



COMMISSION OF THE EUROPEAN COMMUNITIES

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Recommendation for a

**COUNCIL OPINION**

**in accordance with the third paragraph of Art. 5 of  
Council Regulation (EC) No 1466/97 of 7 July 1997**

**On the updated stability programme of Belgium, 2005-2009**

(presented by the Commission)

## EXPLANATORY MEMORANDUM

### **Background**

The Stability and Growth Pact, which entered into force on 1 July 1998, is based on the objective of sound government finances as a means of strengthening the conditions for price stability and for strong sustainable growth conducive to employment creation. In 2005, the Pact was amended for the first time. The reform acknowledged the Pact's usefulness in anchoring fiscal discipline but sought to strengthen its effectiveness and economic underpinnings as well as to safeguard the sustainability of the public finances in the long run.

Council Regulation (EC) No 1466/97 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies<sup>1</sup>, which is part of the Pact, stipulates that Member States have to submit, to the Council and the Commission, stability or convergence programmes and annual updates thereof (Member States that have already adopted the single currency submit (updated) stability programmes and Member States that have not yet adopted it submit (updated) convergence programmes). The first stability programme of Belgium was submitted in December 1998. In accordance with the Regulation, the Council delivered an opinion on it on 15 March 1999 on the basis of a recommendation from the Commission and after having consulted the Economic and Financial Committee. In accordance with the same procedure, updated stability and convergence programmes are assessed by the Commission and examined by the Committee mentioned above, while the Council may examine them.

In these programmes, Member States need to specify their medium-term objective for the budgetary position and set out the policy measures to achieve and maintain it, including the accompanying economic assumptions. Following the reform of the Pact, the medium-term objective should be differentiated for individual Member States in the light of the economic and budgetary heterogeneity in the Union, including as regards the fiscal risk to sustainability. Other elements of the reform are that a more symmetrical approach to fiscal policy over the cycle through enhanced budgetary discipline in economic good times should be achieved, while "major structural reforms" with a verifiable impact on long-term sustainability should be taken into account for a temporary deviation from the medium-term objective or the adjustment path towards it.

Taking into account the Commission services' autumn 2005 forecast, the code of conduct<sup>2</sup>, the commonly agreed methodology for the estimation of potential output and cyclically-adjusted balances and the broad economic policy guidelines included in the integrated guidelines for the period 2005-2008, the Commission has examined the recently submitted update of the stability programme of Belgium and, based on its assessment below, has adopted a recommendation for a Council opinion on it.

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<sup>1</sup> OJ L 209, 2.8.1997, p. 1. Regulation as amended by Regulation (EC) No 1055/2005 (OJ L 174, 7.7.2005, p. 1). All the documents referred to in this text can be found at the following website: [http://europa.eu.int/comm/economy\\_finance/about/activities/sgp/main\\_en.htm](http://europa.eu.int/comm/economy_finance/about/activities/sgp/main_en.htm)

<sup>2</sup> "Specifications on the implementation of the Stability and Growth Pact and guidelines on the format and content of stability and convergence programmes", endorsed by the ECOFIN Council of 11 October 2005.

## Assessment

- (1) The 2005 update of the Belgian stability programme was submitted on 5 December 2005, one week after the deadline. It covers the period 2005-2009. The programme broadly follows the model structure and data provision requirements for stability and convergence programmes specified in the new code of conduct<sup>3</sup>.
- (2) In Belgium, real annual GDP growth over the last decade has been close to 2% on average, slightly above the euro area average. However, the employment rate is low (around 60%) and unemployment is characterised by significant regional disparities and a high level of long-term unemployment. Since 2000, Belgium has maintained a budgetary position close to balance.
- (3) The macroeconomic scenario presented in the programme foresees a moderate improvement of real GDP growth to 2.2% on average over the period 2006-2009 after a relatively weak performance in 2005 (1.4%), accompanied by a slow but steady growth in employment (0.7% annually). This scenario can be considered plausible and differs only marginally from that in the Commission services' autumn 2005 forecast. Towards the end of the programme period, the programme foresees a narrowing of the negative output gap. Although the inflation projections in the programme are slightly higher than in the Commission services' autumn forecast, they appear realistic given the somewhat less favourable external assumptions.
- (4) In its opinion of 17 February 2005 the Council endorsed the budgetary strategy presented in the 2004 update of the stability programme of Belgium. As regards budgetary implementation in 2005, the Commission services' autumn 2005 forecast projects a balanced general government budget for 2005, which is in line with the target in the previous update of the stability programme, despite significantly lower GDP growth. However, the statistical recording of some one-off transactions still has to be clarified with Eurostat and might lead to a large one-off increase in the 2005 deficit outcome<sup>4</sup>.
- (5) The budgetary strategy outlined in the update aims at keeping a balanced general government position until 2006 and at building up surpluses afterwards (up to 0.7% of GDP by 2009), in order to maintain the debt ratio on a downward trend. After a gradual decline from 7.2% of GDP in 2001 to 4.3% in 2005, the primary surplus should stabilise at just above 4% of GDP from 2006 onwards. The programme foresees a decrease in the government revenue ratio (mainly as a result of a reduction of the tax burden on labour), but this is more than compensated by a cut in the expenditure ratio (mainly interest expenditure). One-off and other temporary measures still play a significant role in 2006 (0.6% of GDP), although the Belgian authorities project that the recourse to such measures should decrease from 2006 onwards. The new update largely confirms the budgetary strategy outlined in the previous programme against a broadly similar growth outlook.

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<sup>3</sup> The programme does not have a separate section on institutional features of public finances. It also has gaps in the compulsory data and does not provide all optional data prescribed by the new code of conduct.

<sup>4</sup> For the time being, the assumption of railway company debt (2.5% of GDP) by the government in 2005 has been treated without direct impact on the government deficit, while the securitisation of tax arrears in 2005 (0.2% of GDP) has been recorded as deficit-reducing.

- (6) Based on Commission services' calculations on the basis of the programme, according to the commonly agreed methodology, the structural balance (i.e. cyclically adjusted, net of one-off and other temporary measures) is estimated to improve by almost 1% of GDP over the programme period. It deteriorates from zero in 2005 to a deficit of 0.25% of GDP in 2006, followed by an improvement to a surplus of 0.5% of GDP in 2007. Thereafter, the improvement in the structural position, to a surplus of almost 1% of GDP in 2009, is more gradual. The Belgian authorities have identified a medium-term objective (MTO) as meant in the Stability and Growth Pact as a structural surplus of 0.5% of GDP, which is expected to be reached by 2007. As the MTO is more demanding than the minimum benchmark (estimated at a deficit of around 1% of GDP), its achievement should fulfil the aim of providing a safety margin against the occurrence of an excessive deficit. The MTO can be considered appropriate under the current assessment, as it lies within the range indicated for euro area and ERM II Member States in the Stability and Growth Pact and the code of conduct and is more demanding than implied by the debt ratio and average potential output growth in the long term.
- (7) On balance, the budgetary outcomes could be worse than projected in the programme, especially in 2006-2007. While the macroeconomic scenario can be considered plausible and the government has recently introduced new measures to better control health-care expenditure, for 2006 the tax revenue envisaged in the programme appears to be on the optimistic side and the expenditure projections do not seem to provide an adequate buffer against adverse developments. For 2007 the programme does not explain how it will compensate for the expiration of a significant package of one-off and other temporary measures. However, it should be acknowledged that the Belgian authorities have in the recent past demonstrated a strong commitment to achieving their balanced budget targets.
- (8) Taking into account the risk assessment above, the budgetary stance in the programme may not be sufficient to ensure that the programme's MTO is achieved by 2007 as foreseen by the Belgian authorities. However, as stated above, the programme's MTO is more demanding than required by the Stability and Growth Pact and the programme's budgetary strategy seems sufficient to achieve a budgetary position in structural terms that can be considered as appropriate under the Pact throughout the programme period. The budgetary stance in the programme also provides a sufficient safety margin against breaching the 3% of GDP deficit threshold with normal macroeconomic fluctuations. Although the average annual improvement in the structural balance is small, the pace of adjustment towards the MTO can be considered as broadly appropriate. In 2006, however, the adjustment is not in line with the Pact, as the structural balance is planned to deteriorate by 0.25% of GDP in a situation where the output gap (though still negative) is narrowing.
- (9) The Belgian debt ratio remains well above the 60% of GDP reference value (94% of GDP at the end of 2005) but has been on an impressive downward path since 1993 (137% of GDP). After a temporary slowdown in 2005 following a debt take-over from the national railway company SNCB (of 2.5% of GDP), the debt ratio is projected to continue its decline, to below 80% of GDP by 2009. The main driver behind the decline continues to be the high primary surplus (which however has decreased from over 7% of GDP in 2001 to over 4% in 2005). Debt developments could be less favourable than projected in the programme given the above-mentioned possibility of worse-than-anticipated budgetary outcomes. Nevertheless, the debt

ratio seems to be sufficiently diminishing towards the reference value and approaches it at a rapid pace.

- (10) With regard to the sustainability of public finances, Belgium appears to be at medium risk on grounds of the projected budgetary costs of ageing populations. The current level of gross debt, while declining, remains well above the reference value and a steady reduction of the debt ratio hinges upon sustaining high primary surpluses for a prolonged period of time. The Belgian strategy of putting longer-term concerns at the heart of fiscal policy, including by reducing debt, will undoubtedly alleviate sustainability risks and the ‘ageing fund law’ reinforces the political commitment by setting legally binding budgetary targets. Furthermore, recent measures aimed at increasing the effective retirement age and the employment ratio should contribute positively to sustainability. However, the current budgetary position may not be sufficient to cover fully the substantial increase in expenditure due to ageing populations, underlying the importance of maintaining large primary surpluses in the coming years.
- (11) The envisaged measures in the area of public finances are broadly consistent with the broad economic policy guidelines included in the integrated guidelines for the period 2005-2008. In particular, the debt ratio is being reduced at a satisfactory pace and some reforms are undertaken to improve the sustainability of the social security system. However, the deterioration of the structural balance in 2006 is not fully in line with the integrated guideline that calls for taking all necessary corrective measures to achieve the MTO.
- (12) The National Reform Programme (NRP) of Belgium, submitted on 26 October 2005 in the context of the renewed Lisbon strategy for growth and jobs, identifies the following challenges with significant implications for public finances: (i) to support employment by reducing the tax burden on labour, and (ii) to keep the general government budget close to balance and to start building up surpluses from 2007 onwards, in order to maintain the debt ratio on a downward trend. However, the budgetary implications of the actions outlined in the NRP are not sufficiently reflected in the budgetary projections of the stability programme. Measures in the area of public finances envisaged in the stability programme seem to be broadly in line with the actions foreseen in the NRP.

In view of the above assessment, the budgetary position can be considered sound and the continued debt reduction envisaged in the programme provides an example of fiscal policies conducted in compliance with the Pact. However, it would be appropriate for Belgium to step up the structural adjustment in 2006 and, in the subsequent years, to identify and implement additional structural measures to reach the budgetary targets, thereby limiting the recourse to one-off measures.

Recommendation for a

## COUNCIL OPINION

**in accordance with the third paragraph of Art. 5 of  
Council Regulation (EC) No 1466/97 of 7 July 1997**

**On the updated stability programme of Belgium, 2005-2009**

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community,

Having regard to Council Regulation (EC) No 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies<sup>5</sup>, and in particular Article 5(3) thereof,

Having regard to the recommendation of the Commission,

After consulting the Economic and Financial Committee,

HAS DELIVERED THIS OPINION:

- (1) In Belgium, real annual GDP growth over the last decade has been close to 2% on average, slightly above the euro area average. However, the employment rate is low (around 60%) and unemployment is characterised by significant regional disparities and a high level of long-term unemployment. Since 2000, Belgium has maintained a budgetary position close to balance.
- (2) In its opinion of 17 February 2005 the Council endorsed the budgetary strategy presented in the 2004 update of the stability programme of Belgium.
- (3) As regards budgetary implementation in 2005, the Commission services' autumn 2005 forecast projects a balanced general government budget for 2005, which is in line with the target in the previous update of the stability programme, despite significantly lower GDP growth. However, the statistical recording of some one-off transactions still has to be clarified with Eurostat and might lead to a large one-off increase in the 2005 deficit outcome<sup>6</sup>.

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<sup>5</sup> OJ L 209, 2.8.1997, p. 1. Regulation as amended by Regulation (EC) No 1055/2005 (OJ L 174, 7.7.2005, p. 1). The documents referred to in this text can be found at the following website: [http://europa.eu.int/comm/economy\\_finance/about/activities/sgp/main\\_en.htm](http://europa.eu.int/comm/economy_finance/about/activities/sgp/main_en.htm)

<sup>6</sup> For the time being, the assumption of railway company debt (2.5% of GDP) by the government in 2005 has been treated without direct impact on the government deficit, while the securitisation of tax arrears in 2005 (0.2% of GDP) has been recorded as deficit-reducing.

- (4) On [14 February 2006] the Council examined the updated stability programme of Belgium, which covers the period 2005 to 2009. The programme broadly follows the model structure and data provision requirements for stability and convergence programmes specified in the new code of conduct<sup>7</sup>.
- (5) The macroeconomic scenario underlying the programme envisages that real GDP growth will pick up from 1.4% in 2005 to 2.2% on average over the rest of the programme period. Assessed against currently available information, this scenario appears to be based on plausible growth assumptions. The programme's projections for inflation also appear realistic.
- (6) The budgetary strategy outlined in the programme aims at keeping a balanced general government position until 2006 and at building up surpluses afterwards (up to 0.7% of GDP by 2009), in order to maintain the debt ratio on a downward trend. After a gradual decline from 7.2% of GDP in 2001, the primary surplus should stabilise just above 4% of GDP from 2007 onwards. The programme foresees a decrease in the government revenue (mainly as a result of a reduction of the tax burden on labour), but this is more than compensated by a cut in the expenditure ratio (mainly interest expenditure). The new update largely confirms the budgetary strategy outlined in the previous programme against a broadly similar growth outlook.
- (7) Over the programme period, the structural balance (i.e. the cyclically-adjusted balance net of one-off and other temporary measures) calculated according to the commonly agreed methodology is planned to improve by almost 1% of GDP. The authorities set the medium-term objective (MTO) for the budgetary position at a structural surplus of 0.5% of GDP and aim at achieving this position by 2007. As the MTO is more demanding than the minimum benchmark (estimated at a deficit of around 1% of GDP), its achievement should fulfil the aim of providing a safety margin against the occurrence of an excessive deficit. The MTO can be considered appropriate under the current assessment, as it lies within the range indicated for euro area and ERM II Member States in the Stability and Growth Pact and the code of conduct and is more demanding than implied by the debt ratio and average potential output growth in the long term.
- (8) The budgetary outcome could be worse than projected in the programme, especially in 2006 and 2007. In particular, while the macroeconomic scenario can be considered plausible and the government has recently introduced new measures to better control health-care expenditure, for 2006 the tax revenue envisaged in the programme appears to be on the optimistic side and the expenditure projections do not seem to provide an adequate buffer against adverse developments. For 2007 the programme does not explain how it will compensate for the expiration of a significant package of one-off and other temporary measures. However, it should be acknowledged that the Belgian authorities have in the recent past demonstrated a strong commitment to achieving their balanced budget targets.

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<sup>7</sup> The programme does not have a separate section on institutional features of public finances, but some information on these issues is provided in other sections. It also has gaps in the compulsory data and does not provide all optional data prescribed by the new code of conduct.

- (9) In view of this risk assessment, the budgetary stance in the programme may not be sufficient to ensure that the programme's MTO is achieved by 2007 as envisaged in the programme. However, as stated above, the programme's MTO is more demanding than required by the Stability and Growth Pact. The budgetary strategy seems sufficient to achieve a budgetary position in structural terms that can be considered as appropriate under the Pact throughout the programme. In addition, the budgetary stance in the programme seems to provide a sufficient safety margin against breaching the 3% of GDP deficit threshold with normal macroeconomic fluctuations throughout the programme. As for the adjustment path towards reaching the MTO, although the average annual improvement in the structural balance is small, the pace of adjustment towards the MTO can be considered as broadly appropriate. In 2006, however, the adjustment is not in line with the Pact, as the structural balance is planned to deteriorate by 0.25% of GDP in a situation where the output gap (though still negative) is narrowing.
- (10) The debt ratio is estimated to have reached 94% of GDP at the end of 2005, far above the 60% of GDP Treaty reference value. The programme projects the debt ratio to decline by 16 percentage points of GDP over the programme period, to less than 80% of GDP. The evolution of the debt ratio might be less favourable than projected in the programme given the risks to the budgetary targets mentioned above. Nevertheless, the debt ratio seems to be sufficiently diminishing towards the reference value and approaches it at a rapid pace.
- (11) With regard to the sustainability of public finances, Belgium appears to be at medium risk on grounds of the projected budgetary costs of ageing populations. The current level of gross debt, while declining, remains well above the reference value and a steady reduction of the debt ratio hinges upon sustaining high primary surpluses for a prolonged period of time. The Belgian strategy of putting longer-term concerns at the heart of fiscal policy, including by reducing debt, will undoubtedly alleviate sustainability risks and the 'ageing fund law' reinforces the political commitment by setting legally binding budgetary targets. Furthermore, recent measures aimed at increasing the effective retirement age and the employment ratio should contribute positively to sustainability. However, the current budgetary position may not be sufficient to cover fully the substantial increase in expenditure due to ageing populations, underlying the importance of maintaining large primary surpluses in the coming years.
- (12) The envisaged measures in the area of public finances are broadly consistent with the broad economic policy guidelines included in the integrated guidelines for the period 2005-2008. In particular, the debt ratio is being reduced at a satisfactory pace and some reforms are undertaken to improve the sustainability of the social security system. However, the deterioration of the structural balance in 2006 is not fully in line with the integrated guideline that calls for taking all necessary corrective measures to achieve the MTO.
- (13) The National Reform Programme (NRP) of Belgium, submitted on 26 October 2005 in the context of the renewed Lisbon strategy for growth and jobs, identifies the following challenges with significant implications for public finances: (i) to support employment by reducing the tax burden on labour, and (ii) to keep the general government budget close to balance and to start building up surpluses from 2007 onwards, in order to maintain the debt ratio on a downward trend. However, the



budgetary implications of the actions outlined in the NRP are not sufficiently reflected in the budgetary projections of the stability programme. Measures in the area of public finances envisaged in the stability programme seem to be broadly in line with the actions foreseen in the NRP.

In view of the above assessment, the Council is of the opinion that, overall, the budgetary position is sound and the continued debt reduction envisaged in the programme provides an example of fiscal policies conducted in compliance with the Pact. However, Belgium should step up the structural adjustment in 2006 and, in the subsequent years, identify and implement additional structural measures to reach the budgetary targets, thereby limiting the recourse to one-off measures.

### Comparison of key macroeconomic and budgetary projections

		2004	2005	2006	2007	2008	2009
Real GDP (% change)	<b>SP Dec 2005</b>	<b>2.6</b>	<b>1.4</b>	<b>2.2</b>	<b>2.1</b>	<b>2.3</b>	<b>2.2</b>
	COM Nov 2005	2.6	1.4	2.1	2.0	n.a.	n.a.
	<i>SP Dec 2004</i>	<i>2.4</i>	<i>2.5</i>	<i>2.5</i>	<i>2.1</i>	<i>2.0</i>	<i>n.a.</i>
HICP inflation (%)	<b>SP Dec 2005</b>	<b>1.9</b>	<b>2.9</b>	<b>2.8</b>	<b>2.0</b>	<b>1.9</b>	<b>1.7</b>
	COM Nov 2005	1.9	2.7	2.6	1.9	n.a.	n.a.
	<i>SP Dec 2004</i>	<i>1.9</i>	<i>2.0</i>	<i>1.8</i>	<i>1.8</i>	<i>1.8</i>	<i>n.a.</i>
Output gap (% of potential GDP)	<b>SP Dec 2005<sup>1</sup></b>	<b>-0.2</b>	<b>-0.8</b>	<b>-0.6</b>	<b>-0.6</b>	<b>-0.5</b>	<b>-0.4</b>
	COM Nov 2005 <sup>2</sup>	-0.1	-0.8	-0.8	-1.0	n.a.	n.a.
	<i>SP Dec 2004<sup>1</sup></i>	<i>-0.8</i>	<i>-0.5</i>	<i>-0.2</i>	<i>-0.4</i>	<i>-0.5</i>	<i>n.a.</i>
General government balance (% of GDP)	<b>SP Dec 2005</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.3</b>	<b>0.5</b>	<b>0.7</b>
	COM Nov 2005	0.0	0.0	-0.3	-0.5	n.a.	n.a.
	<i>SP Dec 2004</i>	<i>0.0</i>	<i>0.0</i>	<i>0.0</i>	<i>0.3</i>	<i>0.6</i>	<i>n.a.</i>
Primary balance (% of GDP)	<b>SP Dec 2005</b>	<b>4.8</b>	<b>4.3</b>	<b>4.1</b>	<b>4.2</b>	<b>4.1</b>	<b>4.1</b>
	COM Nov 2005	4.8	4.4	3.8	3.4	n.a.	n.a.
	<i>SP Dec 2004</i>	<i>4.9</i>	<i>4.5</i>	<i>4.4</i>	<i>4.5</i>	<i>4.7</i>	<i>n.a.</i>
Cyclically-adjusted balance (% of GDP)	<b>SP Dec 2005<sup>1</sup></b>	<b>0.1</b>	<b>0.4</b>	<b>0.3</b>	<b>0.6</b>	<b>0.8</b>	<b>0.9</b>
	COM Nov 2005	0.1	0.4	0.1	0.0	n.a.	n.a.
	<i>SP Dec 2004<sup>1</sup></i>	<i>0.5</i>	<i>0.3</i>	<i>0.1</i>	<i>0.5</i>	<i>0.9</i>	<i>n.a.</i>
Structural balance <sup>3</sup> (% of GDP)	<b>SP Dec 2005<sup>4</sup></b>	<b>n.a.</b>	<b>0.0</b>	<b>-0.3</b>	<b>0.4</b>	<b>0.7</b>	<b>0.9</b>
	COM Nov 2005 <sup>5</sup>	-0.6	0.0	-0.4	0.0	n.a.	n.a.
	<i>SP Dec 2004</i>	<i>n.a.</i>	<i>n.a.</i>	<i>n.a.</i>	<i>n.a.</i>	<i>n.a.</i>	<i>n.a.</i>
Government gross debt (% of GDP)	<b>SP Dec 2005</b>	<b>94.7</b>	<b>94.3</b>	<b>90.7</b>	<b>87.0</b>	<b>83.0</b>	<b>79.1</b>
	COM Nov 2005	96.2	94.9	91.1	88.1	n.a.	n.a.
	<i>SP Dec 2004</i>	<i>96.6</i>	<i>95.5</i>	<i>91.7</i>	<i>88.0</i>	<i>84.2</i>	<i>n.a.</i>

**Notes:**

<sup>1</sup> Commission services calculations on the basis of the information in the programme.

<sup>2</sup> Based on potential growth of 2.0%, 2.1%, 2.1% and 2.3% respectively in the period 2004-2007.

<sup>3</sup> Cyclically-adjusted balance (as in the previous rows) excluding one-off and other temporary measures.

<sup>4</sup> One-off and other temporary measures taken from the programme (0.4% of GDP in 2005 and 0.6% in 2006; all deficit-reducing). The figures for the one-off measures from 2007 onwards (0.2% in 2007, 0.1% in 2008 and 0.0% in 2009) were provided by the Belgian authorities after the submission of the programme with the caveat that they "should be considered as assumptions and do not prejudice any decision by the Belgian authorities".

<sup>5</sup> One-off and other temporary measures taken from the Commission services' autumn 2005 forecast (0.4% of GDP in 2005 and 0.5% in 2006; all deficit-reducing).

**Source:**

*Stability programme (SP); Commission services' autumn 2005 economic forecasts (COM); Commission services' calculations.*