

Federal Republic of Germany

Rating report

Rating rationale

Wealthy, large, diversified economy: Germany's economy proved resilient during the Covid-19 pandemic and the energy crisis. However, the country's high value-added, export-oriented, energy imports-dependent economy has been slow to recover compared with peer countries due to global supply chain disruptions and sharply higher inflation following the escalation of the Russia-Ukraine war. After a decline in economic output of 0.3% last year, we expect stagnant growth in 2024 of 0.2%, with the recovery delayed until 2025 when GDP is expected to grow 1.4%.

Robust fiscal framework: Germany's solid fiscal policy framework and strong record of fiscal discipline are anchored by its constitutional debt brake. The constitutional court's ruling on the federal supplementary budget of 2021 and its strict interpretation of debt-brake borrowing limitations have reinforced the country's rigid fiscal rules. We expect the debt-to-GDP ratio to fall to 63% this year and gradually decline to 59% by 2028.

Highly competitive external sector: The economy's external strength is reflected in its large and persistent current account surplus. This declined in 2022 due to the sharp rise in energy import prices and weaker external demand from key trading partners but recovered in 2023. The surplus is expected to remain slightly below pre-pandemic levels in the medium term.

Rating challenges include: i) transition risks for energy-intensive industries given carbon neutrality targets and low levels of public and private sector investment relative to peers; ii) an ageing population, resulting in rising pension liabilities and downward pressure on the country's medium-term growth potential; and iii) vulnerabilities related to global geopolitical risks.

Figure 1: Germany's sovereign rating drivers

| Risk pillars | | Quantitative | | Reserve currency* | Political risk** | Qualitative *** | Final rating |
|-------------------------------------|-----------------------|--------------|-------------------|-------------------|------------------|-----------------|--------------|
| | | Weight | Indicative rating | Notches | Notches | Notches | |
| Domestic economic risk | | 35% | aaa | EUR | Germany | - 1/3 | AAA |
| Public finance risk | | 20% | aa- | | | 1/3 | |
| External economic risk | | 10% | aaa | | | 2/3 | |
| Financial stability risk | | 10% | aaa | | | 1/3 | |
| ESG risk | Environmental factors | 5% | bbb+ | [+1] | [-0] | - 1/3 | |
| | Social factors | 7.5% | b- | | | 0 | |
| | Governance factors | 12.5% | aaa | | | 0 | |
| Sovereign Quantitative Model | | aaa | | | | +1 | |
| Additional considerations | | | | | | 0 | |

*The reserve-currency quantitative adjustment applies to currencies in the IMF's Special Drawing Rights (SDR) basket.

**The political-risk quantitative adjustment is based on the World Bank's Political Stability & Absence of Violence/Terrorism index.

***The qualitative scorecard analyst adjustments, capped at one notch per rating pillar, are weighted equally with an aggregate adjustment rounded to the nearest integer. For details, please see Scope's [Sovereign Rating Methodology](#). Source: Scope Ratings.

Foreign currency

Long-term issuer rating/Outlook

AAA/Stable

Senior unsecured debt

AAA/Stable

Short-term issuer rating/Outlook

S-1+/Stable

Local currency

Long-term issuer rating/Outlook

AAA/Stable

Senior unsecured debt

AAA/Stable

Short-term issuer rating/Outlook

S-1+/Stable

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Credit strengths and challenges

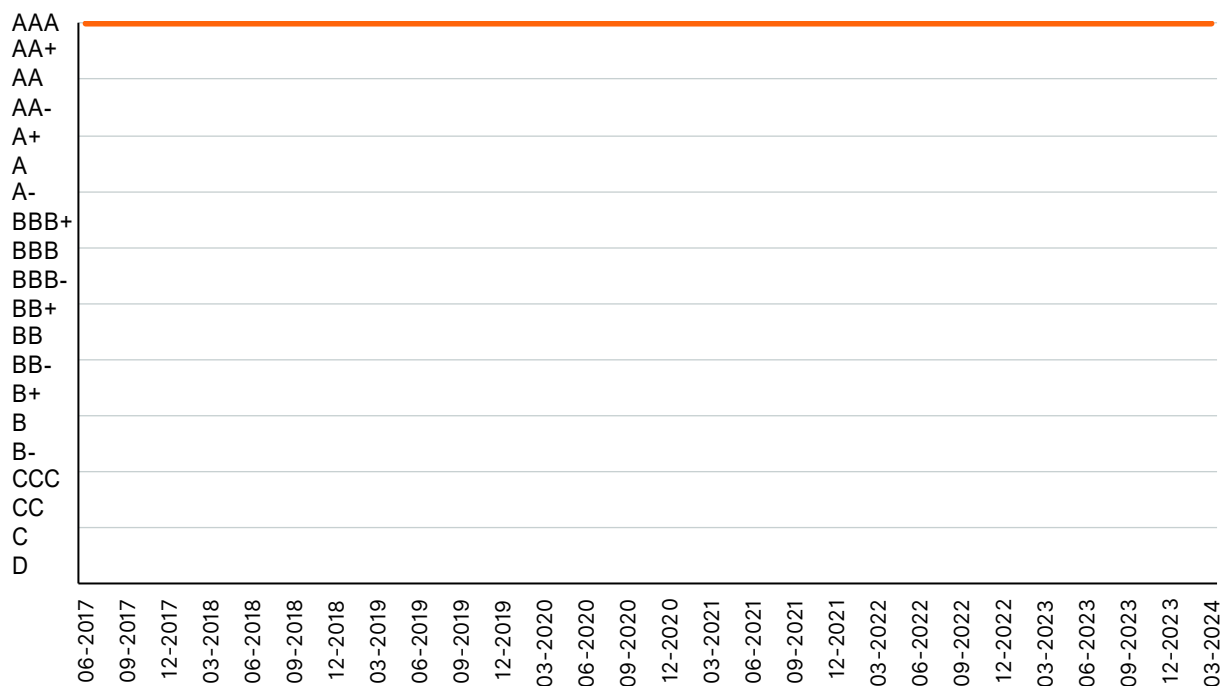
| Credit strengths | Credit challenges |
|---|--|
| <ul style="list-style-type: none"> Wealthy, large, diversified economy Robust fiscal framework and strong track record of fiscal discipline Highly competitive external sector | <ul style="list-style-type: none"> Transition risks for energy-intensive industries, and low levels of public and private sector investment Ageing population, resulting in rising pension liabilities and lower growth potential Vulnerabilities related to global geopolitical risk |

Outlook and rating triggers

The Stable Outlook reflects Scope’s view that risks to the ratings are balanced.

| Positive rating-change drivers | Negative rating-change drivers |
|---|---|
| <ul style="list-style-type: none"> N/A | <ul style="list-style-type: none"> Fiscal deterioration, resulting in a material increase in public debt Severe macroeconomic or financial system shock, resulting in a weaker growth outlook |

Figure 2: Rating history¹



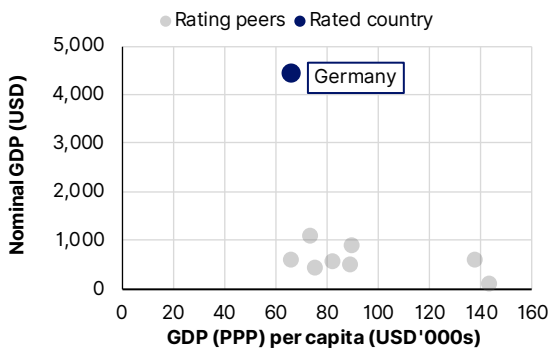
¹Foreign-currency long-term issuer rating. Positive/Negative Outlooks are treated with a +/-0.33-notch adjustment. Credit Watch positive/negative with a +/-0.67-notch adjustment. Source: Scope Ratings.

Domestic economic risk

Overview of Scope's assessments of Germany's Domestic Economic Risk

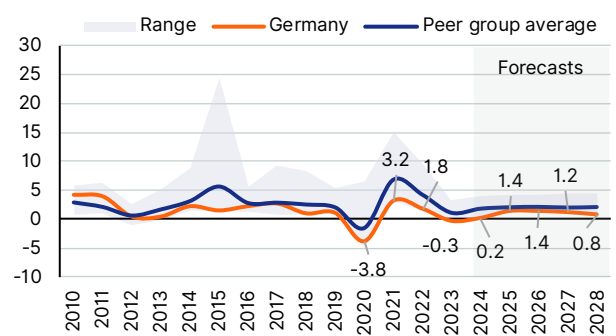
| SQM* indicative rating | Analytical component | Assessment | Notch adjustment | Rationale |
|------------------------|--|------------|------------------|--|
| aaa | Growth potential and outlook | Weak | -1/3 | Weak growth potential reflecting demographic challenges, a large investment gap and structural challenges in key industries |
| | Monetary policy framework | Neutral | 0 | ECB is a highly credible and effective central bank; effective policy framework and transmission over the cycle |
| | Macroeconomic stability and sustainability | Neutral | 0 | Competitive and diversified economy but weaknesses in digitalisation, labour market challenges related to ageing; high resource dependence and trade linkages with other countries |

Figure 3: Nominal GDP and GDP per capita



Source: IMF World Economic Outlook (WEO), Scope Ratings

Figure 4: Real GDP growth, %



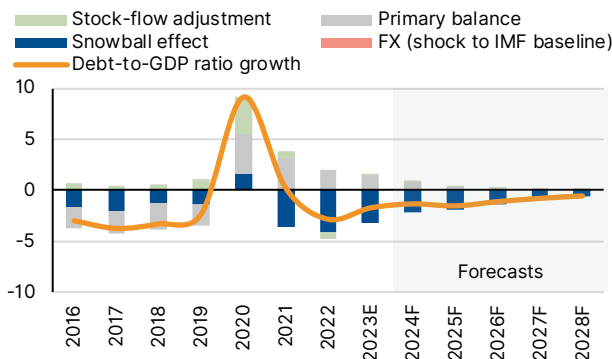
Source: IMF WEO, Scope Ratings forecasts

Public finance risk

Overview of Scope's assessments of Germany's Public Finance Risk

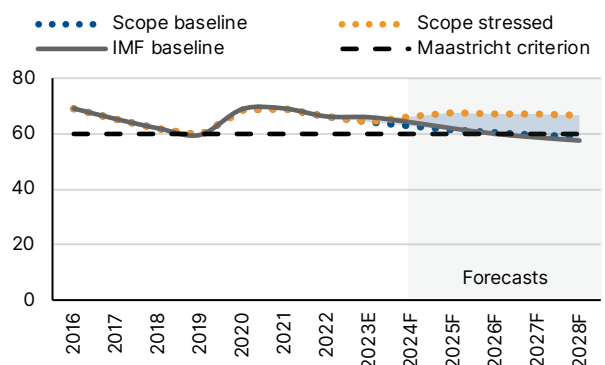
| SQM indicative rating | Analytical component | Assessment | Notch adjustment | Rationale |
|-----------------------|--------------------------------|------------|------------------|--|
| aa- | Fiscal policy framework | Neutral | 0 | Strong policy response to energy crisis; constitutionally anchored debt brake at federal and regional level that was reinforced by the constitutional court's ruling |
| | Long-term debt trajectory | Neutral | 0 | Moderate public debt with high resilience to adverse scenarios; rising pension liabilities |
| | Debt profile and market access | Strong | +1/3 | Primary benchmark issuer in euro area, reflected in low interest payments despite heightened debt levels |

Figure 5: Contributions to change in debt levels, pps of GDP



Source: IMF WEO, Scope Ratings forecasts

Figure 6: Debt-to-GDP forecasts, % of GDP



Source: IMF WEO, Scope Ratings forecasts

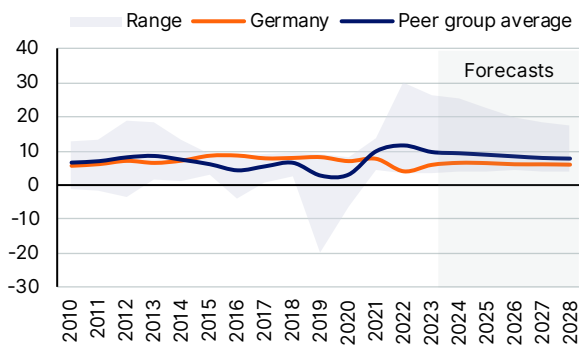
*Sovereign Quantitative Model.

External economic risk

Overview of Scope's assessments of Germany's External Economic Risk

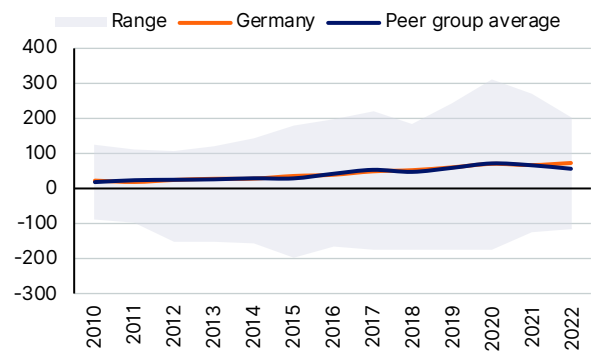
| SQM indicative rating | Analytical component | Assessment | Notch adjustment | Rationale |
|-----------------------|--|------------|------------------|---|
| aaa | Current account resilience | Strong | +1/3 | Diversified and competitive export base; strong track record of current account surpluses |
| | External debt structure | Neutral | 0 | Moderate external debt |
| | Resilience to short-term external shocks | Strong | +1/3 | Benefits from euro area membership; large external-creditor position |

Figure 7: Current-account balance, % of GDP



Source: IMF WEO forecasts, Scope Ratings

Figure 8: Net international investment position (NIIP), % GDP



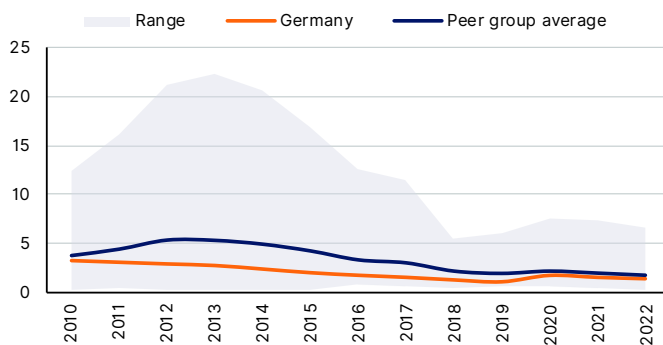
Source: IMF, Scope Ratings

Financial stability risk

Overview of Scope's assessments of Germany's Financial Stability Risk

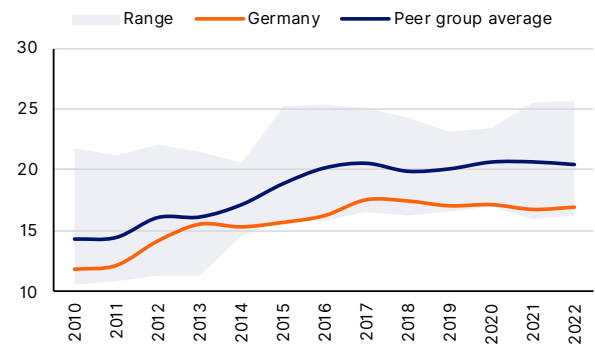
| SQM indicative rating | Analytical component | Assessment | Notch adjustment | Rationale |
|-----------------------|---|------------|------------------|--|
| aaa | Banking sector performance | Neutral | 0 | Low return on equity and unfavourable cost structure of banking sector balanced by adequate capitalisation and moderate exposure risk to nonfinancial corporate debt |
| | Financial sector oversight and governance | Neutral | 0 | Oversight under National Supervisory Authority and ECB as part of banking union |
| | Financial imbalances | Strong | +1/3 | Moderate household and private sector indebtedness; closely monitored systemic risks in financial system |

Figure 9: Non-performing loans (NPLs), % of total loans



Source: World Bank (WB), Scope Ratings

Figure 10: Tier 1 capital, % of risk-weighted assets



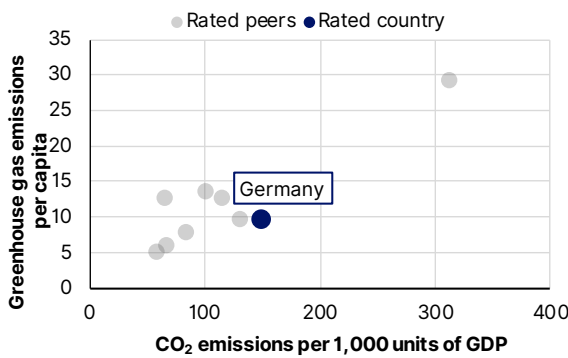
Source: IMF, Scope Ratings

Environmental, Social and Governance (ESG) risk

Overview of Scope's assessments of Germany's ESG Risk

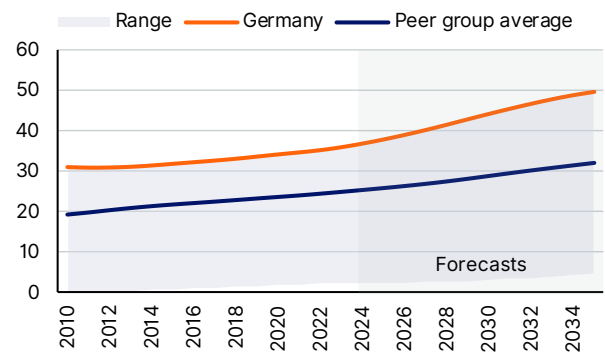
| SQM indicative rating | Analytical component | Assessment | Notch adjustment | Rationale |
|-----------------------|-----------------------|------------|------------------|---|
| aa- | Environmental factors | Weak | -1/3 | Structural challenges related to transition risk in view of carbon neutrality targets and economic importance of energy-intensive key industries |
| | Social factors | Neutral | 0 | Weak demographics given an ageing workforce, balanced by high social inclusion and improving labour force participation; rising inequality risks, reinforced by the Covid-19 pandemic and energy crises |
| | Governance factors | Neutral | 0 | High-quality institutions and stable political environment |

Figure 11: CO₂ emissions per GDP, mtCO₂e



Source: European Commission (EC), Scope Ratings

Figure 12: Old-age dependency ratio, %



Source: United Nations (UN), Scope Ratings

Reserve-currency adjustment

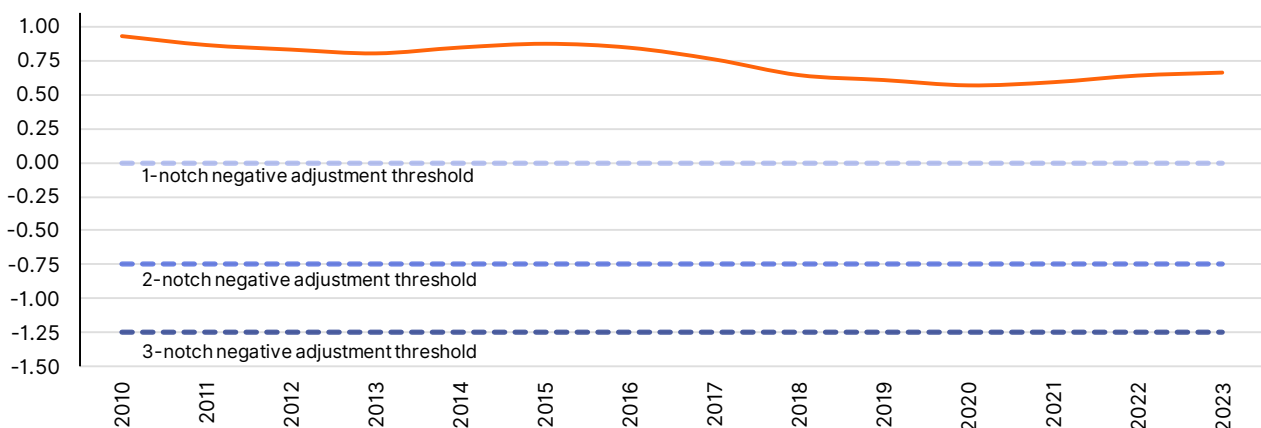
Figure 13: IMF SDR basket and Scope reserve-currency adjustment

| Currency | U.S. dollar | Euro | Chinese yuan | Japanese yen | Pound sterling | Other |
|------------------------------|-------------|-------------|--------------|--------------|----------------|-------|
| IMF SDR basket weights, % | 43.4 | 29.3 | 12.3 | 7.6 | 7.4 | 0.0 |
| Positive adjustment, notches | 3 | 1 | 1 | 1 | 1 | 0 |

Source: IMF, Scope Ratings

Political-risk adjustment

Figure 14: WB Political Stability & Absence of Violence/Terrorism index, Germany, 3-year moving average



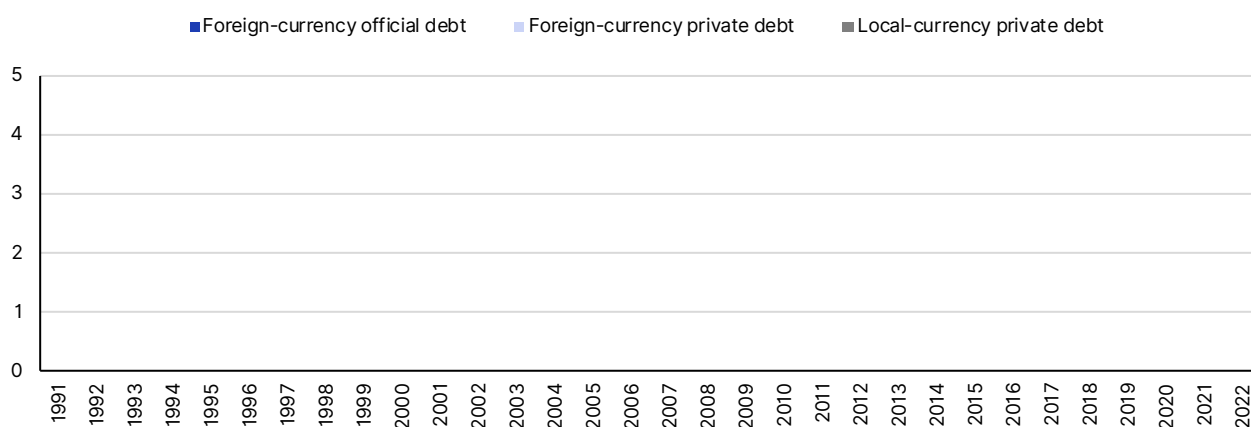
Source: WB, Scope Ratings

Additional considerations

No adjustment was applied to the rating from additional considerations.

Appendix I. Sovereign default history

Figure 15: Sovereign default history, USD m



Depicted private-debt defaults may not always constitute a credit event under [Scope's credit-rating definitions](#).
 Source: [Bank of Canada-Bank of England Sovereign Default Database](#), Scope Ratings.

Appendix II. Rating peers

Rating peers are related to sovereigns with an indicative rating in the same rating category or adjacent categories, as assigned by Scope's sovereign quantitative model after accounting for methodological reserve-currency and political-risk adjustments.

| Peer group* |
|-------------|
| Denmark |
| Luxembourg |
| Netherlands |
| Norway |
| Sweden |
| Switzerland |

*Select publicly-rated sovereigns only; the full sample of sovereign-rating peers may be larger.

Appendix III. Economic development and default indicators

| | |
|---|------------------|
| IMF Development Classification | Advanced economy |
| 5y USD CDS spread (bp) as of 7 April 2024 | 10.1 |

Appendix IV. Statistical table for selected SQM indicators

This table presents a selection of the indicators (24 out of 30 – with the governance indicator reflecting a composite of five indicators) used in Scope's quantitative model, in line with Scope's Sovereign Rating Methodology. The metrics and sources for the data presented here ensure comparability across global country peers and may therefore differ from data from national and other select international statistical series.

| Pillar | Core variable | Source | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 |
|---------------------|---|--------|-------|-------|-------|-------|-------|-------|
| Domestic Economic | GDP per capita (PPP), USD '000s | IMF | 55.0 | 56.5 | 55.0 | 59.3 | 64.1 | 66.0 |
| | Nominal GDP, USD bn | IMF | 3,976 | 3,890 | 3,885 | 4,281 | 4,086 | 4,430 |
| | Real growth, % | IMF | 1.0 | 1.1 | -3.8 | 3.2 | 1.8 | -0.5 |
| | CPI inflation, % | IMF | 1.9 | 1.4 | 0.4 | 3.2 | 8.7 | 6.3 |
| | Unemployment rate, % | WB | 3.4 | 3.1 | 3.9 | 3.6 | 3.0 | - |
| Public Finance | Public debt, % of GDP | IMF | 61.9 | 59.5 | 68.7 | 69.0 | 66.1 | 65.9 |
| | Net interest payment, % of government revenue | IMF | 1.6 | 1.3 | 1.0 | 0.9 | 1.2 | 1.7 |
| | Primary balance, % of GDP | IMF | 2.7 | 2.1 | -3.9 | -3.1 | -1.9 | -2.1 |
| External Economic | Current-account balance, % of GDP | IMF | 8.0 | 8.2 | 7.1 | 7.7 | 4.2 | 6.0 |
| | Total reserves, months of imports | WB | 1.3 | 1.5 | 2.0 | 1.8 | 1.7 | - |
| | NIIP, % of GDP | IMF | 50.7 | 58.7 | 68.5 | 65.1 | 71.0 | - |
| Financial Stability | NPL ratio, % of total loans | IMF | 1.2 | 1.1 | 1.7 | 1.5 | 1.4 | - |
| | Tier 1 ratio, % of risk-weighted assets | IMF | 17.5 | 17.1 | 17.2 | 16.8 | 17.0 | 17.2 |
| | Credit to the private sector, % of GDP | WB | 78.2 | 79.4 | 85.0 | 84.2 | 83.4 | - |
| ESG | CO ₂ per EUR 1,000 of GDP, mtCO ₂ e | EC | 168.1 | 154.9 | 147.9 | 153.5 | 149.6 | - |
| | Income share of bottom 50%, % | WID | 18.3 | 16.8 | 17.2 | 19.2 | 19.3 | - |
| | Labour-force participation rate, % | WB | 79.1 | 80.1 | 78.8 | 78.9 | - | - |
| | Old-age dependency ratio, % | UN | 33.1 | 33.6 | 34.2 | 34.7 | 35.2 | 36.0 |
| | Composite governance indicators* | WB | 1.6 | 1.6 | 1.5 | 1.5 | 1.5 | - |
| | Political stability, index | WB | 0.6 | 0.5 | 0.6 | 0.7 | 0.6 | - |

*Average of the following five World Bank Worldwide Governance Indicators: *Control of Corruption, Voice and Accountability, Rule of Law, Government Effectiveness, Regulatory Quality*.

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