

Comments on “Time for a Supply Side Boost? The Macroeconomic Effects of Labor and Product Market Reforms in Advanced Economies” Ch. 3, WEO, April 2016, presented by Romain Duval

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Overview

- ✦ Structural reform is the most important policy for most advanced economies, where the fiscal space is limited and the monetary policy is constrained by the zero interest rate.
- ✦ This WEO chapter provides a birds-eye view on the frontier of structural reform analysis, utilizing a wide range of long historical data for labor and product market reforms.
- ✦ Unfortunately, results are a bit mixed, calling for supplementary monetary and fiscal policies.
 - ✦ The theoretical model shows long-run gains with short-run pains.
 - ✦ Regressions show many positive effects during economic booms but some negative effects during recessions.

Reverse Causality: Recession → Reform?

- ✚ Political economy suggests that recession / crisis is the key driver for past reforms (Box 3.1, Abiad and Mody (2005)).
- ✚ Then, regression results of
[Reform → Slow economic growth]
may be actually representing
[Recession → Reform → Slow economic growth]
- ✚ To be precise, better to have counterfactuals, which are not available. The second best is theoretical model predictions, which indeed show positive long-run effects of reforms.
- ✚ Why not reporting more on model-based empirical studies (e.g., Townsend and Ueda (2010))?

Credit Constraint Matters

- ✚ Credit constraint matters in both theoretical model and regression studies.
- ✚ Then, why not include financial sector structural reform, often known as financial liberalization? There is a long history of such studies at the IMF RES and MCM, including myself.
- ✚ During financial crisis periods, credit constraints are tightened and, your theory keeping credit constraint same (I think), would not describe the reality well.

Should China be praised as a country having minimal protection of workers?

- ✦ Labor protection is likely minimal. Rather the problem is prevalence of sweat shops.
- ✦ Claessens and Ueda (2016, early version IMFWP 08) show that employment protection may have inverse-U shape effects on economic growth.
 - ✦ Basic worker rights protection is good for both firms and workers because some level of job security provides workers for incentives to build (firm-specific) skills.
 - ✦ Generous employment protection seen in continental Europe and Japan is detrimental to growth.