BELGIAN DEBT AGENCY

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NationalBank OF BELGIUM
Eurosystem

Belgian Prime News

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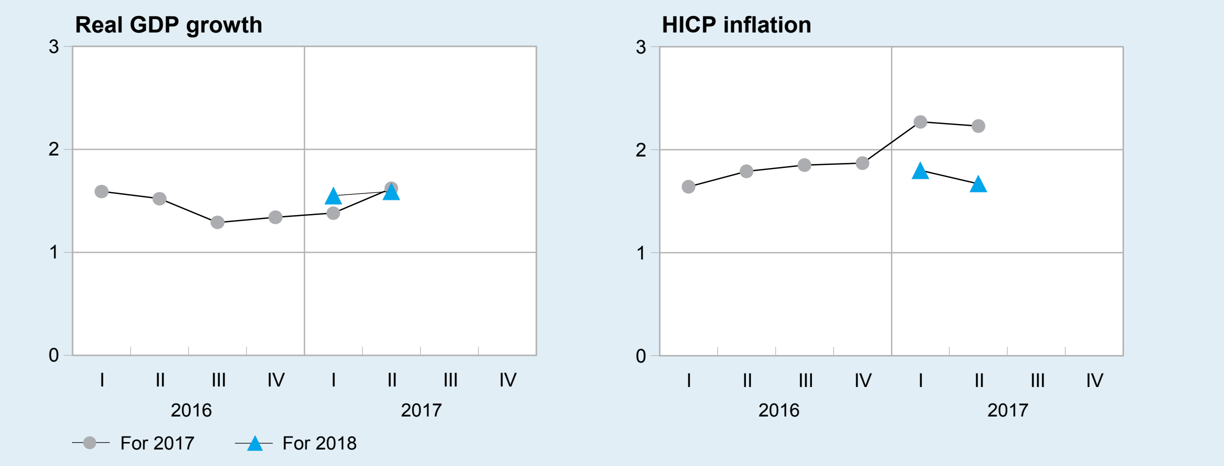
- Further stable GDP growth expected in Belgium (BPN Consensus: 1.6 % in 2017 and in 2018), as well as the euro area. HICP inflation Belgium (2.2 % in 2017, 1.7 % in 2018) should converge downwards towards the euro area inflation rate as base effects from tax and regulated price increases unwind (see Macroeconomic Developments).
- Public debt back on a slight downward trend. Additional measures in the budget for 2018 and 2019 should reinforce this movement (see Special Topic).
- The Belgian Debt Agency's activities have been going smoothly since the beginning of the year. 55 % of the funding programme had been completed by end-May (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	1.6 (1.4)	1.8 (1.6)	1.6 (1.5)	1.6 (1.6)
Inflation (HICP)(1)	1.8	0.2	2.2 (2.3)	1.6 (1.7)	1.7 (1.8)	1.3 (1.4)
General government balance(2)	-2.6	-1.7	-2.1 (-2.3)	-1.4 (-1.6)	-2.0 (-2.1)	-1.3 (-1.5)
Public debt(2)	106.0	91.5	105.1 (106.1)	89.3 (89.7)	104.3 (105.4)	88.1 (88.7)

Numbers in parentheses refer to the previous consensus forecast of March 2017.
(1) Percentage changes.
(2) EDP definition; percentages of GDP.

SUCCESSIVE FORECASTS FOR BELGIUM



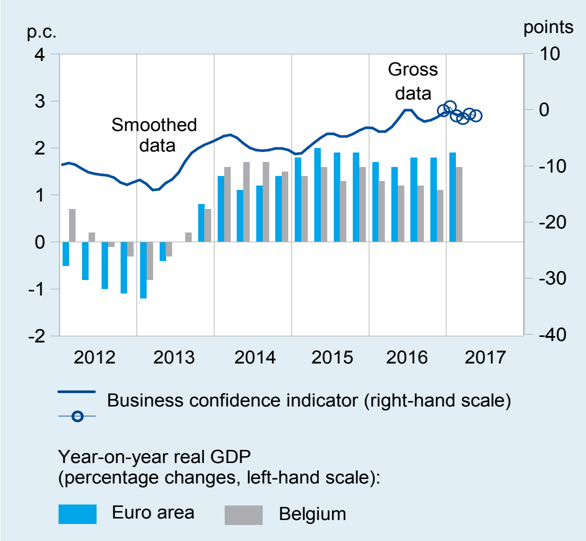
Source: Belgian Prime News.

Macroeconomic Developments

So far in 2017, the euro area has progressed further on the path of moderate growth that it has been on for more than three years now. Although still supported by an accommodative monetary policy, the recovery has widened in terms of drivers, as both domestic demand and exports are contributing favourably. In general, international institutions' and the private sector's forecasts converge in expecting this scenario to continue apace over the rest of current year and in 2018. But while activity, employment and demand are gaining momentum, inflation is still running below target, owing to subdued domestic cost developments.

In Belgium as in the euro area, GDP growth reached 0.6 % in the first quarter of 2017, slightly above most expectations. Domestic activity benefited from the combined support of private consumption, housing and business investment, and exports, while import dynamics remained strong too. The labour market also improved further, as the unemployment rate subsided below 7 %. In the period up to June, business and consumer confidence indicators stabilised at a level consistently above their historical averages. Against this backdrop, the consensus forecast was revised slightly upwards in 2017 (+0.2 percentage point for Belgium), and marginally in 2018. **The average BPN participants' Belgian GDP forecast edges up to 1.6 % in 2017 and in 2018. In the euro area, GDP should increase by 1.8 % in 2017 and 1.7 % in 2018.**

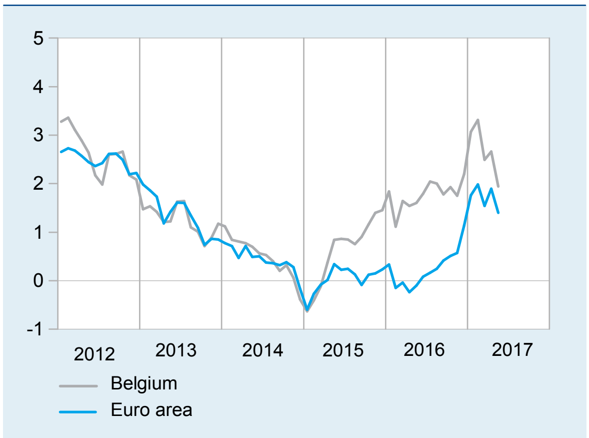
GDP GROWTH AND BUSINESS CYCLE INDICATOR



Sources: EC, NAI, NBB.

After having peaked to 3.3 % in February, HICP inflation in Belgium dropped just below the 2 % mark in May 2017 (1.9 %). This movement stems partly from weaker oil price developments, but also from the unwinding of base effects of previous indirect tax or regulated price increases. As a result, the gap with the average euro area inflation came down to 0.5 of a percentage point, against a 1.6 percentage point differential on average in 2016. According to the consensus forecast, the gap is expected to stabilise at the current level, as stronger services inflation would prevent a further decline. **Belgian inflation is forecast to reach 2.2 % on average in 2017, before slowing down to 1.7 % in 2018 (and even further due to the cancellation of an environmental tax in Flanders by the Constitutional Court). In the euro area, it is forecast at 1.6 and 1.3 %, respectively.**

INFLATION (HICP)
(annual percentage changes)



Source: EC.

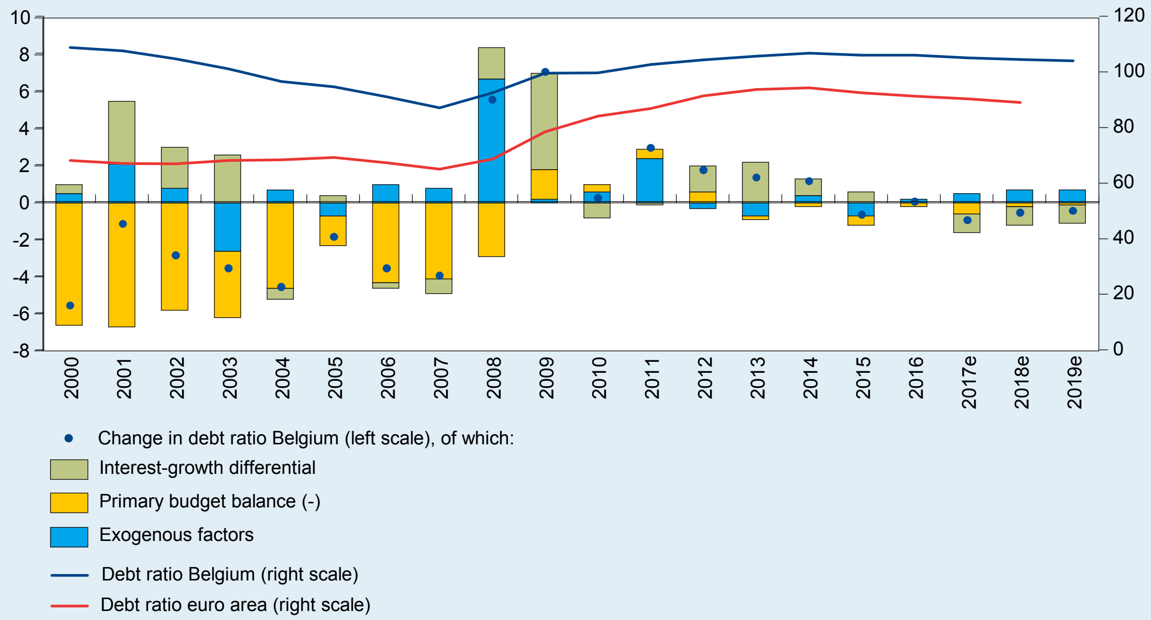
The first official public accounts for the year 2016 published by the National Accounts Institute were slightly better than foreseen. The deficit worked out at 2.6 % of GDP. **A further fall should bring it down to 2.1 % in 2017 and 2.0 % in 2018, according to the average of the BPN forecasts.** Some 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. This path foresees a balanced budget (in structural terms) by 2019, which would reinforce the decline in the debt ratio. On the basis of their own macro and budgetary forecasts, **the BPN participants anticipate a slight dip in the Belgian public sector debt, from 106.0 % of GDP in 2016 to 104.3 % in 2018.**

Special Topic: Public debt ratio back on a declining path; further consolidation efforts will firm up this trend

The financial crisis had reversed a significant 15-year downward trend in Belgium's public debt. The debt ratio increased by nearly 20 percentage points of GDP between 2007 and 2014, before stabilising at around 106 % of GDP, too high a level in view of the future challenges and the possibility of economic downturns. However, most available projections, including those established at unchanged policy, show the return of a – slight – downward trend in Belgian public debt in the coming years. The average of the BPN participants' forecasts suggests a decline to 104.3 % of GDP by 2018 (see Consensus table). It will thus have taken ten years, since the outset of the financial crisis, to bring debt back on a downward trajectory.

The National Bank of Belgium's June 2017 economic projections suggest a similar decline, that would bring public debt just below 104 % of GDP in 2019. The reduction in the debt ratio is primarily driven by a favourable interest-growth differential. As maturing bonds continue to be refinanced at lower rates, the implicit interest rate paid on average by the Treasury is likely to fall below nominal GDP growth rates. Primary budget surpluses should also contribute to the debt reduction, albeit to a smaller extent. With no change in policy, the primary budget balance is expected to remain slightly positive, but less so than on average in the euro area. This explains why Belgian debt is expected to fall by less than euro area debt.

DEBT RATIO IN BELGIUM AND THE EURO AREA
(in % of GDP)



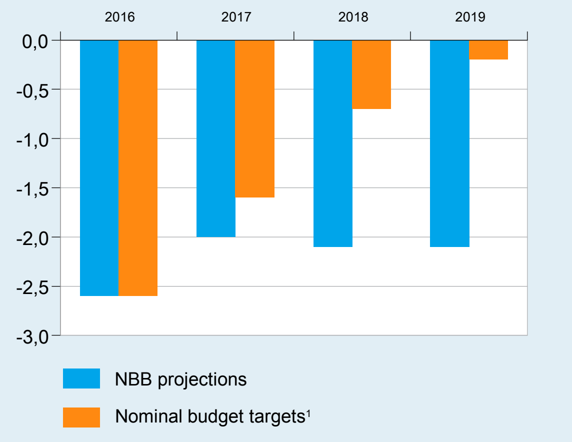
Sources: EC, NAI, NBB.

A substantial reduction in the public debt is necessary to rebuild the financial buffers to absorb negative shocks and create scope for meeting the budgetary costs of population ageing and addressing the new challenges facing society. This can only be achieved through continued fiscal consolidation that is conducive to growth. This strategy should lead to the build-up of sizeable primary budget surpluses, as was the case for sustained debt reduction in the 2000s.

The Belgian authorities recognise the need for further fiscal consolidation. In their stability programme submitted to the European Commission (EC) in April 2017, they commit to reach the medium-term objective (MTO) of a balanced structural budget – that is the budget corrected for cyclical and temporary factors – by 2019. Given the slightly negative output gap still expected, this corresponds to a small headline deficit.

According to the National Bank of Belgium's assessment, taking into account only those policy measures that are sufficiently specified, there is an important consolidation gap between the currently projected figures and the government's targets. By 2019, this gap is expected to reach almost 2 % of GDP at the general government level, which means that governments need to decide on additional consolidation measures on this scale in order to reach the target. The budget for the coming years will be prepared in the coming weeks, starting with an updated assessment of the consolidation gap. While a recent report by the federal Monitoring Committee suggests that it could turn out to be lower than previously expected, significant additional measures are necessary to reach the target. Because of the federal and regional elections in June 2019, it is advisable that the governments incorporates the required consolidation measures as soon as possible into a multi-annual budget plan.

BUDGET BALANCE TARGETS AND PROJECTIONS
(in % of GDP)



Sources: FPS Finance, NBB.
[1] Nominal budget targets of general government as in the April 2017 stability programme for Belgium.

Such additional efforts are also necessary to comply with the requirements of the European budgetary governance framework. In May 2017, the European Commission assessed the compliance of EU countries with the fiscal rules of the Stability and Growth Pact (SGP) and issued country-specific recommendations. In 2016, when the deficit remained clearly below the 3 %-of-GDP mark, Belgium made prime facie insufficient progress towards compliance with the debt reduction benchmark set out in the corrective arm of the SGP. The EC therefore had to draft a report in accordance with Article 126(3) of the Treaty. Based on the report's analysis of relevant factors, the EC decided not to open an excessive deficit procedure against Belgium at this point in time. At the same time, the EC stated that additional fiscal measures need to be taken in 2017 to make sufficient annual progress towards its MTO. While an improvement of the structural balance by 1.1 % was required over 2016-2017, taking account of additional expenditure associated with the exceptional inflow of refugees and the extra security measures, the EC concluded on the basis of its Spring forecast that the improvement would only amount to 0.6 % of GDP, 0.4 percentage point of which resulting from reduced interest payments. For 2018 too, the EC considers Belgium at risk of significant deviation from the path to the MTO, if policy remains unchanged.

Apart from the budgetary targets, the European Commission recommends that the various governments in Belgium agree on an enforceable distribution of fiscal targets between them. At the moment, there is no agreement on sharing out the burden of the targets as proposed by the High Council of Finance, which prevents this institution from playing its monitoring role and affects the credibility of Belgium's stability programme. The Commission also recommends that Belgium should remove any distortive tax expenditure and improve the composition of public spending in order to make room for infrastructure investment, and especially on transport infrastructure.

All in all, fiscal indicators in Belgium are showing the first signs of sustained improvement. Further efforts for a smart, growth-friendly consolidation should be made to reinforce the progress. Combined with the pension and labour market reforms, and the recently conducted policy of wage moderation and labour cost reduction, they will put Belgium on a stronger footing.

Treasury Highlights

The results of the two OLO syndications earlier this year were published in the March BPN issue. In addition to the launch of these new lines, three OLO auctions (in March, April and June) and one OLO syndication (in May) were held, resulting in a total of € 13.69 billion of funding being raised.

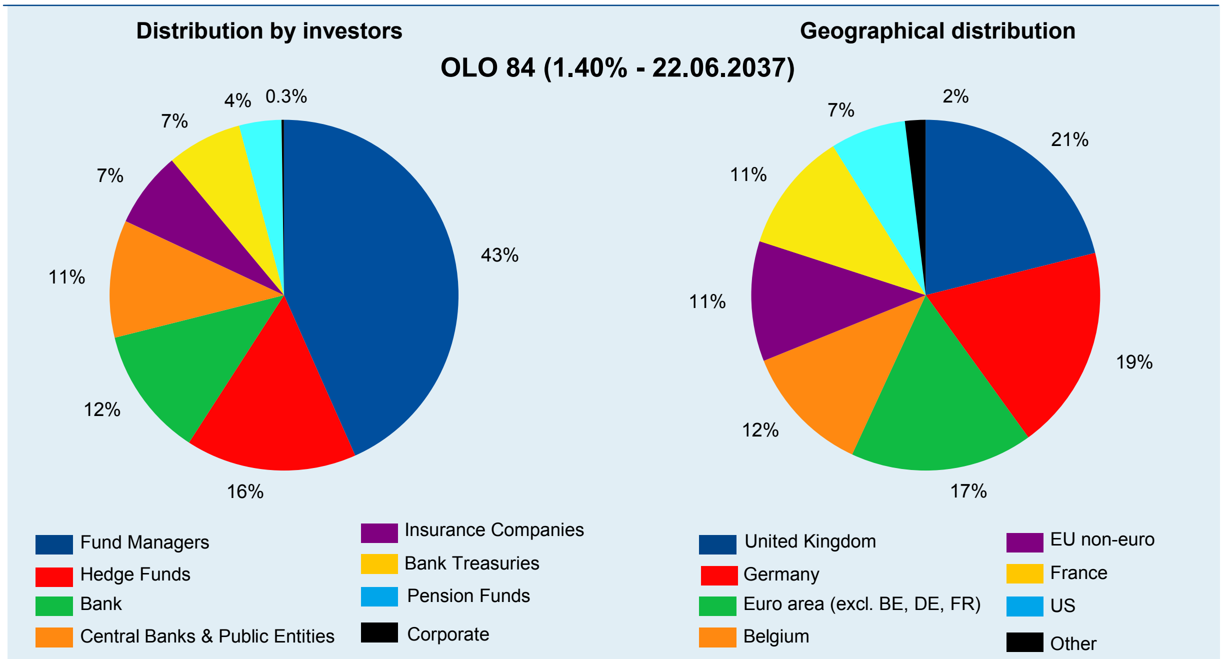
OLO auctions (€ 6.63 billion)

Auction date	OLO	Nr	Issued (€ billion)	Yield	Bid-to-cover
March 20	OLO 0.80 % 22/06/2026	OLO 81	1.435	0.933 %	1.52
	OLO 1.90 % 22/06/2038	OLO 76	1.008	1.591 %	1.62
	OLO 4.25 % 28/03/2041	OLO 60	0.756	1.640 %	1.60
Non-competetive tour			*0.838*		
Total March			**4.037**		
April 24	OLO 0.20 % 22/10/2023	OLO 79	0.901	0.117 %	1.57
	OLO 0.80 % 22/06/2027	OLO 81	1.600	0.777 %	1.60
Non-competitive tour			*0.096*		
Total April			**2.597**		
June 19	OLO 0.50 % 22/10/2024	OLO 82	0.931	0.162 %	1.48
	OLO 0.80 % 22/06/2027	OLO 81	1.326	0.599 %	1.76
	OLO 1.60 % 22/06/2047	OLO 78	0.933	1.612 %	1.45
Non-competitive tour			*0.876*		
Total June			**4.057**		

OLO syndication (€ 3.0 billion 20-year benchmark)

Besides those two auctions, Belgium also organised a new 20-year benchmark issue in May. The new € 3 billion OLO 84, falling due on 22 June 2037, pays an annual coupon of 1.40 % and was priced at a spread of 8 bps over the interpolated mid-swap reference rate, implying a reoffer yield of 1.485 %.

Distribution of the new OLO at issuance



Source: Belgian Debt Agency.

The auction scheduled for 22 May was cancelled.

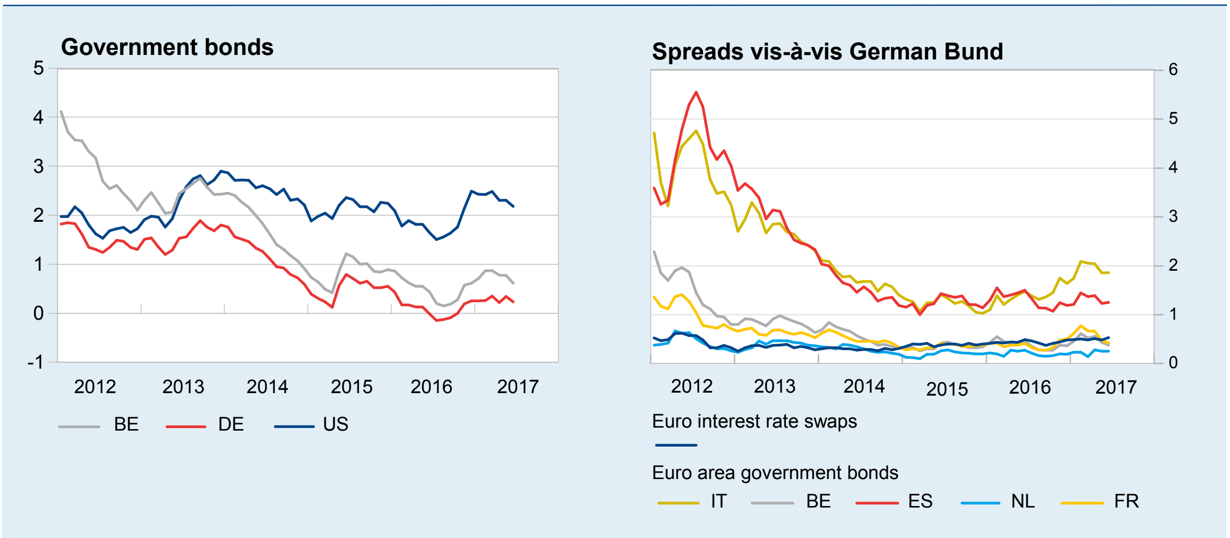
So far, there have been no EMTN or *Schuldscheine* issues.

Belgium has therefore already issued € 25.7 billion, corresponding to 65.5 % of its € 39.25 billion funding target.

In terms of portfolio structure, the average life of the portfolio is now 9.27 years (end-May) and it has an implicit yield of 2.42 %.

Government Securities Market

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

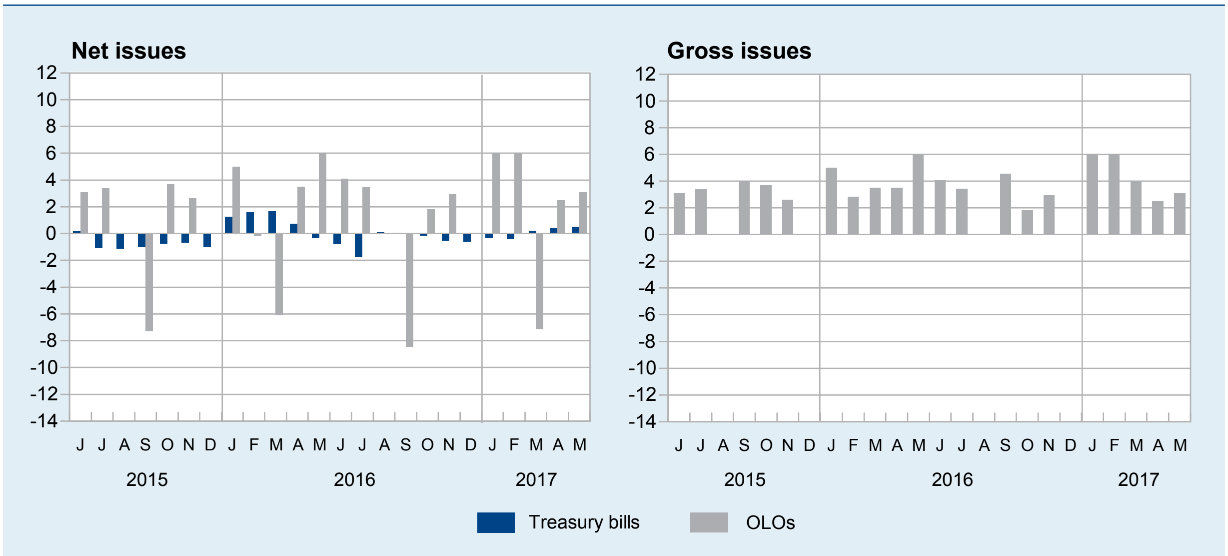


Sources: BIS, Datastream.
Average over the first 21 days for June 2017.

Between March and mid-June 2017, long-term sovereign bond yields fell slightly overall in the euro area and the US, bringing a halt to the period of rising nominal yields that both regions had seen in the preceding six months. In Germany and Belgium, the ten-year sovereign yield dropped by respectively 12 bp and 26 bp, to reach 0.23 % and 0.61 % in June. These declines mainly reflect moderation in global inflation expectations and more negative economic surprises outside the euro area. The decrease was more pronounced in the US, where the ten-year sovereign yield dropped by 30 bp to 2.18 %, despite the FOMC's decision in mid-June to raise the target range for the federal funds rate by a quarter of a percentage point to 1 % - 1.25 %.

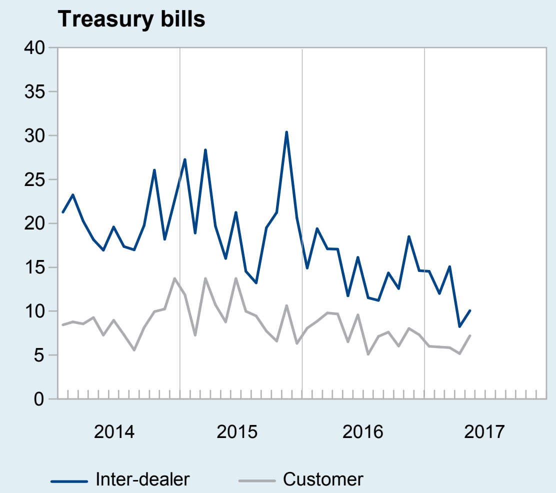
Over the period under review, long-term euro area sovereign spreads vis-à-vis Germany tended to narrow, especially in countries showing gradual strengthening of economic growth and an improved economic outlook. In Portugal for instance, ten year sovereign bond spreads declined by 91 bp to 274 bp in June. Ten-year spreads also came down in Italy and Spain, but to a lesser extent: they narrowed by respectively 19 bp and 12 bp to 186 bp and 125 bp. The spread decreases also occurred against the background of declining political uncertainty. In particular, the ten-year spread in France dropped by 25 bp to 42 bp, while in Belgium, it narrowed by 14 bp to 38 bp. In Greece, the ten-year spread contracted by 112 bp to 570 bp in the context of the agreement reached with the Eurogroup and the IMF on its bailout programme. Overall, financial markets volatility remained relatively low over the period under review, with the exception of the spike observed at the time of the first round of the French presidential election.

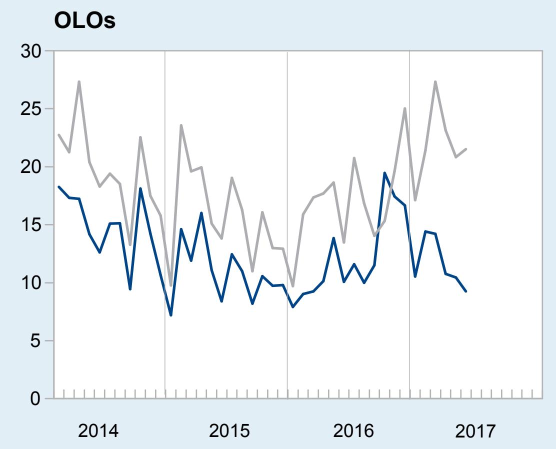
PRIMARY MARKET
(billions of euros)



SECONDARY MARKET TURNOVER

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





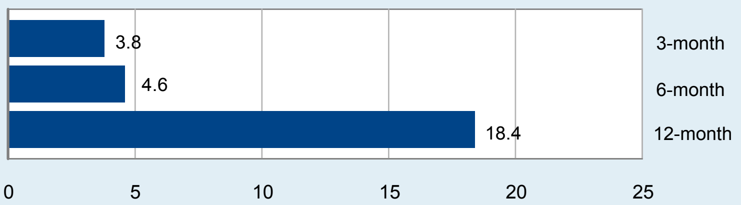
Source: Belgian Debt Agency.

OUTSTANDING AMOUNTS AND TURNOVER

(billions of euros)

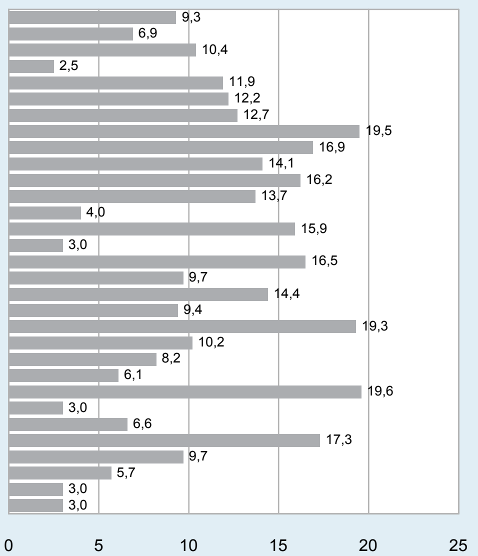
TREASURY BILLS

Nominal outstanding amounts at end of May 2017

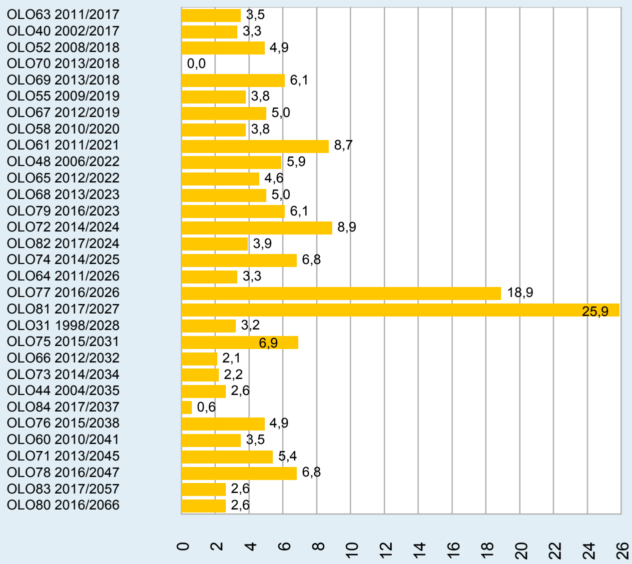


OLOs

Outstanding amounts at 15 June 2017

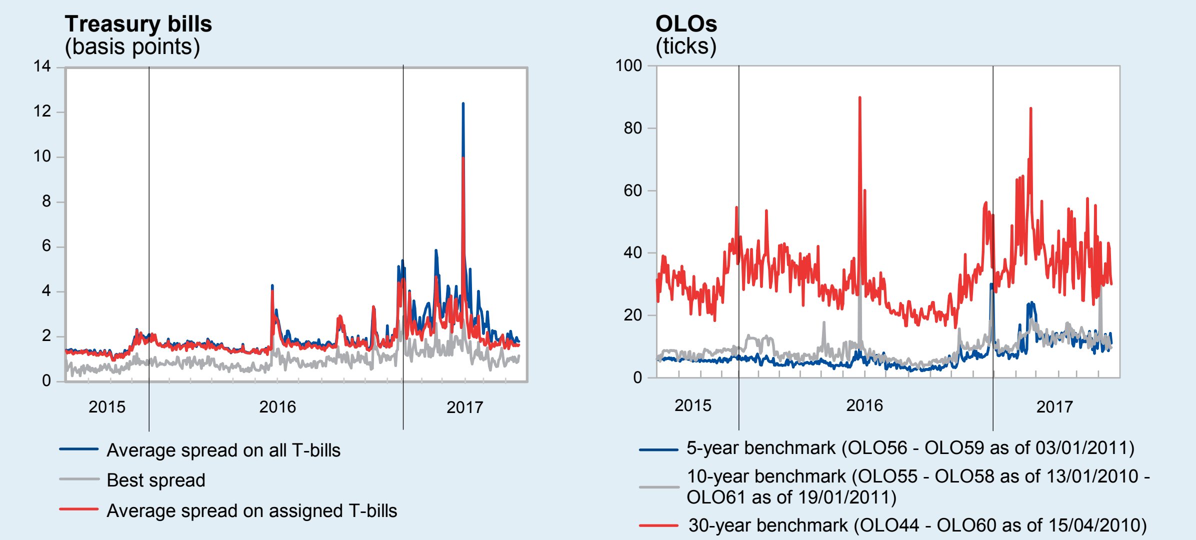


Outright turnover in May 2017



Source: Belgian Debt Agency.

BEST BID/OFFER SPREADS[1]



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

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