

19.07.2018

Address on taking up office as a member of the Council of State

Pablo Hernández de Cos
Governor

Madame Chair of the Council, Council Members, Lawyers, ladies and gentlemen,

First I would like to thank Mr. Alberto Aza and Mr. Juan Velarde for having agreed to be my sponsors in the ceremony today. It is a real honour for me to take up office as an ex officio member of the Council of State, the highest-ranking advisory body of the Government and a time-honoured institution in Spain.

According to the Spanish Royal Academy dictionary, an “adviser” is someone who gives an opinion on what they consider beneficial or necessary for the advisee. It is indeed an important aspect of the functions of the Banco de España, in accordance with its law on autonomy, to advise the Government on economic and financial matters.

From this dual status as a member of the Council of State and as governor of the Banco de España, allow me to take the opportunity here to briefly reflect on what are the main challenges facing the Spanish economy.

In the past five years our economy has seen sharp growth in activity and a marked reduction in the unemployment rate, enabling a gradual correction of the imbalances built up before and during the economic crisis.

Availing myself of my recent council member status, I would say that the guiding principle should be to avoid becoming complacent and, on the contrary, to harness the economic expansion so as to adopt the measures that may provide for sustainable growth, a greater degree of stability and more extensive room for manoeuvre in the face of potential future crises.

This advice stems from a diagnosis that is worth emphasising: the Spanish economy still has significant factors of vulnerability. These include most notably high external debt, a level of public debt close to its historical high, an unemployment rate double that of our European partners and a financial system facing considerable challenges; and this in a scenario where the economy must face the impact of the phenomenon of population ageing and the structural problem of low productivity.

It is further worth recalling that, although the recovery has rested on a diverse set of measures, in Spain and in Europe alike, it has also been underpinned by the support afforded by the European Central Bank’s extraordinarily expansionary monetary policy. Additionally, this expansion has been accompanied by a significant fiscal impulse in recent years. However, the effect of these monetary and fiscal impulses will tend gradually to fade in the coming years.

Against this background it is necessary, firstly, to deepen the fiscal consolidation process. The high level of public debt is harmful to the economy’s financing conditions, it restricts the countercyclical leeway of budgetary policy and it means a high volume of resources must be set aside to pay the interest burden.

There is room, moreover, for the fiscal consolidation process to be compatible with a revision of the structure of public revenue and spending, making it more efficient and

enhancing its contribution to growth. And, at the same time, a greater degree of fiscal co-responsibility should be promoted across the different tiers of general government.

It is likewise a priority to pursue further reductions in unemployment and its persistence among specific groups, especially the lesser-skilled. The high level of joblessness is also closely related to the notable increase in inequality that came about during the crisis. Achieving this will require not only labour market measures but also, more broadly, actions targeting employee skills and training, to encourage their greater adaptability to a new environment marked by technological progress, the automation of productive processes and the knowledge economy.

In parallel, despite the significant progress in recent years, the financial sector continues to face deep-seated challenges. These include the need to tackle the effects of the far-reaching changes in regulation, technology and competition, to improve low profitability levels and to complete the ongoing reduction of problem assets.

Looking ahead to the medium and long term, population ageing is probably the main challenge the developed societies face. According to projections by the National Statistics Institute, in the next 50 years the over-65 population, which currently accounts for less than one-fifth of the total population, will grow to represent more than one-third. This phenomenon will exert – and is already doing so – an adverse effect on the economy's participation rate, employment and productivity, and most singularly on public finances, raising spending on pensions, health and long-term care.

The scale of this challenge means a broader and longer-term strategy must be defined where, along with revising the arrangements for our welfare state and its financing, in order to ensure its sustainability, it will also be particularly important to have policies encouraging worker participation in the labour market, to align migratory policy with labour market needs and to pursue policies promoting the birth rate so as to draw it closer to the rates in other European countries.

The Spanish economy also evidences very poor figures in terms of productivity. Reversing this dynamic will require measures in various areas including, among other aspects, improvements in education, the quality of institutions, competition in product and service markets and investment in research, innovation and development, along with a reduction in temporary employment in the labour market.

I would like to conclude by stressing the importance of making Europe's challenges our own. In short, on the economic front, this currently involves two goals: completing the Banking Union and shoring up the fiscal stabilisation capacity of the euro area countries.

With the supervisory pillar in place, completing the Banking Union still calls – as the euro area Heads of State and of Government recently concluded – for a common backstop for the Single Resolution Fund. And, above all, the creation of a European Deposit Guarantee Scheme.

In the fiscal policy arena, fiscal stabilisation capacity in the euro area needs to be completed through two channels: improving the member countries' fiscal headroom and developing supranational cyclical insurance instruments.

To conclude, I turn once more to the Spanish Royal Academy, which defines "challenge" as an aim it is difficult to achieve and which is thereby an incentive and a test for whosoever faces it. Economic policy-making requires constantly facing the challenges our society throws up. To quote Jean Monnet, "Nothing would be more dangerous than to regard difficulties as failures".¹

Thank you.

¹ Jean Monnet, *Memoirs*, William Collins Sons & Co. Ltd., Great Britain, 1978.