FOR INFORMATION

FO/DIS/20/54

March 24, 2020

To:	Members of the Executive Board
From:	The Secretary
Subject:	**Belgium—Staff Report for the 2020 Article IV Consultation—Statement by the Executive Director**

Board Action:	Executive Directors' **information**
Additional Information:	The attached statement from the Executive Director for Belgium, is being issued on Belgium—Staff Report for the 2020 Article IV Consultation (SM/20/69, 3/16/20) which is being considered on a lapse of time basis.

Statement by Mr. De Lannoy and Mr. Cools on
Belgium—Staff Report for the 2020 Article IV Consultation

We thank staff for the insightful report, its annexes and the Selected Issues Paper *'The Appropriate Fiscal Stance: A Model Assessment'*. We also thank staff for the productive interactions with the Belgian authorities, and for their flexibility to adapt the draft report in light of the unfolding COVID-19 crisis.

Recent Developments

On March 17, a new Federal Government led by Ms. Sophie Wilmès was sworn into office. On March 19, a vote of confidence garnered a large majority in the Lower House of the Federal Parliament[1]. The new government obtained a specific mandate to address the fall-out from the COVID-19 crisis, which at the time of issuance has infected 3743 citizens and caused 88 casualties in Belgium. On Thursday March 26, the Lower House is expected to delegate exceptional legislative powers to the Federal Government to enable a swift implementation of its mandate. This delegation of powers encompasses public health, social policy, labor law, public order, and economic policy. The acts adopted by the Government on the basis of this delegation can enter into effect immediately upon enactment and shall be submitted to the Lower House for ex post validation within three months upon enactment. A similar extraordinary delegation of powers was most notably used in 1996 when far reaching measures were needed to meet the Maastricht convergence criteria for joining the Economic and Monetary Union.

Both the outgoing and the new Federal Government have adopted a string of targeted fiscal and financial measures in response to the COVID-19 outbreak. On the fiscal side, this includes enhanced access to temporary unemployment, deferred payment of personal income and corporate taxes, withholding tax, VAT, and social security contributions, exemptions of social security contributions, replacement incomes for the self-employed, and suspension of penalties for public contractors, as well as several sector-specific support measures. On March 19, the Lower House approved a 1 billion EUR additional expenditures package to combat the COVID-19 crisis.

With the support of the National Bank of Belgium (NBB), the Federal Government has agreed with the financial sector on a 50 billion EUR (about 10% of GDP) guarantee scheme for all new credit with a maximum duration of 12 months, extended up till end September 2020 to viable businesses. The financial sector has also agreed to accept deferred payments to September 30 on all loans to viable businesses. Finally, on March 11, the NBB entirely released the countercyclical capital buffer of 0.5% of banks' risk weighted assets. This release will remain in force for at least a year.

The three Regional Governments of Flanders, Wallonia and Brussels have also adopted a series of targeted measures, as they manage extensive levers of economic policy. They, among others, extended crisis guarantees to affected firms, created compensation schemes for affected businesses, and suspended energy bill payments for vulnerable groups.

The authorities welcome the Eurogroup statement of March 16, including the wording on flexibility under the Stability and Growth Pact, and the guidance of the European Commission on state aid to affected firms.

[1] The Lower House gathered in a severely restricted format due to the COVID-19 crisis.

They also welcome the bold actions by the European Central Bank ('ECB') to support all sectors of the economy and its commitment to do everything, as much as necessary and for as long as needed. Finally, they welcome the ECB Banking Supervision's announcement on temporary capital and operational relief measures to stimulate bank lending.

Outlook and risks

While staff rightly noted that GDP growth was resilient prior to the COVID-19 outbreak, reaching 1.4% in 2019, significant downward revisions are now expected for 2020. Risks to growth, now firmly to the downside, were already tilted downwards prior to COVID-19. A hard outcome from the negotiations between the EU and the UK on their future trading relationship in particular and continued trade uncertainty globally remain significant risks to Belgium's open economy.

Return to a Structural Equilibrium

Once the COVID-19 crisis will have abated and the related temporary targeted fiscal measures will have run their course, a return to the medium-term objective of a structural equilibrium will be the top priority for Belgium. The authorities agree with staff that a credible, sustained, and growth-friendly medium-term consolidation strategy is needed to put the deficit and debt on a firm downward path, and have taken good note of the case made in the Selected Issues Paper on the high marginal benefit of building buffers. They agree with staff that a medium-term strategy should be pursued by containing aging costs, reorienting the budget toward growth-enhancing areas, and improving spending efficiency. In that light, they very much welcome the annex on Benchmarking and Prioritizing Spending Reforms.

While committed to the European Union's fiscal rules, the authorities also recognize that flexibility with regards to investment will be necessary, given Belgium's important need for infrastructure and green investments. Finally, guaranteeing the sustainability of public finances is a task for both the federal state as well as the Regions and Communities, especially as the latter now oversee a much greater portfolio since the 2011 devolution of powers under the sixth State Reform.

Structural Reforms

The authorities largely agree with staff's advice to remove structural growth constraints, and thus to improve Belgium's competitiveness and external position.

Prior to the COVID-19 outbreak, the Belgian labor market was operating at an all-time high, with the unemployment rate at 5.4%, and the employment rate at 70.5% in 2019, compared to 67.2% in 2015. The authorities agree with staff that further efforts will be needed to increase labor force participation, especially among vulnerable groups. The regional active labor market policies implemented by the three regional governments last year are key tools here. They are all the more important as the working age population is set to shrink in the future, as a result of population ageing. Belgium's labor shortage[2] can prevent firms from investing, muting productivity growth. Yet productivity gains are essential to generate sustainable growth, once the labor potential has been fully exploited. It is therefore vital to render the economic fabric more dynamic and to step up investments in growth-enhancing infrastructure, in line with the National Pact on Strategic Investments.

---

[2] Belgium has the highest vacancy rate in the euro area: Staff Report, figure 5, p. 35.

Boosting the growth potential by increasing productivity and the number of people at work is the only sustainable source of purchasing power and income creation. If more people are integrated into the labor market, growth will also become more inclusive, as employment is a powerful driver of social inclusion, and the best protection against poverty. Generating more growth and employment also makes it easier to consolidate public finances. That is the only way to continue mobilizing sufficient resources to provide an effective social security safety net in the face of population ageing.

Financial Sector

The Belgian financial sector is well positioned to weather adverse shocks given its high levels of capitalization and solid liquidity buffers. To address the rise in private leverage, the NBB has adopted consecutive macroprudential measures in the residential real estate sector, including last year, as well as the above mentioned CCYB, now released due to the COVID-19 crisis.

The authorities agree with staff that supervision of systemic financial conglomerates should be further operationalized, especially given their weight in the Belgian financial sector. The authorities therefore welcome the development of technical standards on the reporting of intragroup transactions, risk concentration, and capital adequacy for systemic financial conglomerates. The authorities also agree with staff that the feasibility and effectiveness of bank-resolution strategies shall be ensured, including by maintaining a sufficient and consistent allocation of MREL across banking groups. Finally, a compliant implementation of Basel 3.5 in European law will be crucial to ensure financial stability.

Climate

The authorities would like to thank staff for their intention to dedicate a specific section in next year’s Article IV staff report on the climate transition.