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Fitch Downgrades Ireland's Sovereign Rating to 'AA+'; Outlook Negative Ratings

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Fitch Ratings-London-08 April 2009: Fitch Ratings has today lowered the Republic of Ireland's Long-term foreign and local currency Issuer Default Rating (IDR) to 'AA+' from 'AAA'. The Short-term foreign currency IDR is affirmed at 'F1+' and the Country Ceiling is affirmed at 'AAA', the ceiling appropriate for euro area members. The Outlook on the Long-term IDR is revised to Negative. This action resolves the Rating Watch Negative assigned to Ireland's 'AAA' ratings on March 6, 2009.

The outlook for Ireland's public finances and fiscal risks is no longer consistent with an 'AAA' rating. The government's recently published budget projections show that, even ignoring the impact of the National Asset Management Agency initiative (NAMA), gross government debt will rise to around 80% of GDP by 2011, a more than three-fold increase from its pre-recession level of 25% at end-2007. This is a much faster increase than expected in any other 'AAA' rated sovereign.

A severe economic downturn - with GDP now expected to decline by 8% in 2009 as activity suffers from both the domestic property market correction and the international recession - has taken a heavy toll on public finances. The collapse in government revenues - which in 2009 are expected to fall by 16% following similar declines in 2008 - has also revealed structural weaknesses in the underlying budgetary position, previously disguised by property and asset market related revenue buoyancy.

The fiscal tightening measures taken by the government in the latest supplementary budget show considerable resolve and will contain slippage in the 2009 deficit relative to the previous 9.5% of GDP target to just over 1ppt. However, the need to engage in pro-cyclical fiscal tightening in the midst of the steepest recession in recent memory demonstrates the government's lack of policy flexibility.

The proposal to 'carve-out' property development and investment loans from banks' balance sheets is an innovative and bold measure to shore up confidence in the Irish banks. However, the up-front costs of this measure, to be funded directly on the government's balance sheet with government debt issued to the banks, will be very substantial. The face value of loans to be purchased is up to EUR90bn - equivalent to around 50% of 2008 GDP. Although these loans will be purchased at a discount from the banks, the associated crystallisation of losses for the banks is likely to entail a requirement for additional capital support from the government. While the government is acquiring assets, the return on these loans is uncertain.

With economic prospects remaining very weak and the fiscal deficit expected to remain very large in the near term, the Outlook is Negative.

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