
SUMMARY AND RECOMMENDATIONS

The Advice of the Section “Public Sector Borrowing Requirements” is part of the preparation of the Stability Programme 2019-2022 which is to be submitted to the European Commission by the end of April 2019. The Advice complies with the provisions of the Cooperation Agreement of December 13, 2013 by formulating recommendations on the budgetary objectives for the general government on the one hand, and on the distribution of these objectives among the various levels of government on the other hand.

Economic Outlook 2019-2024 of the FPB (February 14, 2019)

The budgetary path 2019-2022 recommended by the Section derives from the Economic Outlook 2019-2024 of the Federal Planning Bureau (FPB), based on the data available on January 31, 2019. Both the budgetary and macro-economic parts of the Economic Outlook 2019-2024 are summarised in Table 1 and explained in detail in Chapter 1 of this Advice.

In the unchanged policy scenario, which has been used as benchmark for determining the necessary primary budgetary efforts regarding the path recommended by the Section, the nominal budget balance would amount to -2.3% of GDP in 2022. Therefore, the decline would concurrently amount to 1.5 percentage points of GDP compared to the budget balance estimation of 2018.

As the share of interest charges in the GDP decreased by 0.3 percentage point of GDP, the decline in the primary balance is sharper (-1.9 percentage points of GDP). Indeed, from 2021 onwards, a primary deficit of -0.4% of GDP is again forecast under unchanged policy (compared to a primary surplus of 1.5% of GDP in 2018).

Table 1
Summary of the perspectives 2019-2024 of the Federal Planning Bureau

MACROECONOMIC COMPONENT		2018	2019	2020	2021	2022	Δ2018-2022
Real GDP (% growth)	(1)	1.4%	1.3%	1.4%	1.4%	1.2%	
Potential GDP (% growth)	(2)	1.4%	1.3%	1.4%	1.4%	1.3%	
Output gap	(3)	<u>0.1%</u>	<u>0.1%</u>	<u>0.1%</u>	<u>0.1%</u>	<u>0.0%</u>	<u>0.0%</u>
Δ	=Δ(3)=(1)-(2)	0.0%	0.0%	0.0%	0.1%	-0.1%	
Nominal GDP growth (% growth)	(5)	2.7%	3.1%	3.0%	3.0%	2.9%	
GDP deflator (% growth)	(6)	1.2%	1.7%	1.6%	1.6%	1.7%	
BUDGETARY COMPONENT (general government, % of GDP)							
Total revenue	(7)	49.5%	48.6%	48.4%	48.4%	48.5%	-1.1%
Total expenditure	(8)	50.3%	50.3%	50.4%	50.7%	50.8%	0.4%
Primary expenditure	(7a)	48.1%	48.2%	48.5%	48.8%	48.9%	0.8%
Interest charges	(7b)	2.2%	2.1%	2.0%	1.9%	1.9%	-0.3%
Nominal budget balance	(9)=(7)-(8)	<u>-0.8%</u>	<u>-1.7%</u>	<u>-2.0%</u>	<u>-2.3%</u>	<u>-2.3%</u>	<u>-1.5%</u>
Δ nominal budget balance (FPB)		0.1%	-0.9%	-0.3%	-0.3%	0.0%	
Primary balance	(10)=(6)-(7a)	1.5%	0.4%	0.0%	-0.4%	-0.4%	-1.9%
Cyclical component	=0,61*(3)	0.0%	0.0%	0.0%	0.1%	0.0%	0.0%
One shots	(10)	0.7%	0.2%	0.0%	0.0%	0.0%	-0.7%
Structural balance	(11)=(9)-(4)-(10)	<u>-1.5%</u>	<u>-1.9%</u>	<u>-2.0%</u>	<u>-2.4%</u>	<u>-2.3%</u>	<u>-0.8%</u>
Structural primary balance	(12)=(10)-(4)-(10)	0.8%	0.2%	-0.1%	-0.5%	-0.4%	-1.2%
p.m. Budget balance Entity I (corrected for impact AF)		-0.4%	-1.5%	-1.7%	-1.9%	-2.0%	-1.6%
p.m. Budget balance Entity II Communities and Regions as a whole (corrected for impact AF)		-0.7%	-0.4%	-0.2%	-0.3%	-0.3%	-1.3%
Local authorities		-0.4%	-0.2%	-0.4%	-0.4%	-0.4%	0.1%
		-0.1%	0.0%	0.1%	0.1%	0.1%	-0.3%
		0.0%	0.0%	0.1%	0.1%	0.1%	0.1%
GOVERNMENT DEBT (general government, % of GDP)							
Debt ratio	(13)	<u>102.2%</u>	<u>101.7%</u>	<u>101.5%</u>	<u>101.4%</u>	<u>101.4%</u>	
Δ	=Δ(13)		-0.5%	-0.2%	0.0%	0.0%	-0.8%
Endogenous evolution	=Δ(13a)		-1.4%	-0.9%	-0.6%	-0.6%	-3.6%
Exogenous evolution	=Δ(13b)		0.8%	0.7%	0.6%	0.6%	2.8%

Source: HCF calculations based on FPB (February 2019): Economic Outlook 2019-2024.

Normative paths for the general government

The Section notes that the external environment in which the recommendation should be situated, is currently characterised by various factors of uncertainty. Firstly, there is **uncertainty about the underlying parameters**. Recent OECD and ECB prospects indicate a deterioration of the international economic context and significant political uncertainties (such as a slowdown in international trade, the risk of a no-deal Brexit).

In addition, some uncertainty exists about the extent of the decline in revenue from corporate income tax (CIT) (in share of GDP), after having risen to a historically high level in 2018. The extent to which a drop is observed from 2019 onwards is crucially dependent on the assumption regarding the cause of the increase in advance payments observed in the period 2017-2018. Should it have been a pure shift of the payment schedule of the total tax to be paid, the initial increase will be fully compensated later by lower corresponding assessment rolls. However, if the increase in advance payments was also caused by a structural increase in CIT revenue (e.g. due to a larger tax base), the correction will be more limited.

The FPB will publish the final version of the "Economic Outlook 2019-2024" in June 2019, which will take into account the latest information on both elements.

Secondly, there is uncertainty about the **underlying European requirements regarding the budgetary path**. Belgium is currently subject to the preventive arm of the European Stability and Growth Pact (SGP). Given the structural deficit of -1.5% of GDP in 2018 according to the FPB projection, the MTO (structural balance) ¹ has not yet been achieved. Therefore, a certain adjustment path towards the MTO must be followed. As the Belgian government debt has been assessed as high, an annual improvement of the structural balance of 0.6% of GDP is required by the SGP (until the MTO is achieved).

The Council of the EU can allow flexibility regarding the fixed adjustment path towards the MTO if a Member State has implemented structural reforms and a set of further requirements has been met. Within the framework of the Draft Budget 2019 (October 2018), Belgium has requested the application of the so-called "structural reform clause" based on reforms as regards pensions, taxes (*tax shift*, corporate income tax reform), labour market policy and government administration.

¹ The Section clarifies that a new minimum MTO was set early 2019 by the EC for the period 2020-2022. This is the structural balance. Due to modified demographic forecasts among others, the ageing-related costs, which are an important factor for determining the minimum MTO, are currently estimated by the EC at a higher level compared to 2016 (when the minimum MTO for the period 2017-2019 was calculated). This results in an upward revision of the minimum MTO. Therefore, the previous negative margin of -0.5 percentage point of GDP compared to the structural balance achieved in the period 2017-2019, has faded away. Based on an Advice of the Section (March 2016), it was decided to retain the structural balance as MTO in the Stability Programmes of April 2016, 2017 and 2018, and thus to set a more ambitious medium-term objective than the minimum required.

If flexibility is granted, a *lump sum* deviation from the adjustment path of 0.5% of GDP will be allowed in 2019, resulting in a required structural improvement of 0.1% of GDP.

In the context of its assessment of the Belgian Stability Programme 2019-2022 (April 2019), the Council of the EU will make in July 2019 its final decision as to whether flexibility is granted or not. Consequently, the Section considers it is appropriate to recommend two different scenarios, depending on the decision regarding the flexibility clause.

The recommended annual budgetary objectives are set in terms of a recommended improvement of the structural balance, in compliance with both the European budget rules and the Section's previous Advices. Adjustments for the impact of the economic cycle and one-off measures (*one shots*) were based on the forecasts of the FPB within the context of the "Economic Outlook 2019-2024" (February 2019).

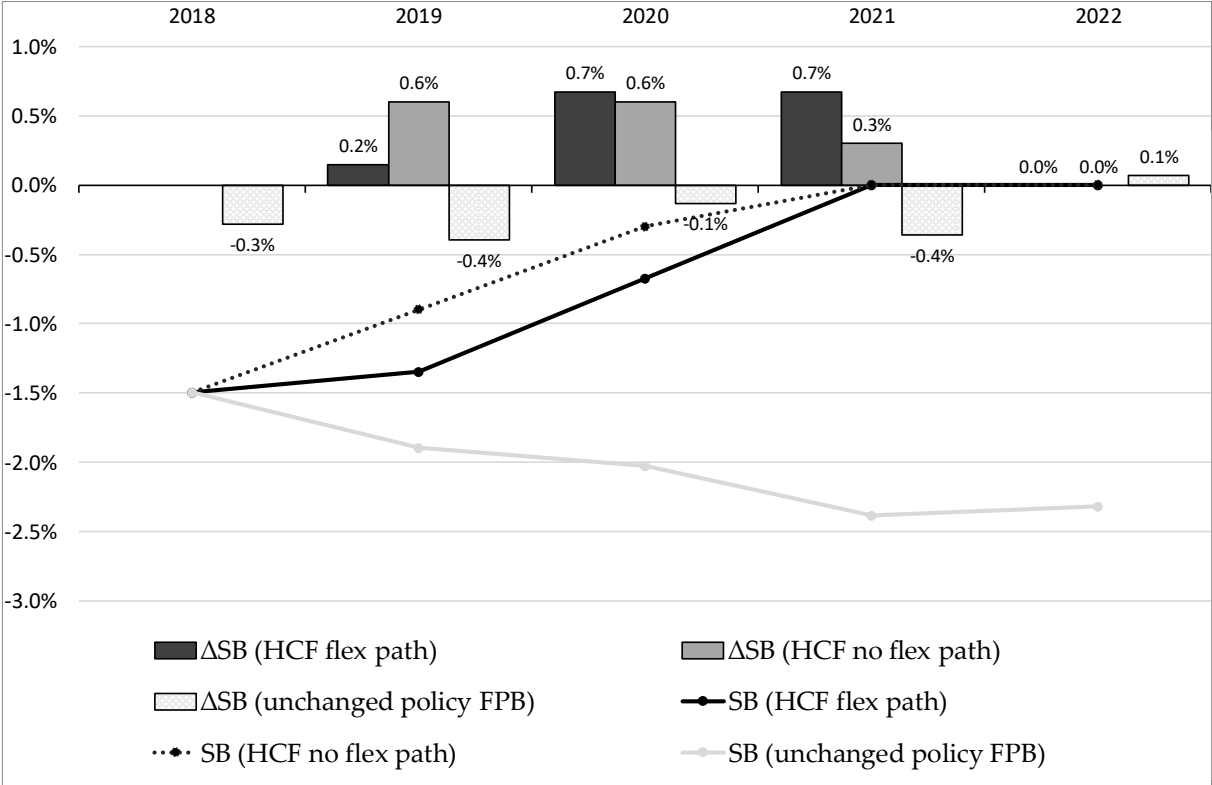
Both paths are illustrated in Chart 1 below. For a detailed explanation of the paths (standardised nominal budget balance, corresponding debt ratio), it is referred to point 2 of the Advice.

The MTO (structural balance) will be achieved in 2021 in both paths, but via different adjustment paths:

- In the first path, conditional to the approval of the flexibility clause, the Section takes note, for 2019, of the structural improvement of 0.2% of GDP corresponding to the commitment of the Belgian governments in the draft budget for 2019 (October 2018). The remaining structural improvement below, necessary to achieve the MTO in 2021, is then divided equally between 2020 and 2021.
- A second path, in case the flexibility clause is not granted. Here a different adjustment path towards the MTO is recommended. If the request for the application of the flexibility clause is not granted, an annual structural improvement of 0.6% of GDP is required based on the preventive arm of the SGP, until the MTO (structural balance) is achieved. In this path, the Section therefore recommends a structural improvement of 0.6% of GDP for 2019 and 2020. Finally, a structural improvement of 0.3% of GDP in 2021 remains necessary to achieve the structural balance.

The first path is more ambitious than what is strictly necessary according to the European criteria that will apply if the flexibility clause is granted by the Council of the EU. The Section considers that this path is opportune as it notices that the current FPB forecast estimates a structural deterioration of -0.3% of GDP in 2018. This is considerably lower than the requirements of the preventive arm of the SGP (namely a structural improvement of 0.6% of GDP) and previous commitments of the Belgian governments (draft budget 2018 and the Stability Programme 2018-2021).

Chart 1
Overview of the different recommended paths
and the scenario under unchanged policy



Source: HCF calculations based on FPB (February 2019): Economic Outlook 2019-2024.

Distribution of the paths of the general government

As provided for in the Cooperation Agreement of 13 December 2013, the Section has to elaborate an Advice on the budgetary objective in nominal and structural terms, for the various levels of government and for each community and region.

In order to achieve the MTO (structural balance) at the level of the general government in 2021, **the Section recommends that every sub-entity, including every community and region, should achieve the structural balance and maintain it for the rest of the path.**

The Section applied the following principles to determine the **adjustment path** towards the structural balance (MTO):

- The path suggested for the local authorities depends on the path relevant at the level of the general government. The Section recommends the achievement of the structural balance from 2019 onwards and it must be maintained for the duration of the path. This corresponds to a reduction in the structural surplus towards a structural balance, which must then be maintained.
- For determining the paths for the individual communities and regions (C&R), the Section upholds the principle that individual C&R that achieve a structural surplus in 2018 must at least maintain the structural balance (MTO) from 2019 onwards. If a structural deficit is still recorded in 2018, the structural balance must be achieved by 2021 at the latest. The distribution of the adjustment path towards this objective depends on the path considered at the level of the general government.
- Subsequently, the required structural improvement for Entity I was determined as the difference between the required improvement for the general government and the required structural improvement that derives from the paths for the local authorities and the C&R.

The Section considers that the implementation of the principles stated above results in an adjustment path that is similar for all levels of government that still showed a structural deficit in the starting year (2018).