MOODY'S
INVESTORS SERVICE

CREDIT OPINION
16 December 2022

Update

Send Your Feedback

RATINGS

Walloon Region

Domicile	Belgium
Long Term Rating	A3
Type	LT Issuer Rating - Dom Curr
Outlook	Stable

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

Contacts

Matthieu Collette +33.1.5330.1040
VP-Senior Analyst
matthieu.collette@moodys.com

Mathilde Bonvin +33.1.5330.1036
Associate Analyst
mathilde.bonvin@moodys.com

Sebastien Hay +34.91.768.8222
Senior Vice President/Manager
sebastien.hay@moodys.com

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454

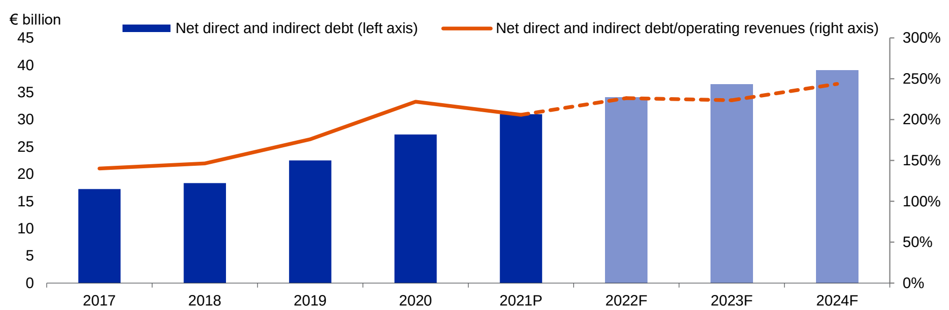
Walloon Region (Belgium)

Update to credit analysis

Summary

The credit profile of the Walloon Region (A3 stable) reflects a mature and robust legislative background, prudent but sophisticated debt management and its unquestioned market access as well as its tax autonomy. Our assessment of the Walloon Region's creditworthiness also takes into account the recurring financing deficits we expect the region to post going forward and our expectation that the region's debt burden will remain very high. The Walloon Region benefits from a high likelihood of support from the government of Belgium (Aa3 stable) if it were to face acute liquidity stress.

Exhibit 1
The Walloon region's debt and debt burden will remain permanently very high



P: Preliminary data, F: forecast
Source: Walloon Region, Moody's Investors Service

Credit strengths

» A mature and robust legislative background with well-defined responsibilities amid a complex Belgian institutional system

» Sophisticated but prudent debt management underpins unquestioned market access

» Revenue flexibility is high, and the region is committed to increasing its expenditure flexibility and to proceeding with spending cuts

Credit challenges

» The region's debt burden will remain very high on the back of recurring financing deficits

» An economy which compares unfavorably with national and European peers

Rating outlook

The stable outlook reflects our view that strong debt and liquidity management as well as strong market access and high debt affordability are consistent with an A3 rating.

Factors that could lead to an upgrade

An upgrade of the Walloon Region's rating would require consecutive years of balanced budgets or financing surplus, leading to a downward trend in the debt burden ratio towards pre-pandemic levels. An upgrade of Belgium's sovereign bond rating would also have positive implications for the region.

Factors that could lead to a downgrade

A continuation of the increase in the region's debt burden from already very high levels, due to a failure to implement savings and/ or to a less supportive economic growth than currently expected, would weigh on the ratings. A material increase in the region's interest burden and/ or a material weakening in its market access would also be credit negative. A downgrade of Belgium's sovereign bond rating would have negative implications for the Walloon Region as well.

Key indicators

The Walloon Region

	2017	2018	2019	2020	2021P	2022F	2023F	2024F
Walloon Region								
Gross operating balance / operating revenues (%)	-4.0	-2.9	-6.0	-23.0	-12.3	-7.3	-11.3	-8.4
Interest expenses / operating revenues (%)	2.2	2.3	2.1	2.3	2.2	2.1	2.0	2.4
Capital spending / total expenditure (%)	2.6	2.4	2.6	1.6	4.8	8.0	6.0	10.4
Financing surplus (requirement) / of total revenues (%)	-6.7	-5.5	-8.9	-24.9	-18.0	-14.9	-14.1	-17.9
Direct debt / operating revenues (%)	75.9	89.8	98.9	134.1	130.4	145.3	149.3	169.9
Net Direct and Indirect debt / operating revenues (%)	140.2	146.4	176.0	222.0	205.9	226.3	223.7	243.7

P: Preliminary data, F: forecast
Source: Walloon Region, Moody's Investors Service

Detailed credit considerations

The credit profile of the Walloon Region, as expressed in its A3 rating, combines a Baseline Credit Assessment (BCA) of baa2 and the high likelihood of extraordinary support from the federal government if the entity were to face acute liquidity stress.

Baseline Credit Assessment

A mature and robust legislative background with well-defined responsibilities amid a complex Belgian institutional system

The country's federal structure of government has gradually, but significantly, evolved over the past decades towards a greater devolution of decision-making power to the six federated entities – one of which is the Walloon Region. This has included greater tax autonomy for regions, with the implementation in 2015 of the Sixth State Reform. The determining characteristic of a region is its geographical area, while that of a community is its culture and language. The Walloon Region represents 55% of the Belgian territory but 32% of its population. The communities cut across the regions and the French Community (CFB, A2 stable) comprises all the residents of the Walloon Region and Brussels-based French-speaking inhabitants (approximately 4.2 million inhabitants).

While the country's regional disparities and divisions are associated with governance complexities at the federal level, the legislative background – which encompasses the arrangements determining intergovernmental relations at all levels, as well as jurisdictional powers and responsibilities – is mature and robust. Exclusive responsibilities assigned to the federated entities are stable, and regions are competent in territorial matters (including economic development, transports, environment, housing) as well as employment. The remaining responsibilities are assigned to the federal government (including foreign affairs, national defence and justice). The distribution of responsibilities is subject to judicial control, exercised by the Constitutional Court of Belgium (which can undo legislation that contravenes the division of powers), and by the Council of State. For the Walloon Region, it also means that revenues and spending responsibilities are well-defined, that tax autonomy is ensured and that changes could not occur suddenly. Any change to the legislation that governs Belgian sub-sovereigns must be approved by a majority in both linguistic groups (French and Dutch/German) in the national Parliament, in addition to a two-thirds overall majority.

Sophisticated but prudent debt management underpins unquestioned market access

As one of the federated regions and communities in Belgium, the region has always benefitted from a very strong access to diversified funding sources. The region implemented a debt agency in order to optimize its funding and cash management. Debt management is based on prudent rules, including: (i) debt due within one and five year(s) must remain below 15% and 50% of total outstanding debt, respectively; (ii) the target share of variable-rate debt is 15%; (iii) there is no exposure to foreign currency risk; (iv) the use of swaps is non-speculative (the region always holds an underlying asset – outstanding commercial paper is therefore considered as long-term debt based on the maturity of the associated swaps). We note that over the past few years the region took over the debt of several satellite organizations (*Unités d'Administration Publique*) in order to minimize their funding costs and achieve greater transparency. The region also now centralizes its satellites organizations' cash and cash management. It results, for the region, in a confortable cash buffer: as of 30 November 2022, the average 2022 cash position was €4.8 billion. The region starts December 2022 with a very comfortable €5.6 billion liquidity position, covering 5.0 times debt servicing and 2.3 times the likely financing deficit for 2023.

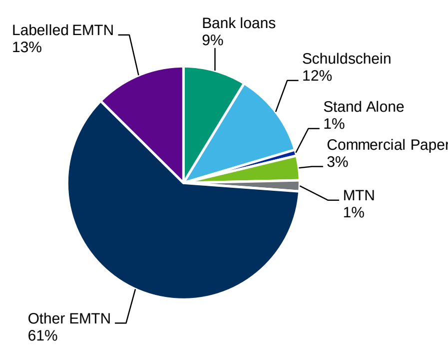
The region also benefits from very strong access to external liquidity. Funding instruments comprise: (i) a €20 billion EMTN (Euro Medium Term Note) programme; (ii) MTN (Medium Term Note) programmes, which can be used for short- (*billets de trésorerie*) and long-term maturities (€1.25 billion with BNP Paribas Fortis SA/NV [A1/A2 stable]; and €2.5 billion with Belfius Bank SA/NV [Belfius, A1/A1 stable]); and (iii) a €3 billion overdraft cash facility to date – including a firm commitment underwriting agreement – with Belfius. In addition, in 2021, the region signed a financing agreement with the European Investment Bank (EIB, Aaa stable) for a total of €1.1 billion to fund social housing energy efficiency works and flood resilience projects.

In 2021 and 2022, the Walloon Region issued two benchmark bonds of €2.2 billion and €1 billion, respectively, as part of the region's strategy since 2019 to regularly issue debt in a benchmark format in order to build a yield curve and increase its investor base. The 2022 benchmark issuance attracted an order book at 1.4 times its issuance size, demonstrating the region's robust market access, in spite of the rising interest rates and the European Central Bank (ECB)'s exit from its monetary policy support programmes. This issuance was part of the region's strategy to cover all of its 2022 and part of 2023 funding needs. In 2022, the region overall issued €1.1 billion new debt with an average maturity of 10.8 years and an average spread against OLO of 34.3 bps (compared to 30.5 bps in 2021).

Exhibit 3

The region's debt is well diversified

As a % of direct debt (excluding bank overdraft) as of 30/06/2022



EMTN: Euro Medium Term Notes

Source: Walloon Region, Moody's Investors Service

Revenue flexibility is high, and the region is committed to increasing its expenditure flexibility and to proceeding with spending cuts

The Walloon Region benefits from a high degree of tax autonomy. The region has rate-setting powers on regional taxes (approximately 15% of total revenues). In addition, since the implementation of the Sixth State Reform in 2015, the region benefits from increased flexibility to modify a regional surcharge rate on personal income tax (PIT). This flexibility is limited, however, given that regional PIT proceeds are derived by applying the surcharge rate to federal PIT proceeds – the region has no control over marginal tax rates and brackets, which are both set at the federal level. While there is currently no plan for the Walloon Region to use this flexibility, it better positions the region to mitigate any budget shortfall by raising taxes. Without accounting for potential behavioral effects, a 0.1 percentage point increase in the regional surcharge rate (to 33.357% from 33.257%) would have resulted in close to €10.5 million in additional revenues in 2022. We also note that the region is working on optimizing its tax proceeds, including through an upcoming move towards a greater level of regional collection of taxes which are currently collected by the federal government and then redistributed to the region.

With the 2022 budget, and in line with the spending reviews and "zero-based budgeting" (ZBB) the region has been processing since 2020, the Walloon's government has committed to achieve a so-called "sustainability effort" amounting at least €150 million each year from 2022 onwards over the coming 10 years, so to be able to stabilize its debt-to-revenue ratio over a reasonable time horizon. In 2022, we expect the region to post savings totaling €250 million (or 1.3% of 2022 estimated total spending), mainly through spending cuts but also thanks to more tax revenues. Based on the region's spending reviews that pointed out flexibility on spending totaling €900 million (or 4.5% of 2022 estimated total spending), we still see the €150 million objective as realistic, while it will not be enough to prevent the region's debt burden from further increasing. We will therefore continue to monitor the developments surrounding expenditure management, including the effective implementation of the region's "sustainability plan" as well as the use of the flexibility highlighted with the spending review process.

The region's debt burden will remain very high on the back of recurring financing deficits

At the end of 2022, we expect the Walloon Region's net direct and indirect debt (NDID) to reach €34.1 billion and thus to represent a very high 226% of operating revenues (or 223% of total revenues). According to our forecasts, the region will post average financing deficits of around €2.5 billion each year over 2022-24, against €1 billion in 2019. As a result, the NDID will further increase to around €40 billion, pushing the debt burden, as measured by the NDID-to-operating revenues ratio, around 245% by the end of 2024, which is the end of the current political mandate.

Even if revenues move with and will continue to be supported by nominal gross domestic product (GDP) growth in the two to three coming years - tax revenues move with nominal GDP growth which we expect to remain positive, also providing a natural hedge against price inflation - the region's recurring financing deficits are mainly driven by large spending from the region's recovery plan launched post-coronavirus pandemic. The Walloon Recovery Plan (WRP) has been designed to represent €4.7 billion of capital expenditure over 2022-2024 and also results from the combination with pre-pandemic commitments announced in the 2019 Regional Policy Statement[1]. Out of the WRP, only 30% (€1.5 billion) will benefit from budget neutral funding from the European Union (EU)'s Recovery and Resilience Facility (RRF). The remainder would have to be financed through new debt while the region is focused on delivering first the EU-funded projects - as of mid-2022, about three quarter of EU-funded projects have been initiated.

While the boost in public investment from the WRP should generate medium-to-long-term economic, social and environmental benefits, its large size explains, in our view, why the revenue growth in the two to three coming years and the government's "sustainability plan" (see *"Revenue flexibility is high, and the region is committed to increasing its expenditure flexibility and to proceeding with spending cuts"*) will not be enough to reverse the growing debt trajectory. We therefore expect the Walloon Region's debt burden to remain continue to grow at least in the two to three coming years and stabilizing the debt burden over a reasonable time horizon as the Walloon's government is committed to is a key challenge. We will thus continue to monitor the effective implementation of the WRP - including potential under-execution of CAPEX not funded by the EU - and the resulting new borrowing needs.

At the same time, we currently expect the impact of the ECB's exit from its expansive monetary policy and the resulting increasing interest rates to have a limited impact on the Walloon Region's debt affordability - we expect the region's debt burden to remain below 2.5% of operating revenues by the end of 2024.

The region's economy compares unfavorably with national and European peers

The region's economic fundamentals compare unfavorably with national peers levels. Regional gross domestic product (GDP) per capita in 2019 and 2020 represented 73% and 66% of the national average, respectively. In addition, socio-economic indicators, including disposable income per capita, labor participation and unemployment rates, are structurally weaker than peers. In 2021, the regional unemployment rate reached 8.9%, compared with national and EU rates of 6.3% and 7.1%, respectively.

However, the Walloon economy is diversified, with the proportion of the workforce employed in services, industry and agriculture aligned with national levels. The high share of public employment compared with the Belgian average can also be viewed as a strength when the economy faces a shock, like the coronavirus-induced recession in 2020 – it acts as a macroeconomic stabilizer, which shields the regional economy from strong (both upwards and downwards) fluctuations.

Extraordinary support considerations

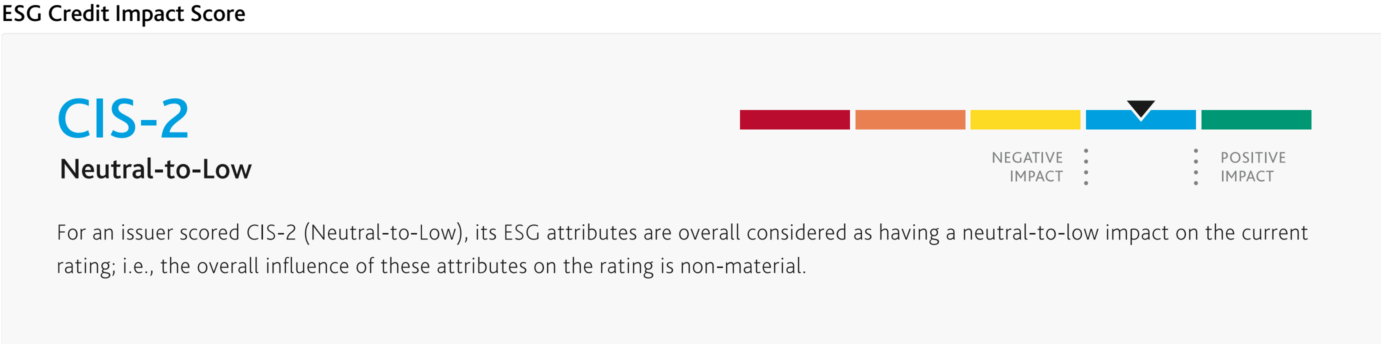
We assign a high likelihood of extraordinary support from the national government, reflecting: (i) our assessment of the reputational risk for the federal government if the Walloon Region were to default; and (ii) indications of support stemming from the federal government's commitment to enabling federated entities to reach sound financials, including Articles 49 and 54 of the 1989 Financial Law – the latter states that regions and communities are entitled to offset insufficient or untimely receipts from the federal government with a guaranteed loan.

ESG considerations

Walloon Region's ESG Credit Impact Score is Neutral-to-Low CIS-2

Exhibit 4

ESG Credit Impact Score



Source: Moody's Investors Service

The Walloon Region' ESG Credit Impact Score is neutral to low (**CIS-2**), driven by moderately negative social risks while governance considerations are neutral and exposure to environmental risks is low.

Exhibit 5

ESG Issuer Profile Scores

Source: Moody's Investors Service

Environmental

The Walloon Region's exposure to environmental risks is generally low. Its overall E issuer profile score is therefore neutral to low (**E-2**).

Social

The Walloon Region faces moderate risks from exposure to social risks (**S-3**). Like Belgium, the Walloon Region faces long-term economic and fiscal pressures from demographic change, marked by a shrinking working age population and a rising dependency ratio. Labor & income, including low participation rates to the labor force, also weigh on the region's social profile. At the same time, Wallonia benefits from widely available high-quality education, good housing availability, high quality healthcare and basic services.

Governance

The influence of governance on Walloon Region's credit profile is neutral to low (**G-2**). The region's financial management is strong as illustrated by prudent but sophisticated debt management. At the same time, the region's track record of unbalanced budget when economic growth was supportive weighs on its G profile.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click here to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

Rating methodology and scorecard factors

The assigned BCA of baa2 is close to the scorecard-indicated BCA. The one-notch difference captures the very high debt ratios relative to peers. The matrix-generated BCA of baa1 reflects an Idiosyncratic Risk score of 5 (presented below) on a 1 to 9 scale, where 1 is the strongest relative credit quality and 9 the weakest; and (2) a Systemic Risk score of Aa3, as reflected by Belgium's Aa3 stable sovereign bond rating.

Exhibit 6

Walloon Region Scorecard 2020

Regional & Local Governments

Baseline Credit Assessment – Scorecard	Score	Value	Sub-factor Weighting	Sub-factor Total	Factor Weighting	Total
Factor 1: Economic Fundamentals				**6.60**	**20%**	**1.32**
Economic Strength [1]	9	69.13%	70%			
Economic Volatility	1		30%			
Factor 2: Institutional Framework				**3**	**20%**	**0.60**
Legislative Background	1		50%			
Financial Flexibility	5		50%			
Factor 3: Financial Position				**4.75**	**30%**	**1.43**
Operating Margin [2]	9	-15.29%	12.5%			
Interest Burden [3]	3	2.25%	12.5%			
Liquidity	1		25%			
Debt Burden [4]	9	222.02%	25%			
Debt Structure [5]	3	10.15%	25%			
Factor 4: Governance and Management				**5**	**30%**	**1.50**
Risk Controls and Financial Management	5					
Investment and Debt Management	1					
Transparency and Disclosure	1					
Idiosyncratic Risk Assessment						**4.85 (5)**
Systemic Risk Assessment						**Aa3**
Scorecard-Indicated BCA Outcome						**baa1**
Assigned BCA						**baa2**

[1] Local GDP per capita as % of national GDP per capita
[2] Gross operating balance/operating revenues
[3] Interest payments/operating revenues
[4] Net direct and indirect debt/operating revenues
[5] Short-term direct debt/total direct debt
Source: Moody's Investors Service; Fiscal 2020.

Ratings

Exhibit 7

Category	Moody's Rating
WALLOON REGION	
Outlook	Stable
Issuer Rating -Dom Curr	A3
Senior Unsecured -Dom Curr	A3
Other Short Term -Dom Curr	(P)P-2

Source: Moody's Investors Service

Endnotes

1 Pre-pandemic and new measures are included in the “Walloon Transition Plan” and “Get up Wallonia”

REPORT NUMBER 1342078

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454

Moody's
INVESTORS SERVICE