worst performing LLM in the Nordic countries, except in Iceland, where both employment and unemployment is similar independent of location. In Finland the difference between the highest and lowest employment rates is 28.4 percentage points, 20.1 percentage points in Denmark, 18 percentage points in Norway, and 5.8 percentage points in Sweden. This is despite the advance employment policies in these countries. Similarly, the unemployment rates varies greatly between LLM in the Nordic countries.

Another indication of the LLM performance is how well they activate different age groups, as well as people with different educational levels.

The capital regions/metropolises in Denmark, Finland, Norway and Sweden shows the strongest positive net flows of labour in the youngest age group while the micro labour areas shows the lowest positive net growth (see Fig. 1.6-1.9) h. In Norway and Finland, the net figures for the age group 35-54 years are rather small but positive, except from regional centres with university in Norway. In Denmark, on the other hand the net figures are negative in all regions. The net figures for the two oldest age groups are generally negative and most negative in medium sized towns and regions in Norway for the age group 55-64 years, and in the capital region for the oldest age group. Similar pattern is found in Denmark and Finland. The net negative flows of labour in the age groups 35-65 in all regions is of special concern for Danish policy makers.

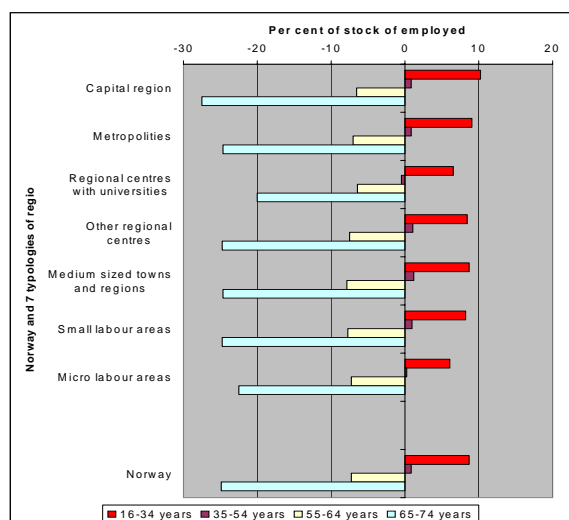


Figure 1.6. Net flows of labour by age groups 1997-1998 in Norway, and 7 typologies of regions.

Figure 1.7. Net flows of labour by age groups 1997-1998 in Sweden, and 7 typologies of regions.

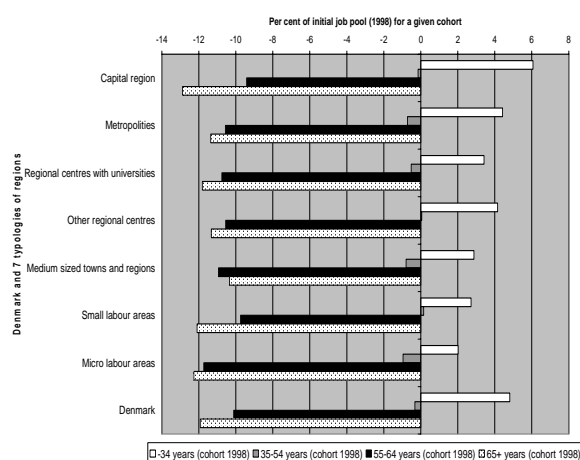


Figure 1.8. Net flows of labour by age groups 1998-1999 in Denmark, and 7 typologies of regions.

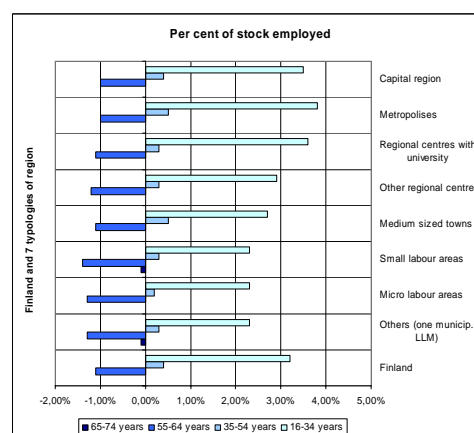


Figure 1.9. Net flows of labour by age groups 1999-2000 in Finland, and 7 typologies of regions.

The positive effects of net flows of employed with higher education is definitely strongest in the capital region and metropolises in all the Nordic countries, followed by regional centres, while micro labour areas show negative net effects of labour flows of higher educated employed (see Fig. 1.10-1.12). The net flows of lower educated labour are mostly negative except from the capital regions (Denmark is an exception here). The net flows of middle educated labour are generally positive, and strongest in regional metropolises and medium-sized towns and regions.

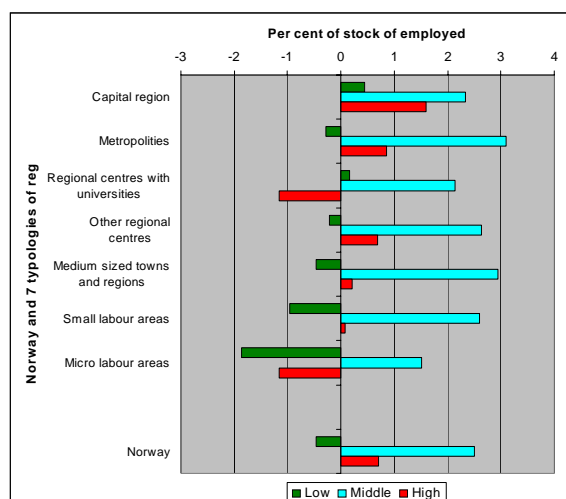


Figure 1.10. Net flows of labour by educational levels 1997-1998 in Norway, and 7 typologies of regions.

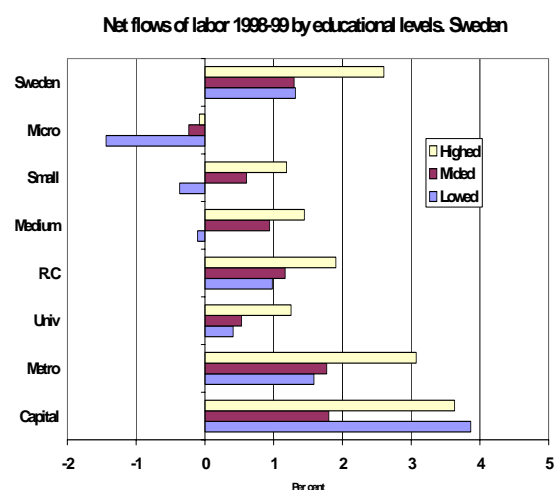


Figure 1.11. Net flows of labour by educational levels 1998-1999, Sweden, and 7 typologies of regions.

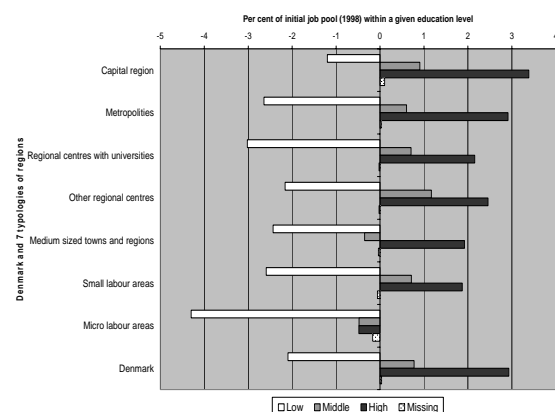


Figure 1.12. Net flows of labour by educational levels 1998-1999 in Denmark, and 7 typologies of regions.

In this section we have seen that the LLMs in the capital regions, metropolises, as well as regional centres with universities seem to perform best in the Nordic countries regarding activating the labour force while micro labour markets have serious problems.

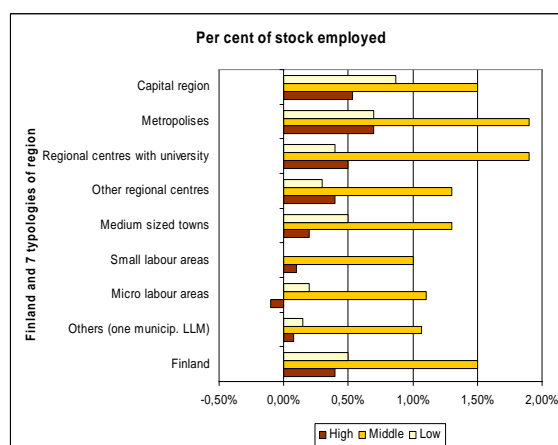


Figure 1.13. Net flows of labour by educational levels 1999-2000, Finland, and 7 typologies of regions.

Policy implication

So far we have seen that the general performance of the labour markets in the Nordic countries is relatively high on a European standard. We have also seen that even within in the Nordic countries with high employment rates, and relatively low unemployment levels, a noticeable difference is observed in the performance of LLM. From this we can conclude that the national employment policy is able to activate the larger LLM, while a more precise policy is needed for the small labour markets.

This paper has shown that the many small labour markets in depopulating regions in the Nordic countries are in particular need for notification. The options for good transitions in these regions are extremely limited and probably decreasing over time, in spite of large input of labour market, social and structural policies. This calls for a Northern dimension of the European policy for full employment and for extraordinary attention. For the large parts of the territories in Sweden, Finland, Iceland and Norway which are sparsely populated, it is questionable whether these regions will ever provide a functional market for labour as their size is below the “critical mass”. They are dominated by a secondary labour market, based on publicly subsidized employment. The aging population in these regions demands services from the shrinking - and also ageing - local labour force. A future challenge for policy is how it could ever be possible for “making transitions pay” in these parts of the European space?

Conclusion

In this paper the focus has been on the cohesion regarding Local Labour Market (LLM) performance in Denmark, Sweden, Iceland, Norway and Finland. This was done, first, by looking the best and worst performing labour markets regarding activation of the labour force and transitions in respective countries. Second, employment policy implications for different types of LLM were considered. Three hypotheses were presented in the paper. These are:

- H1: Given the extensive welfare and labour market policies the employment rates in the Nordic countries is relatively high on a European level.
- H2: Given the extensive welfare and labour market policies there is a relatively small difference in the performance of LLM in the Nordic countries.
- H3: The greatest differences in the performance of LLM will be found in the capital areas/metropolises on the one hand, and small labour markets on the other hand.

The main conclusions of the paper are that the employment rate is quite high in the Nordic countries. It was highest in Iceland, 86.6% (2001) and lowest in Finland, 68.1% (2002). That can be compared to the average 63.9% for the European Union in 2001. This gives some support to Hypothesis I.

Another conclusion is that the employment rate varies a lot between the best and worst performing LLM in the Nordic countries, except in Iceland, where both employment and unemployment is similar independent of location. In Finland the difference between the highest and lowest employment rates is 28.4 percentage points, 20.1 percentage points in Denmark, 18 percentage points in Norway, and 5.8 percentage points in Sweden. This is despite the advance employment policies in these countries. Similarly, the unemployment rates vary greatly between LLM in the Nordic countries. Also, the capital areas and

metropolises in the Nordic countries did function well in activating young people and highly educated workers, while small labour markets had serious problems. This means that Hypothesis 2 is rejected, while Hypothesis 3 gains some support.

The findings of this paper strongly indicate that general national employment policy is not sufficient tool for activating LLM. Although, such policy seems to activate larger LLM, a more refined policy measure is needed for the small labour markets in sparsely populated areas of the Nordic countries.

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