New approaches to global solutions

Building a new growth narrative around complexity to deliver for people's well-being

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BETTER POLICIES FOR BETTER LIVES

The Organisation for Economic Co-operation and Development (OECD) is an international organization that works to build better policies for better lives. Our goal is to shape policies that foster prosperity, equality, opportunity and well-being for all. We draw on almost 60 years of experience and insights to better prepare the world of tomorrow.

Together with governments, policy makers and citizens, we work on establishing international norms and finding evidence-based solutions to a range of social, economic and environmental challenges. From improving economic performance and creating jobs to fostering strong education and fighting international tax evasion, we provide a unique forum and knowledge hub for data and analysis, exchange of experiences, best-practice sharing, and advice on public policies and global standard-setting.

WE ARE CONFRONTED WITH A RANGE OF BAD OUTCOMES...

At least since the onset of the global financial crisis in 2008, it has become increasingly clear that the economic performance of many OECD countries is deficient in a number of important ways.

To begin with, economic growth has slowed. The rate of increase of per capita GDP in OECD countries declined from over 2% per year on average in the twelve years preceding the global crisis to only 1% in the twelve years since. Part of that decline is attributable to the depth of the crisis itself, the sharpest global downturn in 80 years, but even excluding the crisis years of 2008-09, OECD-wide per capita GDP has grown by an annual average of 1.7% over the past 10 years, half a percentage point below the 2.2% recorded in the 10 years to 2007.

Moreover, the fruits of economic growth are not being shared equally. The gap between rich and poor has widened since the 1980s in the large majority of OECD countries. The OECD average Gini coefficient of income inequality stood at 0.32 in 2017, up from 0.29 three decades ago. Today, the richest 10% of the population earns nine and a half times the income of the poorest 10%, up from a ratio of 7:1 in the 1980s; at 8:1 in the 1990s and 9:1 in the 2000s. When combined with slower rates of growth in average incomes, the skewed distribution of the gains has meant that many people in our economies have seen little if any increase in their material standard of living over long periods, sometimes even decades. This is also reflected in surveys showing record-low numbers of people expecting their children to be better off than they are. A related problem is the decline in social mobility seen in many OECD economies: The recent OECD report A Broken Social Elevator? estimates that on average it would now take five generations for a child born into a low-income family to reach the median income, while those at the top will remain there. We call this "sticky floors" and "sticky ceilings". Moreover, this is not a problem of people at the bottom of the income distribution. On the contrary, increased inequalities strongly affect middle classes, who have seen their income stagnate, while the cost of housing, health and education have grown several times more.

Last but not least, the quickening drumbeat of bad news relating to the environment in recent years – be it unprecedented wildfires in Australia, rampant plastic pollution in the oceans, deforestation in the Amazon or the accelerating loss of biodiversity worldwide – has made it indisputably clear that human economic activity is contributing to a series of planetary emergencies. Above all, the costs of ongoing climate change are coming ever more starkly into view.

On current trends, regions of the world will become uninhabitable due to rising sea levels or desertification, the likelihood and intensity of extreme weather events will increase, and changing precipitation patterns and temperatures will affect crops and livestock. Climate change might also lead to so-called "tipping-points", i.e. dramatic changes in the system that could have catastrophic and irreversible outcomes for natural systems and society. Examples of potential non-linear irreversible changes include increases in ocean acidity, which would affect marine biodiversity and fish stocks, accelerated methane emissions from permafrost melting, and rapid climate-driven transitions from one ecosystem to another. Moreover, the world has already experienced damaging conflicts and mass migrations arising from droughts and water stress, and the likelihood that continued climate change would trigger further such episodes is high.

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It is against this backdrop that in 2011 we launched the New Approaches to Economic Challenges (NAEC) initiative at the OECD to explain better how our economy works, with a view to providing better policy advice and fostering better outcomes. NAEC has done this by combining the

OECD's strengths in evidence-based policy advice with the insights and expertise of a network of partners and institutions outside our organization. Such partners include research institutes (e.g. IIASA, INET), public institutions (e.g. the Bank of England and the European Joint Centre for Research), foundations (e.g. Partners for a New Economy), and businesses (e.g. asset managers Baillie Gifford).

...WHICH IN PART REFLECT SHORTCOMINGS IN ECONOMIC ANALYSIS AND POLICY MAKING

In parallel to the growing dissatisfaction with a number of aspects of economic outcomes in OECD countries, there has also been a decades-old questioning of many of the tenets underpinning mainstream approaches to economic growth and its drivers. Researchers have called into question a number of standard assumptions: that economic agents are maximizers (utility for households, profits for firms), that they act atomistically (ignoring other agents), that they are "rational" and homogeneous, that no economic agents have power, that markets have unique stable equilibria etc. It has been shown that all these assumptions are unreal, and that it matters. When agents are heterogeneous, strategic, concerned with relativities, use rules of thumb, have adaptive expectations and are influenced by history, culture and "framing", and when they participate in markets where economic power is important and where multiple and unstable equilibria are possible and path dependence common, outcomes can be quite different to the predictions of the old standard models. Adopting more accurate characterizations of people's economic behavior can be of great help in understanding how we came to have slow growth, damaging financial crises, high levels of inequality and environmental degradation, and in designing policies to achieve better outcomes. Understanding that markets are the result of policies and regulations would help to better frameworks and outcomes.

»Narratives shape what is going to happen and how we react to it.«

Another problematic issue has been the tradition of reductionism – where we separate complex realities into specialized disciplines, fields of research, agencies and ministries, each focused on a part of the overall truth. Thus, even when it was recognized that the ultimate objective is sustainable well-being, which is multi-dimensional (income, health, security, status, fairness etc.), it has tended to be assumed that the dimensions can be considered separately. Thus, the problem of maximizing income (GDP) could be considered in isolation from questions of distribution or the environment. When interactions were considered, there was often a tendency to assume that other aspects of well-being could be relied upon to be correlated with per capita GDP. For example, the well-known Kuznets curve hypothesis predicted that income inequality would continue to decline in rich countries as per capita income rose, and a similar relationship was argued for environmental degradation, implying that raising per capita GDP would tend to solve the problem of pollution. This encouraged the tendency to focus narrowly on GDP growth as the objective of economic policy. A similar assumption of separability afflicted the role of finance in the economy: The financial sector was typically lacking from standard models used to analyse and forecast macroeconomic developments.

The poor outcomes in terms of inequality, environmental quality and economic growth itself strongly suggest that the reductionist tradition has to be rejected and a more systemic approach adopted. Trickle down economics do not work, and the environmental emergency calls for a better understanding of the links between different policy issues and decisive action. We have come a long way toward understanding that the economy, society and the environment are not only complex systems in themselves, but that they form a "system of systems" that is best considered as a whole in trying to promote change that puts people at the centre. This should be the core of our economic thinking today.

Along with better theories and better specifications of policy objectives, we have also realized that there is a need for better data. One aspect of the excessive focus on GDP that there is no other broad aggregate economic indicator which is as timely and internationally comparable and which has such a long time series. These are formidable advantages. As our former Chief Statistician, Martine Durand, used to remind us, however, "we need to measure what we treasure instead of treasuring what we measure". GDP says nothing about distribution, captures only flows and not stocks, excludes unpaid work, puts no value on leisure, subtracts nothing for environmental degradation, and so on. It is at best a very incomplete measure of economic performance. A great deal of work is underway, both inside and outside the OECD, to move beyond GDP and develop a range of indicators that give a fuller and better picture of sustainable well-being. In fact, the leading role that the OECD has played in showing increased inequalities of income and opportunity was possible when the analysis moved from averages to different income groups, and their disposable household income.

THE NEED TO MOVE BEYOND GROWTH

Nobel laureate Robert Shiller, in one of our NAEC debates, argued convincingly that narratives are not just a way of explaining things to ourselves, of understanding what has happened. They also shape what is going to happen and how we react to it. In that spirit, the Secretary-General of the OECD commissioned an Advisory Group[1] on a New Growth Narrative to examine how economic, social and environmental considerations could be integrated into a coherent approach. The group's report, Beyond Growth: Towards a New Economic Approach, drafted by Michael Jacobs, outlines such a new narrative, which has three main elements.

The first is a new conception of economic performance, going beyond GDP to focus on multiple dimensions of human well-being, including economic security, environmental quality, subjective well-being and the provision of public goods. This does not mean a rejection of growth; rather, it means accepting that growth is just one aim among others, and that focussing on it exclusively is counterproductive. Our work on the Well-Being Framework has built the same narrative, by proposing 11 dimensions that can inform better what matters for people – including subjective well-being. Our Inclusive Growth Initiative is also proposing a dashboard of 24 indicators to inform better the policies to counter inequalities, and advancing a better understanding of the distributional outcomes of the policies we propose.

The second element is composed of the new frameworks of economic theory and analysis to explain better how economies work, together with new tools and techniques to help policymakers develop effective policies. This includes gathering new and better data.

Finally, the new narrative also calls for a wider set of policy and institutional reforms, based on the new frameworks and analysis, to achieve the new social and economic goals. Government action matters to counter inequalities, environmental depletion and social fragmentation.

Speaking at an NAEC Conference, Noam Chomsky welcomed the rethinking of economic orthodoxy proposed in Beyond Growth, highlighting how the report cast new light on the proper role of government. It draws on the ideas of Dennis Snower, a member of the Advisory Group and a longstanding supporter of NAEC who has coined the term "empowering state", and Mariana Mazzucato, another Advisory Group member who has argued for the need for the state to shape markets rather than only seeking to correct market failures. The state can redistribute not only money but also incentives and skills in such a way as to achieve the broader policy goals.

TOWARDS A BETTER APPROACH TO FINDING GLOBAL SOLUTIONS

The task remains of fleshing out the three elements comprising the new narrative in Beyond Growth. At all stages – formulating broader policy objectives, understanding how policies act on those objectives and how different dimensions interact, and designing the policies that will achieve better outcomes – we think that a systems approach is needed. We must move away from linearity, equilibrium, assumptions about the rationality and representational characteristics of agents and instead view the economy as a complex adaptive system, where heterogeneous agents interact, systemic properties emerge and the system continually evolves and reorganizes itself in response to multidimensional stimuli at micro to macro levels.

In making that transition, it will help to enrich the insights from economics with those from political science, engineering, physics, psychology, biology and history. For example, at one NAEC presentation, Douglas Erwin, paleobiologist from the Smithsonian Museum of Natural History, explained how the history of life on earth showed repeated long periods of apparent stability ending in rapid collapse, followed by slow recovery in which new things happen.

NAEC is seeking to draw from a wide range of disciplines in order to help provide a stronger scientific basis for policy, based on a systems approach, and yield a better understanding of dynamics, feedback loops, tipping points, and system collapse. That requires a stronger connection between the "science" and "engineering" of economics, that is, between economic analysis and economic policy, and the development of new analytical tools and techniques such as network models and agent-based modelling. The benefit of the systems approach is to understand better the links and interrelationships between the social, economic and environmental systems, and consider possible unintended consequences of acting with a silo perspective.

»A systems-based approach exposes the intricacies and complications of the challenges we face.«

A systems-based approach exposes the intricacies and complications of the challenges we face. But it also shows that the very characteristics of systems that make the problems so difficult can, by the same token, work in our favor. Positive change can be transmitted quickly too, and small positive actions can have big consequences when they are amplified by the numerous interconnections among people and places. New approaches to finding global solutions means being clear about the direction of change we want to follow and identifying the actions that will push us in that direction.

We should not expect a single synthetic "theory of everything" in economics to emerge any time soon, enabling policymakers to maximize policy objectives by applying a universal model. Rather, a proper appreciation of the complexity of the interacting systems of which the economy is a part is likely to mean exercising judgement, applying a range of approaches, drawing on insights from many disciplines, and keeping in mind multiple goals. It is encouraging that the world's endorsement of the Sustainable Development Goals is in this spirit, as indeed is the Paris Agreement on climate change. At the OECD, we have made a good start on several fronts, not only with NAEC but also via the Inclusive Growth Initiative and the Well-Being Framework. This year's Ministerial Council Meeting in May, chaired by Spain, will take stock of the progress made and chart a course toward a more integrated framework.

This is not an academic exercise. The capacity of current approaches to give answers to the people in the streets that are worried by the "end of the month"; and those that care about the "end of the world", is limited. We need to understand better so we can deliver the OECD's motto of better policies for better lives. There is no time to lose, as the urgency of the current situation is clear. The OECD is keenly aware of the need for global solutions and is determined to remain at the forefront of the effort to find the new approaches that will illuminate them.

[1] The group included Andy Haldane, Michael Jacobs, Nora Lustig, Mariana Mazzucato, Robert Skidelsky, Dennis Snower and Roberto Unger.

Why corporate purpose matters

A plea for responsible profit-making

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INTRODUCTION

After several decades in which shareholder value has been promoted as the most rational goal a corporation should pursue, questions are being raised, doubts are arising, and criticism is becoming louder and louder. Among the alternatives to shareholder value that are emerging, the idea that managers should be attentive to the interests of all stakeholders is gaining ground.

In this paper, three questions are examined:

- How could shareholder value be so successful? There must be economic mechanisms that make it a prominent option for the organization of the business sector.
- What is the contribution of a productive firm to society and how can it be maximized? A firm does benefit many stakeholders, and it is possible to rigorously define the total benefit it brings to them.
- How can the stakeholder approach be promoted and implemented concretely in a market economy that puts pressure on most firms to maximize profit rather than focusing on the total surplus generated?