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# Research Report on USA

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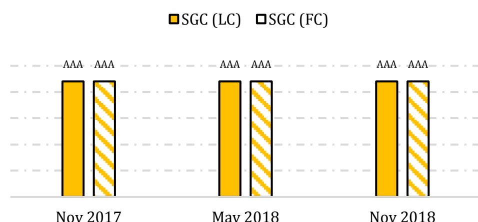
**Ratings**

| | |
|---|---|
| Sovereign Government Credit (LC) | AAA |
| Sovereign Government Credit (FC) | AAA |
| Outlook (LC) | Stable |
| Outlook (FC) | Stable |

* These ratings are unsolicited

**Ratings dynamics**




**Main Economic Indicators of USA**

| Macro indicators | 2015 | 2016 | 2017 |
|---|---|---|---|
| Gross gov. debt, USD bn | 19 092 | 19 986 | 20 499 |
| Nominal GDP, USD bn | 18 219 | 18 707 | 19 485 |
| Real GDP growth, % | 2,9 | 1,6 | 2,2 |
| Gross gov. debt/GDP, % | 104,8 | 106,8 | 105,2 |
| Deficit (surplus)/GDP, % | -3,2 | -3,9 | -3,8 |
| Inflation rate, % | 0,7 | 2,2 | 2,2 |
| Current Account Balance/GDP, % | -2,4 | -2,4 | -2,4 |
| External debt, USD bn | - | - | 19306* |

| Development indicators | 2017 |
|---|---|
| Inequality adj. HDI | 0,92 |
| GDP per capita, USD th | 59,8 |

| Default indicator | 09.11.2018 |
|---|---|
| 5-Year CDS spread, Bp | 21,31 |
| 10Y Gov Bond Yield, % | 3,21 |

Source: RAEX-Europe calculations based on data from the IMF, WB.
* Figure for 2Q 2018

## Summary


Our confirmation of the United States' credit ratings in both national and foreign currency with a stable outlook reflects the country's sound macroeconomic position as well as its resilience to external and domestic shocks.

Gross government debt continued to grow along 2018 as a result of the government's lose fiscal policy and the suspension of the debt limit until March 2019. We expect debt metrics to increase and fiscal deficit to widen by the end of 2018; however, the results of the November 2018 House of Representative elections could make it difficult for the government to follow through with the planned agenda in respect to fiscal policy.

Based on higher inflation expectations and stable economic growth, we anticipate monetary policy normalization to continue in 2019. Therefore, we expect several interest rate hikes within the next 12 months. Inflows of foreign direct investments (FDI) recorded its largest drop since the 2008 financial crisis, showing a slowdown of investments in the country, while trade deficit is expected to widen slightly in 2018. On the one hand, the United States-Mexico-Canada Agreement (USMCA) has alleviated some uncertainty regarding the economic impact of a no-deal between these countries. On the other hand, the trade spat with China could have mixed material effects on the country's trade balance.


**The uncertainty about the fiscal and debt position of the government in 2019 has increased.** The U.S. fiscal balance improved slightly in 2017 to -3,8% of GDP (from -3,9% a year before). For the current year, we expect government revenues to increase at a slower pace than expenditures, which is likely to derive in a wider fiscal deficit, which we forecast at around 4,5% of GDP by the end of 2018 (see graph 1).

However, the results of November 2018 elections can change our expectations about 2019 budget results. A divided Congress, in which the Democrats control the U.S. House of Representatives and the Republicans keep the Senate, makes the president's plan for long term fiscal stimulus much harder to implement. Therefore, the final fiscal gap in 2019 can shrink.

The lose fiscal policy in place for more than two years together with other factors had a positive effect in an economy's dynamic as shown by the GDP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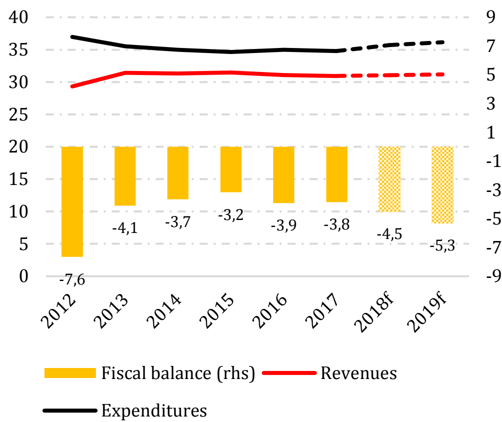
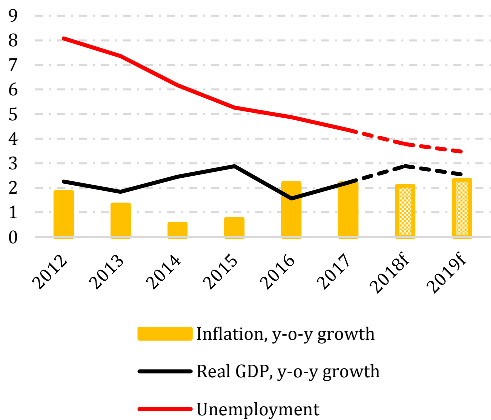
**Graph 1:** Fiscal budget dynamics, % of GDP



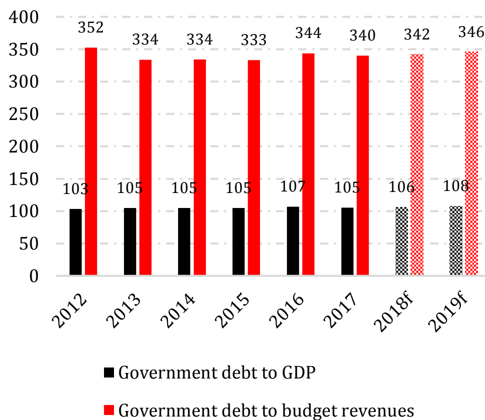

Source: RAEX-Europe calculations based on data from IMF

**Graph 2:** Macroeconomic indicators, %




Source: RAEX-Europe calculations based on data from IMF

**Graph 3:** Government debt dynamics, %




Source: RAEX-Europe calculations based on data from IMF

growth rate, which we forecast at around 3% by the end of 2018 (see graph 2), which is 0,7p.p. higher than a year ago. At the same time, the GDP growth rate is expected to slow in the long run due to a decrease in investments and the negative effects from the U.S. – China trade spat.

Government debt load increased by 2,6% to USD 20,5 tn and remained high at 105,2% of GDP and 340% of budget revenues as of end-2017 (see graph 3). We expect the gross government debt to increase by around 1p.p. up to 106% of GDP in 2018, taking into account the decision to raise government spending and suspend the government's debt ceiling once again until March 2019. However, there is a high probability of intensification of politicking between the legislative and executive branches of the government on debt ceilings in 2019, as we have observed before when the executive and legislative bodies are represented by different parties.

The maturity structure of U.S. government debt remains favorable, as shown by the ratio of short-term debt to GDP and budget revenues, that despite having increased slightly in 2017 to 10,3% and 33,4% respectively, has remained fairly constant in 2018.

**Positive GDP dynamics and low unemployment have benefited from the government fiscal policy, while FDI showed a negative trend.** The U.S. economy in general had a positive impact from the fiscal stimulus, as evidenced by the positive GDP dynamic (see graph 2). This led to a persistent unemployment rate decline that stood at 3,7% as of October 2018. Going forward, we expect the unemployment rate to reduce the pace of its decline and to stabilize at around 3,6% following the potential slowdown of the economy's growth and the move of the national output gap from negative to positive ground.

The key negative consequence of the government's policy, including the fiscal reform, is a sharp decline of the inflow of foreign investments, which, coupled with an increase in outflows, pushed the net FDI to post a negative figure in 2017 for the first time since 2014.

**The economy's leverage remains high but with a sound financial system.** The economy remains highly leveraged as indicated by the volume of private credit to GDP, which reached 240% in 2016. We expect this metric to be around 243% in 2017 and to continue in a slight upward trend in 2018.

However, the banking system soundness remains at acceptable levels, as evidenced by constantly declining level of non-performing loans which reached the lowest point over the last six years at 1,1% by end-2017;

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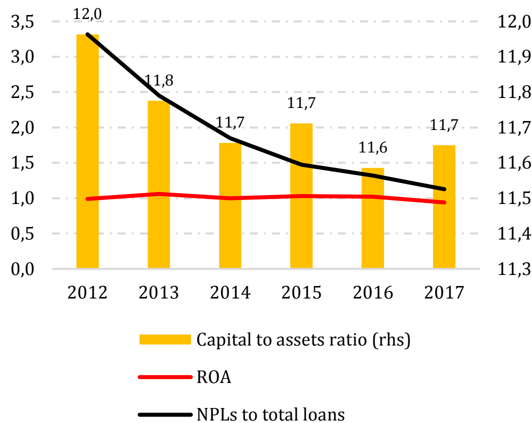
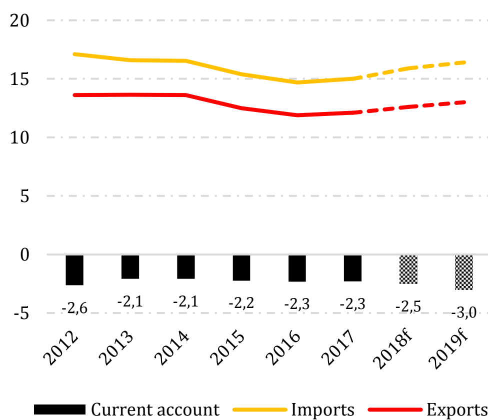
**Graph 4:** Financial soundness indicators, %




Source: RAEX-Europe calculations based on data from the IMF, WB, FED

**Graph 5:** External sector indicators, % of GDP




Source: RAEX-Europe calculations based on data from the IMF and WB

positive ROA recorded by the banks; as well as stable ratio of bank's capital to assets at 11,7% by the end of 2017 (see graph 4).

The country is also characterized by highly developed and liquid stock markets as evidenced by the market capitalization of listed companies at 165,7% of GDP by end-2017. The key stock indexes remained stable within the first three quarters of 2018, reflecting the investors' positive expectations on the performance of the national economy. However, recently increased volatility on the national stock exchanges is worrisome.

**Interest rates are expected to experience further hikes in 2019, but in a more gradual manner.** Following the increase in inflation rates and stronger economic growth, the Federal Open Market Committee (FOMC) intensified the monetary policy normalization as the FED funds rate corridor was increased several times along 2017-2018. Going forward, we expect at least one more hike of the interest rate before the end of 2018. At the same time, the FED's rate is expected to be increased more gradually along 2019 as a result of increasing inflation and further widening of the positive output gap. The projections also revealed most officials believed interest rates over the long-run should settle around 2,75% or 3%.

**Uncertainty over trade increased.** The U.S. trade deficit widened to 2,9% of GDP in 2017 and we expect it to post a figure of around 3,4% of GDP in 2018. This is a result of imports rise to a record high. Considering the first nine months of the year, the goods and services deficit went up by 10,1%, with exports rising by 8,2% and imports by 8,6%. The U.S. trade deficit increased with all main trading partners except Japan, while the goods trade deficit with China jumped 4,3% to a record high of USD 40,2 bn despite the new tariffs. The long term trade policy of the U.S. remains unclear despite the government having taken a number of measures aiming at limiting imports and narrowing the trade balance deficit. The deal on the new USMCA agreement, which replaced the North American Free Trade Agreement (NAFTA), partly mitigated the risks regarding the country's trade balance. However, the continuing "trade war" with other major partners, especially China, keeps uncertainty about the U.S. external sector and overall economy performance.

**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:

https://raexpert.eu/reports/Press_release_USA_09.11.2018.pdf

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

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