

# Foreign financial transactions of Belgian non-financial sectors

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## Introduction

Belgium is a small, open economy which not only exports and imports goods and services on a substantial scale, but also records significant financial flows in relation to other countries. Yet recent analyses have rarely addressed the financial transactions of resident sectors with the rest of the world. However, in the past few years, and more specifically since the introduction of the euro, these transactions have profoundly altered the structure of the financial wealth of Belgian sectors. The purpose of this article is to examine the foreign assets held and foreign liabilities contracted by Belgian non-financial sectors, and describe how they have changed over time. It therefore provides some information on the way in which these sectors have participated in the international financial integration.

First, the article analyses Belgium's net external position, and how it has changed in the past ten years, thus identifying price effects in the developments observed.

The rest of the article details the transactions of households, non-financial corporations and Belgian general government with the rest of the world. It examines the movement in the market share of the rest of the world in the assets and liabilities of these sectors, and the instruments and transactions underlying those movements.

## 1. Belgium's net external position

### 1.1 Situation at the end of 2007

Defined as the difference between the assets and liabilities of resident sectors vis-à-vis the rest of the world, Belgium's net external position is decidedly positive. At the end of 2007, it stood at 147.1 billion euro, thanks to the net external position of households and financial corporations, as at that time their financial balances vis-à-vis the rest of the world came to 146.8 and 243.9 billion euro respectively. Conversely, at the end of 2007, non-financial corporations and general government recorded net financial liabilities of 91.3 and 152.3 billion euro respectively in relation to other countries.

### 1.2 Movement over the past ten years

In the past ten years, Belgium's net external position has grown, rising from 84.1 billion euro at the end of 1997 to 147.1 billion euro, representing 38 and 44.4 p.c. of GDP respectively.

At the end of 1997, this position was attributable solely to the positive financial balance of households in relation to other countries, totalling 179.8 billion euro. The other economic sectors recorded a negative net external position of 28.5 billion for non-financial corporations, 60.2 billion for general government and 7.1 billion for financial corporations.

**TABLE 1** BELGIUM'S NET EXTERNAL POSITION: SITUATION AT THE END OF 1997 AND AT THE END OF 2007  
(billions of euro, unless otherwise stated)

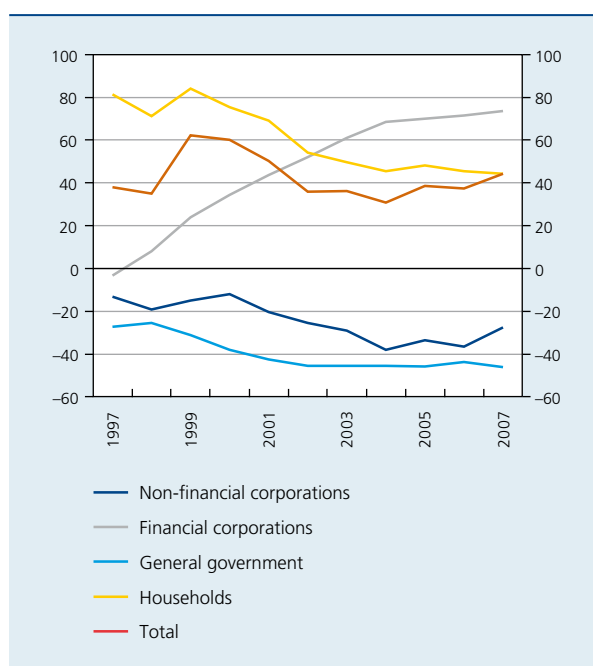
	Assets		Liabilities		Balance		Balance as p.c. of GDP	
	1997	2007	1997	2007	1997	2007	1997	2007
Households .....	179.8	146.8	-	-	179.8	146.8	81.3	44.3
Non-financial corporations .....	101.5	444.7	130.0	536.0	-28.5	-91.3	-12.9	-27.5
General government .....	1.2	3.1	61.4	155.4	-60.2	-152.3	-27.2	-45.9
Financial corporations .....	304.0	1,087.1	311.1	843.2	-7.1	243.9	-3.2	73.6
<b>Total .....</b>	<b>586.5</b>	<b>1,681.7</b>	<b>502.5</b>	<b>1,534.6</b>	<b>84.1</b>	<b>147.1</b>	<b>38.0</b>	<b>44.4</b>

Source : NBB.

There were notable changes between 1997 and 2007. The main one concerned financial corporations which, in the space of ten years, moved from a slightly negative net external position in 1997 to a very positive net external position. If credit institutions are considered on their own, it is evident that this change occurred over a smaller number of years, broadly speaking from 1999 to 2004.

Various factors contributed to this development. First, the steadily advancing internationalisation of the financial institutions played an active part. In recent years, Belgian credit institutions have progressively expanded their foreign activities owing to the limited scope for growth on the domestic market. That international expansion had already taken the form of the establishment of binational groups in the 1990s, with credit institutions from neighbouring countries, and more recently led to acquisitions in Central and Eastern Europe and in Turkey. Moreover, following the changeover to the euro, the Treasury increased the diversification of investments in government securities. Belgian financial institutions also diversified their portfolio of securities and replaced Belgian government paper with foreign instruments.

**CHART 1** MOVEMENT IN THE NET EXTERNAL POSITION OF THE BELGIAN SECTORS  
(percentages of GDP)



Source : NBB.

All these changes explain the considerable increase in both the financial assets and the financial liabilities of Belgian credit institutions vis-à-vis the rest of the world. While their gross financial assets came to 249.3 billion euro at the end of 1997, they totalled 786.7 billion at the end of 2007. Similarly, their gross financial liabilities increased from 284.5 billion euro at the end of 1997 to 677 billion at the end of 2007.

The growth of the banks' foreign liabilities was outstripped by the increase in their assets, a primary factor being the profound change which has taken place in recent years in Belgium's special financial relationships with Luxembourg and the Netherlands. The substantial investments by Belgian residents in Luxembourg and the Netherlands brought the banks in those countries an inflow of Belgian francs which they used to grant interbank loans to Belgian banks.<sup>(1)</sup>

(1) The Luxembourg banks were also able to use these funds to subscribe directly to Belgian Treasury certificates.

The changeover to the euro, and particularly the implementation of the European savings tax directive (see section 2.1) curbed that practice and therefore reduced the external debts of the Belgian financial sector.

It must also be said that, over the years, both investments and liabilities in relation to the rest of the world have steadily expanded for all the various Belgian sectors, except for households. While the latter's net external position at the end of 1997 represented 81.3 p.c. of GDP, it was down to 44.3 p.c. of GDP at the end of 2007. Conversely, the net financial liabilities of non-financial corporations vis-à-vis the rest of the world came to 12.9 p.c. of GDP at the end of 1997, compared to 27.5 p.c. of GDP ten years later. The government also focused more on other countries: at the end of 1997, its net financial liabilities equalled 27.2 p.c. of GDP, against 45.9 p.c. at the end of 2007. As already mentioned, the biggest change concerned the situation of financial corporations: while their net financial liabilities came to 3.2 p.c. of GDP at the end of 1997, by the end of 2007 Belgian financial corporations held net financial assets in relation to the rest of the world worth the equivalent of 73.6 p.c. of GDP.

### 1.3 Financial transactions and price effects

The financial accounts record the outstanding amount of the financial wealth at the end of a period and the flows of financial assets and liabilities (or the financial transactions, according to the ESA 95) during a period. However, the change in the stock of financial assets and liabilities between one year and the next does not correspond to the flows recorded between those dates. The total figure for equities as recorded in the financial accounts is calculated at the end of each year at market prices<sup>(1)</sup>

(i.e. on the basis of the values recorded at the end of each period). Apart from the recorded volume of transactions, it includes changes in the valuation of assets and liabilities occurring during the year. Those changes may be due to revaluation of the assets or to exchange rate fluctuations. The changes in the outstanding amounts also include other volume changes (e.g. sectoral reclassifications, shifts between financial instruments or exceptional events).

To analyse the financial position of the various economic sectors it is necessary to be able to separate the price effects from the volume of transactions when observing financial movements. Depending on their size, fluctuations in financial prices in either direction will often have a significant impact on the outstanding amount of the financial portfolio of Belgian sectors.

To estimate the effect of revaluations over the past ten years, it is necessary to reconstruct, on the basis of the outstanding total at the end of 1997, a theoretical total which takes account only of the amounts invested each year (in other words, the cumulative flows from 1998 to 2007, or the effect due exclusively to transactions). Comparison of the respective changes in the theoretical and recorded totals provides an estimate of the size of the fluctuations in financial prices (i.e. the price effect) in the movement in the recorded outstanding total.

If the change in the total is smaller (greater) than the cumulative flows, that implies that the total at the end of the period has been driven down (up) by a negative

(1) Other instruments (fixed-income securities, loans) are recorded at their acquisition cost. However, they may be subject to price changes via exchange rate fluctuations.

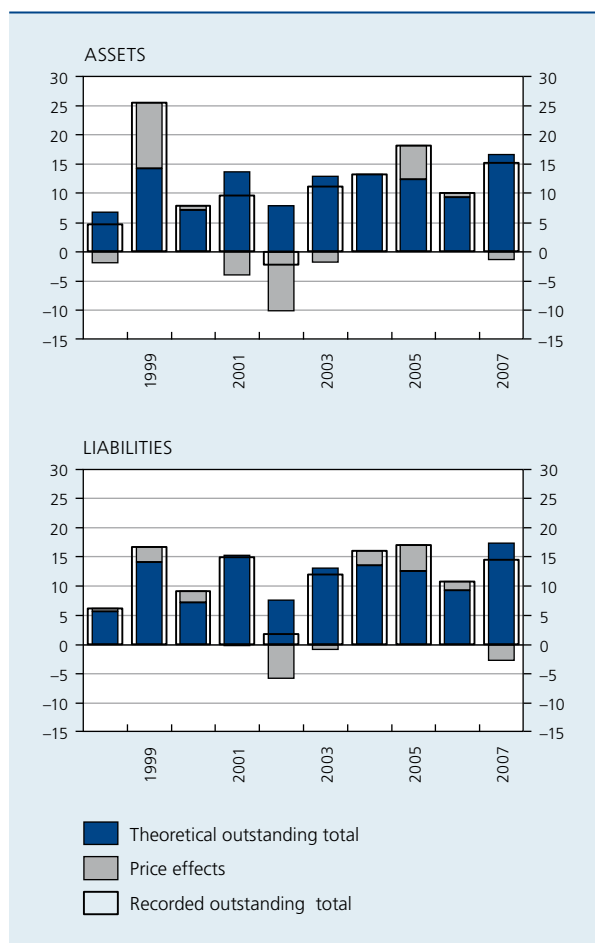
**TABLE 2** CHANGES IN OUTSTANDING AMOUNTS BETWEEN THE END OF 1997 AND THE END OF 2007,  
BROKEN DOWN INTO PRICE EFFECTS AND FINANCIAL TRANSACTIONS  
(billions of euro)

	Assets		Liabilities	
	Financial transactions	Price effects	Financial transactions	Price effects
Households .....	-6.0	-27.0	-	-
Non-financial corporations .....	331.4	11.8	358.3	47.7
General government .....	2.6	-0.7	83.3	10.7
Financial corporations .....	793.1	-10.0	567.8	-35.7
<b>Total</b> .....	<b>1,121.1</b>	<b>-25.9</b>	<b>1,009.4</b>	<b>22.8</b>

Source: NBB.

**CHART 2** IMPORTANCE OF PRICE EFFECTS AND FINANCIAL TRANSACTIONS IN THE CHANGES OF OUTSTANDING TOTALS DURING THE PAST DECADE

(annual percentage change)



Source : NBB.

(positive) price effect. For the assets, these revaluations are put at -25.9 billion euro over the past ten years, for the Belgian economic sectors as a whole. For the liabilities, the figure is 22.8 billion euro.

The sectors facing significant negative price effects are households, in asset formation, and financial corporations, in the formation of assets and liabilities. That probably reflects the fact that households are attracted by high-yield assets, particularly those denominated in foreign currencies, but with risks (e.g. the exchange rate risk) that may prove considerable if the euro appreciates, as has happened in the past few years. The various

(1) In 1998, a new data collection system was set up for the financial accounts, which affected in particular the recording of changes in volume other than flows. The entry into force of this new system causes a break in the data series.

episodes of financial turbulence at the end of the period considered seem to have affected the foreign transactions of financial corporations (drop in their share prices and in the US dollar exchange rate).

Chart 2 illustrates the importance of price effects on the changes in the outstanding totals during the past decade. In 1999<sup>(1)</sup> the price effects were positive, reflecting the stock market boom. These price effects diminished in 2000 following the bursting of the technology bubble and the stock market crash, thus driving down the recorded outstanding total. Between 2001 and 2003 they became negative. In 2002, at the bottom of the cycle, financial asset prices fell by 10.2 p.c., causing a 2.3 p.c. decline in the recorded outstanding total, despite positive financial flows. During that same year, financial liability prices also dropped by 5.8 p.c., tempering the expansion in flows by a corresponding amount.

Between 2004 and 2006, the increase in the recorded outstanding total of the financial assets is due both to the expansion of the flows and the price recovery. The same applies to the growth of the financial liabilities over the same period.

In 2007, while the volume of transactions increased fairly strongly, the price effects were again negative for both assets and liabilities, probably owing to the various episodes of financial market turbulence.

## 2. Financial transactions vis-à-vis the rest of the world

### 2.1 Households

#### 2.1.1 Foreign financial liabilities

Owing to the absence of information, the financial accounts do not record the foreign financial liabilities of Belgian households. In all probability, they are negligible, reflecting the current segmentation of the household credit market at European level. Conversely, Belgian households have long been in the habit of acquiring financial assets from foreign counterparties. The next section is devoted to analysis of these financial instruments held in other countries.

#### 2.1.2 Foreign financial assets

This section looks at recent developments concerning foreign financial assets held by Belgian households, in the light of the many events which may have influenced

saving patterns over the past ten years: introduction of the euro, creation of Euronext, the one-off regulation securing release from tax liability, the European savings tax directive, etc.

### 2.1.2.1 Comments on methodology

According to the methodology of the financial accounts, the foreign character of an asset is determined exclusively by the debtor's country of residence: neither the currency in which it is denominated nor the place where it is held is taken into account. For example, a dollar deposit on an account held with a Belgian bank will be regarded as a domestic asset, while American bonds or shares held on a securities account with the same bank will be recorded as foreign assets. This method causes a problem in the case of undertakings for collective investment (UCIs): units in Belgian UCIs are recorded as domestic assets even if those UCIs hold a portfolio of foreign securities; conversely, units in foreign UCIs held by Belgian residents are classed as foreign assets even if the portfolio consists of Belgian securities. This rule will therefore be disregarded for the purpose of the analysis: investments by households in units of Belgian or foreign UCIs investing in foreign securities will be regarded as foreign assets, and investments in units in Belgian or foreign UCIs investing in Belgian securities will be regarded as domestic assets.<sup>(1)</sup>

In general, the figures relating to household assets in other countries have to be interpreted with caution, as the Belgian financial accounts usually estimate the assets of households as a residual figure, which implies that any error in the recording of financial assets of other sectors inevitably affects the household data. Moreover, the figures for the outstanding totals are mostly based on the cumulative flows in the balance of payments, which are then revalued on the basis of various assumptions. Consequently, portfolio switches between assets held abroad (e.g. the acquisition of foreign shares financed via a sight deposit with a foreign bank) go unrecorded, and that probably introduces some distortion in the analysis of the breakdown by instruments of claims on other countries.

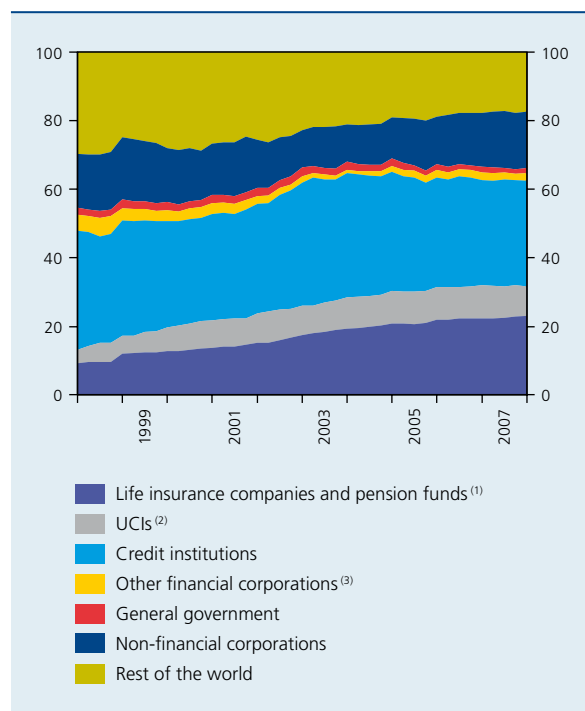
### 2.1.2.2 Overall movement in the holding of foreign assets

At the end of 2007, foreign claims represented 17 p.c. of the financial portfolio of Belgian households. The rest of the world is thus the third largest channel for

investment by individual investors, coming behind two domestic subsectors: credit institutions (31 p.c. of assets) and life insurance companies and pension funds (23 p.c.). Disintermediated investments in equities and bonds issued by non-financial corporations came to 16 p.c. on 31 December 2007, and units in Belgian UCIs stood at 9 p.c. Finally, the liabilities of general government and entities in the "other financial corporations" category represented only a minor direct counterpart to the financial assets of households at the end of 2007.

Although still substantial, the share of external assets has declined very sharply in the past ten years: at the end of 1997, claims on the rest of the world still represented 30 p.c. of the household portfolio. In the space of ten years, the proportion of foreign assets has therefore fallen by over 10 percentage points. That decline is also perceptible in the absolute value: as stated in section 1.2, the total stock of foreign financial assets held by households was down from 179.8 billion euro at the end of 1997 to 146.8 billion at the end of 2007.

**CHART 3** FINANCIAL ASSETS OF HOUSEHOLDS:  
BREAKDOWN BY COUNTERPARTY SECTOR  
(end-of-quarter data, percentages of the outstanding total)



Source: NBB.

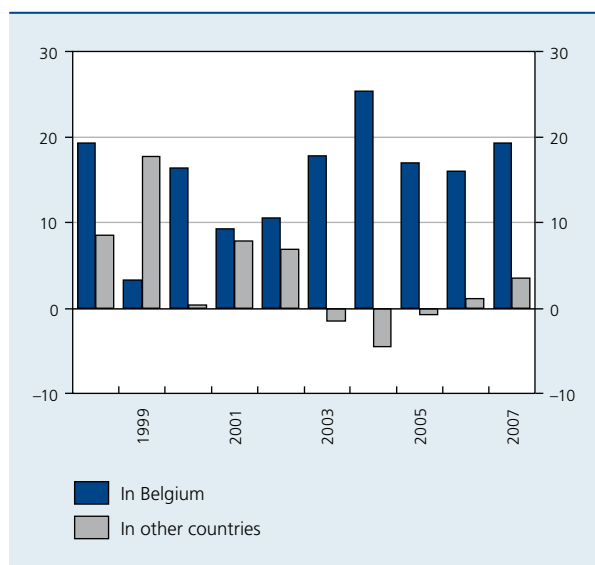
(1) Including pension savings funds.

(2) Excluding pension savings funds.

(3) This category comprises the NBB, financial auxiliaries, the "non-life" branches of insurance companies, and financial intermediaries not included under other headings.

(1) This adjustment is made only in the subsequent analysis of the financial transactions. To maintain consistency with the financial accounts in general, and with section 1 of this article in particular, the figures for the outstanding totals are not adjusted.

**CHART 4** FORMATION OF FINANCIAL ASSETS BY HOUSEHOLDS  
(flows, billions of euro)



Source : NBB.

In the past ten years, the financial transactions of Belgian households with other countries can be divided into two phases:

- up to 1999, the amount of Belgians' capital exports was similar to the amount of financial assets constituted in Belgium;
- since the year 2000, foreign investment flows have been systematically – and often very considerably – smaller than the formation of domestic assets.

### 2.1.2.3 Movement per asset category

However, this overall picture conceals changes which were diametrically opposed, depending on the asset category considered. Thus, the weight of the total stock of interest-bearing assets (deposits, fixed-income securities and monetary or bond UCIs), which represented around 70 p.c. of the foreign portfolio of households in 1997, has since halved. Conversely, equities and units in equity UCIs, which ten years ago represented only 12 p.c. of foreign assets, now form the dominant category in the foreign portfolio of households (42 p.c.). Finally, technical insurance reserves, which were still negligible in 1997, now account for 13 p.c. of the foreign financial assets of Belgian households.

To identify the factors determining these changes, the following paragraphs endeavour to give a year-by-year breakdown of the flows of financial transactions between Belgian households and the rest of the world according to the type of financial instrument used. The analysis thus compares successively the formation of interest-bearing assets, equities and units in equity UCIs, and technical insurance reserves in Belgium and in other countries.

#### a) Interest-bearing assets

Examination of the movement in the interest-bearing assets of Belgian households reveals that the formation of foreign financial assets slowed sharply from 1998 and that it rapidly lost its predominance over the formation of domestic interest-bearing assets. In 2001, for the first time, Belgian households showed a very marked preference for domestic investments in their portfolio of

**TABLE 3** FOREIGN FINANCIAL ASSETS OF HOUSEHOLDS: BREAKDOWN BY INSTRUMENT  
(end-of-period outstanding totals)

	1997			2007		
	billions of euro	p.c. of the total	p.c. of GDP	billions of euro	p.c. of the total	p.c. of GDP
Interest-bearing assets	126.8	70.5	57.4	49.3	33.6	14.9
Equities and units in equity UCIs	22.2	12.3	10.0	61.6	42.0	18.6
Technical insurance reserves	2.7	1.5	1.2	19.1	13.0	5.8
Other <sup>(1)</sup>	28.1	15.6	12.7	16.8	11.4	5.1
<b>Total</b>	<b>179.8</b>	<b>100.0</b>	<b>81.3</b>	<b>146.8</b>	<b>100.0</b>	<b>44.3</b>

Sources: NAI, NBB.

(1) This item consists mainly of errors and omissions, as well as units in UCIs not included in other categories in the table and cash.

interest-bearing assets. From 2002 to 2006, households repatriated this type of capital each year, exchanging their foreign interest-bearing assets for Belgian assets of the same type, as is evident from the symmetry of the chart showing flows of funds. These opposing movements in foreign and domestic interest-bearing investments probably reflect the anticipation of the European savings tax directive, which thus influenced the saving habits of Belgian households even before it actually came into force on 1 July 2005. In 2007, flows of investments in foreign interest-bearing assets became positive again.

In this comparison, the interest-bearing assets comprise deposits, fixed-income securities and units in monetary UCIs or UCIs investing mainly in bonds. These categories of instruments were not put together at random, as they constitute an approximation of the interest-bearing assets governed by the European savings tax directive.<sup>(1)</sup> Since political agreement had already been reached in 2000 on the main points of the directive, many households were able to adjust their portfolio of financial assets in advance, despite the uncertainty over the date of entry into force of the directive. The one-off tax regulation may also have encouraged some households to adjust their assets before the directive was actually implemented.

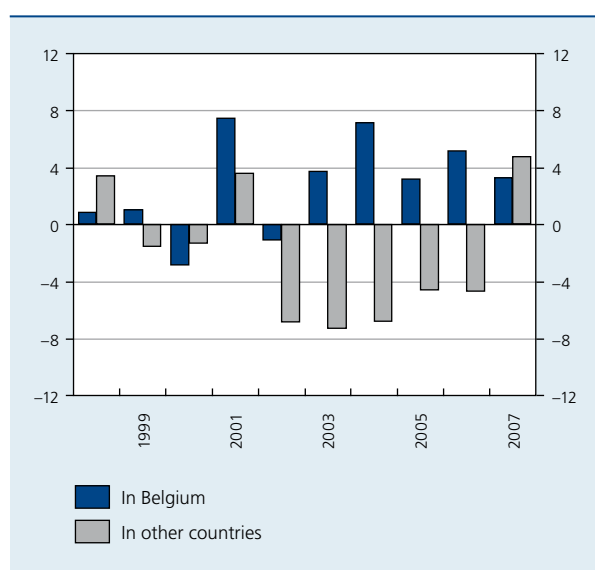
However, it is difficult to identify how any anticipation of the entry into force of the savings tax directive influenced the investment behaviour of Belgian households, since

other factors may also have been at work. Households' decisions are determined not only by their appraisal of the opportunities on the financial markets but also by technical or fiscal factors: the development of tax-free domestic products, whether or not the household prefers dematerialised securities, the effectiveness of the efforts to control fraud and tax evasion, the application of inheritance tax rules of varying stringency, etc. It must be said that, for some years now, a number of changes concerning these factors have made it less attractive for households to hold foreign financial assets.

b) Equities and units in equity UCIs

Comparison of the net acquisitions of Belgian and foreign equities and units in equity UCIs by Belgian households provides further interesting information. Thus, the very marked preference for foreign investments in 1999 is attributable to massive purchases of equities and units in equity UCIs issued by foreign enterprises. These investments seem to have been financed in particular by the sale of Belgian equities and units in equity UCIs. It is not by chance that this surge of enthusiasm coincided with the introduction of the euro. Owing to the elimination of the foreign exchange risk and exchange commission fees, the universe of household investments now extended to a far more varied and liquid range of securities than just those quoted on the Brussels stock exchange. Investors therefore turned away from Belgian stocks and took more interest in the leading euro area equities.

**CHART 5** FORMATION OF INTEREST-BEARING ASSETS<sup>(1)</sup>  
BY HOUSEHOLDS  
(flows, billions of euro)



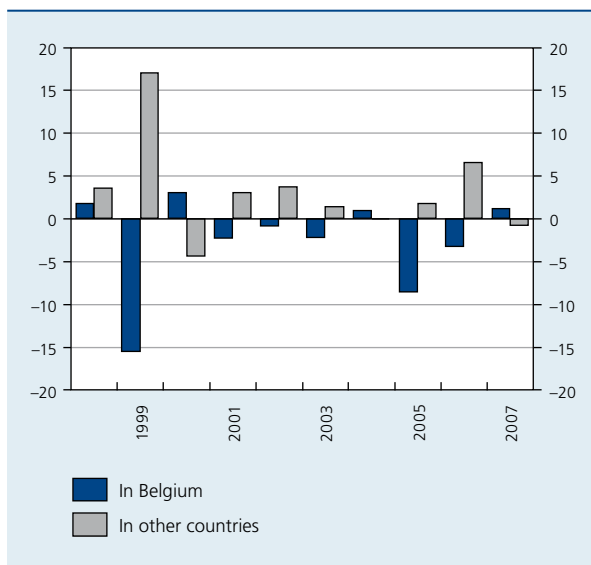
Source : NBB.

(1) Namely deposits, fixed-income securities and units in monetary and bond UCIs.

It must be said that the end of the 1990s was a period of euphoria regarding businesses involved in technology and telecommunications, two sectors which at that time were very under-represented on the Brussels stock exchange, which was dominated by financial corporations. Logically therefore, the bursting of this speculative bubble should have curbed investors' interest in foreign equities and units in equity UCIs. That seems to have happened in the year 2000, when households reverted, albeit cautiously, to net acquisitions of Belgian equities and units in equity UCIs. However, on 22 September 2000, a further step was taken towards the integration of the financial markets with the creation of Euronext, which provided somewhat easier access to the French and Dutch stock markets. In almost every year since 2001, households have therefore preferred foreign securities to those issued by Belgian firms.

(1) In reality, all fixed-income securities were taken into account, including bonds issued before 1 March 2001, which are not covered by the directive. Conversely, investments in mixed funds which place over 40 p.c. of their assets in bonds are not covered by the definition used in this part of the analysis concerning interest-bearing assets.

**CHART 6** NET ACQUISITION OF EQUITIES AND UNITS IN EQUITY UCIS BY HOUSEHOLDS  
(flows, billions of euro)



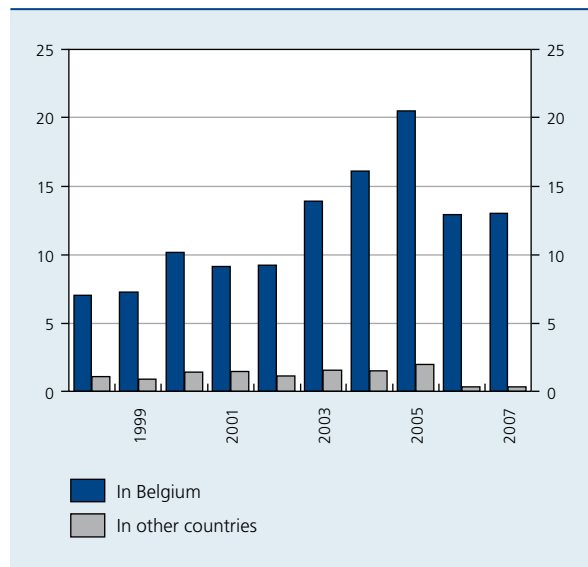
Source : NBB.

The last decade has also seen a number of Belgian listed companies being taken over by major foreign firms. These developments led to shifts between domestic and foreign counterparties in the equity portfolio of Belgian households. For example, in 2005 the public offer by Suez for shares in Electrabel resulted in the sale of Belgian shares in exchange for foreign shares. Adjustments of this type, which also concerned Petrofina and Total shares in 1999, were undeniably a factor in strengthening the position of foreign stocks in the portfolio of Belgian households. However, they do reflect a genuine desire for international diversification of their portfolio on the part of households, as once their positions had become foreign they did not dispose of them on a large scale in order to reinvest in Belgian stocks.

#### c) Technical insurance reserves

The financial accounts provide only a partial picture of foreign subscriptions to insurance technical reserves. Indeed, owing to a lack of information, only the amounts subscribed with companies established in Luxembourg are currently recorded, via the data from the *Commissariat luxembourgeois aux assurances*. Be that as it may, it seems that the formation of foreign technical insurance reserves is still very limited in comparison with the premiums paid to companies based in Belgium and supervised by the CBFA, which often qualify for a favourable tax regime.

**CHART 7** FORMATION OF INSURANCE TECHNICAL RESERVES  
(flows, billions of euro)



Source : NBB.

It is interesting that reserves formed in both Belgium and Luxembourg have tended to increase in the past ten years. Investments in insurance therefore seem to have escaped the “Belgium versus the rest of the world” portfolio adjustments which affected both interest-bearing assets and equities or units in equity UCIs, though in opposing directions. Thus, the marked fall which ended this upward trend in 2006 applied to investments in both Belgian and foreign insurance products. This downturn was due to the introduction, on 1 January 2006, of a 1.1 p.c. tax on premiums for individual life insurance policies. Although some households had anticipated this measure, by effecting at the end of the previous year payments originally scheduled for 2006, it nevertheless seems that many savers preferred to put their savings into alternative financial products.

## 2.2 Non-financial corporations

### 2.2.1 General

The outstanding amount of foreign liabilities of Belgian firms has soared in the past decade, increasing from 130 billion euro at the end of 1997 to 536 billion at the end of 2007, at which point approximately three-quarters of these liabilities took the form of equities.



**TABLE 4** FOREIGN FINANCIAL LIABILITIES OF BELGIAN FIRMS: BREAKDOWN BY INSTRUMENT  
(outstanding amount at end of period)

	1997			2007		
	billions of euro	p.c. of the total	p.c. of GDP	billions of euro	p.c. of the total	p.c. of GDP
Equities .....	74.0	57.0	33.5	404.9	75.5	122.2
Non-bank loans .....	32.5	25.0	14.7	56.2	10.5	16.9
Bank loans .....	10.8	8.3	4.9	50.9	9.5	15.4
Fixed-income securities .....	3.6	2.8	1.6	24.0	4.5	7.2
Other <sup>(1)</sup> .....	9.0	7.0	4.1	0.0	0.0	0.0
<b>Total</b> .....	<b>130.0</b>	<b>100.0</b>	<b>58.8</b>	<b>536.0</b>	<b>100.0</b>	<b>161.7</b>

Source: NBB.

(1) This item includes errors and omissions on Belgium's financial account with the rest of the world.

In absolute terms, the gross external assets of Belgian firms stood at 444.7 billion euro at the end of 2007 compared to 101.5 billion at the end of 1997. On 31 December 2007, around 46 p.c. of those assets consisted of equities and 38 p.c. inter-company loans.

The share of the non-resident sector in the total liabilities of non-financial corporations has thus increased from 24 to over 37 p.c. during the past ten years. The corollary to that increase was a decline in the share of resident sectors, particularly the financial sector (including credit institutions and other financial corporations), which dropped from 25 to 10 p.c. of the total, and that of households, down from 17 to 10 p.c. of the total. That partly reflects

the marked deceleration – and even contraction from 2002 to 2004 – of lending by Belgian banks to resident enterprises, and partly the succession of negative price effects incurred by Belgian households on their holdings of equities issued by Belgian firms, more particularly from 2000 to 2003.

On the assets side of the balance sheet of Belgian firms, the share of other countries also increased in relation to other counterparty sectors, rising from 28 to 39 p.c. of the total between 1997 and 2007. Here, too, it was the resident financial sector that saw the most significant drop in its relative share, down from 27 to 12 p.c. of the total.

**TABLE 5** FOREIGN FINANCIAL ASSETS OF BELGIAN FIRMS: BREAKDOWN BY INSTRUMENT  
(outstanding amount at end of period)

	1997			2007		
	billions of euro	p.c. of the total	p.c. of GDP	billions of euro	p.c. of the total	p.c. of GDP
Equities .....	46.5	45.8	21.0	205.7	46.3	62.1
Non-bank loans .....	23.5	23.1	10.6	169.9	38.2	51.2
Bank loans .....	6.2	6.1	2.8	36.1	8.1	10.9
Fixed-income securities .....	1.2	1.2	0.5	7.6	1.7	2.3
Other <sup>(1)</sup> .....	24.2	23.8	10.9	25.4	5.7	7.7
<b>Total</b> .....	<b>101.5</b>	<b>100.0</b>	<b>45.9</b>	<b>444.7</b>	<b>100.0</b>	<b>134.2</b>

Source: NBB.

(1) This item includes errors and omissions on Belgium's financial account with the rest of the world.

Finally, it should be pointed out that the financial links between Belgian firms – essentially links between associated companies forming part of the same group and recorded in full in the non-consolidated financial accounts drawn up by the Bank – have intensified in the past ten years. Thus, on 31 December 2007 an estimated 42 p.c. of the liabilities of Belgian firms had another resident non-financial enterprise as their counterparty (compared to 32 p.c. at the end of 1997), while in the case of their financial assets the figure was 52 p.c. (compared to 48 p.c. at the end of 1997).

The net external position of Belgian firms deteriorated steadily between 2001 and 2004, and then stabilised. As at 31 December 2007, it stood at 91 billion euro, or 28 p.c. of GDP, against 28 billion, or 13 p.c. of GDP, ten years previously.

### 2.2.2 Direct investment and inter-company loans: the role of the coordination centres

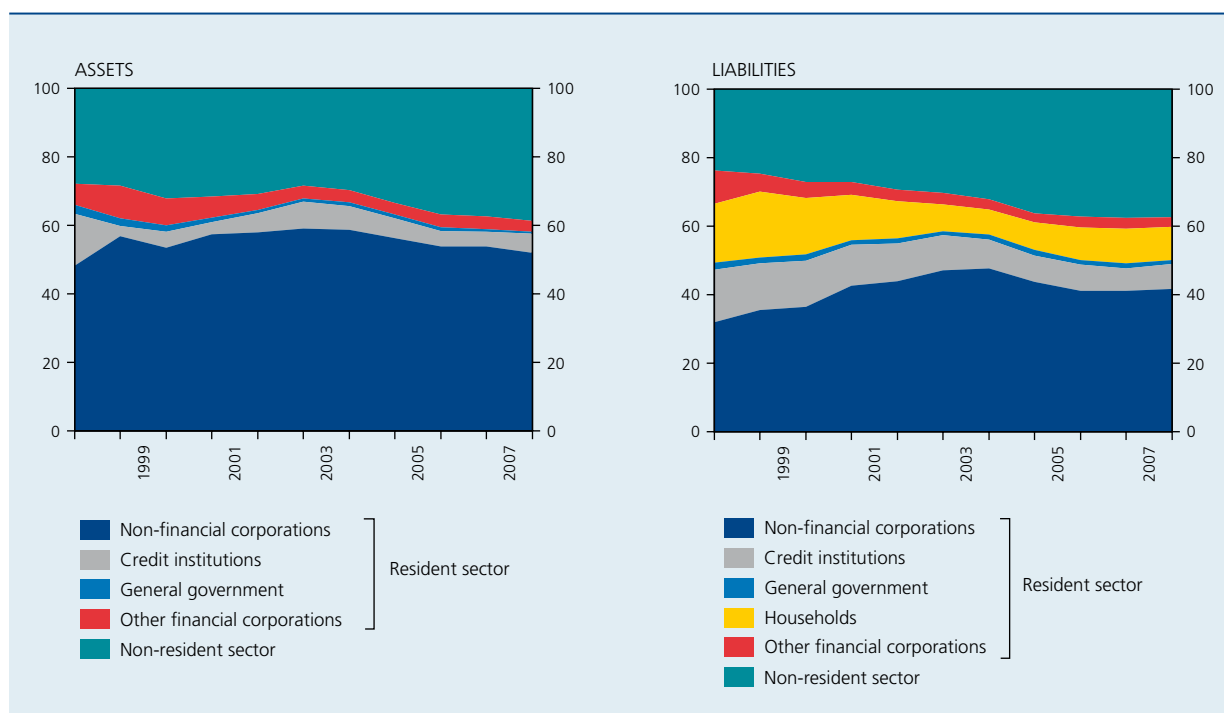
As explained in section 1.3, the movement in the net external position expressed as an outstanding amount is due to the accumulation of net financial flows and possible price effects. In the past decade, except in the years 1998, 2000 and 2005, the value of new liabilities has

systematically exceeded the value of new foreign asset formation. In other words, net capital inflows have generally been recorded, giving rise to the steady increase in the net external debt of Belgian firms.

Examination of the breakdown by instrument of the financial flows in relation to other countries shows that the net external liabilities are dominated by shareholdings in the form of foreign direct investment (FDI), while inter-company loans are significant at the level of the net external assets. This situation is due partly to the presence in Belgium of the coordination centres, though their particularly attractive tax status is currently being dismantled.

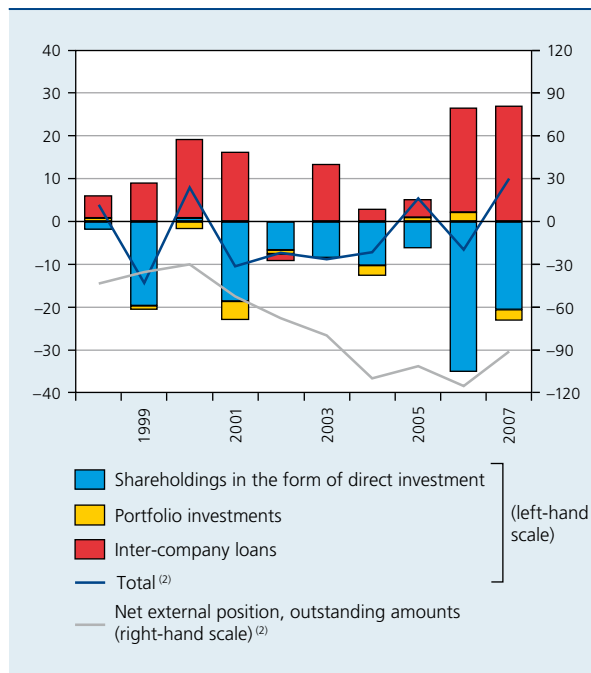
Under a preferential tax regime, Belgium-based coordination centres generally acted as the “internal banker” for a multinational group. Firms acquired shares in their coordination centre and received tax-free dividends from it. When they needed new money, they borrowed from the centre at interest, which was deductible as an expense. On the basis of the Bank’s internal estimates, the financial flows passing through the coordination centres represented around 33 p.c. of foreign direct investment in Belgium and 36 p.c. of direct investment by Belgium in other countries over the period 1995-2005.

**CHART 8** FINANCIAL ASSETS AND LIABILITIES OF NON-FINANCIAL CORPORATIONS: BREAKDOWN BY COUNTERPARTY SECTOR  
(outstanding amounts at end of period, percentages of the total)



Source: NBB.

**CHART 9** MAIN NON-BANK TRANSACTIONS AFFECTING THE NET EXTERNAL POSITION OF FIRMS  
(net flows <sup>(1)</sup>, billions of euro, unless otherwise stated)



Source : NBB.

- (1) A positive figure corresponds to the formation of a net external asset following a capital outflow. A negative figure corresponds to a net external liability and gives rise to a capital inflow.
- (2) The Total and Net External Position lines take account of all foreign transactions, and not only those detailed here. This means that they also include transactions between Belgian firms and foreign banks (loans and deposits) and issuances of fixed-income securities by Belgian firms with foreign subscribers.

Apart from the funds channelled through the coordination centres, in the past decade there has been extensive trading of shareholdings between Belgian and foreign firms, on account of mergers and acquisitions. These operations, which often led to the absorption of large Belgian companies by European (often French) multinationals, resulted in FDI inflows and contributed to the deterioration in the net external position of the target Belgian companies whose shares were transferred to foreign ownership. Following completion of the merger/acquisition, it is possible that the foreign company now controlling the Belgian company may continue to inject capital into the company and its subsidiaries, if any, causing additional FDI inflows and contributing still further to the deterioration in the net external position of firms.

### 2.2.3 The expanding role of bank transactions with the rest of the world

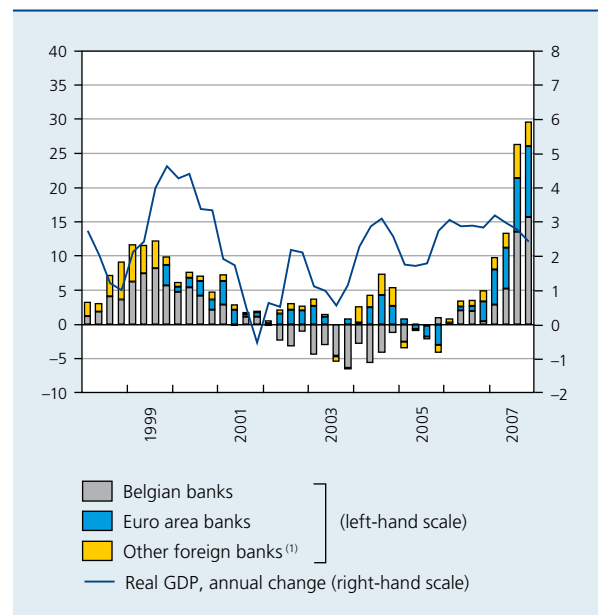
The net external position of firms also depends on the loans granted to them by foreign banks and the formation of any deposits with those same banks. Belgian firms

have made increasing use of foreign banks to meet their financing needs in the past decade. Thus, from 1998 to 2007, foreign banks granted the equivalent of 51 billion euro in new bank loans to Belgian firms, while Belgian banks lent only 36 billion. From 2002 to 2004, the funds supplied by foreign banks (9.6 billion euro) to Belgian firms more or less offset the 10 billion decline in loans granted by Belgian banks. Consequently, the share of foreign lenders in the outstanding total of bank loans to Belgian firms increased from 12 p.c. at the end of 1997 to 35 p.c. at the end of 2007.

The increasingly international character of businesses, the mergers and acquisitions, the elimination of barriers to freedom to provide services and the introduction of the euro are important factors which have contributed to this development. Banks based elsewhere in the euro area have in fact been the main source of lending to Belgian firms, accounting for around two-thirds of bank loans subscribed abroad. It should also be remembered that the internationalisation of bank services is probably even farther advanced than indicated by the figures, since loans granted to resident enterprises by subsidiaries of foreign banks established in Belgium are regarded as transactions between residents. Section 1.2 shows that, during the

**CHART 10** BANK LENDING TO NON-FINANCIAL CORPORATIONS, GEOGRAPHICAL BREAKDOWN OF LENDERS AND CYCLICAL DEVELOPMENTS  
(contribution to the annual growth of bank lending, unless otherwise stated)

(contribution to the annual growth of bank lending, unless otherwise stated)



Source : NBB.

- (1) Up to the third quarter of 1999, lending by "other foreign banks" includes lending by banks in the euro area.

past decade, Belgian banks have also exhibited a desire to diversify and extend their operations beyond the national market.

### 2.3 General government

At the end of 2007, the gross financial liabilities of general government stood at 337 billion euro (or 101.7 p.c. of GDP). The two principal holders of Belgian public debt are resident financial institutions, with 116.3 billion, and the rest of the world with a total of 155.4 billion. However, there has been a major change in their relative shares over the past ten years. Estimated at 61.4 billion at the end of 1997, the financial assets of the rest of the world on Belgian general government (the vast majority, over 95 p.c., being securities issued by the Belgian State) have grown steadily since 1999, and that growth has been at the expense of Belgian credit institutions.

At the end of 2007, 46 p.c. of the Belgian public debt was held by the rest of the world, 35 p.c. by resident financial corporations, 13 p.c. by general government, 4 p.c. by households and 2 p.c. by resident non-financial corporations.

For comparison, the financial assets held by Belgian general government on the rest of the world are very modest in scale. At the end of the year, public authorities are in fact encouraged<sup>(1)</sup> to place their long-term assets in Belgian public securities and their short-term assets in a current account opened with the NBB in the name of the Treasury, to minimise Belgium's consolidated gross debt and facilitate compliance with the Maastricht targets for the public debt.

The assets of Belgian general government on the rest of the world represented 3.1 billion euro at the end of 2007. They consisted mainly of loans between States, investments by local authorities in UCI units, and claims on the European Union.

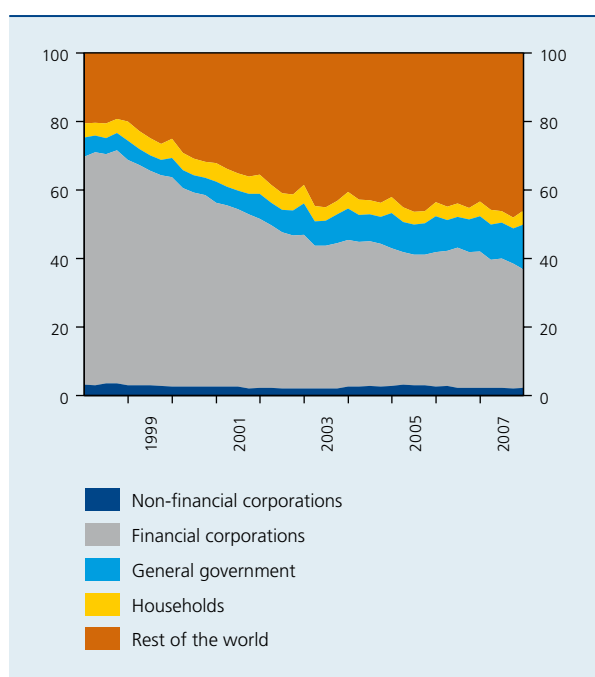
Regarding the financial liabilities of Belgian general government, the federal authority is responsible for 99.1 p.c. of the public debt held by the rest of the world, or 154 billion euro. The debt of the communities and regions in relation to other countries is very small, representing only 1.4 billion at the end of 2007. Local authorities and social security bodies had no financial liabilities in relation to the rest of the world at the end of that period.

It should be remembered that the general government debt consists essentially of securities, linear bonds (OLOs) and Treasury certificates. Some loans are also taken into account.

The share of Belgian public debt securities held by the rest of the world has grown steadily in recent years. While the proportion of foreign-held OLOs was around 20 p.c. at the beginning of 1999, it came to almost 55 p.c. at the end of 2007. The share of Treasury certificates held by the rest of the world has also followed an upward trend, rising from 42 p.c. at the beginning of 1999 to almost 77 p.c. at the end of 2007. This situation reflects the strong foreign demand engendered by the relative scarcity of short-term government securities in euro with a good rating from the rating agencies.

This development calls for several comments. First, the Treasury established some years ago a strategy for the more efficient management of the public debt. That strategy was motivated partly by a desire to diversify the debt securities, in order to ensure the liquidity of the securities issued for professional investors (OLOs and Treasury certificates). To ensure that liquidity, the Treasury concluded contracts with primary dealers and recognised dealers, who are responsible for promoting Belgian public debt

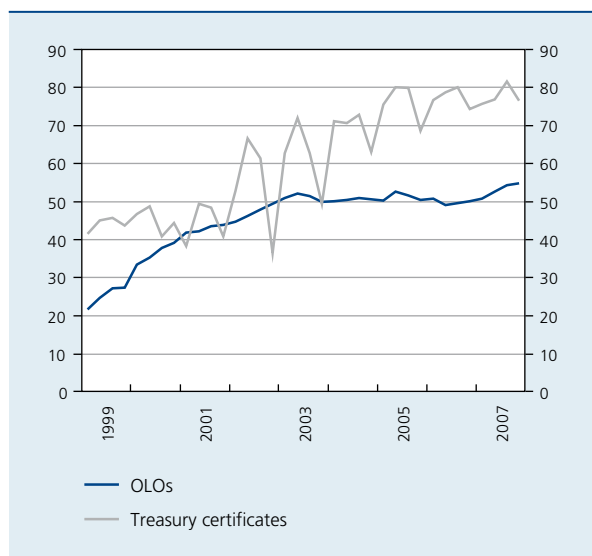
**CHART 11** FINANCIAL LIABILITIES OF GENERAL GOVERNMENT : BREAKDOWN BY COUNTERPARTY SECTOR  
(end-of-quarter data, percentages of the outstanding total)



Source : NBB.

(1) Royal Decree of 15 July 1997 modifying the legal framework for government investments (M.B. of 25 July 1997).

**CHART 12** PROPORTION OF FOREIGN-HELD OLOS AND  
TREASURY CERTIFICATES ISSUED BY THE BELGIAN  
STATE  
(end-of-quarter data, percentages of the total)



Source : NBB.

securities and stimulating activity on the primary and secondary markets (for more details, see NBB Report 2007, box 16). Improved liquidity for the securities in fact has a positive effect on the pricing of financial instruments and hence on the cost of the debt.

Finally, it is evident that foreign investors have maintained their interest in Belgian public debt securities in recent years, particularly owing to the pursuit of a relatively sound policy on public finances, which led the rating agencies to upgrade the rating of Belgian public debt securities.

## Conclusion

The openness of the Belgian economy is equally apparent in the financial links which Belgium has formed with other countries. At the end of 2007, Belgium's net external assets totalled 44.4 p.c. of GDP.

In the past ten years, Belgium's net financial assets have grown considerably, in the context of the switch to the single currency and the ongoing process of financial integration and globalisation. The extent to which the various non-financial sectors have adapted to these developments varies greatly from one sector to another.

General government is the sector which has seen the biggest increase in the share of the debt held by the rest of the world: that share in fact increased from almost 20 p.c. at the end of 1997 to around 46 p.c. at the end of 2007. At the time of the introduction of the euro on the financial markets, it was essential for the Treasury to widen its investment base: appropriate diversification of the group of primary dealers and recognised dealers was one of the ways in which it achieved that.

Non-financial corporations, which traditionally maintain very close international financial contacts, saw a steady increase in the share of the rest of the world in their financial transactions between 1997 and 2007: in the case of financial liabilities, the figure was up from 24 p.c. to over 37 p.c. and for financial assets it was up from 28 p.c. to 39 p.c. However, these orders of magnitude are subject to a strong upward influence exerted by the coordination centres based in Belgium, which perform the function of a financial intermediary for the multinational group to which they belong. In the past decade, there have been frequent exchanges of shareholdings between Belgian and foreign companies, reflecting the process of mergers and acquisitions, and these have also contributed to the growth of direct investment between Belgium and the rest of the world. Finally, it should be noted that foreign banks, and more particularly those located in the euro area, are granting a growing volume of loans to Belgian firms.

The share of foreign assets in the household portfolio dropped from 30 p.c. at the end of 1997 to 17 p.c. at the end of 2007. Naturally, that is due partly to the introduction on 1 July 2005 of the European savings tax directive; it has now ceased to be possible for individuals to avoid the tax on income from interest-bearing assets held in other countries, and that has ultimately led to the repatriation of those assets. In contrast, in the case of non interest-bearing assets, foreign investment flows have been positive in the past ten years. Finally, it should be pointed out that the share of the rest of the world in the liabilities of households is still negligible.