

Rating-Agentur Expert RA confirmed at 'AAA' the ratings of Germany. The rating outlook is stable.

Rating-Agentur Expert RA confirmed the sovereign government credit rating (SGC) of Germany 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. The rating outlook is stable which means that in the mid-term perspective there is a high probability of maintaining the rating score.

MAJOR FACTORS THAT INFLUENCED BOTH TYPES OF RATINGS:

Positive factors:

- We anticipate government debt to GDP to have finally broken the 60% threshold in 2019 and to post a figure of around 58,6% of GDP. This metric has been gradually declining since 2012 mainly as a consequence of prudent fiscal policies, as well as a persisting low and currently negative interest rate environment for government obligations. Going forward, we expect the level of debt to continue in a declining trend as fiscal buffers remain vast and financing rates will remain depressed;
- Short-term debt remains low as, by the end of 3Q 2019, it stood at about 12,6% of GDP;
- Germany is one of the world's leaders in real GDP per capita at PPPs, which is expected to be around USD 53,6 th in 2019. Moreover, economic development remains a key strength as the country occupied the seventh position in the World Economic Forum's Competitiveness Index and the 22nd position in the World Bank's Business Ranking in 2019;
- The inflation rate, as measured by the HCIP, stood at 1,53% in 2019, remaining fairly stable as previously anticipated. We expect the inflation rate to stay below the 2% the upper target of the ECB's price stability policy;
- The spread between 10-year German and US bonds is about -2p.p. German bonds continue to have a negative yield, which is gradually declining and has reached record levels;
- Fiscal policy remains prudent as Germany is expected to post a new surplus of around 1,5% in 2019. The government already approved reforms to increase social spending in the form of the introduction of the basic pension, as well as a reduction in the tax burden on the population. We expect the fiscal surplus to remain at about 1% of GDP in 2020;
- Despite the lingering slowdown in the economy, demand for labor remains high, reaching a historically low unemployment rate of 3,2% by end-2019. In the mid-term, demand for employees will be stimulated by the gap from ageing of the current working population;
- The banking system remains stable, with favorable liquidity metrics, although we have observed some signs of upside risk. The credit-to-GDP gap has gradually increased potentially showing some overheating of the credit market. Nonetheless, NPLs ratio remains extremely low as it stood at 1,3% as of 1H 2019. Moreover, capital adequacy ratio remains quite solid at 18,6% by 3Q 2019 and the liquid assets to total short-term liabilities ratio was strong at 152% as of the same date;
- Highly developed national stock market with a capitalization to GDP ratio of 54% in 2019.

Restricting factors:

- Economic growth continued to decline in 2019 as compared to a year before as the real GDP grew by a mere 0,6% with null growth in 4Q 2019. Nonetheless, the year-end number was mostly in line with the figure anticipated in our previous review. The slowdown was marked by a contraction in manufacturing resulting from lower demand for exports, while construction and services hiked consistently. Even though domestic consumption was overall strong during the year, it was markedly slower in 4Q 2019. We anticipate growth to remain weak mainly as a result of negative external shocks continuing to affect manufacturing output;
- Aging population and low birth rates in Germany continue to be a concern in regards to the shrinking working force in the country. These dynamics are expected to have a direct impact on economic growth and public finances in the long-term as pension and healthcare spending are projected to grow significantly. Moreover, the recent approval of the basic pension increases public spending while not solving the long-term issue;
- Total assets of the banking sector as a percentage of GDP increased by 9p.p. y-o-y in 2019 after having declined by 5,1p.p. y-o-y in 2018. The increase was mainly driven by portfolio derivatives as loans to non-banks increased by 3,9%. Even though credit has resumed an upward trend, there is also evidence that banks have relaxed loan requirements restrictions in order to increase profitability;
- The average banks' capital to assets ratio remained subdued in 2019 at around 6,5%, slightly below the average 7% for European Union.

Negative factors:

- The German banking system continues to struggle delivering profitability as interest rates remain extremely low, operating profit remains narrow and capital requirements have increased as a result of the introduction of the countercyclical capital buffer¹ back in July 2019. Moreover, solid credit growth to domestic enterprises and households combined with looser lending conditions could make the financial system vulnerable to a potential economic downturn;
- Germany's exposure to potential contingent liabilities remains one of the highest in the EU, as the country has one of the most elevated amount of government guarantees among the 28 EU amount of as they represent about 12,8% of GDP at the end of 2018; while liabilities of public corporations were about 90,5% (mostly related to *Landesbanken* and *Sparkassen*) as of the same date². Both figures remain among the top-5 countries in the EU. In the event of materialization of such liabilities, the government would have to meet obligations and endure unanticipated pressure on the budget. Despite this, the risk of these obligations transferring to the balance sheet of the government is relatively low.

Support factors:

- Germany participates and is a key member of the European Union (very strong support-factor);
- The country has an extremely strong financial system which affects other countries (very strong support-factor);
- The country has a strong, stable and important reserve currency (Euro) (moderately weak support-factor).

¹ The countercyclical capital buffer is intended to make the banking system more resilient to cyclical systemic risks. BaFin raised the buffer to 0,25% of risk-weighted domestic exposures with effect from the third quarter of 2019 with a 12-month phase-in period.

² According to Eurostat Report "Contingent liabilities and non-performing loans in the EU Member States in 2018".

SENSITIVITY ASSESSMENT:

The following developments could lead to an upgrade:

- Prolonged economic downturn as a result of negative external factors which will result in deteriorating public finances;
- Substantial deterioration in financial soundness indicators in the banking system as a result of materializing shocks from a lower economy.

ESG Disclosure:

Inherent factors:

- Quality of fiscal policy; quality of monetary policy; natural resources; natural and climatic threats; environmental threats; Level of corruption, CPI; Government Effectiveness Index; quality of the business environment; position in Doing Business Ranking; level of investment in human capital, adjusted for inequality; Rule of Law Index; transparency of government policymaking Index; level of information transparency of the government; Political Stability and Absence of Violence/Terrorism Index; natural disasters, constant exposure to difficult natural conditions.

Drivers of change factors:

- None.

“The ratings of Germany at ‘AAA’ are supported by the excellent position of the government’s public finances, the outstanding external stance as well as a still resilient and solid economy with low and stable levels of unemployment. Moreover, the banking sector remains well capitalized and with a strong liquidity position, as well as solid asset quality.

However, risks threatening the economic stance and the stability of the banking sector have built up as of late, but we estimate these not to threaten the country’s creditworthiness in the mid-term perspective as the government has enough buffers and tools to weather these uncertainties. Factors such as, contingent liabilities, profitability and the widening of the credit-to-GDP gap in the banking sector, ageing population and lower external demand could potentially hurt the strong position of Germany in the external sphere, negatively impact economic growth and create imbalances in its public finances.” – Clarified Hector Alvarez, Associate Director of Rating-Agentur Expert RA.

Research report on Germany is available at:

https://raexpert.eu/reports/Research_report_Germany_28.02.2020.pdf

Next scheduled rating publication: 28 August 2020. The full sovereign rating calendar can be found at [Sovereign Rating Calendar 2020](#)

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RATING HISTORY:

Date	Review reason	SGC		Outlook	
		National currency	Foreign currency	National currency	Foreign currency
30.08.2019	Scheduled revision of both types of ratings	AAA	AAA	Stable	Stable
01.03.2019	Scheduled revision of both types of ratings	AAA	AAA	Stable	Stable
07.09.2018	Scheduled revision of both types of ratings	AAA	AAA	Stable	Stable
09.03.2018	Scheduled revision of both types of ratings	AAA	AAA	NA	NA
15.09.2017	Scheduled revision of both types of ratings	AAA	AAA	NA	NA
17.03.2017	Scheduled revision of both types of ratings	AAA	AAA	NA	NA
23.09.2016	Scheduled revision of both types of ratings	AAA	AAA	NA	NA
15.04.2016	First assignment of both types of ratings for the country	AAA	AAA	NA	NA

Minute's summary

The rating committee for Germany was held on 28 February 2020. 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 – Full Public Version](#) (from April 2019). Descriptions and definitions of all rating categories can be found 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.

The definition of default can be found on the Agency's website in the section for [Internal policies](#).

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, German Bundesbank, European Central Bank, Ministry of Finance of Germany, Deutsche Börse, Destatis, Cbonds.

ESG Disclosure

We consider Environmental, Social, and Governance (ESG) risks and opportunities in the creditworthiness analysis of our Sovereign entities. The disclosure document can be found on the Agency's website in the section: [ESG factors in RAEX-Europe's Credit Ratings](#)

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

SGC ratings can be used for regulatory purposes according to the ESMA definition.

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

The Agency disclaims all liability in connection with any consequences, interpretations, conclusions, recommendations and other actions directly or indirectly related to the conclusions and opinions contained in the Agency's press-release and research report.

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.