Geneva (Republic and Canton of)

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**Major Rating Factors**

**Strengths:**
- "Predictable and supportive" institutional framework.
- "Positive" financial management.
- Wealthy and resilient economy.

**Weaknesses:**
- High debt burden.
- Sizable unfunded pension liabilities.
- Cyclical revenue and social-related expenditure base.

**Rationale**

The rating on the Swiss Republic and Canton of Geneva reflects Standard & Poor's Ratings Services' view of the "predictable and supportive" institutional framework for Swiss cantons, as well as Geneva's wealthy and resilient economy and its "positive" financial management. The rating is constrained, however, by the canton's heavy debt burden, its sizable unfunded pension liabilities, and the sensitivity of its budget to economic cycles.

Swiss cantons benefit from an extremely stable and predictable political and institutional system, which we assess as "predictable and supportive" under our methodology for rating international local and regional governments.

We view Geneva's financial management as "positive" for its credit standing, given its high transparency and prudent debt and liquidity management.

The rating also benefits from Geneva's wealthy and resilient economy owing to its status as an important financial and international center, demonstrated by GDP per capita exceeding Swiss francs (CHF)98,000 at year-end 2011. This fuels the canton's tax revenue, which makes up the bulk of its operating revenue (75% in 2011). We note, however, that Geneva's economic prospects are more uncertain. The size of its financial sector and international scrutiny of the tax advantages granted to holding companies in Switzerland could become risks in the medium term.

In 2011, the canton posted a low 4% operating margin (before amortization), up from 3% in 2010, but well short of the 10% average over 2006-2009. Geneva posted high revenue growth of 7% in 2011, primarily driven by tax revenue, notably corporate profit tax. Despite this increase, though, the operating margin remains tight, reflecting high operating expenditure, up 5% in 2011, especially due to increased social charges.

After historically high net investments in 2010 of CHF0.65 billion, net capital expenditure decreased to CHF0.58 billion in 2011 and deficit after capital accounts to 3% from 6% in 2010. Still, Geneva's debt increased in 2011 beyond its investment funding requirements, owing to high working capital needs, contrary to trends until 2010. This is primarily because the canton made quicker payments to the Swiss Confederation and to operators and also had to refund some taxpayers for tax advances. The canton's direct debt therefore increased by CHF0.74 billion to CHF11.2 billion (or
146% of operating revenue). We view Geneva's tax-supported debt (including its direct debt and that of its non self-supporting dependent entities) at year-end 2011 as very high, at 138% of consolidated revenue.

Under our base-case scenario, we project some deterioration in Geneva's operating margin until 2014. In light of less favorable economic prospects, we now estimate that operating revenue will grow at an average annual 1.4% over 2012-2014 (including 2% average annual growth in tax revenue), while operating expenditure will grow by 2.3% on average annually. Therefore, under our base-case scenario, the operating margin will decrease to 1.5% in 2014. While partly reflecting some internal decisions (tax cuts and allowances for families), this deterioration largely results from the impact of less favorable economic conditions on tax revenue growth and social expenditure. It also stems from some external factors, such as new charges reflecting changes in national legislation on unemployment benefits and hospital funding, growing transfers under the cantonal equalization system, and a diminishing share in net profits from the Swiss National Bank.

We anticipate that the decrease in operating margin will result in increasing debt, despite the canton's recent decision to adjust its ambitious capital investment program in 2012-2014. Our base-case scenario anticipates an average CHF725 million of net capital investments from 2012 to 2014, including a sizable cash injection into the canton's public pension funds in 2013. As a result, we expect the deficit after capital investment will reach about 6% in 2012-2014. We project that tax-supported debt will increase to a high 156% of operating revenue at year-end 2014.

Geneva posted unfunded pension liabilities of CHF6.56 billion at year-end 2011, accounting for more than 85% of its operating revenue. These liabilities are very high by international standards, and we expect them to increase from 2012 given the lower technical interest rate of 3.5% compared with 4.5% previously. Under our base-case scenario, we expect the comprehensive reform of the canton's public pension funds—which will be subject to a popular referendum in March 2013-- to be carried out with limited cash injections by the canton. In the absence of such a reform, the canton would have to fully recapitalize its public pension funds and create a reserve fund. This recapitalization would require the canton to take on significant new debt, which would increase its debt burden and weigh on its future budgetary performance, and consequently place pressure on the rating.

**Liquidity**

We assess Geneva's liquidity as "neutral." The canton aims to limit its average level of debt and actively uses short-term debt and its contracted and non-contracted liquidity lines to manage its daily cash flows. We estimate that Geneva's average available amounts on its contracted bank lines will represent around 70% of its total debt service over the next 12 months.

In our view, the canton has strong access to external liquidity as reflected by its regular access to capital markets (with frequent issuance of public bonds) and sizable treasury facilities. Geneva currently benefits from extensive short-term facilities, comprising CHF1.17 billion of contracted bank lines (with six counterparties) and CHF2.68 billion of non-contracted liquidity lines with more than 10 public sector entities and Swiss and international banks.
Outlook

The stable outlook reflects our base-case scenario expectations that Geneva will contain the deterioration of its operating margin and limit its deficit after capital accounts to below 10% of total revenue in 2012-2014.

Under our upside scenario, we would consider raising the rating if Geneva enhanced its operating balance, structurally trimmed its deficit after capital accounts to below 5%, and reduced its unfunded pension liabilities.

Under our downside scenario, we would consider lowering the rating if the canton recorded a structurally growing deficit after capital accounts exceeding 10% on average in 2012-2014, which could lead us to revise downward our assessment of its financial management. The rating could also come under downward pressure if the canton failed to structurally reform its public pension funds before year-end 2013 and limited the related cash injection.

However, we view both our upside and downside scenarios as very unlikely at this stage.

Comparative Analysis

We consider that most of Geneva's peers operate under a "predictable and supportive" institutional framework, the highest score on a scale ranging from '1' (highest score) to '6' (lowest score). The only two exceptions are the City of Geneva (AA-/Stable/--) and the region of Brussels-Capital (AA/Negative/--), for which we view the institutional framework as "predictable and well-balanced," with a score of '2'.

Geneva and all of its peers benefit from very favorable economic profiles.

We assess Geneva's financial management as "positive," similar to that of the City of Geneva and the Canton of Basel-City (AA+/Stable/A-1+). We view the other peers' financial management as "very positive."

We believe that the City of Geneva and Stockholm County Council (AA+/Stable/A-1+) are less exposed to off-balance-sheet commitments than peers, especially compared with the cantons of Geneva and Vaud (AA+/Positive/--), which are majority shareholders in cantonal banks.

We view Geneva's liquidity position as "neutral," as we do Brussels-Capital's and the City of Geneva's, while we view that of other peers as "positive."

Geneva reports the highest debt burden among peers--though in line with the City of Geneva--and has much highest unfunded pension fund liabilities.

The Canton on Vaud and the City of Geneva record the most solid budgetary performance among peers. We project they will face limited funding needs in 2012-2014, in contrast with other peers.
### Table 1

<table>
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<th>Canton of Geneva 2012 Peer Comparison</th>
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<tr>
<td><strong>Issuer Credit Rating</strong></td>
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<td>Geneva (Republic and Canton of)</td>
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<tr>
<td>AA+/Stable/A-1+</td>
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<td>AA+/Positive/--</td>
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### Predictable And Supportive Institutional Framework

In our view, Swiss cantons benefit from an extremely stable and predictable political and institutional system, which we assess as predictable and supportive under our methodology for rating international local and regional governments. The score assigned to the institutional framework of Swiss cantons is '1', the highest on a scale of one to six.

The main characteristics of the institutional framework for Swiss cantons are detailed in "Public Finance System Overview: Swiss Cantons," published on July 30, 2009 on RatingsDirect on the Global Credit Portal. In this analysis, we will focus on the cantonal equalization system and the modified law for public pension funds.

**Geneva is a net contributor to the Swiss cantonal equalization system**

Switzerland supports financial equalization among the cantons under its constitution. This leads to a very strong revenue and expenditure balance for the cantons.

Switzerland reformed the cantonal equalization system (CES) in 2008, largely based on three funds:

- A revenue-related equalization fund that aims to reduce financial and tax disparities among cantons. Switzerland finances this fund, and provided CHF2.1 billion in 2012 with CHF2.2 billion expected for 2013. Cantons with high revenue potential also contribute, having given CHF1.45 billion in 2012 with CHF1.5 billion expected for 2013.
- An expenditure-related equalization fund that compensates for the excessive charges that some cantons incur because of their topography, demography, or social characteristics. Switzerland contributed CHF738 million to this funding in 2012, and is expected to contribute CHF730 million in 2013.
A temporary “neutralization” fund that is set to temporarily compensate for the effect of implementing CES. In 2012 the state contributed CHF244 million and the cantons CHF122 million to this fund. In 2013 the state will contribute CHF239 million and the cantons CHF120 million.

Eight cantons are net contributors to the CES in 2012: Zurich (CHF432 million), Zug (CHF263 million), Geneva (CHF246 million), Schwytz (CHF108 million), Basel-City (CHF101 million), Vaud (CHF28 million), Nidwald (CHF14 million), and Basel-Country (CHF10 million). In 2013, Geneva's contributions will increase to CHF257 million.

A structural reform of pension funds before January 2014

The new federal law on public pension funds came into effect on Jan. 1, 2012. It includes a minimum mandatory coverage ratio of future pensions by reserves of 80% for public pension funds, to be achieved within a 40-year period, or no later than 2052, with two successive thresholds of 60% in 2020 and 75% in 2030. Public pension funds have a transition period until Jan. 1, 2014, to apply this new regulation, and under our base-case scenario, we expect Geneva to reform its pension funds over this period.

A Wealthy And Resilient Economy

A small territory with a dynamic demographic profile

Geneva is a small, densely populated Swiss canton with 468,741 inhabitants at end-October 2012, up 0.6% from the same date the previous year. Geneva's population dynamics outpace the national average, increasing by an average 1.1% in 2001-2010 compared with 0.9% nationwide, despite the canton's small territory and very low housing supply. This robust growth in population has been mostly triggered by positive net immigration. The proportion of non-Swiss nationals in the canton is high, at 40% of the its population at the end of 2011, and almost twice the national level. Most foreigners are of working age.

According to recent estimates by the cantonal statistics office, based on current trends the cantonal population could gain around 112,000 inhabitants from 2010-2035. This population growth will translate into increasing education, health and social care, and public infrastructure cost, but it also fuels tax bases. We note that while Geneva's population is currently fairly young, demographic ageing will result in 20% of the population being over 65 in 2040 compared with 16% in 2011, and a doubling of people over 80 to 40,000 residents in 2040 compared with 2011. That means the canton will have to build new homes and home-care systems.

A wealthy and resilient economy, though growth prospects are less certain

Based on cantonal estimates from Office Cantonal de la Statistique; OCSTAT), Geneva reported very high GDP per capita at CHF98,346 (over $110,000) in 2011. Geneva's GDP per capita has exceeded the Swiss average by over 30% since 2001 and the canton has the highest salaries in Switzerland, according to data from the Swiss statistics office (OFS), which is positive because about 50% of the canton's operating revenues are derived from personal income tax. High-value-added operations are concentrated in Geneva, demonstrated by its gross value added (GVA) per worker, which was around 12% above the national average in 2011.

Geneva also has an exceptionally large employment base, with two jobs for every three inhabitants, reflecting its attractiveness to businesses and their employees. The number of cross-border workers--those who live in France but work in Geneva--has doubled since 2002 and now represents around 20% of the canton's jobs.
Geneva is experiencing a faster economic rebound following the 2007-2008 world economic recession than Switzerland—its GDP grew 2.6% in 2011 compared with 1.9% for Switzerland. But Geneva's economic fabric depends on the global economic situation, so its economic prospects are uncertain given sluggish global growth and the negative impact of a strong Swiss franc on exports. Recent economic forecasts from Geneva's Groupe de Prévisions Économiques in December 2012 anticipated slow growth in 2012 (1.2%), 2013 (1.7%) and 2014 (2%). Under our base-case scenario, we expect Geneva's economic growth to slightly outpace Switzerland's, which we view as stagnating for 2012 at 0.1%, but recovering to 1.2% in 2013 and 2.4% in 2014.

A diversified economy, though the significant importance of banking activities and holding companies could become risks in the medium term

The cantonal economy has increasingly diversified since the beginning of the 1990s. Services made up 85% of the workforce, excluding agriculture, as of September 2008. Public and semi-public activities including health, education, and social services contributed about 22.1% of Geneva's GDP in 2010 (most recent data available). Retail and wholesale trade activities represented 16% of cantonal GDP and business services represented 12.7% in 2010. The industrial sector, excluding construction, is comparatively modest in employment terms, as it accounted for 9.6% of the cantonal workforce as of September 2008, but it is focused on high-value-added activities such as high technology, luxury goods—particularly jewelry and watches—telecommunications, fine chemicals, and biotechnologies. These sectors are largely geared toward international markets and they make up the bulk of Geneva's exports, with concentration on high-growth countries, especially in Asia.

The public and semi-public sector employed about 24.5% of the canton's workforce as of September 2008, which provides significant stability to the employment base. This stems from the presence of a wide variety of international organizations. Although most of their personnel are tax exempt, these employees contribute to Geneva's development through their exceptional skills and high purchasing power, while their organizations pay corporate taxes. Geneva is also a worldwide center for conference activities and business tourism.

Geneva's financial sector now ranks second in terms of its weight in the cantonal GDP, representing 21.2% in 2010, and 10 of the canton's 30 biggest employers are financial institutions. Compared with other financial centers such as Zurich, Geneva was relatively sheltered from the recent turmoil in the capital markets because investment banking is not its main financial activity. Instead, the canton's financial institutions primarily focus on asset management and commodities trading. Although the crisis has also damaged these sectors, they have shown more resilience. In addition, some important hedge funds decided to settle in Geneva over recent years.

However, current efforts to combat against tax evasion and fraud, especially from the EU, could negatively affect the Swiss banking sector, including Geneva. We cannot assess their potential financial influence on the canton's finances at this time. Overall, we expect the financial sector, which has been the main impetus behind tax revenue growth accounting for over a third of the corporate tax, to post lower margins and profits and possibly to reduce or limit staff and compensation, leading to lower tax revenues for the canton.

We also note that the Swiss government and the EU have started talks on tax advantages granted to holding companies in Switzerland, which the EU would like to see abolished. These companies account for about 20,000 direct jobs and 50,000 including indirect jobs in Geneva and they pay around CHF1 billion in cantonal and municipal taxes. If
these tax advantages rebates were abolished, the canton estimates that, in the absence of a reduction in cantonal and municipal taxes, most companies would leave Geneva, resulting in a significant loss of jobs and tax revenues. As a consequence, Geneva is considering a reduction in the corporate profit tax in 2017-2018, which would cut the canton's tax revenues by CHF400 million, and the municipalities', mostly the City of Geneva, by CHF70 million. If that happened, the canton would have to compensate its constituent cities for their loss in tax revenues. The canton believes it may be eligible for compensation from the Swiss government, for example in the form of a reduction of its transfers to the cantonal equalization system.

Positive Financial Management

Under our methodology for rating international local and regional governments, we view the canton's financial management as positive for its creditworthiness.

Consensus-based governance supporting fiscal balance strategy

The canton's citizens choose Geneva's parliament and government for five-year terms in simultaneous elections. The parliament is dominated by a right-wing majority coalition, and a small right-wing majority holds the government with four seats out of seven. Consensus-based governance is favored by the semi-direct democratic system, using frequent referenda. The next elections are scheduled for October 2013.

Geneva's law on financial management postulates a balanced operating budget--if there is a deficit it must not exceed a canton's specific reserve. Assumptions for the budget are generally prudent, especially with regard to resources. In addition, if the canton posts two consecutive years of deficit under International Public Sector Accounting Standards (IPSAS) standards, its parliament must submit measures to popular vote through a referendum with clear set options--increasing tax rates or reducing expenditure to reach a balanced budget.

However, the canton's parliament can avoid this process if financial projections show that after two years in operating deficit it is most likely to return to a positive operating balance the following year.

At the end of 2011, the canton's government introduced a set of new measures under its 2012-2015 multiyear financial plan to generate additional revenues and curb operating expenditure, with the goal of a total positive financial impact of CHF0.65 billion in 2012-2015. Through these measures, the government aims to prevent any structural deterioration of its budgetary situation and to balance its accounts by the end of 2014 under IPSAS standards. However, the canton's parliament opposes some of the measures, including new taxes. Under the draft 2013 budget, the canton's government therefore skipped some measures and introduced sharper controls over operating expenditure, capping it at 1.5% growth per year from 2013-2016, and limiting net capital expenditure (capex) at CHF500 million per year from 2013-2016, with the aim of reaching a balanced operating budget in 2016. Contrary to previous years, parliament rejected this draft budget in October 2012, and as a result the operating and investment charges budgeted in 2012 will be rolled over for the first half of 2013.

High level of transparency and disclosure

We view Geneva's financial accounts as well-documented, comprehensive, and disclosed in a timely manner. Since 2010 the canton has publicly provided consolidated accounts, including for cantonal companies like transport, airport,
hospital, and multi-utility companies, along with its own accounts.

The canton applies consistent principles based on accrual accounting and annually posts balance sheets. It reports its budgets and accounts according to IPSAS standards. In this report we systematically refer to cash-adjusted figures.

Geneva makes four-year projections, which are updated annually. The latest one (2013-2016) was published in December 2012. These projections include clear-cut and conservative expectations that comply with publicly released fiscal targets.

The Accounts Court ("Cour des Comptes") has been in charge of performing an independent audit of the canton, the cantonal companies, and its subsidized organizations, since 2005. Geneva's authorities have close relationships with the companies in which the canton holds stakes to monitor their economic and financial situations. All organizations that benefit from the canton's subsidies must provide their financial accounts.

**Efficient budgeting and cost monitoring**

Cost-control is the main impetus of budget decisions, even though the operating part is increment-based. We note some deviations between actual and budgeted figures for revenues owing to the canton's tax estimation system, which does not allow fully reliable tax projections.

Geneva exercises intense budgetary monitoring through monthly reporting on expenditures and revenues. The provisioning policy is subject to cantonal laws and, in our view, is currently quite conservative, especially for taxes--the provision represents around 7% of tax receivables while 3% are usually never collected.

**Prudent debt and cash management**

We view Geneva's medium-term debt policy as well formulated and prudent. It limits the use of derivatives to simple, plain-vanilla operations. This strategy has the following goals for 2013:

- Limiting the average interest rate to 2.2%;
- Reporting exposure to variable rates not higher than 30% of the stock of debt;
- Containing short-term debt at 25% of total debt; and
- Targeting an average maturity of medium- and long-term debt of 8 years.

The canton also aims to smooth its annual debt amortization profile to around CHF800 million after 2013, and avoid a significant debt redemption peak in the course of the year.

We view cantonal cash management as efficient and proactive. Geneva has a cash pooling system consolidating the treasury management of all cantonal departments and the most significant cantonal companies. This system helps to limit debt recourse and related interest charges. The canton has contracted short-term facilities for CHF1.17 billion with 6 counterparties, and benefits from CHF2.68 billion of non-contracted liquidity lines with over 10 public sector entities and Swiss and international banks. These lines cover its infra-annual cash needs.

**Budgetary Flexibility**
Low flexibility in practice on tax revenues

Although, like all Swiss cantons, Geneva has extensive legal flexibility in setting personal income and corporate profit tax rates, we regard its revenue raising flexibility as limited, because:

- A referendum is necessary to approve any change in the tax code. Tax hikes are therefore difficult to implement, as shown by referenda held in 2005 and 2007; and
- There is strong tax competition between cantons. This was confirmed by recently-decided tax cuts by the cantons of Neuchatel (not rated) and Jura (not rated), which may prompt other cantons to also reduce their own tax rates.

Geneva’s operating revenues are largely composed of locally-collected taxes (see chart 1). These are sensitive to economic cycles, notably the corporate tax, but they are mostly levied on individuals, which limits their volatility. The canton estimates that a 1% change in Swiss GDP currently has a CHF70 million impact on Geneva’s tax revenues levied on households, which is quite limited, accounting for 1.2% of tax revenue in 2011. We note that there is, however, some concentration in personal income tax, which includes taxes on affluent people and private bankers.

Corporate tax represents a comparatively high share of operating revenue—at 16% in 2011 compared with 8% for Vaud—and has evolved erratically over recent years, reflecting high concentration on a few large companies—the 20 biggest taxpayers accounted for 35% of corporate profit tax in 2010. A 9% fall in revenue from the corporate profit tax in 2010, as in 2009, followed by a 15% rebound in 2011 illustrates this volatility.

Chart 1

Canton of Geneva 2011 Adjusted Operating Revenues

Source: Canton’s 2011 Standard & Poor’s-adjusted accounts 2011.
© Standard & Poor’s 2013.
Fairly rigid cost structure
The canton's expenditure flexibility is limited by the high proportion of operating costs in its budget--they accounted for 90% of total spending in 2011. In addition, 95% of operating charges are fixed items, including personnel and financial charges, rigid social and health care subsidies, and subsidies to higher education and public transportation.

Cost control remains a chief priority, as demonstrated in 2011 by the stability of general expenditure and the 0.9% reduction in personnel. We note that the 5% increase in operating expenditure in 2011 related mostly to increasing social charges and additional payments under the cantonal equalization system, which are largely out of the canton's control. We expect a limited increase of 1.2% per year in personnel charges from 2012-2014, as a result of a cap on hiring, cuts in temporary jobs, and limited indexation of wages. These measures are in line with Geneva's 2013-2016 multiyear financial plan.

Sizable reduction in capex
We estimate that Geneva's investment program is flexible. The canton announced in 2012 that it will significantly reduce its capex program to CHF560 million per year, including capital revenues, well below its previous projection and our 2011 estimate of an average CHF900 million per year. We note however that some large projects like the extension of the public transport network, which may experience lags, will offer little flexibility once started because payments will have to be made progressively to companies during the construction periods, implying potential payment peaks.

Budgetary Performance

Projected deterioration in budgetary performance
The economic downturn of 2008-2009 affected cantonal finances from 2010 on tax income--taxes fell 6% in 2010 compared with 2009--and expenditure, especially social expenditures, as subsidies grew by over 3% in 2010. The canton also implemented a package with tax cuts for families. In 2011, the canton posted a low 4% operating margin before amortization, up from 3% in 2010 but short of average 10% margins from 2006-2009. Despite high growth in revenues of 7% in 2011, primarily driven by tax revenues and especially corporate profit tax, the operating margin remains tight, reflecting high operating expenditure which rose 5% in 2011, especially social charges. After historically high net investments of CHF0.65 billion in 2010, net capex fell to CHF0.58 billion in 2011 and the canton's deficit after capital accounts narrowed to 3% from 6% in 2010.

Under our base-case scenario, we project some deterioration in Geneva's operating margin until 2014. In light of less favorable economic prospects, we now estimate that operating revenue will grow at an average annual 1.4% over 2012-2014, including 2% average annual growth in tax revenue, and that operating expenditure will grow by 2.3% on average annually. Therefore, under our base-case scenario, the operating margin will decrease to 1.5% in 2014. While partly reflecting some internal decisions like tax cuts and allowances for families, this deterioration largely results from the impact of less favorable economic conditions on tax revenue growth and social expenditure. It also stems from some external factors, such as new charges reflecting changes in national legislation on unemployment benefits and hospital funding, growing transfers under the cantonal equalization system, and a diminishing share in net profits from the Swiss National Bank.
We expect the deficit after capital investment to reach about 6% in 2012-2014 compared with 3% in 2011 under our base-case scenario, despite the canton's recent decision to adjust its ambitious capital investment program in 2012-2014. This reflects the decrease in the operating margin and a one-off sizable cash injection into the canton's public pension funds in 2013, which we treat as capex under our criteria. Our base-case scenario anticipates an average CHF725 million of net capital investments from 2012 to 2014. We therefore project that the canton's tax-supported debt will increase to a high 156% of operating revenue at year-end 2014.
Under our upside scenario, more buoyant operating revenue at 1.8% per year in 2012-2014 coupled with less dynamic social expenditures would help maintain Geneva's operating margin at about 6% on average in 2012-2014, and contain its deficit after capital accounts at 2% on average over the same period. Under this scenario, Geneva's tax-supported debt burden would grow more slowly to 145% of adjusted consolidated operating revenue at the end of 2014.

Our downside scenario factors in more sluggish operating revenue at 0.7% per year and more dynamic social expenditures, which could lead to a negative operating balance from 2013, at negative 4% by the end of 2014. Taking into account annual net capital investments of CHF808 million on average in 2012-2014, including the cash injection to the public pension funds in 2013, Geneva's deficit after capital accounts could deepen to 10% on average in 2012-2014. Under this downside scenario, tax-supported debt would increase sharply to 170% of operating revenue by the end of 2014.

However, we view both our upside and downside scenarios as unlikely at this stage.
High Debt Burden

High tax-supported debt
We view Geneva's tax-supported debt as high, at 138% of consolidated revenue at the end of 2011. This includes the canton's direct debt as well as that of its non-self-supporting dependent entities, mainly the 100%-controlled public transport operator TPG and public hospital HUG. We project that it will reach 156% by the end of 2014, reflecting mostly increasing direct debt to fund the canton's capex and, to a lesser extent, TPG's increasing debt.

While the canton's direct debt had decreased for four consecutive years from 2006-2010, in 2011 it increased beyond its investment funding requirements, owing to high working capital needs and contrary to trends until 2010. This was primarily because the canton made faster payments to the Switzerland operators, and also had to refund some taxpayers for tax advances. The canton's 2011 direct debt therefore increased by CHF0.74 billion to CHF11.2 billion, or 146% of operating revenue).

Chart 4

Canton of Geneva Debt (Base-Case Scenario)

Debt service represented a high 17% of operating revenue in 2011 compared with 20% in 2010 owing to the structure of the debt, which included significant bullet bonds in 2010-2011 and has a short maturity in an international context. Interest charges represented 3.9% of operating revenues in 2011. Under our base-case scenario, we project that debt
service will represent an average 15% of operating revenue in 2012-2014, reflecting lower interest rates on recently-drawn debt and lower debt repayment installments, and interest charges that we expect to average 3.7% of operating revenues in 2012-2014.

Debt amortization is fairly even at about CHF1 billion in 2012-2013, after significant repayment peaks in 2008-2010 that were still lower than the 2008 CHF1.7 billion peak. The canton is currently aiming to reduce its annual principal repayment to CHF0.8 billion by lengthening its total debt maturity, which was 6.2 years at the end of December 2012, up from 2.3 years at the end of 2002. About 82% of Geneva's long-term debt was at fixed rates at the end of 2012, which largely protected the canton from interest rate risk. Geneva's average interest rate was low at 1.93% at the end of December 2012. In addition, foreign currency debt was limited to 3% of total debt at the end of December 2012, and it was fully hedged through currency swaps to avoid currency risk. The canton has discarded entering into swaps, derivatives, and options beyond plain-vanilla currency or interest rate swaps, with hedging as the sole purpose.

75% of Geneva's direct debt at the end of December 2012 exceeded one year and was mostly made up of private bonds and, to a lesser extent, public bonds. The canton's debt maturing before 12 months stood at 25% of total debt, in line with the internal target set at 25%.

**Sizable unfunded pension liabilities, requiring a capital injection that may be significant if the reform of public pension funds fails**

Geneva recorded unfunded pension liabilities of CHF6.56 billion at the end of 2011 at a 4.5% discount rate, or over 85% of its operating revenue, which is very high by international standards. Pensions are currently managed by four public pension funds. Geneva's pension obligations are based on defined benefits and financed by a mixed of capitalization and pay-as-you-go, except for the Police Pension Fund which is fully capitalized.

We expect unfunded pension liabilities to have increased automatically to around 110% of the canton's operating revenue in 2012, given the use of a lower technical interest rate of 3.5% compared with 4.5% previously, reflecting expected lower capital market returns.

A new national regulation requires a minimum mandatory coverage ratio for Swiss public pension funds with a target of 80% to be achieved within a 40-year period, and the canton drafted a comprehensive reform of its public pension funds in June 2011, to allow its public pension funds to meet new national minimum mandatory coverage ratios and keep their defined benefits and mixed financing. This reform includes the merger of the two largest pension funds--Caisse de Prévoyance du Personnel Enseignant de l'Instruction Publique et des Fonctionnaires de l'Administration du Canton de Genève (CIA) for teachers and Caisse de prévoyance du personnel des établissements publics-médiiaux du canton de Genève (CEH) for medical personnel--which will result in economies of scale and raise the combined fund's coverage ratio and better balance the demographic profile. The reform also includes structural measures like hikes in the retirement age and in contribution rates, and a sizable capital injection into CIA by the canton in 2013, partly in the form of a cash injection and transfers of assets.

The reform was voted on by Geneva's parliament in September 2012, and the law will be subject to a popular referendum in March 2013.
We note that if the law is approved in the March 2013 referendum, the measures reforming the public pension funds will come into force at the end of 2013. If the law is rejected CIA and CEH will no longer fulfil the Swiss legal requirements to keep their mixed financing system. This would require specific measures to rebalance public pension funds unless a new cantonal law was passed before Jan. 1, 2014 including a new financial plan for the public pension funds that would have to be validated by the Cantonal Public Pension Funds Surveillance Authority.

In the absence of a cantonal law merging the two largest public pension funds, under the new national regulation the canton would have to fully capitalize CIA's obligations to its current pensioners, which would cost it about CHF1 billion. If no consensus is found under a new cantonal law to keep the mixed funding scheme for public pension funds, the new national regulation will require full recapitalization of public pension funds, including the creation of a reserve fund accounting for 15% of pension obligations. Based on CIA and CEH's unfunded liabilities at the end of 2011, their 115% capitalization would represent CHF11 billion. This recapitalization—which could be spread over several years—would require the canton to take on significant new debt, which would increase its debt burden, weigh on its future budgetary performance, and consequently place pressure on the rating.

In the extreme case, in the absence of a cantonal law allowing the full capitalization of public pension funds, the surveillance authority could require their closure. The canton would then have to extend its guarantee to allow for the payment of pension obligations.

**Moderate Contingent Liabilities**

We view the canton's contingent liabilities as moderate. We understand it does not currently report any substantial risks related to litigation. Debt guarantees of CHF0.7 billion at the end of 2011 were partly granted to social housing foundations. Debt guarantees granted to the canton's non self-supporting entities like TPG are included in its tax supported-debt.

Until the end of 2009 Geneva's largest contingent liabilities were related to Banque Cantonale de Geneve's (BCGE; A+/Stable/A-1) past problems, related to bad loans and lengthy real-estate problems. BCGE had to be bailed out by the canton in 1999, through an ad hoc defeasance structure set up in 2000, with total estimated losses of CHF1.9 billion for the canton. BCGE's only remaining guarantee from the canton consists of a legal guarantee on a portion of the bank's retail savings deposits, which amounted to CHF5.2 billion in 2011. The canton has decided to progressively remove this guarantee scheme by 2017.

The canton has also granted its guarantee on life annuities proposed by Rentes Genevoises (not rated), a public right, non-for profit, mutual insurance institution. At the end of 2011, these guarantees amounted to CHF1 billion. We view related risk as limited given the entity's current solid coverage ratio.

Geneva is responsible for the supervision of municipalities located in its territory. The canton oversees and approves any decision of municipal councils relating to financial matters. Still, municipalities are autonomous and the canton is not financially responsible for them.
Rating Factor Scores

Table 2

<table>
<thead>
<tr>
<th>Canton of Geneva--Summary Of Published Rating Factor Scores*</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Institutional framework</strong></td>
</tr>
<tr>
<td>Financial management</td>
</tr>
<tr>
<td>Liquidity</td>
</tr>
<tr>
<td>Indicative credit level</td>
</tr>
<tr>
<td>Overriding factors</td>
</tr>
</tbody>
</table>

*Standard & Poor's assigns scores across eight main rating factors, of which we publish three.

Financial Statistics Tables

Table 3

<table>
<thead>
<tr>
<th>Canton of Geneva Financial Statistics--Base-Case Scenario</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Mil. CHF</strong></td>
</tr>
<tr>
<td>Adj. operating revenues</td>
</tr>
<tr>
<td>-Adj. operating expenditures</td>
</tr>
<tr>
<td>=Operating balance</td>
</tr>
<tr>
<td>Operating balance (% of adj. operating revenues)</td>
</tr>
<tr>
<td>+Capital revenues</td>
</tr>
<tr>
<td>-Capital expenditures (capex)</td>
</tr>
<tr>
<td>=balance after capital accounts</td>
</tr>
<tr>
<td>Balance after capital accounts (% of adj. total revenues)</td>
</tr>
<tr>
<td>-debt repaid</td>
</tr>
<tr>
<td>=new borrowings</td>
</tr>
<tr>
<td>Balance after borrowings</td>
</tr>
<tr>
<td>Direct debt (outstanding at year-end)</td>
</tr>
<tr>
<td>Direct debt (% of adjusted operating revenues)</td>
</tr>
<tr>
<td>Tax-supported debt (% of adjusted operating revenues)</td>
</tr>
</tbody>
</table>

CHF--Swiss franc. BC--Standard & Poor’s base-case scenario. Sources: Canton’s annual accounts adjusted by Standard & Poor’s, Standard & Poor’s projections.

Table 4

<table>
<thead>
<tr>
<th>Canton of Geneva Financial Statistics--Downside-Case Scenario</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Mil. CHF</strong></td>
</tr>
<tr>
<td>Adj. operating revenues</td>
</tr>
<tr>
<td>-Adj. operating expenditures</td>
</tr>
<tr>
<td>=Operating balance</td>
</tr>
<tr>
<td>Operating balance (% of adj. operating revenues)</td>
</tr>
<tr>
<td>+Capital revenues</td>
</tr>
<tr>
<td>-Capital expenditures (capex)</td>
</tr>
<tr>
<td>=balance after capital accounts</td>
</tr>
</tbody>
</table>
### Table 4
**Canton of Geneva Financial Statistics—Downside-Case Scenario (cont.)**

<table>
<thead>
<tr>
<th>Balance after capital accounts (% of adj. total revenues)</th>
<th>(12.2)</th>
<th>(15.2)</th>
<th>(3.5)</th>
<th>(3.2)</th>
<th>(6.0)</th>
</tr>
</thead>
<tbody>
<tr>
<td>-debt repaid</td>
<td>726</td>
<td>980</td>
<td>1,011</td>
<td>1,037</td>
<td>1,388</td>
</tr>
<tr>
<td>+new borrowings</td>
<td>1,684</td>
<td>2,182</td>
<td>1,515</td>
<td>1,778</td>
<td>1,132</td>
</tr>
<tr>
<td>Balance after borrowings</td>
<td>0</td>
<td>0</td>
<td>219</td>
<td>487</td>
<td>(699)</td>
</tr>
<tr>
<td>Direct debt (outstanding at year-end)</td>
<td>13,959</td>
<td>13,002</td>
<td>11,800</td>
<td>11,204</td>
<td>10,463</td>
</tr>
<tr>
<td>Direct debt (% of adjusted operating revenues)</td>
<td>179</td>
<td>166</td>
<td>149</td>
<td>146</td>
<td>145</td>
</tr>
<tr>
<td>Tax-supported debt (% of adjusted operating revenues)</td>
<td>169</td>
<td>158</td>
<td>142</td>
<td>139</td>
<td>138</td>
</tr>
</tbody>
</table>

CHF—Swiss franc. DC—Standard & Poor's downside-case scenario. Sources: Canton's annual accounts adjusted by Standard & Poor's, Standard & Poor's projections.

### Table 5
**Canton of Geneva Financial Statistics—Upside-Case Scenario**

<table>
<thead>
<tr>
<th>Mil. CHF</th>
<th>2014 (UC)</th>
<th>2013 (UC)</th>
<th>2012 (UC)</th>
<th>2011</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>Adj. operating revenues</td>
<td>8,131</td>
<td>8,036</td>
<td>7,994</td>
<td>7,690</td>
<td>7,193</td>
</tr>
<tr>
<td>-Adj. operating expenditures</td>
<td>7,658</td>
<td>7,523</td>
<td>7,390</td>
<td>7,361</td>
<td>6,985</td>
</tr>
<tr>
<td>=Operating balance</td>
<td>473</td>
<td>513</td>
<td>604</td>
<td>329</td>
<td>208</td>
</tr>
<tr>
<td>Operating balance (% of adj. operating revenues)</td>
<td>6</td>
<td>6</td>
<td>8</td>
<td>4</td>
<td>3</td>
</tr>
<tr>
<td>+Capital revenues</td>
<td>110</td>
<td>120</td>
<td>215</td>
<td>177</td>
<td>146</td>
</tr>
<tr>
<td>-Capital expenditures (capex)</td>
<td>600</td>
<td>1,150</td>
<td>720</td>
<td>759</td>
<td>797</td>
</tr>
<tr>
<td>=balance after capital accounts</td>
<td>(17)</td>
<td>(517)</td>
<td>99</td>
<td>(253)</td>
<td>(443)</td>
</tr>
<tr>
<td>Balance after capital accounts (% of adj. total revenues)</td>
<td>(0.2)</td>
<td>(6.3)</td>
<td>1.2</td>
<td>(3.2)</td>
<td>(6.0)</td>
</tr>
<tr>
<td>-debt repaid</td>
<td>726</td>
<td>980</td>
<td>1,011</td>
<td>1,037</td>
<td>1,388</td>
</tr>
<tr>
<td>+new borrowings</td>
<td>743</td>
<td>1,497</td>
<td>1,515</td>
<td>1,778</td>
<td>1,132</td>
</tr>
<tr>
<td>Balance after borrowings</td>
<td>0</td>
<td>0</td>
<td>603</td>
<td>487</td>
<td>(699)</td>
</tr>
<tr>
<td>Direct debt (outstanding at year-end)</td>
<td>12,334</td>
<td>12,317</td>
<td>11,800</td>
<td>11,204</td>
<td>10,463</td>
</tr>
<tr>
<td>Direct debt (% of adjusted operating revenues)</td>
<td>152</td>
<td>153</td>
<td>148</td>
<td>146</td>
<td>145</td>
</tr>
<tr>
<td>Tax-supported debt (% of adjusted operating revenues)</td>
<td>145</td>
<td>146</td>
<td>140</td>
<td>139</td>
<td>138</td>
</tr>
</tbody>
</table>

CHF—Swiss franc. UC—Standard & Poor's upside-case scenario. Sources: Canton's annual accounts adjusted by Standard & Poor's, Standard & Poor's projections.

### Economic Statistics Tables

#### Table 6
**Canton of Geneva Economics Statistics**

<table>
<thead>
<tr>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Population</td>
<td>447,584</td>
<td>453,439</td>
<td>457,628</td>
<td>463,919</td>
</tr>
<tr>
<td>Unemployment rate (%)</td>
<td>6.3</td>
<td>5.7</td>
<td>6.8</td>
<td>7.0</td>
</tr>
<tr>
<td>Nominal GDP per resident (Swiss Francs)</td>
<td>95,141</td>
<td>98,617</td>
<td>95,073</td>
<td>96,951*</td>
</tr>
</tbody>
</table>

Related Criteria And Research

- Methodology For Rating International Local And Regional Governments, Sept. 20, 2010
- Institutional Framework Assessments For International Local And Regional Governments, Jan. 14, 2013
- Methodology And Assumptions For Analyzing The Liquidity Of Non-U.S. Local And Regional Governments and Related Entities And For Rating Their Commercial Paper Programs, Oct. 15 2009

### Ratings Detail (As Of January 15, 2013)

<table>
<thead>
<tr>
<th>Geneva (Republic and Canton of)</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Issuer Credit Rating</td>
<td>AA-/Stable/--</td>
</tr>
<tr>
<td>Senior Unsecured</td>
<td>AA-</td>
</tr>
</tbody>
</table>

**Issuer Credit Ratings History**

- 20-Sep-2010: AA-/Stable/--
- 11-Dec-2008: A+/Stable/--
- 02-Apr-2004: A/Stable/--

**Default History**

None

**Population**

468,741 (source: OCTSAT, as of Oct. 31, 2012)

**Per Capita GDP**

98,066 Swiss Francs (CHF) (c. 105,000 USD) (Source: OCSTAT, 2011 figure)

**Current Government**

A right-wing coalition has the majority in both the parliament and the executive body.

**Election Schedule**

- Last: October 2009
- Next: October 2013

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.*

**Additional Contact:**

International Public Finance Ratings Europe; PublicFinanceEurope@standardandpoors.com
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