

Interview with Dr. Laurence Boone, Chief Economist at the Organization for Economic Cooperation & Development (OECD)

G lobal Economic Outlook Not So Grim as G20 Summit in Osaka Approaches

By Japan SPOTLIGHT

The G20 Summit in Osaka this year will highlight the challenges facing the global economy based on assessments of current conditions. What are these conditions and challenges likely to be? We interviewed Dr. Laurence Boone, the chief economist at the Organization for Economic Cooperation and Development (OECD), a global policy forum that works with more than 100 countries on interdisciplinary analyses aimed at promoting the economic and social well-being of people worldwide.

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Introduction

JS: First of all, could you tell us about your academic background and the kind of economics that you specialize in?

Boone: I have a Ph.D. in econometrics from the London Business School where I studied some econometric tools and their application in analyzing the structural unemployment rate or the business cycle or energy demand, for example. After that, I spent two years at a French think-tank in Paris and then joined the OECD as an economist, where I was first in the modeling team and then involved in surveillance of the EU economy, before joining the private sector. I headed European economic research at the Bank of America and then joined French President Francois Hollande as his advisor on European and international financial and economic affairs. I am more of a macro economist.



Dr. Laurence Boone

We are very concerned whether countries are actually prepared for a downturn if it were to happen. There are two things that we can say with relation to preparation. First, because, there is little room for further monetary policy easing as interest rates are still low, we should make sure that there is enough space on the fiscal side. Second, should a downturn materialize, countries should have investment projects ready to be put in place to provide productive fiscal support and act in a coordinated way if possible.

There are two other areas for cooperation that could mitigate risk: one is obviously reforming the WTO, and bringing countries back to the negotiating table together, which would provide some reassurance to the world. The other, continuing to strengthen the financial resilience of our economies. In this respect, the G20 has an important role to play, first because it brings around the table the 20 most important economies, including the US and China, as a forum for discussion. And second, because it works by consensus, the G20's objectives or actions are actually things that the 20 members can agree upon. If you take the example of trade in the Buenos Aires communiqué, there is a commitment to reform the WTO. We are all sure that it is better to address trade issues through the WTO and its reform rather than through tit-for-tat hikes in tariffs around the world.

The G20 has been instrumental in redesigning financial regulations in the wake of the financial crisis, and will continue playing a role assessing the effectiveness of these regulations. But I think that all countries agree that at the core of the G20's work it is essential that we strengthen the financial architecture, and discuss and build consensus on issues such as climate change, migration and many

Assessment of the Global Economy

JS: What is your personal assessment of the global economy?

Boone: The global expansion continues losing steam, slowing more than was previously anticipated. Growth in Europe has been particularly disappointing, as trade growth both within the EU and with external partners has stalled. Business and consumer confidence has plummeted in advanced economies as trade tensions persist, high levels of policy uncertainty in Europe linger, and the pace of China's slowdown continues to raise concerns.

others.

JS: What do you think about the US economy? It does seem to be having some difficulties this year.

Boone: The US economy is still growing at a very healthy pace – the government shutdown earlier this year obviously did not help – and the fundamentals are good. US GDP growth is strong, the unemployment rate is at a historical low, and people are doing better in general. This performance has been, in part, supported by the fiscal stimulus that President Donald Trump has put in place. But this stimulus is coming to an end next year. At the same time, the central bank has appropriately started normalizing monetary policy, so some additional stimulus is being removed. With less fiscal and monetary support there should be some slowdown in US growth, but we are not too concerned about this. However, there are pockets of risk in the financial markets and very high levels of corporate debt – there were also high levels of equity valuation but they have started to be corrected – and I think that what concerns us most is that trade tensions could also have some impact on US economic growth. So it is very important to solve these trade issues and at the same time to continue improving financial regulation and monitoring risks from the financial sector. I should add that a cause of slight concern is also the non-banking sector, where we have much less data on leverage and activities, so we are trying to more closely monitor activity there as well.

JS: Are Japanese businessmen too optimistic about the global economy and the Japanese economy?

Boone: I think growth is still good, and OECD countries should continue to grow at a healthy pace – although we should watch debt levels. In the medium term, aging will increase costs in terms of pensions, health and long-term care for the elderly, and I don't think that all countries are prepared, including most of the OECD countries. Even if you are optimistic in the short term, it is the right time to prepare for this medium-term challenge, and the G20 are looking at policy best practice, including on working longer in a more flexible way.

Principal Challenges for G20

JS: I had a look at your *Financial Times* article in which you seem to view the trade issue as a challenging one. However, fiscal policy and international coordination is possible in your view. Could you elaborate on this?

Boone: Economists and policymakers know that trade will always be beneficial but has a cost for some sectors, some workers, and mostly in the middle-class in OECD countries. In contrast, in a

downturn everybody will gain if governments plan some coordinated fiscal stimulus, because it will support growth everywhere. If we do it in a coordinated way, then the money that each country will spend can be lower for the same result.

JS: As you mentioned in your article as well, we have a growing amount of public debt – most OECD countries would face difficulty in adopting a loose fiscal policy.

Boone: This is right, there is a growing amount of debt and if one country in isolation was implementing a fiscal stimulus by itself then perhaps financial markets would disapprove and interest rates would go up. Again, if it is a coordinated action then the fiscal stimulus of each country can be lower and coordination would send a strong signal to financial markets in terms of the capacity to cooperate and react. This might be sufficiently powerful to stop interest rates from rising. However, it has to be temporary and very well targeted on productive investment so that it doesn't translate into higher debt. We ran simulations and we believe that if countries do this for a couple of years in a very targeted way debt barely increases.

JS: To be more concrete, you said that coordinated fiscal policy should be focused on investment. Is that corporate tax reduction?

Boone: The focus should be on investment plans. Some countries have a list of investment plans for the next several years ahead where the legal matters have been dealt with and they can invest very quickly, but they tend to spread these investments unwisely over the years. If you had planned to build a bridge in 2022 but there was a downturn in 2020, then you could start the construction earlier. President Trump wants to make these infrastructure investments when the economy is doing well, whereas you should do this when it is not going that well. Some countries like Germany have low debt and lack investment and infrastructure so they can build anytime. Other countries like the United Kingdom or France have infrastructure projects but they have to be spread over time because they have high debt; in a downturn they could start these projects earlier.

JS: Turning to fiscal policy, Japan is in a very serious situation. The government is keen to raise the consumption tax rate, which should happen in October this year. Basically, as an economist, do you believe that this kind of effort to reduce debt is important in order to achieve sustainability of the economy?

Boone: Yes, it is important to have fiscal space and buffers to use during a downturn. Debt is useful to fund public projects like schools



or hospitals or roads, which will benefit several generations. While there is no optimal level of debt, debt should not be too high and Japan has one of the highest levels of debt. It's therefore important to restore some fiscal space. In that respect, the planned consumption tax hike appears appropriate. Compared to the previous consumption tax hike, this time half of the expected revenue will fund child care and a lot of other social benefits, targeted at lower-income people, which should help buffer the shock of the consumption tax on income and growth. So I think it's a well-designed policy.

JS: Inclusive growth is very important – in particular in the Asian economy context. In that respect, people are paying more attention to social security expenditure and also tax policy in order to achieve inclusive growth that they believe is sustainable. This is a key question for sustainability.

Boone: Sustainable inclusive growth does not directly mean income redistribution. I think what is very important is first to address inequality of opportunities, providing good education to everyone, access to public services, transport, healthcare, infrastructure, digital technologies – making sure that each individual can get the skills they need to find a good job. Then, redistribution can help for people who have been left behind or who have difficulties.

JS: In the context of the Asian economies, we call it the “middle-income” trap. To mitigate this trap, I think more equal income distribution is important to build up the middle-class. In that sense, expenditure for infrastructure is very important as well, but spending resources for tax cuts to mitigate income inequality is also very important for the Asian economies.

Boone: Both are important. For a lot of Asian economies, it is important that children and women and migrants receive the education and qualifications that they need. Yes, sometimes you also need redistribution to increase the income of some people. When you redistribute, it should be targeted at the people who need it most. For middle-income people, for example, it is important to ensure that they have decent housing, and access to places where there are jobs and where they can send their kids to school.

JS: In terms of structural reforms in the Japanese economy, I believe that today macro-economic issues are closely related to micro-economic issues. Structural economic reform is a typical example of this.

Boone: It is very important – a lot of the work at the economic department at the OECD is to make the links between macro- and micro-economic issues. The government in Japan has implemented a welcome package of reforms that has inspired many countries. In particular, it has been spectacular to see the results in terms of employment, including female employment. The reforms in migration policy will help offset some of the negative effects from aging on the labor force. Reforms have also been instrumental in terms of trying to get wages to grow. So overall, these structural reforms for trade, workforce and supporting technology and SMEs have been good.

JS: How about the structural economic reforms in OECD countries in general?

Boone: We are in the process of completing an assessment of progress with structural reforms in OECD countries, and will publish the results in our annual flagship publication on structural reforms, *Going for Growth*, this year. What is quite striking is that there seems to be some “reform fatigue” among countries: many are doing fewer reforms than before. Part of this is related to the financial crisis, because countries tend to implement more structural reforms in tough times, but part of it is also that people are getting tired and want more protectionist policies and fewer reforms.

JS: We organizes symposiums with other countries, including informal discussions on structural reforms. Through these exchanges of information and views we are exercising a kind of peer pressure. There is a serious problem posed by rising sentiment against globalization and against structural reforms. These kinds of informal exchange constitute a sort of soft diplomacy or soft foreign policy.

Boone: We review the structural reforms of countries every two years, and these reviews are examined by all member countries of

the OECD and each of them shares their experience and exerts peer pressure on the policy recommendations that we make.

JS: I would like to hear your candid opinion on what the most important issues will be for the G20 Summit in Osaka. Trade issues, or fiscal policy?

Boone: I think there will be a lot of focus on trade, on migration, on strengthening the international financial architecture and economic resilience. Also, a lot of sharing of thoughts on aging and what are the best practices to address this very serious issue.

JS: The aging issue seems to have structural aspects as well, related to social security and the labor market.

Boone: We have done a lot of work at the OECD on pension issues and aging-related issues including the fiscal cost. One of the most trying issues is that we live much longer and better, yet people retire at about the same age as they did 10 years ago. We have looked at the kind of policies that could entice people to work longer, and this involves a flexible labor market, allowing retirees to work while receiving a pension in a way that they aren't financially punished if they continue to work till 70 or 75, for example. If you consider that life expectancy will be closer to 90 by 2050, it would be strange to retire at 65, so it is very important to address this. We have seen a lot of progress in participation among people aged 55-64 but I think we can do a lot better.

Innovation is also a key issue everywhere. The new competition challenges that digitalization is creating will need to be addressed, such as gaining a competitive advantage by retaining consumer data.

Issues Beyond G20 in 2019

JS: There is a view that unemployment could be a source of populism. One argument is that globalization is causing unemployment, while another is that innovation is causing unemployment, for example AI.

Boone: The combination of globalization and digitalization has changed the manufacturing sector a lot and has displaced some jobs across countries – jobs that were not highly skilled or could be replaced. Any job which has a high level of routine can now be automatized and contrary to what people think, these are not necessarily low-skilled jobs, they could be medium-skilled jobs. This combination of globalization and digitalization over the last decade has in fact impacted jobs for those with middle-skill qualifications. This is a worry, and we need to make sure that people who lose their jobs can find another one quickly.

JS: How do you assess regional integration? You mentioned that WTO reform would be a key issue at the G20, but there are some other formats that could contribute to multilateral free trade negotiations.

Boone: Agreements are good, and the larger the better as they work for more people and allow the free flow of goods, services and capital. The EU is a regional agreement and has not prevented others from having agreements with it, for example Japan, so in that context regional agreements work. What are less desirable are bilateral agreements where one country puts constraints on another. There are a lot of impediments to trade, such as non-tariff measures including regulations on health, environment, and security. There is a lot of scope to work at the regional and global level at harmonizing or building consensus regarding regulations. Sometimes it is easier to start at the regional level and then expand from there.

JS: The US is now very reluctant to go back to multilateralism, but if TTP11 works well and if the EU-Japan FTA works well, then US industries might have some complaints about it. Would this be a good way of calling the US back to multilateralism?

Boone: Yes, it could be. The US is not *per se* against multilateralism as they signed the last Buenos Aires communiqué which is calling for a reform of the WTO. I think their concern is that the WTO is not working for a number of reasons, and so the more we can get back to the negotiation table, and the quicker we progress on WTO reform, the better.

JS: You mentioned domestic policy issues in the context of organizing multilateral trade negotiations. How can we manage to integrate those domestic policy issues into WTO multilateral formats? For example, competition policy.

Boone: There is a network of competition authorities, for example within the OECD, and this is good because they can coordinate on these new issues. For trade agreements, there are funds in the US and Europe that are supposed to be dedicated to working with those who suffer from the consequences of globalization, but usually these funds are too small and not well targeted, so we could use them a lot more efficiently. When negotiating trade agreements, we can make sure that there are some standards on environment or health or security that are respected as conditions for trade agreements. **JS**

Written with the cooperation of Joel Challender, who is a translator, interpreter, researcher and writer specializing in Japanese disaster preparedness.