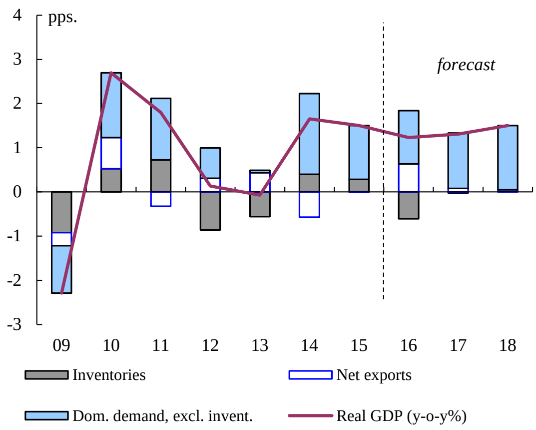
1. BELGIUM

Modest growth, strengthening labour market

Economic growth is expected to remain fairly stable, at 1.2% in 2016, 1.3% in 2017 and 1.5% in 2018. Domestic demand continues to be the main growth engine with a particular impetus from investment and private consumption progressively gaining momentum over the forecast horizon, assisted by job and wage growth. The fiscal deficit is expected to widen again in 2016 to 3.0% of GDP before falling back to 2.3% in 2017, when public debt would level off at around 107% of GDP.

The Belgian economy lost some steam in the first nine months of the year. This deceleration coincides to some extent with the March terrorist attacks and their aftermath. Any impact from the March events is expected to be transitory, though, in spite of a continuing slump in tourist arrivals. Activity is set to expand by 1.2% in 2016, the same as in the spring projections. Domestic demand has been the prime growth driver in recent quarters and this is expected to remain the case over the forecast horizon as private consumption rebounds and joins the rather dynamic growth in investment. In spite of a less supportive external environment, also following the British leave vote and the relatively tight trade links with the United Kingdom, external demand is expected to deliver a small, positive contribution to overall growth in coming years.

Graph II.1.1: **Belgium - Real GDP growth and contributions**



Brightening outlook for private consumption

After several years of low wage growth due to the government's strategy of sustained wage moderation, employees are seeing an uptick in their pay cheques in 2016 as wages are again being adjusted for the cost of living, some real wage increases have been negotiated and income tax cuts are being enacted. These factors compensate for the dampening effect of higher inflation on purchasing power and are set to remain in place in coming years. Overall, household consumption is expected to grow by 0.7% in 2016 and to rise to 1.3% in 2017 and 1.4% in 2018.

The positive outlook for private consumption is underpinned by the good performance of the labour market, with comprehensive job creation in the private sector. While leading indicators suggest a mild fall-back in upcoming quarters from recent rates, continued economic growth and the prospect of additional cuts in social security contributions for employers in 2018 are expected to keep net job creation at 40,000 and 45,000 in 2017 and 2018, compared to 53,000 in 2016. This implies a decline in the unemployment rate from a peak of 8.5% in 2015 to 7.6% in 2018.

Broad-based increase in investment

The expected increase in investment of 3.3% in 2016 and about 3% in coming years is broad-based across sectors. Business investment has been leading the way, following a steady increase in profit margins as a result of labour cost reductions. Together with supportive financing conditions, improving competitiveness relative to peer-countries further underpins business investment, with risks surrounding this positive outlook mainly rooted in the external environment. Construction investment has also been dynamic recently, due to housing and public infrastructure projects, such as school buildings. While historically low mortgage interest rates and comparatively low yields for alternative investment assets create the setting for a continuation of housing investment, the investment cycle of local governments and the start of large infrastructure works are forecast to drive public investment in 2017-18.

Inflation to remain around 1.7%

HICP inflation is forecast at 1.7% in 2016, compared with 0.6% in 2015. Annual price pressures peaked at 2% over the summer but the fading impact of a number of past government measures has led to slower price growth since.

Rising oil prices and dynamic service prices should keep inflation nevertheless broadly at 1.7% in the coming years, higher than the euro area average.

Fiscal consolidation halts in 2016, taken up again in 2017

The general government deficit is projected to widen to 3.0% of GDP in 2016, pausing the slow-moving consolidation of public finances. The deterioration from the 2.5% of GDP deficit in 2015 is revenue-driven. The reductions in income taxes and social security contributions mentioned above have not been fully compensated for by alternative financing measures, which add to generally disappointing tax collection. Lower one-off revenues contribute to the decline in the revenue-to-GDP ratio. Conversely, spending restraint is thwarted by temporary expenditures related to asylum-seekers and the terrorist threat (0.2% of GDP in total), one-off expenditure and high inflation leading to faster-than-initially-anticipated indexation of public wages and social benefits. In spite of a further decline in interest expenditure (0.4% of GDP), the structural balance is projected to deteriorate slightly in 2016.

In 2017, the deficit is expected to narrow to 2.3% of GDP. Primary expenditure growth should be curtailed by the disappearance of part of the temporary expenditure increases mentioned above, savings in health care (0.2% of GDP) and other social benefits. Government wages and social benefits are projected to be indexed in the third quarter of 2017. Interest expenditures are forecast to decrease by another 0.2% of GDP next year. On the revenue side, indirect taxes (0.1% of GDP) and taxes on income (0.1% of GDP) contribute to the overall consolidation of public finances. The structural balance is projected to improve by around ¾ pps. of GDP in 2017.

Under a no-policy-change assumption, the deficit is estimated to increase again to 2.4% of GDP in 2018, with the structural balance deteriorating by around ¼ pps. of GDP given planned tax cuts for which financing has not yet been identified.

Public debt is expected to increase from 105.8% in 2015 to around 107% in 2016 and 2017, before starting to decline again as of 2018. Stock-flow adjustments stemming from regional loans and interest rate swaps contribute to the increase in government debt.

Table II.1.1:

Main features of country forecast - BELGIUM

		2015			Annual percentage change					
	bn EUR	Curr. prices	% GDP	97-12	2013	2014	2015	2016	2017	2018
GDP		410.4	100.0	1.9	-0.1	1.7	1.5	**1.2**	**1.3**	**1.5**
Private Consumption		210.2	51.2	1.4	0.7	0.6	1.1	**0.7**	**1.3**	**1.4**
Public Consumption		98.1	23.9	1.6	0.1	1.4	0.5	**0.4**	**-0.3**	**0.3**
Gross fixed capital formation		94.4	23.0	2.2	-1.5	5.1	2.4	**3.3**	**2.9**	**2.9**
of which: equipment		31.2	7.6	1.9	-1.4	8.5	0.7	**3.9**	**2.6**	**2.9**
Exports (goods and services)		340.3	82.9	4.3	0.8	5.1	4.3	**3.7**	**3.9**	**4.4**
Imports (goods and services)		333.4	81.3	4.1	0.3	5.9	4.3	**2.9**	**3.9**	**4.4**
GNI (GDP deflator)		410.5	100.0	1.9	-0.8	0.5	1.0	**1.3**	**1.3**	**1.5**
Contribution to GDP growth:	Domestic demand			1.6	0.1	1.8	1.2	**1.2**	**1.2**	**1.4**
	Inventories			0.1	-0.6	0.4	0.3	**-0.6**	**0.0**	**0.0**
	Net exports			0.3	0.4	-0.6	0.0	**0.6**	**0.1**	**0.1**
Employment				1.0	-0.3	0.4	0.9	**1.2**	**0.9**	**1.0**
Unemployment rate (a)				7.9	8.4	8.5	8.5	**8.0**	**7.8**	**7.6**
Compensation of employees / head				2.6	2.5	1.0	0.0	**0.8**	**1.9**	**1.8**
Unit labour costs whole economy				1.7	2.2	-0.2	-0.5	**0.7**	**1.5**	**1.2**
Real unit labour cost				0.0	1.0	-0.9	-1.4	**-0.6**	**-0.1**	**-0.5**
Saving rate of households (b)				15.8	12.3	12.1	11.7	**12.7**	**12.1**	**12.2**
GDP deflator				1.8	1.2	0.7	0.9	**1.3**	**1.6**	**1.7**
Harmonised index of consumer prices				2.1	1.2	0.5	0.6	**1.7**	**1.7**	**1.8**
Terms of trade goods				-0.6	0.4	1.0	1.8	**-0.1**	**-0.5**	**-0.1**
Trade balance (goods) (c)				1.7	-0.7	-0.7	0.3	**0.0**	**-0.5**	**-0.5**
Current-account balance (c)				3.5	1.1	-0.1	0.2	**0.6**	**0.6**	**0.6**
Net lending (+) or borrowing (-) vis-a-vis ROW (c)				3.5	1.0	-0.4	0.2	**0.5**	**0.7**	**0.7**
General government balance (c)				-1.7	-3.0	-3.1	-2.5	**-3.0**	**-2.3**	**-2.4**
Cyclically-adjusted budget balance (d)				-1.9	-2.1	-2.6	-2.3	**-2.8**	**-2.0**	**-2.2**
Structural budget balance (d)				-	-2.7	-2.9	-2.6	**-2.7**	**-2.0**	**-2.2**
General government gross debt (c)				102.8	105.4	106.5	105.8	**107.0**	**107.1**	**106.4**

(a) as % of total labour force. (b) gross saving divided by gross disposable income. (c) as a % of GDP. (d) as a % of potential GDP.