S&P Global
Ratings

RatingsDirect®

Research Update:

Swiss Canton of Basel-City 'AAA/A-1+' Ratings Affirmed; Outlook Stable

November 8, 2019

Overview

- We assume that the upcoming change in financial management will not significantly alter the Canton of Basel-City's financial politics.
- We believe revenue losses from the national tax reform will affect the canton's budgetary performance, but not lead to significant deficits since it has created sufficient headroom.
- We are affirming our 'AAA' long-term and 'A-1+' short-term ratings on the Canton of Basel-City and maintaining our stable outlook.

PRIMARY CREDIT ANALYST

Thomas F Fischinger
Frankfurt
(49) 69-33-999-243
thomas.fischinger
@spglobal.com

SECONDARY CONTACT

Alois Strasser
Frankfurt
(49) 69-33-999-240
alois.strasser
@spglobal.com

ADDITIONAL CONTACT

EMEA Sovereign and IPF
SovereignIPF
@spglobal.com

Rating Action

On Nov. 8, 2019, S&P Global Ratings affirmed its 'AAA/A-1+' long- and short-term issuer credit ratings on the Swiss Canton of Basel-City. The outlook remains stable.

We also affirmed our 'AAA' issue ratings on Basel-City's senior unsecured debt.

Outlook

The stable outlook reflects our view that Basel-City will continue to achieve sound budgetary performance over the next few years. We regard potential deficits after capital accounts as small and temporary, and therefore expect that the canton can refrain from debt accumulation over the next two years.

Downside scenario

All other things remaining equal, we could lower the rating if the canton's management fails to exercise budgetary discipline and loosens its grip on financial performance. In addition, pressure on the ratings would build if the cantonal bank were to call upon the canton for support. However, we currently view this scenario as unlikely.

Rationale

The ratings reflect the canton's very strong economic fundamentals with very high wealth levels and low unemployment rates. Excellent financial results have created room to weather the temporary effect from the TP17 Swiss corporate tax reform without a substantial debt increase. The ratings also benefit from the canton's excellent liquidity situation and high flexibility to alter its tax rates if unforeseen developments occur. The canton's potentially sizable contingent liabilities from its stake in a commercial bank add to its relatively high debt burden.

Basel-City is a donor canton to the national equalization system

Due to its very favorable economic and financial profile, Basel-City is one of only seven cantonal contributors to weaker cantons in the national equalization system. For 2020, the canton is obliged to pay Swiss franc (CHF) 108 million (about €98 million or equivalent to 2.5% of operating revenue) to other cantons. The Swiss cantons' institutional framework is mature and extremely predictable, in our view, with major reforms planned well in advance and widely discussed, notably between the government and the cantons, and among the cantons themselves. Switzerland (AAA/Stable/A-1+) is currently implementing a nationwide corporate tax reform (TP17 or TRAF, see Related Research below), which will take effect from 2020. In short, the reform provides for the discontinuation of certain tax privileges of foreign holdings, domiciliary, and mixed companies. Basel-City receives a considerable amount of taxes from these special-status companies, and so is particularly affected by the reform.

We believe that the canton's management has created enough financial headroom to deal with the effects of the upcoming reform, indicating managerial strength. In our base-case scenario, we assume more optimistic revenue growth rates than the canton, which regularly outperforms its budgetary plans. Although a new individual will head the financial department from 2020 onward following the election of the previous finance minister to the national parliament in October 2019, we do not expect that the canton will deviate from its sound financial practices.

Basel-City is one of the wealthiest regions in the world. Swiss cantons achieve a GDP per capita of more than CHF83,000 (equivalent to more than €75,000). Basel-City achieves about twice this already very high national average, highlighting its credit strength. The canton is home to some of the largest corporations in the pharmaceutical and chemical sector globally, which has proven to be relatively resilient over recent years. Ongoing diversification within the life science industry reduces the canton's exposure to a single subsector or product cycle. Moreover, we observe that the canton's tax revenue does not exhibit elevated volatility from the sector. The large number of companies that are located in the canton provides jobs that attract a significant amount of national and international commuters, helping to keep unemployment at a very low 2.7% in September 2019. This is slightly higher than the national average of 2.1% but Basel-City's unemployment figures usually follow national trends.

Past exceptional budgetary results are unlikely to be repeated in the next few years

Basel-City managed to achieve excellent budgetary results, with surpluses after capital accounts, over the past two years. We believe that the canton will outperform budgeted figures again in 2019. However, in our view, tax code changes that come into effect from next year might halve operating surpluses, and lead to small deficits after capital accounts of 0.3%-2.6% of operating revenue from 2020 to 2022. We view this as a structural deterioration compared with the surplus after capital accounts achieved recently. We estimate capital expenditure will increase to about 10% of operating revenue by 2023, reflecting the canton's current ambitious investment plan, which includes improvements to traffic infrastructure and harbor facilities.

Despite these budgetary headwinds, we estimate that the canton's overall sound budgetary path will not be altered in our base case. This is because surpluses, including our estimate for 2019, have built up sufficient headroom to cope with the temporary decrease in budgetary performance. In addition, Basel-City has consistently outperformed its financial plans, especially with the help of higher-than-budgeted tax revenue and sound budgetary discipline to keep expenditures under control. We note that the canton enjoys high flexibility to alter its tax rates if unforeseen developments arise. Compared with national peers, Basel-City also enjoys the flexibility to alter municipal revenue if necessary.

We project Basel-City's direct debt will hover at about 90% of operating revenue through 2023. The canton does not have any outstanding debt denominated in foreign currency. Basel-City's main contingent liability is Basler Kantonalbank (AA+/Stable/A-1+), its cantonal bank, since the canton legally guarantees practically all of the bank's liabilities. In our opinion, Basel-City's creditworthiness could be harmed if the bank called on the guarantee or had to rely on the canton for significant capital contributions. However, we currently view the likelihood of such a scenario as remote. The canton's other contingent liabilities, such as guarantees or stakes in dependent companies, are minor relative to operating revenue. We therefore assess the canton's contingent liabilities as moderate overall.

Basel-City has exceptional liquidity, in our view. Cash, liquid assets, and committed facilities cover far more than 120% of debt service over the next 12 months. The canton has reduced its own cash levels, due to the current negative interest rate environment, but intends to keep a defined minimum cash level. To offset the low amount of liquid assets, Basel-City has signed a CHF900 million credit line with Basler Kantonalbank, which the canton may use during the year for daily cash management. Basel-City benefits from strong access to the deep, liquid Swiss capital market, as demonstrated by regular bond issues, even in times of heightened financial market volatility.

Key Statistics

Table 1

Basel-City (Canton of) Selected Indicators

(Mil. CHF)	2016	2017	2018	2019bc	2020bc	2021bc	2022bc
Operating revenues	4,266	4,144	4,200	4,239	4,048	4,155	4,253
Operating expenditures	3,991	3,648	3,672	3,744	3,788	3,863	3,970
Operating balance	275	496	528	495	260	291	283
Operating balance (% of operating revenues)	6.4	12.0	12.6	11.7	6.4	7.0	6.7
Capital revenues	19	19	10	6	(12)	20	20
Capital expenditures	393	513	321	315	315	325	415
Balance after capital accounts	(98)	2	217	185	(67)	(14)	(112)
Balance after capital accounts (% of total revenues)	(2.3)	0.0	5.2	4.4	(1.7)	(0.3)	(2.6)

Table 1

Basel-City (Canton of) Selected Indicators (cont.)

(Mil. CHF)	2016	2017	2018	2019bc	2020bc	2021bc	2022bc
Debt repaid	1,392	300	803	400	600	400	525
Gross borrowings	1,981	200	809	450	420	392	637
Balance after borrowings	408	(184)	185	255	(226)	0	(0)
Direct debt (outstanding at year-end)	3,926	3,772	3,778	3,828	3,648	3,640	3,752
Direct debt (% of operating revenues)	92.0	91.0	90.0	90.3	90.1	87.6	88.2
Tax-supported debt (outstanding at year-end)	3,926	3,772	3,778	3,828	3,648	3,640	3,752
Tax-supported debt (% of consolidated operating revenues)	92.0	91.0	90.0	90.3	90.1	87.6	88.2
Interest (% of operating revenues)	0.7	0.7	0.7	0.9	0.4	0.4	0.6
Local GDP per capita (CHF)	168,367	169,529	N/A	176,811	180,258	183,791	187,394
National GDP per capita (CHF)	78,568	78,917	80,700	82,087	83,747	85,580	87,810

The data and ratios above result in part 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. The main sources are the financial statements and budgets, as provided by the issuer. bc--Base case reflects S&P Global Ratings' expectations of the most likely scenario. N/A--Not applicable. N.A.--Not available. N.M.--Not meaningful. CHF--Swiss franc.

Ratings Score Snapshot

Table 2

Basel-City (Canton of) Ratings Score Snapshot

Key rating factors	Scores
Institutional framework	1
Economy	1
Financial management	1
Budgetary performance	1
Liquidity	1
Debt burden	4
Stand-alone credit profile	aaa
Issuer credit rating	AAA

S&P Global Ratings bases its ratings on non-U.S. local and regional governments (LRGs) on the six main rating factors in this table. In the "Methodology For Rating Local And Regional Governments Outside Of The U.S.," published on July 15, 2019, we explain the steps we follow to derive the global scale foreign currency rating on each LRG. The institutional framework is assessed on a six-point scale: 1 is the strongest and 6 the weakest score. Our assessments of economy, financial management, budgetary performance, liquidity, and debt burden are on a five-point scale, with 1 being the strongest score and 5 the weakest.

Key Sovereign Statistics

- Sovereign Risk Indicators, Oct. 10, 2019. An interactive version is available at http://www.spratings.com/sri

Related Criteria

- Criteria | Governments | International Public Finance: Methodology For Rating Local And Regional Governments Outside Of The U.S., July 15, 2019
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- Summary: Switzerland, Aug. 23, 2019
- Default, Transition, and Recovery: 2018 Annual International Public Finance Default And Rating Transition Study, Aug. 19, 2019
- Institutional Framework Assessments For International Local And Regional Governments, July 4, 2019
- Two Popular Votes, Two Approaches To Corporate Tax Reform In Switzerland, May 21, 2019
- Local Government Debt 2019: Slower Debt Reduction For German States And Little Change For Swiss And Austrian LRG Debt, March 1, 2019
- Banking Industry Country Risk Assessment: Switzerland, Nov. 30, 2018
- Public Finance System Overview: Swiss Cantons, Nov 20, 2018
- International Public Finance Rating Trends: German, Austrian, And Swiss Local And Regional Governments, Oct. 22, 2018
- Will The Swiss Tax Reform Plan TP 17 Cost Some Cantons More Than Others?, Aug. 29, 2018

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's assessment of the key rating factors is reflected in the Ratings Score Snapshot above.

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

Ratings Affirmed	
Basel-City (Canton of)	
Issuer Credit Rating	AAA/Stable/A-1+
Senior Unsecured	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.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings 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.

Copyright © 2019 by Standard & Poor's Financial Services LLC. All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of Standard & Poor's Financial Services LLC or its affiliates (collectively, S&P). The Content shall not be used for any unlawful or unauthorized purposes. S&P and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively S&P Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. S&P PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives. Rating-related publications may be published for a variety of reasons that are not necessarily dependent on action by rating committees, including, but not limited to, the publication of a periodic update on a credit rating and related analyses.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw or suspend such acknowledgment at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain non-public information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, www.standardandpoors.com (free of charge), and www.ratingsdirect.com (subscription), and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.

STANDARD & POOR'S, S&P and RATINGSDIRECT are registered trademarks of Standard & Poor's Financial Services LLC.