

Post Crisis Growth Issues Observations for the G-24 Technical Group Meeting (March 21, 2013)

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Global Realities 2013

- * The recovery has been weak and uneven
- * The employment effects go beyond Reinhart and Rogoff's historical work, reflecting a fundamental shift away from labor
- * The perfect storm of asset collapses, lack of aggregate demand, worsening distribution and joblessness in many advanced economies is taking its toll
- * Apart from China there are some new darlings as seen in Peru, Panama but with special features
- * Hence the global outlook is not a good one and the IMF's proposed policy actions to support "fragile recovery" seem absent

Results of Bellagio Conference

- * The new growth paradigm involves a potentially greater role for the state, but exactly what?
- * Disconnect between job destruction and job creation with low employment elasticities
- * Low growth co-exists with higher deficits and greater indebtedness, creating a fiscal dilemma
- * Chinese growth and raw materials purchases bolster overall picture, but also skew global demand away from manufactures
- * Global convergence co-exists with greater in country income inequality

The Changing Role of the State

- * The strategic state according to Aghion (2012) should focus on the supply side and on innovation
- * The state invests in education and promotes competition
- * The smart state helps SMEs to thrive and supports product and labor market flexibility
- * The effective state uses public funds to promote investment in sectors with clear externalities and growth potential—targets sectors not firms
- * The state has roles as manager, guarantor, and redistributor, but also the investor
- * As Growth Commission stated: “one can be agnostic on the size of the state but not on its effectiveness.”

The Jobs Story

- * Unemployment has reached peaks in the US and Europe with longest spells in modern time
- * Companies have adjusted their capital-labor mix in both rigid and flexible labor markets
- * Even those with flex-security did poorly in this crisis and plant closures continue to plague manufacturing in the OECD
- * Mixed picture in MICs with India and Brazil on opposite ends of the spectrum in job creation
- * ILO simulations not encouraging on global jobs, with a huge jobs deficit being forecast

The Fiscal Trap

- * Most countries, esp. the EU periphery, the US and Japan, have a long way to go in fiscal consolidation (Blanchard, 2013)
- * If fiscal stimulus adds to debt more than to growth, it deters external finance, adds to cost of servicing and creates unhealthy equilibrium
- * Hence the over-reliance on monetary policy to kick-start growth, but investors are reluctant to take the bait, consumers timid, and gov't constrained. The key is confidence renewal based on long-term fiscal sustainability plans that are politically elusive.

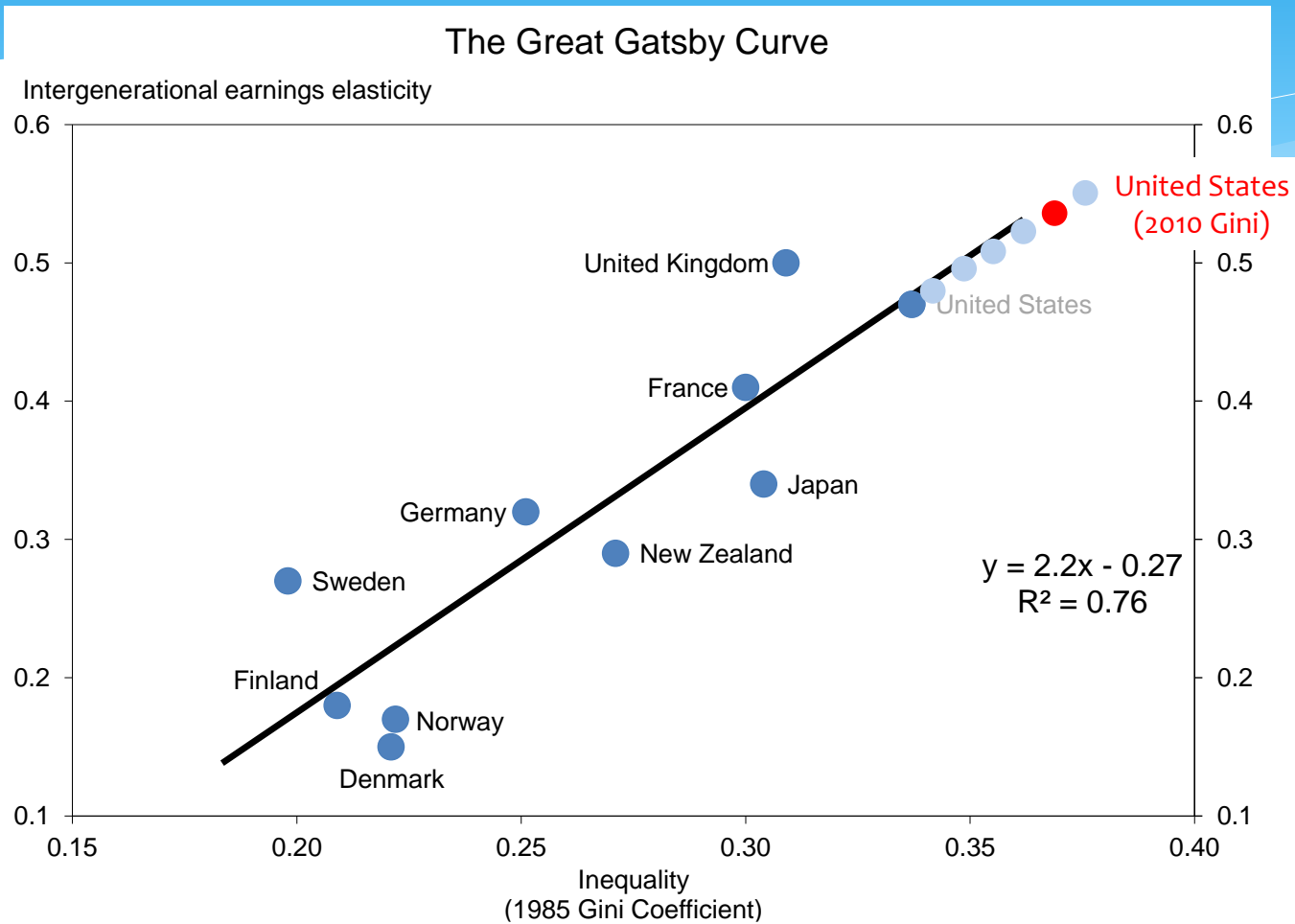
The Changing Structure of Manufacturing Employment-ILO

- * Comparing 1975-85 with 1985-2004 shows OECD losing global jobs share in 24 of 28 sectors with low-income, fast growers (China) gaining most jobs, also from MICs in metals, machinery, and transport sectors
- * Slow growing MICs (South Africa) lost employment shares in 17 sectors and fast growing MICs (Malaysia) lost jobs in 10 sectors
- * Pre-crisis landscape was not favoring the OECD, nor many MICs with major jobs displacement
- * Job losses are associated with rising income inequality, especially in the U.S., but also elsewhere—see IMF's Fiscal Monitor, Appendix 1(October, 2012)

Inequality

- * Piketty & Saez document the shape of increasing inequality in the U.S. that preceded the crisis—top 1% commanding 23.%% of NI and the top .01% getting 12%
- * Stiglitz and others argue that this is unhealthy as well as unfair insofar as equality of opportunity is compromised. See inter-generational income elasticities for proof
- * Concerns about the middle income trap and the fate of the “middle class “ reverberate from this experience. What can be done to avoid bad outcomes?

Figure 8: “The Great Gatsby Curve”: Projection



Source: Corak (2011), OECD, CEA estimates

Policy Instruments to Deal with the Aftermath of the Crisis

- * Fiscal policy constrained by debt levels in spenders and by demographics in savers
- * Monetary policy remit being expanded in the US, UK, EU and Japan, but doubts remain as to the impacts of quantitative easing in particular
- * Some CBs do have explicit exchange rate goals, but few admit to this; for others, the ER is an unintended consequence of national policy
- * Supply side policies are hard to identify, costly to implement, and easy to capture

Implications for Developing and Emerging Market Economies

- * An ailing set of advanced economies is in no one's interest as tradeoffs become sharper and “doing the right thing” becomes harder
- * In a world of slower growth, average economic performance will not be enough as there are no “big waves to catch”.
- * South-south trade has many advantages but some disadvantages in terms of economic composition and the adding up problem and a “lack of oxygen”
- * Currency Wars is only one element of what needs fixing in the global system if growth trajectories are to be regained; how to “increase the pie” rather than fighting over shares?

Where Are We Headed?

- * The G-20 has not been able to sort out key policy dilemmas, such as ER management
- * National policies in the OECD are stymied
- * The coordination problem persists and global regulation is exceptionally difficult to implement in a low growth environment
- * China's role has yet to be recalibrated
- * Investments in the globalization framework are weak and not up to the task at hand—collective action lags the requirements of global public needs, in part because of a changing constituencies and fortunes

The World of New Ideas

- * Recycling surpluses to promote (greener) growth—using SWFs and excess reserves
- * Large-scale temporary work programs for the demographically challenged
- * Abandon losing causes, such as EU uniformity, US tax expenditures, and Chinese financial invulnerability to regain sustainable growth
- * Make the G-20 work or reform it into a group with ability to undertake binding commitments

Thanks



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