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Economic Developments in Belgium in 1964

21 pages

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Summary

Aggregate demand increased faster than output during 1964, so that Belgian prices continued to rise at a fairly rapid rate.[1/] To brake the expansion of private credit, the monetary authorities took further restrictive action over the summer months. But this action had the effect of stepping up the rise in Belgium's official gold and foreign exchange reserves, thus frustrating this action in part.

Consumer expenditures in the first half of 1964 appear to have exceeded the level of a year earlier by around 8 per cent at current prices, under the stimulus of further large wage increases, and housing demand has risen sharply this year. Although exports continued to add to incomes in Belgium, their increase has slackened considerably since late last year. The rise in industrial production slowed down in the second quarter, seemingly because of the scarcity of labor and plant capacity limitations, and employment in industry could not be increased during the first half of the year. By September, wholesale prices were 5.2 per cent higher than a year earlier, consumer prices were up 4.7 per cent, and the price rise showed no clear signs of abating.

In the second quarter, the money supply rose at a seasonally adjusted annual rate of over 10 per cent, and bank credit extended to the private sector increased rapidly. In January, the National Bank of Belgium

1/ See Recent Economic Developments in Belgium, November 1963-April 1964, dated May 21, 1964.

attempted to reach an accord obliging the commercial banks to cut the rate of increase of private credit from 20 per cent in 1963 to 10 or 12 per cent in 1964, but without success. Consequently, the National Bank of Belgium raised many of its lending rates by 1/4 or 1/2 of 1 per cent on July 3. At the same time, using authority given to it in 1961, the Banking Commission imposed a cash reserve requirement on the commercial banks. The requirement is currently only 1 per cent of deposits but can be made much more severe.

Treasury operations have been less expansionary so far in 1964, marking a distinct improvement over last year. In the first seven months of 1964 the deficit was well below last year, and the Treasury has enjoyed far more success this year in floating long-term issues. Under these circumstances, there has been a sharp contraction in Treasury recourse to bank credit and foreign borrowing. Budget estimates for 1965 reportedly call for a further drop in the deficit.

Interest rates have continued to rise, but the advance has slowed in recent months. Pressure in financial markets has been somewhat relieved by a reduction in Treasury borrowing requirements and by inflows of capital from abroad.

A balance of payments shift from an $82 million deficit in the last half of 1963 to a $12 million surplus in the first six months of 1964 was probably partly seasonal, but it also stemmed from increased foreign borrowing by local authorities and public sector institutions and enterprises. Because of a widening trade deficit, however, the first half results compare unfavorably with the $78 million surplus in January-June of last year.

Official gold and foreign exchange reserves rose about $170 million from end-June to mid-November, most of the increase occurring in October-November. The most likely explanation of these accruals is capital inflow induced by tighter credit conditions in Belgium.

Consumer demand and exports spark continuing boom

Aggregate demand in Belgium continued to rise rapidly in the first six months of 1964. Most of the increase came from private consumers, whose purchases were up over a year earlier by an estimated 3.9 per cent at constant prices, a rise which would appear to approximate 8 per cent in actual money expenditure. This estimated increase was scarcely smaller than the 8.8 per cent year-to-year increase in 1963 in private consumption at current prices. The higher level of consumption was supported by much higher wage rates, which in January-June were up 9 per cent over a year earlier. (See Table 1.)

Within the six months period January-June, the pace of consumption may well have continued to be as rapid as before, since wage rates in industry rose 5.2 per cent from December 1963 to June 1964, an increase that exceeded the 5.0 per cent rise between December 1962 and June 1963. The continuing rapid rise in wage rates reflects the strong demand for labor, the increasing difficulty in finding workers, and rising consumer prices which raise wage rates through the sliding scale clause contained in virtually all wage contracts. Some observers state that private consumer outlays were not much affected during the first 8 or 9 months of 1964 by the tightening in February of the terms for installment purchases of consumer durables. On the other hand, the drop in seasonally-adjusted department stores sales in the second quarter may indicate that the tightening had some effect.

Although exports continued to add to Belgian incomes in 1964, their increase has been slower this year than last. The gain in seasonally-adjusted exports of 6.3 per cent between the fourth quarter of 1963 and

Table 1. Belgium: Selected Economic Indicators, 1963-64
(1953=100)

	Dept. store sales1/	Wage rates in industry2/	Unemployment (in 000's)1/	Industrial production1/	Wholesale prices	Consumer prices
Quarters						
1963 - I	175	160	38	144	105.5	114.1
II	176	167	33	153	105.1	114.4
III	182	168	30	152	105.0	115.1
IV	185	172	29	157	107.4	116.7
1964 I	193	177	26	162	109.3	117.9
II	189	181	26	163	110.5	118.9
III	n.a.	n.a.	25	n.a.	111.1	120.8
Months						
1964 - March	192	177	25	163	109.6	117.6
June	186	181	25	163	111.1	119.9
July	189	n.a.	25	n.a.	110.7	120.8
Aug.	n.a.	n.a.	24	n.a.	111.3	120.8
Sept.	n.a.	n.a.	25	n.a.	111.4	120.9
Oct.	n.a.	n.a.	n.a.	n.a.	n.a.	121.2

1/ Seasonally adjusted.
2/ End of period.

Source: OECD and National Bank of Belgium.

July-August 1964 was much less rapid than the 15.0 per cent rise in the same period of last year.

Housing demand has been very strong; permits for new house building in the first five months of this year ran some 35 per cent higher than the 1963 monthly average. According to estimates by the National Bank of Belgium, investment outlays by industry (which scarcely rose in 1963) were down 10 per cent in the first half of 1964 from their level in the last half of 1963. Last February, interest subsidies on investment loans were suspended for six months. But surveys of investment intentions indicated that investment in industry would be sharply higher, by 20 per cent, in the final six months. To limit demand pressures, the central government has reportedly been deliberately holding down its own investment expenditures and restricting those of local authorities.

Output in Belgium has not been able to keep pace with demand, as is indicated by both rising prices and the very rapid advance in imports of 14.6 per cent from the fourth quarter of 1963 to July 1964. The National Bank of Belgium reports that it was not possible to increase industrial employment during the first half of 1964, and the further decline in unemployment was negligible. In the first quarter of 1964, seasonally-adjusted industrial production was up 3.2 per cent over the preceding quarter, but the further advance in the second quarter was only 1/2 of 1 per cent. (See Table 1.) In the third quarter, according to the Kredietbank, the labor market tightened further and more business concerns were unable to expand production because of plant capacity limits.

Price increases continue

The fairly rapid increases in prices which began during the summer of 1963 have continued in 1964, and a slackening of the rate of rise during the third quarter appears to have been largely if not entirely seasonal. For the third quarter, wholesale prices averaged 5.8 per cent higher than a year earlier and the comparable rise in consumer prices was 5.0 per cent. (See Table 1.)

Rising prices of imported goods have contributed to the general increase in wholesale prices in the past year, but prices of domestically produced goods have undergone an equally large increase. Prices of agricultural and industrial products have both risen; the latter, in particular, were up 6.6 per cent in the third quarter relative to a year earlier. At the retail level, in the third quarter as a whole, the yearly increases amounted to 5.8 per cent for food and 3.5 per cent for non-food articles; both were exceeded by a 9.1 per cent rise in the index of prices of services, which, however, includes only five items (haircuts, laundering, newspapers, movies, and transportation).

Since February, pork has been subject to retail price controls; ceilings on retail beef prices, also imposed in February, were lifted in June but reimposed in August. Prices of a wide range of commodities in Belgium are also subject to continuing government approval, and many price increases were sanctioned during the spring and summer. In addition, the government announced that increases in these prices would be authorized only on the grounds of increases in the prices of raw materials or wage increases granted under "normal agreements," and ruled out increases based on "competition in the labor market."

Monetary expansion is rapid in second quarter

During the first quarter of 1964 there was no change in the money supply on a seasonally-adjusted basis. But monetary expansion became rapid in the second quarter, when the seasonally-adjusted rise came to nearly 10.5 per cent at an annual rate. Private credit rose substantially more in the second quarter than a year earlier.

In the first quarter, the money supply contracted by BF 4.7 billion, compared with a BF 8.1 billion rise a year earlier. (See Table 2.) Comparing these two periods, there was an adverse shift in the balance of payments, a large contraction in new credit to the Treasury, and a larger rise in quasi-money; in addition, credit to the private sector (business enterprises, individuals, and non-monetary financial intermediaries) contracted in the 1964 first quarter compared with an increase a year earlier.

Of the BF 12.8 billion rise in the money supply in the second quarter, BF 4.6 billion was accounted for by private credit (up from BF 4.1 billion a year earlier) and another BF 2.0 billion by a drop in foreign exchange deposits. Claims on the central government again increased less than a year before, but still rose by BF 4.0 billion.

Credit expansion leads to new restrictive measures

The rise in bank credit in the second quarter was greater than the authorities wished to see, and prompted new restrictive steps in July.

On July 3, the National Bank of Belgium raised its basic rediscount rate from 4.25 to 4.75 per cent, and raised four of its other nine separate lending rates by either 1/4 or 1/2 of 1 per cent. This

Table 2. Belgium: Changes in Money Supply and Counterparts, 1963-64[1]
(in billions of Belgian francs; no sign = increase)

	1963 I	1963 II	1963 III	1963 IV	1964 I	1964 II
I. MONEY SUPPLY[2]	8.1	10.6[3]	-4.5	11.2	-4.7	12.8
(in per cent, unadjusted)	(3.2)	(4.0)[3]	(-1.7)	(4.2)	(-1.7)	(4.7)
(in per cent, seasonally adjusted)	(4.9)	(1.7)[4]	(0.2)	(2.5)	(--)	(2.6)
II. COUNTERPARTS	8.1	10.6[3]	-4.5	11.2	-4.7	12.8
A. Net foreign assets	3.3	0.6	-2.5	-1.5	-0.5	0.3
B. Claims on central government	10.8	4.7	-1.0	5.1	2.9	4.0
C. Claims on local authorities	-1.7	0.4	0.1	0.7	-0.9	1.2
D. Claims on business enterprises and individuals	1.6	4.2	3.2	8.9	-0.8	4.7
E. Claims on non-monetary financial intermediaries	0.2	-0.1	-0.1	0.9	-1.1	-0.1
F. Quasi-money (-=increase):						
1. Time and savings deposits with banks	-2.2	-0.6	-1.8	-1.9	-3.3	--
2. Foreign exchange deposits	--	-0.9	-0.2	-0.7	-1.0	2.0
G. Other (net)	-3.9	2.3	-2.2	-0.3	--	0.7

1/ Based on the consolidated balance sheets of the National Bank of Belgium, the commercial banks, and the Postal Checking Office, and in minor degree selected assets and liabilities of certain other institutions (e.g., Treasury currency, certain non-banks that accept demand deposits).

2/ Currency in circulation, demand deposits, and deposits up to one month.

3/ Based on an old series ending June, 1963.

4/ Based on a new and revised series beginning with June, 1963.

Source: National Bank of Belgium; International Monetary Fund for changes in seasonally adjusted money supply.

was the fourth time that the Bank had increased one or more of its lending rates in the space of 12 months, during which period the increases in the basic discount rate totalled 1-1/4 percentage points. At the same time, the Bank tightened its criteria of eligibility for rediscounts by refusing in the future to rediscount bills created more than one month after date of invoice.

These measures relating to rediscounts were accompanied by the imposition of a compulsory cash reserve requirement for the banks. In December 1961 the Banking Commission was empowered to introduce, upon proposal by the National Bank, a non-interest bearing cash reserve requirement up to the limits of (1) 20 per cent against liabilities at sight and up to one month, and (2) 7 per cent against savings deposits and other liabilities. This power was not used until July 3, 1964 when the Commission introduced a 1 per cent reserve requirement against all liabilities; the funds were deposited with the National Bank in two stages during August and totalled about BF 1.2 billion. The amount of the funds locked up by this action is rather small. However, since the requirement has finally been invoked and can be made much more severe, it was generally accepted that the psychological impact would be considerable.

The need for the July measures was directly related to an earlier failure of efforts to slow credit expansion by moral suasion. Bank credit to business rose 20 per cent in 1963. Last January, the National Bank requested the commercial banks to hold the increase in their loans in 1964 to 10 or 12 per cent; most reports say 10 per cent. Whether the banks actually agreed to such a limitation (as some commentators stated they did) is not known. In any event, a recent article in the National Bank's monthly bulletin states flatly that the National Bank's request was unsuccessful in slowing credit expansion, and that this fact was directly responsible for the restrictive moves made in July.

Treasury position improves

The problem of containing inflationary pressures in Belgium has been closely related to the state of the public finances. Last year, Treasury operations contributed heavily to monetary expansion, because an increased deficit was covered in its entirety by borrowing from the Belgian bank system and foreign lenders. This year, Treasury operations have still been expansionary, but on a much reduced scale. Because of concern over inflationary developments, the 1965 budget reportedly calls for a further contraction in Treasury borrowing requirements.

There have been two major improvements in the public finances in 1964. In the first place, the over-all net deficit (gross deficit less estimated debt redemption) of BF 5.3 billion was much smaller than the BF 14.9 billion deficit in the same months of 1963. (See Table 3.) Receipts have boomed with the expanding tax base, and net extrabudgetary expenditures have been cut back, and the rise in budgetary outlays has slowed.

Second, the composition of Treasury borrowing has altered radically. Much more has been raised through bond loans, the short-end medium-term debt in domestic currency has been reduced, and the further rise in the foreign exchange debt has been minor.[1/] (See Table 3.) The greater success in bond flotations this year has continued through

1/ Much of the debt in foreign currencies is in fact held by Belgian banks.

Table 3. Belgium: Treasury Operations, 1962-64
(In billions of Belgian francs;
1 billion BF = $20 million)

	Year 1962	Year 1963	Jan.-July 1963	Jan.-July 1964
I. Receipts and Expenditures (cash basis)				
A. Budgetary receipts	131.7	140.0	82.8	97.2
B. Budgetary expenditures 1/	147.9	163.4	99.0	109.8
Budgetary balance	-16.2	-23.4	-16.2	-12.6
C. Net extrabudgetary expenditures	-0.6	-6.9	-4.7	-0.3
Over-all gross deficit 1/	-16.7	-30.3	-20.9	-12.9
II. Debt Redemption (approximate) 2/	6.5	9.0	6.0	7.6
III. Over-all Net Deficit (I + II)	-10.2	-21.3	-14.9	-5.3
IV. Financing of Net Deficit	10.2	21.3	14.9	5.3
A. Miscellaneous financing 3/	-0.1	--	-0.3	2.1
B. Increase in debt outstanding 4/	10.3	21.3	15.2	3.2
1. In Belgian francs:				
a. Long-term	14.4	10.0	6.1	13.0
b. Short- & medium-term	5.8	1.8	2.5	-11.2
2. In foreign currencies:				
a. Long-term	0.7	-1.1	-0.6	-0.7
b. Short- & medium-term	-10.7	10.5	7.0	2.1

1/ Including debt redemption, not separately available.

2/ Estimated by comparing the deficit and miscellaneous financing with the change in the debt outstanding. The figures are not precise because the changes in the debt are at face values rather than market values. The estimates refer only to the Treasury's "direct debt." (See note 4.)

3/ Partly use of cash balances.

4/ At face values. Does not include the "indirect debt," which is incurred by parastatal organizations and redeemed by the Treasury, or debt to IMF.

Source: Ministry of Finance.

Table 4. Belgium: Treasury Bond Issues, 1962-64
(gross issues, i.e., before any conversions)

Year and month	Amount (BF millions)	Price	Maturity (years) 1/	Yield (per cent)
1962				
February	7,450	98.5	5, 10, 15, or 20	5.54
June	8,100	100.0	5, 10, 15, or 20	5.26
November	10,030	98.5	10, 15, or 20	5.06
Total	26,030			
1963				
March	5,900	100.0	10, 15, or 20	5.09
June	5,250	99.0	10, 15, or 20	5.72
October	3,232	98.5	10, 15, or 20	5.80
October	4,270	100.0	20	6.00
Total	18,652			
1964				
February	12,000	100.0	5 or 10	6.44
May	7,085	100.0	5-1/2 or 11-1/4	6.41
October	11,000	100.0	5 or 10	6.44
Total	30,085			

1/ Holders may redeem bonds after the number of years specified.

Source: National Bank of Belgium.

October, and has accompanied two modifications in the terms offered. Maturities have been shortened, and yields have been raised. The range of yields in 1964 has been between 6.41 and 6.44 per cent, compared with 5.09 to 6.00 per cent last year. (See Table 4.)

As a result of these two improvements, the inflationary impact of Treasury operations has been markedly lessened. Treasury recourse to bank credit came to BF 6.9 billion in the first half of 1964, down from BF 15.5 billion in January-June 1963. On foreign transactions, central government capital flows were in balance in January-June compared with a BF 2.9 billion net inflow a year before.

In the past, budget expenditures and budget deficits have consistently turned out to be appreciably higher than initially estimated. But the results for the full year 1964 should be much more favorable than those for 1963 on the basis of the results so far and in view of official concern over the need to compress the deficit. According to press reports, the Finance Minister expects that the net financing requirement will in fact be much reduced this year. The budget estimates for 1965 presented to Parliament reportedly show still a further contraction in the net borrowing needs because of another cut in the rate of expenditure increase.

Rise in interest rates slows down

Since their further sharp rise in the first quarter, Belgian interest rates have again moved up but at a perceptibly slower pace. The reduction in the Treasury's borrowing requirements this year has eased some of the pressure in credit markets. In addition, there was a substantial net capital inflow in the first half of the year, and an apparent further importation of funds since mid-year.

Table 5. Belgium: Interest Rates, 1962-64
(end of month)

	1962 Dec.	1963 Sept.	1964 March	1964 July	1964 Sept.	1964 Oct.
I. Treasury Certificates						
3-month (tap rate)	3.00	3.45	4.25	4.50	4.50	4.50
4-month (auction rate)	3.30	3.85	4.75	5.00	5.00	5.10 1/
6-month (auction rate)	3.35	3.90	4.90	5.00	5.15	5.15
9-month (auction rate)	3.40	3.95	5.00	5.00	5.30	5.30
12-month (auction rate)	3.45	4.04	5.05	5.20	5.40	5.40
II. Bonds (5 to 20 years to maturity)						
Government	4.96	5.12	5.50	5.62	5.68	n.a.
Municipalities and parastatal organizations	5.02	5.01	5.47	5.53	5.56	n.a.

1/ November 3.

Source: National Bank of Belgium.

In the market for short-term funds, the auction rate on 4-month certificates of the Treasury and the Securities Stabilization Fund (the most important money market rate) moved up another 25 basis points between end-March and end-July. (See Table 5.) There were no changes after the July 28 auction until a rise to 5.10 per cent occurred on November 4. The tap rate on 3-month Treasury certificates, set by the National Bank of Belgium in the light of market conditions, has been unchanged at 4.50 per cent since late July. However, rates on 9- and 12-month Treasury certificates, sold at monthly auctions, have moved up another 20 to 30 basis points since July.

In the bond market, yields have continued to rise quite steadily, but the advance since last February has been at a reduced rate compared with the sharp increases of the previous six months. From the end of February to the end of September, yields on government bonds maturing in 5 to 20 years rose 17 basis points and yields on bonds of similar maturity issued by cities and parastatal institutions moved up another 12 basis points.

Trade deficit is enlarged

Belgium's foreign trade has witnessed further rapid expansion, but the deficit has widened considerably in recent months.

The exceptionally rapid rise in imports that began in early 1963 continued at about the same rate in 1964. Quarter-to-quarter increases (seasonally adjusted) came to 7.6 per cent in the first quarter and 6.0 per cent in the second. (See Table 6.) Exports, which kept pace with imports during approximately the first three quarters of 1963, have not done so since that time. In the second quarter, they

Table 6. Belgium-Luxembourg: Seasonally-Adjusted Foreign Trade, 1962-64
(In millions of dollars; monthly average or month)

		Imports c.i.f.	Exports	Balance
Quarters				
1962 -	I	358	361	+3
	II	378	356	-22
	III	370	366	-4
	IV	390	369	-21
1963 -	I	374	363	-10
	II	407	405	-13
	III	421	426	+6
	IV	437	425	-12
1964 -	I	470	456	-14
	II	498	452	-46
Months-1964				
	April	498	445	-53
	May	489	445	-43
	June	506	464	-41
	July	501	451	-50
	August	n.a.	455	n.a.

Source: OECD

were 6.4 per cent higher than 6 months earlier (while imports were rising 14 per cent), and in July-August they continued at the second quarter rate. (The rise in exports has been very irregular, and an exceptional bulge in February-March distorts the quarter-to-quarter movements.) The deficit has thus widened from a monthly average of $12 million in the fourth quarter of last year to $46 million in the second quarter of this year.

Balance of payments improves in first half of 1964

The balance of payments of Belgium and Luxembourg shifted from an $82 million deficit in the last half of 1963 to a $12 million surplus in the first half of 1964, in spite of a widened trade deficit. (See Table 7.) However, the small surplus in January-June compares with a much larger surplus of $78 million a year earlier, the difference being entirely due to the faster rise in imports relative to exports.

Four factors caused the shift from the second half of last year. In addition to improvements in services (probably seasonal) and errors and omissions, there was a very large increase in the net foreign borrowings of public sector entities (local authorities and state-owned financial and commercial enterprises), which reached $86 million in January-June of this year. Furthermore, there was an absence of any net capital flows on central government account (despite a $36 million rise in the Treasury's foreign currency debt) compared with an outflow of $18 million in the last half of 1963 (again, notwithstanding a $64 million increase in the foreign currency debt). The striking lack of correlation between government capital

Table 7. Belgium-Luxembourg: Balance of Payments, 1961-64
(in millions of dollars)

	1961 First half	1961 Second half	1962 First half	1962 Second half	1963 First half	1963 Second half	1964 First half
I. Current Account	-40	80	68	28	6	-88	-64
A. Imports 1/	n.a.	n.a.	1,844	1,906	1,976	2,218	2,374
B. Exports	n.a.	n.a.	1,786	1,836	1,922	2,106	2,234
Trade balance	-100	-22	-58	-70	-54	-112	-140
C. Services	54	86	114	86	58	30	70
D. Transfers	6	16	12	12	2	-6	6
II. Capital Movements	-114	60	-12	-32	44	22	66
A. Central government	-124	8	-26	-30	58	-18	--
B. Other public	12	32	--	-8	10	4	86
C. Private	-2	20	14	6	-24	36	-20
III. Errors and Omissions	--	22	26	2	28	-16	10
IV. Over-all Balance (I + II + III)	-152	164	82	-2	78	-82	12
Monetary Movements (-=increase in net foreign assets)	152	-164	-82	2	-78	82	-12
National Bank of Belgium:							
Official reserves	-50	-185	54	-19	-141	-39	13
Other (net)	8	-17	8	-9	-9	-33	-33
Commercial banks and others (net)	194	38	-144	30	74	154	8

1/ Partly c.i.f. and partly f.o.b.

Source: National Bank of Belgium.

movements and the change in the foreign currency debt is caused mainly by the fact that much of this debt is placed with Belgian banks rather than with foreign institutions. Last year, when the foreign currency debt rose a total of $188 million, Belgian banks increased their holdings by $98 million.

Official reserves rise rapidly in July-November

Modest gains in official reserves in the first half of 1964 have been followed by sharp increases in more recent months totalling $170 million, of which most accrued in October-November. These gains are probably related to capital flows caused by tighter credit conditions in Belgium.

In the January-June period there was a $10 million rise in official reserves after adjustment for a $23 million rise in Belgium's IMF position (related to Italy's Fund drawing last March). Since June, official reserves have risen $6 million in July, $21 million in August, $19 million in September, and $125 million from September 30 to November 16. It appears highly unlikely that these increases are related to any dramatic improvement in current account transactions. Because they have taken place since restrictive monetary measures were imposed on Belgian banks in July-August, it seems plausible to ascribe them to capital inflows.

A small part of the rise since August is the result of renewed medium-term foreign borrowing by the Belgian government, which in August obtained a $16.5 million 35-month loan from the Morgan Guaranty Trust Company at 5-1/4 per cent. The funds are to be used to meet payments on Congo bonds guaranteed by the Belgian government.

Because of this inflow of foreign exchange, the Belgian franc has strengthened in foreign exchange markets. The franc was quoted at a little more than 0.2 per cent above par in late June. It rose almost continuously in July-September and since end-September has been at its upper limit against the dollar (0.75 per cent above par).