



Secular Stagnation in Europe and Japan

Bruegel-Kobe University

5 October 2015

INEQUALITIES, AGEING SOCIETIES AND SECULAR STAGNATION: AN OECD VIEW

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Outline of my talk

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- 1. What does secular stagnation have to do with inequalities and ageing populations?**
 - Demand versus supply-side aspects of secular stagnation
 - (Mostly) on the supply-side
 - 2. How did the global financial crisis affect potential growth?**
 - OECD estimates of the “hit” on potential output
 - Possible channels underlying lasting impacts from recessions/banking crisis
 - 3. How rising inequality and population ageing fit into the picture**
 - Inequality trends and their impacts on potential growth rates
 - Population ageing/stagnation reduces the size of the labour force and thus potential growth, while also reinforcing the rise in inequality
 - 4. What should governments do?**
 - Raise participation rates and the earnings of low-paid workers
 - Use the tax-benefit system to redistribute income
 - Much else



Part 1 – What does secular stagnation have to do with inequalities and ageing populations?

- Demand versus supply-side aspects of secular stagnation
- Inequalities and ageing affect both demand and supply, but I will focus largely on supply-side channels



Demand versus supply-side theories of secular stagnation

- Chronically deficient aggregate demand is classic focus, at least in North America
 - Alvin Hansen's 1938 Presidential address to the AEA forecast chronic low demand (very wrong, as did not predict World War II)
 - Slow recoveries from the bursting of Japan's bubble economy in the early 1990s and, more recently, the GFC in the US much of Europe is reviving interest in secular stagnation theory
- Chronic slow/no growth can also reflect low potential growth rates due to supply-side factors:
 - Slow input growth (quantity or quality)
 - Slow productivity growth



Population ageing and rising inequality probably have their strongest impacts on the supply side

- Stagnant/ageing population reduces the growth of labour input
 - Clearly true with respect to the quantity of labour, unless participation rates rise
 - Impact on the quality of labour is less clear
- Rising inequality most strongly effects who benefits from growth, but may also contribute to slowing growth by impeding human capital development
- Both factors can also have demand-side effects
 - Hansen cited slower population growth as a factor leading to low investment spending
 - Rising inequality may lower consumer spending or lead to unsustainable debt levels



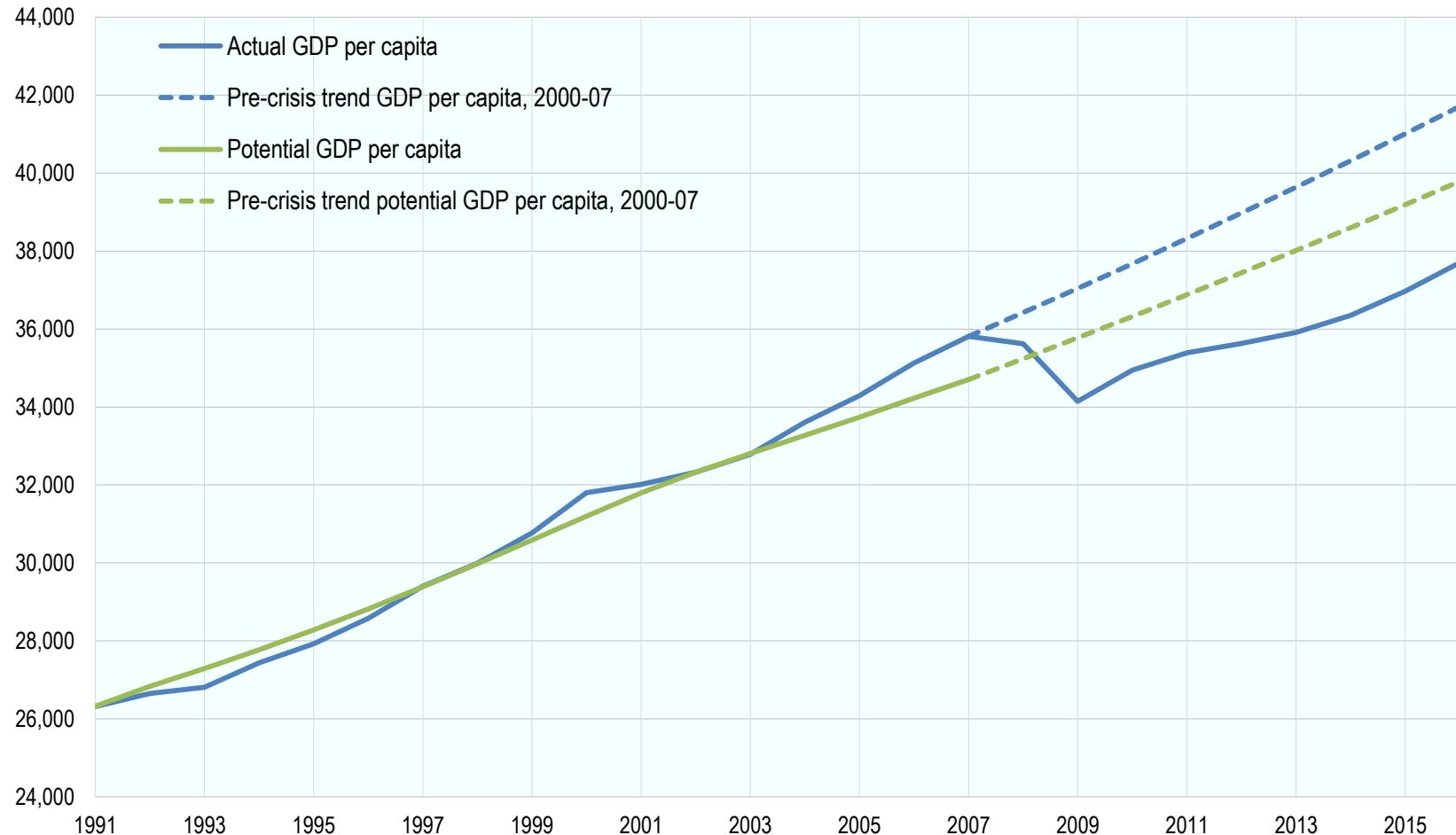
Part 2 – How did the GFC affect potential growth?

- Recent OECD estimates of the “hit” on potential output
- Possible channels from a recession/banking crisis to lower potential growth rates



OECD GDP per capita compared with various pre-crisis trends

In 2010 PPP US dollars

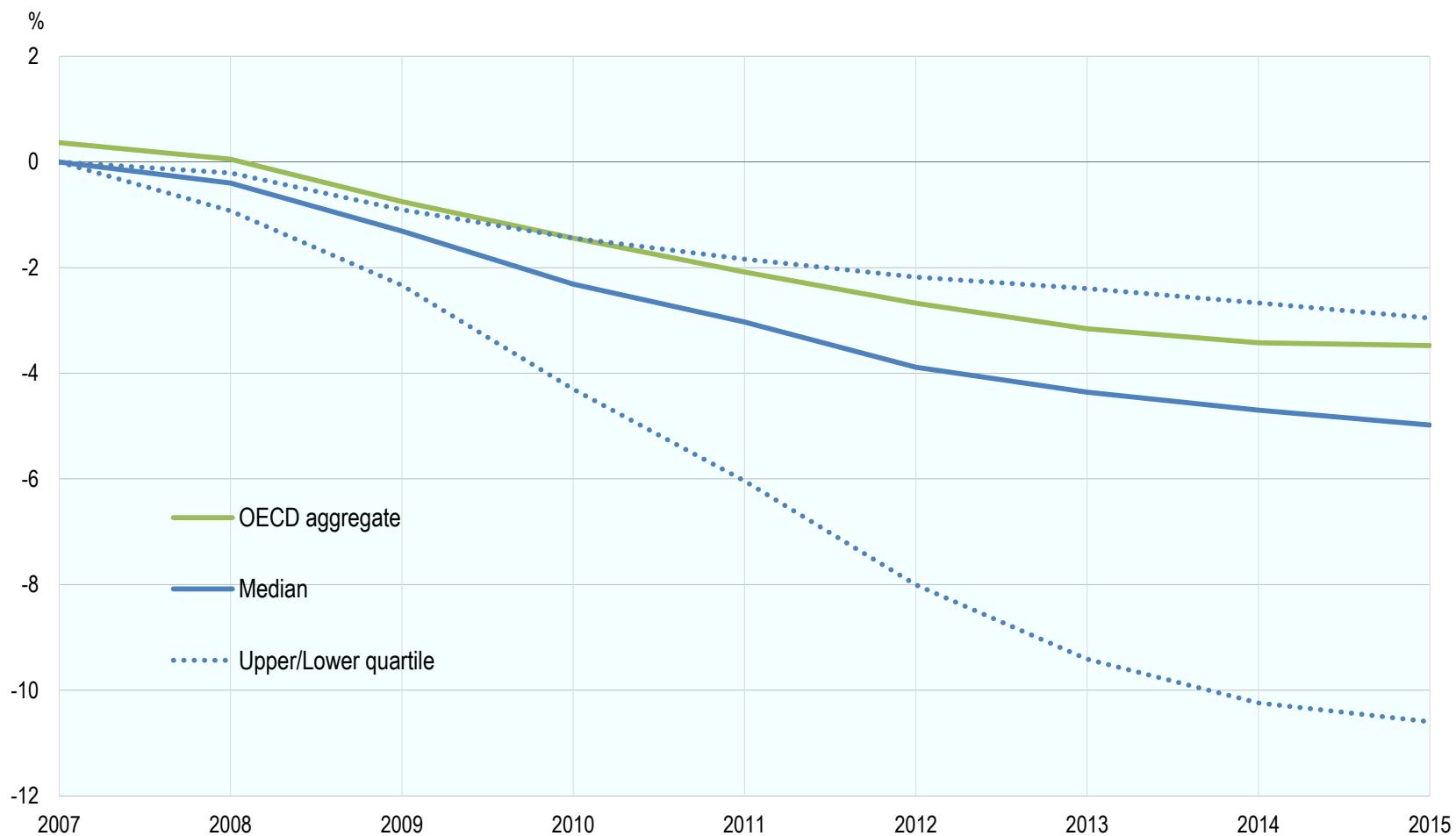


Note: OECD GDP per capita over the period 2014-16 is based on November 2014 OECD Economic Outlook projections.
Source: OECD calculations based on *OECD Economic Outlook, November 2014 long-term database*.



Estimated effects of the crisis on the potential output of OECD countries

Percentage reduction in potential output relative to a pre-crisis counter-factual scenario



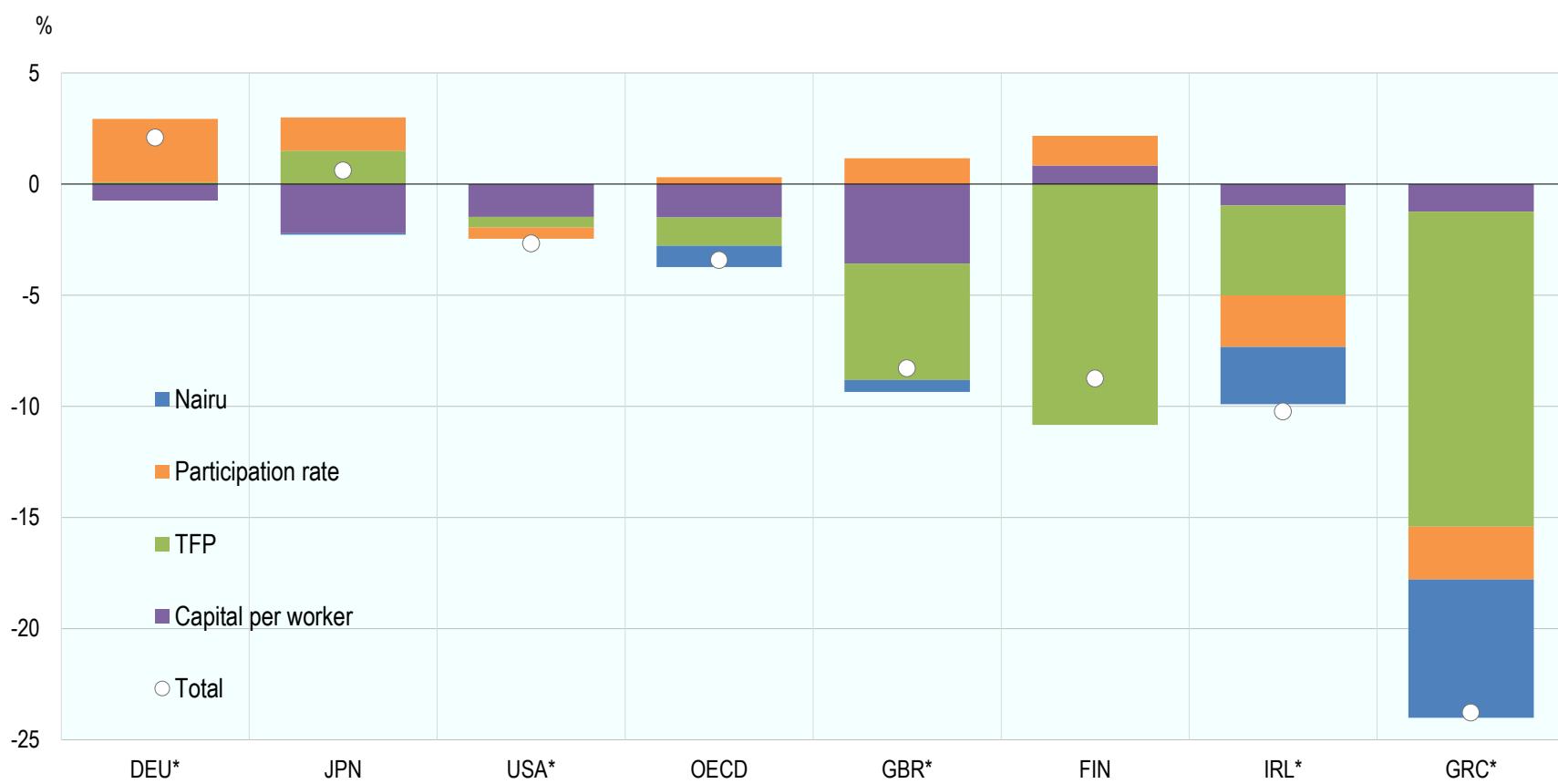
Note: Estimated effects of the crisis are measured relative to a counter-factual scenario in which trend productivity continues at its pre-crisis (2000-7) trend growth rate, structural unemployment rates remain at their pre-crisis (2007) levels and trend participation rates are projected to allow for evolving demographics by holding labour force entry and exit rates constant at pre-crisis levels.

Source: OECD calculations based on *OECD Economic Outlook, November 2014 long-term database*.



Contributions to the effect of the crisis on the potential output for individual OECD countries

Percentage-point differences in 2014, relative to a pre-crisis counter-factual scenario



Note: An asterisk (*) denotes that country is judged to have experienced a banking crisis between 2007 and 2011 based on Laeven and Valencia (2012). Estimated effects of the crisis are measured relative to a counter-factual scenario in which trend productivity continues at its pre-crisis (2000-7) trend growth rate, structural unemployment rates remain at their pre-crisis (2007) levels and trend participation rates are projected to allow for evolving demographics by holding labour force entry and exit rates constant at pre-crisis levels.

Source: OECD calculations based on *OECD Economic Outlook, November 2014 long-term database*.



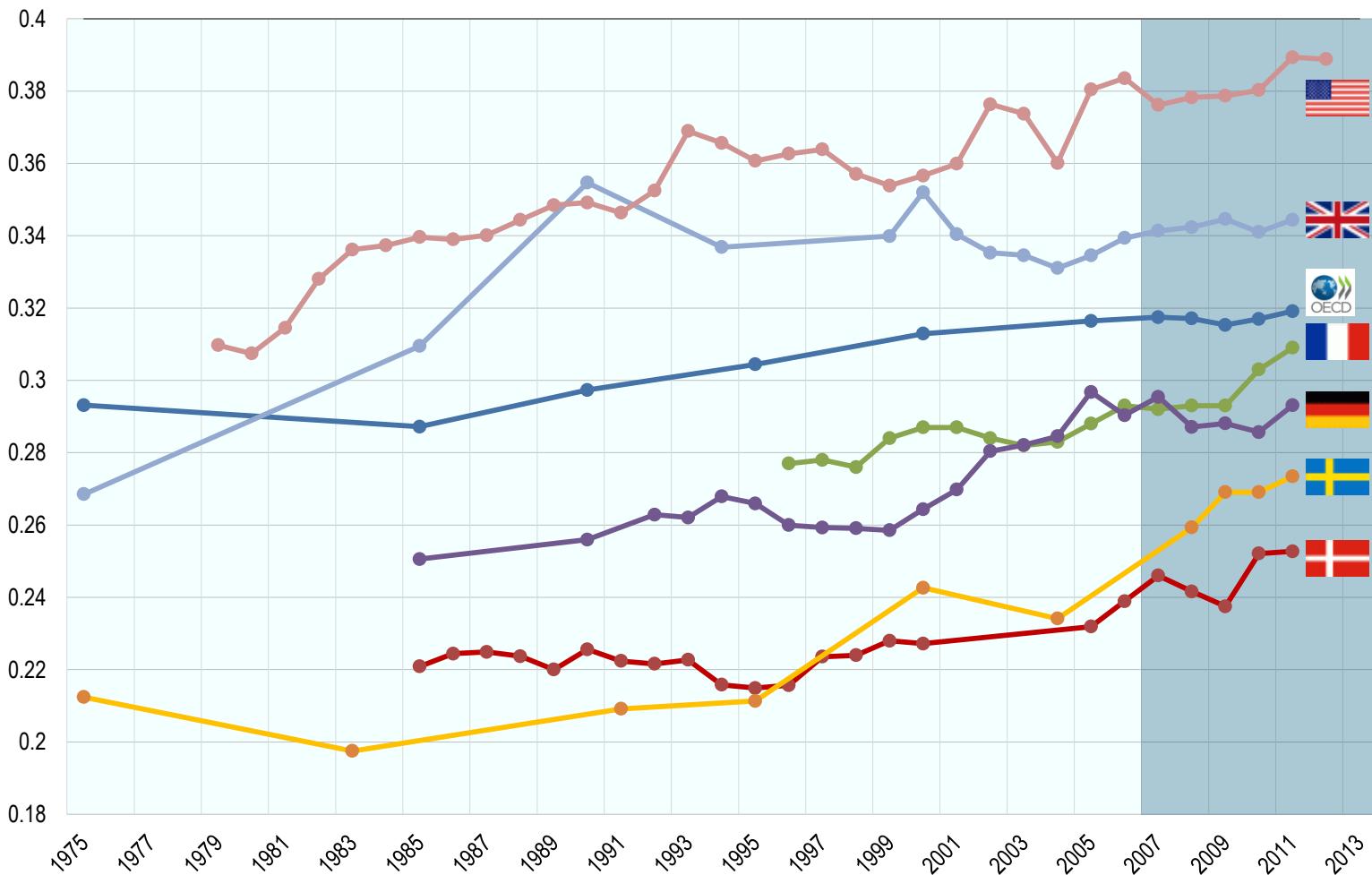
Part 3 – How do inequalities and population ageing fit into the picture?

- Inequality trends and their impacts on potential growth rates
- Population ageing/stagnation reduces the size of the labour force and thus potential growth, while also reinforcing the rise in inequality



Income inequality increased in good times, and it continued increasing in bad times

Long-term trends in inequality of disposable income (Gini coefficient)



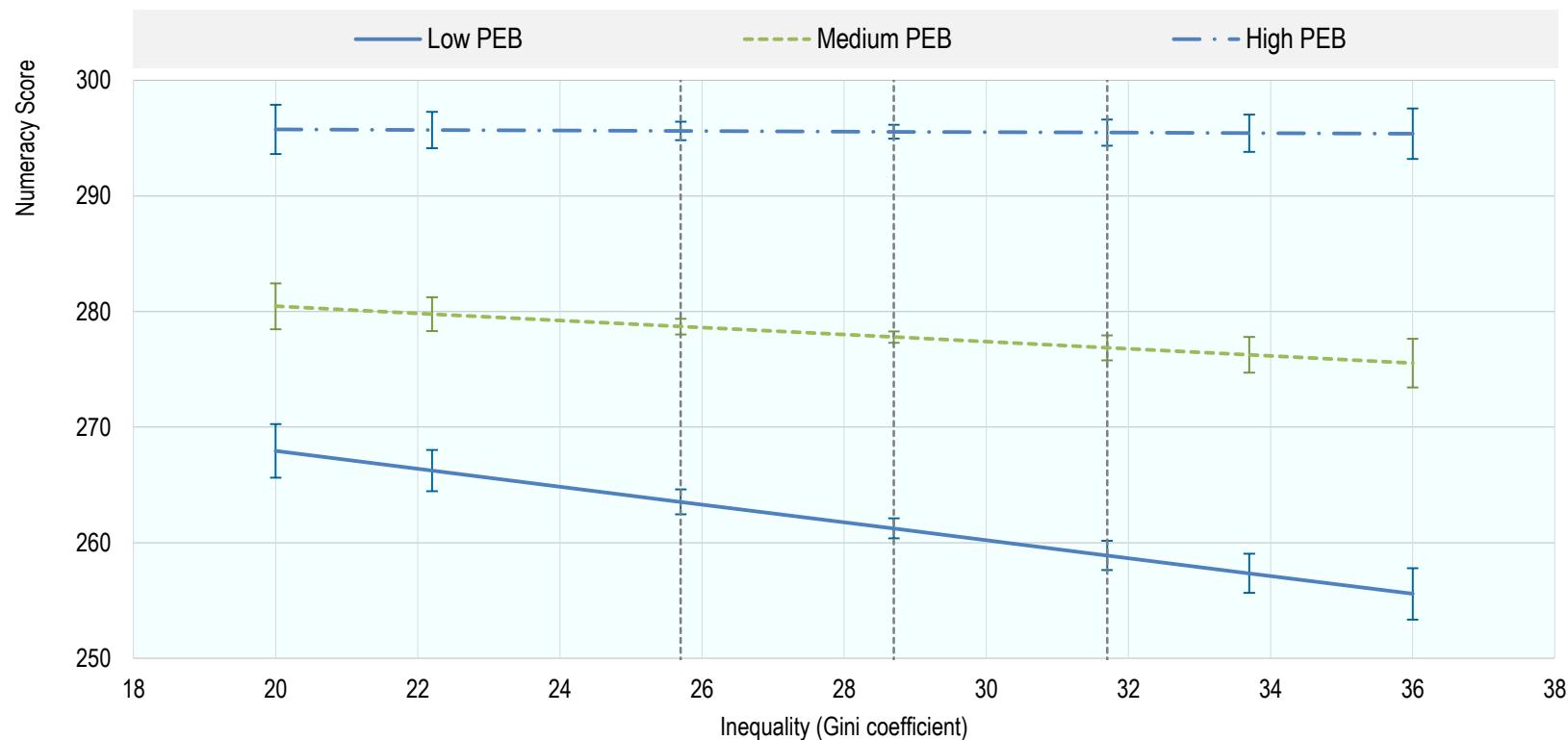
Source: OECD Income Distribution Database, www.oecd.org/social/income-distribution-database.htm.

Note: Income refers to disposable income adjusted for household size.



Inequality drags down economic growth and harms opportunities

Average numeracy score conditional on parental educational background (PEB) and inequality

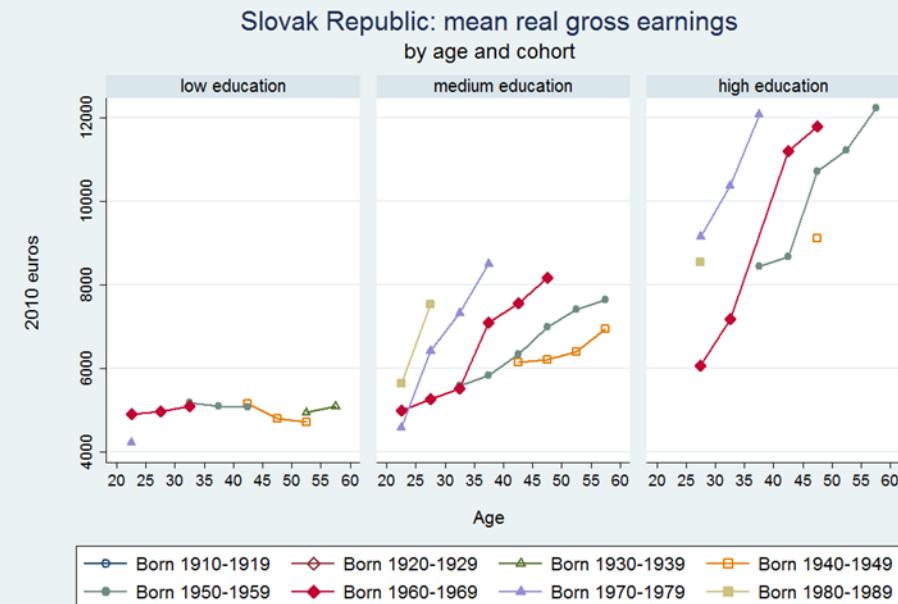
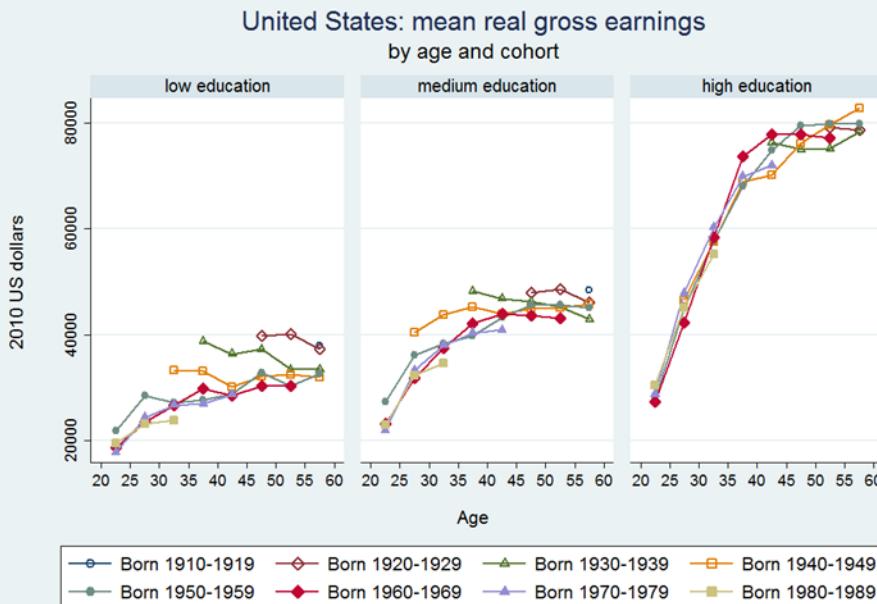


Note: The graph plots the average predicted numeracy score for individuals from low, medium and high family (educational) backgrounds, as a function of the degree of inequality (Gini points) in the country at the time they were around 14 years old. Marginal effects obtained using estimates are shown in Table 2.A1.2, column 7 (i.e. conditioning the degree of formal education). The dotted blue line replicates the results reported in Figure 2.4 in the case of low PEB individuals. Low PEB: neither parent has attained upper secondary education; medium PEB: at least one parent has attained secondary and post-secondary, non-tertiary education; high PEB: at least one parent has attained tertiary education. Dotted lines represent baseline probabilities for each group. The bars indicate 95% confidence intervals. The vertical dashed lines indicate the 25th, the median and the 75th percentiles of the underlying distribution of inequality.

Source: OECD Secretariat calculations based on PIAAC data.



Ageing and slowing growth mean that generational improvements in living standards are slowing in many countries, especially for the less educated (further raising inequality)





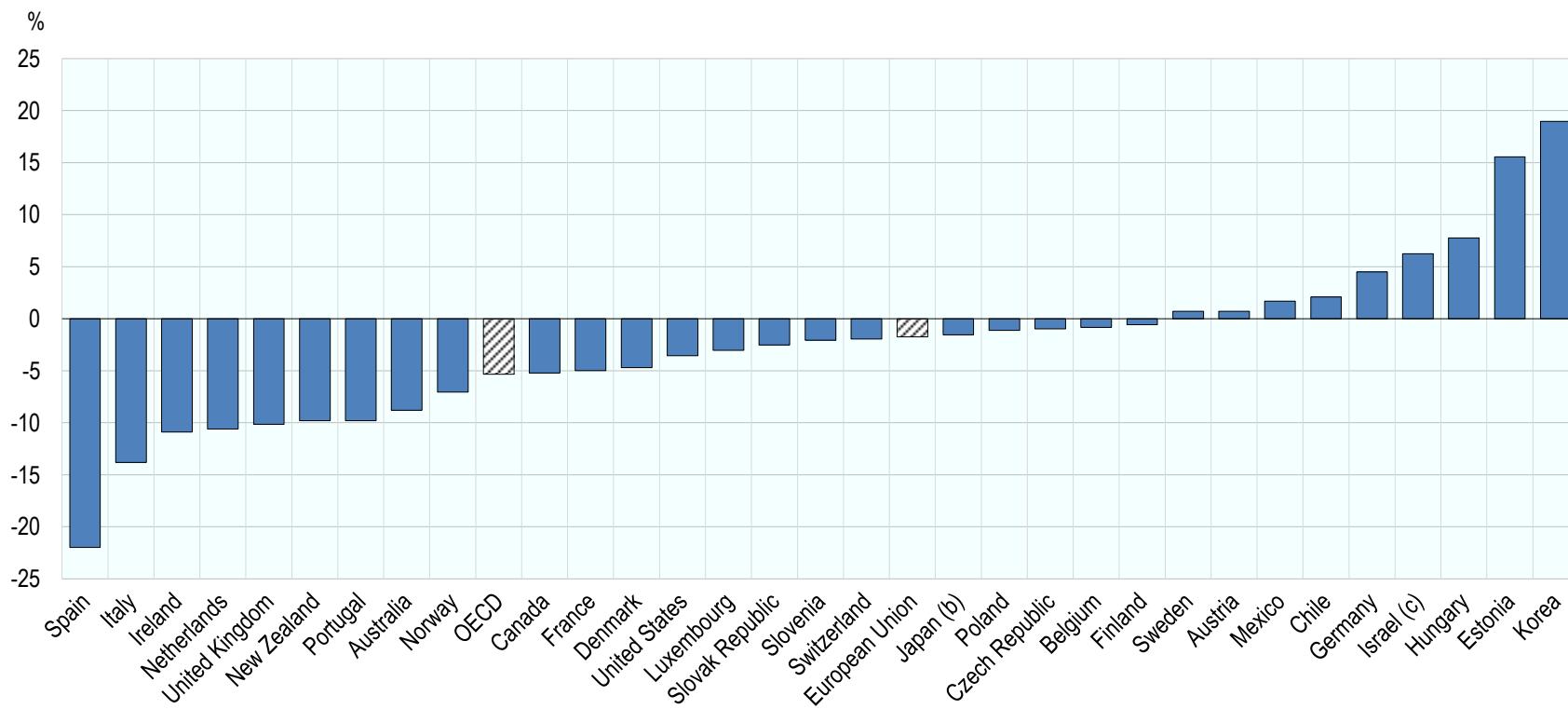
Part 4 – What should governments do?

- **A comprehensive strategy that works on multiple fronts is needed, including measures to:**
 - Raise participation rates (especially of women and older workers)
 - Raise the earnings of low-paid workers
 - Redistribute income via the tax-benefit system
 - And much else (e.g. better macroeconomic policy, immigration, innovation policy,)



Activation measures, targeted to under-represented groups could play a key role

Evolution of ALMP expenditures per unemployed: Annualised average percentage change, 2007-13^a



Note: OECD is the weighted average of the 31 OECD countries reported in this figure (excluding Greece, Iceland and Turkey).

a) 2008-13 for Chile; 2007-11 for Israel and the United Kingdom; 2007-12 for France, Korea, New Zealand, Poland and Spain. Fiscal years for Australia (starting on 1 July), Canada (starting on 1 April), Japan (starting on 1 April), New Zealand (starting on 1 July), the United Kingdom (starting on 1 April), and the United States (starting on 1 October).

b) Short-time work schemes (Employment Adjustment Subsidies and Employment Continuation Benefit of the Employment Insurance) are included in the active labour market spendings for Japan.

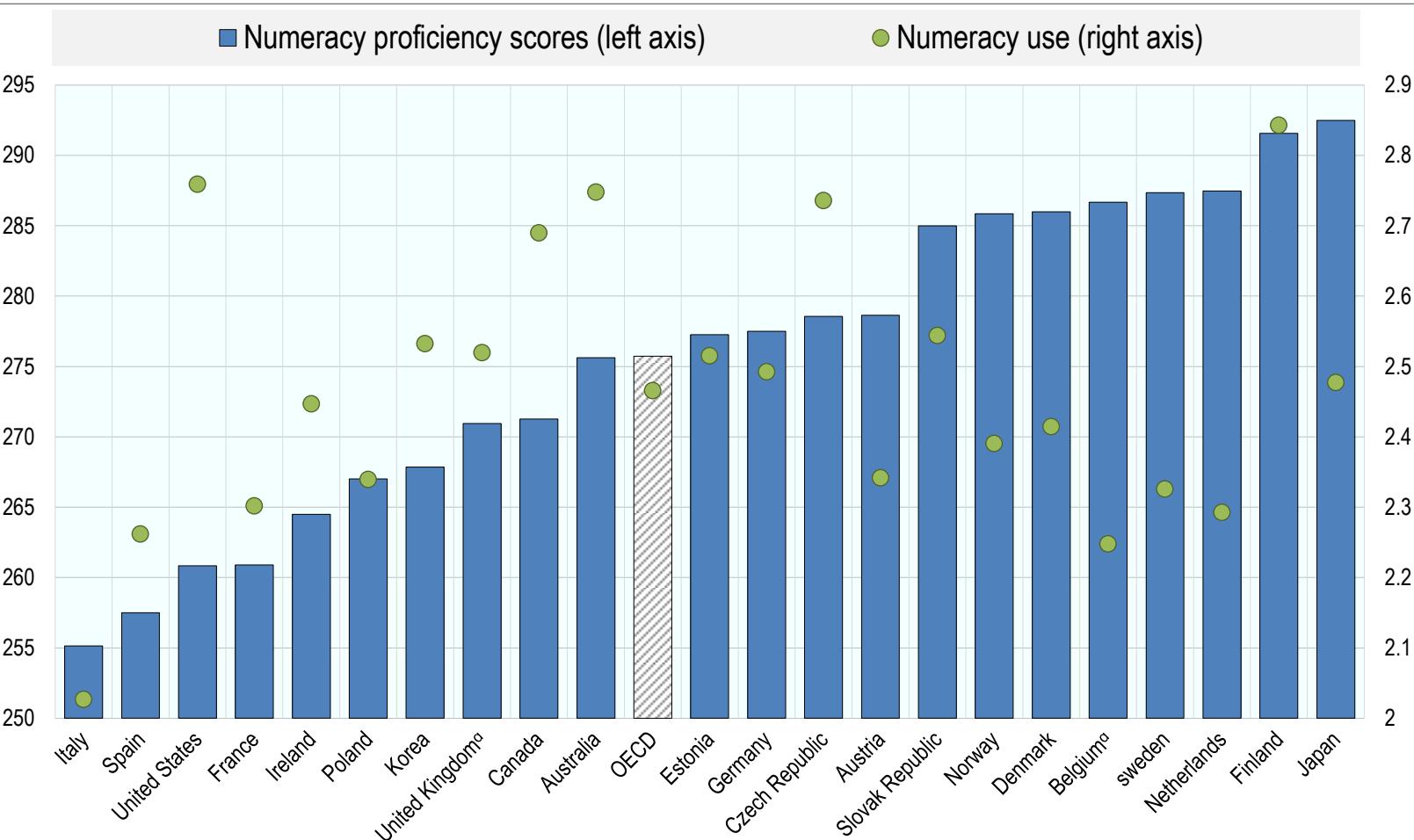
c) Data on unemployment for Israel have been adjusted to be consistent with the data published since 2012 using the chaining coefficient provided by the National Authorities.

Source: OECD estimates based on the *OECD Labour Market Programmes*, Eurostat Labour Market Policy and *OECD Short-Term Labour Market Statistics Database*.



Building relevant skills is key, but also using them in the labour market

Average numeracy scores and average skill use levels

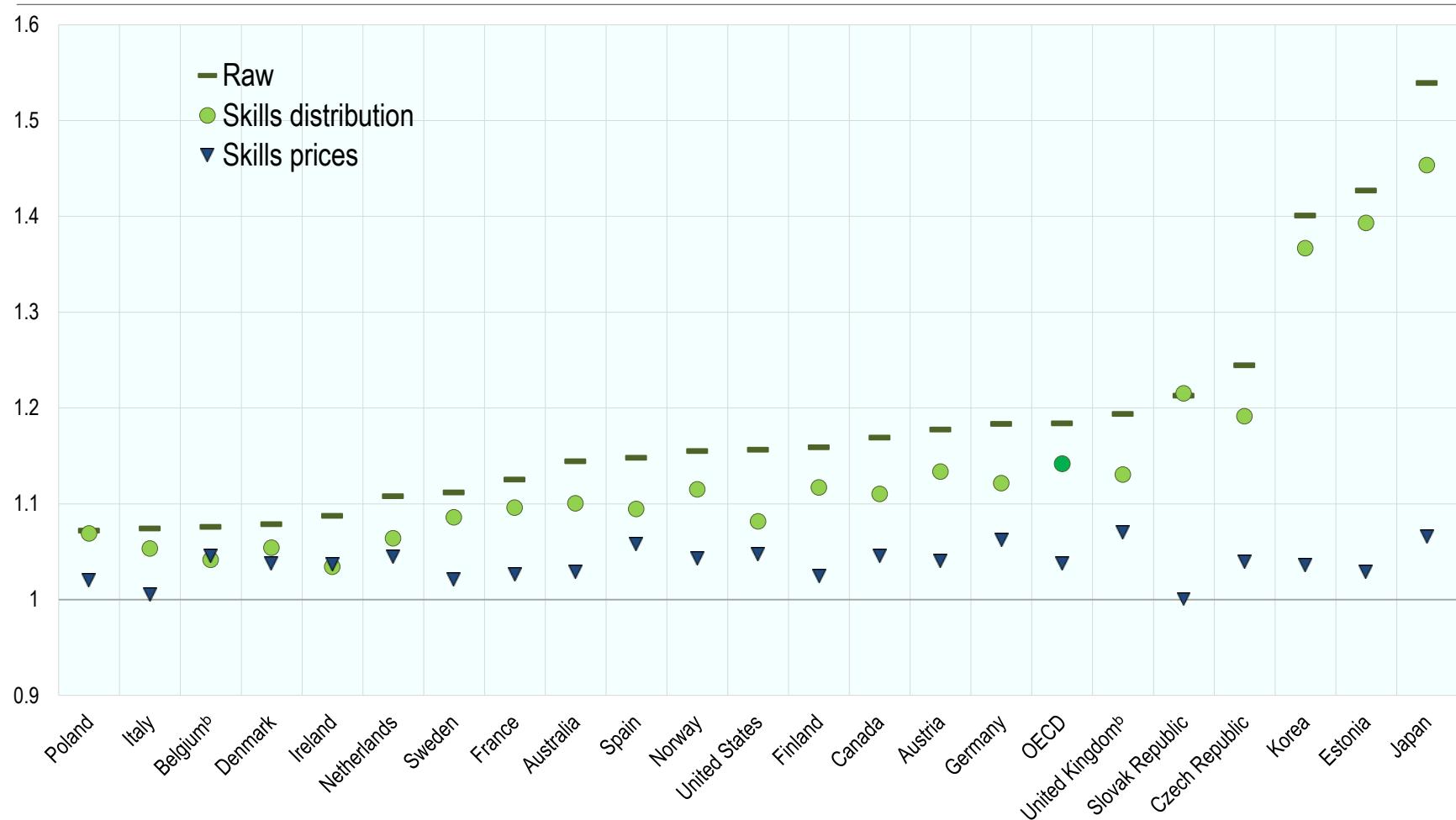


a) The Survey of Adult Skills only covered Flanders (Belgium) and England/Northern Ireland (United Kingdom).
Source: *OECD Employment Outlook 2015*, Chapter 2.



Promoting access to skills in high demand is essential, but also rewarding them equally: the case of gender pay gaps

Male-female wage ratio before and after controlling for skills distribution and price effects^a



a) OECD calculated as the simple, unweighted country average. Wage gaps are expressed as the log of the D9/D1 ratio.

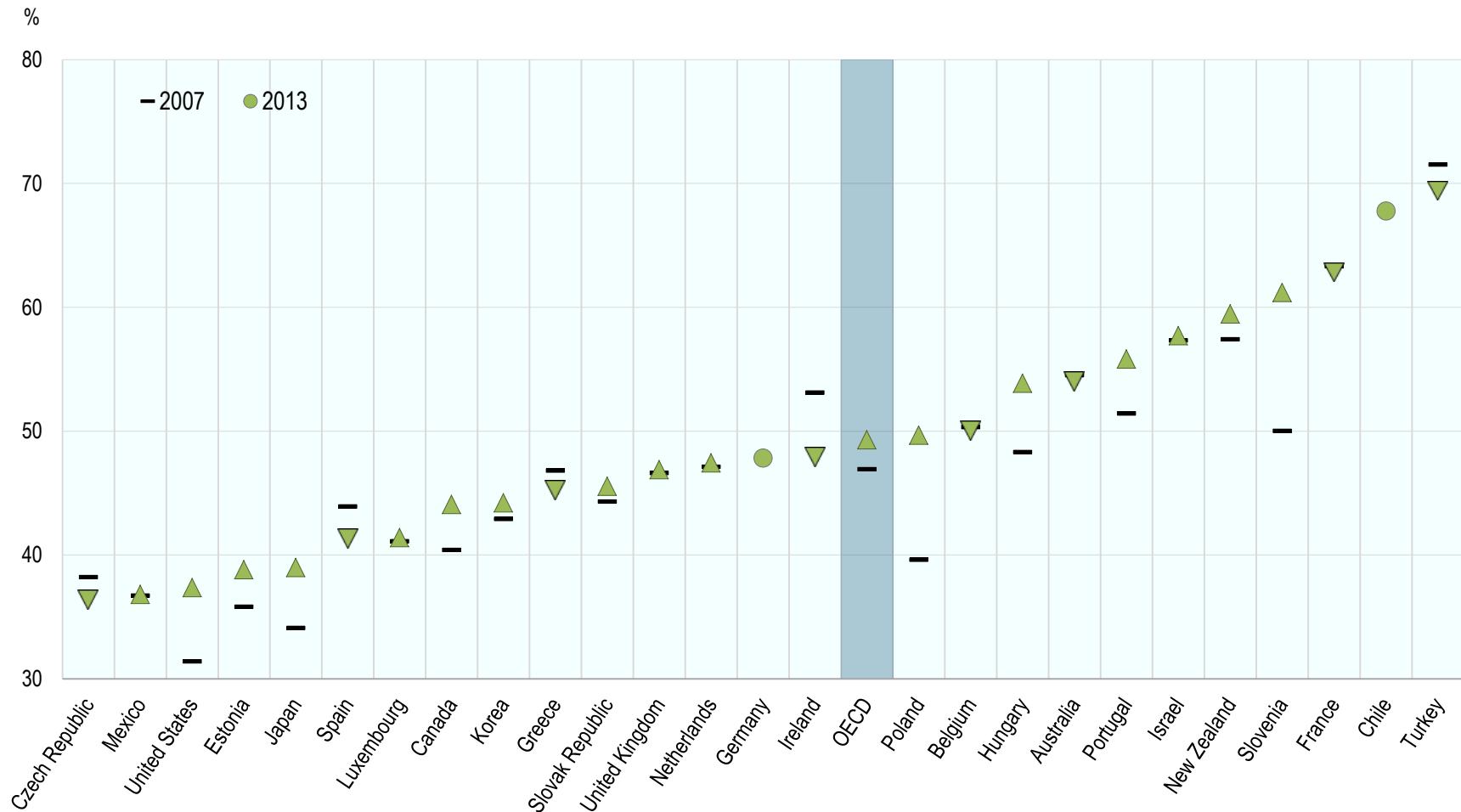
b) The Survey of Adult Skills only covered Flanders (Belgium) and England/Northern Ireland (United Kingdom).

Source: *OECD Employment Outlook 2015*, Chapter 2.



The minimum wage can be a useful tool to combat in-work poverty

Minimum wages as a percent of median and average wages of full-time employees, 2007 and 2013



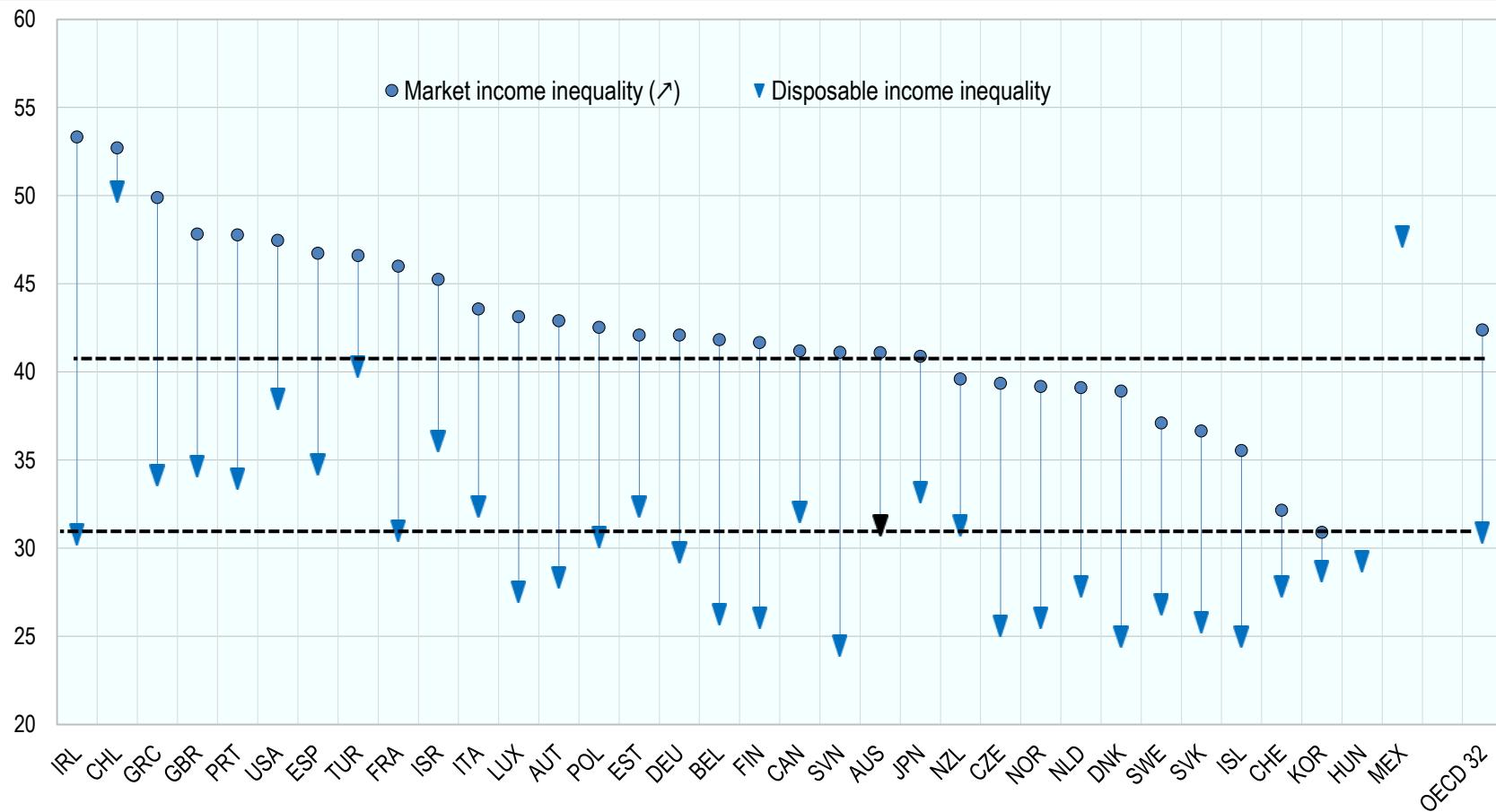
Note: Germany: the minimum-wage level in 2015 is expressed as proportion of the projected 2015 median wage. Projections are based on earnings data from the OECD Economic Outlook Database.

Source: OECD Employment Outlook 2015, Chapter 1.



Redistribution through taxes and benefits plays an important role for decreasing inequality

Inequality of (gross) market and disposable (net) income, working-age population, 2011



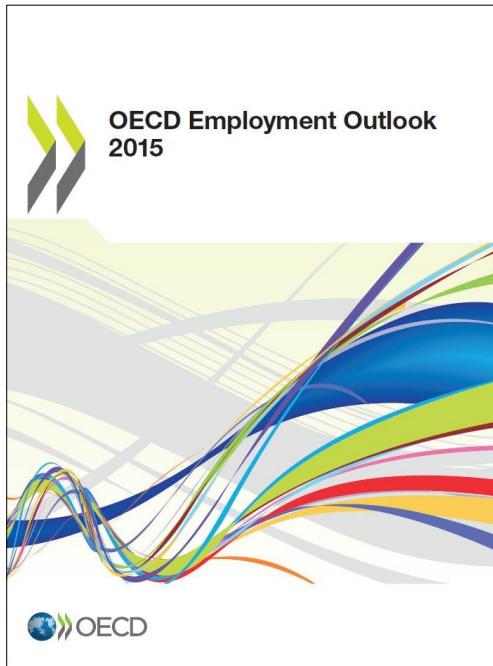
Note: Data for 2007 refer to 2006 for Chile and Japan; and 2008 for Australia, France, Germany, Israel, Mexico, Norway, New Zealand, Sweden, and the United States. Data for 2011 refer to 2009 for Japan; 2010 for Austria and Belgium; and 2012 for Australia, Finland, Hungary, Korea, Mexico, the Netherlands and the United States. For Hungary, Mexico and Turkey data on market income inequality are not available. There is a break in the series in 2011 for the United Kingdom, and results are not strictly comparable. 2011 data for Ireland and the United Kingdom are provisional. OECD-30 average excludes Hungary, Mexico, Switzerland and Turkey.



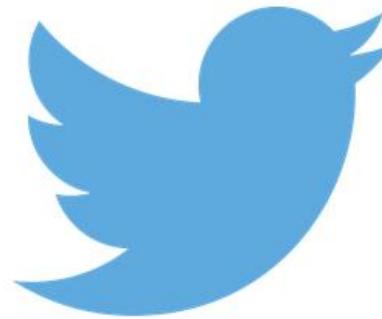
Thank you

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