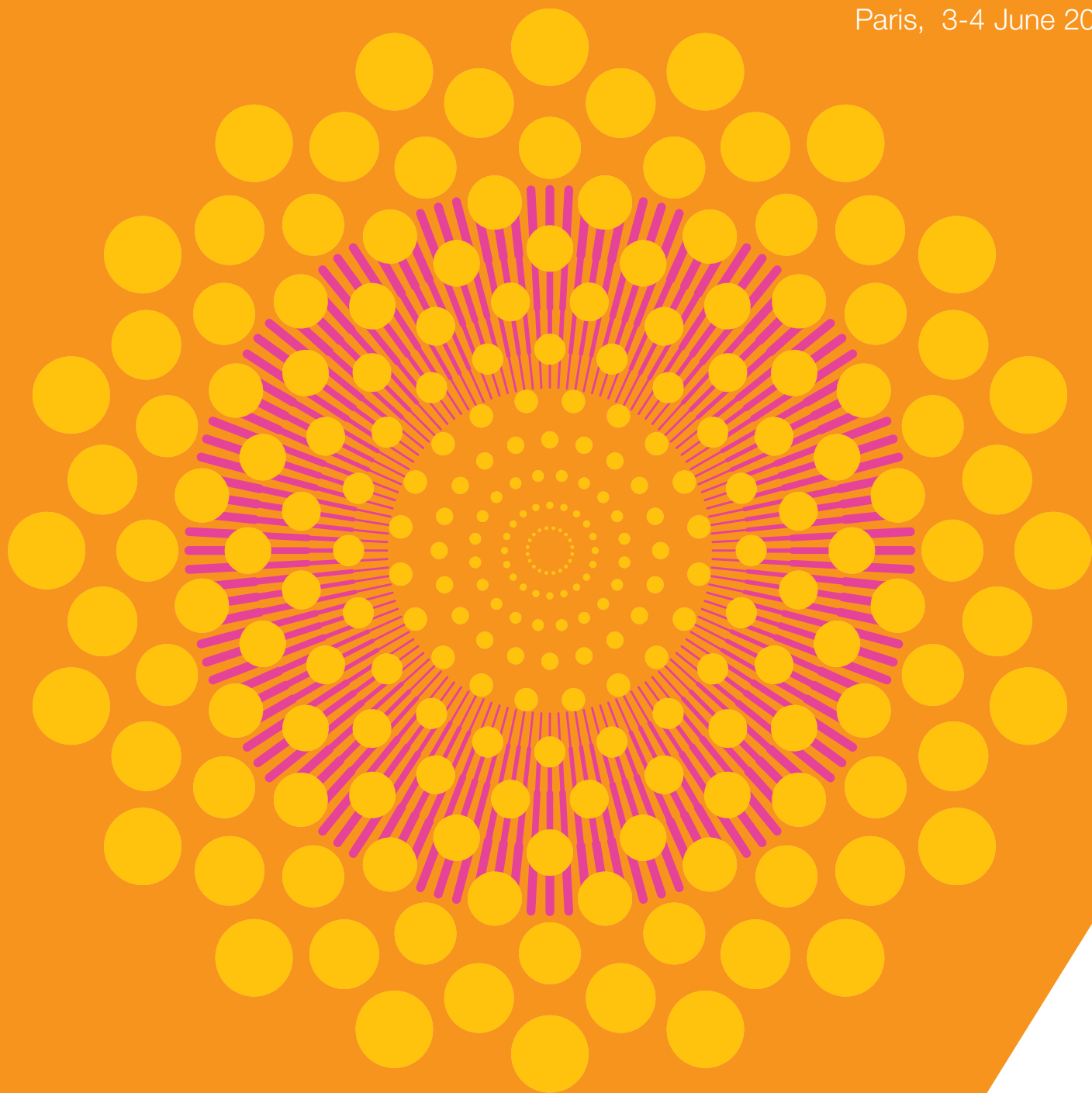


Meeting of the OECD Council at Ministerial Level

Paris, 3-4 June 2015



KEY ISSUES PAPER

Key Issues Paper

This paper follows the structure of the 2015 Ministerial Council Meeting (MCM) draft Agenda and summarises relevant analysis and findings from MCM documents with the aim of informing Ministers' exchanges; the document contains proposed questions for discussion under Items 3, 6, and 7.

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ITEM 1: PRESENTATION OF THE 2015 ECONOMIC OUTLOOK

1. **The global recovery is broadly on track.** Global GDP growth is expected to strengthen progressively and reach close to 4% in 2016, driven by supportive monetary conditions, a slower pace of fiscal consolidation and lower oil prices. World trade growth is also expected to accelerate to 5½% in 2016, the fastest pace since 2011. However, the near-term outlook is still one of moderate economic growth, which is expected to be close to 2½% in 2016 for the OECD as a whole. In addition, the recovery is still fragile, with most of the real income increases accruing from the decline in oil prices.

2. **The projected recovery rests on a progressive acceleration in the growth of investment** (from about 2.5% in 2014 and 2015 to 4% in 2016 on average across the OECD) after years of sluggishness. This acceleration will nonetheless remain milder than in previous cyclical recoveries reflecting the modest acceleration in domestic and global activity, lingering uncertainty, remaining excess capacity in many areas and the drag on investment engendered by lower oil prices in some large economies. As economies continue to recover, as consumption growth accelerates along with the growth in wages and incomes, and confidence in future economic prospects strengthens, firms are expected to increase their investment spending.

3. **Stronger investment is important not only to sustain the cyclical recovery but also to raise productivity.** Further strengthening of business investment will therefore be necessary for the global expansion to be sustained in the medium term. On average, OECD countries have made progress in streamlining administrative procedures for start-ups, simplifying rules for businesses and improving access to information about regulations. As these reforms bear fruit, investment should accelerate, but additional efforts will be needed to eliminate remaining structural obstacles to domestic and cross-border investments.

4. **Employment is still growing too slowly to fully “heal” the labour market.** The share of the working-age population currently employed in the OECD area will remain 1 percentage point below its pre-crisis level by end 2016 (down from 1.8 in early 2015), while the number of unemployed persons will still be 8.3 million greater than it was in the fourth quarter of 2007 (10.6 million in early 2015). Stronger, productive investment can stimulate new hiring while creating the conditions for real wage growth to resume as labour market slack is absorbed and productivity increases. The composition of investment will be a crucial determinant of how quickly labour productivity and workers’ living standards improve. Investments in infrastructure, innovation and skills can play a particularly important role. The impact of such capital spending on jobs could be reinforced by accompanying measures to reduce barriers for people to participate effectively in the labour market.

5. **Another feature of global outlook is the heterogeneity of expected growth performance:**

- In the United States, the recovery in private sector demand is well advanced, although it has recently lost some momentum due to factors such as the stronger dollar and falling investment in the energy sector. These factors are also likely to limit the pick-up in US growth;
- Growth in Japan is expected to pick up in 2015-16 after a sharp contraction following the necessary consumption tax hike in April 2014;
- The favourable tailwinds from lower oil prices, monetary policy easing and a weaker currency will help the Euro-area return to stronger growth rates; and
- The pick-up in growth in 2016 is expected to be stronger in EMEs than in OECD countries, but the path will be quite heterogeneous. While Chinese growth is expected to edge down as the

rebalancing of the economy continues, growth is set to accelerate in others with Russia and Brazil exiting recession, Indonesia accelerating, and India maintaining rapid growth and becoming the fastest-growing major emerging economy.

6. **While exceptional measures to support demand, and resist deflationary tendencies remain necessary in many advance economies, and central bank policies remain crucial to a robust recovery,** an exclusive reliance on monetary policy to manage demand must be avoided. Abnormally low interest rates raise the possibility of increased risk-taking and leveraging driven more by liquidity rather than economic fundamentals. A more balanced approach to policy is required with fiscal and, especially, structural policies providing synergistic support to monetary policy.

7. **Upside risks include a stronger than expected increase in domestic demand, and notably investment, across the different regions as confidence improves.** However, policymakers need to be ready for possible - albeit less probable - high-impact, negative, international events (e.g. increased geopolitical tensions, localised financial crisis, slower growth in emerging markets).

ITEM 2: SCENARIO-BASED POLICY DISCUSSION (WORKING LUNCH)

8. **The Scenario-Based Policy Discussion (SBPD) exercise will invite Ministers to take a long-term view of the policies needed to ‘unlock’ investment for sustainable growth and jobs.** The Secretary-General’s Strategic Orientations, presented at the start of the session, will also inform Ministers’ exchanges. The SBPD exercise will feature three scenarios describing how the global policy context might evolve under different technological, financial, economic, and environmental conditions.

The Strategic Orientations of the Secretary-General: 2015 and Beyond

9. **The Secretary-General’s Strategic Orientations reflect on the policy challenges faced by Member and Partner countries** and highlight how OECD analysis and advice can promote stronger growth, development and well-being. They call for additional efforts to re-fire the cylinders of the global growth engine (trade, investment and credit) in an inclusive and sustainable way, to prevent high unemployment from becoming the new normal and to support efforts to tackle the most pressing global challenges.

10. **Building on the work of the New Approaches to Economic Challenges (NAEC) initiative**, the Strategic Orientations identify possible policy areas where the OECD could undertake further work and offer specific recommendations that take into account policy trade-offs and complementarities. Among these are: measures to stimulate an inclusive growth agenda to help tackle unemployment and ensure that the benefits of growth are shared equally; further developing the OECD productivity and competitiveness agenda, drawing on work on the ‘Next Production Revolution’, innovation and KBC; quantifying the impact of countries’ policy reforms; strengthening OECD contributions to a rules-based international economic system; addressing trade restrictions and access to Global Value Chains (GVC) issues, as well as exploring their linkages with investment; increasing SMEs’ access to financing and promoting entrepreneurship; promoting good corporate governance to stimulate productive investment; developing coherent approaches to fighting corruption in the private and public sectors; strengthening competition and ensuring a level-playing field; contributing to eliminate regulatory divergences; developing national skill strategies in response to changing labour market needs; fostering greater equality and access to economic opportunities for women; promoting the economic and social integration of immigrants and their children; and, promoting more transparent and open governments and strengthening trust on institutions. The overarching aim of the Strategic Orientations is to serve OECD Members and Partners in their collective quest for improved citizen well-being.

Scenario-Based Policy Discussion exercise

11. **The aim of the SBPD exercise is to use three “what if” scenarios¹ to look at possible futures and discuss potential policy implications.** The scenarios are designed to stimulate discussions among Ministers and, through the use of voluntary polling by means of an electronic device, inform their exchanges. Ministers will discuss these megatrends both in table and plenary format, with each of the two sessions in which the SBPD exercise will be organised ending with Ministers being invited to register their views on two questions about which of the scenarios would be most conducive and challenging for investment policies to unlock investment for growth and jobs. The scenarios are identified as ‘Quick Fixes’, ‘Multipolar’ and ‘City Power’:

¹ The scenarios are not forecasting tools and do not reflect OECD views about what could happen.

'Quick Fixes'

12. Globalisation continues with faster policy adjustments enabled by greater transparency and data abundance. Information-empowered citizens and greater responsiveness by national governments keeps the world one-step ahead of most crises. However, progress on long-term strategic planning and international cooperation on major global challenges remain slow. The following trends continue in this scenario:

- Increasingly higher skilled jobs are being lost to automation: inequalities have increased especially between different generations and on a gender and skills basis;
- Entrepreneurs with access to global markets benefit from 'winner-takes-all' outcomes;
- Global environmental risks are increasing, even as resource production becomes more efficient;
- Solar energy is more accessible and affordable.

'Multipolar'

13. The global order is starting to fragment, as regional agreements proliferate and groups of countries choose different routes in pursuit of growth and well-being. Although business and trade is more complex, the diversification of approaches enables progress on some common challenges. The following trends continue in this scenario:

- Countries display different socio-cultural-economic realities and can be broadly classified into three groups:
 - i. open societies, but with an increasing focus on individual wellbeing;
 - ii. cautious, less open economies focused on stability and inclusiveness;
 - iii. other societies, which pragmatically adjust their policies to attract investment (and aid) from the other two groups of countries;
- Alternative global currencies emerge;
- Trade agreements are being concluded, but with a strong regional focus and link to development agendas;
- New regional institutions emerge.

'City Power'

14. As cities compete with one another for the best talent and to attract corporations from around the world, rapid urbanisation is accelerating new models of economic development. Success increasingly depends on the alignment between national and urban policy frameworks. The following trends continue in this scenario:

- The accelerating pace of disruptive innovation;
- The rise in the power of non-state actors, such as cities and new firms, in the global economy;
- New models of co-operative investment are emerging e.g. crowd funding;
- Cities are trying to overcome global policy gridlock on climate change;
- Rural-urban divides are a significant driver of migration.

ITEM 3: UNLOCKING GROWTH: THE ROLE OF INVESTMENT, INNOVATION AND BUSINESS CLIMATE

15. **This Item covers the central theme of the MCM, underlining the multi-faceted role of investment in promoting robust, inclusive, sustainable and resilient economic growth.** It also focuses on the linkages between investment and innovation, skills and responsible business conduct, and how investment is supported by a conducive business climate.

16. **Investment is central to growth and sustainable development.** It expands an economy's productive capacity and drives job creation and income growth. Boosting investment can both support demand in the short-to-medium term while increasing potential growth rates through supply-side effects, by accelerating infrastructure, maintenance and other welfare-enhancing investments in the medium-to-long-term. Well-targeted investment can improve the quality of growth, helping contribute to broader social, economic and environmental goals.

17. **The financial crisis resulted in lower investment, particularly in developed countries, so boosting investment for growth remains a priority.** Private investment in small and medium-sized enterprises and in sectors such as strategic infrastructure is particularly important, as are efforts to reduce economic uncertainties and thereby encourage private investment more generally. There is also scope for public investment in physical (e.g. transport) and social infrastructure (e.g. early childhood education, scholarships for students in need, training measures for youth and long-term unemployed) to help ensure that growth is more inclusive.

18. **The 2015 MCM will focus on the role investment can play in unlocking stronger, fairer, greener, more inclusive and resilient growth and more sustainable development by boosting productivity and employment.** Ministers will explore the role of investment in stimulating productive activities and generating knowledge-based capital (KBC); enhancing human capital through investment in education and skills; assessing the linkages between investment and innovation, trade, and improved business climate, including through well-designed regulation and responsible business conduct (RBC); identifying the role of investment in achieving the Sustainable Development Goals (SDGs); promoting a broader use of the Policy Framework for Investment (PFI); and addressing challenges like water management and climate change. Discussions will have as background ongoing efforts to maintain markets open to investments, facilitate countries' integration into the global economy and promote responsible business conduct, supported by the OECD Declaration and Decisions on International Investment and Multinational Enterprises² and other instruments.

3.1) Investment and inclusive growth

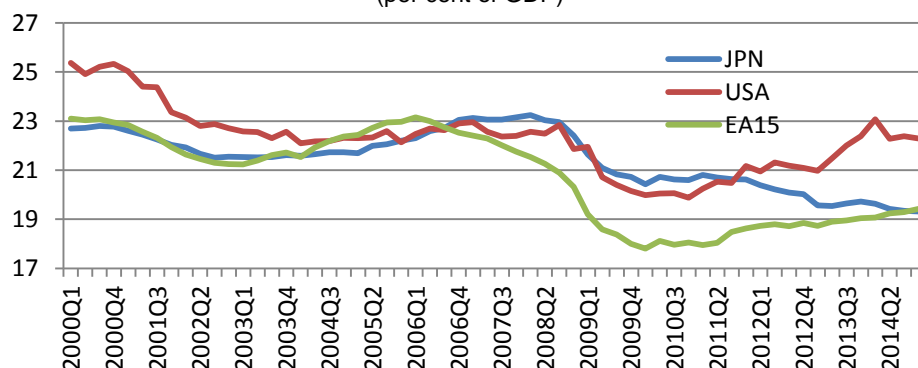
Investment remains below pre-crisis levels

19. **Despite historically low interest rates and steep rises in many asset prices in many OECD countries, investment-to-GDP ratios have not recovered their pre-crisis levels.** The volume of fixed investment is still well below its pre-crisis peak especially in the Euro area and Japan, where the volume of investment is respectively 17% and 5% below its early 2008 level, leaving investment as a share of GDP at less than 23% (Figure 1). In the United States, investment has already caught up with pre-crisis levels, but

² First adopted in 1976, the OECD Declaration and Decisions on International Investment and Multinational Enterprises is a policy commitment by adhering governments (all 34 OECD countries, and 12 non-OECD countries) to provide an open and transparent environment for international investment and to encourage the positive contribution multinational enterprises can make to economic and social progress.

remains short of its long-run trajectory (OECD, 2014b). On the other hand, in some Emerging Market Economies (EMEs), notably China, there is evidence of “over-investment”.

Figure 1: Total investment volume
(per cent of GDP)

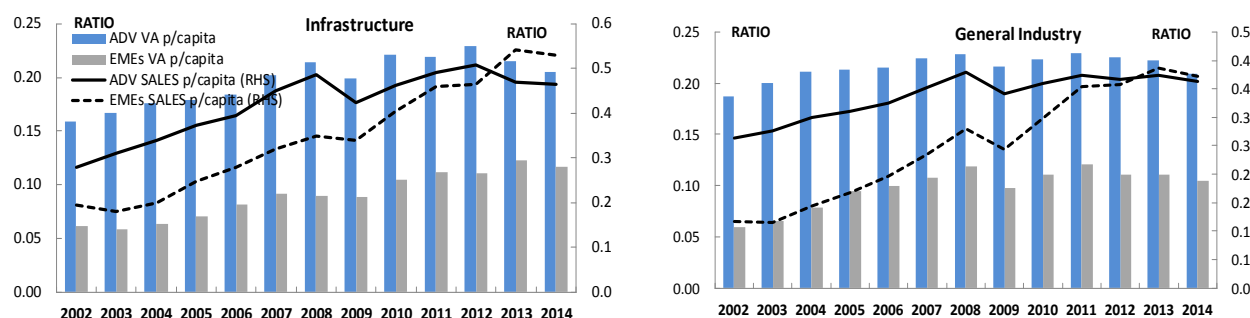


Source: Economic Outlook, November 2014

20. **Investment by large firms in advanced economies has lagged in recent years.** Evidence using individual firm data for large 10 000 listed companies across 75 countries, whose total value-added is approximately 36% of world GDP, shows that impediments to stronger corporate investment by large companies in OECD countries are not due to a shortage of financing. Their operating cash flow is sufficient to cover capital expenditure.

21. **The perceived stagnation of corporate investment in advanced economies may be due in part to a shift in multinational enterprises' activities,** notably through transfer of intellectual property towards emerging markets economies as part of Global Value Chains (GVCs). This has resulted in ‘catch-up’ of sales-per-employee in EME’s companies as well as cash benefits for advanced economies' companies. At the same time, value-added per employee (productivity) in EMEs is not catching up, consistent with declining transfers of intellectual property and low investment in the R&D and innovation necessary to drive long-term productivity growth (Figure 2).

Figure 2: The global productivity catch-up in sales



Source: Bloomberg, OECD calculations.

Investment by SMEs continues to face serious financing constraints

22. **Small-and medium-sized enterprises (SMEs) generally face relatively greater financing challenges.** SMEs and young firms play a significant role in OECD and non-OECD economies as key generators of employment and income, and as drivers of innovation and growth. Improving the performance of SMEs and the creation of new start-ups by enabling them to finance their investments is an essential part of efforts to foster new sources of inclusive and green growth. SMEs financing remains more constrained than before the crisis in absolute terms. For example, according to a 2014 survey of the EU-28,

only a small minority of SMEs reported having used (or considered using) financing instruments such as equity (16%) or debt securities (4%), with bank loans (57%) and overdrafts or credit lines (53%) being the most frequently cited instruments (ECB/EC, SAFE, 2014). As banks continue to deleverage from their excessive pre-crisis debt levels to meet business and regulatory requirements, SMEs may increasingly find it hard to tap bank financing and thus need to diversify their sources of funding.

FDI flows remain subdued, but financing structures have become increasingly complex

23. **Aggregate FDI flows are also below their pre-crisis levels, although they advanced modestly in 2014** to reach USD 325 billion in the second quarter. FDI inflows in the EU, in particular, fell from USD 857 billion in 2007 to USD 208 billion in 2013. When new ways of measuring FDI are used, stripping out global investment related to the activity of special purpose entities (SPEs), global FDI inflows are even smaller, although this effect varies significantly across countries as well as across time. The large (more than half) and long-standing role played by mergers and acquisitions (M&As) in FDI flows suggests, however, that FDI is not making as important a contribution to expanding productive capacities and creating jobs as it could. Furthermore, the high share of cross-border M&A, consisting of deals between multinationals as well as the growing volumes of cross-border divestments (when multinationals sell off international assets), are both trends that suggest we are currently in a restructuring phase of globalisation rather than a growth phase. Moreover, the use of SPEs in complex FDI arrangements has been raised as a source of concern in the context of the OECD Action Plan on BEPS, when such complex arrangements fuel tax treaty abuse and/or harmful tax practices.

Bold policy responses are needed...

24. **Supporting investment requires a combination of macroeconomic policies and structural measures targeted at removing some of its most persistent obstacles** to ensure optimal framework conditions. Besides fiscal and other demand-side policies, it is important to remove such supply-side obstacles (such as burdensome, overly complex or unpredictable regulations, and poorly functioning product and labour markets), including in the sectors with strong knock-on effects on other sectors of the economy such as network industries (telecoms, electricity, and transport) and trade-related services, like financial services and logistics.

25. **Policy solutions have to take into account the fact that investment decisions have become truly global.** Not only do multinationals allocate investment irrespective of frontiers, but also global-value chains have become key drivers of both business investment and demand at local level. This globalisation of investment decisions increases the range of domestic policies that may directly influence the location of investments, including policies on trade and financial openness, as well as regulatory frameworks conducive to legal certainty and sound financial systems. It is important to have sound, fair and transparent regulatory frameworks at the national level, particularly as concerns financial regulation. In this regard, ongoing work on international regulatory cooperation, aimed at minimising unnecessary regulatory barriers to cross-border investment and reducing risks, including that of the Basel Committee on Banking Supervision and the Financial Stability Board, is highly relevant. The goal is to avoid excessive short-term volatility of cross-border investment flows while increasing the stability of the global financial system.

...like promoting competition

26. **Competitive markets provide opportunities for efficient companies to reap the benefits of their investments, enhancing both productivity and growth.** When competition is restricted, which can arise from unduly restrictive regulations, even efficient companies will not invest because of uncertainty and because they cannot enter and expand at the expense of less efficient rivals. OECD research shows that pro-competitive changes in product market regulation can raise GDP in OECD countries by over 8% and in some large emerging economies by as much as 30% (OECD, 2013a). The OECD has developed a manual for governments – the Competition Assessment Toolkit -- to help them identify, assess and revise

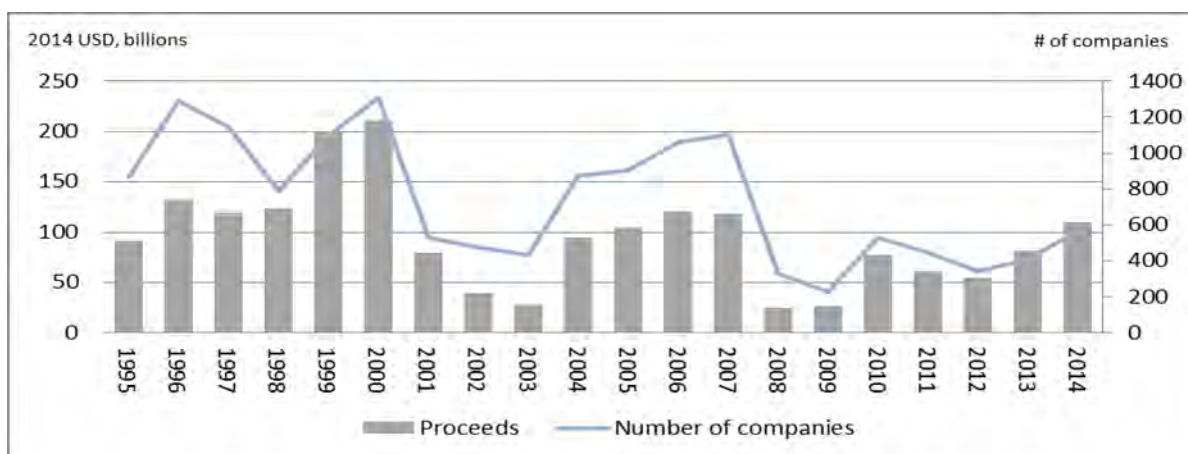
regulations that create barriers to competition. The OECD is also increasingly being called on to advise individual countries on broad sectoral reviews of regulation.

27. **Fair competition requires a level playing field between the private sector and state-owned enterprises (SOEs).** SOEs now account for over 20% of the world’s largest enterprises. Their share of capital formation and international investment is approaching similar levels. To stimulate investment and growth, there is a need to ensure that SOEs operate efficiently and to promote fair competition between public and private firms, avoiding the crowding out of potentially more efficient business, whether public or private. The updated OECD Guidelines on Corporate Governance of State-Owned Enterprises (OECD, 2015b) will provide guidance to achieve both. In addition, preparatory work is underway on the “SOEs in the Global Marketplace” initiative to address these issues in a comprehensive and coordinated fashion.³

...ensuring capital markets foster productive investment

28. **Public equity markets have for decades been seen as an efficient mechanism for funding corporate investments.** However, the number of stock market listings has been trending lower since 2000 (Figure 3). This trend has been accompanied by an increase in the average size of initial public offerings. The hurdle for smaller companies to list their shares on stock markets might have become higher due to more robust listing and corporate governance requirements imposed on public companies, but also because of changes in market structure, trading practices and investment strategies among large institutional investors over the last decade. There is a need to align the incentives in the investment chain, so that both investors and corporations are focused on long-term value creation. The 2015 update of the OECD Principles of Corporate Governance includes recommendations on how corporate governance frameworks should provide sound incentives throughout the investment chain, including on how stock markets function in ways that contribute to good governance in support of investor confidence, economic growth and job creation. Judicious regulations can also contribute to improved financial intermediation that supports productive long-term investment.

Figure 3: New stock market listings by non-financial companies in the OECD
(USD Billions)



Source: Thomson Reuters, OECD calculations.

³ The initiative will explore: (1) how best to address concerns about maintaining a level playing field when SOEs operate across borders; and, (2) how to ensure that the international trade and investment environment remains open and welcoming to foreign SOEs?

...diversifying SME financing

29. **Concerted policy effort is need to improve access to, and conditions of, SME financing.** Bank financing will continue to be crucial for SMEs and it is essential to restore banks' health. However, SMEs need to diversify their sources of finance towards non-bank instruments, and tap sources of private investment, such as capital from institutional investors, reducing their over-reliance on bank lending. This is particularly important for start-ups and innovative high-growth firms.

30. **Several actions could support the development of a diverse set of finance instruments for SMEs.** On the regulatory side, sensible and balanced calibration of the existing regulatory frameworks affecting such instruments could provide further support, particularly given the potential role of institutional investors in providing alternative sources of SME financing. Further support for the development of market-based financing alternatives for SMEs can be had from increased transparency through better credit risk assessment; and addressing SMEs' apparent skills gaps through improving financial literacy. More broadly, there is a need to ensure a diversity of financing options for firms across their life cycle. OECD analysis of the modalities of the various financing options has identified the challenges to uptake and the enabling factors, which could promote the development of these instruments (OECD, 2013b; 2014a).

... improving the investment environment

31. **The OECD Policy Framework for Investment (PFI) aims to mobilise private investment to support steady economic growth and sustainable development,** contributing to global economic and social well-being (see Annex III). Members and Partners are also encouraged to use the PFI as a reference in designing and implementing their investment climate reforms as well as for their development co-operation programmes to foster investment and private sector development. The PFI has so far been used by 30 developing and emerging economies, as well as regional economic communities, such as the Southern African Development Community and the Association of Southeast Asian Nations, to improve their investment climate. The instrument has been updated in 2015 to further address critical investment issues, including in relation to climate change, infrastructure, SME financing, competition, capital markets governance, and helping firms upgrade in global value chains. The updated PFI will also strengthen development co-operation programmes of bilateral and multilateral donors, helping to improve the enabling environment for investment.

32. **Several actions have been identified to further disseminate and promote the effective use of the PFI, including:** i) encouraging greater use of the PFI by more developing and emerging economies, such as through carrying out OECD Investment Policy Reviews; ii) strengthening the follow-up to PFI-based recommendations, such as those emerging from OECD Investment Policy Reviews and sector-specific reviews, and in the context of the Organisation's regional programmes and bilateral projects; iii) encouraging development partners, such as bilateral aid agencies, to use the PFI as a tool for development co-operation programmes in assisting developing countries improve their investment climate; and, iv) further considering methodologies to assess the impact of policy recommendations based on the PFI, in consultation with stakeholders and in close coordination with other international organisations.

...and, boosting investment in infrastructure

33. **There remains significant scope to boost institutional investment in infrastructure, including for climate resilient infrastructure.** As economic actors, the importance of institutional investors has never been greater: total assets under management stood at USD 57 trillion at the end of 2013 – a number that was 120% of the GDP of the OECD as a whole. The OECD estimates that globally, annual infrastructure investment needs will average 3.5% of GDP through 2030. Cumulative investment of USD 53 trillion in energy supply and efficiency will also be needed by 2035 to keep global warming below 2°C. However, in spite of such critical needs, the ratios of fixed investment to GDP are historically low in some

of the world's largest economies, FDI flows are still 40% below their pre-crisis level and the share of FDI in infrastructure has decreased in recent years. While it may be the case that several Canadian and Australian pension funds invest as much as 10% of their assets in infrastructure projects, in general, (direct) investment in such projects remains low—according to OECD data on large pension fund investments, it typically accounts for less than 1% of assets. The OECD/G20 High Level Principles on long-term investment financing by institutional investors aims to facilitate a better matching between this large source of capital and assets and sectors in need of investment, such as infrastructure. Beyond infrastructure, the G20 High Level Principles also provide guidance on other aspects of long-term investment – including inter alia, long-term asset management mandates and integration of environmental, social and governance criteria in investment policies. Going forward, the OECD will also actively contribute to the work of the G20 Global Infrastructure Hub.

34. Building a sound governance framework is a critical enabler of infrastructure investment.

Cost efficient and effective infrastructure procurement and management depends on appropriate regulation, competent regulatory authorities, judiciary quality, and public sector capacity to procure, budget and manage fiscal risks. Infrastructure projects will often cut across levels of government and therefore planning, co-ordination and co-financing arrangements have to be in place between national and sub-national authorities. In addition, the increasing use of PPPs introduces new challenges in terms of affordability and value for financing infrastructure investment. The OECD governance framework for the development and management of infrastructure projects will provide decision makers with a checklist of governance ‘must haves’ for infrastructure development and management. The goal is to clarify the objectives of infrastructure investment, analyse the challenges and opportunities, and map out options to solve challenges while providing guidance during the whole life of the asset (OECD, 2015c). This work has also informed the elaboration of the ASEAN Principles for Public-Private Partnership (PPP) Frameworks.

A broad dialogue on investment is needed

35. Dealing with the above investment issues will require an optimal mix of structural reforms, and an open and comprehensive exchange of views among Members and Partners

to identify policies that can improve the effectiveness of public investment and increase private investment. Following recent meetings of the Investment Committee and its bodies, there is a growing interest to explore the possibility of enhancing the inter-governmental and multi-stakeholder dialogue on investment treaties taking place at the Freedom of Investment (FOI) Roundtable framework. This international investment dialogue would discuss how to improve the global investment climate, while at the same time ensuring that investment contributes to sustainable development. The dialogue would be inclusive and comprehensive and engage Member and Partner countries through the FOI process. To support these efforts, the OECD could identify the net benefits of investment treaties; explore technical aspects linked to the different approaches to legal issues across jurisdictions; explore ways to emphasise RBC in the context of investment treaties; and demonstrate the importance of a conducive business climate to supporting investment. These discussions would not be a negotiation, or even the preparation of negotiations, but would be rather of a technical nature so as to inform the development, for example, of treaty provisions in a non-prescriptive way.

Questions for Discussion Section 3.1:

- *How do Ministers explain the weakness of global investment? What approaches are Governments taking in order to boost investment?*
- *How can the investment climate be improved, including through the use of tools such as the updated PFI?*
- *How could the OECD, building on the work of the FOI roundtable, best support an inter-governmental and multi-stakeholder dialogue on investment treaties and on improving the business climate?*

- *What approaches are governments taking to support the diversification of SME finance sources? What measures could help SMEs better tap capital markets to meet their investment needs?*
- *How can we ensure a level playing field between private and SOE firms?*

3.2) Investment in innovation to foster productivity

36. **New sources of growth are urgently needed to help recover from the economic crisis and strengthen long-term productivity growth.** With demographic shifts, resource scarcity and the changing climate all creating further pressures, new solutions are needed to achieve sustainable long-term growth. Innovation – which involves both the creation and diffusion of new products, processes and methods – is a critical part of the response and provides the foundation for new businesses, new jobs and higher productivity. Innovative economies are more competitive, more resilient and better able to support high living standards. The updated OECD Innovation Strategy (2015) analysis of the digital economy, and work on long-term productivity, provide new insights for policy makers on how to drive innovation and increase productivity in the future.

37. **OECD analysis finds that productivity growth among firms at the global technology frontier⁴ has remained relatively robust in the 21st century, despite the relative weak productivity growth in OECD economies over the past decade.** The strong performance of the global frontier firms is linked to the fact that these firms are typically larger, more profitable, and more likely to patent than other firms. Moreover, they are on average younger, consistent with the idea that young firms possess a comparative advantage in commercialising more radical innovations. They also tend to be large transnational corporations. These features hint strongly at the importance for these firms of investing in knowledge-based capital and harnessing the efficiencies of digitisation, including the ability to orchestrate competencies across the globe into their value chains.

38. **However, the gap in productivity growth between firms at the global frontier and other firms has increased since the beginning of the century** (Figure 4). This raises questions about the ability of: i) the most advanced firms to adopt new innovations developed at the global frontier, a factor particularly important for advanced economies; and, ii) the diffusion of existing innovations from national-frontier firms to laggards. In policy terms, the first dimension is largely a function of openness, with exposure to international trade and foreign direct investment and integration in global value chains (GVCs) being key factors allowing firms to benefit from the global technology frontier. However, this is complicated by the importance of tacit knowledge, which may be less easily absorbed through trade and investment flows and may require more active measures. The second dimension is determined in large part by the capacity and incentives for the most dynamic firms in an economy to upscale, and the ease with which resources are reallocated away from less productive firms.

39. **Firms' incentives to adopt frontier innovations, and the aggregate impact of doing so, depend crucially on the ability of economies to reallocate scarce resources to their most productive uses.** However, relatively high rates of skills mismatches (see section 3.3) in some OECD countries are a barrier to the growth of innovative firms and the widespread diffusion of frontier innovations. Government support measures need to be carefully designed so that they do not contribute to excess capacity in certain

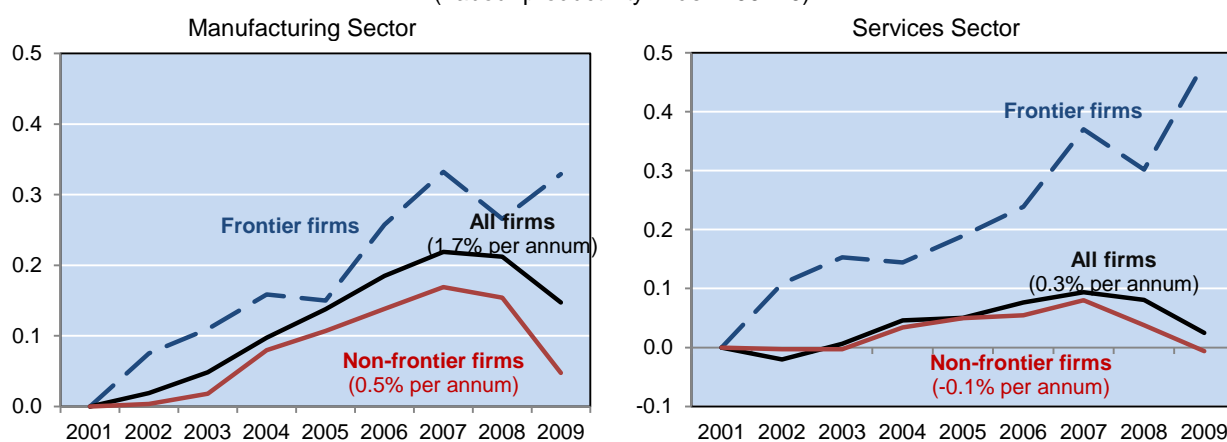
⁴ A firms' distance from the global technology frontier matters for innovative firms. The firm's productive capability is proxied by how far its productivity level (measured either by turnover per employee or value added per employee) is from the top productive firms worldwide. Firms with a large productivity gap at the beginning of the period are considered far from the technology frontier, while those on a par with or with a small productivity gap compared to the top productive firms are close to the technology frontier.

industries, thus hampering the efficient reallocation of resources. Furthermore, while young firms are important for innovation, their growth is limited in some OECD countries, which is problematic since firms at the national frontier typically need to achieve sufficient scale before they can enter international markets and benefit from innovations at the global frontier.

40. **Structural reforms in product, labour and financial markets are important to enable resources – capital and labour – to flow to the most productive firms.** Well-functioning product, labour and capital markets, as well as policies that do not trap resources in inefficient firms – including efficient judicial systems and bankruptcy laws that do not excessively penalise failure – are central. Moreover, despite the importance of young firms for innovation and employment generation, policies in many countries often favour incumbents, and do not always enable the necessary experimentation with new ideas, technologies and business models that underpins the success of young firms.

Figure 4: Solid growth at the global productivity frontier but spill overs have slowed down

(Labour productivity: index 2001=0)



Notes: “Frontier firms” corresponds to the average labour productivity of the 100 globally most productive firms in each 2-digit sector in ORBIS. “Non-frontier firms” is the average of all other firms. “All firms” is the sector total from the OECD STAN database. The average annual growth rate in labour productivity over the period 2001-2009 for each grouping of firms is shown in parentheses.

Source: OECD (2015), *The Future of Productivity Growth*.

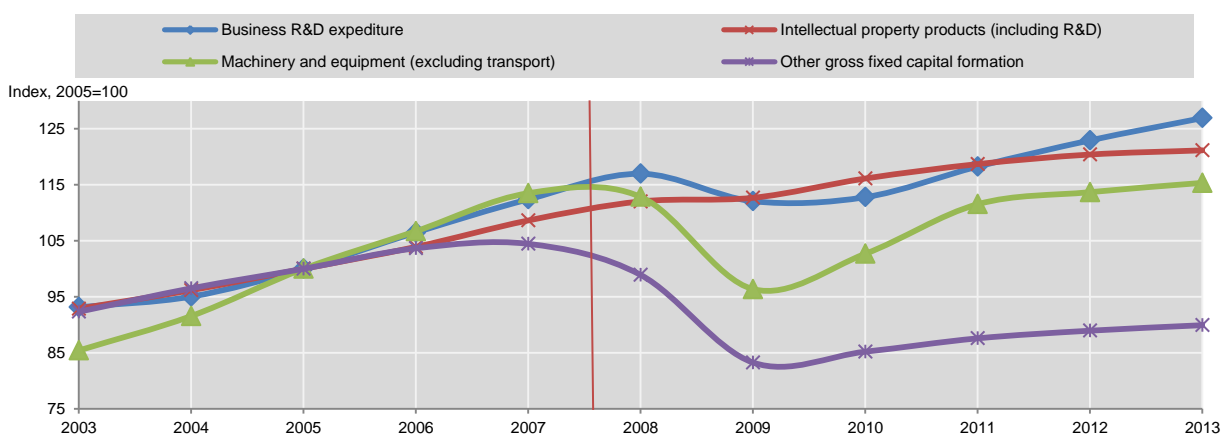
41. **Getting policies for innovation and productivity right is all the more important in a context of rapid technological change to help foster the ‘Next Production Revolution’.** Successful deployment of new technologies and business models by both existing firms and young challengers requires innovation-friendly regulation consistent with a data driven economy, as well as efforts to improve the quality of human capital. The continued spread of the digital economy and the proliferation of massive volumes of data have the potential to transform many industries, including transport, manufacturing, health and education. These and other technological changes (e.g. in biotechnology, nanotechnology, robotics and the production of advanced materials) will not only lead to transformations in production, but also in the jobs associated with that production, their location in global value chains (GVCs), their environmental impact, and the respective roles of manufacturing and services sectors in the economy. The digital economy is key to innovation as almost no business today is run without the help of ICTs. To reap the benefits from this technology for future growth and to support job generation, policymakers will need to keep the Internet open, and provide sound policy frameworks for its governance, e.g. related to access, privacy, security and trust. Investment in new infrastructure like broadband, spectrum and new Internet addresses is key for digitally enabled innovation.

42. **Sound frameworks to foster investment in innovation are also important.** A large share (in some cases, more than half) of business investment in advanced economies is in knowledge-based capital

(KBC), i.e. software, data, R&D and intellectual property (IP), branding, firm-specific skills and organisational capital. While such investments have grown less rapidly over the past few years, they have been more resilient than investment in fixed capital (Figure 5). However, policy frameworks do not always reflect the importance of KBC investment in the 21st century. For example, firms today rely on a wide range of intellectual property rights (IPR) to protect their investments in innovation, but, globally, existing IPR policies are not always well suited to the fast-changing nature of innovation today. Ensuring a well-functioning IPR system is therefore an important priority for policy. Moreover, business investment in KBC must go hand-in-hand with sufficient and well-designed public investment in (especially basic) R&D, education and knowledge infrastructures (e.g. broadband networks).

43. **OECD analysis confirms the importance of investment in basic research.** Basic research drives long-run productivity growth by providing the ingredients for innovation at the global frontier, and facilitates the adoption of innovations across the economy. Both direct public funding and public private partnerships (PPPs) are needed to address the inherent under-investment in basic research by private firms, linked to the large knowledge spill overs from such research. Long-term funding for ‘curiosity-driven’ research must be preserved, as this has been the source of many such innovations in the past, and can help offset the growing focus of business on the short term. At the same time, more project-based funding can allow for greater direct steering of public research towards major public policy objectives. PPPs can help organise such objective-oriented fundamental research, while simultaneously enhancing the chances for this type of research feeding into innovations.

Figure 5: Business investment in knowledge assets weathered the crisis better
(OECD, Index, 2005=100)



Source: OECD (2014), Science, Technology and Industry Outlook

44. **In implementing specific innovation policies, such as R&D tax credits and grants, and to sustain future productivity growth, governments must have an eye to effectiveness.** A focus on high social returns and international good practices in designing such policies is essential. It is also important to ensure that innovation policies are not captured by vested interests and serve to support challengers, e.g. young firms and new market entrants, as well as more radical innovation. Putting innovation at the centre of policymaking in a longer-term perspective will help ensure policy coherence, since innovation policies cross government portfolios and affect a wide range of stakeholders. Strong leadership at the highest political levels, plus enabling regional and local actors to foster innovation in a co-ordinated fashion, is also essential. Finally, preparing for continued technological change will require sound and stable policy frameworks, but also continued learning from, experimentation with and improvement of policies over time. Incorporating policy monitoring and evaluation at the design stage of policymaking will enable such policy learning over time.

45. **There is a need to strengthen the evidence base for innovation policy and support countries in the development and implementation of their policies.** The OECD can help Members and Partners enable the ‘Next Production Revolution’ by identifying science and technology-driven developments in selected production technologies over the next 10-15 years, and focusing on disruptive technologies that could have far-reaching effects on productivity and economic growth. This effort will also identify the risks and opportunities (economic, environmental, and social) created by these developments, and examine policies that enable countries to maximise the net benefits for their economies and societies.

Questions for discussion Section 3.2:

- *What policies promote or inhibit the realisation of new opportunities for innovation? How can innovation and long-term productivity growth be strengthened?*
- *What policies are needed to close the gap in productivity growth between firms at the global frontier and other firms? How can the potential of innovative young firms to generate employment and innovation be realised?*
- *What policies can best harness the opportunities of the digital economy?*

3.3) Investment in skills

46. **Continued improvements in human capital will be required not only to support individual opportunity and social cohesion, but also to drive economic growth,** which has become increasingly reliant on innovation-driven gains in multifactor productivity, and the accumulation of knowledge-based capital (KBC), such as computerised information or intellectual property rights, rather than on the accumulation of labour and capital. While this process is quite advanced in OECD countries, it is increasingly salient in emerging and middle-income countries. Ensuring that the benefits of this growth are widely shared will require policy efforts to both broaden participation in the labour market among women and traditionally disadvantaged groups and to improve job quality for all workers.

47. **Young people have been hit hard by the global economic crisis and the ‘scars’ remain:** youth unemployment rates remain high in most OECD countries – two to three times the adult rates – and more than 15% of young people aged 15 to 29 were neither in employment nor in education or training (NEET) in 2013. Low educational attainment and a lack of relevant skills are two related major contributors to poor employment outcomes for youth.

48. **The risk of being in a low-paid job or out of work altogether and not studying is highest for those with low educational attainment and low skill levels.** As set out in the OECD Action Plan for Youth adopted by Ministers in May 2013, it is essential that all young people are equipped with good foundation skills that will enable them to create and seize economic opportunities. The impact of skills goes far beyond earnings and employment as skills enhance both an individual and society’s well-being in a number of ways. OECD’s Survey of Adult Skills shows that individuals with higher levels of literacy are more likely than those with lower literacy skills to report good health, to believe that they have an impact on political processes, and to participate in associative or voluntary activities. In most countries, they are also much more likely to trust others. Despite significant progress in equipping young people with solid foundation skills, much remains to be done to reduce skills gaps.

49. **Persistent skills mismatches bring considerable costs.** At the individual level, less skilled workers face lower earnings and job satisfaction, as well as a higher risk of unemployment. For employers, recruitment costs rise and productivity and product/service quality can suffer, leading to a potential loss of competitiveness. Skills mismatch can result in higher aggregate unemployment, lower economic growth and greater earnings inequality. There is evidence that low levels of education tend to be perpetuated

across generations, especially countries with high levels of inequality where less educated parents cannot invest in the high quality education of their children, which in turn constrains their potential to move up the income ladder (Cingano, 2014). When large numbers of people do not share the benefits that accrue to more highly skilled populations, the long-term costs to society – for example, in terms of healthcare, unemployment and security– accumulate.

50. **The scope for investment in skills to boost economic growth and social outcomes is significant** A 2010 OECD study suggested that for a person born that year, GDP per capita would be expected to be about 25% above the “education as usual” level by the end of their expected life in 2090 if the country made a 25-point increase in its PISA scores (OECD, 2010a). Non-monetary returns to education are also very large. For instance, in OECD countries, each additional year of education after primary school is associated with more than half a year of additional life expectancy.

51. **However, investing merely in developing more of the same skills is unlikely to be a ‘magic bullet’.** Skills are of little economic value if they remain outside or on the margins of the labour market, or if they are not used effectively in the workplace. Societies that see widening gaps across the population face deteriorating social cohesion and well-being. When in employment, many young people are either in precarious jobs that do not make full use of their skills, or are mismatched in terms of their skills and qualifications. As unused skills are likely to atrophy, this undermines their long-term employability. In some cases, additional measures will be required to get youth into the labour market in the first place. In others, the focus will need to be on getting employers to make better use of the skills of young workers. In line with the OECD Skills Strategy endorsed by Ministers in 2012, policy responses should address a range of aspects.

52. **Education systems can help people develop the right skills by taking a more holistic approach to skills** (including social and emotional ones), developing work-based learning in vocational education and training and in university programmes, providing effective guidance on study choices and having real ‘second chance’ options. Building multiple pathways within the education system, with good bridges between them, provides greater opportunities for all youth to succeed. Governments will also need to do more to strengthen the skill requirements of jobs. This takes the policy discussion to the heart of what goes on in the workplace: the role of leadership and management, incentives for firms to innovate and adopt new technologies, how work is organised, job design, internal mobility, and personnel and recruitment policies more generally.

53. **Efforts to reduce skills mismatches can and should be scaled up.** This will require making skills systems better at anticipating and responding to employers’ changing skills needs. Policies to improve the matching of youth to jobs include the provision of good quality career guidance services, backed up with high quality information about careers and labour market prospects, to help young people make better career choices; and providing on-the-job training and life-long learning to reduce skills mismatch. Interventions are needed to make sure that the skills of youth are activated by improving opportunities and giving greater help to find work. This will involve a mixture of measures aimed at addressing labour costs where these are too high, tackling poor work incentives, providing effective labour market measures, as well reshaping labour market policy and institutions to facilitate access to employment.

54. **Specific measures to improve the skills of distinct groups need to be taken.** Ensuring that all social groups have equal access to education can help promote their participation in the labour market. In most countries, teachers and schools need to do more to help girls see science and math as not just school subjects but as essential to their career and life opportunities (OECD, 2015f). The OECD Gender Initiative’s specific recommendations to improve gender equality in education, employment and entrepreneurship are timely given that women remain severely under-represented in the science, technology, engineering and mathematics (STEM) fields of study and occupations.

55. **People need to continue learning throughout their lives.** Effective learning strategies can – and should – be taught, taking into account of what happens in the workplace. Even though learning can take place in many settings, and experience can be a great teacher, work-based learning, for instance through quality apprenticeships, is of particular importance in this regard. Often what people learn informally is not easily recognised. Education and training providers need to be more flexible and responsive to diverse learners and diverse learning needs so that people can strengthen their cognitive skills at any time as well as develop new technical and professional skills.

Questions for discussion Section 3.3:

- *How can governments widen access to education and help young people develop the right skills to better match the needs of a country's economy? What policy levers are effective in improving skills use at work?*
- *What policies are needed to promote a learning society? What are the most effective strategies to address the needs of different groups of learners?*
- *How can the efficiency of investment in education be maximised?*

3.4) Improving the business climate and promoting responsible investment

56. **A healthy business climate, free of corruption, fraudulent practices and distortive government support measures, supports sustainable investment and economic growth.** While governments assume primary responsibility for improving framework conditions and the business climate, the private sector must also share responsibility. When business leaders choose to steer their companies toward integrity and take due account of social and environmental concerns, they increase their company's potential to have a positive impact on our markets, governments, societies, and our environment.

57. **Governments have recognised this potential** and are strengthening enforcement of laws and fighting corporate misconduct. Pursuant to the obligations under the *OECD Anti-Bribery Convention*, 333 individuals and 111 entities have been sanctioned in 17 jurisdictions since 1999 for offences relating to foreign bribery schemes around the world (OECD, 2014c). Penalties applied to banks for misconduct are reported to have reached €163 billion over the past five years (ESRB, 2014). The number of jurisdictions with competition law enforcement has grown from fewer than 20 in 1990 to about 120 in 2014 (OECD, 2014d). To strengthen this trend, the OECD adopted in 2014 a Recommendation on International Co-operation on Competition Investigations and Proceedings.

58. **Businesses are also redoubling their integrity efforts, but an implementation gap persists.** Compliance industry surveys show that investment in the field has risen as much as 25% since 2010, reflecting, in part, enterprises' efforts to comply both with an increasingly complex regulatory environment and to address the realities of doing business in a multifaceted world economy. Yet, these efforts are undermined when, whether by error, neglect, or by choosing to engage in reckless risk-taking, companies engage in corporate misconduct.

Closing the implementation gap for more Responsible Business Conduct

59. **Overcoming these challenges will require renewed efforts from business and governments.** The OECD has a wealth of legal and policy instruments on business integrity practices, but there is a need to reinforce efforts to close the gap between these instruments and what is being done by businesses to implement them.

60. **The 2013 MCM recognised the importance of trust as a crucial enabler of policy success in creating jobs and promoting greater equality.** At the MCM 2014, Ministers again underlined the importance of trust for inclusive and resilient societies. Building on the work of the Corporate Governance Committee (CG), the OECD is exploring how to restore and strengthen trust by bridging the implementation gap in the application of international rules and recommendations for business conduct. The Trust and Business (TNB) project aims to support the implementation of the recommendations set forth in instruments like the OECD Anti-Bribery Convention, the OECD Guidelines for Multinational Enterprises, the OECD Principles of Corporate Governance, and others. It aims to contribute to sound risk-management and stronger internal controls in companies and explore ways to better integrate these functions into a company's corporate governance, strategy and culture.⁵

61. **Tackling corruption is key to restoring citizens' trust in market and governance institutions.** This requires a full understanding of both the supply and demand drivers of corruption, in public and private sectors, as well as its impact on economic incentives, investment and growth. The OECD is exploring ways to strengthen the connectivity and coherence between all areas of relevant expertise in the Organisation, including public sector integrity, foreign bribery, tax measures for combating bribery, official export credit supports and bribery, illicit flows in relation to official development assistance, anti-competitive conduct, as well as the *CleanGovBiz* Initiative. The goal is to help Members consider more effective policies to help promote integrity in the public and private sectors and support global anti-corruption efforts using the OECD's evidence based approach. As part of these efforts, the Secretary-General has convened an informal high-level advisory group on anti-corruption⁶ to help in the identification of related issues that may be brought to Members' attention.

62. **The OECD Guidelines for Multinational Enterprises are the most comprehensive international instrument on Responsible Business Conduct (RBC) and the only one that offers a grievance mechanism** through the National Contact Points (NCPs) in adhering countries.⁷ The Guidelines provide recommendations on all areas of business ethics, including corporate steps to obey the law, observe internationally recognised standards and respond to other societal expectations. They thereby contribute to strengthening the basis of mutual confidence between enterprises and the societies in which they operate. Moreover, specific guidance developed through multi-stakeholder advisory groups on how to implement the Guidelines (the 'proactive agenda') throughout supply chains in the extractive, textiles, agricultural and financial sectors further helps enterprises meet their responsibilities.

63. **International business has experienced far-reaching structural change and the Guidelines themselves have evolved to reflect these changes.** The grievance mechanism offered by NCPs contributes to the effective implementation of the Guidelines as reflected in the over 300 complaints received by NCPs relating to business operations in over 90 States and jurisdictions. At the same time, there is an uneven performance between National Contact Points. There is, therefore, a need to strengthen the NCP system inter alia by providing adequate means and resources so NCPs can effectively discharge their functions; identifying and addressing obstacles that hinder their performance; facilitating exchange of best practices; and supporting capacity-building initiatives. The OECD Declaration on International Investment remains of crucial importance. Efforts to widen adherence to the Guidelines for Multinational Enterprises should be encouraged, and the OECD could develop options in this regard.

⁵ See <http://www.oecd.org/daf/ca/trust-business.htm>

⁶ The Group met for the first time in March 2015 during the OECD Integrity Week.

⁷ All OECD countries and 12 non-Member countries have adhered to the MNE Guidelines.

Ensuring tax transparency

64. **The international tax system supports economic growth by establishing measures to reduce tax barriers to cross border trade and investment.** The OECD-G20 Base Erosion and Profit Shifting (BEPS) Project is delivering a package of measures to close the loopholes that allow the artificial shifting of profits to low or no tax jurisdictions by restoring coherence to the international tax rules, ensuring that profits are taxed where the economic activities and value creation occur and through increased transparency. These measures will also include the development of a Multilateral Instrument to streamline the implementation of the treaty-related BEPS measures. The full package of BEPS measures, which are being developed by over 60 countries working together, including a number of developing countries, will be finalised by end-2015. Negotiations of the Multilateral Instrument will begin in 2015 and continue in 2016 together with other potential post BEPS-related work.

65. **OECD work on exchange of information and tackling serious financial crimes like tax evasion is progressing.** On the tax and crime front, the OECD launched in 2011 a global dialogue on fighting tax evasion and other financial crimes with a ‘whole-of-Government’ approach. With the support of the G20, this dialogue provides an important institutional platform for the fight against financial crime, including tax crime, money laundering, corruption and organised crime. The 126-member Global Forum on Transparency and Exchange of Information for Tax Purposes is closely monitoring the commitments to the tax transparency standards, including the new Standard on Automatic Exchange of Information delivered in 2014, which more than 93 States and jurisdictions have already committed to implement. The next step is to secure commitments to rapid implementation of the AEOI Standard, including the necessary IT arrangements, based on a timetable that will see first exchanges of information beginning in 2017 and 2018.

Questions for discussion Section 3.4:

- *How can the OECD provide enhanced support to countries’ anti-corruption efforts? How can the Organisation help to ensure a more coherent and strategic approach to doing business with integrity?*
- *How can wider adherence to the Guidelines for Multinational Enterprises be facilitated? How can the system of National Contact Points be strengthened? How can efforts be stepped up to encourage wider adherence to the OECD Investment Declaration?*
- *How can the OECD support the implementation and administration of BEPS measures in adhering countries once agreed? How to encourage a broad and quick implementation of the AEOI standard?*

ITEM 6: INVESTING FOR A LOW-CARBON ECONOMY – SAVING RESOURCES, GREENING INVESTMENT

66. **This Item reflects on the need to better align policies to tackle the global threat of climate change and the associated challenge of transitioning to a low-carbon economy.** It calls attention to the need to track climate finance flows and to address the water-food-energy nexus.

67. **Protecting the planet’s precious natural capital, containing global warming below the agreed 2°C target and ensuring people’s living standards are not undermined by a deteriorating environment will require action across a wide range of policy areas.** This insight underpins the joint OECD, IEA, NEA and ITF project on *Aligning Policies for the Transition to a Low-carbon Economy* (APT) [[C/MIN\(2015\)11](#)]. More countries are implementing core climate policies: carbon pricing including through emission trading schemes, energy efficiency measures, regulatory intervention and targeted support to innovation in, and deployment of, low-carbon technologies as well as promoting investment in renewables. But, the trend of rapidly rising global greenhouse gas emissions needs to be reversed to avoid severe and irreversible climate change impacts.

68. **Climate change is a transformational agenda that requires policy action now.** The APT report provides a broad diagnosis of misalignments between overall policy and regulatory frameworks and climate goals, offering a new approach to facilitate the implementation and improve the effectiveness of climate action. A clear understanding of key misalignments in each country, and options to address them, may help governments move towards more ambitious contributions in light of the upcoming 21st Session of the Conference of the Parties to the United Nations Framework Convention on Climate Change (COP21) in Paris, while also achieving other social and economic goals. Investments to drastically curb emissions are economically wise investments, as shown in the APT report.

69. **Investment policies that encourage the development and deployment of environment-friendly technologies and infrastructure will be a crucial ingredient in the policy response to climate change.** Private sector investment will be needed in order to achieve the transition to a low-carbon economy and manage the effects of a changing climate. It is the responsibility of governments to ensure the business climate is conducive to such private sector investment, including through the use of market based instruments and effective price signals. Climate change, coupled with a rising global population and increasing demand for resources, will sharpen competing economic, social and environmental demands. At the heart of these pressures lies the water-energy-food nexus. Managing these competing pressures will require the close attention of policy makers in developed, emerging and developing economies alike. Risk prevention and building resilience are key responses to handle these challenges

6.1) Aligning policies to facilitate the transition to a low-carbon economy

70. **At their 2014 annual meeting, OECD Ministers declared “Climate change is a major urgent challenge”** and reaffirmed their common resolve to pursue ambitious and cost-effective policy responses, inviting the OECD, IEA, NEA and ITF to examine how to better align policies across different areas for a successful economic transition to sustainable low-carbon and climate-resilient economies. While more countries are taking action to reduce emissions (e.g. carbon pricing including through emission trading schemes, energy efficiency measures, and other market-based instruments, fossil fuel subsidy reform, regulatory intervention, targeted support to innovation in and deployment of low-carbon technologies), key obstacles to climate policy effectiveness persist. Among the most important is the fact that broader policy frameworks and economic interests continue to be geared towards fossil fuels and carbon-intensive activities.

71. **Inadvertently or not, such “misalignment” in existing policy frameworks hinders low-carbon investment and consumption choices.** If governments could identify and remove some of the misalignments embedded in their overall policy mix, climate policies would be easier and less costly to implement. Pricing and subsidy reform are at the very heart of that policy mix. Aligning policies for a low-carbon economy can also contribute to a broader reform agenda for more robust, resilient, sustainable and inclusive growth. Beyond avoiding the severe and irreversible impacts of climate change, reducing CO₂ emissions through energy efficiency measures makes economic sense as it could foster competitiveness and – depending on the technological specificities – improve energy security. Smart climate policies (such as auctioning of emissions permits or fossil fuel subsidy reform) could raise revenue that could be used to lower other distortionary taxes or finance key investments. Low-carbon transport and energy systems could also mean cleaner air, better health, and a more diversified energy supply, as well as better quality of life for citizens, with less commuting times and reduced energy budgets. A first diagnosis of potential misalignments and the policy priorities to address them is suggested below:⁸

- **There is an unprecedented opportunity to ensure that new investment in infrastructure supports the climate and environment agenda, while fostering economic development.** However, the additional short-term costs of shifting to low-carbon, climate resilient infrastructure would amount to just a fraction of the resources that would ultimately be needed to address the long-term impact of climate change in the event that insufficient policy action is taken now. There is no shortage of capital, but new sources of financing need to be mobilised. Transformational change in infrastructure, including in the energy, transport and building sectors, will require large-scale private sector engagement. It is also important to understand and evaluate the potential unintended impact of financial sector rules (accounting, prudential, market) on the supply of long-term finance, essential for the low-carbon transition. Public finance and investment, as well as reducing private sector investment risk, are also key to catalyse the transition to a low-carbon economy as well as help support adaptation efforts. Governments could reconsider their support for investments in greenhouse-gas intensive activities and mainstream low-carbon and climate-resilient development objectives in public procurement, where feasible, and in official development assistance.
- **Clear and credible government commitment to long-term climate goals and core climate policy instruments are important conditions for successful low-carbon innovation.** A stable and predictable policy environment is key to business investment decisions. Innovation for the low-carbon and climate resilient transition is about the creation of new businesses and the restructuring or the phasing out of carbon intensive ones, the emergence of nascent technologies and new business models, and the right support frameworks for innovations to be adopted widely. This includes

⁸ See the report “Aligning policies for the transition to a low-carbon economy” [[C/MIN\(2015\)11](#)] for an in-depth discussion of these issues.

addressing potential skill gaps through education, training and labour market policies. Here too, policies may not be well aligned with the low-carbon transition. Clear frameworks and long-term policies, in line with effective price signals, are all important components for the sustainability and competitiveness of low-carbon solutions

- **Subsidies and tax expenditures favouring the production and use of fossil fuels slow down low-carbon innovation.**⁹ Other taxes and tax provisions deserve a closer look (e.g. property taxes, various corporate income tax provisions) as they may encourage carbon-intensive choices, and reforming them could be one of the most cost-effective ways to support a low-carbon transition. Governments also need to anticipate the impact of the low-carbon transition on tax revenues.
- **If designed appropriately, trade rules and policies can be mutually reinforcing and contribute to positive environmental outcomes.** However, some existing international trade barriers serve to undermine climate objectives. For example, elimination of import tariffs could contribute to further deployment of some technologies needed for the low-carbon transition. An Environmental Goods Agreement, currently under negotiation, would help to reduce the costs of climate-mitigation efforts, among other outcomes. Care needs to be taken by the some countries that are promoting greener growth through favouring their domestic manufacturers of low-carbon technologies (e.g. local content requirements). Where these measures restrict international trade, they may well undermine overall investment and uptake of sustainable low-carbon technologies.
- **Electricity lies at the heart of a successful decarbonisation of energy systems.** However, deregulated electricity markets do not always deliver the long-term price signal needed for investment in high capital-cost, low-carbon and carbon storage technologies, particularly given the stage of development of the latter. Ensuring competitive and timely investment in low-carbon solutions will require new market arrangements, such as long-term supply agreements, as well as a robust and stable CO₂ price signal. Jurisdictions with regulated systems that are considering introducing competition to lower costs and encourage innovation need to adopt market arrangements that encourage such investment.
- **Current transport systems, which rely largely on fossil fuels, impose very high environmental costs (climate change, noise, air pollution), particularly in urban settings.** Policy intervention is needed to provide more energy-efficient and less carbon-intensive mobility. In many cities, land-use and transport planning are poorly co-ordinated and encourage intensive use of private cars. Aligning policy action across levels of governments and between stakeholders could do much to deliver lower-carbon mobility. National frameworks and legislation sometimes leave local governments with little financial or political leeway to make low-carbon choices.
- **Sustainable land-management practices – reduced deforestation, restoring degraded land, low-carbon agricultural practices, and increased carbon sequestration in soils and forests – can contribute significantly to reducing greenhouse gas emissions,** while responding to growing food demands. They could also improve the resilience of our economies to a changing climate by protecting ecosystems and the services they provide (e.g. flood protection). This requires an integrated approach, which breaks down the silos between mitigation, adaptation, agriculture, food security, forestry, water and environment policies. More specifically, countries could intensify their efforts to remove environmentally harmful agricultural subsidies, value ecosystem services, protect forests and minimise food waste.

⁹ For example, the tax treatment of company cars also encourages more CO₂ emissions unless prevented or offset by other instruments.

72. **A better alignment of policies across countries and sectors could boost effectiveness of climate policies and alleviate concerns about distortions of competition.** International co-operation will also be needed to help developing countries make the shift and manage short-term trade-offs associated with a transition to low carbon. An ambitious climate action plan would also require new approaches to policy making across all government ministries to align policies across all sectors of their portfolios with a low-carbon future. A global agreement on greenhouse gas reductions would send a strong signal in this direction and will facilitate the transition to a low-carbon economy.

Questions for discussion Section 6.1:

- *How to mainstream climate objectives in ‘regular’ socio-economic policies? How to find the right balance between aligning policies for the transition to a low-carbon economy and coherence with other social, economic and developmental objectives?*
- *What is the single most important policy change today to unlock investment for a transition to a low-carbon and climate resilient economy in your country tomorrow?*
- *How can the OECD join forces for a meaningful outcome in the COP21 in Paris and beyond to support the implementation of a possible agreement? How can the COP 21 agreement foster greater policy alignment and facilitate the transition to a low-carbon economy?*

6.2) Climate finance

73. **Concrete progress on climate finance will be one of the key elements to a successful outcome of the COP21 in Paris,** as well as its implementation. Attention is focused on tracking progress towards developed countries’ goal of “mobilizing jointly USD 100 billion per year by 2020 to address the needs of developing countries”; the investment flows needed for a transition to a low-carbon climate-resilient (LCCR) economy. Climate finance is an integral part of sustainable development financing and is connected also with issues to be decided at the Third International Conference on Financing for Development (FFD) (July, Addis Ababa) and the UN Summit to adopt the Post-2015 Development Agenda (September, New York).

74. **Climate investment and finance requirements will be linked to the development trajectory that countries adopt.** Current emissions reductions pledges would result in emission levels higher than those judged to be a cost-effective transition pathway to this target. As the recent New Climate Economy report lays out, the next fifteen years will therefore be crucial, with around US\$90 trillion likely to be invested in infrastructure in the world’s urban, land use, water and energy systems. Managed well, the incremental investment needs to make the transition to a low-carbon and climate resilient economy will likely be modest by comparison and result in a range of co-benefits that offset these higher costs.

75. **Governments have a critical role to play in mobilising and reorienting public and private capital to support the transition to a Low-Carbon Climate-Resilient (LCCR) economy.** Carefully designed policies to support R&D and to reap the learning benefits from the deployment of sustainable low-carbon technologies are also needed and provide opportunities for investment. Governments also have a key role in supporting climate science and assessments that are useful for regional and local decision-makers and to help guide public and private investment to build climate resilience.

76. **Governments and public development finance institutions could use limited public funds to leverage much greater levels of private climate finance and investment** through financial risk mitigation and transaction-enabling interventions, as well as the development of promising investment channels for low-carbon, climate resilient infrastructure, such as green bonds. It is also essential for policy reform agendas to strengthen the framework conditions for investment as a foundation for LCCR investment. Climate and investment policies need to be coherent, transparent and predictable.

77. **The OECD is active across a wide range of these inter-related issues.** The OECD collects key data to track public climate-related development finance and provides analysis and methodologies to track private climate finance flows in support of transparent and robust monitoring and reporting by parties to the UNFCCC. The OECD develops analysis and policy guidance on fossil fuel support measures, taxes on energy use, the effective use of climate finance, and a range of policies to reduce GHG emissions and deliver resilience to climate change. It identifies and analyses barriers to investment in LCCR infrastructure and provides policy guidance to establish coherent national and international policy frameworks and to scale up LCCR investment, including by institutional investors.

Questions for discussion Section 6.2:

- *What do governments see as the main challenges in scaling up finance – both domestic and international - for low-carbon climate resilient growth?*
- *How could OECD further support countries' efforts to mobilise climate finance and investment?*
- *How can governments contribute to reducing financial risks for low-carbon climate resilient investment?*

6.3) Climate adaptation and the water-food-energy nexus

78. **A certain amount of climate change is already “locked in” and even if the two-degree goal is met,** there will be significant impacts from changes in rainfall patterns and intensity, sea level rise and a changed distribution of extreme weather events. People and ecosystems will inevitably have to adapt to this, and the success of that adaptation will depend on how well governments can adapt their policies. Institutions, infrastructure and information will affect adaptation responses and future climate uncertainties. This will place a premium on developing flexible policies that can reduce and share risks in an equitable and efficient way, to facilitate co-ordinated and effective responses, avoiding moral hazard.

79. **Climate change, along with the demands of a growing population, means that the inter-linked issues of water, food and energy are moving higher up the political agenda.** How well this water-food-energy nexus is dealt with in a holistic, integrated and risk-based way will be crucial for sustainable long-term economic growth and human wellbeing. Uncoordinated policies aiming at one element of this nexus may undermine those dealing with the others. This can be damaging both to economic development and to the environment. Notwithstanding the strong interrelatedness between the three, water is at the heart of this nexus; therefore, a future oriented, risk-based approach on water management is key. Water, agriculture and energy infrastructure will require significant financing in coming years. To leverage finance sources, Governments should ensure that wherever possible this infrastructure is designed with multiple purposes so that it can serve multiple users. In order to successfully integrate water infrastructure investments into long term planning, governments need to invest in an enabling environment to reduce risks and increase (financial) trust. Investing in “nexus-friendly” infrastructure can strengthen the integrated management of land, water, and biodiversity, while improving sustainable resource management. Public Private Partnerships and risk mitigation instruments may enhance the contribution of the private sector in ‘nexus-friendly’ infrastructure.

80. **Focusing on water as one of the key factors in climate adaptation and pressures confronting the water sector around the world call for action at all levels of government.** Demands for water cut across sectors, places and people, as well as geographic and temporal scales. The governance context for freshwater management has radically changed in the last 25 years. Better and more accessible information can shed greater light on poor practices. Decentralisation has resulted in opportunities to tailor policies to local realities, but has also made tackling institutional fragmentation and market failures more difficult. There is better recognition that bottom-up, inclusive decision-making is key to effective water policies.

81. **Coping with future water challenges raises not only the question of “what to do” but also “who does what”, “why”, “at which level of government” and “how”.** In light of these developments, the OECD’s Principles on Water Governance aim to strengthen the efficiency, effectiveness, trust and engagement with the ultimate objective being to contribute to better water policies for better lives through sound governance framework conditions.

Questions for discussion Section 6.3:

- *What tools do governments need to help them evaluate whether policies and systems are climate resilient, so that they can be strengthened in a targeted way?*
- *How can governments effectively address water, food and energy nexus issues across multiple levels of government?*
- *How can governments work in partnership with civil society, business and other stakeholders to reap the economic, social and environmental benefits of good water management?*

ITEM 7: TRADE, INVESTMENT AND DEVELOPMENT

82. **This Item covers the issues of trade, investment and development and looks at how they are interlinked.** Trade is analysed using the insights garnered from OECD tools such as Trade in Value Added (TiVA) and Global Value Chains (GVCs), and the Service Trade Restrictions Index (STRI). This Item also sets out the OECD's potential contribution to the post-2015 development agenda.

7.1) The Trade and investment nexus

83. **Global trade volumes today are growing roughly in line with GDP, compared to growth rates about twice as fast as output during several decades before.** While discussions continue about the various cyclical and structural causes for this slowdown in trade, insufficient attention is being given to actions that governments can take to reinvigorate trade and investment in ways that results in economic and employment benefits.

84. **The international fragmentation of production and the rise of global value chains have produced a new “trade-investment-services-know-how” nexus.** Trade in intermediate goods, the international movements of capital, global demand for services to coordinate dispersed value chains, and the freer flow of knowledge to spur continuing innovation are increasingly influential in determining growth opportunities. Policies are needed to respond to this new reality and promote a business environment that facilitates firm participation and upgrading in GVCs.

85. **But a number of barriers constrain the further development of GVCs.** These include inefficient customs procedures, long-standing barriers to agricultural and manufacturing trade, explicit and implicit restrictions on cross-border investment, little progress in opening services markets, and ‘murky’ protectionist measures introduced since 2008. With today's interconnected economies, the cumulative effect of even “low” barriers can impose large costs on firms and discourage trade and investment.

86. **On the other hand, the recently concluded Trade Facilitation Agreement represents a major step forward in reducing trade costs** and is particularly important to the development of GVCs. OECD analysis shows that fully implementing the TFA could reduce trade costs by as much as 14% in some countries; 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.

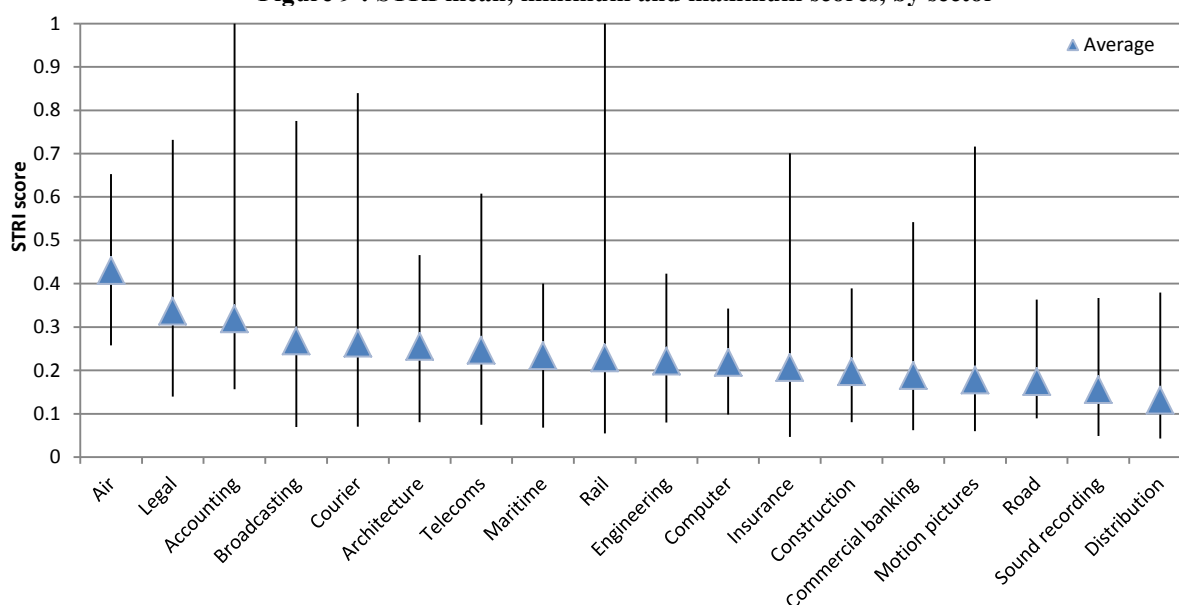
87. **Services are a critical component of the GVC story.** Issues affecting trade in services are similar to, but in some ways distinct from, those affecting trade in goods. Restrictions on market access on services in the international marketplace can have a direct impact on manufacturing, agriculture, and mining. Efficient services sectors contribute to improving productivity and competitiveness across the economy. This is particularly true for those services that act as essential GVC enablers, such as ICT and logistics services, including real-time monitoring of physical assets worldwide through the “Internet of Things.” High-quality professional and financial services also help firms create value in GVCs through differentiation and customisation. It should be noted that the quality of services supporting GVCs in a given country depends not only on market access for qualified foreign providers, but on a robust national education system to train local entrants. Services are at the heart of the trade-investment nexus due to the necessity, in many cases, of a commercial presence in a host country for the cross-border delivery of services.

88. **OECD analysis aim to identify services trade barriers and opportunities for effective reform.** The OECD Services Trade Restrictiveness Index includes a regulatory database and composite indices, and is a practical tool at the national level for diagnosing where reform options are needed, and

how they might best be achieved. The STRI enables governments to take a comprehensive cross-country view of concrete options to improve services sector performance on multilateral, plurilateral or regional levels.

89. **The STRI shows that there is a very large dispersion around the average levels of restrictiveness in each sector, including in countries that are completely closed to trade in some sectors** (Figure 9). Thus, while recognising the potential for judicious regulations to address market failures and support legitimate public policy goals, there is nonetheless scope for reducing unnecessary costs imposed on firms that offers an upside to all countries, since no country is the worst or best performer across all sectors. The STRI also reveals that the policy applied in services is more liberal than what was legally committed to in the GATS. Committing to the services policies in place without undertaking further reforms, would improve certainty and predictability about the business environment facing services suppliers and their customers.

Figure 9 : STRI mean, minimum and maximum scores, by sector



Note: Air transport and road freight currently cover only commercial establishment (with accompanying movement of people). 1 = most restrictive, 0 = least restrictive.

Source: OECD Services Trade Restrictiveness Index, 2015.

90. **The changing architecture of multinational enterprises (MNEs) and investment flows are posing new policy challenges.** In recent years the relative importance of MNE sales of assets to other MNEs and to domestic owners has been growing. These transactions could represent a new phase of GVC development as MNEs restructure their international operations and pursue more arms' length contractual relationships. For some countries the reorganisation of MNE activities may imply significant divestment. A better understanding is needed of the countries, regions, and sectors where these dynamics are likely to have the greatest economic and social consequences.

91. **Boosting cross-border investment requires the removal of explicit and implicit restrictions.** The OECD FDI Regulatory Restrictiveness Index¹⁰ and the Service Trade Restrictiveness Index (STRI) show that many service sectors remain at least partly closed to foreign investors. Furthermore, restrictions are particularly high in key network sectors such as energy and transport, which can have significant spill over effects on the rest of the economy. Companies also face other barriers to foreign investment. These

¹⁰ OECD FDI Regulatory Restrictiveness Index database.

include local content requirements and restrictions on capital flows, notably on operations in foreign currency. OECD research finds a measurable, negative impact of capital flow restrictions on domestic company investment. The OECD Capital Movements Code is a key tool to ensure adequate collective attention to capital flow measures, in light of their implications for other countries, while taking into account risks to countries' financial stability.

92. **Many countries are seeking to establish regional trade agreements (RTAs) –in parallel with multilateral negotiations at the WTO-- to increase openness and spur economic growth.** Disciplines on investment have been increasingly incorporated into RTAs as a means to remove barriers to foreign investment. In addition to removing such barriers, countries can strengthen their investment climate by addressing *inter alia* competition, state-owned enterprises, anti-corruption, and financial regulation and intellectual property rights issues. These can be addressed by individual governments, but are increasingly also included in RTAs such as TPP, TTIP, CETA and RCEP.

93. **As these more ambitious trade and investment agreements cover a broader range of policy areas, they generate greater public and parliamentary debate;** this has been the case on investment issues in the last months. By providing a forum for analysis and the exchange of experiences, the OECD can help governments identify better practices and explain their benefits in order to achieve greater public support.

Question for discussion Segment 7.1:

- *What actions could countries take at the national, bilateral, plurilateral or multilateral level to promote more efficient and trade-oriented services markets?*
- *How should trade and investment policy respond to the emergence of GVCs, where trade and investment are increasingly interconnected? How can the OECD further inform government's efforts to respond to these new policy challenges? How can the OECD's STRI tool help remove restrictions to cross-border trade?*
- *What policies/actions are needed to increase transparency, public acceptance and improve the alignment of international investments in line with changing global conditions? What policies are needed to remove restrictions for foreign investors in service sectors?*

7.2) The Post-2015 development agenda: goals, financing & OECD contributions

94. **The year 2015 provides the world with an unprecedented opportunity to chart a more inclusive and sustainable future for all.** The stakes are high: ending extreme poverty, preserving the environment, addressing climate change, and ensuring shared well-being and prosperity. As we find ourselves in the target year of the Millennium Development Goals (MDGs), we need to strengthen efforts to complete their unfinished business, eradicate poverty and steer a transformational shift towards a more sustainable future. For OECD countries, business as usual is not an option. Their contribution to the implementation of the post-2015 development agenda must be visible and ambitious.

95. **Several decisive summits in 2015 promise to shape international efforts on sustainable development,** among them: the World Conference for Disaster Risk Reduction in March in Sendai; the Third International Conference on Financing for Development (FfD) in July in Addis Ababa; and the UN Special Summit on Sustainable Development to adopt the Post-2015 Development Agenda in September in New York. The outcomes of the 21st Conference of the Parties (COP21) to the UN Framework Convention on Climate Change (December, Paris) will also be relevant. The OECD is actively supporting all of these processes, including through its contribution to the Global Partnership for Effective Development Cooperation. The G20 is also considering these issues under the 2015 Turkish Presidency, either through

specific work related to creating enabling environments for investment in low-income countries, including for energy sustainability, through its agenda on global growth strategies, or by raising awareness over the role of private sector in development.

96. **The international community, including the OECD, will need to adapt its approaches and working methods to support countries in implementing the proposed Sustainable Development Goals (SDGs), which are universally applicable to all countries.** So far efforts to support international development have tended to be concentrated on measuring and improving Official Development Assistance (ODA) and related flows. These efforts remain crucial for the least developed countries, and for those affected by conflict or other sources of fragility; including small island developing states. The MDGs helped to underpin record increases in ODA from OECD Members, and this effort needs to be sustained. At the same time, South-South and Triangular Cooperation have become increasingly important features of the global development cooperation landscape, as emerging economies become themselves important sources of ODA, investment flows and development expertise. The broader scope and ambition of the SDGs will have implications for existing policies and require new approaches from OECD Members and other actors at national and international level.¹¹

97. **The last decade, in particular, has seen a transformation in the way the OECD works on development.** This includes efforts on development finance going beyond ODA, and a concerted effort to put OECD expertise and tools – going well beyond finance – at the disposal of developing countries and all donors. The OECD’s multi-disciplinary structure, analytic tools, efforts to promote policy coherence for development, and its dialogue platforms are unique; indeed, they already help address many of the issues covered by the proposed SDGs.

98. **The OECD Development Assistance Committee (DAC) recently came to an important consensus on how to modernise its statistical framework for measuring development finance to developing countries.** The reform – which will become the standard of reporting from 2018 – recognises that, while both loans and grants are necessary, only the concessional part of the loan should be counted. In this way, more ODA credit will be given for highly concessional loans particularly to LDCs, incentivising more concessional funding to countries most in need. Under both the new and old measurements, ODA has been on an upward trajectory, notwithstanding the impact of the global financial crisis. From an average of USD 122.7bn during the 2004-2012 period – according to the current measure – ODA reached USD 135.1bn in 2013 and USD 135.2bn in 2014. Increasingly, however, alternative sources of financing for development are also coming to the fore.

99. **The private sector plays a critical role in promoting development.** More and better investment will be critical to sustainable development financing going forward. An integrated framework is necessary to increase investment – both foreign and domestic – as a crucial catalyst to create jobs, bring people out of the informal sector, spur innovation and hasten the integration of local enterprises into global value chains. USD 20 trillion will be invested annually across the world in the coming decades and more of this should be directed to green growth and development. The OECD’s Policy Framework for Investment (PFI) helps countries increase their capacity to generate investment, by getting the right policy mix to spur responsible investment with appropriate risk-sharing frameworks that promotes inclusive growth and sustainable development (see Section 3.1). The promotion of RBC enhances the positive contribution businesses can make to economic, environmental, and social progress with a view to achieving sustainable development, and avoiding and addressing adverse impacts. Also, smart use of ODA can also help mobilise and scale up investments from private sector.

¹¹ See document [C/MIN\(2015\)13](#).

100. **More and better tax is another crucial pillar for successful mobilisation of financing for sustainable development.** The vast majority of the money spent on education in the developing world comes from domestic resources. For example, a 1% increase in developing country tax revenues would mobilise twice as much for health, education and roads as total development assistance. A fairer and more transparent tax system is essential for all countries. The OECD/G20 Base Erosion and Profit Shifting Project (OECD, 2014j) is tackling gaps in international tax rules that help curb multinational tax avoidance and offshore tax evasion in developing countries. Engagement of developing countries in the international tax agenda is critical, in particular to ensure they receive appropriate support to address the specific challenges they face. We must respond to capacity needs, and ODA can be used strategically in this respect. The new global standard for Automatic Exchange of Information for tax purposes will also contribute to tackling corruption and fight against tax evasion.

101. **Another top priority for maximising resources for sustainable development is to curb illicit financial flows,** which is considerably bigger than the ODA that developing countries receive each year. The OECD is working to strengthen awareness and share knowledge on effective approaches to tackle issues including illicit trade, money laundering and bribery. The OECD is moving to quantify the size of such illegal markets and illustrate how financial flows are generated through illicit trade in West Africa by following the money trail from its origin to final destination. This will contribute to understanding illicit financial flows and illicit trade better, in a way that ultimately helps shape an adequate policy response both in OECD and developing countries.

102. **The adoption of the Post-2015 Development Agenda by the international community is an opportunity to pursue a transformation in the OECD's work on development for the next decade and beyond.** In some areas, ongoing work is already anticipating the needs of the post-2015 development agenda:

- DAC members have reaffirmed their respective ODA-commitments, including those who have endorsed the UN target of 0.7% of GNI as ODA to developing countries, and to make all efforts to achieve them.
- DAC members have committed to reverse the decline in ODA to LDCs and focus more ODA on countries most in need (including Small Island Developing States, fragile and conflict-affected states) and to develop a new measure of Total Official Support for Development to complement ODA and provide visibility for the full range of development finance.
- The OECD has raised awareness of the importance of a whole of government, whole of OECD approach to achieve Policy Coherence for Development, and is applying it to Illicit Financial Flows, food security and Green Growth/Aligning Policies for the Transition to a Low-carbon Economy.
- The OECD Policy Framework on Investment has been updated to reflect lessons learned in its application to some 30 developing countries;
- The initiative 'Tax Inspectors Without Borders' has been launched and is being piloted in 6 countries, with further projects under development; this in addition to the broader OECD work on taxes.
- Multi-dimensional country reviews (MDCRs) have been undertaken, or are now underway in, 6 countries.
- The OECD has published its first-ever global report on implementation of the Anti-Bribery Convention.

- The pilot project PISA for Development aims to increase developing countries’ use of PISA assessments for monitoring progress towards nationally-set targets for improvement, allowing for institutional capacity-building and for tracking of international educational targets in the post-2015 development framework.

103. **Once the proposed Sustainable Development Goals have been adopted, Members will need to engage in a reflection on how the OECD can best support their achievement by creating an enabling environment both domestically and globally.** As part of these efforts, Members could consider inviting the OECD to deliver, at the MCM a strategic response to guide the Organisation contribution to support such a transformation, including by:

- Raising awareness across the Organisation, and with Members, on the universal nature of the post-2015 development agenda, and integrating this into its work at all levels, including in Committees.
- Supporting Member countries and, where appropriate, Partner countries in their reporting on the sustainable development goals and targets (once adopted by the UN General Assembly), in close collaboration with the United Nations and other international organisations, and supporting Members and Partner countries in defining, measuring and adapting their policies to address the post-2015 development agenda at home and abroad.
- Supporting the international community to tackle global challenges that require collective action, such as resource mobilisation (in particular, taxes and foreign investment) and data collection (e.g., measurement of development finance, trust in public institutions, and gender equality via the Social Institutions and Gender Index).
- Further engaging and seeking greater synergies and complementarities with (i) emerging economies and developing countries (including through the OECD's outreach efforts and its Global Relations Strategy) to share knowledge on the design and implementation of policies for sustainable development and to provide expertise in building statistical capacity through the PARIS21 Partnership, leveraging existing OECD platforms and networks for policy dialogue including those that count on non-OECD Members, and (ii) with the United Nations to provide targeted support for the development of SDG indicators as well as broader knowledge exchange.
- Articulating how the OECD will add value and avoid duplication, working with the UN System and leveraging the Global Partnership for Effective Development Co-operation and other partnerships in support of the new agenda, and supporting OECD Members to improve consistency between policy and development effectiveness commitments made in international fora and practice on the ground in developing countries.
- Strengthening the capacity of the Organisation and its Members to anticipate and respond to emerging trends, global risks and needs (including building greater foresight capacity).
- Fully exploiting the OECD’s data and evidence-based analyses and policy advice to support key elements of the emerging post-2015 development framework (e.g. inclusive growth, NAEC, measuring the root causes of gender inequality, PISA-PIACC-TALIS, TiVA-GVCs, trade in services (STRI), trade facilitation indicators, education and learning outcomes, climate change and the transition to an environmentally sound and socially acceptable low carbon economy, multi-dimensional country reviews, managing the consequences of catastrophic risks, the Policy Framework for Investment).
- Updating the OECD Strategy on Development to articulate the proposed strategic response and programme to guide OECD support to implementing the post-2015 sustainable development goals.

- Updating OECD tools and instruments for Policy Coherence for Sustainable Development (PCSD), aimed at supporting the identification of synergies and trade-offs between economic, social and environmental objectives (e.g. the water-energy-food nexus, trade and investment, social cohesion and migration) and addressing the negative spill overs at the national, regional and global levels, all with a view to help Members and Partner countries implement the SDG framework.
- Gradually integrating the post-2015 framework into OECD reviews (Economic and Development Review Committee (EDRC), economic outlook, environmental performance, energy outlook, regional economic outlooks, peer reviews, OECD Investment Policy Reviews, and others).

104. **These efforts will require engaging emerging economies and developing countries in a two-way exchange of knowledge** on the design and implementation of policies for sustainable development, including through the Knowledge Sharing Alliance (KSA). Members can also leverage the broadening membership of the OECD Development Centre to offer a platform for the exchange of substantive knowledge and policy experiences among OECD and non-OECD countries at different stages of development.

105. **Minimising, mitigating and managing disaster-related risks is a particularly salient issue for developing countries.** The OECD is taking an active role in supporting work on indicators related to disaster risk reduction through the collection of standardised data on social and economic losses from disasters, drawing on the expertise of its High Level Risk Forum. The OECD Recommendation on the Governance of Critical Risks, adopted at the MCM 2014, has played a key role on the current revision to the UN agreement on disaster risk reduction (Hyogo Framework for Action). OECD expertise on the governance of critical risks is being brought to the Post-2015 development agenda context through close collaboration with the United Nations International Strategy for Disaster Reduction (UNISDR) as well as UN Habitat. The OECD will continue contributing to this debate reporting on progress in the implementation of the Recommendation on the Governance of Critical Risks.

Questions for Discussion Segment 7.2:

- *How can OECD help inform the policy debate on, and support the achievement of, the proposed Sustainable Development Goals?*
- *How can OECD best support investment for development, including through the PFI? How can governments leverage private sector financing for development, including through more effective and transparent tax systems, and improve access to markets for developing countries, beyond aid for trade measures?*
- *How can the OECD further support efforts to promote responsible business conduct?*

ANNEX I: SUMMARY OF THE REPORT “FINAL NAEC SYNTHESIS: NEW APPROACHES TO ECONOMIC CHALLENGES” [C/MIN(2015)2]

106. **The starkness and magnitude of the recent crisis and its lingering legacy calls for a serious reflection, to revisit and supplement existing policy approaches** and build a new policy agenda for stronger, more robust, inclusive and sustainable growth. The New Approaches to Economic Challenges (NAEC) initiative is a comprehensive organisation-wide reflection process that is triggering and accelerating a revision of the OECD’s analytical frameworks as well as a renewal and strengthening of its policy instruments and tools.

107. **NAEC is proposing and supporting a change in objectives, perspectives and policy tools to promote growth, as a means to an end and not as an end in itself.** It calls for focusing on well-being and its distribution to ensure that growth delivers progress for all. Policy choices should be informed by an assessment of their impact on different dimensions of well-being as well as of their distributional consequences.

108. **NAEC also calls for better integration of the financial sector, and related risks, into the OECD’s analysis, shedding light on the numerous and complex interactions between finance and the real economy.** NAEC recommends developing the analysis of the world economy as a “complex adaptive system”, taking into account uncertainty, spill overs, systemic risks and network effects. This analysis, among others, may help policymakers get a better grip on rising global interconnectedness. NAEC also emphasises the need to increase macroeconomic stability by implementing an effective regulatory framework, promoting fiscal soundness and fostering the counter-cyclicality of macroeconomic policies.

109. **This should also trigger the adoption of a longer-term perspective that can be informed by enhanced capacity for strategic foresight.** Taking a long-term perspective also leads to further consideration of how economies are embedded in institutions that are shaped by history, social norms and political choices. This would in turn lead to more tailored policy solutions adaptable to countries’ specific needs, conditions, capacities and institutional settings.

110. **To make these changes in perspectives happen, the Organisation needs to develop, where feasible, new instruments and tools, and to deepen, generalise and systematise their use.** It requires measurement of stocks as well as adequate consideration of both stock and flow concepts in analyses. The Organisation needs to further develop its use of micro-data and take advantage of big data. This will allow getting a better grip on the heterogeneity of households and firms, and facilitate analyses to understand and tackle inequality. The Organisation also needs to review and improve its modelling approaches, taking a more integrated approach while noting the limitations of the fundamental assumptions upon which models are built. All these changes in instruments and tools should enrich OECD analysis. They also need to be supplemented with insights from other disciplines that are relevant to policy, such as sociology, psychology, geography and history. The aforementioned new approaches have already led to a series of policy recommendations that would support a stronger, more robust, inclusive and sustainable growth agenda.

111. **NAEC does not claim to have all the answers but points to progress in a number of areas.** Challenges remain in enhancing the OECD’s analytical approaches; accessing and assembling new data; developing modelling capacities; and embracing new ideas and new ways of working across the Organisation. The NAEC Synthesis draws attention to green shoots of change in many parts of the OECD with emerging results that shed light on critical challenges and the strong, robust, sustainable and inclusive growth agenda needed to address them. But a lot remains to be done to develop new approaches to economic challenges.

ANNEX II: SUMMARY OF THE REPORT “UPDATE ON THE INCLUSIVE GROWTH PROJECT” [\[C/MIN\(2015\)4\]](#)

112. **At a time when people in many OECD countries have not seen their real incomes rise for several years, and the gap between rich and poor has widened, promoting stronger and more sustainable long-term investment has never been more important.** Public and private investment choices made today have long-term impacts not just on growth, but on income inequality, social mobility and individual well-being, through their effect on productivity and employment.

113. **In the last twenty-five years, income inequality, as measured by the Gini coefficient, has risen markedly in the majority of OECD countries.** By 2011, the average income of the top 10% of the distribution in the OECD area grew to 9.6 times that of the bottom 10%, up from a ratio of 7.2 in the mid-1980s.* Yet income is just one aspect of life that matters for well-being. In just about every area, whether it be educational attainment, life expectancy, or employment prospects, success is disproportionately determined by socio-economic status, wealth and assets, sex, age, or the places where people live. Labour market disparities have also grown wider. In the wake of the financial crisis, vulnerable groups have borne the brunt of increased unemployment, and equitable access to high-quality jobs has become increasingly difficult to achieve, with non-standard working arrangements now accounting for a third of employment in OECD countries.

114. **In the long run, this may be neither socially, nor economically sustainable.** Indeed, there is mounting evidence to suggest that rising inequality might have diminished growth in a number of OECD countries, by discouraging people in the lower part of the income distribution from investing in education and skills. In the political sphere, widening inequalities erode confidence in public institutions, and diminish trust in government.

115. **The OECD’s approach to Inclusive Growth is premised on the idea that improvements in societal well-being need to be put at the very core of policymaking.** GDP growth is not an end in itself, but rather as a means to enhance well-being. It goes without saying that growth remains essential, but it is not everything - how well people are doing in other areas like jobs, education, and health matters too. It also matters how the benefits of an expanding economy are shared out. Any sensible model of economic progress cannot assume that all growth contributes to well-being equally, regardless of who benefits. This means looking not only at how policies affect the statistically constructed ‘average person’, but also looking at how they affect different social groups like the middle class, the bottom 10, 20 or 40%, youth, or women.

116. **Preliminary OECD work indicates that there are clear ‘win-win’ policies for promoting both growth and inclusiveness, but that there will also be trade-offs.** For instance, pursuing a particular set of growth policies may raise income, but at the same time lead to higher air and water pollution, with unclear net effects on health status and overall living standards. Higher health spending can support a healthier population with potentially positive effects on employment and incomes, but it will also imply higher taxation and hence less material consumption.

117. **Putting in place policies to promote Inclusive Growth requires governments to overcome a number of implementation-based challenges.** In many countries, fragmented systems of governance hinder inclusiveness, leading to avoidable trade-offs and co-ordination failures. Public governance institutions, tools and processes should be designed to improve coherence across sectors and levels of government while empowering the implementation and evaluation of Inclusive Growth policy packages.

* OECD Income Distribution Database (<http://www.oecd.org/social/inequality.htm>).

ANNEX III: SUMMARY OF THE REPORT “POLICY FRAMEWORK FOR INVESTMENT (2015)” [\[C/MIN\(2015\)5\]](#)

118. **The objective of the Policy Framework for Investment (2015) is to mobilise private investment that supports steady economic growth and sustainable development**, contributing to the economic and social well-being of people in developing, emerging and advanced economies. The Framework is a tool, providing a checklist of key policy issues for consideration by any government interested in creating an enabling environment for all types of investment and in enhancing the development benefits of investment to society. In this way, the Framework also aims to advance the implementation of the Sustainable Development Goals and to help mobilise financing for development.

119. **In 2006, a task force of government officials from 60 OECD and non-OECD economies developed the Framework’s content and structure** through regional consultations in Africa, Asia, Latin America and South East Europe. The World Bank, the United Nations and other international institutions, as well as business, labour and civil society organisations also contributed the development of the Framework. Since its development, the Framework has been used world-wide for country-level OECD Investment Policy Reviews, sub-national level applications, numerous regional investment programmes and dialogues, and within regional groupings, such as the Association of Southeast Asian Nations and the Southern African Development Community, as well as in the context of the G20. It has also been used extensively for targeted capacity building activities, peer reviews and knowledge sharing, and technical advisory work on investment and development. Sectoral applications of the Framework have also been developed, such as the Policy Framework for Investment in Agriculture and the Policy Guidance for Clean Energy Infrastructure.

120. **To take this experience and the changes in the global economic landscape into account**, the update of the Framework was carried out in 2014-2015 under a task force co-chaired by Myanmar and Finland. The update also benefitted from the contribution of the OECD Advisory Group on Investment and Development, and various public consultations, online dialogues and seminars.

121. **The updated Framework is comprehensive but does not claim to be exhaustive.** Beyond macroeconomic stability, political predictability, social cohesion and upholding the rule of law, which are pre-conditions for sustainable development, the Framework considers numerous policy dimensions in an integrated manner, drawing on global good practices including: investment policy; investment promotion and facilitation; trade policy; competition policy; tax policy; public governance; corporate governance; policies for enabling responsible business conduct; human resources development; an investment framework for green growth; private investment in infrastructure; and financing for investment. The Framework helps governments consider these policy areas as a whole, supporting policy coherence in support of social, environmental and economic goals. Other policy areas, such as rural development, the promotion of small and medium-sized enterprises, innovation, gender balance and entrepreneurship bear on the business environment as well. While the Framework does not identify these topics as stand-alone chapters, it explicitly captures their importance on the investment environment and for sustainable development through specific questions in different policy chapters.

122. **The OECD, working with Member and non-Member economies, partner organisations, donors and stakeholders, will assist in building institutional capacity for the effective use of the Framework in light of different circumstances and needs.** The Framework also builds on the OECD’s experience and instruments dealing with the different policy areas that are covered and its Committees’ global and regional dialogue with non-Member economies. It complements recent OECD initiatives directed to governments and the business sector, including the OECD Guidelines for Multinational Enterprises updated in 2011, and can work in synergy with the OECD Development Assistance Committee’s work on leveraging private sector-led sustainable growth.

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