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Recommendation for a

COUNCIL RECOMMENDATION

on the National Reform Programme 2011 of Belgium

and delivering a Council opinion

on the updated Stability Programme of Belgium 2011-2014

{SEC(2011) 710 final}

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THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Articles 121(2) and 148(4) thereof,

Having regard to Council Regulation (EC) No 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies[1], and in particular Article 5(3) thereof,

Having regard to the recommendation of the European Commission[2],

Having regard to the conclusions of the European Council,

Having regard to the opinion of the Employment Committee,

After consulting the Economic and Financial Committee,

Whereas:

(1) On 26 March 2010, the European Council agreed to the European Commission's proposal to launch a new strategy for jobs and growth, Europe 2020, based on enhanced coordination of economic policies, which will focus on the key areas where action is needed to boost Europe's potential for sustainable growth and competitiveness.

(2) On 13 July 2010, the Council adopted a recommendation on the broad guidelines for the economic policies of the Member States and the Union (2010 to 2014) and, on 21 October 2010, adopted a decision on guidelines for the employment policies of the Member States,[3] which together form the 'integrated guidelines'. Member States were invited to take the integrated guidelines into account in their national economic and employment policies.

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1 OJ L 209, 2.8.1997, p. 1.
2 OJ C , p. .
3 Maintained for 2011 by Council Decision 2011/308/EU of 19 May 2011.

(3) On 12 January 2011, the Commission adopted the first Annual Growth Survey, marking the start of a new cycle of economic governance in the EU and the first European semester of ex-ante and integrated policy coordination, which is anchored in the Europe 2020 strategy.

(4) On 25 March 2011, the European Council endorsed the priorities for fiscal consolidation and structural reform (in line with the Council's conclusions of 15 February and 7 March 2011 and further to the Commission's Annual Growth Survey). It underscored the need to give priority to restoring sound budgets and fiscal sustainability, reducing unemployment through labour market reforms and making new efforts to enhance growth. It requested Member States to translate these priorities into concrete measures to be included in their Stability or Convergence Programmes and National Reform Programmes.

(5) On 25 March 2011, the European Council also invited the Member States participating in the Euro Plus Pact to present their commitments in time to be included in their Stability or Convergence Programmes and their National Reform Programmes.

(6) On 15 April 2011, Belgium submitted its 2011 Stability Programme update covering the period 2011-2014 and its 2011 National Reform Programme. In order to take account of the interlinkages, the two programmes have been assessed at the same time.

(7) Belgium experienced robust GDP growth averaging 2.3% per year in the decade before 2008. The country felt the full impact of the global economic recession in 2009, and GDP contracted by 2.8%. The impact of the recession on employment was relatively contained. A temporary decline in hours worked and a decline in labour productivity per hour provided a buffer. After a decrease of 0.4% in 2009, employment increased again in 2010. However, unemployment rose from 7% before the recession to 8.3% in 2010. Thanks to the upturn in world trade, the recovery in 2010 was stronger than expected, with GDP growing by 2.2%. Due to the automatic stabilisers and the discretionary measures taken in reaction to the crisis, the general government deficit rose from 1.3% in 2008 to 5.9% of GDP in 2009.

(8) Based on the assessment of the updated Stability Programme pursuant to Council Regulation (EC) No 1466/97, the Council is of the opinion that the macroeconomic scenario underpinning the budgetary projections in the Programme is plausible. Although it is based on slightly less favourable growth assumptions for 2011, it is broadly in line with the latest Commission's Spring 2011 forecast. After a better-than-expected deficit of 4.1% in 2010, the objective of the budgetary strategy outlined in the programme is to further reduce the deficit to 3.6% in 2011 and below the 3% reference value by 2012, the deadline set by the Council for correcting the excessive deficit. The reduction in the deficit planned for 2011 seems feasible in view of the rather cautious economic projections. However, the fiscal effort is likely to be below the 0.75% of GDP average annual effort recommended by the Council, in particular in 2011 and 2012 when it would only amount to 0.4 and 0.3% of GDP in structural terms respectively. Moreover, the deficit targets for 2012 and subsequent years are not supported by specific adjustment measures. Lastly, the medium-term objective, which is a structural surplus of 0.5% of GDP, is not expected to be achieved within the 2011-2014 programme period.

(9) In view of the better-than-expected outcome recorded in 2010, a more ambitious reduction in the deficit in 2011, and faster-than-projected progress towards the 3% of GDP threshold, would be appropriate. Moreover, it will not be possible to bring the excessive deficit to an end by 2012 and to continue to make progress towards the medium-term objective without further consolidation measures. Since the tax burden, especially that on labour income, is already very high in Belgium, these consolidation measures should be essentially expenditure-based.

(10) The economic and financial crisis reversed the previous long-term trend of declining government debt. The debt ratio, which had been on a downward trend since 1993 (when it peaked at 134% of GDP, after which it continued falling to 84% of GDP in 2007), has increased again since 2008 and reached 96.8% of GDP at the end of 2010. The high level of public debt remains a major challenge, in particular because the long-term budgetary impact of ageing is higher than the EU average, mainly as a result of a relatively high increase in pension expenditure, which will put further strains on public finances. Ensuring sufficient primary surpluses over the medium-term and further reforming the Belgian social security system, in particular the pension system, to curb the projected substantial increase in age-related expenditure, should improve the long-term sustainability of public finances.

(11) An important challenge for Belgium is to ensure a stable and well-functioning financial sector, capable of meeting the financial intermediation needs of the real economy. During the past two years, the Belgian financial sector has been severely hit by the financial crisis, resulting in reduced balance sheets, substantial state aid and a modification of banking supervision. The financial situation of the banking sector remains fragile. Furthermore, in Belgium the banking sector is highly concentrated and relatively large compared to the size of the economy.

(12) The 1996 Law on ‘Employment Promotion and Precautionary Protection of Competitiveness’ stipulates that the trend in wages in Belgium should be in line with the wage trend in the three neighbouring countries (France, Germany, The Netherlands), thereby keeping labour costs under control. Nevertheless, this law has not been able to prevent a situation where, over the period 2005-2010, wages have increased faster in Belgium than in the three neighbouring countries, while productivity growth has been slower. As a consequence, unit labour costs have risen at a faster rate in Belgium compared to its neighbouring countries and the euro-area average. This is particularly problematic as Belgium is specialised in goods with relatively low technology content, facing fierce competition from lower-cost countries. Even though the wage rule helps to frame the wage negotiations, it could be improved by taking into account differences in productivity growth and by providing a more effective system to implement corrections *ex post* if the targets are not met.

(13) The labour market is characterised by a number of rigidities that create significant disincentives to taking up work, namely: unlimited unemployment benefit duration; high effective marginal tax rates and high tax wedge (particularly for low paid workers); and the combination of the withdrawal of social assistance benefits and high taxation when taking up work. Moreover, several exit routes for older workers provide incentives to leave the labour market before the statutory retirement age of 65. Further reform of active labour market policies, and extending them to cover the over 50, would help increase the overall employment rate and improve incentives to look for jobs. In addition, further decreases in the level and duration of unemployment benefits

over time would provide younger workers with a greater incentive to enter the labour market. Making the access criteria for early retirement more stringent would encourage older workers to stay within the active labour force, and older workers who have been out of work for a period of time to return to the labour market. Lastly, non-EU nationals have an employment rate (40.9 %) much lower than the EU average.

(14) The overall tax burden on labour in Belgium is one of the highest in the EU; therefore, its reduction would contribute to making work more attractive. However, given the substantial consolidation effort ahead, this needs to be compensated by equivalent increases in less distorting taxes, for example on consumption or by means of a shift towards environmentally-friendly taxes. Belgium has much lower implicit tax rates on energy than neighbouring countries. Combined with the high tax wedge on labour, Belgium has the lowest ratio of environmental taxes compared with labour taxes in the whole of the EU. This has contributed to a situation where high unemployment coexists with a relatively high use of energy, making it more difficult to achieve targets on employment and energy efficiency.

(15) Prices for many goods and services are generally higher than in other Member States, reflecting weak competitive pressures — especially in the retail sector and network industries — and a weak supervisory framework. In the retail sector, barriers to entry and operational restrictions are high. In particular, competition-restricting regulations still restrict opening hours, protect incumbents against new entry and inhibit the spread of new business models and technologies. A common competition problem in the network sectors in Belgium is the strong position of the incumbent and the high entry barriers compared to other Member States, meaning that former monopolists in these sectors can still reap higher profits by charging higher prices than a competitive market would allow.

(16) The Belgian authorities have made a number of commitments related to the Euro Plus Pact[4]. The commitments refer to the four areas of the Pact. They focus on measures to bring down the deficit, keep energy prices under control and encourage competition, control real wage increases, implement a supervisory framework to monitor the financial sector and introduce measures to increase the effective retirement age. However, there is no information on the measures to be taken in order to achieve the required objective on the fiscal side; nor is there any information on how real wage growth or energy prices could be controlled. Concerning early retirement schemes, it is not clear whether and when the 'Generation Pact' will be reviewed and what the impact of that review would be in terms of concrete measures. These commitments have been assessed and taken into account in the recommendations.

(17) The Commission has assessed the Stability Programme and National Reform Programme, including the Euro Plus Pact[5]. It has taken into account their relevance for sustainable fiscal and socio-economic policy in Belgium, and compliance with EU rules and guidance, given the need to reinforce the overall economic governance of the European Union by providing EU level input into future national decisions. In this light, the Commission considers that a more ambitious reduction of the deficit in 2011 should be possible, and that further consolidation measures should be specified for

[4] More details on the commitments made under the Euro Plus Pact can be found in SEC(2011) 710.
[5] SEC(2011) 710.

2012 and beyond. In order to improve the long-term sustainability of public finances, further reform of the pension system is needed. Further steps should also be taken to strengthen competitiveness, to help people into jobs and to shift the tax burden from labour to consumption and energy, as well as opening up more opportunities for investment and growth in the service sector and network industries.

(18) In the light of this assessment, also taking into account the Council Recommendation of 2 December 2009 under Article 126(7) of the Treaty on the Functioning of the European Union, the Council has examined the 2011 update of the Stability Programme of Belgium and its opinion[6] is reflected in particular in its recommendation under (1) and (2) below,

HEREBY RECOMMENDS that Belgium should take action within the period 2011-2012 to:

(1) Take advantage of the ongoing economic recovery to accelerate the correction of the excessive deficit. To this end, take the necessary measures — mainly on the expenditure side — by the time of the 2012 budget to achieve an average structural effort of at least 0.75% of GDP. This should bring the government deficit well below the 3 % of the GDP reference value by 2012 at the latest. Ensure progress towards the Medium Term Objective by at least 0.5% of GDP annually.

(2) Take steps to improve the long-term sustainability of public finances. The focus should be on putting in place a strategy aimed at curbing age-related expenditure, including by preventing early exit from the labour market in order to increase the effective retirement age, and linking the statutory retirement age to life expectancy.

(3) Address the structural weaknesses in the financial sector, in particular by finalising restructuring of the banks in need of an adequately funded and viable business model.

(4) Reform, in consultation with the social partners and in accordance with national practice, the system of wage bargaining and wage indexation, to ensure that wage growth better reflects developments in labour productivity and competitiveness.

(5) Improve participation in the labour market by reducing the high tax and social security burden for the low-paid in a budgetary neutral way and by introducing a system in which the level of unemployment benefits decreases gradually with the duration of unemployment. Take steps to shift the tax burden from labour to consumption and to make the tax system more environmentally friendly. Improve the effectiveness of active labour policies by targeting measures at older workers and vulnerable groups.

(6) Introduce measures to boost competition in the retail sector, by lowering barriers to entry and reducing operational restrictions; and introduce measures to strengthen competition in the electricity and gas markets by further improving the effectiveness of the sectoral regulatory and competition authorities.

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[6] Foreseen in Article 5(3) of Council Regulation (EC) No 1466/97.

Done at Brussels,

For the Council
The President