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**POLICIES FOR LABOR MARKET ADJUSTMENT
IN SWEDEN**

by
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POLICIES FOR LABOR MARKET ADJUSTMENT IN SWEDEN

I Introduction - the Swedish model

Labor market adjustment to structural changes in the economy can, basically, take place in two ways. As long as the speed of structural change is moderate, reallocation between the declining and expanding sectors of the economy can proceed spontaneously in a rather unproblematic way. The new generations entering the labor force will probably be attracted in the first place by the most profitable sectors and firms where the career prospects are likely to be best. For the same reason some voluntary mobility of labor can take place between firms and sectors of the economy. The wage differentials between the sectors can be expected to be crucial for the strength of these mechanisms.

However, in practice all structural changes cannot be realized in this harmonious way. The changes are often so drastic that plants have to be closed rather quickly or at least many workers have to be laid off. In those cases the problems for laid-off workers become more severe. Policies to support their search for new jobs with reasonable pay might be called for.

One typical feature of the Swedish approach to labor market adjustment is that several policies to help laid-off workers have been implemented by the government, whereas the incentives to move spontaneously between firms, stimulated by wage differentials, have been deliberately reduced by the wage policy followed by the trade unions.

To understand this - perhaps contradictory - approach it is important to put both wage policy and adjustment policies for laid-off workers into perspective.

Labor market policies in general and policies for structural adjustment in particular, constitute one important part of the Swedish model for economic policy. This model can be seen as an integrated approach to (i) stabilization policy, (ii) structural policy and (iii) distributional policy. Furthermore, the model gives active roles not only to the government but also to the trade unions. The model was also formulated during the late forties and early fifties by two trade union economists (Gösta Rehn and Rudolf Meidner) whose names are associated with the policy model.

The active role given to the trade unions is not surprising in a Swedish context. First, a large fraction of Swedish wage earners have for a long time been members of trade unions; during 1984 about 80-85 percent were members of a union. The trade unions in turn have been few¹ and wage negotiations and wage setting have been centralized to a great extent. Second, LO, the dominant trade union for blue-collar workers within Swedish industry, has always been strongly connected with the Social Democratic Party, which has been in power continuously since the 1930s with the exception of the 1976-82 period. Hence, the model is to a great extent a political program for the Swedish labor movement. However, during the six years with bourgeois governments the same policies were basically continued. Therefore, a great deal of consensus about the model has prevailed in Sweden during the last two or three decades.

Leaving issues about stabilization policy aside and concentrating on structural and distributional policy, there are three basic ingredients of the model.

The first ingredient is a certain wage policy which is implemented by the trade unions in their negotiations with the employers

¹ There are basically three important trade unions in the Swedish labor market: (1) Landsorganisationen (LO) which dominates among blue-collar workers, (2) Tjänstemännens Centralorganisation (TCO) which dominates among white-collar workers without university degree, and (3) SACO/SR which dominates among employees with university degrees.

federation. The wage policy was labeled "solidaristic" and has in most official documents been described by the phrase "equal pay for equal work". This means that all wage differentials motivated by differences in profits or "wage-paying-ability" between regions, industries or firms should be removed. In this way a relatively hard pressure is put on the declining industries since wage levels below the average are not accepted in these industries. As a consequence capital will be scrapped rather quickly in this part of the economy. On the other hand, the profitable and hence in general the expanding sectors of the economy will benefit from lower wages than would have prevailed with another wage policy.

A characteristic feature of this part of the model is that structural change is enhanced by putting pressure - via higher wage costs - on the declining industries and by stimulating the expanding ones via relatively low wages. In this way the overall growth of the economy would be stimulated. This was one of the main motives with the model besides the distributional goals which are achieved when the wage structure is equalized.

Another characteristic feature is that a strong burden of adjustment is put on the labor force in the declining sectors of the economy. A "smooth" reallocation of labor stimulated by changing relative wages could not be accepted. This alternative was mainly rejected for distributional reasons. However, it was also strongly argued by the trade union economists that mobility decisions are not very sensitive to wage differentials. Therefore flexible relative wages were also considered as an inefficient means of reallocating labor.

Instead a variety of labor market policies were suggested to take care of those who became unemployed in the retarding sectors. These constitute the second part of the model. The most important policies which have been implemented are retraining, mobility grants and labor market information provided by employment exchange offices all over the country. As a consequence laid off workers have had a variety of options in Sweden.

The trade union economists were aware of the risk that the adjustment policies might not be sufficient to counteract the unemployment which might be caused by the wage increases in the declining sectors of the economy. Therefore they argued that a third ingredient might be needed in the policy mix, namely selective employment policies. The purpose of these measures was to provide jobs in those regions and sectors which were most severely hit by structural problems. The need for, and design of, these policies were not specified in any detail when the model was formulated more than thirty years ago. Instead the pragmatic view was that they had to be designed when the real problems appeared.

The purpose of this paper is to summarize the experiences of this approach to economic policy. The main emphasis will be on the adjustment policies to help laidoff workers. The paper is structured in the following way. In section II the main options available to laid-off workers are presented. Section III contains a presentation of the consequences for labor market adjustment. The experiences of laid-off workers are presented in order to give a picture of the adjustment-burden. In section IV a more detailed examination of the specific programs to help laid-off workers is made.

The next section (V) describes the development of overall mobility in the labor market.

In section VI we will discuss "the political economy of adjustment policies". Has the presence of policies to help laid-off workers made it easier for the politicians to abstain from protectionistic employment policies? Has the presence of the policies affected the behavior of unions? Finally, in section VI, some problems and prospects for adjustment policies in Sweden are addressed.

II Options for a laid-off worker

Let us consider the situation for a laid-off worker. The options available for him are regulated by laws, by agreements between the unions and the employers federations and by the policies implemented by the National Labour Market Board.

Advance notification of lay-offs

Before being laid-off the worker in general has the right to be notified in advance. This right was given by "the security of employment law" from 1974.

Lay-offs are subject to a minimum of one month's notice from the employer. An employee who has worked for the same employer for a certain minimum period is entitled to a longer period of notice if he is 25 years old or more. The period of notice increases successively with the age of the employee, from two to six months. It is six months for those who are 45 years and older. This age group was given that right in a law in 1971.

The employee is entitled to his normal pay during the period of notice, even if the employer is partly or wholly unable to offer him employment. The employee also has the right to spend working time searching for new jobs without loss of pay. If the employer is unable to provide employment during the period of notice, the employee is obliged to "place himself at the disposal of the labor market", i.e. to register at the public employment service.

Not only the employee should be notified in advance. When an employer in Sweden intends to lay off more than five individuals, he is required to notify the local employment exchange office at least two months in advance. The local labor market authorities will then form a committee to help the individuals affected.

Unemployment benefits

While laid off, unemployment benefits can be obtained.¹ The main system - the unemployment insurance system - is voluntary but the majority of the wage earners in Swedish industry are covered. In 1980, 72 percent of all labor force participants were members of an unemployment insurance fund. The highly educated with low unemployment risks and "temporary" labor force participants account for a high proportion of the non members.

The funds are organized by industry but blue and white collar workers belong to separate ones. The share of costs covered by the membership fees has declined gradually. During the last five years the share has been less than 10 percent. The rest is covered by subsidies from the government financed by general taxes.

To be eligible for compensation, membership fees must have been paid for twelve months. Another requirement is that the recipient must have worked during five of the twelve months preceding the spell of unemployment.

The maximum period for unemployment benefits was prolonged 1974 to 60 weeks for those below 55 years of age and to 90 weeks for those above.

The replacement ratios are hard to compute exactly because of a waiting period of one week and because of the tax system. However, during the last decades the daily benefit has covered between 60 and 90 percent of forgone income before taxes for most unemployed. In general, the replacement ratio is lower for high income earners.

Because the marginal taxes are very high, a loss of 10 to 40 percent of gross income implies a quite low loss after tax. Applying

¹ See Björklund and Holmlund (1986) for a detailed presentation and discussion of unemployment benefits in Sweden.

a marginal tax of 60 per cent - a quite representative figure during the last decade - it turns out that being unemployed a whole year reduces income after taxes by approximately 10 to 20 per cent.

To receive benefits the unemployed worker is obliged to register at the employment office and search actively for new jobs. There is also a "work test". This means that an offer of a "suitable job" should be accepted, otherwise the benefit can be lost. This rule is not only a formality. During the last ten years the share of unemployed who have lost their benefits because of this rule has varied between one and three percent. It is probably enforced more generously for older than for younger unemployed.

In addition to this unemployment insurance system, which is strongly regulated by the government, the unions and the employers organizations have agreed to pay the costs for some extra benefits for workers older than 40. Both blue and white collar workers, who are laid-off after having worked for the same employer in Swedish industry for at least five years, are eligible to some extra benefits. These are partly paid as a redundancy payment which is approximately equal to one monthly salary. Taking these payments into account means that the replacement ratios are even higher for older unemployed.

These extra benefits are financed by a charge on the total payroll costs of the firms.

Those who are not eligible for compensation from the unemployment insurance funds can receive another type of benefit. This is completely financed by taxes but the benefit level is much lower. Those who have not found a job when the right to unemployment benefits has expired can obtain further compensation from the social welfare program. However, this kind of payment is strongly means-tested and much more stigmatizing than unemployment benefits.

Early retirement

Early retirement with pension for labor market reasons was introduced in 1972. To be qualified, the individual must (i) be at least 60 years old, (ii) have received unemployment compensation during the maximum period of 90 weeks, (iii) have reduced ability to get a new job with "reasonable" qualifications. From the beginning the purpose was to provide an option for those who had not found a job when unemployment benefits expires. However, during the last years the rules have in practice been interpreted more generously. As a consequence the decision to retire has often been made before the decision to lay off.

A firm, which needs to reduce its work force, has been able to "offer" its older employees a period of lay off with unemployment benefits for 90 weeks and thereafter a pension. In those cases the laid-off have very seldom been offered a job by the employment office during the period when unemployment compensation has been received.

During the last five years - and in particular during the recession 1981-83 - early retirement has become a very common tool for firms which need to lay off personnel. The older workers have often voluntarily abstained from their seniority rights when the firm is contemplating lay-offs.

The reason for the attractiveness of early retirement for the firm is that all costs are paid by the government. The replacement ratio for the individual is equivalent to the one obtained from the unemployment compensation system during the first 90 weeks. From then on and until the regular age of retirement, which in general is 65 years, the replacement rate depends on the pension rights of the individual. After taxes the rate is between 70 and 85 percent for most workers.

In addition to this compensation - which is completely provided by the government - the firms sometimes pay some additional compensation. Among white-collar workers some additional opportunities for early retirement exist.

Mobility grants

Mobility costs might be an important deterrent for many laid-off workers when searching for a new job. One ambition in Swedish labor market policy has been to remove this obstacle for adjustment.

To be eligible for any type of mobility grant one must - with some minor exceptions - either be unemployed or in danger of becoming unemployed. Furthermore, one has to be registered at the employment office.

Various types of mobility costs can be paid by the labor market authorities. First, the travelling costs to visit employers at other places can be covered. Second, those who decide to move and accept a job in another region can receive grants which cover the costs to move plus a separate amount as a pure stimulus to move.

The latter stimulus can be regarded as a compensation for the non-monetary costs of moving. It was introduced in 1959 and was increased gradually during the sixties. On July 1, 1984, the size of the stimulus was increased to 15,000 SEK (approximately 1,800 \$) for households and 4,000 SEK (approximately 500 \$) for single persons. All the grants are tax-free.¹ Consequently they are equivalent to quite a high increase of gross income.

Retraining

Of all policies available for laid-off workers most expenditures have been spent on retraining.

¹ Until 1982 the grants were taxable. See below in Section IV.

The capacity to retrain unemployed workers was increased during the sixties and early seventies. During the last decade approximately 1 % of labor force has participated in this type of government supported retraining. Because the retraining courses last slightly less than half a year, more than 2 % of labor force participate during a year. Therefore, the retraining system has become an important part of the educational system and is well-known for most Swedes.

The eligibility criterion is the same as for mobility grants, namely being or running the risk of becoming unemployed. However, if the applicants for a course exceed the capacity, the access to retraining must be restricted. In general though, laid-off workers who need retraining in order to get new jobs with reasonable pay have had good access to retraining courses during the last decade.

The participants receive a stipend during retraining. Those who are eligible for unemployment insurance benefits receive the equivalent amount during retraining, whereas others receive a lower amount.

Employment exchange offices

During the last decades the expenditures spent on labor market information, i.e. mostly on the employment exchange offices, have increased almost twice as fast as GNP.¹ It is also obvious from the presentation of the policy measures above that the employment exchange offices play a central role in Sweden. The offices are notified in advance when lay-offs are planned; the unemployed are obliged to search actively via the offices; the work test is enforced by the offices; most labor market policy measures for unemployed are implemented by the offices. Further-

¹ The development of labor market policy during the last decades is described in Johannesson (1981) and EFA (1985).

more, since the seventies, it is compulsory for firms to inform the exchange offices of all new vacancies. By visiting an office one can easily get an overall view of all available vacancies in the country.

On the other hand, there hardly exist any alternatives to the official exchange offices. Private alternatives run with a commercial motive are prohibited by law. The only exception of some importance is an institution - The Employment Security Council (Trygghetsrådet) - established by the employers federation (SAF) and the union for white collar workers in private industry (PTK) in 1974.

This council is a complement to the policies administered by the National Labor Market Board. It can help white collar workers threatened by lay-offs in several ways. As mentioned above, some additional benefits for unemployed and those who retire in advance can be paid. In addition the council can help with the adjustment needed to get a new job. If the necessary retraining cannot be obtained by courses provided by the National Labor Market Board the foregone income can be covered. Mobility costs which prevent adjustment can be paid by the council. Recently the council has also started to help those who want to start their own business. Special courses in "How to start your own business" have been given and financial help has been given to those who want to try.

Summarizing this section we can conclude that several policies to help laid-off workers have been implemented in Sweden during the last decades.

An "early warning system" was introduced in the early seventies to give both the individual and the local labor authorities some time to find a solution to the adjustment problem before the lay-off takes place. The expenditures on employment exchange offices, on mobility grants and on retraining courses have been increased to help the laid-off workers to get new jobs.

In addition, the monetary losses of unemployment are reduced by an unemployment insurance system which provides rather high replacement ratios. The maximum periods during which unemployment compensation can be received were extended 1974 to 60 weeks for young and prime-aged and to 90 weeks for older workers.

In the early seventies the government also introduced the opportunity for older unemployed to retire with pension before the regular age of retirement.

III Labor market adjustment for laid-off workers

The labor market adjustment for laid-off workers can be analyzed in two steps. First, what are the chances of getting a new job within a certain period of time? Second, conditional upon getting a job, how high is the wage in the new job compared with the old one? In this section we will summarize the available evidence on these issues.

The ability to get a new job varies a lot between the sexes, age-groups, regions and over time. Table 1 displays the distribution on labor market states for laid-off workers after about five months. Breakdowns are done by sex and age.

Several interesting patterns emerge from the table. The percentage of workers who have received a new job is 51.1, slightly higher for men and lower for women. The age pattern is very striking; the ability to get a new job falls drastically with age. This is partly explained by a higher willingness to move on the part of younger workers.

There is a very marked decline in the share who has obtained a new job at the age of 60. The mirror image of the low employment figures for older age group is higher shares of unemployed and retired with pension. This probably reflects the opportunity to get early retirement with pension for those above 60.

Table 1 The labor market status of laid-off workers after about five months during 1974-80 (percent)

	All men and women	Men -24 years	25-44	45-49	50-54	55-59	60-66	All men
1. Obtained a new job	51.1	62.8	68.0	63.8	59.1	48.8	16.8	58.0
1a At the same place of resi- dence	40.6	46.9	50.3	51.9	45.0	43.7	15.5	44.6
1b At another place of resi- dence	10.5	15.9	17.7	11.9	14.1	5.1	1.3	13.4
2. Retraining course	9.6	13.1	11.5	6.3	2.8	1.6	0.1	8.2
3. Relief work and shel- tered employment	3.2	2.2	1.5	3.4	4.0	5.1	2.5	2.5
4. Retired with pen- sion	2.7	0.2	0.0	0.2	2.6	2.1	18.8	2.7
5. Sick	3.8	1.0	1.8	3.9	5.5	7.3	9.7	3.6
6. Unemployed	19.8	6.1	7.9	14.5	18.2	30.6	47.4	16.0
7. Others	9.7	14.7	9.3	8.0	7.9	4.4	4.6	9.0

Source: Edin (1984).

Table 1 Cont.

	Women						All women
	-24 years	25-44	45-49	50-54	55-59	60-66	
1. Obtained a new job	45.7	49.3	46.2	33.3	24.1	8.9	40.8
1a At the same place of residence	36.5	42.4	38.6	28.1	23.1	8.6	34.7
1b At another place of residence	9.2	6.9	7.6	5.2	1.0	0.3	6.1
2. Retraining course	16.1	15.6	10.4	6.6	3.9	0.0	11.8
3. Relief work and sheltered employment	7.1	2.4	2.6	7.8	8.2	3.2	4.5
4. Retired with pension	0.0	0.2	1.0	0.8	4.6	23.6	2.7
5. Sick	2.3	2.9	2.1	5.2	6.1	6.1	4.0
6. Unemployed	15.7	16.0	31.1	35.7	45.3	52.9	25.5
7. Others	13.0	12.7	6.5	10.5	7.8	5.4	10.8

Source: Edin (1984).

Retraining in the government sponsored courses has attracted 9.6 percent of the laid-off. Here too, there is a striking age pattern. The willingness to retrain declines with age.

The changes over time in labor market adjustment are illustrated in Table 2. A trendwise decline in the percentage with a new job can be noted. This development is partly counteracted by more retraining. The share of laid-off workers participating in the retraining courses increased from 5.0 percent during 1966-70 to 9.4 percent 1976-80. Still the table reveals a pattern of declining ability to adjust to structural changes in the labor market.

Some econometric studies of the determinants of the labor market adjustment after lay-offs have been done. (See Edin, 1984, and Heikensten, 1984.) In particular, the percentage with a new job some months after a firm closure has been regressed on potential determinants like: cyclical activity, the size of the closed plant compared with the local labor market, the fraction of white collar workers, the fraction of older workers and a time trend.

The results indicate that: (i) the fraction with a new job is strongly cyclically sensitive, (ii) the propensity to migrate is much higher during upswings too, (iii) the probability of getting a new job is lower the bigger the former plant is and higher for white collar workers and for young workers.

After controlling for these variables there remains a negative trend indicating increasing problems for laid-off workers to adjust in the Swedish labor market. This trend has appeared in spite of increasing expenditures on adjustment policies and new laws to help laid-off workers.

The second dimension of the adjustment problem is the subsequent wage path conditional upon getting a new job.

Table 2 The labor market status for laid-off workers after about five months during 1966-70, 1971-75 and 1976-80, respectively (percent)

	1966-70	1971-75	1976-80
1. Obtained a new job	66.9	58.0	50.4
2. Retraining course	5.0	7.6	9.4
3. Relief work and sheltered employment	3.7	2.2	3.2
4. Retired with pension	2.8	2.0	3.7
5. Sick	4.3	3.8	4.1
6. Unemployed	12.4	21.0	20.2
7. Others	4.9	5.4	9.0

Source: Edin (1984).

The effect of unemployment experience on subsequent wages has been analyzed by Björklund (1981) using panel data and econometric techniques. In this study a distinction is made between "occurrence-" and "duration-effects" of unemployment on subsequent wages. By occurrence-effect is meant a once-and-for-all loss of human capital when unemployment occurs. This can happen if there is a loss of firm-specific human capital. By duration-effect is meant an effect which is higher the longer the person has been unemployed. It can be due to the absence of on-the-job training.

The tests show some evidence of the the latter type of effect, even though the precision is rather low. However, these results were obtained for all types of unemployment whereof only a small fraction (probably about 20 percent) is attributable to lay-offs. Therefore the results do not necessarily hold for laid-off individuals. It is also likely that many laid-off individuals can suffer from deleterious effects on the subsequent wage even though they obtained a new job without intervening unemployment.

In addition to this piece of evidence a couple of case studies of plant closures give some insight into the problem. Those who had obtained a new job were asked about the wage compared to the one in the earlier job. The pattern from these studies is that the fraction with lower wage slightly exceeds the fraction with higher wage.

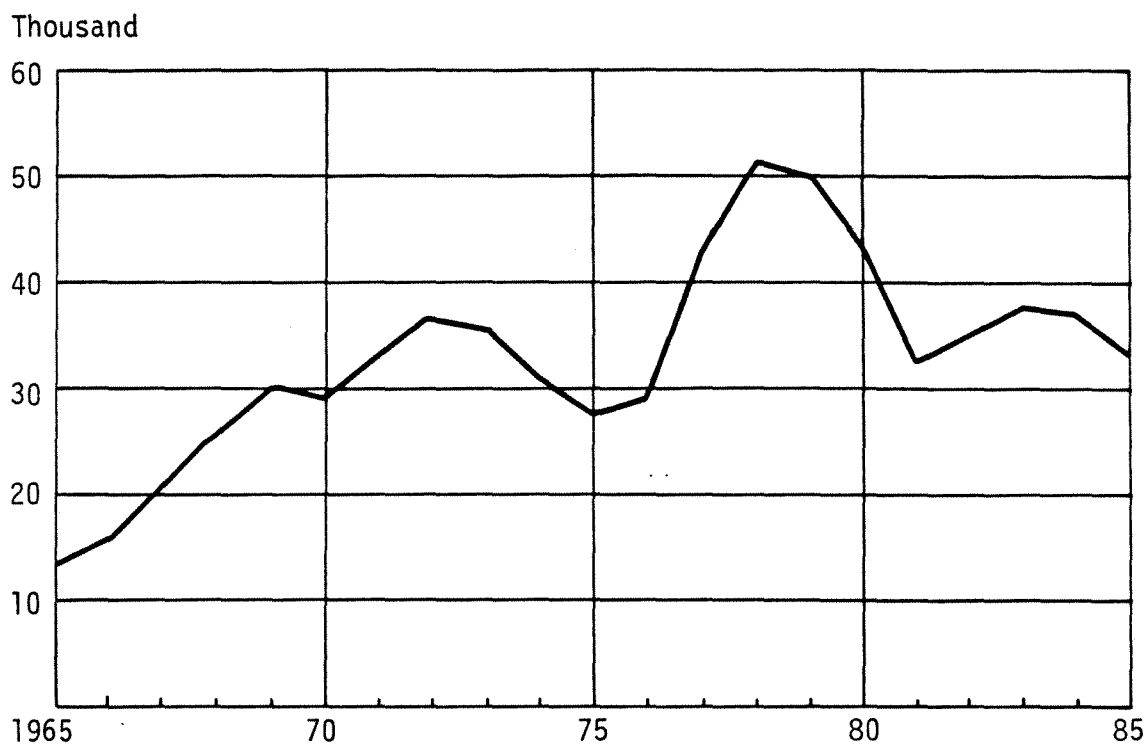
The general impression from these studies is consequently that there exist some wage losses too, even though the nature and size of these losses cannot be estimated with high precision.

IV Experiences of specific programs

IV a Retraining

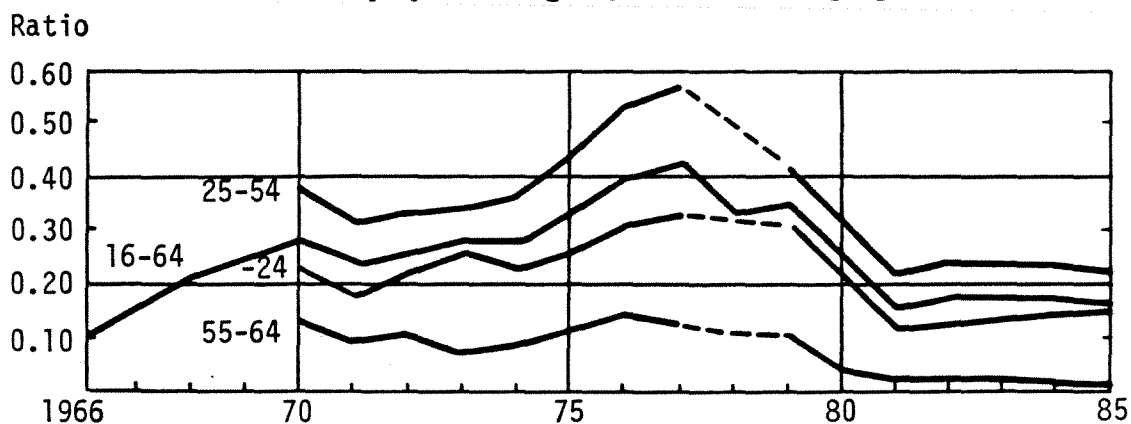
Retraining has become one of the most important measures in Swedish labor market policy, both in terms of persons involved

Figure 1 a The number of participants in labor market training 1965-85



Source: National Labor Market Board.

Figure 1 b The trainees during a year as a fraction of the unemployed during a year, various age-groups



Source: National Labor Market Board, Statistics Sweden.

and expenditures. The quantitative development is displayed in Figures 1 a and 1 b.

The average number of participants in labor market retraining increased during the sixties and the seventies (see Figure 1 a). During the late seventies the number of trainees amounted to 1.2 percent of the labor force. From then onwards the number has declined.

In Figure 1 b the total number of trainees during a whole year is related to the total number of unemployed during a year. It appears that the decline during the last years is not age specific but can be found for all age groups.

The main ambition of the retraining system is to provide the unemployed with vocational qualifications which make it possible to obtain employment. Sometimes some general preparatory training might be needed to follow an occupational training course. Such preparatory training can be given too.

The system as a whole provides courses for occupations in all sectors of the economy. Most of the courses are given by special centres - "Labor Market Training Centres" - which were established during the sixties and early seventies. The regular school system has been used too. However, since 1980 this possibility has been restricted, in order to increase the capacity utilization in the Labor Market Training Centres. This is one of the reasons for the declining number of trainees displayed in the figures above.

It is important to emphasize that the retraining courses are not only designed for "dislocated" workers, i.e. those whose skills have become obsolete because of structural changes in the economy. They also aim at providing skills for "disadvantaged groups", such as the handicapped and immigrants. During the last decade around 20 percent of all trainees have been handicapped and immigrants respectively. Although hard to verify with statistics, it is a general opinion that "disadvantaged groups" have become more important among the participants compared to "dislocated workers".

Early cost-benefit studies

What are the experiences of this measure? Various types of evidence are available.

The most ambitious studies were done in the early seventies. All were cost-benefit studies of the individual as well as the social effects of retraining. Among benefits the main component in all studies is the earnings gain by the participants. Various methods have been used to determine the effect on post-program earnings.

The first study - Dahlberg (1972) - investigated the effects of retraining in one county during 1965. The effects on post-program earnings during 1966-70 were estimated by a comparison between two types of participants: on the one hand those who answered that the training had been useful in subsequent jobs and on the other hand those who answered that it had not been useful.¹ A significant positive effect, amounting to approximately 10 percent earnings increase was found.

In the second study Dahlström (1974) examined the effects of retraining, which was completed during 1968 in four counties. The post-program earnings of trainees were compared with those of a control group consisting of persons with a similar labor market situation when training started.² Again a positive impact of retraining of approximately the same magnitude (11 percent) was found. This study was based on a period 2.5 years after training was completed.

¹ A regression model was used to eliminate the influence of age, sex, marital status and region.

² Again regression analysis was used to control for certain dissimilarities between the groups.

The third study - Kjellman (1975) - used the same methodology as the first one mentioned above. A positive effect on subsequent earnings two years after training was found again, but only about half as big as in the other studies.

In summary, retraining has been beneficial for the individual according to all studies. However, the cost-benefit calculations for the whole economy reveal more ambiguous results. Several crucial components turn out to be very difficult to estimate. Among them are the duration of the income effect for the individual and indirect effects on other individuals in the economy. Only the direct training costs - teachers, rents etc. - can be estimated with some precision.

Dahlberg extrapolates the income effects over 20 years. With this assumption, a discount rate of 6 percent, and rather "pessimistic" assumptions about the effects on other individuals in the economy, the present value of benefits and costs is positive. With the most "realistic" assumptions about the indirect effects, the present value is very high - the equivalent internal rate of return is 44 percent.

The other researchers are more reluctant to extrapolate the income effects. Dahlström concludes that benefits exceed costs only if the income effects persist around 10 years, whereas Kjellman simply concludes that benefits do not cover the costs after three years.

In spite of the high expenditures on labor market training, no more cost-benefit studies have been done during the last decade. Probably the researchers have been discouraged by the hard work to get the data that is needed.

However, one recent study has examined the effects on subsequent wages of training (see Björklund and Moffitt, 1986). The data set is rather small and covers retraining during the period 1976-80.

A so called "self-selection model" is used, which makes it possible to test for the presence of delining marginal returns of training. This hypothesis cannot be rejected. The results display an average effect on wages for all trainees around 11 percent. On the other hand the effect for the marginal participant is negative. This indicates an excessive amount of retraining - unless the courses provide other benefits than higher hourly wages.

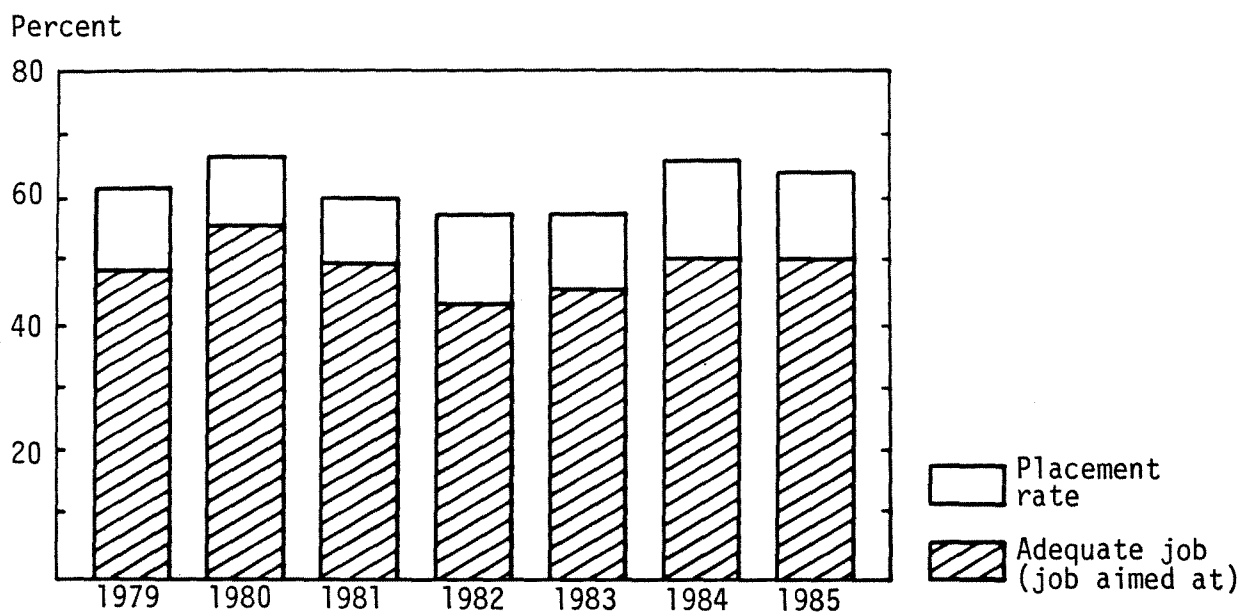
Follow-up studies and other evidence

In addition to studies like these, other types of evidence are available.

The National Labor Market Board undertake yearly follow-up studies of the participants. Even though such studies cannot tell what would have happened if retraining had not been available, they give some idea of the extent to which the aims of the courses are fulfilled.

In Figure 2 the main results from 1979-85 are presented. The differences between the individual years reflect cyclical factors. It is hard to say whether these placement rates are good or not. On the one hand it can be argued that the rates are quite good taking into account that the trainees often are hard-to-place individuals. On the other hand they are hardly at variance with the hypothesis that retraining of unemployed in Sweden is overdimensioned.

Figure 2 The percentage gainfully employed 6 months after the completion of occupational Labor Market Training 1979-1985



Finally, some more casual information about the Swedish retraining system is worth mentioning.¹ First, it has become more difficult to get unemployed workers to start retraining since the late seventies. The decline in participation displayed in the figures above is at least partly due to decreasing popularity of retraining among the unemployed. This might have several reasons. However, it seems to have caused some concern about the administrative efficiency of the retraining system. It has been argued that some of the courses do not provide the occupational skills which are needed in the most attractive occupations. This in turn indicates inadequate flexibility in the system.

Second, the break-off rates have been quite high during the last years, see Table 3.

The table reveals that the break-off rates have been slightly higher in the courses organized by the Labor Market Training Centers than in the courses provided by the regular schooling system. Again it is hard to know the reason, but one hypothesis is that the Training Centers have got a bad reputation.

¹ Most of the information presented here can be found in SOU 1983:22, a report to the government from a committee investigating vocational training.

Table 3 Break-off rates in retraining courses 1979-85

	<u>Labor market training centers</u>			<u>The regular schooling system</u>		
	Comple- tion rate	Break- off rate	Whereof obtained a job	Comple- tion rate	Break- off rate	Whereof obtained a job
1979	77	23	10	86	14	3
80	77	23	9	89	11	3
81	74	23	9	91	9	2
82	-	-	-	-	-	-
83	77	23	12	92	8	5
84	78	22	11	86	14	2
85	78	22	11	86	14	4

Source: National Labor Market Board.

IV b Mobility grants

After the mobility grants were introduced in 1959, the number of movers grew rapidly to about 20,000 per year in 1964. From then on the number has stayed approximately at that level with some cyclical variations (see Figure 3.)

In order to describe the propensity of the unemployed to use the mobility grants, these numbers must be related both to the number of eligible individuals and to the size of grants.

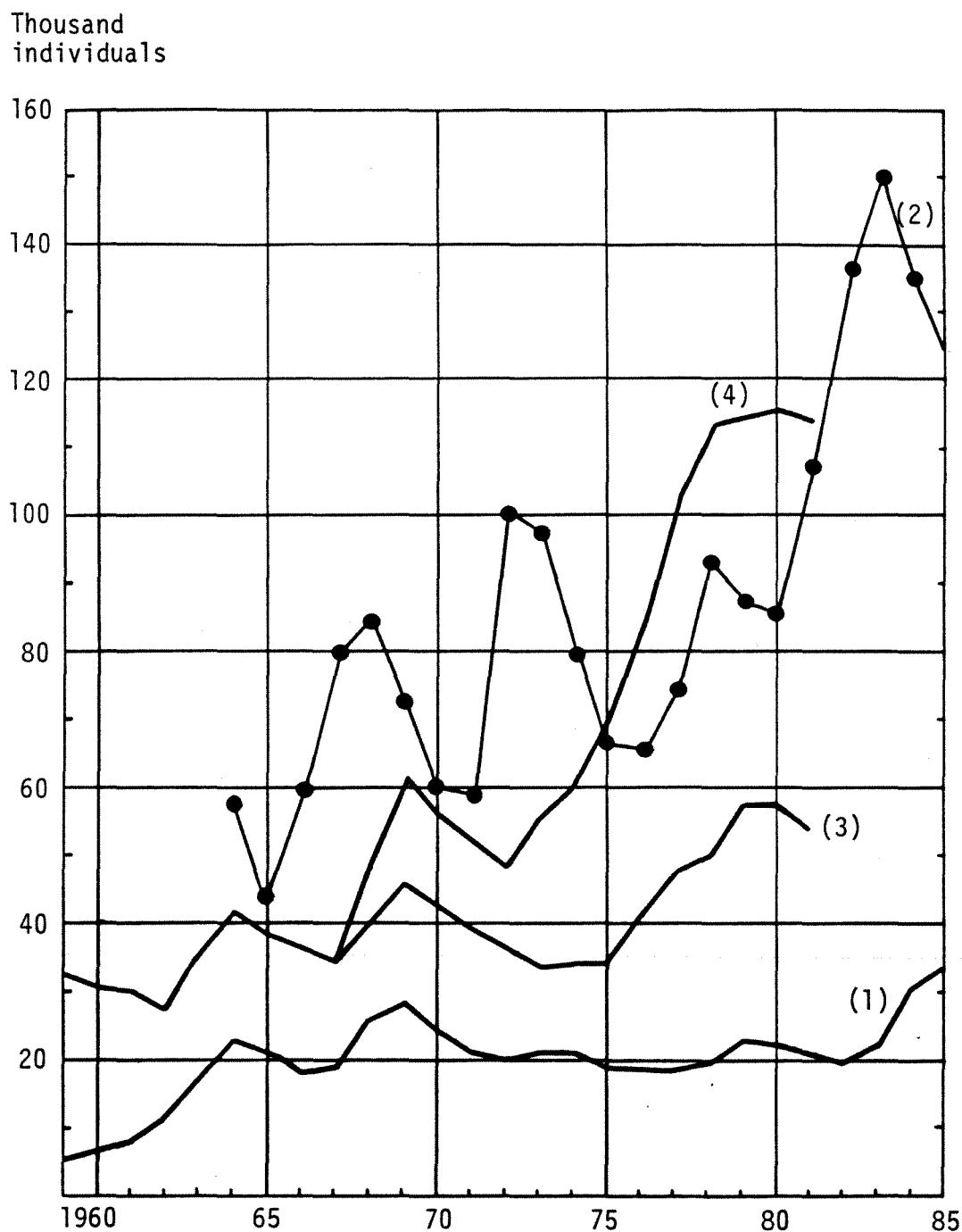
With some minor exceptions eligibility requires unemployment or risk of becoming unemployed. A crude measure of the number of eligible is the average number of unemployed in the economy. As seen in the figure this number has increased, which indicates a declining propensity to be attracted by these grants. This tendency is reinforced by the fact that the grant has been increased gradually (see Figure 3 again).

The declining mobility is disaggregated by age in Figure 4. It appears that there is an absolute decline only for older workers. However, in relation to the number of unemployed there is a decline for all age-groups.

One more ambitious evaluation study of the mobility grants has been done (see Dahlberg (1978, a and b)). The population analyzed was movers with mobility grants from a couple of northern regions in the country in 1969-70. As illustrated in the figures above, the number of movers reached a peak during these years.

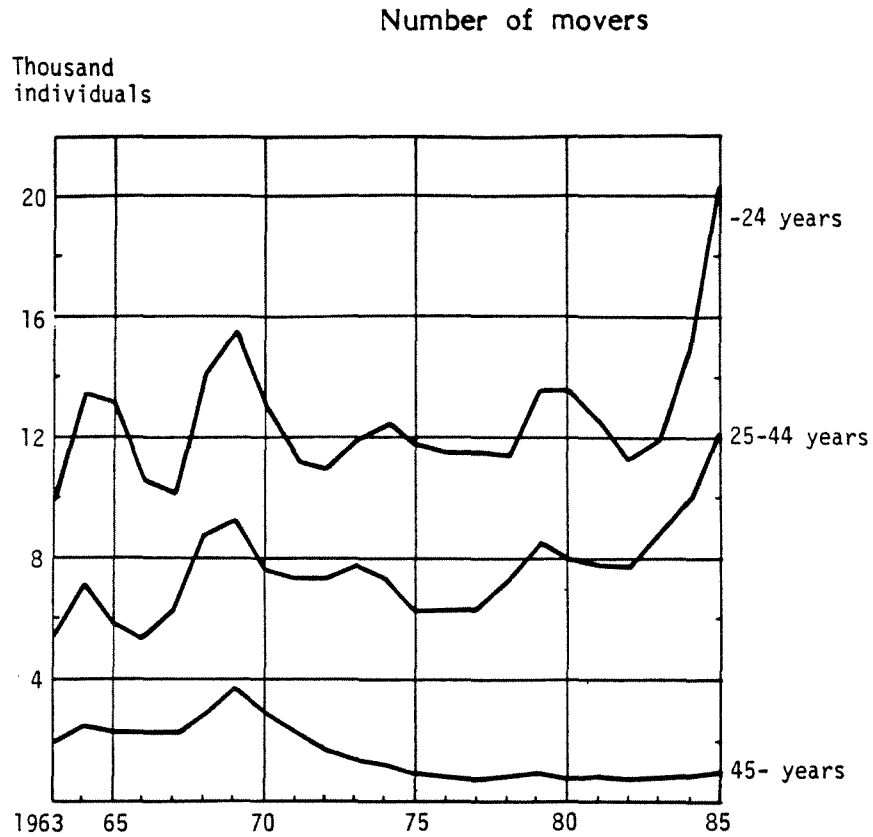
The effects of mobility on employment and income for the movers were estimated by comparison with a control group of stayers. Several control groups were used but most conclusions were drawn from comparisons with a control group of individuals with the same type of unemployment risks as the movers. Additional differences between the movers and the control group were controlled for by means of regression analysis.

Figure 3 The yearly number of movers with mobility grants (1), the number of unemployed (2), the size of the mobility grant for individuals (3) and for families (4) net after taxes, fixed prices



Source: The labor force surveys (Statistics Sweden) and own calculations.

Figure 4 Number of movers with mobility grants and ratio of movers and unemployed for different age groups



Source: The labor force surveys (Statistics Sweden) and own calculations.

The results showed that the movers gained both in terms of income and employment, though most of the gains had disappeared after five years. When the mobility costs - the direct costs for moving, higher costs of living etc, net of the grants - were taken into account, the moving individuals and households had actually made a loss.

For the society as a whole the cost-benefit analysis showed that the benefits in terms of higher production covered the costs. The main reason for the discrepancy between the results for individuals and the society is that taxes and transfers create a wedge between the overall income gain and the outcome for the individual.

The conclusion in this study - with the usual reservations for the methodological problems - is that the program covers its costs. This result was obtained for 1969-70, the peak years of mobility in Sweden.

What about later years? Has the level of mobility gone below its optimum for society? This is a common opinion. The main motivation is that the discrepancy between the profitability for individuals and the society has increased further because of higher taxes and transfers. The grants would probably have been increased further, if the political opposition from the distressed regions had been less.

IV c Early retirement

In contrast to mobility grants and retraining, the passive adjustment measure of early retirement has become a more commonly used tool during the last ten years.

One reason for the increasing use of early retirement is probably that the employment problem has increased for older persons. However, this is not the only explanation. As seen in Table 4, the

Table 4 **Early retirement and unemployment, 60-64 years**

	Newly retired	Stock of retired	Stock of unemployed
1977	1 700		4 900
78	2 050		7 200
79	2 600		7 300
80	3 600	5 000	5 800
81	3 450	5 500	8 100
82	3 700	5 850	12 700
83	5 500	7 600	16 800
84	9 100	12 000	20 400
85	10 500	15 800	16 900

Source: Statistics Sweden (SCB) and National Insurance Board (Riksförsäkringsverket).

number of new retired per year has increased faster than unemployment for 60-64 years old persons. During the last couple of years the increase is dramatic.

Two studies of the individual consequences of early retirement have been done. One of them - Anell, Lindell, Persson (1982) - focuses on white-collar workers who, during 1978, had retired from firms with structural problems. Most of them had abstained from their seniority rights when the firms contemplated layoffs. However, a few (17 percent of the sample) answered that they had felt some pressure to do so. The Employment Security Council was involved in all cases by covering parts of the costs of early retirement.

The individual effects were investigated by comparing the development of certain welfare indicators between a sample of individuals who had retired with pension and a control group of individuals who went on working. The development of welfare from 1978 to 1982 was investigated. All individuals were born in 1918.

The most interesting result is that the results are at variance with the common view - especially in the political rhetoric - that early retirement is strongly stigmatizing. The overall impression is instead that the group of retired workers experienced a better development than the control group. Both physical and mental well-being were improved compared to the control group. It also turned out that the retired were quite successful in finding new activities to spend their time.

Only two percent regretted that they had decided to retire in advance. Both groups had a more positive view of early retirement in 1982 compared to 1978.

One reason for these effects and attitudes might be that the economic terms for early retirement were good. In particular, the pensions were adjusted for inflation. On the other hand,

wages did not keep pace with inflation during these years. Therefore the retired group had improved their position from 1978 to 1982 whereas the control group had not. This development was not intended but it might have contributed to the positive experiences of early retirement.

The conclusions of the second study - by Hedström (1980) - are more ambiguous, even though the study hardly supports the view that early retirement has strong deleterious effects on the individual.

This study is not confined to white-collar workers in the private industry but includes early retirement in the whole economy.¹ The analysis is similar to the one used in the first study. The change in several welfare indicators - physical and psychological health, social activities etc. - of a group of early retired is compared with the experiences of another group with similar measurable characteristics. The change between 1968 and 1974 for individuals who were retired between 1969 and 1972 is analyzed.

There is no clear pattern in the results. The number of relative improvements for the early retired is about equal to the number of impairments.

The more unambiguous results of the first study might be due to a changed pattern of early retirements. Probably early retirement has become more voluntary since the early seventies; those retiring have often voluntarily abstained from their seniority rights. In that case the positive effects are hardly surprising.

Summarizing this section we have found two phenomena which are consistent with each other: (i) early retirement has become very common in firms facing structural problems and (ii) the indi-

¹ It also includes early retirement for other reasons than labor market problems, e.g. handicapped people who can get early retirement if their chances to get a job are low.

vidual welfare effects seem, in general, to be positive or at least not very negative.

Is early retirement cost effective? This is not easy to say. No study has addressed this issue. The costs for the government are obvious. The benefits are more difficult to estimate. There are distributional advantages that the individual consequences of structural change are mitigated. In addition the demands for subsidies - of more or less protectionistic kind - might have been reduced. Some speculation on this issue can be found in Section VI.

V Overall flexibility of the labor market

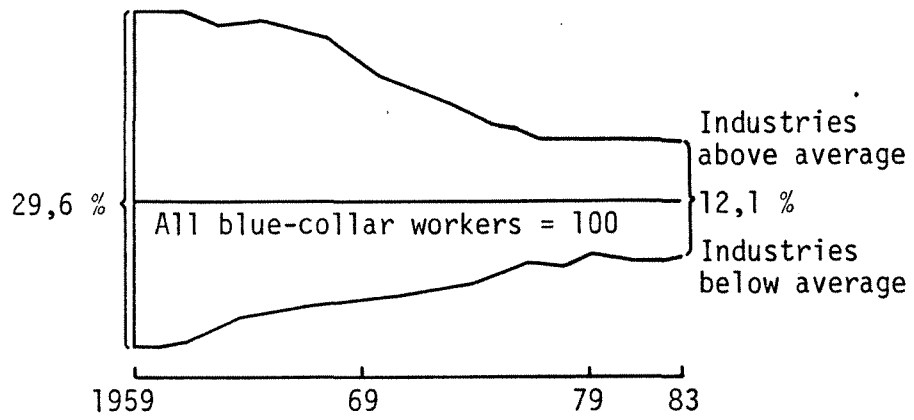
Beside the experiences of the policies to help laid-off workers, the effects of the solidaristic wage policy are crucial for an evaluation of the Swedish model. Is there an efficiency-cost - in terms of lower flexibility of the labor market - if wage differentials between expanding and declining firms and industries are not allowed?

Even though no clearcut answer can be given to this question some empirical evidence which sheds light on the issue can be presented.

First, it can be demonstrated that the wage policy really seems to have been successful in the sense that wage differentials in the Swedish industry have decreased during the last decade. Figure 5 displays that wages for blue-collar workers in various branches have narrowed substantially during the sixties and the seventies. There is also evidence of reduced dispersion of wages within industries for both blue- and white-collar workers (Figures 6 and 7).

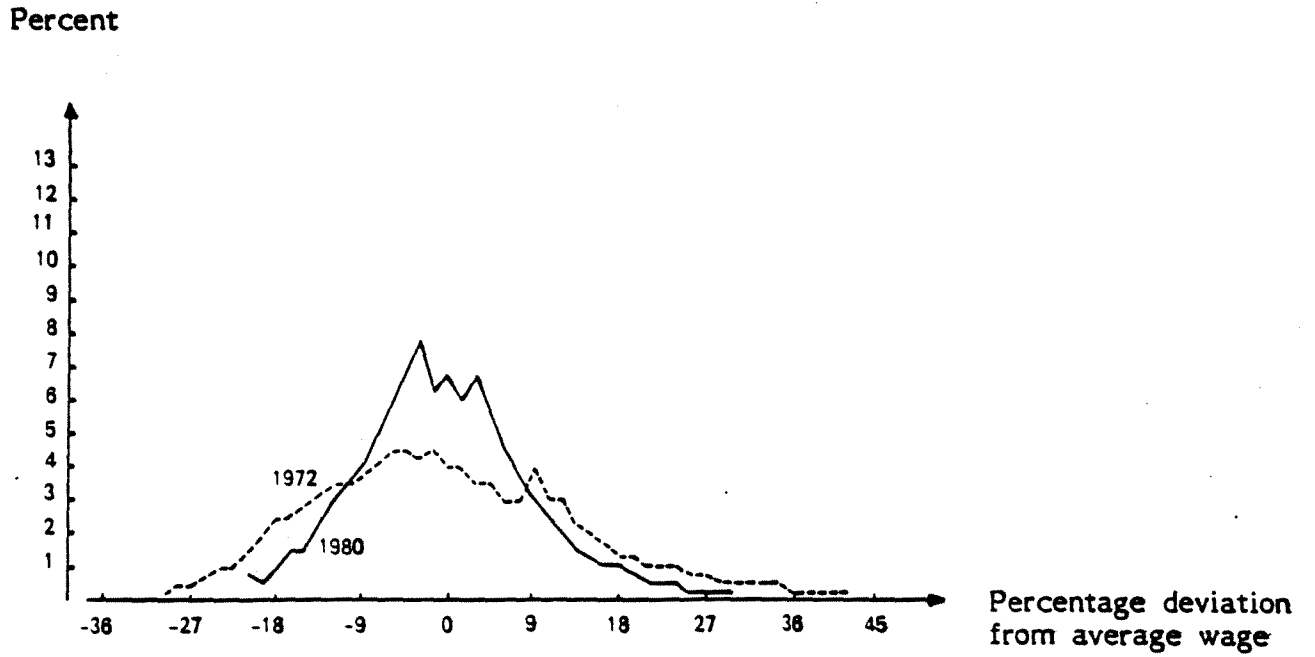
Of course the actual wage structure is not only determined by the goals of unions, in particular not only by the central unions

Figure 5 Dispersion of wages between industries, blue-collar workers



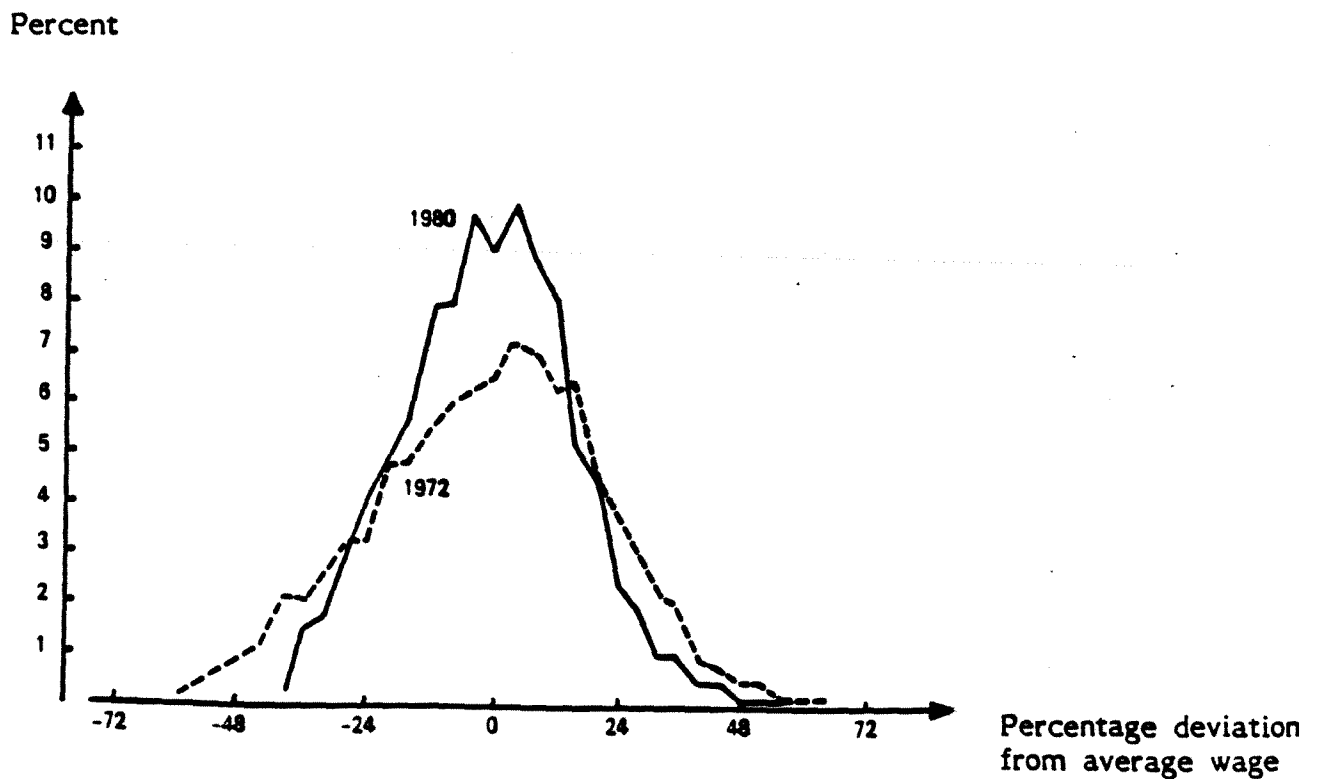
Source: LO.

Figure 6 Wage dispersion among blue-collar workers in engineering industry



Source: Jonsson and Siven (1984)

Figure 7 Wage dispersion among white-collar workers in engineering industry



at the nationwide level. In Sweden the total wage increases are often decomposed into negotiated wage increases and wage drift. The central unions can mainly influence the first component whereas the wage drift in general is determined at the local level with bigger impact of traditional "market forces". About one third of total wage increases can be attributed to wage drift.

However, the declining dispersion of wages is probably mainly caused by the wage agreements in the central negotiations. These agreements have in general had very explicit "low wage profiles", i.e. the percentage wage increases have been higher for those individuals and industries with low wages. Furthermore, lower than average wage increases have not been accepted in declining firms and branches. This conclusion is also supported by a recent econometric study of the determinants of wage dispersion in Swedish industry (Jonsson and Siven (1984)).

Has this development of relative wages reduced the flexibility of the labor market by reducing the incentives to move from declining to expanding firms? This question is hard to answer for at least two reasons: First, it is hard to measure the flexibility of labor markets. Second, it is hard to estimate the importance of flexible relative wages for individuals behavior in the labor market.

One proxy for the flexibility of labor markets is the total number of movers during e.g. a year. It will be used here, even though we are aware of its weakness. A declining number of movers does not necessarily imply efficiency losses. Longer duration of employment spells - and hence lower mobility - might be a consequence of better matching between employers and employees. Furthermore, the incentives to invest in in-plant training increases if expected employment in the firm is long.

The development of the two types of mobility is described in Figures 8 and 9.

According to the first figure, geographical mobility across counties has declined during the last two decades. Even though some of the decline can be explained by cyclical factors there is a clear negative trend.

Figure 9 displays job mobility. The same declining trend can be found for this variable. An interesting finding is the stable pattern among the young, but quite strong decline among the older.

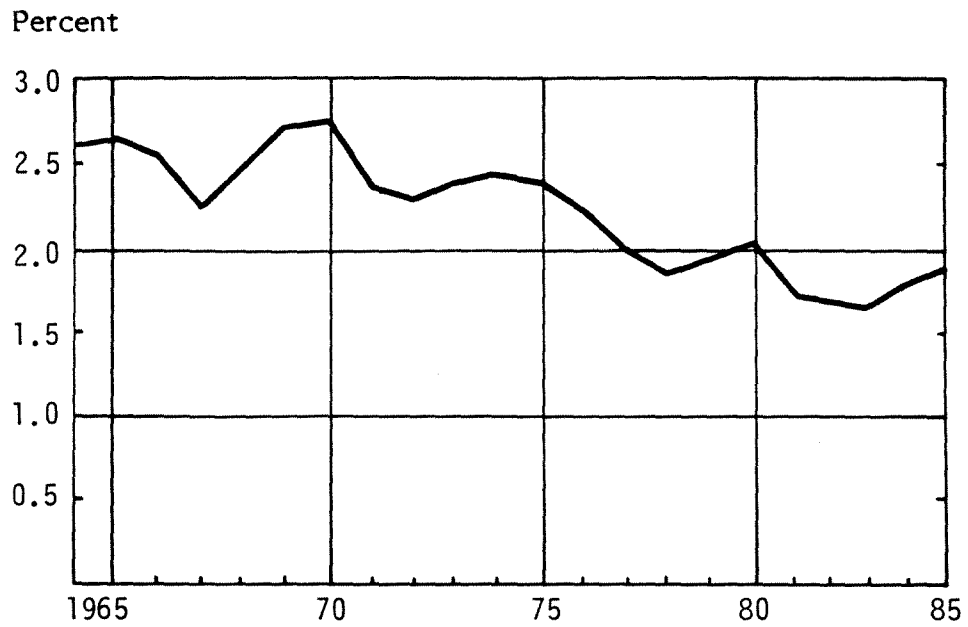
The strong decline for the older can at least partly be explained by the evidence presented above. The participation in retraining and receipt of mobility grants have decreased, whereas early retirement has increased. Furthermore, the seniority rules have sheltered the older workers from lay offs and reduced the incentives to move to higher paid jobs.

However, the basic issue is whether the wage policy has contributed to the declining mobility.

No doubt, the correlation between wage dispersion and mobility lends support to those who have been concerned about deleterious effects of solidaristic wage policy. By more scientific standards than simple correlation analysis it is harder to draw strong conclusions.

The available econometric studies indicate that relative wages do have some impact on various types of mobility decisions. On the other hand they say little about the magnitude of the effect. Holmlund (1984) contains two studies on the issues. The first is an examination of quit rates, both at the establishment and at the individual level. The analysis shows that quit rates at a certain establishment are higher the lower the wage level is compared to the average wage in the whole industry. The elasticity is - absolutely - above one. Individual data on quit intentions also display a highly significant wage-effect with the expected sign.

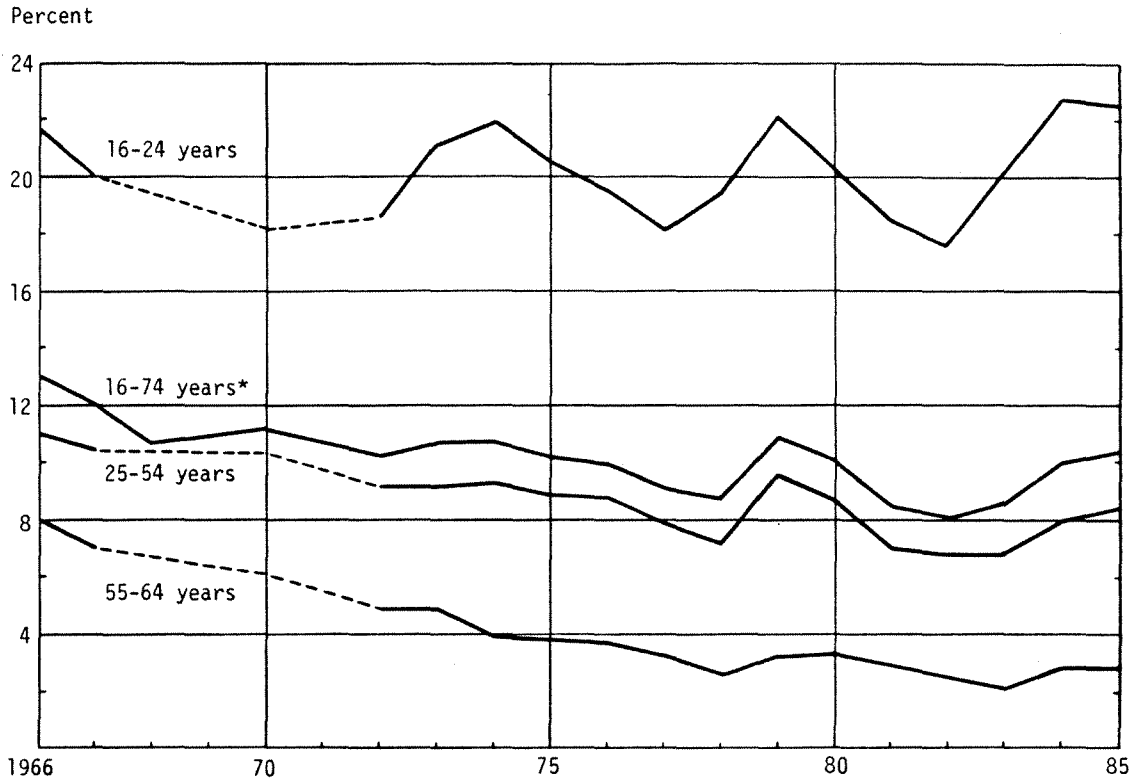
Figure 8 Migration rates between counties, 1964-85



— The number of migrations across county borders in percent of total population

Source: Statistics Sweden (SCB).

Figure 9 Job mobility, 1966-85. The number of persons with at least one change of employer, in percent of the number of persons with some employment experience during the year



* 16-64 years 1985.

Source: The retrospective labor force surveys, SCB.

In the second study, a model, which simultaneously captures the wage-effect of job-mobility and the decision to change employer, is estimated. One result is that the potential wage gain of job mobility is an important determinant of actual decisions to change employer.

In another study - by Nilsson (1982) - pooled cross-section and time-series data on migration between counties are used. In addition to variables capturing excess demand (vacancies) and excess supply (unemployed) relative wages are included among the explanatory variables. Again relative wages (between regions) affect the inter-county migration significantly. However, there is also a significant (negative) trend-variable, indicating that reduced wage-differentials are not the only cause of declining mobility.

Even though those studies confirm the importance of relative wages for mobility decisions, it is hard to use the results to quantify the deleterious effects of wage policy on labor market flexibility.

It is also important to emphasize that there are many other plausible determinants of the declining mobility during the last decades. (See Holmlund, 1984, Ch. 9.) One is the weakened demand for labor during the seventies. A second is the tax system; the marginal tax rate for Swedish income earners has increased from an average 31.5 percent during 1955, 36.4 percent during 1960, 42.2 percent during 1965, 47.4 percent during 1970, 53.4 percent during 1975 and 55.0 percent during 1980 (Hansson 1983).

A third plausible determinant is the growing number of two-earner households. In particular geographical mobility is less likely if both wife and husband are working.

A fourth is that the average plant size has shown a steady increase during the 60s and 70s. Empirical evidence shows that quit rates in large plants are substantially below those in small plants.

VI The political economy of adjustment policy

One of the motives for ambitious adjustment policies is that the gains from structural change can be distributed more evenly. By providing options for laid-off workers, the politicians can hopefully avoid - or at least reduce - demands from representatives of the affected industries to stop the structural change by industrial policies or trade-restrictions of various types.

What has the interplay between adjustment policies and other policies been in Sweden? This is not an easy question to answer. One can only speculate about various hypotheses. Econometric techniques can hardly be used for tests.

Four separate time periods can be distinguished. The first period covers the fifties and the first part of the sixties. During this period the Swedish model started to be implemented. The wage increases among in particular the blue collar workers became more in conformity with the principles of the solidaristic wage policy. Adjustment policies like mobility grants, retraining and employment exchange offices were introduced.

This was also a period with trade liberalization in Europe. The growth in the economy was high, partly because of the trade policy. During this period the attitudes towards adjustment and structural change were very positive. Even the trade unions in the declining industries accepted the consequences of the structural changes in the economy. It is hard to believe that the new adjustment policies did not contribute to these attitudes.

This is not to say that the third part of the model - selective employment policies - were avoided during this period. However, these policies did not to any extent prevent structural change or import competition. The major measures were various types of subsidies for firms to hire handicapped people, relief works in the construction industry during recessions and some rather general subsidies for investments in depressed regions.

A change occurred during the recession in 1967-68, the start of the second period. This recession coincided with a period of rapid structural change. The mobility of labor between regions reached a peak these years and during the following cyclical upturn (see section V). In particular, the mobility from the northern to the growing southern regions was extensive.

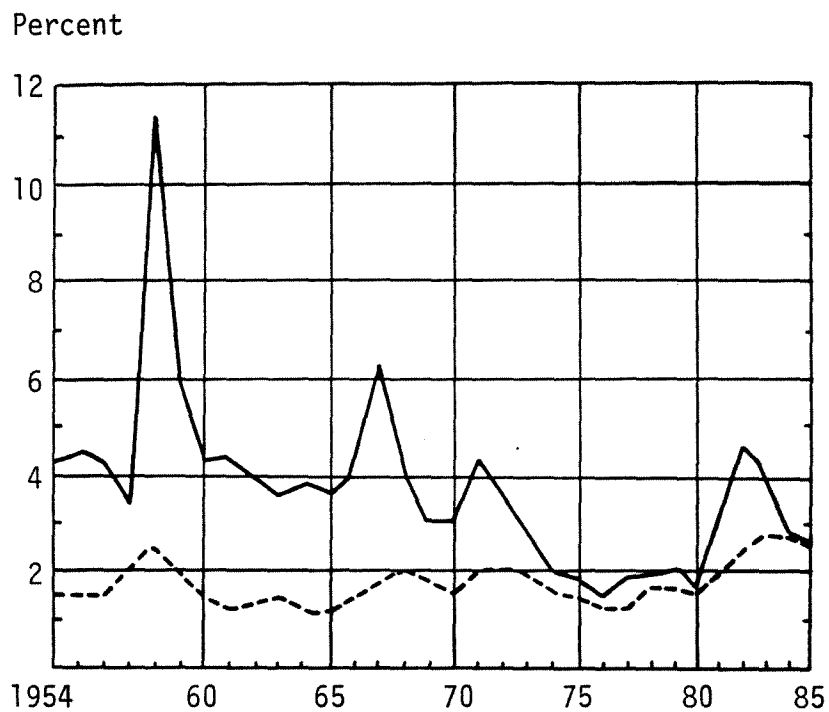
There was a strong reaction against this development. The reaction was reinforced by a couple of studies of the individual employment consequences of plant closures. These studies showed that a large fraction of the laid-off had major difficulties in obtaining a new job. The problems were most severe for older workers.

The policy reaction to these experiences was not industrial policies of protectionistic type. Instead, quite different measures were taken. One has already been mentioned, namely early retirement with pension for older unemployed. Another policy response was the employment security laws taken by the parliament in 1971 and 1974. These laws included the obligation for firms to notify both employees and the labor market authorities before lay-offs were realized. In addition, the older workers were sheltered by seniority rules when lay-offs were undertaken. The principle "last-in-first-out" should be followed. The law also formulated stronger criteria which must be fulfilled before an employee could be laid off.

The importance of these laws has been intensively discussed. Some have argued that they mainly formalized already existing "implicit contracts" between employers and employees. Others have argued that the laws have severely reduced the possibilities for firms to "survive" a structural crisis by laying off the least productive workers and keeping the most productive ones.

Irrespective of the importance of the laws per se, the lay-off rate in Swedish industry has declined from the sixties to the seventies. This decline is not only a cyclical phenomenon (see Figure 10).

Figure 10 Layoff rates in Swedish industry and unemployment among insured employees, 1954-85



— Layoff rate (yearly basis) in mining and manufacturing (blue-collar workers).

- - - - Unemployment rate for insured employees.

Sources: Layoff rate: SCB.
Unemployment rate: AMS.

This development puts the pattern described in section III.1 - the declining adjustment ability of laid-off workers - in a somewhat new perspective. Even though it has become more difficult to find a new job after being laid-off, the number of lay-offs has decreased.

A consequence of this development has probably been increasing difficulties for young workers in the labor market. The "adjustment burden" has been shifted from the older to the younger generation. However, this tendency has to some extent been counteracted by the increasing popularity of early retirement. It has become more and more common that older workers abstain from their seniority rights when lay-offs are contemplated at a firm. Instead they decide to retire in advance with pension.

The third period started in the mid-seventies. The negative effect of the deep cyclical downturn in the world economy after the oil crisis in 1973-74 was in Sweden reinforced by exceptionally high wage cost increases. The consequence was a general deterioration of the competitiveness of Swedish industry at the same time as some important industries were facing long-run structural problems. The shipping, shipbuilding, steel, mining and certain parts of the forest-based industries were particularly hard hit. Together these crisis-stricken industries accounted for some 35 per cent of the total Swedish export. Many firms and even whole industries were facing bankruptcy or drastic cutbacks. The situation created strong political demands for action on the part of the government.

The policy response to these problems was twofold. First, public sector employment was expanded. The expansion took place in several ways. The health and service sectors grew rapidly. The temporary jobs for unemployed, which during the sixties mainly were so called relief works for construction workers, were directed towards youth and the public sector. They also increased in number.

The second and most drastic policy response was the direct actions by the government to save the threatened firms. The major measure to do this was industrial subsidies.

A characteristic feature of the bulk of these subsidies was that they were firm specific. The head of the Ministry of Industry was in general negotiating more or less personally with the firms to find solutions which prevented bankruptcy and drastic reductions of employment. The magnitude of the subsidies grew rapidly from 1973 to 1978. The total industrial subsidies accounted in 1976-79 for between three and four per cent of GNP, whereof almost half were firm specific subsidies. However, parts of these amounts were loans (which often became converted into grants). A study by Carlsson (1983) has shown that the subsidies were high and very selective compared to other West-European countries.

Of course, other more general and less protectionistic measures were tried. Two devaluations of the currency achieved moderate, but mostly temporary, progress. The labor market policies mentioned above were used too, but these measures did not eliminate the demands for political actions from the affected firms and their employees. To some extent they might have reduced the use of industrial subsidies. In particular the use of early retirement was frequent in the firms facing difficulties. This might have reduced the need for subsidies.

Why did this happen? Why was the traditionally positive view on structural change broken by the politicians, the employees and their unions and the employers? Probably many factors coincided in an unlucky way.

The most important reason was probably that the structural problems were very big and coincided with low growth in the rest of the economy. Another factor is that the threatened plants often were the major employers in the local labor markets. This makes the adjustment problem even worse.

It might also be that the traditional adjustment policies were not considered as attractive. The threatened workers were often relatively well-paid. Even with a relatively ambitious retraining course it might have been difficult for these workers to reach the old wage level again.

Finally, the experiences illustrate the consequences of breaking a rule for economic policy. As soon as one firm has received subsidies it is, if course, very difficult to deny the same help to other firms.

The fourth period in the Swedish development started in the early eighties. A combination of two quite large devaluations in 1981 and 1982 and a cyclical upturn in the world economy provided a major boost to the Swedish industry. Very few new subsidies were implemented and the old ones gradually disappeared. However, the real test whether the use of industrial subsidies was a temporary phenomenon or not, will come in the next recession.

Adjustment policies and wage formation

During the last years another potential indirect effect of adjustment policy has been emphasized in the Swedish debate, namely the effect on wage formation. The idea is the following. Consider the incentives facing a trade union and its opposite party of employers when negotiating about wage increases. Both parties have to consider the consequences of excessive wage increases. The employers will suffer from lower profits and deteriorated competitiveness, especially if the industry faces international competition. The trade union must take the unemployment risks into account.

However, when unemployment compensation, adjustment policies and accomodating employment policies are financed by general taxes, the costs of excessive wage increases can, at least partly, be shifted over on others. Therefore, the presence of adjustment policies financed by general taxes decreases the incentives to pre-

vent unemployment caused by excessive wage increases. The policies can become a destabilizing factor in the economy.

This is a moral hazard problem, but of a different nature than the one traditionally dealt with in the literature. It is very hard to evaluate this argument. However, it is important to realize that the discussion about the problem is caused by the tendency of the Swedish economy to be hit by large wage cost problems. During the last decade several devaluations have had to be undertaken to accommodate such problems.

The discussion about these problems has not in the first place led to questioning of adjustment policies in themselves. Instead the financing of the policies has been high-lighted. The idea has been that the costs of adjustment policy should be internalized in the wage formation process as much as possible. By making the unions and the employers organizations financially responsible for the adjustment policies the costs can to some extent be internalized.

VII Problems and prospects for adjustment policy in Sweden

The flexibility of the Swedish labor market has, according to several indicators, deteriorated during the last 15-20 years. As shown above the mobility of labor - defined in various ways - has declined and the problems for laid-off workers to find new jobs have increased. This development has taken place in spite of several ambitious policies to facilitate the adjustment for unemployed.

At the first glance these experiences do not look encouraging for proponents of such policies in general and the Swedish ones in particular. However, the negative development should not necessarily be interpreted as low cost-benefit effectiveness of the policies. A more plausible explanation is that the incentives to adjust in the labor market created by the wage structure and marginal

taxes are much more important. We have shown that the dispersion of wages has been reduced drastically and the marginal taxes have risen continuously. The econometric evidence, though some methodological caveats are in order, does indicate that mobility decisions are affected by wage differentials. A plausible conclusion is that adjustment policies like retraining, mobility grants etc. can only give a small contribution to the overall flexibility of labor market. In particular, the general incentives for mobility and skill training might be the most important factor for adjustment to structural change in the labor market. Of course the interdependence between wage differentials on the one hand, and the desire to participate in programs like retraining on the other hand might be important too. A common opinion is that the relatively low wages for rather unpleasant jobs in the manufacturing industry compared to more pleasant ones in the public sector is one of the main reasons for the difficulties in getting unemployed workers to participate in the retraining courses for industrial occupations.

For the same reasons it is not surprising that the existence of adjustment policies has not been sufficient to make politicians abstain from accommodating employment policies like expansion of the public sector and - during the late seventies - industrial subsidies.

The recent debate about the impact of adjustment policies on the behavior of other agents in the economy has instead focussed more on the impact on wage formation. Whether this will lead to any changes in the financing of the policies is hard to say. One noteworthy change, which partly goes in this direction, is that a counterpart to the Employment Security Council for white collar workers is planned for blue collar workers too. These plans have probably in the first place been caused by dissatisfaction with the policies administrated by the National Labor Market Board. However, an indirect effect will be that the financing of adjustment policies to a greater extent will be tied to the organization responsible for wage formation.

Finally, what about the specific policies? The main experience of early retirement with pension is that it is less stigmatizing for the individual than expected but very costly for the government because of its rising popularity. A reasonable guess is that this type of policy will remain in the policy mix, but its use will be restricted in some way. One alternative is to reduce the possibilities for older workers to abstain from the seniority rights. Another is to finance the costs more by fees by the employers or the union members and less by general taxes. In the latter case the "willingness to pay" for the opportunity to be retired in advance will be tested.

The mobility grant has recently been raised substantially. The effects of this change will probably be crucial for the future of this measure.

Retraining, finally, has faced several problems during the last years. In particular, the difficulties in getting unemployed to retrain has caused concern about the measure. This problem has not led to the conclusion that retraining per se is not needed. Indeed, the need for skill-training both for unemployed and employed is stressed in the present Swedish debate.

Two policy options to make retraining more attractive have been considered. One is - in conformity with the Swedish model - to raise the stipends and compensate for the low individual pay-off caused by the wage structure. Another is to make the courses per se more attractive. So far it seems as though the latter alternative has been chosen. The government has decided to increase competition in the sector for production of retraining courses. The monopolistic position of the retraining system will be broken in the near future. Instead of giving the money directly to the retraining organization, the local labor market authorities will get freedom to buy retraining courses for the unemployed from any organizer of courses. A common opinion is that this institutional change will lead to more in-plant training in the firms.

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