S&P Global
Ratings

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Basel-City (Canton of)

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Basel-City (Canton of)

Key Rating Factors

Issuer Credit Rating
AAA/Stable/A-1+

Credit context and assumptions	Base-case expectations
Excellent budgetary performance despite the COVID-19 pandemic • Basel-City will outperform its 2020 budget despite headwinds. • The diversified and very wealthy economy will digest the economic and social turmoil of the pandemic. • Basel-City is one of few contributors to the very predictable and supportive institutional framework for Swiss cantons.	Economic recovery in 2021 should enable Basel-City to maintain stable debt • We assume a quick economic rebound from the recession in 2020, with Swiss real GDP increasing by nearly 4% in 2021. • We think tax revenue losses will remain contained, and Basel-City's ample budgetary flexibility could offset them if necessary. • We assume Basel-City will be able to reduce its tax-supported debt burden over the next few years thanks to significant surpluses in 2019 and 2020.

Outlook

The stable outlook reflects our view that Basel-City will continue to achieve sound budgetary performance over the next few years, despite pandemic-related economic headwinds. We regard potential deficits after capital accounts as small and temporary.

Downside scenario

All other factors 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, which we expect to remain despite a recession in Switzerland following lockdown measures to fight the spread of the pandemic. Extraordinary high tax revenue from 2019 to 2021, partly a one-off, will help the canton to more than digest the financial effects of the COVID-19 pandemic. The canton was also able to reduce its direct debt burden, so it will not need to borrow debt in 2020. The ratings also benefit from the canton's high flexibility to alter its tax rates if unforeseen developments occur. The ratings take into account the canton's potentially sizable contingent liabilities from its stake in a commercial bank.

Economic recession will lead to lower tax revenue with a time lag

We expect Switzerland's real GDP will contract by 4.3% in 2020 and rebound by 3.9% in 2021 (for more information see "Economic Research: The Eurozone Is Healing From COVID-19," published on Sept. 24, 2020, on RatingsDirect), with the decline having a lesser effect on Basel-City due to the canton's focus on life sciences. The forecasts reflect our expectation that Switzerland will perform better than neighboring countries in 2020 and 2021. With an estimated national GDP per capita in excess of Swiss francs (CHF) 80,000 (about €75,000) in 2020, Switzerland will remain one of the world's strongest economies under any scenario. As a regional center and economic powerhouse, Basel-City achieves about twice this already very high national average. 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 located in the canton provides jobs that attract a significant number of national and international commuters, helping to keep unemployment at a very low 3.9% in September 2020. This is slightly higher than the national average of 3.2%, and Basel-City's unemployment figures usually follow national trends, which are set to rise following the economic recession in 2020.

The COVID-19 pandemic will cause Swiss GDP to decline substantially in 2020. Tax collection mechanics lead to a lag of about one year, since tax revenue is billed on the previous year profits or personal income. We assume one-off revenue in 2021 will more than offset the reduction in Basel-City's tax revenue, since the canton does not need to make any additional expenditure to fight the continuing spread of the virus. We consider the COVID-19 pandemic a temporary phenomenon that should not materially harm the canton's budgetary performance.

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 2021, the canton is obliged to pay CHF85 million--about €80 million or equivalent to 2% of operating revenue--to other cantons, down from CHF108 million in 2020. The reduction of Basel-City's contributions compared to previous years reflect changes in the national equalization system, mitigating the effects of the nationwide corporate tax reform (TP17 or TRAF, see "Will The Swiss Tax Reform Plan TP 17 Cost Some Cantons More Than Others?" published Aug. 29, 2020, on RatingsDirect). In short, the reform provides for the discontinuation of certain tax privileges of foreign holdings, domiciliary, and mixed companies. Basel-City used to receive a considerable amount of taxes from these special-status companies, and so is particularly affected by the reform. Parts of the extraordinary tax revenue received from 2019 and 2020 and also expected for 2021 relate to the change in tax system ("Patentbox").

We think the Swiss cantons' institutional framework is developed and extremely predictable, with major reforms planned well in advance and widely discussed, notably between the government and the cantons, and among the cantons themselves. All Swiss cantons also benefit from increased payouts by the Swiss national bank (SNB; for more information see "Bulletin: Swiss Cantons Will Receive Greater Payouts From SNB, But Will It Last?", published on March 3, 2020, on RatingsDirect).

We think the canton's management has created enough financial headroom to deal with both the corporate tax reform and the pandemic. The canton regularly outperforms its budgetary plans, thanks to higher tax revenue and tight expenditure control. The canton intends to publish interim results twice a year, starting in 2020. We also note that the canton enjoys high flexibility to alter its tax rates if unforeseen developments arise. Compared with national peers, Basel-City additionally has the flexibility to alter municipal revenue if necessary.

Multiple one-offs have helped Basel-City achieve excellent budgetary surpluses and debt reduction

Basel-City achieved excellent budgetary results in 2018 and 2019, with very high surpluses after capital accounts. We think the canton is very likely to outperform 2020 budgetary figures thanks to one-off revenue and increased payouts from the SNB more than covering the extra expenditure of slightly more than CHF130 million during the COVID-19 pandemic. In our base case, we assume the tax code changes and lower tax revenue might reduce the operating surplus to still sound levels of 5%-8% of operating revenue, with small deficits after capital accounts of 0.5%-3.6% of operating revenue from 2021 to 2023 following the canton's plans to increase investments. We note that increased uncertainties following the current second wave of the COVID-19 pandemic might change this forecast, but we think the canton has enough budgetary flexibility to mitigate additional pressure if necessary. We view the potential deficits as a structural deterioration compared with the extraordinary high surpluses after capital accounts achieved in recent years.

Thanks to past budgetary surpluses, the canton was able to considerably reduce its debt burden and is likely to refrain from debt issuance in 2020. We therefore expect Basel-City's direct debt to drop to 59% of operating revenue in 2020 and increase to 68% by 2022. The canton does not have any outstanding debt denominated in foreign currency. Basel-City's main contingent liability is Basler Kantonalbank, its cantonal bank, since the canton legally guarantees almost all of the bank's liabilities. In our opinion, Basel-City's creditworthiness could suffer 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 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 it 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 that 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) -- Key Statistics

Mil. CHF	2017	2018	2019	2020bc	2021bc	2022bc	2023bc
Operating revenue	4,144	4,200	4,725	4,370	4,255	4,262	4,323
Operating expenditure	3,648	3,672	3,811	3,999	3,932	4,026	4,078

Table 1

Basel-City (Canton of) -- Key Statistics (cont.)							
Mil. CHF	**2017**	**2018**	**2019**	**2020bc**	**2021bc**	**2022bc**	**2023bc**
Operating balance	496	528	915	371	323	236	245
Operating balance (% of operating revenue)	12.0	12.6	19.4	8.5	7.6	5.5	5.7
Capital revenue	19	10	8	3	10	15	20
Capital expenditure	513	321	277	350	355	372	420
Balance after capital accounts	2	217	645	24	(22)	(121)	(155)
Balance after capital accounts (% of total revenue)	0.0	5.2	13.6	0.5	(0.5)	(2.8)	(3.6)
Debt repaid	300	803	400	600	400	525	500
Gross borrowings	200	809	450	0	500	720	720
Balance after borrowings	(184)	185	674	(476)	(0)	6	(5)
Direct debt (outstanding at year-end)	3,772	3,778	3,190	2,590	2,690	2,885	3,105
Direct debt (% of operating revenue)	91.0	90.0	67.5	59.3	63.2	67.7	71.8
Tax-supported debt (outstanding at year-end)	3,772	3,778	3,190	2,590	2,690	2,885	3,105
Tax-supported debt (% of consolidated operating revenue)	91.0	90.0	67.5	59.3	63.2	67.7	71.8
Interest (% of operating revenue)	0.7	0.7	0.5	0.4	0.2	0.4	0.6
Local GDP per capita (single units)	185,826	191,382	191,937	182,552	190,164	196,572	201,447
National GDP per capita (single units)	81,764	84,219	84,466	80,338	83,713	86,553	88,715

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. 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 12, 2020. An interactive version is available at http://www.spratings.com/sri
- Research Update: Switzerland 'AAA/A-1+' Ratings Affirmed; Outlook Stable; Aug. 21, 2020
- Swiss Canton of Basel-City 'AAA/A-1+' Ratings Affirmed; Outlook Stable, Nov. 8, 2019

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: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Credit Conditions Europe: Ill-Prepared For Winter, Sept. 29, 2020
- Economic Research: The Eurozone Is Healing From COVID-19, Sept. 24, 2020
- Comparative Statistics: European Local And Regional Government Risk Indicators, June 30, 2020
- COVID-19 Will Test The Financial Flexibility Of LRGs In Germany, Switzerland, And Austria; April 27, 2020
- Bulletin: Swiss Cantons Will Receive Greater Payouts From SNB, But Will It Last? March 3, 2020
- Local Government Debt In Germany, Switzerland, And Austria For 2020, March 2, 2020
- Basler Kantonalbank; Dec 17, 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
- Banking Industry Country Risk Assessment: Switzerland, Nov. 30, 2018
- Public Finance System Overview: Swiss Cantons, Nov. 20, 2018
- Will The Swiss Tax Reform Plan TP 17 Cost Some Cantons More Than Others?, Aug. 29, 2018

Ratings Detail (As Of November 6, 2020)*	
Basel-City (Canton of)	
Issuer Credit Rating	AAA/Stable/A-1+
Senior Unsecured	AAA
Issuer Credit Ratings History	
09-Nov-2018	AAA/Stable/A-1+
10-Nov-2017	AA+/Positive/A-1+

Ratings Detail (As Of November 6, 2020)*(cont.)	
16-Jun-2009	AA+/Stable/A-1+

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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