

Insiders and Outsiders in the Labour Market

Experiences of a Nordic Welfare State in Labour Law Perspective

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1 Introduction

When economists discuss the mechanism governing employment and unemployment and the principles of wage setting, they sometimes start their analysis by dividing the labour force into two main categories: the insiders and the outsiders. The *insiders* are the 'incumbent' employees whose positions are protected by various employment-preserving devices due to their seniority. For several reasons, not only employment protection regulations but also the strength of their unions and the fact that they are experienced collaborators, it is costly for an employer to dismiss them and replace them with someone else. The *outsiders* are those who lack similar protection. They are either unemployed or get work only temporarily or - in some societies - have jobs in the 'informal' sector. Some economists discern also, as a borderline case, *entrants*, *i.e.* employees who have recently entered into employment with a future prospect of gaining the insider status.¹ In practice there is, of course, no sharp distinction between the insiders and the outsiders. The distinction is made, however, for reasons of simplicity and as an aid in the development of further argumentation.

The insiders are much more influential than the outsiders, since they have market power as well as power based on regulations. They participate in wage negotiations, they may take industrial action or exert influence by many other means. Outsiders can do nothing of the kind. In a frequently quoted treatise, *The Insider-Outsider Theory of Employment and Unemployment*,² the economists Assar Lindbeck and Dennis J. Snower have focused their attention on one critical source of power of the incumbent employees, namely the employer's costs connected with the turn-over of his labour force. These include all the costs

¹ See A. Lindbeck & D.J. Snower, *The Insider-Outsider Theory of Employment and Unemployment*, Cambridge, Massachusetts (The MIT Press) 1988, p. 3.

² See note 1 *supra*.

that may arise when employees join or leave a firm. Some costs may be set down by law or other regulations, *e.g.* as regards severance pay or litigation expenses; other costs would be defined by technological conditions, *e.g.* as regards screening and training costs. Yet another kind of costs may be introduced through various union activities, *e.g.* strikes or work-to-rule actions.

After a few central assumptions, Lindbeck and Snower set out their theories on the relation between the power of the insiders in the wage setting procedure, on the one hand, and the level of unemployment, on the other. A key element in their reasoning is that the insiders may, on account of the labour turn-over costs, drive their wages far above the minimum level at which entrants would be prepared to work. The central idea of the authors is, in brief, that the insiders may exercise upward pressure on wages and thereby generate unemployment.

Being a lawyer and not an economist, I will not try to verify or falsify the hypotheses of Lindbeck and Snower.³ The aim of my article is much more modest. By making use of some of the ideas presented in their writings, I wish to shed some light upon the interplay between legal regulations and institutional conditions, on the one side, and social realities, especially the wage structure and the stratification of the labour force, on the other side. I will select illustrations primarily from my own country, Sweden, a North-European welfare state with some 8.5 million inhabitants, and since 1995 a member of the European Union.

From the insider-outsider perspective, a conspicuous feature of the Swedish labour market development during the last 25 years is the country's exemplary record in controlling unemployment in the 1970s and 1980s - when only about 2 % of the labour force could be counted into unemployed outsiders - and the collapse of this record at the beginning of the 1990s when the rate of joblessness increased dramatically to about 14 %. At the end of the 1960s the gross national product per capita was the second highest in Western Europe, but since then Sweden has dropped to about fifteenth position in this country league table. This indicates that a labour law specialist has good reason to ask whether the labour regulation system might have contributed to this course of events.

2 The Institutional Setting

From a comparative perspective, the most spectacular feature of the Swedish industrial relations system is the high percentage of unionized labour. The overall rate is above 80 % of the working population, and this rate seems to be stable, or even increasing. Union membership is high in all three main sectors of the labour market, *i.e.* the private sector, the local government sector and the state government sector. In Europe, only Denmark and Finland have a similar level of organization density. In the manual labour area, the LO (Landsorganisationen - the Confederation of Trade Unions) comprising 21 affiliated unions, is the dominant federation. The LO has long been in close co-operation with the Social Democratic Party. This has been the largest political party since the 1930s and has been in power since 1932, with breaks only between 1976-1982 and 1991-1994. In the salaried employees' area, the TCO is

³ Their hypotheses or propositions seem nowadays to be accepted on the whole in economic science or are, in any case, not much debated.

the largest union federation. There also exists an organization for employees with university education, the SACO. Apart from these three well-established top organizations, there are only a few minor organizations. In Sweden, it is rather unusual for trade unions to compete in organizing the same groups of employees and, as a result, jurisdictional disputes are rare.

The high percentage of unionized labour and the lack of competition between unions are distinctive features of Swedish labour relations. How are these features to be explained? As for the social context, the homogeneity of the working population is a crucial factor, homogeneity as regards language, ethnic origin, religion and political affiliation. But the strength of the trade union movement has been also generated and maintained by various legal regulations. The unemployment insurance system, subsidized by the State, has been administered for sixty years by institutions closely linked with the trade unions, and the system has in fact encouraged trade union membership, even if non-members may also join the system. Moreover, unions that have been strong enough to conclude collective agreements have been accorded a privileged status by various statutory regulations.

These regulations have consolidated the position of the established unions - normally those belonging to the three big federations, the LO, the TCO and the SACO - and counteracted the growth of the minority unions. One example of such regulations is the 1974 Act on Trade Union Representatives. This Act gives the contracting, established union an economic basis for its activities. The local chairman and other representatives of such a union are entitled to full pay when off duty 'for the purposes of trade union activities at the workplace'.

Organizational density is high on both sides of the labour market. Employers in the private sector have long since been organized in a similar way, and on the whole to the same extent as employees. The SAF (the Confederation of Swedish Employers) dominates in this sector. In the state government sector and in the local government sector, three agencies for public employers currently represent the authorities in their capacity as employers in much the same way as the SAF and the federations affiliated to the SAF do in the private sector, that is, by concluding collective agreements on wages and other terms and conditions of work.

Collective bargaining in Sweden has been and still is centralized to an extent which has only a very few counterparts in other market economy countries. For a long time now the pattern on the Swedish labour market has been to conclude collective agreements on minimum wages and other general terms and conditions of work at a central level, covering a whole branch of industry. These industry-wide, central agreements are supplemented in a second bargaining round by plant agreements, which are normally kept, however, within the limits drawn by the central agreement. During the period 1956-1983, bargaining was also done above the level of the national industry negotiations. I am referring here to negotiations between the SAF and the LO which resulted in central framework agreements concerning, in principle, the whole labour force in the private sector.

Influential industrialists and economists of today advocate less centralization in collective bargaining, but it does not seem likely that any profound change will take place here, since attempts to decentralize the bargaining structure are

counteracted by legal regulation of an extensive right to sympathetic industrial action.

When a collective agreement is entered into and in effect, the right to industrial action is suspended under the law, but not unconditionally. The most important exception to this principal rule of a peace obligation during the period of agreement refers to sympathetic industrial action, e.g. a strike or a boycott, to support another organization involved in a lawful labour dispute. This far-reaching right to sympathetic action implies that organizations on each side may turn every local dispute of interest into a nationwide tug-of-war. Naturally, this fact encourages centralization of negotiations and regulation by collective agreement at a high level.

The central labour law statute is the 1976 Act on the Joint Regulation of Working Life (MBL).⁴ This is first and foremost an Act that has to do with the collective agreement and its legal effects, but it also includes important rules for organizations' activities which aim to establish good conditions for regulation through collective agreements. Among these rules designed to promote collective bargaining, those concerning the right to negotiate should be mentioned. These mean, *inter alia*, that if a trade union wishes to communicate with an employer with the aim of reaching collective agreement, then the employer is obliged on request to attend the negotiations and discuss objectively the presented demands. Every union which has at least one member employed by the employer in question has the right to negotiate, but normally only unions affiliated with the LO, the TCO and the SACO make use of this right.

The provisions concerning the right to negotiate do not place on the unwilling party any obligation to reach agreement. If the parties cannot agree during negotiations, which are held because regulation by collective agreement is being demanded, they are usually free to resort to industrial action. It will then depend on the power relationship whether the unwilling party can be induced to accept the proposed agreement. In an international comparison of the trade union's right to take industrial action in this situation, the union's legal right in Sweden appears to be extremely strong.

In Sweden there is no statute in the nature of a general codification of the relationship between an employer and an individual employee. However, the Act of 1982 on Employment Protection (LAS) is particularly important in regard to this. The central rules in the Act mean that a contract of employment will normally apply until further notice and that such a contract may be terminated by an employer only when there is 'good cause'. The Act thus requires that an employee be permanently employed, without first having to complete a qualifying period. A contract of employment for a limited period of time can only be made in certain cases which are listed in the Act; e.g. during temporary work peaks, but then the agreement may be applied for the maximum of six months over a two-year period. The Act also permits an employer and an employee to enter into agreement concerning provisional employment if the trial period is no longer than six months.

⁴ As for literature on Swedish labour law in English, see Adlercreutz, A., *Sweden* in International Encyclopaedia for Labour Law and Industrial Relations, Deventer 1990, and Fahlbeck, R., in Tiberg, H. (ed.), *Swedish Law. A Survey*, Stockholm 1994, p. 240 ff.

If there is a shortage of work in the employer's business, this is considered to constitute sufficient good cause under the LAS for employment contracts to be terminated. The employer may not, however, choose freely which employees shall be dismissed; rather, the employer has to follow a certain order of priority, which is based on the employees' seniority of employment. Another order of priority may be established through a collective agreement at the union level. A person made redundant normally has the right of priority for one year for the purpose of re-employment by the employer. Thus, in this way, the legal employment protection of veritable insider-employees can, therefore, be remarkably strong.

There are also rules in the LAS concerning, *inter alia*, the length of the period of notice and the employer's obligation to provide redundancy payment to employees who temporarily cannot be employed. The LAS applies to both large and small firms. In 1994, the right-wing government then in power introduced certain rules which would have made the rules of the Act less burdensome, particularly for small companies, but these rules were abolished after a change of the political regime in the autumn of 1994.

As in other countries with a market economy, the system of labour law in Sweden is based on the classification of work contracts into two main categories: the contract of employment between an employer and an employee, and the contract for services between a firm and an independent contractor.⁵ This dichotomy, which reflects basic social structures, has in modern labour law gained increased importance in various European countries, with the advent of comprehensive new legislation. Most particularly, employment protection legislation has, to a large extent, given rise to disputes over the delimitation of the two categories. As a consequence of legislation that imposes duties upon employer, new patterns of employment or other labour relationships have emerged, *e.g.* various types of atypical employment forms.

No definition providing effective guidance regarding the content of the employee concept is to be found in Swedish legislation. It has generally been left to the courts to determine whether parties performing work fall within the ambit of the employee concept or not. This concept has, therefore, been formulated largely through case law. According to Swedish legal tradition, for which there does not seem to be any real equivalent in, for instance, British law, the legislator would frequently propose, in the *travaux préparatoires* to Swedish statutes, recommendations as to how the courts should apply the concept, either in relation to a particular work performing group, *e.g.* homeworkers, or in general. During the last few decades, such recommendations have usually been made on the grounds that the concept of who is an employee is not static, but rather, that it is subject to change. The above-mentioned recommendations also inspire a conclusion, especially during the periods when the Social-Democrats have been in power, that the legislature has been sympathetic to the notion that the courts, in marginal cases, should be inclined to find that an employment relationship exists rather than it does not. In other words, the legislature has

⁵ See for the following Sigeman, T., *The Concept of Employee: Some Comparisons between British and Swedish Law*, in Neal, A. C. & Victorin, A. (ed.), *Law and the Weaker Party*, Volume V, London, 1992, p. 49 ff.

taken a benevolent view of the idea that people performing work should be given the status of insiders as often as possible in the sense of being protected by statutes relating to, for instance, security of employment and paid vacation. And the courts have, on the whole, followed suit.⁶

Employment in Swedish industry has fallen over recent years, so that at present less than 30 % of the labour force are employed in that sector. The public sector is large: approximately 35 % of the country's employees are employed by the State or the local authorities.

3 The Balance of Power

When briefly commenting on the balance of power in the Swedish labour market, I will refer to one of the ideas of the late German-British professor Sir Otto Kahn-Freund.⁷ He declared that the main function of the collective labour law of a country is to establish a balance of power, an *equilibrium*, between the competing interests on the labour market, between capital and labour, between rival groups of employees, etc. In this respect, the Swedish system functioned well especially during the three decades dating from the end of the 1930s until the end of the 1960s. In those years, the social partners opposed legislative intervention, which was accepted by the legislature, and assumed responsibility for maintaining industrial peace while not exceeding moderate rises in wage levels and in the standard of living. This was a period of extensive autonomy of the bargaining parties.

The tide turned, however, in the 1970s when Sweden witnessed a massive rush of legislative activity in labour relations, mostly to the advantage of the employee associations' side. At the same time, the balance of power swung in the same direction for other reasons, among other things, the employers' greater vulnerability to industrial action as a consequence of new industrial techniques. The state of equilibrium was further shaken in 1966 when the trade unions in the public sector were given nearly as extensive a right to strike and to bargain over wages as the unions in the private sector. In the bargaining rounds in the 1970s and 1980s, the employees' side made use of the new situation - as will be seen in the next section - by imposing large nominal wage increases.

Recently, during the 1990s, the equilibrium of power has been largely restored, to some extent by legislative interventions but mainly by the influence of market forces.

4 The Inflationary Tendencies of Centralized Wage Bargaining

For an entire century, from 1865 to 1965, Sweden experienced a rate of economic growth that was one of the highest in the western world.⁸ At the end of the 1960s, the gross national product per capita was the second highest in

⁶ See references to cases in the article mentioned in note 5 *supra*.

⁷ See e.g., Kahn-Freund, O., *Labour Relations. Heritage and Adjustment*, Oxford, 1979.

⁸ See Myrman, J., *Hur Sverige blev rikt* (How Sweden became a rich country), Stockholm 1994.

western Europe, with the unemployment rate only 1-2 per cent. The 'Swedish model' was glorified for offering a humane form of capitalism characterized by a tripartite alliance among the State, the trade unions and the employer associations, as well as by the welfare state's massive income redistributions. Poverty had been well-nigh wiped out and the labour market showed stability and order.⁹

This situation changed in the 1970s. As mentioned in section 3 above, the balance of power in the labour market was tipped in favour of the trade unions, for several different reasons. In the bargaining rounds, the employee associations made use of the new disequilibrium by enforcing wage increases which were much larger than the corresponding rate of economic growth of the country. The nominal values of the collectively bargained wage increases were about 6 % per annum on average between 1971-1982 whereas the increase in economic growth was only 2-3 %. During this period, welfare costs increased as well. Particularly excessive were the nominal wage increases in the years 1975-1977, in all about 24 %, at a time when the social insurance contributions paid by the employers under the current legislation were simultaneously raised by about 10 % of the gross wage amount. There may have been many causes contributing to this course of events. As mentioned in section 2 above, the bargaining process took place at three different levels, which raised employees' expectations of receiving substantial wage increases at each of these levels. The LO had changed its leadership in 1973, and it seems that the new leaders were not strong enough to resist the members' extensive demands. And in the public sector, where the trade unions had been given the right to strike a few years before, the employers were weak and indulgent due to their political vulnerability.

The excessive wage increases led, inevitably, to price inflation, with the result that Sweden had a higher inflation rate than most other industrialized countries.¹⁰ In order to maintain the competitiveness of Swedish goods abroad, the government was compelled repeatedly to devalue the Swedish currency. During the period of 1976-1982 the Swedish krona was devalued five times, in all by 45 %.

If we regard all employed workers as the 'insiders' of the labour market, we may notice that during the period between 1971-1982 the insiders were able to exert upward pressure on the nominal wages, which seems to be quite in line with Lindbeck and Snower's suggestions. As regards the movement in real wages, the insiders were not equally successful due to the high inflation rate. They did not generate unemployment that would be harmful to the outsiders, since employment in the public sector increased, and the government pursued an active labour market policy. Thus the unemployment rate was very modest by international comparison.

⁹ With regard to the developments in the wage bargaining system, see Clyde W. Summers, *Comparison of collective bargaining systems*, in *Comparative Labor Law Journal*, Volume 16 no. 4 (1995), pp. 482-484.

¹⁰ See for the following Lindbeck, A. et al., *Turning Sweden Around*, Cambridge, Massachusetts (The MIT Press) 1994; this book is based on a report written for the Swedish government: *Nya villkor för ekonomi och politik*, Statens offentliga utredningar 1993:16, Stockholm 1993.

In the middle and the end of the 1980s, the wage bargaining trends were similar to those prevailing in the preceding period, even if the nominal wage increases were not as excessive as before. Due to the risk of international mistrust of the Swedish currency, the government refrained from taking further depreciatory measures.

At the beginning of the 1990s, Sweden suddenly experienced an extraordinary economic crisis, which was remarkable since this occurred in the absence of any world-wide recession.¹¹ Industrial production and the gross national product fell each year between 1990-1993. Employment in the private sector dropped dramatically, and later on, also in the public sector. The government could no longer control unemployment. At the end of 1993, the ratio of jobless persons rose to over 14 % of the labour force; more than 9 % were unemployed and about 5 % were engaged in various labour board programmes, arranged or subsidized by the labour market administration.¹² The youth unemployment rate reached 21 %. More than 60 % of the gross national product was used for public expenditure, the country's economic position had seriously deteriorated and the budget deficit was large. In November 1992 the fixed exchange rate of the Swedish currency could no longer be defended. Since then the exchange rates of the krona have been floating, at a level about 15-25 % lower than previously. By the end of 1995 the national debt had grown to over US\$200 billion, which corresponded to more than 80 % of the yearly gross national product.

In 1992 the Swedish government asked a group of Swedish social scientists, headed by the economist Assar Lindbeck, for an explanation of the causes of the crisis and recommendations for necessary changes in the national policies. This group saw the crisis primarily as a symptom of long-standing economic deficiencies:

‘The most obvious system failures in the economic sphere are perhaps the high public spending, over-generous social security, wide marginal tax wedges, low private - including household - saving, detailed regulations and cartelization in various markets, lax anti-cartel legislation, and an inflation-prone system of wage formation.’¹³

When diagnosing the causes of the crisis, other evaluators would also tend to attach great importance to the wage bargaining system. Svante Nycander, a political scientist and former editor-in-chief of the leading Swedish newspaper, *Dagens Nyheter*, wrote:

‘The structure of political and trade union power, based upon control of the labour market by way of legislation and superiority in industrial conflicts, has appeared to be inconsistent with economic balance in the community. This

¹¹ See references in note 10 *supra*. See also Freeman, R.B. et al., *Economic Troubles in Sweden's Welfare State*, Stockholm (SNS Förlag) 1995.

¹² About such programmes, see Eklund, R., *Promotion and Regulation of Job Creation Opportunities*, Swedish Report to the XIVth World Congress of Labour Law and Social Security, Seoul 1994.

¹³ Cited from Lindbeck, A., et al., *Turning Sweden Around* (note 10 above), p. 209.

structure of power is the primary cause of inflation and currency devaluations to the subsequent detriment of investments, economic growth and employment.’¹⁴

The social-democratic government, which came into power in the autumn of 1994, presented, and partly carried out, an extensive savings programme with an aim of reducing the budget deficit. The social security system had been curtailed by various parliamentary decisions both before and after the change of government in 1994, including reductions in unemployment allowances from 90 to 75 % of the usual income. In this way, the unemployed outsiders were finally severely hit by a crisis of the 1990s caused, at least to some extent, by the insiders’ and their unions’ bargaining rounds in the preceding years.

After an interval at the beginning of the 1990s, the inflationary or employment endangering tendencies of the bargaining system seemed to reappear once again in the middle of the decade. The wage increases in 1995 were about 4.5 % on average whereas the corresponding figure for other western European countries and that for the economic growth in Sweden was about 3 %.

An important part of the Maastricht Treaty of 1992, establishing the European Union, refers to the creation of economic and monetary union with the objective of price stability.¹⁵ The goal of the monetary union is the introduction of a single currency, tentatively named ‘euro’ (previously ‘ecu’), in all the Member States as from January 1st, 1999. Sweden has declared its intention of joining the monetary union, but it seems uncertain when the country will be able to achieve the high degree of sustainable convergence prescribed by the Treaty.¹⁶ After joining the monetary union, a Member State will be, of course, prevented from neutralizing the inflationary effects of wage increases by currency devaluation.

5 Wage Differentials

From an international perspective, wage differentials are remarkably small in Sweden.¹⁷ Since the 1950s, the LO has been pursuing ‘a solidarity wage policy’ for the purpose of narrowing the range of wage rates.¹⁸ This policy was based on egalitarian ideas but was also seen as a means of promoting the growth of and structural changes in the economy. The LO and its affiliated unions claimed equal pay for equal work, irrespective of the ability-to-pay of the particular firms. They were aware of the fact that this kind of wage policy might put heavy pressure on weaker firms, and subsequently cause unemployment in some

¹⁴ *Juridisk Tidskrift*, volume 7 (1995-96), Stockholm, p. 280.

¹⁵ Art. 102a-109m of the European Community Treaty.

¹⁶ Art. 109j.

¹⁷ See Freeman, R. B. & Katz, L. F., *Rising Wage Inequality: The United States vs. Other Advanced Countries*, in Freeman, R. B. (ed.), *Working under Different Rules*, New York (Russell Sage Foundation), 1994, p. 29 ff., and OECD *Employment Outlook* (July 1993), chapter 5 (Earnings Inequality: Changes in the 1980s).

¹⁸ See for the following Edin, P. -A. & Holmlund, B., *The Swedish Wage Structure: The Rise and Fall of Solidarity Wage Policy?* in Freeman, R. & Katz, L. (ed.), *Differences and Changes in Wage Structures*, Chicago 1995, p. 561 ff. Compare Gifford, D. J. in *Minnesota Law Review* Vol. 72 (1988) p. 1428 f.

industries. They well understood that the solidarity wage policy had to be supplemented by public interventions in the form of an active labour market policy, relocating the workers made redundant in inefficient firms.

The solidarity wage policy was quite successful, especially during the 1960s and 1970s when a sharp wage rate compression took place. Wage differentials may be measured by the ratio between the earnings of an employee in the ninetieth percentile (someone whose earnings exceed those of 90 % of all employees) and the earnings of an employee in the tenth percentile (someone whose earnings exceed only those of 10 % of all employees). From 1968 to 1984 this ratio was reduced from 2.6 to 1.9 in Sweden.

During the 1980s the trend of a decline in wage inequality was broken in Sweden, as in many other countries, but Sweden showed only a modest rise in overall wage inequality. The ratio of the 90th percentile earner to the 10th percentile earner was about 2.1 in 1990. The corresponding figures were 3.2 for the United Kingdom and 4.0 for the United States.

In line with the general wage compression trend in Sweden, the premium received by university graduates has dropped. The ratio between salaries of employees with university education and those with upper secondary school education ('gymnasium') decreased from 1.8 in 1968 to 1.3 in 1991.

In an insider-outsider perspective, the ratio figures in Sweden may be said to imply that most employees have been treated as privileged insiders in the wage setting process. The relative wages of young people were continually increasing up to the mid-1980s. The 'entrants' were thus treated, as soon as they had been employed, as privileged insiders. The wage compression implies, however, a rather high level of minimum wages, the consequence of which is that the employers expect the entrants to show a rather high efficiency level. For the real outsiders, the unemployed and the unqualified, this wage compression can bring about difficulties in finding employment.

There is no minimum wage legislation in Sweden. In its place, collective agreements regularly stipulate the lowest wage rates. In workplaces where the employer is bound by such an agreement, the agreement applies in accordance with the MBL to the members of the contracting union only, and the statute does not provide any explicit solution concerning the application of a collective agreement to non-members (including member-employees of another union). In practice, however, a collective agreement is almost always applied to other employees as well, as a result of the fact that the agreement usually obliges the employer, whether directly or tacitly, not to apply other conditions upon the non-members. The contracting union, but not the non-member, can enforce this obligation. The National Labour Court is strongly inclined to find such an implied obligation in the collective agreements.

6 Unemployment and Non-Regular (or Atypical) Employment

As stated above, the severe economic downturn which afflicted Sweden at the beginning of the 1990s manifested itself in record high unemployment.¹⁹ The

¹⁹ As for statistics, see *Arbetsmarknadsstatistik augusti 1995* (Labour market statistics, August 1995), published by the Swedish Ministry of Labour.

rate of undisclosed employment which was only 2.3 % as late as at the beginning of 1991 rose rapidly to 9.3 % at the end of 1993. During the same period the proportion of persons on the labour board programmes rose from about 2 % to about 5 %. These high unemployment figures seem to be here to stay. In August 1995, the undisclosed unemployment rate was 8 % and the rate of joblessness (which includes people in labour board programmes) was about 12 %. This amounts to more than 500,000 persons being the real outsiders of the Swedish labour market.

Especially worrying is the high rate of youth unemployment. In August 1995, more than 17 % of those 16-24 were unemployed. As mentioned in the previous section, wage compression brings in its wake rises in the minimum wage levels, which in turn makes it difficult for unqualified and inexperienced workers to find gainful employment. The high rate of youth unemployment seems to support this hypothesis.

Near at hand to an observer are comparisons between the labour market situation in the United States and that in Sweden. This calls attention to the interplay between the existing labour market regulations and wage spread, on the one hand, and the rate of unemployment, on the other.²⁰ As stated above, the labour market of the United States displays a much wider wage spread than the Swedish one, but, in return, it also provides work for a much higher rate of unqualified workers. During the last fifteen years, employment has notably increased in the service sector of the United States, especially as regards low income earners. In Sweden there have been no corresponding developments. In 1994, the overall unemployment rate in Sweden was 8 % and in the United States 6 % with the youth unemployment rate 16.6 % and 12.5 % respectively.²¹

Swedish employees in permanent employment normally should be classified as 'insiders' in view of the protection bestowed on this group by the LAS and complementary case law. The number of insiders in this sense has considerably diminished during the economic crisis, falling from 3.7 million at the beginning of 1991 to 3.1 million in August 1995. In return, some groups on the border between insiders and outsider have increased their numbers. Thus, the number of persons engaged in fixed-duration employment increased from about 350,000 at the beginning of 1991 to about 550,000 in August 1995. These figures indicate a restraint or a reluctance on the part of employers, even if they are in need of manpower, to involve themselves in permanent employment relationships of indefinite duration, with the ensuing statutory obligations in periods of economic crises.²² They are, however, keen on making use of the possibilities of fixed-duration employment permitted by the LAS. As stated above, the LAS is based on the principle that a permanent need of labour should be met by permanent employees, which is why a contract of employment for a limited period is only

²⁰ About employment growth and income distribution in the United States, *see e.g.* Krugman, P., *Peddling Prosperity*, rev ed. New York, 1995, compare, e.g. Bean Ch. in *Unemployment: Choices for Europe*, London (Centre for Economic Policy Research), 1995.

²¹ OECD, *Employment Outlook*, 1994.

²² The statistics on overtime work indicate such a reluctance as well. Overtime work is expensive, but it seems that employers prefer making use of such form of work to recruiting new employees. In 1995 the rate of overtime work in industry was about 5 %.

allowed in situations that have been strictly laid down and listed in the Act. In 1994, in order to promote employment, the then right-wing government introduced some rules enlarging the lawful domain of fixed duration employment, but these rules were abolished after the change of the political regime in the autumn of 1994.

The trend towards deregulation and flexibility²³ appearing in the labour law of many countries during the 1980s and 1990s also had a few counterparts in Sweden.²⁴ One evident manifestation of the trend concerns the *hiring-out of manpower*. In Sweden there is a free, public employment exchange. Private labour exchanges (employment agencies), like the hiring-out of manpower, had long been forbidden, but reforms in 1991 and 1993 have changed the legal system in this area. Under the Act of 1993 on Private Employment Exchange and Hiring Out of Employees, both these activities have now been legalized and essentially deregulated.²⁵ Persons operating an employment exchange agency or manpower firm (a 'hiring out firm') are not allowed to charge job applicants or employees for their services. The activities of the manpower firms are expanding and seem to be the answer to the existing market demand. It is estimated that in 1995, 20,000 persons were employed by some 2,000 manpower firms. The trade unions have been showing a sceptical attitude, however, maintaining that many of the new manpower firms frequently fail in their legal duties as employers in accordance with the LAS and other regulations. Some unions, therefore, call for a system of control and authorization of manpower firms in order to prevent precarious forms of temporary work.

The number of self-employed persons has increased during the economic crisis, from about 315,000 in 1991 to about 335,000 in 1995. This increase might arouse suspicions as to whether employers may have reorganized their activities in such a way as to induce their employees to leave employment and perform instead the same or similar work as independent contractors. There is not much indication that the principal purpose of such arrangements has been to circumvent any law or to avoid collective agreements. In this connection there should be mentioned some important provisions of the Act on Joint Regulation of Working Life (MBL), which accord trade unions a special role as monitors of the way in which the rules concerning the employee concept should be applied by the employers under the existing legislation and collective agreements. These provisions (sections 38-40) refer to a situation in which an employer contemplates letting a person perform work on his behalf without thereby employing him. In such a situation, the employer is obliged to notify the trade

²³ Numhauser-Henning, A., *Arbetets flexibilisering* (Flexible Work Patterns), in *Studier i arbetsrätt tillägnade Tore Sigeman* (Studies in Labour Law dedicated to Tore Sigeman), Uppsala 1993, p. 255 ff. with many references.

²⁴ As for working time flexibility, see the European Council Directive 93/103 concerning certain aspects of the organization of working time. The directive will be implemented by Sweden in 1996, see *Statens Offentliga Utredningar* 1995:92, Stockholm 1995 (with a summary in English) and Government Bill 1995/96:162.

²⁵ See Fahlbeck, R., *Employment Exchange and Hiring Out of Employees in Sweden*, in *Tidsskrift for Rettsvitenskap*, Volume 108, Oslo 1995, p. 589 ff., and Eklund, R., *A Look at Contract Labour in the Nordic Countries* in *Juridisk Tidskrift*, volume 7 (1995-96), Stockholm, p. 625 ff.

unions with whom he has entered into collective agreements, and is also obliged to consult the unions. The national trade union then has a right to veto any such decision, if the proposed arrangement would involve disregard of the law or of the applicable collective agreement. Thus, the right of veto may be exercised to prevent sub-contracting or contracting out in a situation when, for example, a prospective entrepreneur has a reputation for disregarding his obligations in relation to employees in earlier contracts. The veto right can also be used in order to prevent a proper employee from being treated as a self-employed person. The trade unions have thus been given under these provisions an opportunity of advance review of any contract of work which the employer intends to make with persons other than employees in the strict sense of the word.

As in many other countries, recent technological developments have led in Sweden to new patterns of work organization. In 1995 it was estimated that about 12 % of the labour force was engaged in various forms of so-called distance-work, especially those involved in computerized work. A good number of those performing distance-work seem to be well-educated and are self-employed.

The rate of part-time employment has not increased significantly in Sweden during the crisis in the 1990s. In August 1995 about 25 % of the labour force had a part-time job (less than 35 working hours per week). From an international perspective the female labour force participation rate is high at some 85 %. As a result, there are normally two income-earners in a family. However, nearly half of all female employees are in part-time employment.

7 Some Concluding Remarks

In the 1970s the Swedish trade unions, inspired by the ideals of egalitarianism, were successful in their endeavour to provide as many workers as possible with the status of privileged insiders in the labour market. Their efforts were facilitated by the wage negotiation system and reinforced by various legislative interventions. A sharp wage compression benefiting primarily the low-income earners also occurred in this period. The ambit of the employee concept had expanded in case law. The new legislation required that an employee should normally obtain permanent employment: contracts for fixed-duration employment could only be made under certain circumstances, strictly enumerated in the Act. Only small numbers of persons were unemployed, and those outsiders were protected by a well-functioning social security network. Inflationary effects of the wage bargaining and social security systems were in some respects neutralized by reiterated depreciations of the Swedish currency.

The economic crisis that struck Sweden at the beginning of the 1990s was most likely caused primarily by macroeconomics factors and the long-standing economic deficiencies which suddenly took their toll. The social sciences show that it is often difficult or even impossible to verify a causal connection between various phenomena and their effects on the labour market. However, some incontrovertible support can be found for the hypothesis suggesting a linkage between the bargaining strength of the insiders and their unions in the 1970s and

the 1980s, on the one hand, and the large increase in the unemployment rate in the 1990s, on the other hand. The excessive augmentation of nominal wages created inflationary tendencies, and the subsequent depreciations aroused international mistrust of the Swedish currency and led to a decrease in investments and slower economic growth. This course of events, together with the rather high level of minimum wages, led in its turn to a sharp increase in the number of unemployed outsiders.

There is hardly any reason to blame the trade unions for the unfortunate course of events, since they were only playing a role assigned to them by the legal and bargaining systems. However, to avoid a repetition of this scenario it seems necessary that these systems must be modified. As for the regulation of employment protection, greater flexibility seems to be advisable. But what appears especially urgent is the reorientation of the wage bargaining system.

As mentioned above, Sir Otto Kahn-Freund asserted that the main function of collective labour law of a country is to establish a balance of power between the competing interests in the society. To my mind, there is a need for an equilibrium not only between capital and labour, but also between, on the one hand, those who want to consume today, and, on the other hand, those who would prefer to invest for the future benefit of the parties in the labour market. But who should represent in the wage bargaining rounds those who will enter the market only ten or twenty years from today? In Finland, a socially advanced, neighbouring country of Sweden with similar economic problems, the government and the labour market parties were recently engaged in tripartite negotiations concerning wages, whose results seem to be useful for the whole economy of the country. The example of Finland might be worth following by other small countries with a similar social structure. In any case, if anyone should ever want to play the role of a defender of the interests of our descendants in any new bargaining rounds, in order to avoid massive outsidership in the future, that someone ought to be the State.

Addendum 1999

Since 1995, when this paper was written, the unemployment in Sweden has markedly decreased. In May 1999, the rate of undisclosed unemployment was 5.5 % and the rate of joblessness (which includes people in labour board programmes) was about 9 %. Unemployment allowances are, since 1997, improved from 75 % to 80 % of the usual income.

As for amendments of labour law regulations in Sweden since 1995, the reader is referred to an article by R. Eklund, *Deregulation of Labour Law – the Swedish Case*, in *Juridisk Tidskrift*, volume 10 (1998-99), Stockholm, p. 531 ff. A new edition of Adlercreutz, A., *Sweden* (mentioned in note 4 above) was published in 1998.