

Economic projections for Belgium – Spring 2007

Introduction

In 2006, the Belgian economy benefited greatly from a buoyant environment. GDP grew by 3 p.c. in volume and, according to the NAI, over 46,000 jobs were created in net terms, the best performance since 2000. This favourable situation persisted in the initial months of 2007. Global activity continued to grow strongly, bolstered in particular by the emerging economies. However, the sources of growth are now more balanced on either side of the Atlantic, as a slowdown in the United States coincided with a marked strengthening in the euro area. In Germany, in particular, contrary to what had been feared six months ago, the three percentage point increase in the rate of VAT at the beginning of 2007 appears to have had hardly any adverse impact on growth, or at least the effects have been offset by the general economic revival. In a context of less accommodating monetary policies, inflation remained under control in the majority of economic regions, partly as a result of the easing of oil prices between August 2006 and January 2007.

The positive growth differential which appeared in relation to the United States contributed to the euro's appreciation against the dollar, and long-term interest rates in Europe have also edged upwards in the past twelve months. Nonetheless, the high level of the recent results of Belgian business and household surveys point to a continuing favourable economic outlook in the short term. The spring 2007 economic projections, which relate to the current year and 2008, are therefore issued in an environment which initially appears to be slightly more favourable than had been predicted six months earlier, at the time of the autumn 2006 projections⁽¹⁾.

Produced as part of a biannual exercise by the Eurosystem central banks – the results for the euro area being obtained by aggregating the results for the various national economies⁽²⁾ – these projections for Belgium are prepared by the Bank on the basis of a set of common assumptions concerning the international environment and movements in interest rates, exchange rates and commodity prices. They also depend on assumptions specific to the Belgian economy as regards variables which are to a large extent influenced by the discretionary action of the economic agents. That applies, for example, to the wage agreements resulting from negotiations between the social partners, and to government decisions on the budget.

For this exercise, an increase of 5 p.c. was assumed for hourly labour costs in the private sector over 2007 and 2008 together. That corresponds to the indicative norm of the central agreement, in the absence of full information on the outcome of the negotiations conducted at joint committee level.

The figures for public finances, in the case of both revenue and expenditure, take account of only those measures which have already been introduced and of recent actual figures. Over the longer term, they result mainly from the endogenous effect of the macroeconomic environment on the revenue, and an expenditure pattern based on past developments. New government measures to be adopted in the months ahead were not taken into account in this projection exercise. In some circumstances, they could in turn affect the projections for the economy as a whole.

(1) NBB (2006), "Economic projections for Belgium – Autumn 2006", Economic Review, December 2006.

(2) The projections for the euro area were published in the ECB's June Monthly Bulletin.

The first section deals with the international environment. It summarises the Eurosystem projections for the euro area and presents the principal common assumptions. The next three sections go into more detail on the recent situation and the projections for the national economy, dealing respectively with activity, employment and the main expenditure components (section 2) – which, in accordance with Eurosystem practice, are presented without taking account of specific seasonal effects and the impact of irregularities in the calendar –, prices and labour costs (section 3), and the public finance figures (section 4). Finally, the main risks relating to the projections are discussed in the last section, which also contains a summary of the results obtained by other institutions.

The projections for Belgium were drawn up on the basis of information available as at 24 May 2007.

1. International environment

1.1 The world economy

The world economy produced exceptionally strong growth in 2006, while inflation remained under control. World GDP expanded by 5.2 p.c., a growth rate almost equaling the 2004 record. This dynamism was due mainly to the very strong expansion recorded by the emerging countries, especially China, India, Russia and a number of Central and East European countries. Taken as a group, the industrialised countries also produced stronger growth in 2006 than in 2005. While economic growth began to slow down in the United States in the second quarter, the other industrialised countries continued to record robust expansion so that the business cycles displayed a more similar pattern across the main economic regions. The vigour of the global economy coincided with very strong growth of world trade, with a rise of some 8.5 p.c. in 2006. The business survey indicators and the available statistics also show that economic activity remained buoyant in the initial months of 2007.

The persistence of very high prices for oil and other commodities in 2006 therefore did little to curb world growth. Having peaked at 78.5 US dollars at the beginning of August, the price of a barrel of Brent crude dropped to an average of 54.3 dollars in January 2007. Nonetheless, it has since risen again, reaching 67.6 dollars in April. The high level of oil prices is due mainly to the vigour of demand and the shortage of spare capacity in both production and refining, while the price volatility chiefly reflects variations in the geopolitical situation and climatic conditions. Prices of industrial commodities increased

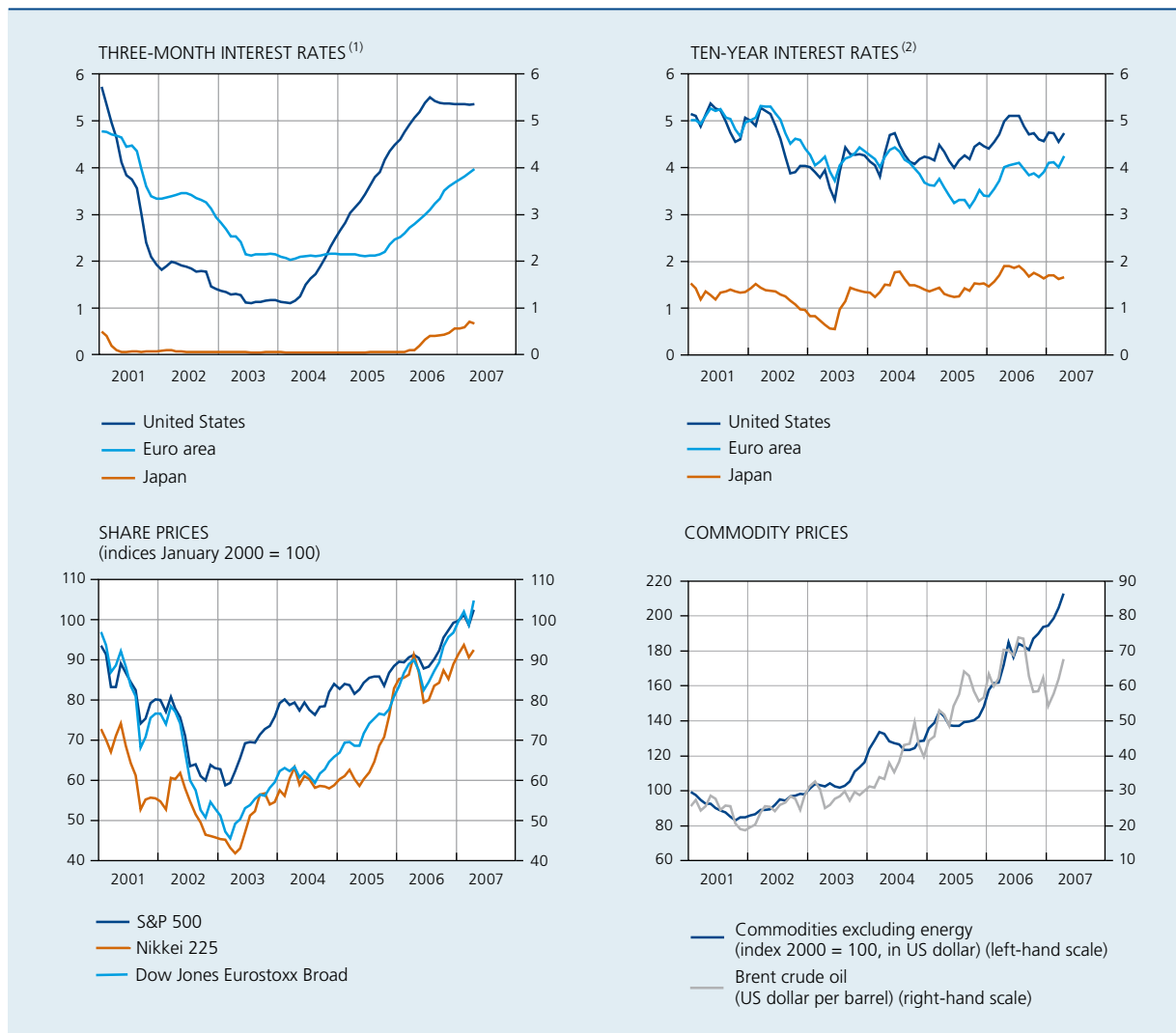
almost constantly in 2006 and the initial months of 2007, driven by very sustained demand. The prices of most commodities are likely to remain high overall in 2007 and 2008.

In response to the increasing risk of inflation, the main central banks raised their key rates in 2006. In the United States, the progressive tightening of monetary policy which had begun in June 2004 continued in the first half of 2006. On 29 June, the target for the federal funds rate was increased to 5.25 p.c. Although the pace of growth in the United States has since slackened considerably, the Federal Reserve has not eased its policy, considering that it could not do so on account of the inflation risk. In the euro area, the ECB Governing Council raised the Eurosystem's key rate in seven successive stages from 2 p.c. in November 2005 to 3.75 p.c. on 8 March 2007, the latest rise on the closing date of the projections⁽¹⁾. In 2006, in the context of waning deflation in Japan, the Bank of Japan ended its policy of granting abundant liquidity at zero interest. It increased its key rate on 14 July 2006 and 21 February 2007, by 25 basis points on each occasion, bringing it to 0.5 p.c. Finally, since mid 2006, the Bank of England has raised its key rate on four occasions, by 25 basis points at a time, bringing it to 5.5 p.c. on 10 May 2007.

Despite the tighter monetary policy, financing conditions remained favourable overall in 2006, and that combined with the substantial corporate profits and the improved labour market situation supported economic activity. Long-term interest rates also remained at relatively low levels, on average, in 2006 and in the initial months of 2007, although they were slightly higher than the rates prevailing in 2005. The main reason lies in the decline of the risk premium included in long-term interest rates, which partly negated the effect of the rise in short-term interest rates. The premiums incorporated in the yields on riskier bonds issued by the governments of emerging countries and by companies also remained exceptionally small. That is probably due to some extent to increased macroeconomic stability, though other factors are also involved, such as strong demand for investments on the part of Asian central banks and oil-exporting countries. The low level of long-term interest rates, plus the vigour of economic growth and the high level of corporate profits, also underpinned the rise in share prices. Despite a temporary correction in May and June 2006, the Dow Jones Eurostoxx index, in particular, recorded a significant rise of almost 30 p.c. between December 2005 and April 2007. Conditions for raising external finance via share issues were therefore favourable once again in 2006.

(1) On 6 June 2007, the Governing Council raised the key rate to 4 p.c.

CHART 1 FINANCIAL AND COMMODITY MARKET DEVELOPMENTS
(monthly averages)



Sources: ECB, HWWA.

(1) Interest on three-month interbank deposits.

(2) Yield on ten-year government bonds (benchmark loans).

The outlook for the global economy therefore appears positive in 2007 and in 2008. According to the European Commission, after a very strong result in 2006 the pace of global GDP growth is expected to dip slightly, dropping to 4.8 p.c. in 2007 and 2008, to equal the 2005 figure. Inflation should remain under control, two factors being the heightened international competition caused by globalisation and the modest rise in unit labour costs.

Although the pace is expected to slacken slightly compared to 2006, the emerging countries of Asia and Russia are likely to remain the main engine of global economic growth in 2007 and 2008. Again slightly lower than the

2006 figure, the expansion of activity is also predicted to be very sustained in the twelve new EU Member States, stimulated by private consumption, housing construction and foreign direct investment. These countries should therefore continue the process of catching up with the euro area.

Most of the industrialised countries not forming part of the euro area are also likely to see robust growth in 2007 and 2008. The outlook for the United States is the main exception to this positive picture: the substantial correction in progress on the housing market is likely to have an even greater impact in 2007 than in 2006. Although there is great uncertainty surrounding the scale of that

TABLE 1 PROJECTIONS FOR THE MAIN ECONOMIC REGIONS EXCLUDING THE EURO AREA

(percentage changes compared to the previous year, unless otherwise stated)

	2006	2007	2008
	Actual	Projections	
GDP in volume			
United States	3.3	2.2	2.7
Japan	2.2	2.3	2.1
United Kingdom	2.8	2.8	2.5
Twelve new EU Member States ⁽¹⁾	6.3	5.7	5.3
Asia (excluding Japan)	8.7	8.3	8.4
China	10.7	10.5	10.4
India	8.7	7.6	7.4
Russia	6.7	6.8	6.5
World	5.2	4.8	4.8
<i>p.m. World trade</i>	<i>8½</i>	<i>7¾</i>	<i>7¾</i>
Inflation⁽²⁾			
United States	3.2	2.3	1.9
Japan	0.2	0.0	0.4
United Kingdom	2.3	2.3	2.0
Twelve new EU Member States ⁽¹⁾	3.2	3.4	3.2
Unemployment rate⁽³⁾			
United States	4.6	4.7	5.0
Japan	4.1	4.1	4.2
United Kingdom	5.3	5.0	4.9
Twelve new EU Member States ⁽¹⁾	9.9	8.7	7.8

Sources: EC (spring forecasts, May 2007) and own calculations.

(1) Weighted averages according to relative size of their GDP in 2006.

(2) Consumer price index.

(3) Percentages of the labour force.

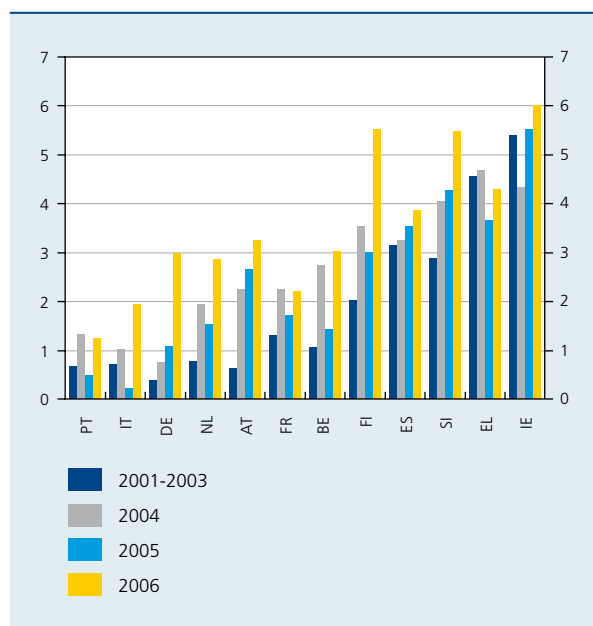
correction, the general opinion is still that its impact on the rest of the US economy will be limited; growth should therefore pick up gradually in 2008, once the housing market correction has disappeared. In that case, the contagion affecting other economies will also be slight. In the other main industrialised countries outside the euro area, such as Japan and the United Kingdom, the expansion of activity should also be steady in 2007 and 2008. In the first year, it should still be sustained mainly by corporate investment, but in 2008 the other components of domestic demand – consumption and investment in housing – should also make a large positive contribution. The expected combination of a continuing growth slowdown in the United States and persistently strong growth in most other industrialised countries outside the

euro area is set to reduce growth differentials between the industrialised countries.

1.2 Eurosystem projections for the euro area

Having lagged behind the vigorous global economy in previous years, the euro area joined in the general trend in 2006. Economic activity expanded strongly, by 2.9 p.c., the highest rate since 2000, despite the high oil prices, the slower pace of growth in the United States and the euro's appreciation. The euro area therefore seems to have been more resilient to external adverse shocks than in the past. Not only did GDP growth show a marked acceleration, it also became more broadly based.

CHART 2 GDP GROWTH IN THE EURO AREA COUNTRIES⁽¹⁾
(percentage changes compared to the previous year)



Source : EC.

(1) Excluding Luxembourg; calendar adjusted data.

First, investment expanded strongly, underpinned by the favourable outlook for demand, rising capacity utilisation rates, high corporate profits and continuing favourable financing conditions. Next, private consumption also revived. Although wage moderation and high oil prices continued to weigh on household purchasing power, the improvement in the labour market situation boosted

consumption. Finally, in contrast to 2005, net exports also made a positive contribution to GDP growth in 2006.

The countries making up the euro area also presented a more balanced picture. In particular, growth differentials between the large countries became narrower, following the marked revival of the German economy, and to a lesser extent the Italian economy, which had remained in the doldrums in 2004 and 2005. The renewed vigour seen in these two countries was accompanied by a marked improvement in the labour market situation. Increased momentum was also evident in the other euro area countries in 2006. However, the very strong GDP growth recorded in Finland must be viewed partly as a recovery following a slowdown in 2005.

According to the initial information available, the consolidation of economic activity in the euro area continued at the beginning of 2007. In particular, it seems in retrospect that fears of a slowdown in Germany, due to the increase in that country's VAT rate on 1 January, were exaggerated. Although the VAT increase undeniably curbed German private consumption in the first few months of the year, the damage to both consumer and business confidence was only very temporary. The expansion of domestic demand and the significant improvement in the labour market situation seem to be reinforcing one another, and have more than offset the adverse impact of the rise in VAT, resulting in consolidation after the strong recovery seen in 2006.

According to the Eurosystem projections, growth should therefore remain vigorous in the euro area in 2007 and 2008. Despite the expected slight slowing of world

TABLE 2 EUROSISTEM PROJECTIONS
(percentage changes compared to the previous year)

	Euro area			<i>p.m. Belgium</i>		
	2006	2007	2008	2006	2007	2008
Inflation (HICP)	2.2	1.8 – 2.2	1.4 – 2.6	2.3	1.6	1.8
GDP in volume	2.9	2.3 – 2.9	1.8 – 2.8	3.0	2.5	2.2
of which:						
Private consumption	1.8	1.7 – 2.1	1.6 – 2.8	2.5	1.9	1.9
Public consumption	2.0	1.0 – 2.0	1.0 – 2.0	1.4	2.0	2.3
Investment	5.1	3.8 – 6.0	1.9 – 5.1	5.7	3.8	3.7
Exports	8.5	4.8 – 7.6	4.0 – 7.2	3.6	5.7	4.6
Imports	8.0	4.6 – 8.0	3.9 – 7.3	4.6	5.4	4.6

Sources : ECB, NBB.

growth, the persistence of high prices for most commodities, and the delayed impact of the recent appreciation of the euro, the external environment should remain favourable overall to activity in the euro area. The steady support of export demand should gradually spread to domestic demand. The investment revival which began in 2006 is expected to continue in the context of high corporate profits and continuing favourable financing conditions. The labour market situation should gradually improve, bolstering private consumption via a rise in disposable income. Average GDP growth in volume terms, which had peaked at 2.9 p.c. in 2006, is projected at between 2.3 and 2.9 p.c. in 2007 and between 1.8 and 2.8 p.c. in 2008.

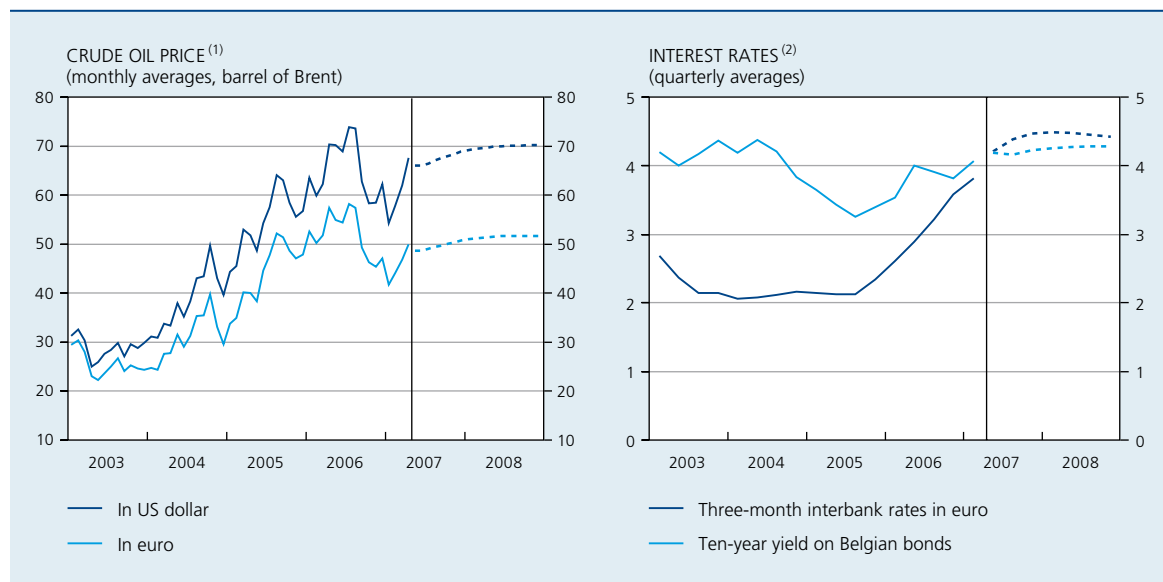
As in 2005, inflation measured by the HICP averaged 2.2 p.c. in 2006, the main factor being the steep rise in oil prices. Conversely, the energy component of the HICP is likely to have a moderating effect on inflation in 2007 and should be more or less neutral in 2008. However, this effect will be partly offset in 2007 by the upward pressure of indirect taxes, particularly in Germany, and labour costs. Those costs are expected to continue accelerating slightly in 2008, but the effect on inflation should be more or less counterbalanced by a smaller increase in corporate profit margins. Inflation should average between 1.8 and 2.2 p.c. in 2007 and between 1.4 and 2.6 p.c. in 2008.

Box – Eurosystem assumptions

The Eurosystem's economic projections for the euro area and the corresponding projections for Belgium are based on the following technical assumptions:

- The interest rates are based on market expectations. The three-month interbank rate in euro stood at around 4 p.c. when the projections were prepared. According to market expectations, it is set to increase to an annual average of 4.2 p.c. in 2007 and 4.5 p.c. in 2008. The benchmark ten-year interest rate for Belgium is projected at 4.2 p.c. in 2007 and 4.3 p.c. in 2008.
- The bilateral euro exchange rates are kept constant at their value as at mid May 2007, namely 1.36 US dollar to the euro.

ASSUMPTIONS CONCERNING THE MOVEMENT IN OIL PRICES AND INTEREST RATES



Source : ECB.

(1) Actual figures up to April 2007, assumption from May 2007.

(2) Actual figures up to the first quarter of 2007, assumption from the second quarter of 2007.

- In accordance with the movement in implicit prices reflected in forward contracts in the first half of May, global oil prices are expected to continue edging upwards during 2007, from around 66 dollars per barrel in the first half of May 2007. Taking an average over the year, Brent is forecast to cost 65 dollars per barrel in 2007 and 69.9 dollars in 2008, compared to 65.4 dollars in 2006.

The expected developments in world trade and the results of the projections for the euro area's partners concerning trade in goods and services can be used to assess the external conditions for the Belgian economy. The exceptionally vigorous volume growth of the export markets in 2006, calculated as the weighted sum of imports of our trading partners, is unlikely to be equalled in the next two years. However, the export markets should continue to expand strongly, by 5.9 p.c. in 2007 and 6.2 p.c. in 2008. The rise in competitors' export prices should be smaller than in 2006, at only 0.2 p.c. in 2007 and 1.2 p.c. in 2008, mainly owing to the expected movement in competitors' prices for exports to countries outside the euro area.

ASSUMPTIONS UNDERLYING THE EUROSISTEM PROJECTIONS

	2006	2007	2008
		(annual averages)	
Three-month interbank rates in euro	3.1	4.2	4.5
Ten-year bond yields in Belgium	3.8	4.2	4.3
Euro exchange rate against the US dollar	1.26	1.34	1.36
Oil price (US dollar per barrel)	65.4	65.0	69.9
		(percentage changes)	
Export markets relevant to Belgium	9.0	5.9	6.2
Export competitors' prices	2.5	0.2	1.2
of which: competitors on euro area markets	2.3	1.6	1.6

Source: ECB.

2. Activity, employment and demand in Belgium

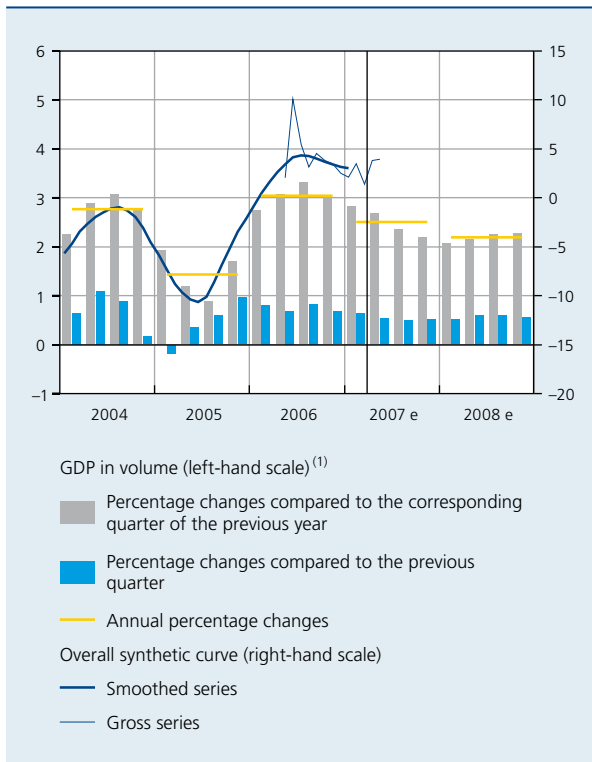
2.1 Activity and employment

In parallel with the recovery in the euro area, economic activity expanded by 3 p.c. in Belgium in 2006. This was the highest growth rate for six years and was also well above the potential growth rate. The sustained recovery began in late 2005 and produced steady growth of between 0.7 and 0.8 p.c. per quarter throughout 2006. However, in year-on-year terms, a very modest slowdown has been apparent since the third quarter of 2006.

This performance was accompanied by a marked restoration of business confidence. The Bank's overall business survey indicator peaked in mid 2006 and has since remained at a high level. While exports were initially weaker compared to the dynamism of the export markets, the recovery apparent in 2006 was based mainly on domestic demand, underpinned by a further increase in investment growth and a notable improvement of the labour market.

The persistent buoyancy of business confidence and the favourable response of the labour market indicate that the recovery has become more sustainable in recent months, and more broadly based, a situation also seen in the euro area. For 2007, the GDP growth projection for Belgium has therefore been upgraded by 0.4 percentage

CHART 3 ACTIVITY AND BUSINESS SURVEY INDICATOR
(seasonally adjusted data)

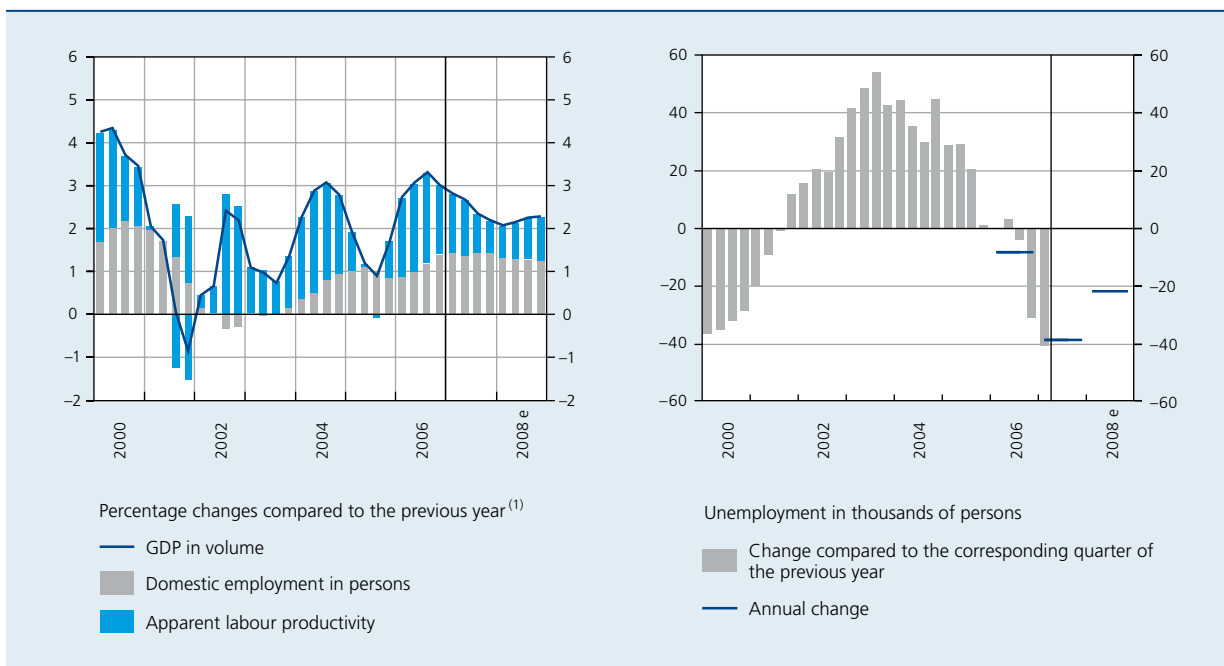


Sources : NAI, NBB.
(1) Calendar adjusted data.

point to 2.5 p.c., as the slowdown expected during the year is proving to be less marked than predicted by the autumn 2006 projections. Growth should be based on both domestic and foreign demand. It is set to continue at 2.2 p.c. in 2008, which is close to the potential level. The recent cyclical upswing considerably augmented the economy's supply capacity so that potential growth should have risen somewhat compared to the low point in 2003-2004.

The employment growth rate is in fact more sustained than at the time of previous recoveries, rising from an average of 0.2 p.c. per quarter in 2005 to 0.3-0.4 p.c. in 2006. Altogether, the number of jobs increased by 46,000 units last year, propelled by the expansion of activity, but also by the increase in net job creation due to the service voucher system. The biggest increases were seen in construction and in the branches comprising financial institutions in the broad sense and business services, while job losses slowed down in manufacturing industry. According to the projections, some 115,000 additional jobs will be created in 2007-2008, encouraged – particularly in the first year – by the cyclical upswing in 2006, as employment usually takes time to respond to cyclical fluctuations in activity. The increase in per capita productivity, which had reached 1.9 p.c. in 2006, will therefore revert to an average of 1 p.c. in 2007 and 2008, compared to an average of 1.3 p.c. over the past ten years.

CHART 4 EMPLOYMENT AND UNEMPLOYMENT



Sources : NAI, NEMO, NBB.
(1) Data adjusted for seasonal and calendar effects.

TABLE 3 LABOUR SUPPLY AND DEMAND

(calendar adjusted data, annual averages; year-on-year changes in thousands of persons, unless otherwise stated)

	2004	2005	2006	2007 e	2008 e
Population of working age	30	44	49	43	33
Labour force	66	61	38	22	33
<i>p.m. Harmonised activity rate</i> ⁽¹⁾	65.9	66.7	66.5	66.4	66.5
National employment	27	41	46	60	55
<i>p.m. Harmonised employment rate</i> ⁽¹⁾	60.4	61.1	61.0	61.5	62.0
Frontier workers	1	0	0	0	0
Domestic employment	27	41	46	60	55
Self-employed	-1	7	8	8	6
Employees	27	34	38	52	49
Public sector	12	-2	4	0	3
Private sector	15	36	35	52	46
Unemployed job-seekers	38	20	-8	-39	-22
<i>p.m. Harmonised unemployment rate</i> ⁽²⁾	8.4	8.4	8.2	7.6	7.2

Sources: EC, NAI, NEMO, NBB.

(1) Percentages of the population of working age (15-64 years).

(2) Percentages of the labour force. This series corresponds to the results of the labour force survey, adjusted monthly in accordance with the Eurostat methodology, using national administrative data.

With an activity rate more or less stable at 66.5 p.c., the increase in the labour supply should be only 55,000 units over the period 2007-2008, following slower growth in the population of working age than in the preceding two years. The number of jobs created over the projection period is therefore significantly greater than the expected increase in the labour force, so that the decline in unemployment which began in 2006 should continue. Unemployment is expected to fall by around 60,000 units, the largest cumulative decline in any two-year period since 1999-2000. The harmonised unemployment rate, expressed as a percentage of the labour force, should fall from 8.2 p.c. in 2006 to 7.2 p.c. in 2008, while the employment rate, calculated as the ratio between the number of jobs and the population of working age, should rise by 1 percentage point during the period covered by the projections, to reach 62 p.c. in 2008.

2.2 Expected developments in the main expenditure categories

In 2006, GDP growth had been sustained by unusually high contributions from domestic expenditure. In 2007 and 2008, these should revert to a more balanced level. Thus, the contribution of domestic expenditure excluding stocks is projected to fall from 2.8 percentage points in

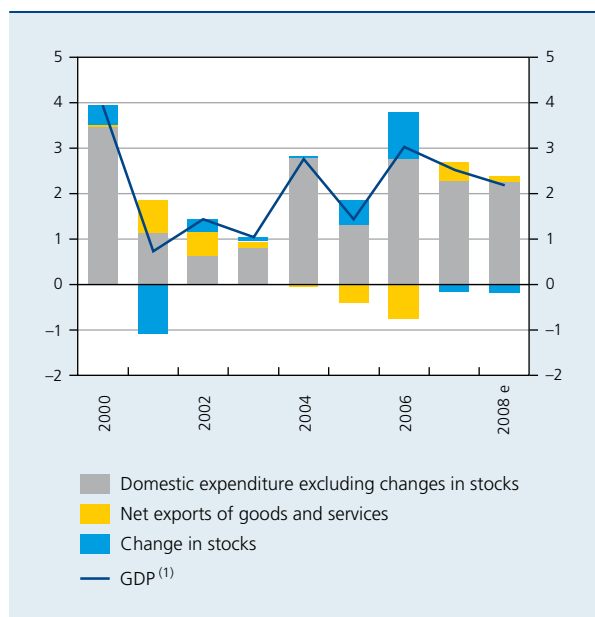
2006 to 2.3 percentage points in the ensuing two years, while the change in stocks is likely to curb GDP growth slightly over that period, after having increased it by 1 percentage point in 2006. Conversely, net exports of goods and services, which had increasingly depressed growth over the past three years, are expected to revive and make a positive contribution again in 2007 and 2008.

Private consumption is forecast to increase by 1.9 p.c. in both 2007 and 2008. While that is weaker than the sustained growth of 2.5 p.c. in 2006, the rise is nonetheless well above the average rate for the preceding five years. These developments largely reflect the movement in household purchasing power. In real terms, the increase in disposable income is expected to drop from an annual average of 3.2 p.c. in 2006 to 2.1 p.c. over the projection period. True, the curbing effect of inflation, measured by the deflator of private consumption, should ease somewhat over that period, but the nominal growth of household disposable income is expected to slow still more, declining from 5.3 p.c. in 2006 to 4.2 p.c. in 2007 and 3.6 p.c. in 2008.

Over the projection horizon, primary household income should be sustained by compensation of employees in the same way as in 2006. This is expected to result mainly from stronger expansion of employment, while the rise in

CHART 5 MAIN EXPENDITURE CATEGORIES

(calendar adjusted volume data; contribution to the change in GDP in percentage points, unless otherwise stated)



Sources: NAI, NBB.

(1) Annual percentage changes.

compensation per person will be less than in 2006. The slower pace of disposable income growth is therefore attributable primarily to the increase in net transfers by individuals to other sectors, especially taxes and contributions paid to the government. The movement in these transfers should become realigned with the growth of primary income, after having lagged behind in 2006 following the implementation of the last major phase of the tax reform which began in 2001. In 2007, disposable income should still benefit to a limited extent from the residual effects of the implementation of that reform and various new smaller-scale measures.

Over the period 2007-2008 as a whole, the growth rate of private consumption should therefore be fairly similar to that of real household disposable income. In a context in which households take a positive view of the general economic situation, as shown by the generally high level of the consumer confidence indicator, there should be hardly any further increase in the private savings ratio, which should hover around 14 p.c. of disposable income after a strong rise in 2006. The main reason for that increase was that households tend to smooth their consumption expenditure in order to offset wide temporary variations in the growth rate of their real disposable income, such as that which occurred in 2006.

TABLE 4 GROSS DISPOSABLE INCOME OF INDIVIDUALS, AT CURRENT PRICES

(percentage changes compared to the previous year, unless otherwise stated)

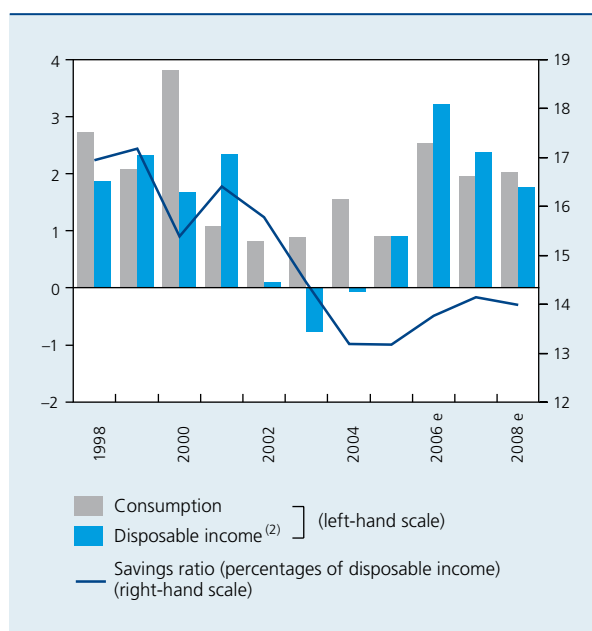
	2004	2005	2006 e	2007 e	2008 e
Gross primary income	2.3	3.6	4.3	4.0	3.6
of which:					
Wages and salaries	2.8	3.4	4.2	4.2	3.9
Compensation per person	2.0	2.4	3.1	2.7	2.5
Employment	0.8	1.0	1.1	1.5	1.4
Incomes other than wages and salaries	1.3	4.1	4.4	3.4	3.0
Current transfers ⁽¹⁾	2.2	2.8	-0.2	3.1	3.8
of which:					
Current taxes on income and assets	3.3	4.1	-0.2	3.4	4.2
Gross disposable income	2.4	3.8	5.3	4.2	3.6
<i>p.m. In real terms</i> ⁽²⁾	-0.1	0.9	3.2	2.4	1.8
Consumption expenditure	4.0	3.8	4.6	3.7	3.9
Savings ratio ⁽³⁾	13.2	13.2	13.8	14.1	14.0

Sources: NAI, NBB.

(1) These are net amounts, i.e. the difference between transfers received from other sectors and those paid to other sectors, excluding transfers in kind.

(2) Data deflated by the private final consumption expenditure deflator.

(3) Gross savings as a percentage of gross disposable income, these two aggregates including the net claims of households on pension funds.

CHART 6 CONSUMPTION, DISPOSABLE INCOME AND SAVINGS RATIO OF INDIVIDUALS(percentage changes in volume compared to the previous year⁽¹⁾, unless otherwise stated)

Sources: NAI, NBB.

(1) Non calendar adjusted data.

(2) Data deflated by the private final consumption expenditure deflator.

With an increase of 5.8 p.c. in 2007 and 3 p.c. in 2008, the rate of expansion of household investment in housing should once again outpace the growth of real disposable income. The easing of property prices on the secondary market which had already begun in 2006 should continue over the next two years, gradually reining in the growth of investment in housing. Conversely, the relatively low level of long-term interest rates is likely to remain a supporting factor.

The growth of consumption expenditure by general government is projected to rise gradually from 1.4 p.c. in 2006 to 2 p.c. in 2007 and 2.3 p.c. in 2008. Following an unusually small increase in health care expenditure in 2005 and 2006, this acceleration can be regarded as a return to the trend growth rate.

On the other hand, public investment is set to grow by only 0.9 p.c. in 2007, compared to modest growth of 1.3 p.c. in 2006. However, these developments are greatly influenced by sales of public buildings, which – according to the accounting conventions – are regarded as disinvestment by general government. In 2006, these transactions represented around 575 million euro. Further property sales should bring in about 200 million euro in 2007. Disregarding the impact of these sales, public investment increased by 10.2 p.c. in 2006 and should see a 5.5 p.c.

TABLE 5 GDP AND MAIN EXPENDITURE CATEGORIES

(calendar adjusted volume data; percentage changes compared to the previous year, unless otherwise stated)

	2004	2005	2006	2007 e	2008 e
Consumption expenditure of individuals	1.4	1.1	2.5	1.9	1.9
Consumption expenditure of general government	2.1	-0.6	1.4	2.0	2.3
Gross fixed capital formation	8.1	4.3	5.7	3.8	3.7
Housing	9.0	3.4	4.7	5.8	3.0
General government	2.9	13.6	1.3	0.9	4.2
Enterprises	8.4	3.4	6.6	3.5	3.8
Change in stocks ⁽¹⁾	0.1	0.5	1.0	-0.2	-0.2
<i>p.m.</i> Total domestic expenditure	3.0	1.9	3.9	2.1	2.1
Net exports of goods and services ⁽¹⁾	-0.1	-0.4	-0.8	0.4	0.1
Exports of goods and services	5.9	3.1	3.6	5.7	4.6
Imports of goods and services	6.3	3.8	4.6	5.4	4.6
GDP	2.8	1.4	3.0	2.5	2.2

Sources: NAI, NBB.

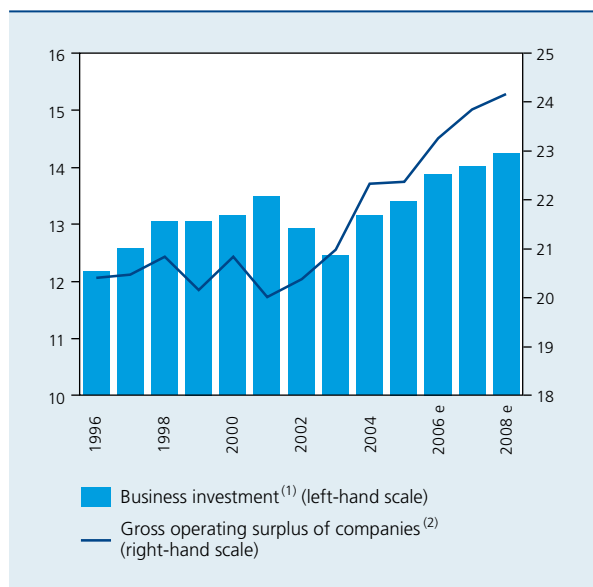
(1) Contribution to the change in GDP.

decline in volume in 2007. This largely reflects the usual profile of local authority investment during a municipal and provincial election year and the year that follows. Although local authority investment is likely to diminish further in 2008, total public investment should expand by 4.2 p.c., though that rate exhibits a slight upward bias as a result of sales of public buildings in 2007.

Enterprises are expected to maintain the steady expansion of their fixed capital investment, continuing the trend which began in 2004 after two years of decline. Investments should expand by 3.5 p.c. in 2007 and 3.8 p.c. in 2008, slightly below the rate recorded from 2004 to 2006 but still outpacing GDP growth. This means that the investment ratio should rise from 12.5 p.c. of GDP in 2003 to 14.2 p.c. in 2008.

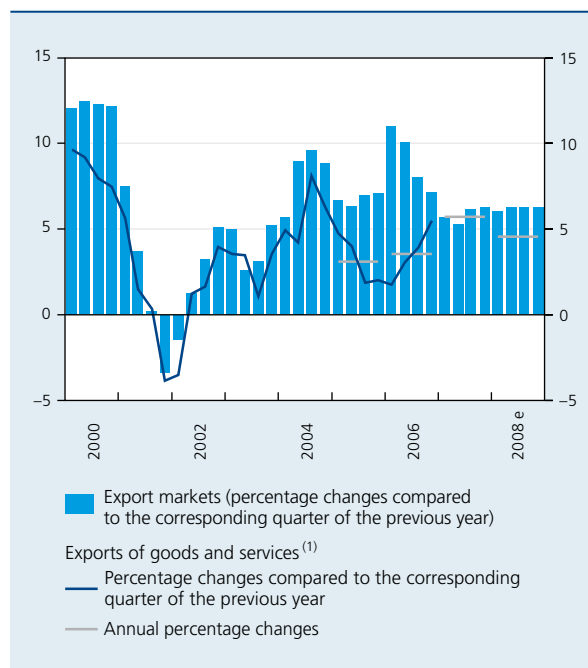
The growth of business investment should be supported mainly by the consolidation of demand prospects in a context in which the economic agents seem to regard the risks to the overall economic environment as relatively minor. Moreover, financing opportunities should remain favourable. In fact, enterprises have substantial funds, generated by a gross operating surplus which came to 23.3 p.c. of GDP in 2006 and should reach 24.2 p.c. in 2008. This further rise is attributable mainly to the sustained growth of the volume of sales, with profit margins

CHART 7 BUSINESS INVESTMENT AND GROSS OPERATING SURPLUS
(percentages of GDP)



Sources: NAI, NBB.
(1) Calendar adjusted volume data.
(2) Non calendar adjusted value data.

CHART 8 EXPORT MARKETS AND EXPORTS OF GOODS AND SERVICES
(seasonally adjusted volume data)



Sources: ECB, NAI, NBB.
(1) Calendar adjusted data.

also increasing, though more slowly than in previous years. Finally, the conditions for raising external finance, by borrowing or by share issues, are unlikely to hamper investment, even if the long-term interest rate were to reach 4.3 p.c. by the end of the period under consideration.

With an average growth rate of 3.6 p.c. in 2006, the rise in the volume of exports of goods and services fell far short of the expansion of the export markets, but the situation improved considerably during the year. The excellent results for the last quarter of 2006 are also part of the reason why export growth is predicted to reach 5.7 p.c. in 2007, a figure close to the expected growth of Belgium's export markets. This increased momentum should be most marked in the case of exports to partners in the euro area, largely reflecting the expected strengthening of that market. Most of the export markets outside the euro area should also see substantial growth, but price competition will be keener there. In 2008, however, the growth in the volume of Belgium's exports is forecast to dip to 4.6 p.c., so that Belgian producers will suffer further losses of market share, though the scale of those losses should be less than in the period 2004-2006, thanks to more competitive prices. Following the steep increases seen from 2004 to 2006, export prices should rise by only 1 p.c.

in 2007 and 2.1 p.c. in 2008, thus outpacing competitors' price increases to a less significant degree than in the past.

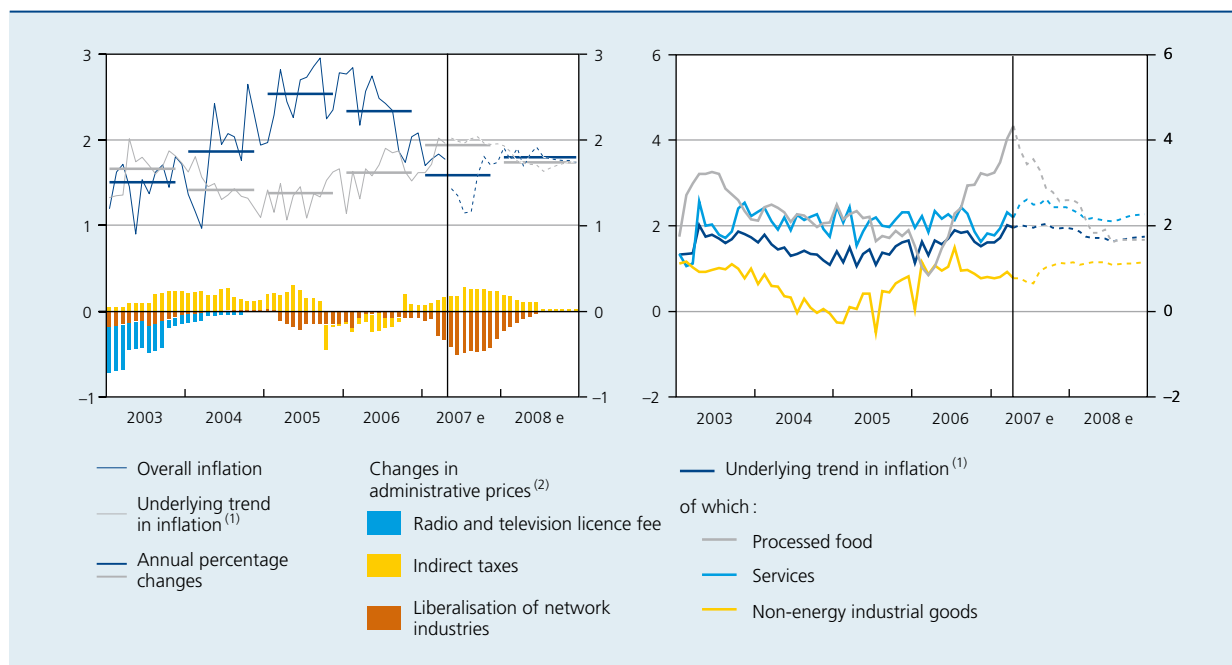
Attenuated by the slower rise in prices of energy and commodities, and by the recent appreciation of the euro, the predicted rise in import prices, of 0.3 and 1.9 p.c. in 2007 and in 2008 respectively, should be less than the rise in export prices. Thus, the improvement in the terms of trade which began in the second half of 2006 is expected to continue in 2007 and 2008. The growth in the volume of imports is forecast to rise from 4.6 p.c. in 2006 to 5.4 p.c. in 2007, before subsiding to 4.6 p.c. in 2008. Net exports will therefore make a positive contribution to GDP growth in 2007 and in 2008, for the first time in four years.

According to these projections, the deterioration in the balance of payments current account which began in 2003 should have ended in 2006. Under the combined effects of more sustained growth in the volume of exports than imports and the improvement in the terms of trade, the current account balance should increase from 2 p.c. of GDP in 2006 to 2.7 p.c. in 2007 and 3 p.c. in 2008.

3. Prices and costs

In recent years, inflation in Belgium had been driven up by rising energy prices, keeping it at over 2 p.c. in 2005 and 2006, but in 2007, the energy component should exert a moderating effect. That is due in part to the movement in oil prices on the international markets. Having risen sharply in 2006, those prices are assumed to remain on average at the same level in 2007 as in the previous year. During the first half of the year, oil prices were actually below the levels prevailing twelve months earlier, producing a favourable base effect during that period; that effect is expected to wane subsequently. In addition, the liberalisation of the gas and electricity markets in Brussels and Wallonia and the new method of recording those prices in the consumer price index should exert strong downward pressure on the movement in energy prices in 2007. From now on, these changes should cause gas and electricity prices to adjust more speedily to international price movements; that is confirmed by the recent trend in the consumer price index which indeed shows these prices falling at the beginning of 2007. Although the exact impact of these changes on overall inflation is surrounded by some uncertainty, it is likely

CHART 9 INFLATION
(HICP – percentage changes compared to the corresponding period of the previous year)



Sources: EC, NBB.

(1) Measured by the HICP excluding energy and unprocessed food.

(2) Impact on overall inflation, in percentage points, of changes in prices associated with measures relating to the radio and television licence fee, changes in the rates charged in those network industries where liberalisation is farthest advanced, namely telecommunications, electricity and gas, and adjustments to indirect taxes.

to be -0.4 percentage point for the year as a whole. In parallel with the movement in the energy component, overall inflation should therefore show a marked fall, dropping from 2.3 p.c. in 2006 to 1.6 p.c. in 2007 before a moderate acceleration to 1.8 p.c. in 2008.

Unlike overall inflation, the underlying trend in inflation – which excludes the energy component and prices of unprocessed food – should maintain the rise which began in 2006 to reach 1.9 p.c. in 2007. In 2008, it should drop to 1.7 p.c., a figure similar to that for the overall HICP. Its movement over the period covered by the projections is due to changes in indirect taxation. Thus, the tobacco price increases – included in the processed food category – accelerated in the initial months of 2007, owing to an increase in excise duty. In addition, the levy on certain disposable products and packaging, planned to take effect in July 2007, should exert slight upward pressure on the underlying trend in inflation in both 2007 and 2008. The overall impact of the rise in indirect taxes on the underlying trend in inflation is estimated at 0.2 percentage point in 2007 and 0.1 percentage point in 2008. Without that effect, the underlying trend in inflation would therefore be relatively stable. That stability is also evident in the prices of services and non-energy industrial goods. Owing to

heightened competition – the corollary of globalisation – and to the euro's appreciation, the rate of increases in prices of non-energy industrial goods should accelerate only moderately, from 0.9 p.c. in 2006 to 1.1 p.c. in 2008. In line with the moderate trend in labour costs, the increases in services prices should accelerate very little, from 2.1 p.c. in 2006 to 2.2 p.c. in 2008.

As indicated by the GDP deflator, the rise in total costs of domestic origin incorporated in all goods and services produced, is expected to remain steady in 2007 at 2 p.c., before edging up to 2.1 p.c. in 2008. The contribution of labour costs should be slightly higher in the projection period, although that small increase is likely to be offset by a smaller contribution from the gross operating surplus. The proportion of wages should continue to decline, falling to 49.9 p.c. of GDP in 2008. Indirect taxes and subsidies are predicted to exert upward pressure on costs, mainly in 2008.

The growing contribution of labour costs to total costs of domestic origin reflects the acceleration of unit labour costs in the private sector, their increase rising from 1.1 p.c. in 2006 to 1.6 p.c. in 2007 and 2008. This growth is due solely to the slowing of labour productivity, resulting

TABLE 6 PRICE AND COST INDICATORS
(percentage changes compared to the previous year, unless otherwise stated)

	2004	2005	2006	2007 e	2008 e
HICP	1.9	2.5	2.3	1.6	1.8
<i>p.m. Impact of price changes in the network industries</i>	0.0	-0.1	-0.1	-0.4	-0.1
<i>p.m. Impact of changes in indirect taxes</i>	0.2	0.1	0.0	0.2	0.1
Health index	1.6	2.2	1.8	1.6	1.7
Underlying trend in inflation ⁽¹⁾	1.4	1.4	1.6	1.9	1.7
Deflators of the demand components and of GDP					
Imports	2.8	4.6	2.5	0.3	1.9
Exports	2.5	3.8	2.9	1.0	2.1
<i>p.m. Terms of trade</i>	-0.3	-0.7	0.4	0.7	0.2
Domestic demand	2.6	2.6	1.6	1.4	1.9
GDP	2.4	2.0	2.0	2.0	2.1
Costs of domestic origin per unit of value added (contributions to the change in the GDP deflator)					
Labour costs	-0.1	1.2	0.6	0.8	0.8
Gross operating surplus	1.8	0.8	1.5	1.2	1.1
Indirect taxes net of subsidies	0.7	0.1	-0.1	0.0	0.2
<i>p.m. Wage share (p.c. of GDP)</i>	50.6	50.8	50.3	50.1	49.9

Sources: EC, NAI, NBB.

(1) Measured by the HICP excluding energy and unprocessed food.

TABLE 7 LABOUR COSTS IN THE PRIVATE SECTOR

(calendar adjusted data; percentage changes compared to the previous year, unless otherwise stated)

	2004	2005	2006	2007 e	2008 e
Labour costs per hour worked	2.4	2.2	2.7	2.4	2.6
Employers' social contributions ⁽¹⁾	-0.5	-0.3	0.0	-0.2	-0.2
Gross wages	2.8	2.5	2.7	2.6	2.8
of which: indexations	1.4	2.1	1.8	1.7	1.6
Labour productivity ⁽²⁾	2.9	0.6	1.6	0.8	0.9
Unit labour costs	-0.4	1.5	1.1	1.6	1.6

Sources: FPS Employment, Labour and Social Dialogue; NAI; NBB.

(1) Contribution to the change in labour costs following the adjustments to the implicit contribution rates, percentage points.

(2) Value added, in volume, per hour worked by employees and self-employed persons.

from the marked expansion in employment in the private sector. Expressed per hour worked, the growth of labour costs should in fact decline slightly compared to 2006, from 2.7 p.c. to 2.4 p.c. in 2007 and 2.6 p.c. in 2008.

These estimates are based on the assumption of a cumulative 5 p.c. increase in hourly labour costs in the private sector. In the absence of information on the outcome of the wage negotiations conducted by the various sectoral joint committees, it corresponds to the indicative norm of the central agreement for the period 2007-2008. Noting that a handicap, estimated at 1.5 p.c. by the Secretariat of the Central Economic Council, had developed over the preceding ten years, the social partners had decided under this agreement to set a norm which was 0.5 percentage point lower than the average increase in hourly labour costs currently forecast in the three main neighbouring countries.

The movement in employers' social contributions is expected to attenuate the growth of labour costs by -0.2 percentage point each year. That includes the reductions introduced pursuant to the generation pact concluded in 2005, granted for the employment of young workers from July 2006 and for workers aged over 50 from April 2007. Apart from the cuts in contributions, firms will also benefit from the increase in the abatements introduced since 2004 for shift work and night work and, from October 2007, the general rebate on the payroll tax, equivalent to 0.15 p.c. of labour costs. According to the national accounts conventions, these measures are regarded as subsidies and are therefore not included in the recorded movement in labour costs.

According to the current projections, the effect of the automatic wage indexation based on the movement in the health index of consumer prices will total 3.4 p.c. over the two years.

4. Public finances

4.1 Overall balance

In 2006, the Belgian government recorded a budget surplus of 0.2 p.c. of GDP. In the macroeconomic context described above, the general government accounts are expected to be in deficit from 2007, although those deficits should be limited to only 0.1 and 0.2 p.c. of GDP respectively in 2007 and 2008. It should be noted that these projections take account only of budget measures which have already been announced and specified in sufficient detail.

The movement in the general government budget balance is due to four factors, namely the fluctuation in interest charges, the business cycle, the influence of temporary factors, and finally, the movement in the structural primary balance.

General government interest charges should continue to decline between 2006 and 2008 by around 0.3 p.c. of GDP. Although the projections are based on rising market rates, the average implicit rate applicable to the public debt should remain relatively stable. That is due to the small proportion of short-term debt securities and the fact that it is still possible for long-term liabilities to be refinanced at lower rates. The decline in interest charges

TABLE 8 GENERAL GOVERNMENT ACCOUNTS⁽¹⁾(percentages of GDP; according to the view taken by Eurostat⁽²⁾, unless otherwise stated)

	2004	2005	2006	2007 e	2008 e
Revenue	49.2	50.0	49.2	48.4	48.2
of which: fiscal and parafiscal revenue	44.4	44.8	44.3	43.7	43.5
Primary expenditure	44.5	47.9	44.9	44.6	44.5
Primary balance	4.7	2.0	4.3	3.8	3.7
Interest charges	4.7	4.3	4.1	3.9	3.8
Financing balance	0.0	-2.3	0.2	-0.1	-0.2
Changes in the financing balance		-2.2	2.5	-0.3	-0.1
due to changes in					
interest charges		0.4	0.2	0.2	0.1
cyclical component ⁽³⁾		-0.7	0.5	0.4	0.2
GDP growth		-0.6	0.5	0.2	0.0
composition effects		-0.1	-0.1	0.2	0.2
non-recurrent factors		-2.8	2.7	-0.5	-0.3
structural primary balance ⁽⁴⁾		0.9	-0.9	-0.4	0.0
<i>p.m. Financing balance according to the view taken by the NAI⁽²⁾</i>	<i>0.0</i>	<i>0.1</i>	<i>0.2</i>	<i>-0.2</i>	<i>-0.2</i>
<i>p.m. Stability programme targets</i>	<i>0.0</i>	<i>0.0</i>	<i>0.0</i>	<i>0.3</i>	<i>0.5</i>

Sources: EC, NAI, NBB.

(1) According to the methodology used in the excessive deficit procedure (EDP). This methodology differs from that of the ESA 95 which was adjusted in 2001 to exclude from the calculation of the financing balance and interest charges the net interest gains on certain financial transactions, such as swaps and forward rate agreements (FRAs).

(2) According to the view taken by the NAI, the Railway Infrastructure Fund (RIF), set up in the context of the BNRC restructuring on 1 January 2005, comes under the non-financial corporations sector. According to the view taken by Eurostat, that Fund forms part of the general government sector and the assumption of the BNRC debt has to be recorded as a capital transfer from that sector to the non-financial corporations sector.

(3) According to the methodology described in Bouthevillain C., Ph. Cour-Thimann, G. van den Dool, P. Hernández de Cos, G. Langenus, M. Mohr, S. Momigliano and M. Tujula (2001), *Cyclically adjusted balances: an alternative approach*, ECB Working Paper Series, n° 77 (September). A less technical description of this methodology may be found in Box 6 *Cyclically adjusted budget balances: calculation method used by the ESCB* in the NBB Report 2003 (Part 1), p. 83-84.

(4) Balance adjusted for cyclical and non-recurrent factors.

is therefore due exclusively to the gradual reduction of the public debt.

The business cycle is also expected to have a favourable impact on the financing balance. Activity looks set to continue expanding strongly in 2007, outpacing the trend growth rate. Moreover, the composition of GDP is likely to be favourable to public finances. Overall, the business cycle should improve the financing balance by 0.6 p.c. of GDP over the period considered.

Furthermore, the projections assume the gradual disappearance of the non-recurrent factors. In 2006, they had inflated the budget balance by 0.7 p.c. of GDP, essentially following the sale of real estate and the structural acceleration of the corporate income tax assessments. In 2007, the impact of non-recurrent factors is estimated at 0.2 p.c. of GDP. Further real estate sales should raise 200 million euro. In addition, this year's budget balance would benefit from the favourable influence of the tax

regularisation operation launched in 2006. Moreover, it is temporarily more advantageous for companies to distribute or invest certain tax-free reserves. The timing of the collection of social contributions on holiday pay on termination of contracts of employment has also been brought forward. Finally, public authorities are expected to securitise and sell off tax arrears in 2007⁽¹⁾. This new operation should bring in an estimated 150 million euro. However, the net impact of the securitisation on the 2007 budget balance will be negative: the operations conducted in 2005 and 2006 led to a fall in revenue, since when the arrears concerned are collected, they accrue to the buyers of the underlying securities. For 2008, the estimates take account only of the negative effects of the securitisation operations on tax revenues in that year.

(1) Eurostat will specify how securitisation operations conducted by public authorities are to be treated.

Adjusted for non-recurrent and cyclical factors, the primary surplus is projected to decline by 0.4 p.c. of GDP between 2006 and 2008. That decline is due partly to the fact that, in view of the relatively low level of advance payments in the initial months of 2007, corporate income tax this year is likely to grow significantly more slowly than the gross operating surplus of companies. Moreover, the projections also point to a further easing of structural fiscal policy.

The difference in relation to the surplus of 0.3 p.c. of GDP planned for 2007 under the latest stability programme is due to various factors. First, the revenue and expenditure estimates are different in some cases. That applies mainly to corporate income tax, for which the expected growth is more modest than in the budget assumptions. Also, in accordance with the ESCB methodology, the projections take no account of budget measures which are not yet sufficiently detailed, as in the case of the intention to take over the first pillar pension liabilities of companies in return for a one-off capital transfer, which should generate revenue of 500 million euro. For the same reason, only one-third of the assumed proceeds of the sales of real estate is taken into account.

4.2 Revenue

General government revenues expressed as percentages of GDP are set to decline in both 2007 and 2008, by 0.7 and 0.2 p.c. of GDP respectively.

That fall is due partly to a reduction in the impact of temporary measures on the revenue side, whose influence over those two years should come to 0.3 and 0.2 p.c. of GDP respectively.

Structural measures are expected to exert downward pressure of 0.1 p.c. of GDP on revenues in both 2007 and 2008. Levies on earned incomes will continue to be slightly lowered during the projection period. The personal income tax reform approved in 2001 and the increase in the pension savings allowance in 2006 will have an impact on personal income tax assessments which is negative for general government. In addition, the percentages and the maximum amount of the standard professional expenses were increased again in 2007 and a standard reduction in personal income tax for professional activities has been applied in the Flemish Region since 1 January 2007. The parafiscal burden on labour will be reduced primarily

TABLE 9 MAIN NON-RECURRENT FACTORS⁽¹⁾
(millions of euro, unless otherwise stated)

	2006 ⁽²⁾	2007 e	2008 e
Real estate sales	953	200	0
Accelerated collection of corporate income tax	900	0	0
Tax regularisation operations	75	50	0
Shifts in the financing of the BNRC Group	100	0	0
Exceptional payment to the Flemish water supply companies and to Aquafin	-100	0	0
Temporary tax regime for tax-free reserves	0	341	0
Change in the timing of the payment of social contributions on holiday pay on termination of employment contracts	0	233	0
Securitisation of tax arrears	333	-176	-358
Total	2,265	648	-358
<i>p.m. Percentages of GDP</i>	<i>0.7</i>	<i>0.2</i>	<i>-0.1</i>

Sources: NAI, NBB.

(1) A positive (negative) figure indicates an improvement (deterioration) in the general government financing balance.

(2) In addition, a temporary measure relating to heating costs in 2006 caused a one-off increase in expenditure (97 million euro), but that effect was offset by a one-off contribution from the electricity and gas sector (around 100 million euro).

by the reductions in employers' contributions for young workers and for older workers, decided in the context of the generation pact. Finally, the operation of the reverse ratchet system on diesel and the gradual abolition of the compensatory excise duty on diesel vehicles will cause a loss of revenue. The effect of the reductions in charges will, however, be partly offset by other specific measures. Thus, the excise duty on tobacco has been increased, a tax on certain disposable products and packaging has been introduced, and the corporate income tax deductibility for company vehicles now depends on carbon dioxide emissions.

There are also some technical factors which will increase general government revenues while having only a limited net influence on the overall balance. That applies to the payment to the government, from 2007, of the social contributions for the pensions of BNRC staff, following

a revision of the system of pension funding⁽¹⁾. In 2008, the social contributions of self-employed persons will increase, as insurance against minor health care risks will then become compulsory for them. Statistically, that insurance will therefore be regarded as a component of social security from then on.

Finally, structural shifts at macroeconomic level will also influence the movement in general government revenues. Earned incomes, which are subject to relatively heavy taxation, should rise more slowly than GDP, the share of earned incomes – compensation of employees and gross mixed income excluding imputed contributions – falling from 55.6 p.c. of GDP in 2006 to 55.4 p.c. in 2008.

(1) From 2007, the first pillar pensions of former BNRC staff, which used to be paid by the BNRC Group itself, will be paid by the federal public sector pensions service. The operation is neutral for the budget, since the government used to provide a grant to make up the difference between the pensions granted by the BNRC Group and the social contributions collected for this purpose.

TABLE 10 STRUCTURAL MEASURES RELATING TO PUBLIC REVENUES

(millions of euro, unless otherwise stated; changes compared to the previous year)

	2007 e	2008 e
Taxes	-106	-123
of which:		
Personal income tax reform ⁽¹⁾	-144	0
Increased tax allowance for pension savings	-57	0
Flemish Region tax abatement	-107	-25
Raising of the standard allowance for professional expenses	-77	0
Gradual abolition of the compensatory excise duty on diesel vehicles	-81	-121
Tax on disposable products and packaging	67	67
Tax deductibility of company vehicles	13	51
Control of tax evasion and more efficient collection	407	0
Reverse ratchet system on diesel	-92	0
Excise duty on tobacco	200	0
Other	-235	-95
Social security contributions	-349	-83
Reduction in employers' contributions	-376	-83
Reduction in employees' contributions	-60	0
Control of evasion and more efficient collection	88	0
Total	-454	-206
<i>p.m. Percentages of GDP</i>	<i>-0.1</i>	<i>-0.1</i>
<i>p.m. Technical factors</i>	<i>214</i>	<i>397</i>
<i>BNRC pension contributions</i>	<i>214</i>	<i>0</i>
<i>Self-employed persons' contributions (minor health care risks)</i>	<i>0</i>	<i>397</i>

Sources: FPS Finance, NSSO, budget documents.

(1) Including the secondary effects on municipal taxes.

4.3 Primary expenditure

Primary expenditure, which had amounted to 44.9 p.c. of GDP in 2006, should decline slightly, dropping to 44.6 and 44.5 p.c. of GDP respectively in 2007 and 2008. Measured in volume, primary expenditure will thus increase by 2.5 and 2.3 p.c. in those two years. However, after adjustment for the influence of non-recurrent and cyclical factors and the effects of indexation⁽¹⁾, the increase comes to 2.1 and 2.2 p.c. in the two years, representing a relatively neutral spending policy in line with the trend growth of activity.

The planned expenditure growth in 2007 is due to varying developments in the subsectors making up the government sector. At the federal government level, the adjusted growth of primary expenditure will be fairly moderate. Expenditure for measures in favour of employment, particularly shift working, which are recorded as subsidies in accordance with the ESA 95, should continue to increase, but more slowly than in 2006. The share of Belgium's contribution to the EU budget, calculated on the basis of Belgian GNI, should also decline in 2007. Conversely, social security expenditure is expected to grow considerably faster than in the previous year, matching the movement in health care expenditure. After two years of particularly moderate growth, health care spending is likely to return again to more vigorous growth levels which are typical for this spending category. In addition, pensions should benefit from a set of measures, notably decided in the context of the generation pact, which will augment expenditure. At local authority level, primary expenditure will decline slightly in 2007 owing to the reduction in investment which traditionally follows the local elections, in this case those held in 2006. At the same time, the primary expenditure of the communities and regions will grow at a fairly sustained rate.

The rate of increase in primary expenditure in 2008 is difficult to estimate as the budgets are not yet available. However, at this stage, the projections include a set of measures to increase social benefits, particularly those decided in the context of the generation pact. While these will add to social security expenditure, the increase in local authority spending should once again be tempered by the reduction in local investment resulting from the electoral cycle. As regards the growth of federal government expenditure and that of the communities and regions, these projections are based on the historical average.

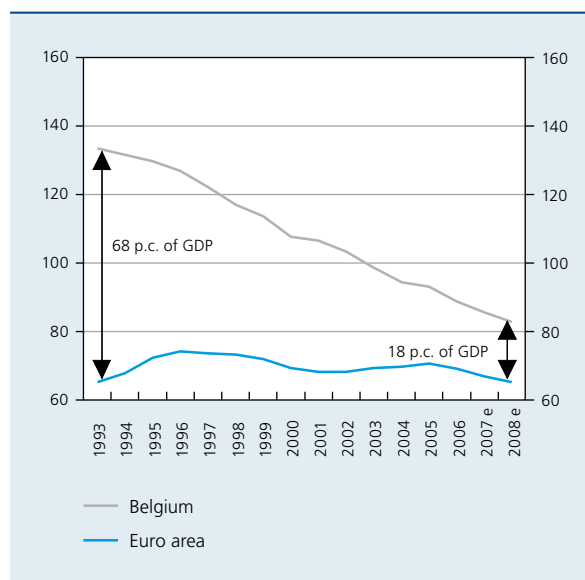
(1) Effects caused by the difference between the actual indexation of public sector wages and social security benefits and the increase in the HICP.

4.4 Debt

Since 1993, when the public debt had peaked at 133.5 p.c. of GDP, the debt ratio has fallen steadily by an average of 3.4 percentage points per annum. At the end of 2006, the general government debt ratio stood at 88.8 p.c. of GDP.

The public debt is expected to continue to decline, dropping to 85.6 and 82.7 p.c. of GDP respectively by the end of 2007 and 2008. The difference between Belgium's debt ratio and the euro area average should thus continue to reduce, reaching 18 p.c. of GDP at the end of the projection period.

CHART 10 CONSOLIDATED GROSS DEBT
(percentages of GDP, according to the view taken by Eurostat⁽¹⁾)



Sources: EC, NAI, NBB.

(1) According to the view taken by the NAI, the Railway Infrastructure Fund (RIF), set up in the context of the BNRC restructuring on 1 January 2005, comes under the non-financial corporations sector. According to the view taken by Eurostat, that Fund forms part of the general government sector.

5. Assessment of the uncertainty of the projections

Under current economic conditions, the economic projections for Belgium for the next eighteen months seem to rest on a sound, stable foundation. The growth of global activity – particularly the increased momentum in the euro area – should be sustainable, and inflation expectations should remain firmly anchored. Moreover, financial conditions look set to remain favourable. Belgium should be able to take advantage of that in a context of wage moderation in line with the central agreement for 2007-2008, the sound financial health of companies, and public finances which are more or less in balance.

However, this outlook is subject to several risk factors.

As regards world growth, the slowdown in the United States is so far largely confined to the residential construction sector. It could persist, and may have contagion effects on the rest of the US economy, possibly spreading to the global economy. The property market situation is also strained in some European economies, although there have recently been signs that it is easing.

The oil markets are also highly volatile. In a context of low reserves of production capacity, both spot and forward prices are very sensitive to movements in demand and to production conditions and decisions by the main producers, but they also react to the geopolitical situation. A further sustained rise in the price of oil would depress growth and risk rekindling inflationary pressures.

More fundamentally, such pressures could also grow if the world economy were to approach the limits of its production capacity. In that case, continuing vigorous growth could cause accelerating wage and price inflation, which would be likely to drive up interest rates. Moreover, large current account imbalances should persist in 2007 and 2008. A sudden exchange rate or interest rate correction would be detrimental to the global economy.

In Belgium, tensions are liable to appear on certain segments of the labour market, as more of the labour reserves are mobilised. That could curb growth and speed up the rise in labour costs and inflation.

TABLE 11 COMPARISON OF THE FORECASTS FOR BELGIUM
(percentage changes compared to the previous year)

	Real GDP		Inflation ⁽¹⁾		Budget balance ⁽²⁾		Publication date
	2007	2008	2007	2008	2007	2008	
NBB – Spring 2007	2.5	2.2	1.6	1.8	-0.1	-0.2	June 2007
<i>p.m. Autumn 2006</i>	2.1	-	1.9	-	-0.4	-	December 2006
Federal Planning Bureau (FPB)	2.3	2.2	1.8	1.9	0.1	-0.5	May 2007
IMF	2.2	2.0	1.9	1.8	0.0	0.0	April 2007
EC	2.3	2.2	1.8	1.8	-0.1	-0.2	May 2007
OECD	2.5	2.3	1.5	1.8	0.2	0.0	May 2007
Belgian Prime News	2.3	2.2	1.9	1.9	-0.1	0.0	March 2007
Consensus Economics	2.3	2.1	1.7	1.8	n.	n.	May 2007
The Economist's Poll	2.5	2.3	1.8	1.9	n.	n.	June 2007
<i>p.m. Actual figures 2006</i>	3.0		2.3		0.2		

(1) HICP, except FPB and OECD: private final consumption deflator.

(2) Percentages of GDP.

TABLE 12 COMPARISON OF THE ASSUMPTIONS

	2007					2008				
	NBB	EC	IMF	FPB	OECD	NBB	EC	IMF	FPB	OECD
Export markets	5.9	7.5	n.	7.3	n.	6.2	6.9	n.	7.2	n.
Oil (dollars per barrel)	65.0	66.2	60.75	61.0	64.7	69.9	70.3	64.75	61.9	65.0
Short-term interest rate	4.2	n.	3.8	3.8	4.1	4.5	n.	3.7	3.9	4.3
Long-term interest rate in Belgium	4.2	n.	n.	4.2	4.2	4.3	n.	n.	4.3	4.3
Dollars per euro	1.34	1.33	1.30	1.305	1.34	1.36	1.34	1.31	1.31	1.35

Incorporating the recent national accounts figures, and underpinned by the current expansion in the euro area, the Bank's growth forecasts for 2007 are slightly higher than those of the other institutions. The inflation forecasts for the same year are at the lower end of the range, probably because they take account of the downward

pressure exerted by the liberalisation of the gas and electricity markets, and the new method of recording those prices in the index. The same factors also account for the revisions compared to the projections drawn up by the Bank in December 2006. For 2008, the results are comparable to those of the other institutions.

Annex

PROJECTIONS FOR THE BELGIAN ECONOMY: SUMMARY OF THE MAIN RESULTS

(percentage changes compared to the previous year, unless otherwise stated)

	2004	2005	2006	2007 e	2008 e
Growth (calendar adjusted data)					
GDP in volume	2.8	1.4	3.0	2.5	2.2
Contributions to growth:					
Domestic expenditure, excluding change in stocks	2.8	1.3	2.8	2.3	2.3
Net exports of goods and services	-0.1	-0.4	-0.8	0.4	0.1
Change in stocks	0.1	0.5	1.0	-0.2	-0.2
Prices and costs					
Harmonised index of consumer prices	1.9	2.5	2.3	1.6	1.8
Health index	1.6	2.2	1.8	1.6	1.7
GDP deflator	2.4	2.0	2.0	2.0	2.1
Terms of trade	-0.3	-0.7	0.4	0.7	0.2
Unit labour costs in the private sector	-0.4	1.5	1.1	1.6	1.6
Hourly labour costs in the private sector	2.4	2.2	2.7	2.4	2.6
Hourly productivity in the private sector	2.9	0.6	1.6	0.8	0.9
Labour market					
Domestic employment (annual average change in thousands of units)	26.5	40.8	46.4	60.1	55.1
Harmonised unemployment rate ⁽¹⁾ (p.c. of the labour force) ...	8.4	8.4	8.2	7.6	7.2
Incomes					
Real disposable income of individuals	-0.1	0.9	3.2	2.4	1.8
Savings ratio of individuals (p.c. of disposable income)	13.2	13.2	13.8	14.1	14.0
Public finances ⁽²⁾					
Overall balance (p.c. of GDP)	0.0	-2.3	0.2	-0.1	-0.2
Primary balance (p.c. of GDP)	4.7	2.0	4.3	3.8	3.7
Public debt (p.c. of GDP)	94.3	93.2	88.8	85.6	82.7
Current account					
(p.c. of GDP according to the balance of payments)	3.5	2.6	2.0	2.7	3.0

Sources: EC, NAI, NSI, NBB.

(1) Adjusted series (Eurostat).

(2) According to the methodology used in the excessive deficit procedure (EDP) and according to the Eurostat point of view (see table 8).