PRIVATE CONSUMPTION: AN UMBRELLA FOR THE COMING STORM

Belgian GDP remains on a positive growth trajectory, even as monetary-induced clouds are forming. The historically large wage-indexation that benefitted a significant number of workers at the start of the year should spur on consumption in the short run. With disappointing corporate and household-real estate investments, and international trade decreasing, government spending is the only other positive contributor to growth, making for unsustainable public finances.

The Belgian economy surpassed expectations by growing 3.1% across 2022. However, after a strong first semester, the year's third and fourth quarter did entail a slowdown, as was the case in most large European economies. What sets the Belgian economy apart is its automatic wage-indexation, which results in regular wage hikes whenever inflation crosses a certain threshold. At the current juncture, large wage indexation is taking place, just as average inflation starts to decline. This bodes well for private consumption.

This should be enough to offset a slowdown in most other components of GDP. The balance of risks, chief amongst them the harder-than-expected monetary tightening, remains tilted firmly to the downside.

GROWTH & INFLATION

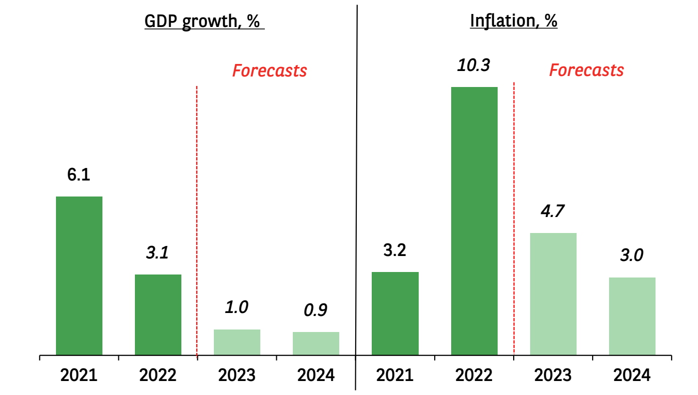

CHART 1 SOURCE: NATIONAL ACCOUNTS, BNP PARIBAS FORTIS

INFLATION DROPPED BELOW 6%

Inflation on a yearly basis, as measured by the HICP, came in at 5.5% for February. In doing so, it dropped below 6% for the first time in 16 months. In fact, the average price level has declined by almost 3% from its October peak.

This reflects a break in the underlying mechanics. Since January, energy-driven price pressures are no longer the largest contributor to headline inflation. Meanwhile, food prices have been surging, increasing on average by 1.2% every month since the start of 2022. It is also concerning that core inflation continues to accelerate.

HOUSEHOLDS ARE LESS WORRIED

Consumer confidence continues its recovery from October's low-point. Households are now less worried about employment loss, with the unemployment rate hovering just below 6% for the last three years.

Slower, but still strong employment growth and the above-mentioned wage-indexations spur on income growth. The Federal Plan Bureau expects real disposable income to increase by 4.2% in 2023.

If the current trends prevail, private consumption could accelerate over the next four quarters. The strong real income growth reminds us of early 2009. If household spending follows a similar trajectory as in the wake of the global financial crisis, it could mean a bonus of one percentage point for total GDP.

Such a bonus would help offset the turning tide Belgian firms are now facing. A tight labour market, still elevated input prices and more restrictive financing conditions conspire to lower profit margins.

Business confidence is recovering from last year's dip, but clearly at a slower pace than consumer sentiment. Retailers and manufacturers are increasingly worried about their outlook. Overall, gross fixed capital formation by firms has shown little signs of a revival over the last two quarters.

PUBLIC FINANCES

Government consumption is now slowing down from its 2021 peak, when health-related expenditures picked up from their pandemic low. Investment spending should increase markedly throughout 2023, as defense spending shoots up and local governments gear up for the 2024 elections.

Against the backdrop of rising interest rates, government debt remains a big worry. In its most recent publication, the IMF strongly recommends imposing fiscal adjustment at the sub-national level as part of the general government's consolidation plans, and they further recommend strict spending limits and internalising the cost of overborrowing on the regional level.

It remains to be seen to what extent Alexander De Croo's broad coalition of governing parties will do as the doctors prescribe.

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