

Getting the most out of Fintech in Estonia

Category: Estonia,finance,Uncategorized

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Pioneers of the Estonian Fintech need a fair level playing field. Estonia, at the forefront of alternative finance should seize the moment to set framework conditions right.

Estonia is a frontrunner in alternative finance and a host to some of the most innovative Fintech start-ups in the OECD – i.e. start-ups using technology and technology-facilitated new business models in the provision of financial services. Some Fintech companies based or born in Estonia have a world-wide reach. These include one of the largest European peer-to-peer lending platforms for unsecured consumer loans, the first worldwide secondary market for venture capital and a platform that allows individuals and small businesses to transfer money between international accounts at much lower cost than traditional banks.

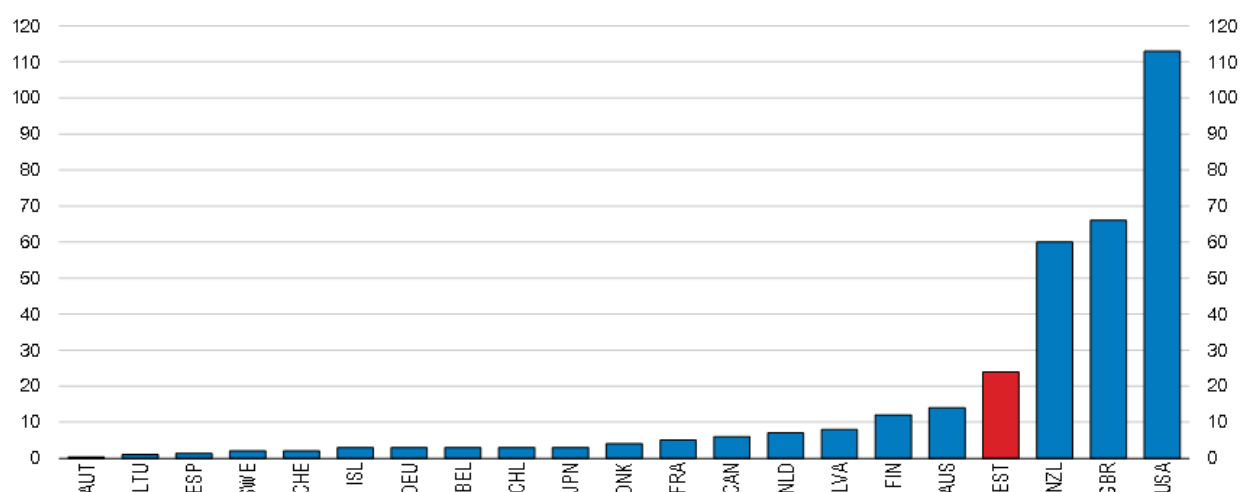
For some, Fintech will revolutionize the traditional banking industry as we know it today, but for the moment, the platforms finance mostly risky projects. At one end of the platform, there are retail investors who choose whom they would like to finance. On the other end, there are SMEs and start-ups that do not go to banks, often because they cannot provide standard guarantees. The platforms generate profits from the origination and servicing fees that they charge to funders and fundraisers. The investors bear all investment risks, providing a natural ‘bail-in’ mechanism. Equity crowdfunding platforms can complement angel- and venture-

capital, by allowing individuals to invest in start-ups and buy shares which are not listed on the regulated stock market.

For the moment the scale of finance channelled through Fintech platforms remains limited (Figure 1) and peer-to-peer lending to SMEs lags far behind consumer lending. The *2017 Economic Survey of Estonia* stresses that a sustainable development of this 'alternative finance' requires a creation of a level playing field between the traditional and the alternative sources of credit in terms of access to information, regulation, and taxation.

Figure 1. Estonia is a frontrunner in alternative finance but amounts are low

Volumes, in euros per capita, 2015



Note: Alternative finance includes peer-to-peer lending, equity crowdfunding, donation and reward crowdfunding, as well as balance sheet lending.

Source: Cambridge Centre for Alternative Finance.

To build confidence in these new financing forms, a necessary condition to their development, consumer protection of Fintech users should be reinforced. The Estonian authorities should introduce licencing and transparency requirements and require the platforms to have resolution plans in place to ensure that repayments continue to be collected in case of bankruptcy. By establishing a well-designed credit information-sharing scheme covering all borrowers (firms and individuals) it could help to move the industry forward, by facilitating the use of big

data and algorithms to screen and monitor borrowers. Finally, the level playing field should be established also when it comes to taxes. Taxation of investment via Fintech platforms should be harmonised with that of bond and equity securities, by allowing investors to deduct their losses from their income tax base.

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Brighter futures or dashed expectations? The global recovery needs to deliver gains for all

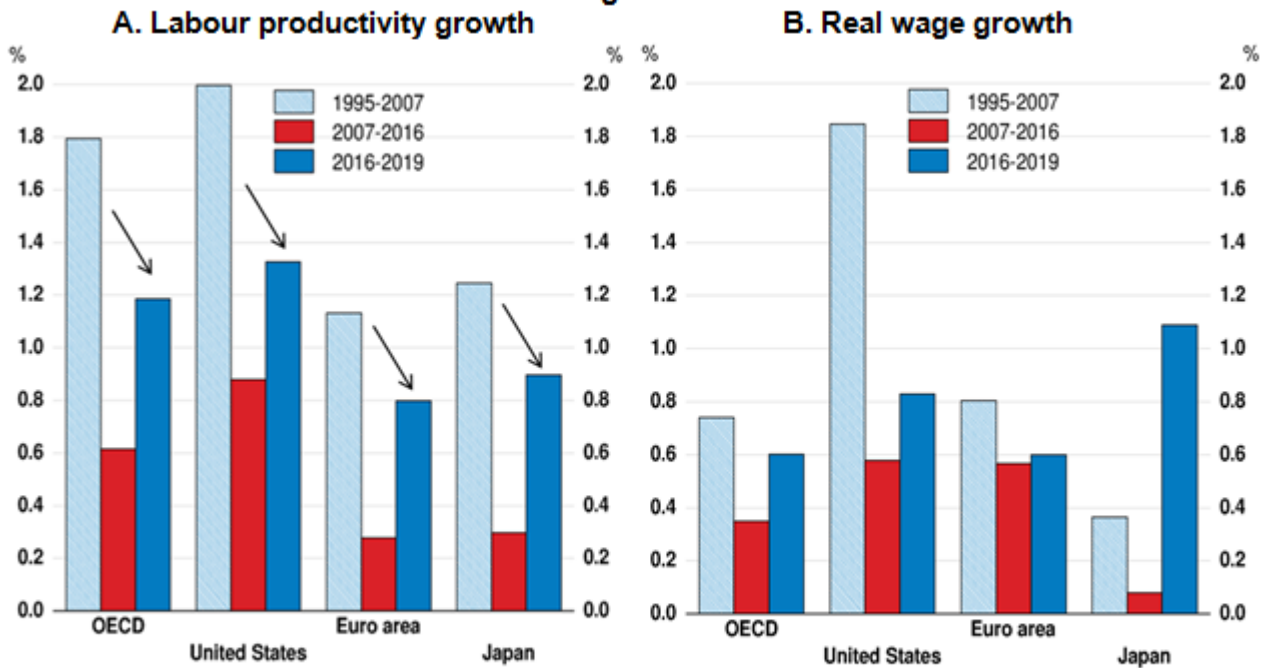
Category: Economic outlook, Productivity, Uncategorized

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By Lukas Lehner and Dorothee Rouzet, OECD Economics Department

Global growth has gained momentum in 2017 and the economic recovery is moving forward, as shown in our latest Economic Outlook. Labour productivity is improving from its decade-long sluggishness. Yet, expected productivity gains still lag far behind pre-crisis norms, and will not be sufficient to set the stage for long-term improvements in living standards (Figure 1, Panel A). Multiple structural obstacles – including a lack of competition and business dynamism and high shares of “zombie” capital – slow down the investment, innovation, and technology diffusion that are crucial for productivity growth.

Figure 1



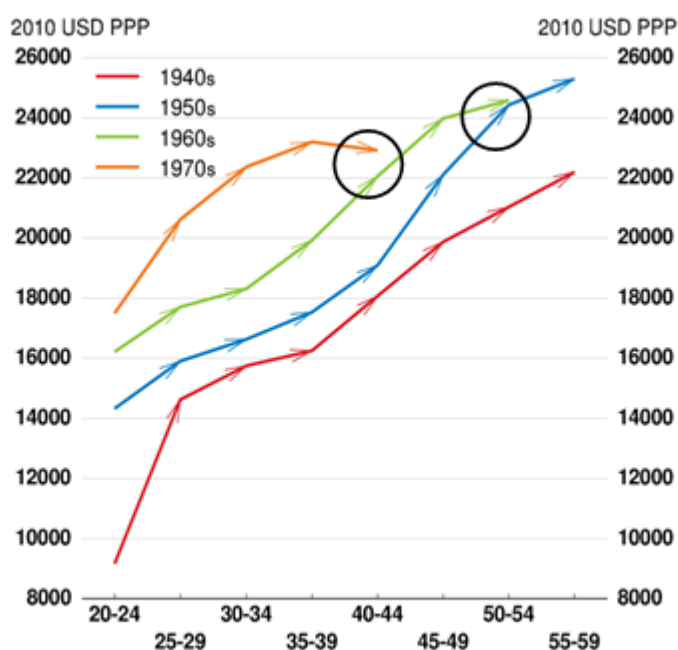
Note: Labour productivity growth is the average annual growth rate of output per person employed. Real wage growth is calculated from nominal wage growth and the GDP deflator. 2017-2019 are projections. Source: OECD Economic Outlook database.

Slow labour productivity growth has been a driver of slow increases in real wages, alongside remaining hidden labour market slack, a rise in non-standard forms of employment and weakened labour market institutions (Figure 1, Panel B). This means that in most advanced economies, incomes are unlikely to rise in line with the pace that households experienced in pre-crisis decades, and that they have come to expect for the future.

Without stronger and more widely shared productivity, wage and income growth, promises to younger generations will not be kept. In the past, each generation used to enjoy rising incomes over their working lives and higher living standards than their elders. These trends have slowed or even reversed in the last decade for generations currently in their prime working age (Figure 2). Real incomes have decreased for people born in the 1970s, feeding into public dissatisfaction. Ensuring that this lost decade does not become a “lost generation” is a call for deeper policy changes.

Figure 2: Income gains across generations have slowed

Real disposable income by age and birth decade, OECD



Note. Data cover 24 OECD countries. The series shown are derived for each cohort from a specification controlling for country and age fixed effects.

Source: [Preventing Ageing Unequally](#), based on data from the Luxembourg Income Study.

To raise prospects for better living standards for their populations, policymakers need to take action to catalyse more robust investment and productivity gains towards higher wages and incomes for all. Reform packages should focus on promoting competition and trade, improving active labour market policies and social protection, and developing human capital to seize the opportunities of the future. The short-term momentum provides a window for bold action that could and should promote stronger and more inclusive growth.

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OECD (2017), *OECD Economic Outlook, Volume 2017 Issue 2*, OECD Publishing, Paris.

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<http://dx.doi.org/10.1787/9789264279087-en>

Investment, an engine of global growth that has yet to fire up

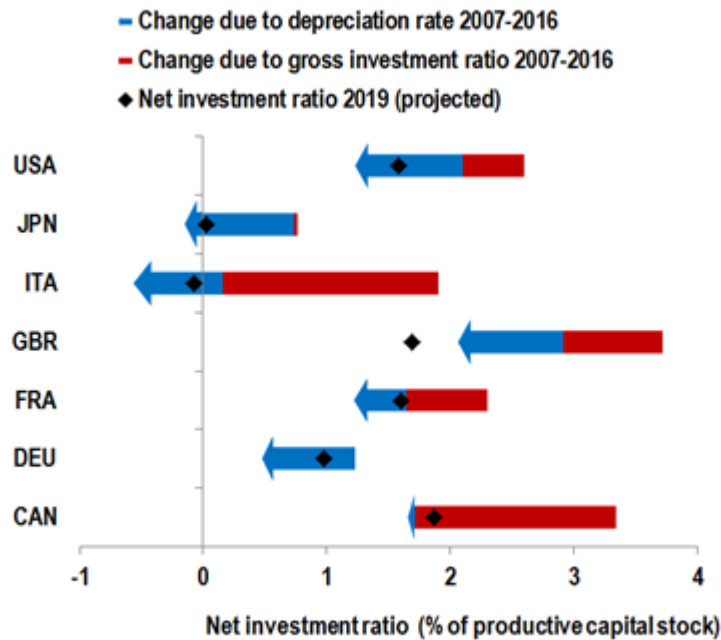
Category: Economic outlook, investment, Uncategorized

written by oecdecoscope | December 5, 2017

By Théodore Renault and Dorothee Rouzet, OECD Economics Department

Global growth has strengthened, but policymakers face the challenge of lifting their economies' long-term potential to ensure it remains robust and more inclusive. Private sector investment has slowed substantially in the past decade. Even though they have started to recover in most advanced economies, net investment rates remain well below pre-crisis levels and are projected to rise only modestly for the next two years (**Figure 1**) – see our latest Economic Outlook. The capital stock has been eroded by the double whammy of declining gross investment rates and faster depreciation – in part due to the shorter lifespan of technology investments. As a result, stronger investment than in the past is needed to maintain, grow or upgrade the capital stock, and to turn the opportunities offered by new technologies into sustained productivity growth.

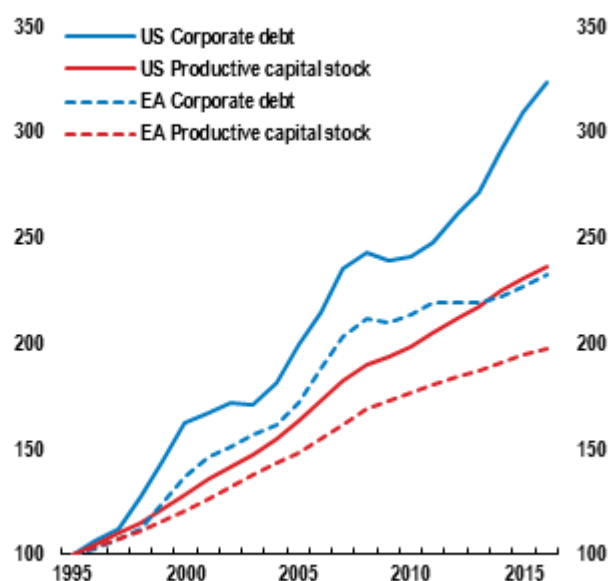
Figure 1 – Net investment ratios have fallen



Note: The net investment ratio is defined as the gross investment ratio minus the depreciation rate in % of the productive capital stock. It includes business plus government investment.
Source: OECD Economic Outlook database; and OECD calculations.

Investment rates have declined even as corporate debt has soared in the post-crisis period, as highlighted in the OECD Economic Outlook special chapter on “Resilience in a Time of High Debt”. This raises questions about what the funds are used for. If borrowing is well used, rising corporate indebtedness can contribute to economic growth by raising productive capacity or improving productivity. This has by and large not been the case: corporate debt has for long risen faster than the productive capital stock in major economies, such as the United States or the euro area (**Figure 2**). A number of studies suggest that a substantial share of new debt has been used to return funds to shareholders through share buybacks and dividends, rather than financing investment (OECD, 2016). The gap between the cost of equity and debt may have also been a motivation to shift towards debt financing.

Figure 2 – Disconnect between debt and productive capital



Note: Based on nominal series. Excludes financial corporations.

Source: OECD National Accounts; OECD Economic Outlook database; and OECD calculations.

The divergence between investment and corporate debt raises concerns that too much debt may signal inefficient capital allocation. High levels of debt can hamper the ability of corporations to undertake new borrowing to finance productive investment. Over-indebted firms tend to lose dynamism, often even failing to keep up with the required investment to remain competitive, and thus can become “zombie” firms, not only impairing their own prospects but also holding back the performance of competing firms (Adalet McGowan et al., 2017).

Broad structural policy packages are needed to catalyse business investment towards stronger long-term growth prospects. Policy action to make product markets more competitive would raise the prospective rate of return on new investments and encourage innovation, leading to higher productivity growth and ultimately supporting wage and income growth. Reducing the tax bias towards debt and improving the design of insolvency regimes would help the financial system to be more resilient to shocks, thereby minimising the risks of sub-par growth in the medium term.

References

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Publishing, Paris.

OECD Economic Resilience website

Adalet McGowan, M., D. Andrews and V. Millot (2017), "Insolvency Regimes, Technology Diffusion and Productivity Growth: Evidence from Firms in OECD Countries", *OECD Economics Department Working Papers*, No. 1425, OECD Publishing, Paris. <http://dx.doi.org/10.1787/36600267-en>

Caldera Sánchez, A., et al. (2017), "Strengthening Economic Resilience: Insights from the Post-1970 Record of Severe Recessions and Financial Crisis", *OECD Economic Policy Papers*, No. 20, OECD Publishing, Paris. <http://dx.doi.org/10.1787/6b748a4b-en>

OECD (2016), *OECD Business and Finance Outlook 2016*, OECD Publishing, Paris. <http://dx.doi.org/10.1787/9789264257573-en>

The Policy Challenge: Catalyse the private sector for stronger and more inclusive growth

Category: Economic outlook, Uncategorized

written by oecdecoscope | December 5, 2017

by Catherine L. Mann, OECD Chief Economist and Head of the Economics Department,

Global economic growth is strengthening, with incoming data

surprising on the upside. We project global GDP growth to be between 3 $\frac{1}{2}$ and 3 $\frac{3}{4}$ per cent through the projection horizon, closer to long-run averages. Will this synchronised momentum finally propel the global economy to gather enough speed to raise productivity, real wages, and living standards for all?

OECD Economic Outlook projections

Real GDP growth

Year-on-year, %

Arrows indicate the change in growth rate from previous year

	2016	2017 November projections	2018 November projections	2019 November projections
World	3.1	3.6	3.7	3.6
United States	1.5	2.2	2.5	2.1
Euro area ¹	1.8	2.4	2.1	1.9
Germany	1.9	2.5	2.3	1.9
France	1.1	1.8	1.8	1.7
Italy	1.1	1.6	1.5	1.3
Japan	1.0	1.5	1.2	1.0
Canada	1.5	3.0	2.1	1.9
United Kingdom	1.8	1.5	1.2	1.1
China	6.7	6.8	6.6	6.4
India ²	7.1	6.7	7.0	7.4
Brazil	-3.6	0.7	1.9	2.3
Russia	-0.2	1.9	1.9	1.5

More robust and higher quality private sector investment, including in intangibles and skills, is key for long-term productivity and real wage growth. There are positive signs: surveys indicate that businesses intend to invest, particularly in technology-embodied capital; and the now synchronous global upturn signals demand for investment, particularly given the erosion of the capital stock. But, projected investment rates remain too low to sustain the acceleration of activity. As a result, our projection for global GDP for 2019 shows a tempering of growth rather than continued strengthening.

A myriad of obstacles (different across countries) stand in the way of the more robust investment crucial for productivity growth to meet the public's expectations for higher living

standards, and to fulfil the longer-term commitments of governments to provide solid career paths for the young and adequate pensions for the old. For example, services restrictions create hurdles to invest, particularly for smaller firms; judicial delays hinder the clean-up of balance sheets and capture resources in poorly performing firms; housing policies can make it difficult to hire workers with the right skills, undermining investment by both workers and firms.

Some people think that the per capita income growth enjoyed in previous decades is out of reach, and that those expectations are unrealistic or even inappropriate, given demographic and environmental considerations. On the former, OECD research shows that changes in pension policies to promote longer working careers and increased participation of women can offset much of the demographic drag on potential output. On the latter, the OECD report "Investing in Climate, Investing in Growth" shows a path to better well-being consistent with climate change commitments. More robust productivity growth is needed to raise wage prospects in advanced economies and higher investment—in social, public, human, and physical capital (with different combinations for different countries)—is needed for emerging economies to sustain catch-up in living standards.

Financial markets provide additional signals that real investment has yet to fully fire, and that incentives are misaligned. When firms invest in financial assets rather than in real capital, asset prices rise relative to long-term growth prospects. Evidence continues to build that financial asset prices are inconsistent with expectations for future growth and the policy stance, exacerbating the risks of financial corrections and growth downdrafts. Vulnerabilities appear through a number of channels: volatility measures are low even as the probability of sharp corrections is high, equity prices are high relative to expected growth rates and

discount rates, credit spreads are narrow relative to risks, bond yields are low relative to probable outcomes of fiscal and monetary policies, and historically-high duration exposes bond holders to interest rate normalisation. Current global growth rates, and fiscal and monetary space are too limited to weather a financial downdraft. This puts an even greater premium on structural policy efforts.

Policymakers need to trigger deeper changes to their policies to catalyse investment, productivity, and real wage growth and make growth more inclusive. The OECD's *Going for Growth* exercise documents that many countries have focussed and made progress on policies that enhance labour market fluidity and participation by redesigning benefits and "making work pay", and by improving childcare so as to enhance labour force inclusion of women. These reforms have paid off with higher employment rates, particularly among groups that typically have been more weakly attached to the labour market. However, for these reforms to be reflected in high productivity and real wage growth, opportunities for right-skilling need to improve and productivity gains need to diffuse from the frontier to all firms. Further, competition in markets enhances competition for workers, making for better skill matching and higher real wages. Policymakers' efforts on product market reforms have been less ambitious, in particular on anti-trust/competition policy action and on trade and investment policies; indeed, threats to roll back openness permeate the policy landscape. Although progress has been made on financial market repair, zombie firms still capture too much labour and capital, taking a toll on business dynamism, productivity and real wage growth.

The financial crisis prompted structural reform and new regulation of parts of the financial system, but private sector debt remains high. The past decade has seen a growing reliance by firms on bond financing at attractive rates, with deteriorating credit quality and use of international

issuance, as set out in Chapter 2 of this *Economic Outlook* on “Resilience in a Time of High Debt”. While credit is needed to support economic activity and innovation, it can increase risks, lower growth and raise inequality. An integrated policy approach is needed to enhance the financial resilience of economies to shocks and to minimise the risks of sub-par growth in the medium term. Financial regulation should not focus only on risk, but also on growth.

Policy fatigue and sluggish growth in the past decade have curbed reform ambitions. And some might suggest that the global upturn means that no more policy effort is needed. In fact, the rapid pace of technological change – digitalisation, robotics, artificial intelligence, cloud computing – demands deeper and more extensive reforms, not complacency. Attention to the local challenges of global and technological changes has to ensure that opportunities will be shared. Those countries that step up policy efforts will create a better environment for their firms and public. With the global upturn putting wind under the wings of policy, now is the time to redouble the effort.



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OECD (2017), *OECD Economic Outlook, Volume 2017 Issue 2*, OECD Publishing, Paris.

Should we worry about high household and corporate debt?

Category: Economic outlook, Uncategorized

written by oecdecoscope | December 5, 2017

By Catherine L. Mann, OECD Chief Economist and Head of the Economics Department, and Filippo Gori, Economist, Macroeconomic Policy Division, OECD Economics Department

Household and corporate debt in many advanced and emerging market economies is high in the wake of the financial crisis and following a decade of low global interest rates. Should we be worried by these developments?

The forthcoming OECD Economic Outlook special chapter on “Resilience in a Time of High Debt” looks at how high debt-to-GDP ratios can increase vulnerability in the short run. While higher indebtedness does not necessarily imply that problems are just around the corner, it does increase vulnerability to shocks and the on-going deterioration of credit quality, changes in the structure of corporate financing, increased forex risk and buoyant asset price dynamics raise concerns.

The impact of high debt on the sustainability of growth in the medium term is often overlooked. While finance is needed to support economic activity and innovation, it can increase risks, lower growth, and raise inequality in the longer term.

The assessment highlights some key features of the post-crisis expansion of private sector debt for risk:

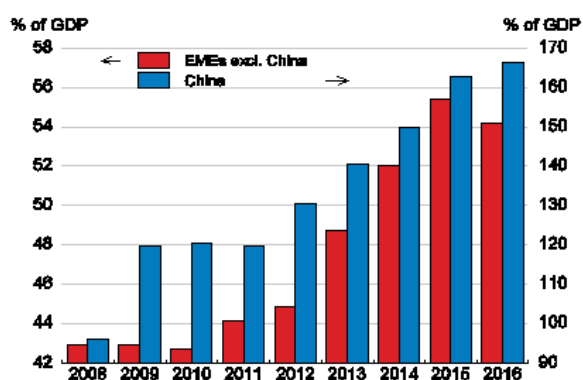
- There has been a significant shift in corporate finance towards bonds and a substantial decrease in credit quality, including a surge in issuance of non-investment

grade bonds, weaker covenants and low bond ratings (Çelik et al., 2015). While deepening of bond markets can be positive, this points to higher credit risk and rollover risk.

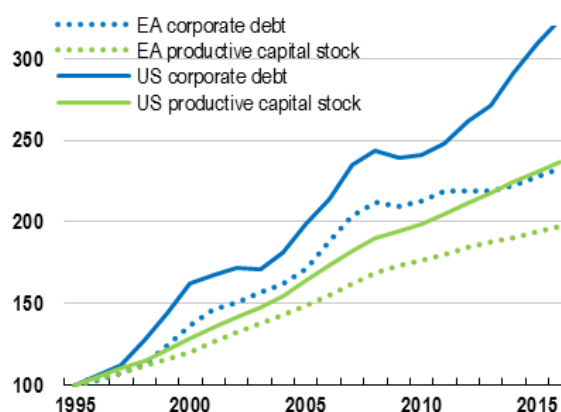
- There has been a substantial expansion of international bond markets and foreign-currency borrowing. This helps to share risk and improves access for countries with limited domestic financial markets. However, it increases the risk of international spillovers. The rise in foreign-currency denominated bond issuance – much of which via foreign subsidiaries – exposes borrowers more to exchange rate risk.
- On the asset side, more credit risk now lies with bond holders. They also face interest rate risks and the low level of coupon rates and rising maturity means that there are now record levels of duration risk, implying that bond values are very sensitive interest rate changes.
- Household debt ratios are closely linked to house prices and the credit cycle in mortgages: some OECD countries that have experienced the strongest increases in household debt since the crisis have also the steepest rise in house prices. The housing cycle is an important risk factor as excessive house price developments are predictive signals of future recessions (Caldera Sánchez, et al., 2017). A number of advanced economies have experienced worrying increases in house prices in recent years, while household debt as a share of income in some Asian countries is reaching levels typically seen in advanced economies.

Figure 1

A. Corporates in EMEs accumulated significant debt



B. The expansion of corporate debt has far outpaced investment



The efficiency of capital allocation is critical to ensure that corporate debt is sustainable and does not weigh on medium-term growth. However, weak investment since the crisis raises concerns that debt is not being used to finance long-term productive capacity. Over-indebted firms tend to lose business dynamism, failing to keep up with the required investment to remain competitive, and become “zombie” firms, not only impairing their own prospects but also reducing performance by competing firms (Adalet McGowan et al., 2017).

An integrated policy approach is needed to enhance the financial resilience of economies to shocks and minimise the risks of sub-par growth in the medium term, balancing risks and the growth impacts. This needs to draw on a familiar menu of policy tools including an appropriate balance of macroeconomic policies and use of macroprudential instruments.

However, the approach needs to go beyond cyclical fixes and address underlying structural features of the economy and policy that can lead to too much corporate and household debt. For corporate finance, a sounder and healthier financial system would reduce the tax bias towards debt, deepen equity markets and improve the design of insolvency regimes. For housing markets, removing tax and other subsidies for housing and making housing supply more fluid would enhance the resilience of household debt.



Download Presentation

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Adalet McGowan, M., D. Andrews and V. Millot (2017a), "Insolvency regimes, zombie firms and capital reallocation", *OECD Economics Department Working Papers*, No. 1399, OECD Publishing, Paris. DOI: <http://dx.doi.org/10.1787/5a16beda-en>

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A Response to Queen Elizabeth's Question on the Global Financial Crisis

Category: Uncategorized

written by oecdecoscope | December 5, 2017

Dave Turner, Head of the Macroeconomic Analysis Division, OECD Economics Department

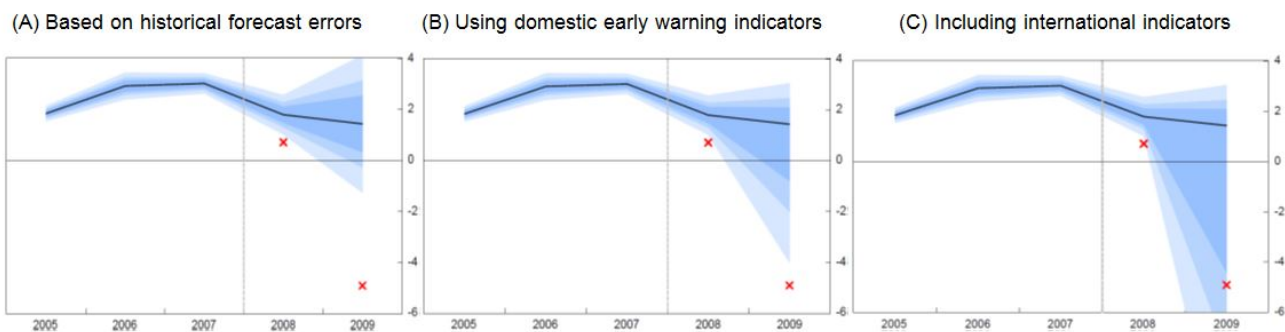
"Why did no one see it coming?" was the disarmingly blunt question asked by Queen Elizabeth in the aftermath of the global financial crisis. A number of economists (some with greater reliance on hindsight than others) claimed that there had been "worrying developments" in finance and the global economy for a long time prior to the crisis. Nevertheless, in the eyes of many, the economics profession was damned by the failure of mainstream forecasters, including the OECD and IMF, to predict the crisis. This failure should not, however, have been surprising; forecasters always had a poor track record in predicting economic downturns, particularly because getting the timing right is so difficult [1]. However, they could do a much better job in conveying what those "worrying developments" mean in terms of risks surrounding their forecasts.

Recent OECD research has found that rapid growth in housing-market and credit-related variables can be useful as early warning indicators of severe downturns [2]. These indicators are also correlated with large forecast errors of GDP growth related to (failures to predict) downturns and so can be used to assess the uncertainty surrounding a forecast, distinguishing between a "safe" regime, where forecast errors

are expected to be symmetrical, and a “downturn-risk” regime where errors are more likely skewed to the downside [3]. These distributions can then be used to design a fan chart around the central forecast to provide a visual representation of the risks and uncertainties.

What would such fan charts have looked like just prior to the crisis? As an illustration, a series of fan charts are computed around OECD forecasts of GDP growth for the United Kingdom, one of the major economies most severely affected by the crisis. Each fan chart is represented by a series of successively lighter shaded prediction intervals, so that the probability that the outcome lies within successive intervals is assessed at 50%, 70% and 90%. A first fan chart is constructed as a ‘straw man’, being based on historical forecast errors assuming symmetry in the underlying distribution of errors and ignoring the early warning indicators. On this basis, the outcome for 2009 GDP growth at almost -5% is well outside even a 90% prediction interval on the fan chart (panel A). An alternative asymmetric fan chart (panel B), which takes into account a domestic early warning alarm for rapid credit growth, implies the outcome is closer to, but still outside, the lower 90% prediction limit of about -4%. Thus, perhaps unsurprisingly, to encompass the extreme negative outcome, it is essential to take account of the international dimension of the crisis. Indeed, in the first half of 2008 early warning alarms were flashing for all G7 countries except Japan and Germany. A third fan chart, whereby the skew is calculated on the basis of both domestic early warning alarms and alarms in other major OECD countries, encapsulates the outcome, which falls within the 50-70% prediction interval (panel C). Moreover, similar fan charts computed for other G7 countries confirm that taking into account the early warning alarms, ensures that fan charts are much better at encapsulating the crisis outcome.

Alternative fan charts for the May 2008 *Economic Outlook* growth forecast for the United Kingdom



Note: Shaded blue areas show successively the 50%, 70% and 90% prediction intervals. The solid black line is the outturn up to 2007 and the projection for 2008 and 2009, as reported in the May 2008 *Economic Outlook*. The red crosses show the outturn according to the *Economic Outlook* published in the year following the first outturn data. The prediction intervals around the historical growth path reflect the extent to which historical estimates of GDP growth are subsequently revised.

Source: Turner (2017).

Despite ongoing efforts to improve forecasting models [4], it is likely that forecasters will continue to struggle to predict the timing of future downturns. However, by monitoring credit and housing-market developments and other early warning indicators, they could do a better job of both assessing and presenting the risks surrounding their forecasts. Indeed, perhaps the best possible outcome would be if downturn warnings proved to be false alarms because policy-makers heeded the warnings and took appropriate early action.

Further reading

[1] The following studies provide evidence of the poor performance of all forecasters in predicting downturns:

Abreu, I. (2011), "International Organisations' vs Private Analysts' Forecasts: An Evaluation", Banco de Portugal Working Papers, 20/2011, July.

Fildes, R. and Steckler, (2002), "The state of macroeconomic forecasting", *Journal of Macroeconomics*, 24(2), pp. 435-468.

Loungani, P. (2001), "How accurate are private sector forecasts? Cross-country evidence from consensus forecasts of output growth", *International Journal of Forecasting*, 17(3), pp. 410-432.

[2] This paper describes recent OECD work to evaluate the

usefulness of early warning indicators of downturns in OECD economies:

Hermansen, M. and O. Röhn (2016), "Economic Resilience: The Usefulness of Early Warning Indicators in OECD Countries", *OECD Journal: Economic Studies*, No. 1, Vol. 2016, Issue, 1, pp. 9-35. OECD Publishing, Paris.

[3] The following paper provides further discussion of the rationale for, and details underlying, the design of the fan charts referred to in this post:

Turner, D. (2017), "Designing Fan Charts for GDP Growth Forecasts to Better Reflect Downturn Risks", *OECD Economics Department Working Papers*, No. 1428, OECD Publishing, Paris.

[4] This study draws lessons from the financial crisis which have been, or are in the process of being, reflected in OECD forecasts:

Pain, N. and C. Lewis (2014), "Lessons Learned from OECD Forecasts During and after the Financial Crisis", *OECD Journal: Economic Studies*, No. 5, Vol. 2104, Issue, 1, pp. 9-39, OECD Publishing, Paris.

This paper describes the current process of how models are combined with judgement in determining OECD forecasts:

Turner, D. (2016), "The Use of Models in Producing OECD Macroeconomic Forecasts", *OECD Economics Department Working Papers*, No. 1336, OECD Publishing, Paris.

Maintaining Switzerland's

enviable living standards into the future

Category: Switzerland,Uncategorized

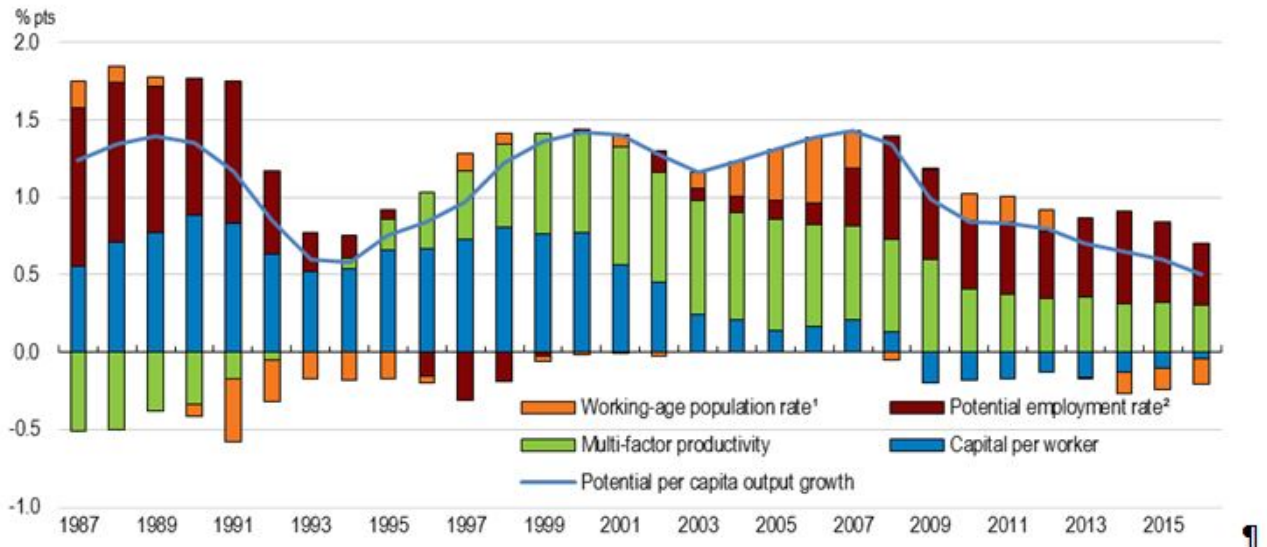
written by oecdecoscope | December 5, 2017

by Christine Lewis, Switzerland Desk, Economics Department

Switzerland's high living standards and quality of life are renowned. It has the third-highest level of GDP per capita in the OECD. Likewise, survey data show Swiss have the OECD's second-highest rate of life satisfaction. Unemployment is low, including for young people. And income inequality (after taxes and transfers) is around the OECD average.

But Switzerland cannot take these enviable outcomes for granted. Indeed, trends are slowly eroding this favourable position. The rate of potential growth in per capita income has slowed to just 0.5%. While Swiss GDP per hour worked was one of the highest 40 years ago, growth has stalled due to slow increases in investment and in multi-factor productivity (Figure). Demographics are also playing a role by reducing the share of the population that is of working-age. And immigration, which had helped offset this effect and ease skills shortages, is slowing too. Ageing will add to the fiscal burden: spending on pensions, health and long-term care is projected to increase by 3.5 percentage points of GDP in the next three decades, which risks crowding out other spending and pushing up debt (Federal Department of Finance, 2016).

Decomposition of the slowing-in-potential-per-capita-income-growth ¶



Source: OECD, OECD Economic Outlook 102 database, preliminary version. ¶

The OECD's latest *Economic Survey of Switzerland* highlights several win-win policies that can counter these trends by raising labour supply and skills while contributing to the inclusiveness of growth (OECD, 2017):

- **Increasing affordability of childcare** would allow mothers to increase their hours if they so choose and help them to maintain a career path. By better allocating women's skills it would also raise productivity. Likewise, the disincentives in the tax system to take on more hours should be removed by shifting to taxation of individual incomes or undertaking some equivalent measure.
- **Participation in life-long learning should be promoted** more actively to ensure that workers continue to maintain and adapt their skills as the economy changes at an ever-faster pace. Swiss workers have high levels of participation in continuing education and training overall, but it is not broad-based with a heavy concentration on those with strong educational attainment. To ensure that other workers are not left behind, subsidies should be offered to workers from groups with low participation rates.

- **Incentivising and assisting workers to delay retirement** will help combat the effects of ageing on growth as well as alleviating fiscal pressures. Pension reform is urgently needed to ensure the financial sustainability of the system; reform should raise retirement ages and index them to life expectancy and also include stronger incentives to work longer. Promoting take-up of preventative health programmes, as well as career planning and tailored job-search assistance would lengthen healthy working lives.

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Federal Department of Finance (2016), *Report on the Long-term Sustainability of Public Finances in Switzerland*, Federal Department of Finance, Bern.

OECD (2017), *OECD Economic Survey of Switzerland*, OECD Publishing, Paris.

Where to get the best bang for the buck in the United Kingdom? Industrial strategy, investment and lagging regions

Category: Productivity,Uncategorized,United Kingdom

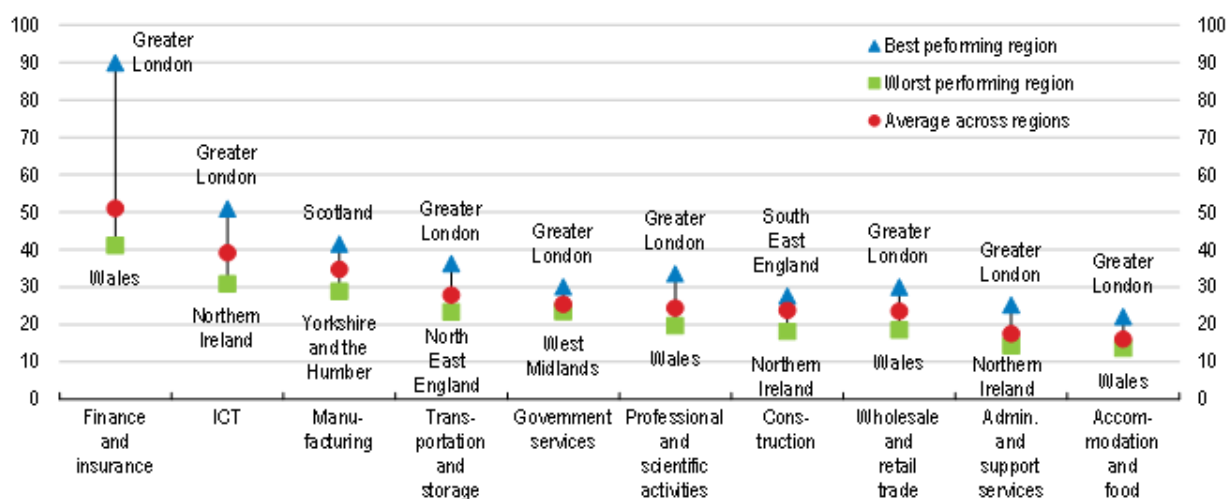
written by oecdecoscope | December 5, 2017

by Rafal Kierzenkowski, Head of UK Desk, Peter Gal, Economist,

Productivity Workstream, and Gabor Fulop, Analyst at the UK Desk, OECD Economics Department

The United Kingdom has large regional disparities in productivity which contribute to differences in living standards across the country, while its less productive regions also hold back overall economic performance (OECD, 2017). High levels of productivity in London are widespread across nearly all sectors, especially among knowledge intensive services such as finance and insurance and information and communication technologies (ICT) (Figure 1).

Figure 1. Productivity differences across regions tend to be the largest for knowledge intensive services
Labour productivity measured by gross value added per hour, in GBP, 2015¹



1. Sectors are ranked in descending order of the average level of labour productivity. The chart uses the TL2 definition of regions which yields 12 regions for the UK.

Source: ONS (2017), "Labour productivity: April to June 2017", Office for National Statistics, October.

To narrow these gaps in productivity, the government is preparing a modern industrial strategy to boost labour productivity across the whole country (HM Government, 2017). The strategy has a broad sectoral focus, going beyond manufacturing industries, and aims to improve the local and regional business environment so that both successful businesses and potential new ones can thrive. Devising the optimal strategy raises the question of the optimal allocation of scarce resources in meeting these targets. Our recent study (Kierzenkowski et al. 2017) aims to contribute to the policy choices linked to the strategy and finds that the catch up of

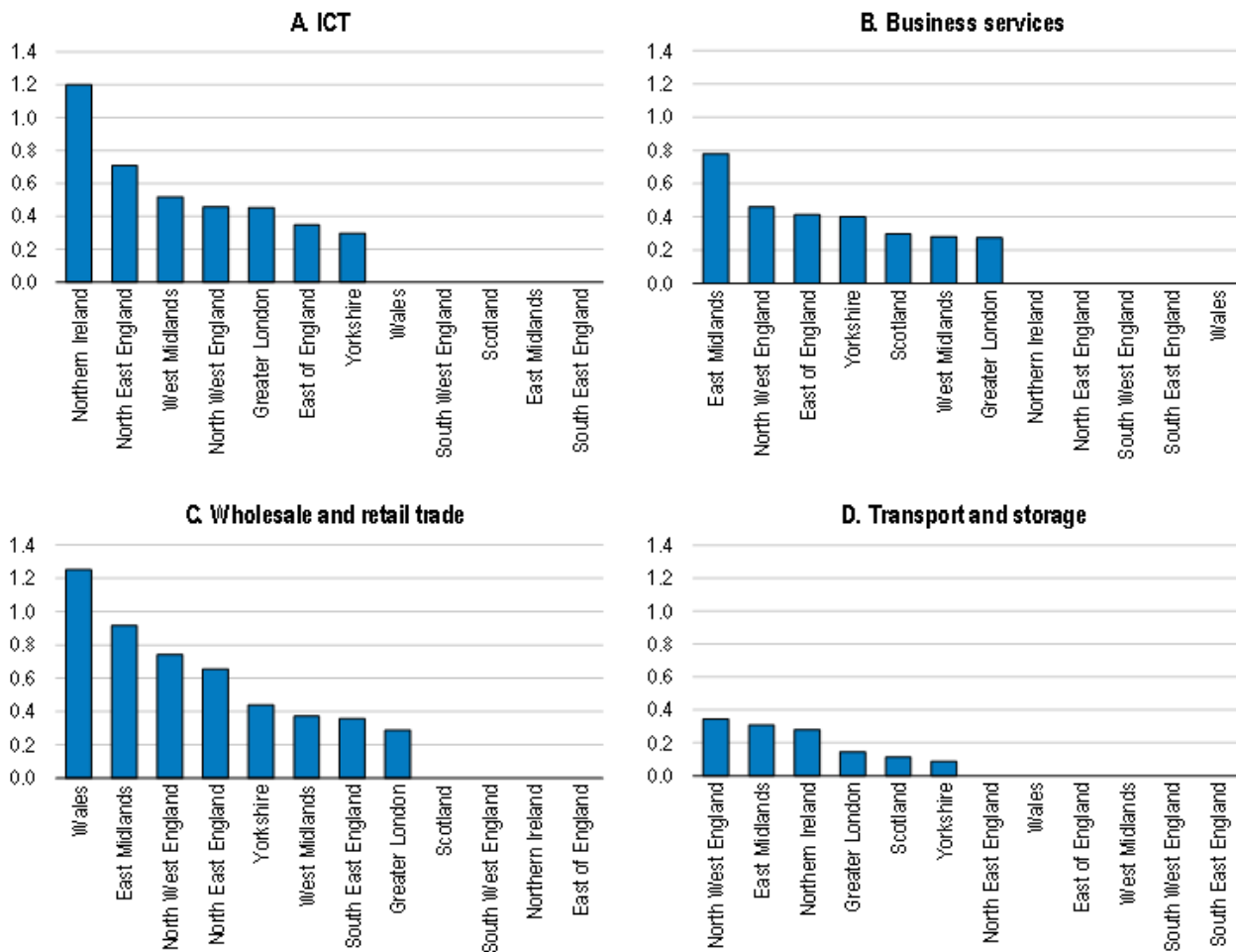
firms with the national best performers in services sectors can give large productivity benefits for most lagging regions, in particular knowledge intensive services such as ICT and business services, but also wholesale and retail trade.

Our study also identifies the sectoral strengths of each region and shows that while each region has productivity leaders, the concentration of such firms is the highest in the south of England, surrounding London, especially in ICT and business services. In turn, differences in the representation of the most productive firms in regions are strongly related to differences in regional productivity.

Given low levels of investments in the UK economy and the role new capital goods can play in adopting the latest technologies, our study quantifies the amount of regional and sectoral productivity increases that can be achieved by raising capital intensity. The greatest potential to increase productivity in most regions is by raising the capital intensity of services sectors, which are more responsive to capital intensity increases, in particular in many lagging regions (e.g. northern parts of England, Northern Ireland) (Figure 2).

Figure 2. Sector-region labour productivity impacts in services sectors

Impact of 1% increase in capital intensity on labour productivity, per cent¹



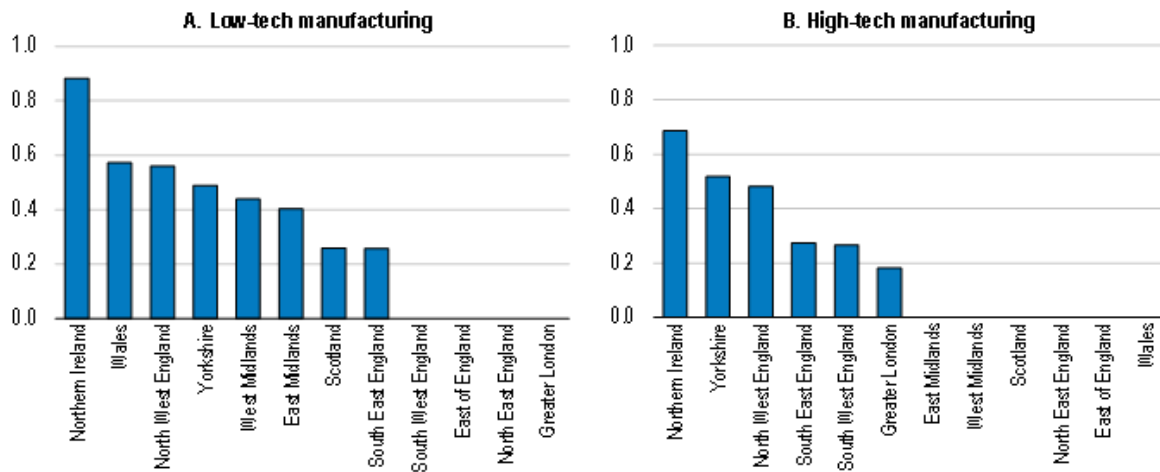
1. The values are obtained using equation (4). The impacts are measured in percentages (approximated by changes in logarithms) and are ranked from the largest to the smallest impact. Only those sectors are shown where the estimated impacts are correctly signed and significant, and which represent a significant share of total regional employment. Yorkshire refers to Yorkshire and The Humber.

Source: Calculations based on the Orbis firm-level data by Bureau van Dijk.

A strong focus on services would also be consistent with the position of UK sectors in global value chains (Criscuolo and Timmis, 2017). However, more granular analysis regarding the type of investment used to raise capital intensity suggests that R&D spending could be effective in raising the productivity of the manufacturing sector in some regions (Figure 3).

Figure 3. Sector-region productivity impacts of higher R&D capital intensity in the manufacturing sector

Impact of 1% increase in R&D on labour productivity, per cent1



1. The values are obtained using equation (4). The impacts are measured in percentages (approximated by changes in logarithms) and are ranked from the largest to the smallest impact. Only those sectors are shown where the estimated impacts are correctly signed and significant and which represent a significant share of total regional employment. Yorkshire refers to Yorkshire and The Humber. R&D: research and development.

Source: Calculations based on the Orbis firm-level data by Bureau van Dijk and ONS (2016), "Annual gross fixed capital formation by Industry and Asset", Dataset, Office for National Statistics, September.

Of course, there are several complementary factors to capital intensity that are likely to play a key role in boosting productivity of lagging regions but which can be harder to take into account in a systematic, quantitative manner. Key among them is the availability of skills and their matching to jobs, especially given that regional job-to-job mobility is likely to be held back by a low price elasticity of housing supply. In addition, the ecosystem of companies including the role of infrastructure as well as the density of consumers and suppliers are also likely to play a crucial role.

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Reducing inequality to raise incomes and expand well-being for all Colombians

Category: Colombia, Inequality, Uncategorized

written by oecdecoscope | December 5, 2017

By Christine de La Maisonneuve, Economist on the Colombia desk, Economics Department

Growth has become more inclusive in recent years. Living standards have improved and poverty has declined (Figure 1). However, the gap between rich and poor remains among the highest in Latin America. The peace agreement will boost economic growth, but to share it fairly Colombia must also achieve better educational outcomes and bring more people into the more productive formal economy.

Figure 1. Living standards have improved

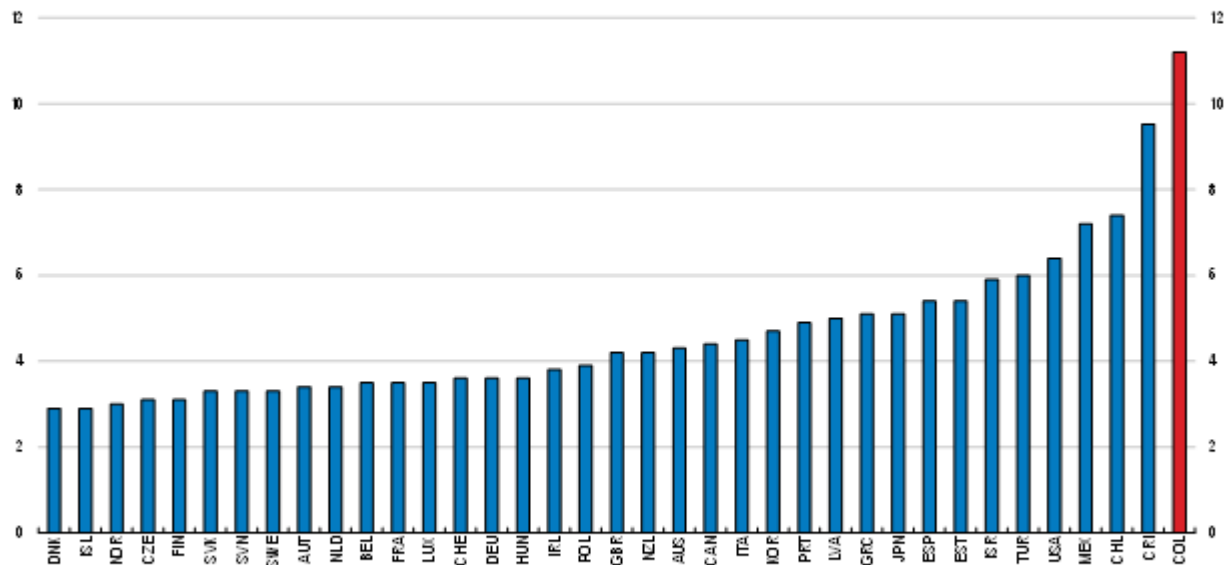


Source: World Bank, World Development Indicators database.

One of the key challenges facing Colombia is the **creation of better quality jobs**. Although the economy has grown strongly for some time, income and regional inequalities remain important (Figure 2). Informality is high in the labour market and keeps more than half of the workers in marginal, insecure, low paying jobs without access to social benefits. The earnings gap between formal and informal workers is significant. The Colombian authorities have promoted the formalisation of labour over the past decade. In particular, the tax reform of 2012, which reduced non-wage labour costs by eliminating some labour taxes led to a significant increase in formal job creation. To reduce informality more, focus should be placed on further reducing the non-wage labour burden on wages; and simplifying the complex procedures for the registration of companies and the affiliation of workers to social security.

Figure 2. Income inequality remains high

P90/P10 ratio, 2014 or latest available year



Note: The P90/P10 ratio is the ratio of income of the 10% of people with highest income to that of the poorest 10%.

Source: OECD (2016), OECD Employment Outlook.

Despite significant progress in reducing gender inequalities in education and providing more opportunities for women to develop their careers, gender employment and wage gaps still remain; in particular for low-income, low-educated and rural women. Greater and more affordable child, elderly and disability care could open the job market to more women. Colombia should also increase investment in active labour-market policies such as training to reduce the gender gap in labour market participation.

A key ingredient to enhance inclusive growth is to **raise the quality of education** at every level, starting in pre-primary. The performance of the education system has improved in recent years as shown by the new PISA results (an internationally standardised test for 15 year olds). Colombia has made impressive gains in expanding access to education but the quality is still highly unequal and too many students leave education without the basic skills they need to succeed in life and work. Raising the quality of teaching will be vital to improve student learning.

The social system could also redistribute more. Public social spending has increased remarkably since the 1990s due to commitments in the Constitution and greater decentralisation of public expenditure. Nonetheless, social spending remain low relative to GDP and compared to the OECD average, are not always well targeted and have a very limited redistributive impact. The pension system leaves many elderly in poverty. The high level of informality and stringent eligibility requirements generate a low coverage especially for women and lower-skill workers. The government provides old-age income support for the poor through *Colombia Mayor* but coverage and benefits are too low. A reform of the pension system is needed to extend coverage and increase the elderly well-being.

Health coverage is almost universal. Out-of-pocket payments have substantially declined and almost all citizens have access to an equal basket of services whether they are in formal or informal employment. However, access to quality services remains difficult for the poor and in rural areas. Given the remoteness of many areas in Colombia, poor availability of health centres and health professionals, deficient transportation and high transportation costs make it challenging to ensure an adequate standard of care quality in all regions. Consequently, health outcomes differ across regions. A different delivery and financing model is needed in rural and remote areas to achieve levels of access and quality that are comparable to advanced urban settings. This will require forging a sustained service network between rural and urban health care providers.

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The Slovenian economy is bouncing back

Category: Slovenia,Uncategorized

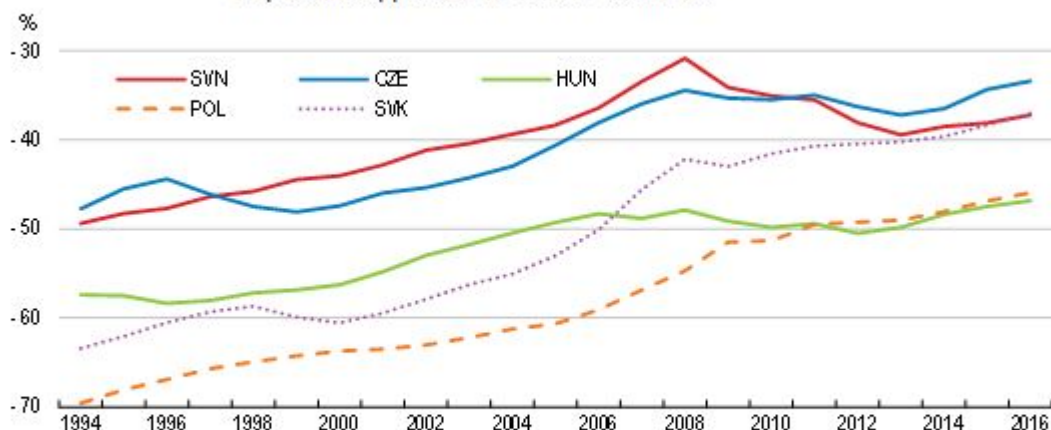
written by oecdecoscope | December 5, 2017

by Rory O'Farrell, Slovenia Desk, OECD Economics Department

Slovenia would do well if its economy performed as well as its ski-jumpers. In 2015, Slovenian Peter Prevc became the first ski-jumper in history to jump 250 metres. As impressive has been his ability to land successfully, being among the few jumpers to receive a perfect 20 points for style. While the Slovenian economy has been successful in bounding forward, it has taken hard falls in the past, and a lack of resilience means it has taken a long time to recover.

Prior to the international crisis, the bounding Slovenian economy converged with advanced OECD economies, before suffering a double hard landing with the onset of the international financial crisis and a subsequent domestic banking crisis. However, thanks to recent structural reforms, business restructuring, supportive monetary conditions and improved export markets, Slovenia is leaping forward again. GDP growth is accelerating and broadening, unemployment is down, and both consumer confidence and the trade balance are reaching record highs. The government may need to step in early with tighter fiscal policy to ensure a controlled landing.

Convergence in GDP per capita has faltered, unlike other countries in the region Gap to the upper half of OECD countries¹



1. Percentage gap with respect to the weighted average using population weights of the highest 17 OECD countries in terms of GDP per capita (in constant 2010 PPPs).
Source: OECD, National Accounts and Productivity Databases.

However, unlike its agile youthful ski-jumpers, Slovenia is not breaking any records in terms of productivity. Indeed, its growth has lagged that of regional peers. Labour productivity is low compared to the OECD average, in part due to large numbers of workers employed in relatively low-productivity small firms, and this has yet to show a strong improvement. Productivity gains were also held back by low investment, as the crisis-afflicted banking sector was unable to lend to domestic firms, and Slovenia has been less successful in attracting foreign direct investment than other countries in the region. In addition, a lack of competitive pressure, due to heavy regulation and ineffective competition policies and enforcement, has inhibited Slovenian firms from developing the efficiency needed to drive productivity forward.

The nimbleness of the Slovenian economy is also being reduced by a rapidly ageing population. Older workers with obsolete skills have tended to take early retirement rather than retrain, and a poor reallocation of labour is leading to labour shortages. In the past such shortages were filled by training young Slovenians, but a shrinking youth population means this is no longer possible. In addition, public spending pressures due to ageing (in terms of health and pensions) are mounting.

However, with an improving economy Slovenia is in a good position to move ahead with reforms that will boost long-term growth. As with any ambitious endeavour, occasional mishaps are inevitable. The just released OECD Economic Survey of Slovenia highlights the need to maintain a fiscal cushion to soften future landings as well as the reforms needed to create a more agile economy to sustain incomes and well-being.

Find out more:

OECD (2017), *OECD Economic Surveys: Slovenia 2017*, OECD Publishing, Paris.