



OECD Centre Tokyo

Tokyo, 30 May 2005

Economic Policy Reforms: Going for Growth

Jean-Philippe Cotis

Chief Economist, OECD

Growth is back at the centre-stage of public attention throughout the OECD,. This renewed focus is not accidental. Disappointment with long-term economic performance has been increasingly noticeable in many OECD countries. At the same time, it is widely felt that regaining growth momentum is key to preserving standards of living at a time of rapidly ageing societies.

Achieving stronger growth presents national policy makers with serious challenges. Learning from past mistakes and strengthening even successful policies will be important. But learning by doing, in isolation, may not be enough. Learning from others may be equally or even more important to raising national performance.

In large part, this is why the OECD was created, at a time of widespread confidence in the capacity of less advanced member countries to achieve full economic convergence with the best performers. Learning from others has often been impeded however by the sense that one's own circumstances are too singular to allow for meaningful transposition from abroad. Indeed, many signs are suggesting that economic convergence among industrialised countries has stalled or even backtracked since the 1980s, indicating that adaptation of OECD surveillance may be needed.

Surveillance processes at the OECD already include country-specific and sector-specific surveys that cover all member countries. What they do not yet include, however, is cross-country surveillance of growth, based on systematic benchmarking and with a view to advising member countries on national priorities. In the context of stalling convergence, benchmarking may help expose more clearly the areas where countries are lagging.

Successful benchmarking may also be easier to accomplish at a time when substantial progress has been made in cross-country data availability and econometric analysis. Methodological progress has made it possible to go beyond what may be described as "superficial benchmarking", where one makes international comparisons of GDP per capita, labour productivity or employment rates without knowing what lies behind apparent differences in performance. For example, a relatively low level of GDP per capita may have strikingly different welfare implications depending on whether it reflects the prevalence of public policies inhibiting economic initiative or a genuinely stronger preference for leisure. In the latter case, higher GDP per capita does not translate into higher quality of life, which is nonetheless the ultimate objective of national policies.

Our new publication, *Economic Policy Reforms*, is an attempt at "deep benchmarking" involving carefully constructed structural policy indicators with a proven, econometric link to economic performance. This should help assess the extent to which divergence in performance reflects differences in the effectiveness of public policies, rather than differences in tastes and societal choices.

The main aim of this new publication is therefore to facilitate the transfer of successful national experiences while avoiding the pitfalls of "one-size-fits-all" policy prescriptions that would impinge on legitimate international diversity.

To illustrate the usefulness of "deep benchmarking", it is instructive to consider the extreme variability of employment rates of persons aged 55 or over across OECD member countries. Analysis suggests that this diversity was mainly caused by disincentives embedded in public policies rather than different attitudes towards retirement age. For those countries which currently suffer from low rates of employment of ageing workers, there may thus be hope that better policies can tap an important source of

growth. This example also highlights that growth surveillance may serve to increase not only standards of living, but welfare in a wider sense by promoting fuller participation in economic and social life.

Because this publication addresses complex issues, considerable efforts have been made to ensure it is transparent and self-contained. All the indicators are documented with graphs and their construction made as clear as possible to the reader. A special thematic chapter is devoted to our indicators of product market regulation. The link between some key policy indicators and performance are explored in two thematic chapters dealing with the impact of public policies on the supply of labour from ageing workers and women. This analytical material is intended to provide clear justifications for our assessment of OECD-wide progress achieved in the field of growth-oriented structural reforms. It is also central to understanding the motivation behind the selection of five policy priorities for each member country.

When dealing with national priorities, it is important to also leave room for individual considerations. However well designed, a set of comparable indicators will never fully capture national circumstances. Here the expertise of our country specialists has been used to tailor two policy priorities for each country that may or may not be reflected in the standardised indicators.

For all its many contributors, representing various OECD Directorates, there is a clear recognition that the launch of *Economic Policy Reforms* is only the starting point of a long process leading to further learning along the way. Wider coverage of potential sources of growth, such as financial markets and innovation policies, will be sought in the future, as will methodological and presentational improvements. We also hope that interested readers will help us, through their constructive remarks and critiques, to make this publication increasingly useful, relevant, and, hopefully, interesting.

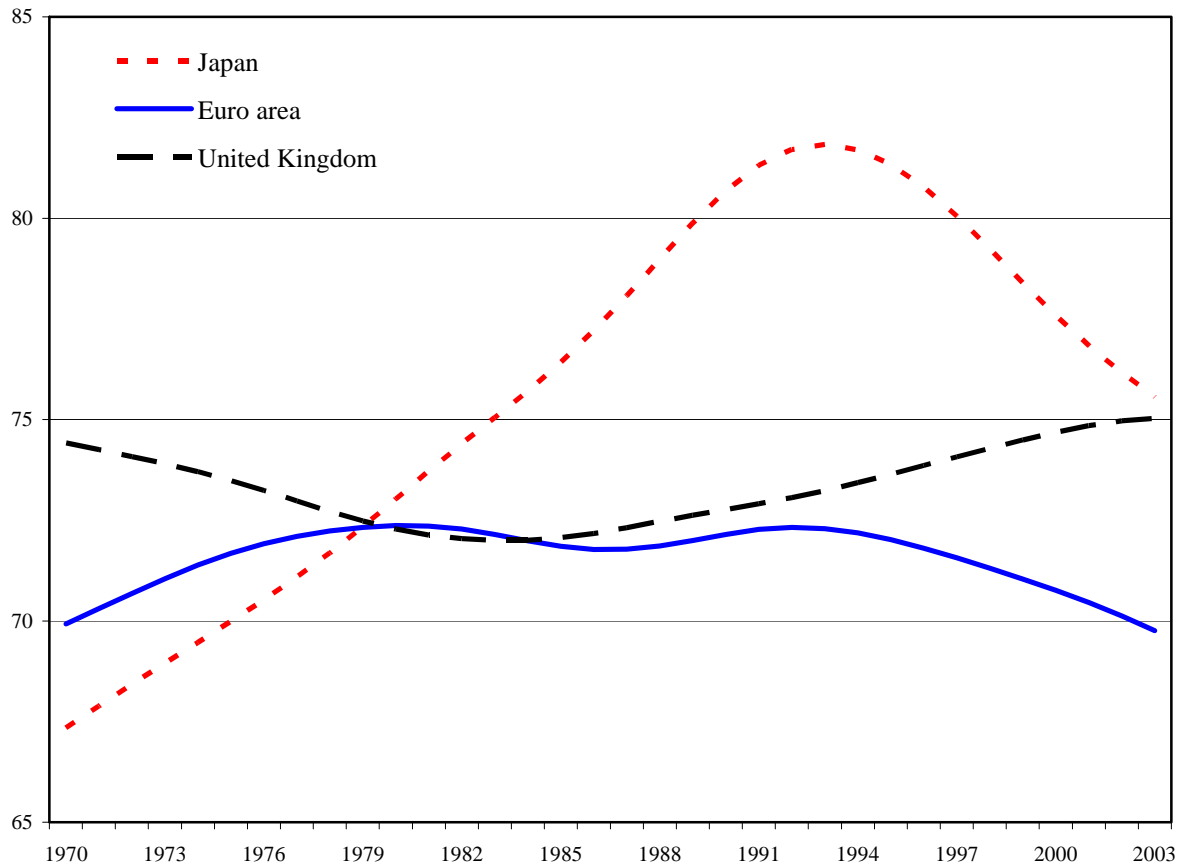
A handwritten signature in black ink, reading "JP Cotis". The signature is written in a cursive style with a horizontal line underneath the name.

Jean-Philippe Cotis
OECD Chief Economist

Graph 1: In Japan per capita GDP relative to the US has receded abruptly

Trend indices, based on 2000 PPPs and 2000 prices ¹

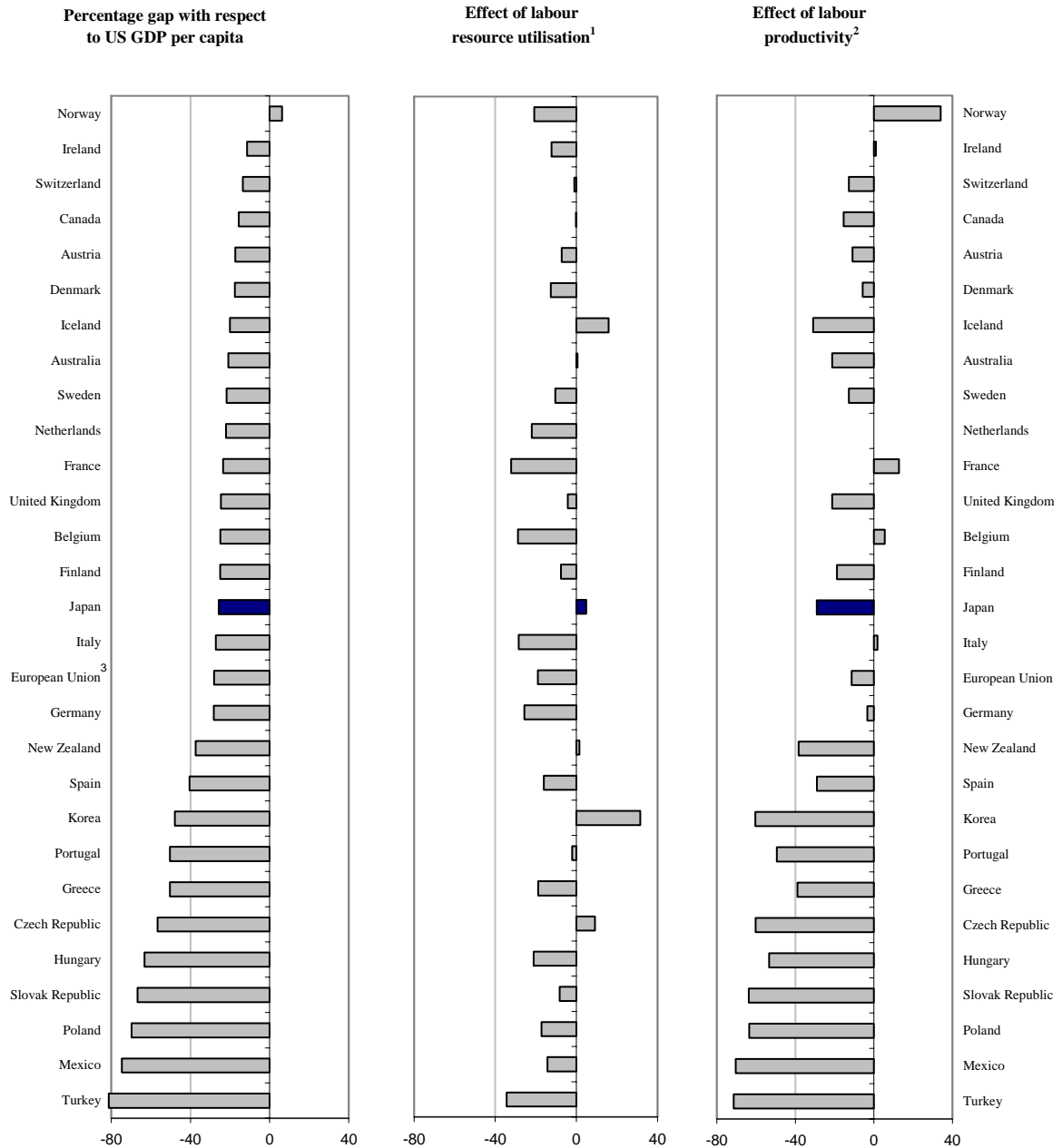
Index US GDP per capita
= 100



1. The trend is calculated using a Hodrick-Prescott filter (smoothing parameter set to 100) over a period which includes projections through 2010.

Source: OECD Annual National Accounts.

Graph 2: What's been driving the gap in per capita incomes?



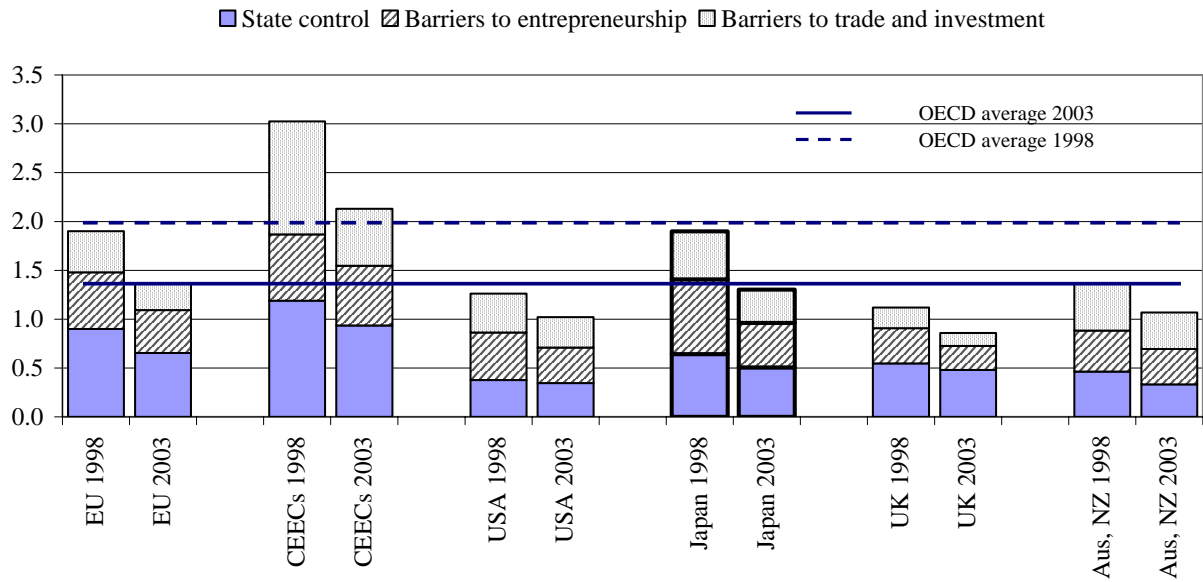
1. Labour resource utilisation is measured as total number of hours worked divided by population.

2. Labour productivity is measured as GDP per hour worked.

3. Excluding Luxembourg.

Source: OECD National Accounts of OECD Countries, 2004; OECD Labour Force Statistics, 2004 and OECD Economic Outlook, No. 76.

Graph 3: Product market regulation restrictiveness is converging towards a more liberal stance in all OECD countries...

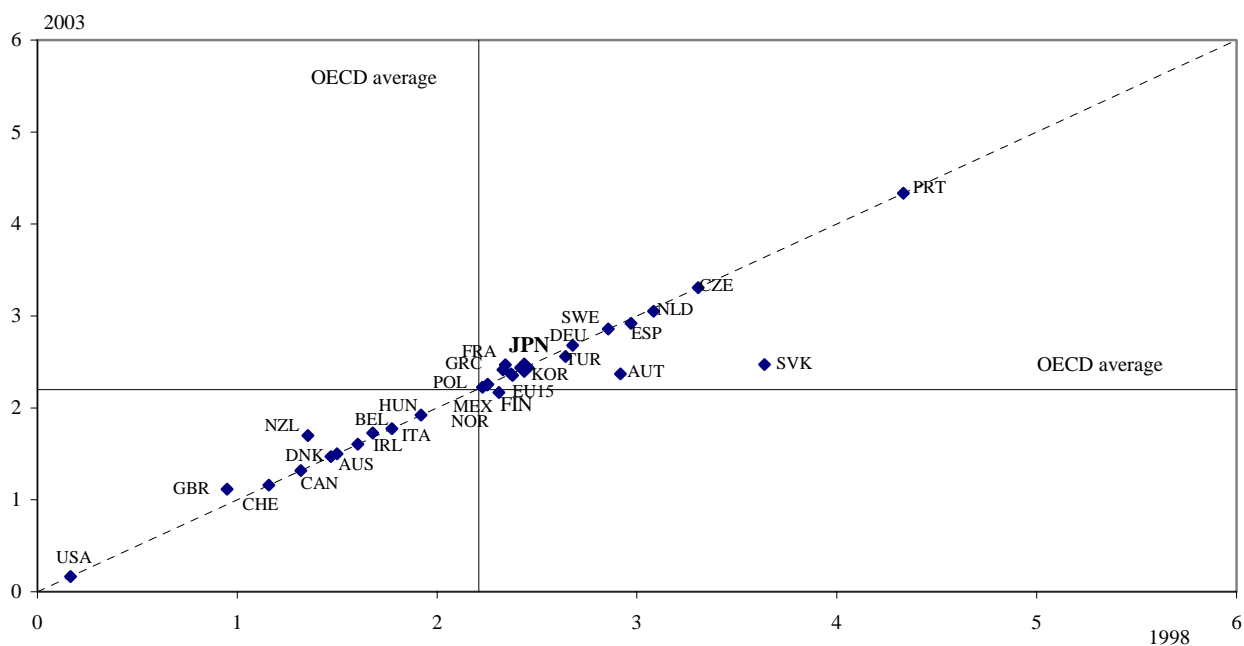


Source: OECD Indicators of Product Market Regulation (www.oecd.org/eco/pmr)

Graph 4: ...but no progress has been made in reforming employment protection legislation

Restrictiveness of protection legislation on regular employment¹

Index scale of 0-6 from least to most restrictive



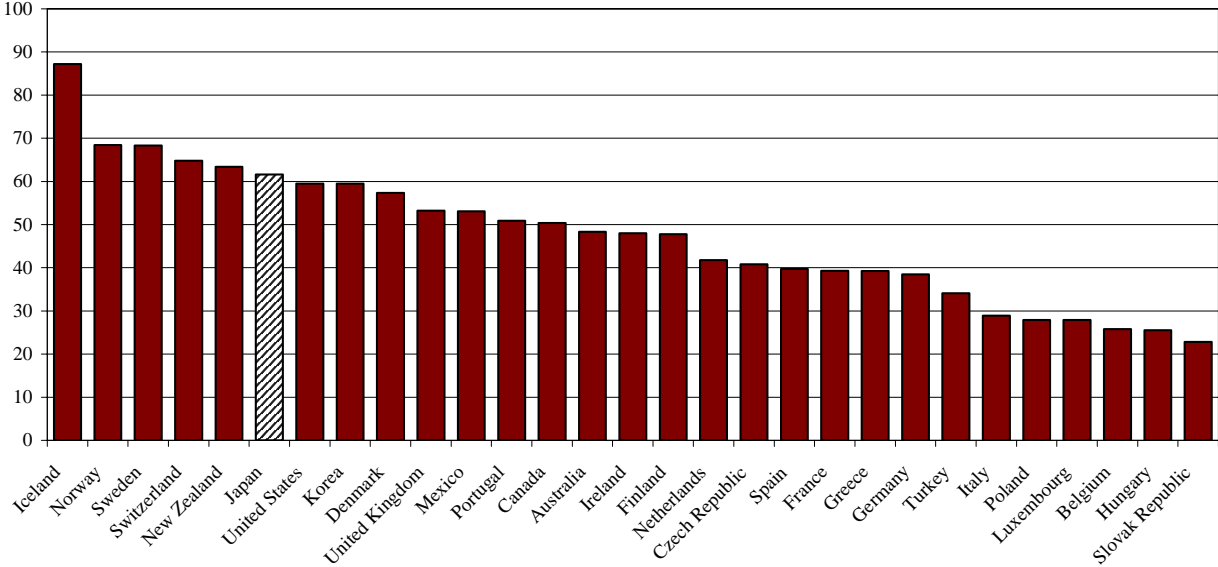
1. EU15, excluding Luxembourg.

Source: OECD Employment Outlook, 2004

Graph 5: There is a wide dispersion in older worker employment rates...

Employment of men and women in the age group 55-64 as a percentage of the population in the same age group, 2002

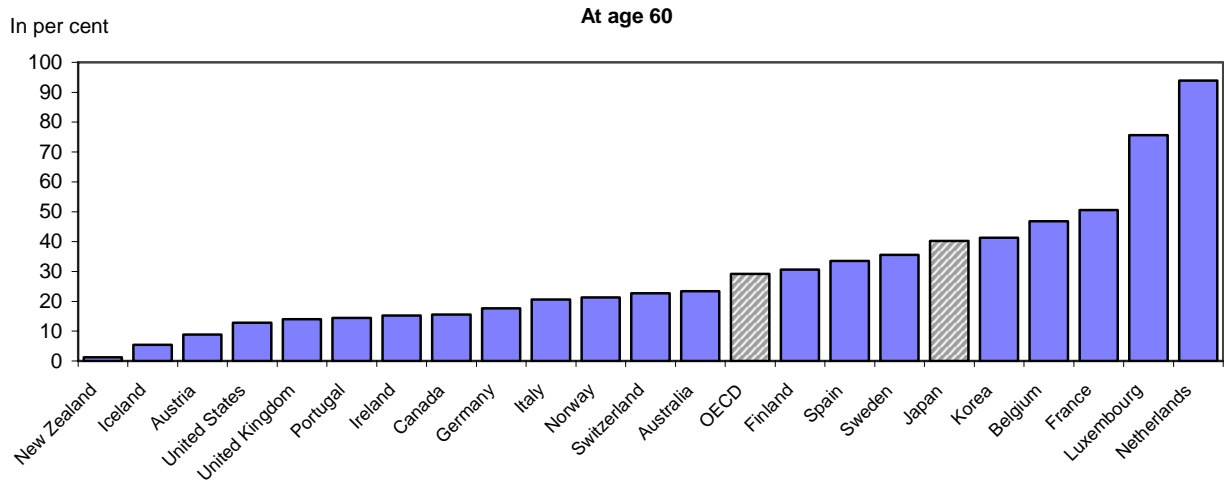
% of population aged 55-64



Source: OECD.

Graph 6: ...which is largely explained by disincentives in old age pension systems...

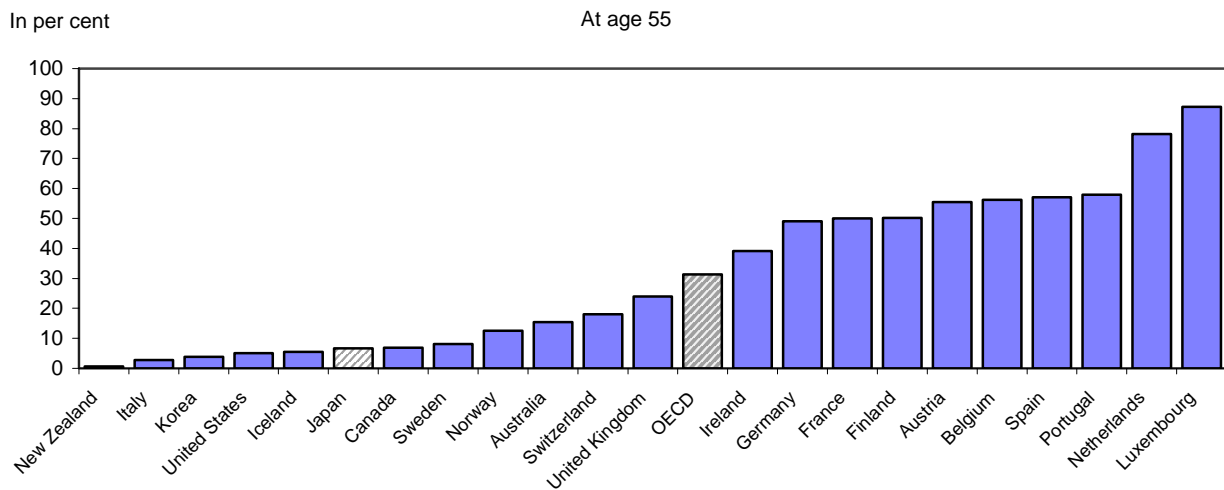
Implicit tax rates on continued work over next 5 years in current old-age pension systems¹



1. Single worker with average earnings.
Source: OECD.

Graph 7: ...and in social transfer programmes

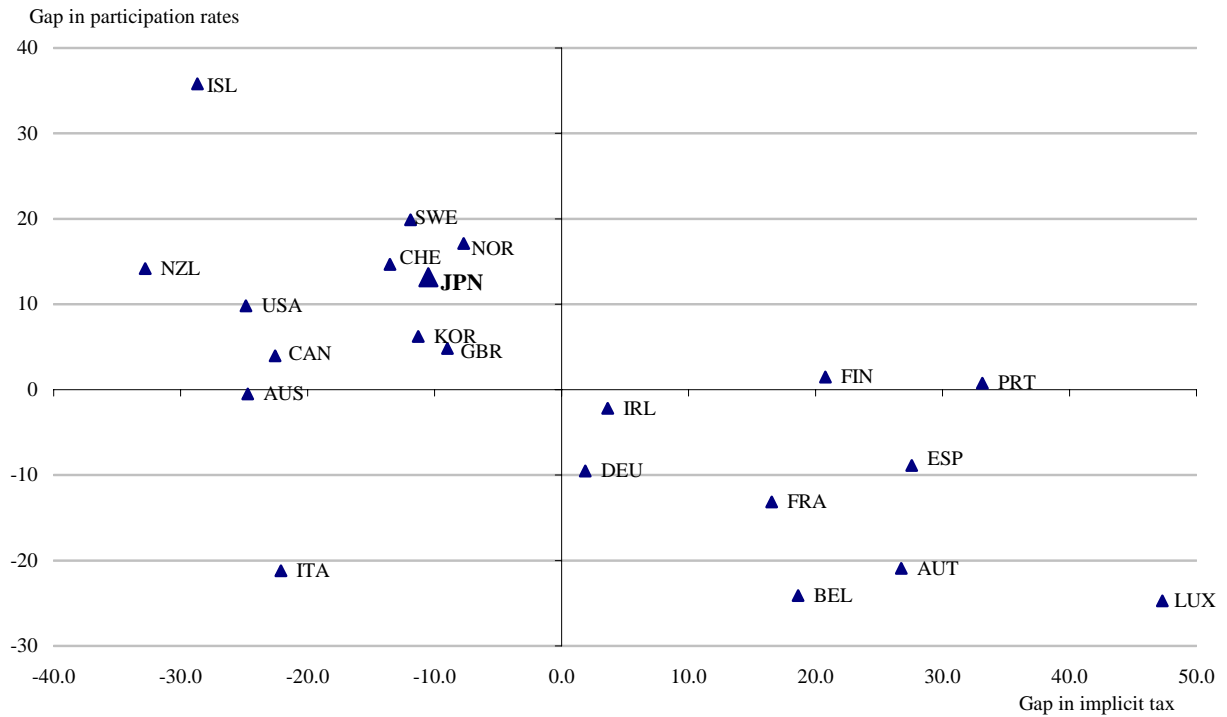
Implicit tax rates on continued work over next 5 years in current social transfer programmes¹



1. Single worker with average earnings.
Source: OECD.

Graph 8: Labour force participation rates of the population aged 55-64 and the implicit tax on continued work¹

Labour force participation rates of population aged 55-64 and the implicit tax on continued work¹
Percentage points gap vis-à-vis OECD average

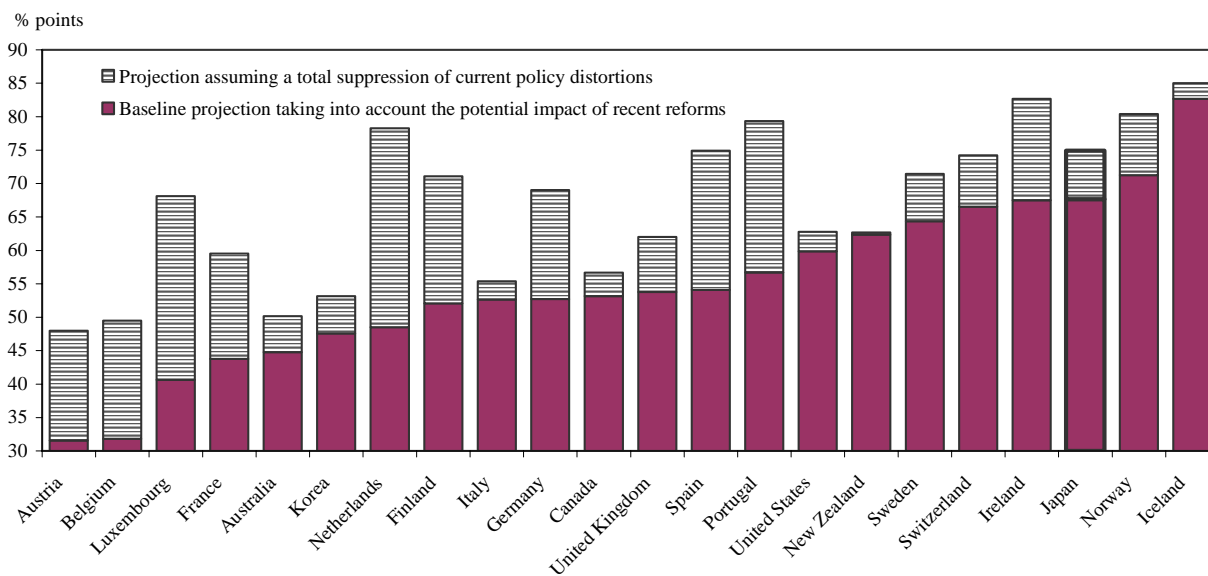


1. Average of implicit tax on continued work in early retirement route, for 55 and 60 years old.

Source: OECD Labour Force Statistics, 2004; OECD Transforming Disability into Ability, 2003 and Chapter 5 in this publication.

Graph 9: Suppressing various policy distortions would have a large positive impact on the labour force participation of older workers

Simulated level of labour force participation of older workers in 2025 under different pension reform scenarios



Source: OECD.

Table 1.1. **Structural policies and performance: proposed priorities**

Performance areas		
Labour utilisation	Labour productivity	
Australia	<p>Refocus disability benefit schemes to encourage work by those with substantial work capacity.</p> <p>Increase the weight of employability in the setting of minimum wages ("award wages").</p> <p>Strengthen employment prospects for lower-skilled workers by improving vocational education.</p> <p><i>Reduce tax wedge on low-income workers to improve work incentives for this group.</i></p>	<p><i>Accelerate reforms aimed at lowering barriers to entry in network industries.</i></p>
Austria	<p>Reduce implicit tax on continued work to cut disincentives to work at older ages.</p> <p><i>Reform child support benefit system to weaken inactivity traps.</i></p>	<p>Raise overall human capital by improving graduation rates from tertiary education.</p> <p>Reduce administrative costs for start-ups and ease entry regulations in professional services.</p> <p><i>Strengthen competition law and enforcement by giving more powers to the competition authority.</i></p>
Belgium	<p>Strengthen work incentives by reducing the tax wedge on labour income.</p> <p>Reduce disincentives to work at older ages by limiting early retirement through unemployment.</p> <p><i>Reduce the incidence of long-term unemployment by strengthening job-search requirements and improving skills of the unemployed.</i></p>	<p>Ease sectoral regulations and subject all new regulations to an efficiency test.</p> <p><i>Improve educational outcomes for students from ethnic backgrounds.</i></p>
Canada	<p>Strengthen incentives to move from welfare to work via stricter job search and activation requirements.</p> <p><i>Restrain growth in public health care costs to limit increases in taxation and labour costs.</i></p>	<p>Switch from foreign ownership barriers to other means to pursue cultural goals, etc.</p> <p>Further liberalise professional services by removing inter-provincial trade restrictions.</p> <p><i>Reduce effective taxation on capital to encourage business investment.</i></p>
Czech Republic	<p>Stimulate hiring by cutting the costs of EPL for regular workers.</p> <p>Reduce tax wedge on low-income workers to strengthen work incentives for this group.</p> <p><i>Further liberalise the rental housing market to increase labour mobility.</i></p>	<p>Implement intended reform of bankruptcy laws and simplify business registration.</p> <p><i>Reform system of taxes and benefits to reduce poverty traps for non-employed households.</i></p>
Denmark	<p>Strengthen work incentives by reducing the tax wedge on labour income.</p> <p>Assist disabled beneficiaries to rejoin the labour force part time, and introduce a waiting period and stronger certification for sickness benefit.</p> <p><i>Reduce implicit tax on continued work embedded in the early retirement scheme.</i></p>	<p>Reduce barriers to entry in industries to strengthen competition in product markets.</p> <p><i>Improve educational achievements to raise the efficiency of the work force.</i></p>
Finland	<p>Strengthen work incentives by reducing the tax wedge on labour income.</p> <p>Reduce implicit tax on continued work at older ages by reforming early retirement pathways.</p> <p><i>Promote greater flexibility in centralised wage agreements to expand employment opportunities.</i></p> <p><i>Reduce the incidence of long-term unemployment by tapering unemployment benefits with duration.</i></p>	<p>Reduce the scale of public ownership, especially raising private provision of publicly-funded services.</p>

Table 1.1. **Structural policies and performance: proposed priorities** (cont.)

Performance areas		
	Labour utilisation	Labour productivity
France	<p>Stimulate hiring by cutting the costs of EPL for regular workers.</p> <p>Stimulate labour demand for youth and low-skilled by allowing for a relative decline in the minimum cost of labour.</p> <p>Reduce implicit tax on continued work at older ages by reforming early retirement pathways.</p>	<p><i>Accelerate reforms aimed at lowering barriers to entry in network industries.</i></p> <p><i>Promote greater competition in retail distribution by reviewing regulation concerning retail outlet locations and pricing rules.</i></p>
Germany	<p>Strengthen work incentives by reducing the tax wedge on labour income.</p> <p><i>Reduce disincentives to work at older ages by removing preferential unemployment benefit eligibility conditions for older workers.</i></p>	<p>Improve secondary education achievements to raise efficiency of the workforce.</p> <p>Liberalise professional services by phasing-out binding fee schedules in specific professions.</p> <p><i>Raise competition in government procurement to increase public spending efficiency.</i></p>
Greece	<p>Reduce age/gender imbalances in unemployment by easing the most stringent provisions of EPL.</p> <p><i>Reduce disincentives to work at older ages by linking pension to lifetime earnings.</i></p>	<p>Accelerate reforms aimed at lowering barriers to entry in network industries.</p> <p>Promote greater domestic competition by reducing administrative costs for start-ups.</p> <p><i>Simplify the tax code to reduce compliance costs for businesses and to boost private investment.</i></p>
Hungary	<p>Reduce the tax wedge for low-income workers to improve their incentives to work in the formal economy.</p> <p><i>Refocus disability benefit schemes to encourage work by those with substantial work capacity.</i></p> <p><i>Downsize the housing loan subsidy programme to reduce housing market distortions and facilitate labour mobility.</i></p>	<p>Reduce state control on the operations of network industries to allow prices to better reflect market signals and to facilitate entry.</p> <p>Promote greater domestic competition by reducing administrative costs for start-ups.</p>
Iceland	<p><i>Reduce government backing of bonds issued by the Housing Finance Fund to reduce housing market distortions and facilitate labour mobility.</i></p>	<p>Lower barriers to entry for domestic and foreign firms especially in the energy and fisheries sectors.</p> <p>Raise overall human capital by improving enrolment and graduation rates from upper-secondary education.</p> <p>Reduce producer support to agriculture, especially the most trade-distorting type.</p> <p><i>Raise public-sector efficiency by accelerating performance measurement and management.</i></p>
Ireland	<p>Strengthen work incentives for lower-skilled second earners via a tax credit or a subsidy for child care.</p> <p><i>Phase-out tax deductibility of mortgage payments to reduce housing market distortions and facilitate labour mobility.</i></p>	<p>Ease regulatory burden on business operations to reduce compliance costs.</p> <p>Promote greater competition in network industries and retail distribution by facilitating entry.</p> <p><i>Strengthen enforcement of competition law by giving the competition authority more power.</i></p>
Italy	<p>Strengthen work incentives by reducing the tax wedge on labour income.</p> <p><i>Promote greater flexibility in wage bargaining by decentralising wage-setting arrangements in the public sector.</i></p>	<p>Reduce the scope of public ownership by allowing for more competition in the provision of public local services.</p> <p>Raise overall human capital by improving access to, and graduation rates from, upper-secondary and tertiary education.</p> <p><i>Improve corporate governance by strengthening directors' independence and minority shareholder rights.</i></p>

Table 1.1. **Structural policies and performance: proposed priorities** (cont.)

		Performance areas	
		Labour utilisation	Labour productivity
Japan	Stimulate hiring by cutting the costs of EPL for regular workers.		<p>Promote greater competition in network industries and professional services by facilitating entry.</p> <p>Reduce producer support to agriculture, especially the most trade-distorting type.</p> <p><i>Improve the soundness and functioning of financial system by resolving the non-performing loan problem.</i></p> <p><i>Reduce barriers to foreign direct investment to enhance technological transfers from abroad.</i></p>
Korea	Stimulate hiring by cutting the costs of EPL for regular workers.		<p>Promote greater competition in network industries and professional services by facilitating entry.</p> <p>Reduce producer support to agriculture, especially the most trade-distorting type.</p> <p><i>Improve the soundness and functioning of the financial system by extending privatisation and strengthening financial supervision.</i></p> <p><i>Reduce barriers to foreign direct investment to enhance technological transfers from abroad.</i></p>
Luxembourg	<p>Reduce implicit tax on continued work at older ages by reforming early retirement pathways.</p> <p>Strengthen incentives to move from welfare to work by raising in-work benefits at low wages relative to unemployment benefits.</p>		<p>Improve primary and secondary education achievements to raise efficiency of the work force.</p> <p><i>Raise public-sector efficiency by expanding the role of e-government and simplifying administrative procedures.</i></p> <p><i>Reduce barriers to competition in telecommunications to reap further benefits from liberalisation.</i></p>
Mexico	<i>Shift burden of taxation towards consumption by broadening the value-added tax base.</i>		<p>Improve secondary education achievements to raise efficiency of the workforce.</p> <p>Promote greater competition in product markets by reducing barriers to entry in industries.</p> <p>Reduce barriers to foreign ownership to enhance technological transfers from abroad.</p> <p><i>Strengthen investors' confidence by improving the enforceability of contracts.</i></p>
Netherlands	<p>Strengthen work incentives by reducing the tax wedge on labour income.</p> <p>Refocus disability benefit schemes to encourage work by those with substantial work capacity.</p> <p><i>Stimulate labour mobility by reforming residential zoning restrictions.</i></p>		<p>Reduce compliance costs for businesses by simplifying administrative procedures.</p> <p><i>Promote greater competition in network industries and retail distribution by facilitating entry.</i></p>
New Zealand	<p>Strengthen incentives to move from welfare to work via activation requirements and back-to-work bonuses.</p> <p><i>Stimulate labour demand by reconsidering recent measures that have raised labour costs.</i></p>		<p>Reduce barriers to foreign ownership and use other means to protect sensitive land.</p> <p>Improve educational achievement, in particular among ethnic minorities.</p> <p><i>Improve the regulatory framework for addressing infrastructure bottlenecks.</i></p>
Norway	<p>Refocus disability and sickness benefit schemes to encourage work by those with substantial work capacity.</p> <p><i>Use direct transfers rather than provisions of labour market and natural resource policies to achieve regional objectives.</i></p> <p><i>Reduce future pension contributions by using the Petroleum Fund to pre-fund part of pension liabilities.</i></p>		<p>Reduce the scope of public ownership by pursuing privatisation of competitive activities in network industries.</p> <p>Reduce producer support to agriculture, especially the most trade-distorting type.</p>

Table 1.1. **Structural policies and performance: proposed priorities** (cont.)

Performance areas		
	Labour utilisation	Labour productivity
Poland	<p>Refocus disability benefit schemes to encourage work by those with substantial work capacity.</p> <p><i>Increase labour mobility by improving transport and housing infrastructure.</i></p> <p><i>Stimulate labour demand for youth and low-skilled by allowing for a relative decline in the minimum cost of labour.</i></p>	<p>Intensify competitive pressures in a number of sectors by strengthening the privatisation programme.</p> <p>Reduce barriers to foreign ownership to enhance technological transfers from abroad.</p>
Portugal	<p>Stimulate hiring of regular workers and facilitate labour mobility by cutting the costs of EPL.</p>	<p>Improve secondary education achievements to raise efficiency of the workforce.</p> <p>Reduce state control in certain network industries to promote effective competition.</p> <p><i>Raise public-sector efficiency by accelerating the reform of public administration.</i></p> <p><i>Simplify the tax system to reduce compliance costs for businesses.</i></p>
Slovak Republic	<p>Reduce the tax wedge for low-income workers to improve their incentives to work in the formal economy.</p> <p><i>Promote a rules-based business environment by strengthening the governance of the judicial and enforcement systems law.</i></p> <p><i>Reduce future pension contributions by raising standard retirement age.</i></p>	<p>Reduce state control in certain network industries to promote effective competition.</p> <p>Raise overall level of human capital by improving secondary education achievements and access to tertiary education.</p>
Spain	<p>Promote greater flexibility in wage determination by limiting the extent of administrative extension of collective agreements.</p> <p>Stimulate hiring of regular workers by cutting the costs of EPL for this group.</p> <p><i>Reduce future pension contributions by making the public pension system actuarially fair.</i></p> <p><i>Phase out tax advantages for home ownership to reduce housing market distortions and facilitate labour mobility.</i></p>	<p>Raise overall level of human capital by improving upper-secondary and tertiary education achievements.</p>
Sweden	<p>Refocus sickness and disability benefit schemes to encourage work by those with substantial work capacity.</p> <p>Strengthen work incentives by reducing the tax wedge on labour income.</p> <p><i>Reduce work disincentives by reconsidering measures that would result in lower working hours.</i></p> <p><i>Improve labour mobility by reducing housing market distortions.</i></p>	<p>Reduce the scope of public ownership by allowing for more competition in the provision of public local services.</p>
Switzerland	<p><i>Refocus invalidity pension schemes to encourage work by those with substantial work capacity and to stem rises in tax burden.</i></p> <p><i>Promote competition in the provision of medical products and services to contain increases in health care costs.</i></p>	<p>Further liberalise professional services by removing inter-cantonal trade restrictions.</p> <p>Promote greater competition in product markets by reducing barriers to entry in network industries.</p> <p>Reduce producer support to agriculture, especially the most trade-distorting type.</p>

Table 1.1. **Structural policies and performance: proposed priorities** (cont.)

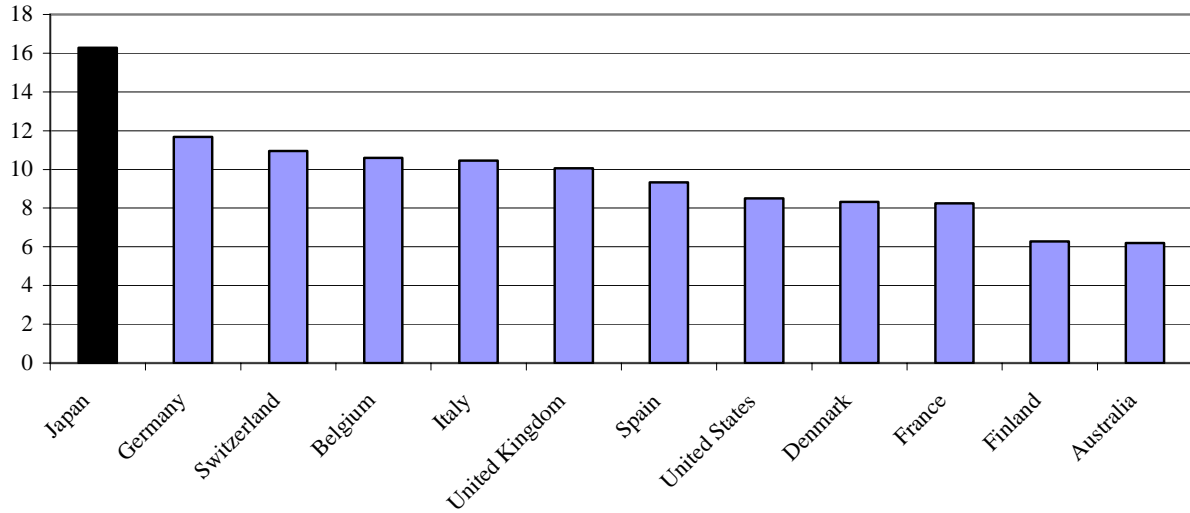
Performance areas		
	Labour utilisation	Labour productivity
Turkey	Strengthen incentives to work in formal activities by reducing the tax wedge on labour income.	Promote greater domestic competition by reducing administrative costs for start-ups. Reduce the scope of public ownership to allow for more competition in network industries. <i>Raise public-sector efficiency by implementing results-oriented budgeting in core public activities.</i> <i>Reduce genders imbalances in education by raising educational enrolments by women.</i>
United Kingdom	Refocus invalidity pension schemes to encourage work by those with substantial work capacity. Strengthen employment prospects for low-skilled workers by improving vocational education at the upper-secondary level.	Improve public infrastructure, especially for transport to further reduce bottlenecks. <i>Raise public-sector efficiency by strengthening incentives to pursue performance targets in publicly-funded services.</i> <i>Enhance competition in some service sectors by reviewing planning restrictions.</i>
United States	Limit increases in labour costs by reforming Medicare to restrain health care costs. <i>Encourage private saving by shifting the burden of taxation towards consumption.</i>	Improve primary and secondary education achievements to raise efficiency of the workforce. Reduce producer support to agriculture, especially the most trade-distorting type. <i>Stand firm on promoting transparency and accountability in corporate governance.</i>
European Union	<i>Improve intra-EU labour mobility by enhancing portability of pension and other benefit entitlements.</i>	Ease internal regulatory obstacles to cross-border trade and entry to strengthen competition. Promote greater competition in product markets by further reducing barriers to market contestability in network industries. Reduce producer support to agriculture, especially the most trade-distorting type. <i>Enhance competition in financial services by ensuring full implementation of Financial Services Action Plan.</i>

Notes

1. Given that the high ranking of Norway partly reflects the contribution from exploiting its oil reserves, the United States is considered as the leading country in terms of GDP per capita.
2. However, GDP per capita overstates the level of living standards in Ireland because of large income transfers to abroad from foreign subsidiaries (see Annex 1.A.1).
3. The indicators displayed in Chapter 2 are generally comparable across countries and over time. However, movements in some of the indicators may also reflect changes in the methodology used for the calculation.
4. The efficiency of the health sector is considered even though the link with growth performance is perhaps not as obvious as in the case of education. The reason is that fast-rising health care costs, as have been observed in many countries in recent years, can have an adverse influence on employment rates by putting upward pressures on indirect labour costs. In countries where health care is provided by the public sector, the associated costs are reflected in social security contribution rates and hence the tax wedge. And, in countries where health care is, to a large extent, provided by the private sector, the cost increases will not show up in the measured tax wedge, but will nonetheless be reflected in labour costs.
5. The policy areas covered by indicators will be expanded in the future as planned special studies on particular policy-performance linkages will enrich the indicator set used for surveillance.

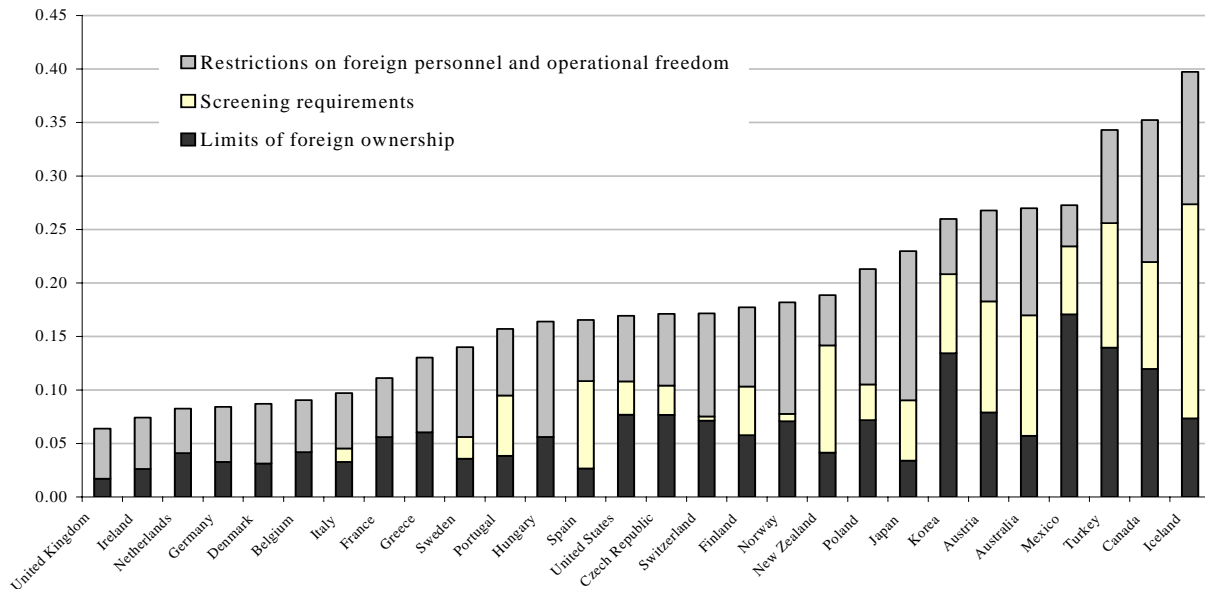
Graph 10: Household electricity prices are high in Japan

Pre-tax price per 100Kwh in US dollars, 2002



Source : OECD Energy prices and taxes, 2004.

Graph 11: Japan has relatively high obstacles to FDI¹

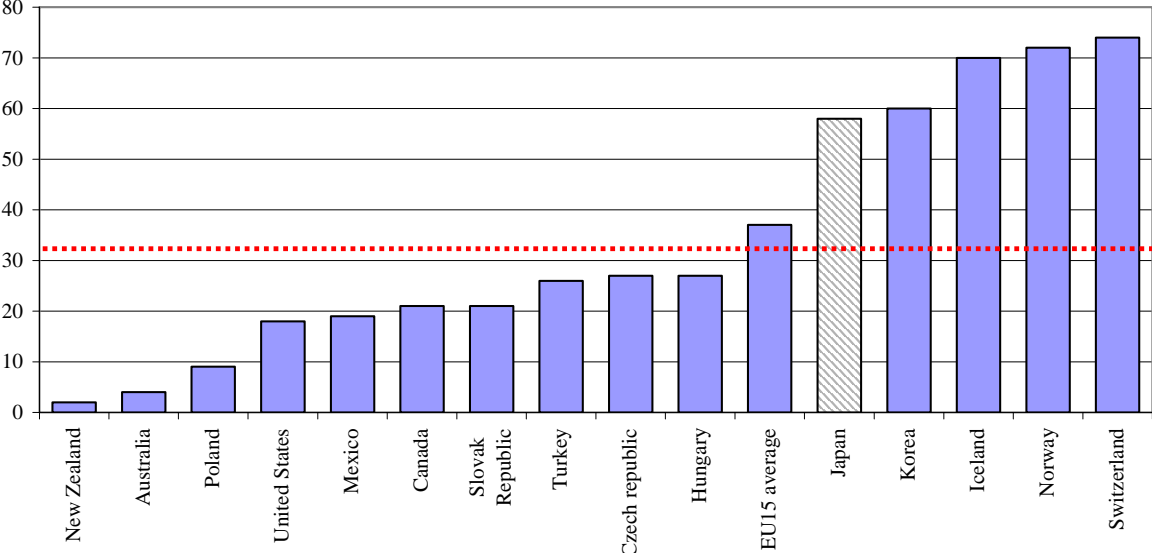


1. The indicator ranges from 0 (least restrictive) to 1 (most restrictive).

Source: OECD

Graph 12: In Japan, subsidies account for more than half of farm incomes¹

Percentage of total value of agricultural production, 2003



Note: The dotted line represents the simple average for the OECD.

1. A single producer support estimate is calculated for EU countries.

Source : OECD Producer and consumer support estimates database.