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**BELGIAN STABILITY PROGRAMME**

**(2011-2014)**

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## Contents

<b>1</b>	<b>Introduction</b> .....	<b>1</b>
<b>2</b>	<b>Economic situation and macroeconomic assumptions</b> .....	<b>3</b>
2.1	Introduction .....	3
2.2	The economic outlook of the Federal Planning Bureau .....	3
2.3	Trend in economic activity.....	5
2.4	Outlook for 2011-2014.....	6
<b>3</b>	<b>Excessive deficit procedure</b> .....	<b>9</b>
3.1	Belgium facing recommendations.....	9
3.2	Budget outcomes in 2010 .....	11
3.2.1	Financing balance.....	11
3.2.2	Revenue and expenditure .....	16
3.2.3	Substantial improvement in the structural balance .....	19
3.2.4	Halting the snowball effect .....	20
3.3	2011 budget .....	23
3.3.1	Reduction in the deficit to 3.6 %.....	23
3.3.2	Measures taken at the level of Entity I.....	24
3.3.3	Measures taken at the level of Entity II .....	26
3.3.3.1	Walloon Region and French Community .....	27
3.3.3.2	Flemish Region .....	28
3.3.3.3	Brussels Capital Region .....	32
<b>4</b>	<b>Path for 2011-2014</b> .....	<b>34</b>
4.1	Medium-term path of Belgian public finances in accordance with the European recommendations .....	34
4.2	Allocation of the effort between the entities .....	36
4.3	Structural reduction in the public deficit in accordance with the European recommendations .....	38

4.4	Progressive reduction in the public debt consistent with the draft European directives .....	41
<b>5</b>	<b>Comparison with the 2009-2012 stability programme and sensitivity analysis .</b>	<b>45</b>
5.1	Consolidation speeded up compared to the previous stability programme.....	45
5.2	Sensitivity analysis.....	46
5.2.1	Deviations in terms of GDP growth.....	46
5.2.2	Deviations in terms of interest rates.....	48
5.2.3	Oil price fluctuation .....	49
<b>6</b>	<b>Sustainability of public finances .....</b>	<b>51</b>
6.1	Introduction.....	51
6.2	Budgetary consequences of ageing .....	51
6.2.1	Estimates of the Study Committee on Ageing .....	51
6.2.2	International comparison of the sustainability of public finances .....	55
6.3	The government strategy on ageing .....	56
<b>7</b>	<b>Sustainable consolidation of public finances, quality of public finances and macroeconomic challenges .....</b>	<b>58</b>
7.1	Main points of fiscal consolidation.....	58
7.2	The macroeconomic challenges .....	62
7.2.1	Boosting competitiveness and employment.....	63
7.2.2	Ensuring the sustainability of public finances .....	66
7.2.3	Strengthening financial stability .....	66
7.3	Quality of public finances .....	68
7.3.1	Combating fraud.....	68
7.3.2	Good and effective governance.....	70

# 1 Introduction

The economic and financial crisis caused a serious deterioration in public finances. Today, 23 of the 27 European Union members are subject to an excessive deficit procedure, and Belgium has been among that group of countries since 2 December 2009.

In recent months, in the wake of the economic and financial crisis, the creditability of the euro and Economic and Monetary Union has been in doubt. In response to these pressures, the European authorities decided to reform economic governance, to revamp the Lisbon Strategy (EU2020) and to set up the European Semester. This new *ex ante* coordination strengthens the consistency between the national reform programme - reflecting the main lines of economic and social policy – and the stability programme, which sets out the strategy for the sustainable consolidation of public finances.

It is against this new backdrop that the Belgian government is presenting its national reform programme and the stability programme.

On the basis of the figures published by the National Accounts Institute (NAI), the budget outcomes for the year 2010 are significantly more favourable than the target initially fixed in the January 2010 stability programme. In fact, with a deficit of 4.1 % of GDP in 2010, compared to 5.9 % in 2009, and a structural improvement ranging between 0.8 % of GDP and 1.3 % depending on the methodology, Belgium is a year ahead of the initial path for the consolidation of public finances. In addition, the rise in the public debt in 2010, amounting to 0.6 % of GDP, bringing the total to 96.8 % of GDP, is probably the smallest in the euro area.

True, this improvement in the general government budget balance is due to the stronger than expected revival in economic activity which, following a 2.7% decline in GDP in 2009, recorded 2.1 % growth, thus taking full advantage of the dynamism of the global economy and being supported by the good performance of the labour market, particularly following the crisis measures taken by the Belgian government. As well as fiscal prudence, the implementation of the measures provided for in the 2010-2011 multi-annual budget, with an impact of 1 % of GDP in 2011, and the measures taken by the federated entities are also contributing to the marked improvement in Belgian public finances.

On 24 March 2011, the federal government approved the 2011 budget containing fiscal measures amounting to 0.6 % of GDP. The Belgian government intends to respect its commitments in relation to the excessive deficit procedure, In particular, under this new stability programme, the Belgian government is adhering firmly to its commitment to reduce the public deficit below 3 % of GDP by 2012 at the latest and to restore balanced public finances in 2015. The proposed consolidation path is actually faster than the one laid down in the January 2010 stability programme.

With a target deficit of 3.6 % of GDP in 2011, the Belgian government aims to stabilise the endogenous public debt and start reducing the general government debt ratio by 2012. Moreover, if the economic environment proves more favourable than expected under this programme, the federal government is resolved to use the resulting additional revenue and decline in expenditure to reduce the deficit more quickly.

Apart from the fiscal measures, this consolidation of public finances will be based mainly on the implementation of economic and social reforms designed to boost the employment rate and sustainable, inclusive growth, in line with the EU2020 Strategy and the Euro Plus Pact. The initial decisions on the subject are explained in more detail in this stability programme and in the national reform programme.

The caretaker government is fully committed to adhering to the path mapped out in that stability programme. It is a prudent path.

It is for the next government to update the path, if appropriate, and to define the specific measures to ensure the sustainable consolidation of public finances.

## **2 Economic situation and macroeconomic assumptions**

### **2.1 Introduction**

The recession which started in 2008 had a major impact on the global economic situation in 2009 and 2010. The recession is also expected to continue having noticeable repercussions in the coming years. However, a recovery is undeniably perceptible, e.g. in the rebound of global trade. While the Asian countries are clearly recording strong economic growth, the other industrialised countries are also seeing growth pick up, albeit more slowly in the second half of 2010 than in the first half of the year.

In the medium term, the assumption is that the industrialised world will see an economic recovery. For the euro area, annual growth is forecast to average 2.2 % in the medium term, thanks in particular to Germany's sound economic performance. Nonetheless, the euro area's economy remains vulnerable, especially in the wake of the debt crisis, the uncertainty on the financial markets and the stronger competition from emerging industries. Commodity price volatility is another major risk to economic growth.

### **2.2 The economic outlook of the Federal Planning Bureau**

An April 2011 draft of the Federal Planning Bureau's economic outlook forms the basis of the path defined in this stability programme. In the short term (2011 and 2012), the Federal Planning Bureau's outlook is based on the January 2011 economic budget, but with adjustments to take account of the latest developments on the labour market and the latest inflation forecasts. The figures for the international economic environment in 2011 and 2012 are based on the European Commission's short-term (Autumn) forecast and on the latest economic data concerning the euro exchange rate and the oil price. In the medium term (2013 and 2014), the November 2010 OECD Economic Outlook is used.

The Federal Planning Bureau expects Belgium to see GDP growth of 2 % in 2011 and 2.3 % in 2012, compared to figures of 1.8 % and 1.9 % respectively for the EU. After that, Belgian

growth is expected to average 2.2 %, which is the figure which the OECD predicts in the medium term for the euro area. In Belgium's specific case, the Federal Planning Bureau forecasts economic growth of 2.1 % in 2013 and 2.3 % in 2014, while the growth figures forecast for the EU are 2.3 and 2.4 % respectively.

**Table 1: External environment**

	2010	2011	2012	2013	2014
Short-term interest rate (annual average)	0,8	1,6	2,5	2,6	2,8
Long-term interest rate (annual average)	3,3	4,2	4,5	4,6	4,7
USD/euro exchange rate (annual average)	132,6	139,6	139,2	139,2	139,2
Nominal effective exchange rate (2000=100)	109,6	107,2	107,8	107,8	107,8
GDP-growth - world (excluding EU)	5,6	4,6	4,6	4,6	4,6
GDP-growth - EU	1,9	1,8	1,9	2,3	2,4
Growth of relevant external markets	11,0	6,6	6,4	6,7	7,0
Global imports by volume (excluding EU)	13,8	8,2	8,0	7,5	7,5
Oil price (USD)	79,6	111,8	110,0	113,0	117,4

Source: Federal Planning Bureau

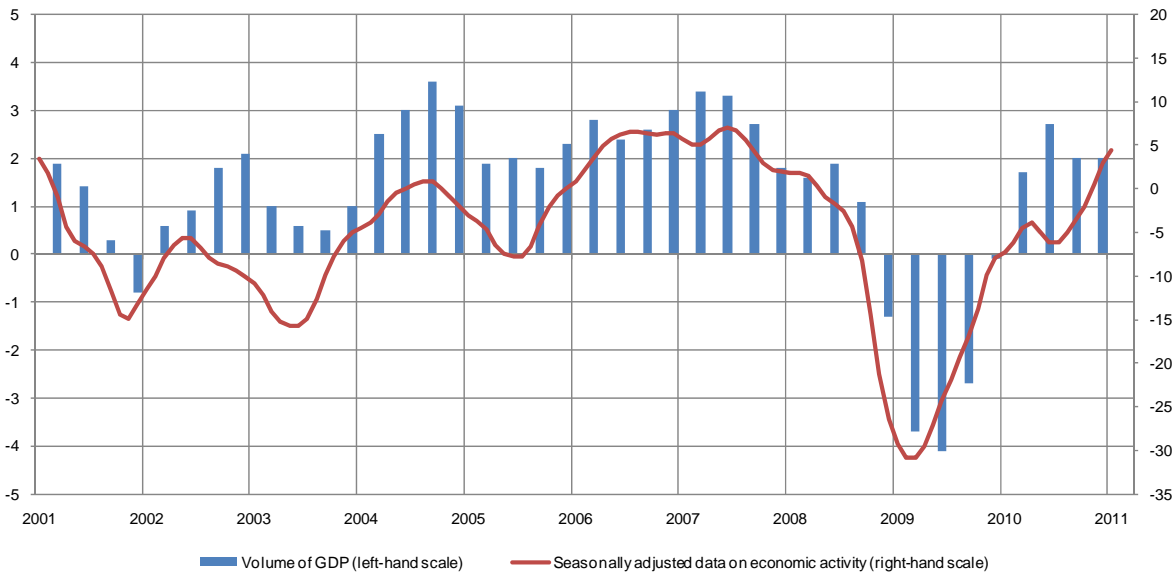
**2.3 Trend in economic activity**

Following a year of decidedly negative growth, GDP expanded significantly again in 2010. While the 2009 decline was not entirely offset, the Belgian economy recorded a strong performance (see chart 1). In that regard, one of the explanatory factors is the growth revival and strong recovery in Germany, which are having a positive impact on the Belgian economy. The global economic recovery is another key factor which had a positive influence on exports.

Similarly, consumer confidence rose strongly in 2010. The main improvement was in expectations concerning unemployment. In the past six months, consumer confidence has stabilised around its historical average.

The National Bank of Belgium’s business survey reveals a substantial improvement in the last year, especially in the second quarter of 2010. The first quarter of 2011 also shows an improvement in business confidence. That offers a sound basis for continuation of the good economic performance.

**Chart 1: Real quarterly GDP growth in % compared to the corresponding period of the previous year and the trend in economic activity**



Source: National Bank of Belgium



## 2.4 Outlook for 2011-2014

The Federal Planning Bureau predicts growth of 2 % in 2011 and 2.3 % in 2012. Belgium is therefore expected to continue outperforming the euro area average, as it did in 2009 and 2010. Similarly, the latest *consensus forecast* issued by *Belgian Prime News* in January – indicating the average prospects assumed by the large financial institutions in Belgium – expects Belgium to see stronger growth than the euro area countries, and forecasts 2% economic growth in 2011. Taking account of the uncertainty surrounding the projections, the government considers that 2 % growth in the medium term is realistic.

**Table 2: Detailed medium-term macroeconomic projections**

<i>percentage change unless otherwise stated</i>	2010	2010	2011	2012	2013	2014
	in € billion					
1. Real GDP	289,0	2,1	2,0	2,3	2,1	2,3
2. Nominal GDP	351,4	3,6	4,0	4,3	3,9	4,3
	Components of real GDP					
3. Private consumption expenditure	150,4	1,4	1,5	1,7	1,7	1,8
4. Government consumption expenditure	62,8	1,1	1,1	2,1	1,9	2,0
5. Gross fixed capital formation	61,3	-1,9	2,9	3,4	1,5	2,4
6. Changes in inventories and net acquisition of valuables	0,1	0,1	0,0	0,0	0,0	0,0
7. Exports of goods and services	249,9	10,1	4,6	4,4	4,7	4,9
8. Imports of goods and services	236,1	7,8	4,2	4,3	4,3	4,6
	Contributions to real GDP growth					
9. Final domestic demand	-	0,2	1,5	2,1	1,7	1,9
10. Changes in inventories and net acquisition of valuables	-	-0,5	-0,1	0,0	0,0	0,0
11. External balance of goods and services	-	1,9	0,5	0,2	0,4	0,4

Source: Federal Planning Bureau

The recovery is perceptible in the various sectors. Domestic demand is assumed to make a large contribution to GDP growth. Exports are also a key driver. Following 10% expansion in 2010, export growth will revert to a more modest level in the medium term. However, the expansion falls short of the export market growth so that market shares are being eroded. Nevertheless, the trade balance remains in surplus for the time being. Owing to the improvement in confidence, investment is also expected to expand considerably, gathering momentum in 2012, despite the rise in interest rates.

**Table 3: Prices in the medium term**

<i>% change</i>	2010 (2000=100)	2010	2011	2012	2013	2014
1. GDP deflator	121,6	1,5	1,9	1,9	1,8	1,9
2. Private consumption deflator	122,6	2,3	3,3	1,9	1,9	2,0
3. HICP	122,7	2,3	3,5	1,9	1,9	2,0
4. Public consumption deflator	136,4	1,3	2,8	2,3	1,9	2,0
5. Investment deflator	116,0	0,8	1,8	1,6	1,5	1,7
6. Export price deflator (goods and services)	113,8	4,4	4,2	2,1	1,9	2,2
7. Import price deflator (goods and services)	115,5	6,2	6,2	2,1	1,9	2,2

Source : Federal Planning Bureau

The Federal Planning Bureau expects inflation to gather pace in 2011, predicting a rise of 3.5% in the harmonised index of consumer prices. The index is expected to drop to 1.9 % in 2012 and stabilise at that level in the medium term. Price increases in Belgium are noticeably higher than the euro area average, certainly in 2011. In fact, the Belgian consumer price index is more sensitive to increases in commodity prices, especially the oil price. That may be due to the high energy consumption of households, relatively low excise duties and the substantial and swift impact of energy price increases on gas and electricity tariffs. Against that background, the federal government recently took the first steps to reduce the volatility of energy prices (see chapter 7).

The oil price will continue to be a major determinant of price levels in the future. In that regard, a number of uncertain factors are involved, such as the impact of the political turmoil in North Africa on oil supplies and oil prices.

**Table 4: Labour market**

<i>% change, unless otherwise stated</i>	2010 Level		2010	2011	2012	2013	2014
1. Domestic employment	4.466,6	(a)	0,6	0,9	0,9	1,0	1,1
2. Numbers of hours worked	6.473,2	(b)	0,8	1,2	1,1	1,0	0,9
3. Unemployment rate (% Eurostat definition)	8,4		8,4	8,3	8,3	8,1	8,0
4. Labour productivity, persons	64.700	(c)	1,4	1,1	1,4	1,1	1,3
5. Labour productivity, hours worked	44,6	(c)	1,2	0,8	1,2	1,1	1,4
6. Compensation of employees	182	(d)	1,6	4,3	3,8	4,3	4,8
7. Compensation per employee	48.700	(c)	1,0	3,3	2,7	3,1	3,5

(a) thousands; (b) millions of hours ; (c) € ; (d) € billion

Source : Federal Planning Bureau

The economic crisis had a relatively limited impact on employment in Belgium. That was due to the action of the automatic stabilisers, intensive use of federal and regional anti-crisis measures, such as the system of temporary lay-offs, the crisis time credit, and the reduction in working time during the crisis, the reduction in employers' labour costs for certain target groups (the "Win-Win" plan), and some additional crisis measures, notably targeted fiscal measures in favour of labour-intensive sectors such as the hotel and restaurant trade and the construction industry, primarily during the first phase of the crisis. Total employment is expected to increase by 0.9 % in both 2011 and 2012, exceeding the forecasts for the euro area (increases of 0.4 % and 0.8 % respectively). In the medium term, too, that growth looks set to continue. As a result of this favourable trend, the unemployment rate is also expected to fall, declining from 8.4 % in 2010 to 8 % in 2014 if the policy is unchanged (Eurostat definition).

## **3 Excessive deficit procedure**

### **3.1 Belgium facing recommendations**

On 2 December 2009, for the first time since the start of Economic and Monetary Union, Belgium was subjected to an excessive deficit procedure, in common with 22 other Member States at present.

In that context, the European Council of 2 December 2009 recommended that the Belgian government should put an end to the excessive deficit procedure in 2012 at the latest by making a structural effort averaging 0.75 % of GDP per annum. The European Council also advocated the earliest possible implementation of the measures laid down in the 2010/2011 multi-annual budget.

In January 2010, Belgium submitted a stability programme under which the excessive deficit procedure would end in 2012 and public finances would be restored to balance in 2015. At the July 2010 European Council, the Heads of State and Government considered that Belgium had acted in accordance with the recommendations (see annex).

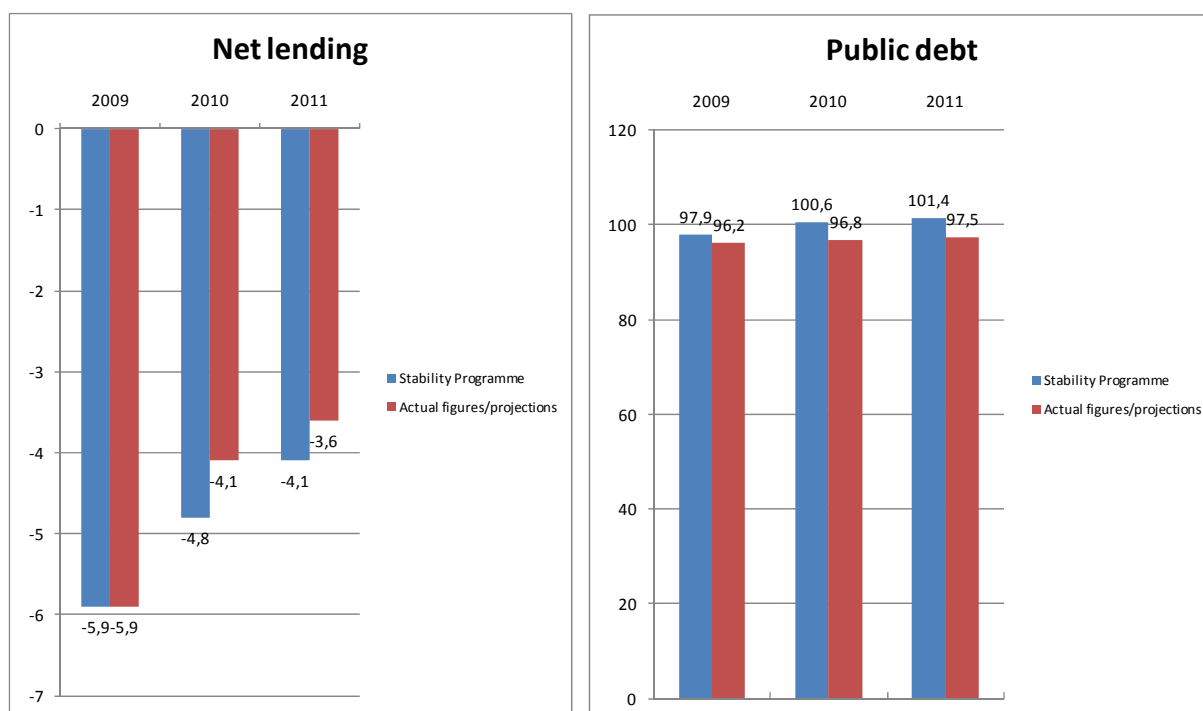
Since then, the Belgian government considers that it has continued to produce a good response to the European recommendations in view of the fact that:

- The budget outcomes for 2010 are considerably better than the targets set in the 2010 stability programme, with a general government deficit of 4.1 % of GDP, compared to the original figure set at 4.8 %. Belgium is thus a year ahead of the original targets.
- In consequence, and taking account of the active management of the public debt, Belgium recorded the smallest rise in the public debt in the euro area (on the basis of the currently available data). The public debt came to 96.8 % of GDP in 2010, compared to 96.2 % of GDP in 2009.

- The improvement in the structural balance in 2010 ranged between 0.8 % of GDP and 1.3 % of GDP, depending on the methodology used.
- Moreover, the 2011 budget provides for a deficit of 3.6 % of GDP for general government as a whole, or 0.5 % of GDP less than under the 2010 stability programme. That target permits stabilisation of the endogenous debt ratio. It should be noted that the 2011 budget was based on a deficit of 4.5 % of GDP in 2010. It is therefore possible that the 2011 budget outcomes may also outperform the target.
- The government is steadfastly committed to satisfying the conditions permitting the excessive deficit procedure to end in 2012 at the latest.

**Chart 2: Financing balance and public debt**

(In % of GDP)



Sources : 2010 stability programme, National Accounts Institute (2011)

## 3.2 Budget outcomes in 2010

### 3.2.1 Financing balance

According to the NAI's initial estimates published on 31 March, the 2010 budget outcomes are much better than the targets set by the Belgian government in 2010, with a general government deficit of 4.1 % of GDP, compared to the 4.8 % of GDP initially expected.

In relation to 2009 (-5.9 % of GDP), the general government balance thus shows an improvement of 1.8 percentage points in 2010, bringing to an end the deterioration in Belgian public finances apparent since 2007. That improvement is also tending to be much better than the average improvement recorded in the euro area (0 % of GDP)<sup>1</sup>.

**Table 5: Financing balance (in % of GDP)**

	% GDP				Change	
	2009	2010			Actual figures for 2010 versus 2009	Actual figures for 2010 versus Stability Programme
	Actual figures	Stability programme January 2010	NBB - 2010 Annual Report Targets (February 2010)	National Accounts Institute Actual figures (March 2011)		
<b>General government</b>	<b>-5,9%</b>	<b>-4,8%</b>	<b>-4,6%</b>	<b>-4,1%</b>	<b>1,8%</b>	<b>0,7%</b>
* Entity I	<u>-5,0%</u>	<u>-3,8%</u>	<u>-3,4%</u>	<u>-3,2%</u>	<u>1,8%</u>	<u>0,6%</u>
+ Federal government	-4,2%	-3,3%	-3,3%	-3,1%	1,1%	0,2%
+ Social Security	-0,8%	-0,5%	-0,2%	-0,1%	0,7%	0,4%
* Entity II	<u>-0,9%</u>	<u>-1,0%</u>	<u>-1,1%</u>	<u>-0,9%</u>	<u>0,0%</u>	<u>0,1%</u>
+ Communities and Regions	-0,8%	-0,6%	-0,8%	-0,7%	0,1%	-0,1%
+ Local authorities	-0,1%	-0,4%	-0,4%	-0,2%	-0,1%	0,2%
Gross debt (Maastricht)	96,2%	100,6%	97,5%	96,8%	0,6%	-3,8%

Sources: National Accounts Institute, National Bank of Belgium.

The movement in the 2010 financing balance is due mainly to:

- 1) the marked improvement in economic growth;
- 2) the implementation of a multi-annual budget at the level of Entity I and economy measures at the level of the federated entities;
- 3) a prudent fiscal policy;

- <sup>1</sup> European Commission (November 2010).

- 4) downward revision of the local authority deficit as a result of an improvement in the quality of the local authority accounts.

**Table 6: 2010 financing balance and economic growth**

<i>In % of GDP</i>	Economic growth	2010 financing balance
Stability programme complement (September 2009)	0,4%	-6,0%
Budget for 2010-2011 (October 2009)	0,4%	-5,4%
Stability Programme (January 2010)	1,1%	-4,8%
+ budget audit (March 2010)		
Actual figures (March 2011)	2,1%	-4,1%

According to the initial estimates available for the national accounts, economic growth came to 2.1 %, whereas the January 2010 stability programme had predicted 1.1% growth. The Belgian government has thus fully respected its commitment to allocate the benefits of more favourable economic growth to the reduction of the deficit and the public debt.

This improvement in the economic environment is not the only factor contributing to the substantial reduction in the deficit, especially as economic growth in 2010 was driven mainly by foreign demand, which generates smaller tax revenues.

These better results also reflect the prudence displayed by the government in producing its estimates and in drawing up the multi-annual budget for 2010/2011 in October 2009. The government's approach is relatively conservative in that the budget did not include all the known instances of under-use of expenditure. In that way, the government indirectly created "buffers" which act as a cushion for some potentially adverse developments.

As explained in detail in the 2010 stability programme, the main measures for the consolidation of public finances in 2010/2011 concern:

- 1) Substantial efficiency gains in the public sector. These efforts seem to be bearing fruit; the measures introduced at the level of federal government personnel are reflected in a 5% reduction in the workforce over the period 2008-2011; also, in 2010, remuneration expenditure was down by 0.3 % in real terms at the level of general government, and 1.8 % in the federal authority (see chapter 7.3.2).

- 2) Savings on health care and expenditure control in this sector; despite the statutory target of 4.5 % in real terms, the effective real growth of health care expenditure came to 0.5 % in 2010.
- 3) A tax structure which encourages ecologically responsible behaviour. To that end, the government decided, in particular, to make company car users aware of the CO<sub>2</sub> emissions of the vehicles chosen (charging of personal income tax on the benefit obtained, and variable corporation tax allowance depending on the CO<sub>2</sub> emission). The ratchet system was also extended to diesel fuel. Moreover, the windfall effects were eliminated from the measures to promote energy-saving investments (restriction of a large proportion of the tax concessions to homes at least 5 years old).
- 4) A contribution from the financial sector in response to the support given by the Belgian government during the financial crisis; that contribution is tending to exceed the amount initially foreseen owing to the stronger expansion of deposits (+ € 26 million in 2010 and € 150 million in 2011).
- 5) Major efforts to curb social security fraud and tax evasion (see chapter 7.3.1).





period was estimated on the basis of the commitments included in the accounts for the actual financial year. While this approach avoided the multiple accounting which would have resulted if all the commitments entered in the accounts for the full year had been included, it nevertheless caused a time bias, since the investments were recorded at the time of signing of the public contract and not as at their effective date. From now on, municipal investments are being estimated on the basis of imputed figures entered in the accounts for the full year.

The NAI and the Regions will continue to collaborate in the coming months in order to improve the quality of the statistical data in the local authority accounts, and thus meet the Eurostat requirements on the subject.

At federal level, despite the absence of a government with a full mandate since 26 April 2010, public finances have been kept under control, notably by close monitoring of expenditure and revenue. The federal government thus recorded a small deficit on the primary balance of 0.1 % of GDP in 2010, following a deficit of 0.8 % of GDP in 2009.

Taking account of the nervousness of the financial markets at the time, the excessive deficit procedure which Belgium is undergoing and the continuing high level of the Belgian debt, the federal authorities in fact decided, on 7 May 2010, to implement various measures in order to ensure that Belgian public finances remain under control:

- Creation of a Monitoring Committee, comprising representatives of the heads of the authorities in charge of Finance, Social Security and the Budget ; that committee is intended to conduct regular monitoring of budget developments and to report regularly to the Minister and the State Secretary for the Budget, and to the government.
- Establishment of a budget discipline procedure: that procedure requires all new expenditure by federal State departments with a budgetary cost of more than € 31,000 excluding VAT to be submitted for the approval of the Council of Ministers.

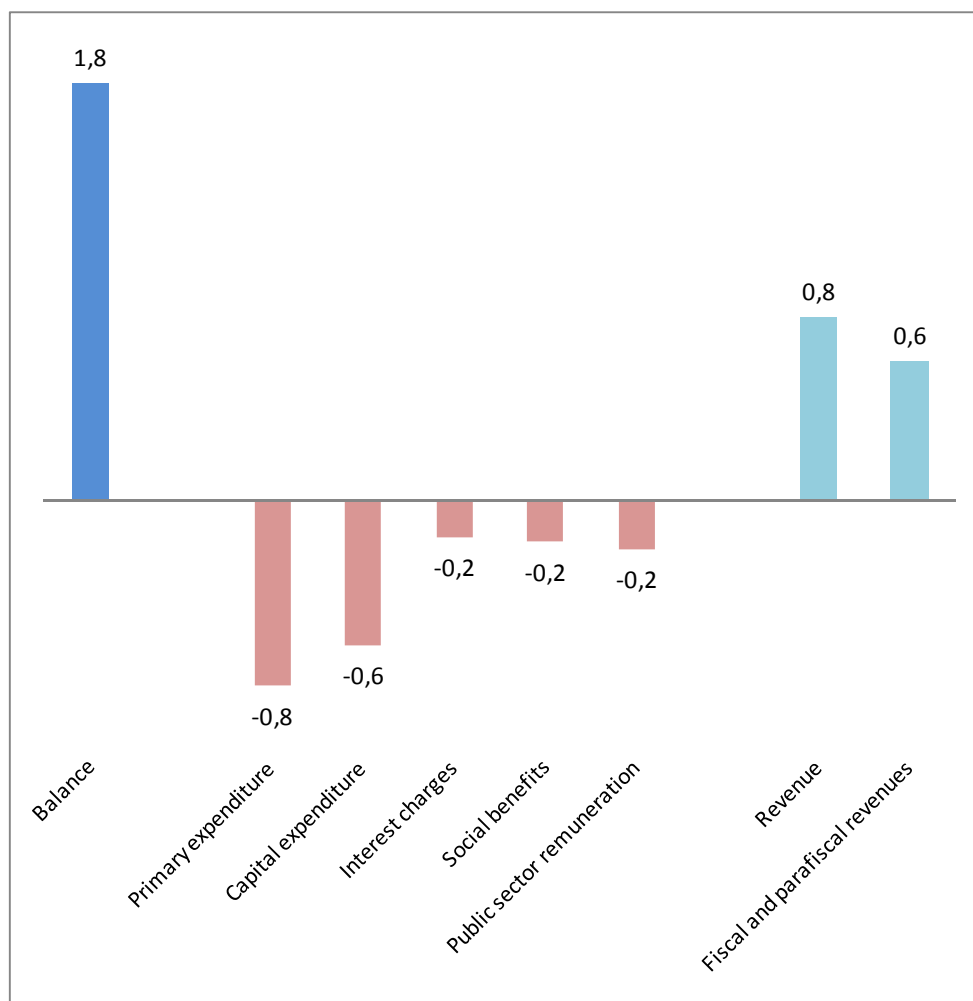
Only measures which are vital to the efficient operation of the departments will be approved. This procedure thus tends to slow the growth of primary expenditure by the federal State.

### 3.2.2 Revenue and expenditure

The improvement in the balance between 2009 and 2010 is due both to a reduction in expenditure (-1.0 % of GDP) and a rise in total revenues (+0.8 % of GDP).

**Chart 3: Main factors accounting for the improvement in the 2010 balance**

(in % of GDP)



Source: National Accounts Institute (2011)

Primary expenditure declined by 0.8 percentage point to 49.6 % of GDP in 2010. Interest charges were down by 0.2 percentage point to 3.4 % of GDP, taking account of the steep fall in interest rates on the financial markets and active management of the debt.

Remuneration (-0.3 % of GDP) and social benefits (-0.2 % of GDP) account for half of the decline in expenditure. These figures indicate that the economy measures concerning personnel and the efficiency gains in the public sector have borne fruit, as have the measures to control health care expenditure.

Capital expenditure accounts for the other half, with a decline of -0.5 % of GDP. In 2009, that expenditure had been influenced by the repayment, ordered by the courts, of certain taxes unlawfully collected in the past from companies receiving dividends from foreign subsidiaries, on the one hand, and from married unemployed persons on the other.

**Table 8: Real growth of primary expenditure\***

<i>% change compared to the previous year</i>	2009	2010
Total primary expenditure	7,2	-0,2
Remuneration	4,1	-0,3
<i>of which: at federal level</i>	1,9	-1,8
Social benefits	7,2	0,7
<i>pensions</i>	6,0	0,9
<i>unemployment</i>	19,5	-3,2
<i>incapacity</i>	8,6	6,0
<i>health care</i>	7,3	0,5
<i>p.m. economic growth</i>	-2,9	2,1

\*deflated by the harmonised index of consumer prices

Source: National Accounts Institute

With an overall decline in primary expenditure of 0.2 % in real terms, Belgium is thus responding favourably to the European recommendations, and in particular to the Annual Growth Survey, which – in the case of Member States subject to an excessive deficit procedure – provides that the real growth of expenditure must be less than the GDP growth. The recorded difference between the rate of GDP growth and primary expenditure is therefore 2.3 % in 2010.

Revenues increased by 0.8 % of GDP to reach 48.9 % of GDP. The revenue growth is due to the rise in both fiscal and parafiscal revenues (0.5 % of GDP) and in non-fiscal and non-parafiscal revenues (0.2 % of GDP), which are increasing mainly as a result of the payments made by financial institutions following the State interventions at the time of the financial crisis.

**Table 9: Revenues**

<i>In % of GDP</i>	2009	2010
<b>Total revenues</b>	<b>48,1</b>	<b>48,9</b>
Fiscal and parafiscal revenues	45,2	45,7
Direct taxes	15,2	15,6
<i>Households</i>	12,5	12,7
<i>Enterprises</i>	2,7	2,9
<i>Other sectors</i>	0,1	0,0
Indirect taxes	12,6	12,9
Taxes on capital	0,7	0,7
Social security contributions	16,8	16,5
Other	2,9	3,2

The increase in direct taxes on households is attributable, at the level of the Flemish Region, to the abolition of the flat-rate reduction introduced in 2007 and to the fact that the “personal income tax” assessments present a smaller negative balance than in 2010. The impact of these two factors on revenues was only partly offset by the impact of the measures taken by the federal government to reduce the tax burden.

Corporation tax revenues picked up slightly after the crisis in 2009, but are still below the level prevailing before that date.

The increase in the weight of direct taxation in 2010 is due in particular to the favourable trend in private consumption and the considerable rise in excise revenues following the introduction of the ratchet system on diesel.

The interventions in the financial sector have the corollary of additional interest charges to finance capital stakes or loans in favour of financial institutions receiving public support. Whereas in 2008 and 2009, the net result – i.e. the difference between the remuneration generated by these interventions and the interest charges resulting from the interventions (excluding the deposit protection fund), was slightly negative, in 2010 there was a positive result of +€ 252 million, or +0.1 % of GDP.

**Table 10: Impact on the financing balance of the public interventions and guarantees for financial institutions**

<i>In € million, unless otherwise stated</i>	2008	2009	2010
Dividends	53	121	192
Guarantee premiums	25	508	682
Interest paid	-96	-655	-622
Other	-10	-7	0
<b>Impact</b>	<b>-27</b>	<b>-33</b>	<b>252</b>
Impact in % of GDP	0,0	0,0	0,1
<i>Deposit protection fund</i>	25	93	251

Source: NBB, Report 2010, Economic and financial developments

### 3.2.3 Substantial improvement in the structural balance

Sustainable consolidation of public finances necessarily entails a reduction in the structural financing balance.

According to the European Commission’s methodology concerning cyclical effects, the structural deficit declined from -3.4 % of GDP in 2009 to -2.6 % of GDP in 2010, i.e. a 0.8 % improvement, in line with the European requirements. In a more favourable than expected economic context, the “output gap” was revised upwards, tending to increase the cyclical component. The latter is estimated at 1.4 % of GDP. Temporary measures contribute -0.1 % of GDP.

Moreover, according to the methodology developed by the European System of Central Banks (ESCB), the structural balance is assessed at -3.5 % of GDP in 2010 compared to -4.8 % of GDP in 2009, an improvement equal to 1.3 % of GDP, which is almost twice the figure stipulated by the Council.

The difference between the results indicated by the two methodologies is due mainly to the fact that the ESCB methodology takes account of the composition of the growth and of the specific cyclical dynamics of the various tax bases. Conversely, the European Commission methodology is based on a fixed elasticity of around 51 % for calculating the structural balance. As already stated, growth in 2010 was driven more by external demand, which generates lower tax revenues. Among other things, that accounts for the bigger improvement in the structural balance recorded according to the ESCB methodology.

In general, we can therefore conclude that Belgium respects the requirements in regard to 2010.

### **3.2.4 Halting the snowball effect**

Following two substantial consecutive increases of 5.4 % of GDP in 2008 and 6.6 % of GDP in 2009 (partly as a result of the support measures granted to the financial sector, amounting to 6.35 % of GDP, and partly in the wake of the economic crisis which caused both a steep decline in GDP and a significant deterioration in public finances), the expansion of the public debt slowed considerably in 2010.

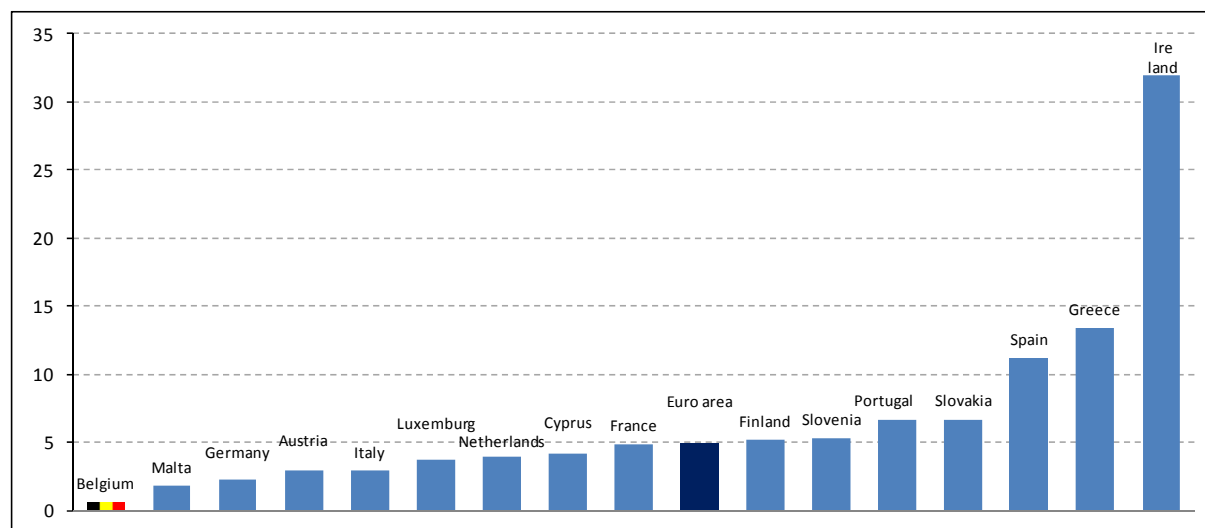
According to the information currently available, Belgium recorded one of the smallest increases in the public debt within the euro area in 2010, with a rise of 0.6 % of GDP, of which 0.2 % of GDP was due to the loan to Greece under the European support mechanism. In the euro area, the increase in the public debt averaged around 5 % of GDP<sup>2</sup> in 2010.

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- <sup>2</sup> European Commission (November, 2010)

**Chart 4: Increase in the public debt in the euro area in 2010**

(in % of GDP)



Source: National Accounts Institute, European Commission (2010)

This performance is a significant improvement on the targets originally set in the 2010 stability programme (100.6 % of GDP), despite the loan to Greece under the European aid plan for that country (0.2 % of GDP), which was not planned at the time.

In 2010, the snowball effect diminished rapidly, as is evident from the adjusted nominal differential<sup>3</sup> which, thanks to the marked revival in economic activity and the decline in the implicit interest rate, was greatly reduced (from 5.8 % in 2009 to -0.1 % in 2010). Consequently, the primary balance needed to stabilise the debt ratio is down sharply (from 5.2 % of GDP in 2009 to 0.2 % in 2010). The significant improvement in the primary balance (from -2.3 % of GDP in 2009 to -0.7 % of GDP in 2010) therefore strongly restrains the endogenous rise in the debt ratio.

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<sup>3</sup> The adjusted nominal differential is the ratio between, on the one hand, the difference between the implicit interest rate on the debt and nominal GDP growth, and on the other hand, 1 plus nominal GDP growth.



**Table 11: Debt ratio and its determinants**

<i>In % of GDP</i>	2006	2007	2008	2009	2010	Annual averages	
						2006-2008	2009-2010
<b>Actual debt ratio</b>	<b>88,1%</b>	<b>84,2%</b>	<b>89,6%</b>	<b>96,2%</b>	<b>96,8%</b>	<b>87,3%</b>	<b>96,5%</b>
<i>Annual differential (% of GDP)</i>	-4,0%	-3,9%	5,4%	6,6%	0,6%	-0,8%	3,6%
Required primary balance (RPB)	-0,5%	-0,6%	1,4%	5,2%	0,2%	0,1%	2,7%
Actual primary balance (APB)	4,1%	3,5%	2,5%	-2,3%	-0,7%	3,4%	-1,5%
<b>(1) Endogenous debt adjustment (RPB) – (APB)</b>	<b>-4,6%</b>	<b>-4,1%</b>	<b>-1,1%</b>	<b>7,5%</b>	<b>0,9%</b>	<b>-3,3%</b>	<b>4,2%</b>
(2) Transactions outside the financing balance	0,6%	0,2%	6,5%	-1,0%	0,0%	2,4%	-0,5%
<b>Technical parameters</b>							
Implicit interest rate "I"	4,5%	4,6%	4,6%	4,0%	3,7%	4,6%	3,8%
Nominal GDP growth "n"	5,1%	5,3%	3,0%	-1,7%	3,5%	4,4%	0,9%
Real GDP growth	2,7%	2,9%	1,0%	-2,8%	2,1%	2,2%	-0,3%
<b>Adjusted nominal differential "(i-n)/(1+n)"</b>	<b>-0,5%</b>	<b>-0,7%</b>	<b>1,6%</b>	<b>5,8%</b>	<b>-0,1%</b>	<b>0,1%</b>	<b>2,8%</b>

Source : National Accounts Institute

This small increase is due to more favourable budget outcomes and a larger rise in nominal GDP, but also to active management of the public debt, particularly via swaps.

In fact, during the second quarter of 2010, the Treasury cancelled the interest rate swaps (receiver swaps) which it had contracted in 2009 in order to increase its sensitivity to short-term interest rates. This concerned a total notional amount of €15.0 billion. The steep decline in swap interest rates had inflated the market value of these positions, so that cancellation of these swaps raised a total of €1.04 billion (0.30 % of GDP). During the same period, the Treasury had also cancelled a series of other historical positions of the same type (receiver swaps) for a total notional amount of € 7.0 billion. Those cancellations raised € 1.12 billion for the Treasury (0.31 % of GDP).

In all, the debt was therefore cut by € 2.16 billion, or 0.61 % of GDP, following the swap cancellations. Part of this amount was imputed to the 2010 public deficit, but most of it will not be imputed until 2011 and subsequent years, in proportion to the residual term of the cancelled swaps.

In addition, the interest rate swaps also had a positive impact on the public deficit since the coupons received exceeded the coupons paid. Thus, in 2009 the swaps contracted in that year

already produced an economic saving of € 185.8 million on the interest. In 2010, that saving amounted to € 395.97 million.

### **3.3 2011 budget**

#### **3.3.1 Reduction in the deficit to 3.6 %**

Apart from the measures taken under the multi-annual budget for 2010/2011 in October 2009, on 24 March 2011 the Belgian government approved the 2011 budget which will replace the provisional loans and the Finance Law previously passed. This budget will be presented to Parliament in mid-April. The target which the Belgian government has set itself for the deficit is 3.6 % of GDP. That target:

- 1) is 0.5 % of GDP more favourable than the target set in the January 2010 stability programme;
- 2) should permit stabilisation of the endogenous debt;
- 3) is more favourable than the target recommended by the High Council of Finance.

It is always possible that the budget outcomes might be even better than expected, as the target set by the Belgian government takes no account of the more favourable performance in 2010.

On that basis, in comparison with the stability programme introduced in January 2010, the Belgian general government deficit should already have declined to close to the threshold for the excessive deficit procedure during 2011. The Belgian government therefore considers that it is fully respecting its European obligations for the year 2011.

### 3.3.2 Measures taken at the level of Entity I

The Entity I budget is based on the Monitoring Committee's report dated 14 February 2011<sup>4</sup>. With no change of policy, the estimates indicated a deficit of 4.5 % of GDP for general government as a whole and 3.7 % for Entity I.

At federal level, despite its caretaker status, the government decided to take the necessary measures to comply with the European requirements by placing the emphasis partly on expenditure control and partly on optimising the collection of public revenues and stepping up the control of social security fraud and tax evasion. The measures taken at Entity I level amount to 0.6 % of GDP.

**Table 12: Summary of the measures taken at Entity I level under the 2011 budget**

<i>In € million</i>	Entity I measures 2011 budget
<b>Primary expenditure</b>	<b>506</b>
<b>Social security</b>	<b>501</b>
<i>of which: health care</i>	252
<i>social security fraud</i>	78
<b>Tax revenues</b>	<b>693</b>
<i>of which: banking secrecy, regularisation, court settlements</i>	460
<i>notional interest</i>	50
<b>Non-fiscal revenues</b>	<b>592</b>
<i>of which: additional dividends from financial institutions</i>	422
<b>Total effort</b>	<b>2.292</b>
Total effort (in % of GDP)	0,6

At the level of primary expenditure, the Belgian authorities focused on efficiency gains. Apart from the fact that the initial budget was based on provisional twelfths and the take-up was re-assessed according to the level seen in previous years, it was decided to reduce the ministerial office appropriations by 10 % over the year 2011 (€ 6 million).

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<sup>4</sup> [www.begroting.be](http://www.begroting.be)

Regarding social security, the emphasis was also on controlling expenditure, especially in the health care sector. In that sector, economy measures were applied in both 2010 and 2011, mainly in the medicinal products sector and in the sectors with strong expenditure growth (clinical biology and medical imaging). In addition, taking account of the very modest growth of health care expenditure in 2010, spending will be cut by a further € 252 million in 2011, on top of the € 1.094 million approved on 15 October 2010.

Additional measures were also passed in connection with fraud prevention, notably in order to combat the “sham self-employed workers” in the service voucher sector and in regard to temporary lay-offs, particularly by widespread recourse to electronic returns. In the service voucher sector, the government decided to tighten up the approval conditions and to take a set of tougher measures to control infringements and fraud.

In regard to tax revenues, the Belgian government also took two key decisions with a view to improving the proper collection of taxes in an international context of increasing data exchange and in the context of the Savings Directive: 1) the lifting of banking secrecy and 2) amicable settlements (court cases).

The federal Parliament recently decided to lift banking secrecy in regard to income taxes, subject to conditions guaranteeing privacy protection. Those measures should increase the effectiveness of the control of tax evasion in Belgium, and will also avoid international sanctions, owing to the existence of a legal instrument permitting the exchange of banking information with other Member States with a view to the assessment of income tax by those countries. These new decisions should most definitely encourage many citizens to apply for regularisation in the coming months, by payment of the tax due and a fine.

The federal Parliament also approved a court settlement procedure. In particular, amicable settlements provide for a number of measures giving rise to an extension of the system of dropping criminal proceedings on payment of a sum of money, known as the “settlement”. That settlement will only be possible following payment of the defrauded taxes or social security contributions, including interest, and with the agreement of the tax or social security authorities. This measure should enable the Belgian government to recover more of the sums due more quickly.

Together, these measures plus the tax regularisations and measures to cut abuse under the notional interest system should generate € 510 million.

The federal State is also receiving growing remuneration from the financial sector, as a result of both the increase in dividends from some institutions, in a context of increasing profitability, and a rise in the yield from the new deposit guarantee system in view of the expansion in the volume of deposits.

**Table 13: Impact on the budget of contributions from the financial sector in 2011**

<i>In € million</i>	Contributions from the financial sector 2011
Participating interests	361,6
Loans	425,1
Guarantees	622,5
Special protection fund	751,9
<b>Total</b>	<b>2.161,1</b>

As will be explained in more detail in chapter 7 and in the national reform programme, the Belgian government also adopted certain measures to boost the competitiveness of the Belgian economy, to support domestic demand, to increase the flexibility of the labour market and to make it easier for persons affected by a disability to return to work.

**3.3.3 Measures taken at the level of Entity II**

The federated entities also implemented significant economy measures designed essentially to increase efficiency in the public sector.

The following three sub-sections set out the respective contributions of the federated entities.

### *3.3.3.1 Walloon Region and French Community*

“In the summer of 2009, the Governments of Wallonia and of the French Community passed a package of measures aimed at controlling the growth of primary expenditure of the two Entities. Measures were also adopted in order to improve the yield on certain regional revenues. The two Governments aimed to place Wallonia and the French Community on a path returning them to balance in 2015 while ensuring funding for the stated regional and community policy, particularly the Marshall 2. Green Plan.

These measures were already implemented at the time of the 2009 budget adjustment, and at the latest during preparation of the 2010 budget. The main economy measures are recurrent throughout the 2009-2015 period:

- In 2009, a 15 % cut in expenditure on the operation of ministerial offices and a cut in the number of Ministers.
- Freezing of the operating allowances paid to the Walloon Parliament and to the French Community Parliament.
- Freezing of the operating and/or investment subsidies granted to public interest agencies and to the RTBF [French language broadcasting company].
- Dropping of a range of new policies considered when the economic situation was more favourable.
- A 3 % cut in expenditure on the civil service.
- A cut of around 30 % in the Wallonian communication budget.
- Freezing of the appropriations allocated to certain primary expenditure.

At the level of the French Community, the phasing of certain multi-annual expenditure plans (uprating of operating allowances and subsidies for educational institutions, university funding, etc.) was revised in order to smooth the impact over the period in question.

In essence, the measures passed by the governments correspond to structural savings and have an effect over the whole of the period covered by the present stability programme.

In 2010 and 2011, the governments of Wallonia and of the French Community decided that part of the additional revenues generated by the revival in economic activity would be allocated to reducing the financing requirement, at a rate of €100 and €222 million respectively in 2010 and 2011.

### *3.3.3.2 Flemish Region*

Safeguarding sound public finances was and is one of the major challenges facing the current Flemish government.

Cutting the expenditure of the Flemish public sector in general in order to create the budgetary margin for the future, to maintain a sound socio-economic fabric and restore a balanced budget from 2011 was and is one of the major challenges facing the current Flemish government.

When it took office, the government calculated that – taking account of the deterioration in revenues following the financial and economic crisis – a structural consolidation effort of over € 2 billion spread over the period 2009-2011 was needed; in that scenario, the deficit would come to € 1 billion in 2009, and € 500 million in 2010, with a balanced budget in 2011.

Immediately on taking office (July 2009), the government passed a safeguard measure: use of expenditure and commitments was limited to a maximum of 8/12. This measure was relaxed at the beginning of September (10/12) and October 2009 (11/12), then abolished at the end of October.

At the end of October 2009, the budget documents (2009 budget audit and compilation of the 2010 budget) were in fact submitted to parliament.

The recommended target – a balanced budget in 2011 – has since been achieved. From 2011 onwards, the Flemish budget will be in balance.

In 2010, the following savings were achieved:

- selective allocation of the index provision: € 100 million;
- zero indexation of non wage-linked appropriations in 2009 and 2010: € 120 million;
- increased efficiency of the administrative system (2.5 % on the wage element and 5 % on the operating element): € 133 million;
- efficiency gain on optional subsidies (5 %): € 45 million;
- saving on regulated subsidies (2 %): € 28 million;
- communication and consultancy budgets (-20 %): € 8.5 million;
- more selective application of the flat-rate reduction in payroll tax: € 635 million;
- specific measures (e.g. Hermes Fund, cabinet appropriations, re-assessment of the interest rate, increase in Mina Fund revenues, extension of the Aquafin depreciation period, slowing of wage indexation, etc.): € 150 million;
- a small number of specific measures: sale of VMM land: € 125 million, activation of existing reserves of the VMSW and the Woningfonds : € 95 million.

In order to achieve the balanced budget recommended for 2011, the first step was to make the savings agreed when the government was formed.

- zero indexation of non wage-linked credits in 2011 ;
- additional saving on appropriations for the administrative system amounting to 1.5 % on the wage element and 2.5 % on the operating element;
- additional 5% saving on optional subsidies;



- additional 2% saving on other subsidies, except for certain social and welfare sectors such as care of the disabled, crèches, youth welfare, home care, sheltered workshops and rent subsidies;
- additional 10% saving on communication and consultancy appropriations.

In addition, a number of specific savings were also achieved totalling € 376 million.

There was no saving on investments.

Moreover, in 2011 under-utilisation was drastically reduced to € 120 million, so that the 2011 budget is realistic and the recommended budget balance will be achieved.

Thanks to the sustained economy measures and a number of positive developments on the revenue side, it was possible to take new policy measures in 2010 and 2011 to strengthen the socio-economic fabric.

The savings are not an end in themselves. They are necessary to safeguard the future. When the government was formed, a growth path was defined in regard to the policy to be adopted.

In 2010 : € 77.5 million

In 2011 : € 150 million, in order to arrive at a figure of € 1 billion or 1.4 billion by the end of the parliament, depending on the economic situation.

The following additional expenditure could already be granted in 2010:

- € 22.5 millions provision for the employment plan;
- an extra € 10 million for crèches;
- an extra € 22.5 million for the disabled sector;
- an extra € 22.5 million for investments.

The new policy launched in 2010 was continued and reinforced in 2011 :

- new social policy (crèches): increase of € 10 million to € 20 million;

- care of the disabled (clearing of waiting lists) /welfare: increase of € 45 million to € 67.5 million;
- employment and investment plan: increase of € 7.5 million to € 30 million;
- housing: € 12.9 million;
- foreign policy/tourism: € 4.1 million;
- agriculture/rural environment: € 3.8 million;
- economy/taxation (mileage levy): € 2.6 million;
- Flemish periphery: € 0.6 million;
- culture : € 0.9 million;
- investments : € 7.5 million.

In terms of capital participations, the budget figure is € 310 million. In addition to this, there is a figure of € 10 million for capital stakes in “IMEC” and “Vlaams Instituut voor Biotechnologie”.

In the coming years, the following increases have been agreed on the expenditure side:

2011: € 150 million; 2012: € 350 million; 2013: € 600 million and 2014: € 1 billion(€ 1.4 billion).

In addition, over the whole of the parliamentary term, € 800 million is earmarked for capital investments.

During the current 2011 budget audit, the strategy outlined above will be maintained. Positive developments on the expenditure side in the wake of stronger GDP growth (2 % instead of 1.7 %) and higher inflation (2.7 % instead of 2 %) will be largely used to form essential provisions and to honour past commitments, and thus to continue creating a budget buffer.

The Flemish budget is sound for the following reasons:

- realistic estimate of the payment appropriations required and formation of the necessary provisions;

- small increase in the debt (€ 345 million in 2010, € 133 million in 2011) and, from 2011, implicit reduction in the debt;
- reduction in the estimated under-utilisation in the budgets, cutting it from € 456 million in 2010 to € 120 million in the 2011 budget.

In the years ahead, a rigorous fiscal policy will be maintained. The balanced multi-annual budget for 2011-2014, submitted to the Flemish parliament on 30 April 2010, will be updated with that in mind so that, in the years 2012-2014, the Flemish budget will continue to be in structural balance.”

### *3.3.3.3 Brussels Capital Region*

“The 2010 budget was compiled on the basis of a target deficit of € 312,509,000. In that regard, a 13% saving in relation to 2009 had been recommended, to be achieved in particular (but not solely) on “reducible” - non-organic – expenditure; alternative funding of € 55 million in favour of the STIB/MIVB [urban public transport] investment programme had been devised via the Beliris Fund, and debt management had been improved in order to save € 10 million on the interest.

Finally, the provisional execution of the 2010 budget results in a deficit in ESA terms of €259,849,296 (down by € 52,659,704).

From a socio-economic angle, the Brussels Capital Region faces the following priority challenges. It needs to respond to the population explosion (population up by almost 10 % between 2004 and 2010), the high unemployment rate, mainly in the case of the low-skilled, and the impoverishment of its residents. Nonetheless, the target set in compiling the 2011 budget was the same as in 2010. In that regard, the additional expenditure in relation to 2009 was best offset on the basis of the principle of no change of policy, except for statutory obligations and the indexations laid down by law. The priority was to reduce the outstanding amount, an implicit debt.

The government also undertook to continue limiting this deficit given correct financing of the Brussels Capital Region. The Region’s resources must be sufficient not only to be able to

offer its residents a legitimate policy, but also to finance the services offered by the Region to the entire Belgian and European population.

The multi-annual budget is therefore heavily dependent on the annual refinancing of the Region. The multi-annual path is therefore provisional and indicative, in view of the uncertain institutional context. That path will change radically according to the talks being conducted at federal level concerning the adaptation of the Special Finance Law and the correct financing of Brussels, which implies that – depending on the changes made – the path in question may be adjusted in a positive or a negative sense.

**Table 14: Financing balance of the Brussels Capital Region**

<i>In € million</i>	2011	2012	2013	2014	2015	2016
Financing balance of the Brussels Capital Region	313,0	-254,1	-172,5	-116,5	-40,9	0,0

## 4 Path for 2011–2014

In view of the absence of a government with a full mandate, the caretaker government wanted to seek the opinion of the High Council of Finance (HCF) in order to prepare the new consolidation path for Belgium's public finances. The HCF issued an opinion to the federal government on 16 March 2011.

This being a caretaker government, the new path proposed in this stability programme by the Belgian government is based on the recommendations which the High Council of Finance - a body in which the federated entities have equal representation – set out in its latest opinion.

Since then, it is true that new information has become available, in particular the actual figures for public finances in 2010. The path proposed can therefore be considered prudent. The next fully mandated government will be able to update it.

### ***4.1 Medium-term path of Belgian public finances in accordance with the European recommendations***

Under the January 2010 stability programme, Belgium was to satisfy the conditions for ending the excessive deficit procedure in 2012. The Belgian government also undertook to restore Belgium's public finances to balance in 2015.

Meanwhile, the macroeconomic outlook has improved considerably in the short term, so that the 2010 deficit has contracted significantly, as already stated.

In that context, the Belgian government decided to update the budget path originally planned in order to speed up the reduction of the public deficit.

This new fiscal consolidation path for Belgian public finances in the short and medium term is still anchored around two key dates:

- in 2012, Belgium aims to secure release from the excessive deficit procedure, by setting a target of -2.8 % of GDP, compared to -3.0 % of GDP in the January 2010 stability programme;

- in 2015, the Belgian government now aims to form a surplus of 0.2 % (structural balance) to move towards the medium-term objective (MTO).

**Table 15: Target financing balance of general government**

<i>In % of GDP</i>	2009	2010	2011	2012	2013	2014
2009-2012 stability programme (January 2010)	-6,0	-4,8	-4,1	-3,0	-2,0	-1,0
2011-2014 stability programme (April 2011)	-5,9	-4,1	-3,6	-2,8	-1,8	-0,8
Difference	0,1	0,7	0,5	0,2	0,2	0,2

The new targets defined by the Belgian government thus provide for an improvement in the general government primary balance of +1.0 % of GDP in 2012, +0.9 % of GDP in 2013, and +1.0 % in 2014, i.e. a cumulative improvement of 2.9 % over the period 2012-2014 (see table 28).

In view of its caretaker status and the establishment of the Monitoring Committee, the federal government is expecting the latter to keep a close eye on Entity I's revenue and expenditure. The federated entities conduct budget audits at regular intervals in order to ensure that their respective budget targets are actually achieved.

The Belgian government is committed to speeding up the deficit reduction in the event of more favourable developments in the macroeconomic environment. Moreover, if the government were to see early redemption of its stakes in the financial sector before 2015, with possible capital gains, the whole of those amounts would be allocated to quicker debt reduction.

The government considers that this path corresponds to the recommendations of the European Council in that it provides for Belgian public finances to return to conformity with the Stability and Growth Pact by no later than 2012, and the efforts are spread evenly over the whole period.

## 4.2 Allocation of the effort between the entities

In an institutional structure like Belgium, where many powers and financial resources are decentralised, it is important to determine the optimum allocation of the fiscal consolidation effort. Furthermore, that is a requirement stipulated by the European Commission.

However, in the current political context with a caretaker government and institutional negotiations aimed, in particular, at reforming the financial flows between the federal State and the federated entities<sup>5</sup>, the federal government cannot decide on the allocation of the effort between the levels of power. By way of indication, it has to be content with referring to the recommendations of the High Council of Finance on the subject. The allocation formula proposed by the latter corresponds to the respective share of each entity in the total primary expenditure of general government, namely 65 % and 35 % respectively for Entity I and Entity II.

**Table 16: Target financing balance per entity proposed by the High Council of Finance**

In % of GDP	2010	2011	2012	2013	2014
General government	-4,6	-3,7	-2,8	-1,8	-0,8
Entity I	-3,4	-3,2	-2,5	-2,0	-1,6
Entity II	-1,1	-0,5	-0,4	0,2	0,8

Source : High Council of Finance (2011)

For the period 2011-2012, the allocation of the effort proposed by the High Council of Finance corresponds to the targets which the federated entities set themselves in their respective multi-annual budgets.

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- <sup>5</sup> In these negotiations, the Brussels Capital Region is the subject of particular attention because it has found that there is structural under-funding.

For 2013, the HCF advocates an additional effort of 0.1 % compared to the path planned by the federated entities, which should be made possible by the extra financial resources which that level of power will receive from the federal government under the Special Finance Law, following the improvement in the economic parameters, resources which the federated entities have not yet taken fully into account.

From 2014 onwards, the allocation of the effort relating to the consolidation of public finances recommended by the HCF gives rise to an increasingly asymmetric path, in that Entity I could be satisfied with a deficit of 1.6 % of GDP while Entity II would have to accumulate budget surpluses amounting to 0.8 % of GDP in 2014. The HCF states that this asymmetry does not in any way reflect a divergence in the fiscal policy stance of the different levels of power; it is due simply to the fact that 90 % of the ageing costs and 100 % of the interest charges on the historical public debt are charged to Entity I.

According to the HCF, this apparent asymmetry in the actual expected budget paths is far from ideal. It considers that the sustainable consolidation of public finances requires a reform of the current funding flows and the institutional framework. That is one of the major issues in the current institutional negotiations. In the view of the HCF, that revision must lead to increased accountability for the different levels of power, increased fiscal sustainability for the Federal State – which bears the bulk of the charges on the public debt – and sustainable convergence of budget balances.



Regarding local authorities, the September 2009 cooperation agreement between the Federal State and the Regions (supervisory power) ultimately provided for strict adherence to the ESA 95 accounting standards. That agreement was first implemented in the NAI's revision of the local authority accounts (see Focus pp. 14-15). These new harmonised statistics should enable the Regions to improve the exercise of their supervision over local authorities. Thus, in line with the 2009 cooperation agreement, the Flemish government recently approved the "golden rule" providing for structural equilibrium of the local authority accounts over the whole of the local government's term (so as to take account of the entire local authority investment cycle).

Regarding the Walloon Region, Article L1314-1 of the Code of Local Democracy and Decentralisation mentions that the local authority expenditure and revenue budget must never record an ordinary or extraordinary balance in deficit, nor a fictitious equilibrium or surplus. Considering the investment cycle, that rule should result in ESA equilibrium on a multi-annual basis.

Regarding the Brussels Capital Region, Article 252 of the New Municipal Law stipulates that the budgets and accounts must be in equilibrium for both ordinary and extraordinary transactions. That equilibrium is strictly observed by the local authorities with the aid of the Brussels Capital Region which, in agreement with the Federal State, injects € 30 million each year to cover the local authority deficits in order to neutralise that operation. This fiscal principle and the Region's aid should enable the local authorities to move towards equilibrium over the local government legislative term".

#### ***4.3 Structural reduction in the public deficit in accordance with the European recommendations***

In the excessive deficit procedure, the European Council recommends the Belgian government to effect an average annual reduction of 0.75 % of GDP over the period 2010-2012.

The proposed path provides for a cumulative structural improvement in the financing balance of 1.5 % over the period 2010-2012.

It is important to note that, for the year 2012, non-structural factors will affect the financing balance, although the European Commission's methodology does not take them into account as temporary factors. This concerns in particular:

- the effect of relative prices, which have an adverse impact on public finances in 2012 in view of the acceleration of inflation in 2011; these delayed inflation effects are evident mainly at the level of public expenditure and social benefits, and in personal income tax revenues on account of the delayed indexation of the tax scales;
- the effect of the local authority electoral cycle, amounting to 0.2 % to 0.3 % of GDP; this factor mainly affects investment at that level of power.

Moreover, so long as economic growth hovers around the potential growth rate, the government is firmly committed to fulfilling the conditions for ending the excessive deficit procedure in 2012.

Over the period 2013-2014, the structural improvement in the financing balance should be 1.4% , in accordance with the European Council's stipulations.

**Table 17: Components of the structural financing balance**

% of GDP	2009	2010	2011	2012	2013	2014
1. Real GDP growth	-2,8	2,1	2,0	2,3	2,1	2,3
2. Net lending of general government	-6,0	-4,1	-3,6	-2,8	-1,8	-0,8
3. Interest expenditure	3,6	3,4	3,5	3,6	3,7	3,7
4. One-off and other temporary measures	-0,9	-0,1	0,0	-0,1	0,0	0,0
5. Potential GDP growth	1,4	1,5	1,6	1,6	1,7	1,8
contributions:						
- labour	0,5	0,5	0,5	0,4	0,4	0,4
- capital	0,3	0,3	0,4	0,5	0,4	0,5
- total factor productivity	0,5	0,5	0,6	0,7	0,8	0,8
6. Output gap	-3,1	-2,7	-2,2	-1,6	-1,2	-0,6
7. Cyclical budgetary component	-1,7	-1,4	-1,2	-0,8	-0,6	-0,3
8. Cyclically-adjusted balance (2 - 7)	-4,3	-2,7	-2,4	-2,0	-1,2	-0,5
9. Cyclically-adjusted primary balance (8 + 3)	-0,7	0,7	1,1	1,6	2,5	3,2
10. Structural balance (8 - 4)	-3,4	-2,6	-2,4	-1,9	-1,2	-0,5

The structural component of the financing balance is based on average potential growth estimated at 1.6 % over the period 2010-2012 and 1.8 % over the period 2013-2015. Note that this macroeconomic variable is still below the potential growth observed before the financial crisis, fluctuating around 2 %. In fact, the financial crisis has had a lasting impact on potential growth, particularly via a decline in the capital stock and an increase in structural unemployment, which tends to be reflected in a loss of human capital.

However, these estimates are highly uncertain, notably because of the potential impact of the economic and financial crisis on the potential growth of the economy. Also, the extent to which the decline in potential growth due to the financial crisis and population ageing will be structural and therefore permanent depends on the economic policy measures implemented now and in the future by the various levels of power. In that context, the Belgian government aims to achieve a sustainable increase in the employment rate and at the same time to step up the measures designed to encourage R&D expenditure under the EU2020 strategy (see national reform programme). These measures should provide sustainable support for the potential growth of the Belgian economy.

Furthermore, the Belgian government is adhering to its aim of converging as quickly as possible towards the MTO, set at 0.5 %, and thus to prefinance part of the cost of ageing. The MTO is therefore not confined to simply restoring the structural balance of public finances but also means recording structural surpluses. In fact, the Belgian government considers that it is vital to ensure that the costs of ageing are shared fairly between the generations in order to prevent future generations from having to bear a disproportionate financial burden.

#### ***4.4 Progressive reduction in the public debt consistent with the draft European directives***

Following a substantial fall of 29.5 % of GDP over the period 1999-2007, the public debt ratio increased sharply to 96.8 % in 2010, compared to 84.2 % in 2007, thus halting what had been a continuous decline since 1993. Apart from the endogenous rise in the public debt ratio in the context of a fall in gross domestic product and a significant deterioration in public finances in the wake of the economic crisis, the increase in the debt is also due to the size of the exogenous factors determining the movement in the debt in connection with the interventions in the financial sector, essential to restore the sector's stability. The contribution of these factors to the expansion of the debt comes to 6.3 % of GDP.

In view of the high debt ratio and, hence, the vulnerability of the Belgian economy to sudden interest rate movements, the Belgian government aims to stabilise the public debt ratio as quickly as possible. Taking account of the impact of certain operations to assist Greece and

Ireland under the European support system, it is important to reduce the endogenous debt ratio first, and then to start reducing the overall public debt ratio.

In the coming years, and taking account of the assumptions made, the endogenous debt ratio should stabilise in 2011, taking account of a minimum target for the deficit of -3.6 % of GDP. However, the overall debt is expected to continue rising, owing to the 2<sup>nd</sup> tranche of the loan to Greece of € 1.28 billion (or 0.35 % of GDP), in accordance with the commitments given by Belgium under the support mechanism for that country, and owing to the aid to Ireland amounting to € 607 million, or 0.16 % of GDP.

By 2012, the general government debt ratio, according to the EDP definition, should begin to fall, given that the level of the effective primary balance is higher than the primary balance required to stabilise the public debt. In 2015, the public debt should thus subside below the 90 % mark to approach the level recorded in 2007, with a debt ratio of 88.4 %<sup>6</sup>.

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<sup>6</sup>For the time being, the Debt Agency is not planning any interest rate swaps like those in 2009 and 2010, in view of the fact that the aim of lengthening the maturity of the debt securities portfolio will be achieved in the normal way with the programme for the issue of long-term securities. In the event of persistent inflationary pressure, the Treasury could nevertheless make provision for *payers swaps* (the Treasury pays a fixed interest rate and receives a floating rate) in order to limit the market risk (risk of interest rate adjustments). *Mutatis mutandis*, if a recession is looming, it can conclude swaps, as it did in the first half of 2009. However, those positions have since been liquidated.

**Table 18: Debt ratio**

<i>% of GDP</i>	2010	2011	2012	2013	2014
1. Gross debt	96,8	97,5	96,5	95,1	92,2
2. Change in gross debt ratio	0,6	0,7	-1,0	-1,4	-2,9
	Contributions to changes in gross debt				
3. Primary balance	-0,7	0,1	0,7	1,8	2,9
4. Interest expenditure	3,4	3,5	3,6	3,7	3,6
5. Stock-flow adjustment	0,1	0,8	0,2	0,2	0,2
<i>p.m. implicit interest level</i>	3,7	3,7	3,8	3,9	4,0
<i>p.m. endogenous debt</i>	96,7	96,7	96,3	94,9	92,0

With a decline of 9.1 % in the public debt over the period 2011-2015, and therefore an annual average fall of 2.3 %, Belgium is already responding well to the future European requirements under the preventive element of the Stability and Growth Pact which, in Belgium's case, provides for a minimum annual reduction in the debt equivalent to around 2 % of GDP<sup>7</sup>.

**Table 19: Primary balance required to stabilise the endogenous debt ratio**

<i>In % of GDP</i>	2010	2011	2012	2013	2014
Required primary balance	-0,2	-0,3	-0,4	0,1	-0,2
Target primary balance	-0,7	-0,1	0,7	1,8	2,9

It should be noted that this movement in the public debt is consistent with the objectives previously defined in terms of the financing balance, and is based on the absence of any repayment by the financial institutions over the period 2011-2014. In the light of the commitment made by the Belgian government concerning the allocation of any reductions in its stake in the financial sector, repayment by certain financial institutions during the period 2011-2014 would mean a corresponding reduction in the Belgian public debt.

Against the backdrop of the financial crisis, the Belgian government granted guarantees to the financial sector to ensure that the sector functioned normally. Unlike capital investments and loans, those guarantees have no impact on the consolidated gross debt since they are considered in the national accounts as contingent liabilities and are recorded off the balance

<sup>7</sup> Minimum reduction of 1/20 of the difference between the public debt and 60 % of GDP. For Belgium, the figures are therefore  $(96.8\% - 60\%) / 20 = 1.8\%$  of GDP

sheet. Those guarantees totalling € 55.7 billion at the end of 2010, against € 92.4 billion in 2009, constitute a maximum theoretical risk. For 2011, those guarantees should amount to € 41.2 billion, or 11% of GDP. Up to now, there has been no need to activate any of the guarantees. In order to control this risk, the movement in the various underlying assets covered by guarantees is constantly monitored and checked by the Monitoring Committee.

**Table 20: Actual grant of guarantees to the financial sector by the federal government**

<i>In € billion</i>	End of 2010	2011 (estimate)
Dexia	26,9	14,0
FSA	5,2	5,2
Fortis Bank	3,9	3,9
RPI	4,6	4,6
KBC	15,1	13,5
<b>Total</b>	<b>55,7</b>	<b>41,2</b>
<i>in % of GDP</i>	<i>15,9 %</i>	<i>11,3 %</i>

## 5 Comparison with the 2009–2012 stability programme and sensitivity analysis

### **5.1 Consolidation speeded up compared to the previous stability programme**

The consolidation path for public finances proposed by the Belgian government under this stability programme speeds up the reduction in the deficit and the public debt.

Table 21 compares the growth assumptions and budget targets set under successive stability programmes.

As explained earlier, the government is committed to speeding up the consolidation if the environment is more favourable than expected. While economic growth was revised upwards in the short term (a cumulative figure of 0.7 % over the period 2010-2011), in view of the stronger and quicker revival in economic activity, in the medium term the outlook for growth is largely similar, hovering around 2.2 %.

The revised path means an improvement in the financing balance of 0.5 % of GDP in 2011 and 0.2 % over the period 2012-2014 compared to the previous stability programme.

This revision of the budget targets is also reflected in a quicker reduction in the public debt ratio, which should be down to 92.2 % of GDP in 2014, compared to 96.2 % under the previous stability programme. This faster reduction and the formation of budget surpluses in the medium term is essential not only to reassure the markets but above all in the context of population ageing.



**Table 21: Comparison between the current stability programme and the January 2010 programme**

<i>% of GDP</i> (in comparison with the 2010 stability programme)	2010	2011	2012	2013	2014
<b>Real GDP growth</b>					
Previous update	1,7	1,7	2,2	2,1	2,2
Current update	2,1	2,0	2,3	2,1	2,3
Difference	0,4	0,3	0,1	0,0	0,1
<b>General government net lending</b>					
Previous update	-4,8	-4,1	-3,0	-2,0	-1,0
Current update	-4,1	-3,6	-2,8	-1,8	-0,8
Difference	0,7	0,5	0,2	0,2	0,2
<b>General government gross debt</b>					
Previous update	100,6	101,4	100,6	98,6	96,2
Current update	96,8	97,5	96,5	95,1	92,2
Difference	-3,8	-3,9	-4,1	-3,5	-4,0

## **5.2 Sensitivity analysis**

As already stated, the economic outlook remains uncertain in a context of a steep rise in oil prices and the ever-present risk of contagion concerning the sovereign crisis in the euro area.

In this context, in accordance with the code of conduct, it is important to conduct sensitivity analyses on the macroeconomic parameters for the path laid down in this stability programme.

### **5.2.1 Deviations in terms of GDP growth**

Three alternative scenarios are examined. The first two correspond to a deterioration in the economic environment over the 2011-2014 horizon. The first scenario assumes that economic growth slows by 0.5 percentage point per annum, or a cumulative 2 % over the period considered. The second scenario examines the effects of a sharper fall in economic growth amounting to 1 percentage point per annum. In contrast, the last scenario assumes that GDP growth over the period 2011-2014 is 0.5 percentage point higher than in the scenario used for the stability programme. However, in view of the risks facing the economy, the government considers that alternative scenario to be less likely.

In this connection, it should be noted that the elasticity of public finances to GDP is assumed to be constant (namely 0.54, i.e. 0.47 for revenue and 0.07 for expenditure).

**Table 22: Sensitivity of the financing balance to growth variations**

<i>In % of GDP</i>	2011	2012	2013	2014
<b>Stability programme</b>				
Real GDP growth	2,0	2,3	2,1	2,3
Financing balance	-3,6	-2,8	-1,8	-0,8
<b>Negative variation of 0.5 percentage point</b>				
Real GDP growth	1,5	1,8	1,6	1,8
Financing balance	-3,9	-3,3	-2,6	-1,9
<b>Negative variation of 1 percentage point</b>				
Real GDP growth	1,0	1,3	1,1	1,3
Financing balance	-4,1	-3,9	-3,4	-3,0
<b>Positive variation of 0.5 percentage point</b>				
Real GDP growth	2,5	2,8	2,6	2,8
Financing balance	-3,3	-2,3	-1,0	0,3

In the first two scenarios the analysis indicates an increase in the deficit of around 1.1 % and 2.2 % of GDP in 2014, depending on the scale of the economic slowdown. That increase in the deficit is due partly to a decline in revenues, taking account of the fall in consumption and investment and the deterioration in the labour market, and partly to a rise in expenditure, particularly at the level of unemployment benefits. So long as economic growth hovers around the potential growth rate (first sensitivity scenario), the government is firmly committed to fulfilling the conditions for ending the excessive deficit procedure in 2012.

Conversely, if the years ahead bring growth which is systematically 0.5 basis points higher than the estimates, and if the automatic stabilisers are allowed to operate, a surplus of 0.3 % of GDP would be recorded by 2014 (instead of a deficit of 0.8 %). If growth were to exceed the forecasts, the federal government is firmly committed to allowing the automatic stabilisers to operate and to using that surplus to speed up the reduction of the public debt.

### **5.2.2 Deviations in terms of interest rates**

In the current economic environment, and in view of the vulnerability of public finances to interest rates, it is essential to analyse the sensitivity of the public debt to interest rates.

A rise in market interest rates affects public finances via various channels. First, that increase should have a direct impact on interest charges, in view of the continuous need for refinancing, and that would cause a direct deterioration in the balance. Moreover, a rise in interest rates also exerts an adverse influence on economic activity (consumption and investment) via the conventional interest rate channel, and indirectly on the balance of public finances. In addition, depending on the nature of the interest rate rise (short or long term), financial institutions could see their profitability decline (increase) in a context of flattening (rising) of the yield curve.

If both short- and long-term interest rates were to rise by 100 basis points from 1 March over the entire period 2011-2014, the impact on the federal public debt interest charges (over 90 %), taking account of the average maturity of the debt, is estimated at: +€0.41 billion in 2011 (0.11 % of GDP) and + €1.75 billion in 2014 (0.43 % of GDP).

**Table 23: Sensitivity of interest charges to a 100 basis point increase in the interest rate on the federal debt**

<i>In % of GDP</i>	2011	2012	2013	2014
Difference in interest charges compared to the scenario described	0,11	0,28	0,38	0,43

That effect on the financing balance only concerns the direct effect of an increase in interest rates on the financing balance. The potential indirect effect on the economy and public finances of an increase in interest rates is not included in this sensitivity analysis.

### 5.2.3 Oil price fluctuation

In view of the nervousness of the petroleum product markets resulting from the tense political situation in certain North African countries, and taking account of the Belgian economy's relatively high sensitivity to energy price fluctuations, we considered it essential to analyse the impact of a steeper rise in energy prices on the Belgian economy and public finances.

The sensitivity analysis considers a doubling of energy prices. This change in the external environment is reflected in adjustments to import prices and global export prices.

**Table 24: Impact of a doubling of the crude oil price per barrel**

<i>% difference compared to the baseline scenario with no oil shock</i>	t	t+1	t+2	t+3	t+4
Potential export market	-1,4	-2,22	-2,81	-3,21	-3,48
Global import prices	9,14	10,06	11,44	11,87	12,09
Global export prices	3,05	4,11	4,83	5,11	5,16

Source : Federal Planning Bureau

The impact of such a rise in energy commodity prices could trigger a steep increase in the prices of intermediate consumption and private consumption, amounting to 4.2 % in t + 1 and 6.7 % in t + 4. That higher inflation would lead to a reduction in producers' profit margins – and hence corporate profitability and investment – and a decline in purchasing power and consumption. The effect on GDP growth compared to the baseline scenario would be relatively considerable, in view of the Belgian economy's dependence on energy, at -0.44 % after one year and -1.1 % after 4 years.

Such a shock would have a very adverse impact on public finances. After one year, the financing balance would deteriorate by almost 2 % of GDP, and nearly 3.1 % of GDP after 4 years. That deterioration would be due partly to the decline in tax revenues in the short term, in a context of lower activity and employment. However, in the medium term revenues would be slightly higher than in the baseline scenario, owing to the rise in prices and wages (increase in indirect revenues and social contributions). Also, expenditure would be up as a result of the rise in wages and social benefits following indexation. Moreover, the deterioration of the jobs market would drive up unemployment expenditure, while the increase in the deficit would lead to higher interest charges.

**Table 25: Impact of a doubling of the price of crude oil per barrel**

<i>Difference in % compared to the baseline scenario</i>	t+1	t+2	t+3	t+4
GDP	-0,4	-0,7	-0,9	-1,1
Consumer prices	4,2	5,2	6,0	6,7
Health index	3,4	4,4	5,1	5,7
Total employment (in %)	-0,4	-0,7	-0,8	-1,0
Total unemployment	2,5	4,0	5,3	6,3
Unit labour costs	2,3	2,8	3,0	2,9
Financing balance (in % of GDP)	-1,9	-2,3	-2,7	-3,1

## 6 Sustainability of public finances

### 6.1 Introduction

Like most west European countries, Belgium faces major changes in terms of the age structure of its population, mainly owing to the decline in the birth rate and the considerable increase in life expectancy. In the future, a smaller active percentage of the population will have to fund social benefits for a growing number of inactive persons. Apart from pensions, there will be a particularly large increase in health care costs.

Owing to the economic crisis, the policies pursued in 2009 and 2010 focused primarily on the short-term issues. However, the sustainability of public finances in the medium and long term is very important, and presents a considerable challenge for the future. The issue of population ageing must be at the centre of the priorities set by the different levels of power. The procedure provided for by the Law of 5 September 2001 guaranteeing a continuous reduction in the public debt and the creation of an Ageing Fund offers a safeguard here. It in fact provides that the Study Committee on Ageing will publish an annual estimate of the cost of population ageing, and that the government will explain its policy on the subject.

### 6.2 Budgetary consequences of ageing

#### 6.2.1 Estimates of the Study Committee on Ageing

The latest report by the Study Committee dates from June 2010<sup>8</sup>. It calculates the overall budgetary cost of ageing, a concept defined as the variation in total social expenditure over a given period. In the Study Committee's reference scenario (projecting annual productivity growth of 1.5 % and a structural unemployment rate of 8 % in the long term), total social expenditure increases by 6.3 % of GDP between 2009 and 2060. 4.7 percentage points of that

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- <sup>8</sup> High Council of Finance, Study Committee on Ageing, *Annual Report*, June 2010.

increase can be attributed to the growth of expenditure on pensions (rising from 9.7 % to 14.4 % of GDP), and 3.6 percentage points to the rise in health care costs. Under the assumptions applied, unemployment expenditure would decline by 1.1 % of GDP (from 2.3 % to 1.2 % of GDP). The cost of family allowances is also assumed to fall, namely by 0.4 percentage point of GDP between 2009 and 2060 (from 1.7 % to 1.3 % of GDP).

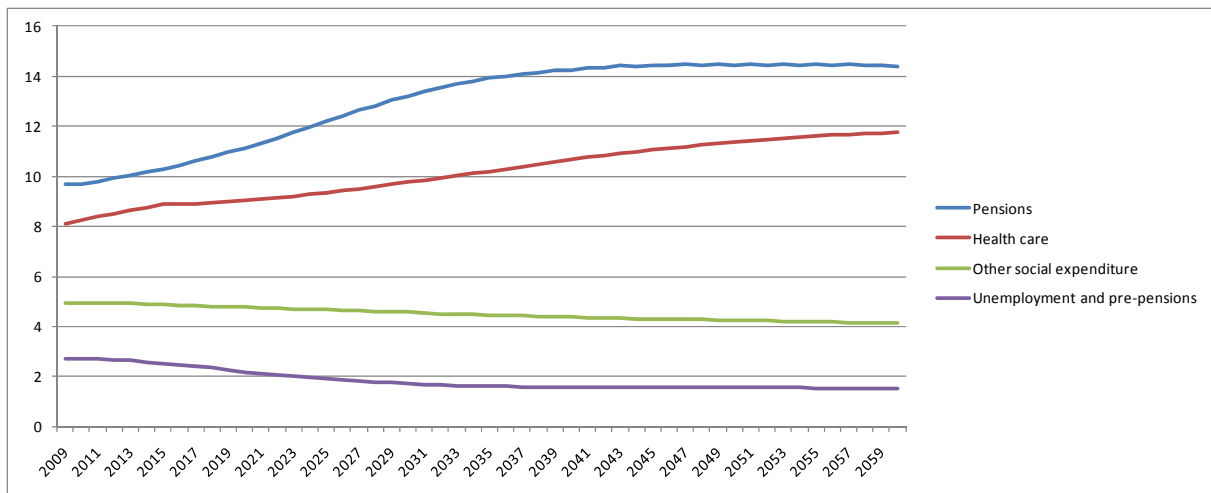
Total social expenditure would come to 31.8 % of GDP in 2060 compared to 25.5 % in 2009, or 0.1 percentage point more than the estimate in the previous report concerning the same period. However, it should be noted that, in the previous report, the budgetary cost of ageing came to 8.2 % of GDP over the period 2008-2060. That percentage included a very large rise in social spending as a ratio of GDP in 2009. A major factor here was the economic and financial crisis which, in 2009, led to a substantial fall in GDP compared to 2008.

In the medium term, from 2009 to 2015, the budgetary cost of ageing is set to rise by 1.1 % of GDP, of which 0.6 percentage point is attributable to pensions and 0.8 percentage point to health care costs. Unemployment costs will decline from 2.3 % of GDP to 2.1 % of GDP.

**Table 26: Budgetary consequences of ageing**

Components of the budgetary cost of ageing (% of GDP)	2009	2015	2030	2060	2009-2015	2015-2060	2009-2060
Pensions	9,7	10,3	13,2	14,4	0,6	4,1	4,7
Employees	5,4	5,8	7,5	8,2	0,4	2,5	2,9
Self-employed	0,8	0,8	1,0	0,9	0,0	0,1	0,1
Public sector	3,5	3,7	4,7	5,2	0,2	1,5	1,7
Health care	8,1	8,9	9,8	11,7	0,8	2,9	3,6
Acute	-	7,4	8,0	8,7	-	1,3	-
Long-term	-	1,5	1,8	3,1	-	1,6	-
Incapacity	1,5	1,6	1,5	1,4	0,1	-0,2	-0,1
Unemployment	2,3	2,1	1,4	1,2	-0,2	-0,9	-1,1
Early retirement	0,4	0,4	0,3	0,3	0,0	-0,1	-0,1
Family allowances	1,7	1,6	1,5	1,3	-0,1	-0,3	-0,4
Other social security expenditure	1,8	1,7	1,6	1,5	-0,1	-0,2	-0,3
<b>Total</b>	<b>25,5</b>	<b>26,6</b>	<b>29,2</b>	<b>31,8</b>	<b>1,1</b>	<b>5,2</b>	<b>6,3</b>
<i>p.m. Remuneration of teaching staff</i>	4,3	4,1	4,1	4,0	-0,2	-0,1	-0,3

**Chart 5: Expected trend in social benefits (in % of GDP)**



Source: Study Committee on Ageing (2010)

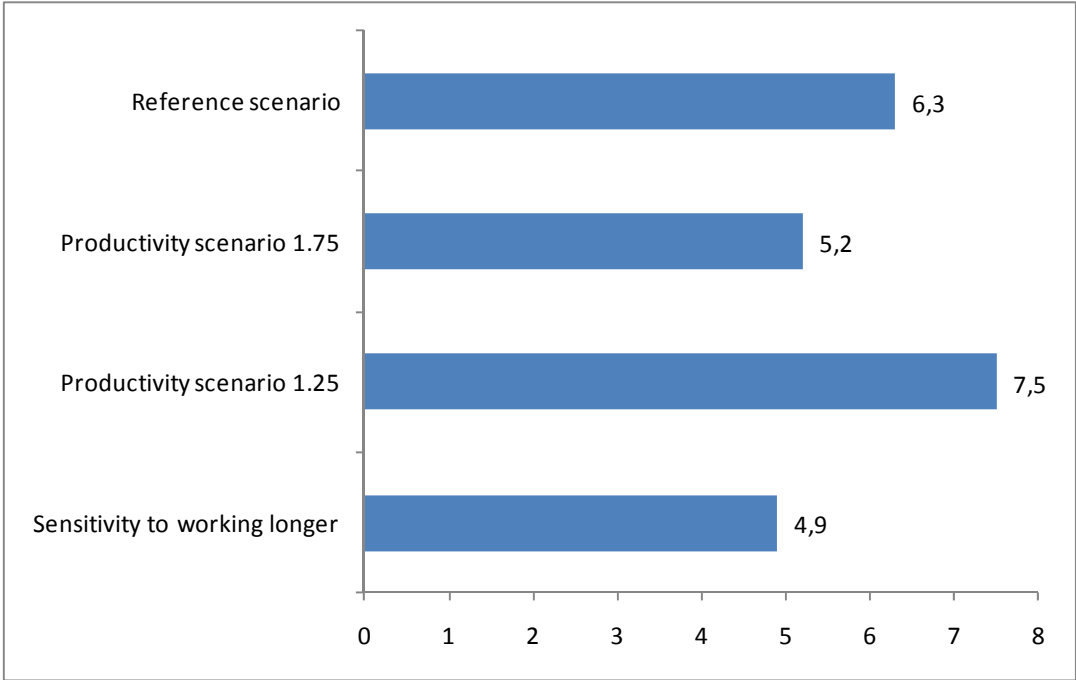
As already stated, the reference scenario used by the Study Committee is based on average annual productivity growth of 1.5 %. Since there is still considerable uncertainty in the wake of the crisis, the Study Committee decided to calculate 2 alternative scenarios, as it did last year, namely a scenario with stronger productivity growth (1.75 % per annum) and a scenario with weaker productivity growth (1.25 % per annum).

In the scenario with weaker productivity growth (averaging 1.25 % per annum from 2015), social expenditure increases and the economic basis contracts, the result being that between 2009 and 2060 the budgetary cost of ageing is 1.2 percentage points higher than in the reference scenario, equivalent to an overall budgetary cost of 7.5 % of GDP. The rise in expenditure as a percentage of GDP is seen mainly at the level of employees' pensions, given that they are calculated over a full career and therefore only gradually feel the influence of weaker productivity growth. The opposite is true in the scenario which assumes stronger productivity growth in the long term, namely 1.75 %, where the budgetary cost of ageing would be 1.1 percentage points lower (corresponding to a budgetary cost of 5.2 % of GDP), once again owing to the impact of employees' pensions.



In the reference scenario, the effective age of departure from the labour market increases by two years over the period considered, from 59.7 years in 2008 to 61.7 years in 2060. The Study Committee proposes a sensitivity analysis based on a bigger increase, namely one additional year compared to the reference scenario, i.e. an increase of 3 years in the effective age of retirement of the population of working age between 2008 and 2060. In that scenario, the budgetary cost of ageing is 1.4 percentage points lower than in the reference scenario as a result of a rise in the employment rate (particularly for persons aged from 55 to 64 years) and a fall in the unemployment rate. In this alternative scenario, it is particularly the pension costs that are lower than in the reference scenario: instead of rising by 4.7 % of GDP, pension costs would increase by only 3.9 % of GDP.

**Chart 6: Sensitivity of the scenarios analysed by the Study Committee on Ageing**



Source: Study Committee on Ageing (2010)

## 6.2.2 International comparison of the sustainability of public finances

A comparison with other countries offers a perspective on the issue of population ageing in Belgium. According to a European Commission analysis, ageing-related expenditure in Belgium will rise by 6.6 % between 2010 and 2060. That puts Belgium in a second group of countries which includes Finland, the Czech Republic, Lithuania, the United Kingdom and Germany, where the cost of ageing is more moderate though still high (between 4 and 7 percentage points of GDP).

**Table 27 : Increase in ageing-related costs in the European Union**

<i>In % of GDP</i>	Pensions		Health care		Long-term care		Unemployment		Total	
	Change 2010 to 2060		Change 2010 to 2060		Change 2010 to 2060		Change 2010 to 2060		Change 2010 to 2060	
	2010	2060	2010	2060	2010	2060	2010	2060	2010	2060
Belgium	10,3	4,5	7,7	1,1	1,5	1,3	7,3	-0,3	26,8	6,6
Bulgaria	9,1	2,2	4,8	0,6	0,2	0,2	3,0	0,2	17,1	3,2
Czech Republic	7,1	4,0	6,4	2,0	0,2	0,4	3,3	0,0	17,0	6,3
Denmark	9,4	-0,2	6,0	0,9	1,8	1,5	8,0	0,1	25,2	2,2
Germany	10,2	2,5	7,6	1,6	1,0	1,4	4,6	-0,4	23,3	5,1
Estonia	6,4	-1,6	5,1	1,1	0,1	0,1	3,2	0,3	14,8	-0,1
Ireland	5,5	5,9	5,9	1,7	0,9	1,3	5,3	-0,2	17,5	8,7
Greece	11,6	12,5	5,1	1,3	1,5	2,1	3,8	0,1	21,9	16,0
Spain	8,9	6,2	5,6	1,6	0,7	0,7	4,8	-0,2	20,0	8,3
France	13,5	0,6	8,2	1,1	1,5	0,7	5,8	-0,2	29,0	2,2
Italy	14,0	-0,4	5,9	1,0	1,7	1,2	4,3	-0,2	26,0	1,6
Cyprus	6,9	10,8	2,8	0,6	0,0	0,0	5,8	-0,6	15,5	10,7
Latvia	5,1	0,0	3,5	0,5	0,4	0,5	3,3	0,3	12,3	1,3
Lithuania	6,5	4,9	4,6	1,0	0,5	0,6	3,5	-0,4	15,1	6,0
Luxembourg	8,6	15,3	5,9	1,1	1,4	2,0	4,0	-0,3	19,9	18,2
Hungary	10,5	0,6	5,8	1,3	0,3	0,4	4,5	-0,3	21,0	2,0
Malta	8,3	5,1	4,9	3,1	1,0	1,6	5,0	-0,7	19,2	9,2
Netherlands	6,5	4,0	4,9	0,9	3,5	4,6	5,6	-0,2	20,5	9,4
Austria	12,7	1,0	6,6	1,4	1,3	1,2	5,2	-0,2	25,7	3,3
Poland	10,8	-2,1	4,1	0,8	0,4	0,7	3,8	-0,6	19,1	-1,1
Portugal	11,9	1,5	7,3	1,8	0,1	0,1	5,6	-0,4	24,9	2,9
Romania	8,4	7,4	3,6	1,3	0,0	0,0	2,7	-0,2	14,7	8,5
Slovenia	10,1	8,5	6,8	1,7	1,2	1,7	5,1	0,7	23,1	12,7
Slovakia	6,6	3,6	5,2	2,1	0,2	0,4	2,9	-0,6	14,9	5,5
Finland	10,7	2,6	5,6	0,8	1,9	2,5	6,4	0,0	24,7	5,9
Sweden	9,6	-0,2	7,3	0,7	3,5	2,2	6,6	0,0	27,1	2,7
United Kingdom	6,7	2,5	7,6	1,8	0,8	0,5	4,0	0,0	19,2	4,8
European Union (EU)	10,2	2,3	6,8	1,4	1,3	1,1	4,9	-0,2	23,2	4,6
Euro area	11,2	2,7	6,8	1,3	1,4	1,3	5,0	-0,2	24,5	5,1

### **6.3 The government strategy on ageing**

For the Belgian government, population ageing is one of the major challenges of the coming decades. To meet that challenge, it has developed a strategy based on three fundamental priorities. The first is the budgetary priority, namely reducing the public debt. A second priority is economic, and concerns boosting the employment rate and encouraging economic activity. The third priority concerns the sustained development of strong social security based on solidarity.

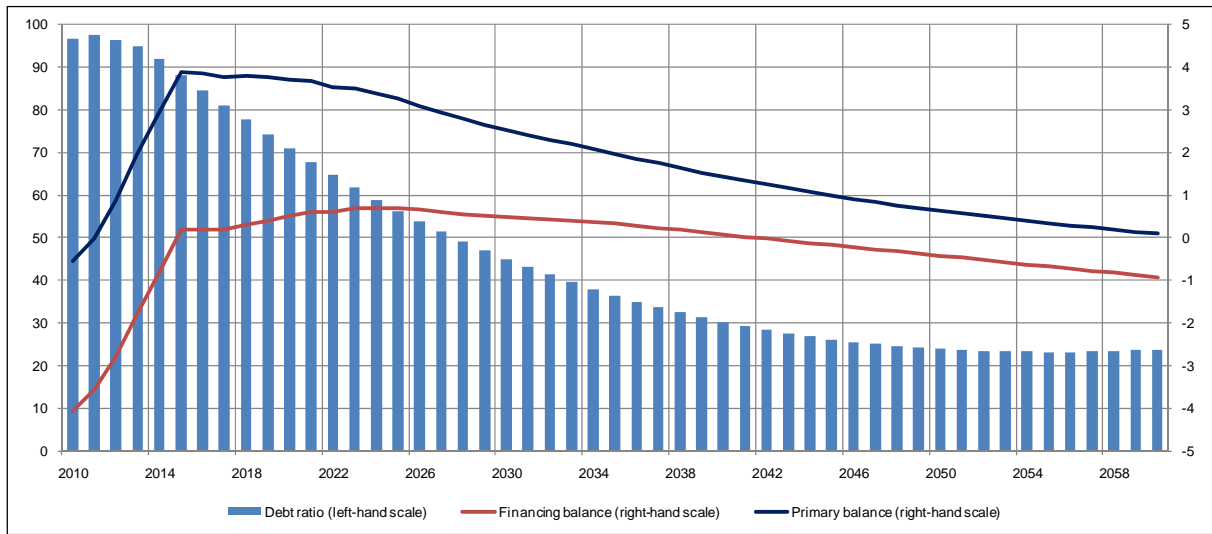
The government strategy on fiscal policy aims to ensure the sustainability<sup>9</sup> of public finances. That is why the reduction in the debt ratio, cutting future interest charges, is one of the main objectives. The scope thus created can then be used, among other things, to cope with the increased expenditure on social protection. The global financial crisis and the uncertain economic situation are the main reasons prompting the government to accord priority to supporting economic growth and maintaining consumer and business confidence.

With the particular aim of guaranteeing the long-term sustainability of public finances, this stability programme devised a path which provides for a small surplus by 2015. After that, an illustrative scenario is constructed on that basis for coping with much of the increase in the cost of ageing over the period 2015-2060 by reducing the primary balance without any excessive increase in the debt ratio. The chart below presents the essential data of that scenario, aiming at a small surplus after 2015, which will then be gradually reduced from 2025 onwards. In the long term, small deficits will be generated but without causing any unsustainable debt dynamics.

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<sup>9</sup>The “Borrowing Requirements” section defines the concept of sustainability as follows: “Sustainability must be viewed as a situation in which, given a more or less constant level of revenue, the government manages to absorb the impact of demographics on part of its expenditure, without reducing the share of other primary expenditure in GDP and without endangering the attainment of various targets for public finances.”

**Chart 7: Debt ratio, financing balance and primary balance in the long term (in % of GDP)**



## 7 Sustainable consolidation of public finances, quality of public finances and macroeconomic challenges

### 7.1 *Main points of fiscal consolidation*

The Belgian government has set itself the priority of ensuring sustainable fiscal consolidation in the coming years. That consolidation is an essential condition for supporting sustainable economic growth because, without consolidation, the increase in the deficit and the debt ratio in the context of population ageing and the return of the snowball effect would lead to a big increase in the risk premium and long-term interest rates, discouraging consumption and investment. In that context, it is essential to have a credible strategy for the consolidation of public finances aimed at reducing the public debt.

The Belgian government also considers that this effort cannot be sustained without the implementation of structural reforms in line with the objectives of the EU2020 Strategy, the Euro Plus Pact, and the recent conclusions of the European Council on 23-24 March.

On the expenditure side, the budgetary effort will focus mainly on:

- increasing the efficiency and quality of public services;
- labour market reforms designed to boost the employment rate and, in particular, the participation of target groups in the labour market, in accordance with the aims defined in the national reform programme;
- reforms aimed at increasing efficiency gains in health care while maintaining quality health care accessible to all;
- controlling certain expenditure, particularly on service vouchers and time credit;
- global reform of the pension system in order to increase the effective retirement age while maintaining an appropriate pension system; in that context, the federal government will continue to perform that task and will define the process for the adoption of decisions on reforming and strengthening the pension system. In October 2011, in order to raise the effective retirement age, Belgium will also evaluate the

policy aimed at restricting early retirement (e.g. pre-pensions) and encouraging retention in employment in the context of the measures laid down in the Generation Pact;

- reducing the complexity and increasing the transparency of the tax system;
- stepping up the measures to combat social security fraud, particularly via tighter controls and the cross-checking of databases, made possible by the investments made in recent years in that regard;
- cutting expenditure on interest charges by reducing the deficit.

On the revenue side, the measures to be taken will be analysed in a context of convergence at European level. Therefore:

- The accent will be on green taxation, which is still lagging behind the European level (in % of GDP), notably in order to encourage members of Belgian society to modify their behaviour and thus facilitate the transition to a sustainable economy.
  - The government is studying the possibility of introducing a tax on nuclear fuels. To that end, the National Bank of Belgium was asked to conduct a study analysing the appropriateness and details of such a tax.
  - The government is also studying the possibility of introducing a tax on “first class” and “business class” air tickets. Consultation with the regions is in progress on this subject.

- The emphasis will be on an appropriate contribution from the financial sector, aimed partly at compensating for the adverse effects of the financial crisis on public finances, and partly at reducing the risks taken by the sector.
- The government is of the opinion that taxes on labour will not be increased in view of their already high level.
- There will be stronger efforts to continue combating tax evasion and to improve revenue recovery.

Table 28 shows the general government financing balance to which the Belgian government is expressly committed and for which it will take the necessary measures. The breakdown from 2012 shown in the table below is purely a guide and does not in any way prejudge the actual implementation of the measures mentioned above, which will be decided by the next government.

**Table 28: General government budget outlook<sup>1</sup>**

	2010 volume (in € billion)	2010 % of GDP	2011	2012	2013	2014
<b>Net lending by sub-sector</b>						
1. General government	-14,4	-4,1	-3,6	-2,8	-1,8	-0,8
2. Central government	-10,9	-3,1	-3,1	-1,9	-1,7	
3. Communities and regions and local authorities	-3,2	-0,9	-0,5	-0,4	0,2	
4. Social security authorities	-0,3	-0,1	0,0	-0,5	-0,3	
<b>General government</b>						
5. Total revenue	172,2	48,9	49,8	49,6	49,9	49,9
6. Total expenditure	186,6	53,1	53,4	52,4	51,7	50,7
7. Net lending/borrowing	-14,4	-4,1	-3,6	-2,8	-1,8	-0,8
8. Interest expenditure (EDP)	12,0	3,4	3,5	3,6	3,7	3,6
9. Primary balance	-2,4	-0,7	-0,1	0,8	1,9	2,8
10. One-off and other temporary measures	-0,3	-0,3	-0,1	0,0	0,0	0,0
<b>Selected components of revenue</b>						
11. Total taxes	103,0	29,3	29,6	29,5	29,5	29,5
11a. Taxes on production and imports	45,5	12,9	13,0	13,0	12,9	12,9
11b. Current taxes on income, wealth, etc	55,1	15,7	15,9	15,8	15,9	15,9
11c. Capital taxes	2,5	0,7	0,7	0,7	0,7	0,7
12. Social contributions	58,1	16,6	16,7	16,7	16,8	16,8
13. Property income	3,0	0,9	1,1	1,0	1,0	1,0
14. Other	8,1	2,3	2,4	2,5	2,6	2,6
15. Total revenue	172,2	49,1	49,8	49,6	49,9	49,9
p.m. Tax burden	163,1	46,4	46,9	46,9	47,0	47,0
<b>Selected components of expenditure</b>						
16. Final consumption expenditure	58,0	16,6	16,2	15,8	15,5	15,0
17. Social payments	88,9	25,3	25,4	25,4	25,4	25,4
18. Interest expenditure	12,0	3,4	3,5	3,6	3,7	3,6
19. Subsidies	8,7	2,5	2,5	2,1	2,0	2,0
20. Gross fixed capital formation	5,9	1,7	1,9	1,9	1,7	1,7
21. Other	13,1	3,6	3,9	3,5	3,4	3,0
22. Total expenditure	186,6	53,1	53,4	52,4	51,7	50,7

<sup>1</sup> The breakdown between the federal government on the one hand, and the Communities, Regions and local authorities on the other, over the period 2013-2014 depends in particular on the results of the national reform which is under discussion.

For the period 2011-2014, the stability programme is based on the 2011 budget drawn up by the federal government on 24 March. That budget was presented to Parliament. In preparing the budget the government assumed a deficit of 4.5 % of GDP in 2010. Since then, on 31 March the NAI published its first estimates of the public deficit, indicating that the budget deficit was reduced to 4.1 % of GDP.



## 7.2 The macroeconomic challenges

The Belgian economic fundamentals are sound.

- Belgium recorded GDP growth averaging 1.6 % over the period 2000-2010, compared to 1.4 % in the euro area. The growth prospects for 2011 are also tending to exceed the average for the euro area (2 % versus 1.7 %).
- In 2010, unemployment reached 8.4 % in Belgium, a rate which was below the average for the euro area (10 %). In 2011, unemployment should decline further to 8.3%.
- In terms of external performance, Belgium does fairly well in the European context. After declining more or less to equilibrium in 2008, owing to the combined effects of the strength of domestic demand and losses on the terms of trade due to higher commodity prices, the balance of current transactions in Belgium became positive again in 2009 and is forecast to remain so in 2011. Regarding net external assets, Belgium has a net balance in excess of 50 % of GDP, well above the European average.
- As regards private sector debt, no imbalance is evident:
  - the private savings ratio (in % of disposable income) in Belgium stood at 17.2 % in 2010 ;
  - in 2010, the household debt ratio in Belgium was close to 54 % of GDP and the corporate debt ratio was in the region of 43 % of GDP<sup>10</sup>.

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- <sup>10</sup> Belgium is home to many subsidiaries of multinationals, which even base their general financial headquarters there for the rest of Europe. That therefore generates large flows of finance, capital and loans between Belgium and the rest of the world. To gain a proper understanding of the economic reality it is vital to take that into account. Thus, inter-company loans are a less important factor for assessing a country's macroeconomic stability. That is why the analysis mentioned above is based on the consolidated series of statistics published by Eurostat. Since the non-consolidated series is available for a larger number of Member States it is often used for the purpose of international comparisons. Analyses based on non-consolidated data overestimate the macroeconomic risk associated with the gross debt ratio of Belgian firms. In Belgium, the difference between the consolidated and non-consolidated data is in fact over 100 % of GDP, whereas the euro area average is 16 %.

Despite these sound fundamentals, the Belgian government is aware of certain weaknesses in the Belgian economy, particularly in relation to the labour market, the costs of ageing (see chapter 7 on the sustainability of public finances) and competitiveness.

In that context, the Belgian government is committed to making a consistent response in the coming 12 months to the 4 priorities put forward by the Heads of State and Government.

Moreover, the measures taken recently by the government already offer a partial response to those priorities.

### **7.2.1 Boosting competitiveness and employment**

On 11 February the government concluded an agreement in principle on a set of measures concerning the labour market in the biennial wage negotiations in the private sector. On 25 February the detailed texts of that agreement were presented to the Council of Ministers for a first reading. The draft law is currently before Parliament pending approval.

- The government set a wage norm for the private sector as a whole which limits real wage growth to 0.3 % over the period 2011-2012. Moreover, the wage increase will not be granted until 2012.
- Belgium has an employment protection system which distinguishes between white-collar and blue-collar workers. A start has been made on eliminating the differences in the rules on employment law between blue-collar and white-collar workers. Various measures will be phased in during 2011: redundant blue-collar workers will receive redundancy pay; white-collar workers can also be temporarily laid off by their employer if there is no work. And from 2012 the periods of notice to be given to blue-collar workers will be extended, while those applicable to highly paid white-collar workers will be reduced. In addition, a limited tax exemption will take effect in the case of remuneration and/or compensation in connection with compulsory and/or voluntary redundancy from 1 January 2012. That exemption will be up to € 600 in 2012 and 2013 and up to €1200 in 2014<sup>11</sup>.

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- <sup>11</sup> 2011 index

- Workers being paid the minimum wage will receive a net increase of € 120 per annum via a tax credit amounting to a fixed percentage of the actual reduction in personal social security contributions. In order to avoid “ tax spikes”, this reduction will be gradually tapered off for workers receiving slightly more than the minimum wage. The rule will apply from 1 April. This measure alleviates the benefit traps and thus facilitates the return to the labour market.
- The Generation Pact will be assessed before October 2011. At present, men who have worked for 37 years and women who have worked for 33 years can retire on a pre-pension. If the employment rate of the over 50s does not increase 1.5 times as fast as in the EU, the law provides that the eligibility conditions for retiring on a pre-pension will be tightened up and increased to 40 years. Conversely if the employment rate of the over 50s does increase 1.5 times as fast as in the EU, the eligibility condition will be increased to 38 years for men and 35 years for women from 2012, and 38 years from 2014.
- The system of temporary lay-offs for white-collar workers has been made permanent. In addition, the social partners have been asked to devise a mechanism whereby firms which have made excessive use of this system have to carry the responsibility.

Under the budget, an action plan was approved which aims to encourage the voluntary return to work of disabled persons:

- For those going back to work part time, levies on their benefits will be adjusted to make it easier for them to combine benefits and a return to work.

- The procedures for authorising a return to work will be simplified by abolishing prior authorisation and replacing it with retrospective authorisation.
- The financial incentive to encourage disabled persons to attend training will be stepped up.
- The quality and consistency of the medical assessment of incapacity for work will also be improved.

## *Competition & Energy Market*

- In connection with the transposition of the third Energy Directive, to be approved at the Council of Ministers on 15 April, the functioning of the energy market will be improved. Changes to the indexation formulas for gas and electricity suppliers will be subject to ex-ante control by the CREG, while price changes resulting from the formula for indexation, which will in future be permitted only every three months, will be subject to ex-post control. These measures should curb the volatility of energy prices.
- In order to cope with higher inflation, the federal government decided, in the 2011 budget, to confer additional powers on the Price Observatory to monitor the movement in prices of certain products. In that connection, the competition authority may ask the Price Observatory to conduct surveys and may use the Observatory's analyses for the purpose of its surveys on infringements of competition law.

### **7.2.2 Ensuring the sustainability of public finances**

See above (point 6).

### **7.2.3 Strengthening financial stability**

In the context of the financial crisis which spread to all financial centres and the global economy, the government wanted to reform financial supervision while also providing for legal instruments to reduce the global risk of the financial sector.

#### *Reform of supervision*

The legislature wanted to learn the lessons of the financial crisis and develop the Belgian financial supervision structure in the same direction as the reforms implemented in a number of European countries.

Thus, the legislature opted for the “Twin Peaks” supervision model. Since 1 April the supervision architecture of the financial sector has operated as follows:

- The National Bank of Belgium is responsible for maintaining the macroeconomic and microeconomic stability of the financial system. From now on, the NBB is therefore in charge of the individual prudential supervision of the financial players. It thus ensures that the financial institutions subject to its supervision are financially sound, e.g. by setting solvency, liquidity and profitability requirements for those institutions. Financial undertakings which come under the prudential supervision of the NBB will be approved by the NBB.
- The FSMA (Financial Services and Markets Authority) – formerly the CBFA (Banking, Finance and Insurance Commission) – continues to perform its traditional task of safeguarding the smooth functioning, transparency and integrity of the financial markets, and watching out for the illicit offering of financial products and services. It will also check on compliance with the code of conduct applicable to financial intermediaries in order to ensure that customers receive honest, fair and professional treatment.

The Committee for Systemic Risks and Systemic Financial Institutions, which has been responsible for supervising “systemic” institutions since the last quarter of 2010, is therefore giving way to a fundamental reform of the financial supervision architecture in Belgium.

This model presents a number of advantages, notably the avoidance of conflicts of interest between microprudential supervision and consumer protection. More fundamentally, it means that micro- and macro-prudential supervision can be brought together to combine all the relevant information for determining systemic risks in a single institution, the NBB. This institution is also the lender of last resort.

The FSMA – the former CBFA – will be given new powers concerning consumer protection and financial training.

### Strengthening the financial regulation and reinforced legal framework

Apart from these large-scale reforms the government has set up a new legal framework – in accordance with the IMF’s recommendations - enabling it to intervene in the event of a serious financial crisis threatening financial stability. In future, that framework will enable the government to effect the assignment, sale or contribution of financial undertakings concerning assets, liabilities or various branches of activity, or securities or shares issued by financial institutions, whether or not in accordance with voting rights. Also, when the State wants to make use of the powers to order the assignment of assets or securities, it will have to refer the matter to the court of first instance for the latter to verify both the legality of the act of assignment and the fairness of the proposed payment. Moreover, there is now provision for sanctions to apply in the event of the circulation of information or rumours which could give false or misleading impressions about the situation of a credit institution, insurance company or clearing house, such as to damage its financial stability.

The government has also transposed the directive on remuneration policies in the financial sector, intended to reduce the risks taken by those institutions. In particular, the new regulations provide for the creation of a remuneration committee in accordance with the European requirements on the subject, and stipulate that the payment of the variable element of remuneration must not exceed 30 % in the first year.

## **7.3 Quality of public finances**

### **7.3.1 Combating fraud**

The battle against fraud is a battle in favour of justice and fair competition. A sustained battle against tax evasion and social security fraud is also the best remedy against increases in tax and social contributions. In the past few years, the battle against fraud has not been just a balancing item but rather an effective approach accompanied by stated revenue figures.

Under the government agreement, it was decided from the start to adopt a resolute approach to combating fraud. During the previous legislative term, a State Secretary for the Coordination of Fraud Control was appointed for the first time. In order to carry out this coordination task, he can enlist the services of two new bodies set up since then: the College and the Ministerial Committee for the Control of Tax Evasion and Social Security Fraud.

The College is made of up senior officials from the social, fiscal, economic, police and judicial services involved in combating fraud. The composition of the College ensures that it can rely on the expertise and practical knowledge of the elite in the administration, police and judiciary.

The second body is the Ministerial Committee for the Control of Tax Evasion and Social Security Fraud. This comprises the Prime Minister, the State Secretary and members of the government who are involved in combating fraud on account of their particular responsibilities. It is and remains the duty of every minister to combat fraud in his own area of responsibility.

In each of its first two years of operation, the College drew up an action plan comprising over 100 projects and action points. These plans are based on data exchange as a central basic condition for taking effective action against fraud. The action points cover the entire chain of the battle against fraud, ranging from better prevention and detection to a more effective policy on prosecution and sanctions, and including tighter controls.

Each action plan aims at maximum commitment on the part of the players concerned and, if necessary, modification of the existing structures. That is all achieved without setting up any new institutions. Apart from the action plans, other specific projects have been launched, whether or not involving study groups.

In this way, various recommendations by the parliamentary commission of inquiry into major cases of tax evasion have been implemented by the creation of a working group of experts comprising members of the judiciary, the tax authority and the police.



Recently, Parliament approved the proposals for laws on banking secrecy and court settlements. These enable both the tax authority and the judiciary to take firm action against serious forms of tax evasion.

The outgoing government had undertaken to achieve a structural figure of €1 billion by combating fraud by the end of the parliament. The figures produced in preparing the 2011 budget show that this target can easily be achieved.

**Table 29: Result of fraud control 2009-2011**

<i>In € million</i>	2009	2010	2011
Result of fraud control	422	621	1.006

In order to consolidate or even improve these results in the future, a vision statement was drafted in collaboration with the federal authorities. That text comprises 12 elements for continuing the battle against fraud, approved by the College for the Control of Tax Evasion and Social Security Fraud.

**7.3.2 Good and effective governance**

Since 2008, the government has made a special effort to continue reinforcing the effectiveness and efficiency of the federal administration. The fact that 40 % of federal officials are due to retire in the period 2008-2018 provides a favourable framework in that regard. From 2008 onwards, the various federal administration entities have adopted a selective approach to replacing the civil servants who have retired (or those leaving the government for other reasons). Table 30 shows the trend in the number of full-time equivalents (FTE) in the federal administrative civil service and the Special Corps.

**Table 30: Federal government workforce <sup>(12)</sup>**

<i>In FTE</i>	2008	2009	2010	2011	Change 2008-2011	
					<i>in FTE</i>	<i>in %</i>
Federal level personnel	141.728	138.767	137.079	133.972	-7.756	-5,47%

Source: <http://www.Pdata.be>

In 2009, the government saved around € 60 million (0.91 %) on staff appropriations via a policy of selective replacements, and it also set a ceiling of 98 % on the use of staff appropriations. In 2010, a saving of 0.7 % was achieved on staff appropriations in addition to an extra reduction of € 100 million ( $\pm$  1.55 %). Specifically in the case of public social security institutions, the government cut the overall resources by € 10 million in 2010. In 2011, the government will save a further 0.7 % on staff appropriations, and the plans provide for these economy measures to continue in 2012 and 2013.

The size of the federal administration's workforce was cut by 5.47 % during the period 2008-2011, a large part of that percentage being due to staff cuts in the army. The measures taken led to a reduction in the workforce without compromising the quality of the service to society.

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- 12 Federal administrative civil service: Federal Public Services (FPS), Public Planning Services (PPS), Scientific Institutions (SI), Public Interest Bodies (PIB), Public social security institutions (PSSI) and Special Corps : Army, Judiciary, Council of State, Federal Police and Tax Inspectorate.”

## **Annex 1: Council recommendation of 2 December 2009**

(1) Recognizing that Belgium's budgetary position in 2009 resulted from measures amounting to ½ % of GDP, which is an adequate response to the downturn in view of the limited fiscal room for manoeuvre and were broadly in line with the European Economic Recovery Plan principles, as well as the free play of automatic stabilizers, the Belgian authorities should put an end to the present excessive deficit situation by 2012.

(2) The Belgian authorities should bring the general government deficit below 3 % of GDP in a credible and sustainable manner by taking action in a medium-term framework. Specifically, to this end, the Belgian authorities should:

(a) implement the deficit-reducing measures in 2010 as planned in the draft budget for 2010, and strengthen the planned fiscal effort in 2011 and 2012;

(b) ensure an average annual fiscal effort of ¾ % of GDP over the period 2010-2012, which should also contribute to bringing the government gross debt ratio back on a declining path that approaches the reference value at a satisfactory pace by restoring an adequate level of the primary surplus;

(c) specify the measures that are necessary to achieve the correction of the excessive deficit by 2012, cyclical conditions permitting, and accelerate the reduction of the deficit if economic or budgetary conditions turn out better than currently expected;

(d) strengthen monitoring mechanisms to ensure that fiscal targets are respected.

(3) In addition, the Belgian authorities should seize opportunities beyond the fiscal effort, including from better economic conditions, to accelerate the reduction of the gross debt ratio back towards the reference value.

(4) The Council establishes the deadline of 2 June 2010 for the Belgian government to take effective action to implement the deficit-reducing measures in 2010 as planned in the draft budget for 2010 and to outline in some detail the strategy that will be necessary to progress towards the correction of the excessive deficit. The assessment of effective action will take into account economic developments compared to the economic outlook in the Commission services' autumn 2009 forecast.

### **Council opinion of July 2010 on effective actions**

The Council examined a communication from the Commission assessing the action taken by Belgium, the Czech Republic, Germany, Ireland, Spain, France, Italy, the Netherlands, Austria, Portugal, Slovenia, Slovakia and the United Kingdom to bring their government deficits below the 3 % reference value set by the Treaty for the ratio of deficit to gross domestic product (GDP).

The Council shared the Commission's view that, according to the information currently available:

– those thirteen Member States had up to now acted in accordance with its recommendations;

– no additional step in the excessive deficit procedure is therefore necessary at this stage.

Belgium, the Czech Republic, Germany, Italy, the Netherlands, Austria, Portugal, Slovenia and Slovakia have been subject to an excessive deficit procedure since December 2009, as have Ireland, Spain and France since April 2009 and the United Kingdom since July 2008.

In the recommendations addressed to them on corrective action to be taken, the Council required Belgium and Italy to bring their deficits below the 3 % of GDP threshold in 2012 at the latest and the Czech Republic, Germany, the Netherlands, Austria, Portugal, Slovenia and Slovakia to do so in 2013.

**Annex 2 : Table Sectoral Balance (Table 1d Code of Conduct)**

<i>% of GDP</i>	2010	2011	2012	2013	2014
1.Net lending/borrowing vis-à-vis the rest of the world	2,3	1,5	2,3	3,0	3,7
of which: -balance of goods and services					
-balance of primary incomes and transfers					
-Capital account					
2.Net lending/borrowing of the private sector	6,5	5,2	5,1	4,8	4,5
3.Net lending/borrowing of general government	-4,1	-3,6	-2,8	-1,8	-0,8
4.Statistical discrepancy	-0,1	-0,1	0,0	0,0	0,0

## Annex 3: Structural indicators

### Balance of current transactions with the rest of the world

(% GDP)

	2008	2009	2010e	2011e
Belgium	0,2	2,0	3,0	3,3
Euro area	-0,9	-0,6	-0,4	-0,3
Germany	6,6	5,0	4,8	4,8
France	-3,3	-2,9	-3,3	-3,6
Netherlands	4,2	3,9	5,9	6,4
Italy	-3,1	-3,2	-3,2	-2,9
Greece	-9,5	-5,1	-4,6	-4,5
Spain	-13,8	-13,1	-10,3	-8,6
Portugal	-12,1	-10,5	-10,1	-10,0
Ireland	-5,2	-2,9	-0,9	-0,6
United Kingdom	-1,5	-1,3	-1,8	-2,0

Source: EC (National Accounts)

### Net external position, total economy

(% GDP)

	2005	2006	2007	2008
Belgium	25,6	18,1	33,2	50,6
Euro area	-8,4	-10,0	-8,4	-8,6
Germany	13,5	17,8	19,3	20,9
France	8,0	4,9	14,3	-4,2
Netherlands	27,4	38,4	44,4	42,8
Italy	-2,5	-0,4	0,7	-6,8
Spain	-56,0	-66,1	-77,0	-78,7
Greece	-84,2	-96,5	-107,6	-90,2
Portugal	-69,1	-79,6	-89,6	-94,8
Ireland	-24,7	-5,3	-19,5	-58,4
United Kingdom	-20,1	-27,0	-18,8	-3,4

Sources: EC, NBB (Financial Accounts) – Note: difference between total assets and total liabilities of the domestic sectors

### Real effective exchange rate based on unit labour costs – Total economy

(indices 2000 = 100)

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010e	2011e
Belgium	100,0	102,5	103,9	107,4	106,9	106,8	107,6	109,1	111,8	114,2	112,5	113,0
Germany	100,0	98,5	99,0	103,5	104,1	100,8	97,9	97,3	97,6	100,8	98,2	96,8
France	100,0	100,4	103,1	107,9	109,6	109,5	110,7	112,0	113,6	113,8	112,0	112,2
Netherlands	100,0	103,3	107,4	112,4	112,7	110,6	110,3	111,6	113,3	117,1	114,7	114,0
Italy	100,0	101,3	105,0	113,4	116,7	117,3	118,6	120,0	123,4	126,3	125,1	125,3
Spain	100,0	101,2	103,2	108,2	110,9	112,3	114,7	118,0	121,6	119,2	116,6	116,3
Greece	100,0	97,0	106,6	109,9	111,7	111,9	111,3	112,6	114,3	118,7	117,3	116,7
Portugal	100,0	101,5	103,7	108,9	109,7	111,3	111,0	111,2	113,1	115,6	115,7	116,4
Ireland	100,0	103,1	103,9	112,6	118,9	122,8	125,6	128,9	137,9	131,2	123,0	120,5
United Kingdom	100,0	99,5	100,5	97,4	102,8	102,2	103,7	106,6	92,4	83,7	83,4	83,5

Source: EC

**Private savings**

(% GDP)

	2008	2009	2010e	2011e
Belgium	23,4	25,7	25,7	25,7
Euro area	19,7	21,0	21,5	21,6
Germany	23,4	22,7	24,5	24,9
France	18,3	19,7	20,2	19,8
Netherlands	20,4	22,3	24,3	23,8
Italy	17,2	17,7	17,7	18,2
Spain	18,6	25,0	22,8	22,0
Greece	12,4	15,3	13,1	15,8
Portugal	11,2	15,0	14,4	13,8
Ireland	18,2	19,1	18,5	19,6
United Kingdom	16,9	19,0	19,3	18,9

Source: EC

**Household debt**

(% GDP)

	2005	2006	2007	2008
Belgium	43,1	45,2	46,9	49,4
Euro area	58,5	60,4	61,2	61,6
Germany	69,4	67,0	63,4	61,0
France	43,9	46,4	48,5	50,7
Netherlands	114,1	117,6	118,5	119,8
Italy	34,8	37,1	39,0	39,5
Spain	71,9	79,3	83,4	84,0
Greece	36,3	42,0	47,4	50,6
Portugal	84,9	89,8	94,2	95,8
Ireland	84,4	93,3	98,7	109,3

Source: EC

**Corporate debt**

(% GDP)

	2005	2006	2007	2008
Belgium	36,2	34,8	40,5	42,9
Euro area	51,5	54,6	57,7	60,9
Germany	39,3	39,1	40,3	43,4
France	54,6	55,6	56,5	59,9
Netherlands	54,4	54,3	58,9	61,7
Italy	49,7	53,8	57,8	60,2
Spain	65,0	78,5	87,5	90,5
Greece	41,3	42,6	47,3	54,8
Portugal	75,0	78,4	85,4	95,5
Ireland	70,9	85,5	95,6	104,3

Sources: ECB, EC and NBB (Financial accounts and statistics on MFIs).

Note: Loans from MFIs in the euro area and debt securities.

**Net asset position, individuals**

(% GDP)

	2005	2006	2007	2008
Belgium	222,0	224,8	212,1	180,6
Euro Area	139,2	141,9	134,8	109,4
Germany	117,5	121,5	123,7	115,4
France	126,0	132,2	133,0	117,0
Netherlands	174,7	172,8	169,8	122,3
Italy	198,7	197,1	188,5	165,1
Spain	95,4	101,1	95,5	68,2
Greece	108,0	102,2	92,9	55,1
Portugal	129,4	131,2	133,0	125,0
Ireland	83,5	82,4	64,4	44,5
United Kingdom	187,5	191,4	169,9	123,5

Sources: EC, NBB (financial accounts)

**Net asset position, non-financial corporations**

(% GDP)

	2005	2006	2007	2008
Belgium	-112,1	-127,5	-103,5	-53,1
Euro area	-99,3	-108,5	-107,5	-82,1
Germany	-59,8	-63,9	-67,4	-59,3
France	-92,9	-111,8	-115,6	-87,9
Netherlands	-95,8	-89,7	-87,2	-48,5
Italy	-104,1	-104,3	-105,2	-100,3
Spain	-124,6	-143,5	-157,3	-138,3
Greece	-83,4	-91,1	-94,0	-63,7
Portugal	-143,0	-157,3	-170,6	-163,4
Ireland	-84,6	-74,1	-75,8	-97,5
United Kingdom	-140,0	-152,5	-130,6	-74,5

Sources: EC, NBB (financial accounts)