What is wrong with Belgian growth?

Current Belgian GDP growth is disappointing even though other economic variables point to a strong expansion. What's behind the growth puzzle?

The catch-up effect

Belgian GDP growth has been below the Eurozone average over the past 6 quarters (with one exception in Q1 2017). To be sure, part of this underperformance can be explained by a catch-up effect: other EZ countries, and particularly from the South, encountered a deep recession in 2008-2010 and in 2012-2014. So it is quite normal that these countries (like Spain) outperform in the recovery period, pushing up the Eurozone average. Measured since the start of the crisis, Belgian GDP is still about 2% higher than the Eurozone average.

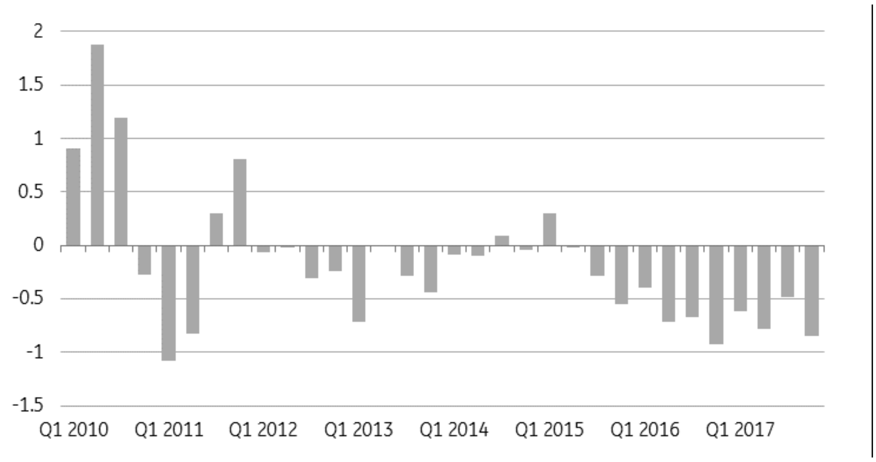
Having said that, there is probably more to say about the current relative underperformance of the Belgian economy. Indeed, if Belgian GDP growth appears to be below the EZ average, it remains also below its previous standard, and particularly at this stage of the cycle. In the recovery part of the cycle, growth levels between 2 ¼ % and 2 ¾ % should be observed. So, why is it this time different?

Puzzling relations

It is also remarkable to note that many other economic variables are pointing to a strong economic expansion that isn't reflected in the GDP growth figures. As a consequence, some structural relations between economic indicators and GDP growth are temporarily not working. Or maybe they are just obsolete.

First, business confidence that in the past has been the best proxy for activity growth in Belgium is currently at levels that would justify a stronger GDP growth (figure1).

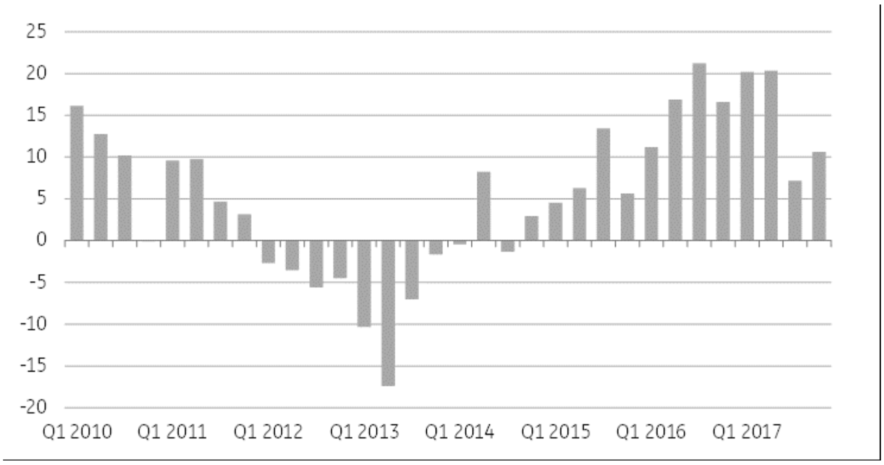
Figure 1: Difference between effective GDP growth (YoY, in percentage point) and calculated growth based on ING model.



Source: Source: NBB, computation: ING

Second, as there is a close link between economic activity and employment (called the Okun's law), it is possible to compute what is the theoretical level of employment growth associated with any level of GDP growth. However, over the last two years, jobs creation has been systematically higher than what could be modelled (figure2).

Figure 2: Difference between effective job creation (YoY; ,000) and calculated through ING Okun's law.



Source: Source: NBB; computation: ING

So, what is wrong?

There are several elements to explain the growth puzzle in Belgium:

1. It could just be a temporary effect, due to a negative contribution of inventories, or another statistical effect.
2. The efforts made by the government in order to decrease the budget deficit (what is often called “austerity”) could play a role. That said, this explanation would also imply some impact on business and consumer confidence or employment, which is not the case. So it could play only a minor role.
3. More importantly, the answer could be in private consumption. Strong employment growth has increased real disposable income of households, but without any strong impact on consumption. On the other hand, because of the saving surplus of Belgian households, Belgium benefits less from the low interest rate environment than other countries. The Belgian National Bank actually linked the decline of the saving ratio with falling interest income from financial wealth. Households might now prefer to stabilise or even to increase their saving ratio. This could explain why, in a period of economic recovery, strong job creation and high confidence, private consumption is so weak. It would then be good news, as this phenomenon is only temporary and guarantees that the financial fundamentals of the Belgian economy remain sound.
4. In fact, there is a fourth possible explanation: maybe the basic relations between economic variables, computed on the period 1995-2013, are not valid anymore. We might have to re-consider structural relations as economies enter a new world: the potential growth of the economy has maybe changed, affecting “old” relations. The GDP computation itself is maybe incorrect, as it has difficulties in capturing the e-commerce activity or the platform economy. But if this were true, why is it only the case in Belgium?

To conclude, more data and more time will be needed to better explain why Belgian GDP growth shows such a troubling pattern. We highlighted here some explanations, with a focus on consumption that at this stage seems to play an important role. Even if this effect is temporary, one has to consider that in 2018, once again, Belgian GDP growth is likely to be below the EZ average.

The National Bank of Belgium has linked the decline of the savings ratio with declining interest income from financial wealth (in French):

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