
BELGIAN STABILITY

PROGRAMME

(2009-2012)

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Introduction

The financial crisis that hit the global economy produced an unprecedented shockwave.

As in many Member States, public finances in Belgium were severely affected by the economic and financial crisis. Whereas Belgian public finances had still shown a slight surplus on average over the period 2006-2007, a major deficit has opened up since then, reaching -1.2% of gross domestic product (GDP) in 2008 and -5.9% in 2009.

Given the dynamics of interest charges and the growth in expenditure linked to ageing, an economic recovery – even a vigorous one – would not allow the deficit to be brought back below the 3% threshold authorised by the Maastricht Treaty. In the medium term, the deficit would reach 5.4% of GDP and the public debt should continue its upward trend, reaching 107% of GDP in 2014.

With the effects of the ageing of the population looming, the current development of Belgian public finances is therefore untenable and undesirable, particularly in the context of maintaining solidarity between the generations.

Healthy public finances are essential with the aim of meeting the costs of ageing and therefore ensuring the permanence of the Belgian economic and social model.

The Belgian authorities have defined a consolidation programme. This envisages an adjustment of the path defined previously in the supplement to the stability programme in September 2009, by taking account of the improvement in the business cycle and the budgets for 2010 as well as the multi-year budgets put together by the various levels of government.

Moreover, the distribution of these budgetary targets by level of government forms the subject of a formal agreement with a horizon of 2009-2010. With regard to the period 2011-2012, the agreement is still being finalised. This revision complies with the recommendations of the Ecofin Council dated 2 December 2009.

The consolidation programme defined by the Belgian authorities is aimed at reinforcing the credibility of Belgian public finances and thus favouring a fall in long-term interest rates. In turn, this reduction should facilitate the consolidation of the budget and favour a downward normalisation of the savings rate, thereby stimulating the (potential) growth of the economy.

Furthermore, this reinforcement of credibility is essential in view of Belgium's high level of debt and the sensitivity of public finances to sudden movements in interest rates.

The budgetary consolidation programme must go hand in hand with lasting economic growth that is both more balanced and at a higher level. The ageing of the population, climate change, higher raw materials prices and the increasing globalisation of the world economy represent challenges that cannot be ignored and which will have to be tackled positively by integrating them into decisions on economic, budgetary, environmental and social policy. These challenges notably demand a modernisation of the labour market and social security, better interaction between the economy and the environment and a more equitable, greener tax system.

Lasting potential growth and a higher rate of employment, particularly among young people and the elderly, are essential requirements with the aim of ensuring better social cohesion and preserving the Belgian economic and social model.

1 Economic situation and macroeconomic scenarios

1.1. Economic context

In the aftermath of the impact of a particularly severe recession on the world's economy, signs of an upturn became more and more apparent during 2009. Initial fears of a collapse in the financial system steadily abated, notably following the intervention of monetary authorities and governments. The stimulus plans implemented by public authorities supported the weak level of economic activity. Six months ago, it was still being assumed that growth would only start to re-establish itself at the beginning of 2010. However, the results from the third quarter of 2009 show that this upturn is already making its effects felt in several major economic areas, notably the euro area.

Having been constantly revised downwards since 2007, economic forecasts were therefore revised upwards in the course of the second half of 2009. However, the climate of uncertainty persists, particularly with regard to the lasting nature of the economic recovery. In the first place, the financial sector continues to be seen as fragile ; reorganisation and stabilisation need to be pursued with the aim of being able to bring support to the real economy. Secondly, it remains to be seen how economic activity will react to the reduction in incentives, both monetary and budgetary. This reduction is indispensable in order to prevent new financial and monetary imbalances being created and in order not to compromise the conditions for lasting development in the long term. However, it is extremely difficult to define the right timing for a crisis exit strategy. Thirdly, the development of unemployment could hamper the re-establishment of consumer confidence, an aspect which would therefore weigh on both consumption and investment, the pillars of lasting economic growth.

This uncertainty is reflected in the disparity between the economic forecasts for 2010 and 2011, even though they all point to a recovery in economic activity.

This, therefore, is the economic context - more favourable but still fragile and uncertain - that this stability programme fits into.

1.2. Economic forecasts of the Federal Planning Bureau

International environment

The economic outlooks of the Federal Planning Bureau in December 2009 form the basis for the path described in this stability programme. They included two macroeconomic scenarios. The first of these is based on very cautious growth assumptions which were perfectly in line with the external assumptions of the European Commission (October 2009). The second scenario takes account of more recent developments, including the results of the third quarter, growing confidence amongst investors and the recovery in international trade, given impetus notably by certain emerging countries such as China. In order to adhere most closely to the expected situation, it was decided to use this second scenario which is the most likely and envisages GDP growth of 1.1% and 1.7% in 2010 and 2011 respectively. A comparison of these growth prospects with the growth assumptions of the most important neighbouring countries demonstrates that they are in line with the latter.

In order to set up this simulation, the Federal Planning Bureau went back to the most recent *Economic Outlook* from the OECD (November 2009, covering the period 2009-2011). Two differences can be seen with respect to the European Commission's base assumptions. On the one hand, more marked growth is envisaged for all the countries in the OECD, with growth in the euro area therefore, in 2010 and 2011, at 0.9% and 1.7% respectively (compared to the 0.7% and 1.5% envisaged in the external assumptions of the European Commission). On the other hand, slightly stronger growth is also expected from the relevant foreign (non-EU) markets. The assumptions on interest rates, exchange rates and the price of oil in turn remain unchanged compared to the November projections from the European Commission.

In drawing up its outlooks for 2012, the FPB used the OECD's medium-term projections (June 2009).

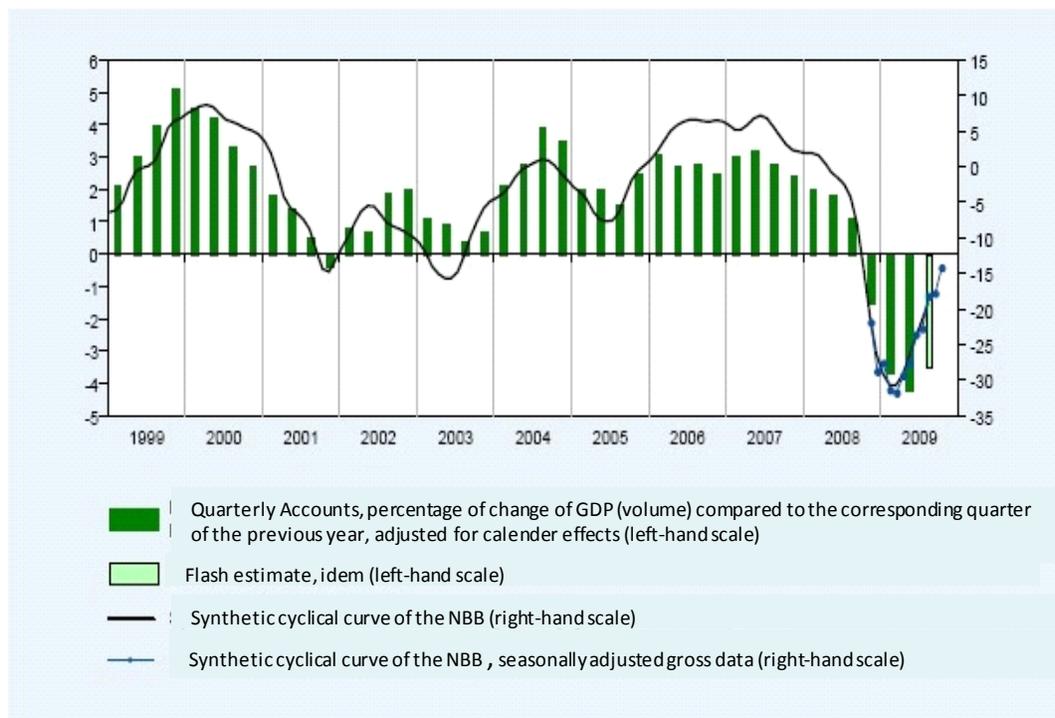
Table 1: External environment

	2008	2009	2010	2011	2012
Short-term interest rate (annual average)	4,6	1,3	1,5	2,5	2,5
Long-term interest rate (annual average)	4,2	3,7	3,7	4,1	4,5
USD/euro exchange rate (annual average)	146,6	139,2	148,2	148,2	148,2
Nominal effective exchange rate (2000=100)	111,9	113,1	113,9	113,9	113,9
GDP-growth - world (excluding EU)	3,8	-0,4	3,8	4,1	5,0
GDP-growth - EU	0,8	-4,1	0,9	1,7	2,3
Growth of relevant external markets	2,3	-11,0	3,6	4,8	6,4
Global imports by volume (excluding EU)	4,6	-12,6	4,6	5,0	7,0
Oil price (USD)	96,9	61,3	76,5	80,5	84,5

Development of the business cycle

After four successive quarters of negative growth, the National Accounts Institute estimates growth of 0.5% for the third quarter compared to the previous quarter. The development of quarterly GDP compared to the corresponding quarter of the previous year also shows a reversal of the trend (see Chart 1). With effect from Spring 2009, confidence amongst both manufacturers and consumers grew almost continuously, although the latter recorded a new decline in December down to the level seen in the months June - August, chiefly due to the fear of an increase in unemployment in 2010. Similarly, in January, confidence amongst consumers is stabilising at this relatively low level. Nonetheless, the upturn in business indicators in the course of 2009 provides grounds for presuming that after a relatively favourable second half of 2009, the economy will pursue its growth path. With regard to 2009, the various estimates currently converge on a contraction of 3.1% in the economy.

Chart 1: Real quarterly growth of GDP in % compared to the corresponding six months of the previous year and development of the business cycle



Source : NAI

Forecasts for 2010 - 2012

Following the strong contraction in the economy in 2009 (-3.1%), the recovery observed in the second half of 2009 is forecast to continue in 2010. The current starting point is a growth rate of 1.1%. These projections still appear to be cautious. A comparison of these growth prospects with the growth scenarios of the most important neighbouring countries demonstrates that they are close to the growth figures on which they are based and that they are even below the latter in most cases. The last projections from the IMF on 26 January 2010 also indicate an upward revision of growth for the euro area to 1% in 2010 and 1.6% in 2011. The macroeconomic trends for France and Germany, which are major trading partners of Belgium, are also more favourable, at 1.4% in 2010 and 1.7% in 2011 for France and 1.5% in 2010 and 1.9% in 2011 for Germany. The last Consensus projections in the Prime News for January – which represent the average of large Belgian financial institutions – forecast growth of 1.5% for 2010 in Belgium.

These figures are therefore highly similar to the scenarios adopted in the framework of this stability programme.

Based on the scenarios used with regard to the international environment (see above), growth is forecast to move beyond its potential level with effect from 2011 to settle at 1.7% in 2011 and 2.2% in 2012 (potential growth of 1.4% and 1.5 % respectively). These medium-term projections are of course tinged with greater uncertainty than those for the shorter term, and indeed more so than previously. In fact, it is difficult to determine the extent to which the economic and financial crisis will weigh on the potential growth of the economy.

Table 2: Detailed macroeconomic forecasts for the medium term

<i>percentage change unless otherwise stated</i>	2008	2008	2009	2010	2011	2012
	In miljard euro					
1. Real GDP	291,6	1,0	-3,1	1,1	1,7	2,2
2. Nominal GDP	344,6	2,9	-2,0	2,4	3,6	4,1
	Components of real GDP					
3. Private consumption expenditure	150,8	1,1	-1,3	0,8	1,4	1,6
4. Government consumption expenditure	62,9	3,3	2,2	1,1	1,3	2,1
5. Gross fixed capital formation	67,9	4,4	-3,7	0,2	2,1	2,8
6. Changes in inventories and net acquisition of valuables	-	1,2	0,1	0,5	0,5	0,5
7. Exports of goods and services	267,7	1,6	-12,0	2,3	3,6	4,7
8. Imports of goods and services	261,5	3,0	-10,9	2,3	3,3	4,4
	Contributions to real GDP growth					
9. Final domestic demand	-	2,3	-2,1	1,1	1,5	2,0
10. Changes in inventories and net acquisition of valuables	-	-0,1	-1,1	0,4	0,0	0,0
11. External balance of goods and services	-	-1,2	-1,0	0	0,2	0,2

In 2009, households were hesitant in terms of their spending (-1.3%), not least owing to the negative economic climate and the banking crisis. The real disposable income of households increased overall in 2009, in spite of the fall in employment. This can be explained chiefly by the fact that in 2009, salary indexation was still partly reflecting the high inflation of 2008. Furthermore, households were able to benefit from tax reductions, notably those living in Flanders ('jobkorting'), as well as fast-tracking of tax assessments for individuals. Moreover, in 2009, the rise in unemployment remained rather limited given the seriousness of the recession, notably thanks to the measures decided by the government to counteract the crisis (time credit and reduction in working time).

A slight upturn in private consumption (0.8%) is expected in 2010, in line with the emerging recovery in the economic environment. This is forecast to rise to 1.4% in 2011 and 1.6% in 2012, influenced by the employment trend and the increase in salaries and unearned income.

In contrast, investment displayed a marked fall in 2009 (-3.7%). The weakness in demand gave rise to over-capacity and credit terms were tightened up. It is not until mid-2010 that the investment climate is forecast to start slowly recovering, on the back of improved market prospects. A limited rise in investment is still expected for 2010 as a whole (+0.2%) due to the marked drop in the level of manufacturing capacity utilisation and the major decline in firms' profitability. A more marked increase in investment on an annual basis should again be seen as from 2011 (an increase of 2.1% in 2011 and 2.8% in 2012).

During the fourth quarter of 2008 and first quarter of 2009, exports displayed a marked fall following the downturn in foreign markets. In the second half of the year, export volumes recovered slightly. On an annual basis, exports are forecast to decrease by 12%. Imports also show a marked drop in 2009 (-10.9%), following the decrease in domestic demand and the contraction in exports. They should recover steadily in 2010 and 2011, influenced by the recovery in economic activity. However, the fall in imports was less pronounced than that for exports in 2009, an aspect which produced a more negative balance of trade. With effect from 2010, a stronger increase in exports is again expected, which will allow a partial recovery in the balance of trade.

As shown by Table 2, inventories were markedly reduced in 2009. With regard to 2010, inventories are expected to be rebuilt, which should have a positive impact on GDP.

Table 3: Development of prices in the medium term

<i>% change</i>	2008 (2000=100)	2008	2009	2010	2011	2012
1. GDP deflator	118,2	1,9	1,2	1,3	1,9	1,9
2. Private consumption deflator	122,3	4,2	0,0	1,5	1,7	1,8
3. HICP	120,0	4,5	0,0	1,5	1,7	1,8
4. Public consumption deflator	126,9	3,5	3,2	0,9	1,9	1,8
5. Investment deflator	114,4	2,5	-1,5	1,4	1,5	1,7
6. Export price deflator (goods and services)	117,7	4,3	-4,2	0,8	1,7	1,9
7. Import price deflator (goods and services)	120,7	6,6	-5,5	0,9	1,9	2,0

Overall inflation was zero in 2009. This exceptionally low rate is the result of the trend in oil prices, giving rise to a negative year-to-year inflation during a number of months in 2009 (the health index is not dependent on the price of petrol and diesel and will therefore be less influenced by this development). With regard to other goods and services, inflation remains positive, even though it is limited due to the slowdown in the business cycle and the consequences of falling energy prices for the prices of other goods and services. With effect from 2010, following the increase in the prices of petroleum products, a more normal inflation rate of 1.5% in 2010, 1.7% in 2011 and 1.8% in 2012 is again expected on an annual basis.

According to the forecasts, the GDP deflator amounts to 1.2% in 2009 and 1.3% in 2010, after which a normal level will be resumed again (1.9%). Price levels, not only for investments but also for imports and exports, displayed a major fall in 2009. As shown by Table 3, a steady normalisation is forecast with effect from 2010.

Table 4: Development of the labour market

<i>% change, unless otherwise stated</i>	2008	2008	2009	2010	2011	2012
	Niveau					
1. Domestic employment	4.446,9 (a)	1,9	-0,7	-1,0	0,5	0,9
2. Numbers of hours worked	6.538 (b)	1,2	-2,4	-0,1	1,1	0,8
3. Unemployment rate (% , Eurostat definition)	7,0	7,0	8,2	9,4	9,6	9,5
4. labour productivity, persons	65.600 (c)	-0,8	-2,4	2,1	1,1	1,3
5. Labour productivity, hours worked	44,6 (c)	-0,2	-0,7	1,2	0,6	1,4
6. Compensation of employees	177 (d)	5,4	0,5	1,1	3,1	3,7
7. Compensation per employee	47.400 (c)	3,3	1,2	2,2	2,6	2,8

(a) thousands; (b) millions of hours; (c) EUR; (d) billions of EUR

In 2009, employment decreased by 0.7%. This decline is markedly less pronounced than that for economic activity, since schemes for temporary unemployment and reduced working time allowed part of the decrease in demand to be offset. Furthermore, a time-lag effect can still be observed between economic growth and the labour market. This is the reason why domestic employment only started to deteriorate in the first quarter of 2009. However, by virtue of this mechanism, employment will still continue to decline by 1% in 2010. It is only from 2011 onwards that a slight recovery in employment is forecast, specifically +0.5% in 2011 and +0.9% in 2012, although this will not allow a return to the 2008 level.

The Eurostat harmonised unemployment rate should rise from 7% in 2008 to 9.6% in 2011, then decrease slightly and settle at 9.5% in 2012.

The macroeconomic scenarios used during the preparation of this stability programme are a little more favourable than those used by both the Federal Government and the Communities and Regions during the drafting of their budgets for 2010 and their multi-year budgets or budgetary paths for the year 2011.

2 Budgetary path for 2009-2012

This chapter sets out the budgetary trend for the period 2009-2012. This budgetary trend represents a revision of the path initially proposed by the Belgian authorities in September 2009 in order to take account of the improvement in economic prospects, the budgets filed in the respective Parliaments and also the co-operation agreements between the federal level and the federate entities.

This revision of the path complies with the recommendations of the Ecofin Council on 2 December 2009, by forecasting a return to a deficit of 3% of GDP in 2012.

2.1 Budget for 2009

According to the provisional figures, the balance for the public administrations should post a deficit of 5.9% of GDP in 2009, the highest deficit since 1993 at the time of the crisis of the European Monetary System. For the first time since the inception of the European economic and monetary Union, therefore, Belgium has exceeded the threshold of 3% of GDP authorised by the Stability and Growth Pact.

However, as the Ecofin Council pointed out in its recommendations to Belgium¹, this situation is the result of “special” circumstances. In particular, the financial crisis had a dramatic effect on economic activity, thus weighing heavily on Belgium’s public finances, by way of the cyclical component on the one hand and by way of the structural component associated notably with the stimulus plan on the other, as recommended by the European Commission in October 2008.

The deterioration in the balance by 4.7 percentage points of GDP in 2009 results exclusively from a drop in the primary balance of 4.8 percentage points (-2.3% in 2009). This fall in the latter is offset by a slight fall in interest charges (-0.2% of GDP) in a climate of softening monetary policy, increased aversion to risk and economic recession.

The deterioration in public finances affected all entities of the public administrations. However, entity I – the federal government and social security - suffered markedly more severely from the effects of the

¹ ESA Document (2009) 1548/2.

economic and financial crisis owing to the markedly more significant action of the automatic stabilisers at that level. Whilst entity I's deficit deteriorated by 4 percentage points to reach -5% of GDP in 2009, that of entity II – Regions/Communities and local authorities - underwent a markedly more limited decline of 0.6 percentage points to reach -0.8% of GDP in 2009.

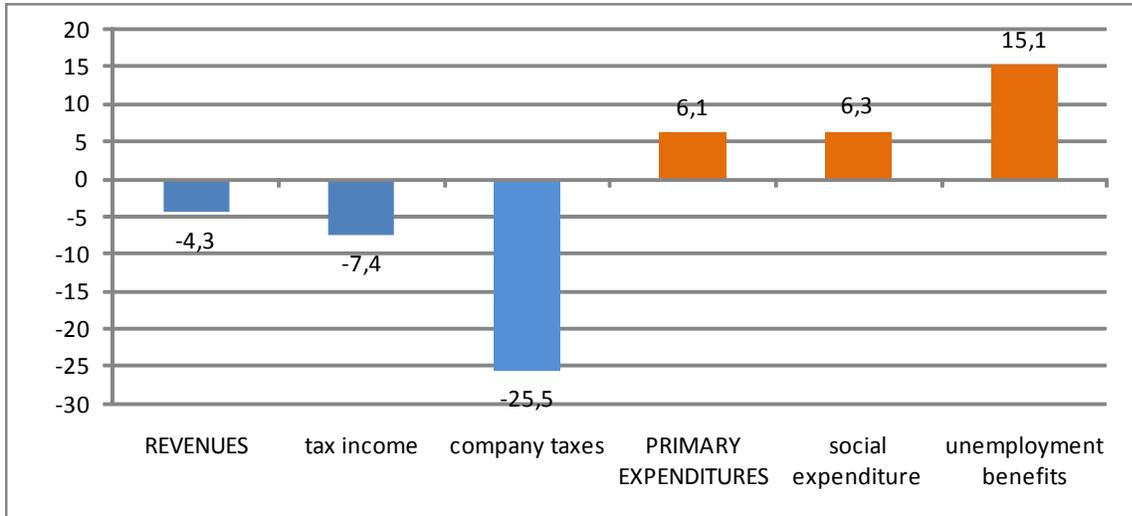
In terms of primary expenditure, a significant rise of +6.1% was recorded in 2009 compared to 2008. This rise is particularly significant for social security (+6.3%), taking account notably of the impact of the economic crisis on expenditure for unemployment (+15.1%) and the beginning of the effects of the ageing of the population. Another by no means negligible factor stems similarly from the time lag between the rise in prices, which occurred in 2008, and that in salaries and social benefits which weigh heavily on the increase in expenditure in 2009.

The economic crisis had a similarly major effect on revenues, showing a fall of 4.3%, which includes -7.4% for tax revenues. This drop is difficult to explain in terms of the historical elasticity of tax revenues in response to economic growth² ; the deep recession seems to have brought with it – as in other countries – a more significant fall than was forecast initially. It is chiefly company taxation (-25.5%) and also withholding tax on unearned income (-22%) that are suffering the full force of the economic and financial crisis. Moreover, discretionary measures to lower charges relating to employment have been decided ('jobkorting' in the Flemish Community and measures under the central agreement for 2009-2010).

Moreover, temporary measures relating to both revenues and expenditure are having an adverse effect on the balance of 0.8% of GDP. These involve notably the fast-tracking of tax assessments, certain judicial decisions (Cobelfret) and certain measures under the stimulus plan, such as intervention regarding households' electricity and gas bills, the speeding-up of certain investments and the temporary lowering of VAT for the building industry.

² Around 1.3

Chart 2: Factors explaining the deterioration of the balance in 2009 (percentage variation compared to 2008)



Source : NBB (2009)

Although very large, the deficit in Belgium's public finances nonetheless remains below the European average. The deficits anticipated for the euro area and the EU-27 are in fact -6.4% of GDP and -6.9% of GDP respectively, according to the European Commission's projections in November 2009.

This relatively better result stems from the concern of the Belgian authorities to avoid budgetary drift in view of Belgium's high level of debt. Thus, various actions have been undertaken with the aim of limiting the deficit of the public administrations.

Various budgetary controls have been carried out; the governments of the Regions and Communities have adjusted their budgets several times and measures have been taken notably in the area of operating costs relating to the cabinets and administrations and grants/allocations. Moreover, in accordance with the European Commission's recommendations, the stimulus plans put into effect have been more limited owing notably to the inherent characteristics of Belgium's open-market economy.

On top of this, the various levels of government entered into a co-operation agreement on 15 December which fixes the targets for 2009, not only for entity II (and sub-entities) but also for entity I.

2.2 Medium-term path for Belgian public finances in line with the recommendations of Europe

In the supplement to the stability programme in September, the Belgian authorities had undertaken to restore balance to Belgian public finances in 2015 at the latest. Furthermore, it was forecast that the threshold of -3% of GDP authorised by the Treaty would, for its part, be achieved in 2013. This path forecast an effort of 1.5% of GDP over the period 2010-2011 and subsequently an annual effort of 1.3% of GDP.

Table 5: Comparison of the path (January 2010) and the supplement to the stability programme (September 2009)

% GDP	2008	2009	2010	2011	2012
Stability Programme Complement September 2009	-1,2	-5,9	-6,0	-5,5	-4,4
Stability Programme January 2010	-1,2	-5,9	-4,8	-4,1	-3,0

In the meanwhile, macroeconomic prospects have improved considerably in the short term with a relatively marked revival of the business cycle in the third quarter of 2009, whereas what was expected a few months ago was a recovery of activity only in the first half of 2010.

Moreover, in the context of the excessive deficit procedure, the Ecofin Council issued recommendations with regard to Belgium on 2 December 2009. In particular, the Council recommended expanding the programme of budgetary consolidation and achieving the threshold of -3% of GDP as from 2012.

More recently, in its last opinion on 15 January, the High Council of Finance (HCF) expressed itself in favour of an adjustment of the path initially proposed in September 2009, taking account of more recent macroeconomic developments and budgets as published by the various levels of government. Based on these elements, it adopted a path of budgetary consolidation in keeping with the recommendations of the Ecofin Council.

It is in this context that the Belgian government decided to update its budgetary path as initially forecast. The budgetary consolidation path for Belgium's public finances in the short and medium terms is based on two essential objectives:

1. The balancing of public finances in 2015 at the latest, thus confirming the undertaking made by the Belgian authorities in April 2009 ;
2. The intermediate target of a deficit of not more than 3% to be achieved in 2012.

The targets defined by the Belgian authorities provide for an improvement in the public administration balance of +1.1% of GDP in 2010, +0.7% of GDP in 2011 and +1.1% in 2012, representing a cumulative improvement of 2.9% over the period 2009-2012.

Table 6: Normalised overall balance

% GDP	2009	2010	2011	2012	2013	2014	2015
General government	-5,9	-4,8	-4,1	-3,0	-2,0	-1,0	0,0
Entity I	-5,1	-3,8	-3,6	-2,6			
Entity II	-0,8	-0,9	-0,5	-0,4			
Balance improvement		1,1	0,7	1,1	1,0	1,0	1,0
Cumulative balance improvement		1,1	1,8	2,9	3,9	4,9	5,9

The path proposed takes as its point of departure the multi-year budgets of the various entities implemented in the course of October :

- The federal government has not only implemented the budget for 2010 but has also drawn up a detailed preliminary calculation for 2011, thus breaking with the tradition of an annual budget. This multi-year adjustment programme has been drawn up for the federal level and social security. Moreover, the targets forecast initially have been adjusted with the aim of taking account of the impact of the more favourable economic position;
- At the federate entity level, the reduction in the deficit corresponds to the path published by the various entities over the period 2010-2012.

A special chapter details all the measures taken by the various levels of government. For entity I, the whole package of measures amounts to 2.1 billion EUR in 2010 and 3.4 billion EUR in 2011. In accordance with the opinion of the HCF, the measures present a steadily growing budgetary return: limiting of the reference rate for notional interest, contribution of the banking sector, steps to combat fraud and partial non-replacement of the number of officials receiving a pension (see Chapter 4 for further details).

The programme presented in the special chapter and decided in Autumn 2009 displays responsibility and solidarity. It shows responsibility in that the Government is opting, in view of Belgium's high level of

debt, to begin budgetary consolidation as from 2010. Furthermore, it shows solidarity at various levels. Concrete measures have been taken to combat tax and social fraud, to reduce behaviour harmful to the environment and to force the sector at the root of the crisis to make a contribution. Moreover, measures have been taken with the aim of reducing the negative effects of early retirement on the employment rate of the elderly (solidarity between generations).

At the federal level, other measures have been decided that will be presented in greater detail in a supplement to be filed on 2 June 2010 at the latest. Thus, the federal government has undertaken to propose a reform of the pensions of local authority officials for the budgetary control in March 2010, with the target of application on 1 January 2011. This draft law will need to uphold the principle of solidarity on the one hand and promote increased responsibility amongst local authorities on the other.

In accordance with the Ecofin Council's recommendations, the orientation of the strategy aimed at correcting the excessive deficit will be presented in a supplement that will be filed on 2 June 2010 at the latest. The figures for revenue and expenditure for the years 2011 and, chiefly, 2012 are therefore included by way of an estimate, their values being essentially indicative.

With the aim of anticipating any non-realisation of targets, particularly enhanced budgetary controls will be held at shorter intervals. A budgetary circular has been approved at the federal level, which provides that no new initiatives may be proposed by the various departments, even if they are compensated for. If the Council of Ministers were to decide, in spite of everything, to approve a measure exceptionally, it would moreover have to be offset entirely by cost savings of the same nature and that present the same return. If it should turn out that the budgetary measures envisaged do not produce the anticipated budgetary return, the measures will be adjusted as a consequence.

The targets defined by the Belgian authorities are conditional on the development of the economic cycle, which is still largely uncertain. If economic growth is insufficient to achieve the target of a deficit of 3% in 2012, the government is willing to take the necessary exceptional measures to achieve the undertakings for 2012. Stabilisation of the public debt and a rapid return to balance are essential conditions for ensuring the sustainability of public finances in the longer term.

Nonetheless, if the recovery in the business cycle proves not to be lasting and economic performance is significantly below the scenarios adopted ("double dip recession"), the defined path and, in particular, the interim target of 3% would be more difficult to achieve. In contrast, if economic growth were to be more vigorous, the automatic stabilisers will allow a more rapid reduction in the deficit and the public debt.

As for the undertaking to return to balance in 2015, this has been entirely maintained.

Moreover, if the government were to benefit prior to the horizon of 2012 from early repayments of the holdings in the financial sector and any added value, the entirety of these amounts would be allocated to a more rapid reduction of the debt and/or the deficit.

The government believes that this path complies with the Ecofin Council's recommendations, in that it provides for Belgium's public finances to conform once again to the Stability and Growth Pact as from 2012 and in that the efforts are spread in a balanced way over the whole period.

2.3 Co-operation agreements

In accordance with the government's undertaking in the context of the supplement to the stability programme in September 2009, the distribution of the effort between levels of government was formalised in two successive co-operation agreements (see the annexed documents). Following on from the decisions taken in September, the distribution of efforts is based on a 65/35 split for entity I and entity II respectively on average over the period 2010-2012.

These agreements are essential with the aim of strengthening the sustainability of Belgium's public finances in the short and medium terms. These are the first formal agreements since 2000. However, new undertakings will be necessary in the longer term with the aim of ensuring viability of public finances and spreading budgetary charges fairly in the context of population ageing.

The agreement of 15 December 2009 fixes the budgetary targets for 2009 and 2010. This agreement not only determines the targets for entity II but also for entity I. Moreover, it separates out the targets by sub-entities (Walloon Region, French Community, Flemish Community, Brussels-Capital Region, French Community Commission and German-speaking Community).

A second agreement will be signed in February with the aim of fixing the respective targets for the years 2011 and 2012.

As well as formalising the targets for entity I and entity II, the co-operation agreements also contain major undertakings aimed at improving the quality of the ESA 95 accounts of local authorities. In future, these data will be completed and transmitted more rapidly.

In the context of the recently signed co-operation agreements, the Regions, acting as the respective supervisory governments for the local authorities, have undertaken to oversee strict observance of the ESA 95 standards for local authorities' accounts. However, a transition period has been provided for (2012-2013)³.

In this context, a working group met on 25 January, under the direction of the National Bank of Belgium, with the aim of determining the methods and timetable for applying the ESA 95 regulations at local authority level. It was agreed that the working group will deliver a first report on how the work is progressing on 19 March 2010.

This formalisation of budgetary agreements thus reinforces the credibility of the Belgian authorities' undertaking on budgetary consolidation and thus complies with the various recommendations of the international institutions (IMF/OECD).

2.4 The year 2010 marks the end of structural deterioration of public finances in an economic climate that remains fragile and in a context of population ageing

Since the beginning of the financial crisis, estimates of potential growth have been considerably downgraded. Whereas prior to the financial crisis, potential growth was estimated at slightly over 2%, recent projections on this topic seem to indicate that it is rather in the area of 1.3% - 1.5%. Between 2008 and 2010, potential growth should fall from 1.8% to 1.3%, subsequently picking up slowly and reaching 1.5% in 2012 (and 1.6% in 2013-2014)⁴.

However, estimates of potential growth are very uncertain, and particularly so in periods of crisis characterised by major volatility of the economic data. To determine the likelihood of the crisis causing a

³ The ESA 95 regulations must be applied on a multi-year basis (one municipal legislature) in order to take account of the investment cycle of the local authorities.

break in the trend and/or changes in behaviour of economic agents, a certain degree of distance will in fact be necessary.

However, account can be taken of certain elements that support the proposed estimates. The financial crisis seems to have affected potential growth via various channels. In the first place, the capital base has been negatively affected to a significant extent, notably following numerous insolvencies (9,382 firms in bankruptcy in 2009, up by 10.7% compared to 2008) and the major reduction in investment (-3.7% in 2009). Secondly, the increase in unemployment and the closure of firms is likely to give rise to a major loss of human capital and a rise in structural unemployment. Finally, taking account of the financial constraints placed on firms, notably following the rise in the cost of credit and the potential fall in availability (-2.8% of the volume of lending in November 2009⁵), the crisis could lead to a reduction in expenditure on R&D.

In spite of this substantial fall in potential growth, the output gap has turned decidedly negative taking account of the scope of the recession. From +1.8% in 2008, it decreases to -2.8% in 2010, subsequently increasing and reaching -1.8% in 2012.

This revision of potential growth is not without effect on estimates of the structural balance, in two respects.

Firstly, the revision of potential growth relates not only to the future but also to the past, an aspect not without consequences for the level of the structural deficit during the preceding period. In fact, whereas in 2007 and 2008 all the estimates were still indicating that Belgium's public finances were virtually in balance in 2007, the recent revision of potential growth (and therefore the output gap) gave rise to a deterioration in the structural balance of public finances for the past.

Secondly, the downward revision of potential growth in the next few years further reinforces the negative level of the structural balance.

⁴ The European Commission adopts different scenarios and obtains a different potential growth. For a comparison of the methodology and scenarios used in this note with those of the European Commission, see working paper 10-09 of the Federal Planning Bureau (www.plan.be) : Igor Lebrun, «Impact de la crise financière sur le PIB potentiel de la Belgique» (September 2009).

⁵ However, a major part of this fall results from the fall in demand.

Table 7: Cyclical and structural development of the overall balance

<i>% of GDP</i>	2008	2009	2010	2011	2012
1. Real GDP growth	1,0	-3,1	1,1	1,7	2,2
2. Net lending of general government	-1,2	-5,9	-4,8	-4,1	-3,0
3. Interest expenditure	3,8	3,6	3,7	3,7	3,8
4. One-off and other temporary measures ¹	0,0	-0,8	0,0	0,0	0,0
5. Potential GDP growth	1,8	1,4	1,3	1,4	1,5
contributions:					
- labour	0,6	0,4	0,3	0,3	0,3
- capital	1,0	0,8	0,8	0,8	0,8
- total factor productivity	0,2	0,2	0,2	0,3	0,4
6. Output gap	1,9	-2,6	-2,8	-2,5	-1,8
7. Cyclical budgetary component	1,0	-1,4	-1,5	-1,4	-1,0
8. Cyclically-adjusted balance (2 - 7)	-2,2	-4,5	-3,3	-2,7	-2,0
9. Cyclically-adjusted primary balance (8 + 3)	1,6	-0,9	0,4	1,0	1,8
10. Structural balance (8 - 4)	-2,2	-3,7	-3,3	-2,7	-2,0

Taking account of the scenarios adopted and the set budgetary targets, the structural balance should again undergo an improvement of 1.7% of GDP over the period 2010-2012, after deteriorating steadily for several years (-2.7% of GDP over the period 2004-2009). The structural deficit should thus return, by 2012, to a lower level than that observed in 2008. The improvement in the primary structural balance is even more marked (+1.9%), taking account of the increase in interest charges over the time frame adopted.

2.5 A responsible budgetary policy for both revenue and expenditure in a difficult and uncertain economic climate

The budgetary consolidation programme fits in with controlling the growth of expenditure and a fairer tax system. However, in order not to compromise the frail economic recovery, various governments wished to avoid taking overly sharp measures. In fact, in this phase of the crisis, it is important to avoid harming the foundations of a lasting economic recovery and damaging the fragile confidence.

Excluding expenditure on social security, the ratio of expenditure (% of GDP) shows a reduction of -0.4% of GDP in 2010. This reduction is the result of the overall package of measures taken in the context of the various respective budgets. These measures - which are detailed in Chapter 4 – are intended to increase

efficiency and control of public service costs and to ensure the budgetary sustainability of social security (service cheque measures, time credit measures, healthcare measures and early retirement measures).

In the wake of the budgetary measures that have been decided, the anticipated rise in the revenue ratio amounts to 1.4% of GDP⁶ in 2010. These rises - which may seem exaggerated in an economic climate that remains fragile - are the result of various factors which tend to reinforce themselves :

- Budgetary measures (1.1 billion at the entity I level and around 600 million EUR at the level of the Regions)
- Technical corrections and the effect of cyclical measures producing a sum of 5.3 billion EUR (fast-tracking of tax assessments in 2009, decision of the Court of Appeal in 2009, over-reaction to the cyclical mechanism for notional interest)

Apart from the withdrawal of the 'jobkorting' measure in the Flemish Region, the increase does not result in any way from a rise in the tax system relating to employment.

On the contrary, with the aim of supporting employment, the government has even set out various measures – temporary and structural – during the preparation of the budget. Thus, the measures set out in the anti-crisis law of 19 June 2009 allowing firms to increase flexibility in the labour force (time credit, reduction in working time and temporary suspension of employees' employment contracts) have been extended until 30 June 2010. These measures are aimed at limiting as far as possible the effects of the crisis on employment and thus avoiding – as historical experience shows – a rise in structural unemployment (hysteresis effect). Moreover, temporary and structural measures to lower targeted payroll charges have similarly been decided for young people and older workers – specifically the target groups for which the employment rate is still very low.

Other measures, such as the reduced rate of VAT in the building industry, have also been extended with the aim of supporting certain sectors of activity that have been affected more severely by the economic crisis.

Similarly for 2012, it will be necessary to adopt a scenario of balanced efforts between revenue and expenditure.

⁶ For further details, see the note « estimations des recettes fiscales 2010-2011 », Valenduc (2009)

Table 8: Budgetary prospects for general government

	2008 level	2008 % GDP	2009	2010	2011	2012
Net lending by sub-sector						
1. General government	-4.061	-1,2	-5,9	-4,8	-4,1	-3,0
2. Central government	-5.424	-1,6	-4,3	-3,3	-3,3	-2,6
3. State government	-205	-0,1	-0,6	-0,6	-0,3	-0,2
4. Local government	-279	-0,1	-0,2	-0,4	-0,2	-0,2
5. Social security funds	1.848	0,5	-0,8	-0,5	-0,3	0,0
General government						
6. Total revenue	168.192	48,8	47,7	49,1	49,5	49,8
7. Total expenditure	172.426	50,0	53,7	53,9	53,6	52,8
8. Net lending/borrowing	-4.061	-1,2	-5,9	-4,8	-4,1	-3,0
9. Interest expenditure	13.002	3,8	3,6	3,7	3,7	3,8
10. Primary balance	8.936	2,6	-2,3	-1,1	-0,4	0,8
11. One-off and other temporary measures		0,0	-0,8	0,0	0,0	0,0
Selected components of revenue						
12. Total taxes	102.689	29,8	28,0	29,4	29,5	29,7
12a. Taxes on production and imports	43.261	16,6	15,0	16,3	16,4	16,6
12b. Current taxes on income, wealth, etc	57.058	12,6	12,4	12,4	12,4	12,4
12c. Capital taxes	2.370	0,7	0,7	0,7	0,7	0,7
13. Social contributions	55.605	16,1	16,7	16,6	16,5	16,6
14. 14. Property income	2.626	0,8	0,8	0,8	0,9	0,9
15. Other	7.273	2,1	2,2	2,4	2,5	2,6
16. Total revenue	168.192	48,8	47,7	49,1	49,5	49,8
p.m. Tax burden	160.512	46,6	45,4	46,7	46,8	47,2
Selected components of expenditure						
17. Compensation employees + intermediate consump	54.262	15,7	16,7	16,5	16,1	15,7
18. Social payments	80.249	23,3	25,3	25,8	25,9	25,7
19. Interest expenditure	13.002	3,8	3,6	3,7	3,7	3,8
20. Subsidies	7.131	2,1	2,1	2,3	2,4	2,2
21. Gross fixed capital formation	5.717	1,7	1,7	1,7	1,8	1,9
22. Other	12.066	3,5	4,2	3,8	3,7	3,6
23. Total expenditure	172.426	50,0	53,7	53,9	53,6	52,8

2.6 The year 2011 marks the end of the snowball effect

Following a major fall of 29.5% of GDP over the period 1999-2007, public debt has increased strongly in the last few years (from 84.2% in 2007 to 97.9% in 2009), thus bringing an end to an uninterrupted decline since 1993.

This rise does not result primarily from budgetary policy in the strict sense but rather from interventions in the financial sector, amounting to 6.3% of GDP, which were indispensable to stabilise the financial system.

The guarantees granted to the financial sector have, on the other hand, no impact on gross consolidated debt⁷, since they are regarded in the national accounts as contingent liabilities and are taken off the balance sheet. These guarantees, reaching a total of 92.4 billion EUR, or 27.4% of GDP, constitute a maximum theoretical risk. With the aim of controlling this risk, the development of the various underlying assets benefiting from the guarantees is tracked and controlled on a permanent basis by a monitoring committee.

Two-thirds of these guarantees apply to interbank debts or “wholesale market” debts of the credit institutions (61 billion EUR) and close to one-third to possible future losses relating to structured credit (31.4 billion EUR). In accordance with European regulations, the guarantees are granted to the Belgian institutions in exchange for a payment in line with market conditions. With regard to the year 2009, the total revenue⁸ forecast to come from this assistance is budgeted at 666.1 million EUR. The impact on interest charges of these capital interventions is estimated at a little over 500 million EUR. In the strict sense, the interventions have therefore had a positive impact on the budget up to now.

⁷ For further details of the guarantees granted in the context of operations to rescue the financial system, see “Impact de la crise financière et des mesures d’aide sur la gestion de la dette de l’Etat et sur l’évolution des finances publiques”, National Audit Office, December 2009.

⁸ Including the guarantee on bank deposits and branch 21 products.

Table 9: Impact of support measures taken by the Belgian State on public debt and granting of guarantees

	LENDING & PARTICIPATIONS						Net total 2008-2009	GUARANTEES (e)
	federal 2008	non federal 2008	total 2008	federal 2009	non federal 2009	total 2009		
Fortis: first recapitalisation	4,7		4,7				4,7	Fortis Holding (Cashes) 2,35
Fortis: second recapitalisation	4,72		4,72				4,72	Fortis Holding (financ. SPV) 1
Fortis: capital injection SPV RPI	0,6		0,6	0,14		0,14	0,74	SPV RPI 4,365
Fortis: loan to the SPV RPI (a)	2		2	-2		-2	0	Fortis Bank portfolio toxic assets 1,5
Fortis: bridging loan for Fortis Holding (a)	3		3	-3		-3	0	
total Fortis	15,02	0	15,02	-4,86		-4,86	10,16	
Dexia: recapitalisation federal government	1		1					interbank loan (d) 60,5
Dexia: recapitalisation Flemish government (b)		0,5	0,5					port. FSA (f) 7,2
Dexia: recapitalisation Walloon government		0,35	0,35					
Dexia: recapitalisation Brussels government		0,15	0,15					
total Dexia	1	1	2				2	
Ethias: recapitalisation federal government	0,5		0,5					
Ethias: recapitalisation Flemish government (b)		0,5	0,5					
Ethias: recapitalisation Walloon government		0,5	0,5					
total Ethias	0,5	1	1,5				1,5	
KBC: loan federal government	3,5		3,5					port. CDO's 15,32
KBC: loan Flemish government					3,5	3,5		
total KBC	3,5		3,5		3,5	3,5	7	
Grand Duchy of Luxembourg: loan (Kaupthing)(c)				0,15		0,15	0,15	
Municipal holding (g)								0,25
Total	20,02	2	22,02 (a)	-4,7	3,5	-1,2	20,82	92,49
% of GDP			6,39			-0,36		27,44

Source : HCF (2010)

Unlike in 2008, the rise in the debt of 2.6% of GDP in 2009 results entirely from the deficit recorded in the context of the recession.

Table 10: Development of the public debt ratio

% of GDP	2008	2009	2010	2011	2012
1. Gross debt	89,8	97,9	100,6	101,4	100,6
2. Change in gross debt ratio	5,6	8,0	2,7	0,8	-0,8
	Contributions to changes in gross debt				
3. Primary balance	2,6	-2,3	-1,1	-0,4	0,8
4. Interest expenditure	3,8	3,6	3,7	3,7	3,8
5. Stock-flow adjustment	6,8	0,3	0,2	0,2	0,2
Implicit interest rate on debt	4,6	4,0	3,9	3,9	3,9

Taking account of the scenarios adopted, the debt should continue to grow in 2010 and 2011, driven by higher interest charges on the one hand and the inherent dynamics of the primary balance on the other. In fact, the anticipated level of the latter does not allow the debt ratio to be stabilised before 2011.

However, stabilisation, and more precisely reduction, of public debt will be evident as from 2012, when the debt ratio should again approach the limit of 100%.

Table 11: Primary balance required to stabilise debt

<i>% GDP</i>	2008	2009	2010	2011	2012
Required primary balance for debt stabilisation	1,4	5,4	1,4	0,3	-0,3
Primary balance Stability Programma january 2010	2,6	-2,3	-1,1	-0,3	0,8

3 Comparison with the supplement to the stability programme for 2009-2013 and sensitivity analysis

3.1. Acceleration of paths compared to the previous stability programme

The previous revision of the stability programme took place in September 2009 at the request of the European Commission. The supplement to the stability programme introduced in April 2009 already took account of the strong slowdown in growth in 2009.

As was emphasised in Chapter 1, even if economic prospects improved between September 2009 and January 2010, nonetheless uncertainty persists in the medium term.

The table below compares the underlying growth in GDP and also the targets appearing in the supplement of September 2009 with those in the present stability programme.

Table 12: Comparison of growth, overall balance and debt with the supplement to the previous stability programme

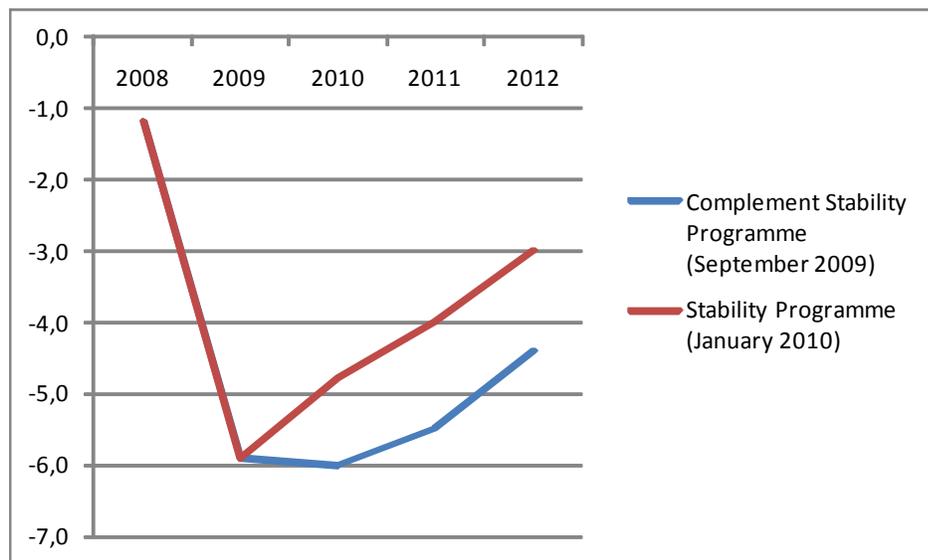
% of GDP	2008	2009	2010	2011	2012
Real GDP growth					
Previous update	1,1	-3,1	0,4	1,9	2,4
Current update	1,0	-3,1	1,1	1,7	2,2
Difference	-0,1	0,0	0,7	-0,2	-0,2
General government net lending					
Previous update	-1,2	-5,9	-6,0	-5,5	-4,4
Current update	-1,2	-5,9	-4,8	-4,1	-3,0
Difference	0,0	0,0	1,2	1,4	1,4
General government gross debt					
Previous update	89,7	97,5	101,9	103,9	104,3
Current update	89,8	97,9	100,6	101,4	100,6
Difference	0,1	0,4	-1,3	-2,5	-3,7

As already indicated above, the estimate for economic growth in 2010 adopted in the present stability programme is greater than that in September. For 2011 and 2012, the growth forecasts are a little lower today.

Taking account of the budgets for 2010, the multi-year plans and budgets of the various federate entities and the more favourable economic forecasts, the adjustment of the budgetary consolidation programme constitutes an ambitious programme complying with the recommendations of the Ecofin Council dated 2 December, which should allow the credibility of public finances to be strengthened in the medium term.

The deficit as forecast in this programme would decrease by 2.9% over the period 2009-2012 based on the proposed growth scenarios. The reduction in the deficit is therefore greater than that forecast during the supplement to the stability programme in September 2009, amounting to 1.4% of GDP, in a context where cumulative growth has been reviewed with +0.3% over the same period. In fact, the preceding programme forecast a deficit of 4.4% of GDP in 2012.

Chart 3 : Comparison of the overall balance



This adjustment in the path also gives rise to an improvement in the structural balance of 1.7% of GDP over the period 2009-2012.

As a consequence, and taking account of similar scenarios in the area of interest rates, the debt ratio improves by 3.7%. Public debt (in % of GDP) should thus begin to fall not with effect from 2014, but from as early as 2012, when it should again be close to the critical threshold of 100%.

3.2. Sensitivity analysis

The events of the last 18 months illustrated the unpredictable nature of economic development. Uncertainty continues to weigh on the current forecasts. In the highly uncertain current economic climate, an analysis of sensitivity is extremely important. Consequently, the question of the impact that a gap in terms of real GDP growth and fluctuations in interest rates would have on the overall balance has been examined.

3.2.1. Gap in terms of GDP growth

For GDP growth, three alternative scenarios have been examined. The first scenario starts from the premise that GDP growth during the period 2009-2012 would be greater by 0.5 percentage points compared to the scenario used in the framework of the stability programme. In the second scenario, it would be lower by 0.5 percentage points. The third scenario examines the effects of a downturn of 1% on an annual basis, given that there is a risk of a new downturn or limited economic recovery.

It is important to emphasise in this respect that a constant elasticity of public finances is assumed compared to GDP (specifically 0.54, including 0.47 for revenue and 0.07 for expenditure).

Table 13: Sensitivity of the overall balance to variations in growth

<i>% of GDP</i>	2010	2011	2012
Stability programme			
Real GDP growth	1,1	1,7	2,2
Financing balance	-4,8	-4,1	-3,0
0,5 percentage point positive variation			
Real GDP growth	1,6	2,2	2,7
Financing balance	-4,5	-3,6	-2,2
0,5 percentage point negative variation			
Real GDP growth	0,6	1,2	1,7
Financing balance	-5,0	-4,6	-3,8
1 percentage point negative variation			
Real GDP growth	0,1	0,7	1,2
Financing balance	-5,3	-5,2	-4,6

If, in the years to come, growth were systematically 0.5 basis points greater than the estimates and the automatic stabilisers were left free to act, the gap compared to the central scenario would amount to 0.8% of GDP in 2012. In this scenario, a deficit of 2.2% of GDP would then be recorded instead of a deficit of 3%. If growth were to exceed the forecasts, the federal government has undertaken to use this surplus to speed up the reduction of public debt.

In the case of growth 0.5 basis points lower than the estimates, the deficit would amount to 3.8% of GDP in 2012. If annual growth were 1% lower, the deficit would amount to 4.6% of GDP in 2012.

3.2.2. Gap in terms of interest rates

A rise in interest rates on the markets affects public finances via various channels. In the first place, this increase directly affects interest charges, which in turn damages the overall balance. Given the scope of Belgium's debt, which is still considerable, it remains sensitive to fluctuations in interest rates. Moreover, volatility on the bond market has increased somewhat over the last few months, investors having expressed some doubt as to the ability of some Member States to cope with their level of debt.

Secondly, a rise in interest rates has an unfavourable influence – via the traditional channel of interest rates - on economic activity (consumption and investment) and consequently, on the balance of public finances. In addition, depending on the nature of the rise in interest rates (short vs long term), financial institutions could see their profitability fall in the context of a flattening of the yield curve. Given that the position of the financial institutions remains fragile, the unfavourable impact on economic activity could therefore be further strengthened.

Taking account of these elements, a sensitivity analysis is important in the case of Belgium. Management of the federal government’s debt (which accounts for more than 90% of total public debt) is notably focused on controlling the various risks (exchange rate risk, interest rate risk and refinancing risk). This control of risk fits in with the framework of the general directives on debt, drawn up every year.

In view of the average duration of debt liability, an increase in the interest rate will affect interest charges after a certain time lag.

The table below illustrates the impact of an uplift of 100 basis points in the interest scenarios for the period 2010-2012 on interest charges. In the short term, a rise in interest rates would have an impact of 0.2% of GDP on the balance; in the medium term, the impact could climb to 0.4% of GDP on an annual basis. In this respect, it is worth noting that a non-linear rise in short-term and long-term interest rates could occur. In fact, in the event of inflation speeding up, there is a risk of seeing the short-term interest rate increasing, whereas the long-term rate could show a more significant rise in the wake of higher risk premiums.

Table 14: Impact of a modification of interest assumptions

<i>% of GDP</i>	2010	2011	2012
Degree to which interest charges deviate from the scenario	0,2	0,3	0,4

4 Budget for 2010 – 2011

4.1. Lines of force and macroeconomic starting points

Reducing the public deficit in an economic climate that remains fragile

Following in the footsteps of other European countries, Belgium has been faced, in 2009, with a public deficit growing under the effect of the negative economic trend. For 2009, the deficit is now estimated at 5.9% of GDP. A deficit of such a scale is not sustainable. The risk of the debt snowballing is again looming on the horizon, consumer confidence is dented and the financing of the cost of ageing is saddled with an additional burden. When the budget for 2010 (and 2011) was being drafted, the challenge consisted in preserving the sustainability of public finances whilst at the same time mapping out an improvement path that did not compromise the fragile recovery in growth. In this respect, it is important for the reduction of the public deficit to go hand in hand with the steady ending of a range of stimulus measures.

Multi-year outlook

Now more than ever, it was important to set the budget for 2010 in a multi-year approach. The government developed its medium-term strategy in the supplement to the stability programme sent to the Commission in September 2009. This was fleshed out earlier by the various levels of government. At the entity I level (federal government and social security), a determined decision was made to draw up, at the same time as drafting the budget for 2010, a detailed preliminary calculation of the budget for 2011. For their part, the Communities and Regions have mostly combined the drafting of their budget for 2010 with the compilation of a more or less detailed multi-year budget, or at least determined the path for their balances.

Table 15 provides a snapshot of the overall balances for 2010 and 2011. For 2010, these were defined in the co-operation agreement entered into with the Communities and Regions on 15 December 2009. This agreement incorporates the balances as they appear in the various budgets for the sub-sectors. The various levels of government have undertaken to consider the targets incorporated in the latter for 2010

as minimum targets. This agreement will be supplemented by a second co-operation agreement in February which will fix the targets for the period 2011-2012.

Table 15: Co-operation agreement of 15 December 2009 and targets for the stability programme 2009-2012

% GDP	Budgets		Objectives		Difference	
			Stability Programme			
	2010	2011	2010	2011	2010	2011
Entity I (1)	-4,1	-4,0	-3,8	-3,6	0,3	0,4
Federal government	-3,6	-3,7	-3,3	-3,3	0,3	0,4
Social security	-0,5	-0,3	-0,5	-0,3	0,0	0,0
Entity II	-1,0	-0,5	-0,9	-0,5	0,0	0,0
Communities and regions (1)	-0,6	-0,3	-0,6	-0,3	0,0	0,0
Local governments (2)	-0,4	-0,2	-0,4	-0,2	0,0	0,0
Gezamenlijke overheid	-5,1	-4,5	-4,8	-4,1	0,3	0,4

- (1) The budgetary figures are based on the annual budgets and also the multi-annual budgets for entity I and the Communities and Regions respectively.
- (2) There are no consolidated budgets for the local authorities ; for the budgetary figures relating to 2011, the table above uses the figures incorporated in the supplement to the stability programme in September 2009.

Improved economic situation

The budgets for 2010-2011 were based on the economic budget drawn up by the Federal Planning Bureau at the request of the National Accounts Institute in September 2009. As already explained in Chapter 1, the recovery emerged more strongly than forecast during the second half of 2009. This justifies an upward adjustment of the forecasts for 2010. Table 16 compares the growth prospects used in the context of drafting the budget, both by the federal government and the various Communities and Regions, with those used currently to prepare the stability programme.

Table 16: Macroeconomic assumptions

<i>% change, unless otherwise stated</i>	Budget 2010-11			Stability programme 2009-12		
	2009	2010	2011	2009	2010	2011
Real GDP growth	-3,1	0,4	1,9	-3,1	1,1	1,7
Nominal GDP	337,1	343,1	356,0	337,9	346,0	358,3
Consumption price index	0,0	1,5	1,6	0,0	1,5	1,7
Unemployment (% , Eurostat definition)	8,2	9,4	9,6	8,2	9,4	9,6
Short term interest rate (3 months)	1,3	1,5	2,7	1,3	1,5	2,5
Long term interest rate (10 years)	4,0	4,1	4,5	3,7	3,7	4,1

A detailed analysis of the impact of the business cycle on the budgetary balance will certainly be carried out during the budgetary control that traditionally takes place in Spring 2010. It is apparent in any case from a comparison of the macroeconomic starting points that the various governments have used cautious scenarios when drafting the budgets for 2010 (and 2011). Given that growth is expected to be greater than forecast at the time, the updated prospects do not jeopardise the budgetary result in any way. Over the whole of the two years, a positive growth differential of 0.5% can be seen. The updated estimates do not therefore jeopardise the advocated budgetary result. On the contrary, the government is undertaking to allocate the full amount of any windfalls stemming from growth in excess of the forecasts to improving the balance.

4.2. The main measures taken in the context of drafting the budget for entity I for 2010 and 2011

4.2.1. General outline

Table 17 provides an overview of the measures taken at the entity I level when the budget for 2010-2011 was drafted. The table follows the logic of the budgetary conclave. An initial package of measures will produce a structural effect of 3.5 billion EUR, or around 1% of GDP. A second package of measures should, once it is in full flow, offset a range of new initiatives so as to preserve the structural improvement in the balance.

Table 17: Outline of the measures decided during the drafting of the budget for 2010-2011

<i>Millions of EUR</i>		2010	2011	Recurrent effect
Economies on expenses		951	1.153	1.153
Primary expenses		200	200	200
of which Personnel		100	100	100
Other		100	100	100
Health care		644	812	812
Social security		107	141	141
Tax income		696	1.075	1.269
of which Professional diesel		141	141	141
Click system for diesel		140	285	290
Deduction for 'Participation exemption'		140	140	140
Tobacco duty		59	118	118
Company cars (emissions)		95	105	105
Advantages in natura (fuel cards)		117	109	109
Other measures		547	1.180	1.100
Fiscal fraud		134	232	232
Social fraud		48	133	133
Financial sector		130	580	500
Energy sector		235	235	235
		2.194	3.408	3.522
Additional measures to compensate new initiatives		338	528	488
of which Deduction of risk capital		200	300	300
New initiatives		719	594	594
Extension of anti-crisis measures		238		
of which VTA reduction for construction		150		
Employment measures		85		
Measures for the self-employed		3		
Complementary measures for labour market		124	204	204
Horeca VTA-reduction		255	255	255
Tax regime farming sector		20	20	20
Poverty plan and social integration		26	26	26
Self-employed		25	58	58
Various measures concerning primary expenses		31	31	31
Net effort Entity I		1.813	3.342	3.417
(% of GDP)		0,5	0,9	1,0

4.2.2. The main measures taken at the level of the federal government and social security

Primary expenditure

Leaving aside the special allocation in favour of social security, growth in the federal government's primary expenditure (according to the budgetary definition) was limited to 1.6% in 2010, representing zero growth in real terms. In this context, a further sum of 126 million EUR has been released in order to implement a range of new initiatives. The increase in primary expenditure was limited due to a series of specific cost savings and a set of linear measures focused on reducing the State's operating costs. Thus, expenditure on operating costs has been reduced by 1.6%. Over and above the cost saving of 0.7% on human resources expenditure for the years 2009 and 2010, a measure that was decided in 2009, an additional reduction of 100 million EUR has been implemented.

Social security

In the field of healthcare, the current legal growth standard (4.5% in real terms) is maintained but part of the resources provided will not be spent, but rather held in reserve. Thus, in the years 2010 and 2011, to uphold its budgetary target, sickness insurance will transfer sums of 350 and 450 million EUR respectively to the overall managements in order to contribute to the financial sustainability of social security. Furthermore, the Future Healthcare Fund will continue to be funded both in 2010 and 2011. For 2010, this involves a sum of 300 million EUR and, for 2011, a sum of 289 million EUR. A sum of 305 million EUR has been released in favour of new initiatives. Partly to create the margin necessary for the latter, a variety of measures focused on controlling expenditure have also been taken; this results in an actual cost saving of 202 million EUR in 2010, of which 60 million EUR falls within the sector of pharmaceutical specialities and 100 million EUR within the sectors of clinical biology and medical imaging.

The financial balance of social security has been sorely tested by the economic crisis. For this reason, the government has decided to provide, in 2010 and 2011, additional financial resources in favour of social security. An exceptional allocation has been granted, of 2.5 billion EUR in 2010 and 2.8 billion EUR in 2011 respectively. Furthermore, an interest-free loan of 1.7 billion EUR in 2010 and 1 billion EUR in 2011 has been granted.

This has not prevented the government from taking a series of measures focused on reducing costs without, however, undermining the confidence of the people within the system. In this case also, cost savings have been made on operating costs, both at the level of the social security institutions (10 million EUR) and at that of the reimbursement of third-party management costs (16 million EUR in 2010, rising to 32 million EUR in 2011). In order to rein in the strong growth in expenditure in the area of service cheques, a series of supplementary measures has been taken in the context of drafting the budget. With effect from 2010, the number of service cheques will be limited to 500 units per user and per calendar year (a cost saving estimated at 23 million EUR in 2010 and 24 million EUR in 2011). Adaptations to the time credit and career break systems, including raising the age limit to be able to qualify for the enhanced benefit for elderly workers reducing their work commitments, should decrease expenditure by 30 million EUR in 2010 and 40 million EUR in 2011. The financial conditions relating to early retirement have also been tightened up. With effect from 1 April, the employer's contributions will vary from 50% to 10% of the additional benefit depending on the age of joining (50% when joining at 52 years of age or less ; 40% when joining at the age of 53 or 54 ; 30% when joining at age 55, 56 or 57, 20% when joining at age 58 or 59 and 10% when joining at age 60 or over). The product of these measures is estimated at 3.9 million EUR in 2010 and 12 million EUR in 2011.

Moreover, a specific contribution of 0.02% has been introduced to cover expenditure resulting from the phenomenon of under-declaration of accidents at work, which brings about a transfer of charges to the sickness/invalidity sector, whereas it should be taken up by the work accidents sector. This measure will provide a return of 15 million EUR with effect from 2010.

Revenue

In the area of tax revenues, a range of measures has been taken which not only exerts a positive impact on the anticipated revenues but which also encourages the population to adopt a more responsible attitude with regard to the environment. The impact of these measures is estimated at 696 million EUR in 2010 and 1,075 million EUR in 2011. Thus, refunds for users of professional diesel will be adapted as from 1 January 2010 to the minimum duty applicable with effect from that date. This represents a reduction in refunds of 25 EUR per 1,000 litres. This measure is estimated to produce 141 million EUR in 2010 and 2011. The government has decided to apply, in 2010 and 2011, the so-called ratchet system for diesel, that is to say the duty on fuel will be increased by a sum corresponding to half the fall in the price, excluding VAT. The product of this measure is estimated at 140 and 285 million EUR respectively. With

regard to company cars, a new system of taxable benefits of all kinds has been established, based on the CO₂ emissions of the vehicle in question. Moreover, the deductibility of car expenses is modulated more strictly depending on the CO₂ emissions and it will be higher for battery-powered cars (both in terms of the purchase price and recharging installations). On top of this, the deductibility of fuel expenses is lowered from 100% to 75%.

Independently of green tax systems, a series of additional tax measures has also been taken. In order to estimate the revenues from duty and VAT on tobacco products, account was taken of the price increase envisaged by the sector (the impact of this measure is estimated at 59 million EUR in 2010 and 118 million EUR in 2011). The conditions for allowing deductibility of definitively taxed income have been tightened up, the minimum sum being raised from 1.2 million EUR to 2.5 million EUR. The product of this adaptation is estimated at 140 million EUR. Also, a series of actions has been decided focused on improving control and collection and on making the operation of SPF Finances more efficient.

Furthermore, the campaign against tax and social fraud is being pursued, notably the international collection of tax credits, the accelerated collection of employee withholding tax and the cross-referencing of the Sigedis and ONSS databases as well as the Dimona database and the database relating to time credit. Moreover, all the databases relating to benefits will now be linked to each other as well as to tax data and foreign income. The impact of these measures has been cautiously estimated at 134 million EUR for the measures relating to tax matters and 48 million EUR with regard to social fraud in 2010, and at 232 million EUR and 133 million EUR respectively in 2011. Only those measures incorporating sufficient detail have been made into a revenue entry for budgetary purposes.

With effect from 1 January 2011, the Special Deposit Protection Fund will protect deposits and “branch 21” products up to 100,000 EUR. In return for this protection, the participating banks and stock exchange companies will deposit in two equal instalments, one in 2010 and the other in 2011, an entry fee of 10 basis points calculated on the deposits on 30 September 2010. The annual contribution payable prior to 31 January of each year is 15 basis points calculated on the deposits on 30 September of the previous year. This is due in the first instance in 2011. As from 1 January 2011, membership of the deposit protection fund will be compulsory for all insurance firms subject to the prudential control of the CBFA. The annual contribution payable prior to 31 January of each year is 15 basis points calculated on the branch 21 holdings on 30 September of the previous year. It is due in the first instance in 2011. The contribution demanded from the financial sector will amount to 130 million EUR in 2010 and 580 million EUR in 2011.

Moreover, the government has decided to put back by 10 years the first stage of the phase-out of nuclear energy in order to preserve the supply of electricity. To this end, use is being made of a clause provided in the current law on the phase-out of nuclear energy (Law of 31 January 2003 on the gradual phasing out of nuclear energy for the purposes of industrial electricity production) which provides that in the event of uncertainty about the continuous supply of energy, it is possible to extend the lifetime of the nuclear power stations. The closure of the oldest nuclear power stations has been put back by 10 years until 2025. Apart from a series of obligations relating to investment in renewable energy and on green energy measures, an annual contribution of 215 to 245 million EUR is being imposed on the nuclear energy sector, intended to finance the government's nuclear policy.

4.2.3. Extension of measures to combat the crisis and new initiatives

The government has granted an additional effort of 388 million EUR in 2010 and 528 million EUR in 2011 in order to create the margin necessary to implement a series of new initiatives. Adaptation of the system for deducting notional interest⁹ constitutes a major element of this effort. The interest rate used to calculate the notional interest deductible on own funds is now no longer fixed as a function of the ten-year yield on the OLO but limited to 3.8% for the tax years 2010 and 2011. This measure is estimated to produce 200 million EUR in 2010 and 300 million EUR in 2011.

In this phase of the crisis, it is important not to undermine burgeoning confidence and throw away the foundations of a lasting economic recovery. A number of measures taken in the context of the stimulus plan will achieve their full effect in 2010. In order to create the financial margin for firms, they have not only been granted temporary payment facilities in 2009 with regard to fiscal and parafiscal debts, but complementary measures have also been taken in order to reduce the cost of labour. The exemption from payment of employee withholding tax has been raised, specifically from 0.25% to 0.75% in 2009 and to 1% in 2010. This represents an additional decrease of 370 million EUR in the cost of labour in 2010. In order to support those industrial sectors that have been affected severely by the recession, reductions in contributions for night work and shift work and also for overtime have been further increased, being raised from 10.7% to 15.6% with effect from 01/06/2009. The impact of these measures was taken into account during the preparation of the budget for 2010 and 2011.

⁹ Established by the Law of 22 June 2005 establishing a tax deduction for risk-bearing capital.

It has also been decided to extend a certain number of measures provided for in the anti-crisis Law of 19 June 2009. This law relating to a variety of provisions in the area of employment during the crisis provided for a reduction in social security contributions in the event of a temporary and collective decrease in working time. This measure has been extended until 30 June 2010. The law referred to also provided for the establishment of the so-called “crisis time credit” system: workers in firms experiencing difficulties (faced with a fall of 20% in their turnover) who reduce their working time are entitled to an additional benefit from the National Employment Office (NEO). These measures have also been extended until 30 June 2010 and the conditions applying to them have been relaxed. Similarly, the system of temporary and collective or partial suspension of the employment contract is extended until mid-2010. These measures have been supplemented by the establishment of a so-called crisis bonus. A manual worker whose employment contract termination is notified between 1 January and 30 June 2010 is entitled to a bonus of 1,666 EUR net. The cost of extending the anti-crisis measures is estimated at 85 million EUR for the arrangement covering salaried workers. Under the self-employed arrangement, measures to help the self-employed threatened by bankruptcy have been extended (3.4 million EUR).

The reduced rate of VAT in the building industry has been extended. Initially, this reduced rate applied to building permits requested up to 31 December 2009; the measure is now extended to 31 March 2010. Its budgetary impact is estimated at 150 million EUR.

The extension of anti-crisis measures has been supplemented by a series of new initiatives focused on stimulating economic activity, particularly the labour market, and supporting purchasing power.

In times of crisis, it is essential to provide additional incentives for the recruitment of groups who have a weak position in the labour market. The so-called “win-win” plan provides, in 2010 and 2011, an enhanced activation of unemployment benefit for young and elderly jobseekers. To this end, a budget of 25 million EUR has been reserved in 2010 and 50 million EUR in 2011. Furthermore, the “low salaries” element in the structural reduction of charges is strengthened, representing 42 million EUR in 2010 and 2011. In the non-profit sector, the reduction in charges for employers is raised, the cost of this measure being estimated at 43 million EUR in 2010 and 85 million EUR in 2011. Moreover, additional sums (14 million EUR in 2010 and 26 million EUR in 2011) are reserved in favour of a series of measures focused on encouraging the training of workers.

With effect from 1 January 2010, VAT will be put back to 12% for meals in the catering sector. This fall is accompanied by an undertaking by the sector to increase the number of jobs and also by a series of

supervisory measures focused on combating black-market working and black-market income in the sector. The reduction in the VAT rate costs 255 million EUR per year.

In order to confront the difficulties currently faced by the agricultural sector, the government will grant a reduction in tax on certain bonuses awarded to the sector, which will have a financial impact of 20 million EUR per year.

When the multi-year budget for 2010-2011 was drafted, the government took account of the application of the Law of 23 December 2005 relating to the adaptation of social benefits to prosperity. The re-evaluations provided for in the allowance for 2009-2010 will reach their full effect in 2010 and increase purchasing power by some 500 million EUR. The projections for 2011 made provision for the resources necessary to pursue the application of the mechanisms set out in the law. Furthermore, an additional effort has been granted in order to support purchasing power : over 50 million EUR in 2010 and 85 million EUR in 2011. This involves, in particular, a new increase in minimum pensions for self-employed workers and measures to help the children of poor families.

The Finance Law, adopted on 23 December 2009 and published on 30 December in the official journal of laws (het Staatsblad/le Moniteur), already includes a large proportion of the measures announced in the context of the budget for 2010 with, in most cases, entry into force as from 1 January 2010. This applies to the contribution by sickness insurance to social security and the new special contribution to social security, the cost saving to be made on the administration costs of insurance bodies, the measures relating to the status of the self-employed, a variety of other measures for social security, the tax measures, the measures to support agriculture, the lowering of VAT in the catering sector, the measures relating to combating tax fraud, the measures focused on making the tax system greener and the contributions of both the financial sector and the nuclear energy sector.

Other measures have already been published but will enter into force at a later date. This applies to the measures relating to social fraud (1 April or later) and a variety of other measures for social security (1 April).

4.3. The main measures taken in the context of drafting the budget for the Regions and Communities for 2010

4.3.1. Flanders

In 2010, the main recurring cost saving consists in reducing expenditure for the employment measure referred to as "jobkorting", by 635 million EUR. Moreover, cost savings are being made on grants of 73.2 million EUR (44.6 million EUR on optional grants and 28.6 million EUR on regulated grants), whilst funding relating to communication and consultancy is being reduced by 8.5 million EUR.

Due to a more realistic evaluation of depreciation periods, expenditure to help Aquafin is being decreased by 59 million EUR. Further items recorded comprise isolated savings of the order of 54.6 million EUR (for example within the Fonds Hermès and the funding intended for the cabinets), 2.3 million EUR less of funding for the cost of ageing, 27 million EUR of final cost savings and, lastly, a product of 58.7 million EUR resulting from the delayed exceeding of the pivot index.

Furthermore, recurring measures have been taken, of 398.5 million EUR, which are being given concrete form by the departments and agencies in the budget for 2010, in particular: selective distribution of the provision index (100 million EUR), zero indexation on funding not linked to salaries (120.4 million EUR), additional efficiency gains on the apparatus (133.1 million EUR) and a variety of other measures (45 million EUR). Savings of a one-off nature represent 215 million EUR, made up of 95 million EUR resulting from utilising the reserves of VMSW and VWF, 125 million EUR stemming from the sale of plots of land belonging to VMM to Aquafin, 20 million EUR of additional resources for the MINA-fund and 20 million EUR less of expenditure at VFLD. Finally, an isolated negative saving in the education sector of the order of 45 million EUR is also being brought into the account owing to the alignment of savings with the academic years.

4.3.2. Walloon Region and French Community

Since being installed, the governments of the Walloon Region and the French Community have implemented a range of measures to control their expenditure and implement cost savings. Some of these measures were applied with effect from the budgetary adjustment carried out at the end of 2009, others during the preparation of the initial budget for 2010. Finally, a range of measures applies to the future undertakings made by the Region and/or the Community.

The main cost saving measures are as follows:

- A contribution by the Parliaments and Ministerial Cabinets, as well as a reduction in the number of ministers for these entities ;
- In the French Community, the freezing of allocations awarded to public interest and similar bodies until 2013 ;
- In the Walloon Region, the freezing of allocations awarded to public interest and similar bodies until 2015 ;
- The withdrawal of a range of new policies planned when the economic cycle was more favourable ;
- The reduction of funding for the civil service from 2010 (4% in the French Community and the Walloon Region) ;
- In the French Community, the freezing of non-organic and non-personnel funding with effect from the budgetary adjustment for 2009 and until 2012;
- In the Walloon Region, the non-indexation of all expenditure referred to as “primary expenditure” until 2015. Furthermore, this expenditure has been decreased by 2.5% (including a reduction of the order of 30% in the communication budget for the Region).

In the Walloon Region, the reserves of a variety of bodies are being mobilised on a multi-year basis in order to make a structural contribution to improving the financial situation of the entity.

Finally, the French Community had already undertaken a range of new expenditure for the next few years. These multi-year plans have been reviewed in order to reduce and/or spread the planned expenditure.

Similarly in the Walloon Region, certain redistributions have been provided for. Most of the measures decided by the governments of the Walloon Region and the French Community relate to structural cost

savings. The essential elements of these have already entered into force and will produce their effects over the whole of the period to which the present Stability Pact relates.

4.3.3. Brussels-Capital Region

The global economic crisis has greatly affected the public finances of the Brussels-Capital Region, both from the viewpoint of the fall in fiscal revenues and that of the upward pressure on some expenditure of a socially-oriented nature.

Thus, the Brussels Region has seen its revenues decrease by 15% in 2009 and 2010. In order to deal with this decrease, the Government has chosen to implement an effort of 240 million EUR for the year 2009 and close to 290 million EUR for the year 2010.

The budget for 2010 is motivated by 2 targets :

- To implement serious budgetary savings (on expenditure and revenues) so as not to compromise the future for the inhabitants of Brussels by making them foot the bill for the deficit ;
- To watch over the maintenance of essential policies for the inhabitants of Brussels.

This involves a transitional budget that puts back certain investments beyond the period of budgetary difficulties and anticipated refinancing of the Brussels-Capital Region.

The main efforts that have been implemented have been in mobility and at the level of infrastructure, whilst at the same time making sure that account is taken of the state of progress on projects: mobility (STIB: 22 million EUR deferred) and public works (road/rail/waterways and green spaces) and infrastructure (55 million EUR).

Substantial efforts have also been made in terms of operating costs, such as a decrease of 10% in the costs of Ministerial Cabinets (2 million EUR) and administration and similar items (25 million EUR).

Moreover, certain assets of GOMB/SDRB will be sold with a value of 19.5 million EUR.

The fiscal pressure on firms and households has not been increased; nonetheless, the revenues expected from registration fees are increasing via the deployment of restrictions on tax schemes focused on evading payment of these fees.

5 Medium-term strategy

The year 2009 represents an “annus horribilis”. Much like the rest of the EU, Belgium was plunged into the most severe financial and economic crisis since the Second World War. A unanimous and forceful intervention by the Belgian authorities proved necessary to stabilise the financial system and prevent an even deeper recession.

The government has therefore set out as a matter of priority to take measures focused on supporting the financial markets both via recapitalisations of the system’s institutions and by granting guarantees and supporting economic activity.

With the aim of supporting economic activity, stimulus plans have been undertaken at the various levels of government – in accordance with the European recommendations in this area. The stimulus plans are centred on the structural challenges posed by the economic climate and take account of the limited budgetary margin. They are tied to the competitiveness of firms and employment. At the same time, action has been taken to strengthen the long-term socio-economic levers and increase investment in a greener economy.

The financial crisis that has descended on the world’s economy constitutes an evident break with the past. In future, economic growth will have to be more balanced and more sustainable. This means taking account of the challenges of the future, which are in particular the ageing of the population, climate change and the intensification of globalisation. A modernisation of the labour market and a reform of pensions that take account in particular of the lengthening of life expectancy and that provide for closer interaction between the economy (employment) and the environment will be essential for increasing the growth potential of an economy greatly affected by the financial crisis. Better supervision and also better regulation of the financial sector are also essential with the aim of reducing the risk of future crises.

It is in this new context that the various governments have defined the various priority themes of their economic, budgetary, social and environmental policies, centred notably on a rise in the rate of potential growth in the economy and the employment rate, particularly amongst young people and the elderly. In this context, the EU2020 strategy will be a cornerstone of economic policies for the next few years.

The success of these policies will also depend on the degree of collaboration between various levels of government. It is in this spirit that a strengthening of the “co-operation model” with the federate entities

has developed. In the longer term, new undertakings and/or a new institutional framework allowing a more balanced distribution of financial charges, particularly in the context of the ageing of the population, and also a better matching of resources and competencies will have to be planned.

5.1. Labour market

In the context of the financial crisis, the government concentrated its efforts on limiting the rise in unemployment as far as possible and thus preventing a rise in structural unemployment in the next few years. Various measures have been taken in this context. Up to the present time, these measures seem to have shown some effectiveness, the rise in unemployment (from 7% in 2008 to 8.2% in 2009) in Belgium actually being more limited than in the euro area (from 7.5% to 10%).

Apart from these policies, more structural measures have also been taken with the aim of stimulating the employment rate and combating certain structural problems in the Belgian labour market, particularly in the areas of early retirement, reduction of labour charges and training.

5.1.1. Anti-crisis measures

The main measures comprise:

Temporary and collective reduction of working time

This measure provides for a lowering of social security contributions in the case of a temporary and collective reduction of working time. This decrease in social security contributions ranging between 600 and 750 EUR per half-year is increased by 400 EUR when the reduction in working time is accompanied by the introduction of a four-day week.

Reduction of work commitments and temporary suspension of employees' contracts of employment

If a firm fulfils certain criteria (fall in turnover, fall in production, etc.), it can take advantage of the crisis time credit system (individual and temporary reduction in work commitments) and/or temporary suspension of employees' contracts. The system for reducing commitments provides that, if an

agreement exists between the worker and the employer to reduce working time by 1/5 or 1/2 for a period of at least one month and at most 6 months, the worker will receive a payment of a gross amount of 442 EUR for half time and 188 EUR for 4/5 if the worker is under 50 years of age or 248 EUR if the worker is aged 50 or over.

With regard to the system for temporary suspension of employees' contracts, the worker will receive a benefit for this suspension of enforcement of the employment contract equal to 70 or 75% of his or her salary limit for contributions from NEO and a matching amount from the employer.

Restructuring reduction card

In order to facilitate a return to the labour market after a redundancy due to bankruptcy, closure or company liquidation, this measure provides that workers made redundant up to 30 June 2010 at the latest can take advantage of a restructuring reduction card. In the case of resuming work, these workers benefit from a lowering of personal contributions and the new employer benefits from a major reduction in employer's contributions. This type of measure also allows the barriers to employment to be reduced.

5.1.2. Recruitment plan

This involves a massive recruitment plan, centred as a priority on young jobseekers, elderly jobseekers and those who have been unemployed for a total of between 1 and 2 years, that is to say the most vulnerable groups during the crisis. The target is to drastically decrease the cost of employing them by activating their unemployment benefit. The activation of unemployment benefit is an employment subsidy through which jobseekers who obtain work can keep part of their unemployment benefit. Employers can deduct this sum from the net salary to be paid. This therefore involves an incentive for the recruitment of certain categories of unemployed and a drastic reduction in the cost of labour. A reduction ranging between 1,000 euro and 1,100 euro for a maximum of 24 months is therefore granted to the employer in the case of employing young people under 26 years old, elderly persons (+50 years old) and those who have been unemployed for a total of between 1 and 2 years.

5.1.3. Lowering of structural charges weighing on labour

The high cost of labour in Belgium is one of the Achilles heels of the labour market and more generally of the Belgian economy. Pursuing decreases in the charges weighing on labour, in particular for middle and low incomes, represents an essential theme of the federal government's socio-economic policy. Numerous measures have been taken recently with the aim of stimulating employment.

During the central agreement for 2009-2010 signed by the social partners, various measures were provided for which will play a full part in 2010. Thus, employers have been benefiting from a structural salary correction of 0.25% of employee withholding tax since 2007. This device has been strengthened by raising the exemption percentage to 0.75% in June 2009 and 1% as from January 2010. The budgetary impact amounts to 233 million EUR in 2009 and 590 million EUR in 2010.

With the same target of reducing the Belgian wage handicap, the government increased the payment exemption percentage for employee withholding tax for night work and shift work from 10.7% to 15.6% in June 2009. This reduction in charges represents 160 million EUR in 2009 and 311 million EUR in 2010.

In addition, the maximum number of overtime hours conferring the right to tax advantages has been increased, rising from 65 hours to 100 hours in 2009 and 130 hours in 2010. These tax incentives consist of an exemption for employee withholding tax for the employer and a reduction in tax for the worker. The budgetary cost of the measure amounts to 23 million EUR in 2009 and 45 million EUR in 2010.

The social partners also drew up a framework in order to simplify the system of charge reductions. Various "target groups" will thus be removed at the federal level and the reduction for low salaries will be further strengthened, since it is from this latter that the maximum effect on employment is expected. For its part, the Flemish authority has increased the bonus intended to encourage firms to employ workers aged 50 and over; due to this, the number of bonuses applied for has continued to grow, in 2009 also. More than 8,000 jobseekers over 50 years of age have found a job thanks to this bonus.

Moreover, the federal government is encouraging research and development activities by granting employers a reduction in earned income withholding tax on the pay of researchers. Following the harmonisation of the rates applicable to the various categories of researcher with the maximum rate of 65% in July 2008, this rate was raised to 75% in January 2009, in particular in order to prevent the crisis exerting a negative impact on the employment of researchers. The cost of this increase amounts to 85 million EUR.

5.1.4. Enhancement of employer's contributions on early retirement

The rate of employment amongst the elderly is particularly low in Belgium, notably owing to favourable early retirement systems. In the context of the budget for 2010, the financial consequences for the employer associated with admission to early retirement have been greatly reinforced by taking account of the age of the person at the time of early retirement.

At the current time, the cost of this is as follows: the flat-rate contribution by the employer is between 125 and 250 EUR/month and the contribution by the worker is 6.5% on the early retirement pension.

Table 18 contains the new system of increased employer's contributions that will apply with effect from April 2010 to early retirement in the profit sector.

Table 18 : Employer's contributions for early retirement (commercial sector)

Early retirement age	Employer's contribution private sector
52y and less	50%
53y and 54y	40%
55y, 56y and 57y	30%
58y and 59y	20%
60y and more	10%

The age of starting early retirement will therefore determine the amount of this contribution, which increases as the age decreases. This measure constitutes a major step towards reducing the favourable system of early retirement pensions. Other measures have been set out for firms undergoing restructuring and the non-profit sector.

5.1.5. Importance of training

Training plays an essential role in preserving employment and represents a major factor in integration, promotion, development and professional mobility. Furthermore, training contributes to increased added value and improving manufacturing processes. The emphasis is therefore placed on making a considerable investment in the training of workers and jobseekers, with an even greater effort for certain target groups. In the context of the budget for 2010, the government has assigned funds of 14 million EUR in 2010 and 26 million EUR in 2011 in order to finance new measures focused on developing the skills of workers and future workers.

5.2. An environment favouring the competitiveness of firms

The development of a fiscal and regulatory framework favourable to business activity is an essential priority. This type of regime contributes to stimulating employment, innovation and investment and consequently to energising the growth potential of the economy. Several provisions have already made the tax environment more attractive during the last few years, such as the deduction of notional interest and the deduction for patent income.

The government wishes to continue this improvement. The option of introducing a legal framework relating to the budgetary consolidation, in a neutral budgetary context, will be examined and new bilateral agreements will be signed to stimulate investment. Firms will also benefit from a renewed relaxation of their administrative charges, with a reduction in publication costs for electronic filing of documents, an extension of the functions of the Crossroads Bank for Enterprises (in particular for the professions) and a continued lowering of statistics charges. More recently, the decisions taken in the area of electronic billing – providing for freedom of choice in terms of sending, receipt and archiving - should also allow a reduction in firms' costs, but also the promotion of the environment. According to the Belgian Task Force for E-Invoicing, the cost saving that could be implemented by firms is valued at 3.5 billion EUR.

The efforts undertaken in the last few years by the public authorities in the area of reducing administrative charges seem to have borne ample fruit. Thus, according to a recent study by the Agency for Simplified Administration and the Federal Planning Bureau, firms now spend less on administrative charges, which have fallen from 3.5% of GDP (8.7 billion EUR) in 2000 to 1.7% in 2008 (5.9 billion EUR¹⁰).

Specific attention has been paid to small and medium-sized enterprises, with the adoption at federal level of an action plan for SMEs in October 2008. This plan includes about forty measures to promote the framework of activity amongst these firms, stimulate entrepreneurship and reduce administrative charges. These provisions are focused more specifically on encouraging the setting up and development of firms, strengthening the security of entrepreneurs and improving relations with the public authorities, the labour market and the social status of the self-employed.

Moreover, other initiatives have been taken to limit liquidity problems amongst firms and support certain sectors that are more sensitive to the business cycle, such as the building industry and the catering sector (the fall in VAT). Moreover, in order to support exports, the tax of 9.25% on credit insurance agreements covering commercial risks and country risks was removed in April 2009. An additional and temporary state guarantee (Belgacap) was also established in August 2009, extending to the end of 2010.

5.3. Rise in potential growth of the economy and industrial policy

Increasing the intensity of R&D in the Belgian economy is a priority for the various authorities in the country. More specifically, the policies put into effect are intended to increase the public funding allocated to R&D, stimulate private research by way of subsidies and tax policies, encourage knowledge transfer and exploit the results of research, mobilise human capital and reinforce the use of ICT by households and firms.

¹⁰ These figures originate from the survey carried out every two years by the Agency for Simplification of Administration (ASA) and the Federal Planning Bureau Plan amongst around 7,600 self-employed workers and firms.

The new regional governments have undertaken to adopt new measures to reach the standard of 3%¹¹. With regard to the federal government, the budgetary funding allocated to R&D should increase considerably between 2008 and 2009, rising from 463 million EUR to 514 million EUR.

Future-oriented industrial policy and the knowledge economy

Both in Flanders and Wallonia, the active policy in the area of clusters and centres of expertise plays a crucial role in industrial policy. In fact, bringing all the stakeholders together and creating networks makes for a strengthening of competitiveness.

In the three regions, the structural funds are concentrating on the main targets arising from the Lisbon strategy, specifically stimulating the knowledge economy and innovation, encouraging entrepreneurship, improving spatio-economic factors and promoting urban development.

In Flanders, several agreements entered into with centres of competence expired in 2008-2009. Subsequently, following evaluation of their operation, the modes of assistance have been renewed and frequently increased. On 15 May 2009, the Flemish government approved the financing of 2 new centres of competence: Flanders' Synergy and Flanders' Plastic Vision. At the centre of competence Flanders' Drive, the innovation centre for the motor vehicle industry in Flanders, a start was made in 2009 on gathering together all the scientific and industrial knowledge on "the vehicle of tomorrow", with the aim of developing scenarios for Flanders to follow so as to be able to play a role in the trend heading towards hybrid vehicles.

In the Wallonia Region, the cluster policy is focused on the development of (trans-)sectorial networks of enterprises. There are currently 14 recognised clusters in Wallonia (73% of their members are SMEs), including a new one since the beginning of this year (Plastiwin: innovations in plastics and elastomers), all of these clusters having developed from numerous inter-cluster and international partnerships.

With regard to the policy on centres of competitiveness, a fifth call for projects was launched in November 2008 intended for the 5 centres and 24 projects were adopted and labelled by the government in June 2009 (5 without conditions and 19 with conditions). With regard to the first 4 calls,

¹¹ The Flemish multi-year budget for 2006-2009 expires in 2009. This budget provided for a total net rise of 525 million EUR in public resources allocated to the science policy for this period. The additional resources were centred as a matter of priority on the following targets : strengthening of the research environment, of innovation via R&D projects within firms, of co-operation between firms and research centres and implementation of the Career Action Plan in research ('Actieplan Onderzoekslaan'). In the Walloon Region, apart from the resources devoted to research in the Priority Action Plan (i.e. 270 million EUR over the period 2006-2009), the ordinary budgets supporting research amount to 177 million EUR in 2009.

120 projects were supported with a public budget of 240 million EUR. Moreover, the Walloon Region took measures in 2009 with the aim of putting its industrial policy on a more sustainable track, by creating an 'interclusters' platform (TWEED, CAP 2020, Eco-construction, Val+) and by launching a technological innovation partnership in the field of construction for the long term. In the context of the Marshall Plan 2.Green, the government decided to launch a sixth centre dedicated to the new environmental technologies.

5.4. Social security

In addition to promoting employment and the competitiveness of the Belgian economy, another essential theme of the federal government's socio-economic policy is the development of a high-quality system of social protection. A regime of this type makes it possible to ensure well-being, prosperity and solidarity between citizens, as well as to combat poverty. In addition, this mechanism makes a contribution to supporting economic activity, by ensuring a decent income for households, in particular those on low incomes.

These targets seem all the more relevant in the present more difficult economic climate. Numerous measures have therefore been taken, depending on the available budgetary limits, to enhance a whole set of social benefits, including pensions. In addition, access to healthcare forms the subject of continuous improvement, whilst upholding the financial balance within social security.

5.4.1. Pensions

Pursuing the raising of pension levels is a major priority. Apart from the enhancements provided for by the prosperity items, other additional measures have been earmarked in favour of pensions, particularly the lowest.

Thus, within the system of salaried workers, pensions in payment for more than 15 years were increased by 2% and minimum pensions were increased by 3% in June 2009. Furthermore, the minimum entitlement per year of service has been raised by 3%. The other categories of pension also benefited from a rise of 1.5% in June 2009.

With regard to the self-employed, minimum pensions received a rise of 20 EUR per month in May 2009, in order to reduce the gap with respect to pensions of salaried workers. The amount of the minimum pension was also increased by 3% on 1 August 2009. Other pensions also received an increase of 1.5% on the same date. In 2010, the pensions of the self-employed will benefit from an additional rise of 20 EUR for a joint pension and 25 EUR for a single-life or surviving-dependant's pension in August 2010.

In total, the pensions of salaried workers have benefited from a rise of 657 million EUR, together with 329 million EUR for the self-employed over the period 2007-2010.

With the aim of consolidating the legal system for pensions, the government is providing for three major platforms. Thus, it is undertaking that it intends to:

- 1) Move into the framework of the national conference on pensions. The purpose of this conference is to reform and strengthen the Belgian pension system and to initiate a debate on the methods used to calculate pensions, on the constraints relating to setting up a pension linked to mobility between the various pension systems, on adaptation to new challenges such as the increase in life expectancy, but also the position of certain categories of worker such as part-time workers, contract workers in the civil service and certain categories of self-employed workers. The work of the pensions conference should culminate at the end of 2010 in concrete proposals for reform.
- 2) Reform the financing of local public pensions. A draft bill proposal will be made at the time of the budgetary control in March 2010. This reform of the system of local pensions will be detailed in the supplementary document which will be filed with the European Commission on 2 June 2010.
- 3) Develop the supplementary pensions of contract personnel working in the civil service.

5.4.2. Healthcare centred on controlling expenditure whilst improving the accessibility and quality of healthcare

Controlling the development of expenditure on healthcare is focused on providing a lasting guarantee of financial balance within social security and is furthermore associated with the target of strengthening the high-quality regime of social protection. The government wishes to make the healthcare sector into a sector that creates quality jobs with a high level of added value.

In 2010, in a difficult budgetary context, the government had the target of controlling expenditure on healthcare on the one hand whilst allowing the implementation of various priority themes on the other.

In terms of controlling expenditure, an overall margin of 650 million EUR was released within the budgetary target, one part of which was earmarked for reducing the deficit of the other branches of social security, thus contributing to stabilising the public finances of the public administrations, and another part for contributing to the Future Fund for Healthcare, intended to offset, with effect from 2012, the future medical costs involved with the ageing of the population.

With the aim of strengthening the quality of the sector, both in terms of employment and accessibility of healthcare, the government's new measures hinge on 6 major priorities:

- A plan to make the nursing profession more attractive;
- Development of accessibility of healthcare particularly in the field of drugs and medicines and with regard to admissions to hospital, in particular through the removal of room supplements in the case of two-bed rooms, and also by further measures for the benefit of the chronically ill and persons suffering from cancer;
- Honouring the undertakings made in the area of enhancing the fees of healthcare providers;
- Fairer financing of healthcare institutions;
- Greater accountability of the parties acting within the health sector;
- Creation of a system of liability for compensation for harm resulting from therapy.

With regard to releasing the margins needed to implement the new initiatives, it was also necessary to adopt various measures for controlling expenditure, allowing a real cost saving of 201.8 million EUR in 2010, including 60 million EUR for the pharmaceutical specialities sector and 100 million EUR in the sectors of clinical biology and medical imaging, following the Task Force created at the instigation of the government in 2009.

5.5. Reform of the financial architecture

In the light of the financial crisis, numerous failures to function have appeared both in terms of regulation and financial supervision. Taking account of the disastrous effects of the financial crisis not

only on activity but also on social cohesion and the public finances, the Belgian government has undertaken to reform the current model of supervision in Belgium.

Following in the footsteps of other countries, the Belgian government has opted for the “twin peak” model, which will radically transform the architecture of supervision. As from 2011, the National Bank of Belgium will be responsible for the prudential control of all financial institutions. Moreover, macro-prudential control will be further developed there, in line with the new responsibilities of the ECB in this respect.

For its part, the CBFA will be given new powers in the area of consumer protection and financial training.

Apart from these large-scale reforms, the government has equipped itself – in accordance with the recommendations of the IMF – with a new legal framework allowing it to intervene in the event of serious financial crisis jeopardising financial stability. This framework will then allow the government to carry out transfers, sales, or contributions to financial enterprises relating to the assets, liabilities or several branches of activity or of shares or holdings issued by the financial institutions in accordance with a voting right or not. Moreover, if the State wished to make use of the powers to instruct the transfer of assets or shares, it will have to apply to the court of first instance for the latter to verify the legality of the act of transfer on the one hand, and the fair nature of the compensation provided for on the other. In addition, it is envisaged from now on that sanctions can be taken in the case of dissemination of information or rumours likely to give erroneous or misleading indications about the position of a credit institution, insurance enterprise or liquidation body, of such a kind as to undermine its financial stability.

The government has also undertaken to further restrict variable payments in the financial sector. From now on, these will have to comply with strict criteria. In particular, they must be spread out over a time frame of 3 years, with the aim of preventing short-term behaviour which could harm financial stability from taking precedence over the long-term value of investments.

6. Sustainability of public finances in the long term

6.1. Introduction

Like most countries in Western Europe, Belgium is faced with major changes regarding the demographic structure of its population, notably owing to the fall in the fertility rate and the considerable increase in life expectancy. In the future, a smaller number of working persons will have to finance the pensions and other social benefits for a growing number of non-working persons. Between now and 2050, the number of persons receiving a pension will grow by 1.2 million units, whilst the group of persons of working age will only increase by 400,000 units. In 2050, there will only be two working persons for each person receiving a pension. The dependency ratio will in fact rise from 25.9% in 2007 to 45% in 2050.

In order to ensure that a sufficiently high level of collective prosperity is maintained over the medium term, a coherent strategy has been developed. Apart from a targeted budgetary approach, this includes major political, economic and social initiatives.

In the wake of the economic crisis, the policy conducted in 2009 and 2010 is centred primarily on the short-term issues. This does not take away the need to devote sufficient attention to the sustainability of public finances over the medium and long term. The procedure envisaged in the Law of 2001 which provides the guarantee of a continuous reduction in public debt and the creation of an Ageing Fund (Law of 5 September 2001) is the proof of this. This Law effectively stipulates that the Study Committee on Ageing must publish an annual estimate of the costs linked to ageing and that the government must set out its policy in this respect.

6.2. Budgetary consequences of ageing

The more recent report from the Study Committee on Ageing dates from June 2009.¹² According to the Study Committee's reference scenario, the overall budgetary cost of ageing would stand at 8.2% of GDP between 2008 and 2060. Total social expenditure would amount to 31.3% of GDP as against 23.2% in

¹² High Council of Finance, Study Committee on Ageing, Annual Report, June 2009.

2008. This involves a considerable increase compared to the previous report which set the growth in social expenditure between 2008 and 2050 at 6.3%. Several reasons can be put forward to explain this increase. A major reason is certainly the economic crisis, which not only gives rise to a fall in GDP figures (denominator effect) but also a rise in the unemployment figures, which explains why the achievement of the recommended level of structural unemployment is delayed. The impact of the crisis is estimated at 1.2% in terms of GDP.

Table 19: Budgetary consequences of ageing¹³

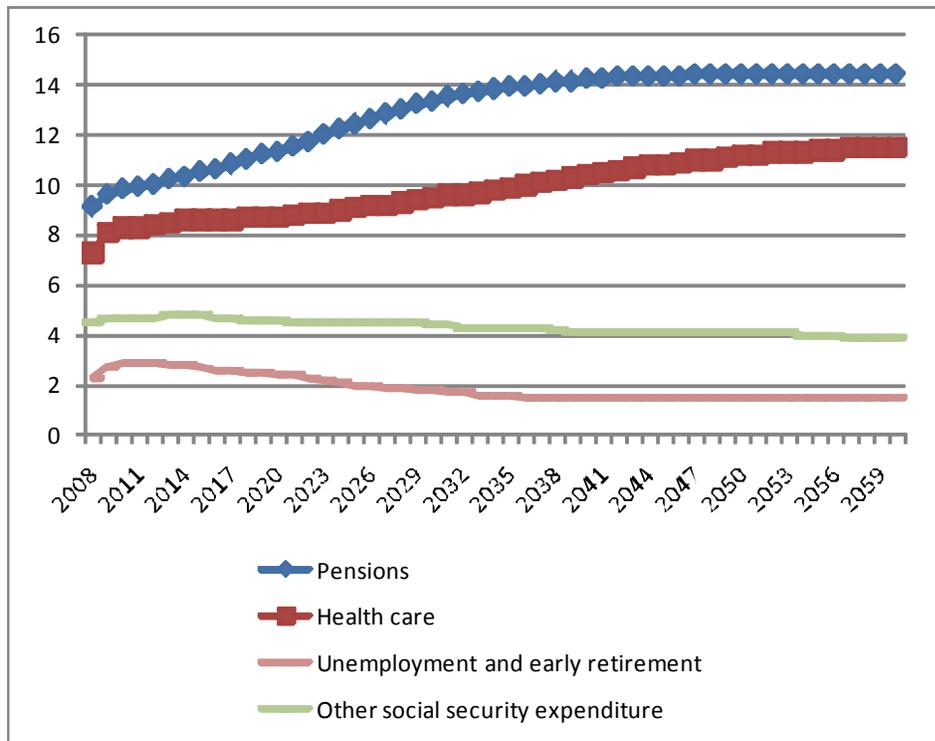
Components of the budgetary cost of ageing (% of GDP)	2008	2014	2030	2060	2008-2014	2014-2060	2008-2060
Pensions	9,1	10,3	13,3	14,4	1,2	4,1	5,3
Employees	5,0	5,7	7,5	8,2	0,7	2,4	3,2
Self-employed	0,7	0,8	0,9	0,9	0,1	0,1	0,1
Public sector	3,3	3,8	4,9	5,3	0,5	1,5	2,0
Health care	7,3	8,6	9,5	11,5	1,3	2,9	4,2
Acute	6,1	7,2	7,9	8,8	1,1	1,5	2,6
Long-term	1,2	1,4	1,6	2,8	0,2	1,4	1,6
Incapacity	1,3	1,5	1,4	1,3	0,1	-0,1	0,0
Unemployment	1,9	2,3	1,5	1,2	0,4	-1,1	-0,7
Early retirement	0,4	0,5	0,3	0,3	0,0	-0,1	-0,1
Family allowances	1,6	1,6	1,4	1,2	0,0	-0,4	-0,4
Other social security expenditure	1,6	1,7	1,6	1,4	0,1	-0,3	-0,2
Total	23,2	26,4	29,0	31,3	3,2	4,9	8,2
P.m. remuneration of teaching staff	3,9	4,0	3,9	3,8	0,1	-0,1	-0,1

A second factor explaining the increase in budgetary cost is the revision of the productivity scenario. The mean annual growth in activity has been revised from 1.75% in the previous reports to 1.5% currently. This revision stems from taking better account of the achievements of the last few years. The impact of this modification amounts to 0.9% of GDP. Added to this is a lengthening of the period of projection (up to 2060), which represents 0.3% of GDP. These three causes, taken as a whole, explain the increase in the budgetary cost compared to the previous estimate (+2.3%).

¹³ The figures of the Study Committee on Ageing only depart to a small degree from the most recent revision by the *Ageing Working Group*. See *The 2009 Ageing Report – Economic and Budgetary projections for the EU-27 Member States (2008-2060)*. The AWG evaluates the budgetary cost of pensions in 2060 at 14.7% of GDP, as against 14.4% in the estimate from the Study Committee. For healthcare, the second major element in the budgetary cost of population ageing, the differences between the estimates are even more insignificant : 8.8% of GDP for acute healthcare and 2.9% for chronic healthcare in the projection from the AWG as against 8.8% and 2.8% respectively in the projection from the Study Committee on Ageing.

In the relatively short term, between 2008 and 2014, the rise in social expenditure is expected to be 3.2% of GDP, or 2.1 percentage points more than the estimate in the previous annual report. In this case too, the economic crisis is the main cause (1.9 percentage points of additional expenditure).

Chart 4 : Development of social benefits (% GDP)



Source: Annual Report of the Study Committee on Ageing, June 2009

6.3. Strategy of the public authorities on ageing

For the Belgian public authorities, the ageing of the population represents one of the main challenges of the decades to come. In order to confront this challenge, a coherent strategy has been developed. This hinges on three basic policies:

1. On the budgetary level: pursuing the reduction of public debt and establishing the reserves necessary for the Ageing Fund;
2. On the economic level: raising the employment rate and stimulating economic activity;
3. On the social level: pursuing the development of a social security system characterised by strength and social solidarity.

The last two policy options were set out earlier in Chapter 4. The following statement is focused on budgetary policy.

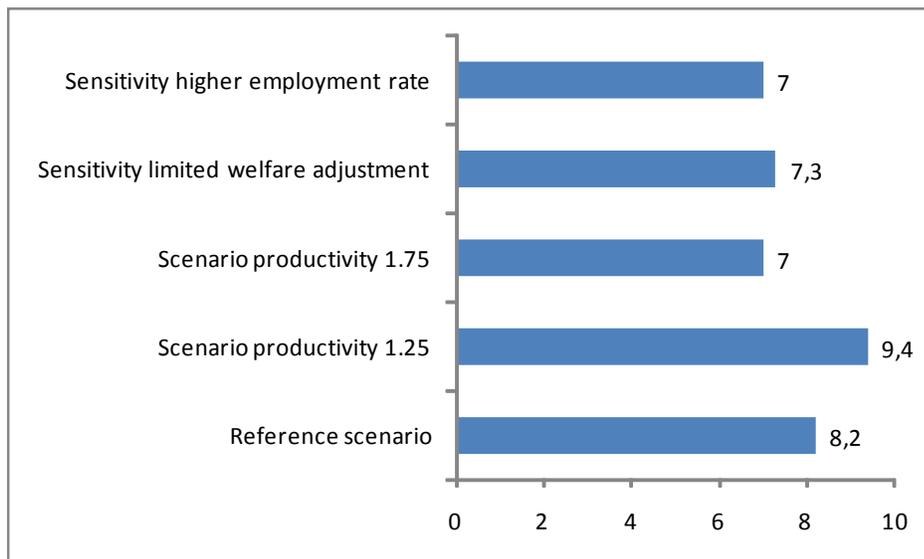
In this context and in view of the uncertainties, the Study Committee on Ageing (2009) carried out certain sensitivity analyses, specifically regarding variations in productivity on the one hand and regarding participation in the labour market on the other.

In a scenario of weaker gains in productivity (an annual average of 1.25% as from 2015), social expenditure weighs more heavily on a reduced economic foundation. Consequently, between 2008 and 2060, the budgetary cost of ageing is expected to be 1.3 percentage points greater compared to the reference scenario, representing an overall budgetary cost for ageing of 9.4% of GDP. The increase in expenditure as a percentage of GDP is found mainly in the pensions of salaried workers, in that these are calculated on a whole career and therefore only gradually undergo the effect of the fall in productivity gains. In contrast, for the scenario forecasting a higher productivity gain in the long term – notably following a rise in R&D efforts - specifically 1.75% (the old basic scenario), the budgetary cost of ageing would be 1.1 percentage points lower (7% of GDP), once again mainly influenced by the pensions of salaried workers.

Since the employment rate is still relatively low in Belgium and the strategy of the Belgian government is not only to reduce debt but also to raise the employment rate, the Study Committee on Ageing (2009) carried out an exercise starting with the basic scenario that the employment rate for persons over 55 years of age would be increased by 14 percentage points to reach the average in Scandinavia. This

obviously results in a lower rate of structural unemployment (-1.5 percentage points), higher GDP (+4.2% in 2060) and consequently a reduction in the budgetary cost of ageing: 7% of GDP between 2008 and 2060, or 1.2 percentage points less than in the reference scenario proposed previously. It should be noted that in order to implement this scenario, the employment rate for men aged over 55 would have to rise from 47% to 67% and that for women from 28% to 59% between 2008 and the middle of the 2030s.

Chart 5 : Sensitivity scenarios analysed by the Study Committee on Ageing



Source : Study Committee on Ageing (2009)

The strategy of the public authorities on budgetary policy is focused on ensuring the sustainability¹⁴ of public finances. Therefore one of the initial targets of budgetary policy consists in lowering the debt ratio in order to reduce future interest charges. The margin released in this way can then be used in particular to tackle growing expenditure in the area of social protection without having to cut other expenditure or increase revenues.

¹⁴ The Public Sector Borrowing Requirement Section has defined the notion of sustainability as follows: "Sustainability must be considered as a situation in which, at a more or less constant level of revenue, the public authorities manage to absorb the impact of demographics on part of their expenditure, without the share of other primary expenditure in GDP being reduced and without jeopardising the attainment of various public finance standards."

Owing mainly to the impact of the global financial crisis and the appalling economic situation, the government is departing in the short term from the recommended target. Simply maintaining the fixed budgetary targets would effectively mean that budgetary policy would have a contracting effect, which would only worsen the economic and budgetary situation.

With the particular aim of ensuring the long-term sustainability of public finances, the present stability programme proposes a path that allows a balance to be established between now and 2015. Based on this, an illustrative scenario was then prepared to allow a large part of the additional cost of ageing to be offset, over the period 2015-2050, by the reduction in the primary balance and to do so without a significant increase in the debt ratio. Chart 6 shows the main key elements in this scenario, which results in a slight surplus after 2015 which is steadily eroded from 2025 onwards. In the long term, limited deficits are generated without giving rise to an unsustainable process of rising debt.

Chart 6 : Public debt ratio, overall balance and long-term primary balance (expressed in % of GDP)

