# THE NEW MODEL OF ECONOMIC GROWTH OF OECD COUNTRIES - NORMATIVE REFERENCE FOR ROMANIA

**Beatrice CHIRIAC,**
National Scientific Research Institute for Labor and Social Protection – INCSMPS, Romania
*beatrice.chiriac@yahoo.de*
**Cristina LINCARU,**
National Scientific Research Institute for Labor and Social Protection – INCSMPS, Romania
*cristina.lincaru@yahoo.de*

**ABSTRACT**
*In this article we present some intermediary results from the study "New geography of employment in Romania. Spatial perspectives of the labor market". Our interest was focused on the delimitation of theoretical aspects and new normative theory regarding economic growth, used by the Organization for Economic Cooperation and Development countries, for the application of a new model of economic growth. The problems identified in 2000 for which were formulated policies sets dedicated remained and are still persistent, which determined initiating a process of change in these sets of policies. Demographic problems, high unemployment and persistent lack of labor force participation, low productivity, high deficits and public debt and prolonged effects of the financial crisis still affecting the economy and society largely. Additionally, the recent crisis has caused a significant distortion of reforms, removing them from goals.*
*Our article highlights briefly on theoretical elements: concept and types of models of economic growth factors and ways to use the factors of production. The results of OECD Report is a normative reference for the analysis of the above mentioned study. Employment and economic growth are the subject of implementation of reforms in different areas, each country choosing its own model, but the analysis of these results represent a valuable input for Romania.*

**Keywords:** employment, economic growth, models.
**JEL Classification:**: O057, O052

## 1. Introduction

The research review presented in the OECD (Organization for Economic Cooperation and Development) Report could be a normative reference for sketching modern paths of growth. Given that growth and employment represents those days the hot subjects in many countries. Regardless of the theoretical approaches there are also many ways of implementing reforms in different areas, each country chooses for own model. The experiences of OECD member countries on growth and jobs are synthetized under the **new economic model** which represents a valuable input for Romania.

## 2. Research question

Our interest was focused on the delimitation of new normative theory and on economic growth, used by the OECD countries, for the application of **a new model of economic growth**. Following the experiences of developed countries it was concluded that it cannot apply a single **model of economic growth** for all countries.

## 3. The new background

**The globalisation** as a process influenced also the theory and policy approach regarding growth modelling. Hervé et. al. (2010) proposed among the International Macroeconomic Models (also Grainer) the OECD's **New Global Model**, upgrading the previous OECD INTERLINK model (Richardson (1988) and Dalsgaard et al.(2001) cited by Hervé et. al. 2010, p.6). This model is characterised by "country and regional models combining short-term Keynesian-type dynamics with a consistent neoclassical supply-side in the long run" (Hervé et. al. 2010, p.6) We emphasise the fact that the spatial perspective is complentary to the development ranking countries classifications. This econometric model includes next to OECD countries – countries with high level of development all other countries. These other countires are geographically clustered ("Other non-OECD Asia", "Non-OECD Europe" and "Africa, the Middle East and Latin America"). The quantitative models analysis are complemented with "*the **mapping of performance** and **policy weaknesses**, and **country-specific expertise**" (OECD, 2015, p.27)* with the purpose to shape reform priorities. The large and complex spectrum of economic growth priorities and objectives are differentiated by time period and by country. This is an expression that defines the ability of a country to give its citizens a chance for a better life. The importance and great interest in this concept gives the size of the major objective of macroeconomic policy. The recent common value for all OECD country which synthetize the essence of the **new model of economic growth** is represented by the *"**ability to improve long-term material living standards through higher productivity and labour utilisation**."(OECD, 2015, p.27)*

Bakhshi et.a al. (2013) propose a Manifesto for the Creative Economy in UK. This economy is centred on „digital technologies”. Bakhshi, et.a al. (2015b), realise The Geography of the UK’s Creative and High–Tech Economies, both highly innovative sectors and with high local externalities and global markets (Moretti, 2012) These new sectors prove to become on long term the new drivers for change of the economies structures providing higher employment potential (see Bakhshi et.a al. (2015a) Pratt et.a al. (2015), Nathan, et.a al. (2016). The mentioned authors already notified that “comparisons between countries where occupational data are available at the 4–digit ISCO resolution shed more light on different creative economy structures across the EU: Sweden has proportionately the largest creative economy workforce (11.92 per cent in 2013), followed by the Netherlands (10.9 per cent in 2013), UK (9.93 per cent), Germany (7.96 per cent), France (7.54 per cent) and then Poland (5.62 per cent)”. (p.31)

## 4. Approaches and discussions

The problems identified in 2000 for their dedicated formulated policy sets were maintained, which triggered a process of change in these sets of policies. Demographic problems, high unemployment and persistent lack of labor force participation, low productivity, high public deficits and debt and prolonged effects of the financial crisis still affecting the economy and society. Additionally, the recent crisis has caused a significant distortion of reforms, removing them from goals. It became necessary to identify national policy successful experiences based on avoiding so-called "one size fits all" in terms of policy recommendations.

The OECD report **"Economic Policy Reforms 2015 - Going for Growth"** makes reference to the evolution of policy priorities targeting economic growth based on systematic monitoring of indicators based on a set of policies and economic performance. After applying the necessary policy sets shows that the pace of structural reforms has remained constant in OECD countries, with the exception of an acceleration in 2011-2012. Although the pathways for growth are the same for all countries, they cannot be treated the same countries differing from each other as opportunities to improve their economic situation over time. By monitoring these processes for the implementation of reforms in various fields and measuring their effectiveness through positive or negative can make a painting that portrays the efficiency and effectiveness of policies implemented in close connection with economic elements specific to each country. The actions taken were often too modest and did not lead to changes imposed by the complete policy recommendations in most countries. In Australia, Greece, Portugal and the Slovak Republic seems to have been a reform process more active and that in general, structural reforms implemented in the early 2000s contributed to increasing potential gross domestic product (GDP) per capita by about 5% (with most of the gains from productivity high). It predicts that "by continuing reform in the direction of best practices could increase potential GDP per capita up to 10%" on average in OECD countries, according to the level of ambitions.

Post-crisis all OECD countries show signs of slowing down reform in almost all areas. Innovation and product market regulation had the best results on enhancing productivity. Labor utilization was evident in **labor taxation, the incentives employed persons and for active policies on the labor market.** Following the crisis has taken steps backward in terms of labor productivity, and social protection, active in the labor market (with policies to cope with sudden and persistent increase in unemployment due to the recession) (Table 1).

**Table 1**

**Evolution of Going for Growth priorities by area**

| *The share of Going for Growth priorities by area (percentage)* | ***2007*** | ***2011*** | ***2015*** |
|---|---|---|---|
| ***Labour utilisation*** | | | |
| *Tax system – emphasis on the level of labour tax wedges* | *9* | *8* | *7* |
| *Social benefits and active labour market policies (ALMPs)* | *15* | *14* | *17* |
| *ALMPs and unemployment benefits* | *4* | *5* | *10* |
| *Retirement and disability schemes* | *11* | *9* | *6* |
| *Retirement systems* | *6* | *6* | *4* |
| *Disability and sickness schemes* | *5* | *3* | *2* |
| *Policy barriers to full-time female participation* | *5* | *3* | *5* |
| *Labour Market Regulation and Collective Wage Agreements* | *11* | *11* | *9* |
| *Job protection legislation* | *6* | *8* | *6* |
| *Minimum wages and wage bargaining systems* | *5* | *3* | *3* |
| *Housing/planning policies/barriers to labour mobility* | *3* | *2* | *2* |
| ***Total labour utilisation*** | ***42*** | ***38*** | ***39*** |
| ***Labour productivity*** | | | |
| *Human capital* | *14* | *15* | *16* |
| *R&D and innovation policies* | *2* | *2* | *6* |
| *Product market regulation, trade and FDI* | *24* | *25* | *21* |
| *Agriculture and energy subsidies* | *5* | *4* | *5* |

| | | | |
|---|---|---|---|
| *Tax system – structure and efficiency* | *3* | *5* | *5* |
| *Efficiency of public spending* | *5* | *5* | *4* |
| *General efficiency* | *3* | *3* | *2* |
| *Efficiency of the healthcare sector* | *2* | *2* | *2* |
| *Public infrastructure* | *2* | *2* | *2* |
| *Legal infrastructure and the rule of law* | *2* | *1* | *1* |
| *Financial market regulation* | *1* | *1* | *0* |
| *Housing/planning policies/barriers to labour mobility* | *1* | *1* | *1* |
| ***Total productivity*** | ***58*** | ***62*** | ***6 1*** |
| | | | |
| ***Total number of priorities*** | ***155*** | ***175*** | ***1 75*** |

***Surse:*** *OECD (2015), "Going for Growth ten years after: Taking a longer perspective on reform action", Economic Policy Reforms 2015: Going for Growth, p. 108, OECD Publishing, Paris. https://www.oecd.org/eco/growth/Going-for-Growth-2015-Going-for-Growth-ten-years-after-Taking-a-longer-perspective-on-reform-action.pdf*

Countries converge towards best practice: countries that were furthest from best practices in 2000 are now those who have made the most progress during this period. "(Economic Policy Reforms, OECD 2015, p. 107)

**The main structural reforms implemented in developed countries**

**a. Reforms to encourage labor "making work pay".**

Countries have progressed in terms of targeting/directing benefits more toward work than for non-employment, but in varying degrees between early retirement schemes, pension and invalidity benefits. In most countries where routes of withdrawal of labor prevailed, they were reduced significantly or simply closed. One of the measures was the phasing out of transition in unemployment, the unemployment process acts as an antechamber to exit the business or retirement. As a result, labor force participation of older workers survived surprisingly well during the last crisis, compared with other categories of workers.

*"In many countries, the closure of early routes to retirement and the tightening of eligibility*

*conditions to unemployment insurance have raised the risk of seeing a substantial increase in the number of disability benefit recipients. While the number of recipients remains high in any countries, governments have focused on reducing the flow into disability through improved gate-keeping measures. In the provision of* *income support for the unemployed, the OECD summary measure of net replacement rates indicates that the magnitude of reforms has been fairly modest over the last 15 years. In order to reduce disincentives to take-up work, governments have used a mixture combining the tightening of eligibility conditions (e.g. minimum number of work weeks required for entitlement), with the reinforcement of job search requirements and sanctions and the possibility to cumulate benefits and earnings up to a time and threshold limits* ". (OCDE 2015, p. 114)

Reforms to replace high labor costs and increasing earnings from second income were important, but only for certain countries.

"*While the tax was reduced in most countries since 2000, the reductions were small in most cases. To limit the budgetary costs, governments should implement measures aimed at reduction of taxation on low wages where the employment impact is likely to be greatest."*

OCDE 2015, p. 114)

Public spending on childcare services grew up significantly in most countries; which has helped to increase childcare services segment, the net cost to parents depends on the fees and benefits in the form of tax rebate or deduction per child. Measures affecting net cost of childcare for single parents.

**b. Reforms in support of innovation.**

They were more moderate. Specific recommendations were made to increase the level and effectiveness of public support for innovation, including support directly or indirectly (through taxation of income). Starting countries since 2000 have followed these recommendations and reform work in this area has been intense. Reforms direct support for research and development have created a model less clear, disorderly as in the case of countries which have significantly reduced direct support (Germany, France, Israel and Sweden) while others have increased considerably this support throughout this period (Austria, Hungary, Korea and Slovenia).

**c. The reforms in taxation and regulation work.**

In policy sets were modest changes. The stringency of the procedures and conditions for redundancy combined with high compensation payments have contributed to the persistence of high unemployment so discouraging employment. Reforms have focused on easing the rules and conditions on fixed-term contracts, thus creating two levels of employment protection, with varying degrees of restrictions on contracts: fixed-term or indefinite. The reforms undertaken were modest. Remain large differences between countries in terms of equity and productivity on the two forms of contracts. Negative consequences were observed, as reported differences between the work contracts of fixed-term protection and indefinite work contract. The recommendations called for changing taxation (direct income taxation) the consumer-oriented (and real estate), and those who promoted efficiency increasing productivity. While some countries have moved to a more flexible charging more favorable taxation mixed (Belgium, Finland, Germany, Sweden and the United States), most countries have on global tax structure unchanged. Several countries have changed much grille tax on indirect taxation (Chile, and to a lesser extent, Iceland and Korea).

• Potential and realised gains of structural reforms in OECD countries. The expected effects of previous structural reforms undertaken between 2000 and 2012 on the potential productivity/potentially output are considerable. (OCDE 2015, p. 119). The impact of structural reforms will contribute to increasing GDP per capita average by approximately 5%, which is about a fifth of the observed increase in OECD countries between 2000 and 2012. Regarding the areas of product market regulation policies and support innovation through reforms succeeded in GDP growth potential/potential GDP by 4%, while 1% was obtained from the use of labor (reforms to improve labor utilization). This is largely explained by the strong convergence that has occurred in product market regulation, an active area of reforms generated significant gains.

Low convergence of labor market policies is due to the fact that a number of reforms in this area go in the opposite direction of the recommendations of **New economic model** to increase growth for some countries, reducing their impact on average. Reforms to improve the productivity tend to have a greater cumulative impact on potential output in the long term compared with measures to improve labor utilization (see Bouis and Duval, 2011). (OCDE 2015, p. 116). OCDE 2015 Report concludes that: ”*Overall, reforms identified in Going for Growth are estimated to have delivered large output gains. The magnitude of the estimated effects varies widely by country, with countries with the initially least growth-friendly policies having obtained considerable gains from reforming, while some countries with more pro-growth initial policy stance have had smaller estimated gains.*”

● **Different scenarios on policy.** OECD economists forecast that the reforms and policies on productivity potential gain OECD area could be from 3.9 to 9.5%, depending on how close to best practice measures are being taken.

● **A modest reform scenario** would bring all countries to a point where the gap in sets of policies to the best practices would not be more than 50% after reform, with a 3.9% increase in potential GDP could be achieved on average. In this scenario slight convergence gains are realized through greater support for innovation, better use of labor, boosting employment and taxation, and to a lesser extent by reducing labor costs.

● In a **more ambitious scenario of convergence**, which sets policy gap vis-à-vis best practices should not exceed 34% after the reform, the average gain potential GDP could reach 7.3%. The relative contribution of various policy areas would be similar to the first scenario, except for gains realized through additional convergence product market regulation.

● Finally, **a scenario of strong convergence**, for example if the gaps in sets policy vis-à-vis the best practice no more than 25% after the reforms could generate an increase of almost 10%, the potential yield level. In this case, support for innovation should remain the main contributor, as in the other two scenarios. However, improving reforms in terms of growth of the labor force - would get about half of the potential gains.

These illustrative scenarios indicate that, by bringing the best practices in a wide range of policies, countries could compensate for the loss of productivity due to the presence of the crisis, pushing the yield potential back to pre-crisis level.

## Conclusions

The recent experiences of developed countries (OECD) in the application of ***reforms indicates following tendencies:***

- Theoretical paths to increase growth are convergent for all countries, but policies differ by country by ability to identify and explore the new opportunities to improve their economic situation over time;
- Harmonization towards a **growth model focused on labor productivity growth**;
- A radical reform in benefits targeting from non-employment towards supporting work.

The core **benefit policies content** are profoundly changed. The main tendencies of policy recommendations **were aimed at**:

- Reducing or simply closing the channels of withdrawal from work;
- Tighten of the eligibility conditions for unemployment insurance;
- Taxation reduction;
- **increasing public support innovation and efficiency** (through innovation can lead to economic growth);

The reforms and policies on productivity potential gain OECD area could be from 3.9% to 9.5%, depending on how close to best practice measures are being taken. (OECD, 2015)

Under the globalization and technological progress has been shaped a new growth model with all actors implication and interdependence regardless the level of development and location. Economics systems becomes more and more complex and highly interdependent.

**The conclusion is that the new macroeconomic and Romania's economic performance require urgent priority initiate a new Emergency Economic Growth Agenda that must follow closely the experiences and outcomes of OECD countries,** attentive to become an active partner.

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