FOR AGENDA

SM/83/257

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INFORMATION

December 29, 1983

To: Members of the Executive Board

From: The Acting Secretary

Subject: Belgium - Recent Economic Developments

This paper provides background information to the staff report on the 1983 Article IV consultation discussions with Belgium, which was circulated as SM/83/255 on December 21, 1983.

If Executive Directors have technical or factual questions relating to this paper prior to the Board discussion, they should contact Mr. Leipold, ext. 73743.

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INTERNATIONAL MONETARY FUND

BELGIUM

Recent Economic Developments

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Approved by the European Department

December 21, 1983

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Basic Data

Population (mid-1982):	9.85 million
GNP per capita (1982):	US$8,670

National accounts (in BF and as a percentage of GNP)

	1975		1982	
	BF	Percent	BF	Percent
Private consumption	1,421.1	61.1	2,599.6	66.6
Public consumption	388.4	16.7	740.1	19.0
Gross fixed capital formation	512.1	22.0	666.9	17.1
Exports of goods and services	1,156.5	49.7	3,132.7	80.3
Imports of goods and services	1,139.7	49.0	3,226.6	82.7
GNP	2,325.8	100.0	3,902.9	100.0

	1980	1981	1982	1983 1/
Demand and supply (volumes)	(Changes in percent)			
Private consumption	2.1	1.4	1.1	-3.0
Public consumption	1.6	0.9	-1.6	-1.5
Gross fixed investment	5.0	-14.5	-2.6	-1.7
Final domestic demand	2.6	-3.7	-0.1	-2.5
Stockbuilding 2/	-0.9	-0.4	--	0.3
Total domestic demand	1.7	-4.1	-0.1	-1.2
Exports of goods and services	7.6	8.7	2.6	3.5
Imports of goods and services	5.9	4.1	1.6	-0.5
Foreign balance 2/	0.9	3.0	0.8	2.9
GNP	2.6	-1.2	0.7	0.7
Industrial production 3/	-0.9	-2.5	-0.5	1.5
Manufacturing output	-1.2	-2.5	-0.5	2.4
Employment and unemployment	(In thousands; mid-year)			
Labor force	4,172	4,189	4,220	...
Employment	3,837	3,757	3,708	...
Unemployment	336	432	512	...
(In percent of civilian labor force) 2/	9.1	11.2	13.1	14.5
Prices and incomes	(Changes in percent)			
GNP deflator	4.3	5.3	7.0	7.5
Consumer price index	6.7	7.6	8.7	7.8
Terms of trade 3/	-3.4	-3.2	0.1	...
Hourly compensation (manufacturing)	9.6	8.1	5.3	5.6
Unit labor costs (manufacturing)	6.1	2.6	0.5	2.4
Real disposable income (households)	2.4	0.6	-1.8	-2.1
Personal savings ratio (level)	15.4	16.2	14.8	15.0

	1980	1981	1982
Public finances	(In percent of GDP)		
General government 4/			
Expenditure	57.5	62.4	63.5
Revenue	45.7	46.3	47.9
Financial balance	-11.8	-16.1	-15.6
(In percent of gross private savings)	56.9	74.9	75.1
Central government financial balance 5/	-8.5	-12.5	-12.9
Balance of payments 6/	(In billions of Belgian francs)		
Trade balance 7/	-109	-109	-93
Services balance	3	2	27
Net private transfers	-11	-15	-11
Net official transfers	-27	-33	-45
Current account balance	-144	155	-122
(In percent of GDP)	(-3.9)	(-4.0)	(-3.0)
Net private capital flows	1	-201	-162
Net public capital flows	154	258	256
Change in net reserves of National Bank	27	-96	-38

1/ Staff projections and/or estimates.
2/ Annual averages
3/ Ratio of deflator of exports of goods and services to deflator of imports of goods and services; national accounts definition.
4/ National accounts definition.
5/ Administrative basis.
6/ Belgium/Luxembourg Economic Union (BLEU).
7/ Including third country trade.

I. Developments in the Domestic Economy

1. General overview

The year 1982 constituted in many ways a watershed for economic policy and economic developments in Belgium. On February 21, 1982 the Belgian franc was devalued by 8 1/2 percent and a partial wage and price freeze was introduced. These two measures constituted the main elements of a policy package, the prime aim of which was the restoration of price and cost competitiveness of Belgian producers under conditions of stable growth and low unemployment. 1/ In the past, the maintenance of international competitiveness had required the exploitation of productivity gains from labor shedding and from the elimination of marginal firms. The related increase in unemployment and loss of tax revenue had increasingly burdened the public finances, raising the public sector deficit to one of the highest in industrial countries. At the same time, the deteriorating profitability of the enterprise sector, notably the tradable goods sector, increasingly reduced the incentive to supply, with severe consequences for the external balance. In view of these developments, the policy measures of February 1982 attempted to simultaneously restore international competitiveness and to provide incentives to supply through increased profitability of enterprises. The measures taken by the authorities were believed to bring about a swift and substantial improvement in the external balance. They were also thought to increase output and employment, and to reduce the public sector deficit, although with a certain time lag.

In the event, the current account deficit of Belgium dropped from 4 1/2 percent of GDP in 1981 to slightly below 4 percent in 1982. 2/ The bulk of the improvement occurred in the services balance but the import cover ratio also increased and the deterioration in the terms of trade came to a halt. 3/ Examined from the financial balance perspective, the improvement in the current account was primarily the result of a massive redistribution of income from households to enterprises and--to a lesser degree--to General Government. The related drop in real disposable income of households curtailed their consumer

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1/ Other measures of the policy package included tax concessions to stimulate purchases of corporate shares; a reduction from 48 percent to 45 percent in the standard rate of corporate income tax; a reduction by about 9 1/2 percent in gas and electricity rates for industry; and a number of other measures, most of which were aimed at improving the earnings position of enterprises and, directly or indirectly, at stimulating production and employment.

2/ Derived from national accounts data on sectoral financial balances. For a detailed analysis of current account developments by way of an examination of data on sectoral financial balances, see Appendix I.

3/ For a detailed description of the effects of the February policy package, notably the devaluation, see Appendix II.

and capital spending--notwithstanding a large decline in the savings ratio--without generating an equivalent spending response of the enterprise sector or the public sector. Thus, enterprises' and public sector financial positions improved by substantially more than households' position deteriorated and, on aggregate, the nation's savings/investment balance improved. The improvement in the current account accelerated in early 1983 as households' real disposable income continued to decline and the fall in households' savings rate came to a halt while enterprises' demand remained sluggish and government spending slowed. Preliminary data suggests that Belgium's current account deficit will in 1983 be less than half that of 1982.

Economic activity, as measured by the growth of output, picked up in 1982. Real GNP increased by 0.7 percent and real GDP by 1 percent. 1/ The relative performance of the Belgian economy improved by a considerable margin, as the growth differential with the average of industrial countries turned from -2.7 percentage points in 1981 to 0.3 percentage points in 1982. Still, unemployment continued to rise sharply, notwithstanding a decline in the participation rate. In late 1982, the Government therefore introduced a package of measures aimed at reducing unemployment through work-sharing.

Inflation accelerated in 1982 despite the prevalence of price control measures. Unlike in earlier years, wage cost-push inflation was not a factor for the acceleration in the inflation rate. Instead, increases in prices reflected primarily the effects of high import prices and increases in profit rates. In the first half of 1983, the inflationary momentum slowed somewhat but inflation rates remained considerably higher than in most competitor countries.

2. Developments in demand and supply

After having fallen by 1.2 percent in 1981, GNP increased by 0.7 percent in 1982 (Table 1). Total domestic demand was neutral in 1982, in contrast to a strong negative contribution to growth in 1981 (-4.2 percent). The foreign balance continued to grow in 1982. However, its contribution to growth (0.8 percent) was sizably lower than in 1981 (3 percent). One of the reasons for this decline was the sharp increase in net factor payments abroad which reflected the strong growth of net foreign indebtedness of Belgium in 1981 and 1982 and the related need to service the foreign debt. As a consequence of increased net factor payments abroad, GNP grew less (0.7 percent) than GDP (1 percent) in 1982. 2/

1/ There remains some uncertainty about the measurement of private consumption. In case of a downward revision of the order that has been mentioned would result in a zero growth of GNP.

2/ For an evaluation of changes in the structure of demand, see the calculation of shares of demand components in Table 1.

Domestic demand remained weak in 1982 although the sharp decline of 1981 was not repeated in 1982. Private consumption increased by 1.1 percent after a decline by 1.4 percent in 1981 which had been the first fall in 25 years. In 1981, the drop in private consumption had been primarily due to special factors and to a significant strengthening of the contingency motive for saving. Against this backdrop, the increase in 1982, was modest. Still, given the drop in real personal disposable income by 1.8 percent (Table 3) even this modest growth necessitated the decline in the personal savings ratio to the lowest level in the last ten years. The drop in real disposable income also affected the demand for residential construction. After having declined by a spectacular 40 percent in 1981, residential construction fell by an additional 6.5 percent in 1982. Excess capacities, high costs of financing, rising unemployment and adverse demographical trends were other reasons for the weakness of demand for housing. They were obviously not compensated by the reduction, effective March 1, 1982, in the value-added tax on residential construction from 17 percent to 6 percent. 1/

Reflecting the precarious state of the public finances and the commitment of the authorities to bring the growth of public sector spending under control, aggregate public sector demand at constant prices decreased considerably in 1982. The brunt of the reduction in public sector spending was carried by public investment which fell by 6.3 percent in 1982, after having already dropped by 7.3 percent in 1981. Investment spending of local authorities was particularly weak. Public consumption fell for the first time ever, reflecting a sizable reduction in purchases of goods and services and a virtual stop of the growth of public sector employment. Although its decline was less than initially planned, the interruption of the steady upward trend of public consumption is a significant break from the past.

Private productive investment turned around in 1982 from a drop of 3.4 percent in 1981 to a stabilization at zero percent in 1982. The investment performance of the private productive sector fell nevertheless short of what could have been expected from the sharp improvement in the earnings position of the enterprise sector. 2/ In light of high levels of unused capacities and continued uncertainty about prospective developments in demand, firms remained cautious in their investment decisions. Against this backdrop, firms preferred to strengthen their financial position in an effort to improve their current and future self-financing ability. Investments took place primarily in the service sector and in those industrial sectors where international competition required it. As in 1981, no growth impulse derived from stockbuilding in 1982.

1/ This reduction did not affect social housing for which the value-added tax was already 6 percent before March 1982.

2/ In 1982, the gross operating surplus of corporate enterprises increased by some 17 percent, raising its share in GDP from 10.8 percent in 1981 to 11.7 percent in 1982. For a more detailed discussion see section on income distribution.

Planned reductions in inventories in some sectors reflected falling demand. They were partly offset by an involuntary buildup of inventories in other sectors. In yet other sectors, stocks were increased somewhat after they had apparently reached their technical minimum.

Export growth 1/ dropped significantly in 1982 despite the February devaluation. Continued increases in market shares, albeit at a reduced rate, were largely offset by the sluggish growth of partner countries' import demand. 2/ In the event, exports of goods and services grew by 2.6 percent in 1982, compared with 8.7 percent in 1981. Imports of goods and services, which had increased by 4 percent in 1981, continued to grow in 1982, albeit at a more moderate rate (1.6 percent). One of the reasons for the relative stability of import growth was the sharp increase of factor payments abroad mentioned earlier; other reasons were the growth overhang from 1981 and speculative purchases in the first half of 1982 when the exchange rate situation remained unsettled. Import growth was apparently negative in the second half of the year. 3/

In the first half of 1983, domestic demand appears to have weakened again. Private consumption was particularly depressed on account of the continued and accelerated decline of real disposable income of wage earners which was accompanied by a renewed strengthening of the contingency motive for savings. Retail sales, which represent about one half of private consumption, were down sharply (Chart 1). Purchases of services appear to have stabilized somewhat. Demand for residential construction--as measured by the growth of building permits--picked up somewhat in mid-1983 after having dropped very strongly in the first quarter of the year. The usual time lag between permits and construction starts points to a continued weakness of residential construction until late 1983. Public sector investment declined further because, in particular, the local authorities substantially reduced their expenditure for financial reasons. Judging by the declarations for value added tax purposes, private productive investment appeared to stabilize in real terms, with the growth of nonindustrial investment still outpacing that of industrial investment, albeit at a reduced rate. Foreign demand, meanwhile, picked up sharply in the second quarter of 1983, after a more moderate rise in the first quarter ahead of the EMS realignment in March.

1/ The discussion in this section concentrates on data on exports and imports of goods and services including factor payments. For an evaluation of data which exclude factor payments, see the memorandum items in Tables 1 and 2.

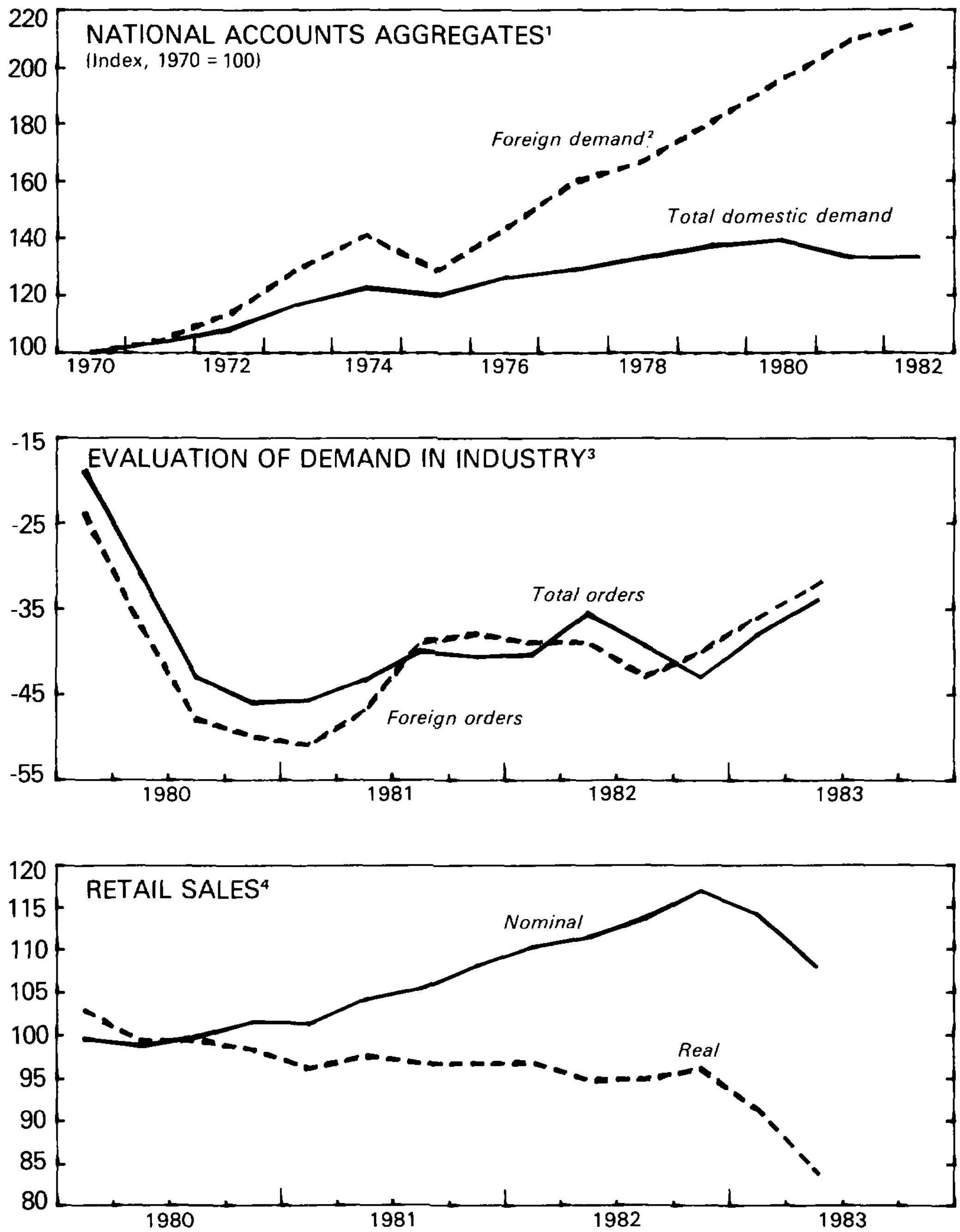
2/ For an evaluation of export performance, see Chapter IV on external developments.

3/ No quarterly or semi-annual data exist for imports in the national accounts definition. However, measured in the customs definition and excluding service imports, the volume of imports increased by 5.3 percent in the first half of 1982, but declined by 2.2 percent in the second half (year-over-year).

CHART 1

BELGIUM

SELECTED INDICATORS OF DEMAND



Sources: OECD, *Main Economic Indicators;* National Bank of Belgium, *Bulletin;* and International Monetary Fund, *International Financial Statistics.*

[1] In constant prices, 1975=100.

[2] Exports of goods and services.

[3] Difference between firms reporting order books above (+) or below (-) normal, as percentage of replies to survey. Industry, excluding construction.

[4] Index, 1980=100; seasonally adjusted.

Domestic import demand, in turn, was affected by diverging influences: households' demand appeared to have fallen in line with private consumption--with energy products experiencing a particularly steep decline. On the other hand, imports of intermediate products increased as enterprises stepped up production and replenished their inventories.

In 1982, some established trends in value added deflators were reversed. For the first time since 1974--and for the second time only since the late 1960s--the relative value added deflator of manufacturing rose faster than the deflator for GDP while the deflator for public services rose by less (Table 4). For the manufacturing sector, this development must be primarily attributed to the February 1982 policy package. The growing disincentive for resource transfer to the manufacturing sector was thus halted in 1982.

Recent developments in industrial output point to a continued weakness of construction activity and some strengthening in manufacturing output (Table 5 and Chart 2). In the first quarter of 1983, the growth of output of consumer durable goods was quite buoyant (6 percent) exceeding the average growth in previous years (0.6 percent) by a large margin. The same applies to the production of investment goods which increased by 3.6 percent compared with an average growth of 0.6 percent between 1975 and 1982. Industrial output dropped by 4.4 percent if construction is included, but increased by 2.6 percent if construction is excluded. This performance compares with average growth rates between 1975 and 1982 of -0.4 percent (including construction) and 1.6 percent (excluding construction).

After rising briefly in 1976, the rate of utilization of the nation's productive capacities 1/ has continually declined (Chart 3). In 1982, the rate of decline slowed but some 11 percent of potential output was nevertheless left unused. The picture that emerges from business surveys in the manufacturing sector is quite different as no continuous downward trend is indicated for the period under consideration. However, the movements of capacity utilization in manufacturing are similar to the fluctuations of the overall capacity utilization measure relative to its trend (Chart 3).

3. Labor market developments and policies

a. Labor market developments

Since the early 1970s, the labor market situation has developed less favorably in Belgium than in most other industrial countries. In 1970, the unemployment rate in Belgium equaled roughly the average for the EC countries and the seven largest industrial countries (some 2 percent). However, in 1982, the unemployment rate in Belgium (13.7 percent) exceeded that of the EC (9.4 percent) and of the seven largest industrial countries (8.1 percent) by a considerable margin.

1/ The rate of overall capacity utilization is measured by the ratio of actual real GNP to an estimate of potential real GNP.

The structure of employment has shifted considerably since the early 1970s. Increases in public sector employment have tended to offset to a considerable extent the fall in private employment (Table 6). Between 1974 and 1982, public sector employment increased by a cumulative 20 percent while total private sector employment dropped by 9 percent, lowering the share of private employment in total employment from 86.2 percent in 1974 to 82.4 percent in 1982. Within the private sector, employment dropped after 1974 in all subsectors, except in the service sectors (Table 7). The decline was most significant in industry (26 percent), where manufacturing employment even declined by 27 percent.

After many years of large increases, there appears to have been a moderate decline in participation rates in recent years, especially since 1980. 1/ The observed acceleration in the unemployment rate therefore has been primarily a reflection of the sharp drop in private sector employment on account of cyclical and cost factors. Furthermore, the decline in employment in the private sector was, after 1980, not to the same extent offset by an increase in public sector employment as in earlier years (Table 6). As in 1981, the drop in employment was in 1982 particularly strong in the construction sector. By contrast, labor shedding slowed in industry, and in the first half of 1983, employment in the manufacturing sector appears to have stabilized somewhat for the first time since 1973. An improvement in labor market conditions in at least some selected sectors is also suggested by the steep increase in unfilled vacancies (Chart 3), although the special employment programs may have exercised a strong positive influence on these data.

b. Labor market policies

The deterioration in the labor market since the mid-1970s has given rise to a great number of comprehensive employment promotion schemes and individual measures. They initially focused on the promotion of (a) early retirement; (b) a requirement of firms to absorb a large part of school-leavers into training schemes; and (c) the employment of eligible unemployed in special temporary employment schemes (cadre spécial temporaire) which provided public interest jobs in both government and in nonprofit organizations. On top of these three main employment-support schemes, the Government has at times taken sector-specific measures and has granted selected tax

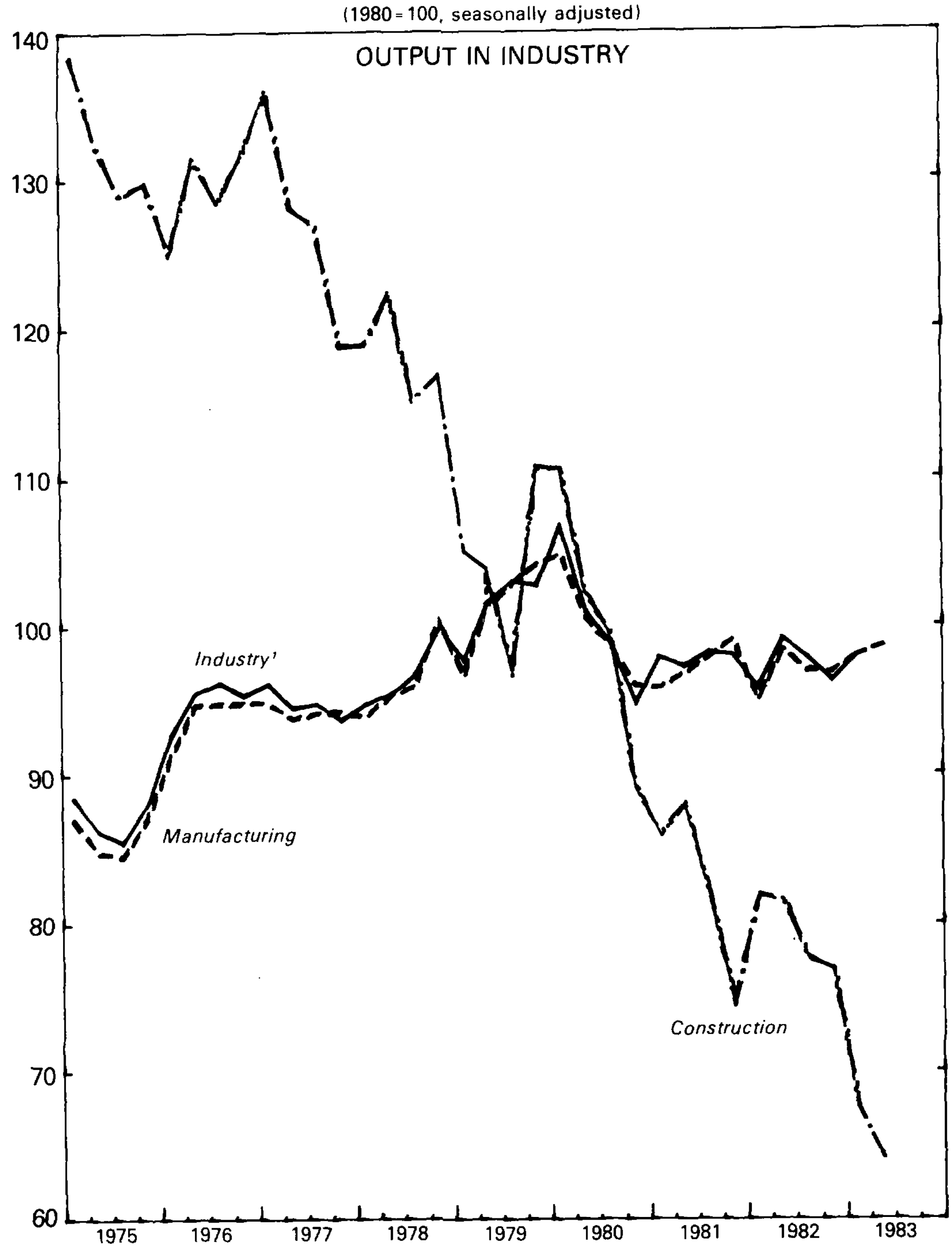
1/ One element of the apparent decline in participation rates is the growth in early retirement schemes. Since 1976, they have continually reduced the measured rate of unemployment in terms of insured workers (Table 6; Memorandum item). In 1982, this rate would have reached roughly 20 percent without early retirement. The overall rate of unemployment would have risen to about 16 1/2 percent.

CHART 2

BELGIUM

SELECTED INDICATORS OF SUPPLY

(1980 = 100, seasonally adjusted)



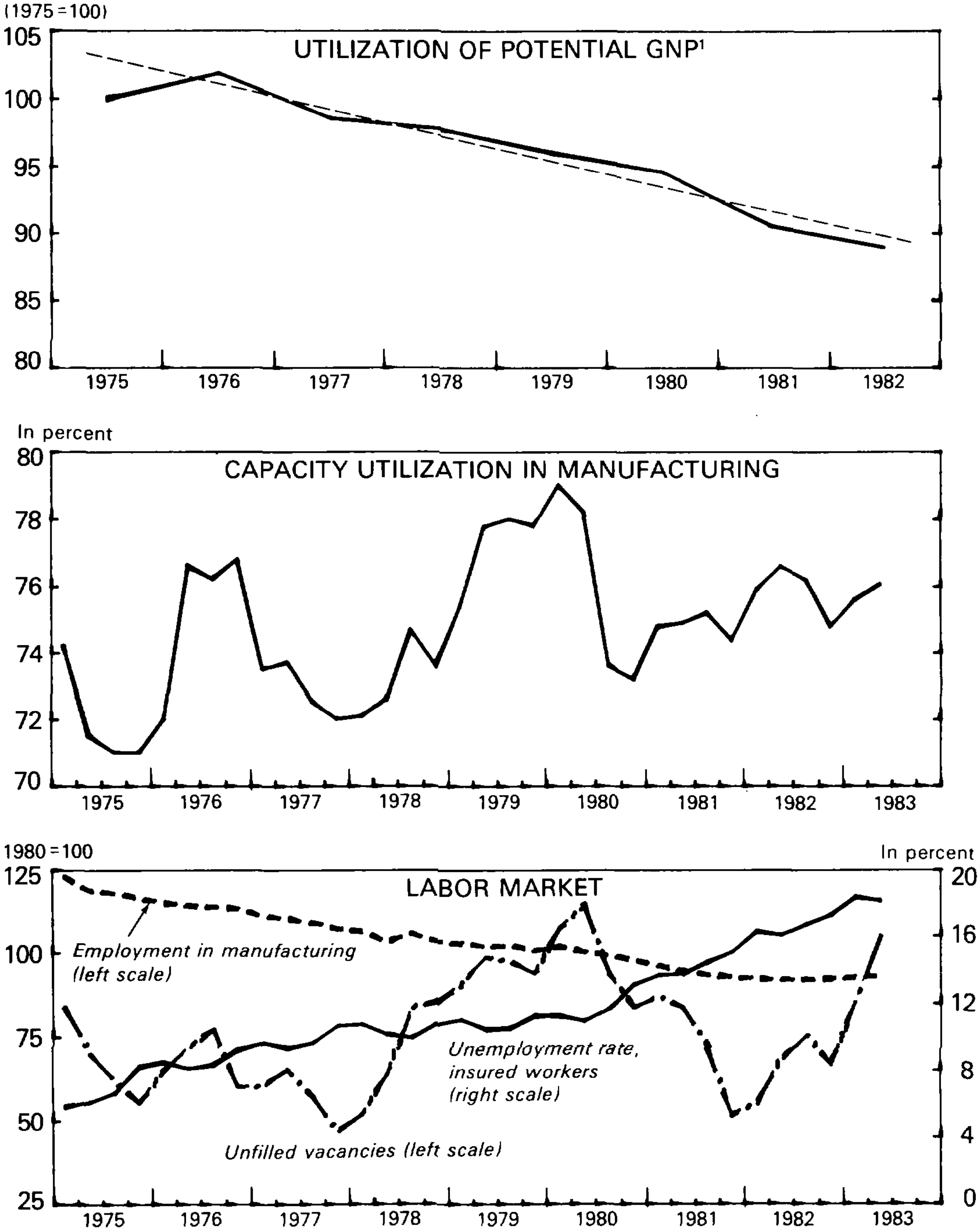
Sources: International Monetary Fund, *International Financial Statistics;* OECD, *Main Economic Indicators.*

[1] Excluding construction.

CHART 3

BELGIUM

UTILIZATION OF PRODUCTIVE CAPACITIES



Sources: International Monetary Fund, *International Financial Statistics;* OECD, Main Economic Indicators; and staff estimates.
[1] Ratio of index of observed real GNP to index of potential real GNP; 1975=100.

concessions in an attempt to induce enterprises to increase employment. 1/ In 1982, the prime attention of employment support measures turned toward long-term unemployment. A program called the "third circuit" (troisième circuit du travail) was introduced which provided fixed-term employment contracts to people eligible for unemployment benefits who had been out of job for more than two years. Although giving specific attention to long-term unemployment, the Government continued in 1982 to support youth training and part-time employment schemes.

Observing the continued deterioration in the labor market, the Government proposed in late 1982 to the social partners a work-sharing scheme, to be effective in 1983. The scheme involved a prolongation of the suspension of full indexation beyond the initially set expiration date of end-1982. This extension of wage controls was expected to lower wage and salary increases some 3 percent below the level that would have materialized in the case of a return to indexation. In return for the wage restraint, firms would be obliged to reduce working hours by 5 percent and to increase employment by 3 percent by the end of 1983. 2/ A special system applied to small- and medium-sized enterprises which, as a sector, had to raise employment by at least 2 1/2 percent. 3/ Any reduction in short-time was considered as additional employment. Firms which raised employment without reducing work-time would be rewarded by a reduction in social security contributions for up to 2 percent of additional employment, and by other fiscal benefits. Agreements on the work-sharing scheme were to be reached between the social partners without the direct involvement of the Government. Failing a national agreement, agreements were to be sought at a sectoral and, subsequently, at the enterprise level. In the absence of an agreement, the benefits deriving from wage moderation had to be transferred to a newly created Employment Fund (Fonds pour l'Emploi). 4/

In early April 1983--the deadline set by the Government--a great number of agreements had been reached in the private sector covering more than 3/4 of its labor force. Agreements displayed a high degree of pragmatism. Sector-specific and even firm-specific factors were flexibly incorporated into the agreements. As a result, the average decline in work hours will be more likely 2 1/2 percent instead of the envisaged 5 percent and the additional employment may only be 2 to 2 1/2 percent instead of the initial target of 3 percent. Furthermore, the implementation lag appeared to be longer than anticipated. The bulk

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1/ In a broader sense, the increase in capital transfers to enterprises from 2 1/2 percent of GDP in 1975 to 4 1/2 percent in 1982 can perhaps also be considered an employment support measure, if only an indirect one.

2/ The combination of work-sharing (Royal Decree No 179) and wage restraint (Royal Decree No. 180) became known as the "3-5-3" formula.

3/ This sector accounts for about 45 percent of private sector employment.

4/ Royal Decree No. 181.

of the employment effect can therefore not be expected before 1984. The total employment effect was initially estimated by the Government at 40,000 by the end of 1983 and at 70,000 at the end of 1984. Agreements in the public sector were believed to raise employment by 10,000 above the level of the reference period (1979). This would have roughly offset the planned reductions in public sector employment, leaving employment in the public sector unchanged in net terms. Current estimates suggest an ultimate increase in private sector employment by some 45,000, of which 10,000 by the end of 1983. For the public sector, recent strike-related agreements may result in a moderate increase in public sector employment above the initially planned level.

4. Costs, productivity, and competitiveness

Wage restraint measures have dominated developments in costs and competitiveness. Effective February 2, 1982, the indexation of wages and salaries was suspended for all earnings in excess of BF 27,357 until end-May 1982. Between June 1 and December 31, 1982 a flat sum system was applied whereby earnings exceeding the minimum wage were raised by BF 536 (2 percent of the minimum wage) every time an adjustment would have taken place under the old indexation scheme; earnings up to the minimum wage remained indexed. In November 1982, the Government decided to extend the wage restraint measures until about the middle of 1983. A return to full indexation was intended after the index trigger had been passed twice in 1983. However, the new index will be calculated as a smoothed average over four months instead of the monthly calculation method applied earlier. Furthermore, a general policy of wage restraint will remain in operation through the end of 1984 (the so-called "competitive" or "double norm", which requires that domestic wage increases, including those due to indexation, do not exceed the weighted average of Belgium's seven main partner countries). Finally, there will be no catching-up of earnings lost during the past period of wage restraint, and, in any event, no wage increases will be granted above the ones indicated by the indexation mechanism.

In the event, the wage restraint measures substantially reduced the growth of hourly earnings in 1982 and early 1983 (Table 8). Overall production costs 1/ continued to grow at a high rate on account of a sharp increase in the cost of intermediate inputs which reflected, above all, the large effective devaluation of the Belgian franc.

Productivity growth picked up in 1982, with the exception of the manufacturing sector. Nevertheless, international competitiveness of the manufacturing sector increased in 1982 at an even higher rate than in 1981 (Chart 4). This development continued in the first quarter of 1983, slowed in the second, and continued thereafter.

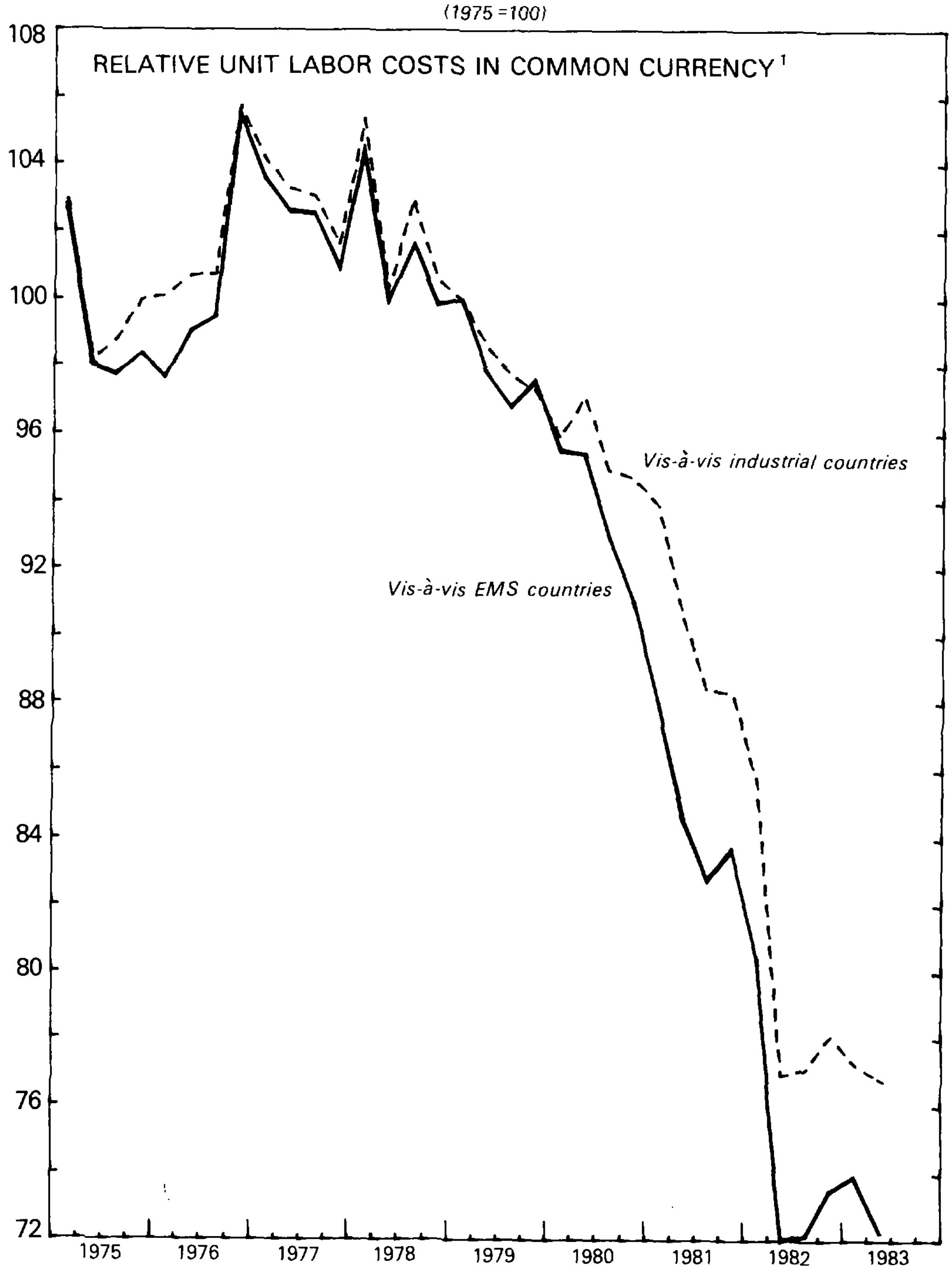
1/ Estimated as a weighted average of costs of intermediate input and labor costs.

CHART 4

BELGIUM

INDICATORS OF COMPETITIVENESS

(1975 = 100)



Source: Staff calculations

[1]Manufacturing sector.

5. Prices

Inflation accelerated in 1982 despite the price control measures introduced by the Government in connection with the February devaluation (Table 9 and Chart 5). 1/ However, the price control measures appear to have prevented an even stronger acceleration of inflation. Nevertheless, price developments in Belgium differed from those in partner countries where inflation rates tended to decline by substantial margins. The contribution of selected factors--such as import prices and wage costs--to price developments in Belgium changed considerably in 1982, compared with the preceding years. Although the effective exchange rate of the Belgian franc depreciated sharply in 1982, imported inflation was not a contributing factor to the acceleration of inflation in Belgium: the growth of import unit values remained unchanged from a year earlier as the price-raising effect of the renewed and accelerated depreciation of the Belgian franc was fully offset by the deceleration in the growth of import prices denominated in foreign currency, notably raw material prices. Furthermore, unlike in earlier years, wage developments did not add to cost push inflation, as the comprehensive wage restraint measures of the Government resulted in a steep fall in the growth of labor costs. The increase in the rate of inflation therefore mirrored the pricing policy of domestic producers and distributors and was reflected almost in full in an increase in the profit margin of enterprises. This development appears to have strengthened in 1983: the deceleration of costs does not seem to have been fully reflected. This applies in particular to prices of the domestic sheltered sectors. By contrast, the exposed sectors were faced with a slowing of price increases of foreign competitors which limited their room for profit margin increases. As a result, the relative value added deflator of the exposed sector appears to have fallen again in 1983 after its exceptional increase in 1982.

The rate of inflation, as measured by the GNP deflator, increased by almost 2 percentage points to 7 percent in 1982 (Table 9). By contrast, the growth of the domestic demand deflator dropped by a full percentage point from a year earlier. The difference in the development of the two deflators is primarily a reflection of the very sharp rise in the growth rate of the export deflator 2/ which suggests that exporters have almost fully used the room for price increases offered by the effective depreciation of the Belgian franc. 3/ Measured by the consumer

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1/ All prices were frozen until end-May at their February 15, 1982 level. From April 1 onward, selective price increases were granted mainly to pass on higher import costs. At the end of May, price controls were modified and extended to end-1982. In December 1982, the Government, using its special powers, renewed the selective price controls until end-1983, and in late 1983 it announced that price controls would remain in effect throughout 1984.

2/ The growth rate of the export deflator increased from 9.3 percent in 1981 to 13.4 percent in 1982.

3/ Apart from its impact on inflation, this pricing policy was a key factor for the increase in profitability (see below).

price index, inflation increased by little more than a percentage point to 8.7 percent in 1982. Food and nonfood prices rose faster than prices of services and rents. The increase in nonfood prices would have been considerably higher, had not the growth of energy prices dropped by about one third. Having surged after the lifting of the price freeze in the second quarter of 1982, inflation slowed somewhat in the second half of the year, although not by as much as would have been permitted by cost factors. This development continued in the first half of 1983, and the rate of inflation therefore remained considerably higher in Belgium than in most competitor countries (Chart 5).

6. Income distribution and profitability of enterprises

The package of policy measures taken in February 1982 has brought about important breaks in established income distribution trends. The wage restraint measures interrupted the continuous upward movement of the share of wages and salaries in GDP from 57.2 percent in 1975 to 59.7 percent in 1981; in 1982 the share dropped to 58.6 percent (Table 10 and Chart 6). 1/ By contrast, the share of corporate enterprises' gross operating surplus (before subsidies) increased from 9.1 percent in 1981 to 10.1 percent in 1982, after having dropped almost continuously between 1975 and 1981 from an initial level of 12.4 percent. The turnaround in enterprises' gross operating surplus rested primarily on an increase in the profit rate by 25.5 percent in 1982 (Table 11) on account of the moderate increase in wage costs and the strong growth of sales prices, notably export prices, permitted by the devaluation. The effect of volume growth on profits was negligible.

The share of households' disposable income in GDP dropped in 1982 much in line with the wage and salary component. The increase in the component "Other earned income" of households reflected a continued strong growth in property income which was accompanied by a sharp pickup in incomes of small-scale enterprises which are included in the household sector. The growth of current transfer payments to households slowed in 1982 on account of a deceleration in the growth of unemployment and of policy measures which reduced social transfers. The growth of direct taxes accelerated from 5 to 15 percent and social security payments also grew at an accelerated pace. In net terms, households therefore transferred in 1982 an increased part of their primary income to the public sector, whereas in the two preceding years the growth of transfers received by households had exceeded that of their direct taxes and social security contributions. In the event, net disposable income of households dropped from 78 percent of GDP in 1981 to 76.9 percent in 1982. The share of corporate enterprises' disposable income in GDP increased in 1982 by a 0.5 percentage point to 7 percent, which was only half the increase in their operating surplus because net transfers to the public sector also rose considerably. By contrast, corporate enterprises' net payments of interest and dividends grew only slowly in

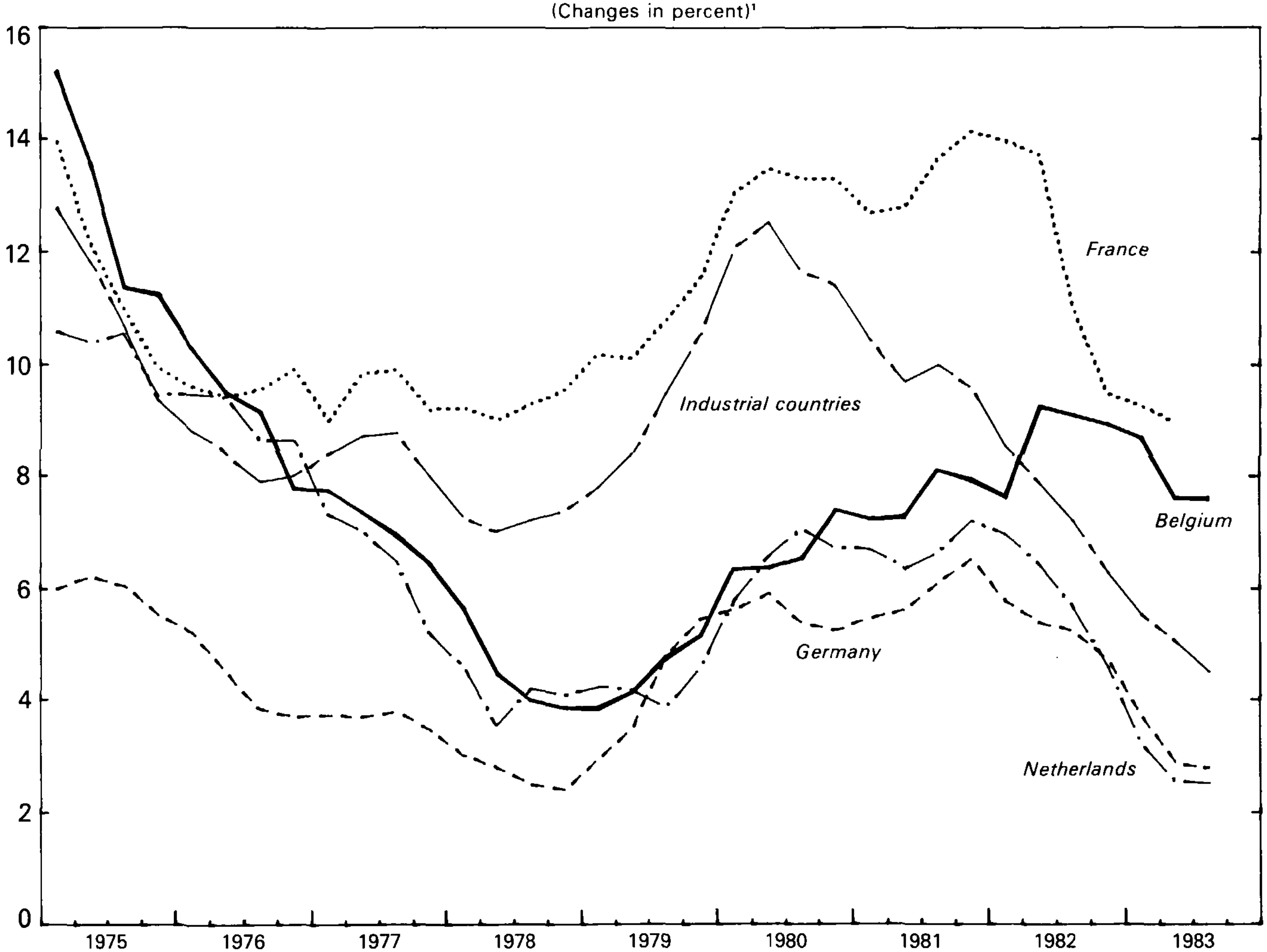
1/ Apart from the wage restraint measures, the decline in this share was also affected by the drop in employment.

CHART 5

BELGIUM

INFLATION RATES

(Changes in percent)[1]



Source: International Monetary Fund, *International Financial Statistics.*

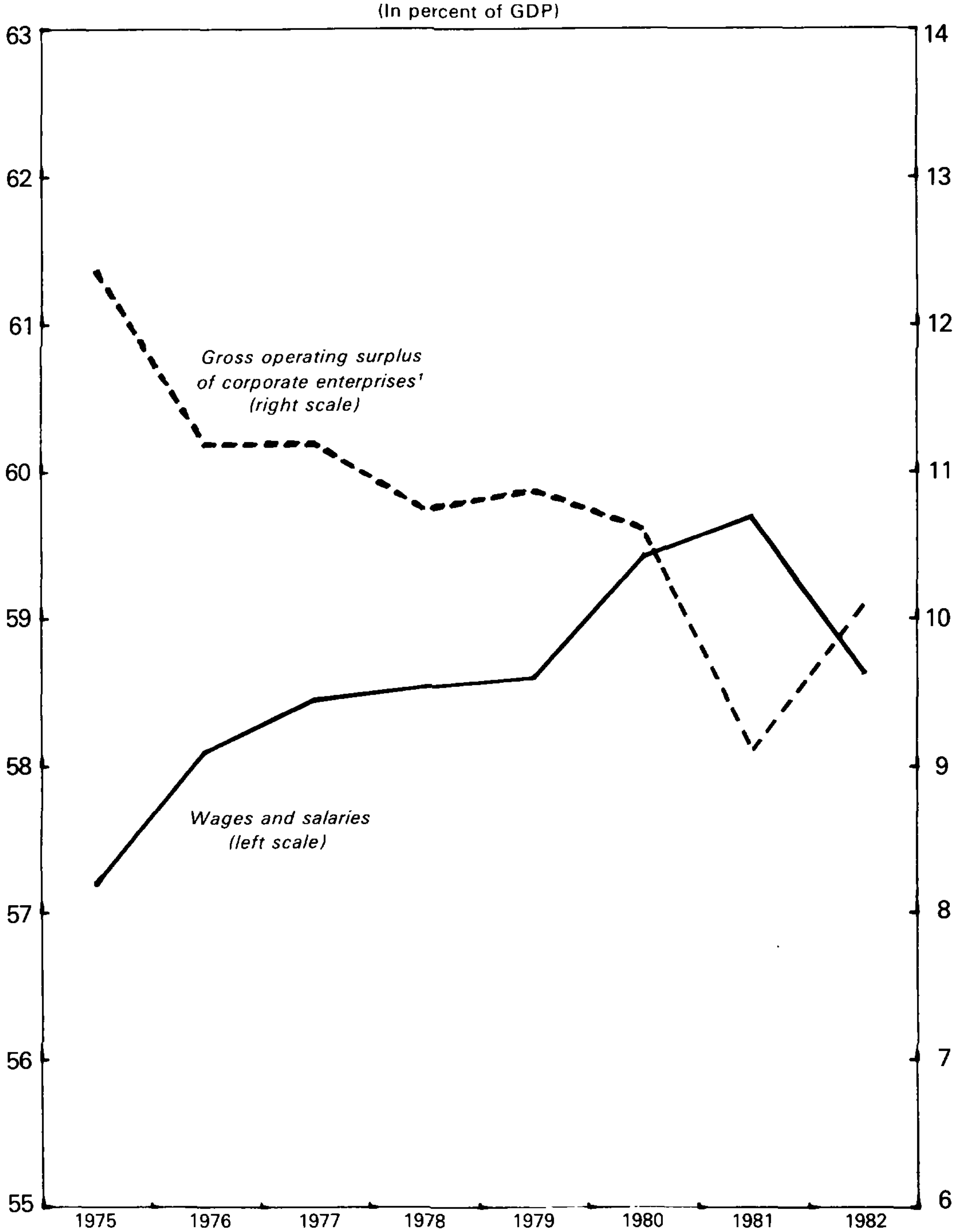
[1]Compared with same quarter of preceding year.

CHART 6

BELGIUM

DISTRIBUTION OF INCOME

(In percent of GDP)



Sources: National Bank of Belgium, *Annual Report 82;* and staff calculation.

[1]Before subsidies.

1982 because enterprises, on the one hand, gave a high priority to building up reserves and, on the other hand, earned higher income on their own financial investments. General government's share of gross primary income in GDP continued to increase in 1982, if interest payments on the public debt are excluded. 1/ However, it dropped sharply again after inclusion of interest payments, reflecting the strong growth of public sector debt and high interest rates. Nevertheless, after having fallen consistently in the past, the share of Government disposable income in GDP increased in 1982 on account of the strong growth of net transfer payments to the Government (i.e., direct taxes minus current transfers) by both households and enterprises.

Enterprises' profitability developed favorably in 1982 as all measures of profitability recorded a sizable increase (Table 11). The share of the gross operating surplus (before subsidies) of corporate enterprises in value added increased by 1.3 percentage points to 14 percent, and the rate of return on capital increased by a 0.7 percentage point to 7.5 percent. The improvement in the rate of return on capital was even more significant if measured in relative terms, i.e., compared with the real rate of return on financial investments. After having dropped continuously from 12.3 percent in 1975 to close to zero in 1981, the relative rate of return of all corporate enterprises increased in 1982 to 2.7 percent. The improvement in rates of return was even more pronounced in the manufacturing sector. However, all rates of return remained in 1982 still very much below historical rates. 2/ This fact goes far in explaining the attentism of enterprises in their investment decisions.

For the manufacturing sector, the data in Table 11 show that the continous and large increase in the unadjusted share of wage costs in value added came to a halt in 1982. Other things equal, enterprises in manufacturing could thus, for the first time, earn a profit without the need to increase productivity through labor shedding. After adjustment for labor productivity, the share of wage income in value added of the manufacturing sector dropped by 2.3 percent, the largest fall ever recorded.

1/ As in earlier years, the increase was primarily due to the strong growth of interest and dividends received from the National Bank of Belgium and from financial intermediaries fully or partly owned by the Government. Furthermore, indirect taxes grew stronger (8 percent) than in the preceding years (some 5 percent in 1980-81).

2/ For the period 1971-74, the average relative rate of return on capital was 7 1/2 percent for all corporate enterprises, and 13 3/4 percent for manufacturing.

Table 1. Belgium: Aggregate Demand in Constant Prices 1/

	Changes in Percent								Shares in GNP		
	1975	1976	1977	1978	1979	1980	1981	1982	1971	1975	1982
Private consumption	0.4	5.1	2.4	3.0	4.7	2.1	-1.4	1.1	59.1	61.1	63.1
Public consumption	4.9	4.0	2.7	6.0	2.6	1.6	0.9	-1.6	15.8	16.7	17.1
Fixed investment	-1.6	3.0	-0.1	2.7	-2.0	5.0	-14.5	-2.6	21.9	22.0	17.3
Public	9.8	5.5	1.2	-2.5	5.5	8.7	-7.3	-6.3	4.7	3.8	3.4
Residential	-3.3	15.7	1.8	6.3	-12.6	-1.0	-40.3	-6.5	4.9	6.2	3.3
Private productive	-3.9	-4.4	-1.8	2.3	2.5	7.2	-3.4	--	12.3	12.1	10.6
Final domestic demand	0.7	4.4	1.9	3.4	2.9	2.6	-3.7	-0.1	96.8	99.8	97.5
Stockbuilding 2/ 3/	-2.9	0.9	0.1	--	0.5	-0.9	-0.4	--	1.3	-0.5	-0.2
Total domestic demand	-2.2	5.4	2.0	3.4	3.4	1.7	-4.1	-0.1	98.1	99.3	97.3
Exports of goods and services	-8.9	11.2	11.3	4.3	8.3	7.6	8.7	2.6	46.2	49.7	73.0
Imports of goods and services	-9.7	10.5	14.4	4.7	10.5	5.9	4.1	1.6	44.3	49.0	70.3
Foreign balance 2/	0.4	0.4	-1.5	-0.3	-1.4	0.9	3.0	0.8	1.9	0.7	2.7
GNP	-1.8	5.7	0.5	3.2	2.1	2.6	-1.2	0.7	100.0	100.0	100.0
Memorandum items:											
GDP 4/	-1.8	5.6	0.7	3.3	2.5	3.1	-1.1	1.0	99.3	99.5	100.9
Exports of goods and services 5/	-8.9	12.6	12.3	3.7	7.9	4.5	3.7	2.0	43.0	45.8	62.8
Imports of goods and services 5/	-9.7	12.1	14.9	4.0	9.5	2.1	-1.4	0.2	41.8	45.6	59.1

Sources: National Institute of Statistics, Statistical Bulletin; data supplied by the National Bank of Belgium; International Monetary Fund, International Financial Statistics; and staff calculations.

1/ 1975 = 100.
2/ Contributions to growth in percent.
3/ Including statistical discrepancy.
4/ At market prices.
5/ Excluding factor incomes.

Table 2. Belgium: Aggregate Demand in Constant Prices

(Percentage point contributions to the growth of GNP at 1975 prices)

	1975	1976	1977	1978	1979	1980	1981	1982
Private consumption	0.3	3.1	1.5	1.9	2.9	1.3	-0.9	0.7
Government consumption	0.8	0.7	0.5	1.0	0.5	0.3	0.2	-0.3
Gross fixed investment	-0.4	0.7	--	0.6	-0.4	1.0	-3.0	-0.5
Public	0.3	0.2	--	-0.1	0.2	0.4	-0.3	-0.2
Residential	-0.2	1.0	0.1	0.4	-0.9	-0.1	-2.4	-0.2
Private productive	-0.5	-0.5	-0.2	0.2	0.3	0.8	-0.4	--
Final domestic demand	0.7	4.4	1.9	3.4	2.9	2.6	-3.8	-0.1
Stockbuilding 1/	-2.9	0.9	0.1	--	0.5	-0.9	-0.4	--
Total domestic demand	-2.2	5.3	2.0	3.4	3.5	1.7	-4.2	0.1
Exports of goods and services	-4.8	5.6	5.9	2.5	4.8	4.7	5.6	1.9
Imports of goods and services 2/	5.2	-5.2	-7.4	-2.7	-6.2	-3.8	-2.7	-1.1
Foreign balance	0.4	0.4	-1.5	-0.3	-1.4	0.9	3.0	0.8
GNP	-1.8	5.7	0.5	3.2	2.1	2.6	-1.2	0.7

Memorandum items:

Table 3. Belgium: Personal Income, Consumption and Savings

(Changes in percent; current prices)

	1975	1976	1977	1978	1979	1980	1981	1982
ion of employees	14.8	15.4	8.7	7.6	6.9	8.8	4.8	6.0
rned income 1/	9.4	12.5	5.9	7.7	6.5	7.7	9.6	11.9
ransfers	29.0	16.2	12.3	9.6	8.9	7.9	11.9	9.4
sonal income	15.8	14.9	8.7	8.0	7.2	8.4	7.3	8.1
axes	29.1	12.9	18.2	16.2	9.4	5.0	4.7	15.4
ecurity premiums	21.0	12.9	10.0	4.5	7.4	8.0	6.2	7.7
posable income	12.9	15.5	6.8	7.0	6.7	9.3	8.2	6.7
disposable income 2/	0.2	5.8	-0.3	2.4	2.1	2.4	0.6	-1.8
ion	13.2	13.2	9.6	7.1	8.5	8.9	7.2	8.6
atio 3/	17.1	18.7	16.6	16.6	15.2	15.4	16.2	14.8
m items:								
GNP	10.6	13.7	7.8	7.5	6.3	7.0	4.0	7.8
r price index	12.7	9.2	7.1	4.5	4.5	6.7	7.6	8.7

: National Institute of Statistics, Statistical Bulletin; and staff calculations.

cludes incomes of small enterprises not included in the enterprise sector, incomes
employed, and property incomes, including incomes on financial assets.
posable income deflated by the consumer price index.
a percentage of disposable income.

Table 4. Belgium: Value Added of Sectors and Relative Value-Added Deflators 1/

(In percent of GDP at market prices, 2/ and as index numbers 1970=100)

	1970	1975	1976	1977	1978	1979	1980	1981	1982
Agriculture									
Nominal	3.6	2.9	2.9	2.4	2.5	2.2	2.2	2.3	2.4
Real	3.6	2.9	2.7	2.7	2.9	2.9	2.9	3.0	3.3
Deflator	100.0	101.1	110.6	88.8	85.7	79.1	76.7	78.8	73.5
Industry									
Nominal	42.3	38.5	38.5	38.1	37.5	36.7	36.1	34.5	34.1
Real	38.3	38.5	39.2	39.5	39.1	39.3	38.3	36.5	36.0
Deflator	100.0	90.7	89.1	87.4	87.0	84.8	85.5	85.6	86.0
Mining									
Nominal	0.9	0.8	0.7	0.6	0.6	0.5	0.5	0.5	0.5
Real	1.2	0.8	0.8	0.7	0.6	0.6	0.6	0.5	0.5
Deflator	100.0	131.3	126.5	124.4	117.6	109.1	115.8	124.5	128.5
Manufacturing									
Nominal	32.1	27.4	27.4	26.9	26.4	25.8	24.6	24.0	24.0
Real	27.4	27.4	28.1	28.2	27.9	28.2	27.2	26.8	26.7
Deflator	100.0	85.2	83.0	81.3	80.6	77.9	77.0	76.2	76.7
Electricity, gas, etc.									
Nominal	2.3	3.1	3.0	3.0	3.1	3.2	3.5	3.6	3.5
Real	2.1	3.1	3.1	3.3	3.5	3.7	3.6	3.5	3.4
Deflator	100.0	92.6	89.2	84.2	81.9	81.4	87.6	96.0	96.8
Construction									
Nominal	6.9	7.2	7.4	7.5	7.5	7.2	7.5	6.3	6.0
Real	7.6	7.2	7.2	7.3	7.2	6.8	6.9	5.6	5.3
Deflator	100.0	110.0	112.6	112.9	115.2	116.8	120.3	123.0	123.8
Service sector									
Nominal	54.9	59.8	60.4	62.0	62.7	63.5	64.5	66.3	66.5
Real	59.2	59.8	59.2	59.5	59.7	60.4	60.5	61.3	61.5
Deflator	100.0	108.0	110.9	112.4	113.3	113.5	115.0	116.7	116.7
Commerce, banking, etc. 3/									
Nominal	25.4	26.3	27.4	27.5	27.5	27.8	28.1	28.7	29.1
Real	26.1	26.3	26.3	26.2	26.3	26.8	26.8	26.7	27.0
Deflator	100.0	102.9	107.0	107.5	107.2	106.8	107.8	110.4	110.7
Transportation, communication									
Nominal	7.2	7.7	7.7	7.7	7.8	8.0	8.3	8.5	8.6
Real	8.7	7.7	7.6	7.6	7.7	7.8	8.0	8.3	8.2
Deflator	100.0	120.8	121.3	122.5	122.9	123.6	126.0	124.7	125.4
Services									
Nominal	22.2	25.7	25.9	26.8	27.4	27.7	28.0	29.0	28.8
Real	24.4	25.7	25.4	25.7	25.7	25.8	25.7	26.3	26.2
Deflator	100.0	109.7	112.0	114.6	116.8	117.7	119.4	121.0	120.5
Private services									
Nominal	11.6	12.5	12.6	13.2	13.4	13.3	13.3	13.5	13.5
Real	12.0	12.5	12.3	12.5	12.3	12.2	12.2	12.5	12.6
Deflator	100.0	103.1	105.5	108.9	112.0	112.3	111.6	111.2	110.5
Public services									
Nominal	10.6	13.2	13.3	13.7	14.0	14.3	14.8	15.5	15.3
Real	12.4	13.2	13.1	13.2	13.4	13.6	13.5	13.8	13.6
Deflator	100.0	116.9	119.2	120.8	122.3	123.7	128.0	131.6	131.3

Source: National Institute of Statistics, Statistical Bulletin.

1/ "Relative value added deflators" are a sector's value added deflator relative to the GDP deflator.
2/ GDP at market prices, including statistical discrepancies; real GDP at 1975 prices. Data may not add up due to statistical discrepancies and rounding.
3/ Includes imputed banking services free of charge.

Table 5. Belgium: Industrial Production

(Changes in percent from same period of preceding year)

	1980	1981	1982	1982 Q1	1982 Q2	1982 Q3	1982 Q4	1983 Q1	1983 Q2	Compound Growth Rate 1975–82
Manufacturing	-1.2	-2.5	-0.5	-1.1	1.5	--	-2.3	2.4	-0.3	1.4
Investment goods	-3.2	-3.8	0.5	2.0	0.4	-0.4	-0.4	3.6	...	0.6
Durable consumer goods	-0.6	-2.6	2.7	3.3	3.1	2.6	1.6	6.0	...	0.6
Nondurable consumer goods	-0.1	1.0	3.4	3.0	5.0	3.5	1.7	2.9	...	2.2
Intermediate goods	-1.3	-4.0	-1.8	-3.1	1.6	-2.1	-3.7	2.2	...	1.7
Extractive industry	2.6	-6.3	1.4	-2.4	0.7	-1.5	5.5	0.8	...	-4.0
Electricity, gas, water	1.8	-5.1	-2.2	...	...	...	...	...	...	3.6
Construction	4.9	-17.3	-3.9	-4.9	-7.0	-5.3	2.7	-17.4		-7.0
Industry										
Excluding construction	-0.9	-2.5	-0.5	-2.0	1.9	0.2	-2.1	2.6	...	1.6
Including construction	--	-5.7	-1.1	-1.4	0.4	-1.8	-1.1	-4.4		-0.4

Sources: National Statistics Institute, _Communiqué Hebdomadaire_; OECD, _Main Economic Indicators_; and International Monetary Fund, _International Financial Statistics_.

Table 6. Belgium: Labor Market Developments

(Changes in percent from same period of preceding year)

	1975	1976	1977	1978	1979	1980	1981	1982 1/	1983 QI	1983 Q2
Working age population 2/3/	0.9	1.0	1.0	1.0	0.9	0.7	0.5	0.6	...	...
Labor force 2/4/	0.5	0.8	0.6	0.7	1.5	0.4	0.4	0.7	...	...
Employment 2/										
Total 4/	-1.5	-0.7	-0.2	--	1.2	-0.1	-2.1	-1.3	...	...
Private sector	-1.9	-1.1	-0.6	-0.8	0.3	-0.5	-2.6	-1.7	...	...
Public sector 4/	1.9	2.3	2.1	5.2	5.6	1.9	0.4	0.6	...	...
Manufacturing	-5.8	-4.0	-3.8	-4.0	-2.6	-2.1	-5.1	-3.6	-2.5	
Unemployment rate 5/										
Total 6/	5.0	6.5	7.5	8.1	8.4	9.1	11.2	13.1	14.2	14.3
Insured workers	6.7	8.6	9.8	10.5	10.9	11.8	14.2	16.6	18.3	18.1
Men	4.8	5.5	6.0	6.3	6.3	6.9	9.6	12.0	13.9	13.3
Women	10.8	14.8	12.3	18.1	19.0	20.1	22.0	24.6	26.2	25.4
Unfilled vacancies	-69.6	--	-17.0	23.5	35.7	3.5	-25.4	-9.1	54.5	50.0
Memorandum item:										
Incidence of early retirement 7/	(--)	(-0.2)	(-0.8)	(-1.3)	(-1.8)	(-2.3)	(-2.7)	(-3.2)	(...)	(...)

Sources: Data supplied by the National Bank of Belgium; OECD, Main Economic Indicators; European Communities, European Economy; International Monetary Fund, International Financial Statistics; and staff calculations.

1/ Partly preliminary data, or estimated.
2/ Data of June 30th.
3/ Population aged 15-64 years.
4/ Including armed forces.
5/ In percent.
6/ In percent of civilian labor force.
7/ Data measure the percentage by which the actual unemployment rate has been reduced (-)--in percent of ensured labor force--on account of early retirement.

Table 7. Belgium: Employment in the Private Sector

(Changes in percent, and index numbers)

	Changes in Percent								Index
	1975	1976	1977	1978	1979	1980	1981	1982	1982 1/
Agriculture	-2.7	-5.9	-4.1	-3.3	--	-5.4	-2.4	-2.3	76.6
Industry 2/	-5.5	-3.9	-3.7	-3.9	-2.6	-2.0	-4.8	-3.4	73.8
Construction	0.2	1.3	0.6	-1.3	0.8	-3.0	-10.3	-8.8	80.6
Services 3/ (cyclically sensitive)	0.1	-0.1	0.7	0.6	1.5	1.1	-0.7	-0.6	102.6
Services 4/ (cyclically less sensitive)	1.1	2.4	3.1	2.7	3.2	1.2	0.9	1.7	117.4
Total private employemnt	-1.9	-1.1	-0.6	-0.8	0.3	-0.5	-2.6	-1.3	91.8

Sources: National Bank of Belgium, Annual Report 1982; data supplied by the National Bank of Belgium; and staff calculations.

1/ 1974 = 100.
2/ Excluding construction.
3/ Commerce, transport and communications, financial services, insurance and other services rendered to enterprises.
4/ Medical professions, garages, housing, and other services rendered to individuals.

Table 8. Belgium: Indicators of Costs, Productivity, and Competitiveness

(Changes in percent from same period of preceding year)

	1975	1976	1977	1978	1979	1980	1981	1982	1982				1983	
									QI	Q2	Q3	Q4	Q1	Q2
Hourly earnings														
Economy	20.2	11.1	9.1	7.1	7.7	9.3	10.1	6.2	8.3	5.7	6.4	4.5	3.8	4.0
Manufacturing	21.4	13.2	12.0	8.0	7.7	9.6	8.1	5.3	6.5	4.6	5.7	4.5	3.8	5.2
Unit labor costs														
Economy 1/	16.9	9.3	6.8	3.3	4.3	5.6	6.0	5.1	...	...	...	...	...	...
Manufacturing	15.2	2.7	4.9	2.7	1.1	6.1	2.2	3.3	2.2	--	4.1	6.0	0.7	5.0
Costs of intermediate inputs	-4.6	6.4	1.2	-1.8	6.0	9.1	8.3	11.7	14.8	16.0	11.2	5.6	3.6	4.1
Production costs 2/														
Economy	2.6	8.0	4.0	1.5	6.6	9.2	9.0	9.5	12.2	11.9	9.4	5.1	3.7	4.1
Manufacturing														
Unadjusted 3/	0.5	8.0	3.9	0.8	6.4	9.2	8.2	9.9	12.3	12.6	9.6	5.3	3.6	4.4
Adjusted 3/	0.5	5.3	2.3	-0.5	4.5	8.2	6.5	9.3	11.1	11.4	9.3	5.7	2.8	4.3
Productivity														
Enterprise sector 4/	-1.5	7.2	1.9	3.5	2.8	2.1	-0.3	1.6	...	...	...	...	...	...
Industry 4/5/	-0.4	12.4	5.2	5.5	7.0	1.1	2.0	4.6	...	...	...	...	...	...
Manufacturing 6/	5.3	10.2	6.7	5.2	6.4	3.4	5.7	2.2	4.2	4.6	1.5	-1.4	3.1	0.2
Competitiveness 7/														
In relation to:														
Industrial countries	1.0	1.2	2.0	-0.9	-3.3	-4.2	-9.5	-11.5	-8.8	-14.5	-12.0	-11.0	-8.3	0.3
EMS	--	1.9	1.2	-0.7	-3.8	-2.8	-5.6	-11.4	-8.7	-14.7	-12.0	-10.4	-9.8	-0.1
Memorandum item:														
Profit rate 1/8/	-9.2	2.3	--	1.0	0.7	-5.8	1.0	5.7	...	...	...	...	...	...

Sources: National Bank of Belgium, Annual Report 1982; OECD, Main Economic Indicators; International Monetary Fund, International Financial Statistics; and staff calculations.

1/ Change in wages and salaries to change in real GDP.

2/ Calculated as a weighted average of costs of intermediate inputs and labor costs. Weights are those of input/output tables for 1975.

3/ Unadjusted series applies hourly earnings in the calculations, adjusted series applies unit labor costs.

4/ Value added per person employed.

5/ Excluding construction.

6/ Output per manhour.

7/ Measured by unit labor costs in common currency. A plus sign indicates a higher growth of costs in Belgium and, thus, a deterioration in competitiveness in relation to (a) 14 industrial partner countries; and (b) EMS partner countries.

8/ Measured as the change in the ratio of the value added deflator to unit labor costs.

Table 9. Belgium: Price Developments

(Changes in percent from same period of preceding year)

	1977	1978	1979	1980	1981	1982	1982				1983		
							Q1	Q2	Q3	Q4	Q1	Q2	Q3
GNP deflator	7.2	4.2	4.2	4.3	5.3	7.0	...	...	...	...	...	...	...
Total domestic demand deflator	7.1	4.2	4.1	6.8	8.1	7.1	...	...	...	...	...	...	...
Consumer price index	7.1	4.5	4.5	6.7	7.6	8.7	7.6	9.2	9.1	8.9	8.7	7.6	7.6
Food	6.7	1.5	0.5	3.6	6.0	9.5	9.1	10.2	10.4	8.4	8.0	8.0	...
Nonfood	...	3.3	6.0	9.0	9.5	9.5	8.1	10.3	9.3	10.2	8.9	6.8	...
Of which: Energy products	3.1	1.2	17.4	27.9	21.1	14.8	...	...	...	...	...	...	...
Services	11.3	8.3	5.5	5.7	5.9	7.1	5.7	7.2	7.8	7.5	8.9	8.1	...
Rents	9.2	7.2	6.0	7.6	10.2	8.1	8.2	8.3	7.5	8.6	9.2	9.3	...
Wholesale price index	2.4	-1.9	6.3	5.8	8.1	7.7	8.9	9.0	6.9	6.2	3.7	2.7	...
Agricultural products	4.6	-7.0	7.1	1.8	10.6	7.1	8.7	9.0	6.0	4.7	2.2	-0.3	...
Industrial products	1.9	-0.6	6.0	6.8	7.6	7.9	9.0	9.0	7.2	6.6	4.1	3.4	...
Import unit value	1.9	1.3	10.4	15.6	14.4	14.3	13.0	13.1	12.6	16.9	8.5	7.5	...
Memorandum item: Effective exchange rate (MERM)	5.6	3.7	2.4	0.2	-6.8	-9.8	-7.0	-10.6	-10.0	-11.6	-6.3	-1.8	...

Sources: National Bank of Belgium, Bulletin; and International Monetary Fund, International Financial Statistics.

Table 10. Belgium: Distribution of National Income

(In percent of GDP)

	1975	1976	1977	1978	1979	1980	1981	1982 1/
Households								
Wages and salaries	57.2	58.1	58.5	58.5	58.5	59.3	59.7	58.6
Other earned income	23.7	23.5	23.1	23.1	23.0	23.1	24.4	25.2
Current transfers	18.6	19.1	19.8	20.2	20.6	20.7	22.4	22.5
Personal income	99.5	100.7	101.4	101.8	102.2	103.1	106.3	106.2
Direct taxes, including social security	25.7	25.6	27.0	27.8	28.3	28.0	28.3	29.3
(Net direct taxes) 2/	(7.1)	(6.5)	(7.2)	(7.6)	(7.7)	(7.3)	(6.1)	(6.8)
Disposable income	73.8	75.1	74.3	74.0	73.9	75.1	78.0	76.9
Corporate enterprises								
Gross operating surplus before subsidies	12.4	11.2	11.2	10.7	10.9	10.3	9.1	10.1
Subsidies	1.2	1.4	1.4	1.5	1.7	1.5	1.6	1.6
Gross operating surplus	13.6	12.6	12.6	13.3	12.6	11.8	10.8	11.7
Disposable income	7.0	6.8	7.0	7.3	7.4	6.8	6.5	7.0
General Government								
Gross primary income								
Excluding interest on public debt	10.5	10.7	10.8	10.7	10.7	11.4	11.8	12.1
Including interest on public debt	7.0	7.0	6.7	6.2	5.6	5.3	3.9	2.9
Disposable income	16.3	15.6	15.8	15.8	15.5	14.1	11.0	11.3
Total disposable income	97.4	97.8	97.4	97.3	96.9	95.9	95.9	95.9
Memorandum item:								
GDP (change in percent)	10.6	13.5	8.0	7.6	6.8	7.5	4.1	8.1

Sources: Data supplied by the National Bank of Belgium; and International Monetary Fund, International Financial Statistics.

1/ Estimates of the National Bank of Belgium.
2/ Direct taxes, including social security, minus current transfers.

Table 11. Belgium: Measures of Profitability of Enterprises

(Ratios and changes in percent)

	1975	1976	1977	1978	1979	1980	1981	1982 1/
All corporate enterprises								
Gross operating surplus as a percentage of value added 2/	17.0	15.2	15.3	14.8	15.0	14.2	12.7	14.0
Rate of return 3/	8.1	7.7	7.9	7.7	7.9	7.6	6.8	7.5
Relative rate of return 4/	12.3	7.8	6.1	3.7	2.9	2.2	0.8	2.7
Profit rate 5/	...	...	...	...	...	1.7	-7.5	25.5
Manufacturing sector								
Rate of return 3/	9.5	9.5	9.7	9.6	9.9	7.5	7.5	9.5
Relative rate of return 4/	13.7	9.6	7.9	5.6	4.9	2.1	1.4	4.7
Labor cost developments								
Unadjusted 6/	16.0	7.7	6.9	4.1	5.6	6.6	3.9	-0.2
Adjusted 6/	10.1	-2.2	--	-1.0	-0.7	3.1	-1.7	-2.3
Memorandum item:								
Real interest rate 7/	-4.2	-0.1	1.7	4.0	5.0	5.4	6.1	4.8

Sources: Belgian National Bank, Annual Report 1982; National Institute of Statistics; Bulletin of Statistics; International Monetary Fund, International Financial Statistics; and staff calculations.

1/ Partly preliminary.
2/ Gross operating surplus before subsidies.
3/ Gross operating surplus as a percentage of gross capital stock.
4/ Rate of return minus real interest rate.
5/ Changes in percent. Estimates of National Bank of Belgium, based on output price and input cost developments.
6/ Changes in growth of labor cost index to growth of value added deflator index. The unadjusted measure uses the index of hourly compensation of employees for wage costs; the adjusted measure uses the unit labor cost index.
7/ Government bond yield minus rate of change of consumer price index.

II. Public Finance

1. Introduction

A central element of the adjustment program initiated by the authorities in early 1982 concerned a halving of the public sector deficit to 7 per cent of GNP by 1985, to be achieved essentially by restraining expenditure growth. The emphasis on this aspect stemmed from recognition of the interdependence between the imbalance in public finances and the other major disequilibria in the Belgian economy, especially the external deficit. After the first oil crisis, public sector deficit spending had to some extent been considered both justified and necessary to counter the decline in private sector activity and offset the contraction in demand. By the end of the 1970s, however, the adverse consequences, particularly on the external position, of such a counter-cyclical policy in the face of a protracted recession had become increasingly evident. The sharp rise in the public sector's net financing requirement, from 4 percent of GNP in 1974 to over 16 percent in 1981, was recognized as a factor, along with the rapid growth of wages and salaries and an insufficiently responsive industrial structure, in sustaining total absorption well above the level warranted by the increase in domestic output, thereby contributing to the continued deterioration of the current account. The external imbalance thus had its counterpart in the public deficit. The excessive level of public expenditure furthermore sustained inflation in the nonindustrial sector of the economy. Financing the deficit by nonmonetary means also became increasingly difficult, imposing a heavy strain on domestic resources and requiring extensive recourse to foreign funds. Finally, the borrowing requirement was seen to be approaching a self-perpetuating level through the increase in the debt service burden.

The main items of general government transactions which led to this situation are reviewed below, identifying the causes of the imbalance by major expenditure and revenue categories.

2. The deterioration of Belgian public finances, 1974-81

A strong growth of the public sector and a marked expansion of public sector spending, well above that of nominal output, were developments common to almost every industrial country, not only after the first oil crisis in late 1973, but also during the preceding years. A number of factors, however, single out the Belgian case. Firstly, the initial position of the early 1970s was in itself comparatively less favorable: in 1973, the share of public expenditure in GNP was already some 6 percentage points higher than in other industrial countries, and the general government borrowing requirement, at over 5 percent of GNP, was larger than in all other main partner countries. The long-term trend toward an expanding government role, reflecting diffuse social and political pressures to allocate a growing share of national income to publicly-provided services (in the form of extended or improved social security, health care, and education), thus appears to have been relatively more intense in Belgium than in other industrial countries already in the 1960s and early 1970s. Secondly, the increase in general government spending after the first oil crisis was the most rapid among major industrial countries, taking place on a truly massive scale, with public sector expenditure rising by almost 20 percentage points of GNP, from 44 percent in 1974 to 63 percent of GNP in 1981. Over the same period, the average change in the share of public spending in national income in other EC member countries was, at some 10 percent, only half the Belgian rate of increase. Finally, the authorities' use of the budget for counter-cyclical purposes was not only more intense but also more prolonged than in other major industrial countries, continuing even after the second oil crisis. While in the three-year period 1979-81 almost all industrial countries tightened their fiscal policy stance, withdrawing fiscal stimulus, 1/ in Belgium a markedly expansionary thrust persisted, with an additional stimulus of some 4 percent of GNP being imparted over the period, largely as a consequence of expenditure growth well above that of potential output. As a result, while the general trend in 1979-81 was toward a stabilization or even a decline in the public deficit as a proportion of GNP, in Belgium it expanded even more rapidly than in previous years, doubling in nominal terms and passing from 8.9 percent to 16.2 percent of GNP (Chart 7).

a. Public expenditure

Although in the period under review all categories of expenditure grew considerably faster than nominal output (Tables 12, 13 and 14), the biggest single increases were recorded by current transfers to households and by interest payments, which together contributed almost half of the overall increased claims of the public sector on resources between 1974 and 1981.

Current transfers to households 2/ rose from 16.5 percent to 23 percent of GNP over the period, bringing the contribution of government transfers to the formation of households' net disposable income up from 22 percent in 1974 to 29 percent in 1981. 3/ The strongly upward trend in transfer payments may be ascribed to the widespread index-linking of benefits (on average about 60 percent of current expenditure in the 1974-81 period was linked to price or wage developments), the growth in the number of beneficiaries and a general extension of eligibility criteria. Belgium has a comprehensive social security system, covering

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1/ For the seven major industrial countries the withdrawal of stimulus (Central Government) has been estimated at 1 percent of GNP, on the basis of a "cyclically neutral budget" analysis. For methodology, see International Monetary Fund, World Economic Outlook, May 1983, Appendix A.2.

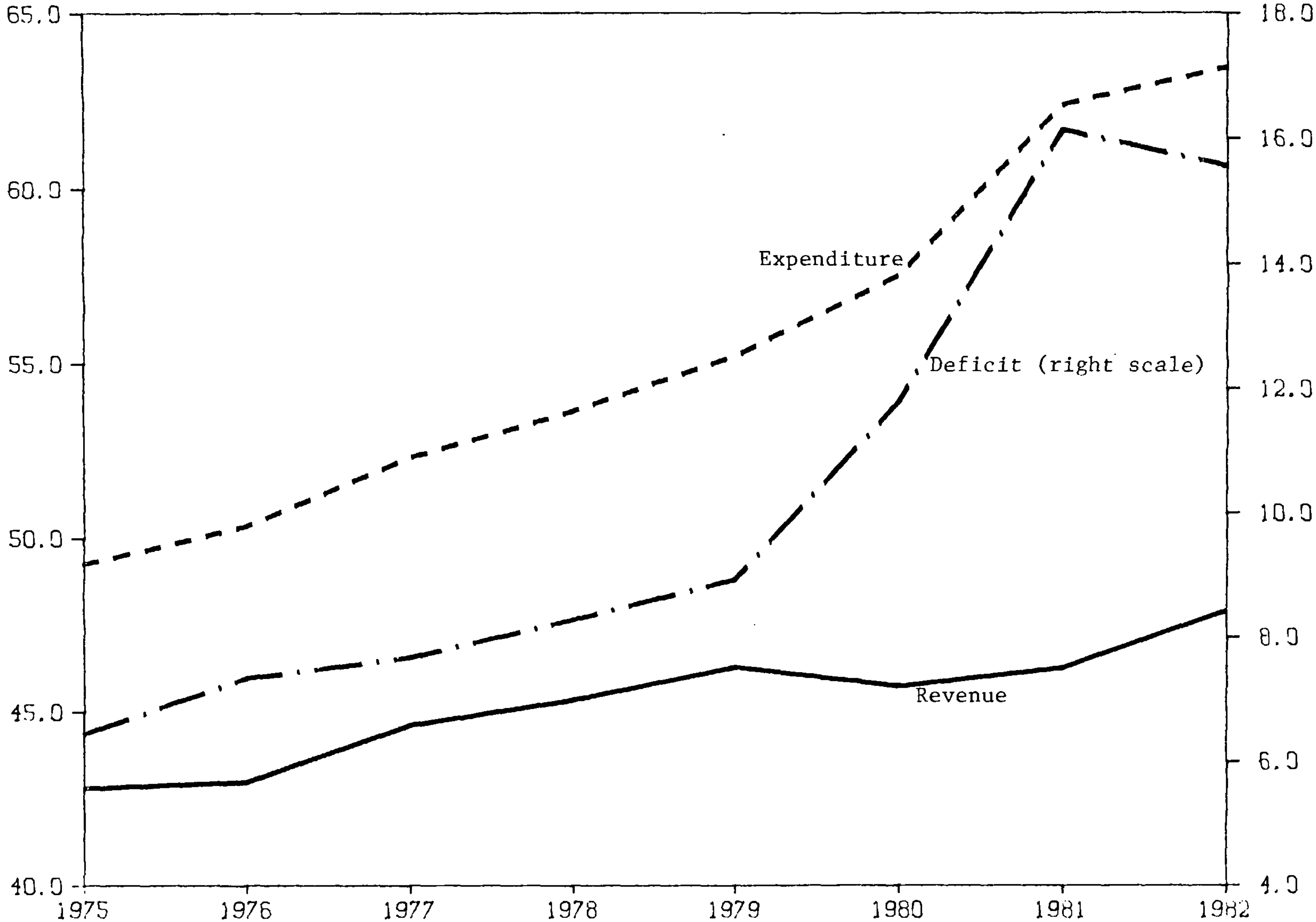
2/ Including unemployment benefits, subsumed in Tables 12 to 14 under the item "Unemployment and employment promotion".

3/ On a net basis (government transfers to households minus direct taxes and social security contributions), the contribution did not change significantly over the period, passing from about -9 percent of disposable income in 1974 to -8 percent in 1981.

Chart 7

Belgium: Indicators of General Government Finances

(In percent of GDP)



Source: National Bank of Belgium, Annual Report, 1982

both replacement and supplementary incomes, with separate programs administering pensions, sickness and invalidity, unemployment, family and holiday allowances, work accidents, professional illnesses and income guarantees for the elderly. It is governed by complex institutional arrangements: the system has separate schemes for salaried workers in the private sector, the self-employed and the public employees; the five major social security funds are administered autonomously by their own commissions representing employers, employees and the Government; different contribution rates are set for each sector and separate arrangements exist with respect to State subsidies; several ministries oversee the system (including the Ministry of Social Affairs, the Ministry of Employment and Labor, the Ministry of Middle Classes, and the Ministry of Public Health). The complexity of the institutional arrangements has led to dispersive decision-making, overlapping competences and the lack of a central overview and control of the system. The widespread granting of legal entitlements to beneficiaries has rendered many of the transfer programs ever more deeply entrenched and their corresponding expenditure increasingly intractable.

By far the most dynamic component in social transfer expenditure has been unemployment benefits, whose nominal amount increased sevenfold between 1974 and 1981, with its share in total social security spending rising from 5 percent to 14 percent. Some two thirds of the increase may be attributed to the rise in unemployment, and the remainder to the indexation of benefits to wages. The "generosity" of the Belgian unemployment scheme, as measured by the amount of income replaced by the unemployment benefits, 1/ is--at 66 percent in 1980--not out of line with that of other industrial countries. Belgium is however unique in having no limits on the duration of benefits (although benefits are gradually reduced for nonfamily heads), so that the cumulative cost to the Government has become very substantial over time, while the unemployed are also induced to spend more time in job search.

Despite their rapid rise, the share of unemployment benefits in total social spending is still proportionally small: the largest expenditures within the social security system are for pensions and sickness-invalidity, which throughout the period 1974-81 accounted for around 35 percent and 30 percent respectively of total benefits paid. Medical expenditure in particular recorded a significant increase in the volume of disbursements per beneficiary, while contribution rates remained broadly unchanged. The uptrend was due not only to the general increase in health care costs and to the development of a hypertrophic medical infrastructure, 2/ but also to institutional and demographic

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1/ The so-called "replacement ratio", equal to unemployment benefits after tax as a percentage of former disposable income, for an average production worker.

2/ In 1970 there were in Belgium 15,000 doctors, 5,000 kinesthesists, and 80,000 hospital beds; in 1979, with the total population remaining virtually unchanged, the numbers had risen to 24,500 doctors, 11,000 kinesthesists and 90,000 hospital beds (i.e., one every 100 inhabitants).

factors. The group of beneficiaries which weighs most heavily on the medical insurance program in Belgium are widowers, invalids, pensioners and orphans (the so-called VIPO-WIGW group), who are entitled to most medical services free of charge, while other beneficiaries participate on a cost-sharing basis. Although the group represents less than a quarter of participants, it absorbs about half of total sickness and invalidity expenditure. The aging of the population, whereby Belgium in 1981 had one of the highest proportions among OECD countries of inactive persons aged 64 and over to the labor force (some 33 percent), as well as increased recourse to early retirement in the face of a worsening employment situation, both contributed to significantly swell the number of beneficiaries in the VIPO-WIGW group, deteriorating the financial situation of the sickness-invalidity insurance program. The same phenomena also contributed to the growth in pension payments, while family allowances increased at a comparatively lower rate, due again to demographic factors (a decline in the proportion of child allowances).

The other major category of expenditure which has increased substantially as a proportion of national income has been interest payments on the public debt. Its rate of growth towards the end of the period under review, at over 1 percentage point of GNP per annum, was by far the most rapid and accounted for the majority of the increase in the expenditure ratio.

Belgium: Public Sector Interest Payments: Selected Ratios

	Average 1974-80	1981	1982
Annual percentage increase	19.7	35.4	25.8
Interest payments as a percentage of:			
Current expenditure	9.6	14.6	16.6
Current revenue	10.3	17.9	20.2
GNP	4.4	7.9	9.3

Source: National Institute of Statistics, Statistical Bulletin; and staff calculations.

Almost half of the rise in the public sector borrowing requirement in the three years to 1981 was due to heavier debt servicing, and with interest payments approaching 15 percent of current expenditure and 18 percent of current revenue, the scope of fiscal policy became increasingly constrained. The steep rise in interest payments stemmed from the combined effect of rapid public debt accumulation and higher interest rates. The average interest rate on the public debt rose from 7 percent in 1974 to over 10 percent in 1981. More importantly, over the same period, the total public debt (Central Government, debudgetized sector 1/ and local authorities) doubled in relation to output, rising from 58 percent of GNP in 1974 to 116 percent in 1981, and its maturity structure and composition changed considerably, shifting from long- and medium-term to short-term debt and from domestic to foreign currency debt (Tables 20 and 21). Whereas in 1974 only some 15 percent of the central government debt was short-term (with an initial maturity of less than one year), the proportion had risen to almost 40 percent by 1981. Similarly, up to 1978 the Treasury had not had recourse in any significant way to foreign currency loans to meet its commitments, and the outstanding balance due on these loans had been reduced to BF 3.3 billion by the end of 1977. From 1978, however, the public sector borrowing requirement increasingly outstripped the financial surplus of the private sector, and the foreign currency debt of the Central Government accordingly rose, as a percentage of GNP, to 1.8 percent in 1979, 4.4 percent in 1980 and 10.7 percent (BF 388 billion) in 1981.

A large part of the increased weight of the public sector between 1974 and 1981 was therefore due to the burgeoning of mandatory expenditure items (unemployment benefits and interest payments), arising automatically from chronically weak growth; but at least part of the deterioration in public finances may also be attributed to discretionary policy decisions aimed at alleviating the effects of the economic crisis. Various employment support measures, 2/ enacted since 1975, have weighed heavily on the budget, costing about BF 30 billion (approximately 1 percent of GNP) in 1981. Public employment has grown very rapidly, by 120,000 persons between 1974 and 1981 (while private sector employment declined by some 240,000 persons), adding more than BF 100 billion to expenditure. Higher civil service recruitment was also spurred on by the implementation of regional reform and the developing role of local authorities, whose consumption has increased more rapidly than that of the Central Government. Further deliberate policy actions in support of economic activity have taken the form of tax reliefs to improve the situation of businesses and sustain investment and aid for crisis industries or sectors, through the granting of interest subsidies and other transfers. As a proportion of GNP, current transfers to enterprises amounted to 3.5 percent and capital transfers (credit and equity investments) to 2.7 percent in 1981. "Tax expenditure" has also grown briskly, giving rise to a relatively complex system of tax reliefs and exemptions whose overall effect in terms of foregone tax revenue is considerable; for example, the net tax burden on enterprises, i.e., after deduction of tax concessions,

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1/ Debt serviced (principal and interest) by the Treasury, though it does not appear as such in the national debt budget (for further details, see footnote to Table 20).

2/ Such as the temporary employment scheme (cadre special temporaire) the "third employment alternative" (troisième circuit du travail), part-time work and early retirement schemes (see Chapter I).

subsidies and transfers, has been calculated by the Ministry of Finance to have been equal to only some 40 percent of the theoretical amount of company tax toward the end of the 1970s, against some 60 percent in 1975. 1/

b. Public revenues

The rise in Belgian tax pressure (direct and indirect taxes and social security contributions), although largely insufficient to offset the acceleration in expenditure, has been one of the most rapid among industrial countries: while tax receipts in Belgium accounted for 1.5 percent of total OECD tax revenue at the beginning of the 1970s, the proportion had risen to 2.25 percent by the end of the decade. The upward trend was however broken in 1980-81, when concern over the long-term effects of rising tax pressure on output and growth led to the granting of various tax reductions. There was particular concern that the high tax burden might have encouraged the underground economy (involving 8 percent of the active population according to recent estimates by the International Labor Office) and tax evasion. Although there are no official estimates as to the extent of tax evasion, the draft budgets in recent years have systematically contained entries ranging from BF 10 to 15 billion (between 1 and 1.5 percent of central government current revenue) to be "recovered" by means of stricter controls and improved tax collection.

The increase in tax pressure has been mainly due to direct taxation, largely under the impact of fiscal drag, as Belgian income tax thresholds are not fully adjusted for inflation. At almost 20 percent of national income the burden of direct taxation is considerably higher than in most partner countries, the average ratio of direct taxation to GNP in other EC countries being equal to approximately 15 percent. The ratio of indirect taxation, on the contrary, has remained broadly stable, at around 12 percent of national income, whereas it has tended to rise to some 15 percent in other EC countries. The percentage of GNP taken by receipts from social security contributions has been rising, in line with developments in main partner countries, even though widely different methods of financing social security benefits detract from the significance of cross-country comparisons in this area.

The tax structure has thus changed appreciably from the early 1970s (Table 15), with the share of direct taxation in total tax and quasi-tax revenue rising from 32 percent in 1970 to 42 percent in 1981, and with all of the increase being accounted for by a rising share of taxes on personal income. The proportion of direct taxes paid by households grew from 78 percent in 1970 to 86 percent in 1981, with a corresponding decline in the share of corporate income taxes, reflecting the marked deterioration in profitability. The relative reliance on

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1/ This calculation conceals results which differ according to the category of firms, as taxation hits firms which make profits while subsidies go mainly to firms in difficulty.

indirect taxation has, conversely, decreased, its share in total taxation falling from 38 percent to 27 percent between 1970 and 1981, while the share of social security contributions has remained broadly stable at 30 percent of total taxation, with a slightly declining proportion being paid by employers.

3. The 1982 shift in fiscal policy stance

The developments outlined above in the main expenditure and revenue categories brought the disequilibrium in public finances to a particularly disquieting level: as a percentage of GNP, the public sector borrowing requirement (PSBR) doubled between 1974 and 1978 and again between 1978 and 1981, reaching 16.2 percent of GNP. Even though some concern for the state of public finances had already been apparent in the 1980 and 1981 budgets, the policy of gradual adjustment which was adopted, aiming at a constant real level of noncompulsory expenditure (i.e., excluding unemployment benefits and interest payments), proved itself to be gravely insufficient given the scale of the disequilibrium.

It was only in the context of the broader recovery program of early 1982 that fiscal adjustment became a prime objective, with fiscal policy assuming a distinctly more restrictive stance, at the same time also being directed at accelerating the shift in income distribution from households to enterprises. The emphasis was put on curbing expenditure while lowering certain taxes in order to sustain supply. The authorities set the medium-term objective of reducing the public sector borrowing requirement to 7 percent of GNP by 1985 which, when formulated--on the basis of preliminary estimates for the 1981 outturn--implied a yearly reduction of 1.5 percent of GNP. Given the sharp overrun recorded in 1981 with respect to these estimates, attainment of the target subsequently implied a reduction in the PSBR of 2.3 percentage points of GNP per annum between 1982 and 1985.

The 1982 budget was drafted with this medium-term objective in mind, aiming at reducing the central government deficit to BF 424 billion or 11 percent of GNP, from BF 455 billion or 12.6 percent of GNP in 1981. The main spending cuts were in the social security field, most particularly in family allowances, sickness allowances, holiday grants and unemployment benefits. On the revenue side, the budget introduced a number of tax measures to improve firms' financial position (the standard rate of corporate income tax was reduced from 48 to 45 percent) 1/ and to promote the raising of risk capital and the investment in shares via profit tax exemptions for increases in equity capital and personal income tax deductibility of new equity investments and their earned dividends. Substantial investment allowances were also granted, with the standard deduction on corporate taxable income being set at 13 percent of the value of the new investment; other rates vary between

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1/ This measure entered into effect as from 1983 (on 1982 corporate income). The reduction in tax liability is to be used within the firm to finance new investment, create employment or improve the financial structure.

5 and 25 percent according to the type of investment, with the largest deduction (subsequently raised to 35 percent) being granted for energy-saving outlays. The rate of VAT on residential construction was reduced from 17 percent to 6 percent, in an attempt to revive this sharply declining sector. 1/ On the other hand, some social security contributions were increased, notably the pension contributions paid by employees (up from 6.25 percent to 7 percent) and patients' contributions to health costs; a special 10 percent levy on household net taxable incomes over BF 3 million was introduced to finance the unemployment fund; and the special "solidarity" contribution on public service salaries, due to expire, was extended for a further period.

Although the central government budget targets were overrun, with the net financing requirement equalling BF 508.6 billion (13 percent of GNP), the difference between original plans and outcome was notably less marked than in 1981 (Table 17) and on a cyclically-adjusted basis represented a significant withdrawal of stimulus. The overshoot was furthermore largely attributable to a spending overhang from the previous year, with a considerable carry-over of 1981 commitments, and to the late adoption of the budget (in March 1982) which reduced its operational time span.

At general government level, the borrowing requirement declined as a proportion of GNP, for the first time since 1974, passing from 16.2 percent to 15.7 percent. The improvement may be attributed mainly to a strong pickup in revenues, which actually exceeded original projections despite slower than expected GNP growth. Direct tax receipts, in particular, rose sharply, by almost 2 percentage points of GNP (from 18.1 percent of GNP in 1981 to 19.7 percent in 1982). The increase in direct tax revenue was due not only to the effects of fiscal drag as inflation accelerated, but also to transitory once-and-for-all developments. These were the catch-up, at the beginning of 1982, on the previous backlogs in tax collection (arising from the considerable delays in tax assessments in 1981), a speeding up of tax assessments in the second half of 1982 and, to a lesser extent, to the introduction of a "voluntary tax payments" system (volontariat fiscal), whereby rebates are granted for advance payment of personal income and property taxes not deducted at source. Indirect taxes and social security contributions grew at the same pace as GNP, so that their combined share in national income remained constant at slightly over 26 percent.

On the expenditure side, the series of measures adopted to curb current expenditure succeeded in keeping such expenditure, excluding interest payments, almost unchanged relative to GNP (close to 47 percent). The rise in total current expenditure from 54.5 percent to 55.7 percent of GNP was thus almost entirely due to the growth in interest payments, up from 7.9 percent to 9.3 percent of GNP. 2/ The heavier interest burden

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1/ The measure, originally in effect from March 1982 to end-1983, has since been extended to end-1985.

2/ By way of comparison, interest payments as a percentage of GNP/GDP in the 13 main OECD countries was around 3 percent in 1981.

stemmed both from the increase in the total public debt (Central Government, debudgetized and local authorities) from BF 3,277 billion at end-1981 to BF 3,905 billion at end-1982, and from the effects of the Belgian franc's depreciation on interest outlays on the foreign currency component of the debt, which rose from BF 402 billion to an estimated BF 683 billion. The February 1982 devaluation of the Belgian franc within the EMS alone is estimated to have added about BF 4 billion to interest payments.

The stability of total capital expenditure as a percentage of GNP (8.3 percent) conceals two contrasting developments. On the one hand, a continued fall in direct public investment, mainly as a result of sharp cutbacks in the investment programs of local authorities in the face of severe financial difficulties. On the other hand, net capital transfers in the form of loans and participations continued to increase rapidly, reflecting public assistance to ailing sectors, particularly the iron and steel industry.

4. The 1983 budget and the draft budget for 1984

The 1983 central government budget, which was tabled in August 1982 and slightly modified in its presentation to Parliament in October 1982, provided for a reduction in the net financing requirement to BF 443 billion or 10.5 percent of GNP, down from 13.0 percent in 1982. Current spending growth was planned to be curbed from 14 percent in 1982 to 7.5 percent in 1983, implying a decline in real terms (on the basis of the budget's assumption of an 8.5 percent inflation rate). Expenditure cuts were made mainly in the field of social security (see section five below), and by halving the partial budgetization of employers' social security contributions ("Opération Maribel", implemented in July 1981), with a cost to firms of some BF 15 billion in terms of higher nonwage labor costs. The reduction in contributions is furthermore no longer calculated as a proportion of wages but as a flat-rate amount of BF 17,000 per worker. 1/ The budget provided for an even sharper cut in capital expenditure, set to remain unchanged in nominal terms. The overall growth of expenditure (excluding Treasury operations) of 7 percent would reduce the share of public expenditure in GNP, on the basis of the budget's assumptions of a 9 percent growth in nominal GNP, split into 1.3 percent in volume and 7.6 percent in price.

Revenues were estimated to increase by 10.2 percent, mainly through strengthened taxation of transfer incomes and the raising (from January 1, 1983) of the standard VAT rate from 17 percent to 19 percent (estimated to yield approximately BF 15 billion). Preliminary steps were also taken in the reform of direct taxation, one of the elements of the Government's program, although the budgetary constraint could not allow much headway to be made toward the general objective of reducing the tax burden for

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1/ The relief is reduced to BF 5,000 per worker for those firms who fail to reach an agreement under the government's work-sharing scheme.

families and low-income earners and of indexing income tax threshholds. 1/ The Government nevertheless restated its intention to undertake an in-depth reform of the personal income tax system.

By early March 1983 it became clear that the execution of the budget was coming up against the familiar problems of an excessively sanguine estimate for the previous year's deficit (BF 464 billion instead of an outcome of BF 509 billion), compounded by slower than forecast nominal GNP growth for the current year (revised to 7 percent from the budget assumption of 9 percent, due to a lower projection for both real growth and the deflator). The combined effect was calculated to lead to a budgetary overshoot of BF 52.4 billion (BF 40.9 billion in additional expenditure and BF 11.5 billion in lower revenue) and supplementary measures were announced to recoup this amount. Although this "budgetary control" procedure may be taken to reveal a general improvement in fiscal management and monitoring techniques, not all of the measures could be implemented in a timely fashion and the 1983 Central Government budget targets will once again not be met. The deficit (cash basis) for the first nine months of the year amounts to BF 501 billion and the authorities now project a net financing requirement for the year as a whole of between BF 530 and BF 545 billion (some 13 percent of GNP, the same as in 1982, against a budgetary target of 10.5 percent of GNP). While expenditure growth has fallen in real terms and thus remained broadly in line with budgetary plans, so that net supplementary credits have been kept to a negligible level, there has been a sharp shortfall in receipts. Current receipts are now estimated to grow by less than 6 percent, against a budget estimate of over 10 percent. The budget figure had been based on an elasticity of revenues to nominal GNP growth of 1.2; the actual outcome corresponds to an elasticity of 0.8. The authorities attribute this result largely to technical or temporary factors, and have maintained an elasticity coefficient of 1.2 in the elaboration of the 1984 budget. The 1983 shortfall in tax revenue may be ascribed to abnormally slow growth in two of its major components, the précompte professionel (employees' pay-as-you-earn income tax deducted at source) and VAT receipts. The rise in the VAT rate at the beginning of 1983 did not boost revenues as much as expected, as its effects were temporarily pre-empted by widespread anticipatory purchases by households towards the end of 1982. The slow growth in receipts from the précompte professionel was, for its part, largely due to delays by local authorities and other public bodies in paying into the Central Government the amounts withheld from the wages and salaries of their employees. The Government has given itself the means, under its newly-granted special powers, to recoup these amounts.

1/ The main measures regarded an increase of about 40 percent in tax credits for dependent children and a reduction in the marginal tax rate for lower income families (earning between BF 750,000 and BF 1.5 million of taxable income) by means of changes in the system of splitting and noncumulation of incomes; the concomitant abolition of the lump-sum deduction of BF 10,000 from all professional incomes largely finances the above measures so that overall revenue is not significantly affected.

In early October 1983, in strict accordance with the budgetary timetable, the Government presented its draft budget for 1984. Based on the assumption of a nominal GNP growth of 6.6 percent (1 percent in volume and 5.5 percent in prices), it aims at a Central Government net financing requirement of BF 507.4 billion (11.5 percent of GNP). This represents a reduction of a little over 1 percent of GNP on the estimated outcome for 1983. Current expenditure (excluding Treasury operations) is projected to rise by 5.5 percent; excluding interest payments, the growth rate is of 4.5 percent, a little under the assumed inflation rate of 5.5 percent. This compares with a "spontaneous" increase under unchanged policies of approximately 10 percent. Interest payments on the public debt will continue to weigh heavily on the budget: at BF 320.5 billion, they amount to some 20 percent of current expenditure and 25 percent of current revenues. Capital expenditure is projected to remain constant in nominal terms. Total revenues are expected to increase by 3.8 percent. The main measures announced are in the social security field, with limits on the cumulation of replacement incomes, the taxation of holiday grants, the nonindexation of pensions above a certain level, a tightening of entitlement criteria for unemployment benefits, increases in certain social security contributions (sickness-invalidity and pensions) and greater cost-sharing by beneficiaries. The withholding tax on interest and dividend income (précompte mobilier) is to be raised from 20 percent to 25 percent with such earnings being exempted from any further declaration in income tax returns. The measure is expected to yield BF 15 billion in additional revenue. To limit the assumed advantage for high investment income earners, the portion of such income above BF 1.1 million is to be reinvested, within two years, in new shares or bonds of Belgian companies, to be kept for five years. Failure to reinvest will give rise to a compensatory levy at a progressive rate, according to the amount concerned, from 27 percent to 47 percent. A fiscal amnesty is to be granted with respect to any capital invested by Belgian residents in employment-creating activities by December 31, 1985, with no need to justify the origin of the funds. One eleventh of the amount in question is however to be invested in five-year noninterest bearing Treasury certificates. In a further attempt to revive the construction industry, the withholding tax on real estate income (précompte immobilier) becomes the taxpayer's final tax liability on income from new residential housing property.

The draft budget for 1984 implies a slowdown in the pace of adjustment originally envisaged in the multi-annual budget strategy to 1985, under which the Central Government's net financing requirement should have amounted to BF 380 billion in 1984 (against the BF 507 billion projected in the budget). In this respect, the authorities point to concerns over excessive deflation, in the context of a more sluggish world economic environment than forecast at the time of the adjustment program's formulation in early 1982. The objective of halving the deficit between 1982 and 1985 is now recognized to be unattainable; the Planning Bureau, notwithstanding a projected sharp pickup in corporate taxes as firms' profitability improves, forecasts a Central Government net financing requirement of 11 percent of GNP in 1985 and of 9.6 percent in 1987.

5. Social security finances

Social security spending has been one of the most dynamic forces underlying the growth of public expenditure in Belgium, contributing about two fifths of the overall increased share of public spending in GNP between 1974 and 1981. 1/ Despite various increases in the contribution rates and in the ceiling on wages subject to contributions, the growth of disbursements has far outstripped that of contributions (Table 18); between 1974 and 1981, total contributions (by employers, employees and self-employed) rose from 12 percent to 14 percent of GNP, while benefit payments rose from 14 to 20 percent. At the same time, the disposable reserves of the social security system have been all but eroded and Central Government subsidies have consequently been called upon to play an ever increasing role in the financing of the system, especially for its unemployment and sickness-invalidity programs. Whereas in 1974 contributions covered 80 percent of social security expenditures, the ratio had fallen to 60 percent by 1981. Revenue deficiencies are especially pronounced in the unemployment insurance fund, with contributions covering a mere 25 percent of benefit payments. Both sluggish growth and demographic factors have contributed to the sharp fall in the ratio between the number of employed persons subject to contributions and the number of beneficiaries. The number of unemployed per every 100 employed persons thus rose from 5 in 1970 to 16 at present; in the pension program, the number of beneficiaries per every 100 contributors has risen from 39 in the early 1970s to 54 at present, and is projected to reach 68 in 1987.

Since 1982, the authorities have adopted a two-pronged approach in the face of the deterioration in social security finances. On the one hand, with recourse largely to legislation under its special powers in the course of 1982, the Government took a number of measures to reduce the social security deficit, without however fundamentally altering the system's overall workings and criteria. On the other hand, in the realization that the system's mechanisms were conceived in a period of strong growth and in anticipation of continued high growth rates, the Government is in the process of defining a more fundamental and longer-term reform of the system (Plan Dehaene), 2/ to better adapt it to the economy's present capacity and prospects. The reform, which is being prepared in concertation with the social partners and will be adopted through the normal legislative procedures, should be implemented in the course of 1984 or by January 1, 1985 at the latest. The main points of the plan are: (1) while maintaining the individual right to social security, to give priority to households for whom social security benefits represent the major source of income; (2) to harmonize the different regimes and to eliminate all forms of cumulation of social

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1/ See Section 2a. above.
2/ Minister for Social Affairs, Proposition du Ministre des Affaires Sociales en vue de Réfomer la Sécurité Sociale, May 1983. In its projections to 1990, this study reveals the build-up of particularly large deficits in the health care and pension programs.

security benefits; (3) to rationalize the medical care structure; (4) to maintain direct financing of the social security funds, avoiding the system of earmarking certain tax receipts in the Central Government budget; (5) to ensure that the way social security contributions are levied does not hinder the extension of all forms of worksharing; (6) to eventually seek a form of financing which would not distort the relative cost of labor, such as a tax on firms' gross value added. The authorities intend pursuing the latter proposal at European level.

In the shorter term, the main measures taken in 1982, and renewed in 1983, realized a number of significant savings in social insurance benefits, strengthened the taxation of transfer incomes and raised certain social security contributions. A first set of measures was taken between March and July 1982, to produce a saving of around BF 40 billion via essentially a reduction of unemployment benefits (by 4 percent for heads of households and by 6 percent for cohabitants), of family allowances (by BF 500 a month per family) and of sickness allowances. On the revenue side, workers' pension contributions were raised from 6.25 percent to 7 percent and patients' participation in health costs were increased. A number of special or "solidarity" levies were also introduced as follows: a 10 percent tax on individual net taxable incomes above BF 3 million (the proceeds being used to finance the unemployment insurance fund); a solidarity contribution on families with no dependent children (BF 900); and a contribution of 7 percent of the double holiday bonus. Furthermore, with effect from October 1982, the ceilings on reference wages for the calculation of social security contributions were abolished and workers' and employers' contributions were broadly aligned.

At end 1982, before the expiry of special powers, all of the above measures were renewed for 1983, including the special solidarity levies originally conceived as "temporary" contributions; the deduction on the double holiday bonus was increased from 7 to 11 percent. Further savings were realized by curtailing the family allowance for the first child (suppression of the 13th and 14th month allowances) and by limiting the cumulation of benefits from retirement and work accidents or professional illnesses. The indexation of social security benefits was also modified, in accordance with the new provisions governing wages, with payments being linked to a four-month moving average of the consumer price index.

The 1984 draft budget contains further measures in the social security area, to trim spending by an estimated BF 32 billion, with some of the measures already effective as from the third quarter of 1983. In essence, the main measures concern stiffer taxation of unemployment benefits when cumulated with other income (no rebates being granted above a taxable income of BF 750,000); the de-indexation of the portion of pensions above BF 32,052 a month; a number of savings and greater cost sharing by beneficiaries in the health care program; higher social security contributions for both employers and employees; and a 12 percent levy on civil servants' holiday bonus. On the other hand, the reduction in family allowances is to be brought down from

BF 500 to BF 375 and the special solidarity contribution on households with no dependent children is likewise reduced from BF 900 to BF 675. The special 10 percent tax on incomes above BF 3 million in favor of the unemployment fund is, for its part, to be maintained in 1984.

6. The finances of the local authorities

The deficit on the finances of the local authorities was reduced in 1982, to an estimated BF 54 billion (or 8.8 percent of the total PSBR), from the record level of BF 61 billion (14.8 percent of the PSBR) recorded in 1980. The improvement is not however very firmly based: it is mostly attributable to a very sharp decline in local authorities' investment (down by 7.5 percent in nominal terms), to an unwinding of the considerable backlog developed in 1981 in the Treasury's payments to the local authorities of the municipal and provincial taxes assessed on their behalf, and--to a lesser extent--to the reimbursement by the Sickness-Invalidity Fund of part of its debts to the public social assistance centers, which thus had lesser recourse to municipal subsidies.

It is in the most important sector of local authorities, that of municipalities, 1/ that the most severe difficulties were experienced, with serious financial strains coming to the fore in a number of large cities in the course of the year and requiring special advances or loans from the Central Government. The deterioration in the finances of municipalities may be summarized in a number of key figures: the deficit on the ordinary budgets (broadly comprising current transactions) has risen from BF 4.4 billion in 1979 to a budgeted deficit of BF 34.1 billion in 1982, with half of the amount being accounted for by the five large cities (Antwerp, Brussels, Charleroi, Ghent and Liège); whereas in 1979 there were 457 municipalities with balanced or surplus budgets (77 percent of the total) and 139 in deficit; the situation had been completely reversed by 1982, with 527 municipalities in deficit and only 69 in a balanced or surplus position. The deterioration is largely attributable to the unchecked growth of expenditure, which has recorded an average annual growth rate of close to 11 percent since 1979. The percentage breakdown of the different categories of municipal expenditure has remained broadly stable, with all items growing at approximately the same rate. The bulk of expenditure is on personnel costs (47 percent of total ordinary expenditure in 1982), due especially to the steep growth in the number of civil servants. The debt service is the next most important item, accounting for a little under 30 percent of ordinary expenditure. On the revenue side, these developments have meant a heavy reliance on State transfers through the Municipal Fund (financed by a credit in the budget of the Ministry of the Interior), which accounted for some 28 percent (or BF 57 billion) of municipal revenue in 1982. Another 35 percent was

1/ The local authorities include mainly provinces and municipalities, as well as various administrative bodies such as the public social assistance centers and inter-municipal associations.

constituted by fiscal receipts, which mainly take the form of a surtax on the précompte immobilier (withholding tax on real estate income) and a surtax on personal income tax (subject to a 6 percent limit until end-1982).

In December 1982, availing itself of its special powers, the Government adopted a decree with a view to imposing balanced budgets on the local authorities. The decree provides that, as from 1988 (which coincides with the year of the next municipal elections), the budgets of provincial and municipal authorities may no longer present deficits, on either the ordinary (current transactions) or extraordinary (capital transactions) budget. With a view to this objective, local authorities showing deficits as from the 1984 budget year are to align staff salary levels with those of the Central Government. In case of failure in achieving these objectives, the administration of the local authorities' budgets may be taken over by the Central Government. In order to provide the municipalities with greater financial resources, the 6 percent limit on the local surtax on personal income tax has been abolished. Although it appears likely that most municipalities will avail themselves of the greater revenue raising possibilities thus offered, the impact on the total tax burden should not be significant: a 1 percent increase in the surtax on the part of all municipalities would yield approximately BF 3.5 billion (0.1 percent of GNP).

7. The public debt

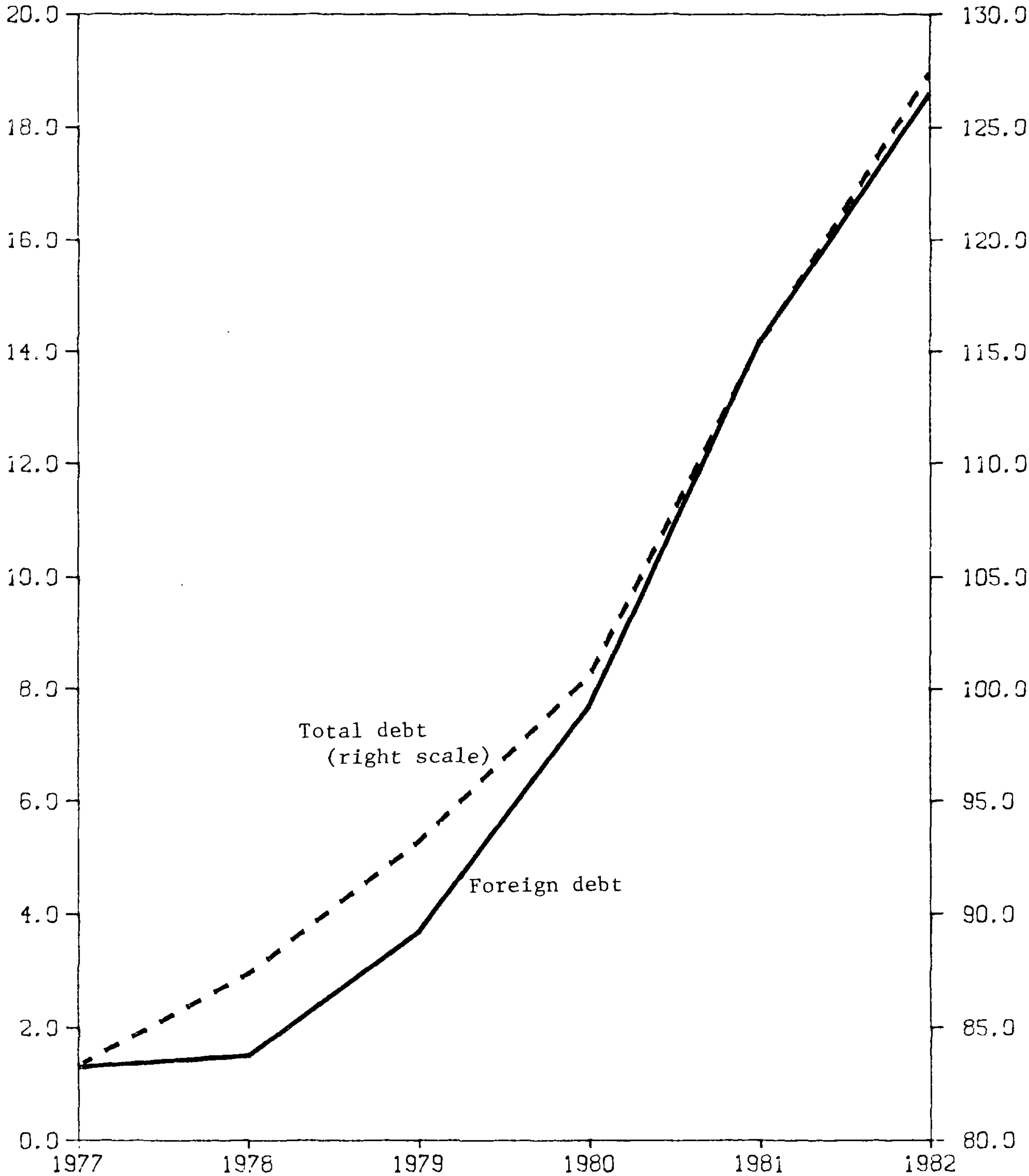
The above developments in public finances have entailed a burgeoning of the public debt (Tables 20 and 21, and Chart 8), with total public and publicly-guaranteed debt more than doubling since 1977 and approaching BF 5,000 billion (close to 130 percent of GNP) at end-1982. The Central Government debt accounts for some three fifths of total public sector indebtedness. The shortage of funds on the domestic markets has also meant a strong expansion in the foreign currency component of the debt, from a mere BF 31 billion in 1977 to close to BF 926 billion (24 percent of GNP) at present. The steep rise in the foreign currency debt is largely attributable to the transactions of the Central Government, as well as to the increase in government guarantees for borrowings by enterprises in crisis industries, particularly steel. The situation has worsened most markedly since 1979, when net official reserves (excluding gold) were still marginally larger than the official external debt. An eightfold increase in the debt and the decline in net foreign exchange reserves have meant that the level of readily mobilized reserves now covers less than a quarter of Belgium's public and publicly-guaranteed external debt. Nearly half of the Central Government's outstanding external debt was short-term at end-1982, but the proportion of short-term debt has been declining in the course of 1983 as the authorities have been pursuing a deliberate policy of consolidation (see Table 22, also for the currency composition of the debt). The amortization of the Central Government foreign debt shows a marked bunching of repayments in 1987-88 (Table 23).

The exchange rate risk on external indebtedness is illustrated, ex post, by the losses incurred as a result of exchange rate variations (Table 24). Exchange rate losses on the Central Government consolidated debt amounted to BF 20.5 billion in 1981, BF 34.3 billion in 1982 and BF 30.8 billion in the first seven months of 1983, thus accounting for some 40 percent of the overall increase in the external consolidated debt expressed in Belgian francs over the 1981 to July 1983 period.

Chart 8

Belgium: Central Government Debt

(In percent of GDP)



Source: Ministry of Finance, Bulletin de Documentation.

Table 12. Belgium: Level and Changes in General Government Transactions, 1974-82

(In percent of GNP at current prices)

	Levels			Changes	
	1974	1981	1982	1974-81	1981-82
Total expenditure	43.6	62.8	64.0	19.2	1.2
Goods and services	14.2	17.6	17.4	3.4	-0.2
Transfers to households	15.6	20.0	19.9	4.4	-0.1
Unemployment and employment promotion	0.9	4.2	4.1	3.3	-0.1
Interest payments	3.5	7.9	9.3	4.4	1.4
Subsidies to enterprises, credits and equity investments 1/	3.6	6.2	6.4	2.6	0.2
Gross fixed capital formation	3.5	4.1	3.8	0.6	-0.3
Total receipts	39.5	46.6	48.3	7.1	1.7
Direct taxes	14.3	18.1	19.7	3.8	1.6
Indirect taxes	11.8	12.6	12.7	0.8	0.1
Social security contributions	11.9	13.6	13.5	1.7	-0.1
Net financing requirement	4.1	16.2	15.7	12.1	-0.5
(In percent of net private savings) 2/	(96.6)	(138.7)	(132.6)	(42.1)	(-6.1)

Source: National Bank of Belgium, Annual Report, 1982; and National Institute of Statistics, Statistical Bulletin.

1/ This item includes both current and capital expenditure deriving mainly from public support of crisis sectors and industries.
2/ Savings of households and enterprises, national accounts basis.

Table 13. Belgium: Consolidated Revenue, Expenditure and Net Borrowing Requirement of General Government 1/, 1974-82

(In billions of Belgian francs)

	1974	1975	1976	1977	1978	1979	1980	1981	1982 2/
1. Total revenue	831	990	1,129	1,266	1,384	1,508	1,601	1,686	1,886
Direct taxes	300	374	416	482	553	608	632	655	768
Indirect taxes	248	270	325	356	386	414	435	457	496
Social security contributions	251	304	343	377	395	425	459	494	526
Capital receipts	5	7	8	10	11	13	13	13	13
Other revenue	27	35	37	41	39	48	62	67	83
2. Total expenditure	916	1,139	1,322	1,484	1,637	1,799	2,014	2,274	2,500
Current expenditure	792	994	1,152	1,297	1,436	1,582	1,739	1,972	2,175
Of which:									
Goods and services	297	367	415	459	505	538	581	637	678
Interest payments	73	82	98	117	138	166	212	287	361
Unemployment and employment promotion	18	39	51	68	84	104	120	151	171
Current transfers to households	328	412	476	524	569	619	666	725	776
Subsidies to enterprises	56	68	84	95	102	111	115	126	132
Net current transfers to rest of the world	20	26	28	34	38	44	45	46	57
Capital expenditure	124	145	170	187	201	217	275	302	325
Of which:									
Direct investment	74	88	102	109	112	124	143	146	150
Credits and equity investments	20	26	33	40	49	50	78	98	115
Other net capital transfers	30	31	35	38	40	43	54	58	60
3. Net borrowing requirement (= 1-2)	-85	-149	-193	-218	-253	-291	-413	-588	-614

Source: National Bank of Belgium, Annual Report, 1982; and National Institute of Statistics, Statistical Bulletin.

1/ Central Government, local authorities and social security funds. On national accounts basis.
2/ Provisional.

Table 14. Belgium: Consolidated Revenue, Expenditure and Net Borrowing Requirement of General Government, 1/ 1974-82

(In percent of GNP at current prices)

	1974	1975	1976	1977	1978	1979	1980	1981	1982 2/
1. Total revenue	39.5	42.6	42.7	44.4	45.2	46.4	46.0	46.6	48.3
Direct taxes	14.3	16.1	15.7	16.9	18.1	18.7	18.1	18.1	19.7
Indirect taxes	11.8	11.6	12.3	12.5	12.6	12.7	12.5	12.6	12.7
Social security contributions	11.9	13.1	13.0	13.2	12.9	13.1	13.2	13.6	13.5
Capital receipts	0.2	0.3	0.3	0.3	0.3	0.4	0.4	0.4	0.3
Other revenue	1.3	1.5	1.4	1.5	1.3	1.5	1.8	1.9	2.1
2. Total expenditure	43.6	49.0	50.0	52.1	53.5	55.3	57.8	62.8	64.0
Current expenditure	37.7	42.8	43.6	45.5	46.9	48.6	49.9	54.5	55.7
Of which:									
Goods and services	14.2	15.8	15.7	16.1	16.5	16.5	16.7	17.6	17.4
Interest payments	3.5	3.6	3.7	4.1	4.5	5.1	6.1	7.9	9.3
Unemployment and employment promotion	0.9	1.7	1.9	2.4	2.7	3.2	3.4	4.2	4.1
Current transfers to households	15.6	17.7	18.0	18.4	18.6	19.0	19.1	20.0	19.9
Subsidies to enterprises	2.6	2.9	3.2	3.3	3.3	3.4	3.3	3.5	3.4
Net current transfers to rest of the world	0.9	1.1	1.1	1.2	1.2	1.4	1.3	1.3	1.5
Capital expenditure	5.9	6.2	6.4	6.6	6.6	6.7	7.9	8.3	8.3
Of which:									
Direct investment	3.5	3.8	3.8	3.8	3.7	3.8	4.1	4.0	3.8
Credits and equity investment	1.0	1.1	1.3	1.4	1.6	1.6	2.2	2.7	8.0
Other net capital transfers	1.4	1.3	1.3	1.4	1.3	1.3	1.6	1.6	1.5
3. Net borrowing requirement (= 1-2)	-4.1	-6.4	-7.3	-7.6	-8.3	-8.9	-11.9	-16.2	-15.7

Sources: National Bank of Belgium, Annual Report, 1982; and National Institute of Statistics, Statistical Bulletin.

1/ Central Government, local authorities and social security funds. On national accounts basis.
2/ Provisional.

Table 15. Belgium: Current Revenue Structure 1/

	1960	1970	1975	1981	1982	1983
	(As a percent of total tax and quasi-tax current revenue)					
Direct taxes	29.0	32.3	40.4	42.1	44.1	42.0
Indirect taxes	43.8	37.7	28.2	28.0	27.2	28.0
Social security contributions	27.2	30.0	31.4	29.9	28.7	30.0
	(As a percent of GNP)					
Direct taxes	7.5	11.0	16.1	18.1	19.7	19.1
Indirect taxes	11.3	12.8	11.2	12.1	12.1	12.1
Social security contributions	7.1	10.2	12.5	12.8	12.8	13.6
Total current revenue	25.9	33.9	39.8	43.0	44.6	45.5

Sources: Data provided by Belgian authorities (based on 1970-82: National Institute of Statistics, Statistical Bulletin; 1983: Ministry of Economic Affairs, Budget Economique, 1983).

1/ On a national accounts basis.

Table 16. Belgium: Central Government Budget, 1980-84

(In billions of Belgian francs)

	1980	1981	1982	1983 Original budget	1983 Outcome 1/	1984 Budget
Current receipts	991.7	1,012.4	1,151.0	1,264.1	1,218.2	1,315.3
Of which: tax revenue	(946.2)	(953.5)	(1,076.1)	(1,209.0)	(1,152.0)	(1,247.9)
Current expenditure	1,139.1	1,276.9	1,458.8	1,524.0	1,540.9	1,625.4
Current balance	-147.4	-264.5	-307.8	-259.9	-322.7	-310.1
Capital receipts	12.7	13.9	13.6	14.1	5.3	3.1
Capital expenditure	157.3	184.4	192.6	193.2	193.5	193.2
Capital balance	-144.6	-170.5	-179.0	-179.1	-188.2	-190.1
Budget balance	-292.0	-435.0	-486.8	-439.0	-510.9	-500.2
Treasury operations	-5.1	-19.9	-21.8	-4.0	-20.0	-7.2
Net financing requirement	-297.1	-454.9	-508.6	-443.0	-530.9	-507.4
(As a percentage of GNP)	(8.6)	(12.6)	(13.0)	(10.5)	(12.8)	(11.5)
Debt repayment	120.2	157.5	157.9	222.4	222.4	244.7
Gross financing requirement	-417.3	-612.4	-666.5	-665.4	-753.3	-752.1

Source: Chamber of Representatives, Receipts and Expenditures Budget, various years.

1/ As estimated in the presentation of the 1984 Budget (October 1983).

Table 17. Belgium: Comparison of Central Government Budget Statements and Outturns, 1981-83

(In billions of Belgian francs)

	1981	1982	1983
Total revenue			
1. Budget	1,118.6	1,158.8	1,278.2
2. Outturn	1,026.3	1,164.6	1,223.5 2/
3. Difference (2-1)	-92.3	5.8	-54.7
Total expenditure 1/			
1. Budget	1,360.7	1,582.8	1,721.2
2. Outturn	1,481.2	1,673.2	1,754.4 2/
3. Difference (2-1)	120.5	90.4	33.2
Net financing requirement			
1. Budget	-242.1	-424.0	-443.0
2. Outturn	-454.9	-508.6	-530.9
3. Difference (2-1)	-212.8	-84.6	-87.9

Source: Chamber of Representatives, Receipts and Expenditures Budget, various years.

1/ Including Treasury operations, net.
2/ As estimated in the presentation of the 1984 Budget (October 1983).

Table 18. Belgium: Social Security System, Current Account, 1974-82

(National accounts basis; in billions of Belgian francs)

	1974	1978	1979	1980	1981	1982
Receipts						
Employers' contributions 1/	158.8	246.5	264.5	286.2	290.2	290.4
Other contributions (employees and self-employed)	81.7	131.1	140.9	151.5	174.5	210.0
State subsidies	78.2	197.9	210.1	225.7	291.0	333.6
Miscellaneous other income	12.6	14.4	13.9	16.5	21.6	19.1
Total receipts	331.3	589.8	629.4	679.9	777.3	853.2
Expenditures						
Benefit payments 1/	295.8	553.7	604.1	655.7	734.8	803.7
Operating expenses	16.9	31.3	33.2	36.1	40.3	43.1
Total expenditures	312.7	585.0	637.3	691.8	775.1	846.8
(In percent of GNP)	(14.9)	(19.1)	(19.6)	(19.9)	(21.4)	(21.7)
Balance	18.6	4.8	-7.9	-11.9	2.2	6.4

Source: National Institute of Statistics, Statistical Bulletin.

1/ Excluding payments of factory workers' vacation allowances.

Table 19. Belgium: Revenue Structure of Social Security System, 1974-82

(In percent)

	1974	1978	1979	1980	1981	1982
	(In percent of total social security revenues)					
Employers' contributions 1/	47.9	41.8	42.0	42.1	37.3	34.0
Other contributions (employees and self-employed)	24.7	22.2	22.4	22.3	22.5	24.6
State subsidies	23.6	33.6	33.4	33.2	37.4	39.1
Miscellaneous other income	3.8	2.4	2.2	2.4	2.8	2.2
	(In percent of GNP)					
Employers' contributions 1/	7.6	8.1	8.1	8.2	8.0	7.4
Other contributions (employees and self-employed)	3.9	4.6	4.3	4.4	4.8	5.4
State subsidies	3.7	6.9	6.5	6.5	8.0	8.6
Miscellaneous other income	0.6	0.5	0.4	0.5	0.6	0.5

Source: National Institute of Statistics, Statistical Bulletin. On national accounts basis.

1/ Excluding payments of factory workers' vacation allowances.

Table 20. Belgium: Total Public and Publicly-Guaranteed Debt in Domestic and Foreign Currencies

(In billions of Belgian francs; end of period)

	1977	1978	1979	1980	1981	1982	1983 August
A. Central Government	1,229	1,427	1,639	1,957	2,439	3,085	3,595
1. Consolidated	987	1,130	1,266	1,407	1,532	1,843	2,101
2. Medium term	6	6	6	6	6	3	47
3. Short term	236	291	367	544	901	1,239	1,446
B. Debudgetized sector 1/	246	278	323	374	421	377	...
C. Local authorities 2/	234	260	290	351	417	443	...
D. Publicly-guaranteed debt 3/	665	711	782	823	903	1,068	...
1. Consolidated	630	683	735	759	823	986	...
2. Short term	35	28	47	64	80	82	...
E. Total 4/	2,374	2,676	3,034	3,505	4,180	4,973	...
As per cent of GNP	83.3	87.4	93.2	100.6	115.4	127.4	...

Sources: Ministry of Finance, Bulletin de Documentation; Communiqué Mensuel du Ministre des Finances; and data provided by the National Bank of Belgium.

1/ Debt serviced (principal and interest) by the Treasury; it comprises debt incurred by the Treasury owing to the fact that financial intermediaries finance on its behalf part of the "national industries" in difficulty, the building premiums and the "government portion" of loans to the local authorities; the public authorities' participation (through the Fonds National du Logement) in the servicing of the debt incurred by the Société Nationale du Logement and the Société Nationale Terriene; and the debt taken over by the Treasury of certain social security programs (sickness and invalidity, pensions of self-employed).

2/ Net of debt included in the debudgetized sector, and net of financial assets held by local authorities.

3/ Debt guaranteed (principal and/or interest) by the Treasury and incurred mainly by public enterprises and semi-governmental financial institutions (typically the Société Nationale de Crédit à l'Industrie), which serve largely to support ailing industries.

4/ Net of debt included in the debudgetized sector or under guaranteed debt.

Table 21. Belgium: Foreign Currency Public and Publicly-Guaranteed Debt

(In billions of Belgian francs; end of period)

	1977	1978	1979	1980	1981	1982	1983 August
A. Central Government	3	15	57	154	388	642	787
1. Consolidated	3	3	13	85	183	333	410
2. Short term	--	13	44	69	205	309	377
B. Debudgetized sector 1/	--	--	--	--	8 2/	35 2/	...
C. Local authorities 3/	3	3	3	5	6	6	...
D. Publicly-guaranteed debt 4/	25	23	53	107	190	243	...
1. Consolidated	19	16	46	102	169	218	...
2. Short term	6	7	7	7	21	25	...
E. Total 5/	31	41	113	268	592	926	...
As per cent of GNP	1.1	1.3	3.5	7.7	16.4	23.7	...
As per cent of total debt (in domestic and foreign currencies)	1.3	1.5	3.7	7.7	14.2	18.6	...

Source: Ministry of Finance, Bulletin de Documentation; Communiqué Mensuel du Ministre des Finances; and data provided by the National Bank of Belgium.

1/ See footnote 2, Table 20.
2/ Estimates.
3/ Net of debt included in the debudgetized sector.
4/ See footnote 4, Table 20.
5/ Net of debt included in the debudgetized sector or under guaranteed debt.

Table 22. Belgium: Central Government Foreign Currency Debt:
Currency and Maturity Breakdown

(As per cent of total)

	1977	1978	1979	1980	1981	1982	1983 1/
Currency composition 2/							
Deutsche mark	29.4	6.0	52.4	44.1	34.8	33.4	31.9
Swiss franc	8.8	1.3	23.4	29.4	25.6	25.3	24.5
US dollar	23.5	85.2	22.6	24.7	27.4	26.7	28.5
Netherlands guilder	38.2	7.4	1.6	1.6	8.1	10.0	10.7
Yen	--	--	--	0.2	4.0	3.1	3.2
Maturity							
Short term	--	81.9	77.8	45.1	52.7	48.1	40.2
Medium- and long-term	100.0	18.1	22.2	54.9	47.3	51.9	59.8

Source: Ministry of Finance, Bulletin de Documentation; Communiqué Mensuel du Ministre des Finances.

1/ End-August 1983.
2/ Calculated on outstanding amounts expressed in Belgian francs.

Table 23. Belgium: Amortization Schedule of Central Government Consolidated Debt in Foreign Currencies 1/

(In millions of currency units)

	1983	1984	1985	1986	1987	1988	1989	1990
U.S. dollars	2.8	72.1	293.6	304.8	1,079.7	1,066.6	391.3	257.9
Deutsche marks	8.2	128.4	143.3	246.7	2,326.9	927.9	482.2	492.9
Swiss francs	1.6	1.7	151.7	282.6	1,087.1	1,111.8	329.8	124.2
Netherlands guilders	29.0	29.0	54.0	165.0	199.0	117.2	146.0	55.7
Yen	--	--	11,606.8	1,000.0	12,812.5	4,500.0	6,400.0	6,400.0
Total in Belgian francs 2/	881.2	7,061.2	26,142.0	31,702.4	138,704.4	117,444.5	43,143.5	29,388.9

Source: Data provided by the Belgian authorities.

1/ Situation as at end-August 1983; prevailing exchange rates applied.
2/ Including other foreign currency debt (in pounds sterling, Italian lire and French francs), not shown.

Table 24. Belgium: Changes in Central Government Consolidated External Debt

(In billions of Belgian francs)

	1980	1981	1982	1983
Level, end of period	84.3	183.5	333.3	395.7 1/
Change, including exchange rate variation	71.6	99.2	149.8	150.2 2/
Exchange rate variation 3/	4.0	20.5	34.3	36.1 2/
Change, excluding exchange rate variation	67.6	78.7	115.5	114.1 2/

Source: Ministry of Finance, Communiqué Mensuel du Ministre des Finances.

1/ End July 1983.
2/ Over the 12 months ending in July 1983.
3/ Changes in central government external debt due to exchange rate losses (+) or gains (-) on consolidated debt. Debt denominated in EMS currencies is converted at the ruling central rates.

III. Money and Credit

1. The general setting for monetary policy

The defense of the exchange rate has traditionally been the major intermediate objective of Belgian monetary policy. The main justification of the choice lay in the degree of openness of the economy and in the rigidity of the domestic wage-fixing procedure, in the presence of widespread formal indexation arrangements. The exchange rate norm has in effect served as the main anchor of monetary policy and of price stabilization policies, with the strong currency option helping to sharply reduce the inflation rate, especially between 1974-75 (12.8 percent) and 1978-79 (4.5 percent). But it could not per se prevent the lack of adjustment in the real economy, and most particularly in wage and public finance developments, from eventually bringing the basic disequilibria of the Belgian economy to a head.

It is in particular the strong increase in public sector expenditure and public sector borrowing requirements that has limited the scope and reduced the effectiveness of monetary policy in Belgium in a number of ways. The insensitiveness of public sector expenditure to interest rate changes has, for example, blunted the monetary signal most readily available to the Central Bank and has meant that, to achieve an equivalent result, the monetary authorities would have had to apply stronger corrective measures directed at a smaller and weaker private sector. Furthermore, the Government has also engaged in significant capital transfers in the form of loans to certain sectors, using the proceeds of its own borrowings to lend selectively within the economy, so that the distribution of a proportion of domestic credit has been governed to a growing extent by considerations beyond the scope of monetary policy.

The most significant constraint on monetary policy has however arisen from the fact that, in the absence of any institutional rule or formal commitment limiting credit to the public sector, the Central Bank has not been in a position to resist monetization of new public debt, either indirectly by providing additional liquidity to banks in order to facilitate their lending to the Government or--more importantly--by directly financing the deficit through the purchase of the proceeds of the Treasury's foreign currency borrowing and through direct advances to the public sector. Firstly, with respect to public borrowing abroad, the Central Bank is obliged to purchase the foreign currency proceeds from the Treasury and, secondly, central bank financing of the Treasury has assumed a quasi-automatic and permanent character.

The monetary authorities' claims on the public sector consist essentially of a portfolio of government bonds with the National Bank (a consolidated debt of BF 34 billion); a credit line of the Treasury with the National Bank (subject to a ceiling of BF 37 billion since

1977); and, above all, special assistance to the Fonds des Rentes. 1/ This assistance was formalized in a protocol to an agreement between the Ministry of Finance, the National Bank and th Fonds des Rentes (15 July 1977), whereby the Treasury can sell Treasury certificates to the Fund to cover "seasonal and unforeseen deficits beyond its credit line with the National Bank". This credit line (BF 37 billion) was in fact already exhausted by end-1977. If the liquidity position of the Fonds des Rentes (which may finance its operations by issuing its own securities and by borrowing on the call money market) is insufficient to accommodate the Treasury, it can turn to what the protocol defined as "momentary recourse" to the Central Bank (by way of a special advance or of a subscription to the Funds' own certificates), subject to a variable ceiling. The ceiling may be changed by mutual agreement between the National Bank and the Fund, "in relation to the requirements stemming from seasonal and unforeseen deficits of the central government".

The rationale of the agreement was that the Central Bank would need to accommodate "temporary" recourse to monetary financing by the public sector (for example to bridge a transitory or seasonal gap between expenditure and revenue flows) if it wished to avoid exceedingly sharp fluctuations in interest rates; the public announcement of the ceiling on such special assistance by the Central Bank was intended to act as "a guarantee that temporary support would not become permanent support". 2/ In practice, however, the process proved to be irreversible and the ceiling has become a more apparent, than real, limit on government financing. Although in its early existence the ceiling (initially set at BF 15 billion) was changed both upward and downward in keeping with its original spirit, it is now regularly revised only in an upward direction, rising by BF 30 billion per annum between 1978 and 1980, by BF 60 billion in 1981 and by BF 40 billion in 1982: it amounted to BF 190 billion at end-1982 and stands at BF 210 billion at present. The direct and indirect access of the Treasury to the Central Bank is thus now close to BF 250 billion, and what was intended as "temporary support" by the Bank has been transformed into permanent financing of government expenditure.

The results are apparent in the development of the sources of the money base (Table 25): the predominance of external sources on the assets side (66 percent of the total in 1977) has been rapidly supplanted by the public sector position, under the effect of the ever-growing advances to the Fonds des Rentes to purchase Treasury bills. Claims

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1/ The Fonds des Rentes (or Securities Stabilization Fund) is a public institution responsible for regulating the market for medium- and long-term public funds. To carry out this role, it normally uses the call money market, either for obtaining the resources it needs or, alternatively, for investing its possible surplus funds. Its normal financing is through the weekly issue of four-month certificates.

2/ National Bank of Belgium, Bulletin, July 1977.

on the public sector rose from 22 percent of total sources in 1977 to nearly 70 percent in 1982, bringing the domestic components of the base to 83 percent of the total. Chart 9 visualizes these developments, highlighting the sharp scissor movement between the National Bank's net foreign assets and its claims on the public sector since 1980.

Given the weight of external sources and of claims on the public sector, the other domestic components of the money base, rediscounts and advances to commercial banks, has played only a minor role as a source of change in the base. The domestic refinancing operations of the commercial banks would appear to be, on the face of the traditional instruments employed by the National Bank (discount rate and discount ceilings), the most closely controlled. Changes in the discount rate have however tended to be dictated almost exclusively by external considerations, while refinancing at the Bank has only a slight direct effect on the total cost of financial intermediaries' resources, as the share of recourse to the National Bank in the banks' total resources has on average been very low. It is, however, true that changes in the discount rate propagate to other rates (such as those charged by the Rediscount and Guarantee Institute) and eventually to rates on all resources whose remuneration depends on money market conditions (interbank claims, large deposits, nonresidents' Belgian franc deposits) so that changes in the Bank's official rates indirectly bring pressure to bear on the cost of a significant part of banks' total resources.

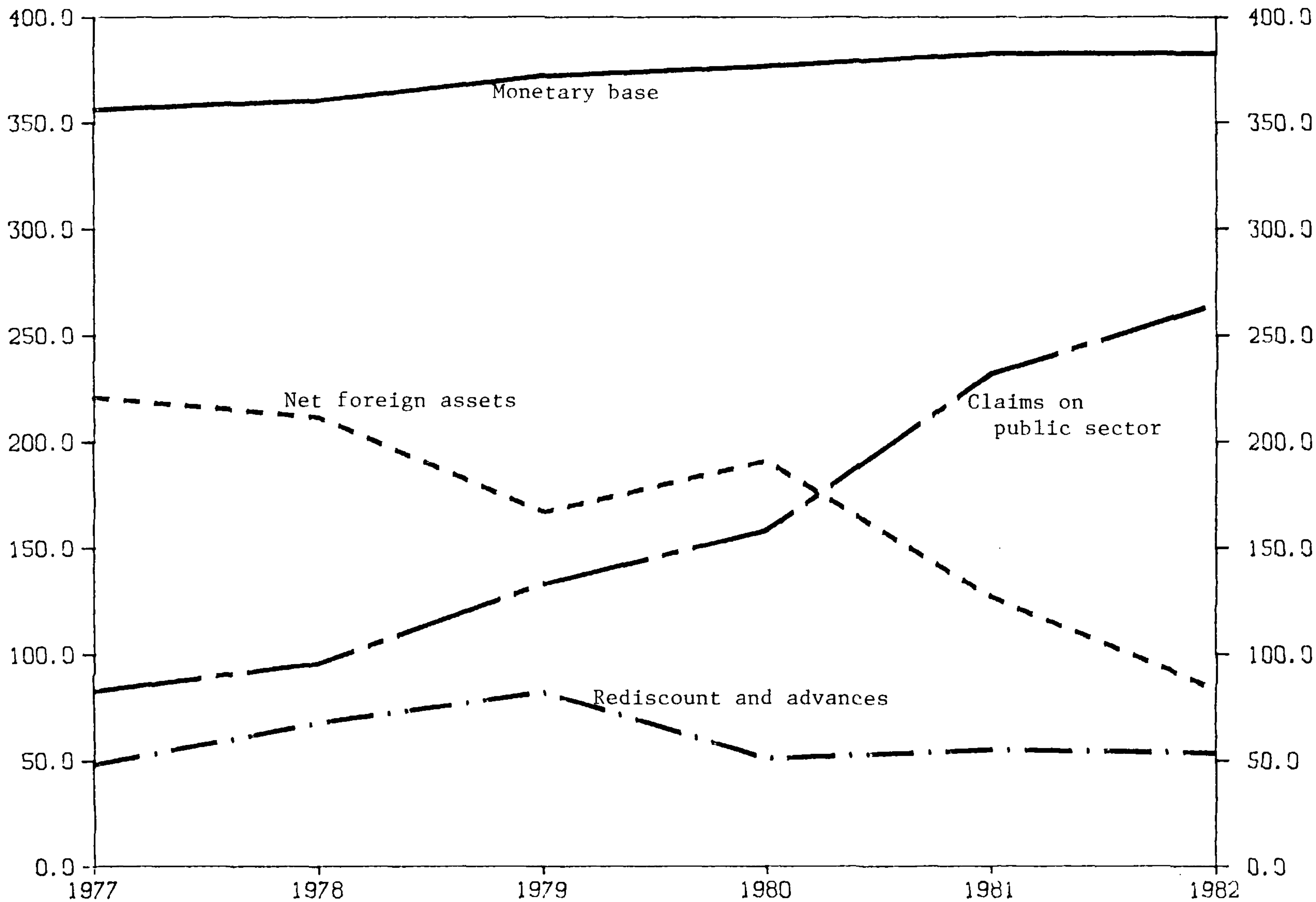
Apart from the effects of discount rate changes on the cost of banks' resources, it is also clear that the quantity of refinancing is only partially controlled by the monetary authorities once the rediscount rate is set unless the discount ceilings are imposed at a level which effectively curtails the amount of rediscounts and advances below that desired by the banks. 1/ The existence of large unused margins (especially since March 1980, when the Bank's modification in the method of fixing quotas for advances further raised the financial

1/ Although the Central Bank can to some extent influence the amount of refinancing by manipulating the differential between the cost of such refinancing and the yield on Treasury certificates, it cannot fully determine the Banks' behavior in this respect. While at times a relatively small differential has been sufficient to induce banks to use rediscounting facilities to subscribe to short-term Treasury certificates, the imposition in the past of minimum portfolio holdings of such certificates (based on the level of holdings at a given time) has rendered banks cautious in placing all their liquidity in short-term public paper and advised them to maintain a certain unused margin under the rediscount ceilings.

Chart 9

Belgium: Sources of Monetary Base

(In billions of Belgian francs; end of period)



Source: IMF, International Financial Statistics.

intermediaries' potential access to the Central Bank) 1/ indicates that the ceilings have not been used to regain control over this money base source. The ceilings have not been "biting" and control by the National Bank of banks' liquidity through refinancing has been limited in its volume aspect.

Although the monetary authorities in Belgium do not set themselves any intermediate target in the form of monetary or credit aggregates, they do have an informal objective in terms of the Central Bank's net foreign assets. The determination of this objective is based on a Central Bank balance sheet analysis, as follows: "given an estimate of the demand for cash, defined in terms of bank notes on the liability side of the National Bank, and given an estimate of credit by the Bank to the money markets, leaves the difference between the two to be allocated between credit to the Treasury and reserves". 2/ This formulation brings to the fore the importance of a close control over the domestic components of the monetary base and, most particularly, over central bank financing of the public sector.

Both public sector borrowing from the Central Bank and from abroad add to bank liquidity and, in the absence of any offsetting action (the proceeds from Treasury foreign borrowing are purchased by the Central Bank without subsequent sterilization), allow interest rates not to adjust fully to the financial pressures resulting from the excessive public deficit. Domestic monetary conditions are thus kept easier than they would otherwise have been: seldom has any real tightening of liquidity occurred, as shown in the generally wide margins available under the Bank's rediscount ceilings, an indication of the degree of pressure on the money markets. The impression of a largely accommodating policy is also confirmed by the close correlation between budget deficits and the variations in bank credit expansion, with finance of the public authorities through the banking sector following closely the upward trend in budget deficits. Financing through the nonbank private sector has for its part remained relatively stable.

1/ Each financial intermediary has a rediscount ceiling and a monthly quota of advances at the National Bank. Since March 1980, advance quotas are equal to three times the size of that part of the rediscount ceiling which is associated with temporary cash requirements. In addition, those intermediaries which have a portfolio of rediscountable commercial bills which is smaller than their rediscount ceiling, have the possibility of converting part, or the whole, of the difference into an additional quota.

2/ Minutes of Meeting No. 3, 1982 Article IV Consultation. See also National Bank of Belgium, Annual Report, 1982: "(The Bank) had set itself the aim of not allowing any further losses of reserves beyond a clearly specified limit; this limit automatically fixed that for the advances it could make in francs to the Treasury."

Excessive liquidity injection into the economy via both domestic credit expansion and external financing of the Treasury (these two sources more than fully compensating the loss of liquidity through the current account deficit) may therefore largely explain the significant net private capital outflows recorded in recent years, as greater domestic liquidity has led the private sector to diversify its asset portfolio at least partly in favor of foreign assets. Nor have the dual market arrangements really affected this mechanism: the many exceptions to a complete segregation of the two markets have led to a growing surplus on the current transactions going through the free market, thus impairing the rationale of the system and allowing the financing of significant net private capital outflows.

2. Recent developments

In recent years the conduct of monetary policy, and most particularly of interest rate management, in Belgium has attempted to reconcile the conflict arising from, on the one hand, the widening deficits of public finances and of the current account and their financing requirements and, on the other hand, from concerns over the impact of higher domestic interest rates on weak economic activity and a falling rate of fixed capital formation in the private sector. These conflicts were particularly marked in 1981, when their resolution appears to have been guided by greater emphasis on the latter set of considerations, with as much downward pressure as possible being kept on interest rates in order to prevent further growth of the debt service burden and a deepening of the recession. The rise in short- and long-term interest rates in 1981 was generally less marked in Belgium than in other countries, with a consequent narrowing of interest rate differentials which--compounded by adverse exchange rate expectations and the abundance of liquidity in the economy--led to considerable net private capital outflows, reversing the trend of the 1970s.

These conflicting requirements persisted in 1982, but the devaluation of the Belgian franc, the improvement in the current account, the stabilization of the public sector deficit relative to GNP, and the easing of international interest rates, all contributed to a somewhat less constrained setting for the operation of monetary policy in the course of the year. This generally easier setting also prevailed in 1983, with the exception of the first quarter which saw the buildup of strongly adverse exchange rate expectations and concomitant net private capital outflows. Clearly, however, the persistence of a large public sector deficit will continue to confront monetary policy with difficult choices, especially in periods of tension within the European Monetary System.

a. The financial survey

The imbalance between the availability and demand for funds on the domestic financial markets, which had widened continually up to 1981, reaching some 8 percent of GNP, narrowed significantly in 1982 and even more so in 1983, falling to between 3 and 4 percent of GNP (Table 27). The private sector's financial asset formation increased substantially in both years, after having stagnated in nominal terms between 1976 and 1980 and falling as a proportion of GNP from 17.6 percent to 13.4 percent over the same period (Table 28). Total private sector asset formation in 1982 amounted to BF 623.6 billion, equal to 16 percent of GNP or 18.3 percent of the private sector's gross disposable income, a further rise from that recorded in 1981. The relatively high figure of 1981 was however totally due to the strong increase in the formation of financial assets in foreign currencies; in 1982, a more cautious interest rate policy, with a slower decline in Belgian rates than in those of major competing markets and the appearance of a larger interest rate differential in favor of the Belgian franc, led to a significant reversal in this respect, with a marked shift away from the preference for foreign currency assets. These grew by only BF 82 billion, slightly more than half the amount of 1981. The sharp decline is totally attributable to a contraction in the formation of short-term foreign currency assets, from BF 112 billion in 1981 to BF 32 billion in 1982 (of which BF 6 billion with domestic banks; all figures adjusted for exchange rate changes), while new investments in longer-term foreign currency assets increased slightly from BF 39 billion to BF 50 billion, as expectations of a decline in foreign currency interest rates induced a shift from short- to longer-term placements (essentially bonds, while investments in foreign shares actually declined). Consequently, whereas asset formation in foreign currencies accounted for over a quarter of the total in 1981, its share stood at 13 percent in 1982. The shift away from preference for foreign currency assets, and especially from their short-term component, persisted in the first quarter of 1983, despite adverse exchange rate expectations, and their share in total asset formation declined further, to only 7 percent. The formation of financial assets in Belgian francs, on their part, after having declined continually (even in nominal terms) from 1977 to 1981, increased strongly to BF 508 billion in 1982, up by 41 percent on 1981. Both the formation of short-term assets (with the advance in time deposits more than offsetting a decline in sight deposits) and of long-term assets (an increase in bonds and bills issued by the Government and public financial intermediaries) in Belgian francs was greater than during the previous year. Investments in shares rose particularly sharply (by BF 21 billion, against a cumulative figure of under BF 7 billion in the three preceding years) as a result of the granting of tax advantages, although the proportion of shares in total financial assets remains relatively small.

As a result of the above developments, the domestic sectors' gross financing requirements could be met to a greater extent by funds available on the domestic market. The share of these funds in the meeting of total requirements, which had declined constantly from nearly full coverage in 1975 to about half in 1981, rose again to some three quarters in 1982 and increased further in 1983. The improvement, although less marked, is also apparent in the ratio of the public sector borrowing requirement to funds available on the domestic market: after having risen from 0.5 in 1975 to more than 1.5 in 1981, it declined to 1.2 in 1982.

The smaller shortfall of domestic financial savings relative to financial needs in 1982-83 was however also due to a decline in the latter, with the increase in the general government's cash requirements being more than offset by the continued sharp contraction in the private sector's demand for credit. Accentuating the decline observed over the last three years, new liabilities incurred by enterprises and households (Table 29) fell to only BF 157 billion (4 percent of GNP) in 1982, half of the increase (BF 310 billion or 9.5 percent of GNP) observed in 1979. The trend has continued into 1983, with new liabilities in the first semester amounting to BF 36 billion, against BF 68 billion in the corresponding period of 1982. The decline has occurred mainly in the private sector's new liabilities to Belgian financial intermediaries, with the main determinant being a decrease in outstanding liabilities of enterprises, as firms have used the improvement in their profit positions and greater net financing capacity to reduce their indebtedness to the banking system. Households for their part maintained the outstanding amount of personal loans and hire-purchase credits broadly unchanged in 1982, and have been actually decreasing them in 1983, while the continued slump in residential construction has led to a further decline in new liabilities contracted in the form of mortgage loans for housing. The greater financing possibilities offered by the domestic market have, on the other hand, been, reflected in the increase in new liabilities toward the Belgian nonfinancial sector (essentially enterprises' share and bond issues), up from BF 10 billion in 1981 to BF 25 billion in 1982, and to BF 24 billion in the first semester of 1983 alone. This year has also seen a sharp slowdown in loans raised abroad by enterprises.

b. Financing of the public sector

Although to a lesser extent than in past years, the public deficit continued to be financed largely by money creation in 1982, with the funding of the public sector more than offsetting the external drain on domestic liquidity. Up to 1978, the Treasury's borrowing requirement had been met largely through the issue of long-term debt: it accounted for four fifths of Treasury financing in that year. But the inverted yield structure which appeared in 1980 and 1981, and persisted through most of 1982, induced a marked shift in the term preference of households and financial intermediaries and forced the Treasury to borrow increasingly at short-term maturities. At the same time, as its borrowing requirement increasingly exceeded the private sector's financial surplus, it has had extensive recourse to external financing.

External borrowing covered 47 percent of the Treasury's deficit in 1981; the proportion declined marginally to 42 percent in 1982, with the National Bank purchasing directly from the Treasury BF 220 billion (BF 214 billion in 1981) of foreign currencies borrowed abroad (Table 30). 1/ In addition, in the course of 1982, the Bank increased

1/ These purchases largely financed the Bank's intervention sales on the official market, which totaled BF 265 billion in the course of the year (BF 316 billion in 1981).

its direct aid to the Treasury by raising the ceiling on its special assistance to the Fonds des Rentes to purchase Treasury bills from BF 150 billion to BF 190 billion. During the year as a whole, the portfolio of Treasury bills held by the Fonds des Rentes and financed by the Bank increased by BF 31 billion (against BF 72 billion in 1981). As a result of these transactions, the creation of liquidity relating to operations of the Treasury through the Bank's purchases of foreign currencies and its advances to the Fonds des Rentes declined for the first time since 1977, with the larger growth of foreign currency debt being more than offset by the fall in advances to the Fund. Monetary financing of the Treasury, which had risen rapidly from only BF 15.1 billion (9 percent of the deficit) in 1977 to BF 286.5 billion (63 percent) in 1981, thus fell to a still considerable BF 251.3 billion, or just under half of the deficit, in 1982.

The decline in monetary financing reflects the greater absorption capacity of the domestic capital market: the amount of long-term funds which the Treasury was able to raise in the domestic market increased, especially in the second semester with the return to a positively sloped term yield curve, and the consolidated debt in Belgian francs rose by BF 65 billion, covering 13 percent of the deficit (against only BF 26 billion or 6 percent in 1981). The high yield on short-term Treasury certificates continued however to exercise a relatively stronger attraction on financial intermediaries for the most part of 1982, and accounts for the large amount raised in this way; the increase in the short-term debt placed outside the Central Bank amounted to BF 193 billion (or 38 percent of the Treasury's requirements) in 1982 against BF 142 billion (31 percent) in 1981.

These broad trends have persisted in 1983 and have contributed to improving the outlook for the deficit's financing. The larger financial surplus of the private sector, the dramatic drop in its demand for funds and the return to a more normal interest rate structure--along with expectations of a decline in long-term interest rates--have allowed a significant increase in the proportion of long-term funds raised on the domestic market, as shown by the record figures of BF 112 billion and BF 140 billion raised by the long-term Treasury loans issued in early March and June 1983 respectively. By way of comparison, the "special loan" of 1981, despite the tax and exchange rate guarantee incentives attached to it, raised only BF 78 billion. Domestic long-term funds may well cover half of the Treasury's shortfall in 1983, the remainder being funded by external borrowing and short-term financing. Although recourse to foreign borrowing has continued in 1983, with the Bank purchasing over BF 100 billion of foreign currencies from the Treasury, all of the new indebtedness occurred in the first three months of the year, with subsequent borrowings being simply to consolidate debt in the same currency. Short-term domestic financing has occurred without need of the Central Bank's assistance to the Fonds des Rentes. The ceiling on such assistance was raised to BF 210 billion in early 1983, but the available margin under the ceiling has remained large; the portfolio of Treasury certificates held by the Fonds des Rentes and financed by the Bank amounted to BF 187 billion at end-October 1983, almost the same level as at end-1982. On present trends, monetary financing of the Treasury deficit should thus decrease appreciably in 1983.

c. The liquidity of the financial intermediaries

The financial institutions have been highly liquid over the past year, as reflected by developments in the main components of their liquidity, i.e., their portfolio of short-term public securities and their unused rediscount margins at the National Bank (Table 31). The liquidity injection from Treasury operations and the additional resources supplied by greater private sector asset formation were only absorbed to a very small extent by new lending to nonfinancial enterprises and individuals. Given the reduced credit demands made upon them by the private sector, the financial intermediaries were able to increase their holdings of short-term public paper (Treasury and Fonds des Rentes certificates) by almost BF 200 billion (from BF 381 billion at end-1981 to BF 576 billion at end-1982). Public credit institutions, in particular, almost doubled their holdings of such certificates from BF 135 billion to BF 260 billion. The financial intermediaries also used their surplus funds to reduce their indebtedness to the Central Bank, cutting down on the outstanding amount of their rediscounted bills: the available margins under the rediscount ceilings thus rose from BF 31 billion to BF 44 billion between end-1981 and end-1982, and to BF 86 billion in September 1983. Since the overall ceiling on rediscount facilities was raised from BF 117 billion to BF 129 billion during the same period, 1/ the degree of utilization of such facilities by financial intermediaries (as measured by the percentage ratio of bills rediscounted to the ceilings) fell sharply from 74 percent at end-1981 to 65 percent at end-1982, and to a mere 33 percent in September 1983; the financial intermediaries' outstanding amount of rediscounted bills is now at its lowest level in several years. The reduced utilization of the Central Bank's rediscount facilities was also due to the sharp narrowing of the differential between the yield on Treasury certificates and the cost of rediscounting: whereas the difference in favor of the former had in 1981 induced banks to increase their use of rediscounting in order to subscribe to certificates, the differential contracted appreciably in December 1981 and has remained relatively small since then (even becoming negative at the end of the third quarter of 1982), detracting from the attractiveness of this form of arbitrage.

1/ The raising resulted from the application of the normal rules for the quarterly adjustment of the ceilings without any changes having been made to the method of calculation, based on coefficients applied to various elements of the financial intermediaries' statement of account. The National Bank also extended for a further period of one year (to December 1, 1983) the supplementary rediscount facility introduced in 1981 to facilitate the rediscounting of export credits with up to one year to run.

d. The monetary survey

Developments in the monetary and credit aggregates in 1982 (Tables 32 and 33) reflected a faster decline in the external drain of liquidity than in the public sector's requirement for monetary finance, or, in broad terms, a more rapid improvement in the external deficit than in the public deficit. As a result, the rate of growth of the broad money stock accelerated further, while the rate of domestic credit expansion declined marginally, remaining nevertheless much higher than that of monetary growth.

Belgium: Contribution to Changes in Money and Quasi-Money, 1981-82

(In percent and in percentage points)

	1981	1982
Change in money and quasi-money (in percent)	6.4	7.1
Contribution to change (in percentage points) of:		
Total domestic credit	15.9	14.7
Of which:		
Credit to private sector	(4.3)	(1.5)
Credit to public sector	(11.6)	(13.2)
Net foreign assets	-11.4	-7.3
Other items	1.9	-0.3

Source: Staff calculations on data from National Bank of Belgium, Bulletin.

The rate of increase of broadly defined money (money plus quasi-money), which had already quickened from 3.3 percent in 1980 to 6.4 percent in 1981, rose further to 7.1 percent in 1982. Viewed over a longer time span, these rates of growth are still more moderate than those observed in the early 1970s (when the contribution of the net foreign position to monetary growth was positive), and the rates of monetary expansion recorded since 1979 are considerably lower than those reached after the first oil crisis, when the average annual rate of growth of the broad money stock was in the order of 13 percent. The acceleration of inflation in Belgium over the last years has for its part caused a steep decline in the real monetary growth rate, which has remained low or negative since early 1980. As in past years, the rate of growth of quasi-money (10.3 percent) was considerably more buoyant than that of narrow money, even though demand for the latter quickened somewhat under the impact of lower interest rates, rising by 3.9 percent during 1982, against virtual stagnation in 1980 and an expansion of 2.3 percent in 1981. As a result of these developments, the long-term fall in the ratio of narrow money to broad money, reflecting the economies made in the holding of cash and transactions balances and their declining importance for making payments, has continued apace. The ratio fell from 84 percent in 1960 to 65 percent in 1970; in 1981, the amount of quasi-money exceeded that of narrow money for the first time, with the ratio thus falling marginally below 50 percent; it stood at 47.6 percent at end-1982. The ratio of broad money to GNP, for its part, remained unchanged at 46.5 percent in 1982, continuing to display a relatively high degree of stability.

Among the counterparts of the money supply, total domestic credit slowed down slightly from the sustained expansion recorded in 1980-81, growing by 11.2 percent from the fourth quarter of 1981 to the fourth quarter of 1982. The deceleration was totally due to a falling-off in loans to the private sector, and especially to enterprises, with the most marked fall occurring in the second semester. Credit to the private sector grew by 2.4 percent during the year (6.7 percent in 1981), and the sharp deceleration continued in the first quarter of 1983, when the private sector actually reduced its indebtedness to the banking system. The contribution of credit to the private sector in the growth of broad money thus fell from 4.3 percentage points to only 1.5 percentage points between 1981 and 1982, and became negative at the beginning of this year.

Domestic credit to the public sector, on the other hand, continued to grow rapidly during 1982, at approximately the same rate (19.5 percent) as in the previous year, picking up further in the first quarter of 1983 (20.1 percent over the first quarter of 1982). Whereas most industrial countries managed in 1982 to limit or decrease the contribution of public sector credit to money supply growth, it continued to be the main determinant in Belgium, rising to 13.2 percentage points. The expansionary effect on domestic liquidity was offset, albeit to a lesser degree than in 1981, by a decline in the net foreign assets of the consolidated banking system of BF 122.7 billion between end-1981 and end-1982, with almost all of the fall (BF 113.9 billion) occurring in the first quarter.

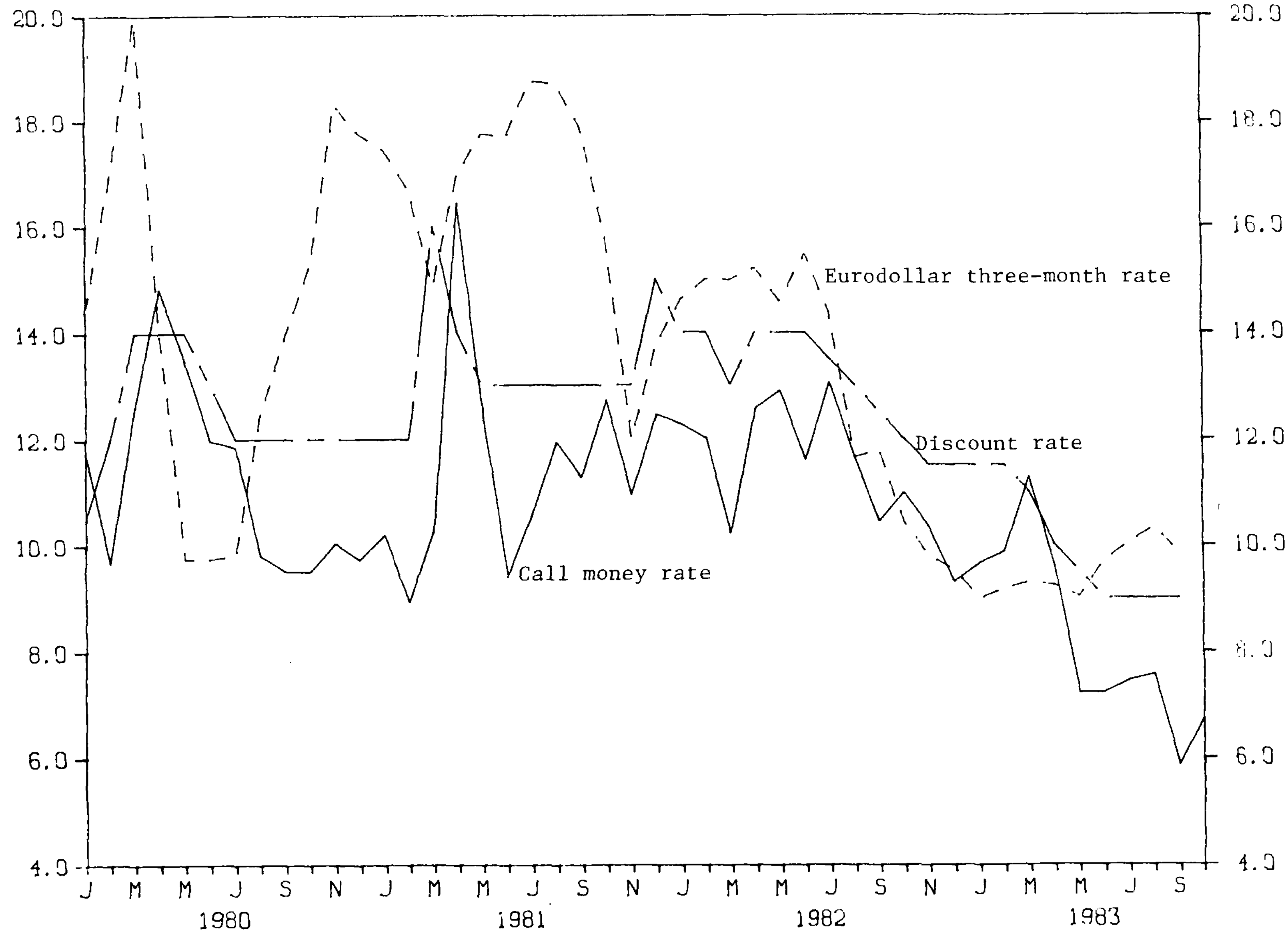
e. Interest rate management

Continued heavy borrowing by the public sector abroad and the general easing of international interest rates both contributed to alleviate the pressures on the Belgian domestic markets in the period under review (Charts 10 and 11). After the devaluation of the Belgian franc within the EMS on February 22, 1982, tensions on the exchange markets did not however subside immediately, with the Belgian franc continuing to be weak partly as a result of the currency diversification

Chart 10

Belgium: Interest Rates

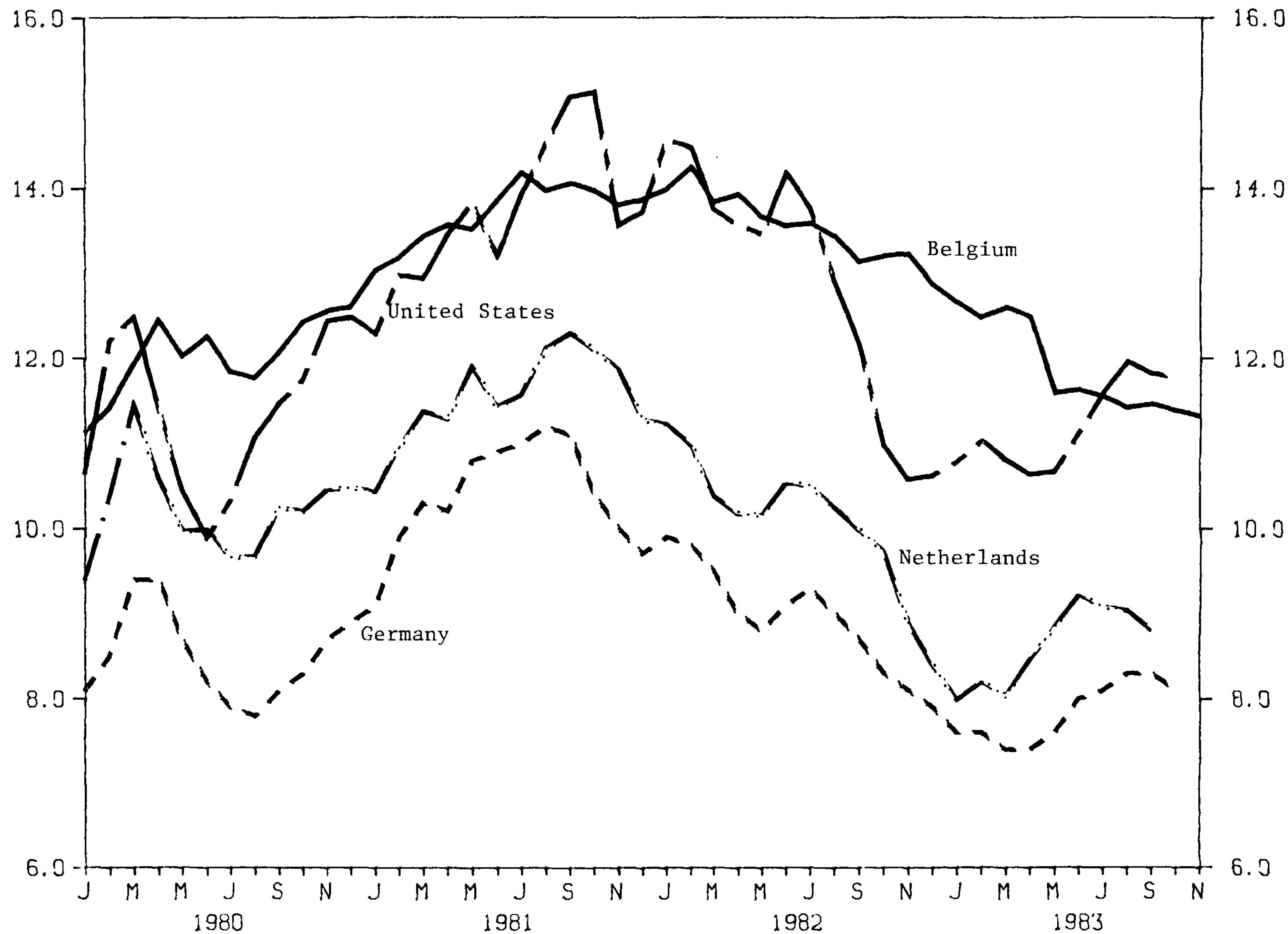
(In percent)



Source: IMF, International Financial Statistics.

Chart 11

Belgium: Government Bond Yields



Source: IMF, International Financial Statistics.

operated by Luxembourg banks. It was only in the second semester of the year--as interest rates in the United States and in Europe also began to fall significantly--that the Belgian authorities gained sufficient scope to bring down domestic interest rates from the high levels reached in the earlier months of the year. Between end-July and mid-November 1982, the official discount rate was lowered each month, in five half-percentage point steps, from 14 percent to 11.5 percent, with the rate on ordinary advances similarly being taken from 15 percent to 12.5 percent. Money market rates responded accordingly, with the rate on three-month Treasury certificates falling from 15.5 percent at the end of June to 12.25 percent at the end of the year. Bond yields, on the other hand, fell only marginally, with the rate on long-term (over 5 years) central government bonds declining from 13.59 percent to 12.87 percent over the same period, as issuing activity on the bond market--which is dominated by public sector issues--remained heavy. The resistance to a more rapid rate decline in the long-term market would indicate continued concern about the implications over the medium term of persistently large budget deficits. With bond yields thus coming down much less than money market rates, the term yield curve became positively sloped, after a protracted period of an inverted interest rate structure.

The above decline in official rates was however completely reversed in early March 1983, as the Belgian franc--together with the French franc--came under renewed pressures within the European Monetary System. With effect from March 9, 1983, the National Bank raised its discount rate from 11.5 percent to 14 percent and its rate on advances from 12.5 percent to 15 percent, i.e., to the levels they had stood at in the crisis months of early 1982. The realignment within the EMS, however, followed shortly thereafter, on March 21, 1983, so that the rise in policy-controlled rates was felt only briefly and marginally on the money markets. Given also the limited amount of rediscounting, the weighted average rate practiced by the National Bank, which measures the average cost of recourse to the lender of last resort (calculated by taking the mean of various official rates weighted by the outstanding amount of the financing obtained by the financial intermediaries at these rates), hardly rose at all between February (11.03 percent) and March 1983 (11.16 percent). The EMS realignment, in which the Belgian franc marginally revalued, restored confidence in the currency and the authorities regained scope for a new and relatively steep round of interest rate reductions, immediately (on March 24, 1983) taking the discount rate down by three percentage points to 11 percent, its lowest level in three years. Three further cuts took place in April, May and June 1983 and the official rates (discount rate of 9 percent and rate for advances of 10 percent) are now at their lowest levels since mid-1979, not having been raised even after the increases in administered rates in Germany and the Netherlands in September 1983. As a result, the positive short-term interest rate differential with Germany narrowed considerably between the first and third quarters of 1983: as measured by three-month Eurocurrency rates, it fell from 7.3 to 3.7 percentage points. Bond market conditions equally eased, with secondary market yields on government bonds over five years maturity declining from 12.6 percent in March to 11.5 percent in September 1983. The continued sharper decline in short-term interest rates than in bond yields further steepened the positive slope of the yield curve, increasing the incentive in favor of longer-term investments and favoring the domestic placement of large long-term Treasury loans in the course of 1983.

Table 25. Belgium: Sources and Uses of Base Money

(In billions of Belgian francs; end of period)

	1977	1978	1979	1980	1981	1982
Sources						
Net foreign assets 1/	220.7	211.5	166.9	190.8	126.6	83.2
Claims on public sector	82.6	95.8	133.0	158.3	231.6	264.5
Of which: Advances to the Fonds des Rentes	(2.8)	(16.0)	(52.5)	(77.1)	(149.5)	(181.1)
Rediscounts and advances	47.9	67.7	82.3	50.9	54.9	53.4
Other net	-15.3	-14.6	-10.1	-23.5	-30.5	-18.1
Total	335.9	360.4	372.1	376.5	382.6	382.6
Uses						
Currency in circulation	327.4	349.7	359.0	364.2	370.1	369.5
Banks' cash reserve holdings	8.5	10.7	13.1	12.3	12.5	13.1
Total	335.9	360.4	372.1	376.5	382.6	382.6
(Percentage growth rate)	(8.6)	(7.3)	(3.3)	(1.2)	(1.6)	(--)

Source: Staff calculations based on data of the National Bank of Belgium, Bulletin.

1/ Net of valuation changes and of net cumulative allocation of SDRs.

Table 26. Belgium: Different Measures of Base Money and Selected Ratios

(In billions of Belgian francs; end of period; and percentages)

	Base money				Unborrowed base money 1/				Domestic components of base money			
	Level	Percentage growth rate	Ratio to M2	Ratio to domestic credit	Level	Percentage growth rate	Ratio to M2	Ratio to domestic credit	Level	Percentage growth rate	Ratio to M2	Ratio to domestic credit
1966	177.1	2.9	2.5	2.1	169.2	1.6	2.6	2.2	54.9	-0.4	7.9	6.8
1967	180.2	1.8	2.6	2.2	174.4	3.1	2.7	2.3	45.7	16.8	10.2	8.8
1968	184.1	2.2	2.8	2.5	172.0	-1.4	3.0	2.7	64.5	41.1	7.9	7.1
1969	184.4	0.2	2.9	2.7	175.3	1.9	3.1	2.8	61.7	-4.3	8.7	8.1
1970	189.8	2.9	3.1	2.9	184.4	5.2	3.2	3.0	55.5	-10.0	10.5	9.8
1971	203.4	7.2	3.2	2.9	193.3	4.8	3.4	3.1	51.9	-6.5	12.7	11.5
1972	232.0	14.1	3.3	3.0	214.4	10.9	3.6	3.3	58.3	12.3	13.2	12.1
1973	260.9	12.5	3.4	3.1	237.0	10.5	3.7	3.5	67.9	16.5	12.9	12.1
1974	272.0	4.3	3.5	3.3	250.9	5.9	3.7	3.6	68.3	0.6	13.9	13.3
1975	290.0	6.6	3.8	3.6	278.8	11.1	3.9	3.7	60.7	-11.1	18.1	17.0
1976	309.1	6.6	4.0	3.9	276.6	-0.8	4.5	4.4	99.1	63.3	12.5	12.1
1977	335.9	8.6	4.0	4.1	288.5	4.3	4.6	4.8	130.5	31.7	10.3	10.6
1978	360.4	7.3	4.0	4.3	293.6	1.8	4.9	5.2	163.5	25.3	8.8	9.4
1979	372.1	3.3	4.1	4.7	289.8	-1.3	5.3	6.1	215.3	31.7	7.1	8.2
1980	376.5	1.2	4.2	5.2	325.6	12.4	4.8	6.0	209.2	-2.8	7.5	9.4
1981	382.6	1.6	4.4	5.8	328.6	0.9	5.1	6.8	286.5	37.0	5.9	7.8
1982	382.6	--	4.7	6.4	329.2	0.2	5.5	7.5	317.9	11.0	5.7	7.7

Source: Staff calculations based on data from National Bank of Belgium, Bulletin.

1/ Base money net of rediscounts and advances.

Table 27. Belgium: Financial Balances

(In percent of GNP)

	1977	1978	1979	1980	1981	1982 1/	1983 1/
Domestic financial asset formation 2/	14.6	12.8	12.1	11.1	11.1	13.2	14.0
New liabilities	15.7	15.9	17.3	17.2	19.4	17.4	17.0
Private sector 3/	(8.1)	(7.6)	(8.4)	(5.3)	(3.2)	(1.7)	(1.0)
Public sector 4/	(7.6)	(8.3)	(8.9)	(11.9)	(16.2)	(15.7)	(16.0)
Shortfall of funds	1.1	3.1	5.2	6.1	8.3	4.2	3.0
Memorandum item:							
Domestic surplus available to public sector	6.5	5.2	3.7	5.8	7.9	11.5	13.0

Sources: Staff calculations from National Bank of Belgium, Annual Report, 1982; and Bulletin.

1/ Partly estimated.
2/ Total domestic asset formation by nonfinancial agents, including foreign currency asset formation with national financial institutions.
3/ Total private sector liabilities to Belgian financial intermediaries and to Belgian nonfinancial sectors.
4/ Public sector net financing requirement.

Table 28. Belgium: Private Sector Financial Asset Formation

(In billions of Belgian francs)

	1975	1976	1977	1978	1979	1980	1981	1982	1983-S1
Domestic currency assets	328.0	384.3	411.8	396.1	385.9	375.0	359.1	507.9	131.9
Of which:									
Short term	215.7	229.9	187.5	224.8	178.1	116.0	149.2	188.8	-9.3
Long term	112.3	154.4	224.3	171.3	207.8	259.0	209.9	319.1	141.2
Foreign currency assets 1/	39.7	33.8	35.0	20.2	32.0	72.6	150.9	81.8	9.5
Of which:									
Short term	7.2	19.6	18.3	--	20.7	49.7	111.6	31.7	-4.7
(With national financial institutions)	(4.5)	(10.4)	(5.7)	(-3.8)	(8.4)	(12.9)	(41.1)	(6.1)	(-5.5)
Long term	32.5	14.2	16.7	20.2	11.3	22.9	39.3	50.1	14.2
Total 2/	356.4	464.1	451.9	451.1	465.9	467.2	593.5	623.6	134.6
Memorandum items:									
Rate of gross financial saving 3/									
In domestic currency	17.0	17.3	17.3	15.5	14.1	12.7	11.3	14.9	...
In foreign currencies	2.1	1.5	1.5	0.8	1.2	2.5	4.8	2.4	...
Foreign currency assets as percent of total asset formation	11.1	7.3	7.8	4.5	6.8	15.5	25.4	13.1	7.1

Sources: National Bank of Belgium, Annual Report, 1982; Bulletin; and staff calculations.

1/ Exchange rate adjusted changes.
2/ Including other, not shown.
3/ As percent of private sector gross disposable income.

Table 29. Belgium: Private Sector's New Liabilities

(In billions of Belgian francs)

	1976	1977	1978	1979	1980	1981	1982	1983-S1
To Belgian financial intermediaries	214	219	211	268	176	106	42	-5
To Belgian nonfinancial sector	26	12	22	6	9	10	25	24
To foreign sector	37	46	44	36	62	98	89	17
Total	277	277	277	310	247	213	156	36
(As percent of GNP)	(10.5)	(9.7)	(9.0)	(9.5)	(7.1)	(5.9)	(4.0)	(...)

Sources: National Bank of Belgium, Annual Report, 1982 and data provided by the Belgian authorities.

Table 30. Belgium: Financing of the Treasury, 1978-83

(In billions of Belgian francs)

	1978	1979	1980	1981	1982	1983 Jan.-May
Net financing requirement	182.9	211.8	296.7	454.6	508.8	337.3
Monetary financing by National Bank	24.8	78.8	117.0	286.5	251.3	72.7
Of which:						
Advances to the Fonds des Rentes	(13.2)	(36.5)	(24.7)	(72.4)	(31.5)	(-28.8)
Purchases of foreign currencies	(11.6)	(42.3)	(92.3)	(214.1)	(219.8)	(101.5)
Other financing in Belgian francs	158.1	133.0	179.7	168.1	257.5	264.6
Of which:						
Short-term	(14.4)	(6.9)	(110.1)	(141.5)	(192.5)	(176.8)
Long-term	(143.7)	(126.1)	(69.6)	(26.6)	(65.0)	(87.8)

Source: National Bank of Belgium, Bulletin.

Table 31. Belgium: Main Components of the Liquidity of Financial Intermediaries 1/

(In billions of Belgian francs)

	1978	1979	1980	1981	1982	1983-Q3
Holdings of short-term public paper 2/	108	124	244	381	576	...
Available margins under rediscount ceilings	18	18	53	31	44	86
(Degree of utilization, in percent) 3/	(80)	(80)	(51)	(74)	(65)	(33)
Total of recorded liquidity components	126	142	327	412	620	...

Sources: National Bank of Belgium, Annual Report, 1982; and Bulletin.

1/ Deposit money banks (Belgium and Luxembourg), public credit institutions and private savings banks.
2/ Short-term Treasury and Fonds des Rentes certificates in Belgian francs.
3/ Percentage ratio between bills rediscounted and rediscount ceilings.

Table 32. Belgium: Monetary Survey, 1980-83

	1980				1981				1982				1983
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1
	(In billions of Belgian francs, end of period)												
Money	772.4	817.4	783.6	806.7	798.5	873.6	799.5	824.9	821.2	880.6	851.8	856.8	840.4
Quasi-money 1/	764.2	750.4	754.3	771.4	798.0	821.5	839.6	853.8	893.1	902.9	935.5	941.6	937.9
Money plus quasi-money	1,536.6	1,567.8	1,537.9	1,578.1	1,596.5	1,695.1	1,639.1	1,678.7	1,714.3	1,783.5	1,787.3	1,798.4	1,778.3
Net foreign assets	-54.7	-7.3	-13.6	-51.9	-99.4	-108.0	-175.3	-231.0	-344.9	-340.8	-354.2	-353.7	-422.2
Domestic credit	1,807.7	1,869.1	1,872.6	1,961.0	2,022.8	2,147.6	2,148.0	2,211.5	2,326.0	2,406.2	2,414.3	2,458.2	2,565.2
Private sector	933.1	965.8	963.9	1,011.2	1,020.7	1,032.8	1,045.5	1,079.4	1,092.3	1,099.9	1,076.2	1,104.8	1,083.6
Public sector 2/	874.6	903.3	908.7	949.8	1,002.1	1,114.8	1,102.5	1,132.1	1,233.7	1,306.3	1,338.1	1,353.4	1,481.6
Other (net)	-216.4	-294.0	-321.1	-331.0	-326.9	-344.5	-333.6	-301.8	-266.8	-281.9	-272.8	-306.1	-364.7
	(Percentage changes over corresponding period in preceding year)												
Money	-0.9	-1.5	1.4	0.2	3.4	6.9	2.0	2.3	2.8	0.8	6.5	3.9	2.3
Money plus quasi-money	5.0	3.0	3.8	3.3	3.9	8.1	6.6	6.4	7.4	5.2	9.0	7.1	3.7
Domestic credit	19.8	15.8	14.8	12.3	11.9	14.9	14.7	12.8	15.0	12.0	12.4	11.2	10.3
Private sector	17.5	14.6	11.4	8.1	9.4	6.9	8.5	6.7	7.0	6.5	2.9	2.4	-0.8
Public sector 2/	22.2	17.1	18.8	17.2	14.6	23.4	21.3	19.2	23.1	17.2	21.4	19.5	20.1

Sources: National Bank of Belgium, Bulletin; and staff calculations.

1/ Excluding certificates of deposits and bonds (bons de caisse et obligations).
2/ Including advances to the Fonds des Rentes.

Table 33. Belgium: Components of Money and Quasi-Money

(In billions of Belgian francs, end of period)

	1975	1976	1977	1978	1979	1980	1981	1982
National Bank								
Base money	290.0	309.1	335.9	360.4	372.1	376.5	382.6	382.6
Of which:								
Currency in circulation	(281.2)	(299.5)	(327.4)	(349.7)	(359.0)	(364.2)	(370.1)	(369.5)
Deposit money banks								
Demand deposits (in BF)	236.3	248.1	278.6	291.7	296.8	293.7	306.9	334.6
Time deposits (in BF)	434.2	518.8	560.4	623.3	684.5	716.5	748.3	814.4
Foreign currency deposits	23.0	31.4	35.8	29.8	37.7	54.1	103.8	125.8
(p.m.: Certificates of deposit and bonds)	(58.2)	(74.3)	(104.4)	(125.6)	(153.0)	(201.0)	(245.0)	(300.2)
Public monetary institutions 1/								
Liabilities to private sector	85.1	92.4	97.7	103.5	104.0	106.5	110.9	112.5
Liabilities to public sector	35.9	43.1	36.8	39.6	43.6	41.3	34.7	38.1
Totals								
Money	640.3	684.1	741.5	784.9	804.7	806.7	824.9	856.8
Quasi-money 2/	457.5	550.5	596.9	654.0	722.9	771.4	853.8	941.6
Money and quasi-money	1,097.8	1,234.6	1,338.4	1,438.9	1,527.6	1,578.1	1,678.7	1,798.4
Memorandum item:								
Liquidity ratio 3/	47.2	46.7	46.9	47.0	46.9	45.5	46.5	46.5

Sources: National Bank of Belgium, Bulletin; and staff estimates.

1/ Consolidation of the Belgian Monetary Fund, the Belgian Municipal Credit Institution, the Rediscount and Guarantee Institute, and the Postal Cheque Office.
2/ Excluding certificates of deposit and bonds.
3/ Money and quasi-money as a percent of nominal GNP.

IV. External Sector 1/

1. Exchange rate developments

For many years a key objective of economic policy in Belgium has been the stability of the exchange rate vis-à-vis the principal trading partners. In practice this has meant the participation of Belgium in the original "snake" exchange rate arrangement and, later, in the European Monetary System (EMS). The attainment of the exchange rate objective has sometimes had to rely on the existence of a two-tier exchange system, in which the official franc, used mainly for current transactions, is linked to EMS currencies, and the financial franc, used mainly for capital transactions, is freely floating. Although the separation of transactions between the two markets has become increasingly difficult, this arrangement has helped to protect official reserves during periods of exchange market unrest and has made it largely unnecessary to impose restrictions on capital flows other than the prescription of the exchange market through which they had to be channeled.

The Belgian franc was devalued by 8.5 percent on February 21, 1982 against all participating EMS currencies, except the Danish kroner which was devalued at the same time by 3 percent. The devaluation was preceded by massive capital outflows which, on occasion, raised the spread between the official and the financial rate above 10 percent and--despite the dual exchange market regulations--spilled over into the official market where they aggravated the loss of reserves due to speculative adjustments in trade flows. 2/ After the devaluation, the Belgian franc assumed temporarily a position of relative strength within the EMS and its rate moved away from the lower intervention limit (Chart 12). However, confidence in the Belgian franc was not yet fully restored and speculations about a more comprehensive realignment within the EMS added to the renewed weakening of the franc, causing a substantial further loss of reserves and a renewed increase in the exchange rate spread to close to 10 percent. The exchange market situation calmed down after the EMS realignment of June 1982 3/ and the National Bank of Belgium regained a part of the reserves it had spent on interventions in the first half of 1982; 4/ the exchange rate spread diminished but continued to be larger than on average in 1978-80 (Table 34).

1/ Unless otherwise indicated, developments described in this chapter refer to the BLEU.

2/ In the first quarter of 1982, the loss of net official assets amounted to some US$204 million (Table 34).

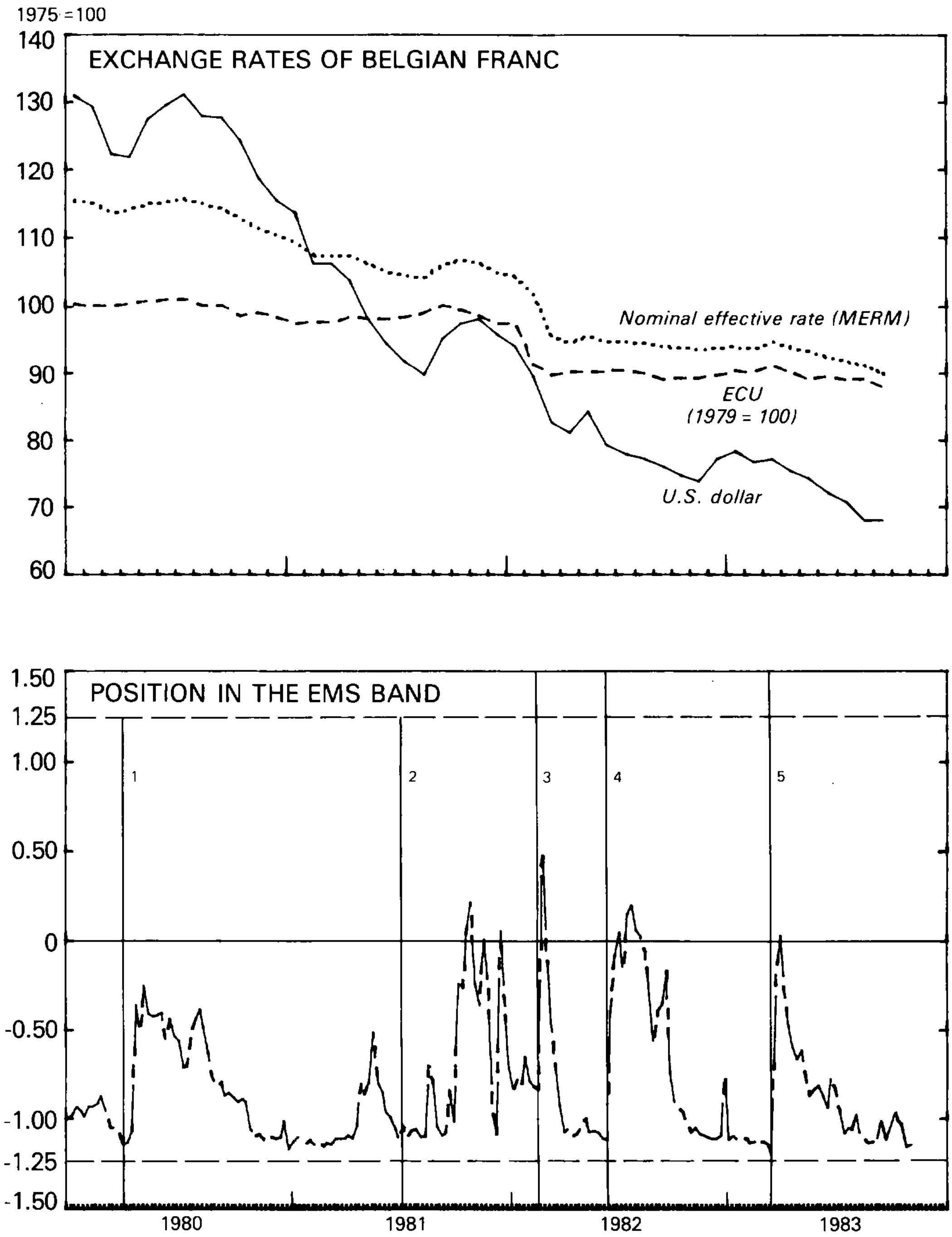
3/ In this realignment, the deutsche mark and the Netherlands guilder were revalued by 4.25 percent and the French franc and the Italian lira were devalued by 5.75 percent and 2.75 percent, respectively. The impact effect left the nominal effective exchange rate of the Belgian franc virtually unchanged against the EMS currencies while it resulted in an effective depreciation of 1 1/2 percent against all currencies.

4/ The reserve position also improved on account of the fall in the current account deficit and continued large-scale external borrowing of the public sector.

CHART 12

BELGIUM

EXCHANGE RATE DEVELOPMENTS



[1]Devaluation of Italian lira by 6.0 percent.
[2]Revaluation of deutsche mark and Netherlands guilder by 5.5 percent; devaluation of French franc and Italian lira by 3.0 percent.
[3]Devaluation of Belgian franc by 8.5 percent; devaluation of Danish kroner by 3.0 percent.
[4]Revaluation of deutsche mark and Netherlands guilder by 4.25 percent; devaluation of French franc by 5.75 percent and of Italian lira by 2.75 percent.
[5]Revaluation of Belgian franc by 1.5 percent, of Danish kroner by 2.5 percent; of deutsche mark by 5.5 percent, and of Netherlands guilder of 3.5 percent; devaluation of French franc and of Italian lira by 2.5 percent and of Irish pound by 3.5 percent.

Toward the end of 1982 and in early 1983, speculative pressures reemerged within the EMS. Although the Belgian franc was not the target of speculation, it came under pressure on account of expectations about adjustments in other currency rates. The exchange rate spread widened again and reserve losses increased. In the March 20, 1983 EMS realignment the Belgian franc was revalued by 1.5 percent. As in the case of the June 1982 realignment, the impact effect of the realignment left the nominal effective exchange rate of the Belgian franc unchanged vis-à-vis EMS currencies and resulted in a depreciation by 1 1/2 percent vis-à-vis all currencies. After the realignment, net (private) capital flows of Belgium turned around to a more significant extent than ever after a change in parities within the EMS. Within less than two months the National Bank had recouped the reserve losses of the unrestful period before the realignment. A particularly forceful indicator of the relative strength of the Belgian franc was the virtual elimination of the spread between the official and the free market exchange rate (Table 34). 1/ Furthermore, the discount and advances rates were lowered in successive steps by 2 1/2 percentage points without visible effects on capital flows and the exchange rate spread. Finally, effective May 26, 1983 the authorities permitted banks to sell in the official market foreign exchange acquired in the free market. The intention was to avoid the emergence of a positive exchange rate spread which could have hampered the observed reflow of capital or even have invited new outflows. 2/

The devaluation of February 1982 dominated the fall of the Belgian franc against the ECU by an average of 7.9 percent in 1982, compared with a 1 percent depreciation in 1981. Some strengthening of the Belgian franc vis-à-vis the ECU in the first quarter of 1983 was followed by a renewed decline in the second and third quarters. The fall in the second quarter was probably more a result of technical factors before and after the March 1983 realignment than a reflection of shifts in the strength of the Belgian franc. 3/ Along with other EMS currencies, the exchange rate of the Belgian franc has registered large fluctuations in relation to non-EMS currencies. After a depreciation against the dollar by 21 percent in 1981, the Belgian franc continued to fall for most of 1982 and, in the event, depreciated on average by almost 19 percent (Table 34). A short recovery in the first quarter of 1983 was followed by a renewed drop from end-March onward which continued into late 1983.

1/ The fact that the Belgian franc has nevertheless remained mostly at the bottom end of the EMS band reflects the interest rate and intervention policy of the Belgian authorities and is less significant for an evaluation of the relative strength of the Belgian franc.

2/ The derogation to the regulation whereby foreign exchange purchased by the banks in one market may not be sold in the other, opened a one-way link between the free and the official market and left in essence capital outflows as the only major transaction which has to go through the free market.

3/ When evaluating the exchange rate vis-à-vis the ECU, it also has to be remembered that ECU rates are influenced by movements of the pound sterling. These were erratic and entailed no obligation to intervene.

In nominal effective terms (MERM), the cumulative depreciation of the Belgian franc in 1981-82 amounted to 16 1/2 percent. Some strengthening in the first quarter of 1983 was followed by a renewed and accelerating depreciation in the next six months. Nevertheless, the drop in the MERM rate slowed to 4 percent in the first nine months of the year, compared with an average drop of 11.5 percent in 1982.

2. Balance of payments 1/

a. General overview

The policy measures taken by the Belgian authorities in February 1982 have in the course of 1982 and so far in 1983 substantially reduced the external constraint on domestic policy. After many years of steady deterioration, most components of the balance of payments improved significantly in 1982 (Tables 35 and 36). The trade deficit declined by BF 11 billion from BF 134 billion in 1981 to BF 123 billion in 1982. 2/ The improvement in the services balance by BF 25 billion was even more pronounced, owing primarily to a strong reduction in the travel deficit which accompanied the sharp drop in households' real disposable income. By contrast, the transfer balance deteriorated further on account of an increase in the contributions to the European Communities. Altogether, the current account deficit (transactions basis) of the BLEU was reduced from 4 percent of GDP in 1981 to an estimated 3 percent in 1982. 3/ The drop in the current account deficit was accompanied by a virtually unchanged level of public sector foreign borrowing (BF 256 billion) which eased the liquidity situation considerably while, at the same time, private sector demand for credit slowed perceptibly. Private capital outflows (excluding trade finance) therefore rose to BF 171 billion in 1982, compared with BF 157 billion in 1981. However, selective policy measures which provided incentives to invest in Belgian financial assets, and an apparent increase in investors' confidence kept private capital outflows in check despite high liquidity and adverse exchange rate expectations (see above). In the event, the loss of net reserves of the National Bank was reduced from BF 96 billion in 1981 to BF 38 billion in 1983. This improvement strengthened in the first half of 1983 when net reserves increased by BF 58 billion, compared with a loss of BF 31 billion a year earlier.

1/ The discussion in this section refers to balance of payments developments of the Belgium-Luxembourg Economic Union (BLEU).

2/ Measured on a transactions basis and excluding third country trade. On a cash basis, the trade deficit was reduced from BF 178 in 1981 to BF 115 in 1982 and the current account deficit from BF 199 billion to BF 119 billion.

3/ Measured in percent of the combined GDP of Belgium and Luxembourg.

b. Current account developments 1/

In 1982, the current account deficit of the balance of payments was reduced by BF 30 billion to BF 125 billion (Table 36). The swing in the current account was even more significant--an improvement of BF 43 billion was registered--if official transfers are excluded. The improvement in the current account in 1982 occurred despite a record deficit of BF 108 billion in the first half of the year. It is notable that this sharp break from a long period of growing deficits was achieved at a time of sluggish growth in world trade and under conditions of a deterioration in Belgium's relative cyclical position (Chart 13). By contrast, a favorable factor was the fact that the sharp fall in the terms of trade in 1980 and 1981 came to a halt in 1982 despite the devaluation. A considerable deceleration in the growth of world market prices of major imported goods and a swift upward adjustment of export prices of domestic producers following the devaluation account for this development. In the first half of 1983, the favorable development of the current account continued despite a large increase in speculative trade flows in the first quarter. In the event, the current account deficit (cash basis) was reduced from BF 104 billion in the first half of 1982 to BF 24 billion in the same period in 1983.

An analysis of current account developments from the perspective of sectoral financial balances, 2/ and restricted to Belgium, suggests that the improvement in the current account in 1982 was to a large extent the result of the income redistribution which followed the February 1982 policy measures. An increase in the financial surplus of the enterprise sector--by 1 percent of GDP--was only partly offset by the decline in the surplus in the household sector (by 0.9 percent of GDP) (Table 37). The devaluation increased the scope for price increases of firms without loss of competitiveness, while the wage restraint measures at the same time reduced the costs of firms and lowered wage and salary incomes of workers. The related fall in households' disposable income translated into a considerable slowing in household spending notably investment spending. The financial surplus of households therefore fell only moderately. At the same time, the sharp increase in enterprises' operating surpluses did not immediately generate an offsetting spending response of enterprises, thus raising their financing capacity. The resulting improvement in the current account was strengthened by the slowing of public sector spending growth in 1982 which was accompanied by a strong revenue growth. In the event, the financing requirement of the public sector dropped as a percentage of GDP for the first time since 1974. Taken together, the large redistribution of incomes between sectors and their concomitant spending responses led to the first improvement in Belgium's current account in many years; a development which appears to be strengthened in 1983 as the redistribution of incomes continues.

1/ Unless otherwise indicated, the discussion in this section refers to data on a transactions basis.

2/ National accounts aggregates.

c. Merchandise trade 1/

Although the trade balance on a customs basis remained almost unchanged in 1982 from a year earlier, the improvement within the year was remarkable for both the overall and the non-oil balance. The overall trade balance moved from a deficit of BF 106.6 billion in the first quarter of the year to a deficit of BF 16.5 billion in the fourth quarter (Table 38). All of the improvement occurred in the non-oil trade balance which moved from a deficit of BF 55 billion in the first quarter into a surplus of BF 38 billion in the fourth quarter. The swift improvement in the trade balance was the result of (a) the virtual absence of a negative terms of trade effect despite the devaluation in February 1982; and of (b) a sizable volume response, notably of imports, in the second half of the year. On the other hand, the volume growth of exports was less pronounced than could have been expected from the gains in price and cost competitiveness (Chart 13) deriving from the February policy package and from the continued depreciation of the Belgian franc later in the year. The data in Table 39 suggest that exporters, faced with the options of (a) moderate price increases combined with larger gains in market shares; or (b) higher price increases at more moderate volume growth, chose the latter option. In the event, the improvement in overall export performance 2/ slowed in 1982 to 1.2 percent, from 1.7 percent in 1981, while, at the same time, domestic exporters raised their prices such that the export price advantage over competitors 3/ declined from 9.6 percent in 1981 to 3 percent in 1982 (Table 39). The result is somewhat different when looking at non-oil trade. Here, export performance improved in

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1/ Data are on a customs basis and cover the entire BLEU. Normally, large differences exist between data on transactions and customs basis. The discrepancies between transactions data and customs data in the BLEU recording of external transactions arise from the following factors.

-- The customs data are f.o.b. for imports and c.i.f. for imports, while transactions data are f.o.b. for both exports and imports to the extent possible.

-- The customs data regarding trade over the Belgium-Netherlands border are imperfectly recorded, owing to the limited controls exercised on that border. The transactions data contain an estimate of this trade.

-- Customs data record separately temporary imports and exports for reprocessing, while the transactions data record only net receipts or payments for reprocessing.

-- The exchange rate applied to customs data may be different from that used for transactions data, because of timing differences. The value applied to merchandise at the customs is market price, which may differ from the actual price resulting from the exchange records statistics, which is used for the transactions data.

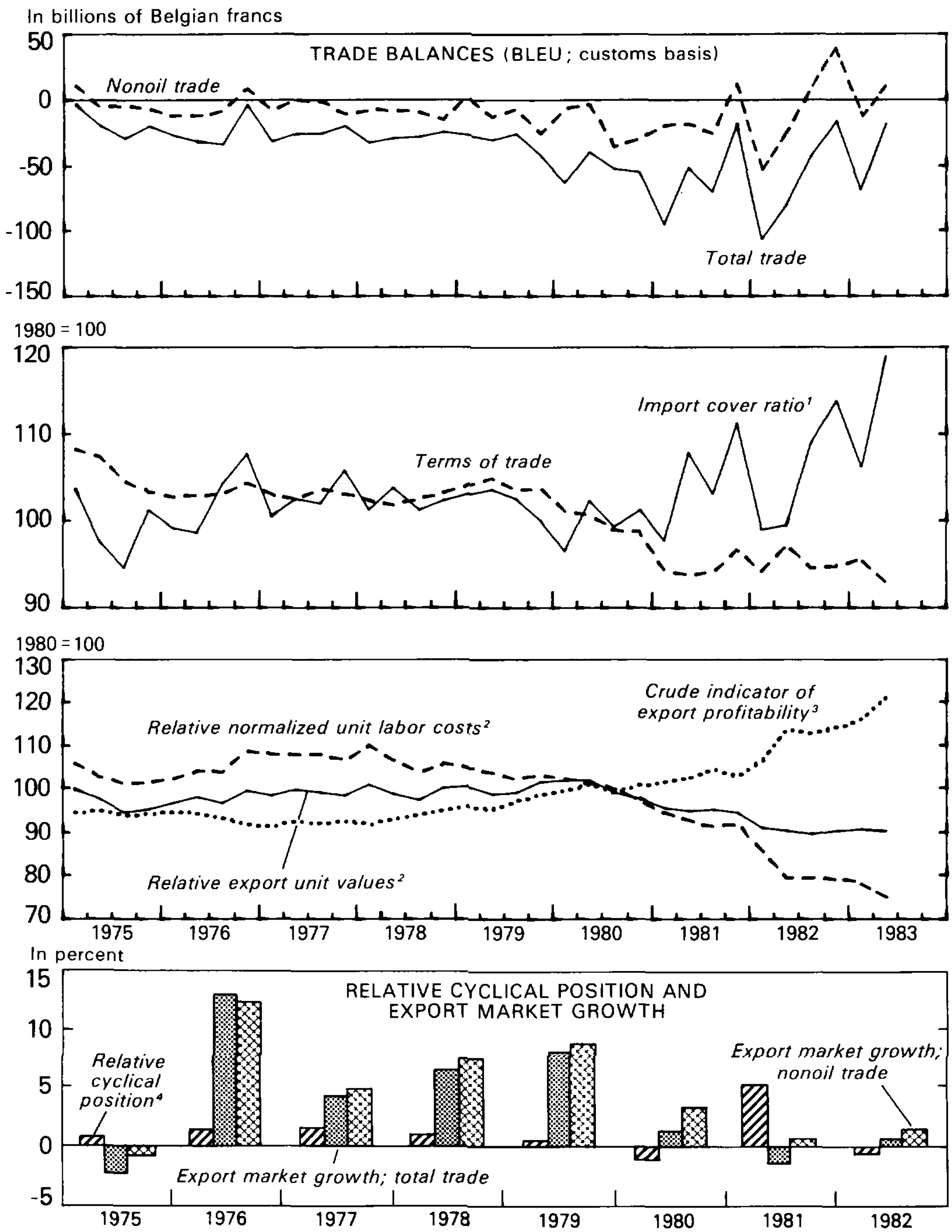
2/ Measured as the difference between export market growth and observed export growth for total trade.

3/ Measured as the growth of relative export unit values in common currency.

CHART 13

BELGIUM

BALANCE OF PAYMENTS INDICATORS



[1] Ratio of export volume to import volume indexes.
[2] In common currency.
[3] Ratio of export unit value to unit labor cost indexes.
[4] Growth rate of total domestic demand in all industrial countries minus corresponding growth rate for Belgium, a positive value indicates a favorable cyclical position.

1982 and, as a result the first gain in market shares was recorded after six consecutive years of losses and stagnation. However, apparently again on account of the pricing policy of exporters examined earlier, the gain was rather modest (0.6 percent) given the large effective depreciation of the Belgian franc. Although the rate of depreciation of the Belgian franc increased in 1982, the improvement in price competitiveness more than halved to 3.5 percent, compared with 7.5 percent in 1981. 1/ Thus, even in non-oil trade, price adjustments appear to have dominated over volume changes. Preliminary data on the first half of 1983 suggest, that there has been some strengthening of the volume response of exporters. However, there is no evidence that exporters are actually seeking gains in market shares at the expense of profitability per unit sold. While the pricing policy of exporters was a major factor for the large increase in enterprises' profitability and their operating surplus, (Table 11 and Chart 13), it appears to have reduced demand and, thus, actual growth of output and employment below achievable rates. 2/

In early 1983, the trade balance (customs basis) deteriorated very significantly ahead of the EMS realignment (BF -70 billion in the first quarter; see Table 38). The anticipation of important exchange rate adjustments thus appears to have again exercised a strong influence on trade flows and the terms of payments. After the realignment, the import and export volume growth assumed again the pattern which had prevailed in the second half of 1982. In the second quarter of 1983, the import cover ratio improved by 13 1/2 percent, reflecting a growth of export volumes of 3 1/2 percent and a drop in import volumes of 9 percent. The trade deficit shrunk to BF 19 billion in the second quarter of 1983, compared with a deficit of BF 83 billion in the second quarter of 1982. There are thus strong indications that the trade balance is heading for a major improvement in 1983.

The structure of BLEU trade changed quite significantly in 1982 (Table 40). Most important was the increase in exports of consumer durables (5.8 percent) which was accompanied by an equally large decline in imports of consumer durables (-4.2 percent). Thus, within a year, the export/import ratio of consumer durables improved by a full 10 percentage points. The ratio for consumer nondurables also rose, albeit only moderately, while the ratios of primary products and investment goods fell. The latter development may more reflect the strengthening of the investment climate in Belgium relative to partner countries, rather than attest to a loss of price and/or nonprice competitiveness

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1/ In manufacturing, price competitiveness--measured by relative export unit values in common currency--appears to have improved on average in 1982 at an unchanged pace from a year earlier (Table 39 and Chart 13).

2/ In some export industries the choice between price and volume adjustments may, however, have been dictated by production constraints which did not permit an expansion of production to the extent of incipient demand. This would attest to the need for structural adjustment in the traded goods sector.

of Belgian producers of investment goods. In early 1983, the export/import ratio of investment goods improved again on account of a drop in imports. The trade balance with EMS countries deteriorated in 1982 (Table 41), despite the first devaluation of the Belgian franc against other EMS currencies. 1/ However, the trade balance with all industrial countries taken together improved, as did the balance with oil-producing countries.

d. Services account

In 1982, the services account surplus increased by BF 24.7 billion to BF 27 billion (Table 42). The swing in the service account was the main contributing element to the improvement in the current account balance. Of particular importance was the fall in the travel deficit from BF 47 billion in 1981 to BF 28 billion in 1982. Outlays of Belgian travelers declined sharply, reflecting the strong drop in households' real disposable income. On the other hand, foreign travel to Belgium picked up on account of improved price competitiveness which was also a major factor for the improvement in the transportation and insurance balance by BF 12 billion. By contrast, the deficit on investment income rose by BF 5.3 billion to BF 8.3 billion, notwithstanding a sharp increase in incomes from financial intermediation of Belgian and Luxembourg banks. However, this increase was more than compensated by the strong growth in interest payments on public sector foreign debt.

e. Capital account

The very wide and diverging gap between capital movements of the private and public sectors which had emerged in 1981, with a sharp rise in public foreign borrowing (BF 258 billion) being accompanied by heavy net private capital outflows (BF 201 billion), was marginally reversed in 1982. While public sector foreign borrowing remained at approximately the same level (BF 256 billion), net private capital outflows were some BF 39 billion lower than in 1981, amounting to BF 162 billion (Tables 43, 44 and 45). In the first semester of 1983, public sector borrowing abroad declined considerably with respect to the corresponding period of 1982 (falling from BF 168 billion to BF 100 billion), with most of the borrowing taking place in the first three months of the year. The private sector's net capital movements were broadly in balance, with strong outflows in the first quarter being reversed after the March 1983 realignment. Incipient private capital outflows reappeared however in the course of the third quarter, as the interest rate differential in favor of the Belgian franc narrowed considerably.

The slowdown in net private capital outflows in 1982 (Table 46) was the result of a number of contrasting developments. The main improvement was in the short-term operations of both residents and nonresidents. Residents' net foreign currency assets with banks in the BLEU, which had increased steeply in the course of 1981 (by BF 86 billion), rose more

1/ Trade balance measured in U.S. dollars.

slowly, by BF 53 billion, in 1982. The turnaround was even more evident in nonresidents' net Belgian franc assets with BLEU banks. Nonresidents' holdings of Belgian francs had been converted massively into foreign currencies in the course of 1981, declining by BF 52 billion and reaching a minimum needed to finance transactions. They were reconstituted for an amount of BF 16 billion in the course of 1982. In 1983, developments in residents' and nonresidents' short-term operations differed markedly between the first and second quarters, showing a notable improvement after the March 1983 realignment within the EMS.

The positive impact of these developments on the capital account were however largely offset in 1982 by a sharp increase in the banking sector's net foreign currency assets (by BF 111 billion), largely as a result of the Luxembourg banks' conversion of part of their Belgian franc assets after the devaluation of February 1982. The currency diversification was carried out mainly by the Luxembourg subsidiaries of German banks, who had traditionally kept their capital and reserves in Luxembourg or Belgian francs, but decided to convert them back into the currency of the parent bank after the devaluation.

The decline in residents' preference for short-term foreign currency assets in 1982 was partly offset by a shift in favor of longer-term portfolio investments in foreign securities, which rose by BF 56 billion (BF 41 billion in 1981). This shift continued in 1983. Foreigners' portfolio investments in the BLEU recorded a relatively high net inflow for the first time since 1979. While Belgian and Luxembourg companies actually disinvested abroad, foreign direct investment in the BLEU continued to be substantial, rising from BF 52 billion in 1981 to BF 68 billion in 1982. Finally, Belgian enterprises had a lesser recourse to long-term loans abroad, as the possibilities of raising funds, especially risk capital, on the domestic markets improved substantially.

The loss in the National Bank's net official reserves (after valuation adjustments) was thus limited to BF 37.5 billion in 1982, against BF 95.7 billion in 1981. There was a significant change in the composition of reserves: whereas in 1981 the decline was reflected mainly in an increase in net ECU liabilities to the European Monetary Cooperation Fund (EMCF), in 1982 it was totally attributable to a very sharp fall in the National Bank's holdings of convertible foreign currencies, essentially in U.S. dollars (Tables 47 and 48). The decline, which was concentrated in the first and last quarters of the year, brought such holdings down from BF 112 billion at the end of 1981 (46 percent of total reserves) to a mere BF 49 billion (24 percent of total reserves) at the end of 1982, its lowest level in several years. The loss of reserves continued apace in the first quarter of 1983, with a decline of BF 41 billion, due especially to a build-up of liabilities vis-à-vis the EMCF following extensive recourse to the very short-term financing facility for interventions within the EMS. Liabilities to the EMCF peaked at BF 102 billion in the week ending on March 14, 1983. Following the realignment of March 22, 1983, the National Bank was able to substantially replenish its reserves, totally reimbursing the debt to the EMCF as from early June. The first semester of the year actually recorded a net gain in reserves of BF 58 billion. However, gross reserves (excluding gold) still fall short of covering a month of imports of goods and services, and the reserve/import ratio, at 6.5 percent, remains low by international standards (Table 49); by way of comparison, the reserve/import ratio for all countries was 19.1 percent at end 1982, and reached an average 22.8 percent for Japan, Germany and Switzerland. 1/ With respect to the composition of reserves, the share of convertible foreign exchange remains rather small, amounting to only about 20 percent of total reserves; at BF 50 billion (end October 1983) it is equal to less than half the foreign exchange held by the National Bank in early 1981.

3. Exchange and trade relations

Since the last Article IV consultation with Belgium, the most important change in the exchange and trade system consisted in a modification of the dual exchange market arrangements, 2/ with effect from May 26, 1983. The change takes the form of a derogation to the regulation whereby foreign currencies purchased in one exchange market may not be sold on the other, opening a one-way link between the two markets by allowing authorized banks to sell on the official market currencies acquired on the financial (free) market. As a consequence, the financial exchange rate for the Belgian franc cannot show a premium relative to the official rate, which acts as an effective ceiling for the financial rate. Under such an arrangement, capital inflows are not discouraged and capital outflows not encouraged. However, the possibility remains for the financial rate to move to a discount relative to the official rate, thereby discouraging capital outflows. Since the introduction of this change it has been observed that the spread between the two rates has seldom narrowed to less than 0.5 percent; this would seem to be attributable to the fact that whenever the spread approaches 0.5 percent, nonresidents tend to sell financial francs forward, buying them for delivery as soon as the spread widens again. Given that the free rate cannot rise above the official rate, the operation is practically risk-free.

Other exchange measures were introduced by the Belgium-Luxembourg Exchange Institute (IBLC) in early March 1983 to counter mounting pressures on the exchange rate, as follows: (a) foreign currency export receipts could no longer be deposited in residents' convertible foreign exchange accounts, but would have to be sold immediately on the official market; existing foreign exchange assets on such accounts were to be

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1/ Bank for International Settlements, Fifty-Third Annual Report, June 1983.

2/ For a description of the arrangements as at December 31, 1982, see International Monetary Fund, Annual Report on Exchange Arrangements and Exchange Restrictions, 1983, pp. 96-100.

either used or converted on the official market by April 15, 1983; (b) each bank's ceiling on its foreign currency spot long position (position à la hausse) on the official market was reduced to BF 20 million, putting an end to the higher individual ceilings which had been granted to the major banks in relation to the overall volume of their operations; 1/ and (c) from March 14 to March 22, a penalty rate of interest, payable to the IBLC, was charged on advances on nonresidents' convertible franc accounts. The easing of exchange rate tensions following the EMS realignment of March 21, 1983 induced the authorities to abrogate as from April 5, 1983, the first of these measures, which constituted a severe constraint on firms engaged in foreign trade.

The exchange rate system of Belgium and Luxembourg was reviewed on the occasion of the 1982 Article IV consultation, when it was noted that the maintenance of dual exchange rates gave rise to a multiple currency practice subject to Fund approval under Article VIII, Section 3; approval for the maintenance of the practice was not granted. The spread between the two markets has narrowed to less than 2 percent since April 1983, thus eliminating the multiple currency practice for the time being.

4. Development assistance

Belgian official development assistance (ODA) increased by 7 percent in 1982, remaining unchanged as a percentage of GNP from 1981 (0.59 percent in both years). For 1983, budgetary outlays for ODA represent 0.62 percent of GNP, and the authorities remain committed to the achievement of the 0.7 percent aid target.

1/ This measure was dictated by the fact that part of the speculation against the Belgian franc came from nonresidents, through forward sales of convertible francs, which the banks would cover with spot purchases of foreign assets (or liquidation of foreign liabilities). Since the traditional structure of Belgian foreign trade (with forward sales of foreign currencies by exporters exceeding forward purchases by importers) would normally induce banks to take a short foreign currency spot position (position à la baisse), the appearance of a long position may be taken as an indication of speculation by nonresidents.

Table 34. Belgium: Exchange Rate Developments of the Belgian Franc

(Changes in percent from preceding period)

	U.S. Dollar		ECU		MERM	Real	Memorandum Item:
	Rate	Spread 1/	Rate	Divergence Indicator 2/	Rate	Effective 3/ Exchange Rate	Change in Net Official Assets 4/
1975	6.0	...	...	...	1.0	1.0	523
1976	-4.8	...	...	...	1.4	1.2	-577
1977	7.6	...	...	...	5.6	12.0	-111
1978	13.9	-1.5	...	...	3.7	-0.9	-336
1979	7.3	-2.8	...	...	2.4	-3.3	-1,445
1980	0.4	-1.5	-2.5 5/	-44.5	-0.2	-4.2	1,212
1981	-21.0	-5.2	-1.0	-51.2	-6.8	-9.5	-1,931
1982	-18.7	-6.5	-7.9	-30.3	-9.8	-11.5	-536
1982							
1st quarter	-8.7	-9.8	-7.9	-38.0	-5.2	-4.1	-204
2nd quarter	-8.1	-9.1	0.7	-41.6	-5.5	-9.7	-211
3rd quarter	-5.4	-5.6	-1.4	-14.1	-0.6	0.8	1,227
4th quarter	-2.4	-3.5	0.7	-57.7	-0.6	2.3	-1,348
1983							
1st quarter	2.9	-4.5	1.7	-55.7	0.4	-1.5	-699
2nd quarter	-4.6	-0.6	-1.9	-28.2	-1.0	-1.3	2,038
3rd quarter	-6.6	-0.7	-1.1	-54.2	-2.2	...	-542

Sources: International Monetary Fund, International Financial Statistics.

1/ Spread between official and financial rate in percent.
2/ Divergence from central rate in percent of maximum permissible divergence (+/- 100 percent).
3/ Relative unit labor costs in common currency.
4/ Changes in millions of U.S. dollars.
5/ Relative to average of March-December 1979.

Table 35. BLEU: Balance of Payments Summary

(In billions of Belgian francs, and in percent) 1/

	1978	1979	1980	1981	1982	1982				1983	
						Q1	Q2	Q3	Q4	Q1	Q2
Trade balance	-42	-92	-117	-134	-117	-75.5	29.0	-1.4	-10.6	52.6	19.6
Third country trade	8	19	8	25	24	7.2	7.6	10.2	-0.7	0.1	15.4
Services balance	33	12	3	3	27	1.6	8.4	5.9	11.1	-4.4	13.1
Transfer balance	-26	-28	-38	-48	-56	-14.0	-16.2	-15.2	-10.5	-14.9	-18.9
Current account balance	-26	-89	-144	-155	-122	-80.7	29.2	-1.0	-10.7	-71.8	29.2
In percent of GDP 2/	(-0.8)	(-2.6)	(-3.9)	(-4.1)	(-3.0)	(...)	(...)	(...)	(...)	(...)	(...)
Private capital flows, net	-2	-11	1	-201	-162	- 2.1	-70.7	9.2	-98.4	...	...
Public capital flows, net	8	72	154	258	256	73.7	88.0	44.0	44.4	87.4	12.1
Capital account balance	6	61	155	57	94	77.6	17.3	53.2	-54.0	...	...
Errors and omissions	4	-4	16	-2	-10	-7.7	-8.2	8.1	-1.8	-15.6	4.4
Overall balance 3/	-16	-32	27	-96	-8	-10.8	-20.5	60.3	-66.5	-41.4	99.3

Sources: National Bank of Belgium, Bulletin; and International Monetary Fund, International Financial Statistics.

1/ Transactions basis, except for current account data for 1983 which are on a cash basis. Data for 1982 are preliminary.
2/ GDP of the BLEU.
3/ Equal to changes in the net official reserves of the National Bank of Belgium.

Table 36. BLEU: Current Account Developments

(In billions of Belgian francs) 1/

	1978	1979	1980	1981	1982 2/	1982 2/ Q1	1982 2/ Q2	1982 2/ Q3	1982 2/ Q4	1983 2/ Q1	1983 2/ Q2
Exports 3/	1,295	1,550	1,734	1,932	2,307	507.4	592.4	570.0	637.2	592.7	603.0
Imports 3/	1,337	1,642	1,851	2,066	2,424	582.5	621.4	571.9	647.8	645.3	583.4
Trade balance	-42	-92	-117	-134	-117	75.5	-29.0	-1.9	-10.6	-52.6	19.6
Third country trade	8	19	8	25	24	7.2	7.6	10.2	-0.7	0.1	15.4
Service exports	529	669	939	1,367	1,562	366.9	400.4	411.5	383.0	366.8	357.6
Service imports	497	557	936	1,364	1,535	365.3	392.0	405.6	371.9	371.2	344.5
Services balance	32	12	3	3	27	1.6	8.4	5.9	11.1	-4.4	13.1
Private transfers	-9	-10	-11	-15	-11	-3.9	-3.2	-1.8	-2.1	-2.5	-2.4
Official transfers	-16	-18	-27	-33	-45	-10.1	-13.0	-13.4	-8.4	-12.4	-16.5
Transfer balance	-25	-28	-38	-48	-56	-14.0	-16.2	-15.2	-10.5	-14.9	-18.9
Current account											
Excluding official transfers	-10	-71	-117	-122	-77	-70.6	-16.2	12.4	-2.3	-59.4	45.7
Including official transfers	-26	-89	-144	-155	-122	-80.4	-29.3	-1.0	10.7	-71.8	29.2
Memorandum item:											
Trade balances; cash basis	-63	-95	-137	-178	-112	-46.4	-52.6	-2.0	-14.5	-52.6	19.2
Current account; cash basis	-47	-92	-164	-199	-116	-51.6	-52.8	-2.9	-14.6	-71.8	29.2

Sources: National Bank of Belgium, Bulletin; and International Monetary Fund, International Financial Statistics.

1/ Figures may not add up due to rounding.
2/ Preliminary data for 1983 are on a cash basis.
3/ Including subcontracting (travail à façon).

Table 37. Belgium: Sectoral Financial Balances and the Current Account

(In billions of Belgian francs and in percent) 1/

	1975	1976	1977	1978	1979	1980	1981	1982
Households	174	209	175	172	185	218	366	359
In percent of:								
Gross disposable income 2/	9.9	10.3	8.0	7.4	7.4	8.0	12.4	11.4
Gross domestic product	7.5	8.0	6.2	5.6	5.7	6.2	10.0	9.1
Enterprises	-35	-18	1	32	13	34	58	104
In percent of:								
Gross disposable income 2/	-21.5	-10.0	0.5	14.3	5.4	14.3	24.4	37.5
Gross domestic product	-1.5	-0.7	--	1.0	0.4	1.0	1.6	2.6
Public sector	-149	-193	-218	-253	-291	-413	-588	-614
In percent of:								
Gross disposable income 2/	-39.5	-47.1	-48.4	-52.3	-57.7	-84.4	-149.2	-137.5
Gross domestic product	-6.4	-7.3	-7.7	-8.3	-8.9	-11.8	-16.1	-15.6
Economy (=current account)	-9	-3	-42	-49	-93	-161	-164	-151
In percent of:								
Gross domestic product	-0.4	-0.1	-1.5	-1.6	-2.8	-4.6	-4.5	-3.9

Sources: Data supplied by the National Bank of Belgium; and National Bank of Belgium, Annual Report, 1982.

1/ Data may not add due to rounding.
2/ This measure reflects the "financial" savings/dissavings ratio.

Table 38. BLEU: Merchandise Trade

(Changes in percent from same period of preceding year)

	1978	1979	1980	1981	1982	1982				1983	
						Q1	Q2	Q3	Q4	Q1	Q2
Total trade											
Volumes											
Exports	3.8	5.2	2.3	0.3	1.6	3.5	0.6	1.8	0.5	5.6	3.3
Imports	3.8	6.2	1.4	-4.4	1.1	2.5	7.6	-3.7	-2.1	-0.1	-8.9
Unit values											
Exports	0.7	12.0	11.3	9.1	14.2	12.8	17.1	13.1	14.7	10.5	4.7
Imports	1.2	10.4	15.6	14.4	14.3	13.0	13.1	12.6	16.9	8.5	7.5
Values											
Exports	4.9	17.8	13.8	9.1	16.1	16.7	17.8	15.2	15.3	16.6	8.2
Imports	5.4	16.9	17.7	9.9	14.4	15.9	21.8	8.4	14.3	8.3	-2.1
Import cover ratio	--	-1.0	0.9	5.0	0.4	0.9	-6.5	5.7	2.7	5.7	13.4
Terms of trade	-0.6	1.4	-3.7	-4.7	-0.1	-0.2	3.5	0.5	-1.9	1.8	-2.6
Trade balance 1/	-115.7	-123.2	-210.4	-247.5	-247.8	-106.7	83.2	-43.1	-16.7	-69.6	19.0
Non-oil trade											
Volumes											
Exports	4.7	4.3	1.9	1.4	1.5	3.3	--	1.9	1.1	6.2	4.0
Imports	5.3	6.4	1.9	-3.8	1.7	4.4	4.9	-2.0	-0.7	-0.2	-6.3
Unit values											
Exports	1.2	10.2	10.0	7.0	14.4	12.7	17.8	12.9	14.2	10.9	4.6
Imports	2.1	7.8	11.6	10.6	13.2	12.1	12.7	12.5	15.6	8.5	9.5
Values											
Exports	6.0	14.9	12.1	8.5	16.1	16.4	17.7	15.0	15.4	17.8	8.8
Imports	7.4	14.7	13.8	6.3	15.1	17.0	18.2	10.3	14.8	8.7	2.6
Import cover ratio	-0.5	-2.0	-0.1	5.4	-0.2	-1.0	-4.7	4.0	1.8	6.0	11.0
Terms of trade	-0.8	2.2	-1.4	-3.3	1.0	0.5	4.6	0.3	-1.3	2.1	4.5
Trade balance 1/	-40.2	-43.5	-76.0	-42.8	-30.2	-54.6	-23.8	10.0	38.2	-13.5	10.1

Sources: Interntional Monetary Fund, International Financial Statistics; and staff calculations.

1/ In billions of Belgian francs. Sums of quarterly data may not add up to annual figures due to delay in revisions.

Table 39. BLEU: Export Performance and Export Pricing

(Changes in percent)

	1978	1979	1980	1981	1982	1983 1/ 1st half
Volume performance						
Total trade						
(1) Market growth	6.4	8.0	1.3	-1.4	0.5	1.6
(2) Export growth	3.8	5.2	2.3	0.3	1.7	4.4
(3) Export performance = (2)-(1)	-2.6	-2.8	1.0	1.7	1.2	2.8
Non-oil trade						
(1) Market growth	7.5	8.6	3.1	0.5	1.4	2.7
(2) Export growth	4.7	4.3	2.4	0.5	2.0	4.1
(3) Export performance = (2)-(1)	-2.8	-4.3	-0.7	--	0.6	1.4
Pricing behavior						
Total trade						
(1) Partner countries' export prices in dollars	11.8	18.0	17.4	-4.2	-4.1	0.3
(2) Export prices of domestic producers in BF	0.7	12.0	11.3	9.1	14.3	2.8
(3) BF/dollar rate	13.9	7.3	0.4	-21.0	-18.7	-0.7
(4) Export prices of domestic producers in dollars	14.7	19.8	11.8	-13.8	-7.1	2.1
(5) Relative price of exports = (4)-(1)	2.9	1.8	-5.6	-9.6	-3.0	2.4
Non-oil trade						
(1) Partner countries' export prices in dollars	13.3	15.0	11.8	-7.0	-4.0	0.3
(2) Export prices of domestic producers in BF	1.2	10.7	9.1	8.0	13.7	2.5
(3) BF/dollar rate	13.9	7.3	0.4	-21.0	-18.7	2.4
(4) Export prices of domestic producers in dollars	15.3	18.8	9.5	-14.5	-7.6	0.1
(5) Relative price of exports = (4)-(1)	2.0	3.8	-2.3	-7.5	-3.5	0.2
Memorandum item:						
Relative export unit values in common currency: manufacturing	0.3	0.7	0.5	-5.0	-5.1	0.3

Sources: International Monetary Fund, International Financial Statistics; and staff calculations.

1/ Compared with second half of 1982; partner countries' data partly estimated.

Table 40. BLEU: Structure of Foreign Trade

(Volume indices, ratios and percentage changes over previous year)

	1975	1976	1977	1978	1979	1980	1981	1982	1983 1st Qtr.
Exports									
Primary products	118	138	146	155	161	156	156	157	170
	(-13.9)	(16.9)	(5.8)	(6.2)	(3.9)	(-3.1)	(--)	(0.6)	(-20.6)
Consumer durables	142	173	177	184	187	184	189	200	222
	(2.9)	(21.8)	(2.3)	(4.0)	(1.6)	(-1.6)	(2.7)	(5.8)	(6.7)
Consumer nondurables	148	159	168	173	191	202	212	217	228
	(-5.7)	(7.4)	(5.7)	(3.0)	(10.4)	(5.8)	(5.0)	(2.4)	(6.5)
Investment goods	166	184	185	185	199	209	207	206	208
	(1.8)	(10.8)	(0.5)	(--)	(7.6)	(5.0)	(-1.0)	(-0.5)	(-1.0)
Imports									
Primary products	125	149	155	163	170	170	168	175	188
	(-8.1)	(19.2)	(4.0)	(5.2)	(4.3)	(--)	(-1.2)	(4.2)	(7.2)
Consumer durables	161	188	198	205	223	233	215	206	223
	(-1.2)	(16.8)	(5.3)	(3.5)	(8.8)	(4.5)	(-7.7)	(-4.2)	(1.4)
Consumer nondurables	164	189	198	212	226	232	230	235	236
	(0.6)	(15.2)	(4.8)	(7.1)	(6.6)	(2.7)	(-0.9)	(2.2)	(-5.2)
Investment goods	149	156	165	166	179	186	171	176	171
	(-0.7)	(4.7)	(5.8)	(0.6)	(7.8)	(3.9)	(-8.1)	(2.9)	(-3.4)
Export/import ratios									
Primary products	94.4	92.6	94.2	95.1	94.7	91.7	92.8	89.7	90.4
Consumer durables	88.2	92.0	89.4	89.8	83.9	79.0	87.9	97.6	99.6
Consumer nondurables	90.2	84.1	84.8	81.6	84.5	87.1	92.2	92.7	96.6
Investment goods	111.4	117.9	112.1	111.4	111.2	112.4	121.1	117.0	121.6

Sources: National Institute of Statistics, _Statistique du Commerce_; and _Communiqué Hebdomadaire_.

Table 41. BLEU: Direction of Foreign Trade

(As a percentage of total trade; and in millions of dollars)

	1975	1976	1977	1978	1979	1980	1981	1982	1983 1st Qtr.
Industrial countries									
Exports	83.0	85.3	83.5	83.3	85.2	84.1	82.5	83.3	83.2
Imports	82.7	82.2	81.5	83.1	82.8	80.5	79.5	79.6	81.4
Balance 1/	-1.44	-1.06	-1.53	-2.86	-2.13	-3.41	-3.50	-2.40	-0.11
EMS countries									
Exports	64.1	67.7	64.4	64.3	64.9	62.9	60.8	60.4	59.6
Imports	60.9	60.7	59.7	60.5	59.7	54.9	53.7	55.9	54.1
Balance 1/	-0.23	0.70	0.98	-0.43	0.48	1.19	0.52	-0.66	0.50
Germany									
Exports	22.3	23.3	22.5	22.9	22.8	21.3	20.1	20.4	20.6
Imports	22.1	22.6	22.2	23.1	22.1	19.7	18.9	20.0	20.8
Balance 1/	-0.35	0.35	-0.54	-0.91	-0.53	-0.37	-0.55	-0.88	-0.11
Non-oil developing countries									
Exports	9.3	7.8	8.8	9.3	8.5	8.7	9.4	9.6	9.4
Imports	7.5	8.6	8.2	8.1	8.1	8.0	8.1	8.6	8.3
Balance 1/	0.37	-0.50	--	0.27	-0.08	-0.08	0.02	0.03	0.11
USSR, Eastern Europe,etc.									
Exports	2.8	2.1	1.9	1.6	1.6	1.7	1.7	1.5	1.9
Imports	1.9	1.5	1.7	1.6	1.6	2.2	2.2	3.1	3.6
Balance 1/	0.24	0.15	0.03	-0.06	-0.11	-0.51	-0.42	-1.00	-0.25
Oil-producing countries									
Exports	4.0	3.9	4.9	4.8	4.0	4.7	5.3	4.4	4.4
Imports	7.8	7.5	8.4	7.0	7.3	9.1	10.0	8.4	6.4
Balance 1/	-1.23	-1.35	-1.54	-1.20	-2.17	-3.57	-3.23	-2.55	-0.31
Total trade balance	-1.84	-2.54	-2.75	-3.54	-4.21	-7.21	-6.45	-5.47	-0.45

Sources: International Monetary Fund, Direction of Trade.

1/ In millions of U.S. dollars.

Table 42. BLEU: Services Balance

(In billions of Belgian francs)

	1978	1979	1980	1981	1982	1982 Q1	1982 Q2	1982 Q3	1982 Q4	1983 Q1	1983 Q2
Receipts											
Transportation and insurance	102.1	118.0	152.8	181.5	201.4	44.2	52.5	54.3	50.4	47.3	51.9
Travel	40.8	47.9	52.9	60.6	72.1	12.7	18.7	24.5	10.2	15.9	23.0
Revenues on investment	216.0	320.6	521.6	881.3	1,021.6	247.7	263.6	263.2	247.2	233.3	212.2
Public sector transactions	37.9	39.7	45.1	50.9	59.0	14.5	14.4	14.5	15.6	15.2	14.9
Other	131.9	143.0	166.3	192.4	207.7	47.8	51.3	55.0	53.6	55.1	55.6
Total	528.7	669.2	938.7	1,366.8	1,561.8	366.9	400.4	411.5	383.0	366.8	357.6
Outlays											
Transportation and insurance	93.7	107.4	136.8	166.7	174.9	40.3	44.3	43.5	46.8	43.6	43.1
Travel	75.0	87.0	95.6	107.5	100.1	19.7	25.4	36.1	18.9	21.9	26.3
Revenue on investment	196.4	310.2	523.7	884.3	1,031.2	253.7	267.5	268.4	241.6	244.6	216.0
Public sector transactions	10.7	12.8	13.0	14.0	15.9	4.9	4.6	3.2	3.2	4.6	3.6
Other	120.9	130.1	166.9	191.9	212.7	46.7	50.2	54.4	61.4	56.5	55.5
Total	496.7	656.6	936.1	1,364.4	1,534.8	365.3	392.0	405.6	371.9	371.2	344.5
Services balance	32.1	12.6	2.6	2.3	27.0	1.6	8.4	5.9	11.1	-4.4	13.1

Source: National Bank of Belgium, Bulletin.

Table 43. BLEU: Capital Account Summary, 1979-83 1/

(In billions of Belgian francs)

	1979	1980	1981	
Public sector 2/	72.3	153.9	258.2	2
Direct foreign borrowing	36.3	89.1	138.5	1
Foreign borrowing from BLEU banks	36.0	64.8	119.7	1
Private sector	-10.8	0.8	-201.0	-1
Transactions with abroad	-63.6	-50.6	-62.6	-1
Residents' foreign exchange deposits with BLEU banks	11.3	-13.0	-86.5	-
Non-residents' BF deposits with BLEU banks	41.5	64.4	-51.9	1
Total capital account	61.5	154.7	57.2	9

Sources: National Bank of Belgium, Bulletin; and data provided by the Be authorities.

1/ For greater detail see Table 44.
2/ Including state enterprises and public financial intermediaries.
3/ Excluding trade credits.

Table 44. BLEU: Capital Account, 1979-83

(In billions of Belgian francs)

	1979	1980	1981	1982	1982 Q1	1982 Q2	1982 Q3	1982 Q4	1983 Q1	1983 Q2
Private sector	25.2	65.6	-81.3	-38.9	35.1	-26.6	23.0	-70.4	...	...
Nonbanking sector 1/	-49.4	-13.5	6.3	-22.7	-16.7	20.8	-26.4	-0.4	4.5	
BLEU capital	-86.0	-86.1	-102.2	-93.8	-29.4	-2.3	-45.4	-16.7	-32.5	-23.8
Portfolio investment	-13.7	-23.4	-41.1	-56.3	-13.0	-14.9	-17.8	-10.6	-24.2	-20.1
Direct investment	-32.8	-1.8	-1.1	3.5	-0.4	12.5	-5.8	-2.8	1.8	-6.1
Other 2/	-39.5	-60.9	-60.0	-41.0	-16.0	0.1	-21.8	-3.3	-10.1	2.4
Foreign capital	36.6	72.6	108.5	71.1	12.7	23.1	19.0	16.3	34.3	-8.2
Net commercial credits	-25.0	-20.7	-61.0	7.7	27.0	-26.3	17.4	-10.4	...	...
Banking sector 3/	99.6	99.8	-26.6	-23.9	24.8	-21.1	32.0	-59.6	2.3	78.5
In domestic currency	41.5	64.4	-51.9	16.4	1.2	5.6	33.7	-24.1	-34.0	23.2
In foreign exchange	58.1	35.4	25.3	-40.3	23.6	-26.7	-1.7	-35.5	36.3	55.3
Net foreign exchange	10.8	-16.4	-7.9	-110.7	6.4	-47.8	-14.0	-55.3	35.2	18.2
Net position on private sector	11.3	-13.0	-86.5	-52.7	-20.0	-23.0	-1.5	-8.2	-41.9	29.6
Net position on public sector	36.0	64.8	119.7	123.1	37.2	44.1	13.8	28.0	43.0	7.5
Public sector	36.3	89.1	138.5	133.0	42.5	43.9	30.2	16.4	44.4	4.6
General Government	4.3	25.7	107.1	117.3	42.7	40.4	32.0	2.2	45.9	3.2
Other public sector 4/	32.0	63.4	31.4	15.7	-0.2	3.5	-1.8	14.2	-1.5	1.4
Total capital account	61.5	154.7	57.2	94.1	77.6	17.3	53.2	-54.0	...	...

Source: National Bank of Belgium, *Bulletin*.

1/ Excluding commercial credits.
2/ Mainly deposits abroad in domestic or foreign currencies.
3/ Spot operations only.
4/ Broad concept of public sector. Includes state enterprises (*organismes publics d'exploitation*) and public financial intermediaries.

Table 45. BLEU: Capital Transactions of the Public Sector, 1979-83

(*In billions of Belgian francs*)

	1979	1980	1981	1982	1982 Q1	1982 Q2	1982 Q3	1982 Q4	1983 Q1	1983 Q2
General Government 1/	40.3	90.5	207.0	233.5	78.7	81.6	41.4	31.8	88.9	10.7
Direct foreign borrowing	(4.3)	(25.7)	(107.1)	(117.3)	(42.7)	(40.4)	(32.0)	(2.2)	(45.9)	(3.2)
Foreign borrowing from BLEU banks	(36.0)	(64.8)	(99.9)	(116.2)	(36.0)	(41.2)	(9.4)	(29.6)	(43.0)	(7.5)
Other public sector 2/	32.0	63.4	51.2	22.6	1.0	6.4	2.6	12.6	-1.5	1.4
Direct foreign borrowing	(32.0)	(63.4)	(31.4)	(15.7)	(-0.2)	(3.5)	(-1.8)	(14.2)	(-1.5)	(1.4)
Foreign borrowing from BLEU banks	(--)	(--)	(19.8)	(6.9)	(1.2)	(2.9)	(4.4)	(-1.6)	(--)	(--)
Total public sector	72.3	153.9	258.2	256.1	79.7	88.0	44.0	44.4	87.4	12.1

Sources: National Bank of Belgium, *Bulletin*; and data provided by Belgian authorities.

1/ Including the Fonds des Rentes.
2/ Broad concept of public sector. Includes state enterprises (*organismes publics d'exploitation*) and public financial intermediaries.

Table 46. BLEU: Private Sector Capital Transactions, 1979-83

(In billions of Belgian francs)

	1979	1980	1981	1982	1982 Q1	1982 Q2	1982 Q3	1982 Q4	1983 Q1	1983 Q2
Trade credits	-25.0	-20.7	-61.0	7.7	27.0	-26.3	17.4	-10.4	...	...
Other non-bank residents										
Foreign exchange deposits with resident banks	11.3	-13.0	-86.5	-52.7	-20.0	-23.0	-1.5	-8.2	-41.9	29.6
Other	-86.0	-86.1	-102.2	-93.8	-29.4	-2.3	-45.4	-16.7	-32.5	-23.8
Other non-residents										
BF deposits with resident banks	41.5	64.4	-51.9	16.4	1.2	5.6	33.7	-24.1	-34.0	23.2
Other	36.6	72.6	108.5	71.1	12.7	23.1	19.0	16.3	34.3	-8.2
Commercial banks	10.8	-16.4	-7.9	-110.7	6.4	-47.8	-14.0	-55.3	35.2	18.2
Total	-10.8	0.8	-201.0	-162.0	-2.1	-70.7	9.2	-98.4	...	...

Sources: National Bank of Belgium, Bulletin; and data provided by the Belgian authorities.

Table 47. Net Foreign Assets of the National Bank of Belgium, 1979-82

(Changes in billions of Belgian francs)

	1979	1980	1981	1982	1982 Q1	1982 Q2	1982 Q3	1982 Q4	1983 Q1	1983 Q2
Gold	--	--	--	--	--	--	--	--	--	--
IMF position, net 1/	-4	-4	-2	-1	--	1	-1	-1	-2	-1
Net claims on or liabilities to the European Monetary Cooperation Fund: 2/										
ECUs	-25	-27	-79	48	19	-3	27	6	19	16
Other	-1	28	-3	-14	3	--	--	-17	-65	82
Foreign currencies	-1	30	-10	-74	-34	-15	32	-56	6	-6
Belgian francs 3/	--	--	-2	3	2	-3	2	2	--	-3
Total	-31	27	-96	-38	-11	-20	60	-67	-41	99

Sources: National Bank of Belgium, Annual Report, 1982; and data provided by the Belgian authorities.

1/ IMF position (quota, holdings of SDRs and advances) net of net cumulative allocation of SDRs.
2/ The plus sign indicates an increase in net claims or a decrease in net liabilities; the minus sign indicates a decrease in net claims or an increase in net liabilities.
3/ Difference between claims on foreign countries (other than commercial claims) and liabilities to foreign countries, particularly to the central banks and the European institutions.

Table 48. BLEU: International Reserves, 1978-83

(In millions of SDRs; end of period)

	1978	1979	1980	1981	1982 Q1	1982 Q2	1982 Q3	1982 Q4	1983 Q1	1983 Q2
Gold 1/	1,491	1,197	1,196	1,196	1,196	1,196	1,196	1,196	1,196	1,196
SDRs	422	488	508	643	649	690	690	687	653	625
IMF reserve position	616	533	501	402	388	369	352	340	331	324
Foreign exchange	2,024	3,110	5,147	3,236	2,571	2,071	3,144	2,560	3,517	4,085
Total	4,553	5,328	7,352	5,477	4,804	4,326	5,382	4,783	5,697	6,230

Sources: IMF, International Financial Statistics; and National Bank of Belgium, Bulletin.

1/ Valued at SDR 35 per ounce.

Table 49. BLEU: Gross Reserves 1/ as Percentage of
Total Imports of Goods and Services

	1979	1980	1981	1982	1983 2/
Percentage ratio 3/	6.6	8.9	5.6	4.8	3.5
Number of weeks of import cover	3.4	4.6	2.9	2.5	3.4

Sources: International Monetary Fund, International Financial Statistics: National Bank of Belgium, Bulletin; and staff estimates and projections.

1/ Excluding gold holdings.
2/ Estimates.
3/ Ratio of year-end reserves to imports of goods and services during the year indicated (except for 1983: ratio of end-June reserves to imports of goods and services projected for year as a whole).

Belgium - Sectoral Financial Balances and the Current Account

1. Introduction

Table 38 in the main text summarizes the developments of aggregated financial balances of the three domestic sectors of the economy (households, enterprises and the public sector). Their sum is the counterpart to the current account surplus or deficit. At this level of aggregation, the steady deterioration of the current account position of Belgium for most of the period under review is seen to be almost entirely attributable to the sharp increase in the net financing requirement of the public sector. 1/ As a percentage of GDP the net financing requirement increased from 6.4 percent of GDP in 1975 to 16.1 percent in 1981; after which it dropped to 15.6 percent in 1982. Between 1976 and 1979 households also contributed to the deterioration in the current account, as their financing capacity dropped from 8.0 percent of GDP in 1976 to 5.7 percent in 1979. After 1979, households' financing capacity rose again, most spectacularly so in 1981 owing to a precipitous decline in housing investment. In 1982, households financing capacity dropped again, reflecting to a large extent the decline in real disposable income. Enterprises' financial position strengthened fairly steadily from a deficit of 1.5 percent of GDP in 1975 to a surplus of 2.6 percent in 1982. Enterprises' transactions have thus increasingly reduced the current account deficit. This fact, as well as the fact that the enterprise sector has been a net lender since 1977 are rather unusual features by international standards.

2. Households' financial balance

The share of households' disposable income in GDP has increased between 1975 and 1981 primarily on account of a steady rise in the share of wages and salaries--which are a cost to enterprises and thus weaken their financial balance--and in current transfer payments--which are an expenditure of the public sector and thus burden its financial balance (Appendix Table 50). 2/ Households' gross disposable income, i.e., disposable income including depreciation, has fluctuated considerably as a percentage of GDP, but has, nevertheless, followed an upward trend, reaching 79.7 percent in 1982, compared with 76.3 percent in 1975. Because the trend growth of consumption was even higher, gross savings and capital resources of households have had a tendency to decline. 3/

1/ An examination of factors underlying the deterioration of the public finances thus assumes a prominent role in the analysis of current account developments. Such an examination is attempted here, although on a rather general and aggregate level.

2/ However, on a net basis, i.e., taking the sum of households' transfers from Government minus their direct taxes and social security contributions, households transfer receipts have fluctuated fairly narrowly around minus 7 percent of GDP, without a visible trend.

3/ The trend decline in households' gross savings and capital resources was interrupted in 1981 when households' real disposable income kept rising while real GDP declined by more than 1 percent. The related strengthening of the contingency motive for saving raised the share of savings

The fact that the net financing capacity of households has nevertheless on average increased considerably in 1981-82 owes much to the sharp decline in households' gross capital formation, notably residential construction.

3. Corporate enterprises' financial balance

Between 1975 and 1981, the gross operating surplus before subsidies of enterprises (in percent of GDP) has displayed a strong trend decline (Appendix Table 51). Increased subsidies--which burdened the public finances--have only partly offset this fall. The prime reason for the decline in the operating surplus has been the growth of wages and salaries which increasingly exceeded enterprises' scope for price increases. This applied in particular to the exposed sector. As a share of value added (at market prices) of enterprises, wages and salaries increased from 60 percent in 1975 to 62.8 percent in 1981. In addition, the share of production taxes and other components increased from 22.9 percent in 1975 to 24.4 percent in 1981. Thus, the share of the gross operating surplus (before subsidies) in value added fell from 17 percent to 12.7 percent over the same period. In 1982, both measures of enterprises' operating surplus increased by about 1 percentage point of GDP on account of a sharp increase in sales prices--reflecting to a large extent the effects of the February devaluation of the Belgian franc--and a strong deceleration of wage costs--reflecting the partial suspension of indexation. Despite the trend deterioration of enterprises' primary incomes out of production, their disposable income (= gross savings) has not displayed a trend decline. The prime reason for this development was the strong decline of net property income paid by enterprises which was to a large extent a reflection of the past development of enterprises' financial balance: because the initial net financing deficit has turned into an increasing financing surplus, enterprises continued to increase their stock of financial assets, and interest earnings on these assets tended to increasingly offset enterprises' debt service payments. Thus, on aggregate, enterprises have at least partly compensated the decline (in terms of GDP) of earnings from production by increasing earnings from net financial asset holdings. 1/ A further factor for the improvement in enterprises' financial balance has been the fall in the propensity to invest which accompanied the decline in profitability of production at a time when the real return on financial investments increased. 2/

3/ (cont'd from p. 100) in GDP temporarily. However, in 1982, the share of savings dropped again on account of households' attempt to maintain an accustomed level of real consumption in the face of the sharp decline in real disposable income which followed the partial suspension of wage indexation.

1/ It has to be remembered in this context that the data are aggregate data for the entire corporate enterprise sector, i.e., including the National Bank of Belgium and private sector financial intermediaries. The decline in net interest paid therefore reflects in part the growing importance of the financial sector in Belgium (compare Table 4 in main text).

2/ Compare Table 11 in main text.

However, the most important factor for the favorable development of enterprises' net financing capacity has been the growth of net capital transfers received from the Government 1/ which increased from 1.6 percent of GDP in 1975 to 3.8 percent in 1982. It appears that these transfers--contrary to their intention--have not succeeded in generating a concomitant increase in investment, at least not if judging by the aggregated data in Appendix Table 51. On balance these aggregated data suggest that capital transfers appear to have primarily improved the financial position of enterprises rather than to have generated investment in real assets.

4. Public sector financial balance

The development of the public sector's financing requirement (Appendix Table 52) has been dominated--although in the opposite direction--by movements of the same components of the financial balance, notably current and capital transfers, which have upheld or improved the financing capacity of households and enterprises. Existing social legislation combined with adverse demographic trends and an acceleration in unemployment have resulted in a dynamic growth of transfers to households. At the same time, the attempt to maintain workplaces and/or to soften the burden of structural adjustment in industries which continued to lose international competitiveness have led to a strong increase in transfers to enterprises. In the event, the dynamics of government current and capital transfers to these two sectors, combined with a continuous growth of public consumption exceeded the revenue generating capacity of the economy despite a number of increases in tax and social security rates. The related increases in the net financing requirement of the public sector fed onto themselves through the steep growth of interest payments on public debt from 3.5 percent of GDP in 1975 to 9.2 percent in 1982. 2/ A large part of these interest payments has benefited the two domestic private sectors and has thereby--in addition to transfer payments received from the public sector--upheld their consumption and capital spending.

5. Summary

In the case of Belgium, it appears that the trend deterioration in the current account 3/ originated in the strong and steady increase--at the time of a sharp deterioration of the terms of trade--in the purchasing power of the household sector (here measured by gross disposable income) and the related growth of this sector's absorption of resources. The increase in households' incomes involved a deterioration in the financial position of both enterprises (through increases in wages and

1/ These capital transfers include among others, and most importantly, increased participations of the Government in ailing enterprises.

2/ Since early 1980, the growth of interest payments has also been influenced by the sharp increase in interest rates.

3/ As measured by the net financing requirement of the economy as a whole.

salaries, and given the limited scope for price increases in the exposed sector) and the public sector (through current transfers). The related deterioration in the earnings position of enterprises was largely offset by current and capital transfers of the public sector in an attempt to restore the financial health of enterprises and their capacity to invest. However, this policy added to the deterioration of the public finances without generating a corresponding containment of public sector claims on the domestic product. In the event, total absorption increasingly exceeded domestic output and the current account deteriorated continuously through 1980.

The improvement after 1980 had two different reasons. In 1981, it was almost entirely a reflection of a sharp decline in households' gross capital formation, notably housing, which was accompanied by a significant increase in households' "voluntary" saving on account of a strengthening of the contingency motive of saving and of the strong decline in housing investment. By contrast, in 1982, the improvement was the result of the massive redistribution of income which followed the implementation of the February 1982 policy package and which was contemplated by strong increases in direct taxes (including social security contributions). The sharp drop in households' real disposable income "enforced" precipitated a further strong fall in housing investment, while the strong growth in enterprises' operating surplus and capital resources did not immediately generate an offsetting claim on resources by the enterprise sector. Furthermore, for the first time since the early 1970s, public sector consumption fell as a share of GDP and the growth in transfer payments was kept under tight control. Thus, the financing requirement of the public sector dropped and the net financing requirement of the economy as a whole improved considerably in 1982.

Table 50. Belgium: Derivation of Households' Net Financing Capacity/Requirement

(In billions of Belgian francs and in per cent of GDP)

	1975	1976	1977	1978	1979	1980	1981	1982
1. Wages and salaries	1,323 (57.2)	1,526 (58.1)	1,658 (58.5)	1,785 (58.5)	1,907 (58.5)	2,075 (59.3)	2,176 (59.7)	2,307 (58.6)
2. Other earned income	548 (23.7)	618 (23.5)	655 (23.1)	705 (23.1)	751 (23.0)	809 (23.1)	887 (24.4)	992 (25.2)
3. Current transfers	431 (18.6)	501 (19.1)	562 (19.8)	616 (20.2)	671 (20.6)	724 (20.7)	810 (22.2)	886 (22.5)
4. Personal income =(1)+(2)+(3)	2,302 (99.5)	2,645 (100.7)	2,876 (101.4)	3,106 (101.8)	3,328 (102.2)	3,609 (103.1)	3,874 (106.3)	4,186 (106.2)
5. Direct taxes, incl. soc.sec.	595 (25.7)	672 (25.6)	767 (27.0)	849 (27.8)	922 (28.3)	979 (28.0)	1,032 (28.3)	1,156 (29.3)
6. Net disposable income =(4)-(5)	1,707 (73.8)	1,973 (75.1)	2,108 (74.3)	2,256 (74.0)	2,407 (73.9)	2,629 (75.1)	2,841 (78.0)	3,030 (76.9)
7. Depreciation 1/	59 (2.6)	65 (2.5)	73 (2.6)	79 (2.6)	85 (2.6)	91 (2.6)	100 (2.7)	110 (2.8)
8. Gross disposable income =(6)+(7)	1,766 (76.3)	2,038 (77.6)	2,182 (76.9)	2,336 (76.5)	2,492 (76.5)	2,720 (77.7)	2,941 (80.7)	3,140 (79.7)
9. Consumption	1,421 (61.4)	1,610 (61.3)	1,764 (62.2)	1,888 (61.9)	2,049 (62.9)	2,233 (63.8)	2,394 (65.7)	2,600 (66.0)
10. Gross savings =(8)-(9)	344 (14.9)	429 (16.3)	418 (14.7)	448 (14.7)	442 (13.6)	488 (13.9)	547 (15.0)	541 (13.7)
11. Net capital transfers	8 (0.3)	9 (0.3)	8 (0.3)	7 (0.2)	8 (0.2)	8 (0.2)	6 (0.2)	3 (0.1)
12. Capital resources =(10)+(11)	352 (15.2)	438 (16.7)	426 (15.0)	455 (14.9)	450 (13.8)	496 (14.2)	553 (15.2)	544 (13.8)
13. Gross capital formation	178 (7.7)	229 (8.7)	251 (8.8)	283 (9.3)	265 (8.1)	278 (7.9)	187 (5.1)	185 (4.7)
14. Net financing capacity (+) or requirement (-); = (12)-(13)	174 (7.5)	209 (8.0)	175 (6.2)	172 (5.6)	185 (5.7)	218 (6.2)	366 (10.0)	359 (9.1)

Sources: Data supplied by the National Bank of Belgium and Annual Report 1982; International Monetary Fund, Data Fund.

1/ For some years derived as a residual.

Table 51. Belgium: Derivation of Corporate Enterprises' Net Financing Capacity/Requirement

(In billions of Belgian francs and in per cent of GDP)

	1975	1976	1977	1978	1979	1980	1981	1982
1. Value added	1,678 (72.6)	1,929 (73.4)	2,077 (73.2)	2,221 (72.8)	2,364 (72.6)	2,539 (72.5)	2,615 (71.7)	2,827 (71.8)
2. Wages and salaries	1,008 (43.6)	1,170 (44.5)	1,269 (44.7)	1,359 (44.5)	1,442 (44.3)	1,588 (45.4)	1,643 (45.1)	1,757 (44.6)
3. Production taxes, etc. 1/	384 (16.6)	465 (17.7)	490 (17.3)	534 (17.5)	568 (17.4)	592 (16.4)	639 (17.5)	674 (17.1)
4. Gross operating surplus before subsidies = (1)-(2)-(3)	286 (12.4)	294 (11.2)	318 (11.2)	328 (10.7)	354 (10.9)	360 (10.3)	333 (9.1)	369 (10.1)
5. Subsidies	28 (1.2)	37 (1.4)	40 (1.4)	47 (1.5)	56 (1.7)	53 (1.5)	60 (1.6)	65 (1.6)
6. Gross operating surplus = (4)+(5)	314 (13.6)	331 (12.6)	358 (12.6)	375 (12.3)	410 (12.6)	412 (11.8)	393 (10.8)	461 (11.7)
7. Net property income paid	81 (3.5)	79 (3.0)	83 (2.9)	69 (2.3)	78 (2.4)	84 (2.4)	68 (1.9)	71 (1.8)
8. Current transfers (net) to government	70 (3.0)	73 (2.8)	76 (2.7)	82 (2.7)	92 (2.8)	90 (2.6)	87 (2.4)	113 (2.9)
9. Disposable income = gross savings = (6)-(7)-(8)	163 (7.0)	179 (6.8)	199 (7.0)	224 (7.3)	240 (7.4)	238 (6.8)	238 (6.5)	222 (7.0)
10. Net capital transfers received	36 (1.6)	46 (1.8)	55 (1.9)	64 (2.1)	63 (1.9)	103 (3.0)	128 (3.5)	149 (3.8)
11. Capital resources = (9)+(10)	199 (8.6)	225 (8.6)	254 (8.9)	288 (9.4)	303 (9.3)	341 (9.7)	366 (10.0)	426 (10.8)
12. Gross investment	234 (10.1)	243 (9.2)	253 (8.9)	256 (8.4)	290 (8.9)	307 (8.8)	308 (8.5)	322 (8.2)
13. Net financing capacity (+) or requirement (-); = (11)-(12)	-35 (-1.5)	-18 (-0.7)	1 (0.0)	32 (1.0)	13 (0.4)	34 (1.0)	58 (1.6)	104 (2.6)

Sources: National Bank of Belgium, Annual Report 1982; National Institute of Statistics, Statistical Bulletin.

1/ Includes, for example, earnings of small enterprises not included in the enterprise sector, and of self-employed.

Table 52. Belgium: Derivation of the Public Sector's Net Financing Capacity/Requirement

(In billions of Belgian francs and in per cent of GDP)

	1975	1976	1977	1978	1979	1980	1981	1982
1. Revenue	990 (42.8)	1,129 (43.0)	1,266 (44.6)	1,384 (45.4)	1,508 (46.3)	1,601 (45.7)	1,686 (46.3)	1,887 (47.9)
a. Direct taxes, including social security	678 (29.3)	759 (28.9)	859 (30.2)	948 (31.1)	1,033 (31.7)	1,091 (31.2)	1,143 (31.4)	1,294 (32.8)
b. Indirect taxes	270 (11.7)	325 (12.4)	356 (12.6)	386 (12.6)	414 (12.7)	435 (12.4)	457 (12.5)	496 (12.6)
c. Other revenues	42 (1.8)	45 (1.7)	51 (1.8)	50 (1.6)	61 (1.9)	75 (2.1)	86 (2.4)	96 (2.4)
2. Expenditure	1,139 (49.2)	1,322 (50.3)	1,484 (52.3)	1,637 (53.6)	1,799 (55.2)	2,014 (57.5)	2,274 (62.4)	2,500 (63.5)
a. Consumption	388 (16.8)	441 (16.8)	489 (17.2)	543 (17.8)	588 (18.0)	644 (18.4)	701 (19.2)	740 (8.8)
b. Interest on public debt	82 (3.5)	97 (3.7)	116 (4.1)	137 (4.5)	165 (5.1)	212 (6.1)	287 (7.9)	361 (9.2)
c. Transfers and other current expenditures	524 (22.7)	614 (23.4)	691 (24.4)	756 (24.8)	829 (25.4)	882 (25.2)	984 (27.0)	1,074 (27.3)
d. Capital expenditure	145 (6.3)	170 (6.5)	187 (6.6)	201 (6.6)	217 (6.7)	275 (7.9)	302 (8.3)	325 (8.2)
Of which: Gross fixed investment	88 (3.8)	102 (3.9)	109 (3.8)	112 (3.7)	124 (3.8)	143 (4.1)	146 (4.0)	150 (3.8)
Capital transfers	57 (2.5)	68 (2.6)	78 (2.7)	89 (2.9)	93 (2.9)	132 (3.8)	156 (4.3)	175 (4.4)
3. Net financing capacity (+) or requirement (-); =(1)-(2)	-149 (-6.4)	-193 (-7.3)	-218 (-7.7)	-253 (-8.3)	-291 (-8.9)	-413 (-11.8)	-588 (-16.1)	-614 (-15.6)

Sources: Data supplied by the National Bank of Belgium; and Annual Report 1982.

Belgium: The Devaluation of February 1982: An Examination of Selected Short-Run Responses

1. Introduction

Effective February 22, 1982, the Belgian franc was devalued by 8 1/2 percent against all other EMS currencies. 1/ Before this devaluation, the Belgian franc had experienced substantial changes in its effective exchange rate and its bilateral rates vis-à-vis other currencies as a result of general floating (Table 34 and Chart 12). However, the devaluation of February 1982 was the first official change in the Belgian franc rate since the inception of the EMS in March 1979. In this sense, the devaluation was a special event which could not be expected to generate exactly the same effects on major economic variables as earlier changes in the exchange rate of the Belgian franc. Furthermore, the devaluation was accompanied by major changes in the wage and price policy. 2/

This note will present data on selected variables in each of the broad areas of influence of a change in the exchange rate 3/ (e.g., prices, costs, profitability, output, employment, and trade and current account balances) without making an effort to entering an econometric study. 4/

2. Exchange rate developments 1/

The immediate effect of the devaluation of the Belgian franc was an increase in the average Belgian franc/U.S. dollar rate by 8 percent from February 1982 to March 1982 (Chart 12). After March, the Belgian franc/U.S. dollar rate was again dominated by movements of the major EMS currencies vis-à-vis the dollar as had been the case before the devaluation. The ECU rate of the Belgian franc increased by 6.8 percent from end-January to end-February, i.e. by less than the devaluation because the Belgian franc temporarily moved away from the lower intervention limit in the EMS band (Chart 12). However, the position of relative strength of the Belgian franc was not maintained for long and by end-March the ECU rate was 8.7 percent higher than at end-January. In terms of the nominal effective exchange rate (MERM), the Belgian franc fell on average by 6.3 percent from February to March

1/ On the same day, the Danish kroner was devalued by 3 percent.
2/ For details see Chapter I.
3/ Most of the data will be discussed in the text only and will not be preented in a table.
4/ When analyzing the effects of the devaluation of February 1982, it has to be kept in mind, that the Belgian franc had aready lost considerably in value in the 16 months preceding the devalation and continued to fall afterwards.
5/ Only developments in the offical rate are being considered in this paragraph.

1982. After March, the MERM rate moved narrowly with a moderate tendency to fall. Later developments of the exchange rates of the Belgian franc have been described in Chapter IV.

3. Price developments

The most immediate effect of a devaluation is commonly exerted on import prices. The carryover of import price changes into the CPI and other general domestic price indices is primarily determined by the weight of imported goods in these indexes and the pricing policy of domestic producers of importcompeting products and of wholesalers and retailers. For the speed of adjustment the degree of homogeneity of products is important: the more homogeneous products are, the swifter is usually the adjustment. 1/ As a result, changes in relative prices between (a) different subsectors in the exposed sector, and (b) the exposed and the sheltered sector will occur. Price adjustments will also result from the cost-push effects of higher costs of imported inputs. Finally, apart from the above cost-pricing factors, demand factors will, at least in the short-run, affect pricing behavior. However, in the case of Belgium, the price controls mentioned earlier clearly played the dominant role for domestic price developments in 1982. This does not apply to export prices, which did not fall into the realm of price controls.

As expected, the data on price developments indicate that the great number of influences other than the devaluation obscure the effects of the devaluation on prices. For example, in the second quarter of 1982 the change in import prices (2.7 percent) fell short of the change in the MERM rate (5.5 percent) possibly reflecting a parallel decline in selected foreign prices of Belgian imports such as oil. As a result, the terms of trade improved unexpectedly in the second quarter of 1982. However, in the third quarter the increase in import price (3.7 percent) exceeded the fall in the exchange rate (0.6) and the terms of trade deteriorated by 2.6 percent. The feed-through of import prices into the consumer price index and the wholesale price index remained incomplete throughout 1982 and the ratio of domestic to import prices therefore continued to decline (Appendix Chart 14). Wholesale prices increased by less than the consumer price index, suggesting that price controls may have been more effective at the wholesale than at the retail level. Relative wholesale prices, relative value-added deflators, and relative export unit values (all for manufacturing and measured in common currency) declined sharply in the second quarter of 1982, reflecting the impact effects of the devaluation. However, the decline was smaller than the devaluation would have suggested because a swift upward adjustment in the respective domestic currency prices occurred. Nevertheless, the trend decline in the relative export unit values in common currency, which started in 1979 and accelerated thereafter in conjunction with the

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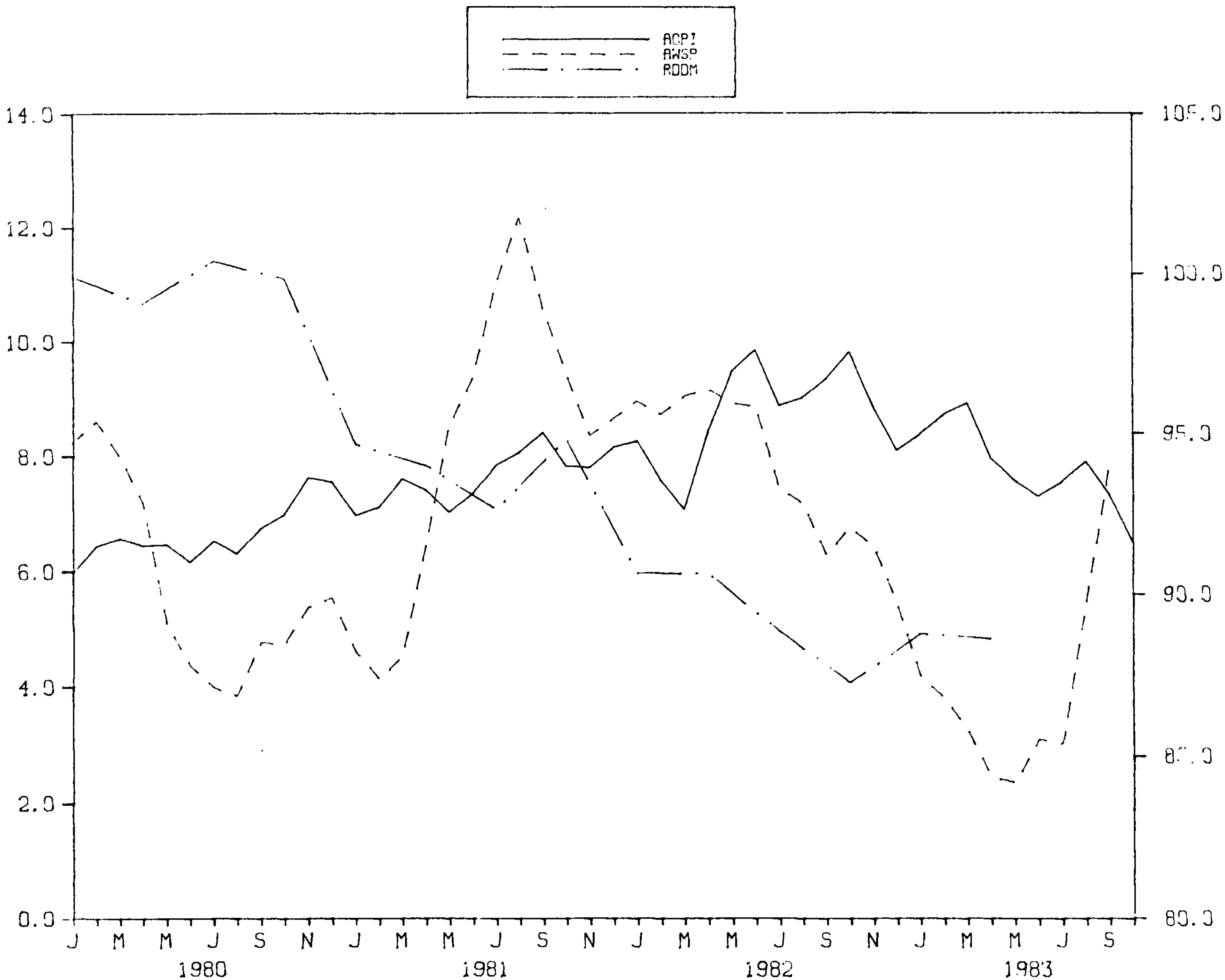
1/ For example, the adjustment of prices for semifinished products, which are commonly rather homogeneous, tends to be faster than the adjustment for the more heterogeneous finished products.

Chart 14

Belgium: Price Developments



ACPI = Growth rate of consumer price index (year-over-year; left scale)
AWSP = Growth rate of wholesale price index (year-over-year; left scale)
RDDM = Ratio of domestic prices to import prices (right scale)

effective depreciation of the Belgian franc continued in 1982 at a sharply reduced pace: between the second quarter of 1982 and the second quarter of 1983 there was virtually no change in relative export unit values. This suggests that the less-than-complete short-term pricetaking behavior of Belgian exporters of manufactured goods observed since early 1982 came to an end after the devaluation. Furthermore, gains in their international price competitiveness came to a halt. However, after substantial losses in competitiveness in the interim period, the level of price competitiveness, which had returned in 1981 to the level of the early 1970s remained high in 1982 and 1983.

4. Production costs and profitability

The first effect of the devaluation of a currency on domestic production costs stems commonly from the increase in prices of imported intermediate inputs. The second, often more significant effect, results from increases in domestic wages and domestically produced intermediate inputs triggered by the increase in import prices. In Belgium, the indexation of wages and salaries to the consumer prices index had in the past resulted in a swift upward adjustment of wages and salaries in line with increases in the CPI. Thus, the initially existing scope for an increase in profit margins in the exposed sector which had resulted from the effective depreciation of the Belgian franc since July 1980 was usually eliminated rapidly by the concomitant increase in labor costs. In fact, total domestic costs in the exposed sector, i.e., including costs of intermediate inputs from the domestic sheltered sector, appear to have risen by even more than was indicated by the depreciation of the Belgian franc and this has resulted in a disproportionate increase in costs and a compression in profits in the exposed sector. The policy package of February 1982 has brought about a sharp reversal of this development because it contained increases in labor costs while offering ample scope for price increases to exporters. 1/

The data on production costs and profitability indicate that the wage freeze has strongly reduced the growth of the wage component of production costs. Combined with continued labor shedding, the "effective" labor costs, 2/ as measured, for example, by the unit labor costs in manufacturing, were flat in the second quarter of 1982. The increase in production costs observed after the devaluation therefore reflects primarily increases in costs of intermediate inputs, not least due to the strong rise in wholesale prices of imported goods 3/ which may be a good indicator of the rise in prices of imported intermediate inputs. Still, the growth

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1/ However, domestic import-competing producers were initially restricted in their pricing policy because their prices were frozen initially and remained under control later.

2/ I.e., labor costs after productivity adjustments, including in particular those of adjustments in employment.

3/ These rose at an annual rate of almost 13 percent in the second quarter of 1982.

rate of production costs in manufacturing, whether measured by using hourly wages or unit labor costs, slowed considerably in 1982. The same holds for the index for the whole economy. These results are reflected in the various measures on profitability (Appendix Chart 15). 1/ All profitability indexes for the manufacturing sector rose in the second quarter of 1982, having in most cases declined in the preceding periods. In the third quarter they fell again somewhat but remained above the level of the preceding periods. The profitability indexes for the economy as a whole also increased in the second quarter of 1982 and remained flat thereafter, interrupting the long downward trend.

5. Production, employment and productivity

The production response to a devaluation is primarily influenced (a) by the overall demand effect, and (b) by the "supply-incentive effect" which results from the price-cum-cost effect on profitability. Domestic demand as measured by the volume of retail sales dropped sharply in the second quarter of 1982 (2.8 percent, year-on-year). However, as in 1981, the most significant drop in demand was recorded in construction. Because construction is essentially nontraded production, the fall in domestic demand was in the construction sector not offset by an increase in foreign demand and production dropped strongly despite lower labor costs. By contrast, in selected tradable goods industries, the increase in foreign demand partly compensated or even overcompensated the fall in domestic demand. Furthermore, given the scope for price increases in export, there was a strong incentive to meet the demand. Thus, production in these sectors firmed after the usual time lags despite a renewed slack in world trade and a pricing policy of domestic exporters which apparently placed more emphasis on the improvement in profit margins than on the gain of market shares. The production response was especially favorable in early 1983 when the production of tradables increased by an appreciable margin. However, the labor market remained on aggregate largely unaffected by the observed movements in the production indexes: employment continued its downward trend and unemployment increased at a high rate in the second half of 1982. However, in some sectors there was a noticeable slowing in labor shedding and in some others even an expansion of the workforce. The divergent movements in output and employment between sectors were reflected in corresponding adjustments in productivity.

6. Business expectations, orders, stocks, and investment

Available data on business expectations, orders, stocks, and investment did not immediately show a systematic positive influence of the

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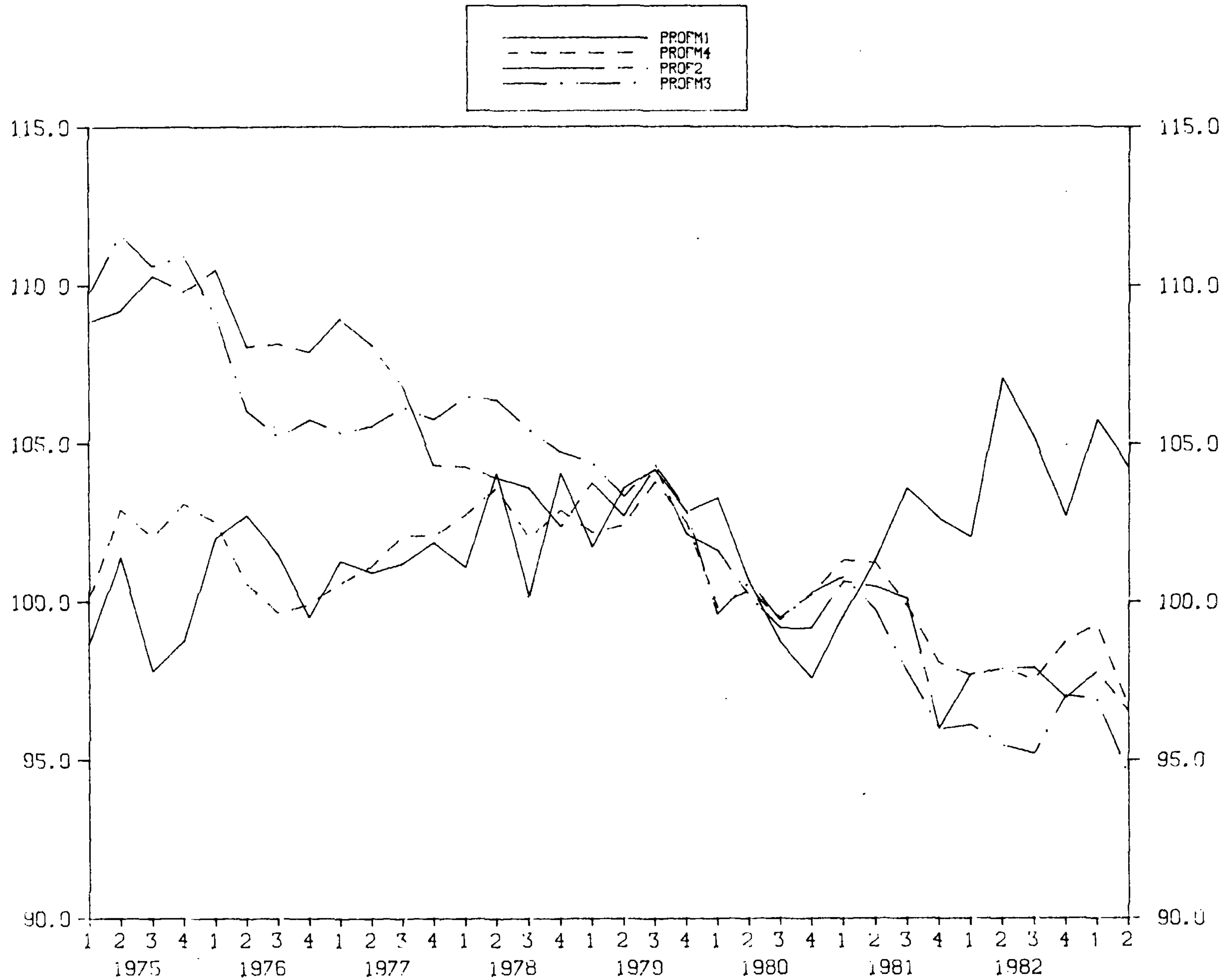
1/ PROFM1 in Appendix Chart 15 equals the ratio of the value added deflator to unit labor costs; PROFM4 equals the ratio of the value added deflator to the weighted ratio of unit labor costs and costs of intermediate inputs; PROFM3 equals the ratio of the value added deflator to hourly wages plus costs of intermediate goods; PROFM2 equals the ratio of wholesale prices to hourly earnings.

Chart 15

Belgium: Profitability Indexes



PROFM1, PROFM4 = "Effective" profitability indexes, manufacturing; 1980=100
PROFM3 = "Unadjusted" profitability index, manufacturing; 1980=100
PROF2 = "Unadjusted" profitability index, whole economy; 1980=100

devaluation. The composite index of business sentiment (CSYN) suggested a moderate improvement in expectations in the second quarter of 1982 which was followed by a sharp fall in the two last quarters of the year (Appendix Chart 16) as domestic demand dropped at a rapid pace. A moderate improvement followed in early 1983, but it remained without a clear trend. A parallel adjustment took place in the evaluation of orders. Furthermore, the level of stocks was steadily and increasingly judged too high in 1982. Investment spending responded most consistently to the improvement in profitability as it increased by 10, 17 and 15 percent respectively (year-on-year) in the three quarters following the devaluation. In real terms, investment remained weak although its decline was stopped.

7. Trade and current account developments

The developments in the trade balance (customs basis) and in the current account (transactions basis) have been described in Chapter IV of the report. Due to both strong and swift increases in export prices and a favorable development of import prices. They indicated the virtual absence of a "J-curve" effect following the devaluation. Thus, contrary to usual developments, the terms of trade did not drop significantly (Appendix Chart 17) and the volume effect dominated the improvement in the trade balance. The volume response (measured by changes in the import cover ratios) was very strong, but occurred--as expected--with a certain time lag (Appendix Chart 18). The export performance, measured by the growth of Belgian exporters relative to the growth of markets (both measured in volume terms) continued to improve for both total and non-oil exports. However, the speed of improvement slowed. 1/ At the same time, the degree of import penetration fell sharply in 1982 after the second quarter with some rebound in the first quarter of 1983 because of speculative imports at a time of particular slack in domestic demand (Appendix Chart 19).

8. Business failures

The number of business failures should be expected to decline if a devaluation achieves its main objectives, namely, to enhance (restore) the competitiveness of domestic producers and to increase profitability in the exposed sector. Both improvements have indeed taken place in 1982 (see Chapter I). On the other hand, a drastic change in income distribution and relative prices entails large shifts in demand which may speed up business failures in selected sectors. The data in Appendix Table 53 suggest that, although the absolute number of business failures still increased, the momentum of business failures has, on balance, slowed. Especially if compared with the performance in three selected competitor countries, the Belgian record of business failures has clearly improved in the past two years, after having strongly and almost continuously deteriorated between 1975 and 1980. For the first half of 1983, there was

1/ For the reasons see Chapter IV and Table 39.

Table 53. Belgium: Bankruptcies in International Comparison

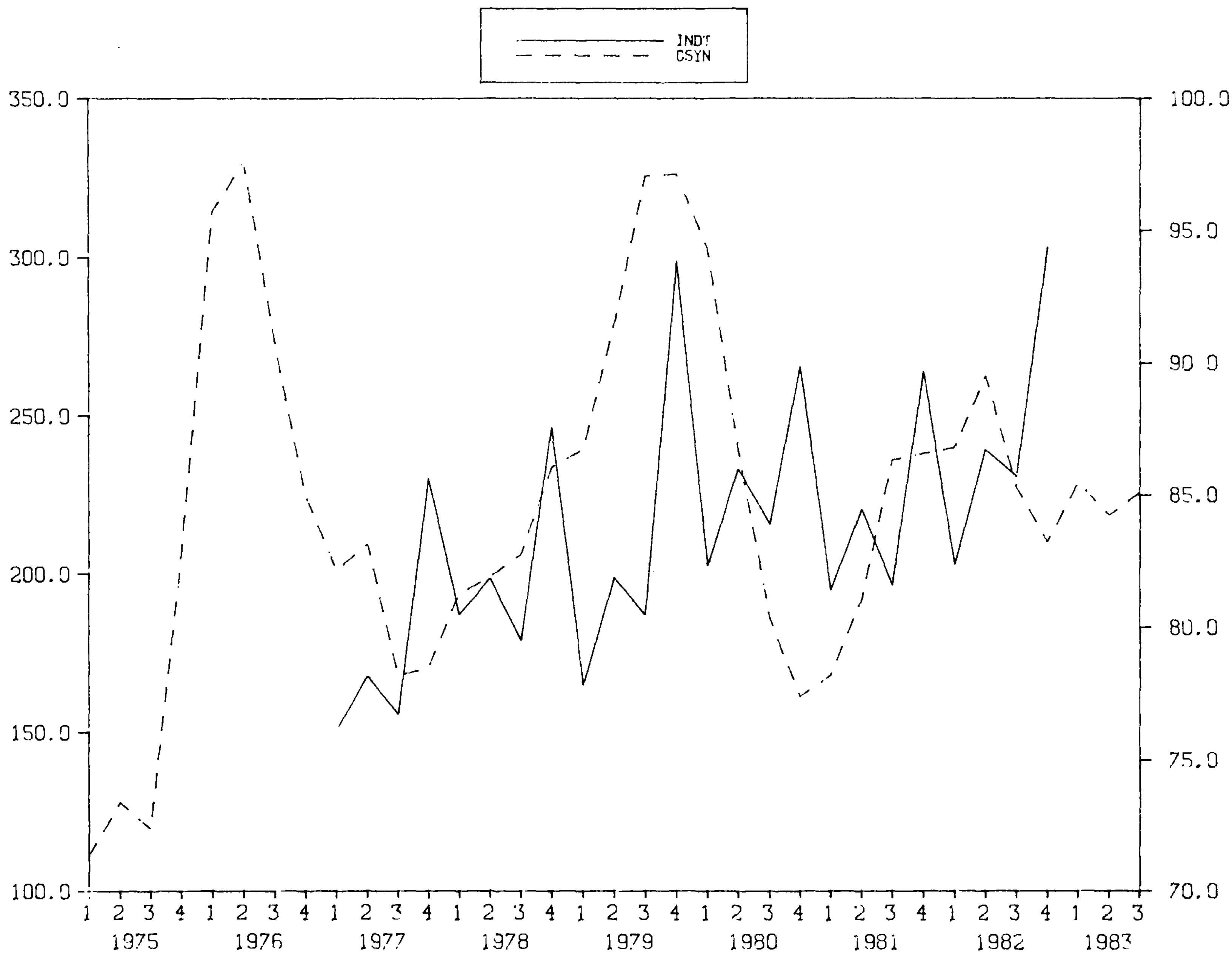
	Belgium Number	Belgium Per cent Change	Belgium Index 1975=100	Germany Number	France Number	Netherlands Number	Relative performance of Belgium 1/
1971	...	...	...	4,437	...	2,753	...
1972	1,555	...	69.4	4,575	...	2,605	...
1973	1,849	18.9	82.5	5,515	9,441	2,545	...
1974	1,881	1.7	83.9	7,722	10,400 2/	3,155	...
1975	2,242	19.2	100.0	9,195	12,400 2/	3,394	100.0
1976	2,459	9.7	109.7	9,362	13,400 2/	3,387	104.8
1977	2,471	0.5	110.2	9,562	13,842	3,257	103.3
1978	2,789	12.9	124.4	8,722	15,589	3,074	113.5
1979	2,921	4.8	130.3	8,319	15,863	3,499	117.6
1980	3,519	20.5	157.0	9,140	17,375	5,116	124.0
1981	4,133	17.4	184.3	11,653	20,895	7,275	115.7
1982	4,230	2.3	188.7	15,877	20,468	8,640	104.8
1983 January-June	2,236	-- 3/	...	...	...	...	...

Sources: Agéfi, various issues; Frankfurter Allgemeine, various issues; INSEE, Informations Rapides; Central Bureau of Statistics, Statistisch Dagboek; and Statistisch Bulletin.

1/ Belgium number of bankruptcies relative to the sum of Germany, France and Netherlands (Index, 1975=100).
2/ Estimate.
3/ Compared with same period of 1982.

Chart 16

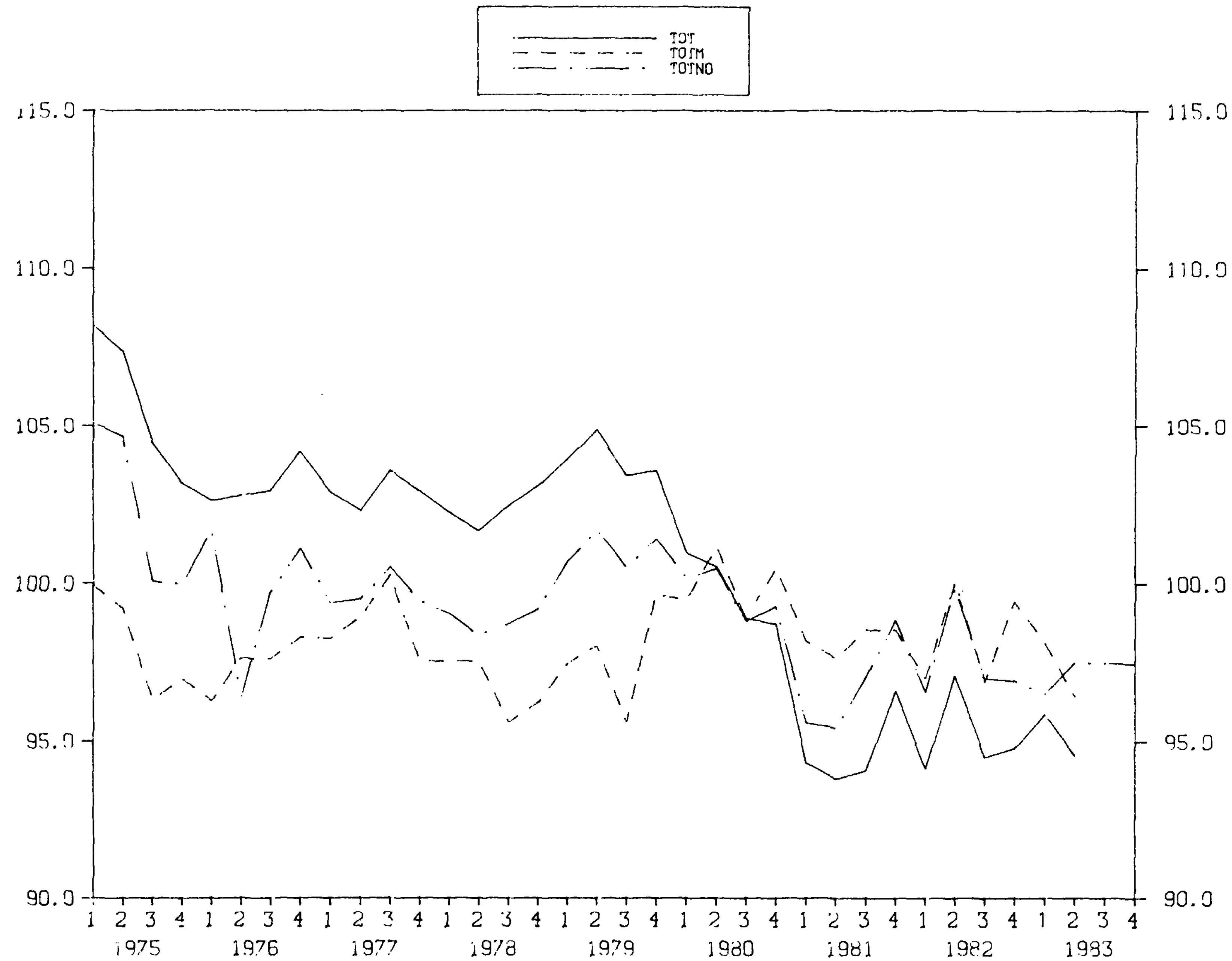
Belgium: Business Sentiment and Investment



CSYN = Composite index of business sentiment (right scale)
INDT = Investment index, total (left scale)

Chart 17

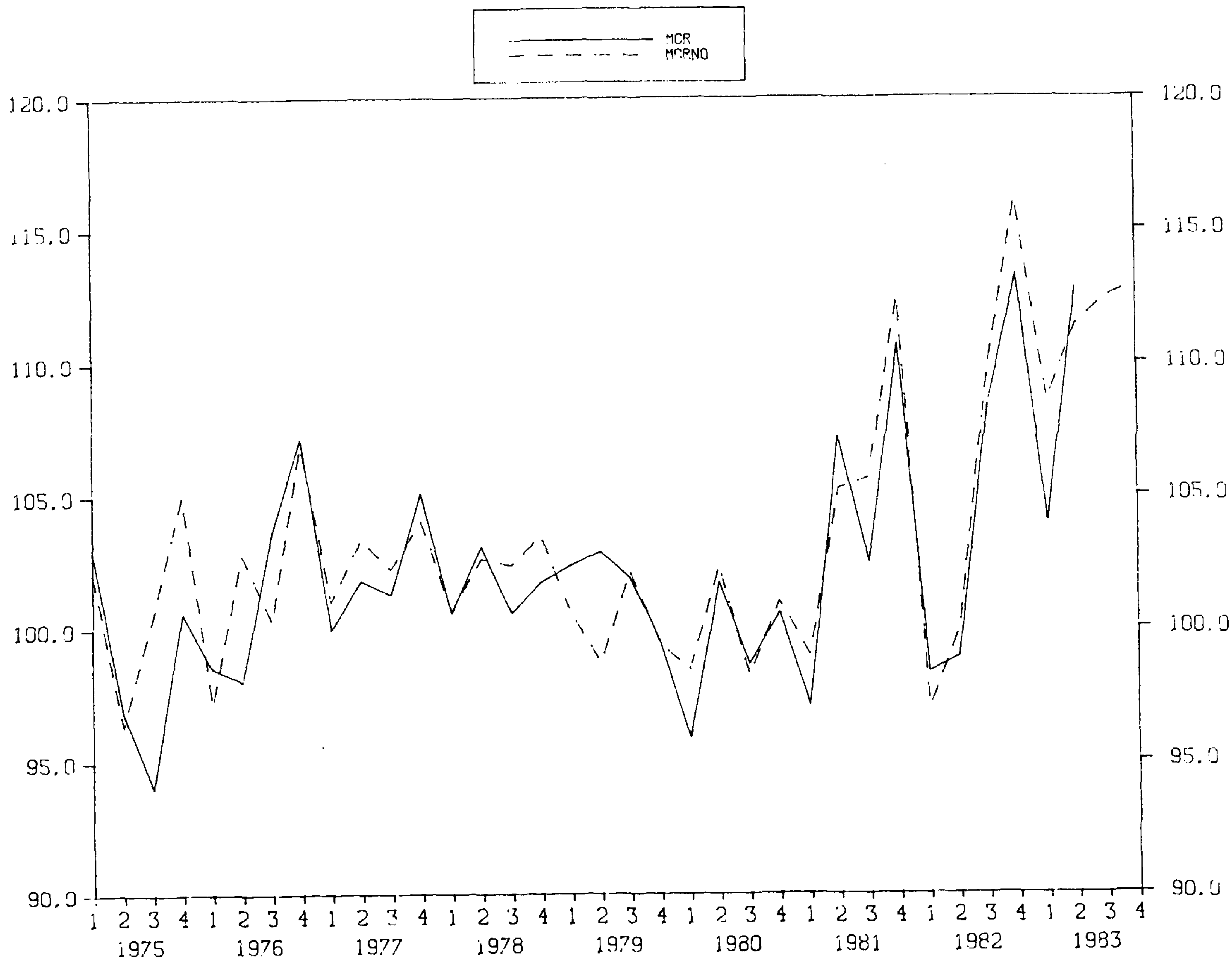
Belgium: Terms of Trade



TOT = Total
TOTM = Manufactured goods
TOTNO = Non-oil

Chart 18

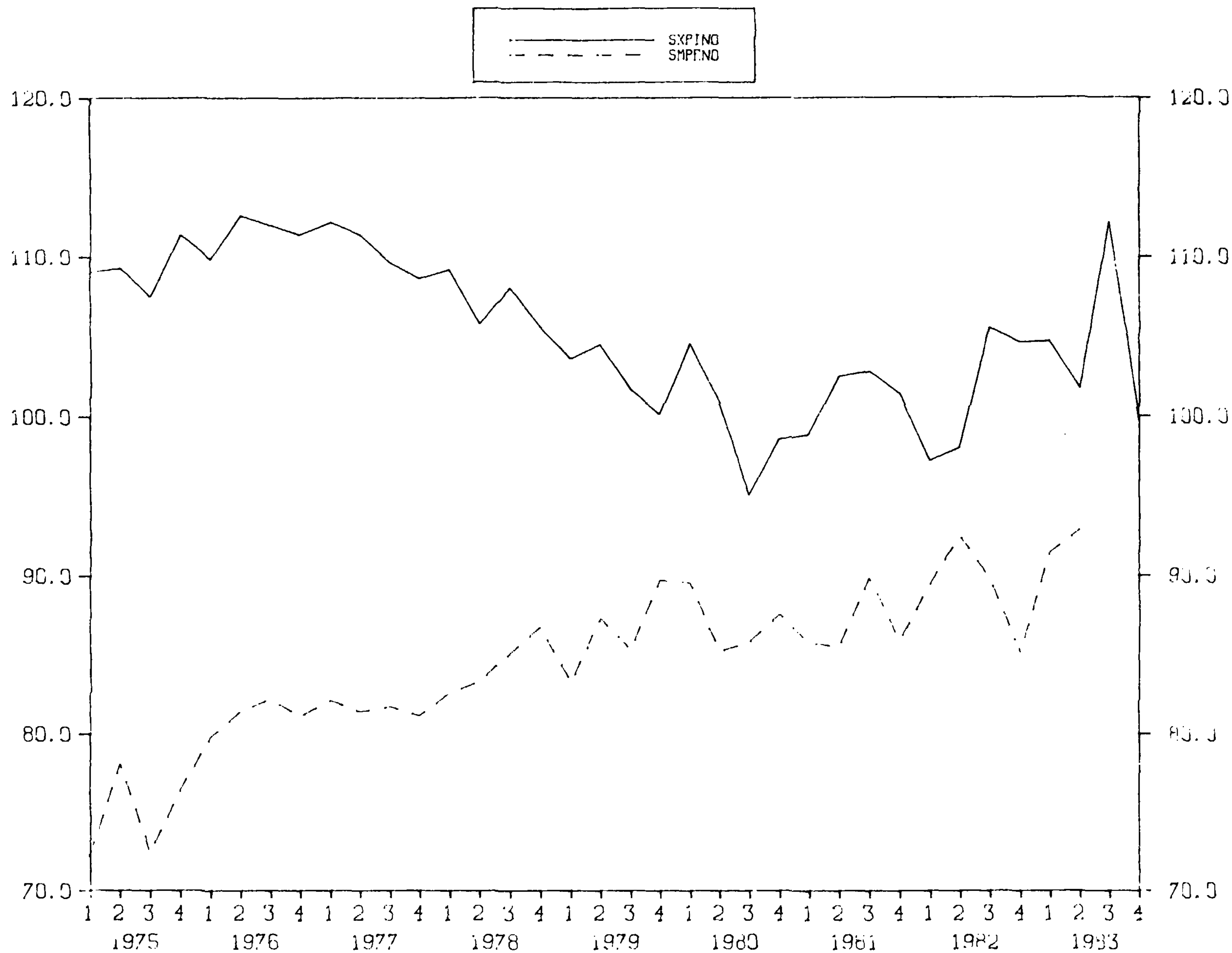
Belgium: Import Cover Ratios



MCR = Import cover ratio, total.
MCRNO = Import cover ratio, non-oil.

Chart 19

Belgium: Export Performance and Import Penetration



SXPINO = Export performance, non-oil products, volumes, seasonally adjusted.
SMPENO = Import penetration, non-oil products, volumes, seasonally adjusted.

Belgium: Chronology of Trade Issues and Measures

The following is a chronological list of the main trade issues concerning Belgium or the BENELUX, and of the most important trade measures taken by the Belgian authorities from the last quarter of 1982 to the time of the most recent information available. Relevant material from Trade and Payments Division files and other sources is attached.

Issues and measures concerning the EEC as a whole are not reported. However, measures authorizing special treatment for Belgium or the BENELUX under EEC rules, as well as main European Court of Justice rulings involving trade-related disputes, are reported.

November 8 and 21, 1982. The European Commission decided to initiate Article 93(2) procedures in respect of three planned aid measures notified by the Belgian government to assist a stockings and tights firm, and two carpet and floor-covering firms.

February 9, 1983. The European Commission ruled that two aid measures proposed in August under the Belgian textile plan to assist a combed wool spinning firm and a carpet and floor-covering firm were incompatible with the common market.

February 10, 1983. The European Commission notified the Belgian government that its plan to aid the textile and clothing industry could only be implemented if it conformed to several conditions (refer to Attachment 1).

March 9, 1983. The European Court of Justice found Belgium guilty of maintaining an obstacle to intra-Community trade through a 1975 Royal Decree making the marketing of pesticides subject to governmental authorization (Attachment 2).

April 19, 1983. The European Commission initiated Article 93(2) procedures in respect of a plan by the Belgian government to give aid to one stockings and tights manufacturing firm and one toweling fabrics and toilet linen firm.

May 12, 1983. The European Commission ruled that Belgium had failed to fulfill its treaty obligations by levying storage charges on goods originating in a member state or in free circulation, which were imported into Belgium and presented solely for the completion of customs formalities at a special store.

July 26, 1983. The European Commission authorized BENELUX countries to carry out intra-Community surveillance on rubber footwear imported from Japan, and iron and steel tubes and pipes imported from Romania.

August 10, 1983. The European Commission protested an aid project in the amount of BF 725 million for a firm manufacturing artificial fibers and tufted carpets (Attachment 3).

August 23, 1983. The European Commission adopted a regulation setting provisional quantitative limits for imports into the BENELUX countries of a number of textile products originating in China. The limits apply to goods imported during 1983.

"EUROPE" Friday 11 February 1983

TEXTILES: THE EUROPEAN COMMISSION'S APPROVAL OF THE BELGIAN AID PLAN IS SUBJECT TO SEVERAL CONDITIONS.

BRUSSELS (EU) Thursday 10 February 1983 - The European Commission has decided that the Belgian plan to aid the textile and clothing industry can only be approved if certain conditions are met. The Belgian government has been informed that it can implement its plan on the following conditions:

- the total budget for aids in 1983 must not exceed BFR 4,000 million;
- only up to 50% of restructuring investment may be financed by loans from public funds (with a maturity of up to ten years), which may carry interest subsidies of 7% for five years.
- if the loans are raised on the capital market, aid may extend only to an interest subsidy. In such cases a supplementary State guarantee may be granted for up to 50% of the funds so borrowed;
- firms in the sensitive sectors of combed sheep's wool yarn, tights, woven pile fabrics, tufted carpets and the synthetic fibre industry must be excluded from the aid scheme;
- aid to a further eleven sub-sectors is subject to prior notification if the recipient has a work force of more than 150;
- aid may be granted only to viable firms which satisfy particular minimum requirements concerning their financial position;
- the aid must not lead to increases in capacity;
- firms in the textile and clothing industry must not be granted any additional or alternative aid;
- all cases of aid are subject to subsequent checking.

ATTACHMENT 2

C O U R T O F J U S T I C E : BELGIUM FOUND GUILTY OF RESTRICTIONS TO PESTICIDE TRADE

LUXEMBOURG (EU) Wednesday 9 March 1983 - The European Court of Justice has just found Belgium guilty of still maintaining in force a 1975 Royal Decree on the intra-Community marketing of pesticides. The European Judges are thus following the Commission, for which this Decree harms non-Belgian producers, and constitutes, by this fact, an obstacle to intra-Community trade. The Royal Decree of 5 June 1975 submits the marketing of pesticides and phytopharmaceutical products to governmental authorization. This authorization may only be obtained by a person established in Belgium, and who, in addition, must be the manufacturer, the importer, the owner or the agent of the product. Hence the Commission's criticisms, the latter considering this condition to being contrary to the provisions laid down in the EEC Treaty. The Belgian Government defended itself during the proceeding, saying that the measure was justified, taking into account the dangerous character of the products, by the need of protecting public health. Furthermore, the Belgian Government said, the aggregation arrangements for these products were not yet harmonized at Community level. The European Court did not follow the Belgian reasoning, and declared that the Belgian measure would only be justified if it were proven that it is necessary and that the protection of the public health cannot be achieved by measures which are less restrictive to the free circulation of goods within the Community. As, according to the Judges, the Belgian Government had not given this proof, Belgium is found guilty of the offense.

"Europe," August 11, 1983

A I D S : COMMISSION CONTESTS BELGIAN AID PROJECT FOR TEXTILE INDUSTRY

BRUSSELS (EU) Wednesday 10 August 1983 - The European Commission has just addressed a letter to the Belgian Government, contesting the accordance with the Belgian Textile Plan and the rules of the Treaty of an aid project to the amount of BF 725 million, to the FABELTA company, which manufactures notably manmade fibres and tufted carpets. The matter concerns, in fact, products for which there are overcapacities of notable productions in the Community. Furthermore, the Beaulieu company, taking over the bankrupt FABELTA, contributes only a 21.6% share to the earmarked investments, whereas the Belgia Textile Plan stipulates alone the support of private capital of at least 50% in the sector's restructuring operations.

The Belgian Government now has four weeks in order to carry out the necessary amendments to its aids projett. Meanwhile, the aid cannot be paid.