

2005-09-27

## PRESS RELEASE

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### **The potential growth of the Belgian economy and its determinants**

**(Article published in the Economic Review, 3<sup>rd</sup> quarter 2005)**

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The potential growth path of the economy is at the centre of various fundamental economic questions. It arises, in particular, in connection with the conduct of monetary policy and the management of public finances. The growth potential combined with the trend in the population also determines the progress of the level of prosperity in the economy. In recent years, renewed interest in this question has been kindled in the European economies by the dramatic advances in the new information and communication technologies (ICT) and their impact on productivity. The European debate on the Lisbon strategy also aims to strengthen growth potential, particularly in a context of population ageing.

Potential output is not recorded directly and therefore has to be estimated by indirect means. There are various assessment methods available for this purpose. The Bank has adopted a method of estimation based on the use of a production function. In this analysis framework, which is widely used, particularly by international institutions such as the EC, growth potential is linked to three determinants, namely the labour and capital available in the economy, and total factor productivity (TFP), which indicates the efficiency with which those production factors are used. That efficiency depends partly on technological progress.

The analysis reveals that in Belgium potential growth has averaged 2.2 p.c. for the private sector and 2.1 p.c. for the economy as a whole over the past twenty years, placing the country in the middle group of EU-15 countries. The largest contributions to potential growth come from the factor capital – which is also the source of the most marked fluctuations in potential growth around its average – and TFP. However, the contribution of the latter, which was the main engine of growth in the early 1980s, was halved between the start of the 1980s and the mid 1990s. Since then there has been a very gradual revival. The factor labour makes a structurally smaller contribution to growth, although that contribution has increased progressively over the years as a result of a trend increase in the participation rate and a slower reduction in working time.

The growth path can also be assessed by highlighting trends recorded in the past in terms of the volume of labour and apparent labour productivity. This exercise was carried out not only for Belgium but also for the EU-15 average and the United States. It appears that transatlantic growth has long benefited from a strong rise in the volume of labour, underpinned by a substantial increase in the population of working age, a high employment rate and the maintenance of working time. This relative advantage has nevertheless been steadily eroded since the mid 1990s, and the rate of increase in the volume of labour in the United States is now roughly equivalent to the European rate. The volume of labour in Belgium has tended to suffer from stagnation in the population of working age, a particularly low employment rate and a reduction in average working time, mirroring that seen in the EU-15 as a whole. Nonetheless, the situation has improved since 1995 as a result of favourable developments in terms of the employment rate and working time, which has been stable for several years.

The improvement in the performance of the US economy since the mid 1990s in terms of productivity growth contrasts with the downward trend in the productivity growth rate in the EU-15. Belgium has experienced the same deceleration. However, in the past ten years this was due mainly to a lower capital intensity. After declining between 1985 and 1995, growth of TFP – which in principle measures the overall productive capacity of the economy – stabilised at a level above the European average and close to that of the United States. This relatively good performance could be due to the fairly widespread use of ICT, as Belgium's investment expenditure on this item is greater than that of the majority of European countries. The highly skilled labour force is also a factor supporting TFP, although its impact has not been quantified in the case of the Belgian economy.

In the face of the adverse trend in the population of working age forecast for the coming decades, it is necessary to continue and reinforce measures to support the volume of labour available in the economy, notably by encouraging increased participation in the labour market. Other levers could also be used in order to stimulate productivity progress. Despite the statistical uncertainty surrounding this type of estimate, empirical studies appear to indicate that expenditure on research and development and efforts to improve the quality of the labour force are the most productive. They are yet more effective if market forces offer appropriate incentives to the economic agents.