INTERNATIONAL MONETARY FUND

IMF Country Report No. 18/71

BELGIUM

March 2018

2018 ARTICLE IV CONSULTATION—PRESS RELEASE; STAFF REPORT

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2018 Article IV consultation with Belgium, the following documents have been released and are included in this package:

- A **Press Release** summarizing the views of the Executive Board as expressed during its March 7, 2018 consideration of the staff report that concluded the Article IV consultation with Belgium.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on March 7, 2018, following discussions that ended on December 18, 2017, with the officials of Belgium on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on February 21, 2018.
- An **Informational Annex** prepared by the IMF staff.

The documents listed below have been or will be separately released.

Selected Issues
Financial Stability System Assessment

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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FOR IMMEDIATE RELEASE
March 8, 2018

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

IMF Executive Board Concludes 2018 Article IV Consultation with Belgium

On March 7, 2018, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with Belgium.

The economic recovery is gaining momentum, with real GDP growth expected to approach 2 percent this year after an estimated 1.7 percent in 2017. It is driven by strong investment and solid consumption growth, and supported by favorable financial conditions as well as a strengthening recovery throughout Europe. Employment growth has picked up, thanks in part to past reform efforts. The fiscal position has improved, reflecting a mix of cyclical, structural, and one-off factors. The medium-term outlook, however, remains subdued in the absence of further structural reforms to raise potential growth, and subject to both external and domestic risks.

Against this favorable economic context, the governing center-right coalition is making another reform push, agreeing on a new package of tax and labor market measures. The centerpiece of the agreement is a reform of the corporate income tax system, designed to promote investment by lowering the comparatively high statutory rate while broadening the tax base to preserve revenue neutrality.

Looking ahead, Belgium faces challenges on several fronts. Notwithstanding the strong fiscal outturn in 2017, fiscal consolidation remains a priority given the high level of public debt that has only just started to decline. Achieving the government's goal of structural balance will require significant efforts to make spending more efficient while safeguarding revenues. Another important challenge is raising Belgium's productivity growth, which has lagged peers, in part reflecting sectoral shifts common to many advanced economies, but also underinvestment in infrastructure and lack of competition in some service sectors. Despite recent employment gains, the labor market remains fragmented, as evidenced by entrenched high unemployment among certain groups and significant regional disparities.

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

While the soundness of the financial sector has improved considerably since the crisis, cyclical vulnerabilities are rising, and there are pockets of vulnerability in the housing market. The banking sector faces the challenge of adapting to a changing economic, technological, and regulatory environment. The transition toward a full European Banking Union is another important issue to be navigated by banks and supervisors.

Executive Board Assessment[2]

The Executive Directors commended the Belgian authorities for their reform efforts which have contributed to a strengthening of economic recovery, a pickup in employment growth, and a significant reduction of the fiscal deficit. Directors encouraged the authorities to take advantage of the current favorable economic conditions to push ahead with additional reforms to enhance the resilience and long term growth potential of the economy.

Directors agreed that gradual fiscal consolidation remains a priority in light of the high level of public debt. They emphasized the need for deeper reforms to make public spending more efficient, which will require coordination and participation across all levels of government.

Directors welcomed the reform of the corporate income tax system, which should help boost investment while broadening the tax base. They saw scope for additional reforms to address remaining distortions in the tax system and safeguard revenues in the context of the next phases of the tax shift.

Directors stressed that raising Belgium's rate of productivity growth is important to improve external competitiveness and mitigate the impact of population aging on potential growth. To this end, they encouraged the authorities to increase investment in transport infrastructure, enhance competition in services, and foster innovation.

Directors observed that the fragmentation of the labor market prevents Belgium from realizing its full employment and growth potential. To better integrate vulnerable groups, Directors highlighted the need to address educational gaps, improve on the job training, and reduce barriers to geographical mobility. They noted that the wage setting process should take into account not only comparator country wages but also productivity developments and broader labor market conditions in Belgium.

Directors welcomed the improved soundness of the financial sector, but noted that cyclical risks are rising, including growing pockets of vulnerability in the housing market and rising corporate debt. They supported enhancing the central bank's ability to deploy macroprudential measures in a timely manner when warranted by rising balance sheet risks in the financial sector. Directors

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[2] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.imf.org/external/np/sec/misc/qualifiers.htm.

emphasized that the financial sector should continue to adapt to economic, technological, and regulatory changes. They encouraged the authorities to carefully navigate the transition to a full European Banking Union, including by continued close supervision of systemically important subsidiaries of euro area banks operating in Belgium.

Belgium: Selected Economic Indicators, 2015–19

	2015	2016	Est. 2017	Projections 2018	Projections 2019
	(Percent change, unless otherwise indicated)				
Real economy					
Real GDP	1.4	1.5	1.7	1.9	1.7
Domestic demand	1.4	2.1	1.4	1.8	1.7
Private consumption	0.9	1.7	1.1	1.4	1.6
Public consumption	0.5	0.5	0.7	0.7	0.6
Gross fixed investment	2.7	3.6	1.1	3.7	3.2
Stockbuilding[1]	0.2	0.2	0.4	0.0	0.0
Foreign balance[1]	0.0	-0.6	0.3	0.1	0.0
Exports, goods and services	3.3	7.5	4.5	4.7	4.0
Imports, goods and services	3.3	8.4	4.3	4.6	4.1
Household saving ratio	11.9	11.2	11.6	12.3	12.3
Potential output growth	1.2	1.2	1.4	1.5	1.5
Potential output growth per working age person	1.0	1.1	1.1	1.4	1.5
Output gap (in percent)	-0.8	-0.6	-0.3	0.1	0.3
Employment					
Unemployment rate (in percent)	8.5	7.9	7.3	7.0	6.8
Employment growth	0.9	1.2	1.2	1.1	0.9
Prices					
Consumer prices	0.6	1.8	2.2	1.6	1.8
GDP deflator	1.1	1.6	1.8	1.6	1.7
	(Percent of GDP; unless otherwise indicated)				
Public finance					
Revenue	51.3	50.7	51.1	50.4	50.1
Expenditure	53.8	53.2	52.3	51.7	51.4
General government balance	-2.5	-2.5	-1.2	-1.3	-1.3
Structural balance	-2.2	-2.2	-1.1	-1.4	-1.5
Structural primary balance	0.8	0.7	1.5	0.9	0.7
Primary balance	0.6	0.4	1.4	1.0	0.8
General government debt	106.0	105.7	103.3	101.1	99.1
Balance of payments					
Goods and services balance	1.7	1.3	1.0	1.1	1.0
Current account	-0.1	0.1	0.1	0.3	0.2
Exchange rates					
Euro per U.S. dollar, period average 2/	0.9	0.9	0.8	...	...
NEER, ULC-styled (2005=100) 2/	97.9	98.9	101.3	...	...
REER, ULC-based (2005=100) 2/	98.3	98.5	105.0	...	...
Memorandum items					
Gross national savings (in percent of GDP)	23.4	24.0	23.9	24.5	24.8
Gross national investment (in percent of GDP)	23.6	23.9	23.8	24.1	24.5
Nominal GDP (in billions of euros)	410.4	423.0	438.1	453.5	468.8
Population (in millions)	11.2	11.3	11.4	11.4	11.5

Sources: Haver Analytics, Belgian authorities, and IMF staff projections.

[1] Contribution to GDP growth.

[2] As of December 2017.

INTERNATIONAL MONETARY FUND

BELGIUM

STAFF REPORT FOR THE 2018 ARTICLE IV CONSULTATION

February 21, 2018

KEY ISSUES

The recovery is gaining momentum, with real GDP growth projected to rise to close to 2 percent in 2018. Job growth is picking up and the fiscal position is improving, as past reforms pay off and the recovery strengthens throughout Europe. This favorable economic context is an opportunity to enhance the resilience and long-term growth potential of the Belgian economy.

The near-term priority is to push ahead with growth-oriented, revenue-neutral tax reforms while continuing with gradual spending-based budget consolidation to reduce the high level of public debt. Over the medium term, reforms are needed to raise productivity growth and reduce labor market fragmentation while adapting the financial sector to a changing environment, with cyclical vulnerabilities rising. Staff welcomes the government's ongoing policy and reform efforts in this regard, and recommends:

- Complementing the corporate income tax reform and next phases of the tax shift with measures to safeguard revenues and address distortions in the tax system.
- Gradually moving toward a balanced budget, supported by efficiency-oriented spending reforms at all levels of government, while shifting from current to investment spending.
- Boosting productivity growth by upgrading infrastructure, particularly in transport and energy, and by strengthening competition in services.
- Unlocking the large untapped labor market potential by improving education and training of vulnerable groups and increasing mobility.
- Mitigating vulnerabilities in the mortgage market by raising risk-based capital requirements.
- Carefully navigating the transition toward a European Banking Union.

Approved By
Ms. Detragiache (EUR), Mr. Zeidane (SPR)

Discussions took place in Brussels December 5–18, 2017. The staff team comprised C. Mumssen (head), A. Jewell, A. Shabunina, and S. Voigts (all EUR) and was assisted at headquarters by T. Mohd Nor and K. Vanegas. A. de Lannoy, J. Clicq (both OED), and J. Hamann (MCM) participated in the discussions. Staff met with J. Smets (Governor of the National Bank of Belgium), J. Van Overtveldt (Minister of Finance), K. Peeters (Minister of Economy and Labor), S. Wilmès (Minister of Budget), J. Crucke (Minister of Budget, Finance, Energy, Climate, and Airports of Wallonia), senior officials from Flanders and the Brussels Capital Region, other senior government officials, representatives from the private sector, and trade unions.

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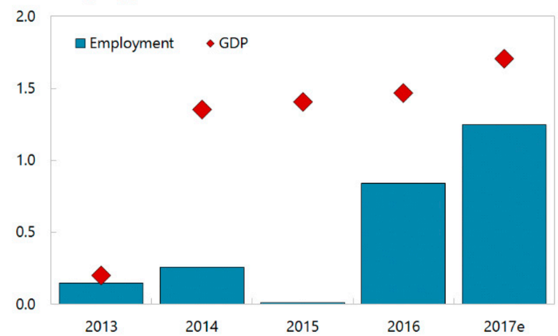
ANNEXES

CONTEXT—A HEALTHY RECOVERY AND RENEWED REFORM EFFORTS

1. **The government is making another reform push ahead of an upcoming election period.** Several important reforms have been implemented in recent years, including reductions in the labor tax wedge, the temporary suspension of wage indexation, and pension reform. The reform momentum slowed in 2016, particularly with respect to fiscal policies, but fiscal consolidation accelerated in 2017, and the governing center-right coalition agreed on a new package of tax and labor market measures. The centerpiece of the agreement was a reform of the corporate income tax system. These are important achievements as Belgium heads into local elections this year and regional and federal elections in 2019.

2. **The economic recovery has contributed to healthy employment growth.** Real GDP is estimated to have increased to 1.7 percent in 2017 from 1.5 percent in 2016. The recovery has been driven by strong business investment and solid private consumption growth, and aided by a combination of improving labor market conditions and favorable financial conditions supported by continued monetary accommodation by the ECB. The unemployment rate fell to 7.3 percent, approaching pre-crisis levels, and employment expanded by an estimated 1.2 percent, thanks in part to previous reforms to reduce taxes on labor (the "tax shift"), contain wage growth (the "index jump," a one-time suspension of wage indexation), and increase the effective retirement age.[1] Inflation rose to 2.2 percent, owing to higher domestic energy prices. Core inflation, at 1.5 percent, remained higher than the euro area average, partly reflecting price dynamics in service sectors such as restaurants, cafes, and telecommunications, where competition is relatively limited.

GDP and Employment Growth
(Percent, y-o-y growth)



Sources: Eurostat, IMF World Economic Outlook and IMF staff calculations.

3. **The current account is estimated to have remained close to balance in 2017, moderately weaker than implied by medium-term fundamentals.** After recording consistent surpluses prior to the global financial crisis, the current account has hovered around balance in recent years. Over 1999−2015, Belgium's share of world goods exports fell by 22 percent (from a 3.3 percent share to 2.6 percent) versus an average decline of 15 percent in high-income OECD countries. This trend is partly explained by the fact that Belgium's exports are concentrated in a European market that has become relatively less important in size. In addition, unit labor costs have risen more rapidly than in some peer countries, although wage moderation since 2013 has helped narrow the competitiveness gap. The ULC-based REER appreciated 13 percent from 2000 to 2013 before declining sharply in 2014 and 2015. Since end-2015, however, the ULC-based REER has

[1] According to a study by the National Bank of Belgium, the tax shift reform of 2015 is expected to result in 52,100 new jobs by 2021.

been on an appreciating trend once again. The external balance assessment (EBA) model yielded a cyclically adjusted current account norm of 1.8 percent of GDP in 2017 compared to an estimated actual surplus of 0.1 percent, implying a real effective exchange rate overvaluation of about 3 percent (Annex II).

4. The fiscal deficit decreased significantly thanks to a mix of cyclical, structural, and one-off factors. The headline deficit halved from 2.5 percent of GDP in 2016 to an estimated 1.2 percent in 2017, surpassing the target of 1.6 percent in the April 2017 Stability Program (Table 1). Corporate income tax revenues surged due to the cyclical recovery and measures taken by the government to encourage advanced payments. Spending on wages and unemployment benefits declined, reflecting the job-rich recovery and the payoff from previous reforms. Lower spending was also the result of large windfall savings from low interest rates and a significantly smaller contribution to the EU budget. Public debt, which stabilized at 106 percent of GDP in 2016, declined to an estimated 103 percent in 2017.

Table 1. Belgium: Budget and Projected Outturns

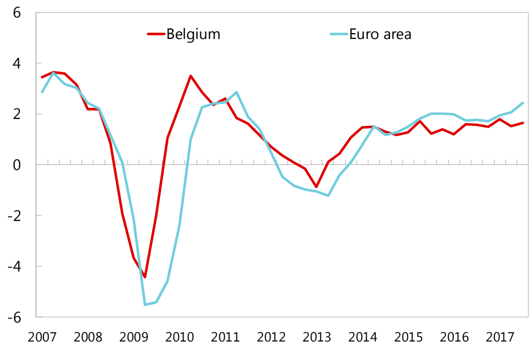
	2016 Outturn	2017 DBP 1/	2017 SP 2/	2017 Est.	2018 DBP 1/	2018 Proj.
			(Percent of GDP)			
Revenues	50.7	51.0	50.9	51.1	50.7	50.4
Expenditures	53.2	52.7	52.5	52.3	51.8	51.7
o/w: Wages	12.4	12.2	12.2	12.3	11.9	12.1
Social benefits	25.2	25.1	25.1	25.0	25.1	24.9
Subsidies	3.2	3.4	3.3	3.4	3.3	3.3
Interest	2.9	2.3	2.6	2.6	2.3	2.3
Balance	-2.5	-1.7	-1.6	-1.2	-1.1	-1.3
Authorities' structural balance	-2.0	-1.1	-1.0		-0.8	
Staff's structural balance	-2.2			-1.1		-1.5

Sources: Haver Analytics, Belgian authorities, and IMF staff calculations.
[1] Draft Budgetary Plan, submitted to the European Commission in October preceding the budget year.
[2] Stability Program submission, consistent with revised budget submitted in May.

Figure 1. Belgium: Macroeconomic Context

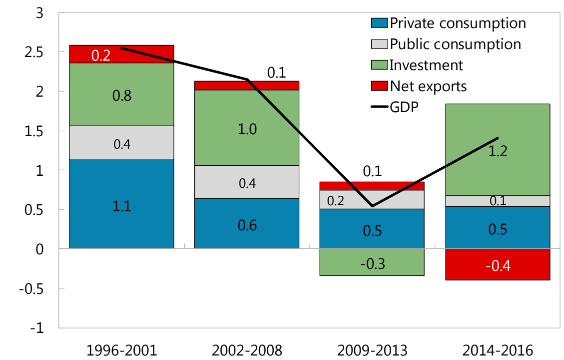
Growth has trailed the euro area average since 2015.

Real GDP growth
(Quarterly yoy growth rates in percent)



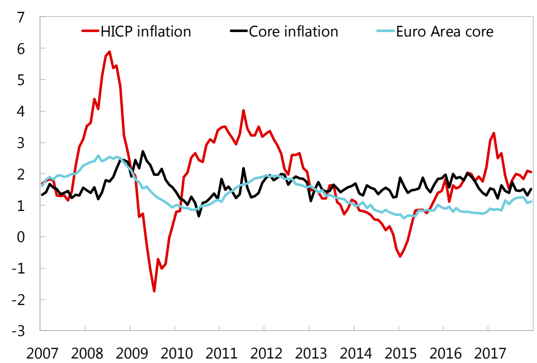
Investment has been the key driver of growth in recent years while net exports have turned negative.

Real Growth by Component
(In average annual growth over the period)



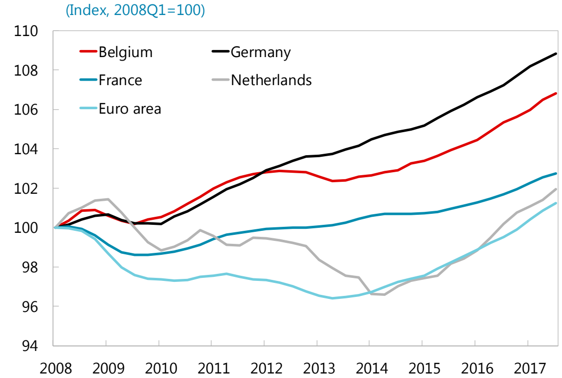
Headline inflation has recently subsided, while core inflation has remained above the euro area average.

Annual Inflation
(In percent)



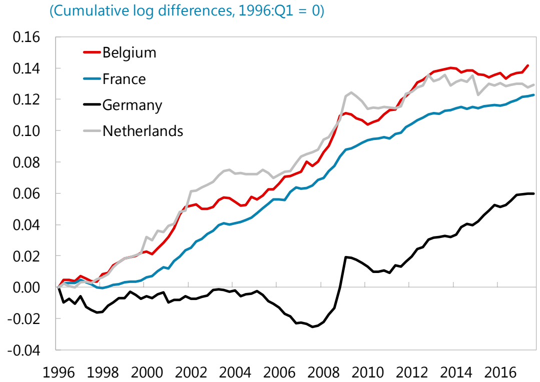
Employment growth has been healthy on account of the recovery as well as labor, tax, and pension reforms.

Employment
(Index, 2008Q1=100)



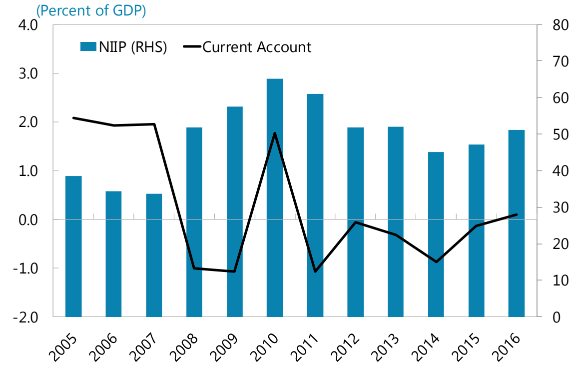
Unit labor costs have stabilized since 2013 reflecting wage moderation and a temporary suspension of indexation.

Evolution of Unit Labor Cost
(Cumulative log differences, 1996:Q1 = 0)



The current account has hovered close to balance since the crisis, while the NIIP remains strong.

Current Account Balance and NIIP
(Percent of GDP)



Sources: Haver Analytics, Eurostat, national statistical authorities, and IMF staff calculations.

OUTLOOK—RECOVERY GAINING MOMENTUM BUT RISKS DOWN THE ROAD

5. The recovery is gaining pace, but the medium-term outlook remains subdued. Staff projects growth to increase to close to 2 percent this year. Business investment should remain strong, supported by the improving economic outlook, rising capacity utilization in the manufacturing industry, and continued low interest rates. Private consumption growth is expected to increase as further tax reductions in 2018 and 2019 under the tax shift boost disposable income. Net exports, on the other hand, are not expected to contribute to growth, reflecting continued competitiveness challenges, which are partly related to weak productivity growth. Over the medium term, real GDP growth is expected to fall back to about 1½ percent. Potential output growth is currently estimated at around 1.4 percent, and projected to increase gradually as past and ongoing reforms and investment lead to higher potential employment and labor productivity growth. Headline inflation is projected to decline to 1½ percent in 2018 as energy prices recede while core inflation should increase gradually to over 2 percent as the output gap turns positive.

6. Risks to the outlook include potential external shocks and domestic political developments (Annex III). As a small, open economy highly dependent on external demand, Belgium is vulnerable to growth shocks in Europe. While the impact of the Brexit referendum has been limited so far, a "hard" Brexit would be detrimental given Belgium's close economic ties with the United Kingdom.[2] Geopolitical shocks or monetary policy normalization in advanced countries could lead to volatility and higher financing costs. A combination of lower growth and higher interest rates could result in adverse debt dynamics and eventually undermine investor confidence (Annex IV). On the domestic side, stock market valuations have risen substantially (albeit in line with other major European stock markets when abstracting from one large company), and sustained increases in housing prices coupled with pockets of high household leverage have increased risks. Reform momentum could slow in the run-up to federal elections in 2019, and the elections themselves could lead to a protracted period of uncertainty if the winning parties are unable to form a new coalition government.

[2] The United Kingdom is the fourth biggest market for Belgian exports and the fifth largest supplier of goods to Belgium. Trade in services between the two countries is also important, as are investment flows.

POLICY DISCUSSIONS—MAINTAINING THE REFORM MOMENTUM

7. **The current recovery is an opportunity to strengthen the resilience and growth potential of the Belgian economy.** The government's ability to deal with future shocks will depend on whether it implements the right policies now while the economy continues to recover.

- First, with public debt above 100 percent of GDP and only starting to come down, Belgium still has a long way to go to rebuild buffers and achieve a more sustainable fiscal position. This will require following through on plans to gradually move toward structural balance.

- Second, with real GDP growth projected at only around 1½ percent for the foreseeable future, further labor and product market reforms are needed to increase productivity growth, raise potential output, and integrate vulnerable groups into the labor market.

- Third, although the financial sector has recovered since the crisis and is generally sound, cyclical vulnerabilities are rising and new challenges are emerging, suggesting the need for vigilance and proactive policies.[3]

8. **The government agreed last summer on a new package of measures related to taxation, the labor market, and social benefits** (Table 2 and Box 1). The most notable reform was a reduction in Belgium's corporate income tax (CIT) rate from 34 percent to 25 percent, to be phased in over the next three years (SMEs will benefit from a reduced rate of 20 percent starting in 2018). To compensate for the resulting revenue loss, the notional interest rate deduction (NID) was modified to apply only to incremental corporate equity rather than to the total stock, and new anti-tax avoidance measures were introduced consistent with Belgium's EU obligations.[4] Together, the measures are designed to enhance Belgium's competitiveness while preserving revenue neutrality.

9. **Policy discussions focused on the importance of maintaining the reform momentum and not yielding to complacency.** Achieving the balanced budget goal will require efforts at all levels of government to make spending more efficient and safeguard revenues (Section A). A combination of policies and reforms could help raise productivity growth, including increasing investment in infrastructure and enhancing competition in services (Section B). To fully realize Belgium's employment potential, it will be critical to address the severe fragmentation of the labor market (Section C). To preserve financial stability, the authorities should address vulnerabilities in the mortgage market and carefully navigate the transition toward a European Banking Union (Section D).

[3] A comprehensive assessment of Belgium's financial sector took place in 2017 under the Financial Sector Assessment Program (FSAP).

[4] The NID aims to neutralize the CIT treatment of debt and equity by supplementing the deductibility of interest with a deduction that is the product of corporate equity and a notional interest rate.

Table 2. Belgium: Reform Agenda

	Tax policy
Previous reforms	• Previously agreed tax shift measures to take effect in 2018–20, including further reductions in employer social security contributions and reductions in personal income tax rates.
New measures	• Lower CIT rates, phased in over 2018–20, combined with measures to offset the revenue loss, including anti-tax avoidance measures and a modification of the NID. • New taxes on securities accounts and sugary drinks. • Various rate increases and base-broadening measures related to the taxation of investment income. • Tax breaks for investments and pension savings.
Staff assessment	Further reductions in the labor tax wedge under the tax shift are welcome but will lead to revenue losses that could be offset through measures to broaden the tax base. The reduction in the CIT rate and anti-tax avoidance measures are appropriate but a variety of distortions remain in the broader system of capital taxation.
	Labor market and social policies
Previous reforms	• The 2015 pension reform increased the statutory retirement age to 66 in 2025 and 67 in 2030. • Tighter eligibility for early retirement and stricter job search requirements for older unemployed people. • Revision of the 1996 law on employment and competitiveness requires social partners to include a safety margin and correct for past slippages when calculating the wage norm. • Suspension of the wage indexation mechanism from April 2015 to April 2016 (“index jump”). • Strengthening of incentives for work through the redefinition of “suitable jobs,” tighter eligibility for unemployment benefits, and a greater decline in unemployment benefits over time. • Reduction in the labor tax wedge through the tax shift (see above).
New measures	• Measures to introduce more flexibility in the labor market. • Further reductions in social contributions for certain workers. • Tax breaks for hiring young workers and for working a second job. • Strengthening of rules requiring the unemployed to accept job offers. • Various measures aimed at increasing the effective retirement age.
Staff assessment	Staff supports measures to further reduce the labor tax wedge and introduce more flexibility in the labor market. Continued efforts to integrate the youth, the low skilled, and non-EU immigrants would help unlock Belgium’s labor market potential. Changes to the pension system rightly focus on the retirement age rather than on the level of benefits.

A. Rebuilding Fiscal Buffers

10. Fiscal consolidation remains a priority. Prior to the crisis, Belgium had a solid track record of running primary surpluses and reducing public debt. Post-crisis fiscal adjustment, however, has been weak, causing debt to climb back above 100 percent of GDP. Real primary spending growth has been at the root of the problem, driven mainly by social spending and the public sector wage bill. Tax revenues as a share of GDP, meanwhile, remain high by European standards despite a downward trend since 2013 linked to the tax shift.

11. The strong fiscal performance in 2017 is encouraging, but further measures are needed to achieve a balanced budget in the medium term. Approximately a third of the decline in spending in 2017 (as a share of GDP) was due to windfall interest savings; future interest savings are expected to be more modest and are subject to considerable uncertainty. The spike in advanced payments boosted CIT revenues in 2017 but should not affect future CIT revenues, which are projected to decline modestly. Meeting the government's medium-term objective of structural balance is further complicated by the fact that the next phases of the tax shift, to take effect in 2018–20, will likely lead to revenue losses. In addition, the government will need to gradually reorient public expenditure from current to investment spending in order to deliver on its plans to increase public investment in the coming decade.[5] The package of reforms agreed last summer contained some new taxes but noticeably lacked expenditure reforms. In the absence of further measures, the structural deficit is projected to remain at around 1½ percent over the medium term.

12. The CIT reform will help boost investment and should be complemented with additional measures to safeguard revenues while reducing distortions in the tax system. The CIT reform appropriately lowers the high statutory rate while broadening the tax base to offset the revenue losses. However, a reduced rate for SMEs could create a disincentive for companies to grow, and the changes to the NID regime will reintroduce bias toward debt financing. The CIT reform should be complemented by measures that further broaden the tax base and address remaining distortions in the tax system. Environmental taxation could be strengthened and certain deductions and exemptions, including on VAT and company cars, could be eliminated. To create a more level playing field across business and investment activities, it would be useful to review other aspects of the tax system, including the taxation of interest, dividends, and capital gains; the targeting of profit tax deductions; the preferential tax treatment of rental income and real estate; and tax preferences on savings accounts.[6]

13. Staff reiterated the need for efficiency-oriented spending reforms, and for a gradual shift from current to investment spending. The high levels of public spending in Belgium have not necessarily translated into better services or social outcomes. Previous analytical work by staff

[5] The federal government has established a Strategic Investment Pact aimed at mobilizing public and private funds for investment. The pact calls for €60 billion in investment over the period 2017–30.

[6] See De Mooij et al., 2017, "Growth-Enhancing Corporate Tax Reform in Belgium," IMF Country Report 17/70.

suggests that there is significant scope to make spending more efficient.[7] Reducing the wage bill to the EU average (for example, by streamlining the civil service) would yield 2½ percent of GDP in savings.[8] Subsidies are 1½ percent of GDP higher than the EU average and 1½ percent of GDP higher than the average in France, Germany, and the Netherlands. Further savings could be achieved by containing growth in health care costs, better targeting social benefits to the most vulnerable, and improving administrative efficiency and coordination across levels of government. Achieving a significant reduction in current spending is all the more important as Belgium's growth prospects depend critically on making up for years of underinvestment in public infrastructure (Box 2 in Section B).

Authorities' Views

14. The authorities agreed that reducing spending was the key to achieving their medium-term objective of structural balance. They argued that many of the reforms already put in place will continue to pay dividends, including reforms to contain health care spending, encourage later retirement, and tighten requirements for the unemployed to accept job offers. They are working to improve the integration of workers with disabilities and better target social benefits. They emphasized that Belgium's federal structure, whereby all levels of government are on equal footing, makes coordination more complicated. They expect the CIT reform to be revenue neutral, and pointed out that the dynamic effects of the reform (i.e., the favorable effects on investment) could even lead to net revenue gains. They maintained that a reduced rate for SMEs made sense given the prominent role that SMEs play in Belgium's economy. They acknowledged that the next phases of the tax shift will require offsetting measures to safeguard revenues.

[7] See Hallaert, J.J., 2016, "Belgium—Making Public Expenditure More Efficient," IMF Country Report 16/78.

[8] Although public employment at the Entity I level (federal government and social security) has steadily declined since 2008, it has been rising at Entity II level (regions, communities, and local authorities).

Box 1. Corporate Income Tax Reform

The corporate income tax reform reduces the standard CIT rate from 33 percent to 29 percent in 2018, and to 25 percent in 2020, compared to an average CIT rate of 24 percent in the euro area in 2017. The 3 percent austerity surcharge (imposed since 1991) falls to 2 percent in 2018 and to zero in 2020. SMEs, which were previously subject to a progressive rate structure, henceforth benefit from a single reduced rate of 20 percent on the first €100,000 of their tax base. The CIT reform includes other advantages for companies, including (i) an increase in the dividend received deduction (ii) a temporary increase in the investment deduction for investments made by SMEs and independent workers; and (iii) the possibility for companies belonging to the same group to consolidate their tax results starting in 2020.

To compensate for the resulting revenue loss, the reform broadens the tax base through a series of measures. This includes important changes to the NID scheme. Whereas the NID previously applied to the entire equity stock, it will now apply only to incremental equity, defined on a 5-year moving average basis. In addition, a limit on the NID and other deductions is established, equal to €1 million plus 70 percent of the balance after the investment deduction is applied. The reform further broadens the tax base by introducing various measures against tax avoidance, such as interest deduction limitations, controlled foreign company (CFC) rules, and exit taxes. These measures are consistent with Belgium's obligation to comply with the EU's Anti-Tax Avoidance Directive (ATAD). Because the effects of the base-broadening measures will not be felt immediately, the reform includes some administrative measures—for example, increasing the penalty for insufficient advanced payments—designed to boost revenues in the interim and render the reform revenue-neutral in all years.

Staff assessment: The reduction in the headline CIT rate should help improve Belgium's competitiveness and attract foreign investment. However, the increased gap between the CIT rate and personal income tax rates, combined with the lack of capital gains taxes, could create incentives for individuals to register as a corporation, which can lead to organizational inefficiencies, revenue losses, and misallocation of capital. The narrowing of the NID, while serving as an important revenue compensating measure, reintroduces a degree of debt bias into the tax system by increasing the cost of equity capital, while interest deductions remain in place. Moreover, the CIT reform does not address inefficiencies related to preferential treatment of income from intellectual property.

Analysis by the National Bank of Belgium (NBB) finds the reform to be broadly revenue neutral, though with some degree of uncertainty. The revenue effects of narrowing the NID depend on the reaction of companies and on the evolution of the notional interest rate, which is tied to the rate on Belgian government bonds.

Estimated Budgetary Impact of CIT reform
(EUR millions)

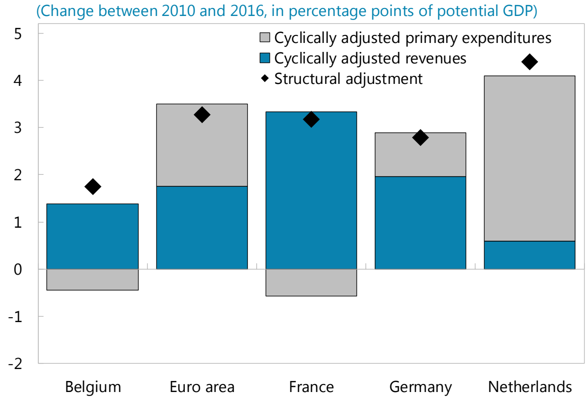
	2018	2019	2020	Steady state
Costs				
Reduction in rates	-1243	-1807	-3778	-4766
Other measures	-254	-326	-417	-705
Total	-1496	-2133	-4195	-5471
Compensating measures				
NID changes	477	834	1352	2239
Overall limit on deductions	316	456	517	521
ATAD measures	0	0	339	1210
Other measures	912	1151	2095	1625
Total	1704	2441	4303	5595
Estimated budgetary impact	208	308	108	124

Source: National Bank of Belgium.

Figure 2. Belgium: Fiscal Context

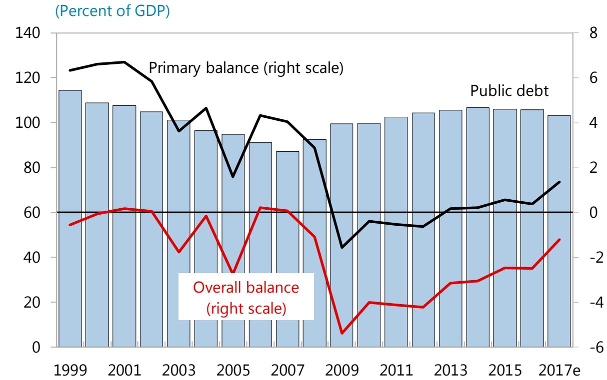
Prior to 2017, there had been relatively little post-crisis adjustment compared to peers.

Structural Fiscal Adjustment
(Change between 2010 and 2016, in percentage points of potential GDP)



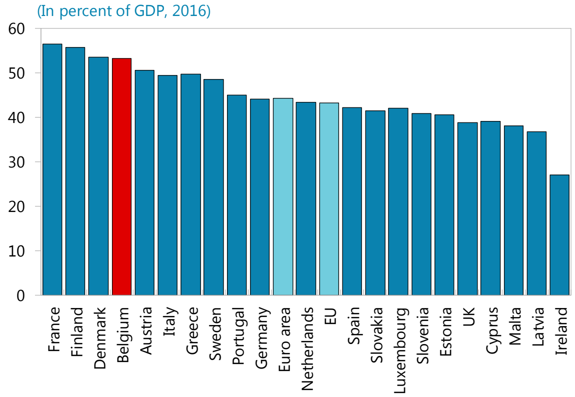
Fiscal consolidation accelerated in 2017, and public debt declined.

General Government Debt and Budget Balance
(Percent of GDP)



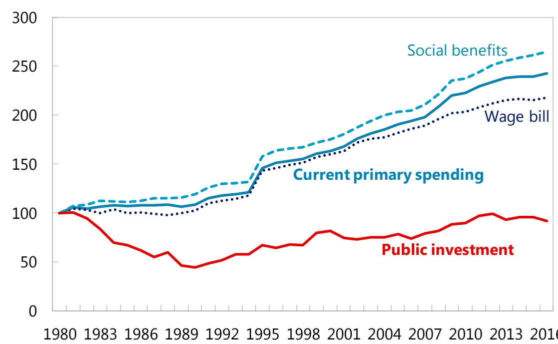
Government spending remains among the highest in Europe.

General Government Expenditure
(In percent of GDP, 2016)



Current spending has long outpaced public investment.

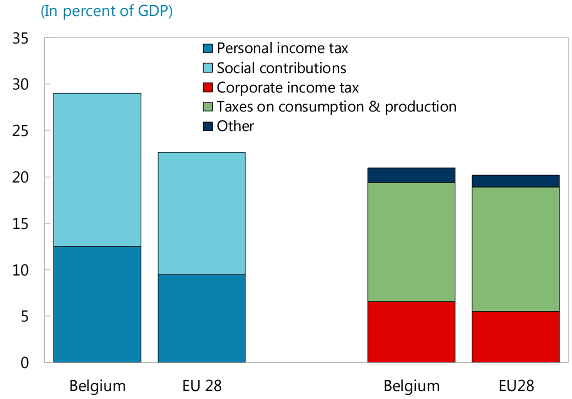
Real Public Current Spending and Investment
(Index, 1980=100)



Note: All variables adjusted by GDP deflator.

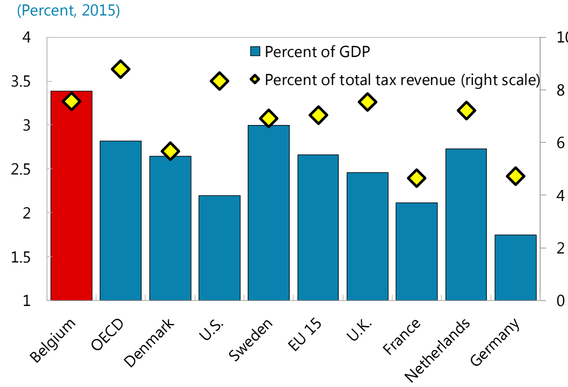
Taxes are relatively high...

Tax Revenue and Social Contribution, 2015
(In percent of GDP)



...including corporate taxation.

Taxes on Corporations
(Percent, 2015)

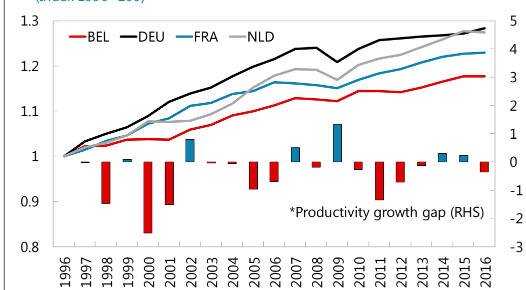


Sources: Haver Analytics, IMF World Economic Outlook, Eurostat, OECD, and IMF staff calculations.

B. Boosting Productivity

15. Productivity growth in Belgium has lagged peers. While many advanced economies have experienced a slowdown in productivity growth over the past two decades, the trend has been more pronounced in Belgium, with respect to both labor and total factor productivity growth. The literature has identified several common structural headwinds, including aging societies, slowing global trade, and a waning ICT boom.[9] In addition, continued deindustrialization of advanced economies has implied a reallocation of resources to sectors where productivity growth is generally slower and declining. Policy distortions, including regulations that limit competition in services, have also been identified as potential culprits.[10] Belgium faces many of these features common among advanced countries.

Evolution of Real GVA per Hour Worked
(Index 1996=100)



*Note: Difference between productivity growth in Belgium and the average of Germany, France, and the Netherlands.
Source: Eurostat.

16. Sectoral reallocation effects explain part of the productivity gap with neighboring countries. Productivity developments have been heterogeneous across economic sectors: while industry, construction, and finance are performing at or above the regional average in terms of value-added per hour worked, service subsectors with large employment shares—including trade, travel, accommodation, public administration, education, and science—have seen subdued productivity growth. Labor productivity growth in ICT services has been particularly poor compared to peer countries and might have negatively affected TFP in the rest of the economy. The adverse productivity trend is amplified by the growing employment share of sectors with low labor productivity growth. Staff has performed a "shift-share analysis" to assess how shifts in the relative economic weight of different sectors affect overall labor productivity growth. The comparison with neighboring countries indicates that these sectoral reallocation effects, including deindustrialization, explain about half of the cumulative productivity growth gap with peers since 1996.[11]

17. An aging workforce and slower human capital accumulation are additional constraints on productivity growth. Demographic changes and increased participation rates have resulted in high employment growth of older workers. The share of 55+ workers in Belgium has increased two-fold from 6.5 percent in 2000 to 15 percent in 2017. While increased participation by older workers is a positive development in general, it may have had an impact on labor productivity growth, with several studies linking workforce aging to declining labor productivity.[12] Possible explanations

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[9] See Adler et al., 2017, "Gone with the Headwinds: Global Productivity," Staff Discussion Note No. 17/04.

[10] See Dabla-Norris et al., 2015, "The New Normal: A Sector-level Perspective on Productivity Trends in Advanced Economies," Staff Discussion Note No. 15/3.

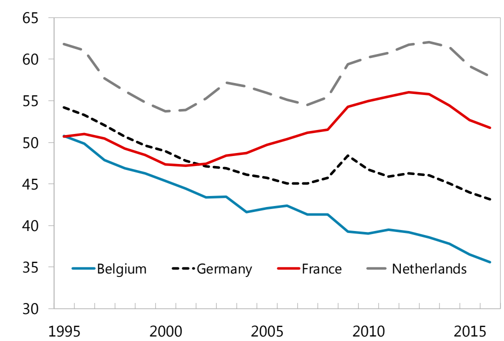
[11] See Shabunina, A., 2018, "Understanding Productivity Growth in Belgium: Sectoral and Firm-level Analysis," accompanying IMF Selected Issues Paper.

[12] Aiyar et al. (2016) estimated that a 1 percentage point increase in the share of 55+ workers corresponds to 0.4 percentage point reduction in annual TFP growth. See also Feyrer (2007) and Adler et al. (2017).

include age-related changes in physical capability, knowledge depreciation (which could in some cases outweigh positive experience accumulation effects), and insufficient propensity to upgrade skills and adopt innovation.

18. Underinvestment in public infrastructure and its deteriorating quality are likely to be significant factors constraining productivity growth in Belgium. Public investment as a share of GDP has declined by half since 1970. At 2.2 percent in 2016, it stood significantly below the EU average of 3.9 percent. In real terms, public investment is barely at its level in 1980, whereas current primary spending has more than doubled. The decline in the 1980s was mainly the result of fiscal consolidation efforts that targeted public investment rather than current expenditures. Because of low investment, the stock of general government fixed assets amounts to only 36 percent of GDP, well below peers.[13] Empirical studies show that improving infrastructure quality can have a significant positive impact on firms' productivity. Staff has modeled the impact of a budget-neutral shift from current to capital spending that brings Belgium's capital stock in line with its neighbors, demonstrating the significant positive effects on productivity growth and GDP (Box 2).

General Government Fixed Assets
(Percent of GDP)



Source: Eurostat.

Box 2. Simulating an Increase in Public Investment

Staff used the IMF's Global Integrated Monetary and Fiscal Model (GIMF) to simulate the effects of an increase in public investment in transport infrastructure.[1] GIMF is a large-scale dynamic stochastic general equilibrium (DSGE) model that considers the implications of policy changes for the demand and supply sides of the economy. It was calibrated using Belgian macroeconomic data.

The simulation assumes a gradual expenditure-neutral shift from current spending towards public investment (peaking at 2 percent of GDP after 5 years). This causes the public capital stock to increase gradually, from 36 percent of GDP initially to 51 percent of GDP by 2029, undoing the deterioration since 1995 and bringing it in line with the average public capital stock level in neighboring countries. The higher capital stock increases productivity and thereby lowers prices, leading to a gradual real exchange rate depreciation and increase in net exports. Higher productivity also creates a wealth effect that boosts private consumption.

Overall, the model predicts a cumulative GDP increase of around 6 percent in the long run. While this magnitude is broadly in line with similar simulations using DSGE models, it should be interpreted with caution in the Belgian case, given country-specific characteristics that were not modeled.[2]

[1] See Voigts, S., 2018, "Simulating an Increase in Public Investment in Belgium," accompanying IMF Selected Issues Paper.

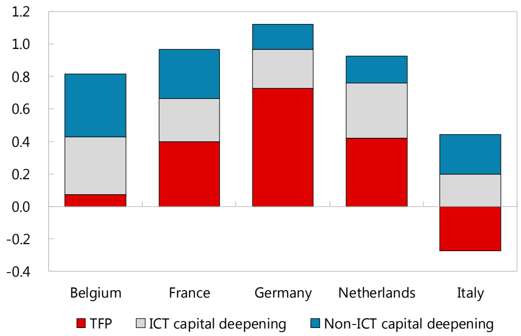
[2] While the model is comparatively detailed, it remains stylized and does not account for all relevant factors. For instance, it does not consider Belgium's (relatively high) import share of exports, which implies that the growth impact of public investment via export demand could be significantly less pronounced in practice than modeled.

[13] Under European System of National and Regional Accounts (ESA 2010) rules, the definition of general government excludes entities controlled by the government but considered "market producers." The amount of fixed assets held by these entities may differ across countries. Hence, the picture presented here may not reflect the evolution of fixed assets of the broader public sector.

Figure 3. Belgium: Productivity

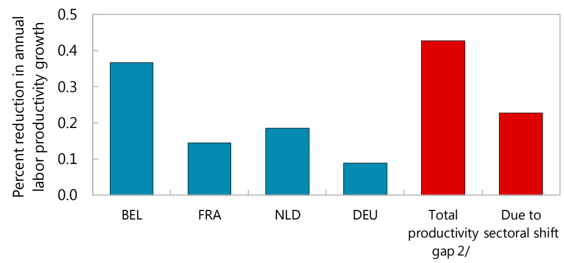
Productivity growth In Belgium has lagged some peers.

Labor Productivity Contributions
(Average annual growth, 2000 - 2016)



Sectoral shifts explain about half of the cumulative productivity growth gap according to staff analysis.

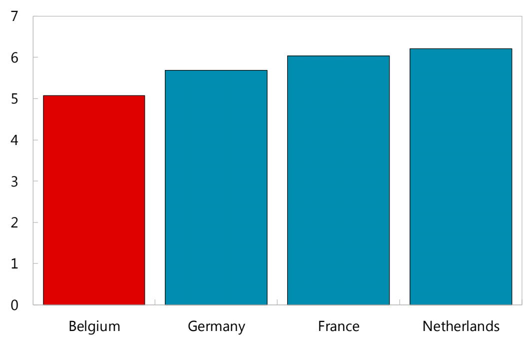
Productivity Growth Slowdown Due To Sectoral Shifts 1/
(Percent)



1/ Calculated by comparing actual productivity with a hypothetical level that assumes employment shares remain constant at their 1996 level.
2/ Difference between productivity growth in Belgium and the average of Germany, France, and the Netherlands.

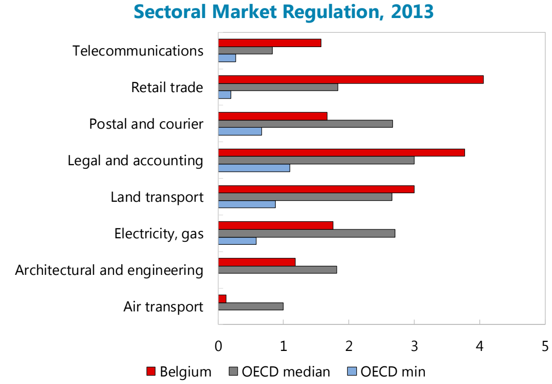
Low public investment and declining quality of infrastructure likely had a negative impact on productivity.

Quality of Infrastructure
(Scale from 1 (worst) to 7 (best))



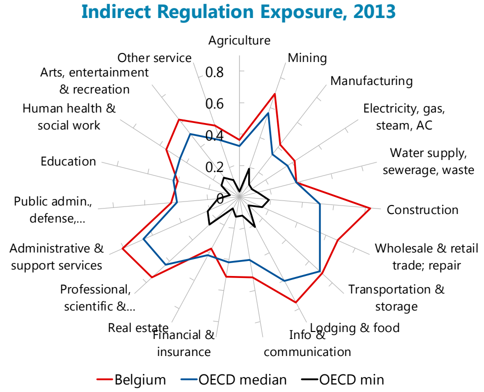
Regulatory hurdles in network and professional services are comparatively high.

Sectoral Market Regulation, 2013



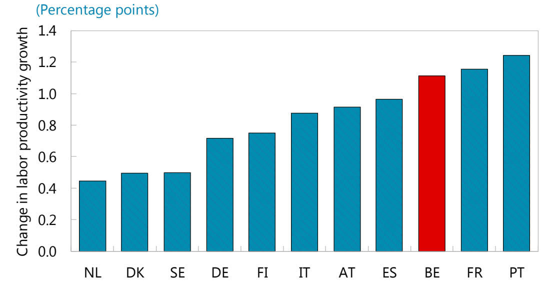
Indirect regulatory spillovers in Belgium are above OECD average.

Indirect Regulation Exposure, 2013



Staff's empirical analysis suggests that labor productivity gains from minimizing sectoral regulation could be high.

Annual Average Labor Productivity Growth Gains From Minimizing Sectoral Regulation*
(Percentage points)



*Staff estimates based on the counterfactual exercise assuming bringing sectoral regulation to the lowest level in the EU. Please see accompanying SIP "Understanding Belgium's productivity: firm-level analysis".

Sources: Eurostat, World Economic Forum, OECD, ORBIS and IMF staff calculations.

19. **Limited competition in service sectors appears to have had both direct and indirect effects on productivity**. While Belgium's overall product market regulation score is not worse than the OECD average, many service sectors, including telecommunications, retail, legal and accounting, and land transportation, face comparatively high barriers to entry and competition. Cross-country analysis by staff using firm-level data shows that high levels of sectoral regulation are associated

with lower productivity growth, as regulatory protection reduces firms' incentives to innovate and raise efficiency. While the direct effects on total productivity are limited by the small share of these sectors in the economy, large spillovers to all the sectors using inputs from the business services make the total drag on productivity significant. Staff econometric analysis indicates that reducing the degree of regulation to the best practices in the EU could raise annual TFP growth by 1 percentage point, largely due to reducing the adverse regulation spillover effect.[14]

20. These findings suggest that lifting Belgium's productivity growth requires a combination of reforms. Efforts should focus on: (i) increasing public investment in critical infrastructure, especially energy and transport, which is an important constraint on Belgium's growth potential; (ii) boosting competition in services by enhancing institutional capacity to foster competition and lowering regulatory barriers closer to the level of best practice observed in the EU; (iii) fostering innovation through the appropriate design of planned tax reforms, including by reforming the innovation income deduction;[15] (iv) strengthening lifelong learning, especially in ICT. Boosting productivity growth through such reforms could help improve external competitiveness and mitigate the impact of population aging on potential growth.

Authorities' Views

21. The authorities are concerned about slow productivity growth and agreed that upgrading infrastructure and strengthening competition would help. They observed that slow productivity growth is a common problem in advanced economies and pointed to the recently created National Productivity Council, which will focus on this issue. They agreed that some sectors (professional services, telecommunications, construction, retail) would benefit from more competition and said the legal and regulatory framework could also be improved. They highlighted recent reforms in the energy sector that have helped increase competition, as well as a new telecommunications law that facilitates switching carriers ("easy switch"). They drew attention to new tax incentives in the CIT reform aimed at boosting investment and R&D expenditures (e.g., a temporary increase in the investment deduction for SMEs and the self-employed, a broader exemption from withholding tax for researchers, tax incentives for growth financing, and the development of a tailor-made financial ecosystem for growth companies). They also noted plans to increase investment in mobility, energy transition, digitalization, education, health and security under the Strategic Investment Pact.

C. Addressing the Fragmentation of the Labor Market

22. The labor market is improving, reflecting the positive impact of reforms. Pension reforms in 2013 and 2015 have contributed to a significant increase in the participation rates of the older workers. Recent reforms to reduce taxes on labor and contain wage growth have also paid off, resulting in strong employment growth and declining unemployment rates, with older workers accounting for much of the employment increase.

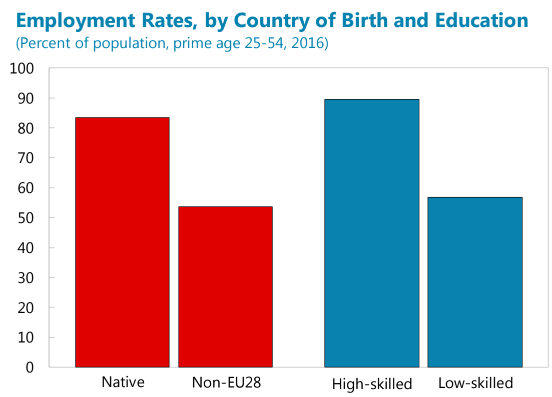
[14] See Shabunina, A., 2018.

[15] See De Mooij et al., 2017.

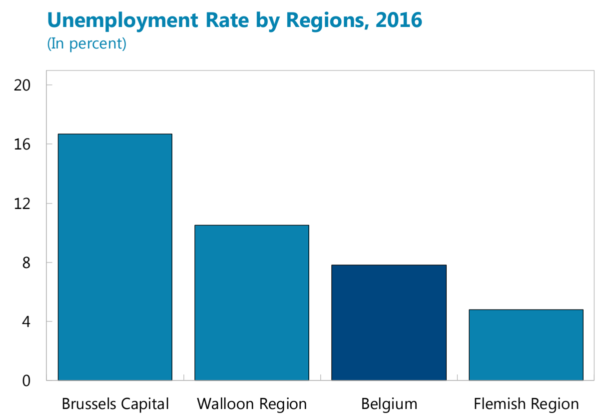
23. However, fragmentation of the labor market remains high. Youth unemployment, at 20 percent in 2016, remains above the EU average and could have long-lasting effects on young people's productivity and incomes, as well as their social prospects.[16] Large regional disparities in unemployment rates persist. Employment rates among the low-skilled and immigrants born outside the EU remain very low, and skills mismatches are growing (Figure 4). Staff analysis using micro census data to examine the relative likelihood of being employed conditional on belonging to a certain socioeconomic group confirms that there are significant disadvantages for the young, the low-skilled, and especially non-EU immigrants when controlling for other individual characteristics. The limited progress in integrating these vulnerable groups into the labor market is not only a social and fiscal issue but also an important constraint on potential growth in Belgium.

Figure 4. Labor Market Fragmentation

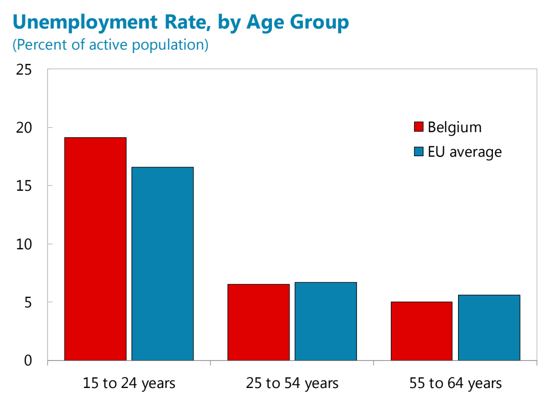
Non-EU born migrants and low-skilled workers have very low employment rates.



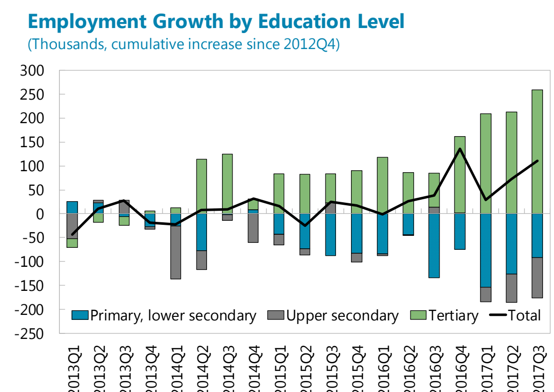
There are significant regional differences in unemployment rates.



Youth unemployment is high.



Employment growth has been driven by high-skilled workers.



Source: Eurostat.

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16 See Chen et al., 2018, "Inequality and Poverty Across Generations in the European Union," Staff Discussion Note No. 18/01.

24. Recent labor market measures will help, though more could be done to unlock Belgium's large untapped labor market potential. The 2017 summer agreement included some new measures to reduce the tax wedge for younger workers and increase labor market flexibility (Table 2). To better integrate vulnerable groups into the labor market, it will be crucial to address educational gaps including in languages, improve the supply of and demand incentives for vocational training, develop apprenticeship programs, and reduce barriers to geographical mobility.[17] The wage setting process, guided by the revised 1996 law, has recently supported wage moderation. To ensure that it supports growth and employment, it should reflect not only comparator country wages but also productivity developments as well as regional and sectoral labor market conditions. The new National Productivity Council could play a useful role in informing social partners in this respect. Moreover, ensuring an adequate degree of flexibility for labor agreements at the enterprise level would support employment and competitiveness.

Authorities' Views

25. The authorities highlighted recent progress in addressing labor market challenges while acknowledging that more efforts are needed. Past reforms to moderate wage growth and reduce the labor tax wedge have contributed to the current job-rich recovery. The authorities also pointed to several measures in the 2017 summer package that could help integrate vulnerable groups into the labor market, including shorter notice periods during the first six months of employment, "flexi-jobs" in retail industries, more working-hour flexibility in the e-commerce industry, tax advantages for employers hiring young workers, and "mystery calls" to combat discrimination in the hiring process. They acknowledged that increasing productivity without reversing gains in the integration of low-skilled workers was a key challenge. Another challenge is to ensure that older workers who extend their careers receive the training necessary to keep their skills up to date.

D. Preserving Financial Stability

26. The soundness of the Belgian financial sector has improved significantly since the crisis. Capital buffers have increased, with Tier I capital ratio rising by about 300 basis points since 2009 to 16.2 percent. Non-performing loans have fallen to 2.4 percent of gross loans. Profitability has recovered, and banks' migration to the new Basel III standards is well underway. The banking sector is now more focused on traditional financial activities and markets, while the insurance sector has restructured itself in response to a protracted period of sluggish growth and low interest rates. Stress tests on banks and insurance companies conducted in the context of the 2017 FSAP confirm that they can absorb credit, sovereign, and market losses in the event of a severe deterioration in macro financial conditions.[18]

27. Nevertheless, cyclical vulnerabilities are rising. Whereas household debt in the euro area has been falling since the crisis, household debt in Belgium continues to increase and currently stands at 60 percent of GDP, with mortgage debt accounting for 90 percent of the total. Although the aggregate financial position of households remains strong thanks to a very high level of assets,

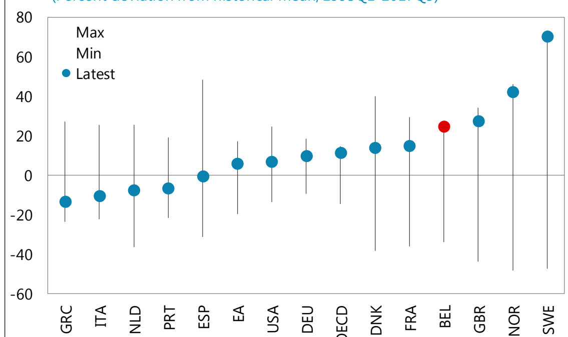
[17] See staff report for the 2017 Article IV Consultation, IMF Country Report No. 17/69.

[18] See Belgium Financial System Stability Assessment, March 2018.

households have become net borrowers (on a flow basis) for the first time in nearly a decade. Consolidated non-financial corporate (NFC) debt has increased to 129 percent of GDP (as of June 2017), well above the euro area average of 79 percent. However, nearly half of this amount consists of intragroup debt with small residual exposures for the Belgian financial system. The increases in household and corporate leverage have coincided with a steady increase in housing and equity prices in the context of low interest rates and low risk premia. Price-to-earnings (P/E) ratios exceed P/E ratios in the euro area and the United States (as of September 2017).[19]

28. The housing market appears to be only moderately overvalued, but pockets of vulnerability exist. Having grown rapidly in the 2000s, residential housing prices did not experience a sharp decline during the crisis, and have since risen by about 20 percent in nominal terms. The price-to-rent and price-to-income ratios stand well above their historical averages. More sophisticated measures, however, indicate only a moderate overvaluation.[20] Since 2015 there has been a reversal in the tightening of mortgage lending standards, as evidenced by a growing share of loans with high loan-to-value (LTV) and/or high debt service-to-income (DSI) ratios.[21] Risks are mitigated to some extent by the fact that Belgian households generally hold considerable financial assets. Nevertheless, nearly a third of outstanding mortgage debt is held by households whose liquid financial assets cover less than six months of debt service.[22]

Price-to-Rent Ratio
(Percent deviation from historical mean; 1995Q1-2017Q3)



Source: OECD and IMF staff calculations.

29. It will be important to stand ready to tighten macroprudential conditions further if balance sheet risks were to grow significantly. To address growing risks in the housing market, the NBB in 2014 introduced a 5 percent risk weight add-on for banks using internal ratings models to determine their minimum regulatory capital requirements for mortgage loans. In 2017, the NBB proposed a tightening of macroprudential policies through a targeted increase in capital charges linked to the riskiness of exposures, proxied by LTV ratios. However, as this proposal was not accepted by the government, the NBB subsequently proposed a new macroprudential measure requiring banks with riskier mortgage portfolios to hold more capital. This measure should be

[19] Excluding one large company, however, P/E ratios in Belgium are in line those in the euro area.

[20] The NBB estimates that housing prices are overvalued by 6 percent, based on a regression that takes into account household disposable income, mortgage rates, the number of households, and other determinants of housing prices. The European Central Bank uses four different valuation methods, with results ranging from an undervaluation of 2 percent to an overvaluation of 28 percent (as of 2016Q4). Various private sector models point to an overvaluation of less than 10 percent.

[21] One tenth of outstanding mortgages have an LTV ratio greater than 90 percent. Nearly 13 percent have a DSI ratio greater than 50 percent.

[22] See Du Caju, P., 2017, "Pockets of Risk in the Belgian Mortgage Market: Evidence from the Household Finance and Consumption Survey (HFCS)," National Bank of Belgium, Working Paper No. 332.

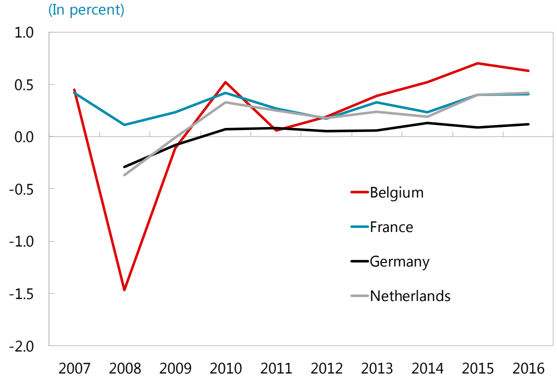
enacted promptly. Looking ahead, it will be important to strengthen the NBB's ability to deploy cyclical macroprudential measures in the financial sector in a timely manner.

30. Belgium's banks need to continue adapting their business models to an evolving economic and technological environment. Although profitability has recovered since the crisis, it has more recently come under pressure from persistently low interest rates. Should rates remain low, profitability could suffer further, particularly as mortgages continue to be refinanced. Thus, staff stressed the need for banks to further reduce operating costs and diversify revenue sources to boost profitability. More broadly, the financial sector will need to adapt to the growing digitalization of finance and step up protections against cyber security risks. Banks were also encouraged to carefully manage their interest rate risk, particularly against an abrupt increase in market rates that could put downward pressure on their interest margins if their liabilities were to reprice faster than their assets.

Figure 5. Belgium: Financial Sector Developments

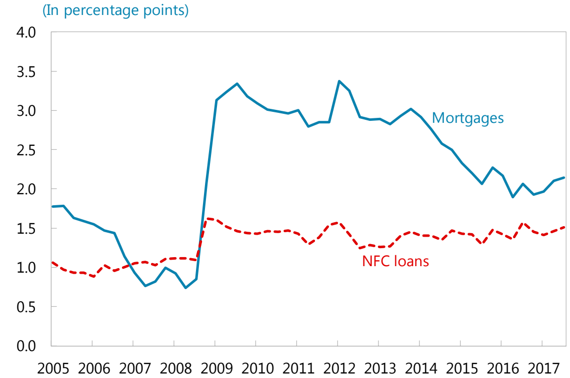
Belgian banks have restored profitability…

Return on Assets
(In percent)



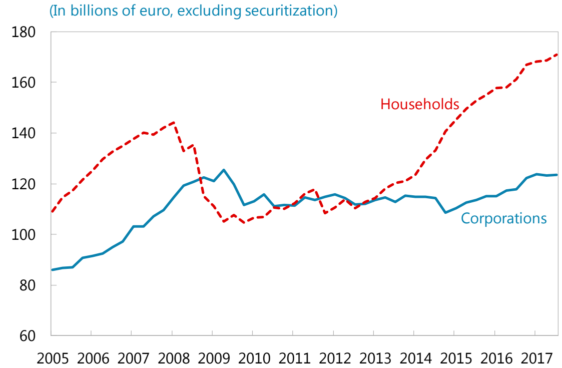
…but profitability could suffer as margins on mortgage loans are squeezed by low interest rates and refinancing.

MFI Lending Margins
(In percentage points)



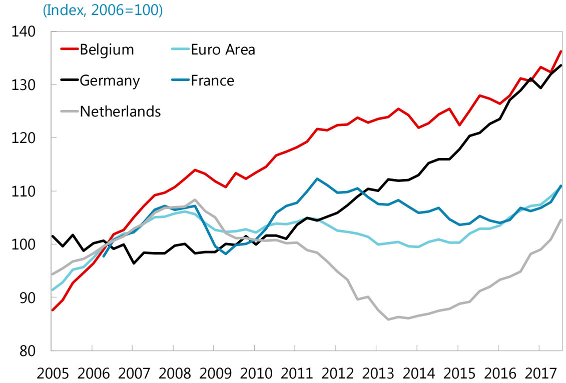
Credit growth has been driven by residential mortgage lending…

Loans to Households and Corporations
(In billions of euro, excluding securitization)



…contributing to higher house prices.

International Comparison of House Price Evolutions
(Index, 2006=100)



Source: Haver Analytics.

31. Carefully navigating the transition to a European Banking Union poses important institutional challenges. Completion of Banking Union is a central objective for Europe, with significant potential benefits. Progress is being made, especially with respect to the resolution framework. Close cooperation between the NBB, the ECB, and the Single Resolution Board is necessary to address challenges arising from the key role subsidiaries of euro area banks play in Belgium's banking sector. These systemically important euro area subsidiaries should continue to be closely supervised under the Single Supervisory Mechanism, and they should maintain sufficient capital and loss absorbing capacity until the completion of the Banking Union.

Authorities' Views

32. The Belgian authorities broadly shared staff's assessment. They agreed that cyclical vulnerabilities were rising while stressing that risks are currently not elevated. Risks associated with increasing household leverage were to some extent mitigated by the high level of assets combined with a relatively low share of variable rate loans, while the level of NFC debt was not too high when adjusted for the high share of intragroup lending. The authorities do not believe the residential housing market is strongly overvalued, but agreed that systemic risk is building and that some segments pose heightened risks. The NBB is addressing these risks through macroprudential measures. They confirmed their determination to work toward a European Banking Union and help ensure that in the transition period the systemically important subsidiaries of euro area banks hold sufficient loss absorbing capacity.

STAFF APPRAISAL

33. The strengthening recovery is an opportunity to boost the resilience and long-term growth potential of the Belgium economy. The government has made important progress in delivering on its reform agenda. With the economic recovery strengthening, the government should maintain the reform momentum and lay the foundation for stronger, more inclusive growth in the future. Fiscal consolidation remains a priority, and further labor and product market reforms are needed to increase productivity growth, raise potential output, and integrate vulnerable groups into the labor market. Such reforms will not happen overnight, but it is important not to yield to complacency.

34. Given the high level of public debt, Belgium should continue pursuing gradual fiscal consolidation based on deeper reforms to make public spending more efficient. The sharp decline in the budget deficit in 2017 is encouraging and at least partly reflected the payoff from previous reforms. Nevertheless, more efforts will be needed to achieve the government's objective of structural balance in the medium term and create fiscal space for more public investment. Further adjustment should be driven by reforms to make spending more efficient, in particular by reducing subsidies, making the division of labor between levels of government more efficient, accelerating ongoing reductions in public employment, and better targeting social benefits. Coordination and participation across all levels of government will be essential.

35. The welcome reform of corporate income and labor taxation should be complemented by additional measures to safeguard revenues and promote economic efficiency. The reform of the corporate income tax system appropriately lowers the high statutory rate and broadens the tax base, including through anti-tax avoidance measures. Additional tax reform should focus on addressing distortions in the current system while safeguarding revenues, particularly given the expected revenue losses from the next phases of the tax shift. There is scope to further broaden the tax base by eliminating certain deductions and exemptions. Restoring balance between different forms of business income and limiting tax arbitrage would make the system more efficient.

36. Raising the low rate of productivity growth would help improve external competitiveness and mitigate the impact of population aging on potential growth. While the decline in productivity growth partly reflects deindustrialization and sectoral shifts toward services common to many advanced countries, Belgium has lagged its peers in part due to a long period of underinvestment and limitations to competition in some service sectors. It will thus be important to step up efforts to upgrade infrastructure, particularly transport and energy, coordinated among all levels of government. There is also scope to enhance competition in services by lowering regulatory barriers and to foster innovation through tax reforms and support for education and training. Faster productivity growth could help improve Belgium's external position, which is moderately weaker than implied by medium-term fundamentals.

37. To fully realize Belgium's employment potential, it is critical to address the fragmentation of the labor market. Older workers account for much of recent employment gains, whereas less progress has been made integrating immigrants born outside the EU, the young, and the low-skilled. Moreover, significant regional disparities persist. Further reforms are needed to address educational gaps, improve the supply of and demand incentives for training, and reduce barriers to geographical mobility. The wage setting process, guided by the revised 1996 law, should not only reflect comparator country wages but also productivity developments as well as local and sectoral labor market conditions.

38. The resilience of the financial sector has improved considerably since the crisis, but cyclical vulnerabilities are rising and new challenges are emerging. Household and corporate leverage is increasing, partly reflecting the low interest environment. It will be important to stand ready to tighten macroprudential conditions further if balance sheet risks were to grow significantly, which could be facilitated by enhancing the NBB's ability to deploy macroprudential measures in a timely manner. The transition to a full European Banking Union needs to be carefully navigated, including by continued close supervision of systemically important subsidiaries of euro area banks operating in Belgium. Banks should further reduce operating costs and diversify revenue sources to adapt to a changing economic, technological, and regulatory environment.

39. It is proposed that the next Article IV consultation take place on the standard 12-month cycle.

Table 3. Belgium: Selected Economic Indicators, 2014–23

				Est.		Projections				
	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
				(Percent change, unless otherwise indicated)						
Real economy										
Real GDP	1.4	1.4	1.5	1.7	1.9	1.7	1.5	1.5	1.5	1.5
Domestic demand	2.2	1.4	2.1	1.4	1.8	1.7	1.5	1.5	1.5	1.5
Private consumption	0.6	0.9	1.7	1.1	1.4	1.6	1.6	1.6	1.6	1.6
Public consumption	0.7	0.5	0.5	0.7	0.7	0.6	0.6	0.7	0.6	0.6
Gross fixed investment	6.0	2.7	3.6	1.1	3.7	3.2	2.1	2.1	2.2	2.2
Stockbuilding[1]	0.3	0.2	0.2	0.4	0.0	0.0	0.0	0.0	0.0	0.0
Foreign balance[1]	-0.6	0.0	-0.6	0.3	0.1	0.0	0.0	0.0	0.0	0.0
Exports, goods and services	5.2	3.3	7.5	4.5	4.7	4.0	3.8	3.4	2.9	3.1
Imports, goods and services	6.2	3.3	8.4	4.3	4.6	4.1	3.9	3.4	2.9	3.1
Household saving ratio	12.4	11.9	11.2	11.6	12.3	12.3	12.5	12.5	12.5	12.5
Potential output growth	1.1	1.2	1.2	1.4	1.5	1.5	1.5	1.5	1.6	1.5
Potential output growth per working age person	1.0	1.0	1.1	1.1	1.4	1.5	1.5	1.5	1.5	1.5
Output gap (in percent)	-1.0	-0.8	-0.6	-0.3	0.1	0.3	0.2	0.2	0.1	0.1
Employment										
Unemployment rate (in percent)	8.6	8.5	7.9	7.3	7.0	6.8	6.7	6.7	6.6	6.6
Employment growth	0.4	0.9	1.2	1.2	1.1	0.9	0.7	0.6	0.6	0.6
Prices										
Consumer prices	0.5	0.6	1.8	2.2	1.6	1.8	1.8	1.9	2.0	2.0
GDP deflator	0.7	1.1	1.6	1.8	1.6	1.7	1.6	1.6	1.6	1.7
				(Percent of GDP; unless otherwise indicated)						
Public finance										
Revenue	52.1	51.3	50.7	51.1	50.4	50.1	49.9	49.9	49.9	49.9
Expenditure	55.2	53.8	53.2	52.3	51.7	51.4	51.2	51.1	51.2	51.1
General government balance	-3.1	-2.5	-2.5	-1.2	-1.3	-1.3	-1.3	-1.2	-1.3	-1.3
Structural balance	-2.9	-2.2	-2.2	-1.1	-1.4	-1.5	-1.4	-1.3	-1.3	-1.3
Structural primary balance	0.4	0.8	0.7	1.5	0.9	0.7	0.7	0.7	0.6	0.5
Primary balance	0.2	0.6	0.4	1.4	1.0	0.8	0.8	0.7	0.7	0.6
General government debt	106.8	106.0	105.7	103.3	101.1	99.1	97.4	95.7	94.1	93.0
Balance of payments										
Goods and services balance	0.0	1.7	1.3	1.0	1.1	1.0	1.1	1.2	1.0	1.1
Current account	-0.9	-0.1	0.1	0.1	0.3	0.2	0.5	0.6	0.4	0.5
Exchange rates										
Euro per U.S. dollar, period average 2/	0.8	0.9	0.9	0.8	...	...	...	...	...	...
NEER, ULC-styled (2005=100) 2/	102.1	97.9	98.9	101.3	...	...	...	...	...	...
REER, ULC-based (2005=100) 2/	104.0	98.3	98.5	105.0	...	...	...	...	...	...
Memorandum items										
Gross national savings (in percent of GDP)	22.5	23.4	24.0	23.9	24.5	24.8	25.1	25.3	25.4	25.6
Gross national investment (in percent of GDP)	23.3	23.6	23.9	23.8	24.1	24.5	24.6	24.8	25.0	25.1
Nominal GDP (in billions of euros)	400.3	410.4	423.0	438.1	453.5	468.8	483.4	498.6	514.3	531.0
Population (in millions)	11.2	11.2	11.3	11.4	11.4	11.5	11.5	11.6	11.7	11.7

Sources: Haver Analytics, Belgian authorities, and IMF staff projections.

[1] Contribution to GDP growth.

[2] As of December 2017.

Table 4. Belgium: Balance of Payments, 2014–23

				Est.	Projections					
	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
					(In percent of GDP)					
Balance on current account	-0.9	-0.1	0.1	0.1	0.3	0.2	0.5	0.6	0.4	0.5
Balance on goods and services	0.0	1.7	1.3	1.0	1.1	1.0	1.1	1.2	1.0	1.1
Balance of trade (f.o.b., c.i.f.)	118.2	111.0	117.1	121.1	124.2	126.2	127.5	128.1	127.8	127.0
Exports of goods and services	82.0	80.4	82.9	85.5	87.8	89.1	90.1	90.6	90.3	89.8
Exports of goods	58.4	55.7	58.7	60.5	62.1	63.1	63.8	64.1	63.9	63.6
Exports of services	23.5	24.7	24.2	25.0	25.6	26.0	26.3	26.5	26.4	26.2
Imports of goods and services	-81.9	-78.8	-81.5	-84.5	-86.6	-88.2	-89.0	-89.4	-89.2	-88.7
Imports of goods (f.o.b.)	-59.8	-55.3	-58.4	-60.5	-62.0	-63.1	-63.7	-64.0	-63.9	-63.5
Imports of services	-22.2	-23.4	-23.1	-24.0	-24.6	-25.0	-25.3	-25.4	-25.3	-25.2
Income, net	0.7	-0.2	0.6	0.8	0.9	1.0	1.1	1.2	1.2	1.2
Current transfers, net	-1.6	-1.6	-1.9	-1.7	-1.7	-1.8	-1.8	-1.8	-1.8	-1.9
Balance on capital account	-0.2	0.0	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Balance on financial account	-0.8	0.4	0.0	0.2	0.5	0.4	0.6	0.7	0.5	0.6
Direct investment, net	1.6	3.5	-1.7	-1.5	-1.3	-1.1	-0.9	-0.7	-0.5	-0.2
Portfolio investment, net	-3.4	-4.4	1.3	1.0	0.9	0.4	0.1	-0.1	-0.8	-1.1
Financial derivatives, net	0.8	-0.7	-0.1	-0.1	-0.2	-0.1	-0.1	-0.2	-0.1	-0.1
Other investment, net	0.4	2.3	0.8	1.0	1.2	1.4	1.6	1.8	2.0	2.2
Reserve assets	-0.3	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2
Errors and omissions, net	0.3	0.6	-0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Sources: Haver Analytics, Belgian authorities, and IMF staff projections.

Table 5. Belgium: General Government Statement of Operations, 2014–23

				Est.	Projections					
	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
	(In percent of GDP)									
Revenue	52.1	51.3	50.7	51.1	50.4	50.1	49.9	49.9	49.9	49.9
Taxes	30.8	30.3	30.1	30.5	30.1	29.7	29.8	29.8	29.8	29.8
Personal income tax	13.3	13.0	12.5	12.3	12.1	11.8	11.9	11.9	11.9	11.9
Corporate income tax	3.2	3.4	3.5	3.9	3.7	3.7	3.6	3.6	3.6	3.6
Taxes on property	2.2	2.1	2.0	2.1	2.1	2.1	2.1	2.1	2.1	2.1
VAT	6.9	6.7	6.5	6.5	6.5	6.5	6.5	6.5	6.5	6.5
Excise	2.1	2.1	2.2	2.3	2.3	2.3	2.3	2.3	2.3	2.3
Other taxes	3.1	3.0	3.3	3.3	3.3	3.3	3.3	3.3	3.3	3.3
Social contributions	16.7	16.6	15.9	15.8	15.6	15.6	15.4	15.4	15.4	15.4
Actual social contributions	14.3	14.3	13.7	13.6	13.4	13.3	13.1	13.1	13.1	13.1
Imputed social contributions	2.4	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3	2.3
Other revenue (incl. grants)	4.7	4.5	4.7	4.7	4.7	4.7	4.7	4.7	4.7	4.7
Expenditure	55.2	53.8	53.2	52.2	51.7	51.4	51.1	51.1	51.2	51.2
Expense	51.0	50.2	49.9	48.9	48.4	48.1	47.8	47.8	47.8	47.8
Compensation of employees	12.7	12.5	12.4	12.3	12.1	12.0	11.9	11.9	11.9	11.9
Use of goods and services	4.3	4.1	4.0	4.0	3.9	3.9	3.9	3.9	3.9	3.9
Interest	3.3	3.0	2.9	2.6	2.3	2.2	2.1	2.0	2.0	1.8
Subsidies	3.4	3.4	3.2	3.4	3.3	3.2	3.2	3.1	3.1	3.1
Grants	1.2	1.2	1.3	1.0	1.2	1.2	1.2	1.2	1.2	1.2
Social benefits	25.3	25.2	25.2	24.9	24.9	24.8	24.8	25.0	25.0	25.2
Other expense	0.9	0.8	0.9	0.8	0.8	0.8	0.8	0.8	0.8	0.8
Net acquisition of nonfinancial assets	4.2	3.6	3.3	3.3	3.3	3.3	3.3	3.3	3.3	3.3
Gross operating balance	1.1	1.1	0.8	2.2	2.0	2.0	2.1	2.1	2.0	2.1
Net lending/borrowing	-3.1	-2.5	-2.5	-1.1	-1.3	-1.3	-1.3	-1.3	-1.3	-1.3
Net financial transactions	-3.1	-2.5	...	...	...	...	...	...	...	...
Net acquisition of financial assets	1.1	1.7	...	...	...	...	...	...	...	...
Currency and deposits	-0.1	0.0	...	...	...	...	...	...	...	...
Securities other than shares	-0.6	0.0	...	...	...	...	...	...	...	...
Loans	1.2	0.9	...	...	...	...	...	...	...	...
Shares and other equity	0.2	-0.8	...	...	...	...	...	...	...	...
Other financial assets	0.4	1.6	...	...	...	...	...	...	...	...
Net incurrence of liabilities	4.0	4.2	...	...	...	...	...	...	...	...
Currency and deposits	0.0	0.0	...	...	...	...	...	...	...	...
Securities other than shares	2.3	2.7	...	...	...	...	...	...	...	...
Loans	1.9	0.4	...	...	...	...	...	...	...	...
Other liabilities	-0.2	1.2	...	...	...	...	...	...	...	...
Memorandum items										
Primary balance	0.2	0.6	0.4	1.5	1.0	0.8	0.8	0.7	0.7	0.6
Structural fiscal adjustment	0.2	0.7	0.0	1.2	-0.4	-0.1	0.1	0.0	0.0	0.0
Structural fiscal primary adjustment	0.2	0.5	-0.1	0.9	-0.6	-0.2	0.0	0.0	0.0	-0.1
Gross government debt	106.8	106.0	105.7	103.2	101.0	99.1	97.4	95.6	94.0	93.0
Real growth of primary expenditure[1]	0.2	-0.9	0.6	0.3	1.5	1.2	1.2	1.6	1.6	1.7

Sources: Haver Analytics, Belgian authorities, and IMF staff projections.
[1] Excludes the 2012 Dexia recapitalization.

Table 6. Belgium: General Government Consolidated Balance Sheet, 2009–16

	2009	2010	2011	2012	2013	2014	2015	2016
				(In percent of GDP)				
Net worth and its changes	...	...	...	...	...	...	...	...
Nonfinancial assets	...	...	...	...	...	...	...	...
Net financial worth	-82.9	-81.6	-83.4	-92.1	-90.3	-100.4	-97.9	-96.5
Financial assets	26.6	26.1	27.0	28.3	28.0	29.5	29.0	31.2
Currency and deposits	4.6	4.8	4.9	4.6	4.5	4.3	4.3	4.4
Securities other than shares	0.8	0.6	0.5	0.5	0.4	0.3	0.3	0.3
Loans	5.9	5.9	6.4	7.6	8.1	8.4	8.3	8.6
Shares and other equity	10.5	10.0	10.1	10.6	10.0	11.3	10.9	12.3
Insurance technical reserves	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Financial derivatives	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts receivable	4.9	4.8	5.0	5.0	5.0	5.2	5.3	5.5
Liabilities	109.5	107.8	110.4	120.4	118.3	129.9	126.9	127.6
Special Drawing Rights	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Currency and deposits	0.4	0.4	0.4	0.4	0.4	0.3	0.3	0.3
Securities other than shares	90.6	88.5	89.7	98.7	96.0	105.5	103.1	105.0
Loans	14.5	15.1	16.5	17.3	18.2	20.4	19.6	18.8
Shares and other equity	0.0	0.0	0.0	0.0	0.0	0.1	0.2	0.0
Insurance technical reserves	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.0
Financial derivatives	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other accounts payable	3.9	3.6	3.6	3.8	3.5	3.4	3.5	3.4

Sources: Haver Analytics and IMF staff calculations.

Table 7. Belgium: Financial Soundness Indicators for the Banking Sector, 2009–16[1]

	2009	2010	2011	2012	2013	2014	2015	2016
Earnings and profitability								
Return on assets	-0.1	0.5	0.0	0.1	0.3	0.5	0.6	0.6
Return on equity	-2.7	10.7	0.7	3.0	5.9	7.7	10.1	9.1
Net interest income to total income	79.1	68.3	71.2	71.6	62.6	70.2	67.7	66.0
Interest margin	0.8	1.2	1.2	1.3	1.2	1.6	1.8	1.8
Average yield on assets	2.8	2.8	2.9	2.9	2.6	2.7	2.6	2.6
Average cost of funding	2.0	1.6	1.7	1.7	1.4	1.1	0.8	0.6
Noninterest income to gross income	20.9	31.7	28.8	28.4	37.4	29.8	32.3	34.0
Of which: Net fee and commission income	30.1	25.6	26.8	28.3	27.7	25.8	26.7	25.1
(Un)realized capital gains booked in P&L	-14.5	-0.2	-3.9	0.2	6.0	-0.3	5.3	6.7
Cost/income ratio	77.7	66.0	67.3	73.4	62.4	61.2	58.6	58.4
Structure assets								
Total assets (in percent of GDP)	349.2	323.2	310.2	278.7	251.0	249.0	236.5	266.1
Of which (in percent of total assets):								
Loans to credit institutions	13.1	17.0	15.2	12.4	12.3	9.1	8.5	7.5
Debt securities	22.3	20.1	18.5	18.4	18.9	19.6	18.0	16.4
Equity instruments	0.8	0.5	0.4	0.6	0.4	0.6	0.7	0.4
Derivatives	11.3	11.6	14.6	11.5	6.8	8.4	6.4	5.8
Loans to customers	45.0	44.0	44.4	48.1	53.9	54.1	56.4	55.4
Of which: Belgian residents (in percent of loans)	59.0	64.0	69.7	72.0	69.4	69.2	69.2	71.0
Other EMU residents (in percent of loans)	19.0	19.0	16.9	15.0	15.7	16.2	16.1	15.1
Rest of the world (in percent of loans)	22.0	17.0	13.4	13.0	14.9	14.5	14.7	13.9
Mortgage loans (in billions euros)[2]	158.0	178.5	183.9	188.3	190.8	202.4	216.1	229.7
Consumer loans (in billions euros)[2]	17.0	23.7	23.2	24.0	26.9	17.2	19.7	24.8
Term loans (in percent of loans)	44.0	42.3	40.0	39.3	40.8	n.a	n.a	n.a.
Reverse repo operations (in percent of loans)	7.3	7.3	4.2	3.3	3.1	2.3	2.5	2.8
Funding and liquidity (in percent of total assets)								
Debts to credit institutions	14.1	15.4	11.2	11.0	10.7	9.1	8.5	10.3
Bank bonds and other debt securities[3]	12.6	10.9	8.8	10.6	10.1	9.3	9.1	9.3
Customer deposits	46.8	46.0	46.5	49.3	54.7	58.5	61.0	58.4
Of which: Sight deposits[4]	13.2	13.7	12.6	15.1	18.1	24.2	28.4	26.4
Saving deposits[5]	13.7	16.2	16.0	18.9	21.0	19.9	20.8	25.6
Term deposits[4]	8.9	8.5	9.6	9.2	9.6	8.9	8.1	6.2
Retail deposits[5]	23.8	26.1	26.5	30.6	34.8	33.5	35.1	35.6
Repo's	7.1	5.0	5.2	2.3	2.7	2.3	1.7	0.2
Liquid assets[6]	31.5	32.5	34.3	36.4	36.8	32.8	32.2	32.5
Asset quality								
Sectoral distribution of loans (in percent of total assets)								
Credit institutions	13.1	17.0	15.2	12.4	12.3	9.1	8.5	6.1
Corporate (until 2013) /Non financial corporations (as of 2014)	20.5	17.2	16.4	16.3	18.5	20.6	22.0	21.4
Retail (until 2013) / Households (as of 2014)	19.9	22.1	22.9	26.3	29.4	25.5	27.4	27.5
Central governments (until 2013)/ General government (as of 2014)	1.2	1.0	0.8	0.8	1.0	4.4	4.3	4.1
Non-credit institutions (until 2013) / Other financial corporations (as of 20	3.4	3.8	4.3	4.7	5.0	3.5	2.7	2.4
Non-performing loans (NPL) as percent of gross loans[6]	2.7	2.8	3.2	3.2	3.1	2.7	2.6	2.4
Provisions and write-offs as percent of NPL[6]	51.0	53.0	49.4	53.0	54.1	57.1	54.3	55.7
Capital adequacy								
Regulatory capital to risk-weighted assets	17.3	19.3	18.5	18.1	18.7	17.3	18.7	18.8
Regulatory Tier 1 capital to risk-weighted assets	13.2	15.5	15.1	15.8	16.4	15.1	16.0	16.2
Capital to assets	4.5	5.0	4.6	5.8	6.4	6.6	6.5	7.1
NPL net of provisions as percent of Tier 1 capital[6]	13.8	12.2	14.2	13.4	12.3	12.0	12.9	10.7
Net open position in foreign exchange to capital	4.7	3.3	1.4	2.1	2.1	3.4	2.6	2.1

Sources: National Bank of Belgium.

[1] Consolidated data. Data are based on the IAS/IFRS reporting scheme.

[2] Only loans to households as of 2014

[3] Excluding saving certificates as of 2014

[4] Deposits booked at amortized cost only.

[5] Only household deposits as of 2014

[6] Unconsolidated data.

Annex I. Main Recommendations of the 2017 Article IV Consultation and Authorities' Response

Fund Recommendations	Policy Actions
Fiscal policy	
Implement a credible 2017 budget, backed by realistic revenue and spending assumptions, and supported by high quality measures.	The reduction in the 2017 deficit exceeded what was anticipated under the 2017 Stability Program, thanks to a combination of cyclical, structural, and one-off factors.
Make public spending more efficient through measures to reduce subsidies and public employment, better target social benefits, streamline the division of labor between levels of government, and improve the budget process across all levels of government.	Overall public employment levels have stabilized and are expected to decline in coming years. Efforts are ongoing to contain health spending, tighten requirements for the unemployed to accept job offers, and better target social benefits.
Pursue further tax reforms that safeguard revenues while making the system more supportive of jobs and growth.	The CIT appears to be broadly revenue neutral and should help improve Belgium's competitiveness and attract foreign investment.
Structural reforms	
Link wage growth to broader labor market and economic conditions.	The reform of the 1996 law on competitiveness allows the *Conseil Central de l'Economie* to take into account deviations in labor productivity between Belgium and partner countries when calculating the wage norm. This provision has not yet been used, however.
Further reduce the labor tax wedge.	The next phases of the tax shift will enter into effect in 2018-20. The 2017 summer agreement included some measures to reduce social contributions for certain categories of workers.
Improve education and on-the-job training, while promoting the integration of non-EU immigrants. Address barriers to geographic mobility.	The 2017 summer agreement included several measures to help integrate vulnerable groups, including the reintroduction of a trail period, "flexi-jobs," more working hour flexibility, and "mystery calls."
Develop a comprehensive and prioritized strategy to upgrade public infrastructure, agreed between all levels of government and reflected in medium-term budget plans.	The government has established a Strategic Investment Pact aimed at mobilizing public and private funds for investment.
Foster greater competition in services, including in telecommunications, retail, and the legal, architectural, and accounting professions.	A new regulation in telecommunications that facilitates switching the operators ("easy switch") came into force in July 2017. In the Flemish region, the authorities have agreed to lift barriers to entry in certain service professions.
Structural reforms	
To adapt to an environment of low growth and low interest rates, banks should pursue further cost reduction and diversification of revenue sources.	Banks have started to gradually shift income generation toward fees and commissions instead of interest flows.
Closely monitor pockets of vulnerability in the mortgage market.	The NBB proposed a tightening of macroprudential policies to address growing risks in the mortgage market.

Annex II. External Sector Report

	Belgium	Overall Assessment
Foreign asset and liability position and trajectory	**Background**. The net international investment position (NIIP) remains strong at 50 percent of GDP as of 2017Q3, reflecting the continued positive net financial wealth of households. Gross foreign assets were large at 485 percent of GDP, inflated to some extent by intra-group corporate treasury activities. Gross foreign assets of the banking sector stood at 88 percent of GDP, down considerably from the pre-crisis peak. External public debt was 64 percent of GDP as of 2017:Q2, predominantly denominated in euros. Short-term external debt accounted for 29 percent of total external debt. **Assessment**. Belgium's large gross international asset and liability positions are inflated by the presence of corporate treasury units, without creating macro-relevant mismatches. The remaining risk exposures on the asset side mostly relate to financial sector claims. Risk exposures on the liability side are related to external public debt. Based on the projected current account and growth paths, the NIIP to GDP ratio is expected to decline gradually going forward. The strongly positive NIIP and its trajectory do not raise sustainability concerns.	**Overall Assessment**: *The external position in 2017 was moderately weaker than medium-term fundamentals and desirable policy settings would imply.* Recent measures to improve competitiveness, together with stronger external demand, point toward a modest strengthening of the external position over the medium term. The strong net international investment position mitigates vulnerabilities associated with the high external public debt. **Potential policy responses**: Steady fiscal consolidation, reductions in labor taxes, and continued wage moderation would help make the external position fully consistent with fundamentals and policy settings. Productivity enhancing structural reforms (especially reforms to address the severe labor market fragmentation) would also be helpful.
Current account	**Background**. Since the global financial crisis, the current account has hovered around balance, averaging -0.3 percent of GDP over the period 2008–2016. 1/ The stability in the current account balance masks significant movements in the trade and primary income balances. The goods balance moved back into a surplus in 2015 for the first time since the crisis, whereas the primary income balance began to decline in 2013 and turned negative in 2015, driven by a worsening in the investment income balance. In the first half of 2017, the current account recorded a deficit of less than ½ percent of GDP. **Assessment**. Preliminary EBA model estimates point to a CA gap of -2.2 percent of GDP for 2017. Staff estimates a gap in the range of -3¼ to -1¼ percent of GDP. 2/ The CA is projected to remain in small surplus over the medium term, supported by strong external demand and an improving investment income balance as monetary conditions normalize.	
Real exchange rate	**Background**. Wage moderation contributed to a depreciation of the REER in 2014–15. Since end-2015, however, the ULC-based REER has appreciated by 8 percent while the CPI-based REER has appreciated by 5½ percent. **Assessment**. The EBA model points to an REER overvaluation of between 3 and 11 percent, based on the CA and REER methodologies. Staff's assessment is an overvaluation in the range of 3 to 8 percent. 3/	
Capital and financial accounts: flows and policy measures	**Background**. Gross financial outflows and inflows were on an upward trend during the pre-crisis period as banks expanded their cross-border operations. Since 2007, these flows have shrunk and become more volatile as banks have deleveraged. In 2016, short-term debt accounted for about 40 percent of external liabilities and the gross financing need. The capital account is open. **Assessment**. Belgium remains exposed to financial market risks but the structure of financial flows does not point to specific vulnerabilities. The strong NIIP reduces the vulnerabilities associated with the high public debt.	
FX intervention and reserves level	**Background**. The euro has the status of a global reserve currency. **Assessment**. Reserves held by the euro area are typically low relative to standard metrics, but the currency is free floating.	
Technical background notes	1/ The Belgian CA numbers underwent major revisions in 2015 and 2016, complicating the comparison with previous ESR assessments. 2/ Belgium's status as a center of corporate treasury activities, and its resulting large gross foreign asset and liability positions, complicate the measurement of the current account, and thus are a source of uncertainty about the CA assessment. 3/ The REER gap assessment is consistent with staff's CA gap assessment, considering the relatively high ratios of exports and imports to GDP, which tend to make the CA more responsive to the REER.	

Annex III. Risk Assessment Matrix

Source of Risk and likelihood	Impact if realized and transmission channel	Policy response
High Structurally weak growth in key advanced economies due to low productivity growth, a failure to fully address crisis legacies and undertake structural reforms, and persistently low inflation.	**High** Weak growth in partner countries would negatively impact Belgian exports and discourage export-related investment. A protracted growth shortfall could lower potential growth, raise structural unemployment, and complicate fiscal adjustment.	*Implement reforms to improve productivity and raise potential growth.*
Medium Policy and geopolitical uncertainties (e.g., post-Brexit negotiations, two-sided risks to U.S. growth, evolving political processes), and increasing protectionism and economic isolationism.	**High** An increase in protectionism could result in a loss in external demand and make fiscal and structural reforms more difficult. Failure to keep up with competitiveness gains in the rest of the euro area would trigger adverse growth-fiscal dynamics.	*Gradual fiscal adjustment to reduce public debt should be a driving policy objective. Pursue complementary reforms in product markets and reduce the regulatory burden.*
High Tighter global financial conditions due to continued monetary policy normalization and changes in global risk appetite.	**Medium** Limited exposure of domestic banks to global risks. Sovereign-bank nexus is gradually being unwound. Effects would be mainly indirect, through spillovers from neighbors. However, lower U.S. corporate income tax rates and higher yields in the U.S. could lead to capital outflows and constrain investment.	*Euro area monetary policy is first line of defense against liquidity stress, supported by activation of backstops and resolution mechanism.*
Medium Political uncertainty related to the 2019 federal elections.	**High** Reforms could stall ahead of the elections, or if the winning parties are unable to form a new coalition government.	*The government should lock in difficult reforms now, at a time when economic conditions are improving.*
Medium Rapid and disruptive housing price correction.	**Medium** By some measures, Belgium's housing prices are significantly overvalued. The direct impact of a housing price correction on banks could be followed by losses associated with weak consumption if households were to deleverage aggressively. Depressed mortgage loan valuations would also impact banks' asset encumbrance and increase funding costs.	*The NBB should stand ready to tighten macroprudential conditions further if balance sheet risks grow significantly.*

Annex IV. Debt Sustainability Analysis

Public debt sustainability risks remain high. Under the baseline scenario, the public debt-to-GDP ratio is projected to decline to 93.0 percent by 2023 under broadly unchanged policies and steady, but moderate, growth. Gross financing needs are estimated at 16½ percent of GDP in 2018 and are expected to decline slightly over the medium term. The projected decline in public debt is sensitive to a real GDP growth shock, a combined macro-fiscal shock, and a contingent liability shock.

Baseline Scenario and Realism of Projections

In the baseline scenario, the economic recovery and broadly unchanged policies result in a decline in the public debt ratio over the medium term—an improvement compared to the DSA from the 2017 Article IV consultation thanks to significant fiscal consolidation in 2017 and upward revisions to growth in 2017–20.

- **Macroeconomic assumptions.** Growth is expected to increase to 1.9 percent in 2018 but fall back to about 1½ percent over the medium term. The output gap is projected to close in 2018, leading to a modest acceleration in inflation, which is projected to reach 2 percent by the end of the projection period.

- **Fiscal outlook.** Following the strong fiscal performance in 2017, the deficit is projected to remain at about 1¼ percent over the medium term in the absence of clearly identified measures. This leads to a structural deficit of 1.3 percent in 2023. The primary surplus is projected to decline over the projection period, mainly due to revenues losses linked to the next phase of the tax shift.

- **Debt levels and gross financing needs.** Belgium's high level of government debt calls for using the higher scrutiny framework.[1] Government gross debt has increased significantly since 2007, reflecting sizable fiscal stimulus, declining real and nominal growth, and a large recapitalization of (and financial support to) the banking sector. After peaking at 106.8 percent of GDP in 2014, debt has started to gradually decline and is projected to fall to 93.0 percent by the end of the projection period. Gross financing needs are projected to average 15 percent of GDP over the medium term.

- **Realism of baseline assumptions.** The median forecast errors for real GDP growth (0.11 percent), the primary balance (-0.01 percent), and inflation (0.06 percent) are all relatively small, measured over the period 2007–15.

- **Cross-country experience suggests that the projected fiscal path is realistic.** The cyclically-adjusted primary balance (CAPB) is projected to be relatively stable over time, reflecting broadly unchanged policies.

[1] For advanced economies that (i) have a current or projected debt-to-GDP ratio above 60 percent; or (ii) have current or projected gross financing needs-to-GDP ratio above 20 percent; or (iii) have or are seeking exceptional access to Fund resources; teams are required to use an extended set of tools to identify and assess specific risks to debt sustainability. For these "higher scrutiny" cases, teams are also required to produce a standardized summary of risks in a heat map and prepare a write-up to discuss risks, including any country-specific considerations.

- **Heat map.** Risks from the debt level are deemed high given that the relevant threshold to which Belgium's values are compared is 85 percent and this threshold is breached under baseline and all stress test scenarios. Belgium's gross financing needs are below the benchmark of 20 percent of GDP in 2018 and decline slightly over the medium term. Belgium also faces risks relating to its external financing requirement and the large share of public debt held by foreigners. At 83 percent of GDP, the external financing requirement is significantly above the upper threshold of early warning benchmarks, and the share of debt held by foreigners is relatively high at 54 percent of total.

Stress Tests

Stress tests suggest that debt levels are sensitive to a real GDP growth shock and a combined macro-fiscal shock. Debt would increase significantly under a financial sector contingent liability shock.

- **Growth shock.** Under this scenario, real GDP growth is reduced by one standard deviation starting in 2018–19, i.e., 1.6 percentage points relative to the baseline scenario. The assumed decline in growth leads to lower inflation (0.25 percentage points per 1 percentage point decrease in GDP growth). Under this scenario, the debt-to-GDP ratio increases to 106 percent of GDP in 2019 and declines thereafter.

- **Interest rate shock.** This scenario examines the implications for debt sustainability of an increase in interest rates by 496 basis points (calibrated based on a historical high in interest rates observed in 1995) starting in 2018. The debt-to-GDP ratio continues to decline, but at a slower rate. Gross financing needs are 2½ percentage points of GDP higher in 2022 relative to the baseline scenario.

- **Exchange rate shock.** This scenario assumes 10 percent depreciation in the real exchange rate in 2017. This shock results in small effects relative to the baseline.

- **Primary balance shock.** This scenario examines the implications of a revenue shock and a rise in interest rates leading to a cumulative 1.7 percentage points of GDP deterioration in the primary balance (one standard deviation shock) in 2018–19. This scenario illustrates risks of delayed fiscal adjustment, due to insufficient adjustment measures. This shock leads to a modest deterioration in the debt-to-GDP ratio relative to the baseline scenario.

- **Combined macro-fiscal scenario.** This scenario aggregates shocks to real growth, the interest rate, the exchange rate, and the primary balance while avoiding double-counting the effects of individual shocks. Under this scenario, debt stands at 106 percent of GDP and gross financing needs equal 20 percent of GDP at the end of the projection period.

- **Contingent liability shock.** In this scenario, non-interest expenditures in 2018 increase by the equivalent of 10 percent of banking sector assets, and growth slows by 1 standard deviation for two years. Debt increases to 127 percent of GDP before declining slowly.

Belgium: Public Sector Debt Sustainability Analysis (DSA)—Baseline Scenario

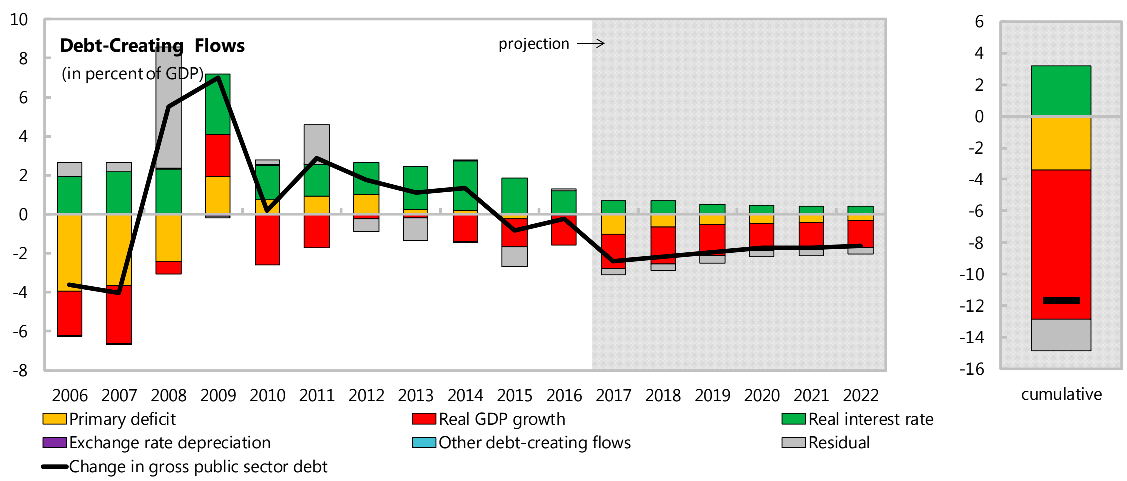
(in percent of GDP unless otherwise indicated)

Debt, Economic and Market Indicators [1/]

	Actual			Projections						As of September 30, 2017		
	2006-2014 [2/]	2015	2016	2017	2018	2019	2020	2021	2022	Sovereign Spreads		
Nominal gross public debt	98.8	106.0	105.7	103.3	101.1	99.1	97.4	95.7	94.1	EMBIG (bp) 3/		28
Public gross financing needs	10.4	10.5	9.9	17.4	16.6	15.3	14.0	13.0	15.6	5Y CDS (bp)		19
Real GDP growth (in percent)	1.2	1.4	1.5	1.7	1.9	1.7	1.5	1.5	1.5	Ratings	Foreign	Local
Inflation (GDP deflator, in percent)	1.6	1.1	1.6	1.8	1.6	1.7	1.6	1.6	1.6	Moody's	Aa3	Aa3
Nominal GDP growth (in percent)	2.8	2.5	3.1	3.6	3.5	3.4	3.1	3.2	3.1	S&Ps	AA	AA
Effective interest rate (in percent) [4/]	3.9	2.9	2.8	2.5	2.3	2.2	2.1	2.1	2.1	Fitch	AA-	AA-

Contribution to Changes in Public Debt

	Actual			Projections							
	2006-2014	2015	2016	2017	2018	2019	2020	2021	2022	cumulative	debt-stabilizing
Change in gross public sector debt	1.3	-0.8	-0.2	-2.4	-2.2	-1.9	-1.7	-1.7	-1.6	-11.6	primary
Identified debt-creating flows	0.5	0.2	-0.3	-2.1	-1.9	-1.6	-1.4	-1.4	-1.3	-9.7	balance [9/]
Primary deficit	-0.6	-0.2	-0.1	-1.0	-0.7	-0.5	-0.5	-0.4	-0.3	-3.4	-1.0
Primary (noninterest) revenue and grants	49.7	51.0	50.4	50.8	50.1	49.7	49.5	49.5	49.5	299.3	
Primary (noninterest) expenditure	49.2	50.8	50.3	49.7	49.4	49.2	49.1	49.1	49.2	295.9	
Automatic debt dynamics [5/]	1.0	0.4	-0.3	-1.1	-1.2	-1.1	-0.9	-1.0	-1.0	-6.3	
Interest rate/growth differential [6/]	1.0	0.4	-0.3	-1.1	-1.2	-1.1	-0.9	-1.0	-1.0	-6.3	
Of which: real interest rate	2.2	1.8	1.2	0.7	0.7	0.5	0.5	0.4	0.4	3.2	
Of which: real GDP growth	-1.1	-1.5	-1.5	-1.7	-1.9	-1.6	-1.4	-1.4	-1.4	-9.5	
Exchange rate depreciation [7/]	0.0	0.0	0.0	…	…	…	…	…	…	…	
Other identified debt-creating flows	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes [8/]	0.9	-1.0	0.1	-0.3	-0.3	-0.3	-0.3	-0.3	-0.3	-2.0	



Source: IMF staff.

1/ Public sector is defined as general government.

2/ Based on available data.

3/ Long-term bond spread over German bonds.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ Derived as [(r - π(1+g) - g + ae(1+r)]/(1+g+π+gπ)) times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

6/ The real interest rate contribution is derived from the numerator in footnote 5 as r - π (1+g) and the real growth contribution as -g.

7/ The exchange rate contribution is derived from the numerator in footnote 5 as ae(1+r).

8/ Includes asset changes and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

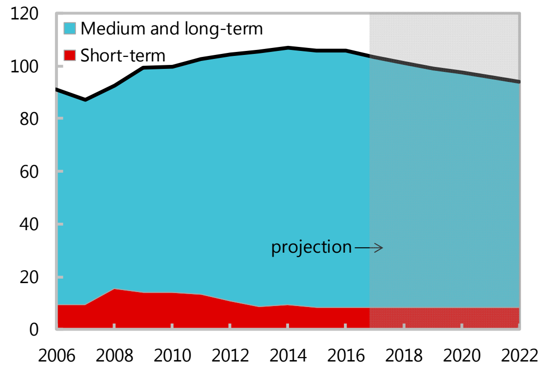
9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Belgium: Public DSA—Composition of Public Debt and Alternative Scenarios

Composition of Public Debt

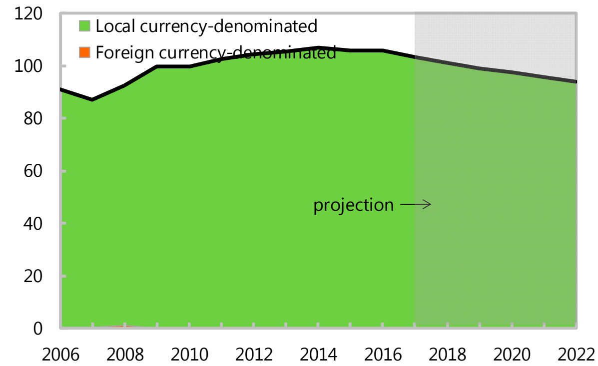
By Maturity

(in percent of GDP)



By Currency

(in percent of GDP)

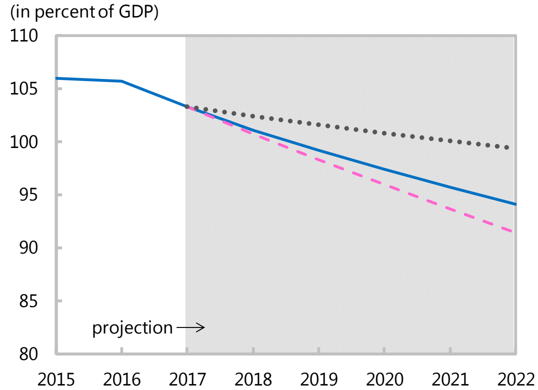


Alternative Scenarios

Baseline — Historical — Constant Primary Balance

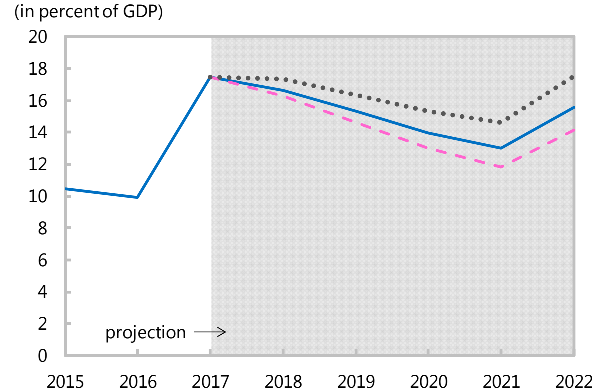
Gross Nominal Public Debt

(in percent of GDP)



Public Gross Financing Needs

(in percent of GDP)



Underlying Assumptions

(in percent)

Baseline Scenario	2017	2018	2019	2020	2021	2022
Real GDP growth	1.7	1.9	1.7	1.5	1.5	1.5
Inflation	1.8	1.6	1.7	1.6	1.6	1.6
Primary Balance	1.0	0.7	0.5	0.5	0.4	0.3
Effective interest rate	2.5	2.3	2.2	2.1	2.1	2.1
Constant Primary Balance Scenario						
Real GDP growth	1.7	1.9	1.7	1.5	1.5	1.5
Inflation	1.8	1.6	1.7	1.6	1.6	1.6
Primary Balance	1.0	1.0	1.0	1.0	1.0	1.0
Effective interest rate	2.5	2.3	2.2	2.2	2.1	2.1

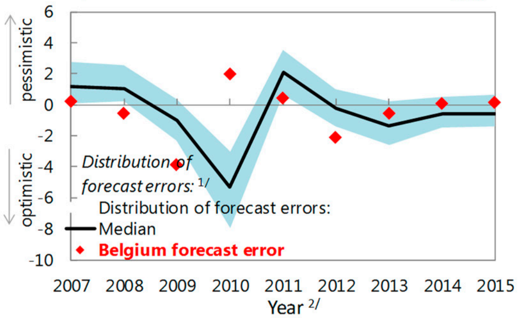
Historical Scenario	2017	2018	2019	2020	2021	2022
Real GDP growth	1.7	1.1	1.1	1.1	1.1	1.1
Inflation	1.8	1.6	1.7	1.6	1.6	1.6
Primary Balance	1.0	0.1	0.1	0.1	0.1	0.1
Effective interest rate	2.5	2.3	2.4	2.4	2.5	2.6

Source: IMF staff.

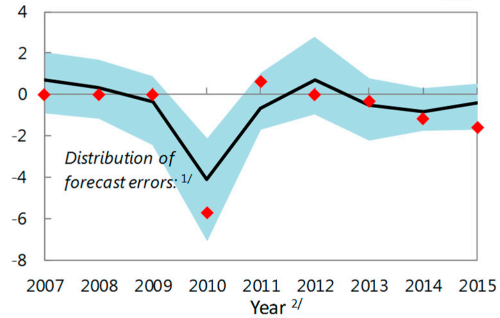
Belgium: Public DSA—Realism of Baseline Assumptions

Forecast Track Record, versus all countries

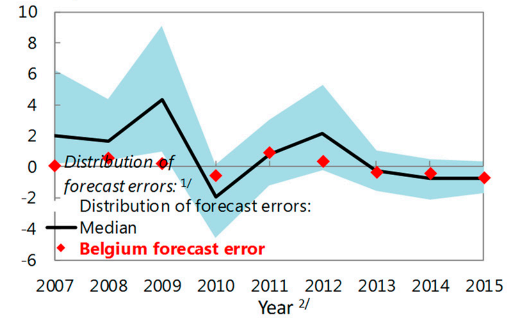
Real GDP Growth
(in percent, actual-projection)
Belgium median forecast error, 2007-2015: 0.11
Has a percentile rank of: 77%



Primary Balance
(in percent of GDP, actual-projection)
Belgium median forecast error, 2007-2015: -0.01
Has a percentile rank of: 48%

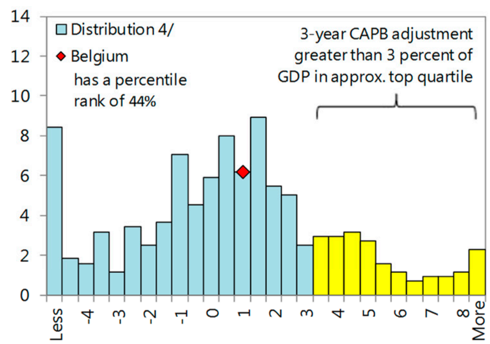


Inflation (Deflator)
(in percent, actual-projection)
Belgium median forecast error, 2007-2015: 0.06
Has a percentile rank of: 39%

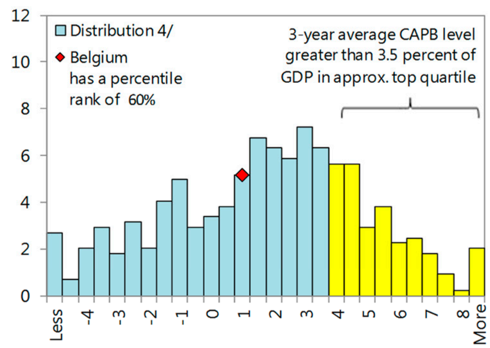


Assessing the Realism of Projected Fiscal Adjustment

3-Year Adjustment in Cyclically-Adjusted Primary Balance (CAPB)
(Percent of GDP)

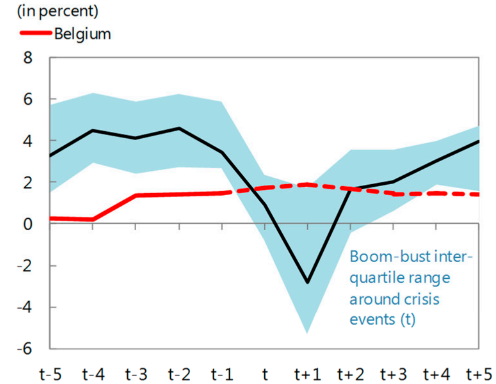


3-Year Average Level of Cyclically-Adjusted Primary Balance (CAPB)
(Percent of GDP)



Boom-Bust Analysis 3/

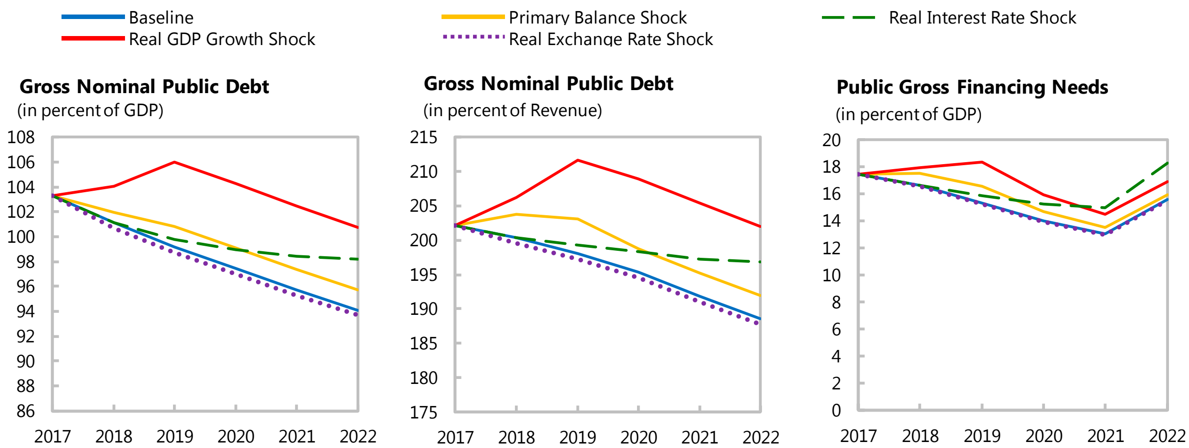
Real GDP growth
(in percent)



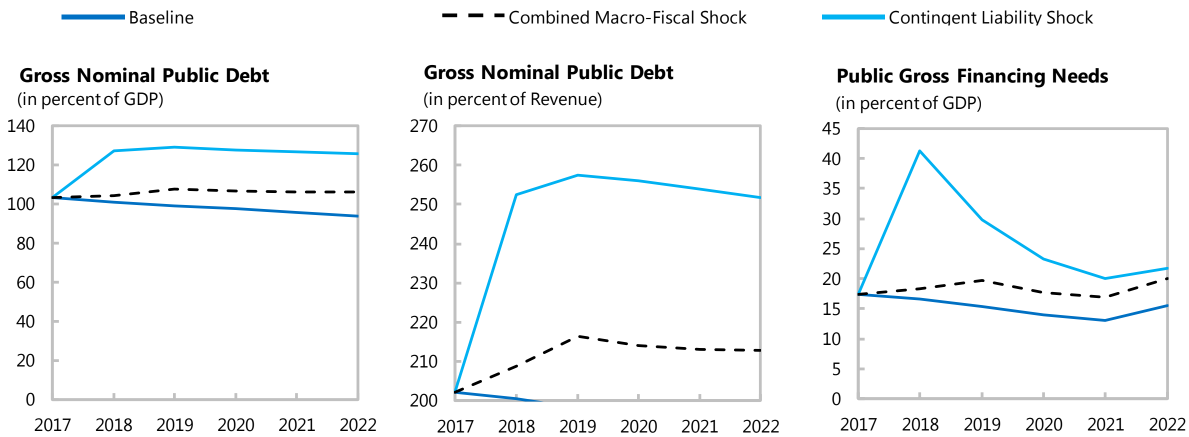
Source : IMF Staff.
1/ Plotted distribution includes all countries, percentile rank refers to all countries.
2/ Projections made in the spring WEO vintage of the preceding year.
3/ Belgium has had a cumulative increase in private sector credit of 38 percent of GDP, 2013-2016. For Belgium, t corresponds to 2017; for the distribution, t corresponds to the first year of the crisis.
4/ Data cover annual obervations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

Belgium: Public DSA—Stress Tests

Macro-Fiscal Stress Tests



Additional Stress Tests



Underlying Assumptions

(in percent)

	2017	2018	2019	2020	2021	2022
Primary Balance Shock						
Real GDP growth	1.7	1.9	1.7	1.5	1.5	1.5
Inflation	1.8	1.6	1.7	1.6	1.6	1.6
Primary balance	1.0	-0.2	-0.3	0.5	0.4	0.3
Effective interest rate	2.5	2.3	2.2	2.2	2.1	2.1
Real Interest Rate Shock						
Real GDP growth	1.7	1.9	1.7	1.5	1.5	1.5
Inflation	1.8	1.6	1.7	1.6	1.6	1.6
Primary balance	1.0	0.7	0.5	0.5	0.4	0.3
Effective interest rate	2.5	2.3	2.8	3.1	3.4	3.6
Combined Shock						
Real GDP growth	1.7	0.3	0.1	1.5	1.5	1.5
Inflation	1.8	1.2	1.3	1.6	1.6	1.6
Primary balance	1.0	-0.7	-1.9	0.5	0.4	0.3
Effective interest rate	2.5	2.3	2.9	3.2	3.4	3.7

	2017	2018	2019	2020	2021	2022
Real GDP Growth Shock						
Real GDP growth	1.7	0.3	0.1	1.5	1.5	1.5
Inflation	1.8	1.2	1.3	1.6	1.6	1.6
Primary balance	1.0	-0.3	-1.4	0.5	0.4	0.3
Effective interest rate	2.5	2.3	2.2	2.2	2.1	2.1
Real Exchange Rate Shock						
Real GDP growth	1.7	1.9	1.7	1.5	1.5	1.5
Inflation	1.8	2.0	1.7	1.6	1.6	1.6
Primary balance	1.0	0.7	0.5	0.5	0.4	0.3
Effective interest rate	2.5	2.3	2.2	2.1	2.1	2.1
Contingent Liability Shock						
Real GDP growth	1.7	0.3	0.1	1.5	1.5	1.5
Inflation	1.8	1.2	1.3	1.6	1.6	1.6
Primary balance	1.0	-23.5	0.5	0.5	0.4	0.3
Effective interest rate	2.5	2.4	3.3	2.8	2.8	2.8

Source: IMF staff.

Belgium: Public DSA Risk Assessment

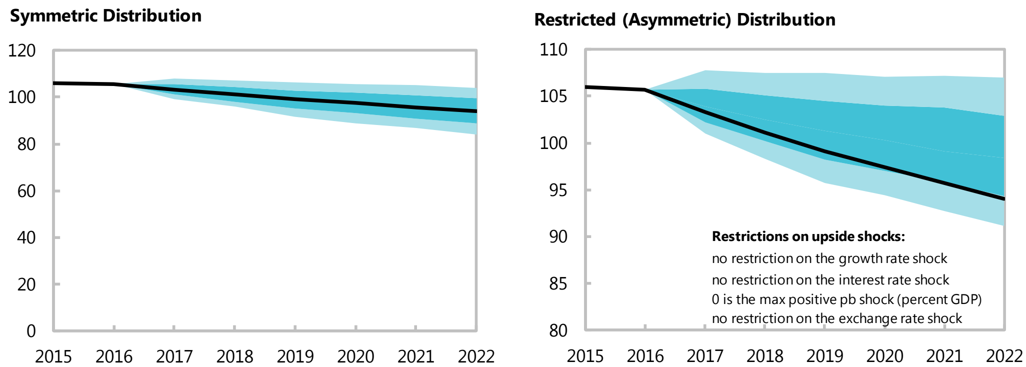
Heat Map

Debt level 1/	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability shock
Gross financing needs 2/	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock
Debt profile 3/	Market Perception	External Financing Requirements	Change in the Share of Short-Term Debt	Public Debt Held by Non-Residents	Foreign Currency Debt

Evolution of Predictive Densities of Gross Nominal Public Debt

(in percent of GDP)

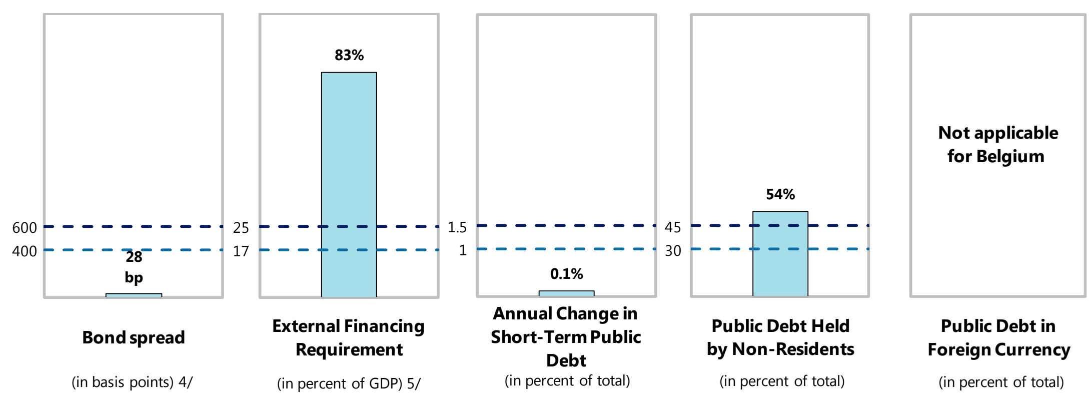
Baseline   Percentiles: 10th-25th   25th-75th   75th-90th



Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks, in 2016)

Belgium   Lower early warning   Upper early warning



Source: IMF staff.

1/ The cell is highlighted in green if debt burden benchmark of 85% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

2/ The cell is highlighted in green if gross financing needs benchmark of 20% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant, cell is white.
Lower and upper risk-assessment benchmarks are:

400 and 600 basis points for bond spreads; 17 and 25 percent of GDP for external financing requirement; 1 and 1.5 percent for change in the share of short-term debt; 30 and 45 percent for the public debt held by non-residents.

4/ Long-term bond spread over German bonds, an average over the last 3 months, 02-Jul-17 through 30-Sep-17.

5/ External financing requirement is defined as the sum of current account deficit, amortization of medium and long-term total external debt, and short-term total external debt at the end of previous period.

Annex V. Labor Market and Pension Reform Measures

Date of reform	Description	Status
UNEMPLOYMENT BENEFITS		
Search requirements		
January 1, 2012	Suitable job is 25 km away or less → Suitable job is 60 km away or less.	Implemented
January 1, 2012	Restrict rights to search for the same kind of job to six months → Restrict right to search for the same kind of job to three months (young unemployed) and five months (other unemployed).	Implemented
July 1, 2014	Monitor search efforts for 18–21 months after unemployment, with an annual follow-up → Monitor search efforts nine months (<26 years old) or 12 months (26 or older) after start of unemployment, with follow-ups every nine months.	Implemented
January 1, 2015	Search requirement until 60 → Search requirements applicable until 60 and according to concept of "adequate availability" between 60 and 65. Exemptions are still possible according to the length of the career.	Pending the agreement on the definition of "adequate availability"
January 1, 2015	Exemption of search requirements for familial and social reasons → Use of the exemption is restricted (exemption for caregivers with more restrictive access conditions).	Implemented
	To obtain unemployment benefits, unemployed have to be registered as job seekers within 2 weeks from the day they are laid off → Registration as job seeker has to be done within 4 weeks following the notice of lay-off.	Postponed at request of the social partners
Unemployment benefit levels		
November 1, 2012	Initial unemployment benefits are 60 percent of last wage, falling after one year to 55 percent for people living alone and 40 percent for people living in a family with another income → Initial unemployment benefits are 65 percent of last wage for three months, then 60 percent for the following nine months. After 13 months there is a reduction to 55 percent for people living alone and 40 percent for people living in a family with another income. Between 15 and 24 months of unemployment, depending on career length before unemployment, a stepwise reduction to arrive after maximum 48 months at a level just above social assistance.	Implemented
November 1, 2012 November 1, 2015 November 1, 2016	No degressivity of unemployment benefits for unemployed proving long periods of work → Required career length did raise from 20 years in 2012, to 23 years in 2015, and will become 25 years from November 2016 on.	Implemented
September 1, 2012	Higher unemployment benefits for unemployed above 50 (Seniority complement) → Eliminated for new entrants, except in specific cases related to collective dismissals or heavy jobs.	Implemented

	Unemployment benefit based on the wage of the last work period of at least 4 weeks → Unemployment benefit based on the average wage of the last 12 months.	Administratively complicated to implement; considering alternatives with the same goal
January 1, 2015	Involuntary part time workers can obtain an allowance for income support so that their net income is higher than the unemployment benefit in case of full unemployment → Allowance for income support in case of part time job (AGR) is divided by 2 after two years of work. Replaced by mechanism to suspend allowance when employee does not accept more hours; employer who does not give available supplementary hours to part time workers with an allowance pays an extra charge. Calculation of the allowance for income support (AGR) is reviewed based on the calculation that was made before 2008	In draft law. Adapted calculation: implemented.
Unemployment benefits for the young entering the labor force		
January 1, 2012	Available after nine months of unemployment → Available after 12 months of unemployment.	Implemented
August 1, 2013	Evaluation of search efforts before opening the right on unemployment benefits for young people leaving school → Two evaluations of search efforts 7 and 11 months after registering as jobseeker. Opening of right on unemployment benefits only after two positive evaluations.	Implemented for all youth that have left school after June 1, 2013
July 1, 2014	Search effort requirement every 12 or 16 months when on unemployment benefits based on studies (insertion benefits, the earlier waiting allowances) → Evaluation of search requirements every six months. In case of negative evaluation: no UB until the next evaluation, and no earlier than after 6 months.	Implemented
January 1, 2012	Unlimited → Limited to three years (five years for worker on the margin of the labor market) for unemployed living with family with other income, or until the age of 33 in other family situations. Period of three years could be extended by six months if at least worked six months in the last 24 months.	Implemented—first application started in January 2015
September 1, 2015	Young school leavers can apply for unemployment benefit if they have participated in the secondary education final exam → Until 21, young school leavers can apply for unemployment benefit if they have obtained a secondary education degree or another degree opening good prospects on the labor market.	Implemented
January 1, 2015	For school leavers, the maximum age to introduce a demand for unemployment benefits is 30 → Maximum age reduced to 25.	Implemented

Easing the transition to the labor market for low-skilled youth		
January 1, 2014 September 1, 2015	At sectoral level social partners have to conclude collective agreements addressing the employment needs of groups at risk for the equivalent of at least 0.10 percent of gross wage cost of the whole sector. → 2013: at least one quarter (0.025 percent) of the money spent has to go to unemployed youth < 26 years. 2015: sectors are invited to raise the effort for youth: at least 0.05 percent has to go to actions for youth.	Implemented
September 1, 2015	Supplementary efforts at sectorial level for so called "ingrown" jobs for youth < 26 years without work-experience → Sectorial plans to offer supplementary job experience for youth in ingrown-jobs (total budget of €12 million), only accessible for sectors that have foreseen an effort of at least 0.05 percent (see previous line).	13 plans approved—implementation in 2016–17
Government subsidy for temporary unemployment		
January 1, 2012 April 1, 2016	Without employer penalty → Employers will pay a penalty if there is excess use of the system.	Implemented and strengthened from 2016 on
January 1, 2015	Allowance for temporary unemployment is 70 percent of last salary → Reduced to 65 percent of salary.	Implemented
January 1, 2012 April 1, 2016	No limits on the use by employers of temporary unemployment → Stronger penalty in case of excessive use.	Implemented
Government subsidy for time-credit and career break system		
January 1, 2012 September 1, 2012 January 1, 2015 April 1, 2017	Five-year duration before the age of 50 → 2013: One-year duration (two to five years if part-time), with supplementary credit of maximum 36 months for specific motivated breaks, such as childcare or studies (maximum 48 months for specific cases such as taking care of a handicapped child less than 21 years old). 2015: Removal of the rights to benefits for one-year non-motivated break. The rights to a one-year non-motivated break are maintained, but without any payment. For childcare, one supplementary year of break with benefits. 2017: Abrogation of the rights to a one-year non-motivated break.	Implemented Implemented Implemented
January 1, 2012 September 1, 2012 January 1, 2015	Unlimited duration above the age of 50 (time reduction) → 2013: Unlimited duration above the age of 55 (time reduction). 2015: Unlimited duration (time reduction) above the age of 60 and 25 years of seniority (with transitional measures and possible derogations till 2019).	Implemented Implemented with some exceptions (age limit 55) for long periods of night- and shiftwork
January 1, 2012	72-month duration in public sector → 60-month duration in public sector.	Implemented

	More favorable rights on career breaks in the public sector → Progressive harmonization of career break in the public sector with time credit in the private sector (full harmonization by 2020).	Planned by the government
PENSION BENEFITS		
Supplementary pensions		
January 1, 2019	Previously: pre-pension years count fully towards pension rights at the last wage level. Implemented by previous government: pre-pension years below the age of 60 do not count towards pension rights at last wage level but on a lower fictive level. Planned by this government: from January 1, 2019 onwards, all pre-pension years will count towards pension rights at a lower fictive level (cf. infra).	Will be applicable from January 1, 2019 onwards.
2018	The possibility of installing a supplementary pension (second pillar) will be available to self-employed workers who are not company managers.	Submitted to Parliament
2018	Employees will have the opportunity to voluntarily invest in a supplementary pension in the second pillar through payroll deductions made by the employer.	Principles approved by the Council of Ministers
Pre-pension benefits (renamed to "Unemployment benefits with employer top-up")		
January 1, 2012 January 1, 2015	Minimum age and career length: 60/30 (men) 60/26 (women) → 2012/13: Minimum age and career length 60/40 for new collective agreements (60 years in 2015 for existing agreements with 40 years career in 2015 for men and in 2024 for women).	Implemented
January 1, 2012 January 1, 2015	Or: 58/37 (men) and 58/33 (women) for long careers → 2012/13: 60/40 for men, 35 for women (40 in 2015) for new collective agreements. For existing agreements: 60 in 2015 for men and 38 for women (40 in 2017)	Implemented
January 1, 2015	Or: 58/35 for heavy jobs → 58/35 for heavy jobs Minimum age 58 for new entrants in case of hardship jobs (60 on a date to be fixed by the National Labor Council) Special schemes 56/33 become 58/33 (60 on a date to be fixed by the National Labor Council).	Implemented – transitional period 2015–2017 with possibility to maintain 60 instead of 62
SPF Pensions	Pre-pension years count fully towards pension rights at the last wage level → Pre-pension years below the age of 60 do not count towards pension rights at last wage level but on a lower fictive level	Implemented
January 1, 2016 and January 1, 2017	Reduced social security contributions on employer's top-up payment → Employer social security contributions will be higher and linked to age of worker entering pre-pension	Implemented
January 1, 2015	The age limit in restructuring companies and loss-making companies is between 50 and 55 → 2015: The age limit is 55 in 2015 and rises every year with one year to arrive at the minimum age of 60 in 2020 for companies in difficulty. For companies undergoing restructuring, the age limit will be 60 in 2020.	Implemented

January 1, 2016	Top-up from the employer is submitted to taxation → No taxation during periods of work by another employer	Implemented
Part-time pre-pension system		
	Part-time pre-pension system → No new entries from 2012	Implemented
Government subsidy for working time reduction to part time (time-credit with unlimited duration)		
January 1, 2012	Minimum age 50 → 2013: Minimum age 55 (with exceptions for physically demanding jobs)	Implemented
January 1, 2015	2015: Minimum age 60 (with exceptions for physically demanding jobs). Only for the benefits (not the rights).	Planned by the new government
Statutory early retirement benefit		
	2013: minimum age increased by six months every year to 62 by 2016, career length increased by one year every year to 40 years by 2015. Exceptions for long career: 61/41 or 60/42 in 2016.	Implemented by previous government
Program Act of December 19, 2014	From 2015 onwards: minimum age will increase by six months in 2017 and 2018 to 63 on condition of a full career length that will increase by one year to 41 in 2017 and to 42 in 2019. Exceptions for long career will be stricter: required career length to retire at 60 will increase from 42 years in 2016 to 43 years in 2017 and 44 in 2019 (and for an early retirement at the age of 61 career length rises from 41 in 2016 to 42 in 2017 and 43 in 2019).	Implemented
Program Act of December 19, 2014	After introducing a unified pension bonus for workers, self-employed persons and statutory government employees by the previous government, the pension bonus is phased out. Only people who met conditions for early retirement by December 31, 2014 or were 65 years old and had a career of 40 before December 31, 2014 were still eligible to a pension bonus.	Implemented
Law of April 28, 2015	Diploma bonus for career condition early retirement: years spent to get a bachelor or a master degree required to become civil servants are accounted for in the calculation of the career condition for early retirement. Diploma bonus is being phased out since the start of 2016.	Implemented
Law of October 2, 2017	Harmonization of the diploma bonus for the pension calculation: the years spent to get a bachelor or a master degree required to become civil servants were taken into account for free in the pension calculation of statutory government employees. This will be abolished from December 1, 2017 onwards, and the same system of paid regularization of the study period will be applicable to all pension regimes.	Implemented
January 1, 2019	Introduction of "heavy jobs" in the pension system—will replace the so-called "tantièmes" in the civil servants' scheme: the preferential career fractions ("tantièmes") will be adapted and integrated in the general pension scheme for civil servants.	Will be applicable from January 1, 2019 onwards

	The preferential regimes that exist for the military and the mobile personnel of the national railway company will be abolished. These measures will be accompanied by the introduction of specific pension measures for "heavy jobs" ("zwaar werk"/"métier lourd" = particularly demanding and tough jobs).	
Employer obligations towards older workers		
January 1, 2013	Draw up a plan to retain older workers	Implemented by collective agreement n° 104
Social security contributions and wage subsidies		
January 1, 2014 January 1, 2015 January 1, 2016 January 1, 2017	Reduction for small SME's → 2014: First hiring in SMEs extended to 4 and 5 2015: strengthening for first three 2016: First hirings extended to 6+, strengthening for 1–5 hirings (complete exemption for 1st employee during unlimited period) 2017: further strengthening (period of advantage extended to 3 years for 4th to 6th employees)	Fully implemented
July 1, 2016	Following the 6th state reform, reductions in social security contributions for target groups became a regional competence. In Flanders, the existing reductions for the youth, older workers, and the long-term unemployed were reformed into two major reductions: for the hiring of young workers (<25) without a higher education degree and with a low wage, and for older workers (55+), with a higher reduction when hiring older jobseekers.	Implemented
Encourage longer employment via pension system reforms		
Law of August 10, 2015	Legal pension age of 65 is increased to 66 in 2025 and 67 in 2030.	Implemented
Law of August 10, 2015	Previously: survivors' pension for widow(er)s: always for survivors of 45 years and older; under certain conditions in case of survivors younger than 45. Previous government: for widow(er)s younger than 45 survivors' pension replaced by transition allowance (12 months if no children, 24 months if children) that can be combined without limitation with work income, followed by automatic access to unemployment benefit if no gainful occupation and entitled to appropriate and early guidance. Eligibility age of 45 increased gradually to 50 by 2025. This government: as for 2025, the eligibility age of 50 will increase gradually by one year each year to reach 55 in 2030.	Implemented Overturned by the Constitutional Court in November 2017.
Royal decree of January 20, 2015	Previous government: for pensioners aged 65 or more, ceiling on permitted earned incomes is abolished for those with careers spanning more than 42 years. From 2015 onwards: no limits to income for pensioners who are 65 years old or have a career of 45 years.	Implemented

January 1, 2019	Previously: full valorization of assimilated periods in pension calculation at last wage earned: unemployment, unemployment with company top-up and time credit. Previous government: limited valorization of assimilated periods in pension calculation of the 3rd period of unemployment, unemployment with company top-up before 60 and end of career time credit before 60 at pension minimum wage. Unmotivated time credit limited to 1-year assimilation. From 2019 onwards, assimilated periods of the 2nd and 3rd period of unemployment as well as unemployment with company top-up, regardless of age, at pension minimum wage. Exceptions to these principles include, • with regard to unemployment: periods of unemployment after the age of 50; • with regard to unemployment with company top-up: companies in restructuration and companies in difficulties, unemployment with company top-up after a career of "heavy job" as well as unemployment with company top-up for medical reasons.	Applicable from January 1, 2019 onwards
Royal decree of December 30, 2014	Unmotivated time credit is no longer taken into account for pension calculation from 2015 onwards, as an unemployment benefit is no longer granted for this type of time credit.	Implemented
January 1, 2019	Previously: principle of career unity in pension calculation in pension schemes of workers, self-employed persons and statutory government employees: career fraction or sum of career fractions cannot exceed 1 (45/45). Previous government: from 2015 onwards, notion of career no longer expressed in years (45), but in full time equivalent days (14,040). From 2019 onwards: all days that are effectively worked will result in pension rights, even if they exceed the reference career of 14.040 days. Days of unemployment or pre-pension that exceed the reference career of 14.040 days will no longer result in supplementary pension rights.	Voted in Parliament November 23, 2017
January 1, 2019	Introduction of the partial pension. The partial pension will allow taking up a part of the pension rights while accumulating pension rights for the (partially) continued activity.	Applicable from January 1, 2019 onwards
Law of December 18, 2015	Access to the second pillar pension has been adapted to be in line with the statutory retirement age: second pillar pension accessible only when conditions for legal pension are met.	Implemented
Decrease pension expenditure		
Program Act of December 19, 2014	Previously: pension complement for frontier or seasonal workers in workers' pension scheme: frontier or seasonal workers residing in Belgium granted pension complement to increase foreign pension to level of pension they would have received if they had worked in Belgium.	Implemented

	As of 2015, pension complement for frontier or seasonal workers is no longer granted to people who did not work as frontier or seasonal workers before 2015. For those who have worked as a frontier or seasonal worker before December 1, 2015, the pension complement: • takes into account all other pension benefits; • is only granted when the foreign legal pension is taken up.	
Royal decree of December 9, 2014	Minimum pension: Career condition to benefit from 1/45th of the minimum pension is 30 years of 208 days. If condition is met, 1 day suffices to obtain an additional 1/45 of the minimum pension. From 2015, at least 52 days in a year are required to obtain 1/45th of the minimum pension.	Implemented
December 1, 2017	Introduction of the "mixed pension": the periods during which a civil servant worked as an employee and not as a statutory member of the personnel will no longer be taken into account for the statutory pension but create a pension as employee. The legal framework for supplementary pensions will be adapted to encourage public administrations and companies to offer a supplementary pension scheme to their employees. The federal government will install a supplementary pension system, financed by sufficient contributions, for its employees.	Discussed in Parliament
	Abolition of the pension for physical incapacity: the government has presented a proposal and possibilities to the local authorities to replace the pension for physical incapacity, which exists only in the public sector, with a similar system to the social security system of benefits for incapacity and invalidity applicable in the private sector. This approach will act as a stimulus for the professional reintegration of the civil servant, whereas the pension for physical incapacity that exists today functions as an inactivity trap.	Negotiations between different levels of the government
	Structural reform of the pension scheme: a points-based pension system will be implemented by 2030. This will allow a closer and more transparent monitoring of the financial sustainability and equilibrium of the Belgian pension system.	Preparatory debates in the National Pensions Committee
Sources: Belgian Federal Public Service Employment, Labor and Social Dialogue, National Bank of Belgium, National Employment Office, Federal Planning Bureau, Ministry of Pensions, and Belgian Stability Program 2012–15.		

INTERNATIONAL MONETARY FUND

BELGIUM

February 21, 2018

STAFF REPORT FOR THE 2018 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

Prepared By | European Department

CONTENTS

FUND RELATIONS

(As of December 31, 2017)

Membership Status: Joined December 27, 1945; Article VIII.

General Resources Account:

	SDR Million	**Percent of Quota**
Quota	6,410.70	100.00
IMF's Holdings of Currency (Holdings Rate)	6,111.68	95.34
Reserve Tranche Position	299.05	4.66
Lending to the Fund		
New Arrangements to Borrow	441.70	

SDR Department:

	SDR Million	**Percent of Allocation**
Net Cumulative Allocation	4,323.34	100.00
Holdings	3,892.00	90.04

Outstanding Purchases and Loans: None

Latest Financial Arrangements:

Type	Date of Arrangement	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
Stand-By	Jun 19, 1952	Jun 18, 1957	50.00	50.00

Overdue Obligations and Projected Payments to Fund [1/]

(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2018	2019	2020	2021	2022
Principal					
Charges/Interest	3.30	3.32	3.32	3.31	3.32
Total	3.30	3.32	3.32	3.31	3.32

[1/] When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

Implementation of HIPC Initiative: Not applicable

Safeguards Assessments: Not applicable

Exchange Rate Assessments:

- Belgium's currency is the euro, which floats freely and independently against other currencies.
- Belgium has accepted the obligations under Article VIII, Section 2(a) and 3, and maintains an exchange system free of restrictions on payment and transfers for current international transactions except for restrictions maintained solely for security reasons, which have been notified to the Fund pursuant to Executive Board Decision No. 144-(52/51).

Last Article IV Consultation:

The last Article IV consultation was concluded on March 13, 2017. The associated Executive Board assessment is available at http://www.imf.org/en/News/Articles/2017/03/17/pr1788-imf-executive-board-concludes-2017-article-iv-consultation-with-belgium and the staff report (IMF Country Report No. 17/69) at http://www.imf.org/~/media/Files/Publications/CR/2017/cr1769.ashx. Belgium is on the standard 12-month consultation cycle.

Financial Sector Assessment Program (FSAP) Participation

- **Belgium: Financial System Stability Assessment** — IMF Country Report (forthcoming)

Summary: The FSAP conducted in late 2017 concluded that the Belgian financial sector has become more resilient as a result of structural changes experienced since the global financial crisis, but is facing growing vulnerabilities, mostly in the form of risky mortgages. Nonetheless, banks and insurance companies remain capable of absorbing credit, sovereign, and market losses in the event of a severe deterioration in macro financial conditions. To contain rising mortgage-related risks, macroprudential policies recently proposed by the NBB should be enacted promptly. Other risks, including banks' capacity to cope with interest rate shocks, credit risk vulnerabilities in selected portfolios, and growing liquidity risk in insurance companies, should be monitored closely.

Financial sector supervision and crisis management arrangements have been upgraded markedly. However, the transition to a full banking union must be carefully managed by national and European authorities given the presence in Belgium of large subsidiaries of euro area banks. Sufficient capital and loss absorbing capacity should be kept in these subsidiaries to ensure the viability of group resolution strategies. The NBB and European authorities should continue ongoing efforts to upgrade their supervisory and crisis management frameworks and operational capacity, including by prioritizing the resolution planning for important banks and strengthening the deposit insurance system. It will also be important to address the challenges posed by complex financial conglomerates, ongoing changes in the risk profile of the insurance sector, and potential challenges arising from the low quality of some insurers' capital.

The oversight arrangement for the Belgium-based Society for Worldwide Interbank Financial Telecommunication (SWIFT) has proven effective, but is being challenged by new risks. To strengthen the NBB's ability to exercise its role as overseer and protect Belgium's reputation as a key hub for financial market infrastructures, the authorities should consider complementing the NBB's use of moral suasion with regulatory and supervisory powers and should enhance the NBB's ability to share information with foreign authorities.

Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT):

Belgium's AML/CFT framework was last assessed by the Financial Action Task Force (FATF) in July 2014. The FATF evaluation found a well-established regime, notwithstanding some deficiencies. Since then, steps have been taken to strengthen the framework, notably with respect to combating the financing of terrorism and AML/CFT supervision. However, efforts need to continue to fully implement the FATF's recommended actions.

STATISTICAL ISSUES

Belgium's economic and financial statistics are adequate for surveillance purposes. The National Bank of Belgium (NBB) regularly publishes a full range of economic and financial data and provides calendar dates of main statistical releases. On-line access to these comprehensive databases is facilitated by the NBB's data search engine, NBB.Stat. Belgium is a SDDS subscriber. Statistics for International Financial Statistics on banking institutions and monetary aggregates are prepared on a monthly basis and are timely.

Belgium adopted the European System of Integrated Economic Accounts 2010 (ESA 2010) in 2014. Revisions of national accounts were released in September 2014 to comply with EUROSTAT requirements to provide national accounts statistics in ESA 2010. Unlike in other countries, the central bank is responsible for compiling national accounts statistics. Quarterly accounts are published within a lag of three months. Both annual and quarterly accounts data are of good quality, with shortcomings mainly related to export and import deflators, which are based on unit values, rather than prices collected directly from exporters and importers.

Belgium compiles and publishes a complete set of general government accounts on an accrual basis (ESA 2010). The NBB publishes annual and quarterly data on general government revenue, expenditure, and net lending/ borrowing; transactions in financial assets and liabilities and a financial balance sheet data; and details on the consolidated gross debt.

The overall quality and availability of financial indicators are good. The authorities are providing quarterly updates of financial sector indicators (FSIs) in a timely manner.

Key publicly accessible websites for macroeconomic data and analysis are:

NBB.Stat, http://stat.nbb.be/?lang=en

National Statistics Institute, www.statbel.fgov.be

National Bank of Belgium, www.nbb.be

Federal Planning Bureau, www.plan.be

High Council of Finance, https://www.highcounciloffinance.be

Central Economic Council, www.ccecrb.fgov.be

Belgium: Common Indicators Required for Surveillance

(As of January 2018)

	Date of latest observation	Date received	Frequency of Data[6]	Frequency of Reporting[6]	Frequency of Publication[6]
Exchange Rates	12/17	1/18	M	M	M
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	12/17	1/18	M	M	M
International Investment Position	2017:Q3	12/17	Q	Q	Q
Reserve/Base Money	11/17	12/17	M	M	M
Broad Money	11/17	12/17	M	M	M
Central Bank Balance Sheet	12/17	1/18	M	M	M
Consolidated Balance Sheet of the Banking System	12/17	1/18	M	M	M
Interest Rates[2]	12/17	1/18	M	M	M
Consumer Price Index	12/17	1/18	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3]—General Government[4]	2017:Q3	12/17	Q	Q	Q
Revenue, Expenditure, Balance and Composition of Financing[3]—Central Government[5]	11/17	12/17	M	M	M
Stock of Central Government Debt	11/17	12/17	M	M	M
External Current Account Balance	9/17	12/17	M	M	M
Exports and Imports of Goods and Services	9/17	12/17	M	M	M
GDP/GNP	2017:Q3	11/17	Q	Q	Q
Gross External Debt	2017:Q3	12/17	Q	Q	Q

[1] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.

[2] Both market-based and officially-determined, including discount rates, money market rates, and rates on treasury bills, notes and bonds.

[3] Foreign, domestic bank, and domestic nonbank financing.

[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds), and state and local governments.

[5] This information is provided on a budget-accounting basis (not on a national accounts basis).

[6] Daily (D), weekly (W), monthly (M), quarterly (Q), annually (A), irregular (I), and not available (NA)