

GENERAL DISTRIBUTION

OCDE/GD(93)103

PROGRESS AND PRIORITIES IN STRUCTURAL REFORM

ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

Paris 1993

>

This statement was adopted by the OECD Economic Policy Committee at its meeting on 18 May 1993. The OECD Council agreed on 27 May 1993 to make it available to the public after presentation to the Council meeting at Ministerial level on 2 June 1993.

STATEMENT BY THE ECONOMIC POLICY COMMITTEE TO MINISTERS

PROGRESS AND PRIORITIES IN STRUCTURAL REFORM

1. Overview. Over the past decade or longer, all OECD countries have engaged in wide-ranging programmes of structural reform aimed at making national economies more open, more resilient, more competitive and hence more productive. In a number of areas -- notably that of financial markets -- regulatory reform has extended to cross-border transactions and has been achieved not only through national governments acting individually, but also through both formal and informal international co-operation.
2. The current downturn in OECD activity has not deterred continued reform efforts; in almost every Member country and within the European Community, the process of liberalisation and structural reform has been taken further during the past three years. In general, progress has been greatest in countries that previously had been least active in designing and implementing reform. Hence, there has been some measure of convergence of structural policies across the OECD area since 1990.
3. Despite the progress achieved, the importance of intensifying the reform effort is highlighted by a number of developments, in particular: cyclical increases in unemployment superimposed on the upward trends over past decades; the deteriorating climate for international trade; the relatively sluggish growth of productivity; the persistent pressures on governments' fiscal positions; and turbulence in financial markets. Although problems in these areas have been aggravated by the prolonged cyclical downturn, their durability points to deep-seated causes for which structural remedies are required.
4. Against this background, this note first reviews progress and priorities in structural reform in four key areas -- labour markets, product markets, the public sector and financial markets -- and concludes with a summary of the tasks facing multilateral structural surveillance.
5. Labour markets. Reforms designed to improve the functioning of labour markets so as to reduce unemployment and create more jobs have been undertaken by most OECD governments. These have been implemented under several main headings: improving wage flexibility and the collective bargaining process; relaxing employment protection legislation so as to reduce the reluctance of employers to hire workers with few skills and little work experience; attempting to alter the effects of welfare arrangements (or in some cases the combined effects of taxation and transfer systems) on the incentives to seek employment or to remain in work; and moving from passive income support towards active labour-market policies, while reviewing and attempting to improve the effectiveness of such policies.
6. Despite the measures taken to date, the reform of labour markets still has a long way to go. A sustained recovery in output is a necessary condition for enabling the present high rates of unemployment to be reduced; but in many if not most Member countries, especially in Europe, it is not a sufficient condition for bringing these rates down lastingly to levels which could be viewed as acceptable. In almost all countries, further action is required under some -- or all -- of the above headings. These and other avenues for effective policy action are being explored in the context of the OECD's Employment/Unemployment Study. Remedies will have to reflect each country's particular situation, but in all cases are most likely to achieve their objectives if implemented as a coherent and comprehensive set of policy changes.
7. Beyond creating the environment for an increase in employment, governments are concerned to assure a more productive use of human resources more broadly. This requires strengthening the institutions and incentives that facilitate the upgrading and adaptation of skills. In particular, policy changes are needed in many countries to address current weaknesses in national education and training systems operated by both the public and private sectors. Two related concerns here are the inadequacy of vocational training and preparation and the low levels of knowledge and qualifications typically attained by less skilled workers. Hence the growing attention that education and training are receiving -- and must continue to receive -- as areas of structural reform, including in terms of the need to secure value for money in the education system.

8. Product markets. Open and efficient markets for goods and services, fully exposed to domestic and international competition, provide the crucial underpinning for high-employment, high-income economies, enjoying the benefits of technological innovation. But progress towards domestic and international liberalisation has been uneven and in important respects disappointing.

9. Domestically, the removal of industrial subsidies, barriers to entry and tax distortions in the markets for goods and services would add greatly to economic efficiency and welfare. Large parts of the service industries, and most notably those operated or regulated by the public sector, remain sheltered from competitive pressures. Services account for a growing share of output and employment, and improving their efficiency is therefore becoming increasingly important to a good overall performance. Opening these markets as fully as possible to domestic and international competition is a matter of priority.

10. Internationally, significant liberalising steps have been taken in the context of regional trading arrangements. A key feature of these regional arrangements is that they have not only focused on the elimination of trade barriers but have also been accompanied by a wide range of other market-oriented policies to encourage greater competition and foreign investment, at least on an intra-regional basis. To a certain extent, other countries can also benefit from these liberalisation measures so long as efforts at regional integration do not erect barriers to third parties, preclude new entrants or slow the pace of structural reform, and the market grows as a result of integration.

11. But these moves cannot ease concerns about continuing deterioration in the multilateral trading system. The disturbing delay in bringing the GATT Uruguay Round to a successful conclusion has undermined confidence in open and non-discriminatory market access. This has been accompanied by increased recourse to trade protection, almost always applied outside the multilateral framework of trade rules and in a manner which imposes large economic costs. The problems remain most acute in agriculture. Some measures have been taken to reform agricultural markets; but trade distortions there remain pervasive and the changes which have been made, difficult though they were to achieve, can hardly be viewed as more than a first step. In manufacturing too, the attempt to solve the immediate difficulties of individual firms at the expense of consumers and of trading partners has become disturbingly widespread; and there is concern that managed trade will become an accepted feature of international economic relations.

12. International trade is a powerful engine of growth, raising productivity and creating wealth and jobs. In contrast, protectionist measures, once adopted, have consistently proven difficult to reverse, and inevitably slow the process of adjustment, reducing economies' competitiveness and eroding their capacity durably to increase living standards. Achieving the full benefits of international trade will require adjustment by individuals and communities; in some instances, ensuring smooth and effective adjustment may be facilitated by providing help to those experiencing adjustment difficulties.

13. Public sector. Many countries have attached priority to public-sector reform in recent years, implementing a range of measures such as liberalisation of traditionally regulated industries; privatisation; increasing contestability and introducing greater competition where possible; contracting out services; reforming pricing and user-cost policies; and improving the composition of public investment through better criteria for project selection or widening the range of permitted choices. With a view to preventing the introduction of further distortions to the incentives to work and save, it is important that the reduction of public-sector deficits and debt -- essential in most countries -- be achieved primarily through constraining the long-term growth of outlays rather than increasing taxation.

14. Further progress in public-sector reform is crucial if economies are to function better. Reforms must be intensified along the lines set out above. Greater attention must be given to identifying and implementing shifts in the composition of public expenditure and taxation, and associated reforms to public-sector management, that would improve the efficiency and effectiveness of the public sector. However, the pursuit of this objective cannot rely on simple rules, such as the prescription to shift public expenditure from consumption and transfers to public investment. Each of the main activities of the public sector should be reviewed systematically with a view to identifying efficiency gains both within and across them. Carrying out the necessary reviews and implementing desirable changes in composition will require time and resources, but the rewards of improving the efficiency of resource use within the public sector and its allocation through public-sector intermediation are likely to be great, given the sector's large size in OECD countries. High

priority on the future policy agenda in many countries will be given to the ongoing and complex problems of health-service reforms -- including the need to contain rising costs -- and the financing of social security schemes, including public pensions.

15. Financial markets. Considerable progress in structural reform has already been achieved in financial markets, in ways that have enhanced both the attractiveness of saving and the flexibility of investment. Savers have benefited from a greater variety of choices of, and higher returns on, financial investment. Abolition of credit ceilings and development of bond and other markets have enabled borrowers to have greater access to finance at market-related rates without rationing. The widespread elimination of exchange controls has allowed greater freedom for international transactions. The increasing availability of new financial instruments has provided greater scope for managing risks involved in financial market operations. More generally, liberalised and globalised financial markets can impose -- and have at times imposed -- helpful discipline on governments' conduct of macroeconomic policies.

16. While the benefits of deregulated financial markets are clear, there has been concern about episodes when these markets displayed abnormal behaviour in the 1980s and early 1990s: apparently excessive asset-price movements and instances of instability and turbulence. These characteristics, which stem from the periodic inability of financial markets to form expectations accurately and to correct them promptly when they are wrong, reflect the uncertain environment in which these markets operate and are not directly caused by liberalisation. Rather, they point to the importance of stable non-inflationary macroeconomic policies, particularly commitment of monetary policy to price stability over time. These must be supported by adequate supervisory arrangements.

17. In many countries there is room for further financial market reform, whose broad thrust should be to enhance competition and the scope for portfolio diversification. To achieve this, impediments to operating and investing across regional or national borders and restrictions on the types of activities in which financial institutions may engage should be reduced. At the same time, the overall prudential framework should be improved by specific measures including the application of minimum capital-adequacy requirements, harmonised internationally as appropriate, to a wider range of risks involved in the operations of financial institutions and prompt corrective action to deal with troubled institutions while avoiding moral hazard.

18. Multilateral Structural Surveillance. Determined policy actions along the lines of structural reform identified above -- and in areas not covered in this statement -- would provide a firmer foundation for sustained growth in living standards. Multilateral structural surveillance can assist this process by: allowing the sharing of experience; identifying general principles for dealing with common problems; ensuring that market reforms and the evolution of the institutional framework keep pace with each other; maintaining the pressure of peer review; increasing the transparency of government interventions, including through the development of appropriate indicators; co-ordinating action where the gains from doing so are greatest; and providing the public with informed and authoritative assessments of what needs to be done and the potential gains from reform. Governments can help themselves and each other by working together to advance a renewed agenda for reform. Insofar as reform efforts can be concerted or co-ordinated, they are likely to be easier to implement -- and are very likely to be more effective.

19. An effective programme of structural reform enhances economies' long-term growth potential and employment opportunities. Realising the full benefits of such a programme requires sound management of macroeconomic policies, such that private agents have a stable and predictable economic environment in which to take saving and investment decisions. But it is also true that effective structural policies contribute to making sound macroeconomic policies easier to implement. Likewise, synergy between macroeconomic performance and structural policy change is also important: structural reform is easier to achieve when growth is robust, and sustained growth will be supported by economic structures capable of adjusting to changing economic conditions. Such adjustment may well have short-term costs -- which are particularly difficult to bear in economic downswings -- but attempting to avoid pain by delaying adjustment will serve only to increase the ultimate costs over the longer term.

20. The Economic Policy Committee, and the Economic and Development Review Committee, will continue to attach high priority to supporting the assessment of actual and desired structural reform; to making surveillance more effective; and to contributing to coherent policy-making in this area, {inter }

{alia} because structural reform is most effective when undertaken across a range of policies.

END-OF-TEXT