

Doc. 11985
07 July 2009

The activities of the Organisation for Economic Co-operation and Development (OECD) in 2008-2009

Report¹

Committee on Economic Affairs and Development
Rapporteur: Ms Anna LILLIEHÖÖK, Sweden

Contents	Page
A. Draft Resolution	2
B. Explanatory memorandum by Ms Lilliehöök, rapporteur	6
1. Background	6
2. Introduction: prospects for the world economy	6
2.1. A synchronised recession, extraordinary in speed and scale	6
2.2. Signs of a slow policy-induced recovery, posing new challenges	7
3. A survey of selected economies	8
3.1. The Americas	8
3.2. Asia	9
3.3. Europe	10
3.4. Problems of middle income economies	12
4. Core areas of OECD activity	12
4.1. The OECD's response to the crisis and beyond: for a stronger, cleaner, and fairer world economy	12
4.2. Countering tax evasion and corruption	18
4.3. Fostering development assistance	20
4.4. "Going for growth": an update	21
4.5. The energy and climate change issue	22
4.6. Measuring the progress of societies	22
5. Prospects for OECD enlargement	23
6. Concluding remarks	23

1. Reference to committee: Standing mandate.



A. Draft Resolution

1. For the purpose of debating the activities of the Organisation for Economic Co-operation and Development (OECD), the Parliamentary Assembly of the Council of Europe meets annually in an enlarged forum including delegations from the non-European member States of the OECD and the European Parliament. The enlarged Parliamentary Assembly has reviewed the activities of the OECD in 2008-2009 in the light of the OECD's latest annual report, the report submitted by the Assembly's Committee on Economic Affairs and Development, and the contributions of other Assembly's Committees in the fields of health and social policy, the environment, agriculture, migration, education and science.

OECD enlargement

2. The enlarged Assembly hopes for progress towards full membership of Chile, Estonia, Israel, the Russian Federation and Slovenia. Furthermore the enlarged Assembly looks forward to further participation of Brazil, China, India, Indonesia and South Africa in the substantive work of the OECD under the "Enhanced Engagement" programmes, leading up to accession talks, as well as to further co-operation between the OECD and Southeast Asia as a priority region. The enlarged Assembly believes that full respect for democracy, human rights and the rule of law, including international law, should constitute an essential criterion for judging whether a candidate country should be invited to join.

The global economy

3. The enlarged Assembly deplores the depth and effects of the current recession, which the OECD in its June 2009 Economic Outlook, characterises as "the deepest decline in post-war history", and which has brought some countries to the brink of bankruptcy. The OECD estimates that output in the OECD economies will fall by 4.1% this year, with an ensuing recovery "likely to be weak and fragile for some time to come". The enlarged Assembly especially emphasises the severe impact of the crisis on unemployment and the continuing challenges this poses to governments. Unemployment will peak in 2010-2011 at double digit levels in many countries. The enlarged Assembly believes that more resources should be channelled to supporting employment than has hitherto been the case.

4. The enlarged Assembly welcomes the OECD's September interim assessment, based on recent indicators to be taken with due caution, that a tentative recovery has begun. Such signs of recovery identified by the OECD include, in the United States, stronger than expected retail sales and manufacturing orders and a slowing of the rise in the number of unemployment benefit claims, together with more positive indicators of confidence among manufacturers and consumers, also apparent to a degree in Europe, with better than expected second quarter growth figures. Although financial market conditions have shown improvements, concerns remain about the health of the banking sector.

5. The enlarged Assembly is concerned by the OECD's warning about the generally deteriorating state of member countries' public finances, with debt ratios in some that have reached record and unsustainable levels. The enlarged Assembly urges the OECD and its member states and those of the Council of Europe, as well as the International Monetary Fund (IMF), to monitor the situation closely with a view to bringing the situation under control as soon as the financial and economic crisis permits. In the meantime member states should pursue or resume the process of structural reform designed to return their economies to a sound footing in order to position themselves better to withstand future crises.

6. The enlarged Assembly welcomes the OECD's "Strategic Response to the Crisis" designed to bring forward proposals in support of G20 action to counter the effects of the recession in a range of areas, notably the resolution of the financial sector crisis, corporate governance, pensions and financial education, as well as strategies for maintaining open markets and measures to improve tax transparency and co-operation. The enlarged Assembly underlines the particular importance of international co-operation with a view to strengthening supervision of the financial sector and invites the OECD, in co-ordination with the other international economic and financial institutions concerned, to pursue vigorously its efforts to help end the crisis and to prevent future such episodes.

7. The enlarged Assembly welcomes the conclusions of the OECD Ministerial Council meeting of 24-25 June 2009, adopted by the OECD member states and accession countries and relevant for all open market economies, and the strong emphasis they place on implementing structural reforms needed to transform the current policy-driven recovery into self-sustained growth.

8. The enlarged Assembly encourages the member countries of the Council of Europe and the OECD to take account of the significant input by the OECD to the G8 process, which involves substantive co-operation in areas ranging from taxation and market integrity to development. At their summit held in L'Aquila on 8-10 July 2009 the G8 leaders welcomed the continuing support provided by the OECD to the G8+G5 process through its analytical contributions and the work of the OECD's Heiligendamm L'Aquila Process Support Unit, which will continue to focus on investment, innovation, energy and development, and will start addressing vulnerable states and food security.

9. In particular, the 2009 G8 Summit welcomed the OECD's work on tax transparency and asked the OECD to continue its efforts by expanding participation in the Global Forum on Transparency and Exchange of Information for Tax Purposes, establishing a peer review process, considering a multilateral approach for the exchange of information and developing a set of effective countermeasures. The Global Forum has since met and established the peer review mechanism. In this context, the enlarged Parliamentary Assembly urges the OECD and the Council of Europe to update the Convention on Mutual Administrative Assistance in Tax Matters (ETS No. 127). The enlarged Assembly also emphasises that in the matter of Tax Information Exchange Agreements, it should be made quite clear that respect for normal bank confidentiality must be the rule, and that only in cases of tax evasion and criminal activity should it be lifted. The enlarged Assembly also asks the OECD to study the effectiveness of the Tax Information Exchange Agreement system in relation to the claims made for it.

10. The enlarged Assembly encourages the OECD to reflect further as to the nature and operation of today's market economy and that of financial markets in facilitating the production of goods and services, the implications of government ownership of the means of production, and the nature of an economic and financial system based on sound and sustainable principles. The enlarged Assembly also calls on the OECD to make a detailed study and recommendations concerning the global imbalances, for example as between China and the United States in savings, consumption and investment rates, that contributed to the present crisis and which still may not be resolved. Taking note of both the serious effects of the downturn on middle-income economies, including those in Central and Eastern Europe, and of the important role of the emerging economies such as Brazil, China, India, Indonesia, and South Africa in the global economy, the enlarged Assembly invites the OECD to expand its coverage of these economies in its work.

11. The enlarged Assembly notes with concern that the OECD forecasts a staggering 16% drop in world trade growth in 2009, and urges all countries to avoid any steps, including domestic support measures, that could provoke protectionist reactions, and to maintain open markets and free trade. Every attempt should be made to revive the Doha Round of trade negotiations and to bring them to a successful conclusion, not least in a spirit of solidarity with the least developed countries. In this context, the enlarged Assembly welcomes the promising results of the OECD's co-operation with the World Trade Organization (WTO) in promoting assistance for the low income countries with a view to increasing their trading capacity.

12. The enlarged Assembly welcomes the OECD's efforts to promote international investment under such principles as non-discrimination, and encourages the OECD to continue to monitor and report on international investment measures, in co-operation with the United Nations Conference on Trade and Development (UNCTAD), the WTO and the IMF, as well as under the Freedom of Investment Project.

13. The enlarged Assembly notes with satisfaction that in 2008, total net official development assistance (ODA) from members of the OECD's Development Assistance Committee (DAC) increased by 10.2% in real terms to \$119.8 billion, the highest ever recorded in dollar terms. However, this represents only 0.3% of members' combined Gross National Income (GNI), well short of the 0.7% United Nations target. The enlarged Assembly welcomes OECD's new partnership with the African Development Bank (AFDB) to support the efforts of African governments and business to fight bribery and corruption and enhance corporate integrity. The enlarged Assembly stresses the importance of the OECD's work to evaluate and improve the results and effectiveness of aid, in line with the Paris Declaration on Aid Effectiveness (2005) and the Accra Agenda for Action (2008).

14. The enlarged Assembly welcomes the work of the International Energy Agency (IEA), within the OECD framework, to forecast energy needs and promote rational energy policies. It notes and endorses the IEA's call for massive investment in energy infrastructure to maintain long-term energy supply, not only in oil and gas but especially in non-fossil fuel alternatives; for increasing energy efficiency; and for maximising energy security through diversification of the energy mix. The enlarged Assembly endorses the OECD's view that "nuclear energy is the only virtually carbon-free technology with the proven track record on the scale required" to meet global emission targets and commitments.

15. The enlarged Assembly is deeply concerned by the growing unemployment rate in the OECD countries, which is projected to rise through 2010, approaching a new postwar high of 10% with 57 million unemployed, according to the *2009 OECD Employment Outlook*. In this regard, the enlarged Assembly welcomes the OECD Restated Jobs Strategy, a tool of current relevance which provides a framework for assessing policy responses to support those most affected by the economic downturn. Attention should remain high on vulnerable groups particularly affected by the crisis, youth, immigrants, low-skilled and older workers, and those on temporary contracts, who may become trapped into long-term unemployment. In addition, both the research community and policymakers should pay special attention to the family and propose concrete support measures when formulating social cohesion strategies and planning a response to the current crisis.

16. Furthermore, considering that people in lower socio-economic groups tend to have higher rates of disease, disability and mortality, the enlarged Assembly encourages the OECD to further examine national prevention health care and health promotion policies aiming at reducing inequalities in health status and ensuring adequate or equal access based on need.

Environment and agriculture

17. The enlarged Assembly expresses its concern about the effects of the economic crisis on the environment in general, and invites states to continue their efforts to reduce the risks resulting from climate change and to ensure that the development of renewable energies is not neglected for economic reasons. It takes this opportunity to welcome the adoption, at the meeting of the OECD Council at Ministerial Level on 25 June 2009, of the "Declaration on Green Growth", which invites the OECD to draw up a Green Growth Strategy in order to achieve economic recovery and environmentally and socially sustainable economic growth.

18. The enlarged Assembly welcomes the OECD's work on the economics of climate change as an important contribution to the ongoing international negotiations, helping countries to put the post-2012 agreement onto a solid economic footing and to put in place cost-effective policies for tackling climate change.

Migration and population

19. The enlarged Assembly commends the work undertaken by the OECD in seeking responsive, fair and effective migration and integration policies that could adjust to the current crisis and beyond. It encourages the OECD to invite its members to step up efforts towards working out functional, coherent and long-term migration management policies with a view to maximising the benefits of migration. Channels of regular migration should remain open with a view to meeting continued demand for migrant workers, thus helping to prevent irregular migration and trafficking in human beings.

20. The enlarged Assembly remains particularly concerned about the protection of the rights of migrants and equality of treatment during the economic downturn and, to this end, calls upon the OECD to seek guarantees from its member countries that the rights of migrants are adequately and effectively protected in terms of human rights, working and living conditions and in the event of loss of employment, and that migrants are offered adequate protection from any form of discrimination and xenophobia.

21. The enlarged Assembly urges the governments of OECD countries to strengthen their co-operation with developing countries, including by promoting measures to facilitate remittance flows through initiatives of tax deductibility of both remittances and money placed in special savings accounts to support development projects, by reducing obstacles to returns through improved assistance, greater protection of social rights and transformation of the potential of these returned migrants into "brain gain", and by addressing the risks of "brain drain" through responsible recruitment policies.

22. The enlarged Assembly notes with concern the increasing hostility to migration and immigrants in public opinion. It therefore encourages the OECD to join efforts and support projects of awareness raising, in particular through public media, about the valuable economic and social contributions made by migrants. Additionally, it encourages the OECD to work with civil society groups, and notably with diaspora associations, with a view to challenging the stigmatisation of migrant workers.

Education and science

23. The enlarged Assembly welcomes the organisation of a meeting with the Governing Board of the Programme for International Student Assessment (PISA) of the Organisation for Economic Co-operation and Development (OECD) and the International Association for the Evaluation of Educational Achievement (IEA) in order to explore the pedagogical and ideological grounds of their work and examine the possibility of expanding the scope of their assessment to include civic awareness, creative skills and cultural education.

24. The enlarged Assembly again encourages the OECD to pursue its studies on the efficiency of teaching and learning processes in order to formulate proposals to reverse the existing trend of increased educational expenditure with no improvement in educational results. Improving the efficiency of learning processes is essential in order to tackle the current insufficiency in adult competencies and to ensure the sustainability of adequate lifelong learning and continuing education systems.

25. The enlarged Assembly encourages the OECD to consider looking into entrepreneurial thinking and behaviour treated as a factor of increasing the knowledge-based model of economy as – in particular in countries with more centralised economies - all activities geared to improving entrepreneurial thinking and behaviour, especially in the younger generations, could be important and effective factors for both economic and social growth.

B. Explanatory memorandum by Ms Lilliehöök, rapporteur

1. Background

1. On 30 September 2009, the enlarged Parliamentary Assembly of the Council of Europe will meet in Strasbourg for its annual debate on the work of the OECD. Prepared specifically for that debate, this report focuses on the economic aspects of its work and is based mainly on information provided to the rapporteur and to the Committee on Economic Affairs and Development by OECD staff in June, as well on the results of the OECD's Ministerial Session on 24-25 June and on its mid-year Economic Outlook and September interim revision. The revised provisional draft resolution will be submitted for adoption at the meeting of the Enlarged Economic Committee to be held on 29 September, and the resulting draft resolution will be voted on by the Enlarged Parliamentary Assembly following the debate the next day. It should be noted that parallel reports are being prepared this year by the following committees: Social, Health and Family Affairs; Culture, Science and Education; Migration, Refugees and Population; Environment, Agriculture and Local and Regional Affairs. These committees will also propose additions, where appropriate, to the provisional draft resolution.

2. The rapporteur wishes to express her gratitude to all at the OECD who have helped in the report's compilation. In a period of extraordinary economic drama, this has been a fascinating and thought-provoking task. It has also demanded some caution, given the uncertainty attached to forecasts and predictions at this time. Bearing that in mind, the paper offers an overview of the factors driving economic circumstances and a summary of developments in OECD member countries and other key emerging economies.

3. Naturally, the report focuses on the OECD's efforts to help address the global downturn. It examines the OECD's co-operation with the G20, including action on tax havens. It assesses the specific challenges faced by developing countries and discusses the OECD's priorities for a sustainable recovery.

2. Introduction: prospects for the world economy

2.1. A synchronised recession, extraordinary in speed and scale

4. In last year's report, the rapporteur suggested that prospects for the world economy were finely balanced, between what the OECD called a "relatively benign" outcome and a darker scenario, whereby a global credit crunch might feed through into domestic markets, causing a global slump: "the fat tail to the downside". Last September, with the collapse of Lehman Brothers, the world economy moved rapidly down this latter path, and by December the OECD talked of being "on the verge of a protracted recession of a magnitude not experienced since the 1980's". In an interim Economic Outlook, published in March, the OECD downgraded its forecasts, citing "the deepest and most synchronised recession in our lifetimes".

5. Why did this happen, and with such remarkable speed? In essence, the recession was triggered by a near-meltdown in global credit markets, caused by excessive lending to high-risk areas, such as low-income mortgages in the United States, using complex financial products which were little understood, for which risk controls were inadequate and whose scale and concentration have been disastrous. But the recession's ferocity was then driven by a sudden decline in private demand, across all markets but especially in those countries that had been most consumer-oriented, as sentiment gave way under a combination of factors: the ongoing credit squeeze and uncertainty as to its duration, continuing declines in property values and a dramatic fall in stock prices, and a fundamental loss of confidence, at first relating to retail banking and mortgages, but increasingly driven by fears of unemployment, and even doubts as to the ability of governments to manage the situation. All this exacerbated the collapse in world trade.

6. This sudden recessionary shock has been all the more severe because, unlike in previous recent downturns, no region has been able to escape its effects, and thereby act as an engine for recovery. In part, this is due to the integrated, globalised nature of today's trading system, and especially the power of global credit markets. But as such, it is also associated with the imbalances that have arisen in recent years between "consumer" economies, such as the United States, the United Kingdom and Australia, and "saver" economies, such as China and Japan. For some time, the OECD has been warning that this makes global growth dangerously dependent on the confidence of a relatively small number of consumers, and on a great deal of borrowing. On top of that, many governments failed to use the years of buoyant revenues to correct their fiscal positions, leaving them with little room for manoeuvre in the face of the recession and significant debt problems to come.

7. The scale of the slowdown has been astonishing. OECD-wide economic activity fell by -7.8% in the fourth quarter of 2008 and -8.3% in the first quarter of 2009. After two decades of almost unbroken growth, a -16% fall in world trade is expected this year, and growth of only 2.1% is suggested in 2010, which will imply continuing recession for many countries. Accordingly, unemployment in the OECD area, which was 5.6% in 2007, will reach 9.8% in 2010; over the same period, fiscal deficits will worsen from -1.4% to -8.8%, while the “output gap”, which measures demand versus production capacity, will go from a positive 1.7% of GDP, suggesting supply constraints which tend to force up prices, to -5.8%. This heralds near-zero inflation and, in some countries, deflation.

2.2. Signs of a slow policy-induced recovery, posing new challenges

8. However, the OECD considered in its June Economic Outlook that the recession was approaching the bottom, although the recovery was likely to be “weak and fragile for some time” and the negative economic and social consequences of the crisis would be “long-lasting”. Nevertheless, the growth projections published in that issue had been revised upwards since the previous issue “for the first time since June 2007”. Apparently, the lessons of the 1930s having been borne in mind, the response to the crisis has been broadly correct. Heavy intervention in financial markets averted disaster, and brought an element of stability, while interest rates were brought to near-zero and a range of monetary “easing” policies introduced to address credit shortages. In particular, the stimulus packages put in place by most OECD members and some other major economies had a positive impact, with the measures announced for the period 2008-10 likely to amount to some 3.5% of OECD-wide GDP, according to the March Interim Report.

9. A policy-induced recovery is therefore likely to gather pace during 2010, with the United States and China – which both have substantial stimulus programmes – leading the way. Indeed, the latest (for July 2009) OECD “composite leading indicators” (which attempt to indicate turning points in economic activity approximately six months in advance) pointed to stronger signs of recovery in most of the OECD economies. Clear signals of recovery are now visible in all major seven economies, in particular in France and Italy, as well as in China, India and Russia. The signs from Brazil, where a trough is emerging, are also more encouraging than in June’s assessment.

10. All this suggests that the worst is probably behind us – but “on the way out it looks as if recovery will take hold in a staggered manner across countries” and it is too soon to be confident that further shocks will not, once more, transform the picture. The very scale of recent declines should make us wary of predicting a straightforward rebound, and a host of challenges will remain in the aftermath of the crisis, which will leave the global economy vulnerable.

- The financial system, while fairly stable, has not fundamentally recovered, and the issue of “toxic assets” remains; significant further action will likely be necessary. When this is achieved, governments will be left with a host of emergency measures that will need to be unravelled if it is once more to drive global growth.
- Many governments will be left with a combination of hugely-inflated deficits, high unemployment and deflationary pressure. There is a risk of rising protectionism in the context of a “deflationary recovery”, in which growth rates are stubbornly low; or conversely, this may be countered by a burst of inflation that secures short-term growth but forces up interest rates and creates a whole new set of economic problems.
- As mentioned above, the boom of recent years was founded on growing imbalances between consuming and saving nations. If the recovery is based solely on persuading those consumers to spend again, this pattern is likely to continue, increasing the likelihood of a recurrence. Similarly, the place of developing countries in the world trading system needs to be addressed, if they are not once again to be at risk of the disproportionate difficulties seen during this slowdown.

11. To amplify these points, we will take a brief look at the specific circumstances in the world’s key economies, as seen through the lens of the OECD’s experts. We will then assess in more detail how the OECD has actively engaged with the challenges posed, and look at the solutions it is promoting, to help the world economy to emerge in good long-term health.

3. A survey of selected economies²

3.1. The Americas

12. In the *United States*, consumer demand (representing about 70% of economic activity) has been crucial to sustaining growth during the last few years, even as house prices fell drastically. But with the addition of the credit crunch, reduced stock values and sharply rising unemployment, consumer confidence suddenly collapsed in the United States, with GDP shrinking by -6.3% in the final quarter of 2008 alone, and -5.7% in the first quarter of this year. But this rate of decline has slowed dramatically (to -1% in the second quarter), so that the United States' economy is projected to contract by only around -2.8% this year, and should achieve growth by early 2010 if not before. Unemployment, however, will continue to surge, from 5.8% in 2008 to 9.3% this year, and 10.1% in 2010. This will have a dampening effect on consumer spending, down by 1.2% in the second quarter of 2009, while the savings rate, close to nil before the crisis has risen to 5.2%, the highest since 1998.

13. In the OECD's view, the projected recovery will be largely attributable to the Federal monetary policy and fiscal stimulus, which represents some 2.1% of GDP in 2009 and 2.4% in 2010. As long as commodity prices remain low, there is thought to be little threat of inflation – in fact, deflation is more likely, given that a wide “output gap” is emerging, as production capacity outstrips demand. To tackle this, the Federal Reserve will want to maintain its near-zero interest rate stance. The OECD underlines, however, that once a recovery is in place, it will need to move promptly to reverse this so as to restrain inflation. For the present, the OECD would like to see the announcement of an inflation target to more firmly anchor inflation expectations. With the deficit already projected to reach 11.2% of GDP in 2010, once the projected recovery takes hold, the Federal government will need to undertake a stringent overhaul of its finances.

14. It is worth remembering that the key to securing a recovery, in the United States and beyond, lies in ensuring stable financial conditions and normal flows of credit. Despite recent improvements in financial markets, the measures of the Financial Stability Plan, including “stress tests” for the major banks, and the Public-Private Investment Program, the OECD believes that government may still need to inject public funds in pursuing the systematic restructuring and recapitalising of banks and other financial institutions encumbered by bad assets. Financial supervision and regulation need further improvement. Overall, the financial system remains fragile.

15. For *Mexico*, with around 20% of its economy geared to exports to the United States, the effect of lower demand has been acute. GDP shrank by -8.2% during the first quarter, and though lower oil production was partly responsible, manufacturing exports fell by -22.8%. The influenza epidemic will also have contributed to the downturn, with its negative effects on businesses and tourism. Despite the sharp drop in demand, however, inflation has remained relatively high, mainly because of a lag in adjustment to lower world prices. This has limited the central bank's scope for lowering interest rates. With Mexico likely to see its weakest economy since 1995, government spending has been increased by some 13%, and a fiscal deficit is expected this year and next. With monetary and fiscal stimulus, and world activity reviving, the OECD projects that demand should stabilise, with quarterly growth rates becoming positive towards the end of 2009 to reach an annual rate of some 4% by the end of 2010.

16. Since late 2008, exports from *Canada* have also fallen sharply, as have all forms of household spending, especially on housing. GDP fell by 5.4% in the first quarter of 2009, although the decline has slowed since then. This year the economy is likely to contract by -2.6%, stabilising in 2010. The unemployment rate was 8.7% in August, and is expected to stabilise at just below 10% in 2010. Authorities have taken action to support financial markets and stimulate the economy through expansionary measures and monetary easing, with the Bank of Canada, for example, lowering its policy interest rate to 0.25% and committed to holding that level until the end of June 2010 on condition that inflation follows the expected path. Given the strong fiscal position established in recent years, the OECD says there is scope for further stimulus, should economic conditions warrant. However, lower tax revenues and increased government spending measures will result in a large general government deficit for the first time since the mid-1990s.

17. In the case of *Brazil*, the OECD feels that the current policy mix is supportive, and current monetary easing policies can be continued for the time being; there is, however, little room for further fiscal initiatives, given the pressure on domestic credit markets. Having grown 5.1% last year, the economy is likely to contract

2. The OECD has cautioned that certain figures used by the rapporteur in this section reflect countries' latest national account and short-term data releases which could lead to upward revisions in the OECD's growth projections.

by around -0.8% this year, before resuming growth of 4.0% in 2010. Despite sharp decelerations in the last quarter of 2008 and first quarter of 2009, by mid-year industrial production was expanding and retail sales were particularly resilient. Domestic demand was poised to gather momentum in the second semester.

3.2. Asia

18. The speed of decline in demand from the United States and in world trade generally has had a severe impact in the world's second largest economy, *Japan*, where GDP is likely to decline by some -6.8% this year, and deflation has returned. A collapse of -34% in Japanese exports has been exacerbated by a strong (25%) rise in the value of the yen; and as corporate profitability declined, stock prices halved. Business confidence plummeted causing a major cutback in investment plans. However, there are signs that the trade-induced contraction is close to the end, thanks not least to fiscal stimulus. Nevertheless, recovery is likely to be slow and there is uncertainty on the policy that will be implemented by the newly elected government.

19. By 2010, unemployment is expected to reach 5.7%, and deflation will remain unchanged at -1.4%; private consumption will remain weak as the decline in wages that began last year accelerates. The four government fiscal stimulus packages introduced since August 2008, amounting to 4% of GDP, will help to soften the length and depth of the recession, taking growth into positive territory from the second half of 2009, although at a rate under 1% through 2010. Performance could be more positive if overseas markets were to recover sharply.

20. Although the OECD supports the fiscal stimulus packages already introduced, it suggests that there is little scope for additional measures, with Japan's budget deficit set to increase from 3% of GDP in 2007 to about 10% in 2010 and the debt ratio projected to approach 200% in that year, the highest ever recorded in the OECD area. In the OECD's view, the government should focus on fiscal consolidation as the economy stabilises, maintaining the commitment to a primary budget surplus, and should pursue pro-growth tax and social insurance reforms, accompanied by structural reforms, especially in the service sector, in order to improve living standards in the context of a shrinking working-age population. Meanwhile, the Bank of Japan should keep interest rates close to zero and maintain measures to increase liquidity until underlying inflation is firmly positive.

21. *Korea*, whose economy is highly-g geared toward exports, suffered a -5.1% GDP fall in the last quarter of 2008 compared to the previous quarter, and exports declined at an annualised rate of -31% at the end of the year. However, this decline was reduced by half in the first quarter of 2009, thanks in part to a depreciation of the won, but has by no means been reversed since. Nevertheless, it appears that the economy has bottomed out, with overall reported growth of 0.1% in the first quarter and 2.3% in the second, as fiscal stimulus took effect. Unemployment rose from 3.2% in the fourth quarter of 2008 to 4% in June 2009, and the consumer price index dropped from 5.9% in August 2008 to 1.9% in June 2009 over the previous year's figures. The key to continued recovery will be the resumption of export growth, not least to China. Combined with the ongoing fiscal stimulus, this is projected to increase output growth to about 4.5% by late 2010.

22. *China's* output growth slowed throughout 2008, and GDP growth fell back to 9% from 13% in 2007. This year 7.7% is expected. With private consumption and investment reacting positively to the stronger economic situation expected to result from monetary and fiscal stimulus and improvement in the global trade environment, growth next year is projected at 9.3%. Significant stimulus has been applied, including an investment plan valued at 5.6% of GDP over 2009-2010, parts of which relate to projects already in the pipeline such as reconstruction following the 2008 earthquake. About one-third (1.6% of GDP) will be financed through the central government's 2009 budget. The total increase in central and local government spending attributable to stimulus spending this year is estimated at 2.6% of GDP. In addition, value added tax rebates on exports and investment have been raised, at a cost of 0.9% of GDP, although this will be partly offset by the introduction of a 20% tax on petroleum products. An increasing number of indicators suggest the recovery is already underway in China, though risks remain, in particular that of deterioration in the quality of bank loans if expansion of lending continues unabated to fuel increasing investment spending and consumption.

23. Growth in *India*, which had approached 10% in 2006, is likely to be around 6% this year and 7.2% in 2010. Although the rate of decline in exports has eased, lower overseas demand will continue to offset rising domestic consumption. The government introduced a new stimulus package at the beginning of 2009, following sizeable increases in public spending in 2008. The result is a total public sector deficit estimated at -11% of GDP in 2009. The OECD sees the deterioration in the fiscal position as reducing the scope for further discretionary fiscal policy action. The OECD sees a need for tighter fiscal discipline, a speeding up of structural reform and increased sales of public assets. Although interest rates have been eased, allowing the stock market to stabilise, the OECD sees further room for monetary easing. It also warns against the growing use of protectionist measures.

3.3. Europe

24. In June the OECD projected that the *euro area economy* would contract by -4.8% this year and pick up only gradually in 2010, as financial markets improve and the full effects of stimulus policy are felt. Inflation is expected to remain low, at about 0.7%, compared to 0.5% this year and 3.3% in 2008. From 7.5% in 2008, unemployment is projected to jump to 10% this year and 12% in 2010.

25. Europe's manufacturing powerhouse, *Germany*, is expected to suffer a fall of -18.9% in exports this year; GDP will decline by -6.1%, and will barely grow next year, as unemployment reaches 12%. This will mirror unemployment in the euro area generally, which will rocket from 7.5% last year to 12% in 2010. The outlook has slightly improved since June. Figures released by Eurostat at the end of July showed a slightly lower than expected increase in unemployment although a greater than expected fall in inflation. European figures also showed that the contraction in manufacturing and services had slowed markedly. Business confidence increased and the euro rose against the US dollar. Signs of stabilisation and recovery were strongest in Germany, reflecting better export prospects.

26. Member states have so far introduced measures equal to more than 1% of GDP in 2009, and rather less next year. Additional stimulus is coming from the automatic stabilisers (eg. unemployment benefit) which are relatively large in the euro area, as well as from measures to support the financial sector. The OECD warns that fiscal deficits and debt ratios are rising rapidly. The euro area budget deficit is projected to rise to 5.5% of GDP in 2009 and 7% in 2010. All member states need to make credible plans for fiscal sustainability and to end stimulus measures once recovery is deemed sufficiently robust. Nevertheless, additional fiscal stimulus measures could still be undertaken if necessary by those countries which have budgetary scope. In addition, given the disinflationary trend, the European Central Bank (ECB) is recommended to use quickly their remaining scope for cutting interest rates, and to introduce quantitative easing policies. Around Europe, stimulus activity varies widely. Germany has undertaken support equivalent to over 3.75% of GDP in 2009-2010. The OECD also underlines that, to protect its medium-term growth prospects, the European Union as a whole must safeguard its internal market, and liberal external trade and investment regimes.

27. Having fallen by -1% in 2008, GDP growth in *Italy* is expected to decrease by -5.2% in 2009, with minimal growth forecast for 2010, according to the OECD. Italy has been particularly hard hit by the contraction in world trade, with a projected fall in exports of -20.9% in 2009, and this together with deteriorating financial conditions, despite a relatively healthy banking system, has considerably reduced investment. Given its weak underlying fiscal position, Italy has refrained from additional discretionary fiscal spending while stimulating domestic demand, notably private consumption, within the framework of the existing budget. Unemployment benefit has been extended and support has been increased for low-income families. The OECD points out that economic performance can be enhanced over the long term by both macroeconomic and structural policy reforms.³

28. In *France*, stimulus measures amounting to 1.3% of GDP have been put in place, focusing on investment in infrastructure and liquidity support for small and medium-sized firms. Moreover, further measures including tax concessions should moderate the contraction in domestic demand. In March the OECD predicted the economy would shrink by about -3% this year, recovering only slowly to 0.2% in 2010, but output in the second quarter of 2009 rose by 0.3%, according to provisional figures released by the French INSEE, and in September the OECD revised its forecast for 2009 upwards to -2.1%. With the government deficit already set to reach around 8% next year, a clear medium-term plan to return to fiscal sustainability is called for. On structural reform, the OECD believes that one priority must be to increase the employment rate, forecast to rise from 7.4% in 2008 to 9.7% in 2009 and 11.2% in 2010. A second priority is to increase the competitiveness of firms in order to halt a continuing erosion of market share in world trade.

29. Nowhere in the Euro area are the employment effects of the crisis more visible than in *Spain*, where the unemployment rate is projected at 18.1% for 2009, rising to 19.6% in 2010. Young unqualified workers are particularly affected, with the rate exceeding 33% in April 2009. With output expected to fall by 4.25% in 2009 and a further 1% in 2010, the government is implementing budgetary stimulus equivalent to about 2% of GDP this year, including a programme to boost investment spending by local governments, abolition of the wealth tax and accelerated payment of tax credits. The general government's budget balance is expected to reach 9.5% of GDP in 2010, when most central government measures designed to stimulate the economy are likely to be withdrawn.

3. OECD, Economic Survey of Italy 2009.

30. The *United Kingdom* is experiencing severe recession, with output projected to decline by 4.3% in 2009 and recover only sluggishly in 2010. In the second quarter of 2009, GDP fell by 0.8%, giving a year on year figure of 5.6%. The sterling depreciation has not been sufficient to offset the decline in demand for exports. Unemployment is expected to rise to 9.7% in 2010, while wage growth and inflation are falling. With its policy rate at near zero, the Bank of England has undertaken quantitative easing, which should help cushion the recession, although its scope remains uncertain. The pressure on government finances is very acute. For while net debt levels were only 2.7% in 2007, the structural balance has been deteriorating for some time, and with the demands of economic stimulus (around 1.6% of GDP in 2009), and support for the financial industry, the deficit is set to reach 12.8% this year and 14% next year. The government's room for manoeuvre in responding to future shocks is therefore limited, and the OECD calls for it to "continue to develop its fiscal consolidation plans, within a strong and credible medium-term fiscal framework". The OECD believes that financial conditions are still unfavourable, and that although they have improved in 2009, "economic recovery will require restoration of the financial system and the supply of credit." There is also considerable uncertainty surrounding recovery of the housing market.

31. In *Hungary* real GDP contracted by an annualised 7.2% in the fourth quarter of 2008 and 9.6% in the first quarter of 2009. Monetary policy however has remained tight in the face of loss of confidence in the forint, specifically related to the large foreign currency loans held by households and the recession in the euro area export market. The situation has been improved by the provision of \$25.5 billion in loans from the World Bank, IMF and European Union, but a painful process of fiscal consolidation is in prospect. Unemployment is projected to reach 11.7% in 2010. The OECD considers that the main downside risk to recovery "is that the parliamentary elections scheduled for 2010 lead to excessive public expenditures, triggering a confidence crisis".

32. The collapse of its three main banks in October 2008 deepened the contraction of domestic demand already under way in *Iceland*. Consumers slashed spending, residential and business investment as well as imports fell drastically, credit dried up, unemployment shot up as well as consumer price inflation in the face of the collapse of the currency. Iceland entered into a \$2.1 billion loan agreement with the IMF with a view to stabilising the exchange rate, restoring normal activity and returning public finances to a sustainable path. Exchange controls on capital account transactions were imposed and the official policy interest rate was raised to 18%, subsequently reduced to 12%. The OECD considers that restoring the smooth functioning of the banking system is the top priority. On 20 July the Icelandic Finance Ministry announced a plan to recapitalise all three of the banks, all of which had been nationalised.

33. The economy in *Russia*, which had slowed to 5.6% growth last year, will see contraction of -6.8% this year, undermined by a collapse in oil prices and massive capital outflows, leading to a 30% cumulative depreciation of the rouble and tighter monetary policy. The government meanwhile introduced fiscal stimulus measures amounting to about 3.5% of GDP (but only approved by the Duma in April 2009) which will support demand through the rest of the year. These included some tax cuts and increase benefits to address the social impact of the crisis, but expenditure was mostly geared to support for firms, which may hamper competition and efficiency, in the OECD's view. Commodity prices have rebounded and capital outflows were reversed in the second quarter of 2009 for the first time in a year, raising the probability of a resumption of growth. However, banks have curtailed lending and the banking sector remains fragile. Seeking to restore banking confidence, the government introduced a recapitalisation plan totalling \$4.8 billion in 2009 and \$10 billion in 2010. The fiscal balance has moved from a 4.8% surplus to a -6% deficit. The OECD suggests that the fiscal stimulus measures should be implemented quickly, in particular for social protection and active labour market policies. Further resort to protectionist measures should be avoided, not least in the context of Russia's prospects for joining the World Trade Organization.

34. *Ukraine*⁴ is heavily dependent on foreign credit, and its main export is steel. In the summer of 2008, as credit markets froze and commodity prices plunged, its currency lost 40% of its value and banking confidence collapsed. By early 2009, GDP was falling by an annual equivalent of 25%, while the greater part of a stabilisation loan had been frozen by the IMF, due to domestic political disagreements. With the loan now restored, a start has been made on financial restructuring, and consumer confidence is showing small signs of recovery. There has also been a recovery in steel production, helped by the lower exchange rate. On 3 August 2009, the European Commission announced that the European Bank for Reconstruction and Development (EBRD), the European Investment Bank (EIB) and the World Bank had agreed to lend Ukraine about \$1.7 billion to pay its gas bills to Russia and to modernise its natural gas transit system.

4. Information based on non-OECD sources, since OECD does not produce economic projections for Ukraine.

3.4. Problems of middle income economies

35. Six Council of Europe member states (Albania, Armenia, Azerbaijan, Georgia, Moldova and Ukraine) fall into the category of Lower Middle Income Economies (LMIE) defined by the World Bank as those whose 2008 Gross National Income *per capita* was between \$976 and \$3855, while eleven (Bosnia and Herzegovina, Latvia, Lithuania, Montenegro, Poland, Romania, Russia, Serbia, the Former Yugoslav Republic of Macedonia and Turkey) belong to the category of Upper Middle Income Economies (UMIE), with *per capita* GNI between \$3856 and \$11905. Of the non-European countries mentioned so far, China and India are in the first category, Brazil and Mexico in the second. Mexico, Poland and Turkey are already member states of the OECD, an organisation usually thought of as made up of the high income advanced industrial countries, while Chile, an upper middle income economy, and Russia are on the path to membership, and Brazil, China, India, Indonesia and South Africa, all middle income countries, enjoy an “enhanced engagement” relationship with the OECD.

36. The impact of the global crisis has been particularly severe on the middle income countries, many of which had recently been showing strong growth, although Asian middle income economies have now rebounded strongly and are likely to emerge from the crisis earlier than OECD countries. One key problem has been an imbalance in the degree of exposure to international currency markets. In many countries of Eastern Europe, for example, budget and balance of payments deficits were financed to a large extent by contracting external debt, especially private foreign currency loans. This has made these countries more vulnerable to capital outflows and reductions in foreign direct investment. The middle income countries may thus be more vulnerable to the effects of the global recession on their exports. They may need more advice on the lessons to be learned from previous crises, for example placing too much emphasis on exports and not enough on domestic demand. Nor should it be forgotten that these countries represent models for the future trajectory of developing countries.⁵

37. Most of the middle income economies that are Council of Europe member states are countries of operations of the EBRD. However, since non-European middle income countries, as well as developing countries, also come within the remit of the OECD, it could well intensify its coverage of European middle income economies in its analyses and recommendations.

4. Core areas of OECD activity

4.1. The OECD's response to the crisis and beyond: for a stronger, cleaner, and fairer world economy

38. When the leaders of the G20 gathered in November 2008 and in April this year, the outlook for the world economy was particularly bleak. The OECD credits the agreements and declarations issued at these summits with helping to begin the process of restoring confidence, and it supports the G20 pledges to restore confidence, growth and jobs, to strengthen the financial system, promote global trade and investment and to reject protectionism, so building an inclusive and sustainable recovery for all. Indeed the OECD has been closely involved in framing the response to the crisis and helping to shape the global economy that emerges from it, not only at the various meetings of the G20 but also at its own Ministerial Council Meeting held in Paris on 24-25 June 2009 and at the G8 held in Italy in July. The OECD is continuing to work on challenges to transform the current policy-driven recovery into self-sustained growth, with its Strategic Response presently focussing on six pillars: (i) Short term assessment and exit strategies, (ii) Long term growth (including fiscal sustainability and assessment of stimulus packages, innovation, SMEs and green growth), (iii) Employment and social issues, (iv) Market openness, (v) Finance, competition and governance, and (vi) Development issues. These are also key priorities expected to be at the centre of G20 Leaders' discussions in which the OECD has been invited to take part.

39. The OECD believes that reforms need to ensure that such a crisis cannot recur, but without stifling the ability of markets to raise, allocate and measure the success of capital, on which so much of recent world prosperity has depended. It believes that emergency measures taken so far should be kept under review so as to monitor their contribution to stabilisation and a balanced, sustainable recovery. The distorting potential of government-sponsored enterprises and guarantees should also be monitored and adjusted as necessary so

5. See Alejandro Foxley, *Recovery : The Global Financial Crisis and Middle-Income Countries*, Carnegie Endowment for International Peace, Washington, D.C., 2009.

as not to impede the recovery of markets. Past financial crisis have indeed told us that recoveries were delayed when competition enforcement was relaxed. The OECD sees several overall priority areas for governments and regulatory bodies.

- To bring the lingering financial crisis to an end, restoring market confidence and enabling bank lending. This is likely to mean removing toxic assets and promoting bank recapitalisation, even, if necessary, via temporary nationalisation.
- For those countries that can prudently do so, to continue monetary and fiscal stimulus as long as the recovery has not taken hold.
- Avoid disguised protectionism in the form of support and subsidy to domestic enterprises.
- Once recovery is secured, authorities will need to act swiftly and decisively to reverse many of the emergency measures that have been taken.

40. In December 2008, the OECD launched its *Strategic Response to the Financial and Economic Crisis*, which was fed into the G20's work. This has been revised since and a detailed report on this strategy was presented to the OECD Ministerial Council Meeting in June. Here are some of the key points from the report synthesis:⁶

41. The OECD acknowledges that "the response to the crisis has been impressive for its magnitude, intensity and degree of global co-ordination". The crisis "has also confirmed the need to involve all major players in global economic governance. However, these are only the first steps of a process towards a more sustainable global economy. More needs to be done and the emphasis must shift to a medium- to long-term perspective. The global economy must move from a policy driven recovery to self sustained growth. Just as important is the need to tackle the consequences of rising unemployment which could yet turn the economic crisis into a major social crisis."

42. The OECD believes that "once the recession is over, the global economy should not go back to business as usual, as past practices have proven to be unsustainable. Governments must already begin to address the issue of how to exit from the exceptional measures they have taken, on several fronts, to face the crisis. To do so, they will have to ask not only how or when to exit, but also towards what to exit." The OECD sees the post-crisis global economy in terms of growth that is:

Stronger...

43. There should be "better regulation of financial markets, a healthy balance between markets and government, and policies to promote more innovative long-term growth in a more balanced global economy. Global imbalances should not be allowed to widen as in the past. Addressing them requires looking at both a macroeconomic and a structural dimension. Excess investment over savings in some countries also reflects excessive debt issuance. And, excessive savings in others reflect a high degree of risk aversion due to the lack of adequate social protection. A sustainable growth environment requires addressing these underlying factors in the global distribution of saving and investment. This in turn requires structural and medium term policy action in addition to macroeconomic adjustment to be undertaken in a co-ordinated framework."

Cleaner...

44. "The crisis offers the opportunity to put the global economy onto a low carbon growth path, in line with ongoing efforts to mitigate climate change. Governments should seek out "win-win" opportunities that are good for both economic recovery and for the environment. Growth going forward should also be smart and more knowledge-intensive. To be sustainable and equitable, it must also be supported by a transparent environment with strong co-ordinated initiatives to fight corruption, tax evasion, bank secrecy, and promote more transparency and a level playing field in investment."

And fairer...

45. There should be "more effective trade, investment, and development policies, strong social frameworks and a common global governance structure based on co-operation between developed emerging and developing countries with more opportunity and less inequality. Open markets remain a fundamental principle of well-functioning economies. The dramatic, generalised and very rapid fall in trade, if not reversed, undermines the activity of dynamic firms that operate in the tradable sectors, where productivity growth is

6. OECD, Synthesis report on the strategic response, 5 June 2009, C/MIN (2009)9.

higher, with potentially disruptive consequences on the global value chains. Open markets remain a key driver of growth as well as of innovation diffusion. Protectionism would be a very serious mistake. The poor and the most exposed to the risk of exclusion should not be left out. Growth must be socially sustainable and based on increasing employment. Unemployment breeds poverty and curtails long term growth. Social pressure caused by rising unemployment could exacerbate protectionist pressures.”

Finance, competition and governance: priorities for reform and strategies to phase out emergency measures⁷

46. The OECD says that in order to restore public confidence in financial markets incentives should be put in place to encourage a prudent balance between risk and the search for return in banks and other financial institutions. Allowing for variations between countries, urgent strategic priorities for policy reforms include streamlining the regulatory framework, emphasising prudential and business conduct rules and strengthening incentives for their enforcement; stressing the integrity and transparency of markets, including disclosure and protection against fraud; reforming capital regulations to ensure much more capital at risk (and less leverage) in the system than in the past; avoiding impediments to international investment flows; strengthening governance of financial institutions and ensuring accountability to owners and creditors with capital at risk, and, once the crisis has passed, allowing people with capital at risk, including large creditors, to lose money when they make mistakes; strengthening understanding of how tax policies affect the soundness of financial markets; and improving education and consumer protection programmes.

47. The OECD rightly points out that, while stabilizing the economic and financial situation will take time, once this occurs governments should begin the process of exit from the unusual support measures taken in tackling the crisis. As recovery will be fragile, it should not be jeopardised by a precipitous withdrawal of support measures. Getting the exit process right will be more important than speed, the OECD says. Again, clear guiding principles should be established early on. For example, the time-line for exit (including a full sell down in government voting shares) should be conditional in part on progress with regulatory reforms such as those mentioned above. Level competitive playing fields should be re-established and support eventually withdrawn. Viable firms restored to health should be expected to operate on a competitive basis in the market place. Support should not be withdrawn precipitously but should be priced on an increasingly realistic basis. As adequate pools of equity capital become available, state-owned or controlled financial firms should be privatised. The bad assets and associated collateral that remains in governments' hands should be managed with a view toward recovering as much for the taxpayer as is feasible over the medium term. Public confidence in private pension systems and their financial soundness should be reinforced.

Public governance challenges

48. The nature of the current financial and economic crisis highlights on a global scale the unique role of government in serving the public interest and directs renewed attention towards the institutions, policies and tools that help governments deliver what citizens and businesses need and expect. With government revenues falling due to the economic downturn and public expenditures rising given greater public investment, there is less money available for other government spending. This often impacts the national and sub-national capacity to provide public goods and services. Meanwhile, higher unemployment levels and scarce job opportunities increase demand for a variety of public services, including unemployment welfare benefits, labour adjustment programmes, education (e.g. retraining and skills improvements), health care, etc. As a result, attention is turning to the role of the public sector and the value for money it offers. The quality, flexibility and effectiveness of the public governance systems within a country are central to how rapidly and satisfactorily administrations can move to implement necessary changes or advance reform programmes in order to meet such needs. However, through work undertaken for the OECD's *Government at a Glance* it has become increasingly evident that countries struggle with this issue.

49. While the main cause of the current financial and economic crisis was the failure of the financial markets, regulatory gaps, and lack of transparency coupled with poor levels of integrity also played a part. Governance issues is not a phenomenon solely driven by the current crisis and many OECD countries have advanced work in developing and revising their governance institutions, frameworks or tools as part of broad reform and changed agendas. Thus, the fallout of the current economic crisis has largely acted to shine a spotlight on aspects of governance or governmental institutions where further changes may be needed, or where additional consideration may be required on how best to give real effect to reform efforts. The OECD's *Public Governance Reviews*, while still at an early stage, have demonstrated the links between strategic

7. See Finance, competition and governance: priorities for reform and strategies to phase out emergency measures [C/MIN(2009)9/ANN1].

planning, institutional arrangements, tools, and capacity to ensure the smooth functioning of a country's public governance frameworks (institutions, public management, public administration) and sustainability of public administrations. These comprehensive reviews help countries assess how their institutional frameworks and governance arrangements are performing from an international comparative perspective, in terms of: their ability to deliver on government objectives, in particular from a whole-of-government perspective; and their preparedness to meet current and future challenges.

50. A clean recovery needs to proactively promote a level playing field and fair competition in government contracting. In addressing these issues enhanced transparency, good management, accountability and control throughout the entire procurement cycle—from the definition of needs to bidding, contract management and payment—is crucial. Actions taken today will have a lasting impact as public funds are used to renew public infrastructure and invest in new technologies in the future. To restore and maintain confidence, governments are expected to prove their accountability for every cent of taxpayers' money spent as part of the stimulus packages. The OECD Principles for Enhancing Integrity in Public Procurement, approved in the form of a Recommendation in October 2008, provides a policy instrument to guide governments in preventing waste, fraud and corruption in public procurement. In 2011, OECD countries will report on progress made in implementing this Recommendation.

Maintaining open trade and investment⁸

51. The OECD warns that although governments have largely resisted protectionist pressures so far, the dangers of trade and investment protectionism call for continued vigilance. Many governments have adopted measures to earmark public investment and subsidies for specific sectors. Under some programmes, they attach conditions that may discourage either trade, particularly imports, or investment flows. If such measures are not carefully designed, there is a risk of a drift toward discriminatory policies that could prejudice a return to sustainable growth.

52. Trade agreements and OECD investment instruments allow governments a certain flexibility when responding to crises. However, they also require that such measures should not unduly damage other countries' interests.

53. Meanwhile, multilateral trade negotiations remain stalled. The OECD urges countries to strengthen their efforts to conclude the Doha Development Agenda in 2009 not only for the benefit of the developing world but also for the systemic health of the global economy.

54. As far as preserving freedom of investment is concerned, the challenge is for governments to use their crisis response powers to address economic and social problems while minimising barriers to inward and outward foreign investment.

Aligning stimulus measures with long term growth

55. The OECD emphasises that governments' macroeconomic and structural policies should be consistent with three broad objectives: supporting high potential growth, avoiding unsustainable payment imbalances, and ensuring fiscal sustainability. The timing and composition of fiscal stimulus measures should be aligned with these objectives.

56. The OECD reminds us that the need for additional discretionary fiscal stimulus varies across countries because automatic stabilizers (e.g. unemployment benefit) operate more powerfully in some economies. In this context, the biggest constraint on introducing additional fiscal stimulus is the reaction of financial markets to greater government borrowing needs.

57. The OECD makes a number of recommendations on stimulus packages.⁹ First, crisis measures should not be allowed to undermine competition. Secondly, action should be co-ordinated in order to allow it to generate a larger overall output effect than if any country acted alone. Thirdly, the OECD again underlines that many of the emergency measures taken could pose a threat to long-term growth and sustainability if not properly unwound. Measures should be temporary and the least distortive possible, with a clear and credible plan for phasing them out (exit strategies) as recovery takes hold. Fourth, governments should announce a clear commitment to long term fiscal sustainability in order to strengthen the credibility of the medium term fiscal framework. Fifth, credible fiscal consolidation plans may require tax reforms, including the broadening of tax bases and better tax compliance to ensure sustainable revenues. Indeed, as economies emerge from

8. See Keeping markets open for trade and investment: issues for discussion [C/MIN(2009)4].

9. See Aligning stimulus measures with long-term growth [C/MIN(2009)9/ANN2].

recession, it is likely to be necessary to raise additional revenues, and permanent cuts in expenditure will have to be implemented. Two further important OECD policy recommendations are the need to focus on “double-dividend” measures (which can at the same time support the economy in the short-term and boost potential output in the long-term); and the necessity to improve spending efficiency.

Tax measures

58. In the OECD’s view, growth-oriented tax reforms should usually involve shifting revenue from corporate and personal income taxation or social security contributions to consumption and property taxes, including housing taxation. However, any tax policy would need to take account of its impact on income distribution, given that the poor should have particular consideration during an economic recession. Tax cuts that benefit workers with modest incomes can improve living standards by increasing their disposable income and giving them a greater incentive to work.

Labour, social and education measures

59. The OECD believes that subsidy schemes designed to expand labour demand should be temporary and well targeted, while early retirement options should be avoided. Countries with weak unemployment benefit systems may wish to consider extending their coverage and the maximum length of their benefit schemes during the recession. Expanding effective active labour market programmes would be important to maintain the activation stance. But it may be difficult to match the rise in job seekers with greater resources for public employment services, not least because it takes time to recruit and train good case managers. Thus, there may be opportunities for co-operation between public and private employment agencies to provide a range of contracted-out activation services.

60. Macro-economic responses by governments are vital, but action is also needed at the local level to tackle job losses and return economies to prosperity. Strategic thinking is required locally to provide foundations for the creation of sustainable employment which provides opportunities for progression and accessibility. There should be a better integration between labour market policy, training and economic development. Public programmes must be made sufficiently flexible so that they can be targeted to relevant groups and adapted to local conditions. Stronger emphasis is required on building local intelligence to inform policy implementation.

61. There should also be support for education and training that enables the transition to new jobs and emerging opportunities, as well as policies to help young people in their transition from school to work. Migrants should be fully integrated into the labour market components of stimulus packages. In this regard, the OECD Labour and Employment Ministerial Conference of 28-29 September 2009 represents a key opportunity to discuss how labour market and social policies can best help workers and low-income households weather the storm of the current jobs crisis.

Pensions

62. In view of their vulnerability, pensions could be part of economic stimulus packages. The OECD recommends that governments should strengthen safety nets to prevent increased old-age poverty, that there could be different investment portfolios and shift to riskier assets near retirement in private (defined-contribution) plans, while longer periods could be allowed for employer (defined-benefit) pension funds to recover.

63. The OECD reminds governments that they should not resort to early retirement or disability schemes in an attempt to stem the increase in unemployment. On the contrary, some countries propose to raise the pension age to help pension-scheme finances.

Infrastructure investment

64. According to OECD, most economic stimulus packages focus on improving the national infrastructure, mostly through public works. Such infrastructure includes roads, railways, public transport, airports, water and sanitation, child-care facilities, schools and universities, hospitals, energy networks and security, and broadband communication infrastructure. Infrastructure projects should consider taking account of such principles as the following:

- Projects should be advanced enough in planning to be implemented quickly and effectively in a period of crisis. Priority should be given to modern projects with the most potential to raise the efficiency of energy and resource use, and which support long-term environmental sustainability.

- Investment in high speed broadband communication networks should be accompanied by regulatory frameworks which support open access and competition in the market. Such investment should also aim at stimulating the use of ICT to secure economic and social benefits such as training and job searching.
- Spending should mobilise idle resources, especially vulnerable groups at greater risk of falling into the unemployment trap such as relatively unskilled young people, women and older workers.

Green growth

65. One of the OECD's main messages for ending the crisis is that of "green growth", which was the object of a special declaration adopted by OECD Ministers on 25 June.¹⁰ The essence of this message is that economic growth and environmental goals, e.g. reducing greenhouse gas emissions, can and should go hand-in-hand. Thus there are opportunities for mutually reinforcing policies in pursuit of both objectives in the long-term. For example: (i) green tax reform (shifting the tax base away from labour and capital towards pollutants or polluting activities) and auctioned pollution permits that generate revenues - they are good for the environment and also contribute towards the goal of fiscal sustainability; (ii) reforming or removing inefficient policies, especially subsidies to fossil fuel production and consumption - with the added benefits of removing inefficiency in resource allocation in the economy, pushing the green agenda and saving governments and tax payers money; and (iii) removing barriers (e.g. market and information failure) to greater energy and transport efficiency.

66. In addition, many of the "green" investments in infrastructure in the stimulus packages are directed towards increasing public investments in energy efficiency of buildings, public transport, renewable energy networks, more efficient water treatment supply and sanitation, as well as infrastructure to prevent flooding, and other environmental risks and degradation. These can contribute to increased environmental quality, and seize the opportunity of the crisis to spur public infrastructure investment to contribute a low carbon economy. Meanwhile, some elements in stimulus packages, such as new road building and auto-scrapping programmes, might be carefully assessed for their potentially negative environmental impacts.

Promoting innovation

67. The OECD, which is developing an Innovation Strategy for the 21st Century,¹¹ points out that the crisis has already had a negative impact on innovation through its effects on investment, finance, trade, entrepreneurship and employment.¹² R&D expenditure by businesses as well as patent applications have moved in parallel with GDP, slowing considerably during the economic downturns of the early 1990s and early 2000s.

68. Innovation, says the OECD, is one of the keys to coming out of the recession and putting countries back on a path to sustainable growth. Many governments have incorporated measures to strengthen innovation in their stimulus packages, and could also take further action to improve their long-term potential for innovation.

69. The crisis has highlighted widely acknowledged market failures in the financing of innovation. Such investment is now considered even more risky than before and some of the longer term investment in new technologies has been particularly affected. Moreover, stimulus measures offer an opportunity to put available resources for innovation (notably skilled labour) to good use.

70. In supporting private investment in innovation, the OECD warns that care should be taken to ensure that government spending provides good value for money; the less promising innovation projects are typically abandoned first by the private sector and the OECD sees no reason to revive these with public money. The OECD advises that policies in this context could include focusing public support on research and innovation most affected by the crisis; better use of public-private partnerships; encouraging investment in research infrastructure, which can contribute both to stimulating demand in the short term and supply in the longer term; and using open and competitive public procurement to support R&D, especially where it contributes to solving social challenges.

10. Declaration on Green Growth, 25 June 2009, C/MIN(2009)5/ADD1/FINAL.

11. See Interim Report on the OECD Innovation Strategy.

12. See Fostering innovation for sustainable growth [C/MIN(2009)9/ANN3].

71. Governments also need to focus on medium to long-term actions to strengthen innovation. As discussed in the OECD's Interim Report on the Innovation Strategy, a broad range of policy reforms will be needed in OECD countries to respond to the changing nature of the innovation process and strengthen innovation performance to foster sustainable growth and address key global challenges.

Entrepreneurship and industrial renewal

72. The OECD also advises that in changing their approaches to innovation, governments should also consider how best to support risk-taking, such as investment in innovative start-up companies. Regulatory reform of financial markets to address the financial crisis could look at the role of venture capital markets and the securitisation of innovation-related assets (e.g. intellectual property) which are key sources of financing for many innovative start-ups. Moreover, new business opportunities and the reallocation of resources from declining activities towards emerging opportunities are vital to recovery. The OECD points out that governments will need to avoid locking-in old economic structures and business models. Governments can prepare for the next phase of innovation-led productivity growth by encouraging the entry and expansion of new businesses or the exit or re-orientation of existing businesses facing difficulties. SMEs are playing an increasing role in R&D, chiefly at the local level. More attention needs to be devoted to identifying and fomenting entrepreneurship skills linked to innovation processes.

SME and Entrepreneurship Financing

73. The OECD points out that access to financing continues to be one of the most significant challenges for the creation, survival and growth of Small and Medium-sized Enterprises.¹³ The problem has been strongly exacerbated by the financial and economic crisis.

74. The OECD therefore advances a number of policy recommendations designed to tackle long-standing deficiencies in the SME financial environment by, for example, strengthening their relationships with banks, improving their access to micro-finance, improving SMEs' and entrepreneurs' information and competencies in the field of finance; improving knowledge of the situation of SMEs and entrepreneurs' financing; exploring ways to facilitate the establishment of "business angel networks" which may greatly enhance information and capital flows; increasing entrepreneurs and SMEs' involvement in relevant finance-related policies and programmes from the outset to ensure that their perspectives and needs are well understood and taken into account.

4.2. Countering tax evasion and corruption

75. As was pointed out by OECD officials during the meeting of the PACE Committee on Economic Affairs and Development on 19 June 2009, although tax havens were not the cause of the financial crisis, their effect is to divert tax revenue from the governments of the countries where the income or savings arises. In an effort to protect public finances and financial systems, the G20 Summit in London on 2 April 2009 agreed to transparency and exchange of information, and to "take action against non-co-operative jurisdictions". The OECD defines a tax haven in terms of specific criteria as follows:

"Four key factors are used to determine whether a jurisdiction is a tax haven. The first is that the jurisdiction imposes no or only nominal taxes. The no or nominal tax criterion is not sufficient, by itself, to result in characterisation as a tax haven. The OECD recognises that every jurisdiction has a right to determine whether to impose direct taxes and, if so, to determine the appropriate tax rate. An analysis of the other key factors is needed for a jurisdiction to be considered a tax haven. The three other factors to be considered are:

- Whether there is a lack of transparency*
- Whether there are laws or administrative practices that prevent the effective exchange of information for tax purposes with other governments on taxpayers benefiting from the no or nominal taxation.*
- Whether there is an absence of a requirement that the activity be substantial.*

"Transparency ensures that there is an open and consistent application of tax laws among similarly situated taxpayers and that information needed by tax authorities to determine a taxpayer's correct tax liability is available (e.g., accounting records and underlying documentation).

13. See The Impact of the Global Crisis on SME and Entrepreneurship Financing and Policy Responses [C/MIN(2009)9/ANN5].

“With regard to exchange of information in tax matters, the OECD encourages countries to adopt information exchange on an “upon request” basis. Exchange of information upon request describes a situation where a competent authority of one country asks the competent authority of another country for specific information in connection with a specific tax inquiry, generally under the authority of a bilateral exchange arrangement between the two countries. An essential element of exchange of information is the implementation of appropriate safeguards to ensure adequate protection of taxpayers’ rights and the confidentiality of their tax affairs.

“The no substantial activities criterion was included in the 1998 Report as a criterion for identifying tax havens because the lack of such activities suggests that a jurisdiction may be attempting to attract investment and transactions that are purely tax driven. In 2001, the OECD’s Committee on Fiscal Affairs agreed that this criterion would not be used to determine whether a tax haven was co-operative or unco-operative.”¹⁴

76. Over recent years, the OECD has led the way in setting, and finding agreement for, international standards on the exchange of information for tax purposes. These standards, which were developed by OECD and non-OECD countries in the context of the OECD’s Global Forum on Taxation, were endorsed by G20 Finance Ministers in 2004 and by the United Nations Committee of Experts on International Co-operation in Tax Matters in October 2008. Essentially, they require exchange of information on request in all tax matters for the enforcement of domestic law, without regard to bank secrecy. At the same time, they create safeguards to protect the confidentiality of the information exchanged.

77. At their Ministerial Council Meeting on 24-25 June 2009, the Ministers “welcomed the near universal endorsement of the principles of transparency and effective exchange of information on tax matters developed by the OECD. We look forward to a strengthening of the Global Forum on Transparency and Exchange of Information including the expansion of its membership. We support the establishment of a robust and comprehensive peer review process within the Global Forum and the development of a toolbox on defensive measures to ensure an effective implementation of agreed standards and instruments on a global basis.”¹⁵

78. As was emphasised by members of the PACE Committee on Economic Affairs and Development at their meeting on 19 June, it should be made quite clear that in the exchange of tax information there should be respect for normal bank confidentiality – only in cases of tax evasion and criminal activity could it be lifted.

79. Following the London Summit, according to the OECD’s Secretary-General, “more was achieved to improve transparency in two or three weeks than in the last decade”, with tax agreements signed and commitments made by jurisdictions around the world, including the Cayman Islands, Costa Rica, Macao, China, the Philippines, Switzerland and Uruguay. The OECD has been charged with monitoring compliance, and its Secretary-General has pledged to “watch like a hawk” to ensure that commitments are followed up with legislative and administrative action. However, some have questioned the effectiveness of such international tax agreements, pointing out that they have given rise to very few information requests because it is so hard to determine the real ownership of accounts hidden by trust arrangements, for example.¹⁶

80. Nevertheless, the OECD sees the existence of its comprehensively-designed international standard as crucial to success in global policy, and believes that this can be a model for progress on integrity and transparency in other areas. Accordingly, it is intensifying its work with partner organisations to identify standards and instruments which can help to strengthen the global regulatory framework. This is why the OECD is pleading in favour of the rapid updating of the joint OECD-Council of Europe Convention on Mutual Administrative Assistance in Tax Matters (ETS No. 127), and the rapporteur strongly supports this.

81. Tax policy is also increasingly featuring alongside aid issues – in fact, the OECD has called this the “new frontier” in international development. The role of tax havens in reducing revenues for developing countries has come under scrutiny, as efforts to tackle cross-border tax evasion have gathered pace worldwide. The OECD believes that donors should support a strengthening of developing countries’ tax systems and administrations through specially-targeted aid. And for their part, developing countries need to show that such initiatives can be effective, by battling tax avoidance and bearing down on corruption.

14. OECD website.

15. OECD 2009 Ministerial Conclusions, 25 June 2009, C/MIN(2009)5/FINAL.

16. See Richard Murphy, founder of the Tax Justice Network and Director of Tax Research LLP, at <http://www.financialtaskforce.org/2009/08/10/the-oecd-meeting-1-2-september-2009/>

82. Last year, the OECD celebrated the tenth anniversary of the entry into force of its landmark Convention on Combating Bribery of Foreign Public officials in International Business Transactions. So far 38 countries, all 30 OECD member countries plus Argentina, Brazil, Bulgaria, Chile, Estonia, Israel, Slovenia and South Africa, have joined the Convention, which creates a strong basis for supporting member countries' efforts to prevent and repress bribery and corruption through stringent standards and an effective peer review mechanism.

4.3. Fostering development assistance

83. Like the rest of the world, developing countries have been hit by restricted credit markets and curtailed international investment, falling trade and lower commodity prices, but they even more vulnerable to the knock-on effects of the global crisis, such as lower remittance payments from overseas workers and the threat of local conflict, as competition for resources grows. In previous years, this report has regularly discussed the work of the OECD's Development Assistance Committee (DAC), particularly in the fields of co-operation, knowledge transfer and the measurement of aid effectiveness. In its 2009 report, the DAC takes stock of the current situation, and calls upon the international community to retain its commitment to fighting poverty and encouraging sustainable development.¹⁷

84. Overall, in 2008 aid was at the highest levels ever recorded, in dollar terms. The DAC's latest figures show an increase of 10% in real terms in 2008, with an increase of 11% currently projected over the next two years to 2010. The current outlook suggests that at least USD 10-15 billion must still be added to current forward spending plans if donors are to meet their current 2010 commitments which imply an ODA level of USD 121 (expressed in 2004 dollars). Some recent signs of a decline in net aid suggest the risk of this shortfall increasing. To address this, the OECD Secretary-General has launched an "Aid Pledge", and received commitments from DAC members to uphold their aid plans. Moreover, donors are being urged to advance their forward spending, and with the World Bank and IMF estimating that the global crisis calls for additional aid provision of about \$25 billion, this is all the more important. With programmed debt relief set to decline, the report points out that other forms of aid will need to rise substantially if targets are to be met.

85. Of course, the way aid is given and spent is as critical as the totals. In September 2008, 130 countries took part in the Third High Level Forum on Aid Effectiveness in Accra. They launched the Accra Agenda for Action, whereby donors undertook to make aid more predictable, while recipients pledged to boost their own financial and budgetary systems, and improve transparency. Success in these commitments will be increasingly significant, since the level of aid channelled directly through the budgets of developing countries is likely to rise in the next few years.

86. At the same time, donors still need to address the amount of politically-motivated and "tied" aid they offer, as well as reducing duplication and waste. Globally, there are now about 225 bilateral and 242 multilateral agencies, funding over 35,000 activities per year. Indeed, fragmentation is a major challenge and the more partner countries that have to deal with a large number of donors that provide a small share of aid, fragmentation is then significant: the 2009 Development Co-operation Report points out that 32 recipient countries had to deal with 15 to 23 donors which together represented less than 10% of the total aid provided to these countries. If aid was provided more coherently, the transaction costs involved would be substantially reduced, for both donors and recipients.

87. In other words, as the report points out, effective global governance is more important than ever in development aid. All parties need to take responsibility in coordinating and focusing their efforts, and the report offers five key principles that should be respected in line with the *Paris Declaration on Aid Effectiveness* (2005) and the *Accra Agenda for Action* (2008): developing countries should set their own development strategies, improve their institutions and tackle corruption; donor countries bring their support into line with these objectives and use local systems; donor countries should co-ordinate their action, simplify procedures and share information to avoid duplication; developing countries and donors should focus on producing, and measuring, results for the sake of efficiency; and donors and developing country partners should be mutually accountable for development results.

88. On 27-28 May 2009, the OECD DAC adopted an Action Plan to support poor countries trying to cope with the effects of the financial and economic crisis. Despite progress, notably with the US Administration's promise to double its foreign assistance over the next five years, many donor countries were unlikely to meet their commitments and the DAC determined that only renewed efforts could bring the collective performance back onto target. With the Action Plan, DAC members agreed to help developing countries by reaffirming their existing ODA commitments, especially with regard to Africa; by helping low-income countries finance both

17. OECD/DAC, Development Co-operation Report 2009.

short and long term priorities; by making the most effective possible use of aid; by financing international financial institutions in a timely and predictable manner; and by tackling the crisis using all policy instruments available, not just official aid.

89. Last year's report to the Assembly provided information on the joint OECD/WTO Aid-for-Trade Initiative, launched in 2005, the aim of which is to help low-income countries develop the capacity, whether in terms of policies, institutions or infrastructure, to exploit the opportunities that the global trading system has to offer. The second monitoring report on Aid for Trade, published in July 2009, shows that this initiative has been a success. Thus aid for trade flows have increased by over 20% in real terms between 2005 and 2007. Total new concessional commitments that fall into this category reached more than US \$25 billion in 2007, and preliminary data for 2008 were good but it is not yet possible to say whether this momentum has been maintained in the face of the crisis.

4.4. "Going for growth": an update

90. This year's "Going for Growth" includes special chapters on infrastructure, taxation, market regulation, and population structure. As OECD Secretary General Angel Gurría said on launching the publication, "the report is a critical part of the OECD's response to the crisis."

91. One of the main themes is how best to boost labour productivity and labour use, especially over the long term. Looking in depth at countries' performance and policies, the OECD identifies five structural policy priorities for each one – and for the European Union as a single economic unit. These priorities may change over the years, as countries implement reforms and new issues develop. They mainly relate to labour and product markets, but also to other areas, notably education, health and innovation, said Mr Gurría.

92. The Secretary General said that "Going for Growth" identifies policies aimed at increasing labour productivity for all OECD countries and the European Union. Reforms to strengthen human capital are identified as a priority for most countries, as are reforms to strengthen competition in product markets, particularly by reducing entry barriers. Reforms of agricultural policies are also called for in the United States, the European Union and Japan, as well as in a few other countries with particularly high support levels.

93. Policies for increasing labour utilisation are recommended in nearly all OECD members, he continued. While reforms of tax and benefit schemes are identified as necessary in most OECD countries in Europe, reforms of the health care systems are recommended in the United States and New Zealand. Reforms of labour markets are also identified as a priority for the European Union, as well as in Japan, Korea and Turkey.

94. "With the exception of a few specific areas, such as financial regulation, where there has been major re-thinking," said Mr Gurría, "the policy priorities identified in this edition are broadly similar to those of our previous edition. Indeed, 86% of each OECD country's priorities have been retained fully or in part. This is not encouraging, although these policies sometimes need time to show their impact. We, the OECD, and our Member countries must do better. Of the 14% remaining priorities, which actually changed, less than two-thirds were replaced as a result of reforms undertaken; while the remaining ones were changed based on a re-consideration of newly available evidence. Thus, while the results of this exercise reflect modest reform progress, they clearly imply that much reform work is still pending."

95. Former OECD Chief Economist Klaus Schmidt-Hebbel pointed out that among other things, the study "shows that a significant proportion of the cross-country difference in employment rates and average productivity levels, and thus GDP per capita, is accounted for by differences in population structure, in particular educational attainment. It re-emphasises the importance of education, especially in the long run."

96. The report concludes, said Schmidt-Hebbel, with the very important message that "the economic crisis facing OECD countries should not be allowed to slow down structural reforms. Opportunities for reforms should be exploited to strengthen economic dynamism and living standards. Under no circumstances should mistakes from previous crises be repeated. In particular, attempts to cut unemployment by reducing labour supply would prove as damaging as in the past and leave our societies poorer. State subsidies to particular industries and firms should be kept to a minimum. Keeping external markets open and avoiding new protectionism is key to strengthening prosperity throughout the world."

97. The rapporteur agrees with Mr Gurría that "If the opportunity is seized to make lasting reforms that will improve long-term economic performance, we may look back at this period as one where we repositioned our economies to achieve stronger, cleaner and fairer growth."

4.5. The energy and climate change issue

98. The International Energy Agency (IEA), an institution that is part of the OECD framework, works to forecast energy needs and promote rational energy policies. In the rapporteur's talks with its officials, she noted, and endorses, the IEA's call for massive investment in energy infrastructure to maintain long-term energy supply, not only in oil and gas but especially in non-fossil fuel alternatives; for increasing energy efficiency; and for maximising energy security through diversification of the energy mix.

99. Henceforth the energy issue cannot be dissociated from that of the environment, and the OECD believes, on the basis of its analyses of the effects of carbon emissions on climate change in line with those of the United Nations Intergovernmental Panel on Climate Change and those of the Nuclear Energy Agency, that "nuclear energy is the only virtually carbon-free technology with the proven track record on the scale required" to meet emission targets.¹⁸ The recent PACE debate on nuclear energy, and the resulting resolution, certainly took a cautiously positive view, while emphasising the heavy responsibilities incumbent on governments pursuing this path. As the OECD puts it, these include "maintaining continued, effective safety regulation; ensuring the maintenance of the skills base, fostering progress on facilities for waste disposal; maintaining and reinforcing international non-proliferation arrangements; and providing the regulatory, policy and fiscal stability that investors require."¹⁹

100. The two-year OECD project on the Economics of Climate Change mitigation confirms that tackling climate change should not be delayed, and that ambitious action to reduce greenhouse gas (GHG) emissions is economically rational. The economic crisis provides no room for complacency. At most, it might slightly reduce global emissions temporarily, after which an upward trend will resume. Delaying action on climate change would only necessitate larger cuts later.

101. Ambitious mitigation goals should be achieved through a policy mix, with an emphasis on price-based instruments. To build support for action, countries need to use least cost policies to achieve significant emission cuts. To keep the costs low, the policy mix should include a strong emphasis on putting a price on GHG emissions, e.g. through cap-and-trade schemes, to discourage the behaviour that generates emissions and encourage emitters to seek abatement options wherever they are cheapest. But no single instrument will be sufficient to tackle the wide range of sources and sectors emitting GHGs. Given market and information barriers, price instruments will need to be complemented by standards (e.g. building codes, electric appliance standards) and measures to boost innovation and facilitate the uptake of cleaner technologies.

102. Pricing carbon will lead to additional financing flows for clean technologies, and can be a critical spur for the deployment of new technologies. Thus, OECD analysis finds that a carbon price path consistent with achieving a stabilisation of greenhouse gas concentrations at a safe level could lead to a four-fold increase in world energy R&D spending by 2050. At the same time, major new breakthroughs will be needed to bring down the costs of climate action over the long-term, and the private sector is unlikely to invest sufficiently in R&D given the gap between the social and private expected returns from these investments. As such, government has an important role to play in supporting R&D, including to reverse the dramatic trend in declining public energy-related R&D expenditure that has been occurring in OECD countries since the early-1980s.

4.6. Measuring the progress of societies

103. Gross domestic product (GDP) came to represent the standard, almost universally accepted measure of the progress of societies. But recent years have seen a growing debate about the need for new measures of progress that complement GDP to include social and environmental information. Thanks to pioneering work by the OECD in conjunction with other bodies including the European Commission and the Council of Europe, this concept is being revised. The point is that GDP does not reflect many factors that are important in people's lives nor progress towards the sustainability of our societies that is essential to their survival. There is now a growing movement to discuss what constitutes progress in society and how it should be measured. A milestone in the OECD-hosted Global Project on "Measuring the progress of societies" will be the 3rd OECD World Forum, to be held in Busan, Korea, on 27-30 October 2009. The PACE Committee on Economic Affairs and Development hopes to be represented at that Forum in order to present the report on *Wealth, Welfare and Wellbeing: how to reconcile them in a changing Europe* being prepared by Mr Constantinos Vrettos.

18. OECD, The crisis and beyond: building a stronger, cleaner and fairer world economy. Key information for the meeting of the OECD Ministerial Council 2009.

19. *Ibid.*

104. The rapporteur believes that the OECD is well suited to such visionary and in-depth thinking and would encourage the Organisation to reflect further on such issues as the nature and operation of today's market economy and of financial markets, the implications of government ownership of the means of production, and the nature of an economic and financial system based on sound and sustainable principles.

5. Prospects for OECD enlargement

105. Tackling the financial and economic crisis has clearly shown the need for enhanced co-operation and involvement in decision-making of the widest possible circle of governments affected and able to contribute to solutions. That is why it is so important that the OECD launched, already in 2007, accession negotiations with five countries: Chile, Estonia, Israel, Russia and Slovenia, and a process of "enhanced engagement" with a view to possible membership with five others: Brazil, China, India, Indonesia and South Africa. These countries already take part in many OECD activities, including the 2009 Ministerial Council Meeting, and the purpose is clearly to "strengthen the Organisation's relevance as a global hub for economic dialogue".²⁰

106. The accession process begins with the submission of an initial memorandum by the candidate country followed by an accession review conducted by various OECD bodies. These are all well under way with the exception of Russia, which submitted its memorandum during the June 2009 Ministerial Council Meeting. In that connection, OECD officials have warned that trade liberalisation commitments might be a stumbling block, as they are for Russia's accession to the World Trade Organization.

107. The rapporteur would like to emphasise once again, as the enlarged Assembly pointed out in its resolution on the OECD and the world economy last year, that full respect for democracy, human rights and the rule of law, including international law, should constitute an essential criterion for judging whether a candidate country should be invited to join the OECD.

6. Concluding remarks

108. In making the case for both addressing today's systemic failures and embarking on policies for long-term growth, the OECD is directly addressing concerns regarding the economic and social implications of the most severe recession in recent times. Many questions of ethics and transparency have been raised, and while these may not be the direct cause of the crisis, they are perceived to be inextricably linked to it. This year's G8 presidency is promoting a worldwide "Legal Standard", while Chancellor Merkel has proposed a "Global Charter" for sustainable growth. Both are part of an important effort to avoid a backlash against open markets, and this deserves support. As the OECD's Secretary-General says, "Economically, it makes sense. Politically, it seems inevitable".

109. The OECD feels that it can play a crucial role in this. Over the last 15 years, it has worked with governments and institutions to develop a comprehensive range of policy rules. Whether legally binding, in the form of soft law or as policy recommendations, they provide best practices for designing and carrying out sound policies and they also offer guidelines for the conduct of global business. Up till now, they have operated in separate and individual contexts, but by bringing them together, in a systematic and coherent manner, and working together with sector-specific partners such as the IMF, WTO and ILO, such provisions could turn out to be the building blocks of a new "Global Standard".

110. Much will be learnt from this crisis, and perhaps few messages are as eloquent as the need for countries to work together, to everyone's advantage. As President Obama joked at the G20 Summit, previous agreements could be reached by a few major powers "over brandy and cigars", but today's trading world is more diverse, more complex and, despite this crisis, will be increasingly prosperous. This is, then, a moment of great challenge and opportunity and, as the OECD's Secretary-General puts it, "co-operation is what the OECD stands for".

Reporting committee: Committee on Economic Affairs and Development

Reference to committee: Standing mandate

Draft resolution unanimously adopted by the Enlarged Committee on 29 September 2009

20. *Ibid.*

Members of the committee : **Mr Márton Braun** (Chairman), **Mr Robert Walter** (Vice-Chairman), **Mr Pedro Agramunt Font de Mora**, Mrs Doris Barnett (Vice-Chairperson) (alternate : **Mr Kurt Bodewig**), Mrs Antigoni Papadopoulos (Vice-Chairperson), MM. **Ruhi Açıkgöz**, Ulrich Adam, Roberto Antonione, **Robert Arrigo**, Badea Viorel Riceard, Mrs Veronika Bellmann, MM. **Vidar Bjørnstad**, Luuk Blom (alternate : **Mr Tuur Elzinga**), **Mrs Maryvonne Blondin**, MM. **Fernand Boden**, Patrick Breen (alternate: **Mr Frank Fahey**), **Mr Erol Aslan Cebeci**, Lord David Chidgey (alternate: **Mr James Clappison**), MM. Kirtcho Dimitrov, Relu Fenechiu, Guiorgui Gabashvili, **Marco Gatti** (alternate: Mr Pier Marino Mularoni), **Paolo Giaretta**, **Francis Grignon**, Mrs Arlette Grosskost, Mrs Azra Hadžiahmetović, Mrs Karin Hakl (alternate: **Mr Karl Donabauer**), MM. **Stanislaw Huskowski**, **Igor Ivanovski**, Čedomir Jovanović, Mrs Nataša Jovanović, MM. **Antti Kaikkonen**, **Oskars Kastens**, Emmanouil Kefaloyiannis, Serhiy Klyuev, **Albrecht Konečný**, **Bronislaw Korfanty**, **Anatoliy Korobeynikov**, **Ertuğrul Kumcuoğlu**, Bob Laxton, Harald Leibrecht, **Mrs AnnaLilliehöök**, MM. Arthur Loepfe, Denis MacShane, Yevhen Marmazov, Jean-Pierre Masseret, **Miloš Melčák**, José Mendes Bota, **Mrs Lilja Mósesdóttir**, **Mr Alejandro Muñoz Alonso**, **Mrs Olga Nachtmannová**, **Mrs Hermine Naghdalyan**, **Mr Gebhard Negele**, Mr Jean-Marc Nollet, **Mrs Mirosława Nykiel**, Mrs Ganira Pashayeva, Mrs Marija Pejčinović-Burić, MM. Petar Petrov, Viktor Pleskachevskiy, Mr Jakob Presečnik, **Mr Maximilian Reimann**, **Mr Andrea Rigoni**, Mrs Teresa Rodríguez Barahona (alternate: **Mr Alejandro AlonsoNúñez**), **Mrs Maria de Belém Roseira**, MM. Giuseppe Saro (alternate: **Mrs Anna MariaCarloni**), Hans Christian Schmidt, Predrag Sekulić, MM. Samad Seyidov, Leonid Slutsky, **Serhiy Sobolev**, MM. Christophe Steiner, **Vyacheslav Timchenko**, **Mr Joan Torres Puig**, Mrs Arenca Trashani, Mr Mihai Tudose, Mrs Ester Tuiksoo, MM. Árpád Velez, **Mrs Birutė Vėsaitė**, MM. Oldřich Vojtř, Konstantinos Vrettos, Harm Evert Waalkens (alternate: **Mr Pieter Omtzigt**), **Paul Wille**, **Mrs Maryam Yazdanfar**.

Representative of the Turkish Cypriot Community: Mr Mehmet Çağlar

Observers:

Japan: Mr Hidetoshi Nishijima, Mr Youetsu Suzuki

Mexico: Mrs Gurwitz Yeidckol Polevnsky

Secretariat of the committee: Mr Newman, Ms Ramanauskaite, Mr de Buyer and Mr Pfaadt.