BELGIAN PRIME NEWS
Quarterly publication

BELGIAN DEBT AGENCY

NationalBank OF BELGIUM
Eurosystem

Participating Primary and Recognised Dealers:

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N° 78 January 2018 Last update: 3 January 2018 Next issue: March 2018

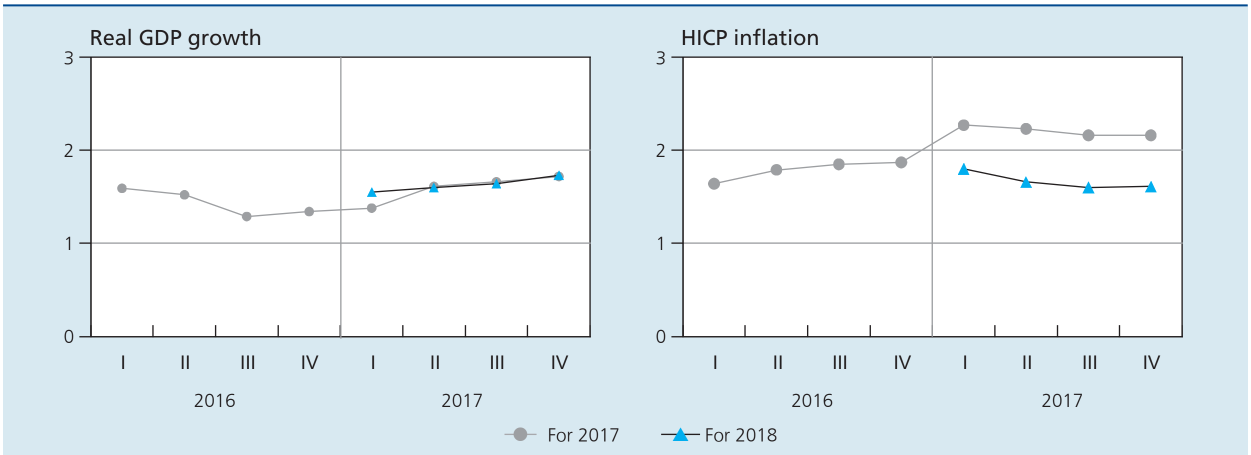
- MACROECONOMIC DEVELOPMENTS: Belgium continues to benefit from the global economy's momentum
- SPECIAL TOPIC: Elevated corporate debt in Belgium: should we be worried?
- FINANCIAL MARKETS AND INTEREST RATES: Low interest rates in the euro area and the US, but diverging dynamics
- TREASURY HIGHLIGHTS: 2017 funding programme successfully completed and funding plan for 2018 adopted

CONSENSUS Average of participants' forecasts

	Belgium			Euro area		
	2016	2017p	2018p	2016	2017p	2018p
Real GDP(1)	1.5	1.7	1.7	1.8	2.3	2.2
Inflation (HICP)(1)	1.8	2.2	1.6	0.2	1.5	1.4
General government balance(2)	–2.5	–1.7*	–1.4	–1.5	–1.3	–1.2
Public debt(2)	105.7	103.7	102.2	91.1	88.8	87.3

(*) Some participants' forecasts could not take into account recent positive fiscal developments. NBB's general government balance projections at mid-December 2017: –1.2 % in 2017, –1.3 % in 2018.
(2) Percentage changes.
(3) EDP definition; percentages of GDP.

SUCCESSIVE FORECASTS FOR BELGIUM



Source: Belgian Prime News.

Belgium continues to benefit from the global economy's momentum

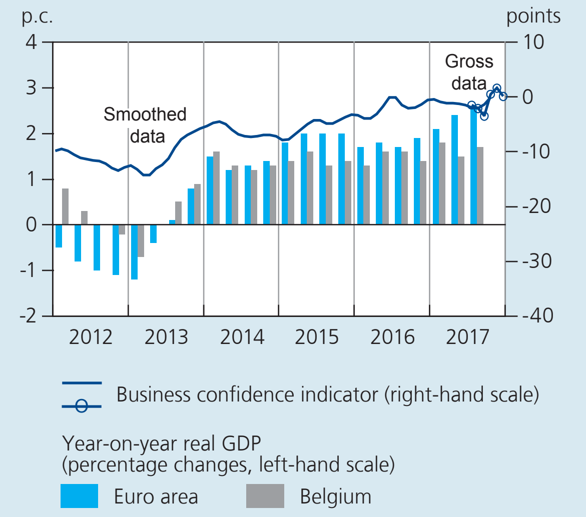
Global growth, as well as trade flows, picked up quite strongly in the first half of 2017. The euro area economy performed well too. Benefiting from the global momentum and (continuing) accommodative monetary policy, euro area GDP in the third quarter of 2017 expanded at a robust rate of 0.6 % quarter-on-quarter, which is also the average over the past four quarters. Although growth was mostly driven by domestic demand, net exports also made a positive, albeit small, contribution. However, inflation has remained below the ECB target.

Turning to the Belgian economy, following a strong first half-year, growth lost some momentum in the third quarter. The quarter-on-quarter rate fell to 0.3 % and came in slightly below expectations. Private consumption growth was somewhat disappointing, especially given the high overall level of confidence. Compared to the previous year, it appears that the purchases of durable goods have lost some steam. Business investment growth, on the other hand, remained solid, and could be expected to remain an important contributor to growth in the fourth quarter, as business confidence has clearly strengthened since October.

The labour market conditions remained favourable and 2017 now seems to be heading towards a peak in net job creation. The positive surprise in employment growth in the course of 2017 seems to be partly related to a positive surprise in the participation rate, especially of older workers.

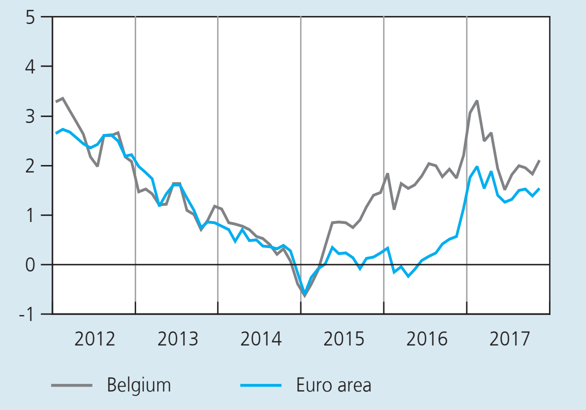
Against this backdrop, the consensus forecast was revised slightly upwards for 2018 (+0.1 of a percentage point for Belgium), but remained unchanged for 2017. **The average BPN participants' forecast for GDP growth in Belgium is 1.7 % in 2017, as well as in 2018. In the euro area, GDP is expected to increase by 2.3 % in 2017 and 2.2 % in 2018.**

GDP GROWTH AND BUSINESS CYCLE INDICATOR



Sources: EC, NAI, NBB.

INFLATION (HICP)
(annual percentage changes)

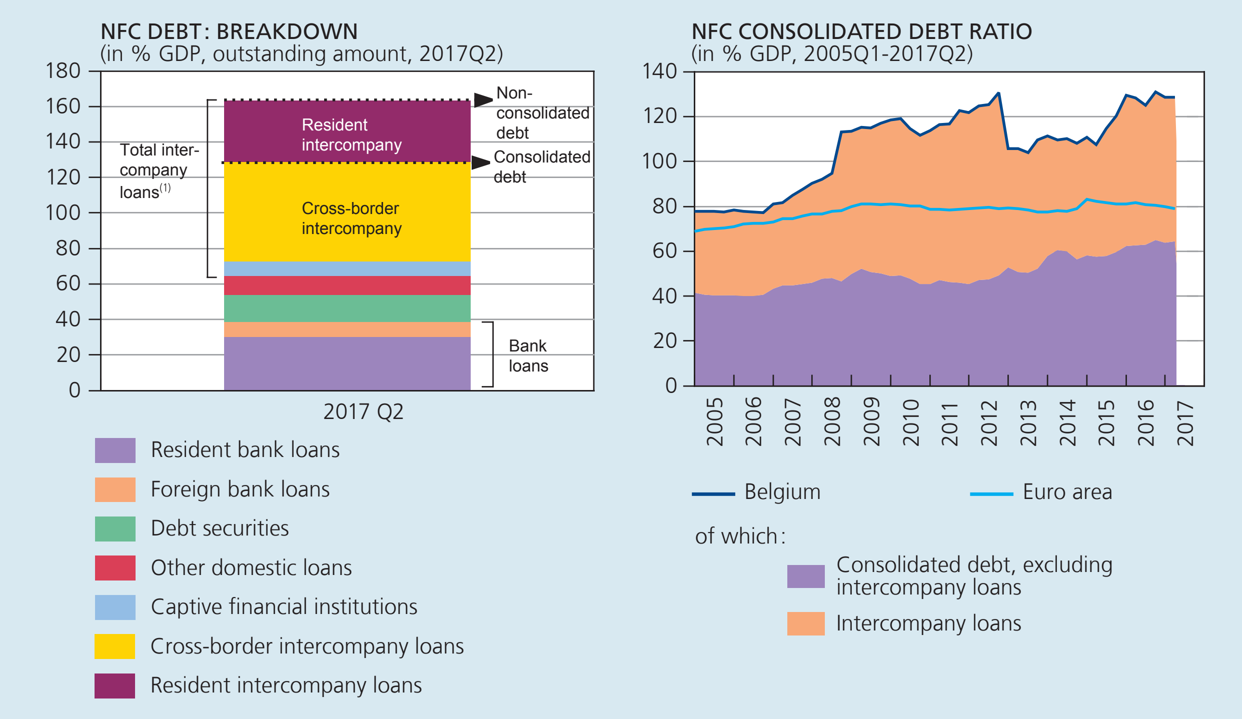


Source: EC.

HICP inflation in Belgium has remained close to the 2 % mark in recent months. Price pressures in 2017 largely stemmed from a pick-up in energy prices, while underlying inflation remained stable at about 1.5 %. Inflation in Belgium is projected to be more moderate in 2018, as a result of the tax on household electricity consumption in the Flemish Region being scrapped. Hence, the inflation gap with the average euro area inflation rate, which has already narrowed recently, could be expected to continue shrinking. **According to the consensus forecast, inflation should reach 2.2 % in 2017 and 1.6 % in 2018 in Belgium, while it is expected to be 1.5 % and 1.4 % in the euro area for these two years.**

Belgian Prime News participants expect the Belgian public sector deficit to come down in 2017, from 2.5 % of GDP in 2016 to 1.7 % in 2017 and 1.4 % in 2018. It should be noted that some participants' estimates for 2017 do not yet incorporate favourable revenue developments observed at the end of the year. The National Bank's projections published at mid-December 2017 feature a public deficit amounting to 1.2 % of GDP in 2017 and 1.3 % of GDP in 2018. In any care, additional consolidation efforts would thus be required to comply with the path set out in the stability programme submitted by the Belgian authorities to the European Commission in April 2017, which foresees a balanced budget (in structural terms) by 2019. **On the basis of their own macro and budgetary forecasts, the BPN participants anticipate a slow reduction in the Belgian public sector debt, from 105.7 % of GDP in 2016 to 102.2 % in 2018.**

CORPORATE DEBT IN BELGIUM LOW WHEN INTERCOMPANY LOANS ARE EXCLUDED

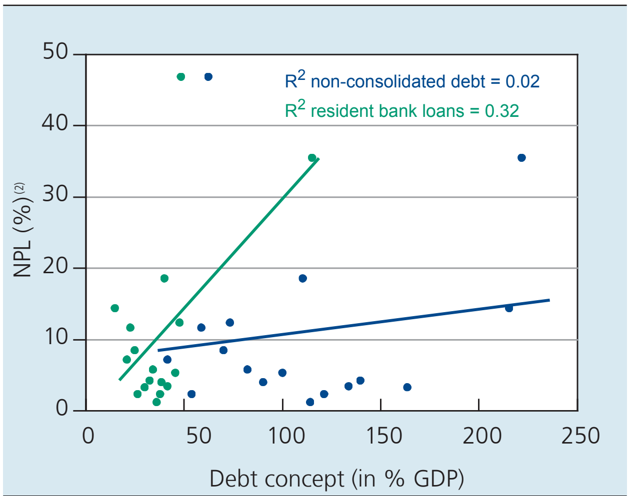


Sources: ECB, NBB.
(1) Total of resident and cross-border intercompany loans and loans granted by captive financial institutions.

Total debt of non-financial corporations (NFCs) stands at a relatively high level in Belgium. Moreover, in contrast to most euro area countries, the debt-to-GDP ratio has continued to rise since the financial crisis. While credit supports investment, excessive levels of corporate debt entail financial stability risks and exert downward pressure on economic activity through deleveraging forces and drags on productivity. This Special Topic puts the relatively high corporate debt level into perspective and shows that risks for financial and macroeconomic stability are currently low. This assessment is based on both statistical and economic arguments.

From a statistical point of view, measurements of corporate debt (both non-consolidated and consolidated debt) in Belgium are inflated by intercompany lending, mostly on the account of non-financial holding companies, treasury centres, etc. For an assessment of debt sustainability, it is preferable to exclude these intercompany loans. Besides data quality issues, there are various reasons why these intercompany loans might overestimate sustainability risks. First, given these loans mostly occur between units of the same group (intragroup), there is no external counterpart risk. Furthermore, in most cases, these loans are merely accounting operations – which fit into tax-optimisation strategies – implying that the liability is often matched by a corresponding financial asset, with no significant link to real economic activity and financial stability. As can be seen from the chart, corporate debt concepts which include intercompany loans (e.g. non-consolidated debt) generally tend to have a weaker link with credit risk compared to debt concepts which exclude intercompany loans (e.g. bank loans).

BANK LOANS (1) HAVE A STRONGER LINK WITH NON-PERFORMING LOANS
(euro area countries, 2017Q2)



Sources: ECB, NBB.
(1) Loans of resident banks to resident non-financial corporations, including securitised loans.
(2) Non-performing loans ratio of domestic banking groups and stand-alone banks, calculated as the gross non-performing loans and advances in percent of total gross loans and advances.

In its implementation of the macroeconomic imbalance procedure (MIP), the EC bases its assessment of private debt on consolidated debt of NFCs (129 % of GDP in 2017Q2) and households (59.8 % of GDP). The EC acknowledges that this consolidated measure can still lead to biased results, given the consolidation only holds for intercompany loans between resident NFCs. Excluding all intercompany loans would result in a corporate debt level of 64.5 % of GDP. As such, together with household debt, private debt (124 % of GDP) would fall below the MIP threshold of 133 %.

There are also economic reasons behind the argument as to why the current corporate debt level and dynamic credit growth largely go without sustainability issues. First, Belgian NFCs have a relatively large capital base (thanks to the beneficial impact in the past of the notional interest deduction scheme), which results in favourable debt-to-equity ratios. Secondly, while credit growth has been dynamic due to a surge in corporate bond issuance (the outstanding amount of bonds in Belgium has tripled since the financial crisis from 5 to 15 % of GDP) and dynamic bank credit growth (5 % on an annual basis in October 2017), much of this increase can be explained by favourable financing conditions and increased economic activity. Based on the (bank) credit-to-GDP gap for the private sector – which is used in the context of the countercyclical capital buffer (CCyB) – the credit cycle is still largely neutral (gap below 2 percentage points) and displays no clear systemic cyclical risks and thus no need to activate the CCyB. Finally, cash reserves are high and the share of long-term corporate bank loans has increased, which tends to support investment and limits the roll-over risk in the event of an interest rate rise.

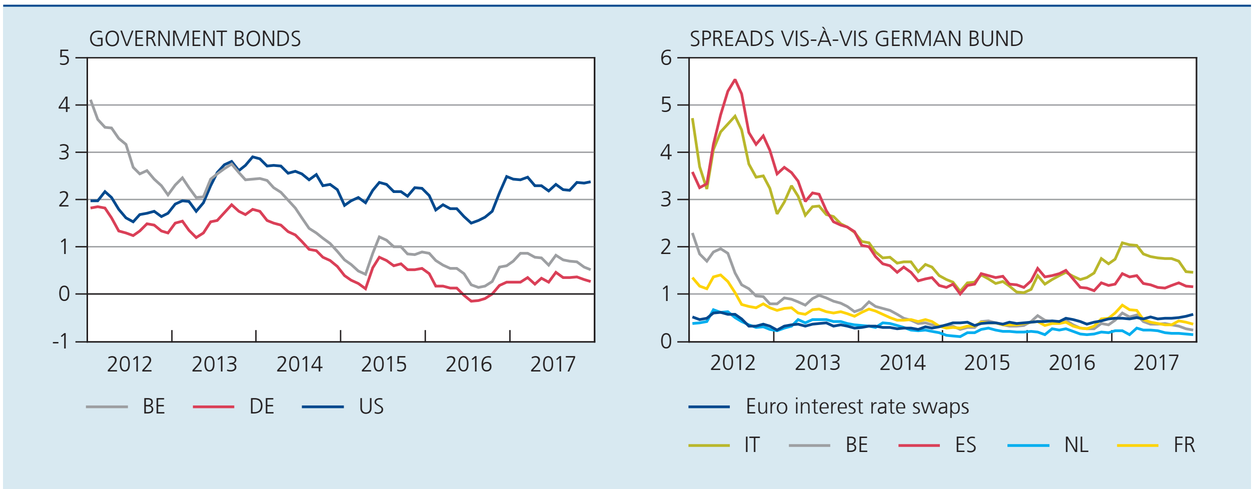
FINANCIAL MARKETS AND INTEREST RATES **Low interest rates in the euro area and the US, but diverging dynamics**

In the last quarter of 2017, the overall monetary policy stance remained accommodative, both in the euro area and the US, keeping interest rates at historically low levels. Stock markets continued to show signs of stretched valuations in the US, whereas major euro area stock indices stalled over the period under review in a context of disappointing earnings reports. Realised and implicit financial markets volatility indices as well as risk premiums remained low.

Despite the low policy rates in both the euro area and the US at the moment, the future course of monetary policy is expected to differ across the two regions. In the euro area, monetary policy can be expected to remain accommodative for a prolonged period of time, as was indicated by the ECB in October and confirmed in December. In the US, monetary policy is being gradually normalised by the Fed, which raised the target range for the federal funds rate in December, for the fifth time since the financial crisis, to 1.25 % – 1.50 %. This difference in dynamics helped stop the appreciation of the euro against the US dollar in the last quarter of the year; the euro stabilised around 1.18 US dollar. Furthermore, short-term sovereign yields continued to increase in the US (+35 bp for the one-year yield), while they remained low and stable on average for AAA-rated euro area government bonds.

Over the period under review, diverging developments have also been observed in long-term bond markets in the euro area and the US. Long-term sovereign yields came down in the euro area for (almost) risk-free sovereign bonds as they continued to be dragged down by the ECB's (revamped) asset purchase programme and falling inflation risk premiums. In Germany and Belgium for instance, ten-year sovereign yields declined by respectively 10 and 17 bp, to 0.27 % and 0.52 %

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



Sources: BIS, Thomson Reuters.
Average over the first 20 days for December 2017.

in December 2017 (monthly averages). In the US, by contrast, progress made towards tax reform (comprising a significant fiscal stimulus) has supported long-term yields, implying that they remained relatively stable throughout the review period. Ten-year US sovereign yields however rose moderately in the days following the ratification of the reform by the US Congress, also triggering an increase in core euro area countries.

Long-term euro area sovereign spreads vis-à-vis Germany continued to narrow in general, mainly due to the strong pace of economic expansion and to a substantial improvement in the growth outlook (see the Eurosystem staff macroeconomic projections released in December). Ten-year spreads declined for instance in Belgium, France and the Netherlands, by respectively 7, 7 and 2 bp, to reach 25, 37 and 15 bp. Similarly, data up to the day before the elections held in Catalonia show that the ten-year spread also narrowed in Spain, by 8 bp to 116 bp, despite the internal political uncertainties. Ten-year spreads declined most in Italy, Portugal and Greece (figures not shown for the latter two countries), where they narrowed by 24, 40 and 94 bp, to respectively 146, 155 and 428 bp, on account of more favourable country-specific developments (including improved credit ratings), subsiding risks in the banking sector and the improved economic and fiscal outlook.

TREASURY HIGHLIGHTS **2017 funding programme successfully completed and funding plan for 2018 adopted**

Date	OLO		Issued (€ Billion)	Yield	Bid to cover
October 23	OLO 0.20 % 22/10/2023 OLO 4.50 % 28/03/2026 OLO 1.60 % 22/06/2047	OLO79 OLO64 OLO78	1.012 0.875 0.915	**0.020 %** **0.368 %** **1.786 %**	**1.62** **1.78** **1.56**
Non-competitive tour			*0.431*		
Total October			3.233		

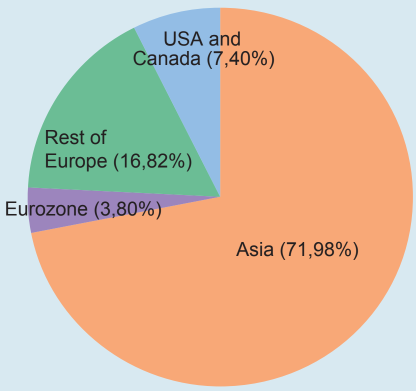
The OLO auction in October resulted in a total of € 3 233 billion of funding.

The OLO auction scheduled for November was cancelled due to the finalisation of the funding plan.

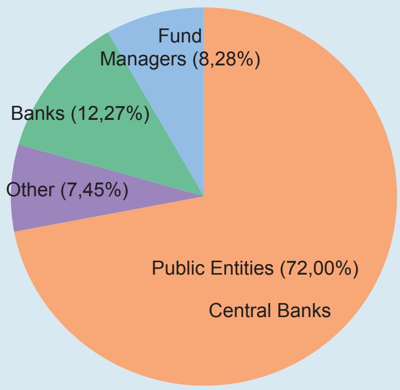
On Thursday 28 September, the Belgian Debt Agency issued a new long 2-year USD 1.5 billion Note. This Note pays a coupon of 1.625 % and was priced at mid-swaps – 4bp. The proceeds were swapped in euro; resulting in a negative yield for the Kingdom.

Asian investors showed great interest in the deal, taking up 71.98 % of the issue, as well as non-euro investors taking 16.82 %. In terms of investor type, the large proportion of central banks (72.00 %) was striking.

EMTN – GEOGRAPHICAL DISTRIBUTION OF THE TRANSACTION IN USD IN 2017



EMTN – DISTRIBUTION BY INVESTOR TYPE OF THE TRANSACTION IN USD IN 2017



No further EMTNs or Schuldscheine were issued. Taking into account the € 2.7 million worth of State Notes issued in December, the total long-term funding for 2017 amounted to € 36.85 billion.

The average life of the debt portfolio reached 9.25 years as at 30 November 2017, and the average duration came to 8.21 years.

The implicit cost of the portfolio came down even further to 2.29 % as of that date.

Funding plan for 2018

The Belgian Debt Agency plans to issue € 31.00 billion worth of OLOs, € 4.55 billion less than the € 35.55 billion issued in 2017. It expects to launch two new OLO fixed-rate benchmarks: a 10-year benchmark and a benchmark in the 15 to 20 year area. The latter will be issued as a Green OLO.

The Debt Agency also expects to issue € 3.00 billion via its EMTN programme or other alternative funding instruments such as Schuldscheine.

State Note issuance for private investors is expected to result in just € 0.25 billion of funding, given the low interest rate environment.

As for short-term funding, net short-term debt is projected to fall by € 1.00 billion in 2018. The volume of Treasury Certificates, forecast to reach € 25.3 billion at year-end 2017, is not expected to change over the year 2018. With regard to short-term financing, some changes are being made to the Treasury Certificate programme, but the issuance calendar remains unchanged, with two auctions per month. But the number of maturities will be reduced from twelve to six per year. Exceptionally, the Treasury will offer a supplementary line.

In 2018, both the maximum for the 12-month refinancing and the refixing risk will be lowered by 2.50 %, to 17.50 %.

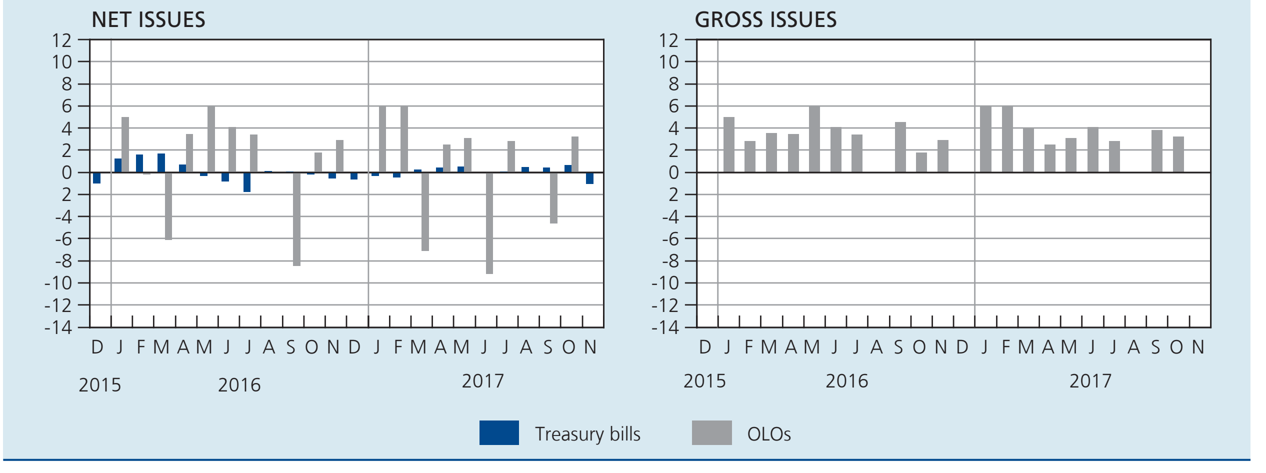
The maximum for the 60-month refinancing and refixing risk will also be lowered, by 5.00 %, to 42.50 %.

In 2018, the average life of the debt portfolio is required to be higher than 9.00 years, or half a year higher than the prevailing minimum for 2017.

The details of the 2018 Funding Plan are available on the Belgian Debt Agency's website: www.debtagency.be.

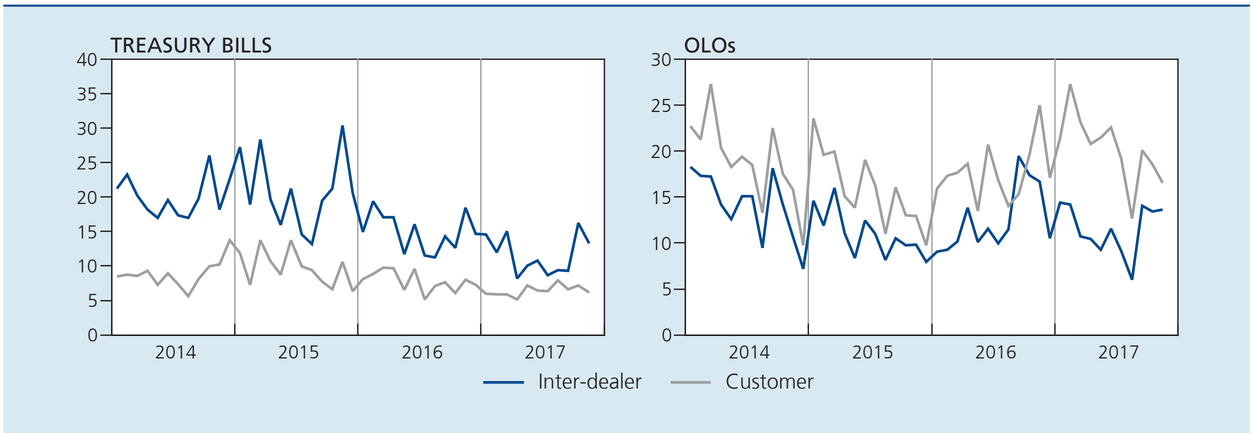
GOVERNMENT SECURITIES STATISTICS

PRIMARY MARKET
(billions of euros)



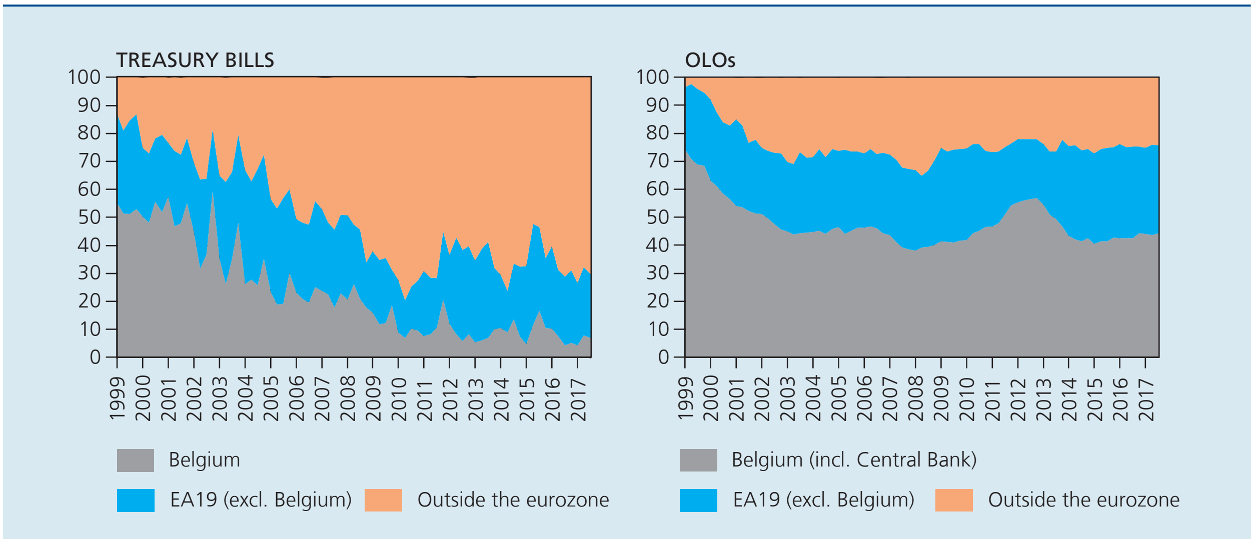
Source: Belgian Debt Agency.

SECONDARY MARKET TURNOVER
(as reported by primary and recognised dealers to the Treasury, billions of euros)



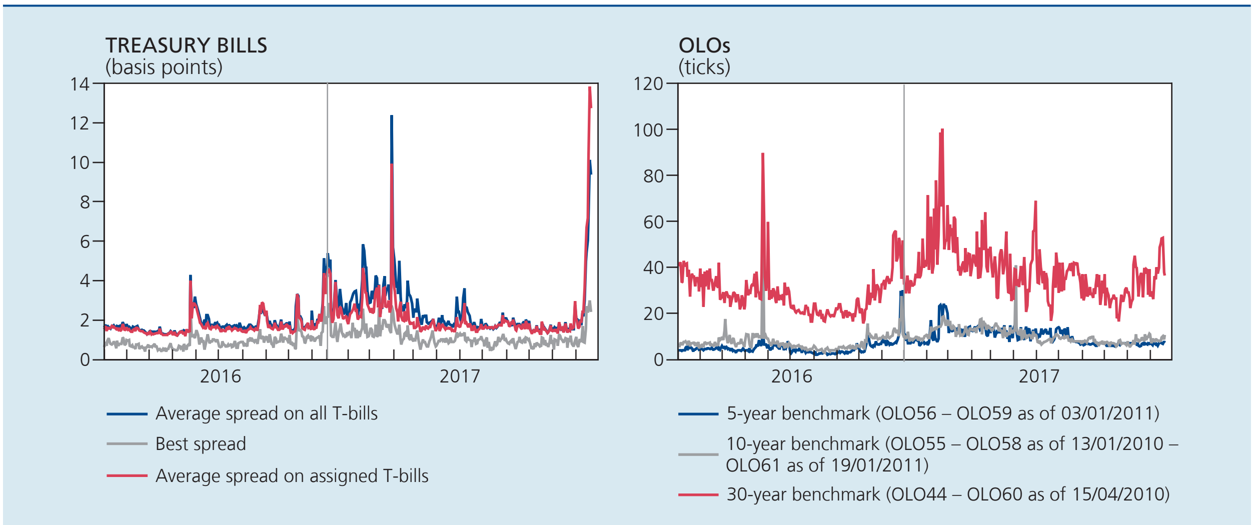
Source: Belgian Debt Agency.

HOLDERSHIP BELGIAN SECURITIES
(in %)



Source: NBB.

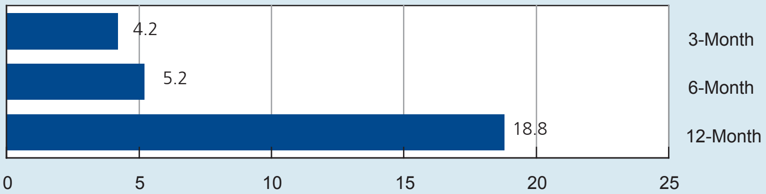
BEST BID/OFFER SPREADS (1)



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

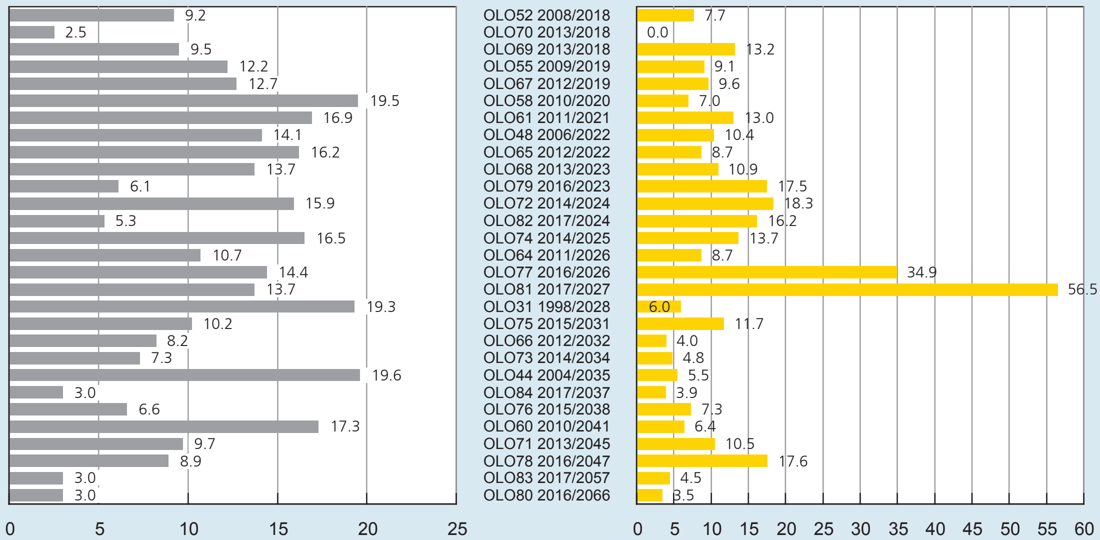
OUTSTANDING AMOUNTS AND TURNOVER
(billions of euros)

TREASURY BILLS
Nominal outstanding amounts at end of December 2017



OLOs
Outstanding amounts at 22 December 2017

Outright turnover Jan.-Nov. 2017



Source: Belgian Debt Agency.

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Published by: National Bank of Belgium (NBB).
Sources: NBB, unless otherwise stated.
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