

## Incomes Policy - Danish Style

### The Background

Under the regime of fixed exchange rates instituted by the Bretton Woods Agreements, Denmark was one of the countries that during the whole post-war period suffered from chronic balance of payments difficulties. By this I mean that, whereas a number of other countries, notably Great Britain, the Netherlands, Norway and Sweden, experienced periods of virtually full employment without any balance of payments difficulties and were able when such difficulties arose to counteract them by mild credit restrictions and contractionary fiscal policies, with only slight setbacks in employment, Denmark from 1948 till 1962 never attained full employment, but had to curb the effective demand by heavy credit restrictions, the result being a fall in employment to a very unsatisfactory level (see table below which compares unemployment percentages for the countries just mentioned).

Danish economic policy was often described as following a zig-zag course: when employment was low and the state of the balance of payments satisfactory, expansionary measures were taken, but as soon as the expansion had gathered momentum and long before full employment was attained, the threat of a deficit on the balance of payments re-emerged, and the process had to be reversed, the outcome again being serious unemployment.

In an attempt to explain this unsatisfactory state of affairs, a theory which I should term "the income-race theory" was invented. It was launched by the Radical Party, a parliamentary group that is small, but influential because it stands at the centre of the scale of political opinion and so is able to turn the scale by joining the Right or Left according to its liking. This theory, which in fact has won supporters among professional economists, may be summarized as follows.

If equilibrium in the economy is to be maintained, the rise in expenditure for consumption and investment must not exceed the increase in output. However, trade unions, civil servants' unions, professional organizations, and associations of manufacturers and traders pay little or no attention to the equilibrium of the national economy. On the contrary, their purpose is to improve the position of their own members by raising their income. But as that goal

### UNEMPLOYMENT IN A NUMBER OF COUNTRIES (\*)

(percentages)

Year	United Kingdom	The Netherlands	Norway	Sweden	Denmark
1948	1.6	1.0	1.0	2.8	8.6
1949	1.6	1.5	1.0	2.7	9.6
1950	1.6	2.0	0.9	2.2	8.7
1951	1.3	2.3	1.1	1.8	9.7
1952	2.1	3.5	1.2	2.3	12.5
1953	1.8	2.7	1.5	2.8	9.2
1954	1.5	1.9	1.3	2.6	8.0
1955	1.2	1.3	1.2	2.5	9.7
1956	1.3	0.9	1.4	1.7	11.1
1957	1.6	1.2	1.4	1.9	10.2
1958	2.2	2.3	2.3	2.5	9.6
1959	2.3	1.8	2.2	2.0	6.1
1960	1.7	1.2	1.7	1.4	4.3
1961	1.6	0.9	1.2	1.2	3.9
1962	2.1	0.6	2.2	1.3	2.3

(\*) Source: Bulletin Mensuel de Statistique, U.N.

can be attained only at the expense of other groups, an initial success of any group leads other groups to demand higher incomes and to try to secure them through their own organizations or as individual enterprises. Thus a race in raising income is started.

It is immaterial which group initiated this race at the very beginning: as things are today, it may be started by business enterprises that autonomously raise prices or profit margins. As a result, the trade unions feel that their members are being left behind in the race for higher income, and accordingly they advance claims for higher wages. Next come the organizations of civil servants,

physicians, teachers and so on. When the round has been completed those who initiated it feel that, relatively, nothing has been gained, so they start another round, and the whole process is repeated. I have assumed that business initiated the process, but it can equally be started or accelerated by any other group, such as civil servants, trade unions or farmers' organizations, pressing for and obtaining subsidies, protective measures, etc.

As long as these competitively rising incomes have not overtaken the current productivity gains, the process is all to the good, for it is a way of securing an equal share of the rising real income for all groups. But when it has overtaken the productivity gain — as it has had a very strong tendency to do very quickly — a deficit on the balance of payments emerges (1), and the authorities have to intervene. As they have no power to reverse the rise in income which has already taken place, and as exchange rates are fixed and resort to equivalent taxation measures and subsidies in foreign trade is also ruled out (because of the free trade system that has found general acceptance), nothing but contractive credit and fiscal measures are left.

Whatever name and description may be applied to these measures, they all work through a contraction of monetary demand, and as the level of money incomes consistent with a given level of employment is fixed, employment must yield. When the balance of payments has been corrected in this manner and more or less unemployment has been created in the process, political pressure will be brought to bear for expansive measures to relieve unemployment. But as soon as an improvement in the employment situation gets under way, a claim from some group for a rise in income again emerges and the whole upward spiral, and its unavoidable suppression, is repeated.

It must be strongly emphasized that the theory here described maintains that not only contractual incomes (wage rates, salaries, etc), but also entrepreneurial incomes can be arbitrarily fixed and maintained as long as the monetary authorities are willing to finance the increase. In other words, according to the theory, just as the trade unions may negotiate agreement with the employers on a rise in wage

(1) I have here described the current argument; in actual fact what produces the balance of payments deficit is not the relation between income and productivity, but between domestic and foreign costs.

rates from a given day and thus determine — provided employment is not affected — the workers' income, so entrepreneurs, by fixing prices, can likewise determine their income. In both cases employment will be unaffected as long as the authorities allow credit to be expanded so that the higher income may be financed (this of course cannot be done when exchange rates are fixed). The struggle is a question of income distribution, not necessarily of employment.

If the entrepreneurs arbitrarily raise their profits, and the workers acquiesce without raising claims for higher wages, and if the authorities passively supply the finance, the only thing that will have happened is a change in distribution in favour of the entrepreneurial class, and a new equilibrium will have been reached at a higher price and income level. If, on the other hand, the workers demand and obtain compensation for the higher prices, and if the entrepreneurs answer by another round of price raising, a spiral is set in motion, which some day must be stopped by the authorities, with unemployment as the result.

This process is exactly equivalent to the one often described in the case of wages: wages are fixed arbitrarily; if employers acquiesce, and if the authorities supply the finance, nothing but a redistribution of income in favour of wage earners need take place; for the increased income of the workers is sufficient to buy the goods which the entrepreneurs have to forgo. If the entrepreneurs do not acquiesce, but raise prices equally with wages, a vicious spiral has been started.

Some theorists (among them the present author) hold that an arbitrary rise in wages, assuming that the authorities do not put obstacles in the way of its financing, is neutral with respect to distribution and employment. For as the workers proportionately increase their monetary demand, the entrepreneurs will be able to sell an unchanged amount of goods at prices increased by the same percentage as wages. If prices are not raised by this percentage, there will be a surplus demand that could only be met by rising prices. A wage-price spiral may develop, because the rise in money income obtained through the rise in wages is frustrated by the equal rise in prices. But it can be avoided neither by government intervention to ban price rises, nor by voluntary abstinence on the part of entrepreneurs; cost may not be fully covered, production may go down, or excess demand develop.

This theory is rejected by the "income-race-theory", which maintains that the above argument could be reversed, taking entrepreneurial income and the rate of profit as the starting point. It does not attach any importance to the distinction between contractual and residual income because the latter is determined by market conditions, while the former could be arbitrarily fixed and thus determines the latter. Both categories of income, according to the "income-race-theory", are determined by the same forces, and both are conceived of as cost as well as income.

The competitive demand for higher money income is a struggle for raising the shares in real income of the groups, and shares can be changed, but in the process financial stability is jeopardized to the detriment of production and, in the end, of all concerned. For this reason a co-ordination of the group-interests is needed with a view to financial stability and a just distribution of income.

On the basis of these ideas the Danish Parliament in 1955 adopted a resolution requesting the Minister of Finance to appoint a committee "to investigate to what extent the economic and foreign exchange difficulties were due to deficient co-operation between the agencies and organizations exercising a major influence on the economic policy of the country and to consider ways and means to secure the best possible co-operation in the future".

The committee was appointed on December 14, 1955. It had 23 members of whom five formed a Presidium made up mainly of professional economists, whereas 18 members represented organizations of the main economic interests. The Presidium was to report to the Minister of Finance and to Parliament before the end of February 1956.

After a series of meetings of the committee, the Presidium submitted a report containing an analysis on the lines indicated above. It concluded with a proposal for establishing a system of agencies for economic analysis and deliberation: (a) an Economic Research Institute, headed by so-called "independent" personality appointed by Parliament; (b) a Research Council of seven members appointed by Parliament and drawn from the staff of the universities, the Central Statistical Bureau and the Central Bank; (c) a Board of Councillors consisting of members representing the main organizations for the promotion of economic group interests. The function of the Board was to give advice on practical matters to the Research Council, the members of which were to take part in the meetings

of the Board; (d) a Social Economic Council of three members appointed by Parliament. Its function was to impart information and to serve as arbitrator between conflicting interests, especially emphasizing the long view. It was empowered to call conferences of representatives of group interests, public agencies and to summon any personality to give evidence before it. It was made a legal duty to attend the conferences called or appear before the Council when summoned.

The report was submitted in June 1956, but no immediate action was taken by the Government or Parliament. Everything proceeded as usual. The years 1954 and 1955 had been marked by relatively high activity, but also by great strain on the balance of payments, resulting as usual in several rounds of contractive fiscal measures: increase in taxation, reduction of public investment, licensing of residential building combined with subsidies, and in addition a tightening up of credit policy.

In spite of a continuing high prosperity in the rest of Europe, these measures succeeded in dampening down economic activity in Denmark. Unemployment rose in the course of 1955 and reached a very high level in 1956 and 1957. Wages continued their rise at the usual rate in spite of the high level of unemployment. Then from 1958 a new era seems to begin. In connection with a mild recession that was proceeding in the main European countries in 1957, halting a strong inflationary trend, a considerable fall in raw material prices, including metals and fuel, took place. This meant a very great improvement in the Danish terms of trade and thus in the balance of payments: foreign reserves began to rise, liquidity became abundant and interest rates fell greatly.

As activity in the rest of Europe also resumed its upward trend, and as this process continued and even gained momentum, activity rose in Denmark too, and as this was for a time even followed by a rising surplus on the balance of payments, the whole process accelerated. The number of insured workers rose considerably and the unemployment percentage fell, reaching unprecedentedly low levels, in fact, levels almost as low as any that had prevailed in the other Scandinavian countries, the Netherlands and Great Britain during the entire postwar period. In a country not accustomed to such a tight labour market, the rise in wages accelerated. Yet, as the balance of payments on current account was positive from 1957

through 1959 and only slightly negative in 1960, no restrictive action was taken.

However, as the deficit expanded in 1961, a turnover tax of 9 per cent of prices at the wholesale level was imposed in the summer of 1962 on practically all commodities. About half of the proceeds were to be compensated by a reduction in income taxes, to come into force six months later.

During the discussion that preceded the adoption of this tax a buying spree developed, resulting in a large deficit on the balance of payments. As wages had risen by 11-12 per cent per annum for two years in succession, as large claims for increases were to be advanced by the trade unions when the time came for the collective agreements to be renewed (at the beginning of 1963), and as a large deficit in the balance of payments was envisaged for that year too, great political anxiety developed.

This mood was sharpened by the expectation of a lull in the general prosperity of the main European countries. The fact that the Employers' Association, influenced by the general pessimistic outlook, stated in advance its disinclination to grant any increase in wages, even demanding removal of the sliding-scale clause which traditionally was part of the collective agreements, and that in these circumstances a major wage conflict was probable, rendered the situation still more critical.

In view of this the Radical Party, now a partner in the coalition Government, revived its "co-ordination ideas" and urged its coalition partner, the Social Democrats, to support the placing before Parliament of a Bill incorporating these ideas.

#### The Establishment of an Economic Council

The foregoing are the events that led up to the introduction of the Act of September 1962 establishing a Council for Economic Co-ordination (2). The Act was adopted with the smallest possible majority. The parties right of the centre pointed out that the Government — and the people — already had ample and easy access to impartial analysis and information on economic matters. Besides private sources, there were two governmental agencies of this kind.

(2) Law No. 102 of 5 September 1962 "om økonomisk samordning".

The new institution, in their view, would serve only to relieve the Government of a responsibility which it alone ought to shoulder. The extreme left voted against the Bill as a device which could be used by the Government to betray the interests of the workers.

The Council was appointed by the Minister of Economy and consisted of a Presidium of three economic experts, elected for an initial period of 6 years, one of whom was nominated Chairman by the Minister (3), and a certain number of members, appointed for an initial period of three years. Of these one is nominated by the Minister of Finance, one by the Central Bank, while 15 represent trade unions, employers' associations, industrial and commercial organizations, etc. Four other members, possessing economic knowledge, were appointed by the Minister of Economy.

The Presidium is empowered if it so wishes to invite representatives of other ministerial departments or organizations to join the Council for the discussion of specific problems. The task of the Council is "to follow the economic development of the country and to contribute to the co-ordination of the various economic interests".

The Council convenes at the decision of the Presidium and/or at the request of at least three ordinary members. In any case it is to meet twice a year. The meetings are presided over by the Chairman of the Presidium.

A secretariat is established to conduct research and collect information at the request of the Presidium. The head of the secretariat is appointed by the Minister of Economy on the proposal of the Presidium. The members of the Presidium and the Secretary General are not to be members of Parliament, and the Secretary General must in addition be independent of business enterprises, industrial and commercial organizations, and organized labour and employers.

After deliberation in the Council, the Presidium submits a statement or report to the Government, and it may if it so chooses make the document public. It may if it wishes attach an account of the views expressed in the Council.

(3) The members of the Presidium are Professors Søren Gammelgaard, Erik Hoffmeyer, and Carl Iversen (Chairman).

## The Council at work

### (a) *The scope of its activity*

The task assigned to the Council (or its Presidium) is very vague indeed. A clue could be sought in the background that I have just described and in utterances made by the sponsors of the Bill during its discussion in Parliament. Unfortunately these statements are not very clear either. The conclusion I should draw from these sources would be that the problem that prompted the creation of the new Council was the trouble connected with maintaining fixed exchange rates and a high and stable level of employment within the framework of a market economy, and that it would be the function of the Council (or rather the Presidium) to contribute, by means of impartial analysis and enlightenment, to the solution of this problem.

From a press release containing the opening speech of the Presidium's chairman, we are able to get a fairly clear idea of what the Presidium conceives to be its function.

According to this statement the Presidium accepts in principle the philosophy and working method outlined in the report of 1956 on economic co-ordination. The main idea seems to be that the Council should be a contact agent, a sort of debating club. It is not to pass resolutions or issue statements: this task is reserved solely to the Presidium. It is the task of the Presidium (and the other economists attached to the Council), according to the speech, "to contribute to the purely objective analysis of the economic development and of the consequences of concrete measures of economic policy".

At each meeting the Presidium is to place before the plenum of the Council an analysis of the subject to be discussed, and it is the task of the ordinary members to speak their mind on the subject in general and the information or arguments presented by the Presidium in particular.

The Presidium does not intend to limit its activity to dealing with any one single problem, but will welcome suggestions from the Council members with respect to subjects that ought to be examined. In this respect the Presidium warned that it will not confine itself to formulation of a wage policy. On the contrary, in order not to be

biased against any single income group, it will follow in equal measure the development of all categories of income.

Apart from this central problem, questions such as the long run economic development, the conditions for a vigorous long-term economic growth, structural changes, especially with respect to agriculture, and problems in connection with Denmark's possible membership of the Common Market, will be taken up for discussion.

Thus we see that the Council (or rather the Presidium) intends to establish itself as a general economic analytical agency with regard to all problems of the present and the future.

As we have seen, the deliberations of the Council are only intended as guidance for the Presidium, which alone and on its own responsibility issues statements or reports to the Government and the public. As to the contemplated character of these reports, I quote from the speech:

"The purpose must be to provide not only the Government, but also the public with a better basis for passing a judgment on the economic situation and economic policy. The main objective must be to reveal the consequences, direct and indirect, immediate and prospective, of taking or refraining from taking this or that measure. Naturally it may also be a question of indicating the instruments of economic policy which might be employed to attain specific economic and political objectives."

At this stage it might be useful to consider for a moment the expediency of the structure of this institution as a basis for general analysis.

As we have seen the Council is divided into two categories, viz., the Presidium, which does the analysis and draws the conclusions, and the ordinary members, who are allowed to give their opinion and answer questions if asked. They may also listen to lectures given by members of the Presidium. Now suppose that land-holding legislation is on the Agenda. There are at most three members who have any technical knowledge of agriculture which could be of any interest to the Presidium. For the rest of the members it would be a sheer waste of time to sit and hear this discussion. They might have some political prejudice regarding this question, but as the Presidium is interested in analysis rather than in politics, and as political prejudices are settled in Parliament, it ought to be possible to find a better instrument for dealing with this problem, e.g. a special committee consisting solely of agricultural experts

and economists. In fact, there is already such a committee working in Denmark.

Or suppose that the problem of economic growth is to be dealt with. It is not clear what is meant by economic growth, but let us assume that it is defined as the increase in gross national product per head. The fact is that not one of the representatives for the various trades would be able to say anything but platitudes on that particular subject. It is being investigated by a number of economists all over the world and nothing of practical use could be expected to emerge from the Council on this subject. Some think that economic growth depends greatly on that part of the national product that is consumed, but no scientific body would be able to express a view about the future welfare effect of any given suspension of consumption in favour of other purposes. It would be a purely political matter. This Council would hardly be a useful agent in dealing with such a subject.

I cannot think of any specific problem requiring technical knowledge which could be usefully dealt with in this Council as a basis for political action.

There would at best be very few of the members who would possess a well-founded opinion on the question.

The position is different if the questions discussed are, for example, price, wage, salary and profit control. On these questions the members who represent the group-interests will hold an opinion and they will have knowledge that may be useful for the Presidium, and vice-versa. This is why such problems are bound to be the main concern of the Presidium.

This is not to say however that the new institution is particularly well equipped for dealing with similar questions. But this is a matter that can best be decided by experience, so let us turn to the activity of the Council up to the present.

#### (b) *Analysis and recommendations*

As I have already indicated, a new exchange crisis was maturing during 1962, the deficit on the current balance of payments having mounted to something of the order of 1-1.5 milliard Danish kroner, or a little more than 10 per cent of total imports. It is true that a considerable part of this deficit was due to the introduction in the summer of 1962 of a turnover tax and the buying spree to which this

gave rise. However, there undoubtedly was a considerable genuine deficit, which was expected largely to persist in 1963. In addition, the labour market was very tight and the workers were pressing for higher wages, which to a large extent were granted, so that average earnings rose by some 8 per cent during the year. To this should be added the fact that the collective agreements were expiring in the spring and ambitious wage claims were being raised by the unions. The employers on their part insisted that no increases could be granted since costs were already too high and a slackening of the boom abroad was expected. As an additional strong argument they pointed to the fact that large tax increases had been introduced in the summer for the purpose of curtailing demand and that a further deficit on the balance of payments was envisaged.

Faced with this situation the Council acted speedily. The members were appointed at the beginning of November 1962 and on December 18 the Presidium issued a report addressed to the Government and the public, the reasoning behind which — as far as I understand it — could be summarized as follows: There is such a thing as an economic equilibrium in society (or rather the nation) as a whole. Deviations from this equilibrium spell something bad. While this concept of equilibrium is not clearly defined, it means, according to the report, "especially the interdependence between production and employment, the level of prices and cost and the balance of payments".

If the equilibrium has been lost it may, the report suggests, be re-established in this manner: make an estimate of the increase of real national product for a subsequent period, one year, for instance (4), allow for the current disequilibrium (manifesting itself as a deficit in the balance of payments on current account), deduct the planned increase in government expenditure on goods and services and you have the part of the increase in production which is available for distribution between the various social groups.

As far as the equilibrium is concerned, it is immaterial to which categories of incomes the surplus is distributed: it could be distributed to increase wages of a definite group of workers, to a general increase in wages, to old age pensions, to any form of social benefits, to subsidies to farmers, to increase profit margins, to dividends to shareholders, etc.

(4) A decrease in production would be treated similarly.

In this calculation no distinction is made between an increase in income due to an increase in the labour force employed, in capital or in productivity, nor has consideration been given to the fact that the two first mentioned items automatically would accrue to those possessing the additional factors, according to the prevailing rates of pay and profit margins. The Presidium seems to assume that this income, too, could be redistributed arbitrarily.

Armed with this theory, the Presidium went on to make this calculation for the case actually before it: the increase in total production was put at nearly 2,000 million Danish kroner for the year 1963 (ex post it turned out to be about half that figure). The rise in government expenditure was estimated at about 500 millions. In the case of the balance of payments the Presidium abstained from making an estimate because the outlook was considered uncertain. Thus the amount available could at most be put at 1,500 millions.

However, taking as a basis the sliding-scale clause in the collective agreements, it was estimated that wages and salaries in the spring would rise by about 1,000 millions, plus the adjustment in the government employees' wages, which were tied to the rise in the private sector's wages, and plus the cost of farming subsidies, if they were to be continued (which was to be expected, as no essential change in the farming situation had occurred since the subsidies were introduced).

Thus the conclusion was that the whole prospective surplus had in fact already been disposed of, and that no further general increases in income could be granted if equilibrium was to be obtained and maintained.

As we have seen, the Presidium had strongly emphasized that the distribution of income was a purely political matter and no part of their responsibility (5). They felt it was a duty, however, to facilitate the task of the politicians in this respect by throwing light on the actual development of the various income categories, so that the authorities could see who had gained over whom and take steps to distribute income more equitably.

For this purpose the Presidium had started to collect detailed statistics and it suggested to the Government that an attempt be

(5) In spite of this it did venture to suggest that such income increases as might be granted should preferably be given to such groups of workers which according to available statistics had lagged behind as recipients of real wage rises in recent years.

made to persuade the labour organizations to postpone the pending wage negotiations until these statistics had been processed (6).

Further, it urged the authorities, in making their decision on the distribution of any production surplus, to take account of the alleged sociological law of the "income-race". For this purpose it was paramount that all claims for income increases which might conceivably be advanced should be settled simultaneously in one "package deal" (7).

For if the income claims advanced by one group — in the case in question the trade unions — were settled in isolation, difficulty would be found in persuading it to moderate its claims, as the situation required, since it would be impossible to know in advance which claims would be raised by other groups — and perhaps granted. However, if the first group obtained a rise, then according to (alleged) experience, the remaining groups would make similar or perhaps larger demands. In so far as the authorities might feel obliged to grant those demands, wholly or in part, it would probably be impossible to establish equilibrium, and it would be necessary to fall back on the restrictive credit policy to curtail income, with unemployment as the outcome (8).

### (c) *The reaction of the Government*

As soon as the Government had received the report it called meetings of the major political parties and of representatives of business and labour. All seemed to sympathize with the ideas of the report, but no decisions were taken. In the meantime the negotiations for a wage settlement continued without result; the trade unions maintained their rather ambitious claims, and the employers

(6) This suggestion was not followed, but on February 25 the Presidium did hand over to the Government the result of its investigation of income developments by categories, viz. various groups of workers' and entrepreneurial incomes in industry and agriculture. However, in its accompanying comments it warned that the figures were not particularly suitable as a guide for deciding which groups should have increases, since, it was pointed out, shifts as between the groups served to optimize the allocation of resources and thereby the increase in productivity.

(7) "Helhedsløsning" became the term used to denote this simultaneous settlement of a number of political issues. I do not know how it should be translated. I suggest "universal settlement", "overall settlement", "total settlement". None of these is satisfactory. As a technical term I shall use "package deal".

(8) Cf. CARL IVERSEN, "Koordinierung der für die Wirtschaftspolitik entscheidenden Kräfte in Dänemark, *Weltwirtschaftliches Archiv*, 1963, vol. II, heft I.

stood firm in their refusal to consider essential rises in wage costs. The Government, heavily dependent on the labour vote (the Social Democratic party is the major coalition party), was in a very difficult position, for the gulf between the claims of the unions and the maximum concessions these could expect to obtain from the employers was so great that the unions would lose face if they had to yield to the extent necessary to avoid a major conflict that in any case could probably only end in their defeat.

The Presidium's report strengthened the position of the employers, because it brought out clearly that no basis existed for a rise in wages. The suggestion in the report that rising wages for the lowest paid groups might be justified was met by the claim, based on experience, that the wage structure could not be changed arbitrarily. An increase for the low-wage groups would gradually spill over across the whole labour market, and any general increase would encroach upon profit margins to such an extent that unemployment would result.

In this situation the Government prepared a scheme for a settlement based on the idea of a "package deal". Its content was as follows: a lump sum was fixed for wage increases not exceeding a certain maximum, which was to be distributed by negotiations between the organizations, the sliding scale clause was to remain in force but taxes were to be removed from the index used for the scale, and certain fringe benefits were to be granted and their cost borne equally by workers and employers. These benefits would mean an addition of about  $1\frac{1}{2}$  per cent to the whole wage bill, but it was to be distributed so as to increase a low-paid group of wages by 4-5 per cent (the actual increase of average earnings of industrial workers for the year 1963 has been estimated at some 8 per cent,  $2\frac{1}{2}$  of which is due to the sliding scale clause). For the year 1964 fixed general rises were to be given universally. Strikes and lock-outs were prohibited for this two-year period. Other Bills provided for similarly limited increases in the wages of the lower-paid groups of government workers (actually wages of officials and civil servants have risen by about the same percentage as those of industrial workers) and for increases in old age and disablement pensions.

For the alleged purpose of preventing an increase in profit margins and of securing equitable treatment of workers and entrepreneurs, corporations were forbidden to distribute dividends in excess of the average for the preceding three years.

Another Bill established that no firm could raise its prices or increase its gross profit margin unless it could prove that the purchase price of supplies and other current expenses had risen. Wage cost above the rates fixed in the labour law were not to be included in costs. This "price freeze" Act was to be only temporary and was to be replaced by an Act granting power to the Monopoly Inspection to extend its activity to any section of the economy when it was suspected that competition was not sufficiently effective. It was empowered to impose a temporary price freeze and permanent price ceilings if it saw fit to do so.

Rent control, which some years earlier had been lifted as far as new houses were concerned, was again made universal.

In addition to these measures, aimed directly against "primary" incomes, fiscal restrictions were stiffened in so far as a tax remission that was due to come into force in the spring was neutralized by other fiscal measures.

The scheme was approved by the trade unions, but opposed by the Employers' Association. It was brought before Parliament and adopted by the votes of the governing coalition parties only.

The Prime Minister maintained that this "package deal" was "socially balanced", and the representative of the minor coalition party, the Radicals, hailed the package of Bills as the initiation of a new era in which the idea of co-ordination of interests originally introduced by his party had been realized (9).

#### (d) *The effect*

It is impossible on the basis of experience to say anything up to the time of writing about the effect of these measures. The balance of payments improved greatly from the beginning of and during 1963; a considerable surplus, in fact, developed, especially during the second half of the year. Employment has remained high, although the pressure on the labour market has been somewhat relieved. Thus it could be said that the two objectives, viz.

(9) The same view is held by the Chairman of the Presidium, for in the article referred to above he comments: "The unified settlement (Gesamtlösung) introduced something fundamentally new into Danish economic legislation, for never before had interference in the formation of incomes been undertaken, with the fixing of a definite limit for the development of the entire money income in order to establish a suitable equilibrium between the rise in money income and the development of total production".

equilibrium in the balance of payments and full employment have been realized (but not the programme that money income should increase in step with the rise in production only, for income has increased practically at the same rate as in the preceding year and far in excess of production). This — as I feel it — satisfactory development could easily be explained by the fiscal policy introduced in the summer of 1962 and favourable harvest and export conditions, in conjunction with continued high prosperity in all industrial countries.

If, on the other hand, we try to appraise the set of measures which made up the package, I feel that on a logical basis three questions emerge: (a) what would have happened if the Government had allowed the conflict on the labour market to follow its own course?; (b) what are the merits or demerits of the individual measures in the package?; and (c) in what respect, if any, could they be regarded as a co-ordinated whole? All questions should of course be answered in the light of the established targets: full employment and equilibrium in the balance of payments with fixed exchange rates.

As to (a), my own view is that the rise in wages would have been no greater than has actually been the case. The report of the Council no doubt hardened the attitude of the Employers' Association, but if the trade unions had offered to settle for something equivalent to what they finally got, a settlement might have been obtained — with or without a work stoppage. In no circumstances would the final rise in wages have been greater.

As to (b), there seems to be a fair consensus of opinion among businessmen that on the whole the law on the price freeze was ignored, and no attempt of any importance was made by the authorities to enforce it. The fact that business conditions at the time of the settlement were such that in general there was no incentive to raise prices or profit margins makes it very unlikely that there would have been any greater rise in prices in the absence of the "price freeze". It has been claimed that the measure has served to stiffen the resistance of employers towards the so-called "wage drift"; but in spite of the fact that the labour market has been less tight than in the preceding year the rise in earnings has been considerably greater than that envisaged in the settlement.

The freezing of dividends was without any significance from an immediate social-economic view, as incorporated business is of relatively small importance in Denmark. As a permanent or recur-

rent measure it would certainly be detrimental to incorporated business.

The extension of rent control will serve to disorganize still further the market for dwellings and increase the waste of resources which rent control implies.

The subsidies to agriculture would have been continued unchanged in any case, as no fundamental change in the agricultural situation had taken place.

The question of an increase in social security benefit would not have come up at the time, but it is in any case a matter of pure redistribution of income and has no bearing on the problem of economic equilibrium.

The fiscal measures taken have proved to be justified in so far as the labour market, contrary to expectations, has remained fairly tight. But it might well have been replaced by other and more rational measures.

As to (c), only the interference in wage settlement and the fiscal measures have any logical connection in relation to the problem of maintaining equilibrium in the balance of payments and full employment. The other links have no bearing on the problems and could have been left out or changed in any manner, and the effects as far as the balance of payments and employment are concerned could have been neutralized by a suitable change in the combination of the two first mentioned instruments.

In speaking of a "total", "universal" or "co-ordinated" settlement emphasis, therefore, must be placed on the "social balance" of which the Prime Minister was speaking. The increase in social security benefit, the tightening up of rent control, and the intervention regarding prices, dividends, etc., although they hardly benefited the workers and were mainly of an ostentatious character, must be considered as tactical measures to secure the political support of the trade union membership which was absolutely necessary to the existence of the Government.

#### (e) *The ex post discussion*

There has been an extensive discussion of the significance of the settlement. We have seen that the Chairman of the Presidium, Professor Carl Iversen, in a lecture delivered in Kiel in June 1963, considered it to be the inauguration of a new era in Danish economic

policy, viz. the simultaneous fixing by government intervention of all sorts of income for a future period so as to maintain the relation between money and real income approximately unchanged (or to control it in some definite way). Instead of the usual "monetary policy" an "incomes policy" had been introduced.

Some politicians have shared this view, but others have emphasized that the "deal" did not constitute a precedent. The economists, too, have been divided in their views. Most Danish economists argue that entrepreneurial income could not be determined in any definite way by fixing prices, that an attempt to do so would be incompatible with a market economy, and that the settlement of all kinds of political problems in one package every time a wage settlement has to be made is neither necessary nor expedient for realizing the goal of maintaining a fixed exchange rate and a high and stable level of employment. It is also doubted that a general wage settlement involves the problem of the distribution of income. This latter problem can be solved by expenditure and taxation laws regardless of the movement of wages and other primary incomes.

Gradually and in keeping with trends elsewhere the discussion is being carried on under the heading: "Incomes policy". This fashion has its origin in the experience that during the postwar period a high level of employment has been correlated with an ever-rising price level, which has caused much anxiety.

In 1961 (10) a committee of well-known economists reported to the OEEC on this problem, and reached the conclusion that the price level and the level of employment could be stabilized by the control of total demand by means of credit and fiscal policy supplemented by some form of wage control, whereas they did not consider it necessary to interfere with prices of individual commodities except by means of monopoly control. They did not believe in the theory of "income-race", for they held that entrepreneurial income was determined by market conditions.

However, the representatives of labour in the OECD maintained that the report was biased against labour, and a working party of government officials was appointed to investigate the matter and reach a conclusion more acceptable to the labour representatives. This new committee reported in 1963 and found that a policy for the attainment of full employment and a stable price level, if it

(10) *The problem of rising prices*, published by the OEEC.

were to be equitable, involved a control of the incomes of all groups (11).

I know that the Council has studied this report and the general subject of "incomes policy" most thoroughly. Some clue to the thinking of the Presidium could be gathered from an article by one of its members, Professor Erik Hoffmeyer (12).

He defines incomes policy as "the measures which may be applied to influence wage and price rises at a given level of employment and a given increase in production". And he adds: "Thus incomes policy comprises wage and labour market policy, price and monopoly control plus a policy of control of the industrial structure". (To me it is not evident that what is said in the conclusion follows from the definition. For if employment and the increase in productivity are given, prices will be unequivocally determined by wage rates; any deviation from such relationship dictated by employment and technical "know-how" — both of which Professor Hoffmeyer considers fixed — will be impossible under these assumptions. Therefore, if the desire is to control prices in any definite way, it is sufficient to control money wages.)

Professor Hoffmeyer further holds that all these interventions must take place simultaneously. The reason given for this is that the various income groups must be taught to see the problems as an integrated whole; this, he thinks, would change their behaviour. The simultaneity, therefore, is not only one of tactics, but is of importance for the efficiency of the measures adopted.

As I have submitted above, there is only one problem, viz. the control of wages, and therefore no question of simultaneity of measures. But it must be admitted that it would be very important if people could be made to realize this. However, the author does not contribute to this enlightenment.

After having concluded that incomes policy as defined above implies direct public intervention in prices and technical conditions, Professor Hoffmeyer proceeds to deal with the problem of realizing such a policy. He starts by summarizing the immediate objectives:

(a) The rise in incomes must not be allowed to exceed productivity;

(11) *Policies for price stability*, published by OECD.

(12) *Nationaløkonomisk Tidsskrift*, 1964.

(b) the market economy must be kept intact, because it is of importance for productivity; and

(c) social tension created by large and abrupt shifts in income distribution must be avoided.

I fail to see how (b) and (c) could be called objectives of an incomes policy; to me they seem to be restraints on the means that may be used for realizing (a) (13).

In the subsequent discussion of the possibility of carrying out an incomes policy, comprising a direct intervention in all sorts of incomes and in the structure of industry, he does, in fact, conclude that direct intervention in the market mechanism (apart from monopoly control, which is assumed to be a permanent feature of the system) is ruled out by condition (b).

He does think, however, that entrepreneurial incomes must be included in the incomes policy and, as a means of achieving this, he mentions liberalization of imports and monopoly control. But as far as I can see they may be considered part of the framework within which control of incomes in accordance with (a) and subject to the restraint (b) is taking place.

Next he mentions as a means the compilation of income statistics, making it possible for the workers to ascertain that restraint in income demands on their part does not lead to a reduced share of total income; but this seems to me quite unnecessary, for if there is equilibrium in the balance of payments and full employment, this share must be determined by the market mechanism plus the monopoly control.

Further, Professor Hoffmeyer mentions improved statistics on incomes and capital ownership for the purpose of ascertaining that no undesirable shifts in income and capital distribution take place. Should these occur, then changes in income and capital taxation should, he thinks, be effected to correct them. However, I fail to see that this has anything to do with (a) or with the incomes policy as he defines it (cf. p. 20).

It seems to me, therefore, that his discussion of the ways and means to carry on an incomes policy as he defines this term boils down to some form of wage control as the only necessary and sufficient means to realize the policy in question.

(13) The condition (c) has however nothing to do with the problem under (a) and could be left out.

### Has the "Incomes Policy" Problem been solved in Denmark?

I could have left it to the reader to find his own answer to this question on the basis of the account and analysis given above. However, a brief summary of my own views on the significance of the establishment of the Council for Economic Co-ordination may be of some interest. Here they are:

(1) On the basis of experience so far, I think that the Council will be of considerable importance as an instrument for tactical manoeuvring for the political parties, the labour market organizations and perhaps other pressure groups, particularly agricultural organizations. It is beyond any doubt that the Government skilfully exploited its possibilities in this respect in the winter of 1962-1963. Even if the Government could have put together a similar package of Bills without the statements of the Presidium, such statements did strengthen the position of the Government, especially in view of the fact that the report of December 18 was received with approval by the opposition parties as well.

As we have seen also the attitude of the Employers' Association was stiffened.

The fact that the Presidium has declared its intention of dealing with any economic problem offers the various groups wide scope to exploit its statements for their own specific purposes.

(2) With respect to the problem for the solution of which the Council was specifically established, viz. to find ways and means of avoiding the current exchange crises without returning to the doldrums of too low a level of employment, the outlook is not encouraging because the Presidium's philosophy is too muddled on this question to be able to analyse the issues and thus enlighten the public.

It would not be desirable that the "package deal", model 1963, should be made a recurring feature. But even if the Presidium had a clearer view of this fundamental problem, the present structure of the Council is an obstacle. Much would be gained if the Council statements and reports were made as a unity, for this would stimulate the interest of the members forcing them to commit themselves and argue their case not only during discussions within the Council, but also in public if a unanimous report was not achieved. In my opinion it cannot be doubted that reports and statements of that kind

would offer far greater prospects of sensible proposals, and carry much greater weight in their practical execution.

(3) In any case, it can be concluded that we have not found any solution of the "incomes policy" problem in Denmark. Perhaps it is not so important that one should be found. For after all, we know from experience that a number of countries have maintained very high levels of employment without any formal incomes policy. Inflation has been rife, it is true, but the people have prospered; and that, I submit, is the supreme goal.

*Aarhus*

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