

The incomes and financing balance of individuals and companies

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Introduction

In Belgium, the share of wages in GDP has declined quite sharply over the past five years, the main counterpart being a growing share for the operating surplus. These developments have attracted close attention of late, with frequent references to a shift in incomes from individuals to firms. Against the current backdrop of rising inflation, such discussions often mention a possible fall in the purchasing power of individuals. However, a downward trend in the wage share does not necessarily imply a fall in the incomes and purchasing power of individuals. It merely reflects a weaker relative rise in wages compared to the total income generated by the economy. In any case, wages are not the only income category for individuals: their income from wealth, such as interest and dividends, must also be taken into account, as must social benefits and taxes.

This article aims to promote the objectivity of this social debate, partly by clarifying exactly what lies behind such concepts as wage share, operating surplus and corporate profit. In addition, the recent decline in the wage share raises a number of questions which this article aims to answer in the light of a historical and international comparison. How is value added divided among the various primary income categories, namely wages, indirect taxes and residual operating surplus? Has the recent contraction of the share of wages in value added reduced the wage share to an exceptionally low level? Was it followed by a redistribution of incomes, e.g. between companies and individuals? Have individuals and companies adjusted their spending in line with their change in income, or are all the changes absorbed by more saving or dissaving?

The distribution and allocation of incomes are analysed on the basis of the national accounts data, which offer a systematic description of the various phases in the economic process: production, income formation, income distribution and income allocation. The official NAI data on the sectoral accounts are available only for the period 1995-2006; for 2007, the analysis is based on the spring projections which the Bank produced recently as part of the common, biannual exercise conducted by the Eurosystem central banks⁽¹⁾.

This article is structured as follows. Section 1 concerns the formation of incomes as a direct result of the production process, with a detailed examination of movements in the wage share, i.e. the share of value added which is paid out in the form of wages. Then follows an analysis of the redistribution of income between sectors and the purposes for which the economic agents use their income. Section 2 focuses this analysis on individuals, examining in turn their disposable income, their savings ratio and their financing balance. Section 3 contains a similar analysis for companies, focusing mainly on their gross operating surplus and their financing balance. Finally, the main findings of this study are summarised in the conclusion.

(1) For more information on the Bank's spring projections and the underlying assumptions, see NBB (2008), "Economic projections for Belgium – Spring 2008", Economic Review, June, 7-28. The NAI will not publish the official data for 2007 until the end of September 2008.

1. Formation of incomes as a direct result of the production process

This first section describes how gross domestic product, i.e. total value added, is generated and how that value added is distributed between the production factors (labour and capital) and general government (via net indirect taxes, i.e. after deduction of subsidies). It analyses the income flows from the point of view of the sector generating the output.

Since it is not possible to consider all economic agents individually, they are grouped into “institutional sectors” in the national accounts, on the basis of their principal activity. For the analysis in this article, some of these sectors are aggregated, leaving three main domestic sectors, namely companies, individuals and general government. The companies sector comprises both financial and non-financial corporations. The individuals sector covers not only households, including self-employed workers, but also non-profit institutions serving households⁽¹⁾. Companies and individuals together form the private sector, i.e. the total economy excluding general government.

1.1 The creation of value added

In order to make a product, a producer uses not only the production factors labour and capital, but also commodities, intermediate products and services supplied by other producers. To avoid double counting, the value added of an individual producer is defined as the value which he adds to the commodities, intermediate products and services of other producers which he uses, with the aid of his own workers and equipment. The value added can therefore be calculated as the difference between the sale value of the output and the amounts paid to other producers for the supply of commodities, intermediate products and services, known as intermediate consumption⁽²⁾.

Since the principal activity of companies consists in producing market goods and services, it is not surprising that they create more value added than individuals and general government. The relative share of companies in total value added has risen steadily over the past ten years. In 2006, companies generated total gross value added of 190.6 billion euro, representing 60.2 p.c. of GDP at current prices, compared to 57.9 p.c. in 1996. While the value added of companies showed an annual average increase of 4.5 p.c. between 1996 and 2006, GDP increased by an average of 4.1 p.c. per annum at current prices.

This weaker GDP growth was due mainly to the fact that the value added created by individuals grew less rapidly during that period. Although this reduced the share of individuals from 17.8 p.c. of GDP in 1996 to 15.4 p.c. in 2006, the value added created by individuals still represented 48.7 billion euro in 2006. That value added originates mainly from the activity of self-employed workers (totalling 23.3 billion euro) and the production of housing services, whether or not for own use (totalling 22.2 billion euro). It is mainly the value added of self-employed workers that has grown more slowly in the past ten years, at an annual average of 1.9 p.c. compared to 3.1 p.c. for the production of housing services. This is due largely to a decline in the number of self-employed workers, which dropped from a total of around 711,000 in 1996 to 679,000 in 2003, before climbing back to 695,000 in 2006.

Of these three main domestic sectors, it is general government that generates the lowest value added. In 2006, the value added of the public sector came to 42.6 billion euro or 13.5 p.c. of GDP. In the past ten years, it has fluctuated between 13 and 14 p.c. of GDP without displaying any clear trend.

1.2 Incomes arising from value added

Producers use the value added created to pay their labour costs and net indirect taxes, i.e. after deduction of subsidies. The national accounts define the remainder as the surplus (or deficit) resulting from production activity, known as the sector's gross operating surplus: this can be viewed as remuneration for the capital used. For self-employed workers, who belong to the individuals sector, the remainder also implicitly contains the labour income for work carried out by the owners or by members of their family. Since that income cannot be distinguished from the operating profit made by them as entrepreneurs, the remainder is referred to as mixed income.

In 2006, about half of the gross value added of the Belgian economy as a whole was used to pay for the production factor labour. The other half was divided between net indirect taxes (11.8 p.c.) and the gross operating

(1) Non-profit institutions serving households include unions, professional associations, political parties, sporting associations and charitable institutions financed by voluntary contributions from other institutional sectors.

(2) However, there are two exceptions to this general rule, namely housing services offered by individuals and non-market services offered by general government. The gross value added which individuals create by producing housing services is calculated as the difference between the rents received (in the case of owner-occupied housing, these are imputed rents) and housing-related expenses which are generally borne by the owners (such as the cost of a plumber or electrician). The gross value added generated by general government via non-market services is calculated as the sum of labour costs and depreciation. Such services – law and order, education and infrastructure – are usually provided free of charge or at far less than cost price, so that the application of the general rule would lead to a serious underestimate of the value added of the general government sector.

surplus plus mixed income (38.2 p.c.). However, there are considerable variations between the three main domestic sectors.

The remuneration of labour as a production factor forms a very large part of the gross value added of the general government sector, at 88 p.c. Moreover, that proportion has risen steadily since the 1995 figure of 86.1 p.c. The other 12 p.c. represents the gross operating surplus, which consists mainly of depreciation. In 2006, companies paid 60.6 p.c. of the value added which they generated in the form of wages, against an average of 64.3 p.c. in the 1995-2002 period. The main counterpart of the recent contraction in the wage share in the value added of companies lies in the share of the gross operating surplus, which came to 39.4 p.c. of value added in 2006, against an average of 35.1 p.c. between 1995 and 2002. Finally, individuals used only 10.6 p.c. of the value added which they created to pay for the production factor labour (for domestic staff and for employees of self-employed workers). The major part – namely 83.9 p.c. – of the value added of individuals corresponds to their gross operating surplus and mixed income.

1.3 The wage share

The wage share reflects the way in which incomes resulting directly from the production process are divided between the production factors. The economic debate, particularly that between the social partners, therefore pays close attention to this concept, especially if the wage share is changing significantly, as in the last few years.

1.3.1 Various possible definitions

The *wage share in the total economy* is often defined as the ratio between the wages paid by the three main domestic sectors combined and GDP. According to that definition, during the period 1995-2000 the wage share hovered around 51 p.c. of GDP, then increased to a peak of 52.4 p.c. of GDP in 2002, before subsiding to an average of 50.2 p.c. between 2005 and 2007.

The advantage of this concept is that it is very easy to calculate with a minimum of data, but it is also subject to various limitations. For instance, it is better to disregard net indirect taxes if the aim is to focus on the distribution of wealth between the production factors labour and capital. That is the only way of ensuring that the sum of the wage share and the share of the operating surplus is always equal to 1. If net indirect taxes are disregarded and the wage share is therefore *expressed as a percentage of value added at factor cost*, then on average it exceeds the wage share as a percentage of GDP by 6.8 percentage points. However, given that the net indirect taxes keep closely in step with value added, this refinement has only a minor impact on the movement in the wage share, so that it virtually parallels the wage share in GDP. In the past three years, the wage share in the total economy averaged 56.8 p.c. of value added at factor cost.

In addition, the simple definitions of the wage share make asymmetric use of the data on self-employed workers. The value added which they generate is included in GDP and in value added, but their labour income does not form part of the labour costs. This means that the

TABLE 1 BREAKDOWN OF GROSS VALUE ADDED BY SECTOR IN 2006

	Gross value added / GDP	Labour costs ⁽¹⁾		Indirect taxes after deduction of subsidies		Gross operating surplus ⁽²⁾	
	billions of euro	billions of euro	percentages of value added	billions of euro	percentages of value added	billions of euro	percentages of value added
Companies	190.6	115.5	60.6	0.1	0.0	75.0	39.4
Individuals	48.7	5.2	10.6	2.7	5.5	40.9	83.9
General government	42.6	37.5	88.0			5.1	12.0
Not broken down ⁽³⁾	34.7			34.7			
Total economy	316.6	158.2	50.0	37.5	11.8	121.0	38.2

Source: NAI.

(1) In the national accounts, labour costs include both gross wages and employers' social security contributions.

(2) For individuals and the total economy, this concerns both the gross operating surplus and gross mixed income.

(3) Unlike other taxes on production – such as taxes on pollution or taxes on the use of fixed assets for production purposes – taxes on products cannot be broken down among the various institutional sectors. This last category includes VAT, taxes on imports and excise duties.

above definitions underestimate the true share of labour income in total value added. Since the labour income of self-employed workers cannot be measured directly, an allocation formula has to be used to break down the gross mixed income of self-employed workers into a notional imputed labour income and the residual gross operating surplus. For this purpose, self-employed workers are often assigned an imputed labour income equal to the average labour costs per employee. In the period 2005-2007, the thus *adjusted wage share in the total economy* averaged 67.8 p.c. of value added. Since the relative share of self-employed workers in total employment in Belgium displayed a downward trend in the period 1997-2003, the adjusted wage share recorded a somewhat larger decline than the non-adjusted wage share. In 2002, the adjusted wage share in the total economy still came to 71.1 p.c. of value added. In international comparisons it is advisable to use such an adjusted wage share; this is because the degree to which the non-adjusted wage share underestimates the true share of labour income varies from one country to another, owing to differences in the percentage of self-employed labour in total employment.

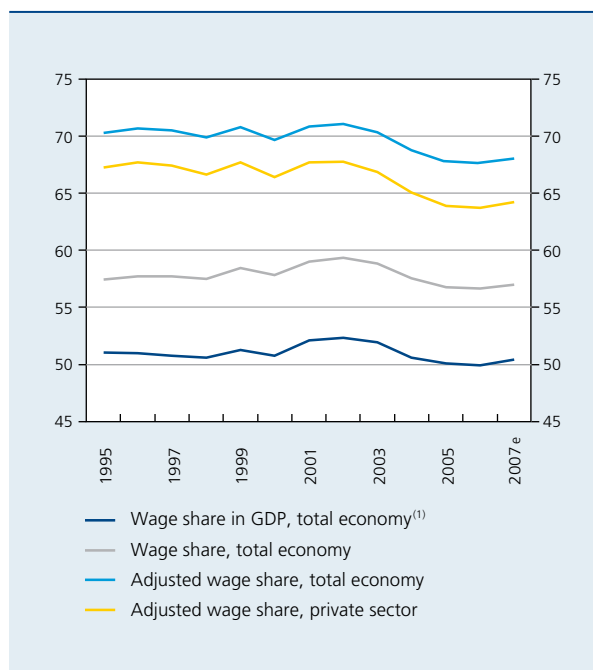
Finally, the analysis of the wage share is often confined to the private sector. For instance, the Central Economic Council calculates an *adjusted wage share in the private*

sector in its technical report on the maximum available margins for increases in labour costs. Such an indicator can be used as a synthetic yardstick for assessing the recent movement in labour costs. It can also be used, for example, to examine the impact of globalisation on the wage share. Since the share of labour costs in value added is much greater in the general government sector than in the private sector, exclusion of the former results in a wage share which is 3.4 percentage points lower, on average. In the past three years, the adjusted wage share in the private sector has averaged 64 p.c. of value added at factor cost.

The various definitions of the wage share therefore lead to substantial differences in terms of level. Of all the definitions used here, the simple concept of the wage share in the total economy (as a percentage of GDP) results in the lowest level, while the adjusted wage share in the total economy (as a percentage of value added) gives the highest level. In general, however, all the definitions indicate a similar picture: a fairly stable pattern in the second half of the 1990s followed by a moderate rise and then a slightly steeper fall during the period 2003-2005; since then there has been little change in the wage share.

1.3.2 Possible reasons for the recent movements in the wage share

CHART 1 VARIOUS DEFINITIONS OF THE WAGE SHARE
(percentages of value added at factor cost, unless otherwise stated)



Sources: NAI, NBB.
(1) Percentage of GDP.

Up to now, the wage share has been considered only as the ratio between labour income and value added. However, the wage share can also be broken down into a number of components which provide more information on what is happening. Thus, a first step is to redefine the wage share as the ratio between real wages and value added in real terms. Changes in the wage share can therefore be seen as changes in real unit labour costs. This reveals that it is not only wages and economic activity that determine the movement in the wage share, but also inflation measured by the value added deflator. Finally, the impact of the number of persons in work can be isolated by regarding the wage share as the ratio between real labour costs per employee and (apparent) labour productivity.

The adjusted wage share can therefore be written as:

$$\frac{C(T/E)}{YN} = \frac{(C/P)(T/E)}{YR} = \frac{C_E/P}{YR/T}$$

where C represents labour costs; E , is the number of employees; T , is the total number of persons in work including self-employed workers; YN , is value added at current prices; YR , is value added in real terms; P is the value added deflator and C_E , is labour costs per employee.

Consequently, real unit labour costs – and hence the adjusted wage share – will decline if real labour costs per employee rise less quickly than labour productivity. The movement in the wage share is therefore determined by numerous factors, many of which are sensitive to the business cycle. The recent movements in the wage share should therefore be analysed in the context of the global deterioration in the economic situation in 2001 – caused by the bursting of the stock market bubble and the subsequent cuts in business investment – and the economic recovery which started in 2004. In order to clarify the impact of the business cycle, this section will consider only developments in the private sector, as they are more sensitive to the cycle. However, the conclusions are the same if the total economy is considered.

Since (apparent) labour productivity is calculated here as the ratio between value added and the number of persons in work, that figure shows a strong positive correlation with the business cycle. Generally speaking, several quarters elapse before employment responds to cyclical fluctuations, as it takes time and money to adjust production capacity in line with changing prospects. The slackening pace of growth in 2001 therefore caused (apparent) labour productivity to decline by 0.1 p.c., compared to an average annual rise of 1.4 p.c. over the period 1996-2007 as a whole, or 1.5 p.c. during the period 1996-2000. This was a significant factor behind the steep increase in the adjusted wage share in 2001. During the ensuing years, labour productivity again grew relatively strongly as a result of drastic corporate restructurings which curbed the

expansion of employment, contributing to a reduction in the adjusted wage share. Combined with the incipient economic recovery in 2004, this boosted labour productivity by 2.2 p.c. in that year.

The major difference between the period 1996-2002 – which ended with a slight increase in the adjusted wage share – and the more recent period 2003-2005 concerns the movements in real labour costs per employee. Here, too, the business cycle played a very important role. In response to the deteriorating economic situation in 2001, companies tried to keep their labour costs down. In 2001 and 2002, that was achieved mainly by adjusting the number of hours worked per employee in line with the slowdown in production, via the system of temporary layoffs and by cutting the amount of overtime. This effect was in addition to the structural trend towards shorter working hours as a result of the expansion of part-time work. However, the impact on labour costs per employee was limited during those years because hourly labour costs continued rising by more than 4 p.c. per annum. In Belgium, the movement in private sector labour costs is influenced mainly by collectively agreed wages, via real agreed adjustments or indexations. Under the law on the safeguarding of competitiveness, the increase in nominal hourly labour costs is largely determined by the indicative wage norm, defined by the social partners in the biennial negotiation of a central agreement on the basis of the expected movement in labour costs in the three main trading partners – Germany, France and the Netherlands – and any adjustments for slippages in the preceding two years.

TABLE 2 BREAKDOWN OF THE ADJUSTED WAGE SHARE IN THE PRIVATE SECTOR
(percentage changes, unless otherwise stated)

	Average 1996-2000	2001	2002	2003	2004	2005	2006	2007 e
1. Number of hours worked per employee	0.1	-0.6	-0.8	-0.2	-0.4	-0.2	0.2	0.2
2. Hourly labour costs	2.1	4.3	4.2	1.6	2.5	1.8	3.0	3.7
3. Labour costs per employee (1 × 2) ..	2.2	3.7	3.5	1.4	2.1	1.6	3.2	4.0
4. Value added deflator	1.0	1.8	1.4	1.4	2.6	2.3	1.9	2.0
5. Real labour costs per employee (3:4)	1.2	1.9	2.0	0.0	-0.5	-0.7	1.3	1.9
6. Labour productivity	1.5	-0.1	1.9	1.4	2.2	1.1	1.6	1.1
7. Real unit labour costs (5:6)	-0.3	2.0	0.1	-1.4	-2.6	-1.8	-0.2	0.8
<i>p.m. Adjusted wage share (percentages of value added)</i>	67.2	67.7	67.8	66.8	65.1	63.9	63.7	64.2

Sources: NAI, NBB.

In 2001 and 2002, companies were therefore bound by the central agreement concluded at the end of 2000 and based on a more favourable economic situation expected at that time. Altogether, real labour costs per employee increased by roughly 2 p.c. per annum in 2001 and 2002, exceeding the change in labour productivity and therefore expanding the adjusted wage share.

Although the number of hours worked per employee continued to fall in subsequent years, during the period 2003-2005 it was mainly the slower rise in hourly labour costs which curbed the growth of labour costs per employee. This was due in particular to the lower indicative norms for the increase in nominal hourly labour costs during the years 2003-2004 and 2005-2006, which reflected the expected wage moderation in the three main trading partners. In addition, during 2003-2005 the wage drift was virtually non-existent, presumably because of the gradually deteriorating labour market situation. Finally, the increase in hourly labour costs was also contained by the reduction in employers' social security contributions. Overall, the rise in labour costs per employee in the private sector averaged only 1.7 p.c. per annum in 2003-2005. Moreover, in 2004 and 2005 labour costs per employee increased by less than inflation, measured by the value added deflator, so that real labour costs per employee declined by 0.5 and 0.7 p.c. respectively, after remaining virtually unchanged in 2003. Combined with an increase in (apparent) labour productivity averaging 1.6 p.c. per annum, the fall in real labour costs per employee, averaging 0.4 p.c. per annum, led to a significant decline in the adjusted wage share in the period 2003-2005.

It was therefore not until 2006 that the decline in the wage share was halted. In the past two years, real labour costs per employee have climbed back up by an average of 1.6 p.c. per annum, in the context of favourable economic conditions and rising tensions on the labour market. Not only did the number of hours worked per employee start rising, there was also a substantial increase in the wage drift. As a result, the rate of growth in real labour costs per employee was realigned with the increase in labour productivity, so that the reduction in the adjusted wage share gave way to stabilisation. In 2007, the adjusted wage share actually increased again as a result of the sharp rise in hourly labour costs.

1.3.3 Has the wage share dropped to an exceptionally low level in recent years?

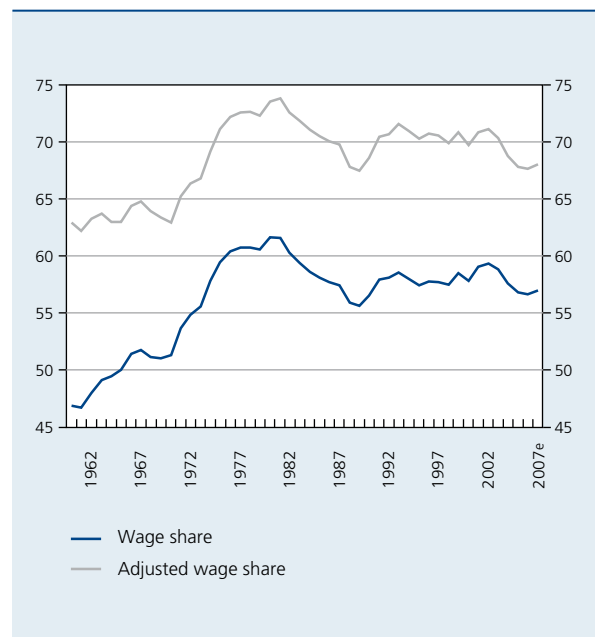
Now that the wage share has reached its lowest level for the past ten years, the question is whether that share is exceptionally low in historical terms. Considered over a longer period, the movement in the adjusted wage share

in Belgium can be divided into three phases⁽¹⁾. During the 1960s, the adjusted wage share in the total economy fluctuated around 63.5 p.c. of value added. During the 1970s, however, it increased steadily, peaking at almost 74 p.c. in 1981. It then gradually subsided to around 68 p.c. of value added.

The very marked rise in the adjusted wage share during the 1970s was attributable to a gradual slackening of labour productivity growth which was not accompanied by a slower rise in real labour costs per employee. On the one hand, the industrial countries recorded a structural slowdown in their productivity growth, a trend which was further reinforced by the oil crisis which drove up the costs of companies and exerted further downward pressure on their value added and labour productivity. Also, automatic wage indexation in Belgium meant that the oil price rises were passed on in higher wage increases which in turn fuelled inflation, triggering a "wage-price spiral". This derailment of labour costs not only dented corporate profitability in Belgium: combined with the weakening productivity growth, it also led to a steep rise in real unit labour costs and hence in the wage share. Since labour costs in Belgium rose faster than those in the main trading

(1) Figures cannot be calculated for the private sector because there have been no harmonised data per sector since 1960.

CHART 2 HISTORICAL VIEW OF THE WAGE SHARE IN THE TOTAL ECONOMY
(percentages of value added at factor cost)



Sources: EC, NBB.

partners, these developments also brought a substantial loss of competitiveness for Belgian companies.

In the early 1980s, several measures were taken to restore that competitiveness. For instance, in February 1982 the Belgian franc was devalued by 8.5 p.c. To temper the influence of that devaluation on domestic prices and costs, simultaneous measures were taken to control labour costs. To that end, the link between the increase in hourly labour costs and inflation measured by the consumer price index was temporarily abolished. In 1993, it was decided to make that link structurally less rigid, by using the "health index" as the benchmark for indexation. These measures produced the desired effect. Thanks to cost control, the expanding sales opportunities led to an increase in corporate profitability, so that value added rose faster and the wage share began gradually falling.

The recent decline in the adjusted wage share can therefore be seen as part of a downward trend since the peak of the early 1980s. The steepest fall occurred in 1982-1989, followed by a partial recovery which has now been totally dissipated. The level of the past few years is therefore comparable with that of the late 1980s. We need to go back to the early 1970s to find an adjusted wage share which is lower than the figures recorded in recent years. Although the very substantial increase in the adjusted wage share amounting to 10.6 p.c. of value added during the 1970s has not yet been entirely neutralised, rather more than half of it has since been offset by a gradual decline amounting to 5.5 p.c. of value added in the past three decades.

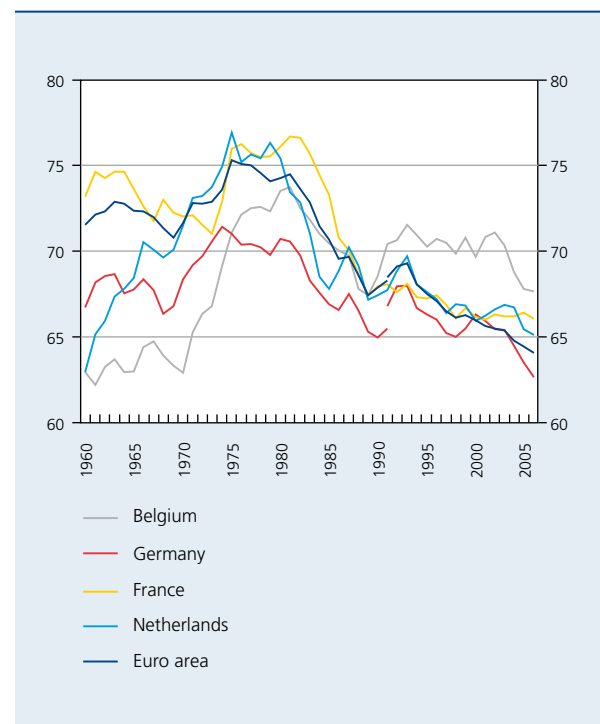
Another way of assessing the recent fall in the wage share in Belgium is to compare it with the situation prevailing in other euro area countries. When making an international comparison, it is desirable to focus mainly on the movement in the wage share rather than the level, because the level varies widely from one country to another, even if the definition is confined to the private sector and incorporates an adjustment for the labour income of self-employed workers. However, those differences of level are difficult to interpret because they are due to such factors as the structure of the economy (e.g. the relative share of the various branches of activity, or the weight of taxation and social contributions on labour income) and methodological differences in the compilation of the national accounts (such as the estimate for undeclared employment).

Compared to what is seen in most other euro area countries, the adjusted wage share has contracted relatively sharply in Belgium of late, declining from 71.1 p.c. of

value added in 2002 to 67.6 p.c. in 2006. That represents a percentage fall of 4.8 p.c. compared to a fall of only 2.2 p.c. in the euro area as a whole. However, in Germany the adjusted wage share also declined by 4.3 p.c., as a result of strict wage moderation. Conversely, in France the adjusted wage share recorded a much smaller fall. Possible reasons for that are the significant rise in the minimum wage and the steady extension of the 35-hour week. In so far as the resulting slower growth of labour productivity was not totally offset by a slower rise in real labour costs per employee, this resulted in a larger wage share.

However, if the recent decline in the adjusted wage share is viewed as part of the downward trend which began in the early 1980s, then the relationships are reversed. In comparison with most other euro area countries, the downward trend in the adjusted wage share in the total Belgian economy since 1980 has been less pronounced so far, at 8 p.c. For example, the adjusted wage share in the euro area as a whole dropped by 13.8 p.c. In Belgium's three main neighbouring countries – Germany, France and the Netherlands – the decline was 11.5 p.c., 13.2 p.c. and 13.7 p.c. respectively. Moreover, since the time series for Germany before 1991 relate only to West Germany, the

CHART 3 INTERNATIONAL COMPARISON OF THE ADJUSTED WAGE SHARE IN THE TOTAL ECONOMY
(percentages of value added at factor cost)



Source: EC.

contraction in the wage share in Germany and in the euro area as a whole is probably somewhat underestimated.

In addition, the slower downward trend in the adjusted wage share in Belgium followed a much stronger rise during the 1970s. Consequently, the adjusted wage share in the total Belgian economy is currently still 7.5 p.c. larger than in 1970, whereas in the three main neighbouring countries together and in the euro area the 2006 figures are respectively 8.3 and 10.6 p.c. lower than in 1970.

Overall, the wage share in Belgium thus exhibited a similar picture to that seen in the euro area: stabilisation in the 1960s, then an increase in the 1970s followed by a gradual decline. The synchronised nature of these trends in the wage share in most euro area countries and elsewhere suggests that the pattern was dictated mainly by common factors. In the literature, the downward trend in the wage share is often linked to structural developments such as globalisation, technological progress and the growing importance of the tertiary sector of the economy⁽¹⁾.

One of the effects of the globalisation of the economy is a marked increase in the world labour supply. Depending on the source, the integration of China, India and the former Eastern bloc countries into the global economy has doubled or even quadrupled the world labour supply compared to 1980. The impact of this additional labour is reflected mainly in a strong rise in the industrial countries' imports of labour-intensive goods and services from those emerging economies. Since the industrial countries are specialising in more capital-intensive goods and services, there will be a decline in the share of the remuneration of the relatively scarce production factor labour in total value added. At the same time, however, globalisation is stimulating productivity and output via further specialisation, so that the total wage bill is also rising. The net effect of globalisation on the total wage bill in the industrial countries therefore need not be negative.

The impact of the growing world labour supply is also felt via increasing immigration and the offshoring of certain activities, which is weakening the bargaining position of employees in the industrial countries. This offshoring was stimulated in particular by the gradual liberalisation of trade and capital movements and by technological progress, which has made it possible to divide up

successive phases in the production process and conduct them at different locations. This has made the choice of production locations much more sensitive to relative movements in labour costs in the various countries.

In addition, technological progress has also increased the capital intensity of the production process. In that context, the link between the new technologies and the workers' skills is very important. While information and communication technology (ICT) and highly-skilled workers are essentially complementary, ICT tends to be in competition with low-skilled labour. ICT has therefore tended to reduce demand for low-skilled labour and increase the productivity of highly-skilled labour. In both cases, this leads to a larger share for the remuneration of the production factor capital and a smaller wage share.

Finally, the expansion of the tertiary sector of the economy has also tended to reduce the wage share in Europe. Since the wage share is lower in the services sector than in industry, its growing importance in the value added of the total economy has caused a reduction in the average wage share. According to an EC study⁽²⁾, that effect was particularly significant in Belgium in 1986-1995, whereas since 1995 it has hardly been a factor.

2. Disposable income, savings ratio and financing balance of individuals

Broadly speaking, the primary incomes described above accrue in the first instance to individuals (in the form of wages), to general government (in the form of net indirect taxes) and to companies (what is left after paying labour costs and net indirect taxes). These primary incomes are then partly redistributed between the institutional sectors. Thus, individuals and companies pay interest on their outstanding loans, and receive interest on their savings or their bond portfolio. As shareholders, individuals also receive dividends from companies. In addition, both individuals and companies pay taxes and social contributions to general government, which uses part of these resources to finance social benefits to individuals. Finally, the three domestic sectors may also receive incomes from abroad or pay incomes to the rest of the world. The primary incomes described above, arising from domestic output, are therefore not the only factors which determine the disposable income of individuals and companies.

This section first examines the movement in the total disposable income of individuals, a concept which covers not only the wage bill⁽³⁾ but also the gross operating surplus of individuals (including gross mixed income), net interest received, dividends and social benefits received, and

(1) Cf. for example EC (2007), *The labour income share in the European Union*, Employment in Europe 2007, 237-272, and IMF (2007), *The globalisation of labor*, World Economic Outlook, April, 161-192.

(2) EC (2007), *Labour market and wage developments in 2006, with special focus on relative unit labour cost developments in the euro area*, European Economy, N° 4.

(3) The concept of the wage bill as a percentage of GDP is slightly different from the wage share concept used above, because the standpoint here is that of the recipient sector. This means that account is also taken of the wages of Belgian employees paid by the rest of the world, whereas wages paid in Belgium to foreign workers are disregarded.

also takes account of the taxes and social contributions paid and the balance of other current transfers. The aim is to examine whether the weaker growth in the wage bill during the period 2003-2005 was offset or reinforced by the movement in the other components of disposable income. The next step is to analyse to what degree changes in individuals' disposable income have had repercussions on their final consumption expenditure, or conversely, whether they have been prompted to modify their savings ratio. Finally, if the investment of individuals is also taken into account, the scale of the changes in their net financial wealth becomes clear. It is thus possible to assess the extent to which the reduction in the wage share has led to a fall in the financing balance of individuals.

2.1 Disposable income of individuals

Since the mid 1990s, the disposable income of individuals has always exceeded the wage bill. However, this gap between gross disposable income and the wage bill has declined steadily, dropping from 14.8 p.c. of GDP in 1995 to 7.9 p.c. in 2005, after which it expanded slightly again. While the wage bill as a percentage of GDP has changed little since the mid 1990s, there has been a downward trend in the total gross disposable income of individuals as a percentage of GDP. This means that, taken together, the other components of the disposable income of individuals have grown more slowly than the wage bill over that period.

Taking the period 1995-2007 as a whole, the gross disposable income of individuals declined almost constantly in relation to GDP, falling by a total of 7.3 p.c. of GDP. Almost the whole of that fall is attributable to the

movement in net property income, more specifically interest income. As a result of the downward trend in interest rates this component of disposable income dropped by 6.3 p.c. of GDP between 1995 and 2007. Conversely, the decline in the wage bill, down by only 0.7 p.c. of GDP over that long period, was certainly not the main determinant of the movement in the disposable income of individuals.

However, when expressed as a percentage of GDP, the disposable income of individuals slowed during the period 2003-2005 at twice the rate recorded in preceding years. That sharper decline was due mainly to the movement in the wage bill, which declined by an annual average of 0.7 p.c. of GDP during that period, whereas between 1996 and 2002 it had increased by an average of 0.2 p.c. of GDP per annum. However, the impact on disposable income was partly offset by fact that the weaker growth of the wage bill also slowed the amount of taxes and social contributions paid. During the period 2003-2005 the latter actually declined by 0.5 p.c. of GDP per annum; the tax reform introduced in 2001 was also a factor here. In the context of a further, similar decline in interest income as a percentage of GDP, the slower growth of the wage bill therefore caused a substantial decline in the disposable income of individuals, averaging 1.2 p.c. of GDP per annum, compared to an average fall of 0.6 p.c. of GDP over the period 1995-2007 as a whole.

The downward trend in the disposable income of individuals as a percentage of GDP does not imply a continuous reduction of the income itself. On the contrary, there was an increase averaging 3 p.c. per annum between 1995 and 2007. In real terms, after application of the private final consumption expenditure deflator, the gross

TABLE 3 COMPONENTS OF THE DISPOSABLE INCOME OF INDIVIDUALS
(percentages of GDP)

	1995	2001	2002	2003	2004	2005	2006	2007 e
Wage bill	52.3	53.3	53.6	53.2	51.9	51.4	51.2	51.6
Gross operating surplus ⁽¹⁾	15.0	14.5	13.8	13.7	13.2	13.1	12.9	12.8
Net property income	13.5	11.5	10.4	9.2	8.7	8.4	8.1	8.6
Social benefits	19.0	18.4	18.8	19.1	18.7	18.5	18.3	18.0
Taxes and social contributions (-)	33.6	34.0	34.2	33.9	33.1	32.7	31.7	31.9
Other current transfers	0.8	0.6	0.6	0.6	0.7	0.7	0.8	0.7
Gross disposable income	67.1	64.2	63.0	62.0	60.1	59.3	59.4	59.8

Sources: NAI, NBB.

(1) Including gross mixed income.

disposable income of individuals increased by an average of 1.1 p.c. per annum. However, that average rise conceals some fluctuations. The steady rise in the volume of the gross disposable income of individuals in the period 1997-2001 was followed by a slight fall in the ensuing four years; in 2006 and 2007, there was a return to strong growth.

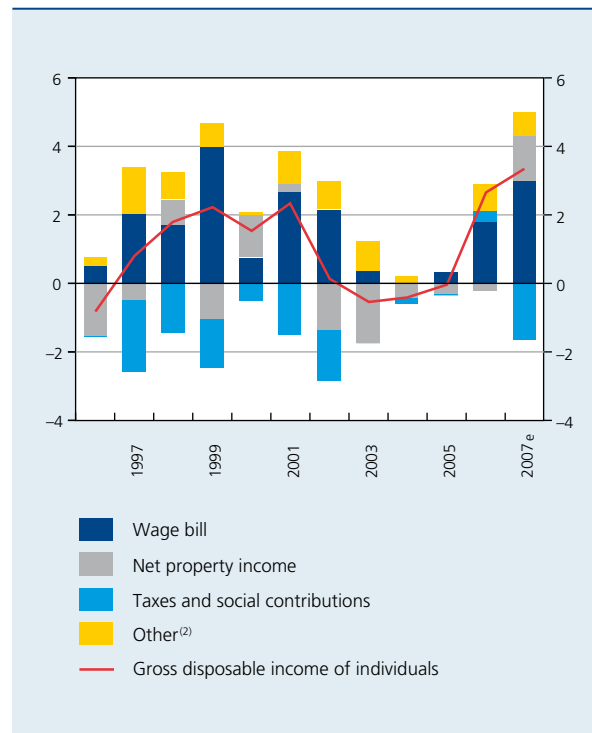
During the period 1998-2001, the disposable income of individuals increased by an average of 2 p.c. per annum in real terms, mainly as a result of the substantial growth of the wage bill during that period, although net property income and the gross operating surplus (including gross mixed income) both also contributed around 0.3 percentage point per annum to the growth of disposable income.

In contrast, in 2002-2005 disposable income recorded (almost) negative growth in real terms. This was due partly to the deteriorating economic situation during the period 2002-2003, which prompted companies to curb their labour costs, as already discussed in section 1. During that period, the contribution of the wage bill was therefore unusually small. In addition, net property income made a considerable negative contribution to disposable income growth in real terms, particularly in 2002 and 2003. This was due mainly to the decline in interest income, but property income was also depressed by the negative contribution from dividends received during that period. However, it is worth noting that in the period 1998-2001 dividend income had risen very strongly, so that it had reached an unusually high level in 2001, namely 4 p.c. of GDP, compared to an average of 3 p.c. of GDP in the period 1995-2000. Despite the small positive contribution from taxes in 2003 – due to the abolition of the complementary crisis contribution and the implementation of the personal income tax reform – the gross disposable income of individuals declined by 0.5 p.c. in real terms that year. In 2004 and 2005, there was again negative growth of disposable income in real terms, as the very meagre increase in the wage bill was too small to offset the negative contribution from net property income.

It was 2006 before disposable income really recovered. Not only did that year bring an increase in the wage bill of 2.1 p.c. in real terms, the implementation of the final part of the tax reform initiated in 2001 also contributed to a 2.7 p.c. increase in gross disposable income in 2006. In 2007, taxes and social contributions again depressed disposable income, as in most other years, yet there was still 3.3 p.c. growth of disposable income, bolstered by the strong increase in the wage bill and by net property income which had a positive impact on the disposable income of individuals for the first time since 2001.

CHART 4 MAIN COMPONENTS OF THE DISPOSABLE INCOME OF INDIVIDUALS, IN REAL TERMS⁽¹⁾

(contribution to the growth of the disposable income, percentage points)



Sources: NAI, NBB.

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

(2) The gross operating surplus, gross mixed income and the balance of current transfers excluding taxes and social contributions.

2.2 How do individuals use their disposable income?

Individuals use the bulk of their disposable income to finance their final consumption expenditure. The remainder is classified in the national accounts under gross savings which, when expressed in relation to the disposable income of individuals, constitute the savings ratio.

Like gross disposable income as a percentage of GDP, the final consumption expenditure of individuals also displayed a downward trend as a percentage of GDP. However, the decline was far less pronounced than the fall in disposable income. The reduction in the gross disposable income of individuals as a percentage of GDP was therefore largely reflected in a downward trend in the savings ratio, which declined from 20 p.c. of disposable income in 1995 to a low point of 12.2 p.c. in 2005.

The decline in interest income as a percentage of the disposable income of individuals was a contributory factor in this downward trend in the savings ratio. Since interest income is perhaps less likely than labour income to be spent on consumption, such a shift in the composition of the disposable income of individuals drives up the consumption ratio and therefore reduces the savings ratio. However, in general such a reduction will only persist if individuals consider that their income prospects will remain robust, both during their working life and in retirement. In that respect, the consolidation of public finances which has taken place provides significant support.

In the period 2003-2005, the savings ratio declined faster than in the preceding years. The reason is that individuals tend to smooth their final consumption expenditure to some extent in the event of major fluctuations in their disposable income. The relatively steep fall in that income therefore did not produce a corresponding fall in final consumption expenditure – both considered in relation to GDP – but led to a sharper reduction in the savings ratio.

In the past two years, however, the savings ratio has risen again. Not only has the gross disposable income of individuals grown more strongly, but final consumption expenditure has also continued falling slowly as a percentage of GDP. The assertion that individuals try to maintain the level of their final consumption expenditure in the event of a dip in their disposable income is therefore equally valid for periods in which that income increases strongly. Thus, the rise in disposable income in 2007, as a percentage of GDP, did not trigger higher final consumption expenditure, but was fully reflected in higher savings.

As well as consuming, individuals also invest, principally in the form of housing construction and renovation. The savings ratio is therefore much higher than the eventual financing balance of individuals. In contrast to their savings, which displayed a downward trend as a percentage of GDP, the investment of individuals as a percentage of GDP did not exhibit any clear trend in the 1995-2003 period. During that period, the fall in the savings ratio was therefore almost entirely reflected in a decline in the financing balance of individuals as a percentage of GDP. Since 2004, however, individuals have considerably increased their expenditure on housing construction and renovation, including in relation to GDP. This strong propensity to invest was underpinned mainly by the very low mortgage interest rates, while the boom in house prices on the secondary market also propelled the growth of investment in housing. This was reflected in a strong decline in the financing balance of individuals, down to less than 1 p.c. of GDP since 2005, compared to 8.1 p.c. in 1995.

2.3 The financing balance of individuals in an international perspective

Whereas in 1995 the financing balance of Belgian individuals had exceeded the unweighted average for the three main neighbouring countries by 4.3 p.c. of GDP, in 2006 only the Netherlands still had a lower financing balance. The downward trend in the financing balance of Belgian individuals (totalling 7.6 p.c. of GDP since 1995) is in stark contrast to the upward trend in the financing balance of German individuals (amounting to 2.9 p.c. of GDP), while

TABLE 4 DISPOSABLE INCOME AND FINANCING BALANCE OF INDIVIDUALS
(percentages of GDP, unless otherwise stated)

	1995	2001	2002	2003	2004	2005	2006	2007 e
1. Gross disposable income ⁽¹⁾	67.7	64.8	63.5	62.6	60.8	59.9	60.0	60.4
2. Final consumption expenditure	54.1	54.2	53.5	53.4	52.7	52.6	52.5	52.4
3. Gross savings (1 – 2)	13.6	10.6	10.0	9.2	8.1	7.3	7.5	8.0
<i>p.m. Savings ratio</i> (percentages of disposable income)	20.0	16.4	15.8	14.7	13.3	12.2	12.5	13.2
4. Gross investment	5.8	5.2	5.3	5.3	5.7	6.1	6.5	6.8
5. Other uses ⁽²⁾	-0.4	0.2	0.1	0.3	0.4	0.4	0.5	0.5
6. Financing balance (3 – 4 – 5)	8.1	5.2	4.6	3.6	2.0	0.8	0.5	0.7

Sources: NAI, NBB.

(1) Including the change in the net claims of households on pension funds.

(2) Net capital transfers paid to other sectors and net acquisitions of non-produced non-financial assets such as land and patents.

in the case of French individuals it is only in the last few years that the financing balance has begun to decline as a percentage of GDP. The Netherlands was the only country where the financing balance of individuals recorded a downward trend throughout the period, though the fall was less marked than in Belgium. These divergences largely reflect the pattern of disposable income: while the growth of disposable income in Belgium and the Netherlands did not keep pace overall with GDP growth, the ratio of disposable income to GDP remained practically unchanged in Germany and France.

Differences in spending patterns also played a role. In Belgium, the slower growth of disposable income was largely absorbed by a decline in savings as a percentage of GDP, so that final consumption expenditure was not particularly hard hit, whereas this was less true in the Netherlands. In addition, individuals in both countries stepped up their other expenditure – principally investment spending – to roughly the same degree. The smaller decline in savings as a ratio of GDP in the Netherlands was therefore reflected in a smaller reduction in the financing balance. In 2006, that balance had still been lower than in Belgium, and in 2005 and 2006 it was actually negative, implying that Dutch individuals saw a contraction in their net financial wealth as a percentage of GDP.

Differences in spending patterns were also the reason for the divergent trend in the financing balance in Germany and France. While disposable income in both countries remained virtually unchanged as a percentage of GDP, German individuals saw an increase in their financing balance, while in France the balance declined. The difference is due to the investment profile. Although German individuals did slightly increase their final consumption expenditure, the downward impact on the financing balance was more than offset by the fact that they invested considerably less in relation to GDP. In Germany, the financing balance therefore grew steadily to around 6 p.c. of GDP. In contrast, in 2006 French individuals invested more as a percentage of GDP than in 1995, reducing their financing balance to around 3.5 p.c. of GDP.

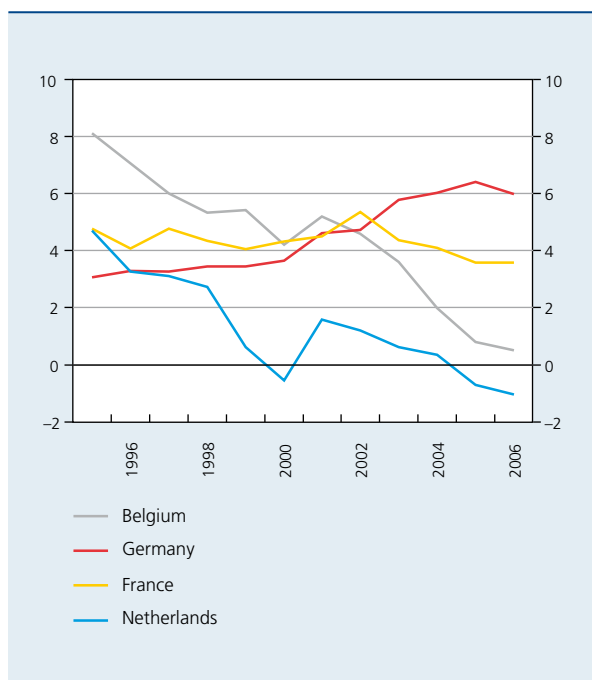
3. The operating surplus, profit and financing balance of companies

Whereas gross disposable income is a key concept which is often used in the case of individuals, it is normally only the gross operating surplus that is considered in the case of companies. The importance of that concept is due mainly to the fact that other forms of corporate income are much less significant than they are for individuals. For example, companies do not receive any social benefits and their net interest income is modest compared to that of individuals. Nonetheless, in order to take account of other forms of corporate income, this article uses a gross profit measure based on the national accounts data. This measure is calculated as the sum of the gross operating surplus, net property income – but excluding dividends – and the balance of current transfers, excluding the taxes on corporate income and wealth. Examination of the purposes for which the profit according to this concept is used reveals the extent to which the steep rise in the operating surplus of companies has also benefited the other domestic sectors, and particularly individuals.

3.1 The operating surplus and profit of companies

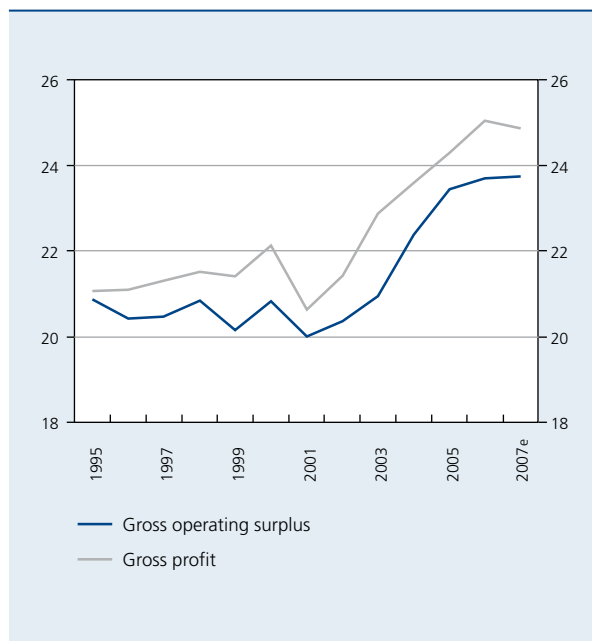
Between 1995 and 2002, the gross operating surplus of companies fluctuated around 20.5 p.c. of GDP. However, in the ensuing three years it increased sharply; since 2005 it has totalled roughly 23.5 p.c. of GDP. On average, the gross profit of companies was roughly 1 p.c. of GDP higher than their gross operating surplus, and followed a fairly similar trend. The main difference lies in the balance of current transfers, excluding taxes on income and wealth, which averaged 0.7 p.c. of GDP. During the 1995-2007 period, the net property income of companies,

CHART 5 INTERNATIONAL COMPARISON OF THE FINANCING BALANCE OF INDIVIDUALS (percentages of GDP)



Source: EC.

CHART 6 GROSS OPERATING SURPLUS AND GROSS PROFIT OF COMPANIES (percentages of GDP)



Sources: NAI, NBB.

even disregarding the net dividends paid to other sectors, averaged only 0.3 p.c. of GDP.

The gross operating surplus is therefore by far the most important income source for companies. Since 2002 it has risen strongly, especially in 2004 and 2005 with increases of 12.7 and 9.2 p.c. respectively. For a better understanding of the movement in the gross operating surplus of companies it is useful to consider a breakdown between the gross operating margin per unit of sales and the number of units sold⁽¹⁾. This breakdown shows that companies have managed to achieve a substantial rise in their gross operating margin per unit of sales in every year since 2002, in contrast to the situation during the second half of the 1990s, and since 2004 they have also achieved a relatively strong increase in their volume of sales.

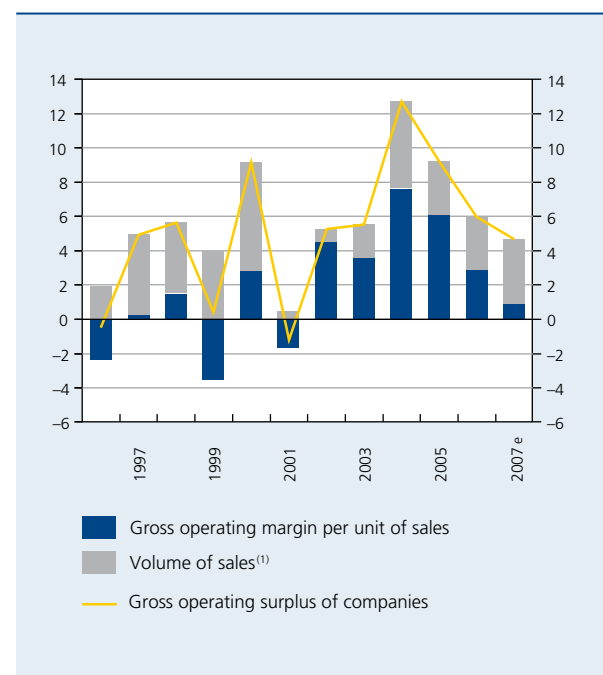
Nevertheless, the significant increase in the gross operating surplus followed the mediocre results recorded by companies in 2001, when their gross operating surplus had dropped by 1.2 p.c. In that year, costs of domestic origin – principally labour costs – rose strongly in comparison with the increase in selling prices. The resulting downward pressure on the operating margin was partly offset by the slight improvement in the terms of trade, as

(1) Including the change in stocks.

the rise in prices of imported inputs lagged slightly behind the increase in selling prices on the export markets, thus bolstering corporate margins. Yet this could not prevent the gross operating margin per unit of sales from falling by 1.7 p.c. In addition, growth in the volume of sales was very feeble at 0.5 p.c., compared to an average of 4.2 p.c. in 1996-2000.

Following the sharp economic slowdown in 2001, which severely depressed both selling prices and demand, companies tried to restore their gross operating margin per unit of sales by curbing the rise in labour costs. In 2002 they could only do this by boosting labour productivity, since the increase in hourly labour costs was already stipulated in the central agreement concluded at the end of 2000. The expansion of the operating margin in that year was therefore due primarily to a substantial improvement in the terms of trade, as import prices fell more steeply than selling prices on the export markets. During 2003-2005 companies were able to increase their operating margin further as a result of the weaker rise in costs of domestic origin, including labour costs, and thanks to the relatively strong rise in selling prices on the domestic market. In 2004 and 2005, the impact of the increase in the operating margin was considerably reinforced by

CHART 7 MAIN COMPONENTS OF THE GROSS OPERATING SURPLUS OF COMPANIES (contribution to the growth of the gross operating surplus, percentage points)



Sources: NAI, NBB.

(1) Including the change in stocks.

the vigorous growth in the volume of sales on both the domestic and the export markets. The strong increase in the operating margin per unit of sales combined with a substantial rise in the volume of sales therefore explains the exceptionally steep increase in the operating surplus in those two years.

In 2006 and 2007, the increase in the operating margin per unit of sales was less pronounced. For one thing, selling prices on the domestic market did not rise as quickly as in the preceding years. Also, costs of domestic origin – and especially labour costs – accelerated again in response to the rising tensions on the labour market. At the same time, however, strengthening demand helped to limit the impact of the stronger rise in labour costs on the operating surplus of companies, since they were thus able to continue expanding their volume of sales fairly substantially.

3.2 How do companies use their profit?

The past five years have seen a surge in corporate gross profit, with an average rise of 7.5 p.c. per annum, mainly as a result of the strong increase in their gross operating surplus. The question is whether this substantial rise has also benefited the other domestic sectors, and more particularly individuals. To answer that question, this article examines the extent to which companies have also stepped up their expenditure or increased their financing balance. If the increase in the gross operating surplus has led to a rise in the amount of taxes paid on income and wealth or an increase in the net dividends paid to other

sectors, there is clearly some redistribution of the income flows. If the larger gross operating surplus has led to more investment, that can also be viewed as a form of redistribution between sectors. All other things being equal, higher investment boosts the economy's growth potential, and that in turn leads to a stronger rise in the wage bill and hence the disposable income of individuals.

Whereas, on average over the past three years, companies' gross profit exceeded the 2002 figure by 3.3 p.c. of GDP, their financing balance increased by 2.2 p.c. of GDP over the same period. At first sight, individuals therefore seem to have gained less benefit than the companies themselves from the strong profit growth. Nevertheless, the taxes which companies paid on income and wealth kept fairly closely in line with the movement in their gross profit. Thus, in the period from 2005 to 2007, those taxes exceeded the taxes paid in 2002 by 0.6 p.c. of GDP, representing 18 p.c. of the increase in their gross profit. In addition, the gross investment of companies expressed as a percentage of GDP has also increased from 12.2 p.c. in 2002 to an average of 13.5 p.c. in the past three years. In the last two years in particular, owing to the strong growth of the gross profit, the gradual increase in external financing costs has not weakened corporate propensity to invest. The fairly strong increase in the financing balance of companies is therefore due mainly to the gradual decline in the net dividends paid to other sectors, as a percentage of GDP. During 2005-2007, the net dividends which companies paid to other sectors were down by an average of 0.4 p.c. of GDP compared to 2002, even though their gross profit after tax was up by 2.7 p.c. of GDP. For completeness, it should be mentioned that in the

TABLE 5 GROSS PROFIT AND FINANCING BALANCE OF COMPANIES
(percentages of GDP)

	Average 1995-2000	2001	2002	2003	2004	2005	2006	2007 e
Gross profit	21.4	20.6	21.4	22.9	23.6	24.3	25.0	24.9
Taxes on income and wealth (–)	3.0	3.2	3.2	3.0	3.3	3.6	3.9	3.8
Net dividends paid to other sectors (–)	4.2	5.2	5.5	5.5	5.0	5.2	4.9	5.2
Gross investment (–)	13.1	13.6	12.2	12.2	12.9	13.0	13.7	13.9
Other uses ⁽¹⁾ (–)	0.1	0.4	0.3	1.4	0.5	0.3	–0.2	–0.4
Financing balance	0.9	–1.7	0.3	0.9	1.9	2.2	2.7	2.4

Sources: NAI, NBB.

(1) Net capital transfers paid to other sectors, net acquisitions of non-produced non-financial assets such as land, patents and goodwill, and the change in the net claims of households on pension funds.

past three years companies have received more net capital transfers than in 2002, and that has also contributed to the increase in their financing balance.

However, the weaker growth of net dividends paid by companies to other sectors over the past five years needs to be qualified, as there was a very strong rise in the net dividends which they paid in the period 2000-2002. On average, during 1995-1999 those dividends represented 22.6 p.c. of gross profit after tax, but in 2001 and 2002 that ratio increased to 30 p.c. If the 2002 peak is taken as the benchmark, then net dividends paid as a percentage of GDP declined fairly sharply in the ensuing years. However, by reference to the period 1995-2000, the net dividends paid by companies to other sectors have actually risen faster than GDP.

The years 2001-2002 also constituted an exceptional period for gross investment. After the bursting of the stock market bubble and the general economic slowdown, gross investment grew very slowly because companies gave priority to consolidating their balance sheets. The strong expansion of investment in subsequent years must therefore be regarded partly as making up lost ground.

In the past three years, the gross profit of companies has been 3.3 p.c. of GDP higher than in the reference period 1995-2000. That rise has resulted in an increase in their redistributive expenditure in the broad sense (including investment) amounting to 2 p.c. of GDP, and an increase of 1.5 p.c. of GDP in their financing balance. Whatever the reference period considered, the financing balance of companies has therefore still risen significantly. That improvement means that companies have gradually been able to finance more of their investment out of internal resources, so that their degree of financial independence – i.e. the ratio between equity capital and total liabilities – has steadily increased.

3.3 The financing balance of companies in an international perspective

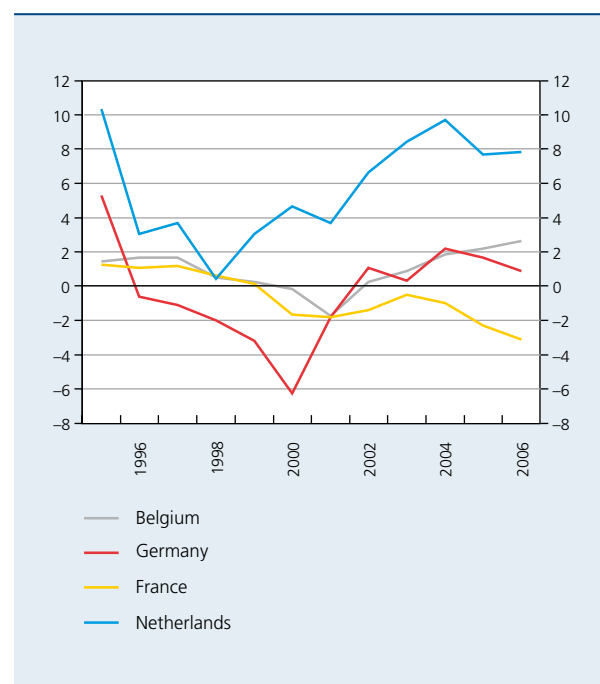
In Belgium's three main neighbouring countries, the financing balance of companies also showed a drop in 2000-2001. However, the speed and strength with which that balance recovered in subsequent years varied greatly from one country to another.

Germany was the country where the financing balance of companies showed the sharpest fall (down to -6.3 p.c. of GDP in 2000), but it recovered very quickly. In 2002, the deficit had already been converted to a surplus of 1.1 p.c.

of GDP. This was due partly to the increase in the gross operating surplus (particularly thanks to wage moderation), but the main factor was the weak growth of investment. In the ensuing years, the gross operating surplus of companies continued to grow strongly, while the rate of expansion in gross investment lagged behind. However, this did not lead to any further upward tendency in the financing balance, which fluctuated between 0.3 and 2.2 p.c. of GDP without displaying any clear trend. For one thing, the increase in the gross operating surplus was partly negated by the fact that companies also paid more taxes. Also, the increase was offset by a fall in net property income and in net capital transfers received, both in relation to GDP.

Much the same pattern emerged in the Netherlands. Although the financing balance of companies hardly declined at all in 2001, it still recorded a very strong rise totalling 6 p.c. of GDP in the period 2002-2004. In the Netherlands, too, that increase was due mainly to the sharp fall in the investment ratio, although the gross operating surplus did grow slightly faster than GDP. However, in 2005 and 2006, although the gross operating surplus continued to grow strongly, the financing balance declined as a result of a sharp deceleration in net property income.

CHART 8 INTERNATIONAL COMPARISON OF THE FINANCING BALANCE OF COMPANIES (percentages of GDP)



Sources: EC, NAI.

In contrast, in France the financing balance of companies did not tend to recover in the period 2001-2006. Although that balance was 1.3 p.c. of GDP higher in 2003 than in 2001, it then subsided to well below the 2001 level. This recent pattern reflects the phenomenon mentioned earlier, namely that the wage share in France has not contracted in the past few years, in contrast to the situation in most other euro area countries. The strong rise in real labour costs per employee (outstripping productivity growth) has driven up costs and therefore reduced the gross operating surplus of companies. Conversely, in Belgium, Germany and the Netherlands wage moderation made a positive contribution to the increase in the operating surplus and financing balance of companies.

Conclusion

This article analyses the income flows of individuals and companies on the basis of the national accounts. Although much attention focuses on the movement in the wage share, the article is broader in scope than that, because it also examines the redistribution of incomes between sectors and the purposes for which individuals and companies use their income. The main findings can be summarised as follows.

Analysis of the primary incomes arising from domestic production reveals that companies generate the most value added. In 2006, they used 60.6 p.c. of that value added to cover labour costs, a share that has however declined in recent years, as during 1995-2002 the average figure was 64.3 p.c. Conversely, general government creates the least value added but pays out most of it in the form of labour costs, namely 88 p.c. in 2006, compared to 86.1 p.c. in 1995. In the case of the value added of individuals – both self-employed workers and home owners – only 10.6 p.c. was paid out in the form of labour costs in 2006.

There are various definitions of the wage share and they produce very different results in terms of level, but they mostly still present a similar picture. Thus, all definitions indicate a fairly stable pattern in the second half of the 1990s, followed by a slight rise and subsequently a somewhat sharper fall during 2003-2005. In the past two years, there has been no further significant change in the wage share. Its contraction in 2003-2005 was partly a reflection of the business cycle. In response to the slackening pace of activity in 2001 and 2002, companies tried to reduce their labour costs via corporate restructurings and wage moderation. In addition, the recent pattern can also be regarded as part of the downward trend in the wage share since the early 1980s, just as in most other euro

area countries. In the literature, that downward trend is often linked to structural developments such as globalisation which has expanded the labour supply worldwide, technological progress which has made production more capital intensive, and the growing importance of the services sector which features a smaller wage share.

However, wages are not the only income category of individuals to have declined as a percentage of GDP. Since 1995, the rise in the total gross disposable income of individuals has almost continuously lagged behind GDP growth. That is due mainly to the downward trend in net interest income as a percentage of GDP, which in turn reflects the falling interest rates. However, the downward trend in individuals' disposable income as a percentage of GDP does not mean that those incomes have also declined in absolute terms. On average, the disposable income of individuals increased by 3 p.c. per annum between 1995 and 2007. Even taking account of inflation as measured by the private final consumption expenditure deflator, disposable income increased in real terms by an average of 1.1 p.c. per annum. Yet this positive average conceals the fact that disposable income did fall in absolute terms in certain years, or for certain population groups.

Like the gross disposable income of individuals in relation to GDP, their final consumption expenditure also displayed a downward trend, as a percentage of GDP. However, this was far less pronounced, and that was therefore reflected in a downward trend in the savings ratio, from 20 p.c. of disposable income in 1995 to a low of 12.2 p.c. in 2005, after which a gradual recovery set in. That recovery is not, however, evident in the financing balance of individuals, as they do not only consume but also invest, primarily in the form of housing construction and renovation. Since 2004, individuals have recorded a strong rise in their investment expenditure, underpinned by the very low mortgage interest rates and the surge in house prices, and that has been reflected in a further decline in their financing balance which has been below 1 p.c. of GDP in the past three years.

The principal counterpart of the recent contraction in the wage share is the sharp increase in the gross operating surplus of companies, that surplus also being by far their main source of income. However, that increase has not led to a corresponding rise in the financing balance of companies, because the latter have also paid more taxes on income and wealth, and their investment spending has expanded faster than GDP. In comparison with the period 1995-2000, companies have also paid out more to other sectors in net dividends, as a percentage of GDP, though dividends were even higher in the period 2001-2003. In all, individuals have therefore also benefited from the strong

corporate profit growth. Nevertheless, the financing balance of companies has also risen steadily to an average of 2.4 p.c. of GDP in the past three years. Although this rise can be viewed partly as making up lost ground, following the deterioration during the period 1998-2001, the recent improvement still looks significant. It has enabled companies to move gradually towards financing more of their investment out of internal resources, thus further consolidating their balance sheets.

The trend shifts in income flows described in this article are not peculiar to Belgium since they also occurred in most other euro area countries. To some extent, they are due to structural developments such as globalisation, technological progress and population ageing. Although such developments are inevitable, policymakers can do much to provide support, in particular by creating a robust and stable macroeconomic framework backed by efficient labour and product markets. Finally, it should be pointed out that there is no guarantee that the recent developments will continue at the same pace in the future, as is already apparent from previous long-term movements.