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BELGIUM: MACRO FISCAL ASSESSMENT
AN ANALYSIS OF THE APRIL 2008 UPDATE OF THE STABILITY PROGRAMME

(Note for the Economic and Financial Committee)

The Stability and Growth Pact requires each EU Member State to present an annual update of its medium-term fiscal programme, called “stability programme” for countries that have adopted the euro as their currency and “convergence programme” for those that have not. The most recent update of Belgium’s stability programme was submitted on 21 April 2008.

The attached technical analysis of the programme, prepared by the staff of, and under the responsibility of, the Directorate-General for Economic and Financial Affairs (DG ECFIN) of the European Commission, was finalised on 23 June 2008. Comments should be sent to Pim Lescrauwaet (pim.lesrauwaet@ec.europa.eu). The main aim of the analysis is to assess the realism of the budgetary strategy presented in the programme as well as its compliance with the requirements of the Stability and Growth Pact. However, the analysis also looks at the overall macro-economic performance of the country and highlights relevant policy challenges.

The analysis takes into account (i) the Commission services’ spring 2008 forecast, (ii) the code of conduct (“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) and (iii) the commonly agreed methodology for the estimation of potential output and cyclically-adjusted balances. Technical issues are explained in an accompanying “methodological paper” prepared by DG ECFIN.

Based on this technical analysis, the European Commission adopted a recommendation for a Council opinion on the programme on 11 June 2008. The ECOFIN Council is expected to adopt its opinion on the programme on 8 July 2008.

* * *

All these documents, as well as the provisions of the Stability and Growth Pact, can be found on the following website:

http://ec.europa.eu/economy_finance/about/activities/sgp/main_en.htm

TABLE OF CONTENTS

SUMMARY AND CONCLUSIONS.....	5
1. INTRODUCTION.....	9
2. KEY CHALLENGES FOR PUBLIC FINANCES WITH A PARTICULAR FOCUS ON THE NEED TO REDUCE LABOUR TAXATION WHILE CONTINUING FISCAL CONSOLIDATION.....	9
2.1. Introduction.....	9
2.2. The need for fiscal consolidation in the view of ageing.....	11
2.3. The tax wedge on labour.....	14
2.4. How to reconcile fiscal consolidation with a further reduction in labour taxation.....	17
2.4.1. Compensating measures on the revenue side.....	17
2.4.2. Compensating measures on the expenditure side.....	18
2.5. Conclusions.....	20
3. MACROECONOMIC OUTLOOK.....	21
3.1. Economic activity.....	21
3.2. Labour market and cost and price developments.....	24
4. GENERAL GOVERNMENT BALANCE.....	26
4.1. Budgetary implementation in 2007.....	26
4.2. The programme's medium-term budgetary strategy.....	28
4.2.1. The main goal of the programme's budgetary strategy.....	28
4.2.2. The composition of the budgetary adjustment.....	30
4.3. Risk assessment.....	33
4.4. Assessment of the fiscal stance and budgetary strategy.....	37
5. GOVERNMENT DEBT AND LONG-TERM SUSTAINABILITY.....	38
5.1. Recent debt developments and medium-term prospects.....	38
5.1.1. Debt projections in the programme.....	38
5.1.2. Assessment.....	40
5.2. Long-term debt projections and the sustainability of public finances.....	41
5.2.1. Sustainability indicators and long-term debt projections.....	41
5.2.2. Additional factors.....	43
5.2.3. Assessment.....	44
6. STRUCTURAL REFORM, THE QUALITY OF PUBLIC FINANCES AND INSTITUTIONAL FEATURES.....	45

7. CONSISTENCY WITH THE NATIONAL REFORM PROGRAMME AND WITH THE BROAD ECONOMIC POLICY GUIDELINES	46
Annex 1: Compliance with the code of conduct	49
Annex 2: Key indicators of past economic performance	56

SUMMARY AND CONCLUSIONS

As part of the preventive arm of the Stability and Growth Pact, each Member State that uses the single currency, such as Belgium, has to submit a stability programme and annual updates thereof. The most recent programme, covering the period 2007-2011, was submitted on 21 April 2008.

Over the last 10 years, real GDP has grown by some 2¼% on average, slightly above the average growth rate in the euro area. This relatively high GDP growth led to a decline in the unemployment rate, while the employment rate (especially of the younger and older workers) and the hours worked remain low, reflecting high labour taxation and labour market rigidities, low job search requirements and a low effective retirement age. The budget has been hovering around a balanced position since 2000 (except in 2005), and the debt ratio, which had fallen from 134% of GDP in 1993 to 108% of GDP in 2000, continued its impressive decline and is now below 85% of GDP. Increasing the employment rate, together with ambitious budgetary positions, would contribute to the long-term sustainability of public finances.

The macroeconomic scenario underlying the programme projects real GDP growth to fall from 2.8% in 2007 to 1.9% in 2008 and stabilise around 2% in the following years. Domestic demand is projected to remain the driver of economic growth throughout the programme period. Assessed against currently available information, the scenario for 2008 and 2009 appears to be based on favourable growth assumptions, given the deteriorated external environment and higher inflation since the projections included in the programme were finalised. Growth assumptions for 2010-2011 are broadly plausible. The programme update expects inflation to rise to 3.0% in 2008, and to slow down to 1¾% over the period 2009-2011. The programme's inflation projections for 2008-2009 appear to be on the low side in view of the marked rise in commodity and processed food prices in recent months. Furthermore, the employment growth projections of around 1% per annum in the programme update appear to be relatively high in view of below-potential GDP growth throughout the programme period. While the programme's wage growth projections are on the low side for 2008, they appear high for the following years (3¼ - 3½ %), especially compared to the projected low inflation rate.

Although the output gap estimated in the Commission services' spring 2008 forecast gradually becomes more negative, reaching almost -1.0% of potential GDP in 2009 and that projected tax elasticities are in line with the standard ones estimated by the OECD, the economy is assessed to still be in neutral times (but leaning toward bad times in 2009) as employment and wage growth remains relatively strong and private consumption remains slightly above the average of 2002-2006.

For 2007, the general government deficit was 0.2% of GDP, against a surplus target of 0.3% of GDP set in the previous update of the stability programme. The worse outturn in 2007 was due to higher expenditure growth than planned which was only partly offset by a small positive base effect from a better-than-expected outcome in 2006 and a positive revenue growth surprise. Higher-than-planned expenditure reflected, in particular, a strong increase in subsidies paid to companies under the service voucher scheme and a lower-than-expected impact of one-off measures. The revenue surprise resulted chiefly from higher-than-expected social contributions and occurred in spite of the non-implementation of a number of planned revenue-increasing one-offs. The budgetary implementation in 2007 was thus not fully in line with the invitation in the Council

opinion of 27 March 2007 on the previous update of the stability programme and with the April 2007 Eurogroup orientations for budgetary policies, since unexpected extra revenue was used for higher-than-budgeted expenditure.

The main goal of the medium-term budgetary strategy in the programme is to ensure a continuous reduction of the still high debt ratio of close to 85% of GDP in 2007 to around 71% of GDP in 2011 through a gradual build-up of headline budgetary surpluses to 1% of GDP in 2011, starting from a balanced budget in 2008. The primary surplus, which has been decreasing since 2001 (from 7.0% to 3.7% of GDP in 2007) in parallel to the progress in debt reduction, is projected to increase to 4.4% of GDP by 2011. As a result of the worse-than-expected outturn in 2007, the budgetary targets (both in nominal and structural terms) are below the ones in the previous update throughout the programme period. The structural balance, calculated according to the commonly agreed methodology, is expected to improve from a deficit of ¼% of GDP in 2007 to a surplus of almost 1½% of GDP in 2011. Compared to what was envisaged in the previous update of the stability programme, the achievement of the medium-term objective (MTO) - a surplus of 0.5% of GDP in structural terms (i.e. in cyclically-adjusted terms net of one-off and other temporary measures) - is delayed by one year to 2009. The adjustment takes place on both the expenditure and revenue side. The planned expenditure reduction of 0.7 percentage point of GDP in nominal terms is attributable chiefly to a fall in interest expenditure which results from the projected decline in the debt ratio. The revenue increase amounts to 0.5% of GDP and follows from the expected growth of tax bases. In contrast to the previous update, the programme explicitly foresees no further recourse to one-off measures after 2008.

The budgetary outcomes could be worse than projected in the programme. First, the macroeconomic environment could be worse than projected in the programme update, especially in 2008 and 2009. In particular, the favourable assumptions regarding employment, wage and consumption growth may have led to an overestimation of tax revenue. In addition, the expected overall tax elasticity seems on the high side in 2008. Regarding primary expenditure, the programme does not include measures that seem necessary to achieve the planned adjustment in a context of rising ageing-related costs and relatively strong projected wage increases. Moreover, excluding the reduction in interest expenditure, the composition of the adjustment is geared strongly to the revenue side, possibly reducing the sustainability of the adjustment. Finally, whilst the budget remained broadly in balance over the last years, the achievement of the aimed-for budget surpluses was postponed. In spite of the good macroeconomic conditions in 2007, the budgetary target was not reached in the absence of a government with full powers following the federal elections in June. In 2008, further measures seem necessary to achieve the target. In view of the risks to the macroeconomic outlook and the budgetary targets mentioned above, the development of the debt ratio is likely to be somewhat less favourable than projected in the programme, although the debt remains on a firm downward path.

In view of this risk assessment, the budgetary stance in the programme may not be sufficient to ensure that the MTO is achieved by 2009, as envisaged in the programme. However, a sufficient safety margin against breaching the 3% of GDP deficit threshold with normal cyclical fluctuations will be provided throughout the programme period. The pace of adjustment towards the MTO implied by the programme should be strengthened in 2008 by implementing additional structural budgetary measures in the context of the planned budget control exercise in order to ensure that the objective of a balanced budget is met. In 2009, it should be backed up by measures, in particular on the expenditure

side, to be in line with the 0.5 % of GDP benchmark improvement specified in the Stability and Growth Pact and to reach the MTO as planned. It should also be noted that the budgetary plans for 2008 are not fully consistent with the April 2007 Eurogroup orientations for budgetary policies. Although the debt ratio may decrease less than projected in the programme, it seems to be sufficiently diminishing towards the reference value over the programme period.

Belgium appears to be at medium risk with regard to the sustainability of public finances. The long-term budgetary impact of ageing is above the EU-27 average, influenced notably by a relatively high increase in pension expenditure as a share of GDP over the coming decades. The effective retirement age in Belgium is one of the lowest in the EU, and raising it is the aim of the Generation Pact which brought a number of changes to the pension system. Although this represents a step in the right direction, national projections show that this reform would not reduce the sustainability gaps. The budgetary position in 2007 as estimated in the programme, though slightly worse than the starting position of the previous programme, contributes to offsetting the projected long-term budgetary impact of population ageing but is not sufficient to fully offset future spending pressures. Maintaining high primary surpluses over the medium term, bringing the debt ratio below the Treaty reference value and implementing further measures aimed at addressing the substantial increase in age-related expenditure would contribute to reducing risks to the sustainability of public finances.

Belgium's national reform programme identifies as key priorities in order to create growth and jobs: the sustainability of public finances; the reduction of labour costs; the creation of a more dynamic labour market; the stimulation of the economy through investment and reforms; strengthening the social security system; and strengthening synergies between environmental protection and growth. In its Strategic Report of 11 December 2007 on the renewed Lisbon strategy for growth and jobs, the Commission considered that Belgium has made good progress on implementing the 2005 national reform programme over the 2005-2007 period, despite some slowdown in the pace of reforms in 2007. The stability programme seems to be consistent to some extent with the October 2007 implementation report of the national reform programme. In particular, both reports consider the sustainability of public finances in light of population ageing as a key challenge for the Belgium economy. The stability programme however does not contain a qualitative assessment of the overall impact of the October 2007 implementation report of the national reform programme within the medium-term fiscal strategy nor systematic information on the direct budgetary costs or savings of the main reforms envisaged in the national reform programme. On the other hand, the budgetary projections of the programme seem to take into account the public finance implications of the actions already implemented on the basis of the national reform programme. The budgetary strategy in the programme is broadly consistent with the country-specific broad economic policy guidelines included in the integrated guidelines and the guidelines for euro area Member States in the area of budgetary policies issued in the context of the Lisbon strategy.

The overall conclusion is that, after an impressive reduction in the debt ratio since 1993 to 85% in 2007, the programme envisages a continued and rapid reduction through a gradual build-up of headline surpluses following the budgetary deterioration in 2007. The budgetary consolidation mainly builds upon a reduction in interest expenditure and an increase in tax revenue, while efforts on primary expenditure remain small. There are risks to the achievement of the budgetary targets particularly in view of the relatively favourable underlying macroeconomic assumptions and the fact that the programme does

not specify measures which seem required to meet the targets. The adjustment to the MTO in 2008 does not appear to be sufficient and it seems unlikely that the MTO will be met in 2009, as planned, in the absence of additional measures.

Comparison of key macroeconomic and budgetary projections

		2006	2007	2008	2009	2010	2011
Real GDP (% change)	SP Apr 2008	2.8	2.7	1.9	2.0	2.0	2.0
	COM Apr 2008	2.8	2.7	1.7	1.5	n.a.	n.a.
	SP Dec 2006	2.7	2.2	2.1	2.2	2.2	n.a.
HICP inflation (%)	SP Apr 2008	2.3	1.8	3.0	1.7	1.8	1.8
	COM Apr 2008	2.3	1.8	3.6	2.3	n.a.	n.a.
	SP Dec 2006	2.4	1.9	1.8	1.8	1.9	n.a.
Output gap ¹ (% of potential GDP)	SP Apr 2008	0.1	0.3	-0.1	-0.4	-0.5	-0.8
	COM Apr 2008 ²	0.1	0.3	-0.3	-1.0	n.a.	n.a.
	SP Dec 2006	-0.3	-0.4	-0.4	-0.4	-0.3	n.a.
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	SP Apr 2008	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
	COM Apr 2008	3.4	3.2	2.6	2.4	n.a.	n.a.
	SP Dec 2006	2.0	2.0	2.2	2.4	2.7	n.a.
General government balance (% of GDP)	SP Apr 2008	0.3	-0.2	0.0	0.3	0.7	1.0
	COM Apr 2008	0.3	-0.2	-0.4	-0.6	n.a.	n.a.
	SP Dec 2006	0.0	0.3	0.5	0.7	0.9	n.a.
Primary balance (% of GDP)	SP Apr 2008	4.3	3.7	3.7	3.8	4.1	4.3
	COM Apr 2008	4.3	3.7	3.3	2.9	n.a.	n.a.
	SP Dec 2006	4.1	4.2	4.1	4.1	4.2	n.a.
Cyclically-adjusted balance ¹ (% of GDP)	SP Apr 2008	0.3	-0.4	0.0	0.5	1.0	1.4
	COM Apr 2008	0.3	-0.3	-0.2	-0.1	n.a.	n.a.
	SP Dec 2006	0.2	0.5	0.7	0.9	1.1	n.a.
Structural balance ³ (% of GDP)	SP Apr 2008	-0.4	-0.3	0.0	0.5	1.0	1.4
	COM Apr 2008	-0.6	-0.3	-0.2	-0.1	n.a.	n.a.
	SP Dec 2006 ⁴	-0.4	0.1	n.a.	n.a.	n.a.	n.a.
Government gross debt (% of GDP)	SP Apr 2008	88.2	84.9	81.5	78.1	74.7	71.1
	COM Apr 2008	88.2	84.9	81.9	79.9	n.a.	n.a.
	SP Dec 2006	87.7	83.9	80.4	76.6	72.6	n.a.

Notes:

¹Output gaps and cyclically-adjusted balances from the programmes as recalculated by Commission services on the basis of the information in the programmes.

²Based on estimated potential growth of 2.5%, 2.5%, 2.2% and 2.2% respectively in the period 2006-2009.

³Cyclically-adjusted balance excluding one-off and other temporary measures. According to the most recent programme, one-off and other temporary measures are deficit-reducing for 0.7% of GDP in 2006 and deficit-increasing for 0.1% of GDP in 2007. According to the Commission services' spring forecast, one-off and other temporary measures are deficit-reducing for 0.9% of GDP in 2006 and deficit-increasing for 0.1% in 2007.

⁴The December 2006 update of the stability programme did not provide information on the use of one-off measures in the years 2008 to 2010.

Source:

Stability programme (SP); Commission services' spring 2008 economic forecasts (COM); Commission services' calculations

1. INTRODUCTION

The 2007 update of the Belgian stability programme was submitted on 21 April 2008 to the Commission and the Council.¹ The important delay compared to the deadline of 1 December specified in the code of conduct results from the longer-than-expected time needed to form a new government following the federal elections of 10 June 2007. The outgoing government stayed in the office until 21 December 2007 and did not consider itself in a position to decide on a budget for 2008 and submit an update of the stability programme. The budget for 2008 was finally agreed on 26 February 2008 by an interim government and the stability programme was submitted by the new government, after its approval by the government on 18 April 2008. It has not been formally adopted by Parliament, but it incorporates the results of the 2008 budget, as approved by Parliament on 22 May 2008. The programme covers the period 2007-2011.

This assessment is further structured as follows. Section 2 discusses the key challenges for public finances in Belgium, with a particular focus on the need to reduce labour taxation while continuing fiscal consolidation. Section 3 assesses the plausibility of the macroeconomic scenario underpinning the public finance projections of the stability programme against the background of the Commission services' economic forecasts. Section 4 analyses budgetary implementation in the year 2007 and the medium-term budgetary strategy outlined in the new programme. Taking into account risks attached to the budgetary targets, it also assesses the appropriateness of the fiscal stance and the country's position in relation to the budgetary objectives of the Stability and Growth Pact. Section 5 reviews recent debt developments and medium-term prospects, as well as the long-term sustainability of public finances. Section 6 discusses the quality of public finances and structural reforms, while Section 7 analyses the consistency of the budgetary strategy outlined in the programme with the national reform programme and its implementation reports and with the broad economic policy guidelines. The annexes provide a detailed assessment of compliance with the code of conduct, including an overview of the summary tables from the programme (Annex 1) and selected key economic indicators of past economic performance (Annex 2).

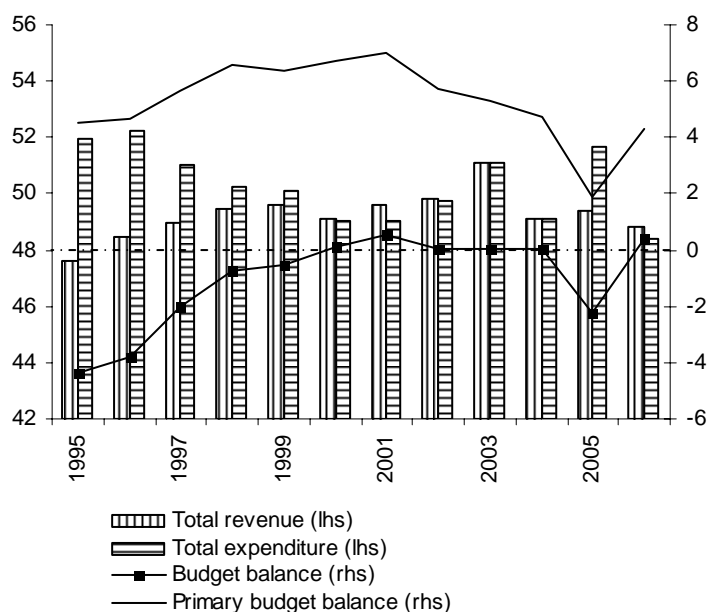
2. KEY CHALLENGES FOR PUBLIC FINANCES WITH A PARTICULAR FOCUS ON THE NEED TO REDUCE LABOUR TAXATION WHILE CONTINUING FISCAL CONSOLIDATION

2.1. Introduction

Economic growth in Belgium broadly matched the euro area average over the last decade. Household consumption expenditure was strong in this period, underpinned by a continuous fall in the household saving rate (from 17.0% in 1998 to 12.5% in 2007). Consumer price inflation (HICP) also remained close to the euro area average. Net exports contributed by about ¼ percentage point on average to real annual GDP growth during the last ten years, in spite of falling export market shares. The unemployment rate (7.5% in 2007) is around the euro area average, but the employment rate remains relatively low, especially for older people.

¹ The English translation was made available on the Belgian dedicated website on 5 May 2008.

Figure 1: Development of government revenue, expenditure and headline balance (percentages of GDP)



Source: National Bank of Belgium.

After a period of significant deficits, in particular in the 1980s, the strong political will to meet the Maastricht criteria and, subsequently, to respect the Stability and Growth Pact fuelled the consolidation drive from the beginning of the 1990s. The entire consolidation was based on reducing interest expenditure, both related to a continuous reduction of government debt and a decline in interest rates, and increased revenue (Figure 1). In 2000, the consolidation effort resulted in a balanced general government budget. Thereafter, the Belgium budget hovered around a balanced position (except in 2005, when the government assumed the debt from the national railway company SNCB), using the continuous fall in interest expenditure (as the government debt continued to fall) to finance new government policies. The cyclically adjusted primary surplus showed a less favourable development, declining from 6.7% of GDP in 2001 to 3.7% in 2007. Government debt continued its downward trend, albeit at a decreasing speed, and fell to 84.9% of GDP at the end of 2007. In order to achieve balanced budgets and to support the reduction of the debt, the authorities have often taken recourse to one-off measures (amounting to 0.6% of GDP on average annually since 2001²).³

The sustained reduction in government debt, through the achievement of sufficiently high primary surpluses is also a cornerstone of the Belgian strategy to absorb in the future the expected sharp increase in public expenditure as a result of ageing (see section 2.2). In view of this strategy, further considerable fiscal consolidation is required in the coming years, despite the fact that as a percentage of GDP deficit reduction in Belgium was larger than in the euro area as a whole.

² This excludes the negative one-off for about 2.4% of GDP related to the take-over of the national railway company's debt by the Fund for Railway Infrastructure, which, at the time, was considered by the Belgian authorities to be without impact on the budget.

³ See for challenges facing Belgian public finances also the economic assessment of the stability programme of Belgium (update of December 2006).

When deciding on measures to create such surpluses, the high overall tax rate in Belgium (45.5% compared to an EU-27 average of 39.6% in 2005⁴) should be considered. Taxes are especially high on labour, with the implicit tax rate amounting to 42.8% of GDP in 2005, compared to an EU-27 and euro area average of 35.2% and 36.8% of GDP respectively. The high tax rate is one of the causes of the low employment rate in Belgium, limiting potential growth and thus making it harder to manage the (budgetary) consequences of an ageing population. In recent years, government policy has focused on reducing the tax burden on labour and the National Reform Programme envisages a further reduction to the average level of the neighbouring countries by 2010.⁵

Although both the planned increase in primary surpluses and a further reduction of the tax burden on labour, by increasing employment, contribute to the long-term sustainability of public finances, both will constitute a challenge for the conduct of public finances in the short and medium run. Therefore, a number of policy lines have been debated recently in Belgium that should allow combining these two objectives.

The section is organised as follows. Subsection 2 analyses the need for further fiscal consolidation. Subsection 3 discusses the need to further reduce the tax wedge on labour. Subsection 4 points to a number of possible options to combine these two objectives. Subsection 5 concludes.

2.2. The need for fiscal consolidation in the view of ageing

The most recent report of the High Finance Council's⁶ (HFC) Study Committee on Ageing⁷ estimates the increase in age-related government spending between 2006 and 2050 at 6.2% of GDP. As can be seen from the Ageing Report endorsed by the Ecofin Council on 14 February 2006, these costs are amongst the highest in the EU-27.⁸

As mentioned above, a cornerstone of the Belgian strategy to deal with the relatively high future budgetary costs of ageing has been to pre-fund these costs through the accumulation of sufficiently high primary surpluses in the coming years.⁹ This strategy

⁴ Eurostat (2007), "Taxation trends in the European Union".

⁵ Belgian National Reform Programme 2005-2008: Progress report 2007.

⁶ The HFC is an independent body composed of high level experts. Its main duties are to analyse fundamental issues of budgetary, financial and fiscal nature and to advise the government on fiscal policy issues. It monitors fiscal policy of the regional governments, recommends each year a coordinated fiscal plan for the various levels of government and evaluates the implementation of the stability programme.

⁷ Comité d'étude sur le vieillissement (2007), "Rapport Annuel", June 2007, High Finance Council.

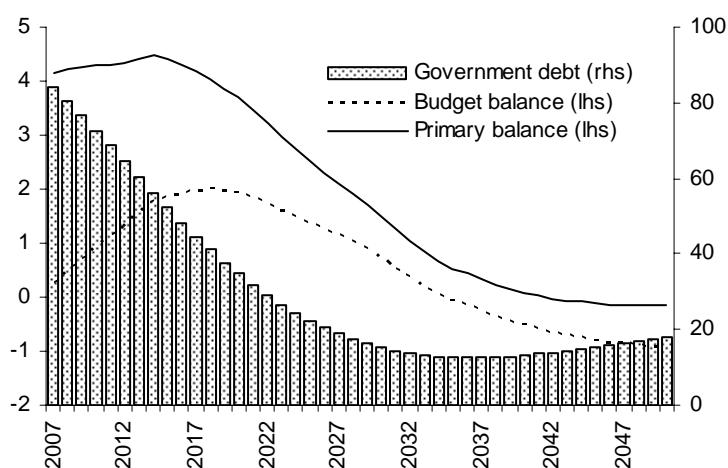
⁸ Economic Policy Committee and European Commission, "Report on the impact of ageing populations on public spending", February 2006, *European Economy*, 2006, n. 1. There are a number of differences between the methodology of the HFC's Study Committee on Ageing and that of the EPC's Ageing Working Group, as a result of which their estimates are not fully comparable. The difference is also due to the fact that the HFC's Ageing Working group estimate is more recent and thus includes the impact of more recent measures and is based on more up-to-date macroeconomic assumptions. See section 5.2 for more information on the differences in assumptions.

⁹ Alternative strategies to prepare for the budgetary cost of ageing could be to reform the labour market and the pension system. The Federal Planning Bureau calculated that a reduction of ageing-related budgetary costs in the long run by about 25% through structural reform measures in the labour market and/or in the pension system would permit the continuation of the policy of balanced budgets while ensuring long-term budgetary sustainability. See Saintrain, M. and S. Weemaes (2008), "Accumuler des surplus budgétaires pour faire face au vieillissement démographique en Belgique: réalités et perspectives", *Working Paper*, n. 5/08, Federal Planning Bureau.

has been anchored in a specific law (the so-called Silver Law)¹⁰. An amendment to this Law prescribes a path until 2012 of growing budget surpluses¹¹; no path has been fixed by Law for the subsequent years. However, as foreseen in the Law, on a regular basis the HFC advises the government on the budgetary path up to 2050 that is required to assure the long-term sustainability of public finances in the view of ageing. It takes into account the annually revised estimates of the budgetary costs of ageing by its Study Committee on Ageing. Up to 2012, the path of the HFC coincides with the one in the Law.

The most recent advice of the HFC (March 2007)¹² is based on the June 2006 report of the Study Committee on Ageing¹³, the latest available at that time (which estimated the budgetary cost of ageing at 5.8% of GDP). This advice targets a 0.3% of GDP surplus in 2007, to be increased by 0.2 percentage points of GDP annually until 2012. In order to realise this path, the primary surplus should increase to 4.4% of GDP by 2012, compared to 3.7% of GDP in 2007. Thereafter, this surplus may be depleted in the period up to 2050, financing 80% of the estimated budgetary cost of ageing in this period (see Figure 2). The HFC's recommended path further implies a continued increase in the budget balance to a surplus of about 2% of GDP by 2017 as a result of lower interest rate expenditure. After that, the implied headline balance starts to decline, reaching a balanced budget around 2035 and falling to a 1% of GDP deficit by 2050.

Figure 2: Budgetary path proposed by the HFC (% of GDP)



Source: High Finance Council and National Bank of Belgium.

¹⁰ Law of 5 September 2001 “portant garantie d’une réduction continue de la dette publique et création d’un Fonds de vieillissement”, *B.S.* 14 September 2001 and Law of 20 December 2005 “modifiant la loi du 5 septembre 2001 portant garantie d’une réduction continue de la dette publique et création d’un Fonds de vieillissement”, *B.S.* 14 March 2006. For more information, see Buffel, L. (2006), “De aangepaste organieke wet op het Zilverfonds”, *Documentatieblad*, FOD Financiën, n. 1, 2006.

¹¹ The path puts forward the objectives and coincides with the path in the December 2006 update of the stability programme up to 2010. The actual contribution to the Silver Fund depends on the achieved budget balance however.

¹² High Finance Council (2007), “Vers des finances publiques soutenables et neutres sur le plan intertemporel dans le contexte du vieillissement”, March 2007, High Finance Council.

¹³ Comité d’étude sur le vieillissement (2006), “Rapport Annuel”, June 2006, High Finance Council.

The HFC's path pre-funds 80% of the estimated budgetary cost of ageing. As shown in section 5.2, pre-funding the entire cost would require a very rapid build-up of high primary surpluses (to over 6% of GDP by 2010) in the absence of reforms that reduce the budgetary cost of ageing. The remaining 20% of the cost should be financed through a further decrease of the non ageing-related primary expenditure by about 1% of GDP in the period between 2010 and 2050. To realise this, the annual growth rate of this kind of expenditure should be limited to 1.5% in real terms as of 2015 (compared to a maximum growth rate of 2% in 2007-2015 and an annual rise in total expenditure of 2.5% over 2000-2006) (see Table 1).

Table 1: Growth rates of the main aggregates under the budgetary path defined by the HFC in March 2007¹ (%)

	2007-2050	2007-2011	2011-2015	2015-2050
GDP	1.8	2.2	2.4	1.7
Total primary expenditure	2.0	2.3	2.4	1.9
Age-related expenditure	2.3	2.8	2.6	2.2
Other expenditure	1.6	1.8	2.1	1.5

Note: (1) Assuming unchanged total government revenue as a percentage of GDP.
Source: High Finance Council (2007), "Vers des finances publiques soutenables et neutres sur le plan intertemporel dans le contexte du vieillissement", March 2007.

In June 2007, the Study Committee on Ageing revised upward its projections for the budgetary cost of ageing on which the HFC's recommended budgetary path was based. The revision amounts to 0.4 p.p. (from 5.8% to 6.2% of GDP) for the period 2006-2050, mainly resulting from a more pessimistic macroeconomic scenario for the years ahead, less beneficial assumptions about the development of relative prices, a higher estimate for the cost of state pensions for officials and employees of the Belgian postal services, an increase of the guaranteed income for the elderly and the takeover by the government of the pension liabilities of the railway company NMBS/SNCB. In a subsequent report, the HFC¹⁴ briefly assessed the impact of these revisions on the available expenditure margins in the short and medium term. It concluded that, given the higher estimated budgetary cost of ageing, considerable additional efforts would be required in order to comply with the budgetary path set out above. In fact, the budgetary margins for non-ageing related expenses would be reduced by 0.6 p.p. per year in the period between 2007 and 2015.

Some other elements may further add to the required consolidation effort in the coming years and also point to the need for further structural reforms to support the long-term sustainability of public finances. First, the HFC's path assumes a budgetary surplus of 0.3% of GDP in 2007 and 0.5% of GDP in 2008, which was not achieved in 2007 and will not be obtained in 2008 given that the government now aims for a balanced budget. Second and more importantly, the path also assumes a constant rate of government revenue to GDP. In view of the need to further reduce the tax wedge on labour, expenditure margins may turn out to be even tighter.

¹⁴ High Finance Council (2007), "Evaluation de l'exécution du Programme de stabilité en 2006 et perspectives 2007-2011", July 2007, High Finance Council.

2.3. The tax wedge on labour

Wage taxation in Belgium consists of social contributions, part of which have to be paid by the employer (standard rate for employees of 34.72% of the gross salary) and part by the employee (standard rate for employees¹⁵ of 13.07% of the gross salary), as well as income taxes paid by employees according to a system of progressive tax rates. The implicit tax rate on labour in Belgium amounted to 42.8%¹⁶ in 2005, which is the third highest in the EU-27 (after Sweden and Italy), although the decline in the previous years narrowed the gap with the EU-27 average (Table 2). The difference with the EU-27 average is mainly due to higher personal income taxes in Belgium.

Table 2: Implicit tax rate on labour

	Belgium	Germany	France	Netherlands	EU average
Level in 2005 (% of labour cost)	42.8	38.7	42.1	30.7	36.5
p.p. change compared to 2000	-1.1	-2.0	0.0	-3.6	-0.6
p.p. change compared to 1995	-1.0	-0.7	0.9	-3.7	-0.5

Source: European Commission.

Wage taxation affects both the supply and the demand for labour and may introduce distortions in labour markets. In Belgium, the high tax wedge is accompanied by a particularly low employment rate. This rate, at 62.0% in 2007, remains well below the euro area average of 65.7% and is especially low for young (27.5% in Belgium compared to 38.0% in the euro area) and older people (34.4% in Belgium compared to 43.3% in the euro area). For the elderly, the employment rate has increased more rapidly than the euro area average, whereas for the younger people the Belgian performance has been below the euro area average. In fact, the employment rate of the younger has declined since 2002. The employment rate is lower for women than for men and there exist considerable regional disparities, with Flanders recording a significantly higher employment rate (65% in 2006) than Wallonia (56.1%) and Brussels (53.1%).

Changes in the tax system could be used to reduce distortions and, hence, increase employment. It is however not always easy to estimate the macro-economic impact of changes in labour taxation. The final impact of such changes on wages and employment depends on the interaction between labour supply and demand, labour market structure and the institutional design of the labour market, such as the wage bargaining process, unemployment benefits and the minimum wage.

In the short run (i.e. with fixed wages), a reduction in employers' contributions only impacts upon labour costs, while a reduction in employees' taxation in turn is entirely translated into an increase in net wages. The first type of measure encourages the replacement of capital by labour with a positive impact on labour demand and employment (at least to the extent that there is a match between the additional demand and supply of labour). The second type of measure, *i.e.* by increasing the difference between unemployment benefits and the net salary when entering into employment and by lowering marginal tax rates, reduces unemployment traps and makes work pay, thus

¹⁵ Different rates apply to self-employed and statutory government staff.

¹⁶ This figure does not take into account the final stage of the personal income tax reform in 2006. On the basis of a not fully comparable estimate for 2006, a further 0.4 percentage point decline could be expected in that year (High Finance Council (2007), "Taxation du travail, emploi et compétitivité", August 2007, High Finance Council.

leading to a higher labour supply. In the long run, with flexible wages, empirical evidence¹⁷ suggests that a reduction of employers' contributions would lead to a smaller decrease of wage costs compared to the short run and, hence, a smaller increase in employment, as wage negotiations allow employees to capture part of the employer's gain in the form of a rise of gross wages. On the other hand, a reduction of employees' contributions or personal income taxes would in the long run drive gross wages down, as part of the initial gain in net salaries would be recaptured by employers during the wage negotiations, creating more new jobs.

Raising employment is particularly important in Belgium as it would boost potential growth and attenuate the budgetary impact of ageing by widening the tax base and reducing expenditure in social benefits. A number of measures have been taken in recent years to reduce the tax wedge on labour (see Box 1). In fact, fiscal measures between 2000 and 2006 are estimated to have lowered the tax wedge by between 1.6 and 2.3 p.p.¹⁸, although other developments have broadened the tax base, such as the general progressivity of the tax system and the erosion of measures that grant reductions in nominal or digressive terms. Furthermore, some of the measures aimed at reducing the tax wedge – mainly the reductions in employers' social contributions – have been partly passed on to employees in the form of higher net wages.¹⁹

Box 1: recent measures to reduce the tax wedge on labour

The tax wedge on labour steadily increased between 1970 and 1996, after which a certain reduction was observed as a result of measures that lowered both employers' and employees' social contributions as well as personal income taxation. The most important measure was the reform of the personal income tax system between 2001 and 2006. It included an extension of the income brackets with the lowest and middle tax rates, a suppression of the highest tax rates of 52.5% and 55%, an increase of the threshold of tax-exempt income and an increase of the deductible lump-sum for professional expenses. A further increase of the deductible lump-sum for professional expenses was introduced in 2006. In addition, the Flemish region introduced, as of 2007, a fixed-rate reduction in income taxes. Finally, in 2008, the federal government increased the amount of tax-exempt income.

Further reductions in the tax wedge took place through a lowering of employers' social contributions. First, structural reductions in social contributions were significantly stepped up in 2000 and further extended in 2004 and 2005. These apply to all wages, but the amount is higher for the lowest (in order to stimulate labour supply for the low-skilled) and the highest incomes (aimed at encouraging the employment of highly skilled workers and, hence, at promoting innovation). Second, there are a number of reductions for the risk groups on the labour market. These groups are the older workers, long-term job seekers, the first employees recruited by a firm, young workers, workers affected by a collective reduction in working time and the four-day week, and finally, workers affected by restructuring. Overall, the reductions in employers' social

¹⁷ See for instance Basilière D., F. Bossier, I. Bracke, I. Lebrun, L. Masure, P. Stockman (2005), "Variantes de réduction des cotisations sociales et de modalités de financement alternative", *Planning Paper*, n. 97, Federal Planning Bureau, January 2005.

¹⁸ High Finance Council (2007), "Taxation du travail, emploi et compétitivité", August 2007, High Finance Council.

¹⁹ Ooghe, E., E. Schokkaert and J. Flechet (2000), "The incidence of social security contributions: an empirical analysis", *Discussion Paper*, DPS 00.23, Center for Economic Studies, KUL.

contributions (compared to the standard rate) amounted to €4.7 billion in 2007²⁰ (up from €3.2 billion in 2003) and are expected to increase to €5.1 billion in 2013.²¹

Employers finally benefited from an increase in wage subsidies. Most of these are targeted to a number of vulnerable groups of employees and/or industries, lowering the tax burden on shift work, overtime work, night work and on highly skilled workers. As part of the intersectoral wage agreement 2007-2008, the government introduced a general wage subsidy amounting to 0.25% of gross wages. Wage subsidies are also provided by the social security system (e.g. the system of service vouchers) and by the regions. Total wage subsidies amounted to an estimated €2.3 billion in 2007, compared to €0.7 billion in 2003, and are projected to increase to €3.9 billion in 2013.

As for employees' social contributions, a digressive work bonus was introduced, aiming to increase the net wage of low income earners in order to reduce unemployment traps. It only applies to workers with labour income below a certain threshold. This threshold was reviewed upward regularly, so that in 2006, 40% of all employees could benefit from the system, compared to 10% in 2000. The budgetary cost of the reductions in employees' social contributions amounted to €0.6 billion in 2007, compared to €0.2 billion in 2003. Assuming no policy changes, a decrease to €0.5 billion is expected by 2013, as nominal wage increases will reduce the number of eligible workers.

In the context of the Lisbon strategy, the Commission recommended in December 2007 to Belgium to “*continue efforts to further reduce the tax burden on labour towards the average of the neighbouring countries, especially by reducing the tax wedge on low-skilled workers, as targeted in the National Reform Programme, by 2010*”²². In order to achieve this target, and taking into account the measures already taken before May 2007 to lower the tax wedge on labour, the Planning Bureau calculated, using its medium term projections, that an additional reduction of the wedge by 1.5% of GDP would be needed.²³ Since then, no significant measures have been taken, also because the longer-than-expected time needed to form a new government following the elections of 10 June 2007 made it impossible to take new initiatives at the federal level for the largest part of 2007.

According to the estimates of the Federal Planning Bureau (see Table 3), the most effective way to increase employment in Belgium would be to reduce employers' social contributions, in particular for low-income earners. Such a measure would also have the most positive impact on economic growth and the lowest net budgetary cost. The reason is that the tax wedge has an especially negative impact on labour demand at the lower end of the labour market, comprising less productive labour. However, also the reaction of wages to the reduction in employers' social contributions and to the fiscal compensation measures determines the impact on employment. The more the initial reductions in employers' social contributions are used to finance higher gross wages, the less positive the impact on employment will be.²⁴

²⁰ National Bank of Belgium (2008), “Rapport Annuel 2007”.

²¹ Federal Planning Bureau (2008), “Perspectives économiques 2008-2013”, May 2008.

²² Communication from the Commission to the European Council, “Strategic report on the renewed Lisbon strategy for growth and jobs: launching the new cycle (2008-2010)”, 11.12.2007, COM(2007)803.

²³ Basselière, D., F. Bossier, I. Lebrun and P. Stockmans (2007), “Le programme national de réforme de la Belgique, Effets macroéconomiques de réductions de charges sur le travail”, *Working Paper*, n. 11/07, September 2007, Federal Planning Bureau.

²⁴ Burggraeve, K. and Ph. Du Caju (2003), “The labour market and fiscal impact of labour tax reductions: the case of reduction of employers' social security contributions under a wage norm regime with automatic price indexing of wages”, *Working Paper Research Series*, 2003/03 n. 36, National Bank of Belgium.

Table 3: Impact of reductions in labour taxation on employment and growth (impact of a 0.5% of GDP tax reduction over a period of 7 years)

	Fixed wages(2)			Flexible wages(2)		
	General reduction in employers' contributions	Reductions in employers' contributions for low wages	Reduction in employees' contributions	General reduction in employers' contributions	Reductions in employers' contributions for low wages	Reduction in employees' contributions
Change in employment (units)	24310	60590	4520	14320	34040	26470
Change in GDP (%)	0.24	0.37	0.15	0.17	0.18	0.28
Change in gov balance (% of GDP)	-0.32	-0.39	-0.32	-0.28	-0.23	-0.44

Notes:
(1) These results do not include the direct impact of changes in the tax wedge on wage formation decisions, but only the impact via the changes in unemployment and productivity.
(2) Fixed wages assume that the tax measures have no impact on wage developments, whereas under flexible wages, wages are negotiated freely and may thus take into account the tax measures.

Source:
Basilère D., F. Bossier, I. Bracke, I. Lebrun, L. Masure, P. Stockman (2005), "Variantes de réduction des cotisations sociales et de modalités de financement alternative", Planning Paper, n. 97, Federal Planning Bureau, January 2005.

Although there is not necessarily a firm link between labour costs and labour taxation, the high tax wedge may also be one of the reasons for the high cost of labour in Belgium, with a negative impact on competitiveness. Whereas wage moderation in order to safeguard competitiveness is primarily the responsibility of the social partners, a reduction of the tax rate on labour could also contribute to limiting the rise in wage costs.

2.4. How to reconcile fiscal consolidation with a further reduction in labour taxation

As pointed out above, the still high tax wedge and low employment rate call for a more comprehensive strategy of reforms of the labour market and the social security system. These reforms should include further reductions in wage taxation, in particular by reducing employers' social contributions for low-wage earners and older workers, given the particularly low employment rate of those in Belgium. Specific reductions for older workers could for instance be realised by making the low-wage thresholds age dependent. The HFC has recently made a number of proposals regarding the possible design of future reductions in labour taxation.²⁵

Whereas reductions in labour taxation may in the long run contribute to fiscal sustainability, the budgetary cost of these reforms requires corrective measures at the government expenditure and/or revenue side in the short run, particularly in view of the fact that the government aims to accumulate increasing primary surpluses over time.

2.4.1. Compensating measures on the revenue side

In principle, additional revenue can be obtained by directly and indirectly broadening the tax base, but also by raising non-labour tax rates. In the latter case, the tax rates in the

²⁵ High Finance Council (2007), "Taxation du travail, emploi et compétitivité", August 2007, High Finance Council. First, the HFC proposes a reduction of employers' social contributions for low income earners for 1% of GDP. Second, it proposes tax credits targeted at low-income earners so as to increase their net wages for 0.5% of GDP. Finally, to support competitiveness, the HFC proposes measures for 0.5% of GDP to encourage research and development (by reducing labour taxes for researchers), to promote investment and to enhance training.

neighbouring countries should be taken into account in order to avoid the tax base to disappear, in particular for mobile tax bases, such as capital.

In deciding on further compensating measures, macro-economic effects have to be considered. In fact, most compensating taxes destroy part of the employment effects stemming from the initial tax reductions. Moreover, compensating measures should not undermine the long-term sustainability of public finances. Finally, they should take into account the division of fiscal powers in Belgium, as raising taxes falling to a different level of government than the one which will lose part of its revenue would entail a number of practical problems.²⁶ Taking all this into account, the HFC discussed a number of options to compensate for the reduction in labour taxes.²⁷

A first option is to increase the tax base of labour taxation by reducing tax expenditures, exemptions, deductions and reductions in personal income taxation, which are considerable in Belgium and may even distort the features of the tax system. Second, certain reforms of capital taxation may lead to additional revenue. However, the HFC deems the scope for additional revenue rather limited in view of the fact that capital is a mobile and a relatively small tax base, although a streamlining of the savings taxation system – which now includes numerous different rates and exemptions – and an introduction of a capital gains taxation, may yield additional revenue. Third, taxation could be geared more towards polluting activities, especially as the share of these taxes in total taxes in Belgium is lower than the euro area average. Fourth, a shift of the tax burden to consumption, by increasing VAT or excise duty rates or by expanding the taxable base could be envisaged. While this alternative may have certain advantages as to the potential amount of additional revenue given the broad tax base, the HFC warns that the macro-economic effects are not clear-cut.²⁸ The fact that an increase of consumption taxation disproportionately falls on the low-income (as was for instance observed when Germany increased the VAT rate in 2007) earners may call for specific corrections. Furthermore, the already high rate in Belgium may limit the scope for further increases.

Given the considerable budgetary impact of reductions in labour taxation, various measures will need to be combined. In addition, a strengthening of alternative policies to increase employment, including a further reform of the pension system (in particular the early retirement system), more effective activation policies and a reform of the system of unemployment benefits, may also greatly contribute to the broadening of the labour tax base. Also measures that increase potential growth would contribute to the long-term sustainability of public finances.

2.4.2. *Compensating measures on the expenditure side*

Empirical studies found that fiscal consolidation mainly based on a reduction of current primary expenditure are often the most successful.²⁹ Government expenditure in Belgium

²⁶ See Bethuyne, G. (2005), “Federalisation and fiscal consolidation: the Belgian experience”, *ECFIN Country Focus*, vol. 2 issue 16, European Commission.

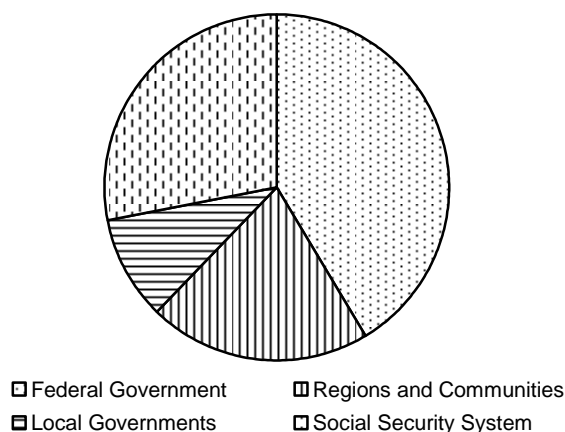
²⁷ Based on High Finance Council (2007), “Taxation du travail, emploi et compétitivité”, August 2007, High Finance Council.

²⁸ To the extent that the loss in purchasing power leads to an upward pressure on wages, it might cause an inflationary spiral. If, on the other hand, wages remain stable, household purchasing power decreases, with negative effects on domestic demand.

²⁹ European Commission (2007), “Public finances in EMU – 2007”, *European Economy*, n. 3/2007. Empirical literature in general finds that cuts in expenditure are more effective than tax increases in

grew by 3.7% per year in nominal terms between 1998 and 2007. Primary expenditure (excluding the declining interest expenditure) increased by on average 4.5% per year over the same period. The growth rates increased slightly in the second half of this period. This mainly resulted from a more rapid expansion of spending by regional and local governments. The share of the latter two remains relatively limited however: the federal level and the social security system respectively account for 41.4% and 27.9% of expenditure in 2007, compared to 20.8% and 9.9% for regional and local governments (see Figure 3).

Figure 3: Expenditure by government level in 2007 (% of total)



Source: National Bank of Belgium.

Government expenditure in recent years increased more rapidly mainly as a result of increases in pensions, subsidies to companies (mainly to increase employment) and social security expenditure (mainly health care expenses, but also including subsidies to support employment). Controlling healthcare spending is key to ensuring a financially balanced social security system over the long term. In 2003, the maximum annual increase in public healthcare spending was fixed at 4.5% in real terms. When this growth limit was exceeded in 2003-2004, the federal government implemented structural cost-cutting measures, which effectively kept spending increases below the limit in the subsequent years. The installation of a fund in 2007, which will contain the positive difference that are expected to be realised each year between targeted (on the basis of the 4.5% maximum rate of increase) and effective expenditure, is a step in the right direction. Going forward, it could be envisaged to further lower the spending limit.³⁰

making consolidation successful. Reductions in public sector employment and wages, and in transfers are found to be particularly conducive. Thus far, this result represents ‘conventional wisdom’. More recent studies, focusing on country cases, provide evidence that both expenditure and revenue-based consolidation can be successful but that other factors may be more important, such as the presence of good fiscal governance and the combination with structural reforms.

³⁰ Note that the social security system is currently mainly financed through employees’ and employers’ social security contributions. To the extent that these are being reduced, alternative financing means need to be found. This has already been done to some extent, for instance by allocating to the social security budget a (larger) share of VAT receipts and excise duties on tobacco. In case more substantial new financing means should be necessary, a general social contribution (not only for workers) or a levy on value added could be envisaged. See Jeanfils, Ph., Ph. Delhez, L. Van Meensel, K. Burggraeve, K. Buysse, Ph. Du Caju, Y. Saks and K. Van Cauter (2006), “Réduction linéaire de

Furthermore, the general government's wage bill, which accounts for roughly one fourth of its total expenditure, has in recent years increased more rapidly than GDP. In 2006, around 797 thousand people worked in the general government sector. This represents an increase of about 10.2% compared to 1996. The bulk of employment growth occurred at the local government level (+17.8% between 1996 and 2006).³¹ This level now accounts for about 35% of total public employment.

In general, given that the negative budgetary impact of reductions in labour taxation (needed to increase employment) should be compensated to ensure the long-term sustainability of public finances, government spending needs to be reduced as a percentage of GDP and should become more effective. This requires a close evaluation of expenditure decisions, taking into account the effect of expenditure on economic growth in the medium and long term, so as to improve the effectiveness of expenditure for health care, education and government administration. In this connection, also a reform of the early retirement system and the benefit system for unemployed could be considered. In addition, giving priority to expenditure that encourages greater labour market participation and investment in an efficient way contributes to fiscal sustainability.

2.5. Conclusions

In view of the high projected budgetary cost of ageing and the still high government debt level, a number of strategies can be combined to ensure the long-term sustainability of public finances. A first strategy is to build up sufficiently high primary surpluses in the coming years and thus reduce the debt stock, so as to create budgetary room to address the costs of population ageing. A second strategy is to increase the employment rate in order to improve economic growth and raise government revenue. A third strategy is to reduce the budgetary cost of ageing, for instance by bringing changes to the pension system. Although all these strategies contribute to the long-term sustainability of public finances, they may be somewhat conflicting in the short and medium term. Indeed, a reduction of labour taxation could in the short and medium term undermine the building up of sufficiently high primary surpluses in the absence of corrective measures, either on the revenue or the expenditure side.

Tax revenue can be raised by broadening the tax base, for instance in the field of personal income taxation by suppressing tax expenditures, or by increasing tax rates, taking into account the percentages in the neighbouring countries (especially for the more mobile tax bases). Fiscal consolidation may also be realised – and perhaps more successfully – by taking measures on the expenditure side. In general, expenditure decisions should take into account the effect on economic growth in the medium and long term. Priority should be given to orienting expenditure so as to encourage greater labour market participation and investment.

Given the considerable budgetary impact of reductions in labour taxation, various measures will need to be combined. In addition, further structural reforms to increase employment or to reduce the budgetary cost of ageing, including a further reform of the pension system (in particular the early retirement system), more effective activation

cotisations patronales à la sécurité sociale et financement alternatif “, *Working Paper Research Series*, n. 81, March 2006, National Bank of Belgium.

³¹ National Bank of Belgium (2007), “Rapport Annuel 2006”.

policies and a reform of the system of unemployment benefits, may also greatly contribute to fiscal consolidation by reducing social security expenditure and broadening the labour tax base.

3. MACROECONOMIC OUTLOOK

This section assesses the plausibility of the macroeconomic scenario (economic activity, labour market, costs and prices) underpinning the public finance projections of the programme. It also examines whether good or bad economic times in the sense of the Stability and Growth Pact prevail. Finally, it describes macroeconomic vulnerabilities and how they are expected to develop according to the programme.

3.1. Economic activity

GDP growth came out at 2.8% in 2007 and was mainly driven by domestic demand. Private consumption was buoyant, mainly on the back of increasing real household disposable income. Investment growth was impressive, reflecting the important increase in production. Despite the slower growth of export markets and the appreciation of the euro, exports recovered from the unusually low expansion rate in 2006 as Belgian exporters were able to limit their loss of market share. Imports increased faster however, reflecting higher final demand, so that the contribution of net exports to GDP growth became negative (0.6% of GDP).

The programme update projects GDP growth at 1.9% in 2008 and at 2.0% in the subsequent years. Throughout the programme period, domestic demand is expected to be the main driver of GDP growth. Its contribution to GDP growth is projected to amount to 2.0% in 2008 and to 1.8% thereafter. The contribution of consumption on average amounts to 0.9%. Investment accounts for 0.6% of GDP growth throughout the programme period. The contribution of net exports to GDP growth remains slightly negative in 2008 but is projected to turn positive as of 2009. Overall, the expected contribution of the individual demand components is broadly in line with historical averages.

Although GDP growth levels included in the programme are slightly below the average growth rate over the last 10 years (2¼%), they are above the Commission services' forecast for 2008 (1.7%) and 2009 (1.5%) (see Table 4). The macroeconomic projections for 2008 included in the programme update date back to the beginning of the year and thus do not take into account to the same extent the deteriorated external environment, high inflation and tighter lending criteria. The programme acknowledges that downward risks to the projections have increased since their finalisation. For 2009, the programme update states that the macroeconomic scenario *"is more of a consistent macroeconomic reference framework that is quite plausible for a prescriptive exercise where the details still need to be fine-tuned, than actual forecasts in the strict sense"*. This may also explain why the external assumptions are different from these in the Commission services' spring 2008 forecast, which, however, may have been not yet available at the time of the drafting of the programme. The most recent mid-term projections of the Federal Planning Bureau forecast GDP growth at 1.7% in both 2008 and 2009, below the projections in the programme update.³² For 2010 and 2011, the Federal Planning Bureau forecasts GDP growth at 2.3% and 2.4% respectively.

³² Federal Planning Bureau (2008), "Perspectives économiques 2008-2013", May 2008.

Against the background of the potential growth estimated by the Commission services for 2009, the growth forecast in the programme update for 2010 and 2011 years seems broadly plausible.

For 2008, the main difference between the programme's and the Commission services' scenario is due to the latter's lower expected growth rate of private consumption, which is the result of the more pessimistic assumptions as to inflation, employment and real wage increases: the Commission services forecast consumption growth at 1.5% in 2008, compared to 1.8% in the programme. This difference is partly related to the dynamic employment and wage growth assumptions in the programme update, compared to the particularly low inflation rate (see section 3.2). The most recent projections of the Federal Planning Bureau forecast consumption growth in 2008 at 1.4%. As for 2009, both the Commission services and the programme update project similar growth rates for private consumption.

Table 4: Comparison of macroeconomic developments and forecasts

	2007		2008		2009		2010	2011
	COM	SP	COM	SP	COM	SP	SP	SP
Real GDP (% change)	2.7	2.7	1.7	1.9	1.5	2.0	2.0	2.0
Private consumption (% change)	2.5	2.5	1.5	1.8	1.4	1.5	1.6	1.6
Gross fixed capital formation (% change)	5.1	5.1	2.2	2.4	1.9	2.7	2.5	2.7
Exports of goods and services (% change)	4.6	4.6	3.9	4.5	3.6	5.6	5.6	5.6
Imports of goods and services (% change)	5.0	4.9	4.3	4.8	3.8	5.6	5.6	5.6
<i>Contributions to real GDP growth:</i>								
- Final domestic demand	2.9	2.8	1.8	2.0	1.7	1.8	1.8	1.8
- Change in inventories	0.0	-0.2	0.0	0.0	0.0	0.0	0.0	0.0
- Net exports	-0.2	-0.1	-0.2	-0.1	-0.2	0.2	0.2	0.2
Output gap ¹	0.3	0.3	-0.3	-0.1	-1.0	-0.4	-0.5	-0.8
Employment (% change)	1.7	1.6	0.9	1.1	0.4	0.9	0.9	0.8
Unemployment rate (%)	7.5	7.6	7.3	7.3	7.5	7.1	7.0	6.7
Labour productivity (% change)	1.0	1.1	0.8	0.8	1.1	1.1	1.2	1.3
HICP inflation (%)	1.8	1.8	3.6	3.0	2.3	1.7	1.8	1.8
GDP deflator (% change)	1.7	1.6	2.6	2.6	2.1	2.1	1.9	1.9
Comp. of employees (per head, % change)	3.0	3.1	3.5	3.2	2.9	3.3	3.4	3.4
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	3.2	n.a.	2.6	n.a.	2.4	n.a.	n.a.	n.a.
<u>Note:</u>								
¹ In percent of potential GDP, with potential GDP growth according to the programme as recalculated by Commission services.								
<u>Source:</u>								
Commission services' spring 2008 economic forecasts (COM); Stability programme (SP)								

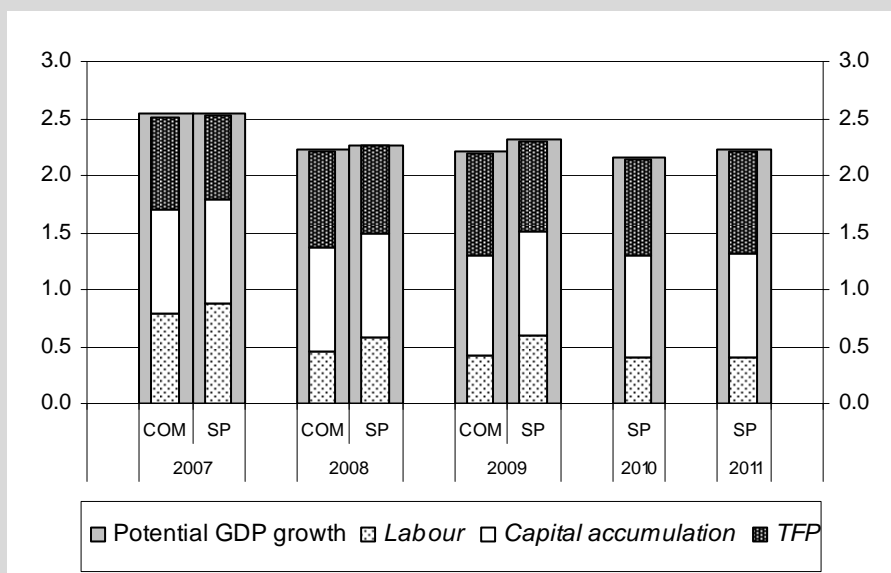
A second reason for the difference, in particular concerning 2009, relates to the more unfavourable assumptions in the Commission services' spring 2008 forecast on the international economic environment, including the lower projected GDP growth of Belgium's main trading partners (Germany, France and the Netherlands) as well as the US, and a stronger euro, which are expected to put an additional drag on exports. World GDP growth (excluding the EU) in the programme is projected at 5.3% in 2008 and 5.5% in 2009, markedly higher than the 4.4% and 4.2% projected in the Commission services' spring 2008 forecast. The programme assumes a dollar/euro exchange rate of 1.39, compared to slightly above 1.50 in the Commission services' spring 2008 forecast. The oil price assumption is 74.9 USD per barrel in 2008 and 72.7 USD in 2009 vs. 101.2 USD and 100.0 USD in the spring forecast. As a result of the higher expected growth rate of exports, the programme projects a higher contribution of net exports to GDP growth than the Commission services' spring 2008 forecast, in particular in 2009. The

most recent projections of the Federal Planning Bureau are more in line with the Commission services forecast for 2009.

Box 2: Potential growth and its determinants

Potential output growth in the programme update (as recalculated by the Commission services using the commonly agreed methodology) is between 2.2% and 2.3% per year over the whole programme period. This is broadly in line with potential growth estimates in the Commission services' spring 2008 forecast (2.2% for both forecast years), although the programme projects a slightly higher potential growth rate in 2009 (see Figure).

Potential growth and its determinants



Potential growth in the programme is in line with GDP growth rates observed in the past 10 years, and below growth rates observed in the recent past. The contribution of the different components remain broadly unchanged and is largely comparable with the projections in the Commission services' spring 2008 forecast, although the programme foresees a higher contribution of labour to potential growth in 2009. This can be explained by the expected sustained decrease in the unemployment rate. This, combined with the particularly low inflation forecasts in the programme update, both for 2008 and 2009, leads to a reduction of the non-accelerating wage rate of unemployment (NAWRU from 7.6% in 2007 to 7.2% in 2009 (and further to 6.7% in 2011), thus pushing up potential growth. The Commission services' spring 2008 forecast expects the NAWRU to remain stable until 2009.

For the same reasons, potential growth figures for the years 2010 and 2011 might also be slightly overestimated. In case the NAWRU implied by the programme update would be replaced by the one of the Commission services' spring forecast (also for 2010 and 2011), potential growth in 2008 and 2009 would be the same as projected in the Commission services' spring 2008 forecast and decline to 2.0% thereafter.

The Commission services' forecast for investment is also more negative, in particular regarding 2009, where it projects a further slowdown whereas the programme update foresees a pickup, which would require a strong rebound of quarterly growth as of the end of 2008.

Overall, the programme's macroeconomic assumptions are favourable in the first two years, in particular in 2009, and seem broadly plausible thereafter.

The output gap implied by the programme update and recalculated by the Commission services on the basis of the commonly agreed methodology is assumed to gradually widen. Starting from a 0.3% of potential GDP positive gap in 2007, the gap is set to

become slightly negative in 2008 and to deteriorate further at a slow pace to -0.8% of potential GDP in 2011.³³ The programme update thus implies a slightly smaller negative output gap in 2008 and 2009 than the Commission services' spring 2008 forecast. This is explained by the fact that the programme update expects considerably higher GDP growth figures in both 2008 and 2009. However, given that the programme projects a slightly higher potential growth rate than the Commission services (see Box 2), potential GDP may have been overestimated in the update, so that the output gap becomes somewhat too negative over the programme period.

3.2. Labour market and cost and price developments

Both the programme update and the Commission services' spring forecast point to continued strong employment increase in 2008 (1.1% and 0.9% respectively). For 2009, the Commission services' employment growth projections (0.4%) are markedly lower than those in the programme update (0.9%), largely reflecting the former's less benign overall macroeconomic scenario for that year and possibly also the lower projected growth of subsidised employment. Employment growth projections for 2008 and 2009 in the current programme are 0.1 p.p. higher than in the December 2006 update, while GDP growth projections are markedly lower. The programme's employment growth projections might also be slightly optimistic for 2010 (0.9%) and 2011 (0.8%) in view of below-potential GDP growth in these years. In its most recent projections, the Federal Planning Bureau still expects employment to increase by 1.1% in 2008 and by 0.8% in 2009, broadly in line with the programme's forecast. For 2010 and 2011, the Federal Planning Bureau expects employment growth of 0.9% and 1.0% respectively, but in combination with considerably higher GDP growth than in the programme update (see Section 3.1).

The labour content of real GDP growth, calculated as the percentage increase in employment vis-à-vis the percentage increase in real GDP, averages 0.5 over the programme period, compared to an 0.6 average over the last 10 years. However, the latter figure has been driven upward by the increase of employment in the public sector and the growth of subsidised employment in recent years. Indeed, employment growth in the public sector (i.e. excluding subsidised employment in the private sector) accounted for almost 20% of total employment creation in the period between 1996 and 2006. Since the introduction of the so-called service vouchers (a system to promote the employment of low-skilled workers through subsidised jobs) in 2003, the scheme led to over 60,000 new jobs³⁴, accounting for almost 30% of total employment creation in this period. In the Commission services' spring forecast, the labour content of GDP growth amounts to only 0.4 on average for 2008 and 2009, partly due to a lower expected contribution of subsidised and government employment than in the past.

The programme update expects the unemployment rate to fall from 7.6% in 2007 to 7.1% in 2009 and further to 6.7% in 2011. This appears optimistic compared to the Commission services' spring 2008 forecast, which foresees a slight increase in the unemployment rate in 2009 (from 7.3% to 7.5%), in line with the more pessimistic macroeconomic projections. It may also be slightly on the high side in view of the

³³ The figures provided in the programme are for all programme years considerably different from these recalculated by the Commission services on the basis of the information in the programme. Whereas the recalculated figures point to a positive output gap in 2007, becoming negative over the programme period, the programme update estimates a negative output gap in 2007 and expects the gap to close by the end of the programme period.

³⁴ Office National de l'Emploi, Rapport Annuel 2007. Figure at the end of 2007. Given that the system mainly generates part-time employment, the creation of FTE jobs is much lower (about 27,000).

programme update's GDP growth projections, even if the government would step up activation policies in order to increase employment, as mentioned in the programme update.

The compensation of employees is set to increase by 3.2% in 2008 in the programme update, as compared to the 3.5% projected in the Commission services' spring forecast. The increase in the programme update seems low in view of recent high inflation data. From 2009, wages are projected to increase by about 3.3%. This appears to be relatively high compared to the historical average (2.1% over 1998-2007) and is somewhat higher than the 2.9% increase in the Commission services' spring forecast for 2009, which is based on the Commission services' projections for Germany, France and the Netherlands. The projected wage increases do not seem consistent with the low inflation projections in the programme (see below) for these years. The outlook for productivity growth is in line with the Commission services' spring 2008 forecast.

The programme update expects inflation at 3.0% in 2008 (compared to 1.8% in 2007), and foresees a moderation to about 1.8% afterwards. This is more than 0.5 p.p. below the Commission services' spring 2008 forecast for 2008 and 2009. The figures in the programme update for these years seem low in view of the inflation rates observed in recent months, following the marked rise in commodity and processed food prices. In its most recent mid-term projections, the Federal Planning Bureau forecasts inflation at 3.8% in 2008 and 2.0% in 2009.

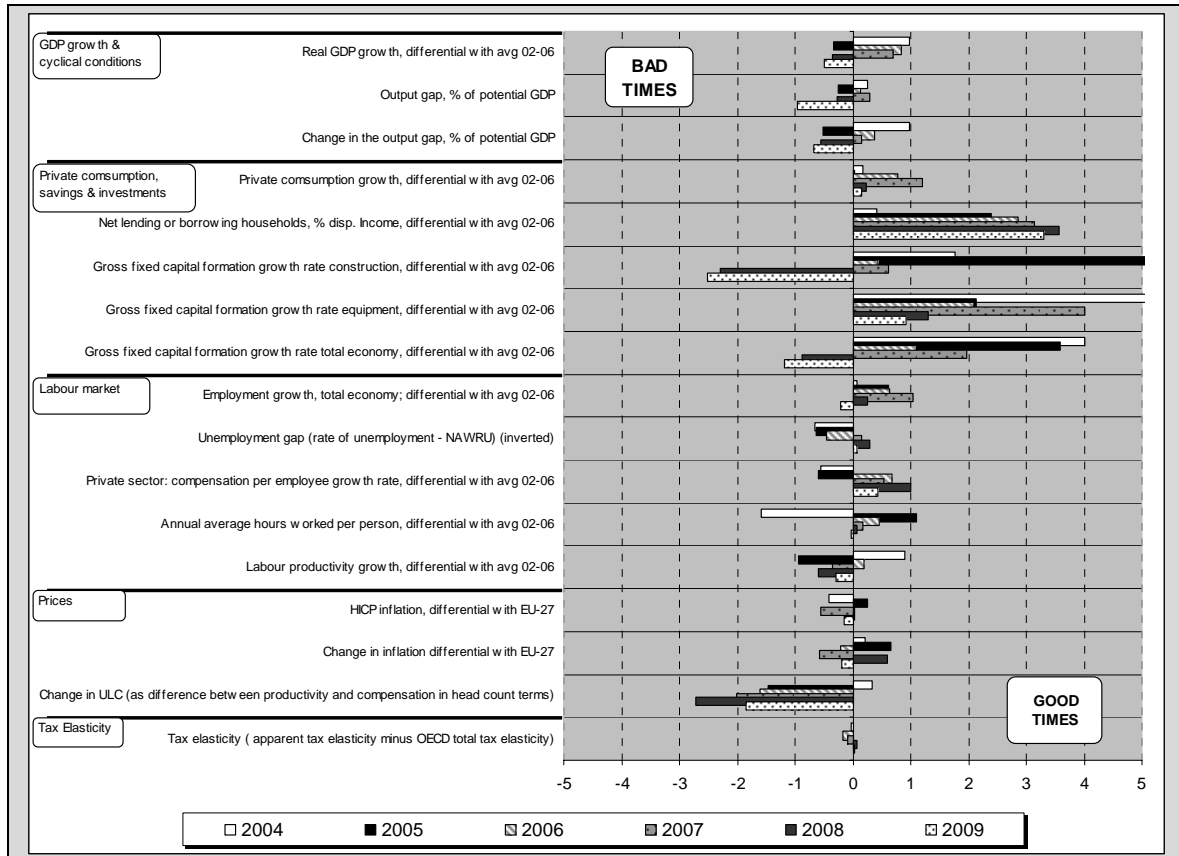
The relatively low inflation projections do not seem to be in line with the assumed dynamic development of wages. The combination would, as from 2009, imply real salary increases above those observed in the past (with the annual increase averaging 2.6% over the last 10 years), although productivity growth is not expected to improve markedly. While labour shortages are currently observed in certain parts of the country and for certain professions, these are at this point not expected to drive up wages and could moreover soften in view of GDP growth below potential throughout the programme period.

Box 3: Good or bad economic times?

According to the code of conduct, the assessment of whether the economy is experiencing good or bad economic times starts from the output gap, but draws on an overall economic assessment, which should also take into account tax elasticities. The figure below presents a set of macroeconomic indicators drawn from the Commission services' spring 2008 forecast. Overall, the economy seems to be in neither good nor bad ("neutral") economic times taking into account tax elasticities in the period 2007-2009, but to be leaning toward bad times in 2009. The output gap estimated in the Commission services' spring 2008 forecast gradually becomes more negative, reaching almost -1.0% of potential GDP in 2009 and projected tax elasticities are in line with the standard elasticities estimated by the OECD.

On the other hand, investment in equipment and private consumption both remain slightly above the 2002-2006 average in the forecast years. Employment growth remains relatively dynamic and the unemployment rate does not (significantly) increase. Also wages are expected to develop relatively dynamically compared to the 2002-2006 average, partly related to the relatively high inflation rate compared to the euro area average, in particular in 2008. This also explains the bad performance in terms of unit labour costs in 2008. Therefore, the economy is assessed to still be in neutral times, but to be leaning toward bad times in 2009.

Good versus bad times



4. GENERAL GOVERNMENT BALANCE

This section consists of four parts. The first part discusses budgetary implementation in the year 2007 and the second presents the medium-term budgetary strategy in the new update. The third analyses the risks attached to the budgetary targets in the programme. The final part assesses the appropriateness of the fiscal stance and the country's position in relation to the budgetary objectives of the Stability and Growth Pact.

4.1. Budgetary implementation in 2007

Table 5 compares the 2007 revenue and expenditure targets (as a percentage of GDP) from the previous update of the stability programme with the budgetary outcome as mentioned in the April 2008 update of the stability programme. The difference between the revenue and expenditure targets for 2007 and the projected outcome is decomposed into a base effect, a GDP growth effect on the denominator and a revenue / expenditure growth effect³⁵:

- The base effect captures the part of the difference that is due to the actual outcome for 2006 being different from what was projected in the previous update in the programme (either because the actual revenue / expenditure level in 2006 was different from the estimated outcome in the previous programme or because GDP turned out to be different from the scenario in the previous update of the programme). The base effect therefore also captures the effect of revisions to the GDP series.
- The GDP growth effect on the denominator captures the part of the difference that is related to current GDP growth projections for 2007 turning out higher or lower than

³⁵ A fourth, residual component is usually small, except if there are very large differences between the autumn forecast and the target (the full mathematical decomposition is in the methodological paper mentioned above).

anticipated in the previous update of the programme (therefore reducing / increasing the denominator of the revenue and expenditure ratio).

- The revenue / expenditure growth effect captures the part of the difference related to the revenue / expenditure growth rate in 2007 turning out to be higher or lower than targeted in the previous update of the programme. This would typically be due to GDP developments different from those expected in the previous update of the programme, or as a result of apparent tax elasticities different from the ex ante tax elasticities (or both).

Table 5: Budgetary implementation in 2007

	2006		2007	
	Planned	Outcome	Planned	Outcome
	SP Dec 2006	SP Apr 2008	SP Dec 2006	SP Apr 2008
Revenue (% of GDP)	49.1	48.8	48.9	48.7
Expenditure (% of GDP)	49.1	48.5	48.6	48.9
Government balance (% of GDP)	0.0	0.3	0.3	-0.2
Nominal GDP growth (%)			4.3	4.4
Nominal revenue growth (%)			3.9	4.2
Nominal expenditure growth (%)			3.2	5.3
Revenue surprise compared to target (% of GDP)				-0.2
<i>Of which</i> ¹ : 1. Base effect				-0.3
2. GDP growth effect on the denominator				0.0
3. Revenue growth effect				0.1
<i>Of which: due to a marginal elasticity of total revenue w.r.t. GDP larger than 1</i> ²				0.1
Expenditure surprise compared to target (% of GDP)				0.3
<i>Of which</i> ¹ : 1. Base effect				-0.6
2. GDP growth effect on the denominator				0.0
3. Expenditure growth effect				0.9
Government balance surprise compared to target (% of GDP)				-0.5
<i>Of which:</i> 1. Base effect				0.3
2. GDP growth effect on the denominator				0.0
3. Revenue / expenditure growth effect				-0.8
Notes:				
¹ A positive base effect points to a higher-than-anticipated outcome of the revenue / expenditure ratio in 2006. A positive denominator effect indicates lower-than-anticipated economic growth in 2007. A positive revenue / expenditure growth effect points to higher-than-anticipated revenue / expenditure growth in 2007. The three components may not add up to the total because of a residual component, which is generally small.				
² Equal to (2)+(3). A positive sign means that the marginal elasticity of revenue with respect to GDP exceeds one.				
<i>Source:</i>				
Commission services				

The December 2006 update of the programme set a surplus target of 0.3% of GDP for 2007, based on an expected balanced budget outcome in 2006. Although the final outcome for 2006 was more positive than expected (0.3% of GDP surplus), leading to a positive base effect on the balance in 2007, the outcome for 2007 was 0.5 p.p. below the target. The worse outcome of the government balance in 2007 compared to what had been planned in the December 2006 programme update (Table 5) was due to a number of factors. On the revenue side, a negative base effect of 0.3 % of GDP has been partly compensated by a positive growth effect (0.1% of GDP). Overall, revenue was 0.2% of GDP lower than planned. On the expenditure side, the impact of lower expenditure in 2006 (-0.6% of GDP base effect) has been more than offset by higher-than-projected expenditure (0.9% of GDP), as a result of which expenditure was 0.3% of GDP higher than planned.

Unexpected revenue in 2007 mainly resulted from higher-than-expected social contributions. If planned revenue-increasing one-offs for 0.2% of GDP (i.e. the take-over by the government of private pension funds) had been carried out (which was not possible as the outgoing government, in caretaker capacity, did not consider itself in position to go ahead with these operations), the total positive revenue surprise would have amounted to 0.3% of GDP.

Expenditure was higher than planned as a result of various developments. The most important reasons are the higher-than-expected government consumption and wage subsidies paid to companies (in order to increase employment of certain target groups), in particular under the service voucher scheme. These expenditure overruns should be seen against the background of the absence of the traditional budget control exercises. The non-implementation of a number of expenditure-reducing one-offs (sale of real estate) for 0.2% of GDP combined with unexpected deficit-increasing one-offs (mainly the repayment of corporate taxes to a number of companies) of about 0.2% of GDP further explain the expenditure surprise. This resulted in an increase in expenditure (as a percentage of GDP) in 2007, whereas the December 2006 update of the stability programme actually planned a 0.5 p.p. of GDP reduction.

The policy invitation included in the Council opinion of 27 March 2007 on the previous update of the stability programme was to “*ensure that the budgetary target for 2007 is met [...] including through a reduction of the recourse to one-off measures.*” Contrary to plan (the government initially intended to have deficit-reducing one-offs for 0.5% of GDP), the overall impact of one-offs was not deficit-reducing, but slightly deficit-increasing. The budgetary outturn was below the target and expenditure turned out higher than planned. Against this background, the policy invitation was not fully followed in 2007.

4.2. The programme’s medium-term budgetary strategy

This section describes the medium-term budgetary strategy outlined in the programme - and how it compares with the one in the previous update - as well as the composition of the budgetary adjustment, including the broad measures envisaged.

4.2.1. The main goal of the programme’s budgetary strategy

In line with previous updates, the April 2008 update aims at ensuring a further continuous reduction of the still high debt ratio to around 71% of GDP in 2011, through a gradual build-up of nominal budgetary surpluses (from 0.3% in 2009 to 1.0% in 2011), to pre-fund the ageing-related costs ahead (see Section 2). The corresponding primary surplus is expected to gradually increase from 3.7% of GDP in 2007 to 4.3% of GDP in 2011. The latter increase is somewhat smaller than that of the headline balance as interest charges as a percentage of GDP are expected to decrease further thanks to the gradual reduction of the debt (while the implicit interest rate is expected to stabilise).

The programme update aims at achieving the MTO of 0.5% of GDP (unchanged compared to the previous update) in 2009. The structural balance (as recalculated by the Commission services according to the commonly agreed methodology on the basis of the information in the programme) increases from -0.3% of GDP in 2007 to 0.0% in 2008, 0.5% in 2009 and further to 1.4% in 2011. About one third of this 1.7 p.p. of GDP improvement is due to a reduction of interest expenditure. This suggests a mildly restrictive stance throughout the programme period.

Compared with the previous programme update, the budgetary path has been loosened and the achievement of the MTO is postponed from 2008 to 2009 (see Table 6). Because the surplus targets for 2007 and 2008 set in the December 2006 update have not been achieved, the targets (both in nominal and structural terms) for the coming years have been reviewed downward. In order to try to partly make up for this worse starting position, the annual adjustment of the headline balance is higher in the current update: whereas the previous update provided for a 0.2 p.p. of GDP annual improvement of the headline balance throughout the programme period (i.e. starting in 2007), the current update puts forward an annual improvement of between 0.3 p.p. and 0.4 p.p. of GDP (starting in 2008). In addition, the programme now explicitly mentions that the surplus should be reached without using one-offs and the targets should be achieved against the background of a slightly more pessimistic macroeconomic scenario. As explained in Subsection 4.3, the achievement of both the headline and the structural targets is subject to a number of risks.

Table 6: Evolution of budgetary targets in successive programmes

		2006	2007	2008	2009	2010	2011
General government balance (% of GDP)	SP Apr 2008	0.3	-0.2	0.0	0.3	0.7	1.0
	<i>SP Dec 2006</i>	<i>0.0</i>	<i>0.3</i>	<i>0.5</i>	<i>0.7</i>	<i>0.9</i>	<i>n.a.</i>
	COM Apr 2008	0.3	-0.2	-0.4	-0.6	n.a.	n.a.
General government expenditure (% of GDP)	SP Apr 2008	48.5	48.9	49.0	48.5	48.3	48.2
	<i>SP Dec 2006</i>	<i>49.1</i>	<i>48.6</i>	<i>48.4</i>	<i>48.1</i>	<i>47.8</i>	<i>n.a.</i>
	COM Apr 2008	48.4	48.8	49.0	49.3	n.a.	n.a.
General government revenue (% of GDP)	SP Apr 2008	48.8	48.7	49.0	48.8	48.9	49.2
	<i>SP Dec 2006</i>	<i>49.1</i>	<i>48.9</i>	<i>48.9</i>	<i>48.8</i>	<i>48.7</i>	<i>n.a.</i>
	COM Apr 2008	48.8	48.7	48.7	48.6	n.a.	n.a.
Structural balance ¹ (% of GDP)	SP Apr 2008	-0.4	-0.3	0.0	0.5	1.0	1.4
	<i>SP Dec 2006</i>	<i>-0.4</i>	<i>0.1</i>	<i>n.a.</i>	<i>n.a.</i>	<i>n.a.</i>	<i>n.a.</i>
	COM Apr 2008	-0.6	-0.3	-0.2	-0.1	n.a.	n.a.
Real GDP (% change)	SP Apr 2008	2.8	2.7	1.9	2.0	2.0	2.0
	<i>SP Dec 2006</i>	<i>2.7</i>	<i>2.2</i>	<i>2.1</i>	<i>2.2</i>	<i>2.2</i>	<i>n.a.</i>
	COM Apr 2008	2.8	2.7	1.7	1.5	n.a.	n.a.
Note:							
¹ Cyclically-adjusted balance excluding one-off and other temporary measures. Cyclically-adjusted balances according to the programmes as recalculated by the Commission services on the basis of the information in the programmes. One-off and other temporary measures are 0.7% of GDP in 2006 and -0.1% of GDP in 2007 deficit-reducing according to the most recent programme and -0.9% of GDP in 2006 and -0.1% in 2007, all deficit-reducing, according to the Commission services' spring forecast.							
Source:							
<i>Stability programmes (SP); Commission services' spring 2008 economic forecasts (COM)</i>							

The current programme update also differs from the previous in that it now classifies the “fund for railway infrastructure” (FIF) in the government sector. Up to recently, the Belgian statistical authorities deemed that this fund, which was created in 2005 in the context of the railway restructuring and that assumed 2.5% of GDP of debt from the railway company SNCB, should be classified in the corporate sector, which was contested by Eurostat. Belgium entered a case in the European Court of First Instance, since Eurostat amended the fiscal data reported by Belgium (Case T-403/06, OJ C 42 of 24.02.2007, p.36). In March 2008, Belgium agreed to the Eurostat interpretation of the ESA 95 accounting rules on the sectoral classification of FIF and withdrew the case from court.

This has an impact on both the headline balance and government debt. The difference between the old and the new budget balance figures in relation to the FIF's sectoral classification is relatively small, the new budget balance being 0.1 p.p. of GDP better

than before in each year, except in 2005 where the FIF has a negative impact on the headline balance of 2.4% of GDP. The debt level has increased from 2005 as a result of the new classification of the fund inside the government sector. The difference amounts to 1.4 p.p. of GDP in 2007 and is projected to decline further to 0.7 p.p. of GDP by 2011, according to the programme update (see also section 5.1).

4.2.2. *The composition of the budgetary adjustment*

The improvement of the headline balance over the period 2007-2011 amounts to 1.2 p.p. of GDP and is to be realised through a 0.7 p.p. of GDP reduction in expenditure combined with a 0.5 p.p. of GDP increase in revenue (see Table 7).

According to the programme update, the increase in revenue as a percentage of GDP should not follow from a rise in tax rates but rather from a broadening of the tax base, for instance as a result of the increase in employees' compensation and higher employment, *i.a.* thanks to the intensified activation of unemployed. An important part of the projected increase in revenue should be realised in 2008, in spite of the economic slowdown. Revenue is expected to decrease again in 2009, before increasing strongly in 2011, whereas the growth rate of the different tax bases is broadly stable throughout the programme period. Comparing the revenue projections in the April 2008 update with those in the previous update reveals that the current programme is markedly more optimistic concerning revenue: the current update expects a 0.2% higher government revenue-to-GDP ratio in 2010 in spite of the 0.2% of GDP worse starting position in 2007 and the worse economic environment. The programme does not provide detailed explanations as to the expected development of revenue throughout the programme period.

On the expenditure side, the 0.7% of GDP reduction is to be realised mainly through a reduction of interest expenditure (0.5% of GDP), following the further fall of the government debt. This is broadly in line with the Commission services' spring 2008 forecast for the years 2008 and 2009, with the higher interest rate assumptions in the programme compensating for the expected more rapid reduction of the government debt.

Primary expenditure is to be reduced by 0.2% of GDP (thus accounting for ¼ of the improvement in the primary balance). In particular, the compensation of employees and intermediate consumption should be reduced from 15.5% of GDP in 2007 to 14.9% of GDP in 2011, while this kind of expenditure grew slightly more rapidly than GDP over the last 10 years and that it is expected to stabilise in the Commission services' spring 2008 forecast for the years 2008-2009. The programme does not provide information on measures that should allow for this reduction in expenditure.

The planned reduction in the compensation of employees and intermediate consumption is partly compensated by rising expenditure in certain other fields. Social security expenditure is set to increase by 0.5 p.p. of GDP between 2007 and 2011. As 0.4 p.p. of this increase is expected to already occur in 2008, social security expenditure is projected to develop broadly in line with GDP between 2009 and 2011. This is below the Commission services' spring 2008 forecast, which expects social security expenditure to increase further to 23.3% of GDP in 2009.

Table 7: Composition of the budgetary adjustment

(% of GDP)	2006	2007	2008	2009	2010	2011	Change: 2011-2007
Revenue	48.8	48.7	49.0	48.8	48.9	49.2	0.5
<i>of which:</i>							
- Taxes on production and imports	13.2	12.9	13.1	13.0	n.a.	n.a.	n.a.
- Current taxes on income, wealth, etc.	16.5	16.4	16.5	16.5	n.a.	n.a.	n.a.
- Social contributions	15.7	15.9	15.9	16.0	n.a.	n.a.	n.a.
- Other (residual)	3.4	3.5	3.5	3.3	n.a.	n.a.	n.a.
Expenditure	48.5	48.9	49.0	48.5	48.3	48.2	-0.7
<i>of which:</i>							
- Primary expenditure	44.5	45.1	45.3	45.0	44.9	44.9	-0.2
<i>of which:</i>							
Compensation of employees and intermediate consumption	15.5	15.5	15.4	15.2	15.0	14.9	-0.6
Social payments	22.4	22.6	23.0	23.0	23.0	23.1	0.5
Subsidies	1.7	2.0	2.0	1.9	1.9	1.9	-0.1
Gross fixed capital formation	1.7	1.7	1.7	1.6	1.6	1.8	0.1
Other (residual)	3.2	3.3	3.4	3.3	3.4	3.3	0.0
- Interest expenditure	4.0	3.8	3.7	3.5	3.4	3.3	-0.5
General government balance (GGB)	0.3	-0.2	0.0	0.3	0.7	1.0	1.2
Primary balance	4.3	3.7	3.7	3.8	4.1	4.3	0.6
One-off and other temporary measures	0.7	-0.1	0.0	0.0	0.0	0.0	0.1
GGB excl. one-offs	-0.4	-0.1	0.0	0.3	0.7	1.0	1.1
Output gap ¹	0.1	0.3	-0.1	-0.4	-0.5	-0.8	-1.1
Cyclically-adjusted balance ¹	0.3	-0.4	0.0	0.5	1.0	1.4	1.8
Structural balance²	-0.4	-0.3	0.0	0.5	1.0	1.4	1.7
<i>Change in structural balance</i>		<i>0.2</i>	<i>0.3</i>	<i>0.5</i>	<i>0.5</i>	<i>0.4</i>	
Structural primary balance ²	3.5	3.5	3.7	4.0	4.4	4.7	1.2
<i>Change in structural primary balance</i>		<i>0.0</i>	<i>0.2</i>	<i>0.3</i>	<i>0.4</i>	<i>0.3</i>	
Notes:							
¹ Output gap (in % of potential GDP) and cyclically-adjusted balance as recalculated by Commission services on the basis of the information in the programme.							
² Structural (primary) balance = cyclically-adjusted (primary) balance excluding one-off and other temporary measures.							
<i>Source:</i>							
<i>Stability programme; Commission services' calculations.</i>							

The programme moreover mentions that these projections do not include the impact of the plans to raise certain pensions and social benefits and to further lower the tax wedge on labour included in the government agreement³⁶ and which could be expected to be implemented in the coming years. Public investment is set to decrease from 1.7% of GDP in 2007 to 1.6% of GDP in 2009 and 2010, broadly in line with the long-term average (corrected for the one-off sales of real estate in recent years up to 2006). In 2011, public investment is expected to rise to 1.8% of GDP in view of increased investments by municipalities in the run up to local elections in 2012, as observed in previous local elections.

Compared to the December 2006 programme update, expenditure is expected to turn out higher in 2008 and the projected reduction over the programme period is smaller. Given that the current update projects higher revenue as a percentage of GDP and a smaller

³⁶ However, it should be acknowledged that the government agreement also includes measures that should contain expenditure, such as the limitation of the duration of unemployment benefits and the increase of the effective retirement age, or should increase revenue, such as the activation of unemployed.

reduction of expenditure, the consolidation effort in the current update is more geared towards the revenue side.

For 2008, the programme update refers to the main measures that have been included in the budget law that was approved by the Belgian parliament on 22 May 2008 (see Box 4). Although a number of measures were taken in order to achieve a balanced budget, such as a reduction of expenditure growth in the social security system and of the regions and communities, an additional tax on the energy sector and efforts to step up tax fraud detection.

Box 4: The budget for 2008

Given the longer-than-expected time needed to form a government following the federal elections on 10 June 2007, the budget for 2008 could only be agreed by the end of February and was approved by the Parliament on 22 May 2008. The government targets a balanced budget (against a 0.2% of GDP deficit in 2007 and a planned surplus of 0.5% of GDP in the December 2006 update of the stability programme).

The budget includes expenditure-increasing measures (0.1% of GDP), mainly aiming at increasing households' purchasing power. These include i.a. a revalorisation of the lowest pensions and an extension of the measures to cushion the impact of rising heating fuel prices for the most vulnerable households. On the other hand, the decision not to spend part of the health care budget, the agreement that the regions and communities will achieve a 0.1% of GDP surplus and the measures to improve the activation of the unemployed should contain expenditure.

The two main revenue-increasing measures are a specific tax for the energy sector and the reinforcement of fraud detection, especially in the field of corporate taxation (0.1% of GDP each). The budget does not seem to include one-off measures on the basis of currently available information. The planned sale of real estate is limited and does not seem to constitute a one-off, contrary to previous years, given that it concerns the final sale of unused buildings and will not entail additional expenditure in the following years. On the other hand, it is currently not possible to determine whether or not the specific tax for the energy sector is a one-off tax.

The federal government level is expected to reduce its deficit from 1.0% of GDP in 2007 to 0.6% of GDP in 2008. The local governments, which achieved a balanced budget in 2007, should realise a 0.1% of GDP surplus this year. The 2007 surpluses of both the regions and communities and the social security system (of 0.3% and 0.6% of GDP respectively) are set to decrease to 0.1% and 0.4% of GDP respectively.

The structural balance for 2008 provided in the April 2008 update of the stability programme (as recalculated by the Commission on the basis of the information in the programme) points to a broadly neutral budgetary stance.

Main measures in the budget for 2008

Revenue measures*	Expenditure measures**
<ul style="list-style-type: none"> ○ Specific tax on the energy sector (0.1% of GDP) ○ Measures to improve the effectiveness of the fight against tax fraud (0.1% of GDP) 	<ul style="list-style-type: none"> ○ Increase of certain pensions (0.1% of GDP) ○ Agreement not to spend part of the healthcare budget (-0.2% of GDP) ○ Measures to step up the activation of unemployed (-0.1% of GDP) ○ Agreement with regions and communities to achieve a surplus (-0.1% of GDP)

* Estimated impact on general government revenue.

** Estimated impact on general government expenditure.

Sources: Commission services and Chambre des Représentants de Belgique, Budget des recettes et des dépenses: exposé général.

The programme explicitly mentions that the targets will be achieved in a structural way which implies that the new government should refrain from using one-offs in order to achieve the targets put forward. As far as 2008 is concerned, the budget does not seem to contain one-offs (with the possible exception of the tax on the energy sector which is not yet sufficiently specified in order to determine whether or not it concerns a one-off tax).

The budgetary adjustment foreseen in the programme would be mainly the result of fiscal consolidation by the federal government, which is planned to move from a 0.2% of GDP deficit in 2007 to a 1.0% of GDP surplus in 2011. This is in line with the fact that the reduction in interest expenditure will mainly fall on the federal level given that the bulk of the government debt belongs to the federal level. Awaiting an agreement between the federal level and the regions and communities regarding the latter's contribution to fiscal consolidation as from 2009, the programme assumes the federal government to achieve a balanced budget in 2009-2011. The local government level will obtain a slightly higher surplus in 2009 and 2010, but in view of the local elections in 2012 this surplus is set to decrease again in 2011, according to the update. The social security system is set to achieve a 0.4% of GDP surplus in 2008 (compared to 0.6% of GDP in 2007), which is expected to slightly increase to 0.6% of GDP by 2011.

4.3. Risk assessment

This section discusses the plausibility of the programme's budgetary projections by analysing various risk factors. For the period until 2009, Table 8 compares the detailed revenue and expenditure projections in the Commission services' spring 2008 forecast, which are derived under a no-policy change scenario, with those in the updated programme.

As concluded in Section 3.3, the macroeconomic scenario appears favourable for 2008 and even more for 2009, both as regards GDP growth and the development of employment. This is broadly confirmed by the most recent projections of the Federal Planning Bureau. Lower GDP growth will have an impact, through the functioning of the automatic stabilisers, on government revenue and, to a lesser extent, expenditure. In particular, the Commission services expect both household disposable income and consumption, two important tax bases, to grow considerably less in 2008 and 2009 than forecast in the programme update. In addition, higher unemployment, as projected in the Commission services' spring 2008 forecast, in particular for 2009, may have an impact on expenditure. The less benign environment constitutes a clear risk to the achievement of the headline targets.

While GDP growth in the programme update seems broadly plausible as from 2010, employment growth projections may turn out slightly optimistic in view of the below-potential growth also in these years. This may even be the case if employment growth is to be supported by intensified activation measures (which have not yet proven their effectiveness, especially in a more negative economic environment), as mentioned in the programme update. In case employment were to increase less, this would negatively affect government revenue.

The sensitivity analysis in the programme update shows that a reduction in GDP growth by 0.5% would lead to a headline balance which is 0.3% below the initial target in 2008, 0.2% lower in 2009 and 0.1% lower in 2010 and 2011. Commission services' simulations of the cyclically-adjusted balance under the assumptions of (i) a sustained 0.5 percentage point deviation from the real GDP growth projections in the programme over the 2007-2011 period; (ii) trend output based on the HP-filter and (iii) no policy response (notably, the expenditure level is as in the central scenario), reveal that, by 2011, the cyclically-

adjusted balance is 1.0 p.p. of GDP below the central scenario. Hence, in the case of persistently lower real growth, additional measures of around 1.0 percentage point of GDP would be necessary to keep the public finances on the path targeted in the central scenario.

Table 8: Comparison of budgetary developments and projections

(% of GDP)	2006	2007		2008		2009		2010	2011
	COM	COM	SP	COM	SP	COM ¹	SP	SP	SP
Revenue	48.8	48.7	48.7	48.7	49.0	48.6	48.8	48.9	49.2
<i>of which:</i>									
- Taxes on production and imports	13.2	12.9	12.9	13.0	13.1	13.0	13.0	n.a.	n.a.
- Current taxes on income, wealth, etc.	16.5	16.4	16.4	16.4	16.5	16.5	16.5	n.a.	n.a.
- Social contributions	15.7	15.9	15.9	16.0	15.9	16.0	16.0	n.a.	n.a.
- Other (residual)	3.4	3.4	3.5	3.3	3.5	3.2	3.3	n.a.	n.a.
Expenditure	48.5	48.9	48.9	49.1	49.0	49.3	48.5	48.3	48.2
<i>of which:</i>									
- Primary expenditure	44.5	45.0	45.1	45.4	45.3	45.7	45.0	44.9	44.9
<i>of which:</i>									
Compensation of employees and intermediate consumption	15.4	15.5	15.5	15.5	15.4	15.5	15.2	15.0	14.9
Social payments	22.4	22.6	22.6	22.9	23.0	23.3	23.0	23.0	23.1
Subsidies	1.7	2.0	2.0	2.1	2.0	2.1	1.9	1.9	1.9
Gross fixed capital formation	1.7	1.7	1.7	1.7	1.7	1.7	1.6	1.6	1.8
Other (residual)	3.2	3.3	3.3	3.3	3.4	3.3	3.3	3.4	3.3
- Interest expenditure	4.0	3.9	3.8	3.7	3.7	3.6	3.5	3.4	3.3
General government balance (GGB)	0.3	-0.2	-0.2	-0.4	0.0	-0.6	0.3	0.7	1.0
Primary balance	4.3	3.7	3.7	3.3	3.7	2.9	3.8	4.1	4.3
One-off and other temporary measures	0.9	-0.1	-0.1	0.0	0.0	0.0	0.0	0.0	0.0
GGB excl. one-offs	-0.6	-0.1	-0.1	-0.4	0.0	-0.6	0.3	0.7	1.0
Output gap ²	0.1	0.3	0.3	-0.3	-0.1	-1.0	-0.4	-0.5	-0.8
Cyclically-adjusted balance ²	0.3	-0.3	-0.4	-0.2	0.0	-0.1	0.5	1.0	1.4
Structural balance³	-0.6	-0.3	-0.3	-0.2	0.0	-0.1	0.5	1.0	1.4
<i>Change in structural balance</i>		0.4	0.2	0.0	0.3	0.1	0.5	0.5	0.4
Structural primary balance ³	3.4	3.6	3.5	3.4	3.7	3.4	4.0	4.4	4.7
<i>Change in structural primary balance</i>		0.2	0.0	-0.1	0.2	0.0	0.3	0.4	0.3
Notes:									
¹ On a no-policy-change basis.									
² Output gap (in % of potential GDP) and cyclically-adjusted balance according to the programme as recalculated by Commission services on the basis of the information in the programme.									
³ Structural (primary) balance = cyclically-adjusted (primary) balance excluding one-off and other temporary measures.									
<i>Source:</i>									
Stability programme (SP); Commission services' spring 2008 economic forecasts (COM); Commission services' calculations									

Throughout the programme period, wages are expected to rise considerably more than the long-term average. Whereas, in 2008, dynamic wage developments can be explained on the basis of the expected high inflation (although the inflation forecast in the programme update still seems relatively low), this is no longer the case for the outer years. Indeed, for these years, the programme expects wage increases above those expected in 2008 in combination with particularly low inflation rates, which does not seem to be consistent. A more moderate development of wages as of 2009 could clearly lead government revenue to fall short of the projections in the programme update.

Tax revenue projections in the programme update are based on an expected high tax intensity of economic activity, in particular in 2008 (see Table 9). The programme

expects the tax-to-GDP ratio to increase by 0.3%, mainly resulting from a high tax elasticity this year: 1.2, compared to 1.0 in the Commission services' spring 2008 forecast (equal to the OECD standard elasticity). The expected increase in the tax-to-GDP ratio seems unwarranted in view of the macroeconomic scenario of the programme. Higher-than-projected inflation may lead to a higher tax elasticity, given that income brackets in the personal income tax system are indexed to consumer price inflation with a lag (an opposite effect would then be expected in 2009). However, the Commission services' spring forecast already expects higher inflation than the programme (3.6% vs. 3.0%) and still projects a lower tax elasticity than the programme. Even though since the finalisation of the spring forecast, inflation has surprised on the upside, the programme's tax elasticity even appears on the high side in the current circumstances (especially in view of measures to reduce labour taxation and of the non-repetition of one-off revenues achieved in 2007).

Table 9: Assessment of tax projections

	2008			2009			2010	2011
	SP	COM	OECD ³	SP	COM ¹	OECD ³	SP	SP
Change in tax-to-GDP ratio (total taxes)	0.3	0.1	0.0	0.0	0.1	0.0	n.a.	n.a.
Difference (SP – COM)	0.2		/	-0.1		/	/	/
<i>of which</i> ² :								
- discretionary and elasticity component	0.4		/	-0.1		/	/	/
- composition component	-0.1		/	0.1		/	/	/
Difference (COM - OECD)	/	0.1		/	0.1		/	/
<i>of which</i> ² :								
- discretionary and elasticity component	/	-0.3		/	-0.1		/	/
- composition component	/	0.5		/	0.2		/	/
p.m.: Elasticity to GDP	1.2	1.0	1.0	1.0	1.0	1.0	n.a.	n.a.
<u>Notes:</u>								
¹ On a no-policy change basis.								
² The composition component captures the effect of differences in the composition of aggregate demand (more tax rich or more tax poor components). The discretionary and elasticity component captures the effect of discretionary fiscal policy measures as well as variations of the yield of the tax system that may result from factors such as time lags and variations of taxable income that do not necessarily move in line with GDP, e.g. capital gains. The two components may not add up to the total difference because of a residual component, which is generally small.								
³ OECD ex-ante elasticity relative to GDP.								
<u>Source:</u>								
<i>Commission services' spring 2008 economic forecasts (COM); Stability programme (SP); Commission services' calculations; OECD (N. Girouard and C. André (2005), "Measuring Cyclically-Adjusted Budget Balances for the OECD Countries", OECD Working Paper No. 434).</i>								

Overall, the optimistic macroeconomic and tax revenue projections in the current programme update may lead to an overestimation of government revenue over the programme period. As the programme update foresees the consolidation effort to be largely concentrated on the revenue side (when excluding the decline in interest expenditure), this may have a considerable impact on the achievement of the surplus targets.

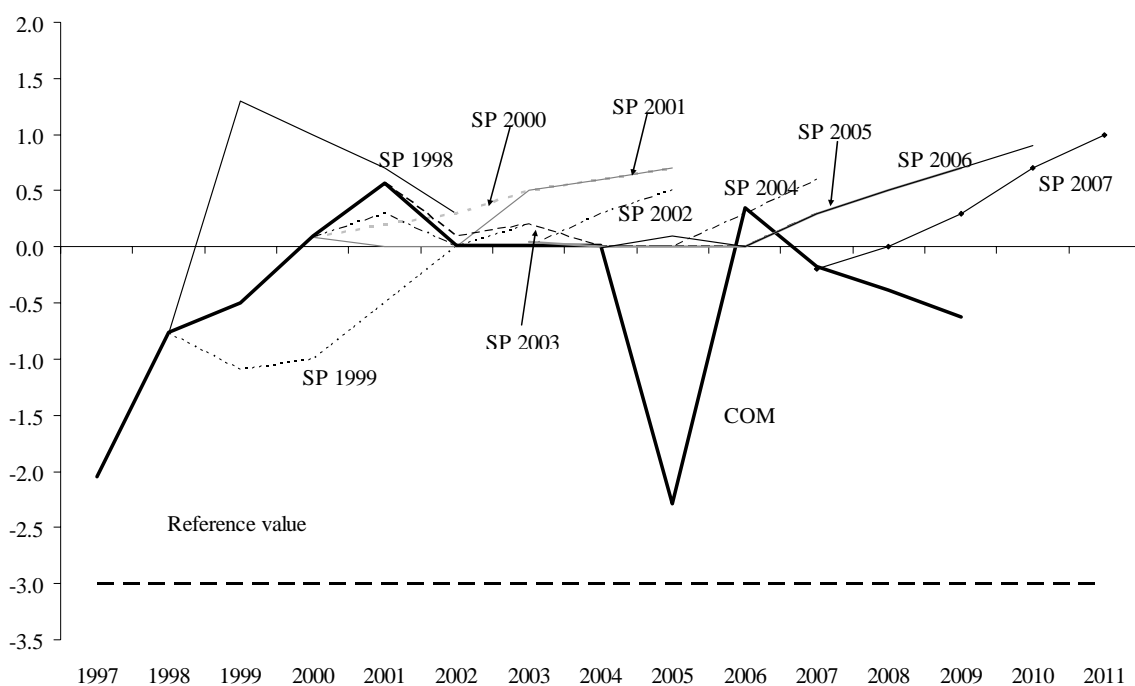
The achievement of the budget balance is also subject to the risk that the reduction in primary expenditure, which is quite limited, will not materialise as planned, in particular as no measures were included in the programme to ensure that the targets are met. However, reducing primary expenditure by 0.2 p.p. of GDP as programmed, in a context of rising ageing-related costs and the projected rapid wage increases (impacting the government wage bill), is likely to require additional measures. Indeed, the planned reduction in government consumption and wages seems on the high side, in particular in view of high inflation and the high projected increase in wages. In addition, social

security expenditure could increase more than projected in view of ageing and a number of measures taken in recent years to increase certain pensions and social security allocations. Finally, unemployment benefits could be underestimated as unemployment may turn out higher than projected in the programme.

Besides the fact that the planned reduction in expenditure does not seem sufficiently backed by measures, the programme update only plans a relatively limited effort on the expenditure side, also compared to the previous programme update, possibly reducing the sustainability of the consolidation effort.

Another risk relates to the fact that the Belgian authorities have a mixed track record in achieving budgetary targets. In particular, the Belgian authorities have in subsequent programme updates postponed the realisation of headline surpluses (see Figure 4). In spite of the good macroeconomic environment in 2007, the target has not been reached and also in 2008 the target may be missed in the absence of further measures.

Figure 4: government balance projections in successive programmes (% of GDP)



Source: Commission services' spring 2008 forecast (COM) and successive stability/convergence programmes

Finally, the possible further mounting of tensions in the run-up to the regional elections in 2009, may not constitute an enabling environment for the achievement of the budgetary targets and the implementation of structural deficit-reducing measures.

The consolidation in structural terms is subject to the additional risk that the negative output gap on the basis of which the structural balances have been calculated will be smaller than expected in the programme update (recalculated by the Commission services), as explained in Box 2. As a consequence, the improvement of the structural balance should be interpreted with caution. Replacing the output gap calculated on the basis of the information in the programme with an output gap calculated on the basis of a higher NAWRU (comparable to the one in the Commission services' spring 2008 forecast) throughout the programme period (see Section 3) would lead to a 0.1% of GDP smaller improvement of the structural balance for all years.

Taking the above into account, there is a clear risk that the budgetary outcomes, both in nominal and structural terms, will be worse than targeted in the programme throughout the entire programme period.

4.4. Assessment of the fiscal stance and budgetary strategy

Table 10 offers a summary assessment of the country's position relative to the budgetary requirements laid down in the Stability and Growth Pact. In order to highlight the role of the preceding analysis of the risks that are attached to the budgetary targets presented in the programme, this assessment is done in two stages: first, a preliminary assessment on the basis of the targets taken at face value and, second, the final assessment also taking into account risks.

Table 10: Overview of compliance with the Stability and Growth Pact

	Based on programme⁴ (with the targets taken at face value)	Assessment (taking into account risks to the targets)
• Safety margin against breaching 3% of GDP deficit limit ¹	Throughout the programme period	Throughout the programme period
• Achievement of the MTO	From 2009 onwards	Not before 2010
• Adjustment towards MTO in line with the Pact ² ?	Should be strengthened in 2008 and broadly in line thereafter	Should be strengthened in 2008 and backed by measures thereafter, in particular on the expenditure side
• Fiscal stance in line with Pact ³ (after achievement of the MTO)?	In line	Not applicable
<p><u>Notes:</u></p> <p>¹The risk of breaching the 3% of GDP deficit threshold with normal cyclical fluctuations, i.e. the existence of a safety margin, is assessed by comparing the cyclically-adjusted balance with the above mentioned minimum benchmark (estimated as a deficit of around 1¼% of GDP for Belgium). These benchmarks represent estimates and as such need to be interpreted with caution.</p> <p>²The Stability and Growth Pact requires Member States to make progress towards their MTO (for countries in the euro area or in ERM II, this has been quantified as an annual improvement in the structural balance of at least 0.5% of GDP as a benchmark). In addition, the structural adjustment should be higher in good times, whereas it may be more limited in bad times.</p> <p>³According to the Stability and Growth Pact, countries which have already achieved their MTO should avoid pro-cyclical fiscal policies in “good times”.</p> <p>⁴Targets in structural terms as recalculated by Commission services on the basis of the information in the programme.</p> <p><u>Source:</u> Commission services</p>		

The budgetary stance in the programme provides a sufficient safety margin against breaching the 3% of GDP deficit threshold with normal macroeconomic fluctuations throughout the programme horizon. The outlined budgetary stance should enable Belgium to reach the MTO within the programme period, although this may happen somewhat later than foreseen in the programme (i.e. 2009) in view of the various risks mentioned above.

The choice of a more demanding MTO than strictly required in view of the high debt ratio and the long term potential growth is part of Belgium's forward-looking strategy to prepare for the ageing shock by building up increasing primary surpluses and reducing the debt ratio (see Section 2). However, reaching the MTO alone would not permit to achieve the planned pre-funding of the budgetary cost of ageing. In so far as the Belgian authorities do not bring changes to their strategy to deal with the budgetary cost of

ageing, for instance by focusing more on structural reforms, a continued restrictive budgetary stance would be required once the MTO has been achieved. The further improvement of the headline balance projected in the programme update is broadly in line with the long-term sustainability path proposed by the HFC (see Section 2), which requires a primary surplus of 4.4% in 2012 (the programme update plans to achieve a 4.3% of GDP primary surplus in 2011). However, because of the lower primary surpluses included in the programme update up to 2011, the debt reduction will be smaller than proposed by the HFC.

As regards the adjustment path towards the MTO, the structural balance is expected to improve by around ¼% of GDP and reach a balanced position in 2008 (according to the programme), after which the adjustment is expected to accelerate to ½%, so that the MTO would be reached in 2009. Taking into account the risks related to the budgetary outcome, the adjustment towards the MTO is likely to turn out to be smaller than the 0.5% benchmark for euro area and ERM II countries, not only in 2008 but also in 2009 and should therefore be strengthened in 2008 and backed by measures in 2009. The slow adjustment towards the MTO cannot be attributed to cyclical conditions, as Belgium appears to be neither in economic good nor bad times and tax elasticities in 2008 and 2009 are estimated to be slightly better than in the previous years, *i.a.* as a result of a less negative impact of discretionary measures.

5. GOVERNMENT DEBT AND LONG-TERM SUSTAINABILITY

This section is in two parts. A first part describes recent debt developments and medium-term prospects, including risks to the outlook presented in the programme. A second part takes a longer-term perspective with the aim of assessing the long-term sustainability of public finances.

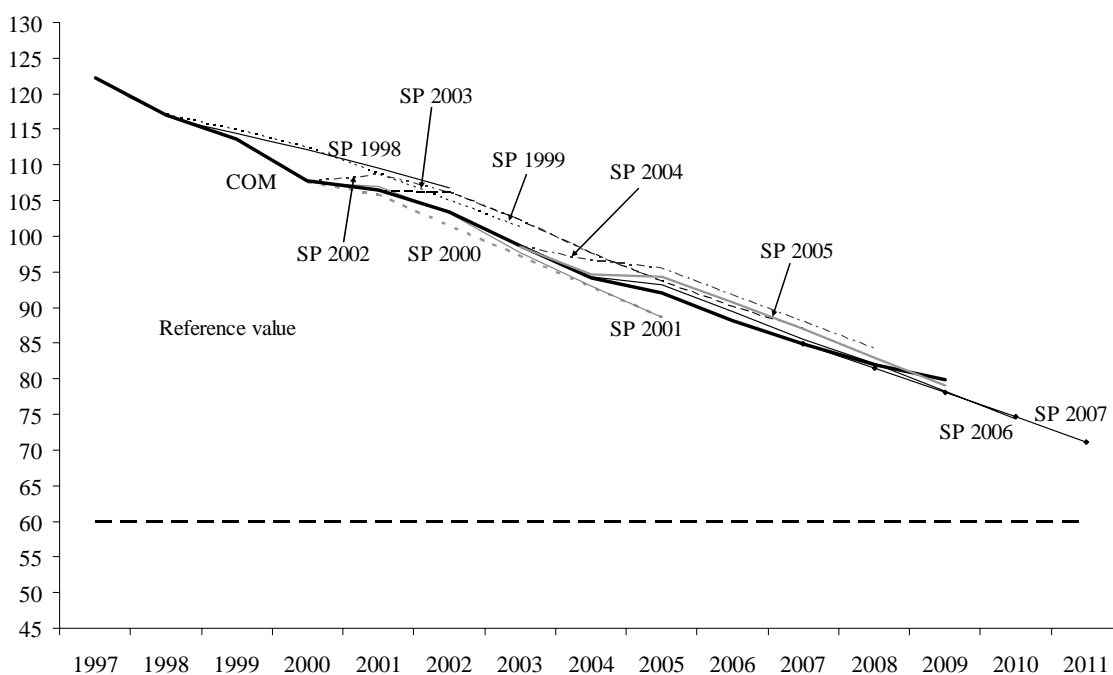
5.1. Recent debt developments and medium-term prospects

5.1.1. Debt projections in the programme

The Belgian debt ratio has been on a steady downward path since 1993 (when it stood at 134% of GDP) until today (84.9% of GDP at the end of 2007, see Figure 5). This important decline mainly stems from high – though decreasing – primary surpluses. The debt development also benefited from declining interest expenditure. The assumption of the SNCB/NMBS debt in 2005 caused a temporary slowdown of the trend, but without reversing it.³⁷ Increasing the primary balance to around 4.3% of GDP as foreseen in the programme should ensure the continuation of the reduction of the still high debt ratio. The path is broadly comparable to those provided in previous programme updates and in particular the last one. The update does not foresee major operations (such as privatisations) affecting the debt through the stock-flow adjustment.

³⁷ Note that the December 2006 programme update did not include the SNCB/NMBS debt due to the classification of the Fund for Railway Infrastructure outside the government sector, which was contested by Eurostat. In the current update, the classification of the FIF is consistent with the Eurostat view.

Figure 5: Debt projections in successive programmes (% of GDP)



Source: Commission services' spring 2008 forecast (COM) and successive stability programmes

Table 11: Debt dynamics

(% of GDP)	average 2002-05	2006	2007		2008		2009		2010	2011
			COM	SP	COM	SP	COM	SP	SP	SP
Gross debt ratio¹	97.1	88.2	84.9	84.9	81.9	81.5	79.9	78.1	74.7	71.1
Change in the ratio	-3.6	-3.9	-3.3	-3.3	-2.9	-3.4	-2.0	-3.4	-3.4	-3.6
<i>Contributions²:</i>										
Primary balance	-4.4	-4.3	-3.7	-3.7	-3.3	-3.7	-2.9	-3.8	-4.1	-4.3
"Snow-ball" effect	1.3	-0.2	0.2	0.2	0.1	0.0	0.7	0.3	0.4	0.5
<i>Of which:</i>										
Interest expenditure	5.0	4.0	3.8	3.9	3.7	3.7	3.6	3.5	3.4	3.3
Growth effect	-1.7	-2.5	-2.3	-2.3	-1.3	-1.5	-1.2	-1.6	-1.5	-1.4
Inflation effect	-2.0	-1.7	-1.4	-1.4	-2.2	-2.2	-1.7	-1.6	-1.5	-1.4
Stock-flow adjustment	-0.4	0.7	0.2	0.2	0.2	0.3	0.2	0.1	0.3	0.3
<i>Of which:</i>										
Cash/accruals diff.	0.3	0.7	-0.4	n.a.		n.a.		n.a.	n.a.	n.a.
Acc. financial assets	-0.6	0.0	0.6	n.a.		n.a.		n.a.	n.a.	n.a.
Privatisation	-0.1	0.0	n.a.	n.a.		n.a.		n.a.	n.a.	n.a.
Val. effect & residual	-0.1	0.0	0.0	n.a.		n.a.		n.a.	n.a.	n.a.

Notes:

¹End of period.

²The change in the gross debt ratio can be decomposed as follows:

$$\frac{D_t}{Y_t} - \frac{D_{t-1}}{Y_{t-1}} = \frac{PD_t}{Y_t} + \left(\frac{D_{t-1}}{Y_{t-1}} * \frac{i_t - y_t}{1 + y_t} \right) + \frac{SF_t}{Y_t}$$

where t is a time subscript; D , PD , Y and SF are the stock of government debt, the primary deficit, nominal GDP and the stock-flow adjustment respectively, and i and y represent the average cost of debt and nominal GDP growth (in the table, the latter is decomposed into the growth effect, capturing real GDP growth, and the inflation effect, measured by the GDP deflator). The term in parentheses represents the "snow-ball" effect. The stock-flow adjustment includes differences in cash and accrual accounting, accumulation of financial assets and valuation and other residual effects.

Source:

Stability programme (SP); Commission services' spring 2008 economic forecasts (COM); Commission services' calculations

5.1.2. Assessment

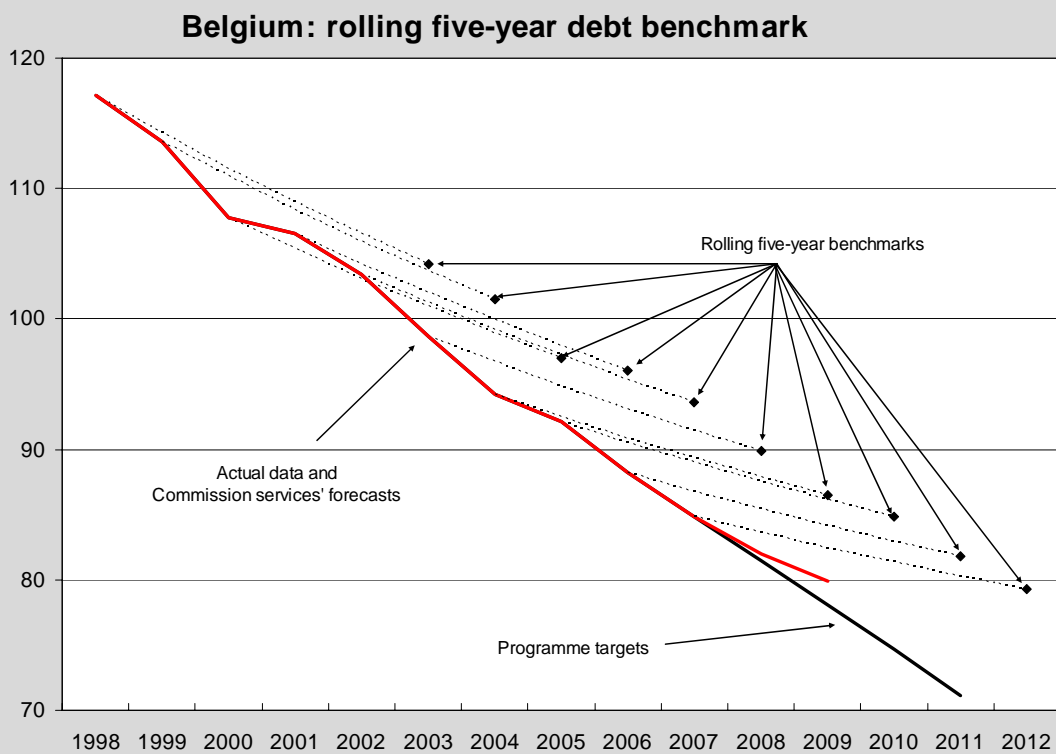
Overall, the differences between the Commission services' forecast for the debt ratio and the targets in the April 2008 update of the programme are relatively small and explained by the less optimistic budgetary outcomes (see also Section 4.3 above) and lower projected GDP growth (see also Section 3.1 above) in the Commission services' forecast, partly compensated by the lower interest rate assumptions in the Commission services' forecast (see Table 11). Other than the risks attached to the budgetary outcomes mentioned before, the specific risks related to debt developments seem broadly balanced.

Box 5: The rolling debt reduction benchmark

The debt ratio has exceeded the 60% of GDP reference value since the presentation of the initial stability programme in 1998.

A tentative assessment of the pace of debt reduction over a medium-term horizon is presented in the accompanying graph. It shows historical data, the Commission services' spring 2008 forecasts until 2009 (which are on a no-policy change scenario) and the multi-annual debt projections in the update and compares them with the paths obtained by applying an illustrative "rolling debt reduction benchmark" (*). The benchmark reflects the idea that a minimum debt reduction should be ensured not year after year but over a medium-term horizon (five years in the graph). For instance, the debt projection for 2008 is compared with the value obtained for the same year by applying the formula starting in 2003. Debt level projections in the programme exceeding those obtained by applying the benchmark are taken as an indicator of a slow reduction in the debt ratio.

The graph clearly shows that the planned reduction of the debt ratio in the update is more than implied by the five-year rolling debt reduction benchmark.



Source: Stability programme and Commission services

(* The rolling debt reduction benchmark for successive five-year periods is defined as a reduction in the difference between the debt ratio and the 60% of GDP reference value of 5 percent per year:

$$\left(\frac{D_{t+1}}{Y_{t+1}}\right)_{\text{benchmark}} = \left(\frac{D_t}{Y_t}\right)_{\text{benchmark}} - 5\% \times \left[\left(\frac{D_t}{Y_t}\right)_{\text{benchmark}} - 60\right],$$

where t is a time subscript and D and Y are the stock of government debt and nominal GDP, respectively. In the first year of the five-year period, the debt ratio in the previous year is the actual debt ratio. Given the usual approximation of the change in the debt ratio $\frac{D_t}{Y_t} - \frac{D_{t-1}}{Y_{t-1}} = \frac{DEF_t}{Y_t} - \frac{y_t}{1+y_t} \times \frac{D_{t-1}}{Y_{t-1}} \cong \frac{DEF_t}{Y_t} - y_t \times \frac{D_{t-1}}{Y_{t-1}}$ and assuming that the stock-flow adjustment is zero, it is easy to show that the rolling debt reduction benchmark describes the path for convergence of the debt ratio towards 60% of GDP which would take place with the deficit at 3% of GDP and nominal GDP growth at 5%. In other words, the 5 percent per year benchmark is the value that makes consistent a continuous respect of the 3% of GDP deficit threshold and an asymptotic respect of the 60% of GDP debt reference value.

Over the past decade, the structure of Belgian public debt has been gradually improved to reduce the interest rate sensitivity of the debt. Profiting from low interest rates, the term structure of the debt has been geared gradually towards long-term debt; debt with a residual maturity of more than 1 year (and generally carrying fixed interest rates) amounts to around 88% of GDP (2006 figure for the federal government level, which carries over 90% of total government debt according to the programme update). The effective duration of the federal government debt amounted to about 4.5 years in 2006, so that an increase in interest rates only has a gradual and lagged impact on interest expenditure. The programme update projects that a 100 basis points increase of interest rates would drive up interest expenditure by about ¼% of GDP throughout the programme period. Since the introduction of the euro, the debt denominated in foreign currency represents less than 1% of GDP, thereby almost eliminating exchange rate risks.

In view of the strong sustained downward trend and also taking into account the abovementioned risks, the debt ratio can be considered to be sufficiently diminishing towards the reference value over the programme period (see also Box 5).

5.2. Long-term debt projections and the sustainability of public finances

This section analyses the long-term sustainability of public finances. It uses long-term projections of age-related expenditures to calculate sustainability gap indicators and make long-term government debt projections so as to assess the sustainability challenge the country concerned is facing. The issue is already touched upon in Section 2, which deals with the combination of fiscal consolidation and a reduction of labour taxation in order to ensure long-term sustainability of public finances.

5.2.1. Sustainability indicators and long-term debt projections

Table 12 shows the evolution of government spending on pensions, healthcare, long-term care for the elderly, education and unemployment benefits according to the EPC's projections and property income received by general government according to an agreed methodology.³⁸ Non age-related primary expenditure and primary revenue is assumed to remain constant as a share of GDP.

The projected increase in age-related spending in Belgium is significantly above the EU average, rising by 6.3% points of GDP between 2004 and 2050. This is particularly due to pension expenditure being projected to rise more than on average in the EU, by 5.1% points of GDP. The increase in health-care expenditure is projected to be 1.4% points of GDP, lower than on average in the EU. For long-term care, the projected increase of 1.0% points up to 2050, is above the average in the EU.

³⁸ See the accompanying "methodological paper" for a description of the property income projections. These projections differ from those of the HFC's Study Committee on Ageing, as explained below.

Table 12: Long-term age-related expenditure: main projections

(% of GDP)	2004	2010	2020	2030	2040	2050	Change up to 50
Total age-related spending	25.4	25.1	26.6	29.9	31.6	31.7	6.3
- Pensions	10.4	10.4	12.1	14.7	15.7	15.5	5.1
- Healthcare	6.2	6.4	6.8	7.1	7.5	7.6	1.4
- Long-term care	0.9	0.9	1.1	1.3	1.6	1.8	1.0
- Education	5.6	5.2	4.9	5.0	5.0	5.0	-0.7
- Unemployment benefits	2.3	2.0	1.8	1.8	1.7	1.8	-0.5
Property income received	0.7	0.6	0.6	0.5	0.5	0.5	-0.2

Source: Economic Policy Committee and Commission services.

Based on the long-term budgetary projections, sustainability indicators can be calculated. Table 13 shows the sustainability indicators for the two scenarios; the 2007 scenario assumes that the structural primary balance in 2007 is unchanged for the rest of the programme period and the programme scenario assumes that the programme's budgetary plans are fully attained.

Table 13: Sustainability indicators and the required primary balance

Value	2007 scenario			Programme scenario		
	S1	S2	RPB	S1	S2	RPB
Value	1.6	3.0	6.3	0.4	1.8	6.3
<i>of which:</i>						
Initial budgetary position (IBP)	-2.5	-2.4	-	-3.7	-3.6	-
Debt requirement in 2050 (DR)	0.3	-	-	0.2	-	-
Long-term change in the primary balance (LTC)	3.8	5.4	-	3.8	5.4	-

Source: Commission services.

In the “2007 scenario”, the sustainability gap (S2) which satisfies the intertemporal budget constraint would be 3% of GDP.³⁹ The sustainability gap has widened by ¼ percentage points compared with last year's assessment. This is mainly due to a reduction in the estimated structural primary surplus in 2007 as recalculated by the Commission services (at 3.4% of GDP) compared with the structural primary balance in 2006 estimated in the December 2006 assessment (at 3.7% of GDP).

The initial rather strong budgetary position contributes to the reduction of gross debt and the accumulation of financial assets, but would not suffice to cover the long-term cost of ageing. The programme plans a structural primary budgetary consolidation of 1.2% of GDP between 2007 and 2010. If achieved, such a consolidation would appreciably reduce risks to long-term sustainability of public finances by reducing the S2 sustainability gap to 1.8% of GDP (“programme scenario”). The difference between the initial budgetary position in the “2007 scenario” and the “programme scenario” illustrates how the full respect of the stability programme targets would contribute to tackling the budgetary challenges raised by the demographic developments.

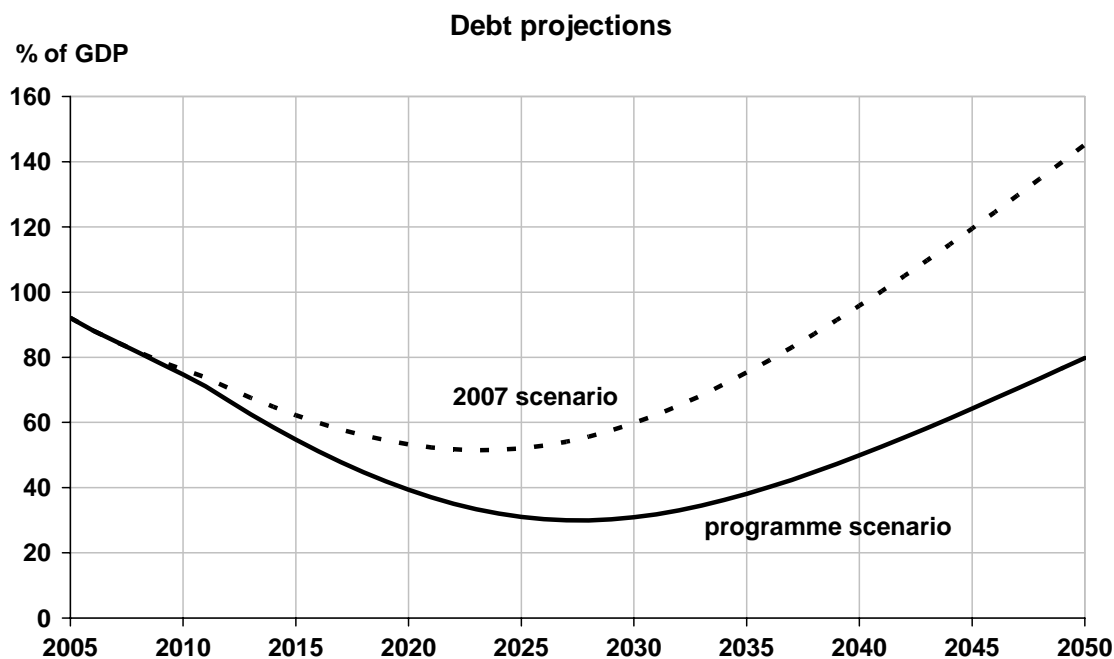
The required primary balance (RPB) is over 6¼% of GDP, which is higher than the structural primary balance of about 4.7% of GDP in the last year of the programme period.

The sustainability gap indicators would increase by up to ¼% of GDP if the planned budgetary adjustment was to be postponed by 5 years, highlighting that budgetary savings can be made if action is taken sooner rather than later.

³⁹ The sustainability gap (S1) that assures reaching the debt ratio of 60% of GDP by 2050 would be 1.6% of GDP.

Another way to look at the prospects for long-term public finance sustainability is to project the debt/GDP ratio over the long-term using the same assumptions as for the calculations of the sustainability indicators. The long-term projections for government debt under the two scenarios are shown in Figure 6. At 84.9% of GDP, the gross debt ratio has exceeded the 60%-of-GDP reference value in 2007. According to the “2007 scenario”, the debt ratio is projected to fall below the 60%-of-GDP reference value by 2015 but to exceed it after 2030, reaching about 145% of GDP by 2050. In the “programme scenario”, thanks to the stronger budgetary position in 2011, debt would fall below 60% of GDP a little earlier and remain so up to the mid-2040s, but reach finally about 80% of GDP by 2050.⁴⁰

Figure 6: Long-term projections for the government debt ratio



Source: Commission services

5.2.2. Additional factors

To reach an overall assessment of the sustainability of public finances, other relevant factors are taken into account, which in addition allow to better appreciate where the main risks to sustainability are likely to stem from.

First, the current level of debt is still high, although it has been resolutely reduced for many years. Indeed, debt reduction is the backbone of the Belgian strategy to face ageing.⁴¹ Ensuring a reduction of debt to below the 60% of GDP reference value at a satisfactory pace is necessary to strengthen the resilience of public finances to adverse shocks and to reduce public finance sustainability risks.

⁴⁰ It should be recalled, however, that being a mechanical, partial-equilibrium analysis, the long-term debt projections are bound to show highly accentuated profiles. As a consequence, the projected evolution of debt levels should not be seen as a forecast similar to the Commission services' short-term forecasts, but as an indication of the risks faced by Member States.

⁴¹ The reduction of the government debt as a strategy to prepare for the ageing of population is often described in connection with the existence of an ageing fund. The ageing fund, however, holds debt of other government sectors, which therefore is consolidated in general government debt and does not reduce net debt further.

Second, the projections of the programme are not those of the Ageing Report. They are based on different demographic and macroeconomic assumptions. The programme makes a reference to national projections made by the HFC's Study Committee on Ageing (see also Section 2), which would differ from the common projections of the Ageing Report by three factors, which are (i) the former is based on more recent data and different methodology, (ii) it revised past data and (iii) includes more recent policy measures. The effect of (i) on the sustainability gaps would be very small.⁴² In its June 2007 Report, the Committee takes issues (ii) and (iii) into account. *Ceteris paribus*, the Committee finds that the data revision (wage data in national accounts) would reduce the increase in age-related costs between 2004 and 2050 by little (0.3% of GDP). As for (iii), the *Generation Pact* (adopted in autumn 2005) was intended to raise the effective retirement age. Its principal measures were the increase in the threshold age for eligibility of early retirement and a pension supplement for those who continued working after 62 (the statutory retirement age is at 65 years). The Committee finds – on the basis of the common projections for the Ageing Report – that the first measure would reduce the increase in pension expenditure by 0.1% of GDP between 2004 and 2050, while the second would result in an increase by 0.3% of GDP.⁴³ Therefore, both the wage data revision and the most recent pension reform would not alter the sustainability gaps by much.⁴⁴

Third, the tax burden on labour in Belgium is among the highest in the EU and the government's current strategy is to reduce it. These measures, aiming at increasing employment rates and fostering growth, could therefore ease pressure on public finances in the long term, though it may reduce revenue in the short term (see Section 2).

5.2.3. Assessment

Belgium appears to be at medium risk with regard to the sustainability of public finances.

The long-term budgetary impact of ageing is above the EU-27 average, influenced notably by a relatively high increase in pension expenditure as a share of GDP over the coming decades. The effective retirement age in Belgium is one of the lowest in the EU, and raising it is the aim of the *Generation Pact* which brought a number of changes to the

⁴² In its May 2006 Report, the Committee provides a comparison between its own projections (with somewhat different demographic and macroeconomic projections) and those of the Ageing Report, both excluding the effects of the most recent pension reform (*Generation Pact*). According to these national projections (excluding the *Generation Pact*), pension expenditure are projected to increase by around 1¼% points of GDP less than in the common projections between 2004 and 2050, notably due to a lower number of beneficiaries. On the other hand, health-care and long-term care spending are more dynamic in the national projections, by around 1¼% points of GDP. This is chiefly due to an assumption of a higher income elasticity of healthcare and a more pessimistic assumption regarding the health status of elderly citizens; the Belgian national scenario is close to a scenario variation in the Ageing report where all the gains in life expectancy are assumed to be spent in bad health. The national projection further projects unemployment benefits to decrease by more due to a larger reduction in the unemployment rate and a declining replacement rate. Finally, the Belgian authorities now project a decrease in child-care benefits (of around ½ points of GDP). Overall, the Committee projects the increase in age-related expenditure ½ percentage points of GDP lower than the Ageing Report. Therefore, the national projections (excluding the *Generation Pact*) would reduce the sustainability gaps only little. Report available at:

http://www.docufin.fgov.be/intersalgfr/hrfcsf/adviezen/PDF/veillissement_2006_05.pdf

⁴³ See Table 56 in Annex 4 of the Report, available at:

http://www.docufin.fgov.be/intersalgfr/hrfcsf/adviezen/PDF/viellissement_2007_06.pdf

⁴⁴ However, the Committee argues that the tax-to-GDP ratio would rise indirectly through the reform, thus providing a “very light positive impact” on the general government budget over time (p. 130).

pension system. Although this would represent, if fully implemented, a step in the right direction, national projections show that this reform would not reduce the sustainability gaps.

The budgetary position in 2007 as estimated in the programme, though slightly worse than the starting position of the previous programme, contributes to offsetting the projected long-term budgetary impact of population ageing. However, this is not sufficient to fully cover future spending pressures. Maintaining high primary surpluses over the medium term, bringing the debt ratio below the Treaty reference value and implementing further measures aimed at addressing the substantial increase in age-related expenditure would contribute to reducing risks to the sustainability of public finances.

6. STRUCTURAL REFORM, THE QUALITY OF PUBLIC FINANCES AND INSTITUTIONAL FEATURES

The stability programme recalls the recent government initiatives to support economic growth, mainly taken in accordance with the national reform programme (see also Section 7).

The government, which took office on 23 March 2008, plans further structural reforms to promote employment. These include the continuation of the policy to activate the unemployed and to reduce labour taxation, in particular for the lower and average incomes. The plans also aim at supporting entrepreneurship and strengthening the social security system. As acknowledged in the programme update, the measures backing the reform intentions included in the government agreement remain to be decided. As a result, the budgetary impact is not yet known and the budgetary targets in the programme update do not take them into account.

In 2007, the contribution of one-off measures to the budget balance was slightly negative, unlike in most previous years, when the government frequently used such operations to achieve a balanced budget. While the budget for 2007 announced one-offs amounting to 0.5% of GDP, the government, which stayed on in a caretaker capacity for most of the year (awaiting the installation of a new government following the elections on 10 June) was not in a position to go ahead with the bulk of these operations (0.4% of GDP). In addition, unexpected deficit-increasing one-offs for 0.2% of GDP occurred. For the coming years, the programme update announced that the new government will achieve the targeted surpluses without the support of one-off measures, which is a positive development if fully implemented. However, it is not uncommon for the Belgian authorities to step up recourse to one-offs during the year and this often seems to be inspired by the need to achieve the short-term headline budgetary targets.

In view of Belgium's decentralised government structure, which includes substantial autonomy of communities and the regions over their budgets, coordination of fiscal policy between the different levels is crucial. A key element of the coordination mechanism is the annual advice to the government of the "Public Sector Borrowing Requirements" section of the HFC on the budgetary policy to be adopted. This advice includes recommendations on the budget balances of the various levels of government (see also Section 2) and form the basis of a series of budgetary conventions, which take the form of political agreements between governments at federal and regional level, setting the medium-term budgetary targets for the different levels of government and acting as internal stability programmes. So far, as confirmed in the programme update, no such agreement has been concluded for the years covered in the programme, although these are an important tool to ensure budgetary discipline and have contributed to

Belgium's budgetary performance in the past. The conclusion of such an agreement seems to depend on the conclusion of an agreement between the different levels of government on the further reorganisation of the State. As stated in the programme, this would according to the authorities, improve the functioning of the federation, make competencies more coherent and homogenous and adapting the financing of the different levels of government.

7. CONSISTENCY WITH THE NATIONAL REFORM PROGRAMME AND WITH THE BROAD ECONOMIC POLICY GUIDELINES

The stability programme recalls the government initiatives taken in accordance with the national reform programme to support economic growth through the stimulation of labour demand and supply, the improvement of competitiveness, the optimisation of the corporate tax system and the strengthening of social protection, while containing expenditure and improving fiscal governance. In both reports, the sustainability of public finances in the light of population ageing is considered as a key challenge for the Belgian economy, which is at medium risk with regard to the sustainability of public finances (as indicated in Section 5.2). The measures in the stability programme appear to be broadly in line with the National Reform Programme and the progress recorded in the implementation report submitted in October 2007 in the context of the renewed Lisbon strategy for growth and jobs.

The stability programme does not contain a qualitative assessment of the overall impact of the National Reform Programme (NRP) within the medium term fiscal strategy, nor detailed or systematic information on the direct budgetary costs (or savings) associated with the main reforms envisaged in the NRP. On the other hand, the budgetary projections of the programme seemingly take into account the public finance implications of the actions already implemented, including those foreseen in the 2008 budget, on the basis of the national reform programme. The budgetary impact of further measures required to achieve the targets set in the national reform programme, for instance to lower the tax wedge on labour by 2.2% of GDP between 2005 and 2010, is not included in the programme update. As a result, the two programmes only seem to be consistent to some extent.

Box 6: The Commission assessment of the implementation report of the National Reform Programme

On 11 December 2007, the Commission adopted its Strategic Report on the renewed Lisbon strategy for growth and jobs, which includes an assessment of the October 2007 implementation report of Belgium's national reform programme⁴⁵ and is summarised as follows.

Belgium's national reform programme identifies as key priorities in order to create growth and jobs: the sustainability of public finances; the reduction of labour costs; the creation of a more dynamic labour market; the stimulation of the economy through investment and reforms; strengthening the social security system; and strengthening synergies between environmental protection and growth.

Overall, the Belgian implementation report shows good progress on implementing the 2005 National Reform Programme (NRP) over the 2005-2007 period. The pace of progress appears to have decreased in 2007 in view of the longer-than-expected time needed to form a new government following the federal elections of 10 June 2007.

⁴⁵ Communication from the Commission to the European Council, "Strategic report on the renewed Lisbon strategy for growth and jobs: launching the new cycle (2008-2010)", 11.12.2007, COM(2007)803.

Against the background of the strengths and weaknesses identified, the Commission recommends that Belgium is recommended to take action in order to reduce the tax-burden on labour while continuing fiscal improvement, and to take further measures aimed at reducing regional disparities in unemployment. Against the background of progress made, the Commission recommends that Belgium is encouraged to also focus on the areas of: long term sustainability of public finances; the competition in gas and electricity markets; R&D and innovation performance; and the employment rate for older workers and vulnerable groups.

The tables below provide an overview of whether the strategy and policy measures in the stability programme are consistent with the broad economic policy guidelines in the area of public finances issued in the context of the Lisbon strategy for growth and jobs. The first table makes the assessment against the integrated guidelines for the period 2005-2008, adopted by the Council in July 2005. The second table makes the assessment against the country-specific recommendations / points to watch and the recommendations for the euro area, adopted by the Council in March 2007. The budgetary strategy in the stability programme is broadly consistent with the country-specific recommendations / points to watch and the recommendations for the euro area.

Table 14: Consistency with the broad economic policy guidelines (integrated guidelines)

Broad economic policy guidelines (integrated guidelines)	Yes	Steps in right direction	No	Not applicable
1. To secure economic stability				
– Member States should respect their medium-term budgetary objectives. As long as this objective has not yet been achieved, they should take all the necessary corrective measures to achieve it ¹ .		X		
– Member States should avoid pro-cyclical fiscal policies ² .				X
– Member States in excessive deficit should take effective action in order to ensure a prompt correction of excessive deficits ³ .				X
– Member States posting current account deficits that risk being unsustainable should work towards (...), where appropriate, contributing to their correction via fiscal policies.				X
2. To safeguard economic and fiscal sustainability				
In view of the projected costs of ageing populations,				
– Member States should undertake a satisfactory pace of government debt reduction to strengthen public finances.	X			
– Member States should reform and re-enforce pension, social insurance and health care systems to ensure that they are financially viable, socially adequate and accessible (...)		X		
3. To promote a growth- and employment-orientated and efficient allocation of resources				
Member States should, without prejudice to guidelines on economic stability and sustainability, re-direct the composition of public expenditure towards growth-enhancing categories in line with the Lisbon strategy, adapt tax structures to strengthen growth potential, ensure that mechanisms are in place to assess the relationship between public spending and the achievement of policy objectives and ensure the overall coherence of reform packages.		X		
Notes:				
¹ As further specified in the Stability and Growth Pact and the code of conduct, i.e. with an annual 0.5% of GDP minimum adjustment in structural terms for euro area and ERM II Member States.				
² As further specified in the Stability and Growth Pact and the code of conduct, i.e. Member States that have already achieved the medium-term objective should avoid pro-cyclical fiscal policies in “good times”.				
³ As further specified in the country-specific Council recommendations and decisions under the excessive deficit procedure.				

Broad economic policy guidelines (integrated guidelines)	Yes	Steps in right direction	No	Not applicable
<i>Source:</i> <i>Commission services</i>				

Table 15: Consistency with the broad economic policy guidelines (country-specific recommendations and points to watch)

Broad economic policy guidelines (country-specific recommendations and points to watch)	Yes	Steps in right direction	No	Not applicable
1. Country-specific recommendations				
– continue fiscal improvement		X		
2. Points to watch				
– ensure the long-term sustainability of public finances		X		
3. Recommendations for euro area Member States				
– Make use of the favourable cyclical conditions to aim at or pursue ambitious budgetary consolidation towards their medium-term objectives in line with the Stability and Growth Pact, hence striving to achieve an annual structural adjustment of at least 0.5% of GDP as a benchmark		X		
– Improve the quality of public finances by reviewing public expenditure and taxation, with the intention to enhance productivity and innovation, thereby contributing to economic growth and fiscal sustainability		X		
<i>Source:</i> <i>Commission services</i>				

* * *

Annex 1: Compliance with the code of conduct

This annex provides an assessment of whether the programme respects the requirements of Section II of the code of conduct (guidelines on the format and content), notably as far as (i) the model structure (Annex 1 of the code of conduct); (ii) the formal data provisions (Annex 2 of the code of conduct); and (iii) other information requirements is concerned.

(i) Model structure

The table of contents of the programme update adheres to the code of conduct. All topics, with the exception of the sectoral balances, are covered in the programme.

(ii) Data requirements

The programme update provides all compulsory data specified in the standard tables in Annex 2 of the code of conduct with the exception of the data on the sectoral balances. Some of the optional data have not been provided. Table 2 (general government budgetary prospects) is incomplete. First, only the sum of compensation of employees and intermediate consumption is reported, while the breakdown between the two is missing. Second, only the aggregate social payments are reported, while the breakdown in social transfer in kind and transfers in other than in kind is missing. Third, government consumption is missing. Table 3 (General government expenditure by function) is missing. Table 4 (general government debt developments) is incomplete: the missing variables are the breakdown of the stock-flow adjustment, the liquid financial assets and net financial debt. Table 7 (long-term sustainability) is largely incomplete: the programme only provides information about pension and health care expenditure.

The tables on the following pages show the data presented in the April 2008 update of the stability programme, following the structure of the tables in Annex 2 of the code of conduct. Compulsory data are in bold, missing data are indicated with grey-shading.

(iii) Other information requirements

The table below provides a summary assessment of the adherence to the other information requirements in the code of conduct.

The SCP...	Yes	No	Comments
<i>a. Involvement of parliament</i>			
... mentions status vis-à-vis national parliament.		X	
... indicates whether Council opinion on previous programme has been presented to national parliament.		X	
<i>b. Economic outlook</i>			
... (for euro area and ERM II Member States) uses “common external assumptions” on main extra-EU variables.		X	
... explains significant divergences with Commission services’ forecasts ¹ .		X	The scenario was outdated
... bears out possible upside/downside risks to economic outlook.	X		
... analyses outlook for sectoral balances and, especially for countries with high external deficit, external balance.		X	
<i>c. Monetary/exchange rate policy</i>			
... (CP only) presents medium-term monetary policy objectives and their relationship to price and exchange rate stability.			Not applicable
<i>d. Budgetary strategy</i>			
... presents budgetary targets for general government balance in relation to MTO and projected path for debt ratio.	X		
... (in case new government has taken office) shows continuity with respect to budgetary targets endorsed by Council.	X		
... (when applicable) explains reasons for deviations from previous targets and, in case of substantial deviations, whether measures are taken to rectify situation (+ provides information on them).	X		
... backs budgetary targets by indication of broad measures		X	Not after 2008

The SCP...	Yes	No	Comments
necessary to achieve them and analyses their quantitative effects on balance.			
... specifies state of implementation of measures.		X	
<i>e. "Major structural reforms"</i>			
... (if MTO not yet reached or temporary deviation is planned from MTO) includes comprehensive information on economic and budgetary effects of possible 'major structural reforms' over time.			Not applicable
... includes quantitative cost-benefit analysis of short-term costs and long-term benefits of reforms.			Not applicable
<i>f. Sensitivity analysis</i>			
... includes comprehensive sensitivity analyses and/or develops alternative scenarios showing impact on balance and debt of: a) changes in main economic assumptions b) different interest rate assumptions c) (for CP only) different exchange rate assumptions d) if common external assumptions are not used, changes in assumptions for main extra-EU variables.	X X	X	Not applicable
... (in case of "major structural reforms") analyses how changes in assumptions would affect budget and potential growth.			Not applicable
<i>g. Broad economic policy guidelines</i>			
... provides information on consistency with broad economic policy guidelines of budgetary objectives and measures to achieve them.		X	
<i>h. Quality of public finances</i>			
... describes measures to improve quality of public finances, both revenue and expenditure sides.		X	No concrete new measures announced
<i>i. Long-term sustainability</i>			
... outlines strategies to ensure sustainability.	X		
... includes common budgetary projections by the AWG and all necessary additional information (esp. new relevant information).		X	
<i>j. Other information (optional)</i>			
... includes information on implementation of existing national budgetary rules and on other institutional features of public finances.	X		
<p>Notes: SCP = stability/convergence programme; CP = convergence programme ¹To the extent possible, bearing in mind the typically short time period between the publication of the Commission services' autumn forecast and the submission of the programme.</p> <p>Source: Commission services</p>			

Table 1a. Macroeconomic prospects

	ESA Code	2006	2006	2007	2008	2009	2010	2011
		Level	rate of change	rate of change	rate of change	rate of change	rate of change	rate of change
1. Real GDP	B1*g	310.9	2.8	2.7	1.9	2.0	2.0	2.0
2. Nominal GDP	B1*g	316.6	4.9	4.4	4.6	4.1	4.0	4.0
Components of real GDP								
3. Private consumption expenditure	P.3	162.2	2.0	2.5	1.8	1.5	1.6	1.6
4. Government consumption expenditure	P.3	68.7	0.0	2.6	2.6	1.8	1.9	1.8
5. Gross fixed capital formation	P.51	63.9	4.2	5.1	2.4	2.7	2.5	2.7
6. Changes in inventories and net acquisition of valuables (% of GDP)	P.52 + P.53	n.a.	0.9	-0.2	0.0	0.0	0.0	0.0
7. Exports of goods and services	P.6	268.4	2.6	4.6	4.5	5.6	5.6	5.6
8. Imports of goods and services	P.7	257.2	2.7	4.9	4.8	5.6	5.6	5.6
Contributions to real GDP growth								
9. Final domestic demand		-	2.9	2.8	2.0	1.8	1.8	1.8
10. Changes in inventories and net acquisition of valuables	P.52 + P.53	-	0.9	-0.2	0.0	0.0	0.0	0.0
11. External balance of goods and services	B.11	-	0.0	-0.1	-0.1	0.2	0.2	0.2

Table 1b. Price developments

	ESA Code	2006	2006	2007	2008	2009	2010	2011
		Level	rate of change	rate of change	rate of change	rate of change	rate of change	rate of change
1. GDP deflator		102	2.0	1.6	2.6	2.1	1.9	1.9
2. Private consumption deflator		102.5	2.5	2.0	2.9	1.7	1.8	1.8
3. HICP¹		102.3	2.3	1.8	3.0	1.7	1.8	1.8
4. Public consumption deflator		103	3.0	2.5	3.1	2.6	2.3	2.3
5. Investment deflator		102.7	2.7	1.9	2.5	2.0	2.0	2.0
6. Export price deflator (goods and services)		103.4	3.4	2.7	1.9	0.9	1.2	1.4
7. Import price deflator (goods and services)		104	4.0	2.3	2.0	0.8	1.2	1.4

¹ Optional for stability programmes.

Table 1c. Labour market developments

	ESA Code	2006	2006	2007	2008	2009	2010	2011
		Level	rate of change	rate of change	rate of change	rate of change	rate of change	rate of change
1. Employment, persons¹		4278	1.2	1.6	1.1	0.9	0.9	0.8
2. Employment, hours worked ²		6328.6	1.4	1.6	1.0	0.8	0.8	0.7
3. Unemployment rate (%)³		8.2	8.2	7.6	7.3	7.1	7.0	6.7
4. Labour productivity, persons⁴		72.6	1.6	1.1	0.8	1.1	1.2	1.3
5. Labour productivity, hours worked ⁵		49.1	1.4	1.1	0.8	1.2	1.3	1.4
6. Compensation of employees	D.1	158.2	4.5	4.7	4.2	4.3	4.4	4.4
7. Compensation per employee		44.1	3.2	3.1	3.2	3.3	3.4	3.4

¹ Occupied population, domestic concept national accounts definition.

² National accounts definition.

³ Harmonised definition, Eurostat; levels.

⁴ Real GDP per person employed.

⁵ Real GDP per hour worked.

Table 1d. Sectoral balances

% of GDP	ESA Code	2006	2007	2008	2009	2010	2011
1. Net lending/borrowing vis-à-vis the rest of the world	B.9	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
<i>of which :</i>							
- Balance on goods and services		n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
- Balance of primary incomes and transfers		n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
- Capital account		n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
2. Net lending/borrowing of the private sector	B.9	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
3. Net lending/borrowing of general government	EDP B.9	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
4. Statistical discrepancy		n.a.	optional	optional	optional	optional	optional

Table 2. General government budgetary prospects

	ESA Code	2006	2006	2007	2008	2009	2010	2011
		Level	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP
Net lending (EDP B.9) by sub-sector								
1. General government	S.13	1096	0.3	-0.2	0.0	0.3	0.7	1.0
2. Central government	S.1311	220	0.1	-1.0	-0.6	-0.3	0.0	0.3
3. State government	S.1312	621	0.2	0.3	0.1	0.0	0.0	0.0
4. Local government	S.1313	-717	-0.2	0.0	0.1	0.2	0.2	0.1
5. Social security funds	S.1314	971	0.3	0.6	0.4	0.4	0.5	0.6
General government (S13)								
6. Total revenue	TR	154480	48.8	48.7	49.0	48.8	48.9	49.2
7. Total expenditure	TE ¹	153384	48.5	48.9	49.0	48.5	48.3	48.2
8. Net lending/borrowing	EDP B.9	1095	0.3	-0.2	0.0	0.3	0.7	1.0
9. Interest expenditure	EDP D.41	12594	4.0	3.8	3.7	3.5	3.4	3.3
10. Primary balance²		13690	4.3	3.7	3.7	3.8	4.1	4.3
11. One-off and other temporary measures³		2260	0.7	-0.1	0.0	0.0	0.0	0.0
Selected components of revenue								
12. Total taxes (12=12a+12b+12c)		96232	30.4	30.1	30.4	30.1	30.2	30.3
12a. Taxes on production and imports	D.2	41708	13.2	12.9	13.1	13.0	optional	optional
12b. Current taxes on income, wealth, etc	D.5	52363	16.5	16.4	16.5	16.5	optional	optional
12c. Capital taxes	D.91	2161	0.7	0.7	0.7	0.7	optional	optional
13. Social contributions	D.61	49743	15.7	15.9	15.9	16.0	optional	optional
14. Property income	D.4	1817	0.6	0.6	0.6	0.6	optional	optional
15. Other⁴		6688	2.1	2.1	2.1	2.1	optional	optional
16=6. Total revenue	TR	154480	48.8	48.7	49.0	48.8	48.9	49.2
p.m.: Tax burden (D.2+D.5+D.61+D.91-D.995)⁵			46.8	46.6	47.0	46.8	47.0	47.2
Selected components of expenditure								
17. Compensation of employees + intermediate consumption	D.1+P.2	48927	15.5	15.5	15.4	15.2	15.0	14.9
17a. Compensation of employees	D.1	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
17b. Intermediate consumption	P.2	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
18. Social payments (18=18a+18b)		70938	22.4	22.6	23.0	23.0	23.0	23.1
18a. Social transfers in kind supplied via market producers	D.6311, D.63121, D.63131	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
18b. Social transfers other than in kind	D.62	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
19=9. Interest expenditure	EDP D.41	12594	4.0	3.8	3.7	3.5	3.4	3.3
20. Subsidies	D.3	5540	1.7	2.0	2.0	1.9	1.9	1.9
21. Gross fixed capital formation	P.51	5324	1.7	1.7	1.7	1.6	1.6	1.8
22. Other⁶		10259	3.2	3.3	3.4	3.3	3.4	3.3
23=7. Total expenditure	TE ¹	153582	48.5	48.9	49.0	48.5	48.3	48.2
p.m.: Government consumption (nominal)	P.3	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.

¹Adjusted for the net flow of swap-related flows, so that TR-TE=EDP B.9.

²The primary balance is calculated as (EDP B.9, item 8) plus (EDP D.41, item 9).

³A plus sign means deficit-reducing one-off measures.

⁴P.11+P.12+P.131+D.39+D.7+D.9 (other than D.91).

⁵Including those collected by the EU and including an adjustment for uncollected taxes and social contributions (D.995), if appropriate.

⁶D.29+D4 (other than D.41)+ D.5+D.7+D.9+P.52+P.53+K.2+D.8.

Table 3. General government expenditure by function

% of GDP	COFOG Code	2005	2010
1. General public services	1	n.a.	n.a.
2. Defence	2	n.a.	n.a.
3. Public order and safety	3	n.a.	n.a.
4. Economic affairs	4	n.a.	n.a.
5. Environmental protection	5	n.a.	n.a.
6. Housing and community amenities	6	n.a.	n.a.
7. Health	7	n.a.	n.a.
8. Recreation, culture and religion	8	n.a.	n.a.
9. Education	9	n.a.	n.a.
10. Social protection	10	n.a.	n.a.
11. Total expenditure (=item 7=23 in Table 2)	TE ¹	n.a.	n.a.

¹Adjusted for the net flow of swap-related flows, so that TR-TE=EDP B.9.

Table 4. General government debt developments

% of GDP	ESA Code	2006	2007	2008	2009	2010	2011
1. Gross debt¹		88.2	84.9	81.5	78.1	74.7	71.1
2. Change in gross debt ratio		-3.9	-3.3	-3.4	-3.3	-3.5	-3.6
Contributions to changes in gross debt							
3. Primary balance²		4.3	3.7	3.7	3.8	4.1	4.3
4. Interest expenditure³	EDP D.41	4.0	3.8	3.7	3.5	3.4	3.3
5. Stock-flow adjustment		0.7	0.2	0.3	0.2	0.2	0.2
<i>of which:</i>							
- Differences between cash and accruals ⁴		n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
- Net accumulation of financial assets ⁵		n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
<i>of which:</i>		-	-	-	-	-	-
- privatisation proceeds		n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
- Valuation effects and other ⁶		n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
p.m.: Implicit interest rate on debt⁷		4.5	4.5	4.5	4.5	4.5	4.6
Other relevant variables							
6. Liquid financial assets ⁸		n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
7. Net financial debt (7=1-6)		n.a.	n.a.	n.a.	n.a.	n.a.	n.a.

¹As defined in Regulation 3605/93 (not an ESA concept).

²Cf. item 10 in Table 2.

³Cf. item 9 in Table 2.

⁴The differences concerning interest expenditure, other expenditure and revenue could be distinguished when relevant.

⁵Liquid assets, assets on third countries, government controlled enterprises and the difference between quoted and non-quoted assets could be distinguished when relevant.

⁶Changes due to exchange rate movements, and operation in secondary market could be distinguished when relevant.

⁷Proxied by interest expenditure divided by the debt level of the previous year.

⁸AF1, AF2, AF3 (consolidated at market value), AF5 (if quoted in stock exchange; including mutual fund shares).

Table 5. Cyclical developments

% of GDP	ESA Code	2006	2007	2008	2009	2010	2011
1. Real GDP growth (%)		2.8	2.7	1.9	2.0	2.0	2.0
2. Net lending of general government	EDP B.9	0.3	-0.2	0.0	0.3	0.7	1.0
3. Interest expenditure	EDP D.41	4.0	3.8	3.7	3.5	3.4	3.3
4. One-off and other temporary measures¹		0.7	-0.1	0.0	0.0	0.0	0.0
5. Potential GDP growth (%)		2.3	2.3	2.1	2.0	2.0	1.9
contributions:							
- labour		0.6	0.6	0.4	0.3	0.3	0.3
- capital		0.7	0.6	0.6	0.7	0.7	0.7
- total factor productivity		1.0	1.0	1.0	1.0	1.0	1.0
6. Output gap		-0.7	-0.3	-0.3	-0.3	-0.2	-0.1
7. Cyclical budgetary component		-0.4	-0.2	-0.2	-0.2	-0.1	-0.1
8. Cyclically-adjusted balance (2 - 7)		0.7	0.0	0.2	0.5	0.8	1.0
9. Cyclically-adjusted primary balance (8 + 3)		4.7	3.8	3.8	4.0	4.2	4.3
10. Structural balance (8 - 4)		0.0	0.1	0.2	0.5	0.8	1.0

¹A plus sign means deficit-reducing one-off measures.

Table 6. Divergence from previous update

	ESA Code	2006	2007	2008	2009	2010	2011
Real GDP growth (%)							
Previous update		2.7	2.2	2.1	2.2	2.2	n.a.
Current update		2.8	2.7	1.9	2.0	2.0	2.0
Difference		0.1	0.5	-0.2	-0.2	-0.2	n.a.
General government net lending (% of GDP)	EDP B.9						
Previous update		0.0	0.3	0.5	0.7	0.9	n.a.
Current update		0.3	-0.2	0.0	0.3	0.7	1.0
Difference		0.3	-0.5	-0.5	-0.4	-0.2	n.a.
General government gross debt (% of GDP)							
Previous update		87.7	83.9	80.4	76.6	72.6	n.a.
Current update		88.2	84.9	81.5	78.1	74.7	71.1
Difference		0.5	1.0	1.1	1.5	2.1	n.a.

Table 7. Long-term sustainability of public finances

% of GDP	2000	2005	2010	2020	2030	2050
Total expenditure	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Of which: age-related expenditures	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Pension expenditure	n.a.	8.9	9.1	10.5	12.5	13.4
Social security pension	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Old-age and early pensions	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Other pensions (disability, survivors)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Occupational pensions (if in general government)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Health care	n.a.	7.0	7.7	8.4	9.2	10.5
Long-term care (<i>this was earlier included in the</i>	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Education expenditure	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Other age-related expenditures	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Interest expenditure	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Total revenue	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Of which: property income	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
<i>Of which</i> : from pensions contributions (or social contributions if appropriate)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Pension reserve fund assets	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
<i>Of which</i> : consolidated public pension fund assets (assets other than government liabilities)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Assumptions						
Labour productivity growth	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Real GDP growth	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Participation rate males (aged 20-64)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Participation rates females (aged 20-64)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Total participation rates (aged 20-64)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Unemployment rate	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Population aged 65+ over total population	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.

Table 8. Basic assumptions

	2006	2007	2008	2009	2010	2011
Short-term interest rate ¹ (annual average)	2.9	4.2	4.1	4.0	3.8	3.7
Long-term interest rate (annual average)	3.8	4.2	4.2	4.3	4.5	4.6
USD/€ exchange rate (annual average) (euro area and ERM II countries)	125.50	135.00	139.00	139.00	139.00	139.00
Nominal effective exchange rate	107.1	109.4	110.0	110.0	110.0	110.0
(for countries not in euro area or ERM II) exchange rate vis-à-vis the € (annual average)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
World excluding EU, GDP growth	5.8	5.6	5.3	5.5	5.3	5.2
EU GDP growth	3.0	2.8	2.4	2.4	2.3	2.3
Growth of relevant foreign markets	8.9	6.7	6.5	7.0	6.9	6.9
World import volumes, excluding EU	8.4	7.5	6.8	7.5	7.5	7.5
Oil prices (Brent, USD/barrel)	65.2	69.5	74.9	72.7	73.6	74.6

¹If necessary, purely technical assumptions.

Annex 2: Key indicators of past economic performance

Standard text: This annex displays key economic indicators that summarise the past economic performance of Belgium. To put the country's performance into perspective, right-hand side of the table displays the same set of indicators for the euro area.

Table: Key economic indicators

	Belgium						Euro area					
	Averages			2005	2006	2007	Averages			2005	2006	2007
	'96 - '05	'96 - '00	'01 - '05				'96 - '05	'96 - '00	'01 - '05			
Economic activity												
Real GDP (% change)	2.1	2.7	1.6	1.7	2.8	2.7	2.1	2.7	1.5	1.6	2.8	2.6
<i>Contributions to real GDP growth:</i>												
<i>Domestic demand</i>	1.8	2.4	1.3	2.0	2.9	2.9	2.0	2.7	1.3	1.8	2.6	2.2
<i>Net exports</i>	0.3	0.3	0.3	-0.3	0.0	-0.2	0.1	0.0	0.1	-0.2	0.2	0.4
Real GDP per capita (PPS; EU27 = 100)	121	122	120	120	119	119	113	114	112	110	110	109
Real GDP per capita (% change)	1.8	2.5	1.2	1.1	2.2	2.5	1.7	2.5	0.9	1.0	2.2	2.0
Prices, costs and labour market												
HICP inflation (%)	1.8	1.6	2.0	2.5	2.3	1.8	1.9	1.5	2.2	2.2	2.2	2.1
Labour productivity (% change)	1.2	1.5	0.9	0.4	1.6	1.0	1.3	1.7	1.0	1.1	1.5	0.9
Real unit labour costs (% change)	-0.4	-0.4	-0.4	-1.0	-0.4	0.3	-0.5	-0.6	-0.5	-0.8	-0.8	-0.7
Employment (% change)	0.9	1.1	0.6	1.2	1.2	1.7	1.2	1.5	0.9	0.9	1.6	1.7
Unemployment rate (% of labour force)	8.3	8.7	7.8	8.4	8.2	7.5	9.1	9.7	8.5	8.9	8.2	7.4
Competitiveness and external position												
Real effective exchange rate (% change)	-0.7	-2.8	1.3	-0.1	0.5	1.3	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Export performance (% change) ¹	-1.9	-2.8	-0.9	-2.3	-5.4	0.1	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	4.5	5.0	4.0	2.9	3.4	3.2	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Public finances												
General government balance (% of GDP)	-0.9	-1.4	-0.3	-2.3	0.3	-0.2	-2.3	-2.1	-2.6	-2.5	-1.3	-0.6
General government gross debt (% of GDP)	108.3	117.5	99.0	92.1	88.2	84.9	70.6	72.2	69.0	70.2	68.5	66.4
Structural balance (% of GDP) ²	n.a.	n.a.	-0.7	-0.2	-0.6	-0.3	n.a.	n.a.	-2.7	-2.2	-1.2	-0.7
Financial indicators												
Short-term real interest rate (%) ³	1.5	2.3	0.8	-0.3	1.1	2.5	1.3	2.5	0.6	0.3	1.2	2.1
Long-term real interest rate (%) ³	3.2	4.2	2.3	0.9	1.8	2.6	n.a.	n.a.	2.0	1.5	1.9	2.1
<p>Notes:</p> <p>¹Market performance of exports of goods and services on export-weighted imports of goods and services of 35 industrial markets.</p> <p>²Cyclically-adjusted balance net of one-off and other temporary measures; available since 2003.</p> <p>³Using GDP deflator.</p> <p><i>Source:</i> Commission services</p>												

