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IMF Staff Country Report No. 00/31

Belgium: 1999 Article IV Consultation

The 1999 Article IV consultation with Belgium resulted in the release of the following documents, included in this package:

- the staff report for the 1999 Article IV Consultation;
- the supplement to the staff report; and
- the Public Information Notice, summarizing the Executive Board views of the Article IV Consultation Report.

The staff report was prepared by a staff team of the International Monetary Fund following discussions with the officials of Belgium on economic development and policies. The supplement to the staff report gives an update on fiscal developments and policies since the issuance of the staff report. The views expressed in these reports are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF and the authorities of Belgium.

These reports were considered by the IMF's Executive Board in the context of the IMF's periodic consultation with Belgium, as required under the Article IV of the IMF Articles of Agreement. The views of the Executive Board as expressed in the discussion of the Article IV Consultation staff reports are summarized in the Public Information Notice (PIN).

The policy of publication of Article IV staff reports and PINs allow for the deletion of market sensitive information.

Further background documentation prepared by IMF staff for the consultation may be published separately at a later date.

The Article IV staff report is published—both in hard copy and on the IMF's website (http://www.imf.org)–as part of a pilot project. To assist the IMF in evaluating the pilot project for release of Article IV staff reports, reader comments on the staff report are invited prior to October 5, 2000, and may be sent by e-mail to Pioltproject@imf.org.

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INTERNATIONAL MONETARY FUND

BELGIUM

Staff Report for the 1999 Article IV Consultation

Please note that since the main staff report was issued, additional information on economic and budgetary developments was received and staff projections were updated. This is reflected in a supplementary document entitled "Staff Report for the 1999 Article IV Consultation – Supplementary Information," which is also included in this publication.

INTERNATIONAL MONETARY FUND

BELGIUM

Staff Report for the 1999 Article IV Consultation

Prepared by the Staff Representatives for the 1999 Consultation with Belgium

Approved by C. M. Watson and G. Russell Kincaid

February 29, 2000

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I. Introduction

1. A staff team comprising Mr. Ford (head), Ms. Louppe, and Messrs. Martijn and Pani (EP) (all EU1), visited Brussels from November 12 to 22, 1999 for Article IV discussions. Messrs. Kiekens (Executive Director) and Josz (Assistant to the Executive Director) were also present at the meetings. The last consultation was concluded on February 12, 1999 (SUR/99/20). Directors commended the authorities on the impressive progress on macroeconomic reforms over the past decade. They stressed, however, that the debt burden needed to be cut decisively over the medium term. Directors urged the authorities to move ahead with sweeping structural reforms to foster job creation and reduce hard core unemployment, including a sizable reduction in taxes on labor, stronger incentives for the unemployed to enter work or training, more flexible wage formation, and improved product market functioning.

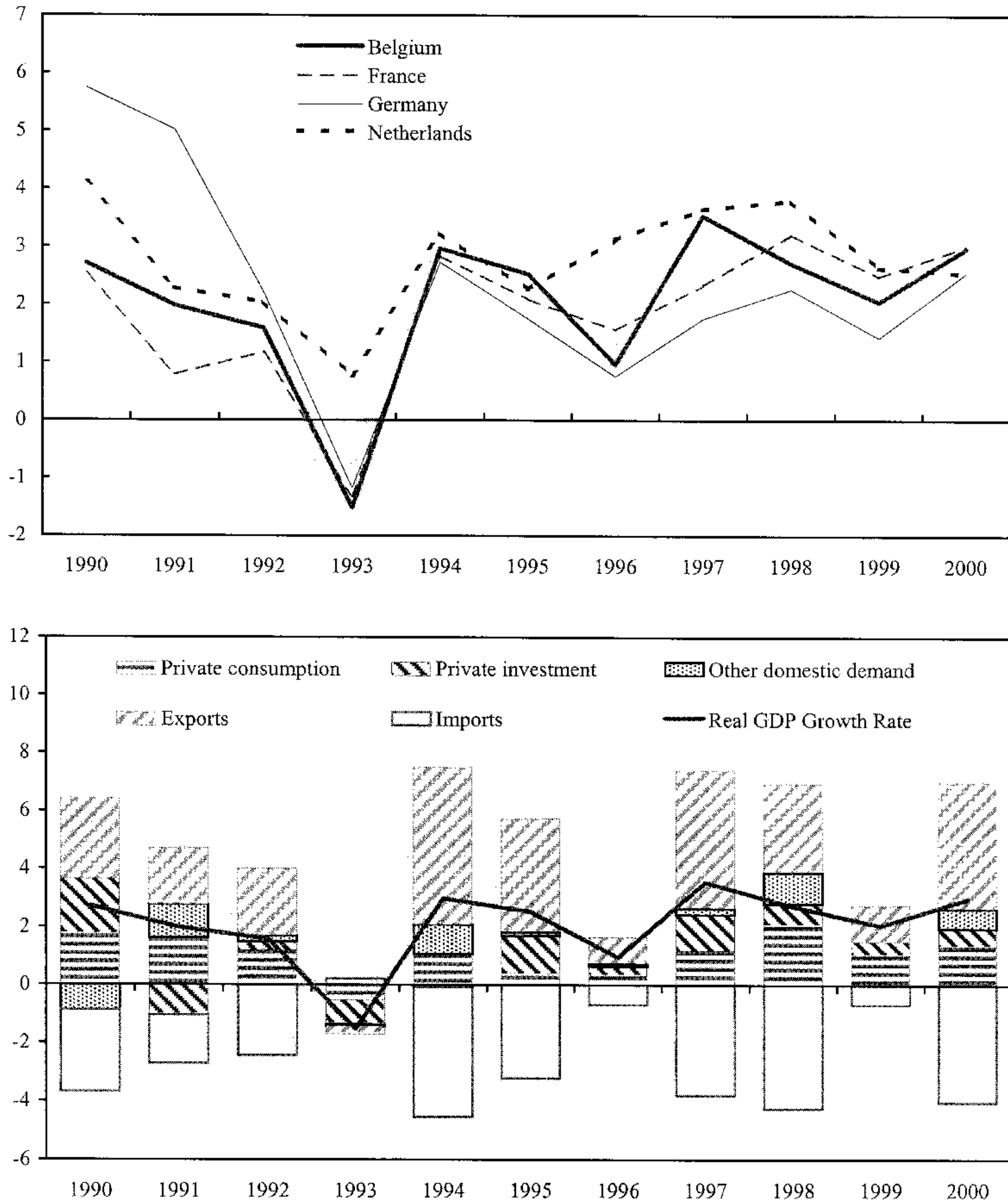
2. The Belgian authorities have notified the Managing Director of their intention to participate in the pilot project to publish Article IV Staff Reports. Belgium has accepted the obligations of Article VIII, Sections 2, 3, and 4 (see Appendix II).

II. Background to the Discussion

3. **After a contraction in late 1998, economic activity picked up in the course of 1999, despite the dioxin crisis of mid-year (Figure 1).** The decline in real GDP in the fourth quarter of 1998 was largely due to weak export markets in the wake of world financial turmoil. As these markets recovered, GDP growth resumed and business and consumer confidence improved. Household confidence and consumption slowed temporarily, but were sustained by continued gains in employment and declines in the unemployment rate. More broadly, monetary conditions—determined by the peg of the Belgian franc to the deutsche mark until the end of 1998 and by Euro-area monetary policy since—have been generally supportive of activity in Belgium (Figure 2). The adverse macroeconomic effects of the dioxin crisis of mid-1999, estimated by the Belgian authorities to have been about ¼ of 1 percent of GDP, also dissipated as exports and consumer confidence rebounded by the end of the summer.

4. **Despite some improvement, the situation in labor markets remains unsatisfactory, with a high unemployment rate and a very low participation rate.** Though the unemployment rate, on a harmonized basis, fell by ½ of 1 percentage point during 1999, at about 8¾ percent it is still high. Moreover, there are considerable regional disparities in labor-market performance, as unemployment has remained very high in much (but by no means all) of Wallonia, while shortages have emerged in most areas of Flanders (and some parts of Wallonia). Long-term unemployment remains stubbornly high (Figure 3). Both the employment rate and the participation rate are well below the EU average, a situation that is particularly marked for youth (to a large extent reflecting high educational enrollment) and

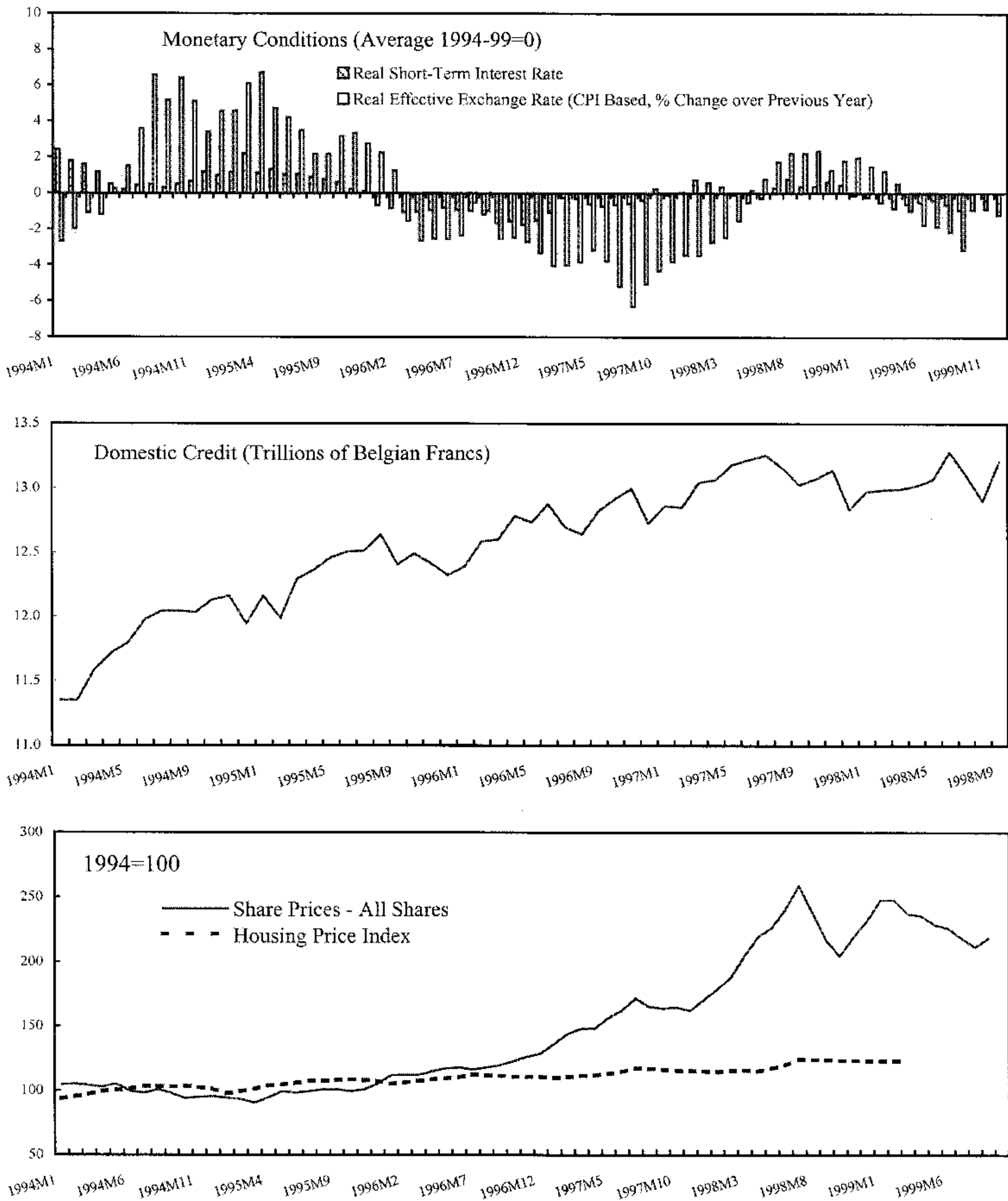
Figure 1. Belgium: Real GDP and Contribution to GDP Growth 1/



Source: IMF, World Economic Outlook; and data provided by the authorities.

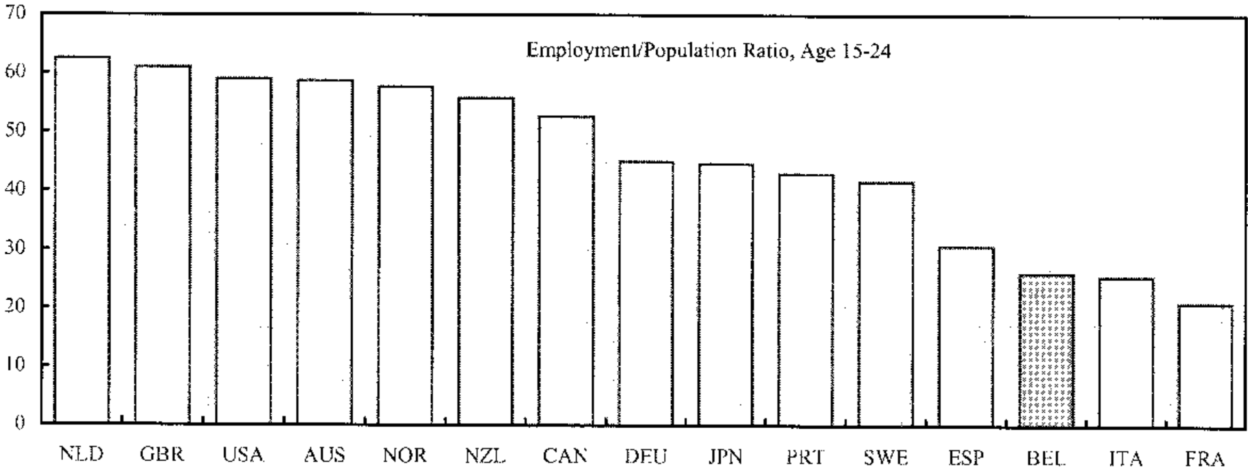
1/ On a SEC 95 basis for Belgium; data for 1999 and 2000 are staff projections.

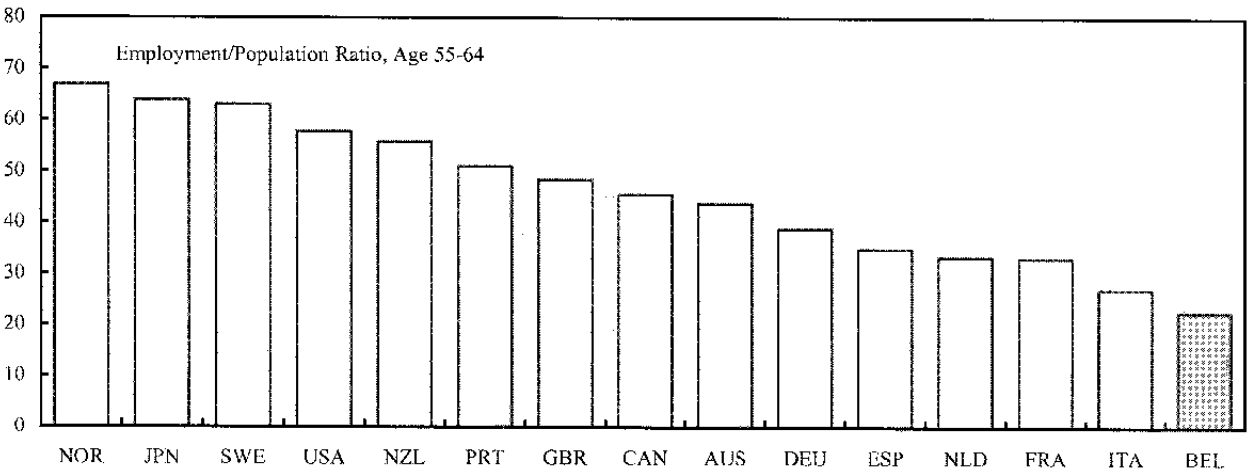
Figure 2. Belgium: Monetary and Financial Conditions

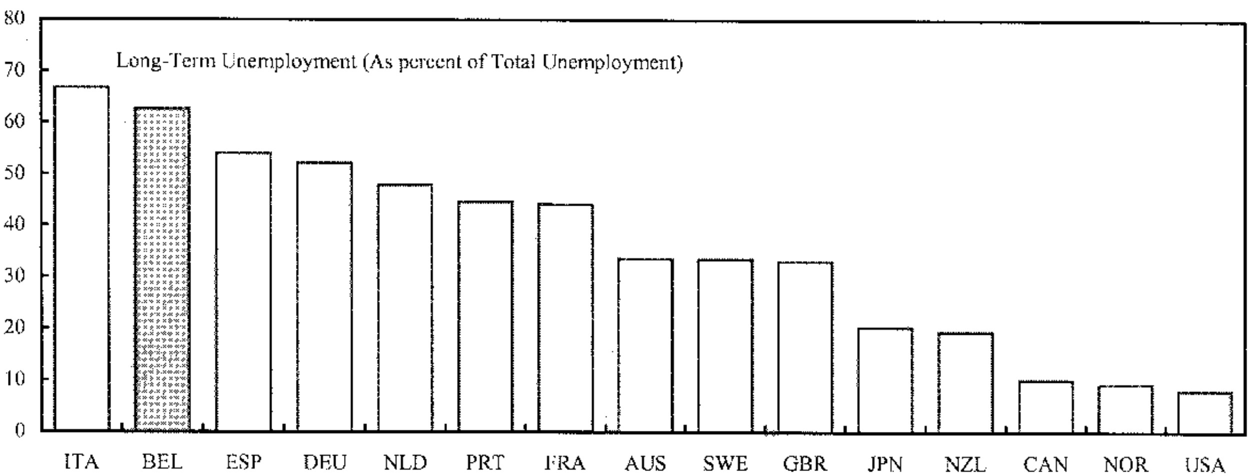


Sources: WEFA Intline Database; and IMF, International Financial Statistics.

Figure 3. Belgium: Labor Market Indicators in Selected Countries 1/







Source: OECD, Employment Outlook, June 1999.
1/ Data are for 1998.
Countries are: AUS=Australia, BEL=Belgium, CAN=Canada, FRA=France, DEU=Germany, ITA=Italy, JPN=Japan, NLD=Netherlands, NZL=New Zealand, NOR=Norway, PRT=Portugal, ESP=Spain, SWE=Sweden, GBR=United Kingdom, USA=United States.

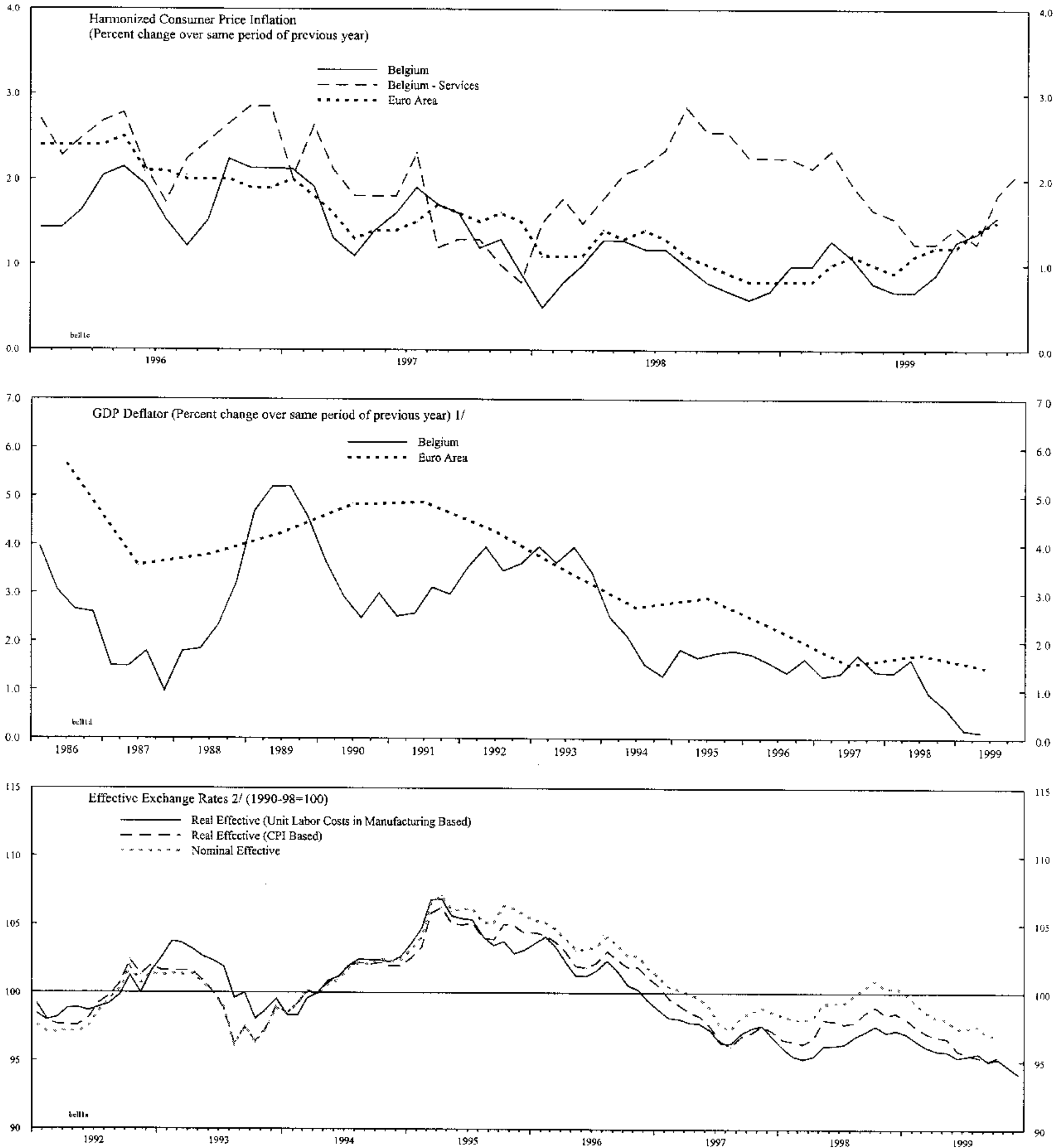
those above 50 years of age (who benefit from generous early retirement schemes). In contrast to unemployment, differences in employment rates are less marked between Flanders and Wallonia.

5. **At end-1999, there was still a margin of excess capacity in the country as a whole and, in the absence of generalized pressures in product and labor markets, inflation has tended to fall along with the Euro-area average.** Staff estimates the output gap to be about 1½ percent of potential GDP and the unemployment rate to be above the NAIRU, implying Belgium's cyclical position is close to that of the Euro-area average. Measured by the harmonized index of consumer prices (HICP), inflation rose slightly in 1999 due entirely to increases in energy prices but remains close to the Euro-area average (Figure 4). Non-traded goods price increases remained moderate, and compensation rose by 4 percent. Moderate inflation and a weaker nominal effective exchange rate improved Belgian competitiveness slightly, although buoyant import demand and a flagging world economy narrowed the current account surplus by almost 1 percentage point of GDP in 1998, to about 4¾ percent of GDP, where it remained through 1999.

6. **The fiscal situation improved markedly over the past decade, though both the debt ratio and the tax burden remain high.** The debt-GDP ratio peaked at 136 percent in 1993, but has since declined rapidly as the fiscal deficit was cut from 7.2 percent of GDP in 1993 to 0.9 percent in 1999 (Figure 5). Over half of this improvement was due to falling interest costs, though the reduction in the expenditure share accounted for about one-quarter of the overall narrowing of the deficit. Nevertheless, the debt ratio still amounted to 115 percent at end-1999, and at more than 46 percent the revenue ratio (including social security contributions) is one of the highest in the euro area (reflecting high interest costs). There was significant progress on the expenditure side, with the ratio of general government expenditure to GDP falling by about 5 percentage points over this period. The key to fiscal control has been the policy of enlarging the primary surplus and then, from about 1997, maintaining it at 6 percent of GDP or higher. Targeting the primary, as opposed to the overall, balance enhanced the consolidation effort, since during this period interest rates declined but primary outlays were not allowed to increase in consequence. The overriding need to reduce the deficit ruled out tax cuts. Both average and marginal tax wedges on labor are well above those in neighboring countries.[1] On the other hand, capital is relatively lightly taxed; the basic corporate tax rate

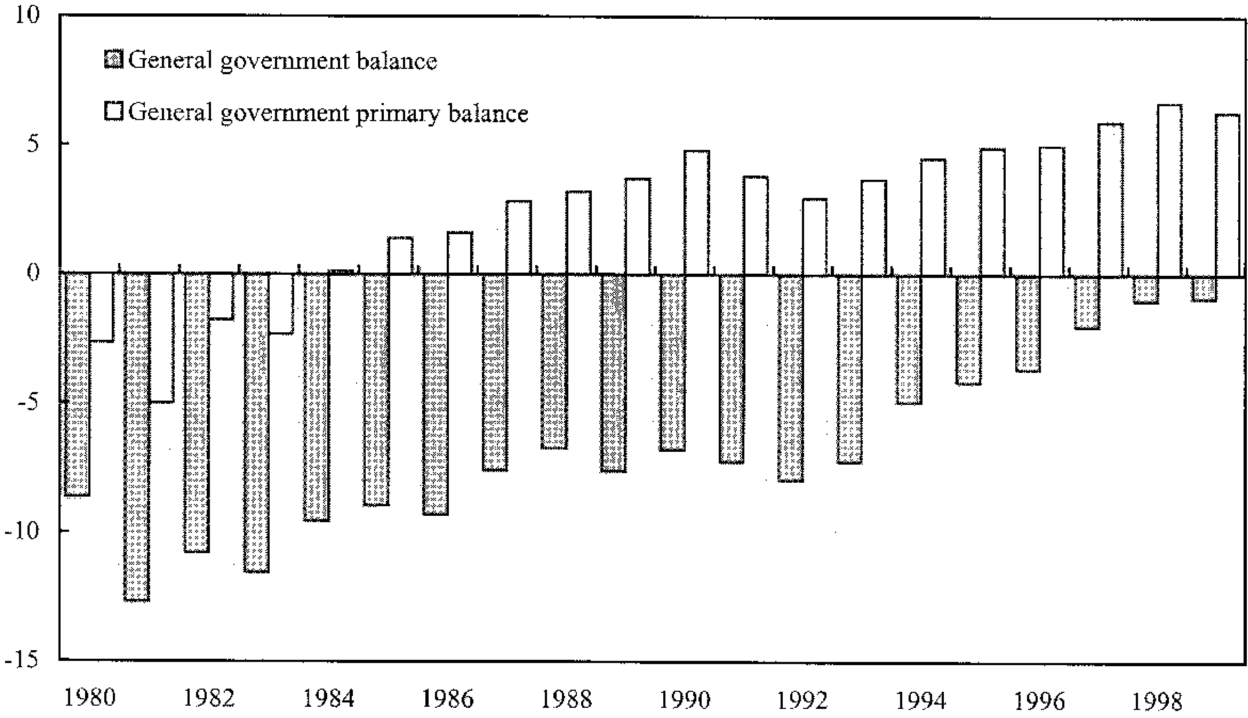
[1] For a single production worker, the average (marginal) tax wedge in 1996 was about 56 (67) percent in Belgium, compared to 51 (60) percent in Germany, 50 (55) percent in France, 44 (58) percent in the Netherlands, and 46 (55) percent in the EU as a whole (Federal Planning Bureau, website).

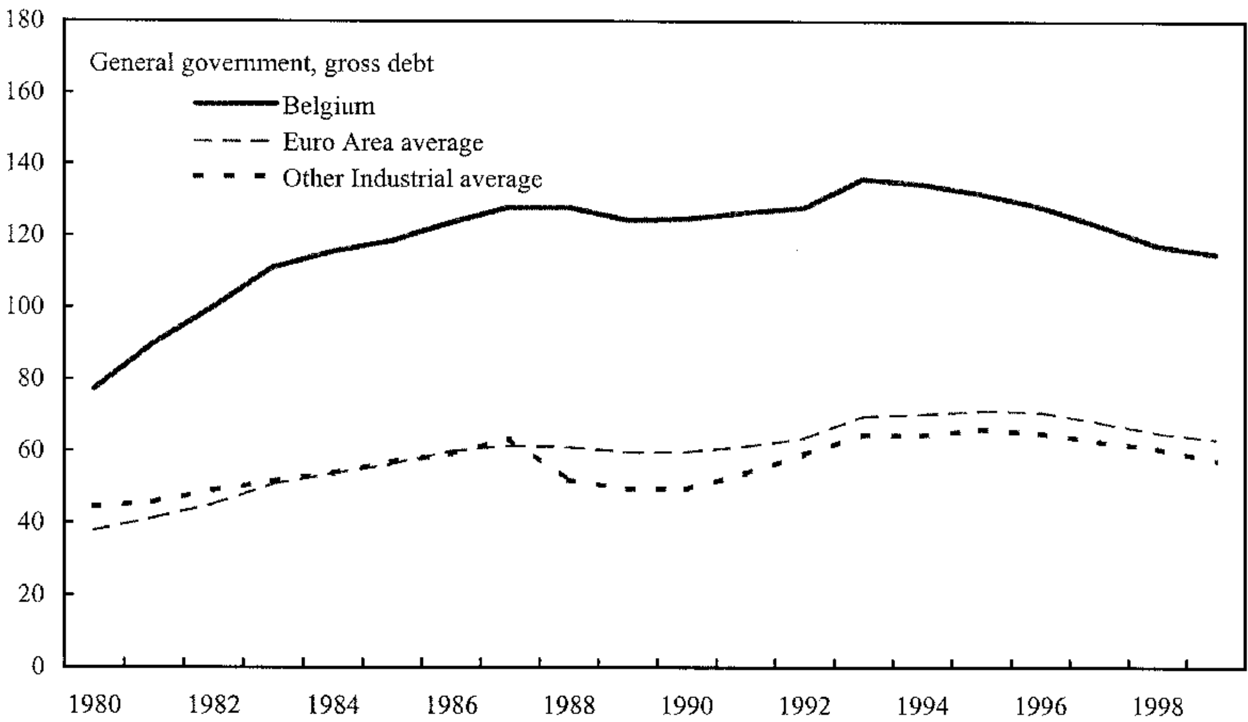
Figure 4. Belgium: Price Developments



Sources: IMF, International Financial Statistics; and Eurostat.
1/ On a SEC 95 basis.
2/ An increase indicates an appreciation.

Figure 5. Belgium: Fiscal Indicators
(In percent of GDP)





Source: IMF, WEO.

of 40 percent is broadly in line with other EU countries, but because of exemptions the effective rate is low.[2]

7. **An important aspect of fiscal policy in Belgium is its federal nature.** The regional and community governments have considerable fiscal autonomy, though key decisions are negotiated with the Federal government, and the High Council of Finance has successfully promoted cooperation among the three levels. In addition, the Federal level collects a substantial amount of taxes and is responsible for the social security system. As a result, there are significant interregional and inter-community transfers built into the fiscal system.[3] The process of fiscal federalization reached a way-point at the end of 1999, as the 10-year "transition regime" was replaced by the "definitive regime" (see Box 1). One consequence is that the growth of real budgetary means transferred from the federal government to the regional and, especially, the community levels is set to fall sharply—to approximately the growth of real output for the regions and to zero for the communities.[4] Taking account of municipalities, growth in non-federal, non-social security expenditures would be held to below 1½ percent a year in real terms, compared to 3.3 percent during the "transition regime." This will require substantial effort; the Francophone Community government has already received more money for education for 2000.

8. **The short-term economic prospects are improving, with real GDP projected by the staff to grow by 3 percent in 2000, but the risks seem mainly on the upside.**[5] This projected strength reflects three factors. First, macroeconomic policies are assumed to remain accommodative. The 2000 Budget is expansionary by ½ to ¾ of 1 percent of GDP (as measured by the change in the structural balance and the structural primary balance), and the actual budget deficit is projected to decline only slightly relative to GDP (Table 1). Monetary conditions are likely to remain supportive of further expansion. Second, the external situation is likely to continue to improve, particularly in view of the anticipated pickup of activity in Germany and France. And finally, consumption is likely to continue to be strong, as

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[2] For 1990–96, the effective corporate tax rate was 21 percent in Belgium, compared to 39 percent in Germany, 33 percent in France, 32 percent in the Netherlands, and 27 percent in the EU as a whole (MARC, *Corporate Effective Tax Rates in the European Union*, University of Maastricht, 1999).

[3] These have been estimated by the KBC Bank to have amounted to 2.2 percent of GDP in 1996.

[4] Community expenditures are dominated by education, the funding for which is adjusted for inflation and the number of school-aged children. Thus real budgetary resources for educational expenditure are not linked to real output or wage growth.

[5] The January Consensus Forecast is 2.9 percent for 2000 and 2.7 percent for 2001.

Box 1. Fiscal Decentralization

During the past twelve years there has been a substantial devolution of responsibilities from the central government to the regions and communities. There are three regions (Wallonia, Flanders, and Brussels) and three communities (French, Flemish, and German). The French and Flemish communities broadly correspond to the Walloon and Flanders regions, and the Flemish community and Flanders regional governments are merged (with joint competence being shared in the Brussels region).

The 1989 Special Law (amended in 1993) provided for a shift of resources towards the lower levels of government, with this shift phased in over a 10-year "transition" period. At the end of 1999, this "transition" regime gave way to the so-called "definitive" regime. The federal government remains responsible for nationwide functions, including the judiciary, defense and foreign policy. The regions are responsible for territorial planning, economic development, environmental protection, and other matters of regional interest. The communities are responsible for education and culture, and regions and communities are governed by their own parliaments and executives, and are not subordinate to the federal government. They also have financial autonomy, and can, within limits, raise their own taxes and issue debt.

Regions and communities are financed mainly through taxes collected at the central level and shared between various government entities in accordance with so-called "repartition keys". Shared taxes account for more than 80 percent of the revenue of the regions and communities. Each region and community receives a share of personal income taxes (IPP) that is proportional to the funds collected on its territory. There is, however, a correction for national solidarity, granting additional funds to the regions with lower tax receipts than average. Under the "definitive" regime, the regions' IPP share is to increase each year in line with real GDP and the CPI (with possibly some minor corrections until 2005). Communities also receive a share of the IPP, calculated on the same criterion, but their main revenue source is a share of the value-added tax (VAT), calculated on the basis of the number of school-aged children and linked to inflation.

Total expenditure of the regions and communities is set to grow much more slowly under the "definitive" regime than under the "transition" regime. During the 10-year "transition" regime, the real primary expenditure of these two entities combined grew by 3.6 percent a year on average. Under the "definitive" regime, the regions' revenue will grow broadly in line with potential GDP—slightly above 2 percent annually in real terms—and the communities' real revenue will remain approximately constant. This will only to a small extent be offset by the projected disappearance by 2010 of their current combined budget surplus. As a result, average real growth of primary spending by the regions and communities is likely to decline to about 1 percent a year.

Table 1. Belgium: Public Finances, 1993-2000

(In percent of GDP)

	1993	1994	1995	1996	1997	1998	1999 Est.	2000 Proj.
Revenue	45.4	45.7	45.4	46.0	46.3	46.4	46.3	45.4
Expenditure	52.6	50.6	49.6	49.7	48.3	47.5	47.1	46.2
Primary expenditure	41.7	41.1	40.5	40.9	40.4	39.8	40.0	39.4
Federal	14.1	13.8	13.2	13.2	13.1	12.7	12.8	12.5
Social security	19.3	18.8	18.8	19.1	18.5	18.3	18.2	18.0
Local government	5.3	5.4	5.2	5.2	5.2	5.2	5.3	5.2
Regions and communities	11.4	11.4	11.5	11.4	11.4	11.3	11.2	11.2
Intergovernment transfers	-8.4	-8.3	-8.1	-8.0	-7.7	-7.6	-7.5	-7.5
Interest payments	10.9	9.5	9.1	8.7	7.9	7.7	7.1	6.8
Balance	-7.2	-4.9	-4.2	-3.7	-2.0	-1.0	-0.9	-0.8
Federal	-5.8	-4.6	-3.8	-3.4	-2.7	-1.9	-1.8	-1.5
Social security	-0.5	0.5	0.0	-0.2	0.4	0.4	0.5	0.5
Local government	-0.1	0.1	0.4	0.3	0.3	0.2	-0.1	-0.1
Regions and communities	-0.8	-0.9	-0.7	-0.4	-0.1	0.2	0.5	0.3
Memorandum items:								
Primary balance	3.7	4.5	4.9	5.0	5.9	6.6	6.3	6.1
Structural balance	-5.3	-3.2	-2.8	-1.7	-0.8	-0.2	0.0	-0.4
Structural primary balance	5.7	6.3	6.3	7.1	7.1	7.5	7.1	6.4
Output gap	-3.8	-3.0	-2.5	-3.4	-2.1	-1.5	-1.5	-0.6
Debt	135.9	134.5	131.8	128.3	123.0	117.4	115.0	111.2
Net debt	126.7	126.2	125.3	122.4	118.0	112.3	...	...
				(Growth rate, in percent)				
Total expenditure	1.0	-1.0	0.5	1.1	0.8	0.9	1.4	0.7
Primary expenditure	1.6	1.6	0.9	2.0	2.3	1.2	2.6	1.1
Federal government	-1.4	0.2	-1.8	0.8	3.0	0.0	2.7	0.4
Social security	0.5	0.7	2.0	3.0	-0.1	1.7	2.0	0.9
Local government	5.8	5.3	-1.9	1.7	2.1	2.6	4.7	1.8
Regions and communities	2.6	3.6	2.9	0.2	3.7	1.8	1.5	1.8

Sources: Data provided by the authorities; and Fund staff projections.

employment growth and household confidence hold up. Given the degree of aggregate economic slack and the already negotiated wage settlement (a maximum cumulative increase in wage costs of 5.9 percent in 1999–2000) underlying inflation and labor cost growth are projected to remain moderate.

III. Policy Discussions

9. **Discussions focused on fiscal policy, especially in the medium term, and on the need for broader structural measures to improve economic performance.** There was broad agreement on the short-term outlook and that monetary conditions (set at the level of the euro area) should support Belgian economic growth without undue risk of inflationary pressures. The fiscal discussions revolved on the tradeoff between the two medium-term fiscal goals of further reducing the ratio of public debt to GDP and beginning to lower the tax burden. The mission emphasized expenditure control as the key to meeting both goals. Closely linked to these fiscal goals are labor-market structural reforms. Success in expanding employment would increase the tax base, allowing for lower tax rates; and lower rates would stimulate employment and economic activity. The authorities indicated that they are relying heavily on tax cuts to reduce labor-market inefficiencies and spur employment. Against the backdrop of an improving economic climate and the shadow of population aging, however, the staff argued that time was ripe for rapid and decisive implementation of a much broader and more comprehensive package of labor and product market reforms.

A. Fiscal Policy

10. **The 2000 Budget projected an overall deficit of 1 percent, though the outturn is likely to be lower (Box 2).** The Budget projections were predicated on deliberately conservative assumptions regarding GDP growth (2.5 percent in 2000) and interest rates.[6] Reflecting a higher growth projection, the staff expected the deficit to be about 0.8 percent of GDP. This outcome would imply a fiscal stimulus of about ½ to ¾ of 1 percentage point of GDP which, in the staff's view, was not needed to sustain the momentum of the economic recovery and represented a missed opportunity to reach budget balance as soon as possible. The high debt level and the prospective fiscal effects of population aging argue for a particularly strong and sustained fiscal consolidation program. The authorities pointed out that the primary surplus would remain above 6 percent of GDP, and that real general government primary expenditure growth is to be restricted to 1 percent in 2000. They had made a deliberate policy decision to significantly cut taxes now rather than accelerate deficit reduction. The tax cut was mainly in the form of employers' social security contributions, by

[6] The downgrading of Belgium's credit rating last year by one agency had no effect on debt sales or spreads over benchmark securities.

Box 2. The 2000 Budget

The 2000 budget contains cuts in revenue well in excess of those projected in the 1999-2002 Stability Program. The budget is based on 2.5 percent economic growth, and the government has announced that deficit reduction would be given priority in allocating windfalls from higher growth. On staff estimates, with GDP growth at 3.0 percent, reductions in taxes and social security contributions would amount to 0.9 percent of GDP, while real primary expenditure would increase by 1.1 percent (compared to 1.6 percent in the Stability Program). The effect of these measures would be to reduce the primary surplus by 0.2 of 1 percentage point relative to 1999, to 6.1 percent of GDP, and the overall deficit by 0.1 of 1 percentage point.

At the central government level (comprising the Federal Government and the social security system, responsible for 22 percent and 46 percent, respectively, of total primary expenditure), budgeted primary expenditure will increase by 0.7 percent. With total primary expenditure at BEF 2585 billion (about 27 percent of GDP), the main spending measures at this level are:

- Additional investment in railway infrastructure (BEF 8.5 billion);
- An increase in the real growth norm of social security spending on health care from 1.5 percent to 2.5 percent (BEF 5 billion), and higher coverage for chronically ill patients (BEF 1 billion);
- An increase in the lower pensions as of July 2000 (BEF 0.9 billion);
- Additional development assistance, including debt reduction (BEF 2.5 billion).

Several measures will reduce revenue, mainly through lower social security charges:

- Reduced social security contributions for employers (about BEF 40 billion) starting in April 2000—the design of which will be specified in consultation with unions and employers organizations;
- Lower social security contributions for firms that create jobs for those leaving the education system—a program that will be broadened to jobs for all unemployed up to 25 years of age (BEF 4 billion);
- A targeted employment subsidy for nonprofit organizations, through lower social security contributions (BEF 2.5 billion);
- A reduction of the poverty trap through targeted reductions in workers' taxes and social security contributions (BEF 6.7 billion);
- A lowering of the VAT rate on home improvement and small repairs of shoes, clothing, and bicycles from 21 percent to 6 percent;
- The 1999 restoration of the indexation of income tax brackets to inflation was continued (BEF 8.5 billion) and a first step was made to eliminate the crisis surcharge on income taxes (BEF 2 billion);
- Higher tax deductions for childcare.

some BEF 50 billion, or ½ of 1 percentage point of GDP.[7] In their view, this would raise employment and the tax base, allowing further tax rate cuts in the future. The mission expressed reservations regarding the likely size of the employment effect in the short term and in the absence of more comprehensive structural reforms, a point taken up later.

11. **The authorities' commitment to the fiscal goals of the 1999–2002 Stability Program—in particular budget balance by 2002—remain attainable.** The Stability Program assumed real GDP growth of 2.3 percent a year on average, and implied a growth rate of real expenditures of 1.6 percent a year on average. Operationally, the program hinges on stabilizing the general government primary surplus at about 6 percent of GDP.[8] The staff and the authorities concurred that budget balance in 2002 would be well within reach, despite the lack of progress on deficit reduction planned for 2000. However, the staff emphasized that expenditure growth would have to be restrained and, in line with the authorities' intentions, any budgetary windfalls (from higher growth or lower interest rates than expected) devoted to deficit reduction. Indeed, given these provisos, the authorities and the mission agreed that room for further cuts in taxes or social security contributions seem feasible in 2002.

12. **There was agreement that, over the medium term, control of expenditures would be the key to further reductions in the debt ratio and cuts in the tax burden.** To this end, the mission recommended, as it did the year before, that real primary general government spending growth be held to 1½ percent a year over the medium term. The authorities were fully aware of the need for overall expenditure restraint, though they also pointed to areas in which there were increasingly urgent needs, notably infrastructure, health care, and the police and judiciary. In view of the likely difficulties of controlling spending, the mission suggested that an explicit expenditure framework be developed, along the general lines of those in Finland, the Netherlands, and the United Kingdom (Appendix IV). The authorities stated that there were no plans along these lines.

13. **Beyond 2002, and given the spending path, there is an issue as to the relative weight to be given to early cuts in taxes (including social security contributions) versus more rapid reduction in the debt-GDP ratio, which would reduce vulnerability to**

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[7] Employers' social security contributions are to be reduced by on average BEF 32,000 per employee per year, beginning in the second quarter of 2000. This would amount to about one-third of the social security contribution paid for a worker earning the minimum wage.

[8] In detail, the federal government primary surplus (including social security) was to remain at 5.3 percent of GDP, with lower levels of government having a primary surplus of 0.7 percent of GDP and an overall balance.

higher interest rates and ultimately permit higher sustainable primary spending.[9] The difference between the mission and the authorities was one of emphasis: whether to accelerate debt reduction somewhat, or to cut taxes earlier. The mission argued for maintaining the 6 percent primary surplus somewhat beyond 2002, until a small overall surplus was achieved, and then to maintain that overall surplus. This policy would help cement the government's reputation for fiscal prudence, particularly in an environment where fundamental structural reforms might not be implemented and, in any case, are unlikely to bear fruit in the short term. It would also be compatible with the Stability and Growth Pact, with a needed cushion to account for Belgium's poor public debt position. In particular, the large public debt implies that Belgium's fiscal position would deteriorate particularly sharply in the event that interest rates rise, as might occur as the Euro-area recovery matures (see Appendix V). Hastening debt reduction would allow for somewhat greater tax cuts in the longer run and help to prepare for the fiscal impact of population aging. Finally, by 2002 the Belgian economy is likely to be at or above capacity, and budget balance at that time would therefore be the minimum acceptable medium-term position. The authorities argued that a balanced-budget target would be more credible, in part because it would be easier than a surplus for the public to understand. Most importantly, in their view, it would allow somewhat larger tax cuts in the first half of the decade, which would help to boost employment, output, and the tax base.

14. **The substantial "gray economy" has eroded the tax base, and distorted economic activity.** The size of the gray economy (that is, economic activity that escapes taxation but is otherwise legal) and its fiscal effects are, by nature, difficult to estimate (Box 3). But there was agreement that it is substantial and results in a significant loss of revenue. Taxes have been reduced in some particularly affected sectors, such as home repair, and other schemes had been introduced to bring unrecorded activity into the open. The mission pointed out that selective tax measures themselves undermined the tax base and perpetuated economic distortions, and it would be necessary to consider reducing the overall tax burden, shifting the composition of taxes to those less easily avoided, and strengthening enforcement. The authorities agreed, but argued that selective tax cuts were nevertheless useful because bringing workers into the recorded economy would increase their access to social benefits and to protections such as work safety regulations.

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[9] Staff simulations illustrating this issue are presented in Appendix V. They show that, compared with budget balance, a small general government surplus from 2002 to 2015 implies a slightly higher revenue burden in the early years, and a slightly lower one subsequently (but a substantially lower debt-GDP ratio). The simulations also show that slippage on expenditure control would result in higher taxes in the medium term and, conversely, progress in labor and product market reform would allow a more rapid reduction in the tax burden.

Box 3. Belgium's Gray Economy[1/]

The gray (or underground) economy comprises economic activities that are legal but not declared to the authorities, typically to escape taxes and social contributions, and to circumvent regulations. In Belgium, the gray economy is large and raises particular concern because it undermines the fiscal position. The gray economy has been estimated to range between 12 percent and 22 percent of official GDP.

The size of the gray economy is linked to low recorded employment rates, the high tax wedge, and a minimum wage that prices low-skilled workers out of the recorded economy. It is also associated with small firms in the services and construction sectors. Clearly, estimating the factors affecting the gray economy, and even its size, is subject to wide margins of error. By definition, direct evidence is unavailable.

The most widely used method of estimating the size of the gray economy is the currency-demand approach. This approach is based on the consideration that gray economic activity is essentially run on a cash basis. Regressions estimates of the sensitivity of currency use to the tax rate are used to compute money demand in the absence of taxes, on the assumptions that in this case there would be no underground economic activity. The difference between actual currency demand and that in the absence of taxes (and underground activity) is multiplied by money velocity to estimate the size of the underground sector. Although this approach is obviously based on strong assumptions and involves large margins of errors, it is widely used due to its low data requirements. For Belgium, academic studies based on this approach assess the size of the gray economy at between 11 percent and 18 percent of official GDP.

New estimates by the staff on the underground economy in Belgium, using the currency-demand approach but dealing explicitly with the nonstationarity of the variables, are reported in the Selected Issues paper. As in other studies, the estimates show a slight increase in the size of the informal economy during the 1970s, followed by a substantial decline after 1980, which may be attributed at least in part to reductions in the tax pressure by two or three percentage points. By the mid-1990s, the grey economy is estimated to have been about 13 percent of recorded GDP.

[1/] This box summarizes the Selected Issues paper of the same name.

15. **The challenges of population aging may require reforms to existing pension systems and the enlargement of private pension arrangements, in addition to continuing fiscal consolidation.** Public pensions—comprising part of the social security system and a separate system for public-sector employees—will likely come under pressure by 2010. The authorities argued that the overall sustainability of the pension systems would be assured by their policies to increase employment, together with declines in interest payments.[10] The staff suggested that efforts should nevertheless be made to develop a larger private pension system, although at this point, the scope for building up significant funds before population aging begins would be limited.[11] In this regard, the authorities argued that social security system pensions were indexed to prices, though with additional discretionary adjustments from time to time. The consequent decline relative to wages over time would provide an incentive for private supplementary pension arrangements. In addition, employers' pension contributions are to be removed from the ceiling for wage increases under the Competitiveness Law (which governs collective bargaining).[12] As a result, there would be room for negotiating private pension arrangements between the social partners. Pensions for public-sector employees, by contrast, are indexed to wages, which the mission argued would prove to be excessively costly. The authorities envisaged no change to this arrangement, pointing to a tacit understanding that generous retirement provisions are compensation for relatively modest civil service salaries.

B. Structural Reform

16. **Resolving the key structural problem of poor labor market performance will be crucial to several policy areas.** Raising employment on a durable basis would help to

[10] According to 1997 projections made by the Federal Planning Bureau, the public pension system would be sustainable with only a 1.5 percentage point increase in the share of social expenditure in GDP by 2030 in spite of population aging. These projections assume a drop in the ratio of average pensions to average wages from 32 percent to 29 percent and an increase in the employment ratio of 7 percentage points. A recent study by the central bank, using less optimistic assumptions, projected a 4.5 percentage point increase in the share of social expenditures.

[11] Total (private plus public) pension funds assets amount to only about 10 percent of GDP in Belgium, compared with 86 percent in the United Kingdom and 141 percent in the Netherlands.

[12] The Competitiveness Law caps the increase in total labor costs (including employers' social security contributions), based on the evolution of labor costs in Germany, France, and the Netherlands. Subject to this cap, negotiations are carried out at the central, sectoral, and enterprise level. There is a mechanism for assessing ex post whether labor costs have stayed under the cap, and incorporating any differences in the subsequent round of negotiations.

resolve problems associated with poverty, marginalization, and exclusion. From a fiscal perspective, it would both increase the tax base and ease pressures on social spending, particularly on unemployment benefits, early retirement schemes, and welfare. Moreover, as the authorities have stressed, a significantly higher employment rate will be necessary if the current old-age pension systems are to be sustainable as the population ages.

17. **The staff supported the authorities' strategy of cutting the tax wedge, but argued that a broader set of initiatives would be required if it is to be fully effective.** The tax cuts (including cuts to social security contributions) introduced by the previous government, as well as those in the 2000 Budget, were designed to increase labor demand by lowering total labor costs. However, with labor markets tightening in much of the country, increased labor demand may not translate into sustainably higher employment, but instead increase wage pressures.

18. **Specifically, the mission argued that an important part of the problems in the labor market is due to inadequate support for finding work and blunted incentives to take a job, and suggested a range of policies to increase labor supply.** The scope for such reform—without undermining the traditional social protection—is substantial, as suggested by the examples of Denmark and the Netherlands (Box 4). Needed reform includes enhancing active labor market policies, such as training and the functioning of the public employment services. Reforms are also needed to benefit programs, including increased enforcement of obligations to seek work. Particularly controversial was the mission's suggestion to limit the duration of unemployment benefits (which are now unlimited) to help reduce long-term unemployment.[13] The staff also suggested that the special unemployment insurance regime for older people, which exempts those over 50 from seeking re-employment, be abolished and early retirement schemes be phased out. Such measures would help to boost labor force participation of that group, but more importantly would help to ensure that the incentives facing the next generation do not again result in the experience of premature withdrawal from the labor force.

19. **The authorities favored in principle a comprehensive approach, but they anticipated only a gradual pace of reform.** Regarding benefit programs, the authorities expressed concern that limiting access would lead to unacceptable increases in poverty and exclusion, and stated that they had no plans in this direction. However, they pointed to a number of initiatives to encourage labor supply, including: provisions in the 2000 Budget to reduce unemployment traps; increases in the early retirement age; an extension of the "young employment" program, which is designed to give recent school graduates work experience; and more rapid transformation of benefits into employment subsidies, including for private

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[13] Unemployment insurance is limited in duration in both Denmark and the Netherlands, but the replacement rates are higher than in Belgium.

Box 4. Labor Market Reforms in Denmark and the Netherlands

Supply-side labor market reforms in Denmark and the Netherlands have been instrumental in lowering unemployment, thereby contributing to higher growth and improving public finances.

In Denmark, emphasis has been put on strengthening incentives to work and enhancing employability. The maximum duration of the unemployment benefit was set at 7 years in 1994 and reduced to 5 years in 1996 and 4 years in 1999. The employment requirement for benefit entitlement was doubled in 1997 to 12 months. Supervision of availability was strengthened, and sanctions were progressively tightened in case of refusal to participate in active employment schemes; the jobless must now accept jobs outside their occupational area after three months of receiving benefits. The full and part-time early retirement schemes were merged, in order to make the system more transparent and efficient. Tax and benefit incentives were given to extend full-time work until age 62, including larger earned income tax credit, and a change in the payment schedule of early-retirement benefits. Furthermore, income incentives were enhanced for early retirees who want to work.

In the Netherlands, sustained labor cost moderation since the early 1980s has been complemented by social security reforms to strengthen labor supply. Maximum unemployment and disability benefits were reduced from 80 percent to 70 percent of the last-earned wage in 1986, and subsequently benefit eligibility and duration were tightened in several steps. Furthermore, to limit the inflow into the benefits system, the responsibility for sick leave benefits has been shifted to employers (1996), experience rating by firm has been introduced for disability insurance contributions (1998), and part of unemployment insurance contributions have been differentiated by sector (1998). Since the mid-1990s, a series of reforms has been launched to shift away from a system managed by the social partners to one managed by the government and then to decentralize and enhance competition among benefit providers. Finally, to reduce the poverty trap, a small earned-income tax credit will be introduced by 2001.

sector jobs. The issue of coordination of public employment services (PES), which may be a factor in limiting mobility because services in one region tend not to press job seekers to take employment in other regions, was widely recognized, though no concrete steps to correct the situation were envisaged.

20. **Regional disparities in labor market performance remain a serious problem.** The high unemployment rate in much (but by no means all) of Wallonia has proved resistant to the current economic upswing. Although the historical origins of such disparities are well known, the factors perpetuating them remain in some dispute. There are no significant differences in labor-market policies that might account for them. Thus, it might be expected that labor mobility would tend to narrow the differences over time. Though there are obvious linguistic barriers to interregional mobility, these do not explain the significant intra-regional disparities. Mobility may be reduced by the very high tax (registration fee) on house purchases and by inadequate inter-city public transport. The mission argued that at least part of the explanation lay in the more generalized problem of inadequate incentives to take a job, and in the lack of coordination among the PES.

21. **The mission argued that greater wage dispersion also would ease interregional labor market imbalances, as well as helping to increase employment among the low skilled.** The authorities agreed that, in principle, more wage dispersion would be desirable for these reasons, but argued that the centralized bargaining system among social partners was necessary to ensure moderate labor cost growth. There has been a degree of flexibility at the sectoral and enterprise level, within the framework of the centralized agreement, and some felt that negotiations at the enterprise level appear to have become more prevalent. However, as the 1998 bargaining round (for wages in 1999–2000) was the second under the new Competitiveness Law, the extent to which such negotiations will lead to greater wage differentiation was still unclear.

22. **Progress in product market reform has been limited**. The mission argued that competition in services needed to be improved through a reform of entry conditions, zoning laws, licensing procedures, and opening hours. The authorities noted that liberalization of network industries was keeping pace with EU requirements; the telecommunications market would soon be open to a third competitor, and electricity deregulation was underway along with the establishment of a new regulatory body meant to ensure access to the network. The new government has announced partial asset sales in telecommunications (Belgacom), transportation (Sabena), and banking (Dexia). Greater resources have been provided to the competition authority, and the authorities have also established a commissioner and an agency to address the issue of the administrative burden of the public sector, although concrete results are not expected for some time.

23. **Belgium's financial sector has undergone a sweeping transformation since 1996, spurred by European integration and the advent of EMU, with major banks now partly or wholly foreign-owned.** The authorities reported that the industry was in a "digestion" period, during which the costs of the acquisitions needed to be absorbed and little further

acquisition activity is anticipated. Nevertheless, they reported no vulnerabilities that might affect the system, and noted that profitability had been sustained in 1999 by buoyant market conditions. The wave of consolidation did not seem to have reduced competition; indeed, margins appeared to be quite low as institutions attempt to increase market share. Moreover, the European single market and Economic and Monetary Union have greatly increased the number of potential competitors for most lines of business (though for the time being at least, not at the retail level). However, the sector faces long-standing structural problems that have not yet been solved by the recent consolidations. In particular there appears to be considerable scope for reducing the number of branches and, especially, for rationalizing employment.[14] There seemed to be broad consensus that these adjustments would occur, though labor-market rigidities would limit the pace.

24. **The agglomeration of banking and securities institutions with insurance companies has raised potential supervisory issues.** Regarding cross-border aspects, the Belgian supervisors have made arrangements with their counterparts in other countries to supervise institutions that are partly foreign owned (such as Fortis). Such arrangements should be viewed in the broader context of the evolution of financial supervision in the EU as a whole, the direction of which remains uncertain. Within Belgium, there has been no move to merge insurance supervision (the responsibility of the Economics Ministry) with banking supervision (the Banking and Finance Commission), in part because, as a legal matter, full mergers between banks and insurance companies are not possible. In addition, the authorities noted that the two businesses are quite different and therefore require different regulatory expertise and approaches, though they were well aware that in practice the fates of the two types of institutions are becoming more closely intertwined, and that in some cases, they sell effectively the same financial product. The staff urged that adequate relations between the regulators be ensured, given the changing circumstances in the industry.

C. Other Issues

25. **On trade,** the authorities fully supported the EU position at the WTO negotiations, including the establishment of a working party at the WTO to discuss labor and environmental issues. **Data provision** is adequate for surveillance purposes (see Appendix III). With regard to **development assistance**, aid has risen gradually to 0.36 percent of GDP, higher than in many other countries, though below the United Nations target of 0.7 percent. The mission encouraged greater effort and welcomed the commitment in the 2000 Budget to continue to increase this percentage.

[14] See Jan Smets and Thierry Timmermans, "Stratégies individuelles et restructuration collective des banques belges," Revue de la Banque, 1999.

IV. Staff Appraisal

26. **With economic prospects brightening, it is time to complete the task of putting the public finances on a sound footing and to begin to implement comprehensive structural reforms.** It now appears that the economic recovery is solidly based, with output and employment growth having weathered international financial turbulence and the dioxin crisis. Since Belgium's cyclical position is close to the Euro-area average, the supportive monetary conditions should help to ensure a continued recovery without undue risk of rising inflation. Against this promising macroeconomic backdrop, the authorities should move quickly and decisively to meet the two major economic policy challenges. The first is to continue the task of fiscal consolidation; in particular, reduction of the debt-GDP ratio. The second is to move on a broad front to address the pervasive and long standing weaknesses in the labor market.

27. **There has been a marked improvement in the fiscal situation over the past decade, but addressing the two chief medium-term priorities—ensuring the medium-term health of the public finances and improving labor-market performance—remains urgent.** Control of fiscal deficits, notably by maintaining the key fiscal anchor of the 6 percent primary surplus, has turned the fiscal situation around. Nevertheless, there is still a need to continue to maintain this primary surplus in order to reduce the high debt-GDP ratio further. Debt reduction would free up fiscal resources for other uses, particularly to deal with population aging, and would reduce the vulnerability of the public finances to interest rate increases. However, it will inevitably constrain the pace with which the tax burden can be cut. At the same time, however, the high labor-tax wedge remains an important factor in limiting recorded employment and sustaining the gray economy. And these factors cut into the tax base. Clearly, breaking out of this circle will require coordinated action on several fronts: keeping public expenditure in check; reducing the tax wedge; and implementing broad-based structural reforms to leverage the employment-creating effect of the tax cuts.

28. **In the short term, it will be crucial to redeem the promise of a balanced budget by 2002.** In this perspective, the 2000 Budget was a lost opportunity to take another step toward this goal. The lack of progress in reducing the structural deficit in 2000 will not jeopardize the more important goal of a balanced budget in 2002, but it will make that goal somewhat harder to reach. The reduced room for maneuver underscores the need to maintain the primary surplus anchor until at least 2002. Apart from its direct contribution to fiscal discipline, this rule sends an important signal regarding the authorities' commitment to consolidation. It will also be important to keep tight control on expenditures. Thus, any windfalls from unexpectedly high growth or low interest rates should be devoted first to deficit reduction, and not to spending.

29. **Beyond 2002, a sustainable position of budget balance is needed to ensure fiscal soundness.** However, given the need to reduce rapidly and steadily the very high public debt, it would be better to maintain the 6 percent primary surplus rule for two or three years beyond 2002 in order to build up a modest budget surplus. Such a policy would hasten the pace of

debt reduction, thus helping to prepare for population aging. In any case, the automatic stabilizers should be allowed to operate, and in the current relatively buoyant economic climate the proceeds should be used for deficit reduction.

30. **In the medium term, expenditure control will be the key to reducing the debt-GDP ratio further, and to sustainably lowering the tax burden.** Holding the average real growth of general government primary expenditures to 1½ percent a year is a realistic goal that would provide the room for debt reduction and tax relief. There are, however, already pressures on expenditures—at the federal level, for the judiciary and police, infrastructure, and health care; and at the community level, for education—that must either be contained or be offset by lower growth in other spending. A successful program of structural reform would hold the prospect of savings on outlays for income support. In addition, the authorities should consider developing an explicit expenditure framework. This would strengthen an expenditure restraint policy, both directly by restricting the scope for increased outlays and indirectly by influencing the public's expectations. Such a framework could take many forms, but it needs to cover most public expenditures, have a multi-year horizon, and be transparent.

31. **Addressing the structural weaknesses of the labor market calls for a sustained, comprehensive, and balanced approach that goes beyond the current policy of focusing on the tax wedge.** Much is at stake: increasing employment and reducing regional disparities will be vital to the long-term economic and fiscal outlook. Raising the employment rate will be key to sustained reductions in tax rates and to meeting the fiscal challenge of population aging. The authorities' policy of reducing the tax wedge (including social security contributions) is clearly an important part of the solution, and should be pursued to the extent the overall fiscal position allows. The cuts in the 2000 Budget have been geared toward reducing non-wage labor costs, a goal worth pursuing. Taken alone, however, this policy is likely to prove insufficient, particularly as labor supply constraints are already beginning to be felt in much of the country.

32. **The incentives to seek work and keep a job need to be enhanced by increasing the attractiveness of work relation to income support benefits.** An obvious way to tackle the very high incidence of long-term unemployment is to limit the duration of unemployment benefits, or reduce the size of the benefit as the spell of unemployment lengthens. Likewise, phasing out early-retirement programs and the special unemployment regime for those over 50 would help to increase the labor-force participation of older people. In any case, measures such as these will be critical to ensure that the cohort now between 40 and 50 years old does not face special inducements to leave the workforce prematurely, which would prove doubly costly. Finally, the obligations of benefit recipients to actively seek work or to engage in effective training need to be strongly enforced.

33. **It will also be important to enhance programs to increase employability.** Closer cooperation among the PES, which are a regional responsibility, would help to alleviate interregional employment disparities. Likewise, increased collaboration between the PES and the federally run social security administration (which provides benefits) could usefully steer

the unemployed away from income support and into jobs. There also appears to be scope for better adapting training to job needs, and encouraging those receiving benefits to enroll in training instead.

34. **With the macroeconomic situation improving significantly, it is now a propitious time to introduce the needed fundamental reforms.** Measures to sharpen incentives and raise labor supply would likely result in some disruption as the process of adjustment is played out. On the one hand, the extensive Belgian social safety net would surely act as a cushion in this regard. Perhaps more importantly, the buoyant macroeconomy should help to ensure that those who are displaced find alternative employment opportunities, thereby limiting adverse effects of the adjustment process.

35. **Comprehensive product market reform, by increasing economic dynamism, would also increase job opportunities.** Barriers to business creation and expansion should be lowered, for example, by reforming zoning rules and reducing red tape. This is particularly the case in the services sector, which has been a source of growth in many countries and could usefully be further developed in Belgium. The public sector can have a direct impact by reducing the administrative burden it places on the private sector, and in this context the staff welcomes the establishment of the commissioner and agency to address this issue, but urge the authorities to ensure they receive adequate resources and cooperation from the rest of the public administration.

36. **The recent wave of consolidation ought to strengthen the financial sector, but raises supervisory issues.** Though concentration in the Belgian market has increased as a result, competition remains strong and, in any case, is increasingly coming from the euro area as a whole. As the consolidation process has involved links across borders and across lines of business, it will be important for supervisors to keep pace. In particular, the links between Belgian banking and insurance supervisors should be reviewed and upgraded as needed.

37. It is proposed that the **next consultation** be conducted on the normal 12-month cycle.

Belgium: Basic Data

Demographic and other data:

Population (end-1997)	10.2 million
GNP per capita (1997)	US$ 23,640
Social indicators (1993)	
Life expectancy at birth	
Male	74
Female	81
Infant mortality rate	6 per 1,000 live births
Population per physician (1995)	437
Population per sq. km. (1995)	335

	1988		1998	
	Billions of BF	Percent of GDP	Billions of BF	Percent of GDP
Private consumption	3,192	55.7	4,890	53.8
Public consumption	1,219	21.3	1,917	21.1
Gross capital formation	1,170	20.4	1,918	21.1
Exports of goods and services	3,942	68.8	6,868	75.6
Imports of goods and services	3,791	66.2	6,502	71.5
GDP	5,730	100.0	9,088	100.0

	1994	1995	1996	1997	1998	1999 Est.	2000 Proj.
			(Changes in percent)				
National Accounts							
Demand and output (volume)							
Private consumption	1.9	0.7	0.6	2.2	3.8	2.0	2.5
Public consumption	1.5	1.3	2.2	0.1	1.3	2.5	1.7
Gross fixed investment	-0.1	5.6	1.0	6.5	3.7	2.9	3.1
Of which:							
Enterprise investment	-2.5	7.8	4.2	7.2	4.7	3.6	3.5
Stockbuilding 1/	0.6	0.1	-0.3	0.1	0.8	-0.7	0.3
Total domestic demand	2.1	1.9	0.8	2.7	4.1	1.6	2.8
Exports of goods and nonfactor services	8.4	5.7	1.3	6.8	4.2	1.7	6.0
Imports of goods and nonfactor servises	7.3	5.0	1.0	5.8	6.3	1.0	5.8
Foreign balance 1/	0.9	0.7	0.3	0.9	-1.2	0.6	0.3
GDP	3.0	2.5	1.0	3.5	2.7	2.0	3.0
Output gap (in percent of potential GDP)	-3.0	-2.5	-3.4	-2.1	-1.5	-1.5	-0.6
Manufacturing production	4.5	2.7	0.0	4.6	0.0	2.0	2.1

	1994	1995	1996	1997	1998	1999 Est.	2000 Proj.
				(Changes in percent)			
Labor market							
Labor force (national definition)	0.3	0.6	0.3	0.4	0.2	0.2	0.3
Employment (national definition)	-0.8	0.7	0.4	0.8	1.0	1.0	0.6
Unemployment rate (national definition) 2/	12.9	12.9	12.6	12.4	11.6	10.9	10.6
EU harmonized unemployment rate /2	10.0	9.9	9.7	9.4	9.5	9.0	8.8
NAIRU	8.4	8.4	8.3	8.2	8.1	8.1	8.1
Prices, wages and incomes							
GDP deflator	1.8	1.8	1.2	1.3	1.6	1.2	1.1
Terms of trade (goods)	-0.8	-1.1	-0.4	-0.6	1.2	-0.1	-0.2
Consumer price index 3/	2.4	1.4	1.8	1.5	0.9	1.1	1.4
Compensation 4/	2.5	2.6	1.4	2.7	2.7	3.0	3.5
Labor productivity 4/	3.1	1.8	0.3	3.0	2.4	2.0	2.0
Unit labor costs 4/	-0.6	0.8	1.1	-0.3	0.3	1.0	1.5
Real disposable income	-0.6	0.3	-0.2	0.5	2.6	1.6	1.3
				(In percent)			
Interest rates							
Money market rate 5/	5.7	4.8	3.2	3.5	3.6	3.0	...
Government bond yield	7.8	7.3	6.3	5.7	4.7	4.8	...
				(In percent of GDP)			
Saving and investment							
Private saving	32.5	27.3	26.7	25.8	24.5	23.9	24.1
Of which:							
Household saving as percent of disposable household income	18.5	19.7	18.7	17.5	16.4	16.1	15.3
Private investment	17.6	18.8	18.4	19.0	19.5	19.3	19.4
Private saving surplus	14.9	8.5	8.3	6.9	5.0	4.7	4.6
Government saving surplus	-11.1	-4.2	-3.7	-1.8	-1.0	-0.8	-0.6
National saving surplus	3.8	3.7	3.6	4.1	3.5	3.5	3.7
Public finances, general government							
Revenue	45.7	45.4	46.0	46.3	46.4	46.3	45.4
Expenditure	50.6	49.6	49.7	48.3	47.5	47.1	46.2
Of which:							
Interest on public debt	9.5	9.1	8.7	7.9	7.7	7.1	6.8
Fiscal balance	-4.9	-4.2	-3.7	-2.0	-1.0	-0.9	-0.8
Primary balance	4.5	4.9	5.0	5.9	6.6	6.3	6.1
Structural balance	-3.2	-2.8	-1.7	-0.8	-0.2	0.0	-0.4
Structural primary balance	6.3	6.3	7.1	7.1	7.5	7.1	6.4
Gross public debt	134.5	131.8	128.3	123.0	117.4	115.0	111.2

	1994	1995	1996	1997	1998	1999 Est.	2000 Proj.
	(In billions of Belgian francs)						
Balance of payments 6/							
Current account balance	421	420	435	499	440	450	478
(In percent of GDP of Belgium)	5.4	5.2	5.2	5.7	4.8	4.8	4.9
Trade balance	231	282	269	279	274	334	344
(In percent of GDP of Belgium)	3.0	3.5	3.2	3.2	3.0	3.6	3.5
Official reserves (US$ billion) 7/	13.9	16.2	17.0	16.2	18.3	10.9	...
Reserve cover (months of imports of GNFS)	1.1	1.1	1.1	1.1	1.2	...	...
Exchange rates							
Euro per U.S. dollar (December 30, 1999) 8/						1.00	
Nominal effective rate (1990=100)	96.1	100.0	97.9	93.9	93.9	92.8	...
Real effective rate (1990=100) 9/	96.5	100.0	97.3	93.2	92.1	91.3	...

Sources: Data provided by the authorities; and Fund staff estimates and projections.

1/ Contribution to growth.
2/ Percent of the labor force
3/ Harmonized consumer price index as of 1996.
4/ Manufacturing, full-time equivalent.
5/ For 1999, Euro rate.
6/ Belgium-Luxembourg Economic Union (BLEU) on a transactions basis.
7/ Excluding gold; since January 1999, Eurosystem's definition.
8/ Belgium entered the final stage of EMU on January 1, 1999 at a rate of 40.3399 Belgian francs to the euro.
9/ Based on relative normalized unit labor costs in manfacturing.

Belgium: Fund Relations
(As of December 31, 1999)

I. **Membership Status**: Joined 12/27/45; Article VIII

II. **General Resources Account**:	**SDR Million**	**% Quota**
Quota	4,605.20	100.0
Fund holdings of currency	2,936.83	63.8
Reserve position in Fund	1,668.38	36.2
Operational budget transfers (net)	-51.00	

III. **SDR Department**:	**SDR Million**	**% Allocation**
Net cumulative allocation	485.25	100.0
Holdings	197.10	40.6
Designation plan	3.00	

IV. **Outstanding Purchases and Loans**: None

V. **Financial Arrangements**: None

VI. **Projected Obligations to Fund** (SDR Million; based on existing use of resources and present holdings of SDRs): None

VII. **Exchange Rate Arrangement**:

Until December 31, 1998, Belgium formed a monetary union with Luxembourg in which the Belgian and Luxembourg franc were at par, while also participating in the exchange rate mechanism of the European Monetary System. Belgium entered the final stage of European Economic and Monetary Union on January 1, 1999 at a rate of 40.3399 Belgian francs to the euro.

VIII. **Article IV Consultations**:

Belgium is on the 12-month cycle; the last consultation was completed on February 12, 1999 (EBM/99/15).

IX. Belgium retains restrictions vis-à-vis Iraq, the Socialist People's Libyan Arab Jamahiriya, and the Federal Republic of Yugoslavia (Serbia and Montenegro) pursuant to U.N. Security Council resolutions 661, 883, and 757, respectively. These restrictions have been notified to the Fund pursuant to Decision No. 144-(52/51) in EBD/90/251 (8/17/90), EBD/94/187 (11/29/94), and EBD/92/139 (7/7/92). The residual restrictions vis-à-vis the Federal Republic of Yugoslavia (Serbia and Montenegro) relate solely to balances of the former National Bank of Yugoslavia that remain frozen, since they are subject to unresolved legal claims.

Belgium: Statistical Data Issues

Data provision has been improved, notably for the national accounts and trade data. Specifically annual and quarterly national accounts are provided by the National Accounts Institute; financial and balance of payments data are provided by the National Bank of Belgium (NBB); and fiscal data are provided by the Ministry of Finance, and converted on a national accounts basis by the NBB. The authorities subscribe to the Special Data Dissemination Standards, and provide information on data and dissemination practices on the Dissemination Standards Bulletin Board. The process of migrating from the ESA79 to ESA95 national accounts has been temporarily disruptive, but appears to be on schedule for completion by early 2000.

Belgium: Core Statistical Indicators

As of end-December 1999

	Exchange Rates	Interest Rates	Consumer Price Index	Exports/ Imports	Current Account Balance	Overall Government Balance	GDP/GNP
Date of Latest Observation	12/30/99	12/30/99	11/99	9/99	6/99	1998	Q2/99
Date Received	12/30/99	12/30/99	12/1/99	10/8/99	10/8/99	8/99	8/99
Frequency of Data	Daily	Daily	Monthly	Monthly	Quarterly	Annually	Quarterly
Frequency of Reporting	Daily	Daily	Monthly	Monthly	Quarterly	Annually	Quarterly
Source of Update	Reuters	Reuters	NBB 1/	NBB 1/	NBB 1/	NAI 2/	NBB 1/
Mode of Reporting	Electronic	Electronic	NBB Website	NBB Website	NBB Website	E-mail	NBB Website
Confidentiality	Public	Public	Public	Public	Public	Public	Public
Frequency of Publication	Daily	Daily	Monthly	Monthly	Monthly	Annually	Quarterly

1/ National Bank of Belgium.
2/ National Accounts Institute.

Medium-Term Public Expenditure Programming in the Netherlands, the United Kingdom, and Finland

	Netherlands	United Kingdom	Finland
Horizon	Four years, set at outset of coalition period	Three years on a two-year rolling basis (i.e., with successive frameworks overlapping by one year) for non-cyclical expenditures (see coverage); cyclical or volatile spending is managed on an annual basis	Four years, on annually rolling basis
Objective	To achieve a parallel reduction in the deficit and tax burden	Over the cycle, to balance the current budget and maintain investment (and hence borrowing) at a sustainable level, while meeting the Government's priorities	In past, mainly geared to deficit reduction; in future also to provide room for tax cuts
Coverage of medium-term spending targets	Expenditures of central government (excluding infrastructure fund) and social security funds; subceilings on central government, health, and social security	Departmental Expenditure Limits (DELs), covering most non-cyclical primary expenditures (some half of total expenditures); includes central government support for local government but not local authoritity's self-financed expenditure	Total central government expenditures and subceilings for individual ministries, including transfers to local governments and social security funds; excludes local governments' self-financed expenditure
Statutory nature of medium-term spending targets	Budget year binding; outer years politically but not legally binding; submitted to parliament for information; contingency reserve to deal with changing circumstances	Budget year binding; outer years not legally binding but overall DELs announced in parliament; contingency reserve to deal with changing circumstances	Budget year binding; outer years agreed by cabinet as nonbinding norm to ministries; published but not submitted to parliament
Nominal or real targets	Medium-term at constant prices; for one-year budget, translated to current prices based on projected GDP deflator	All targets set in current prices	Medium-term at constant prices of budget year; for new budget translated to current prices based on specific price and cost deflators

	Netherlands	United Kingdom	Finland
Macroeconomic assumptions	Growth forecast cautious; rule splits "growth dividend" between additional deficit and tax cuts	Growth forecast at conservative end of potential output range	Underlying assumptions reflect central forecast
Adjustments in target levels for outer years	No adjustment in real expenditure; only "automatic" translation of targets into current prices based on aggregate inflation forecast	Medium-term DELs in current prices are adjusted only if new inflation forecasts differ significantly from original projections	Ceilings for outer years can be adjusted; automatic adjustment for wage and salary increases
Autonomy and incentives at lower levels	Ministries and agencies bound by annual budget; part of funds can be carried over to next year; no penalties have been imposed for repeated healthcare overruns	Individual departments bound by DELs; within these limits departments can recycle any efficiency savings they make; unspent DEL funds can be carried over to next year; overruns are avoided by strict DELs	Ministries and agencies bound by annual budget; some appropriations transferable, avoiding "forced" consumption at end of fiscal year
Output objectives and quality control	No formalized output objectives	Publication of Public Service Agreements alongside spending plans, stating departments' goals and setting specific quantified policy and efficiency targets	Agencies establish result and efficiency targets, with ex-post evaluation by ministries

Source: International Monetary Fund, 1999, "Finland: Selected Issues", *IMF Staff Country Report*, No. 99/122.

Four Scenarios for the Public Finances

This appendix presents four scenarios for the public finances, illustrating the rewards from expenditure restraint and the scope for accelerating tax cuts. In each scenario, the general government deficit is eliminated by 2002, in line with the Stability Program. The decrease in the revenue share in these scenarios broadly corresponds to the degree of primary expenditure restraint and the gradual decline in interest costs. As the latter would amount to about 3 percentage points of GDP over the next decade, a significant tax cut could be achieved in combination with continued primary spending restraint.

Reflecting Belgium's high debt level, interest rate increases have a considerable fiscal impact. In broad terms, slightly less than 20 percent of total debt is short term, with the rest being divided between 5-year and 10-year debt. The effects of a change in interest rates can be illustrated by assuming a one percentage point increase in interest rates at all maturities, holding maturity structure of debt constant, and assuming budget balance from 2002 onwards (as specified in the Stability Program). In the first year, interest rate payments would rise by 0.2 percentage points of GDP, reflecting a debt ratio somewhat higher than 100 percent and a share of short-term debt slightly lower than 20 percent. After five years, interest costs would be about 0.6 percentage points of GDP higher. Costs would continue to rise until 2010, when they would amount to 0.8 percentage points of GDP, reflecting a debt ratio that had fallen to 80 percent.

The calculations also indicate that the fiscal repercussions of population aging can be absorbed if expenditure restraint is preserved. After 2005, aging is projected to imply slightly higher growth of social security spending—in particular on pensions and health care—and after 2010, an anticipated decline in the working-age population would dampen growth. Both the interest savings from debt reduction and a possible increase in the employment ratio, boosting the tax base, could help offset the resulting squeeze of the public finances.

If annual real primary expenditure growth remains at 1.5 percent, a sustainable reduction in the revenue share, of about 5 percent of GDP, could be achieved by 2010. In the baseline scenario, which corresponds to the staff projection, and is presented in the top panel of the table, primary spending growth is kept at 1.5 percent until 2005. Subsequently, primary spending increases slightly faster, reflecting the aging-induced rise in social security spending. Maintaining fiscal balance leaves room for a cut in the revenue-GDP ratio from 46.4 percent in 1999 to 41.3 percent in 2010, while the debt ratio declines to 78.4 percent of GDP. After 2010, the gains from an ongoing decrease in interest costs broadly offset the effects of population aging on expenditure and growth.

An initially more ambitious target for the fiscal balance, would eventually create room for somewhat larger tax cuts. The second panel of the table illustrates the effects of maintaining a surplus of 1 percent of GDP up to 2015, when the debt stock has declined to

less than 60 percent of GDP. On this basis, the revenue share would be reduced to about 40 percent by 2030.

The critical role of expenditure restraint is illustrated in the third scenario, which features higher spending growth. Annual spending growth is 0.5 of 1 percentage point higher in this secnario than in the baseline projection, leaving little room for tax cuts. Following a minor reduction in the revenue ratio by 2010, this ratio would return to its high current level by 2030.

The fourth scenario illustrates the scope for accelerated tax cuts in the context of improved growth performance. Technically, this scenario shows that, with an increase in the employment ratio of 3 percentage points by 2010, the spending and fiscal balance goals of the baseline scenario are consistent with an additional 2 percent decline in the revenue share. Such an improvement in the employment rate could be achieved partly from the tax cuts themselves, and partly from other reforms to the labor market.

Table 2. Belgium: Four Fiscal Scenarios, 1997-2030

	1997	1998	1999	2000	2001	2002	2003	2010	2020	2030
Baseline scenario					(In percent of GDP)					
Revenue	46.3	46.4	46.3	45.4	45.0	44.7	44.0	41.3	40.1	40.4
Expenditure	48.3	47.5	47.1	46.2	45.3	44.7	44.0	41.3	40.1	40.4
Primary expenditure	40.4	39.8	40.0	39.4	39.1	38.8	38.5	37.0	36.9	38.0
of which: Social security	18.5	18.3	18.2	18.0	17.8	17.7	17.6	17.3	17.9	19.0
Interest payments	7.9	7.7	7.1	6.8	6.3	5.9	5.5	4.2	3.1	2.4
Balance	-2.0	-1.0	-0.9	-0.8	-0.3	0.0	0.0	0.0	0.0	0.0
Primary balance	5.9	6.6	6.3	6.1	6.0	5.9	5.5	4.2	3.1	2.4
Debt	123.0	117.4	115.0	111.1	107.5	103.9	100.5	78.9	58.5	44.7
Memorandum items:					(In percent)					
Primary expenditure growth	2.3	1.2	2.6	1.1	1.5	1.5	1.5	1.7	1.7	1.8
Employment rate	56.7	57.4	57.9	58.4	58.8	58.9	59.1	59.3	59.3	59.3
GDP growth	3.5	2.7	2.0	3.0	2.4	2.2	2.2	2.3	1.7	1.4
Baseline, with a small surplus up to 2015					(In percent of GDP)					
Revenue	46.3	46.4	46.3	45.4	45.0	44.7	44.5	42.0	39.6	40.1
Expenditure	48.3	47.5	47.1	46.2	45.3	44.7	44.0	41.0	39.6	40.1
Primary expenditure	40.4	39.8	40.0	39.4	39.1	38.8	38.5	37.0	36.9	38.0
Interest payments	7.9	7.7	7.1	6.8	6.3	5.9	5.5	3.9	2.7	2.1
Balance	-2.0	-1.0	-0.9	-0.8	-0.3	0.0	0.5	1.0	0.0	0.0
Primary balance	5.9	6.6	6.3	6.1	6.0	5.9	6.0	4.9	2.7	2.1
Debt	123.0	117.4	115.0	111.1	107.5	103.9	100.0	72.2	50.2	38.4
Memorandum items:					(In percent)					
Primary expenditure growth	2.3	1.2	2.6	1.1	1.5	1.5	1.5	1.7	1.7	1.8
Employment rate	56.7	57.4	57.9	58.4	58.8	58.9	59.1	59.3	59.3	59.3
GDP growth	3.5	2.7	2.0	3.0	2.4	2.2	2.2	2.3	1.7	1.4
Higher expenditure growth					(In percent of GDP)					
Revenue	46.3	46.4	46.3	45.4	45.2	45.0	44.6	43.1	43.8	46.4
Expenditure	48.3	47.5	47.1	46.2	45.5	45.0	44.6	43.1	43.8	46.4
Primary expenditure	40.4	39.8	40.0	39.4	39.2	39.2	39.1	38.9	40.7	44.0
of which: Social security	18.5	18.3	18.2	18.0	17.9	17.9	17.9	18.0	19.3	21.4
Interest payments	7.9	7.7	7.1	6.8	6.3	5.9	5.5	4.2	3.1	2.4
Balance	-2.0	-1.0	-0.9	-0.8	-0.3	0.0	0.0	0.0	0.0	0.0
Primary balance	5.9	6.6	6.3	6.1	6.0	5.9	5.5	4.2	3.1	2.4
Debt	123.0	117.4	115.0	111.1	107.5	103.9	100.5	78.9	58.5	44.7
Memorandum items:					(In percent)					
Primary expenditure growth	2.3	1.2	2.6	1.1	2.0	2.0	2.0	2.2	2.2	2.2
Employment rate	56.7	57.4	57.9	58.4	58.8	58.9	59.1	59.3	59.3	59.3
GDP growth	3.5	2.7	2.0	3.0	2.4	2.2	2.2	2.3	1.7	1.4

	1997	1998	1999	2000	2001	2002	2003	2010	2020	2030
Baseline, with higher economic growth					(In percent of GDP)					
Revenue	46.3	46.4	46.3	45.4	44.8	44.2	43.4	39.2	38.1	38.4
Expenditure	48.3	47.5	47.1	46.2	45.1	44.2	43.4	39.2	38.1	38.4
Primary expenditure	40.4	39.8	40.0	39.4	38.9	38.4	37.9	35.2	35.1	36.2
of which: Social security	18.5	18.3	18.2	18.0	17.8	17.6	17.4	16.5	17.0	18.1
Interest payments	7.9	7.7	7.1	6.8	6.3	5.8	5.4	4.0	3.0	2.3
Balance	-2.0	-1.0	-0.9	-0.8	-0.3	0.0	0.0	0.0	0.0	0.0
Primary balance	5.9	6.6	6.3	6.1	6.0	5.8	5.4	4.0	3.0	2.3
Debt	123.0	117.4	115.0	111.1	107.0	102.8	98.9	75.0	55.6	42.6
Memorandum items:					(In percent)					
Primary expenditure growth	2.3	1.2	2.6	1.1	1.5	1.5	1.5	1.7	1.7	1.8
Employment rate	56.7	57.4	57.9	58.4	59.1	59.6	60.0	62.3	62.3	62.3
GDP growth	3.5	2.7	2.0	3.0	2.9	2.7	2.7	2.8	1.7	1.4

Sources: Data provided by the authorities; and Fund staff projections.

INTERNATIONAL MONETARY FUND

BELGIUM

Staff Report for the 1999 Article IV Consultation
Supplementary Information

Prepared by the European I Department

(In Consultation with other Departments)

Approved by C. M. Watson and G. Russell Kincaid

February 24, 2000

1. This supplement is based on information on economic and financial developments in Belgium since the issuance of the staff report (SM/00/20) on February 2, 2000. This additional information does not alter the broad thrust of the staff appraisal. However, it does modify the fiscal outlook.

2. The latest cyclical indicators suggest improved short-term growth prospects. The staff's projection of real GDP growth for 2000 has been revised upward to 3.3 percent, from 3 percent in the staff report.

3. As a result of this revision (as well as lower assumed interest costs), the general government fiscal deficit is now projected to fall from 0.9 percent of GDP in 1999 to 0.5 percent of GDP in 2000 (rather than to 0.8 percent in the staff report). It has thus become even likelier than at the time of the mission discussions that the Stability Program goal of actual budget balance in 2002 can be achieved, assuming fiscal consolidation efforts are continued as the authorities plan. Depending on growth in 2001, budget balance could even be reached in that year.[1] The Belgian government adopted a new 2000–03 Stability Program at end-1999 and will soon be considered by the ECOFIN Council. Compared to the 1999–2002 Stability Program available at the time of the mission, the medium-term fiscal plan is close to the staff appraisal. In particular, real primary expenditure growth is now to be held to 1.5 percent a year as recommended by staff and a small structural budget surplus after 2002 (rather than a structural balance) is deemed desirable by the authorities. Thus, while the budget remains expansionary, the revisions for 2000 and the medium-term changes to the Stability Program mitigate concerns in the staff report that deficit reduction targets in 2000 were insufficiently ambitious.

4. Regarding monetary conditions, the ECB raised its policy rate by 25 basis points on February 3, 2000. In itself, this had only a marginal impact on the generally supportive monetary conditions for Belgium.

[1] In a recent statement, the National Bank concludes that balance could be reached by 2001.

Belgium: Public Finances, 1993-2000

(In percent of GDP)

	1993	1994	1995	1996	1997	1998	1999 Est.	2000 Proj.
Revenue	45.4	45.7	45.4	46.0	46.3	46.4	46.3	45.2
Expenditure	52.6	50.6	49.6	49.7	48.3	47.5	47.1	45.7
Primary expenditure	41.7	41.1	40.5	40.9	40.4	39.8	40.0	39.1
Federal	14.1	13.8	13.2	13.2	13.1	12.7	12.8	12.4
Social security	19.3	18.8	18.8	19.1	18.5	18.3	18.2	17.8
Local government	5.3	5.4	5.2	5.2	5.2	5.2	5.3	5.2
Regions and communities	11.4	11.4	11.5	11.4	11.4	11.3	11.2	11.1
Intergovernment transfers	-8.4	-8.3	-8.1	-8.0	-7.7	-7.6	-7.5	-7.4
Interest payments	10.9	9.5	9.1	8.7	7.9	7.7	7.1	6.6
Balance	-7.2	-4.9	-4.2	-3.7	-2.0	-1.0	-0.9	-0.5
Federal	-5.8	-4.6	-3.8	-3.4	-2.7	-1.9	-1.8	-1.1
Social security	-0.5	0.5	0.0	-0.2	0.4	0.4	0.5	0.2
Local government	-0.1	0.1	0.4	0.3	0.3	0.2	-0.1	0.1
Regions and communities	-0.8	-0.9	-0.7	-0.4	-0.1	0.2	0.5	0.3
Memorandum items:								
Primary balance	3.7	4.5	4.9	5.0	5.9	6.6	6.3	6.1
Structural balance	-5.3	-3.2	-2.8	-1.7	-0.8	-0.2	0.0	-0.3
Structural primary balance	5.7	6.3	6.3	7.1	7.1	7.5	7.1	6.3
Output gap	-3.8	-3.0	-2.5	-3.4	-2.1	-1.5	-1.5	-0.3
Debt	135.9	134.5	131.8	128.3	123.0	117.4	115.0	110.7
Net debt	126.7	126.2	125.3	122.4	118.0	112.3	...	...
				(Growth rate, in percent)				
Memorandum items:								
Primary expenditure	1.6	1.6	0.9	2.0	2.3	1.2	2.6	1.1
GDP growth	-1.4	3.0	2.5	1.0	3.5	2.7	2.0	3.3

Sources: Data provided by the authorities; and Fund staff projections.

INTERNATIONAL MONETARY FUND

Public Information Notice

EXTERNAL RELATIONS DEPARTMENT

Public Information Notice (PIN) No. 00/16
FOR IMMEDIATE RELEASE
March 3, 2000

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Concludes Article IV Consultation with Belgium

On February 25, 2000, the Executive Board concluded the Article IV consultation with Belgium.[1]

Background

Economic activity picked up in the course of 1999, despite the dioxin crisis of mid-year, due to a recovery in export markets following the world financial turmoil of late 1998, supportive monetary policy in the euro area, improvements in business and consumer confidence, and continued growth in employment. At end-1999, there was still a margin of excess capacity and, in the absence of generalized pressures in product and labor markets, **inflation** has tended to fall along with the Euro-area average. Moderate price and wage inflation has preserved Belgian competitiveness, though buoyant import demand and a flagging world economy resulted in a narrowing of the current account surplus by almost 1 percentage point of GDP in 1998, to about 4¾ percent of GDP, where it remained through 1999.

The situation in **labor markets** remains unsatisfactory, with a high unemployment rate and a very low participation rate. Though the unemployment rate, on a harmonized basis, fell by ½ of 1 percentage point during 1999 and at about 8 ½ percent in January, 2000 it is still high. Moreover, there are considerable regional disparities in labor-market performance, as unemployment has remained very high in much (but by no means all) of Wallonia, while shortages have emerged in most areas of Flanders (and some parts of Wallonia). Long-term unemployment remains stubbornly high. Both the employment rate and the participation rate are well below the EU average, a situation that is particularly marked for those above 50 years of age (who benefit from widespread early retirement schemes).

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. In this PIN, the main features of the Board's discussion are described.

The **fiscal situation** improved markedly over the past decade, though there is much more to be done. The debt-GDP ratio peaked at 136 percent in 1993, but has since declined rapidly as the fiscal deficit was cut from 7.2 percent of GDP in 1993 to only 0.9 percent in 1999. More than half of this reduction is accounted for by falling interest costs (and most of this, by lower interest rates), though increases in the primary surplus were important as well. There was significant progress on the expenditure side, with the ratio of general government expenditure to GDP falling by 5 ½ percentage points over this period. However, the overriding need to cut the deficit ruled out a decline in the tax burden (the ratio of general government revenue to GDP). The key to fiscal control has been the policy of enlarging the primary surplus and then, from about 1997, maintaining it at 6 percent of GDP or higher. Despite this progress, both the debt ratio and the tax burden remain high. The debt ratio still amounted to 115 percent at end-1999, and at more than 46 percent the revenue-GDP ratio is one of the highest in the Euro area. However, the 2000 budget contains significant tax reductions, mainly in the form of lower employers' social security contributions, of some ½ of 1 percent of GDP.

The short-term **economic prospects** are improving, with real GDP projected by the staff to grow by 3.3 percent in 2000. This projected increase in growth reflects three factors. First, macroeconomic policies are assumed to remain accommodative. The 2000 Budget is, in the staff's evaluation, slightly expansionary in thrust (as measured by the change in the structural balance), although the actual budget deficit is projected to decline significantly. Monetary conditions are also likely to remain supportive of further expansion. Second, the external situation is set to continue to improve, particularly in view of the anticipated pickup of activity in Germany and France. And, finally, consumption should continue to be bolstered by household confidence and employment gains. Given the degree of aggregate economic slack and the already negotiated wage settlement (a maximum cumulative increase in wage costs of 5.9 percent in 1999–2000) underlying inflation and labor cost growth are projected to remain moderate.

Executive Board Assessment

Executive Directors commended the Belgian authorities for the marked improvement in their fiscal situation in recent years which had helped turn around the public debt dynamics. They welcomed the pickup in economic activity in the course of 1999, and noted that high household confidence, expanding export markets, and supportive monetary conditions should help ensure a continued economic recovery. Moreover, they observed that inflation would remain moderate in view of the existing economic slack and already negotiated wage settlements. Against this backdrop, Directors urged the authorities to continue their program of fiscal consolidation and debt reduction, and to accelerate the implementation of needed structural reform so as to strengthen their medium-term growth prospects and further address weaknesses in the labor market.

Directors welcomed the authorities' determination to achieve a balanced budget at least by 2002, and were encouraged by the recent progress made in reducing the deficit for the 2000 fiscal year. They also welcomed the authorities' intention to allocate any windfall gain from favorable economic circumstances primarily to deficit reduction. Directors did not share the staff's characterization of the 2000 budget as a lost opportunity, and noted that the prudent pace of expenditure growth in that budget permitted both deficit reduction and tax cuts, while

ensuring that the goal of a balanced budget could be reached sooner than 2002. They supported the authorities' policy to further reduce the tax burden, in particular to lower the high tax wedge on labor in the short run. But a few argued that a higher priority should have been given to debt reduction, in view of the still high debt and the budget's vulnerability to interest rate movements. Directors stressed that the envisaged tax cuts, together with further reductions in the debt to GDP ratio, would require continued strict spending discipline in the face of sometimes intense demands. In this context, a number of Directors saw merit in developing an explicit multiyear expenditure framework that could further help strengthen the authorities' commitment to expenditure restraint. Directors also encouraged the authorities to broaden the tax base and address distortions in their tax system so as to enhance its efficiency and contribute to reducing the size of the gray economy.

Pointing to the low employment rate and high unemployment, Directors urged that comprehensive structural reforms be adopted to complement the authorities' policy of reducing nonwage labor costs. They observed that the recovery provided a timely opportunity for implementing broad-based structural reforms. Taking action during the cyclical upswing would help ensure that jobs would be available for those in search of work. By increasing the economy's productive capacity, such reforms would also help to prolong the recovery phase. Noting the significant consolidation of the Belgian financial sector, Directors also encouraged the supervisory authorities to keep pace with the changing circumstances in the industry.

Directors encouraged the authorities to expand active labor market programs to ensure that those seeking work were well qualified and would be matched with suitable employment opportunities. They also urged the authorities to strengthen further the incentives to seek employment by increasing the attractiveness of work relative to income support programs—while preserving the core of the social safety net. Some Directors suggested limiting the duration of unemployment benefits in order to increase the job search incentives of the long-term unemployed. They also encouraged the authorities to strictly enforce the obligations for employment benefit recipients to seek work or enter training programs. To address the very low employment rate for older people, Directors underscored the importance of phasing out early retirement schemes and the special unemployment regime for those over 50 years of age. In light of the persistent regional labor market disparities, some Directors encouraged the authorities to promote more wage dispersion.

Directors considered that product market reform could help promote economic dynamism and increase job opportunities. They welcomed the recent progress in the liberalization of utilities and telecommunications, noting that there was still considerable scope for improving the functioning of markets. They encouraged the authorities to press ahead with such reforms, including by reforming zoning rules, reducing the administrative burden, and liberalizing shop opening hours. Directors welcomed the recent establishment of a commissioner and an agency to address the issue of the administrative burden of the public sector.

Directors commended the authorities for the increase in the budget for development assistance and welcomed the intention to move further toward the United Nations target.

Public Information Notices (PINs) are issued, (i) at the request of a member country, following the conclusion of the Article IV consultation for countries seeking to make known the views of the IMF to the public. This action is intended to strengthen IMF surveillance over the economic policies of member countries by increasing the transparency of the IMF's assessment of these policies; and (ii) following policy discussions in the Executive Board at the decision of the Board. As part of a pilot project, the staff report (use the free Adobe Acrobat Reader to view this pdf file) for the 1999 Article IV consultation with Belgium is also available on the IMF's website (http://www.imf.org).

Belgium: Selected Economic Indicators 1/

	1996	1997	1998	1999	2000 2/
Real economy (change in percent)					
Real GDP	1.0	3.5	2.7	2.0	3.3
Domestic demand	0.8	2.7	4.1	1.6	3.0
CPI (year average)	1.8	1.5	0.9	1.1	1.4
Unemployment rate (in percent)	9.7	9.4	9.5	9.0	8.5
Public finance (percent of GDP)					
General government balance	-3.7	-2.0	-1.0	-0.9	-0.5
Structural balance	-1.7	-0.8	-0.2	0.0	-0.3
Primary balance	5.0	5.9	6.6	6.3	6.1
General government debt	128.3	123.0	117.4	115.0	110.7
Interest rates (percent)					
Money market rate 3/	3.2	3.5	3.6	3.0	...
Government bond yield	6.3	5.7	4.7	4.8	...
Balance of payments (percent of GDP) 4/					
Trade balance	3.2	3.2	3.0	3.6	3.6
Current account	5.2	5.7	4.8	4.8	5.0
Official reserves (US$ billion) 5/	17.0	16.2	18.3	10.9	...
Reserve cover (months of imports of GNFS)	1.1	1.1	1.2	...	...
Exchange rate					
Exchange rate regime		Member of euro area			
Euro per U.S. dollar (February 29, 2000)				0.96	
Nominal effective rate (1995=100)	97.9	93.9	93.9	92.8	...
Real effective rate (1995=100) 4/ 6/	97.6	93.4	92.1	91.3	...

Sources: Data provided by the Belgian authorities, and IMF staff projections.

1/ National accounts and fiscal data reflect the adoption of ESA95.
2/ Staff projections.
3/ For 1999, Euro rate average.
4/ BLEU on a transactions basis.
5/ Excluding gold; since January 1999, Eurosystem's definition.
6/ Based on relative normalized unit labor costs in manufacturing.