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Research Update:

Principality of Liechtenstein 'AAA/A-1+' Ratings Affirmed; Outlook Stable; Off Watch Neg

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Overview

- We have reviewed our ratings on Liechtenstein, after placing them on CreditWatch with negative implications (CWN) on Feb. 12, 2016.
- We have concluded that Liechtenstein will be able to cope with complex regulatory challenges in the coming years, while maintaining high wealth levels and debt-free public accounts.
- We are thus affirming our 'AAA/A-1+' long- and short-term sovereign credit ratings on Liechtenstein and removing the ratings from CreditWatch negative.
- The stable outlook signals that we see less than a one-in-three probability that we will lower the long-term rating within the next two years, given the country's strong fundamentals and its demonstrated proactive policymaking.

Rating Action

On Feb. 26, 2016, Standard & Poor's Ratings Services affirmed its 'AAA/A-1+' long- and short-term sovereign credit ratings on the Principality of Liechtenstein and removed them from CreditWatch, where they had been placed on Feb. 12, 2016, with negative implications. The outlook is stable.

As a "sovereign rating" (as defined in EU CRA Regulation 1060/2009 "EU CRA Regulation"), the ratings on Liechtenstein are subject to certain publication restrictions set out in Art 8a of the EU CRA Regulation, including publication in accordance with a pre-established calendar (see "Calendar Of 2016 EMEA Sovereign, Regional, And Local Government Rating Publication Dates," published Dec. 22, 2015, on RatingsDirect). Under the EU CRA Regulation, deviations from the announced calendar are allowed only in limited circumstances and must be accompanied by a detailed explanation of the reasons for the deviation. In this case, the reason for the deviation is the resolution of the CreditWatch, where the ratings had been placed on February 12. The next scheduled rating publication on the sovereign rating of Liechtenstein will be on July 29, 2016.

Rationale

The affirmation reflects Liechtenstein's strong fiscal position and wealthy economy, as well as our assumptions about the ability of policymakers to face international regulatory and political challenges to the country's economic model.

Liechtenstein's fiscal accounts are in a structural surplus. The central government is free of debt and the general government has negligible debt. We expect the general government will achieve an average surplus of nearly 3% of GDP over 2016-2019. This reflects the government's successful consolidation efforts in recent years and sound social security balances. The government will be examining ways to strength its social security system even further in its 2016 agenda. The general government's fiscal assets, including social security, totaled nearly 100% of GDP at year-end 2014. The public employees' pension system holds additional assets totaling 20% of GDP. We note that a large majority of these public-sector fiscal assets are either denominated in Swiss francs or hedged. Given our projection of budgetary surpluses, we do not expect Liechtenstein will tap capital market debt over the coming years and thus think that the government's net asset position relative to GDP will increase, albeit with some downside valuation risks due to currency and equity market movements.

We estimate Liechtenstein's per capita GDP will be $135,000 in 2016, making it one of the highest in the world. Even taking into account the impact of nonresident workers--about one-half of all employees, mostly residing in neighboring Switzerland, Austria, and Germany--per capita income still remains very high, which makes Liechtenstein one of the wealthiest nations in the world and underlines the robustness of its labor market.

That said, Liechtenstein's economy is volatile, which is to be expected of an open economy with a population of 37,000. The economy contracted by 16% in 2009 during the Great Recession, for example. Economic growth in Liechtenstein relies predominantly on the industrial and financial sectors. Industry is the largest sector, contributing about 40% to gross value added (GVA), and is made up of a few relatively large industrial companies that are niche players in global markets, such as Hilti and ThyssenKrupp Presta, and a high number of small and midsize enterprises. We expect slow real GDP growth in 2016 at just over 1%, rising to 2% in 2017-2019. Since 2008, Liechtenstein's economy has been coping with a strong Swiss franc, which has appreciated nearly 20% in real effective terms over the past five years and experienced a significant appreciation against the euro since Jan. 15, 2015, when the Swiss National Bank (SNB, the Swiss central bank) abandoned its franc/euro floor. The principality's fourth-quarter 2015 business survey indicates that Liechtenstein's business leaders are confident in their prospects. Liechtenstein modified its financial statistics last year and reported revised financial data (for 2011-2013), albeit with a time lag, based on European System of Accounts 1995 methodology (ESA95).

Liechtenstein's low-tax regime, banking secrecy, and its stable political environment have supported the development of a large financial services sector, which contributed about 24% of GVA in 2012. Although we do not view the financial industry as monolithic--it consists of regional banks, asset managers, insurance companies, and trusts--we consider the sector poses a moderate contingent liability for the government. For example, domestic credit to GDP exceeded 250% in 2015, and the financial system's assets under management are 40 times Liechtenstein's GDP. However, the banks are well capitalized and well funded, and the reputation of asset managers is unblemished. We rank Liechtenstein in group '2' under our Banking Industry Country Risk Assessment (BICRA; scores range from '1' to '10', with the lowest-risk banking systems in group '1' and the highest-risk in group '10').

Given the size of its financial system and its international orientation, Liechtenstein is exposed to changes in international norms for financial regulation and fiscal cross-border cooperation. Our affirmation expresses our view that

Liechtenstein will rise to the challenge, as it has in the past, thanks to the effectiveness of its institutions. We see the government as having proactively addressed some of these risks by adopting international standards in a timely manner and by meeting the demands of international regulators, for instance via anti-money-laundering legislation and its willingness to exchange tax information with other jurisdictions automatically (for example, with the EU as of January 2016 and with the U.S. as of January 2015). In recent years, Liechtenstein has amended several double-taxation agreements and signed new tax-information-exchange agreements with other countries. Such agreements allow for the exchange of tax information or the payment of withholding taxes to foreign tax authorities.

We expect that policymaking will remain consensual in the run-up to the 2017 legislative elections. In that regard, we note that Liechtenstein is a hereditary monarchy under a constitution with sovereign powers jointly exercised by the prince and the people. Although the prince has extensive powers--unlike those in ceremonial monarchies--granted by the constitution, that same constitution contains checks and balances between the prince and parliament. One of the most effective checks is provided by the extensive use of direct democracy (plebiscites) in the principality.

Liechtenstein is in a monetary union with Switzerland, although the principality has no vote on the SNB's monetary policy council and receives no benefit from seigniorage. Being the junior member in this monetary union reduces Liechtenstein's monetary flexibility. The monetary union is based on a 1980 currency treaty, which establishes the Swiss franc as legal tender for the principality. The treaty also provides Liechtenstein's three-largest banks (although not its other banks) access to SNB liquidity facilities against eligible collateral on par with any Swiss financial institution. We do not expect, however, that the SNB would act as a lender of last resort to Liechtenstein's banks.

We find that the 1980 currency treaty anchors Liechtenstein's economy and strengthens its economic links with Switzerland. We do not think the monetary union, and in particular last year's sharp nominal appreciation of the franc, will disproportionately affect Liechtenstein's economic development vis-à-vis that of Switzerland, given the two countries' similar economic structures.

The affirmation also takes into consideration the lack of data for external accounts. There is only limited data available for external trade, balance of payments, and the international investment position. In line with our criteria, we therefore base our assessment of Liechtenstein's external position on that of the Swiss Confederation. That is, we define Switzerland as the "host country" and use Switzerland's external position as a starting point. We then adjust the initial assessment downward for the lack of external data because these data gaps reduce the visibility of external risks. That said, Liechtenstein's large net asset position and its local banks' predominant business model as asset managers would otherwise suggest a strong external position.

Outlook

The stable outlook incorporates our assessment of the ability of policymakers to adapt to a changing international environment on the tax and financial services fronts. We expect that Liechtenstein's industrial and financial sectors will maintain their vitality and thus the strong tax base for the economy, notwithstanding the changing environment and competiveness challenges of a strong currency.

Downward pressure on Liechtenstein's ratings could emerge if our assumptions about Liechtenstein's economic vitality no longer held. A change in our BICRA assessment, for example, could be a harbinger of pressure on the sovereign's creditworthiness. Loss of market share of the asset managers or financial distress at one of Liechtenstein's major corporations could be another. If the international tax or financial regulations became especially hostile to financial centers, many jurisdictions would come under rating pressure and Liechtenstein would be among them. However, we do not expect such a destabilizing occurrence within the next two years.

Key Statistics

Table 1

Principality of Liechtenstein Selected Indicators

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
ECONOMIC INDICATORS (%)										
Nominal GDP (bil. CHF)	5	5	5	5	5	5	5	5	5	6
Nominal GDP (bil. $)	5	6	5	6	6	5	5	5	5	5
GDP per capita (000s $)	140.6	157.4	148.1	154.1	154.3	141.4	135.4	131.4	132.8	134.3
Real GDP growth	9.6	(3.5)	0.9	4.6	0.3	0.8	1.1	1.9	2.1	2.1
Real GDP per capita growth	8.8	(4.3)	(0.1)	3.7	(0.3)	0.0	0.3	1.1	1.3	1.3
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	62.7	65.3	65.8	63.4	65.4	61.0	60.6	60.1	59.0	57.9
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	2.6	2.3	2.4	2.5	2.4	2.4	2.4	2.4	2.4	2.4
EXTERNAL INDICATORS (%)										
Current account balance/GDP	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Current account balance/CARs	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Trade balance/GDP	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Net FDI/GDP	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Net portfolio equity inflow/GDP	N/A	N/A	N/A	N/A	N/A	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
Net external liabilities/CARs	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A

Table 1

Principality of Liechtenstein Selected Indicators (cont.)

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
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
Reserves/CAPs (months)	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	0.3	2.4	(2.4)	(1.1)	3.9	1.1	2.6	2.4	3.3	3.4
Change in debt/GDP	0.0	0.4	0.2	(0.1)	(0.1)	(0.1)	(0.1)	(0.0)	(0.1)	(0.0)
Primary balance/GDP	0.3	2.4	(2.4)	(1.1)	3.9	1.1	2.6	2.4	3.3	3.4
Revenue/GDP	24.3	33.8	34.4	29.0	29.0	29.0	29.0	29.0	29.0	29.0
Expenditures/GDP	23.9	31.4	36.8	30.2	25.1	27.9	26.4	26.6	25.7	25.6
Interest /revenues	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Debt/GDP	0.0	0.4	0.6	0.5	0.5	0.3	0.2	0.2	0.1	0.1
Net debt/GDP	(88.9)	(92.9)	(99.2)	(102.6)	(97.6)	(97.7)	(97.7)	(97.9)	(96.8)	(95.6)
Liquid assets/GDP	88.9	93.4	99.9	103.1	98.0	98.0	97.9	98.1	96.9	95.7
MONETARY INDICATORS (%)										
CPI growth	0.7	0.2	(0.7)	(0.2)	(0.0)	(1.1)	(0.3)	0.4	0.7	0.7
GDP deflator growth	(1.3)	(0.4)	(0.5)	(0.9)	(0.7)	(1.0)	(0.4)	(1.2)	(0.2)	(0.2)
Banks' claims on resident non-gov't sector growth	5.8	2.5	(7.7)	1.6	8.0	0.0	1.0	1.0	1.0	1.0
Banks' claims on resident non-gov't sector/GDP	245.5	261.6	240.7	235.9	255.8	256.3	257.1	257.8	255.5	253.3
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

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 assets held by nonresidents minus financial-sector loans to, deposits with, or investments in nonresident entities. A negative number indicates net external lending. CHF--Swiss franc. CARs--Current account receipts. FDI--Foreign direct investment. CAPs--Current account payments. N/A--Not available. The data and ratios above result from Standard & Poor's own calculations, drawing on national as well as international sources, reflecting Standard & Poor's independent view on the timeliness, coverage, accuracy, credibility, and usability of available information.

Ratings Score Snapshot

Table 2

Principality of Liechtenstein Ratings Score Snapshot

Key rating factors	
Institutional assessment	Strength
Economic assessment	Strength
External assessment	Neutral
Fiscal assessment: flexibility and performance	Strength
Fiscal assessment: debt burden	Strength
Monetary assessment	Neutral

Standard & Poor's 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). Section V.B of Standard & Poor's "Sovereign Rating Methodology," published on Dec. 23, 2014, summarizes how the various factors are combined to derive the sovereign foreign currency rating, while section V.C details how the scores are derived. The ratings score snapshot summarizes whether we consider that the individual rating factors listed in our methodology constitute a strength or a weakness to the sovereign credit profile, or whether we consider them to be neutral. The concepts of "strength", "neutral", or "weakness" are absolute, rather than in relation to sovereigns in a given rating category. Therefore, highly rated sovereigns will typically display more strengths, and lower rated sovereigns more weaknesses. In accordance with Standard & Poor's sovereign ratings methodology, a change in assessment of the aforementioned factors 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 assessments.

Related Criteria And Research

Related Criteria

- Criteria - Governments - Sovereigns: Sovereign Rating Methodology - December 23, 2014
- General Criteria: Methodology For Linking Short-Term And Long-Term Ratings For Corporate, Insurance, And Sovereign Issuers - May 07, 2013
- General Criteria: Methodology: Criteria For Determining Transfer And Convertibility Assessments - May 18, 2009

Related Research

- Global Sovereign Rating Trends 2016, Jan. 6, 2016
- Sovereign Risk Indicators, Dec. 14, 2015. An interactive version is also available at http://www.spratings.com/sri.
- Default, Transition, and Recovery: 2014 Annual Sovereign Default Study And Rating Transitions, May 18, 2015
- Banking Industry Country Risk Assessment: Liechtenstein, Nov. 13, 2015
- Bulletin: Switzerland Ratings And BICRA Unaffected By Swiss National Bank's Change In Exchange Rate Policy, Jan. 15, 2015

In accordance with our relevant policies and procedures, the Rating Committee was composed of analysts that are qualified to vote in the committee, with sufficient experience to convey the appropriate level of knowledge and understanding of the methodology applicable (see 'Related Criteria And Research'). At the onset of the committee, the chair confirmed that the information provided to the Rating Committee by the primary analyst had been distributed in a timely manner and was sufficient for Committee members to make an informed decision.

After the primary analyst gave opening remarks and explained the recommendation, the Committee discussed key rating factors and critical issues in accordance with the relevant criteria. Qualitative and quantitative risk factors were considered and discussed, looking at track-record and forecasts.

The committee agreed that all key rating factors were unchanged.

The chair ensured every voting member was given the opportunity to articulate his/her opinion. The chair or designee reviewed the draft report to ensure consistency with the Committee decision. The views and the decision of the rating committee are summarized in the above rationale and outlook. The weighting of all rating factors is described in the methodology used in this rating action (see 'Related Criteria and Research').

Ratings List

	Rating	
	To	From
Liechtenstein (Principality of)		
Sovereign Credit Rating		
Foreign and Local Currency	AAA/Stable/A-1+	AAA/Watch Neg/A-1+
Transfer & Convertibility Assessment	AAA	AAA

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information.

Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com and at spcapitaliq.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following Standard & Poor's numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.

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