BELGIAN DEBT AGENCY

Participating Primary and Recognised Dealers:
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NationalBank OF BELGIUM Eurosystem

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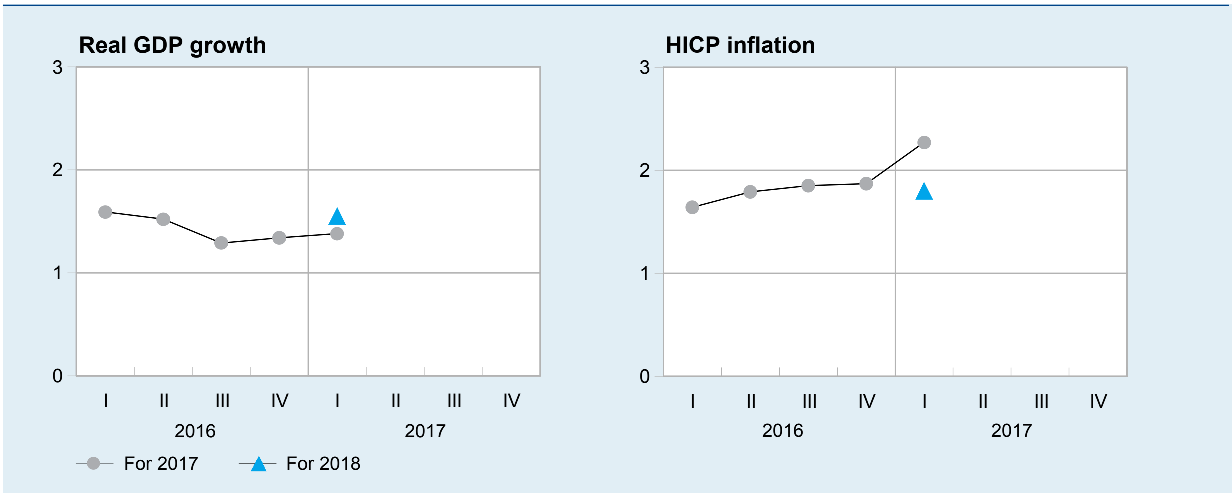
- Economic activity is expected to expand at a steady but moderate pace in Belgium and in the euro area. According to the consensus forecast, Belgian GDP should grow by 1.4 % in 2017 and 1.5 % in 2018. Fuelled by energy prices, HICP inflation Belgium is set to peak at 2.3 % in 2017, well above euro area outcomes. It should come down to 1.8 % in 2018 (see Macroeconomic Developments).
- Significant progress has been achieved recently in structural reforms. They should be complemented to put Belgium on a stronger footing in a rapidly evolving environment (see Special Topic).
- Since the beginning of the year, the Belgian Debt Agency has issued its new 10-year benchmark and two additional 7-year and 40-year tranches. Together with an additional auction, it has completed 40 % of its 2017 funding programme (see Treasury Highlights).

Consensus: Average of participants' forecasts

	2016		2017 p				2018 p	
	Belgium	Euro area	Belgium		Euro area		Belgium	Euro area
Real GDP[1]	1.2	1.7	1.4	(1.3)	1.6	(1.4)	1.5	1.6
Inflation (HICP)[1]	1.8	0.2	2.3	(1.9)	1.7	(1.3)	1.8	1.4
General government balance[2]	-2.8	-1.7	-2.3	(-2.2)	-1.6	(-1.7)	-2.1	-1.5
Public debt[2]	106.6	91.5	106.1	(106.1)	89.7	(89.9)	105.4	88.7

Numbers in parentheses refer to the previous consensus forecast of January 2017.
(1) Percentage changes.
(2) EDP definition; percentages of GDP. Figures for 2016 are estimates.

SUCCESSIVE FORECASTS FOR BELGIUM



Source: Belgian Prime News.

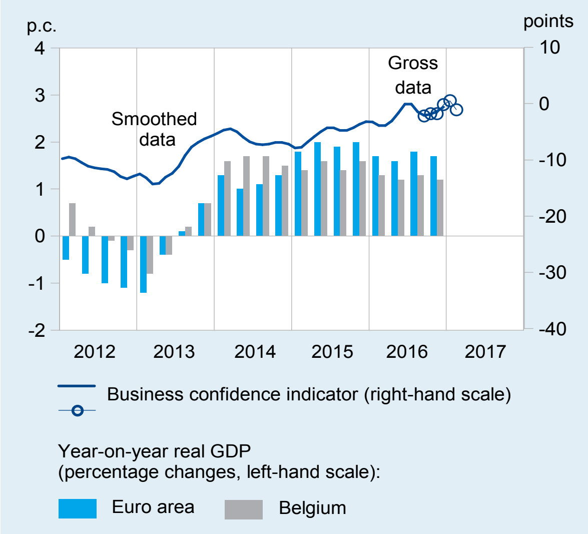
Macroeconomic Developments

Despite an unusual string of economic, political and security events in 2016, economic activity in the euro area has proven resilient, with growth even accelerating a little in the second half of the year and job creation gaining further momentum. Looking ahead, uncertainty remains high, not least about the format for the UK's exit from the EU and the future economic policies of the US Administration; elections are coming up in several large European countries, adding to policy uncertainty. Very favorable conditions – low oil prices, a cheap euro – that have supported growth in the last few years are now fading away and central banks will eventually start to withdraw from their highly accommodative monetary policy stance, if the situation continues to improve and inflation will converge in a sustainable manner towards the medium-term objective.

In Belgium, GDP growth edged up to 0.5% in the final quarter of 2016, mainly driven by domestic demand and, more particularly, by business investment. The labour market remains very healthy, continuing the upward trend started in mid-2013. Job creation is generalised across all branches, which may be another sign, on top of the cyclical upswing, that labour market policies are bearing fruit. Even though the business and consumer confidence indicators dropped back slightly in the first quarter, they still point to a further steady expansion of activity. **According to the consensus forecast, Belgian GDP is expected to grow at a pace of 1.4 % in 2017 and 1.5 % in 2018.** In the euro area, GDP should increase by 1.6% in 2017 and in 2018. The (limited) negative growth gap with the euro area is mainly due to fiscal consolidation measures that imply a lower increase in public expenditure. Private consumption growth, which has been curbed in Belgium in recent years in a context of wage moderation policies and several tax hikes, is set to recover and gradually catch up with the pace in the euro area.

Mainly fuelled by rising energy prices, HICP inflation peaked to 3.3 % in February in Belgium, clearly above euro area standards. **Belgian inflation is forecast to reach 2.3 % on average in 2017 before slowing down at 1.8 % in 2018.** The stronger inflation dynamics may be traced back to the (structural) higher sensitivity of Belgian inflation to oil prices and to the various increases in indirect taxes. In addition, services inflation remains persistently high, despite the unprecedented wage moderation policies implemented in recent times.

GDP GROWTH AND BUSINESS CYCLE INDICATOR



Sources: EC, NAI, NBB.

INFLATION (HICP)
(annual percentage changes)

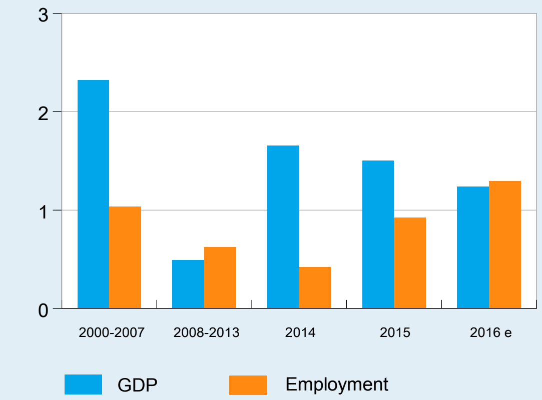
Source: EC.

Coming down from 2.8 % in 2016, the Belgian public sector deficit should work out at 2.3 % in 2017 and 2.1 % in 2018. Some additional consolidation efforts would thus be required to comply with the path set out in the budgetary plans submitted by the Belgian authorities to the EC. The BPN participants anticipate slight inflexion in the Belgian public sector debt, which should decline from 106.6 % of GDP in 2016 to 105.4 % in 2018.

Special Topic: Belgian economy on sounder foundations: major progress achieved should be further consolidated

Like the euro area, Belgium has faced a climate of great economic uncertainty over the last years, against the backdrop of a slowdown in global trade, geopolitical uncertainty and waves of uncertainty in the financial markets. Even though Brexit has had little impact up to now, Belgium has significant trade exposure to the UK. Also, GDP growth was tested by the repercussions of the terrorist attacks in Paris in November 2015 and in the Brussels area on 22 March 2016. Nevertheless, growth proved resilient overall. It came to 1.5 % in 2015 and 1.2 % in 2016, as economic activity was temporarily weak at the beginning of the year.

ECONOMC GROWTH AND JOB CREATION
(average annual growth in %)



Sources: NAI, NBB.

Progress in the structural reforms is bearing fruit

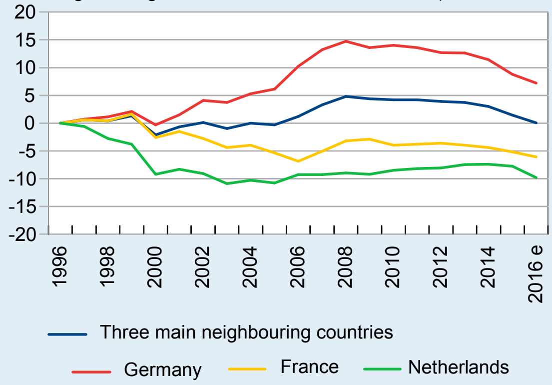
As recognised by both the IMF and the European Commission in their recent country reports, this resilience was at least partly supported by the progress made with the structural reforms undertaken since 2011. Those reforms aim to limit the impact of adverse economic conditions and to remedy the structural weaknesses of the Belgian economy.

In particular, the pension reform law enacted in 2011 and 2015, including measures to tighten up the conditions for early retirement, have contributed to reduce the number of labour market exits in the 55-plus bracket. Through their combined effect of stronger potential output and lower ageing-related budgetary costs, those reforms have significantly improved the long-term sustainability of public finances.

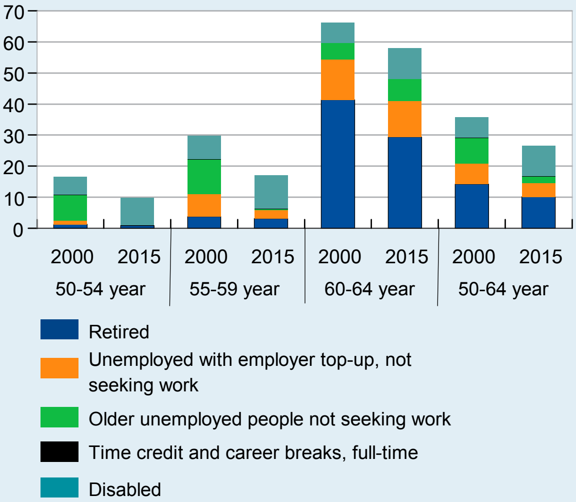
Measures have also been taken in the past two years to consolidate the wage moderation efforts. They include the temporary suspension of indexation and the implementation of the first stage of cuts in employers' social security contributions embodied in the so-called tax shift. According to the Central Economic Council, the hourly wage gap that has accumulated since 1996 compared to the three main neighbouring countries was closed completely in 2016. The tax shift measures also comprise a reduction in the tax wedge on labour income, focused on low wages, which reinforces the financial incentives to work.

STRUCTURAL REFORMS HAVE AN IMPACT ON ECONOMIC DEVELOPMENTS

Private sector's hourly labour cost differential with neighbouring countries
(percentage differences compared with the three main neighbouring countries, cumulative since 1996)



Reduced early retirement from the labour market among 50-64-year olds
(in % of the corresponding population



Sources : CEC, NBB.

Together with the continuing recovery of economic activity, those measures have contributed to strong job creation and a broad-based improvement in the labour market. Employment grew by 1.4 % in 2016 and unemployment declined across all categories of people: low-skilled, youth and older-aged short-term as well long-term unemployed.

Looking forward, additional stages of the tax shift are to be phased in the next three years. The law governing wage formation in Belgium has been amended with a view to preventing any new divergences in wage levels from emerging vis-à-vis the three main neighbouring countries, and to ensuring that wage-setting makes the maximum contribution to job creation. In January 2017, the social partners concluded an interprofessional agreement in line with that; the maximum margin for real wage increases beyond indexation is set at 1.1 % for 2017 and 2018 combined.

Consolidating the restored competitiveness and safeguarding the sustainability of public finances

For the future, it is necessary to make every effort to consolidate Belgium's restored competitiveness. At the same time, progress must be achieved in fiscal consolidation. Finally, to foster potential growth, the economic fabric needs to be made more productive, more dynamic and more inclusive.

Indeed, some developments such as the relatively high level of inflation in Belgium call for vigilance. Despite the moderation of labour costs, inflation has risen from 0.6 % in 2015 to 1.8 % in 2016, a level cleary higher than in the euro area (0.2%). That is due in part to the increase in indirect taxes under the tax shift, and to price rises resulting from the fiscal consolidation efforts undertaken by various governments. Together, those factors have driven up inflation by around 1 percentage point. Furthermore, inflation in services has reached around 2 % in each of the past five years and has also systematically outpaced services inflation in the three neighbouring countries. The working group set up by the Minister of the Economy to determine the causes of the high inflation in services in Belgium has identified specific issues in the telecoms sector and in restaurants. Wage-setting and pricing therefore not only have their own roles to play in safeguarding competitiveness, they also complement one another to a very considerable degree.

The reduction of the budget deficit stalled in 2016. Yet public finances benefited from a further decline in interest charges. Continued control over expenditure was in fact thwarted by a number of temporary factors and by the exceptional efforts made to combat terrorism and to accommodate asylum-seekers. Together, these last two factors represented 0.2 % of GDP. Revenues declined because of the reductions in taxes on labour which were only partly offset by an increase in other taxes. The debt ratio rose to 106.6 % of GDP. Bringing down the public debt sufficiently quickly is needed to provide the necessary buffers and scope to address the challenges ahead, particularly in order to absorb the remaining costs of population ageing and safeguard social protection in the long term.

In an environment marked by globalisation and technological change, strengthening productivity growth at macroeconomic level entails more innovation, but also better dissemination of innovations and a more fluid allocation of labour and capital. Investment in R&D in Belgium is heavily concentrated on a small number of sectors and firms. Belgium has a low rate of both creation of new businesses and destruction of existing ones, and the reallocation of resources here has appeared to be less a source of productivity gains in recent years. In that regard, the low level of entrepreneurship is an impediment, but the tide seems to have turned recently. More new businesses are starting up, and more workers are adopting self-employed status. The fluidity of the reallocation process should benefit from the elimination of unnecessary administrative, legal and fiscal barriers, an effective and transparent regulatory framework, and efficient public administration.

Despite improvement in the labour market, some people, particularly the less skilled, the young, and residents from non-EU countries, face greater difficulty in gaining or maintaining a foothold in the labour market. The action taken by the Regions and Communities should be reinforced to improve education for vulnerable groups and provide improved technical and vocational education. Owing to the extension of working life, it is also essential to invest in lifelong training.

Potential growth and productivity could also benefit from a more efficient infrastructure, especially in mobility and energy supply. In this respect, a national plan for strategic investment has been announced by the federal government and should be worked out with the involvement of the regional entities.

Putting Belgium on a stronger footing

The work done recently to put Belgium on a stronger footing in view of structural challenges ahead and to better withstand the shocks and uncertainties surrounding economic developments has already started to bear fruit. However, all stakeholders should be mobilised to further establish an environment based upon sound macroeconomic policies, sustainable fiscal prospects and an efficient and flexible economy. Offering greater opportunities to everyone, in a dynamic and open economy, is the best and only way to overcome the prevailing troubles and grasp the benefits of a rapidly evolving world.

Treasury Highlights

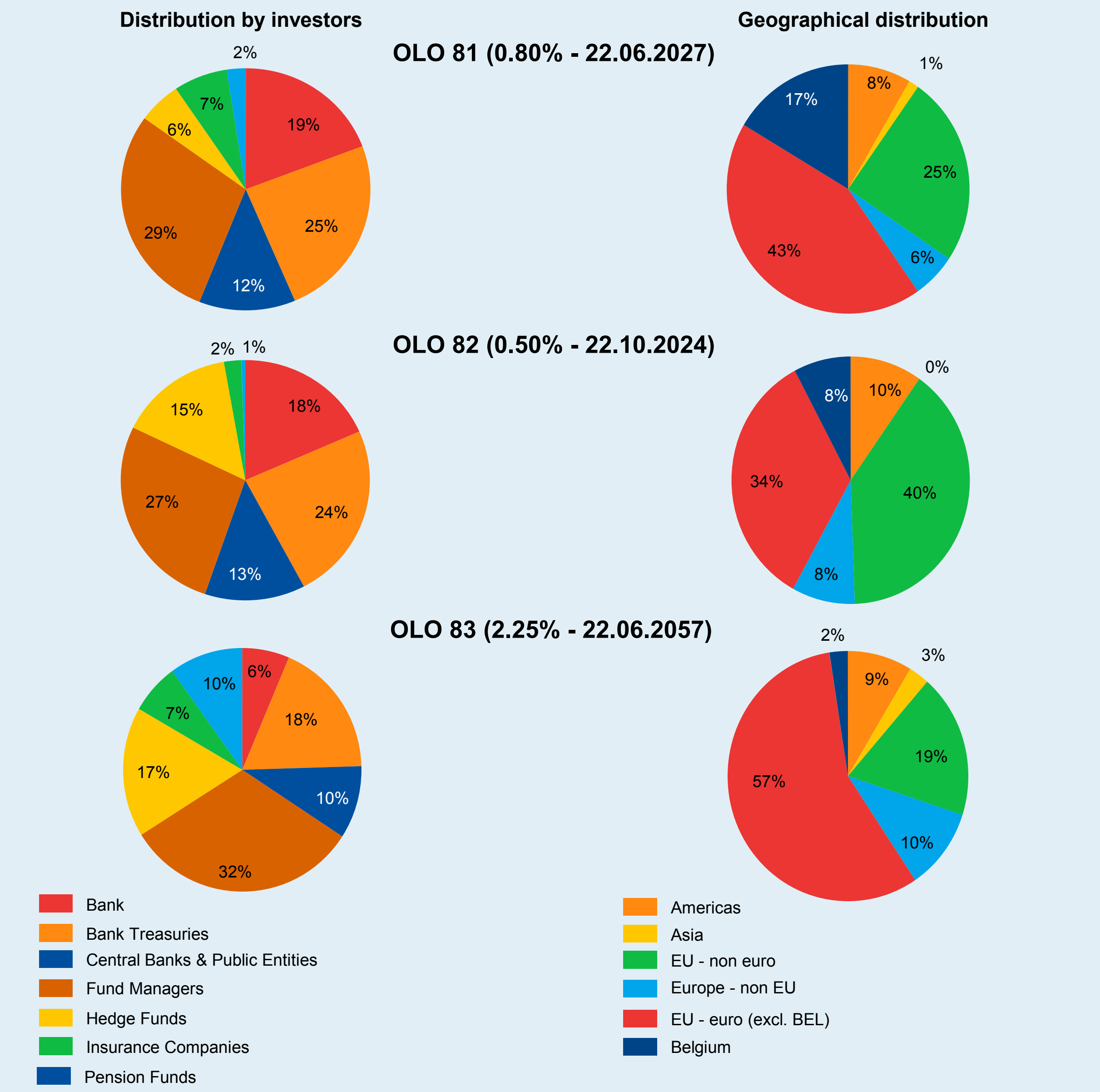
In January, Belgium started off its € 39.25 billion long-term funding programme with the traditional launch of its new 10-year benchmark. The € 6 billion OLO 81 – 0.80 % 22/06/2027 – was issued on 17 January 2017 at a spread of MS+10bps. For the first time ever, Belgium was able to issue € 6 billion of its 10-year benchmark, with a fine geographical distribution and a book size of almost € 21.5 billion.

Besides the new 10-year benchmark, Belgium also organised a dual-tranche issue in February, comprising new 7-year and 40-year lines.

The new € 3 billion OLO 82, due 22 October 2024, pays an annual coupon of 0.50 % and was priced at a flat spread against the interpolated mid-swap reference rate, implying a reoffer yield of 0.508 %.

The new € 3 billion OLO 83, due 22 June 2057, pays an annual coupon of 2.25 % and was priced at a spread of +87bps against the interpolated mid-swap reference rate, implying a reoffer yield of 2.228 %.

Distribution of the new OLO at issuance



Source: Belgian Debt Agency.

The auctions scheduled for 23 January and 20 February were cancelled.

Moreover the Treasury has issued € 4 billion through the auction of 20 March, tapping the OLO 81 (2027), OLO 76 (2038) and OLO 60 (2041).

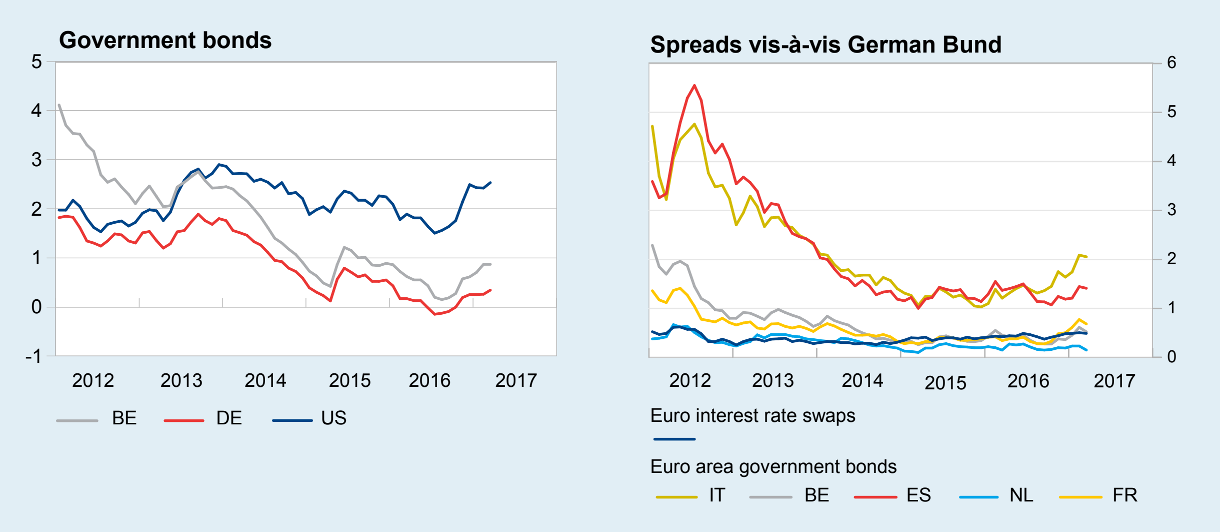
So far, there have been no EMTN or *Schuldscheine* issues.

Belgium has therefore already issued € 16.0 billion, corresponding to 40.9 % of its € 39.25 billion funding target.

In terms of portfolio structure, the average life of the portfolio is now 9.15 years (end-February) and it has an implicit yield of 2.53 %.

Government Securities Market

10-YEAR INTEREST RATES
(percentage points, monthly averages)

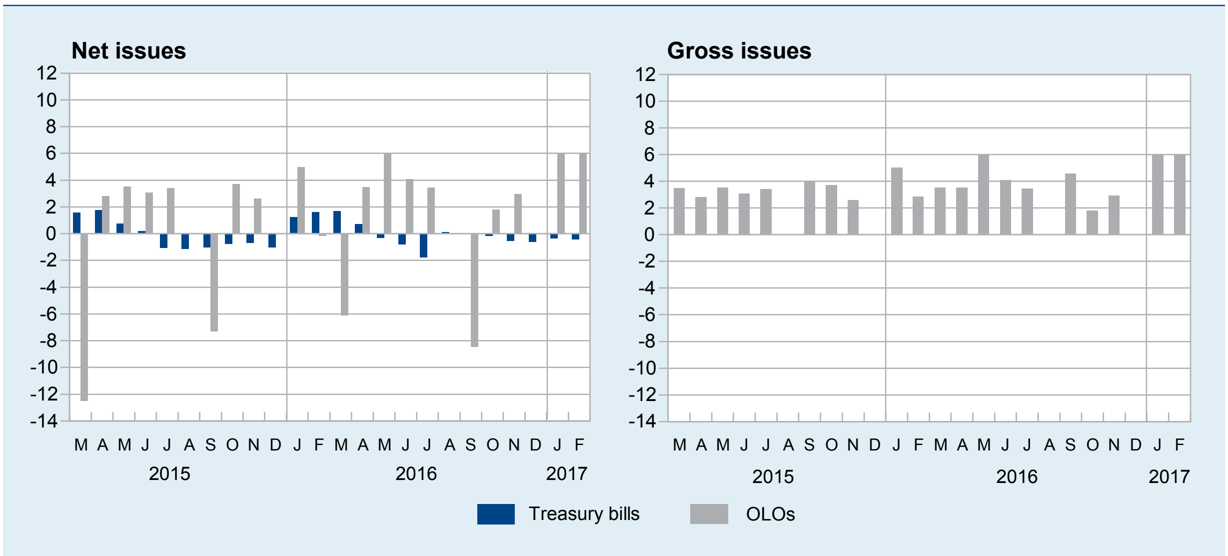


Sources: BIS, Datastream.
Average over the first 20 days for March 2017.

Between December 2016 and mid-March 2017, long-term sovereign bond yields continued to increase in the euro area, albeit at a slower pace than in the previous months. However, developments were heterogeneous across the euro area. Ten-year yields increased by 9 bp in Germany, to reach 0.34 % on average in March, while they rose by 25 bp in Belgium, to 0.87 %. In the US, ten-year yields remained relatively stable; edging up by a mild 4 bp to 2.53 % despite the FOMC's decision to raise the target range for the federal fund rates to 0.75% - 1%.

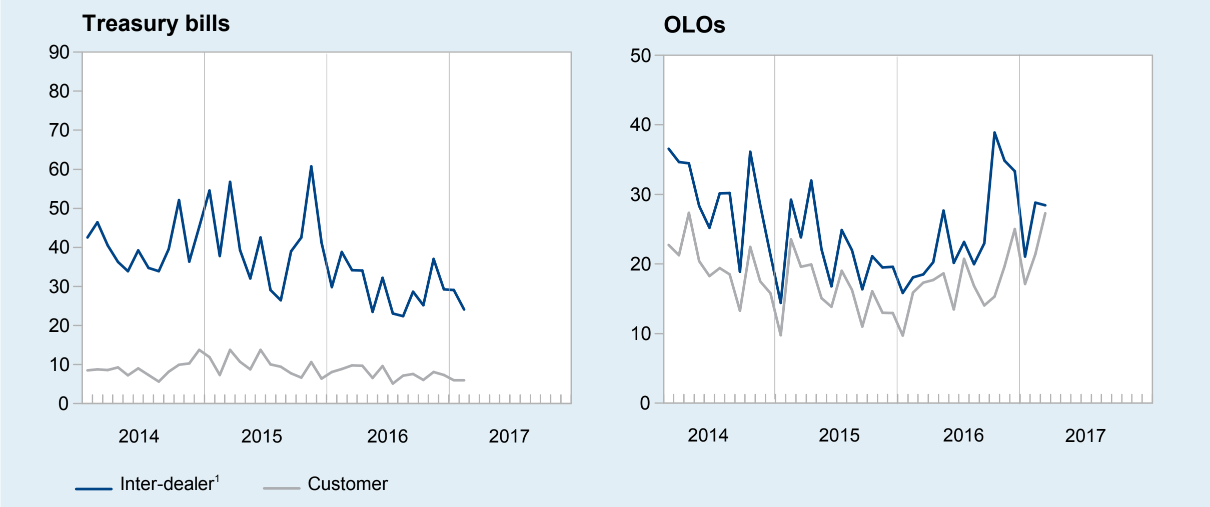
Over the period under review, long-term euro area sovereign spreads vis-à-vis Germany remained relatively stable in some countries, such as Austria, Finland and the Netherlands, whereas they continued to widen in other countries, especially those with relatively low ratings, mainly as a result of political uncertainty. In France, the ten year spread increased by 18 bp reaching 68 bp in March in the context of the upcoming presidential election. In Italy and Spain, ten-year spreads increased by respectively 41 bp and 22 bp to stand at 205 bp and 141 bp in March. In Belgium, the ten-year spread rose by 16 bp to 52 bp in March. Over the review period as a whole, sovereign bond yields showed some volatility.

PRIMARY MARKET
(billions of euros)



SECONDARY MARKET TURNOVER

(As reported by primary and recognised dealers to the Treasury, billions of euros)



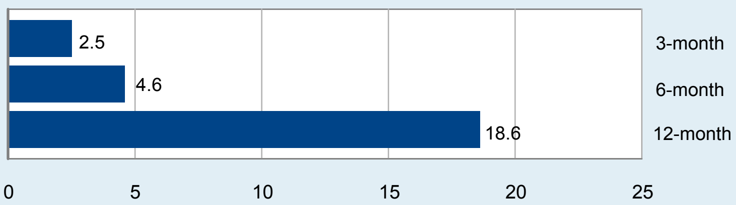
¹ Please note that inter-dealer turnover is double-counted in these figures.

OUTSTANDING AMOUNTS AND TURNOVER

(billions of euros)

TREASURY BILLS

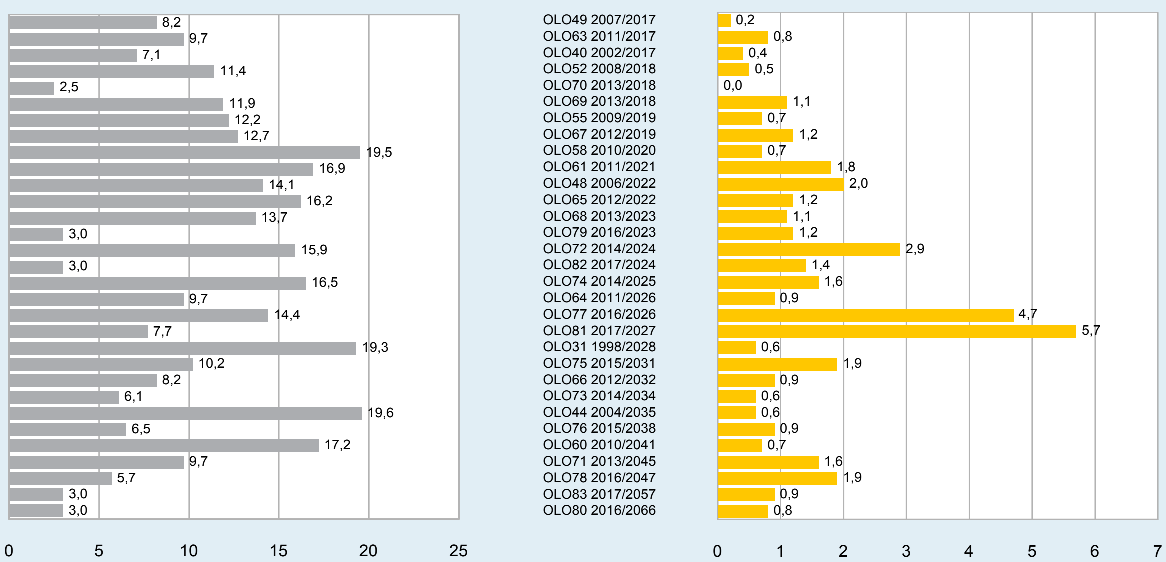
Nominal outstanding amounts at end of February 2017



OLOs

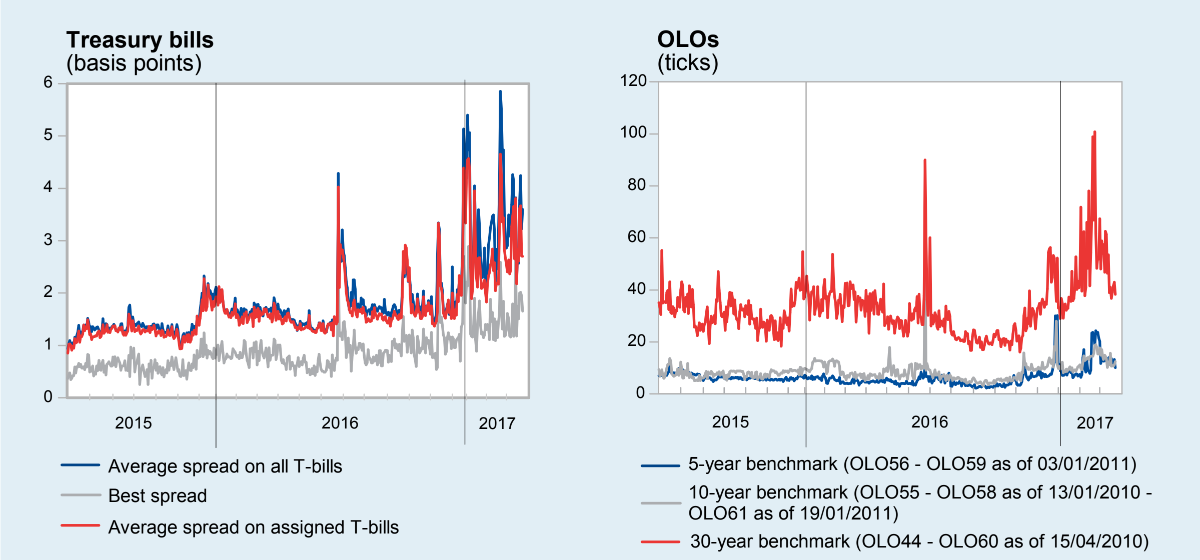
Outstanding amounts at end of February 2017

Outright turnover in February 2017



Source: Belgian Debt Agency.

BEST BID/OFFER SPREADS[1]



Source: Treasury.
[1] As reported by three electronic platforms (MTS, Broker Tec and BGC eSpeed).

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