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Economic growth slowed in 2018 and is projected to remain at around 1½ per cent in 2019 and 2020. Domestic demand will be the main driver of growth. Government investment will be strong in 2020, and private investment will also support growth in the coming two years. Underlying price inflation will pick up gradually due to increasing wage growth in a tight labour market.

Public debt is projected to decline throughout the projection period, despite some loosening of fiscal policy due to a reduction of taxes. Raising skills and work opportunities for disadvantaged groups would make growth more inclusive. To make growth greener, transport infrastructure should be improved and congestion charges extended, while productivity would be enhanced by reducing barriers to firm entry and exit.

Growth has weakened

Economic growth has weakened as private consumption growth has decreased, despite continued employment growth supported by labour tax cuts. Consumer and business confidence have weakened somewhat in recent months but remain above average. Government investment has increased and business investment is strengthening. Exports show signs of recovering somewhat after a weak start to 2018. Inflation increased during 2018 reflecting sharp price rises for energy products. Wage growth has increased, outpacing underlying inflation, notwithstanding recent reforms of the wage setting system designed to allow the framework to better take into account international cost competitiveness.

Inclusiveness and productivity could be enhanced

The budget deficit will rise in the coming two years, reaching 1.4% of GDP in 2020. As public debt is high, it is important that the government adheres to its medium-term fiscal targets to ensure a steady reduction of the debt-to-GDP ratio. Public investment, which has

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been low for several decades, should be increased to boost productivity growth. To ensure fiscal sustainability, this investment should be financed through reductions in inefficient public spending, higher user fees or through tapping private sources of finance.

Improving transport infrastructure around major urban areas, extending congestion charges and amending the favourable tax treatment of company cars would make growth greener. To make growth more inclusive, the skills and labour market performance of immigrant, low-skilled and older workers should be enhanced. Further reducing labour taxes, especially for low-skilled workers would help, as the tax wedge on labour earnings remains one of the highest in Europe. Further engaging social partners in firm-level diversity plans, including in the public sector where the share of immigrant employees is low, would facilitate the increased employment of immigrants in particular.

Productivity would benefit from increased competition, innovation and business dynamism. Regulatory barriers to firm entry and exit should be reduced and the insolvency regime reformed. Ensuring that appropriate financing tools are available for the scaling up of young, innovative firms and further streamlining public support for R&D and innovation are of particular importance. The regulation of retail services should also be eased, and a single regulator for each network industry established.
Growth is projected to stabilise

GDP growth is projected to remain at around 1½ per cent in 2019 and 2020. Private consumption will be an important driver of growth, supported by past and announced additional reductions in labour taxation. Private investment will remain robust over the projection period, supported by favourable financing conditions and high levels of profitability. Government investment will contribute to economic activity in 2020 with the launch of some major public investment projects. Employment growth is projected to continue, leading to further declines in the unemployment rate to 5.9% in 2020.

Economic growth could be weaker if private consumption growth is lower than expected. On the upside, business investment could be stronger than expected, if the tight labour market leads to more labour-saving investment than projected.