2022-12-06

PRESS RELEASE

Market notice by the National Bank of Belgium

Regulated information (inside information) circulated by the National Bank of Belgium on 6 December 2022 at 18.00 CET.

Financial year 2022: earnings and dividend expectations

In its market notice of 21 September 2022, the National Bank of Belgium ("the Bank") expressed the expectation that, given recent increases in European Central Bank (ECB) policy rates, (i) it would end the current financial year (2022) with a loss and (ii) losses would continue to mount in subsequent financial years.

We would like to recall that, for years, the Bank has taken into account possible loss scenarios due to interest rate hikes.[1] In that context, the Bank modified its reserve policy in 2016[2] and has reserved 50% of its profits every year since. Indeed, the Bank's reserves act as financial buffers in the event of losses.[3] These buffers, currently valued at €7.08 billion, will have to be utilised for the first time at the end of this financial year.

In the meantime, the Bank has carried out another interim analysis of the risk scenarios and earnings forecasts and is now, closer to year end, able to shed light on the impact these developments are expected to have on its earnings and dividend distribution.

Earnings for financial year 2022

Based on the abovementioned earnings forecasts, the Bank expects to close the current financial year with a loss, estimated in the range of €600 million to €800 million.[4]

The Bank's mark-to-market (MTM) portfolios necessitate a comment in this regard, given the uncertainty surrounding market developments up to year's end.[5] Consequently, depending on the market value of these portfolios on the balance sheet date, the final result may differ.

Furthermore, the aforementioned analysis revealed that the estimated financial risks to which the Bank is exposed exceed its accrued financial buffers.

In this regard, it should be noted that an interim analysis of risk scenarios and earnings forecasts is a less in-depth exercise than the annual analysis carried out after the balance sheet date, which is used to determine the final allocation of profits.[6] Moreover, various uncertainties still need to be factored in (see below).

Nevertheless, the possible degree of deviation from the situation on the balance sheet date has become much smaller. Consequently, at this stage, it can be confirmed with a high degree of certainty that, based on

[1] See the references in the aforementioned market notice of 21 September 2022 to previous publications of the Bank, including its Corporate Report 2021.
[2] See https://www.nbb.be/doc/ts/enterprise/press/2016/cp160323ben.pdf.
[3] In keeping with the reserve policy, a negative result for the financial year is first charged to the available reserve, which currently amounts to €4.76 billion. If necessary, any excess can be covered by the reserve fund, which currently stands at €2.65 billion. It should be noted that the reserve fund includes €324.79 million in depreciation accounts which are not included when calculating the Bank's total financial buffers, which consequently amount to €7.08 billion.
[4] For more information on the Bank's financial calendar, see https://www.nbb.be/en/about-national-bank/shareholder-information/financial-calendar.
[5] See Section 3.1.1.1 of the Bank's Corporate Report for more information on these MTM portfolios.
[6] See Section 3.2.7.3 of the Bank's Corporate Report.

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current forecasts, the estimated financial risks will exceed the Bank's financial buffers on the balance sheet date.

Possible scenarios for the more distant future

The Bank's risk scenarios and earnings forecasts are subject to significant uncertainties, including future market developments and, possibly, policy decisions by the ECB's Governing Council. The further ahead one looks, the greater the uncertainty.

That being said, having regard to the intrinsically uncertain nature of such projections, current market expectations indicate that the Bank may post losses through FY 2027, before returning to profit. Should such a scenario materialise, which, again, is subject to substantial uncertainty, the result would be total losses of around €9 billion over this period, assuming a constant balance sheet composition.

Even if the Bank's financial buffers were to be depleted over the course of the coming years, this would not call into question its stability. After all, a central bank can continue to operate, at least temporarily, with a negative capital position.

Sensitivity analysis

The main factor driving the anticipated losses is the rising cost of financing monetary policy portfolios: interest expenses on the deposits held by credit institutions with the Bank have increased compared to the low yields at which the - mostly long-term - securities in those portfolios were acquired.

In addition, it should be pointed out that the ECB policy rate hikes in the second half of 2022 will impact full-year earnings for the first time in 2023.

In this context, the Bank wishes to reiterate its tasks as a national central bank within the Eurosystem whose main mission is to maintain price stability. In doing so, the Bank takes part in the implementation of monetary policy that is centrally determined by the Governing Council of the ECB. The performance of these public interest tasks entails financial risks which may result in losses.

Assuming a constant balance sheet composition, an increase in ECB policy rates of 25 basis points raises the Bank's costs by around €310 million on an annual basis.[7] The sensitivity of the Bank's costs to such interest rate increases is linear.[8]

Furthermore, if applicable, an increase in long-term interest rates would have a positive impact on the Bank's earnings. Indeed, assuming unchanged ECB Governing Council policy, maturing securities in the Bank's monetary policy portfolios would then be reinvested at higher interest rates. However, the positive impact of a possible increase in long-term interest rates would offset only very partially the negative impact of higher policy rates.[9]

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[7] For purposes of this calculation, it is assumed that ECB policy rates will move in tandem in the future. The ECB Governing Council could, of course, decide otherwise.

[8] For example, a 50-basis-point rise in policy rates will cause an increase in annual costs of about €620 million, a rate hike of 75 basis points will lead to increased costs of €930 million, and so on. Similarly, a 25-basis-point decrease in interest rates will lead to a reduction in costs of approximately €310 million.

[9] An increase in long-term interest rates by 25 basis points would lead to an increase in income of approximately €50 million on an annual basis.

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Impact on the dividend

In 2009, the Bank's Council of Regency adopted a dividend policy, which has been consistently applied ever since.[10] The general principles of this policy are set out below.

The Bank's dividend consists of two components, namely a fixed dividend of €1.5 per share and a variable dividend which, assuming sufficient profits, amounts to 50% of the net return on the statutory portfolio. This portfolio is made up of assets that form a counterpart to the reserve fund and the available reserve.

The fixed dividend is covered by both the available reserve and the reserve fund, even when annual earnings are negative.[11]

The variable dividend is covered by the available reserve, unless drawing down this reserve would result in a level of reserves insufficient to cover the estimated risks. Priority is given to ensuring the financial soundness and independence of the Bank.

As it is expected with a high degree of certainty that the estimated financial risks on the balance sheet date will exceed the level of the financial buffers (€7.08 billion, less the losses to be absorbed for FY 2022), application of the Bank’s reserve and dividend policy does not allow a variable dividend to be paid for financial year 2022.

[10] See the market notice of 22 July 2009 and the market notice of 23 March 2016.

[11] Consequently, a fixed dividend will be paid for financial year 2022.

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