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NEW APPROACHES TO ECONOMIC CHALLENGES (NAEC)

EXECUTIVE SUMMARY

OECD

BETTER POLICIES FOR BETTER LIVES

New Approaches to Economic Challenges (NAEC)

Executive Summary

KEY MESSAGES

The New Approaches to Economic Challenges (NAEC) initiative was launched at the OECD in 2012 as an organisation-wide reflection process on the roots and lessons from the crisis, as well as long-term, global trends, with the aim to continuously improve the OECD analytical frameworks and policy advice. NAEC was also launched as part of a broader effort to build an inclusive and sustainable agenda for growth and well-being.

The NAEC initiative recognises the increased interconnectedness and complexity of the global economy, and the need to better understand how it works. It calls for a multidisciplinary perspective to address social and economic challenges, avoiding a silo approach and considering the trade-offs and synergies among different policy objectives. It underlines the need to focus policies on improving people's wellbeing, through a multidimensional approach, where income is one important element, among many more that matter for people's lives, including health, environment, education and life satisfaction. Finally, it recognises global trends that are impacting decision making, including climate change, population ageing, natural resource depletion, increased inequality, and therefore the need to consider "stocks" or "wealth creation" and shift away from the current heavy emphasis on "flows".

Some preliminary policy recommendations that are emerging from this 'work in progress' are presented in this Executive Summary, which distils the main messages of a broader Synthesis paper [C/MIN(2014)2].

Message 1: Increase macroeconomic stability

NAEC emphasises the need to increase macroeconomic stability by implementing an effective regulatory framework, promoting fiscal soundness, fostering the counter-cyclicality of macroeconomic policies and improving the stability, inclusiveness and sustainability of the financial sector. In particular, it recommends policy makers to:

- Undertake ambitious and well-calibrated **structural reforms** to build the foundations of resilient, adaptive and dynamic economies.
- Pay close attention to the **choice of consolidation instruments,** when the containment and reduction of public debt levels is needed.
- Make **contingent liabilities of the public sector visible** and introduce **safeguards between the public and the financial sector.**
- Enhance the counter-cyclicality of fiscal policy by strengthening **automatic stabilisers**, where appropriate.
- Focus the attention of central banks and other supervisory bodies on a **broader set of indicators** and consider the longer term when targeting inflation, according to their respective mandates.
- Continue **strengthening the regulatory and supervisory framework of the financial sector**, including by tracking and disclosing a leverage ratio in addition to other existing and more commonly used indicators, so that financial markets can safely perform their role as conveyor belts of the economy.
- **Re-integrate consumers in business models of financial services providers**, including by enhancing financial consumer protection and financial education.

Message 2: Move towards a more inclusive growth

The last three decades have seen a rise of inequality, which can affect economic growth, weaken social cohesion and sap trust in markets and institutions. To address the growing concerns linked to increasing inequality, policy makers are advised to support a **move towards a more inclusive and sustainable economic approach** and to:

- **Move towards an inclusive growth model** in which income inequality is one element, but broaden it to include several other dimensions that matter for people's well-being, including health, employment and the environment. Put more focus on **multidimensionality** of policy objectives and **distributional issues**.
- **Develop more effective policies to tackle social challenges**, focusing on the median and household disposable income and avoiding average indicators that hide disparities.
- Pay more attention to **trade-offs and complementarities** when designing and implementing structural reforms, and **consider their short- and long-term distributional implications**.

- Foster **new sources of employment**, including by promoting policies that allow young firms to experiment and ensure a level playing field for new and innovative firms.
- Pay more attention to **job quality**.
- Invest in **education, skills and life-long learning for all** and develop new dimensions in education objectives, encompassing soft skills that foster creative thinking, team work, self-awareness and tolerance.
- Ensure **fairness in the tax system**, including tax compliance by all taxpayers.

Message 3: Address long-term challenges linked to population ageing and the environment, in particular climate change

Another important message emerging from NAEC is the urgency of **addressing long-term challenges, in particular those linked to the environment and population ageing:**

- Avoid uni-dimensional silo approaches and **develop whole-of-government strategies** to address challenges resulting from ageing populations, cutting across many policy areas, such as pensions, labour markets, education, innovation, migration and financial markets regulation.
- Find **co-operative policy solutions to face the global consequences of climate change, air pollution, biodiversity loss, deforestation, and water scarcity**.
- Another critical challenge relates to the expected **growing dependence of long-term economic growth on investment in knowledge-based assets, the related skill-biased technical progress and their effects on multi-factor productivity**. Policy implications will be analysed further as relevant NAEC work deliver specific results.

Message 4: Rebuild trust in institutions

Governments are faced with a dramatic decrease in public trust towards markets, public institutions and governments themselves. To **rebuild trust**, policy makers are advised to:

- Invest in building **institutional capacities** and reinforce governments' capacity to **implement reforms** and **to measure and monitor progress.**
- Reinforce and effectively implement policies aiming at ensuring **citizens' engagement, access to information and open government.**
- Reinforce and effectively implement policies aiming at **managing conflict of interest**, fostering **high standards of conduct in the public sector**, and adequately **regulating lobbying and political finance.**

Message 5: Enhance international co-operation, including regulatory co-operation, and policy co-ordination

In an increasingly interconnected world economy, it is important to **enhance international co-operation.** To this end, NAEC recommends policy makers to:

Increase international co-operation in regulatory policy and competition law enforcement with a view to improving regulatory design and implementation, increasing policy effectiveness, and reducing unnecessary costs.

- **Enhance policy co-ordination**, including on stabilisation, structural policies and the environment, both to pursue shared goals and to address international spill-overs.
- **Reduce unnecessary barriers to trade and investment** that hinder development of global value chains and constrain development, growth and job opportunities.

Message 6: Continue updating, renewing and strengthening OECD analytical frameworks and tools

The work under NAEC also underlines **several areas in which the OECD should deepen its efforts** to provide more relevant, better targeted and new evidence-based analysis, and to broaden its analytical toolkit to include a multidisciplinary approach. Some avenues are as follows:

- Upgrade the Organisation's **surveillance framework and strengthen its surveillance capacity** by regularly checking the vulnerabilities and resilience of economies against short and long-term shocks.
- Further **develop strategic foresight capabilities**.
- Further **strengthen and mainstream work on well-being,** including on Inclusive Growth and Green Growth.
- Reinforce the analysis of the **linkages between the financial system and the real economy** and further develop analytical tools to improve the understanding of the health of the financial sector, including evidence-based analysis of the business models of banks and of their distance to default, as well as related work on how to ensure **appropriate financing of long-term investment**.
- Further develop the **databases on Trade in Value Added** and accelerate efforts to build new cross-country datasets to provide insights into other aspects of Global Value Chains, notably investment, jobs and skills.
- **Put more focus on the measurement of stocks** of economic, human, social and natural capital, to complement the current flow-based analysis **and facilitate the shift to more sustainable and long-term approaches.**
- **Accelerate OECD work on environmental degradation** to better understand the impact of environmental degradation on growth, fully grasp the distributional impacts of environmental policies, and better integrate the environment in economic projections and horizon scanning exercises.
- Use a **greater variety of models**, continuously update them, and enhance participation in multi-model comparisons. Continuously review and update fundamental assumptions*, e.g.* on the nature of risk and the distribution of risk factors or the role of the financial sector.
- **Use microdata more systematically** and connect microdata from different national and thematic sources. Further **explore the potential of "big data",** and the challenges related to its collection, transportation, storage and use.
- Further develop the use of **alternative economic approaches, including behavioural economics**, and provide a platform for sharing knowledge and national experiences on applying such insights in policy making.
- Further reinforce **horizontal work and interaction**.
- Strengthen support to **international policy co-ordination.**

1. The New Approaches to Economic Challenges (NAEC) initiative was launched in 2012 as an organisation-wide reflection on the roots and lessons of the crisis with the aim to catalyse a process of continuous improvement of the OECD analytical frameworks and policy advice. NAEC was also launched as part of a broader effort to build an inclusive and sustainable agenda for growth and well-being. A NAEC Interim Report was presented at the 2013 Ministerial Council Meeting (MCM), which outlined 29 specific projects that are being undertaken as part of NAEC.

2. This paper discusses lessons from the crisis and presents a summary of the Synthesis [C/MIN(2014)2] of main results emerging from the NAEC initiative until now, while the Synthesis itself catalogues a number of more specific issues. This paper also sketches implications for the OECD, both in terms of policies, as well as analytical tools and methods that should be further developed to better advise governments on how to address the challenges of an increasingly interconnected and complex global economy. These preliminary results might evolve as the discussion within and across Committees continues. The Synthesis and its Executive Summary will be key resources as OECD Directorates and Committees collaborate and formulate Programmes of Work and Budget.

I. Reflection on the crisis

3. The NAEC initiative has highlighted how, among other factors, the increasing financial market integration and interdependence that followed deregulation in the 1980s and the 1990s contributed to the build-up of unsustainable financial imbalances. The crisis erupted against the backdrop of a range of weaknesses in many countries' financial sectors, including flawed incentives across a wide spectrum of financial market participants. These factors pushed down interest rates and led to excessive debt accumulation by households, firms and some governments, while facilitating the build-up of global imbalances in savings and investment, among others, given the policy divergence between some advanced and emerging economies. In addition, these developments were paralleled by insufficient fiscal discipline and lack of structural reforms in many OECD countries in the years before the crisis.

4. However, while there were numerous signs of trouble ahead of the crisis, by and large, policy makers and economists underestimated the tensions that were building up in the global economy. Prevalent analytical approaches often failed to capture the complexity of the global economy and society as a whole, and the interconnectedness between and within economies. We were not equipped to fully understand the inter-linkages between the financial sector and the real economy, and how these could lead to unstainable imbalances. Many analysts, OECD included, were also looking at and interpreting evidence with approaches and models which did not adequately reflect the behaviour of economic agents. The definition of people as "rational agents", as well as assumptions like the capacity of markets to stabilise themselves, led to an overestimation of the resilience of economic systems and of their capacity to overcome imbalances in the face of a historically large shock. At the international level, the "single issue focus" of intergovernmental organisations may have prevented them from cross-pollinating, comparing notes, and signalling sources of concerns. This caused us to miss the onset and the magnitude of the problems and to underestimate the severity of their impact.

5. At the same the rise in inequalities of market income and wealth was insufficiently addressed by policy makers. In fact, there was a secular decline of the ability of the tax and benefit systems to contain the increase in inequalities. While the debate about the role of inequality in the run-up to the crisis is not fully settled as of now, the rise of inequality has certainly complicated the response of policy makers to the crisis, *inter alia* by making fiscal consolidation measures and structural reforms politically and socially very difficult. Further analysis suggests that certain patterns of inequality might be detrimental to growth, for example when inequality of opportunities prevents low income households to invest in education. As a result, there is increasing awareness amongst policy makers and economists alike of the urgent need to design and implement more inclusive models of economic growth.

6. Group thinking sometimes precluded hearing diverse and diverging views, while lobbying by interest groups, in some cases, prevented necessary reforms. The prioritisation of efficiency criteria and a silo approach in policy making sometimes brought unintended consequences. Preferential use of quantitative models also led at times to disregard important qualitative aspects of well-being. As a consequence, growth has often been considered as an end, rather than a mean to improve the well-being of the population. Therefore, issues such as inequality and environmental harm were sometimes treated as secondary effects to be addressed at a later stage. This prevented a balanced analysis of the trade-offs and synergies between different policy options and a thorough understanding of the unintended consequences of policy decisions.

7. Several reforms after the crisis have gone in the right direction. The crisis and ensuing recession have indeed acted as a catalyst for a range of structural reforms. However, we are still in a context of a weak and uneven recovery, and further efforts are necessary to rebuild trust, continue banking sector reforms, fight high unemployment and underemployment, tackle inequality, reduce public debt, deal with large central bank balance sheets and outstanding guarantees, and encourage innovation and growth. Moreover, while the recent crisis reflected systemic vulnerabilities in the financial sector, future systemic vulnerabilities may originate from elsewhere and may be transmitted through other channels.

II. Emerging policy themes and recommendations

8. The NAEC Synthesis outlines some emerging policy themes and recommendations to build a more solid path to resilient economic growth and well-being. The insights and recommendations outlined in this note present a partial and preliminary view of what is emerging from the NAEC initiative. They will inform the work of OECD Committees, will in turn benefit from their guidance and should then be carried out and mainstreamed in OECD work. The crisis has sparked a reflection on what went wrong, but also on what lies ahead. The project "*OECD@100: Policies for a Shifting World*" is an initial attempt to provide new insights on future trends and tensions that are likely to shape the policy environment over the next fifty years.

(i) The first message emerging from NAEC is a call to increase macroeconomic stability to improve the resilience of economies to large shocks.

9. The crisis has highlighted the need to make our economies more resilient to large shocks. To achieve greater macroeconomic stability, the counter-cyclicality and sustainability of macroeconomic policy needs to be increased. It is also important to strengthen, when appropriate, automatic stabilisers and the responsiveness of public spending, such as unemployment compensation, food programmes, and welfare benefits to the cycle. In addition, a number of discretionary macroeconomic policy options should be considered. Many governments continue to face a need for fiscal consolidation to reduce and stabilise public debt. To achieve this, it is first critical to contain and reduce public debt levels during expansionary phases. When consolidation is needed, close attention also needs to be paid to its timing and the choice of consolidation instruments to mitigate its distributional impacts, particularly on the most vulnerable populations. It is also necessary to make contingent liabilities of the public sector visible and to introduce safeguards between the public and the financial sector. In addition, central banks and other supervisory bodies might focus on a broader set of indicators and consider the longer term when targeting inflation, according to their respective mandates.

10. Improving the stability, inclusiveness and sustainability of the financial system is also essential to increase macro resilience and to foster growth. NAEC has underlined the importance for the financial sector to return to fulfilling its essential role of intermediation and to provide the necessary capital for productive activities. To start with, financial repair needs to be completed, and risk taking behaviour reduced. Furthermore, the OECD has called for a strengthening of the regulatory framework and for

making it more effective. To this end, the OECD Secretariat has proposed methods to assess its effectiveness (*e.g.* based on a distance-to-default indicator) as well as complementary proposals (*e.g.* structural separation requirements applicable to banking groups and leverage ratio), in addition to other existing and more commonly used measures. OECD member countries have not reached consensus on the proposals of the OECD Secretariat. Co-ordinated work of the OECD with the International Monetary Fund (IMF) and the Financial Stability Board (FSB) on cross-border consistencies and global financial stability implications, currently taking place under the auspices of the G20, will inform future recommendations. Finally, to support an orderly and efficient functioning of financial markets, it is also urgent to (re-)integrate consumers in financial models, including by enhancing financial consumer protection and financial education.

(ii) The second main message emerging from NAEC is to move towards more inclusive growth.

11. The reflection on the crisis highlights the need to further mainstream a holistic approach to policy making where people are put at the centre of the economic and social policy. Enhanced productivity and growth are necessary to increase wealth and to achieve social inclusion. However, while growth can contribute to a higher standard of living, its benefits will not automatically trickle down evenly to all sectors of society. Growth should thus be recognised as a mean but not an end. It is also critical to pay more attention to trade-offs and complementarities when designing and implementing structural reforms, particularly between growth and equity, as well as to consider short- and long-term distributional implications of structural reforms along income and non-income dimensions that matter for subjective well-being. This will be helpful to inform the policy debate and provide policymakers with a toolkit for country-specific strategies for inclusive growth.

12. Income and wealth inequality was on the rise in the run-up to the crisis, as well as after the crisis. With growth increasingly driven by knowledge and skills, earning inequality before taxes and transfers in the average OECD country could rise by more than 30% by 2060 if nothing is done (OECD@100), pointing to the size of the potential redistributive challenge. Against this background, governments need to consider ways to effectively address inequality and pressures on social institutions as well as the distributional impact of different policies. This refers not only to income, wealth and access to public services (*e.g.* education, health, housing), but also to the opportunities for people to thrive and succeed. Effective policies to tackle inequality should focus in particular on low-income households and on preventing the middle-class from falling behind.

13. Structural reforms that promote inclusiveness and sustainable growth should be part of a comprehensive package, which includes measures to promote better paying jobs, more effective active labour market policies, measures to improve the match between the skills provided by the education system and those demanded by a changing economic environment, and efforts to help incumbent workers gain the skills needed to move into more highly skilled jobs. It is also crucial to investigate and monitor the effects of different labour market policies on disadvantaged groups, in particular on youth. Policies that increase female participation in labour markets, that reduce the gender wage gap and that foster the integration of immigrants are also warranted. To ensure more inclusive growth, there should be adequate safety nets and social welfare policies need to compensate for differences in exogenous factors ("circumstances") that reduce opportunities.

14. Another critical avenue in moving towards more inclusive growth is to foster new sources of employment. To this end, policies that support the creation and expansion of new businesses should be promoted, as young businesses, and start-ups in particular, are key drivers of job creation. This involves reducing barriers to firm entry, to the growth of firms over time, and to the potential exit or failure of firms. It is also crucial to ensure a level playing field for new and innovative firms and to promote access to finance and other business services that promote entrepreneurship. Moreover, policies need to allow

knowledge and innovations to be diffused throughout society, *e.g.* through competition policies and policies aimed at knowledge transfer. Inclusive innovation policies are also necessary in order to enhance access to knowledge and enable more individuals and firms to engage in innovation. It is also important to ensure the redistribution of benefits from innovation through social policies, as innovation does not benefit all individuals and groups in society to the same extent and may therefore not directly contribute to more inclusive growth.

15. Paying attention to job quality is also warranted. It is in particular necessary to investigate further the impact of job quality on well-being, and more specifically on household income inequality, access to training and social benefits systems, and on poverty risk in general. Moreover, emerging evidence suggests that while non-standard work might be an important first step to (re-)enter the labour market for some groups, the probability to use non-standard work as an entry to standard work is particularly small for young temporary workers. This evidence also calls for paying special attention to the vulnerable economic situation of households with only low-paid/ non-standard work arrangements.

16. Emerging recommendations under NAEC also reiterate the call to invest in education, skills and life-long learning for all. Governments need to focus their attention on how skills are being developed, activated and used, and in particular to implement policies that increase equality of opportunities in skills development. Public funding should be focused on where social benefits are the highest, *i.e.* early stages of education and disadvantaged individuals. It is also crucial to develop links between the world of learning and the world of work, and to pay particular attention to those most at risk of poor or declining skills efficiency, such as foreign-language migrants and ageing workers.

17. Policies also need to support the development of non-cognitive skills, such as perseverance, diligence, respect, solidarity and self-esteem, as they can be as powerful as cognitive skills to build successful individuals and societies. Education and skills are not only tools to succeed in the labour market. OECD work should also take a hard look at “soft skills” and the role of education to promote more inclusive, democratic and peaceful societies.

18. Last but not least, there is a need to ensure a fair tax system: one that both helps to achieve equity goals and promotes tax compliance by all taxpayers, as well as to design more equity-friendly fiscal consolidation programmes that balance the need to increase tax revenues with social objectives. Work undertaken as part of NAEC demonstrates that it is possible to consider both equity and growth objectives when designing and implementing necessary fiscal consolidation measures. It also discusses circumstances when ensuring tax fairness could be achieved by raising taxes for top income recipients, in particular by raising their average tax rate without raising their marginal tax rates. The tax base could also be enlarged by tackling illicit financial flows, including off-shore tax evasion, money laundering and international bribery. Fighting against Base Erosion and Profit Shifting (BEPS) is another major and necessary step towards a fairer tax system, and the NAEC initiative reiterates the call for implementing the BEPS Action Plan.

(iii) The third main message emerging from NAEC is an urgent call to address long-term challenges, linked to the environment and population ageing, in order to secure a sustainable growth.

19. Whole-of-government strategies are needed to face the strong headwinds that ageing populations will pose to economic growth and well-being. These strategies need to cut across many and closely entwined policy areas, including pensions, labour markets, education, innovation, and financial markets regulation. Spending and tax reforms, as well as structural reforms are proposed to deal with the fiscal pressures posed by ageing populations and to improve the efficiency of the health system. Technological, organisational and social innovation could also help to improve the quality of health care, patient safety

and care co-ordination. Further, in order to alter the proportion of those paying for and those receiving services, NAEC suggests regularly updating pension schemes to longevity, to the extent that distributional impacts are considered and the population's health status can be maintained throughout the higher age. Migration-friendly policies could also help alleviating the natural decline in the working age population of the OECD.

20. On the environment, first results from NAEC suggest significant negative impacts of climate change on long-term growth, and call for a co-operative policy solution to face the global consequences of climate change, air pollution, biodiversity loss, deforestation and water scarcity. They also point to possible lock-in effects, which may make it much more costly to take action on environmental challenges in the future if little action is taken now. For example, business as usual growth is likely to lead to a 50% increase in greenhouse gas emissions by 2050. NAEC insights also indicate that there is scope for more stringent environmental policies without necessarily harming innovation or productivity growth. However, policy makers need to ensure that these policies are competition-friendly and cost-efficient, so as to level the playing field among incumbents and new entrants, to encourage new and more environmentally-friendly technology adoption and to allow entry of firms with new business models. Environmental indicators need to become part and parcel of the tools to design sound economic policies.

21. Another challenge relates to the expected increasing dependence of long-term economic growth on multi-factor productivity growth, as the contribution of labour input is expected to decline in most OECD countries. Further, EEs might move towards more skill-based activities. Productivity growth is critical for raising wages and requires well-functioning, competitive markets that drive innovation. Policies that support open markets, investment and private sector-led growth, and that foster innovation, as well as investment in knowledge-based capital, are thus central. Policies that help economies to better adjust to structural changes will also be useful. Work under NAEC on long-term productivity growth is still at an early stage and more results will be outlined as the work evolves.

(iv) The fourth message is a renewed call to rebuild trust in public institutions.

22. Governments are faced with a dramatic decrease in public trust towards both market and public institutions, as well as towards the governments themselves. To rebuild trust, policies aiming at ensuring citizens' engagement, access to information and open government need to be reinforced and effectively implemented. Effectively managing conflicts of interest, high standards of conduct in the public sector, and adequate lobbying and political finance regulation are also crucial to limit undue influence and build safeguards to protect the public interest.

(v) The fifth message is the need to increase international regulatory co-operation and policy co-ordination.

23. It is urgent to increase international regulatory co-operation, with a view to improving regulatory design and implementation, increasing policy effectiveness, and reducing unnecessary costs on society, individuals, and businesses. Co-operation on cross-border enforcement is also becoming more necessary and may require the exploration of new tools to make co-operation more effective, particularly on competition. More generally, policy co-ordination may help countries to pursue their shared goals and to address international spill-overs. Increasing macroeconomic stability, moving to a more inclusive growth, and properly addressing long-term challenges such as environmental sustainability, may benefit from deeper and more effective international co-ordination, including regarding stabilisation and structural policies.

III. Moving ahead: implications for OECD work

24. NAEC was born as an OECD reflection on the causes of the crisis. But its most important contribution is to spur work towards policies that allow not only to overcome the crisis, but also to build more resilient, inclusive and prosperous societies. In this sense, it seeks to address the legacies of the crisis, such as high debts, unemployment and rising inequality, to foster structural reforms and to reignite the engines of the international economy, including trade, investment and growth in emerging and developing economies.

25. The work under NAEC underlines several areas in which the OECD should deepen its efforts to provide more relevant, better targeted and new evidence-based analysis to member and partner countries. Some of the avenues discussed in this section are already being explored under NAEC and might have already been mainstreamed. Others might require new undertakings or still need to become part of the regular analytical, advisory, deliberative work programme of the OECD Directorates and Committees, which should remain essential for deciding on how to do so.

26. It is important to continually review and strengthen forecasting processes, as well as to review their relevance to policy making. The OECD – and many other Organisations – underestimated the fragility of the international financial system in the run-up to the crisis, as well as its potential impacts on the real economy. It also did not sufficiently consider the rising global interconnectedness and how quickly the impacts of the crisis would spread globally. Significant progress has subsequently been made in revising forecasting processes. The Organisation needs to continue reflecting on and reforming these processes to better identify various risks, particularly by better integrating the financial sector and related risks in its analysis, by further developing scenario analysis, and by deepening its exploration of tail risks. The Organisation could also upgrade its surveillance frameworks and strengthen its surveillance capacity by regularly checking the vulnerabilities and resilience of economies against short- and long-term shocks, while considering the scope and findings of other international and regional organisations' relevant work. This will enhance the complementarity of OECD work with that of the other international and regional organisations which carry out surveillance.

27. It is also critical to better understand interconnectedness, its policy implications and resulting policy trade-offs. The OECD thus needs to better understand multidimensionality and to further strengthen and mainstream existing work on well-being, which provides a major opportunity to analyse trade-offs and complementarities among policy objectives. One particularly promising avenue to make the well-being agenda policy-actionable is the ongoing initiative on Inclusive Growth.

28. Further, reinforcing the analysis of the linkages between the financial system and the real economy is key not only to improve forecasting and the accuracy of our analytical models, but also to develop relevant policy options to foster appropriate financing of long-term investment. As we aim to better understand the workings of the international economy, it is necessary to strengthen our evidence base by further developing our databases on Trade in Value Added (TiVA) and by accelerating efforts to build new cross-country datasets that provide insights into other aspects of Global Value Chains (GVCs), notably investment, jobs, and skills, which are critical to understand the complexity of our global economy.

29. Global economic growth over past decades has come at an increasing cost to the environment. Unless more significant policy action is taken now, continued environmental degradation will pose severe risks to human well-being. OECD work on environmental degradation needs to be accelerated. In particular, more analysis is needed to better understand the impact of environmental degradation on growth and to fully grasp the distributional impacts of environmental policies. It is also necessary to further mainstream OECD work on green growth, as well as to better integrate the environment in economic projections and horizon scanning exercises.

30. Another major challenge for the OECD going forward is to develop tools to better grasp interconnectedness, heterogeneity and complexity. The crisis indeed confirmed the need to continuously rethink, adapt and enhance our analytical frameworks and tools. The OECD should thus use a greater variety of models, continuously update them, enhance its participation in multi-model comparison exercises, while keeping in mind the limitations and boundaries of different models and explicitly stating the assumptions on which they are built. It should also take into account different data to look at evidence from complementary angles. In order to reinforce the relevance of our analysis, we need to enrich our tool box by drawing more on qualitative inputs from other disciplines. In addition to the search for new models, the OECD should continuously review and update its fundamental assumptions, *e.g.* on the nature of risk and the distribution of risk factors or the role of the financial sector.

31. With regards to data, the Organisation should strengthen its efforts to provide access and more systematically use microdata, including household and firm-level data linked across national and thematic sources. The OECD is very well-placed to develop new indicators from microdata and to ensure co-ordination among countries in this field. Similarly, the collection and exploitation of large data flows from global data traffic, called "big data", provides a huge resource for innovative analyses. "Big data" could for example prove helpful for analysing productivity growth and innovation in the long term, but also for developing well-being indicators on trust, reciprocity, discrimination, etc. The OECD could further explore the potential use of "big data", as well as the challenges related to its collection, transportation, storage and use. It should also put more focus on the measurement of stocks and consider both stock and flow concepts in its analyses.

32. In addition, insights from academic research, including in behavioural economics and different strands of social sciences, as well as close consultation with different disciplines and stakeholders could be helpful. In particular, the Organisation could further develop the use of behavioural economics for designing better policy making. It could also provide a platform for sharing knowledge and national experiences among member and partner countries on applying behavioural insights in policy making.

33. More fundamentally, the OECD needs to continue strengthening its strategic foresight capabilities to encourage a more open, forward-looking strategic conversation in policy analysis and to be better prepared for interconnected future challenges. In particular, anticipatory knowledge exchange needs to be promoted and facilitated and capabilities in participatory policy simulation/ gaming need to be cultivated in order to identify trade-offs and synergies relevant to whole-of-government policy frameworks. The OECD empirical evidence base should be extended to include and use anticipatory data to clarify and test business-as-usual assumptions underpinning long-term outlooks and to develop effective early warning and surveillance systems.

34. The Organisation also needs to further reinforce horizontal work and interaction across the house. Building on the OECD's multi-disciplinary character, horizontal work will allow a better understanding of the interlinked policy challenges.

35. Finally, it is crucial for the OECD to strengthen its support to international policy co-ordination. The OECD has already deepened its contributions to the G8 and G20 agendas in the last five years, working closely with the troika Presidencies to support their work with evidence-based analysis. This has been instrumental in shaping the policy agenda of the G20 and the agreements that have been reached.

IV. Next Steps and mainstreaming NAEC

36. A final Synthesis will be presented at the MCM 2015, focusing on NAEC projects that will have been delivered by then. The emerging messages, such as the focus on well-being and inclusive growth, should be mainstreamed in the work of Committees. The long-term objective is for the Directorates and

Committees to be inspired by the recommendations emerging from NAEC on how to continue to improve analytical frameworks and policy recommendations and identify important issue areas. This should happen including through the current discussion within OECD Committees of the 2015-2016 Programme of Work and Budget.

37. The NAEC initiative has already had a catalysing effect for Committees to exchange views and better inform themselves on the work done by other Committees. The NAEC seminars have also allowed experts and Ambassadors to discuss important topics that can later inform the work in Committees. That should be maintained and will strengthen the unique comparative advantage of the Organisation in cross-country comparative analysis in a broad range of areas. NAEC is also an impulse to be at the forefront of economic thinking and policy advice, an impulse that nurtures Committees' discussion when preparing for the upcoming Programme of Work and Budget.

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