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WORLD BANK GROUP
INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL FINANCE CORPORATION
INTERNATIONAL DEVELOPMENT ASSOCIATION
INTERNATIONAL CENTRE FOR SETTLEMENT OF INVESTMENT DISPUTES
MULTILATERAL INVESTMENT GUARANTEE AGENCY
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Statement by the Hon. **GORDON BROWN**,
Governor of the Fund for the **UNITED KINGDOM**,
at the Joint Annual Discussion

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Global financial stability depends on individual national governments pursuing strong domestic policies. There are two supremely important tasks which national governments must undertake in order to succeed in the global marketplace - first, building a platform of stability based on openness and transparency in policy making, and second pursuing structural economic reform to promote productivity and employment.

In today's global economy, there is little place for the fine tuning of the past which tried to exploit a supposed long-term trade-off between inflation and unemployment which proved elusive. But equally in today's deregulated liberalised financial markets, governments can no longer try to deliver stability through the application of rigid monetary targets.

The answer to the uncertainty and unpredictability of ever more rapid financial flows is, first , clear long-term policy objectives, second, the certainty and predictability of well-understood procedural rules for monetary and fiscal policy, and, third, an openness that keeps markets properly informed and ensures that objectives and institutions are seen to be credible.

On the continent of Europe, where the search for macro-economic stability is being pursued through monetary union, the same lessons are being learnt with a commitment to monetary stability through the creation of an independent European Central Bank; a commitment to fiscal sustainability through the stability and growth pact of the European Union; and a system of multilateral surveillance within Europe involving commitment to fiscal targets and rigorous peer review.

As I said in my October 1997 statement to the British Parliament, we are committed to making an economic assessment of the case for British membership. The decisive test as to whether and when we will enter will be based on five economic tests we have set out.

## STABILITY IN BRITAIN

In Britiain we have set out clear long term policy objectives:

- the monetary framework promotes price stability through a pre-announced inflation target of 2.5% - a symmetrical target. Inflation outcomes below target are viewed just as seriously as outcomes above target;

- in fiscal policy, we have set two strict fiscal rules to ensure sustainable public finances: the golden rule requires that over the cycle we balance the current budget, and the sustainable investment rule requires that, as we borrow for investment, debt is set at a prudent and stable level.

And we have established well understood procedural rules:

- setting the inflation target, a clear remit for the Monetary Policy Committee of the Bank of England to meet this target and the open letter system; and an equivalent and equally important set of fiscal procedures legally enshrined in the Code for Fiscal Stability.

Openness and transparency keeps markets properly informed and ensures that objectives and institutions are seen to be credible. We have enhanced the transparency and openness of monetary policy in Britain. And the Code for Fiscal Stability requires the Government to conduct fiscal policy in a transparent and responsible way, with key fiscal assumptions independently audited.

Following our own monetary and fiscal reforms I believe that we have now a sound and credible platform for stability for the British economy.

Over the last 10 months inflation has remained within 0.5 percentage points of the Government's target. Headline inflation is down to 1.1 per cent and underlying inflation at 2.1 per cent - around its lowest level for almost 5 years, and inflation is expected to remain close to target.

Short-term interest rates peaked at half their early 1990s level and have fallen from 7½% in October to 5.25% now. Long-term interest rates and mortgage rates are their lowest levels for over 30 years. The 10 year bond differential with Germany has fallen from 1.7 percentage points in April 1997 to around 0.7 percentage points now.

Public borrowing has been reduced by £31 billion over the past two years - a cumulative fiscal tightening of 3¼ per cent of GDP, the largest fiscal tightening since 1981 - and we will continue to lock in that fiscal tightening by keeping the public finances under control, while allowing fiscal policy to continue to support monetary policy in the next stage of the cycle. As a result of our cautious and prudent approach to managing the public finances, we remain on track to meet the fiscal rules while guaranteeing an extra £40 billion for schools and hospitals over the next three years and more than doubling public investment, including in transport and our infrastructure.

So against a difficult world economic background, through early and decisive action on monetary and fiscal policy, both financial markets and the British public see that Britain is delivering - for the first time in this generation - economic stability. We have brought inflation to its target and the fiscal deficit under control. And at the same time, the economy has continued to grow and create jobs throughout this year with the consensus of outside forecasts now predicting growth in 1999 of 1.4 per cent - within the Government's own Budget forecast range of 1 to 1.5 per cent. We will publish new economic forecasts next month in our Pre-Budget Report.

## BRITAIN'S NATIONAL ECONOMIC POTENTIAL

Our task now is to raise our national economic potential.

This year's Pre-Budget Report will focus on the next stage of reforms to labour, capital and product markets needed to exploit the growth potential of Britain.

I believe that the British economy has the potential to reach the upper end of our growth ranges and in a way consistent with meeting our inflation target. But we can only do so if we combine prudence with long-term economic reform and modernisation of our economy. The four conditions for our economy achieving high and stable levels of growth and employment opportunity for all - the modern definition of full employment for the 21st century - are therefore:

- first, a pro-active monetary policy and prudent fiscal policy;

- second, strengthening the programme to move the unemployed from welfare to work;

- third, responsibility and an avoidance of short-termism in pay and wage bargaining across the private and public sectors; and

- fourth, a commitment to what matters for higher productivity - namely, high quality long term investment in science and innovation, new technology and skills.

All of these conditions must be met. And if we can achieve these, then I believe Britain can not only continue steer a course for stability and steady growth, but secure higher prosperity for all.