Belgisch Instituut voor Overheidsfinanciën

17.01.2023

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DE BELGIQUE VAN BELGIË
Eurosystem

How sustainable are the finances of the federal government, the regions and communities in Belgium?

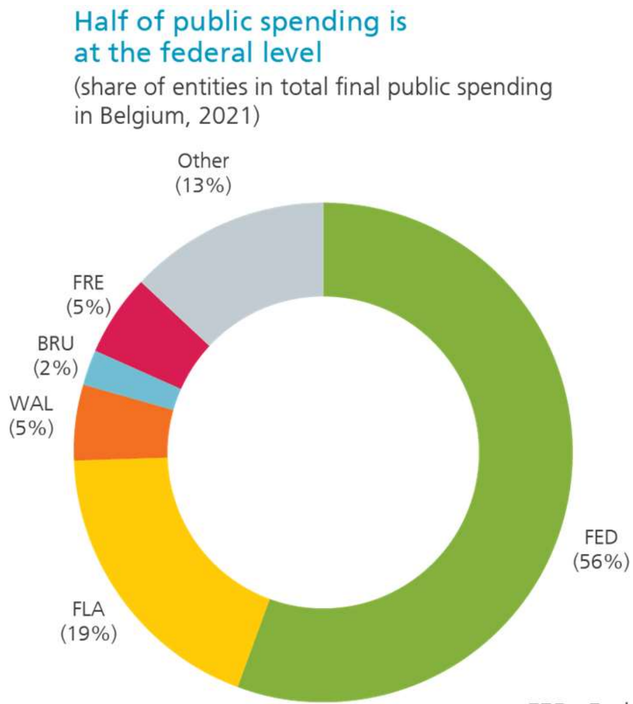
David Cornille, Marjolein Deroose, Hervé Godefroid,
Wim Melyn, Pierrick Stinglhamber and Stefan Van Parys

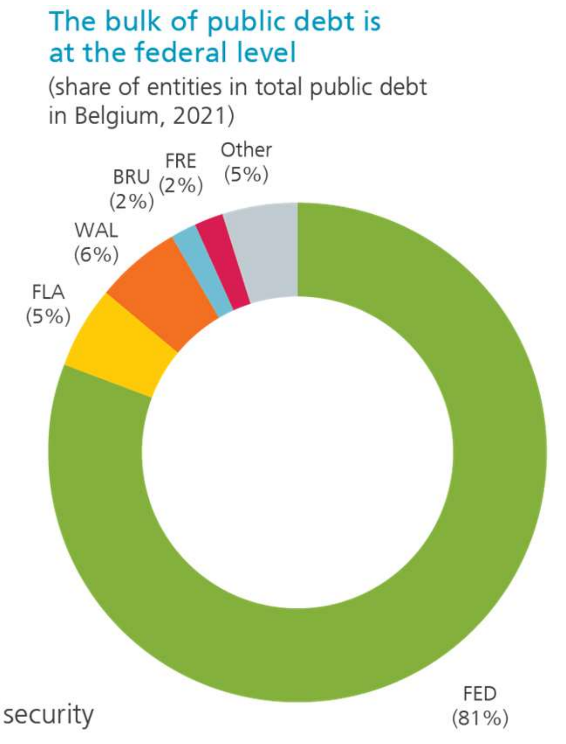
21 December 2022

This presentation is based on an article published in the NBB Economic Review on 24 November 2022

1. Main characteristics and fiscal outlook of the government entities
2. Debt sustainability analysis
3. Towards public debt of 100% of GDP in 20 years
4. Conclusion

Belgian public debt is overwhelmingly concentrated at the federal level





FED: Federal government and social security

FLA: Flemish Community

WAL: Walloon Region

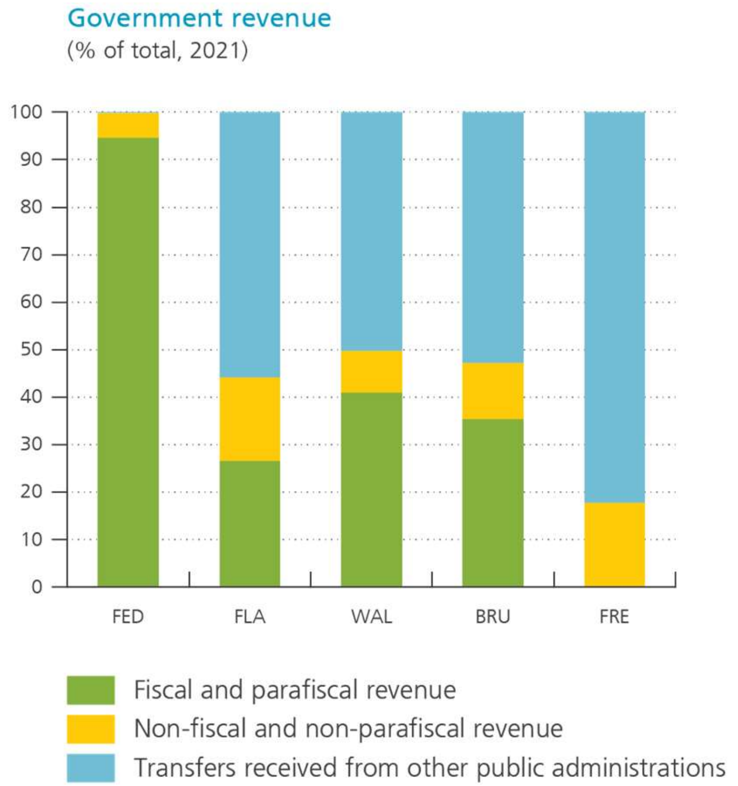
BRU: Brussels-Capital Region and Common Community Commission

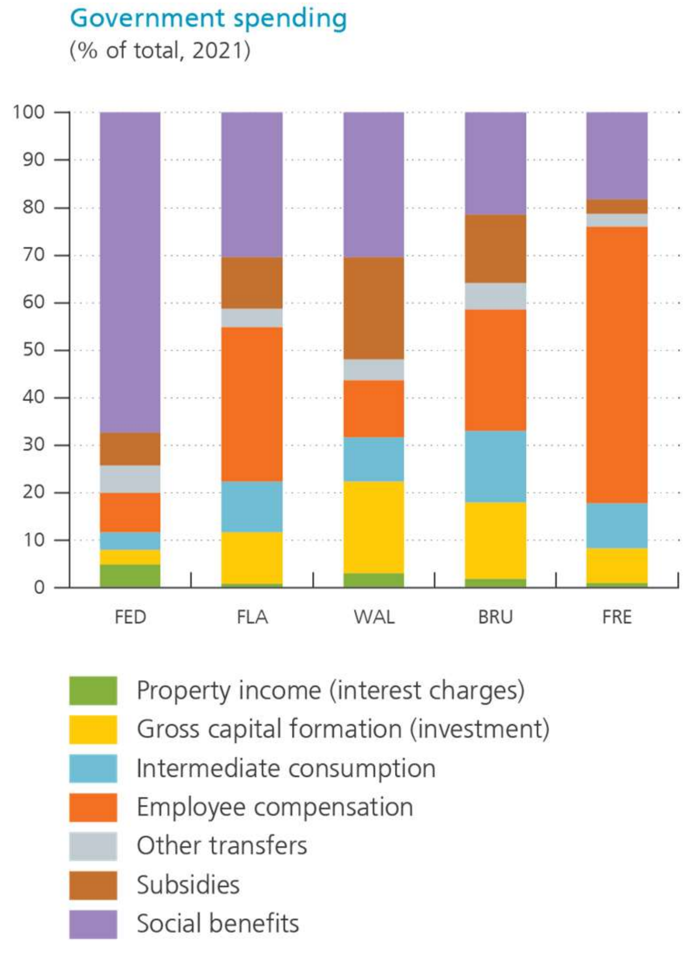
FRE: French Community

Other: (mainly) Local government

Sources: NAI, NBB.

Sources of revenue and types of spending differ between government entities





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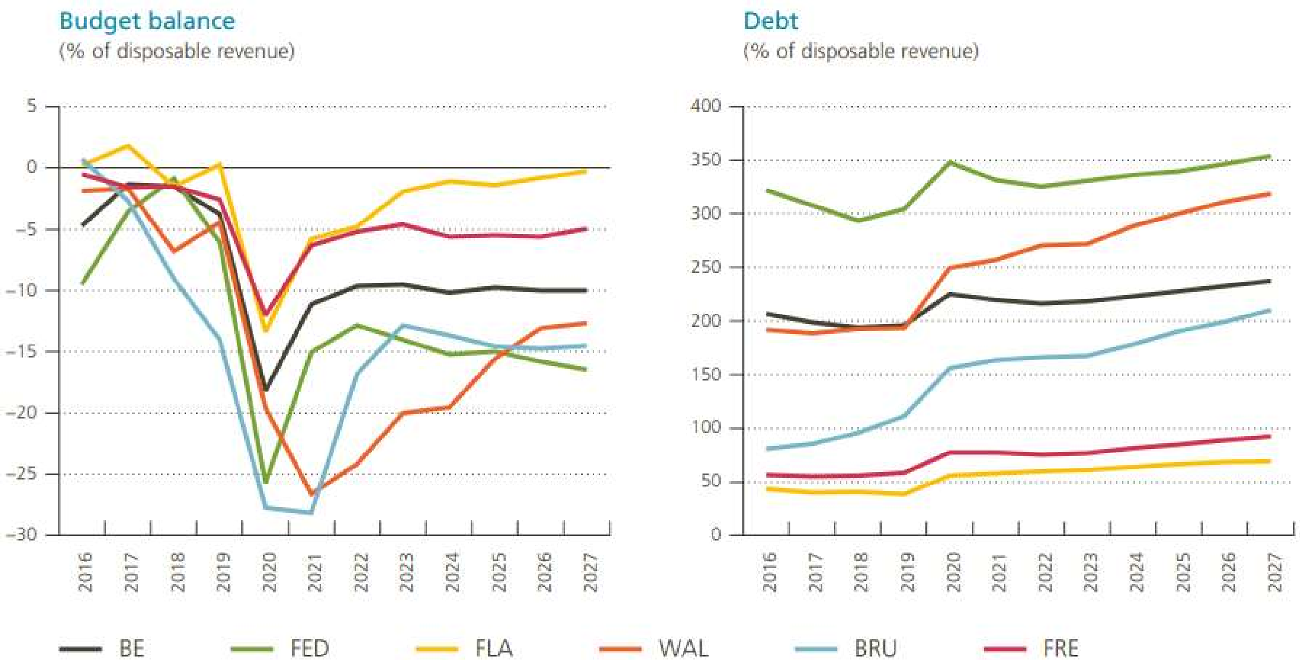
Sources: NAI, NBB.

Since the COVID-19 crisis, debt ratios have been rising but are not equally under control in all government entities



To increase comparability across entities, budget balance and debt are expressed **as a share of disposable revenue**, a proxy for their financial resources:

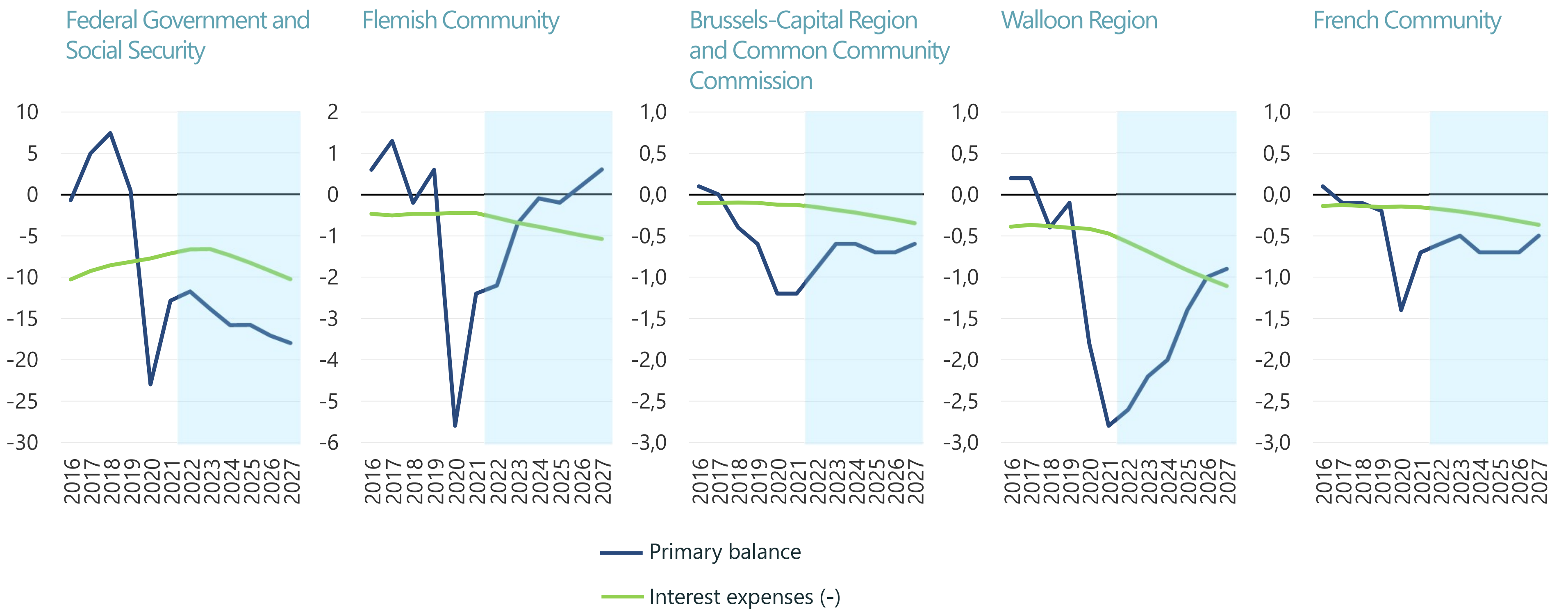
$$Disposable\ revenue_{entity} = Revenue_{entity} - Transfers\ paid\ to\ other\ entities$$

$$Revenue_{BE} = \sum_{entities} Disposable\ revenue_{entity}$$

Sources: BISA, FPB, IWEPS, Statistics Flanders, NAI, NBB.

The fiscal outlook at unchanged policy of the government entities is heterogeneous

(in € billion)



Sources: BISA, FPB, IWEPS, Statistics Flanders, NAI, NBB.

Downward trend in transfers from the federal government to federated entities

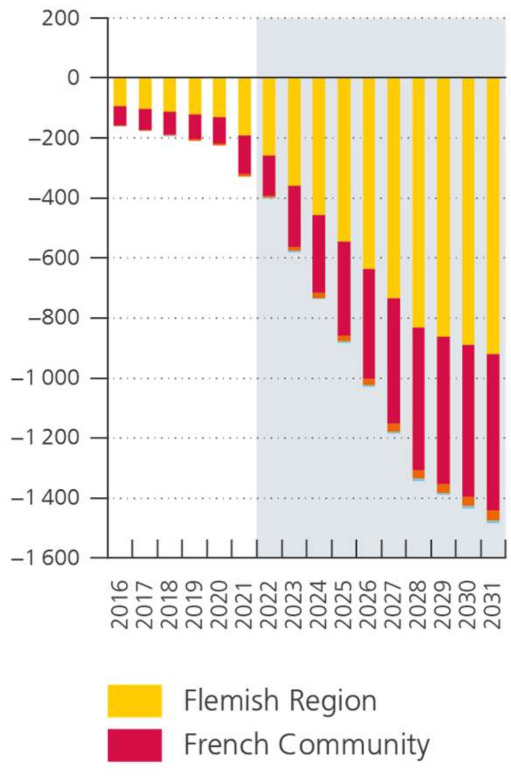
(Special Finance Act)

Incomplete linkage of transfers to GDP growth

(Grants, % of GDP)

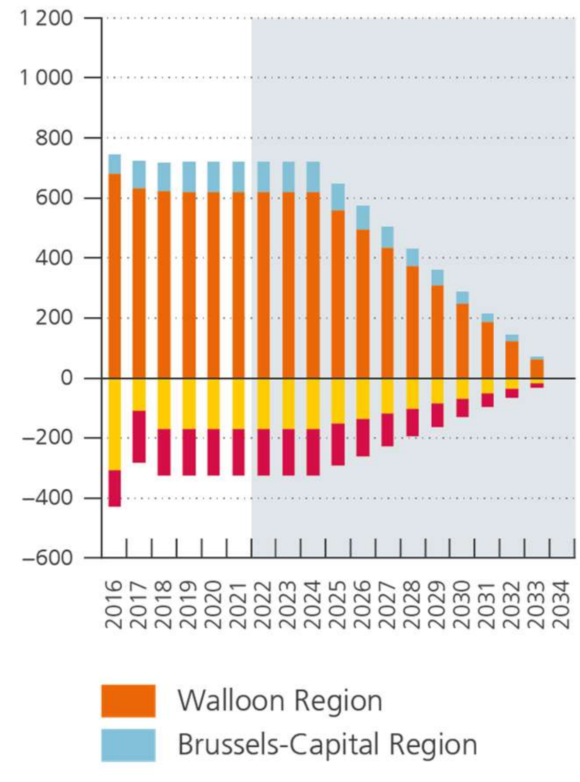
Increase of the contribution to cover pension liabilities

(in € million)



Phasing out of the transition mechanism

(in € million)



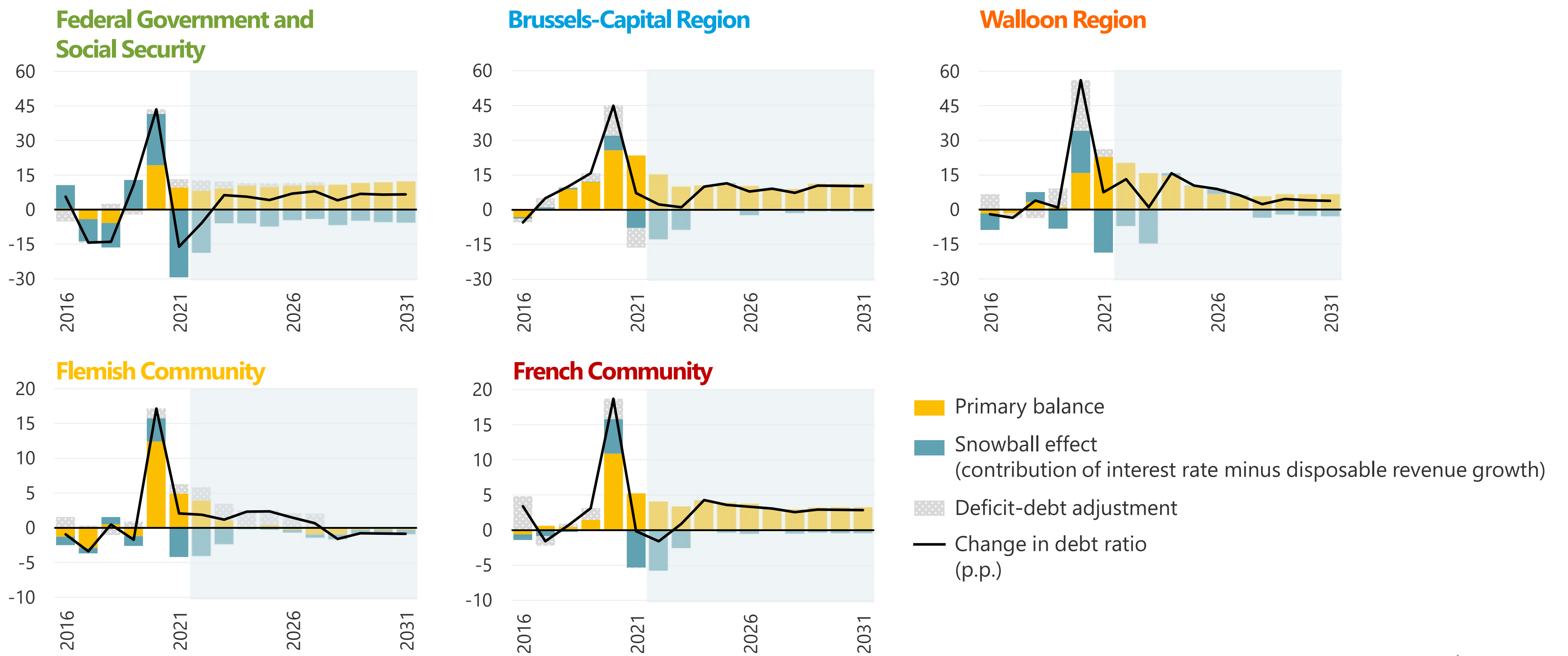
Sources: BISA, FPB, IWEPS, Statistics Flanders, NAI, NBB.

Medium term risks: assessing the sustainability of public finances under 4 alternative scenarios

	Baseline	Symmetric GDP scenario	Asymmetric GDP scenario	Interest rate scenario	Investment scenario
Belgian real GDP growth	Until 2027 projections FPB, afterwards Study Commission on Ageing	**-0.25pp from 2023**		=	Baseline nominal GDP growth + Δ inv
Regional real GDP growth	/	/	**3 subscenarios -0.25ppt from 2023**	/	/
Public investment exp.	Until 2027 projections FPB, afterwards inv-to-GDP ratio constant	=	=	=	**investment-to-GDP ratio up from 3% in 2024 to 4% in 2030**
Primary balance	Until 2027 projections FPB, afterwards pb-to-GDP ratio constant + ageing costs	+ impact Δ GDP	+ impact Δ regional GDP	=	+ impact Δ inv & Δ GDP
Interest charges	Own calculations: refinanced and new debt financed at market rates	=	=	**+250 bp from 2023**	=

Primary deficits will continue to push up debt in the baseline scenario

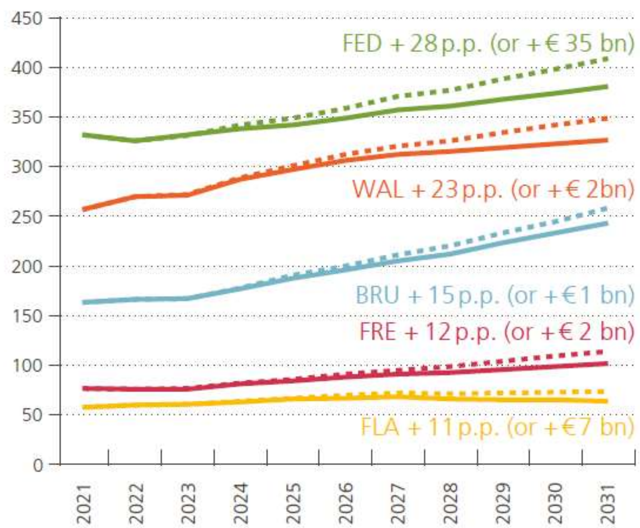
Drivers of the change in the debt ratio
(as a % of disposable revenue)



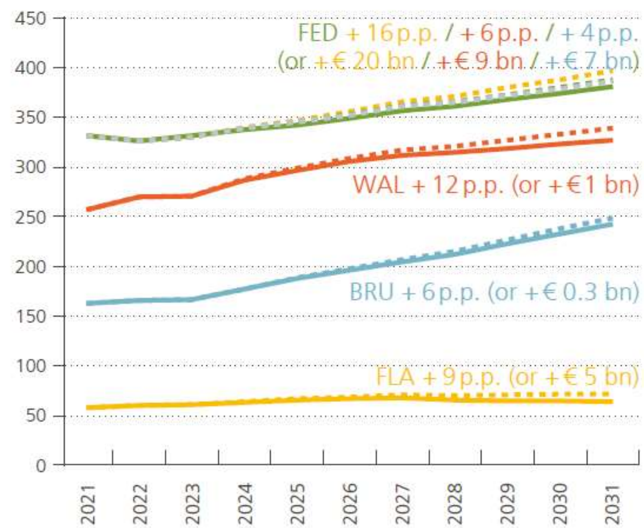
Sources: BISA, FPB, IWEPS, Statistics Flanders, NAI, NBB.

An adverse national GDP shock worsens all debt paths significantly, while the impact of an adverse regional GDP shock is cushioned[1,2]

Symmetric GDP shock
(government debt as a % of disposable revenue)



Asymmetric GDP shock
(government debt as a % of disposable revenue)



Baseline ▪▪▪▪ Scenario

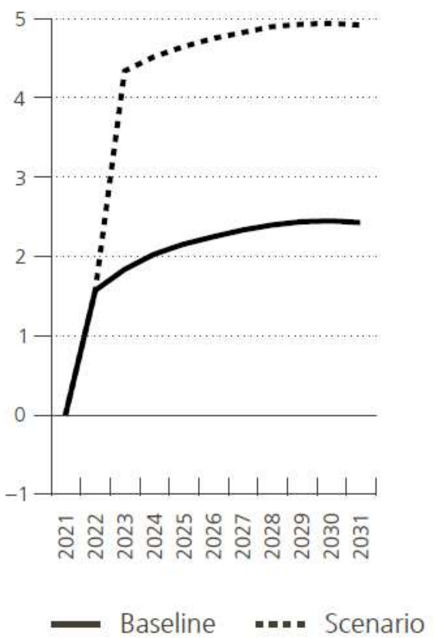
Source: NBB.

[1] The baseline scenario reflects the Federal Planning Bureau's 2022-2027 macroeconomic and fiscal projections, except for government interest payments which were calculated based on the implicit interest rates on debt and the market interest rates on Belgian government bonds over May 2022. Beyond 2027, macroeconomic projections were taken from the Study Committee on Ageing's 2022 Report. The primary balance-to-national GDP ratio was kept constant as from 2028, to which the cost impact of population ageing (as projected by the Study Committee on Ageing) was added. Stock-flow-adjustments were set to zero.

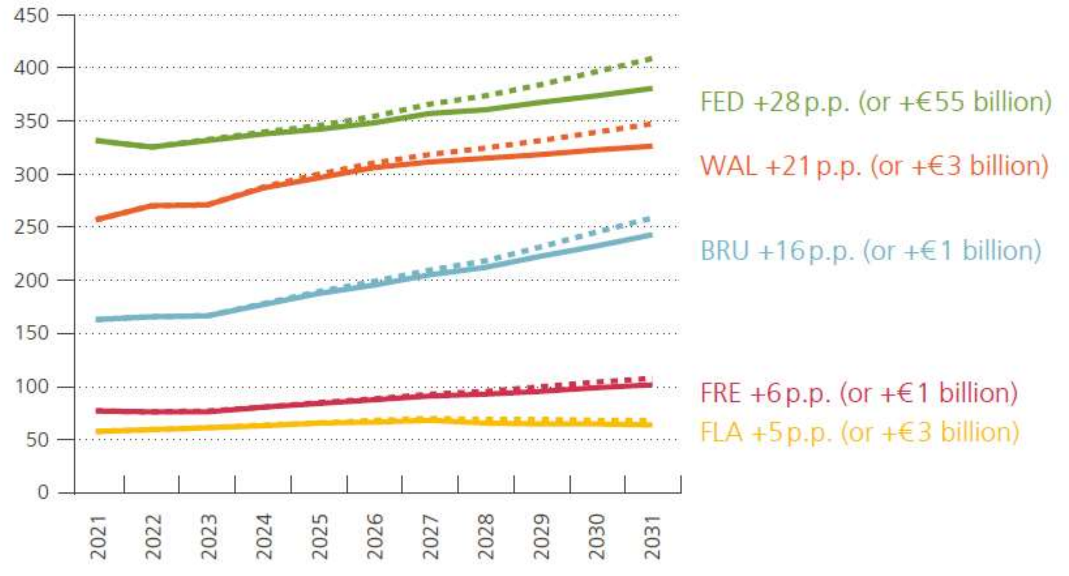
[2] The symmetric GDP shock scenario assumes that Belgian real GDP growth declines by 0.25 p.p. per year as from 2023 with the shock affecting all regions symmetrically. In contrast, the asymmetric GDP shock scenario assumes that regional real GDP growth declines by 0.25 p.p. per year as from 2023 with the shock hitting the three regions in turn. The primary balances are affected through entity-specific revenue and expenditure elasticities (GDP effect) and a related change in Special Financing Act transfers.

A continued rise in interest rates will significantly raise public debt projections for all entities[1]

250 bp increase in interest rates as from 2023
(10y Belgian OLO rate, %)



Risk premium shock
(government debt as a % of disposable revenue)



Source: NBB.

[1] The baseline scenario reflects the Federal Planning Bureau's 2022-2027 macroeconomic and fiscal projections, except for government interest payments which were calculated based on the implicit interest rates on debt and the market interest rates on Belgian government bonds over May 2022. Beyond 2027, macroeconomic projections were taken from the Study Committee on Ageing's 2022 Report. The primary balance-to-national GDP ratio was kept constant as from 2028, to which the cost impact of population ageing (as projected by the Study Committee on Ageing) was added. Stock-flow-adjustments were set to zero.

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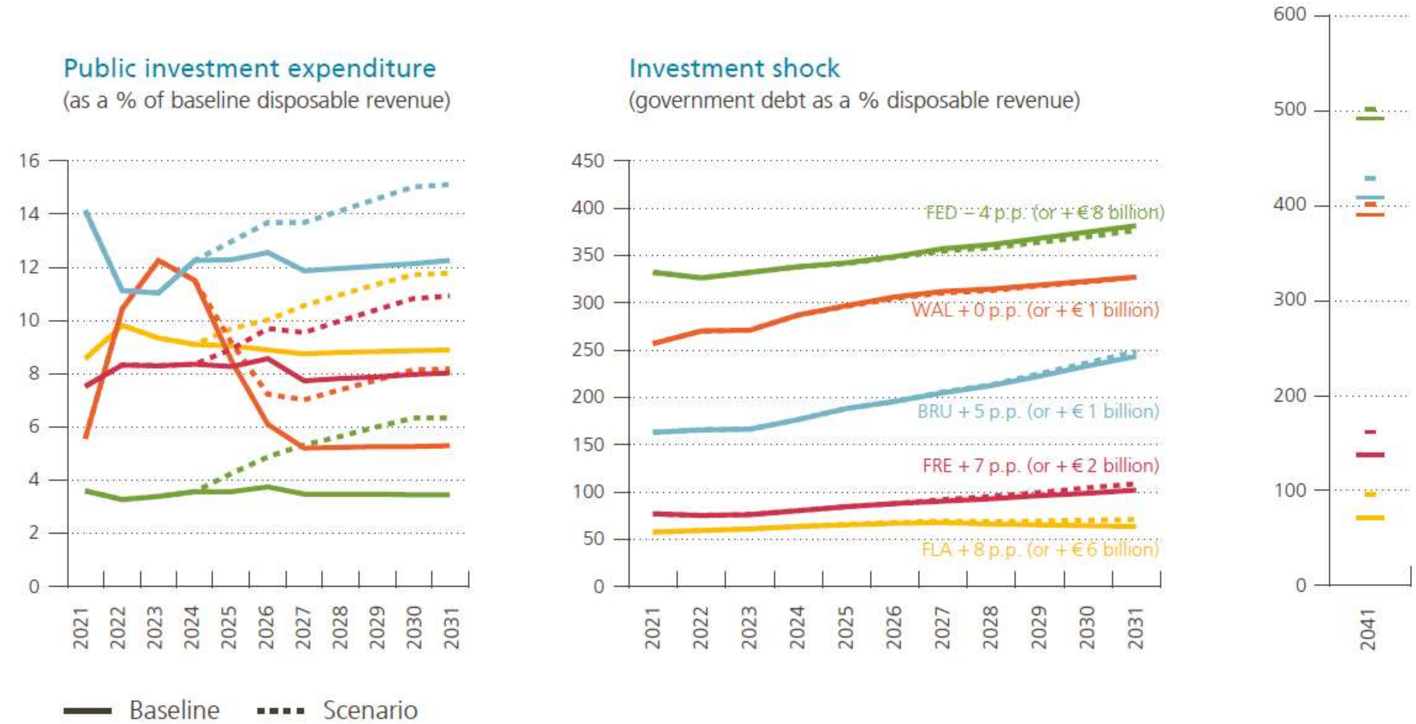
The increase in debt due to additional public investment expenditure is initially softened by the improvement in Belgian GDP[1,2]



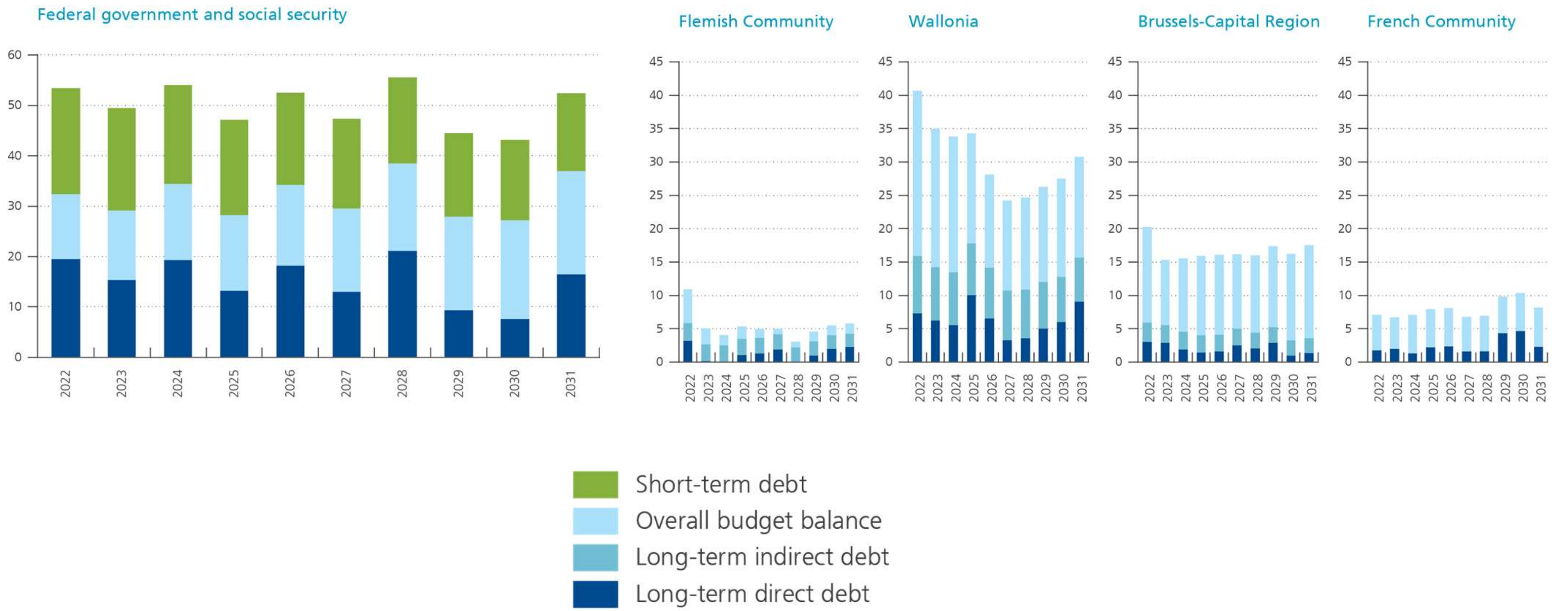
Source: NBB.

[1] The baseline scenario reflects the Federal Planning Bureau's 2022-2027 macroeconomic and fiscal projections, except for government interest payments which were calculated based on the implicit interest rates on debt and the market interest rates on Belgian government bonds over May 2022. Beyond 2027, macroeconomic projections were taken from the Study Committee on Ageing's 2022 Report. The primary balance-to-national GDP ratio was kept constant as from 2028, to which the cost impact of population ageing (as projected by the Study Committee on Ageing) was added. Stock-flow-adjustments were set to zero.

[2] The investment scenario assumes that public investment expenditure increases from 3% of GDP in 2024 to 4% in 2030. The short-and long-term investment multiplier equals one. The primary balances are affected through the increase in public investment expenditure, entity-specific revenue and expenditure elasticities (GDP effect) and a related change in Special Financing Act transfers.

Short term risks: gross financing needs differ across government entities

(as a % of disposable revenue)



Sources: Belgian Debt Agency, Regional administrations and NBB.

Except for the Flemish Region, the debt ratings of the regions and communities in Belgium are less favourable than those of the federal government

Long-term rating

(based on latest available evolution for each sub-sector)

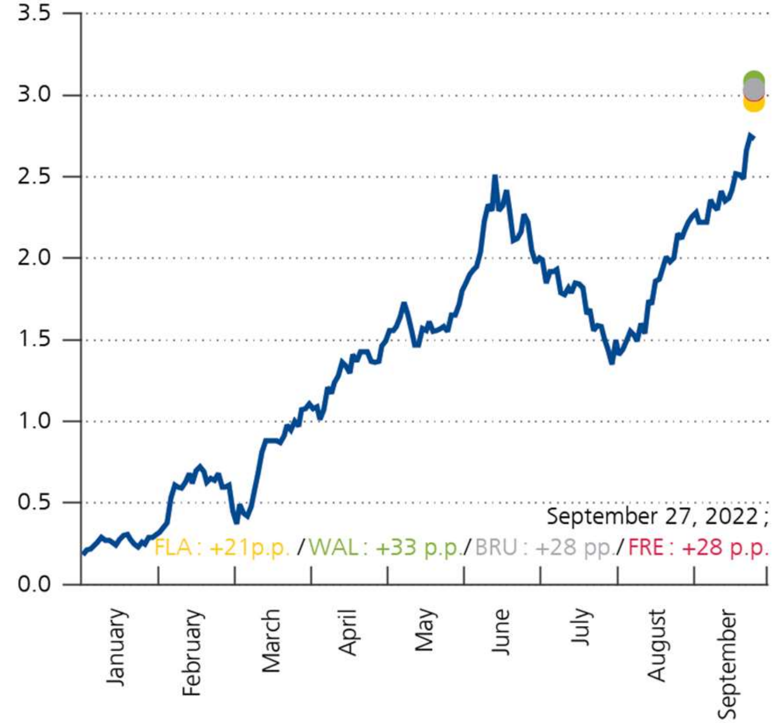
Standard & Poors		Moody's		Fitch Ratings		
Long-term	Short-term	Long-term	Short-term	Long-term	Short-term	
AAA	A–1+	AAA	P–1	AAA	F1+	Optimal security
AA+		AA1		AA+		Good quality at lower average quality
AA		AA2		AA		
AA–		AA3		AA–		
A+	A–1	A1		A+	F1	
A		A2		A		
A–	A–2	A3	P–2	A–	F2	
BBB+		BAA1		BBB+		
BBB+	A–3	BAA2	P–3	BBB	F3	
BBB–		BAA3		BBB–		
BB+	B	BA1	NOT	BB+	B	Speculative
BB		BA2	PRIME	BB		
BB–		BA3		BB–		
B+		B1		B+		
B		B2		B		
B–		B3		B–		
CCC+	C	CAA				Extremely speculative
CCC+		CA		CCC	C	
CCC–		C				
D		/		DDD		In default
				DD		
				D		

FED FLA WAL FRE BRU

Stable perspective for all sub-sectors, except BRU (negative)

Long-term interest rate

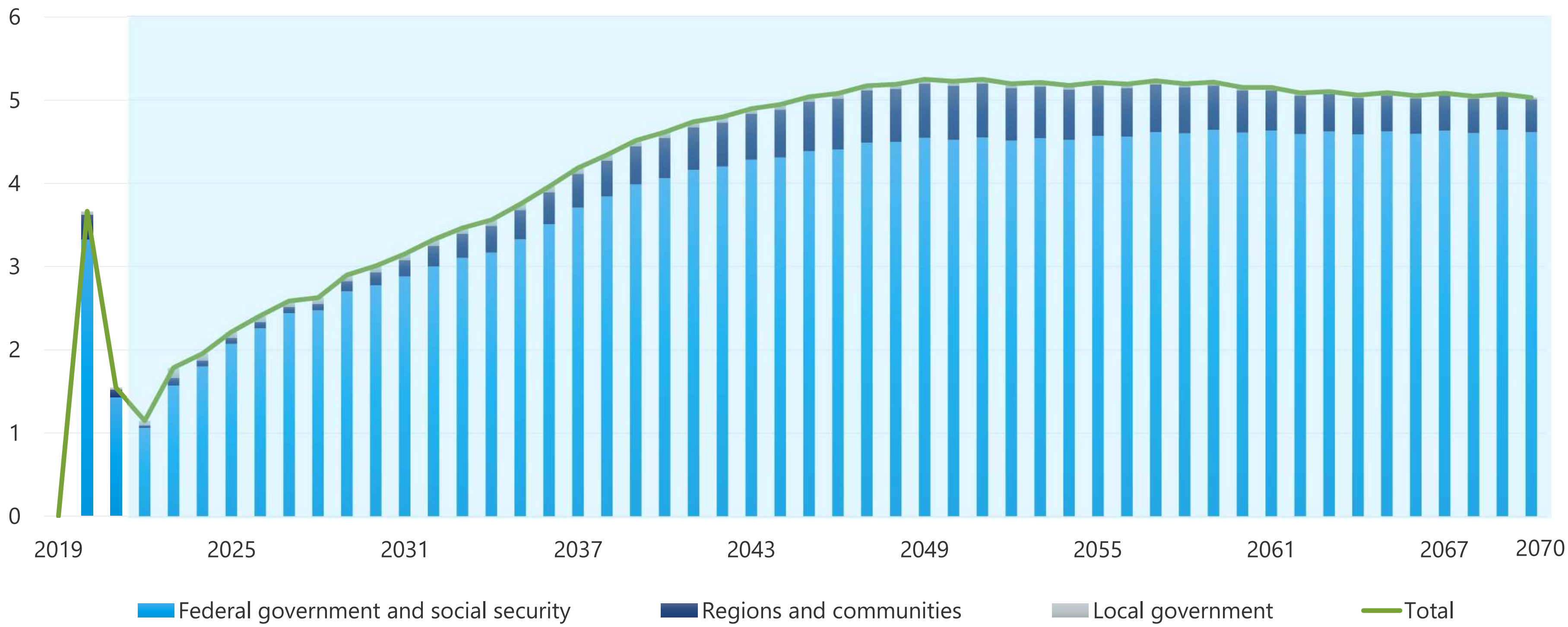
(10 year OLO and spread per sub-sectors, 2022)



Sources: Belgian Debt Agency, Regional administrations and NBB.

Long term risks: ageing costs are mainly situated at the federal level

(change in social benefits in percentage points of GDP compared to 2019)



Source: Study Committee on Ageing (SCA).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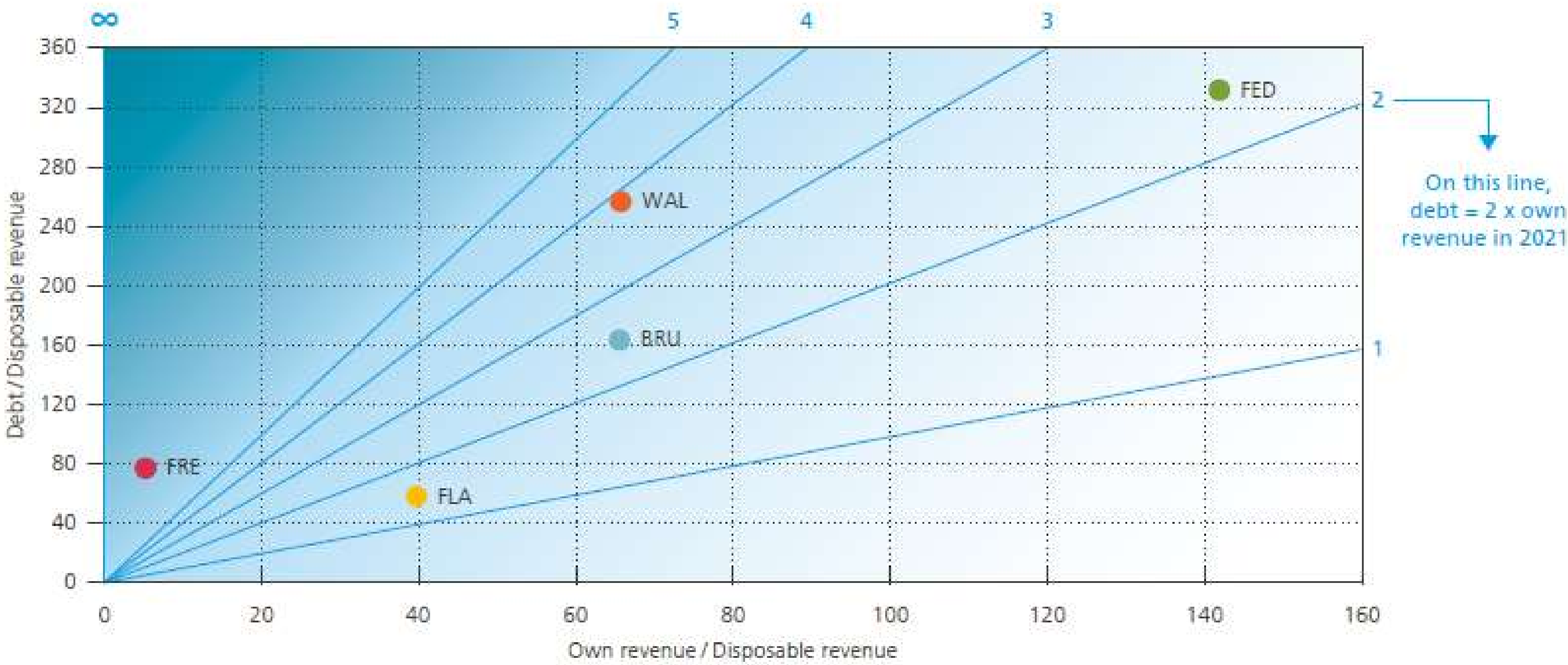
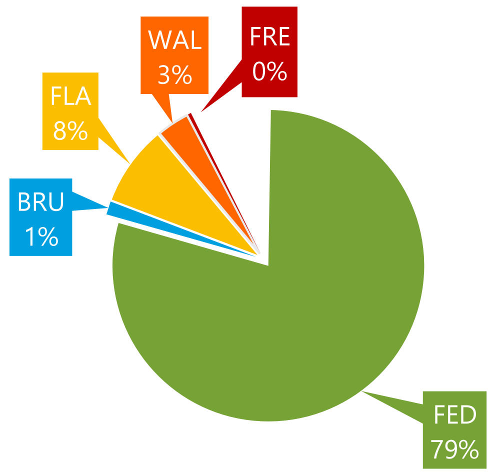
Federal government has highest debt ratio but also highest degree of revenue autonomy



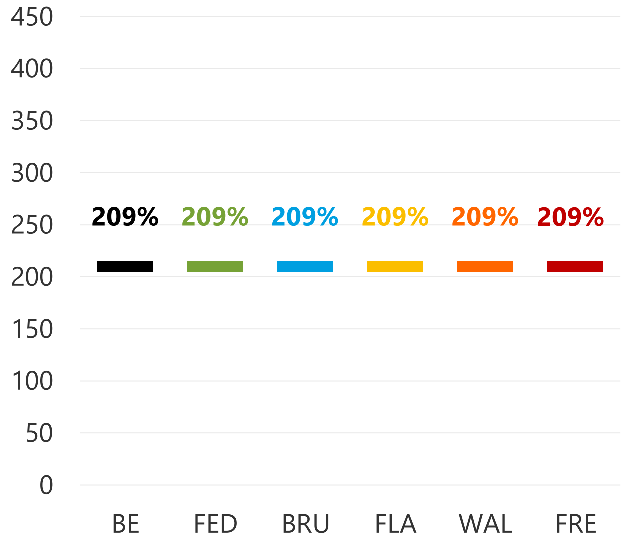
Sources: BISA, FPB, IWEPS, NAI, Statistics Flanders and NBB.
Note that "own revenue" equals total government revenue less transfers received from the government, imputed social security contributions and production for own final use.

How to distribute a 100% debt-to-GDP norm for Belgium? A possible avenue

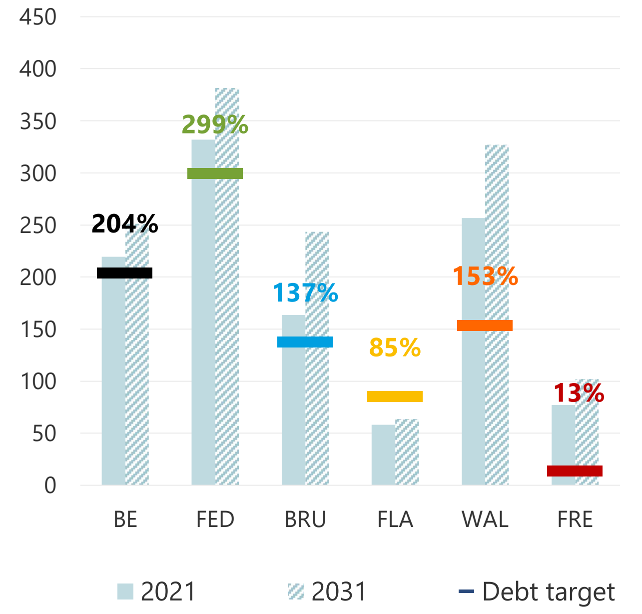
Distribution of a **100% debt-to-GDP norm for Belgium**
(distribution key: share in 2016 own revenue)



Debt norm
(in % of 2016 own revenue)

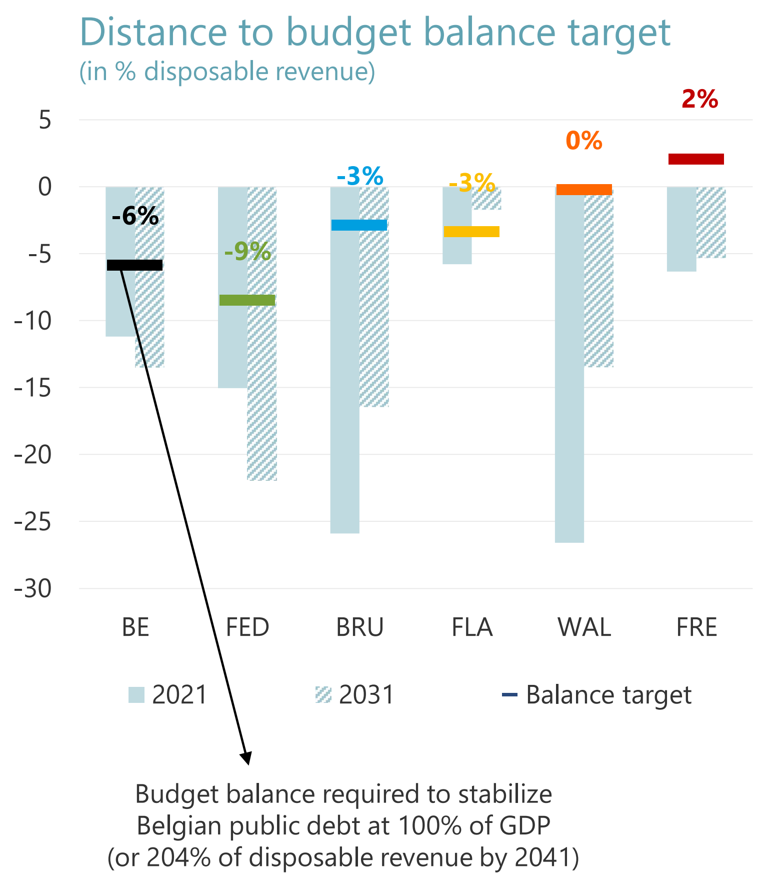


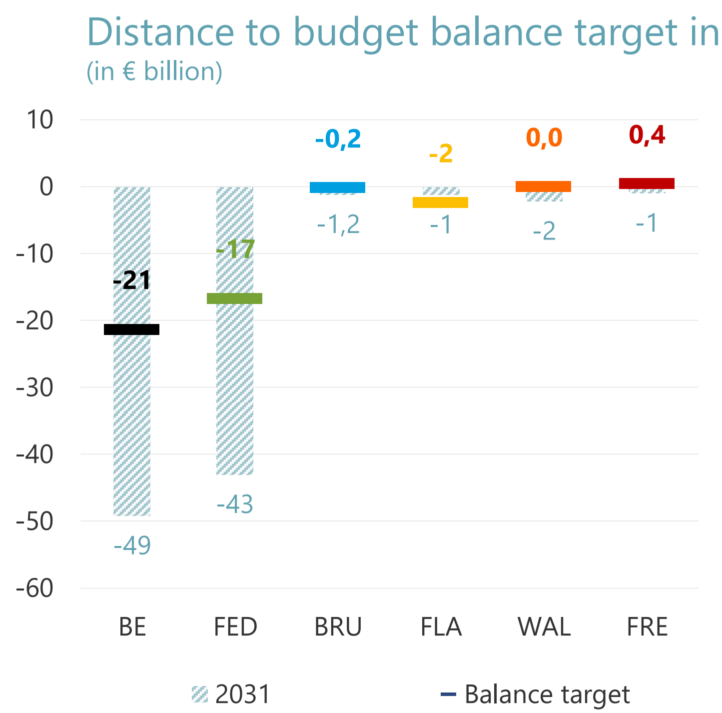
Distance to debt target
(in % of disposable revenue)



Sources: BISA, FPB, IWEPS, Statistics Flanders, NAI, NBB.

Fiscal effort required to stabilize Belgian public debt at 100% of GDP by 2041





Sources: BISA, FPB, IWEPS, Statistics Flanders, NAI, NBB.

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4. **Conclusion**

Conclusion

- Public debt has risen substantially in all government entities in recent years
- At unchanged policy, debt dynamics are not under control in the medium run, except in FLA
- Transfers from the federal government to the regions and communities are growing slower than GDP
  ⇨ regions and communities need to keep their primary expenditures in check to reduce budget deficits
- A decline in Belgian GDP growth will increase the debt ratio more in entities with higher debt levels (FED, WAL, BRU)
- A decline in regional GDP growth will have a more limited impact on regional debt ratio's due to the solidarity embedded in the Special Financing Act
- An interest rate shock will again be most damaging to those entities with the highest debt ratios (FED, WAL, BRU)
- Debt-financed public investment should be highly productive, with fiscal multipliers far above one, so as not to enhance debt sustainability risks
- Regions and communities face less favourable ratings and financing conditions than the federal government, except for FLA
- Ageing costs considerably increase the federal government's long term sustainability risks
- Substantial consolidation efforts are needed to only bring the Belgian debt ratio down to 100% of GDP

Thank you

How sustainable are public finances of the federal government and the regions and communities in Belgium?

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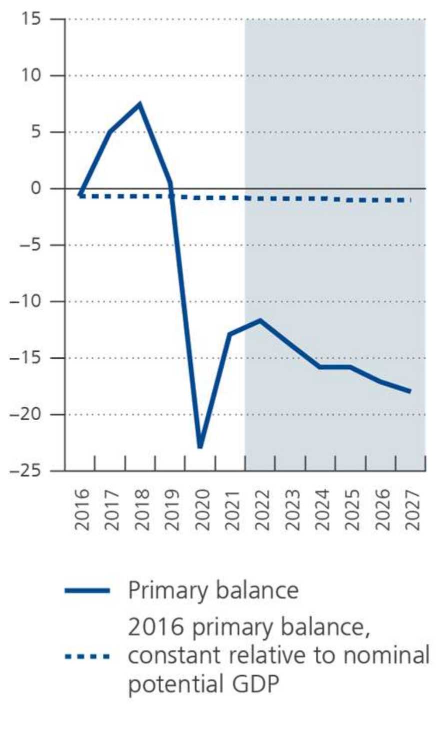
Reserveslides

Primary deficit is projected to increase primarily driven by current expenditure

FEDERAL GOVERNMENT AND SOCIAL SECURITY

Primary balance

(in € billion)



Revenue

(deviation from the trend based on nominal potential GDP since 2016, in € billion)

Primary expenditure

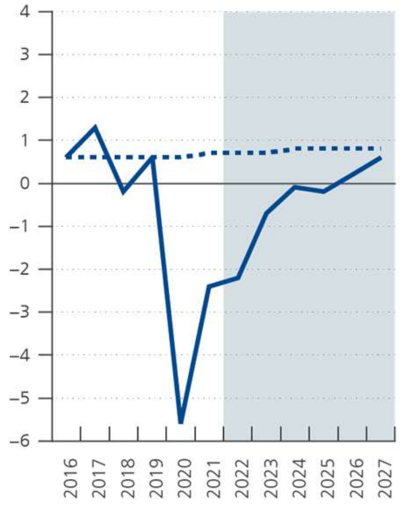
(deviation from the trend based on nominal potential GDP since 2016, in € billion)

Sources: BISA, FPB, IWEPS, Statistics Flanders, NAI, NBB.

Primary deficit is projected to disappear gradually under the impulse of a lower growth in primary expenditure than revenue

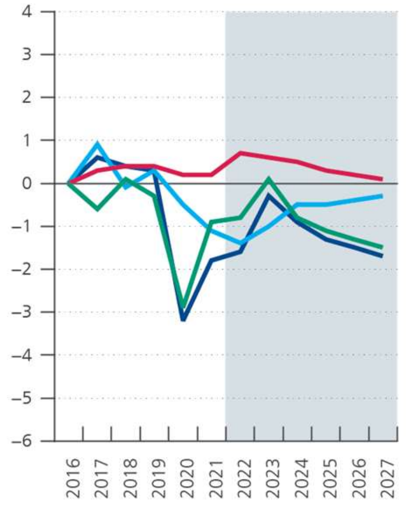
FLEMISH COMMUNITY

Primary balance
(in € billion)



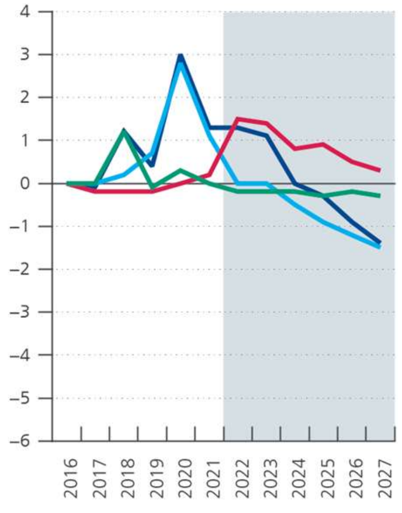
Primary balance
2016 primary balance, constant relative to nominal potential GDP

Revenue
(deviation from the trend based on nominal potential GDP since 2016, in € billion)



Total
Fiscal and parafiscal
Non-fiscal and non-parafiscal
Transfers from other public administrations

Primary expenditure
(deviation from the trend based on nominal potential GDP since 2016, in € billion)



Total
Current
Capital
Transfers to other public administrations

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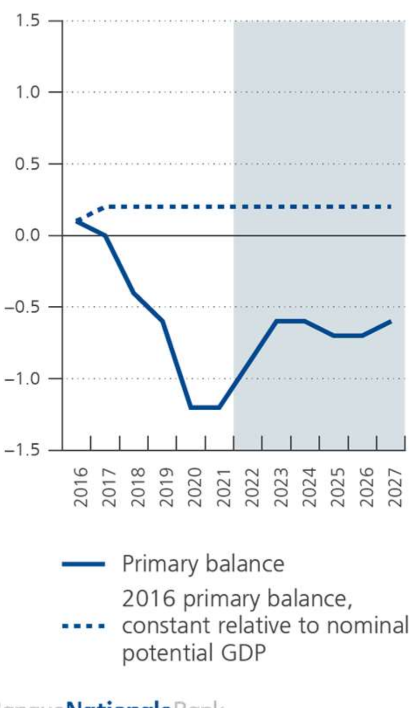
Sources: BISA, FPB, IWEPS, Statistics Flanders, NAI, NBB.

Primary deficit is projected to decrease at first, and then to stabilize as revenue and primary expenditure would expand at a similar pace

BRUSSELS CAPITAL REGION AND COMMON COMMUNITY COMMISSION

Primary balance
(in € billion)



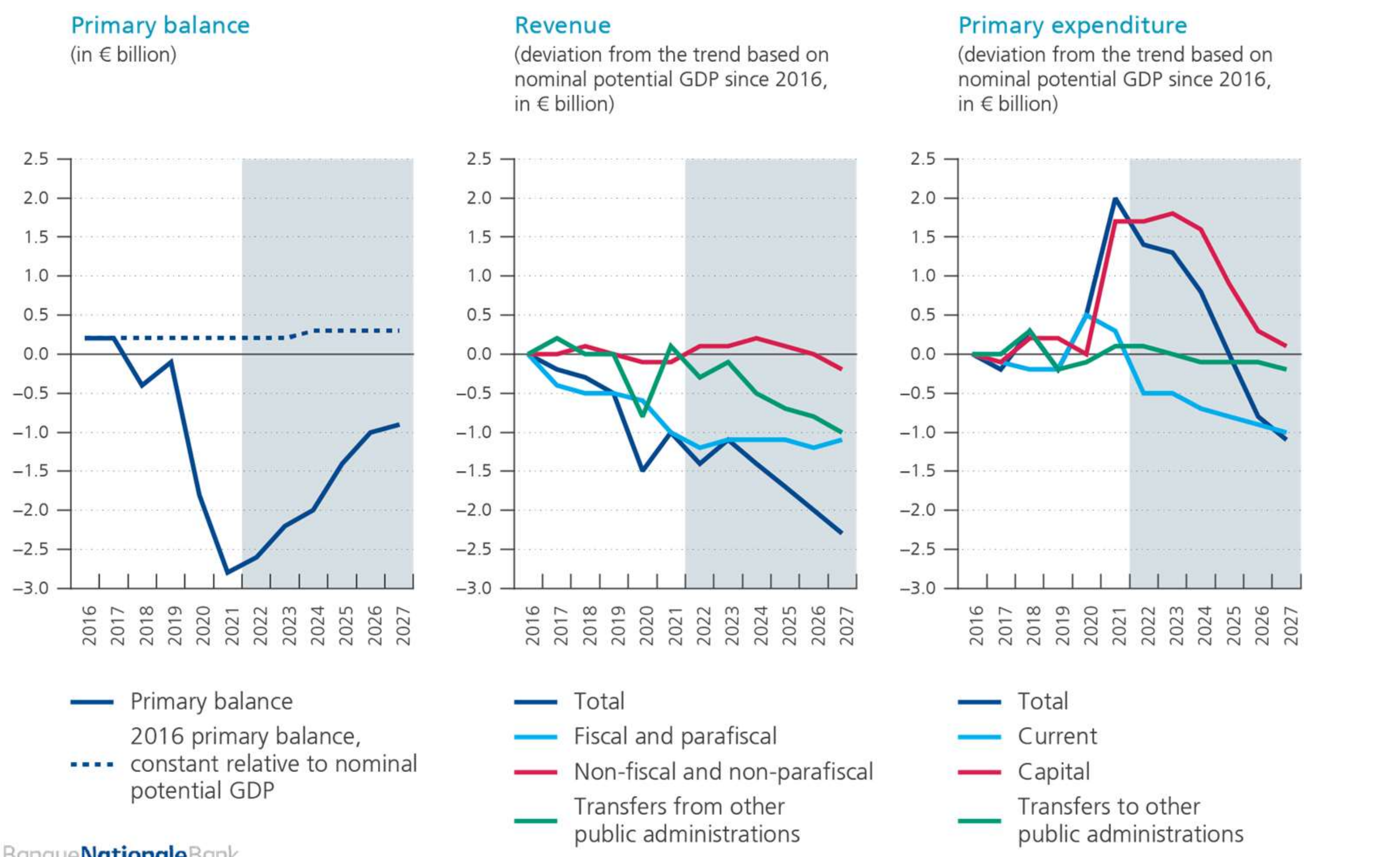
Revenue
(deviation from the trend based on nominal potential GDP since 2016, in € billion)

Primary expenditure
(deviation from the trend based on nominal potential GDP since 2016, in € billion)

Sources: BISA, FPB, IWEPS, Statistics Flanders, NAI, NBB.

Deficit reduction gradual and incomplete as revenue remains lower than primary expenditure

WALLOON REGION



Sources: BISA, FPB, IWEPS, Statistics Flanders, NAI, NBB.

A persistent deficit is expected in the coming years as revenue and primary expenditures are expected to decline at a similar pace

FRENCH COMMUNITY

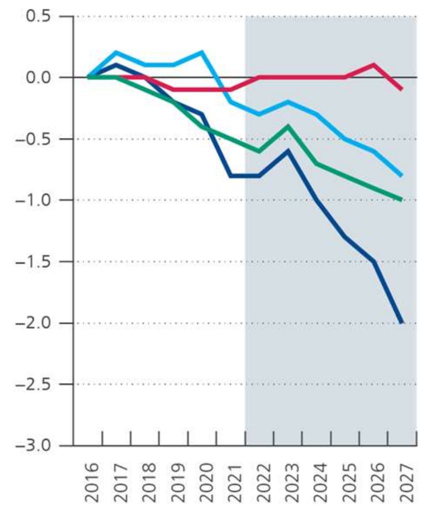
Primary balance
(in € billion)

- Primary balance
- 2016 primary balance, constant relative to nominal potential GDP

Revenue
(deviation from the trend based on nominal potential GDP since 2016, in € billion)

- Total
- Fiscal and parafiscal
- Non-fiscal and non-parafiscal
- Transfers from other public administrations

Primary expenditure
(deviation from the trend based on nominal potential GDP since 2016, in € billion)



- Total
- Current
- Capital
- Transfers to other public administrations

Sources: BISA, FPB, IWEPS, Statistics Flanders, NAI, NBB.