Participating Primary Dealers: Barclays Capital, Citigroup, Dexia Bank, Dresdner Kleinwort, Fortis Bank, ING, KBC Bank, Société Générale Corporate & Investment Banking, UBS Limited

Belgian Prime News

QUARTERLY PUBLICATION

No. 39 March 2008

Special topic: Long-term challenges and short-term uncertainty call for a sound budget path in Belgium

Last update: 26 March 2008

Next issue: June 2008

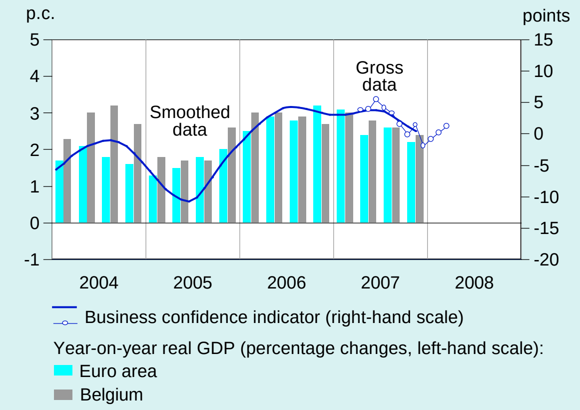
Consensus: Average of participants' forecasts

	2007		2008 p				2009 p	
	Belgium	Euro area	Belgium		Euro area		Belgium	Euro area
			Consensus	Previous consensus	Consensus	Previous consensus	Consensus	Consensus
Real GDP(1)	2.7	2.6	1.7	1.8	1.5	1.9	1.9	1.8
Inflation (HICP)(1)	1.8	2.1	3.0	2.4	2.8	2.2	2.0	2.1
General government balance(2) (3)	-0.1	-0.8	-0.3	-0.3	n.	n.	-0.2	n.
Primary balance(2) (3)	3.7	2.1	3.3	3.3	n.	n.	3.2	n.
Public debt(2) (3)	85.1	66.5	82.5	80.8	n.	n.	80.6	n.

(1) Percentage changes.
(2) Percentages of GDP.
(3) EDP definition. Taking account of Eurostat's decision that the Railway Infrastructure Fund is part of the general government sector.
n. Not available.

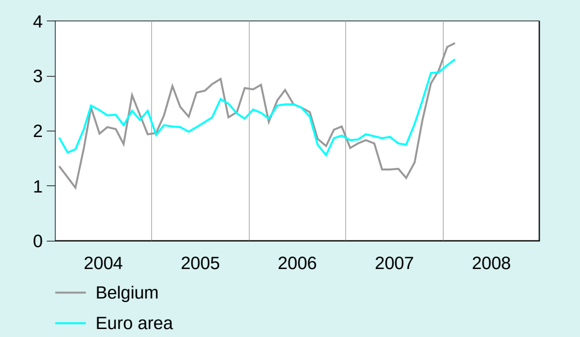
Macroeconomic developments

GDP GROWTH AND BUSINESS CYCLE INDICATOR



Sources: EC, NAI, NBB.

HARMONISED INDEX OF CONSUMER PRICES
(annual percentage changes)



Source: EC.

The Belgian economy grew by 0.5% during the last quarter of 2007, resulting in a growth rate of 2.7% for the year as whole, which was slightly stronger than anticipated. Although the economy thus has remained resilient up to now to the major global shocks, activity is expected to slow down considerably during 2008. The continued strong euro and the less supportive global environment are expected to weigh on exports and indirectly also on investment and employment. In combination with higher inflation, the lower employment creation should also dampen consumption. **The primary dealers have reduced their GDP growth forecasts for 2008 to an average of 1.7%.** This downward revision of 0.2 percentage point is clearly smaller than that for the euro area, where growth is now expected to fall to 1.5% in 2008. **For 2009, the primary dealers expect growth to recover somewhat, to 1.9% in Belgium** and 1.8% in the euro area. These forecasts are surrounded by a high degree of uncertainty, though, particularly as to the impact of the financial turmoil and of the severe downturn in the United States.

Annual HICP inflation in Belgium has increased further in recent months and stood at 3.6% in February. This rise continues to reflect sharp increases in energy and processed food prices. Primary dealers expect inflation to remain high in the coming months and to moderate only in the second half of the year. As a result **they have revised their inflation forecast for 2008 upwards, to 3%, while expecting inflation to come down to 2% on average in 2009.** For the euro area, they expect a similar pattern, although somewhat smoother, in that euro area inflation is forecast to increase to 2.8% in 2008 and then to come down to 2.1% in 2009.

On average, the primary dealers expect the general government budget to show a deficit of 0.3% of GDP in 2008 and of 0.2% of GDP in 2009, primarily due to a less supportive economic outlook. This is slightly lower than the balanced budget target that was announced by the government at the end of February 2008. **The debt ratio should however continue to decline gradually and is expected to reach 82.5% of GDP at the end of 2008 and 80.6% at the end of 2009.** These forecasts were finalised before the new federal government took office on 23 March 2008.

Special topic: Long-term challenges and short-term uncertainty call for a sound budget path in Belgium

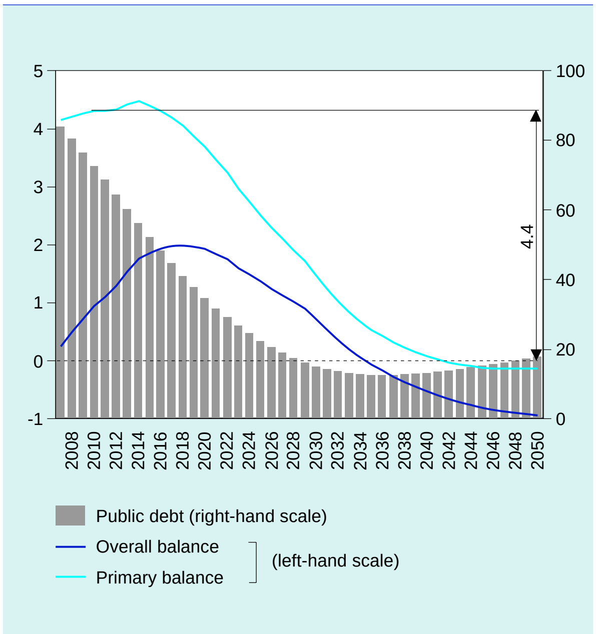
Today, individuals, companies and investors face a dramatic rise in uncertainty, fuelled by a broadening financial crisis. In that context, sound budgetary policies are needed to foster stable prospects by economic agents. Moreover, a continued consolidation of public finances remains a key element to deal with the costs of population ageing.

In Belgium, the High Council of Finance, a leading advisory body, plays a major role in that respect. Its “Public Sector Borrowing Requirement” section analyses fiscal policy and makes recommendations on the subject. In the past, the Section’s opinions have generally underpinned the medium-term fiscal programmes and the corresponding agreements concluded by the federal government and the communities and regions.

The Section issued a new report in March 2007, for the first time since 2004. That report was based on the conclusions of the Study Group on Ageing concerning the budgetary impact of demographic developments. According to the Group’s latest estimate, public spending on pensions and health care will increase by around 8 percentage points of GDP between 2006 and 2050. However, since unemployment benefits and expenditure relating to family allowances, incapacity and pre-pensions should diminish, the net increase in public spending associated with demographic changes is estimated to attain 6.2 percentage points of GDP during that period. Obviously, such long-term estimates are surrounded by a significant degree of uncertainty.

Two key considerations guided the Section in its recommendation of the path to be followed by the government in order to attain an overall budget balance. First, that path must be sustainable, in that the public debt must tend in the long term towards a low and stable level. Second, it must ensure as far as possible the intertemporal neutrality of fiscal policy, which implies that the burden of any budget adjustments necessary to ensure that sustainability is not passed on to future generations.

BUDGET PATH RECOMMENDED BY THE HIGH COUNCIL OF FINANCE
(percentages of GDP)



Source: HCF.

According to the path recommended by the Section, which assumes a structural budget surplus of 0.3% of GDP in 2007, the overall balance of general government should increase by 0.2 percentage point of GDP per annum to reach 1.3% of GDP in 2012. That scenario is in line with the budget targets set in Belgium’s December 2006 stability programme and, while that stability programme has not been updated yet, the government that took office in March 2008 has already confirmed its commitment to reach a significant surplus by the beginning of the next decade. However, the Section pointed out that this medium-term path should be regarded as the minimum effort. The budget surplus should continue its expansion beyond 2012, rising to around 2% of GDP during the period 2017-2019. After that, it should gradually diminish, reverting to a balanced budget in 2035 and turning into a deficit of just under 1% of GDP in 2050.

According to this scenario and assuming a constant ratio of the non-ageing-related part of the primary balance to GDP, the budgetary costs of ageing in the period 2010-2050 would be largely, but not entirely, prefinanced. In fact, four-fifths of the increase in public expenditure associated with demographic changes during that period, or 4.4% of GDP, could be offset by the fall in interest charges, due to the reduction of the public debt, combined with the steady reduction of the budget surplus and, finally, its turning into a modest deficit.

In accordance with the three-pronged strategy to guarantee fiscal sustainability against the background of population ageing that was formulated at the Stockholm European Council in 2001, fiscal consolidation efforts may be complemented with further structural reforms of pension and healthcare schemes and measures aimed at increasing employment and activity growth. As pointed out in the National Bank of Belgium’s 2007 annual report and in a Federal Planning Bureau working paper[1], recent fiscal outcomes fall short of the targets. Against that background, increased fiscal discipline, as announced by the new government, will be key to successfully preparing the country for the macroeconomic and budgetary impact of population ageing.

[1] Saintrain M. and S. Weemaes (2008) “Accumuler des surplus budgétaires pour faire face au vieillissement démographique en Belgique: Réalités et perspectives”, Federal Planning Bureau WP 5-08.

Treasury highlights

1. The Treasury started its 2008 OLO benchmark programme with the issuance of a new 10-year benchmark bond. On 23 January, OLO 4.00% 28/03/2018 (OLO52) was issued for an amount of € 4 billion at a re-offer price of 98.030%, the equivalent of a yield of 4.244%. The bond offered a yield spread of 30 basis points over the German government bond due January 2018. Lead Managers were Citi, Fortis, HSBC and UBS.
   Market conditions were challenging and the spread guidance had to be revised upwards during the bookbuilding process. The additional momentum that followed the spread revision resulted in a final orderbook with orders from 150 separate accounts for a total amount of € 6.9 billion. In order to ascertain secondary market performance in volatile market conditions, it was decided to issue a € 4 billion transaction.

Treasury highlights (continued)

In terms of distribution, it was interesting to note the participation of Asian central banks (16%) and of real money investors in general (79%):

By region			
Belgium	27%	Other EU	4%
Other euro area	28%	Asia	16%
UK	17%	Americas	3%
Scandinavia	5%		

By type of investors			
Fund Managers	35%	ALM	15%
Central Banks/off.	24%	Hedge Funds	5%
Financial Institutions	16%	Insurance Comp.	5%

2. On 25 February, the Treasury issued a second new OLO benchmark. As a 3-year bond, OLO 3.50% 28/03/2011 (OLO53) was issued through an auction rather than by syndication.
   The Debt Agency accepted bids for a total amount of € 3.465 billion at a weighted average yield of 3.663%. The auction had a bid-to-cover ratio of 1.65.
   The choice for a 3-year tenor was motivated by the demand for short maturities as well as by the attractive funding level. In addition, OLO53 will improve the regularity of the redemption schedule.

3. Liquidity in the government bonds and bills markets in the euro area diminished considerably during the month of March. Market makers do not seem to be able to comply any more with the standards that used to be set in recent years, and bid/offer spreads widened whereas the spreads between the bonds of non-core countries and core countries further increased.

The OLO auction dates for the remaining of 2008 are the following:

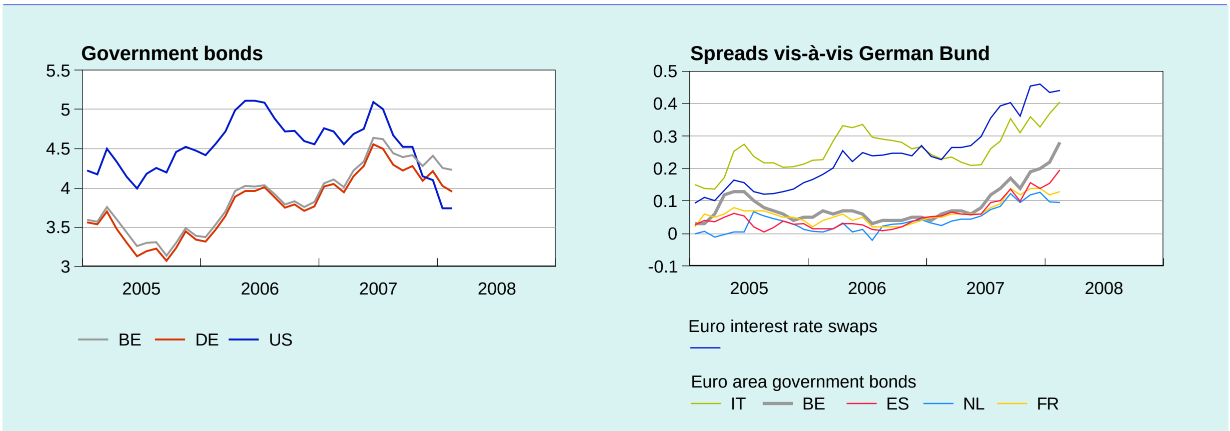
Issuance date	Settlement date
31 March	3 April
26 May	29 May
28 July	31 July

Issuance date	Settlement date
29 September	2 October
24 November	27 November

Please note that this schedule may be modified and that a syndicated new issue may replace an auction.

Government securities market

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



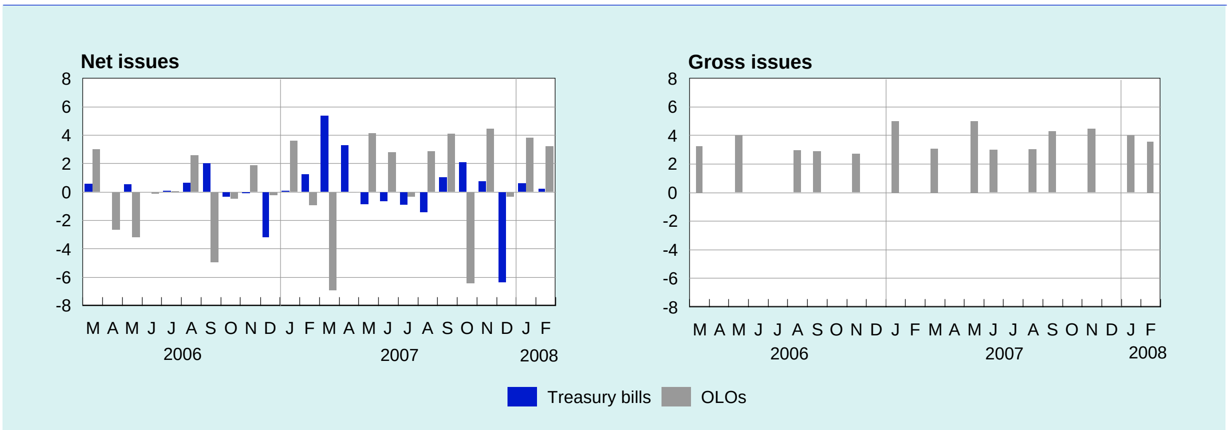
Sources: BIS, Datastream.

The decline in the long-term interest rates on government bonds, which started in July last year and was triggered by distress in the subprime segment of the United States mortgage markets, continued during recent months when market participants, due to their risk aversion, were continuously in search of a "safe haven" for their investments.

This decrease in interest rates was more pronounced in the United States where, from December 2007 and for the first time since early 2004, the interest rate level is again below that in the euro area. In the United States as well as in the euro area this decline was mainly the result of lower real long-term interest rates, but, due to their cyclical position, this factor was a lot more important in the United States. Ten-year break-even inflation rates only showed a minor decrease in both areas.

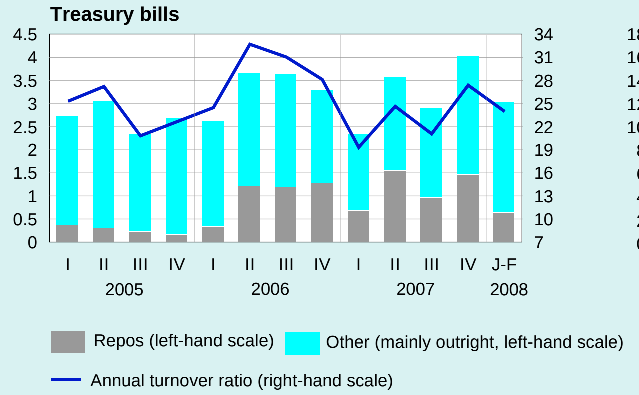
The financial turmoil also led to an increase of government bond spreads and of the spread on euro interest rate swaps vis-à-vis the German Bund which benefited from its high liquidity, a strong plus in these turbulent times.

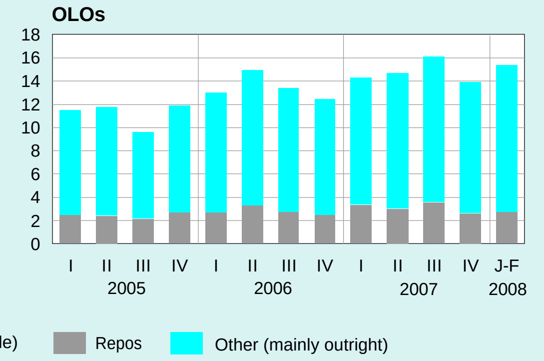
PRIMARY MARKET
(billions of euros)



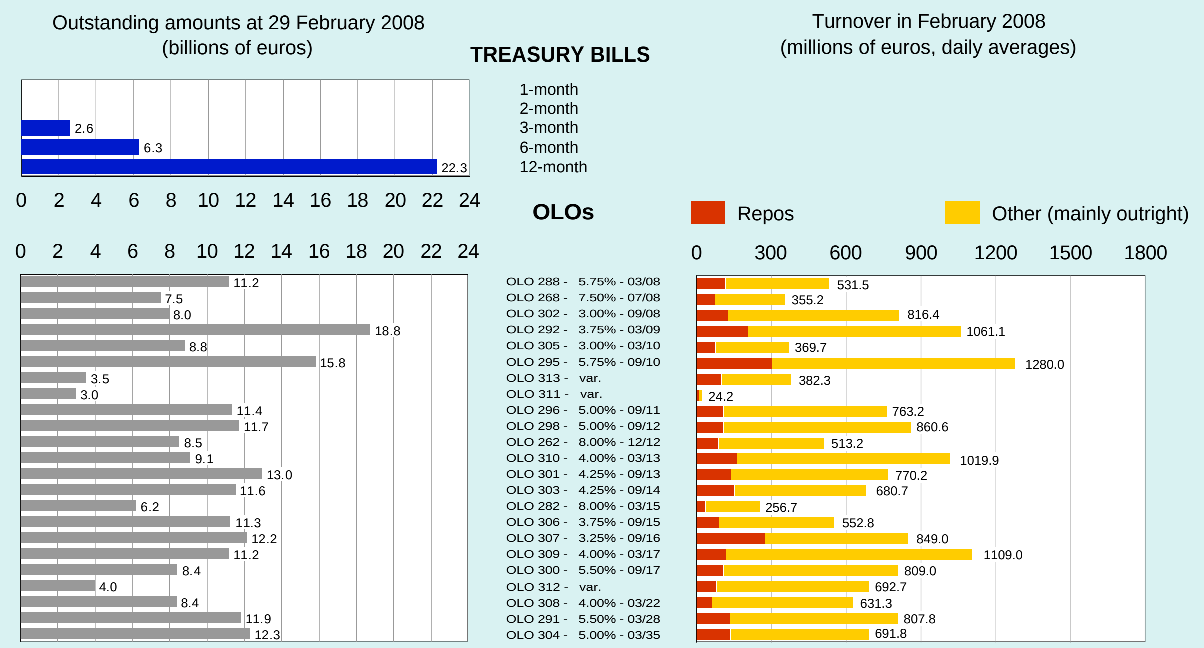
Government securities market (continued)

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





OUTSTANDING AMOUNTS AND TURNOVER



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Sources: NBB, unless otherwise stated.

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