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Statement by the Hon. Mr. **RODRIGO DE RATO FIGAREDO**,
Governor of the Bank and the Fund for **SPAIN**,
at the Joint Annual Discussion

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I. Salutation

Mr. Chairman,
Mr. President of the World Bank,
Mr. Managing Director of the IMF,
Distinguished Governors,
Ladies and Gentlemen:

II. Overcoming the International Crisis

Description of the crisis

1. A year ago, we met in **circumstances very different** from those prevailing today. We were then at the worst moment of one the most important international crises of recent times. Because of its geographical scope, the number of markets affected, its repercussions on international trade, and its real effects on many countries, it can be considered the most severe crisis of the decade.
2. We then worked intensely **to design institutional mechanisms and propose economic policy approaches** that would enable us to deal with the crisis and alleviate as far as possible its impact on the most vulnerable economies. Today, we can say that our work and the staunch support of all those involved have facilitated the beginning of recovery and more satisfactory growth forecasts for the world economy as a whole.
3. I believe that we can already state **that the worst of that crisis is behind us**, and that the future of the global economy rests on solid foundations for stable growth in the future.

United States

4. On the one hand, we note that the U.S. economy **continues to experience strong growth** and is maintaining a low rate of inflation, all of which is consistent with low unemployment. This favorable performance of the U.S. economy has been one of the key factors of the incipient recovery of the world economy, although I am convinced that in the coming year many more countries will act as engines of recovery.

Japan

5. Mr. Chairman, I believe that we can be **optimistic regarding developments in the Japanese economy**. In the last few months it has shown signs of recovery, brought about by the implementation of expansionary economic policies, together with the introduction of structural reforms specifically focused on the financial sector. Japan should implement fiscal and tax policies aimed at building consumer confidence and promoting growth. The return of Japan to a path of growth is important, not only for Japan, but also for the other Asian economies and for the world economy.

Latin America

6. Let me draw your attention now to Latin America, a region in which the majority of countries have made a great effort to implement orthodox policies and to follow the recommendations of the Bank and the Fund. **Their efforts have not always borne fruit**, and the countries of the region that had made the greatest effort have been unable to isolate themselves from the contagion effect. I would also like to be sure to mention the positive results of the creation of the Contingent Credit Lines and the action of the Brazilian authorities and the international community in solving Brazil's financial crisis. For sustained growth in Latin America, it is necessary to apply appropriate adjustment measures and to address the required tax reforms and the unfinished process of market liberalization. In this context, it is very important to make progress in the trade negotiations with the European Union.

European Union

7. Mr. Chairman, I would like to stress that among the main achievements of the current fiscal year, the **birth of the euro** as the common currency of eleven member countries of the European Union is of special importance. This will no doubt be one of the most transcendental events of the end of this century. The euro is born with a **vocation of stability**, not only for the member countries concerned, but also for the world economy as a whole. The euro is also born with the **vocation of being an internationally used currency**, and its use is becoming widespread in international financial markets and in world trade.

8. The Monetary Union has come accompanied by an important **improvement in the economic outlook for many of the European countries**. In the second half of this year, we are starting to note an acceleration of growth rates in the EU, which will be gradually taking greater responsibility as a catalyst of growth in the world. This outlook will no doubt be somewhat enhanced by the European countries' progress in fiscal affairs and by their continued efforts to make markets more flexible and to increase competition. It is very important for us to make progress in developing the European domestic market and, more concretely, in creating a single financial market. Lastly, attaining a balanced budget or a budget surplus and moving ahead with the structural reforms will continue to be a priority on our agendas.

III. Reference to the Spanish Economy

Structural change in the Spanish economy

9. I would like to draw your attention to the case that I know best, in which I feel I can state that the fiscal consolidation and market reform policies we are proposing have been successful. For three years now, the Spanish economy has been growing at over 3 percent a year; inflation is contained at around 2 percent in a context of price stability; and the job creation rate remains high, thus helping to reduce the unemployment rate by 7 points over the last three years. We believe that these results have been possible because there has been **a structural change in the Spanish economy**, which has generated sustained growth at over 3 percent a year without leading to inflationary processes or to a strong deterioration in the external sector.

Policies implemented

10. We also believe that this structural change is attributable not to chance, but rather to **perseverance in a number of policies** based on four fundamental pillars:

11. **FISCAL CONSOLIDATION.** First, a major effort was made to reduce the public deficit. The deficit amounted to 7.1 percent of GDP in 1995, but has now been reduced to 1.4 percent, and we expect to achieve budgetary balance in 2002. The reduction of the public deficit has led to a significant decline in interest rates and the freeing up of a large amount of financial resources which have been used to finance consumption and investment by households and enterprises. Fiscal policy credibility has been strengthened by the achievement, year after year, of the budgetary objectives set by the government and the passing of legislation officially holding the Executive to its budgetary commitments.

12. **STRUCTURAL REFORMS.** The second monetary policy line of action is the structural reform of goods and services markets. The privatization of many monopolistic public enterprises and the introduction of competition in such fundamental markets as energy, electricity and telephony have made it possible to improve resource allocation while reducing costs to our enterprises and have afforded many opportunities for investment and job creation.

13. **LABOR MARKET.** The third line of action consists of improving the functioning of the labor market. Through social dialogue, it has been possible to reduce hiring costs, increase stable employment, and foster new ways of joining the labor market, all of which surely lie behind the good behavior of labor market variables. At the same time, measures have been implemented to increase the labor force participation rate by improving human capital and reducing the fiscal wedge on the lowest wages. To this end, a large effort has been made in terms of proactive employment policies, direct taxes on

labor and social contributions have been reduced, and a full package of measures favoring the development of small and medium-sized enterprises has been implemented.

14. TAX REFORM. Lastly, I must not fail to stress the importance of the recent tax reforms to the change experienced by Spain's economy. I believe we can assert today that economic growth in any country is closely linked to the existence of a tax system that is efficient, transparent, and simple in its collection and control procedures. Past experience has shown us that excessive taxation, far from representing an element of solidarity and social cohesion, has only discouraged saving and entrepreneurship and introduced unnecessary complexity into the tax system. We are convinced that reforms aimed at encouraging work, saving, and investment eventually lead to countries' economic development and ultimately to larger tax collections.

IV. Reform of the International Institutional Framework

15. Mr. Chairman, I wish to express the importance Spain gives to the **need to strengthen the international institutional framework**. There can be no doubt that we have progressed over the past year in resolving the recent financial problems; nevertheless, the strengthening of the international monetary and financial system should remain the top priority on our agenda, even if we are not faced with such pressing problems as in the recent past.

16. In this regard, I firmly believe that the institutions born under the Bretton Woods Agreement must continue to be the **cornerstone of the international monetary and financial system**. To play this central role, however, they must adapt their operations to the new international environment, and in particular to the new challenges posed by the increasing integration of markets, the emergence of new players, and the increased mobility of financial flows. Accordingly, we welcome the measures aimed at strengthening the role and improving the functioning of the **Interim Committee**. We must not allow the debate on the international financial architecture to be shifted to illegitimate groups or fora, and we must ensure that all countries concerned are brought into the discussions.

17. The free flow of capital promotes growth, and we must insist on this objective. The liberalization process must take into account the particular circumstances of each country, especially the extent of its development and market liberalization, its integration into the international economy, and the degree of development of its financial supervision and control mechanisms.

18. We also believe in the search for voluntary consensus solutions for **effective private sector participation in forestalling and solving financial crises**.

V. Poverty Reduction

19. I would like to conclude by drawing your attention to the problems of the least privileged countries. The **fight against poverty** is no doubt a process that requires a long horizon. This is why we welcome the emphasis given in the agenda of the Bretton Woods institutions to aspects related to protecting the least privileged and creating social safety nets for the weakest. Of course, we will not succeed in reducing poverty without sustainable growth. But poverty reduction is not merely a matter of growth; we must have an effective strategy to reduce it. For all these reasons, we support the World Bank's Comprehensive Development Framework and the initiatives being made by the Fund in this regard. In support of this effort, **Spain has just pledged to provide the Fund with financing for structural adjustment loans to the lowest income countries in the amount of US\$180 million.**

20. We also welcome the **new debt relief initiative for the highly indebted poor countries**, which is more generous and comprehensive than the previous one. The Spanish government has argued without reservation for this needed initiative, which constitutes a landmark in economic and financial cooperation for the poor countries of our planet and fits in perfectly with the desires of the Spanish people and the political objectives of their government—one of the few that has been increasing its official aid to development in recent years. But this financial effort will be insufficient unless it is ensured that the resources made available will be used by the benefiting countries to finance projects that promote sustained economic and social development. Moreover, if debt relief is to have a lasting effect, we must ensure that developing countries become a part of the international economy and are able to benefit from the opportunities offered by the global economy.

21. For this initiative to become reality, we must find a **solution for its financing**. The Spanish government believes that this financing should consist of additional aid and must in no event diminish the resources flowing to other developing countries. In addition, it must not affect the financial soundness of international financial institutions nor drive up the cost of their loans. Accordingly, we rich countries must review our contributions to these institutions.

22. To this end, Spain has assumed a cost of **US\$100 million** within the framework of the **first HIPC Initiative**, including multilateral debt relief and bilateral debt forgiveness.

23. To contribute to the financing of the enhanced HIPC Initiative, Spain **will make available to the multilateral financial institutions a contribution** proportional to our share in the capital of these institutions.

24. Spain **reiterates** once again its proposal to assume the cost of its bilateral debt relief in accordance with the agreement reached at the European Summit in Cologne, in such terms as are agreed by the Paris Club. **This presupposes the forgiveness of the equivalent of US\$600 million dollars** in NPV terms.

25. We, the European ministers, have agreed to contribute the remaining **balances in the European Development Fund** (EDF) for debt relief for the ACP countries, and we would like to see this contribution extended to the other HIPC countries as well.

26. In conclusion, and to guarantee the linkage between debt relief and the fight against poverty, Spain is proposing the **creation of local currency funds** as a counterpart to bilaterally forgiven concessional debt. In this regard, we are considering the possibility that these funds might be managed by the multilateral financial institutions.