CREDIT OPINION
6 November 2024

Update

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RATINGS

Walloon Region

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

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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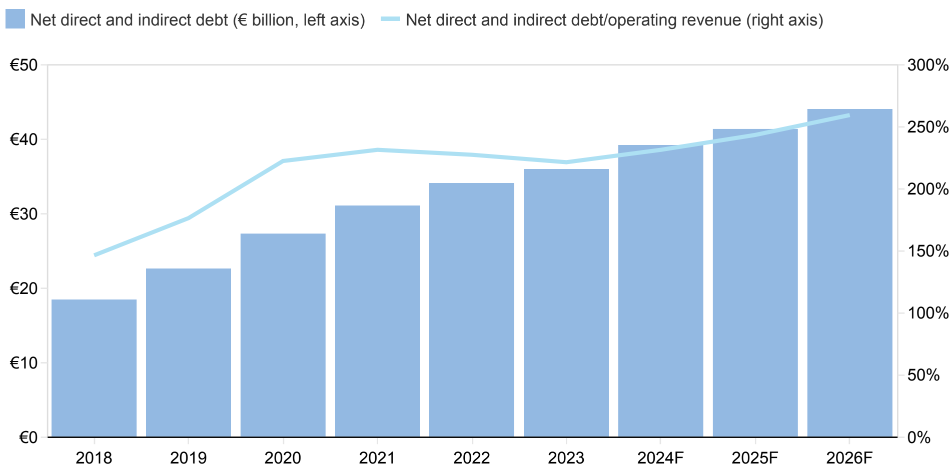
Walloon Region (Belgium)

Update following outlook change to negative

Summary

The credit profile of the Walloon Region (A3 negative) reflects a mature and robust legislative background, sophisticated but prudent debt management, unquestioned market access, and 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 negative) 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 Ratings

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 negative outlook reflects the institutional, operational and financial linkages between the Government of Belgium (Aa3 negative) and the Walloon Region.

Factors that could lead to an upgrade

Given the negative outlook on the Wallon Region's rating, positive rating action is not likely. However, the outlook could be stabilized at the current rating level if the outlook of Government of Belgium's was stabilized. The outlook could also be stabilized if the Walloon Region implemented effective fiscal consolidation measures that provide clear direction toward significantly reducing deficits, leading to a downward trend in the debt burden towards pre-pandemic levels.

Factors that could lead to a downgrade

One or a combination of the following could result in downward pressure on the ratings: a downgrade of the Government of Belgium sovereign rating; 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.

Key indicators

Exhibit 2

The Walloon Region

Walloon Region	2019	2020	2021	2022	2023	2024F	2025F	2026F
Primary operating balance / operating revenues (%)	-3.92%	-20.69%	-21.61%	-12.46%	-13.50%	-7.36%	-2.65%	-8.69%
Capital spending / total expenditure (%)	2.59%	1.57%	4.88%	3.88%	3.78%	6.29%	6.01%	3.09%
Self-financing ratio	-2.1	-11.7	-3.8	-3.1	-3.4	-1.3	-0.8	-3.3
Direct debt / operating revenue (%)	98.87%	134.06%	146.61%	148.05%	149.30%	160.91%	169.65%	182.99%
Net Direct and Indirect debt / operating revenues (%)	175.99%	222.02%	231.37%	227.24%	220.70%	231.31%	242.65%	259.10%
Interest expenses / operating revenues (%)	2.13%	2.30%	2.48%	2.11%	2.20%	2.56%	2.86%	3.23%
Debt repayment / operating revenue (%)	4.99%	6.78%	4.45%	5.90%	5.10%	8.44%	5.50%	2.79%

F: forecast

Source: Walloon Region, Moody's Ratings

Detailed credit considerations

On 15 October 2024, we affirmed the A3 rating and changed the outlook to negative from stable for the Walloon Region. This followed our change in outlook of the Government of Belgium's Aa3 rating to negative from stable on 11 October 2024. The change in outlook reflects our view that the federal government's muted response to the structural decline in public finances over recent years, along with weak fiscal coordination between the federal government, regions, and communities, creates challenges for the Walloon Region to effectively reduce its substantial fiscal deficit, despite recent consolidation efforts.

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 Government of Belgium 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 cannot 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 benefitted from a very strong access to diversified funding sources. Funding instruments comprise: (i) a €30 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 negative]; and €2.5 billion with Belfius Bank SA/NV [Belfius, A1/A1 stable]); and (iii) a €2.25 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 centralizes the cash and cash management of its satellites organizations, resulting in a comfortable cash buffer. At the end of 2023, this amounted to €3.3 billion, including €256 million directly from the region.

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, the Walloon Region's net direct and indirect debt (NDID) to reach €36 billion and thus to represent a very high 220% of operating revenues. According to our forecasts, the region will post average financing deficits averaging €2.3 billion over 2024-25, against €1 billion in 2019. As a result, the NDID will further increase to around €41 billion, pushing the debt burden, as measured by the NDID-to-operating revenues ratio, around 243% by the end of 2025.

The region's recurring financing deficits are mainly driven by large spending related to the Walloon Recovery Plan, which will represent €5 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 also contributes to the large financing deficits until 2027.

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, the region has achieved its targets and announced €268 million savings in 2025. While these efforts demonstrated the credibility of the region's commitment, they will not prevent the region's debt burden from growing until at least 2027.

Meanwhile, we expect debt affordability to remain strong. Based on our forecasts, interest payments will reach 2.9% of operating revenue in 2025, from 2.2% in 2023, 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 2022. In addition, socio-economic indicators, including disposable income per capita, labor participation and unemployment rates, are structurally weaker than peers. In 2023, the regional unemployment rate is 8.2%, 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 3
ESG credit impact score

CIS-2

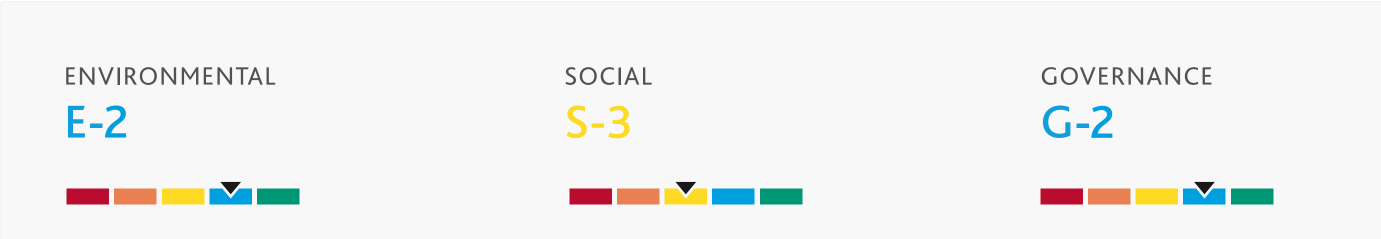
ESG considerations do not have a material impact on the current rating.

Source: Moody’s Ratings

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 4

ESG issuer profile scores



Source: Moody's Ratings

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 in line with the BCA scorecard-indicated outcome.

For details about our rating approach, please refer to Rating Methodology: Regional and Local Governments, 28 May 2024.

Exhibit 5

Walloon Region

Regional & Local Governments

Baseline Credit Assessment – Scorecard	Score	Value	Sub-factor Weighting	Sub-factor Score	Factor Weighting	Total
Factor 1: Economy					**25%**	**1.19**
Regional Income [1]	3.95	51090.73	15%	0.59		
Economic Growth	9.00	baa	5%	0.45		
Economic Diversification	3.00	aa	5%	0.15		
Factor 2: Institutional Framework and Governance					**30%**	**2.25**
Institutional Framework	6.00	a	15%	0.90		
Governance	9.00	baa	15%	1.35		
Factor 3: Financial Performance					**20%**	**2.80**
Operating Margin [2]	17.55	-13.50%	10%	1.76		
Liquidity Ratio [3]	17.90	1.57%	5%	0.89		
Ease of Access to Funding	3.00	aa	5%	0.15		
Factor 4: Leverage					**25%**	**2.49**
Debt Burden [4]	12.67	220.68%	15%	1.90		
Interest Burden [5]	5.86	2.18%	10%	0.59		
Preliminary BCA Scorecard-Indicated Outcome (SIO)						**(8.73) baa2**
Idiosyncratic Notching						**-1.0**
Preliminary BCA SIO After Idiosyncratic Notching						**(9.73) baa3**
Sovereign Rating Threshold						**Aa3**
Operating Environment Notching						**0.5**
BCA Scorecard-Indicated Outcome						**(9.23) baa2**
Assigned BCA						**baa2**

[1] Regional GDP per capita in terms of purchasing power parity (PPP) terms, in international dollars
[2] Primary Operating Balance / Operating Revenue
[3] Cash and Cash Equivalents / Operating Revenue
[4] Net Direct and Indirect Debt / Operating Revenue
[5] Interest Payments/ Operating Revenue
Source: Moody's Ratings; Fiscal 2023.

Ratings

Exhibit 6

Category	Moody's Rating
WALLOON REGION	
Outlook	Negative
Baseline Credit Assessment	baa2
Issuer Rating -Dom Curr	A3
Senior Unsecured -Dom Curr	A3
Other Short Term -Dom Curr	(P)P-2

Source: Moody's Ratings

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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CLIENT SERVICES

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