BELGIAN PRIME NEWS
Quarterly publication

BELGIAN DEBT AGENCY

NationalBank OF BELGIUM
Eurosystem

Participating Primary and Recognised Dealers:
Barclays, Belfius Bank, BNP Paribas Fortis, Citigroup, Crédit Agricole CIB, HSBC, KBC Bank, Morgan Stanley, Natixis, NatWest (RBS), Nomura, Société Générale Corporate & Investment Banking

N° 85 September 2019 Last update: 30 September 2019 Next issue: January 2020

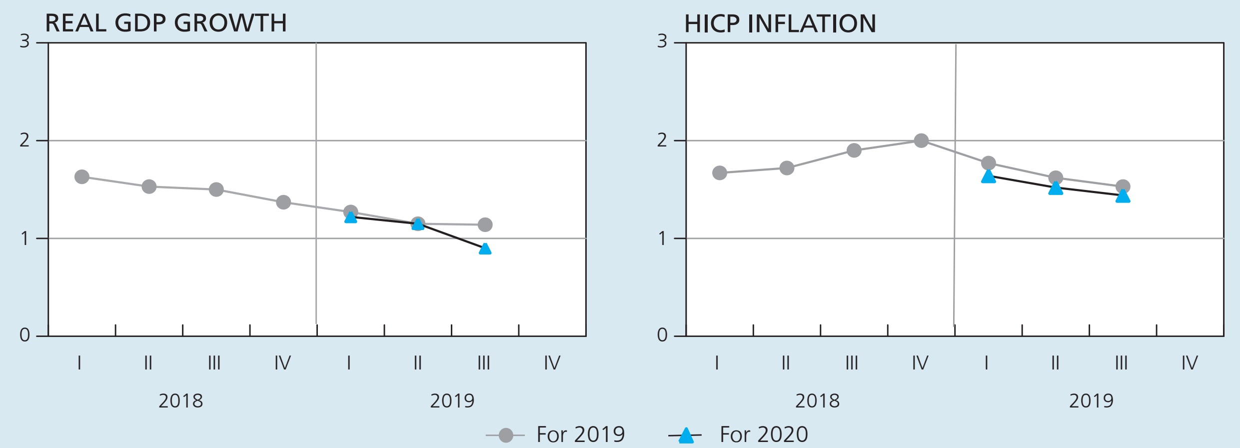
- MACROECONOMIC DEVELOPMENTS: Global downturn in manufacturing industry
- SPECIAL TOPIC: Lower interest charges and reduced risks: a balancing act for debt management
- FINANCIAL MARKETS AND INTEREST RATES: Falling sovereign bond yields amidst monetary policy accommodation
- TREASURY HIGHLIGHTS: The execution of the 2019 funding plan is well on track

CONSENSUS **Average of participants' forecasts**

	Belgium			Euro area		
	2018	2019p	2020p	2018	2019p	2020p
Real GDP(1)	1.4	1.1	0.9	1.9	1.1	1.0
Inflation (HICP)(1)	2.3	1.5	1.4	1.8	1.2	1.2
General government balance(2)	-0.7	-1.4	-1.7	-0.5	-0.9	-1.0
Public debt(2)	102.0	101.4	100.9	85.1	85.4	84.6

(1) Percentage changes.
(2) EDP definition; percentages of GDP.

SUCCESSIVE FORECASTS FOR BELGIUM



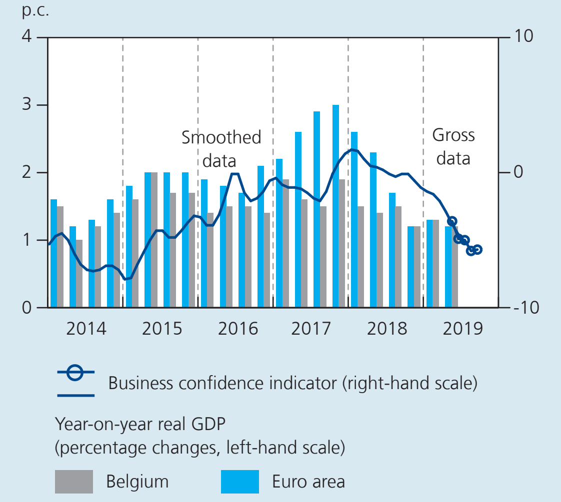
Source: Belgian Prime News.

MACROECONOMIC DEVELOPMENTS **Global downturn in manufacturing industry**

The world economy is facing ongoing uncertainties that are mostly related to trade. Trade tensions between China and the United States have dragged on in recent months and disrupted global supply chains. While the global manufacturing industry is considered to have slid into a recession, the services industry and domestic demand have so far remained more resilient, backed by a robust labour market, providing some support for GDP growth. However, as US-China trade tensions escalated again in August and overall business sentiment is worsening, it is unlikely that the global economy will regain traction in the near term. The Brexit process also adds to the overall uncertainty.

In the euro area, quarterly GDP growth slowed to 0.2% in the second quarter, which was in line with expectations. While the slowdown was broad-based across the large euro area countries, it was most obvious in the German economy, which even contracted as a result of a sharp drop in exports. Most high-frequency euro area indicators and especially those related to the manufacturing industry have continued to worsen over the last few months and are definitely not indicative of any strong rebound in the near term. All in all, BPN participants have revised their forecasts downwards from the June estimate: they now see the **euro area economy growing by 1.1% in 2019 and 1.0% in 2020. Euro area inflation is expected to remain moderate, at around 1.2% in both years**.

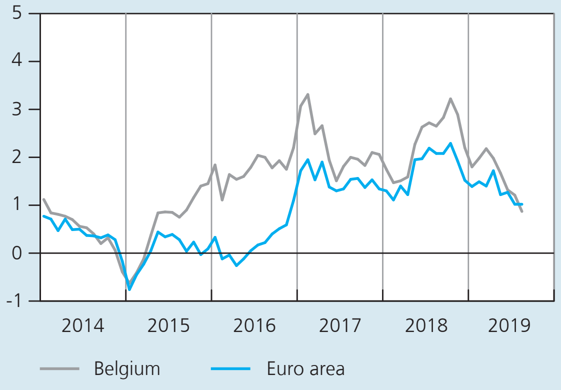
GDP GROWTH AND BUSINESS CYCLE INDICATOR



Sources: EC, NAI, NBB.

In Belgium, economic growth also edged down marginally in the second quarter of 2019 as quarterly GDP growth came in at 0.2%, slightly below the pace recorded at the start of the year. This slowdown was in line with wider euro area developments and consistent with the weakening of domestic confidence indicators. Belgian producer confidence, for instance, clearly deteriorated in the course of the second quarter and has continued its downward path in the last couple of months. **BPN participants currently expect growth in Belgium to reach 1.1% in 2019 and 0.9% in 2020**. This implies a downward revision of 0.2 percentage point for 2020 compared to the June estimate.

INFLATION (HICP)
(annual percentage changes)



Source: EC.

The Belgian labour market has remained surprisingly buoyant as domestic employment continued to expand at a pace that is clearly higher than the quarterly growth rate of GDP. On the other hand, a decline in the volume of temporary agency work has been observed, which could partly be the result of a slowdown in overall labour demand. Meanwhile, on the nominal side, HICP inflation in Belgium has softened considerably in recent months, on account of energy inflation. In August, the overall HICP rate stood at 0.9%. **According to the consensus forecast, inflation in Belgium should come to 1.5% on average in 2019 and 1.4% in 2020.**

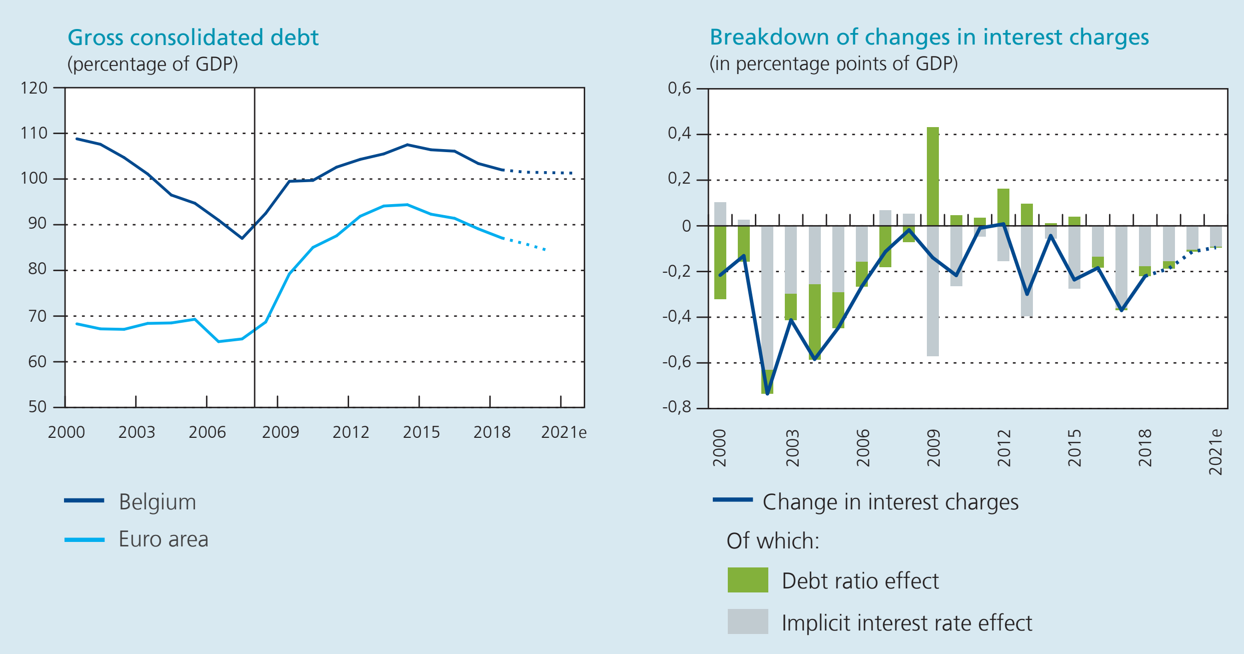
Belgian Prime News participants expect the government deficit to widen substantially from an average of 0.7% of GDP in 2018 to 1.4% of GDP in 2019 and 1.7% of GDP in 2020. In 2019, the tax on labour income is being cut further as part of the phased tax shift programme and corporate income tax revenues are expected to drop because of lower tax assessments, following the shift towards advance payments that has temporarily driven up revenues in the last two years. The rising structural deficit implies that additional fiscal consolidation efforts are required to achieve the medium-term objective of a balanced budget in structural terms by 2021, the target put forward in the 2019 Stability Programme. However, the current federal government is still acting in a caretaker capacity, as a new one is yet to be formed following the general elections held at the end of May. On the basis of their own macro and budgetary forecasts, **BPN participants anticipate a further reduction in the Belgian public sector debt, albeit only slowly, from 102% of GDP at the end of 2018 to just over 100% in 2020**.

SPECIAL TOPIC **Lower interest charges and reduced risks: a balancing act for debt management**

Since the financial crisis, the euro area countries' debt burden has increased significantly. Belgium is no exception to this trend. **Government debt is still very high, running at 102% of GDP in 2018 and the process of debt reduction is relatively slower than the euro area average**. Belgian Prime News participants expect the debt ratio to remain above 100% of GDP in the coming years, similarly to the Bank's latest macroeconomic projections at unchanged policy.

Interest rates have declined significantly over the last few years, pursuing their downward path to hit an all-time low recently. In early July this year, the reference rate on 10-year OLOs fell below the symbolic 0% mark. On July 22, The Belgian Treasury issued 10-year OLOs at a negative interest rate (–0.038%) for the first time ever on the primary market. In August, the rate fell to its lowest level ever, –0.28% on average.

SINCE THE FINANCIAL CRISIS, THE DECLINE IN INTEREST CHARGES HAS MAINLY BEEN DUE TO FALLING INTEREST RATES RATHER THAN LOWER DEBT



Source: EC, NBB.

As a result of the trend of declining interest rates, interest charges paid by the government have fallen continuously over the last years. They reached 2.3% of GDP in 2018, against 6.7% in 2000 and 11.5% in 1990. Since the implicit interest rate on the public debt (currently about 2%) is higher than the market rates, interest charges are expected to decline further in the coming years in the context of a prolonged period of low rates.

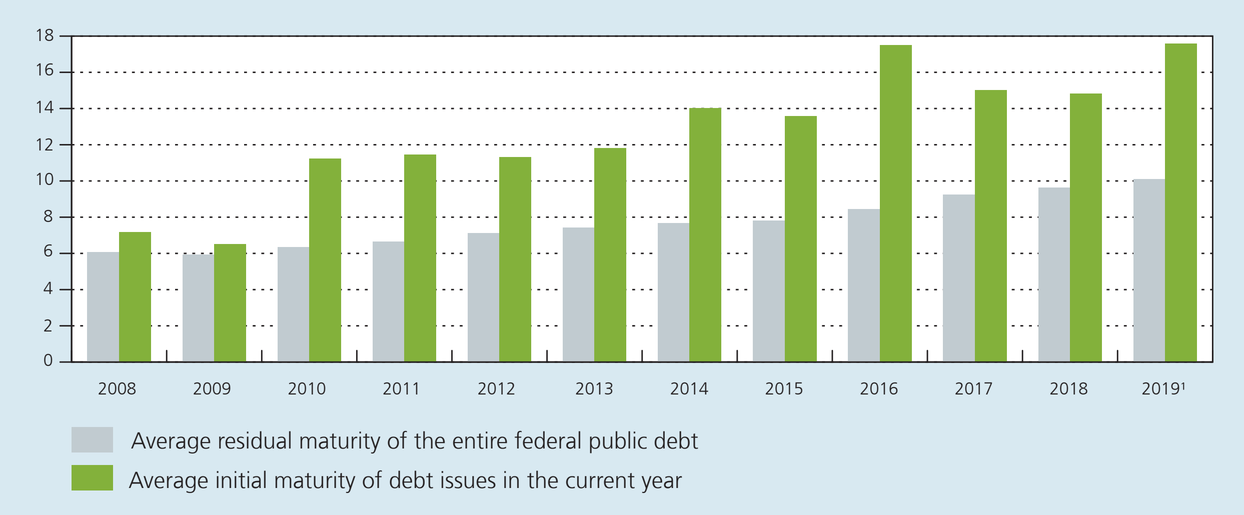
Debt management: maturity extension strategy

Against a backdrop of rising public debt and successive unexpected interest rate shocks during and in the aftermath of the financial and the euro area sovereign debt crises, the federal government's debt management strategy has aimed at continually reducing risks. The average life and duration of the debt have been extended, resulting in a material reduction in the refinancing risk. In fact, each time debt instruments are issued, neither the market rate nor the rate that the Belgian State will have to pay is known in advance and may turn out to be higher than expected.

In this context of low interest rates, **the average maturity for the Belgian federal government debt has gone up from 6 years in 2010 to close to 10 years in 2019.** In practice, the maturity extension observed over the last few years is essentially the result of issues of very long-term OLOs, some of which will fall due in 2047, 2057 and 2066. The strategy of extending the debt maturity is considered to be near completion. Over the next few years, the average maturity should therefore stay close to the level currently observed.

An extension of public debt maturities has been observed in several other countries as well. Over the last decade, the average maturity for public debt in the OECD has gone up from 6.3 to 7.9 years, while it has increased by about 4 years in Belgium.

EXTENSION OF THE RESIDUAL MATURITY OF THE BELGIAN FEDERAL GOVERNMENT DEBT FROM 2010
(residual maturity of the federal debt, in years)



Sources: Belgian Debt Agency.
[1] Figures as at 24 June for the year 2019.

The debt maturity extension does of course come at a price in the short term. In a recent NBB study [1], the additional interest charges in 2018 resulting from the extension of the maturity of the debt since 2010 is estimated at about 0.42% of GDP. However, this cost should be put in a wider context of an overall decline in the cost of debt servicing.

At the same time, the maturity extension offers good protection against a possible rate rise in the future. Extending the debt maturity brings a significant reduction in the risks (including budgetary risks) associated with refinancing, which may be heavy in countries with a high public debt ratio like Belgium. The Belgian federal State's gross borrowing requirements have come down from close to 24% of GDP in the period 2009-2011 to 14% in 2018. They should stabilise around that level over the next few years.

Lower long-term borrowing requirements help to protect a larger part of the debt in the event of a rate rise. In the absence of any rise in interest rates above their current level, the increase in the residual maturity of the debt can be considered an undeniably costly hedge. However, it would only take a moderate, yet lasting, rise in rates for the maturity extension strategy to become more worthwhile. The higher the rate increase, the quicker this strategy will pay off.

Finally, if the markets and rating agencies considered a longer-term debt to be relatively safer (less financing risk and less sensitive to a rate rise), the maturity extension may help exert a downward effect on the interest rate spread between Belgian government bonds and German Bunds.

Capitalising on the low interest environment to put the debt on a sustained downward path

Since the implicit interest rate on the debt has fallen below nominal GDP growth from 2016 onwards, the risk of a snowball effect from interest charges on the debt ratio is limited. However, the current situation of low – and even negative – interest rates cannot be considered as the benchmark scenario in the medium and long run. It would be reckless for fiscal policy and debt management to rely on the assumption that these conditions will last.

Reducing the government debt must remain the key objective of fiscal policy in Belgium. The fiscal room offered by the current rate environment should be used to support sound public finances, while building up a sufficiently high primary balance in order to reduce the deficit and public debt.

[1] Cornille C., H. Godefroid, L. Van Meensel and S. Van Parys (2019), "How risky is the high public debt in a context of low interest rates?", NBB, ***Economic Review***, September.

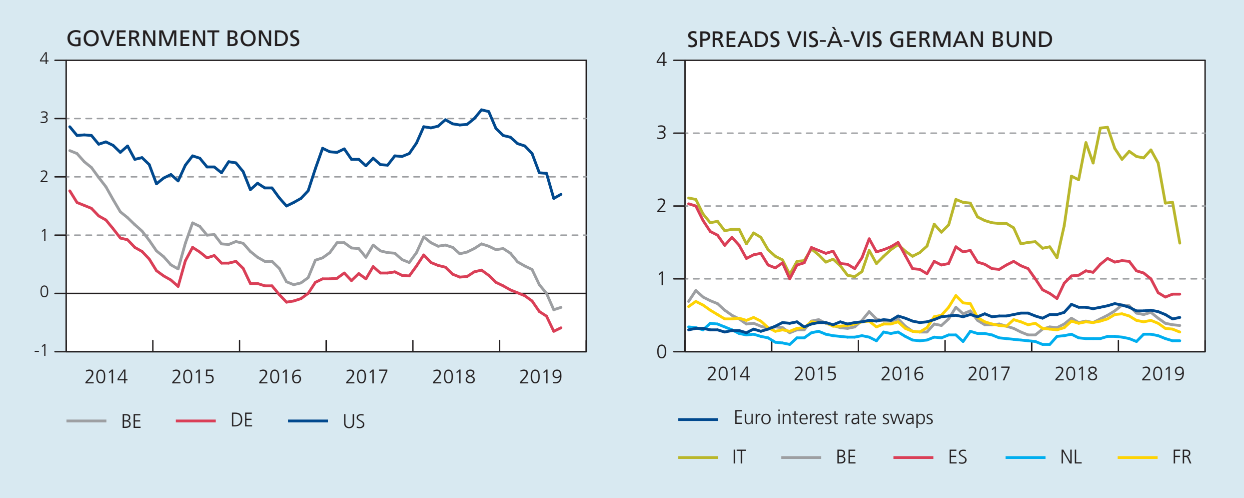
FINANCIAL MARKETS AND INTEREST RATES

Falling sovereign bond yields amidst monetary policy accommodation

While long-term sovereign bond yields continued to fall in the US and the euro area in July and August, they rebounded in September, partially offsetting the downward trend observed over the preceding two months. German and Belgian 10-year yields dropped by 28 and 39 basis points respectively over the third quarter, to settle at −0.59% and −0.24%. A similar fall occurred in the US, where the 10-year yield dropped by 37 basis points to 1.70%. The higher bond yields in the US than in the euro area mainly reflects the different position of the US economy in the business cycle.

The fall in global long-term yields has coincided with expectations of monetary policy easing by the ECB and the Federal Reserve System. In September, the ECB cut its deposit facility rate from −0.4 to −0.5% and decided to resume net purchases under the Governing Council's asset purchase programme, while the Federal Reserve lowered its target range for the federal funds rate by 25 basis points to between 1.75 and 2%. Sovereign bond yields also reflected, to a certain extent, investors' 'flight-to-safety' behaviour as a result of the uncertainties surrounding trade disputes and Brexit. They were also affected by the release of various macroeconomic data indicating decelerating growth, a contraction in global trade and lower inflation expectations. It is also worth noting that the yield curve has remained inverted in the US since the second quarter of 2019, a pattern usually associated with upcoming recessions.

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



Sources: BIS, Thomson Reuters.
Average over the first 25 days for September 2019.

Against a backdrop of monetary easing and the more negative economic outlook, the euro depreciated against safe-haven currencies such as the US dollar, the Japanese yen and the Swiss franc in July and August. Uncertainty surrounding trade and Brexit caused episodes of high volatility for the British pound and the Chinese renminbi. Share prices also stumbled in August, before recovering in September. Despite these ups and downs, financial market volatility has remained relatively low throughout the period considered, with the VIX and VSTOXX standing at respectively 16% and 17% at the end of September (with values below 20% generally associated with stable periods).

The relative tranquillity on the stock market is also reflected in sovereign bond spreads in the euro area, which tended to shrink during the third quarter. In Belgium, the 10-year spread vis-à-vis Germany narrowed by 10 basis points. Most notably, the Italian spread contracted by 110 basis points between June and September but remains relatively high at 1.49%.

TREASURY HIGHLIGHTS **The execution of the 2019 funding plan is well on track**

Two OLO auctions were held in July and September resulting in a total of **€ 5.915** billion worth of funding.

OLO AUCTIONS

Date	OLO	NR	Issued (€ Billion)	Yield	Bid to cover
July 22	OLO 0.90% 22/06/2029 OLO 1.25% 22/04/2033	OLO87 OLO86	1.208 0.779	-0.038% 0.255%	1.42 2.14
Non-competitive subscriptions			*0.669*		
Total July			2.656		
September 23	OLO 1.00% 22/06/2026 OLO 0.90% 22/06/2029 OLO 1.90% 22/06/2038	OLO77 OLO87 OLO76	0.588 1.210 1.011	-0.469 % -0.262 % 0.237%	2.16 1.85 1.86
Non-competitive subscriptions			*0.450*		
Total September			3.259		

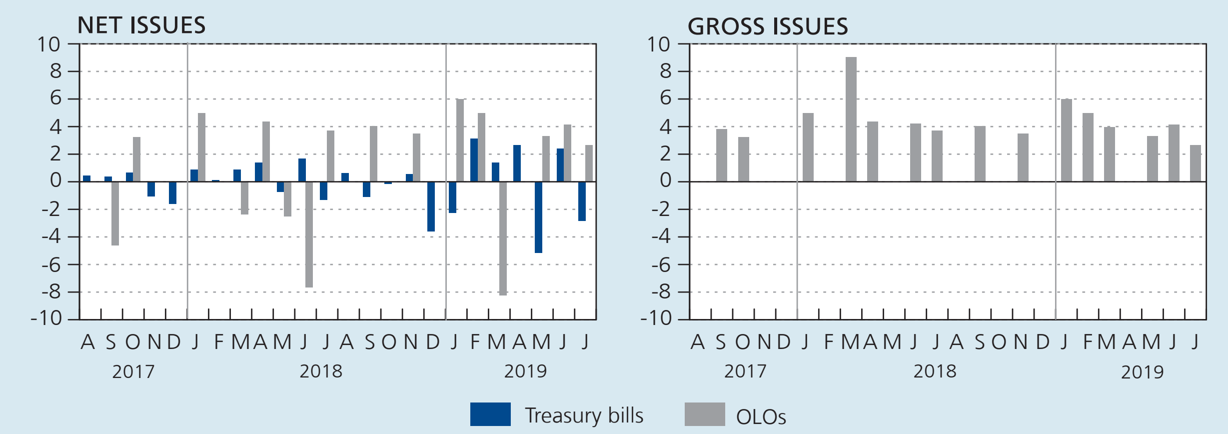
Total issuance now amounts to € 28.43 billion, corresponding to 94 % of its € 30.25 billion funding target.

In terms of portfolio structure, the average life of the portfolio was 9.97 years (end of August). The implicit yield on the portfolio has further declined to 2.04 % (end of August).

With respect to the green OLO, the Belgian Debt Agency has published the Allocation Report for 2018. The Impact Report will be published by the end of the year.

GOVERNMENT SECURITIES STATISTICS

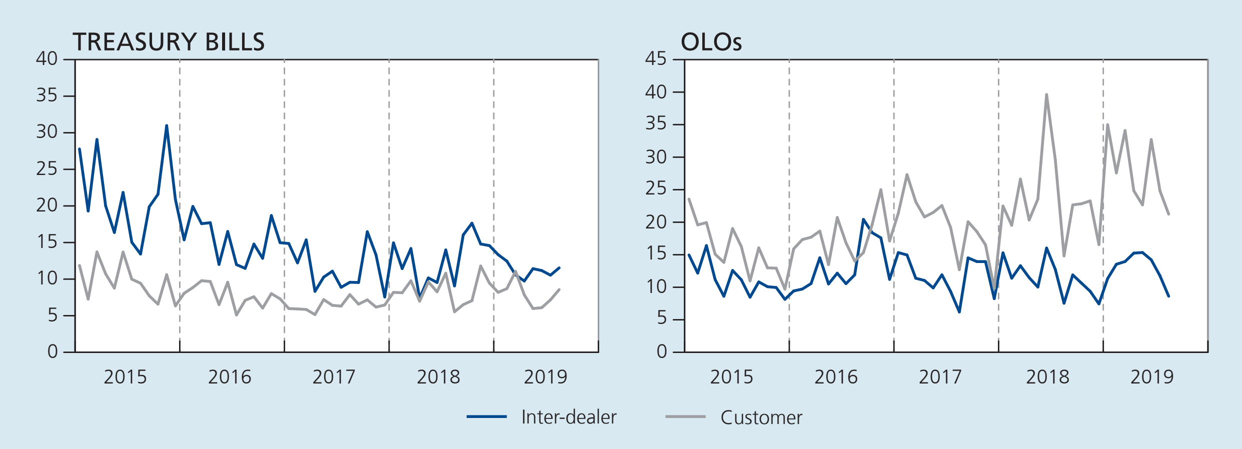
PRIMARY MARKET
(billions of euros)



Source: Belgian Debt Agency.

SECONDARY MARKET TURNOVER

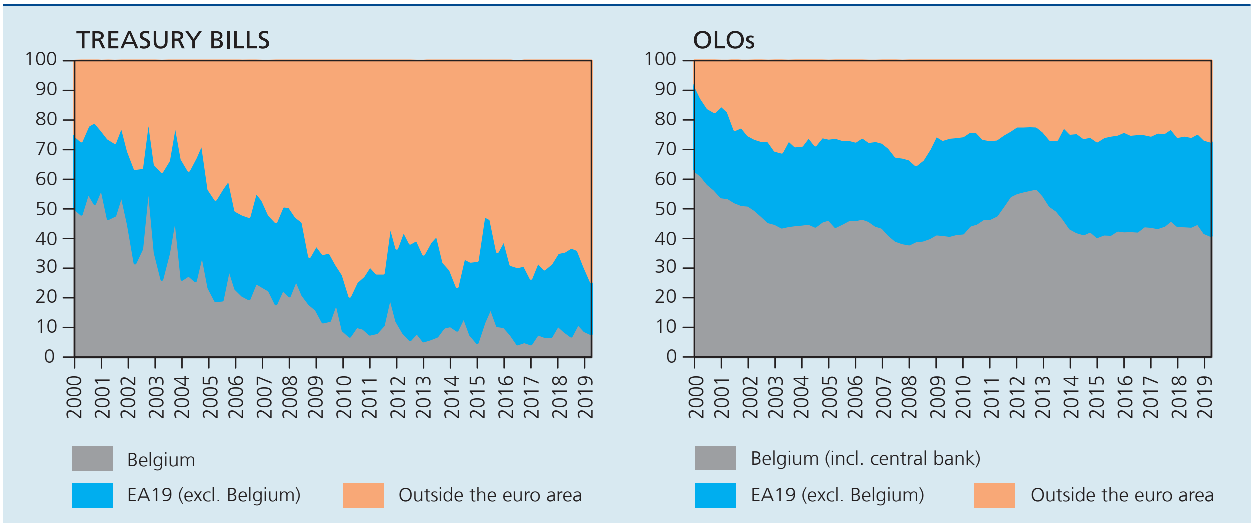
(as reported by primary and recognised dealers to the Treasury, billions of euros)



Source: Belgian Debt Agency.

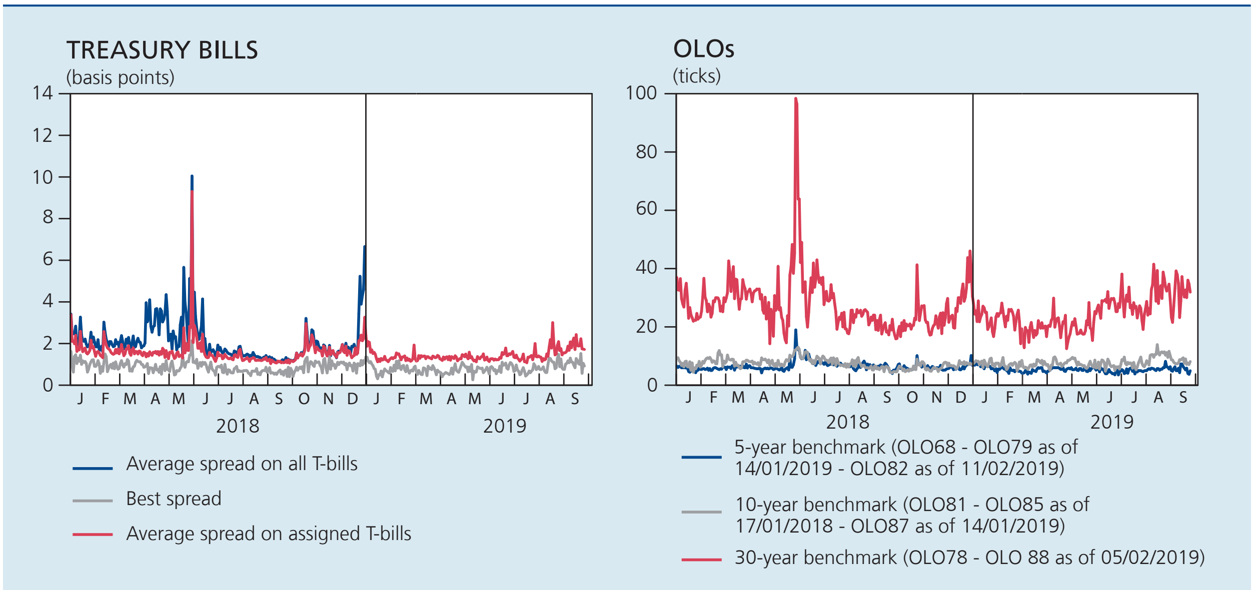
HOLDERSHIP BELGIAN SECURITIES

(in %)



Source: NBB.

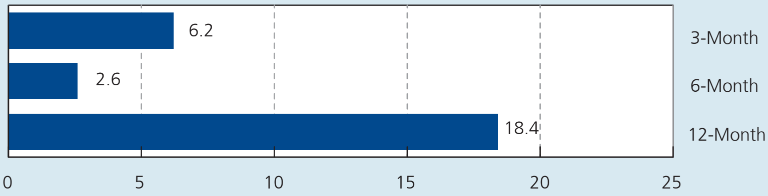
BEST BID/OFFER SPREADS [1]



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

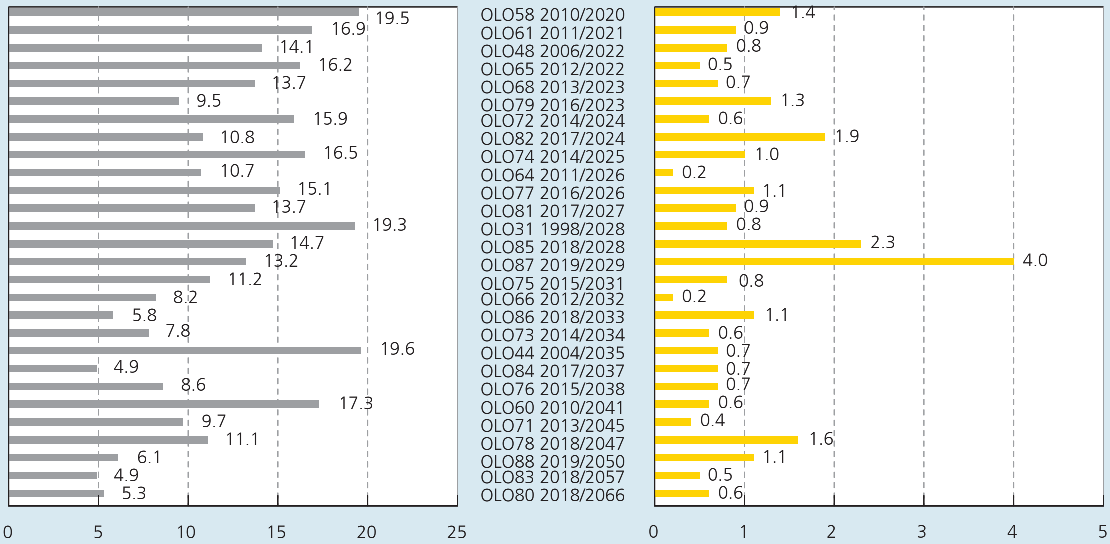
OUTSTANDING AMOUNTS AND TURNOVER
(billions of euros)

TREASURY BILLS
Nominal outstanding amounts at the end of August 2019



OLOs
Outstanding amounts at 30 September 2019

Outright turnover in August 2019



Source: Belgian Debt Agency.

LIST OF CONTACT PERSONS

PARTICIPATING INSTITUTIONS	TECHNICAL EDITORS	TELEPHONE	E-MAIL
Belgian Debt Agency	Mr Jean Deboutte	+32 2 574 72 79	jean.deboutte@minfin.fed.be
Barclays	Mr François Cabau	+44 20 3134 3592	francois.cabau@barclays.com
Belfius Bank	Ms Catherine Danse	+32 2 222 71 13	catherine.cd.danse@belfius.be
BNP Paribas Fortis	Mr Philippe Gijsels	+32 2 565 16 37	philippe.gijsels@bnpparibasfortis.com
	Mr Arne Maes	+32 2 312 12 10	arne.maes@bnpparibasfortis.com
Citigroup	Mr Guillaume Menuet	+44 20 7986 3281	guillaume.menuet@citi.com
Crédit Agricole CIB	Mr Louis Harreau		louis.harreau@ca-cib.com
	Mr Ludovic Martin	+33 1 43 23 39 37	ludovic.martin@credit-agricole-sa.fr
HSBC	Mr Olivier Vigna	+33 1 40 70 32 66	olivier.vigna@hsbc.fr
KBC Bank	Mr Peter Wuyts	+32 2 417 32 35	peter.wuyts@kbc.be
	Mr Jan Van Hove	+32 2 429 59 50	chiefeconomist@kbc.be
Morgan Stanley	Mr Daniele Antonucci	+44 20 7425 8943	daniele.antonucci@morganstanley.com
Natixis	Mr Jean-Christophe Machado		jeanchristophe.machado@natixis.com
NatWest (RBS)	Ms Oriane Parmentier	+44 20 3361 1743	oriane.parmentier@natwestmarkets.com
Nomura	Mr Marco Brancolini	+44 20 7102 0724	marco.brancolini@nomura.com
Société Générale Corp. & Inv. Banking	Mr Michel Martinez	+33 1 42 13 34 21	michel.martinez@sgcib.com
	Mr Yvan Mamalet	+44 20 7762 5665	yvan.mamalet@sgcib.com

GENERAL INFORMATION

National Bank of Belgium	Mr Luc Dresse	+32 2 221 20 39	luc.dresse@nbb.be

Published by: National Bank of Belgium (NBB).
Sources: NBB, unless otherwise stated.
This publication is also available on the website: www.nbb.be.
Information on the Belgian government debt can be found on the Treasury website: www.debtagency.be.
General information on the Belgian government's action can be found on the website: www.belgium.be.