S&P Global Ratings

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Research Update:

Republic and Canton of Geneva 'AA' Ratings Affirmed; Outlook Still Positive

June 14, 2024

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Overview

- Despite announced tax cuts, we expect the Republic and Canton of Geneva will continue to post solid performance and sound financial management, and stabilize its debt burden.
- We affirmed our 'AA' long-term foreign and local currency issuer credit ratings on the Republic and Canton of Geneva and maintained the positive outlook.
- The positive outlook reflects our view that Geneva's tax revenue could outperform our forecasts, while the canton maintains fiscal discipline.

Rating Action

On June 14, 2024, S&P Global Ratings affirmed its 'AA' long-term foreign and local currency issuer credit ratings on the Republic and Canton of Geneva (the canton or Geneva). The outlook remains positive.

Outlook

The positive outlook reflects the possibility that taxes could increase beyond our current expectations. This, coupled with continuous cost control and well-measured cantonal decisions on fiscal policies, could enable Geneva to achieve stronger performance than our base-case expectations over 2024-2026.

Upside scenario

We could upgrade Geneva over the next 12 months if, amid historically high tax revenue, Geneva's management sticks to sound financial policies and limits borrowing needs.

Downside scenario

We could revise the outlook to stable if Geneva maintains capital account ratios close to balance or posts minor deficits due to lower revenue, or because management loosens its tight financial policies.

Rationale

While the canton is engaging in a series of tax cuts, we still factored in our outlook the possibility that tax revenue could outperform our forecasts. If this materializes, and Geneva maintains sound financial policies, it should be able to further reduce its debt.

The rating on Geneva is supported by the strengths in the institutional framework for Swiss cantons. It is also underpinned by the canton's diversified and resilient economy and high-income levels, which lifted tax revenue in recent years. Also, Geneva benefits from uninterrupted access to deep capital markets and European banks, supporting its very strong liquidity position.

The rating remains constrained by a high debt burden compared with other Swiss cantons, as well as contingent risks, mainly linked to the pension funds:

- Caisse de Prévoyance de l'Etat de Genève;
- Fondation de Prévoyance en faveur du personnel des Transports Publics Genevois; and
- Caisse de Prévoyance des fonctionnaires de police et des établissements pénitentiaires.

Nevertheless, we believe Geneva manages such risks and aims to anticipate the needs of the pension funds.

Strong value-added economy and very supportive institutional framework remain key credit strengths

The institutional framework for Swiss cantons is very predictable and supportive. Amendments are made only after consultation with all cantons and, in many cases, are voted on in a public referendum. This means changes to the framework take place only after extensive discussions and incrementally, including mitigating measures where required. Swiss cantons benefit from large fiscal revenue and can adjust tax rates to accommodate funding needs. Also, the Swiss national fiscal equalization system continues to support the institutional framework. Geneva is the third-largest net contributor to the system, and could become the second-largest contributor by 2026 according to the latest forecasts from Institut Bak.

Geneva benefits from one of the highest global standards of living, with a GDP per capita that reached Swiss franc (CHF) 117,000 in 2023. Its diversified and open economy is supported by a strong wristwatch industry, financial services, and a large trade sector. We expect Geneva's GDP to grow in line with that of Switzerland. The economy should remain resilient amid lower external demand for Swiss goods and strong franc appreciation versus the euro and U.S. dollar. We forecast GDP growth in Switzerland will gradually accelerate to 1.4% in 2025 and 2026, from 1.0% in 2024.

In our view, Geneva's financial management has proven its commitment to financial discipline, with strong institutional rules that ensure cost containment, as well as limited debt intake in recent years. The canton's new executive took office in June 2023. We understand the main priorities are maintaining elevated capital expenditure (capex) and containing operating expenditure growth, but other considerations include reducing specific tax items, notably for the middle class. Tax cuts could total CHF435 million in 2025, including a CHF326 million reduction of the personal income tax. Nevertheless, we expect Geneva will abide by its deficit target rules and continue to contain its relatively high debt burden.

In 2019, the canton failed in its bid to reform its pension system by moving to a defined contribution scheme from a defined benefit scheme, after rejection via a popular referendum. This would have helped structurally reduce its unfunded pension liabilities. However, the canton closely monitors its pension funds and its government-related entities (GREs) and is ready to intervene in case of extraordinary needs, adequately analyzing the risks and provisioning for them. For instance, it provisioned the recapitalization of the police pension fund in 2023 for CHF194 million, with cash outflows in 2024.

Geneva's debt and liquidity management remains very prudent. The canton ensures it has sufficient liquidity lines to cover intra-year liquidity needs. Moreover, it maintains limited exposure to variable rates and short-term maturities, shielding it from rapid repricing. With the very high tax revenue collected, the canton generates extra cash, which is invested only in short-term deposits (less than three months) with investment-grade counterparts to limit credit risk.

Solid fiscal revenue will limit borrowing needs, as long as the canton maintains a very strong liquidity position

We forecast Geneva's operating margins should gradually abate toward 5% through 2026. In 2023, the canton posted a very solid operating balance of 16.5%, though slightly below 2022 (20.9%). Fiscal revenue continued to outperform our forecasts because companies, notably in the trade sector, paid large settlements linked to 2022. In the meantime, operating expenditure were lifted by the annual indexation of public servant salaries, and by increased social spending and transfers to the canton's GREs.

We expect Geneva's fiscal revenue will decline over 2024-2026. First, we forecast the trade sector will return to its historical performance, and this will not be entirely offset by solid growth in other economic areas. Second, the canton has engaged in a series of tax cuts that total CHF435 million (or close to 5% of the taxes it collected in 2023). The main impact will stem from the personal income tax. The canton will update its income brackets, and this should reduce revenue by CHF326 million. While a popular referendum will be held Nov. 24 on that matter, we have included the full impact of measure passing in our forecasts. Other fiscal reforms could also face legal or referendum challenges but are equally included in our forecasts. In the meantime, operating expenditure should continue to grow. We note the main drivers to operating expenditure growth remain personnel (about 30% of the canton's operating expenditure) and social spending. However, we expect a sharp increase in Geneva's contribution to equalization. This is because its fiscal revenue growth has significantly outpaced the national average. Also, we note that underfunding pension liabilities on its main pension fund, Caisse de Prévoyance de l'Etat de Genève, could affect Geneva's financials in case of recapitalization. Geneva's operating balance should average 7.4% over 2024-2026.

Due to reduced operating margins, the canton should post moderate deficits after capital accounts in 2025-2026, compared with large surpluses over 2021-2024. In recent years, Geneva's capex execution rate underperformed. We forecast capex should expand to about CHF732 million annually through 2026. This is because the canton wants to invest significantly to improve its infrastructure, including transportation with extended tram lines, and digitalization. We factor in our capex for 2024 the CHF194 million recapitalization of the police pension fund. As consequence, Geneva's debt burden should stabilize through 2026, after a significant reduction post 2020.

Tax-supported debt--which includes the canton's direct debt and the debt of the transportation company, the hospital, and the public assistance office--should reach 121% of consolidated operating revenue in 2026, about the same level as in 2023. Also, we note Geneva benefits from a favorable debt profile, with most of its debt stock at fixed rates and long maturities. Geneva benefits from relative low interest rates in the Swiss capital markets. Therefore, we don't expect interest charges will weigh on its performance.

Given Geneva's solid operating performance, we expect the canton will maintain a solid liquidity position. Cash and committed bank lines totaling CHF1.19 billion should cover more than 80% of the canton's debt service over the next 12 months. We note Geneva also has access to direct and indirect liquidity lines of about CHF4 billion with various public-sector entities and Swiss and international banks. Coupled with a strong market access through short-term placements or long-term issuances in the past, we view Geneva's access to external liquidity as strong.

Key Statistics

Table 1

Republic and Canton of Geneva--Selected indicators

	--Fiscal year ended Dec. 31--				
Mil. CHF	**2022**	**2023**	**2024bc**	**2025bc**	**2026bc**
Operating revenues	11,363	11,643	10,979	10,608	10,851
Operating expenditures	8,994	9,726	9,718	10,003	10,314
Operating balance	2,369	1,917	1,261	605	537
Operating balance (% of operating revenues)	20.8	16.5	11.5	5.7	4.9
Capital revenues	88	38	35	35	35
Capital expenditures	570	543	815	684	698
Balance after capital accounts	1,887	1,412	481	(44)	(125)
Balance after capital accounts (% of total revenues)	16.5	12.1	4.4	(0.4)	(1.2)
Debt repaid	1,735	1,626	1,648	1,553	1,275
Gross borrowings	686	641	801	1,597	1,401
Balance after borrowings	838	427	(366)	0	1
Direct debt (outstanding at year-end)	15,222	14,238	13,391	13,435	13,561
Direct debt (% of operating revenues)	134.0	122.3	122.0	126.7	125.0
Tax-supported debt (outstanding at year-end)	16,533	15,646	14,827	14,900	15,055
Tax-supported debt (% of consolidated operating revenues)	129.1	119.0	118.5	122.4	121.0
Interest (% of operating revenues)	1.7	1.6	1.8	1.9	2.0
Local GDP per capita (CHF)	114,971	115,834	N/A	N/A	N/A
National GDP per capita (CHF)	88,647	89,480	90,823	92,369	93,755

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.

Ratings Score Snapshot

Table 2

Republic and Canton of Geneva--Ratings score snapshot

Key rating factors	Scores
Institutional framework	1
Economy	1
Financial management	3
Budgetary performance	3
Liquidity	1
Debt burden	4
Stand-alone credit profile	aa
Issuer credit rating	AA

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 our "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, April 8, 2024. An interactive version is available at http://www.spratings.com/sri

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Criteria | Governments | International Public Finance: Methodology For Rating Local And Regional Governments Outside Of The U.S., July 15, 2019
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Subnational Debt 2024: Fiscal Policy Differences Influence Borrowing In Developed Markets, March 5, 2024
- Subnational Debt 2024: Switzerland, Resilient Budget Surpluses Should Enable Further Deleveraging, Feb. 29, 2024
- Switzerland, Feb. 12, 2024
- Sorry, Cantons: No Profit Distributions From The SNB In 2024 And Possibly 2025, Jan. 4, 2024
- Economic Outlook Eurozone Q1 2024: Headed For A Soft Landing, Nov. 27, 2023

- Swiss Cantons Benefit From Autonomy And Robust Checks And Balances, May 23, 2023

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

Geneva (Republic and Canton of)	
Issuer Credit Rating	AA/Positive/--
Senior Unsecured	AA