GROUP OF TWENTY

# G-20 SURVEILLANCE NOTE

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Prepared by Staff of the

INTERNATIONAL MONETARY FUND*

*Does not necessarily reflect the views of the IMF Executive Board.

# EXECUTIVE SUMMARY

**The global expansion continues, but it has become more uneven and there are signs that growth may be moderating.** The October World Economic Outlook (WEO) projected global growth to continue at a high level through 2019. However, for many G-20 economies growth was expected to weaken, reflecting the maturing business cycle in most advanced economies, the expected unwinding of the fiscal stimulus in the *United States*, and the continuing rebalancing of the Chinese economy. Recent data suggests that this deceleration could be faster than expected under the baseline, as financial conditions have tightened especially in emerging markets and trade tensions have increased, prompting policy easing in some countries (e.g., *China*). Many emerging markets have reacted to rising external pressures by deploying a variety of measures, including policy rate hikes, foreign exchange interventions, and import tariffs. Core inflation pressures remain low across most of the G-20 despite narrowing output gaps.

**Downside risks have risen.** Financial conditions in advanced economies are still accommodative but could worsen abruptly—for example, due to a more drastic drop in equity markets or faster-than-expected U.S. monetary policy tightening should procyclical fiscal policy lead to a surprise increase in inflation. This would likely add to the pressure on emerging markets and highly leveraged advanced economies (e.g., *Italy*), as would a worsening of risk sentiment. A further escalation of trade tensions could dent confidence and trigger more substantial output losses, as could uncertainty around a Brexit deal in Europe. The lack of policy space would amplify the impact of these risks.

**Progress toward the G-20 goals of more balanced, sustainable, and inclusive growth remains slow.*** External imbalances could further increase given the combination of U.S. fiscal expansion and limited fiscal and demand-enhancing structural policies in some advanced excess surplus economies (e.g., *Germany*), raising the possibility of a disorderly adjustment later. Renewed policy loosening in *China* could slow domestic rebalancing. At the same time, financial vulnerabilities have increased across the G-20, with high and rising debt among many non-financial corporates, households and sovereigns. Slow productivity growth—linked, in part, to population aging—continues to dim medium-term prospects. Progress toward more inclusive growth has been slow, which could undermine support for necessary structural reforms.

**Working together, policymakers can contain risks, strengthen the global expansion over the medium term, and ensure the benefits of growth are widely shared.** This requires decisive action to:

- *Reduce vulnerabilities.* High-debt sovereigns need fiscal consolidation to rebuild buffers and procyclical expansions should be reversed. Monetary normalization in advanced economies should continue in a well-communicated, gradual, and data-driven manner. Emerging economies with well-anchored inflation targets should rely on exchange rate flexibility to mitigate external pressures and avoid tariffs or other policies that may weaken market confidence. Where pressures threaten to be disruptive, capital flow management measures could have a role to play as part of a broader policy package addressing vulnerabilities and strengthening policy frameworks.
- *Renew multilateral cooperation.* There is an urgent need to de-escalate trade tensions, reverse recent tariff increases, and to modernize the global trading system, including by reducing barriers to trade in services. Cooperation is also necessary to bring down external imbalances, avoid rollback of post-crisis advances in financial sector regulation, coordinate support for low-income countries, and to address other global challenges such as climate risks, and international taxation.
- *Address financial risks.* Risks from highly leveraged non-financial sector balance sheets, deteriorating credit quality, and high exposure to foreign currency or foreign-owned debt in several emerging economies call for action, including the proactive use of micro- and macroprudential tools.
- *Boost balanced, sustainable, and inclusive growth.* Avoiding procyclical fiscal policies in deficit countries, using fiscal space to lift potential output in excess surplus countries, and policies to reduce excess saving will help narrow excess external imbalances and keep domestic vulnerabilities in check. Jointly undertaking structural reforms would add 4 percent to global real GDP in the long term. Depending on country needs, investment in human capital—for example, through education—in combination with strong social safety nets, appropriate fiscal redistribution and access to health care are key to preparing for the future of work and ensuring that the benefits of growth are widely shared.

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* G-20 Report on Strong, Sustainable, Balanced, and Inclusive Growth, 2018.

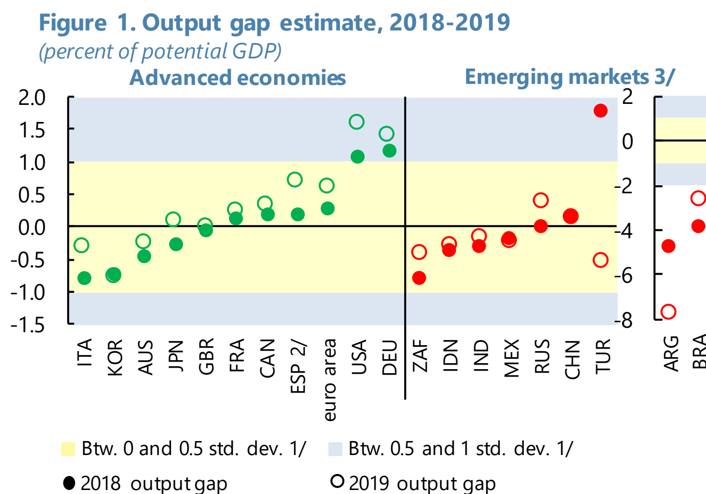
Prepared by a team led by Helge Berger, including Adil Mohommad, Philipp Engler, Eric Bang, Jung Sung Eun, and Ilse Peirtsegaele.

# RECENT DEVELOPMENTS, OUTLOOK, AND RISKS

*The October WEO projected continuing high global growth through 2018 and 2019, but the expansion has become more uneven and there are indications that growth may be moderating. In many G-20 economies growth was expected to slow, reflecting the unwinding of cyclical factors in advanced economies as well as headwinds from trade-policy disputes and tighter financial conditions especially in emerging markets. However, recent data have surprised on the downside, suggesting the deceleration could be faster than expected under the baseline. A further escalation of trade tensions and a more rapid tightening of financial conditions remain key downside risks given limited policy space in many countries. The medium-term outlook remains for lower growth particularly in advanced economies. At the same time, the IMF's 2018 G20 Report on "Strong, Sustainable, Balanced, and Inclusive Growth" suggests there has been little progress toward the broader set of G-20 goals since 2017. These shortfalls add further downside risks and could weaken the support for necessary structural reforms.*

## A. STRONG GROWTH FOR NOW

**1. The October WEO predicted global growth to plateau at a high level, with the growth momentum slowing in many G-20 economies.** World growth was expected to continue at 3.7 percent in 2018 and 2019, 0.2 percentage points below the July forecast but the same as last year when it reached the highest level since the post-crisis rebound. Unemployment rates are low and output gaps have narrowed considerably in most G-20 countries (Figure 1). However, the share of economies expected to grow faster than the previous year fell from about three quarters of global GDP in 2017 to less than half of global GDP in 2018 (in purchasing-power-parity terms).




Sources: IMF, *World Economic Outlook* October 2018; and IMF staff calculations.
1/ Standard deviations are calculated from 1990 to 2016, excluding outliers above 99% and below 1% for each income group.
2/ ESP is a permanent invitee.
3/ For SAU, output gap estimates for 2018 and 2019 are not available.

**2. Recent data have surprised on the downside, suggesting the deceleration could be faster than expected under the baseline**, both in advanced and emerging market economies:

- *Growth is slowing in most advanced economies* (Figure 2). Growth decelerated faster than expected under the baseline in the *euro area*—especially in *Italy* and in *Germany*, which saw negative GDP growth in Q3—and in *Japan,* reflecting a combination of idiosyncratic factors along with the fading momentum from very strong trade and investment growth in the second half of 2017. Buoyed by fiscal stimulus, growth in the *United States* has remained strong even as the Federal Reserve

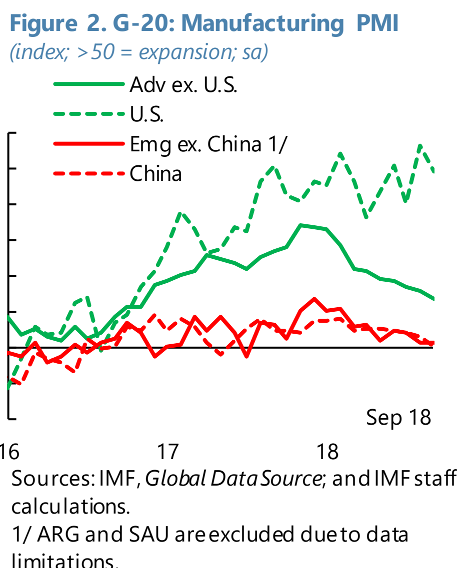



**Figure 2. G-20: Manufacturing PMI**
*(index; >50 = expansion; sa)*

Sources: IMF, *Global Data Source*; and IMF staff calculations.
1/ ARG and SAU are excluded due to data limitations.

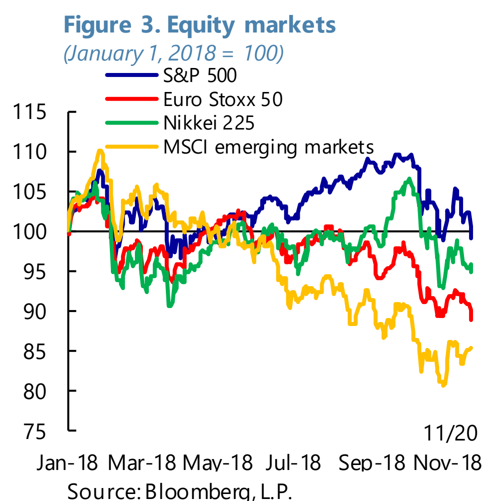



**Figure 3. Equity markets**
*(January 1, 2018 = 100)*

Source: Bloomberg, L.P.

continues to raise interest rates. However, monetary normalization in the *United States*, the phasing out of unconventional monetary support in the *euro area*, and a drop in equity markets (Figure 3) have contributed to making financial conditions less accommodative across G-20 advanced economies. At the same time, weakening sentiment indicators in many countries point to rising uneasiness among investors as uncertainty about the future of the multilateral trade system intensifies.

- *Emerging economies are facing external and financial pressures*. Many have seen a significant tightening of financial conditions linked to accelerating capital outflows and U.S. dollar strength (Figure 4), with the strongest impact felt in the most vulnerable countries (e.g., *Argentina, Turkey*). In addition, there are signs that the ongoing trade tensions have begun to leave a mark—for example, while *China* continues on its path to lower, more sustainable growth rates, high frequency indicators suggest that weaker-than-expected private sector activity has coincided with the intensification of the trade dispute with the *United States.*

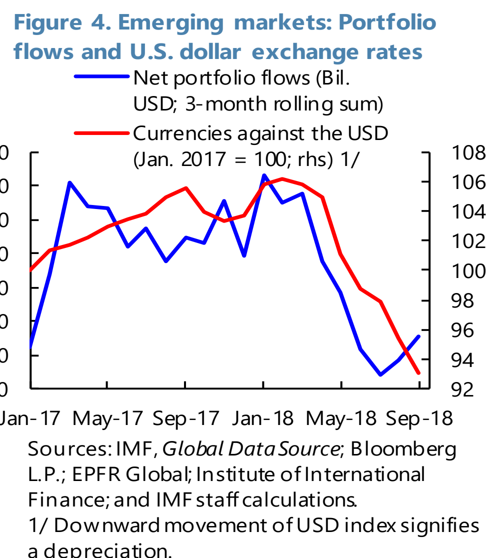


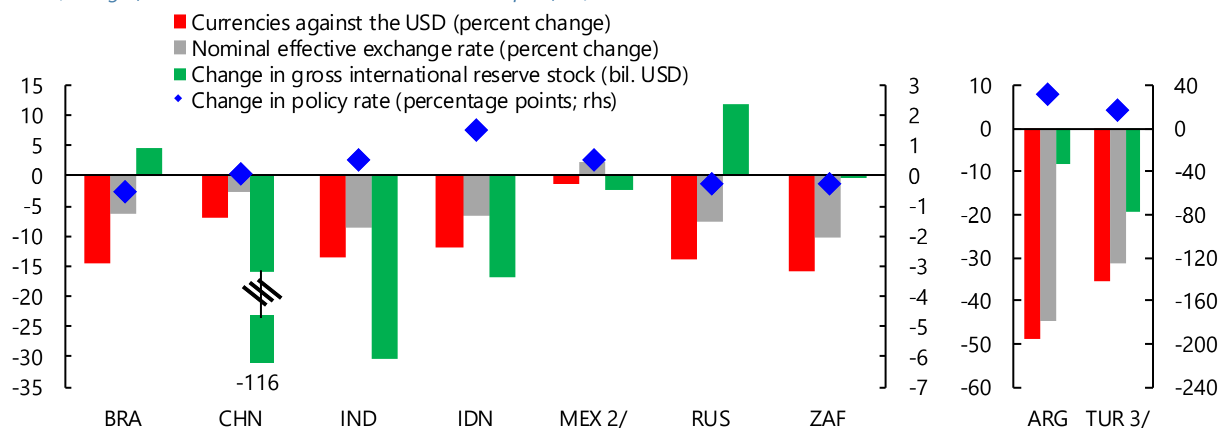

**Figure 4. Emerging markets: Portfolio flows and U.S. dollar exchange rates**

Sources: IMF, *Global Data Source*; Bloomberg L.P.; EPFR Global; Institute of International Finance; and IMF staff calculations.
1/ Downward movement of USD index signifies a depreciation.

**3. Emerging market policymakers have taken steps to counter the mounting pressures** (Figure 5). *China* has moved to ease monetary conditions, support credit supply, and strengthen public investment, which could undermine progress on deleveraging, while the renminbi has depreciated both vis-à-vis the U.S. dollar and, by less, in effective terms. Other G-20 members have raised policy rates—most dramatically *Turkey* and *Argentina*. Several have used foreign exchange reserves to mitigate currency depreciation or have introduced import tariffs to counter current account pressures, with a number of countries deploying a mix of measures (e.g., *India, Indonesia*). *Argentina* has received IMF support for its economic reform program.

**Figure 5. G-20 emerging markets**

*(change from Jan. to Oct. 2018, unless otherwise specified) 1/*



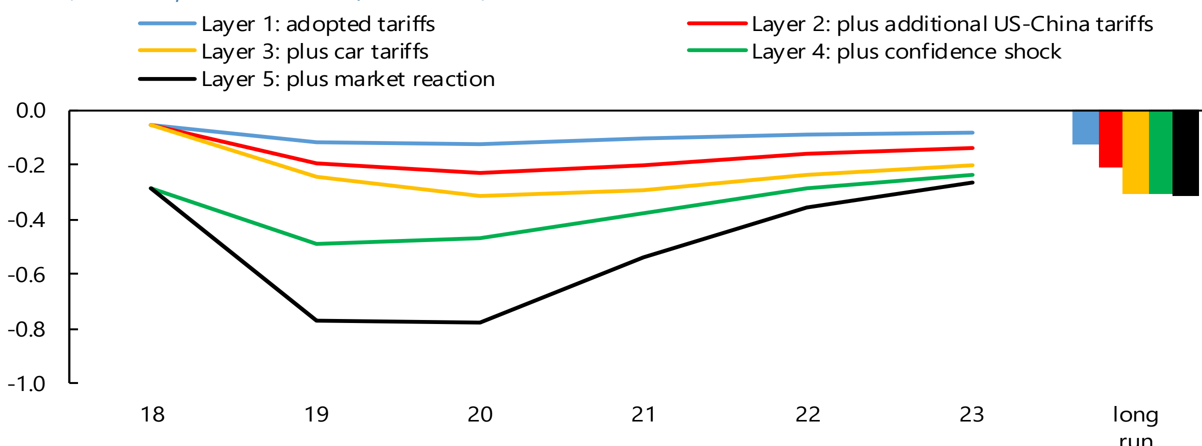

Sources: IMF, *Global Data Source*; Bloomberg L.P.; and IMF staff calculations.
1/ Downward movement of USD and NEER signify a depreciation.
2/ Change in official reserve assets of the central bank from Jan. to Sep. 2018.
3/ Change in the central bank's reserves from Jan. to Aug. 2018.

## B. DOWNSIDE RISKS TO THE OUTLOOK HAVE INCREASED

**4. Trade tensions could well escalate, and Brexit risks remain acute.**

- *Trade tensions could rise.* While the direct output costs of implemented and expected tariffs continue to add up—especially for the *United States* and *China*—"worst-case" scenarios point to the importance of possible secondary confidence and financial market effects. Uncertainty is bound to increase and tighten the credit conditions firms face if trade tensions escalate further owing, for example, to new tariffs and counter-tariffs on automobiles and parts between the *United States* and trading partners outside of the recently negotiated USMCA. Such a development would reduce investment and growth. Staff simulation suggests that the resulting short-term losses could lower global GDP by about ¾ percent (Figure 6). Longer-term losses—including the cost and productivity losses associated with the readjustment of existing global value chains (GVCs)—are estimated to be lower as percent of annual global GDP as confidence and financial market reactions dissipate, but they will be permanent and accumulate over time.

**Figure 6. Simulations: Global GDP impact of trade tensions**
*(real GDP; percent deviation from control)*



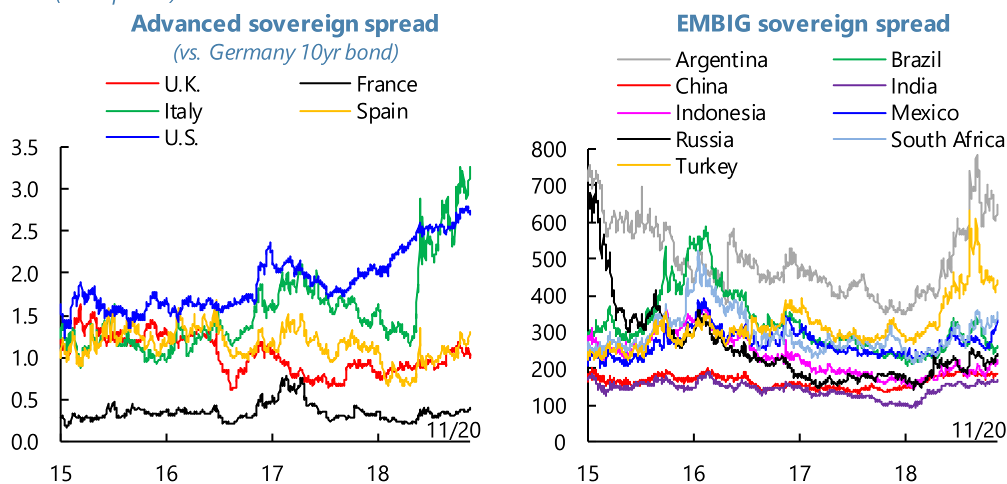

Source: IMF staff estimates.
Note: The Global Integrated Monetary and Fiscal Model scenario incorporates: (i) the already implemented US 10 percent tariffs on steel, 25 percent tariff on aluminum and on US$50 billion imports from China, and the additional 10 percent import tariffs on US$200 billion of US imports from China that subsequently increases to 25 percent—all trading partners are assumed to respond and levy tariffs on an equivalent amount of US exports, except in the case of the 10 percent tariff on $200 billion in Chinese imports; (ii) a 25 percent tariff on a further $267 billion of imports from China and a response by China such that all imports from the U.S. also face a 25 percent tariff; (iii) a 25 percent increase in tariffs on US imports of cars and car parts from all countries except Canada and Mexico, and retaliation by the affected countries on the same amount of US exports; (iv) an impact of trade tensions on confidence and firms' investment plans; and (v) a tightening of financial conditions associated with trade tensions. For details, see IMF, October 2018, *World Economic Outlook*, Chapter 1 Scenario Box.

- *Brexit concerns persist.* In Europe, failure to navigate a smooth *United Kingdom* exit from the *European Union* would entail significant economic costs for the U.K. economy and to a lesser extent for the *European Union* economies.

5. **Financial conditions could tighten rapidly and expose high financial vulnerabilities.** One possible trigger might be sharply rising U.S. policy rates as procyclical fiscal expansion fuels an increase in inflation. Another possibility is a rapid shift in market sentiment—caused, for example, by escalating trade or geopolitical tensions—that would accelerate portfolio shifts away from risky assets, including in emerging markets. Elevated financial vulnerabilities are present in high levels of household (*Canada*, *United Kingdom*) and corporate (*China*) debt, declining private sector credit quality (*Turkey*), and high emerging market exposure to capital flow reversals and currency mismatches. These vulnerabilities have the potential to amplify significantly the economic costs of adverse shocks.

6. **Sovereign risk concerns could rise.** Sovereign debt is above pre-crisis levels in many G20 advanced economies and some emerging economies. Sovereign spreads have increased in some countries (Figure 7), including in *Italy*, where concerns over high public debt, and policy slippages could trigger further adverse market reactions. Moreover, remaining gaps in the *euro area* banking union and insufficient risk reduction in the banking sector imply that the sovereign-bank nexus could re-emerge, with higher sovereign spreads spilling over to banks.

**Figure 7. Selected G-20 sovereign spreads**
*(basis points)*

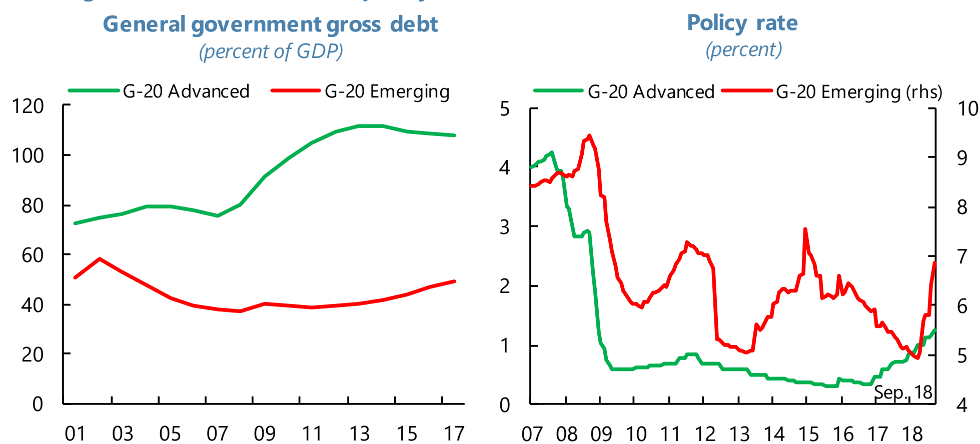



Source: Bloomberg, L.P.

**7. At the same time, constrained policy space threatens policymakers' ability to contain these risks.**

- *Higher public debt means less fiscal space*. Across the G-20, fiscal policy space narrowed as sovereign debt levels increased in the wake of the crisis (Figure 8). According to the IMF's most recent assessment, just *Australia*, *Germany*, and *Korea* have "substantial" fiscal space to counter materializing downside risks, nine G-20 members have "some" fiscal space, while fiscal space in the remaining G-20 economies is currently assessed as only "limited."[1]
- *Monetary policy has little room for maneuver*. In many advanced economies, the still very low level of policy rates limits the room for conventional monetary policy support. In addition, in many G-20 economies, estimates of real natural (or neutral) rates have declined since the crisis, further limiting the available conventional monetary policy space.

**Figure 8. Public debt and policy rate**




Sources: Bloomberg, L.P.; Haver Analytics; IMF, *Global Data Source*; IMF, *World Economic Outlook* October 2018; and IMF staff calculations.

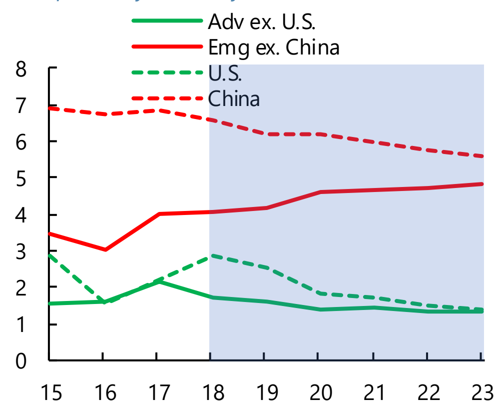
[1] IMF, 2018, Assessing Fiscal Space: An Update and Stocktaking.

## C. SUSTAINABLE, BALANCED, AND INCLUSIVE GROWTH IS STILL ELUSIVE[2]

**8. Even under the baseline, the current levels of strong growth will be difficult to sustain.**

- *Slow productivity growth still holds back G-20 economies*. This is particularly true for advanced economies. G-20 emerging economies are expected to see broadly stable economic growth of around 5 percent over the medium term, as the transition to lower, more sustainable growth in *China* is balanced by higher growth elsewhere (e.g., *India*). In contrast, G-20 advanced economies including the *United States*, are projected to see their average GDP growth rates decline from about 2.2 percent in 2018 to about 1.4 percent in 2023 (Figure 9). The main reasons for this slowdown are the expected weakening of cyclical forces and the low rate of underlying productivity growth linked to headwinds from aging, a slowdown in structural reforms, and the waning influence of past innovation—such as information and communication technologies and the cross-border integration of production processes into GVCs.

**Figure 9. G-20: Real GDP**
*(percent; year-over-year)*




Sources: IMF, *World Economic Outlook* October 2018; and IMF staff calculations.

- *A disruption of global trade would reduce productivity further*. GVC disruption would reduce productivity in advanced and emerging market economies alike, slow the international diffusion of technology, and hurt consumers everywhere through higher prices (see Figure 6).

**9. Global imbalances are poised to increase, raising the possibility of a disorderly adjustment over the medium term.** While excess current account imbalances remained broadly unchanged in 2017, they are set to widen due to a combination of procyclical fiscal expansion in the *United States*, an excess deficit country, and limited growth and demand-enhancing policies in excess surplus countries such as *Germany*. *China's* excess surplus has narrowed significantly, and recent easing measures appear consistent with rebalancing toward more consumption-led growth—for example, by pairing measures aimed at boosting finances for local government and SMEs with tax measures to boost consumption. Failure to lower global imbalances now could lead to sharp and disruptive currency and asset price movements in indebted countries later. Such developments would diminish global growth, also harming the surplus economies.[3]

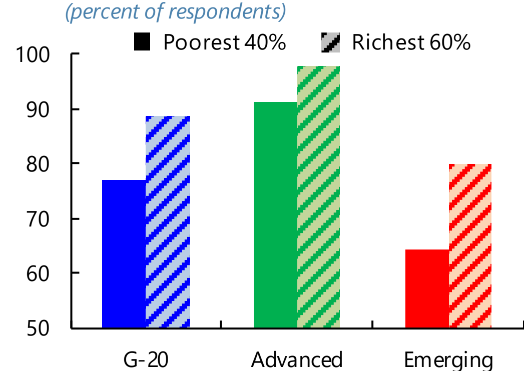
[2] An in-depth discussion of all dimensions of the G-20 goal of strong, sustainable, balanced, and inclusive growth (SSBIG) is provided in IMF's 2018 SSBIG Report.

[3] IMF, 2018, External Sector Report.

**10. Achieving more inclusive growth remains challenging.** Inclusion is important to make growth sustainable, maintain support for reforms, and preserve economic and political stability.

- *In many G-20 economies, income and opportunities are distributed unequally*. After 1990, inequality as measured by the Gini coefficient rose across most G-20 advanced and many emerging economies, and it remains high even in those emerging markets where it has fallen. The trend of generally rising inequality halted but did not reverse itself after the financial crisis. Income gains are not being shared equally between high-income and low-income households—for example, in 2012, on average across the G-20, households in the top decile of the income distribution earned about twelve times the income of the bottom decile. Persistent income inequalities both reflect and reinforce uneven access to economic opportunities, including education, healthcare, and financial services (Figure 10).

**Figure 10. Adults with financial institution account, by income level (2017)**
*(percent of respondents)*




Sources: World Bank, FINDEX; IMF, *World Economic Outlook* October 2018; and IMF staff calculations.

- *Technological progress could make matters worse down the road*. New technologies such as automation hold the promise of raising productivity and income, but they could also drive down demand for low-skilled work and increase skill premia. The advance of the "gig economy" may not provide the same access to health and pension benefits as more traditional forms of employment unless policy frameworks such as social spending programs and their financing adapt to the new context.[4]

[4] IMF, 2018, G-20 Note: Future of Work, Measurement, and Policy Challenges.

# POLICIES

*Working together, policymakers can contain risks and ensure that the global expansion continues to the benefit of all. To reduce vulnerabilities and adjust macroeconomic policies to the maturing economic cycle, fiscal buffers need to be rebuilt while monetary normalization should continue gradually in line with country-specific conditions. Where possible, emerging markets should allow exchange rates to buffer external shocks while pursuing economic policies that support financial market confidence. Multilateral action is urgently required to de-escalate trade tensions and improve the multilateral trading system. Micro- and macroprudential tools should be deployed to reduce financial sector risks. And more efforts are needed to make growth more sustainable, balanced, and inclusive, while stepping up support of low-income developing countries.*

## A. CONTAIN RISKS AND REDUCE VULNERABILITIES

**11. For most G-20 economies, the time for meaningful fiscal consolidation is now.** With growth still high in many economies, the window of opportunity to lower public debt is still open. Faster fiscal consolidation will help create fiscal space for automatic stabilizers and discretionary fiscal policy should cyclical growth weaken further, or downside risks materialize. By lowering debt levels, this strategy will also lower interest rates going forward, thereby reducing debt-servicing costs, crowding in private investment, and boosting consumption.

- *Advanced economies*: While many advanced G-20 economies are planning fiscal consolidation, in some cases a more ambitious effort is needed.[5] This is particularly critical in *Italy*, where debt is already high, and growth exceeds potential. The procyclical fiscal expansion in the *United States* should be reversed, while *Spain* should resume structural fiscal consolidation.
- *Emerging economies*: With a few exceptions, emerging market fiscal policies are already geared toward consolidation. However, additional efforts are needed—for example, in *India, South Africa,* and *Turkey*. If external pressures intensify further and downside risks to growth materialize, those with available fiscal space should use it to avoid a hard landing.

**12. Monetary policy in advanced economies should continue to normalize in a well-communicated and gradual fashion, in line with evolving country conditions.** This applies to the Federal Reserve in the *United States,* but also for the European Central Bank as it continues to exit from unconventional monetary support. Experience suggests that while rising interest rates in advanced economies will inevitably lead to some retraction in capital flows to emerging markets, any negative spillovers on emerging markets are likely to be lower if the underlying cause of rising advanced economy interest rates is higher advanced economy growth.[6]

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[5] IMF 2018 SSBIG Report.

[6] Indeed, as the IMF 2014 Spillover Report shows, real shocks associated with higher interest rates—reflecting stronger than expected growth in advanced economies—produce smaller increases in emerging market yields and output tends to rise (and not fall) in the affected economies.

**13. In the *euro area*, faster progress towards completing the institutional architecture would go a long way towards containing future risks.** The euro area crisis exposed shortcomings in the functioning of the currency union, and further integration would make the *euro area* more resilient to shocks. This entails completing the banking union—including through a common deposit insurance scheme and a common fiscal backstop to the Single Resolution Fund—to help weaken the bank-sovereign nexus; deepening capital market integration to improve private cross-border risk sharing; and greater fiscal risk sharing (e.g., through a central fiscal capacity) along with a reform of the fiscal rules.[7]

**14. In emerging market economies, policies should be responsive to changing external conditions**. In countries with flexible exchange rates and strong inflation targeting regimes, exchange rate flexibility will help offset external shocks. Simulations suggest that raising interest rates to avoid depreciation in response to an abrupt tightening in U.S. interest rates could result in four times greater output loss relative to letting exchange rates adjust.[8] However, policy rates should be raised if high pass-through from depreciation to inflation threatens to dislodge inflation expectations, and foreign exchange intervention could be used to avoid disorderly market conditions by countries with adequate reserves. Countries should avoid ad hoc measures such as import taxes that hurt trade and might dent confidence.

**15. Where capital flows threaten to turn disruptive, additional action may be warranted**. Capital flows carry significant benefits to recipient countries by financing investment and facilitating consumption smoothing as well as the diversification of risks. But capital flows can reverse quickly, putting macroeconomic and financial stability at risk. In crisis or near-crisis situations, capital flow management measures may be used, provided they do not substitute for warranted macroeconomic adjustment and are part of the broader policy package.[9] Reforms to improve the business climate can help to attract less volatile equity inflows over debt.

## B. RENEW MULTILATERAL COOPERATION

**16. Working together, policymakers can upgrade the global trading system, work to reduce global imbalances, and strengthen the global safety net.** Multilateral action is urgent along multiple frontiers:

- *Fostering trade*. Undoing recently enacted tariffs and stepping up efforts to reduce existing obstacles to trade would boost global trade, investment, and productivity at a critical time. Simulations suggest that reducing trading costs for services by 15 percent—similar to the extent of the decline in trade costs for goods since the mid-1990s—would add about 0.5 percent or 350 billion U.S. dollars to G-20 GDP over the longer term.[10] Services trade liberalization could also make a small, but useful, contribution to reducing global external imbalances.

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[7] IMF, 2018, A Central Fiscal Stabilization Capacity for the Euro Area.

[8] IMF 2018 SSBIG Report.

[9] IMF, 2018, The IMF's Institutional View on Capital Flows in Practice.

[10] IMF 2018 SSBIG Report.

- *Reducing excess external imbalances*. Adjusting fiscal policies in countries with excess current account deficits (e.g., *United States, United Kingdom*) and surpluses—for example, using fiscal space to support growth-enhancing policies (*German*y) and measures to expand labor supply (*Korea*)—will contribute to shrinking global imbalances. In addition, there is a role for structural reforms. For example, in *China*, measures to enhance the social safety net would help lower saving, which would further reduce the country's excess current account surplus.
- *Strengthening the global financial safety net.* Given the rise in financial vulnerabilities in recent years, timely provision of resources to distressed institutions and sovereigns requires better coordination across the global financial safety net. This includes maintaining swap lines between central banks to provide foreign exchange liquidity during times of systemic financial stress. Regional financing agreements and IMF support can complement central banks' efforts to secure external buffers.[11]
- *Addressing common global risks.* Geopolitical tensions—for example, in the Middle East—and climate change—which comes with large economic and social costs, especially for smaller economies—are global risks G-20 leaders can and should tackle through collaborative action. Digital taxation, and achieving greater transparency in low-income country debt, are also areas for fruitful global cooperation.

**17. The G-20 should also step up its support of low-income developing countries (LIDCs).** Many LIDCs have been falling behind their Sustainable Development Goals and debt vulnerabilities have risen across a wide range of LIDCs, reflecting shocks such as falling commodity prices, civil conflict, and looser fiscal policies. At the same time, the increasing importance of non-Paris Club bilateral lenders and plurilateral creditors may complicate debt restructuring, where needed, in the future. G-20 leaders could encourage lenders to consider the benefits of subscribing to the principles for sustainable lending and borrowing which it championed, and to work with existing international fora for creditor information sharing and coordination. Greater transparency on the scale and terms of lending is also needed to avoid further debt surprises and support cooperative solutions to debt workout situations. Lenders can play an important role in this regard, including by sharing information with international financial institutions.

## C. ADDRESS FINANCIAL SECTOR RISKS

**18. Financial sector risks require action.** Progress since the crisis includes more bank capital, fewer non-performing loans in many G-20 countries and higher external reserve levels in most emerging economies. However, pressure is building to roll back recent financial sector reforms at a time when additional progress would be needed—including on insurance regulation, liquidity risk management and derivatives disclosure of investment funds, cross-border bank resolution, and international cooperation on money laundering and terrorism financing, and securing the international financial system against cyber-attacks.

[11] IMF, 2017, Collaboration Between Regional Financing Arrangements and the IMF.

**19. Countries should act to contain risks from high private sector leverage**, with the specific priorities depending on country circumstances.

- *Advanced economies*: Where private sector leverage is high and underwriting standards have deteriorated, policymakers should improve corporate debt restructuring mechanisms, accelerate the recognition of non-performing loans where that is still needed, and raise buffers—for example, through countercyclical capital requirements (implemented recently in the *United Kingdom* and *France*). *Germany* should take steps to increase housing supply, while further strengthening macroprudential toolkits with the addition of debt-to-income and debt-service-to-income ratios.
- *Emerging markets*: In *China*, policymakers should continue to ensure that recent credit-easing policies do not erode gains in deleveraging and de-risking the financial sector. In other emerging market economies, faster and fuller recognition of non-performing assets, along with speedier resolution of bad assets, are important policy priorities. Recent steps by *India* to speed up resolution of bad assets and fuller recognition of weak assets are welcome, but efforts to improve governance and reduce the footprint of public sector banks need acceleration. Countries with high exposures to foreign-owned or foreign currency denominated debt (e.g., *Argentina, Indonesia, Turkey*) need to maintain adequate reserve buffers, develop more liquid domestic bond markets, and use macroprudential tools to mitigate currency mismatch and rollover risks.

## D. BOOST SUSTAINABLE AND INCLUSIVE GROWTH

**20. A strong structural reform effort can help sustain current levels of growth over the medium term.** There is ample scope for action in most countries, including the continued implementation of in-progress growth strategies related to the "2 in 5" G-20 ambition.[12]

- Most advanced economies would benefit from relaxing product market regulations to ease market entry—in particular, for professional services (e.g., France, Germany, Italy, Japan). The regulatory environment for investment could also be improved in many countries. Encouraging innovation requires more spending on research and development. Countries should pursue policies to boost labor supply in the face of aging, including through measures to raise female labor force participation (e.g., Japan, Korea).
- *Further improving allocative efficiency remains key in emerging market economies*—for example by advancing product and labor market reforms, increasing the use of less distortionary taxes, and advancing trade liberalization. Where reforms have stalled, they need to be revitalized (e.g. *South Africa*). In *India*, labor market reforms to encourage more formal-sector employment, along with increasing women's labor force participation, should be key priorities. *China* should continue to rebalance and enhance the role of markets. In light of continuing commodity price volatility, economic diversification remains a priority for exporters (e.g., *Saudi Arabia*).

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[12] In 2013 at the Brisbane Summit, G-20 Leaders formulated the ambition to raise their collective GDP by 2 percent above baseline by 2018.

**21. The long-term benefits of implementing this reform agenda across the G-20 are sizable**. Simulations suggest that joint implementation of this structural reform agenda across G-20 economies would help lift long-term output by about 4 percent over the current WEO baseline, mainly by increasing productivity. The effect of these reforms is boosted by sizable spillovers among G-20 members, including from trade, foreign investment, and the transmission of knowledge across borders.[13]

**22. Further efforts are needed to ensure that the benefits of high growth are widely shared.**

- *Fiscal policies and targeted structural measures are key*, subject to differing country needs, social preferences, and available fiscal space. Progressive fiscal policies can involve both the revenue and the expenditure side, while a well-designed tax-benefit system can reduce distortions. Possible structural measures include action to ensure equal access to quality education and health services or to remove gender barriers, for example in the labor market. Investment in human capital focused on the disadvantaged groups will lift productivity while also ensuring that the resulting higher income is more widely shared.
- *Enhancing financial inclusion is essential as well*. This task will require legal and regulatory frameworks that facilitate information sharing, protect consumers, and provide risk-based supervision. Tax measures can support low-income household saving, for example, in the form of education and retirement accounts.
- *Preparing for the "future of work."* Social insurance systems and safety nets should be adapted to more fragmented work careers and increasing geographical and sectoral mobility expected to be associated with the advancement of new technologies.

[13] IMF 2018 SSBIG Report. The precise structural reform recommendations underlying this simulation represent a consensus assessment by the IMF and OECD.