Business Cycle Monitor

March 2024

Belgian economy expected to grow by 0.4% in the first quarter of 2024[1]

- According to the revised statistics Belgian economic growth declined marginally to 0.3% in the fourth quarter of 2023. This expansion of economic activity is in line with the estimate in our December BCM but slightly below the NAI's earlier flash estimate of 0.4%.
- In the fourth quarter, GDP growth benefited once more from robust private consumption growth. Household consumption growth should only moderate slightly in the first quarter of this year. Consumer confidence is still up compared to the fourth quarter but purchasing power growth is losing some traction.
- Fourth-quarter business investment in volume terms fell markedly, mostly due to unanticipated, exceptional factors. Fundamentals remain quite sound, however, and firm investment is expected to return to moderately positive (underlying) growth in the current quarter. Residential investment shrank in the fourth quarter and is likely to decline further in 2024.
- Government consumption growth was positive in the fourth quarter and should continue to grow at a moderate pace. Similarly, government investment growth should remain clearly positive, boosted by the roll-out of investment plans and the electoral cycle.
- Net exports increased activity growth in the fourth quarter but this was due to the aforementioned exceptional sales of investment goods abroad. Gradually improving competitiveness and the recent bottoming out of world trade should start supporting underlying export growth, which should most likely lead to an improvement of the growth contribution of net exports in the current quarter already.
- The NBB's BREL nowcasting models currently estimate growth in the first quarter at 0.3 to 0.4%, while the R2D2 model is less optimistic, predicting a growth rate of around 0.1%.
- All in all, we currently expect economic activity to expand by 0.4% in the first quarter of 2024. This is at the high end of the range of model nowcasts but below the median predictions of the one-indicator models. Positive risks are deemed limited, while negative risks mostly relate to possibly lower-than-anticipated growth in firm investment and trade.

[1] This is a short-term NBB estimate which should not be confused with the official statistics published by the National Accounts Institute (such as the flash GDP estimate, which is released one month after each quarter). This estimate is based on nowcasting models and expert judgment and incorporates information up to 8 March 2024. Like all estimates and forecasts, it is subject to a degree of uncertainty.

The euro area economy has again stagnated in the fourth quarter of 2023 and growth should remain sluggish in the current quarter

According to the latest statistics euro area GDP has again flatlined in the fourth quarter of 2023. The euro area economy has essentially teetered on the edge of a recession throughout the year: in annual terms, the growth rate amounted to just 0.1%. This is partly due to the notoriously volatile statistics for Irish GDP, that declined sharply in all quarters of 2023. This is unlikely to reflect the underlying development of the Irish economy.[2] Excluding Ireland, the euro area economy still only shows a very moderate expansion: quarterly growth edged up to 0.2% in the final quarter, with growth coming in at just 0.5% in year-on-year terms.

Current statistics suggest that euro area GDP growth was supported by minor increases in both household and government consumption and by an acceleration in business investment. Inventory drawdowns and negative net exports weighed on GDP growth.

Table 1

Real GDP growth
(%, adjusted for seasonal and calendar effects)

	Quarter-on-quarter change				Year-on-year change
	2023Q1	**2023Q2**	**2023Q3**	**2023Q4**	**2023Q4**
Euro area (EA)	0.0	0.1	-0.1	0.0	0.1
p.m. EA excl. Ireland	0.2	0.2	0.0	0.2	0.5
Germany	0.1	0.0	0.0	-0.3	-0.2
France	0.0	0.6	0.0	0.1	0.7
Italy	0.5	-0.2	0.2	0.2	0.6
Spain	0.5	0.5	0.4	0.6	2.0
Netherlands	-0.5	-0.4	-0.3	0.3	-0.8
Belgium	**0.4**	**0.3**	**0.4**	**0.3**	**1.5**
p.m. Ireland	-1.9	-0.4	-1.9	-3.4	-9.1
EU	0.1	0.1	-0.1	0.1	0.3
UK	0.2	0.0	-0.1	-0.3	-0.2
US	0.6	0.5	1.2	0.8	3.1
JP	1.1	1.0	-0.8	-0.1	1.1

Sources: EC, US Department of Commerce, Cabinet Office Japan.

Growth performances were somewhat uneven across member states with the German economy clearly lagging the euro area average. This is mostly due to the new sharp decline in private investment, as the growth contribution of net exports was zero and household consumption only grew moderately. All in all, the German economy contracted by 0.3% in the final quarter after a stagnation in the previous quarters. Domestic demand was sluggish as well in France and Italy but this was offset by positive growth in net exports, leading to a marginally positive growth rate. The Dutch economy, on the other hand, benefited from robust household consumption growth that more than offset a decline in private investment. Finally, Spain continued to outpace all other large euro area countries and growth even edged up to 0.6% in the final quarter of 2023. In year-on-year terms this translates to a solid 2% expansion.

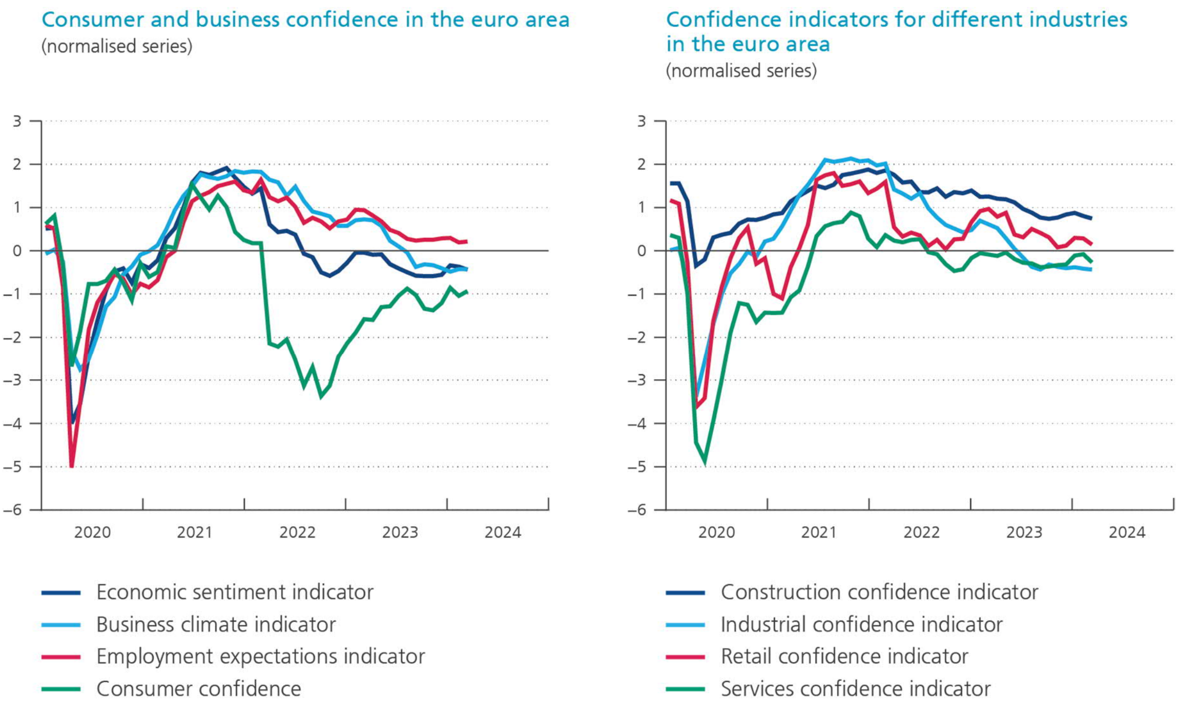
[2] The volatility in Irish GDP statistics is mostly due to operations involving intangible assets. These transactions usually do not reflect the Irish or euro area business cycle and are related to tax optimisation by large foreign-owned multinationals. See Andersson et al (2023) for a detailed discussion.

Among the major developed economies outside the euro area, the US economy continued to post strong growth numbers and expanded by 0.8% in the fourth quarter. In volume terms, the US economy has now grown by over 3% over the past four quarters. On the other hand, economic activity contracted in the UK in the fourth quarter and, after new statistical revisions, annual growth is now negative again, at -0.2%. The Japanese economy experienced a weak second half of 2023, with economic activity shrinking marginally again in the fourth quarter. However, in annual terms, fourth-quarter GDP growth remains above 1%. Overall, growth in the euro area is, on average, noticeably lower compared to most other major advanced economies, except for the UK.

Survey indicators suggest that economic sentiment in the euro area remains relatively weak. The EC's Economic Sentiment Indicator (ESI) for the euro area edged down in February. While it is still marginally above its fourth-quarter average, it remains below its long-term average. The mild decline can be attributed to weaker business confidence, in particular among services, retail trade and construction managers, while manufacturing confidence was largely unchanged. Euro area consumer confidence had improved in the fourth quarter and edged up somewhat in February but is still well below its long-term average (see Figure 1). The outlook for the labour market remains sanguine: the employment expectations index, reflecting managers' employment expectations, remained stable at a level that is still clearly above its long-run average.

Figure 1

Sentiment indicators for the euro area



Source: EC.
Note: The original series are normalised around their historical average and divided by their standard deviation.

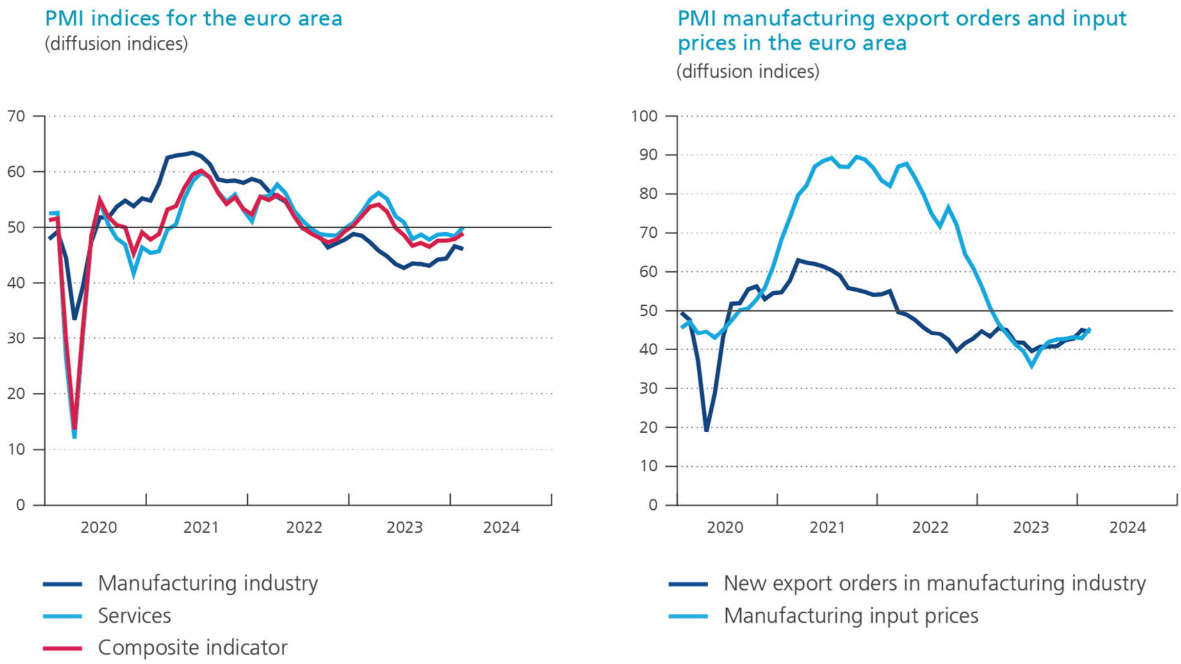
A look at the different components of the composite business confidence indicators for the main euro area industries shows that much of the downturn in recent months is related to the evaluation of the recent past, while reports on managers' outlook often appears to be somewhat more upbeat. This was the case in the manufacturing industry, for example, with managers' reports on higher-than-normal inventory levels being offset by some brightening of production expectations. In the retail sector as well, inventories increased and the recent business situation was assessed to have worsened but the outlook remained stable. Confidence in the construction industry also deteriorated in February as both employment expectations and managers' assessments of order books worsened but the trend of activity was said to be improving. The downturn in the confidence indicator for the services industry, on the other hand, was broad-based downturn in February.

The PMI indicators also point to continued weakness in the current quarter but suggest that the economic situation is slowly improving. The composite indicator for the euro area again edged up slightly in February, maintaining the gradual upward trend that started last November (see Figure 2, left-hand graph). However, the indicator remains below the level of 50 in the first quarter of 2024, which in principle corresponds to a contraction. The uptick of the composite PMI in February was fueled by improving sentiment in the services industries, which returned to just above the 50-level for the first time since late summer. On the other hand, conditions in the manufacturing industry are reported to remain bleak and a new worsening in manufacturing confidence in February moved it further below the 50-mark. However, despite some short-run volatility, the manufacturing PMI has trended up in recent months and is now well above the mid-2023 trough.

Despite new disruptions in supply chains, notably related to the maritime trade in the Red Sea, pipeline pressures on prices continue to ease. The relevant PMI for manufacturing input prices has trended up but remains firmly below the 50-mark, indicating a continued decrease in prices (see Figure 2, right-hand graph). Prices for natural gas, in particular, have reached their lowest level since early 2021. This decline can be attributed to mild winter weather and declining manufacturing output, leading to lower European energy demand. Nevertheless, current prices for energy remain higher than in other economies, such as the US, China and India. This erodes the cost competitiveness of energy-intensive European manufacturing. These unfavourable conditions are reflected in the subdued developments of the new export orders PMI for the manufacturing industry, which has been below 50 (pointing to negative growth) for two years now. **Overall, despite a gradual improvement of conditions, the sentiment indicators point to continued weakness in euro area economic activity in the first quarter of 2024 and GDP growth is expected to remain close to zero.**

Figure 2

PMI indices



Source: HCOB.

The Belgian economy grew by 0.3% in the fourth quarter

According to the revised statistics Belgian economic activity decelerated marginally to a growth rate of 0.3% in the fourth quarter of 2023, which is still above the euro area average. This expansion of economic activity is exactly in line with the estimate in our December BCM but slightly below the NAI's earlier flash estimate of 0.4%.

As regards the demand components, our expectations in the December BCM were quite accurate for most demand components. Household consumption continued to expand in the fourth quarter and accelerated slightly to a quarterly growth rate of 0.5%, while housing investment continued to fall, as expected. Developments for government spending were also accurately anticipated, with government consumption expanding at a moderate pace and government investment growth remaining positive, in line with the expected boost in the run-up to local elections. As always, it should be noted that quarterly statistics on government spending in particular are prone to significant revisions. GDP growth was also bolstered by a moderate degree of inventory building.

However, our estimates for business investment and net exports in the fourth quarter were off by quite some margin. While we had anticipated a moderate expansion, business investment actually declined by 8.5% on a quarterly basis. At the same time, exports expanded more than expected and net exports turned neutral. This shift between firm investment and exports can be mostly traced back to unanticipated, very large sales of ships by a domestic company to a foreign counterparty. While such transactions do not affect GDP growth, they reduce business investment and increase exports to the same extent. However, correcting for these specific sales, business investment actually still posted a (limited) decline in the fourth quarter, which was below our expectations. The underlying contribution of net exports to GDP (excluding these sales) remained negative, as anticipated in the December 2023 BCM.

Turning to the production approach to GDP, developments in the last quarter of 2023 remain very much in line with those in preceding quarters. Activity growth was again mainly driven by services, which were up by 0.6% from the previous quarter. Both market and non-market services contributed positively, with the main contribution to growth again coming from the former. Activity accelerated in the construction industry, which expanded by 1.0%, up from 0.6% in the third quarter. Given the difficult conditions reported by construction firms, this is again a surprisingly vigorous pace. Value added in the manufacturing industry declined further: this was the fifth consecutive quarter of negative growth.

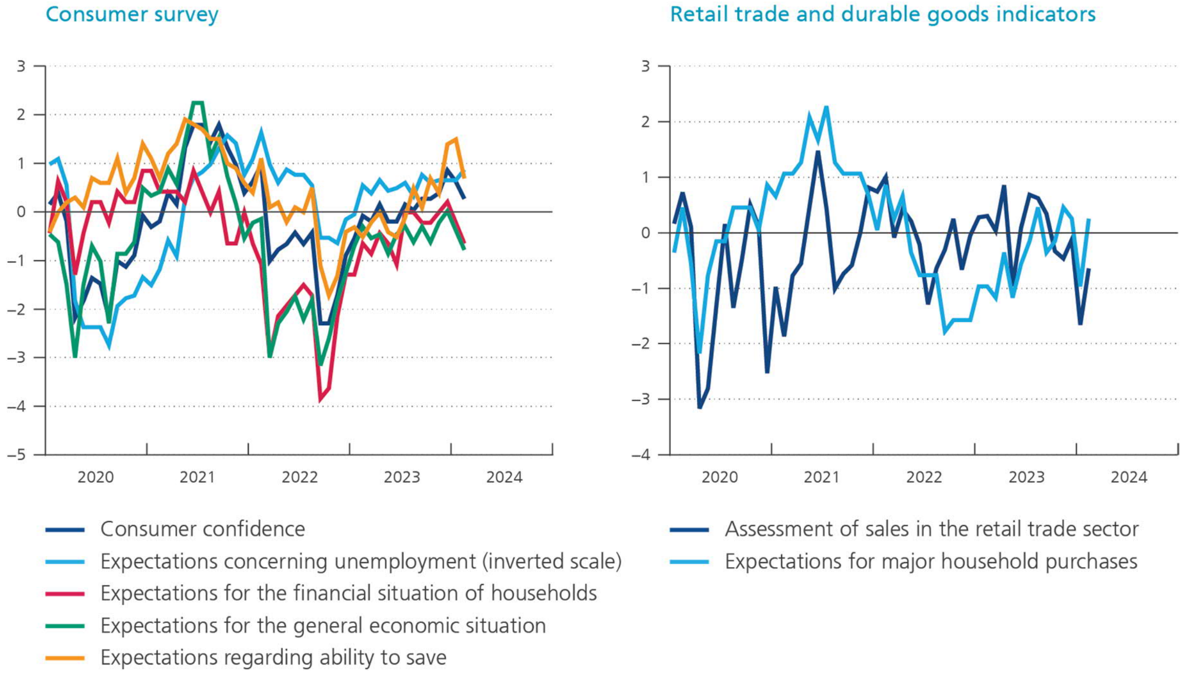
Household consumption growth should continue to expand at a robust pace in the first quarter

The slight acceleration in household consumption growth in the previous quarter is in line with overall developments in consumer confidence, which peaked late in the fourth quarter of 2023 after having recovered from the lows reached in autumn 2022 (see Figure 3, left-hand graph). In January and February consumer confidence has weakened slightly. Households' outlook on the general economic situation for the next twelve months has deteriorated, which is also the case for their saving intentions and their expectations for their financial situation. However, the unemployment expectations, i.e. the component of consumer confidence that has the greatest predictive power for actual consumption, continued to improve.

Other indicators also paint a mixed picture. The survey indicator on households' expectations for major purchases in the next 12 months had essentially moved sideways since the second half of 2023 but is now back to just above its long-term average (see Figure 3, right-hand graph). However, certain sentiment indicators in the retail industry, such as the assessment of sales, have been trending down since mid-2023. As noted in the previous BCM, business intelligence collected in the fourth quarter of last year already pointed to a slowdown in activity and some inventory build-up in non-food retail. Moreover, consumers were said to have become increasingly price conscious. However, respondents also mentioned that at least part of the slowdown in retail was the result of an ongoing shift in spending away from goods towards services, which seems to have been confirmed in the latest statistics for market services. At the same time, the synthetic curve for retail trade has shown some improvement in the most recent months (see Figure 4, left-hand graph) but the upswing is mostly the result of a marked improvement in the situation for food retail and car sales. Conditions remain challenging for non-food retail.

Figure 3

Indicators of household consumption growth
(normalised series)



Source: NBB.
Note: The original series are normalised around their historical average.

Household consumption should still be supported by strong fundamentals, although perhaps to a lesser extent than in previous quarters. While employment growth remains positive, it has moderated since late 2022 and came in clearly below its long-term average in the fourth quarter of 2023. Job creation is expected to remain positive but to moderate in the current and upcoming quarters, thereby lending somewhat less support to household incomes. Inflation has fallen rapidly but is edging up again in recent months (mostly due to the unwinding of government measures). In addition, the rapid disinflation in 2023 implies that nominal wages are boosted less by the automatic price indexation. All in all, purchasing power growth is now clearly moderating, after the strong increase in 2023.

All in all, we expect household consumption growth to remain robust but moderate slightly in the first quarter of 2024.

While firm investment growth should recover somewhat, housing investment is expected to shrink again in the first quarter

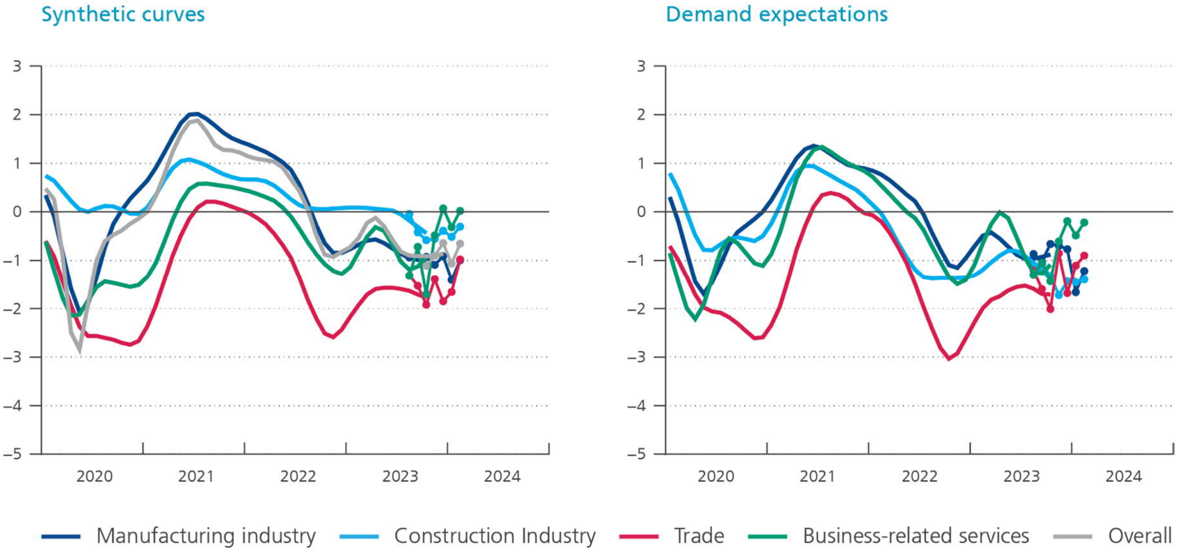
Even after correcting for the exceptionally large sales of ships, business investment declined slightly in the fourth quarter. The downturn comes after a remarkable surge up to the third quarter of 2023. Even with the sharp decline in the last quarter, overall business investment in 2023 was still up by over 6%. Firms reported having ramped up their investment in automation and digitalisation in response to higher wage costs and a tight labour market while energy price volatility and a progressively stringent regulatory environment prompted (energy-intensive) firms to intensify the 'greening' of their production processes.

Business confidence had weakened somewhat in the second and third quarters of 2023 but may have bottomed out in the fourth (see Figure 4, left-hand graph). Results for the current quarter point to a tentative recovery in confidence among firms. At industry-specific levels, sentiment remains weakest in the manufacturing industry, with the uptick in the February reading only reversing the sharp drop in January. Sentiment in the business-related services industries, on the other hand, has strongly improved from late 2023 onwards and confidence edged up in the trade industry. Overall, sentiment in the services industries has improved noticeably in recent months. Although confidence among respondents in the construction industry remains downbeat, business sentiment may have passed the trough: the business sentiment indicator is currently somewhat higher than in the fourth quarter of 2023.

Turning to firms' demand expectations, the outlook in the manufacturing industry remains on a downward trend. However, the demand outlook for business services and trade improved somewhat, while the construction industry's outlook remained relatively stable (Figure 4, right-hand graph). All in all, these indicators suggest that recent trends will likely continue.

Figure 4

Business sentiment and demand expectations
(normalised series)



Source: NBB.
Note: The original series are normalised around their historical average and divided by their standard deviation.

The recent surge in business investment has left investment needs in (additional) production capacity at relatively low levels. In January, production capacity utilisation in the Belgian manufacturing industry as measured by the quarterly NBB survey came in stable at 74.4%. This is the lowest level since 2020 and clearly below the long-run average of around 80%. The downbeat outlook for the manufacturing industry, which accounts for the bulk of firm investment, may further reduce investment needs.

Financial conditions tightened significantly in the past year, as interest rates rose. However, credit conditions were reported to have eased recently, with the 'credit constraint perception' by firms in the NBB's quarterly survey on the assessment of financing conditions declining from 41.8% in October 2023 to 27.6% in January 2024. This is the lowest level since mid-2022, even if it remains much higher than the figure of 10% recorded in early 2022. At the same time, it should be stressed that access to financing has not been a key determinant of recent investment developments. Firms generally have large cash balances (see e.g. Piette and Tielens, 2023) or, in the case of larger groups, can call upon intra-group financing. Hence, the slight easing of financial conditions should in itself not push up investment that much.

Finally, it should be stressed that, according to the current information, additional ships may be sold abroad in the near future. While the exact timing is uncertain, this may again affect headline numbers for investment and exports in the current quarter. As these transactions have no significant impact on GDP, we exclude them from the assessment in this Business Cycle Monitor in order to focus on the underlying trends.

All in all, we expect business investment (corrected for exceptional transactions) to return to moderately positive growth in the first quarter, as the drive towards greater automation and digitalisation as well as greening of production processes should continue. The growth rate should however be much lower than the one observed in the first three quarters of 2023.

Based on the latest statistics, residential investment contracted again in the fourth quarter of 2023 bringing the annual decline to 5.7%. Despite strong fundamentals in household income, the rise in interest rates resulted in a reduction in demand: mortgage lending was down by 24% on average in 2023 compared to 2022, but the decline was reported to be tapering off in the final quarter. Other leading indicators such as building permits have plummeted as well. Survey indicators show a marked lack of confidence in the construction industry, but the most recent data suggest that the industry may be near the trough. As mentioned earlier, expectations for demand have stabilized in recent months. **In sum, we expect residential investment to continue to fall in the first quarter of 2024, albeit possibly at a slower pace.**

Taken together, the expected moderate growth of firm investment and the continued slump in residential investment will likely lead to total private fixed investment growth in the current quarter that is sluggish at most.

Government investment, on the other hand, grew by 0.5% in the fourth quarter. **The further roll-out of recovery plans and the regular electoral cycle should continue to support government investment in the near term.**

Government consumption should continue to expand moderately

Government consumption growth in real terms came in positive in the fourth quarter, in line with expectations. As always, it should be stressed that the quarterly statistics on demand components, for government spending in particular, are often subject to subsequent revision. **Nonetheless, we expect government consumption growth to continue its moderate expansion in the first quarter of 2024.**

Even without exceptional transactions the contribution of net exports to growth should improve gradually

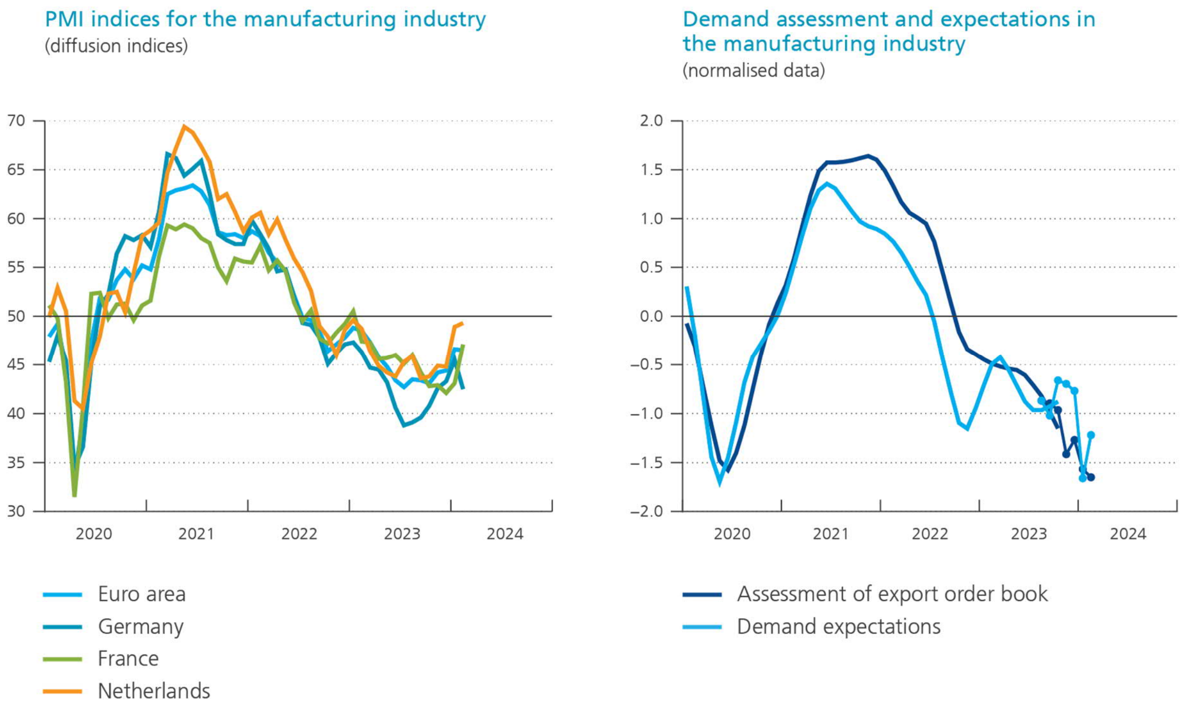
The external environment for Belgian exporters remains challenging. International trade has been very weak throughout most of last year. **While current indicators suggest that the growth in global goods trade has turned positive again in the last quarter of 2023, euro area exports volumes are continuing on the downward trend that started in late 2022.** The PMI manufacturing indices for Belgium's main neighbouring countries, which are also its primary trading partners, and the euro area are still at levels that in principle indicate a contraction, despite the clear upturn since the summer (see Figure 5, left-hand graph). In addition, the observed recovery remains fragile, as evidenced by the new weakening for the euro area and Germany in particular in the beginning of this year. However, manufacturing sentiment in the Netherlands and France continued to improve.

At the same time, the cost competitiveness of Belgian exporters that had worsened significantly recently, should now be on the mend and the losses in their export market shares should gradually narrow. Energy prices have declined substantially, which reduces the costs gap with respect to firms outside the euro area. In addition, nominal wages costs are now rising faster among the euro area trading partners. Still, demand expectations for the Belgian manufacturing industry as recorded in the NBB's monthly business survey (see Figure 5, right-hand graph) remain pessimistic and firms' assessments of export orders continue to plummet, approaching the low point witnessed in 2020.

Overall, the outlook for export growth in the first quarter remains highly uncertain but the recent bottoming out of world trade and gradually improving competitiveness should start supporting growth in exports, most likely in the current quarter already. While imports should accelerate as well, the growth contribution of net exports should improve (irrespective of additional sales of ships).

Figure 5

PMI indicators in neighbouring countries and export orders in manufacturing



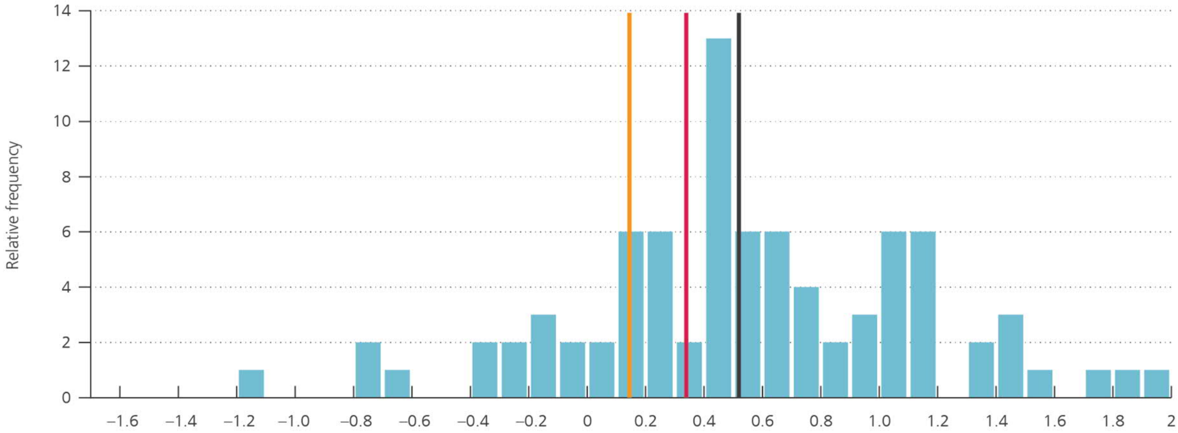
Sources: Markit, NBB.
Note: The series in the right-hand graph are normalised around their historical average and divided by their standard deviation.

The median value of the mechanical nowcasts points to an acceleration of GDP growth in the first quarter of 2024

The informational content of the most recent survey and financial data can be summarised by looking at the range of mechanical GDP predictions using one-indicator bridge models. **The median of the various predictions points to positive growth of 0.51% in the first quarter of 2024** (see Figure 6). The range has broadened, however, at [-1.2;2.0], indicating that uncertainty has increased, and is skewed slightly towards the higher end. It should be noted that the past forecast performance of these simple models suggests that individual predictions should be interpreted with caution, even under normal circumstances.

Figure 6

Histogram of one-indicator bridge model predictions using a broad set of survey and financial data and NBB nowcasting model predictions of real GDP growth in the first quarter of 2024. Relative frequency in percentage terms.



Source: NBB.
Note: The black line corresponds to the median of the one-indicator bridge model predictions of current quarter GDP growth, while the red and orange lines correspond to the predictions by the BREL bridge model and the R2D2 dynamic factor model, respectively.

Economic activity expected to continue to expand at a broadly stable pace in the first quarter of 2024

Of the NBB's more elaborate standard nowcasting models, BREL predicts positive quarterly growth of 0.34% in the first quarter, while R2D2 estimates growth at around 0.14%. A preliminary estimate using an improved BREL model,[3] recalibrated to take into account the unusual volatility of the pandemic period, indicates a somewhat higher growth estimate, of 0.44%. As always, these model-based estimates should be complemented by information gathered from other sources, as well as expert judgment.

Despite the continued weakness of the external environment, the recent performance of the Belgian economy has remained remarkably robust. Domestic demand has been a strong growth driver. The outlook for the current quarter suggests that activity can be expected to accelerate slightly. Household consumption growth could moderate slightly. On the other hand, excluding possible additional transactions that have affected investment and exports in the previous quarter, business investment growth is expected to turn positive again, while the contribution to GDP growth from net exports should also improve.

All in all, we currently expect economic activity to grow by 0.4% in the first quarter of 2024. This estimate is at the higher end of the model nowcasts. Upside risks are deemed limited, but again mainly related to possible positive surprises from domestic demand. Specific downside risks pertain to possibly lower-than-anticipated growth in firm investment and trade.

[3] Further analysis on the robustness of this improved model is needed. We expect a technical Working Paper on this subject to be published in the second half of 2024.