

RATING ACTION COMMENTARY

Fitch Affirms Andorra at 'A-'; Outlook Stable

Fri 04 Apr, 2025 - 5:00 PM ET

Fitch Ratings - Frankfurt am Main - 04 Apr 2025: Fitch Ratings has affirmed Andorra's Long-Term Foreign-Currency Issuer Default Rating (IDR) at 'A-' with a Stable Outlook.

A full list of rating actions is at the end of this rating action commentary.

KEY RATING DRIVERS

Strong Structural Fundamentals: Andorra's credit profile is supported by GDP per capita and governance indicators that exceed the median for 'A' category peers. A prudent fiscal framework has maintained fiscal and macroeconomic stability despite external challenges. Significant financial buffers and a public debt-to-GDP ratio below the 'A' category median further support the rating. These strengths are counterbalanced by Andorra's small economy and limited diversification. The large banking sector also exposes the economy and government balance sheet to potential vulnerabilities in the event of a severe adverse shock.

Economic Resilience: Andorra's economy grew by 3.4% in 2024, following a 2.6% increase in 2023. As tourism activity normalised post-pandemic, the primary drivers of GDP growth in 2024 were the construction and financial services sectors. Risks to the macroeconomic outlook are balanced. The service-dominant economy, lacking large-scale manufacturing or goods exports typically affected by tariffs, faces limited direct exposure to the global trade war. However, Andorra's large structural dependency on imports leaves it exposed to external developments of key trading partners, particularly through prices. Imported goods and services account for roughly 46% of the CPI basket.

Limited Growth Potential: We project Andorra's growth at 1.8% in 2025, slowing towards 1.5% in 2026. Challenges to increasing potential growth include a small domestic market, limited economic diversity, tight labour market and ageing population. Activity in the construction sector is strong, but the supply of affordable housing is limited and remains a government priority. Government efforts to position the country as a destination for higher value-added foreign investment are gradually progressing,

but a substantial shift in its economic model is unlikely in the medium term. The effect of climate change also brings challenges to Andorra's winter tourism sector.

Fiscal Prudence: Strong fiscal metrics support the rating. The national fiscal framework, with a central government debt ceiling of 40% of GDP and deficit limit of 1% of GDP, has anchored fiscal credibility. Conservative budgeting practices, particularly for revenue, help prevent overspending, even when tax receipts exceed expectations. Andorra's status as a highly competitive tax economy also makes major tax reform unlikely. We expect central government fiscal deficits to average 0.5% of GDP in 2025 and 2026, reflecting increased public investment in transport infrastructure, public housing and healthcare.

Low Debt Ratio: At 33.2% of GDP at end-2024 (Fitch's estimate), Andorra's general government debt ratio is below the 'A' category median ratio (57.4%). We project it will gradually decline to 30.8% of GDP by 2026. The country faces no external financing requirements until February 2027, when a EUR500 million Eurobond matures. Domestic debt obligations, averaging 0.6% of GDP in 2025 and 2026, will be managed using the government's fiscal buffer, which was 11.6% of GDP at end-2023.

Ageing Pressures, Pension Reform: Long-term debt sustainability is challenged by demographic pressures and rising age-related spending. Andorra has some of the lowest public pension expenditure in Europe, but the IMF projects significant increases over the next two decades. Strong immigration-driven population growth has deferred deficits in the public social security fund until after 2026, later than the government's earlier estimate of 2024. We expect the fund's sizeable assets (approximately 48% of GDP) to help mitigate the rising fiscal costs of an aging population. Pension reform remains a key government priority, with a consensus to outline a reform strategy this year.

EU Association Agreement: The Association Agreement (AA) is pending approval by the EU Council, following an agreement on its terms between Andorra and the EU in December 2023. If approved, Andorra plans to present the AA for a national referendum. Fitch believes the AA will facilitate Andorra's further integration into the EU internal market, expand export opportunities and potentially support economic diversification over the medium to long term. However, a prolonged delay in ratification at the EU level could create uncertainty over the referendum and public support.

Banking Sector Resilience: The banking sector is large (with consolidated assets close to EUR19 billion or 5x GDP), but Andorran banks maintain satisfactory capital and liquidity buffers over requirements. Profitability has been resilient, supported by higher interest rates, recent consolidation and low asset-quality pressures. The latest assessment by the Andorran Financial Authority indicates the sector's credit-to-GDP gap as below

long-term trend but set to turn positive by end 2025. High interest rates have weighed on credit growth in both the corporate and household sectors, and despite significant growth in the construction sector, loans related to this sector (including real estate loans) have remained stable.

ESG - Governance: Andorra has an ESG Relevance Score of '5[+]' for both Political Stability and Rights and for the Rule of Law, Institutional and Regulatory Quality and Control of Corruption, as is the case for all sovereigns. These scores reflect the high weight that the World Bank Governance Indicators (WBGI) have in our proprietary Sovereign Rating Model (SRM). Andorra has a high WBGI ranking at 89.6 percentile, well above the 'A' median, reflecting strong institutional capacity and effective rule of law.

RATING SENSITIVITIES

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

-Structural Features: A severe shock to the banking sector that would result in sizeable spillovers to Andorra's economic performance and public finances, given the large size of the banking sector.

-Public Finances: A material increase in the government debt ratio, for example, due to a macroeconomic shock or erosion of international competitiveness resulting from changes in tax policy.

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

-Structural Features/Macro: An improvement in growth potential, for example, via the implementation of structural reforms to improve the business environment, progress on economic diversification and/or further integration with the EU.

-Public Finances: A material decline in general government debt or reduction in contingent liability risks, for example, given improved resilience of the banking sector, including access to Eurosystem liquidity facilities.

SOVEREIGN RATING MODEL (SRM) AND QUALITATIVE OVERLAY (QO)

Fitch's proprietary SRM assigns Andorra a score equivalent to a rating of 'A-' on the Long-Term Foreign-Currency (LTFC) IDR scale.

Fitch's sovereign rating committee did not adjust the output from the SRM to arrive at the final LTFC IDR.

Fitch's SRM is the agency's proprietary multiple regression rating model that employs 18 variables based on three-year centred averages, including one year of forecasts, to produce a score equivalent to a LT FC IDR. Fitch's QO is a forward-looking qualitative framework designed to allow for adjustment to the SRM output to assign the final rating, reflecting factors within our criteria that are not fully quantifiable and/or not fully reflected in the SRM.

COUNTRY CEILING

The Country Ceiling for Andorra is 'AAA', six notches above the Long-Term Foreign-Currency IDR and at the upper limit of the rating scale. We view the risk of exchange and capital controls as minimal.

Fitch's Country Ceiling Model produced a starting point uplift of +3 notches above the IDR. Fitch's rating committee applied a further +3 notch qualitative adjustment under the Long-Term Institutional Characteristics, reflecting Andorra's fully euroised economy.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

The following limitations were identified and addressed:

Broad money estimates are unavailable; we have used information from the consolidated balance sheets of Andorran banks.

Balance of payments statistics by the authorities and IMF are only available for 2019-2023 and the international investment position statistics for 2019-2023. Fitch has estimated historical and latest data with reasonable confidence using national accounts data and consolidated balance sheets of Andorran banks. The data used was deemed sufficient for Fitch's rating purposes because it expects that the margin of error related to the estimates would not be material to the rating analysis.

ESG CONSIDERATIONS

Andorra has an ESG Relevance Score of '5[+]' for Political Stability and Rights as World Bank Governance Indicators have the highest weight in Fitch's SRM and are therefore highly relevant to the rating and a key rating driver with a high weight. As Andorra has a percentile rank above 50 for the respective Governance Indicator, this has a positive impact on the credit profile.

Andorra has an ESG Relevance Score of '5[+]' for Rule of Law, Institutional & Regulatory Quality and Control of Corruption as World Bank Governance Indicators have the highest weight in Fitch's SRM and are therefore highly relevant to the rating and are a key rating driver with a high weight. As Andorra has a percentile rank above 50 for the respective Governance Indicators, this has a positive impact on the credit profile.

Andorra has an ESG Relevance Score of '4[+]' for Human Rights and Political Freedoms as the Voice and Accountability pillar of the World Bank Governance Indicators is relevant to the rating and a rating driver. As Andorra has a percentile rank above 50 for the respective Governance Indicator, this has a positive impact on the credit profile.

Andorra has an ESG Relevance Score of '4[+]' for Creditor Rights as willingness to service and repay debt is relevant to the rating and is a rating driver for Andorra, as for all sovereigns. As Andorra has a track record of 20+ years without a restructuring of public debt and captured in our SRM variable, this has a positive impact on the credit profile.

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/topics/esg/products#esg-relevance-scores.

RATING ACTIONS

ENTITY / DEBT ⚡	RATING ⚡			PRIOR ⚡
Andorra	LT IDR	A-	Affirmed	A-
	ST IDR	F2	Affirmed	F2
	Country Ceiling	AAA	Affirmed	AAA

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APPLICABLE CRITERIA[Country Ceiling Criteria \(pub. 24 Jul 2023\)](#)[Sovereign Rating Criteria \(pub. 24 Oct 2024\) \(including rating assumption sensitivity\)](#)**APPLICABLE MODELS**

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

[Country Ceiling Model, v2.0.3 \(1\)](#)[Debt Dynamics Model, v1.3.2 \(1\)](#)[Macro-Prudential Indicator Model, v1.5.0 \(1\)](#)[Sovereign Rating Model, v3.14.2 \(1\)](#)**ADDITIONAL DISCLOSURES**[Dodd-Frank Rating Information Disclosure Form](#)[Solicitation Status](#)[Endorsement Policy](#)**ENDORSEMENT STATUS**

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