

Report to the Parliamentary Assembly of the Council of Europe on the activities of

THE ORGANISATION FOR ECONOMIC
CO-OPERATION AND DEVELOPMENT (2013-14)



BACKGROUND

The Council of Europe's Parliamentary Assembly (PACE) reviews and debates the state of the world economy and the work of the OECD annually. In the past, the OECD participated in a year-long process by which the Committee on Political Affairs and Democracy – which oversees the work of the OECD – identified a rapporteur, who after a fact-finding mission at OECD Headquarters, prepared a report on the activities of the Organisation. The process culminated in an exchange of views between the enlarged PACE Assembly and the Secretary-General of the OECD (SG) on October 1 of each year in Strasbourg.¹

While the enlarged Assembly debates on the activities of the OECD continue to take place, starting this year and every other year the debate will be based on a report authored by the OECD Secretariat. Every second year, the report will be drafted by the Committee on Political Affairs and Democracy.

This year's exchange of views with the Secretary-General will be based on the report below drafted by the OECD Secretariat.

INTRODUCTION

1. The report that follows aims to inform the enlarged PACE Assembly on the activities of the OECD since Secretary-General Ángel Gurría participated in the annual exchange of views with PACE in October 2013.

2. The report includes OECD activities, including those identified in the Strategic Orientations of the Secretary-General issued in May 2014 setting out how the OECD will continue to support Member and Partner countries in addressing the four main legacies of the global financial crisis – low growth, high unemployment, declining trust and rising inequality.²

3. The report is not exhaustive of all OECD activities but aims to highlight the major initiatives that – based on the analysis of global trends, the definition of new strategic approaches and the identification of drivers of growth – are being undertaken by the Organisation to achieve a fairer, more equitable and sustainable world economy.

¹ The PACE Assembly is enlarged to include the delegations of national parliaments of the OECD member States that are not members of the Council of Europe, as well as a delegation of the European Parliament.

² The Strategic Orientations of the Secretary-General were delivered to the Ministerial Council Meeting (MCM) held on 6-7 May, 2014.

I. THE GLOBAL OUTLOOK, SOCIAL AND FINANCIAL SITUATION

1.1 The Economic Outlook

4. **The global economy is recovering at a moderate and uneven pace according to the OECD's September 2014 Interim Economic Outlook.** Growth in the United States is strong, while in Japan it is expected to pick up speed in the second half of 2014 and 2015. However, the recovery in the euro area remains fragile and hesitant. Growth in major emerging economies will continue to strengthen and nourish global growth, although some, such as Brazil, will face significant challenges to sustain solid growth rates. Trade and investment growth remain sluggish, but private-sector confidence is gradually improving in most advanced economies. The downward pressure from fiscal policy is also falling as the pace of fiscal consolidation eases.

5. **Most OECD countries' GDP potential, however, remains below what it would have been without the economic crisis, by as much as 6% for the euro area. There are also downside risks that could knock the recovery off course.** Geopolitical risks have increased since the start of the year. While financial market conditions have been benign, a renewed deterioration in financial conditions for emerging economies remains a possibility and could spill globally. Persistently low inflation and high unemployment in the euro area raises the risk of deflation and prolonged stagnation.

6. **Monetary policy in advanced economies should remain accommodative in many countries,** especially in the euro area given the low inflation, and in Japan, where asset purchases should be continued as planned. In the United States, asset purchases should be ended and policy rates start to be raised during 2015. In China, monetary policy will need to be eased if growth were to slow sharply.

7. **Recent improvements in fiscal sustainability should be preserved but the increased fiscal space allows some support for activity.** Euro area countries have made significant progress in fiscal consolidation. The needed front-loaded consolidation has contributed to weak demand but the recent improvement in lending conditions is larger than anticipated. Countries should use room within the EU fiscal rules to maintain this policy in a flexible way, and best balance tax and spending instruments, particularly public investment, to boost jobs and growth.

8. **The crisis has left deep scars in the labour market, mainly in the form of higher unemployment and lower participation of the more vulnerable groups of society.** Unemployment will remain well above its pre-crisis levels in many OECD countries despite a projected recovery, with average jobless rates in the OECD area decreasing slightly from 7.4% in mid-2014 to 7.1% at the end of 2015.³ Almost 45 million people are still out of work, 12 million more than just before the crisis. Globally, an estimated 202 million people are unemployed, with many more in low-paid and precarious jobs.

³ *OECD Employment Outlook 2014.*

9. Given these developments, **structural measures to enhance growth should be stepped up and focused on raising productivity and incomes, rather than just reducing costs.** Promoting demand should remain a key policy objective where the recovery has been less robust, accompanied by reinforced measures to combat structural unemployment. In recent years, a number of euro area countries, notably those most affected by the crisis, have stepped up the pace of reforms, including by taking difficult but much needed steps to make it easier for firms to hire new workers and improving regulation for competition. Effective implementation of these measures is now key.

10. Looking ahead, **countries should promote job creation and boost productivity by deploying active labour market policies, improving their skills and innovation policies and further removing barriers to domestic and international competition,** notably in the services sector. Such policies will also help countries get the most out of global value chains. At the EU level, progress towards a more complete Single Market needs to be accelerated, including improving cross-border regulatory cooperation and infrastructure in network industries and transport. Government procurement could be opened up to greater foreign competition.

11. As economies and societies struggle to return to growth, they are also faced with major social and inequality concerns exacerbated by the crisis, as well as the challenges of ageing and the now urgent need to preserve the environment. Much more needs to be done to make our economies more inclusive and our economic policies greener.

1.2 Social Developments and Social Policies

12. **In line with the October 2013 recommendations by PACE, the OECD has continued to work on income inequality.** Over the past three decades, the share of the richest 1% in total pre-tax income has increased in most OECD countries. The income of the top 10% of the population is now 9.5 times that of the bottom 10%, up by more than 30% in 25 years. Even in countries with more equal distribution, such as Germany, Norway and Sweden, the income ratio of the richest 10% to that of the poorest is up from 5:1 in the 1980s to 6:1 today. The crisis has intensified these long term trends.

13. The youth have now replaced the elderly as the group experiencing the greatest risk of income poverty. While relative income poverty has remained broadly unchanged between 2007 and 2011 in the OECD area, “anchored poverty” increased by nearly 2 percentage points during the same period, and by much more in the countries most affected by the crisis, such as Greece and Spain.⁴ In Greece, “anchored” poverty increased by almost 15 percentage points over the four years to 2011, with large increases (between 9 and 3 points) also experienced in Ireland, Spain, Iceland, Hungary and Mexico.

14. **The 2014 edition of OECD *Society at a Glance* has found that income inequality and social divisions can worsen and become entrenched unless governments act quickly**

⁴ “Anchored poverty” provides an indicator of poverty developments by measuring poverty against a threshold, which in this particular case is fixed in real terms at 2005 level.

to support the most vulnerable members of society. Data show that during the economic crisis, families have cut back on essential spending, probably compromising their future well-being. Public spending on disability, family and unemployment rose during the early phases of the crisis, but these areas are now under budgetary pressure. Governments need to consider any further expenditure cuts carefully. Social spending and investment should target the neediest and across-the-board cuts in social transfers should be avoided, particularly in the case of housing, child and family benefits.

15. In order to strengthen the sustainability of pensions systems and boost retirement income adequacy, the latest edition of the OECD *Pensions at a Glance* publication calls on governments to encourage people to work longer and save more for their retirement. The report also calls on governments to strengthen pension safety nets to avoid rises in inequality among retirees and pensioner poverty. The report shows that the wealth of retirees tends to be very unequally distributed, within and between countries, and between genders. Homeownership and financial wealth are important factors influencing peoples' living standard in old age. At the same time, public services – such as health and long-term care – have a strong redistributive effect in favour of the elderly and on the adequacy of retirees' incomes. Accounting for these assets and services is likely to play a role in the policy debate on the adequacy of incomes and inequalities in retirement.

1.3 Financial Sector Issues

16. While G20 financial sector reforms, especially the implementation of Basel III, are advancing, 'too-big-to-fail' implicit subsidies and the interconnectedness of the banking sector still need to be addressed effectively. High levels of leverage in the banking sector and vast exposures to derivatives and structured financial products can magnify instability at times of financial stress. Furthermore, robust procedures need to be in place to deal with bank failures, as higher regulatory capital is insufficient to make the financial sector resilient to shocks. There is no reasonable ex-ante capital rule for large systemically important financial institutions that will make them safe under all circumstances. Competitive pressures should be expected to lead to the demise and eventual exit of some banks.

17. Making internationally operating banks simpler and smaller will help the management of failure. So far, however, national approaches to bank structural separation (the US Volcker rule, the UK Vickers proposal, as well as recent French and German bank reforms) have been proceeding in a fragmented manner. A more unified approach would be preferable to avoid the regulatory arbitrage that contributed to the build-up of the crisis.

18. Progress has been made on the G20 initiative on structural banking reforms, which the OECD is spearheading together with the Financial Stability Board and the International Monetary Fund. The OECD has for many years now highlighted the potential benefits of structural reforms for financial stability, which should facilitate swift and effective bank failure resolution, thus helping limit the value of implicit bank-debt guarantees and the extent of risk-taking before any potential failure. The OECD's Committee on Financial Markets has highlighted the relevance of this issue; in particular, that persistence of various types of implicit bank debt guarantees for the liabilities of financial firms tend to create moral

hazard, incentivising financial firms to take on excessive risks from a micro perspective and too much counterparty and systemic risk from a macro perspective.

II. INCLUSIVE AND SUSTAINABLE GROWTH

19. **The global crisis has left a dramatic legacy of low growth, unemployment, under-employment, and worsening living standards for many people.** The New Approaches to Economic Challenges (NAEC) Initiative, launched in 2012, aims to engage the OECD in an organisation-wide reflection about the roots and lessons from the crisis and to develop new advice on structural policies to better address the challenges identified.

2.1 New Approaches to Economic Challenges

20. **NAEC is beginning to deliver results, both in terms of specific outputs and in terms of effective changes in the OECD's analytical framework and "regular" products.** About one third of the 29 projects launched under the NAEC Initiative have already delivered specific outputs, summarized in the Synthesis Report delivered to the 2014 Ministerial Council Meeting (MCM).

21. The NAEC initiative has created de facto **a space to think more creatively.** Some **key developments** have been brought out very clearly by NAEC. The Initiative has highlighted the need for a **better recognition of the complexity and interconnectedness of our economies.** It has also put **the inequality issue and inclusiveness agenda back at the centre of policy debates and has highlighted the linkage between the financial sector and the real economy.** NAEC has also **strengthened and mainstreamed OECD work on well-being** and provided the groundwork for further developing the databases on Trade in Value Added.

22. NAEC is also having an **impact on the OECD analytical frameworks and tools.** The initiative has launched a series of OECD internal seminars to discuss cutting-edge and sometimes controversial research and deepen knowledge about new tools. It has promoted the use of new data and analytical tools such as micro-data and behavioural insight, as well as the development of new measurements of some critical concepts, such as job quality and stocks of economic, human, social and natural capital. The NAEC initiative has also led to the use of a greater variety of models and to the update and review of some of our fundamental assumptions, as well as to specific changes in our forecasting practices.

23. The NAEC initiative is also **strengthening horizontality and promoting cross-silo approaches** to policy advice and policy making, and helping adopt a longer-term view while better taking into account uncertainty into our thinking.

24. **While half of the NAEC projects will deliver results at the 2015 OECD Ministerial Council Meeting,** the work undertaken within the NAEC initiative is **already being mainstreamed** throughout the Organisation. It is also having a **strong impact on the OECD Programme of Work and Budget 2015-2016.**

2.2 Inclusive Growth

25. **One of the major objectives of NAEC is to develop new policy analysis and recommendations to support more inclusive growth.** This responds to the OECD's analysis that over the long term, rising living standards across the globe and falling poverty in the developing world have unfortunately been accompanied by widening income inequality.

26. **The OECD's approach to inclusive growth is comprehensive.** First, it reflects the multi-dimensional nature of well-being, including education and skills, job quality, health status, environment, civil participation and social connections (as reflected also in the *How's Life?* publication and also the *OECD Better Life Index*). Second, it focuses on the distribution of economic and social outcomes to ensure that people have fair opportunities to contribute and benefit from growth. Finally, the approach aims to establish clear links between policy instruments and their outcomes.

27. The 2014 OECD report *All on Board: Making Inclusive Growth Happen* has shown that rising income inequality reflects growing inequality of opportunities and is also accompanied by a greater polarisation of education and health outcomes. For instance, data from 14 OECD countries show that at the age of 30, people with the highest educational attainment levels could expect to live 6 years longer on average than their less educated peers.

28. **The initiative has provided an analytical policy framework to identify the adverse effects of rising inequality on growth.** The OECD has shown that greater inclusiveness and the opening up of economic opportunity can act as drivers, not dampeners, of strong economic performance.

29. **Finally, the initiative aims at developing policy synergies and a more tailored approach to target disadvantaged social groups.** For example, one clear-cut lesson is that investing in the education of disadvantaged people pays long-term dividends for the economy, enhances individual well-being and makes societies more inclusive. In reverse, neglecting to make such investment might result in long-term costs in unemployment benefits, health, social cohesion and poor levels of economic growth.

30. Another important example relates to the OECD's analysis developed in the 2014 edition of the *OECD Employment Outlook* on the quality of jobs and their impact on well-being. The report reveals wide differences between countries and between socio-economic groups, with youth and low skilled workers having lower quality jobs (in terms of earnings, job security and employment contract, and work environment). The report also shows that temporary jobs are not necessarily a stepping stone to permanent employment and that there is no trade-off between job quantity and job quality.

2.3 Developing Skills

31. **Developing the right skills that respond to labour-market needs and ensuring that these skills are fully utilised by individuals and employers are crucial for inclusive growth, especially in the context of high unemployment.** In addition, highly skilled adults

are also twice more likely to report good health than the poorly skilled, are more likely to trust others and participate in volunteering activities.

32. **The *OECD Skills Strategy* provides countries with a strategic approach to developing relevant skills to support better jobs and better lives. The OECD is also working with countries in designing and implementing state-of-the-art national and local skills strategies.** In Austria, Korea, Portugal, Spain and Norway the development of these national skills strategies is well underway; other countries are in the process of preparing the ground for this work. The projects are designed to foster a ‘whole of government’ approach to skills development, activation and use, while drawing upon a wide range of stakeholders (business, trade unions, researchers, education institutions).

33. The *OECD Skills Outlook* was launched in 2013, including the initial results of the Survey of Adult Skills (PIAAC), which evaluates the skills of adults in 24 countries. This first-of-its kind assessment shows how skills are distributed across individuals, social groups and countries, how effectively they are used on the job, and their relation to the economic and social outcomes in society.

34. **Subsequent editions of the *OECD Skills Outlook* will provide comparative analysis of key issues, trends and data** in the field of skills development, activation and use, in OECD Member and non-Member countries. The next edition, to be launched in November 2014, will have a particular focus on skills and the employability of youth.

2.4 New Sources of Growth

35. **With lacklustre growth, an ageing labour force, and growing resource constraints across much of the world, finding new sources of growth has become a global policy priority.** Innovation, science and technology are major sources of productivity growth with strong spill-over benefits across the economy. In 2015, the Organisation intends to complete a revision of the *OECD Innovation Strategy* that will set an action-focused agenda for innovation, with indicators and emerging good practices, and a strong focus on implementation. Feeding into this is a suite of recent and current work to examine and better understand the pathways – both technological and non-technological – of future prospects for growth, innovation and productivity across the economy.

2.4.1 Making the most of knowledge-based capital

36. **Investment in innovation – particularly knowledge-based capital (KBC) such as research and development (R&D), software and big data, organisational know-how, and intellectual property – are now a key driver of productivity and account for a growing share of total investment.** In the US and EU, KBC contributes 20% or more of average labour productivity growth. During the global economic crisis, business investment in KBC declined by less and was hence more resilient than investment in physical capital.

37. **Getting the key framework conditions right for investment in KBC is essential and can be a low-cost step for policy makers to strengthen growth and innovation.**

Policies that enable reallocation of resources to innovative firms are critical to promoting an expansion of KBC. Moreover, ensuring that the frameworks for specific knowledge assets, such as intellectual property rights and big data are suited to today's knowledge-based economy is also essential. Work is now underway to better define, measure and guide policy on these crucial knowledge assets.

2.4.2 The role of young innovative firms in employment creation and economic growth

38. Enabling the growth of young, knowledge-intensive firms matters for productivity growth as well as for jobs. Evidence from 18 countries over 2001-11 suggests that even though young firms (5 years old or less) have only a small weight in the economy – they represent on average 17% of employment – they contribute more than twice as much to job creation (42% of the total) and only to 22% of all job destruction, making them (net) job creators.

39. Governments can help unleash the growth potential of young, innovative firms by enabling policies that allow them to experiment with new business models and by facilitating the reallocation of resources towards the most productive firms. Similar to KBC, structural reforms to product, labour and capital markets, notably markets for risk capital, as well as bankruptcy laws that do not overly penalise failure, are essential.

2.4.3 Information and Communications Technology and the Next Production Revolution

40. Information and communications technologies (ICT), notably the Internet, smart phones and big data, coupled with other scientific and technological advances, could contribute to a “next production revolution” – across the manufacturing, services and primary sectors. Such a revolution would have implications for the structural shape of economies and the global system of production, and could help boost growth prospects across the globe.

41. OECD is conducting new work on the potential impact and policy implications of new and emerging technologies on growth and productivity. This future work will focus on technological changes (industrial biotechnology, nanotechnology, machine-to-machine communication, big data and other ICT technologies, 3D printing and other advanced manufacturing technologies) and other drivers that could strengthen future productivity and innovation. Recognising that people's competencies are a key pillar of countries' success in harnessing new technologies and upgrading in the value chain, the OECD will also look at the jobs and skills associated with countries' value creation processes.

2.5 Sustainable Growth: The Zero-Emission Challenge

42. There is increasing evidence that environmental degradation and over-use of resources will have damaging effects on economic and social sustainability. **Innovation in technologies, and how they are applied, are crucial to enabling industry to create new business values while also benefiting people and the planet.**

43. **Among the various environmental challenges, climate change poses the most comprehensive set of global risks.** While the full effects of unfettered greenhouse gas emissions are likely to produce their largest damages after 2060, rising global temperatures will start to affect GDP earlier. New OECD projections from the *OECD@100 and CIRCLE* (Costs of Inaction and Resource Scarcity: Consequences for Long-term Economic Growth) – both projects under NAEC – suggest that climate change may lower world GDP in 2060 by between 0.7% and 2.5% in the case of a 1.5°C to 4.5°C warming.

44. **The OECD promotes the use of an array of tools to help countries tackle climate change; besides carbon pricing, an important one is eco-innovation.** In recent years, manufacturing companies have been upgrading their efforts towards sustainable manufacturing from pollution prevention to integrated approaches that take into account product lifecycles and wider impacts. Eco-innovation helps to enable this evolution. *The OECD Project on Green Growth and Eco-innovation* was launched in 2008, with the initial aim to better understand how innovation can result in new technological and systemic solutions and to provide industry with a means to improve their contributions to sustainable development.

45. **The globally agreed climate goal – keeping the increase in global average temperature below 2 degrees Celsius – implies the need to move towards zero net emissions from fossil fuel combustion in the second half of this century.** This requires a radical departure from current policies. The economic transformation needed to achieve this is not well understood, as no economy has accomplished this transition fully to date. There is, however, a wealth of experience with emission-reduction policies, including some important success stories, but also some clear lessons on the challenges ahead. These include the high costs of poorly aligned sets of policies, the limited effectiveness of a number of policy approaches, and the lack of credible long-term policy frameworks, including carbon pricing.

46. **The OECD and the IEA, together with the International Transport Forum and the Nuclear Energy Agency, will draw on their respective work to report back to Ministers at the 2015 OECD Council Ministerial Meeting with advice on how to implement the transition to a low-carbon economy.** This will draw from different policy domains including: (i) the organisation of the electricity sector and markets; (ii) the role of energy and environmental taxes; (iii) the trade aspects of support measures for the development of clean energy; (iv) how to attract private finance for green infrastructure and (v) the intersection of agricultural and energy policy choices. The potential distributional and competitiveness effects of the low-carbon transition will also be examined.

III. TRUST

3.1 OECD Trust Strategy

47. **In the October 2013 discussion, PACE also emphasized that restoring trust in government is a matter of central concern to senior policy makers.** The deterioration of trust in the last years has been driven by citizens' sense of unfairness concerning the distribution of the costs of the crisis and of the policy responses as compared to the

distribution of the benefits of the expansionary period that preceded it. This is further exacerbated by a public perception that regulators and policy makers did not intervene effectively in the areas which prompted the crisis, particularly financial markets.

48. **Low levels of trust can make it difficult to mobilise support for policy reforms, reduce compliance with regulations, including the willingness to pay taxes, and hit investors' confidence.** In order to rebuild trust, governments will need to demonstrate that they can anticipate crises, are responsive to citizens' expectations and needs, effective in the way they manage markets, and fair and transparent in the way they make policies.

49. The *OECD Trust Strategy* will provide policy support for governments to help them regain public trust, building on core strengths in areas such as integrity, anti-corruption and open government, developing measurement tools, and showing how policies to build trust can help inform and support policy reform in diverse areas such as tax policy, corporate governance, and education. The Trust Strategy will include a substantial component on securing fairness in policy-making. This work will build on ongoing OECD work in key areas such as lobbying, public procurement, post-public employment, and the financing of democracy. The Strategy will also include innovative approaches to measuring trust.

3.2 Base Erosion and Profit Shifting

50. **In 2013, the enlarged assembly of PACE provided strong and specific support for the OECD's work to ensure tax fairness by reforming international tax rules.** This work was launched in 2013 under the auspices of the OECD/G20 Base Erosion and Profit Shifting (BEPS) Project. In light of the pressing need for reforms in this area, OECD members and G20 Leaders committed to an ambitious timeline to deliver outputs relating to 15 key action points by the end of 2015.

51. In recent years, it has become increasingly clear that **the current international tax rules, some of which stem from principles developed in the 1920s, have not kept pace with the way business operates in the 21st century and the globalised economy.** In some cases, the international tax rules, designed to eliminate double taxation, have been used by multinational enterprises to facilitate double-non taxation. The result has been to distort economic activity, thwart the policy objectives of governments, decrease governments revenues, and increase citizens' sense of unfairness.

52. At the **September 20-21 meeting of the G20 Finance Ministers in Cairns, Australia**, the OECD's Secretary-General presented the **2014 deliverables of the BEPS Action Plan**, covering 7 key areas of the international tax rules. They include recommendations on improving transparency of multinational enterprises through country-by-country reporting requirements, addressing existing opportunities for treaty abuse and the gaps caused by mismatches between countries' domestic tax rules, and propose an agreement on the way forward to address the tax implications of the digital economy.

53. **Implementation of the project's recommendations will be crucial.** Implementation will require changes to the international tax rules (such as the OECD's Transfer Pricing

Guidelines) as well as amendments to domestic tax laws. Effective implementation will reduce compliance costs for both businesses and governments, eliminate potential arbitrage opportunities among rules implemented differently and minimise the risk of double taxation.

54. The 2014 deliverables are only the first step in the BEPS Action Plan, which will deliver final outputs—including 8 additional elements— by end 2015.

3.2.1 Automatic Exchange of Information

55. Since 2009, when the Leaders of the Group of 20 declared that “the era of bank secrecy is over”, the *Global Forum on Transparency and Exchange of Information for Tax Purposes* has restructured and expanded. It now comprises more than 120 members committed to implement the international standard on tax transparency and exchange of tax information on request. The Global Forum’s peer-based review system is in place to ensure that countries’ commitments are continually monitored, and an overall compliance rating is assigned – already more than 60 jurisdictions have received an overall rating.

56. **Starting in 2012, automatic exchange of information (AEOI)** – which is the systematic and periodic transmission of bulk taxpayer information – has been central to the OECD’s efforts to modernise the international tax system. **In 2013, the enlarged assembly of PACE itself called for the OECD to “push for a “Big Bang” approach on AEOI.** In February 2014, the OECD released a single common global AEOI Standard. This was followed in July with the release of guidance to complement the Standard and the full technical details necessary for implementation. The development of this global standard has key advantages including process simplification, higher effectiveness, and lower costs for all stakeholders (governments, financial institutions, taxpayers). The AEOI Standard is also in line with the Financial Action Task Force requirements regarding beneficial ownership information.

57. **With the AEOI standard now agreed, the focus must shift to coherent and timely global implementation.** Already more than 60 countries have committed to implementation, and 45 jurisdictions have agreed to an ambitious, specific timetable that will see the first exchanges take place from 2017. The Global Forum is putting in place a commitment process that calls on its 122 members to implement AEOI, and is working on a process to monitor members’ implementation of the Standard. In general, Global Forum members are urged to commit to implement AEOI in accordance with a specific timeline, enabling them to start exchanging information automatically by 2017 or 2018. However, the Global Forum has invited developing countries that are not financial centres to consider committing to AEOI implementation in a timeframe commensurate with their tax reform priorities and capacity.

IV. TRADE AND INVESTMENT

4.1 Decoding the “Trade Genome”

58. Trade and investment remain the linchpin of our growth model. **Over the past years, OECD’s work on Trade in Value Added-Global Value Chains (TiVA-GVC) has**

changed our understanding of global trade, investment and production patterns, leading to better measurement of the gains from trade and the costs of protectionism. Reducing global trade costs by 1% would increase world-wide income by more than USD 40 billion, 65% of which would accrue to developing countries. We have begun to decode the *trade genome* leading to an adjustment on the way in which trade policy is conceived; recognizing that success in international markets depends as much on the capacity to import high-quality inputs as on the capacity to export. The OECD has thus also looked at “behind the border” regulatory measures, as well as “at the border” trade facilitation measures.

59. Since the mid-1990s, **international trade and investment have undergone accelerated changes with the emergence of global value chains (GVCs) and the increasing fragmentation of the production of goods and services across the globe.** In 2009 (latest year available), trade in intermediate inputs made up over 50% of goods and 70% of services trade.

60. Participating in GVCs depends on government policies that affect trade costs. Tariffs and other barriers to trade are cumulative, and even “low” tariffs and other barriers can add up to a significant level when the finished good reaches customers. While open markets are a critical factor of enabling participation in GVCs, they are alone insufficient. GVCs also need to be complemented with labour market, social and competition policies as well as policies for investment in education, skills, technology and strategic infrastructure.

61. In recent years, **many countries have actively sought to establish new bilateral and regional trade agreements (RTAs) to increase trade and spur economic growth.** Current RTAs are already on a path that moves beyond existing multilateral rules on issues like investment, movement of capital and persons, competition and state-owned enterprises, e-commerce, anti-corruption, and intellectual property rights. These are essential issues that need to be addressed in today’s more interconnected markets. Recently-announced mega-regional initiatives are on an entirely new scale. The three largest mega initiatives – the Trans-Pacific Partnership (TPP), the Transatlantic Trade and Investment Partnership (TTIP), and the Regional Co-operation in Asia and the Pacific (RCEP) – represent over three quarters of global GDP and two-thirds of world trade. Initial ambitions of these agreements are certainly high, and some aim to go beyond providing preferential access to member countries’ markets, seeking to establish “high standard” 21st century trade agreements with deep and comprehensive market integration.

62. **This year, the OECD is focusing on improving our understanding of how developing countries and SMEs can better integrate into, and benefit from, GVCs.** This work was centrepiece in this year’s G20 Trade Ministers’ Meeting in Sydney, where the OECD presented a joint report with the WTO and World Bank Group entitled “Global Value Chains: Challenges, Opportunities, and Implications for Policy”.

63. **The OECD’s work on TiVA reveals the importance of services in GVCs. Significant shares of services are embodied in exports of goods and they represent over 30% of the total value added in manufactured goods.** Liberalisation of services trade would thus not just benefit services sectors themselves, but would also enhance the

competitiveness of manufacturing firms. This year, the OECD released a services regulatory database and services trade restrictiveness indices (STRI) for 40 countries across 18 major services sectors. The STRI is a unique tool to identify areas of regulatory strengths, weaknesses and opportunities for improvement of countries' service sector performance. The STRI also provides an indispensable tool for advancing services trade negotiations at multilateral level.

64. **The TiVA database has been complemented with a new set of indicators relating to jobs** and will be further complemented with indicators that provide insights into the role of investment in GVCs, revealing the contribution made by foreign affiliates to value-added and employment, including the value-added that 'sticks' in the host economy. The database will be further updated in Q4 2014 to include indicators for 61 countries across 34 industries.

4.2 Long-term Investment (LTI)

65. **According to the OECD, the total need for global infrastructure investment by 2030 is approximately USD 71 trillion.** Over the last two decades, there has been a strong reduction of public capital committed to such investments. The average ratio of public fixed investments to GDP has fallen from above 4% to about 3%. The private sector has been unable or unwilling to take over from governments: in 2010-2012, only 8% of FDI inflows received by OECD countries were going to infrastructure sectors, as opposed to more than 10% during the period 2007-2009.

66. **Besides the weak economic environment, important deficiencies in framework conditions are reducing incentives and returns to investors, undermining investment in infrastructure.** The OECD FDI Regulatory Restrictiveness Index shows that infrastructure sectors and capital-intensive network industries are among the most restrictive sectors to foreign direct investment in G20 economies. This is especially the case of restrictive regulations such as ownership restrictions. **Structural weaknesses in the financial system,** such as the consequences of the crisis on banks' balance sheets or the impact of new bank regulations, also affect the ability of banks to provide long-term financing.

67. **Alternative sources of LTI exist,** such as institutional investors and the USD 80 trillion euros of assets they manage (2012), but less than 1% of these assets are invested in infrastructure. The obstacles to their wider participation in LTI include a lack of appropriate financing vehicles, regulatory disincentives, and their fiduciary duties that make them especially risk adverse in their cost/benefit analysis of infrastructure projects.

68. **The OECD provides guidance and recommendations to increase private sector participation in infrastructure investment and financing.**⁵ Policy recommendations include: a) enhancing the stability and predictability of the regulatory framework, transparent bidding and awarding procedures; b) improving the incentives structure of systemic banks

⁵ This work is contained in the G20/OECD High-Level Principles on Long-Term Financing by Institutional Investors, approved by G20 Leaders at their Summit in St. Petersburg in 2013, and the OECD Principles for Private Sector Participation in Infrastructure.

through the separation and ring-fencing of their traditional (retail) and most risky (derivatives) activities; and c) strengthening public equity markets and addressing the specific obstacles encountered by institutional investors.

V. THE POST-2015 DEVELOPMENT AGENDA

69. **The OECD will continue to support the international development agenda and to mainstream development**, focusing on promoting greater policy coherence for development and inclusive knowledge-sharing among donors and with development countries, and enhancing its contribution to the global development architecture.

70. **In 2015, the global community is expected to agree a successor framework to the Millennium Development Goals (MDGs)**. The post-2015 development framework will aim to integrate the economic, social and environmental dimensions of sustainable development in a coherent and balanced manner. The OECD is offering its convening power, policy advice, and data for the definition and implementation of the agenda.

71. **The Global Partnership for Effective Development Co-operation -- which benefits from joint support from the OECD and UNDP -- will be an important element for implementing the post-2015 framework**. It offers a platform where all stakeholders come together voluntarily to track progress, hold each other to account and learn lessons for improving the way they work at the country level. It also offers a mechanism for monitoring implementation of commitments, using developing countries' own data and processes to track progress at the global level.

72. **Promoting gender equality will be a key theme for the post-2015 agenda, especially as progress against the existing MDG on gender equality has been limited**. The OECD's *Social Institution and Gender Index*, published in May 2012, is measuring discriminatory social institutions and how they impact gender inequality and therewith development outcomes. The framework includes clear transformative indicators on social norms that hold women back to track progress throughout women's life cycle.

73. **The OECD will also focus on integrating its measurement of well-being into the post-2015 agenda, targets and indicators**. OECD work in this area has been referred to extensively in the context of the UN post-2015 process, including the 2013 UN General Assembly Resolution on Happiness. In general, **the OECD aims at putting into practice a multi-dimensional approach to development encompassing the economic, social and environmental dimensions lying at the heart of the post 2015 agenda**, and in line also with the NAEC and inclusive growth initiatives. The OECD has been adapting the framework used by the OECD in its well-being work (*How's Life?* publication, the *OECD Better Life Index*) to better reflect the priorities of people in low- and middle-income countries. It could be used in the context of the OECD Multi-Dimensional Country Reviews.