Economic projections for Belgium – Autumn 2009

Introduction

After the global economy had suffered the harshest recession of approximately the last sixty years, signs of recovery have multiplied in the course of 2009. Business and consumer confidence has picked up significantly since the spring, while industrial production and international trade – the two aspects which had suffered the most marked decline at the end of 2008 and beginning of 2009 – have stabilised or risen slightly in the main economic regions.

This revival of activity, borne along by the twin factors of economic policy measures and more technical factors, has appeared a little earlier than expected. While the financial crisis had strongly aggravated the slowdown in business activity, fears of a collapse in the financial system abated in the course of 2009 as the determined and massive action of monetary authorities and governments took effect. These fears gradually gave way to a renewed appetite for risk in the positioning of investors. Central banks also maintained their key rates at very low levels in the context of weak inflationary pressure. Furthermore, stimulus-oriented budget plans implemented in the majority of the advanced economies, but also in the emerging countries, gave a far-reaching impetus to the economy. Apart from this, the generalised running-down of inventories – which was a clear sign of the search for liquidity among firms after the financial crisis intensified, paralleling that pursued by the financial institutions – appears to be coming to an end.

It is now thought that, in general, GDP resumed a growth path from the third quarter of 2009, whereas six months ago, the first phase of recovery was only forecast to arrive in the course of 2010. However, there are still serious doubts as to whether the upturn will last beyond the next two quarters, since the impetus from economic policy should tail off and the contribution to growth connected to movements in inventories is temporary by nature. Over and above this, firms and private individuals in the advanced economies, and more particularly in Europe, must adapt themselves to the substantial fall in the level of activity and incomes. These adjustments are expected to continue to weigh on investment, employment and consumer spending for some time.

This is the setting – better than in the spring but nonetheless still very uncertain – in which the updates to the macroeconomic projections for 2009 and 2010, carried out as part of the six-monthly exercise for the Eurosystem, are taking place. The results for the whole area are published in the ECB's Bulletin for December 2009; they indicate that GDP will increase in 2010, albeit at a modest pace, after plummeting by around 4 p.c. this year, while inflation will remain low.

According to the flash estimate from the NAI, GDP in Belgium rose by 0.5 p.c. in the third quarter of 2009 after showing a cumulative decline of more than 4 p.c. during the previous twelve months. This result confirms the expected improvement in short-term prospects and consequently the upward revision of growth projections compared to the results published in June [1]. This contrasts sharply with the very rapid and very substantial downward revisions made over the course of twelve months during successive economic forecasting exercises. On the other hand, the current projections still include a substantial rise in unemployment and a considerable deficit in public finances, while inflation is expected to remain moderate.

(1) The previous version of the economic projections for 2009 and 2010 was presented in more detail in the spring, in the Bank's June 2009 Economic Review.

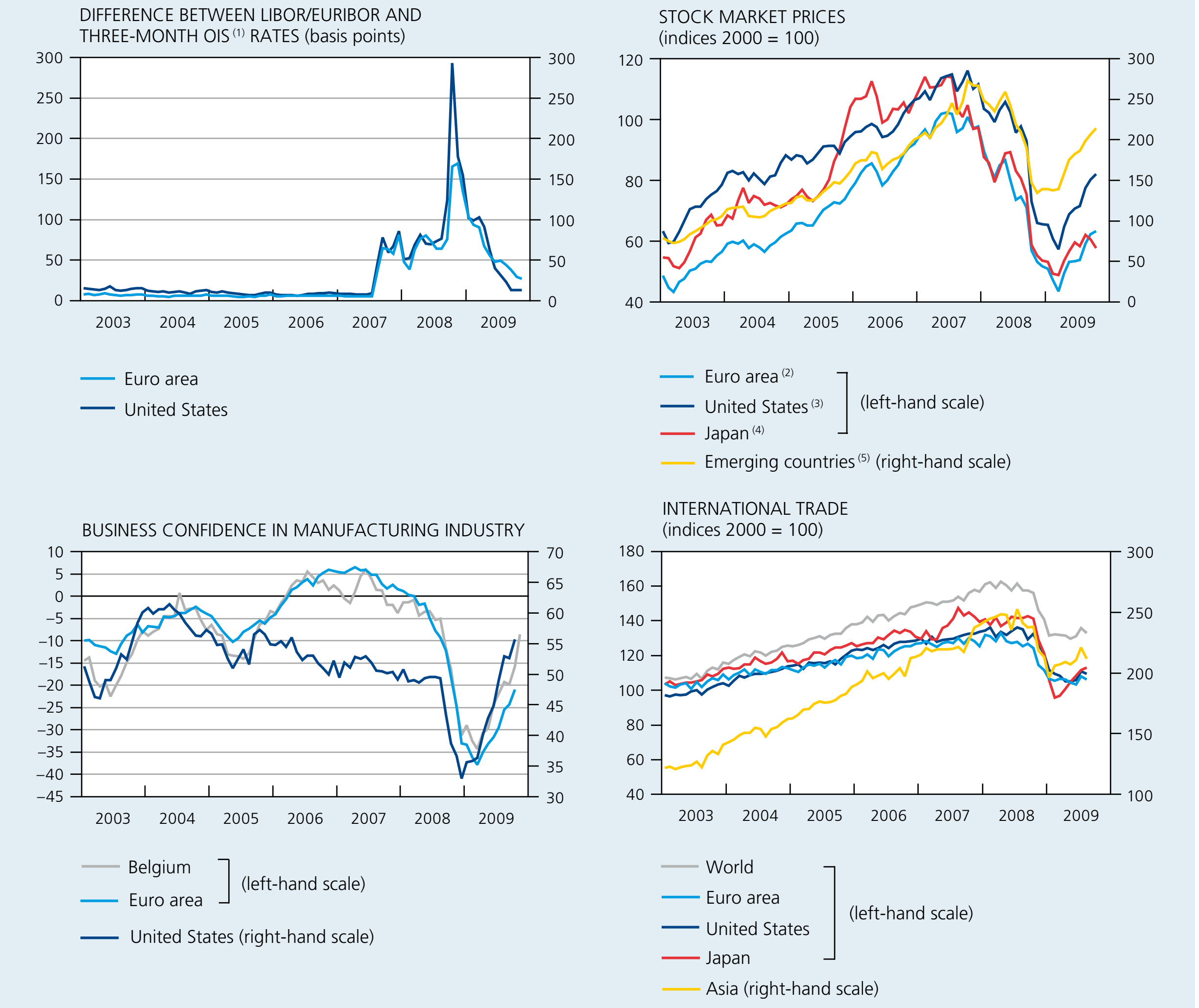
The results presented briefly in this article incorporate the information available as at 20 November 2009. They were compiled on the basis of assumptions common to the Eurosystem, the principles of which are described in the box included in the first section. As is usual in the case of public finances, these projections only take account of measures formally approved by the authorities, particularly for the 2010-2011 federal budget and the 2010 budgets of the Communities and Regions, on which sufficient detail is available.

1. International environment and assumptions

Paralysed by the distinct worsening of the financial crisis and other factors, international trade in goods collapsed by almost 20 p.c. at the end of 2008 and beginning of 2009, very quickly plunging the advanced economies and most emerging economies into a generalised and very deep recession. In the second quarter of 2009, United States GDP expressed in real terms fell by 3.8 p.c.

CHART 1 DEVELOPMENTS ON THE FINANCIAL MARKETS, BUSINESS CONFIDENCE AND INTERNATIONAL TRADE

(monthly averages)



Sources: Bloomberg, CPB, HWWI, Thomson Reuters Datastream.

(1) Fixed rate paid by the party receiving the overnight rate (Eonia for the euro area, actual federal funds rate for the US) in a three-month interest rate swap.

(2) Dow Jones Euro Stoxx Broad index.

(3) Wilshire 5000 index.

(4) Topix index.

(5) MSCI Emerging Markets Index.

compared to the corresponding period of the previous year. The decline reached 4.8 p.c. in the euro area and 5.5 p.c. in the United Kingdom respectively, while it amounted to 8.4 p.c. in Japan in the first quarter. While most economies suffered serious effects, therefore, the scale of the decrease in activity varied from one region to the next, depending on the importance of foreign trade (this having been the main channel through which the recession spread), exposure to the financial sector and, in some cases, the bursting of a bubble in the real estate sector.

From the second half of 2009 onwards, however, the unprecedented measures taken on both sides of the Atlantic to prevent a financial system meltdown and the extremely flexible monetary and budgetary policies quickly put into place in most economies began to produce their effects.

On the one hand, financial tensions gradually eased under the combined impact of government guarantee mechanisms and injections of capital for the benefit of the financial institutions, and also generous grants of liquidity which the central banks took steps to provide. On the money markets, the gap between unsecured interbank deposit rates and those for risk-free investments, which had reached a peak in October 2008, returned to a level comparable to that prevailing prior to the failure of Lehman Brothers. A similar decline in spreads was seen for corporate and government bonds, as investors began to consider moving back into higher-risk investments, whereas they had frantically sought security and liquidity at the height of the financial crisis. On the main stock markets, share prices similarly began an upward movement; in rebounding by around 50 p.c. with reference to their lowest point reached in the course of March 2009, they recovered 30 p.c. to 50 p.c. of the losses suffered during the crisis.

On the other hand, business confidence picked up, in some cases strongly, when it became apparent that the rapid fall in activity had ceased against a background where central banks had maintained their key rates at very low levels since the start of the year and where measures taken by governments were on a massive scale. These stimulus measures took various forms in the United States and Europe, notably the speeding-up of public investment, the easing of taxes and even a helping hand for private investment or the purchase of motor vehicles, the automobile sector having been hit particularly hard by the recession. Emerging countries also implemented measures on a large scale; spending on infrastructure increased strongly in China, for instance.

With government support, rising demand helped to put an end to the process of running down inventories, which had been observed since the end of 2008. This development contributed to a revival in international trade, mainly under the impetus of China and other Asian countries; the recovery remains fragile, however, in the light of the scale of the drop which preceded it. Alongside these initial signs of strengthening demand, prices for raw materials on the international markets similarly picked up from spring 2009 onwards. In particular, the price of a barrel of Brent crude oil, which had fallen from a maximum of around 145 US dollars in July 2008 to about 40 US dollars in December, rose once again to about 80 US dollars in mid-November 2009.

Overall, the trend in activity in 2009 is still mainly dominated by the major recession which was rife at the end of 2008 and beginning of 2009. According to the autumn forecasts from the EC, global GDP is predicted to decrease by 1.2 p.c. in volume terms as an annual average, which would represent the first generalised contraction in activity since the Second World War. Among the large economic areas, GDP is forecast to decline by 2.5 p.c. in the United States, 5.9 p.c. in Japan and 4.1 p.c. in the European Union as a whole; only China and India are expected to maintain positive growth.

The improvement in the environment during the second part of 2009 would put the global economy in a better position in 2010. Consequently, the forecasts point to renewed positive growth in GDP in most areas. This is expected to remain limited, however, since the effects of factors at the root of the recovery underway are temporary in nature and set to tail off rapidly, while elements which should take over and stoke this recovery in a lasting manner are still fragile. Thus, there still seems to be a generous surplus of production capacity, which is directly damping down business investment and, due to the anticipated continuing rising unemployment, consumer spending too. In this situation, following an average decline of almost 13 p.c. in 2009, global trade is only expected to rise by a little over 3 p.c., a rate markedly down on that seen prior to the crisis. As for inflationary pressures, these are expected to remain limited.

By recording a rise in volume of 0.4 p.c., the euro area also returned to positive GDP growth in the third quarter of 2009, after five successive quarters of decline. As in the other advanced economies, this turnaround is based not only on strengthening foreign demand, notably that emanating from Asia, but largely on the effect of support measures announced by governments and on the cyclical movement in changes in stock levels. It has come earlier than previously anticipated so the updated projections for

TABLE 1 PROJECTIONS FOR THE MAIN ECONOMIC AREAS

(percentage changes compared to the previous year, unless otherwise stated)

	2008	2009	2010
	Actual	Projections	
GDP in volume			
World	3.1	–1.2	3.1
of which:			
United States	0.4	–2.5	2.2
Japan	–0.7	–5.9	1.1
European Union	0.8	–4.1	0.7
China	9.7	8.7	9.6
India	6.7	5.7	6.4
Russia	5.6	–7.2	2.3
Brazil	5.1	–0.4	4.2
p.m. World imports	*3.4*	*–12.9*	*3.2*
Inflation (1)			
United States	3.8	–0.5	0.8
Japan	1.4	–1.2	–0.4
European Union	3.7	1.0	1.3
Unemployment rate (2)			
United States	5.8	9.2	10.1
Japan	4.0	5.8	6.3
European Union	7.0	9.1	10.3

Source: EC (autumn forecasts, November 2009).
(1) Consumer price index.
(2) Percentages of the labour force.

the Eurosystem assume a less pronounced drop in GDP for 2009 than the exercise carried out last June and even the interim exercise by the ECB, the results of which were published at the beginning of September. According to the new projections, GDP in the euro area as a whole is forecast to decline at a rate between -4.1 p.c. and -3.9 p.c. in 2009. The improved prospects in terms of activity for the end of the year similarly give rise to an upward revision in the growth envisaged for 2010. This is forecast to remain limited, however, at a level between 0.1 p.c. and 1.5 p.c.

The tentative nature of the recovery is due to the modest hardening of demand both outside the euro area, an issue referred to above, and domestically. In particular, investment by firms should shrink further in 2010 as a result of low levels of production capacity utilisation and falling profitability. A continuation of the adjustments taking place in real estate markets in various countries in the euro area should also lead to a decline in investment in housing. And the rise in consumer spending would be damped down by the expected deterioration in the labour market. While extending certain measures aimed at reducing working hours within firms initially actually softened the impact of the recession on employment in some countries, the adjustment should continue in 2010, giving rise to further growth in unemployment.

Overall inflation in consumer prices, for its part, has been in negative territory since June 2009 in the euro area, as a result of major underlying effects linked to the fall in raw materials prices compared to the previous year. As the impact of these factors rapidly tails off, and even reverses under the effect of the recent oil price

TABLE 2 EUROSYSTEM PROJECTIONS

(percentage changes compared to the previous year)

	Euro area			*p.m. Belgium*		
	2008	2009	2010	*2008*	*2009*	*2010*
Inflation (HICP)	3.3	0.3 / 0.3	0.9 / 1.7	*4.5*	*0.0*	*1.6*
GDP in volume	0.5	–4.1 / –3.9	0.1 / 1.5	*0.8*	*–3.1*	*1.0*
of which:						
Private consumption	0.4	–1.2 / –1.0	–0.2 / 0.8	*1.0*	*–1.6*	*0.8*
Public consumption	2.0	2.2 / 3.0	0.5 / 1.7	*3.3*	*2.2*	*1.1*
Investment	–0.6	–11.3 / –10.5	–3.1 / –0.1	*3.8*	*–4.1*	*–1.3*
Exports	0.8	–14.5 / –12.5	0.6 / 5.6	*1.4*	*–12.1*	*3.0*
Imports	0.9	–12.6 / –11.0	0.4 / 4.6	*2.7*	*–11.5*	*2.7*

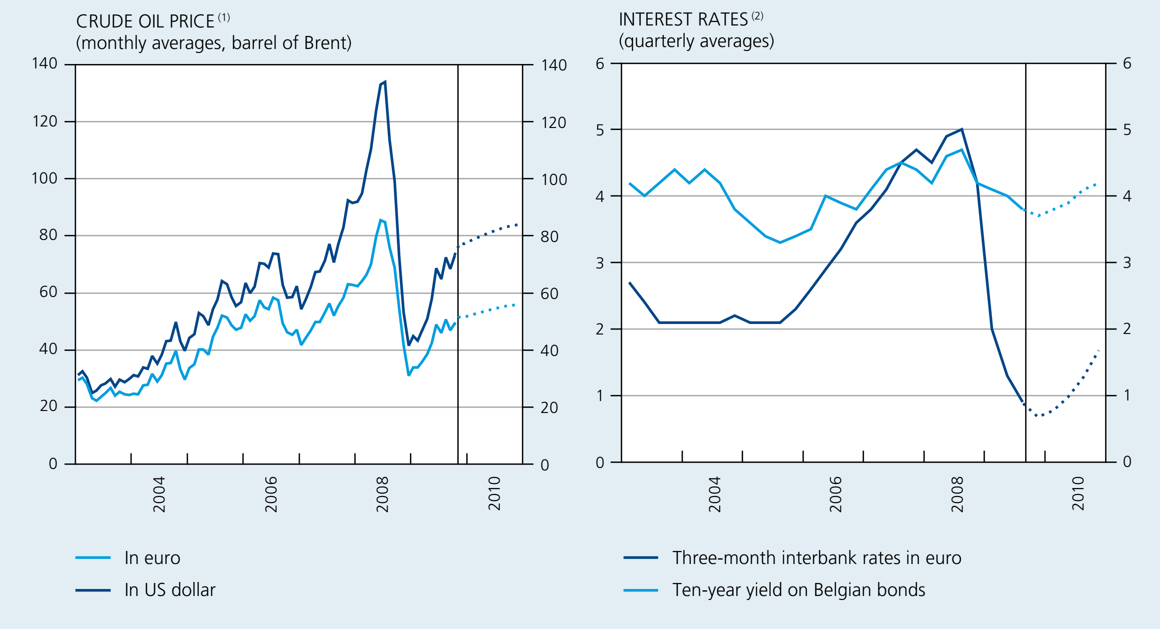
Sources: ECB, NBB.

Box – Eurosystem assumptions

The Eurosystem's economic projections for the euro area and the Bank's corresponding projections for Belgium are based on the following technical assumptions:

- the interest rates are based on market expectations. As an annual average, the three-month interbank deposit rate is forecast to fall from 4.6 p.c. in 2008 to 1.2 p.c. in 2009 and 2010. The yield on ten-year Belgian government bonds is projected at 4.4 p.c. in 2008, 3.9 p.c. in 2009 and 4 p.c. in 2010. As noted above, after widening markedly during the financial crisis, the spreads between these reference yields and those applicable to firms and households generally fell back to a level comparable to that applying previsously;
- bilateral euro exchange rates are kept constant at the level reached in mid-November 2009, namely 1.49 US dollar to the euro. This represents a gain of almost 7 p.c. compared to the average level in 2009;

ASSUMPTIONS CONCERNING THE MOVEMENT IN OIL PRICES AND INTEREST RATES



Source: ECB.
(1) Actual figures up to October 2009, assumption from November 2009.
(2) Actual figures up to the third quarter of 2009, assumption from the fourth quarter of 2009.

- in accordance with the movement in implicit prices reflected in forward contracts, international market prices for a barrel of Brent crude oil are expected to average 62.2 dollars in 2009 and 81.4 dollars in 2010, against 97.7 dollars in 2008;
- relevant export markets for Belgium, measured as the weighted total of imports of the trading partners, including those in the euro area, are only likely to rise by 3.6 p.c. in 2010, after falling almost 11 p.c. in 2009. Given this background, and in view of the appreciation of the euro, prices among competitors on export markets are projected to decrease by 3.7 p.c. in 2009 and 0.6 p.c. in 2010;
- as is usual according to the Eurosystem conventions, the figures for public finances take account of the macroeconomic environment and budget measures which have already been announced and have been specified in sufficient detail.

ASSUMPTIONS UNDERLYING THE EUROSYSTEM PROJECTIONS

	2008	2009	2010
		(annual averages)	
Three-month interbank rates in euro	4.6	1.2	1.2
Ten-year bond yields in Belgium	4.4	3.9	4.0
Euro exchange rate against the US dollar	1.47	1.39	1.49
Oil price (US dollar per barrel)	97.7	62.2	81.4
		(percentage changes)	
Export markets relevant to Belgium	2.1	–10.9	3.6
Competitors' export prices	2.4	–3.7	–0.6

Source: ECB.

increase on international markets, inflation should turn positive again as from the end of the year and remain so throughout 2010. The forecast is for it to remain at low levels, however, in a scenario of persistent weakness in demand and deterioration of the labour market. According to the new Eurosystem projections, inflation is predicted to lie within a range between 0.9 p.c. and 1.7 p.c. in 2010, after reaching around 0.3 p.c. on average in 2009.

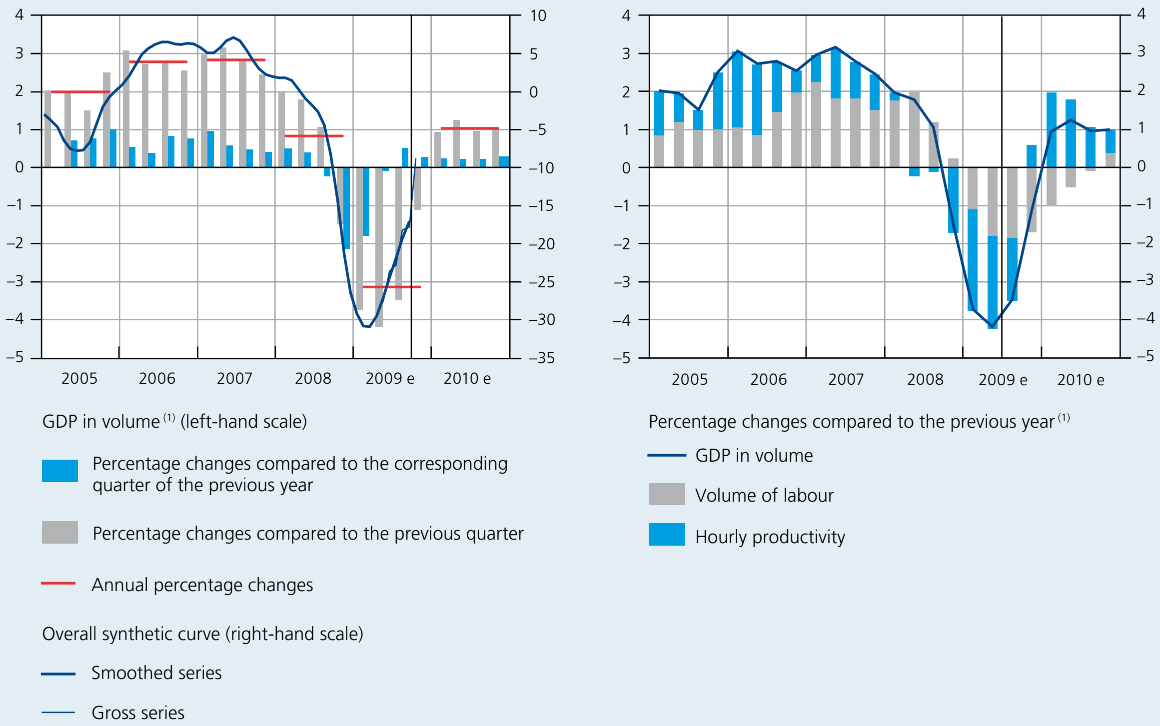
2. Activity, employment and demand

According to the flash estimate from the National Accounts Institute, GDP in Belgium rose by 0.5 p.c. in the third quarter of 2009 after showing a decline for four successive quarters. Having felt the effects of the recession most intensely at the end of 2008 and beginning of 2009, like the euro area as a whole, Belgium moved out of it at the same time as the latter. This parallel development is the direct result of the very close ties uniting Belgium with its partners in the euro area, in particular the neighbouring countries, not only in terms of production and commercial trade but also financial relations, elements that played a crucial role in the crisis. The overall scale of the decline in GDP was historical in Belgium too, reaching 4.2 p.c. between the high point reported in the second quarter of 2008 and the low point registered one year later, even if this is smaller than the drop of 5.1 p.c. seen in the euro area between the first quarter of 2008 and the middle of 2009.

In Belgium, the upturn in indicators of business activity suggests that the economy will maintain a growth path at the end of 2009 and in 2010. However, the rate of rise in Belgium is expected to remain relatively low next year as in the euro area, given the absence of a vigorous recovery in foreign demand and the predicted low levels of investment and private consumption, against a background of deterioration on the labour market. GDP is forecast to decrease by a total of 3.1 p.c. as an annual average in 2009, before growing by 1 p.c. in 2010.

While the labour market initially demonstrated its relative resilience, with only limited job losses in view of the severity of the recession, this situation stems partly from developments set to be reversed. Actually, in spite of intensive use of systems allowing some flexibility in the use of the workforce, the volume of labour mobilised within firms decreased less than production at the end of 2008 and beginning of the current year, this abrupt drop giving rise to very large losses in terms of hourly productivity of labour. In the first half of the year, this latter measure declined by 2.5 p.c. compared to the corresponding period of the previous year over the economy as a whole, dragging down firms' profitability. However, the trend in the volume of labour rapidly followed, gradually worsening in the course of 2009. Firms are expected to continue progressively rebuilding their productivity in 2010, in a climate of limited resurgence in activity, so that, measured as an annual shift, the change in the volume of labour is not forecast to return to positive values until the end of the year.

CHART 2 DEVELOPMENT OF GDP AND VOLUME OF LABOUR
(seasonally adjusted data)



Sources: NAI, NBB.
(1) Calendar adjusted data.

Furthermore, by allowing firms to adapt the volume of their staff without resorting to redundancies, the wide-scale introduction of temporary lay-offs for manual workers greatly contributed to limiting job losses, the average duration of work per employed person decreasing by 1.5 p.c. in the first six months of 2009. As in other European countries, additional measures moving in the same direction were adopted under the stimulus plan in 2009, notably by offering the possibility of suspending, subject to certain conditions, the implementation of employment contracts for clerical workers or by encouraging reductions in working hours. According to the information available, the number of persons affected by these new systems remained low when the forecasts were finalised. Given the anticipated reduction in the use made of these different flexible systems, however, destruction of jobs should continue in 2010 despite strengthening activity.

Overall, while GDP is forecast to show growth of the order of 1 p.c. in 2010, the expectation is that the volume of labour will continue to decline, albeit at a lesser rate than in 2009, with the change falling back from –1.6 p.c. to –0.3 p.c. However, the annual average decrease in employment measured in persons is set to accelerate between these two years, climbing from –0.6 p.c. in 2009, a result bolstered by the rise that was still being recorded at the end of 2008, to –1.5 p.c. in 2010. Compared to the fourth quarter of 2008, 118,000 jobs are likely to be lost in overall terms during the two years covered by the projections, 74,000 of them in 2009. The number of jobless is in turn predicted to grow by 168,000 units over the same period, driven by the effect of the continuing rise in the number of persons coming onto the labour market. Whereas the unemployment rate stood at an average of 7 p.c. in 2008, it is set to climb to 7.9 p.c. in 2009 and 9 p.c. in 2010.

The combination of a virulent financial crisis and a generalised decline in activity had a major effect on households and firms in 2009. Except for consumption and investment in the general government sector, all the components of expenditure weighed on the development of GDP. The modest recovery in growth in 2010 would be

CHART 3 EMPLOYMENT AND UNEMPLOYMENT

Sources: NAI, NEO, NBB.

based on a slight strengthening of private consumption and exports, and a turnaround in movements of inventories. However, the downturn in private investments is expected to continue.

In 2009, firms were faced with a synchronised collapse in most foreign markets such that foreign demand focused on Belgium is estimated to have deteriorated by more than 11 p.c. on average over the year as a whole. In this context, exports of goods and services were to contract by over 12 p.c., constituting the largest drop ever recorded, with the decline being particularly severe at the end of 2008 and beginning of 2009. The volume of exports began to recover in April 2009 but remains weak and so is far from having regained the previous level. Alongside this, imports fell strongly, albeit at a slightly lower rate than that of exports. Overall, net exports would make a negative contribution to the change in GDP, to the tune of 0.6 percentage points. This contribution is expected to be slightly positive in 2010, in the wake of the gradual hardening of foreign demand.

Furthermore, faced with the prospect of a persistent deterioration in demand and anxious to protect their financial position, Belgian firms similarly participated in the broad process of running down inventories seen on the world stage. Over the current year as a whole, this process is likely to cut 1.3 percentage points from the change in GDP. It is expected to come to an end during the second half of 2009, so that the change in inventories would make a small positive contribution to growth in 2010, of the order of 0.4 percentage point.

Finally, the very depressed economic environment should prompt firms, through the workings of a range of factors, to reduce their gross fixed capital formation. In the first place, the recent fall in production gave rise to an unprecedented drop in the degree of production capacity utilisation. According to the Bank's quarterly survey, this fell back from 82.4 p.c. in October 2008 to a historical low of 70.1 p.c. in April 2009. The degree of capacity utilisation increased slightly in the subsequent period, reaching 73.1 p.c. in October, but it remains substantially below the average level of the last thirty years, and the modest demand prospects do not point to a rapid rebound. Furthermore, the recession is forecast to weigh heavily on firms' operational profitability in 2009, due to the substantial decrease both in sales volume and productivity. By pushing up unit labour costs by a considerable amount, such a drop in productivity tends to reduce firms' margins in a scenario where selling prices are still under pressure, notably in foreign markets. However, this effect is largely offset by the fall in the price of imported inputs. Moreover, despite an improvement in the course of the year, real conditions for external borrowing are still affected by the financial crisis. According to the projections, business investments are set to decline by a total of 5.8 p.c. in 2009 and 1.6 p.c. in 2010, whereas they had been rising at a steady rate during the previous years.

TABLE 3 **GDP, EMPLOYMENT AND MAIN CATEGORIES OF EXPENDITURE**
(percentage changes compared to the previous year, calendar adjusted data)

	2007	2008	2009 e	2010 e
GDP [1]	2.8	0.8	–3.1	1.0
Total domestic employment in persons	1.6	1.9	–0.6	–1.5
Total volume of labour [2]	1.9	1.3	–1.6	–0.3
Real disposable income	2.0	1.3	2.1	–1.0
Components of expenditure [1]				
Final consumption expenditure of individuals	1.6	1.0	–1.6	0.8
Final consumption expenditure of general government	2.6	3.3	2.2	1.1
Gross fixed capital formation	5.7	3.8	–4.1	–1.3
Housing	–0.8	–1.6	–2.7	–1.9
Government	3.6	3.4	7.6	2.6
Business	8.7	6.1	–5.8	–1.6
p.m. Domestic expenditure excluding change in inventories [3]	*2.6*	*2.1*	*–1.2*	*0.4*
Change in inventories [3]	0.1	–0.2	–1.3	0.4
Net exports of goods and services [3]	0.2	–1.0	–0.6	0.2
Exports of goods and services	4.4	1.4	–12.1	3.0
Imports of goods and services	4.4	2.7	–11.5	2.7

Sources: NAI, NBB.
(1) In volume.
(2) Total number of hours worked in the economy.
(3) Contribution to the change in GDP.

Private individuals are also expected to rein in their expenditure strongly in 2009, both regarding household consumption and investment in housing. This behaviour mainly indicates a high level of caution in the face of uncertain prospects with regard to employment and future income, since their disposable income is set to increase steadily again – by 2.1 p.c. – in real terms. However, this improvement in purchasing power largely results from the interplay of two temporary factors. On the one hand, the effect of indexation on wages this year is set to be considerably greater than inflation in consumer prices given that, due to the time-lags incorporated in the mechanisms in the various sectors, part of the high inflation recorded in 2008 is reflected in salaries in 2009, and that the rise in the health index, which is used as a reference for indexation, is greater than the overall level of inflation this year. On the other hand, households are benefiting from reductions in tax in 2009, especially those located in Flanders, and from the fast-tracking of personal income tax assessments. This traditionally gives rise, on balance, to payments of refunds to taxpayers by the fiscal authorities. These factors will no longer play a part in 2010. On the contrary, the Flemish government has decided to limit tax reductions, while earned incomes will be affected by the decrease in employment and the modest progress in salaries. Thus, disposable income is forecast to decline by 1 p.c. in 2010.

These short-term movements in disposable income are hardly reflected at all in the trend for private consumption. In fact, in a climate of great uncertainty and substantial losses in value on their financial assets, private individuals strongly reined in their consumption and increased their savings at the end of 2008 and beginning of 2009. The upturn in confidence among households which began in April 2009, notably with regard to general economic prospects and the situation on the labour market, should give rise to a progressive, but limited, strengthening of consumption. In total, private consumption is expected to decline by 1.6 p.c. in real terms in 2009, before increasing by 0.8 p.c. in 2010. At the same time, the savings ratio is forecast to rise by around 3 percentage points in the first year, rising from 16.6 p.c. of disposable income in 2008 to 19.7 p.c. in 2009, before falling back to 18.4 p.c. in 2010. Likewise, private individuals are set to reduce their spending on investments in housing, by 2.7 p.c. in 2009 and 1.9 p.c. in 2010.

3. Prices and costs

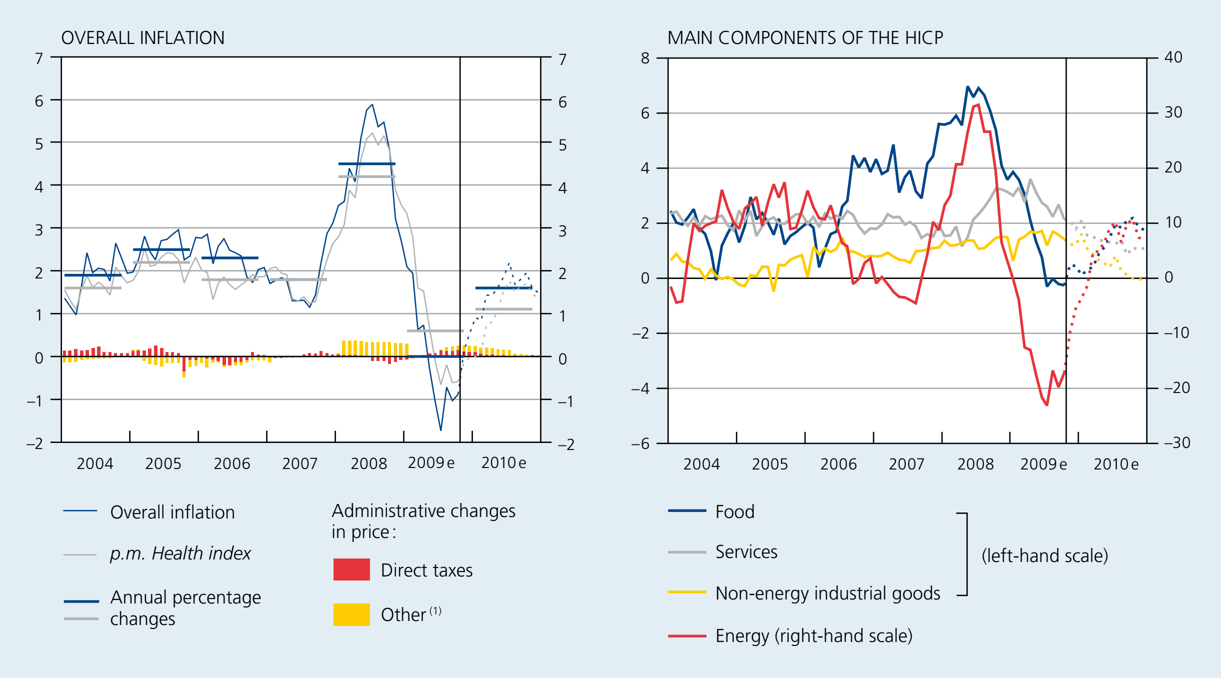
Inflation slowed down markedly in Belgium in the course of 2009, just as in the euro area; it even went into negative territory from May onwards, and appears to have remained so up to November. At its most intense in July, the fall in the index reached 1.7 p.c. compared to the previous year. However, this period of disinflation is forecast to be short-lived. Far from being a general phenomenon, it stems almost exclusively from the considerable decrease in the level of energy prices compared to the situation prevailing a year earlier, when the price of oil on the international markets had reached a peak of more than 140 US dollars per barrel. This fell back to only 40 US dollars at the end of 2008, but the price has virtually doubled since then and according to the assumptions adopted for the current forecasts, it is projected to rise further in 2010. From then on, the underlying negative effects which influenced the development of energy prices for a large part of 2009 will rapidly reverse.

The profile of the "energy" component is therefore the main explanation for the marked slowdown in overall inflation, from an average of 4.5 p.c. in 2008 to 0 p.c. in 2009, just as it accounts for a large part of its anticipated rise in 2010, to a rate of 1.6 p.c. The health index, in turn, is forecast to rise by 0.6 p.c. in 2009 and 1.1 p.c. in 2010.

Food prices also contribute to this V-shaped movement in overall inflation, since they have, as it were, stabilised in the course of 2009 after increasing very sharply in 2008. The expectation is that they will return to a normal rate of rise in 2010. On the other hand, the slowdown in inflation that started in 2009 for non-energy industrial goods and services, that is to say the two main components of the HICP, is set to continue in 2010. This effect follows from an easing of inflationary pressures due to the generally low level of demand, through the import price mechanism and, in 2010, labour costs. Following a rise of 6.6 p.c. in 2008, the deflator for imports is forecast to decrease by more than 7 p.c. in 2009 against the backdrop of an appreciating euro, declining raw materials prices and sluggishness in global trade, before growing slightly by 1.1 p.c. in 2010. For their part, unit labour costs in the private sector are estimated to have risen again steadily by 4.4 p.c. in 2009, before declining by 1.1 p.c. in 2010.

CHART 4 INFLATION

(HICP, percentage changes compared to the corresponding period of the previous year)



Sources: EC, NBB.

(1) Impact on overall inflation, in percentage points, of price changes connected with measures concerning the radio and television licence fee and changes to network industry tariffs.

TABLE 4 PRICE AND COST INDICATORS
(percentage changes compared to the previous year)

	2007	2008	2009 e	2010 e
Total HICP	1.8	4.5	0.0	1.6
Energy products	0.2	19.8	–13.8	5.9
Total excluding energy products	2.0	2.7	1.9	1.0
GDP deflator	2.3	1.8	1.1	0.9
Labour costs in the private sector:				
Unit labour costs	2.2	4.0	4.4	–1.1
Hourly labour costs	3.4	3.3	2.8	0.5

Sources: EC, NAI, NBB.

The strong increase in unit labour costs in 2009 and their marked slowdown the following year both result to a large extent from the status of labour productivity at each point in the business cycle. As explained above, and to an even greater extent than in 2008, when growth in activity had already slowed down markedly, the abrupt contraction in production in 2009 was only partly reflected in the volume of labour. The adjustment in the latter is set to continue again on a large scale in 2010, so that productivity per hour worked is expected to improve again, by 1.6 p.c., after dipping by 0.6 p.c. in 2008 and 1.5 p.c. in 2009.

The rise in hourly labour costs in the private sector is predicted to fall back from 2.8 p.c. in 2009 to 0.5 p.c. in 2010. This development essentially corresponds to the anticipated effect of indexation, the latter reacting with some lag to the hike in inflation measured by the health index in 2008, and then its slowdown in 2009. Moreover, a limited rise in real terms has been taken into account, in line with the provisions of the central agreement, which provide for the option of granting non-recurring bonuses of 125 euro in 2009 and 250 euro in 2010.

4. Public finances

According to the latest information, public finances are expected to end 2009 with a deficit of 6.1 p.c. of GDP. In the macroeconomic context described above, this deficit would shrink in 2010, reaching 5.4 p.c. of GDP.

Expressed as a percentage of GDP, public revenues are projected to decline by 1.1 percentage points in 2009 and rise by 0.6 percentage points in 2010. The fallout from the economic and financial crisis is particularly visible in terms of company taxation, the proceeds of which are set to fall in 2009 by close to one-third compared to the previous year. Revenue originating from registration fees and advance tax on income from securities is similarly projected to show a net downturn. Conversely, the tax take on earned incomes is likely to remain virtually unchanged this year with reference to GDP. It is true that revenues are being weighed down by a certain number of structural measures passed by the federal government with regard to personal income tax as well as the increased amount of the tax reduction granted by the Flemish Region. To this is added the fact that the federal government has speeded up personal tax assessments, a measure which has considerably increased tax refunds to households. However, the effect of these factors is projected to be cancelled out by the sharp increase in the share of earned incomes in GDP, which are subject to relatively heavy fiscal pressure. In 2010, fiscal and parafiscal revenues should once again show a rise due to the disappearance of the negative effect caused by the fast-tracking of assessments in 2009 referred to above. Moreover, several measures are having a favourable influence on revenues. This applies to the tax reduction approved by the Flemish Region, the scope of which will be reduced, and the tax take on company profits, which will increase following a restriction being placed on deductible expenses. For their part, non-fiscal and non-parafiscal revenues are projected to rise by 0.2 p.c. of GDP in 2009 and also in 2010 by virtue of payments made by financial institutions following the financial crisis.

Primary expenditure, which came to 46.2 p.c. of GDP in 2008, should grow to 50.1 p.c. of GDP in 2009, thus reaching a level not seen since the beginning of the 1980s. This increase stems from the concerted

TABLE 5 GENERAL GOVERNMENT ACCOUNTS[1]
(percentages of GDP)

	2007	2008	2009 e	2010 e
Revenues	48.2	48.8	47.7	48.4
Fiscal and parafiscal revenues	43.3	43.7	42.5	42.9
Others	4.9	5.1	5.3	5.4
Primary expenditure	44.5	46.2	50.1	50.1
Primary balance	3.6	2.6	–2.4	–1.7
Interest charges	3.8	3.8	3.7	3.7
Financing requirement (–) or capacity	–0.2	–1.2	–6.1	–5.4
p.m. Effect of non-recurrent factors	*–0.1*	*0.0*	*–0.8*	*0.0*
Consolidated gross debt	84.2	89.8	98.1	102.0

Sources: NAI, NBB.
(1) According to the methodology used in the excessive deficit procedure.

influence of three factors, namely the contraction in GDP, a considerable rise in spending on social security and non-recurring expenditure resulting from two legal judgements awarded against the Belgian State due to tax collected improperly in the past: on the one hand, from certain companies receiving dividends of foreign subsidiaries, and, on the other hand, from married unemployed workers. In 2010, primary expenditure as a percentage of GDP is set to nearly stabilise. Real structural growth in the former is once again set to be greater than the upward trend in GDP, but this effect is likely to be cancelled out by the disappearance of those sums paid out in implementation of the judgements awarded against the Belgian State in 2009.

Interest charges are expected to remain unchanged overall for the entire duration of the period covered by the projections, due to the low level of interest rates. Admittedly, public debt should increase, but the effect of this rise on interest charges is expected to be almost completely offset by the decrease in the implicit interest rate of the public debt.

The borrowing requirement thus estimated at 5.4 p.c. of GDP in 2010 is more favourable than predicted by the federal government (5.6 p.c. of GDP). On the one hand, the budget for general government assumes a scenario where economic growth will amount to 0.4 p.c. in 2010, whereas the current projections are based on it reaching 1 p.c. On the other hand, the federal government is proceeding on the assumption that the Communities and Regions will show a deficit of 1.1 p.c. of GDP in 2010, while the Bank's projections, which take account of the Communities' and Regions' budgets, forecast that this deficit will amount to 0.9 p.c. of GDP.

The downward trend in the debt ratio of general government, which has been recorded since 1993, was suddenly interrupted in 2008. During that year in fact, the debt ratio grew strongly due to loans taken out by the Belgian government in order to come to the aid of financial institutions, notably in the form of injections of capital and loans. It is projected to increase considerably in 2009 under the combined effect of the contraction in nominal GDP and the net growth in borrowing requirement. In 2010, public debt would continue to expand, being projected to reach a level greater than GDP again.

5. Assessment of the risk factors

In Belgium as in the majority of the advanced economies, the recovery in activity which began in mid-2009 arrived earlier than was anticipated six months ago, against a backdrop of easing financial tensions, particularly accommodative economic policies and improving business and household confidence. From then on, the estimated scale of the fall in GDP for 2009 was a little less than in the Bank's previous forecasting exercise published in June and the projections currently refer to growth of 1 p.c. in 2010, while they previously foresaw a slight decrease.

There are grounds for hoping that this recovery will be maintained, or that it will pick up pace over the course of the next few quarters. However, several factors taken into account by the majority of forecasters indicate the

TABLE 6 COMPARISON OF THE FORECASTS FOR BELGIUM
(percentage changes compared to the previous year)

	GDP in volume		Inflation [1]		Budget balance [2]		Date of publication
	2009	2010	2009	2010	2009	2010	
NBB – Autumn 2009	–3.1	1.0	0.0	1.6	–6.1	–5.4	December 2009
p.m. Spring 2009	*–3.5*	*–0.2*	*0.1*	*1.3*	*–5.5*	*–6.0*	*June 2009*
NAI	–3.1	0.4	0.0	1.5	n.	n.	September 2009
IMF	–3.2	0.0	0.2	1.0	–5.9	–6.3	October 2009
EC	–2.9	0.6	0.0	1.3	–5.9	–5.8	November 2009
OECD	–3.1	0.8	–0.1	1.0	–5.7	–5.6	November 2009
p.m. Actual 2008	*0.8*		*4.5*		*–1.2*		

(1) HICP, except for NAI: national consumer price index.
(2) Percentages of GDP.

need for caution since, even if it appears to be over, the effects of the recession will be seen for a long time to come.

On the one hand, having benefited from emergency measures aimed at preventing a systemic collapse, financial institutions need to pursue their reorganisation, which will allow them to get back on a firm footing with a view to safeguarding their role of financing the economy. This kind of reorganisation is a difficult exercise, particularly in a weakened economic situation.

On the other hand, the massive stimulus measures taken by monetary authorities and governments were crucial in preventing the global economy from becoming locked into a scenario of depression. Nonetheless, these interventions cannot continue for long or they risk endangering the conditions for long-term development. The pace and timetable of exit strategies from these flexible budgetary and monetary policies are particularly difficult to determine, since there is a simultaneous need to ensure short-term support for demand and prepare the economy for structural challenges over the long term.

Therefore, beyond the cyclical turnaround in inventories, a sustainable economic recovery would need to be supported by endogenous engines of growth, such as investment and private consumption. Prospects remain dogged by a high level of uncertainty in this respect too. The large amount of surplus production capacity around the world resulting from the contraction in activity should persist and therefore continue to weigh on investment and employment.

These elements have been taken into account in the projections. Nonetheless, in view of the exceptional nature of the current situation, arriving at a precise assessment of the extent to which they will unfold is not easy. The forecasts for 2010 are therefore surrounded by a high degree of uncertainty.

Annex

PROJECTIONS FOR THE BELGIAN ECONOMY: SUMMARY OF THE MAIN RESULTS

(percentage changes compared to the previous year, unless otherwise stated)

	2006	2007	2008	2009 e	2010 e
Growth (calendar adjusted data)					
GDP in volume	2.8	2.8	0.8	–3.1	1.0
Contributions to growth:					
Domestic expenditure, excluding change in inventories	1.7	2.6	2.1	–1.2	0.4
Net exports of goods and services	0.4	0.2	–1.0	–0.6	0.2
Change in inventories	0.6	0.1	–0.2	–1.3	0.4
Prices and costs					
Harmonised index of consumer prices	2.3	1.8	4.5	0.0	1.6
Health index	1.8	1.8	4.2	0.6	1.1
GDP deflator	2.2	2.3	1.8	1.1	0.9
Terms of trade	–0.7	0.3	–2.2	2.4	0.5
Unit labour costs in the private sector	1.7	2.2	4.0	4.4	–1.1
Hourly labour costs in the private sector	3.2	3.4	3.3	2.8	0.5
Hourly productivity in the private sector	1.6	1.2	–0.6	–1.5	1.6
Labour market					
Domestic employment (average annual change in thousands of persons)	50.5	70.3	82.1	–27.3	–64.4
Total volume of labour (1)	1.3	1.9	1.3	–1.6	–0.3
Harmonised unemployment rate (2) (p.c. of the labour force)	8.3	7.5	7.0	7.9	9.0
Incomes					
Real disposable income of individuals	2.8	2.0	1.3	2.1	–1.0
Savings ratio of individuals (p.c. of disposable income)	15.8	16.2	16.6	19.7	18.4
Public finances (3)					
Overall balance (p.c. of GDP)	0.3	–0.2	–1.2	–6.1	–5.4
Primary balance (p.c. of GDP)	4.2	3.6	2.6	–2.4	–1.7
Public debt (p.c. of GDP)	88.1	84.2	89.8	98.1	102.0
Current account (according to the balance of payments, p.c. of GDP)	**2.0**	**2.2**	**–2.5**	**–0.9**	**–0.4**

Sources: EC, DGSEI, NAI, NBB.
(1) Total number of hours worked in the economy.
(2) Adjusted series (Eurostat).
(3) According to the methodology used in the excessive deficit procedure (EDP).