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Making the Case for Reform

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FRIDAY, October 18, 2019

1:00PM - 2:00PM, IMF HQ1, Meetings Halls A&B (HQ1-3-430 A&B)

Making the Case for Reform

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IMF research shows that a major broad-based reform push in the area of governance, trade, finance product and labor market could raise output by as much as 7% over 6 years, providing a big boost to jobs and economic growth at a time when the global economy is slowing down. But is it possible to implement far-reaching reforms without paying a price at the ballot box?



Alesina, Alberto, Davide Furceri, Jonathan Ostry, Chris Papageorgiou, and Dennis Quinn. Forthcoming, 2019.

[“Structural Reforms and Electoral Outcomes: Evidence from a New Database of Regulatory Stances and Policy Changes.” Working Paper, International Monetary Fund, Washington DC.](#)

IMF Working Papers are designed to make IMF staff research available to a wide audience. Nearly 300 working papers are released each year, covering a range of theoretical and analytical topics.

Ciminelli, Gabriele, Davide Furceri, Jun Ge, Jonathan D. Ostry, and Chris Papageorgiou. Forthcoming, Friday October 18, 2019.

[“The Political Costs of Reforms: Fear or Reality?” Staff Discussion Note, International Monetary Fund, Washington, DC.](#)

Many countries are experiencing persistent, weak medium-term growth and limited fiscal space. Against this background, economic policy agendas—in both advanced and emerging market economies—are focusing increasingly on structural reforms. The economic benefits of structural reforms have broad agreement. The political economy of reform is, however, less settled for two reasons. First, reforms may generate gains only in the longer term while distributional effects may be sizable in the short term. Second, governments may lack the political capital needed to confront vocal interest groups, wherein politicians may hold back on reforms, fearing they will be penalized at the ballot box. The aim of this Staff Discussion Note is to examine whether the fear of a political cost associated with structural reforms is justified by the available evidence, and whether the data produce lessons about designing reform strategies to mitigate potential political costs. It provides a major addition to recent IMF analysis examining the output and employment effect of reforms (IMF 2009, 2016, and 2019).

Duval Romain, Davide Furceri, Bingjie Hu, João Tovar Jalles, and Huy Nguyen. 2018.

[“A Narrative Database of Major Labor and Product Market Reforms in Advanced Economies.” Working Paper 18/19, International Monetary Fund, Washington, DC.](#)

This paper describes a new database of major labor and product market reforms covering 26 advanced economies over the period 1970–2013. The focus is on large changes in product market regulation in

seven individual network industries, employment protection legislation for regular and temporary workers, and the replacement rate and duration of unemployment benefits. The main advantage of this dataset is the precise identification of the nature and date of major reforms, which is valuable in many empirical applications. By contrast, the dataset does not attempt to measure and compare policy settings across countries, and as such is no substitute for other publicly available indicators produced, for example, by the ILO, the OECD or the World Bank. It should also be seen as work in progress, for researchers to build on and improve upon. Based on the dataset, major reforms appear to have been more frequent in product markets than in labor markets in the last decades and were predominantly implemented during the 1990s and 2000s.

Duval, Romain, Davide Furceri, and Jakob Miethe. 2018.

[“The Needle in the Haystack: What Drives Labor and Product Market Reforms in Advanced Countries?” Working Paper 18/101, International Monetary Fund, Washington, DC.](#)

The political economy literature has put forward a multitude of hypotheses regarding the drivers of structural reforms, but few, if any, empirically robust findings have emerged thus far. To make progress, we draw a parallel with model uncertainty in the growth literature and provide a new version of the Bayesian averaging of maximum likelihood estimates (BAMLE) technique tailored to binary logit models. Relying on a new database of major past labor and product market reforms in advanced countries, we test a large set of variables for robust correlation with reform in each area. We find widespread support for the crisis-induces-reform hypothesis. Outside pressure increases the likelihood of reform in certain areas: reforms are more likely when other countries also undertake them and when there is formal pressure to implement them. Other robust correlates are more specific to certain areas—for example, international pressure and political factors are most relevant for product market and job protection reforms, respectively.

Duval Romain, and Davide Furceri, 2018.

[“The Effects of Labor and Product Market Reforms: The Role of Macroeconomic Conditions and Policies.” IMF Economic Review 66 \(1\): 31-69.](#)

The paper estimates the dynamic macroeconomic effects of labor and product market reforms on output, employment and productivity, and explores how

these vary with prevailing macroeconomic conditions and policies. We apply a local projection method to a new dataset of major country- and country-sector-level reform shocks in various areas of labor market institutions and product market regulation covering 26 advanced economies over the past four decades. Product market reforms are found to raise productivity and output, but gains materialize only slowly. The impact of labor market reforms is primarily on employment, but it varies across types of reforms and depends on overall business cycle conditions—unlike that of product market reforms. Reductions in labor tax wedges and increases in public spending on active labor market policies have larger effects during periods of slack, in part because they usually entail some degree of fiscal stimulus. In contrast, reforms to employment protection arrangements and unemployment benefit systems have positive effects in good times but can become contractionary in periods of slack. The economy's response to such reforms is significantly improved when they are accompanied by fiscal or monetary stimulus.

Fabrizio, Stefania, Davide Furceri, Rodrigo Garcia-Verdu, Bin G. Li, Sandra V. Lizarazo Ruiz, Marina Mendes Tavares, Futoshi Narita, and Adrian Peralta-Alva. 2017.

[“Macro-Structural Policies and Income Inequality in Low-Income Developing Countries.”](#) *Staff Discussion Note 17/01, International Monetary Fund, Washington, DC.*

Despite sustained economic growth and rapid poverty reductions, income inequality remains stubbornly high in many low-income developing countries. This pattern is a concern as high levels of inequality can impair the sustainability of growth and macroeconomic stability, thereby also limiting countries' ability to reach the Sustainable Development Goals. This underscores the importance of understanding how policies aimed at boosting economic growth affect income inequality. Using empirical and modeling techniques, the note confirms that macro-structural policies aimed at raising growth payoffs in low-income developing countries can have important distributional consequences, with the impact dependent on both the design of reforms and on country-specific economic characteristics. While there is no one-size-fits-all recipe, the note explores how governments can address adverse distributional consequences of reforms by designing reform packages to make pro-growth policies also more inclusive.

International Monetary Fund. 2016.

[“Time for a supply boost? Macroeconomic effect of labor and product market reforms in Advanced Economies.”](#) *In World Economic Outlook, October, 101-142, Washington, DC: International Monetary Fund.*

Over the past three decades, the price of machinery and equipment has fallen dramatically relative to other prices in advanced and emerging market and developing economies alike. Could rising trade tensions, a slowing pace of trade integration, and sluggish productivity growth threaten this potential driver of investment going forward? This chapter sets out to answer this question by documenting key patterns in the price of capital goods, its drivers, and its impact on real investment rates.

International Monetary Fund. Forthcoming, 2019.

[“The Macroeconomic Effects of Structural Reforms in Emerging Markets and Developing Economies.”](#) *In World Economic Outlook, October, Washington DC: International Monetary Fund.*

A survey by the IMF staff usually published twice a year. It presents IMF staff economists' analyses of global economic developments during the near and medium term. Chapters give an overview as well as more detailed analysis of the world economy; consider issues affecting industrial countries, developing countries, and economies in transition to market; and address topics of pressing current interest. Annexes, boxes, charts, and an extensive statistical appendix augment the text.

Ostry Jonathan David, Alessandro Prati, and Antonio Spilimbergo. 2009.

[“Structural Reforms and Economic Performance in Advanced and Developing Countries.”](#) *Occasional Paper 268, International Monetary Fund, Washington DC.*

This volume examines the impact on economic performance of structural policies—policies that increase the role of market forces and competition in the economy, while maintaining appropriate regulatory frameworks. The results reflect a new dataset covering reforms of domestic product markets, international trade, the domestic financial sector, and the external capital account, in 91 developed and developing countries. Among the key results of this study, the authors find that real and financial reforms (and, in particular, domestic financial liberalization, trade

liberalization, and agricultural liberalization) boost income growth. However, growth effects differ significantly across alternative reform sequencing strategies: a trade-before-capital-account strategy achieves better outcomes than the reverse, or even than a “big bang”; also, liberalizing the domestic financial sector together with the external capital account is growth-enhancing, provided the economy is relatively open to international trade. Finally, relatively liberalized domestic financial sectors enhance the economy’s resilience, reducing output costs from adverse terms-of-trade and interest-rate shocks; increased credit availability is one of the key mechanisms.

Ostry Jonathan David, Andrew Berg, and Siddharth Kothari. 2018.

**[“Growth-Equity Trade-offs in Structural Reforms.”](#)
**Working Paper 18/5, International Monetary Fund,
Washington DC.****

Do structural reforms that aim to boost potential output also change the distribution of income? We shed light on this question by looking at the broad patterns in the cross-country data covering advanced, emerging-market, and low-income countries. Our main finding is that there is indeed evidence of a growth-equity tradeoff for some important reforms. Financial and capital account liberalization seem to increase both growth and inequality, as do some measures of liberalization of current account transactions. Reforms aimed at strengthening the impartiality of and adherence to the legal system seem to entail no growth-equity tradeoff—such reforms are good for growth and do not worsen inequality. The results for our index of network reforms as well as our measure of the decentralization of collective labor bargaining are the weakest and least robust, potentially due to data limitations. We also ask: If some structural reforms worsen inequality, to what degree does this offset the growth gains from the reforms themselves? While higher inequality does dampen the growth benefits, the net effect on growth remains positive for most reform indicators.

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