11 May 2018

Rating-Agentur Expert RA confirmed at 'AAA' the ratings of the United States of America

Rating-Agentur Expert RA confirmed the sovereign government credit rating (SGC) of the United States of America at 'AAA' (Highest level of creditworthiness of the government) in national currency and at 'AAA' (Highest level of creditworthiness of the government) in foreign currency.

Rating-Agentur Expert RA confirmed the country credit environment rating (CCE) of the United States of America at 'AAA' (Highest quality of credit environment of the country) in national currency and at 'AAA' (Highest quality of credit environment of the country) in foreign currency.

MAJOR FACTORS THAT INFLUENCED BOTH TYPES OF RATINGS:

Positive factors:

- Highly diversified, technologically advanced and dynamic national economy combined with a favourable geographical and geopolitical stance. The country scored 5,85 out of 5,9 in the 2017 competitiveness index from the World Economic Forum and ranked 8th out of 190 countries in the Doing Business 2018 report published by the World Bank;
- The U.S. is one of the world's wealthiest and most developed countries with a GDP per capita of USD 59 300 in PPP terms in 2017 well above large advanced countries and a Human development index of 0,79 in 2015;
- Highly developed and liquid stock market as evidenced by the market capitalization of listed companies at 146% of GDP by May 2018;
- Real GDP grew over the past six years at an average rate of 2,1% despite slowing down to 1,5% in 2016; the lowest growth rate since 2011. Real output growth of the economy was reported at 2,3% in 2017 and we expect this metric to remain robust along 2018 at around 2,9% following the government's fiscal reform;
- The unemployment rate is still declining and stood at 4,4% in 2017. Going forward, we expect the unemployment rate to reduce the pace of its decline and to stabilize around 3,6% following the move of the national output gap from negative to positive ground. This, in our view, will ultimately derive in a stubbornly higher inflation rate, which in turn will represent a strong challenge for the FED's decision to increase rates and normalize the monetary policy in the long run;
- Short-term debt metrics remain bearable, despite having increased slightly in 2017 to 10,3% of GDP and 33,4% of budget revenues;
- The inflation rate stood at 2,1% in 2017, slightly below the 2,2% figure reported in 2016. Going forward, we expect inflation rates to remain around these figures motivated by the counterbalanced expansionary effects of the recently passed tax reforms and the potential interest rate hike derived from monetary policy normalization.

Restricting factors:

- The economy remains highly leveraged as indicated by the volume of private credit to GDP which reached 240% in 2016 and we expect this metric to be around this value in 2017. However, the interest rate hike which resulted from the monetary policy normalization initiated in early 2017 could potentially curb the credit growth in the country;
- The U.S. fiscal deficit widened by almost 0,4p.p. to 4,6% of GDP in 2017 driven by a decline

in fiscal revenues. We could potentially observe a significant mid- and long-run increase in the fiscal pressure if the tax cut reform introduced by president Trump's administration is not able to push economic growth and job creation in the mid run;

- FDI inflows reached 1,5% of GDP in 2017 after falling by 1,1p.p. from a year before. This is the strongest decline of the metric since 2009, when it declined by 1,2p.p. as a result of the world's financial crisis.

Negative factors:

- Government debt load increased by 4,7% to USD 20,9 tn and remained high at 107,8% of GDP and 346,7% of budget revenues as of end-2017. Following the suspension of the debt ceiling until 1 March 2019 we expect the gross government debt to increase by around 5,5% to USD 22 tn in 2018. This is likely to derive in an increase of debt ratios given our GDP and budget revenues growth rates expectations at 5% and 4% respectively;
- Albeit slightly shrinking from a year ago, the trade deficit remained elevated at around 2,4% of GDP in 2017. The government's commitment to renegotiate a number of trade deals (including NAFTA) and the recent increase of aluminum and steel import tariffs could have mixed material effects on the country's trade balance;
- Persistent politicking between the legislative and executive branches of the government on fiscal policies and debt ceilings that sometimes increases the possibility of a technical debt default. Even though the president belongs to the Republican Party, which holds majority in both the House of Representatives and the Senate, evidence shows that this risk has not been entirely mitigated. Moreover, a win by the democrats in the upcoming midterm elections in November could further extend this issue.

Support factors:

- The U.S. has a strong financial system which affects other countries and the U.S. Treasury bonds serve as international benchmark for fixed income securities (very strong support factor);
- The country has very strong and important global reserve currency: USD (moderately strong support factor);
- Participation in strong trade and political unions (NAFTA, OECD) (moderately strong support factor).

ADDITIONAL FACTORS THAT INFLUENCED CCE RATINGS:

Positive factors:

- High quality and large variety of instruments on the financial market;
- Real interest rate remained stable around 2,1% in 2017 as a result of the combined effect of the increase in the fed funds and inflation rates;
- The U.S. stock market's position remains solid. However, despite having improved steadily through 2017 mainly on the back of the government's expansionary policies, the U.S. stock market showed a negative trend during the first months of 2018.

Restricting factors:

- The country occupies the 41st place out of 180 countries in the ranking of protecting investors from the Doing Business publication.

Negative factors:

- Significant level of private sector debt to GDP at around 253% in 4Q 2017. However, we can expect a reduction of this metric as a result of the progressive interest rate hike in the long term.

SENSITIVITY ASSESSMENT:

The following developments could lead to a downgrade:

- Further increase of the fiscal deficit as a result of lower than expected fiscal revenues or higher expenses. The cut in the corporate tax rate combined with higher interest payments following the hike in the Fed Funds rate could lead to higher deficit figures in the long run;
- Renegotiation or withdrawal from key trade agreements (NAFTA in particular), which could lead to a reduction of the U.S. volume of trade and increase of domestic prices;
- Further decline of net FDI which would reduce overall investments.

"The ratings of the United States are confirmed at 'AAA' and remain underpinned by the country's supportive economic conditions and resilience to external and domestic shocks. However, the deterioration and negative forecast of key macroeconomic metrics challenges the long-term sustainability of these ratings. Gross government debt increased between February and April 2018, following the recently passed tax reform and suspension of the debt limit until March 2019. If this scenario remains in place, we can anticipate debt metrics to increase and fiscal deficit to widen further through 2018.

Monetary policy normalization is set to continue on the back of higher inflation expectations and stable economic growth, which is likely to propel further interest rate hikes throughout the current year. Inflows of foreign direct investments (FDI) recorded its largest drop since the 2009 financial crisis, showing a slowdown of investments in the country. Nonetheless, this might be partially offset by a potential windfall of investments motivated by the recently passed tax reform. In our view, a potential renegotiation of NAFTA and the recent announcement of the federal government to impose import tariffs on aluminum and steel is more likely to derive in a trade war with other countries or a reduction in the volume of trade rather than in a reduction of the trade deficit of the country." – Clarified Gustavo Angel, Rating Associate of Rating-Agentur Expert RA GmbH

Responsible expert: Gustavo Angel, Rating Associate of Rating-Agentur Expert RA GmbH

Reviewer: Hector Alvarez, Rating Associate of Rating-Agentur Expert RA GmbH

Research report on USA is available at:

http://raexpert.eu/reports/Research_report_USA_11.05.2018.pdf

Next scheduled rating publication: 9 September 2018. The full sovereign rating calendar can be found at http://raexpert.eu/sovereign/#conf-tab-5

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RATING HISTORY:

Date	Review reason	SGC		CCE	
		National currency	Foreign currency	National currency	Foreign currency
17.11.2017	Scheduled revision of both types of ratings for the country	AAA	AAA	AAA	AAA
19.05.2017	Scheduled revision of both types of ratings for the country	AAA	AAA	AAA	AAA
25.11.2016	Scheduled revision of both types of ratings for the country	AAA	AAA	AAA	AAA
03.06.2016	Scheduled revision of both types of ratings for the country	AAA	AAA	AAA	AAA
11.12.2015	First assignment of both types of ratings for the country	AAA	AAA	AAA	AAA

Minute's summary

The rating committee for USA was held on 9 May 2018. The quorum for the rating committee was present. After the responsible expert presented the factors, which influenced the rating assessment, the members of the committee expressed their opinions and suggestions within the framework of the Sovereign methodology. The chairman of the rating committee ensured that every member of the committee expressed his/her opinion before proceeding to the voting.

The following methodology was used for the rating assessment: Methodology for Assigning Sovereign Government Credit Ratings and Country Credit Environment Ratings – Short Public Version (from April 2017) can be found under the following link: http://raexpert.eu/files/methodology/Methodology_Short_Sovereign_v2.pdf. Descriptions and definitions of all rating categories can be found under the following link: http://raexpert.eu/sovereign.php under the "Rating scale" section. The user of the rating shall read the methodology in order to have a full understanding of the rating procedure.

These ratings are unsolicited. The rated entity did not participate in the rating process.

Main sources of information International Monetary Fund, World Bank, World Federation of Exchanges, World Economic Forum, Doing Business, United Nations, US Federal Reserve.

Limits of the Credit Rating

During the rating assignment process, Rating-Agentur Expert RA GmbH (the Agency) used publicly available information that was considered to be reliable, complete and non-biased. The responsible expert performed the rating assessment of the country with information considered as the most reliable and up to date in accordance to the overall position of the country and the Agency's internal criteria for selecting data providers. The information and data used for this specific assessment can be considered as of sufficient quality.

Regulatory use

Only SGC ratings can be used for regulatory purposes according to the ESMA definition. CCE ratings are not considered as credit ratings within the framework of Regulation (EC) No 1060/2009.

Conflict of interest

The responsible expert was neither influenced nor biased by third parties during the rating assessment. All employees involved in the rating assessment and revision of the rated entity have reported absence of conflicts of interests before initiation of the rating process.

Rating-Agentur Expert RA GmbH is completely independent from the activities of other agencies of the RAEX group.

Risk warning

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This press-release represents the opinion of Rating-Agentur Expert RA GmbH and is not a recommendation to buy, hold or sell any securities or assets, or to make investment decisions.

Office responsible for preparing the rating

The office responsible for the preparation and issuance of this credit rating is the office of Rating-Agentur Expert RA GmbH in Frankfurt am Main, Germany.

Rating-Agentur Expert RA GmbH is a credit rating agency established in Germany and therefore shall comply with all applicable regulations currently in force in the European Union.

The European Securities and Markets Authority (ESMA), the EU's direct supervisor of credit rating agencies (CRAs), has registered Rating-Agentur Expert RA GmbH as a CRA under Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit rating agencies, with effect from 1 December 2015.

Rating-Agentur Expert RA GmbH applies the Code of Conduct Fundamentals for credit rating agencies issued by the International Organization of Securities Commissions (IOSCO Code) and includes the basic principles of IOSCO Code in its Code of Conduct.