



Structural reform priorities for the G-20

- The G-20 is falling short of its objective of Strong, Sustainable and Balanced Growth, notably through weak growth and productivity developments and labour market weaknesses. Structural reforms, together with appropriate demand policies and financial regulation, can address these shortcomings.
- Priorities include measures to boost total factor productivity, such as promoting trade and investment openness, removing barriers to competition and encouraging innovation. Disappointing investment can be tackled by measures to improve infrastructure and reforms to encourage long-term investment. A range of labour market reforms and improving skills development would help to tackle high unemployment, low employment and participation of specific groups, and high informality in some economies.
- Structural reforms in priority areas should be designed to contribute to fiscal sustainability – including through the most appropriate choice of fiscal instruments – and environmental sustainability and tackle high and rising inequality.
- Reform priorities should reflect country-specific circumstances, including long-term growth and other challenges as well as the state of the economic cycle. Nevertheless, there are common structural reform priorities for G-20 economies based on country experiences and economic research.

With disappointing global growth and ongoing economic challenges, G-20 structural reform efforts need to intensify, alongside appropriate demand policies and financial regulation, to reach the objective of Strong, Sustainable and Balanced Growth (SSBG).

This paper provides evidence for the identified **structural reform priorities** as requested by G-20 Finance Ministers and Central Bank Governors at Shanghai in February,¹ building on the discussions at the March Framework Working Group meeting in Paris.

G-20 structural reform efforts would be strengthened by priorities for the G-20 commonly agreed by members about what reform actions are required, informed by principles about the type of policy actions needed in the different areas. Together with a quantitative framework to assess progress on structural reform, the two pillars would contribute to an enhanced G-20 structural reform agenda, including in the formulation of revisions to Growth Strategies.

The priorities reflect an assessment of the main performance and policy gaps in terms of structural reforms for G-20 economies. Taking into account specific national circumstances is critical to the successful design and implementation of policies in these priority areas.

¹ Communique, G-20 Finance Ministers and Central Bank Governors Meeting, Shanghai, 26-27 February 2016.

Priorities draw on the existing G-20 reform agenda and Growth Strategies, and align with OECD analysis of policy requirements in *Going for Growth* and *OECD Country Surveys*. OECD analysis reflects qualitative and quantitative analysis of structural reforms in advanced and emerging economies over many decades.

This paper sets out structural reform priorities for the G-20 to strengthen growth and meet other SSBG objectives, taking into account demand conditions and country situations.

Structural reform priorities

The G-20 is falling short of the objective of Strong, Sustainable and Balanced Growth

A strong recovery in the G-20 economies remains elusive as world GDP growth slowed in 2015 to its slowest rate in the past 5 years and with forecasts showing a similar outlook for 2016 as growth in emerging market economies has generally slowed and as the recovery in advanced economies has is only progressing sluggishly.² GDP forecasts have been repeatedly revised down and a substantial negative output gap persists in many economies. Trade growth has been very weak and investment has been subdued. There are many signs of labour market weakness. Insufficient demand and low investment has been widespread and this in turn has depressed the rate of growth of potential output. At the same time, growth remains unbalanced and financial risks are high, public debt in many economies is at high levels, inequality is high or rising in many economies and environmental challenges need to be addressed.

A central feature of these challenges is the slowdown in productivity growth in both advanced and emerging economies. This reflects a combination of weak investment since the crisis and a weakening of growth trends in multi-factor productivity (MFP). The weakness of investment in advanced economies is mainly the outcome of a disappointing recovery in business investment, while low housing investment and cuts back in public investment have also contributed.³ Some emerging economies have struggled to mobilise infrastructure investment, while the quality of investment has proved difficult to maintain in others.

The decline in MFP growth appears to have begun in many advanced economies before the financial crisis and has continued during the recovery phase, while the slowdown in MFP growth in emerging economies has emerged more recently. There are signs that the pace of productivity growth and innovation at the technological frontier over the past decade has remained strong, but that slower diffusion of productivity gains from the most efficient firms through the economy is leading to lower aggregate productivity growth (see Figure 1).⁴

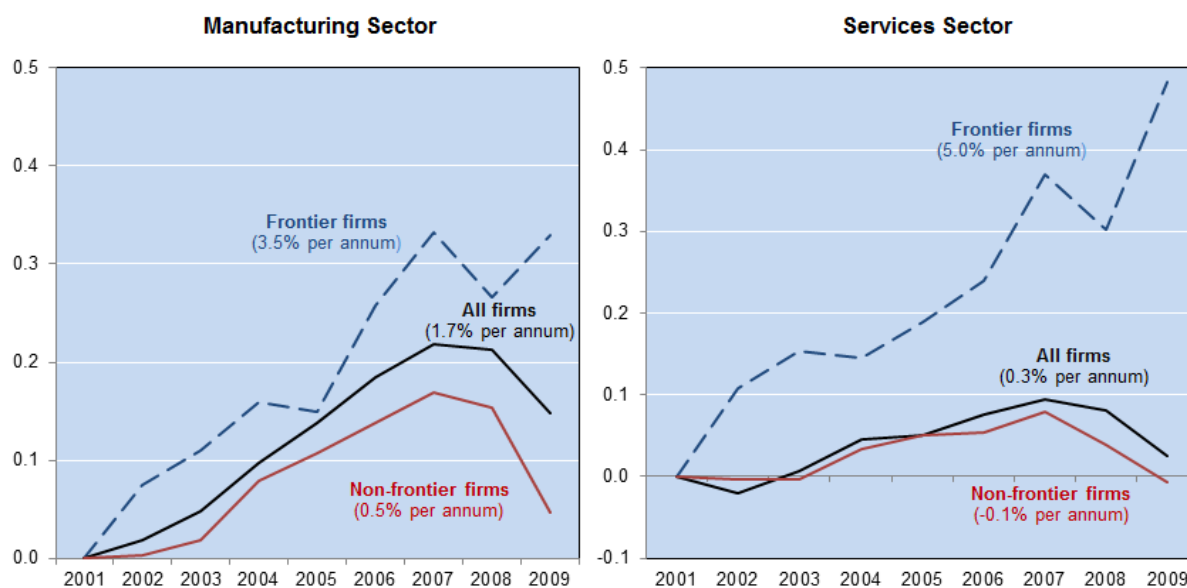
² OECD *Interim Economic Outlook*, February 2016.

³ OECD "Lifting investment for higher sustainable growth" *Chapter 3: OECD Economic Outlook*, June 2015.

⁴ OECD "The Future of Productivity", 2015.

Figure 1. Productivity spillovers have slowed⁵

Growth of labour productivity in “frontier” and other firms. Index: 2001 = 0



There remain more than 120 million people unemployed in G-20 economies, despite some reduction in unemployment rates since the peak. At the same time, significant labour market weaknesses remain in terms of employment growth, participation rates and in specific segments of the labour market, such as employment of women, youth, older workers and the low skilled. Widespread labour market informality remains a problem in a number of G-20 economies.

Low growth has impeded progress towards the G-20's SSBG objective, including the aspects of fiscal sustainability and reducing global imbalances, while income inequality has been increasing in many advanced economies and remains high in emerging economies. Addressing environmental challenges also remains pressing.

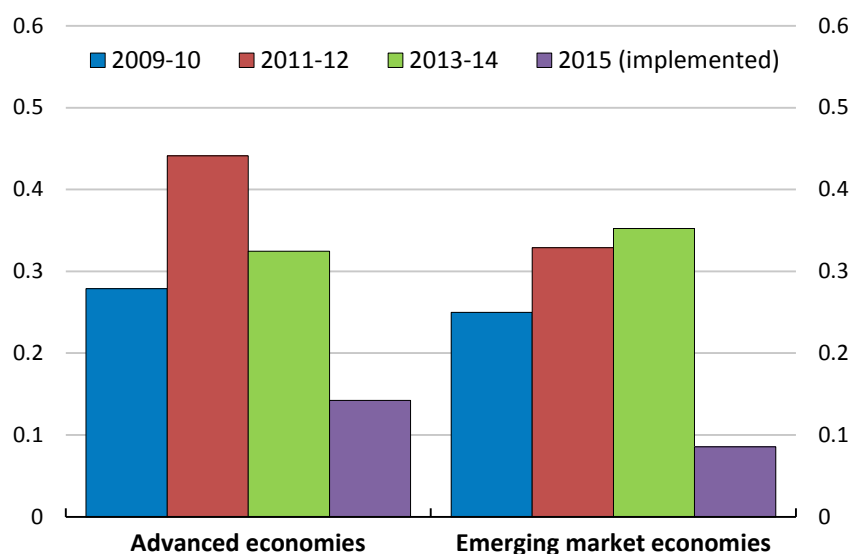
The role of structural reform

With disappointing progress towards the SSBG objective, G-20 structural reform efforts need to intensify, alongside appropriate demand policies and financial regulation. Structural measures essentially provide the only route to better long-term outcomes. There is a clear link between a range of structural policy settings in areas, like trade, competition, taxes and skills, and outcomes.

Progress in structural reforms has been an important driver of growth in the past. A slowing in the pace of reform relative to past norms would therefore contribute to a lowering of growth. The OECD's reform responsiveness indicator provides a measure of reform intensity (see Figure 2). While the pace of reform picked up in the immediate post-crisis period, reform intensity appears to have slowed more recently in both advanced and EME economies. In some countries, there have been significant efforts, but in many very little has been undertaken.

⁵ Andrews, D., C. Criscuolo and P. Gal (2015). "Frontier firms, technology diffusion and public policy: micro evidence from OECD countries", OECD paper.

Figure 2. Share of OECD *Going for Growth* recommendations implemented⁶



Note: Calculated for all countries for which recommendations are available. Emerging market economies include Brazil, Chile, China, Columbia, India, Indonesia, Mexico, Russia, Turkey and South Africa; Mexico and Turkey only for 2009-10. Advanced includes the rest of the OECD.

At the same time, the pace of structural reforms has been inadequate to strengthen the underlying growth trajectory in the face of growing underlying challenges. Considerable space remains to undertake more ambitious structural reforms across a wide range of policy areas.

Delivering on the Brisbane objective to raise collective G-20 GDP by more than 2 percent by 2018 through full and timely implementation of the Growth Strategies would require accelerating progress on reforms. Progress has been made on implementation with around half of policy commitments implemented so far, but those remaining are subject to risks regarding full and timely implementation. The outcome is therefore likely to be closer to a “business as usual” scenario than the required acceleration in reform efforts.

Structural policy priorities

The main policy priorities are to mobilise the core levers to boost total factor productivity, as well as creating more favourable conditions for investment and employment. This would contribute primarily to stronger growth, but also should contribute to fiscal sustainability, improved environmental outcomes and reducing income inequality. **Box 1** summarises the framework used in the OECD’s *Going for Growth* report identify structural reform priorities.

There are a number of trade-offs and complementarities between the objectives and policy levers, although many policies can contribute to multiple objectives. For example, an assessment by the OECD of Growth Strategy Key Commitments shows that many would have a positive effect on reducing income inequality or would have no clear effect on social outcomes, while very few would be expected to add to inequality.⁷

⁶ OECD *Going for Growth* 2016.

⁷ [OECD 2015 Framework Working Group Note: Inequality and Inclusive Growth: Policy tools to achieve balanced growth in G-20 economies.](#)

Box 1 – OECD *Going for Growth* framework to identify structural reform priorities

The OECD's *Going for Growth* report identifies structural reform priorities in OECD and G-20 countries.⁸ First published in 2005, the annual report provides an overview of structural policy developments from a comparative perspective.

Going for Growth uses a framework to assess the influence of policies on GDP per capita through multiple and well-identified channels of labour productivity and labour utilisation. The link between economic outcomes and policies is based on a broad set of indicators of structural policies and performance.

Linking specific policy settings and determinants of GDP per capita is well-grounded from a theoretical and empirical perspective in a vast body of academic literature. This is based on empirical evidence and research of links between policies and outcomes (including by using indicators), recognised policy challenges and problems for countries and informed by international experience. The main relationships have been used empirically in a large set of OECD studies.

The quantitative indicators used in *Going for Growth* measure different outcomes (including income, environment and inequality) and policy settings. A core set of 32 policy indicators (provided as a standalone chapter in each edition) allow for analysing change over time for a particular country as well as a comparison of policy settings across countries. These internationally comparable indicators enable countries to assess their economic performance and structural policies in a broad range of areas. The indicators cover taxation and income support systems and how they affect work incentives, as well as product and labour market regulations, education and training, trade and investment rules and innovation policies.

Three of the five *Going for Growth* reform priorities for each country are chosen based on these indicators and the other two are based on the country-specific circumstances from OECD *Economic Surveys* (see below).

Each *Going for Growth* report also takes stock of recent progress in implementing policy reforms that were identified as priorities in the previous edition.

In addition to *Going for Growth*, the OECD produces *Economic Surveys* every two years for each OECD member country, Brazil, China, India, Indonesia and South Africa (the OECD Key Partners), and for other countries. *Economic Surveys* are peer-reviewed and focus on policies having a potential to improve the economy's long-run performance and the links between structural policies in these areas and macroeconomic performance. In-depth chapters cover a wide range of policy areas including labour markets, competition, innovation, human capital, financial markets, sustainable development, social security, taxation, health care and public spending.

At the same time, specific policies targeted at the wider objectives are likely to be needed, in addition to the effects coming from pro-growth policies. These policies should be designed to achieve their objectives in a growth-friendly way. Changes to the composition of fiscal policy in

⁸ Of G-20 members, only Argentina, the European Union (EU) and Saudi Arabia are currently not covered by the OECD *Going for Growth* exercise. Almost all EU members are included individually and the OECD publishes Economic Surveys of the EU every two years.

terms of the use of different tax and spending instruments can play an important role in supporting growth and improving fiscal sustainability.

The identified 9 structural reform priorities for the G-20 include 6 priorities that would contribute mostly to stronger growth, 2 that focus on more balanced growth, and policies to foster more inclusive growth which also contribute to the SSBG objective (Table 1).

The pro-growth priorities build on the four themes of the Brisbane Growth Strategies: trade, competition, investment and jobs. Encouraging innovation and improving and strengthening financial systems are useful complements to policies in the four areas identified to Brisbane. While reforms under the different areas often have effects on several of the intermediate drivers of growth, these priority areas would likely act in large part through productivity, notably MFP, thereby tackling one of the key challenges in the current conjuncture.⁹ The G-20 has made commitments in many of these priority policy areas, including through the 2025 target for female participation, the youth employment target and G-20 Investment Strategies.

Table 1. G-20 Structural Reform Priority Areas

SSBG objective	Intermediate drivers	G-20 Structural Reform Priorities
Stronger growth	Productivity (multi-factor)	Promoting Trade and Investment Openness
		Encouraging Innovation
		Promoting Competition and an Enabling Environment
	Investment (capital deepening)	Improving Infrastructure
		Improving and Strengthening the Financial System
	Employment	Advancing Labour Market Reform, Educational Attainment and Skills
More sustainable growth	Fiscal sustainability	Promoting Fiscal Reform
	Environmental sustainability	Enhancing Environmental Sustainability
More balanced growth	Inclusiveness	Promoting Inclusive Growth

Note: **Bold** indicates G-20 priorities from Brisbane Growth Strategies.

Boosting productivity growth can be achieved by more policy action in the areas of promoting trade and investment openness, encouraging innovation and promoting competition and improving the overall enabling environment for businesses. Reducing barriers to trade and FDI increases exposure

⁹ The [IMF-OECD note to G-20 on macroeconomic and reform priorities](#) simulations, as well as subsequent quantification of G-20 members' Growth Strategies both suggest MFP as being the most important channel for the impact of reforms in the G-20, although there are also investment and employment gains.

to international competition and strengthens incentives for firms to make productivity improvements. Many of the required policy measures are “behind the border” and therefore have a stronger overlap with measures to reduce barriers to entry in domestic markets. While markets for manufactured goods are generally more open, opening services markets would be one of the main levers to boost productivity in many economies, not least as these services are often relatively tightly regulated. Removing restrictive product market regulations and ensuring effective competition policies are needed to create stronger incentives for the development of new and more efficient activities. Stronger trade and FDI linkages allow countries to reap the benefits from integrating better into global value chains, accelerating technology diffusion and increase productivity via upgrading.

Innovation is a key driver of productivity, growth and wellbeing, and plays an important role in helping address core public policy challenges like health, the environment and food security. Innovation-led productivity growth will become even more important in the future to address key challenges like ageing populations and climate change. Investment in innovation and knowledge-based capital (KBC) is needed not just to move the technology frontier outward but also to facilitate the absorption of technologies and new ideas developed elsewhere and bring them to the market. At the same time, innovation policies are more effective when firms have the incentives to strive for the development of new and better-quality products at lower costs. Competition and open markets are particularly important to provide such incentives.

Strengthening investment, notably in infrastructure, is a priority across the G-20. This requires more and better public investment, as well as financial and regulatory reforms to remove obstacles to investment and especially long-term investment by the private sector in infrastructure. In advanced economies, infrastructure needs often relate to upgrading existing infrastructure, including in making infrastructure smarter by integration of digital technologies, or meeting new environmental needs. In emerging economies, more basic infrastructure is often lacking and holds back private-sector activity and productivity growth. Infrastructure projects promote economic efficiency and add to productive capacity. Deep, liquid and well-regulated financial markets and financial innovation within a prudent regulatory framework are critical to finance investment and new ideas, as well as to channel resources to the best projects.

High and persistent unemployment, low female labour market participation and a large informal labour force undermine making the most out of labour resources, but also can impair labour productivity and contribute to rising or high levels of inequality and social exclusion. Levers to tackle these challenges include labour market policies that protect workers rather than jobs, reduce labour market duality, make wages more responsive to local conditions, and removing barriers to female labour market participation. At the same time, improving equal access to education, investing in skills and creating more opportunities to high quality education and training would support inclusive growth.

Sustainable public finances are a key element to ensure that growth can be sustained over the long-run. Fiscal policy also plays a crucial role in achieving delivering public goods and services and providing social protection using tax instruments that are as growth-friendly as possible. In many countries, there is room for improving the efficiency of the public administration, which would allow doing more with the same amount of resources. Broadening the tax base and eliminating inefficient

tax expenditures, as well as shifting taxation from direct taxation on labour and capital towards consumption, property and inheritance taxation would support growth and contribute to a fairer distribution of the tax burden.¹⁰

Growth-enhancing reforms can in principle both reduce inequality, for example by removing barriers to employment or formal jobs for the low-skilled, but also increase inequality, for example by encouraging technological change that increases the wages of higher-skilled workers relative to those with fewer skills. An OECD assessment of the Brisbane Growth Strategies found that around a quarter of measures would reduce also inequality, with a smaller number increasing wage and income inequality, and most measures having no clear effect. However, given the scale of the challenge of inequalities, the policy response should not rely solely on side-effects of growth-enhancing reforms. Specific policies are needed to address the underlying causes of inequality, such as providing skills and policies to foster employment and quality jobs.¹¹

Economic growth usually comes with higher pressures on the environment. However, at some point, environmental degradation feeds back negatively on future growth and well-being (e.g. because of poorer health, water shortages, land degradation, or extreme weather events). Governments can aid the investment and development of new clean and efficient technologies and infrastructure that will facilitate the necessary transition to a low-carbon economy while sustaining growth. Furthermore, aligning policy frameworks for investment, taxation, energy, labour, agriculture, and others with the goal of transitioning towards a low-carbon economy is essential. The combination of domestic policy action and international cooperation in this area is needed to improve long-term environmental outcomes. Policies in this area should be flexible and neutral with respect to technological choices and minimising regulatory and other barriers to competition. Many countries could undertake growth-enhancing reforms which would encourage investment in cleaner energy, such as shifting the tax burden to environmental taxes, introducing road pricing or removing harmful subsidies encouraging the consumption of fossil fuels.

Common structural reform priorities across the G-20

Within these broad priorities for G-20 economies, country-specific policy priorities depend on the specific challenges economies face, their current policy settings and range of country-specific institutional factors. For example, while some countries face persistently high unemployment, unemployment in other G-20 countries is low both in cyclical and structural terms. There are important interactions between different policies and institutions, for example between incentives for market entry and the availability of credit.

Structural reform priorities therefore vary by country and depend on economy-specific circumstances, existing policies and societal preferences – there is no “one size fits all” approach or specific policy recipe. There are also important trade-offs in the design of reform packages with the state of demand), and other objectives such as fiscal sustainability, environmental outcomes and inequality.

¹⁰ [OECD-IMF Note to the G-20, “Fiscal Policy and Growth: Why, What and How?”, September 2015.](#)

¹¹ [OECD 2015 Framework Working Group Note: Inequality and Inclusive Growth: Policy tools to achieve balanced growth in G-20 economies.](#)

Structural reforms introduced at different points of the economic cycle can also have varying impact. Consideration of priorities should also take account of the macroeconomic context and financial conditions (see **Box 2**). Given current weak global demand, structural reforms which can boost short-term activity, as well long-term growth prospects, should be prioritised.

There are also some areas where collective action is needed, for example in pursuing multilateral trade agreements or around climate change.

Box 2 – Structural reform priorities in difficult macroeconomic conditions

Structural reforms introduced in “normal” times have a different impact to those that are implemented in “bad” times. “Bad” times are a difficult macroeconomic environment such as persistently weak demand and the presence of a large negative output gap. The availability or effectiveness of macroeconomic policies in supporting structural reforms also matters.

Against the current background of subdued global economic prospects, there is a good case for prioritising structural reforms that, in addition to stimulating productivity and employment, can best boost activity in the short term to yield positive short-term gains in employment and domestic demand. Reform strategies that do so include:

- Putting more weight on shifting the composition of public spending towards investment. More specifically, increasing investment in public infrastructure that effectively increases the growth potential in the medium term (e.g. high-speed broadband network) can stimulate private investment in the short term.
- Reducing barriers to entry through product market reforms in services sectors with pent-up demand to facilitate the entry of new firms. Reforming rules restricting the entry of new suppliers (e.g. exclusive rights) and the capacity of existing suppliers to compete (e.g. fees control) in services industries characterised by relatively low entry costs (e.g. professional services and taxis).
- Changing housing policies and job-search assistance programmes to facilitate geographic and job mobility. This includes easing frictions in the reallocation of resources which can increase the speed of employment gains in difficult times. Housing market policies that promote residential mobility include the lowering of transaction taxes or costs on buying properties as well as the reduction of the stringency of rental regulation.
- Adjusting benefit entitlements in health or pension systems to contain future ageing-related costs. This can create the space for short-term stimulus measures and raise their effectiveness, notably through increased confidence in the sustainability of public finances. The gains from such reforms can exceed the cost in the short term to the extent that only future benefits are reduced.

In contrast, the risks that reforms fail to lift activity in the short run – or that they even further depress demand – are highest in the case of reforms that initially put downward pressures on wages or mark-ups, such as reforms of employment protection legislation, minimum wages or product market regulation in network industries. Actions to help mitigate these risks and potential contractionary effects include:

- Packaging simultaneous reforms of labour and product markets. The price reduction resulting from product market reforms eases the downward pressure on the real wage from

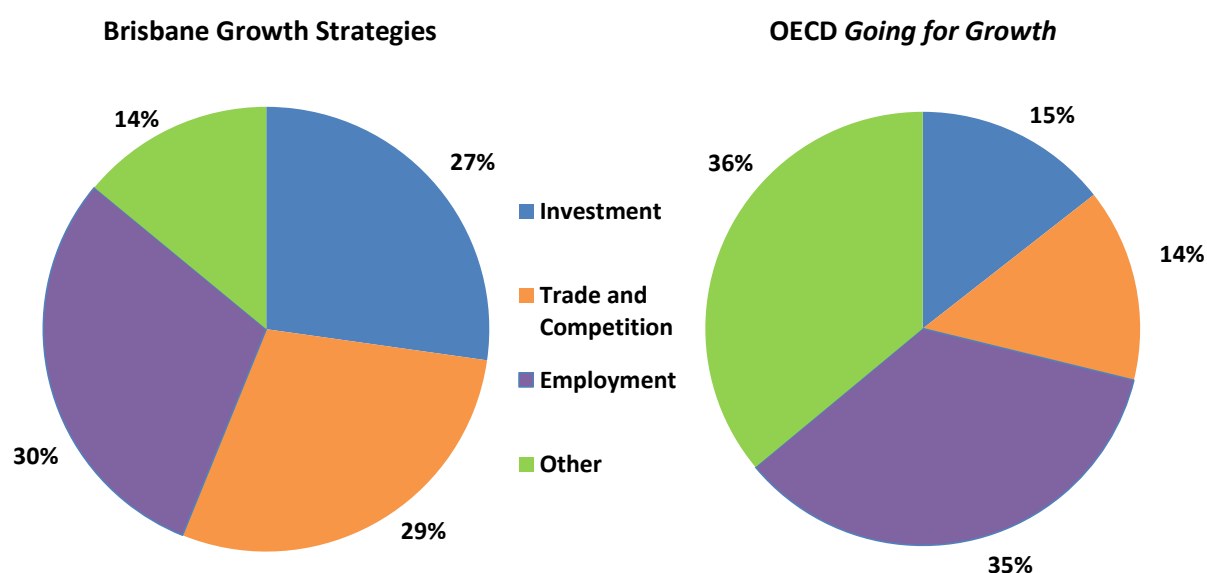
labour market reforms. At the same time, labour market reforms facilitate the necessary reallocation of workers arising from product market reforms as rents are redistributed across firms and sectors.

- Addressing financial sector dysfunctions to improve the flow of credit to households and firms with limited access to financial markets. For example, in the euro area the share of non-performing loans in the banking system remains relatively high in a number of countries. Greater synchronisation of reforms would also help reduce the transition costs by giving greater scope to monetary policy to mitigate the potential rise in real interest rates resulting from persistently low inflation.
- Reducing policy uncertainty through reform strategies that are well communicated and comprehensive. This can create synergies and also provide clearer guidance and boost confidence about the direction and sustainability of policy decisions.

Source: Chapter 2, *OECD Going for Growth 2016*

There are some common patterns across G-20 economies in terms of their reform priorities. The G-20 Growth Strategy commitments reflect countries' own assessment of their priorities, in the context of the four priorities identified at Brisbane and show more employment and investment policies than for trade and competition (see Figure 3). A similar exercise based on the *OECD Going for Growth* priorities for G-20 countries shows some similarity in the prioritisation of reforms in these broad areas. However, there are a number of other reform priority areas such as tax system reform, public spending efficiency, financial market regulation and environmental policies.

Figure 3. G-20 reform priority areas



Note: Share by number of measures and priority recommendations respectively. Trade and competition shown together due to the close links between these policy areas.

Source: OECD calculations based on 2014 G-20 Growth Strategies; and *OECD Going for Growth 2015*.

Structural reforms in these priority areas can be based on economic literature and evidence, as well as country experience. In many policy areas, a balance is needed between different policy

considerations. For example, many regulations provide a necessary response to possible market failures, ensuring that safety standards and consumer information are adequate. At the same time, regulations can be excessive in terms of the burden they impose or their restrictive effect on competition. Equally, while some G-20 economies face challenges in preserving work incentives in their social protection systems, others need to develop wider social coverage. Finally, different countries find themselves at different points of these policy trade-offs, which are partly guided by societal preferences. However, all G20 countries can make meaningful progress in all of the priority areas which would help to achieve the objective of SSBG.

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