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CREDIT OPINION
12 December 2023

Update

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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.

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Walloon Region (Belgium)

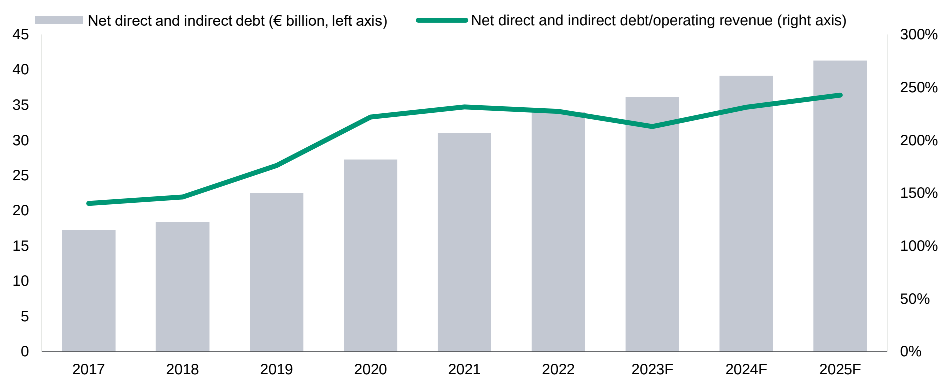
Update to credit analysis

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



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 supportive of the region's credit profile

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

Exhibit 2
The Walloon Region

Walloon Region	2018	2019	2020	2021	2022	2023F	2024F	2025F
Gross operating balance / operating revenues (%)	-2.94	-6.05	-23.00	-24.09	-14.56	-12.44	-9.92	-5.51
Interest expenses / operating revenues (%)	2.26	2.13	2.30	2.48	2.11	2.09	2.56	2.86
Capital spending / total expenditure (%)	2.40	2.59	1.57	4.88	3.88	4.13	6.29	6.01
Financing surplus (requirement) / of total revenues (%)	-5.50	-8.86	-24.92	-30.38	-19.14	-14.95	-14.28	-9.38
Direct debt / operating revenues (%)	89.80	98.87	134.06	146.61	148.05	145.86	160.91	169.65
Net Direct and Indirect debt / operating revenues (%)	146.40	175.99	222.02	231.37	227.24	213.04	231.31	242.65

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.

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. Funding instruments comprise: (i) a €25 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 positive]); and (iii) a €3 billion overdraft cash facility to date – including a firm commitment underwriting agreement – with Belfius. In addition, the region signed a financing agreement with the European Investment Bank (EIB, Aaa stable) in 2021 for a total of €1.1 billion to fund social housing energy efficiency works and flood resilience projects.

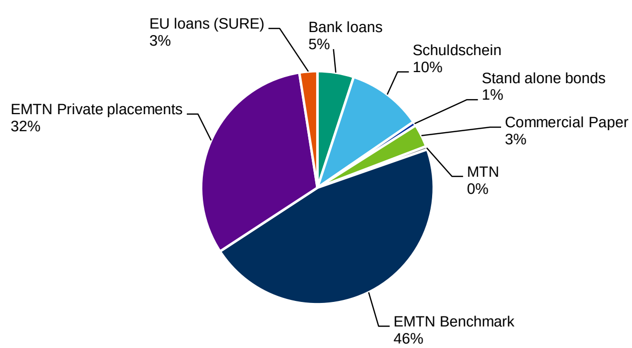
Debt management is based on prudent rules, including: (i) debt due within one and five year(s) must remain below 15% and 50% of total outstanding debt, respectively; (ii) the target share of variable-rate debt is 15%; (iii) there is no exposure to foreign currency risk; (iv) the use of swaps is non-speculative (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: over January-July 2023, the average cash position stood at €3.8 billion. At the end of July, its liquidity position worth €3.7 billion covered 3.4 times debt servicing and 1.4 times the expected financing deficit for 2023.

Exhibit 3

The region's debt is well diversified

As a % of direct debt (excluding bank overdraft) as of 30/06/2023



EMTN: Euro Medium Term Notes

Source: Walloon Region, Moody's Investors Service

Revenue flexibility is supportive of the region's credit profile

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, 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 would result in around €10 million in additional revenues. 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.

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

At the end of 2023, we expect the Walloon Region's net direct and indirect debt (NDID) to reach €36 billion and thus to represent a very high 213% of operating revenues (or 209% of total revenues). According to our forecasts, the region will post average financing deficits averaging €2.5 billion over 2023-24, against €1 billion in 2019. As a result, the NDID will further increase to around €39 billion, pushing the debt burden, as measured by the NDID-to-operating revenues ratio, around 230% by the end of 2024, which is the end of the current political mandate.

The region's recurring financing deficits are mainly driven by large spending related to the Walloon Recovery Plan, which will represent €5.0 billion of expenditure over 2023-2025[1]. Out of the WRP, only 16% (€1.13 billion) will benefit from budget neutral funding from the European Union (EU)'s Recovery and Resilience Facility (RRF). While the boost in public investment from the WRP should generate medium-to-long-term economic, social and environmental benefits, its large size underpins the large financing deficits over the coming years.

Robust revenue growth and savings measures will only partially offset the cost of the Walloon Recovery Plan. Revenues move in line with nominal gross domestic product (GDP) growth, providing a natural hedge against inflation. Meanwhile, the region has committed to achieve a so-called "sustainability effort" amounting to at least €150 million each year over a 10-year period, starting in 2022, in order to stabilize its debt-to-revenue ratio. By the end of 2023, we expect that the region will post accumulated savings of €400 million, and the 2024 budget includes an additional €100 million of savings. This will however not prevent the region's debt burden from growing over the next couple of years.

Meanwhile, we expect debt affordability to remain strong. Based on our forecasts, interest payments will reach 2.9% of operating revenue in 2025, from 2.1% in 2022, reflecting the higher interest rates environment. However, the region continues to benefit from strong market access, which underpins relatively favorable funding conditions.

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 represented 73% of national average in 2021. In addition, socio-economic indicators, including disposable income per capita, labor participation and unemployment rates, are structurally weaker than peers. In 2022, the regional unemployment rate reached 8.4%, compared with a national of 5.6%.

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.

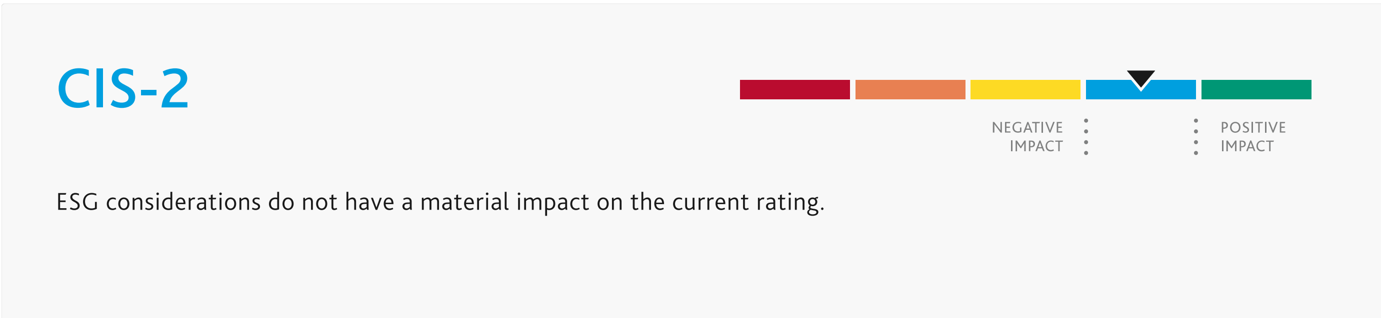
Extraordinary support considerations

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 CIS-2

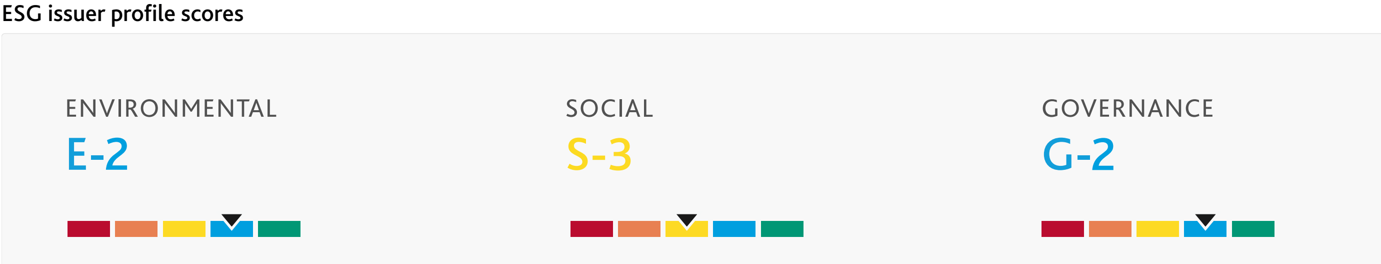
Exhibit 4
ESG credit impact score



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

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	72.92%	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				**4.25**	**30%**	**1.28**
Operating Margin [2]	9	-18.49%	12.5%			
Interest Burden [3]	3	2.24%	12.5%			
Liquidity	1		25%			
Debt Burden [4]	9	227.24%	25%			
Debt Structure [5]	1	6.99%	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						**4.70 (5)**
Systemic Risk Assessment						**Aa3**
Suggested BCA						**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 2022.

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 The plan was launched post COVID-19 pandemic, but also includes pre-pandemic commitments announced in the 2019 Regional Policy Statement

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