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COMMISSION STAFF WORKING DOCUMENT

Analysis of the Draft Budgetary Plan of BELGIUM

Accompanying the document

COMMISSION OPINION

on the Draft Budgetary Plan of BELGIUM

{C(2013) 8000 final}

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COMMISSION OPINION

on the Draft Budgetary Plan of BELGIUM

1. INTRODUCTION

Belgium submitted its Draft Budgetary Plan (DBP) for 2014 on 15 October 2013 in compliance with Reg. 473/2013 of the Two-Pack. Belgium also submitted a report on effective action on 20 September 2013 as recommended by the Council in June 2013.

Belgium is currently subject to the corrective arm of the Pact. The Council opened the Excessive Deficit Procedure for Belgium on 2 December 2009 and recommended to correct the excessive deficit by 2012 at the latest. On 21 June 2013 the Council decided that Belgium had not taken effective action in compliance with the Council's recommendations and decided to give notice. Belgium was given a deadline of 21 September 2013 to take effective action to ensure a sustainable correction of the excessive deficit by 2013. The Council also decided that Belgium shall present structural measures for 2014 which ensure a sustainable correction of the excessive deficit and appropriate progress towards its medium-term objective.

After the correction of the excessive deficit, Belgium will be subject to the preventive arm of the Pact and should ensure sufficient progress towards its medium-term objective (MTO). As the debt ratio in 2013 is projected at 100.4% of GDP, exceeding the 60% of GDP reference value, during the three years following the correction of the excessive deficit which is expected for 2013, Belgium will be subject to the transitional arrangements as regards compliance with the debt criterion. In this period, it should ensure sufficient progress towards compliance.

Section 2 of this document presents the macroeconomic outlook underlying the Draft Budgetary Plan and provides an assessment based on the Commission Forecast. The following section presents the recent and planned fiscal developments, according to the Draft Budgetary Plan, including an analysis of risks to their achievement based on Commission Forecast. In particular, it also includes an assessment of the measures underpinning the Draft Budgetary Plan. Section 4 assesses the recent and planned fiscal developments in 2013-2014 (also taking into account the risks to their achievement) against the obligations stemming from the Stability and Growth Pact. Section 5 summarises the main conclusions of the present document.

2. MACROECONOMIC DEVELOPMENTS UNDERLYING THE DRAFT BUDGETARY PLAN

The macroeconomic scenario underpinning the 2014 Draft Budgetary Plan (DBP) assumes that after a shallow contraction in 2012 (-0.1% of GDP), an equally modest expansion will be

recorded in 2013 (+0.1% of GDP). This development also corresponds to the scenario outlined in the Commission 2013 Autumn Forecast (AF). The main difference between the underlying components concerns a smaller contraction of gross fixed capital formation (-2.3% in DBP vs. -2.6% in AF) and a less marked drop in imports growth (-0.1% in DBP vs. -0.4% in AF). The latter changes the underlying growth composition with net exports contributing less than projected in the AF (0.3 pp. in DBP vs. 0.5 pp. in AF). Overall differences are, however, marginal.

Table 1. Comparison of macroeconomic developments and forecasts

	2012	2013			2014		
	COM	SP	DBP	COM	SP	DBP	COM
Real GDP (% change)	-0.1	0.2	0.1	0.1	1.5	1.1	1.1
Private consumption (% change)	-0.3	0.3	0.4	0.5	0.9	0.8	1.2
Gross fixed capital formation (% change)	-2.0	-1.1	-2.3	-2.6	1.7	0.6	1.0
Exports of goods and services (% change)	1.8	0.5	0.2	0.2	3.1	3.6	4.2
Imports of goods and services (% change)	1.3	0.4	-0.1	-0.4	2.5	3.4	4.1
<i>Contributions to real GDP growth:</i>							
- Final domestic demand	-0.2	0.1	-0.2	-0.2	1.0	0.8	1.0
- Change in inventories	-0.4	0.0	0.0	-0.2	0.0	0.0	0.0
- Net exports	0.4	0.1	0.3	0.5	0.6	0.3	0.2
Output gap ¹	-1.1	-1.9	-1.8	-1.7	-1.4	-1.6	-1.5
Employment (% change)	0.2	0.0	-0.2	-0.5	0.6	0.4	0.4
Unemployment rate (%)	7.6	7.5	8.6	8.6	7.6	8.9	8.7
Labour productivity (% change)	-0.3	0.2	0.4	0.6	1.0	0.7	0.7
HICP inflation (%)	2.6	1.4	1.3	1.3	1.3	1.3	1.3
GDP deflator (% change)	1.9	1.8	1.7	2.1	1.6	1.5	1.2
Comp. of employees (per head, % change)	3.7	1.6	2.0	2.2	1.5	1.4	1.1
Net lending/borrowing vis-à-vis the rest of the world (% of GDP)	-0.3	1.8	0.9	1.1	2.8	1.3	1.0
<p>Note:</p> <p>¹In percent of potential GDP, with potential GDP growth recalculated by Commission services on the basis of the programme scenario using the commonly agreed methodology.</p> <p>Source :</p> <p>Stability programme (SP); Draft Budgetary Plan (DBP); Commission services' 2013 Autumn Forecast (COM); Commission services' calculations.</p>							

Also with regard to 2014 the Draft Budgetary Plan and the Commission 2013 Autumn Forecast project a similar economic growth, at 1.1%. This compares to +1.5% in the Stability Programme as a consequence of lower investment and higher import growth projections. Individual components are generally assessed to increase somewhat more slowly than foreseen in the AF. Private consumption would grow by 0.8% (1.2% in AF), which is consistent with a more negative assessment of labour market dynamics. The largest difference between both scenarios regards trade, with exports forecast to rise by 3.6% (4.2% in AF) and imports by 3.4% (4.1% in AF). Overall this means that the Draft Budgetary Plan assumes a slightly higher contribution from net exports to overall growth (0.3 pp. vs. 0.2 pp. in AF).

With regard to inflationary pressures both scenarios are in line with HICP at 1.3% in 2014, the same level as foreseen in 2013. With regard to wage growth, the difference between the Draft Budgetary Plan and the Commission forecast remains modest (+1.4% vs. +1.1% in

2014) and compensates for a higher Commission's estimate for 2013 (+2.2% vs. +2.0% in DBP). Also in terms of labour market developments, divergences remain small. Both scenarios forecast a further increase in the unemployment rate next year from the same starting point of 8.6% in 2013, although the rise in the Draft Budgetary Plan is slightly higher (+0.3 pp.) than the Commission projection (+0.1 pp.). Given a comparable employment growth projection, this reflects a different appreciation of labour force growth. Considering the relative volatility of the latter series over the past decade, this is not implausible.

All in all, it can be concluded that differences between both forecasts are limited. The macroeconomic scenario used by the Belgian authorities for their Draft Budgetary Plan can therefore be considered to be plausible.

Box 1: The macro economic forecast underpinning the budget in Belgium

Commissioned by the National Account Institute, the macroeconomic forecast underlying the Draft Budgetary Plan was prepared by the Federal Planning Bureau (FPB), providing the federal government as well as regions and communities with a common 'economic budget' that serves as a starting point.

Based on the information available to the Commission at this stage, the statutes of the FPB contain provisions supporting the independence of the institution as a body producing macroeconomic forecasts¹.

As stipulated in the Law of 21/12/1994 that constituted the FPB in its current form, supervision of the institution lies with the Prime Minister and the Minister of Economic Affairs, while guidance on its proceedings originates from the federal cabinet with also the Belgian Parliament and the Central Economic Council or the National Labour Council able to seek an evaluation by the FPB of the federal government's economic, social and environmental policies².

3. RECENT AND PLANNED FISCAL DEVELOPMENTS

3.1. Deficit developments

Belgium's Draft Budgetary Plan confirms the headline deficit target of 2.5% of GDP for 2013, in line with the 2013 Stability Programme (see Table 2). However, according to the Commission 2013 Autumn Forecast, the headline deficit is expected to reach 2.8% of GDP in 2013.

The divergence is partly explained by an expected shortfall at local level. While the Stability Programme counted on a surplus of local authorities of 0.1% of GDP in 2013, the Draft Budgetary Plan expects a deficit of 0.07% of GDP at local level. However, recent estimates

¹ See Art. 2 of *Regulation 473/2013 on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the euro area*, defining 'independent bodies' as those that are structurally independent or endowed with functional autonomy vis-à-vis the budgetary authorities of the Member State, and which are underpinned by national legal provisions ensuring a high degree of functional autonomy and accountability.

² *Wet houdende sociale en diverse bepalingen*, 21 december 1994, TITEL VIII - hervorming van het apparaat voor de statistiek en de economische vooruitzichten van de federale regering, HOOFDSTUK IV. - Het Federaal Planbureau, Art. 124-131.

point towards a deficit of almost 0.15% of GDP at that level. This is only partly offset (up to 0.03% of GDP) by a bigger effort from the federal government compared to the Stability Programme. Regions, which are in charge of the budgetary surveillance of municipalities, would possibly offset the deficit of local authorities by providing a reserve in their own budgets, but discussions on the exact amounts and internal burden sharing are still ongoing.

In addition, the Commission 2013 Autumn Forecast is slightly more pessimistic on tax revenue developments, contributing to around 0.1pp. of GDP of the difference.

For 2014, the Draft Budgetary Plan targets a headline deficit of 2.1% of GDP, compared to a deficit projection of 2.0% in the Stability Programme. This marginal revision is due to the fact that the official target is defined in structural terms, which is confirmed at 1¼ % of GDP, while the economic outlook underpinning the Draft Budgetary Plan is less buoyant than in the macro-economic scenario of the Stability Programme. In the Draft Budgetary Plan, the planned adjustment is mainly on the expenditure side, notably through a reduction in compensation of employees, intermediate consumption and investment, which is linked to the investment cycle at local level. The revenue ratio is expected to remain stable. Although new revenue measures have been announced, they compensate for one-off revenues received in 2013 and have therefore no major impact on the overall revenue ratio. The adjustment in the Stability Programme, which included only a purely indicative composition, foresaw a bigger reduction in the expenditure ratio while projecting a decrease in the revenue ratio.

According to the Commission 2013 Autumn Forecast, the general government deficit is projected at 2.6% of GDP in 2014, i.e. half a point higher than in the Draft Budgetary Plan. In line with the above-described 2013 budgetary developments, around 0.3% of GDP of the difference with the target is due to the base effect stemming from the different outcome projected for 2013. Based on past trends, the Autumn Forecast also projects a higher growth in government expenditure, in particular in social payments and subsidies. In addition, the Autumn Forecast does not count on a further reduction in public investment in 2014, in contrast to the Draft Budgetary Plan. Lastly, there are minor differences in the estimated impact of measures.

Given that the general government target is set in structural terms, a worse than expected macro-economic outcome may push up the headline deficit. On the other hand, the opposite (i.e. a better than expected outcome) may also be the case, although in that case there is a risk that the budgetary margin will not be used for additional deficit reduction. An additional risk for the deficit targets is the uncertainty of the public finance situation of local authorities (see above). Lastly, in the case further interventions in the financial sector would be needed, they would put deficit and debt targets at risk.

In the Draft Budgetary Plan, the (recalculated) structural balance³ is projected to improve by 0.6 pp. of GDP in 2014 (compared to 0.5 pp. in the Stability Programme). According to Commission 2013 Autumn Forecast, the improvement is slightly below ½ pp. of GDP.

³ Cyclically adjusted balance net of one-off and temporary measures, recalculated by the Commission services on the basis of the information provided in the Draft Budgetary Plan, using the commonly agreed methodology.

Table 2. Composition of the budgetary adjustment

(% of GDP)	2012	2013			2014			Change: 2012-2014
	COM	SP	DBP	COM	SP	DBP	COM	DBP
Revenue	51.0	51.3	51.5	51.2	51.1	51.5	51.4	0.6
<i>of which:</i>								
- Taxes on production and imports	12.9	12.9	12.9	12.8	12.9	13.2	13.0	0.3
- Current taxes on income, wealth, etc.	16.5	16.8	17.0	16.7	17.3	17.4	17.2	0.9
- Capital taxes	0.8	0.9	0.9	1.0	0.8	0.8	0.9	-0.1
- Social contributions	17.1	16.9	17.1	17.0	16.8	16.9	17.0	-0.2
- Other (residual)	3.7	3.8	3.6	3.7	3.3	3.2	3.4	-0.4
Expenditure	54.9	53.8	54.1	54.0	53.0	53.7	54.0	-1.3
<i>of which:</i>								
- Primary expenditure	51.6	50.5	50.9	50.9	49.9	50.5	50.9	-1.0
<i>of which:</i>								
Compensation of employees	12.9	n.a.	12.9	12.9	n.a.	12.7	12.7	-0.2
Intermediate consumption	3.7	n.a.	3.6	3.7	n.a.	3.6	3.6	-0.1
Social payments	26.0	26.3	26.4	26.3	26.1	26.4	26.6	0.5
Subsidies	2.7	2.5	2.6	2.7	2.5	2.5	2.7	-0.2
Gross fixed capital formation	1.8	1.6	1.7	1.7	1.5	1.7	1.7	-0.1
Other (residual)	4.5	n.a.	3.7	3.6	n.a.	3.6	3.7	-0.9
- Interest expenditure	3.4	3.3	3.2	3.2	3.1	3.1	3.1	-0.3
General government balance (GGB)	-4.0	-2.5	-2.5	-2.8	-2.0	-2.1	-2.6	1.8
Primary balance	-0.6	0.8	0.6	0.3	1.2	1.0	0.5	1.6
One-off and other temporary measures	-0.3	0.3	0.4	0.4	0.0	0.1	0.0	0.4
GGB excl. one-offs	-3.6	-2.8	-3.0	-3.2	-2.0	-2.2	-2.6	1.5
Output gap ¹	-1.1	-1.9	-1.8	-1.7	-1.4	-1.6	-1.5	-0.4
Cyclically-adjusted balance ¹	-3.4	-1.4	-1.6	-1.9	-1.2	-1.3	-1.8	2.1
Structural balance (SB)²	-3.0	-1.7	-2.0	-2.2	-1.2	-1.3	-1.8	1.7
<i>Change in SB</i>	<i>0.3</i>	<i>1.1</i>	<i>1.1</i>	<i>0.8</i>	<i>0.5</i>	<i>0.6</i>	<i>0.4</i>	-
<i>Two year average change in SB</i>	<i>0.2</i>	<i>0.9</i>	<i>0.7</i>	<i>0.6</i>	<i>0.8</i>	<i>0.9</i>	<i>0.6</i>	-
Structural primary balance ²	0.4	1.6	1.2	0.9	1.9	1.8	1.3	1.4
<i>Change in structural primary balance</i>		<i>1.0</i>	<i>0.8</i>	<i>0.6</i>	<i>0.3</i>	<i>0.6</i>	<i>0.4</i>	-
Expenditure benchmark								
Applicable reference rate ³	-	-	-	-	0.17	0.17	0.17	-
Deviation ⁴ (% GDP)	-	-	-	-	-0.1	-0.2	0.4	-
Two-year average deviation (% GDP)	-	-	-	-	-	-	-	-

Notes:

¹Output gap (in % of potential GDP) and cyclically-adjusted balance according to the programme as recalculated by Commission services on the basis of the programme scenario using the commonly agreed methodology.

²Structural (primary) balance = cyclically-adjusted (primary) balance excluding one-off and other temporary measures.

³Reference medium-term rate of potential GDP growth. The (standard) reference rate applies from year t+1, if the country has reached its MTO in year t. A lower rate applies as long as the country is adjusting towards its MTO, including in year t. The reference rates applicable to 2014 onwards have been updated in 2013.

⁴Deviation of the growth rate of public expenditure net of discretionary revenue measures and revenue increases mandated by law from the applicable reference rate. The expenditure aggregate used for the expenditure benchmark is obtained following the commonly agreed methodology. A positive sign implies that expenditure growth exceeds the applicable reference rate.

Source:

Stability programme (SP); Draft Budgetary Plan (DBP); Commission services' 2013 Autumn Forecast (COM); Commission services' calculations.

3.2. Debt developments

In the Draft Budgetary Plan, the Belgian authorities re-affirm their commitment to limit the gross debt ratio to 100% of GDP in 2013, as already indicated in the 2013 Stability Programme. In order to reach this target, the sale of government assets would be necessary, as current deficit targets are likely to result in a higher gross debt ratio. According to the Commission 2013 Autumn Forecast, the debt ratio is currently projected to reach 100.4% of

GDP at the end of 2013. The positive impact of the reimbursement of a loan by KBC (0.5% of GDP) and the sale of Royal Park Investments (0.2% of GDP) is almost entirely offset by other stock-flow adjustments, such as the contribution by Belgium to the EFSF/ESM.

Table 3. Debt developments

(% of GDP)	2012	2013			2014		
		SP	DBP	COM	SP	DBP	COM
Gross debt ratio¹	99.8	100.0	100.0	100.4	99.0	100.2	101.3
Change in the ratio	1.8	0.2	0.2	0.6	-1.0	0.2	0.9
<i>Contributions²:</i>							
1. Primary balance	0.6	-0.8	-0.6	-0.3	-1.2	-1.0	-0.5
2. “Snow-ball” effect	1.7	1.3	1.4	1.0	0.1	0.5	0.7
<i>Of which:</i>							
Interest expenditure	3.4	3.3	3.1	3.2	3.2	3.1	3.1
Growth effect	0.1	-0.2	-0.1	-0.1	-1.5	-1.1	-1.1
Inflation effect	-1.9	-1.8	-1.7	-2.0	-1.6	-1.5	-1.2
3. Stock-flow adjustment	-0.4	-0.3	-0.6	0.0	0.1	0.7	0.7
<i>Of which:</i>							
Cash/accruals difference		n.a.	n.a.		n.a.	n.a.	
Net accumulation of financial		n.a.	n.a.		n.a.	n.a.	
<i>of which privatisation</i>							
<i>proceeds</i>		n.a.	n.a.		n.a.	n.a.	
Valuation effect & residual		n.a.	n.a.		n.a.	n.a.	

Notes:

¹ End of period.

² The snow-ball effect captures the impact of interest expenditure on accumulated debt, as well as the impact of real GDP growth and inflation on the debt ratio (through the denominator). The stock-flow adjustment includes differences in cash and accrual accounting, accumulation of financial assets and valuation and other residual effects.

Source:

Stability programme (SP); Draft Budgetary Plan (DBP); Commission services’ 2013 Autumn Forecast (COM); Commission services’ calculations.

The Draft Budgetary Plan foresees a further rise in the debt ratio in 2014, in contrast to the 2013 Stability Programme. This upward revision is mainly due to higher debt-increasing stock-flow adjustments⁴, but also because of lower GDP growth (resulting in a bigger 'snowball' effect) and a lower primary surplus. In the Commission 2013 Autumn Forecast, a stronger debt increase is projected as a result of the lower primary surplus as well as the lower nominal GDP growth, which adds to the higher basis. In addition to the risks, stemming from the government balance developments, large contingent liabilities (around 15% of GDP), mainly stemming from guarantees given to financial institutions, represent an additional risk to debt dynamics.

3.3. Measures underpinning the Draft Budgetary Plan

The Draft Budgetary Plan reports 0.4% of GDP of new revenue measures. Some of these measures already entered into force in mid-2013 in the context of the 2013 budget review with an estimated impact of 0.1% of GDP in 2013 (see section 4.1). The additional impact in 2014 is estimated at ¼ % of GDP in the Commission 2013 Autumn Forecast. New measures

⁴ The composition of stock-flow adjustments has not been reported in the DBP.

include an increase in indirect taxation (e.g. increase in excise duties on tobacco and biofuels, introduction of VAT on lawyers, etc.), as well as in direct taxation (such as the introduction of a minimum corporate income tax for companies that pay a dividend, increase in the banking tax on savings deposits). A number of limited stimulus measures have also been introduced, among others, a decrease in social security contributions and personal income tax for workers.

The Draft Budgetary Plan contains 0.7% of GDP of expenditure reductions, compared to an unchanged policy situation. From that, 0.2% of GDP of savings are foreseen in the health care system compared to the growth norm set in the coalition agreement. Partial replacement of retiring staff and lower budgets for functioning costs of ministries at both federal and sub-federal levels are expected to curb the rise in administrative expenditure (compensation of employees, intermediate consumption). The system of service vouchers will be modified in order to contain expenditure on subsidies, which has been rising rapidly in recent years. Lastly, the Draft Budgetary Plan foresees a reduction in investment, especially due to the investment cycle at local level.

In contrast to the 2012 and 2013 budget, the Draft Budgetary Plan for 2014 seems to contain only a limited number of one-off measures, which contributes to the sustainability of the consolidation effort.

Table 4. Main discretionary measures reported in the Draft Budgetary Plan**Discretionary measures taken by General Government – revenue side**

Components	Budgetary impact (% GDP) (as reported by the authorities)		
	2013	2014	2015
Taxes on production and imports	n.a.	0.2	n.a.
Current taxes on income, wealth, etc.	n.a.	0.1	n.a.
Capital taxes	n.a.	0	n.a.
Social contributions	n.a.	0	n.a.
Property Income	n.a.	0	n.a.
Other	n.a.	0.1	n.a.
Total	n.a.	0.4	n.a.
<u>Note:</u>			
The budgetary impact in the table is the aggregated impact of measures as reported in the DBP, i.e. by the national authorities. A positive sign implies that revenue increases as a consequence of this measure.			
<u>Source:</u> Draft Budgetary Plan			

Discretionary measures taken by General Government – expenditure side

Components	Budgetary impact (% GDP) (as reported by the authorities)		
	2013	2014	2015
Compensation of employees	n.a.	-0.1	n.a.
Intermediate consumption	n.a.	-0.1	n.a.
Social payments	n.a.	-0.2	n.a.
Interest Expenditure	n.a.	0	n.a.
Subsidies	n.a.	-0.1	n.a.
Gross fixed capital formation	n.a.	-0.1	n.a.
Capital transfers	n.a.	0	n.a.
Other	n.a.	-0.1	n.a.
Total	n.a.	-0.7	n.a.
<u>Note:</u>			
The budgetary impact in the table is the aggregated impact of measures as reported in the DBP, i.e. by the national authorities. A positive sign implies that expenditure increases as a consequence of this measure.			
<u>Source:</u> Draft Budgetary Plan			

4. COMPLIANCE WITH THE PROVISIONS OF THE STABILITY AND GROWTH PACT**Box 2. Council recommendations addressed to Belgium**

On 21 June 2013, the Council gave notice to Belgium under Art. 126(9) of the Treaty to correct its excessive deficit by 2013. To this end, Belgium shall reduce the headline deficit to 2.7% of GDP in 2013. This nominal improvement is consistent with an improvement in the structural balance of 1% of GDP in 2013, based on the Commission services' 2013 Spring Forecast. Belgium shall adopt and fully implement all the consolidation measures incorporated in the 2013 budget as well as additional measures of structural nature to achieve the recommended structural effort for 2013. Belgium shall stand ready to adopt further measures should risks to the budgetary plans materialise. Budgetary consolidation measures

should secure a lasting improvement in the general government structural balance in a growth-friendly manner.

On 9 July, the Council also addressed recommendations to Belgium in the context of the European Semester. In particular, in the area of public finances the Council recommended to Belgium to adopt additional measures to achieve the structural adjustment effort specified in the Council Decision to give notice to correct the excessive deficit by 2013 and to enhance the sustainability and credibility of the consolidation. A durable correction of the fiscal imbalances requires the credible implementation of ambitious structural reforms which would increase the adjustment capacity and boost potential growth. After the correction of the excessive deficit, pursue the structural adjustment at an appropriate pace so as to reach the medium-term objective by 2016 and ensure that the high debt ratio is put on a firm downward path. To this end, present growth-friendly structural measures for 2014 by 15 October 2013 which ensure a sustainable correction of the excessive deficit and sufficient progress towards its medium-term objective. Ensure that the adjustment path is balanced over time or even front-loaded. Adopt explicit coordination arrangements to ensure that budgetary targets are binding at federal level and sub-federal levels within a medium-term planning perspective including through the prompt adoption of a rule on the general government budget balance/surplus that complies with the requirements of the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union and to increase the transparency of burden sharing and accountability across government layers.

4.1. Compliance with EDP recommendations

The headline balance planned in the Draft Budgetary Plan in 2013 is below the 3% of GDP deficit reference value. According to the Commission 2013 Autumn Forecast, the headline deficit is expected to be slightly above the headline target of 2.7% of GDP set in the Council Decision to give notice of 21 June 2013 (see section 3.1).

The fiscal effort in 2013, measured by the change in the structural balance, was estimated at $\frac{3}{4}\%$ of GDP at the time of the Council Decision to give notice of 21 June 2013, following $\frac{3}{4}\%$ of measures taken in the 2013 budget, $\frac{1}{4}\%$ of GDP of additional measures taken in March 2013 and a fall in interest expenditure of around $\frac{1}{4}\%$ of GDP. Since the Council Decision, both the federal government and sub-federal entities have taken additional measures to keep their budgets on track. The change in the structural balance is currently estimated at 0.8% of GDP. However, when corrected for the downward revision in potential growth since the time of the Council Decision as well as for revenue shortfalls compared to the forecast underlying the Council Decision, the adjusted structural improvement is estimated at 1.0% of GDP, in line with the effort of 1% of GDP required by the Council.

This conclusion is supported by a bottom-up assessment which estimates the size of the additional fiscal effort for 2013 on the basis of the discretionary revenue measures and the expenditure developments between the baseline scenario underpinning the Council Decision and the Commission Autumn Forecast, which shows that since June Belgium has taken additional measures for 2013 adding up to over $\frac{1}{4}\%$ of GDP, in line with the amount of measures deemed necessary to reach the structural target spelled out in the Decision. On the revenue side, Belgium took around 0.1% of GDP of new revenue measures since the June Council Decision. These include the introduction of a minimum corporate income tax for large companies that pay a dividend, an increase in the subscription tax (i.e. a bank tax on

regulated savings deposits) a general increase in excise duties (except for tobacco and energy products) and an enlargement of the scope of the withholding tax on capital income to investment companies with variable capital (SICAVs) without EU passport.

The additional effort on the expenditure side, measured by the change in expenditure compared to the baseline scenario underpinning the June Council Decision and corrected for changes in the number of unemployed and changes in interest expenditure, is estimated at 0.5% of GDP. 0.15 pp. of the reduction is explained by new measures adopted by the federal and sub-federal entities. These include measures in the health care system and a budget reduction for development cooperation, defence and functioning costs of a number of ministries. The remaining downward revision in overall expenditure is due to a re-assessment of earlier measures and a slower increase in expenditure items under the control of the government compared to the baseline scenario, also thanks to a procedure of budgetary caution put in place. This procedure foresees in a monthly follow-up of revenues and expenditure, and administrative restrictions on non-essential expenditure.

4.2. Compliance with the debt criterion

If Belgium corrects its excessive deficit by 2013, it will enter into a three-year transition period to comply with the debt reduction benchmark. In 2014, based on an overall assessment of the Draft Budgetary Plan, Belgium is making sufficient progress towards compliance with the debt criterion. Indeed, based on the Commission 2013 Autumn Forecast, the improvement in the structural balance in 2014 exceeds the minimum linear structural adjustment ensuring the compliance with the debt criterion at the end of the transition period.

Table 5. Compliance with the debt criterion

	2012	2013	2014
		COM ¹	COM ¹
Gap to the debt benchmark ^{2,3}	n.r.	n.r.	n.r.
Structural adjustment ⁴	n.r.	n.r.	0.45
<i>To be compared to:</i>			
Required adjustment ⁵	n.r.	n.r.	0.33
Notes: ¹ Assessment of the consolidation path according to 2013 COM Autumn Forecast and assuming growth follows COM projections. ² Not relevant for Member States that were subject to an EDP procedure in November 2011 and for a period of three years following the correction of the excessive deficit. ³ Shows the difference between the debt-to-GDP ratio and the debt benchmark. If positive, projected gross debt-to-GDP ratio does not comply with the debt reduction benchmark. ⁴ Applicable only during the transition period of three years from the correction of the excessive deficit for EDP that were ongoing in November 2011. ⁵ Defines the remaining annual structural adjustment over the transition period which ensures that - if followed – Member State will comply with the debt reduction benchmark at the end of the transition period, assuming that COM budgetary projections for the previous years are achieved. Source: <i>Commission services' 2013 Autumn Forecast (COM); Commission services' calculations.</i>			

4.3. Adjustment towards the MTO

According to the Draft Budgetary Plan, the change in the (recalculated) structural balance is appropriate, at 0.6% of GDP. However, based on the projections in the Commission 2013 Autumn Forecast, the change is estimated at 0.4% of GDP, just below the required minimum

annual structural adjustment towards the MTO of 0.5% of GDP and below the improvement underlying the calendar for convergence. The difference between both projections stems from the different assessment of the headline deficit (mainly on the expenditure side), while the assessments of the cyclical impact and of the size of one-off measures are broadly concurring. Even if the deviation is not judged to be significant in 2014, it may contribute to a significant deviation the following year. To sum up, although 'taken at face value' progress is appropriate, there is a risk that the structural balance will not show sufficient progress towards the MTO.

According to the information provided in the Draft Budgetary Plan, the growth rate of government expenditure, net of discretionary revenue measures, in 2014 is expected to contribute to an annual structural adjustment towards the MTO by 0.5% of GDP. This is because the growth rate of this expenditure is below 0.17%, the lower rate under the expenditure benchmark. However, the Commission Autumn Forecast shows an expenditure growth, net of discretionary revenue measures, above this reference rate, which indicates a risk that the expenditure benchmark will not be respected. The divergence with the Draft Budgetary Plan is primarily due to higher expenditure growth projections for 2014, but also to a lower estimate of discretionary revenue measures (see section 3.1). The negative impact on the structural balance (measured by the ratio of the excess of expenditure increase to GDP) is estimated at 0.35pp. of GDP. The deviation is therefore not considered significant.

Following an overall assessment of the Belgium's Draft Budgetary Plan, with the structural balance as a reference, including an analysis of expenditure net of discretionary revenue measures, a deviation from the adjustment path towards the MTO is to be expected in 2014 which, if repeated the following year, could be assessed to be significant and could put the compliance with the requirements of the preventive arm of the Pact at risk.

4.4. Other considerations

On 9 July, the Council also addressed recommendations to Belgium in the context of the European Semester. In particular, in the area of public finances the Council recommended to Belgium to adopt explicit coordination arrangements to ensure that budgetary targets are binding at federal and sub-federal levels within a medium-term planning perspective, including through the prompt adoption of a rule on the general government budget balance/surplus that complies with the requirements of the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union and to increase the transparency of burden sharing and accountability across government layers.

On 17 July 2013, the federal government and sub-federal entities agreed on a burden sharing of the general government target for 2014. However, this agreement does not yet take into account the worse than expected situation at local level.

In the medium term, the ongoing sixth reform of the state will thoroughly modify fiscal relations among the different layers of government. In this context, the draft law revising the *Special Finance Law on the Financing of Regions and Communities*, which is expected to be adopted in Parliament before the end of 2013, foresees a contribution of sub-federal entities to the consolidation through a gradual lump-sum reduction in transferred tax revenues between 2014 and 2016. In the longer term, regions and communities are also expected to pay a steadily rising contribution to the pension burden of their own statutory staff. However, the planned further decentralisation of responsibilities and increased tax autonomy of regions, also calls for more explicit coordination arrangements on budgetary targets. However, the Draft Budgetary Plan makes no reference to the adoption of such arrangements and progress

so far seems to be limited. The Council Decision to give notice of 21 June 2013 requires Belgium to submit a report by 31 December 2013 on the intended implementation of the European Semester recommendation on this issue.

The Council also recommended Belgium to shift taxes from labour to less growth-distortive tax bases. Overall, new revenue measures avoid tax increases on labour income, but there is no substantial shift from taxes away from labour. Finally, the Council recommended to simplify the tax system by reducing tax expenditures in income taxation, increasing VAT efficiency and improving tax compliance by closing existing loopholes. A draft law containing a number of procedural simplifications has been tabled outside the context of the 2014 budget. A Green Paper on a more far-reaching tax reform is currently being prepared, but no fundamental reforms are expected before the 2014 parliamentary elections.

5. SUMMARY

Belgium is not expected to reach the headline deficit target set in the Council Decision to give notice of 21 June 2013, but the deficit is projected below 3% of GDP. Moreover, the fiscal effort in 2013 adjusted for changes in potential growth estimates and revenue shortfalls is in line with the fiscal effort recommended by the Council.

In 2014, Belgium is projected to make sufficient progress towards compliance with the debt criterion. Progress towards the Medium Term Objective is appropriate when taken at face value. However, the Commission 2013 Autumn Forecast points to a risk that the structural balance will not show sufficient progress towards the MTO in 2014, although the structural improvement will be close to the required effort. Even if the deviation is not judged to be significant in 2014, it may contribute to a significant deviation the following year.

While the burden sharing of the 2014 consolidation effort between federal and sub-federal levels has been agreed, no further explicit coordination arrangements have been adopted so far.

Annex. EDP related tables

Table A1. Baseline scenario underlying the EDP recommendation

<i>% of GDP</i>	2013
Revenues	51.1
Current revenues	50.1
Discretionary measures with impact on current revenue	0.2
Expenditure	54.2
Real GDP growth (%)	0.0
Nominal GDP growth (%)	1.7
Potential GDP growth (%)	0.9
Structural balance	-2.3
General government balance	-2.9
<i>p.m CAB methodology revenue elasticity</i>	0.94
<i>p.m Apparent revenue elasticity</i>	1.08
<i>p.m Output gap (% of potential output)</i>	-1.9

Source: Commission Staff Working Document accompanying the Recommendation for a Council Decision giving notice to Belgium to take measures for the deficit reduction judged necessary in order to remedy the situation of excessive deficit and the Recommendation for a Council Decision establishing that no effective action has been taken by Belgium in response to the Council Recommendation of 2 December 2009.

Table A2. EDP scenario underlying the EDP recommendation

<i>% of GDP</i>	2013
Real GDP growth (%)	0.0
Potential GDP growth (%)	0.9
Structural balance	-2.0
General government balance	-2.7
<i>p.m Output gap (% of pot. output)</i>	-2.0

Source: Commission Staff Working Document accompanying the Recommendation for a Council Decision giving notice to Belgium to take measures for the deficit reduction judged necessary in order to remedy the situation of excessive deficit and the Recommendation for a Council Decision establishing that no effective action has been taken by Belgium in response to the Council Recommendation of 2 December 2009.

Table A3. Current estimates of the macroeconomic and fiscal developments

<i>% of GDP</i>	2013
Revenues	51,2
Current revenues	50,2
Discretionary measures with impact on current revenue	0,2
Expenditure	54,1
Real GDP growth (%)	0,1
Nominal GDP growth (%)	2,2
Potential GDP growth (%)	0,7
Structural balance	-2,2
General government balance	-2,8
<i>p.m CAB methodology revenue elasticity</i>	0,94
<i>p.m Apparent revenue elasticity</i>	0,95
<i>p.m Output gap (% of potential output)</i>	-1,7

Source: Commission services' 2013 Autumn Forecast

Table A4. Adjustment of apparent structural effort for the revision in potential growth – details of calculation

	Potential GDP growth underlying the Council Recommendation (%)	Potential GDP growth at the time of assessment (%)	Forecast error (%)	Structural expenditure (% of potential GDP)	Correction coefficient α (% of nominal potential GDP)
	(1)	(2)	(3)=(1)-(2)	(4)	(5)=(3)*(4)/100
2013	0.9	0.7	0.1	53.0	0.1

Source: Commission services' 2013 Autumn Forecast

Table A5. Adjustment of apparent structural effort for the revision in revenue shortfalls/windfalls – details of calculation

	Change in current revenues (yoy) (billions of national currency)		Discretionary current revenue measures (billions of national currency)		Nominal GDP growth assumptions (%)		Current revenues in year t-1 (billions of national currency)		Revenue gap (billion of national currency)*	Correction coefficient β (% of nominal potential GDP)
	2013 EDP	2013 AF	2013 EDP	2013 AF	2013 EDP	2013 AF	2013 EDP	2013 AF		
	(1)	(1')	(2)	(2')	(3)	(3')	(4)	(4')	(5)=[(1')-(2')- $\varepsilon^*(3')*(4')$]- [(1)-(2)- $\varepsilon^*(3)*(4)$]	
2013	4.1	4.8	0.8	0.9	1.7	2.2	187.7	187.9	-0.4	-0.10

Source: Commission services' 2013 Autumn Forecast