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Ratings

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Summary:

Dominican Republic

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Issuer Credit Rating	BB-/Stable/B

Key Rating Factors

Institutional and economic profile	Flexibility and performance profile
• Real GDP growth of about 5%, on average, in 2019-2022 would put GDP per capita at about $9,000 at the end of the period. • The likelihood of structural reforms being approved is declining as the 2020 presidential election approaches. • Continued delays in advancing structural reforms diminishes the sovereign's capacity to maintain sustainable public finances in the coming years.	• The Dominican Republic's fiscal deficits should average 4% of GDP in the next three years, which would lead to continued increases in debt and interest payments. • The current account deficit (CAD) is likely to remain moderate, but vulnerable to external shocks. • Inflation should stay within the central bank range in the next two years.

Outlook

The stable outlook balances S&P Global Ratings' expectation that the Dominican Republic will continue to grow at an average of 5% annually during the next three years. We don't expect the current administration to tackle long-standing structural deficiencies in the fiscal and energy sectors during the remainder of its term, despite their importance in lessening the sovereign's fiscal and external vulnerabilities.

We could raise the ratings if the government takes steps to improve structural fiscal trends, such as through energy-sector reform, tackling the quasi-deficit of the central bank, or central government fiscal reform. Lower fiscal deficits, coupled with sustained improvement in external liquidity ratios, could lead to an upgrade during the next two years.

We could lower our ratings if policy decisions or adverse external conditions generate lower potential GDP growth during the next two years. Also, we could lower our ratings if the Dominican Republic doesn't grow faster than peers with a similar level of economic development, which would weigh on fiscal dynamics.

Rationale

Our ratings on the Dominican Republic reflect our expectation of solid and above peers' economic growth over the next three years, which should continue to improve living standards. The ratings also reflect the track record of a sounder monetary policy framework, which includes inflation targeting.

The ratings are constrained by the country's institutional weaknesses, increasing general government debt burden, and still-vulnerable external position that keeps the sovereign exposed to external shocks.

Institutional and economic profile: Economic growth to remain strong despite absence of structural reforms

A dynamic tourism sector should continue to support solid service-sector growth in the coming years, balancing a likely deceleration in construction activities as the construction of the Punta Catalina Plant ends. In addition, remittances growth--which averaged 11% over the last two years--should help to sustain private consumption.

We forecast that the Dominican Republic's real GDP growth will average 5% in 2019-2022, still comparing positively with its regional peers and peers with a similar level of economic development. Indeed, from 2014 to 2018, the sovereign posted the highest growth in the Americas. We project GDP per capita to surpass $9,000 in 2022, which should continue to help reduce the poverty level from the current 23%.

President Danilo Medina, from the Partido de la Liberación Dominicana (PLD), has less than a year and a half left in office, and we don't expect controversial structural reform to be approved within the current administration. Despite the PLD having a formal majority in both legislative chambers, internal divisions in the PLD, corruption allegations, and political motivations have limited progress on passing reforms to its energy sector, its fiscal framework, and the recapitalization law of its Central Bank, among others.

Our overall assessment is that the rule of law in the Dominican Republic is still weak. In addition, the ongoing delays and failure to advance reform in key sectors of the economy reflect, in our view, limited capacity to maintain sustainable public finances and promote balanced economic growth over the longer term.

Flexibility and performance profile: Consistent fiscal deficits will keep the sovereign debt increasing, while the current account remains vulnerable to external shocks

In the absence of fiscal reform and a new recapitalization law of the central bank, we don't expect improvement in the Dominican Republic's fiscal deficits. For 2019-2022, we are forecasting a general government deficit of 4% of GDP, of which around 2% corresponds to the central bank quasi-fiscal deficit. (Our definition of general government includes central government, the central bank quasi-deficit, and the nonfinancial public sector.)

While economic growth and administrative measures should contribute to stable revenue, this does not facilitate higher capital expenditures in a sustainable way in the coming years. The beginning of operations of the Punta Catalina Energy Plant this year could help to further reduce subsidies to the electrical sector in the next years, as well as its physical losses, which are currently at 30%.

We expect the change in general government debt to be close to 5% in 2019-2022, a bit higher than general government deficits, reflecting depreciation of the local currency. This would increase the sovereign's net debt to around 51% of GDP in 2022, from 48% of GDP in 2018. Net debt stock includes central bank certificates (13.7% of GDP in 2018) and excludes the recapitalization bonds that the central government issues to capitalize the central bank (3.3% of GDP) following the 2003-2004 bailout of the banking sector.

Higher debt will keep interest payments high, at an average of 19% of general government revenues up to 2022. This figure is not fully comparable with peers because almost 25% of the central government's interest bill is paid to the central bank to help recapitalize it.

The Dominican Republic has made important enhancements to its debt management. For example, as of today, most of its debt is on fixed rates. That said, domestic debt markets are still comparably shallow, and foreign currency debt is around 55%, which makes the overall profile vulnerable to currency depreciation.

Lower oil prices, as well as growing tourism and remittances, have led to overall declining CADs over the last five years. For 2019-2022, we expect the CAD to rise and average 2.3% of GDP. At the same time, we expect it to be fully covered by foreign direct investment (FDI), which we project at 3% of GDP, on average, over the same period. This would continue to lead to increasing usable reserves, which, in 2018, represented 9.4% of GDP, equivalent to 4.4 months of imports.

Despite a moderate CAD, we believe the Dominican Republic remains vulnerable to external shocks--in particular, to increases in oil prices and a deceleration of the U.S. economy given its close links. Despite further diversification in recent years, 40% of tourism, 77% of remittances, and 25% of FDI come from the U.S. With the coal-driven Punta Catalina Energy Plant coming online, dependence on oil should moderate in the coming years.

We expect the country's gross external financing needs to be slightly above 100% of current account receipts (CAR) plus usable reserves during 2019-2022. Its narrow net external debt is set to average 79% of CAR over the same period.

Since 2012, when the central bank became operationally independent, inflation has remained with its target range (4% plus/minus 1%). In fact, in 2018, inflation was the lowest registered over the last 10 years (1.2%). Still, its monetary transmission mechanism is constrained by quasi-fiscal losses, a low level of domestic credit (below 27% of GDP in June 2018), and shallow domestic debt and capital markets.

Key Statistics

Table 1

Selected Indicators--Dominican Republic

	2012	2013	2014	2015	2016	2017	2018	2019f	2020f	2021f	2022f
Economic indicators (%)											
Nominal GDP (bil. LC)	2,386.02	2,619.77	2,877.53	3,099.65	3,333.42	3,613.15	4,025.09	4,395.40	4,799.78	5,241.36	5,723.56
Nominal GDP (bil. $)	60.66	62.68	66.07	68.81	72.36	76.01	81.30	85.71	90.00	94.50	99.22
GDP per capita ($000s)	6.3	6.4	6.7	6.9	7.2	7.5	7.9	8.3	8.6	9.0	9.3
Real GDP growth	2.7	4.9	7.6	7.0	6.6	4.6	7.0	5.0	5.0	5.0	5.0
Real GDP per capita growth	1.6	3.8	6.6	6.0	5.6	3.6	5.9	4.1	4.1	4.1	4.1
Real investment growth	(0.5)	(2.5)	12.3	20.6	11.4	0.5	13.2	6.0	6.0	6.0	6.0
Investment/GDP	24.3	22.7	23.0	22.6	21.9	21.8	24.4	24.3	24.2	24.2	24.1
Savings/GDP	17.9	18.6	19.7	20.7	20.8	21.7	22.9	22.4	22.0	21.6	21.4

Table 1

Selected Indicators--Dominican Republic (cont.)	2012	2013	2014	2015	2016	2017	2018	2019f	2020f	2021f	2022f
Exports/GDP	24.6	25.2	25.4	24.5	24.9	24.8	25.1	24.8	24.5	24.3	24.0
Real exports growth	5.5	9.0	7.5	2.0	6.6	4.7	6.7	3.0	3.0	3.0	3.0
Unemployment rate	14.7	15.0	14.5	14.0	13.3	10.0	10.3	15.0	15.0	15.0	15.0
External indicators (%)											
Current account balance/GDP	(6.4)	(4.1)	(3.3)	(1.9)	(1.1)	(0.2)	(1.4)	(1.9)	(2.3)	(2.6)	(2.7)
Current account balance/CARs	(19.2)	(12.0)	(9.6)	(5.5)	(3.3)	(0.5)	(4.2)	(5.6)	(6.7)	(7.5)	(7.9)
CARs/GDP	33.3	34.0	34.4	33.6	34.0	34.4	34.3	34.1	34.2	34.4	34.7
Trade balance/GDP	(14.4)	(11.8)	(11.2)	(10.8)	(10.4)	(10.0)	(11.4)	(12.1)	(12.8)	(13.4)	(14.1)
Net FDI/GDP	5.2	3.2	3.3	3.2	3.3	4.7	3.1	3.1	3.1	3.1	2.7
Net portfolio equity inflow/GDP	0.6	2.9	2.2	2.1	2.4	2.3	3.3	2.4	2.4	2.4	2.2
Gross external financing needs/CARs plus usable reserves	114.2	115.1	111.7	109.4	104.6	100.2	100.9	99.6	100.6	102.0	103.0
Narrow net external debt/CARs	78.7	79.4	87.0	81.1	80.4	80.9	75.3	77.8	78.7	79.1	78.8
Narrow net external debt/CAPs	66.0	70.9	79.4	76.8	77.8	80.5	72.3	73.7	73.8	73.6	73.0
Net external liabilities/CARs	166.3	171.5	182.3	184.8	186.2	194.8	185.3	185.1	183.1	180.5	176.3
Net external liabilities/CAPs	139.5	153.1	166.4	175.1	180.3	193.8	177.9	175.4	171.6	167.9	163.4
Short-term external debt by remaining maturity/CARs	14.4	17.4	20.0	21.7	18.5	18.3	16.8	15.3	15.9	16.6	17.2
Usable reserves/CAPs (months)	1.7	1.3	1.8	1.9	1.9	2.2	2.3	2.4	2.5	2.4	2.4
Usable reserves (mil. $)	2,658	3,644	3,777	4,061	4,875	5,552	6,245	6,707	7,042	7,393	7,761
Fiscal indicators (general government; %)											
Balance/GDP	(8.0)	(5.4)	(5.1)	(4.7)	(4.2)	(4.6)	(3.9)	(4.0)	(4.3)	(3.8)	(4.1)
Change in net debt/GDP	8.3	6.8	4.1	3.4	5.6	5.2	5.7	4.9	5.2	4.7	5.0
Primary balance/GDP	(5.6)	(3.1)	(2.7)	(2.3)	(1.5)	(1.9)	(1.2)	(1.2)	(1.5)	(1.0)	(1.2)
Revenue/GDP	13.6	14.2	14.5	14.2	14.5	14.7	14.9	14.9	14.9	14.9	14.9
Expenditures/GDP	21.5	19.6	19.6	18.9	18.7	19.3	18.8	18.9	19.2	18.7	19.0
Interest/revenues	17.4	15.9	16.5	16.8	18.3	18.2	18.3	18.6	18.9	19.0	19.3
Debt/GDP	40.1	44.0	43.4	43.6	46.5	48.2	49.8	50.6	51.5	51.9	52.5
Debt/revenues	295.5	309.4	299.9	307.0	320.6	326.8	334.3	339.3	345.8	348.2	352.2
Net debt/GDP	38.3	41.7	42.0	42.4	45.1	46.8	47.7	48.6	49.7	50.2	51.0
Liquid assets/GDP	1.7	2.3	1.4	1.2	1.5	1.4	2.1	2.0	1.8	1.6	1.5

Table 1

Selected Indicators--Dominican Republic (cont.)											
	2012	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019f**	**2020f**	**2021f**	**2022f**
Monetary indicators (%)											
CPI growth	3.9	3.9	1.6	2.3	1.7	4.2	1.2	4.0	4.0	4.0	4.0
GDP deflator growth	5.1	4.7	2.0	0.6	0.9	3.7	4.2	4.0	4.0	4.0	4.0
Exchange rate, year-end (LC/$)	40.36	42.79	44.36	45.55	46.71	48.30	50.28	52.29	54.38	56.55	58.82
Banks' claims on resident non-gov't sector growth	5.6	14.9	19.9	17.9	12.0	11.5	10.4	9.2	9.2	9.2	9.3
Banks' claims on resident non-gov't sector/GDP	21.9	23.0	25.1	27.5	28.6	29.4	29.1	29.1	29.1	29.1	29.2
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	N/A
Foreign currency share of residents' bank deposits	38.7	39.2	40.8	40.2	39.7	35.2	36.9	36.9	36.9	36.9	36.9
Real effective exchange rate growth	0.2	(3.5)	(2.2)	2.3	(0.9)	(2.2)	(3.3)	N/A	N/A	N/A	N/A

Sources: Central Bank of Dominican Republic (economic indicators), Central Bank of Dominican Republic (external indicators), Ministry of Finance and Central Bank of Dominican Republic (fiscal indicators), and International Monetary Fund (monetary 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 assets held by 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. e--Estimate. f--Forecast. 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

Ratings Score Snapshot--Dominican Republic		
Key rating factors	**Score**	**Explanation**
Institutional assessment	5	Policy choices led to delays in the approval of structural reforms, which may weaken support for sustainable public finances and balanced economic growth.
Economic assessment	3	Based on GDP per capita and growth trends, per selected indicators in table 1.
		Weighted average real GDP per capita trend growth over a 10-year period is around 5%, which is well above sovereigns in the same GDP category.
External assessment	5	Based on narrow net external debt and gross external financing needs/(current account receipts plus usable reserves), per selected indicators in table 1.
		There is a risk of marked deterioration in the cost of or access to external financing, given that net external liabilities are significantly higher than narrow net external debt. The net external liability position is worse than the narrow net external debt position by over 100% of current account receipts, per selected indicators in table 1.

Table 2

Ratings Score Snapshot--Dominican Republic (cont.)

Key rating factors	Score	Explanation
Fiscal assessment: flexibility and performance	5	Based on the change in net general government debt (% of GDP), per selected indicators in table 1.
Fiscal assessment: debt burden	5	Based on net general government debt (% of GDP) and general government interest expenditures (% of general government revenues), per selected indicators in table 1.
		Over 50% of gross government debt is denominated in foreign currency.
Monetary assessment	4	The exchange rate regime is a crawling peg, with the central bank intervening intermittently in foreign exchange markets.
		The central bank has a short track record of operational independence and uses market-based monetary instruments, such as open market operations. CPI as per selected indicators in table 1. The central bank has the ability to act as lender of last resort for the financial system.
Indicative rating	bb-	
Notches of supplemental adjustments and flexibility	0	
Final rating		
Foreign currency	BB-	
Notches of uplift	0	Default risks do not apply differently to foreign- and local-currency debt
Local currency	BB-	

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

- Sovereign Rating Methodology, Dec. 18, 2017
- Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Use Of CreditWatch And Outlooks, Sept. 14, 2009
- General Criteria: Methodology: Criteria For Determining Transfer And Convertibility Assessments, May 18, 2009