GROWTH, FINANCE AND REGULATION

EFFECTS OF GLOBAL CRISIS ON STRUCTURAL POLICIES AND FINANCIAL REGULATIONS: THE COMPARISON OF OECD ECONOMIES

ABDULLAH BAHCE,
YUSUF KARAASLAN

Faculty of Economics and Administrative Sciences
Dokuz Eylul University, Turkey

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Abstract: Global crisis that has affected all economies has also given harms for financial and structural bodies of economies. Near after this financial crisis, governments took different responsibilities to overcome this phenomenon. In this context, priorities in overcoming the crisis have concentrated on the macroeconomic adjustments and regulatory precautions. Measures should have taken by the governments of OECD economies in line of macroeconomic adjustment and crisis exit strategies are outlined briefly.

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Introduction

The current financial crisis has effected every economy in the world, including the developing economies. The crisis, which began in the United States, has weakened the financial markets both in Europe and in the emerging economies. This case has resulted from globalization phenomenon. Because globalization has demonstrated that the world economy became integrated and there cannot be a major downturn in the world's richest economy without implications for every other economies.

Furthermore, the way globalization has been managed allowed the United States to export its "toxic mortgages" all over the world. Had the rest of the world not bought as many of them as it did, the financial decrease in the United States would have been much worse (Stiglitz, 2009). Stiglitz (2009) noted that this crisis has a very clear "Made in the USA" label on it. Not only did the United States export its toxic mortgages, but it also exported the deregulatory philosophy that allowed other economies to buy these mortgages and ensured that regulators abroad did not stop it.

Recent developments have shown that the current crisis will have permanent effects, also highlighted the importance of accelerating structural reforms, and avoiding the introduction of policies in the midst of the crisis that would risk decreasing potential output even further. Accelerating structural reforms in the years ahead would not only improve longer-term growth prospects and enhance resilience to new adverse shocks, but would also contribute to easing fiscal pressures. Besides, it is important that fiscal consolidation measures minimize adverse effects on supply potential, for instance, by limiting any increases in the tax wedge on labour or cutbacks in growth-enhancing spending. (OECD,2009a).

In response to the current financial and economic crisis; firstly governments are taking increasingly robust measures to counter international tax evasion and those who assist in facilitating it. (OECD,2009b). Secondly, economies may further review the regulatory environment for banks and other financial institutions against the current financial crisis and give the assistance to the banking industry, and this may also have implications in the tax area. (OECD,2009b).

A further reason for considering the effect of a fall in structural unemployment on fiscal positions is to gauge the scale of possible effects that structural policy responses to the crisis might have. According to Belot and Ours (2004), policy changes that result in tighter labour and product market regulations could amplify the impact of the crisis on structural unemployment while easing of such regulation could help to mitigate the impact of the crisis, including on fiscal positions.

As a necessary short-term response to the crisis, unemployment benefits have been made more generous in coverage and, sometimes in level. But were such policies to remain in place over the longer term both government spending and structural unemployment would be durably higher. Finally, the need for future fiscal consolidation raises the possibility that the tax wedge might rise, with negative effects for structural unemployment.

Structural policy adjustments in OECD economies based on assumptions of 2010-2019

OECD report provides opportunity to compare some macroeconomic indicators (Table 1) of OECD economies for the period of 2006-2010. Medium-term plan assumptions and estimations based on the macroeconomic indicators of 2006-2010 period are made by OECD experts. Gianella et al. (2008) notes that unemployment will be expected to return to its estimated structural rate in all OECD countries by 2017. Further, it is estimated that oil and other commodity prices will be risen by 3% per annum in real terms beyond 2010. However, exchange rates will remain unchanged in nominal terms. In addition to that, monetary policy rates will remain low and will be directed at avoiding deflation and, towards the end of the scenario, are normalised in order to bring inflation in line with medium-term objectives.

Fiscal policy estimations are based on the assumptions that fiscal stimulus packages in operation during 2010 will be removed from 2011 onwards. Some further improvement in fiscal balances will come about as automatic stabilizing reaction to output gaps being closed. The scale of additional consolidation, over and above the removal of fiscal stimulus packages, is assumed to be dependent on the projected 2010 financial balance (Schich, 2009). At this point, OECD

(2009d) emphasizes the importance of fiscal consolidations to exit from the financial crisis. According to this, some OECD economies, such as Denmark, Finland, Hungary, Korea, Norway, Switzerland, Mexico and Sweden will be expected with a financial deficit of less than half of the OECD average in 2010 (i.e. 4½ % of GDP). So, it is expected to have no fiscal consolidation over and above the removal of temporary fiscal stimulus packages. On the other hand some OECD economies, such as United States, United Kingdom, Spain and Ireland are estimated with a financial deficit of more than the OECD average of around 9% of GDP in 2010. So, it is suggested to have a progressive fiscal consolidation of one percentage point of GDP each year from 2011. Finally all other OECD economies, namely those with a financial deficit of more than 4½ but less than 9% of GDP in 2010, are assumed to have a progressive fiscal consolidation of one percentage point of GDP for three years from 2011.

TABLE 1. MACROECONOMIC INDICATORS OF OECD ECONOMIES, % GDP (2006-2010) *

	Real GDP growth	Real labour Productivity growth	Real employment growth	Structural unemployment	Inflation (GDP Deflator)	Financial deficit	Tax revenues
Australia	4.2/-0.4	1.3/1.0	2.3/1.8	0.1/-0.2	3.9/1.0	1.8/-4.9	3.0/-1.3
Austria	3.0/-4.3	1.2/0.5	0.7/0.4	0.0/-0.4	2.2/1.4	-0.7/-4.3	-0.1/-0.8
Belgium	2.6/-4.1	1.3/1.2	1.2/0.6	0.0/-0.4	2.4/1.0	-0.3/-4.6	1.0/-0.3
Canada	2.5/-2.6	0.7/0.6	1.6/1.1	0.1/-0.1	1.6/0.8	1.0/-1.3	-1.5/-2.4
Czech Republic	6.1/-4.2	-	-	0.3/-0.9	3.4/4.5	-0.6/-4.5	1.1/-2.5
Denmark	1.6/-4.0	0.8/0.7	0.8/-0.3	0.1/-0.3	2.0/1.9	4.5/-2.4	1.5/-0.7
Finland	4.1/-4.7	2.0/1.6	1.3/0.3	0.2/-0.3	3.1/0.6	5.2/-1.5	-1.1/-2.7
France	2.3/-3.0	0.8/0.8	0.8/0.4	0.2/-0.3	2.1/0.0	-1.1/-7.6	-0.4/-0.2
Germany	2.6/-6.1	0.8/0.9	0.4/0.0	0.1/-0.3	1.7/-0.5	8.0/2.8	-0.6/-1.6
Greece	4.0/-1.3	2.3/2.3	1.2/0.4	0.2/-0.4	2.9/1.6	-3.9/-6.1	0.0/0.8
Hungary	1.2/-6.1	-	-	0.4/-1.7	5.9/2.7	-4.9/-4.2	1.3/0.2
Iceland	5.5/-7.0	2.1/0.8	2.8/0.0	0.0/-0.4	5.6/9.2	5.4/-11.5	2.2/5.7
Ireland	6.0/-9.8	1.0/-0.1	2.9/-.1.8	0.0/-1.7	1.4/0.5	0.2/-8.2	-0.1/6.0
Italy	1.5/-5.5	-0.2/0.3	1.1/-0.3	0.2/-0.8	2.2/-0.3	-2.4/-5.4	4.6/0.3
Japan	2.3/-6.8	1.3/1.2	-0.3/-0.6	0.0/-0.1	1.4/-1.4	-2.7/-7.8	6.9/-0.5
Korea	5.1/-2.2	-	-	0.2/0.9	2.1/5.3	4.7/-1.2	4.6/-2.8
Luxembourg	5.2/-4.0	-	-	0.4/1.4	2.1/0.7	3.6/-2.4	-0.7/-2.3
Mexico	3.3/-8.0	0.6/0.5	1.9/1.5	0.4/-1.7	4.5/3.6	-0.8/-0.4	0.1/-0.4
Netherlands	3.5/-4.9	1.2/1.1	0.8/0.1	0.0/-0.4	1.5/1.3	0.3/-4.4	0.4/-1.6
New Zealand	3.0/-3.0	0.7/-0.1	1.9/1.1	0.1/-0.1	4.2/0.2	5.0/-2.8	0.0/-4.1
Norway	3.1/-1.0	2.2/2.5	1.7/0.7	0.2/-0.2	2.2/-1.1	17.7/8.6	-2.2/-0.3
Poland	6.8/-0.4	2.5/2.6	2.1/1.7	-2.3/-1.4	4.0/3.3	-1.9/-6.3	3.8/-0.4
Portugal	1.9/-4.5	0.3/0.3	0.5/-0.1	-0.1/-0.4	3.0/0.3	-2.7/-6.5	0.4/-
Slovak Republic	10.4/-5.0	-	-	1.0/-0.6	2.8/1.8	-1.9/-4.9	-/-0.7
Spain	3.7/-4.2	0.3/1.7	2.8/-0.5	0.1/-1.4	3.2/0.7	2.2/-9.1	6.8/-1.7
Sweden	2.7/-5.5	2.0/1.7	0.9/0.0	0.1/-0.2	2.8/2.1	3.8/-3.3	1.2/-1.7
Switzerland	3.3/-2.7	0.5/1.0	1.5/0.8	0.0/-0.1	1.8/0.6	1.3/-1.5	0.4/-0 2
Turkey	4.7/-5.9	-	-	-0.6/-2.2	6.2/6.6	-4.2/-5.5	1.8/-1.5
United Kingdom	3.0/-4.3	1.4/1.3	0.8/0.0	0.0/-0.3	2.4/1.1	-2.9/-2.6	0.4/-1.5
United States	2.0/-2.8	1.7/1.0	0.7/0.5	0.0/-0.1	3.3/0.2	-5.9/-10.2	9.4/-3.2
Euro Area	2.6/-4.8	0.7/0.9	1.1/0.0	0.1/-0.6	3.3/0.5	-1.9/-5.6	-
Total OECD	2.7/-4.1	1.3/1.0	0.8/0.3	0.1/-0.2	3.2/0.6	-3.2/-7.7	-/-1.9

Source: "OECD Economic Outlook" No.85, Data Base.

Note: * indicates that first percentages show changes between 2006-2008 period, and second percentages show changes between 2008-2010 period.

OECD (2009a) noted that many OECD economies try to establish future fiscal and administration plans. For example in Australia a commitment to hold real growth in government spending below 2% per year has been announced, aiming to halve the budget deficit by 2012-2013 period and achieve a surplus by 2015-2016. In Austria an intention to reduce the budget deficit below 3% of GDP by 2012 has been announced and in Belgium the medium term objective of a balanced budget in 2015 has been specified, involving a structural tightening of about 1% of GDP per year from 2010 onwards. The tightening in each individual year is to remain growth-dependent and no concrete measures to achieve the objective have been proposed. At the same time in Denmark, the tax reform package aims to begin removing fiscal stimulus in 2011, with gradually phased measures to ensure the package is budget neutral by roughly 2013. Measures include higher taxes on pollution and energy consumption, and cuts to the tax deductibility of employment-related expenses and mortgage interest payments.

In Germany; a reformed fiscal rule has been adopted by Parliament and is to be implemented in 2011, requiring the structural budget deficit to not exceed 0.35% of GDP for the central government, and balanced structural budgets for the country. The planned transition path will allow higher, but steadily decreasing structural deficits until 2015 for the central government, and until 2019 for the country. In Italy, fiscal plans intend to keep the underlying fiscal deficit constant at 2.9% of GDP in 2011, and increase the underlying primary surplus from 2.5% of GDP in 2010 to 2.8% of GDP in 2011. In Ireland planned consolidation measures aim to

achieve a fiscal deficit of 3% of GDP by 2013. A combination of spending and revenue measures amounting to over 2.5% of GDP is planned for each of 2010 and 2011, and further consolidation is planned for 2012 and 2013. In Netherlands an announced spending cut is planned in 2011, conditional on growth, with plans to reduce the deficit by at least 0.5% of GDP per year beyond 2011. Expenditure reductions will in part affect childcare and health subsidies. In New Zealand plans to achieve fiscal sustainability involve overall savings of 4% of GDP, in large part over 2011-2013 period. Proposed measures include a delay of the planned personal income tax cut over 2010-2011 period, and a reduction of the operating allowance for new spending in future budgets. In Portugal fiscal consolidation plans are planned to resume upon the recovery of economic conditions, with the objective of reducing the structural budget deficit by 0.5% of GDP per year. Intentions include reforms in public administration, primarily through reducing public sector employment, as well as using public sector resources more efficiently. And also in Spain intention to reduce the budget deficit to 3% of GDP by 2012 has been announced. Measures have been proposed to impose ceilings with respect to household income on the deductibility of interest and amortisation of new mortgages from owner occupiers' income tax liabilities, beginning in 2011.

Furthermore in the US administration plans to consolidate fiscal balances to reduce the federal budget deficit to 3.5% of GDP in 2012. The proposed measures include the scheduled expiry of tax provisions originating in 2001 and 2003, an increase in tax rates on capital gains and dividends, an extension of estate taxes, and a reduction in itemized deductions. In the UK government foresees an annual average fiscal consolidation of 1⅓% of GDP from 2010 to 2014, towards a target of reducing the structural deficit by 8¾% of GDP by 2018. Specific consolidation measures announced include tax increases on fuel, alcohol and tobacco, an increase in the top income tax rate, higher social security contributions, lower growth in current spending and reductions in public net investment (OECD,2009a).

Financial regulations which are reviewed by the Governments

According to Schmidt-Hebbel (2008) future regulatory reform will clearly aim to improve business models, transparency, disclosure, and oversight of financial institutions. At the same time, financial market participants must never assume bailouts are the norm, and reforms must therefore minimize the risk of "moral hazard" affecting future financial market behaviour. Besides, while major regulatory changes on financial and capital markets will be required, both nationally and across countries, there is a clear and present trap to avoid, and that is a risk of a regulatory over-reaction. Excessive regulation can do damage also, by inhibiting future financial innovations, market integration and growth.

Within the EU, a number of instruments, of which the most important are the Mutual Assistance Directive 77/79/EEC, Council Regulation (EC) No 1798/2003 and Council Regulation (EC) No 2073/2004, allow for exchange of information in tax matters. The Mutual Assistance Directive calls for information exchange in direct tax matters between all 27 EU member states. Each of the EU member states is required to put into force the necessary laws, regulations and administrative provisions to comply with the Directive. The Council Regulations suggest for administrative co-operation between EU member states in the field of value added tax and excise duties, respectively. They lay down rules and procedures to enable competent authorities of the member states to cooperate and to exchange with each other any information that may help them effect a correct assessment of VAT and excise duties. The regulations are directly applicable in all EU member states (OECD,2009c).

Concluding remarks

The last crisis that damaged both the developing and developed economies. Solution for this devastating economic problem lies beneath learning from the past experience, strengthening the framework of the regulatory bodies, clarifying the goals to realize business conduct, making financial markets more transparent and more accountable with more realistic and applicable instruments, enhancing confidence for the real sector, applying more audit for the credit agencies, derivatives and also for the government agencies. Further corporate governance of the financial firms should be realized by not forgetting the moral hazard issues. Competition policy rules and all the other regulation concerns are also another applicable issues for the reformation of the new financial architecture.

Regulatory framework should be streamlined for strengthening incentives for their enforcement. Government policies should include priorities of disclosure and protection against fraud for the transparency of markets. At last financial institutions accountability and governance should be strengthened for the soundness of effective solution.

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