Research Report on United States of America

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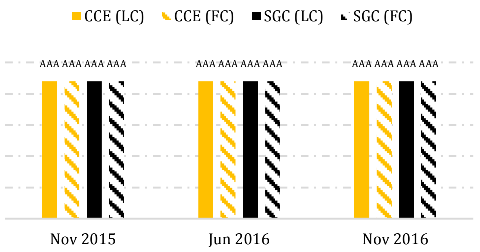
Ratings

Sovereign Government Credit (LC)	AAA
Sovereign Government Credit (FC)	AAA
Country Credit Environment (LC)	AAA
Country Credit Environment (FC)	AAA

* These ratings are unsolicited

Ratings dynamics



Main Economic Indicators of USA

Macro indicators	2013	2014	2015
Gross gov. debt, USD bn	17463	18194	18966
Nominal GDP, USD bn	16692	17393	18037
Real GDP growth, %	1,7	2,4	2,6
Gross gov. debt/GDP, %	104,6	104,6	105,2
Deficit (surplus)/GDP, %	-4,4	-4,2	-3,5
Inflation rate, %	1,3	0,6	0,7
Current Account Balance/GDP, %	-	-	-2,9
External debt, USD bn	-	-	48,9

Development indicators	2015
Inequality adj. HDI	0,76
GDP per capita, USD th	56,1

Default indicator	24.11.2016
5-Year CDS spread, Bp	20
10Y Gov Bond Yield, %	2,35

Source: RAEX (Europe) calculations based on data from the IMF, Census Bureau and DB.

Summary

The Agency is confirming the ratings of USA at 'AAA' under the assumption that, in our mid-term perspective, the country's economic stance will offset the increased policy uncertainty, which emerged after the victory of president-elect Donald Trump.

The US economy has shown significant resilience to external and domestic shocks while the monetary and fiscal policies have well accommodated to economic conditions. A still declining unemployment rate combined with higher expected price levels, creates the conditions for a gradual potential increase in the Fed Funds rate.

A high degree of uncertainty materialized after Donald Trump was elected president on November 8th. During his campaign, he announced possible changes in certain trade deals and in the corporate tax regime, which could lead to a deterioration of the country's economic position in the long run. However, if the Dodd-Frank act is eliminated, as he proposed, financial markets could benefit backed by lower regulations.

Economic conditions remain strong. The US economy keeps showing signs of recovery as unemployment and annual inflation rate stood at 4,9% and 1,6% respectively in October 2016. Real GDP growth, despite decelerating over the past few quarters, remained strong at 1,5% in 3Q 2016 supported by an increase in domestic demand and accommodative macroeconomic policies.

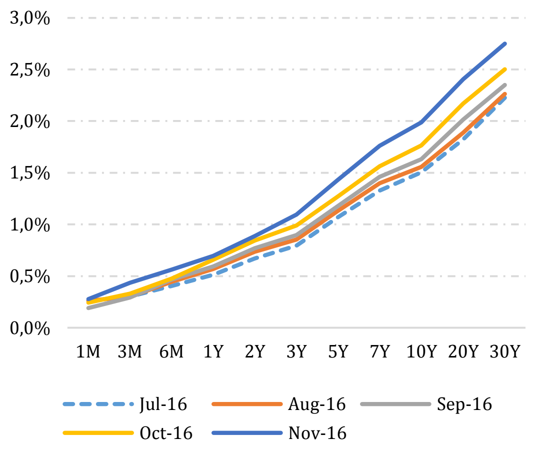
The US economy has constantly proved resilience to financial markets volatility, the appreciation of the USD against major world currencies and poor global growth and demand. However, the country still faces a number of challenges, such as the increasing expenditure on social security, raising poverty and inequality and ageing of basic infrastructure, which could become credit negative in the long term.

In the near term we expect growth to keep its momentum supported by further employment creation, persistently low energy prices and a pick-up in net household formation. In the long run the growth outlook will be conditioned by the policies of the newly-elected government.

Monetary policy still accommodative. Despite lower unemployment rates and higher GDP growth and inflation expectations, the US monetary policy remains accommodative. However, in line with our expected dynamics in our previous research report[1], the Federal Open Market Committee (FOMC) projected in June 2016 the Federal Funds rate at 1,1%, 1,9% and 2,6% for 2017, 2018 and 2019 respectively.

Financial markets have already reacted to higher inflation expectations and therefore a potential increase of the Fed Funds rate, as the Treasury yield curve has been steepening since July 2016 (see graph 1). The yield on the long-term bonds has increased proportionally more than that of the short-term bonds. This also reflects the perception of the market participants about the long-term policy uncertainty which emerged after victory of Donald Trump as president-elect of the US.

Graph 1: Average Treasury yield curve, % rates

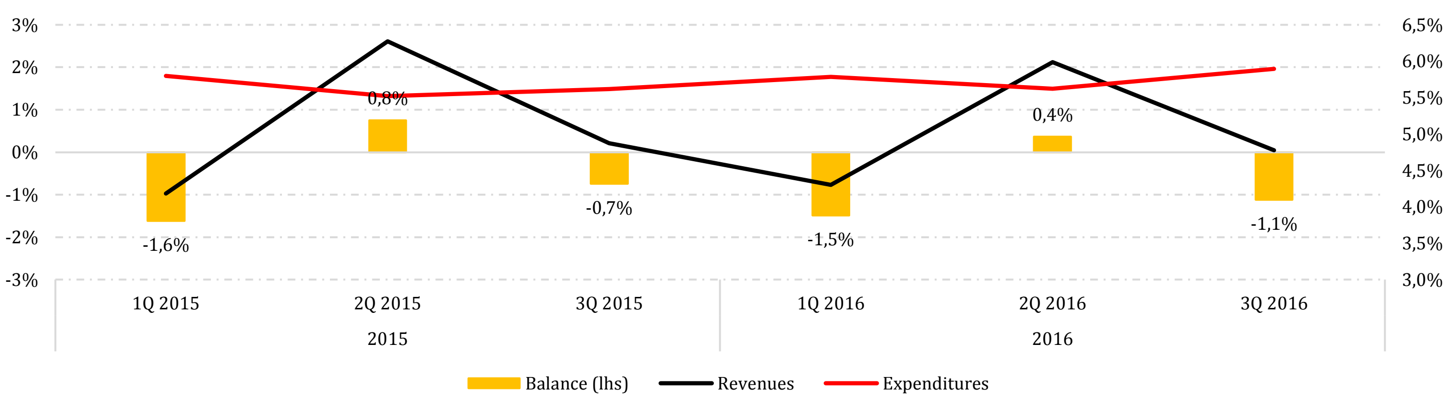


Source: RAEX (Europe) calculations based on data from the Federal Reserve

Fiscal risks emerged. The fiscal deficit of the US government has narrowed significantly over the past years from around 11% in 2010 to 3,5% in 2015. Such a decline resulted from the combined effect of lower interest expenses and higher revenues linked to stronger economic activity. Additionally, part of the general government spending was covered by debt, which increased around 10p.p. from 2010 up to 105% of GDP in 2015. However, fiscal deficits widened during 9m 2016 compared to the same period a year before (see graph 2). For this reason we expect the fiscal balance to revert its trend in 2016, rounding up the year around -4% of GDP.

During his campaign, president-elect Donald Trump announced that he will propose to reduce corporate taxes from 35% to 15% and to decrease a number of regulations aimed at boosting internal production. At the same time, he disclosed his intention to increase spending in infrastructure under his administration. If those reforms materialize and the Federal Funds rate increases, the US fiscal deficit is likely to increase in the long run.

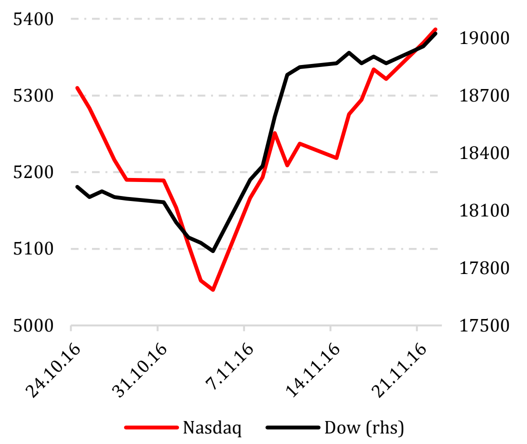
Graph 2: US government fiscal balance, % GDP



Source: RAEX (Europe) calculations based on data from the US Treasury

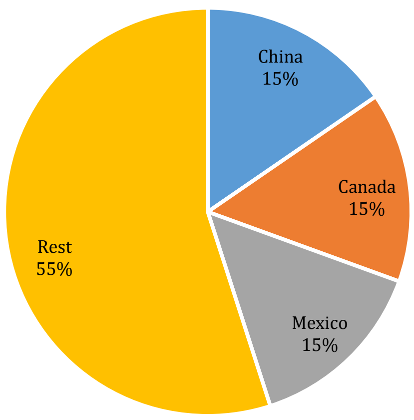
[1] Research Report on United States of America June 3rd,2016 http://raexpert.eu/reports/Research_report_USA_03.06.2016.pdf

Graph 3: Major Stock Market Indexes



Source: RAEX (Europe) calculations based on data from MarketWatch

Graph 4: Trade volume by US trade partners, %



Source: RAEX (Europe) calculations based on data from MarketWatch

Tailwind for the financial markets. The US banking sector remains strong with assets and credits at around 86% and 238% of GDP respectively. Banks were able to maintain positive levels of profitability despite facing an environment of low interest rates. However, the potential hike of interest rates in the upcoming months is likely to increase banks' profitability.

Donald Trump announced during his campaign that he would eliminate the Dodd-Frank act. If it materializes, this could boost growth of the financial markets by reducing regulation. Such a positive outlook for the financial industry was already reflected by the major stock market indexes, which increased by 5% on average during November only (see graph 3). However lower regulation could also translate into banks taking higher risks in the very long term, which ultimately increases the risk of a systemic crisis.

Uncertainty over trade. During his campaign President-elect Donald Trump stated that a number of trade deals, which involve major partners like Canada or Mexico (see graph 4), were going to be revised if elected. More recently he announced that the US will most likely withdraw from the Trans-Pacific Partnership (TPP) after assuming in January 2017. Instead, the US will renegociate separate trade agreements with each country. If enacted, these policies could have a positive effect on the US trade balance by limiting imports. However, the US trade could potentially shrink and internal prices could increase as a counter-effect of such policies in our view. Additionally, trade agreements tend to be negotiated within a long time span, which adds further uncertainty on the final results of such deals.

Political risks could be mitigated. Politicking between the executive and legislative branches is likely to lower as Republicans continue to hold a majority of votes in both the Senate and the House of Representatives. While this could mitigate the risk of technical debt defaults, it increases the risk of higher fiscal spending and government debt increase.

Important note for sovereign ratings

This Research Report shall be treated as a supplementary part of the published Press Release included in the following link:

http://www.raexpert.eu/reports/Press_release_USA_25.11.2016.pdf

Both documents shall be treated as essential parts of each other.

For further information on the factors, their weights, methodologies, risks and limitations of these ratings, and other regulatory disclosures, please refer to the Press Release and the website of the Agency.