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## PRESS RELEASE

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### **Economic projections for Belgium – Spring 2006**

(Article published in the Economic Review of the second quarter of 2006)

Coinciding with the publication in the ECB Monthly Bulletin of the Eurosystem's new projections for the euro area, this article gives a succinct presentation of the results for the Belgian economy for 2006 and 2007. Since the publication in December 2005 of the previous forecast, the expected strength of the global economy has been confirmed while the rise in oil prices has continued, monetary policy has become slightly less accommodating and the euro has risen in value against the US dollar.

In Belgium, growth in economic activity recovered since the end of 2005, at a higher rate than in the euro area as a whole. The backdrop to this new forecasting exercise thus paints a contrasting picture: the initial situation of the projections appears slightly more favourable than last autumn, with the Belgian economy displaying undoubted momentum at the beginning of the year. However, a number of conditions relating to the external environment are likely to be less favourable for growth and inflation.

The Eurosystem projections were compiled taking into account trade, which should remain buoyant and favourable for euro area growth. According to the futures markets, oil prices are likely to stay above the 70-dollar mark, whilst interest rates look set to develop in line with market forecasts. Exchange rates are set constant at the mid-May level, namely 1.27 dollars against the euro. In this context, euro area GDP growth should accelerate in early 2006, before levelling off at a rate of approximately 0.5 p.c. per quarter. Except for the influence of the rise in energy prices in 2006 and the changes to indirect taxes in 2007, inflationary pressures are likely to remain subdued.

In Belgium, there was a gradual but marked strengthening of economic activity, with GDP growth up from 0.1 p.c. in the first quarter of 2005 to 0.6 p.c. in the last quarter, and even 0.8 p.c. during the first three months of 2006, a rate which outstrips the growth potential of the economy. Based on the available indicators, the strengthening of activity is likely to be sustained during the second quarter of 2006. However, due to the increase in the price of oil, the recent appreciation of the euro against the dollar, the rise in interest rates and weakening external demand, economic growth should slow gradually throughout the year to fall more in line with the potential growth rate. All in all, real GDP growth should increase from 1.5 p.c. in 2005 to 2.5 p.c. in 2006. In 2007, it is likely to amount to 2 p.c., which is closer to the rate of growth forecast for the euro area as a whole, after exceeding it in 2006.

Most of the domestic demand categories, as well as net exports, are set to contribute to GDP growth during the two-year projection period, with the composition of growth being more balanced now than in 2004 and 2005. Investment, which had risen at an exceptionally high rate in 2005, should continue to grow, albeit at a more moderate pace. The increase in private consumption is likely to strengthen as a result of an improvement in household purchasing power, on the back of a slowdown in inflation. The effects of the tax reform introduced in 2001, the reductions in social security contributions and the increase in income of movable property, the latter being, however, more likely to be saved compared with other sources of income, should also benefit to their disposable income. There is likely to be little change in the household savings rate, which will reach a level close to 13 p.c. of disposable income. Growth in household expenditure on housing looks set to remain relatively buoyant in 2006, sustained by the continuing low level of long-term interest rates and the increase of secondary market prices, before slowing in 2007. Influenced by the municipal and provincial electoral cycle, public investment by local authorities will remain strong in 2006 but is likely to be offset by further sales of federal buildings. The revival of trade with euro area partners at the start of the year should cause export growth to accelerate in 2006. Growth in export markets should then slow which, when coupled with the delayed impact of the increase in the value of the euro, will curb the rise in exports. Nevertheless, Belgium's loss of market share is expected to be less than was the case in 2005. In 2006, exports are set to rise faster than imports, the latter having been sustained by the exceptional rise in investment in 2005, with the result that net exports should make a positive contribution to growth. In 2007, this contribution, albeit still positive, is likely to be less substantial. Finally, the contribution made by stocks to GDP growth should be positive in 2006, but becoming negligible the following year.

As a general rule, the employment trend follows the fluctuations in activity, albeit with a degree of delay. In 2005, 39,000 additional jobs were created despite the slowdown in economic activity at the start of the year, deemed by employers to be temporary in nature. Rather than make workers redundant, employers have preferred to use flexible measures in organising work. As a result of this phenomenon of labour hoarding, the economic recovery is highly unlikely to lead to a marked increase in the rate of job creation but is instead expected to bring about a higher utilisation rate of the workforce. This will be reflected in a rise in productivity per person, the growth rate of which should average 1.3 p.c. in 2006 and 2007, close to its long-term growth rate, compared to just 0.6 p.c. in 2005. The number of persons in employment in Belgium should increase further, by some 80,000 units over 2006 and 2007. With job creation corresponding broadly to the increase in the population of working age, the harmonised unemployment rate is set to fall only very slightly, from 8.4 p.c. in 2005 to 8.2 p.c. in 2006 and 2007.

Since 2004, the trend in energy prices has been the main factor determining overall inflation movements in Belgium. This is once again likely to be the case during the period covered by the projections, with the energy component continuing to make a key contribution to the rise of the harmonised index of consumer prices until the early months of 2007. On annual average, overall inflation is expected to fall, from 2.5 p.c. in 2005 to 2.4 p.c. in 2006 and 1.9 p.c. in 2007. The underlying inflation trend should, however, only increase moderately, to 1.6 p.c. at the end of 2007, due, among other things, to the moderation in labour costs in Belgium.

Hourly labour costs are likely to increase by 4.2 p.c. for the years 2005-2006 taken together, which is less than the nominal norm of 4.5 p.c. endorsed by the government. The introduction of the new health index in January 2006, the technical effect of which is to reduce the automatic index-linking of wages, has partly contributed to this result. Taking into account the temporary fall in the productivity growth rate in 2005, the increase in unit labour costs totalled 1.6 p.c. in 2005, before reverting to 0.8 p.c. in 2006 and 2007. As far as 2007 is concerned, the 1.9 p.c. rate of growth in hourly costs adopted for this projection, which is of the same order as the rates of previous years, corresponds broadly to the anticipated effect of indexation.

The public finance figures were compiled by taking into account the recent trend in tax revenues, the endogenous effect of the macroeconomic environment, an expenditure pattern based on historical movements and measures which have already been decided. New government measures, which would be adopted during the next few months, on the occasion of the additional budget review announced by the federal government for 2006 and within the framework of the 2007 budget, were not taken into account in this forecasting exercise. In this context, after having shown a limited surplus in 2005, of 0.1 p.c. of GDP, the general government financing balance should turn negative from 2006, by 0.3 p.c. of GDP that year and by 1.2 p.c. in 2007. Interest charges should continue to fall and tax revenues are expected to benefit from the promising economic climate, especially in 2006, although these elements are more than offset by the disappearance of the favourable incidence of the non-recurring factors.

Despite the budget deficits forecast for 2006 and 2007, the debt ratio should continue its downward trend during these two years, falling to 90.4 p.c. of GDP in 2006 and 88.7 p.c. of GDP in 2007.

**Projections for the Belgian economy: summary of the main results**  
(percentage changes compared to the previous year, unless otherwise stated)

	2003	2004	2005	2006 e	2007 e
<b>GROWTH</b> (calendar adjusted data)					
GDP at 2000 prices	0.9	2.4	1.5	2.5	2.0
Contributions to growth:					
Domestic expenditure, excluding change in stocks	1.0	2.0	2.8	1.7	1.9
Net exports of good and services	0.0	-0.3	-0.9	0.4	0.2
Change in stocks	-0.1	0.7	-0.3	0.4	-0.1
<b>PRICES AND COSTS</b>					
Harmonised index of consumer prices	1.5	1.9	2.5	2.4	1.9
Health index	1.5	1.6	2.2	1.7	1.9
GDP deflator	1.7	2.3	2.2	1.5	1.9
Terms of trade	-0.1	-0.5	-0.7	-0.6	0.1
Unit labour costs in the private sector	0.2	0.0	1.6	0.8	0.8
Hourly labour costs in the private sector	1.5	1.9	1.8	2.4	1.9
Hourly productivity in the private sector	1.3	1.9	0.2	1.6	1.1
<b>LABOUR MARKET</b>					
Domestic employment (average annual variation, thousands of units)	-3.3	23.7	38.5	38.2	41.6
Harmonised unemployment rate <sup>1</sup> (percentage of the working population)	8.2	8.4	8.4	8.2	8.2
<b>INCOMES</b>					
Real disposable income of private individuals	-1.0	-0.2	1.3	1.8	2.2
Private savings ratio (percentage of disposable income)	14.3	12.8	13.0	12.7	13.0
<b>PUBLIC FINANCES</b>					
Primary balance (percentage of GDP)	5.4	4.8	4.5	3.9	2.8
General government financing requirement (-) or capacity (percentage of GDP) <sup>2</sup>	0.1	0.0	0.1	-0.3	-1.2
Public debt (percentage of GDP)	98.5	94.7	93.3	90.4	88.7
<b>CURRENT ACCOUNT</b> (percentage of GDP according to balance of payments)	4.1	3.4	1.7	2.1	2.3

Sources: EC, NAI, NSI, NBB.

<sup>1</sup> Adjusted series (Eurostat).

<sup>2</sup> According to the methodology used under the Excessive Deficit Procedure (EDP).