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Taking the Pulse of the New Economy
Chief Economists Outlook

Platform for Shaping the Future of the New Economy and Society

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Chief Economists Outlook

This briefing is the outcome of consultations with leading Chief Economists from both the public and private sectors, organized by the World Economic Forum's Platform for Shaping the Future of the New Economy and Society.

It aims to summarize the emerging contours of the current economic environment and identify priorities for focus and action by policy-makers and business leaders in early 2020. The briefing will be issued on a bi-annual basis going forward.

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Backdrop

The new decade opens with a fragile growth outlook,[1] social tensions over the evident polarization of economic outcomes and high levels of uncertainty.

The current challenges are significant (figures 1-4). Yet trust in institutions has eroded and policy-making is becoming increasingly reactive to single issues or brinkmanship, which has made policy action less predictable and dependable. This has been particularly true for trade policy, where recent policy moves by major trading nations have been perceived as highly disruptive. A similar kind of policy uncertainty is springing from rivalries in the technology arena, most recently in the case of 5G.

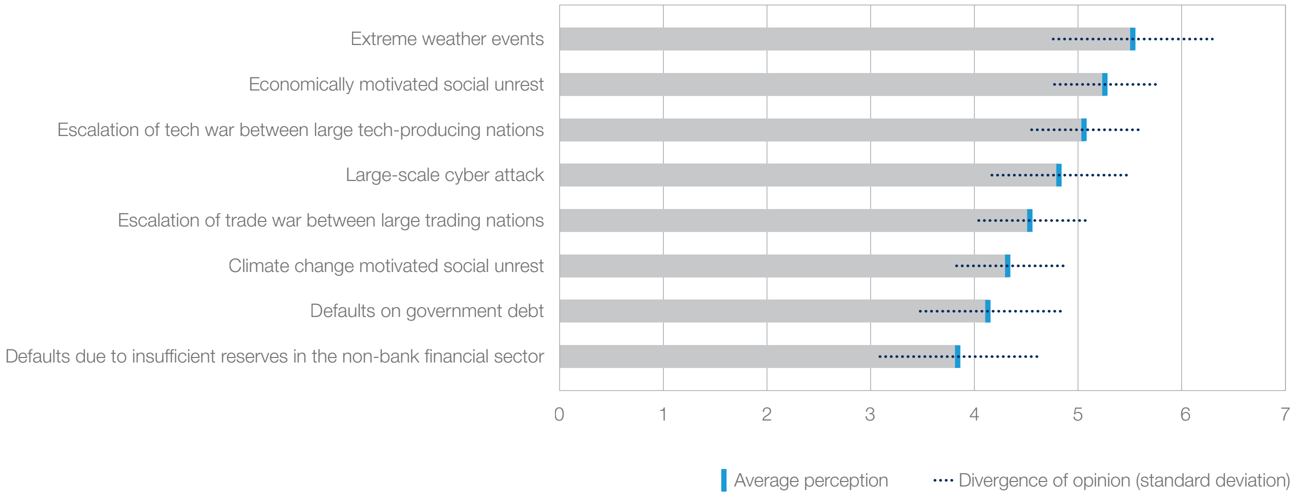
Additionally, traditional policy mechanisms have become less reliable—first and foremost, core elements of monetary and competition policy. Monetary policy tools that traditionally used to smooth over negative shocks or create positive economic momentum have lost much firepower as interest rates in major currency areas remain close to zero. The new dynamics of the digital economy have also left competition authorities with an outdated toolkit.

Structural reforms to enable the transition towards a new economy are revealing delicate trade-offs, at least in the short term, between the digital and green transformations as well as adaptation towards equitable social outcomes amidst changing demographics. For example, in 2018/19 France saw a wave of social unrest in the wake of an attempt to cut carbon emissions by increasing fuel taxes and after a move to reform the national pension system. The transition as it is currently happening is proving to be costly for low-income groups and risks feeding the trend of growing income inequality. Two potential shocks to the economy in 2020 include extreme weather events and imposition of new trade barriers, both of which could further affect low-income groups disproportionately, as low-income households will face more challenges recovering from extreme weather events and new trade barriers will increase prices for consumers.

At the global level, convergence of per capita incomes has been stagnating. Digital leapfrog models have not yet delivered the same growth results for low-income countries as the manufacturing-led development model of the 1990s and 2000s. In addition, a new kind of middle-income trap seems to be on the horizon for some large emerging markets. While the digital revolution initially opened many opportunities for micro-entrepreneurship on digital platforms in emerging markets and thereby provided a way out of poverty, there is a perception that the winner-take-all dynamics which were simultaneously unleashed might potentially block the pathways to opportunity for the next generation. ■

Figure 1

In your opinion, how likely are the following events to happen within the next 12 months? (1 = extremely unlikely; 7 = extremely likely)

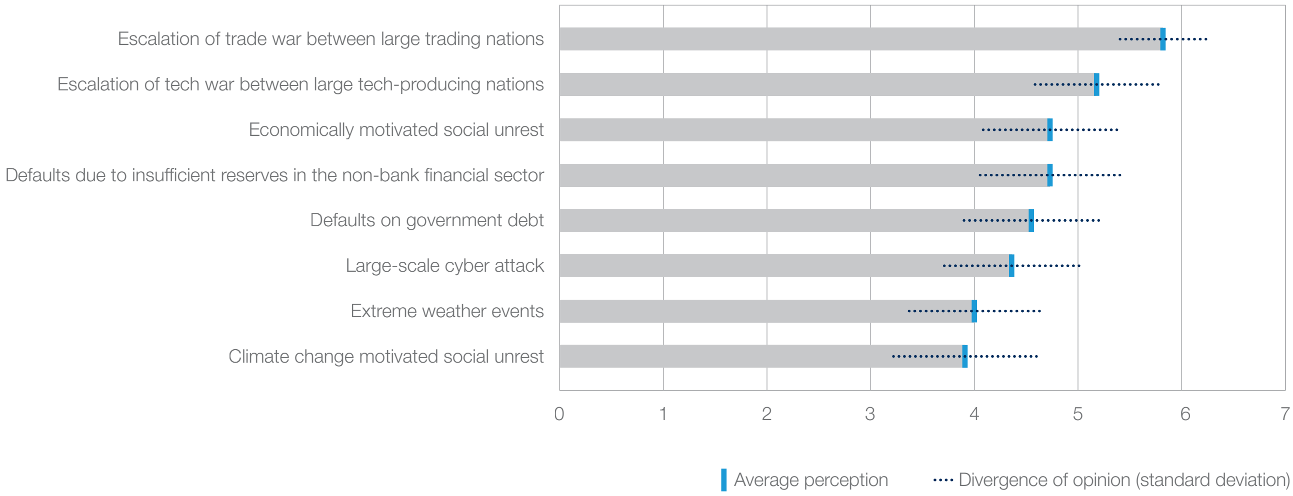


Sources

Chief Economists Survey, World Economic Forum, 2020.

Figure 2

In your opinion, how big would the impact on global economic output be for each of the following events? (1 = negligible; 7 = global economic crisis)

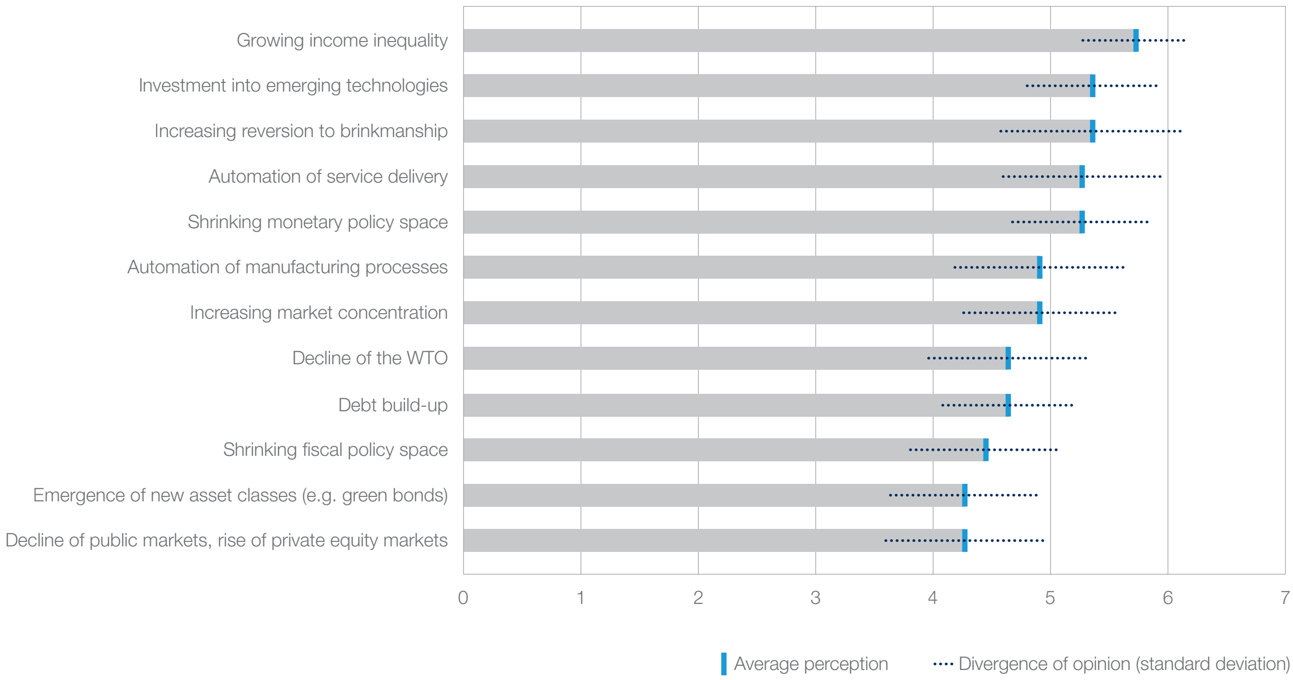


Sources

Chief Economists Survey, World Economic Forum, 2020.

Figure 3

How strongly do you expect the following trends to be shaping the global economy in the next 12 months? (1 = not strong at all; 7 = extremely strongly)

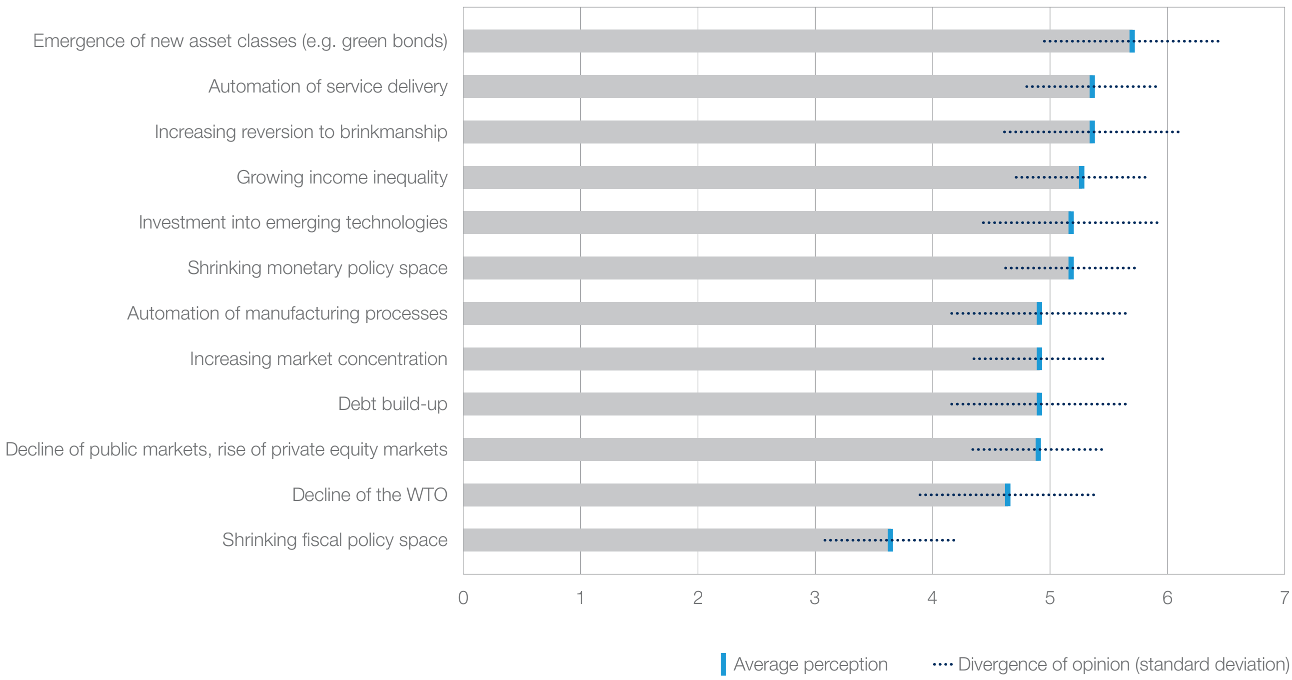


Sources

Chief Economists Survey, World Economic Forum, 2020.

Figure 4

Are these trends currently slowing down or accelerating?
(1 = strongly slowing down; 7 = strongly accelerating)



Sources

Chief Economists Survey, World Economic Forum, 2020.

Silver Linings

There are signs of policy agility and business reform that may lead to a different, better kind of economic growth, but this momentum needs strengthening.

Tax

Global coordination on new, **fairer corporate tax structures** seems within reach thanks to a multi-year effort led by the OECD to reign in tax base erosion and profit shifting (BEPS). Agreement in this space should contribute to greater fiscal space for countries as leakages from profit-shifting are reduced. The effort also presents an opportunity to develop new mechanisms to ensure that digital companies contribute a fair share. This in turn should give more flexibility to governments to facilitate the transition to the new economy by expanding their spending on workforce skilling and stronger social safety nets among other urgent spending needs.

Macro-prudential

There is further a perception that **macro-prudential frameworks** have improved in the aftermath of the global financial crisis and have made the financial sector more resilient to shocks. Reforms under the Basel III agreement have increased banks' capital requirements (with more stringent requirements for the largest banks) and introduced new liquidity requirements as well as an upper limit on leverage and countercyclical capital buffers. One aspect to keep in mind, however, is that the new framework has not yet been tested by a new crisis and that financial activity has been migrating to the non-bank financial sector where oversight is much weaker.

Trade

Progress has also been made by China and the United States in **softening trade tensions**, with a Phase One Deal reached on 13 December 2019. The agreement includes provisions on more product and service purchases by China from the United States, a cut in half of tariffs on approximately $120 billion of Chinese exports to the United States, as well as advancements on intellectual property rights, agriculture, financial services and currency.[2] This can be expected to stabilize trade flows for both countries and have the positive effect of reducing uncertainty globally. The agreement could be the basis for a rebound in global trade and manufacturing production.

Innovation

There is new interest and action around new approaches to **innovation and industrial policy.** The European Commission, for example, is starting to take a bigger role in shaping research and innovation through a "mission driven" approach that sets out to tackle specific societal challenges.[3] With the new needs of the decade ahead, policy-makers globally may have more room for incentivizing the direction of growth, emphasizing aspects such as green infrastructure, education and care.

ESG

Considerable momentum is building for **business action on environmental and social issues going into the new decade.** The number of efforts to make social and environmental business impacts measurable and businesses accountable had taken off in recent years as environmental, social and governance (ESG) standards and metrics proliferated. The Business Roundtable Declaration, signed by 181 US CEOs, resonated widely for helping move forward the debate on the responsibility of business to its shareholders vs all stakeholders, including employees, customers and the communities in which companies are embedded.[4] Better quantification of associated financial risks of climate change have led central banks to stress-test banks on climate risks and brought investors on board in insisting on environmental performance.

Human capital

Environmental impact measures are currently clearer and more globally accepted than those for social impact where better alignment must be found. There is growing consensus on two aspects of social impact action: diversity and training. Forward-thinking business leaders are advancing **diversity and inclusion strategies** for their workplaces, including gender parity (both on leadership positions and pay), as well as inclusion of individuals from minority groups. Business leaders are also starting to develop systematic strategies for **reskilling and upskilling** their workforces in light of rapidly changing employment structures, new technologies and emerging skills needs.

Priorities for Action

Close policy-maker and business leader attention in 2020 will be needed for rethinking fiscal and competition policy as well as the implementation of a fair green and digital transition.

Focus on fiscal policy

A new balance between **monetary and fiscal policy** will have to be found to compensate for the depletion of both traditional monetary policy tools and quantitative easing. New fiscal flexibility will be needed instead in order to jump-start growth and to facilitate the transition to the new economy on a number of fronts, including support of workforce reskilling and upskilling efforts, updated social safety nets and green investments. While fiscal space exists in advanced economies, it is to some extent conditional on accommodative monetary policy going forward; in the case of the United States, fiscal space might be shrinking as demand for US government debt has been waning. Balanced-budget use of the available space should be leveraged more by European economies and the United States to support growth. The Chinese government is moving in this direction with plans for fiscal stimulus in 2020, including tax cuts and increased local government spending, which should be important factors in sustaining global growth and further transition the Chinese economy from being investment-driven to consumption-driven. The amount of fiscal space available for future government spending will also depend on governments' ability to tax, with the digital transformation making tax collection both harder (as intangibles are becoming more important) and easier (as more transactions become traceable).

Upgrade competition policy

The trend towards higher market concentration across many sectors will require rapid updates of **competition frameworks** as a core tool to sustain vibrant markets and safeguard the opportunity for all to participate. In particular, new challenges have arisen in the technology sector as well as in traditional sectors where large data holdings have become a factor of competitive advantage. While the focus of competition policy has traditionally been on price hikes as an indicator for abuse of market power, this benchmark is losing validity in the current setting where large data holdings have become a guarantor of market power and their rapid accumulation a core business objective. The new dynamic favours the pursuit of fast growth over profits and incentivizes companies to integrate rapidly across business lines in order to gain control of critical infrastructure and data flows.[5] Rather than price hikes, anti-competitive behaviour in these types of settings manifests in predatory pricing to speed growth, and in direct exclusion of competitors from critical infrastructure—neither of which are sufficiently recognized in the current doctrine. Competition policy thus needs to be upgraded rapidly. The EU has been at the forefront in exploring new approaches to tackling the competition challenges of the digital economy.

Rethink social safety nets

Social safety nets, too, are in urgent need of updating, having come under pressure from adverse demographics in high-income countries and emerging economies including China, as well as from extremely low or negative interest-rate environments. They will also need to reflect the fact that work volatility in the digital economy can be expected to increase, with more frequent job transitions for workers that will need to be supported and actively facilitated by both policy and business action. A comprehensive rethink will be needed both in terms of costs as well as the type, agility and format of new safety nets.

Facilitate the green transition

Another focal point for careful policy-making will have to be the **transition to a greener economy**. There is much agreement globally that a green transition needs to happen—yet it will have significant distributional implications that could impact its pacing despite the urgency. The transition will necessarily involve greater constraints to consumption and resulting costs to both consumers and producers of the goods in question must not be swept aside but need to be acknowledged and addressed. While the transition to a greener economy is full of opportunities, complementary policy action will matter enormously for benefits to be widely felt and losses to be mitigated.

Accelerate ESG implementation

Business leaders in 2020 will need to stay ahead of **environmental and social impact** measurement and accountability for activities that are at the core of their business models. Despite recent momentum on this front, some caveats apply: (i) disclosure on ESG performance for the moment remains unsystematic and limited due to the fact that reporting is costly, voluntary and lacks a standardized set of metrics;[6] (ii) even when leadership ambitions on environmental and social impact are big, middle managers still lack the tools and sometimes awareness for lasting implementation; (iii) an accelerating trend that will also need to be watched in this context is the shift of financial activities from public to private markets, implying less transparency and oversight, including on impact that would otherwise fall under the growing remit of ESG accountability.

Shape the digital transition

Many business leaders are also still too hesitant to address the **darker sides of their digital** or newly digitalized business models. Gaps around securing personal data, the spread of misinformation, safeguards against cybercrime and adequate measures to deal with algorithmic biases and big-data enabled discrimination are still large. The latter have the potential to further exacerbate current trends of polarization by discriminating against individuals with certain characteristics—for example, when it comes to having access to financial and insurance services, made worse by a lack of accountability and transparency of the factors that determine the outcome of an algorithmic decision-making process.

While there is a range of challenges on the horizon at the dawn of the new decade, there are also promising pathways to greener, more inclusive economies. This briefing presents a snapshot of the present moment based on the views of leading chief economists in the public and the private sector. How the future unfolds depends on the actions of business leaders, policy-makers and societal trends. There is a unique window of opportunity today to mobilize human collaboration and technology to move toward more equitable outcomes in the new decade.

Notes and References

1 IMF, 2019a.

2 Reuters, 2019.

3 European Commission, 2019.

4 Business Roundtable, 2019.

5 Khan, 2017.

6 IMF, 2019b.

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