6. Public finances

Belgium's general government deficit came to 4 % of GDP in 2011, thus remaining virtually unchanged against the previous year. The inadequate reduction in the structural deficit was the main reason for exceeding the target of 3.6 % set by the April 2011 stability programme. The structural growth of primary expenditure continued to outstrip GDP growth, particularly in the social security and local authority sectors. The public debt ratio increased by 2.4 percentage points to 98.6 % of GDP, mainly due to the State's purchase of Dexia Bank Belgium and the loans to the Greek, Irish and Portuguese States.

6.1 General government budget balance and debt

During the year under review, Belgium remained in an excessive deficit situation as defined by the European rules. Owing to the severe recession, the budget deficit had risen well above the threshold of 3 % of GDP in 2009. In December of that year, the Ecofin Council therefore recommended Belgium to cut its public deficit below that threshold by 2012, so long as economic growth did not fall short of the figure expected by the EC in its 2009 autumn forecasts. To achieve that, Belgium had to make

TABLE 13 TARGETS FOR THE OVERALL BALANCE OF BELGIAN GENERAL GOVERNMENT [1]
(in % of GDP)

	2007	2008	2009	2010	2011	2012	2013	2014	2015
Stability programme									
April 2008	–0.2	**0.0**	0.3	0.7	1.0				
April 2009		–1.2	**–3.4**	–4.0	–3.4	–2.6	–1.5	–0.7	0.0
September 2009 (complement)			–5.9	–6.0	–5.5	–4.4	–2.8	–1.3	0.0
January 2010			–5.9	**–4.8**	–4.1	–3.0	–2.0	–1.0	0.0
April 2011				–4.1	**–3.6**	–2.8	–1.8	–0.8	0.2 [2]
Actual figures	–0.3	–1.3	–5.8	–4.1	–4.0 e [3]				
p.m. Structural financing balance									
According to the EC's method	*–1.6*	*–2.2*	*–3.8*	*–3.3*	*–3.0*				
According to the ESCB's method [4]	*–0.7*	*–1.6*	*–4.5*	*–4.2*	*–3.9*				

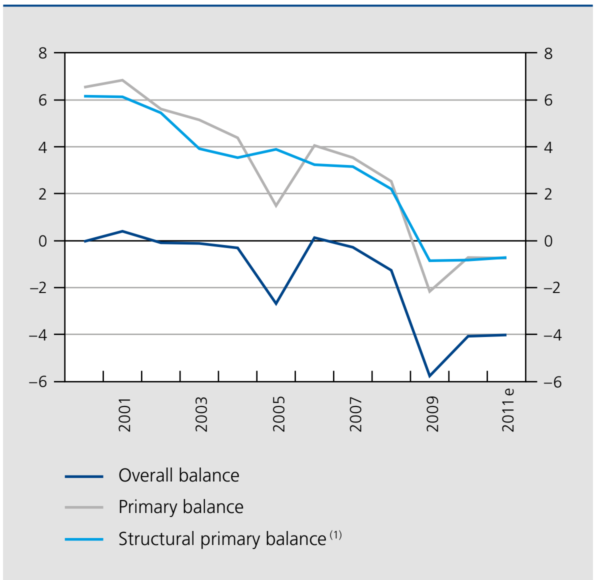
Sources: NAI, FPS Finance, NBB.
(1) As in the other tables and charts in this chapter, including – in accordance with the rules laid down for the excessive deficit procedure (EDP) – net interest gains on financial transactions such as swaps.
(2) In structural terms.
(3) The figures take no account of the possible impact of the guarantee amounting to 0.4 % of GDP granted to the private partners in the Arco group, owing to the uncertainty on the subject.
(4) According to the methodology described in Bouthevillain C., Ph. Cour-Thimann, G. van den Dool, P. Hernández de Cos, G. Langenus, M. Mohr, S. Momigliano and M. Tujula (2001), *Cyclically adjusted budget balances: An alternative approach*, ECB, Working Paper 77.

a structural budget effort averaging 0.75 % of GDP per annum from 2010 to 2012.

Under the stability programme submitted in April 2011, the budget deficit – which was down sharply in 2010 – was to be cut to 3.6 % of GDP in 2011. That target was tougher than the one under the previous stability programme, but the revision was smaller than the improvement seen in the 2010 accounts between these two programmes. However, during the year under review, the deficit remained virtually stable at around 4 % of GDP, or 0.4 percentage point above the target set in the stability programme. That cannot be attributed to lower-than-expected economic growth, as the economy grew by around 2 %, in line with the stability programme figure, despite the slowdown in activity during the second half of the year. The measures adopted in favour of Holding Communal which went into liquidation in December 2011, on account of the financial problems at Dexia, are only part of the reason. The deficit overrun therefore occurred primarily because of an insufficient reduction in the structural deficit.

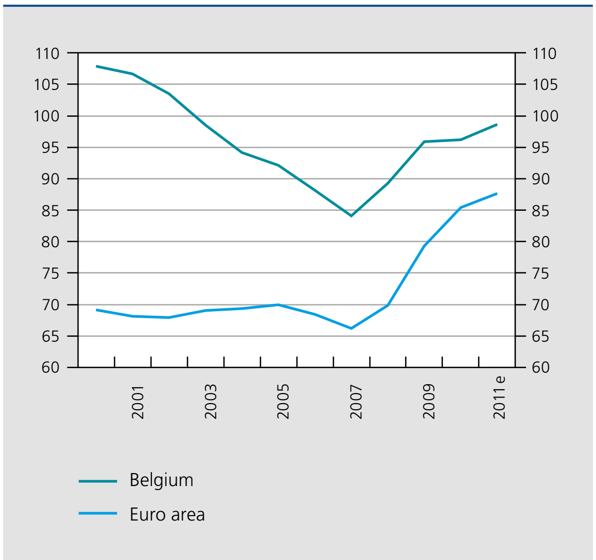
According to the EC's autumn forecasts, the structural deficit was expected to decline by 0.3 percentage point of GDP. However, those forecasts presumed that the budget target would be respected. The estimates which take account of more recent data on the movement in the budget balance, based on the harmonised method of adjustment for cyclical variations used by the ESCB – which also makes adjustments to take account of cyclical shifts in the composition of GDP – show a comparable reduction. The change in the structural balance measured in 2010 and 2011 falls well short of the average annual budget effort required to correct the excessive deficit in accordance with the Ecofin Council recommendations. According to the ESCB methodology, the structural primary balance continued to record a deficit of 0.7 % of GDP in 2011. The deterioration in this balance – totalling around 7 % of GDP since 2000 – indicates a very marked easing of fiscal policy in the past decade.

CHART 62 GENERAL GOVERNMENT BUDGET BALANCES
(in % of GDP)



Sources: NAI, NBB.
(1) According to the ESCB methodology.

CHART 63 CONSOLIDATED GROSS DEBT OF GENERAL GOVERNMENT IN BELGIUM AND IN THE EURO AREA
(in % of GDP)



Sources: EC, NAI, NBB.

The new federal government's coalition agreement confirms the fiscal targets set under the latest stability programme. On 26 November 2011, a large number of consolidation measures concerning both revenue and expenditure were announced in that connection for the period 2012-2014.

Between 1993 and 2007, the consolidated gross debt of general government had fallen continuously, dropping from 133.9 to 84.1 % of GDP. Owing to the public intervention in favour of a number of financial institutions at the end of 2008, it then climbed back to 89.3 % of GDP. The rise became steeper in 2009, owing to the increase in the deficit and the fall in GDP. The debt continued to grow in 2010, though less rapidly than in the previous year. In 2011, the expansion of the debt gathered pace again, taking it to 98.6 % of GDP at the end of the year.

In 2011, the debt was driven up by 2.4 % of GDP as a result of exogenous factors, which influence the debt but not the fiscal balance (for more details, see table 19 in the statistical annex). In October, the federal State bought Dexia Bank Belgium from the Dexia holding company for € 4 billion (1.1 % of GDP). During the year under review, the federal government debt also felt the direct effects of the sovereign debt crisis in the euro area. Thus, loan tranches were granted to Greece under bilateral agreements in the first rescue plan, and to Ireland and Portugal via the EFSF for a total of around 0.5 % of GDP. Another factor which contributed – temporarily – to the rise in debt in the year under review, amounting to 0.4 % of GDP, was the surplus cash resulting from the unexpected success of an issue of State notes which ended in December. Finally, taxes on company profits assessed in November and December 2011, amounting to around 0.2 % of GDP, will not be collected by the tax authority until 2012.

Box 8 – The Belgian budgetary framework in the light of the European requirements

In the context of the worsening sovereign debt crisis in the EU, national budgetary frameworks attract increasing attention. There is a growing conviction that strong and coherent national institutions are necessary to support the supranational regulations. Thus, an essential component of EU governance, reinforced in particular by the six legal texts dubbed the Six Pack, specifically concerns the improvement of the national budgetary frameworks. Council Directive 2011/85/EU, adopted in November 2011, lays down a series of minimum requirements on the subject, which all EU Member States must respect by the end of 2013 at the latest. Euro area countries have undertaken to meet these requirements by no later than the end of 2012.

The requirements defined in the Directive cover various aspects relating to the national budgetary frameworks, ranging from the method of drawing up the budget, and the statistics permitting monitoring of its execution, to numerical fiscal rules, and including medium-term budgetary planning and aspects concerning fiscal policy coordination, notably between levels of government. However, these are minimum requirements which, in many cases, are still relatively vague. Numerous European countries have already done much more to tighten up their budgetary framework, or have announced their intention to do so. Belgium has not yet followed suit, and still needs to take measures in certain areas to meet the EU's minimum requirements.

In regard to preparation of the budget, the Directive stipulates that the macroeconomic and budgetary forecasts used for the purpose must be realistic or prudent. The methodology used must be transparent and form the subject of a regular technical dialogue with the EC. Reasons must be duly given for any significant deviations in relation to the EC's forecasts. In October 2011, the Heads of State and Government of the euro area countries also said that budgets should be based on independent macroeconomic forecasts. In Belgium, the NAI's economic budget, based in practice on the transparent and independent macroeconomic forecasts of the Federal Planning Bureau, plays a key role in that respect. Although there may be doubt over whether this is a statutory obligation, these forecasts traditionally form the basis for drawing up the budgets of the federal government, social security, and the Regions and Communities. In general, any lack of prudence could only be due to delays in making up the budget, possibly causing some macroeconomic assumptions to be out of date. On the other hand, there is considerable room for improvement in the transparency and prudence surrounding the production of the public revenue forecasts, particularly in regard to the estimate of the budgetary impact of new measures. The High Council of Finance has already stressed the importance of an in-depth assessment of the methods used here. It is also important for the medium-term forecasts used in the stability programme to be based on the same principles of prudence and independence, and for the measures permitting attainment of the budget targets in that programme to be sufficiently specific.

More generally, it also seems appropriate to check whether the procedures for drawing up the various expenditure budgets, in which formal and informal indexation mechanisms often still play a major role in Belgium, are sufficiently geared to the need to improve the efficiency of the expenditure.

The Directive likewise lays down specific requirements on the availability of sufficiently reliable statistics, so that the implementation of the budget can be monitored in due course. Particularly in a country like Belgium, where the government is highly decentralised, it is vital to take the necessary measures to ensure that all government sub-sectors respect the new reporting obligation, and more generally, to see that the monitoring of public finances is based on reliable, timely data covering the entire public sector.

In addition, the Directive provides that EU regulations on the budget deficit and debt must be reflected in the national fiscal rules. In that connection, the Heads of State and Government of the euro area countries explicitly stipulated that the obligation to present a balanced budget in structural terms should preferably be anchored in the constitution. Several countries have already included fiscal limits or specific debt ceilings in their constitution, or will do so in the near future. In that connection, it is most usual to provide for specific, partly automatic correction mechanisms in the event of any breach of the rules, as is the case in Germany, Austria, Poland and Slovakia. Belgium has to align its legislative framework with the Directive, and it seems desirable to follow the best practices of other countries in that regard.

Another major aspect of the budgetary framework concerns the existence of an independent budget council, with advisory and supervisory powers. Although the Directive makes only an indirect reference to this, a number of European countries have recently set up such an institution or strengthened existing institutions. In Belgium, the High Council of Finance has significant powers via the Public Sector Borrowing Requirements section. However, there are some indications suggesting that the Council's influence over fiscal policy has weakened since the introduction of the euro (1). In this context, there is a need to examine what measures might enhance the effectiveness of the budgetary recommendations and surveillance by the High Council of Finance. Once again, Belgium could draw inspiration from the approach of other countries, for instance as regards the operating resources and procedures of such councils, the guarantees concerning the members' independence, the reporting obligations and the involvement of parliament and the academic world.

Finally, in the case of countries which have a degree of decentralised government, the Directive imposes obligations relating to the establishment of budgetary coordination mechanisms. The latter must concern all relevant aspects of fiscal policy, ranging from budgetary planning to compliance by all government sub-sectors with the said budgetary rules. To fulfil this obligation, there appears to be a need for new formal cooperation procedures between the federal government and the governments of the Communities and Regions, leading to transparent commitments. In that connection, it could be desirable to introduce automatic correction mechanisms for cases where a particular entity does not respect its budget targets. Moreover, effective policy coordination between the federated entities and the federal government is not only important at the level of fiscal policy, but is likewise necessary to carry out the macroeconomic recommendations under the European Semester and, more especially, to prevent or correct imbalances via the new excessive imbalance procedure (EIP).

(1) Cf. for example Coene L. and G. Langenus (2011), *Promoting fiscal discipline in a federal country : the mixed track record of Belgium's High Council of Finance*, Wirtschaftspolitische Blätter, Volume 58, n° 1.

6.2 Revenue

During the year under review, the fiscal and parafiscal revenues of general government nudged upwards from 43.2 to 43.4 % of GDP. This rise was due to a 0.3 percentage point increase in taxes on company profits and a 0.2 percentage point rise in levies on other incomes and on assets, partly offset by a decline in tax revenues on goods and services due *inter alia* to the gradual weakening of economic activity. Non-fiscal and non-parafiscal revenues were up by 0.3 percentage point, mainly as a result of the payments made by financial institutions.

The virtual stabilisation of levies on earned income resulted from a fall in personal income tax revenues and a slight increase in social contributions.

TABLE 14 REVENUE OF GENERAL GOVERNMENT (1)

(in % of GDP)

	2007	2008	2009	2010	2011 e
Fiscal and parafiscal revenue	43.2	43.5	42.7	43.2	43.4
Levies weighing chiefly on earned income	25.0	25.7	25.9	25.8	25.8
Personal income tax (2)	11.2	11.5	11.2	11.4	11.2
Social contributions (3)	13.9	14.2	14.7	14.5	14.5
Taxes on company profits (4)	3.5	3.4	2.5	2.7	3.0
Levies on other incomes and on assets (5)	3.7	3.7	3.5	3.7	3.9
Taxes on goods and services	10.9	10.7	10.8	11.1	10.8
of which:					
VAT	7.0	6.8	6.8	7.0	7.0
Excise duties	2.2	2.0	2.1	2.2	2.0
Non-fiscal and non-parafiscal revenue (6)	4.8	5.1	5.2	5.5	5.8
Total revenue	48.0	48.6	48.0	48.8	49.2

Sources: NAI, NBB.

(1) In accordance with the ESA 95, total revenue of general government does not include the proceeds of fiscal revenue which the government transfers to the EU.

(2) Mainly withholding tax on earned income, advance payments, assessments and the proceeds of additional percentages on personal income tax.

(3) Including the special social security contribution and the contributions of persons not in work.

(4) Mainly advance payments, assessments and withholding tax on movable property income of companies.

(5) Mainly withholding tax on income from movable property of individuals, withholding tax on income from immovable property (including the proceeds of additional percentages), inheritance taxes and registration fees.

(6) Income from property, imputed social contributions, current transfers and capital transfers from other sectors, plus sales of goods and services produced, including the remuneration on the guarantees granted by the State on individuals' deposits and interbank loans.

Personal income tax revenues were down by 0.2 percentage point of GDP. This decline was due mainly to the acceleration of the tax assessments at the end of the year, one factor being the success of Tax-on-web. That acceleration generated substantial refunds to individuals, which were only partly offset by the simultaneous increase in the additional percentages. The withholding tax on earned income should have gained from the surge in inflation, which normally causes it to expand by more than the tax base. The annual indexation of the scales used to calculate the withholding tax is based on the average increase in consumer prices during the previous year. In combination with the progressive structure of the tax scales, the surge in inflation therefore exerted upward pressure on withholding tax revenues amounting to around € 140 million. However, that increase was not reflected in an improvement in these revenues as a percentage of GDP.

The structural measures had a practically neutral influence on personal income tax. Thus, the phasing out of the fixed reduction in personal income tax in the Flemish Region and the increase in the withholding tax on temporary unemployment benefits boosted revenues by € 111 and 44 million respectively. Conversely, the other measures – such as the system of deductions for mortgage costs on owner-occupied homes and deductions for energy-saving investments – had a negative impact on these revenues in 2011.

Despite the small rise in the share of wages in the value added of the Belgian economy, social contributions remained practically stable as a percentage of GDP because a series of measures continued to reduce these contributions. Thus, the fixed structural reduction in employers' contributions was up by another € 128 million, one factor being the maintenance of the income threshold taken into account for the deductions on high wages, in a context of pay increases. In addition, the social contributions paid by self-employed workers, calculated on their income in the third year preceding the payments, declined as a percentage of GDP, because the year 2008 felt the first effects of the economic and financial crisis.

Taxes on company profits were up again, at 3 % of GDP, thus gradually regaining the average level recorded in the period 1997-2008. During the year under review, this revenue category benefited from the decline in the interest rate used as the reference for calculating the risk capital allowance, so that the negative impact of that system on public finances declined by € 280 million. In addition, the assessments increased sharply, largely as a result of the relatively low level of early payments since 2009.

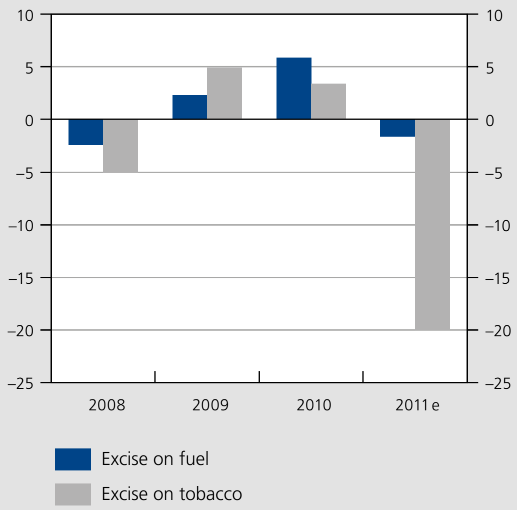
Levies on other incomes and on assets expanded by 0.2 percentage point of GDP during the year under review, notably as a result of the 18.1 % rise in revenues from withholding tax on movable property. This jump almost wiped out the fall in this type of revenue observed in 2009. In particular, it reflects the renewed growth of dividends paid by companies and the rise in interest rates. The withholding tax on income from immovable property, paid by both individuals and companies, also grew strongly by a total of more than 10 %, as did registration fees.

Taxes on goods and services were down by 0.3 percentage point, mainly because of the decline in nominal excise revenues. The rise in excise duty per unit on fuel and tobacco should have boosted revenues, but the fall in the consumption of these products led to the opposite result. VAT revenues, which continued to benefit from the vigorous growth of final demand at the beginning of the year, were also supported by various measures. On the one hand, the reduced VAT rate of 6 % for the construction or purchase of new housing, which had caused a further reduction in revenues of around € 150 million in 2010, was abolished. Also, since 2011, as a result of a decision by the EU Court of Justice, the sale of a plot of land in conjunction with a new house has given rise to a VAT payment instead of registration fees, and that has driven up VAT revenues by around € 100 million. These revenues have therefore remained practically stable as a percentage of GDP. Finally, the € 250 million collected each year from the nuclear power supply company between 2008 and 2010 was not collected in 2011.

Non-fiscal and non-parafiscal revenues grew strongly, partly because of the increase in the new levy under the deposit protection scheme for households, and partly because of the substantial rise in dividend payments to the government in return for its support during the financial crisis, including the first such payment by KBC.

CHART 64 EXCISE REVENUES ON FUEL AND TOBACCO

(percentage changes compared to the previous year)



Sources: NAI, NBB.

The federal government has extensive fiscal powers in relation to total Belgian public revenues, as it is in charge of VAT and the largest part of personal income tax. During the year under review, its revenues amounted to 26.6 % of GDP. However, following adjustment for transfers to other levels of government, the resources available to the federal government came to only 8.5 % of GDP, down by a further 0.5 percentage point compared to 2010. Thus, since the year 2000, the resources which the federal government has at its disposal for its own policies have declined sharply, by a total of 5.5 percentage points of GDP. That drop is attributable partly to the reduction in revenues which fall within its own fiscal powers, but more

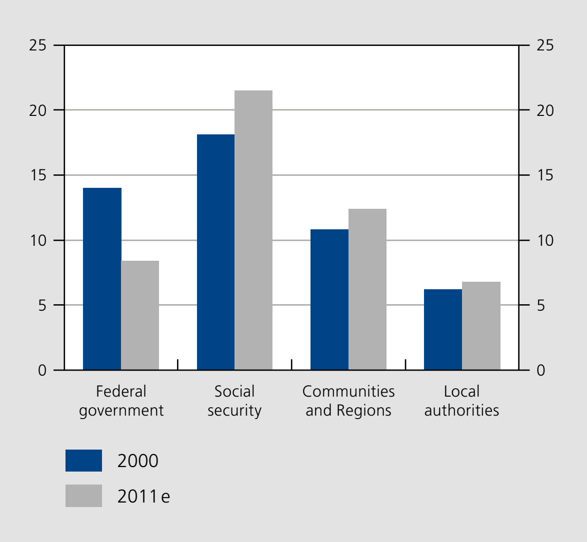
TABLE 15 NON-FISCAL AND NON-PARAFISCAL REVENUES

(in € billion)

	2008	2009	2010	2011 e
Total non-fiscal and non-parafiscal revenues	17.4	17.9	19.5	21.5
of which:				
Remuneration for guarantees on interbank loans	0.0	0.5	0.7	0.7
Remuneration for deposit guarantees	0.0	0.1	0.3	0.8
Commercial bank dividends	0.0	0.1	0.2	1.0

Sources: NAI, NBB.

CHART 65 REVENUES PER GOVERNMENT SUB-SECTOR
(after transfers between sub-sectors, in % of GDP)



Sources: NAI, NBB.

so to the increased transfers to the other government sub-sectors. In that regard, it is mainly social security that has received extra resources, both in relation to 2000 and in relation to 2010. This sub-sector's own revenues have remained practically stable, year on year, whereas it benefited from a further increase in transfers received from the federal government amounting to 0.3 percentage point of GDP. At the same time, the resources of the Communities and Regions recorded a strong 0.6 percentage point expansion, largely as a result of transfers received from the federal government, but also thanks to the growth of their own resources. Finally, local authority revenues were the most stable, being practically the same as last year and only slightly up over the past decade.

6.3 Primary expenditure

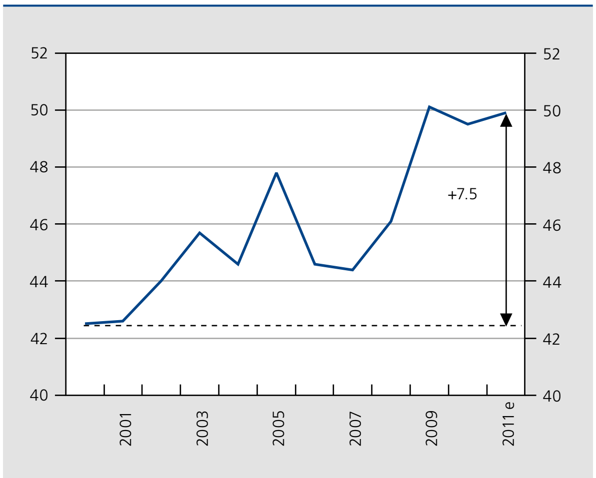
General government primary expenditure, i.e. spending excluding interest charges, was up by 0.4 percentage point of GDP against 2010. It thus came to 49.9 % of GDP, remaining at a very high level in historical terms. Primary expenditure had represented just 42.5 % of GDP in 2000. During the past decade, it has therefore risen by more than 7 percentage points of GDP, the reason being an average real increase of 2.8 % per annum, or 1.2 percentage points more than real GDP growth.

The volume of primary expenditure grew by 1.7 % in 2011. However, to obtain an accurate picture of the underlying trend in government spending policy, it is necessary to eliminate a range of non-structural components. These essentially include temporary factors, the impact of the business cycle on expenditure, and finally, the effect of the difference between the movement in the HICP, which is used to deflate primary expenditure, and the movement in public sector wages and social services resulting from the automatic indexation mechanism.

Non-recurring factors augmented the growth of expenditure by 0.4 percentage point. That was largely due to the impact of government measures in favour of Holding Communal which, as a major Dexia shareholder, felt the full brunt of the collapse of Dexia's share price. The liquidation of Holding Communal led to a capital transfer of 0.2 % of GDP following the assumption of guaranteed debts and non-repayment of short-term loans by Holding Communal. The bulk of this capital transfer was at the expense of the Regions, but the federal government also bore part of the cost of the operation.

In addition, the growth rate of primary expenditure is subject to cyclical fluctuations via the pattern of unemployment benefits. The buoyant economic activity in 2010 and in the first half of 2011 brought down the number of persons totally unemployed and drawing benefits, which tracks the economic cycle with a certain time lag. There was an even steeper decline in the number of persons temporarily laid off, a yardstick which responds faster to cyclical movements. Altogether, the cyclical component thus restrained the rise in expenditure by 0.3 percentage point.

CHART 66 GENERAL GOVERNMENT PRIMARY EXPENDITURE
(in % of GDP)



Sources: NAI, NBB.

TABLE 16 GENERAL GOVERNMENT PRIMARY EXPENDITURE

(deflated by the HICP, percentage changes compared to the previous year, unless otherwise stated)

	2007	2008	2009	2010	2011 e	Average 2000-2011 e
Level recorded (1)	44.4	46.1	50.1	49.5	49.9	46.0
Real growth recorded	3.1	2.3	7.0	0.4	1.7	2.6
Influence of non-recurrent or fiscally neutral factors (2)	1.7	–0.2	0.9	–1.3	0.4	0.2
Influence of cyclical factors (2)	–0.4	–0.2	0.7	0.0	–0.3	0.0
Indexation effect (2) (3)	–0.2	–0.4	1.5	–1.2	–0.5	–0.2
Real growth adjusted for cyclical non-recurrent or fiscally neutral factors and for indexation effects	2.0	3.1	4.0	2.9	2.2	2.8
p.m. Volume growth of GDP (4)	2.8	0.9	–2.7	2.3	1.9	1.6

Sources: DGSEI, NAI, NBB.
(1) In % of GDP.
(2) Contribution to real recorded growth of primary expenditure.
(3) Effect caused by the difference between the actual indexation of public sector wages and social security benefits and the rise in the HICP. The other effects due to differences between inflation measured by the HICP and the movement in price factors influencing other expenditure categories, whether they are attributable to the indexation mechanisms or to a divergent pattern in the prices of certain expenditure categories, are not adjusted owing to the absence of sufficient information or the complexity of the method to be used.
(4) Calendar adjusted data.

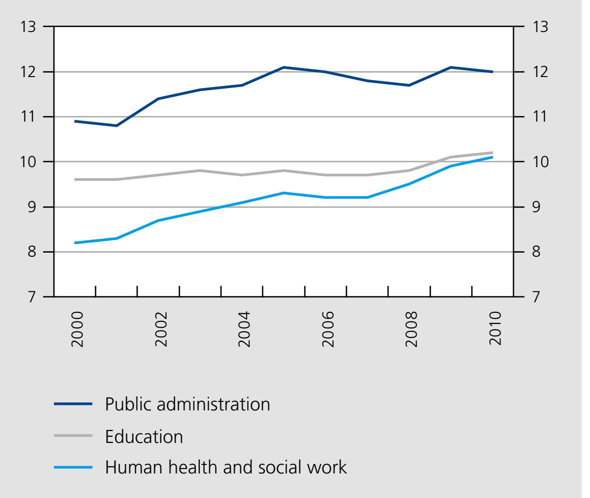
The automatic indexation mechanisms for civil service wages and social benefits are a third external factor which influences the real movement in primary expenditure. Via that mechanism, these wages and benefits, which account for over 60 % of primary expenditure, are linked to the movement in the health index of consumer prices, while the real movement in primary expenditure is measured by deflating the nominal movement by the change in the HICP. In 2011, the health index rose by 0.4 percentage point less than the HICP. In addition, any acceleration in inflation, such as that which occurred in 2010 and up to mid-2011, takes time to be reflected in the indexation of wages and social benefits. In 2011, they were not index-linked until May and June respectively, after the health index had exceeded the trigger index number in April. Overall, this difference depressed the volume growth of primary expenditure, measured against the HICP, by 0.5 percentage point.

After adjustment for these various factors, the real growth of primary expenditure came to 2.2 %. Though that is 0.6 percentage point lower than the average growth since 2000, it is still well above the trend GDP growth.

One of the structural factors which has contributed to the rise in primary expenditure in recent years is the remuneration of public sector workers and staff employed in areas of activity which are largely subsidised by the government, such as public administration, education, health and social work. That remuneration increased from 28.7 % of the total wage bill for all sectors in 2000 to 32.4 % in 2010. The rise was particularly marked in the health and social work branch, where remuneration increased from 8.2 to 10.1 % of the total over the same period. Public

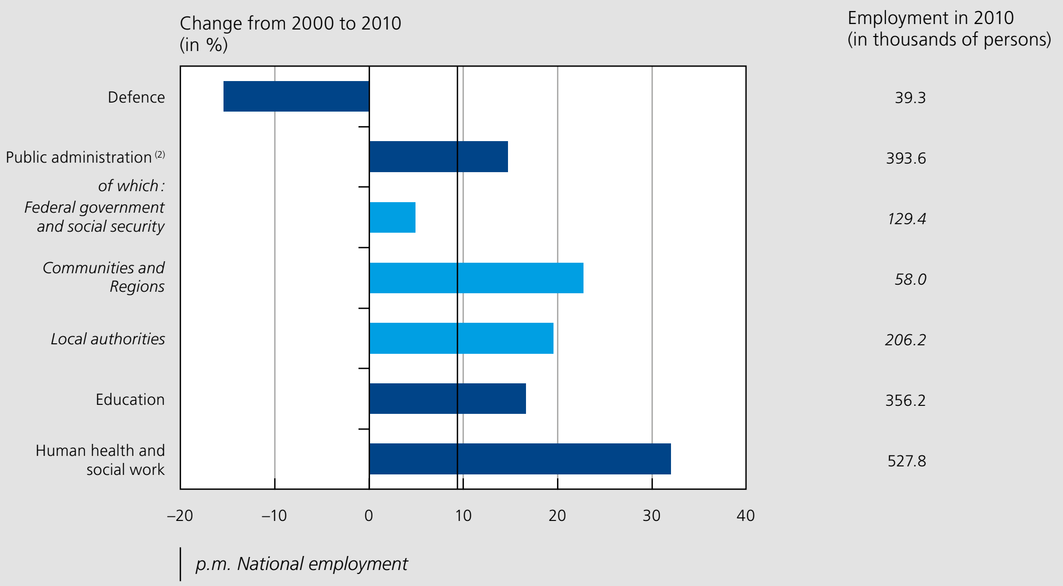
CHART 67 REMUNERATION OF EMPLOYEES IN PUBLIC ADMINISTRATION, EDUCATION, AND HUMAN HEALTH AND SOCIAL WORK

(in % of the wage bill of the Belgian economy)



Sources: NAI, NBB.

CHART 68 EMPLOYMENT IN PUBLIC ADMINISTRATION, EDUCATION, AND HUMAN HEALTH AND SOCIAL WORK (1)



Sources: NAI, NBB.
(1) Excluding the public broadcasting corporations, Aquafin, and the transfer, in 2002, of 8 500 federal police to the local police forces.
(2) Public administration excluding Defence.

administration also recorded strong growth, from 10.9 to 12 %, while the rise was smaller in the education branch, where the wage bill expanded from 9.6 to 10.2 % of the total.

Changes in employment are a key determinant of the rise in the remuneration of employees in these branches of activity. During the period 2000-2010, the number of jobs in these sectors grew by more than 20 %, far outpacing the growth of total national employment, which came to 9.4 %.

Between 2000 and 2010, employment in the public administration branch expanded by 11.1 %. Without the reduction of more than 7 000 units in the number of Ministry of Defence staff, the growth came to 14.7 %. Leaving aside the Ministry of Defence, employment in the federal government and social security was up by 4.9 %.

TABLE 17 ADJUSTED PRIMARY EXPENDITURE (1) BY GENERAL GOVERNMENT SUB-SECTOR (2)

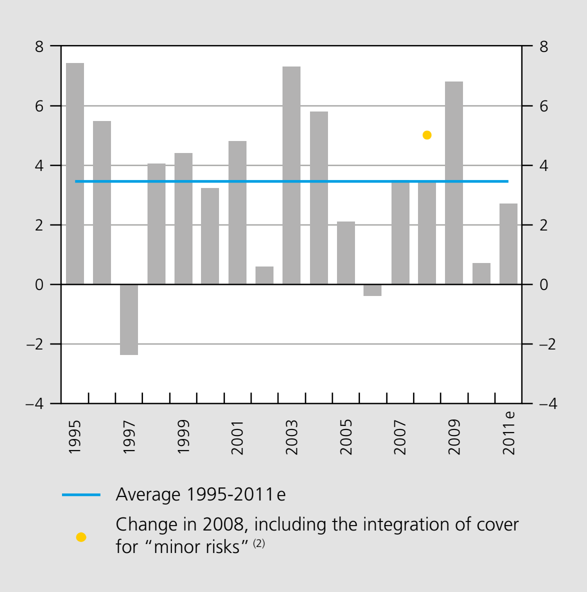
(deflated by the HICP, percentage changes compared to the previous year, unless otherwise stated)

	2007	2008	2009	2010	2011 e	Average 2000-2011 e
Entity I	2.9	3.9	4.5	3.2	2.3	2.9
Federal government	2.2	4.5	4.3	3.8	0.2	2.7
Social security	3.2	3.6	4.6	2.9	3.3	2.9
Entity II	0.3	1.8	3.1	2.3	2.0	2.6
Communities and Regions	1.3	2.5	3.3	2.2	1.7	2.6
Local authorities	–1.2	0.9	2.9	2.5	2.4	2.6

Sources: DGSEI, NAI, NBB.
(1) Real growth adjusted for the influence of cyclical, non-recurrent or fiscally neutral factors, and for indexation effects.
(2) The expenditure of the general government sub-sectors does not include mutual transfers.

CHART 69 PUBLIC HEALTH CARE EXPENDITURE [1]

(deflated by the HICP, percentage changes compared to the previous year)



Sources: NAI, NBB.

(1) Excluding sickness and invalidity benefits, benefits for the disabled, transfers to institutions caring for the disabled, and spending on long-term care insurance.

(2) Insurance against "minor risks" concerning health care became compulsory for self-employed persons in 2008, and increased both social security contributions collected and social security expenditure.

In the Communities and Regions, the number of workers employed in the public administration branch increased by 22.7 %, and in the local authorities the increase came to 19.5 %. In the education branch, the number of workers was up by 16.6 %. The moderate rise in the share of this sector's wages in the total wage bill is due to the large and growing proportion of part-time staff in education, at around 40 % in 2010. Finally, in the health and social work branch, employment grew by no less than 32 % in the period considered.

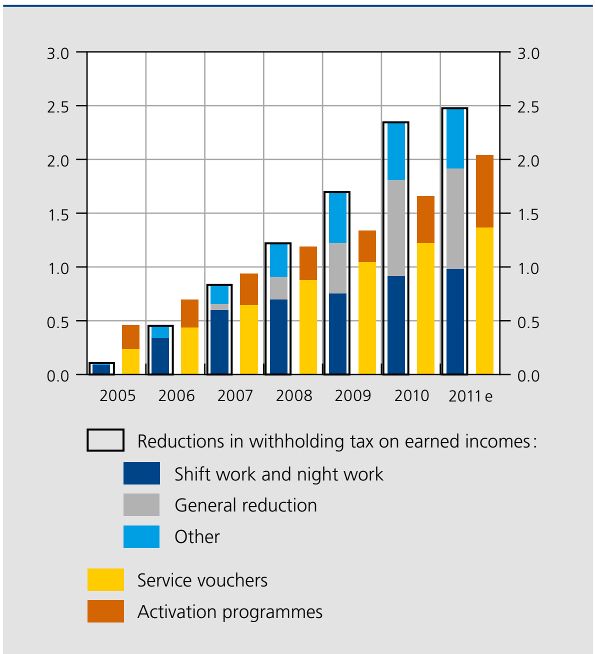
In 2011, the adjusted primary expenditure of federal government increased by 0.2 % in volume, representing a marked deceleration compared to the growth rate in the three preceding years. This very moderate growth is attributable mainly to a decline in staff remuneration in real terms and a sharp fall in intermediate consumption. Other federal primary expenditure rose strongly, notably the investment grants to the BNRC and the investment subsidies resulting from the reductions in withholding tax on earned incomes, both the general reduction and that for shift work and night work.

The volume growth of adjusted social security expenditure speeded up slightly in 2011, to 3.3 %. Expenditure on health care, which represents around one-third of social security spending, was up by 2.7 % in volume. Real expenditure on pensions increased at roughly the same rate as last year. The government measures to raise minimum pensions and the pensions of older retired persons had an impact of around € 90 million. Finally, sickness and invalidity benefits, unemployment benefits and family allowances were adjusted in line with prosperity at a total cost of € 230 million. As a result of these measures, but also the increase in the number of persons concerned, sickness and invalidity benefits recorded very strong growth again in 2011. The trend in this item, apparent for several years, therefore continued in 2011.

Finally, as in previous years, the subsidies paid by social security to enterprises increased strongly. Apart from expenditure relating to service vouchers, expenditure on activation measures for getting people back to work also merits a mention. Activation subsidies were up by € 140 and € 245 million respectively in 2010 and 2011, principally as a result of the Win-Win recruitment plan. The Win-Win plan targets workers in certain risk groups taken on during the period 2010-2011. They qualified for a higher working allowance of up to € 1 100 per month. The service voucher budget increased again

CHART 70 SUBSIDIES GRANTED TO COMPANIES: SERVICE VOUCHERS, REDUCTIONS IN WITHHOLDING TAX ON EARNED INCOMES AND ACTIVATION PROGRAMMES

(in € billion)



Sources: budget documents, NAI, NBB.

– by € 140 million – to almost € 1.4 billion. That figure takes no account of the tax deductions available in addition to users of these vouchers at the time of the personal income tax assessments.

The Communities and Regions kept the growth of their adjusted primary expenditure down to 1.7 %. This slowdown is attributable to various expenditure categories, such as investment and purchases of goods and services.

The volume growth of the adjusted primary expenditure of local authorities was almost stable at 2.4 %. Although the volume growth of local authority investment gathered momentum on account of the electoral cycle, wage increases were fairly modest. However, the effect of the electoral cycle on investment was less marked in 2011 than in other comparable years, because the financial position of local authorities was less favourable than in the past.

6.4 Interest charges and debt management

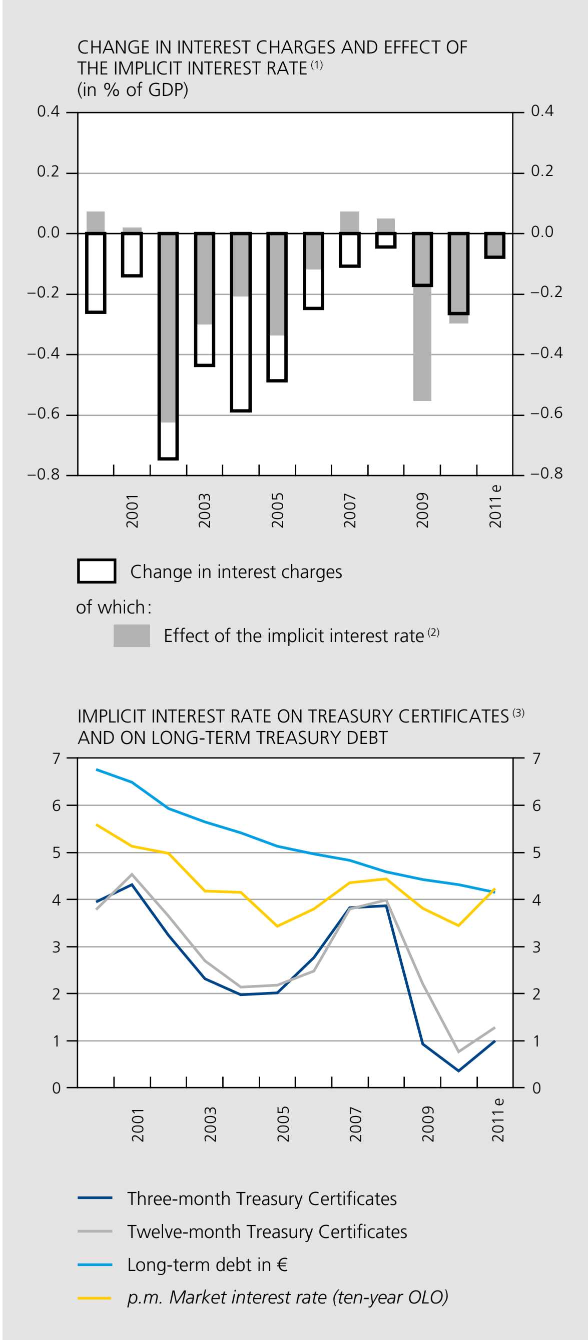
Interest charges

After having peaked at 11.6 % of GDP in 1990, interest charges declined constantly for two decades. That sharp contraction is due mainly to the marked fall in the implicit interest rate on the public debt and, up to 2007, the decline in the debt ratio. However, since 2008 that ratio has been rising again, restraining the fall in interest charges.

In 2011, interest charges were virtually unchanged at 3.3 % of GDP, as the limited rise in the debt ratio was offset by a new, small reduction in the implicit interest rate on the public debt. That is due essentially to the further decline in the implicit interest rate on the Treasury's long-term debt, which is by far the chief component of the total debt of general government. Despite the relatively strong rise in market interest rates in this segment in 2011, the long-term debts which matured or were bought back could still be refinanced more cheaply. However, in the second half of 2011, the market interest rate on Belgian government bonds clearly overtook the implicit interest rate. The decline in the long-term implicit interest rate recorded in 2011 was largely offset by the strong rise in the interest rate on the short-term public debt.

CHART 71 BREAKDOWN OF THE CHANGE IN INTEREST CHARGES

(in %, unless otherwise stated)



Sources: NAI, FPS Finance, NBB.
(1) For general government as a whole.
(2) Ratio between interest charges in the current year and debt at the end of the preceding year.
(3) Ratio between interest charges (including issue premiums for the long-term debt in euro) and the average outstanding debt.

Management of the Treasury debt

In 2011, the Treasury's gross financing requirements came to more than € 50 billion, well in excess of the 2010 figure. The amount of medium- and long-term loans maturing was smaller than in the previous year, but the net borrowing requirement grew significantly, key factors being the increase in the federal government budget deficit and the purchase of Dexia Bank Belgium. The amount of bonds bought back before maturity likewise exceeded the 2010 figure.

The Treasury financed this balance mainly by medium- and long-term issues in euro. The Treasury's short-term debts in foreign currencies remained practically unchanged, while the outstanding amount of Treasury Certificates was down sharply.

Long-term issues mainly concerned OLOs. Nevertheless, in the year under review, the Treasury issued a much larger number of State notes than in the previous year. That growth essentially concerns State notes for which the subscription period ran from 24 November to 2 December 2011, and the volume issued totalled € 5.7 billion. State notes maturing on 4 December 2016 were particularly popular.

TABLE 18 FINANCING REQUIREMENTS AND RESOURCES OF THE FEDERAL STATE

(in € billion)

	2009	2010	2011
Gross financing requirements . . .	28.8	43.5	50.4
Gross balance to be financed	25.7	37.0	42.9
Budget deficit or surplus (–)(1)	7.8	11.2	18.9
Medium- and long-term debt maturing during the year	17.9	25.9	24.1
In euro	17.9	25.3	24.1
In foreign currencies	0.0	0.6	0.0
Buy-backs (securities maturing the next year or later)	3.1	6.5	7.1
Other financing requirements	0.0	0.0	0.4
Funding resources			
Medium- and long-term funding	38.3	45.3	49.5
Linear bonds (OLOs)	35.0	40.9	40.9
State notes and others	3.3	4.4	8.6
Net change in the short-term debt in foreign currencies	–4.0	0.0	–0.1
Change in the outstanding amount of Treasury Certificates	–1.4	0.3	–5.3
Net change in other short-term debts in € and in financial assets	–4.1	–2.1	6.4

Source: FPS Finance.

(1) The budget balance is calculated on a cash basis and, among other things, takes account of financial transactions which are not included in the overall balance of general government which, in accordance with the ESA 95, is calculated on a transaction basis.

Guarantees granted to financial institutions

Against the backdrop of the financial crisis, the Belgian government, principally the federal State, granted guarantees. In principle, these have no influence on the budget balance and the debt unless they are called on. Leaving aside the guarantees on deposits, amounting to € 100 000 per customer and per financial institution, the maximum uncalled guarantees can be estimated at € 61.1 billion, or 16.5 % of GDP, at the end of 2011. Most of these guarantees concern interbank funding for Dexia, which is guaranteed up to a maximum assessed at € 41.9 billion, comprising both the residual guarantees under the old system dating from 2008 and Belgium's 60.5 % share in the new temporary guarantees granted to the Dexia holding company.

6.5 Overall balance of the general government sub-sectors

The accounts of the general government sub-sectors exhibited a divergent pattern following the developments described above and the movement in their mutual transfers. The deficit of Entity I, comprising the federal government and social security, began growing again in 2011. The deterioration in the balance is attributable solely to the federal government. The deficit of Entity II diminished, due to a marked fall in that of the Communities and Regions, while the local authority deficit remained stable. The deficit of Entity II thus remains significantly lower than that of Entity I.

In 2011, the federal government deficit was up from 3 to 3.4 % of GDP. The deterioration in the overall balance of this level of government is due solely to a further strong increase in transfers of tax revenues to the other entities.

These additional tax revenue transfers from the federal government are destined primarily for social security. That explains how the small deficit recorded for this sub-sector last year was maintained, despite higher expenditure on health care, other social benefits and expenditure on service vouchers and activation programmes, and despite the slight reduction in other forms of transfer from the federal government.

TABLE 19 OVERALL BALANCE OF GENERAL GOVERNMENT, AND PER SUB-SECTOR
(in % of GDP)

	2007	2008	2009	2010	2011 e
Primary balance	3.5	2.5	–2.2	–0.7	–0.7
Entity I	3.0	2.3	–1.6	–0.1	–0.5
Federal government	2.6	1.9	–0.8	0.1	–0.4
Social security	0.5	0.5	–0.7	–0.1	–0.1
Entity II	0.6	0.2	–0.6	–0.6	–0.2
Communities and Regions	0.5	0.1	–0.6	–0.5	–0.1
Local authorities	0.1	0.1	0.0	–0.1	–0.2
Interest charges	3.8	3.8	3.6	3.3	3.3
Overall balance	–0.3	–1.3	–5.8	–4.1	–4.0
Entity I	–0.6	–1.2	–4.9	–3.1	–3.5
Federal government	–1.1	–1.6	–4.2	–3.0	–3.4
Social security	0.5	0.5	–0.7	–0.1	–0.1
Entity II	0.3	–0.1	–0.9	–0.9	–0.6
Communities and Regions	0.4	–0.0	–0.7	–0.7	–0.3
Local authorities	–0.1	–0.1	–0.1	–0.3	–0.3

Sources: NAI, NBB.

The overall balance of the Communities and Regions improved significantly in 2011, from –0.7 % of GDP in 2010 to –0.3 % of GDP, as there was an increase in transfers of tax revenues from the federal government under the Special Finance Act. In addition, the Communities and Regions also recorded an increase in their own fiscal and non-fiscal revenues. Primary expenditure was up slightly owing to the non-recurring factor represented by capital transfers from the Regions in favour of Holding Communal. For the future, the revision of the Special Finance Act mechanisms for the Communities and Regions was one of the key aspects of the October agreement on the sixth State reform. The main features of that revision are presented in Box 9.

The local authority deficit remained at the previous year's level of 0.3 % of GDP. Revenue and expenditure increased slightly. Public investment was dynamic in the run-up to the 2012 local and provincial elections.

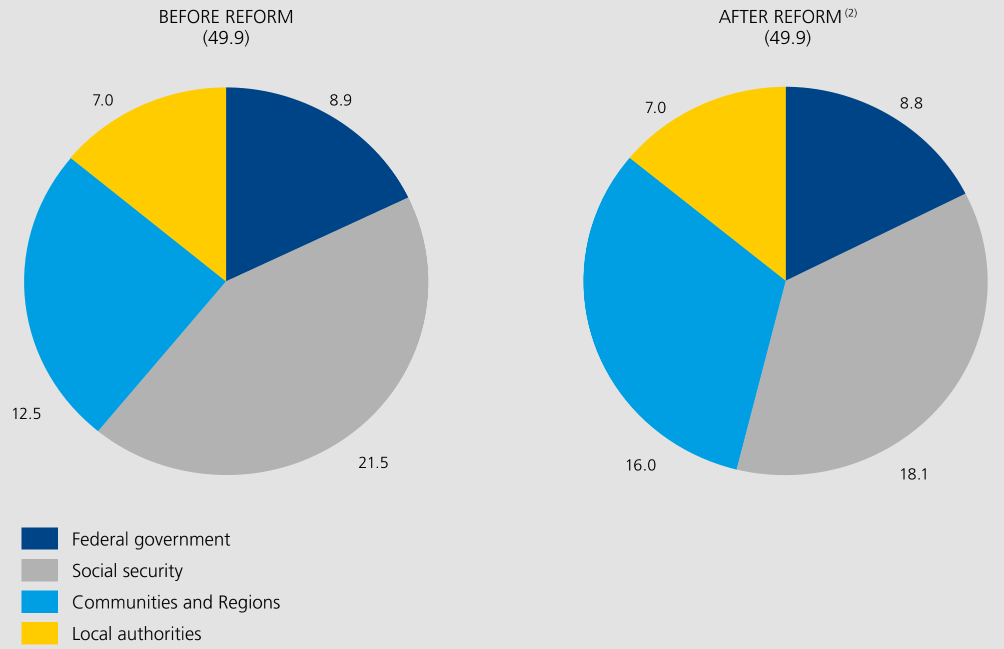
Box 9 – Sixth phase of the State reform and revision of the Special Finance Act

On 10 October 2011, eight political parties with a special majority in the federal parliament concluded an agreement on the sixth State reform which should largely enter into force in 2014.

Apart from more political and institutional aspects, this reform implies an additional transfer of powers from Entity I, comprising the federal government and social security, to the Communities and Regions. On the basis of 2011 data, that transfer would amount to around 4.4 % of GDP. The biggest transfers from a budgetary angle – roughly 2.8 % of GDP – are destined for the Communities: about 1.6 % of GDP for family allowances and 1.1 % of GDP for health care for the elderly (retirement homes, etc.), and for a range of other health care spending. The Regions gain new powers to which the federal government devoted resources equivalent to 1.6 % of GDP: 1 % of GDP on employment (of which 0.3 % of GDP in the form of reductions in revenues, and more specifically,

GENERAL GOVERNMENT SUB-SECTORS' PRIMARY EXPENDITURE [1]

(in % of GDP, estimate based on 2011 figures)



Sources: general policy statement, NAI, NBB.
(1) The expenditure does not include transfers between general government sub-sectors.
(2) Not including the powers transferred on the revenue side (fiscal expenditure, reductions in social security contributions).

reductions in social security contributions), 0.5 % of GDP on miscellaneous tax expenditure concerning mortgage loans, energy-saving investments and use of the service vouchers, and the balance on other areas of responsibility.

This transfer of powers is accompanied by a transfer of resources, requiring adjustments to the Special Finance Act for the Communities and Regions of 16 January 1989, which last underwent substantial revision in 2001 following the Lambermont agreements.

For the Regions, one of the main changes made by the draft new Finance Act concerns the greater tax autonomy which they will enjoy. They can thus levy 'expanded' additional percentages for an amount corresponding to around a quarter of the personal income tax revenues. The tax base is still determined by the federal government, which continues to collect the tax, but the Regions themselves can determine their own tax rates and their tax scales. Adjustments may, to a limited extent, affect the progressive character of the tax.

Apart from these revenues, the Regions receive additional resources for their new responsibilities, transferred on the basis of a fiscal key. These resources do not always cover the expected expenditure, and their growth rate is not fully tied to economic growth. Conversely, within the limits of their fiscal autonomy, the Regions will from now on benefit from a growth in the personal income tax proceeds which exceeds the trend growth of GDP. This results from two factors: the progressive character of the tax and population ageing, as the – rising – amount of the pensions paid forms an integral part of the tax base but not of GDP.

A solidarity mechanism in favour of the Regions whose per capita yield from personal income tax is below the national average is retained, but the detailed arrangements are modified. The reform rectifies 80 % of the discrepancy between the Region's share in the population and its share in the proceeds from personal income tax.

The Communities also receive additional resources for their new powers, but they are allocated on the basis of demographic keys. The resources available to them for their old powers are restructured and comprise an allocation according to the number of pupils in French- and Dutch-speaking schools plus an allocation based on a fiscal key.

Taking account of all the changes made to the method of funding the Communities and Regions, of which only the main ones are mentioned here, some entities would receive less resources under the new system than under the old one. A transitional mechanism in the form of an equalisation factor has been provided in order to ensure that no entity loses resources at the time of the switch from the old law to the new one. The amounts of this factor are fixed in nominal terms for ten years, then phased out over the ensuing ten years.

Apart from that, the Brussels entities – i.e. the Brussels Capital Region, the Community Commissions and the municipalities – receive additional resources totalling around 0.1 % of GDP. These resources come from various mechanisms. Thus, taking account of the net inflow of commuters to the Brussels Capital Region, an adjustment incorporates part of the incomes of commuters from the other two Regions. Another mechanism compensates the Brussels Capital Region for the revenues which it does not collect on the wages of officials of international institutions located in Brussels. Other resources are also earmarked for specific expenditure, such as security, bilingualism premiums and mobility.

Finally, as a contribution to the consolidation of public finances, the Communities and Regions will pay a contribution to the federal State for the pensions of their officials. In practice, it used to be the federal State that bore the whole cost of those pensions. This contribution is proportionately larger for the Communities since they employ more workers, especially teachers.