

The
Economist

SPECIAL REPORT
THE NORDIC COUNTRIES

February 2nd 2013

Northern lights



Northern lights

The Nordic countries are reinventing their model of capitalism, says Adrian Wooldridge

THIRTY YEARS AGO Margaret Thatcher turned Britain into the world's leading centre of "thinking the unthinkable". Today that distinction has passed to Sweden. The streets of Stockholm are awash with the blood of sacred cows. The think-tanks are brimful of new ideas. The erstwhile champion of the "third way" is now pursuing a far more interesting brand of politics.

Sweden has reduced public spending as a proportion of GDP from 67% in 1993 to 49% today. It could soon have a smaller state than Britain. It has also cut the top marginal tax rate by 27 percentage points since 1983, to 57%, and scrapped a mare's nest of taxes on property, gifts, wealth and inheritance. This year it is cutting the corporate-tax rate from 26.3% to 22%.

Sweden has also donned the golden straitjacket of fiscal orthodoxy with its pledge to produce a fiscal surplus over the economic cycle. Its public debt fell from 70% of GDP in 1993 to 37% in 2010, and its budget moved from an 11% deficit to a surplus of 0.3% over the same period. This allowed a country with a small, open economy to recover quickly from the financial storm of 2007-08. Sweden has also put its pension system on a sound foundation, replacing a defined-benefit system with a defined-contribution one and making automatic adjustments for longer life expectancy.

Most daringly, it has introduced a universal system of school vouchers and invited private

schools to compete with public ones. Private companies also vie with each other to provide state-funded health services and care for the elderly. Anders Aslund, a Swedish economist who lives in America, hopes that Sweden is pioneering "a new conservative model"; Brian Palmer, an American anthropologist who lives in Sweden, worries that it is turning into "the United States of Swedeamerica".

There can be no doubt that Sweden's quiet revolution has brought about a dramatic change in its economic performance. The two decades from 1970 were a period of decline: the country was demoted from being the world's fourth-richest in 1970 to 14th-richest in 1993, when the average Swede was poorer than the average Briton or Italian. The two decades from 1990 were a period of recovery: GDP growth between 1993 and 2010 averaged 2.7% a year and productivity 2.1% a year, compared with 1.9% and 1% respectively for the main 15 EU countries.

For most of the 20th century Sweden prided itself on offering what Marquis Childs called, in his 1936 book of that title, a "Middle Way" between capitalism and socialism. Global companies such as Volvo and Ericsson generated wealth while enlightened bureaucrats built the *Folkhemmet* or "People's Home". As the decades rolled by, the middle way veered left. The government kept growing: public spending as a share of GDP nearly doubled from 1960 to 1980 and peaked at 67% in 1993. Taxes kept rising. The Social Democrats (who ruled Sweden for 44 uninterupt-



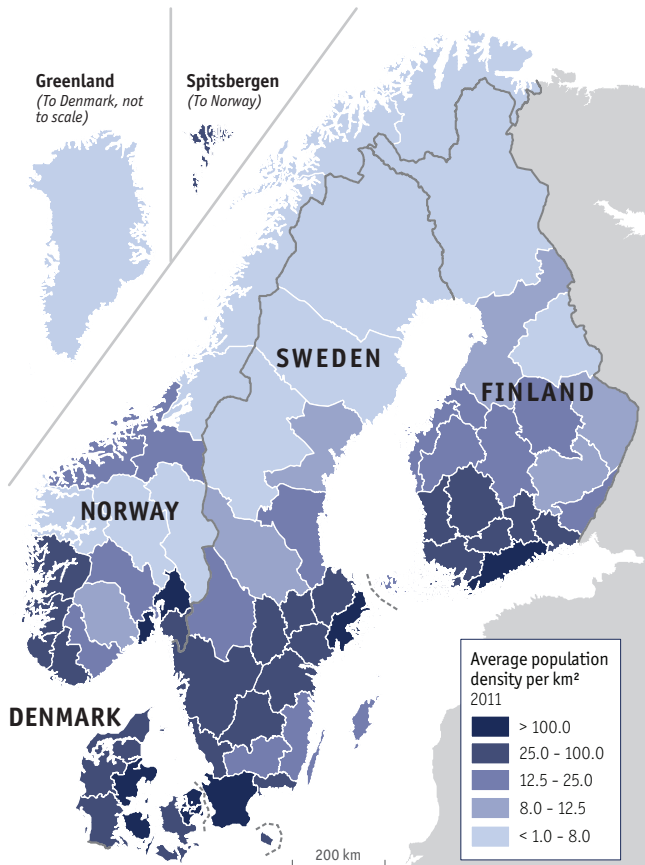
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ACKNOWLEDGMENTS

In addition to the people mentioned in the text, the author would like to express his thanks for their help with this special report to: Matti Alahuhta, Andreas Alsen, Jorn Bang Andersen, Ulf Berg, Ewa Bjorling, Pontus Braunerhjelm, Maria Levin Erixon, Saeid Esmaelzadeh, Magnus Gulbrandsen, Jonas Gustavsson, Mauro Gozzo, Jouko Hayrinen, Magnus Henrekson, Cecilia Hermannson, Kari Herlevi, Anders Hoffmann, Per-Ola Karlsson, Hannu Kosonen, Stefan Larsson, Erling Roed Larsen, Bengt-Ake Ljuden, Jacob Mchangama, Peter Olesen, Mrikka Paananen, Petri Peltonen, Magnus Runnbeck, Ola Pettersson, Parsi Sahlberg, Peter Santesson, Oystein Sjolie, Karin Svanborg-Sjovall, Alexander Triebnigg, Erik Ullenhag, Frederik Verneresson, Hans Vestberg, Pekka Viljakanen and Jacob Warburg.

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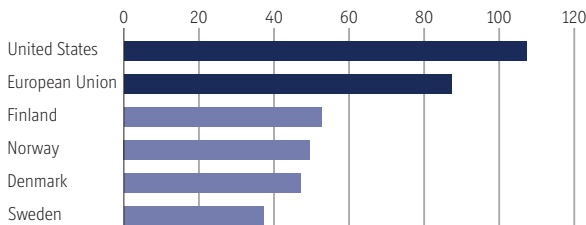


	Population 2012, m	GDP per person 2012, \$'000	GDP, average annual growth rate 2002-12, %
Denmark	5.6	55.4	0.6
Finland	5.4	45.5	1.6
Norway	5.0	99.3	1.6
Sweden	9.5	54.9	2.2

All figures are estimates

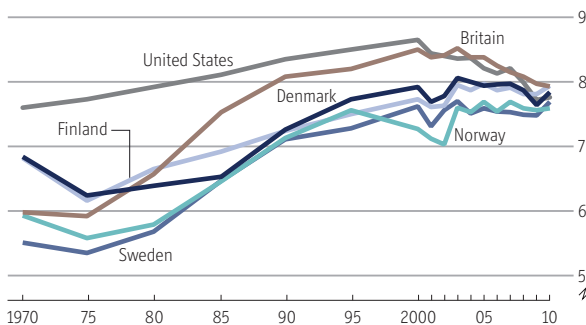
Gross government debt

As % of GDP, 2012 estimate



Economic-freedom ratings

10=maximum



Sources: IMF; national sources; Nordregio & NLS Finland; Fraser Institute; OECD

ed years from 1932 to 1976 and for 21 out of the 24 years from 1982 to 2006) kept squeezing business. "The era of neo-capitalism is drawing to an end," said Olof Palme, the party's leader, in 1974. "It is some kind of socialism that is the key to the future."

The other Nordic countries have been moving in the same direction, if more slowly. Denmark has one of the most liberal labour markets in Europe. It also allows parents to send children to private schools at public expense and make up the difference in cost with their own money. Finland is harnessing the skills of venture capitalists and angel investors to promote innovation and entrepreneurship. Oil-rich Norway is a partial exception to this pattern, but even there the government is preparing for its post-oil future.

This is not to say that the Nordics are shredding their old model. They continue to pride themselves on the generosity of their welfare states. About 30% of their labour force works in the public sector, twice the average in the Organisation for Economic Development and Co-operation, a rich-country think-tank. They continue to believe in combining open economies with public investment in human capital. But the new Nordic model begins with the individual rather than the state. It begins with fiscal responsibility rather than pump-priming: all four Nordic countries have AAA ratings and debt loads significantly below the euro-zone average. It begins with choice and competition rather than paternalism and planning. The economic-freedom index of the Fraser Institute, a Canadian think-tank, shows Sweden and Finland catching up with the United States (see chart). The leftward lurch has been reversed: rather than extending the state into the market, the Nordics are extending the market into the state.

Why are the Nordic countries doing this? The obvious answer is that they have reached the limits of big government. "The welfare state we have is excellent in most ways," says Gunnar Viby Mogensen, a Danish historian. "We only have this little problem. We can't afford it." The economic storms that shook all the Nordic countries in the early 1990s provided a foretaste of what would happen if they failed to get their affairs in order.

There are two less obvious reasons. The old Nordic model depended on the ability of a cadre of big companies to generate enough money to support the state, but these companies are being slimmed by global competition. The old model also depended on people's willingness to accept direction from above, but Nordic populations are becoming more demanding.

Small is powerful

The Nordic countries have a collective population of only 26m. Finland is the only one of them that is a member of both the European Union and the euro area. Sweden is in the EU but outside the euro and has a freely floating currency. Denmark, too, is in the EU and outside the euro area but pegs its currency to the euro. Norway has remained outside the EU.

But there are compelling reasons for paying attention to these small countries on the edge of Europe. The first is that they have reached the future first. They are grappling with problems that other countries too will have to deal with in due course, such as what to do when you reach the limits of big government and how to organise society when almost all women work. And the Nordics are coming up with highly innovative solutions that reject the tired orthodoxies of left and right.

The second reason to pay attention is that the new Nordic model is proving strikingly successful. The Nordics dominate indices of competitiveness as well as of well-being. Their high scores in both types of league table mark a big change since the 1980s when welfare took precedence over competitiveness.

The Nordics do particularly well in two areas where competitiveness and welfare can reinforce each other most power- ➤

► fully: innovation and social inclusion. BCG, as the Boston Consulting Group calls itself, gives all of them high scores on its e-intensity index, which measures the internet's impact on business and society. Booz & Company, another consultancy, points out that big companies often test-market new products on Nordic consumers because of their willingness to try new things. The Nordic countries led the world in introducing the mobile network in the 1980s and the GSM standard in the 1990s. Today they are ahead in the transition to both e-government and the cashless economy. Locals boast that they pay their taxes by SMS. This correspondent gave up changing sterling into local currencies because everything from taxi rides to cups of coffee can be paid for by card.

The Nordics also have a strong record of drawing on the talents of their entire populations, with the possible exception of their immigrants. They have the world's highest rates of social mobility: in a comparison of social mobility in eight advanced countries by Jo Blanden, Paul Gregg and Stephen Machin, of the London School of Economics, they occupied the first four places. America and Britain came last. The Nordics also have exceptionally high rates of female labour-force participation: in Denmark not far off as many women go out to work (72%) as men (79%).

Flies in the ointment

This special report will examine the way the Nordic governments are updating their version of capitalism to deal with a more difficult world. It will note that in doing so they have unleashed a huge amount of creativity and become world leaders in reform. Nordic entrepreneurs are feeling their oats in a way not seen since the early 20th century. Nordic writers and artists—and indeed Nordic chefs and game designers—are enjoying a creative renaissance.

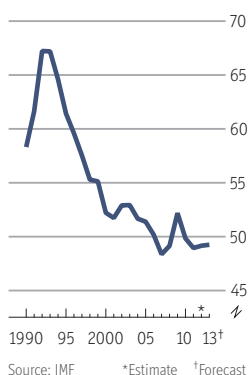
The report will also add caveats. The growing diversity of Nordic societies is generating social tensions, most horrifically in Norway, where Anders Breivik killed 77 people in a racially motivated attack in 2011, but also on a more mundane level every day. Sweden is finding it particularly hard to integrate its large population of refugees.

The Nordic model is still a work in progress. The three forces that have obliged the Nordic countries to revamp it—limited resources, rampant globalisation and growing diversity—are gathering momentum. The Nordics will have to continue to upgrade their model, but they will also have to fight to retain what makes it distinctive. Lant Pritchett and Michael Woolcock, of the World Bank, have coined the term “getting to Denmark” to describe successful modernisation. This report will suggest that the trick is not just to get to Denmark; it is to stay there.

The final caveat is about learning from the Nordic example, which other countries are rightly trying to do. Britain, for example, is introducing Swedish-style “free schools”. But transferring such lessons is fraught with problems. The Nordics’ success depends on their long tradition of good government, which emphasises not only honesty and transparency but also consensus and compromise. Learning from Denmark may be as difficult as staying there. ■

It can be done

Sweden's government spending
As % of GDP



Welfare

More for less

A generous welfare state that does not cost the earth

IN “THE LION AND THE UNICORN”, written in 1941, George Orwell invoked the spirit of England in a handful of images—“solid breakfasts and gloomy Sundays, smoky towns and windy roads, green fields and red pillar-boxes”. When this correspondent tried to summon up appropriate images for the spirit of the Nordic region he found himself turning to the welfare state: Swedish fathers enjoying a leisurely lunch while their children sleep in prams (Sweden’s paternity leave is among the most generous in the world); Danish mothers cycling, helmetless, through the early morning mist with their children in sidecars (Copenhagen has more than 350km of cycle lanes, and a third of the population cycles to work); a Finnish physics teacher discussing the nature of elegance with a class of 15-year-olds (Finland regularly comes near the top of international league tables for educational attainment).

The Nordics still have the world’s most generous welfare states, but a succession of crises put an end to the region’s magical thinking about welfare. Denmark went into freefall in the early 1980s. Finland imploded in the early 1990s when the collapse of communism killed its most reliable market. Sweden and Norway faced serious financial crises at about the same time. These events are still fairly fresh in people’s memories.

Policymakers responded to these near-death experiences by changing their habits, above all by putting their budgets back into balance. The Swedes, for instance, reduced their national debt from 84% of GDP in 1996 to 49% in 2011. They also tackled entitlements to take account of ageing populations. In 1998 Sweden passed the most sweeping pension reform in any rich country, replacing a defined-benefit system with a defined-contribution one and bringing pensions more in line with lifetime incomes.

Denmark has been slower than Sweden to clean out its closets. Public spending as a proportion of GDP increased from 51% to 58% after the 2007-08 financial crisis and is now the highest in the OECD. But the pace of reform is speeding up. In 2006 Denmark increased the state pension age from 65 to 67, to be phased in by 2024-27. In 2010 it halved the upper limit on paying out unemployment benefit from four to two years. In 2011 it hastened the demise of an early-retirement scheme which gave some people the option to leave at 60. In 2012 it announced plans to increase the differential between wages and benefits.

Welfare capitalism

Even more striking than the Nordic world’s commitment to balancing its books is its enthusiasm for experimenting with new ideas. The Swedish state now allows private companies to compete with government bodies for public contracts. The majority of new health clinics and kindergartens are being built by private companies, frequently using private money. The state also allows citizens to shop around for the best services and take the money with them.

The Swedes have done more than anyone else in the world to embrace Milton Friedman’s idea of educational vouchers—allowing parents to send their children to whatever school they choose and inviting private companies or voluntary groups to establish “free” schools. Almost half the country’s schoolchil- ►►



The Finns have one of the world's most successful educational systems without so much as a nod to Friedman

wheelchairs from the same old provider it now plans to order “mobility solutions” from competing companies and then encourage the most successful ones to export their products. “We need to learn how to make businesses out of things that we want to do for political reasons,” says Lars Andersen, head of the Economic Council of the Labour Movement, a think-tank.

It would be an exaggeration to describe these welfare reforms as a triumph for Friedmanism. The most comprehensive study of school reform in Sweden demonstrates that choice has had a positive effect. Anders Bohlmark and Mikael Lindahl examined data for all Swedish schoolchildren between 1988 and 2009 and found that increasing the share of “free” schools in a particular district leads to better performance on a variety of measures, from school grades to university

attendance. The biggest gains are recorded in the regular public schools rather than in the “free” schools. At the same time, though, Sweden’s ranking in the OECD’s annual PISA tables on educational achievement has declined. The Swedish press is full of stories about the misdeeds of private schools and hospitals. Private companies have promised to generate profits year in, year out, particularly if they are backed by private-equity companies; but after the first wave of rationalisation it often becomes more difficult to squeeze savings out of schools and hospitals.

The Finns have one of the world’s most successful educational systems (as measured by the PISA tests) without so much as a nod to Friedman. They have dispensed with the machinery of educational accountability such as detailed national curriculums, school inspections, high-stakes examinations and school vouchers. All children attend comprehensive school from age seven to 16; there is no break between primary and secondary school. Teachers experiment with lots of different styles of teaching but tend to emphasise creativity and group learning. They make extensive use of tests, but only to diagnose students rather than to classify them.

Yet the Finns have also dispensed with many of the shibboleths of the educational left. At age 16 they rigorously divide children up between academic and vocational streams. And they do not spend a huge amount on education: 6.4% of GDP in 2009, compared with 7.3% in America. Finnish teachers talk enviously about how much their British colleagues are paid.

Finland’s success depends neither on accountability (the right-wing panacea) nor on resources (the left-wing one) but on two things that are ignored in the wider educational debate: trust and stability. The government has found it possible to attract high-quality people into a relatively low-paid profession provided they are treated with respect. Teachers are free to design their own curriculums and develop their own tests. And the system has remained almost unchanged since the early 1970s.

Controlling public spending is the hardest job in politics. The Nordics have succeeded because of their willingness to focus on results rather than on ideologies. Still, there is a limit to what pragmatism can achieve. The Nordic countries continue to suffer from what Mitt Romney, the Republican candidate in America’s recent presidential election, called “trickle-down government”. They are run by professional politicians who have no idea that mandating a year’s maternity leave means one thing for a government department and another for a start-up. ■

► dren choose not to go to their local schools. More than 10% of students under 16 and more than 20% of those over 16 attend “free” schools, two-thirds of which are run by private companies.

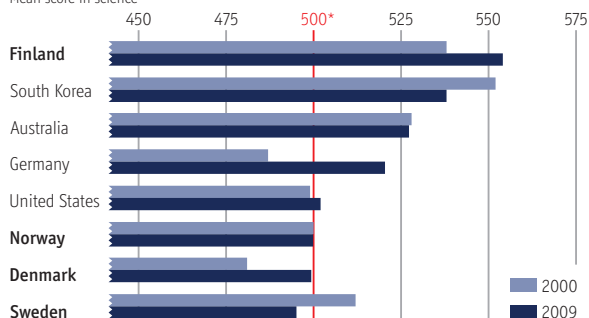
Denmark has added a useful twist to the voucher idea. It not only allows parents to take their public funds to private schools with them but also to top them up (within limits) with their own money. This is creating a flourishing market, particularly in Copenhagen, ranging from academic schools for traditionalists via religious ones for Muslims to experimental ones for ageing hippies. “One of the most popular entertainments in Denmark”, says Mr Mogensen, the historian, “is to spot the latest left-wing politicians to send their children to private school.”

In the workplace Denmark is a pioneer of flexicurity: companies can sack employees with almost American ease but the government provides displaced workers with generous benefits and helps them get new jobs. Most employers like the system because it frees them from one of continental Europe’s biggest problems: a dual labour market divided between heavily protected insiders and casualised outsiders.

Denmark is also a pioneer of what might be called the intelligent state. The government abandoned its fat tax which was intended to nudge people into leading healthier lives because the results were disappointing. But it is also using its purchasing power to encourage innovation: for example, instead of ordering

Fabulous Finns

Education performance of 15-year-olds, selected countries
Mean score in science



Source: OECD PISA

*Mean PISA score for all countries

Immigrants

The ins and the outs

Immigration and growing inequality are making the Nordics less homogeneous

IN 1965 SWEDEN'S Social Democratic Party embarked on the Million Programme, an ambitious plan to build a million new homes in a country of only 7.7m people. These homes had everything that good democratic citizens could want—all mod cons, easy access to public services and green spaces.

The government exceeded its target by 6,000, but in other respects the Million Programme went awry. Swedish workers quickly showed what they thought of the new homes—many of them high-rise blocks of flats on the edge of cities—by skedaddling at the first opportunity. In the 1980s the Million homes were filled by guest workers from the Balkans and Greece. Today, as the guest workers skedaddle in turn, they are being filled by refugees from the world's trouble spots.

Rosengård was once one of the programme's proudest achievements: a high-rise development that was close to the centre of Malmö, one of Sweden's industrial powerhouses, but surrounded by open space. Today over 80% of its population of 24,000 are immigrants. The local shops have names such as Babylon and Lebanon. Women in hijabs and headscarves cart their shopping through the freezing rain. Men sit in cafés drinking strong coffee and keeping dry. A truck sells falafel sandwiches.

The Swedish state does its best to reach out to these immigrants. The city of Malmö's crest is everywhere. The local library has a language café and a chess room. A sports complex includes a swimming pool and a boxing ring. People in red jackets marked "Rosengård hosts"—most of them immigrants themselves—help residents negotiate the complexities of the welfare state.

Yet the relationship between the state and its clients is strained. "In Sweden having a job is everything," says Tobias Billström, the minister for immigration and a former MP for Malmö; but in Rosengård only 38% of the residents have one. Angry youths have taken to rioting, torching bicycle sheds and recycling centres as well as cars.

Per Brinkemo is a former journalist whose life was changed when he wrote a book about a Somali boy who was brought up in war-torn Mogadishu. He now runs an organisation that specialises in helping Somali refugees from the basement of a Rosengård block of flats. The centre's walls are decorated with pictures of high-ranking visitors and prizes awarded to Mr Brinkemo. But he is no fan of government policies, pointing out that politicians have little sense of how difficult it is to integrate Somalis into Swedish society. They hail from nomadic societies where trust is reserved for the clan, literacy is rare and timekeeping is rudimentary. Three-quarters of Somali children drop out of school. "For Somali immigrants [coming to Sweden] is like being transported to Mars," he says.

The sums that don't add up

Mass immigration is posing serious problems for the region. For the Nordic countries to be able to afford their welfare states they need to have 80% of their adults in the workforce, but labour-force participation among non-European immigrants is much lower than that. In Sweden only 51% of non-Europeans have a job, compared with over 84% of native Swedes. The Nordic countries need to persuade their citizens that they are getting a good return on their taxes, but mass immigration is creating a class of people who are permanently dependent on the state.

Torben Tranaes, of Denmark's Rockwool Foundation Research Unit, calculates that in the mid-1990s immigrants in their 40s—the age group that generally contributes most to the public budget—paid only marginally more in taxes than they received in benefits. In Sweden 26% of all prisoners, and 50% of prisoners serving more than five years, are foreigners. Some 46% of the jobless are non-Europeans, and 40% of non-Europeans are classified

as poor, compared with only 10% of native Swedes. Immigrants are so closely associated with the Million Programme, and hence with public housing, that the *Gringo*, a Stockholm newspaper for immigrants, calls them *Miljonsvenskar*, or "Million Swedes".

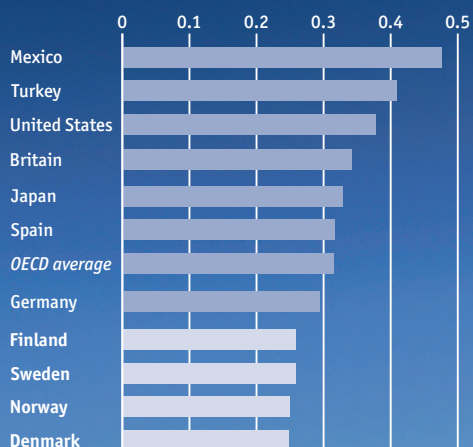
High immigration is threatening the principle of redistribution that is at the heart of the welfare state. Income inequalities in the Nordic countries are generally lower than elsewhere (see chart, next page), but Matz Dahlberg, of Uppsala University, reckons that immigration is making people less willing to support redistribution. The decline is particularly marked among high-income earners. Immigration is also causing culture clashes. Nordics fervently believe in liberal values, especially sexual equality and freedom of speech, but many of the immigrants come from countries where men and women are segregated and criticising the prophet Muhammad is a serious offence. Peaceful Denmark found itself on the front-line of the culture wars when *Jyllands-Posten*, a newspaper, published cartoons making fun of Muhammad. ►►



Out in the cold

Egalitarians all

Gini coefficient of income inequality*
Selected countries, late 2000s



Source: OECD

*0=perfect equality, 1=perfect inequality



opposite its entrance is an establishment calling itself a “facelift centre”. Designer houses cluster around its base. Green’s supermarket sells local organic food and advertises yoga classes and tango lessons on the beach.

Thirty years ago Malmö was the capital of working-class Sweden, a no-nonsense city dominated by solid citizens who worked in the Kockums shipyard and voted for the Social Democratic Party. Then the global economy turned against it. The shipyards contracted and the local factories and textile mills closed. The once-dominant working class shrank to near-invisibility and the population split between professionals living in designer lofts and refugees living in Rosengård’s high-rises. The giant Kockums crane that had become the city’s symbol in 1974 was dismantled and sent to South Korea in 2002. In 2005 the Turning Torso became the city’s new landmark.

The decline of the working class and the increasing polarisation of professionals and immigrants is being repeated across the region. The Nordic countries are still among the world’s most equal, and in one important respect they are becoming more so. In 2010-11 around 60% of university graduates in Finland and Sweden were women. Sweden has almost as many female as male MPs. In Denmark the prime minister and a raft of other ministers are women.

But in other respects money is making the Nordics less equal. As a proportion of the economy, Sweden’s private-equity industry is second only to Britain’s in Europe, and Norway is awash with oil money. Some of the new rich are splashing out on Porsches and big houses, but most prefer to spend their money in subtler and less conspicuous ways. Even so, they live in a different world from the immigrants stuck in Rosengård. ■

Business

Global niche players

Nordic companies have coped well with globalisation, but need new blood

NOVO NORDISK HAS the sheen of a global champion. Its corporate headquarters near Copenhagen is decorated with freshly cut flowers and thought-provoking sculptures, with little bowls of fruit and nuts dotted here and there. The CEO and his fellow executives work from a large open-plan office.

That is all as it should be. Novo produces half the world’s medical insulin and frequently generates shareholder returns approaching 30%. The world market for insulin is growing fast: about 346m people already suffer from diabetes and the number will grow as the emerging world gets richer. Novo is well placed to remain the world’s leading insulin producer for years to come.

The Vikings’ modern descendants believe they can turn globalisation to their advantage. They excel at producing born-global companies. Ericsson, founded in 1876, started selling phones in China in the 1890s. They also outperform more muscular competitors. Torben Pedersen, of the Copenhagen Business School, points out that Nordic countries are past masters at adjusting to rules dictated by big countries such as Germany or America. Surely they can cope with China and India?

Alas, the logic that destroyed brawnwork such as shipbuilding and textile manufacturing is now moving on to brainwork. The best Nordic companies are transforming themselves from export machines into global networks. Ericsson, for exam- ►►

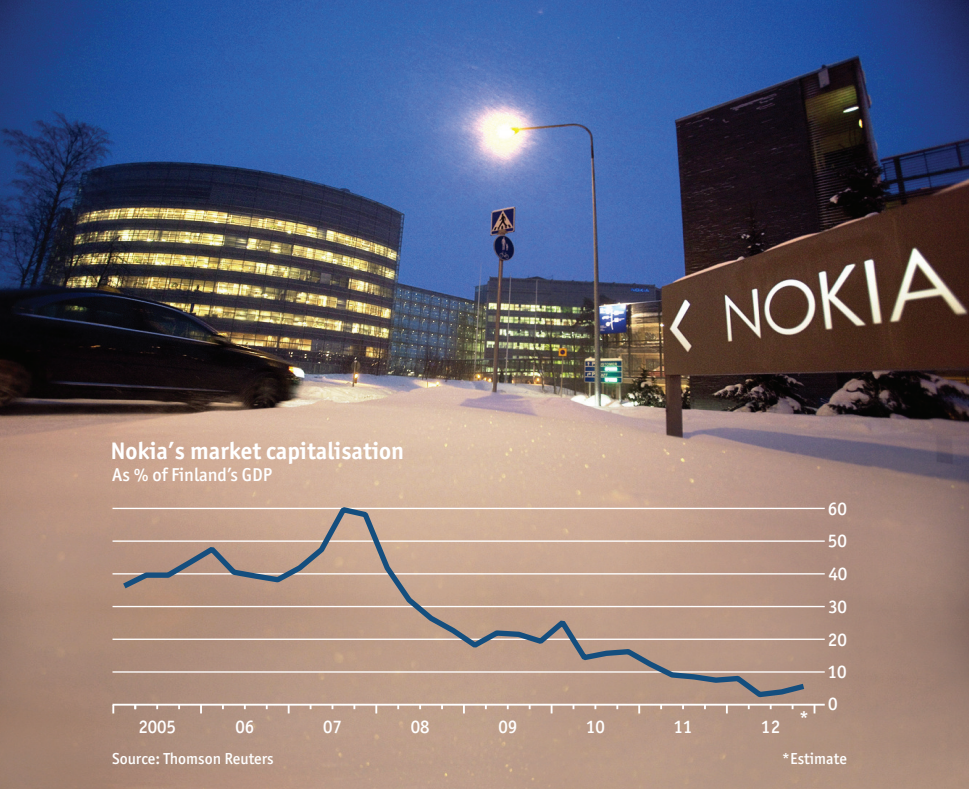
► Immigration has divided the Nordics. The Swedes regard their open-armed approach to asylum-seekers as an expression of what is best in their culture. The Danes revisited their immigration policies in 1999, spurred by the rise of the anti-immigrant Danish People’s Party. They tightened the rules for family reunification, made it more difficult for newcomers to claim benefits and set up an integration ministry. Today Denmark receives more non-European immigrants than ever, but it has radically reduced the number of refugees while increasing the number of people on student and work visas.

The biggest battle is within the Nordic mind. Is it more progressive to open the door to refugees and risk overextending the welfare state, or to close the door and leave them to languish in danger zones? Is it more enlightened to impose secular values on devout Muslims or to dilute liberal values in the name of multiculturalism? Trying to reconcile these contradictions can lead to strange results. Alarmed by reports of female genital mutilation, Nyamko Sabuni, a Swedish cabinet minister, suggested compulsory gynaecological examinations for all young girls in Sweden.

Liberals are increasingly on the defensive. The number of immigration-related attacks is rising. In 2010 Taimour Abdulwahab al-Abdaly blew himself up in the middle of a crowd of Christmas shoppers in central Stockholm; remarkably, he managed to injure only a couple of people. In Sweden median household incomes of non-European immigrants are now 36% lower than for native-born Swedes, whereas in 1991 they were only 21% lower. But Denmark’s much-vilified immigration reforms may be paying off: the employment gap between native Danes and non-Western immigrants has declined to 24 percentage points, compared with 42 in the mid-1990s.

Sweden is now allowing in more skilled workers, having previously combined highly restrictive policies for this group with the world’s most generous policies for refugees. Trade unions used to have a veto over who was admitted and repeatedly used it. This may calm the immigration debate, but it may equally well increase the pressure to open the doors even wider for skilled immigrants while closing them for refugees.

A 20-minute drive from Rosengård to the western harbour takes the visitor to the Turning Torso, a high-rise, high-spec block that twists like a lithe athlete and commands spectacular views over the Oresund bridge linking Malmö to Copenhagen. Directly



► ple, has reduced the number of workers it employs in Sweden from 31,000 in 2001 to 18,000 today. Medium-sized companies are taking advantage of low production costs in the Baltic states as well as in China and India. In turn, foreigners are invading the Vikings' strongholds. Volvo, Sweden's famed car company, has been swallowed by a Chinese upstart, Geely. Danisco, a Danish food-ingredients company, has been taken over by America's DuPont. Ericsson has sold its handset division to Sony. Nokia is a shadow of its former self.

The Nordic countries have an impressive number of globally competitive companies. Denmark is a world leader in hearing aids (Oticon), shipping (Maersk), toys (Lego), drink (Carlsberg) and windpower (with more than 200 companies that account for a third of the world's wind-turbine market). Novo Nordisk is at the centre of a biotech cluster, dubbed Medicon Valley, that stretches from Copenhagen to Malmö in neighbouring Sweden and has an annual turnover of €13.4 billion.

Sweden boasts some world-class manufacturing companies, particularly in mining equipment and machine tools (Sandvik and Atlas Copco), as well as retail stars such as IKEA and H&M. Finland's Kone is one of the world's leading lift and escalator companies. Nokia's problems are being offset by the rise of electronic-games makers such as Rovio, the creator of Angry Birds. Norway is a world leader in oil services and fish farming.

Nordic companies have thrived in well-defined global niches. Lego dominates the market for interlocking bricks. Sandvik is a machine-tool superpower. Volvo Trucks produces the world's best high-quality lorries. Nichification protects high-cost companies from emerging-market competitors. Nobody wants the cheapest machine-tool when a defective one can cause millions of pounds-worth of damage.

They owe their success to four qualities. The first is their commitment to relentless innovation which they apply to even the most basic industries. Tiny Denmark remains the world's eighth-biggest food exporter thanks to its obsession with productivity. Danish farmers use implanted chips to monitor their cows to maximise their milk yield. KJ Industries has developed a way of mechanising the carving up of carcasses by programming the cutting machines with the help of x-rays.

Nordic companies balance their passion for the new with an ability to take the long view. Sweden is still dominated by a

handful of long-established families such as the Wallenbergs and the Bonniers. Denmark has a number of organisations such as the Carlsberg Foundation and the Lego Foundation, set up partly to look after the long-term interests of their parent companies.

The third quality is their consensus-based approach to management. They pride themselves on their flat structures and democratic ways which they feel promote trust and co-operation. BCG thinks the region has the world's most skilled "low-skilled" workers. But they balance co-operation with a fourth quality—a passion for replacing labour with machines. The Copenhagen underground has dispensed with drivers and ticket-sellers. Shops get by on automated checkouts.

To see these forces in action, consider two companies in different industries. Sandvik started making steel in the late 19th century in the small town of Sandviken, two hours north of Stockholm. It is

now a global giant that produces everything from machine tools to steel rods for nuclear reactors. Sandvik's small-town roots have not prevented it from becoming a global leader in its core businesses. "Expanding abroad is how we save jobs at home" is a common refrain.

Sandvik is obsessed by promoting productivity—both its own and its customers'. A giant factory that produces steel rods looks as if it is run by ghosts: four people monitor computer screens in a command centre and a few others patrol the floor. A productivity centre is devoted to pushing forward the frontiers of technology—making the world's fastest drills, for example—and training employees to help customers. The company's mantra is "we sell productivity not products."

Haldor Topsoe founded the company that bears his name back in 1940. Now aged 99, and bright as a button with it, he remains chairman. His company, meanwhile, has grown into a global giant. Mr Topsoe ascribes its success to two things. He found a perfect niche in catalysis. Catalysts accelerate lots of chemical processes that are vital to a modern economy. They are also extremely hard to copy. So demand is growing and barriers to entry are high. He believes that his company benefits from being a family affair, which allows it both to invest for the long term and to take advantage of the global market.

Vulnerable giants

For all their fortifications, the best Nordic companies are nevertheless under assault from two powerful enemies: rich-world rivals and emerging-world upstarts. In 2000 Nokia dominated the mobile-phone business. Scandinavian companies had pioneered the GSM standard for mobile communications and Nokia was the world's biggest producer of handsets. Today it is fighting for its life: since Stephen Elop took over as CEO in 2010, the company has cut a fifth of its workforce. The world's mobile-phone leader was beaten to the discovery of smartphone gold by Apple, a Californian company whose core competence was making computers. Ericsson decided to abandon the handset business in order to focus on making telecoms equipment, but it is now engaged in a mighty battle with Huawei, a Chinese company that did not exist in the early 1980s.

These twin assaults have revealed one of the region's biggest weaknesses: its failure to bring together design and engi- ►►

► neering, two of its core strengths. They have also shown up the downside of two of the region's great virtues, consensus and patience. Consensus-based management can prove a disadvantage when industries are being disrupted by new technologies, and patience can lead to the scrapyard. Nokia put up with a lacklustre CEO for four years. The CEO of Vestas, which specialises in wind power, is still in place even though its stocks have fallen by 90%.

These problems are not insoluble. Ericsson has done better than Nokia in pulling itself out of its tailspin. It is focusing on a defensible global niche, telecommunications networks, and trying to turn itself into a creative hothouse. The company's innovation centre has come up with lots of clever ways to show that "everything that can be connected will be connected." The company is also shifting its emphasis from making equipment to providing services. Its obsession with creativity can be a little trying: does eating your lunch off a table-tennis table really make you more innovative? But Ericsson is a powerful force in the industry—40% of all mobile-phone traffic passes through its networks—and it argues strongly that the market is set to take off.

Even so, the region's best companies are relentlessly moving their activities abroad not just in pursuit of cheaper workers (though that can help) but also in order to be close to the world's most populous markets. Such offshoring exposes the region's biggest weakness: that most of its best companies were founded in the late 19th and early 20th centuries, and that its ability to replenish its corporate stock has declined as the state has got bigger. In California 39 of the state's 100 biggest companies were founded since 1970. In Denmark the number is just three—and one of those three, Bonus Energy, has been taken over by Germany's Siemens. In Sweden the number is just two. A country that prides itself on equality and upward mobility is dominated by a handful of capitalist dynasties.

If the Nordic countries are to generate the high-quality jobs that their citizens regard as their birthright, they need to produce a new generation of successful capitalists. As Karsten Dybvad, the head of the Confederation of Danish Industry, puts it, "you can't keep milking the same cow for ever." ■

Entrepreneurs

If in doubt, innovate

The Nordic region is becoming a hothouse of entrepreneurship

IN 2010 A GROUP of students at Aalto University, just outside Helsinki, embarked on the most constructive piece of student activism in the history of the genre. They had been converted to the power of entrepreneurialism during a visit to the Massachusetts Institute of Technology. When they got home they organised a "summer of start-ups" to spread the word that Finland's future lay with new companies, not old giants. The summer of start-ups turned into a season of innovation.

The Start-Up Sauna—a business accelerator that is still run by young enthusiasts but now funded by government, business and academia—occupies a dilapidated warehouse next to the university. It offers a wide range of services: working space, coaching for budding entrepreneurs, study trips to Silicon Valley and plenty of networking opportunities (including in the Sauna's many saunas).

The Sauna-masters have an understanding of entrepre-

neurship in advance of their years. They recognise that there is more to innovation than high tech: the Sauna also has design and knitting factories. They understand the importance of bridging the gap between engineering and design. They realise that promoting entrepreneurship is a matter of changing culture as much as providing money. They look to Russia and the Baltic states as well as to Boston and San Francisco.

No more Nokias

The student revolution was part of a wider reconsideration of the proper relationship between government and business. This had started in 2008, when the Finnish government shook up the universities (and created Aalto) in an attempt to spur innovation. But it was speeded up by Nokia's problems. Finland had become dangerously dependent on this one company: in 2000 Nokia accounted for 4% of the country's GDP. The government wanted to make the mobile-phone giant's decline as painless as possible and ensure that Finland would never again become so dependent on a single company.

The Finns created an innovation and technology agency, Tekes, with an annual budget of €600m and a staff of 360. They also established a venture-capital fund, Finnvera, to find early-stage companies and help them get established. The centrepiece of their innovation system is a collection of business accelerators, partly funded by the government and partly by private enterprise, that operate in every significant area of business and provide potential high-growth companies with advice and support from experienced businesspeople and angel investors.

As a result, Finland has become much more market- and entrepreneur-friendly. It has produced an impressive number of start-ups, including 300 founded by former Nokia employees. Microtask outsources office work. Zen Robotics specialises in automating recycling. Valkee makes a device that lifts wintry dark moods by shooting bright light into the ear canal. The country has also acquired the paraphernalia of a tech cluster, such as a celebratory blog (Arctic Startup) and a valley-related name (Arctic Valley). The fashionable argument now is that Nokia's decline is "the best thing that ever happened to this country".

The new Finland is particularly proud of its booming video-games industry, including successful companies such as Rovio Entertainment, the maker of Angry Birds and a leading supporter of the Start-Up Sauna, and Supercell, the maker of Clash of Clans. Supercell's employees are what you would expect: men with beards and ponytails who take time out from their computer screens to show off their collections of action figures.

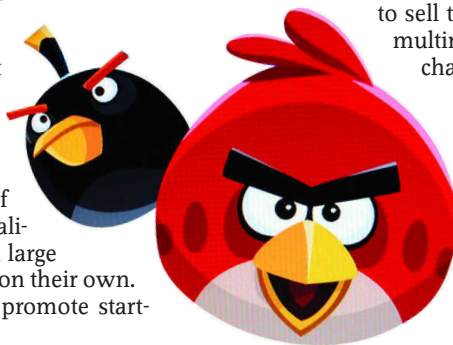
Ilkka Paananen, Supercell's CEO, points out that Finland has spent years preparing for its current success. Helsinki started to host a festival for gamers in the early 1990s. Today the festival is so popular that the organisers have to rent the city's biggest ice-hockey stadium, with room for 13,000, and still turn people away. Kajak University offers courses in video games. Finns have a comparative advantage in the four things that make for great games—blood-soaked storylines (all those sagas), bold design, ace computer programming and what might be politely called "autistic creativity".

The arrival of the iPad and its apps allowed the Finnish industry to break out of its frozen ghetto. Mr Paananen says he now has the wherewithal to build the "company of my dreams". Screens on the wall display how Supercell is doing against its rivals in real time. The games-masters talk about IPOs and "massive growth curves". The company recently moved into new headquarters which, poignantly, used to be Nokia's R&D centre.

The mood reflected in the summer of start-ups can be found across the region: investors everywhere are looking for new opportunities and bright young things are running compa- ►►

► nies in converted warehouses. Hjalmar Winbladh, one of Sweden's leading entrepreneurs, says that the atmosphere has changed completely since he started out in business in the early 1990s. Back then people like him were oddities. Today fashionable young people worship successful tech entrepreneurs such as Niklas Zennström, the co-founder of Skype, and Daniel Ek and Martin Lorentzon, the co-founders of Spotify. Mr Winbladh says that his biggest problem is to attract young talent from other start-ups. They all shudder at the thought of spending their lives in big organisations.

Nordic governments recognise that they need to encourage more entrepreneurs if they are to provide their people with high-quality jobs, and that they can no longer rely on large companies to generate business ecosystems on their own. They are creating government agencies to promote start-



Despite all its entrepreneurial energy, the Nordic region still finds it hard to turn start-ups into enduring companies

ups. They are encouraging universities to commercialise their ideas and generate start-ups. They are telling their schools to sing the praises of entrepreneurship.

Many of the region's most interesting entrepreneurs operate at the low end of the tech spectrum, often to help parents deal with the practical problems of combining full-time work and family. Niklas Aronsson, co-founder of a company called Linas Matkasse, has applied IKEA's do-it-yourself model to family dinners. He delivers bags containing all the ingredients needed for a meal, chopped up and ready to cook—a perfect solution for people who are short of time but prefer not to bring up their children on takeaway pizza.

Monica Lindstedt, founder of Hemfrid, is also in the business of selling time. She has turned her company into a house-cleaning giant, applying professional management to domestic cleaning and turning it into an employment perk. Hemfrid has persuaded the government to treat house-cleaning as a tax-deductible benefit, like a company car. It has also convinced companies that this is a great way to reward their employees and free them from domestic distraction. Hemfrid now has 10,000 regular customers and 1,326 employees, 70% of them born abroad.

Nordic entrepreneurs are also reinventing retirement homes for baby-boomers. A Finnish private housing association, Asunto Oy Helsingin Loppukiri, has built a housing community in the suburbs of Helsinki that is dedicated to the idea of helping people help themselves. The residents took an active part in designing both the buildings' common areas (which include saunas and exercise rooms) and their individual flats. Most of them own shares in the company. It tries to offer a balance between independent living and community involvement. The members eat together once a week and tend a communal allotment whenever they feel like it.

Don't go

Despite all this entrepreneurial energy, the Nordic region still finds it hard to turn start-ups into enduring companies. There are too many examples of successful entrepreneurs who have upped sticks and gone elsewhere. These include not just members of the post-war generation such as Ingvar Kamprad, the

founder of giant IKEA (who lives in Switzerland), and Hans Rausing, the founder of Tetra Pak, a huge packaging company (who went to live in England), but also members of the up-and-coming generation. Mr Zennström, along with many of the brightest Swedish investors and entrepreneurs in his age group, lives in London. Too many successful start-ups still choose to sell themselves to foreign (mainly American) multinationals rather than becoming local champions.

Still, there is reason to hope that the entrepreneurial boom will also produce a new generation of global champions. The region's lifestyle entrepreneurs have a chance of becoming global moguls for the same reason that Mr Kamprad did: because they are riding the wave of demographic change. And the region's high-tech entrepreneurs have a chance of founding enduring companies because they are building up businesses as well as mastering technology.

One example is Rovio Entertainment, which struck gold with Angry Birds, a game that involves catapulting irascible avians at elaborate fortresses constructed by evil pigs. It was downloaded more than 600m times in 2011. Having produced one big hit, most games companies would have started looking for the next one, but instead Rovio set about turning Angry Birds into a brand and extending its reach. It struck licensing agreements with a range of companies to make Angry Birds-branded products, from toys to chocolate to theme parks. It raised capital from outside investors such as Microsoft, which chipped in \$42m. Rovio now has 500 employees in Finland and had a turnover of \$100m in 2011. Michael Hed, the company's CEO, has a traditional corner office, but it is full of stuffed birds and pigs. ■

Creativity

Cultural revolution

One of the world's blandest regions has become one of its most creative

TWENTY YEARS AGO the Nordic region was a cultural backwater. Even the biggest cities were dead after 8pm. The restaurants offered meatballs or pale versions of Italian or French favourites. The region did come up with a few cultural icons such as Ingmar Bergman and Abba, and managed to produce world-class architects and designers even at the height of post-war brutalism. But the few successes served only to emphasise the general dullness.

The backwater has now turned into an entrepot. Stockholm relishes its reputation as one of the liveliest cities in Europe (and infuriates its neighbours by billing itself as "the capital of Scandinavia"). Scandinavian crime novels have become a genre in their own right. Danish television shows such as "The Killing" and "Borgen" are syndicated across the world. Swedish music producers are fixtures in Hollywood. Copenhagen's Noma is one of the world's most highly rated restaurants and has brought about a food renaissance across the region. ►►

► Why has the land of the bland become a cultural powerhouse? Jonas Bonnier, CEO of the Bonnier Group, Sweden's largest media company, thinks that it is partly because new technologies are levelling the playing field. Popular music was once dominated by British and American artists who were able to use all sorts of informal barriers to protect their position. Today, thanks to the internet, somebody sitting in a Stockholm attic can reach the world. Rovio's Michael Hed suggests that network effects are much more powerful in small countries: as soon as one writer cracks the global detective market, dozens of others quickly follow.

All true. But there is no point in giving people microphones if they have nothing to say. The bigger reason why the region's writers and artists—and indeed chefs and game designers—are catching the world's attention is that they are so full of vim. They are reinventing old forms such as the detective story or the evening meal but also coming up with entirely new forms such as video games for iPads.

The cultural renaissance is thus part of the other changes that have taken place in the region. A closed society that was dominated by a single political orthodoxy (social democracy) and by a narrow definition of national identity (say, Swedishness or Finnishness) is being shaken up by powerful forces such as globalisation and immigration. All the Nordics are engaged in a huge debate about their identity in a post-social democratic world. Think-tanks such as Denmark's Cepos flaunt pictures of Milton Friedman in the same way that student radicals once flaunted pictures of Che Guevara. Writers expose the dark underbelly of the old social democratic regime. Chefs will prepare anything under the sun as long as it is not meatballs.

The region's identity crisis is creating a multicultural explosion. The Nordics are scavenging the world for ideas. They continue to enjoy a love-hate relationship with America. They are discovering inspiration from their growing ethnic minorities but are also reaching back into their own cultural traditions. Swedish crime writers revel in the peculiarities of their culture. Danish chefs refuse to use foreign ingredients. A region that has often felt the need to apologise for its culture—those bloodthirsty Vikings! Those toe-curling Abba lyrics! Those naff fishermen's jumpers!—is enjoying a surge of regional pride.

Blood and snow

Over the past decade Scandinavia has become the world's leading producer of crime novels. The two Swedes who did more than anyone else to establish Nordic noir—Stieg Larsson and Henning Mankell—have both left the scene of crime. Larsson died of a heart attack in 2004 before his three books about a girl with a dragon tattoo became a global sensation. Mr Mankell consigned his hero, Kurt Wallander, to Alzheimer's after a dozen bestsellers. But their books continue to be bought in their millions: "Dragon Tattoo" has sold more than 50m, and the Wallander books collectively even more.

A group of new writers, such as Jo Nesbo in Norway and Camilla Lackberg in Sweden, are determined to keep the flame burning. And the crime wave is spreading beyond adult fiction and the written word. Sweden's Martin Widmark writes detective stories for children. Swedish and British television producers compete to make the best version of Wallander. "The Killing" established a new standard for televised crime drama.

The region has a long tradition of crime writing. Per Wahloo and Maj Sjöwall, a Swedish husband-and-wife team, earned a dedicated following among aficionados with their police novels in the 1960s and 1970s. They also established two of Nordic noir's most appealing memes. Martin Beck is an illness-prone depressive who gets to the truth by dint of relentless plodding.



Foraging for fame

The ten Martin Beck novels present Sweden as a capitalist hell-hole that can be saved only by embracing Soviet-style communism (the crime at the heart of the novels is the social democratic system's betrayal of its promise).

Today's crime writers continue to profit from these conventions. Larsson's Sweden, for example, is a crypto-fascist state run by a conspiracy of psychopathic businessmen and secret-service agents. But today's Nordic crime writers have two advantages over their predecessors. The first is that their hitherto homogeneous culture is becoming more variegated and their peaceful society has suffered inexplicable bouts of violence (such as the assassination in 1986 of Sweden's prime minister, Olof Palme, and in 2003 of its foreign minister, Anna Lindh, and Anders Breivik's murderous rampage in Norway in 2011). Nordic noir is in part an extended meditation on the tension between the old Scandinavia, with its low crime rate and monochrome culture, and the new one, with all its threats and possibilities. Mr Mankell is obsessed by the disruption of small-town life by global forces such as immigration and foreign criminal gangs. Each series of "The Killing" focuses as much on the fears—particularly of immigrant minorities—that the killing exposes as it does on the crime itself.

The second advantage is something that Wahloo and Sjöwall would have found repulsive: a huge industry complete with support systems and the promise of big prizes. Ms Lackberg began her career in an all-female crime-writing class. Mr Mankell wrote unremunerative novels and plays before turning to a life of crime. Thanks in part to Larsson, crime fiction is one of the region's biggest exports: a brand that comes with a guarantee of quality and a distribution system that stretches from Stockholm to Hollywood.

Dinner in Copenhagen can come as a surprise to even the most jaded foodie. The dishes are more likely to be served on slabs of rock or pieces of wood than on plates. The garnish often takes the form of leaves or twigs. Many ingredients, such as sea cabbage or wild flowers, are unfamiliar, and the more familiar sort, such as pike, are often teamed with less familiar ones, such ►►



► as unripe elderberries.

Copenhagen is the restaurant capital of Europe, largely thanks to Noma, which has been rated among the world's best restaurants for the past three years, and to its founders, Claus Meyer and René Redzepi. Mr Redzepi, the head chef, eschews the standard fare of Mediterranean cooking such as olive oil and sun-dried tomatoes in favour of local products such as mushrooms, cloudberry, seaweed and flowers, which he collects from beaches and hedgerows. His signature dishes include vegetables in "soil" (a mixture of flour, melted butter and beer) and "the Hen and the Egg" (which customers are asked to cook for themselves, under supervision). Noma's guests should "experience something that can only happen in this particular part of the world and in this particular city", he says. But they need to be patient: the waiting list for bookings is three months.

The thousands who are turned away from Noma still have plenty to choose from. Mr Meyer's food empire includes a bakery chain, a catering business, a vinegar brewery, an organic orchard, a collection of public allotments and a "Nordic Food Lab" that operates from a boat berthed round the corner from Noma, all dedicated to his mission to rid Denmark of its "uniform, generic, passionless food". Noma has dozens of imitators-cum-competitors, such as Geranium in Copenhagen, Malling & Schmidt in Aarhus and Ti Trin Ned in Fredericia. Local supermarkets sell local wild garlic. The beaches and hedgerows are thick with foodies scavenging for their dinner.

Open-source culture

The Bremen theatre used to be one of the mainstays of the pornography industry: mighty printing presses whirled day and night in order to slake the world's thirst for pictures of copulating Danes. Today it is the home of Volcano, a "multifaceted entertainment company" that employs 22 people. Its boss, Kristian Riis, is trying to bring imaginative flair to the often routine business of running a nightclub-cum-concert hall. He mixes concerts with stand-up comedy and quiz nights and particularly prides

himself on his ability to connect different worlds. He helps the foreign ministry feature Danish musicians in Danish embassies abroad. He arranges deals between companies who want to reach the young and bands that want to make money. These deals usually break down because companies lack nuance (they expect bands to wear their logos or T-shirts) and bands constantly worry about selling out. Volcano feels it can bring these two worlds together because "we're not afraid of talking about money."

Much the biggest regional power in the music industry is Sweden. Its record producers and songwriters are a big force in the American record industry: about a third of the records in the Billboard 100 bestsellers have Swedish fingerprints on them. Sweden has also produced groups that have enjoyed international success in their own right, such as Swedish House Mafia, Robyn and, more recently, The Tallest Man on Earth.

So far Finland has not extended its success in video games to other areas of the culture industry. Finnish detective novels are too depressing. Finnish music is too tortured. But do not mistake lack of global reach for lack of creativity: the country that produced Linux, an open-source computer operating system, is also proud to be able to organise "open-source" cultural happenings that allow anyone to have a go.

The biggest annual national opera festival featured an open-source opera in 2012. Helsinki has an annual restaurant day when everybody is encouraged to serve up what they like. Parks fill with pop-up restaurants. Streets are converted into outdoor eateries. Restaurant day has inspired a succession of other "days" such as spring-cleaning day (when Helsinki becomes a giant flea market) and teaching day (when games players teach people how to design games and cobblers how to cobbler). "These kinds of citizen-led events and innovations make Helsinki a really good city at the moment," says Outi Kuittinen of Demos, a local think-tank. "It used to be a lot duller." ■

Norway

The rich cousin

Oil makes Norway different from the rest of the region, but only up to a point

NORWAY IS THE odd man out in the Nordics. While its neighbours are flirting with free markets, Norway is embracing state capitalism. Its national oil champion, Statoil, is the largest company in the region. The Norwegian state owns large stakes in Telenor, the country's biggest telephone operator, Norsk Hydro, its biggest aluminium producer, Yara, its biggest fertiliser-maker, and DNB NOR, its biggest bank. It holds 37% of the Oslo stockmarket, but it also controls some non-listed giants such as Statkraft, a power-generator, which if listed would be the third-biggest company on the stockmarket.

The simple explanation for Norway's penchant for state capitalism is oil. When it was discovered in the North Sea in late 1969 it transformed the country's economy. Today Norway is the world's eighth-largest oil exporter. Petroleum accounts for 30% of the government's revenues as well as a quarter of the country's value added.

There is also a more nuanced explanation. Norwegians ►►

► have always looked to the state to help manage their abundant natural resources—minerals, fjords, forests, waterfalls—and to look after isolated and thinly spread communities. Norway has a population density of only 13 people per square kilometre. Norway also came up with the idea of the state owning shares in private companies: after the second world war the government nationalised all German business interests in Norway and ended up owning 44% of Norsk Hydro's shares. The formula of controlling business through shares rather than regulation seemed to work well, so the government used it wherever possible. "We invented the Chinese way of doing things before the Chinese," says Torger Reve of the Norwegian Business School.

In recent years the Norwegians have been adjusting their model to get the best combination of state control and global competition. In 2007 they merged two state companies, Statoil and Hydro, in order to create a national champion. They also reduced the state's share to 62.5%. For some this shows that Norway is liberalising. But the strategy is remarkably similar to that being adopted in China and other state-capitalist countries.

Norway's state capitalism has resulted in several oddities. It has made the country the only western European member of the OPEC club of oil producers. It is also the only advocate of human rights among them—and a powerful one, thanks to its control of

nance ministry as owner and the central bank as manager. They are now trying to improve returns and diversify risks.

The oil wealth has not destroyed Norway's egalitarian spirit. Finn Jebsen, chairman of the Kongsberg Group, which has large defence interests, points out that his country has some of the world's best-paid manual workers and some of the worst-paid CEOs: blue-collar workers earn three times as much as their British peers, whereas the boss of Statoil earns just a couple of million dollars a year.

Many of Norway's richer citizens live in London to escape from high taxes and a somewhat claustrophobic society.

Still, Norway is changing fast: new wealth is pulling in newcomers from all over the world and shaking natives out of some of their old habits. In Oslo you now see *nouveaux riches* flashing their wealth, drug addicts and dropouts begging for money, an army of Swedish barmen and waitresses and men with prayer beads driving taxis. Some 11% of Norway's residents were born elsewhere.

Like its neighbours, Norway wants to occupy upmarket niches and sell its expertise to the rest of the world. Its government created Statoil out of nothing by compelling private oil companies to hand over some of their expertise in return for their contracts and by building on the country's established skills in shipping. It badgered the company to innovate by taxing profits



The country's principled response to the actions of Anders Breivik, who committed mass murder in the name of white supremacy, was deeply impressive

the Nobel peace prize. Norway has been able to cling onto more of its old social democratic habits than its neighbours. The oil boom led to a boom in public spending: since the 1970s the number of people employed in education has doubled and that in health and social services has quadrupled. The public sector continues to account for 52% of Norway's GDP.

Oil wealth is bringing its own problems. The oil sector is monopolising the nation's technical talent, with more than 50,000 engineers currently being employed offshore. Property prices are rising by nearly 7% a year. McDonalds charges \$7.69 for a Big Mac, against \$4.37 in America.

Oiling the wheels of welfare

Fellow Nordics like to dismiss Norway as the world's most northerly Arab country, but the most striking thing about Norway is how quintessentially Nordic it is. Oil may have filled its coffers and reconfigured its political economy, but it has not changed its culture. Oslo is singularly free from the soaring skyscrapers and bling-filled shopping malls that sprout in other oil capitals. The new opera house is magnificent, but it tries its best to look modest. The Munch Museum, celebrating the country's most famous painter, is housed in a concrete mausoleum.

The Norwegians are well aware of oil's terrible ability to turn riches into rags and sages into fools. Back in 1990 they established a sovereign-wealth fund (formally known as the Government Pension Fund Global) to prepare the country for a post-oil future and to prevent deindustrialisation. They also used the oil industry to promote other local industries such as shipping.

The fund is not without its problems, such as its size (it now accounts for 1% of all the world's stocks), its leisurely approach (it was slow to exploit the opportunities offered by the 2007-08 financial crisis) and its penchant for blacklisting offending companies. But it is nevertheless one of the best-run in the world. The Norwegians have established a clear division between the fi-

heavily but providing generous tax relief on R&D spending.

Norway is now the world's deep-sea drilling capital. Statoil is a leading global company in its own right as well as being at the centre of an elaborate network that includes Norwegian companies such as Aker Solutions and Kongsberg Maritime and the deep-sea divisions of foreign oil companies such as Schlumberger. Norwegian companies have learned how to drill horizontally as well as vertically. They have also cut the cost of exploratory drilling by developing technologies for mobile rigs that allows them to be kept steady in rough weather. The demand for this expertise is booming.

Norway applies the same strategy to traditional industries such as fishing, logging and mining. Its fjords are home to the world's most advanced fish-farming industry. Its pulp and paper companies are moving into biorefining. Its tradition of exploiting natural resources ("we live off what we find in nature" is a common refrain) is giving rise to new occupations such as bioforaging. Norwegian aquaculturists are selling their expertise to other countries that specialise in fish farming, such as Chile.

Norway has also caught the region's enthusiasm for entrepreneurship. The government is promoting new businesses through bodies such as Innovation Norway and university science parks. Venture-capital firms such as Northzone, too, are on the lookout for clever ideas. The Norwegian Institute for Air Research has come up with a device that can measure the levels of volcanic ash in the air. Clean Marine has invented a way of cleaning ships' exhaust. Norway also has a flourishing culture industry: Karl Ove Knausgård, the author of "My Struggle" (in six volumes), is a huge literary talent.

Norway is also a strong exponent of Nordic social values, supporting negotiated solutions abroad and humanitarian policies at home. Of late it has not been a wise guardian of its biggest source of soft power. Giving Barack Obama the Nobel peace prize before he had a chance to do anything, or to the European Union ►►

► in the midst of a euro crisis, might have been fine individually, but doing both in rapid succession was bad management.

Still, the country's principled response to the atrocities perpetrated by Anders Breivik was deeply impressive. Mr Breivik blew up eight government buildings in Oslo, killing eight people, and then shot dead 69 more, most of them teenagers, on the nearby island of Utøya. He committed mass murder in the name of white supremacy. Yet the country's reaction was a model of restraint. The court gave him an impeccably fair trial and sentenced him to 21 years in prison. He now spends his time writing letters complaining about life in his "mini Abu Ghraib" and working on a book to explain his actions. ■

Lessons

The secret of their success

The Nordic countries are probably the best-governed in the world

CECIL RHODES ONCE remarked that "to be born an Englishman is to win first prize in the lottery of life." Today the same thing could be said of being born Nordic. The Nordic countries have not only largely escaped the economic problems that are convulsing the Mediterranean world; they have also largely escaped the social ills that plague America. On any measure of the health of a society—from economic indicators like productivity and innovation to social ones like inequality and crime—the Nordic countries are gathered near the top (see table).

Why has this remote, thinly populated region, with its freezing winters and expanses of wilderness, proved so successful? There was a time when most of its population would have unhesitatingly praised their government, which for most of the 20th century meant the social democrats in one of their various national guises. The government had provided the people with

cradle-to-grave welfare services, rescuing them from the brutal life of their 19th-century forebears, and stepped in to save the capitalist economies from their periodic crises.

But free-marketers have poked holes in the pro-government explanation and offered a powerful alternative. In the period from 1870 to 1970 the Nordic countries were among the world's fastest-growing countries, thanks to a series of pro-business reforms such as the establishment of banks and the privatisation of forests. But in the 1970s and 1980s the undisciplined growth of government caused the reforms to run into the sands. Free-marketers put the region's impressive recent performance down to its determination to reduce government spending and set entrepreneurs free.

Government's role in improving equality is also being questioned. Andreas Bergh, of Sweden's Research Institute of Industrial Economics, argues that the compression of Swedish incomes took place before the arrival of the welfare state, which was a consequence rather than a cause of the region's prosperity—and almost killed the goose that laid the golden eggs.

This special report has supported some of the free-marketers' arguments. The Nordic countries had got into the habit of spending more on welfare than they could afford and of relying more on a handful of giant companies than was wise. They are right to try to trim their states and make life easier for business. But it would be wrong to ignore the role of government entirely.

The Nordic countries pride themselves on the honesty and transparency of their governments. Nordic governments are subject to rigorous scrutiny: for example, in Sweden everyone has access to all official records. Politicians are vilified if they get off their bicycles and into official limousines.

The Nordics have added two other important qualities to transparency: pragmatism and tough-mindedness. On discovering that the old social democratic consensus was no longer working, they let it go with remarkably little fuss and introduced new ideas from across the political spectrum. They also proved utterly determined in pushing through reforms. It is a grave error to mistake Nordic niceness for softheadedness.

Pragmatism explains why the new consensus has quickly replaced the old one. Few Swedish Social Democratic politicians, for instance, want to dismantle the conservative reforms put in place in recent years. It also explains why Nordic countries can often seem to be amalgams of left- and right-wing policies.

Pragmatism also explains why the Nordics are continuing to upgrade their model. They still have plenty of problems. Their governments remain too big and their private sectors too small. Their taxes are still too high and some of their benefits too generous. The Danish system of flexicurity puts too much emphasis on security and not enough on flexibility. Norway's oil boom is threatening to destroy the work ethic. It is a bad sign that over 6% of the workforce are on sick leave at any one time and around 9% of the working-age population live on disability pensions. But the Nordics are continuing to introduce structural reforms, perhaps a bit too slowly but stolidly and relentlessly. And they are doing all this without sacrificing what makes the Nordic model so valuable: the ability to invest in human capital and protect people from the disruptions that are part of the capitalist system.

Getting to Denmark

Most of the rich world now faces the same problems that the Nordics faced in the early 1990s—out-of-control public spending and overgenerous entitlement programmes. Southern Europe needs a dose of Nordic tough-mindedness if it is to get its finances under control. And America needs a dose of Nordic pragmatism if it is to have any chance of reining in entitlements and reforming the public sector.

Top of the class

2012 index rankings

Overall rank*	Country	Global competitiveness	Ease of doing business	Global innovation	Corruption perceptions	Human development†	Prosperity
1	Sweden	4	13	2	4	10	3
2	Denmark	12	5	7	1	16	2
3	Finland	3	11	4	1	22	7
4	Norway	15	6	14	7	1	1
5	Switzerland	1	28	1	6	11	9
6	New Zealand	23	3	13	1	5	5
7	Singapore	2	1	3	5	26	19
8	United States	7	4	10	19	4	12
9	Netherlands	5	31	6	9	3	8
10	Canada	14	17	12	9	6	6
11	Hong Kong	9	2	8	14	13	18
12	Australia	20	10	23	7	2	4
13	Britain	8	7	5	17	28	13
14	Germany	6	20	15	13	9	14
15	Ireland	27	15	9	25	7	10

Sources: World Economic Forum; World Bank; INSEAD and World Intellectual Property Organisation; Transparency International; UNDP; Legatum

*Based on equal weighting of indices †2011 ranking



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► The Nordics are hardly blushing violets when it comes to advertising the virtues of their model. Nordic think-tanks produce detailed studies in English about how they reformed their states. Nordic politicians fight their corner in international meetings and Nordic consultants sell their public-sector expertise around the world. Dag Detter played a leading role in restructuring the Swedish state's commercial portfolio in the 1990s, representing more than a quarter of the business sector. He has since advised governments in Asia and across Europe.

Yet it is hard to see the Nordic model of government spreading quickly, mainly because the Nordic talent for government is *sui generis*. Nordic government arose from a combination of difficult geography and benign history. All the Nordic countries have small populations, which means that members of the ruling elites have to get on with each other. Their monarchs lived in relatively modest places and their barons had to strike bargains with independent-minded peasants and seafarers.

They embraced liberalism early. Sweden guaranteed freedom of the press in 1766, and from the 1840s onwards it abolished preference for aristocrats in handing out top government jobs and created a meritocratic and corruption-free civil service. They also embraced Protestantism—a religion that reduces the church to a helpmate and emphasises the direct relationship between the individual and his God. One of the Lutheran church's main priorities was teaching peasants to read.

The combination of geography and history has provided Nordic governments with two powerful resources: trust in strangers and belief in individual rights. A Eurobarometer survey of broad social trust (as opposed to trust in immediate family) showed the Nordics in leading positions (see chart below). Economists say that high levels of trust result in lower transaction costs—there is no need to resort to American-style lawsuits or Italian-style quid-pro-quo deals in order to get things done. But its virtues go beyond that. Trust means that high-quality people join the civil service. Citizens pay their taxes and play by the rules. Government decisions are widely accepted.

The World Values Survey, which has been monitoring val-

ues in over 100 countries since 1981, says that the Nordics are the world's biggest believers in individual autonomy. The Nordic combination of big government and individualism may seem odd to some, but according to Lars Tragardh, of Ersta Skondal University College, Stockholm, the Nordics have no trouble reconciling the two: they regard the state's main job as promoting individual autonomy and social mobility. Any piece of Nordic social legislation—particularly the family laws of recent years—can be justified in terms of individual autonomy. Universal free education allows students of all backgrounds to achieve their potential. Separate taxation of spouses puts wives on an equal footing with their husbands. Universal day care for children makes it possible for both parents to work full-time. Mr Tragardh has a useful phrase to describe this mentality: “statist individualism”.

Nordic people take this attitude to government with them when they go abroad. In the 19th and early 20th centuries some 1.3m people, a quarter of the Swedish population at the time, emigrated, mostly to the United States. America created an entire genre of jokes about “dumb Swedes” and their willingness to obey rules. These dumb Swedes created the best-governed enclaves in America, such as Minnesota. Even today Americans with Nordic roots are 10% more likely than the average American to believe that “most people can be trusted”.

Size isn't everything

Economists frequently express puzzlement about the Nordic countries' recent economic success, given that their governments are so big. According to a professional rule of thumb, an increase in tax revenues as a share of GDP of ten percentage points is usually associated with a drop in annual growth of half to one percentage point. But such numbers need to be adjusted to allow for the benefits of honesty and efficiency. The Italian government, for instance, imposes a heavy burden on society because the politicians who run it are mainly concerned with extracting rent rather than providing public services. Goran Persson, a former Swedish prime minister, once compared Sweden's economy with a bumblebee—“with its overly heavy body and little wings, supposedly it should not be able to fly—but it does.” Today it is fighting fit and flying better than it has done for decades. ■

