GREEN/20/40

March 26, 2020

Green Statement from Mr. Buisse, Mr. Rozan and Ms. Gilliot on Belgium—Staff Report for the 2020 Article IV Consultation (SM/20/69)

We thank staff for this interesting set of documents which clearly stress that priority should be given to addressing the coronavirus outbreak through near term measures, allowing subsequently to address medium-term structural challenges through a better reallocation of spending to growth-friendly measures and rebuild resilience on sound foundations. We also thank Mr. De Lannoy and Mr. Cools for their informative Buff statement. While we broadly concur with the thrust of the analysis and recommendations of the report, our first thoughts go out to the people of Belgium and those who have lost their lives. We commend the authorities for their prompt responses on the fiscal, financial and monetary side, which have been strongly backed, at the European Union level, by a coordinated policy action from the ECB and the European Commission. Over the medium-term and given this global extremely severe shock, rebuilding fiscal buffer and removing the long-lasting structural impediments to productivity will be essential to enhance Belgium's capacity to react to the next potential shocks, liberate the full potential of the economy and moderate hysteresis effects as demonstrated in the useful Selected Issues Paper.

Like other countries, the authorities should prepare to an adverse scenario as the most likely outcome, although all forecasts are likely to be wrong to some degree. Against exceptional circumstances and given the rate of deterioration of the external environmental, staff's baseline scenario, which, at the time of the mission, may have appeared conservative to some, is likely to be revised downward. The effects of the pandemic could be rapidly magnified by an incomparable uncertainty affecting supply and demand and political paralysis due to the delays in forming a new government. On the positive side, the speed in ensuring that the coronavirus is contained and the entry into office of a new administration would lay the foundations for structural reforms and rapid recovery. Furthermore, we would like to emphasis a few aspects of the report.

1. Fiscal Policy

Designing an adequate medium-term strategy to mitigate rising fiscal risks will be important once the damaging effects of the crisis have been contained. Priority must be given over the short-term to support vulnerable groups and firms affected by the outbreak. This health crisis has also already started to contaminate financial markets severely through massive sell-off of risky assets and tightening financing conditions. As pinpointed in the *Risk Assessment Matrix,* trade deceleration, lower investment and the risk of protracted growth slowdown might complicate fiscal adjustment as levels of deficit and public debt will be already high and rising. Fiscal consolidation needs to be accordingly resumed over the medium-term by concentrating efforts in growth-friendly areas, rationalizing public spending like subsidies (tax exemptions mainly) and the total general government's wage bill, widening the tax base and increasing spending efficiency in health, education and other social protection benefits. Although above the EU14 level, efficiency in social protection spending could be further heightened by aligning better the pace of increase of the effective retirement age and the minimum retirement age with life expectancy. The unemployment system should be revisited to incentivize job-seeking and return to work.

2. Structural reforms

Despite the difficult circumstances, the rise in external and domestic downside risks advocate for a deepening of structural reforms. In line with the 2019 Article IV consultation's recommendations, efforts need to be stepped up to foster labor-force participation, especially among the most vulnerable categories of population like women, young, old or low-skilled. In parallel, labor mobility should be enhanced, and skills mismatches reduced through a more effective training and adequate education policies. Along with active labor market policies, potential growth could be further boosted, and we agree that keeping addressing Belgium-specific factors as pointed out by staff in this report and the past one is warranted. In this regard, a comprehensive tax reform would certainly be a supportive tool to increase female labor force participation, increase labor mobility and promote innovative firms and R&D activities. More needs also to be done to foster competition, facilitate business creation and increase investment in infrastructure if possible. Lastly, we would like to thank staff for their special Box2 related to initial considerations on climate-mitigation efforts in the country. Relatedly we would have appreciated among the policy options presented more specification and quantified targets related to feebates and carbon taxes.

3. Financial system

While macroprudential policies have been tightened last year and the financial sector remains sound and well-supervised, developments in the housing market and credit-growth to households and firms should continue to be closely monitored against the coronavirus outbreak. We welcome the authorities' willingness to carefully follow the evolution of challenges posed by the low interest rate environment, digitalization and private sector leverage as well as their commitment to complete the remaining 2017 FSAP recommendations. Banks are facing the same low profitability issues as in many advanced and emerging countries and we agree that without interfering in banks' business choices, the supervisory authorities should encourage banks to streamline costs, diversify sources of income and complete its transition to digital banking. We agree that the credit-to-GDP remains an important benchmark to assess potential imbalances between credit growth and economic growth and a useful guide for macroprudential policy decisions. Since discrepancies between standard BIS/ECB measures, NBB's proper evaluation and the alternative credit-gap estimates developed by the IMF emerge clearly as non-negligible, a close and continuous monitoring of credit growth is essential to prevent excessive credit growth and the formation of asset-price bubble. We finally encourage the authorities to increase the efficiency of the macroprudential decision-making process and achieve the completion of bank resolution and deposit insurance frameworks.