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Recent Economist Developments in Belgium:
Annual Review

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Recent Economic Developments in Belgium: Annual Review

The past year has been rather unsatisfactory in Belgium from two important standpoints: industrial production decreased during the year in reflection of a weakening pace of aggregate demand, but hourly earnings and unit labor costs kept on increasing very fast. In 1966 there was little slackening of the rise in consumer prices, although wholesale prices ended the year about where they began. Despite the disappearance of excess demand, monetary policy remained restrictive until early in 1967, while in the fiscal area the 1967 budget estimates reflect preoccupation with structural problems rather than the current state of business.

Flagging export demand has helped to shift the external accounts from surplus to deficit, but this should give no cause for alarm because of Belgium's high reserves.

During 1966, aggregate demand seems to have leveled out (or undergone a slight decline), to judge by the movements within the year of industrial production, prices, and foreign trade, and an involuntary build-up of stocks of finished goods. Industrial production (inclusive of construction), corrected for accidental as well as seasonal variations, dropped 4.4 per cent from the first quarter to October 1966, and was probably about unchanged through the rest of the year. (See Table 1.) A major reason for the current pause in growth is to be found in the export sector, which is of particular importance in Belgium where almost 40 per cent of industrial production is sold abroad. After many

Table 1. Belgium: Selected Economic Indicators, 1965-1967

Quarterly	Industrial ^{1/} Production (1958=100)	Hourly ^{2/} Earnings (1960=100)	Consumer Prices (1960=100)	Interest Rates:		Foreign Trade: ^{5/}		Official ^{6/} Reserves (\$ millions)	
				4-Mo. Bills	Gov't ^{4/} Bonds	Imports c.i.f.	Exports Balance		
1965 - I	151.7	143	111.6	5.12	5.58	486	511	25	2,210
II	150.0	147	112.9	4.96	5.54	524	509	-15	2,264
III	150.3	149	114.1	5.07	5.58	534	539	5	2,327
IV	157.0	151	115.0	5.00	5.65	565	570	5	2,304
1966 - I	159.0	154	116.5	5.07	5.67	544	539	- 5	2,279
II	152.3	162	118.7	5.28	5.74	576	566	-10	2,294
III	150.7	163	118.3	5.76	5.83	607	563	-44	2,294
IV	n.a.	167	119.1	5.99	5.93	n.a.	590	n.a.	2,320
Monthly									
1966 - September	151.0	163	118.6	5.77	5.84	611	586	-25	2,294
October	152.0	--	118.9	5.85	5.94	593	550	-43	2,329
November	n.a.	--	119.0	5.99	5.96	602	586	-16	2,322
December	n.a.	167	119.3	6.12	5.90	n.a.	635	n.a.	2,320
1967 - January	n.a.	n.a.	119.5	6.12 ^{7/}	5.85	n.a.	n.a.	n.a.	2,337
February	n.a.	n.a.	n.a.	6.00 ^{7/}	5.88	n.a.	n.a.	n.a.	2,310

^{1/} Adjusted for seasonal and accidental variations, and inclusive of construction. This is the "trend-cycle" index of the National Institute of Statistics.

^{2/} In mining, manufacturing, and transportation.

^{3/} Monthly average auction rates for Fonds des Rentes certificates.

^{4/} Beginning-of-month yields on Treasury bonds of 5-20 years maturity.

^{5/} Seasonally-adjusted monthly average or monthly values.

^{6/} End-of-period. Includes only gold, foreign exchange, and IMF position.

^{7/} Through February 21.

years of high expansion rates, exports advanced only 3-1/2 per cent in the 12 months up to the fourth quarter of 1966, in reflection of weakened demand in Germany, Britain, and elsewhere.

Private domestic spending seems to have been a bit lower at the end of 1966 than it was a year earlier. For the year 1966 as a whole, the annual totals of over-all production and spending (in real terms) will show some small gains when compared with 1965 annual totals. Late last year, the EEC estimated that in 1966 private consumption would be 3 per cent above 1965 and that gross fixed investment would rise 4 per cent (in real terms). These estimates seem consistent with known or probable increases in production and trade in 1966. In terms of annual totals, industrial production last year was about 2 per cent more than in 1965. (Even though it declined during 1966, it began 1966 at a level that was higher than 1965.) Exports last year exceeded the 1965 total by 6 per cent. However, imports showed a comparatively large increase of around 11 per cent. Monthly surveys of the business situation indicate that during 1966 there was a build-up of inventories of finished goods, as well as a declining trend of new orders. Neither of these indicators showed any signs of improvement at the year-end.

Real GNP for the full year 1966 probably rose no more than 3-1/2 per cent; some estimates are lower than that. In contrast, in the boom years 1960-64 Belgian GNP increased an average of 5.4 per cent a year, in real terms. The rise slowed to 3.3 per cent in 1965.

Retail prices in the fourth quarter of 1966 were up 3.5 per cent from a year earlier, a rise that was not much smaller than the one that occurred during 1965. Wholesale prices showed almost no net change from December 1965 to December 1966, although in the interim they rose substantially, and fell back, in response to changes in the prices of imported materials. Last year saw another big increase in labor costs despite the slowing of demand for goods and services. The labor market remained tight. Hourly earnings of blue-collar workers in mining, manufacturing and transportation in 1966 averaged 9.9 per cent above 1965, following a gain of 9.7 per cent in 1965 relative to 1964. Considering that industrial production for the year rose only 2.8 per cent in 1965 and about 2 per cent in 1966, that employment was stable, and that the work week probably did not change significantly, unit labor costs would seem to have risen on the order of 6-1/2 per cent in 1965 and 8 per cent in 1966. One result of the higher unit labor costs has been to intensify the profit squeeze of recent years. According to the Belgian national accounts, corporate profits increased a total of only 14 per cent from 1961 to 1965 compared with increases of around 40 per cent in national income and industrial value added (at current prices).

Belgian financial policies have been cautious, even though excess demand has disappeared from the economy. From the cyclical standpoint, a more stimulative fiscal policy would seem to be called for, but the 1966 and 1967 budgets have instead given first priority to attempts to rectify long-standing structural defects in the Belgian public finances.

The Belgian budget has not been a generator of public saving, and capital outlays have had to be financed entirely by borrowing. In some recent years, the government has in fact been a dis-saver, using borrowed funds to finance part of its current expenditures. In 1965 and 1966, expenditure authorizations rose swiftly (32 per cent in two years), and for 1965 there was a very big increase in the deficit on current operations. To prevent the deficit from widening further, tax rates were increased in 1966. On a cash basis, budget operations in the first nine months of 1966 showed nearly an unchanged deficit from a year earlier. However, fiscal policy was in fact more restrictive in 1966. The deficit was constant despite the near-stagnation of the tax base during the year, and it would have shrunk if economic activity had risen in accordance with the economy's productive capacity.

The 1967 budget estimates call for elimination of the deficit on current operations. For this purpose, the expenditures rise has been slowed down; in addition, Parliament is now being asked to raise certain excise and retail sales tax rates and to raise personal income tax rates in the higher brackets. The original budget bill drawn up last fall did not call for tax increases, but later it was estimated that the tax base would expand less in 1967 than initially projected, and this would lead to a revenue shortfall below expectations unless tax action were taken.

Contrary to the usual pattern, the slowed pace of demand in Belgian markets for goods and services last year was accompanied by a tightening of conditions in the financial markets. As also occurred

in France during the 1964-65 stabilization period, the demand for bank credit remained strong. But a shift in the balance of payments from surplus (in 1965) to deficit (in 1966) slowed down the money supply expansion and put bank liquidity under pressure. With interest rates rising from the spring through the end of the year, the yield on 4-month Fonds des Rentes certificates climbed more than a full percentage point to 6.15 per cent by late December, while long-term bond yields advanced around 25 basis points to peak levels in the fourth quarter.

The two principal measures taken in the monetary area were of a restrictive nature. In April 1966 the National Bank of Belgium requested the banks to limit the increase in their credits during 1966, a request that was later extended through June 1967. It does not appear that the banks had to slow down their rate of credit expansion very sharply to stay within the limits, which seem liberal (allowing credit to rise more than 12 per cent a year). The National Bank itself has called this step a precautionary move, to forestall any possible reappearance of excess demand. The other credit-tightening action was a rise in the discount rate on June 2, from 4-3/4 to 5-1/4 per cent, a move the Bank called a "validation" of tightening credit markets. Rates charged by banks on customer loans went up accordingly. The Bank's annual report for 1966 asserts that an attempt to prevent market rates of interest from rising would have risked not only a renewal of inflationary pressures but also an aggravation of the balance of payments deficit.

During the first quarter of 1967, Belgian interest rates declined. With credit conditions easing in many countries after the fall of 1966, the National Bank reduced the discount rate, by 1/4 of 1 per cent each time, on February 2 and March 23.

Belgium's external accounts shifted from a surplus of \$146 million in 1965 to a deficit in 1966 that can be tentatively placed at \$84 million. All of this shift, and more, was the result of a trade account deterioration. Exports increased very little during 1966. But, as was noted earlier, imports were up substantially, in all commodity groups; in particular, imports of materials and of equipment increased strongly despite declining industrial production and the somber near-term outlook for the economy. All of the 1966 balance of payments deficit was financed by a rise in the commercial banks' net foreign liabilities. National Bank of Belgium foreign assets rose \$34 million last year. The Bank's principal foreign assets--gold, foreign exchange, and IMF position--increased a further \$29 million in the first 2-1/2 months of 1967, and totaled \$2,349 million on March 13 of this year.