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Ratings

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Andorra

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Andorra

This report does not constitute a rating action.

Key Rating Factors

Sovereign Credit Rating
BBB/Stable/A-2

Institutional and economic profile	Flexibility and performance profile
We expect a solid economic recovery during 2021-2024, following the COVID-19-induced recession in 2020. • After Andorra's economy contracted by 12% in real terms in 2020, we expect the economy to rebound by about 5% in 2021 and to recover in line with the economies of Spain and France. • Andorra's economy remains highly concentrated on financial services, tourism, and commerce, which explains the large pandemic-induced contraction in 2020 and first-quarter 2021. • Andorra is now a member of the IMF, which has fostered greater availability of public statistical data.	***Withdrawal of temporary budgetary measures and economic recovery will drive the reduction in government debt-to-GDP ratio.*** • We anticipate that fiscal consolidation will resume from 2022 and contribute to a decline in the government debt-to-GDP ratio. • We expect the government's temporary budgetary measures to be gradually phased out as the economy recovers. • Our assessment of high contingent liabilities from Andorra's large financial sector constrains the sovereign ratings.

Outlook

The stable outlook on Andorra balances downside risks stemming from the pandemic's economic and budgetary impact with the expectation of an economic rebound over the next two years.

Downside scenario

We could lower the ratings if the pandemic's economic impact is more severe or prolonged than our forecasts, putting Andorra's budgetary position under further pressure. We could also lower the rating if the country's financial sector faced heightened risks, or if the government halts the alignment toward international financial standards or the association agreement with the EU.

Upside scenario

We could raise the ratings if Andorra's budget deficits decline faster than we currently expect. Greater availability of statistical data could support its creditworthiness and prompt us to improve our assessment of Andorra's external position.

Rationale

Our ratings on Andorra are supported by our expectation of an economic rebound following the temporary pandemic-induced economic shock. Moreover, we believe that IMF membership could act as a policy anchor contributing to the country's economic and budgetary resilience. We also expect the authorities will continue to pursue an association agreement with the EU, and will continue efforts for converging with international standards on financial reporting and supervision, which has increased since 2015 after a major financial institution failed.

The lockdown measures during first-quarter 2021 hampered economic growth in Andorra, which reported an economic contraction of 9.3% year-on-year. This was mainly because of the loss of visitors during the winter season and the adverse impact on tourism.

All sectors of Andorra's economy contracted during 2020, except for the construction sector, which posted a marginally positive performance. Overall, GDP in 2020 contracted by 12% in real terms, almost 1% less than our previous estimate. We expect the Andorran economy to rebound by 5% in real terms in 2021 and average a real GDP growth of 1.4% in 2022-2024. Our estimate is based on the economy's large concentration in the services sector, and its close economic relationship with its main trade partners, Spain and France.

Previous strong fiscal surpluses and debt reduction provided the authorities with fiscal headroom to adopt budgetary measures to support the economy throughout the pandemic. This resulted in large fiscal deficits in 2020, and these are also expected for 2021, after tourism activity was severely affected during this year's winter season. Positively, the country has diversified its funding base away from the local market, denoted by Andorra's debut in the international bond markets in 2021 and its membership of the Council of Europe Development Bank.

These credit strengths are counterbalanced by Andorra's relatively large financial sector compared with the size of its economy, with total assets exceeding six times the country's GDP in 2020. This, in our view, indicates high contingent liabilities from the banking sector, which together with the lack of monetary flexibility limits the ratings.

Institutional and economic profile: Following the pandemic-induced recession in 2020, we expect a solid economic recovery during 2021-2024

Andorra's economy remains highly concentrated in services, in particular financial services, tourism, and commerce, which together represent close to 75% of gross value added for the entire economy. In our view, this exacerbated the pandemic's adverse impact, particularly in the first quarter of 2021 where the lockdown measures severely restricted the winter tourist season.

Following the large GDP contraction in 2020, we expect the economy to rebound in 2021 and to reach pre-pandemic GDP levels by 2024, in line with our expectations for its neighbors, Spain and France. These two countries are the source of most visitors to Andorra, and are its main trading partners.

While the 2020 economic contraction has been more severe in Andorra than in Spain or France, these economies remain highly relevant to Andorran economic activity. For example, Spain represents 70% of Andorra's exports and 73% of its imports. We estimate real GDP growth for Andorra of about 5% for 2021, somewhat less than our economic forecast contraction for Spain, at 6.3% real GDP growth. According to our forecast, this will result in GDP per capita for Andorra of about $41,900 this year.

Our expectation on Andorra's economic recovery is, besides the cyclical factors following the contraction, based on the authorities' response to the pandemic. About 40% of the population was fully vaccinated by the end of June 2021, and the health system appears to have ample capacity to respond in case of a spike in the number of positive cases.

Contrary to previous episodes of economic recession, Andorra has not observed an increase in emigration, mainly thanks to the government's implementation of a furlough scheme. Indeed, despite the significant economic contraction, the population in 2020 grew by 0.6%. At the same time, support packages from the government have upheld employment levels until the economy fully opens. We expect the unemployment rate to decrease to 1.99% in 2021 from 2.9% in 2020.

The government has continued to show commitment to its key priorities: opening the economy to foreign investors, and reforming the tax system and financial sector regulations to bring them in line with international standards, which we consider will increase general government revenue and its debt-servicing capacity. Given the high concentration of financial services, tourism, and commerce, the government has been promoting economic diversification, which has resulted in significant growth in foreign direct investments.

We consider that Andorra's recent accession to the IMF will continue to promote alignment of its macroprudential policies with international standards, as well as contributing to the economic resilience against future economic or financial crises by providing a policy anchor and potentially funding support if needed.

In our view, the banking crisis that followed the 2015 Banca Privada d'Andorra (BPA) failure led to an accelerated convergence of the country's banking sector and its regulation and supervision toward international standards, particularly those related to the sovereign's monetary agreement with the EU. We expect this government to continue in negotiations toward an association agreement with the EU.

Andorra was removed from the list of noncooperative tax jurisdictions in 2018, and received the Organization for Economic Co-operation and Development's clearance in 2018 after it concluded that the country's preferential regimes are not harmful tax practices. Furthermore, Andorra ranked 20 out of 191 in the World Bank's "paying taxes" ranking of the most competitive tax regimes in the world, published in mid-2020. Given the ongoing negotiations in the context of the OECD framework for establishing a global minimum corporate tax rate, it appears that the current proposal is unlikely to significantly impact the country's corporate tax framework.

Flexibility and performance profile: Withdrawal of temporary budgetary measures and economic recovery will drive the reduction in government debt-to-GDP ratio

Andorra's solid budgetary position before the onset of the pandemic has allowed the government to cushion its adverse economic impact, thus averting a deeper and longer recession. The temporary removal of the government debt limits imposed by the Fiscal Sustainability Law enabled the government to swiftly implement economic stimulus measures, most of which were in place until June 2021, with targeted support for the most affected sectors extended until the end of the year.

We expect Andorra to resume fiscal consolidation from 2022 on the back of the full withdrawal of temporary budgetary measures and cyclical recovery. This is expected to lead to a gradual reduction in gross government debt from 58% of GDP to slightly over 40% by 2024. At the same time, net general government debt is expected to reduce from negative 14% of GDP in 2021 to negative 19% in 2024.

The government's large liquid financial assets, estimated at 73% of GDP in 2021, have steadily increased in 2021, mainly due to Eurobond issuance. Together with the expected budgetary consolidation, this will help maintain its net asset position over 2021-2024.

In our view, local governments will continue to post fiscal surpluses that will result in a steady reduction in their debt. This is helped by the central government's decision to bear the full burden of the pandemic-related budgetary measures at its level. At the same time, we expect both large public companies, Andorra Telecom and FEDA to remain profitable and continue distributing dividends to the central government. We regard the role of these two companies as auxiliary to the sovereign's plans of energy transition and digital modernization.

The Andorran government continues to diversify its funding sources, which include a €50 million credit facility from the local banks, bond issuance, and multilateral funding. The recent inaugural, sustainable €500 million 10-year Eurobond issuance with a 1.25% coupon is, in our view, contributing to the deepening of Andorra's funding sources, while further reducing its banking system's exposure to the sovereign and allowing the banks to fund the needs of the economy's private sector. Moreover, the Eurobond issuance has contributed to extending the average maturity of its outstanding debt, which was historically lower than that of other European peers.

The large contingent liabilities from Andorra's oversized financial sector considerably constrain our government debt assessment. As of year-end 2020, assets under management represented close to 20x our estimated GDP for 2020. The country's financial system contributes to about 12% of GDP and close to 4% of salaried employment.

Although the financial sector has stabilized following the banking crisis triggered by BPA's collapse in 2015 and subsequent policy actions, future banking crises could have important repercussions for the local economy, which could weigh on the country's budgetary position and lead to debt accumulation. In our view, convergence with international norms and transparency standards should lower the risk from the banking sector, but will test Andorran banks' business models by forcing them to compete more directly with much larger global players.

We view positively nonperforming loans' (NPLs') slight reduction in 2020 to 7.3% (4.4% excluding Vall Banc) from 8.6% (5% excluding Vall Banc) in 2019.

Our view of Andorra's sovereign creditworthiness remains constrained by the country's lack of an independent monetary policy. It has used the euro as its official currency, as part of its monetary agreement with the EU, since 2011. Although Andorra lacks a lender of last resort, we recognize that Andorran banks have indirect access to liquidity from the European Central Bank through its subsidiaries in the eurozone, although we consider this support limited.

Because of a lack of sufficient external data, we evaluate Andorra's external position starting from our view of Spain, the country to which its economy is most closely tied, and then proceed to adjust our view to reflect the lack of data. We understand the Andorran government is actively working to address this deficiency and strengthening the country's statistical services. We believe the statistical transparency will improve given the accession to the IMF and its related technical assistance.

Key Statistics

Table 1

Andorra Selected Indicators

	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Economic indicators (%)										
Nominal GDP (bil. LC)	3	3	3	3	3	3	3	3	3	3
Nominal GDP (bil. $)	3	3	3	3	3	3	3	3	4	4
GDP per capita (000s $)	38.9	39.6	40.1	42.3	40.7	36.8	41.9	44.2	45.2	46.0
Real GDP growth	1.4	3.7	0.3	1.6	1.8	(12)	5.3	5.3	1.9	1.3
Real GDP per capita growth	(0.2)	1.8	(1.9)	(0.3)	0.2	(12.5)	5.9	4.2	0.9	0.3
Real investment growth	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Investment/GDP	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Savings/GDP	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Exports/GDP	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Real exports growth	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Unemployment rate	3.6	3.0	1.8	1.5	1.8	2.9	2.0	1.9	1.8	1.8
External indicators (%)										
Current account balance/GDP	N/A	N/A	N/A	N/A	18.1	N/A	N/A	N/A	N/A	N/A
Current account balance/CARs	N/A	N/A	N/A	N/A	19.2	N/A	N/A	N/A	N/A	N/A
CARs/GDP	N/A	N/A	N/A	N/A	93.9	N/A	N/A	N/A	N/A	N/A
Trade balance/GDP	N/A	N/A	N/A	N/A	(42.7)	N/A	N/A	N/A	N/A	N/A
Net FDI/GDP	N/A	N/A	N/A	N/A	(10.2)	N/A	N/A	N/A	N/A	N/A
Net portfolio equity inflow/GDP	N/A	N/A	N/A	N/A	2.2	N/A	N/A	N/A	N/A	N/A
Gross external financing needs/CARs plus usable reserves	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Narrow net external debt/CARs	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Narrow net external debt/CAPs	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Net external liabilities/CARs	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Net external liabilities/CAPs	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Short-term external debt by remaining maturity/CARs	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Usable reserves/CAPs (months)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Usable reserves (mil. $)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Fiscal indicators (general government; %)										
Balance/GDP	2.5	5.4	4.7	0.7	6.7	1.6	(2.2)	1.7	2.5	2.5
Change in net debt/GDP	(2.2)	(4.7)	(5.7)	(0.3)	(4.7)	3.8	2.2	(1.7)	(2.5)	(2.5)
Primary balance/GDP	3.3	6.0	5.2	1.3	7.2	2.2	(1.6)	2.4	3.0	3.0
Revenue/GDP	22.9	25.0	24.6	21.6	27.2	26.3	21.0	23.8	24.0	24.0
Expenditures/GDP	20.4	19.6	19.9	20.8	20.5	24.7	23.1	22.0	21.5	21.5
Interest/revenues	3.2	2.7	2.2	2.4	1.7	2.1	2.5	2.8	2.2	2.1

Table 1

Andorra Selected Indicators (cont.)										
Debt/GDP	41.0	39.7	37.9	36.4	35.4	46.7	58.7	44.6	42.4	40.4
Debt/revenues	178.8	159.0	154.3	168.5	129.9	177.6	280.1	187.7	176.7	168.5
Net debt/GDP	(4.2)	(8.8)	(14.3)	(14.3)	(18.5)	(17.0)	(13.7)	(14.6)	(16.7)	(18.7)
Liquid assets/GDP	45.2	48.5	52.3	50.6	53.9	63.8	72.4	59.3	59.1	59.1
Monetary indicators (%)										
CPI growth	(1.1)	(0.4)	2.6	1.3	0.8	0.3	1.7	1.1	1.4	1.5
GDP deflator growth	0.7	0.3	1.1	1.0	1.5	1.1	1.7	1.1	1.4	1.5
Exchange rate, year-end (LC/$)	0.92	0.95	0.83	0.87	0.89	0.81	0.83	0.83	0.83	0.83
Banks' claims on resident non-gov't sector growth	(4.0)	(9.2)	(8.6)	(0.3)	0.0	0.0	0.0	0.0	0.0	0.0
Banks' claims on resident non-gov't sector/GDP	190.9	166.5	150.1	145.8	141.0	158.5	148.0	139.0	134.6	130.8
Foreign currency share of claims by banks on residents	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Foreign currency share of residents' bank deposits	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Real effective exchange rate growth	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A

Sources: Department D'Estadistica (Economic Indicators), Autoritat Financera Andorrana, European Central Bank (Monetary Indicators), and Ministry of Finance (Fiscal Indicators).
Adjustments:N/A
Definitions: Savings is defined as investment plus the current account surplus (deficit). Investment is defined as expenditure on capital goods, including plant, equipment, and housing, plus the change in inventories. Banks are other depository corporations other than the central bank, whose liabilities are included in the national definition of broad money. Gross external financing needs are defined as current account payments plus short-term external debt at the end of the prior year plus nonresident deposits at the end of the prior year plus long-term external debt maturing within the year. Narrow net external debt is defined as the stock of foreign and local currency public- and private- sector borrowings from nonresidents minus official reserves minus public-sector liquid claims on nonresidents minus financial-sector loans to, deposits with, or investments in nonresident entities. A negative number indicates net external lending. N/A--Not applicable. LC--Local currency. CARs--Current account receipts. FDI--Foreign direct investment. CAPs--Current account payments. The data and ratios above result 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.

Ratings Score Snapshot

Table 2

Andorra Ratings Score Snapshot

Key rating factors	Score	Explanation
Institutional assessment	3	Generally effective policymaking in recent years promoting sustainable public finances and balanced economic growth as reflected by the government's efforts to complete accession to the IMF and continue negotiations with the EU. Parliament has ensured expedited processes in approving all COVID-19-related government plans.
Economic assessment	2	Based on GDP per capita (US$) and growth trends as per Selected Indicators in Table 1.
		Volatile and concentrated economy in the financial sector that represents around one-third of economic activity.
External assessment	5	The sovereign has limited external data. We therefore assign an initial assessment that is the same as the initial assessment that we could apply to Spain.
		The sovereign's external data lack consistency, as there is lack of reliable and sufficient external accounts information.
Fiscal assessment: flexibility and performance	1	Based on the change in net general government debt (% of GDP) as per Selected Indicators in Table 1.
		Based on liquid assets/GDP, which are greater than 50%, as per Selected Indicators in Table 1.

Table 2

Andorra Ratings Score Snapshot (cont.)		
Fiscal assessment: debt burden	3	Based on net general government debt (% of GDP) and general government interest expenditure (% of general government revenue) as per Selected Indicators in Table 1.
		Contingent liabilities are high. The size of Andorra's banking sector is large--total assets under management stood at 20x GDP in 2020, when considering off-balance-sheet assets under management.
Monetary assessment	5	The euro is a reserve currency. Consumer price index is as per Selected Indicators in Table 1.
		The central bank has the ability to act as lender of last resort for the financial system. No monetary flexibility, but inflation is under control.
Indicative rating	bbb+	
Notches of supplemental adjustments and flexibility	(1)	The notch of flexibility down captures additional factors that have an impact on creditworthiness and are not fully reflected in the indicative rating. Mainly, uncertainties around the economic recovery after the impact of the COVID-19 pandemic.
Final rating		
Foreign currency	BBB	
Notches of uplift	0	Default risks do not apply differently to foreign and local currency debt.
Local currency	BBB	

S&P Global Ratings' analysis of sovereign creditworthiness rests on its assessment and scoring of five key rating factors: (i) institutional assessment; (ii) economic assessment; (iii) external assessment; (iv) the average of fiscal flexibility and performance, and debt burden; and (v) monetary assessment. Each of the factors is assessed on a continuum spanning from 1 (strongest) to 6 (weakest). S&P Global Ratings' "Sovereign Rating Methodology," published on Dec. 18, 2017, details how we derive and combine the scores and then derive the sovereign foreign currency rating. In accordance with S&P Global Ratings' sovereign ratings methodology, a change in score does not in all cases lead to a change in the rating, nor is a change in the rating necessarily predicated on changes in one or more of the scores. In determining the final rating the committee can make use of the flexibility afforded by §15 and §§126-128 of the rating methodology.

Related Criteria

- Criteria | Governments | Sovereigns: Sovereign Rating Methodology, Dec. 18, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011
- General Criteria: Methodology: Criteria For Determining Transfer And Convertibility Assessments, May 18, 2009

Related Research

- Sovereign Risk Indicators, July 12, 2021; a free interactive version is available at http://www.spratings.com/sri
- Sovereign Ratings List, June 9, 2021
- Sovereign Ratings History, June 9, 2021
- Default, Transition, and Recovery: 2020 Annual Sovereign Default And Rating Transition Study, April 12, 2021

Ratings Detail (As Of July 19, 2021)*	
Andorra	
Sovereign Credit Rating	BBB/Stable/A-2
Transfer & Convertibility Assessment	AAA
Senior Unsecured	BBB

Ratings Detail (As Of July 19, 2021)*(cont.)	
Sovereign Credit Ratings History	
24-Apr-2020	BBB/Stable/A-2
19-Jul-2019	BBB/Positive/A-2
28-Jul-2017	BBB/Stable/A-2
29-Jul-2016	BBB-/Stable/A-3

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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