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REGIONAL GROWTH IN 2016-2020
- FLANDERS MAINTAINS GROWTH LEAD IN THE SHORT BUT POSSIBLY NOT THE LONG TERM -

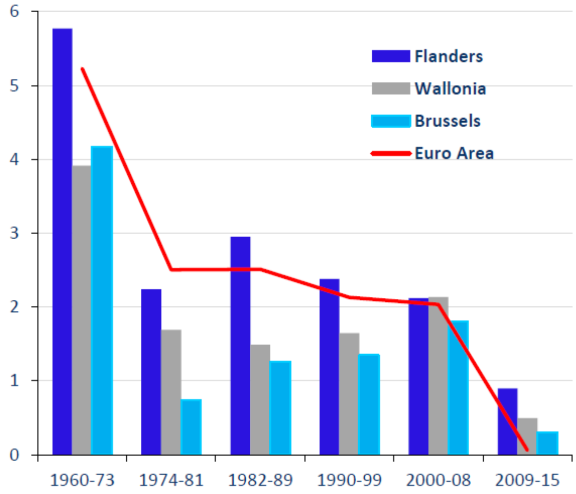
After the regional differences in growth had virtually disappeared in 2000-2008, the Flemish economy once again grew more rapidly than either the Wallonian or the Brussels economy during and after the financial crisis (2008-2015). The improved economic climate since 2013 has also ensured that the regional labour markets have picked up. A notable feature has been the relatively marked increase in the number of Brussels residents in employment, although in part that was attributable to the further increase in the numbers finding work outside the boundaries of the capital region. On account of its more open economy, Flanders will once again benefit more in 2016 from the European economic upturn than the other regions. Since the European recovery is likely to be on the modest side, however, this cyclical growth bonus is also likely remain minimal for Flanders. The terrorist attacks in March have weighed on growth in Brussels, but with the economic consequences likely to die out, the negative impact on growth for the year as a whole will remain limited. In the longer term the low productivity growth will cut across the potential growth of regional output, especially in Wallonia and Brussels. If both these regions benefit to the full from the labour market reforms that are needed in order to lift the employment rate structurally to a higher level, their potential growth rate in the medium term could even approach or even slightly top that in Flanders.

Divergent growth during and after the crisis

Gross regional product (the total value added within the territory of a region) in Flanders grew by an average of 0.9% per annum in real terms between 2008 and 2015, compared with 0.5% in Wallonia and 0.3% in the Brussels Capital Region. After the regional growth differences had virtually disappeared in 2000-2008, Flanders' systematic post-war growth lead on the two other regions therefore came back to the fore (graph 1). This was attributable in particular to the divergent level of activity in 2012-2013. In Belgium as a whole the serious deterioration in the international economy was translated from mid-2011 onwards into a sharp slowdown in growth and subsequently flatlining of the economy in 2012 and early 2013. Regionally this was reflected in a fresh recession of significance in Brussels and Wallonia, whereas Flanders continued to grow, albeit at a slower rate (graph 2). In Wallonia the contraction of economic activity in 2012-2013 was at its most pronounced in industry, and in Brussels in financial services.

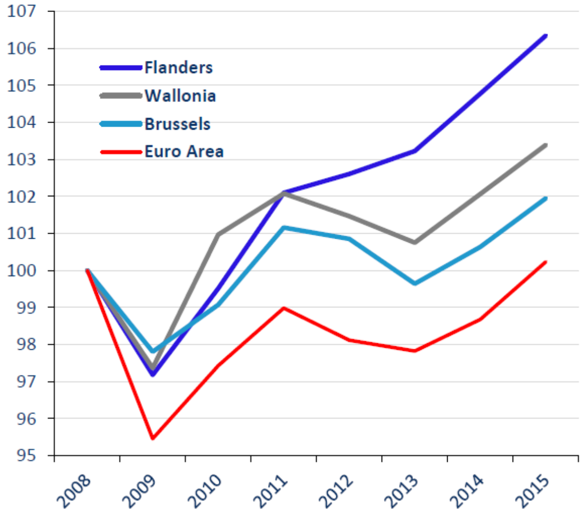
Graph 1 - Real growth gross regional product

(in % per year, period averages)



Graph 2 - Real gross regional product

(2008 = 100)

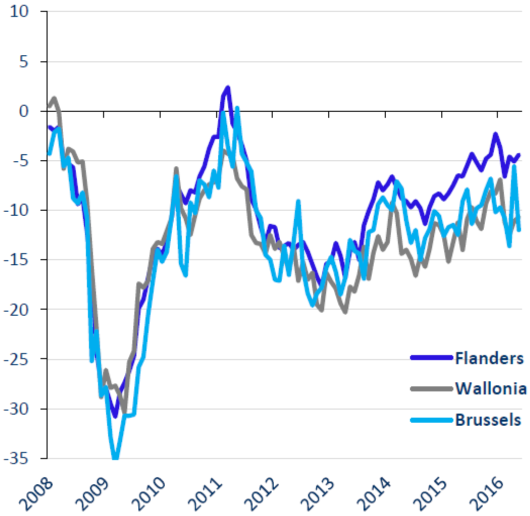


Source: NBB (INR); 2015: KBC estimate

The figures cited are drawn from the most recent Regional Accounts as published at the start of this year by the Belgian Institute for National Accounts (INR). They lag behind the available national GDP figures: the statistics for 2014 are a provisional estimate, while regional growth figures are not yet available for 2015. The 2015 figure in graphs 1 and 2 are therefore a KBC estimate based on the national growth figure that was already available for that year (1.4%). We are working on the assumption that the more open Flemish economy has been able to benefit a little more than either Wallonia or Brussels in 2015 from the European economic recovery, as it did in 2014. We are consequently estimating actual growth in 2015 at 1.5% for Flanders and at 1.3% for Wallonia and Brussels. Towards the end of the year, the Brussels economy – especially the hospitality industry, retail trade and leisure industry – was hit by the heightened terror threat following the attacks in Paris. This may well have depressed growth to some extent in the final quarter.

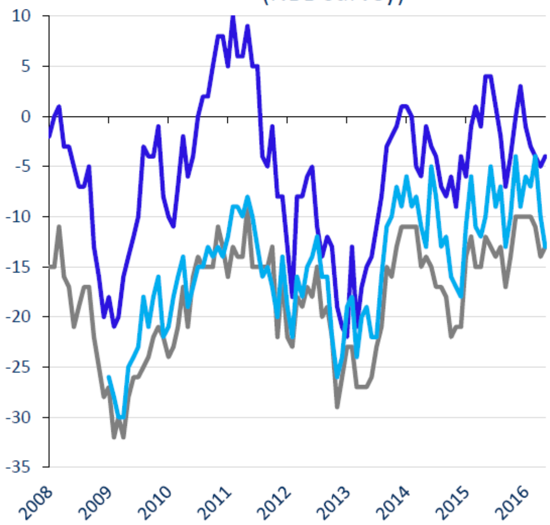
Graph 3 – Producer confidence

(NBB indicator)



Graph 4 – Consumer confidence

(NBB survey)



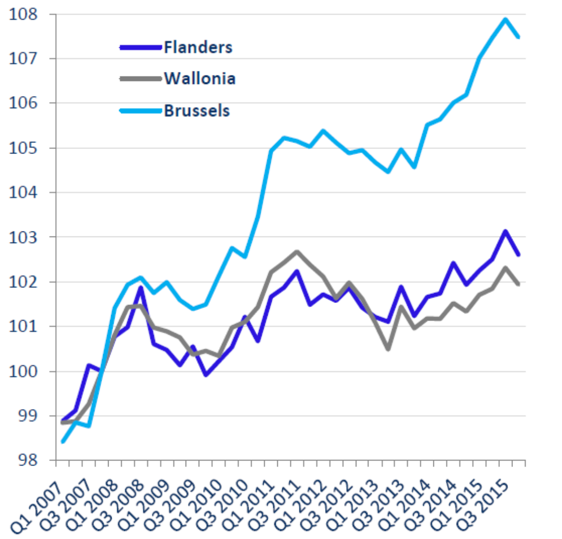
Source: NBB

In Brussels producer confidence had already fallen at the end of 2015 due to the terror threat. The business climate also deteriorated in Flanders and Wallonia in early 2016 (graph 3). At just 0.2%, first-quarter growth in Belgium as a whole was therefore on the weak side. Consumer confidence even fell sharply in the three regions. In March this was related to the announcement that extra austerity measures would be needed in order to keep the reform of public finances on track. In April the attacks in Brussels on 22 March were a factor (graph 4). With the exception of Brussels, May saw a slight improvement in both producer and consumer confidence. Flemish businesses were once again more positive about foreign orders in April/May, while in Wallonia the order position underwent a further deterioration.

Labour markets pick up

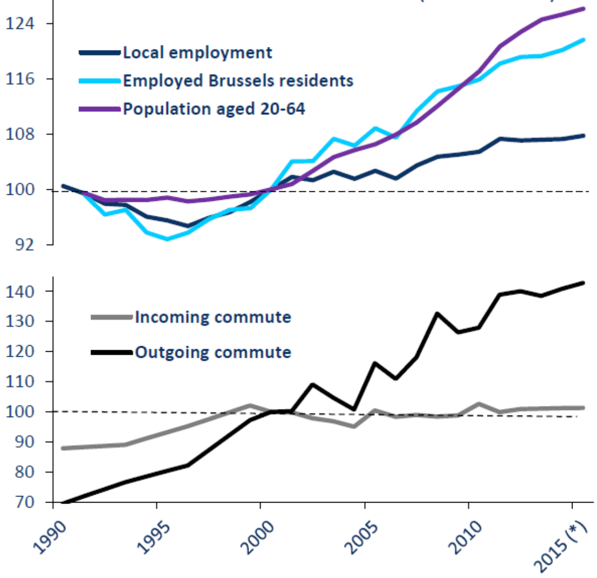
The improvement in the economic climate since early 2013 has also ensured that the regional labour markets have picked up. A notable feature in this regard was the relatively marked increase in the number of Brussels residents in employment, a trend that in fact goes back as far as 2008 (graph 5). The improved labour situation for Brussels residents did however take place against the background of below-average job creation in the Brussels-Capital Region itself. In the Brussels service sectors the number of jobs grew by just 0.3% per year in 2013-2015, as compared with 0.8% in Flanders and 0.6% in Wallonia. During this period industry shed some 1.5% of jobs each year in each of the regions. In net terms there has been barely any increase in local employment in the Brussels region in recent years. The growth of the working population in that region was, accordingly, primarily due to a further increase in the number of Brussels residents finding work outside the regional boundaries, especially in the periphery of the capital city (graph 6). That trend was also reflected in the Brussels employment rate. Until 2013 the growth of the working age population in Brussels exceeded that of the working population, so that the employment rate came down. From 2014 onwards that was no longer the case. In 2014-2015 the employment rate in Brussels rose by 2.3 percentage points, as compared with a virtual stabilisation in the two other regions.

Graph 5 – Number of wage-earners
(according to place of residence, Q4 2007 = 100)



Source: RSZ

Graph 6 - Demographics and Brussels' labour market (2000 = 100)

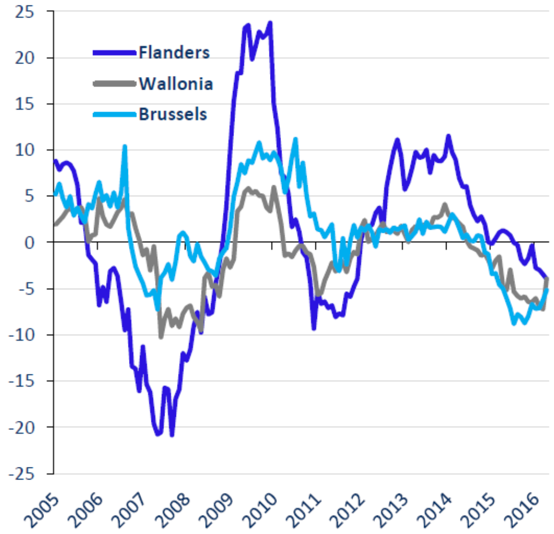


Source: Eurostat; (*) Estimate Federal Planning Bureau

The recent unemployment figures also point to a more favourable situation in Brussels (graph 7). In 2015 the number of unemployment benefit claimants among the Brussels population was on average 6.5% lower than in 2014. In Wallonia the fall amounted to 4.6%, and in Flanders to just 0.2%. In recent months, however, the annual change in the number of benefit claimants in the regions has been less divergent. The favourable labour market trends have also ensured that the Brussels gap on Flanders and Wallonia as regards the unemployment rate narrowed slightly (graph 8). The fall in the Brussels unemployment rate in 2015 by 1.6 percentage points was fairly spectacular. In Wallonia the fall amounted to just half that (-0.8 percentage point), while in Flanders it was minimal (-0.1 percentage point). The improvement applied to all 19 Brussels municipalities and was particularly marked among young people.

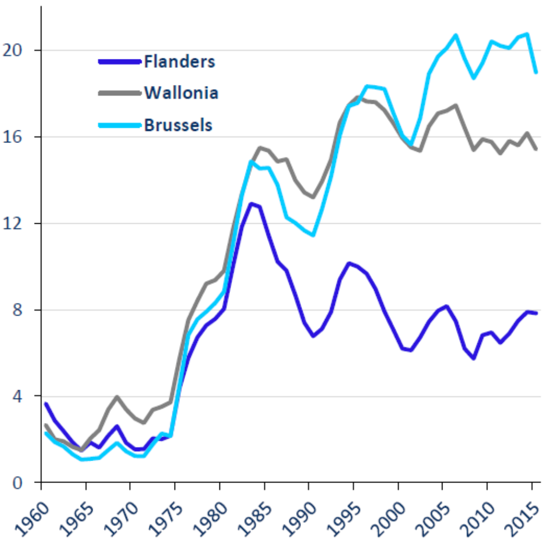
Graph 7 – Number of unemployed persons

(annual change in non-working job-seekers, in %)



Graph 8 – Unemployment rate

(in % of the labour force)

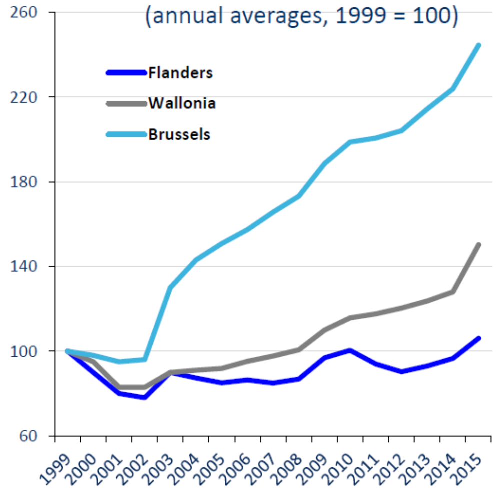


Source: Eurostat; VDAB; Forem; Actiris

Apart from cyclical factors, the sharp decline in unemployment in Brussels was also due to new employment measures, improved cooperation between the regional job placement services and an increasing number of unemployment benefit exclusions. In particular the measures taken by the Brussels administration in order to guide young people more effectively to a job under the so-called *Jongerengarantie* or Youth Guarantee appear to be bearing fruit. Young job-seekers will in future be called up more quickly by Actiris, the Brussels job placement service, and will be offered an entry-level placement more frequently. The increased number of exclusions is related to changes to the unemployment regulations and tighter controls on the availability of work. On account of the new law limiting the integration allowance introduced by the Di Rupo government in 2012 to a period of three years, nearly 30 000 young people in Belgium lost this type of benefit in 2015, a high proportion of them in the Brussels region. Similarly the qualifying requirements for the professional integration period – a waiting period of one year before someone can qualify for an integration allowance – have been tightened.

Graph 9 - Number of minimum subsistence allowance claimants

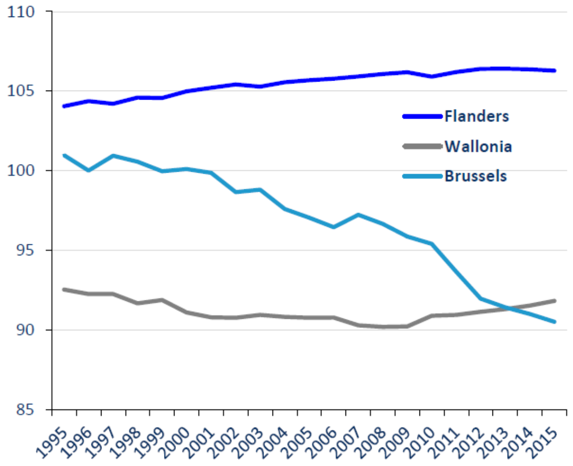
(annual averages, 1999 = 100)



Source: POD Maatschappelijke Integratie

Graph 10 – Disposable income per inhabitant

(Belgium = 100)

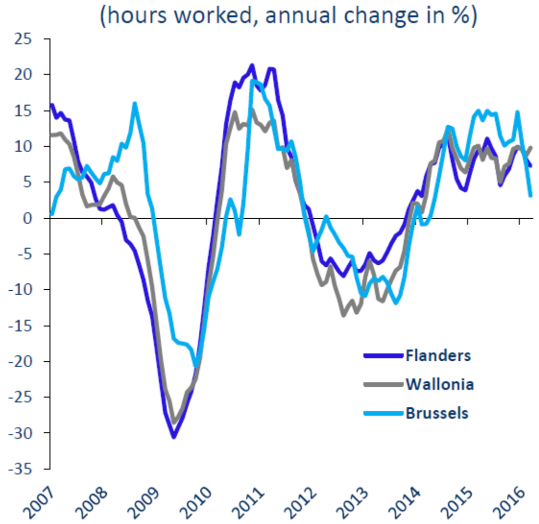


Source: Federal Planning Bureau (2014-2015 estimate)

The growing number of unemployment benefit exclusions has meant that increasing numbers of people have had to turn to national assistance. In 2015 the number of minimum subsistence allowance claimants in the regions increased by 9.9% in Flanders, 17.3% in Wallonia and 9.2% in Brussels. In Wallonia and especially Brussels this has accentuated the structural increase dating back as far as 2002 (graph 9). One in 20 Brussels residents aged between 18 and 64 is now in receipt of a minimum subsistence allowance, while in Wallonia the figure is nearly three per hundred inhabitants in that age group, and in Flanders one in every hundred. Together with the more degressive nature of unemployment benefits, the higher dependence on benefits has contributed towards the fact that the average income position of Brussels residents has fallen in relative terms compared with that of the Flemish and the Walloons. Average disposable income per inhabitant has even fallen since 2014 to below that in Wallonia (graph 10).

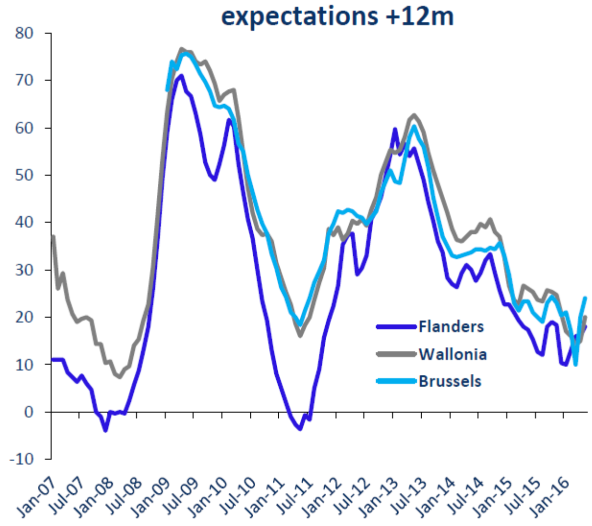
Graph 11 – Temporary employment activity

(hours worked, annual change in %)



Source: Federgon

Graph 12 – Consumers' unemployment expectations +12m



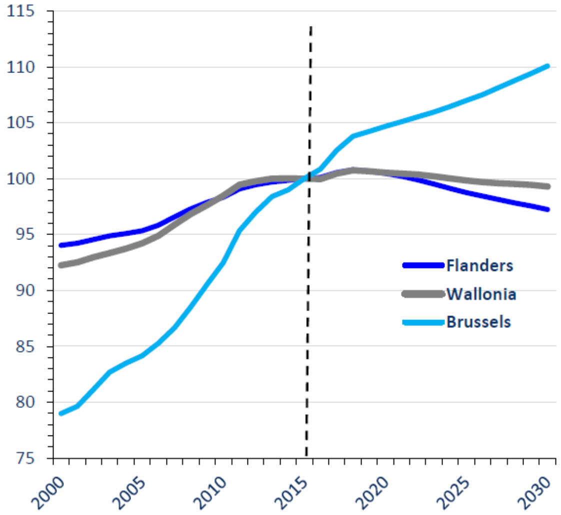
Source: NBB

Recent labour market indicators suggest that Brussels has of late lost something of its positive gloss. As a result of the terrorist attacks on 22 March the number of hours worked by agency workers has taken a serious hit (graph 11). Young people may well have been hit especially hard, since they are overrepresented in the temporary employment sector. Particularly among Brussels people, the attacks have once again slightly increased concerns about their future employment prospects (graph 12). All in all, however, these indicators remain at a reasonably favourable level. The fact that the negative economic consequences of the attacks are likely to be temporary leads us to suspect that the recovery of the labour market will be sustained in the coming quarters.

Regional growth outlook 2016-2020

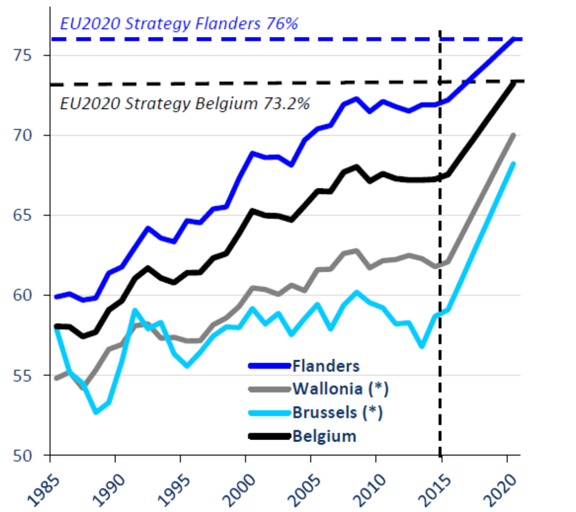
Now that the growth performance in Flanders has on average once again been relatively favourable, the question arises as to whether this will also remain the case in 2016 and beyond. In the short term, cyclical economic factors will work to the advantage of the Flanders region. On account of its greater openness, the Flemish economy generally benefits more than the other regions from an upswing in Europe. Since the further European recovery in 2016 is likely to be on the modest side, however, this cyclical growth bonus is also likely to remain minimal for Flanders. More specifically, the 1.4% growth we anticipate for Belgium as a whole in 2016 translates into 1.5% growth in Flanders and 1.4% growth in Wallonia. In the case of Brussels the attacks on 22 March dragged the forecast growth down to 1.2%. Since the consequences were largely concentrated in March and April and will probably now largely die out, the growth impact for the year as a whole will remain limited. As well as that, the sectors that were hardest hit – the hospitality industry, retail trade and the leisure sector – make up just a little over 3% of the total added value generated in the Brussels region.

Graph 13 – Working-age population
(population aged 20-64, 2015 = 100)



Source: Federal Planning Bureau; Eurostat

Graph 14 – Employment rate
(employed persons in % population aged 20-64)



(*) Wallonia and Brussels do not have separate EU2020 targets of their own. The assumption of an employment rate of 70% (Wallonia) and 68.2% (Brussels) is consistent with the EU2020 targets for Flanders (76%) and Belgium (73.2%)

In the somewhat longer term, regional demographic trends will be a factor determining the potential supply of labour in the region, as will any successful policies to jack up the labour force participation rate and productivity growth. According to the most recent estimate by the Federal Planning Bureau, the working-age population in Flanders and Wallonia will contract over the next 15 years by 2.8% and 0.7% respectively. In Brussels there will be a further increase of 10.1% (graph 13). The demographic impact on the workforce will therefore exert downward pressure on the growth potential of employment in Flanders and Wallonia. That trend can however be (partly) countered by further increasing the employment rate (i.e. the number of employed persons within the working-age population). Although Brussels will see its workforce potential increase in the coming years, it nevertheless also needs to increase its much too low employment rate.

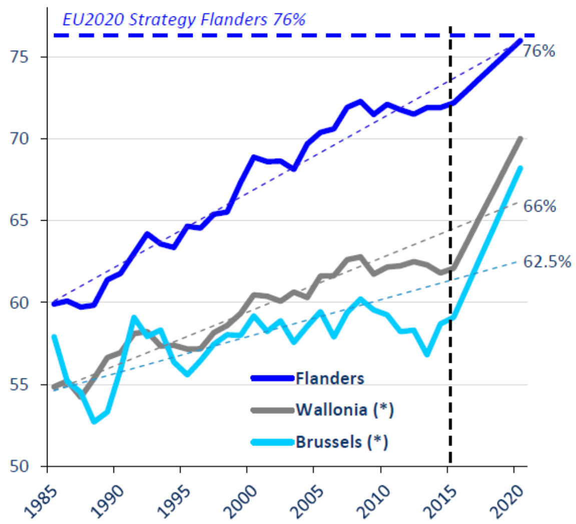
As part of the European EU2020 Strategy, Belgium wants to set 73.2% of its 20-64-year-olds to work by 2020. Flanders has adopted a target of its own of 76%. Wallonia and Brussels have not done so, but in order to contribute towards the national target they would need to jack up their employment rates from 62% and 59% respectively to around 70% and 68% in 2020 (graph 14). Against the background of the demographic trends forecast by the Planning Bureau, this will require an increase in the number of employed Walloons and Brussels residents of around 35 000 and 18 000 per year respectively, i.e. an annual growth of at least 2.5% (Wallonia) and 3.9% (Brussels). That would of course be a highly ambitious target; between 2000 and 2015 the number of employed Walloons and Brussels residents increased on average by just 0.7% and 1.6% per year respectively (table 1).

Table 1 - Scenarios for employment rate and persons employed

	Scenario EU2020 **2016-20**	Scenario KBC (*) **2016-20**
Flanders		
Employment rate 20-64 (end of period)	76.0	76.0
Change in persons employed per year (in '000)	31.6	31.6
Change in persons employed per year (in %)	1.1	1.1
Wallonia		
Employment rate 20-64 (end of period)	70.0	66.0
Change in persons employed per year (in '000)	35.0	18.0
Change in persons employed per year (in %)	2.5	1.3
Brussels		
Employment rate 20-64 (end of period)	68.2	62.5
Change in persons employed per year (in '000)	17.9	9.2
Change in persons employed per year (in %)	3.9	2.1

(*) On the assumption that the regional employment rates will develop on a trend basis, i.e. in 2020 76% in Flanders, 66% in Wallonia and 62.5% in Brussels

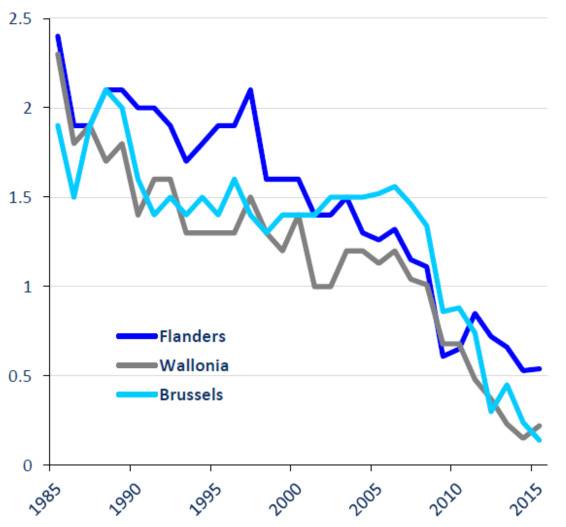
Graph 15 – Employment rate
(employed persons in % population aged 20-64)



A more realistic but still ambitious target would involve ensuring that the trend of recent decades is sustained. That would increase the Wallonian and Brussels employment rates to 66% and 62.5% respectively in 2020 and would imply an annual growth in the number of employed Walloons and Brussels residents of 1.3% and 2.1% (table 1 and graph 15). In the case of Brussels a significant element of the job growth that this requires will need to be realised outside the Brussels-Capital Region. The growth of regional employment within the city of Brussels itself amounted in 2000-2015 to just 0.5% per year, or fewer than 3 000 jobs. In the case of Flanders achieving the EU2020 target it has set itself would appear feasible. It would nevertheless require the working population to increase by 1.1% per annum up to 2020, more than the average 0.7% achieved in 2000-2015. By way of comparison: in its latest medium-term regional growth forecasts the Planning Bureau assumes an annual increase in employment of 0.8% in Flanders and 0.6% in Wallonia and Brussels. These figures seem too low to us, given that the regions will benefit from labour market reforms that will increase their local employment rates. We assume a yearly potential employment growth in 2016-2020 of 1.1% in Flanders and 1.3% in Wallonia, in line with the above scenario for their employment rate. In case Brussels can combine a local employment growth of the same order as in Wallonia (1.3% per year) with a continuing employment of Brussels residents outside its own boundaries, then an increase in the working population in that region as presented in table 1 seems not unrealistic to us.

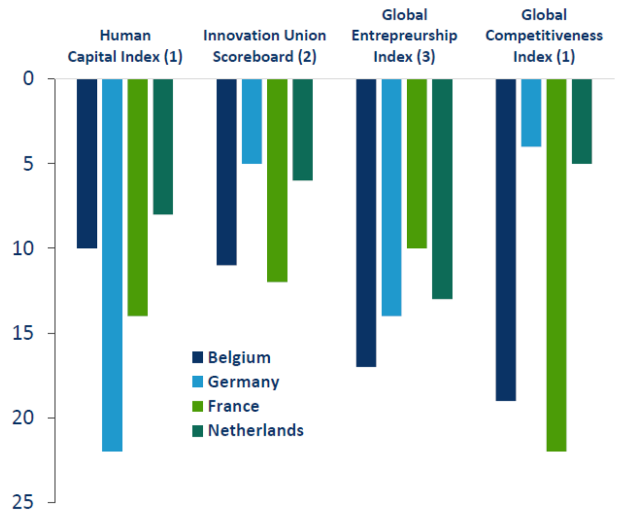
Apart from employment, productivity growth is also a driving force behind economic growth. In recent decades the growth in labour productivity has been in a secular decline (graph 16). Among other things this was because new jobs were generated largely in the service sectors, where the productivity level is generally lower than in industry. The Planning Bureau's forecasts are based on annual productivity growth of 0.9% in Flanders and 0.8% in Brussels. This hypothesis strikes us as overly optimistic. The increase in employment will continue to be concentrated in the service sector in the coming years, so that productivity growth is likely to remain low. The increasing employment moreover requires the engagement in the production process of greater numbers of less well educated and also older workers, and that too is likely to be coupled with downward pressure on average productivity growth.

Graph 16 - Real growth of labour productivity
(10-year moving average, in %)



Source: NBB (INR)

Graph 17 - Levers of productivity growth
(rank order position, 2015)



Source: (1) World Economic Forum; (2) European Commission; (3) Global Entrepreneurship and Development Institute

This needs to be offset by productivity gains from greater efficiency and innovation. That assumes that the regions will do something about their relative weaknesses. Although each region has its own separate problems weighing on productivity (e.g. traffic congestion in Flanders in Brussels; low productivity in services and poorer education in Wallonia), they generally score less well than neighbouring countries on significant levers of productivity growth. Relative improvement remains possible especially in the fields of innovation, entrepreneurship and competitiveness (graph 17). Taking everything together we estimate that the productivity growth in the three regions in the medium term more conservatively at an average of 0.4% per year in Flanders and 0.3% in Wallonia and Brussels. If Wallonia and Brussels are able to combine this with a somewhat stronger relative growth of employment, this means that the potential rate of expansion of regional production in the three regions would end up at virtually the same level in the medium term (table 2). If Wallonia and Brussels take full advantage of the labour market reforms that are currently under way and as needed to lift the employment rate to a structurally higher level, the potential growth rate could even slightly exceed that in Flanders.

Table 2 - KBC outlook for real growth of gross regional product (in %)

	2015	2016	2009-2015 (*)	Potential growth 2016-2020 (*)		
					Employment growth	Productivity growth
Flanders	1.5	1.5	0.9	1.5	1.1	0.4
Wallonia	1.3	1.4	0.5	1.6	1.3	0.3
Brussels	1.3	1.2	0.3	1.6	1.3	0.3
Belgium	1.4	1.4	0.7	1.5	1.2	0.3

(*) Per year, period averages

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