Kingdom of Belgium
Rating Report

SCOPE AA- STABLE OUTLOOK

Credit strengths

- Wealthy and diversified economy
- Favourable debt profile and strong market access
- Strong external position

Credit challenges

- High public debt levels
- Fiscal pressures due to ageing population
- Low productivity growth, labour market rigidities and weak business dynamism

Rating rationale:

Wealthy and diversified economy: Belgium benefits from its high wealth levels and diversified economic structure, supported by high value-added services. This underpins resilience to shocks and shields Belgium's open economy from adverse external developments.

Favourable debt profile and strong market access: Government debt is characterised by a long average maturity, a low share of short-term debt and no foreign currency exposures. This robust debt profile combined with strong market access and the ECB's still accommodative monetary policy stance, partially mitigate risks stemming from high public debt levels.

Sound external position: High net international investment assets combined with diversified destination markets across Europe and the innovativeness and competitiveness of key exporting industries helps to mitigate external risks. Still, Belgium's external position faces several challenges related to adverse developments in competitiveness, including rising labour costs and adverse productivity developments.

Rating challenges include: i) elevated public indebtedness; ii) substantial fiscal pressures related to an ageing population which weigh on the budget balance and limit prospects for material fiscal consolidation; and iii) structural economic weaknesses in the form of declining productivity growth, lagging business dynamism and labour market bottlenecks.

Belgium's sovereign rating drivers

Risk pillars		Quantitative scorecard		Reserve currency adjustment (notches)	Qualitative scorecard	Final rating
		Weight	Indicative rating		Notches	
Domestic Economic Risk		35%	aaa		-1/3	AA-
Public Finance Risk		25%	bbb		-1/3	
External Economic Risk		10%	aa-		0	
Financial Stability Risk		10%	aaa		0	
ESG Risk	Environmental Risk	5%	a+		-1/3	
	Social Risk	5%	bbb-		0	
	Governance Risk	10%	aa+		-1/3	
Overall outcome		aa-		+1	-1	

Note: The sum of the qualitative adjustments, capped at 1 notch per rating pillar, is weighted equally and rounded to the nearest integer. The reserve currency adjustment applies to currencies in the IMF's SDR basket. In line with our methodology, movements between indicative ratings are not immediate but are executed after analyst review of CVS results. The rating committee approved an implied core variable scorecard (CVS) rating of 'aa-'.

For details, please see Scope's 'Sovereign Ratings' methodology. Source: Scope Ratings

Outlook and rating triggers

The Stable Outlook reflects Scope's view that risks to the ratings are balanced over the next 12 to 18 months.

Positive rating-change drivers

- Public debt is placed on a firm downward trajectory
- Economic growth outlook improves over the medium-term

Negative rating-change drivers

- Fiscal outlook deteriorates resulting in increasing public debt trajectory
- Economic growth outlook weakens over the medium-term
- Political instability re-emerges, further hampering effective policymaking

Ratings and Outlook

Foreign and local currency

Long-term issuer rating	AA-/Stable
Senior unsecured debt	AA-/Stable
Short-term issuer rating	S-1+/Stable

Lead Analyst

Thibault Vasse
+33 1 86 26 24 55
t.vasse@scoperatings.com

Team Leader

Dr Giacomo Barisone
+49 69 6677389-22
g.barisone@scoperatings.com

Scope Ratings GmbH

Neue Mainzer Straße 66-68
60311 Frankfurt am Main

Phone +49 69 6677389-0

Headquarters

Lennéstraße 5
10785 Berlin

Phone +49 30 27891-0
Fax +49 30 27891-100

info@scoperatings.com
www.scoperatings.com

Bloomberg: RESP SCOP

Domestic Economic Risks

- **Growth outlook:** The Covid-19 pandemic led to a historic contraction of Belgium's GDP of 5.7% in 2020. GDP growth rebounded strongly in 2021 to 6.1%, mainly driven by the strong recovery in household consumption and private investment that followed the progressive removal of health restrictions. Real GDP edged above the pre-crisis level in 2021 Q3, before growth slowed down at the end of the year following an uptick in Covid-19 cases and supply chain bottlenecks. Despite its moderate direct ties to Russia and Ukraine, the Belgian economy still stands to be negatively impacted by the ongoing war, largely due to the sharp increase in global energy prices as well as to the overall slowdown of the European economy. Long-term challenges to the growth outlook relate to Belgium's declining productivity growth which combined with rising labour costs threatens to erode the competitiveness of Belgium's trade-oriented economy. We expect annual growth to moderate to 2.2% in 2022 before gradually converging towards the medium-term potential of around 1.2% by 2025.

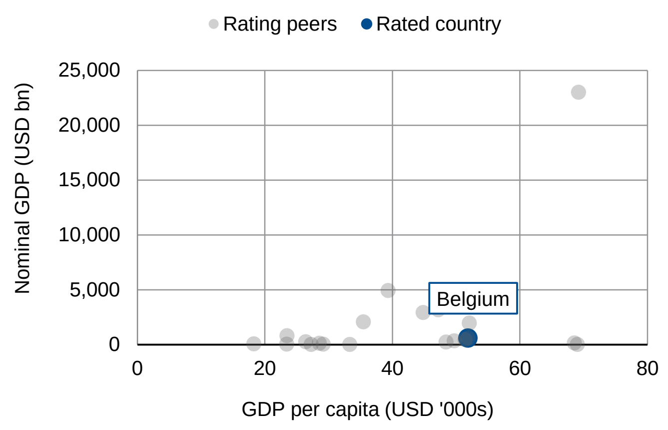
- **Inflation and monetary policy:** Belgium experienced accelerating inflation in the recent period, averaging 3.2% in 2021, and further rising to 9.5% in March 2022, one of the highest rates among EU peers. This is primarily related to the increase in energy prices, though core inflation is well above historical averages as well, at 3.6% in March. Belgium's mechanism of automatic wage indexation to prices could expose the country to a wage-price spiral, also given the tight labour market. However, we expect wage-price pressures to remain contained.

- **Labour market:** The Belgian labour market performed relatively well throughout the Covid-19 pandemic thanks to the strong government support measures and the robust growth in 2021. Total employment increased above its pre-crisis level by end-2021 and the unemployment rate declined to 6% in February 2022. Belgium's employment rate remains low compared to peers, however, at 70% in 2020, 2.3pps below the EU average. Labour shortages have increased, curbing growth in several sectors, primarily construction and manufacturing. The government recently agreed on a labour market reform aimed at modernising the labour code and lifting the employment rate to 80% by 2030, through increased worker flexibility and a push for skills development.

Overview of Scope's qualitative assessments for Belgium's *Domestic Economic Risks*

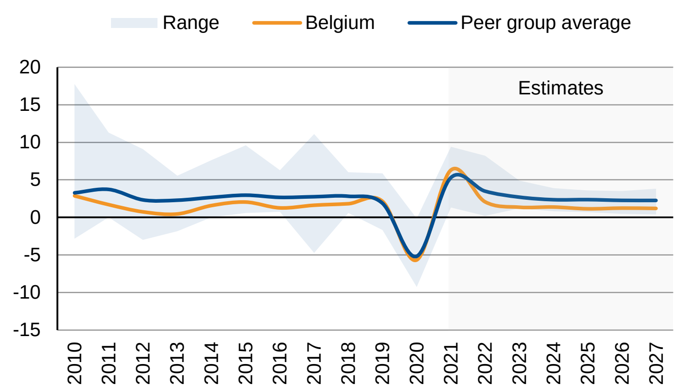
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aaa	Growth potential of the economy	Weak	-1/3	Low and declining growth potential requires policy response
	Monetary policy framework	Neutral	0	ECB is a highly credible and effective central bank; effective policy framework and transmission over the cycle
	Macro-economic stability and sustainability	Neutral	0	Diversified economy supports economic stability; structural pressures on productivity and competitiveness weigh on sustainability

Nominal GDP and GDP per capita, USD '000s



Source: IMF WEO, Scope Ratings

Real GDP growth, %



Source: IMF WEO, Scope Ratings

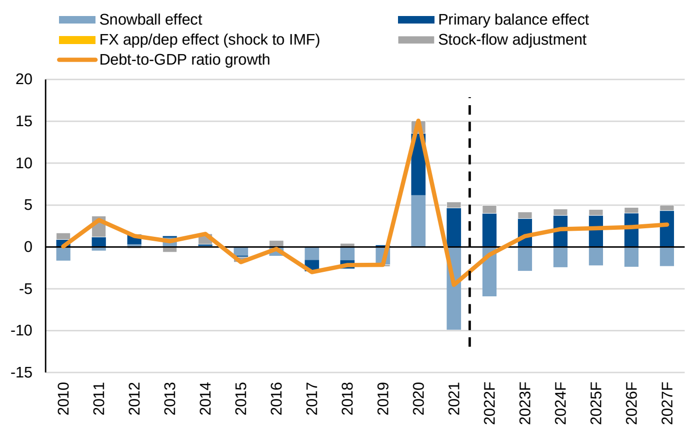
Public Finance Risks

- **Fiscal outlook:** The general government deficit moderated to an estimated 5.5% of GDP in 2021, down from 9.1% in 2020 and below initial forecasts, thanks to a stronger than expected rebound in tax receipts as well as to lower Covid 19-related expenditures. Looking ahead, the fiscal consolidation process will be hindered by the fallout from the war in Ukraine. Government measures estimated at about 0.6% of GDP have been rolled out, aimed at protecting households' purchasing power, reducing the country's reliance on Russian energy imports as well as to welcome refugees. The crisis will also weigh on consumer spending and slow down government revenue growth. Still, we expect the budget deficit to narrow gradually in the coming years to 4.4% by 2023 before widening thereafter due to upward pressures on social spending weighing on the government's fiscal performance.
- **Debt trajectory:** After increasing by 15pps to 112.8% of GDP in 2020 due to the Covid-19 crisis, the government debt-to-GDP ratio declined somewhat to 108.3% in 2021 thanks to strong expansion of economic activity. While we expect the continuation of the recovery to support a further moderate reduction in public indebtedness in 2022, we still expect debt to return to an upward trajectory in subsequent years and to reach 118% of GDP in 2027.
- **Market access:** Belgium benefits from a favourable debt structure with long public maturities (average maturity of 10.2 years as of March 2022) and a stable investor base. The foreign currency share of debt is at 0% after accounting for swaps. Similarly to peers, financing costs have increased somewhat recently in a context of tightening monetary policy, with yields rising to 0.79% on average in March 2022 (up from -0.04% in March 2021). The Belgian Debt Agency aims to issue EUR 44.2bn of debt securities in 2022, nearly 40% of which it had already issued as of 28 April 2022.

Overview of Scope's qualitative assessments for Belgium's *Public Finance Risks*

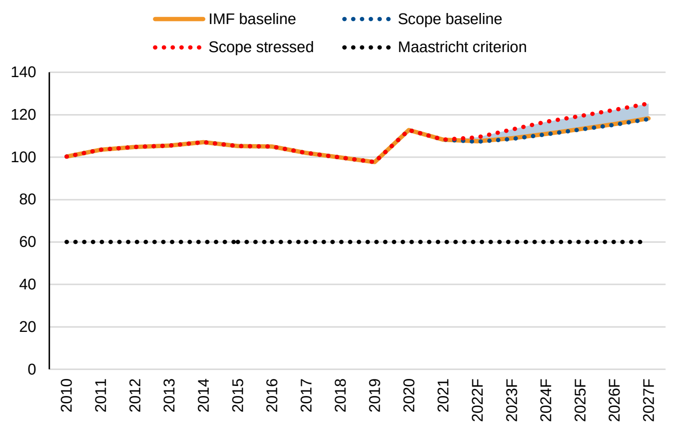
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
a-	Fiscal policy framework	Neutral	0	Post-crisis improvement of fiscal indicators; difficulties in facing expected long-term deterioration in fiscal performance related to social spending pressures
	Debt sustainability	Weak	-1/3	High and increasing public-debt levels, set to remain on an upward trajectory
	Debt profile and market access	Neutral	0	Low and declining interest-payment burden, high average debt maturity, strong market access

Contributions to changes in debt levels, pps of GDP



Source: Scope Ratings

Debt-to-GDP forecasts, % of GDP



Source: IMF WEO, Scope Ratings

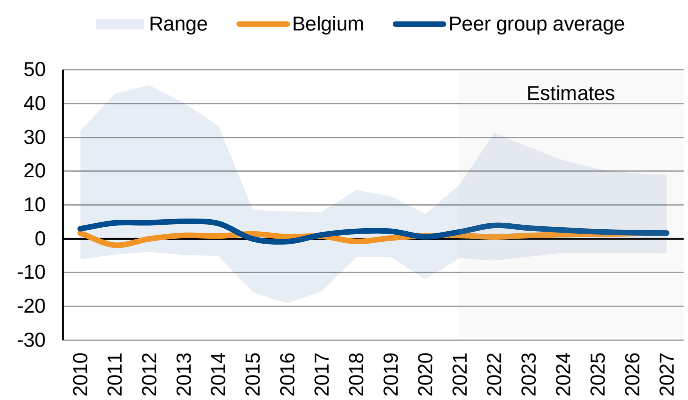
External Economic Risks

- **Current account:** Belgium's current account balance proved resilient throughout the Covid-19 crisis and recovered swiftly from the initial slump that followed the onset of the pandemic, primarily due to a growing trade surplus. This rebound was largely driven by the performance of the pharmaceutical sector and the production of Covid-19 vaccines. After reaching an estimated 0.9% of GDP in 2021, we expect Belgium's current account surplus to remain positive. The sharp rise in energy prices will weigh on the country's trade balance in the short term, however. Direct trade exposure to Russia is limited, representing less than 1% of Belgian exports. The acceleration of inflation and the resulting wage rises risk weakening Belgium's competitiveness, adding to the country's long-standing productivity challenges and potentially weakening its current account.
- **External liabilities and assets:** Belgium's external position benefits from its large and increasing net creditor position with the net international investment position at about 45.1% of GDP as of end-2020. Gross external debt is elevated, at about 257% of GDP, but has a stable and favourable composition, being mostly comprised of long-term, public-sector liabilities and intercompany loans.
- **Resilience to short-term shocks:** Belgium, along with all euro area members, benefits from the euro's status as a global reserve currency, significantly mitigating risks to external shocks.

Overview of Scope's qualitative assessments for Belgium's *External Economic Risks*

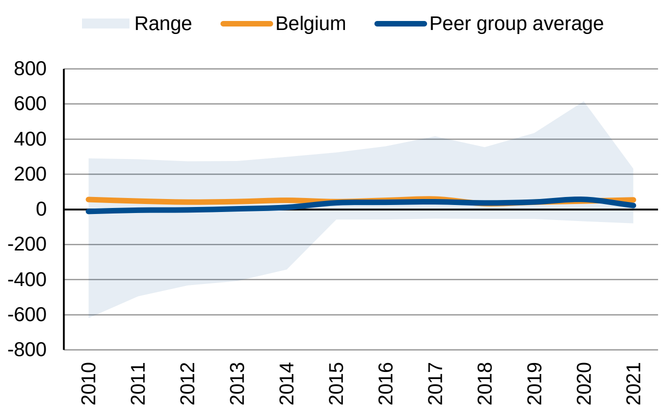
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aa-	Current account resilience	Neutral	0	Post-crisis moderate current-account deficits reflecting competitiveness challenges; diversified export base
	External debt structure	Neutral	0	Large external debt stock, but significant external assets
	Resilience to short-term shocks	Neutral	0	Euro-area membership shields against short-term external risks

Current account balance, % of GDP



Source: IMF WEO, Scope Ratings

NIIP, % of GDP



Source: IMF WEO, Scope Ratings

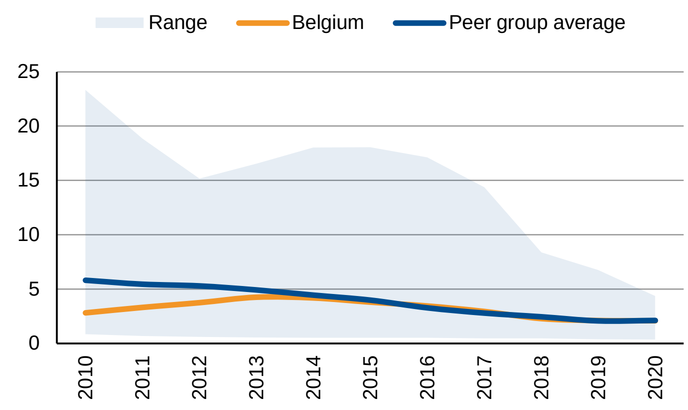
Financial Stability Risks

- **Banking sector:** The Belgian banking sector proved resilient throughout the Covid-19 crisis and recovered well along the rest of the Belgian economy in 2021. Profitability as measured by return-on-equity increased to 9.2% in 2021 Q3, above pre-crisis level. The NPL ratio is low and stable at 3.4% in September 2021, though it could increase somewhat in coming months following the withdrawal of government support measures. The sector benefits from a strong capitalization level, with a 17.7% CET-1 ratio, as well as from comfortable liquidity, with a 180% liquidity coverage ratio in September 2021. Looking ahead, the normalization of monetary policy and the expected increase in interest rates should support profitability further.
- **Private debt:** Leverage in the private sector is elevated and has increased in recent years. Household debt increased to 63% of GDP and non-financial corporate debt to 118% of GDP in September 2021, above the respective euro area averages. Lending conditions remained broadly stable in recent years, even tightening somewhat over the 2020-21 period, following additional prudential measures introduced by the NBB. The risks associated with this high leverage are partially mitigated by the record high level of net financial wealth of Belgian households, which reached EUR 1,500bn in September 2021, a 3.1% increase from January, largely driven by increases in asset valuation.
- **Financial imbalances:** The overvaluation of real estate assets and the elevated level of private debt represent financial stability risks. Housing market activity picked up swiftly in 2021, fueling a rapid price growth in residential real estate (+8.5% over the first three quarters of 2021), above the euro area average. This caused housing affordability to diminish somewhat in recent months, as seen in the rising share of households' disposable income spent on repaying new mortgage loans. The rise in interest rates and the increase in construction costs should hinder the growth in housing supply in the medium-term and further weigh on housing affordability.

Overview of Scope's qualitative assessments for Belgium's *Financial Stability Risks*

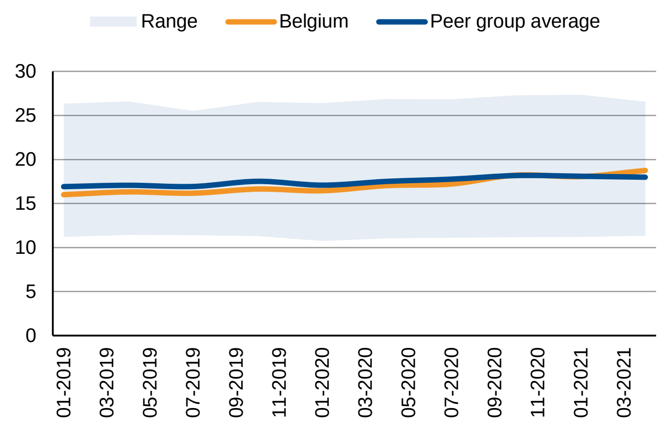
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aaa	Banking sector performance	Neutral	0	Strong capitalisation, asset quality and liquidity buffers; low interest rates pose profitability challenges
	Banking sector oversight	Neutral	0	Robust oversight under the National Bank of Belgium and the ECB as part of Banking Union
	Financial imbalances	Neutral	0	Elevated private debt levels and rising housing market vulnerabilities; large household financial wealth

NPLs, % of total loans



Source: IMF WEO, Scope Ratings

Tier 1 ratio, % of risk-weighted assets



Source: IMF WEO, Scope Ratings

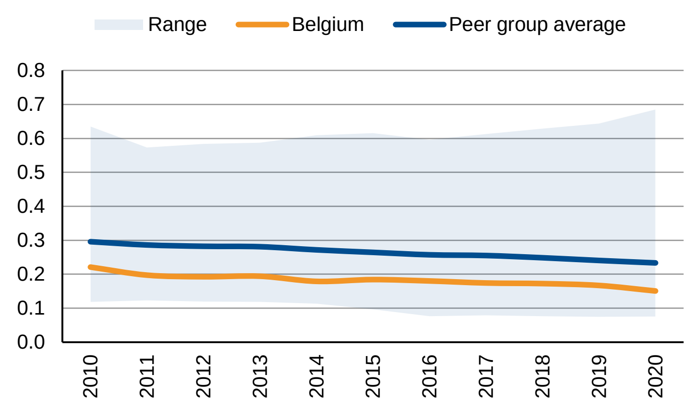
ESG Risks

- **Environment:** With 9.0 mtCO²e emissions per capita in 2019, the Belgian economy is relatively more carbon intensive than European peers and accounts for 3.3% of total EU emissions. Belgium's energy mix is largely made of imported fossil, primarily oil (36%) and natural gas (30%). The share of renewable energy in total energy supply doubled between 2010 and 2020, from 6% to 12%, but remains among the lowest in the EU. The European Commission deems Belgium's National Energy and Climate Plan to be unambitious as regards its contribution to renewable energy. Over 50% of electricity is generated by the seven nuclear reactors, which were initially scheduled to close between 2022 and 2025. Following the breakout of the Ukraine war and the subsequent jump in global energy prices, the government announced its intention to postpone their phase out to 2035 and introduced a EUR 1.1bn investment package in renewable energy to accelerate the transition to climate neutrality.
- **Social**: Labour force participation is weaker than peers with activity rates of 69.8% as of June 2021. Belgium suffers from regional inequality, with a regional GDP per capita in Brussels of EUR 64k versus EUR 38k in the Flemish Region and only EUR 27k in Wallonia. Demographic trends are unfavourable with the UN projecting the old-age dependency ratio to rise from 32.5% in 2019 to 51.8% in 2060, broadly in line with peers but weighing structurally on public finances and economic growth over the long-term.
- **Governance:** The rising political fragmentation and polarisation of Belgium's complex political system weigh on the country's ability to design and implement policies at the national level. After Belgium was run by a caretaker government for almost two years during which national policy making was at almost complete standstill, a new federal government coalition was formed in September 2020. Looking ahead, Scope expects policy making in Belgium to remain constrained given the broad range of views among the coalition partners which comprise seven political parties.

Overview of Scope's qualitative assessments for Belgium's *ESG Risks*

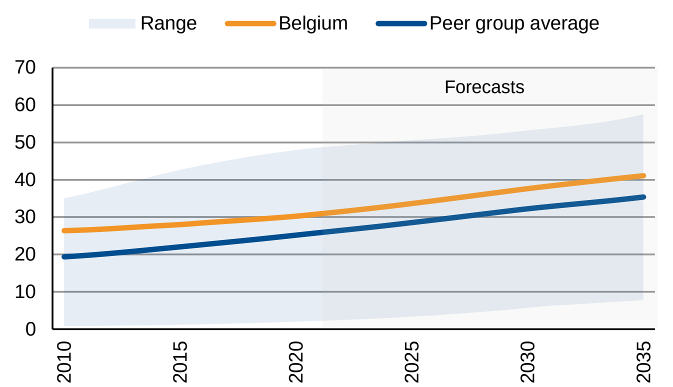
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
a+	Environmental risks	Weak	-1/3	High reliance on fossil fuel imports, slow progress towards climate neutrality objectives, meaningful transition risks
	Social risks	Neutral	0	Strong social safety nets; skills mismatches and persistent regional inequalities are challenges
	Institutional and political risks	Weak	-1/3	Political fragmentation and polarisation constrain effective policy-making; fragile government coalition poses risks of another political stalemate

CO2 emissions per GDP, mtCO2e



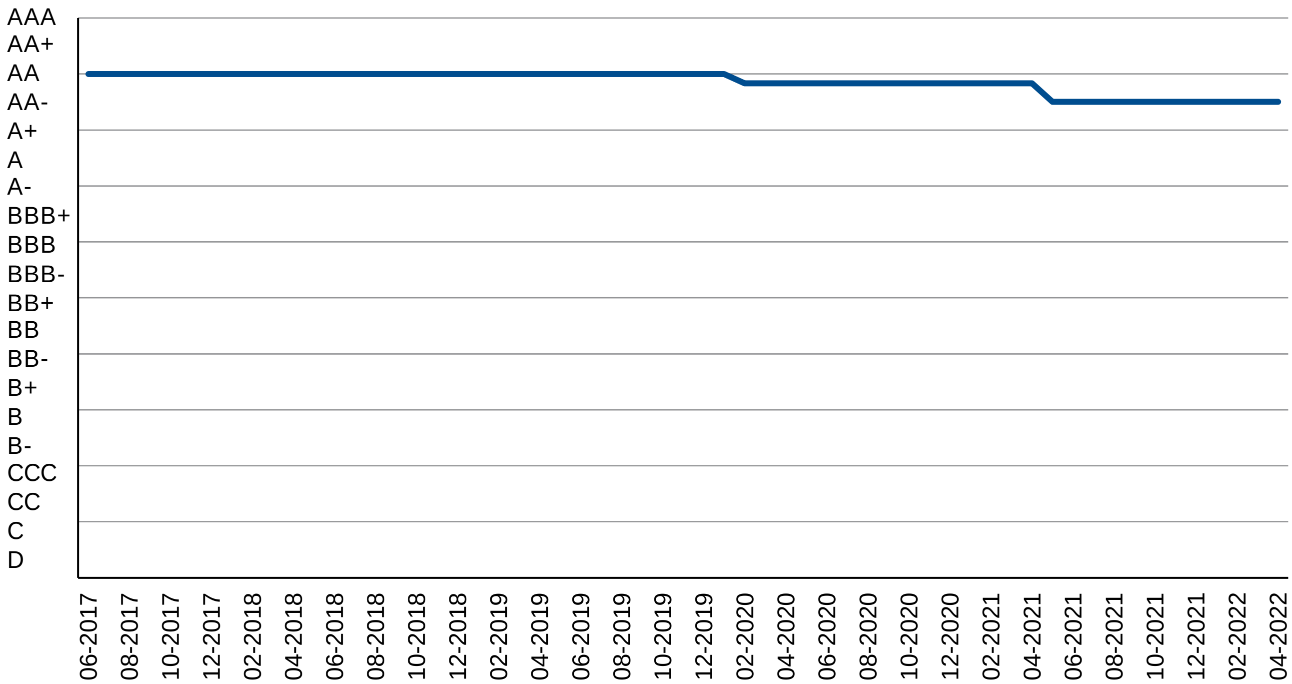
Source: European Commission, Scope Ratings

Old age dependency ratio, %



Source: United Nations, Scope Ratings

Appendix I. Rating history



Appendix II. Rating peers

Rating peers are related to sovereigns with an indicative rating in the same rating category or in adjacent categories per Scope's Core Variable Scorecard.

Peer group*
Belgium
Czech Republic
Estonia
France
Italy
Japan
Lithuania
Malta
Slovenia
United Kingdom
United States

Publicly rated sovereigns only; the full sample may be larger.

Appendix III. Statistical table for selected CVS indicators

This table presents a selection of the indicators (24 out of 29) used in Scope's quantitative model, the Core Variable Scorecard.

	2016	2017	2018	2019	2020	2021E	2022F	2023F
Domestic Economic Risk								
GDP per capita, USD 000s'	42.1	44.3	47.7	46.7	45.3	51.9	52.5	54.8
Nominal GDP, USD bn	475.9	502.6	543.5	535.3	521.4	600.0	609.9	639.7
Real growth, %[1]	1.3	1.6	1.8	2.1	-5.7	6.3	2.2	1.5
CPI inflation, %	1.8	2.2	2.3	1.2	0.4	3.2	8.0	1.3
Unemployment rate, %[1]	7.9	7.2	6.0	5.4	5.7	6.3	6.0	5.8
Public Finance Risk								
Public debt, % of GDP[1]	105.0	102.0	99.9	97.7	112.8	108.3	107.3	108.6
Interest payment, % of government revenue	4.7	4.0	3.6	3.4	3.4	2.8	2.2	2.0
Primary balance, % of GDP[1]	0.0	1.4	1.0	-0.2	-7.4	-3.9	-4.0	-3.4
External Economic Risk								
Current account balance, % of GDP	0.6	0.7	-0.8	0.2	0.8	0.9	0.5	0.9
Total reserves, months of imports	0.6	0.7	0.6	0.7	0.8	-	-	-
NIIP, % of GDP	51.9	59.5	33.3	41.3	47.8	54.6	-	-
Financial Stability Risk								
NPL ratio, % of total loans	3.4	2.9	2.3	2.1	2.1	-	-	-
Tier 1 ratio, % of risk weighted assets	16.2	16.9	16.5	16.6	18.2	18.8	-	-
Credit to private sector, % of GDP	63.4	65.1	68.1	69.9	75.8	-	-	-
ESG Risk								
CO^2 per EUR 1,000 of GDP, $mtCO^2e$	180.3	174.3	172.6	167.1	150.9	-	-	-
Income quintile share ratio (S80/S20), x	4.2	4.2	4.1	4.1	-	-	-	-
Labour force participation rate, %	67.7	68.1	68.6	69.1	-	-	-	-
Old age dependency ratio, %	26.3	26.5	26.6	26.7	26.7	26.7	26.7	26.7
Composite governance indicator[2]	1.3	1.2	1.2	1.2	1.2	-	-	-

[1] Forecasted values are produced by Scope and may differ from those presented in the charts of the previous sections
[2] Average of the six World Bank Governance Indicators
Source: European Commission, IMF WEO, World Bank, Scope Ratings

Appendix IV. Economic development and default indicators

IMF Development Classification	Advanced economy
5y USD CDS spread (bps) as of 22.04.2022	14.1

Scope Ratings GmbH

Headquarters Berlin

Lennéstraße 5
D-10785 Berlin

Phone +49 30 27891 0

Frankfurt am Main

Neue Mainzer Straße 66-68
D-60311 Frankfurt am Main

Phone +49 69 66 77 389 0

Paris

23 Boulevard des Capucines
F-75002 Paris

Phone +33 6 62 89 35 12

Oslo

Karenslyst allé 53
N-0279 Oslo

Phone +47 21 62 31 42

Madrid

Paseo de la Castellana 141
E-28046 Madrid

Phone +34 91 572 67 11

Milan

Via Nino Bixio, 31
20129 Milano MI

Phone +39 02 30315 814

Scope Ratings UK Limited

London

52 Grosvenor Gardens
London SW1W 0AU

Phone +44 20 7824 5180

info@scoperatings.com
www.scoperatings.com