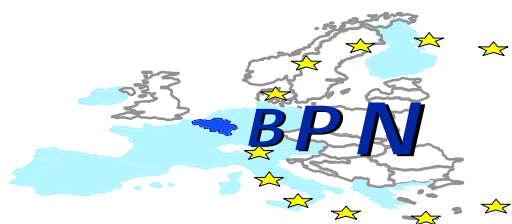


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Special topic :

Budgetary coordination in a federal state - The case of Belgium

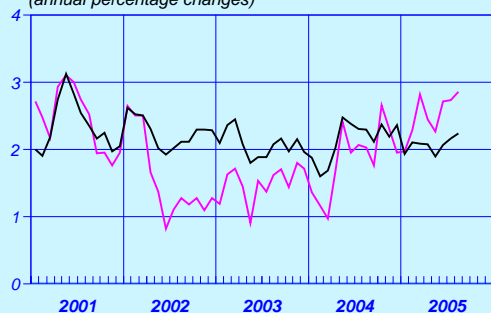
CONSENSUS: Average of participants' forecasts

	2004		2005 p			2006 p		
	Belgium	Euro area ⁴	Belgium		Euro area ⁴	Belgium		Euro area ⁴
			Consensus	Previous consensus		Consensus	Previous consensus	
Real GDP¹	2.7	1.7	1.4	1.4	1.6	2.0	2.1	2.1
Employment¹	0.7	0.6	0.5	0.5	0.7	0.7	0.6	0.9
Consumer prices¹	1.9	2.1	2.6	2.1	1.9	1.9	1.8	1.5
Current account²	3.4	0.6	2.6	2.9	0.6	2.8	3.2	0.6
General government balance^{2,3}	0.0	-2.7	-0.2	-0.3	-2.6	-0.8	-0.7	-2.7
Primary balance²	4.8	0.6	4.3	4.2	0.6	3.4	3.5	0.6
Public debt²	95.7	71.3	95.2	95.6	71.7	92.7	93.2	71.9

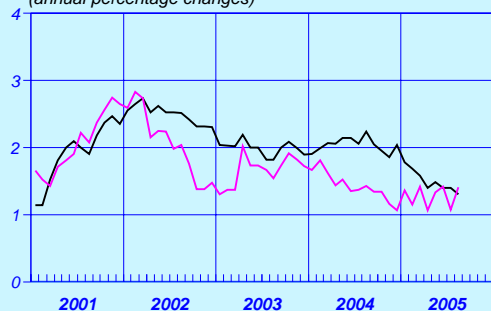
¹ P.c. change. ² In p.c. of GDP. ³ EDP definition. ⁴ European Commission (forecast available since April 2005).

MACROECONOMIC DEVELOPMENTS

HARMONISED CONSUMER PRICES
(annual percentage changes)



UNDERLYING INFLATION TREND
(annual percentage changes)



— Belgium
— Euro area

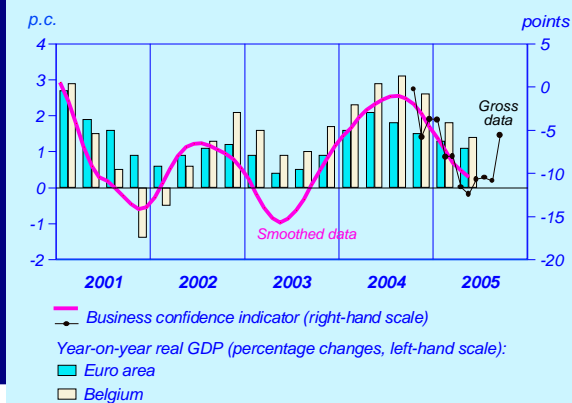
After industrial activity had gone through a soft patch at the beginning of 2005, world trade and economic growth gradually regained some strength during the second quarter. However, oil prices peaked recently. Supported by a protracted strong demand, the price per barrel of Brent jumped to a level close to 70 dollars at the end of August, when some extraction and refinery units in the Mexico Gulf were hit by the Katrina hurricane.

The oil price shock directly affected import and consumer prices. HICP inflation in August 2005 reached 2.9% in Belgium, the highest level since June 2001, and 2.2% in the euro area. As usual, the direct impact has been greater in Belgium than on average in the euro area, owing to the higher weight of oil-related products in the price index and the lower level of excises duties, especially on heating fuel. Those characteristics lead to a higher sensitivity of the overall inflation to oil price movements. Meanwhile, indirect effects and second-round effects on wages are limited at the current juncture. In August, the underlying inflation trend, measured by excluding energy and unprocessed food, came to 1.4% in Belgium and 1.3% in the euro area. **As a result of the higher oil prices, the average inflation forecast of the participating institutions for 2005 has been raised from 2.1% in June to 2.6% in September. For 2006 they expect a deceleration of inflation to 1.9%, i.e. an upward revision by 0.1 point with respect to June.**

The deterioration of the terms of trade stemming from the oil price hike induced the primary dealers to revise their forecast for the current account surplus downwards from 2.9% of GDP to 2.6% for 2005 and from 3.2% to 2.8% for 2006. However, the associated loss of income for the economy has so far exerted limited effects on real activity. Quarter-on-quarter GDP growth returned to a positive value, +0.3%, at the second quarter of 2005, after a stabilization of the level of GDP at the beginning of the year. Therefore, the slowing-down phase which started at the end of 2004 continued, but at a slower pace. Year-on-year GDP growth decelerated from 2.6% in the fourth quarter of 2004 to 1.8% and 1.4% respectively in the

MACROECONOMIC DEVELOPMENTS (continued)

GDP GROWTH AND BUSINESS CYCLE INDICATOR



Sources: EC, NAI, NBB.

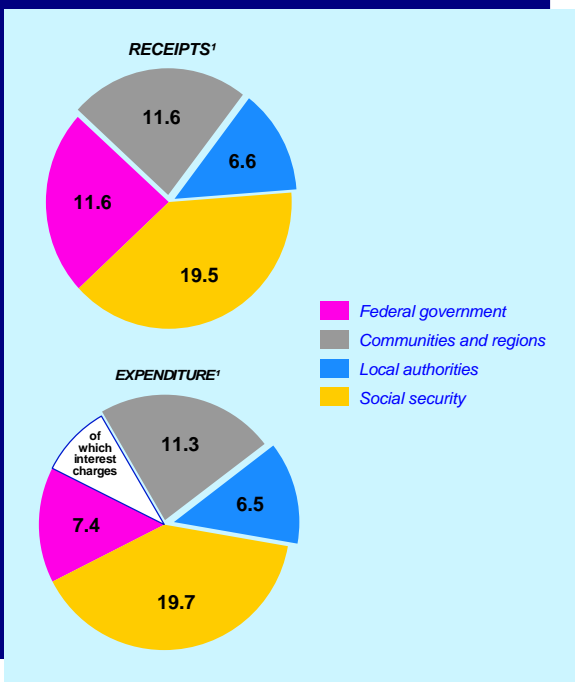
first and the second quarter of 2005. The NBB business survey indicators point to a further stabilisation during the summer months, notably in industry. This feature is shared both by coincident sub-indicators, such as the appreciation on the inventories position, and by leading ones, such as prospects for demand. The latest results, for September, show a marked improvement, boding well for economic prospects if confirmed in the coming months.

As a result, the average forecast of the participating institutions for GDP growth in 2005 amounts to 1.4%, i.e. the same result as in June. The forecasts for 2006 were barely adjusted from 2.1% to 2%. The resilience of the economy rests on the strength of world economy, especially outside the euro area, and on some pick-up in business investment.

The participants also only slightly adjusted their estimate for the general government balance from a 0.3% to a 0.2% of GDP deficit for 2005. For 2006, the deficit is expected to rise to 0.8% of GDP, since at this moment no measures are taken to compensate for the loss of income as a result of the tax reform.

SPECIAL TOPIC: Budgetary coordination in a federal state - The case of Belgium

RECEIPTS AND EXPENDITURE OF THE GENERAL GOVERNMENT SUB-SECTORS (percentages of GDP, 2004)



Sources: NAI, NBB.

¹ Receipts and expenditure are consolidated by deducting from the receipts and expenditure of each government sub-sector the transfers made to other sub-sectors.

Since 1970 Belgium has been gradually transformed into a federal state. Through five successive state reforms government competences have been increasingly devolved from the federal level to the so-called federated entities, i.e. three regions and three communities. The regions are territorially defined entities responsible for e.g. town and country planning, housing, supervision over lower-level authorities and public works. The communities whose main competences are education, culture and welfare comprise the three different linguistic groups.

In 2004 the federal government and the social security system accounted for just over two thirds of general government spending with the share of the regions and communities and of the local authorities amounting to some 20 and 12 p.c. respectively. Given the size of sub-national spending, effective budgetary coordination mechanisms are of the utmost importance. The smooth operation of the latter has proven to be a key element in attaining and maintaining a sound budgetary position in Belgium.

In the stability programs budgetary targets for general government are broken down into targets for each sub-sector. As, in principle, only the federal government is formally responsible for complying with EU fiscal rules, so-called cooperation agreements are signed between the federal government and the regions and communities in order to make the commitments included in the stability programs also binding upon the latter entities. In these agreements which typically cover a period of five to six years but which are updated regularly, the governments of individual regions and communities commit themselves to meeting specific annual budgetary targets. In addition, the regions should ensure as far as possible that public finances of local authorities are consistent with the budgetary target set for that sub-sector.

The budgetary targets for each region and community are typically based upon recommendations by the High Council of Finance, an advisory body bearing a considerable moral authority, which is charged with analysing Belgian public finances. This Council also assesses every year whether all government entities have met their respective budgetary targets.

In the most recent update of the Belgian stability programme of December 2004, a balanced budget is targeted for general government in 2005 and 2006, while 2007 and 2008 would show a small surplus of 0.3 and 0.6 p.c. of GDP respectively. The entity made up of the regions, communities and local authorities, the so-called entity II, would contribute 0.3 p.c. of GDP to the 2008 surplus.

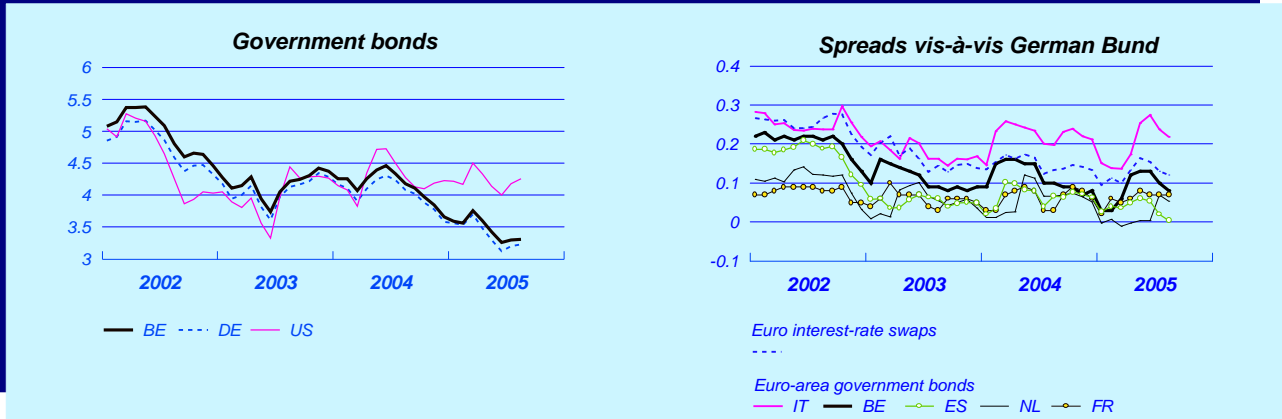
GENERAL GOVERNMENT BALANCE (in p.c. of GDP)

	2001	2002	2003	2004	2005	2006	2007	2008
Stability programme targets								
December 2000	0.2	0.3	0.5	0.6	0.7			
November 2001	0.0	0.0	0.5	0.6	0.7			
November 2002		0.0	0.0	0.3	0.5			
November 2003			0.2	0.0	0.0	0.0	0.3	
December 2004				0.0	0.0	0.0	0.3	0.6
p.m.: Entity II				0.4	0.3	0.1	0.2	0.3
Outcome	0.6	0.0	0.1	0.0				

Sources: Ministry of Finance, NAI, NBB.

GOVERNMENT SECURITIES MARKET

10-YEAR INTEREST RATES (percentage points, monthly averages)



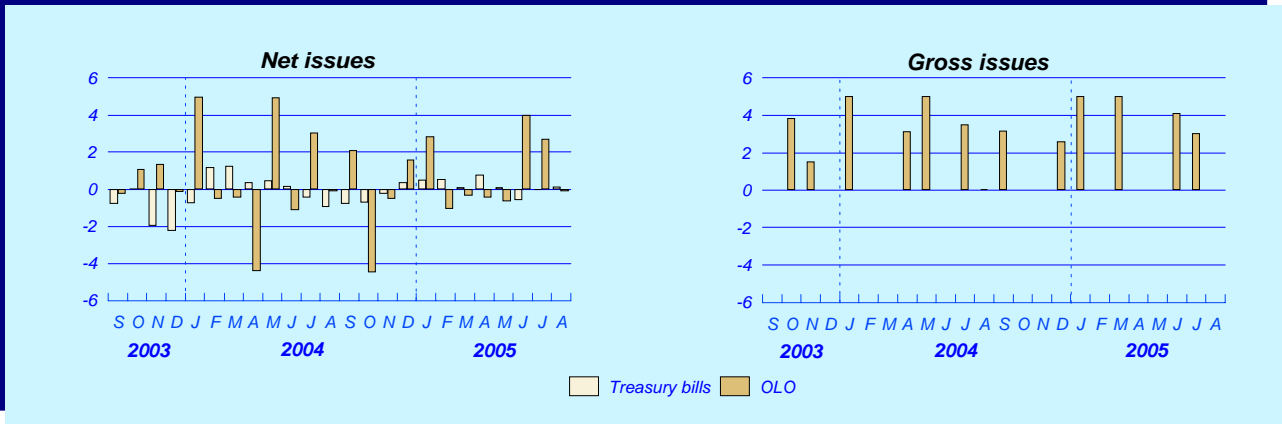
Sources: BIS, Datastream.

After the decrease observed in the first half of 2005, Belgian and German long-term bond yields stabilised at a low level in July and August. In the euro area, the slight increase in inflation perspectives during these two months was compensated by lower real interest rates. In the US, a small increase of the long rate was observed.

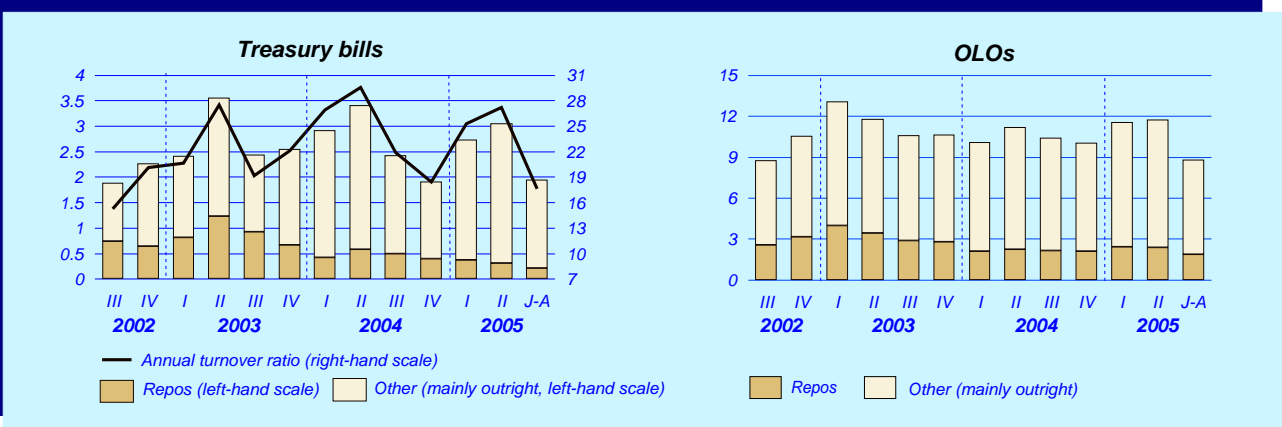
In Belgium, Spain and Italy, the government bond spreads vis-à-vis the German Bund declined in July and August. This development contrasted with the situation in the Netherlands, where an increase in the spread was observed, and France, where no change was recorded. It should be noted that the spread in Italy remained significantly wider than in other countries, probably due to its higher budget deficit and government debt.

Finally, a small decline was registered in the spread for euro area interest-rate swaps in July and August, implying the upward trend of earlier months was reversed.

PRIMARY MARKET (billions of euros)

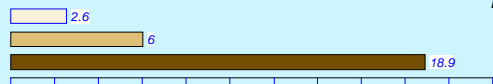


SECONDARY MARKET (billions of euros unless stated, daily averages)



OUTSTANDING AMOUNTS AND TURNOVER

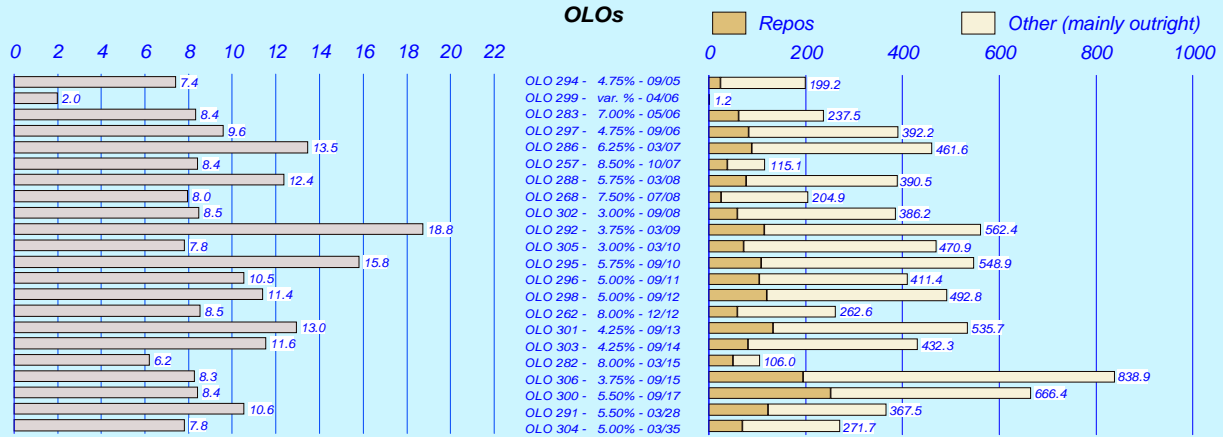
Outstanding amounts at 31 August 2005 (billions of euros)



TREASURY BILLS

3-month
6-month
12-month

Turnover in August 2005 (millions of euros, daily averages)



TREASURY HIGHLIGHTS

- I. The Treasury organised its second OLO auction of 2005 on July 25.

The OLO 45 03/10 and OLO 46 09/15 have been offered. The Treasury took up an amount of 1.41 billion euro for the OLO 45 and an amount of 1.61 billion euro for the OLO 46 (3.02 billion in total). No non-competitive bids have been submitted.

The auction had a bid-to-cover ratio of 1.57.

- II. On June 17, Treasury confirmed to its Primary Dealers the projected OLO issuance of the 2005 funding plan (23.77 billion euro). Gross financing requirements were revised downwards by 2.14 billion euro, resulting in a lower issuance of Treasury Bonds for the Silver Fund and a lower planned issuance of State Notes.

OLO AUCTIONS AND SYNDICATIONS

Month	Date	Settlement
September (Auction)	26	29
November (Auction)	28	1 December

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BNP Paribas
Dexia Bank
Fortis Bank
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KBC Bank
UBS Warburg

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This publication is also available on the internet site www.nbb.be.

Information on the Belgian government debt can be found on the site of the Treasury: www.debtagency.be.

General information on the Belgian government's action can be found on the site www.belgium.be.