REPORT 1999

Part I : Economic and Financial Developments

Part II : Activities and Annual Accounts

National Bank of Belgium

FOREWORD

by Guy Quaden, Governor

The question has been long debated : did the 21st century start on 1 January 2000 or will it not begin until 1 January 2001? For eleven European central banks, including the National Bank of Belgium (NBB), the answer is obvious : the 21st century began on 1 January 1999 with the start of the final stage of European monetary union, the advent of the euro and the integration of these eleven banks into the Eurosystem, linking them to the new European Central Bank (ECB).

Since then, for member countries in the euro area there has been a single monetary policy decided in Frankfurt by the ECB. However, the national central banks are closely involved in this process.

On the one hand, the Governor or President of each national central bank has a seat and a vote – according to the "one man, one vote" rule – on the Governing Council of the ECB, where the main monetary policy decisions are taken. However, the statutes of the ECB stipulate that all members of this Council (including the national governors) must base their decisions on the interests of the euro area as a whole and not on the specific interests of their country of origin. Also, in accordance with the principle of independence, they cannot accept or request any instructions from any other authority whatsoever, be it national or European. But quite obviously, the governors of the national central banks rely heavily on the information supplied to them by the staff of their own institution.

Furthermore, although decisions on monetary policy are now taken centrally in the euro area, the execution of monetary policy remains decentralised. In the Eurosystem, which is unlike the model of any other existing central bank, the national central banks implement in their respective countries the monetary policy operations decided on by the Governing Council of the ECB and are still the primary *partners in discussions with the financial institutions established in their territory. Representatives of the national central banks also take part in various special ECB committees which assist the Governing Council.*

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The NBB, which will celebrate its 150th anniversary in 2000, is also continuing to fulfil its other responsibilities and to pursue a wide range of activities. It performs many services for the Belgian economy which it constantly monitors and analyses.

The Bank prints and issues banknotes and supervises the quality of the notes and coins in circulation. It provides the State Cashier service. It operates interbank payment and securities clearing systems; since 1 January 1999 it has also been made responsible for the oversight of the clearing and payment systems as a whole. In its Central Balance Sheet Office and its Central Credit Offices it collects and processes information on enterprises and individuals.

The studies conducted by the Bank focus on the various aspects of economic activity. Every month it produces and publishes a business survey the results of which attract widespread interest, not only in Belgium but also in other countries. The Bank's statistical work has been extended considerably in the course of the modernisation of the Belgian statistical system, decided on in 1994; in particular, the Bank is responsible for the foreign trade statistics and the compilation of the national accounts on behalf of the National Accounts Institute.

In 1999 the Bank also took over the activities of the Rediscount and Guarantee Institute.

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The Annual Report is the Bank's principal publication. This document, which is still keenly awaited and – I believe – much appreciated, provides useful information on recent economic and financial developments in Belgium – placed in their international context – and, particularly in the message presented by the Governor on behalf of the Council of Regency, offers comments which clarify and stimulate the economic policy debate. It is also the chief instrument whereby the Bank accounts for its actions, in accordance with the principle of responsibility, which goes hand in hand with the high degree of independence which the Bank is guaranteed from now on – as are the ECB and the other central banks belonging to the Eurosystem.

For a long time the NBB's Annual Report has consisted of two separate parts (though until now they were published simultaneously in the same volume), one examining national and international economic and financial developments and the other dealing with the annual accounts of the Bank and its activities as an enterprise. From this year onwards, these two parts will be published, for the French and Dutch versions, in two separate volumes a few weeks apart.

The NBB used to be the first Belgian company ending its financial year on 31 December to circulate its accounts, which came out in February, but it is now dependent on the closure of the ECB's accounts which takes place later. Those accounts are used, for instance, to calculate the monetary income due to each national central bank. For that reason, the Bank's General Meeting is now held on the last Monday in March (and not the last Monday in February).

However, the Bank did not wish to delay the publication of the first part of its Report. Indeed, we know that the early availability of essential information on the national economy, even if that information is provisional, is one of the primary benefits of our Report for the authorities and the public.

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Report presented by the Governor on behalf of the Council of Regency

ECONOMIC AND FINANCIAL ENVIRONMENT

World economy reviving faster than expected but with latent risks

During the year under review the world economy recovered faster than had been expected from the aftermath of the financial and economic crisis in Asia and other emerging economies. The disruption of the financial systems in these countries was brought under control, while the feared contagion effects on the industrialised countries remained on the whole limited, partly thanks to an appropriate easing of monetary policies, which helped to restore confidence on the financial markets. As a result, growth prospects for the world economy improved considerably. However, significant underlying risks are still present. In a number of the countries recently in crisis the adjustment process is far from completed, so that they are still vulnerable to a possible new loss of confidence among their foreign lenders. But the unbalanced growth pattern and external disequilibria of some major industrial countries also give cause for concern.

After the sharp recession of 1998 most of the Asian crisis countries experienced a remarkable economic recovery last year. GDP growth in this region is estimated to have averaged some 4 p.c. in 1999. In some countries, such as South Korea and Malaysia, the revival actually exceeded the most optimistic expectations. Supported by competitive exchange rates, these countries' exports benefited greatly from the upswing in world trade. In the meantime, reforms in the financial sector, which were urgently needed after the turbulences of the preceding years, made good progress and most of the financial market indicators stabilised, permitting – given the slackening of inflation – a relaxation of monetary policy. Now that this part of the Asian region appears to have the wind in its sails again, the temptation to scale down the restructuring efforts must be resisted. In a number of fields, and especially as far as the non-bank enterprise sector is concerned, continued structural reforms remain essential in order to give lasting support to these countries' growth potential.

In Latin America the economic climate was generally very depressed during the past year. Only Mexico, which was able to benefit from the pull exerted by the American economy, again showed strong growth and good trade figures. In Brazil the recession remained on the whole very moderate and there have recently been signs of a recovery. However, the whole region remains vulnerable to new financial disruptions.

The same can be said of a number of transition countries in Central and Eastern Europe, where the aftermath of the Russian crisis is still perceptible and the Kosovo conflict further impeded recovery, especially in the Balkan countries. It is perhaps not by chance that the countries which have already progressed furthest in the transition to a market economy and in the implementation of disciplined macroeconomic and structural policies are precisely those which have been most resilient and put up quite good economic performances last year. Hungary, Poland and Slovenia are illustrative in this respect. It is in fact in the interest of the European Union that the Central European countries are continuing along the road towards lasting economic growth and adhering to stability-oriented policies, in view of the prospect that a number of them may accede to the Union in the not too distant future.

After two years of sharp decline, the Japanese economy, too, appears to be heading for a recovery, although the revival there is still unsta-

ble and precarious. A sustained expansionary monetary and fiscal policy and the indisputable progress made in the consolidation and restructuring of the banking system have restored confidence to some extent, especially among households. Evidence of this is provided by the return to positive growth figures for private consumption and investment in housing. The greatest boost to growth was however given by public investment, which increased by about 14 p.c. in volume and has pushed up GDP growth by over 1 percentage point. Business investment, on the other hand, continued to shrink, albeit less than in the previous year. Unlike in the banking sector, the restructuring of trade and industry is still at a relatively early stage, a situation which is coupled, especially in the traditional industries, with the dismantling of excess or unprofitable production capacity and a contraction in employment.

On its external account, the Japanese economy was, it is true, able to derive some advantage from the strong revival among its main Asian trading partners, but at the same time it had to contend with a loss of competitiveness due to the sharp appreciation of the yen, which also pushed up imports. On balance, therefore, transactions in goods and services with foreign countries broadly made a neutral contribution to growth, while the current account surplus, at nearly 3 p.c. of GDP, remained particularly high.

In view of the continuing uncertainty about the durability and strength of the cyclical recovery, the Japanese authorities have for the time being little choice but to persevere in their stimulation policy. As the monetary authorities have just about exhausted their possibilities, with short-term interest rates close to zero, the main emphasis has perforce been laid on budgetary policy. It has become crucially important, however, to strive for maximum efficiency in government action, something which has not always been achieved in the past. The deterioration in the public finances has actually assumed such disquieting proportions that the growth in indebtedness might become difficult to control. There is therefore a real danger that a further budgetary relaxation may produce adverse effects on households, which, anticipating a subsequent consolidation, might display a greater propensity to save.

The continuing strong growth of the American economy – which, in 1999, reached its eighth year in a row, and still came to some 4 p.c. – has undoubtedly helped to dampen the impact of the recent slowdown elsewhere in the world, but has at the same time given rise to a number of potentially destabilising factors, such as very optimistically valued share prices, a savings ratio of households which has sunk to a particularly low level, a high dollar rate and an unusually large current account deficit, revealing the extent to which the United States depends on foreign financing sources. The baseline scenario assumed for the near future by the leading international forecasters is that of a "soft landing" of the American economy and its gradual return to a lower growth path. Unforeseen shocks, such as an upsurge of inflation or a turn-round in the attractiveness of dollar investments might however lead to a much more abrupt adjustment, which in turn could put a damper on the recovery of the world economy.

This does not alter the fact that the economic performances achieved by the United States during the 1990s have been remarkable in more than one respect and contrast with the rather disappointing record of Europe and above all Japan. These differences in economic results can be the reflection of both demand and supply factors, the former mainly determining the cyclical movement of economic activity and the latter, which relate more specifically to the input of the production factors labour and capital and their associated efficiency or productivity, chiefly determining potential output growth over a longer period.

Research has shown that the higher trend growth of the American economy is to a great *extent based on a relatively stronger expansion of the supply of labour. The latter can in turn be attributed to more dynamic demographic factors, but also – and perhaps to an even greater extent – to a more efficient use of the existing labour potential, due to, among other things, greater flexibility of the labour market, which has benefited the employment of both highly skilled and low-skilled workers.*

This is nothing new, however, and therefore does not offer a satisfactory explanation for the remarkable fact that economic growth in the United States speeded up further in the second half of the past decade and that inflation at the same time remained low and stable, while unemployment fell sharply. Activity had already been showing an upward trend for quite a long time and one would normally have expected that productivity growth would weaken, inflationary strains would develop and eventually the economic expansion phase itself would come to an end. In fact, the non-inflationary growth potential of the American economy appears to have received a new impetus during the past few years. Whether this represents a trend break, or just a temporary combination of favourable factors, is still a controversial question. Some observers regard the atypical acceleration of productivity growth as a sign of the emergence of a "new economy" : the introduction of new information and communication technologies and the concomitant spread of more efficient business methods have, they contend, lifted potential output growth onto a permanently higher level.

These developments are undoubtedly important and have contributed to the recent wave of investment which extended the capacity limits of the American economy for some time ahead. To what extent they differ from the constant stream of innovation which – albeit in waves – has dominated the entire twentieth century and are really capable of bringing about a lasting quickening of economic activity remains an open question for the time being, since the unexpected productivity rises of recent years are not the only factor to have favoured the growth climate in the United States. For instance, domestic demand has been supported not only by the increase in real disposable income but also by wealth effects emanating from exuberant developments on the stock markets. The latter in turn were linked to the favourable profit prospects for American businesses, although these were often of a purely speculative nature, as well as to the inflow of foreign capital which, against the background of the crisis in emerging economies, was in search of a safe haven. As a result, businesses were able to resort to relatively inexpensive financing sources. Furthermore, the until recently weak international environment, coupled with falling commodity prices and a rising dollar rate, ensured that a large proportion of the American demand expansion could be catered for on relatively advantageous terms by recourse to the plentiful production capacity available abroad. The corollary of this was mounting external deficits – rising to over 3.7 p.c. of GDP in 1999 – which however were easily financed from the ample inflow of foreign capital.

While these and other factors have for some time been stifling overheating phenomena in the American economy, they are certainly not a permanent feature, and some of them have in fact already largely disappeared. For instance, the sharp rise in the prices of oil products, followed later in the year by other increases in commodity prices, combined with a moderate fall in the weighted effective exchange rate for the dollar, led to upward pressure on import prices, which subsequently also became evident in the first stages of the production process. At the same time, there were signs of a certain quickening of the rise in unit labour costs. As a reaction to these heightened inflation risks the Federal Reserve raised its key interest rate three times between June 1999 and the end of the year, by a total of 75 basis points. Now that the expansion rates of the world's major economic areas appear to be converging, the cru-

cial factor is whether the American authorities will succeed in adjusting domestic demand to a more balanced growth path, while avoiding serious disruptions in the financial sphere.

Favourable growth prospects with moderate inflation risks in the euro area

The slowing of growth from which most of the euro area suffered in the second half of 1998 and at the beginning of 1999 turned out to be less sharp and of shorter duration than was originally feared. Various factors contributed to this. Firstly, the fall in external demand which was at the origin of the weakening of activity was partly counteracted by direct or indirect exports to the United States, where the markets, as stated, remained unexpectedly dynamic. Secondly, against the background of already low and still falling inflation, the easing of monetary policy decided upon at the end of 1998 and in April 1999 helped to support confidence and hence also domestic demand, especially in those countries where there were fears of a deflationary spiral. Thirdly, weaker growth did not appear to have appreciable consequences for job creation, which partly explains why consumer confidence was hardly affected either. In the sectors which produce mainly for the domestic market, such as the building industry and the service sector, a reasonably high rate of activity was therefore maintained. On the other hand, growth was somewhat artificially reduced in the first months of 1999 by the running down of inventories following the – largely unintentional – formation of stocks of finished products during the second half of 1998. This stock cycle in fact explains about two thirds of the fall in average annual GDP growth in the euro area, from 2.8 p.c. in 1998 to an estimated 2.1 p.c. in 1999.

Later on in the year, however, more and more indications became available supporting the presumption that the latter figure, taken from the OECD's autumn forecasts, somewhat underestimates the actual course of events. From the beginning of the summer onwards, the economic outlook for the euro area in fact improved considerably. The initial impetus came from the aforementioned turn-round in the external environment, the pull exerted by which was further strengthened by an improvement in the competitive position of enterprises due to the depreciation of the effective exchange rate for the euro. All this led to a rapid revival in economic activity : industrial output picked up again, stocks were replenished, partly as a precaution in view of the turn of the millennium, and a strong recovery of business confidence was generally observable.

Employment growth, for its part, appears to have reacted only with a time-lag and to a limited extent to the recent cyclical slowdown, and can be estimated for 1999, despite weaker average GDP growth, at about 1.5 p.c. The trend towards a more labour-intensive growth pattern which became apparent in the previous years may be attributed to a combination of factors. Thanks to the general moderation of wages, real labour costs moved more into line with labour productivity, thus curbing the substitution of capital for labour. Furthermore, employment growth was supported by the greater policy emphasis laid on active labour market measures and by a structural shift to the generally more labour-intensive service sector. In view, however, of the great differences in unemployment rates according to regions and qualification levels, and of the persistence of a considerable degree of structural unemployment within the euro area, further progress in improving the functioning of the labour market is still essential. As taught by the experience of the United States, but also of some individual EU countries, this is likely to substantially increase the chances of lasting non-inflationary growth.

During the year under review, the euro area, like other industrialised countries, had to contend *with a sharp rise in oil prices, but its impact on consumer prices remained on the whole limited. This was partly because the extremely low level reached by oil prices at the end of 1998 could be regarded as exceptional. Their subsequent acceleration therefore rather represented a correction towards a level in line with what had been considered normal since the reverse oil shock of 1986. The worsening of the terms of trade brought about by the oil price rises also remained limited because the industrialised countries have now become much less dependent on oil imports. According to the OECD, oil inputs per unit of output have decreased on average by about 40 p.c. since the first oil shock of the 1970s.*

Despite these external price pressures, added to by the depreciation of the euro, underlying inflation in the euro area ultimately remained quite moderate and stable last year, with percentage rises fluctuating around 1 p.c. The rise in the energy and import bill had hardly any repercussions on the price development of non-energy consumer goods, while service price increases tended to slacken, owing partly to the favourable effects of deregulation and liberalisation in the public utilities sector.

Barring adverse external developments, the prerequisites for a sustained expansion of activity with only limited inflationary pressure appear to be in place in the euro area, so that GDP growth could work out at around 3 p.c. in the near future. Notwithstanding the recent rise in interest rates, the financial situation – including business profitability – is still favourable for investment, while continuing employment growth would help to maintain consumer confidence at a high level and to support private consumption. According to the forecasts made at the end of 1999, consumer price inflation is expected to quicken somewhat further in the first half of 2000, though remaining on average over the whole year under 2 p.c. and thus below the upper limit of what the European Central Bank regards as price stability. This forecast is, however, still subject to risks, in particular with regard to the outcome of the wage negotiations in a number of countries and to the second-round effects of the oil price rises. Continued vigilance is thus called for.

Some concern has also been felt within the euro area about the tendency towards an increasing divergence in the growth and inflation figures of the participating countries. In order to place these in their proper perspective and to allow for an appropriate policy response, it must however be borne in mind that such divergences may have differing causes.

These differences may, firstly, be connected with the catching-up process still taking place in some Member States. Countries starting from relatively low productivity levels will generally show higher labour productivity increases and thus also greater growth potential than the more advanced Member States. The growth differences attributable to this need not, as such, prompt any misgivings, as they are more the expression of the convergence of the countries concerned. The relatively loose monetary conditions which they can at the moment enjoy within the monetary union, as well as the access to a large integrated capital market, do admittedly give them additional support in this process, but they also call for greater watchfulness concerning latent inflationary strains. The primary requirement for the countries in question is thus to maintain an appropriate stability-oriented policy mix and to push on with the implementation of structural reforms in order to heighten the efficiency of their markets for goods and services and to promote the smoother operation of their labour markets.

Further progress in this field would also benefit the other euro area countries by increasing their ability to withstand adverse external developments or asymmetrical shocks. As within the frontiers of individual countries, regional and sectoral structural differences are *unavoidable within a monetary union, too; they can, however, cause the individual Member States to react differently to such shocks. Such factors appear to be partly responsible for the recent weaker growth performances of, for instance, Germany and Italy. Owing to their more direct trade relationships with a number of crisis countries or their greater specialisation in the production and exporting of capital goods and intermediate products, these two countries suffered relatively more from the slackening of world trade than other countries in the euro area. Countries participating in EMU should, however, be able to deal with such situations by ensuring sufficient flexibility in their goods and labour markets and pursuing appropriate fiscal policies. The above-average growth and the sharp fall in unemployment achieved by some countries which have already made appreciable progress in that respect prove that such a policy is rewarding.*

Growth in activity and employment bears witness to the Belgian economy's increased resilience

The Belgian business cycle generally keeps close to that of the euro area as a whole and has recently, according to the Bank's business surveys, even tended to run ahead of it somewhat. That was also the predominant picture during the past year, although it was temporarily clouded by the shock created by the dioxin contamination of part of the food chain. From the first quarter onwards, activity resumed the dynamic expansion which had also prevailed during the period up to the beginning of 1998. Average annual GDP growth, at 2.3 p.c., was admittedly almost half a percentage point lower than in 1998, but, as elsewhere in the euro area, that was due more to the weakened initial position at the beginning of the year than to the actual cyclical movement during the year. If the dioxin crisis had not depressed exports and consumer confidence for a short time during the summer months, the Belgian economy would actually have performed even better, as the loss of value added brought about by this crisis is estimated at about a quarter of a percentage point of GDP. That is however less than was initially feared. The fact that the costs of this asymmetrical shock caused by the dioxin crisis remained restricted both in duration and in extent can undoubtedly be regarded as a favourable side-effect of monetary union. Had it not been for the euro, both the exchange rate and the interest rate would probably have come under pressure and the consequences would have been felt far beyond the directly affected sectors.

Apart from this setback, Belgian enterprises already detected a clear turn-round in export demand early in the year and sooner than elsewhere in the euro area. But as domestic demand in some of our main trading partners, including particularly Germany and Italy, remained slack for a little longer, total exports did not actually begin to pick up until the summer months. Since then, however, exports have risen steeply. On average, the volume growth in exports still amounted to nearly 3 p.c. in 1999, which anyhow represents a decline of about 1.3 percentage point compared to the previous year. Nevertheless, it was mainly the turn-round in stocks, which had increased substantially in the course of 1998 owing to the unexpected weakening of demand from abroad, that depressed average growth during the year under review.

Apart from these predominantly exogenous factors, the spending behaviour of Belgian economic agents on the whole remained very robust. The high rate of utilisation of production capacity and the improved sales prospects stimulated the investment activity of enterprises. With a volume growth of nearly 8 p.c., gross fixed capital formation by enterprises, which was concentrated chiefly in the service sector, therefore proved to be the most important activity-supporting factor. Investment in residen-

tial housing, on the other hand, appears to have hardly risen at all, mainly owing, it seems, to the discontinuance of some fiscal incentives and rising building costs.

The growth in private consumption, which had been exceptionally high, at 3.8 p.c., the previous year, admittedly slowed down to 2 p.c. in 1999, but still proved higher than the 1.5 p.c. increase in real disposable income of households, indicating that consumer confidence was strong enough to induce households to further reduce their savings ratio. This remarkable resilience of consumer confidence shows that households feel less uncertain about the future development of their purchasing power. The policy aimed at macroeconomic stability which led to the integration of Belgium in the monetary union, together with the efforts made to improve the employment-content of growth, clearly played a beneficial role in this respect.

The recent developments on the labour market bear witness to the effectiveness of the more active employment policy pursued in recent years. The combination of sustained wage moderation, limitation of indirect labour costs, activation of unemployment benefits and introduction of more flexible working conditions does indeed appear to be bearing fruit, especially as regards the labour-intensiveness of economic growth. Despite the, on average, weaker GDP growth, the situation on the labour market remained robust : the volume of work in enterprises, measured as the total number of hours worked by employees, increased further, by about 1.1 p.c., last year. Partly because of the further spread of part-time working, which received an additional stimulus from the policy for activating unemployment benefits, the increase in the number of persons working in enterprises, at 1.6 p.c., proved greater still, thus achieving one of the highest growth rates since the beginning of the 1980s. Indeed, not very long ago economic growth of around 2 p.c. was merely sufficient to bring about a stabilisation of employment. Against this background the unemployment figures, too, have continued to decline. At the end of 1999 the harmonised unemployment rate stood at 8.7 p.c., or half a percentage point lower than a year earlier.

Notwithstanding these somewhat tighter labour market conditions, which mainly related to certain sectors and regions or to specific occupational categories, and the fact that the economy has in the meantime come close to its potential growth rate again, few signs of inflationary wage pressure are observable for the time being. As in the previous year, the rate of increase of nominal labour costs per full-time equivalent came to about 2.2 p.c. A favourable influence in this connection has been exerted both by the restraint shown in collective wage bargaining as required by the wage norm and by the wage moderation resulting from the application of the "health index" (which largely offset the incidence of the recent oil price rises), as well as by the lowering of employers' social security contributions. If account is also taken of the increase in productivity, which can be estimated at around 1.9 p.c., the rise in unit labour costs works out at only about 0.3 p.c., or about the same as in 1998.

On the basis of the harmonised index of consumer prices, the inflation rate averaged 1.1 p.c. during the year under review, which was hardly any higher than the 0.9 p.c. rise of 1998. During the second half of the year, however, inflation speeded up somewhat, to reach 2.1 p.c. in December, owing to the rise in energy prices. But the underlying inflationary trend, which can be better assessed if the changes in the prices of energy and unprocessed foodstuffs are disregarded, continued to slow down throughout the greater part of the year, after which it accelerated only slightly, to about 1.3 p.c.

All available forecasts indicate that the Belgian economy will continue to expand in the near future, as the revival now in progress is broadly based. If foreign demand picks up further, as *predicted, and taking into account the favourable development of relative costs, further strong export growth may be expected, with net exports making a positive contribution to GDP growth in 2000 also. Given firm consumer and business confidence, the various domestic expenditure components may also be expected to remain buoyant. With a predicted volume expansion of at least 3 p.c., GDP growth would exceed its trend growth, resulting in a further narrowing of the output gap and sustained employment growth.*

THE EURO AND THE MONETARY POLICY OF THE EUROSYSTEM

The adoption of the euro by eleven Member States of the European Union was a major historical event and a crucial stage in the building of Europe. It is too early to make a final judgment about the single currency at the end of its first year of existence. Some of its advantages will only progressively become apparent : the effects of the deepening of the single market, through the elimination of the exchange risk, the reduction in transaction costs and the increase in price transparency, will be gradual and will become stronger from 2002 onwards, when national currencies will have completely disappeared. Concrete assessment of other advantages will be possible only after a certain length of time. As a matter of course, it will be some years yet before it will become obvious that the Eurosystem – which encompasses the ECB and the national central banks of the euro area – has in fact succeeded in its task of maintaining price stability. It is also too soon to assess the knock-on effects which monetary union will produce on European integration in other fields and what its impact on the international monetary system will be.

However, the euro's first steps can already be said to be promising. The convergence efforts made have been such that the Eurosystem has taken over the reins of monetary policy in an environment of price stability. From the outset it also had the benefit of a high degree of credibility, doubtless primarily due to the guarantees enshrined in the Treaty establishing the European Community – namely its independence and the primacy of the objective of price stability –, as well as to the monetary policy strategy chosen and to the fact that the members of the Governing Council of the ECB adhere, without reservation, to an area-wide approach. Owing to the widespread confidence in the maintenance of the internal value of the euro and thanks to the budgetary consolidations carried out in recent years, real long-term interest rates, which have admittedly risen as a result of better economic prospects in the euro area and the rest of the world, have remained appreciably lower than during the period 1980-1996. On the operational plane, too, the launch of the new currency was a success, thanks to meticulous preparation. The integration of the financial markets is in progress and the euro is already seen to be a leading international currency.

The monetary policy strategy has proved to be well suited to the new context. It has enabled the Eurosystem to inherit the reputation of the central banks which have achieved the best results in terms of price stability, while taking account of the uncertainties created by the change of monetary system.

To guide its action and enable the public to judge it, the Governing Council of the ECB first of all defined more precisely the paramount objective of its policy. Price stability is defined as a rise in the harmonised index of consumer prices of less than 2 p.c. per year in the euro area. It must be maintained in the medium term. The Eurosystem is just as concerned with avoiding deflation as with preventing inflation. To this end, it is willing to accept a slight rise in the index probably exceeding the inherent statistical overestimation of the actual increase in prices, due for instance to the improvement in the quality of the products or to the changes in consumption habits caused by the variations in relative prices. This dual concern is illustrated by the two changes in interest rates in 1999 : on 8 April a reduction of the rate on the main refinancing operations, from 3 to 2.5 p.c., was decided upon in order to counter the downward risks to activity and consequently to prices; on 4 November this rate was brought back up to its initial level because this threat had disappeared and had been gradually replaced by opposite risks for price stability.

The Eurosystem cannot, of course, be held responsible for temporary variations in prices due to shocks such as the rise in the prices of energy products which took place in 1999. But it must take them into account in the formulation of its policy if these shocks jeopardise medium-term price stability. For, given the length of time which it takes monetary policy impulses to work their way through, the Eurosystem's action, even though it can be gradual, must be forward-looking. It is based on the two pillars of the strategy adopted by the Governing Council : a prominent role assigned to money, as signalled by the announcement of a reference value for the growth rate of the broad monetary aggregate M3, and an assessment, based on a wide range of indicators, of the outlook for price developments in the euro area.

The recourse to a reference value for the increase in M3 reflects a degree of continuity with the practice of the German central bank and highlights the Eurosystem's responsibility for the monetary impulses to price movements. It is based on the observation of a fairly stable medium-term relationship, in the past, between this monetary aggregate and prices in the euro area. The reference value was fixed at the annual rate of 4 1/2 p.c. in December 1998. This figure was maintained a year later because there had been no change in the components involved in its calculation : the definition of price stability is unchanged and the estimates of the potential output growth and the trend decline in the velocity of circulation of M3 remained in the region of 2 to 2 1/2 p.c. and 1/2 to 1 p.c. respectively. It should be stressed that it really is a reference value and not an intermediate monetary policy target. Indeed, the demand for money may undergo short-term fluctuations without harming price stability, and the incidence of the shift in monetary regime remains uncertain. Furthermore the Eurosystem does not exert any direct control over the movement of M3.

Interest-rate policy is therefore not determined mechanically by the divergences between the growth in M3 and the reference value. These are first of all analysed and evaluated, in parallel with the overall assessment of the risks to price stability. Thus, the overstepping recorded during the first months of 1999 did not prevent the lowering of interest rates on 8 April because, being still limited, it could be attributed to the temporary effect of the transition to the single currency. By contrast, the observation of a widening discrepancy between the rate of increase in the aggregate and the reference value, accompanied by a sharp expansion both in credit and in the most liquid components of M3, was one of the reasons for the raising of interest rates on 4 November.

The overall assessment of the outlook for price developments in the euro area is based on many other leading indicators, such as price or unit value indices upstream of consumer prices, exchange rates, business cycle indicators, data *on the development of labour costs and on the public finances. The Governing Council also takes into consideration the information on inflationary expectations derived from financial indicators such as long-term interest rates, while remaining aware that this information may be impaired by the lack of liquidity of some markets, over-reactions and, more generally, the variability of risk premiums. In 1999 the Council successively concluded that there were downward and upward risks affecting price stability. The former were due to the continuing weakness of economic activity while the harmonised index of consumer prices was rising only very moderately and industrial producer prices were actually falling. The easing of the interest rate policy responded to this and helped to restore business confidence. Subsequently, the rise in import prices due to the rebound of oil prices and the depreciation of the euro, together with the improvement in the business climate, led to the appearance of the opposite risks. The need then was to make monetary policy less expansionary, in order to prevent excessively generous liquidity conditions from leading to upward pressures on prices.*

Relying on a simple rule for the conduct of monetary would not have been appropriate, given the complexity of developed market economies and the uncertainty surrounding the new situation. The medium-term orientation of this policy precludes "activism", that is, frequent reactions to "news", which would only increase the uncertainty. Moreover, the motivations of the Governing Council of the ECB are explained to the public by means of publications, speeches and monthly press conferences.

Furthermore, the final aim is absolutely clear. The Treaty stipulates that the Eurosystem shall also support the general economic policies in the Community with a view, in particular, to helping to promote growth, employment and economic and social cohesion, but without prejudice to price stability. It is by creating an environment of stability that the Eurosystem will best foster growth and employment and enable the other policies to produce their full effects. This does not prevent measures necessary for the pursuit of the paramount aim of contributing, in the shorter term, to the stabilisation of activity, since pressures on prices are often linked with cyclical fluctuations. The lowering of interest rates decided upon in April is an example of this. On the whole, monetary conditions were particularly favourable to economic expansion in 1999. First, real short-term interest rates were very low in an historical perspective. Secondly, the euro depreciated, mainly because of the cyclical asynchronism vis-à-vis the United States, and subsequently owing to the revival of confidence in the Japanese economy. These boosts are temporary – the exchange rate for the euro, in particular, should appreciate as European growth strengthens – and the Governing Council of the ECB considered that they did not endanger medium-term price stability.

Pursuit of this objective does not mean that there has to be perfect uniformity, within the euro area, of the rates of change in the harmonised indices of consumer prices. Divergences in inflation between countries create hardly any problem if they are due to convergence towards a common price level, resulting from the integration of markets and increasingly similar productivities and standards of living, or if they reflect the movement of relative prices between products whose weights in the various indices are not identical owing to different consumption habits. In other cases, corrective action would be necessary. Thus, budgetary policy should be more restrictive in countries where the strength of business activity is creating inflationary strains. As far as Belgium is concerned, the cyclical situation and price developments were very close to the average for the euro area in 1999.

The assessment of the economic and monetary situation in the area as a whole, which guides the single monetary policy, is nevertheless based on a thorough knowledge of all the spe-

cific factors. The national central banks have given the Eurosystem the benefit of their expertise in this respect. At the same time they have looked beyond domestic concerns so as to consider the euro area as a whole and to attune their thinking to the reality of a large economy which is much less open than those of which it is composed. Most of them have had to assimilate the model of a policy based on the analysis of monetary developments and of price prospects, instead of endeavouring to achieve exchange rate stability, since, for the Eurosystem, the exchange rate does not have the status of a monetary policy objective but is merely one of the indicators taken into consideration in assessing the risks to price stability. In all these respects, the experience of the Eurosystem's first year of operation has been positive and the learning process has been rapid.

The national central banks are also playing an active part in the implementation of monetary policy. Credit institutions hold accounts with their countries' central bank and turn to it to obtain liquidity, providing as collateral, if they wish, securities issued and deposited in other countries. This organisation in no way detracts from the singleness of monetary policy, because the absolute centralisation of decisions guarantees the uniformity of the terms offered to credit institutions, while these institutions are able to perform arbitrages which equalise short-term interest rates in the euro area, thanks to the TARGET payment system. The latter thus plays a crucial role in the integration of the money market, while at the same time helping to reduce the systemic risk, since it ensures the final, immediate and safe settlement of payment orders.

The operational framework chosen by the Eurosystem gave it the means for effectively guiding short-term interest rates in 1999, and money market operators adjusted themselves rapidly to it. The bulk of liquidity was granted by means of the main refinancing operations, that is, the weekly allotments of two-week credits by tender organised at euro-area level. The procedure of fixed-rate tenders was adopted because it was important, during this first year, to send out the clearest possible signals concerning interest rate policy. Credit institutions made appropriate use of the averaging provision over one-month periods attached to the compulsory reserves, which allowed them to absorb very-short-term liquidity fluctuations by adapting their current account balances. Consequently, except during the last days of the maintenance periods, both the recourse to the standing marginal lending and deposit facilities and the volatility of overnight interest rates were slight. Moreover, the overnight rate remained very close to the rate for the main refinancing operations. Finally, the Eurosystem did not carry out any fine-tuning operation during the year under review. A liquidity and credit risk premium appeared temporarily in the interest rates for interbank deposits, because of the possibility of computer problems arising at the time of the changeover to the year 2000. In the end, however, this took place smoothly.

Although the market for interbank deposits is completely unified, largely thanks to the TARGET payment system, the integration of other financial markets, such as those in repurchase agreements, bonds and shares, is still incomplete and sometimes impeded by differences in regulations and tax provisions, whereas it could promote a more efficient allocation of resources. Market integration has nevertheless already made progress owing to the introduction of the euro, as is shown, for instance, by the conversion into euros of most public debt securities and by the diversification of bond portfolios, by the upsurge in bond issues by enterprises, by the links established between securities depositories and by the creation of common trading platforms. Furthermore, the Eurosystem intends to encourage initiatives aimed at heightening the efficiency of cross-border small-value payment systems in the euro area.

The improved functioning of financial markets and the internationalisation of the euro are likely *to strengthen each other. Among the many factors that will promote the latter are the size and liquidity of the euro area's financial markets, which will in turn be increased by more widespread use of the euro by non-resident lenders and borrowers. The euro is already the second-ranking international issue, investment, reserve and anchor currency. During the first nine months of 1999, issues of bonds denominated in euros on the international markets almost reached the volume of issues in US dollars, and their share was appreciably greater than that generally represented by issues in the currencies which were replaced by the euro. The new European currency actually comes first if account is taken only of net issues in a currency other than that of the borrower. Moreover, some Asian central banks announced a diversification of their foreign exchange reserves in favour of the euro and a number of European and African countries pegged their currencies to it.*

The introduction of the euro also gives a new impetus to many other parts of the European integration process. The changeover to the single currency is a sweeping structural reform which will heighten competitive pressures in the single market, to the benefit of economic dynamism. By reforming its markets for labour and products, each country would derive full advantage from its incorporation in the euro area, increase its growth potential and reduce unemployment.

Lastly, a start has already been made on the preparation for two outstanding events : the putting into circulation, on 1 January 2002, of the euro notes and coins, which will make membership of a community more tangible to some 300 million citizens, and the gradual enlargement of the European Union, which should subsequently cause a larger number of countries to adopt the euro.

BUDGETARY POLICY

European monetary union created a new framework for budgetary policy, although this, unlike monetary policy, remains a matter for the national authorities. The guiding principles are laid down in the Stability and Growth Pact, whereby the EU Member States undertook to aim for medium term objectives of budgetary positions close to balance or in surplus, in order to create the necessary scope for allowing the automatic stabilisers to respond to cyclical needs without this giving rise to excessive deficits of more than 3 p.c. of GDP.

This means that the budgetary positions must include a sufficient safety margin to be able to cope with normal cyclical fluctuations in economic activity. These required safety margins may diverge from one country to another depending on the sensitivity of their economies and public finances to cyclical movements. However, other, more structural factors equally need to be taken into account to ensure that excessive deficits are avoided. For instance, it is to be expected that during the coming decades the ageing of the population will exert additional pressure on the public finances of most EU countries. In so far as this pressure is not lessened otherwise, for example by reforms in the pension systems, adequate safety margins need to be provided for this purpose, too. Similarly, Member States with a high public debt will have to take account of the fact that their budgets are more vulnerable to interest rate changes than those of countries with a lower debt ratio.

As more sustainable budgetary positions are achieved in the future, the emphasis in fiscal policy will increasingly have to be placed on the *structural shifts in the revenue and expenditure pattern which are needed to make the public finances more conducive to growth and employment. In that connection the EU's "Broad Economic Policy Guidelines" advocate curbing of the growth in public expenditure in order to permit reductions in the tax burden and allow expenditure redeployments beneficial to investment in physical and human capital. There is also a need for greater efficiency of the tax systems, while pension and health care systems must be reviewed to enable them, in the medium term, to cope with the budgetary repercussions of ageing.*

Belgian budgetary policy has in recent years been predominantly marked by the consolidation which was required in order first to fulfil the conditions for accession to monetary union and then to meet the requirements of the Stability and Growth Pact. The efforts made produced results which compare quite favourably with those of our European partner countries. The public deficit and the debt ratio, which had peaked in 1992 and 1993 respectively, had already decreased by 7 and more than 18 percentage points of GDP in 1998, the last year before the advent of monetary union. The deficit then amounted to 1.0 p.c. of GDP and the debt ratio to 117.4 p.c. of GDP.

In 1999 the overall government deficit worked out at 0.9 p.c. of GDP. That is not only better than the average result of 1.6 p.c. of GDP achieved for the euro area but also below the target of 1.3 p.c. of GDP set in the Belgian stability programme of December 1998.

The primary budget surplus, for its part, amounted last year to 6.3 p.c. of GDP, which is at least in line with the stability programme's target of "around 6 p.c." However, the primary surplus did decline slightly, by about 0.3 percentage point, compared to the previous year. As the cyclical situation was more or less neutral for the public finances, this worsening is mainly attributable to discretionary or non-recurrent factors, and in particular to the additional burden resulting from the dioxin crisis and to the reduction in employers' social security contributions. The decrease in the primary surplus was however more than compensated for by the reduction in the interest charges on the public debt, which was due both to the continuing fall in the debt ratio (from 117.4 p.c. of GDP in 1998 to 115 p.c. of GDP in 1999) and to the further decline in the average implicit interest rate on the public debt. On balance the total financing deficit still improved slightly, namely by 0.1 p.c. of GDP.

A breakdown among the various levels of general government shows that the decrease in the primary balance was mainly accounted for by the federal government, and was chiefly caused by the contraction of 0.5 p.c. of GDP in the tax revenue accruing to the federal government, after allocation of federally collected taxes to the communities and regions and the social security system, as well as by additional non-recurrent outlays amounting to about 0.2 p.c. of GDP due to the dioxin crisis. This was offset, however, by the fall in the interest burden, so that the federal government's total financing requirement remained virtually stable. The social security system's primary surplus increased slightly, so that for Entity I as a whole (the federal government and the social security system combined) the primary balance fell by about 0.3 percentage point. The norm of the stability programme, which basically required Entity I to stabilise its primary balance in relation to GDP, was thus not met. On the other hand, the primary balance of the communities and regions increased by 0.3 percentage point, to 0.8 p.c. of GDP, while that of the local authorities decreased to the same extent, to 0.3 p.c. of GDP.

During the last decade the resources allocated to the communities and regions under the Financing Act grew in real terms, on average, by nearly 4 p.c. a year. This enabled them to maintain a brisk rate of expenditure – with an average real expenditure growth of about 2.5 p.c.

per year, against only 1.5 p.c. for the other sections of general government – and at the same time to reduce their overall financing deficit and recently even to turn it into a surplus. Even if account is taken of the fact that the communities and regions were given new powers as time went on, it must be acknowledged that the provisional financing system facilitated their budgetary consolidation. Now that, in 2000, the final phase of the Financing Act has been reached, this situation will change and the revenues of the communities and regions will actually fall behind national income growth. Against this restrictive background and given the need to continue to maintain a sufficient degree of budgetary discipline in the coming years, it is essential that the different levels of government remain fully committed to attaining the objectives of the updated stability programme and that their respective responsibilities in this connection shall be clearly specified.

The renewed co-operation agreement concerning the budgetary objectives for the period 2000-2002 concluded by the federal state and the communities and regions at the end of November 1999 opens up favourable prospects from this angle, as it provides for a number of procedures which, if appropriately and coherently applied, can cause that agreement to grow into a real internal Belgian stability pact.

In the new stability programme the government undertook to maintain the primary budget surplus for general government at about 6 p.c. of GDP in the coming years and in addition to achieve budgetary balance by 2002. After that a small structural budget surplus was to be maintained, with a view to stabilising the nominal amount of the public debt, while consistently reducing the debt ratio as a proportion of GDP.

As far as the budget for 2000 is concerned, the initial aim was to achieve a small reduction of 0.1 p.c. of GDP in the deficit. This could be regarded as a compromise between two very valid but – certainly in the short term – difficultly reconcilable objectives, namely the continuation of the budgetary consolidation process and a substantial reduction of the collective burden on labour. The object of the latter is to lower the high level of labour costs in Belgium, which hampers employment growth and is partly responsible for the persistence of concealed labour circuits, and thus to strengthen the economic base. The budget was drawn up, however, starting from very cautious macroeconomic assumptions, including economic growth of 2.5 p.c. Although such a circumspect approach is to be welcomed, care should be taken to avoid regarding cyclical budgetary windfalls – which have by now become quite probable – as an additional structural policy margin which can be used to finance new initiatives without being matched by compensatory measures elsewhere. The favourable cyclical conditions therefore call for a new trade-off whereby priority is assigned, in the immediate future, to additional deficit and debt reduction. In the meantime, an assessment should be made of the effectiveness of the reductions in social charges decided upon in the past. In view of the shortages which are already observable in some regional or sectoral segments of the labour market, there is a clear need to make progress in increasing the supply of labour, since that is essential in order to enable the reduction in labour costs to be fully reflected in employment growth.

The budgetary course recommended would make it possible to build up a margin which can be resorted to later when the economic situation is less favourable. In contrast, the using up of cyclical gains nearly always has a procyclical effect : the economy is additionally stimulated at a time when there is no need for it, which increases the likelihood of inflationary overheating phenomena, while subsequently corrective measures have to be taken which additionally impede growth. Particularly in a monetary union it is of crucial importance that budgetary policy shall be allowed to play its stabilising role fully and in a symmetrical manner.

It is thus absolutely essential that the commitment in the stability programme that "the fruits of higher growth in 2000 will be primarily used to reduce the deficit" shall be strictly honoured, even if this means that the primary surplus temporarily reaches a higher level. In order to be consistent with the cyclically neutral budget strategy advocated here, it is advisable that the various budgetary norms be formulated in structural terms, i.e. corrected for temporary cyclical influences. The government's aim expressed in the new stability programme, to build up small structural surpluses after a budgetary balance has been achieved, is to be seen as a move in the right direction. Such a strategy would also benefit from an explicit setting of norms for the acceptable medium-term growth rate of primary expenditure, in order to ensure that the lightening of the fiscal and social charges remains consistent with the need to reduce the debt burden sufficiently fast.

Now that structural budgetary equilibria are within reach, the remaining period before the ageing of the population begins to take its toll offers a unique chance to take another look at the composition and quality of government action in order to improve the economy's investment climate and step up its growth potential. Possible ways of doing that include improving the quality of public services, a judicious increase in public investment, especially in network and mobility infrastructure, greater efforts in the field of scientific and applied research and optimising both school and lifelong education. Lastly, it must be understood that the additional pension and health care burdens which the ageing of the population is likely to bring about are not an inescapable factor but can be largely overcome by appropriate and forward-looking policies. Structural measures aimed at increasing labour market participation and the employment rate can help to keep the dependency ratio between non-working and working persons at a reasonable level; the progression of pension expenditure can be slowed down by, among other things, encouraging older workers to go on working longer; and medical overconsumption can be countered by giving responsibility to both the users and the providers of care.

All this calls for an integrated medium-term strategy aimed at bringing about a structural, permanent consolidation of the public finances in which the various strategic choices of budgetary policy fit in a coherent manner and in which the action taken by the various government authorities is appropriately co-ordinated.

EMPLOYMENT POLICY

In view of the rapid changes in the economy brought about by technical progress and globalisation and owing to the demographic trends which are becoming apparent and the ways in which society is evolving, the European social model must be preserved and enhanced but also reformed. This model is characterised by a relatively high level of social protection and a number of redistribution mechanisms which make it possible, in particular, to keep poverty in check. A stepping up of these systems is necessary because of the continued existence of intolerable situations of distress. But in most of the countries the model also needs to be revised, because insufficient job creation is causing it to miss its target, by relegating part of the population to unemployment, and is threatening its future. A construc-

tive social dialogue can help to bring about these essential changes.

Despite recent progress, unemployment is still too high in Europe and the employment rate is considerably lower than those of the United States or Japan. Some European countries, however, appear to have succeeded in bringing into the working circuit a proportion of the population more or less comparable to that in the United States, while at the same time achieving much better results in the battle against poverty : for instance Denmark, the Netherlands and Sweden. The efforts to promote employment must be intensified in order to reduce unemployment and give more women and men the opportunity to participate actively in social life; to increase non-inflationary growth potential and prosperity; and to support the social security systems and the public finances in coping with the ageing of the population, thanks to stronger growth and a lower dependency ratio.

Since the Amsterdam and Luxembourg European Councils, in 1997, co-ordination and multilateral surveillance of these efforts have been provided for within the framework of the European Union's broad economic policy guidelines and employment guidelines. The promotion of employment calls for a multi-dimensional strategy combining sound macroeconomic policies, an appropriate wage developments, structural reforms of the markets for goods and services and specific measures designed to improve the operation of the labour market. A "macroeconomic dialogue" on these questions was launched in 1999 by the Cologne European Council, thanks to which the political authorities, the social partners and the ECB will be able to exchange information and improve their mutual understanding in order to create the conditions for job-creating growth.

The contribution of monetary policy consists in ensuring the essential environment of stability. It is equally necessary for budgetary policies to be conducted in accordance with the Stability and Growth Pact, so as to help maintain fairly low real interest rates and open up the possibility of anticyclical lines of action, which will be all the more effective for not being perceived as a lasting relaxation in the public finances.

Wage developments must be compatible with the maintenance of price stability and the promotion of employment. Consequently, they must not lead to a substitution of capital for labour and of imports for domestic production. Furthermore, differences in productivity, be it between countries, between regions, between sectors or between skill levels, must be sufficiently reflected in labour costs. A centralisation of wage negotiations in the euro area accelerating the convergence of wage levels without taking account of the difference in national situations would be liable to cause job losses in the countries where productivity is lower. Uniformisation of wage increases leaving the differentials in levels unchanged would also be inappropriate. At the same time, preservation of the European model requires a common base of social safeguards.

The reforms of the labour market mechanisms are a major component of this overall strategy, because the low employment rate in Europe is largely structural. They will increase the advantages of keener competition on the markets for products and of the development of the information society, thanks to a better allocation of labour and the mobilisation of unemployed human resources. Since 1998, national action plans have been implementing the European Union's guidelines aimed at improving employability, developing entrepreneurship, encouraging the adaptability of businesses and their employees and strengthening the equal opportunities policy.

In Belgium, even though the employment rate rose from 1994 to 1999, it is still below the European average, which is itself too low. The efforts must therefore be stepped up.

For several years now, wage moderation has helped to slow down the substitution of capital for labour. The inter-professional agreement for the years 1999 and 2000, whose primary aim is the lasting promotion of employment, does not depart from this objective. The sectoral agreements appear to have complied with the norm for the maximum increase in nominal wages, arrived at by reference to the expected movement of wages in the three main neighbouring countries. Compliance with this rule has been facilitated by the indexation of wages on the basis of the "health index". This excludes most petroleum products and thereby limits the secondary effects of the rises in oil prices. The method of application of the norm derived from the law of 26 July 1996 concerning the promotion of employment and the preventive safeguarding of competitiveness has been slightly changed. Thus, the agreement stipulates that the movement of wages and the training and employment efforts shall be assessed simultaneously and that shortcomings in one field can be weighed against better performance in others. This greater leeway allows for a certain differentiation in wage developments. In recent years the strict application of the wage norm had the merit of ensuring the wage moderation that was needed for putting a stop to job destruction, but it was liable at the same time to be too great an obstacle to any differentiation of wage developments, while on the national plane, too, disregarding of productivity differences and local conditions leads to rationing of employment.

Reductions in social security contributions, which were stepped up in 1999, are a further means of moderating the cost of labour, provided that their proceeds are not used for wage increases. Furthermore, social contributions, together with taxation, are an instrument whereby labour costs, which must be attuned to productivity levels, can be dissociated from net incomes, the formation of which should also satisfy considerations of fairness. Thus, the determination to reduce unemployment among the least-skilled workers without lowering their standard of living justifies the retention of larger reductions in contributions on low wages.

A further requirement for increasing the employment rate and growth potential, is that a greater demand for labour shall be matched by supply, without which the shortages already evident in some quarters are liable to become more acute. Obviously, in Belgium, more extensive action needs to be targeted in three directions : increasing employment of the over-fifties, raising the skills level and preventing long-term unemployment. Moreover, it would be helpful to remove the impediments to mobility, highlighted by the marked geographical disparity in unemployment rates.

The low level of the employment rate in Belgium compared to the European average relates mainly to the low labour market participation of young people, senior citizens and women aged over forty. While the unemployment rate, and particularly that of youth unemployment, varies greatly according to region, the limited degree of participation in the labour market is a common fault. The systems particularly involved are those of early withdrawal from working life, such as the collectively agreed early retirement schemes and that for older unemployed persons not seeking jobs. Originally designed to lessen the social consequences of restructurings of enterprises and to combat youth unemployment, they have spread to such an extent that they are now established practice. These systems are in fact a burden on public budgets and deprive society of an experienced workforce. The employment rate of persons aged 50 to 64 is only 37 p.c., or one of the lowest ratios in Europe, 10 percentage points below that of the three main neighbouring countries. To increase it, even by an extension of part-time working, it is not sufficient to reduce the possibility of early retirement, but it is also necessary to promote a personnel policy which preserves the motivation and productivity of these workers, by providing continuous vocational training *sufficiently early in their careers. The inter-professional agreement and the national action plan for employment rightly regard these problems as priorities and the social partners have recently submitted proposals on this subject to the government.*

The mismatch between demand for and supply of labour is also a major source of the job shortage in Belgium. Even though the phenomenon of over-qualification, due to the recruitment policy of some firms, plays a part in cutting out less-qualified candidates, the shift in demand in favour of workers with an increasingly large fund of knowledge is above all a trend connected with technological advances. The progress needing to be made ranges from school education to continuous on-the-job training. The proportion of the population possessing a higher secondary education certificate should be increased, greater value should be attached to technical education and the gradual incorporation of young people in working life should be promoted by apprenticeship schemes. The efforts made in continuing training should be stepped up, as stated in the inter-professional agreement.

Lastly, it is essential to put an end to and prevent long-term unemployment. That is why the public authorities have taken steps to activate unemployment benefits, aimed mainly at putting low-skilled persons back to work, and have adopted measures to assist the employment of young people, which lower the barriers to entry by socialising part of the cost of first work experience. Furthermore, the competent regional administrations should adopt a customised approach in order to incorporate job-seekers more rapidly in the labour market, by a programme of rehabilitation and guidance in training and job seeking. A system of appropriate incentives could encourage participation in such a programme and proportionate penalties should be applicable in the event of refusal. Another item on the agenda is the combating of unemployment traps, those situations where acceptance of a job brings no financial advantage or even represents a loss. One helpful measure in this direction will be the raising of the lowest net wages by means of a reduction in personal social security contributions or in taxation of earned incomes.

Despite its many dimensions, the active labour market policy calls for greater simplicity, homogeneity and continuity. The proliferation of measures – the High Employment Council listed around a hundred and forty – has turned this into a jungle, has clouded perception of it by the players involved and has reduced its effectiveness. Co-operation between the federal, regional and community authorities is decisive for the necessary degree of coherence.

OTHER STRUCTURAL POLICIES

In addition to more efficient operation of the labour market, structural reforms of the markets for goods, services and capital and greater discernment in public intervention will also help to increase non-inflationary growth potential in the European Union. Improving supply conditions will give each country, especially in the euro area, the possibility of seizing the opportunities due to the integration of the markets and of reacting better to any external shocks that may *occur. Since the Cardiff European summit in 1998, such reforms have formed part of the broad economic policy guidelines. It is necessary, in particular, to expand the internal market by opening up hitherto sheltered sectors to competition, and to encourage the introduction of new techniques, a source of innovation and growth. These structural changes often do not bear fruit until after a certain period of time, but they are no less necessary for that. Sometimes, however, the advantages become evident more quickly. Thus, competition in telecommunications has already led to price reductions and a more diversified supply of services.*

In view of the high degree of openness of the Belgian economy, competition is already brisk on most of its markets for goods and on several markets for services. Economic efficiency can however be still further increased in a number of fields. The broad economic policy guidelines of July 1999 advise Belgium, in particular, to speed up the implementation of the European directives on the single market and the liberalisation of the network industries such as telecommunications, post, energy and transport. Progress has already been made in these respects. In the telecommunications industry, for instance, the backlog accumulated in the transposition of the European directives into Belgian law has been gradually worked off and competition has been organised for mobile telephones and in the national long-distance and international-communications sector. There are plans for gradually opening up postal, electricity and gas services to competition. This process already started in April 1999 for electricity sold to the largest industrial users and in June 1999 for certain postal services. A group of experts commissioned by the government recommended that this process be speeded up in the electricity industry. In addition to these sectoral provisions there has been an increase in the resources devoted to keeping watch on compliance with the rules of competition. Critical examination of the remaining legal and administrative obstacles to competition, such as the barriers to entry into certain fields, is doubtless also called for.

Furthermore, the public authorities are duty-bound to do their utmost to ensure a climate favourable to investment by means of a sound budgetary policy together with a reorientation of expenditure, adjustment of taxation and adaptation of the regulations, which will all serve to make their intervention more effective. Thus a set of measures, including an increase in public investment, should meet the demand for mobility, while respecting the environment. The creation of new products and services should be encouraged by greater support for research and development, public and private expenditure on which represented only 0.4 and 1.2 p.c. of GDP respectively in 1995, against averages of 0.7 and 1.5 p.c. in the member countries of the OECD. Stronger support should be given to the creation of new firms. The quality of the public service should be improved, the administrative simplification continued and the co-ordination of the various administrations increased.

Owing to their central role in the allocation of resources, the financial markets are also growth factors, while generating a specific activity. They are obviously the first to be affected by European monetary unification, which stimulates the development of more efficient, wider and deeper financial markets, subject to keener competitive pressure. As already mentioned, the integration of some markets is still impeded by regulatory and fiscal differences. With regard to the taxing of incomes from capital, the absence of harmonisation is furthermore liable to widen the difference in relation to the taxation of incomes from labour, a less mobile factor of production. The introduction of the euro has already led to – sometimes considerable – portfolio reallocations, owing to the disappearance of the foreign exchange risk within the euro area and the desire to increase the diversification of assets according to criteria other than the currency. An example of this is provided by the development of the balance sheets of Belgian *credit institutions : these have acquired substantial amounts of bonds in euros issued abroad by selling Belgian public debt securities and borrowing liquidity from the Eurosystem.*

The users of the financial markets have everything to gain by the integration of these markets. Companies, especially small and medium-sized enterprises, will be able to obtain venture capital more easily and individuals will have easier access to diversified financial products and services. The public authorities, too, can resort to a wider market for placing their loans. Small countries must however pursue an active policy of promoting their securities on foreign markets, in order to prevent the fact that they are smaller and less well-known from leading to a slower diversification of the portfolios of non-residents in their favour than that of the portfolios of residents to their detriment. The Belgian Treasury has taken a series of initiatives in this direction. It has already succeeded in appreciably improving its conditions for short-term financing in euros. On the other hand, the yield differential between linear bonds and ten-year German government bonds has tended to increase somewhat during the last two years. This development, which is also observable for French and Dutch bonds, appears to be mainly due to a difference in liquidity connected with the upsurge in futures on German bonds of this maturity. The concentration of issues over a smaller number of maturities, decided upon by the Treasury, is likely to increase the liquidity of the Belgian State's linear bonds.

The producers of financial services can benefit from the expansion in activity on the European markets but are also facing very keen competition. They react to this partly by regroupings, in order to achieve economies of scale and keep up with the growth in cross-border transactions. Thus, in the Belgian banking sector, a great wave of concentration involving the largest institutions already occurred from 1996 to 1998. Two characteristics of this process stand out : several operations were aimed at the development of "bancassurance" groups and there were many cross-border mergers or acquisitions. The Belgian banks, although confronted by the dwindling of foreign exchange transactions and the end of the upward movement of bond prices, are now better equipped to face increased competition. They employ various strategies, including a diversification of their activities, towards, for instance, insurance, the issuing of securities or asset management, together with an extension of these activities abroad. These rapid changes in the financial landscape are of course forcing the prudential surveillance authorities to adjust their supervisory methods.

More recently, securities depositories of various countries have also moved closer together. There are in Belgium several, generally very efficient, clearing and payment systems, some of which operate internationally. Since 1 January 1999 the Bank has exercised a surveillance, called "oversight", over these systems, in order to promote their efficiency and soundness, with reference to the rules produced by the European System of Central Banks and the G10 central banks.

The regrouping movement also affects the stock markets, which are furthermore exposed to potential competition from new, entirely electronic trading systems for use by institutional investors. The Brussels Stock Exchange, the CIK and Belfox merged in 1999 to form Brussels Exchanges (BXS). The latter body decided to participate in the project for a common trading platform of eight European stock exchanges. Compared to other financial centres, the Belgian Stock Exchange suffers from a relatively low capitalisation, too small a number of very large listed companies and a fairly pronounced concentration of the shareholdership. The lack of sufficiently well known and liquid securities did in fact depress prices in 1999, a year during which the diversification of portfolios seems to have primarily involved the main securities and the largest markets. Provided, *however, that it actually becomes part of a sufficiently integrated European entity, the Brussels Stock Exchange will still render appreciable services to the Belgian economy, and especially to smaller enterprises wishing to finance their growth. It creates value added not only through its own activity but also thanks to the activities which it is helping to develop in the fields of financial analysis, asset management, the issuing and placement of securities or assistance in connection with mergers and acquisitions.*

CONCLUSION

The immediate economic future looks promising. For the euro area, in particular, the prospects have steadily improved in recent months, influenced by the picking-up of the international markets but above all by strong domestic demand. The stable macroeconomic policy framework created by European monetary union and the results of the considerable efforts made in the European Union in recent years to put the public finances on a sound footing and promote employment have undoubtedly contributed to this.

Despite the dioxin crisis the Belgian economy, too, achieved a much better growth result in 1999 than was thought possible only a few months ago. Thanks to a resolute course, pursued for many years, of macroeconomic stability, budgetary consolidation and income moderation, and to the increase in the employment-content of economic growth, a solid foundation has been laid. In recent months the confidence of both consumers and producers has risen to historically high levels. As for the entire euro area, there is the prospect of an economic expansion phase which can be both strong and lasting.

Advantage must be taken of these favourable circumstances in order to speed up the process of removing the two most important structural handicaps of the Belgian economy : the high public debt and the low activity and employment rate.

The forthcoming period of strong growth is in the first place a perfect opportunity for accelerating the consolidation process planned in the new stability programme and thereby reducing the weight of the public debt to a greater extent than was scheduled. Cyclical budgetary windfalls must thus be used primarily for additional deficit reduction, so as to enable budgetary policy to play an activity-stabilising role in accordance with the European Stability and Growth Pact. But it will be equally necessary to create more scope for a revised revenue and expenditure policy making the greatest possible contribution to strengthening the economy's growth potential. To this end, the coherent medium-term strategy required will have to be based on a judicious combination of a further reduction of the fiscal and parafiscal burden on labour, constrained growth in expenditure and an improvement in the effectiveness of public intervention. The coming decade will be particularly propitious for such an undertaking. To the extent that the best possible advantage is taken of these opportunities and the handicap of the high level of the public debt is overcome, the burden which an ageing population will subsequently bring can be better coped with.

This demographic trend is also a challenge for labour market policy, since, with an unchanged activity rate, it will cause the supply of labour to shrink considerably, and thus also possibly impair the economy's growth potential. In order to safeguard this, participation in the labour market must be vigorously stimulated, especially as the buoyant growth expected is liable to further increase the shortages already appearing in certain segments of the labour market. For all these reasons concerted efforts must be made to avoid and reduce long-term unemployment, to increase the participation of older workers and, more than ever, to improve the level of training both for workers and for those not in employment. This will enable the policy of reducing the burdens on labour to be reflected fully in greater employment.

Finally, lasting growth in activity and employment also requires greater attention to be paid to the supply side of the economy. In an ever more integrated world which is characterised by keener competition, the dynamism of a developed economy such as that of Belgium depends entirely on its ability to tap new technologies and markets and to equip the population for the knowledge and information society.

The year 2000 has begun under a particularly favourable economic constellation. Both in the government budget and in the labour market, spontaneous improvements are to be expected. But these are no justification for complacency. They must serve as an incentive to give the Belgian economy a structural boost and to improve its performance in a world where frontiers are becoming increasingly blurred. Attention must remain focused on the future. Because this future is being prepared today.

Brussels, 2 February 2000.

Economic and financial development

1. INTERNATIONAL ENVIRONMENT

1.1 SUMMARY

After being severely checked by the financial turmoil on the emerging markets, the growth rate of the world economy climbed back from 2.2 p.c. in 1998 to 3 p.c. in the year under review, though it was still well below the 1997 figure of 4.2 p.c. It was mainly the Asian countries which contributed to this revival, while the other economies generally grew at a slower pace.

The acceleration in world growth gave the lie to the rather pessimistic outlook suggested for the year under review at the end of 1998. For example, for 1999 the OECD predicted a marked slow-down in the United States, virtual stagnation in Japan and the emerging Asian countries, and global growth of around 2 p.c., practically the same as in 1998. The negative risks associated with this forecast, particularly the risk of a new crisis in certain emerging countries and continuation of the recession in Japan, were also regarded as high. These scenarios did not materialise and the situation generally improved more than expected, apparently even surpassing the forecasts published by the OECD in its Economic Outlook in December 1999, the main source of the data discussed in this chapter.

TABLE 1 — GROWTH OF THE WORLD'S MAIN ECONOMIES

(Percentage changes in GDP at constant prices compared to the previous year)

	1998	1999	p.m. Weight in the world economy[1]
United States	4.3	3.8	20.8
Japan	−2.8	1.4	7.4
Euro area	2.8	2.1	15.5
Other European Union countries	2.4	2.0	4.4
Other advanced countries[2]	3.3	3.2	3.9
Emerging Asian economies[3]	−6.4	3.7	7.6
China	7.8	7.1	12.5
Latin America	1.5	−0.5	8.9
Russia and other transition countries[4]	−0.6	1.6	4.3
Other countries	1.7	2.5	14.7
World	2.2	3.0	100.0

Sources : OECD, IMF.

[1] Percentages of world GDP in 1998 based on 1997 purchasing power parities and constant prices.

[2] Australia, Canada, New Zealand, Norway, Switzerland.

[3] South Korea, Hong Kong, Indonesia, Malaysia, Philippines, Singapore, Taiwan, Thailand.

[4] Albania, Bulgaria, Estonia, Hungary, Latvia, Lithuania, Poland, Czech Republic, Romania, Slovakia, Slovenia and countries of the Commonwealth of Independent States other than Russia.

Thus, there was a vigorous return to growth in most of the emerging Asian economies, which had been hit by a severe recession in 1998, many of them having implemented effective macroeconomic stabilisation programmes and initiated structural reforms. The rate of expansion of the Chinese economy, affected by the slowdown in exports, dipped slightly in the first half year but subsequently stabilised at a level which was still very high, and actually almost unequalled elsewhere in the world. The transition countries as a whole also moved back into expansion in 1999.

Japan's GDP, which had been falling continuously since the middle of 1997, increased during the year under review. This recovery was brought about by an improvement in consumer confidence, itself encouraged by the on-going reform in the financial sector. The continuing, resolutely expansionist stance on fiscal policy was also a factor, but at the expense of an increasingly serious deterioration in the Japanese public finances : the public debt rose to a very high level and is ballooning rapidly. Fiscal policy, which provides the short-term foundation for the as yet fragile recovery, is therefore subject in the longer term to the constraint of radical reform, especially as the effects of the ageing of the population will be felt more keenly in Japan than in most other advanced countries.

In the euro area, growth was about three quarters of a point lower in 1999 than in the previous year, but this weaker performance is mainly a reflection of the deceleration between the third quarter of 1998 and the first quarter of the year under review. Thereafter, in contrast, the rate of expansion strengthened steadily in most countries in that region. Despite the slower average increase in activity in 1999, the labour market of the euro area did improve : for the second consecutive year, employment expanded substantially and there was a significant fall in unemployment. This result may be due in part to the wage moderation in recent years and to economic policies which are geared more to job creation.

In the United Kingdom, the slowdown in activity seen since the peak reached in 1997 gave way to a strong recovery from the second quarter of the year under review. The latter movement was fuelled by final domestic demand, while the contribution of net exports, still affected by the strength of sterling, remained negative. Average GDP growth over the year was still half a point down, remaining slightly below the figure for the euro area.

In the United States, the turn-round in the cycle, or at the very least the return to more moderate growth, said to be in the offing on several occasions in earlier years, especially at the end of the previous year, was once again deferred : the expansion of activity remained almost as strong in 1999 as in 1998, and was sustained at a much higher rate than in the other advanced countries. This performance, achieved by an economy which has practically the highest level of development in the world, continues a trend which began some twenty years ago. Comparison with Japan and the euro area for each economic cycle in fact shows that the difference in growth has constantly widened since the 1970s in favour of the United States. In particular, the cyclical upswing which the US economy has enjoyed since 1991 has been surprising in its duration and vigour, as well as in its intensification during the period. In the last two decades, the strong relative growth in the United States has been founded on an expanding labour supply and, more recently, faster assimilation of technological progress than in other economies. Not only has the demographic basis of the labour market in the United States been more dynamic than that of the other advanced countries, but the market has also demonstrated a greater capacity to mobilise the population of working age. Furthermore, maintenance of a particularly high rate of expansion in the US economy and the ensuing absorption of unemployment have been achieved without pushing up prices. However these developments were accompanied by the emergence of a high and growing current account balance of payments deficit.

TABLE 2 — LONG-TERM TREND OF THE GDP OF THE MAIN ECONOMIES AT CONSTANT PRICES

(Average percentage changes per economic cycle[1] compared to the previous year)

	Earlier complete cycles		Current cycle
	Cycle before last	Last cycle	
United States	2.7	3.5	3.6
Japan	3.8	3.0	1.2
Euro area	2.3	2.4	2.1

Source : OECD.

[1] Complete economic cycles are defined as periods between two consecutive troughs, namely : 1975-1982 and 1982-1991 respectively for the United States ; 1975-1986 and 1986-1995 for Japan ; 1975-1983 and 1983-1993 for the euro area. The current cycle is defined as the period since the last cyclical trough, namely 1991, 1995 and 1993 for the United States, Japan and the euro area respectively.

1.2 ACTIVITY

United States

In 1999, GDP grew by 3.8 p.c. in the United States. Activity was driven exclusively by final

TABLE 3 — EXPENDITURE IN THE UNITED STATES

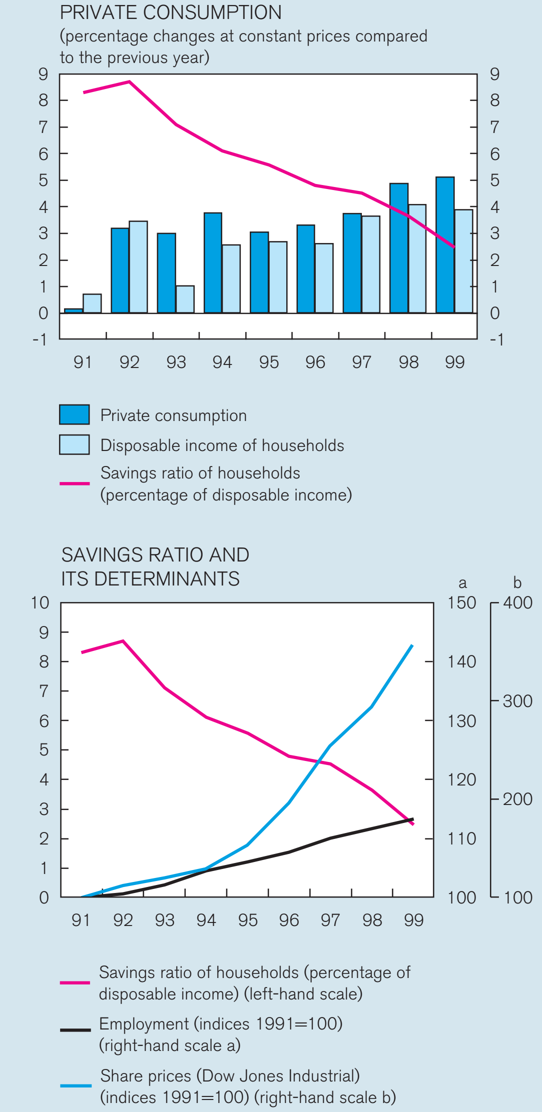
(Percentage changes at constant prices compared to the previous year)

	1998	1999	1999 p.m. Contribution to the change in GDP
Final domestic demand	5.4	5.4	5.5
Private consumption	4.9	5.1	3.4
Public consumption	1.3	2.3	0.3
Investment in housing	9.2	6.6	0.3
Investment by enterprises	12.7	9.1	1.2
Public investment	4.0	7.1	0.2
Change in stocks [1]	0.1	−0.5	−0.5
Net exports of goods and services [1]	−1.3	−1.3	−1.3
Exports	2.2	3.4	0.4
Imports	11.6	12.0	1.7
GDP	4.3	3.8	3.8

Source: OECD.

[1] Contribution to the change in GDP.

CHART 1 — PRIVATE CONSUMPTION AND SAVINGS RATIO IN THE UNITED STATES



Sources: OECD, NBB.

domestic demand, while the change in stocks and that in net exports of goods and services both made a negative contribution.

All components of final domestic demand contributed to the expansion. Public consumption and public investment, which saw the strongest rise since the start of the decade, boosted growth but made only a modest contribution on account of the singularly small proportion of GDP which they represent. Growth was sustained mainly by private consumption, and investment by enterprises and households.

The buoyancy of household consumption, which represents over two-thirds of GDP, is derived both from the rise in the disposable income of households and from a further decline in the savings ratio. The latter has fallen almost continuously since the low point of the cycle in 1991, when it represented 8.3 p.c. of disposable income, dropping to 2.5 p.c. in 1999. This dramatic fall may be attributed mainly to two factors. One is the uninterrupted expansion of employment and the steadily weakening unemployment, giving households a feeling of security and bolstering their confidence. The other is the stock market boom, with prices almost tripling between early 1995 and mid-1999, creating a wealth effect, especially as one-third of household financial assets consist of equities. The asset position of these economic agents therefore improved, at least at market prices : their level of debt increased sharply but their assets grew even more quickly.

During the year, the composition of demand – which remained strong – altered slightly. In the second half-year the external balance made a smaller negative contribution to growth, particularly thanks to a stronger expansion of the export markets, while the increase in final domestic demand slowed down somewhat. In particular, demand from households was curbed by the moderation of the rise in their real incomes and by the slowing, on average, of the rise in share prices. Moreover, the increase in interest rates added to their debt burden and discouraged their spending somewhat.

TABLE 4 — EXPENDITURE IN JAPAN

(Percentage changes at constant prices compared to the previous year)

	1998	1999	
			p.m. Contribution to the change in GDP
Final domestic demand	−3.3	1.5	1.4
Private consumption	−1.1	1.7	1.0
Public consumption	0.7	0.7	0.1
Investment in housing	−13.7	3.1	0.1
Investment by enterprises	−11.3	−5.6	−0.9
Public investment	−0.3	13.9	1.1
Change in stocks [1]	−0.1	0.1	0.1
Net exports of goods and services [1]	0.6	−0.1	−0.1
Exports	−2.3	0.3	...
Imports	−7.5	1.1	0.1
GDP	−2.8	1.4	1.4

Source : OECD.
[1] Contribution to the change in GDP.

Japan

Growth seems to have been resumed in the Japanese economy during the year under review. GDP rose by 1.4 p.c. in 1999, whereas in 1998 it had contracted by 2.8 p.c.

Public investment, which, during the year under review, took place in implementation of the macroeconomic recovery plans announced in 1998, was by far the most dynamic component of expenditure : it increased by 13.9 p.c. and contributed 1.1 percentage points to the growth of GDP. Furthermore, the granting of temporary tax cuts also stimulated investment in housing.

The raising of the ceiling on the credit guarantee system at the end of 1998 in favour of small and medium-sized enterprises permitted a sharp increase in the outstanding total of these guarantees and probably explains the substantial decline in the number of bankruptcies recorded during the year under review. In the banking sector, a few institutions were declared bankrupt in 1999, but they were relatively modest in size and the resulting financial shortfalls were considerably smaller than those of the two big banks provisionally placed under public administration at the end of 1998. The recapitalisation of the financial sector with the aid of public funding was also on a larger scale in 1999 than in the previous year : fifteen big banks together used 7,500 billion yen out of the total budget of 25,000 billion made available for the recapitalisation of the banking sector, or four times the amount recorded up to the end of 1998. Although complete reform will take a long time and entail some uncertainty, the stabilisation of the banking system in 1999 was welcomed by the financial markets. For instance, risk premiums on short- and long-term loans by Japanese banks, which had reached very high levels for a time at the end of 1998 and the beginning of 1999, have declined significantly since then.

The reduction in the total number of bankruptcies and the gradual calming of the anxieties caused by the situation in the financial sector improved household confidence and that increased private consumption, following the slump in 1998. The large contribution of this expenditure category to growth was, however, neutralised by the contribution from investment by enterprises, which suffered a further dramatic fall in 1999. The persistent weakness of this investment activity is due to the rate of utilisation of production capacities, which has remained exceptionally low.

Net exports, which had made a very positive contribution to growth in 1998 owing to the decline in imports associated with falling domestic demand, ceased to make any contribution in 1999. The expansion of the export markets influenced by such factors as the recovery in the emerging countries of Asia was almost entirely offset by the loss of competitiveness due to the appreciation of the yen. Imports increased slightly in 1999 owing to the recovery in domestic demand.

TABLE 5 — EXPENDITURE IN THE EURO AREA

(Percentage changes at constant prices compared to the previous year)

	1998	1999	
			p.m. Contribution to the change in GDP
Final domestic demand	2.9	2.7	2.6
Private consumption	2.9	2.4	1.3
Public consumption	1.3	1.6	0.3
Investment in housing	−0.2	1.9	0.1
Investment by enterprises	6.6	5.9	0.7
Public investment	3.5	3.8	0.1
Change in stocks [1]	0.5	−0.1	−0.1
Net exports of goods and services [1]	−0.5	−0.5	−0.5
Exports	4.3	0.9	0.2
Imports	8.3	4.0	0.6
GDP	2.8	2.1	2.1

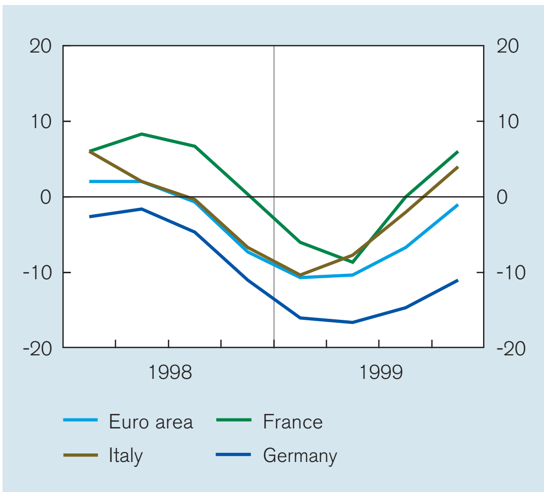
Source: OECD.
[1] Contribution to the change in GDP.

Euro area

Economic growth in the euro area was somewhat less sustained than in the previous year, declining from 2.8 p.c. in 1998 to 2.1 p.c. in 1999. The fall was particularly marked in the case of exports of goods and services, which, especially at the beginning of the year, were still suffering the effects of the weakness of imports by some emerging or transition countries, while the positive contribution to growth made by the change in stocks in 1998 turned slightly negative. On the other hand, final domestic demand from the private sector remained steady, especially in the case of investment by enterprises. For their part, public consumption expenditure and gross fixed capital formation increased at a higher rate.

These movements were not uniform during the year under review. The slowing of activity which became apparent in the second quarter of the previous year, coinciding with the deterioration in the international environment, persisted during the early months of 1999. It then gave way to steadily strengthening growth, as is evidenced

CHART 2 — CONFIDENCE INDICATOR FOR ENTERPRISES IN THE EURO AREA



Source : EC.

by the trend of the confidence indicator for enterprises in the euro area, which is closely correlated with the cyclical component of quarterly GDP and has the advantage of being available almost immediately.

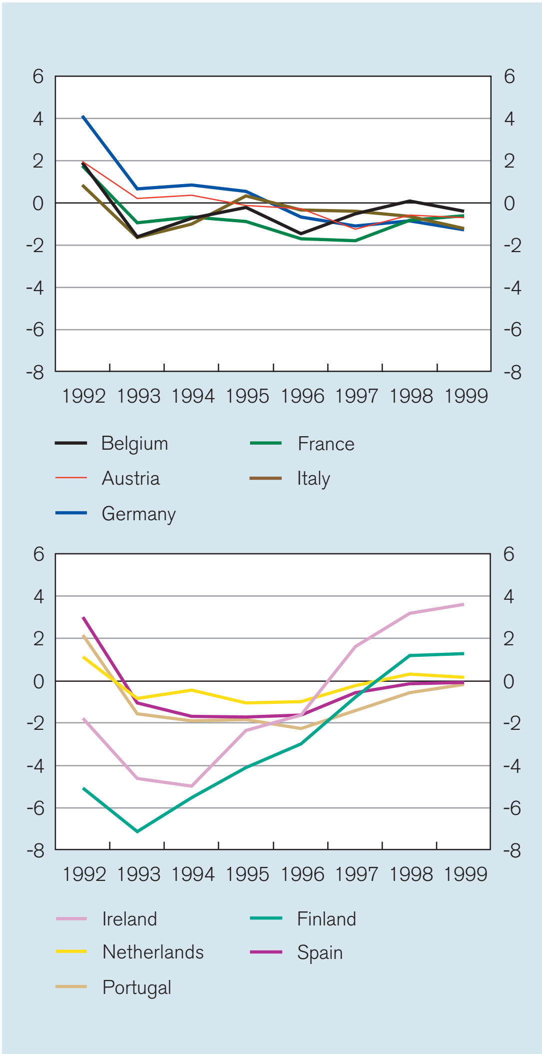
In Italy, however, the upturn in this confidence indicator took place slightly earlier than in the other leading economies of the euro area. The relatively large share of the emerging economies and transition countries in Italy's export markets may have been a factor here : Italian exports were particularly affected by the slackening of demand from those economies between the first quarter of 1998 and the first quarter of 1999, and subsequently benefited more from their recovery. In addition, exports suffered as in the previous year from the mediocre competitiveness of production costs. On annual average, the external balance was a factor which seriously slowed down the growth of GDP in both 1999 and 1998. In contrast, domestic demand – sustained partly by investment in equipment and non-residential building – remained buoyant. Overall, Italy's GDP increased by only 1 p.c. in 1999, against 1.3 p.c. the previous year. This slowdown throughout 1999 came about because the growth achieved at the beginning of the year was weaker than twelve months earlier, a handicap which similarly affected most other countries in the euro area.

In Germany the GDP growth rate dropped from an annual average of 2.2 p.c. in 1998 to 1.3 p.c. in 1999. This slowing was due primarily to stocks, whose contribution to growth, after having been very positive in the previous year declined almost to zero this year. The increase in exports of goods and services was appreciably smaller than in the previous year, but the decline of the rate of expansion of imports was almost as great, so that there was only a marginal rise in the negative contribution to growth made by the external balance. On the other hand, the expansion of final domestic demand fuelled by the very strong growth in investment by enterprises accelerated slightly.

Of the three large countries in the euro area, France enjoyed the strongest growth, as in the previous year. Its GDP grew by 2.4 p.c., or 1 point less than in 1998. As in Germany, this deceleration was very largely due to the fall in stocks and was slightly accentuated by a less favourable contribution from foreign trade. Unlike in Germany, private consumption had a significant slowing effect. However, investment was still vigorous, especially that in the building of residential housing, which speeded up.

CHART 3 — ECONOMIC CYCLES IN THE EURO AREA

(Percentages by which actual GDP deviates from the trend GDP) [1]



Source : EC.

[1] The trend GDP is estimated by the EC using the Hodrick-Prescott method.

Since the decline in the growth of GDP was more marked in France than in Germany, and even more so than in Italy, the disparity in the growth rates of these three large countries, which had increased slightly in 1998, was partly reduced during the year under review.

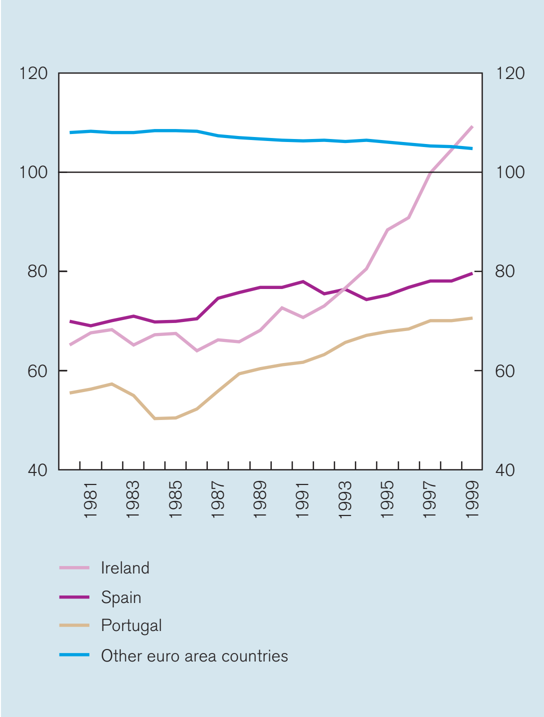
However, differences in gross growth rates are only an imperfect yardstick for measuring divergences in economic situations. Apart from random and seasonal fluctuations, the expansion of an economy can in fact be divided into two elements : a trend component, which reflects the equilibrium growth path for that economy, and cyclical movements, defined as the deviations between the actual growth and the trend rate. Provided that it is measured reliably, the second component provides, in principle, some indications of the tensions between supply and demand, and hence of the future movement of prices. In this connection, data relating to the differences in cyclical situations between countries in the euro area are particularly interesting, since they may reveal potentially divergent inflation rates.

The spread in the cyclical situations between Germany, France and Italy, measured for each country by the difference between actual GDP and trend GDP, has become extremely small since the mid-1990s. Moreover, since 1997, growth in each of these three countries has been closer to the equilibrium rate. If we consider movements over a longer period for all euro area countries, we also find a considerable increase in the convergence of economic cycles within the euro area since 1992, i.e. since the start of the process of transition to EMU provided for by the Treaty of Maastricht. The cyclical differences between the member countries have not entirely disappeared, but they can now be said to be small, given the diversity of levels of development in the area in question.

However, this process of cyclical convergence, reflected in a narrowing of the deviations from the trend GDP, does not in any way mean that the growth rate is the same in all countries in the area. On the contrary, differences are desirable, in that the regions whose development is lagging behind must ultimately be able to catch up with the others. And this does seem to be happening to some extent : the countries with the lowest per capita GDP at the start of the 1980s have now moved closer to the average or even slightly above it.

CHART 4 — TREND GDP PER INHABITANT IN THE EURO AREA

(Indices for euro area = 100) [1]



Sources : EC, NBB.
[1] Not including Eastern Germany.

1.3 LABOUR MARKET

In 1999 the unemployment rate declined once again in the United States, falling to 4.2 p.c. of the labour force against 4.5 p.c. the previous year. It also dropped in the euro area, where it was down from 10.9 to 10 p.c. By contrast, in Japan it increased again, rising from 4.1 to 4.7 p.c. In each of these three large economies the activity rate remained practically unchanged in relation to 1998, so that changes in unemployment essentially reflected opposing movements in the numbers in work.

These developments are largely due to the very different stage of the cycle in the three economies in question. They are also attributable to differences in the trend rate of expansion in these economies, which was highest in the United States, largely because of the faster assimilation of technical progress. But unemployment rates must also be assessed in the light of the structural divergences in the ability of these economies to bring the population of working age onto the labour market. The euro area suffers from a serious handicap in this respect, as is evident from a comparison of the respective levels of activity, employment and unemployment.

TABLE 6 — LABOUR MARKET

(Percentages)

	1991	1998	1999
United States			
Activity [1]	76.2	77.7	77.8
Employment [2]	71.0	74.2	74.6
Unemployment [3]	6.7	4.5	4.2
Japan			
Activity [1]	75.2	78.1	78.1
Employment [2]	73.6	75.0	74.4
Unemployment [3]	2.1	4.1	4.7
Euro area			
Activity [1]	65.7	65.8	66.1
Employment [2]	60.3	58.5	59.3
Unemployment [3]	8.3	10.9	10.0

Sources : EC, OECD.
1 Ratio of labour force to population of working age (15 to 64 years).
2 Ratio of number of persons in employment to population of working age.
3 Ratio of number of unemployed persons to civilian labour force (standardised data).

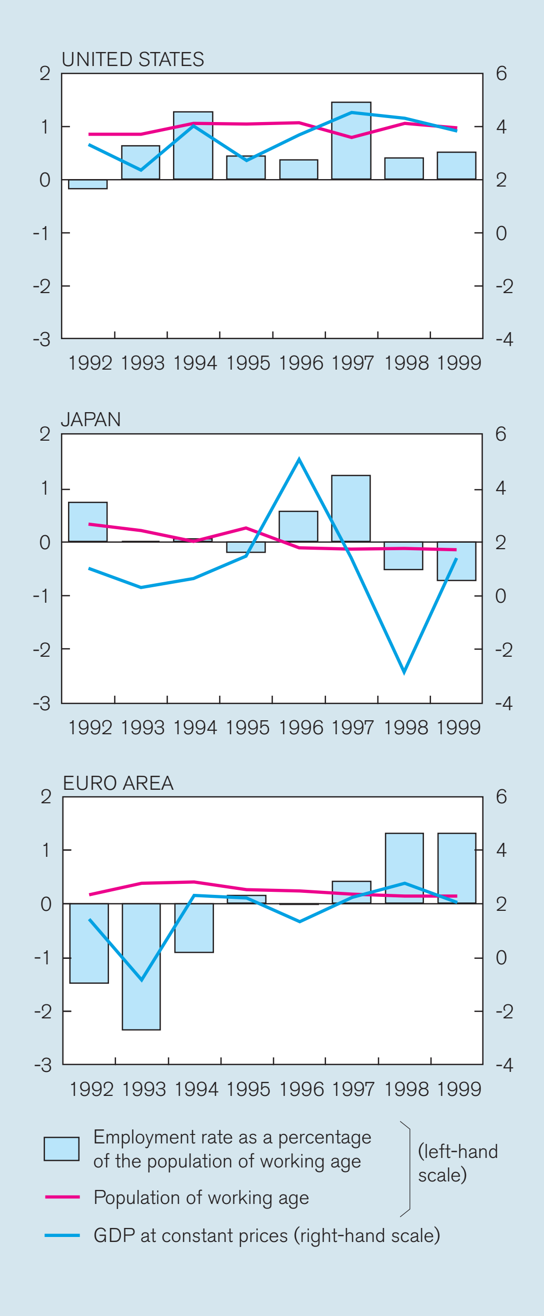
Thus, in 1999 the unemployment rate in the United States dropped to its lowest level since the beginning of the 1970s, falling below the Japanese rate for the first time. In Japan, where unemployment had been consistently below 3 p.c. of the labour force during the 1970s and 1980s, the level reached during the year under review is a historical record. However, it is less than half the figure for the euro area, where the activity rate, i.e. the ratio of the labour force to the population of working age, has in fact remained well below that in the other two major economies. During the past year, the employment rate, defined as the percentage of the population of working age actually in work, was therefore considerably lower in the euro area than in the rest of the industrialised world, remaining below 60 p.c., while it was almost 75 p.c. in the United States and in Japan. This characteristic is found in all EMU countries except Luxembourg. On the other hand, the unemployment rate in the Scandinavian countries (Denmark, Norway, Sweden) has fallen considerably since the 1993 cyclical trough, despite them having some of the highest activity rates among the advanced countries.

This poor performance by the labour market in the countries of the euro area is largely a legacy from the past : by the start of the decade, the employment rate there was already well below that of the other two major economies. However, the difference in relation to the United States has subsequently widened further.

The labour market has in fact proved particularly dynamic in that country, as is evident from its greater capacity for mobilising the population of working age. Since the 1991 cyclical trough, the activity rate and the employment rate, which were already very high at the start, increased almost uninterruptedly, from 76.2 and 71 p.c. respectively of the population of working age during that year to 77.8 and 74.6 p.c. in 1999. Since 1993 the unemployment rate has fallen steadily, dropping by a total of 3.2 points. This improvement, due to the strong economic growth but also to a highly flexible labour market, is all the more remarkable in that it took place in the context of sustained population growth : as a result of natural growth and immigration, the total population of the United States increased by an average of 0.9 p.c. per annum over the period from 1992 to 1999, and the population of working age grew by around 1 p.c.

CHART 5 — MOBILISATION OF THE POPULATION OF WORKING AGE ON THE LABOUR MARKET

(Percentage changes compared to the previous year)



Source : OECD.

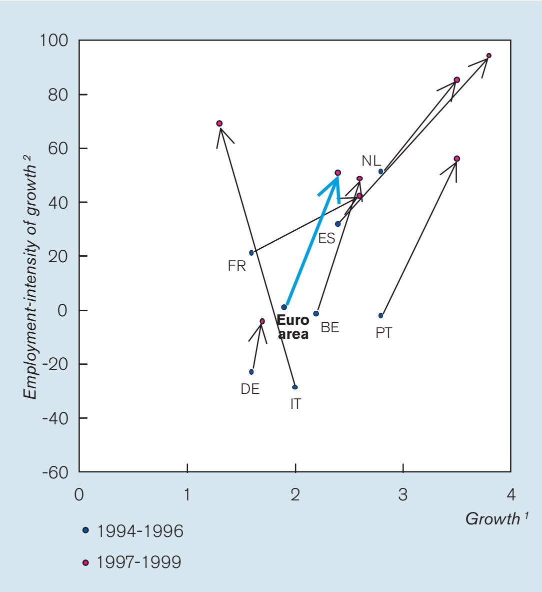
In Japan, where the population of working age remained virtually unchanged over the same period, the activity rate increased from 75.2 p.c. in 1991 to 78.1 p.c. in 1998, stabilising at that level last year. In contrast, the employment rate presented an uneven pattern. From 1991 to 1997 it increased overall despite the low rate of economic growth during that period, thanks to Japanese labour market practices, which encourage flexible pay and working hours in a context of individual job security; but the expansion in total employment was not sufficient to absorb the growth in the labour force. This led to a rise in unemployment, from 2.1 p.c. of the labour force in 1991 to 3.4 p.c. in 1997. The rise in the number of unemployed accelerated from 1998 onwards, as the depth of the recession made falling employment inevitable, even in the special context of Japan.

In the euro area, where the labour market situation was least favourable from the outset and the population of working age increased only slightly, the progress made since the start of the decade has been lacklustre. Even in relation to the 1993 cyclical trough, the activity rate and the employment rate grew respectively by only 1 and 1.3 points overall during the next six years, while the unemployment rate fell by only 0.9 point.

Nevertheless, there appears to have been a certain turn-round during the sub-period in question. During the first three years of this cyclical upswing, the labour market position deteriorated on average, but it showed a strong recovery in the subsequent three years. That recovery is doubtless partly attributable to the slightly faster pace of expansion in output. But it is chiefly due to an increase in the employment-intensity of economic growth, defined as the ratio between the rate of change in employment and the rate of increase in GDP at constant prices. Thus, the annual average growth rate of 1.9 p.c. achieved from 1994 to 1996 brought no increase in employment, while the 2.4 p.c. growth from 1997 to 1999 was accompanied by an average annual increase in employment of 1.2 p.c., which means that the employment-intensity of growth in the euro area increased from zero to just over 50 p.c. from one period to the next. Indeed, this intensity increased in all euro area countries, including those where growth slackened, the only exception being Luxembourg, where the initial position was particularly favourable.

This apparent acceleration in job creation in recent years is due partly to wage moderation throughout the second stage of EMU. The persistence of high unemployment, greater awareness of the link between wage costs and employment and the prospect of exchange rate parities being irrevocably fixed with the advent of the euro contributed towards this development. The latter was actually reinforced during the period : from 1997 to 1999, compensation per employee in the enterprise sector increased by an annual average of just 1.4 p.c. against an annual average of 3 p.c. from 1994 to 1996.

CHART 6 — GROWTH AND EMPLOYMENT-INTENSITY OF GROWTH IN THE MAIN EURO AREA COUNTRIES



Source : OECD.

[1] Average percentage annual change in GDP at constant prices.

[2] Ratio between average annual percentage changes in employment and in GDP at constant prices (percentages).

The improvement in the employment-intensity of growth also coincides with the greater priority assigned to employment in European economic policy since the 1997 Amsterdam European Council introduced provisions into the Treaty of Rome aimed at laying the foundations for a common employment strategy. This new approach was reflected in the coordination of national employment policies according to common guidelines and multilateral monitoring based on the presentation of multiannual action plans by the EU Member States. In this context, the latter adopted various measures aimed at enhancing the efficiency of the labour market, e.g. by reducing the compulsory levies on earned incomes.

A further step in the coordination of European employment-promotion policies was taken at the Cologne European Council in June 1999 with the conclusion of an Employment Pact, comprising as its main provision the decision to organise on a formal basis a regular exchange of views between the Council, the Commission, the European social partners, and the ECB on the direction to be taken by economic and employment policies in the EU. The purpose of this discussion, known as the “macroeconomic dialogue”, is to enable all these agents to contribute towards creating more jobs, while preserving their respective independence, on the basis of strong, non-inflationary growth, mainly thanks to a development of incomes compatible with these objectives.

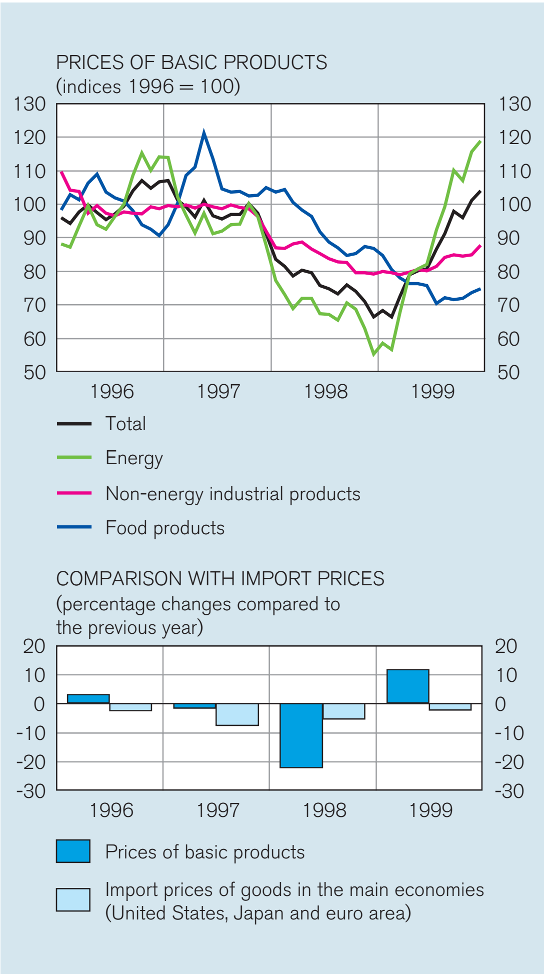
1.4 PRICES AND COSTS

Inflation remained low in the advanced countries during the year under review. Overall, the progress achieved was less striking than in

1998, notably because of the generally smaller decline in imported costs.

Import prices were influenced by the movement of crude oil prices. In December 1998 the downward trend of crude prices which had persisted for about two years came to an end. The price of Brent crude, which was down by then to around 10 dollars per barrel, subsequently remained more or less stable early in 1999. However, from March onwards it rose rapidly as a result of the voluntary output restrictions applied by many oil-exporting countries and the recovery in world demand, particularly in the emerging Asian countries. The temporary halting of exports by Iraq, coupled with the very low level of world stocks and the fear that reserves would be formed at the end of the year to guard against the risks of computer problems due to the transition to the year 2000, reinforced the price rise at the end of the year. In December the price of Brent averaged around 26 dollars per barrel, or well over twice the lowest figure reached in 1998.

CHART 7 – PRICES OF IMPORTS AND BASIC PRODUCTS IN US DOLLARS



Sources : HWWA, OECD.

Seen in historical perspective, the price recorded in December 1999 is not particularly high. The decline in oil prices at the end of 1998, due mainly to the dip in world growth and very favourable climatic conditions, had been exceptionally sharp. Account being taken of the rise in the general level of prices, the real price of crude had fallen at that point to the level prevailing immediately before the first oil shock. The 1999 rise in prices therefore represented in part a return to an absolute and relative price level closer to the figures observed on average since the reverse oil shock in 1986.

The macroeconomic impact of the 1999 rise in the price of crude oil was therefore not comparable to that of the oil shocks in 1973-1974 and 1978-1981. Moreover, the economies of the industrialised countries have become less sensitive to fluctuations in crude prices over the years. In these countries, energy consumption per unit of output has in fact fallen steeply since the 1970s, a trend due partly to the growing importance of the service sector and to energy-saving measures. At the same time, energy dependence, defined as the share of imports in energy consumption, and the share of oil and gas in energy imports, have declined. In 1999 the deterioration in the terms of trade caused by the rise in the price of crude was therefore limited in the case of the industrialised countries. Thus, for the euro area, if the oil price remains at its December 1999 level, namely 26 dollars per barrel, then – all other things being equal – the real loss of income in annual terms represented by this doubling of the price in relation to

TABLE 7 — CONSUMER PRICES

(Percentage changes at constant prices compared to the previous year)

	1998			1999[1]		
		p.m.			p.m.	
		Unit labour costs in enterprises[2]	Prices of imported goods		Unit labour costs in enterprises[2]	Prices of imported goods
United States	1.6	2.6	−5.9	2.2	2.3	−0.3
Japan	0.6	2.2	−5.4	−0.3	−2.8	−12.6
Euro area[3]	1.1	−0.4[4]	−2.3	1.1	1.4[4]	−0.4

Sources: OECD, EC, NBB.

[1] In the case of consumer prices in Japan: percentage changes in the average over the first eleven months of 1999 compared to the average for the first eleven months of 1998.

[2] Industrial and service enterprises in the private and public sectors.

[3] Harmonised consumer prices.

[4] Excluding Luxembourg.

1998 would be only about one quarter and one seventh of the losses suffered respectively at the time of the oil shocks in 1973-1974 and 1978-1981. On annual average, the rise in the price of a barrel of oil in 1999 represented only about two-fifths of this hypothetical figure, so that the loss of income for the year under review was far smaller still.

In all, the energy price index expressed in dollars rose by 30 p.c. compared to 1998. The continuing fall in the price of other commodities and basic products, averaging some 8 p.c., only partially offset that increase. The overall price index for basic products expressed in dollars therefore rose by 12 p.c. in 1999, whereas it had fallen by 22 p.c. the previous year.

Despite this rise in the prices of basic products, import prices expressed in dollars continued to fall in the main economies in 1999, although the fall was less pronounced than in the previous year. Their fluctuations in fact depend largely on the movement of prices of manufactured products, which are becoming a steadily more important part of world trade in goods. The large drops in import prices expressed in dollars, recorded in recent years for manufactured goods, may be attributed to the low level of inflation in the leading economies. As a consequence of the particularly fierce competition in international trade, these prices are not generally keeping pace with the rise in national consumer prices. Furthermore, the relatively slow expansion of world trade may have continued to influence the decline in external trade prices in 1999.

In the United States, the rise in consumer prices remained moderate, although the pace quickened slightly from 1.6 p.c. in 1998 to 2.2 p.c. in the year under review. This was due to the marked slowing of the fall in import prices. The increase in unit labour costs slowed from 2.6 p.c. in 1998 to 2.3 p.c. in 1999 owing to a less rapid rise in compensation per employee, namely 4.4 p.c. in 1999 against 4.9 p.c. in 1998, while the improvement in labour productivity remained practically unchanged.

The strong appreciation of the yen, on average, over the year under review more than offset the rise in the price of crude oil imported by Japan, so that import prices in that country fell by 12.6 p.c. Owing to the persistently unfavourable situation on the labour market, compensation per employee declined by 0.4 p.c. in 1999. After a substantial 2.3 p.c. fall in 1998, labour productivity rose by 2.5 p.c. in 1999 owing to the economic recovery, but also to the decline in employment. Consequently, unit labour costs fell sharply, namely by 2.8 p.c. However, the large fall in total production costs was reflected to only a very marginal extent in the index of consumer prices, which remained virtually unchanged, Japanese enterprises having taken advantage of the recovery to improve their gross operating surplus, which had been seriously eroded during the 1998 recession.

In the euro area, import prices declined somewhat in 1999, but the fall was far less significant than that of a year earlier, mainly because of the movement of exchange rates. Compensation per employee, which had risen by just 0.9 p.c. in 1998, increased a little faster in 1999, by 1.9 p.c. Furthermore, labour productivity, which had increased by a further 1.3 p.c. in 1998, rose by only 0.5 p.c. in 1999. This dip is partly attributable to economic growth, which was slower on average in 1999, but it also reflects structural changes in the European economies causing growth to become more labour-intensive. Unit labour costs, which had fallen slightly in 1998, therefore increased by 1.4 p.c. in 1999. The marked fall in production costs in 1998 was only gradually reflected in the prices of consumer goods in general, and helped to stabilise the rise in those prices in 1999. Overall, the harmonised index of consumer prices for the euro area rose by 1.1 p.c., as it had done in 1998.

1.5 BALANCE OF CURRENT TRANSACTIONS, EXCHANGE RATES AND INTERNATIONAL RELATIONS

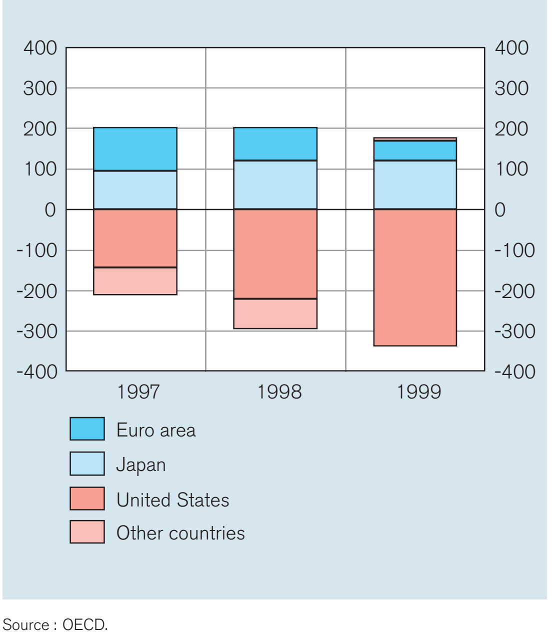
Balance of current transactions

The relative sluggishness of world trade in 1998 persisted during the year under review : in the past two years, the volume of transactions in goods in fact increased by just 5.1 p.c. and 4.9 p.c. respectively, against an average of 6.2 p.c. during the 1990s. The recovery of trade in the emerging countries of Asia and in Japan was counterbalanced by the slower average expansion of trade in the euro area, and by its stagnation in the Latin American countries and its contraction in central and eastern Europe.

The current account imbalances appear to have generally worsened in recent years. In 1999, the current account deficit of the United States continued to expand significantly, rising from 221 billion dollars in 1998 to 338 billion, or from 2.5 to 3.7 p.c. of GDP. It thus beat the previous record dating from 1987 when it stood at 3.4 p.c. of GDP. It represents about one quarter of the average imports and exports of goods and services of the United States. Japan's current surplus remained more or less unchanged in terms of absolute value, standing at 120 billion dollars, but as a percentage of GDP it fell from 3.2 to 2.7 p.c. The

CHART 8 — CURRENT ACCOUNTS OF THE MAIN REGIONS OF THE WORLD

(Balances, in billions of US dollars) [1]



Source : OECD.

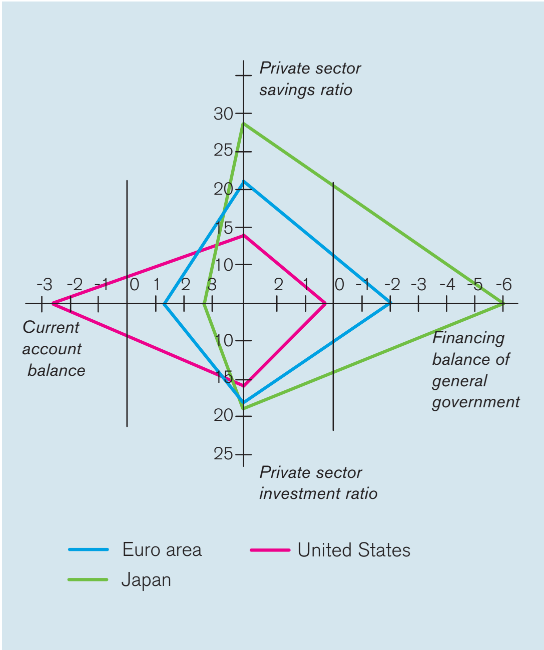
[1] Owing to errors and omissions, the balances do not add up to zero.

euro area's surplus dropped from 83 billion dollars in 1998 to 49 billion in 1999, down from 1.3 to 0.8 p.c. of GDP. On the other hand, the current account deficit of the other countries was converted into a small surplus. Thus, the external deficits of the Latin American countries and those of central and eastern Europe (OECD members and non-members) contracted. However, the improvement in the external account for this group of countries was partly offset by the decline in the current account surplus of China and the emerging countries of Asia, including South Korea. If the oil-exporting developing countries in the various regions are considered separately, it furthermore becomes apparent that the current account external deficit of this group of countries declined markedly. Finally, the problem of the unreliability of world data on the current account balance of payments became still worse in the year under review. While the balances of the various countries should cancel one another out overall, the world statistics reveal an overall deficit for all the economies, which increased in 1999; no satisfactory explanation is available for this.

Up to the beginning of the 1990s, the persistent and growing external deficit of the United States, reflecting the net overall financing requirement of the US domestic sectors, was accompanied by a large public deficit, but in recent years it has been caused by the steadily growing net financing requirement of the private sector. In this sector, investment is at about the same level as in the euro area and Japan, but the savings ratio is particularly low in relative terms. Conversely, households and enterprises combined have a large financing capacity in the euro area, and more so in Japan, where their savings represent a particularly large proportion of GDP. This surplus amply offsets the public deficit, though in the past few years the trend and level of that deficit have become far less favourable in Japan than in the euro area. In these two regions there is therefore a corresponding current account surplus, though Japan's is still much larger than that of the euro area.

CHART 9 — KEY MACROECONOMIC AGGREGATES IN THE MAIN ECONOMIES IN 1998

(Percentages of GDP)



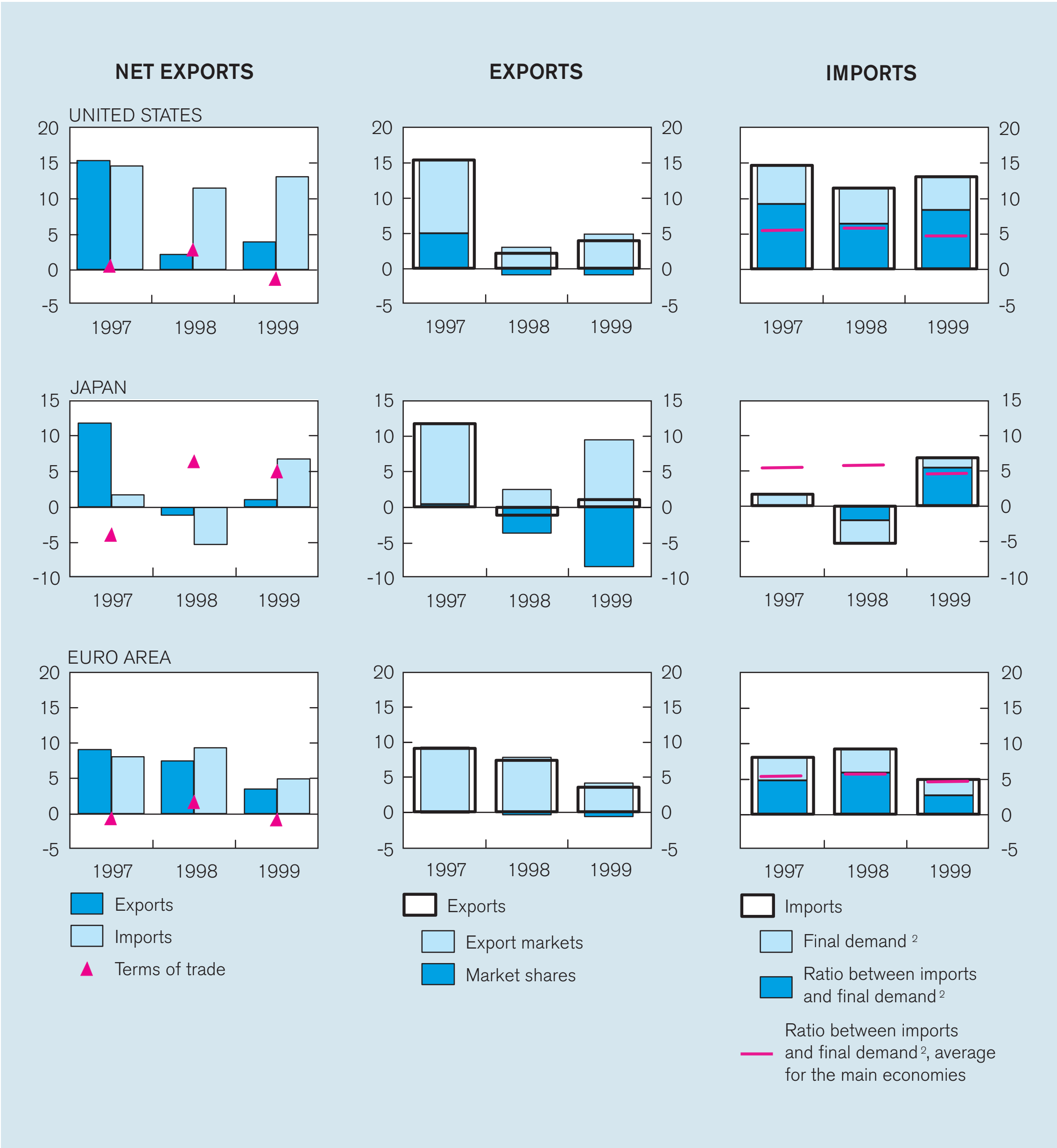
Sources : EC, OECD.

The increase in the United States' current account deficit in 1999 is due mainly to transactions in goods. In volume terms, exports of goods continued to expand at a modest rate on account of the relatively subdued growth of the export markets and a small loss of market shares. Imports remained as buoyant as ever, owing to the persistent expansion of final demand and a further rise in its import content. This relatively large increase in the share of imports in final demand, which has coincided with a loss of export market shares, may indicate that the United States is suffering a decline in its competitiveness. On the other hand, the terms of trade deteriorated during the past year, whereas they had improved in 1998.

Like transactions in goods, factor incomes have produced a growing deficit, which amounted to some 0.2 p.c. of GDP in 1999. This trend is

CHART 10 — TRANSACTIONS IN GOODS AND TERMS OF TRADE OF THE MAIN ECONOMIES

(Percentage changes at constant prices compared to the previous year) [1]



Source : OECD.
[1] For the terms of trade : percentage changes compared to the previous year.
[2] Total of domestic demand and exports of goods and services.

connected with the sharp decline in the net external position of the United States. While that country still enjoyed a surplus of over 2 p.c. of GDP in the mid-1980s, it went into deficit in 1989 and the position deteriorated rapidly in the years thereafter, reaching about 18 p.c. of GDP in 1998. However, net factor incomes remained in surplus until 1997, since the implicit return on the external assets of the United States was higher than the average cost of the country's liabilities. The balance was then reversed by the combined effects of the continuing deterioration in the net external position and the shrinking differential between the return on assets and that on liabilities.

In Japan, the rise in the overall deficit on service transactions and transfers offset a slight strengthening of the balance of transactions in goods. However, this improvement was due solely to the improvement in the terms of trade, while the recovery in the volume of imports, which outpaced the rise in exports, had a negative impact. The competitiveness of Japanese products was in fact adversely affected by the appreciation of the yen, both on domestic markets and abroad. The share of imports in final demand in Japan increased faster than the average for the main economies, and that country suffered a considerable loss of export market shares.

The decline in the current account surplus in the euro area was due to a smaller surplus on the balance of trade, caused mainly by the decline in the rate of coverage of imports by exports in volume terms, and to a lesser extent by a deterioration in the terms of trade. The growth of exports slackened significantly, mainly owing to the substantial slowing of market growth. At the beginning of 1999, exports were in fact still depressed by the widening of the international financial crisis which erupted following the turmoil in the Asian countries in 1997. During the year under review, however, they recovered thanks to the revival in world economic activity. Overall, the decline in the cover ratio remained small, since imports also grew less strongly than in the previous year. Both the rise in final demand and the increase in its import content were in fact smaller in 1999.

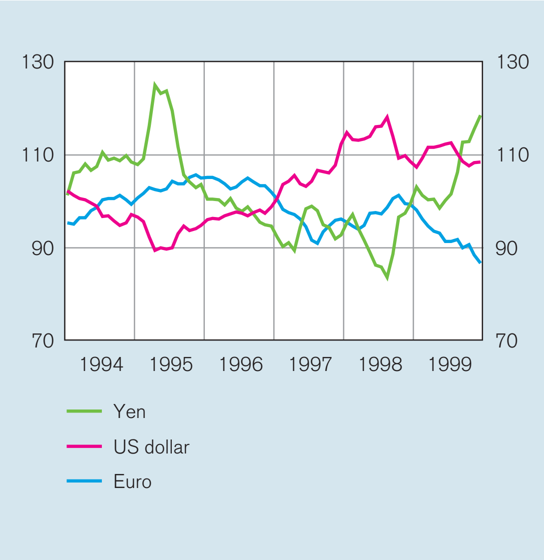
Exchange rates

From the end of 1998 to the end of 1999, the bilateral exchange rates for the dollar and the yen in relation to the euro appreciated strongly, by just over 16 and 29 p.c. However, for an analysis of the trend of the current transactions of the main economies with the rest of the world, the weighted average exchange rate provides more relevant information on the conditions under which trade has taken place, particularly if a comparison is made of its average movement from one year to the next.

The persistence of a particularly buoyant economic situation in the United States bolstered the weighted average exchange rate for the dollar in the first half of 1999, after the substantial correction which occurred during the last few months of 1998. However, owing to changes in relative growth prospects compared to Japan and the euro area and the expectation of a growing external account deficit, the dollar subsequently fell sharply until October. The persistent strength of the US economy nevertheless continued to confound the forecasters, so that this trend of the dollar was again reversed at the end of the period. Overall, the effective exchange rate for the dollar was some 3 p.c. lower in the year under review than the average rate observed in 1998.

CHART 11 — WEIGHTED AVERAGE EXCHANGE RATE

(Indices 1993 = 100, monthly averages)



Source : BIS.

In contrast, the yen weakened at first before appreciating sharply in the second half of the year under review. This strong recovery took place in the context of a turn-round of growth forecasts and a more positive climate on the Japanese financial markets. Thus, the weighted average exchange rate for the yen rose by an annual average of 15 p.c.

The differences in economic growth and short-term interest rates between the United States and the euro area were the main factors behind the marked depreciation in the weighted average rate for the euro in the first half-year. However, the increasingly convergent signs of accelerating growth in the euro area and the financial markets' expectation that short-term rates would rise at the beginning of November slowed down the depreciation of the euro for the greater part of the second half-year. But subsequently, the relative strength of the American economy seems again to have become the dominant factor. Overall, the weighted average exchange rate for the euro depreciated by 5.5 p.c. in 1999 compared to 1998.

International relations

During the year under review, the IMF paid special attention to strengthening the international monetary and financial system. For this purpose, it encouraged its members to improve the quality and transparency of the information supplied, notably by including statistics on external reserves in the Special Data Dissemination Standard. The IMF also launched a pilot project on the disclosure of the reports which it compiles on the supervision of the economic policy of its member countries under Article IV of its Articles of Agreement. Several member countries including Belgium supported this project and are taking part in it.

To improve the stability of the international financial system, the IMF collaborated with other international institutions on the development, circulation and implementation of international standard rules aimed at improving the working of economic policy. Rules on the transparency of monetary and fiscal policy were thus developed. The IMF attached special importance to the soundness and stability of the national financial sectors.

During the year under review, the IMF also examined the role of the private sector in the prevention of financial crises. In this connection, the emphasis was on greater market discipline and more effective assessment of the risks by the private sector. The IMF also tried to involve this sector in crisis management, e.g. by devising schemes for coordinated debt rescheduling mechanisms.

To prevent financial crises more effectively, the IMF Executive Board decided in April 1999 to introduce a contingent credit line. This was in addition to the supplementary reserve facility created in December 1997 for countries already in crisis. It is intended for IMF member countries which pursue a sound economic policy and are not yet in a financial crisis when the funds are committed but which might experience balance of payments difficulties, by contagion, as a result of circumstances beyond their control, especially unfavourable developments on the international capital markets resulting from events in other countries.

In September 1999 the IMF Board of Governors adopted a resolution whereby the Interim Committee would be converted into an International Monetary and Financial Committee and its operating procedures would be adapted.

In the IMF, programmes for the poorest developing countries, social policy and, in particular, poverty reduction, have gained in importance. The Enhanced Structural Adjustment Facility was converted into a Poverty Reduction and Growth Facility. In addition, as part of the debt reduction initiative for highly indebted poor countries, agreement was reached at the annual meetings between the IMF and the World Bank in September 1999 on relaxation of the conditions for access and more rapid and extensive reduction of the foreign debts of these countries.

Moreover, the advent of EMU changed the relations between the IMF and the euro area countries. Technical adjustments were made to the method of calculating the SDR at the beginning of the year under review, the euro being substituted for the German mark and the French franc in the basket of currencies used for these calculations. Furthermore, the ECB was given the status of observer on the IMF Executive Board. Finally, the supervision at national level exercised pursuant to Article IV of the IMF Articles of Agreement was supplemented by broader supervision over the euro area as a whole.

Less use was made of the IMF's financial support in 1999, after two years when it was much in demand as a result of the financial crisis in a number of emerging countries. Gross drawings on the Fund's resources totalled SDR 10 billion in the year under review, against 16.1 and 20.6 billion in 1997 and 1998 respectively. The outstanding amount of credit, including drawings on loans under the poverty reduction and growth facility, also declined, falling from the record level of SDR 66.8 billion at 31 December 1998 to SDR 57.6 billion at the end of last year.

The IMF replenished its resources via the general 45 p.c. increase in quotas which came into force in 1999. This increase had been decided on in 1997 to enable the IMF to perform its role in the achievement of balanced growth and internal and external stability in its member countries. The increase in Belgium's quota from SDR 3,102.3 million to SDR 4,605.2 million took effect in May. In addition, the procedure for approving the fourth amendment to the Articles of Agreement, intended to facilitate a special one-time allocation of SDRs, continued to make progress. In Belgium, this fourth amendment was ratified by a law dated 26 April 1999, but it will not take effect until it has been approved by member countries representing at least 85 p.c. of the voting rights.

In Europe, further progress was achieved in political and economic integration. Leaving aside the efforts to improve the coordination of EU economic policies, and in particular the introduction of a macroeconomic dialogue mentioned elsewhere, it was in the fields of EU enlargement and cooperation between the central banks that the most significant advances were made.

At the Helsinki summit in December 1999, the European Council gave a new impetus to the preparations for enlarging the EU. In particular, it reaffirmed the principle of a single set of arrangements for the process of accession to the EU, for which there are now thirteen candidate countries : the six countries with which negotiations had already begun (Cyprus, Estonia, Hungary, Poland, the Czech Republic and Slovenia), the six with which negotiations are to start during 2000 (Bulgaria, Latvia, Lithuania, Malta, Romania and Slovakia), and Turkey, which is now recognised as a candidate country, aiming to join the Union on the basis of criteria identical with those applicable to the others.

The Council also gave a firm political undertaking that it would do everything possible to complete the work on the Intergovernmental Conference on Institutional Reform by December 2000, so that the EU would be able to welcome new Member States from the end of 2002.

During November, a high-level seminar on enlargement was held in Helsinki, on the initiative of the Eurosystem, which comprises the ECB and the eleven national central banks of the euro area countries, with the central banks of the twelve countries concerned in the accession negotiations. The purpose of this meeting was to identify the main questions for which these institutions are responsible and develop cooperation between the Eurosystem and the central banks of the candidate countries. That co-operation will be extended in the various fields which are of interest to the monetary authorities, particularly the statutes of the central banks, statistics, payments systems and financial legislation.

On 26 September 1999 fifteen European central banks, including the National Bank of Belgium, announced that they would not enter the gold market as sellers for the next five years, with the exception of already decided transactions. The total volume of the latter will not exceed 2,000 tons during that period, and annual sales will not exceed approximately 400 tons. Over the next five years, the signatories to the agreement will not expand their gold leasing and their use of gold futures and options.

1.6 ECONOMIC POLICY

General direction of macroeconomic policies

The divergences in the focus of macroeconomic policies pursued in the main economies largely reflect cyclical differences. In some cases they also address other concerns, such as the need for structural reforms and, in the case of the EU countries, the adjustment of economic policies and structures to cope with the challenges and constraints presented by accession to or participation in a common currency area.

Largely because it is further ahead in the cycle, the United-States has, generally, the most restrictive stance on economic policy of the world's three leading economies. This is evidenced by a short-term interest rate differential in relation to the other currencies which was positive for the fourth consecutive year, the greater improvement in the public finances achieved since the last cyclical trough and the generation of budget surpluses in a context of durable and sustained economic growth. American fiscal policy has also produced an appropriate but still insufficient response to the very low level of private savings.

At the other extreme, Japan – which is emerging from recession – has the most expansionary monetary and fiscal policies of all the OECD countries. The Japanese central bank is pursuing a policy of zero interest rates and the structural primary balance of general government shows a large deficit. Overall, the macroeconomic policy of the Japanese authorities aims to support the considerable efforts to reform the financial institutions and economic regulation in general, without which the restoration of sustained growth would be compromised.

Taken as a whole, the euro area falls between these two extremes as regards the phase of the cycle and the general direction of macroeconomic policies. In this area, the levels of both the net financing requirement of general government and the gross public debt, as well as of short-term interest rates, are in an intermediate position between those of Japan and the United States. The budget balance nevertheless continued its structural decline last year in conformity with the medium-term strategy of the Stability and Growth Pact, which aims in particular to create the optimum conditions for price stability.

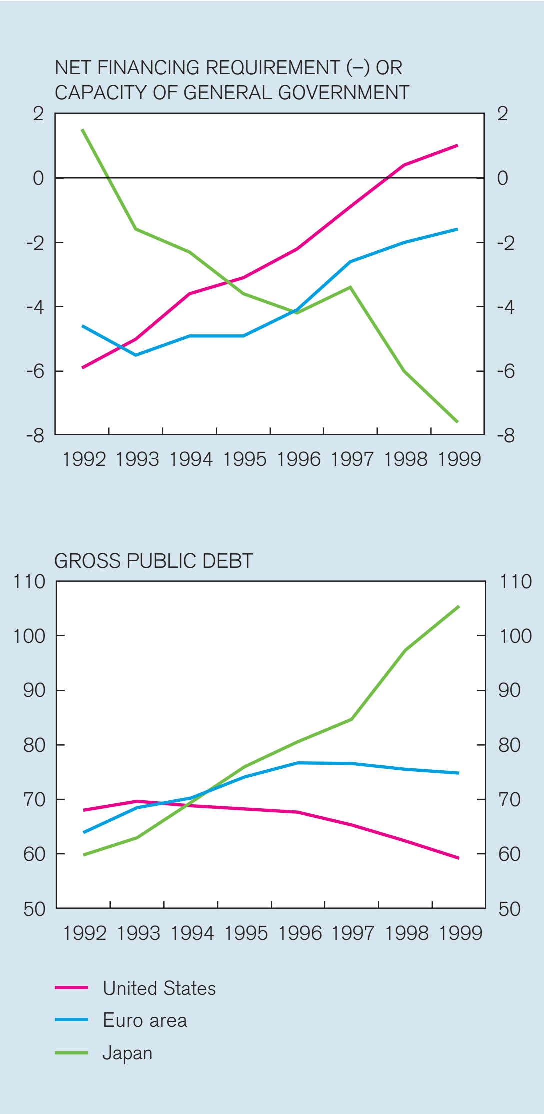
However, the effects of membership of a single currency area are not confined to monetary and fiscal policy. In general, they mean that countries in the euro area have to make a special effort to conform to the more global strategies implemented for some years by the EU as a whole in order to adapt the labour market and improve the operation of the markets in goods and services without prejudice to the continuing harmonisation of legislation for the purpose of widening the scope of the single market. Fiscal policy has also been used as an additional instrument in this connection, notably via reductions in fiscal or in para-fiscal levies on earned incomes in a number of countries.

Fiscal policy

In the United States, the budget surplus increased from 0.4 p.c. of GDP in 1998 to 1 p.c. in 1999. It was accompanied by a further contraction – the sixth in a row – in the public debt ratio, which fell from 62.4 p.c. of GDP in 1998 to 59.3 p.c. in 1999.

CHART 12 – NET FINANCING REQUIREMENT (–) OR CAPACITY OF GENERAL AND GROSS PUBLIC DEBT OF THE MAIN ECONOMIES

(Percentages of GDP)



Source : OECD.

These results were achieved mainly thanks to the energetic fiscal consolidation programme implemented since the beginning of the decade : in 1992, the transactions of general government produced a record deficit of 5.9 p.c. of GDP. Since that peak the net balance has improved by a total of 6.9 percentage points of GDP, of which 4.8 points can be attributed to a reduction in expenditure and 2.1 points to an increase in revenue. The recovery which this produced was due primarily to discretionary measures : according to the OECD their contribution totalled around 70 p.c.

The restrictive line imposed on US fiscal policy has three aims : to overcome the shortage of national savings and eliminate the current deficit, to promote the stability of the macroeconomic environment and therefore to facilitate the conduct of monetary policy, and to anticipate the financial consequences of the ageing of the population.

In Japan, the policy stance on the public finances remains expansionary, as it was last year. It is based on the implementation of a “fifteen-month” budget which offered incentives designed to provide permanent support for the economy throughout the period from January 1999 to March 2000. In November of the year under review, the government also presented a major new recovery programme, partly to be paid for by the 2000 budget.

Since 1992, many fiscal stimulation programmes have already been launched in Japan. They have curbed the decline in economic activity in that country, and have doubtless helped finally to put it back on the road to growth. But they have also caused a serious worsening of the situation in the public finances. The net financing requirement, which was already up to 6 p.c. of GDP in 1998, deteriorated further to reach 7.6 p.c. during the year under review. This movement was accompanied by an increase in the gross public debt from 97.3 to 105.4 p.c. of GDP. The net debt, which increased during this period from

29.8 to 37.2 p.c. of GDP, remained relatively small, but the method of calculating it, based on the book value of the financial assets of general government, could lead to substantial underestimation of the actual debt position. In fact, part of the consolidated assets consists of rather illiquid claims of mediocre quality on public financial institutions. Owing to the crisis which Japan has experienced, the percentage of bad debts in the portfolio of some of those institutions has greatly increased and has reached a high level.

Japan's gross public debt ratio, which was still below that of the United States and the euro area in 1993, far outstripped that of these two major economies in the space of a few years, to reach one of the highest levels in the OECD. The gross public debt would furthermore increase by around two thirds of GDP if the potential commitments relating to the debt guarantee of various public institutions were included, and by a higher amount still if account were taken of certain potential liabilities, such as credit guarantees.

In the euro area, fiscal policy was again tightened on account of the commitments under the Stability and Growth Pact adopted at the Amsterdam Council in June 1997, which clarifies the procedures laid down by the Treaty of Maastricht in respect of excessive public deficits and supervision of fiscal policy. This pact provides that, in normal circumstances, the budget deficits of EU Member States must not exceed 3 p.c. of GDP, and defines as the medium-term objective a budget position which is more or less in balance or in surplus. To attain this objective by 2001-2002, the governments of the countries of the euro area presented multiannual programmes, called stability programmes, at the end of 1998 and the beginning of 1999.

Comparison between the budget balances achieved and those announced as objectives in the stability programmes provides a measure of the progress or delay in the implementation of the national programmes, though it is complicated by the change in the national accounts system introduced in the interim, the impact of which cannot be assessed at this stage. With this proviso, such an exercise shows that, in the past year, the great majority of countries achieved a net financing requirement of less than the target set in their programme. For the euro area as a whole, the deficit was reduced to 2 p.c. of GDP in 1998 and 1.6 p.c. in 1999, while the stability programmes aimed to bring it down, overall, to 2.3 p.c. and 1.8 p.c. The greater progress achieved in the year under review was therefore attributable primarily to the fact that the starting point in 1998 was lower than expected.

Unlike in the two preceding years, the reduction in the public deficit in 1999 was based almost exclusively on a decline in the burden of interest charges in GDP. However, it was sufficient to give rise to a further decline in the level of gross public debt, from 75.6 p.c. to 74.8 p.c. The level of debt in the euro area thus declined for the third consecutive year since the 1996 peak of 76.9 p.c.

Monetary policy

In the United States, where monetary conditions were eased from September to November 1998, mainly because of the impact which the weak international environment was having on the domestic economy, the Federal Reserve returned to a more restrictive policy stance during the year under review.

In the first half of 1999, domestic demand was more buoyant than expected, and the labour market situation became tight, while the international economy strengthened. These developments fuelled expectations of price rises, reflected in higher long-term interest rates. They prompted the Federal Reserve to raise the federal fund rate in June, and then in August and November, increasing it in three stages from 4.75 to 5.5 p.c. The rate on three-month euro deposits in dollars, which remained below 5 p.c.

from January to May, then increased to average 6 p.c. during the final quarter.

The rise in long-term interest rates in Japan, which had taken place since November of the previous year, plus various other factors such as the strength of the yen, the lack of confidence among households and enterprises and the downward pressure on prices, led the monetary authorities to decide on a further relaxation of their policy in February 1999. The Bank of Japan boosted liquidity, and its main key rate, the uncollateralised overnight call rate, was reduced to the lowest possible level : from a quarter of one per cent in January, it dropped to practically zero in April and has remained unchanged ever since.

That decision, the effects of which supplemented those of other general government measures such as raising the ceiling on the credit guarantee system for small and medium-sized enterprises and the recapitalisation of the banking sector, helped to halt the rise in long-term rates, to eliminate the premium on Japanese bank lending rates and to push up share prices.

Short-term market rates edged downwards : thus, the rate on three-month euro deposits denominated in yen dropped from an average of just over 0.3 p.c. in 1998 to just under 0.1 p.c. in 1999.

As explained in more detail in the chapter on monetary policy in the euro area, the ECB Governing Council twice adjusted the Eurosystem's main refinancing rate. In April it reduced it from 3 p.c. to 2.5 p.c. and in November it restored it to its original level.

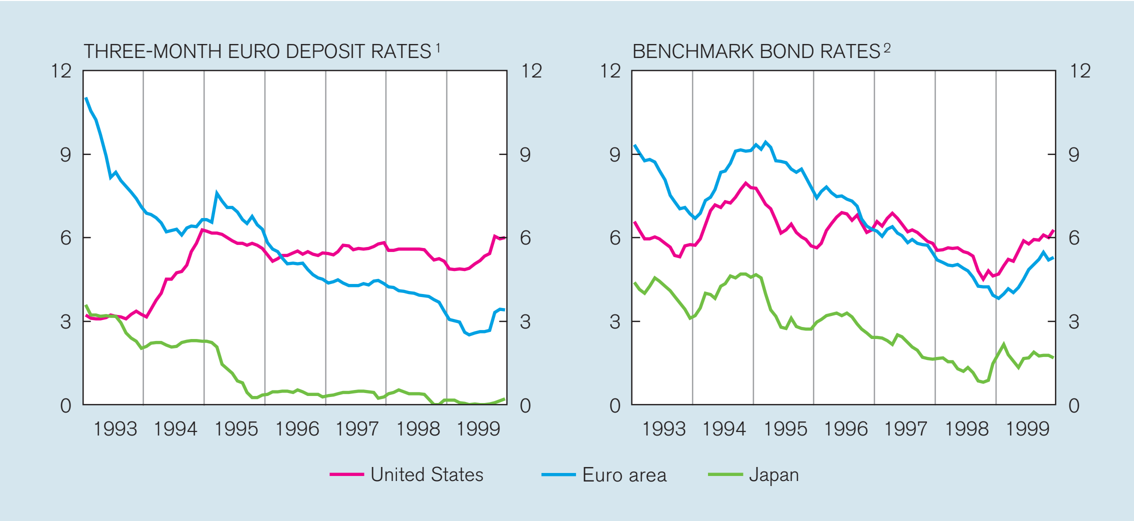
On the money market, the rate on three-month deposits denominated in euros first declined from 3.1 p.c. in January 1999 to 2.5 p.c. in May, before moving back up to reach 3.4 p.c. in December.

Long-term interest rates

The downward trend of long-term interest rates observed since 1995 was interrupted in each of the three main economies, at intervals of just a few months, between November 1998 and February 1999. This rate rise was accompanied

CHART 13 — SHORT-TERM AND LONG-TERM INTEREST RATES IN THE MAIN ECONOMIES

(Monthly averages)



Sources : ECB, BIS, NBB.

[1] For the euro area : up to 1998, weighted average of interest rates offered on the interbank market in national currencies.

[2] For the euro area : weighted average of the rates on the benchmark government bonds of the member countries.

in some cases by a later and smaller rise in short-term interest rates and in other cases by a relative stability in these rates, so that the yield curve rose more steeply in all these economies.

However, there was no evidence that these various movements had a common cause.

The recovery in long-term rates in the United States which began in November 1998 was due to several factors. For one thing, the “flight to quality” observed at the time of the international economic and financial crisis in the autumn of 1998, which was reflected in a particular enthusiasm for investing in US bonds, had come to an end. Furthermore, the improvement in the economic outlook and hence the expectation of upward pressures on prices also contributed to this recovery. Long-term dollar interest rates rose sharply up to the end of the first half-year, and then more moderately, to reach 6.3 p.c. in December.

In Japan, heightened awareness of the seriousness of the outlook for the public finances exerted upward pressure on benchmark government bond rates from November 1998 onwards. This rise continued after the announcement of plans for a substantial reduction in the financing of the public debt by financial institutions dependent on general government. As the central bank had further eased monetary policy, this movement stopped in March. Since then the long-term benchmark interest rate in yen has hovered between 1.5 and 2 p.c.

In the euro area, long-term rates dropped to their lowest level, namely 3.8 p.c., in January 1999, before increasing in the first half-year, doubtless in the wake of the US rates. Their rise then accelerated slightly in the second half-year, in response to more and more signs that growth was picking up in this area. In all, rates rose by 1.5 percentage points compared to the low point in January.

2. THE SINGLE CURRENCY AND MONETARY POLICY

2.1 LAUNCH OF THE EURO

Since 1 January 1999 the euro has been the currency of the eleven countries taking part in European monetary union. Responsibility for the single monetary policy now rests with the Eurosystem, comprising the ECB and the eleven central banks of the countries in the euro area. This system is also responsible for carrying out foreign exchange transactions, managing the Member States' official reserves and promoting the smooth operation of the payment systems.

The national monetary units will continue to exist until 2002 as non-decimal expressions of the euro. On 1 January 2002, euro notes and coins will be placed in circulation. In November 1999 the Council of European Ministers for Economic Affairs and Finance defined the broad outlines of this operation, notably a small-scale advance distribution of the new notes and coins and a maximum period of two months in which the old and new currencies would circulate side by side, on the understanding that exchange will still be possible after the end of February 2002.

Meanwhile, using the euro is neither compulsory nor prohibited for non-financial enterprises and individuals. On the other hand, it has become the only currency used on the money and foreign exchange markets since 1 January 1999, at least for transactions of some size.

The introduction of the euro is an obvious factor in the integration of the financial markets of the euro area. This development is most apparent on the money market : the market in interbank deposits is fully integrated. The Eurosystem has played an important role in this respect. The single monetary policy guarantees common refinancing terms for the credit institutions of all euro area countries. Moreover, the TARGET payment system is helping to align short-term interest rates, since it makes it easy for financial institutions to engage in cross-border arbitrage. A tendency towards greater integration is also observable on other financial markets, especially the bond market, where portfolios which used to contain predominantly national securities are rapidly being diversified. The European financial markets are consequently becoming more liquid. This development is encouraging international use of the euro, as is apparently confirmed by data on bond issues on the international financial markets. Thus, in the first nine months of 1999, net issues of euro-denominated bonds represented 44 p.c. of total international bond issues, against 47 p.c. for the US dollar, while the share represented by the old national currencies of the euro area taken together had fluctuated between 20 and 30 p.c. in the preceding years. If only net issues of bonds denominated in a currency other than that of the issuer are considered, the euro's share exceeded that of the dollar.

2.2 STRATEGIC ASPECTS OF THE EUROSYSTEM'S MONETARY POLICY

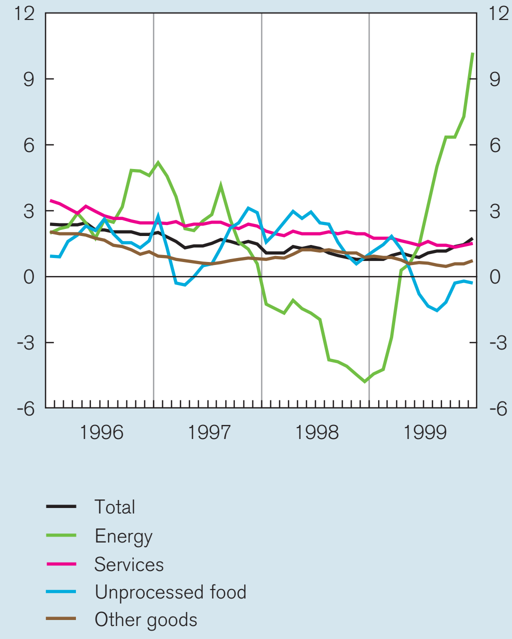
The main objective of the Eurosystem's monetary policy, specified in the Treaty of Maastricht, is price stability. The Eurosystem can exert only an indirect influence over the general price level via its hold over very-short-term interest rates. As a guide, and to enable the public to judge its policy, the Governing Council of the ECB has quantified the main objective and defined the two "pillars" of the strategy to be followed to attain the objective : an essential role for money, emphasised by the announcement of a reference value for the growth in the broad monetary aggregate M3, and broadly based assessment on a wide range of indicators of the outlook for the movement of prices and the dangers for price stability throughout the euro area. This was the strategy applied when monetary policy decisions were taken in 1999, namely a cut in interest rates in April and an increase in November.

After placing the 1999 monetary policy decisions in their strategic context, this section will conclude with a description of the developments in long-term interest rates and exchange rates, which are among the indicators considered in the second "pillar" of the strategy but also play a key role in the process of transmitting monetary policy stimuli, though they still depend on many other factors.

In general, the monetary conditions prevailing in 1999 augur well for the maintenance of price stability, while at the same time favouring the expansion of economic activity in the euro area.

CHART 14 – HARMONISED INDEX OF CONSUMER PRICES IN THE EURO AREA

(Percentage changes compared to the corresponding month of the previous year)



Source : EC.

The final aim of monetary policy

In October 1998 the Governing Council of the ECB defined price stability as a rise in the harmonised index of consumer prices (HICP) of less than 2 p.c. per annum throughout the euro area. Price stability must be maintained in the medium term.

A small rise in the consumer price index is seen as a sign of generally stable prices, since the index has an inherent "measurement bias", caused mainly by changes in spending habits and improvements in the quality of goods and services. It also encourages changes in relative prices if there are nominal downward rigidities and reduces the risk of a deflationary spiral while avoiding the distortions which true inflation would generate.

In 1999 the rise in the HICP in the euro area remained below 2 p.c., as it had done in the two preceding years. Since it generally takes quite a while before monetary policy influences prices, the credit for this state of affairs should be accorded not only to the Eurosystem but primarily to the policies pursued earlier by the national central banks, which bequeathed to the new institution a situation conducive to stability.

Measured by the annual rise in the HICP, inflation was at its lowest, at 0.8 p.c., from November 1998 to February 1999. It then climbed back to reach 1.7 p.c. in December 1999. This acceleration was due to the sudden increase in the energy prices. The prices of unprocessed food products, another volatile component of index, declined from June onwards owing to favourable supply conditions. The rise in the prices of other goods and services continued to slow down until September, mainly because of keener competition in certain sectors such as telecommunications and the delayed effects of the previous year's fall in oil prices, but also thanks to the credibility of monetary policy.

The Eurosystem obviously cannot be held responsible for external shocks such as the rise in oil prices. However, the Governing Council of the ECB must take them into account in formulating monetary policy if they present a threat to the future stability of prices : this analysis is part of the second "pillar" of the monetary policy strategy.

In the euro area, inflation rates showed a remarkably convergent downward trend until 1997. Since then there has been a slight widening of the differences between countries : in the Netherlands, Spain, Portugal and Ireland, the inflation rate was 2 p.c. or higher during 1999, while it did not exceed 1 p.c. in Austria, Germany, France and Luxembourg.

The inflation differentials observed are still modest and similar in magnitude to those found, for example, between major cities in the United States. Apart from technical factors such as differences in the weighting of the components of the index, they appear to be due mainly to two economic causes. First, the convergence of price levels implies that, during a period of transition, countries where prices are relatively low face greater inflation than those where prices are high. This convergence may result from the increased integration of markets, where prices are becoming more transparent, and from the alignment of productivity levels in sectors exposed to international competition, leading to an increase in the purchasing power of employees and in prices in the sheltered sector in countries where the "catching up" takes place. The steeper rise in prices in Spain, Portugal and Ireland could be partly due to this process. Second, differences in the cyclical situation may cause inflation differentials. Thus, stronger growth is associated with higher inflation in Ireland and the Netherlands. Specific factors may also play a role. For instance, the steeper rise in prices in

TABLE 8 — HARMONISED INDEX OF CONSUMER PRICES IN THE COUNTRIES OF THE EURO AREA

(Percentage change)

	1996	1997	1998	1999
Austria	1.8	1.2	0.8	0.5
Germany	1.2	1.5	0.6	0.6
France	2.1	1.3	0.7	0.6
Luxembourg	1.2	1.4	1.0	1.0
Belgium	1.8	1.5	0.9	1.1
Finland	1.1	1.2	1.4	1.3
Italy	4.0	1.9	2.0	1.7
Netherlands	1.4	1.9	1.8	2.0
Spain	3.6	1.9	1.8	2.2
Portugal	2.9	1.9	2.2	2.2
Ireland	2.2	1.2	2.1	2.5
Euro area	2.2	1.6	1.1	1.1
Maximum deviation	2.9	0.7	1.6	1.9
Weighted standard deviation	1.1	0.2	0.6	0.6

Source : EC.

the Netherlands is also due to increases in regulated prices and renewed pay rises after a long period of moderation.

The single monetary policy must be centred on the objective of price stability throughout the euro area. Large and persistent inflation differentials not justified by market integration and the alignment of the economies should therefore prompt correction via other economic policies.

The first pillar of the strategy

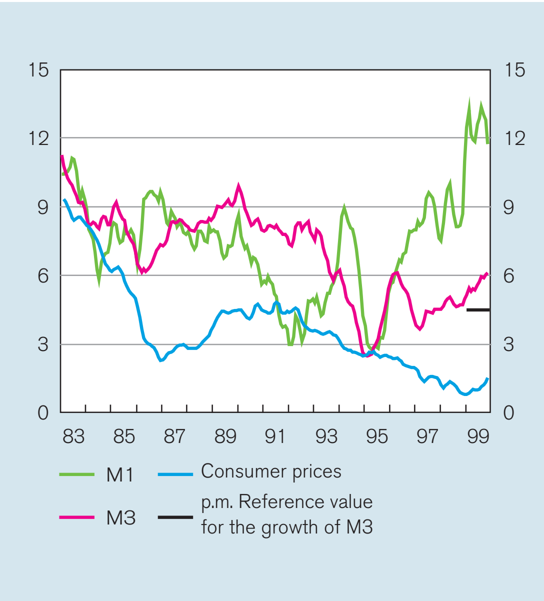
The Eurosystem assigns an essential role to money, and monetary analysis is the first pillar of its monetary policy strategy. This pillar represents continuity in relation to the practice of the German central bank and highlights the Eurosystem's responsibility with regard to inflationary pressure of monetary origin. Furthermore, the development of the money supply is a valuable source of information, since medium-term price movements are ultimately a monetary phenomenon. Thus, historical analysis reveals a fairly stable relationship between the money supply, M3, and prices in the euro area. Medium-term variations in the growth of M3 have preceded changes in inflation rates.

In practical terms, the prominent role assigned to money is expressed by the announcement of a reference value for the growth of the broad monetary aggregate, M3. The Governing Council of the ECB preferred a reference value to an intermediate target and announced a figure rather than a range, which would have aroused expectations of an automatic reaction if the actual growth of M3 were to move outside the boundaries of range. In fact, the link between the rate of expansion of M3 and inflation is a medium-term link rather than a short-term one; also, the change in monetary regime increases uncertainties about the quality of the statistical data and a possible change in behaviour. The Council therefore stressed that the interest rates would not be adapted "mechanically" if there were signs that the growth in the money supply was deviating from the reference value.

Each month, movements in the money supply are compared with the reference value on the basis of the three-month centred moving average of the growth rate of M3 compared to the corresponding months of the previous year. If the rise in M3 in the euro area deviates from the reference value, a detailed analysis of that deviation will try to assess whether there is any threat to price stability. Under the first pillar of the monetary policy strategy, the Governing Council of the ECB also examines the developments in the various components of M3 and in the counterparts to M3 in the consolidated

CHART 15 — MONETARY AGGREGATES [1] AND CONSUMER PRICES [2] IN THE EURO AREA

(Three-month averages of percentage changes compared to the corresponding month of the previous year)



Sources : EC, ECB.

[1] The narrow monetary aggregate, M1, comprises fiduciary money (notes and coins) plus overnight deposits; M3, the money supply in the broad sense, comprises M1 plus time deposits of up to two years, deposits redeemable at a period of notice of up to three months (e.g. savings books or deposits) and liquid negotiable instruments issued by the MFI sector, such as securities of monetary UCIs. Account is taken of the positions of the MFIs in relation to residents of the euro area as a whole. However, these data can be calculated only for the period starting in September 1997. Figures relating to earlier periods were therefore estimated on the basis of national monetary and banking statistics, which were not fully harmonised in the past. See the *Monthly Bulletin* of the ECB, February 1999, for a detailed description.

[2] HICP from 1996 onwards.

balance sheet of the monetary financial institutions – i.e. essentially the national central banks, credit institutions and monetary UCIs.

In December 1998 the Governing Council set a $4^{1}/_{2}$ p.c. reference value for the growth of M3. This value is in line with the ultimate aim of price stability, given the assumptions regarding the economy of the euro area. In fact, the trend growth rate of real GDP in the euro area is estimated at between 2 and $2^{1}/_{2}$ p.c. and the trend decline in the velocity of circulation of M3 at between $^{1}/_{2}$ and 1 p.c. As part of the annual review of the reference value, the Council decided in December 1999 to keep it at $4^{1}/_{2}$ p.c. because the components on which it is based have remained unchanged.

During the first eleven months of 1999, the three-month moving average of the growth in M3 in the euro area always exceeded the stated reference value. However, there are two distinct periods. The overstepping was less than 1 percentage point up to May 1999, then increased in the subsequent months to reach 1.6 points in November.

The historically low level of nominal and real interest rates, and hence the low opportunity cost of holding monetary assets, is possibly an important reason for a marked preference for liquidity. The steadily strengthening recovery of economic activity may also have been a contributory factor. In addition, the rise in long-term interest rates may have initially aroused expectations of an interest rate increase and hence led to a speculative demand for ready cash. Finally, special factors connected with the switch to the euro may have played a part.

The developments in M3 were greatly influenced by those in M1, and more particularly by the expansion of the overnight deposits, which represented around one third of M3 in 1999. The average annual increase in these overnight deposits amounted to 14.7 p.c. Between the end of December 1998 and the end of January 1999 this rise accelerated from 11.7 p.c. to 18.4 p.c. This quickening was probably largely due to technical factors connected with the launch of the third stage of EMU and to the high degree of uncertainty following the introduction of the euro and the international financial situation, which may have led to a preference for liquid investments. The growth remained very rapid in the subsequent months, but the influence of these specific factors gradually dwindled.

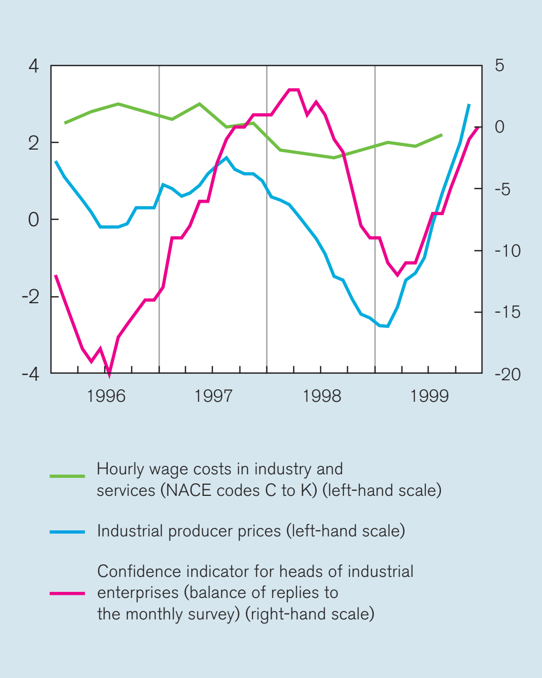
In the consolidated balance sheet of the MFIs, loans to the private sector of the euro area were the main counterpart to the strong expansion in the monetary aggregate, M3. The decline in bank lending rates stimulated the demand for credit, as did the strengthening of economic growth. The large number of mergers and acquisitions and a steep rise in the price of land and housing in some countries were other factors. In addition, some residents of the euro area took out loans to finance their foreign investments. On the supply side, the keener competition among MFIs probably also created easier credit conditions.

The second pillar of the strategy

A global appraisal of the likely trend of prices and the dangers to price stability in the euro area as a whole form the second pillar of the Eurosystem's strategy. This assessment is based on a wide range of indicators which, like the monetary aggregates, foreshadow the movement of consumer prices : indices of prices and costs, especially wage costs, exchange rates, business indicators, information on budgetary policies, etc. The Governing Council of the ECB also considers the forecasts of other institutions and financial market indicators such as long-term interest rates in order to form its opinion on the risks to price stability. As in the case of the first pillar of the strategy, no "mechanical" reaction to the movement in one indicator or another can be expected, given the uncertainty

CHART 16 — INDICATORS OF PRICES, COSTS AND ECONOMIC ACTIVITY IN THE EURO AREA

(Percentage changes compared to the corresponding period in the previous year, unless otherwise stated)



Source : EC.

surrounding the relationship between macroeconomic variables, especially in the new context of monetary union.

During the year under review, the available information has successively revealed the existence of downward and upward risks relating to price stability. At the beginning of the year, when consumer prices were rising very slowly, industrial producer prices continued to fall. In addition, despite the depreciation of the euro and a recovery in oil prices from March onwards, predictions for consumer prices were revised downwards because of flagging growth.

From the summer onwards, the risk of inflationary pressure re-emerged, notably because of the rise in import prices and strengthening growth. On the financial markets, bond yields started to rise faster than in the United States, reflecting the better growth outlook in the euro area, but also the resultant threat to price stability.

Interest rate policy

In December 1998 the Governing Council of the ECB had announced that the Eurosystem's first main refinancing operations would be carried out at a rate of 3 p.c. This level corresponded to the rate to which all the central banks in the area had jointly reduced their key rate on 3 December, with the exception of the Banca d'Italia, which had waited until 23 December to do the same. The rates on the standing marginal lending and deposit facilities were set at 4.5 and 2 p.c. respectively, except for a brief period at the beginning of stage three of EMU during which the "corridor" formed by these rates was narrower (see section 2.3).

The Eurosystem's interest rates were adjusted twice during the year under review : on 8 April and 4 November.

In April the rate on the main refinancing operations was cut by 50 basis points to 2.5 p.c. and the rates on the standing marginal lending and deposit facilities were reduced to 3.5 and 1.5 p.c. respectively. Like the December 1998 cut, the decision in April 1999 was made in response to the possibility that the weakness of activity might exert downward pressure on future consumer prices, at a time when the rise in the HICP was already well below 2 p.c. While it was true that the monetary analysis, the first pillar of the strategy, did not suggest any need to ease interest rate policy, since M3 was growing at above the reference rate. This overstepping was only small, however, and was due to the steep rise in January, which could be regarded as being temporary. Examination of a wide range of indicators which foreshadow the movement of consumer prices, the second pillar of the strategy, revealed downward risks owing to many signs of a more marked slowdown in growth than had been predicted. The Governing

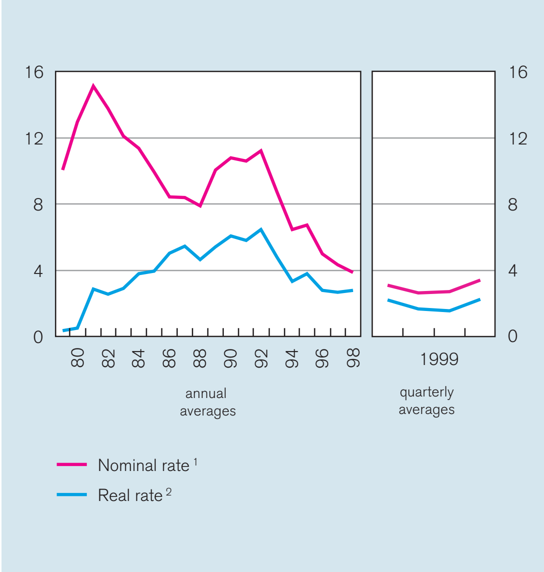
Council regarded the cut in rates as the way to maintain price stability in the medium term while helping to restore the confidence of heads of enterprises in the economic outlook.

In November the interest rate on the main refinancing operations was raised by 50 basis points to 3 p.c., the rate on the marginal lending facility was increased to 4 p.c. and that on the deposit facility to 2 p.c. Information regarding the two pillars of monetary policy pointed in the same direction, indicating a steady upward trend in the overall threats to future price stability, and the disappearance of the downward risks existing at the time of the interest rate cut in April. The steadily widening disparity between the growth of the broad money and the reference value during the preceding months showed that there was ample liquidity in the euro area, confirming the strong expansion of lending and the most liquid components of M3. Moreover, the rate of increase in the HICP was expected to quicken in the short term in the wake of the sudden surge in oil prices since the spring. Finally, the economic environment had improved markedly since the spring and the forecasts had been revised upwards. The level of interest rates applied since April was therefore no longer justified and it was necessary to prevent generous liquidity conditions from being translated into pressure on prices in the medium term.

Raising interest rates seemed the best way of avoiding doubts over monetary policy and future inflation, so as to sustain non-inflationary growth and at the same time contain the volatility of the money market at the end of the year. This was also the interpretation prevailing on the markets, where the decision was welcomed, as is evident from the ensuing temporary fall in long-term interest rates.

Despite the rise in the Eurosystem's rates and a specific risk premium on account of the transition to the year 2000 (see section 2.3), three-month interest rates remained particularly low in the euro area, whether compared with American

CHART 17 — THREE-MONTH INTEREST RATES IN THE EURO AREA



Sources : EC, ECB.

[1] Weighted average of national three-month interbank rates up to 1998; three-month interbank rate in euros (Euribor) in 1999.

[2] Nominal rate minus annual rate of change in the index of consumer prices (from 1996, HICP).

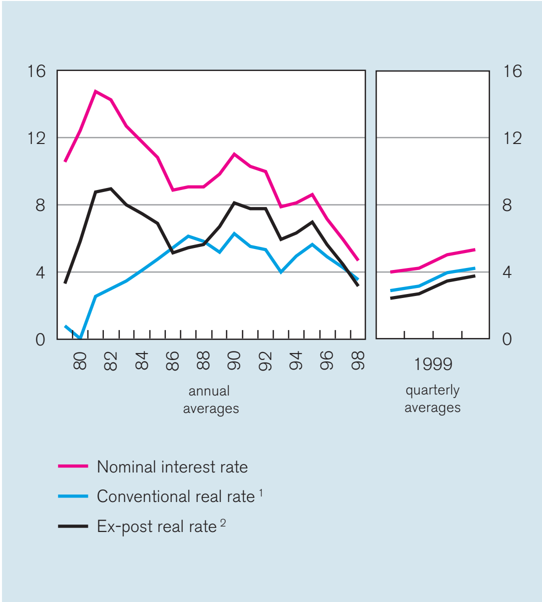
rates or with the rates prevailing in the countries of the same area over the past twenty years. From 1981 to 1995 the difference between the three-month interest rate and the rise in consumer prices was usually between 3 and 6 p.c. in the euro area, whereas in 1999 it shrank to around 2 p.c.

Long-term interest rates

Long-term interest rates are determined by the interaction of many factors, such as the predicted movement of prices and the associated uncertainty, growth expectations, budgetary policy, demographic and institutional factors which affect the propensity to save, the liquidity of the financial markets, the net external position of the economy and rates in other countries. They are influenced by monetary policy, but that effect is not clear-cut. For instance, a short-term interest rate increase may cause bond yields to rise, but it could also make them fall if it reassures financial operators about the central bank's resolute commitment to combating inflation.

In 1999, ten-year interest rates in the euro area reached a low point averaging around 3.8 p.c. in January, then recovered, rising back to 5.5 p.c. in October. The main causes of this recovery seem to have been the pull exerted by US rates, and subsequently the improvement in the prospects for economic activity in the euro area. During the first few months of the year, long-term rates in the United States rose more steeply, widening the differential to over 170 basis points. From mid-June onwards, influenced by signs of growth picking up, the rise in bond yields was more marked in the euro area. The yield curve then recovered, particularly in the medium-term segment, which is the most sensitive to the economic outlook : the differential between three-month and three-year rates widened while that between three-year and ten-year rates remained steady. In November, long-term interest rates dipped for a time following the tightening of the Eurosystem's interest rate policy. The average level of ten-year rates was 5.3 p.c. in December.

CHART 19 — LONG-TERM INTEREST RATES IN THE EURO AREA

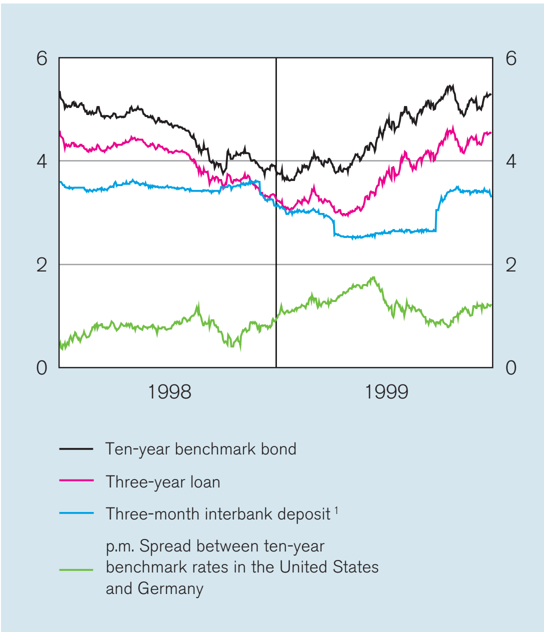


Sources : EC, ECB.

[1] Nominal rate minus the rate of change in the index of consumer prices for the current year (HICP from 1996, onwards).

[2] Nominal rate minus the average rate of change in the index of consumer prices over the next ten years (HICP from 1996 onwards). With effect from 1990, rate calculated on the assumption that inflation will remain at 1.5 p.c. after 1999.

CHART 18 — THREE-MONTH, THREE-YEAR AND TEN-YEAR INTEREST RATES IN GERMANY



Sources : EC, BIS.

[1] Interbank rate in German marks, in 1998; interbank rate in euros (Euribor) in 1999.

Despite their rise, real long-term interest rates in the euro area – hovering around 4 p.c. in the last quarter of 1999 – remained much lower than during the period from 1980 to 1996, when there were substantial risk premiums due to fears of inflation and excessive government deficits. In particular, the countries which strove hard to achieve convergence were the main ones to continue reaping its benefits.

The euro exchange rate

The euro exchange rate does not have a key role in the monetary policy of the Eurosystem. Most of the national central banks used to pursue an exchange rate policy, but the aim was to ensure a stable exchange rate vis-à-vis the reference currency, which was the German mark. The euro area as a whole is much less open than its individual component economies. In the monetary policy strategy of the Eurosystem, however, the euro exchange rate is one of the indicators taken into account in the framework of the second pillar in assessing the risks to price stability. It can influence the level of prices in the area in two ways : it affects the cost of imported goods and services expressed in euro and it has an impact on the competitiveness of resident enterprises, and hence on the demand for their products.

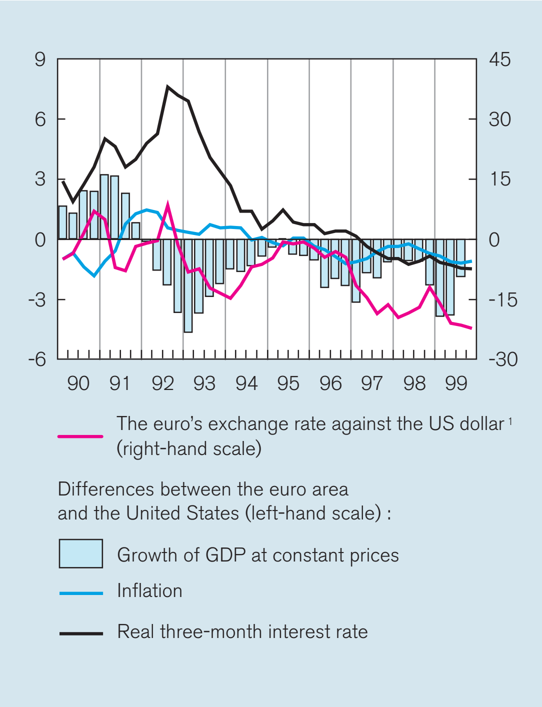
However, the movement of the euro exchange rate does not depend only on the Eurosystem's monetary policy but also on the assessment by financial operators of a set of factors both within and outside the euro area. The dominant factor in 1999 seems to have been the economic outlook.

The weighted average exchange rate for the euro depreciated by 9.9 p.c. between January and December in the year under review. This movement was due mainly to the appreciation of the US dollar and sterling, the currencies of the euro area's main trading partners, and of the yen, while the rate vis-à-vis the Swiss franc remained stable.

The exchange rate for the euro vis-à-vis the US dollar attracts particular attention in view of the importance of the United States as a trading partner and the influence which this rate has on others such as the rate of sterling. The euro depreciated against the dollar by 12.9 p.c. between January and December. Starting from a level of 1.18 dollars on 4 January, it dropped to 1.01 dollars by mid-July. It then recovered to 1.09 dollars by mid-October on account of the improved economic outlook in the euro area. Its subsequent renewed slide to 1 dollar at the beginning of December seems to have been due mainly to a revival of optimism about growth in the United States.

In recent years the dollar rate has in fact reacted primarily to differences in the economic cycle. Longer-term factors, such as the inflation differential or the respective net external positions, should on the other hand tend to encourage appreciation of the euro.

CHART 20 — THE EURO'S EXCHANGE RATE AGAINST THE US DOLLAR AND ITS MAIN DETERMINANTS



Sources : EC, BIS, ECB, NBB.

[1] Percentage differentials in relation to the 1990 average level. From 1990 to 1998, weighted average US dollar exchange rate of the eleven euro area currencies.

2.3 OPERATIONAL ASPECTS

The operational framework adopted by the Eurosystem efficiently performed the functions assigned to it in 1999 : to steer money market interest rates, limit their instability and enable the ECB to send out appropriate monetary policy signals. Credit institutions in the euro area seem to have adapted well to the new environment, and the smooth functioning of the TARGET payments system ensured homogeneous monetary conditions in the euro area.

The Eurosystem acts primarily via open market operations, i.e. transactions initiated by the ECB with credit institutions in the euro area, without discrimination. It also offers them two standing facilities which enable them to borrow or deposit overnight funds at pre-announced rates. Finally, credit institutions are required to maintain minimum reserves totalling 2 p.c. of some of their liabilities. These reserves are fully remunerated, so that they do not cause any relocation of banking activities or disintermediation.

TABLE 9 — CONSOLIDATED AND SIMPLIFIED STATEMENT OF ACCOUNT OF THE EUROSYSTEM

(Assets = +, liabilities = – ; average daily outstanding amounts in 1999 ; billions of euro)

Operations unconnected with monetary policy [1]	–83.3
Notes in circulation	–339.0
Net gold and foreign exchange assets	340.8
Deposits of public authorities	–46.2
Miscellaneous, net	–39.0
Average reserve requirement	–101.6
Total : liquidity requirement of credit institutions	–184.9
Open market operations	185.7
Main refinancing operations	134.9
Longer-term refinancing operations	46.4
Structural operations	...
Fine-tuning operations	...
Other [2]	4.4
Total : residual money market surplus	0.8
Standing facilities	0.2
Marginal lending facility	1.0
Deposit facility	–0.8
Difference between current account assets and the average reserve requirement : surplus (–) ou deficit (+)	–1.0

Source : ECB.

[1] Including debt certificates issued and securities acquired before 1 January 1999.

[2] Operations concluded before 1 January 1999 and maturing in January 1999.

The reserve requirements increase the structural deficit of the money market, i.e. the need felt by credit institutions as a whole to resort to borrowing from the Eurosystem. In 1999 they represented about 55 p.c. of that need for liquidity. It did not prove necessary to change the net position of the Eurosystem in relation to the banking sector by means of structural open market operations such as the issuing of debt certificates.

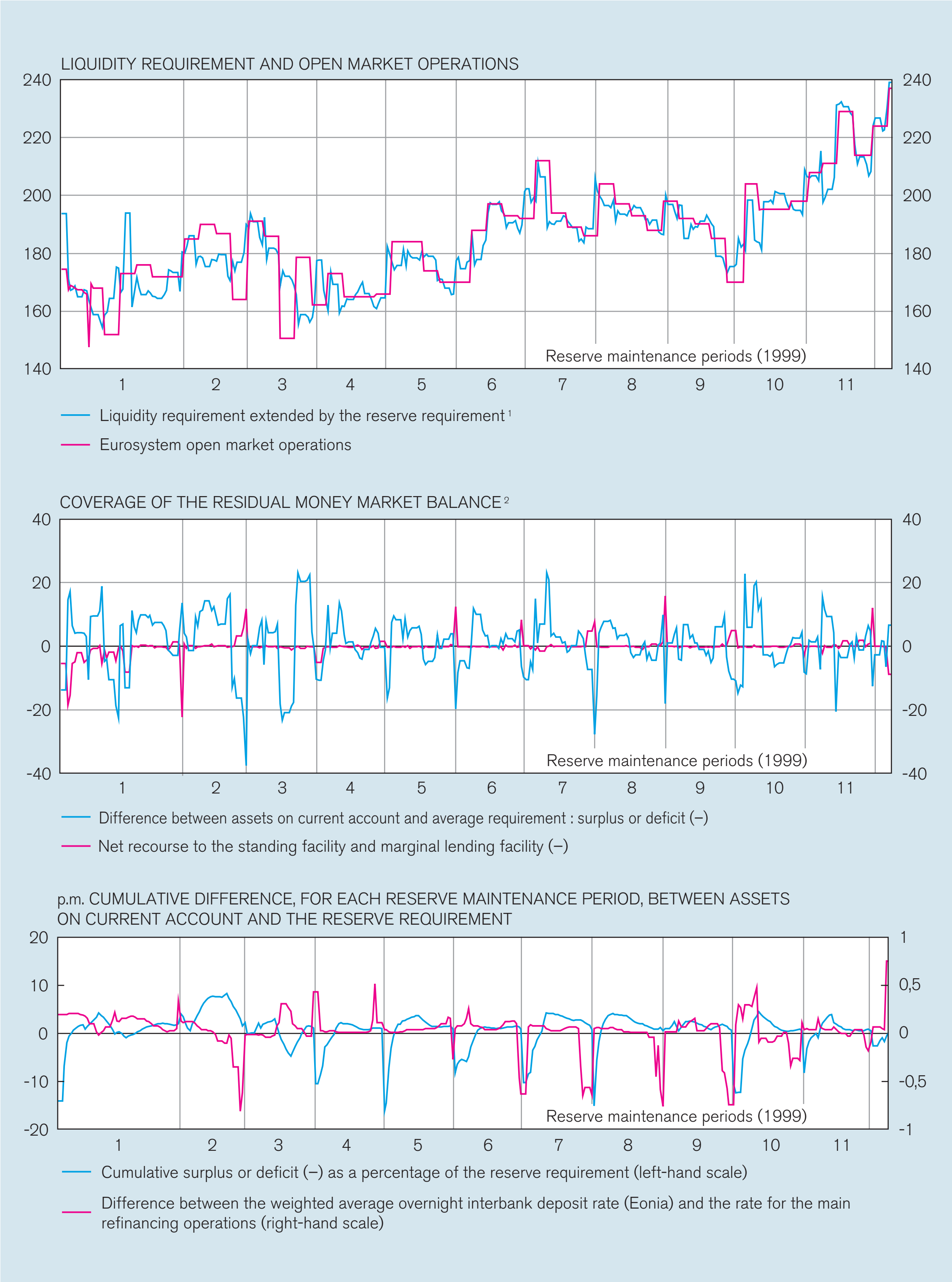
The reserve requirement needs to be respected only on average for a period of one month, so that reserve assets may vary from one day to the next and absorb very-short-term fluctuations in liquidity, such as those due to the variations in the demand for banknotes or in the deposits of public authorities with the national central banks. The system of minimum reserves thus acts as a stabiliser of very-short-term interest rates, making it possible to avoid frequent interventions by the Eurosystem. In 1999, the Eurosystem did not in fact carry out any fine-tuning operation.

The only open market operations carried out by the Eurosystem during the year under review were therefore the regular refinancing operations effected by tenders addressed to all credit institutions in the euro area meeting the counterparty eligibility criteria. The weekly allotments of two-week credits, which are the only ones intended to give monetary policy signals to the markets, represented almost three-quarters of the liquidity injected. The function of the monthly allotments of three-month credits is not to influence interest rates but only to provide a limited amount of longer-term financing.

These monthly tenders are at variable interest rates. In January and February, bidders were served at a single rate ("Dutch-style" tenders); subsequent allotments were at multiple rates ("American-style"). The average rate for these operations, which, like all Eurosystem lending, must be covered by appropriate collateral, remained slightly below the three-month money

CHART 21 — LIQUIDITY POSITION OF CREDIT INSTITUTIONS IN THE EURO AREA

(Daily outstanding amounts, billions of euro)



Source : ECB.

[1] Net liabilities of the Eurosystem resulting from non-monetary-policy operations (and debt certificates issued and securities acquired before 1 January 1999), plus the average reserve requirement.

[2] Residual balance : difference between liquidity injected by open market operations and liquidity requirement.

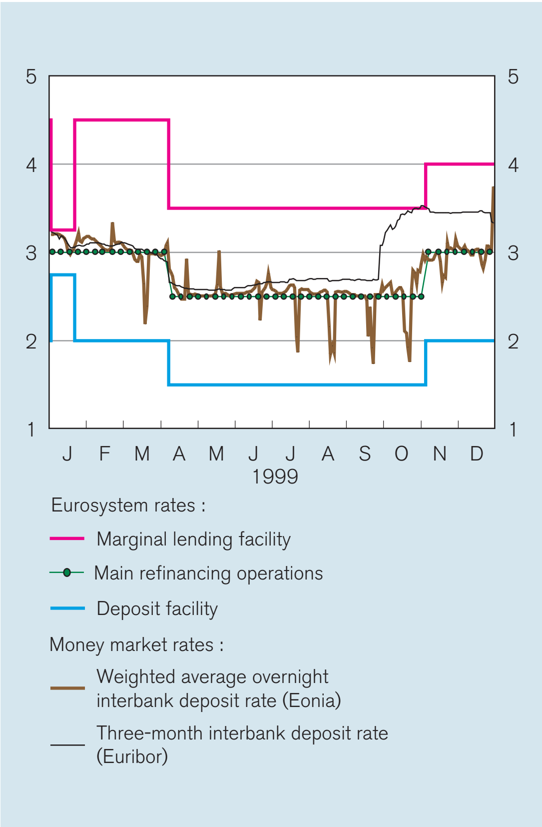
market rate for transactions without collateral. The amount allotted was 15 billion euro up to September. This figure was increased to 25 billion in October, November and December because of the expected rise in demand for banknotes on the eve of the year 2000, so that the outstanding amount of three-month credits rose from 45 to 75 billion.

As regards the main refinancing operations, the ECB reserves the right to choose the method of allotment. In 1999, interest rates for subsequent tenders were always announced at the end of the Governing Council meetings. This procedure made it possible to send out very clear signals regarding the direction of monetary policy. The amounts allotted were determined according to the expected liquidity requirement, and the outstanding amount of two-week credit fluctuated between 106 and 167 billion euro. The ECB systematically permitted credit institutions as a whole to satisfy the reserve requirements in advance : mid-way through the reserve maintenance period, the cumulative assets on current accounts represented, on average in 1999, around 103 p.c. of the reserve requirement.

The aim of this regulation of the liquidity of the money market was to maintain the overnight interest rate at around the rate for the main refinancing operations. The ECB was always successful in injecting liquidity when it so desired, except for the allotment on 6 April (during the third reserve maintenance period) : expectations that the Governing Council would decide to cut interest rates at its meeting on 8 April kept bids down to a particularly low level. Other tenders attracted a surfeit of bids. The first call for tenders brought in bids totalling more than six times the amount allotted, and on 2 November bidding reached a peak of thirty-six times the amount allotted, in anticipation of a decision to raise interest rates at the Governing Council meeting on 4 November. In order to prevent certain credit institutions from being able to benefit excessively from their participation in the weekly allotments, simply because they possess plenty of eligible securities to serve as collateral for their borrowings from the Eurosystem, the ECB was careful to supply sufficient liquid resources. Thus, eight of the eleven reserve maintenance periods in 1999 ended with a net recourse to the deposit facility by the credit institutions. Therefore, after the first reserve maintenance period, the overnight interest rate rarely exceeded the rate for the main refinancing operations by more than 15 basis points, and was sometimes well below it.

Except in the final days of the reserve maintenance periods, recourse to the standing marginal lending and deposit facilities was insignificant, apart from at the beginning of the year : from 4 to 21 January the cost of such recourse was cut by a transitional measure to reduce the

CHART 22 — EUROSYSTEM AND MONEY MARKET INTEREST RATES



Source : ECB.

“corridor” formed by the interest rates on these facilities. During this period in which credit institutions were adapting to the integrated money market of the euro area, the rate on the marginal lending facility was set at 3.25 p.c. and that on the deposit facility at 2.75 p.c.

At the end of this transition period, money market operators seemed sufficiently capable of managing their cash flow in the new environment. The regulation of liquidity by means of the Eurosystem’s weekly tenders and the mechanism of maintaining average reserves over one-month periods were sufficient to contain the volatility of the overnight interest rate. As already mentioned, it generally stayed very close to the rate for the main refinancing operations. It diverged at the end of the reserve maintenance periods when, by definition, the averaging system ceases to play its stabilising role. It usually declined at that point, since the Eurosystem had placed the credit institutions in a situation where they had excess reserves. On the other hand, it was well above the rate on the main refinancing operations both during the days preceding the decision to raise rates on 4 November and again on 30 December, owing to the risk of computer problems due to the advent of the year 2000.

Money market rates for longer-term transactions depend even more on expectations regarding the ECB’s interest rate policy. For instance, the three-month rate was below the overnight rate before the 4 April decision to cut interest rates, and it began to rise by the summer, a trend partly encouraged by the Governing Council’s communication policy. It was in fact the said possibility of computer problems at the time of the transition to the year 2000 that led to the incorporation of a credit and liquidity risk premium in money market interest rates. Thus, the three-month rate rose by almost 40 basis points at the end of September. This premium, which was smaller than that on the US dollar money market, declined in November and December.

The smooth operation of the TARGET cross-border payment system enabled operators to engage in arbitrage, which aligned money market interest rates in the euro area. In this way, participation in the Eurosystem tenders, the pattern of reserve maintenance and the trend of the autonomous factors, such as demand for banknotes or the formation of deposits by public authorities with the central banks, were able to diverge from one country to another without impairing the consistency of the single monetary policy.

Belgian credit institutions seem to have been particularly successful in adapting to the single money market. Their current account assets were fairly volatile and therefore performed efficiently their expected function of absorbing liquidity shocks. These financial intermediaries played little part in most of the monthly tenders, but they obtained plentiful supplies of liquid resources in the weekly allotments.

3. ECONOMIC ACTIVITY

3.1 SUMMARY

The Belgian economy benefited from the improvement in the international environment, especially the recovery in the euro area during the year under review. In the end, the slowdown in economic activity which had begun in Belgium at the beginning of 1998 was only short-lived. The year-on-year GDP growth rate in fact quickened slightly from the first quarter of 1999 onward, and reached 4 p.c. at the end of the year.

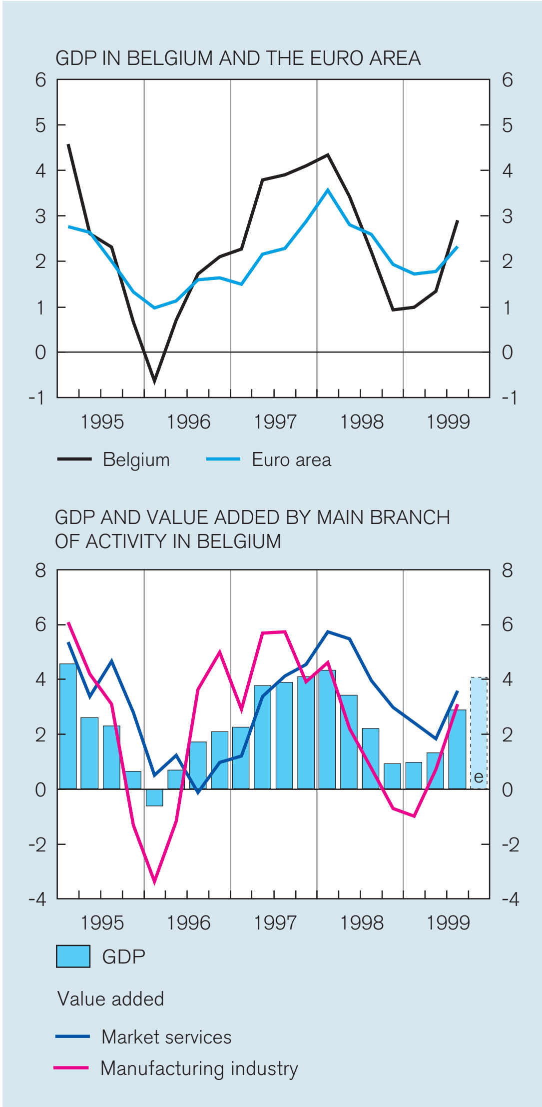
Growth thus reached an average of 2.3 p.c. in 1999, almost half a point down compared to the previous year, because the recovery during the year under review did not compensate for the handicap of a cyclical starting position which was relatively less favourable than in 1998. Thus, if GDP had remained steady throughout 1999 at the level reached at the end of the previous year, then economic activity would have declined by 0.1 p.c. on average, whereas if the same had been the case in 1998 there would have been a rise of 1.6 p.c.

As in the previous year, Belgium's cyclical pattern was slightly more accentuated than that of the euro area, as the more marked deceleration in growth in Belgium in 1998 was also followed by a stronger recovery during the year under review.

The downturn in activity in 1998 occurred in market services and to a still greater extent in manufacturing industry. In the final quarter, the value added in manufacturing industry was actually less than it had been a year earlier, a situation which recurred at the beginning of the year under review. Industry began to recover in the second quarter, despite the "dioxin" crisis, i.e. the contamination of part of the food chain with that substance in June.

CHART 23 — QUARTERLY GDP AND VALUE ADDED BY MAIN BRANCH OF ACTIVITY AT 1995 PRICES

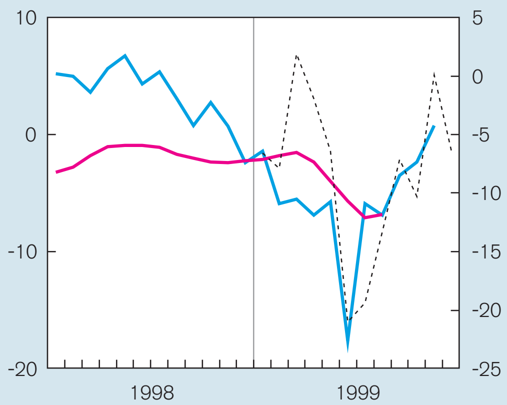
(Percentage changes compared to the corresponding period of the previous year)



Sources : EC, NAI, NBB.

In the end, this incident seems to have had only a minor influence on total value added. It affected the output of certain sectors of agriculture and the food industry from June 1999 onwards, but most of the effects faded fairly

CHART 24 — ECONOMIC SITUATION IN THE FOOD INDUSTRY



Sources : NSI, NBB.

rapidly during the summer. Thus, the large fall in the gross synthetic indicator for the food industry, observed in June in the results of the business surveys, was steadily eliminated thereafter, and by September this indicator was almost back to its pre-crisis level. Similarly, from July onwards the data of the index of food industry output ceased to show any significant effects, even though the trend of activity had still not resumed its normal course in some sub-sectors, notably the meat industry.

Altogether, the contamination of food products with dioxin caused the Belgian economy to suffer an overall loss of value added estimated at around one quarter of a per cent in 1999, account being taken of the indirect effects on other sectors upstream and downstream of agriculture and the food industry. As the analysis of the allocation of output will show, it was mainly exports that were affected.

The loss of earnings suffered during the summer and the costs caused by the crisis obviously impaired the financial position of enterprises operating in the agricultural and food industry sectors; these enterprises are generally small and therefore relatively fragile in the face of unexpected shocks. Various measures were taken, notably in consultation with the tax authorities, social security institutions and banks, in order to limit any cash-flow problems and above all to provide compensation for the cost of destroying unsaleable goods.

3.2 MAIN CATEGORIES OF EXPENDITURE

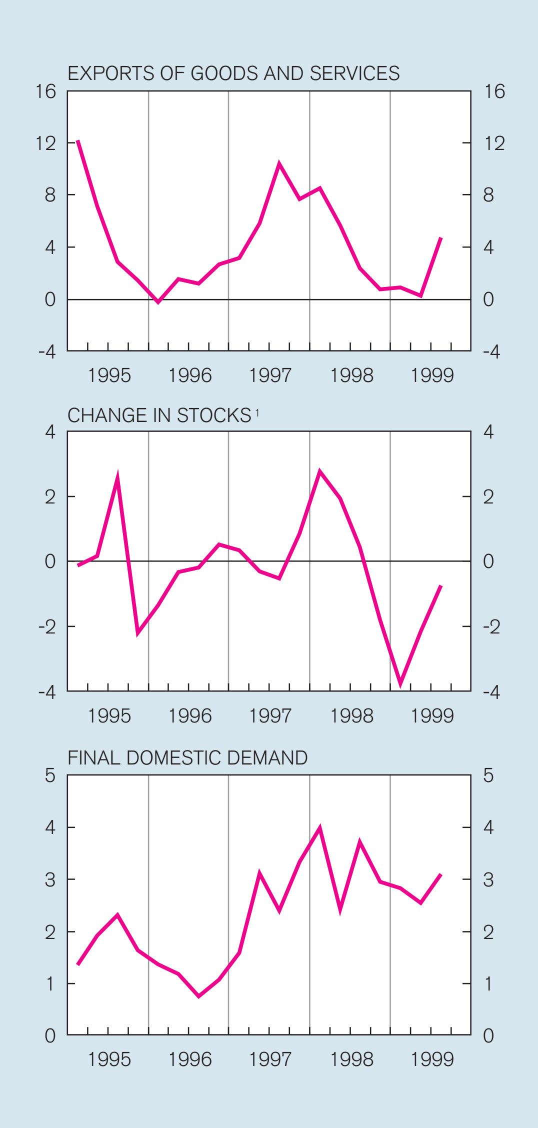
The slower average growth in 1999 was due largely to the slump in external demand which had begun in the second half of 1997 and persisted until the middle of the year under review. This affected not only exports but also – indirectly – the trend of stocks. On the other hand, the growth in final domestic demand remained relatively vigorous.

As in the rest of the euro area, it was mainly from the second half of 1998 onwards that Belgium's exports of goods and services suffered from the sharp slackening of world demand. However, by the beginning of 1999 Belgian enterprises were becoming more optimistic about the outlook for external markets. The results of the monthly business surveys actually reveal that, after a low point in December 1998, firms in manufacturing industry became steadily more upbeat about their export order books. In comparison with enterprises in the euro area, companies based in Belgium also seem to have been quicker to notice the signs of a reversal in the trend, as they had been on several occasions in the past. At the time of each of the last four turning points in the cycle, Belgian economic indicators reacted slightly faster than the indicator for the euro area as a whole. Nevertheless, Belgium's exports generally move in line with those of the euro area.

Thus, exports remained disappointing for the first two quarters of 1999 even though the above-mentioned economic indicator began to recover as early as January. During this period, the more sustained demand on the emerging markets was in fact insufficient to offset the

CHART 25 — COMPONENTS OF TOTAL DEMAND AT 1995 PRICES

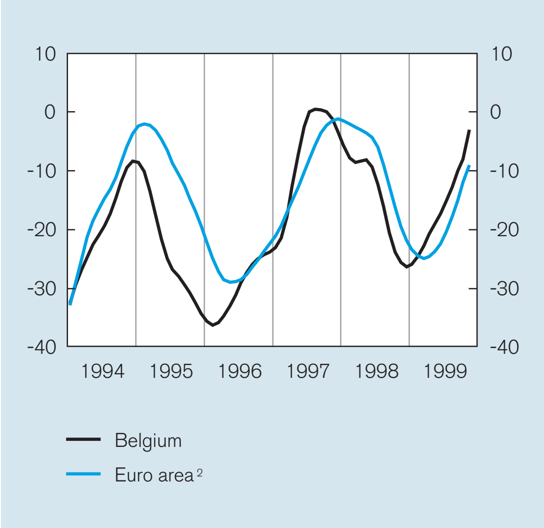
(Percentage changes compared to the corresponding period of the previous year)



Sources : NAI, NBB.
[1] Contribution to the growth in GDP.

CHART 26 — ASSESSMENT OF EXPORT ORDER BOOKS IN MANUFACTURING INDUSTRY

(Smoothed [1], seasonally adjusted data)



Sources : EC, NBB.
[1] From September 1999 onwards, estimates based on gross data.
[2] Data with a one-month time lag, as EC dating is one month later than that adopted for the NBB data for the same survey period.

decline in exports to partners in the euro area. Apart from the weakness of demand from the main trading partners, Belgian exports also suffered from the repercussions of the dioxin crisis : the European Veterinary Committee initially decided to impose a temporary ban on exports of the products directly affected, and then to subject them to highly stringent checks. These measures caused a very marked temporary fall in exports of agricultural and food products : while these exports had declined by 6 p.c. in value during the first five months of the year compared to the corresponding period in 1998, they slumped by more than 20 p.c. in June. Fears that the crisis would persist fortunately proved unfounded. In September, total sales abroad of agricultural and food products were already back to the level prevailing before the outbreak of the crisis, although some sectors such as the meat industry were still experiencing problems.

Though one cannot rule out the possibility that the foreign sales of some other branches of industry may have suffered temporarily from the tarnished image of products made in Belgium, the eventual impact of the dioxin crisis on exports seems to have been relatively modest, measured for 1999 as a whole. It represented some 2.5 percentage points for exports of agricultural products and manufactured foods, but, in view of the minor importance of these sectors in total exports of goods and services, the overall negative effect on the latter can be estimated at around a quarter of a percentage point.

In the second half of the year under review, the downward trend of foreign sales was totally reversed by the strong recovery in demand in the euro area and the other EU countries. Over 1999 as a whole, exports of goods and services increased by 2.9 p.c.

Stocks built up by enterprises at the end of 1997 and the beginning of 1998, when demand was still strong, subsequently proved excessive, in view of the downturn in economic activity which spread to a greater extent than expected from the emerging economies to the EU, and to other regions such as the transition countries, with which some euro area countries maintain close trading links. In the final quarter of 1998 and the first half of 1999, enterprises reduced their stocks to a more appropriate level in the light of expected demand. Over the year under review as a whole, this movement caused a marked deceleration in growth. Incidentally, there is no indication that enterprises increased their stocks temporarily as a precaution against any problems in the transition to the year 2000.

While economic growth was impeded at the beginning of 1999 by factors over which Belgian economic agents have little control, it was, on the other hand, constantly sustained by demand from households, enterprises and general government alike.

After a strong expansion between mid-1997 and the end of 1998, the final consumption expenditure of individuals continued to grow, but at a slightly slower pace. It is mainly purchases of durable goods, particularly cars, that have risen in recent years. New car registrations were up again in 1999, whereas they normally decline in years when the motor show is not held. Apart from more general factors such as the buoyant economy and the historically low level of interest rates, one possible explanation for this trend is the replacement of cars registered at the time of the spate of purchases which followed the opening of the frontiers between eastern and western Europe in the late 1980s. At the time, this led to a massive demand for second-hand vehicles on terms which encouraged the replacement of the stock of cars in Belgium. Consumption of communication products such as mobile phones, personal computers and software has also risen significantly since the middle of 1997.

Overall, private consumption grew by an average of 2 p.c. in 1999, or 1.8 percentage points less than the previous year. This slowdown is linked to the more modest increase in individuals' disposable incomes in real terms.

The increase in total wages and salaries, the main component of the primary income of individuals, slowed down in 1999 as the growth of employment slackened. However, the change in the total wage bill does not necessarily present a true picture of the change in the income which individuals obtain from their work, after the various deductions applied in the form of contributions and direct taxes. Measures were taken in 1999 to reduce the scale of these levies, as is evident from the deceleration in transfers paid to general government. The rise in wages and salaries paid by employers was appreciably slowed down by the new reductions in employers' contributions, applicable for the most part from 1 April 1999, without there having been any direct impact on the disposable income of employees. Conversely, their purchasing power was boosted by the full reindexation of the tax scales used for calculating personal income tax, a measure which has no effect on the total cost of wages and salaries borne by enterprises and general government. Altogether, the rise in net wages outstripped not only the latter but also the previous year's increase.

As regards rents, which form the largest component of the gross operating surplus of households, increases were held down because the health index of consumer prices, used here, as in the case of wages, as a reference for index-linking, rose less steeply than in 1998.

The trend of other resources of individuals was even less favourable. Incomes from property were slightly down compared to the previous year : the increase in the level of investments by individuals was insufficient to offset the fall in the yields on new financial assets compared to those on old investments maturing. Furthermore, the more modest growth in economic activity in 1999 was reflected in the less marked rise in the compensation and profits of self-employed persons, though the situation did vary considerably from one type of occupation to another. For instance, the rise in the incomes of professionals in the medical sector speeded up.

Consumption expenditure by households did not fully reflect the smaller increase in their purchasing power, since their savings ratio declined for the sixth consecutive year.

Expenditure on housing rose only slightly, by 0.2 p.c., in 1999. One of the reasons for this was the expiry in mid-1998 of the measures reducing VAT on the construction of certain categories of housing. In addition, building costs and land prices were rising, while mortgage interest rates rose sharply from June 1999 onwards, though they had admittedly been at a record low. The sluggishness of new housing construction was partly offset by conversion and selling activity on the secondary market, which had been intensifying for several years. In the national accounts, secondary market transactions are reflected in expenditure on housing,

TABLE 10 — GROSS DISPOSABLE INCOME OF INDIVIDUALS AT CURRENT PRICES

(Percentage changes compared to the previous year)

	1996	1997	1998	1999 e	p.m. 1999 e, in billions of euro
Gross primary income	1.4	3.5	3.8	2.6	180.2
Wages and salaries	1.5	3.8	3.8	3.3	121.5
Incomes from property [1]	−0.8	2.6	2.4	−2.0	21.3
Compensation and profits of self-employed persons	1.5	3.0	5.6	2.6	20.5
Gross operating surplus	3.6	3.1	3.9	3.2	16.8
Net current transfers paid [2]	1.6	8.7	4.2	2.3	−32.6
of which :					
From and to general government	0.2	7.9	4.7	1.7	−30.9
Transfers received	2.4	3.1	2.6	2.2	39.7
Transfers paid	1.4	5.1	3.5	2.0	−70.6
Gross disposable income	1.3	2.5	3.7	2.7	147.5
p.m. At constant prices [3]	*−0.7*	*0.8*	*2.7*	*1.5*	*139.3*

Sources : NAI, NBB.

[1] These are net amounts, i.e. the difference between incomes from property received from other sectors and incomes from property paid to other sectors.

[2] These are net amounts, i.e. the difference between transfers received from other sectors and transfers paid to other sectors, excluding transfers in kind.

[3] Data deflated by the national index of consumer prices.

TABLE 11 — GDP AND THE MAIN CATEGORIES OF EXPENDITURE AT 1995 PRICES

(Percentage changes compared to the previous year)

	1996	1997	1998	1999 e
Final consumption expenditure of individuals	0.6	2.2	3.8	2.0
p.m. Individuals' savings ratio[1]	*18.7*	*17.8*	*16.7*	*16.3*
Housing	−4.0	4.9	2.3	0.2
Gross fixed capital formation by enterprises	4.3	7.2	4.5	7.8
Expenditure by general government	1.5	0.4	1.4	2.8
Final consumption expenditure	2.3	...	1.4	2.1
Investment	−7.8	5.2	1.0	11.1
Total final domestic expenditure	1.1	2.6	3.3	3.0
Change in stocks[2]	−0.3	0.1	0.8	−1.1
Exports of goods and services	1.3	6.7	4.2	2.9
Total final expenditure	1.0	4.4	4.2	2.3
Imports of goods and services	1.0	5.8	6.3	2.2
Net exports of goods and services[2]	0.3	0.9	−1.2	0.6
GDP	1.0	3.5	2.7	2.3

Sources : NAI, NBB.

[1] Percentages of individuals' gross disposable income at current prices.

[2] Contribution to the change in GDP.

but only to the extent of the registration fees paid when such transactions take place.

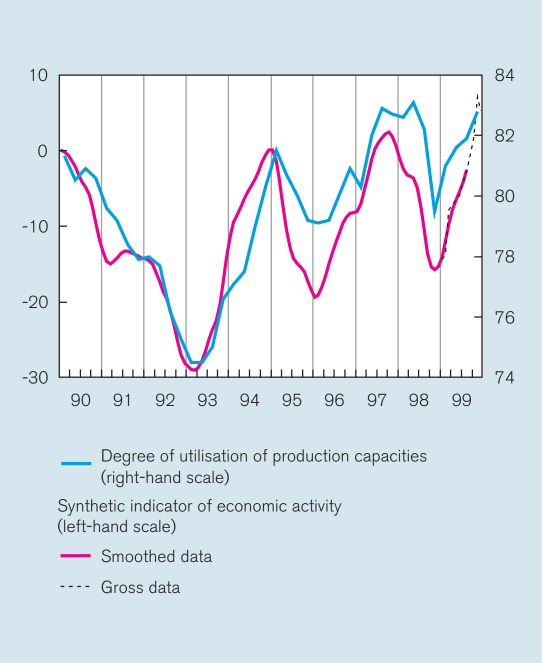
From the final quarter of 1998, enterprises displayed growing optimism about the economic outlook. In this connection, the dioxin crisis does not seem to have spread to enterprises which were not directly concerned. Moreover, rates of utilisation of production capacities once again reached a high level. The profitability of enterprises as a whole also remained satisfactory. In this context, with a rise of almost 8 p.c., investments by enterprises were the most dynamic element of domestic demand in 1999, along with investments by general government.

More detailed analysis of this trend reveals fairly marked differences in behaviour from one branch of activity to another. Firms operating in market services were the main ones to step up their investment substantially. This was the case particularly in the transport and communications sector, owing partly to major projects connected with the continuing expansion of the mobile phone network. Gross fixed capital formation also rose significantly in the business services sector. In industry, on the other hand, it generally remained at a lower level. Certain branches of activity such as textiles and the gas sector had in fact invested heavily in recent years. In the motor vehicles sector, where a number of major projects for increasing production capacity are in progress, there was a large increase in gross fixed capital formation.

Final consumption expenditure by general government grew by 2.1 p.c. in 1999, against 1.4 p.c. in 1998. This quickening was due entirely to expenditure on health care, which – according to the conventions adopted by the NAI in the new reference methodology for the national accounts : ESA 95 – is imputed to the sector which ultimately pays the cost of financing, i.e. in most cases general government, rather than households. The influence of this expenditure on the final consumption of general

CHART 27 — DEGREE OF UTILISATION OF PRODUCTION CAPACITIES AND SYNTHETIC CURVE OF ECONOMIC ACTIVITY IN MANUFACTURING INDUSTRY

(Seasonally adjusted data)



Source : NBB.

government is more visible than that on private consumption calculated by the old methodology, account being taken of the substantial difference in size between these two categories of expenditure. The amount disbursed for health care in fact represents almost one third of the final consumption of general government whereas it constituted only about one tenth of private consumption. Other public consumption expenditure increased less fast than in 1998, and this applied both to compensation and pensions paid to public authority personnel and to purchases of goods and services by general government.

Public investment grew strongly, by more than 11 p.c., in 1999. The impending local elections induced local authorities to initiate major public works programmes.

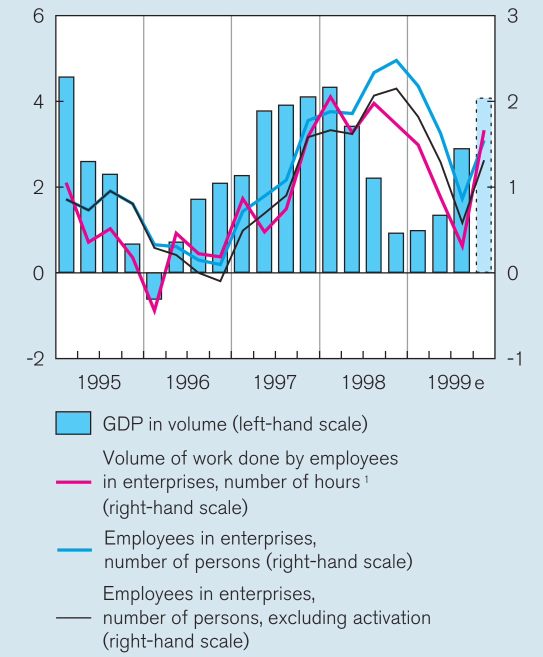
Overall, the increase in total final demand was only 2.3 p.c. during the year under review, whereas it had reached 4.2 p.c. in 1998. However, the impact which this marked slowdown had on GDP was tempered by its repercussions on imports of goods and services, the rise in which slowed from 6.3 p.c. in 1998 to 2.2 p.c. in 1999. Imports were restrained even more by the fact that, among the main categories of final expenditure, it was the most import-intensive expenditure that made the largest contribution to the decline in growth in 1999, namely stock formation and exports. Unlike in 1998, the growth of the latter nevertheless outpaced the rise in imports, so that the contribution of net exports of goods and services to growth became positive again, representing 0.6 percentage point of GDP.

4. LABOUR MARKET

The annual growth in the volume of work done by employees in enterprises kept closely in line with the trend of economic activity, slowing from 1.8 p.c. in 1998 to 1.1 p.c. in 1999. The rise in the number of paid workers employed by enterprises also slackened in 1999, but to a lesser extent, slowing from 2.1 p.c. to 1.6 p.c. The fact that this fall was more moderate is attributable to the continuing expansion of part-time working, particularly via the policy of activating unemployment benefits, while recourse by enterprises to temporary lay-offs does not generally seem to have played a special role in this connection in 1999.

CHART 28 — ACTIVITY AND EMPLOYMENT

(Percentage changes compared to the corresponding quarter of the previous year)



Sources : NAI, MEL, NSI, FPB, NEMO, NBB.

[1] The volume of work corresponds to the number of employees expressed as full-time equivalents multiplied by the contractual annual working hours and adjusted to take account of hours not worked by workers temporarily laid off.

It is true that temporary lay-offs, which enterprises use as a way of avoiding redundancies when coping with changes in activity regarded as incidental or temporary, did increase during the first half of the year following the slackening of growth of the Belgian economy in the second half of 1998 and at the start of the year under review. The fears aroused by the dioxin crisis at the end of the first half of 1999 did not materialise and the crisis made only a marginal contribution towards the increase in temporary lay-offs. In contrast, the strong recovery apparent during the latter part of 1999 was reflected in a marked reduction in this type of unemployment : in terms of seasonally adjusted data, it dropped back during the fourth quarter to below the levels recorded during previous periods of sustained growth of activity.

Although the rate of expansion of paid employment in enterprises was lower on average in 1999 than in the previous year, this movement is still remarkable when viewed in an historical context, since – from the start of the 1980s until 1997 – 1988 was the only year to show a larger annual increase in paid employment.

The employment policy implemented in recent years is one reason for this result. While it is difficult to measure the number of additional jobs created by the many measures which make up this policy, particularly those which provide for reductions in employers' social security contributions, the NEMO payment statistics can be used to assess the success of the measures for getting the unemployed back into work while they continue to draw unemployment benefits. The activation policy, which consists in subsidising a large proportion of the compensation paid to the long-term unemployed taking on part-time work, represents – along with youth employment incentives – one of the pillars of the government's employment policy as defined in the Belgian

TABLE 12 — EMPLOYMENT

(Number of persons in work in thousands of units ; annual averages unless otherwise stated)

	1998	Change in 1999 e	
			(percentages)
Total employment	3,855	40	1.0
Domestic employment	3,801	40	1.0
of which :			
Self-employed workers	693	−1	−0.2
Employees	3,108	41	1.3
of which :			
Public authorities and education [1]	703	3	0.5
Enterprises	2,404	37	1.6
Frontier workers (balance)	54	...	...

Sources : NAI, NBB.

[1] This item corresponds to the Nace-Bel L and M branches as defined by the NAI.

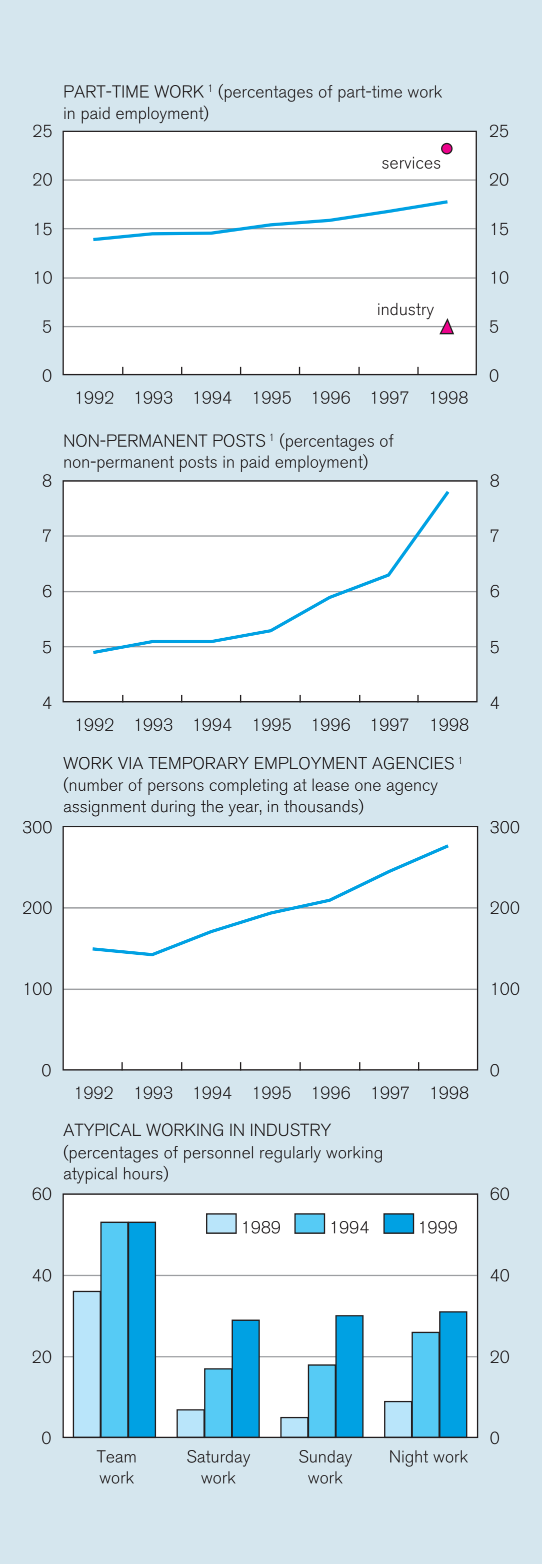
action plan for employment submitted to the European Commission in June 1999.

The number of persons obtaining work under one form or another of the unemployment benefit activation policy was almost 7,500 units higher at the end of 1999 than in December 1998. Altogether, some 29,000 people benefited from these measures : 5,500 were employed in the public sector and NPIs under the occupational transition programmes, 7,500 took a “SMET” job, mainly in the private market sector, and 16,000 worked through Local Employment Agencies, doing sufficient work to be exempted from signing on as job-seekers, and therefore to be recorded as persons in work. Anyone who has done at least 180 hours’ work through a Local Employment Agency job-creation scheme over a period of six months preceding their application is exempt from signing on as a job-seeker. In addition, almost 23,000 other unemployed persons worked an insufficient number of hours to qualify for this exemption, so that altogether around 39,000 unemployed persons were taking part in the Local Employment Agency scheme at the end of the year.

In 1999, 41,000 additional paid jobs were created on average in the economy as a whole, representing a rise of 1.3 p.c. in the number of persons employed. Over a quarter of this is attributable to the different measures for the activation of unemployment benefits mentioned above. The size of the increase in employment recorded in recent years is due to a combination of various factors which together helped to boost the employment-intensity of growth. The above-mentioned activation measures have created jobs for people — especially the low-skilled — who, under current conditions, are having difficulties in getting into the regular labour market. At the same time, the moderate rise in labour costs, by exerting a favourable influence on the comparison between the cost of the labour factor and the cost of the capital factor, has doubtless slowed down the process of substitution of capital for labour. Finally, in recent years, certain labour market trends have increased the scope for adjustments between the supply of and demand for labour, thus conforming to the wishes of enterprises, but also those of some workers.

Thus, part-time working continued to increase its share of total employment. In 1998, part-time workers represented 17.8 p.c. of the number of employees. This type of working should continue to expand, as the jobs being created by the activation of unemployment benefits are all part-time. Moreover, there is still a labour redistribution potential which has been little exploited in industrial sectors, since part-time working represented only 5 p.c. of jobs in 1998, whereas in services it totalled over 23 p.c. Furthermore, employers are making increasing use of workers taken on under fixed-term contracts or agency staff, to cater for temporary labour shortages. This raised the proportion of non-permanent posts from around 5 p.c. at the beginning of the 1990s to almost 8 p.c. in 1998. The number of persons carrying out an agency assignment in 1998 totalled almost 280,000, or close on twice as many as at the start of the decade. Finally, to match the organisation of labour more closely with production requirements, much use is made

CHART 29 — INDICATORS OF THE FLEXIBILITY OF THE LABOUR MARKET



Sources : NSI, Upedi, NBB.

[1] Data on part-time working, non-permanent posts and temporary employment through agencies.

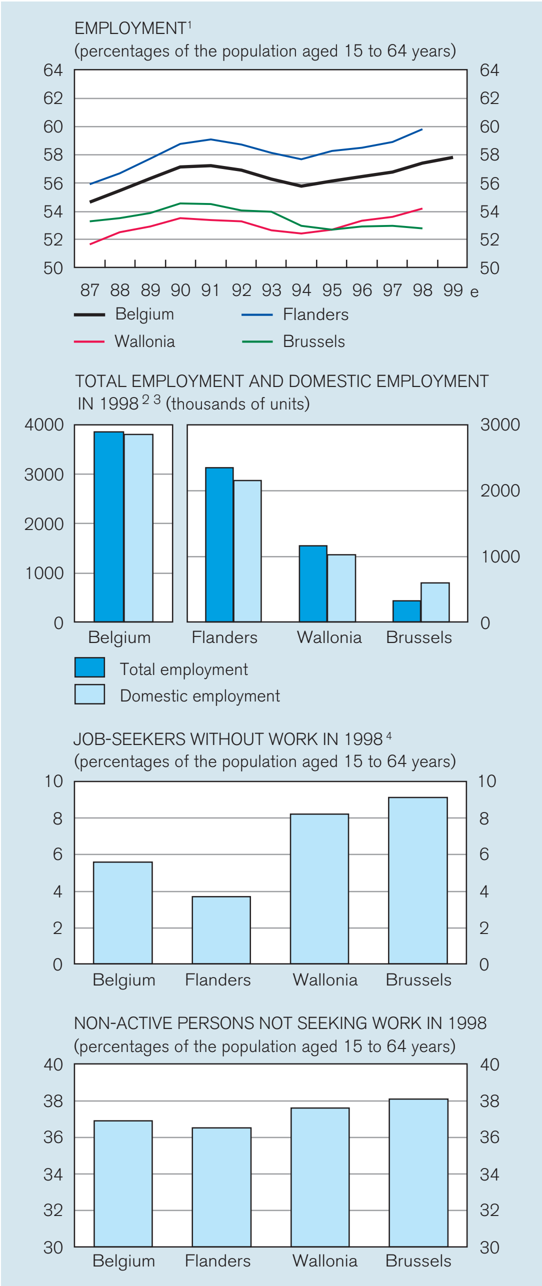
of atypical working hours in Belgium : in 1999, almost a third of the people employed in industry regularly worked on Saturdays, Sundays or at night, and over half were regularly involved in team work. Although the use of atypical hours is, on average, more widespread in Belgium than in other EU countries, Belgium still has some leeway to make up as regards part-time work and non-permanent posts.

The number of self-employed persons remained virtually unchanged in 1999, as did the balance of frontier workers, which represents the difference between the number of residents working abroad and the number of non-residents employed in Belgian production units. As a result, national total employment increased by 40,000 units, roughly the same as paid employment, or by 1 p.c. on average. This development, combined with a modest increase in the population of working age, was reflected in a further rise in the employment rate, which, by relating these two variables, represents the proportion of the population of working age actually in work, be it full-time or part-time. Since 1994, the year when it reached a low point of 55.8 p.c. following the downswing in economic activity in 1993, the employment rate has risen continuously, reaching 57.5 p.c. in 1998 and 58 p.c. in 1999, a level comparable to that recorded at the end of the 1970s. However, the employment rate seen in Belgium is still below that for the EU as a whole, which amounted to 60.8 p.c. in 1998, and even further below the average employment rate of the three main neighbouring countries, Germany, France and the Netherlands, which was 62.9 p.c.

Within the EU or the euro area, the employment rate figures vary widely from country to country. Similarly, within a country there may be large variations from one region to another. In Belgium, while the pattern of the movement of the employment rate observed in the two main geographical regions of the kingdom was generally identical from the late 1980s onwards, the level recorded was very different. On 30 June 1998, the latest date for which the administrative

CHART 30 — BREAKDOWN OF THE POPULATION OF WORKING AGE IN BELGIUM AND IN THE THREE REGIONS

(At 30 June)



Sources : EC, NAI, MEL, NBB.

[1] Employment rate, or the number of persons in work according to administrative sources, expressed as a percentage of the population of working age. The latest data available by region relate to 1998.

[2] The difference between Belgium and the total for the regions is due to employment which cannot be broken down between the regions, particularly civil and military defence personnel working in Germany.

[3] Domestic employment comprises the number of persons working in a particular territory, regardless of their place of residence, while total employment means persons in work, resident in a particular territory, regardless of the place where they work.

[4] Number of unemployed within the meaning of the International Labour Organisation (any person without a job who is actively seeking work and is available for work), according to the labour force survey.

series on employment issued by the Ministry of Employment and Labour are available, the employment rate was 59.8 p.c. in Flanders, against only 54.2 p.c. in Wallonia and 52.8 p.c. in Brussels. In earlier years, the Brussels Capital region had seen a less favourable trend than the other two entities : while the employment rate reached a low point in 1994 and subsequently recovered in Wallonia and Flanders, in Brussels it continued to fall in 1995 and has since remained more or less stable.

At both regional and national level, the employment rate represents the proportion of the population of working age resident in the territory and actually in work, whatever the geographical area where that activity is pursued. This indicator therefore does not necessarily reflect the strength of demand for labour in a given region, since there may be large-scale transfers of workers between geographical areas. In Belgium, the Brussels Capital region absorbs most of the trans-regional transfers of workers. On 30 June 1998, around 335,000 workers not resident in Brussels were pursuing an activity there, while 56,000 residents had a job outside the region where they were living. Net inflows of workers therefore totalled around 279,000 – a figure almost equivalent to the number of residents working in the actual region – while in Flanders and Wallonia net outflows of 199,000 and 135,000 respectively were recorded.

In its recommendations on employment, the European Commission attaches particular importance to increasing the employment rate, placing special emphasis on the low rate of participation by women and older people in the labour market. Calculated by age group, the employment rate in Belgium is particularly low for the population of working age belonging to the youngest age group and for older people, for whom it was 26 and 36.6 p.c. respectively, while the employment rate for the population aged 25 to 49 years was almost 77 p.c., a rate comparable to the average in the three main neighbouring countries.

TABLE 13 — EMPLOYMENT RATE: BREAKDOWN BY AGE AND GENDER[1]

(Percentages of the population of the corresponding age group)

	15-64 years	15-24 years	25-49 years	50-64 years
Men				
Belgium	67.0	29.3	87.0	49.6
Three main neighbouring countries[2]	70.9	41.2	87.0	56.4
Women				
Belgium	47.5	22.5	66.3	24.1
Three main neighbouring countries[2]	54.9	36.1	69.0	38.0
Total				
Belgium	57.3	26.0	76.8	36.6
Three main neighbouring countries[2]	62.9	38.7	78.0	47.1

Sources: EC, NSI.

[1] The data shown in this table were obtained exclusively from the labour force survey. The figures for Belgium therefore differ from those obtained from the other administrative sources used elsewhere in this chapter.

[2] Germany, France, Netherlands.

The low employment rate among the youngest people is due largely to the education and welfare system prevailing in Belgium, which is based mainly on full-time education, in contrast to the German system based on alternation of training and education and the Dutch system which favours part-time working by students. At the other end of the age pyramid, the fact that women join the Belgian labour market later and the use of various systems of early withdrawal from the labour market are the reasons for the low employment rate recorded in Belgium for the population aged 50 to 64 years, namely 36.6 p.c. in 1998, whereas in the three neighbouring countries the rate averaged 47.1 p.c. This peculiarity of the Belgian labour market is already apparent in the 50 to 54 age group, for which the employment rate was 60 p.c. against an average of around 72 p.c. in the three neighbouring countries.

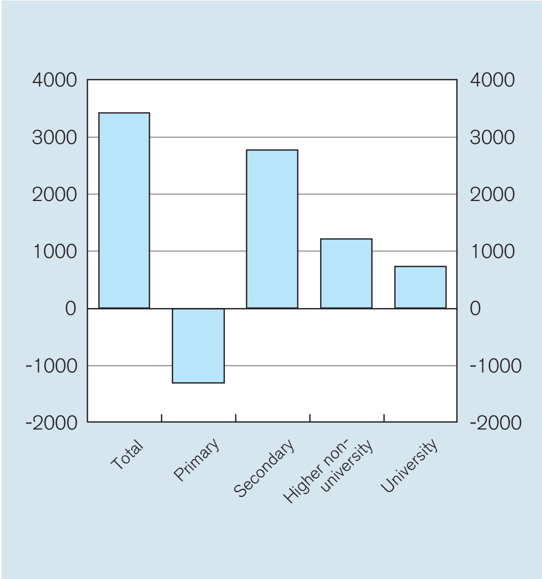
The Belgian labour market features two systems of early withdrawal from working life paid for out of the general government budget, thus depriving the market of a large proportion of the labour force of working age even though, in certain regions, sectors or occupational skills, there is a shortage of workers. Thus, in June 1999 7 p.c. of the population aged 50 to 64 years was covered by the collectively agreed early retirement scheme. Though this proportion has certainly been falling for several years, the decline has been more than counterbalanced by the rise in the number of older unemployed persons not seeking work, who in June 1999 represented 8.2 p.c. of the population aged 50 to 64 years, almost twice the percentage recorded in 1995 before access to this scheme was made easier. Altogether, these two systems of early withdrawal from the labour market concerned 15.2 p.c. of the population aged 50 to 64 years in 1999 : 21.9 p.c. of the men and 8.8 p.c. of the women.

In 1998, non-active persons, i.e. persons of working age who, although without a job, state that they are not seeking work, represented a relatively similar proportion of the population of working age in the three regions, namely 36.5 p.c. in Flanders, 37.6 p.c. in Wallonia and 38.1 p.c. in Brussels. In other words, the differences in employment rates between the three regions were almost entirely reflected in the differing proportions of unemployed job-seekers.

While the comparatively high proportion of non-active persons can be explained in part, at the two extremes of the age pyramid, by peculiarities of the education system or the schemes for withdrawal from working life, some of these persons who are not working also fail to present themselves on the labour market because they consider that there is not a job available for them. The number of these non-active persons, like the number of unemployed, could be reduced, especially by more appropriate training. The employment rate does in fact rise considerably with the level of education : in 1998, the rate in Belgium for the population aged 25 to 59 years was 43.5 p.c. for persons of primary education standard and almost 90 p.c. for university graduates. True, the proportion of highly skilled persons in the population aged 25 to 59 years is higher in Belgium than in the three neighbouring countries, but the proportion of persons with low skills is also higher, thus depressing the production potential of the economy as a whole.

CHART 31 — NET RECRUITMENT [1] IN 1998, BROKEN DOWN BY LEVEL OF EDUCATION

(Units)



Source : NBB.

[1] Balance of workers taken on and leaving, entered in the staff register of enterprises which submit a full social balance sheet to the Central Balance Sheet Office and in which the number of workers on permanent contracts represented at least 98 p.c. of the workforce registered at the end of the 1998 financial year.

The increase in the standard of training required by employers is also a characteristic of the changes taking place on the labour market. The information obtained from the "social balance sheet" highlights this trend. In 1998, net recruitment by enterprises submitting a full set of accounts to the Central Balance Sheet Office and employing mostly workers on permanent contracts related exclusively to workers with at least a certificate of secondary education, while the number of workers of primary education standard declined. This decline involved both male and female workers, whether working full-time or part-time.

While improvement in the level of basic training, by enhancing employability, is one of the keys to raising the employment rate, in-service training enables workers to upgrade their skills and adapt to new technologies. Recognised as one of the guidelines of the European employment policy, investment in human resources is also at the heart of the December 1998 interprofessional sectoral agreement, which stipulates that the efforts made in in-service training must attain the average for the three main neighbouring countries within six years, and total at least 1.4 p.c. of labour costs by the end of the agreement covering the 1999-2000 period.

TABLE 14 — TRAINING IN PRIVATE SECTOR ENTERPRISES

	1997	1998
Training cost *(percentage of labour costs)*	1.3	1.4
Number of persons receiving training *(percentage of total workforce)*	34.2	36.5
Training hours *(percentage of the total number of hours worked)*	0.8	0.9

Source : NBB.

The social balance sheet makes it possible to assess the amount of effort devoted to training by private sector enterprises. Between 1997 and 1998 the budget which they allocated to training increased by over 13 p.c. to represent 1.4 p.c. of labour costs in the private sector as a whole in 1998, though large divergences were evident between the different branches of activity. Over a third of the workforce was involved in a training course during that year, each trained worker having received an average of around 36 hours' training, or 2.3 p.c. of the annual average working hours of a full-time worker. Altogether, however, the total training effort represented just 0.9 p.c. of the number of hours worked.

5. COSTS AND PRICES

5.1 COSTS

In 1999, unlike in earlier years, wage formation in Belgium took place without any direct government intervention. Management and labour had in fact concluded, in December 1998, an interprofessional sectoral agreement for 1999-2000 which, in accordance with the law of 26 July 1996 on the promotion of employment and the preventive safeguarding of competitiveness, set as the reference for negotiations in sectors and enterprises the average wage increase expected in the three main neighbouring countries, which the Central Economic Council estimated at 5.9 p.c. over the two years as a whole. However, some latitude was left in this agreement, in order, for instance, to take account where necessary of situations specific to particular sectors.

It was this agreement that provided the framework for negotiating collective labour agreements in the sectors during the first half of 1999. They concern about two million workers and deal with increasing purchasing power, in-service training and employment, and also other working conditions such as the policy on safety and health in enterprises. It is difficult as yet to make an accurate assessment of the impact of these agreements on the trend of labour costs in 1999. The indices of collectively agreed wages for manual and non-manual workers published by the MEL are the only source offering information on the trend of gross nominal com-

TABLE 15 — INDICES OF LABOUR COSTS [1]

(Percentage changes compared to the corresponding period of the previous year)

	Indices of collectively agreed monthly wages [2]			Hourly labour costs	p.m. Index of hourly labour costs in the three main neighbouring countries [3]
	Total	Indexations	Wage increases under collective agreements		
1996	1.7	1.7	...	1.0	2.1
1997	1.7	1.5	0.2	2.5	2.2
1998	1.9	1.2	0.7	2.1	2.1
1999	1.7	1.1	0.5	n.	n.
1st quarter of 1998	1.9	1.0	0.8	2.0	2.0
2nd quarter of 1998	1.8	1.0	0.8	1.2	2.2
3rd quarter of 1998	2.1	1.5	0.6	2.6	2.1
4th quarter of 1998	1.8	1.3	0.5	2.6	2.2
1st quarter of 1999	1.4	1.2	0.2	2.6	2.2
2nd quarter of 1999	1.7	1.4	0.3	n.	2.1
3rd quarter of 1999	1.8	1.0	0.8	n.	n.
4th quarter of 1999	1.7	0.9	0.8	n.	n.

Sources: EC, MEL.

[1] Industry and services excluding public authorities.

[2] Weighted average of indices of the wages, under collective agreements, of manual and non-manual employees. The index for manual employees has been adjusted to eliminate the effect on hourly wages of the reduction in working hours.

[3] Germany, France and the Netherlands; weighted on the basis of GDP.

pensation derived from the collective agreements concluded by the joint industrial councils. They make it possible to identify the various factors influencing wage scales : wage adjustments made by applying indexation mechanisms, increases decided upon under collective agreements and, for manual workers, those resulting from the reduction in working hours.

For analysis purposes, a single index of wages under collective agreements has been constructed by weighting the movement in the indices of manual and non-manual workers. It shows that labour costs in Belgium continued their moderate rise in 1999. Agreed wages increased by 1.9 p.c. in 1998 and 1.7 p.c. in 1999, mainly on account of the smaller effect of agreed adjustments. The latter in fact presented a fairly contrasting pattern during the year under review, rising initially at a very modest rate – around 0.2 p.c. – which speeded up to 0.8 p.c. in the second half of the year, in line with the increase in the number of agreements being implemented. This acceleration was not, however, reflected to a comparable extent in the movement of nominal agreed wages, since the impact of wage indexation diminished during this period.

However, indices of wages under collective agreements are still incomplete indicators of the movement of wage costs per full-time employee in enterprises, since they take no account of such elements as bonus payments, increases agreed at enterprise level, wage drift and employers' social security contributions. These elements are included in the index of hourly labour costs published on a harmonised basis for the first time in April 1999 by Eurostat for the EU Member States. The aim of this index is to meet the greater need for information to be provided quickly, for the authorities and for management and labour, in the context of monetary union. These costs are an important determinant of the trend of prices and hence of future inflation. Furthermore, the trend of wage costs needs to be kept in line with macroeconomic conditions.

TABLE 16 — LABOUR COSTS IN ENTERPRISES[1]

(Percentage changes compared to the previous year)

	1997	1998	1999 e
Labour costs per full-time employee	3.1	2.2	2.2
Increase resulting from :			
Indexations	1.5	1.2	1.1
Wage increases under collective agreements	0.2	0.7	0.5
Actual social contributions paid by employers to public authorities[2]	0.4	−0.3	−0.4
Other[3]	1.0	0.6	1.0
Productivity per full-time employee	3.8	1.9	1.9
Unit labour costs[4]	−0.6	0.3	0.3

Sources : MEL, NAI, NBB.

[1] Public and private enterprises.

[2] Contribution to the increase in labour costs per full-time employee.

[3] This item includes increases in the form of single bonuses, increases granted by enterprises over and above collectively agreed adjustments for the sector, the difference between estimated and actual indexations, the difference between the estimated and actual effect of the collectively agreed wage increases, the impact of social contributions other than those paid to public authorities, the wage drift resulting from measures to activate unemployment benefits or a change in the composition and structure of employment, and the impact of the change in the actual hours worked per full-time employee.

[4] Per unit of value added in enterprises, at constant prices.

Wage policy now plays a vital adjustment role in the event of asymmetrical economic shocks in a monetary union, where, by definition, exchange rates can no longer perform that function.

In 1998 the increase in hourly labour costs is shown to have been identical in Belgium and its three main neighbouring countries, namely 2.1 p.c., despite wider fluctuations during the year. However, the comparison appears to have been less favourable in the first quarter of 1999, when the rise in Belgium was 2.6 p.c., against 2.2 p.c. in the reference countries. However, the rate of increase should have slowed down subsequently, as the policy on reducing employers' social security contributions was intensified and the effect of indexation diminished.

Taking account of the fact that the number of hours worked per full-time employee hardly changed at all in 1999, the rise in labour costs per full-time employee came to 2.2 p.c. as in the previous year. The total increase resulting from indexations was slightly down in 1999, at 1.1 p.c. against 1.2 p.c. in 1998, as this small reduction only partly reflects the trend of the health-index four-month average, in view of the way in which that index is used in the indexation mechanisms of the various sectors. In 1999 the average effect of increases granted under sectoral collective agreements came to 0.5 p.c. That is within the margin allowed by the wage norm agreed upon in December 1998 by management and labour for 1999-2000, after taking account of the indexation expected at the time of calculation and the wage drift, estimated at 0.5 p.c. per annum. If inflation had been lower than expected in 1999, permitting a larger increase under the wage agreement, that possibility would not normally have needed to be used, since the increase in prices was, on average, also lower than expected in the three neighbouring countries. The aforementioned law of 26 July 1996 provides for mechanisms to adjust the movement of wages in cases where it is found that the rise in wages in Belgium was ultimately greater than that actually recorded in the three main neighbouring countries.

The increase in real wages determined under the sectoral agreements therefore remained modest, in line with the trend which has been apparent since 1994, despite increasing signs in 1999 of a labour shortage in certain regions or sectors and a scarcity of certain skills. In principle, the single wage norm introduced by the law of 26 July 1996 prevents wages from adapting freely to market conditions, but enterprises facing a labour shortage might be tempted to deviate from the norm. Indeed, the latest interprofessional agreement does provide for more flexible appraisal of compliance with the wage norm. In particular, it stipulates that the appraisal will simultaneously consider the trend in wages, training effort and employment, and specifies that any unfavourable development in one of these areas can be offset by favourable developments in the other areas.

Since 1994, wage moderation has also been accompanied by a policy of reducing social security contributions, underpinned by the entry into force on 1 April 1999 of the multiannual plan for reductions in employers' social security contributions. That date marked the end of two social security contribution reduction schemes. This concerned, firstly, the "Maribel" reductions, which applied to manual employees of enterprises engaged in economic, commercial or industrial activities, except for those coming under certain specific joint committees (oil, gas and electricity, financial institutions, insurance), and, secondly, the low-pay measure, which applied to workers earning a gross monthly wage of up to 1,538.25 euros (or 62,053 francs). These provisions had been used very extensively, since, in 1998 – according to MEL data – they applied to some 54 p.c. of workers in enterprises, on average : about two fifths were covered by one of these two measures, while one fifth qualified for both simultaneously. These schemes have been replaced by a "structural reductions in contributions" system which comprises a flat-rate reduction granted for each employee plus a supplementary reduction granted for employees receiving wages not exceeding the threshold of

TABLE 17 – REDUCTIONS IN EMPLOYERS' SOCIAL SECURITY CONTRIBUTIONS [1]

(Millions of euro)

	1998	1999
Structural reductions in contributions	–	734
Maribel	649	327
Low pay measure	379	171
Social Maribel	50	216
Other	575	550
Total	1,653	1,998
p.m. Percentages of total wages and salaries	*1.9*	*2.2*

Source : Chamber of Representatives.

[1] On a cash basis, which lags about three months behind the transactions approach of the national accounts.

the old low-pay measure. This new system is wider in scope than the previous measures, since it concerns all workers except those in the socio-cultural, health and welfare sectors, for whom a special scheme – called “Social Maribel” – has been in force since 1997. This scheme, which links reductions in contributions to job creation, was also made more attractive in the year under review, the reduction in contributions being stepped up from 161.13 to 242.71 euro per quarter from 1 July 1999. As a result of the new reductions in social security contributions for employers, the total reductions granted increased on a cash basis from 1.7 billion euro in 1998 to almost 2 billion euro in the year under review, representing 2.2 p.c. of total wages and salaries. In 1999 this factor reduced the rise in labour costs per full-time employee by 0.4 p.c.

Finally, the movement in labour costs is also influenced by residual factors which consist chiefly of the wage drift, caused mainly by changes in the structure of employment, and the adjustment to working hours resulting from variations in temporary lay-offs. Together, these factors increased labour costs by 1 p.c., against 0.6 p.c. in 1998.

Taking account of the rise in productivity, unit labour costs showed only a small increase, of 0.3 p.c. During the past six years they have been more or less stable, overall primarily because of wage moderation. This has therefore done much to help control prices in recent years.

In 1999 the rise in selling prices, slightly greater than that in unit labour costs, contributed towards the increase in the gross operating sur-

TABLE 18 – DETERMINANTS OF THE GROSS OPERATING SURPLUS OF COMPANIES [1]

(Percentage changes compared to the previous year)

	1996	1997	1998	1999 e
Gross operating margin				
Unit selling price	1.9	3.0	0.1	0.6
On the domestic market	1.5	1.4	0.4	1.6
On the export market	2.4	4.6	−0.3	−0.5
Costs per unit sold	2.2	3.0	…	0.5
Imported goods and services [2]	2.9	5.2	−1.6	0.2
Costs of internal origin per unit produced [3]	1.4	0.3	1.3	0.8
Indirect taxes net of subsidies	5.6	3.3	1.6	2.0
Labour costs	0.6	−0.6	0.3	0.3
Gross operating surplus of self-employed persons	1.8	−2.9	−11.8	−2.3
Gross operating surplus of companies per unit sold	0.2	2.8	0.7	1.3
Volume				
Final sales at constant prices	0.9	5.0	4.5	2.4
On the domestic market	0.6	3.3	4.8	2.0
On the export market	1.3	6.7	4.2	2.9
Gross operating surplus of companies	1.2	8.0	5.3	3.8

Sources: NAI, NBB.
[1] Private and public enterprises.
[2] Expressed in national currency.
[3] Per unit of value added at constant prices in enterprises.

plus of companies per unit sold. On the other hand, the deterioration in the terms of trade, i.e. the ratio of export to import prices, had the opposite effect, as the rise in import prices resulting from higher prices for petroleum products and the depreciation of the euro was not yet entirely reflected in export prices.

The 1.3 p.c. overall increase in the gross operating margin was accompanied by a 2.4 p.c. growth in the volume of sales, so that the gross operating surplus of companies increased further in 1999. However, at 3.8 p.c., its rate of increase was lower than that recorded in 1997 and 1998.

5.2 PRICES

Inflation remained low in Belgium during the year under review. Measured by the harmonised index of consumer prices, it came to 1.1 p.c., or little more than the annual average of 0.9 p.c. recorded in 1998. Price movements in Belgium in 1999 therefore did in fact remain, for the euro area as a whole, within the limits which the ECB considers compatible with price stability, namely an annual increase in the price index of less than 2 p.c.

After accelerating until March in the year under review, the rate of increase in the consumer

TABLE 19 — HARMONISED INDEX OF CONSUMER PRICES

(Percentage changes compared to the corresponding period in the previous year)

	Total	Non-processed food products [1]	Energy products	Underlying inflation [2]	Processed food products	Non-energy industrial products	Services	of which: Rents	p.m. Health index [3]
Weight in p.c.	100	10.2	10.7	79.1	14.1	33.8	31.2	6.0	
1996	1.8	0.7	5.8	1.4	0.8	0.6	2.5	2.4	1.7
1997	1.5	2.7	3.1	1.1	2.3	0.1	1.7	1.4	1.3
1998	0.9	2.2	−3.6	1.4	1.4	0.7	2.1	1.6	1.3
1999	1.1	...	2.1	1.1	0.6	0.8	1.7	1.5	0.9
1999 January	1.0	3.1	−4.8	1.4	0.4	1.2	2.2	1.5	1.2
February	1.0	3.4	−4.8	1.4	0.4	1.2	2.1	1.4	1.2
March	1.3	3.1	−2.8	1.6	0.7	1.2	2.3	1.5	1.3
April	1.1	1.0	−0.6	1.4	0.7	1.1	1.9	1.5	1.1
May	0.8	0.1	−0.5	1.1	0.8	0.7	1.6	1.5	0.7
June	0.7	−0.8	−0.3	1.1	0.9	0.8	1.5	1.5	0.7
July	0.7	−3.0	2.1	0.9	0.6	0.8	1.2	1.5	0.4
August	0.9	−2.2	4.5	0.9	0.6	0.7	1.2	1.5	0.6
September	1.3	−1.3	5.9	0.9	0.6	0.6	1.4	1.5	0.8
October	1.4	0.2	6.1	0.9	0.6	0.6	1.2	1.5	0.9
November	1.6	−1.1	7.5	1.1	0.6	0.6	1.8	1.4	1.1
December	2.1	−2.1	12.3	1.3	0.9	0.6	2.1	1.5	1.3

Sources: EC, MEA, NBB.

[1] Fruit, vegetables, meat and fish.

[2] Inflation excluding the effect of variations in the prices of non-processed food products and energy products.

[3] National consumer price index, excluding the effect of variations in the prices of products considered harmful to health (namely tobacco, alcoholic beverages, petrol and diesel), the energy levy introduced by the law of 22 July 1993, and the excise-duty-compensating tax on diesel vehicles, which came into force in January 1996.

price index slowed down, reaching a low of 0.7 p.c. in June and July. Thereafter, it steadily edged back up.

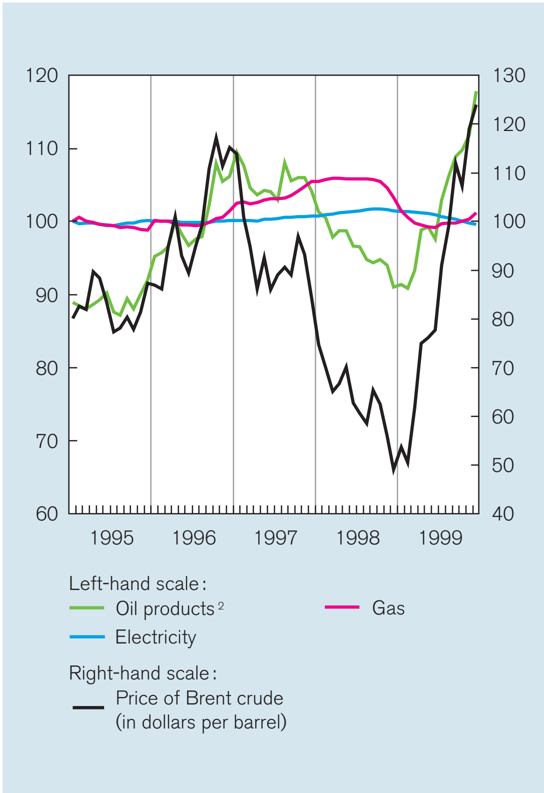
The higher inflation from November 1998 to March 1999 was fuelled by the steep increases in the prices of non-processed food products, particularly vegetables and potatoes, caused by the bad weather during the 1998 harvests. These increases were interrupted in April, while from June onwards prices actually declined on account of generally favourable supply conditions. The dioxin crisis did not, after all, have any significant impact on the consumer price index, though that does not rule out an effect at an earlier stage in the marketing circuit, for example in farmers' producer prices. It is difficult to isolate the effect of the crisis from that of other factors determining these prices, but in June and July a marked fall in producer prices was in fact observed for pigs, poultry and eggs.

For much of the year under review, energy product prices moved in the opposite direction from prices of non-processed food products. The marked reductions noted at the beginning of the year still represented a continuation of the 1998 movement. Prices on the international crude oil market had slumped in 1998 following the contraction of demand caused by the crisis in the emerging or transition countries. The agreement providing for restrictions on output, concluded by the OPEC countries in March of the year under review, reversed this trend, especially as compliance with it was good. The upward trend in oil prices was also bolstered by the recovery in demand generated by the expansion of the world economy, so that prices for Brent crude more than doubled, from just over 10 dollars a barrel in February 1999 to around 26 dollars on average in December of the year under review.

An increase in the crude oil prices quoted on the international market prompts an almost immediate rise in the prices of petroleum products, namely petrol, diesel and fuel oil, which have an overall weighting of 5.1 p.c. in the HICP. Fluctuations in the consumer prices of these products are governed by the programme contract concluded between the State and distributors. The programme contract, which sets maximum selling prices for the products covered, guarantees that changes in oil prices will be reflected in consumer prices without any automatic adjustment to distributors' margins. The prices calculated under this contract in fact take account of the conditions prevailing on the international markets, and of the production costs of enterprises in the Belgian oil sector. In consequence, the movement in consumer prices is not proportional to the change in quoted prices for crude oil. First, it is necessary to take account of the movement in the dollar exchange rate, which may amplify or attenuate the variation in prices

CHART 32 — CONSUMER PRICES OF ENERGY PRODUCTS IN BELGIUM [1] AND CRUDE OIL PRICES

(Indices 1996 = 100)



Sources: EC, NBB.

[1] Measured by the HICP.

[2] Fuel oil, petrol, diesel, LPG and lubricants.

in euros. During the year under review, the euro depreciated on average by about 5 p.c. against the dollar. Next, the effect of a change in the crude oil price is moderated by excise duties, which are flat-rate taxes representing around half the price paid by consumers. Furthermore, this price rise similarly has no direct influence on the value added at the different processing and distribution stages. Altogether, between the first two months of the year and December, consumer prices for petroleum products increased by only about 29 p.c. in Belgium, whereas, even expressed in dollars, the price per barrel for Brent crude more than doubled during that period.

However, an increase in oil prices does have indirect effects on consumer prices, and these become apparent in different phases. It influences, albeit after a time-lag, the prices of the other energy products included in the HICP, notably electricity and gas, with a combined weighting of 5.5 p.c. This time-lag amounts to about three quarters on average for the price of natural gas. It takes even longer before the influence of oil prices affects electricity charges, and the impact is smaller : these charges are in fact calculated taking account of two parameters : the price of fuel and other production costs, including wages. In 1999, oil had only a 1 p.c. share in electricity production, the greater part – 58 p.c. – being produced from nuclear energy, with gas and coal accounting for 27 and 12 p.c. respectively. Thus the fall in oil prices in 1998 did not cause electricity prices to drop until May 1999, and the reduction was only small. From October onwards, these prices were also influenced by the reduction in charges decided upon by the Supervisory Committee for Electricity and Gas, the effect of which will be felt until September 2000. In November 1999 the Supervisory Committee also announced a further rate reduction taking effect in July 2000. This policy on charges is intended to eliminate the current price differentials vis-à-vis some European partners in favour of households and of industry in general.

It also needs to be seen in the general context of the liberalisation of markets in goods and services in the EU. This process was extended to electricity by the European directive dated 19 December 1996 on common rules for the internal market in electricity, transposed into Belgian law by the law of 29 April 1999 on the organisation of the electricity market. Belgium has therefore opened up the first segment of its market to competition since April 1999, without making use of the one-year exemption which it had secured. “Eligible” customers are large enterprises, major electricity consumers (using over 100 GwH per annum), who account for around 33 p.c. of total electricity consumption. There is provision for a progressive widening of the eligibility criteria, and from 1 January 2007 distributors will also have a free choice of supplier for at least 25 p.c. of their needs, with total freedom of choice by 2011 at the latest.

The higher oil prices also influence final consumption prices via their impact on the cost of intermediate inputs at the various stages in the production process. That influence may also be accentuated at a later stage by the indexation of wages. However, the risk that a rise in oil prices might set off a price-wage spiral, as happened in the 1970s, has been considerably moderated since 1994 by the use of the health index as a reference for wage indexation, as the health index excludes petrol and diesel. The deterioration in the terms of trade which a steep rise in oil prices inflicts on the economy is therefore, thanks to the health index, no longer borne solely by enterprises, at least initially, but also by individuals.

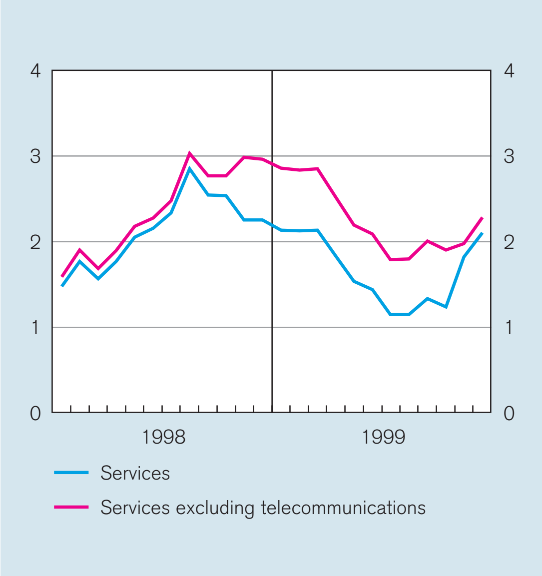
The impact of the rise in oil prices on consumer prices for non-energy industrial products and the prices of services is felt after a certain time-lag. According to the Bank’s quarterly econometric model, it takes at least thirteen quarters before all the effects of an oil price shock are reflected in prices. The assimilation of shocks also depends on macroeconomic conditions. For the consumer, the impact of cost increases, such as oil price rises, depends on many factors, such as the extent to which such increases are considered to be permanent, the economic situation and competition on the market. A temporary shock in oil price quotations is absorbed more readily in gross operating margins than a shock which is regarded as permanent. An upswing in the economy exerts effects in two ways : it leads to higher productivity, which limits the rise in unit output costs, and it is accompanied by a general strengthening of demand, which makes it easier for cost increases to be passed on to consumers. An increase in competition has a moderating effect on prices.

The recent oil price rises have not yet had any visible impact on underlying inflation, which corresponds to overall inflation excluding the effect of changes in the prices of non-processed food products and energy. On the contrary, underlying inflation fell during the first seven months of 1999, and then stabilised before admittedly creeping back up in November and December, but that was because of a quickening of the rise in the prices of services. The increase in the prices of non-energy industrial products slowed down for much of the year, as the 1998 fall in oil prices was still keeping costs down in the year under review, illustrating the time-lags mentioned earlier.

The trend in prices of services, especially in telecommunications, demonstrates the growing pressure of competition unleashed by the move towards deregulation and liberalisation. The marked fall in telephone prices in November 1998 depressed service prices by 0.7 percentage point during the first ten months of the year under review. This kept the rise in service prices down to a very low level in historical terms. Furthermore, the impact of the said reduction on consumer prices is doubtless underestimated, given that the keener competition has until now been evident in specific market segments such as mobile phones or business telecommunications. For one thing, mobile phones are not included in the current price index. Also, the indirect effect of falling telecommunications prices on inflation via the costs of enterprises is hard to quantify. From November 1999 onwards, service prices and hence underlying inflation increased at a faster pace, since the reductions in charges granted a year earlier in the telecommunications sector ceased to influence inflation calculated on an annual basis.

CHART 33 — INFLATION IN SERVICES [1]

(Percentage changes compared to the corresponding month of the previous year)



Source : EC.

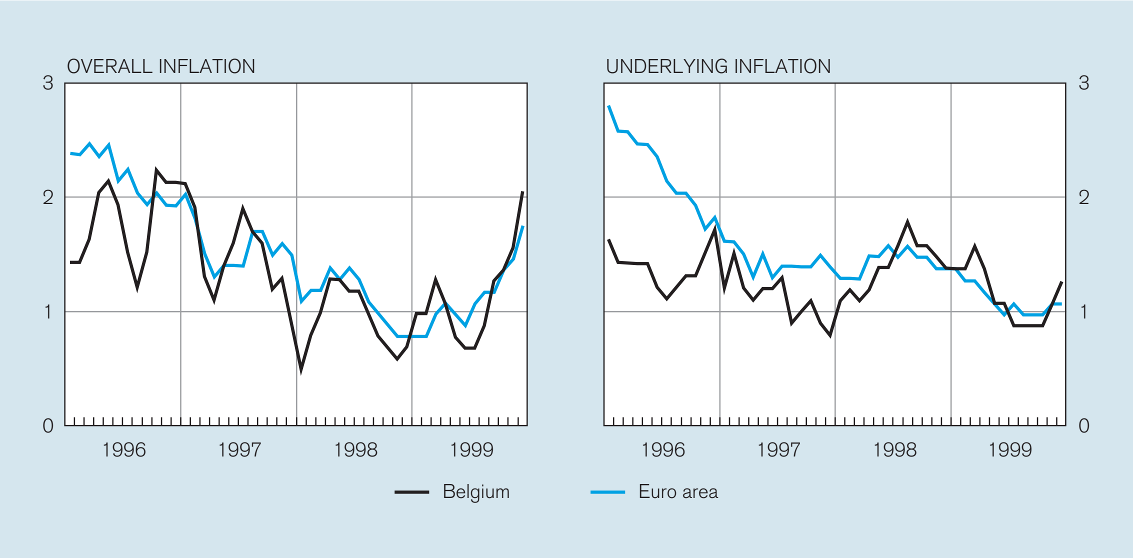
[1] Measured by the HICP.

Rents form an important component of services. During the year under review, they rose at a steady 1.5 p.c. Their real increase was very small, as rents are index-linked on the basis of the health index. In addition, there is a surplus supply of rented housing. In recent years, low mortgage interest rates combined with the improvement in the general economic situation have doubtless encouraged individuals to prefer to cover the cost of a loan rather than rent in their expenditure on housing, and hence to opt in favour of home purchases.

The rise in the prices of processed food products, the other component of underlying infla-

CHART 34 — OVERALL AND UNDERLYING INFLATION [1]

(Percentage changes compared to the corresponding month of the previous year)



Source : EC.

[1] Measured by the HICP. Underlying inflation corresponds to overall inflation excluding the effect of changes in the prices of non-processed food products and energy products.

tion, remained moderate, since the price of coffee – the main product behind the volatility of prices in this category – continued to fall at a more or less constant rate. This price movement speeded up slightly in December owing to the rise in the price of bread, following the decision of the Minister for Economic Affairs to approve the application for an increase in the maximum price of this product, submitted by the bakery sector in 1998 to take account of the rising labour costs.

As in 1998, the overall and underlying inflation rates recorded in Belgium during the year under review were little different from the figures for the euro area as a whole. In the case of overall inflation, the rises and falls were slightly more pronounced in Belgium than on average in the euro area. These more marked fluctuations occurred mainly in non-processed food products and are attributable to the fact that weather conditions and other incidental factors which have a temporary impact on supply, such as livestock diseases, have a major effect on prices for this category of products in a particular country, especially if the country is small, but are reflected in the average price level of the euro area only to the extent of the weighting of that country. Moreover, in that average price the movement in prices in one particular country may be offset by an opposite movement in another country.

6. PUBLIC FINANCES

6.1 REVENUE, EXPENDITURE AND FINANCING REQUIREMENT

European monetary union created a new environment for budgetary policy in the euro area, although this, unlike monetary policy, remains a matter for the national authorities. The EU Member States are henceforth required to comply with the provisions of the Stability and Growth Pact, which specifies the obligations imposed by the Treaty on European Union. In order to prevent, in particular, the development of the public finances from impairing the effectiveness of monetary policy, they undertook by this pact to steer their budgets, in the medium term, towards equilibrium, or even a surplus. The purpose of this objective is to ensure that the incidence of normal fluctuations in economic activity on public revenue and expenditure can be absorbed without this leading to an excessive deficit of more than 3 p.c. of GDP.

The medium-term orientation thus given to budgetary policy is moreover justified for other reasons. It contributes to a faster reduction in the level of indebtedness in the countries where this is still above the reference value of 60 p.c. of GDP, as well as to the creation of scope for coping in the longer term with, among other things, the consequences of the ageing of the population.

In order to give substance to the commitments defined in the Stability and Growth Pact, the Member States are required to draw up each year a stability programme, or a convergence programme in the case of the countries which have not yet adopted the euro. They must describe in this programme the broad lines of their budgetary policy for the next three or four years and indicate the course which they will follow to make their budgetary situation comply with the provisions of the pact. The first series of stability or convergence programmes was presented at the end of 1998 and the beginning of 1999. It constitutes the main reference according to which the budgetary policy pursued by the Member States in 1999 must be assessed.

Belgium's first stability programme, submitted in December 1998, was centred on the maintenance of the general government primary surplus at the expected level for the year 1998, that is, about 6 p.c. of GDP. This strategy, which had already been the subject of a formal undertaking on the part of the Belgian authorities at the beginning of 1998, was to make it possible, thanks to the downward trend of interest charges, virtually to eliminate the budget deficit by 2002 and to reduce the debt ratio by nearly 11 percentage points between 1998 and 2002. In order to make this strategy possible, specific budgetary norms were defined for the various sub-sectors of general government. On the one hand, the primary surplus of Entity I, that is, the federal government and the social security system, was to remain unchanged at the level of 5.3 p.c. of GDP envisaged for 1999. On the other hand, the budget of Entity II, i.e. the regions, communities and local authorities, was to remain in balance. The stability programme, based on a trend economic growth of around 2.3 p.c. per annum for the period from 1999 to 2002, also imposed a strict rule for the allocation of the effects on the budget of a more favourable economic situation, by setting aside the greater part of these for faster reduction of the public deficit and the public debt. The allocation for other purposes was limited, under the best assumption, to at most 0.14 p.c. of GDP per year.

However, the results achieved by the general government account in 1998 were much better than had been forecast : its deficit, which was still estimated at 1.6 p.c. of GDP in the stability programme, was kept down, according to the most recent national accounts, to only 1 p.c. of GDP, while the primary surplus amounted to 6.6 p.c. and not 6 p.c. These more favourable balances are mainly attributable to higher revenues from tax and social contributions, as well as to better results for the communities and regions. These factors were offset to a slight extent by the changeover to the new methodology of ESA 95 for the national accounts. This led to several important changes for the general government account, the final net incidence of which in 1998 proved only slightly negative. With a deficit of 1 p.c. of GDP, the target set by the stability programme for 2000 was already reached in 1998.

In accordance with the European regulations, the Belgian authorities submitted an updated stability programme at the end of the year under review. This new programme applies to the years 2000 to 2003. In addition to the confirmation of the norm for the medium-term stabilisation of the primary surplus for general government as a whole at about 6 p.c. of GDP, a second norm in terms of financing balance is added. Net financing must return to equilibrium in 2002, via intermediate deficit targets of 1 and 0.5 p.c. of GDP respectively for the years 2000 and 2001. The government undertook, however, to reduce the public deficit to a greater extent in 2000 in the event of economic growth in excess of 2.5 p.c., making provision for this purpose for a priority allocation of the resultant margin for manoeuvre. For the year 2003, a slight structural financing surplus must be generated, with a view in particular to counteracting the incidence on the public debt of the transactions which are not taken into account in the net financing balance and thus permitting a stabilisation of the debt in nominal terms.

Such a strategy is in accordance with the recommendations of the Stability and Growth Pact. The dual norm implies that, if the movement of interest rates is in accordance with expectations, the objective of budgetary balance in 2002 will necessitate a primary surplus of about 6.4 p.c. of GDP.

As in the stability programme of December 1998, norms were laid down for the various public entities, to enable each of them to achieve a balanced net financing position in 2002. With regard to Entity I, this calls for a large increase in the primary surplus by then. For the communities and regions as a whole, budgetary balance must be achieved over the entire period, in accordance with the terms of the co-operation agreement of 24 November 1999 between the governments of the federal and federated entities. Lastly, the local authorities must generate a surplus of 0.2 p.c. of GDP for the years 2000 and 2001 and keep their budgets in balance from 2002 onwards.

Revenue

Fiscal and parafiscal revenue amounted in 1999 to 44.9 p.c. of GDP, representing a decline of 0.5 percentage point compared to the previous year.

More than half of this revenue is levied on earned incomes, in the form of taxes or social contributions; the other two categories of levies on incomes – namely taxes on company profits and those on incomes from movable and immovable property – each represent less than one tenth of the fiscal and parafiscal pressure, the remaining quarter being levied on transactions in goods and services.

The fluctuations of the share in GDP of each of these categories can be broken down between the movement of the tax base compared to GDP on the one hand and that of the implicit rate – revenue expressed as a percentage of the tax base – on the other.

From 1996 to 1998, levies weighing chiefly on earned incomes remained practically stable as a percentage of GDP, as a result of opposite

TABLE 20 — REVENUE OF GENERAL GOVERNMENT

(Percentages of GDP)

	1995	1996	1997	1998	1999 e
Levies weighing chiefly on earned incomes	26.4	26.2	26.4	26.3	26.0
Personal income tax [1]	12.5	12.4	12.5	12.6	12.3
Social security contributions [2]	13.9	13.9	13.9	13.7	13.7
Taxes on company profits [3]	2.6	2.8	3.0	3.5	3.2
Levies on other incomes and on assets	3.4	3.4	3.5	3.5	3.3
Of which :					
Levies on income from movable property [4]	1.2	1.0	1.0	0.9	0.8
Levies on income from immovable property [5]	1.8	2.0	2.0	2.1	2.0
Death duties	0.3	0.4	0.3	0.4	0.4
Taxes on goods and services	11.8	12.2	12.3	12.1	12.4
Of which :					
VAT	6.8	7.0	7.0	6.9	7.2
Excise duties	2.4	2.5	2.4	2.4	2.4
Other levies on vehicles [6]	0.6	0.7	0.7	0.7	0.7
Fiscal and parafiscal revenue	44.1	44.6	45.1	45.4	44.9
Federal government	*17.0*	*17.0*	*17.0*	*17.4*	*16.9*
Social security	*14.6*	*14.8*	*15.1*	*14.9*	*15.0*
Communities and regions	*10.3*	*10.5*	*10.7*	*10.8*	*11.0*
Local authorities	*2.2*	*2.3*	*2.3*	*2.2*	*2.1*
Non-fiscal and non-parafiscal revenue	1.3	1.4	1.2	1.1	1.4
Total revenue	45.4	46.0	46.3	46.4	46.3

Sources : NAI, NBB.

1 Withholding tax on earned income, advance payments, assessments and proceeds of additional centimes on personal income tax.

2 Total social contributions, including the special social security contribution and the contributions of persons not in work.

3 Advance payments, assessments and withholding tax on interest income.

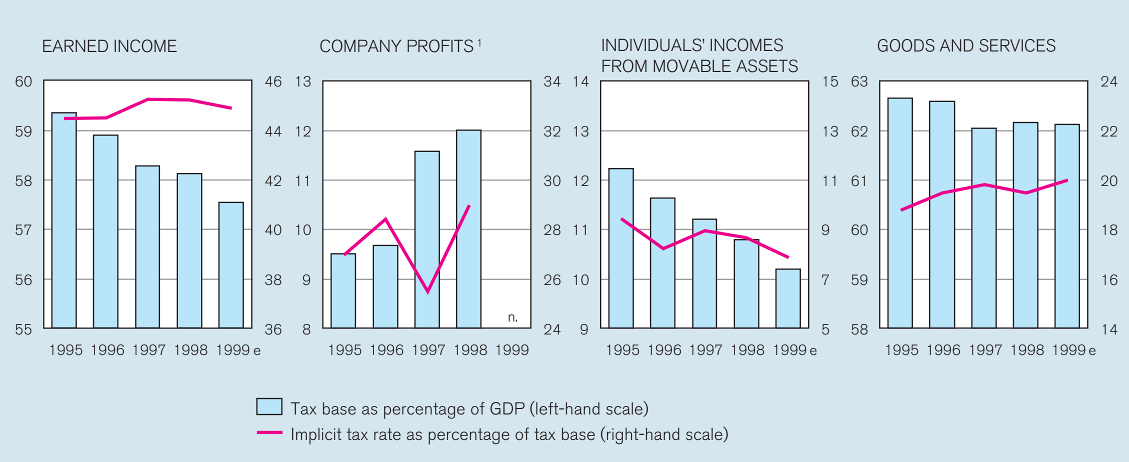
4 Withholding tax on income from movable property of individuals, as well as the taxes on stock exchange transactions, UCIs, listed and bearer securities and long-term savings.

5 Withholding tax on income from immovable property (including the proceeds of additional centimes), registration fees on real estate transactions and mortgage fees.

6 Registration tax, road tax, excise-duty-compensating taxes and Euro tax disc.

movements in the tax base and the implicit rate. The share of earned incomes in GDP showed a downward trend, while on the contrary the implicit rate of taxation on these incomes increased slightly : the incidence of the progressive nature of the scales of personal income tax, heightened by their partial non-indexation, and that of the extension of the special social security contribution, were in fact only partly offset by reductions in employers' contributions. During the year under review, the fiscal and parafiscal pressure on earned incomes declined slightly, as the share of these incomes in GDP stabilised, while at the same time the implicit rate decreased somewhat. This slight reverse movement is due to further reductions in employers' contributions, while the complete reindexation of the tax scales has ended the automatic increase in the tax burden caused by inflation. Although the second of these measures relates to income for the whole of the year 1999, it was applied to the scale of the withholding tax on earned income only with effect from 1 April 1999. The further reductions in the contributions payable by employers were decided upon in implementation of the multiannual programme of reduction of charges on employers announced in the Belgian action plan for employment of April 1998, the

CHART 35 — MAIN DETERMINANTS OF FISCAL AND PARAFISCAL REVENUE



Sources : NAI, NBB.

[1] Pre-tax profits (including capital gains) of non-financial companies and credit institutions with a positive result.

first phase of which became applicable during the year under review. They came into force in April in the market sector, and in July in the non-market sector, at a total budget cost estimated in 1999 at nearly 350 million euro.

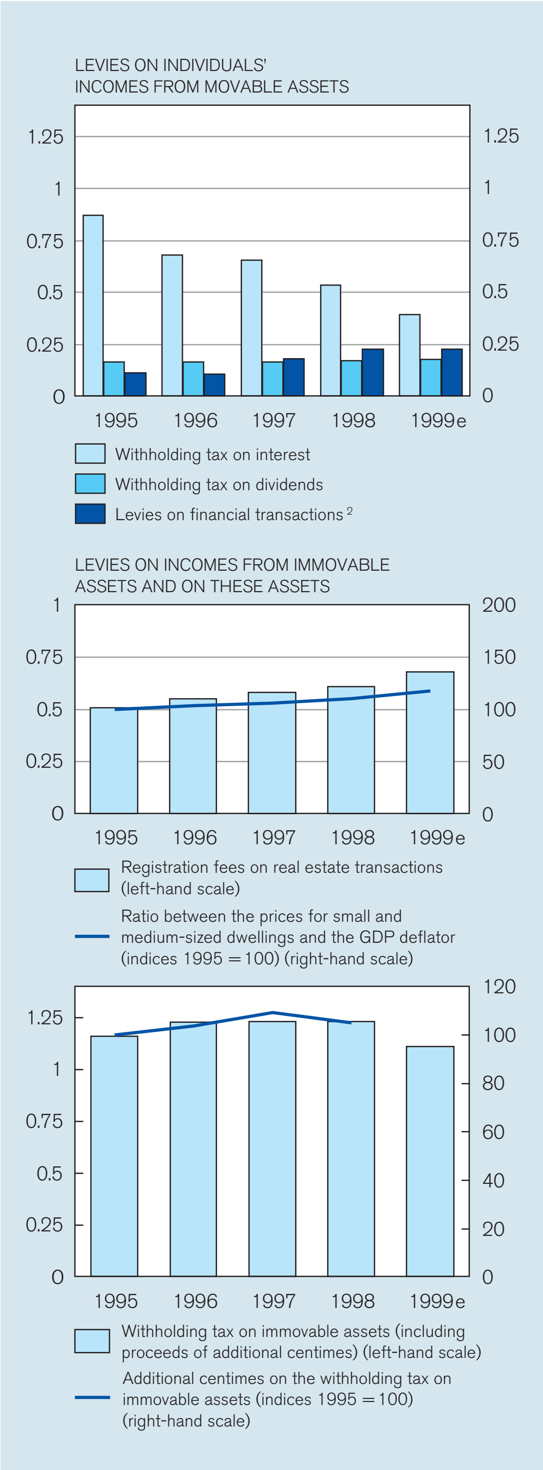
Tax revenues from companies, for their part, increased very markedly until 1998. This rise is mainly due to that in the tax base, which was swollen by substantial capital gains in 1997 and 1998. Despite a rather variable profile, the implicit tax rate also showed a slight upward trend between 1995 and 1998, in the context of a more restrictive policy on fiscal expenditure. In 1999, however, the share in GDP of revenue from companies declined, for the first time in several years. In the absence of measures changing the tax rate, this decrease might be attributable to the fall in taxable profits in relation to GDP.

The share of levies on other incomes and on assets underwent little change from 1996 to 1999. The weight of taxes levied on incomes from movable property decreased, while that of levies on incomes from movable property and on immovable assets increased slightly. Death duties, which affect both movable and immovable assets, also increased somewhat, whereas the nominal rates applicable to the passing-on of family companies were reduced in the three regions, while the general structure of the rates was furthermore changed in the Flemish region.

The decline, since 1995, in levies on individuals' incomes from movable assets is attributable both to the movement of the tax base and to that in the implicit tax rate. As a result of the decline in interest rates, the share of individuals' incomes from movable assets in GDP has in fact been steadily eroded, from over 12 p.c. of GDP in 1995 to about 10 p.c. in 1999. Despite the rise in the nominal rate of the withholding tax on interest incomes in 1996, the implicit tax rate showed a downward trend, owing to the portfolio reallocations in favour of lightly taxed or untaxed financial products, such as the securities issued by UCIs or savings deposits. The fall, as percentages of GDP, in revenue from taxes on incomes from movable assets took place entirely in the withholding tax on interest incomes, since the proceeds of the withholding tax on dividends was stable and the various taxes connected with financial transactions practically doubled, so that they now represent a quarter of this revenue category.

CHART 36 – LEVIES ON INCOMES FROM MOVABLE AND IMMOVABLE ASSETS AND ON THESE ASSETS [1]

(Percentages of GDP, unless otherwise stated)



Sources : Belgian Municipal Credit Institution, Fortis Bank, NBB.

[1] Not including death duties.

[2] Taxes on stock exchange transactions, UCIs, listed and bearer securities and long-term savings.

On the other hand, the proceeds of the taxes on other income and on immovable assets kept closer to the movement of GDP. Registration fees on real estate transactions increased, owing to the rise in the relative prices of real estate and the greater number of transactions. Revenues from the withholding tax on immovable assets, on the other hand, were relatively stable from 1996 to 1998, because the growth in the additional centimes levied by municipalities was slight. It should also be noted that the indexation of assessed property incomes from 1991 onwards helped to prevent a decline in the share of these revenues in GDP. The fairly large decrease in these in 1999 was due to collection delays in the Flemish region, since that region has collected the additional centimes itself from the 1999 fiscal year onwards.

After a substantial rise in 1996 due to the increase of half a point in the standard VAT rate, to the raising of excise duties and to the introduction of an excise-duty-compensating tax on diesel-engined vehicles, taxes on transactions in goods and services, expressed as percentages of GDP, remained practically unchanged until 1998. In 1999 their share in GDP increased again, entirely owing to VAT revenues. In the absence of any significant rise in the VAT tax base, the movement of these revenues is attributable to a rise in the implicit rate due, on the one hand, to the abolition, in the middle of the previous year, of the measures reducing VAT on the building of social or small dwellings, and, on the other hand, to a more favourable structure of private consumption. Sales of products subject to the standard rate of 21 p.c., such as cars, mobile telephones and data-processing equipment, in fact rose faster than those of other goods and services on which the average rate was lower. Excise duties, however, remained unchanged compared to the previous year, during which they had been swollen by exceptionally large payments on tobacco sales in Luxembourg.

The movement of fiscal and parafiscal revenue differed greatly from sub-sector to sub-sector in

1999, the federal government's revenues having contracted by 0.5 percentage point of GDP, whereas those of the communities and regions and those of the social security system increased by 0.2 and 0.1 point respectively.

This divergence is mainly due to the institutional mechanisms whereby the revenues are distributed between the different levels of power. Thus, the already structurally large increase in taxes allocated to the communities and regions was accelerated in 1999 by the assignment of additional resources derived from a settlement of amounts payable for the past. The revenues of the communities and regions therefore increased by 4.3 p.c. in real terms. Furthermore, the amount transferred to the social security system under the alternative financing scheme was also increased, as the counterpart to the additional reductions in employers' contributions. After these allocations, the net revenues accruing to the federal government decreased by 1.2 p.c. in real terms.

A similar divergence is to be seen in the longer-term movement of revenues by sub-sectors, those of the communities and regions having increased annually from 1990 to 1999 by 3.9 p.c. in real terms, that is, a much higher growth rate than that of GDP and that of the revenues of the other components of general government, especially the federal government, whose revenues grew on average by only 1.1 p.c. per annum. The sharp rise in the resources of the federated entities is chiefly due to the mechanisms established for the assignment of personal income tax and VAT revenues – which constitute more than 80 p.c. of the total revenues of these entities – during the transitional period of application of the Communities and Regions Financing Act of 16 January 1989. For personal income tax, various relatively complex adjustment mechanisms resulted in a very strong real rate of increase, of over 7 p.c. per year. The chief mechanisms involved were the gradual freeing of the resources necessary for financing the exercise of the responsibilities transferred to the communities and regions and the gradual alignment of the distribution of the resources assigned to them with the relative contribution of their respective populations to the proceeds of the personal income tax. The volume of VAT revenues allocated for financing education, for its part, moved mainly in line with the – tiny – decline in the population of under-18s in the community where this decline was slowest. But, account being taken of an ad hoc upward correction in 1990 and of the paying up of amounts owed for the past in 1999, it nevertheless showed a very small average increase of 0.4 p.c. per annum from 1990 to 1999. The substantial rise in the revenues of the communities and regions warranted an upward trend in their primary expenditure, of 2.5 p.c., whereas for the other components of general government that trend amounted at the same time to about 1.5 p.c.

In the final phase of the Financing Act starting in the year 2000, the increase in the revenue of

TABLE 21 — FINANCING RESOURCES OF THE COMMUNITIES AND REGIONS

(Annual percentage changes at constant prices) [1]

	Transition period 1990-1999	Final phase 2000-2010	p.m. Structure in 1998 (percentages of total revenue)
Revenue from personal income tax and VAT allocated under the Financing Act [2]	3.9	1.2	82
To finance education	0.4	–0.3	34
For other responsibilities	7.2	2.1	48
Other revenue	4.0	n.	18
Total revenue of the communities and regions	3.9	n.	100
p.m. GDP	*2.0*	*2.2*	

Sources: Chamber of Representatives, NAI, NBB.

[1] Deflated by the national index of consumer prices.

[2] For the year 2000 the data are those of the federal government's initial budget; for the following years they are estimated on the basis of the development of the population (according to the NAI projections published in 1996), of economic growth of 2.2 p.c. and on the assumption that the interregional differences in the per capita proceeds of personal income tax will remain unchanged.

the communities and regions will be appreciably smaller. For the transferred part of the personal income tax, the mechanisms which brought about a very marked increase will disappear and the movement – apart from the amount of the solidarity intervention – will simply be equal to that in GNI (GNP in the former ESA 79 definition). For VAT revenue, on the other hand, the method of calculation is unchanged, i.e. its total amount will continue to be adapted to the number of young people. Assuming real growth of 2.2 p.c. and taking account of the expected decline in the population of persons aged under 18, the real rise in the total amount of revenue transferred can be estimated at about 1.2 p.c. per annum, which, unlike in the past, is below economic growth.

Non-fiscal and non-parafiscal revenue reached 1.4 p.c. of GDP in the year under review against 1.1 p.c. in 1998. This sharp rise is due particularly to the provisional recording, according to the national accounts methodology, of the amount to be refunded by companies for Maribel aids declared to be not in accordance with European competition law.

Primary expenditure

Expenditure excluding interest charges increased by 0.2 point of GDP during the year under review, thus amounting to 40 p.c.

Deflated by the national index of consumer prices, it increased by 2.7 p.c. in 1999, i.e. at a

TABLE 22 — PRIMARY EXPENDITURE OF GENERAL GOVERNMENT [1]

	Percentages of GDP			Percentage changes at constant prices [2]			
	1997	1998	1999 e	1996	1997	1998	1999 e
Compensation	8.7	8.6	8.6	–0.8	1.8	2.2	1.5
Net current purchases of goods and services	1.6	1.6	1.7	2.2	1.8	5.7	4.6
Current transfers to individuals	23.6	23.3	23.3	1.5	0.7	2.0	2.1
of which: Private sector and general government pensions [3]	8.9	8.8	8.7	0.9	2.9	2.2	1.6
Unemployment benefits, early retirement pensions and career interruptions	2.7	2.6	2.5	2.0	–1.2	–1.0	–0.8
Health care	5.5	5.5	5.7	5.2	–2.1	3.4	5.0
Subsidies to enterprises	1.7	1.6	1.7	4.9	–9.7	–0.9	4.5
Current transfers to the rest of the world	1.7	1.7	1.7	6.7	8.0	3.9	3.1
Capital expenditure	3.1	2.9	3.1	–2.4	19.3	–3.5	9.3
p.m. excluding non-recurrent capital expenditure [4]	*2.8*	*2.7*	*2.9*	*1.8*	*0.9*	*–1.2*	*9.4*
Total primary expenditure	40.4	39.8	40.0	1.1	2.0	1.8	2.7
p.m. excluding non-recurrent capital expenditure [4]	*40.2*	*39.6*	*39.8*	*1.4*	*0.8*	*2.0*	*2.7*
Federal government	*13.1*	*12.7*	*12.8*	*–0.1*	*2.7*	*0.5*	*2.8*
Social security	*18.5*	*18.3*	*18.2*	*2.1*	*–0.4*	*2.3*	*2.1*
Communities and regions	*11.4*	*11.3*	*11.2*	*–0.7*	*3.4*	*2.4*	*1.6*
Local authorities	*5.2*	*5.2*	*5.3*	*0.8*	*1.8*	*3.2*	*4.9*
GDP				1.0	3.5	2.7	2.3

Sources: NAI, NBB.

1 Expenditure excluding interest charges. For general government as a whole, the data are consolidated, that is, they exclude transfers between sub-sectors.

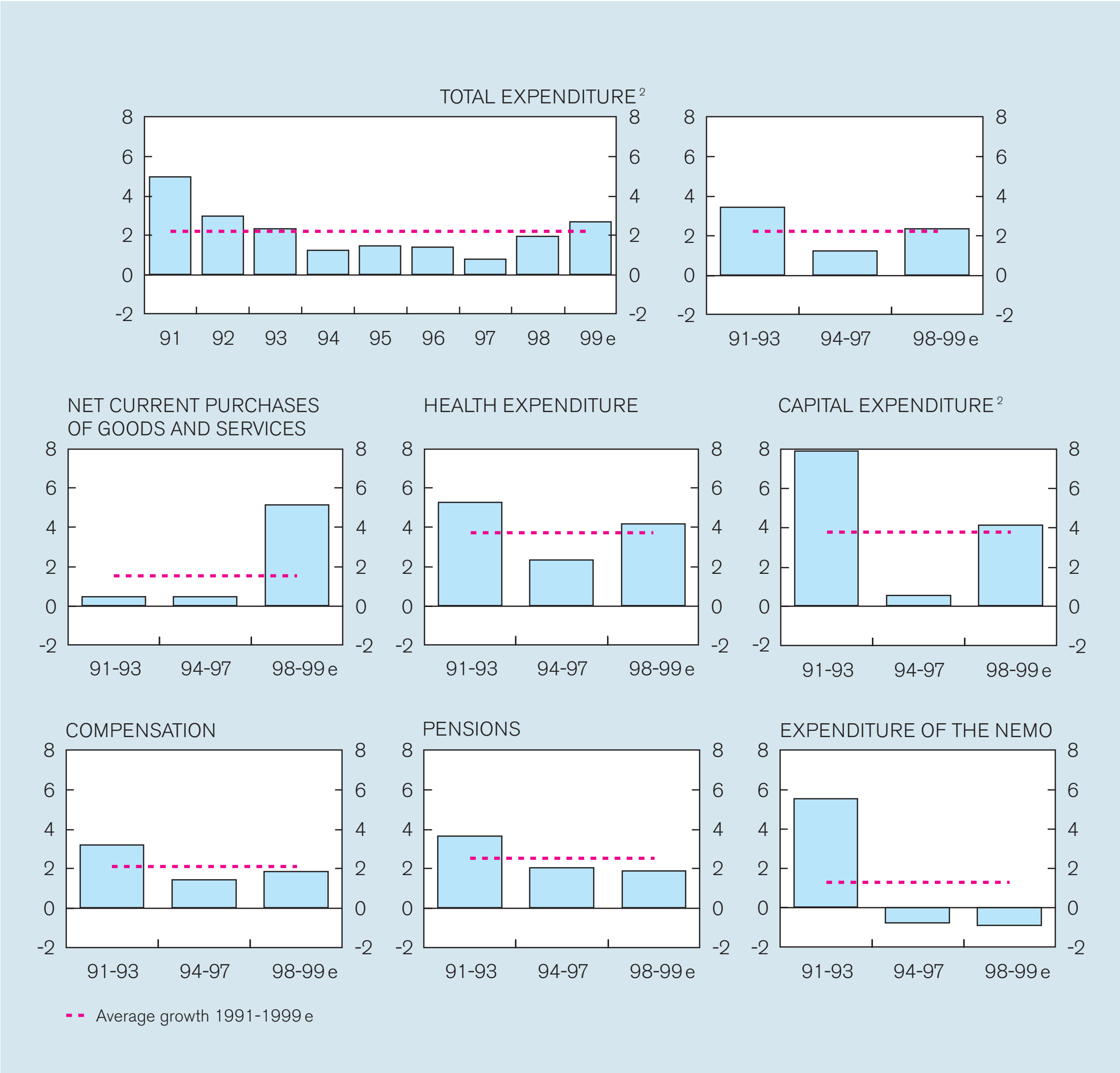
2 With the exception of GDP, the data are deflated by the national index of consumer prices.

3 Including the pensions of Post Office staff and the guaranteed income for old persons.

4 Exercise of the government guarantee for writing off the losses of public sector financial institutions, expenditure connected with the dioxin crisis and transactions deducted from expenses (sales of buildings and grants of licences for mobile telephony).

CHART 37 — GROWTH IN PRIMARY EXPENDITURE AT CONSTANT PRICES [1]

(Percentage changes)



Sources : NAI, NBB.

[1] Expenditure excluding interest charges, deflated by the national price consumer index.

[2] Corrected to eliminate non-recurrent capital expenditure.

considerably higher rate than in the previous year, owing to the sharp increase in health expenditure, subsidies to enterprises and capital expenditure.

The quickening of the rate of expansion of health care insurance interventions took place in hospitalisation expenditure. The latter, which had been curbed more than the other categories of intervention in 1998, accelerated mainly because of measures to boost staffing and pay levels in the hospital sector.

The sharp increase in subsidies in 1999 is artificial, because their level had been reduced the previous year by a repayment from the Post Office to the Treasury, following the change in the method of financing that body's staff pensions.

The movement of capital expenditure was influenced during the last few years by exceptional and non-recurrent transactions. Thus, in 1997 and 1998, this spending had been successively swollen by the investment aid granted for the building of the high-speed train network and by the clearing-off by the Treasury of the exchange losses on foreign currency loans contracted by a public credit institution. Capital expenditure nevertheless contracted in 1998, because, in accordance with the national accounts methodology, the payment to the federal government of the proceeds of the granting of a mobile telephony operation licence was deducted from this expenditure. In 1999, owing to the non-recurrent nature of all these transactions, a further decrease in capital expenditure might have been expected, but this spending increased on the contrary owing to the expenditure of around 420 million euro entailed by the compensation for the losses resulting from the contamination of food products by dioxin. If all this exceptional non-recurrent expenditure is disregarded, the change in capital expenditure appears to have swung from a fall of 1.2 p.c. in 1998 to a rise of 9.4 p.c. in 1999, primarily owing to the increase in investment by local authorities with a view to the municipal elections to be held in 2000.

Looked at from a longer-term viewpoint, the relatively high real growth in primary expenditure in 1998 and 1999 represents a trend break compared to the previous years. Adjusted for exceptional capital expenditure, it actually reached an average of 2.3 p.c. per annum during these two years, against an average of only 1.2 p.c. from 1994 to 1997. This quickening of the rate of rise of primary expenditure is partly the concrete manifestation of the regaining of a certain margin for manoeuvre by general government after years of budgetary consolidation. The small increase recorded until 1997 took place within the special context of the recovery efforts made to meet the Treaty of Maastricht's convergence criteria for the public finances, which were based on, among other things, compliance with a norm for the stabilisation of the federal government's primary expenditure in real terms. In accordance with the commitments entered into by the Belgian authorities at the beginning of 1998, fiscal policy was subsequently based on the principle of stabilisation of the primary surplus at a level of about 6 p.c. of GDP. Under normal economic conditions, this new norm offered Entity I a certain latitude for adapting its revenue or expenditure policy in a less restrictive manner than in the past.

The rise in primary expenditure was however more limited than that observed at the beginning of the 1990s when, after years of severe restrictions, the rise in spending had peaked at an average of about 3.5 p.c. per annum from 1991 to 1993. Various factors had contributed to this runaway movement, including the general revision of civil service scales, the upward adjustment of pensions in the public sector and the raising of pensions in the private sector, the increase in unemployment connected with the cyclical reversal and the particularly sharp increase in health expenditure and capital spending.

Overall, primary expenditure increased during the last two years, and on average also during the past decade as a whole, at a rate close to the trend increase in GDP, but appreciably higher than that, of about 1.5 p.c., assumed for the future in the stability programme.

The quickening of the rate of increase compared to the period 1994-1997 is attributable to that in current purchases of goods and services, health expenditure and capital expenditure. Spending in the first category, which had increased only very slightly in the first part of the 1990s, was influenced in 1999 by the expenditure connected with the elimination of food products contaminated by dioxin, such as analysis, storage and transport costs. The other two categories of expenditure, for their part, show a profile which tends to be repeated in a cyclical manner.

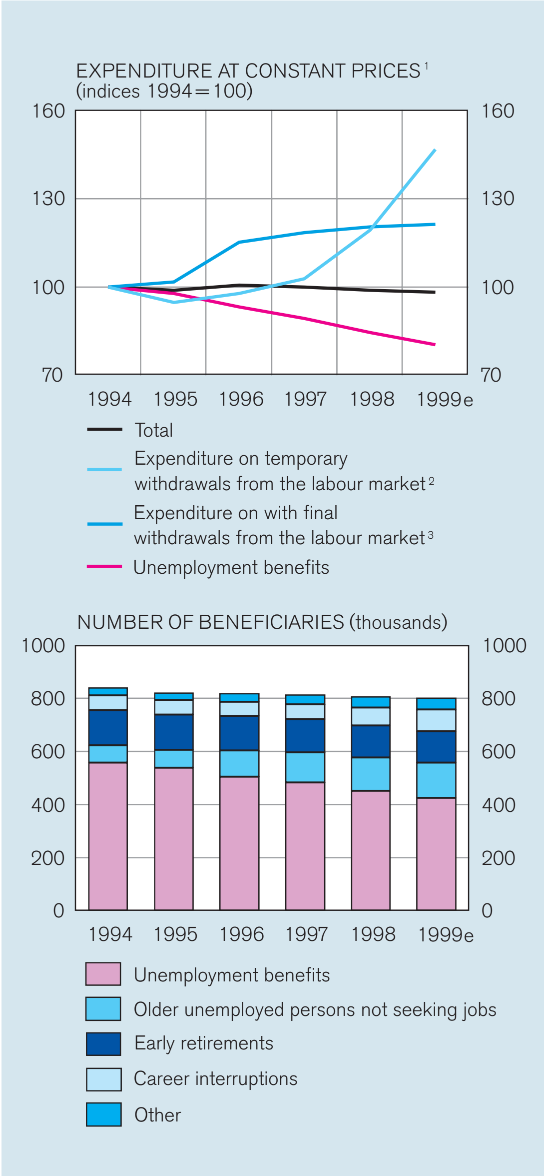
From year to year health expenditure does in fact fluctuate greatly, since periods of sharp rise alternate with periods of much more moderate growth, or even decline as in 1997, without such a profile being entirely explainable by the effect of discretionary measures. Over the past decade as a whole this expenditure increased on average by 3.7 p.c. per annum, or much more than the other categories of current expenditure.

Capital expenditure, for its part, is largely determined by the movement of investment by local authorities, which represents nearly 50 p.c. of public investment and is connected with the cycle of municipal elections every six years. Thus, from 1991 to 1993, the rise in investment by local authorities was particularly large, reaching nearly 30 p.c. in 1993, that is, during the year preceding the last municipal elections. During the following two years, i.e. in 1995 and 1996, this investment contracted on average by about 15 p.c. per annum. It resumed its growth from 1997 onwards, at first moderately and then much faster in 1999, with a view to the municipal elections in 2000.

On the other hand, the rate of increase of compensation and of replacement incomes did not speed up during the last two years.

Unlike the other categories of expenditure, the replacement incomes for which the NEMO is responsible, that is, the expenditure on unemployment benefits, early retirement pensions and career interruptions, have already been showing a slight decline for several years. This decrease has been coupled with an appreciable change in their structure over the years. Interventions for unemployment benefits shrank by nearly 20 p.c. from 1994 to 1999, parallel with the number of beneficiaries, which fell at the same time from about 557,000 units in 1994 to less than 425,000. On the other hand, expenditure on final withdrawals from the labour market increased owing to the rise of about 70,000 units in the number of persons coming under the scheme for older unemployed persons not seeking jobs, which is tending increasingly to take the place of the conventional early retirement system, the number of beneficiaries of which has declined in recent years. Lastly, expenditure on temporary withdrawals from the labour market, although smaller in amount, has also shown strong growth since 1997, the number of persons who have received compensation from the NEMO for career interruptions having risen from 57,000 to about 81,000 units. The greatest success has been

CHART 38 — EXPENDITURE OF THE NEMO



Sources : NEMO, NBB.

1 Deflated by the national index of consumer prices.

2 Career interruptions.

3 Scheme for older unemployed persons not seeking work and early retirement.

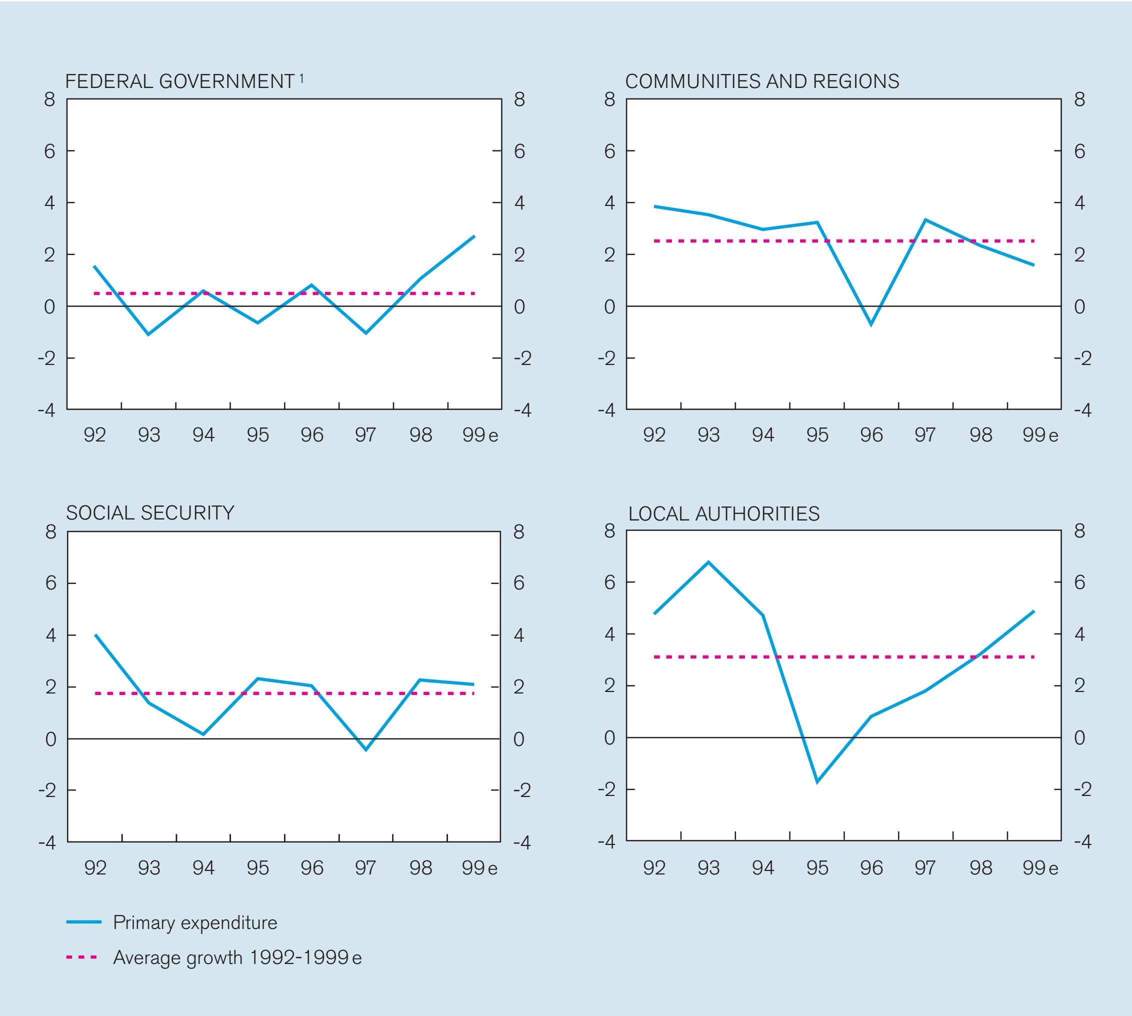
achieved by part-time career interruptions. Altogether, expenditure on unemployment benefits represented only half of the NEMO's total expenditure in 1999.

The increase in the rate of rise of primary expenditure in 1998 and 1999 took place in the accounts of the federal government and the local authorities. Thus, corrected to eliminate non-recurrent capital expenditure, the federal government's spending grew in real terms by 1.1 p.c. in 1998 and by 2.7 p.c. in 1999, whereas it had remained more or less stable on average during the 1990s. After years of severe restrictions, increased needs made themselves felt in some departments, chiefly connected with justice and security. At nearly 5 p.c., the local authorities' spending also grew faster than the long-term average, mainly pushed up by investment expenditure.

The growth in the expenditure of the communities and regions, which was more than 3 p.c. per annum at the beginning of the 1990s, slowed

CHART 39 — PRIMARY EXPENDITURE BY SUB-SECTOR

(Percentage changes at constant prices)



Sources : NAI, NBB.

[1] Corrected to eliminate non-recurrent capital expenditure.

down somewhat in the most recent period. In 1999 it amounted to only 1.6 p.c.

Social security expenditure remained, both in 1998 and 1999, despite the sharp rise in spending on health care insurance, fairly close to its average long-term expansion rate, in line with that of GDP.

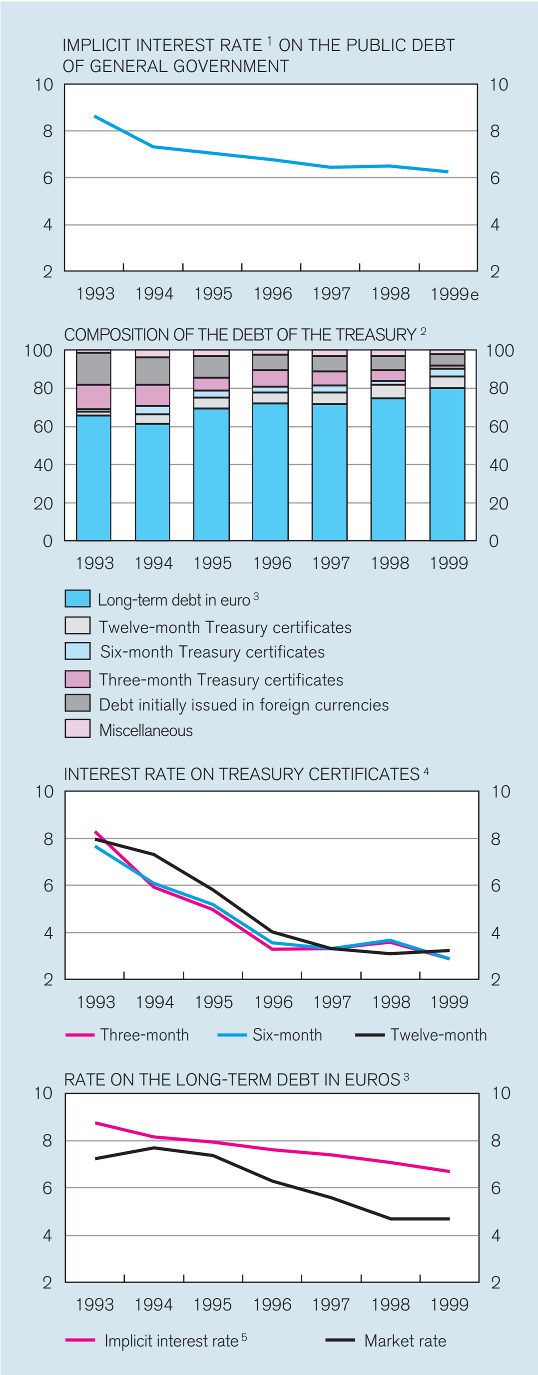
Interest charges

The changeover to the new methodology of ESA 95 entails a substantial change in the method of taking account of interest charges : these no longer have to be recorded at the time of payment but on a transactions basis, that is, taking account of the interest accrued over the whole or part of the year on debts contracted or redeemed during the year. This methodological change can strongly affect both the movement and the level of interest charges. Thus, in the new method, a nominal increase in the debt leads to a relatively faster increase in the charges for the year under review, to the extent of the amounts of interest accrued but not yet due which it generates. Furthermore, fluctuations in interest rates also manifest themselves faster in interest charges. Lastly, the incidence of changes in the financing structure according to maturity is reduced on a transactions basis. This is because the year-to-year shifts in interest payments which accompany these changes no longer affect interest charges, so that the incidence of changes in the financing structure remains restricted to that of the differences in the rates on the various components of the debt.

According to the new accounting method of ESA 95, the interest charges of general government as a whole declined by about 0.6 percentage point of GDP in 1999, to reach 7.1 p.c. of GDP, or the lowest level since the beginning of the 1980s. The sharp fall in interest charges during the year under review is due to the continuance of the contraction in the debt ratio and the further decline in the implicit interest rate on the public debt.

CHART 40 — INTEREST RATE ON THE PUBLIC DEBT

(Percentages)



Sources : Ministry of Finance, NAI, NBB.

[1] Ratio between the interest charges during the current year and the debt at the end of the previous year.

[2] Excluding the certificates disposited with the IMF.

[3] Excluding the loans issued before 1 January 1999 in currencies other than the Belgian franc and excluding variable-rate linear bonds, which are included in the «miscellaneous» category because their rate fluctuates like short-term rates.

[4] Average rate due on Treasury certificates.

[5] Ratio between the interest charges (including issue premiums) on and the average monthly outstanding amount of the debt.

After the rapid downward movement observed since the beginning of the 1990s, the implicit interest rate on the public debt rose again slightly in 1998, before showing a further – albeit limited – decline during the year under review. Its movement is determined chiefly by that of the average rate of the Treasury's debt, which represents the greater part of the public debt. This cost is influenced in turn by the composition of the Treasury's debt and by the rate on its main components.

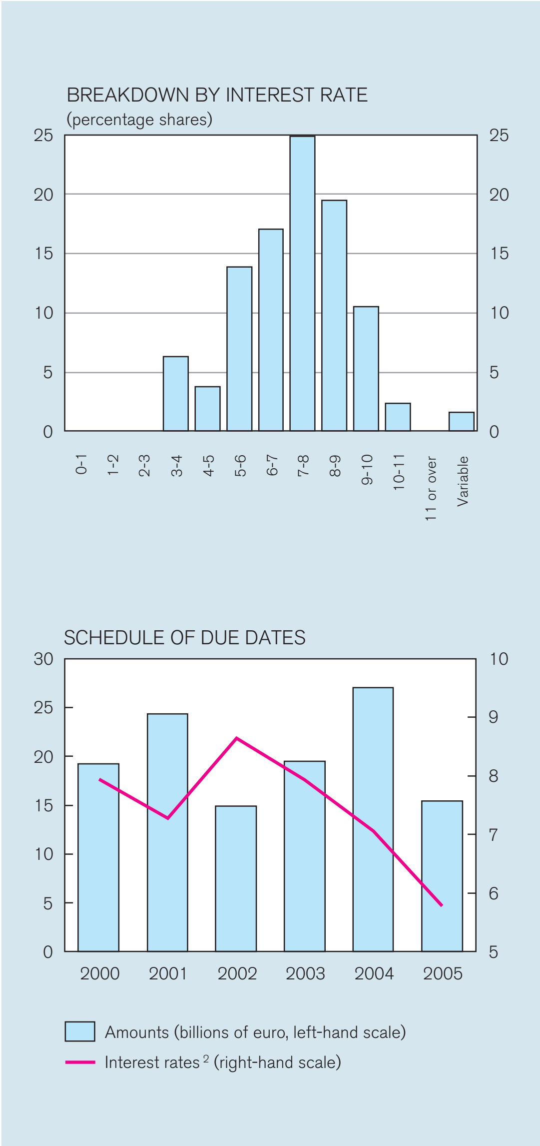
If the temporary decrease in the share of the long-term debt which took place in 1994 is disregarded, a clear trend towards longer maturities is seen to have emerged in recent years in the composition of the Treasury's debt, thus reducing the vulnerability of the public finances to changes in rates, which are difficult to foresee. As interest rates are generally higher the longer the maturity, this opportune increase in the average duration of the public debt resulted in a higher implicit rate on the public debt than if the structure had remained unchanged.

The fall in the implicit rate is therefore solely due to the decline in the rates on the various components of the debt. Short-term rates, the changes in which are reflected almost immediately in the implicit rate, have shown a clear downward trend in recent years. A jump in the rates on three-month and six-month certificates was recorded only briefly in 1998, contributing to the temporary interruption of the downward movement of the implicit rate on the public debt. During the year under review, however, the decline in the average rates on these certificates continued, mainly thanks to the reduction of 50 basis points in the rate for the main refinancing operations which the Governing Council of the ECB decided upon in April and despite the return of this rate to its initial level in November.

Long-term market rates have a less immediate incidence on interest charges, because only a limited proportion of the long-term debt is redeemed and refinanced at new rates each year. The sharp fall in long-term market rates in recent years has therefore not yet been fully reflected in the implicit rate on the long-term debt. During the year under review, this implicit rate was still 6.7 p.c., that is, a level about 200 basis points above the rate observed on average on the market for the Treasury's long-term issues in euro.

CHART 41 – THE TREASURY'S LONG-TERM DEBT IN EURO [1]

(Situation at the end of 1999)



Source : Ministry of Finance.

[1] Excluding loans issued before 1 January 1999 in currencies other than the Belgian franc.

[2] Average nominal rate on loans reaching maturity.

A substantial proportion of the Treasury's long-term debt is in fact still subject to relatively high nominal rates : these reach 6 p.c. or more for about three quarters of the Treasury's long-term debt in euro, and even 8 p.c. or above for one third. Unless market rates rise strongly during the next few years, the implicit rate on the long-term debt will continue to decline, because it will be possible for loans reaching maturity to be refinanced at lower rates.

The decline in interest charges should therefore continue, especially as, under normal economic conditions, general government's indebtedness as a percentage of GDP should continue to contract thanks to the maintenance of a high primary surplus and to the medium-term stabilisation of the debt in nominal terms.

Net financing requirement

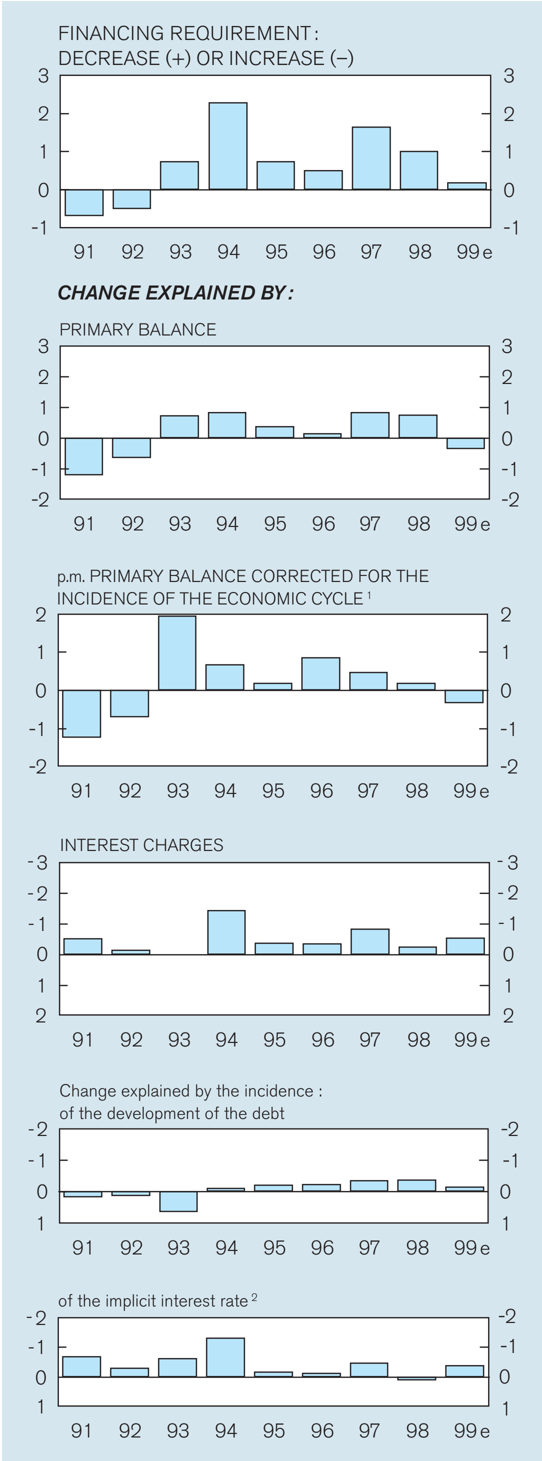
From 1992, during which year it had reached its highest level in the decade, to 1998, general government's net financing requirement decreased uninterruptedly, falling from 7.9 p.c. of GDP to 1 p.c. This reduction was due both to the growth in the primary surplus, which reached the particularly high level of 6.6 p.c. of GDP in 1998, and to the fall in interest charges.

The increase in the primary surplus over this period was chiefly due to the recovery efforts made by general government. This structural improvement was concentrated mainly on the years 1993 to 1997, during which the greater part of the budgetary consolidation measures were taken. In 1998, however, the increase in the primary surplus was mainly attributable to the good business situation, since there was only a small rise in the balance corrected for the influence of the economic cycle.

In 1999, for the first time since 1992 the primary surplus contracted. Thus it fell to 6.3 p.c., a level which is still however above the norm of 6 p.c. which the authorities undertook to comply with. As the incidence of the business situation

CHART 42 — NET FINANCING REQUIREMENT, PRIMARY BALANCE AND INTEREST CHARGES

(Changes compared to the previous year as percentages of GDP)



Sources : NAI, NBB.

[1] Change in the primary surplus corrected for the incidence of the business situation, the effects of changes in the distribution and allocation of the national income, and the incidence of relative prices.

[2] Calculated as a balance.

TABLE 23 — NET FINANCING REQUIREMENT OR CAPACITY OF GENERAL GOVERNMENT

(Percentages of GDP)

	1995	1996	1997	1998	1999 e
Revenue	45.4	46.0	46.3	46.4	46.3
Expenditure excluding interest charges	40.5	40.9	40.4	39.8	40.0
Primary balance	4.9	5.0	5.9	6.6	6.3
Entity I	4.4	4.3	4.9	5.5	5.2
Federal government	4.4	4.5	4.5	5.1	4.7
Social security	...	−0.2	0.4	0.4	0.5
Entity II	0.5	0.8	0.9	1.1	1.1
Communities and regions	−0.4	−0.1	0.2	0.5	0.8
Local authorities	0.9	0.8	0.8	0.6	0.3
Interest charges	9.1	8.7	7.9	7.7	7.1
Net financing requirement (–) or capacity	−4.2	−3.7	−2.0	−1.0	−0.9
Entity I	−3.8	−3.6	−2.2	−1.5	−1.3
Federal government	−3.8	−3.4	−2.7	−1.9	−1.8
Social security	...	−0.2	0.4	0.4	0.5
Entity II	−0.4	−0.1	0.2	0.4	0.5
Communities and regions	−0.7	−0.4	−0.1	0.2	0.5
Local authorities	0.4	0.3	0.3	0.2	−0.1
p.m. Stability programme of December 1998 [1]					
Primary balance			*6.0*	*6.0*	*6.0*
Entity I			*5.2*	*5.3*	*5.3*
Entity II			*0.8*	*0.6*	*0.7*
Net financing requirement (–) or capacity			*−1.9*	*−1.6*	*−1.3*
Entity I			*−2.0*	*−1.5*	*−1.3*
Entity II			*0.1*	*−0.1*	*...*

Sources: NAI, NBB.

[1] The data of the December 1998 stability programme were compiled in accordance with ESA 79. They are not, therefore, fully comparable with the other data in the table, which are compiled according to ESA 95.

was relatively neutral, the deterioration of 0.3 percentage point in the primary surplus is chiefly due to the reductions in employers' social security contributions and the negative effect of the non-recurrent transactions commented upon earlier.

This decline in the primary surplus was however more than counterbalanced by the further reduction in interest charges. Thus, the total net financing requirement declined slightly in 1999, to 0.9 p.c. of GDP, i.e. 0.4 point below the value adopted in the stability programme of December 1998.

The reduction in the primary surplus of general government took place mainly in the accounts of the federal government. It was chiefly due, on the one hand, to the contraction of 1.2 p.c. in real terms in the tax revenue accruing to it on balance after the allocations to the other general government bodies and, on the other hand, to the adverse net incidence of non-recurrent transactions. The primary surplus of the social security system, on the other hand, increased slightly, but, overall, the norm of stabilisation of the primary balance defined in the December 1998 stability programme for Entity I was not complied with. While the changeover to ESA 95 makes it difficult to compare the levels of primary surplus between the actual results and the aims of the stability programme, which was still drawn up according to ESA 79, the fact remains that this entity's primary balance decreased appreciably. This reduction, which amounted altogether to 0.3 point of GDP, is, it is true, partly attributable to accidental factors such as the dioxin crisis and the paying-off of amounts owed for the past to the communities.

Despite this decline in the primary surplus, the net financing requirement of Entity I decreased slightly, since the fall in general government's interest charges mainly benefited the federal government, which is in fact by far the most heavily indebted sub-sector.

The net financing capacity of the communities and regions increased by 0.3 percentage point of GDP in 1999, reaching 0.5 p.c. The rate of growth in their revenue remained very high owing to the application of the Financing Act and the paying-off of the amounts owed for the past. The growth in their expenditure actually slowed down. The local authorities' surplus, for its part, turned into a small deficit, mainly owing to the sharp rise in their expenditure. Altogether, the surplus of Entity II stabilised at the level of 0.5 p.c. of GDP, that is, well beyond the equilibrium rule laid down in the 1998 stability programme. It is only partly attributable to the above-mentioned paying-off, while the change-over to ESA 95 had no significant effect.

Debt

Since 1993, in which year the consolidated gross debt of general government as a whole reached a peak level of nearly 136 p.c. of GDP, the debt ratio has declined uninterruptedly. From 1994 to 1998 the annual contraction in the debt

TABLE 24 — CONSOLIDATED GROSS DEBT

(Percentages of GDP, unless otherwise stated)

	1993	1994	1995	1996	1997	1998	1999 e
Level of the debt	135.9	134.5	131.8	128.3	123.0	117.4	115.0
Change in the debt		−1.4	−2.7	−3.5	−5.3	−5.6	−2.4
Endogenous change		−1.4	−1.4	0.9	−4.0	−4.1	−3.0
Primary surplus required to stabilise the debt[1]		3.2	3.5	6.0	1.9	2.6	3.3
Real implicit interest rate on the debt[2]		5.5	5.3	5.6	5.1	4.9	5.2
p.m. Nominal implicit interest rate[2]		*7.3*	*7.1*	*6.8*	*6.5*	*6.5*	*6.3*
Deflator of GDP[2]		*1.8*	*1.8*	*1.2*	*1.3*	*1.6*	*1.0*
Real growth in GDP[2]		3.0	2.5	1.0	3.5	2.7	2.3
Actual primary balance		4.5	4.9	5.0	5.9	6.6	6.3
Change resulting from other factors		...	−1.4	−4.4	−1.3	−1.6	0.5
Returning of the NBB's surplus gains on gold		...	...	−2.7	...	−1.0	...
Privatisation operations		−0.2	−0.3	−0.9	−1.0	...	−0.1
Acquisitions (+) or sales (−) of other financial assets		−0.4	−1.6	−0.1	−0.8	0.3	0.3
Exchange rate differences		−0.2	...	−0.2	0.4	...	0.4
Other[3]		0.7	0.6	−0.5	0.1	−0.8	−0.1

Source: NBB.

[1] This balance is equal to the difference between the implicit interest rate on the debt and the rate of growth of nominal GDP, multiplied by the ratio between the debt at the end of the previous year and the GDP of the period in question.

[2] Percentages.

[3] Lending, equity investment, taking over of debt and statistical adjustments.

averaged 3.7 percentage points of GDP, the rate actually rising to five, or even nearly six, percentage points in 1997 and 1998.

The debt ratio continued its downward movement during the year under review, but only to the extent of 2.4 p.c. of GDP, a considerably smaller decline than in the preceding years. This slowing is chiefly attributable to two elements.

On the one hand, the contraction in the debt from 1994 to 1998 was connected to a considerable extent with exogenous factors without any incidence on the public deficit, such as the privatisations, the reduction in general government's financial assets with credit institutions and, chiefly in 1996 but also in 1998, the allocation for repayment of the foreign currency debt of the capital gains made by the Bank on the operations of arbitrage of gold against foreign currencies.

Unlike in the preceding years, such exogenous factors did not augment the endogenous reduction in the debt during the year under review, and even partly destroyed it. Around half of the proceeds of the sale of shareholdings in Cockerill-Sambre was actually used to reduce the debt, but this was not enough to offset the adverse incidence of the increase in the level of outstanding financial assets and fluctuations in exchange rates.

On the other hand, the endogenous decline in the debt slowed to 3 percentage points of GDP during the year under review, against about 4 percentage points in 1997 and 1998. This somewhat smaller decrease is attributable both to the slackening of economic growth – GDP at constant prices grew by 2.3 p.c. in 1999, against 3.5 and 2.7 p.c. during the preceding two years – and to the rise in the real implicit interest rate, which increased from 4.9 p.c. in 1998 to 5.2 p.c. during the year under review. This increase of the real implicit interest rate is connected with that in the deflator of GDP, which rose by 1 p.c. during the year under review, whereas it had still increased by about 1.5 p.c. during the previous years. The fall in the deflator was only partly counterbalanced by a very slight decline in the nominal implicit interest rate on the public debt, since the latter reflects the slowing of inflation and the accompanying lower market interest rates only with a certain time-lag, as the longer-term public debt loans are renewed.

6.2 INTERNATIONAL COMPARISON

Euro area

In 1999, with a deficit of 0.9 p.c. of GDP, Belgian general government had a net financing requirement smaller than that of the euro area considered as a whole, in which this sector's financing requirement represented 1.6 p.c. of GDP. According to data estimated by the EC, Belgium was outranked only by the Netherlands, with a slight deficit, and by three other small countries in the area, Finland, Ireland and Luxembourg, whose budgets showed a large surplus.

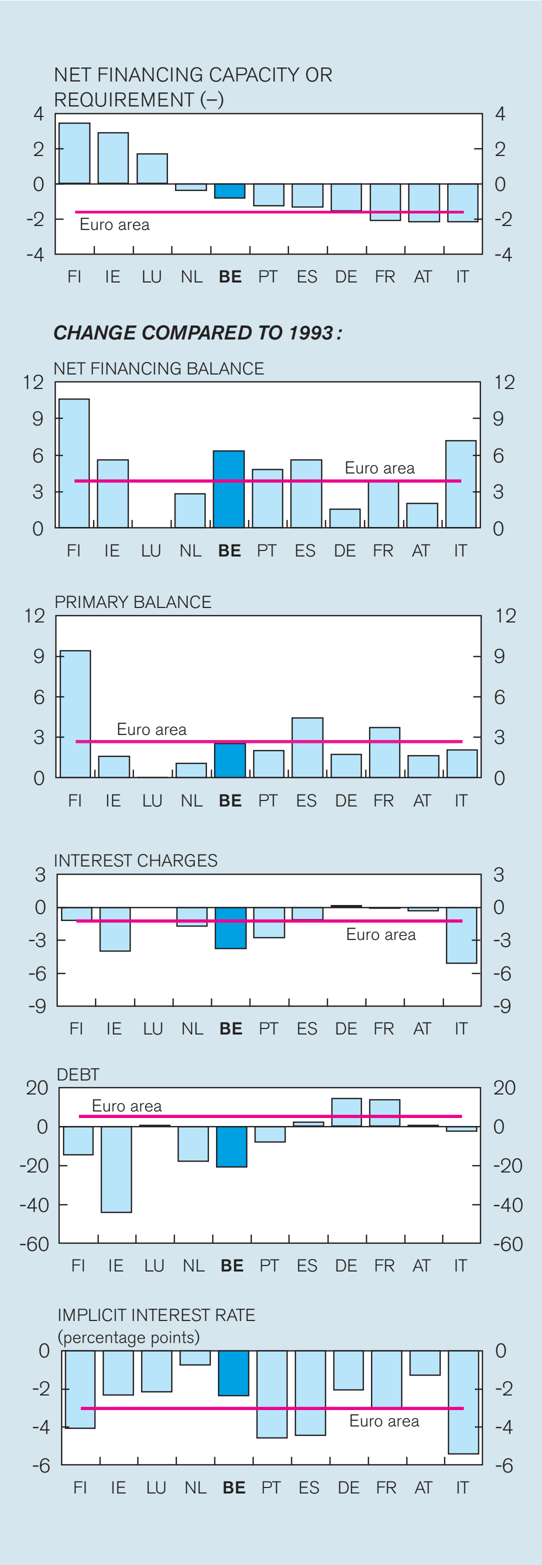
Since 1993, that is, the year during which the deficit of the public finances in the euro area countries reached an historic peak level, the improvement in the budget balance reached about 6.3 p.c. of GDP in Belgium, against 3.9 p.c. for the euro area, where all the countries found themselves in 1999 in a more favourable situation than six years earlier.

In most of the countries, the improvement in the public finances resulted chiefly from the movement of the primary balance, as interest charges underwent little change. In Belgium, however, the fall in interest rates was substantial, as in Portugal, Ireland and, above all, Italy.

In this group of countries where interest charges decreased sharply, Italy and Portugal benefited mainly from a substantial reduction in the implicit interest rate on the debt. These two countries

CHART 43 — PUBLIC FINANCES IN THE EURO AREA IN 1999

(Percentages of GDP, unless otherwise stated)



Sources : EC, NAI, NBB.

derived advantage from the downward convergence of their interest rates during the preparatory period for European Monetary Union. On the other hand, in Belgium and Ireland, as a larger proportion of the convergence of interest rates had already taken place previously, the reduction in the implicit interest rate was smaller during the period in question. The fall in interest rates there was thus largely due to the decrease in the debt, reflecting, to a great extent, the endogenous momentum of debt reduction associated with the high level of primary surplus achieved in both countries.

In Belgium, the debt reduction strategy thus pursued is desirable in order both to ensure that the public debt is reduced at a satisfactory pace towards the reference value of 60 p.c. of GDP, as required by the Treaty of Maastricht, and to generate a sufficient margin to cope with, among other things, the consequences of the ageing of the population.

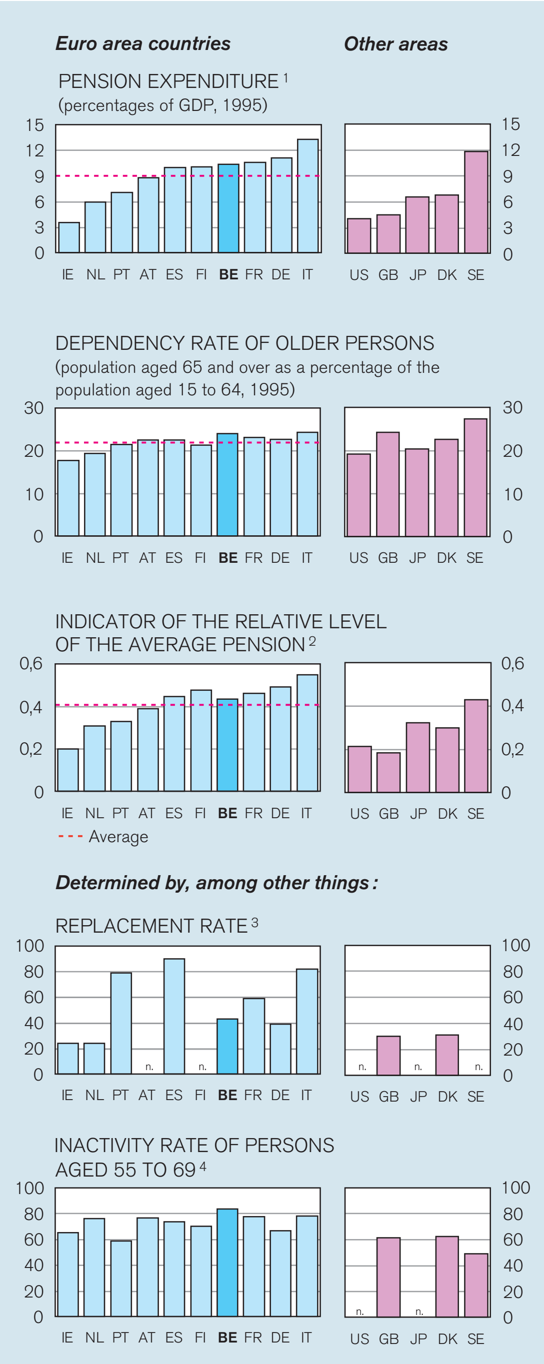
Expenditure on pensions and ageing of the population

During the coming decades the industrialised countries will be faced with a considerable ageing of their population, which will lead to a rise in the interventions of general government for the benefit of older persons, especially pension expenditure.

Actually, the extent of these benefits – financed via pay-as-you-go systems, that is, by the proceeds of social contributions or taxes – varies considerably from one OECD country to another. In 1995 they ranged between barely 4 p.c. of GDP in the Anglo-Saxon countries and 12 p.c. in Sweden and 13 p.c. in Italy. In Belgium they represented, as in France and Germany, about 10 p.c., thus standing at a level above the average for the euro area and appreciably higher than in the Netherlands, where they reached 6 p.c.

These appreciable differences may, in some cases, be attributable to the demographic situa-

CHART 44 — MAIN EXPLANATORY FACTORS OF THE LEVEL OF PUBLIC PENSION EXPENDITURE



Sources : EC, OECD, United Nations.

[1] The OECD figure for Belgium differs from that appearing in Table 22 in so far as it also includes the early retirement and ordinary retirement expenditure of public enterprises.

[2] Ratio between pension expenditure and the dependency rate of older persons or ratio between the average retirement pension per older person and GDP per person of working age, 1995.

[3] Ratio between the statutory pension and the wage for a typical worker (whose wage is equal to twice the average level in industry, whose career is complete and whose partner is dependent), 1989.

[4] Percentages of the population aged 55 to 69 not working and not unemployed, 1997.

tion, basically represented by the ratio between the number of older persons and the population of working age. Thus, the relatively low level of this dependency rate in Ireland, the United States and the Netherlands – where it is below 20 p.c. – helps to reduce the current amount of retirement pensions, while the high dependency rate observed for instance in Sweden, Italy and Belgium – where it reaches 24 p.c. or above – partly explains why expenditure is above average in these countries.

Apart from this demographic factor, different conceptions of the organisation of the social system do even more to explain the level of pension expenditure in the various countries. These conceptions are reflected, as an approximation and greatly simplified, by the ratio between pension expenditure and the aforementioned dependency rate, which provides a rudimentary yardstick for measuring the generosity of the pension system in each country.

On the basis of the figures for 1995, the generosity of the public retirement pension systems is high in Italy and low in the Netherlands and Denmark and, above all, in the Anglo-Saxon countries; Belgium is at a level slightly above the average. These differences are attributable to many factors, two of which can easily be quantified.

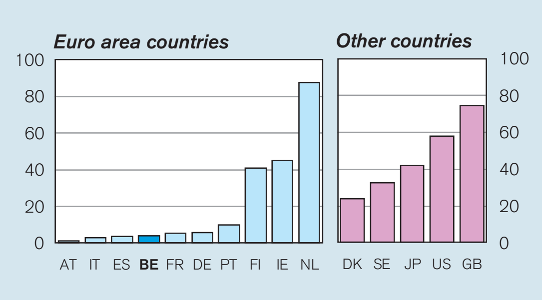
The first one is the replacement rate, that is, the ratio, for a typical worker, between the statutory pension and the wage received. This rate is high in Spain, Italy and Portugal, while it is slightly below the average in Belgium. It is moreover particularly low in the Anglo-Saxon countries, the Netherlands and Denmark, where the benefits paid to retired persons are only slightly, or even not at all, linked with their earlier occupational incomes, but are largely in the form of a flat-rate amount – that is, one identical for everybody.

The extent of the cost of retirement pensions for general government also depends on the number of older persons who receive benefit.

The number of inactive persons aged 55 to 69, that is, persons who do not work and are not unemployed, is an indicator of this, since, in a fair number of cases, these persons are in fact entitled to a retirement benefit. While the replacement rate of pension payments is below average in Belgium, the inactivity rate there is high : as in France, Italy, Austria and the Netherlands, it fluctuates around 80 p.c. Early retirement systems, on the other hand, are much less developed in Sweden, for instance, where the inactivity rate in this age group is slightly below 50 p.c.

CHART 45 — ASSETS OF PENSION FUNDS IN 1996

(Percentages of GDP)



Source : OECD.

The financial resources at the disposal of retired persons do not come exclusively from the social security system, nor from any part of general government. Apart from this first pillar, additional retirement pensions may also be organised via a capitalisation system, either at enterprise or sector – second pillar – level, or at purely individual – third pillar – level. It should furthermore be pointed out that general government also bears part of the burden of these retirement pensions, via fiscal expenditure items earmarked for this purpose.

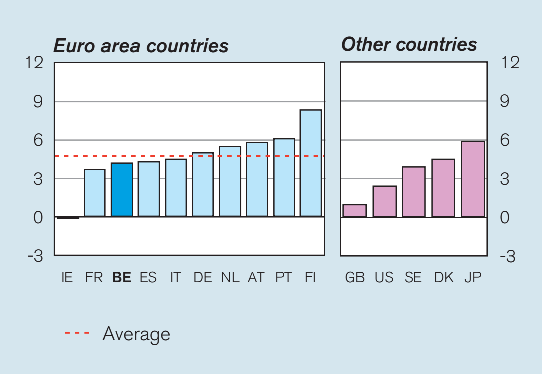
No exhaustive numerical data are available concerning the extent of capitalisation in pension systems. Mention is often made in this connection of the assets held by pension funds. The data on this indicate that the second pillar is not very extensive in countries which have a developed public system, as is the case in Belgium, France, Germany, Italy, Spain or Austria. By contrast, when general government guarantees only a limited replacement rate, as for instance in the Anglo-Saxon countries and the Netherlands, substantial assets are accumulated, per enterprise or per sector, as provision for the future.

However, if an examination is made not only of the resources of pension funds but also of all the financial assets which households accumulate in one form or another – and to which they can if necessary resort at the end of their working life – it becomes apparent that the resources capitalised in this way are very substantial in Belgium : as mentioned in the chapter on financial accounts and markets, the total net financial assets of Belgian households represented 585 billion euro, or about 250 p.c. of GDP, in September 1999.

The available projections show that, owing to the ageing of the population, public pension expenditure will increase substantially during the coming decades in the industrialised countries. The precise extent of this additional budgetary

CHART 46 — INCREASE IN PUBLIC PENSION EXPENDITURE BETWEEN 2000 AND 2030

(Percentages of GDP)



Source : OECD.

burden varies, however, from one study to another, with the figure obtained depending on a multitude of assumptions, concerning, for instance, the development of migration flows, the activity rate, economic growth, and the adaptation of retirements to prosperity. In 1996 the OECD estimated that, by 2030, pension expenditure will, with unchanged policies, be on average about four percentage points of GDP above the level currently observed in the OECD, the bulk of this rise taking place during the period 2010-2030.

In order to prevent the demographic trend from driving the public finances off course in the future, it is important to prepare here and now for this budgetary challenge. That is why the authorities of many countries are envisaging, or already carrying out, pension reforms. Particular emphasis is also placed on measures capable of increasing the employment rate and GDP, since a larger base makes it easier to cope with additional burdens. Lastly, the need for the soundest possible public finances, before the budgetary consequences of ageing make themselves felt, is also stressed.

7. SUMMARY OF TRANSACTIONS BY SECTOR

The summary of transactions by sector provides an overall view of the main movements of the economy, enabling the link to be made between the developments of the real economy and those observed on the financial markets. It reveals the net financing capacity or requirement of the domestic sectors as a whole, which can also be arrived at via the current transactions and capital account of the balance of payments.

From 1998 to 1999 the net financing capacities and requirements of the various domestic sectors underwent little change as percentages of GDP. Overall, the net lending of the Belgian economy to the rest of the world stabilised at about 4 p.c. of GDP.

Gross saving by individuals declined a little more in 1999, both in relation to GDP and as a proportion of disposable income. This further reduction in the savings ratio, from 16.7 p.c. of disposable income in 1998 to 16.3 p.c. in 1999, is attributable to several factors. First, the gradual improvement of the labour market, the realisation that the consolidation of the public finances is bearing fruit and the conviction that the purchasing power of the currency is better protected as a result of Belgium's participation in EMU are all elements which have contributed to the restoration of household confidence, thus reducing the need to build up precautionary savings. Secondly, incomes from property, of which a larger proportion is saved, decreased in 1999, so that their share in disposable income declined further. Moreover, it is quite possible that the wealth effect resulting from the good performance of the stock markets in recent years has also contributed to the fall in the savings ratio, since the capital gains made in recent years on holdings of shares, which constitute a growing proportion of the financial assets of households, are not recorded as incomes but nevertheless increase the financial assets of individuals and may have led to a rise in consumption.

TABLE 25 — NET FINANCING CAPACITY OF INDIVIDUALS

(Percentages of GDP)

	1995	1996	1997	1998	1999 e
1. Gross disposable income	66.2	65.7	64.2	63.8	63.3
2. Change in the pension fund entitlements of individuals	0.6	0.8	0.9	0.7	0.7
3. Final consumption expenditure	53.9	54.2	53.6	53.8	53.7
4. Gross savings (1 + 2 − 3)	12.9	12.3	11.4	10.7	10.3
p.m. Savings ratio [1]	*19.4*	*18.7*	*17.8*	*16.7*	*16.3*
5. Capital transfers [2]	0.4	...	−0.1	−0.1	−0.1
6. Gross capital formation	6.6	6.4	6.5	6.5	6.5
7. Net financing capacity (4 + 5 − 6)	6.7	5.9	4.9	4.0	3.7

Sources: NAI, NBB.

[1] Gross savings expressed as percentages of gross disposable income.

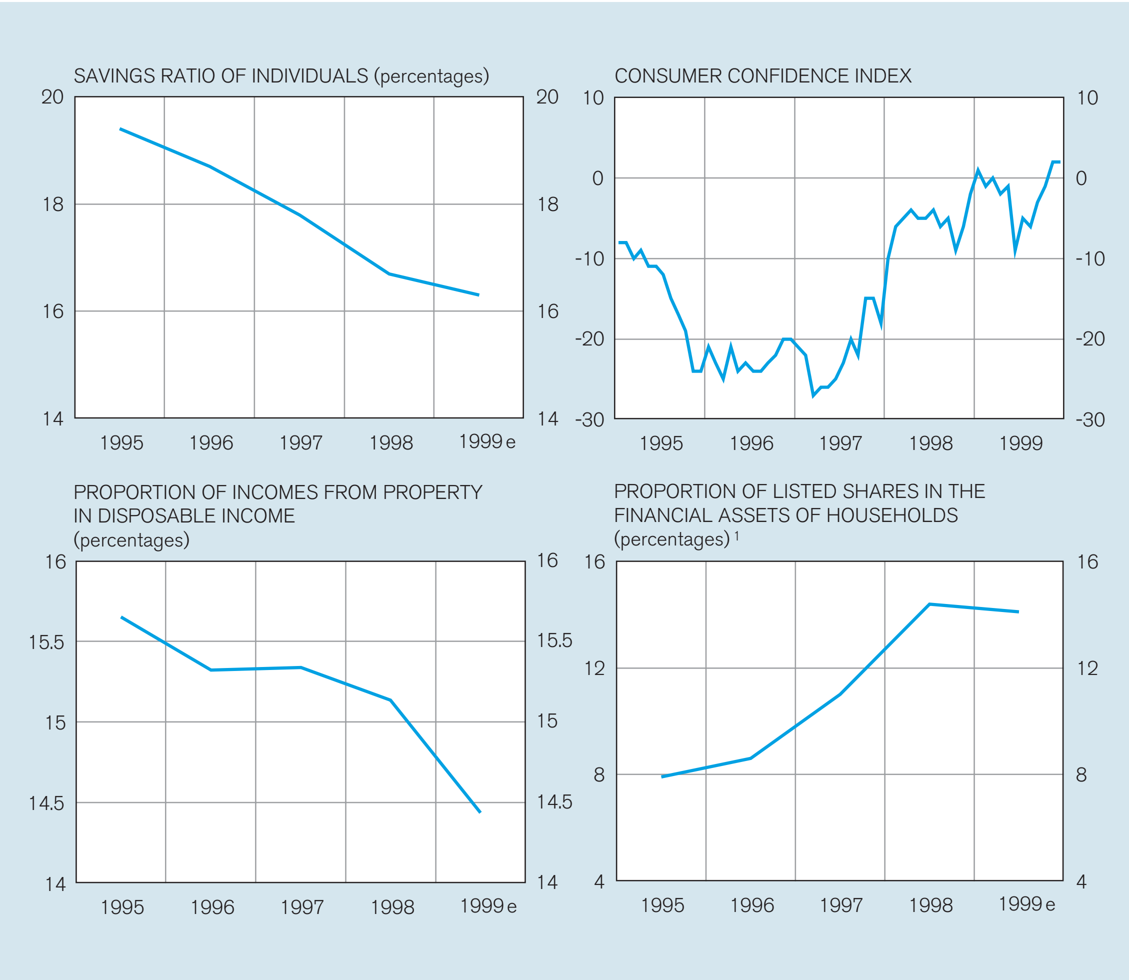
[2] These are net amounts, that is the difference between the transfers received from other sectors and the transfers paid to other sectors, including net acquisitions of non-financial assets.

The rise in capital transfers received by individuals – especially by owner-entrepreneurs in compensation for damage due to the dioxin crisis – was of the same order of magnitude as that in capital taxes, so that, on balance, net capital transfers stabilised. As individuals' propensity to invest also remained unchanged, the decrease in their gross saving was reflected in a further reduction in their net financing capacity.

Unlike during the three preceding years the gross savings of companies did not decrease in 1999, the reduction in current transfers paid to the others sectors, chiefly general government, having been counterbalanced by a similar movement in gross primary income. The latter decreased owing to the rise of 0.3 p.c. of GDP in interest payments and net dividends, while the gross operating surplus remained practically unchanged. As both capital transfers and gross capital formation underwent little change, the net financing capacity of companies remained the same as in 1998.

The net financing capacity of general government decreased by 0.1 p.c. of GDP during the year under review.

CHART 47 — SAVINGS RATIO OF INDIVIDUALS AND SOME DETERMINANTS



Sources : EC, NAI, NBB.

[1] Including shares held indirectly by households via the institutional investors with which part of their savings are invested. Annual average of end-of-year situations, except in 1999, (until September for 1999).

TABLE 26 — NET FINANCING CAPACITY OF COMPANIES

(Percentages of GDP)

	1995	1996	1997	1998	1999 e
1. Gross operating surplus	18.6	18.4	19.0	19.1	19.2
2. Net incomes from property paid to other sectors [1]	–1.9	–1.8	–2.3	–2.3	–2.6
3. Gross primary income (1 + 2)	16.7	16.6	16.6	16.8	16.6
4. Net current transfers to the other sectors [1 2]	–2.7	–2.9	–3.2	–3.7	–3.5
5. Gross savings (3 + 4)	14.0	13.7	13.4	13.1	13.2
6. Capital transfers [1]	...	0.6	1.1	0.9	0.8
7. Gross capital formation	12.1	12.0	12.5	13.0	12.9
8. Net financing capacity (5 + 6 – 7)	1.9	2.3	2.0	1.1	1.1

Sources : NAI, NBB.

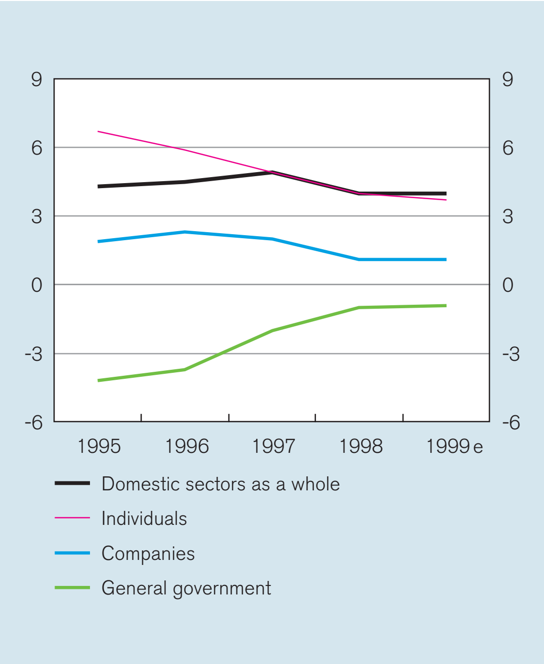
[1] These are net amounts, that is the difference between the transfers received from other sectors and the transfers paid to other sectors.

[2] Including net acquisitions of non-financial assets and changes in individuals' pension fund entitlements.

Overall, the movements described above offset each other, so that the net domestic financing capacity remained unchanged.

CHART 48 — NET FINANCING REQUIREMENT (–) OR CAPACITY BY MAJOR SECTOR

(Percentages of GDP)



Sources : NAI, NBB.

The latter, which is calculated as the sum of the net financing capacities or requirements of the three domestic sectors, should, in principle, correspond to Belgium's net lending to the rest of the world, i.e. the sum of the current account balance and the capital account balance of the balance of payments. Nevertheless, this equality is not apparent in the figures, because the national accounts statistics and the data on the balance of payments, which provide a detailed survey of the transactions of residents with non-residents, are not completely harmonised, particularly as regards incomes.

The balance of Belgium's capital account, which comprises capital transfers – including debt forgiveness and grants for financing investment projects in, among others, developing countries – as well as acquisitions and sales of non-produced non-financial assets, such as land, patents and licences, is generally small and has little influence on the overall course of net lending to the rest of the world. Consequently, the level and development of the latter, which remained virtually stable during the year under review, are almost exclusively attributable to the current account balance.

TABLE 27 — NET LENDING TO THE REST OF THE WORLD ACCORDING TO THE BALANCE OF PAYMENTS

(Balances, billions of euro)

	1995	1996	1997	1998	1999 e
Current account	8.3	8.7	10.4	9.3	9.3
Goods and services	8.2	8.3	9.8	9.1	9.3
Goods	8.1	8.0	8.6	8.5	7.9
Services	0.1	0.3	1.2	0.6	1.4
Incomes	3.0	3.5	3.8	3.9	3.9
Current transfers	–2.9	–3.1	–3.2	–3.7	–3.9
Capital account	0.1	0.1	0.4	–0.1	–0.1
Net lending to the rest of the world	8.4	8.8	10.8	9.2	9.1
p.m. Percentages of GDP	*4.2*	*4.3*	*5.0*	*4.1*	*3.9*
Net financing capacity according to the national accounts	*8.7*	*9.3*	*10.5*	*9.1*	*9.2*

Sources: NAI, NBB.

The greater part of Belgium's current account surplus stems from the surplus in respect of transactions in goods and services with the rest of the world. Traditionally, incomes received from and paid to the rest of the world also generate a positive balance, while current transfers generally show a deficit of the same order of magnitude.

During the year under review the surplus on the goods and services account expanded slightly, while that on the income account stabilised. On the other hand, the deficit in respect of current transfers increased slightly further.

The slight improvement in 1999 in the surplus on transactions in goods and services, amounting to 0.2 billion euro, was due to the so-called level effect, whereby an identical growth in exports and imports in value leads to a larger surplus because the former were greater than the latter the previous year. Whereas in 1998 a substantial improvement in the terms of trade had been more than counterbalanced by a marked worsening of the coverage rate in volume, exactly the opposite developments were recorded during the year under review. Thus, in 1999, the volume of exports increased more than that of imports, to the extent of 0.7 percentage point. At the same time, import prices rose somewhat owing to the sharp increase, of around 40 p.c., in energy prices, while export prices declined slightly, bringing about a worsening of the terms of trade of about 0.7 percentage point.

The movements recorded in transactions in goods and services were not homogeneous.

TABLE 28 — TRANSACTIONS IN GOODS AND SERVICES WITH THE REST OF THE WORLD [1]

(Percentage changes compared to the previous year)

	1998	1999 e
Values		
Exports	3.9	2.4
Imports	4.6	2.4
Volumes		
Exports	4.2	2.9
Imports	6.3	2.2
Unit values		
Exports	–0.3	–0.5
Imports	–1.6	0.2

Sources: NAI, NBB.

[1] Unlike the method of recording used in the balance of payments, goods for processing were recorded in gross terms.

While the surplus on transactions in services increased by 0.8 billion euro, that on transactions in goods decreased by 0.6 billion euro. The improvement in the balance on services was due to net increases in the surpluses under the subheadings transportation and construction services. The slower growth in the volume of goods imports compared to the volumes exported probably led to a sharper fall in expenditure on transportation than in earnings from it. The larger surplus recorded in construction services is attributable to the fact that the building by foreign contractors of a new production unit of a large enterprise in Belgium was completed at the end of 1998, leading to the disappearance of a large amount of expenditure.

The net factor incomes which Belgium receives from the rest of the world did not increase further in 1999. Net compensation of employees did rise slightly more, while incomes from direct and portfolio investment decreased, the downward movement of interest rates having had a greater incidence than the further growth in Belgium's net assets on the rest of the world, which, at the end of September 1999, were estimated at 89 billion euro.

With regard to current transfers, both transfers by individuals and those by general government resulted in a larger deficit than in 1998. For the latter, this is attributable to the rise in Belgium's contribution to the budget of the EU.

8. FINANCIAL ACCOUNTS AND FINANCIAL MARKETS

8.1 FINANCIAL ACCOUNTS

Change of monetary unit

The introduction of the euro radically alters the environment in which financial transactions take place. It requires, on the part of economic agents, adaptations which take place at different rates depending on the sectors, but also in relation to the three major functions of money, namely those of unit of account, means of payment and store of value.

In everyday life, the franc still serves as the unit of account, despite the gradual spread of double price marking. On the other hand, for quotations on the financial markets, the euro was immediately adopted as the reference value. Stock market prices and most securities issued by public and private borrowers are henceforth denominated in euro, and the exchange rates for the currencies of the countries not belonging to EMU are expressed in relation to that currency.

The use of the euro by enterprises is steadily increasing. Several surveys have aimed at measuring the development of this degree of use. In September 1999, according to a survey published by the Federation of Belgian Enterprises, nearly half of enterprises made out at least part of their invoices in euros, while 21 p.c. kept their accounts in that currency. The percentages are considerably higher for export-oriented companies than for those which confine their activities to the domestic market.

While the transition to the new unit of account is gradual, the shift towards the new means of payment is marked by two major steps. The first took place on 1 January 1999, when the changeover from the franc to the euro took place for all monetary policy interventions, all interbank transactions and virtually all transactions on the rest of the money market. The second step, still being prepared for, will correspond to the introduction, in 2002, of euro notes and coins. Between these two phases, economic agents can choose when to convert their bank accounts.

This process made relatively little progress in 1999, since in September, according to an estimate by the BBA, less than 1 p.c. of the accounts of individuals and less than 2 p.c. of company accounts were then expressed in euro.

TABLE 29 — USE OF THE EURO AS UNIT OF ACCOUNT IN BELGIAN NON-FINANCIAL ENTERPRISES

(Percentages of total number of enterprises)

	February 1999	September 1999	of which:		
			Non-exporting enterprises	Enterprises exporting mainly	
				within the euro area	outside the euro area
Enterprises sending out invoices in euro	41	49	39	55	59
Enterprises keeping their accounts in euro	15	21	13	27	23

Source: Survey by the Federation of Belgian Enterprises.

TABLE 30 — DEGREE OF USE OF THE EURO IN SMALL BANK PAYMENTS

(Percentages)

	Number of payments	Amount of payments
1st quarter	0.86	5.77
2nd quarter	1.02	6.86
3rd quarter	1.87	8.38
4th quarter	1.12	8.25

Source: NBB.

The percentage rose, however, to about 15 p.c. for large enterprises, which converted a substantial proportion of their accounts previously expressed in monetary units of the other countries of the euro area.

This relative inertia is reflected in the degree of the use of the euro for small payments between Belgian banks, as measured by the transactions carried out in the CEC. In the fourth quarter of 1999, payment instructions in euro represented only 1.1 p.c. of the total number of orders. In the case of large enterprises, which have advanced proportionally further in the movement of changeover to the euro, the percentage of the total amount of payments during this period was 8.3 p.c. Movements from quarter to quarter indicate that the conversion rate is still very slow.

The transition to the euro as a store of value does not create the same psychological difficulties or operational problems as those connected with the other two functions of money. At this level the change occurred automatically, as the creation of the euro irrevocably eliminated any exchange risk for a wide range of financial assets and liabilities.

This effect remained relatively limited for liabilities, as the debts of individuals were almost exclusively expressed in francs. Furthermore, general government had already substantially reduced its foreign currency borrowings during the preceding years. Lastly, while the foreign currency liabilities of enterprises are relatively

TABLE 31 — BREAKDOWN BY CURRENCY OF THE FINANCIAL ASSETS AND LIABILITIES OF THE MAJOR DOMESTIC SECTORS

(End-of-period outstanding amounts)

	December 1998		September 1999	
	Total in billions of euro	of which: Percentages of currencies other than the franc	Total in billions of euro	of which: Percentages of currencies other than the franc
Financial assets [1]				
Individuals	660	18.7	683	11.2
Companies	331	33.0	360	14.3
General government	21	0.6	23	0.3
Total	1,012	23.1	1,066	12.0
Financial liabilities				
Individuals	93	0.7	98	0.6
Companies	590	7.3	597	4.4
General government	274	6.2	282	3.7
Total	957	6.4	977	3.8

Source: NBB.

[1] The breakdown by currency of the assets built up via institutional investors was calculated on the basis of the structure of the investments made by these investors.

large in absolute amount, their relative share remains small, as a large proportion of the liabilities of companies is in the form of equity. Overall, the introduction of the euro led to a reduction in the proportion of the liabilities of the domestic sectors as a whole which are not denominated in the national currency, from 6.4 p.c. at the end of 1998 to 3.8 p.c. at the end of September 1999.

The single currency had a greater effect on the structure of assets. At the end of 1998 companies held nearly one third of their financial assets in foreign currencies, this high percentage reflecting the substantial direct investments made in foreign enterprises. As these equity investments are largely made in companies in neighbouring countries, the changeover to the euro was reflected in a decrease of over a half in the foreign currency assets of enterprises. The foreign currency position of individuals also fell. At the end of 1998 over 18 p.c. of this sector's investments consisted, directly or indirectly, of claims in currencies other than the national currency. As a result of the introduction of the euro, that percentage was down to 11.2 p.c. at the end of September 1999.

Individuals

The financial surplus of individuals reached 15.2 billion euro during the first nine months of 1999. While the formation of financial assets showed an increase, from 16.3 to 20 billion euro, new liabilities came to only 4.8 billion against 5.1 billion the previous year.

Individuals had, it is true, increased their liabilities very substantially between 1995 and 1998, so that the recent movement represents only a relative decrease. Moreover, expressed as a percentage of disposable income, their debt ratio went on rising. While it is still far below the percentages observed in most of the other industrialised economies, especially the Anglo-Saxon countries and Japan, this rate amounted to 65 p.c. in 1999, compared to 63.3 p.c. the previous year and 56.9 p.c. in 1995. This increase was, however, coupled with a rise in the financial assets held by households, so that, in relation to total financial assets, this sector's debt declined from 15.6 p.c. in 1995 to 14.1 p.c. in 1999.

During the last few years, recourse by individuals to borrowing was undoubtedly stimulated by the decline in the banks' debtor interest rates, as a result of the combined effects of the general fall in interest rates and keener competition on the credit market. After having fallen to historic lows at the beginning of the year, they moved upwards again from the second quarter onwards. This reversal applied both to mortgage loans and to instalment loans, which are the two major traditional forms of financing used by households.

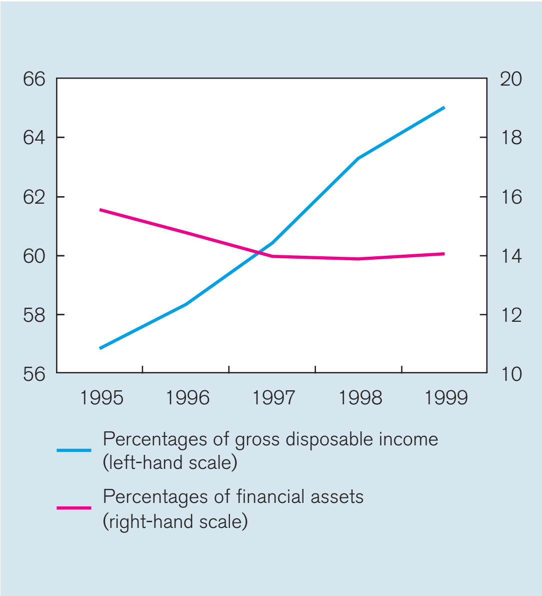
TABLE 32 — FORMATION OF FINANCIAL ASSETS BY AND NEW FINANCIAL LIABILITIES OF INDIVIDUALS

(Billions of euro)

					First nine months	
	1995	1996	1997	1998	1998	1999
Formation of financial assets	19.3	26.2	28.9	22.1	16.3	20.0
New financial liabilities	1.8	4.4	5.5	6.9	5.1	4.8
Financial balance	17.5	21.9	23.4	15.2	11.1	15.2

Source: NBB.

CHART 49 — FINANCIAL LIABILITIES OF INDIVIDUALS [1]



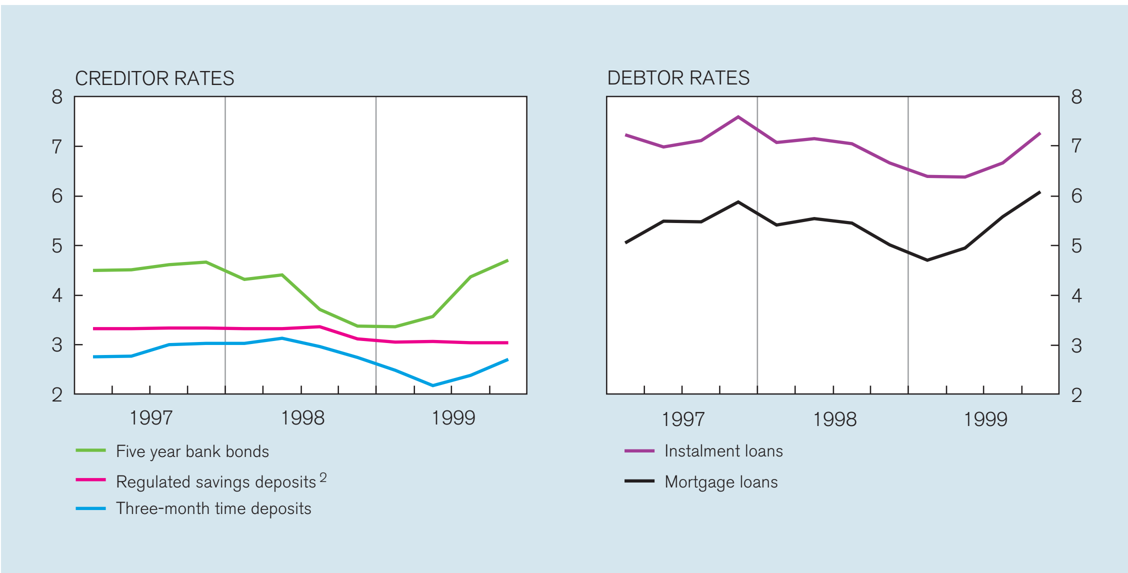
Source : NBB.
[1] End-June data for financial assets and liabilities.

Most of the banks' creditor rates were also raised, although this movement was not uniform for all categories of products. The rates on bank bonds showed the largest rise, reattaining the levels in force at the beginning of 1998. This development reduced the disinclination of individuals to use this form of investment. During the first nine months of 1999 the outstanding amount of bank bonds and other fixed-interest securities issued by banks decreased by only 2.9 billion euro compared to 6.1 billion in 1998. Conversely, the rates on savings deposits were not readjusted upwards. This relative inertia of the conditions offered on savings deposits is not new. The rates on savings deposits have remained very stable during the last three years; their decline during the downward phase of interest rates in the second half of 1998 and the early months of 1999 was only marginal.

While the raising of rates played a part in reducing the unpopularity of investments with credit institutions – which increased overall by 6.4 billion euro during the first nine months whereas they had decreased by 3.9 billion in 1998 – it did not lessen the infatuation of individuals with

CHART 50 — BANK INTEREST RATES [1]

(End-of-period data)



Source : NBB.
[1] Rates obtained by means of a survey among the main credit institutions, weighted by the market share of each of these institutions.
[2] Fictitious gross rate, including the fidelity bonus, calculated on the net rate in such a way as to make it comparable to the gross yield on assets which are not exempt from the withholding tax on movable assets.

TABLE 33 — STRUCTURE OF THE FORMATION OF FINANCIAL ASSETS BY INDIVIDUALS

(Billions of euro)

				First nine months	
	1996	1997	1998	1998	1999
With credit institutions	10.1	2.7	−1.6	−3.9	6.4
Notes and overnight deposits	0.4	0.9	3.2	2.8	4.9
Savings deposits	10.7	7.9	4.5	2.0	2.1
Notes and other fixed-interest securities	−3.4	−8.6	−7.3	−6.1	−2.9
Other	2.3	2.5	−2.0	−2.5	2.2
With institutional investors	10.1	15.4	25.0	21.3	18.0
Guaranteed-capital index UCIs	2.7	4.2	6.7	7.4	2.7
Share UCIs	−0.2	1.4	4.4	3.4	3.8
Other UCIs	1.3	1.5	4.8	3.8	3.7
Insurance companies and pension funds	6.3	8.2	9.0	6.8	7.8
Direct purchases of securities and miscellaneous assets	6.1	10.8	−1.3	−1.2	−4.4
Shares [1]	2.6	2.9	2.0	2.2	4.8
Fixed-interest securities and miscellaneous assets	3.5	7.9	−3.3	−3.4	−9.2
Total	26.2	28.9	22.1	16.3	20.0

Source: NBB.
[1] Including real estate certificates.

stock exchange investments. These investments, which, in 1999, were mainly in foreign shares, once more represented the main method of building up financial assets : the aggregate amount of purchases of units of share UCIs and index UCIs together with direct purchases of shares reached 11.3 billion euro during the first three quarters of 1999, against 13 billion in 1998.

However, these transactions assumed a different form. The interest in guaranteed-capital index UCIs decreased, and individuals displayed a more marked preference for direct purchases. This recent change in the channels via which individuals invest in risk capital might have been due to two reasons. Firstly, the financial conditions were less conducive to the creation of index UCIs with capital protection. In order to offer yields linked to the movement of stock market prices while ensuring the maintenance of the capital invested, these institutions use the funds which they raise not to acquire shares but to acquire bonds or time deposits and options on indices. Now the increase in the volatility of stock market prices had the effect of making these options more expensive, while the low level of long-term rates limits the yields obtained on fixed-interest assets. These index UCIs have thereby become much more expensive to build up, so that they have no longer offered such attractive yields possibilities as previously. Secondly, it is also quite possible that a growing number of individuals have resorted, for their stock market investments, to the asset management services which both credit institutions and investment enterprises have endeavoured to develop and extend during the last few years.

Companies

During the first three quarters of 1999 the financial equity capital which companies have been able to generate through their activities declined slightly, from 17.9 to 16.5 billion euro.

As this sector's investments went on increasing, the financial deficit of enterprises increased.

Both the formation of assets and new liabilities showed an upward trend. The growth in the former is due to a rise in deposits abroad and to equity investments in the form of direct investments. The increase in the latter is attributable especially to the growth in share issues, which were particularly substantial at the beginning of the year.

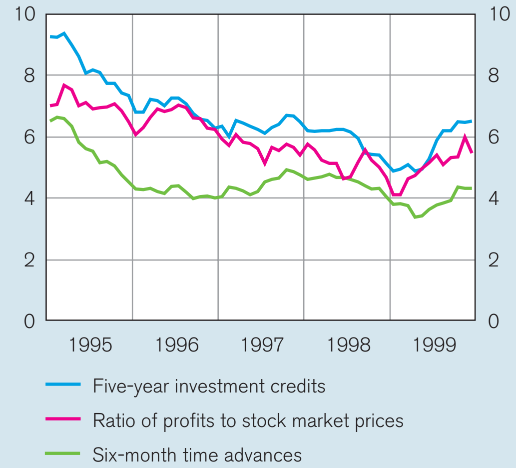
The financing costs of companies, which had gradually decreased from the beginning of 1995 until the start of the year under review, subsequently increased again. This rise was not confined to short-term and long-term bank credits. The decline in prices on the Brussels Stock Exchange also had the effect of making share issues more expensive, as the raising of a given amount of equity capital henceforth led to a greater dilution of the existing capital. This cost increase can be illustrated by the price earnings ratio or, alternatively, by its opposite, the ratio of profits to stock market prices.

The latter percentage, which had declined during the preceding years, recovered in 1999. It thus moved parallel with nominal interest rates, although it is a datum of a different nature, as the ratio of profits to prices is akin to a real yield.

The market price of shares is of course known only for listed securities. Now a large proportion of the issues made by Belgian companies take

CHART 51 — FINANCING COSTS OF COMPANIES

(Percentages)



Sources : BBL, NBB.

TABLE 34 — FINANCING STRUCTURE OF COMPANIES [1]

(Billions of euro)

	1996	1997	1998	First nine months 1998	First nine months 1999
Equity capital	18.5	17.4	22.9	17.9	16.5
Gross fixed capital formation	23.7	25.5	26.7	18.3	19.5
Financial balance	−5.2	−8.1	−3.9	−0.4	−3.0
Formation of financial assets	12.3	10.3	16.1	11.7	25.2
Financial liabilities	17.5	18.4	20.0	12.0	28.2
of which : Share issues	6.3	8.3	9.4	5.9	13.3

Sources : NAI, NBB.

[1] Credit institutions and institutional investors are excluded from the companies sector, because they are treated as pure financial intermediaries whose financial assets are identical to their financial liabilities.

TABLE 35 — ISSUES OF SHARES BY BELGIAN COMPANIES

(Millions of euro)

				First nine months	
	1996	1997	1998	1998	1999
Issues of listed shares	2,038	2,034	1,710	1,022	4,251
On the main market	1,917	1,801	1,569	886	4,174
On specialised markets [1]	121	232	141	136	77
Issues of unlisted shares	4,248	6,260	7,641	4,894	9,005
Risk capital [2]	180	191	417	n.	n.
Other issues	4,067	6,069	7,224	n.	n.
Total	6,286	8,294	9,351	5,916	13,257

Sources : BFC, BXS, European Venture Capital Association, NBB.
[1] EASDAQ and Euro-NM.
[2] Funds raised during the year by companies specialising in risk capital.

place outside the stock exchange. During the first nine months of the year, these private issues amounted to 9 billion euro, while the funds raised on the stock exchange totalled 4.3 billion. Of the latter sum, much larger than in the previous years, more than half is accounted for by a large capital increase made in January by a leading company in the financial sector.

In many respects, the markets for listed shares and for unlisted shares display very different characteristics. This is due not only to the method of trading, as the former can be traded on an organised market while the latter can only change hands by private treaty. Unlisted shares are generally issued by smaller, less well-known companies whose shareholders are mainly family members.

In order to stimulate economic growth and encourage the development of enterprises, it is however important to provide mechanisms which ensure a certain osmosis between these markets. Two processes can be used for this purpose.

The first is the introduction of securities on markets specialising in high-growth-potential companies, possibly as a preliminary to later entry into the main market. In Belgium there are two institutions offering this possibility. They are EASDAQ, a pan-European market established in Belgium as a counterpart to the American NASDAQ, and Euro-NM, an association initially created in collaboration between the Frankfurt, Paris, Amsterdam and Brussels stock exchanges.

Another method is to resort to professional investors which are willing to subscribe for issues of unlisted shares. This enables enterprises which are not sufficiently well known to envisage stock exchange listing immediately to obtain funds in amounts exceeding the personal assets of the entrepreneur or his environment. This system, known under the name of “venture capital”, is highly developed in the United States, but less so in Europe. In October 1999, in order to encourage this form of financing, the EC adopted an action plan designed to encourage Member States to persevere in their efforts in the field of venture capital.

The recent creation, in Belgium, of contact networks should permit a better segmentation of the market. These networks are intended to serve as bridges between, on the one hand,

TABLE 36 — BREAKDOWN OF FINANCING OF ENTERPRISES WITH RISK CAPITAL [1]

(Percentage of total financing in the form of risk capital, average 1993-1998)

	Belgium	Europe [2]
According to type of investor		
Independent funds	11.1	50.8
Captive or semi-captive companies	38.1	44.2
Public sector	50.8	4.9
Total	100.0	100.0
According to the development phase of the enterprise financed		
Creation	26.2	7.9
Expansion	58.2	36.7
Change in shareholdership	15.6	55.4
Total	100.0	100.0

Source: European Venture Capital Association.

[1] While the European Venture Capital Association tries to obtain the widest possible coverage, it is however not able to carry out an exhaustive census of the activity of investors in risk capital. A number of operators, especially among the smaller companies, are therefore not covered by these statistics.

[2] Corresponds to the fifteen countries of the EU excluding Luxembourg, plus Switzerland, Norway and Iceland.

businessmen whose financing requirements are smaller than the minimum amount of the holdings acquired by companies specialising in risk capital and, on the other hand, private investors who place at the disposal of new enterprises not only financial resources but also their professional experience.

The amounts invested in risk capital are still small, both in absolute terms and compared to the neighbouring countries. This situation is due to both supply and demand factors. Many entrepreneurs are reluctant to resort to this form of financing because doing so entails relinquishing part of the ownership of their company. Furthermore, the number of investors willing to make, directly or indirectly, investments in risk capital is still small. The relatively limited savings-gathering role played by life insurance companies and pension funds, in comparison with other countries, is an additional handicap.

In this context, the development of risk capital is still mainly based, in Belgium, on the public sector. During the years 1993 to 1998 the latter provided half of the financing in this form, against an average of barely 5 p.c. in the European countries. A reverse imbalance is observable for independent funds, which provided 50 p.c. of risk capital in Europe against 11 p.c. in Belgium. The market share of captive or semi-captive companies – which operate exclusively or partly on behalf of a parent company, which may be an industrial enterprise or a financial institution – is, on the other hand, fairly close to that recorded in the neighbouring countries.

The Belgian market in fact specialises chiefly in giving assistance for the creation and expansion of enterprises, to the detriment of financing of changes in shareholdership. In other words, the first stage of intervention of risk capital, which relies fairly considerably on public initiative, does not yet appear to be sufficiently followed up in a second intervention stage in the form of replacements of shares or financing of management buy-outs or management buy-ins. This situation might impede the actual development of the first stage, particularly in the form of private initiatives, by reducing the possibilities of further sales of shares, by preventing a faster turnover of participations in the portfolios of risk capital companies and by thus limiting the accumulation of experience in the assessment of new dossiers.

General government

During the first nine months of 1999 the deficit of general government amounted to 5.7 billion euro against 4.8 billion in 1998. The Treasury again gave preference to long-term financing instruments, the debt at over one year having increased by 7 billion. Net issues of Treasury certificates represented only 0.5 billion, while financial assets increased by 1.8 billion. This increase was due solely to the very short-term investment by the Treasury of part of the

TABLE 37 — FORMATION OF FINANCIAL ASSETS BY AND NEW FINANCIAL LIABILITIES OF GENERAL GOVERNMENT

(Billions of euro)

	1995	1996	1997	1998	First nine months 1998	First nine months 1999
Formation of financial assets[1]	−2.4	−4.8	−1.5	−1.7	−1.3	1.8
New financial liabilities	6.1	2.7	3.3	0.5	3.5	7.5
At up to one year	−16.9	−0.6	−0.1	−6.3	1.1	0.5
At over one year	23.0	3.2	3.4	6.7	2.4	7.0
Financial balance	−8.5	−7.4	−4.8	−2.2	−4.8	−5.7

Source : NBB.

[1] Including lending and equity investment.

proceeds from the September 1999 issue of a new line of six-year linear bonds. These operations were intended, in particular, to prefinance the redemption of Treasury certificates maturing in October.

The introduction of the euro had a double effect on the structure of the debt. The first was of an automatic nature. As a result of the conversion into euros of the loans previously denominated in the currencies of countries participating in EMU, the relative share of liabilities in foreign currencies was reduced from 6.2 to 3.3 p.c. The second effect was due more to an instant-reaction policy on the part of the government. The measures taken to diversify the distribution of public debt securities, which are described in detail in the part of section 8.2 dealing with the securities market, caused the share of linear bonds held by the rest of the world to rise from 8.1 p.c. in December 1998 to 21.6 p.c. in September 1999. This increase took place chiefly at the expense of credit institutions, which held only 49.5 p.c. of these securities in September

TABLE 38 — BREAKDOWN OF THE TREASURY'S DEBT BY HOLDER

(Percentages)

	Linear bonds			Treasury certificates		
	December 1996	December 1998	September 1999	December 1996	December 1998	September 1999
Belgium	87.4	91.9	78.4	67.8	56.5	55.7
of which :						
Credit institutions	59.9	61.6	49.5	50.5	41.2	43.9
Other holders	27.5	30.3	28.9	17.3	15.3	11.8
Rest of the world	12.6	8.1	21.6	32.2	43.5	44.3
of which :						
Euro area	n.	n.	12.9	n.	n.	28.5
Other countries	n.	n.	8.8	n.	n.	15.8
Total	100.0	100.0	100.0	100.0	100.0	100.0

Source : NBB.

1999 against 61.6 p.c. nine months earlier. The proportion of Treasury certificates held by foreign countries appears to have stabilised at the much higher level of about 44 p.c.

For a proper assessment of this change it should be noted that this breakdown of public securities by holder disregards the purely temporary changes of ownership due to repurchase agreements, since these serve as collateral for financing transactions and therefore do not fulfil an economic purpose of portfolio diversification.

Now, as will be seen in the part of section 8.2 devoted to credit institutions, repurchase agreements are an instrument frequently used by Belgian banks to obtain net resources in euro abroad on the interbank market. When these transactions relate to general government securities, they in fact offer the advantage of freeing the banks of the equity-capital-cover requirements applying to traditional interbank transactions. Although Belgian credit institutions can henceforth use for this purpose securities issued by both Belgian and foreign general government, they still for the most part use Belgian Treasury securities, as these still constitute the bulk of their portfolios.

A large proportion of the Belgian securities thus sold to foreign banks are allocated by the latter as cover for the credits which they obtain from their central banks. This circuit has the effect of removing from the market a volume of securities which is therefore no longer able to contribute to the liquidity of the secondary market.

Rest of the world

The entry into force of EMU had the effect of changing the conditions under which Belgium carries out its financial transactions with foreign countries. Previously, every investment made or loan contracted outside the BLEU was reflected, directly or indirectly, in a conversion of national currency into foreign currencies or vice versa. By changing the supply and demand conditions on the foreign exchange market, these transactions could therefore interfere with the exercise of a monetary policy whose primary aim was to preserve the stability of the value of the franc vis-à-vis the German mark. This constraint has now been eased, because Belgium forms part of a much wider monetary area which has not set itself a foreign exchange objective.

Although capital movements are therefore no longer a key variable for the conduct of monetary policy, an examination of them nevertheless makes it possible to understand how Belgium's transactions fit into the whole body of the financial markets of the euro area and the rest of the world.

An analysis of the recent transactions carried out with foreign countries reveals two circuits of funds. The former involves the monetary authorities, credit institutions and general government. During the first nine months of 1999 Belgian banks greatly diversified their assets by increasing their net positions on the rest of the world by over 21 billion euro. They financed these additional claims both by reducing their portfolios of Belgian public debt securities and by borrowing from the monetary authorities.

The Treasury thus turned more to foreign countries to obtain its finance, this having been reflected in capital inflows of 18.9 billion euro, contrasting with the outflows of 7.6 billion recorded for the whole of the year 1998. These two movements were not only in opposite directions but were also connected with transactions of very different kinds. Whereas in 1998 general government transactions with foreign countries had chiefly taken the form of redemptions of foreign currency debts, those carried out in 1999 were due to an active policy of international spreading of Belgian public debt securities in euro.

Since the start of the third stage of EMU, Belgian banks have the possibility of accumulat-

TABLE 39 — FINANCIAL BALANCE OF BELGIUM VIS-A-VIS THE REST OF THE WORLD BY COUNTERPARTY SECTOR [1]

(Billions of euro)

			First nine months	
	1997	1998	1998	1999
Monetary authorities	−0.5	2.0	3.1	−10.1
Credit institutions	2.1	−3.8	−4.0	21.1
General government	−2.3	7.6	3.0	−18.9
Institutional investors	6.4	14.4	12.0	5.9
Other sectors	4.8	−11.1	−8.2	8.4
Total	10.5	9.1	5.9	6.6

Source: NBB.
[1] A plus sign indicates a net capital outflow, a minus sign a net inflow.

ing claims on foreign countries by borrowing from the monetary authorities. Previously, the changes in the loans granted by the Bank to credit institutions were due to fluctuations in the deficit on the money market in francs only. This deficit was itself determined chiefly by the development of Belgium's note circulation and foreign exchange reserves.

This link with purely national variables has now disappeared. Belgian banks participate, together with those of the other countries, in the Eurosystem's allocations of credit by tender for meeting the liquidity requirements of the whole of the euro area. By participating actively in these transactions, resident institutions have been able to borrow, via the Bank, substantial amounts which have been partly redistributed in the rest of the area. These net acquisitions of external assets have given rise to transfers, via TARGET, by Belgian banks to other banks in the area, which have deposited the funds thus obtained in accounts with their respective central banks. Against this, the latter have in turn built up claims with the Bank. It is these transactions which explain the bulk of the capital inflows of 10.1 billion euro recorded during the first three quarters of 1999 by the Belgian monetary authorities.

The second circuit is due to the role played by institutional investors in households' investments abroad. The international diversification of the assets of individuals is not a new trend. Substantial capital outflows have been recorded in this form since the beginning of the 1980s. In an initial phase these transactions were carried out directly by households in the form either of deposits with foreign banks or of purchases of securities issued by non-residents. In a second stage the gradual institutionalisation of savings was coupled with a sharp growth in acquisitions of units issued by Luxembourg UCIs specialising in monetary assets or bonds.

The rise in stock market prices subsequently induced households to acquire units of UCIs investing directly or indirectly in shares. Unlike the others, these UCIs were usually set up in Belgium. Contrary to the system in force in Luxembourg, UCIs governed by Belgian law are subject to corporation tax, which enables them to benefit both from the imputation of the withholding tax on income from movable assets and from the provisions contained in international agreements aimed at preventing double taxation.

The increase in these subscriptions for units of UCIs whose yields are linked to stock market prices had been particularly sharp in 1998, having taken place mainly at the expense of direct investments abroad. These purchases therefore gave rise to repatriations of funds by households, which were offset by subsequent outflows from institutional investors when the latter used a large proportion of the funds raised to acquire securities issued by non-residents. The attractiveness of index UCIs and of UCIs specialising in shares decreased in 1999, so that the share of these institutions in capital movements declined, individuals having reverted to making direct investments abroad.

8.2 FINANCIAL MARKETS

Payment systems

In order to enable the financial markets of the euro area to function as efficiently as the national markets, new payment systems common to the whole of the EU were introduced at the beginning of 1999. The TARGET system thus came into operation, linking the fifteen national gross real-time settlement systems, including ELLIPS for Belgium. This system ensures risk-free and rapid execution of transfers in euro between the various member countries for all large-value payments.

In this connection mention should be made of the Belgian law of 28 April 1999 implementing the European directive of 19 May 1998 on the finality of the carrying out of settlements in payment systems and in securities transaction settlement systems. This law is thus aimed at safeguarding the proper operation of payment and securities settlement systems, including collateral for securities, against the adverse effects of insolvency proceedings opened against Belgian or foreign participants in these systems.

By contrast, the progress made in connection with small payments has been slower. These are still usually made via networks of correspondent banks, resulting in longer execution periods and higher transaction costs. The introduction, in 2002, of euro notes and coins, which will make it possible to carry out cross-border cash payments free of charge does, however, require the parallel creation of flexible and inexpensive mechanisms for small-value bank transactions between the various countries of the euro area. In order to encourage the development of such systems, the ECB published in September a notice listing a series of objectives which must be achieved not later than 1 January 2002.

This document recommends that priority be given to bank transfers, especially in view of their importance for the remote execution of small-value cross-border payments. The times taken for these transactions should become comparable to those for domestic bank transfers, while their cost should be substantially reduced and borne exclusively, unless otherwise agreed in advance, by the initiator of the transaction. The participation of individual credit institutions in cross-border small-value payment systems should be facilitated by the application of objective and non-discriminatory access criteria. Lastly, the standardised norms already defined by the European Committee for Bank Norms should enter into force as soon as possible.

The great attention paid by the ESCB to payment systems is not however solely attributable to the desire to ensure integration of the money market of the euro area and a smooth transition to the single currency. It springs from a more fundamental concern, common to all central banks, to contribute to the security and stability of the entire financial system and to maintain public confidence in the currency. Secure and efficient payment systems are essential, not only in order to ensure rapid and transparent transmission of the impulses of monetary policy but also in order to contain one of the greatest potential sources of systemic risk. The object is to prevent the breakdown of a payment system or default by a participant in such system from leading, by a contagion affect, to the disruption of all financial markets. The central banks are directly involved when such crises break out, since they are then called upon to intervene as lender of last resort for credit institutions.

The crucial and fundamental role of payment systems in maintaining the stability of the financial markets and confidence in the currency has long been recognised. It has induced the central banks both to design and operate such systems themselves and, more generally, to exercise oversight over the mechanisms which they do not organise themselves.

The promotion of the proper operation of payment systems was explicitly incorporated in the fundamental tasks of the ESCB and formulated in its statutes. In Belgium, the law of 22 February 1998 establishing the Organic Statute of the Bank stipulates in its Article 8, that "the Bank shall ensure that the clearing and payment systems operate properly and shall make certain that they are efficient and sound. It may carry out all transactions or provide facilities for this purpose. It shall implement the regulation adopted by the ECB in order to ensure the efficiency and soundness of the clearing and payment systems within the European Community and with non-member countries". It is clear from the explanatory statement that this power has a dual-scope, as the Bank is made responsible for supervising both payment systems and securities clearing systems. For payment systems, the general policy guidelines are laid down within the ESCB in consultation with all the national central banks, while the concrete implementation of the surveillance functions is delegated to each central bank.

In the performance of its task, the Bank can also derive support from the work done by the G10 central banks, especially within the Committee on Payment and Settlement Systems. In particular, this committee laid down, in 1990, general norms, the so-called "Lamfalussy norms", and in December 1999 it published a document on the fundamental principles of payment systems.

The Bank's functions include that of monitoring the application of these norms by the various payment and settlement systems operating in Belgium. One principle, however, is very widely recognised at international level : the supervision must not on any account give rise to the granting of a certification, approval or authorisation to the systems in question. The operators themselves must bear the primary responsibility for the security and efficiency of the existing structures.

This activity is less akin to the role of supervisory authority than to that of a body giving advice and making recommendations. This means that those responsible for the systems subject to supervision by the Bank must consult and inform the latter about any important question. The Bank, for its part, will gather all information which it deems useful and will, if necessary, submit proposals for changes designed to improve the reliability of the existing systems.

In Belgium the Bank manages, in agreement with the participants, a number of systems, namely ELLIPS for real-time large value payments, the CEC and the Clearing House for small payments. It also itself operates the Clearing System, which is chiefly used for the delivery, against payment, of dematerialised public securities. It furthermore maintains operational relations with most of the systems under its supervision. In order to avoid any conflicts of interests, a strict separation has been established between these operational activities and the surveillance function.

In addition to the above-mentioned systems, the Bank's supervision relates chiefly to Euroclear, Banksys (especially Proton) and SWIFT. In the last-mentioned case it takes place within the framework of an international co-operation association with the G10's Committee on Payment and Settlement Systems, in which the Bank acts as lead overseer with the support of a number of central banks represented on this committee. In 2000 the Bank will start to supervise the other systems established in Belgium, such as Europay, BXS-Clearing and BXS-CIK. Lastly, the bank is also involved in the supervision of international systems, such as Euro 1 Clearing, managed by the EBA Clearing Company, which was created by the Banking Association for the Euro, and the proposed CLS Banksystem. Their lead overseers are, respectively, the ECB and the Federal Reserve of New York, with the Bank helping to perform these international tasks in its capacity as the central bank of a country in which credit institutions participating in these systems are located.

The Bank also maintains relations with the BFC in the exercise of its supervisory functions. However, each of these two institutions has a specific role to play. Briefly, oversight relates mainly to the systems and the prudential supervision applies to the individual institutions.

There is a long tradition of informal co-operation between the Bank and the BFC. This co-operation will of course be maintained in the context of the activities relating to institutions or systems, such as BXS Clearing, in relation to which both the BFC and the Bank have legally authorised tasks to perform. The purpose of this approach is to avoid any duplication or inadequacy in the performance of the respective tasks of the Bank and the BFC.

Credit institutions and other financial intermediaries

As the banks are at the heart of the payment system, it was in the specific functions which they perform in this field, particularly via the interbank market, that they were most directly affected by the introduction of the single currency.

The most immediate effect was the increase in the volume of interbank transactions carried out

TABLE 40 — INTERBANK TRANSACTIONS OF BELGIAN CREDIT INSTITUTIONS

(End-of-period outstanding amounts on a territorial basis, billions of euro)

	December 1998			September 1999		
	In francs	In foreign currencies	Total	In euro	In foreign currencies	Total
Interbank assets						
Monetary authorities	7.2	–	7.2	5.3	–	5.3
Credit institutions	64.5	138.1	202.6	135.1	64.4	199.6
Claims resulting from repurchase agreements [1]	42.6	8.7	51.3	61.3	3.4	64.7
Other claims	21.8	129.4	151.2	73.9	61.0	134.9
Total	71.6	138.1	209.7	140.4	64.4	204.8
Interbank liabilities						
Monetary authorities	4.0	–	4.0	10.3	–	10.3
Credit institutions	77.0	165.8	242.8	174.5	88.4	262.9
Debts resulting from repurchase agreements [1]	54.8	16.1	70.9	104.2	2.6	106.8
Other claims	22.2	149.7	171.9	70.3	85.8	156.1
Total	81.0	165.8	246.8	184.8	88.4	273.2
Interbank balance	−9.4	−27.7	−37.1	−44.4	−24.0	−68.4

Source: NBB.
[1] Including advances against collateral.

in the national currency. Whereas in December 1998 interbank assets and liabilities in francs represented euro equivalents of 72 and 81 billion respectively, in September 1999 interbank franc assets and liabilities amounted respectively, to 140 and 185 billion euro. This increase was largely counterbalanced by the fall in transactions in other currencies.

Furthermore, the net position of Belgian banks vis-à-vis the monetary authorities was reversed. At the end of 1998 credit institutions held with the Bank, mainly in monetary reserve accounts, assets equivalent to 7.2 billion euro, whereas the outstanding amount of their borrowings was only 4 billion. At the end of September 1999, total recourse to credit from the ESCB amounted to 10.3 billion euro, while balances on accounts totalled only 5.3 billion.

The instruments used on the interbank market in euro will gradually change. Like the development which was observed in Belgium following the money market reform of 1991, the technique of repurchase agreements should spread all over the euro area. A growth in recourse to this instrument was actually observed in Belgium during the first months of EMU. However, this increase has up to the present taken place more in liabilities, i.e. the Belgian banks' borrowings, than in assets, which consist of the liabilities of foreign institutions. The fact is that credit institutions can mobilise prime assets very easily in support of their borrowings, because they hold a substantial portfolio of Belgian public securities. Furthermore, the asymmetrical movement of the use of repurchase agreements might also be due to the Belgian banks' greater familiarity with this technique, which was already a major instrument of the former interbank market in francs.

At the end of September 1999 the outstanding amount of securities lodged as collateral by Belgian banks to cover their interbank transactions in euro was 104 billion. If the amount of the securities deposited with the NBB to cover both monetary policy transactions and the operation of the TARGET gross settlement system is added, the securities pledged by the Belgian banks represented about 70 p.c. of the total outstanding amount of their portfolios of securities in euros. At the same time the Belgian credit institutions were themselves benefiting, to the extent of 61 billion, by similar collateral guaranteeing a large proportion of their loans on the interbank market.

The payment systems and securities settlement systems are thus closely interconnected, which fully justified the aforementioned principle of making the central banks responsible for the simultaneous supervision of these two structures. In order to facilitate pledging transactions, the Bank's securities clearing system was altered by the adoption of a gross settlement method instead of settlement by offsetting. Furthermore, the Bank participated in the implementation, throughout the ESCB, of the so called "correspondent central bank" model. This system permits cross-border use of collateral by enabling the various credit institutions in the euro area to obtain a loan from their central bank of origin in exchange for collateral held with other central banks.

Belgian banks showed a net deficit, on the interbank market, of 68.4 billion euro at the end of September 1999, against 37.1 billion at the end of December 1998. This expansion had as its counterpart an increase in the amount by which their assets vis-à-vis the other sectors exceeded the corresponding liabilities. During the first three quarters of 1999 the latter declined by 1.2 p.c. whereas their assets rose by 7.6 p.c. The last-mentioned percentage is due however, to widely differing changes for the various sectors. Belgian banks reduced their portfolio of Treasury debt certificates, their claims on general government having fallen by 6.8 p.c. This reduction was coupled with an increase in lending to individuals and companies, but was chiefly counterbalanced by an upsurge in purchases of paper issued by the rest of the world, especially

TABLE 41 — BALANCE SHEET STRUCTURE OF BELGIAN CREDIT INSTITUTIONS

(End-of-period outstanding amounts on a territorial basis, billions of euro)

	Asset			Liabilities		
	December 1998	September 1999	Percentage change	December 1998	September 1999	Percentage change
Belgian and foreign credit institutions	209.7	204.8	−2.3	246.8	273.2	+10.7
Other sectors	382.4	411.7	+7.6	386.5	381.7	−1.2
Individuals and companies	169.4	176.6	+4.3	315.6	306.3	−2.9
General government	150.3	140.0	−6.8	3.8	7.0	+86.1
Rest of the world	62.8	95.1	+51.5	67.1	68.4	+1.8
Miscellaneous [1]	–	–	–	−41.1	−38.4	−6.6
Total	592.1	616.5	+4.1	592.1	616.5	+4.1

Source : NBB.

[1] These miscellaneous items, shown net, correspond to non-attributable items, adjustments and valuation differences, especially those between the market value and the book value of credit institutions' equity capital.

foreign general government authorities, as claims on non-resident clients increased by over 50 p.c.

The increase in the profitability of Belgian credit institutions, which was interrupted in 1998, was resumed in 1999. During the first nine months of the year the yield on equity capital reached, on an annual basis, 12.3 p.c. against 11.4 p.c. for the corresponding months of 1998, which points to an increase for the year as a whole. It should be noted that profitability is generally higher during the year than at the end of the year, when equity capital increases as a result of the placing to reserve of undistributed profits.

The increase was proportionally even greater for the return on assets, which rose, from the one period to the other, from 0.35 to 0.41 p.c. This growth was only partly reflected in the return on capital, as the Belgian banks took less advan- tage of the leverage effect. The ratio between

TABLE 42 — PROFITABILITY AND SOLVENCY OF CREDIT INSTITUTIONS GOVERNED BY BELGIAN LAW

(Data on a company basis)

					First nine months [1]	
	1995	1996	1997	1998	1998	1999
Return on equity [2]	8.37	10.38	10.88	9.62	11.40	12.30
Return on assets [2]	0.24	0.29	0.30	0.30	0.35	0.41
Financial leverage [3]	34.3	35.2	35.9	32.0	32.7	30.3
Cover coefficient of assets weighted by risks [4]	11.9	11.7	11.4	11.3	11.4	10.5

Sources : BFC, NBB.

[1] Data on annual basis.

[2] Percentage yield after tax.

[3] Ratio between total assets and equity.

[4] Consolidated end-of-period data.

total assets and equity in fact declined from 32.7 to 30.3.

This greater capitalisation was not coupled with a rise in the coverage coefficient of assets weighted by risks, or risk asset ratio, because the above-mentioned changes in the balance sheet structure were reflected in an increase in claims on private clients, who are given a weighting coefficient of 100 p.c., at the expense of interbank assets or public securities, which are given a small or zero coefficient.

The growth in bank incomes is attributable to interest earnings. Whereas their share in total bank earnings had fallen by about 11 percentage points between 1995 and 1998, it appears to have increased during the first nine months of 1999, reaching 60.9 p.c. of the total against 56.7 p.c. the previous year.

Like the movement already observed in 1998, the interest margin calculated as the difference between the yield on assets and the cost of liabilities, increased, reaching 1.28 p.c. during the first nine months of 1999. As stated above, claims on non-bank customers, which are proportionally more profitable, grew as a share of the banks' balance sheet, at the expense of transactions on the interbank market. On top of this structure effect there was a widening of the interest margin on the latter category of transactions. In fact, the negative differential usually shown by Belgian banks on the interbank market disappeared in 1998 and was replaced by a positive difference of 0.05 p.c. during the first nine months of 1999. The possibility, for Belgian banks, henceforth to carry out a larger proportion of interbank transactions in their own currency, together with the availability of a substantial outstanding amount of public securities which could easily be used as collateral, may well have made it possible to reduce the cost of interbank borrowings abroad.

By contrast, the margin on transactions with customers, which is the main component of interest results, shrank further. Whereas it amounted to 2.30 p.c. in 1996, it reached only 1.98 p.c. during the first three quarters of 1999. This fall took place despite an increase in maturity transformation activity. The share of liabilities

TABLE 43 — INTEREST RESULTS OF BELGIAN CREDIT INSTITUTIONS

(Data on a company basis, percentages)

	1995	1996	1997	1998	First nine months[1] 1998	First nine months[1] 1999
Share of interest results in bank earnings	67.8	65.5	62.5	56.6	56.7	60.9
Overall interest margin[2]	1.29	1.31	1.17	1.22	1.22	1.28
of which:						
Margin on interbank transactions[2]	–0.13	–0.26	–0.15	0.02	–0.01	0.05
Margin on transactions with clients[2]	2.20	2.30	2.06	2.02	2.01	1.98
p.m. Share of claims at over one year in claims on clients[3 4]	*60.3*	*61.2*	*62.1*	*61.9*	*61.7*	*63.3*
Share of liabilities at up to one year in liabilities to clients[3]	*64.8*	*65.8*	*68.4*	*69.8*	*70.7*	*72.0*

Source: NBB.

[1] Data on annual basis.

[2] Calculated as the difference between the yield on assets and the cost of liabilities.

[3] According to term on issue.

[4] Excluding variable-rate advances for terms over one year.

at up to one year in the resources collected from customers rose from 65 p.c. at the end of 1995 to 72 p.c. at the end of September 1999, chiefly owing to the loss of attractiveness of bank bonds. At the same time, the proportion of assets represented by claims at over one year reached 63 p.c. at the end of September 1999, against 60 p.c. at the end of 1995, owing, on the one hand, to the sharp increase in mortgage loans and, on the other hand, to a growth in the proportion of long-term securities in the securities portfolio.

These maturity transformations enabled the Belgian banks to generate substantial incomes in a context where the differential between long-term and short-term rates remained substantially positive and even tended to increase during the last few months. Credit institutions were therefore able to compensate partly for the narrowing of margins due to the keen competition on the financial markets. They also, however, became more vulnerable to sudden changes in the yield curve.

As the other components of bank incomes declined overall, the relative weight of interest incomes increased during the first three quarters of 1999. This development must however be placed in its proper context. On the one hand, the decrease in total income excluding interest is mainly attributable to the results of securities trading. Owing to the rise in long-term rates, several banks suffered losses on this category of transactions, as had in fact also been the case during the previous upward movement in 1994. On the other hand, during each of the four preceding years, incomes excluding interest had shown a very high growth rate, far above that of interest results.

The increase in recent years in activities other than intermediation has spread to most other types of transactions. Three sources of income have however grown more markedly, namely commission on securities transactions and asset management, income from shares and equity and results on realisation of securities.

The rates of increase have not however been identical for all three categories. The increase in equity income is recent and is largely attributable to the various acquisition operations which have recently taken place within the Belgian banking sector.

TABLE 44 — RESULTS EXCLUDING INTEREST OF BELGIAN CREDIT INSTITUTIONS

(Data on a company basis, millions of euro)

	1995	1996	1997	1998	First nine months[1] 1999
Commission on securities transactions and asset management	596	797	1,046	1,500	1,725
Income from shares and equity investment	460	735	519	570	1,044
Result on realisation of securities	798	816	1,155	1,970	1,453
Result of securities trading activity	481	451	323	369	−717
Other commission and income excluding interest, net of commission paid	1,276	1,480	1,779	2,070	2,167
Total income excluding interest	3,610	4,280	4,821	6,480	5,672
Ditto as annual percentage increase	+39.8	+18.6	+12.7	+34.4	−12.5

Source: NBB.

[1] Data on an annual basis.

Results on realisation of securities increased mainly in 1998, but remained very high during the first three quarters of 1999. Credit institutions actually hold a substantial portfolio of securities which were issued several years ago at rates far above the conditions currently in force and on which they therefore acquire latent capital gains. By selling part of these securities they can realise these gains. Such transactions do however have an adverse effect on the future development of the intermediation margin, because the financial resources thus generated have to be reinvested at lower rates.

The steadiest growth has been that in commission on securities transactions and asset management. This nearly tripled between 1995 and 1999. The rise in stock market prices encouraged the issuing and placement of securities. It also stimulated the interest of investors in variable-interest securities. The banks were thus able to step up their portfolio management activities on behalf of third parties, and also the distribution of units of UCIs.

The tapping of these new income sources is helping to change the risk profile of credit institutions. Responding to this, these have endeavoured to adjust their cover instruments and management systems. In the light of this dual development, it became clearly apparent that the international requirements as regards solvency needed to be changed. In June 1999 the Basle Committee on Bank Supervision, which has been working for several years on a revision of the Capital Accord, disseminated for consultation a document presenting the results already achieved.

The Committee's proposal does not confine itself to the minimum solvency requirements. It is also based on two other major pillars. Firstly, it aims to introduce a permanent process of prudential assessment of the equity requirements for each individual institution. Secondly, it emphasises the idea that the transparency of the information published by the various institutions is an essential instrument for improving market discipline and facilitating bank supervision.

The solvency coefficients should cover a wider range of risks than hitherto, because they would henceforth apply also to the interest rate risks run in transactions with customers and to the

TABLE 45 — RESOURCES GATHERED BY FINANCIAL INTERMEDIARIES FROM NON-BANK CUSTOMERS

(Changes, billions of euro)

					First nine months	
	1995	1996	1997	1998	1998	1999
Credit institutions [1]	8.4	20.0	16.3	11.4	12.7	8.8
Institutional investors [2]	6.4	11.1	17.6	28.6	23.9	20.2
Undertakings for collective investment	0.3	4.6	9.1	19.3	16.9	12.2
In fixed-interest assets	0.8	1.3	2.0	1.9	1.8	0.8
Guaranteed-capital and share indices	–0.1	2.6	6.0	12.2	11.5	7.3
Pension saving, mixed and miscellaneous	–0.3	0.8	1.1	5.3	3.6	4.1
Insurance companies	5.6	5.9	7.9	8.8	6.9	8.0
Pension funds	0.5	0.6	0.5	0.5		
Total	14.8	31.1	33.9	40.0	36.6	29.1

Sources: BFC, ISO, Belgian Association of UCIs, Belgian Association of Pension Funds, Luxembourg Insurance Commissariat, NBB.
[1] Belgian credit institutions, on a territorial basis.
[2] Institutional investors operating on the Belgian market.

operational, legal and reputation risks. Although the rules now in force for market risks are not to be significantly changed, a more detailed breakdown of the weighting categories is being considered for credit risks. This classification would be based on the ratings assigned by independent agencies, but the Committee could, under certain conditions, allow recourse to the internal ratings which the banks themselves assign to their counterparties.

Measured by the volume of funds raised from their non-bank customers, the activity of institutional investors fell off slightly during the first nine months of 1999. This movement represented a reversal compared with the trend during the preceding years. The sharp rises recorded on most stock markets had stimulated investment with UCIs, especially those whose yields are linked with the movement of stock market prices. This interest lessened during the first three quarters of the year under review, the funds raised by guaranteed-capital index UCIs or those specialising in shares having fallen from 11.5 billion euros in 1998 to 7.3 billion in 1999.

Despite this decline, it must not be forgotten that several structural factors will continue to exert a favourable influence on investments with institutional investors during the next few years. A growing number of persons are building up savings intended to supplement the legal pension system. Furthermore, in a context where the mastering of inflation has pushed down interest rates, investors are trying to obtain high yields by investing in higher-risk assets. The increased recourse to institutional investors forms part of this diversification strategy.

In so far as these undertakings pursue an active risk-spreading policy, the structure of their portfolios will be influenced by EMU, since the introduction of the euro reduces the range of currencies among which institutional investors can spread their assets. Whereas at the end of 1998 36 p.c. of the assets of these investors were in foreign currencies, this proportion fell to about 16 p.c. as a result of the creation of the single currency.

TABLE 46 — ASSET STRUCTURE OF INSTITUTIONAL INVESTORS

(End-of-period outstanding amounts, percentages)

	December 1998	September 1999
By currency		
In francs	64.0	–
In euro	–	83.6
In other currencies	36.0	16.4
By counterparty		
On Belgium	58.8	56.1
Financial intermediaries	12.5	10.8
General government	24.6	23.8
Other sectors	21.8	21.5
On the rest of the world	41.2	43.9
Financial intermediaries	7.0	9.0
Other sectors	34.2	34.9

Sources : BFC, ISO, Belgian Association of UCIs, Belgian Association of Pension Funds, Luxembourg Insurance Commissariat, NBB.

Institutional investors thus have to look for other methods of diversification, especially by increasing their claims on the rest of the world. Although the available data in this field are still very fragmentary, especially in the case of insurance companies and pension funds, the share of foreign assets appears to have risen, during the first nine months of 1999, from 41.2 to 43.9 p.c.

Two important legal measures also influenced the activity of these institutions during the year. On 30 April 1999 a Royal Decree lowered the maximum reference rate for life insurance transactions from 4.75 to 3.75 p.c. and the discount rate for calculating the minimum financing of collective capitalisation for group insurances from 7 to 6 p.c. Two other Royal Decrees extended these provisions to pension funds. In making these adjustments the government took account of the repercussions, on the conditions of activity of these institutional investors, of the fall in interest rates which had taken place in recent years owing to the slowing of inflation.

A Royal Decree of 7 July 1999 defined the criteria determining the public nature of the financial transactions, which are applicable particularly to UCIs, to seeking to obtain deposits or other repayable funds, to issuing operations and to operations deemed to be equivalent to a public issue. By this provision the government defined the concept of investors who, as they do not specialise in financial matters, should have the benefit of specific protective measures. The more precise definition of the parameters enabling a distinction to be made between professional operators and other investors will give the banks and other financial intermediaries greater legal security in the exercise of their functions of asset management, investment consultancy and the organisation of security issues.

Securities markets

The gradual substitution of companies for general government as the main borrowers on the Belgian securities markets became more pronounced in 1999. Although net issues of linear bonds and Treasury certificates by general government still represented a substantial volume during the first nine months, namely 8.6 billion, this amount is influenced by the September issue of linear bonds intended to prefinance the redemption of Treasury certificates in the following month, but still more so by seasonal factors. The Treasury's financing requirements are concentrated in the first three quarters, so that the deficit and hence the volume of new issues declined, over the year as a whole, to an appreciably lower level.

Capital increases by companies via the stock exchange amounted in the first nine months of the year to 4.3 billion euro, against 2.2 billion in 1998. In addition, companies raised 7.3 billion by issuing fixed-interest securities, especially short-term ones on foreign markets. Although the introduction of the euro was coupled with a substantial increase in issues of that type, the total outstanding amount of these securities in circulation is still much smaller than that of securities issued by general government and of listed shares.

Owing to their size, it is the two last-mentioned markets that are most directly affected by the introduction of the euro. The challenges are much the same in both cases. On the demand

TABLE 47 — NET ISSUES OF SECURITIES ON THE MAIN BELGIAN SECURITIES MARKETS

(Billions of euro)

				First nine months		p.m. Outstanding amount at the end of September 1999
	1996	1997	1998	1998	1999	
Securities issued by general government [1]	9.3	6.3	1.7	4.7	8.6	250.6
Treasury certificates	5.7	1.0	−5.6	1.7	0.9	40.6
Bonds	3.6	5.3	7.3	2.9	7.7	209.9
Listed shares	2.5	2.2	2.9	2.2	4.3	172.7
Fixed-interest securities issued by companies	1.4	0.1	0.6	1.3	7.3	25.9
Total	13.2	8.5	5.3	8.1	20.1	449.2

Sources: BFC, BXS, EASDAQ, NBB.

[1] Including Treasury bills as well as commercial paper issued by the communities and regions.

side, investors now have a much greater range of choice because EMU permits wide geographical diversification without any exchange risk. The supply conditions are also influenced, since issuers, keen to obtain the best financing terms, are turning more to foreign countries in order to derive the greatest advantage from competition. Technological innovations assist this dual development by facilitating relocation of markets, opening up new possibilities for electronic trading or allowing the centralisation of clearing and settlement functions in supranational bodies.

Although they are faced with comparable developments, these two market compartments still have their own distinctive features.

Public debt securities generally display a high degree of homogeneity from country to country, which makes it easy to compare the financing conditions applying to Belgium with those of the other countries of the euro area. Furthermore, the bulk of issues are made by a single borrower, the Treasury, which can thus react quickly to the new market situation.

The Belgian Treasury made several adjustments during the year under review which are in line with provisions already introduced in previous years. Thus, the diversification of the securities offered was continued. After having extended the maturity range of linear bonds in 1998 by making issues with maturities of up to thirty years and launching the first Treasury bills, in the form of commercial paper at up to one year, the federal government issued a new line of floating-rate linear bonds in April 1999. This instrument, the rate on which is linked to that on three-month interbank deposits in euro (Euribor), was the first issue of this type made in euro by a sovereign borrower.

The initial tranche of this linear bond line, like that of the two fixed-rate linear bond lines launched in 1999, was placed by an international syndicate of financial institutions, while the following tranches were placed by the traditional method of tendering. This adjustment of the issue procedures is aimed at increasing the liquidity of these securities by ensuring from the outset that the resultant volume of securities in circulation is comparable with the outstanding amount of those issued by general government in the largest countries of the euro area. This new technique is also intended to attract more foreign investors.

In order to promote the placing of its debt with non-resident investors, the Treasury also accredited several primary dealers established abroad. While offering better access to an international clientele, these made it possible to counterbalance the reduction in the number of Belgian primary dealers resulting from the restructurings in the domestic banking sector. Furthermore, a new category of market operators, the “recognised dealers”, was created at the beginning of 1999. While, unlike the primary dealers, they are not required to comply with the binding norms in terms of volume of activity on the primary and secondary markets, the recognised dealers have the task of placing the securities of the Belgian public debt abroad, on certain markets and with certain targeted investors.

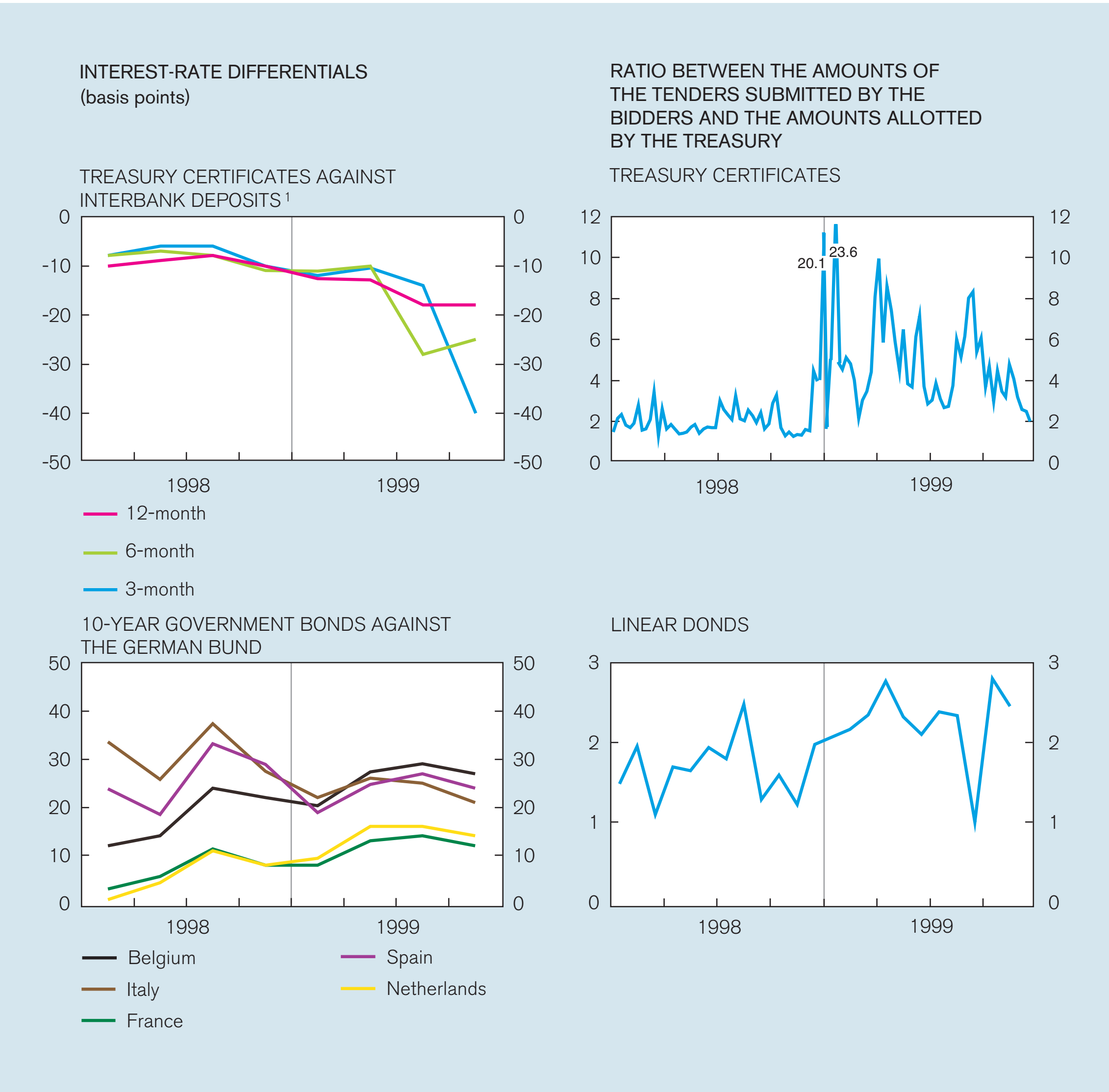
In return for their specific commitments, these two bodies of specialists in Belgian Treasury securities are henceforth the only ones permitted to deal on the primary market, while only the primary dealers are authorised to participate in non-competitive tenders.

The Treasury also continued its policy of regrouping maturities. The interest payments on linear bonds are henceforth concentrated on two due dates, 28 March and 28 September. Treasury certificates, while still being issued weekly, now have only two maturity dates per month, an arrangement which also helps to increase the volume of the lines.

Lastly, the Treasury wished to take advantage of the process of integration of the secondary markets started, within the euro area, by the creation of EuroMTS. This entirely electronic market, operating in real time and still confined to a limited number of operators, opened in April 1999, trading initially in the most liquid loans of Germany, France and Italy. In September Belgium, together with Spain and the Netherlands, was able to benefit by a widening of this market by introducing three linear bond lines which complied with the double criterion of having been recently created and having a substantial volume in circulation. On the national plane the Treasury and the primary dealers agreed to use the same software as that of EuroMTS in order to establish, in 2000, an electronic trading platform, called MTS Belgium, for dematerialised securities of the Belgian public debt.

The lines of action pursued by the Treasury in order to attract more foreign investors did not have identical results for the short-term and long-term debt. On the money market, the nega-

CHART 52 — FINANCING CONDITIONS OF THE BELGIAN PUBLIC DEBT



Sources : Ministry of Finance, NBB.

[1] Rate on interbank deposits in francs (Bibor) until 1998; rates on interbank deposits in euro (Euribor) in 1999.

tive interest rate differential between Treasury certificates and interbank deposits in francs and, since January 1999, in euro, increased during the last two years. The average differential for three-, six- and twelve-month instruments rose from 8 basis points during the first three quarters of 1998 to 11 basis points during the following three quarters. The differential widened further during the second half of 1999, reaching, in the fourth quarter, 18 basis points for the twelve-month certificates, 25 basis points for the six-month certificates and as much as 40 basis points for the three-month securities. This widening of the differential was however largely due to the impending changeover to the year 2000. Credit institutions, keen to have the best possible liquidity at the end of the year, chose to buy Treasury certificates, which are easily mobilisable in the form of repurchase agreements.

On the bond markets, the differential between the ten-year linear bond and the German bund of the same duration, which serves as the benchmark on this market, increased somewhat in 1999. This movement was not however specific to Belgian public securities, as a similar widening was recorded for the long-term public debt of other euro area countries.

This difference between the two markets is also reflected in the increase in the ratio between the amounts of the bids made by the tenderers and the amounts actually allotted by the Treasury. This ratio rose from an average of 2.4 in 1998 to 5 in 1999 for Treasury certificates, but went up only from 1.7 to 2.3 for linear bonds.

The reasons for this divergence are to be found in the two major differentiation factors still existing between the markets for public securities of the member countries of EMU, namely the credit risk and liquidity. These two criteria are hardly discriminatory for Treasury certificates. All the Member States of the euro area do in fact enjoy the highest rating for their short-term debt in euro, while the uniformisation of the money market and the spread of repos within the area means that liquidity differences are now practically without significance for short-term public securities. Furthermore, the Belgian government has a certain advantage in this segment because several countries in the area, especially Germany, issue hardly any short-term public securities.

On the other hand, on the bond markets there are appreciable interest rate differentials between the securities of the various countries. Thus, German ten-year bunds are at a premium compared to the benchmark loans of all the other countries in the area. This differential exists even vis-à-vis the countries which have the same rating as Germany, a fact which highlights the important role played by liquidity. Liquidity influences, in particular, the yields for the ten-year maturities, because the German Treasury certificates of this duration are the basis of the transactions carried on Eurex, which is by far the main futures market for bonds in euro. On the other maturities the interest rate differentials with Germany are generally smaller.

On the stock market, the challenges presented by the single currency were one of the main justifications for the far-reaching reform introduced by the law of 10 March 1999. This law made it possible to combine, in an integrated structure, the Brussels Stock Exchange Company, the Belgian derivatives market (Belfox) and the Securities Deposit and Clearing Office of the Financial Sector.

An overarching company was created, under the trade name of Brussels Exchanges or BXS. This groups the stock markets together and has two subsidiaries, BXS-Clearing, which serves as a clearing body, and BXS-CIK, which is responsible for the safe guarding and settlement of transactions for shares and warrants. The new structure thus brings together all the functions connected with stock exchange transactions, except for the settlement of transactions in fixed-yield securities, which takes place via the Bank's clearing system. It is also responsible for the organisation and supervision of the market and for the dissemination of information. It has a managing committee responsible for implementing the strategy decided upon by the board of directors, a market authority and disciplinary commission. The legislator has given BXS the legal form of a public limited liability company, which makes it possible to safeguard this institution against the risks of a change in equity inherent in a co-operative structure while at the same time offering the possibility of subsequently opening up the shareholdership to third parties, or even of stock exchange listing.

The authorities also took two other more specific measures in order to diversify the securities traded on the Brussels Stock Exchange. On 6 July 1999 they amended the Royal Decree concerning the prospectus to be published when a public securities issue is made. The aim of this measure is to simplify the introduction, on a Belgian secondary market, of securities already listed on a foreign market, by specifying the conditions to be met in order to be exempted from publishing a prospectus.

In addition, the Brussels Stock Exchange, by virtue of an authorisation granted by a Royal Decree of 9 June 1999, launched a new financial instrument called "Index Participating Units" or IPUs, in December 1999. This product, intended mainly for individuals, but also accessible to institutional investors, consists of an option on the Bel20 index enabling the purchaser to acquire part of the value of the basket of securities underlying this index. In practice, the acquisition price of the IPU is at all times equal to the market price of this basket portion, since the price of exercise of the option is zero and the investor is entitled to receive amounts proportionally equivalent to the dividends on the shares which compose the index. The Brussels Stock Exchange is the first European financial centre to offer this type of product.

These various measures, especially the creation of BXS, are designed to enable the Brussels Stock Exchange firstly to contend with the potential competition from new, entirely electronic, cross-border trading systems and, secondly to fit itself better for some of the alliances currently being studied between the major European stock exchange centres. The Brussels, Amsterdam and Luxembourg stock exchanges have already actually moved closer together, as each of the members of these three stock exchanges have been able, since the beginning of 1999, to intervene without an intermediary and without additional cost in the two other exchanges. Other projects are being prepared, such as the interconnection of the trading platforms of the main European stock exchanges or the possible creation of a pan-European clearing and settlement delivery structure. These various projects are aimed at, among other things, meeting the potential competition from non-stock-market operators.

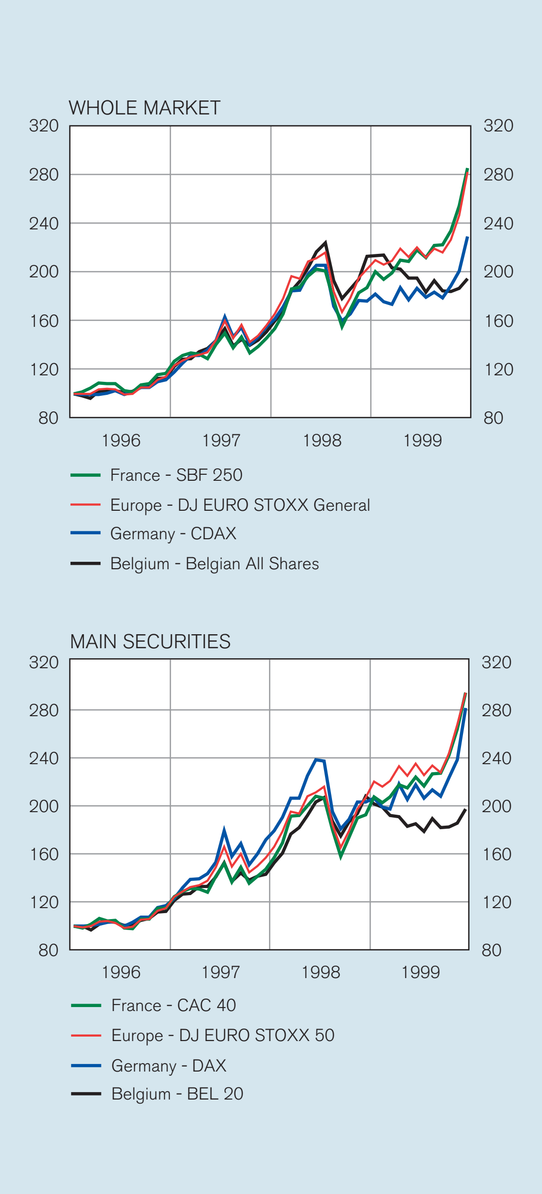
The numerous remaining obstacles to the process of regrouping the various stock exchanges in Europe are not only due to operational or technical difficulties. They are also connected with the specific features of these markets, which, compared to the markets for public debt securities, are far from being standardised. This situation is due to the nature of the securities, which represent risk capital, to the great fragmentation of issuers each with their own characteristics and also to the absence of harmonisation of accounting layouts or tax systems.

Despite these national differences, the Brussels Stock Exchange developed in close correlation with the other main European centres during the period preceding the entry into force of the euro. Thus, from the beginning of 1996 to the autumn of 1998, the Belgian, German and French indices showed very similar fluctuations and also ran in line with the pattern of the Euro Stoxx index. This parallelism applied to the entire market, but also, more specifically, to the indicators relating to the largest listed securities.

However, from the last months of 1998 onwards, and particularly in 1999, the two Belgian

CHART 53 — STOCK MARKET PRICES

(End-of-period data, indices January 1996 = 100)



Sources : National stock exchanges.

indices and the German CDAX diverged from the general trend.

In the case of Germany, this deviation is probably attributable to cyclical factors, as the economic recovery there materialised more slowly than in most of the other EU countries. It is however symptomatic to note that this factor chiefly affected the prices of the smallest securities, because the DAX index, confined to the big companies, moved more in line with the other European indices.

The Belgian cyclical pattern, on the other hand, was relatively more favourable in 1999 than that of the euro area as a whole and therefore can hardly be said to be the cause of the difference in performance on the stock markets. Furthermore, the decline in prices in Belgium applied both to big companies and to other securities.

As the movement was fairly general, it does not appear to have been solely attributable, either, to sectoral causes, such as the considerable weight on the Brussels Stock Exchange, of financial securities or the incidence of the mergers and acquisitions which took place in some branches of activity. Furthermore, these operations are not specific to Belgium.

It seems undeniable, on the other hand, that the entry into force of EMU played a part in changing supply and demand conditions on the stock markets. Owing to the introduction of the euro, purchasers, and especially institutional investors, were able to widen their investment horizon without having to incur any exchange risk. This – both geographical and sectoral – diversification movement seems to be taking place primarily on the largest markets and in the case of the main companies or of enterprises specialising in new technologies. On these various planes the Brussels Stock Exchange suffers from a handicap. Its total capitalisation is far smaller than that of the neighbouring centres, while the fairly few listed companies include only a small proportion of very large enterprises and few technological securities. The concentration of the market, measured by the share of the 5 p.c. of enterprises with the highest capitalisation, amounted in Brussels at the end of 1998 to only 57 p.c., against nearly 70 p.c. for the Paris Stock Exchange and between 70 and 80 p.c. for those of Amsterdam and Frankfurt.

TABLE 48 — CHARACTERISTICS OF SOME EUROPEAN STOCK EXCHANGES [1]

(End-1998 data) [2]

	Number of listed enterprises	Stock exchange capitalisation in billions of euro	Market concentration [3]	Holding of the main shareholder [4]		
				Over 50 p.c.	Between 25 and 50 p.c.	Under 25 p.c.
Brussels	146	210	56.5	68	26	6
Frankfurt	741	931	77.8	68	21	11
Paris	914	837	68.6	37	32	31
Amsterdam	212	512	73.3	44	20	36

Sources : International Federation of Stock Exchanges ; BXS ; E. Wymeersch, *A Status Report on Corporate Governance Rules and Practices in Some Continental European States* in K. Hopt, H. Kanda, M. Roe, E. Wymeersch and S. Prigge (eds), *Comparative Corporate Governance. The State of the Art and Emerging Research*, Clarendon Press-Oxford, 1998.

[1] National securities.

[2] Except for the holding of the main shareholder, where the data relate to 1995 for France, 1996 for Germany and 1997 for Belgium and the Netherlands.

[3] Market share of the 5 p.c. of enterprises with the highest capitalisation.

[4] Percentage of the total number of listed companies.

This situation is furthermore reflected in the representation of Belgian enterprises in the Euro Stoxx 50 index, as only two of them are included in this indicator covering 50 of the largest companies in the EU.

In this context, the diversification of the investments of Belgian investors in securities of other European countries has probably not been counterbalanced by a flow of the same size in the opposite direction to the benefit of securities listed on the Brussels Stock Exchange. This asymmetry has weighed all the more heavily on prices because, for a number of Belgian shares, the markets are fairly narrow, as a very large proportion of the capital is permanently held. The percentage of listed companies whose main shareholder holds over 50 p.c. of the shares is estimated at 68 p.c., while the largest shareholding is less than 25 p.c. in only 6 p.c. of the enterprises. Although comparable percentages are observed in Germany, the concentration of the shareholdership appears to be much less great in France and the Netherlands.

In a context which admittedly differs from that of public debt securities, the trend of prices on the Brussels Stock Exchange therefore comes down to a problem of liquidity which seems to be common to both markets. To strengthen this liquidity, issuers, handicapped by their smallness, are endeavouring to spread their securities more widely on foreign markets, resorting if necessary to non-resident intermediaries.

METHODOLOGICAL NOTE

Unless otherwise indicated, when data are compared from year to year, they all relate to the same period of each of the years in question.

In the tables, the totals shown may differ from the sum of the items owing to rounding.

In order to make it possible to describe the development of various important economic data relating to Belgium in the year 1999 as a whole, it was necessary to make estimates, as the statistical material for that year is inevitably still very fragmentary. In the tables and charts these estimates, which were arrived at in January 2000, are marked by the sign "e". They represent mere orders of magnitude intended to demonstrate the trends which already seem to be emerging. On the other hand, the comments on the international environment and the international comparisons are based on data from international institutions, which for the year under review were closed a few months earlier.

On 1 January 1999 the Belgian franc ceased to be an independent currency and became one of the national denominations of the euro. The euro is therefore the monetary unit used in this Report, when the data relate to Belgium or the euro area. The amounts relating to the periods prior to 1 January 1999 are converted at the irrevocable conversion rates for the euro. The euro area consists of the eleven countries which share the single currency, namely – in addition to Belgium – Austria, Finland, France, Germany, Ireland, Italy, Luxembourg, the Netherlands, Portugal and Spain. For convenience, the term "euro area" is also used to designate this group of countries for periods prior to 1 January 1999.

For the years prior to 1999 the official national accounts data have been included in the Report as they stand. However, account has been taken of the corrections to the definition of the general government deficit, announced by the NAI in its January 2000 publication entitled *Comptes nationaux 1998 – Partie III : Comptes détaillés et tableaux*. These corrections are mirrored in the company accounts[1].

During the year under review the NAI, in accordance with the obligation imposed by Eurostat, applied the ESA 95 methodology for the first time for compiling the national accounts, instead of the ESA 79 methodology used until then. This new system gives a more accurate and complete picture of economic developments. It also proposes a better accounting treatment of products or services whose development was at an early stage when the old system was designed (such as, for instance, software and leasing). Lastly, it does more to ensure the international comparability of macroeconomic data. The implementation of ESA 95 was accompanied by the introduction of a set of new concepts and a number of methodological changes. Although the NAI has already presented the new system in detail, it seems appropriate to comment briefly on certain changes and innovations[1].

With regard to the new concepts, some of them are merely terminological adaptations, while others relate to aggregates which did not exist previously. One of the most noteworthy changes with regard to terminology is that the term "gross national product" (GNP) is replaced in ESA 95 by the concept

[1] For fuller information concerning the new system of national accounts according to ESA 95, see the NAI publication entitled *Comptes nationaux 1998 – Partie I : Estimation des agrégats annuels*. The changes caused by the switch to this new system for general government are specified in more detail in another publication from the same source, entitled *Comptes nationaux 1998 – Partie III : Comptes des administrations publiques*.

of “gross national income” (GNI). Another example is that of the term “depreciation”, which is replaced by the expression “consumption of fixed capital”.

The ESA 95 methodology distinguishes two concepts connected with consumption and disposable income. There is first of all that of final consumption expenditure, which identifies the portion of final consumption paid for by each of the sectors and is matched by the concept of gross disposable income. Actual final consumption, by contrast, measures the acquisition of consumer goods and services independently of the sector which does the spending. The concept corresponding to this is that of gross adjusted disposable income. The difference between these concepts lies in the treatment applied to certain goods and services which are financed by general government or by non-profit institutions serving households but which are provided to the latter in the form of social transfers of individual non-market goods and services, also called transfers in kind. A typical example is that of the interventions of general government in health expenditure. In ESA 79 these were treated as transfers from general government to households and therefore formed part of the latter's final expenditure. In ESA 95 these interventions are regarded as final consumption expenditure of general government made available to households in the form of social benefits in kind. They are then included in the actual final consumption of the latter, but not in their final expenditure. Like the presentation of the national accounts by the NAI, the comments in this Report relate to the concepts of final consumption expenditure and gross disposable income. The data concerning consumption, disposable income and the savings ratio are not comparable, therefore, with the aggregates used in earlier editions.

A number of new concepts, such as the “gross operating surplus of individuals”, are commented upon in greater detail when they are analysed.

The Report furthermore incorporates the new definitions and methods as far as possible into the Bank's traditional form of presentation, which provided a complete and comprehensive picture of the main developments which had taken place in the Belgian economy. It continues, however, to express the data in gross terms although ESA 95 presents the main aggregates obtained from the national accounts in the form of net fixed capital consumption results. The presentation in the form of gross data has the advantage of limiting the problem connected with the valuation of depreciation, which is based on the knowledge, assumed to be perfect, of the stock of fixed capital. Furthermore, the use of the same concepts as in the past makes it easier to interpret certain movements such as the gross operating surplus. For similar reasons the sectoral breakdown groups together, under the heading “individuals”, households and non-profit institutions serving households, which constitute separate sectors according to the ESA 95 methodology.

In the chapter devoted to the international environment, the traditional presentation has been maintained, because the sources used, usually the OECD, have not yet been entirely adapted to the new methodology, or to its equivalent, the United Nations System of National Accounts (SNA 1993).

With regard, in particular, to the content, there are, between ESA 95 and the preceding system, ESA 79, a number of methodological differences which can exert an influence on GDP. For Belgium, only the following changes are important from this point of view :

– in the new system, consumption of fixed capital is extended to bridges, roads and other public works. In so far as the output of general government is conventionally valued as being the sum of costs, of which consumption of fixed capital forms part, the new working method has the effect of increasing the value added of general government and, ultimately, GDP;

– purchases of software and large data banks are no longer regarded as intermediate consumption but are considered to be gross investments in fixed capital. The same applies to the development of software and of large data banks for private use;

– in calculating the output of insurance companies, account is taken henceforth of the total amount of the income from the investment of the technical provisions. The old system took account of only part of the income from the provisions formed in connection with life insurance.

Another significant change is the taking into account of the reinvested profits on foreign direct investments in the calculation of the incomes from property received from and paid to foreign countries. This has no effect on GDP but does have an impact on GNI.

Another consequence of the changeover to ESA 95, or of the clarifications of the national accounts methodology provided in this connection by Eurostat, is the change in sectoral classification for certain institutional units. This leads to slight changes in the financing balances of the major sectors of the economy, especially general government. However these changes are greater for the outstanding amount of its financial assets and liabilities. The nominal amount of the consolidated gross public debt which serves as the reference for the excessive public deficit procedure in the Treaty on European Union had to be revised upwards in this context.

There is no longer a specific chapter devoted to comments on the balance of payments of the BLEU. In the euro area the changes in the financial flows between the BLEU and the other member countries have hardly any significance for monetary policy and the determination of the exchange rate for the euro. On the one hand, the allocation of the financial resources emanating from economic agents with a savings surplus to economic agents with a deficit is no longer determined in the euro area by expectations concerning exchange rates, or by interest-rate differentials due to the existence of several currencies subject to independent monetary and foreign exchange policies. On the other hand, the use of a single currency leads to an integration of the financial markets and an intensification of the financial flows between the countries of the euro area.

However, Belgium's current account balance of payments transactions are still the subject of specific comments, which are grouped together in this Report with the summary of the transactions of the major sectors. They provide indications on the competitiveness of the Belgian economy, as well as, all other things remaining equal, on the development of its financial position vis-à-vis the rest of the world, that is, on the net accumulation of claims on foreign countries.

The breakdown of the financial accounts between individuals and companies is largely based on the data from credit institutions. The information making it possible to break down the other financial transactions of the private sector, especially transactions with foreign countries or purchases of securities, are much more fragmentary. The main statistics which can be used for this purpose, namely the globalisation of the annual accounts of enterprises compiled by the Central Balance Sheet Office, are in fact partial, are produced only annually and are available only after a time-lag of several months. It has therefore been necessary to introduce some assumptions and make various estimates.

CONVENTIONAL SIGNS

–	The datum does not exist or is meaningless
…	zero or negligible quantity
n.	not available
p.c.	per cent
p.m.	pro memoria
e	estimate by the Bank

LIST OF ABBREVIATIONS

BBA	Belgian Bankers' Association
BFC	Banking and Finance Commission
BIS	Bank for International Settlements
BLEU	Belgian-Luxembourg Economic Union
BXS	Brussels Exchanges
CIK	Securities Deposit and Clearing Office of the Financial Sector
CEC	Centre for Exchange and Clearing
EASDAQ	European Association of Securities Dealers Automated Quotation
EC	European Commission
ECB	European Central Bank
ELLIPS	Electronic Large-value Interbank Payment System
EMU	Economic and Monetary Union
ESA	European System of Accounts
ESCB	European System of Central Banks
EU	European Union
FPB	Federal Planning Bureau
GDP	Gross domestic product
GNI	Gross national income
GNP	Gross national product
HICP	Harmonised Index of Consumer Prices
HWWA	Hamburgisches Welt-Wirtschafts-Archiv
IMF	International Monetary Fund
ISO	Insurance Supervision Office
LEA	Local Employment Agency
MEA	Ministry of Economic Affairs
MEL	Ministry of Employment and Labour
MFI	Monetary Financial Institution
NAI	National Accounts Institute
NASDAQ	National Association of Securities Dealers Automated Quotation
NBB	National Bank of Belgium
NEMO	National Employment Office
NPA	Non-profit association
NSI	National Statistical Institute
OECD	Organisation for Economic Co-operation and Development
OLO	Linear bond
OPEC	Organisation for Petroleum Exporting Countries
SDR	Special Drawing Right
TARGET	Trans-European Real-time Gross settlement Express Transfer
UCI	Undertaking for collective investment
UPEDI	Union professionelle des entreprises de travail intérimaire (Association of temporary employment agencies)
VAT	Value added tax

Statistical annex

TABLE I – SUMMARY OF MACROECONOMIC DEVELOPMENTS IN SOME EURO AREA COUNTRIES

	Belgium		Germany		France		Italy		Spain		Netherlands		Austria	
	1998	1999 e	1998	1999	1998	1999	1998	1999	1998	1999	1998	1999	1998	1999
Expenditure at constant prices	*(Percentage contributions to the change in GDP)*													
Final consumption expenditure of individuals [1]	2.0	1.1	1.3	1.0	2.0	1.3	1.1	0.9	2.4	2.5	2.0	2.0	0.9	1.1
Public expenditure	0.3	0.6	...	0.2	0.4	0.4	0.4	0.5	0.6	0.4	0.8	0.9	0.3	0.3
Gross fixed capital formation of the private sector	0.7	1.1	0.3	0.7	1.0	1.1	0.4	0.4	1.8	1.9	1.1	0.3	1.1	0.8
of which gross formation of non-residential fixed capital	0.6	1.1	0.6	0.9	0.8	0.7	0.4	0.4	1.6	1.5	1.1	0.3	1.1	0.7
Total domestic expenditure	3.9	1.7	2.4	1.7	3.7	2.5	2.5	2.2	4.9	5.0	4.0	3.2	2.6	2.2
Exports	3.1	2.1	2.0	0.5	1.7	0.5	0.3	–0.3	1.9	1.9	3.9	2.5	4.4	1.7
Imports	–4.3	–1.5	–2.2	–0.9	–2.1	–0.5	–1.5	–0.9	–2.9	–3.2	–4.2	–2.7	–3.7	–1.7
External balance	–1.2	0.6	–0.3	–0.4	–0.4	–0.1	–1.2	–1.2	–1.0	–1.3	–0.3	–0.2	0.7	...
GDP	2.7	2.3	2.2	1.3	3.4	2.4	1.3	1.0	4.0	3.7	3.7	3.0	3.3	2.2
Inflation	*(Percentage changes compared to the previous year)*													
Harmonised index of consumer prices	0.9	1.1	0.6	0.6	0.7	0.6	2.0	1.7	1.8	2.2	1.8	2.0	0.8	0.5
Unemployment [2]	*(Percentages of the labour force)*													
Number of unemployed (EC data)	9.5	9.0	9.4	9.1	11.7	11.0	11.9	11.3	18.7	15.8	4.0	3.2	4.7	4.4
Public Finance	*(Percentages of GDP)*													
Net financing requirement (–) of general government	–1.0	–0.9	–1.7	–1.6	–2.7	–2.1	–2.7	–2.2	–2.3	–1.4	–0.8	–0.4	–2.4	–2.2
Balance of payments	*(Percentages of GDP)*													
Balance of current transactions	4.1	4.0	–0.2	...	2.8	2.4	1.7	0.6	–0.2	–1.1	5.5	3.6	–2.2	–2.6

Sources: NAI, EC, NBB for Belgium; OECD and EC for other countries.
[1] For Austria: private consumption according to ESA 79.
[2] For 1999: average for eleven months for the Netherlands and ten months for Italy.

TABLE II – GDP AND MAIN CATEGORIES OF EXPENDITURE AT 1995 PRICES

(Percentage changes compared to the previous year)

	1996	1997	1998	1999 e
Final consumption expenditure of individuals	0.6	2.2	3.8	2.0
Housing	−4.0	4.9	2.3	0.2
Gross fixed capital formation by enterprises	4.3	7.2	4.5	7.8
Expenditure of general government	1.5	0.4	1.4	2.8
Final consumption	2.3	...	1.4	2.1
Gross fixed capital formation	−7.8	5.2	1.0	11.1
p.m. Total gross fixed capital formation[1]	*1.0*	*6.5*	*3.7*	*6.2*
Changes in stocks[2]	−0.3	0.1	0.8	−1.1
Total domestic expenditure	0.8	2.7	4.1	1.8
Exports of goods and services	1.3	6.7	4.2	2.9
Total final expenditure	1.0	4.4	4.2	2.3
Imports of goods and services	1.0	5.8	6.3	2.2
p.m. Net exports of goods and services[2]	*0.3*	*0.9*	*−1.2*	*0.6*
GDP	1.0	3.5	2.7	2.3

Sources: NAI, NBB.

[1] Gross fixed capital expenditure by enterprises and gross fixed capital formation by general government.

[2] Contribution to the change in GDP.

TABLE III – DEFLATORS OF GDP AND OF THE MAIN CATEGORIES OF EXPENDITURE

(Percentage changes compared to the previous year)

	1996	1997	1998	1999 e
Final consumption expenditure of individuals	2.1	1.5	0.8	1.1
Housing	1.6	1.4	0.6	1.0
Gross fixed capital formation by enterprises	0.9	1.0	0.5	–1.2
Expenditure of general government	1.2	2.4	2.0	1.5
Final consumption expenditure	1.3	2.4	2.1	1.6
Gross fixed capital formation	0.8	2.0	…	0.5
p.m. Total gross fixed capital formation [1]	*1.0*	*1.2*	*0.5*	*–0.6*
Total domestic expenditure [2]	1.7	1.6	1.0	0.8
Exports of goods and services	2.4	4.6	–0.3	–0.5
Total final expenditure [2]	2.0	2.9	0.4	0.7
Imports of goods and services	2.9	5.2	–1.6	0.2
p.m. Terms of trade	*–0.4*	*–0.6*	*1.3*	*–0.7*
GDP	1.2	1.3	1.6	1.0

Sources : NAI, NBB.

[1] Housing, gross fixed capital formation by enterprises and gross fixed capital formation by general government.

[2] Excluding the change in stocks.

TABLE IV – GNI AND MAIN CATEGORIES OF EXPENDITURE AT CURRENT PRICES

(Millions of euro)

	1995	1996	1997	1998	1999 e
Final consumption expenditure of individuals	108,690	111,660	115,787	121,215	125,091
Housing	10,832	10,560	11,232	11,568	11,708
Gross fixed capital formation by enterprises	26,558	27,945	30,251	31,760	33,840
Expenditure of general government	46,828	48,118	49,443	51,110	53,319
Final consumption expenditure	43,257	44,800	45,882	47,513	49,300
Gross fixed capital formation	3,571	3,318	3,560	3,598	4,019
p.m. Total gross fixed capital formation [1]	*40,961*	*41,823*	*45,043*	*46,926*	*49,566*
Change in stocks	423	–716	–497	593	–343
Total domestic expenditure	193,331	197,566	206,217	216,246	223,614
Exports of goods and services	141,359	146,684	163,815	170,253	174,365
Total final expenditure	334,690	344,250	370,032	386,499	397,980
Imports of goods and services	133,178	138,396	154,058	161,193	165,089
p.m. Net exports of goods and services	*8,180*	*8,287*	*9,757*	*9,061*	*9,276*
GDP	201,511	205,854	215,974	225,307	232,890
Net primary incomes received from the rest of the world	2,059	2,652	2,036	2,138	2,111
GNP	203,570	208,506	218,010	227,445	235,001

Sources : NAI, NBB.

[1] Housing, gross fixed capital formation by enterprises and gross fixed capital formation by general government.

TABLE V – VALUE ADDED OF THE VARIOUS BRANCHES OF ACTIVITY AT 1995 PRICES

(Percentage changes compared with the previous year)

	1996	1997	1998	p.m. Percentages of the 1998 GDP
Agriculture, foresty and fisheries	1.3	1.7	–3.9	1.3
Industry	1.7	4.4	1.5	21.2
Mineral-extracting industry	–7.3	7.9	3.4	0.2
Electricity, gas, water	7.7	3.5	...	2.7
Manufacturing industry	0.9	4.6	1.7	18.3
of which:				
Non-metallic minerals	–6.3	2.5	–1.4	0.9
Iron, steel and non-ferrous metals	–4.0	3.0	0.3	2.7
Metal-working industry	–0.6	3.4	0.2	4.3
Paper, printing, publishing	–2.1	5.9	3.0	1.4
Chemicals and rubber	5.1	6.7	4.8	4.3
Textiles, clothing and footwear	7.0	2.7	2.1	1.1
Food, beverages, tobacco	4.4	6.3	2.5	2.4
Building industry	–4.3	3.4	0.9	4.5
Market services[1]	0.6	3.0	4.1	52.8
Trade and repairs	–2.8	1.6	4.5	11.1
Financial services	6.6	3.8	6.4	6.4
Real estate, renting and services to enterprises	2.5	4.9	2.9	18.7
Transport and communications	–3.5	2.2	7.5	6.6
Health and social services	2.6	0.3	0.3	5.7
Hotels and catering and miscellaneous services to households	–2.3	1.7	4.6	4.3
Non-market services	1.6	0.3	1.4	13.5
Value added of branches, at basic prices	0.8	2.9	2.8	
Financial intermediation services indirectly measured and taxed net of subsidies on products[2]	0.2	0.8	0.1	
GDP	1.0	3.5	2.7	100.0

Sources: NAI, NBB.

[1] Services which are not provided by general government.

[2] Contribution to the change in GDP.

TABLE VI — DEMAND FOR AND SUPPLY OF EMPLOYMENT

(Thousands of units, annual averages)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999 e
1. Population of working age [1] (potential demand for jobs)	6,674	6,675	6,682	6,694	6,703	6,704	6,703	6,706	6,709	6,713
Men	3,358	3,360	3,365	3,372	3,378	3,377	3,376	3,378	3,379	3,381
Women	3,316	3,315	3,316	3,321	3,325	3,326	3,327	3,328	3,330	3,332
2. Employment										
2.1 Total employment	3,794	3,798	3,779	3,752	3,738	3,764	3,777	3,808	3,855	3,895
Men	2,286	2,275	2,250	2,219	2,201	2,204	2,198	2,203	2,218	2,231
Women	1,508	1,523	1,529	1,533	1,537	1,561	1,579	1,605	1,637	1,663
2.2 Frontier workers (balance)	50	50	49	48	50	50	51	52	54	54
2.3 Domestic employment	3,744	3,748	3,731	3,703	3,689	3,714	3,726	3,756	3,801	3,841
Self-employed persons	675	683	687	697	696	699	703	699	693	692
Employees	3,069	3,065	3,044	3,006	2,993	3,015	3,024	3,057	3,108	3,148
Breakdown by branches of activity										
Agriculture	17	17	18	18	18	22	20	19	21	21
Industry and energy	771	758	738	707	683	676	666	655	659	657
Building	173	178	181	186	187	182	176	174	173	176
Services other than public administration and education	1,383	1,400	1,402	1,396	1,416	1,443	1,466	1,505	1,550	1,588
Public administration and education [2]	724	711	704	700	689	692	696	703	703	707
Breakdown by type of jobs										
Activation policy [3]	–	–	–	–	–	–	3	8	15	26
Other job-creation measures [4]	126	127	119	114	115	117	120	126	124	124
Other jobs [5]	2,943	2,938	2,924	2,892	2,878	2,898	2,901	2,923	2,968	2,998
3. Employment rate (2.1 as percentage of 1)	56.9	56.9	56.6	56.0	55.8	56.1	56.4	56.8	57.5	58.0
Men	68.1	67.7	66.8	65.8	65.2	65.2	65.1	65.2	65.6	66.0
Women	45.5	45.9	46.1	46.1	46.2	46.9	47.5	48.2	49.2	49.9

Sources: NAI, NSI, MEL, NEMO, NBB.

[1] Men and women aged 15 to 64.

[2] This item corresponds to Nace-Bel sectors L and M, as defined by the NAI.

[3] LEA workers exempted from having to sign on as job-seekers, persons given work under an occupational transition programme or a "Smet" job.

[4] Third labour circuit, PRIME employment programme (regional projects for insertion in the labour market) of the Walloon region, subsidised contractually employed persons, on-the-job training of young people, interdepartmental budget fund, RD 123 and RD 258.

[5] Balance.

TABLE VII — CONSUMER PRICES [1]

(Percentage changes compared to the previous year)

	Total						
		Non-processed food products [2]	Energy products	Processed food products	Non-energy industrial products	Services	of which: Rents
1992	2.4	−2.0	−1.1	2.5	2.1	4.4	5.9
1993	2.8	−2.5	3.6	1.9	2.4	4.2	5.3
1994	2.4	2.3	0.9	2.1	1.9	3.1	4.6
1995	1.5	1.0	−0.6	1.7	1.1	2.2	2.9
1996	2.1	0.8	6.1	1.0	0.8	2.5	2.5
1997	1.6	2.5	4.0	2.4	0.4	1.6	1.7
1998	1.0	2.5	−4.4	1.3	0.5	2.5	1.2
1999	1.1	0.1	2.0	0.6	0.8	1.7	1.4

Sources: MEA, NBB.

[1] National index of consumer prices. The data differ somewhat from those in Chapter 5 of the Report, where the harmonised index of consumer prices is used. The coverage of the HICP corresponds to just under 94 p.c. of that of the national index of consumer prices.

[2] Fruit, vegetables, meat and fish.

TABLE VIII – INCOMES OF THE VARIOUS SECTORS AT CURRENT PRICES [1]

(Millions of euro)

	1995	1996	1997	1998	1999 e
Individuals					
Gross primary income	161,220	163,422	169,179	175,622	180,154
Wages and salaries [2]	107,509	109,089	113,285	117,553	121,484
Income from property [3]	20,897	20,722	21,254	21,754	21,309
Remuneration and profits of owner enterpreneurs	18,133	18,399	18,955	20,013	20,538
Gross operating surplus	14,681	15,213	15,684	16,302	16,823
Net current transfers paid [4]	−27,736	−28,176	−30,614	−31,906	−32,649
From and to (−) general government	−26,836	−26,889	−29,009	−30,363	−30,893
Transfers received	35,844	36,688	37,820	38,815	39,670
Transfers paid (−)	−62,679	−63,577	−66,829	−69,178	−70,563
To (−) other sectors	−900	−1,287	−1,605	−1,543	−1,756
Disposable income	133,485	135,246	138,564	143,716	147,505
p.m. At constant prices [5]	*133,485*	*132,511*	*133,587*	*137,247*	*139,283*
(percentage changes compared to the previous year)	*(n.)*	*(−0.7)*	*(0.8)*	*(2.7)*	*(1.5)*
Companies					
Gross primary income	33,655	34,229	35,880	37,926	38,772
Gross operating surplus	37,470	37,912	40,927	43,100	44,720
Incomes from property [3]	−3,815	−3,683	−5,048	−5,173	−5,948
Net current transfers to (−) other sectors [4]	−4,319	−4,345	−4,979	−6,878	−6,519
Gross disposable income	29,336	29,883	30,901	31,048	32,252
General government					
Gross primary income	8,695	10,855	12,951	13,896	16,332
Net current transfers from other sectors [4]	30,777	30,909	33,888	36,733	36,752
Gross disposable income	39,472	41,763	46,839	50,629	53,084
Rest of the world					
Gross disposable income	1,278	1,613	1,705	2,051	2,160
GNI	203,570	208,506	218,010	227,445	235,001

Sources : NAI, NBB.

[1] The results in this table are in gross terms, i.e. before deduction of consumption of fixed capital.

[2] Remunerations (excluding those of owner entrepreneurs) including employers' social security contributions and civil service pensions.

[3] These are net amounts, i.e. the difference between incomes from property received from other sectors and incomes from property paid to other sectors.

[4] These are net amounts, i.e. the difference between transfers received from other sectors and transfers paid to other sectors, excluding transfers in kind.

[5] Data deflated by the national index of consumer prices.

TABLE IX – SUMMARY OF THE TRANSACTIONS OF THE MAJOR SECTORS OF THE ECONOMY AT CURRENT PRICES[1]

(Millions of euro)

	1995	1996	1997	1998	1999 e
1. Individuals					
1.1 Gross disposable income	133,485	135,246	138,564	143,716	147,505
p.m. Gross adjusted disposable income	*161,908*	*165,030*	*168,932*	*175,126*	*180,296*
1.2 Change in households' pension fund entitlements	1,135	1,716	1,915	1,558	1,558
1.3 Final consumption expenditure	108,690	111,660	115,787	121,215	125,091
p.m. Actual final consumption	*137,113*	*141,443*	*146,155*	*152,625*	*157,881*
1.4 Gross savings (1.1 + 1.2 – 1.3)	25,929	25,302	24,692	24,059	23,972
p.m. Percentages of disposable income	*19,4*	*18,7*	*17,8*	*16,7*	*16,3*
p.m. Percentages of gross adjusted disposable income	*16,0*	*15,3*	*14,6*	*13,7*	*13,3*
1.5 Capital transfers [2]	864	–53	–144	–294	–169
1.6 Gross capital formation	13,356	13,138	14,046	14,738	15,085
1.7 Net financing capacity (1.4 + 1.5 – 1.6)	13,437	12,111	10,502	9,027	8,718
2. Companies					
2.1 Gross disposable income	29,336	29,883	30,901	31,048	32,252
2.2 Change in households' pension fund entitlements	–1,135	–1,716	–1,915	–1,558	–1,558
2.3 Gross savings (2.1 + 2.2)	28,201	28,168	28,985	29,491	30,695
2.4 Capital transfers [2]	2	1,272	2,347	2,118	1,936
2.5 Gross fixed capital formation	24,034	25,367	27,437	28,591	30,463
2.6 Change in stocks	420	–712	–498	587	–343
2.7 Net financing capacity (2.3 + 2.4 – 2.5 – 2.6)	3,750	4,784	4,394	2,430	2,511
3. General government					
3.1 Gross disposable income	39,472	41,763	46,839	50,629	53,084
p.m. Gross adjusted disposable income	*11,049*	*11,980*	*16,472*	*19,219*	*20,293*
3.2 Final consumption expenditure	43,257	44,800	45,882	47,513	49,300
p.m. Actual final consumption	*14,834*	*15,016*	*15,515*	*16,102*	*16,510*
3.3 Gross savings (3.1 – 3.2)	–3,785	–3,037	957	3,117	3,784
3.4 Capital transfers [2]	–1,097	–1,256	–1,809	–1,854	–1,774
3.5 Gross fixed capital formation	3,571	3,318	3,560	3,598	4,019
3.6 Change in stocks	3	–4	1	5	...
3.7 Net financing requirement (–) (3.3 + 3.4 – 3.5 – 3.6)	–8,456	–7,606	–3,560	–2,341	–2,009
4. Total of domestic sectors					
4.1 Net financing capacity (1.7 + 2.7 + 3.7)	8,731	9,289	10,482	9,116	9,220

Sources: NAI. NBB.

[1] The results in this table are calculated in gross terms, i.e. before deduction of consumption of fixed capital.

[2] These are net amounts, i.e. the difference between transfers received from other sectors and transfers paid to other sectors, including net acquisitions of non-financial assets.

TABLE X — REVENUE, EXPENDITURE AND NET FINANCING REQUIREMENT OF GENERAL GOVERNMENT[1]

(Millions of euro)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999 e
Revenue	71,594	75,655	78,321	83,691	88,241	91,512	94,626	100,006	104,618	107,764
Fiscal and parafiscal revenue	69,224	72,904	75,714	80,984	85,823	88,941	91,747	97,371	102,247	104,619
Levies weighting chiefly on earned incomes	40,311	43,457	46,536	49,515	51,404	53,197	53,973	56,952	59,221	60,601
Personal income tax [2]	18,499	19,715	21,233	23,083	23,929	25,240	25,439	27,039	28,385	28,727
Social security contributions [3]	21,811	23,742	25,303	26,432	27,475	27,957	28,534	29,913	30,836	31,874
Taxes on profits of companies [4]	3,483	3,628	2,952	3,800	4,456	5,170	5,671	6,383	7,849	7,485
Levies on other income and in respect of property [5]	6,494	6,006	5,595	5,933	6,655	6,834	6,982	7,454	7,888	7,592
Taxes on goods and services	18,936	19,813	20,632	21,736	23,308	23,740	25,121	26,582	27,290	28,940
Non-fiscal and non-parafiscal revenue	2,370	2,750	2,608	2,707	2,418	2,571	2,878	2,635	2,371	3,144
Expenditure excluding interest charges	63,736	69,302	72,988	76,897	79,486	81,632	84,239	87,336	89,716	93,206
Current transfers to individuals	36,750	40,142	42,852	44,656	46,096	48,099	49,827	51,007	52,545	54,256
Replacement incomes	20,928	22,693	23,964	25,279	26,072	26,795	27,644	28,540	29,256	29,905
Pensions	13,327	14,428	15,327	16,176	16,843	17,570	18,109	18,952	19,563	20,100
Private sector pensions	9,987	10,726	11,366	11,902	12,265	12,724	13,110	13,450	13,866	14,205
General government pensions [6]	3,340	3,702	3,961	4,274	4,578	4,847	5,000	5,502	5,696	5,895
Old persons' guaranteed income	239	235	238	247	236	235	231	233	231	231
Early retirement pensions	1,202	1,251	1,298	1,277	1,290	1,294	1,305	1,280	1,255	1,215
Unemployment benefits	3,101	3,540	3,776	4,224	4,307	4,219	4,442	4,480	4,476	4,499
Career interruption	125	142	165	153	136	132	130	139	162	198
Sickness and disability insurance benefits	2,217	2,356	2,393	2,416	2,430	2,482	2,543	2,545	2,633	2,723
Industrial accidents	153	160	157	158	158	160	157	156	160	162
Occupational diseases	363	372	382	367	375	367	358	347	351	336
Subsistence allowance	202	210	229	262	297	336	368	409	425	442
Other transfers to individuals [7]	15,822	17,449	18,888	19,377	20,024	21,304	22,183	22,467	23,288	24,350
of which: Health care	7,821	8,831	9,774	10,103	10,314	11,155	11,973	11,916	12,434	13,199
Family allowance	3,418	3,570	3,696	3,815	3,878	3,976	4,145	4,209	4,278	4,364
Other primary expenditure	26,986	29,160	30,136	32,241	33,389	33,533	34,412	36,329	37,172	38,951
Compensations	13,801	14,771	15,592	16,486	17,348	17,956	18,176	18,812	19,418	19,924
Net current purchases of goods and services	2,855	3,188	2,960	3,121	3,232	3,170	3,308	3,424	3,655	3,864
Subsidies to enterprises	3,727	3,823	3,733	3,854	3,737	3,767	4,033	3,701	3,701	3,911
Current transfers to the rest of the world	2,517	2,894	2,885	2,995	3,253	3,115	3,393	3,723	3,904	4,072
Gross fixed capital formation	2,703	2,938	3,201	3,652	3,821	3,575	3,313	3,562	3,603	4,019
Other capital expenditure	1,384	1,546	1,765	2,132	1,998	1,950	2,188	3,107	2,890	3,161
Net amount excluding interest charges	7,858	6,353	5,334	6,794	8,755	9,880	10,387	12,670	14,902	14,557
Interest charges	18,905	18,932	19,654	20,085	18,299	18,336	17,992	17,084	17,244	16,566
Net financing requirement (–)	–11,047	–12,579	–14,320	–13,290	–9,545	–8,456	–7,606	–4,414	–2,341	–2,009

Sources: NAI, NBB.

[1] Following the clarification of the national accounts methodology recently provided by Eurostat, some data have been slightly changed compared to those published by the NAI.

[2] Withholding tax on earned income, advance payments, assessments and proceeds of additional centimes on personal income tax.

[3] Total social contributions, including the special security contribution and the contribution of non-active persons.

[4] Advance payments, assessments and withholding tax on income from movable property.

[5] The withholding tax on income from movable property payable by individuals, the withholding tax on income from immovable property (including proceeds of additional centimes), death duties, registration fees and the tax on stock exchange transactions.

[6] Including pensions of Post Office staff.

[7] Apart from the two main sub-categories mentioned in the table, this item also includes mainly allowances to handicapped persons and transfers to the institutions accommodating them, subsidies to non-profit associations serving households, payments by subsistence funds and pensions to war victims.

TABLE XI – NET FINANCING REQUIREMENT (–) OR CAPACITY OF GENERAL GOVERNMENT AND OF ITS SUB-SECTORS[1]

(Millions of euro)

	Entity I			Entity II			General government as a whole[2]
	Federal government	Social security	Total	Communities and regions	Local authorities	Total	
1990	–11,103	382	–10,721	–686	360	–326	–11,047
1991	–10,722	–896	–11,617	–1,497	535	–962	–12,579
1992	–11,999	–763	–12,763	–1,763	205	–1,557	–14,320
1993	–10,670	–906	–11,576	–1,502	–212	–1,714	–13,290
1994	–8,968	1,000	–7,969	–1,680	104	–1,576	–9,545
1995	–7,683	–29	–7,712	–1,481	737	–744	–8,456
1996	–6,917	–457	–7,374	–837	606	–232	–7,606
1997	–5,752	920	–4,832	–260	678	418	–4,414
1998	–4,169	837	–3,332	444	547	991	–2,341
1999 e	–4,284	1,129	–3,183	1,221	–128	1,175	–2,009

Sources: NAI, NBB.

[1] Following the clarification of the national accounts methodology recently provided by Eurostat, some data have been slightly adjusted compared to those published by the NAI.

[2] Concept used for the implementation of the convergence criteria defined in the Treaty on European Union.

TABLE XII — OUTSTANDING AMOUNT OF GENERAL GOVERNMENT'S DEBT

(End of period, millions of euro)

	Official debt of the Treasury							Gross consolidated debt of general governement [2]
	In national currency [1]			In foreign currencies			Grand total	
	At up to one year	At over one year	Total	In euro area currencies	In other currencies	Total		
1990	47,752	103,784	151,535	12,925	14,634	27,559	179,094	205,439
1991	47,405	117,294	164,699	12,111	15,331	27,443	192,141	218,207
1992	47,673	132,749	180,422	11,271	13,779	25,050	205,471	232,418
1993	42,181	145,055	187,235	21,933	15,747	37,679	224,915	250,329
1994	54,296	143,680	197,976	17,421	16,031	33,453	231,428	259,862
1995	43,093	166,232	209,325	12,220	14,684	26,905	236,230	265,551
1996	46,420	173,504	219,923	7,598	10,600	18,198	238,121	264,108
1997	47,894	175,743	223,637	8,297	11,148	19,444	243,082	265,661
1998	41,888	182,635	224,523	7,830	9,550	17,380	241,903	264,482
1999	36,553	199,762	236,314	–	10,441	10,441	246,755	267,725 e

Sources : Ministry of Finance, NBB.

[1] In Belgian francs up to the end of 1998, in euro from 1999 onwards.

[2] Concept used for the implementation of the convergence criteria defined in the Treaty on European Union.

TABLE XIII – CURRENT AND CAPITAL TRANSACTIONS OF BELGIUM ON A TRANSACTIONS BASIS

(Millions of euro)

	1997			1998			First nine months 1999		
	Credits	Debits	Balances	Credits	Debits	Balances	Credits	Debits	Balances
1. Total current transactions on a transactions basis	184,544	174,138	10,406	193,323	184,041	9,282	145,959	139,389	6,570
Goods and services	154,628	144,827	9,801	160,725	151,654	9,071	120,907	113,674	7,233
Goods	129,044	120,412	8,632	133,864	125,346	8,518	99,664	93,254	6,410
General merchandise	125,446	119,272	6,174	130,313	124,076	6,237	97,207	92,308	4,899
Goods for processing	2,823	625	2,198	2,806	661	2,145	1,879	477	1,402
Repairs to goods	151	240	−89	180	289	−109	147	222	−75
Purchases of goods in ports	551	230	321	496	279	217	384	227	157
Non-monetary gold	73	45	28	69	41	28	47	20	27
Services	25,584	24,415	1,169	26,861	26,308	553	21,243	20,420	823
Transport	8,225	6,510	1,715	8,444	6,515	1,929	6,104	4,520	1,584
Travel	3,996	6,963	−2,967	4,154	7,407	−3,253	3,747	6,378	−2,631
Communications	775	441	334	862	481	381	761	406	355
Building	879	780	99	817	712	105	575	373	202
Insurance	339	391	−52	345	398	−53	284	306	−22
Financial services	1,446	1,310	136	1,676	1,534	142	1,396	1,357	39
Data-processing and information services	1,052	667	385	1,217	863	354	967	714	253
Fees and licence dues	535	892	−357	562	959	−397	478	710	−232
Other services to enterprises	7,045	5,952	1,093	7,481	6,829	652	5,996	5,233	763
of which merchanting (net)	328	–	328	−65	–	−65	512	–	512
Personal, cultural and leisure services	247	318	−71	248	339	−91	168	229	−61
Services provided or received by general government, not included elsewhere	1,045	191	854	1,055	271	784	767	194	573
Incomes	24,816	21,029	3,787	27,540	23,621	3,919	21,687	19,137	2,550
Compensation of employees	3,636	930	2,706	3,647	963	2,684	2,675	653	2,022
Income from direct and portfolio investment	21,180	20,099	1,081	23,893	22,658	1,235	19,012	18,484	528
Current transfers	5,100	8,282	−3,182	5,058	8,766	−3,708	3,365	6,578	−3,213
General government	1,874	4,386	−2,512	1,835	4,653	−2,818	975	3,413	−2,438
Other sectors	3,226	3,896	−670	3,223	4,113	−890	2,390	3,165	−775
2. Total capital transactions	667	286	381	225	290	−65	220	302	−82
Capital transfers	650	216	434	198	237	−39	169	289	−120
Acquisitions and sales of non-produced non-financial assets	17	70	−53	27	53	−26	51	13	38
3. Net lending to the rest of the world (1 + 2)	185,211	174,424	10,787	193,548	184,331	9,217	146,179	139,691	6,488

Source : NBB.

TABLE XIV — FORMATION OF FINANCIAL ASSETS BY AND NEW FINANCIAL LIABILITIES OF INDIVIDUALS

(Millions of euro)

	1993	1994	1995	1996	1997	1998	First nine months 1998	First nine months 1999	p.m. Outstanding amount at the end of September 1999
Formation of financial assets	24,168	24,979	19,314	26,238	28,867	22,056	16,270	19,959	683,157
With credit institutions or by direct purchase of securities	7,934	17,669	7,802	16,726	12,746	7,764	3,193	14,326	507,396
At up to one year	12,664	−674	−2,500	9,446	20,023	16,986	8,550	18,384	198,345
Notes and sight deposits	2,656	369	432	427	932	3,243	2,827	4,921	34,068
Savings deposits	927	11,052	9,987	10,719	7,881	4,520	1,997	2,099	93,809
Term deposits	3,078	−2,459	−8,193	533	250	−1,664	−2,957	3,696	36,758
Securities	6,003	−9,636	−4,726	−2,233	10,960	10,887	6,683	7,669	33,710
At over one year	−5,970	15,500	11,142	5,632	−9,292	−9,086	−5,991	−3,959	317,924
Time deposits	295	948	1,528	167	271	−279	−224	−1,361	5,414
Fixed-interest securities	−6,090	13,539	9,291	2,862	−12,503	−10,813	−7,994	−7,390	133,968
Shares [1]	−176	1,014	324	2,603	2,940	2,007	2,226	4,792	178,543
Other	1,240	2,843	−840	1,648	2,015	−136	634	−98	−8,873
Via institutional investors	16,521	5,994	6,002	10,076	15,354	24,988	21,343	17,995	183,033
Undertakings for collective investment	13,641	2,486	52	3,826	7,137	15,956	14,527	10,162	100,379
Insurance companies and pension funds	2,880	3,508	5,950	6,250	8,217	9,032	6,816	7,833	82,654
Other assets [2]	−287	1,316	5,510	−564	767	−10,697	−8,266	−12,362	−7,272
New financial liabilities	2,102	4,533	1,837	4,370	5,491	6,872	5,128	4,760	98,073
At up to one year	−766	97	−245	362	−35	1,068	1,150	370	7,729
At over one year	2,868	4,436	2,082	4,008	5,526	5,803	3,978	4,390	90,343
Mortgage loans	3,081	3,407	2,156	2,955	3,622	5,615	4,878	6,106	66,838
Instalment loans	55	84	−102	414	593	18	−40	559	8,961
Other	−267	945	28	639	1,311	170	−860	−2,275	14,544
Financial balance [3]	22,066	20,446	17,477	21,868	23,376	15,184	11,142	15,199	585,084

Source : NBB.

[1] Including real estate certificates.

[2] Direct financing transactions, which it has been possible to record, between domestic sector or with the rest of the world, in forms other than securities, instruments whose maturity is not known and errors and omissions. Including, for the outstanding amounts, the statistical adjustments brought about by the methods of valuation of share portfolios.

[3] The balances of the financial accounts of the domestic sector do not correspond to the net financing capacities or requirements as recorded in the real accounts, owing to the differences between the dates of recording of the transactions in these two accounts, statistical adjustments or errors and omissions. Thus, for example, the financial accounts cannot, for lack of data, record most of the commercial claims and debts.

TABLE XV – FORMATION OF FINANCIAL ASSETS BY AND NEW FINANCIAL LIABILITIES OF COMPANIES [1]

(Millions of euro)

	1993	1994	1995	1996	1997	1998	First nine months 1998	First nine months 1999	p.m. Outstanding amount at the end of September 1999
Formation of financial assets	8,919	5,602	14,051	12,346	10,318	16,141	11,662	25,241	360,190
At up to one year	7,536	–902	3,660	7,716	2,155	8,375	5,818	8,821	73,585
Notes, coins and sight deposits	537	–418	2,189	2,085	1,675	1,928	2,175	1,007	19,850
Other deposits	7,163	313	1,045	3,982	–218	3,880	1,888	7,569	47,697
Other	–164	–797	425	1,650	698	2,567	1,755	245	6,038
At up to one year	1,712	1,706	5,208	1,928	5,493	14,558	8,273	16,879	293,136
Shares	–328	1,580	367	235	904	3,006	1,360	3,552	212,344
Fixed-interest securities	–230	–240	–838	645	1,919	1,981	818	516	8,049
Other	2,271	367	5,680	1,048	2,669	9,571	6,095	12,810	72,743
Other [2]	–329	4,798	5,184	2,703	2,670	–6,791	–2,430	–459	–6,531
New financial liabilities	10,122	8,701	14,347	17,499	18,390	20,025	12,047	28,220	596,851
At up to one year	–634	632	4,450	3,248	2,284	4,394	4,162	7,520	58,959
Credits granted by credit institutions	–1,579	818	3,121	3,855	2,385	6,285	5,044	1,287	49,330
Fixed-interest securities	391	804	953	–182	304	307	1,389	6,273	8,852
Other	554	–990	377	–425	–405	–2,199	–2,271	–40	777
At over one year	10,243	6,555	10,427	13,276	15,729	14,678	7,863	20,891	529,013
Shares	6,512	6,391	6,193	6,286	8,294	9,351	5,916	13,257	408,826
Fixed-interest securities	203	–1,404	1,043	1,578	–248	312	–125	982	17,080
Other	3,529	1,568	3,191	5,413	7,683	5,014	2,073	6,652	103,108
Other [2]	513	1,514	–530	975	377	953	23	–191	8,878
Financial balance [3]	–1,203	–3,099	–296	–5,152	–8,072	–3,884	–385	–2,979	–236,661

Source : NBB.

[1] Credit institutions and institutional investors are excluded from the companies sector, because they are treated as pure financial intermediaries whose financial assets are identical to their financial liabilities.

[2] See note 2 to Table XIV.

[3] See note 3 to Table XIV.

TABLE XVI – FORMATION OF FINANCIAL ASSETS BY AND NEW FINANCIAL LIABILITIES OF GENERAL GOVERNMENT

(Millions of euro)

							First nine months	
	1993	1994	1995	1996	1997	1998	1998	1999
Formation of financial assets [1]	2,394	–2,112	–2,381	–4,774	–1,483	–1,728	–1,298	1,838
At up to one year	2,605	–2,131	–2,441	1,898	393	223	–1,841	1,113
At over one year	–212	19	60	–6,671	–1,876	–1,951	543	725
New financial liabilities	17,489	8,115	6,069	2,652	3,340	459	3,515	7,507
In national currency [2]	6,359	11,888	12,557	10,933	3,369	2,528	3,399	7,613
At up to one year	–5,377	12,107	–8,886	4,619	515	–5,381	–90	–72
At over one year	11,737	–219	21,444	6,313	2,854	7,910	3,489	7,686
In foreign currencies	11,130	–3,773	–6,488	–8,281	–29	–2,069	116	–106
At up to one year	10,875	–5,534	–8,004	–5,179	–604	–887	1,219	599
At over one year	255	1,762	1,515	–3,102	575	–1,183	–1,103	–706
Financial balances [3]	–15,096	–10,227	–8,450	–7,426	–4,823	–2,187	–4,813	–5,669

Source: NBB.

[1] Including lending and equity investment.

[2] That is, the Belgian franc up to the end of 1998 and the euro from 1999 onwards.

[3] See note 3 to Table XIV.

TABLE XVII — BALANCE SHEET STRUCTURE OF BELGIAN CREDIT INSTITUTIONS

(Changes, in millions of euro)

							First nine months			
	1996		1997		1998		1998		1999	
	Assets	Liabilities	Assets	Liabilities	Assets	Liabilities	Assets	Liabilities	Assets	Liabilities
By counterparty										
Credit institutions [1]	19,469	15,292	–3,339	–5,096	–5,408	–2,980	–3,626	–1,212	15,498	34,965
Other sectors	15,814	19,990	14,577	16,334	13,828	11,400	15,156	12,742	28,315	8,848
Individuals	4,316	5,516	5,146	1,808	6,153	4,154	5,007	3,307	4,603	2,470
Companies [2]	3,848	9,761	3,293	6,331	2,578	3,710	887	5,042	3,046	1,270
General government	1,924	–857	–2,627	–1,593	1,053	273	4,885	351	–10,997	3,241
Rest of the world [2]	5,725	5,570	8,765	9,788	4,044	3,262	4,375	4,041	31,663	1,867
Total	35,282	35,282	11,238	11,238	8,420	8,420	11,530	11,530	43,813	43,813
By maturity										
At up to one year [3]	14,468	28,884	–2,259	8,920	–2,332	17,717	2,281	12,729	25,418	54,443
At over one year	20,814	2,135	13,497	–3,950	10,752	–8,053	9,249	–3,917	18,395	–6,643
Not broken down [4]	–	4,263	–	6,268	–	–1,244	–	2,717	–	–3,987
Total	35,282	35,282	11,238	11,238	8,420	8,420	11,530	11,530	43,813	43,813

Source : NBB.

[1] Belgian and foreign credit institutions and monetary authorities.

[2] Transactions carried out with institutional investors operating in Belgium have been reclassified in the companies sector.

[3] Including fixed-term advances at over one year with a variable interest rate.

[4] Instruments whose maturity is not known.

TABLE XVIII — NEW LIABILITIES OF INSTITUTIONAL INVESTORS OPERATING ON THE BELGIAN MARKET

(Changes, in millions of euro)

	Undertakings for collective investment [1]	Pension funds	Insurance companies		Total [2]
			Life branches	Other branches	
1993	14,020	324	2,197	599	16,599
1994	3,196	177	3,007	538	6,699
1995	341	474	5,299	296	6,435
1996	4,747	574	5,282	656	10,549
1997	9,602	526	7,364	546	16,575
1998	19,998	493	8,197	569	26,578
First nine months					
1998	17,141		6,986		22,201
1999 e	12,011		8,040		18,103
p.m. Outstanding amount at the end of September 1999 e	*115,708*		*87,805*		*192,130*

Sources: Luxembourg Insurance Commissariat, BFC, ISO, Belgian Pension Funds Association, Belgian Association of Collective Investment Undertakings, NBB.
[1] Including undertakings for investment in claims.
[2] Excluding double counting resulting from liabilities of institutional investors in other institutional investors.

TABLE XIX – NET ISSUES OF SECURITIES BY COMPANIES AND GENERAL GOVERNMENT

(Millions of euro)

	Companies					General governement			Grand total
	Fixed interest securities	Shares [1 2]			Total	Treasury certificates [3]	Bonds [4]	Total	
		Listed shares	Unlisted shares	Total					
1993	593	568	6,031	6,599	7,192	–5,389	8,567	3,179	10,371
1994	–600	1,017	5,559	6,576	5,975	10,693	–309	10,384	16,360
1995	1,996	254	6,109	6,363	8,359	–8,764	24,824	16,060	24,419
1996	1,395	2,487	4,294	6,781	8,177	5,672	3,643	9,315	17,492
1997	56	2,205	7,070	9,275	9,331	958	5,321	6,279	15,610
1998	620	2,912	7,748	10,661	11,281	–5,558	7,290	1,732	13,013
First nine months									
1998	1,263	2,197	5,073	7,269	8,533	1,727	2,938	4,665	13,198
1999	7,255	4,251	8,996	13,247	20,502	881	7,720	8,601	29,103
p.m. Outstanding amount at the end of September 1999	*25,931*	*172,698*	*287,881*	*460,579*	*486,511*	*40,646*	*209,915*	*250,561*	*737,072*

Sources : BFC, NBB.

[1] Including shares issued by credit institutions and the exercise of warrants.

[2] Issues are valued on the basis of the recordings of the documents relating to the formation of companies or to capital increases or reductions published in the *Moniteur belge/Belgisch Staatsblad*.

[3] Including Treasury bills and commercial paper at up to one year issued by the communities and regions and the social security system.

[4] Including commercial paper at over one year issued by the communities and regions and the social security system.

TABLE XX — MAIN INTEREST RATES

(End-of-quarter rates)

		Money market rates			Rates of the ten-year reference linear bond	Creditor rates[3]			Debtor rates[3]			
		Interbank market		Three-month Treasury certificates		Regulated savings deposits[4]	Three-month time deposits	Five-year notes	Overdraft	Six-month fixed-term advances	Five-year investment credits	Mortgage loans
		Overnight[1]	Three month[2]									
1995	I	5.45	5.75	5.64	8.05	4.72	5.08	7.51	9.69	6.60	9.36	8,41
	II	4.53	4.75	4.65	7.55	4.07	4.08	6.01	8.29	5.60	8.07	7,75
	III	4.13	4.34	4.27	7.19	3.80	3.59	5.76	8.01	5.19	7.75	7,20
	IV	3.76	3.80	3.71	6.69	3.82	3.16	5.50	7.75	4.54	7.34	6,63
1996	I	3.31	3.37	3.28	6.80	3.12	2.71	5.73	7.30	4.32	7.22	6,31
	II	3.21	3.35	3.27	6.80	3.10	2.77	5.45	7.28	4.38	7.25	6,42
	III	3.02	3.12	3.04	6.23	3.13	2.55	5.02	7.00	3.98	6.75	6,41
	IV	3.03	3.11	3.04	5.86	2.84	2.51	4.72	7.02	4.01	6.29	5,64
1997	I	3.23	3.39	3.33	5.96	2.82	2.76	4.50	7.02	4.31	6.53	5,05
	II	3.37	3.35	3.27	5.75	2.83	2.77	4.51	7.02	4.22	6.23	5,49
	III	3.73	3.71	3.60	5.61	2.84	3.01	4.61	7.01	4.65	6.42	5,48
	IV	3.80	3.67	3.60	5.39	2.84	3.03	4.67	7.26	4.76	6.49	5,88
1998	I	3.63	3.71	3.68	5.07	2.83	3.03	4.32	7.29	4.70	6.19	5,41
	II	3.61	3.72	3.65	4.93	2.83	3.13	4.41	7.26	4.68	6.24	5,54
	III	3.31	3.52	3.45	4.19	2.86	2.97	3.72	7.26	4.41	5.46	5,45
	IV	3.45	3.27	3.08	4.06	2.65	2.75	3.38	7.27	4.05	5.12	5,01
1999	I	2.99	2.97	2.84	4.25	2.60	2.48	3.36	7.02	3.75	5.10	4,71
	II	2.76	2.67	2.54	4.79	2.61	2.18	3.57	6.52	3.63	5.28	4,95
	III	2.63	3.09	2.57	5.40	2.58	2.39	4.36	6.52	3.93	6.21	5,58
	IV	3.75	3.34	3.20	5.58	2.58	2.71	4.70	6.95	4.32	6.51	6,09

Sources: ECB, NBB.

[1] Until 1998, the average overnight interest rate for the franc on the Belgian interbank market. From 1999 onwards, the weighted average overnight interest rate for the euro on the interbank market of the euro area (Eonia).

[2] Until 1998, the average interest rate offered on the Belgian interbank market for three-month deposits in francs (Bibor). From 1999 onwards, the average interest rate offered on the interbank market of the euro area for three-month deposits in euros (Euribor).

[3] Rates obtained by means of a survey conducted among the main credit institutions and weighted by the market share of each of these institutions.

[4] In 1995 the figure shown is the basic interest rate plus either the fidelity bonus or the growth bonus, whichever is the higher, plus a co-operative member bonus, where appropriate. From 1996 onwards, the figure is the basic rate plus the fidelity bonus.

[5] Owing to a redefinition of the reference contract, the interest rate shown from 1996 onwards is no longer fully comparable.

TABLE XXI – INTEREST RATES OF THE EUROSYSTEM

(Annual percentages, dates of change)

		Rate on the main refinancing transactions [1]	Rate on the marginal lending facility	Rate on the deposit facility	Rate on longer-term refinancing transactions [2]
1999	1 January	–	4.50	2.00	–
	4 January [3]	–	3.25	2.75	–
	5 January	3.00	"	"	–
	13 January	–	"	"	3.08
	22 January [3]	–	4.50	2.00	–
	24 February	–	"	"	3.04
	24 March	–	"	"	2.97
	9 April [4]	–	3.50	1.50	–
	13 April [4]	2.50	"	"	–
	28 April	–	"	"	2.54
	30 June	–	"	"	2.64
	28 July	–	"	"	2.66
	29 September	–	"	"	2.67
	27 October	–	"	"	3.42
	5 November [5]	–	4.00	2.00	–
	8 November [5]	3.00	"	"	–
	24 November	–	"	"	3.27
	22 December	–	"	"	3.29

Source : ECB.

[1] Rate of the weekly allotments allocations of two-week credits.

[2] Weighted average rate of the monthly allotments of three-month credits. This rate is of no significance for monetary policy.

[3] On 22 December 1998 the ECB announced that, as an exceptional measure, a corridor of 50 basis points would be applied between the rate of the marginal lending facility and that at the deposit facility for the period from 4 to 21 January 1999, to facilitate the transition of market operators to the new regime.

[4] Change announced on 8 April.

[5] Change announced on 4 November.

TABLE XXII – EXCHANGE RATES[1]

(National monetary units per ecu or euro, annual averages)

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
US dollar	1.273	1.239	1.298	1.171	1.190	1.308	1.270	1.134	1.121	1.273
Pound sterling	0.714	0.701	0.738	0.780	0.776	0.829	0.814	0.692	0.676	0.714
Japanese yen	183.7	166.5	164.2	130.1	121.3	123.0	138.1	137.1	146.4	183.7
Swiss franc	1.762	1.772	1.818	1.730	1.621	1.546	1.568	1.644	1.622	1.762
Swedish Krona	7.521	7.479	7.533	9.122	9.163	9.332	8.515	8.651	8.916	7.521
Korean won[2]	906.3	912.7	1,015.6	941.7	957.0	999.7	1,007.9	1,069.8	1,568.9	906.3
Hong Kong Dollar[2]	9.930	9.638	10.027	9.047	9.168	10.011	9.684	8.750	8.695	9.930
Danish Krone	7.857	7.909	7.809	7.594	7.543	7.328	7.359	7.484	7.499	7.857
Singapore dollar[2]	2.307	2.142	2.110	1.890	1.810	1.833	1.765	1.678	1.876	2.307
Canadian dollar	1.485	1.420	1.569	1.511	1.625	1.795	1.731	1.569	1.665	1.485
Norwegian Krone	7.949	8.017	8.042	8.310	8.374	8.286	8.197	8.019	8.466	7.949
Greek drachma	201.4	225.2	247.0	268.6	288.0	303.0	305.5	309.4	330.7	201.4
Australian dollar	1.630	1.591	1.769	1.724	1.625	1.765	1.623	1.528	1.787	1.630
p.m. Effective exchange rate for the euro[3] *(indice 1990 = 100)*	*100.0*	*97.0*	*99.9*	*94.6*	*93.2*	*97.8*	*98.2*	*90.4*	*92.3*	*100.0*

Source: ECB.

[1] Until 1998, exchange rate for the ecu. From 1999 onwards, exchange rate for the euro.

[2] As the ECB does not provide reference rates, the rates shown in the table are indicative.

[3] Data compiled on the basis of the weighted averages of the bilateral exchange rates for the euro. The weightings are calculated from the trade in manufactured products done between 1995 and 1997 with the trading partners whose currencies appear in the table and take account of the effects of third markets.

TABLE XXIII – IRREVOCABLE CONVERSION RATES OF THE EURO

(National monetary units)

Belgian franc / Luxembourg franc	40.3399
German mark	1.95583
Spanish peseta	166.386
French franc	6.55957
Irish punt	0.787564
Italian lira	1.936.27
Netherlands guilder	2.20371
Austrian schilling	13.7603
Portuguese escudo	200.482
Finnish markka	5.94573

Source: EC.

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