The role of the OECD in the design of macroeconomic and labour market policy: Reflections of a heterodox economist

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Abstract: Despite theoretical and empirical challenges to the neo-liberal policy framework outlined in the Job Study (1994), supply side initiatives remain central to the OECD's policy agenda, along with conservative macroeconomic policy, notwithstanding concessions made in its 2006 Employment Outlook and subsequent publications. The significant real shocks to economies resulting from the global financial crisis have presented the organisation with new challenges, given the need to reconcile the use of fiscal stimulus packages by some member countries with the principles of so-called sound public finance. There are serious questions about the coherence of its medium term macroeconomic strategy for member countries. An Organisational Discourse perspective (Dostal, 2004) informs our understanding of the conduct of this organisation in the design and dissemination of labour market and macroeconomic policy. While its policy framework is not under challenge from other influential international organisations, its credibility as an impartial disseminator of economic policy would be undermined by any major concessions.

1 Introduction

While nation states remain responsible for their own policy making, they operate within contested transnational knowledge networks in which common policy frameworks are negotiated, if not universally implemented, to address the growing number of regulatory issues in areas including the economy, the environment and communications. Inter-Governmental Organisations (IGOs) are key players in these networks and contribute to policy harmonisation (Mahon and McBride, 2008) and diffusion both cross-nationally and 'in emergent venues of global governance' (Stone, 2004).

The role of the Organisation for Economic Co-operation and Development (OECD) in labour market and macroeconomic policy design and dissemination can be traced back to the early 1990s when member states commissioned the organisation to prepare a report to analyse their persistently high unemployment rates.

High unemployment was attributed to the inability of countries to adapt and innovate in response to economic change and hence was viewed as largely structural in origin. The

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1 Governance is 'a variety of mechanisms of regulation, operating in the absence of an overarching political authority' (Mahon and McBride, 2009).
removal of supply side impediments to the smooth operation of national economies was advocated. The Jobs Study also concurred with the growing macroeconomic conservatism which emphasised the need for a reduction in structural budget deficits and public sector debt over the medium term and the pursuit of low inflation (Mitchell and Muysken, 2008).

The Economics Department had sole responsibility for the Jobs Strategy which was developed in 1995 to operationalise the Jobs Study, by providing policy recommendations (Noaksson and Jacobsson 2003:17-18). As part of the policy dissemination process and as a means of applying pressure to member countries, the OECD conducts Peer Reviews every 18 months to 2 years. The policy reforms, which have been implemented unequally across member countries, have had limited success, however, although official rates of unemployment did decline slowly until 2008 during a period of sustained growth.

A growing body of empirical literature has challenged the OECD’s interpretation of the degree of compliance of member countries (Baker et al, 2004, McBride and Williams, 2001), as well as the underlying neo-liberal policy framework which advocated extensive supply side reform (e.g. McBride and Williams, 2001; Larsen, 2002; Baker et al, 2004; McBride et al, 2008), and, in normal circumstances, rejected a role for active fiscal policy (e.g. Modigliani, 2000; and Mitchell and Muysken, 2008).

Following a reassessment of the original Jobs Study proposals, concessions were made about the effectiveness of some supply side policy reforms (OECD, 2006a). OECD (2006b) acknowledged the existence of two successful policy models, but took a more orthodox perspective about the conduct of macroeconomic policy by limiting it to the stabilization of economic activity around a trend, whereas the Jobs Study allowed for the achievement of a higher growth trajectory (Watt, 2006).

Since the advent of the Global Financial Crisis (GFC), the OECD, and other IGOs, such as the European Union (EU) and the International Monetary Fund (IMF), has acknowledged that fiscal stimulus packages were required in many countries to counter the sharp declines in economic activity and increased unemployment. However, these organisations have continued to advocate conservative macroeconomic policy, namely monetary policy geared to inflation targeting and so-called sound public finance, through the medium term pursuit of fiscal sustainability (ECB, 2009; Freedman et al, 2009; OECD, 2009a,b,c).

Mahon and McBride (2008) pose the question as to whether the changes underway at the OECD, represent the emergence of a new policy paradigm. We argue that the OECD remains wedded to a neo-liberal economic policy framework, but its macroeconomic policy prescription not only has largely avoided scrutiny, but it also lacks coherence because the underlying concept of fiscal sustainability is both under-developed and flawed.

We concur with Dostal (2004) in arguing that the role of the OECD in transnational policy formulation is informed by the adoption of an Organisational Discourse (OD) perspective in which the behavior of organisations is characterised by long-term agenda planning, underpinned by the need for institutional sustainability (see also Mahon and McBride, 2008). Thus, the long term survival of the OECD as an influential IGO would be threatened by any major concessions associated with economic policy design. However there is no direct pressure to make concessions, despite the GFC, because, as noted, these policy areas are uncontested by the major IGOs. Consequently the OECD relies on obfuscation, through the adoption of sanitised, repetitive, and vague forms of exposition, which draw on carefully selected academic research, but lack rigour. By re-specifying some if not all unemployment as structural in line with its NAIRU framework (e.g. OECD, 2009c), the problem of insufficient
aggregate demand and hence the need for ongoing budget deficits is excised, and the imperative for supply side initiatives is reinforced.

We first briefly outline the structure and operation of the OECD, followed by the theoretical perspective to be adopted. In Section 4 the theoretical and empirical challenges to the Jobs Study policy agenda are documented, with particular reference to fiscal sustainability. Section 5 concludes.

2 The structure and operation of the OECD

2.1 Introduction

The origins of the OECD and its conceptualisation as a powerful IGO within a dense web of transnational knowledge networks have been documented at length by, amongst others, Bainbridge (2000), McBride and Williams (2001), Noaksson and Jacobsson (2003), Dostal (2004), and the edited volume by Mahon and McBride (2008), so the reader is directed to these references. However some details of its institutional structure are important in understanding its operation and are presented below.

The Ministerial Council is the governing body and has representatives from all 30 member states and one from the European Commission. The Secretary-General is the chair. Decisions are adopted by mutual agreement of all members.

The Secretary-General leads the Secretariat, which has 15 directorates, including the Economics Department. Over 200 specialised committees, working and expert groups provide assistance. This structure exists alongside informal networks of ad hoc groups, many of them long-standing with their own bureau and elected chair (Dostal, 2004). About 2,500 agents work in the Secretariat which also prepares analytical studies for which the OECD takes responsibility, so that no member is formally bound by the content. Most of the 700 researchers are economists but there are also lawyers, scientists and regulatory experts.

About 40,000 senior officials from national administrations attend committee meetings annually to request, review and contribute to work undertaken by the Secretariat. Official OECD publications, in particular ad hoc policy documents (e.g. OECD, 2006b, 2008b, 2009a,b,c) are written in a stylized manner and underpinned by key assumptions which constitute the conventional wisdom. In this context, Dostal (2004:444-445) argues that Organizational Discourse is not scientific.

In fact, organizational discourse is not necessarily very discursive. Rather, it is based on the power of discursive closure. Organizations create their own knowledge based on strategically selected issues and aim to disseminate resulting expertise in communication with an organization's policy-making environment.

There is a high degree of interaction and interdependency between national government departments and the OECD. In contrast to the operation of the Secretariat, methodological debates about new statistical data and technical criteria for OECD benchmarking exercises occur within working groups which facilitates the emergence of epistemic communities, made up of experts linked by cognitive and professional ties (Haas, 1992).

The Economic Policy Committee (EPC) and the Economic Development and Review Committee (EDRC) are influential in the design and dissemination of economic policy and

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participate in the preparation of both the \textit{Economic Outlook} and country based \textit{Economic Surveys} (Noaksson and Jacobsson, 2003:14). Both committees are linked to the Economics Directorate.

2.2 \textit{The jobs study}

The OECD's conversion to a neo-liberal reform agenda originated in its response to the inflation breakout after the first oil price shock in the mid-1970s and the subsequent stagflation. Although the main causes of inflation were considered political, social and psychological, the McCracken Report (1977) took a narrow ideological perspective by advocating demand management policies, despite its supply side origins, and also a reduction in government regulation through supply-side reforms (Keohane, 1978:124-25, reported in Porter and Webb, 2007).

In response to higher unemployment in Europe in the early 1990s, the Council of Ministers requested that a comprehensive study of structural issues be undertaken, drawing on the inter-disciplinary expertise of the OECD, despite potential difficulties of achieving consensus between directorates.

Three major developments were identified as contributing to rapid economic and social change. First, waves of financial and product market deregulation in the 1980s had greatly enhanced the potential efficiency of national economies. Second, the rate of globalisation had accelerated. Third, pervasive technological change was occurring, especially via new information technologies.

The fundamental cause of higher unemployment in OECD countries was the inability to adapt to this rapid change. The OECD approach reflected its essentially economic mandate to make member countries more innovative and prosperous in an increasingly integrated and competitive global economy. Like the 'Washington Consensus' imposed on developing countries, the reforms were based on the primacy of markets, and the imperative to remove the institutional fetters allegedly inhibiting their operation (LaJeunesse et al, 2006), that is institutions, rules and regulations which particularly affected the operation of labour markets. Thus unemployment was seen as mainly structural. The \textit{Jobs Study} was not supposed to adopt an explicitly political or ideological stand (Noaksson and Jacobsson, 2003:44), but to claim that the free market model is devoid of political and ideological content is at best naive.

A broad range of supply side policies were advocated for member countries, including increased flexibility of working-time; greater responsiveness of wage and labour costs to local conditions and individual skill levels; reform of employment security provisions; active labour market policies; improvement of labour force skills; reform of unemployment and related benefit systems and their interaction with the tax system; and enhancement of product market competition. Thus the agency of the state should be subordinate to market forces whenever possible (Dostal, 2004:447).

Also, OECD (1994:3b) advocated growth enhancing, macroeconomic policy: Macroeconomic policy has two roles in reducing unemployment: over the short term it limits cyclical fluctuations in output and employment; and over the longer term it should provide a framework, based on sound public finances and price stability, to ensure that the growth of output and employment is sustainable, \textit{inter alia} through adequate levels of savings and investment (my emphasis).
These recommendations were supported by member countries whose ministers agreed to implement them, but the OECD had no power to impose sanctions on recalcitrant members. Most OECD documents between 1994 and 2001 took the Jobs Study assumptions as unproblematic and repeated its findings and conclusions (Dostal, 2004).

2.3 Multilateral surveillance and peer review

As part of its role as an IGO, the OECD engages in the production of statistics, analytical work in relationship to soft regulation, such as best practice identification through comparative studies, mutual surveillance, recommendations, peer review and peer pressure and the implementation of hard regulation via standard setting and adoption of binding international agreements (Mahon and McBride, 2008).

The major influence of the OECD in transnational governance through its Secretariat is its meditative function, in which it draws on its significant research capacity to undertake empirical analysis often employing new measures and benchmarks thereby widening the scope of statistical monitoring and comparison of member countries (Mahon and McBride, 2008:10; Marcussen, 2004). These data and the results of cross-country empirical policy analysis appear in OECD publications, including Economic Outlook and Employment Outlook, and Economics Department Working Papers which contribute to the organisation's authority which is predicated on impartial analytical work. 'The organisation aims to depoliticise issues of economic and social policy-making into questions of 'pure' expertise to be dealt with from the position of 'best practice' and without too much institutionalised interference from interest groups' (Noaksson and Jacobsson, 2003:10; see also Dostal, 2004:446), but their best practice policies do not always gain universal acceptance (Ougaard, 2007:4).

The meditative activities involve the power to classify, fix meanings, and diffuse norms (Barnett and Finnemore 1999, 711; Stone, 2004). In particular, the OECD contributes to the ongoing development of a sense of identity for members as it develops policy prescriptions appropriate for modern, liberal-democratic countries which are market-friendly, and efficient (Noaksson and Jacobsson, 2003; Porter and Webb, 2007). The OECD tries to achieve policy convergence through arguments, negotiations and persuasion (Marcussen 2002).

With its access to resources, the Economics Department assumes a major role in the inquisitive mode of regulation, through Peer Review of each member country on a 12-18 month cycle (Noaksson and Jacobsson, 2003:18). A member country is not obliged to follow the OECD recommendations, although there are pressures on states to conform to new standards and practices (Mahon and McBride, 2008), particularly since the OECD publishes information about the degree of compliance to the blueprint by member countries (OECD, 2004b:4). All countries must sign the final report, which is published, after unanimous adoption in the EDRC (Noaksson and Jacobsson, 2003:27-28).

PR is designed to assist each member to improve its policy making by the adoption of best practice and compliance with established standards and principles (Pagani, 2002). The OECD's identity-defining function also helps to explain why member states do not use their power to veto power to eliminate critical recommendations from EDRC reviews, since this would be widely viewed as inappropriate by their peers and, in many cases, domestic public opinion (Porter and Webb, 2007:8).
Another possible motive would be to exploit the OECD's reputation for expert advice to shift domestic public opinion in favour of preferred policies (OECD, 2002:10; Dostal, 2004; Mahon and McBride, 2008). Sometimes states do insist that critical comments be removed.

All OECD findings, both written and spoken, are presented in a non-technical, non-confrontational and stylized manner, which are accessible to a non-specialist audience, particularly policymakers. Policy principles are articulated which can be adapted according to the national circumstances, so country specific policy recommendations are avoided (Lodge, 2005). Notwithstanding PR, Lodge (2005), Dostal (2004) and Mahon and McBride (2008) are unconvinced about the influence exerted by the OECD on policy making.

3 Theoretical perspectives

Our focus is the OECD's design and dissemination of economic policy and specifically how it has responded to theoretical and empirical challenges to its hegemony. As noted, an organizational discourse (OD) perspective appears to be the appropriate theoretical lens within which to understand its behaviour (Dostal, 2004, Mahon and McBride, 2008).

OD, which describes the language and symbolic media used by organizations and their employees, (Grant, 2001), is associated with long-term agenda setting and is underpinned by the need for institutional sustainability. A key aspect of the OECD's discursive power is the repetition of key components of its policy framework in a range of contexts, so that these components can be viewed as part of the conventional wisdom (Dostal, 2004:445; Jackson, 2008). A good example is fiscal sustainability which was articulated in the Jobs Study, and is frequently referred to in OECD policy documents (e.g. OECD, 2009a), with minimal elaboration, despite its potential inconsistency with running fiscal stimulus packages during the current crisis.

The absence of competing discourses about the principles of macroeconomic and labour market policy reflects the continued dominance of the neo-liberal policy framework both within other major IOGs, such as the World Bank, IMF and the ECB, which would have the resources and capacity to challenge the OECD, and also within most academic economics departments which train many employees of these organisations. While recognising the influence of Anglo-American-trained professional economists on the OECD's OD, Mahon and McBride (2008:15) note that directorates develop their own ODs, so they question whether the institution's discourse is merely 'a transmission belt for the ideas dominant in economics departments'.

Certainly neo-liberal ideas have had a profound influence on the framing of the policy template by the Economics Department. Mahon and McBride (2008) contrast the hard neo-liberal economics perspective of the Economics Department which mainly interacts with national Finance Departments and has had minimal interaction with civilian society (Ougaard, 2009).

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2 The IMF promoted the adoption of a global fiscal stimulus, but recognized the financial constraints facing some countries and the need for a commitment to longer term fiscal discipline (Freedman et al, 2009). Likewise the ECB (2009) acknowledged that fiscal policy action was 'largely justified', but cautioned that EU countries were 'bound by their obligations under the Treaty and the Stability and Growth Pact, so it is essential that fiscal policies are conducted within a predictable, medium-term oriented framework'.

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2007), with the *inclusive* or *innovative* liberalism of the Directorate for Education, Employment, Labour and Social Affairs (DEELSA), which communicates with ministries dealing with labour and social issues. “(I)inclusive liberalism” is seen as a distinctive variant of liberalism, of equivalent status to classic, new, or social liberalism and neo-liberalism, but does not pose a fundamental challenge to neo-liberalism’ (Mahon and McBride, 2008:18).

In its policy recommendations, there is an unclear relationship between the OECD’s own research and the best available academic evidence, since the OECD discusses the latter in a selective and superficial manner, but wishes to draw on its scientific authority (Dostal, 2004:450-451).

Through its control of specialist regulatory knowledge, the OECD has also gained a comparative advantage in new areas of policy making, including regulation of private health care and private pensions. Benchmarking new public policy areas also assists the OECD to broaden its OD at its Committees and Ministerial Council meetings and to provide guidance for national policy-makers (Dostal, 2004). The authority of the OECD in these new areas is enhanced by its capacity to develop comprehensive statistical databases as well as amend databases in response to new circumstances.3

However ‘(A)ny organization’s comparative advantage in broader policy networks depends at the same time on the ability to sustain its authoritative voice in specific areas of expertise’ (Dostal, 2004:445). The neo-liberal messages of supply-side reform and sound macroeconomic policy have been largely unchanged over 15 years, which is important for the OECD’s ongoing credibility, despite the absence of competing ODs from other major IGOs.

4 Challenges to the OECD neo-liberal economic policy agenda

4.1 Introduction

We now briefly document evidence of non-compliance by member countries and the theoretical and empirical challenges by heterodox economists to the OECD policy blueprint. The OECD has some leeway in its implementation of supply side policy in the light of empirical contradictions, but to maintain its credibility as an influential IGO within international knowledge networks, it is locked into the principle of ‘sound public finance’ or fiscal sustainability. So we also critically assess the OECD’s conception of fiscal sustainability and its implementation, following the GFC.

4.2 Compliance

Despite implementation of PR, the degree of compliance in the early years after the Jobs Strategy was unimpressive (Rueda and Pontusson, 2000:381). Also outcomes including income inequality, continued to correlate quite strongly with the various ‘styles’ of welfare state. Despite its apparent sensitivity to cross-country differences, the Jobs Strategy was criticised for its decontextualised benchmarking by requiring the achievement of perfectly free labour markets (Hemerijck and Visser 2001), although post-Keynesians deny that such labour markets are either necessary or sufficient for full employment. Also countries with fiercely defended

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3 OECD (2009b:14-16) documents new social financial and other economic statistics which will assist in the development of new economic and social policies in response to the GFC.

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traditions of so-called rigidities, such as employment protection, strong trade unions and relatively high employment benefits, were expected to undertake reforms to reduce workers rights in order to create jobs (Larsson 1998:412 quoted in Noaksson and Jacobsson, 2003:31). On the other hand, OECD (1999a:41) claimed that successful countries had adopted different approaches to labour and product market reform, depending on their social, cultural and institutional characteristics, but reforms had always followed the main thrust of the Jobs Strategy. Armingeon (2007:906) argues that the impact of IGOs on policy making is conditioned by domestic politics, institutions and extant policies. Thus IGOs face a quandary in that decontextualised policy prescription may well be largely ignored by individual countries.

Armingeon (2004) concluded that the OECD's advice enjoyed low efficacity. Even when there appeared to be a strong link between OECD recommendations and member country policy, e.g. the UK, there was little evidence that the OECD set the agenda for change (Manning 2004:209, Mahon and McBride, 2008:17; see also Lodge, 2005). McBride and Williams (2001) noted major inconsistencies in the OECD's assessment of the degree of compliance by some countries. They found no significant association between a country's degree of compliance and its labour market performance.

4.3 Empirical evidence

In the 2006 Employment Outlook OECD (2006a) acknowledged that both youth unemployment and overall labour underutilisation remained high, with the latter being driven in part by increased underemployment. Also income inequality had increased particularly in the USA (OECD, 2008a).

The flaws of the OECD's supply side agenda have been reported at length, by, amongst others McBride and Williams (2001); Baker et al (2002, 2004); Mitchell and Muysken (2004); Bradley and Stephens (2007) and McBride et al (2008) and concessions have been made by OECD (1997:63–92; 1998; 1999a; 1999b: 86–8; 2004a; 2006a), which culminated in a reassessment of the Jobs Study (OECD, 2006b). Little reference was made to the stance of macroeconomic policy.

In its reassessment, OECD (2006b) again emphasised the importance of sound budget balances to the conduct of macroeconomic policy, as well as the removal of obstacles to participation and job creation through tax-benefit reforms, activation policies, workplace flexibility, lifelong learning and removing obstacles and providing incentives to participation of under-represented groups, including the disabled, women and older workers, but the problematic outcomes associated with employment protection legislation were acknowledged (see also OECD, 2008b).

The language of OECD (2006b) is non-technical and no supporting references are provided. For example, 'The record suggests that the 1994 Jobs Strategy remains an effective tool to strengthen labour market performance. Indeed, reforming countries have in general done better in reducing unemployment'. Also 'But new evidence also suggests that, if well-designed and implemented effectively, active labour market programmes can help offset these work disincentive effects and improve re-employment chances of those out of work, while achieving social goals' (OECD, 2006b:9) (my emphasis).

However OECD (2006b) acknowledged that no single combination of policies and institutions is required to achieve and maintain good labour market performance. Market reliant countries including Australia, Canada, Japan, Korea, New Zealand, Switzerland, UK and
USA, combined low welfare benefits and low tax rates to fund these benefits (sic), as well as limited employment protection legislation. These countries achieved an average employment rate of 70.9%, but relatively high income inequality persists.

By contrast, countries, including Austria, Denmark, Ireland, the Netherlands, Norway and Sweden, emphasise 'coordinated collective bargaining and social dialogue', implement more restrictive employment regulations and offer generous welfare benefits but still adopt activation policies. These countries achieved a higher average employment rate (71.9%), lower income inequality but at a higher budgetary cost (sic) (OECD, 2006b:18-19), which reveals that there is no efficiency/equity trade off (Watt, 2006).4

Despite these concessions, the OECD has not encouraged the adoption of the Nordic model by other countries. Possibly there are problems of transferability, but this did not deter the OECD from actively encouraging the take up of the neo-liberal model (Watt, 2006).

Also, '(T)he new Jobs Strategy continues to reflect neo-liberal goals and policy instruments, an indication that any change in direction is one of adjustment rather than transformation' (Mahon and McBride, 2009:19). Thus, consistent with the OD framework, maintaining credibility in the central policy area is crucial to institutional survival. This also requires that other portfolios do not contradict the dominant economic paradigm (Mahon and McBride, 2009:19), which remains the case despite the adoption of inclusive liberalism by DEELSA.

4.4 Fiscal sustainability

The OECD continues to attribute the failure of member countries to achieve full employment and stable inflation to labour market rigidities and other market imperfections (Mahon and McBride, 2008). Thus the OECD remains wedded to a NAIRU based macroeconomic model, which has no role for aggregate demand management, despite evidence to the contrary. Ormerod (1994:203) found that countries which avoided high unemployment rates in the 1970s had a sector operating as an employer of last resort. Aggregate demand determines employment (Modigliani, 2000). Mitchell and Muysken (2008) find evidence of unemployment persistence in selected OECD economies (1960-2006) which challenges the claim that departures from the NAIRU are temporary following aggregate demand shocks. Also they find that the NAIRU is cyclically sensitive (see also Sawyer, 2004), which rejects the supply-determined NAIRU (Layard et al, 1991:18).

Recent documents (OECD, 2009a,b,c) accept the implementation of fiscal stimulus packages in the aftermath of the GFC, particularly given the limited scope for monetary policy if interest rates are already low, but argue for medium-term fiscal sustainability.

A charitable explanation of the OECD's acceptance of, if not enthusiasm for, fiscal stimulus packages in some countries would be that, despite strong equilibrating properties of economies, restoration of the unemployment rate in line with the (higher?) NAIRU after such a major real shock would take time. Both neo-liberal and heterodox economists agree that

4 However, macroeconomic policy failures of OECD countries, including corporatist ones, are mainly responsible for high rates of labour underutilisation. When budget deficits should have been used to generate jobs for all those wanting work, various restrictions have been placed on fiscal policy. Monetary policy has also become restrictive, with inflation targeting – either directly or indirectly – pursued by increasingly independent and vigilant central banks (Mitchell and Muysken, 2008).
prolonged high unemployment is highly deleterious to potential GDP due to hysteresis, which in turn restricts medium term growth prospects. In short, equilibrating forces do not operate quickly enough in reducing actual unemployment to prevent a significant rise in structural unemployment.

The imperative for fiscal sustainability lacks rigor, however with the OECD obfuscating through inconsistent, incomplete and often unsubstantiated statements. Consequently the organisation is unable to provide member countries with a clear set of principles about the future conduct of macroeconomic policy.

First, caution is expressed about further measures:
The scope for further stimulus depends on the degree of government indebtedness. Whether a more ambitious fiscal stimulus than currently planned is appropriate depends on country-specific circumstances. Evidence shows that adverse reactions in financial markets are likely in response to higher government debt and that such reactions may depend on the initial budget situation (OECD, 2009b:10-11).

The OECD then differentiates between countries which have ‘a weak initial fiscal position’ and those with the ‘most scope for fiscal manoeuvre’, but ‘for others, action would only be warranted in case activity looks to turn out even weaker than projected’. Thus there is no iron clad rule in terms of acceptable expenditure levels. The policy objectives are never clearly outlined which makes it difficult to decipher the extent of possible policy trade-offs.

Second, OECD (2009b:17) notes that ‘Fiscal stabilisation is particularly important in countries that do not have national monetary policy’, but fails to explain that some Eurozone countries, including Ireland, have adopted pro-cyclical, rather than counter-cyclical fiscal policy. In 2009(2), Ireland had a 12 percent unemployment rate (and a projected rate of 17 percent in 2010, Bergin et al, 2009) and a projected net debt to GDP ratio of 38 percent whereas Japan had an unemployment rate of 5.7 percent and a projected net debt ratio of 107 percent (OECD, 2009c, Tables 4.4 and 4.5). Yet Ireland introduced a deflationary budget in April 2009 and plans further major budget cuts, while Japan introduced a fiscal stimulus package projected to be 2 percent of GDP over the period 2008-2010 (OECD, 2009b).

The OECD fails to acknowledge that the conduct of fiscal policy is fundamentally different in Eurozone countries, as the above example illustrates, because their governments are budget constrained, by choice, under the Stability and Growth Pact, albeit with a temporary relaxation due to the GFC. By contrast, countries, such as Japan, the USA, the UK and Australia, operate with their own fiat currencies under flexible exchange rates and are not budget constrained (Mitchell and Muysken, 2008). Thus the OECD trivialises the conduct of fiscal policy by appealing to the conventional wisdom that, like prudent households, all governments are budget constrained.

Third, OECD (2009a:124) correctly notes that the impact of fiscal imbalances on interest rates is ‘both mixed and controversial’. Their formal econometric work (Box 3.2), which analyses the determinants of the interest rate spread, is based on 6 (6 monthly) observations between 2005(4) and 2008(4) for 10 EMU countries, but neither the choice of countries, nor the small number of time series observations is justified which is most unsatisfactory because, in contrast to countries with their own independent fiat currencies, EMU countries must formally borrow to finance budget deficits.

5 For example, Ireland is required to restore a budget deficit of 3 percent of GDP or better by 2013.

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An implication of the finding that higher expected deficits increase long-term interest rates is that a temporary fiscal injection may be more effective than a more sustained fiscal injection which is expected to significantly worsen the long-term fiscal outlook (my emphasis).

Whether larger deficits raise long term interest rates (rather than just the spread, if the OECD econometric work is to be believed), depends largely on the behavior of central banks in setting short term rates. *Ceteris paribus*, by increasing the reserves of the banking system, more government spending places downward pressure on short term interest rates in countries with their own fiat currencies. However most central banks in the developed world are independent of their national governments and engage in inflation targeting, which is central to the OECD's policy framework. Consequently there is the possibility of a dysfunctional relationship between fiscal and monetary policy, in the recovery phase, following the implementation of a fiscal stimulus package. For example, in Australia, a country highly compliant to the OECD's policy framework (McBride et al., 2008), the cash rate was raised by 25 basis points in both October and November 2009 following its significant fiscal stimulus, which kept the unemployment rate below 6 percent, but the rate is still expected to rise. A rule of thumb is to double the official rate of unemployment to obtain an hours based measure of labour underutilisation, which also includes hidden unemployment and underemployment (CoFFEE, 2009).

Fourth, OECD (2009c) explores the macroeconomic impact of a number of medium term scenarios for each member country based on fiscal consolidation at an annual rate of 1% of GDP for between 3 and 7 years –depending on the initial fiscal imbalance (deficit) - in addition to the removal of any fiscal stimulus. The impact of fiscal consolidation on aggregate demand and hence output and employment is finessed, despite OECD support for fiscal stimulus packages.

OECD (2009c:219) asserts that, following a deep recession, the substantial rise in unemployment is partially translated into higher structural unemployment (and lower potential output) via hysteresis effects. Short term unemployment is found to be four times as potent as long term unemployment (LTU) in its impact on wage inflation, so that it is argued that (conservatively) 66 percent of any rise in LTU can be treated as structural, thereby reducing potential output. In short the unemployment rate corresponding to close to potential output being produced (ie a small output gap) is significantly higher after a deep recession. If the measurement of potential output is reduced in the recovery because 66 percent of any intervening increase in LTU is deemed to be structural, and also the recovery is weak, then the persistence of high unemployment is at face value largely a structural problem.

In the OECD medium term scenario, unemployment falls in all countries after 2010, with the average rate down from 9.75 percent in 2010 to 6.5 percent by 2017. However, in most European countries their projected unemployment rates remain above pre-crisis levels. ‘This stems from the assumption that hysteresis effects are asymmetric in the sense that they tend to raise the NAIRU when unemployment rises, but do not lower the NAIRU when unemployment falls.’ (OECD, 2009c:230).

The inference here is that the assumption errs ‘on the cautious side’, so that if the extreme assumption of asymmetry had not been assumed, both potential and actual growth would have been higher and unemployment lower. A more realistic proposition is that

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6 Over the medium term scenario, 2011-2017, ‘output gaps are closed as a result of sustained above-trend-growth (despite significant fiscal consolidation)’ (OECD, 2009c:227).

7 This reasoning is extremely dubious.
economies do not have an automatic tendency to equilibrate at the potential (NAIRU) level of output, so a higher level of potential output would reveal higher cyclical unemployment.

Thus, by exaggerating the impact of the recession on the potential output growth rate, via an asymmetric hysteretic process, OECD (2009c) has written out of the script any role for aggregate demand in the determination of output and employment, because, by assumption, output is line with potential by 2017, so there is no cyclical unemployment! The higher level of structural unemployment following the deep recession then reaffirms the need for more structural reforms (OECD, 2009c:214), rather than the adoption of stimulatory fiscal policy.

In summary, the need for fiscal stimulus packages in some member countries is acknowledged, but the OECD claims that there is a need for fiscal sustainability, which is illustrated by medium term simulations, but no attempt is made to provide a coherent justification for the concept. Fiscal sustainability is based on the flawed principle that, like a household, government is budget constrained in an intertemporal sense, (Fulwiller 2006).

Drawing on the principles of functional finance developed by Abba Lerner (Forstater, 1999), Mitchell (1998), Wray (1998) and Mitchell and Muysken (2008) argue that, under a floating exchange rate (so that monetary policy is freed from the need to defend foreign exchange reserves) and the monopoly provision of fiat currency by a national government, there are no constraints on government spending. This spending is the source of funds that the private sector needs to pay its taxes and to net save. Interest bearing government debt is issued to achieve the target interest rate, rather than to finance net government spending.

These arrangements prevail in countries, such as Japan, the USA, Canada and Australia, but not in Eurozone countries which are subject to a voluntarily-imposed monetary system incorporating a common currency. These countries must borrow in order to run budget deficits which are subject to significant constraints through the Stability and Growth Pact.

The systematic achievement of budget surpluses does not normally represent a sustainable full employment policy, because it is associated with ongoing deficits with respect to net private sector savings (saving minus investment), unless the economy is running a large and persistent trade surplus.

Thus, subject to an effective counter-inflation strategy, governments should run budget deficits to fill the prospective spending gap at full employment. Mitchell (1998) argues that the lowest fiscal stimulus required to achieve full employment requires the operation of a Job Guarantee in which all unemployed workers are guaranteed a job at the minimum wage.

Failure to run deficits of sufficient magnitude means that either the economy does not experience full employment or the private sector becomes increasingly indebted, as noted above, which will ultimately lead to a harsh correction in the form of reduced spending when the private sector decides to restore its balance sheets.

8 Members of the Centre of Full Employment and Equity (see http://e1.newcastle.edu.au/coffee/index.cfm ), headed by Mitchell, and other scholars have written extensively about the conduct of macroeconomic policy.

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Despite the OECD apparently exercising considerable trans-national authority in policy formulation, its attempts to impose a neo-liberal policy blueprint on member states have not been particularly successful. Even where there appears to be a consensus concerning the efficacy of certain recommendations, implementation practices differ significantly across countries. The theoretical and empirical challenges to the OECD policy framework have elicited minor concessions with respect to supply side reform. Its macroeconomic policy prescription remains largely consistent with the Jobs Study, so while fiscal stimulus packages have been accepted to address the GFC, the OECD continues to emphasise the imperative for fiscal sustainability through medium term fiscal consolidation.

This paper argues from an Organisational Discourse perspective, that adherence to a neo-liberal macroeconomic policy framework is necessary for the OECD to maintain both its authoritative voice in its specific areas of policy expertise and its influence in broader policy networks. However, recent policy documents reveal inconsistent and unconvincing arguments for fiscal consolidation. The setting of current spending and taxation parameters is not constrained by the past budgetary decisions of those countries operating with their own fiat currencies and under flexible exchange rates, but should reflect the economic, political and social priorities of the government, and geared to the achievement of full employment.

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