Research Update:

Belgian Region of Brussels-Capital 'AA/A-1+' Ratings Affirmed; Outlook Stable

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Overview

- We project that, due to an increase in investments, Brussels-Capital will maintain high deficits through 2019-2021, leading to marginally higher debt.
- Nevertheless, the supportive institutional framework and the region's highly efficient financial management should allow it to contain debt growth and maintain a very comfortable liquidity coverage.
- We are affirming our 'AA/A-1+' long- and short-term ratings on Brussels-Capital and maintaining our stable outlook.

Rating Action

On Sept. 13, 2019, S&P Global Ratings affirmed its 'AA' long-term and 'A-1+' short-term issuer credit ratings on Belgium's Region of Brussels-Capital. The outlook is stable.

Outlook

The outlook is stable because, in our base case, we expect Brussels-Capital will maintain a moderate debt burden and very sound liquidity, while significantly increasing capital expenditure over the next two years.

Downside scenario

We might consider a downgrade over that period if we observed a structural deterioration in Brussels-Capital's budgetary performance, leading to a significant increase in debt. This could stem from, for example, weakening financial positions of government-related entities (GREs) or the region's inability to contain expenditure growth, which would also ultimately have an impact on our perception of the region's financial management.

Upside scenario

We could consider a positive rating action in the next 24 months if Brussels-Capital structurally and significantly improved its budgetary performance, thereby putting its tax-supported debt on a downward path. However, an upgrade would be contingent on a similar action on Belgium, since we consider that Belgian regions and communities do not meet the criteria under which we would rate them higher than the sovereign.

Rationale

In our view, Brussels-Capital has a very proactive and skilled financial management team that can contain the region's debt and maintain ample liquidity to service debt, supported by the region's strong access to capital markets. We believe Brussels-Capital's deficits will remain moderate through our forecast horizon and will stem from the region's strategic investments since 2018. The region's favorable institutional framework and wealthy economy also support the ratings.

The region's economy and skilled financial management remain credit strengths

Brussels-Capital has a buoyant, service-based, and wealthy economy. Its GDP per capita is higher than the national average (we estimate €67,547 versus €40,544 in 2019). However, this is offset by the large number of people that commute to the region for work but pay taxes elsewhere, and higher unemployment than the national average. This results in the region's personal income per capita being one-fifth less, and its tax base somewhat smaller, than the national average. While the region makes up around 18% of Belgium's GDP, it accounts for only around 8% of national personal income tax receipts.

Brussels-Capital benefits from the maturity and stability of the institutional system for Belgian regions and communities, and a generally adequate revenue and expenditure balance, not least due to the regions' relatively high tax autonomy. In our opinion, the gradual implementation of the sixth Belgian state reform since 2015--including the delegation of new responsibilities to regions and communities and revenue sources to regions--has demonstrated the system's predictability. We also think that Belgium's framework enables regions and communities to play an active role in designing and implementing federal reforms, preventing or moderating measures that potentially undermine their institutional and financial position.

The region has shown its capacity to manage new revenue sources and expenditure responsibilities under the sixth state reform. We also view as positive the region's proactive debt and liquidity management. The region continually seeks improvements in its financial practices, demonstrated by ongoing policy efforts to enhance liquidity, debt service, and financial risk management on a consolidated basis, with close monitoring of the region's related entities and other contingent risks, including its well-defined and active guarantee-management system.

We also regard as favorable the new government and management's willingness to implement a spending review to keep deficits under control, and the creation of an investment committee "Comité de Pilotage des investissements strategiques" to closely follow and effectively implement planned strategic investments. The new government is also committed to controlling debt growth.

Deficits will stay relatively high in 2019-2021, with marginal debt increases, partly onlent to its creditworthy municipalities

In 2018, the region's operating balance stood at 9.5% of operating revenues, slightly below our previous forecast of 11%, due to marginally lower tax revenue and higher operating expenditure. Operating performance should stay strong through 2021, with the surplus averaging a high 9.9% of operating revenue.

In line with 2018, the deficit after capital accounts will likely stay high, at close to 9% of total revenues on average through 2021, due to the step-up in strategic investments. We expect capital expenditure will remain slightly higher than €1.5 billion per year on average in 2019-2021, versus an average of €1.1 billion during 2016-2017, and only slightly above 2018 on average. The increase is due to strategic investments started in 2018, linked to the region's mobility infrastructure and security. We forecast a decrease of these strategic investments from 2022 or 2023, which should enable the region to start reducing its deficits.

Brussels-Capital continues to target a balanced budget through 2021, according to ESA 2010 (European System of National and Regional Accounts), excluding strategic investments. If needed, to meet its budgetary target, the region could use its flexibility, in particular concerning expenditure.

Debt-refinancing and funding needs related to strategic investments, which we expect will average €500 million a year in 2019-2021, will continue to push up annual gross borrowing through our forecast horizon. Consequently, we expect Brussels-Capital's tax-supported debt will reach about 120% of consolidated operating revenue in 2021, compared with 92% in 2017. Our estimate of tax-supported debt includes the debt of the municipality fund, "Fonds régional bruxellois de refinancement des trésoreries communales" (FRBRTC), which is fully consolidated under ESA 2010. FRBRTC lends the majority of its debt proceeds to financially sound municipalities in the region. In 2018, this debt represented around 12% of the region's consolidated operating revenues.

Brussels-Capital enjoys a very favorable liquidity position, benefiting from a direct multiyear €1.2 billion account facility, and FRBRTC has €220 million of liquidity lines. We expect these liquidity sources to cover around 120% of Brussels-Capital's debt service needs (including FRBRTC's short- and long-term debt repayments) over the next 12 months. Additionally, the region has strong access to external funding via financial markets, especially through its medium-term note program, Belgian commercial paper program, and access to investors in German "Schuldschein" loans.

Key Statistics

Table 1

Brussels-Capital (Region of) Selected Indicators

	--Fiscal year end Dec. 31--				
(Mil. €)	**2017**	**2018**	**2019bc**	**2020bc**	**2021bc**
Operating revenues	4,463	4,564	4,828	4,836	4,893
Operating expenditures	3,962	4,130	4,292	4,369	4,451
Operating balance	501	434	536	467	442
Operating balance (% of operating revenues)	11.2	9.5	11.1	9.7	9.0

Table 1

Brussels-Capital (Region of) Selected Indicators (cont.)

	--Fiscal year end Dec. 31--				
(Mil. €)	2017	2018	2019bc	2020bc	2021bc
Capital revenues	592	528	574	578	581
Capital expenditures	1,120	1,509	1,564	1,504	1,564
Balance after capital accounts	(27)	(547)	(454)	(459)	(541)
Balance after capital accounts (% of total revenues)	(0.5)	(10.7)	(8.4)	(8.5)	(9.9)
Debt repaid	737	754	723	736	683
Gross borrowings	522	1,123	1,127	1,145	1,173
Balance after borrowings	(241)	(178)	(50)	(50)	(50)
Direct debt (outstanding at year-end)	4,072	4,545	4,949	5,359	5,850
Direct debt (% of operating revenues)	91.2	99.6	102.5	110.8	119.5
Tax-supported debt (outstanding at year-end)	4,105	4,579	4,982	5,392	5,883
Tax-supported debt (% of consolidated operating revenues)	92.0	100.3	103.2	111.5	120.2
Interest (% of operating revenues)	3.7	3.4	3.3	3.5	3.6
Local GDP per capita (single units)	65,000	66,596	67,547	68,508	69,453
National GDP per capita (single units)	38,789	39,601	40,544	41,603	42,731

The data and ratios above result in part from S&P Global Ratings' own calculations, drawing on national as well as international sources, reflecting S&P Global Ratings' independent view on the timeliness, coverage, accuracy, credibility, and usability of available information. The main sources are the financial statements and budgets, as provided by the issuer. bc--Base case reflects S&P Global Ratings' expectations of the most likely scenario.

Ratings Score Snapshot

Table 2

Brussels-Capital (Region of) Ratings Score Snapshot

Key rating factors	Scores
Institutional framework	2
Economy	2
Financial management	1
Budgetary performance	3
Liquidity	1
Debt burden	3
Stand-alone credit profile	aa

Table 2

Brussels-Capital (Region of) Ratings Score Snapshot (cont.)

Key rating factors	Scores
Issuer credit rating	AA

S&P Global Ratings bases its ratings on non-U.S. local and regional governments (LRGs) on the six main rating factors in this table. In the "Methodology For Rating Local And Regional Governments Outside Of The U.S.," published on July 15, 2019, we explain the steps we follow to derive the global scale foreign currency rating on each LRG. The institutional framework is assessed on a six-point scale: 1 is the strongest and 6 the weakest score. Our assessments of economy, financial management, budgetary performance, liquidity, and debt burden are on a five-point scale, with 1 being the strongest score and 5 the weakest.

Key Sovereign Statistics

Sovereign Risk Indicators, July 11, 2019. An interactive version is available at www.spratings.com/sri

Related Criteria

- Criteria | Governments | International Public Finance: Methodology For Rating Local And Regional Governments Outside Of The U.S., July 15, 2019
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Governments | International Public Finance: Methodology: Rating Non-U.S. Local And Regional Governments Higher Than The Sovereign, Dec. 15, 2014
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- Institutional Framework Assessments For International Local And Regional Governments, Nov. 6, 2018
- Default, Transition, and Recovery: 2017 Annual International Public Finance Default Study And Rating Transitions, June 11, 2018

In accordance with our relevant policies and procedures, the Rating Committee was composed of analysts that are qualified to vote in the committee, with sufficient experience to convey the appropriate level of knowledge and understanding of the methodology applicable (see 'Related Criteria And Research'). At the onset of the committee, the chair confirmed that the information provided to the Rating Committee by the primary analyst had been distributed in a timely manner and was sufficient for Committee members to make an informed decision.

After the primary analyst gave opening remarks and explained the recommendation, the Committee discussed key rating factors and critical issues in accordance with the relevant criteria. Qualitative and quantitative risk factors were considered and discussed, looking at track-record and forecasts.

The committee's assessment of the key rating factors is reflected in the Ratings Score Snapshot above.

The chair ensured every voting member was given the opportunity to articulate his/her opinion. The chair or designee reviewed the draft report to ensure consistency with the Committee decision. The views and the decision of the rating committee are summarized in the above rationale and outlook. The weighting of all rating factors is described in the methodology used in this rating action (see 'Related Criteria And Research').

Ratings List

Ratings Affirmed	
Brussels-Capital (Region of)	
Issuer Credit Rating	AA/Stable/A-1+
Senior Unsecured	AA