

**OECD/IMF conference on structural reform in Europe**  
Remarks by Jørgen Elmeskov, OECD Acting Chief Economist

This morning we have two sessions. They deal respectively with the agenda for structural reform in Europe and the lessons one can draw from the past experience in trying to reform. I will deal with both in turn.

Usually when thinking about the agenda of structural reform, we think of increasing economic efficiency. That certainly is the approach that we, the OECD, take in our structural policy surveillance in *Going for Growth* – which was alluded to by the Secretary-General.

I think there is a fair bit of consensus that the policy prescriptions we provide in *Going for Growth* would indeed boost economic efficiency. As explained by the Secretary-General, these policy prescriptions mostly focus on removing barriers to employment and on boosting productivity through human capital investment, product market reform and innovation policies. In the first panel this morning the focus is on labour and product markets. In these remarks, I want to cast the net a little wider than product and labour markets and even go beyond the coverage in *Going for Growth* which, as I mentioned, deals also with policies related to human capital formation and innovation. Are there structural policy recipes for economic efficiency that we do not pick up? I think there are.

An obvious candidate is reform in financial markets. Financial markets obviously play a key role in allocating resources and risks within and across economies as well as in ensuring that resources are used efficiently. Yet, we know less on what constitutes efficiency enhancing policies in financial markets than in labour and product markets. At the same time, on-going events remind us that stability is a crucial concern in setting structural policies in financial markets.

A second area where we are only beginning to scratch the surface is public sector efficiency. Yet, greater efficiency in delivering public services would allow better services to be delivered or spending and taxes to be cut – in both cases boosting economic efficiency. Our recent analysis of efficiency in primary and secondary education points to potentially large gains in efficiency. Ongoing work suggests that the area of health care could have at least as large a scope for efficiency gains in many countries.

A third area is the extent to which countries make full use of human talent. Across countries the link between parents' socioeconomic status and children's education performance varies a lot. The same goes for the linkage between parents' and children's income. In some countries social inheritance clearly seems to be very strong whereas in others it is not. A strong social inheritance may be taken as a sign that children from less fortunate backgrounds do not exploit their talents to the full.

There is probably a parallel here with the extent to which immigrants and their descendants integrate in host country labour markets. In both cases, and in others, tackling the barriers that prevent full use of human resources could be very important.

The bottom line is two-fold. First, we should not lose sight of the need to implement the traditional recipes to boost efficiency. But second, we should also not lose sight of important structural policy challenges outside the currently beaten track.

Let me move to the theme of the second session this morning, namely how to actually achieve reform. Based on our surveillance, the track record differs a lot across countries – and in ways that have little to do with the need to undertake reform. So what are the factors that have made for success?

There is a large literature and we have ourselves contributed to it. So let me present some stylised facts from our empirical work. It would be interesting to understand to what extent the successes and failures that we will discuss in the second session conform or contradict these findings. Let me in quick order mention five issues.

First, on the role of macroeconomic conditions. It is a stylised fact that being in a macroeconomic mess tends to boost structural reform. Weak activity seems to be associated with more reform. This is a rather depressing finding for two reasons. First, it is not very useful – nobody would recommend driving economies into the wall in order to be able to undertake reform. Second, it means that reform is likely to be undertaken when the adjustment costs associated with reform may be high.

Second, on the role of macroeconomic policies for structural reform. There is some evidence that being in good fiscal shape is good for reform. That could be because it makes it easier to buy off people who lose from reform. It could also be because it gives confidence that if the macro economy should deteriorate as a short-term result of structural reform, for example because saving rises due to increased uncertainty, then it will be possible to stimulate the economy. On the other hand, on-going consolidation appears not to be good for reform – there may be only so much policy can do at any one time and if all the political capital is spent on consolidating there may be little left for reform.

Third, and still on the role of macroeconomic policy, there is conflicting evidence as to what monetary union does for reform. On the one hand, there is the TINA argument – TINA for there is no alternative. The point is that if countries don't have the monetary instrument to adjust then adjustment to shocks will have to be market based and countries therefore have a strong interest in getting their markets to function properly. On the other hand, without the monetary instrument the macroeconomic adjustment to structural reform may be slower and adjustment costs higher – which will tend to damp reform enthusiasm. Some have argued that as a consequence of these offsetting influences the process of structural reform under EMU may be more incremental in nature. That is countries may take smaller but more frequent steps. Whatever the merits of these various arguments, qualification for EMU has generally been associated with increased reform.

Fourth, as a stylised fact it looks as if reforms to increase international openness tend to lead reforms in domestic product markets which in turn lead labour market reform. There is no guaranty that this pattern means causality but there are some arguments why it might. So a question is whether reforms in some areas make it easier to get through with reforms in other areas. A more ambitious question is whether any such linkages, if they exist, can be used strategically to advance more rapidly on structural reform.

Fifth, and here we have no hard evidence, there is a suspicion that different ways of providing social protection may give rise to more or less resistance to change. Broadly speaking, some countries have relied on protecting people in the markets by regulating the operation of markets through job protection, minimum wages, or product market regulation. Others have interfered less directly in markets and instead relied more on public transfers and services to ensure protection. At the same time, countries provide different degrees of protection overall.

Now, looking at the backlash against globalisation specifically, and to some extent markets more generally, one gets the impression that it is strongest where overall protection is weak or where it relies fairly heavily on market intervention. By contrast, countries that provide social protection via the public finances seem to experience less of a backlash, if any at all. One might hypothesise that attitudes to structural reform could be shaped by the same influences. Which does not mean that a model of social protection through public finances is without problems. It may, for example be vulnerable if globalisation puts pressure on tax bases.

There are many other potential influences on the success or otherwise of structural reform. The role of the European Union, for example, is likely to be important but we have a session to deal with those issues in the afternoon so I will not go into it here.

Let me instead finish up so that we can get started on the real proceedings. I look forward to hearing this morning both about the agenda for structural reform and on the factors that make for success in carrying it through.