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May 17, 1985

To: Members of the Executive Board  
From: The Secretary  
Subject: Belgium - Decision on Interest Rates

The Secretary has received the following memorandum dated May 14, 1985 from Mr. de Groote:

The National Bank of Belgium has informed me that in view of the climate of easing in the money market and the effective reduction of market interest rates, the Bank has lowered its official discount rate from 11.0 percent to 9.75 percent, and its rate for advances in current account from 12.0 percent to 10.25 percent, effective May 9, 1985.

Moreover, in order to obtain greater flexibility in the handling of its rates, the Bank has decided to change the procedures for setting them. Herewith you will please find the official notification of this change.

I would appreciate it very much if you would inform the members of the Executive Board.

Attachment

Other Distribution:  
Department Heads



ATTACHMENT

Annex to memorandum of May 14, 1985

Translation of telex received from J. Godeaux, Governor of the National Bank of Belgium :

"Since the tensions which arose in the exchange markets of the European Monetary System member countries during the first quarter of 1984 have been resolved, the Bank has gradually arranged for a reduction of rates on the domestic money market. Thus, the rate for three-month Treasury certificates, an important instrument of that market, which had been raised to 12.25 per cent in February 1984, was gradually lowered to 9.50 per cent.

"This lowering had the effect of bringing down other short-term rates, in particular the rates for bank credit, which were reduced by 1.50 to 1.75 per cent depending on the type of credit. In addition, the yield of large Belgian franc deposits with banks decreased by some 3.0 per cent over the same period.

"The Bank's action, undertaken in a climate of easing, resulted in the effective reduction of the cost of credit and of the Treasury's financing costs, whose impact was the broader since that action also facilitated a downward movement of long-term rates.

"These developments occurred without the Bank having aligned its own rates with those of the market. The Bank's hesitation to lower the official rates stems from the following considerations : Changes in the Bank's rates have come to be assigned a traditional importance which greatly exceeds their technical significance. Having become a symbol, the official discount rate is thus today an unwieldy instrument, while for a decade now monetary policy has been faced with much faster, wider swings in the money markets and the exchange market than ever before.

"When easing in the money market puts the market "ex-bank", there is no objection to this inertia of the rates of the Bank, which actually implements its policy through the market rates by encouraging them to come down. However, this does not hold true when the abundance of funds on the money market disappears, especially during periods of tension on the exchange markets: in that case, the Bank must be able to adjust its own rates quickly to match increases in various sectors of the short-term market. If this technical maneuver is delayed by its excessive symbolic significance, the Bank will be forced to replenish the resources of the short-term market for too long at too low a price, and more often than not, will sustain a decrease in its exchange reserves.

"To overcome these problems and obtain greater flexibility in the management of its rates, the Bank has decided to change the procedures by which the rates are set.

"Henceforward the Bank's discount rate will be fixed every Wednesday by the Council of Regents, based on the rate for three-

month Treasury certificates in effect the day before. Simultaneously, and on the same basis, the Council will set lower and upper limits within which the Board of Directors may adjust the discount rate if market developments require that this be done before the next regular meeting of the Council. The rate for secured advances will be set so as to make it very close to the actual cost of rediscounting.

"As in the past, the market will be informed immediately of any change in the discount rate, and the new rate will be effective the day after it is announced.

"On May 8, 1985 the discount rate was fixed at 9.75 per cent and the rate for advances at 10.25 per cent."

J. GODEAUX, GOVERNOR, BANKIONALE