Country report **BELGIUM**

Summary

End 2011 a new government was formed and it immediately announced a credible austerity package for 2012. That said, the new government and the expected state reform should not lead to the conclusion that political instability is off the table for the coming years. Besides that, the government still has to show its commitment to further unpopular pension and labor market reforms, which are inevitable to increase competitiveness and potential economic growth. That said, the financial position of the private sector and the institutional power show the strong fundamentals of the Belgian economy.

Things to watch:

- High need to boost labor participation and reform the pension system
- Spillover of risks from banking sector to state due to sizeable contingent liabilities
- Gradual process of deteriorating competitiveness of Belgian firms

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Belgium

National facts	
Type of government	Constitutional monarchy
Capital	Brussels
Surface area (thousand sq km)	31
Population (millions)	10.6
Main languages	Dutch (60%)
	French (40%)
Main religions	Roman Catholic (75%)
	Other (25%)
Head of State (president)	King Albert II
Head of Government (prime-minister)	Elio Di Rupo
Monetary unit	Euro (EUR)

Economy	2011	
Economic size	*bn USD*	*% world total*
Nominal GDP	513	0.74
Nominal GDP at PPP	426	0.54
Export value of goods and services	431	1.97
IMF quotum (in mln SDR)	4605	2.12
Economic structure	*2011*	*5-year av.*
Real GDP growth	1.9	1.2
Agriculture (% of GDP)	1	1
Industry (% of GDP)	22	23
Services (% of GDP)	78	76
Standards of living	*USD*	*% world av.*
Nominal GDP per head	48224	447
Nominal GDP per head at PPP	40009	324
Real GDP per head	38224	470

Social and governance indicators	rank / total
Human Development Index (rank)	18 / 187
Ease of Doing Business Index (rank)	28 / 183
Index of Economic Freedom (rank)	38 / 179
Corruption Perceptions Index (rank)	19 / 183
Press Freedom Index (rank)	20 / 178
Gini index (income distribution)	33.0
Population below $1.25 per day (PPP)	n.a.

Foreign trade			2010
Main export partners (%)		*Main import partners (%)*	
Germany	19	Netherlands	19
France	17	Germany	16
Netherlands	12	France	11
UK	7	Ireland	6

Main export products (%)	
Chemicals and related products, n.e.s.	31
Machinery and transport equipment	20
Food, drinks and tobacco	9
Mineral fuels, lubricants, and related materials	8
Main import products (%)	
Chemicals and related products, n.e.s.	25
Machinery and transport equipment	23
Mineral fuels, lubricants, and related materials	13
Food, drinks and tobacco	7
Openness of the economy	
Export value of G&S (% of GDP)	84
Import value of G&S (% of GDP)	85
Inward FDI (% of GDP)	15.7

Source: EIU, CIA World Factbook, UN, Heritage Foundation, Transparency International, Reporters Without Borders, World Bank.

Full report:

In comparison to other eurozone member states, the Belgian economy recovered relatively strongly after the recession in 2009 (in which GDP contracted by 2.7%). The recovery was led by strong growth of exports and private consumption. The volume of private consumption was at the end of 2011 already 3.5% above its pre-crisis level, which can be explained by robust wage growth, a steady recovery of employment and large financial buffers of Belgian households. However, during 2011 the slowdown of world trade and the aggravation of the European debt crisis took its toll on the open Belgian economy as it entered a mild recession in 11H2.

For 2012 we expect growth, if any, to be very weak. It should be noted that we are a bit more optimistic than the EIU, which forecasts a GDP contraction of 0.4% this year. The severe slowdown in comparison to last year can be explained by the sizeable austerity measures and the weakening external environment. The former will hamper domestic demand, while foreign demand will slow down as half of total exports is directed to Germany, France and the Netherland, countries which are expected to experience only muted growth or even a contraction this year. During the recovery the unemployment rate decreased from a peak of 8.5% to 7% early 2011. However, in 11H2 the unemployment rate started rising again (currently 7.4%) and, given the weak outlook, we do not expect job creation to be strong enough to reverse this trend anytime soon.

The harsh austerity measures implemented by the new six-party government are necessary given the weak position of Belgium's public finances. Although during the last two decades the government was very successful in bringing down the gross government debt (from 138%-GDP in 1993 to 88%-GDP in 2007), since the financial crisis it rose again to 98%-GDP in 2011. Besides the current high debt level of the government, there exist significant contingent liabilities as a result of bank restructuring and provided guarantees to Belgian banks (together around 15%-GDP). Although the domestic level of non-performing loans remains muted due to a financially solid private sector, these contingent liabilities should be considered as a threat to public finances amid bank's risky foreign exposure (total exposure to Italy, Spain, Ireland, Portugal and Greece equals 14.9%-GDP end 11Q3) and persistent stress in the European banking sector.

Given the relatively low budget deficit it is possible to let the debt ratio trend downwards from 2013 or 2014 onwards. Next to short-term fiscal consolidation, in the medium and long term reforms are inevitable to increase potential economic growth and to enhance the sustainability of public finances. This is especially important given the impact of future aging, even though this is only average from a European perspective. Policy should focus on the pension system and the labour market as both the effective retirement age (59 years) and the labor participation rate (69%) are very low from a European perspective. Regarding the pension system, the government already took a first step by increasing the minimum age for early retirement from 60 to 62 years, but further adjustments remain necessary. Next to the socio-economic reforms, the government has planned a state reform, which comprises the shift of responsibilities and tax autonomy from the federal level to the regional level. Although this reform has no direct impact on public finances, it might improve the efficiency and incentives for fiscal prudence at the regional level. The fact that it took almost 1.5 years to form a government reflects the persistent tensions between the two linguistic communities. The state reform, expected to go through parliament this summer, should not lead to the conclusion that political bickering and instability are off the table for the coming years. However, interest rates on government bonds show that investor confidence has increased significantly since the formation of the government; yields fell from 5.8% in November 2011 to an average yield of 3.5% in the first half of April 2012.

Due to very high household savings (net financial assets amount to 212%-GDP) and only moderate debt levels of firms, the financial position of the private sector is one of the healthiest in Europe. This is beneficial for public finances as the private sector is theoretically able to finance the government domestically and, even more important, there is no need for private deleveraging which would hamper economic growth. Given the importance of a financially healthy private sector, it is crucial to reverse the trend of the deterioration of the competitiveness of Belgian firms, which is reflected by the gradual reduction of the current account surpluses since the late 1970's. Recent years even show very small deficits on the current account. Competitiveness can be improved by muted wage growth (reform or abolishment of the automatic wage indexation) and a better connection to Asian growth markets. The fairly good ranking in the Global Competitiveness Index 2011-2012 (15^{th}, with a 2^{nd} ranking regarding primary education) reflects the institutional capabilities of the country.

Belgium

Selection of economic indicators	2007	2008	2009	2010	2011	2012e	2013f
Key country risk indicators							
GDP (% real change pa)	2.8	0.9	-2.7	2.3	1.9	-0.4	1.2
Consumer prices (average % change pa)	1.8	4.5	0.0	2.3	3.5	2.2	2.4
Current account balance (% of GDP)	1.5	-1.4	-1.7	1.3	-0.6	-0.4	-0.5
Economic growth							
GDP (% real change pa)	2.8	0.9	-2.7	2.3	1.9	-0.4	1.2
Gross fixed investment (% real change pa)	6.1	2.2	-8.1	-0.9	5.1	-1.0	1.1
Private consumption (real % change pa)	1.7	1.9	0.8	2.3	0.8	0.4	0.9
Government consumption (% real change pa)	2.0	2.4	0.8	0.2	0.8	-0.5	0.2
Exports of G&S (% real change pa)	5.2	1.8	-11.3	9.9	4.8	-0.2	2.1
Imports of G&S (% real change pa)	5.2	2.9	-10.6	8.7	5.2	0.1	2.0
Economic policy							
Budget balance (% of GDP)	-0.3	-1.3	-5.9	-4.2	-4.2	-3.1	-2.9
Public debt (% of GDP)	84	89	96	96	98	101	101
Money market interest rate (%)	4.3	4.7	1.2	0.8	1.4	1.0	1.2
M2 growth (% change pa)	4	5	3	6	3	1	7
Consumer prices (average % change pa)	1.8	4.5	0.0	2.3	3.5	2.2	2.4
Exchange rate LCU to USD (average)	3.7	3.7	3.7	3.7	3.7	n.a.	n.a.
Recorded unemployment (%)	7.5	7.0	7.9	8.3	7.2	5.5	5.6
Balance of payments (mln USD)							
Current account balance	7041	-7109	-7816	6351	-3000	-2100	-2400
Trade balance	615	-16124	-6685	-4729	-9700	-17500	-13200
Export value of goods	299407	332384	249749	279702	329500	300600	310000
Import value of goods	298790	348510	256430	284430	339200	318100	323300
Services balance	5772	5162	8140	8545	4500	4600	6400
Income balance	7011	12743	-257	10957	13200	26100	19900
Transfer balance	-6357	-8891	-9015	-8423	-11000	-15300	-15500
Net direct investment flows	13096	-28770	54299	25047	5603	-12260	-17620
External position (mln USD)							
International investment position	142900	191560	273770	361670	n.a.	n.a.	n.a.
Total assets	2452420	2410330	2485260	2391880	n.a.	n.a.	n.a.
Total liabilities	2309520	2218770	2211490	2030210	n.a.	n.a.	n.a.
Key ratios for balance of payments, external solvency and external liquidity							
Trade balance (% of GDP)	0.1	-3.2	-1.4	-1.0	-1.9	-3.6	-2.7
Current account balance (% of GDP)	1.5	-1.4	-1.7	1.3	-0.6	-0.4	-0.5
Inward FDI (% of GDP)	21.0	36.4	12.9	15.5	15.7	15.1	15.8
International investment position (% of GDP)	31.1	37.7	57.9	76.7	n.a.	n.a.	n.a.

Source: EIU

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