Research Update:

Swiss Canton of Basel-Country Outlook Revised To Positive; 'AA+/A-1+' Ratings Affirmed

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Overview

- Basel-Country's budgetary performance showed stronger-than-expected resilience to COVID-19 headwinds, and we believe performance will improve from 2021.
- We believe Basel-Country's financial management will be able to maintain positive balances after capital accounts and debt reduction.
- Basel-Country's debt burden is set to decrease in 2022 thanks to a large maturity, which will be covered from withholding tax receivables currently deposited at the Swiss Confederation's treasury.
- We therefore revised our outlook on Basel-Country to positive from stable, and affirmed our 'AA+' long-term and 'A-1+' short-term ratings.

Rating Action

On Nov. 5, 2021, S&P Global Ratings revised the outlook on the Swiss Canton of Basel-Country to positive from stable. At the same time, we affirmed the 'AA+/A-1+' long- and short-term issuer credit ratings.

Outlook

The positive outlook reflects our view that Basel-Country's financial management will enact the policies needed to sustain healthy budgetary performance over the coming years. Additionally, we forecast the canton will reduce its debt burden by repaying its large bond maturity in 2022, fully from reserves.

Upside scenario

A positive rating action could occur in the next two years if Basel-Country's financial management maintains a positive budgetary performance, with continuous surpluses after capital expenditure (capex), and reduces its debt burden by using available reserves. This could prompt us to positively reassess the canton's financial management.

Downside scenario

We could revise the outlook to stable within the next 24 months if, due to weaker operating margins or significantly higher capex, financial results deteriorate, creating small structural deficits in the near term. If the canton failed to apply its accumulated reserves to debt repayment, we could also revise the outlook to stable.

Rationale

Despite the challenging macroeconomic environment during the COVID-19 pandemic, Basel-Country showed stronger-than-expected resilience. We believe that the canton will be able to manage the financial fallout in 2021 and subsequent years. At the same time, we note that Basel-Country has benefited from its diversified economic structure, based on the wholesaling/logistic, business services, capital goods, and pharmaceutical/chemical industries, which weathered pandemic impacts well.

Although we believe budgetary performance won't reach the 2019 levels yet, there is a high likelihood financial results will remain healthy and reflect strong operating balances and narrow surpluses after capex. This, together with accumulated withholding tax receivables currently parked at the national treasury, will allow Basel-Country to continue decreasing its direct debt while retaining strong liquidity over the coming years. Furthermore, we do not expect a crystallization of contingent liabilities for Basel-Country.

The canton is up against relatively mild pandemic impacts and continues to benefit from a predictable institutional framework

Switzerland's strong economy and an extraordinarily high national GDP per capita, at Swiss franc (CHF) 81,200 (equivalent to almost $86,500) for 2020, continue to provide a strong backdrop for our ratings on Basel-Country. The canton's GDP per capita is only about 88% of the national average, but this still constitutes a very high level of wealth in an international comparison. We note that Basel-Country's economy is diversified, with logistic/wholesaling, business services, capital goods, and chemicals/pharmaceuticals having the largest presence. As such, sectors severely affected by the pandemic, such as hospitality, have a limited share in the local economy. This has curbed increases in the unemployment rate; it hardly moved last year and remains marginally below the Swiss national average.

We consider the institutional framework, under which all Swiss cantons operate, as one of the most predictable and transparent globally. Basel-Country remains a marginal recipient of payments under the Swiss national fiscal equalization scheme, but amounts are negligible.

Switzerland's economic assistance programs to mitigate the impact of COVID-19 were almost exclusively financed at the federal level. This, in our view, accentuates the strong supportiveness of the existing institutional framework for cantons. Basel-Country's had its own supplemental and self-funded local assistance program.

The canton's financial management continues to pursue reforms designed to improve its economic competitiveness. We understand there are plans to realign the taxation of individuals' income and wealth to make the canton a more attractive place of residence for higher-earning taxpayers. Overall, we expect Basel-Country's management to carefully balance long-term strategic initiatives with budgetary constraints.

The financial management is prioritizing debt reduction and maintaining marginal surpluses after capital accounts

Because of pandemic impacts, Basel-Country will likely record deficits after capital accounts during 2021. However, we believe that the financial management will implement the policies needed to maintain positive marginal surpluses after capital accounts in the next years. Basel-Country will benefit from the national economic rebound, high transfers in the form of Swiss National Bank profit distributions, and small, positive inter-cantonal equalization payments. Basel-Country's capex targets roads, building construction, and public transport.

The canton started 2021 with CHF625.3 million of cash and cash-like assets and only CHF85 million of debt maturing in 2021. Despite factoring in CHF100 million of occasional intrayear, short-term borrowing outstanding to our modelling, we continue to assess Basel-Country's liquidity as exceptional. This is primarily thanks to the volume of committed and uncommitted credit lines the canton has established with financial institutions and, in our view, its strong access to the deep capital market for Swiss cantonal borrowers.

Additionally, the canton has high withholding tax receipts parked with the federal treasury, which amounted to CHF606 million in August 2021. We understand that the treasury management intends to liquidate the material withholding tax receivables position with the central government in order to repay the CHF540 million bond maturity in 2022.

We assume Basel-Country will maintain a moderate ratio of debt to operating revenue before our adjustment for contingent liability risk. However, the canton's debt exceeds that of its equally rated domestic peers. A large part stems from past capital injections into the canton's pension fund, which is now fully funded. Considering our assumption that the canton will use its reserve to repay--rather than refinance its 2022 bond maturity--we anticipate Basel-Country's debt will decline markedly to well below 100% of operating revenue by 2022, after a small, COVID-19-related uptick in 2020. The canton follows a conservative debt-management approach, with predominantly fixed-rate, long-dated funding instruments and no foreign currency exposure.

Profitable and well capitalized, Basellandschaftliche Kantonalbank (BLKB) remains a key element of our contingent liability analysis, weighing on our debt assessment. Our view stems primarily from its balance sheet size of almost 10x Basel-Country's operating revenue and the canton's statutory guarantee for practically all liabilities of BLKB. Other contingent liabilities are, in our view, of secondary importance from a cash flow perspective.

Key Statistics

Table 1

Basel-Country (Canton of) -- Selected Indicators

	-Fiscal year ends Dec. 31--					
(Mil. €)	**2018**	**2019**	**2020**	**2021bc**	**2022bc**	**2023bc**
Operating revenues	2,773	2,844	2,720	2,852	2,881	2,875
Operating expenditures	2,489	2,477	2,632	2,689	2,691	2,683
Operating balance	283	366	88	163	190	191

Table 1

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

	-Fiscal year ends Dec. 31--					
(Mil. €)	2018	2019	2020	2021bc	2022bc	2023bc
Operating balance (% of operating revenues)	10.2	12.9	3.2	5.7	6.6	6.7
Capital revenues	28	21	25	18	22	21
Capital expenditures	320	183	203	199	195	208
Balance after capital accounts	(9)	204	(91)	(18)	17	5
Balance after capital accounts (% of total revenues)	(0.3)	7.1	(3.3)	(0.6)	0.6	0.2
Debt repaid	267	460	50	185	640	100
Gross borrowings	294	272	100	100	100	100
Balance after borrowings	(9)	4	(42)	(98)	(518)	10
Direct debt (outstanding at year-end)	3,075	2,888	2,936	2,851	2,311	2,311
Direct debt (% of operating revenues)	110.9	101.5	107.9	100.0	80.2	80.4
Tax-supported debt (outstanding at year-end)	3,096	2,902	2,961	2,886	2,357	2,368
Tax-supported debt (% of consolidated operating revenues)	110.4	100.8	107.7	100.0	80.8	81.4
Interest (% of operating revenues)	1.3	1.2	1.2	1.1	1.0	0.9
Local GDP per capita (single units)	73,550	73,763	70,982	73,069	75,225	76,609
National GDP per capita (single units)	84,179	84,500	81,455	83,789	86,243	87,916

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.

Ratings Score Snapshot

Table 2

Basel-Country (Canton of) -- Ratings Score Snapshot

Key rating factors	Scores
Institutional framework	1
Economy	1
Financial management	2
Budgetary perfomance	1
Liquidity	1
Debt burden	4
Stand-alone credit profile	aa+

Table 2

Basel-Country (Canton of) -- Ratings Score Snapshot (cont.)

Key rating factors	Scores
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 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, 2021. A free interactive version is available at 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: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Full Analysis: Switzerland, Aug. 23, 2021
- Institutional Framework Assessments For International Local And Regional Governments, Nov. 4, 2021
- Local Government Debt 2021: COVID Aftershocks Push German And Austrian LRGs Into Heavy Borrowing, March 25, 2021,
- Local Government Debt 2021: The Pandemic Takes More Of The Shine Off Large Developed Regions' Credit Quality, March 25, 2021
- Local Government Debt 2021: Global Borrowing To Hit $2.25 Trillion, March 25, 2021
- Swiss National Bank's Higher Payout To Government Offers Budgetary Relief, Feb. 3, 2021
- Institutional Framework Assessment: Swiss Cantons, Jan. 14, 2021
- Local And Regional Governments Outlook 2021: Gradual Recovery Will Test Rating Resilience, Dec. 10, 2020
- Basellandschaftliche Kantonalbank, Nov. 10, 2020

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; Outlook Action

	To	From
Basel-Country (Canton of)		
Issuer Credit Rating	AA+/Positive/A-1+	AA+/Stable/A-1+
Senior Unsecured	AA+	AA+