The Finnish Model - Myth and Reality

There is a fundamental misunderstanding regarding Finland's economic achievements over the past decade. Finland's success is not a story of a static Finnish model. It is a story of radical changes.

The past decade has been a golden one for Finland. The country has enjoyed top ranking in almost all walks of life. It has been ranked the most competitive and the least corrupt country. Its system of basic education has been hailed as a model by the OECD. It has been one of the pioneers of mobility in telephony. Last but not least, its ice hockey team has scored some amazing victories.

It is true that not everything in Finland is perfect. Unemployment is still around eight percent. Taxes are high; wages are low. As a result a lot of people have difficulties making ends meet. According to a recent study, more than half a million Finns live within a risk of poverty as defined by the European Union. Yet, Finland has come a long way. Fifteen years ago the country was in a limbo: the banking system had all but collapsed, public debt was running out of control and unemployment rate was soaring over twenty percent.

So what is wrong with outsiders hailing Finland as a model of success? Nothing, if their appreciation is based on reality. Quite a bit, if they rely on a popular myth concerning Finland's success.

The popular myth is that Finland's success is based on a static economic and social model developed in the 1970s. According to the myth, the Finnish model was tested in the early 1990s when Finland entered the most severe depression of any OECD country. Thanks to its economic and social model it came out of the crisis with flying colours.

Nothing could be further from the truth. Finland's economic and social model did not survive the crisis. It was transformed during the crisis. It was the transformation of the Finnish economic and social model that turned Finland into a success story.

The transformation was radical. In fifteen years Finland moved from a closed economy to an open economy. Prior to the 1990s Finland was a typical co-ordinated market economy. The economy was strongly regulated. There was a very low degree of investments both into and out of Finland. Labour markets were controlled by trade unions. All welfare services were produced by the public sector.

The creative destruction of the old Finnish model began in the mid-1980s with a (botched) deregulation of the financial markets. It was hugely accentuated by the demise of trade with the Soviet Union (which had accounted for more than twenty percent of all trade). And it was brought to a climax with a crisis of public finances in the early 1990s.

The crisis began a series of fundamental reforms. Corporate taxes were cut. The tax system was streamlined. Conditions for welfare payouts were reviewed. The banking system was reformed. A very tight fiscal policy was followed. The pension system was changed. As a result, Finland managed as the only country north of Germany to adopt the euro in 2002.

Today Finland is a liberal market economy with a relatively well-functioning labour market. The only part of the old Finnish model that still exists is the municipal sector – and that very sector is today the biggest headache of Finnish decision-makers. The lesson: if you want to copy Finland, copy its reforms. Do not copy the old model that does not exist any longer.

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