BARI POLICY AGENDA

on growth and inequalities

The global economy is facing a prolonged period of modest growth and high or rising inequalities in many countries, notably within countries and with middle and lower income classes being particularly affected. The fruits of economic growth may have been insufficient to meet our citizens' expectations. Excessive inequality undermines confidence and limits future growth potential owing to low investment (notably in human capital) and weak productivity. Persistent income or wealth inequality in turn gives rise to divergences in opportunities and ultimately in living standards. By locking in opportunity privilege and exclusion, inequalities may contribute to regional divides, undermine intergenerational mobility, while putting stress on social cohesion and institutions.

Technological change and global integration, in particular of trade and finance, have made a huge contribution to raising living standards across the world over recent decades. Notwithstanding that, we should work to enable our economies and communities to adjust to the pace of change today, so that the global economy works for everyone. The issue of inclusive growth and its drivers is complex and the extent of inequality and experiences vary widely. Some of these drivers are cross-border in nature and affect most advanced economies, while others largely vary from country to country. In particular, the interaction between skill-biased technological advancement, growth and inclusivity, rising dispersion in firm productivity and wage levels, a trend towards less redistributive tax-and-transfer systems in many advanced countries, demographic changes and persistent high level of unemployment may have been behind rising inequality. In addition, the global financial crisis, the following recession and the subsequent, long period of modest growth also played a role, together with the even more constrained national redistributive powers in most countries.

Policy responses are required to ensure that fruits of economic growth are shared more widely. While there is no single best model for achieving inclusive growth that works for all G7 countries, our common goal remains the achievement of more and better growth. Our policies should aim to lift actual and potential growth while achieving a more even distribution of its fruits. Spreading the benefits of increased prosperity, in turn, requires a multidimensional and country-specific approach. Comprehensive, coherent and effective policy packages, which go beyond the focus on income to cover other key dimensions of well-being, are needed to tackle inequality effectively and contribute to strong, sustainable, balanced and inclusive growth.

The Bari Policy Agenda provides a general framework through a broad “menu” of policy options to foster inclusive growth by exploiting synergies between macroeconomic and structural policies, while mitigating potentially adverse effects on equity. While many potential policy responses are largely domestic, some of them require, *by definition*, a collective effort. Even when policies are specifically domestic, we recognize that their benefits will be magnified by a common resolve to deliver inclusive growth.

The first set of options offers ways in which fiscal policy and the quality of public finances may play an important role in safeguarding macroeconomic stability while at the same time addressing inequality and ensuring that public debt, as a share of GDP, is on a sustainable path in line with respective fiscal frameworks. Reducing the growth divide and providing equality of opportunities may call for higher spending in specific policy areas without necessarily altering the overall budget envelope. More effective budget allocations both on the revenue and on the expenditure sides may offer potential to boost growth and productivity.

Second, and more broadly, we see potential benefits in combining these pro-inclusive growth fiscal policies with comprehensive and balanced “packages” of structural policies to create an enabling environment for broad-based growth, while facilitating adjustment to the dislocations created by technological advances and international trade. Countries may want to reinvigorate innovation and productivity, enhance education (initial and lifelong) incentives to work and active labour market policies to promote the reallocation of workers across industries and jobs, address labour market insecurities, improving equitable access to health care services and training opportunities and reduce obstacles to the participation of women, youth and the elderly in economic life. Good quality public investment, notably in infrastructure and education, has the potential to boost growth and productivity, while also positively affecting job creation and demand in the short run. To this end, we remain committed to promote quality infrastructure investment, in line with the G7 Ise-Shima Principles for Promoting Quality Infrastructure Investment.

Moreover, there might be areas where a collective effort is required due to important cross-border implications. International cooperation is key to respond to increased levels of capital mobility. In this regard, we have been working to ensure a level playing field for international taxation through the implementation of the G20/OECD tax agenda.

PROMOTING INCLUSIVE GROWTH THROUGH FISCAL POLICY

In the current environment of modest growth and limited policy space, G7 countries may identify opportunities for fiscal policies to promote stronger and more inclusive growth, while ensuring a more effective use of the budget.

On the revenue side, possible tax reform options could make the tax system more equity-and-growth friendly. Possible reforms could include broadening the tax base, curtailing inefficient tax expenditures, and reducing tax wedges on labour, particularly for low-skilled workers, to enhance participation in the labour market, while supporting the incomes of working families. G7 countries may have room to reduce inequality by designing taxes and transfers in a more effective way. This may enhance the redistributive power of fiscal policy and address the twin objectives of more equality and more growth via higher wages and better labour conditions. In addition to reducing low-wage tax wedges, G7 countries may consider to enhance tax incentives for skills development and lifelong learning thus encouraging the creation of quality jobs in the formal economy. We remain committed to tackle tax evasion and avoidance by leveraging international tax cooperation. Since our tax systems are challenged by increased levels of capital mobility and the enhanced use of aggressive tax planning, we remain committed in the implementation of the G20/OECD tax agenda, notably the Base Erosion and Profit Shifting (BEPS) package and Automatic Exchange of Financial Account Information for Tax Purposes (AEOI). Moreover, as part of the BEPS project, the Task Force on the Digital Economy (TFDE) has been mandated to monitor and evaluate the developments related to the digitalization of the economy, and, depending on conclusions of this work, as appropriate, develop policy options to address related tax challenges. We look forward to the Interim Report by the TFDE to the G20 in 2018.

On the spending side, we recognize that growth-friendly and inclusive fiscal policy is not just a matter of the sign and size of the budget, but also very much of its composition and quality. G7 countries may gain value in a constrained fiscal environment by focusing on the efficiency and investment-related potential of social services (including education, labour markets, and health care) and better targeting the people and places most in need. In particular, countries may find value in improving access to quality education from the youngest ages up and ensuring that investment in human capital is rewarded through access to productive and rewarding jobs. This could include improving the quality of schooling in the most disadvantaged areas, by developing adequate educational infrastructures and by championing lifelong learning for all.

Countries can consider interventions to improve the targeting and efficiency of social protection systems, provided that poverty traps and excessive administrative burdens are avoided and support labour market participation. Countries may also consider improving access to affordable housing and broader economic development in distressed regions including by promoting network infrastructure.

PRO-INCLUSIVE GROWTH STRUCTURAL REFORMS

Comprehensive policy packages of structural reforms may improve the framework conditions for inclusiveness while compensating the most vulnerable. The twin challenges of rising inequality and slowing productivity among countries and firms as one of the main factors responsible for wage dispersion and inequality should be addressed, when appropriate. G7 countries may want to promote market competition and a level playing field while encouraging firms to adopt and adapt to innovation. To this end, G7 countries may consider policies that promote investments in R&D, skills, organizational know-how and other forms of knowledge-based capital, and ensure that such investment supports economic growth across the country. We welcome the assessment Methodology of G20/OECD Principles of Corporate Governance and support continued work on corporate governance, which can foster long-term investment and facilitate access to capital markets A lean and efficient public administration is a critical factor for policies implementation. We could also consider the implications of the digital economy, including at international level, as it can lead to greater competition and consumer choice. However, there is a need to better understand the potential market impact of new business models, the risks of higher concentration, and the challenges for taxation.

Furthermore, reducing labour market segmentation and duality can boost growth and productivity while enhancing inclusiveness. Countries may seek to lower barriers to the labour market and to strengthen active labour market policies, with the aim to increase labour force participation, and to support skills and training programs. Actions should be considered to address segmentation and inequalities between regions, supporting growth in local areas, including through investment in infrastructure, skills and connectivity, and ensuring the right institutions are in place to facilitate growth. In a context where globalization and technological change are disrupting traditional forms of employment and increasing demand for high-skilled workers, G7 countries may consider to take steps to ensure the labour force has the skills required for the future of work. Meanwhile, countries may seek to work with employers to foster a culture of life-long learning, to enable workers to continue to develop their skills through their careers in a context of rapid technological change and longer working lives.

Recognizing that the gender gap, notably in the labor market, remains a challenge in many countries, with detrimental effects on economic growth, we commit to promote gender equality and increase the integration of women in economic activities. In some cases, women's labour market participation could be increased including by providing incentives to individual and business investment in skills. G7 countries may want to emphasize the importance of childcare that is accessible, high quality and affordable and promote policies that address other barriers to women's labor force participation throughout their life-cycle. Closing the wage gap between women and men including by promoting formalization of the informal economy and increasing women's wages faster than the national average may also address inequality. In addition to promoting greater pay transparency, G7 countries could consider measures to enhance women's earnings and leadership potential through education, training, and mentorship that create paths to equal opportunities for successful careers in high-wage, high-growth sectors. Performance budgeting practices can play a role in promoting equality and fair access to opportunities for all. We recognize the importance of integrating equity considerations into policy-making. In this respect, gender budgeting could be a valuable tool to operationalize inclusive growth by promoting gender equality throughout the budgetary process.