

Belgium: Political situation remains murky

As the overall economic context darkens, the Belgian economy continues to grow at a moderate pace. After elections in May, the process of forming a new government will take a while and that will prevent any policy action this year



The interim Belgian Prime Minister, Charles Michel, voting in May's elections. A government still hasn't been formed.

Slower growth

Considering the 1.2% year-on-year growth in the first quarter of this year and the creation of nearly 19,000 new jobs, we really can't say the Belgian economy is not doing well. However, we are convinced that the growth momentum remains unsatisfactory.

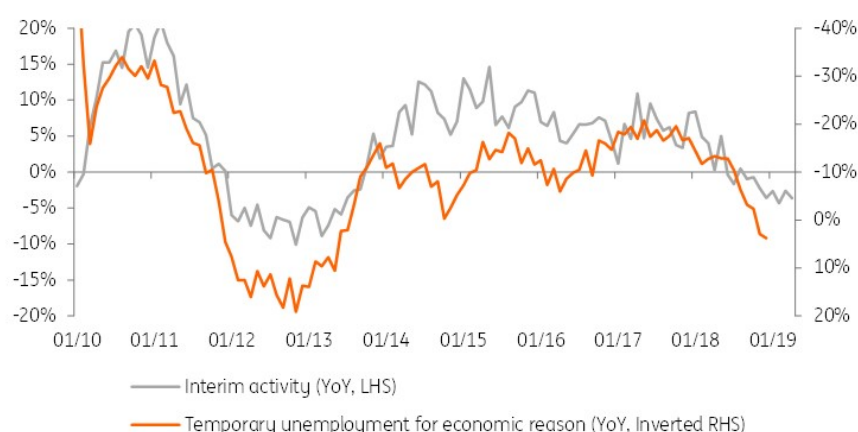
Real growth in household consumption remains particularly weak. Over a year, it only grew by 0.4%. Strong job creation helped to support household disposable income (it increased by 3.8% in 2018). However, relatively high inflation (2.1% in 2018) erased a large part of this growth. In addition, the decline of household confidence was reflected in a slight increase in the savings rate, to the detriment of consumption growth.

Corporate confidence is declining

Despite an investment dynamic that remains positive (corporate investment grew by 2.9% last year in real terms), companies active in foreign markets seem to be feeling the effects of slowing growth in the eurozone economy and of global trade tensions. As a result, corporate confidence is declining, especially in the manufacturing sector, which has the most exposure to global trade.

Lower confidence among managers in a context of economic slowdown and trade and geopolitical tensions are expected to maintain this subdued growth momentum. To be sure, economic indicators remain compatible with positive economic growth, but that should be limited to 0.2% to 0.3% per quarter. In this context, it is unlikely that job creation will remain as dynamic as it has been in the past three years. Indeed, one can observe a decrease of nearly 4% of activity in the temporary work sector over the last year. Similarly, temporary unemployment for economic reasons has increased by 4% over the same period. As these are two leading indicators of the labour market, job creation will at best offset the increase in the labour force, which should stabilise the unemployment rate at the current level (around 6%).

Leading indicators of the Belgian labour market aren't looking that great

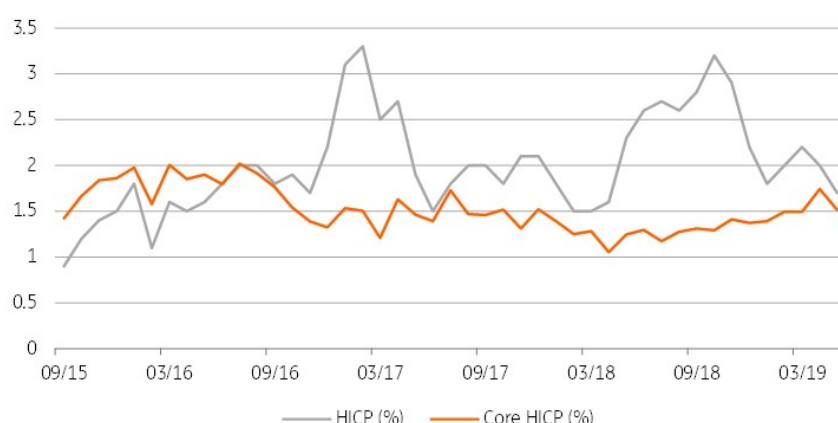


Source: NBB, ING

The inflation conundrum

In terms of inflation, two elements must be noted: first, general inflation remains above the average of the euro area, and it's been like this since 2015. No single element can explain this phenomenon. It is more a combination of elements, including a lack of competition in some sectors, but also probably the automatic wage indexation that pushes business costs up. Secondly, it should be pointed out that underlying inflation is creeping up slowly and reached 1.5% in May 2019. At the beginning of 2018, it was limited to 1.1%

Core inflation is seemingly gaining traction



Long negotiations in sight

A month after the federal and regional elections, the country's political situation remains murky. At the federal level, consultations between political parties are ongoing with complete discretion, and no majority or even the beginning of negotiations between different parties seem to be taking shape. Political parties seem to be waiting for the situation to clear up at the regional level before moving forward at the national level. The opposite scenario would have been worse: the negotiations were likely to go in opposite directions at national and regional levels, which could have created a complete blockage.

At that regional level, the process of forming majorities is likely to take time, except in the Brussels region, where negotiations between the PS (Socialists), Ecolo (Greens) and Défi (centre of the political spectrum, with a focus on defending the interests of French-speaking people) have begun.

We're not really expecting a working government in Belgium before the second half of this year

In the other two regions (Flanders and Wallonia) majorities could easily be formed. But it would not really take into account some signals sent by voters during elections. Therefore, the dominant parties are exploring other ways:

In Flanders, while the majority previously in place could be renewed, the sharp increase of the Vlaams Belang (extreme right-wing party and Flemish nationalist) electoral score disturbs the process of seeking a majority. Therefore, the discussions between the parties are prolonged. Although the likelihood of Vlaams Belang's accession to the next government remains very low, the party is currently associated to the talks.

In Wallonia, two parties have up to now been excluded from the discussions: the Cdh (at the centre of the political spectrum, which decided to withdraw from the discussions) and the PTB (far left party). The only possible majority is, therefore, an alliance between the PS and the MR (liberals), to which could be added Ecolo. Nevertheless, Ecolo wishes to avoid any alliance with the MR.

Discussions are therefore continuing only between the PS and Ecolo, with a view to forming a regional minority government. However, this scenario has little chance of success.

We need to be patient, again

Given the constraints and requirements of the various parties, in our view, the scenario which looks the most probable remains an alliance between the N-VA (nationalist), the VLD (liberals) and the CD & V (center) in Flanders (renewal of the previous majority) and an alliance between the PS, the MR and Ecolo in Wallonia. These majorities would pave the way for a federal majority composed of all these parties with the exception of Ecolo. But again, given the signals by voters, the formation of such majorities will take time.

So, we're not really expecting a working government in Belgium before the second half of this year. As the 2020 budget has to be negotiated in October, this means no change will be made to the budget of 2019. So we should expect nothing in terms of economic policy and budget effort this year. Nevertheless, the public deficit is expected to be limited to 1.4% of GDP, which would be more than enough to reduce the debt ratio below 100% of GDP this year.

For next year, budgeting will depend heavily on the composition of the government, but it's worth noting that no political party included in the current discussions wants to deviate from European budgetary rules, which should maintain a strict framework for further budget negotiations, especially given the fact that without any corrective measure the deficit is expected to rise again in 2020.

This article is taken from the Eurozone Quarterly, which you can find [here](#)

The Belgium economy in a nutshell (%YoY)

| | 2018 | 2019F | 2020F | 2021F |
|----------------------------|------|-------|-------|-------|
| GDP (%) | 1.4 | 1.0 | 1.0 | 0.9 |
| Private consumption (%) | 1.0 | 0.6 | 1.1 | 1.1 |
| Investment (%) | 2.9 | 3.2 | 1.3 | 0.8 |
| Government consumption (%) | 0.9 | 0.7 | 1.2 | 1.5 |
| Net trade contribution (%) | 0.3 | 0.3 | 0.4 | 0.0 |
| Headline CPI (%) | 2.1 | 1.8 | 1.7 | 1.6 |
| Budget balance (% of GDP) | -0.7 | -1.4 | -1.4 | -1.5 |

Source: NBB, ING estimates

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