Dutch employment growth

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Dutch employment growth: an analysis

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Abstract

After documenting rapid Dutch employment growth in recent years, this article explores the main reasons behind recent strong employment growth in the Netherlands. Subsequently, it discusses the unfinished agenda facing Dutch policymakers. Finally, the lessons for other countries of the recent Dutch experience are summarized.

Samenvatting

Na cijfers over de recente sterke werkgelegenheidsgroei in Nederland gepresenteerd te hebben, bespreekt dit artikel de belangrijkste verklarende factoren voor deze groei. Daarna komen de nog aan te pakken zwakke punten van de Nederlandse economie aan de orde. Tenslotte worden de lessen voor andere landen van de Nederlandse ervaringen samengevat.

Introduction[1]

The Dutch economy has received a great deal of acclaim recently. Indeed, recent attention for the Netherlands is due to not only its EU presidency but also its good economic performance, especially as far as employment is concerned. Twenty years ago, economists were discussing the Dutch disease. Now, they talk about the Dutch miracle.

This article addresses the following three questions. What is behind the 'wonderful' healing of the Dutch economy? To what extent has the Dutch patient really recovered at the moment and what is the unfinished agenda facing Dutch policymakers? What can the other EU countries learn from the Dutch? Before turning to these questions, we examine some aggregate data.

Labor-market developments

Employment

Employment (in persons) in the Netherlands grew at an annual rate of about 1.4% a year between 1983 and 1995. The corresponding figure for the EU-15 countries was only 0.4% (see Figure 1). If we express employment in terms of hours, the picture does not change fundamentally; in terms of employment growth, the Netherlands has been outperforming the rest of Europe by a considerable margin during the last 15 years (see Figure 2).

This employment growth reflects rapid growth of labor supply during this period. Two main factors boosted Dutch labor supply: relatively rapid population growth and a gradual catching up of the low female labor-force participation rate to the European average (see Figure 3).

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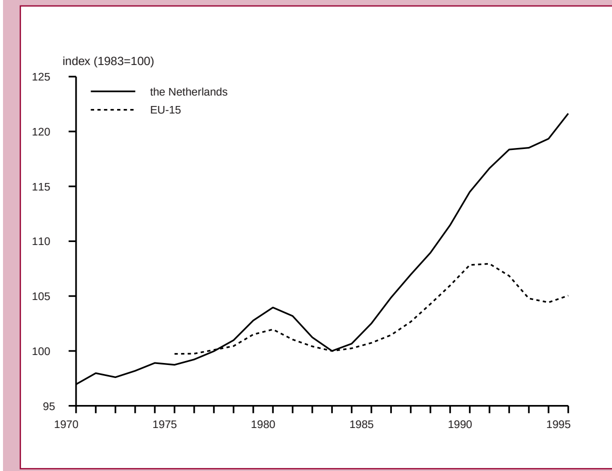
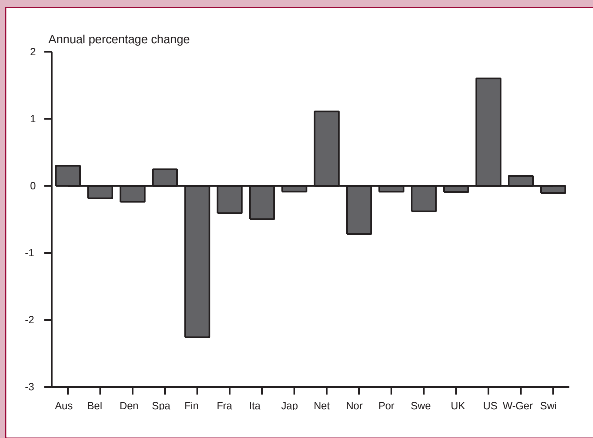
Figure 1 Employment in persons



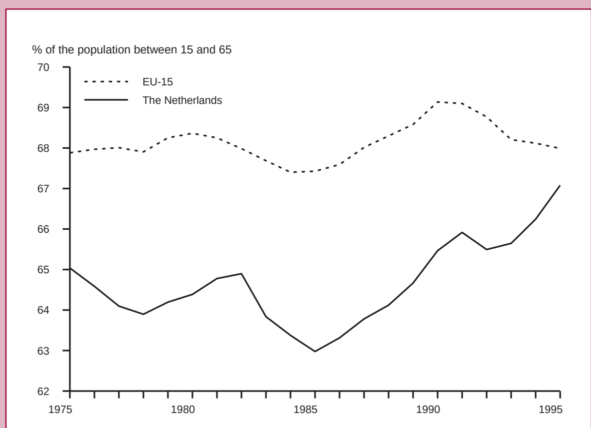
Source: Wildcat, CPB

Figure 2 Growth of total hours actually worked, 1984-1994



Source: Maddison, 1991, 1995; Pilat, 1996; DIW; CPB

Figure 3 Gross participation rate, 1975-1995



Source: Wildcat, CPB

Despite the rapid expansion of labor supply, unemployment (measured in an internationally comparable manner, namely as the number of persons who are actively looking for work and are available to start work within two weeks) fell substantially. Figure 4 illustrates the turn-around in the Dutch relative performance in the EU. In 1983, the Dutch unemployment rate of 12 percent exceeded the corresponding rate in the other EU countries by more than 2 percentage points. In 1996, in contrast, the Dutch rate of 6.5 percent was 4 percentage points lower. The EU unemployment rate in 1996 was higher than in 1983. The Dutch unemployment rate, in contrast, was almost cut in half between 1983 and 1996 and is now close to the corresponding rate in the United States.

Labor costs

Rapid employment growth in the Netherlands was facilitated by wage moderation. Whereas unit labor costs in Dutch manufacturing remained roughly constant during the last fifteen years, unit labor costs in Germany, which featured about the same inflation rate as the Netherlands during this period, rose on average by about 2 1/2 percent per year (see Figure 5).

Wage moderation boosted employment through three main channels. First, it restored profitability of businesses, thereby creating the room and the incentive to boost investment (see Figure 6). The share of labor income in net enterprise income declined from 95% in 1981 to around 83% in recent years. Second, it improved the competitive position on world markets (see Figure 7), thereby raising net exports. Third, it rendered growth more labor intensive. Indeed, the growth of labor productivity per hour worked lagged that in other European countries.[2] Due to the increase in employment in hours, however, growth of GDP per capita exceeded that in other member states of the EU (see Table 1). In terms of GDP per head (purchasing power parities), the Netherlands ranks now 7th in the EU, while it had declined to the 11th position by 1988 (see Figure 8).

The recent Dutch experience provides evidence for the effectiveness of wage moderation in stimulating employment. Table 2 reveals that during the periods 1973-1982 and 1983-1996, growth of relevant world demand was similar. Dutch employment performance, however, was substantially better over the latter period. The main explanatory factor behind the improved performance of employment during 1983-1996 is wage moderation.

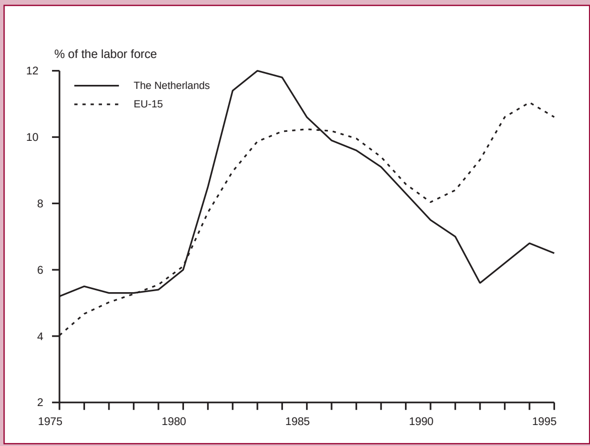
Factors behind recent employment growth

A deep crisis

In the beginning of the eighties, the Dutch economy was in dire straights: the fiscal deficit had widened to record levels, about two thirds of GDP was spent or redistributed by the government, taxation and social security contributions accounted for about half of GDP (see Figure 9), business profitability and investment had plummeted dramatically, and for every ten employed persons there were about eight persons on social benefits (see Figure 10). Moreover, GDP per head grew much slower than in other EU countries (see Figure 8).

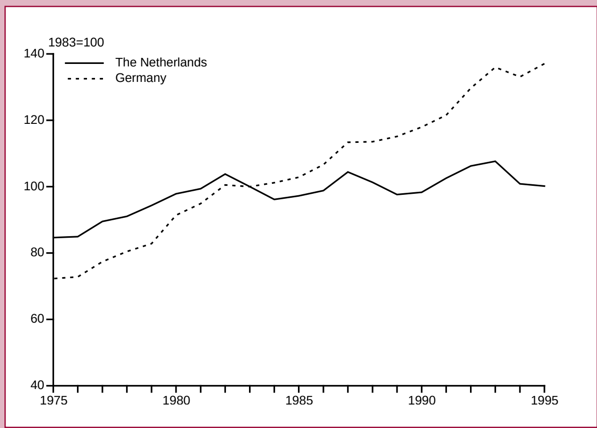
In order to understand the origins of this crisis, we should go back to the sixties, when the welfare state expanded substantially and rapid wage growth eroded profitability. Subsequently, the Netherlands, like all OECD countries, was hit by stagflation as a result of the abrupt

Figure 4 Unemployment rate, 1975-1995



Source: Wildcat, CPB

Figure 5 Unit labor costs, manufacturing



Source: Wildcat, CPB

Table 1 GDP, hours per worker and employment/population, 1982-1995

	EU4	Netherlands
annual percentage changes		
GDP per capita	1.85	2.02
GDP per hours worked	3.77	2.60
Hours per worker	–1.79	–1.06
Employment/population	–0.06	0.60

Sources: CPB: Wildcat (release CEP97), except hours per worker: Bureau of Labor Statistics.

increases in oil prices in the early seventies. Initially, the Dutch government attempted to address the economic downturn through expansionary policies and employment creation in the public sector. The rapid expansion of the public sector was financed by higher revenues from natural gas, higher taxes and premiums, and a widening fiscal deficit (see Figure 9). At the same time, generous benefits in combination with lax administrative controls allowed employers and unions to put low productive, redundant workers in social security schemes with open-ended benefits, such as the disability scheme (see Figure 10). Hence, the stagnation and subsequent decline in private-sector employment did not produce a rapid rise in open unemployment.

When the second oil crisis hit at the end of the seventies, Dutch policymakers had lost all room for expansionary

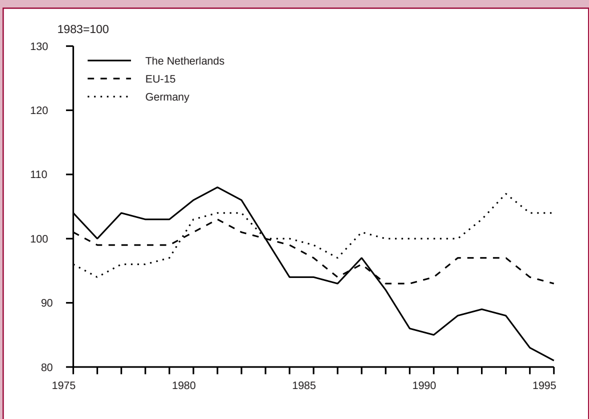
Table 2 World trade, employment and labor costs, 1973-1996

	1973-1982	1983-1996
annual percentage changes		
Relevant world trade[a]	4.7	5.3
Employment		
- hours	–1.6	0.9
- persons	–0.8	1.4
Production	1.9	3.0
Real labor costs	3.8	0.8
annual absolute changes in level (x 1000)		
Employment growth		
- labor years	–33	50
- persons	–31	55
Labor share in value added (%)	1.2	–0.8

[a]World imports, excluding energy, reweighted to geographical distribution and product-mix of Dutch exports.

Source: CPB: Wildcat (release CEP97).

Figure 6 Labor income share, manufacturing

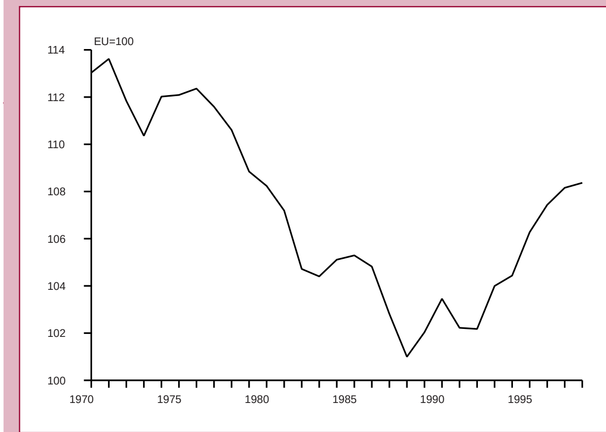


Source: Wildcat, CPB

Figure 7 Unit labor costs, relative to competitors

Source: Wildcat, CPB

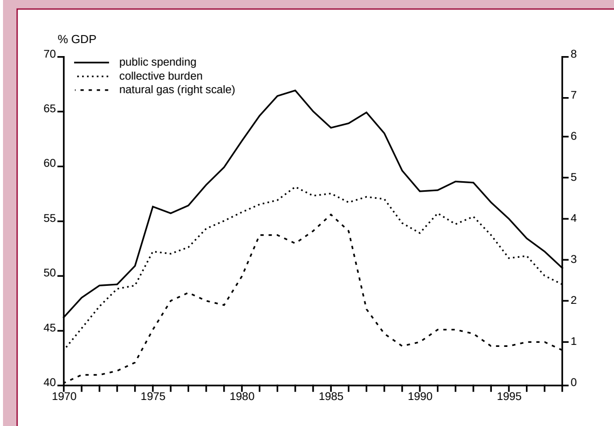
Figure 8 Dutch GDP per capita (purchasing power parities) in terms of GDP per capita in the EU, 1970-1998[a]



[a]1996-1998 are CPB estimates

Source:OECD, National Accounts, main aggregates, vol. I, 1997 edition.

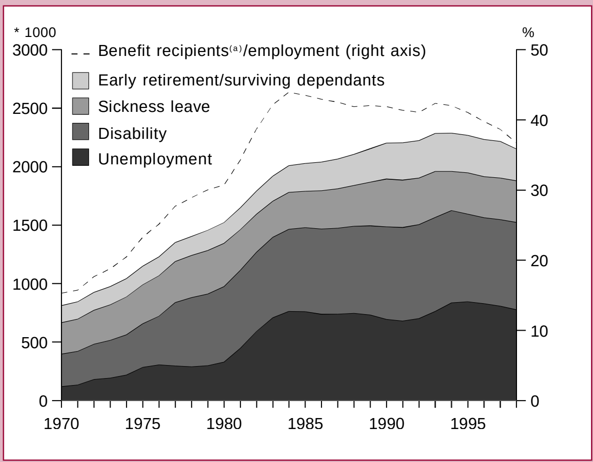
Figure 9 Public finances, 1970-1998[a]



[a]1997 and 1988 are estimates

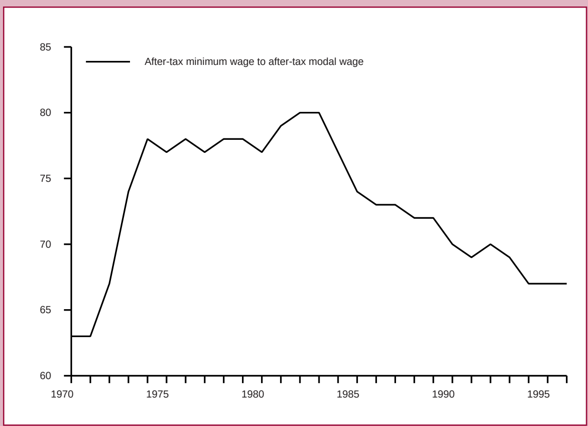
Source: CPB

Figure 10 Number of benefit recipients younger than 65 years old



[a]Excluding (early) retirement
Source: CPB

Figure 11 Minimum wage



Source: CPB

Figure 12 Average tax wedge, 1979-1998[a]

[a]1997 and 1998 are estimates
Source: CPB

policies: the fiscal deficit was approaching 10% of GDP, resulting in an explosion of the public debt to GDP ratio. At that time, the Dutch economy was caught in a vicious circle of less employment and more claims on the welfare state. By raising the cost of labor, higher premiums depressed employment further. With the welfare state acting as a 'social hammock', the adverse macroeconomic shocks of the seventies threatened the viability of the system.

In the beginning of the eighties, when unemployment was exploding, the need for drastic measures became increasingly apparent. In taking these measures (see below), the first Lubbers administration, which came to power in 1982, did not bargain with the social partners, i.e. the unions and employers. Indeed, the character of the relationship between the government and social partners changed from bargaining over mutual concessions, such as trading tax reductions for wage moderation, to the development of common policy orientations, such as a strong employment performance. In this way, responsibilities of government and social partners were better delineated.

Social partners concluded a number of successful bilateral agreements in the eighties and nineties with non-binding qualitative recommendations on specific issues. These agreements contrast with the failed attempts to arrive at detailed 'social accords' of the seventies. While the central organizations issue broad guidelines and agreements, these guidelines are actually implemented on a more decentralized, sectoral level. Actual wage negotiations, for example, are taking place at a sectoral level. This mix of centralized and decentralized negotiations has served the Netherlands quite well over the past fifteen years.

Wage moderation was facilitated by an agreement between social partners in 1982. Initially, the main factor behind wage moderation was the weak bargaining position of organized workers due to rapidly rising unemployment. Later on, the positive results of wage moderation strengthened confidence in the revised consultation economy. Hence, compared to other EU countries, the Netherlands started the reform process earlier because it was confronted with a deep crisis at a relatively early stage.

Fiscal policy

The government initially supported wage moderation by spending cuts, which resulted in lower replacement rates for social benefits. Among other things, the government broke the link of wages in the public sector and social benefits to wages in the private sector. Hence, rather than passively following wages in the private sector, the government actively set a trend in wages in the public sector and social benefits, thereby affecting private wages. Statutory social benefits were cut from 80% to 70% of gross wages. In addition, the minimum wage, to which the minimum social benefits are linked, was frozen in nominal terms in a number of years. This reduced the after-tax minimum wage in terms of the after-tax modal wage from about 80% in 1981 to 67% in 1996 (see Figure 11). In addition, in-work tax benefits were increased. Finally, youth minimum wages were cut substantially.

The public spending to GDP ratio fell from 67% in 1983, which exceeded the EU average at the time by more than 10 percentage points, to 54% in 1996, which is close to the EU average. Initially, the government used spending cuts to reduce the fiscal deficit rather than the tax burden (see Figure 9). Fixed targets for deficit reduction became the main guiding post for fiscal policy in the eighties. The Dutch experience thus shows that deficit reduction can be quite consistent with employment growth.

Only when the deficit was reduced substantially in the beginning of the nineties, was the government in a position to support wage moderation through substantial reductions in the tax burden. In recent years, the government has reduced the tax wedge on minimum incomes substantially (see Figure 12). This was done in order to stimulate employment of low-skilled workers.

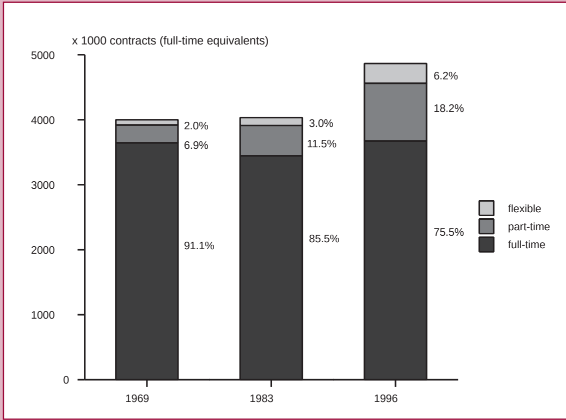
Social insurance

It took a long time not only to get the public finances under control but also to stop the vicious circle of rising inactivity. The ratio of social security claimants to those employed stayed roughly constant between 1983 and 1995, despite rising employment. Only in recent years has it been possible to stabilize the number of social security recipients and has the ratio of social security beneficiaries to employment started to fall. Cutting benefits had not been successful in reducing the number of recipients (see Figure 10), in part because supplementary arrangements negotiated in collective labor agreements offset some of the cuts in unemployment, disability and sickness benefits.

In the nineties, eligibility criteria for social benefits were tightened. In 1993, the legal definition of the appropriate job was widened in the disability scheme. With residual earning power determining benefits, people who in the past would have received full benefits now receive only partial benefits. At the same time, the government reduced the discretion of the executive organizations by issuing specific criteria for determining disability and residual earning power. For existing claimants, a program of reassessment was started in 1994.

More recently, social security is being reformed more fundamentally by the introduction of competition in disability insurance and by the privatization of sickness insurance. These reforms have two related primary aims. First, competition ensures that contributions closely match actuarial risks. Hence, employers are directly confronted with the costs and benefits of their actions on these risks; they can no longer shift the costs of their behavior onto a collective pool. This encourages employers to reduce risks by improving working conditions and by cutting supplementary benefits. Second, the introduction of competition is expected to reap efficiency gains in the implementation and administration of the insurance. Private insurers and public administrators face more incentives to revalidate the sick and disabled. Organizations that are most successful in preventing disability and encouraging revalidation and reintegration can exploit this as a competitive advantage.

Figure 13 Fixed and flexible contracts, employees



Source: Wildcat, CPB

Labor-market flexibility

Another major factor behind the growth of employment (and the moderation of wages) is the growth of part-time and flexible jobs. These types of jobs account for most (three quarters) of the growth in employment since 1983 (see Figure 13). During the period 1983-1993, most of the growth came from part-time work. More recently, flexible contracts started to grow faster. At the moment, more than 40% of Dutch workers have either a flexible contract (12%) or part-time contract (30%).

A flexible contract features a limited duration (a fixed term) or a variable number of working hours. Especially work through temporary work agencies rose substantially in the last few years (to about 3.5% of working hours). Dutch employers make more extensive use of temporary work agencies than any other EU country. More generally, employers increasingly use flexible contracts to avoid employment protection, to screen new employees, and to meet their need for flexibility. Regulations that restrict the use of flexible contracts are quite liberal in the Netherlands.

Part-time work also enhances working time flexibility with respect to regular fluctuations in work loads. Moreover, it meets the needs of parents with young children who want to enter the labor market. Accordingly, by facilitating the access of women to the labor market (and exploiting their latent labor supply), part-time work has helped the participation rates of especially younger and middle-aged women to catch up to the European level. The job share of part-time work of 30 percent is more than twice as high as the EU average.

The match between the needs of employers and employees in the case of part-time work illustrates the win-win principle, namely that enhanced flexibility can benefit not only the employer but also the employee; as tastes of employees become more heterogeneous and variable, market-oriented flexible working arrangements can tailor to the individual needs of employees. In the same vein, rather than relying on uniform reduction of the work week, unions and employers have recently started to look for solutions that allow individual employers and workers to find tailor-made solutions. Also in the selection of the retirement age, unions and employers are increasingly looking for such tailor-made solutions that meet individual preferences on the basis of actuarially fair prices.

Flexible and part-time work contribute to a strong employment performance through other channels as well. First, they keep more (especially young) people in touch with the labor market, thereby protecting their human capital and working skills. This, together with the improved access to the labor market, boosts effective labor supply and provides better insurance against human-capital risk.

Second, a more flexible labor market is consistent with the need to tailor to technological and organizational innovations that demand more flexibility. For the same reason, the Dutch government is currently deregulating markets for goods and services. The policies of deregulating the markets for labor, goods, and services are mutually reinforcing.

The unfinished agenda

Now that we have examined the impressive side of the Dutch model, it is time to turn the coin. The Dutch economy still faces a lengthy unfinished agenda.

Access of vulnerable groups to work

Most of the employment growth in recent years benefited those who did not draw on social benefits--such as the partners of breadwinners and young people lacking sufficient work history to be eligible for benefits. The recent reduction in the ratio between benefit recipients and employment has been attained mainly through an increase in employment rather than a decline in the number of benefit recipients.

Benefit recipients still seem to have very limited access to work. This is reflected in the high share of the long-term unemployed in overall unemployment. While the unemployment rates in the Netherlands and the United States are rather similar at the moment, the incidence of long-term unemployment is much higher in the Netherlands (see Table 3). Indeed, in terms of long-term unemployment and the low access of vulnerable workers without many marketable skills to work, the Dutch labor market is very much European rather than American. Thus, also the Dutch have not yet been able to reconcile high benefit levels for needy groups with high levels of employment for these groups.

Reducing high inactivity (in persons)

The current unemployment figure of 7% substantially underestimates the overall level of inactivity in the Netherlands. Broadly defined unemployment, including hidden unemployment, may well exceed 20%. In particular, the number of people collecting unemployment benefits is about 75% higher than the number of unemployed who are

Table 3 Long-term unemployment in various countries

	1985	1990	1995
	% of unemployment		
Netherlands	58.8	47.1	46.7
Germany	53.7	45.7	48.7
European Union	54.6	51.0	49.2
United States	9.5	5.6	9.7

Sources: United States: OECD ‘Employment Outlook 1996’.
Other countries: European Commission ‘Employment in Europe 1996’.

actively looking for work. A large portion of those collecting benefits but not looking for work are older than 57 1/2 years old, an age above which they no longer have to look for work in order to be eligible for unemployment benefits. At the same time, in addition to discouraged workers and involuntary part-time workers, a substantial number of disability claimants are estimated to be hidden unemployed. Indeed, the number of people collecting disability benefits is still about two to three times the rate in neighboring countries. Disability, unemployment, and early retirement schemes have reduced the participation rate of those aged 50-64 to low levels (see Table 4).

This low participation rate for elderly people is particularly worrying in light of the ageing of the population. Inadequate labor supply may give rise to tensions on the labor market. These tensions may reduce profitability and investment, thereby bringing employment growth to an abrupt end and setting in motion the old vicious circle.

The low unemployment rate thus may be a sign of weakness rather than strength because it indicates that not many people on social security benefits are actively looking for work. Indeed, the success of the Dutch economy should not be judged on the basis of the unemployment rate but rather on the way it utilizes the human capital of its population. On this latter score, the Dutch still have a long way to go.

Utilizing human capital

Labor supply can be increased through four channels: First, activating people drawing on social security; second, increasing the effective retirement age; third, raising labor productivity by more accumulation of human capital per worker; and fourth, increasing the average working hours per worker.

1. Activating benefit claimants

A first major challenge for the Dutch economy in the coming decades will be to activate the latent labor supply locked in social security schemes and to increase the access of vulnerable groups to work. Technological and organizational developments increasingly put at risk vulnerable individuals with few marketable skills.

To prevent long-run dependency and social exclusion, the government should shift away from passive towards

Table 4 Employment in persons in different age groups, 1995

age	Netherlands	EU-15	Germany	United Kingdom	France
in % of the population					
25-49	75.9	74.3	77.7	77.8	77.8
50-64	42.0	46.6	50.0	57.0	43.3
25-64	66.6	65.4	67.9	71.6	67.9

Source: Eurostat, Labor Force Survey 1995.

Table 5 Working hours, 1994

	United States	United Kingdom	W-Germany	Netherlands	Sweden
in hours per year					
Per employee	1599	1531	1592	1329	1490
Per head	749	654	663	567	715

Source: DIW, CPB; Pilat, 1996

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active support that strengthens the earning capacity, skills, adaptability, and employability of vulnerable individuals. In this connection, conditional transfers based on the transaction principle (i.e. balancing the carrot of the benefit with the stick of certain obligations) can be used to screen claimants, thereby alleviating moral hazard. Moreover, in-kind transfers can link support to activities (such as training, unpaid trial employment, community work) that encourage rather than discourage re-entry into employment. At the moment, wage subsidies for hiring long-term unemployed are already being used as a particular form of in-kind benefits. In addition to stimulating and strengthening supply, lower taxes on low-skilled labor can help to boost demand. The same holds true for deregulation of sheltered sectors.

A shift toward more active policies involving conditional and in-kind benefits calls for tailor-made solutions implemented by a decentralized benefit administration that exploits its information advantage about individual circumstances.

2. Raising the effective retirement age

Another channel through which labor supply can be increased is a higher average effective retirement age. This age is currently below 60 years in the Netherlands. Also this requires a mix of instruments at both the demand and supply sides. Moreover, lifelong learning should increase the employability of older workers by increasing their capability to learn and adapt. At the demand side, employers can be encouraged to employ elderly workers not only by increasing the skills of the elderly but also by reducing wage costs. To achieve this, age-related pay schemes may have to be reconsidered so that wages can be better adjusted to individual productivity levels.

At the supply side, early retirement schemes should be made actuarially fair to facilitate efficient retirement decisions. As people become more flexible, it is more important that they are confronted with the right incentive structures. Moreover, an early announcement of a higher statutory retirement age can help to increase the effective retirement age by lengthening the planning horizon of workers.

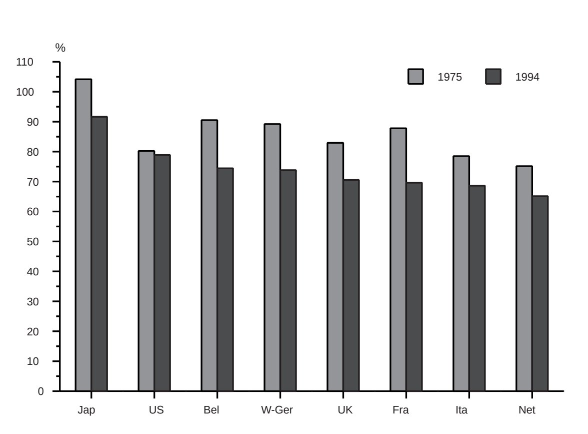
3. Investing in human capital

The increased knowledge intensity of production requires more human capital accumulation. In addition, more human capital can alleviate the scarcity of labor as the population ages. An increased capacity to learn also increases the flexibility of people. Until now, a relatively small number of flexible workers bear the burden of the need to enhance the flexibility of the labor market. In the future, also the core of the labor market ('the insiders') will need to become more flexible, even if workers stay with the same employer. This will help to reduce the dichotomy between the two segments on the labor market. As noted above, lifelong learning can help to ensure that human capital lasts longer, thereby raising the effective retirement age. Thus, various arguments call for more investment not only in vulnerable groups (see above) but in the population at large. Creating the institutional arrangements that facilitate the investment in people in an increasingly flexible labor market is one of the greatest challenges facing the Dutch economy in the coming years.

4. Raising the number of hours worked

The number of hours worked per Dutch person is low by international standards (see Table 5). Hence, the participation rate in terms of hours is still low (see Figure 14). To

Figure 14 Participation rate in hours: Actual hours worked/potential annual hours[a] worked



[a]Potential annual hours worked = labor supply in persons *48 weeks *40 hours
Source: Maddison, 1991, 1995; Pilat, 1996; DIW, CPB

encourage labor supply and boost the tax base of the government, a further reduction in the overall tax burden would be welcome. A lower aggregate tax burden would reconcile the need to, on the one hand, increase the access to work of low-skilled labor by reducing tax rates on lower incomes and, on the other hand, encourage workers to increase their working hours by reducing marginal tax rates. Indeed, as individuals become more flexible in selecting their own working hours, high marginal tax rates become more distortionary. In this connection, lower marginal tax rates could help to facilitate a further expansion of female labor supply. There still is substantial room to raise the female participation rate, especially in the number of hours. Survey information does indeed indicate that many women would like to work more hours. Also better child-care facilities would facilitate this process.

Lessons from the Dutch model

Break the vicious circle

The Dutch experience reveals the importance of breaking the vicious circle of more inactivity, higher spending on social insurance, premium increases, higher labor costs, and more employment reductions. If the vicious circle is allowed to run along for an extended period, it leaves a hard core of long-term unemployed and benefit recipients drawing on open-ended social security benefits. Consequently, stopping this vicious circle takes a long time.

Protect profitability

The share of profits in enterprise income is an important guidepost in determining the appropriate levels of wages. If profitability is low, wage moderation is an important instrument in boosting employment.

Is wage moderation also an important instrument to stimulate employment in the larger EU countries or will it result in a recession? CPB's world model (WEB) suggests that wage moderation can be effective also in a large country. Simulations with this model show that wage moderation associated with a decline in the natural rate of unemployment does not generate much foreign demand in a large economy less dependent on foreign trade. However, wage moderation is effective in boosting domestic demand through the channels of lower interest rates, lower inflation, higher profitability, and, eventually, more wage earners. Indeed, whereas monetary policy in the Netherlands is tied by the fixed exchange rate policy vis-à-vis the D-mark, wage moderation in a large economy (or in Europe as a whole) allows a more expansionary monetary policy to offset the smaller contribution of foreign demand. Moreover, in a large economy, there is less demand leakage to other economies than there is in a small open economy. Hence, a large economy has to absorb fewer losses in terms of trade to stimulate demand.

Implement institutional reform

Wage moderation needs to be supported by institutional reform aimed at reducing the natural rate of unemployment. This includes lower replacement rates, lower tax rates, and more flexible labor and commodity markets. It includes also tight eligibility criteria as well as a more efficient administration of social security. Indeed, the Dutch reform process increasingly involved fundamental changes in incentive and institutional structures. The emphasis gradually changed from macroeconomic policy and ad-hoc measures towards fundamental changes in (microeconomic) incentive structures. Now that inactivity is concentrated among specific vulnerable groups, these microeconomic policies are becoming increasingly important.

Markets in social insurance

It is still too early to evaluate the recent market-oriented reforms in disability and sickness insurance in the Netherlands. These reforms are likely to provide useful lessons for other countries in reforming their social insurance systems. The proposed Dutch system of disability and sickness insurance can be seen as a mix of coordination through control and competition. The statutory benefits are determined by the political process. Moreover, several regulations protect the position of vulnerable groups. A pragmatic mix of control and competition helps to exploit the strengths of both coordination mechanisms. Also the pragmatic combination of central broad guidelines and decentralized execution in industrial relations has served the Netherlands well.

A pragmatic mix

This pragmatic mix illustrates a broader principle. A panacea for the unemployment problem is not available. Hence, countries should rely on a broad range of measures. Employing several instruments is attractive also for political reasons: costs and benefits are spread over several groups, thereby protecting social cohesion. Moreover, by using both carrots and sticks, governments prevent the alienation of specific groups. To illustrate, to reduce the claims of low-skilled workers on social security, the government can combine the stick of lower unconditional benefits, aimed at raising supply, with the carrot of tax cuts and deregulation of sheltered sectors, aimed at raising the demand for low-skilled labor.

Taking action on several fronts also diversifies risks. Indeed, the process of social innovation is a process of trial and error in the face of current problems and newly emerging trends. Finally, policies are often complementary in the sense that the effect of each policy is greater when it is implemented together with other policies than when it is introduced in isolation.

A flexible labor market

A flexible labor market can meet the needs of both employers and employees. Technological and organizational developments and a more heterogeneous society demand more flexibility and tailor-made solutions.

Fiscal policy in a medium-term framework

The present government has drawn two lessons from the experience of fiscal policy in the late eighties and the early nineties. First, fixed targets for cuts in the fiscal deficit, although needed in the eighties to cut the excessive fiscal deficit, make fiscal policy rather sensitive to the business cycle. Second, a fiscal program based on a medium-term forecast for the economy can seriously disrupt the budgetary process if growth turns out to be slower than anticipated. In order to avoid unrest in the budgetary process and better control spending, the present government has set a ceiling on public spending and estimated receipts on the basis of a cautious economic scenario. In this way, the fiscal deficit is allowed to fluctuate with the business cycle up to a certain ceiling. These innovations have contributed to a more predictable, cyclically neutral, fiscal policy, thereby contributing to confidence in the private sector.

Conclusions

Is there a Dutch miracle? As with a lot of miracles, the Dutch miracle disappears to a large extent when it is scrutinized. Still, the Dutch experience yields several lessons, not least for the Netherlands itself. The switch from macroeconomic to microeconomic policy is still in full swing.

Adapting institutions and incentive structures to newly emerging trends has to be a continuous process. Not only do exogenous trends demand adjustments, but also endogenous unintended responses to policies usually become apparent and fully understood only after some time. Both the inadequate response of Dutch economic policy in the seventies to the change of times and the fundamental and persistent reform process that started in the early eighties show the importance of anticipating trends and gaining insight into how the economy functions. Economic ideas, when communicated clearly, do matter. By anticipating future trends, economic policymakers can reconcile stability and social cohesion with timely adjustments to new circumstances. This is the continuous challenge for policymakers all over the world.

Notes

[1] This article is based on a contribution to the Economic Policy Roundtable of the Centre for Economic Policy Research (CEPR) in Amsterdam on May 12, 1997. The author would like to thank two referees and numerous colleagues for comments on this paper. In particular, Hans Roodenburg, Marc Pomp, Adri den Ouden, Rudy Douven, Maya Verhoeve, and Erwin Zijlerman contributed in important ways to this article. Of course, the author remains responsible for any errors.

[2] The level of GDP per hour worked, however, is still very high compared to other EU countries and matches that in the United States.

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