Business Cycle Monitor

September 2024

Belgian economy expected to post broadly stable growth of 0.2% in the third quarter of 2024[1]

- According to the latest statistics, Belgian economic growth came in at 0.2% in the second quarter of 2024. This is in line with the NAI's earlier flash estimate but lower than the 0.4% estimate set out in the June 2024 Business Cycle Monitor (BCM), which can be attributed in part to an asymmetric shock that affected vehicle manufacturing through a bankruptcy and production declines.
- Household consumption grew moderately in the second quarter. Consumer sentiment rebounded in the meantime, but the fundamentals remain quite weak for now. Overall, household consumption growth is expected to remain sluggish in the third quarter of 2024.
- Business investment growth was boosted by exceptional transactions in the second quarter, but the underlying momentum was very weak and we expect the growth rate to remain close to zero in the current quarter. Residential investment should remain sluggish as well.
- Government consumption is likely to moderate slightly in the current quarter, while government investment growth should continue to benefit from the electoral cycle as well as the roll-out of large investment programmes.
- Net exports (excluding exceptional sales of investment goods abroad) boosted activity growth in the second quarter. Trade growth is likely to remain sluggish in the near term, but a gradual improvement in Belgian competitiveness should support export growth in the near term. All in all, the underlying contribution of net exports to GDP growth should remain positive in the current quarter.
- The NBB's BREL nowcasting model currently estimates growth in the third quarter at 0.3%, which is also the median of the one-indicator models. The R2D2 model, on the other hand, sees growth at -0.2%.
- Overall, a growth rate of 0.2% in the third quarter of 2024 currently appears to be the most plausible estimate. While private demand and manufacturing output are likely to remain quite weak, the gradual unwinding of the exceptional asymmetric shock on vehicle production should support growth. In the third quarter, value added of motor vehicle manufacturing is indeed unlikely to decline to the same extent.

[1] This is a short-term NBB estimate which should not be confused with the official statistics published by the National Accounts Institute (such as the flash GDP estimate, which is released one month after each quarter). This estimate is based on nowcasting models and expert judgment and incorporates information up to 6 September 2024. Like all estimates and forecasts, it is subject to a degree of uncertainty.

Activity growth in the euro area should remain subdued in the current quarter

The latest statistics for the second quarter of 2024 show euro area GDP decelerating slightly to 0.2%. Activity had stalled in the wake of the energy crisis but started to pick up recently. Year-on-year growth came in at 0.6% in the second quarter. Excluding the notoriously volatile Irish GDP statistics,[2] the economic performance of the euro area improves somewhat, posting a year-on-year growth rate of 0.8%.

Table 1

Real GDP growth
(%, adjusted for seasonal and calendar effects)

	Quarter-on-quarter change				**Year-on-year change**
	2023Q3	2023Q4	2024Q1	2024Q2	2024Q2
Euro area (EA)	0.0	0.1	0.3	0.2	0.6
p.m. EA excl. Ireland	0.1	0.1	0.3	0.2	0.8
Germany	0.2	-0.4	0.2	-0.1	0.0
France	0.1	0.4	0.3	0.2	1.0
Italy	0.3	0.1	0.3	0.2	0.9
Spain	0.5	0.7	0.8	0.8	2.9
Netherlands	-0.4	0.2	-0.3	1.0	0.6
Belgium	**0.3**	**0.3**	**0.3**	**0.2**	**1.1**
p.m. Ireland	*-1.9*	*-1.7*	*0.6*	*-1.0*	*-4.1*
EU	0.2	0.1	0.3	0.2	0.8
UK	-0.1	-0.3	0.7	0.6	0.9
US	1.2	0.8	0.4	0.7	3.1
Japan	-1.0	0.1	-0.6	0.8	-0.8

Sources: EC, US Department of Commerce, Cabinet Office Japan.

The growth rate for the euro area as a whole masks divergent growth rates among member states. In Germany, economic activity declined by 0.1%, following a moderate rebound in the first quarter of 2024. This was primarily due to very weak final domestic demand. While GDP was supported by government spending and inventory build-up, a drop in household consumption and a pronounced decrease in private investment, by more than 2%, reduced overall activity. Compared with the same quarter last year, German GDP remains unchanged. In France, second-quarter GDP growth was 0.2%, largely driven by positive growth in net exports, while domestic demand and inventory changes had a neutral effect on GDP. The modest expansion of Italian economic activity also continued, driven by moderate growth in domestic demand, which helped counterbalance the negative impact of net exports on overall growth. In the Netherlands, a surge in exports, government spending and investment offset a decline in household consumption, leading to GDP growth of 1% in the second quarter. Lastly, Spain's economy continues to outpace that of the euro area as a whole: it grew by 0.8% for the second consecutive quarter, supported by strong domestic and external demand, pushing year-over-year growth to nearly 3%.

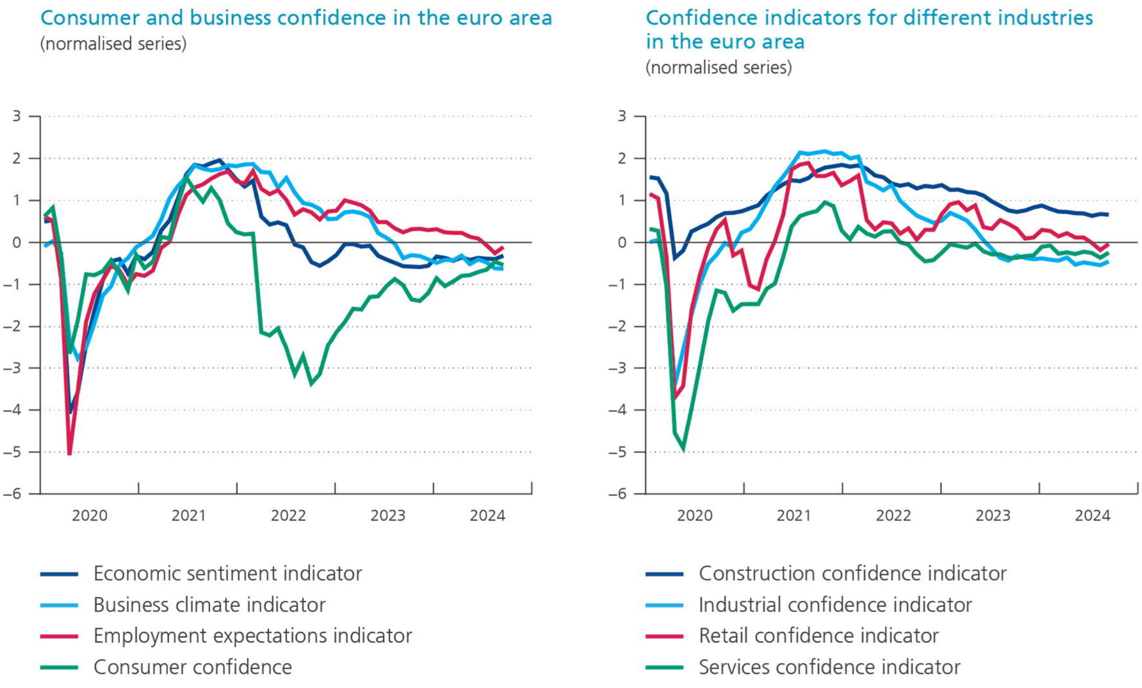
[2] The volatility in Irish GDP statistics is mostly due to operations involving intangible assets. These transactions usually do not reflect the Irish or euro area business cycle and are related to tax optimisation by large foreign-owned multinationals. See Andersson *et al* (2023) for a detailed discussion.

GDP growth was much stronger among the major developed economies outside the euro area. Following a brief slowdown in the first quarter, the US economy regained momentum, expanding by a solid 0.7% in the second quarter. Over the past year, the US economy has grown by more than 3%. After declining in the second half of 2023, real GDP in the UK began to expand again in the first quarter of 2024; this momentum continued in the second quarter, bringing year-on-year growth to 0.9%. The Japanese economy rebounded sharply after a challenging 2023 and a contraction in the first quarter of 2024. However, year-on-year, second-quarter GDP growth remains negative at -0.8%.

Survey indicators show that economic sentiment in the euro area remains subdued. The EC's Economic Sentiment Indicator (ESI) for the euro area has not moved much since early 2024 and remains below its long-term average. The latest observation for August revealed a slight uptick driven by an improvement in confidence in services, manufacturing and retail trade. Sentiment among managers in construction was mostly stable and euro area consumer confidence edged down. The employment expectations index, which reflects the labour market outlook, has weakened gradually in recent months and sits below its long-run average despite a partial recovery in August (see Figure 1).

Figure 1

Sentiment indicators for the euro area



Source: EC.
Note: The original series are normalised around their historical average and divided by their standard deviation.

The improvement in manufacturing confidence in August was primarily driven by more optimistic production expectations on the part of managers. However, any recovery remains tentative, as order books and recent production trends held steady at low levels and export orders continued to decline. The improvement in the services industries was quite broad-based, with both recent and expected demand reported to have improved. In the retail industry, managers were downbeat about their situation in the recent past but reported significantly improved expectations about their business situation in August. Confidence in the construction industry remained mostly stable, with a more positive assessment by managers of recent activity offsetting a decline in their outlook, as reflected in the continued slight decline in their assessment of order books.

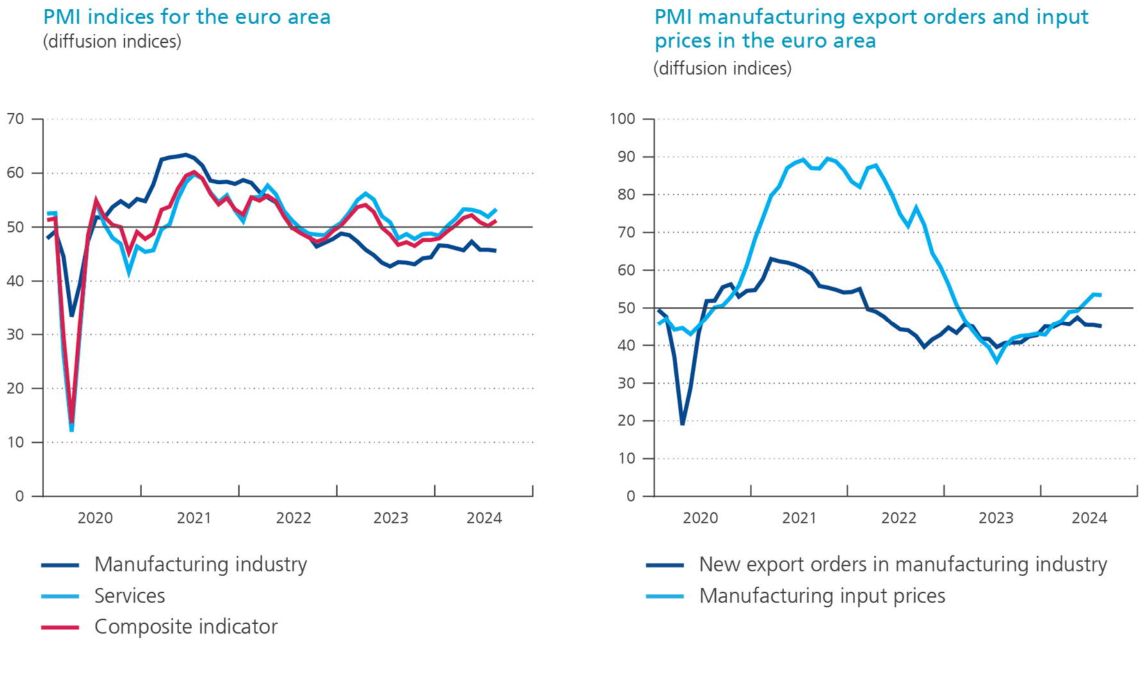
The PMI indicators for the euro area show that, overall, business confidence in the euro area recovered in the first quarter but slid back in the second. The most recent observations show the composite indicator recovering somewhat and hovering above the 50-point mark (see Figure 2, left-hand graph). This suggests that overall euro area economic activity should continue to expand in the third quarter. Recent developments in the composite PMI have largely been driven by sentiment in the services industries. Conditions in the manufacturing industry remain challenging, with the manufacturing PMI virtually stable since early 2024.

Price pressures remain mostly mild. The PMI for manufacturing input prices exceeded the 50-point mark late in the second quarter, suggesting that input prices are, on average, rising again after having declined for most of the past year (see Figure 2, right-hand graph). Prices for natural gas on the European market, for example, have been increasing since reaching a low in February. This underscores the ongoing structural challenges faced by energy-intensive manufacturing firms in Europe, as reflected in the PMI for new export orders in the manufacturing industry: the upward trend in the indicator, which began in the second quarter of 2022, was interrupted in the second quarter of 2024, with the indicator since dropping further below the 50-point threshold.

Overall, sentiment indicators point to stable yet subdued growth in euro area economic activity in the third quarter of 2024.

Figure 2

PMI indices



Source: HCOB.

The Belgian economy grew by 0.2% in the second quarter

According to the latest statistics, Belgian economic activity also decelerated slightly in the second quarter of 2024, to 0.2%. This is in line with the euro area average and weaker than the June BCM estimate of 0.4%. Much of the deceleration appears due to an asymmetric demand shock that hit Belgian vehicle manufacturing plants. Consumers have been shifting away from the electric vehicle models made in Belgium, and a large company in the industry declared bankruptcy in the second quarter. A more “normal” evolution in value added in vehicle manufacturing would have put the overall quarterly growth rate at 0.3%, as forecast in the Bank’s June 2024 economic projections, thus only marginally below the aforementioned BCM estimate.

Despite the overprediction of the growth rate, the June 2024 BCM was in fact quite accurate for most demand components. Household consumption growth remained moderate and housing investment turned negative again in the second quarter; both developments were in line with our expectations. The continued growth of government-driven components was also accurately anticipated. Government consumption growth edged down but continued to expand at a moderate pace. In addition, government investment growth contributed positively to GDP growth in the second quarter, mostly due to increased investment in the run-up to local elections – although the deceleration in this component was somewhat sharper than anticipated. As always, it should be noted that quarterly statistics on government spending, in particular, are prone to significant revisions.

Two components are somewhat harder to interpret, however. The statistics published by the NAI at the end of August show continued robust business investment growth and a negative contribution by net exports to GDP growth. However, as mentioned in previous issues of the BCM, recent business investment and export statistics have been affected by the (GDP-neutral) sale of ships by a domestic company to a foreign counterparty. Although these transactions took place in the fourth quarter of 2023 and the first quarter of 2024, they continued to affect growth rates in the second quarter. Accounting for these transactions, business investment growth came in at close to zero and, hence, somewhat below the BCM prediction of moderate growth. The underlying contribution of net exports to GDP (excluding the aforementioned sales), on the other hand, improved slightly, as anticipated in the June BCM.

Turning to the production approach to GDP, private sector value-added production in the second quarter of 2024 decelerated further, to a quarterly growth rate of just 0.1%. In volume terms, manufacturing activity declined by 0.3% (which partly reflects the strong decline in output in car manufacturing), while market services expanded by just 0.2%. On the other hand, the construction industry returned to robust positive growth and, more importantly for GDP, value added in non-market services expanded by 0.4% in the second quarter. It should be stressed that this expansion, mostly financed through government funds, explains about half of overall economic growth in the second quarter.

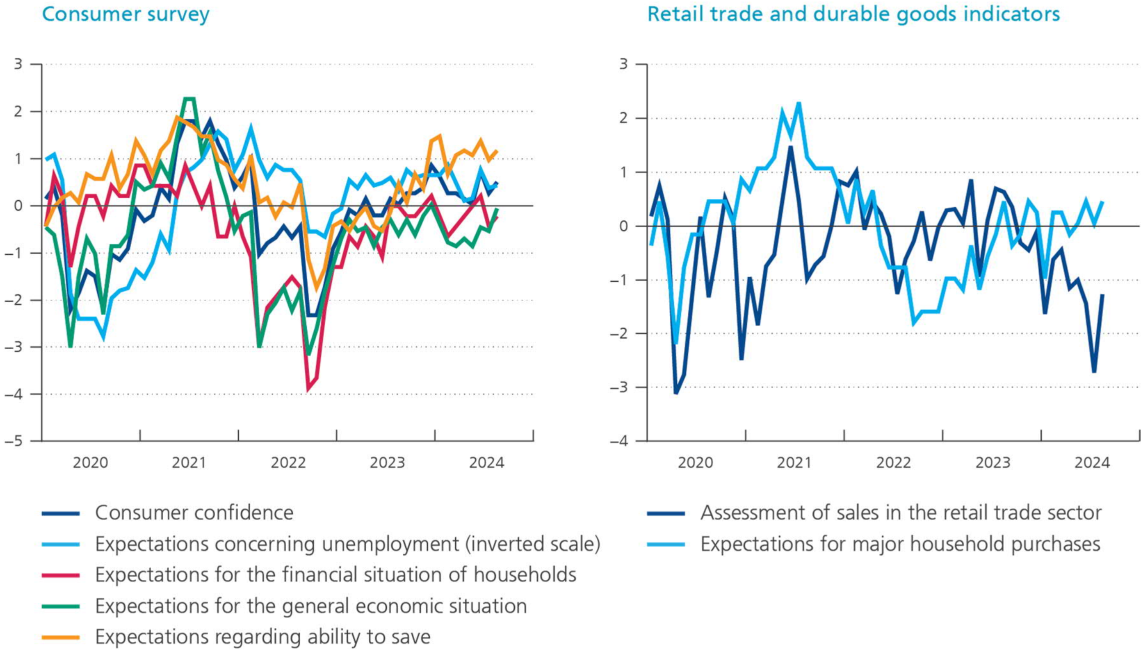
Household consumption should continue to expand at a moderate pace in the third quarter

Survey indicators for private consumption present a mixed picture. Consumer sentiment rebounded in the third quarter, after having deteriorated since early 2024 on the back of worsening unemployment expectations, the component of consumer confidence that typically has the greatest predictive power for actual consumption. This may have been partly due to extensive media coverage of redundancies among several large and well-known manufacturing firms (including the aforementioned vehicle manufacturing firm that went bankrupt). However, this was a temporary phenomenon. Unemployment expectations – and consumer confidence – improved again in June and, some short-run volatility notwithstanding, have more or less returned to their early-2024 levels. Moreover, households' outlook for the general economic situation brightened markedly in recent months, while their expectations for their own financial situation remain quite robust and saving intentions are high. **Overall, the consumer survey results suggest slightly better conditions for private consumption in the near term.**

Expectations for major purchases in the next twelve months remained close to their long-term average, as has been the case since mid-2023. This suggests that sales of durable goods can be expected to hold up quite well. However, specific indicators for the consumption of non-durables, which account for the bulk of household goods consumption, continued to worsen. The assessment of sales in the retail industry has been trending down since mid-2023 and deteriorated suddenly in July to its lowest level since the spring of 2020, before bouncing back somewhat in August (see Figure 3, right-hand graph). This is in line with the synthetic indicator for retail trade, which dropped from already low levels in the early summer before recovering somewhat in August (see Figure 4, left-hand graph). Retail conditions were already reported to have deteriorated in the May 2024 Business Echo, and conditions do not appear the have improved since.

Figure 3

Indicators of household consumption growth
(normalised series)



Source: NBB.
Note: The original series are normalised around their historical average.

The fundamentals for household consumption have also weakened compared to last year. Following the strong increase in 2023, purchasing power growth slowed in the first half of 2024 due to the normalisation of indexation-driven wage growth and a significant slowdown in employment growth. As predicted, inflation climbed again, mostly due to the disappearance of base effects relating to energy inflation and the unwinding of government support measures. These factors are likely to keep consumption growth low in the third quarter as well. However, fundamentals should gradually strengthen again, along with the expected recovery in employment, while the continued steady decline in goods and services inflation should boost real income growth.

All in all, we expect household consumption growth to remain moderate in the third quarter of 2024.

Third-quarter private investment growth is expected to remain close to zero

The pace of business investment normalised in early 2024, after the spectacular surge that started in mid-2022. Correcting for large and exceptional divestments (the aforementioned sales of ships) in the preceding quarters, second-quarter business investment growth was near zero. In addition, if an exceptionally large inflow of investment in the ICT industry in the second quarter[3] is also corrected for, underlying business investment growth was even negative. While the underlying growth rate was somewhat weaker than expected, Business Echo interviews conducted before the summer indeed suggested that tighter profit margins have prompted widespread cost-cutting, including reductions in certain types of investment expenditure. Ongoing investments were reportedly focused on improving efficiency and modernising production processes, while expansionary investments were frequently cancelled or postponed

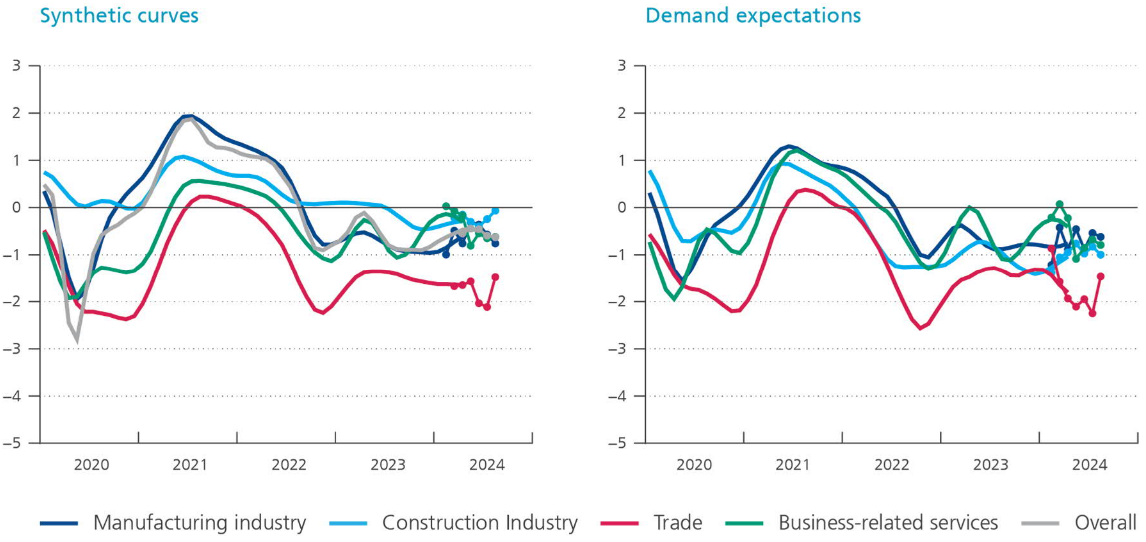
[3] See https://www.nbb.be/doc/dq/e/dq3/histo/neat24ii.pdf.

The NBB business survey indicates that the tentative upward trend in overall business confidence observed in early 2024 came to an end in the second quarter, with the most recent results showing a gradual decline in the third quarter (see Figure 4, left-hand graph). This downturn in the overall synthetic indicator is mainly driven by respondents from the manufacturing industry, coupled with eroded confidence among respondents in business-related services, an industry that is being affected by belt-tightening measures in the wider economy. On the other hand, confidence in the construction industry is clearly up in the third quarter of 2024 after briefly deteriorating in the second. Finally, as mentioned above, confidence in trade declined in June and July but rebounded slightly in August; overall, confidence in this industry has remained at low levels since early 2023.

Firms' demand expectations are more volatile, with some interesting divergences from the headline figures across the various industries. Most notably, the outlook in the manufacturing industry continues to trend up gradually in the third quarter. The demand outlook for business-related services has also started to recover in recent months, following a sharp decline early in the second quarter. The outlook in the trade industry deteriorated significantly throughout the first half of 2024 but suddenly improved in August (Figure 4, right-hand graph). Demand expectations in the construction industry, on the other hand, have largely stabilised in recent months after improving in the second quarter. All in all, **the specific outlook for demand appears slightly more benign than the synthetic curves**, which suggests that respondents generally expect somewhat better business conditions beyond the near term.

Figure 4

Business sentiment and demand expectations
(normalised series)



Source: NBB.
Note: The original series are normalised around their historical average and divided by their standard deviation.

At the same time, the need to boost production capacity remains low, as evidenced by the low capacity utilisation rate reported in the NBB's latest quarterly survey on production capacity. In July, the capacity utilisation rate edged up to 74.2%, which is still far below the long-run average of around 80%.

Finally, financial conditions are not reported to be a constraining factor for business investment. The NBB's quarterly survey on credit conditions points to a continued easing of conditions throughout 2024.

Overall, we expect business investment (corrected for the effects of exceptional transactions in previous quarters) to remain broadly flat in the third quarter of 2024.

As anticipated in the June BCM, residential investment in volume terms declined again in the second quarter of 2024, dropping by nearly 2% from the first quarter. Looking at the broader trend, residential investment has fallen by nearly 9% since early 2023 and over 15% since its peak in mid-2021. The fundamentals for household investment remain weak, with higher prices for building materials and still-high interest rates weighing on investment decisions by households. In addition, the heavy costs associated with – and the uncertainty regarding – renovation obligations may push households to delay renovations. There are tentative indications that the housing market may be turning the corner, as transaction volumes are on the rise and confidence and demand expectations in the construction industry are recovering. However, any recovery in the short term is likely to be weak until the fundamentals improve. **In sum, we expect residential investment to remain weak, with slightly negative growth in the third quarter of 2024.**

All in all, we expect near-zero private fixed capital investment growth in the current quarter.

Government investment expanded by 0.5% in the second quarter of 2024. **The implementation of recovery plans and the regular electoral cycle should continue to support government investment in the near term.**

Government consumption growth is likely to moderate slightly

In the second quarter, government consumption growth in real terms came in at 0.6%, thereby exceeding the long-run average of approximately 0.4%. **We expect government consumption growth to continue to expand in the third quarter of 2024, most likely at a slightly more moderate pace.**

The contribution of net exports to growth is expected to improve gradually

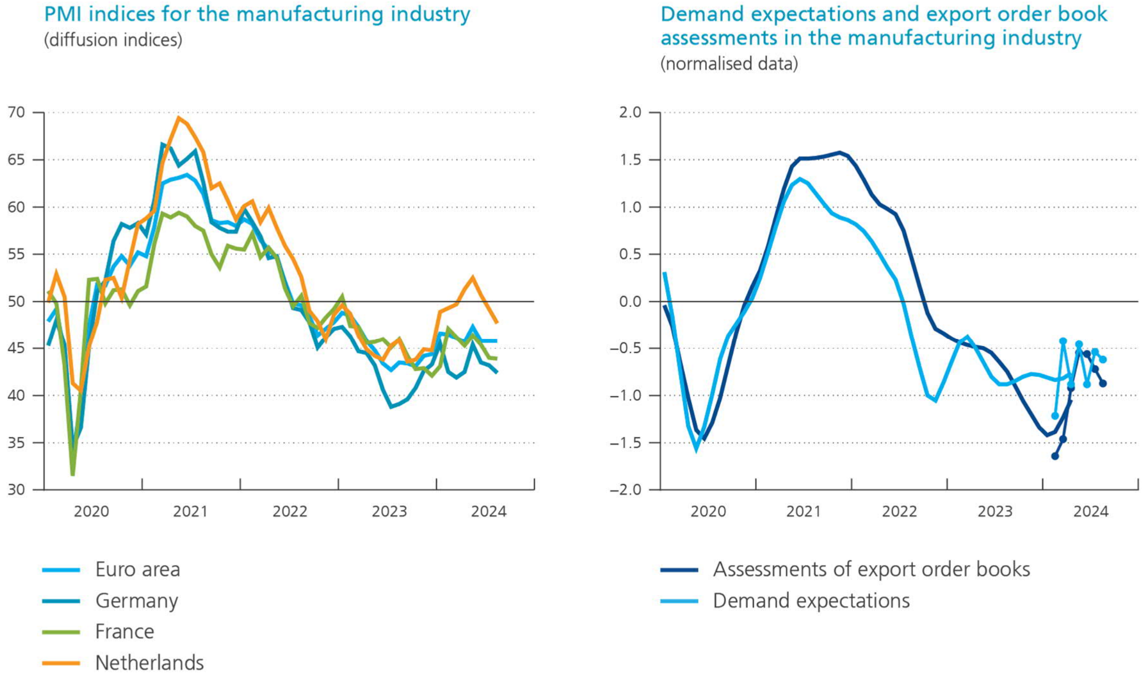
Global trade has virtually stagnated over the past two years. Despite some early optimism in 2024, recent signs of weakness in heavily traded industrial production, particularly in Europe, coupled with risks of greater protectionism, may imply that **trade growth is likely to remain sluggish in the near term**. After a brief uptick in the second quarter, the PMI manufacturing indices for Belgium's largest neighbours – and main trading partners – have been trending down in recent months and are below 50, signaling in principle a contraction in activity. Only the Netherlands briefly saw its indicator reach levels typically associated with an expansion. The euro area aggregate indicator has essentially moved sideways in contractionary territory since early 2024, and demand for European products may continue to struggle.

At the same time, the cost competitiveness of Belgian exporters is improving gradually, as nominal wage cost growth among euro area trading partners is now outpacing that in Belgium. The NBB's monthly business survey shows demand expectations in the Belgian manufacturing industry trending up gradually. However, recent weakness in the European manufacturing industry could pose a threat to this recovery. Assessments of export order books, for example, have taken a hit in recent months, after surging briefly in the second quarter (see Figure 5, right-hand graph).

Overall, world trade should still recover gradually and improving cost competitiveness will support Belgian export growth. As domestic demand growth is likely to remain more moderate, the associated import growth should be subdued, and **net exports are likely to make a positive contribution to growth in the near term.**

Figure 5

PMI indicators in neighbouring countries and export orders in manufacturing



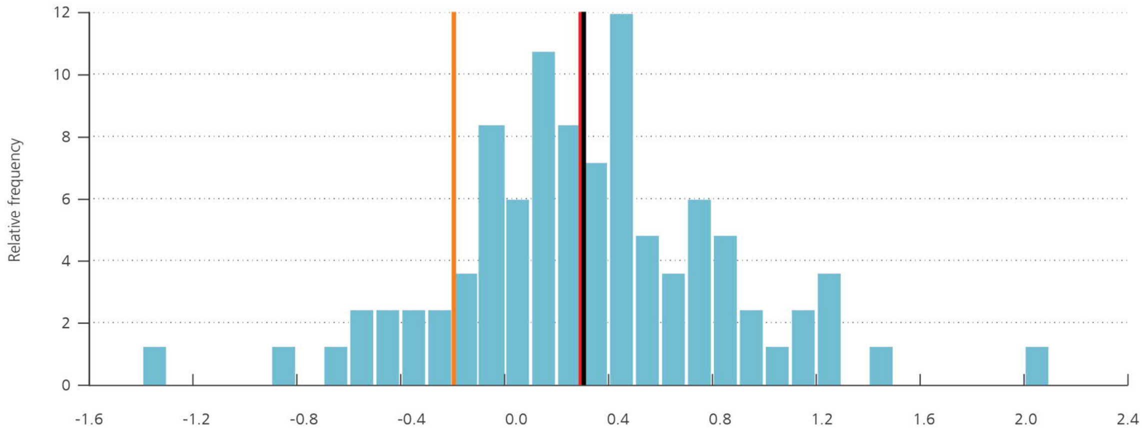
Sources: Markit, NBB.
Note: The series in the right-hand graph are normalised around their historical average and divided by their standard deviation.

The median value of the mechanical nowcasts points to stable GDP growth in the third quarter of 2024

The informational content of the most recent survey and financial data can be summarised by looking at the range of mechanical GDP predictions using one-indicator bridge models. **The median of the various predictions points to positive growth of 0.3% in the third quarter of 2024** (see Figure 6). The range has narrowed substantially compared with previous issues of the BCM but is still rather wide at roughly [-0.8;1.5]. The forecast distribution is quite symmetrical and does not point to significant upside or downside risks. It should be noted that the past forecast performance of these simple models suggests that individual predictions should be interpreted with caution, even under normal circumstances.

Figure 6

Histogram, in percentages, of one-indicator bridge model predictions using a broad set of survey and financial data and NBB nowcasting model predictions of real GDP growth in the third quarter of 2024



Source: NBB.
Note: The black line corresponds to the median of the one-indicator bridge model predictions of current quarterly GDP growth, while the red and orange lines correspond to the predictions of the BREL bridge model and the R2D2 dynamic factor model, respectively.

Economic activity is expected to expand by 0.2% in the third quarter of 2024

Of the NBB's more elaborate standard nowcasting models, BREL sees GDP growth at 0.3% while R2D2 predicts a contraction of 0.2% in the third quarter of 2024. An improved BREL model,[4] recalibrated to take into account the unusual volatility of the pandemic period, indicates a preliminary growth estimate of 0.2%. As always, these model-based estimates should be complemented by information gathered from other sources, as well as expert judgment.

In this regard, it should be stressed that while private demand and manufacturing output are likely to remain quite weak, second-quarter growth was affected by an exceptional asymmetric shock. It appears unlikely that value added of vehicle manufacturing will decline to the same extent in the third quarter (e.g. as the impact of the aforementioned bankruptcy on the growth rate should mostly unwind). As such asymmetric shocks are not sufficiently captured by macro models, this may imply a slight upward risk to growth. On that note, a potential resumption of vehicle manufacturing in the Brussels-Capital Region could boost growth by about 0.1 pp in the near-term.

All in all, a growth rate of 0.2% in the third quarter of 2024 appears the most plausible estimate. This is close to the median of the one-indicator model predictions and the BREL nowcasts. In addition to the aforementioned idiosyncratic risks associated with vehicle manufacturing, a potentially more favourable growth contribution from inventories, after two consecutive negative contributions to quarterly GDP growth, can also be regarded as an upward risk to this nowcast.

[4] We are currently finalising the operationalisation of this and other new nowcasting models and expect to formally introduce them in the December 2024 Business Cycle Monitor.