BELGIUM

STEADY GROWTH, REAL ESTATE TO RECOVER

Belgian economic growth remains close to trend rates, even as a shift in the underlying drivers is taking place. Corporate investment rebounded from last quarter's one-off dip. More encouraging is the bottoming-out of household investment in dwellings. Real estate prices have remained on an upward trend throughout the ECB's now ended hiking cycle and the depressed activity levels are expected to slowly recover. Public finances remain a challenge, as the spectre of prolonged government formation talks once again casts a shadow over the Belgian economy.

First quarter GDP growth was recently confirmed to have been 0.3% q/q. Besides private consumption, usually the engine of growth, corporate investment rebounded, after its Q4 dip (offset by a related improvement in the trade balance, both the result of transactions in the maritime sector). Another positive sign is that household investment also contributed to overall growth for the first time in more than a year, even if total expenditure in this category remains 13% below pre-COVID levels. With the labour market gradually cooling off and inflation expected to resume declining – after topping the EU27-charts recently – we anticipate an increased appetite for private real estate. Additional rate cuts by the ECB could further speed up the pending recovery of activity levels in the real estate market.

BETTER NEWS ON THE REAL ESTATE MARKET

As in the neighbouring countries, Belgian real estate prices accelerated further during the COVID-19 crisis, albeit at a more gradual pace than in Germany and the Netherlands. Up until the ECB's first rate hike, in mid-2022, housing price growth had in fact been in excess of the historical average of about 4% per year. To quantify a possible pending market correction, we simulated a shock of six consecutive housing price declines of a magnitude only experienced in 5% of all quarters between 1973 and 2020. Yet even in this quite negative scenario, prices would only drop back to their 2021 levels, indeed a quite modest correction. Now, almost two years later, housing price growth has surprised even more on the upside. In fact, since the start of the ECB's hiking-cycle, housing prices have barely deviated from their long-term trend. However, activity levels did drop significantly.

The National Belgian Bank reports a decline of about 20% in secondary transactions throughout 2023. The increased interest rates pushed the NBB's metric for housing affordability to an all-time (expensive) record level, which offers some explanation for this dip. However, the decline in transactions is likely also related to a recent regulatory change. As of January 2023, dwellings carrying a poor energy performance certificate are mandated to be renovated within five years of purchase. Anecdotal evidence suggests that the housing price dip in late 2022 was related to a large influx of this type of property, aiming for a quick sale to help the buyer steer clear of the new requirements. In parallel, the number of new mortgage credits actually declined even faster than the activity levels in the market. In 2023, there were almost 30% fewer new housing loans. The number of building permits also declined during this period.

Now, in early 2024, the first positive signs are appearing. The NBB recently reported interest rates on new mortgages of an average 3.23% for maturities of at least 10 years, down from the December 2023 peak of 3.6%. Household sentiment has recovered from its double COVID/energy dip and the unemployment rate has only marginally increased, as a soft landing on the labour market lurks. Furthermore, nonperforming loans are stable and household debt continues its downward trajectory, evidencing the relative stability of real estate market throughout the rate cycle. Over the short term, we expect housing price growth at around the trend pace as activity levels on the market gradually pick up again.

GROWTH AND INFLATION

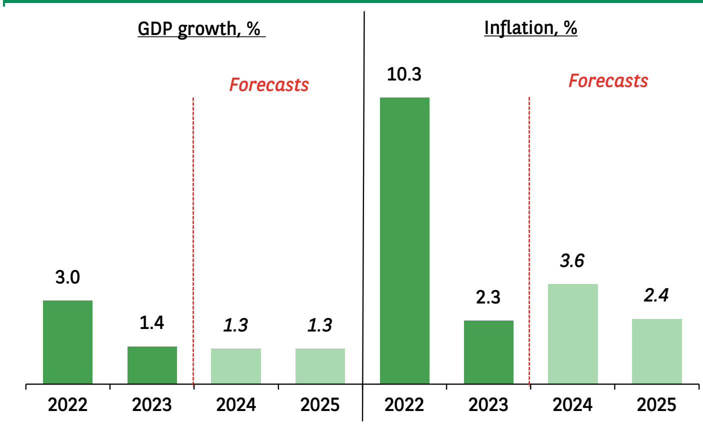

CHART 1

SOURCE: BNP PARIBAS FORTIS, BNP PARIBAS

PUBLIC FINANCES REMAIN A CHALLENGE

Households and firms seem to have weathered the impact of higher rates quite well. But this is not the case for public finances. One-off expenditures like COVID-19 and energy-bill support appear to have pushed the deficit structurally higher. Despite the Belgian Debt Agency's best efforts to tie in low rates for longer, average yields on outstanding government debt started to creep up again already in 2022. At the beginning of this year, yields stood at 1.92%, almost 50 bps above their low point in 2021. Average maturity was almost 11 years. As a result, yearly debt servicing charges are picking up. Having bottomed out at 1.2% of GDP in 2022, interest paid on outstanding debt could be double that by 2025. The popular one-year bond emitted last year, encouraged by fiscal support, could be interpreted as a sign of strong market demand for Belgian debt, but too much optimism seems unwarranted, especially as a stubborn deficit and rising (rather, no longer falling) interest rates conspire to push government debt ever higher. The interest rate snowball is indeed in full swing: the debt ratio could top 110% by 2026. Fiscal consolidation will be a key-priority for a yet-to-be-formed government, as a European budget reprimand looms large.

Belgian GDP cumulatively outgrew the Euro Area by about 1% since the start of 2022. True to type, the economy overperformed during rough times, at least partially due to significant government intervention. This is a two-part act: Belgian growth, close to trend, will be outpaced by most other European countries over the short term, especially as rates decline further. Inflation, meanwhile, is normalising but still in excess of almost all other EU-member countries. Core inflation, spurred by subsequent wage indexation, is one culprit, higher energy-price sensitivity is another.

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