PART I

Progress in Responding to the 2005 Policy Priorities

As a general rule, the cut-off date for information used in Part I is end-2005.

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Economic Policy Reforms
Going for Growth

PART I

Chapter 1

Progress in Responding to the 2005 Policy Priorities: Overview

This chapter provides an overview of the progress achieved by member countries over the past year in taking measures consistent with the policy priorities identified in the 2005 edition. Overall, several important steps have been taken to reform competition-restraining regulations in product markets and towards improving educational outcomes in most countries where this was seen as a priority. However, less progress has been made in responding to priorities in the area of labour market policies.

Introduction

The 2005 edition of *Going for Growth* identified five policy priorities for each OECD country and the European Union to raise GDP per capita.*

This chapter provides an overview of the progress that countries have made over the past year in taking measures that are in line with these identified policy priorities. It is based on notes for each OECD country and the European Union as a whole that give more details on progress for each of the five specific priorities (see Chapter 2). In addition to the passing of legislation or other decisions to implement reforms, the chapter records earlier stages of reforms, such as government announcements and draft legislation presented to parliaments. Given that the quantitative indicators have not been updated to reflect actual or planned changes in policies, the assessment of progress is qualitative in nature. The chapter focuses on whether reforms that have been undertaken or planned are in line with the general thrust of the country-specific priorities rather than if they correspond to the detailed formulation of the priorities in the 2005 edition of *Going for Growth*.

The chapter reviews progress in reforming policies to improve labour productivity performance and labour utilisation. The key results are as follows:

- With respect to policy priorities to raise labour productivity, moves consistent with the identified policy priorities are underway or have already been made towards easing controls on entry in product markets and other competition-restraining regulations, strengthening human capital formation and reforming various other policy areas that affect labour productivity. The striking exception to this pattern is the absence of agricultural reforms, where significant progress depends on the outcome of the Doha trade round.
- With respect to policy priorities to raise labour utilisation, reforms along the lines of the identified policy priorities, especially for continental European countries, have in most cases neither taken place nor been planned. For example, few moves are underway to reduce the still high implicit tax on working beyond certain ages, cuts in tax wedges have been modest if any and reforms of employment protection legislation, labour cost floors and wage bargaining system have been virtually absent. A greater tendency towards reform can be observed in the area of disability and sickness benefit systems for the countries where this was identified as a priority.

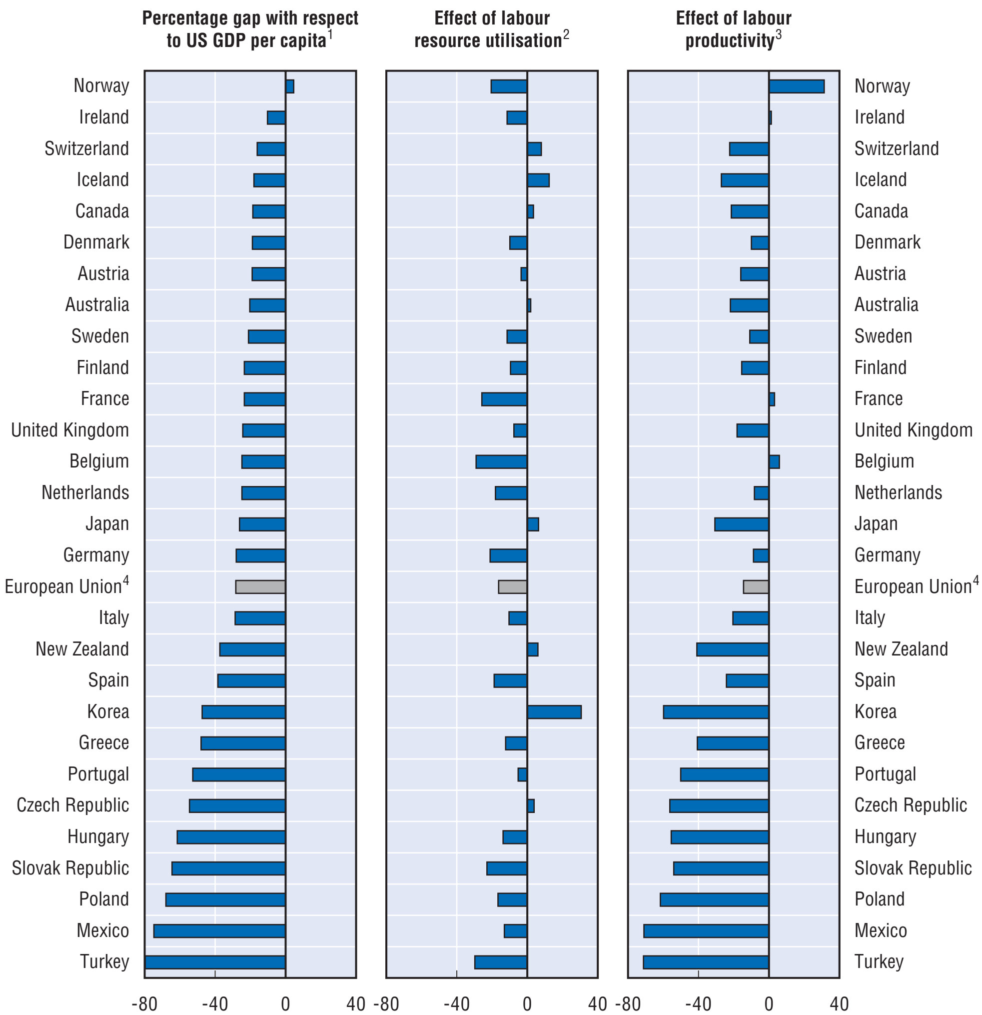
These policy changes notwithstanding, the priorities reported in the 2005 edition of *Going for Growth* still constitute by and large a relevant programme for necessary reforms.

* Three of the priorities were determined with the help of internationally-comparable indicators of performance and policy settings, which were used to uncover weaknesses in specific performance areas and to identify policy settings that could alleviate these weaknesses. The remaining two priorities were not necessarily derived on the basis of indicators – though some were – and rather drew on country-specific expertise. The indicator-based priorities were mostly confined to labour and product market policies, supplemented by policies in the areas of education and health, whereas the other policy priorities extended to various areas.

Policies to improve labour productivity performance

At least one policy priority to improve labour productivity performance was identified for all OECD countries and for the European Union. In many cases, this reflected large gaps in productivity levels *vis-à-vis* the leading country (Figure 1.1). In some countries with relatively high recorded productivity levels, it was motivated by lacklustre productivity growth rates over the past decade (Figure 1.2) and the possibility that high recorded productivity levels overstated the real strength in this area as they might be related to policy-induced under-employment of low-productivity workers. The identified policy actions to improve labour productivity performance included the easing of product market entry controls and other competition-restraining regulations, cuts in agricultural support, measures to improve educational outcomes and various other measures.

Figure 1.1. **The sources of real income differences, 2004**

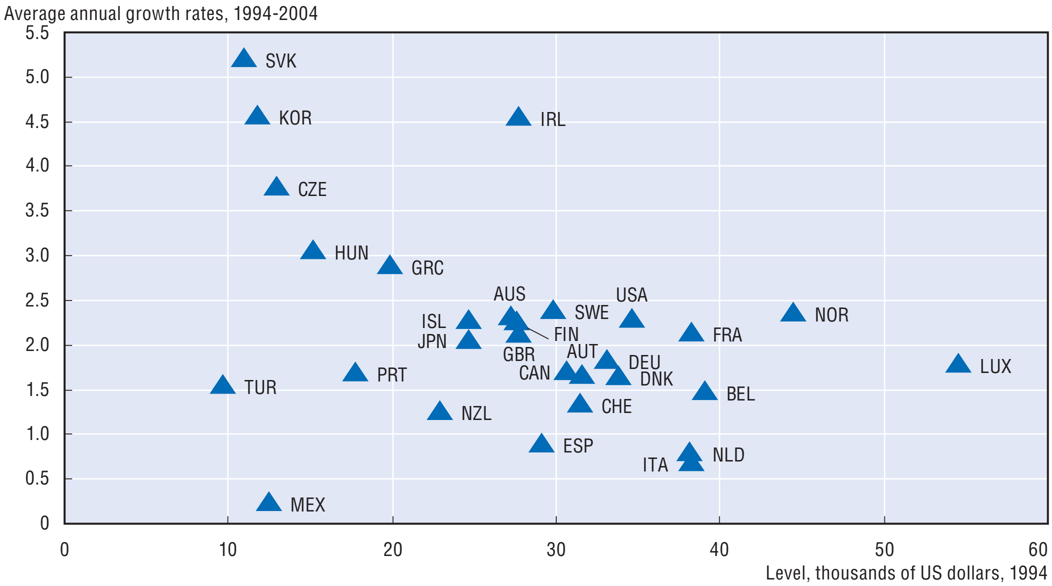


1. Based on year 2000 purchasing power parities (PPPs).
2. Labour resource utilisation is measured as total number of hours worked divided by population.
3. Labour productivity is measured as GDP per hour worked.
4. Excluding Luxembourg.

Source: OECD, *National Accounts of OECD Countries*, 2005; OECD, *Economic Outlook*, No. 78; and OECD, *Employment Outlook*, 2005.

StatLink: *http://dx.doi.org/10.1787/727533324237*

Figure 1.2. **Labour productivity:**[1] **level and growth**



1. Measured as US dollar GDP in year 2000 PPPs per hour worked.

Source: OECD, *National Accounts of OECD Countries*, 2005; and OECD, *Employment Outlook*, 2005.

StatLink: *http://dx.doi.org/10.1787/727533324237*

Easing of entry controls and other competition-restraining regulations

Given their comparatively restrictive policy stance in this area, recommendations to ease entry controls and other competition-restraining regulations were concentrated on the European Union and European member countries. The European Union has continued its effort to strengthen competition in the internal market. The draft services directive submitted to the European Parliament in April 2005 was in line with the recommendation to ease internal regulatory obstacles to cross-border trade and entry so as to strengthen competition. It remains to be seen to what extent the proposed competition-enhancing provisions will be enacted as they have raised concerns about "social dumping" from low-wage EU member countries and about the ability of national authorities to enforce national social protection legislation. The draft directive on ports introduced in late 2004 is also in line with the recommendation, although the phasing in of measures is planned over a very long period. As had been decided earlier, rail transportation for freight and passengers will be fully liberalised by 2007 and 2010, respectively, and competition in standard postal services will come into force in 2006.

At the national level, most European countries have taken some measures that are in line with the country-specific priorities to relax competition-restraining measures:

- Barriers to entry and regulations on business operations in services and industries in general, and network industries and professional services in particular, are in the process of being eased in many of the countries where such action was considered to be a priority (Table 1.1). In some cases the reform process is at an early stage. In other countries, draft legislation has been introduced for discussion in parliaments or new laws have been enacted in the area.

Table 1.1. **Progress achieved in countries with recommendations to strengthen competition law, reduce entry controls and other competition-restraining regulations**[1]

"x" denotes action

	Reviews/laws announced	Public consultation	Draft legislation introduced	Legislation concluded	Other measures
Strengthen competition law and enforcement					
Austria					X
Ireland		X			
Reduce entry controls in services and/or industries in general					
Canada					X
Denmark					X
Japan			X	X	
Korea					X
Netherlands					X
Reduce entry controls in network industries					
Australia	X				
France					
Greece				X	
Hungary					X
Ireland		X			
Korea					
Mexico				X	
Portugal					X
Slovak Republic					X
Switzerland			X		
Reduce entry controls in professional services					
Germany	X				
Switzerland			X		

1. The table covers only countries with policy recommendations in the area listed.

StatLink: *http://dx.doi.org/10.1787/727533324237*

- Administrative burdens in general, and on start-ups in particular, have been reduced through legislation or through other means in eight of the nine European countries for which action was called for in this domain (Table 1.2). In the remaining country, a review has been announced. The planned reform in the Netherlands, scheduled to be fully implemented in 2007, is particularly ambitious, aiming at cutting such costs by 25%.
- The extent and scope of public ownership has been reduced in most of the European countries where this was identified as a policy priority. Significant privatisation of government-owned commercial companies has continued in Finland and Poland. Less extensive opening up to private capital in government companies has taken place in Italy and Norway.

Outside Europe, there has also been progress in reducing barriers to entry and competition-restraining controls in the few countries where this was identified as policy priority. In Japan, the recommended regulatory reform measures are being introduced on a nation-wide basis, and a new competition law, with greater penalties and stronger detection mechanisms, was voted by parliament in April. Regulatory reforms are also continuing in Korea, with a review of existing regulations scheduled over the coming two years.

Table 1.2. **Progress achieved in countries with policy recommendations to reduce administrative costs and public ownership**[1]

"x" denotes action

	Reviews/laws announced	Public consultation	Draft legislation introduced	Legislation concluded	Other measures
Reduce administrative burdens					
Austria					X
Belgium					X
Czech Republic					X
Greece				X	
Hungary					X
Ireland		X			
Netherlands	X				X
Portugal				X	
Turkey					X
Reform bankruptcy law and corporate governance					
Italy			X	X	
United States					X
Reduce the scope of public ownership					
Finland				X	
Italy					X
Norway				X	
Poland				X	
Sweden					
Turkey	X			X	

1. The table covers only countries with policy recommendations in the area listed.

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Agriculture

Pending the outcome of the Doha trade round, no major initiatives to reduce high support to agriculture have been taken in the countries where such action was seen as a priority to raise GDP per capita. The failure to agree thus far on negotiating modalities at the WTO does not point to significant future movements in this area, and high support, albeit falling or remaining broadly constant in OECD countries in 2004 except in the United States and Korea (Table 1.3), looks set to persist on announced policies. However, some policy changes have been announced recently. For example, in the European Union, reductions in price support granted to sugar producers have been agreed, and further reductions in trade-distorting support, in particular, are being discussed. In the United States, some legislative changes have been announced to reduce assistance to farmers and further policy changes are being considered, in preparation for a new farm Bill, as the current Act will expire at the end of 2007. Moreover, in Japan, agricultural products have been included in a bilateral free trade agreement.

Human capital

Almost all countries for which strengthening some aspects of their education system was a policy priority have announced or taken relevant measures. In a few countries reforms are at an early stage. In other countries with a policy priority in the broad area of human capital improvement, the following policy changes have taken place:

- Curricula reforms at the secondary level (Iceland, Italy, Mexico and Portugal).

Table 1.3. **Agriculture: Producer support estimate,[1] 2002-04**

Percentage of gross farm receipts

	2002	2003	2004p
Australia	5	4	4
Canada	21	25	21
Czech Republic	25	29	n.c.
European Union	34	36	33
Hungary	33	28	n.c.
Iceland	70	72	69
Japan	58	59	56
Korea	65	61	63
Mexico	26	19	17
New Zealand	2	2	3
Norway	74	72	68
Poland	19	8	n.c.
Slovak Republic	21	25	n.c.
Switzerland	73	71	68
Turkey	20	29	27
United States	18	15	18
OECD	31	30	30

p: Provisional.

n.c.: Not calculated.

1. The monetary value of transfers from consumers and budgetary payments to producers.

Source: OECD, *Agricultural Policies in OECD Countries: Monitoring and Evaluation*, 2005.

StatLink: *http://dx.doi.org/10.1787/727533324237*

- Establishment of nation-wide educational standards in some fields (Germany).
- Organisational changes to increase efficiency in general (Iceland and Mexico) or at the tertiary level in particular (Austria).
- More efforts to strengthen educational achievements of particular groups: ethnic minorities (Belgium, Germany and New Zealand) and girls (Turkey).
- Easier access to vocational education (Australia and Luxembourg).

Other priorities and reforms

Significant progress in reforms has also been recorded in other policy areas that were identified for several countries as important to strengthen their productivity performance:

- *Public sector efficiency.* All countries with an identified policy priority in this broad area have taken actions that are in line with the recommendations. Contestability has been raised in public services in the United Kingdom, new financial management arrangements have been introduced in Iceland and Turkey, new technology is being harnessed to simplify procedures in Luxembourg, a new staff management system (including performance-related pay and a new career management system) has been announced in Portugal, and a new law on public procurement is being prepared in Germany.
- *FDI restrictions.* Of the five countries with a priority to ease restrictions on foreign direct investment, Japan, Korea and New Zealand took some action in this area.

There was also some progress in responding to policy recommendations that were concentrated on a smaller set of countries. Thus, measures have been taken, or are planned, to improve public infrastructure (New Zealand and the United Kingdom), reduce capital income taxes (Canada), reform the financial sector (Japan and Korea), strengthen corporate governance and reform bankruptcy legislation (Italy and the United States) and ease planning and zoning restrictions (the Netherlands and the United Kingdom).

Policies to increase labour utilisation

Given their relatively low labour utilisation, corrective policy priorities in this area were concentrated on continental European countries. In many of these countries, labour force participation rates are relatively low, especially among older workers; levels of unemployment are relatively high; and annual working hours are shorter than in other OECD areas (Figure 1.3). Reforms to reduce disincentives to work were considered to be less pressing outside continental Europe. Nevertheless, policy priorities were identified for many countries outside continental Europe, most notably to slow the increase in the number of disability benefit recipients over the past decade and if possible reduce the numbers where these are already large. Recommendations in this area dealt with, in particular, the disincentives to work at older ages, the taxation of labour income in general and of low labour incomes in particular, employment protection legislation, and wage determination, especially for low-productivity workers.

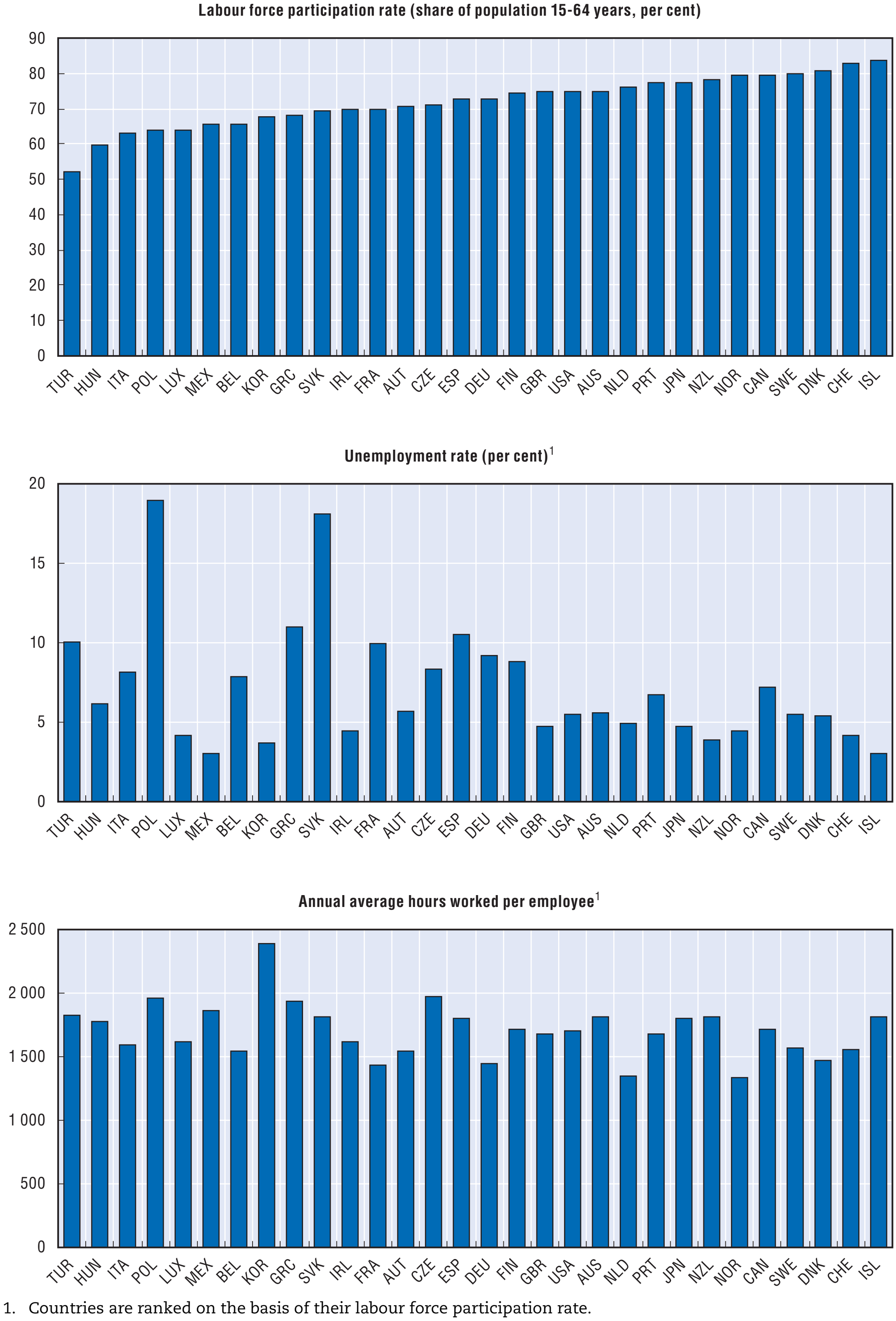
Financial disincentives to work at older ages

Limited progress has been achieved in reducing the financial disincentives to work at older ages over the past year in those European countries where this was seen as a policy priority to increase GDP per capita. Some of these countries (Finland and Italy) had earlier taken significant, though insufficient, measures to reduce disincentives in either pension systems or *de facto* early retirement systems, and recent efforts have been concentrated on implementing these reforms. Other countries have introduced new reforms to lower disincentives. Germany will reduce the length of time to which older workers are entitled to unemployment benefits as of 2008, and the government plans to phase-in an increase in the statutory retirement age from 65 to 67 over a long period. Belgium will raise the minimum age limit for entry into the early retirement pension scheme. France has announced measures in early 2006 to increase the incentives to work at ages over 57. Austria has further reduced financial disincentives to work at older ages, in addition to aligning pension arrangements for public sector workers on those in the private sector. Norway has introduced a major pension reform, setting out the principles for the future evolution of the retirement system, but crucial elements affecting work incentives are being reconsidered. No recent moves towards reform of pension or other benefit systems have been recorded in Greece, Luxembourg, the Slovak Republic or Spain.

Tax wedges

Moves to reduce tax wedges on labour income in general, and on low income in particular, have been modest in most of the countries where such action was called for to stimulate growth. A few countries (Belgium, Denmark and Slovak Republic) have programmed or stated their intent to introduce tax cuts when the state of public finances allows. To create room to lower social security contributions, the Netherlands has made some changes in the unemployment benefit system. The lack of fiscal room prompted Hungary to limit *de facto* cuts in employer social security contribution to specific groups of workers. In the most recent period, Australia, Finland and Sweden have taken the strongest measures to lower tax wedges in line with the recommendations for these

Figure 1.3. **Labour resource utilisation, 2004**



1. Countries are ranked on the basis of their labour force participation rate.

Source: OECD, *Economic Outlook*, No. 78; OECD, *Labour Force Statistics*, 2005; and OECD, *Employment Outlook*, 2005.

StatLink: *http://dx.doi.org/10.1787/727533324237* countries. In Australia, it reflected the comfortable budget situation; in Finland it was decided as part of an incomes policy agreement; and in Sweden, it was achieved by shifting the tax base towards green taxes. Italy has also taken measures to cut taxes on labour use over the coming three years. Germany recently announced a reduction in employers' social security contributions together with an increase of indirect taxes.

Labour market policies

The modest progress in most European countries in reducing financial disincentives to work at older ages and cutting tax wedges also extends to other labour market policies:

- *Employment protection legislation* has remained unchanged in three of the five European countries where an easing was identified as a priority (Czech Republic, Portugal and Spain). However, France decided to repeal a tightening of statutory employment protection that had been decided but where implementation had been repeatedly postponed, and has recently extended to two years the length of the trial period for new recruits to firms with 20 employees or less and for workers of age under 26 who are recruited for the first time by a firm with more than 20 employees. Greece has recently abolished permanent contracts for new employers in all public entities and entreprises.
- *Minimum labour costs* are to be cut in France by eliminating remaining social security contributions at the level of the minimum wage by 2007, partly offsetting the impact of the significant increase in hourly minimum wages in mid-2005. In Poland, the increase in the statutory wage floor had been kept below overall wage increases, but the minimum wage is now set to rise relative to the average wage in the next few years.
- *Wage bargaining arrangements* have not changed in the three European countries where increased flexibility in wage determination was identified as a priority (Finland, Italy and Spain).
- *Unemployment benefit systems* reform has been initiated in Belgium with closer monitoring of entitlement conditions for recipients has been initiated in Belgium. On the other hand, no action has so far been taken in Finland or Luxembourg to reduce disincentives in their benefit systems.

Outside Europe, some movements towards reforms in labour market policy areas have been recorded in the few countries where this was seen as a priority. This is notably the case in Australia, where a reform of the industrial relation system has been announced which would include changes in the determination of minimum wages ("award" wages). Canada has started pilot projects in high-unemployment areas to examine the impact of changes in entitlement conditions. With respect to employment protection legislation, a roadmap for reforms has been proposed by the authorities in Korea and is being discussed by the social partners; no legislative changes in this area have been announced in Japan.

Reforming disability and sickness benefit systems

Some progress has been achieved in reforming disability and/or sickness benefit systems in the nine countries where this was seen to be a key policy priority. A major reform of the disability benefit system in the Netherlands was decided in June 2005, including the abolition of benefits for those with modest disabilities and stronger financial incentives to work for those with residual work capacity. Elsewhere, actual changes have been less comprehensive, focusing on stronger medical guidelines for assessing disability (Denmark, Hungary); time limits on benefits without reviews and organisational changes to improve implementation of policies (Sweden); and greater employment assistance, and training and rehabilitation services (Australia). Major reforms have been announced in Norway, Switzerland and the United Kingdom, stressing the importance of early intervention to encourage closer attachment to the labour market of beneficiaries with remaining work capacity.

The abandonment or postponement of earlier plans to reform disability benefit systems in a few countries demonstrates the difficulties in moving forward in this area. In Poland, the country with the highest proportion of the working-age population not working and receiving disability benefits in the OECD, plans for greater monitoring of entitlement conditions and imposing limits on benefit periods without re-examination will not concern existing recipients of disability pensions. Also, in Norway the planned reduction in replacement rates in the sickness benefit system has been postponed, and in Denmark negotiations concerning co-financing of sickness benefits in large municipalities are on hold.

Other priorities and reforms

The record of OECD countries in reforming other areas considered to be a priority to increase labour utilisation and mobility has been mixed. With respect to housing policy, the authorities have stated their intention to reform mortgage lending. The Netherlands has presented its policy in the area of zoning restrictions that affects housing supply. However, little action has yet taken place in some countries where it was identified as a priority to liberalise the rented housing market (Czech Republic and Sweden) and improve the housing infrastructure (Poland), and in the case of Hungary and the Slovak Republic moves went in the opposite direction, with an increase in mortgage subsidies. No action was recorded in reducing the tax subsidy to housing loans in Ireland or Spain.