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Supplementary Analysis:

Geneva (Republic and Canton of)

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Supplementary Analysis:

Geneva (Republic and Canton of)

This report supplements Standard & Poor's Ratings Services' research update "Swiss Canton of Geneva Rating Affirmed At 'AA-'; Outlook Stable," published Nov. 13, 2015. To provide the most current information, we may cite more recent data than that stated in the previous publication. These differences have been determined not to be sufficiently significant to affect the rating and our main conclusions.

Rationale

Issuer Credit Rating
AA-/Stable/--

The rating on the Republic and Canton of Geneva reflects our view of the extremely predictable and supportive institutional framework for Swiss cantons, as well as the Canton of Geneva's very strong economy in an international context. Moreover, the rating factors in the canton's strong financial management.

The rating also incorporates the Canton of Geneva's average budgetary flexibility and budgetary performance, as well as its moderate contingent liabilities. Additionally, the rating reflects the canton's adequate liquidity, notably thanks to strong access to external funding.

However, the rating remains constrained by the Canton of Geneva's very high debt burden incorporating unfunded pension liabilities. The long-term rating is at the same level as the canton's stand-alone credit profile, which we assess at 'aa-'.

In our view, the Canton of Geneva continues to benefit from a wealthy and diversified economy, with real GDP per capita at Swiss franc (CHF) 113,472 (more than $112,000) in 2014, which is very high in an international context. However, compared with previous years, the canton's GDP growth has recently slowed, and we expect this trend will continue until 2016 in line with Switzerland's (see "Sovereign Risk Indicators," published Oct. 12, 2015. A free-of-charge interactive version is available at http://www.spratings.com/sri). We believe this trend in GDP growth will have a significant impact on the canton's finances, since the bulk of its operating revenues is made of locally collected taxes (close to 80% as of 2014). In that regard, the increase in operating margins in 2014 to 7.2% of operating revenues from 4.4% in 2013 is mainly linked to higher-than expected tax revenues (up 4% from 2013), especially on personal income tax, as well as a very tight grip on operating expenditures (up 0.3% from 2013).

Like all Swiss cantons, the Canton of Geneva has extensive legal flexibility in setting personal income and corporate profit tax rates, but we regard its revenue raising flexibility as low in practice, because tax hikes are subject to popular referendum, tax rates are high in a Swiss context, and, given the nature of the corporations it hosts, the Canton of Geneva is particularly sensitive to global tax competition. This, combined with the largely rigid nature of operating expenditures (mostly consisting of personnel, social aid, and allowances and transfers for health care and public transport) and limited capital expenditures in an international context (8.3% of total expenditures on average over 2015-2017 under our base-case scenario), supports our view of limited budgetary flexibility.

In the context of the upcoming abolition of the cantonal lump-sum taxation system for holding companies, the canton has stated its willingness to cut the corporate tax rate to 13% from about 24% currently for normal status corporations (and 11% for holding companies) to retain international corporations in its territory. We understand that this could lead to a reduction in revenues of up to CHF500 million per year. However, at this stage, we understand that the Canton of Geneva is still refining its policy response for a possible implementation from 2019, since there is no settled view on its potential impact on the Canton of Geneva, including likely compensation from the Swiss Confederation. Consequently, we do not include it in our base-case scenario at this stage. Given our view of an extremely predictable and supportive institutional framework for Swiss cantons, we expect this reform would be implemented progressively and negotiated with cantons, notably with regard to financial compensation from the Swiss Confederation for cantons' tax cuts.

We still assess the Canton of Geneva's financial management as strong. Given the canton's current political situation with no clear political majority at the cantonal parliament, the cantonal executive needs to build a consensus around its strategy, especially regarding the corporate tax reform. We positively view the cantonal executive's renewed commitment to controlling debt and implementing cost-cutting measures starting in 2015. Moreover, the canton continues to display, in our view, prudent debt and liquidity management.

Under our base-case scenario, we expect that the Canton of Geneva will record average budgetary performance in 2015-2017. We expect that the operating balance will progressively contract to 3% of operating revenues in 2017 (in line with our previous base case). We expect that reduced tax revenues (in the context of lower GDP growth prospects) and increasing social aid and health expenses will be partly mitigated by lower-than-expected equalization transfer payments and cost-control and cutting measures, including on personnel expenditures and transfers. In line with our previous base case, we anticipate capital expenditures will average CHF696 million over 2015-2017, compared with CHF772 million in 2014 (including a one-time cash injection in the public pension fund of CHF146 million). This, combined with a decreasing operating margin and a one-time asset sale of CHF100 million expected in 2015, would lead to deficits after capital accounts of close to 4% of total revenues in 2015-2017 (1% in 2014).

Consequently, and also given lower working capital needs on the back of sizable tax prepayments by individuals and corporates, we anticipate that the canton's tax-supported debt will slightly decrease in 2015 to 152% of consolidated operating revenues from 154% in 2014 and then increase to 160% at year-end 2017. We include in our calculation of tax-supported debt the Canton of Geneva's direct debt and as well as the debt for non-self-supporting government-related entities (such as transportation company Transports Publics Genevois and the public hospital Hôpitaux Universitaires de Genève). Meanwhile, interest charges should remain limited, in our view, at close to 3% of operating revenues through year-end 2017. The canton also records high unfunded pension liabilities, representing 91% of the canton's operating revenue at year-end 2014, and we expect these liabilities will remain sizable in the coming years, which erodes our assessment of its debt burden.

In our view, the canton has moderate risks associated with contingent liabilities, mainly through the cantonal bank Banque Cantonale de Genève (BCGE; A+/Stable/A-1), of which it remains the majority shareholder.

Liquidity

We assess the Canton of Geneva's liquidity as adequate, according to our criteria. This reflects our expectation that the canton's average available amounts on its bank lines will cover more than 50% of its debt service over the next 12 months. The canton currently benefits from extensive short-term facilities, comprising CHF1.3 billion of contracted bank lines and CHF2.8 billion of liquidity lines, which are not formally contracted but generally available, with various public sector entities and Swiss and international banks.

In our view, the canton continues to exhibit strong access to external funding via the financial markets, as reflected by frequent public bond issuances in recent years.

Outlook

The stable outlook reflects our base-case expectation that the Canton of Geneva will maintain average budgetary performance and limit debt accumulation over 2015-2017.

In our upside scenario, we could consider a positive rating action if the Canton of Geneva improved its budgetary performance so that it could structurally enhance its liquidity position.

In our downside scenario, we could consider lowering the rating if the canton recorded structurally negative operating margins and increasing deficits after capital accounts, prompting increased debt accumulation, which would lead us to revise downward our assessment of the canton's financial management.

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

Extremely Predictable And Supportive Institutional Framework

In our view, Swiss cantons benefit from a very stable political and institutional system, which we assess as extremely 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 our 1 to 6 scale.

The main characteristics of the institutional framework for Swiss cantons are detailed in "Public Finance System Overview: Swiss Cantons," published May 4, 2015. In this analysis, we focus on the cantonal equalization system and the potential impact of a reform of lump-sum cantonal taxation currently discussed between cantons and the Swiss federal government.

Geneva is a net contributor to the Swiss cantonal equalization system

Switzerland supports financial equalization among the cantons under its constitution, and the current cantonal equalization system (CES), last reformed in 2008, is largely based on three funds:

- A revenue-related equalization fund that aims to reduce financial and tax disparities among cantons. Switzerland finances this fund, providing CHF2.3 billion in 2015 and with CHF2.3 billion to be provided in 2016. Cantons with high revenue potential also contribute, having given CHF1.6 billion in 2015 and set to contribute CHF1.6 billion in 2016.
- 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 CHF726 million to this fund in 2015, and we expect it will contribute CHF718 million in 2016.
- A temporary "neutralization" fund that is set to temporarily compensate for the effect of implementing CES. In 2015,

Switzerland contributed CHF239 million and the cantons, CHF120 million. In 2016, Switzerland will likely contribute CHF227 million and the cantons CHF114 million.

In 2015, Geneva remained the third-largest contributor to CES, with CHF256 million, after the Zurich and Zug cantons. In 2016, for the second year in a row, Geneva's contributions will decrease to CHF246 million.

Geneva's finances could be significantly affected by a reform in corporate taxation, currently under discussion between Switzerland and the cantons

The Swiss Confederation is currently pursuing its reform aiming to abolish cantonal lump-sum taxes on businesses. This reform--still underway--is being negotiated between the cantons and the Swiss federal government, in the context of the latter's negotiations on corporate tax regimes with the European Union. The reform could be adopted by the federal parliament in late 2015 or early 2016.

We understand the canton seeks to retain within its territory holding and auxiliary companies that would be particularly affected by the upcoming abolition of cantonal lump-sum taxation under the reform. These are key employers and tax contributors for Geneva. According to the federal administration, companies benefiting from the lump-sum taxation represented close to 32% of total corporate tax revenues in Geneva on average over 2008-2010, whereas the national average stood at 21% (this is the fifth-highest share among Swiss cantons after Basel-City, Zug, Schaffhausen, and Basel-Country). We further understand that the canton's goal is to cut the corporate tax rate to approximately 13% from about 24% currently for normal-status corporations (and 11% for holding and auxiliary companies). However, at this stage, we note that the Canton of Geneva is still refining its policy response for a possible implementation from 2019. If the general cut is implemented, it could affect Geneva's finances, as it could result in a CHF500 million drop in tax revenues for Geneva. Local firms have proposed, in exchange for this general tax cut, to fund CHF55 million per year for kindergartens and professional training. They also proposed to fund about CHF30 million for construction of a professional training center. According to the federal government in its June 2015 message, other options could be retained, such as exemptions for research and development expenses or the so-called "patent box."

To our knowledge, the reform might be implemented from 2019, but we exclude it from our projections at this stage because we do not have a clear view on its potential impact on Geneva, including compensation from the Swiss federal government and the potential reform of the current CES. However, in its September 2014 report, the federal government indicated that the cantons could be compensated by raising their share of revenues derived from personal income tax or corporate tax to 20.5% from 17%. According to the federal government, the cantons should consequently benefit from compensation of CHF1 billion. Within this plan, the Canton of Geneva should receive CHF129 million. Given our view of the extremely predictable and supportive institutional framework for Swiss cantons, we would also expect the reform to be implemented only progressively. We will, however, monitor this reform and potential measures that the canton may take as a part of it.

A Very Strong Economy

A dense territory with a dynamic demographic profile

Geneva is a small (282 square kilometers), densely populated (1,735 residents per square kilometer) Swiss canton with 489,959 inhabitants at end-September 2015, up a high 1.5% from December 2014 figures. Geneva's population dynamics outpace the national average, having increased by an average 1.1% in 2001-2014, compared with 1% 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 41% of the its population at end-December 2014, almost twice the national level. Most foreigners are of working age and active.

Based on recent trends, the cantonal statistics office estimates that the cantonal population could gain about 100,000 inhabitants by 2040. This would translate into increasing education, health and social care, and public infrastructure costs, while also fueling tax bases. Moreover, it would create further pressure on housing construction, in a context of already scarce land availability. We note that while Geneva's population is currently fairly young, demographic ageing will result in 20% of the population being over age 65 in 2040 compared with 16% in 2014, and a doubling of inhabitants over age 80 to 40,000 residents in 2040, compared with 2011 data. That means the canton will have to build new homes and home-care systems.

A wealthy and resilient economy

Based on cantonal estimates from Office cantonal de la statistique (OCSTAT), Geneva reported very high GDP per capita of about CHF113,472 (more than $112,000) in 2014. Geneva's GDP per capita has exceeded the Swiss average by more than 40% since 2001, and the canton has the highest salaries in Switzerland, according to data from the Swiss statistics office (OFS). The high salaries are positive because the canton derived more than one-half of its operating revenues from personal income tax in 2014 (51%). High-value-added operations are concentrated in Geneva, demonstrated by its gross value added (GVA) per worker, which was about 12% higher than 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--living in France but working in Geneva--has doubled since 2002 and now represents approximately 20% of the canton's jobs.

Geneva experienced a faster economic rebound than that of Switzerland following the 2007-2008 world economic recession. According to the latest data and projections from the economic think tank "Groupe de Perspectives Economiques," Geneva's economic growth has outperformed the national average by close to 30 basis points; OCSTAT estimates 2014 growth for Geneva at 2.2% versus 1.9% nationally. For 2015, due the decision of the Swiss National Bank (SNB, the central bank) to let the Swiss franc float, coupled with deteriorated global economic conditions, we expect economic growth in Geneva will slow in line with that of Switzerland. Under our base-case scenario, in line with our projections on Switzerland, we expect this trend to continue until 2016 in line with Switzerland's (see "Sovereign Risk Indicators"). Moreover, we expect that the positive difference in terms of growth compared with the Swiss national average will gradually disappear. By 2016, Geneva's economic growth will be equal to that of Switzerland, which we project at 0.8% in 2015, 1.2% in 2016, and 2% in 2017.

A diversified economy, although banking activities and holding companies are increasingly under international pressure

The canton's economy has increasingly diversified since the beginning of the 1990s.

Services made up 84.5% of value-added in 2014 (source: OCSTAT), with agriculture at 0.3% and industry at 15.4%. Industry focuses on high-value added activities, including luxury watches (4.7%), construction (3.5%), chemical and pharmaceuticals (2.4%), and precision engineering (1.5%). Overall, these sectors are largely geared toward international markets, and they make up the bulk of Geneva's exports, with a concentration on high-growth countries, especially in Asia.

The public and semi-public sector accounted for 22.1% of GDP at year-end 2014, against about 20.2% for wholesale and retail and 13.9% for business services. The public and semi-public sector employs about one-fourth of the canton's workforce, which provides significant stability to the employment base. This stems from the presence of a wide variety of international organizations that employs close to 8.6% of Geneva's workforce. Geneva is also a worldwide center for conference activities and business tourism.

Geneva's financial sector represented 14.7% of local GDP in 2014, a sharp reduction from 24.6% in 2000. Still, 10 out of the canton's 30 biggest employers remain financial institutions. Compared with other financial centers such as Zurich, Geneva was relatively sheltered from recent turmoil in the capital markets. Geneva's financial institutions primarily focus on asset management and commodities trading. Although the crisis has also damaged these sectors, they have shown resilience. However, Geneva's strong specialization as the leader in commodities trading--representing 3.5% of Geneva's GDP and 22.5% of corporate profit tax revenues--could negatively affect the canton if the sector continued to face difficulties. The current efforts to combat tax evasion and fraud, especially from the EU and the Organisation for Economic Cooperation and Development, could negatively affect the Swiss banking sector, including Geneva. We cannot assess their potential financial influence on the canton's finances at this time.

In light of the upcoming abolition of tax advantages granted to holding companies in Switzerland, it is worth noting that these companies account for about 20,000 direct jobs and 50,000 indirect jobs in Geneva and they pay about CHF1 billion in cantonal and municipal taxes (or close to 32% of corporate taxes between 2008 and 2010). If these tax advantages were abolished, the canton estimates that, in the absence of a reduction in cantonal and municipal taxes, several companies would leave Geneva, resulting in a significant loss of jobs and tax revenues. As a consequence, Geneva is currently considering a general reduction in its corporate profit tax rate to 13%.

Strong Financial Management

Under our methodology for rating international local and regional governments, we view the canton's financial management as strong, owing to its commitment to controlling debt and to implement measures to increase operating revenues, as well as its prudent debt and liquidity management.

Political and managerial leadership is consensus-based but with a clear strategy to stabilize debt

The canton's citizens choose Geneva's parliament and government for five-year terms in simultaneous elections. Consensus-based governance is favored by the semi-direct democratic system, using frequent referendums.

Since the elections in October-November 2013, the cantonal parliament has changing majorities given the three-way split of almost equal weight: a center-left/left group, including the socialist and green parties, and the left-wing Ensemble à gauche, with 34 seats; a center-right/right group comprising the PLR and PDC parties, with 35 seats; and a populist group made up of the UDC and MCG parties, with 31 seats. In the meantime, the government retains a right-wing (PLR, PDC) majority with four seats out of seven. In this context, the executive must build a consensus on projects during its current tenure. Consequently, the implementation of the canton's strategy depends on the executive's ability to find a sizable majority at the cantonal parliament, which can lead to lengthy negotiations, such as those for the 2015 budget. Moreover, the cantonal parliament can sometimes go further than the executive and pass laws that were opposed by the government. In November 2015, a broad right-wing majority passed, against the government, a law stipulating a stabilization of operating and staff expenditures as long as direct debt exceeds 100% of the canton's annual revenues (about CHF9 billion). As debt is currently approximately CHF12.8 billion, this will have the effect of freezing operating and staff costs for the coming years (unless two-thirds of parliament members authorize an increase of up to 1% for operating charges and up to 0.5% for staff expenses). This highlights both the strong willingness of the canton's parliament to pursue strong financial discipline and the need for the executive to build a consensus at the parliament. The left-wing minority has announced a popular referendum on this project, hoping to derail it.

In June 2014, the cantonal executive released its strategy for 2014-2018. Among others, the canton renewed its commitment to contain debt accumulation and to increase operating revenues. These goals are deemed necessary for the canton in order to regain flexibility. In this context, the canton aims to better manage its assets and to prioritize its investments.

Geneva's law on financial management stipulates a balanced operating budget: if there is a deficit, it must not exceed the canton's specific reserve, and the canton's four-year financial projections must forecast a balanced budget. Assumptions for the budget are generally prudent, especially with regard to resources. In addition, if the canton posts two consecutive years of deficits under International Public Sector Accounting Standards (IPSAS) standards, the canton's parliament must submit measures to popular vote through referendums--with clear set options--increasing tax rates or reducing expenditures in order to achieve a balanced budget. However, the canton's parliament may avoid this process if financial projections show that, after three years of operating deficits, the canton is most likely to return to a positive operating balance the following year.

Moreover, since Jan. 1, 2014, a new mechanism for capital expenditures has come into force in order to limit new debt. It implies a qualified vote at the parliament for new investment projects (excluding renewals), with 51 members of parliament (MPs) out of 100 as long as cantonal debt exceeds CHF13.3 billion, and 67 members of parliament if it is over CHF14.8 billion. These debt ceilings are not indexed and are in practice long-term brake mechanisms on Geneva's debt, targeting long-term debt decreasing to one year of revenues (under IPSAS).

Firm cost control

Cost control is the main impetus of budget decisions, even though operating expenditures and operating revenues are 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 about 7% of tax receivables while 3% are usually not collected.

Besides, within the revised financial projections, the canton has also released a set of measures aimed at improving the financial results either by reducing operating expenditures (a general 5% decrease in staff costs has been proposed to be negotiated with trade unions), curbing operating expenditure growth, notably on staff expenditures or increasing operating revenues by CHF385 million over 2015-2019.

Efficient long-term capital and financial planning

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 key 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 (excluding amortization and provisions, for instance).

Geneva makes four-year projections, which are regularly updated. The latest projections for 2015-2018 were published in November 2014. These projections include clear-cut and conservative expectations that comply with publicly released fiscal targets. The revised projections forecast a gradual improvement of the canton's operating result, thanks to an accentuated grip over operating expenditures that would grow at 1.6% per year (this includes a set of measures defined by the executive to curb operating expenditures growth) and good operating revenue growth, especially tax revenue growth, thanks to positive economic growth. We note, however, that these projections do not incorporate the latest forecasts from the Groupe de Perspectives Economiques, which has recently lowered its growth projections for Geneva. The four-year projections also integrate an average investment program of CHF633 million per year, leading to significant financing needs.

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 2015:

- Limiting the average interest rate to 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 eight years;

The canton also aims to smooth its annual debt amortization profile 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, notably its public transportation company, Transports Publics Genevois (TPG), its social aid entity Hospice Général, and the public hospital, Hôpital Universitaire de Genève (HUG). This system helps to limit debt recourse and related interest charges.

As of end 2015, the canton has contracted short-term facilities of CHF1.3 billion, and benefits from CHF2.8 billion of non-contracted liquidity lines with several public-sector entities and Swiss and international banks. These lines cover its annual cash needs.

Good management of its related entities

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 maintain 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.

Average Budgetary Flexibility

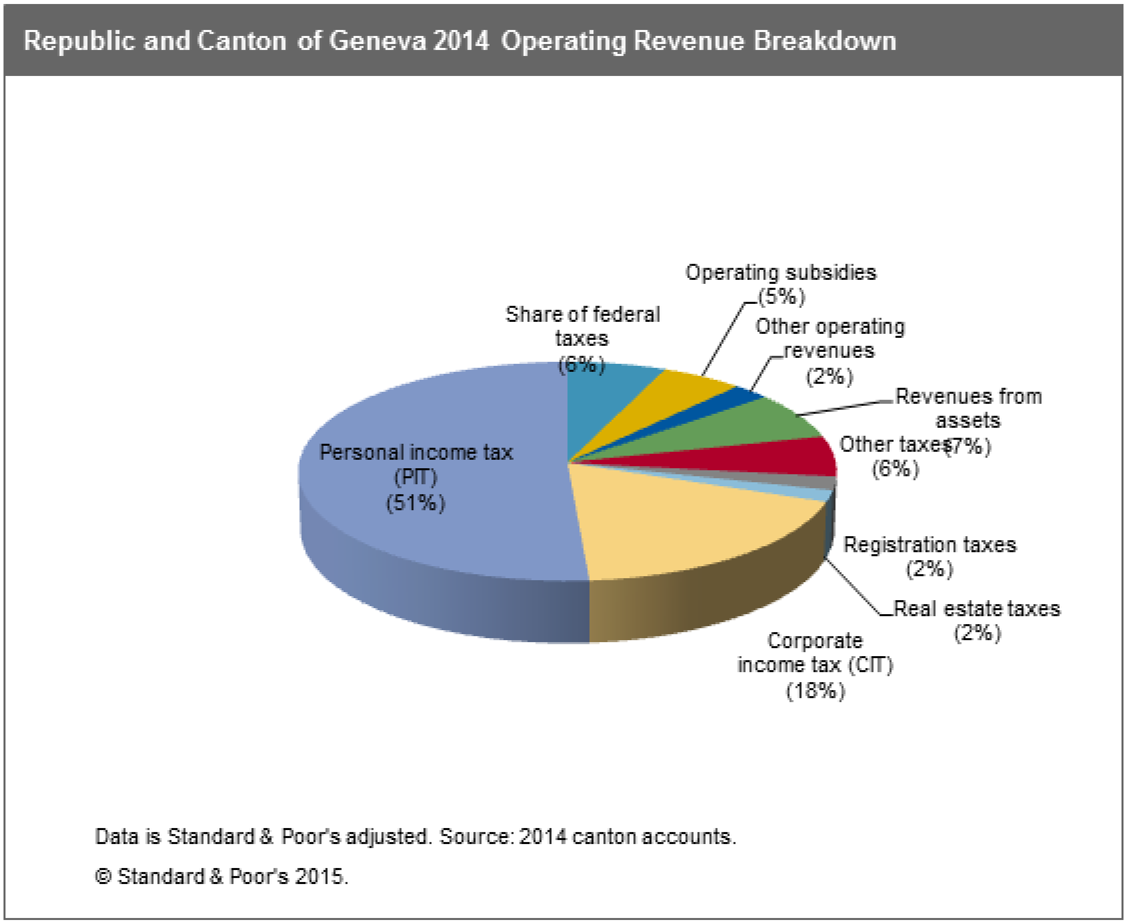
Low flexibility in practice on tax revenues

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 referendums held in 2005 and 2007; and
- There is still tax competition between cantons, limiting in practice cantons' increases of their own tax rates. Moreover, under the upcoming reform of lump-sum taxation, many Swiss cantons, including Geneva, are contemplating a general decrease in their corporate tax rate. Geneva has indicated it is contemplating a unified corporate tax rate of about 13%, versus the current 24% for non-holding companies and 11% for holding and auxiliary companies. The effective rate of 24% for non-holding companies is already comparatively high among Swiss cantons, against 21% in Zurich and 11.5% in Zug.

Geneva's operating revenues are largely composed of locally-collected taxes (see chart 1). Some are sensitive to economic cycles, notably the corporate tax, but taxes are mostly levied on individuals, which limits their volatility. We note that there is, however, some concentration in personal income tax, which includes taxes on affluent taxpayers, as well as on corporate tax. The 20 biggest taxpayers accounted for close to 39% of corporate profit tax in 2013.

Chart 1



Fairly rigid cost structure

The canton's expenditure flexibility remains limited by the high proportion of operating costs in its budget. They accounted for 91% of total spending in 2014. In addition, 95% of operating charges are fixed items, including personnel and financial charges, and rigid social and health care subsidies, as well as subsidies to higher education and public transportation, tax compensations to French local governments, and payments to other Swiss cantons under the equalization scheme.

Cost control remains a chief priority, as demonstrated since 2011 by tight controls over general expenditures and personnel. In 2011-2014, operating expenditures grew by a limited 1.4% annually despite increasing social charges and additional payments under the cantonal equalization system, which are largely out of the canton's control.

Potential adjustments to capital expenditures, if needed

We estimate that Geneva has flexibility in its investment program, if necessary. The canton stated in its legislative program that it will prioritize its capital expenditure program. In 2015-2018, under Geneva's multiyear plan, we note that capital expenditures (net of capital revenues) would average CHF633 million per year, down from CHF733 million annually over 2014-2017 in the previous multiyear plan published in November 2013. 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 payment peaks.

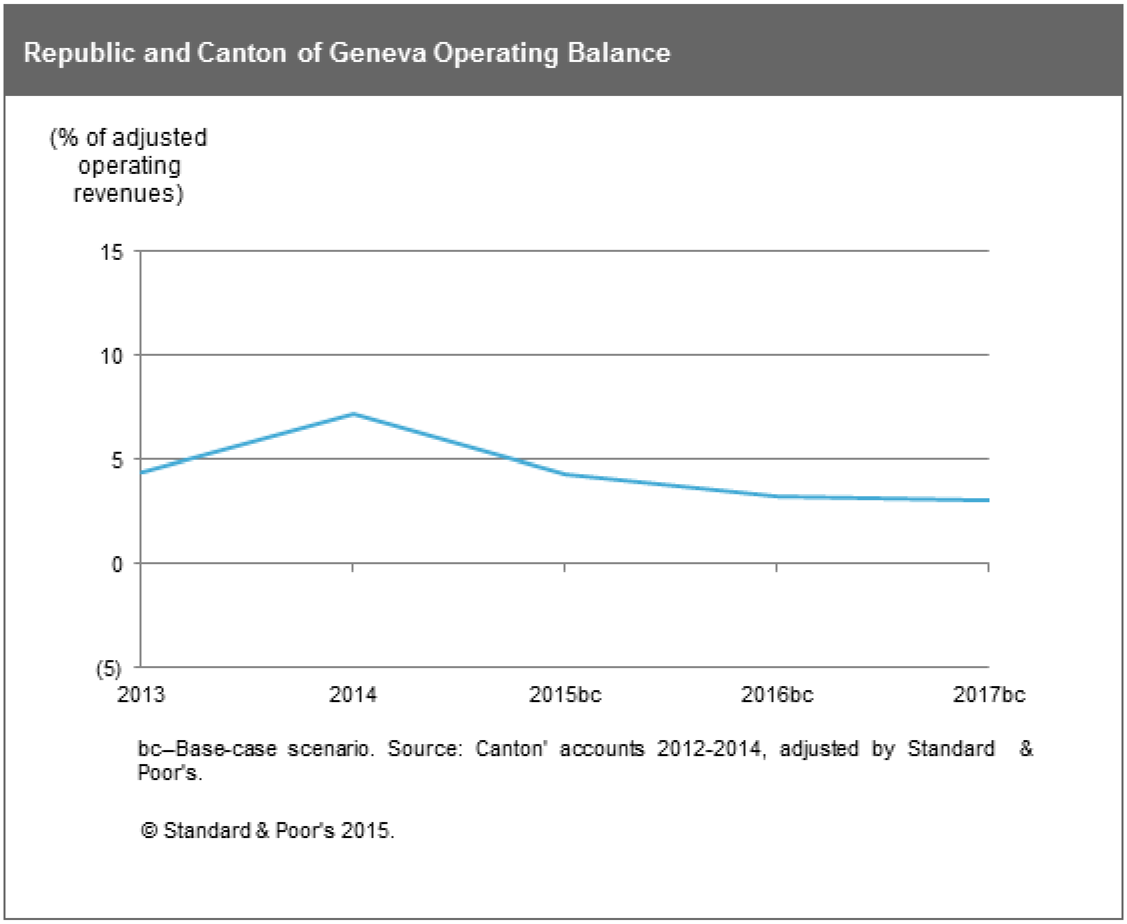
Average Budgetary Performance

In 2012-2014, the canton posted a fair 6.3% operating margin (before amortization) on average, and 7.2% in 2014 (up from 4.4% in 2013). These 2014 results are significantly higher than what we forecasted in our previous base-case of December 2014 (3.2%) due to operating revenues increasing by 3.4% in 2014 owing to exceptional revenues linked to the conclusion of a fiscal deal with a taxpayer that led to an increase of the tax revenues by 4%, mostly on personal income tax and inheritance tax. Moreover, despite increasing costs related to social aid, operating expenditures barely grew at 0.3%, notably staff costs that remained stable in 2014.

Following the CHF549 million cash injection into public pension funds in December 2013, Geneva's capital expenditures peaked at CHF1.2 billion, leading to a temporary high deficit after capital accounts of 10% of total revenues in 2013, from 1% in 2012. Excluding the impact of recapitalization of the pension funds, the deficit after capital accounts would have stood at 3% of total revenues. In 2014, capital expenditures stood at CHF772 million (including another onetime recapitalization of the public pension fund amounting to CHF146 million), with a moderate deficit after capital accounts of 1.4% of total expenditures. As in 2013, Geneva's debt increased beyond its investment funding requirements in 2014, owing to high working capital needs, reflecting quicker payments to federal government and operators, and refunds to some taxpayers for tax advances. The canton's direct debt therefore increased by CHF0.6 billion in 2014 to CHF13.4 billion or a high 166% of operating revenues.

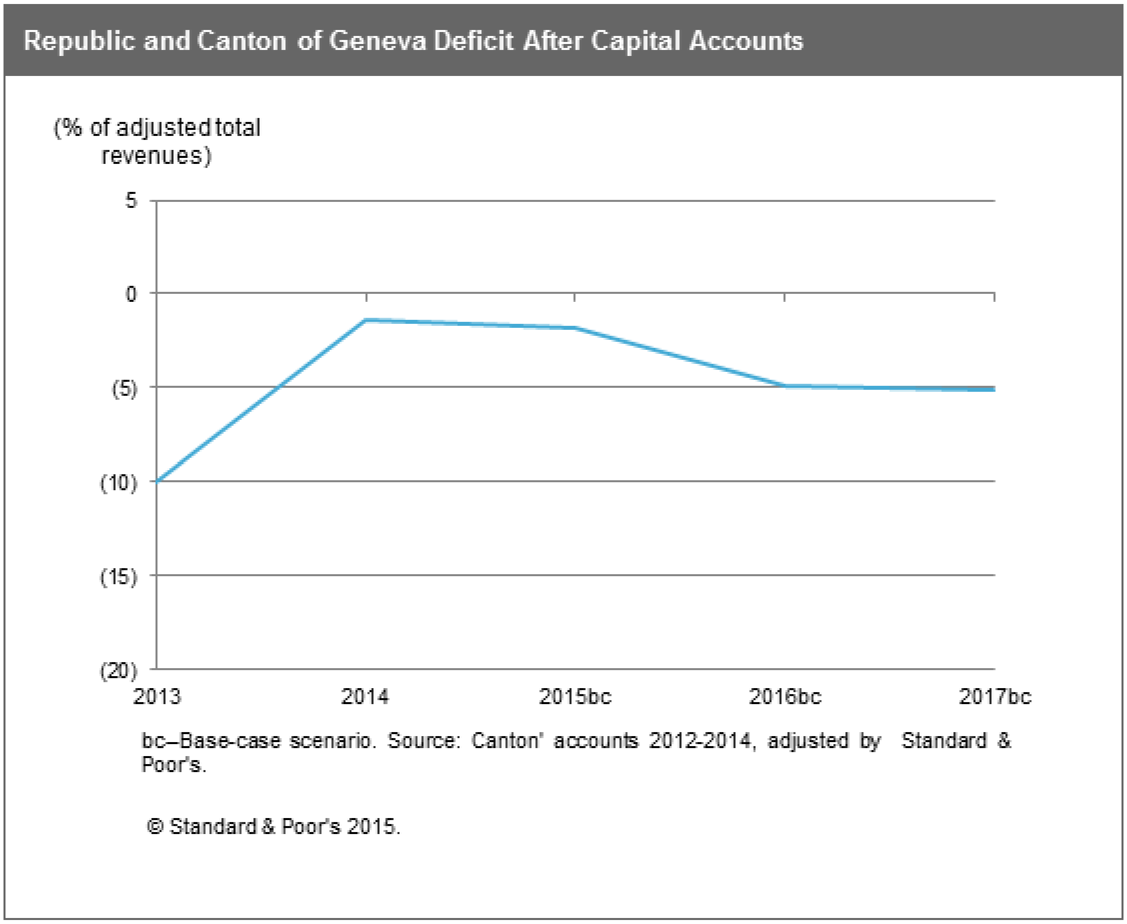
Under our base-case scenario, we assume that the canton will record average budgetary performance in 2015-2017. We expect that the operating balance will progressively contract to 3.1% of operating revenues in 2017, a slight reduction from 6.3% on average over 2012-2014 (see chart 2). We estimate that operating revenues will remain stable on average, in 2015-2017, compared with 2.5% over 2012-2014, notably reflecting less dynamic tax revenues (in the context of lower GDP growth prospects) and the absence of dividends from the Swiss National Bank in 2016 (while the Canton received CHF 77 million in 2015). We also forecast that operating expenditures will increase by 1.4% on average per year, despite increasing social aid and health expenses because we expect the canton to implement measures to limit operating expenditures growth, notably staff costs, starting in 2015. Moreover, in line with the federal government's recent announcements, the canton will contribute about CHF 14 million less in 2015 and about CHF 10 million less in 2016 to inter-cantonal equalization transfers.

Chart 2



We project that capital expenditures will decline to CHF696 million over 2015-2017 because the canton has adjusted its capital expenditure (capex) plan, and expects a lower realization rate than in the past, at 85%. In the context of a slight decrease of the operating margin, this adjustment in capital expenditures should enable Geneva to post an average deficit after capital accounts of 3.9% of total revenues over 2015-2017 (see chart 3). As a result of these deficits after capital accounts and, to a lesser extent, working capital needs, we project that tax-supported debt will increase to about 160% of operating revenue at year-end 2017 (from 153% in 2014).

Chart 3

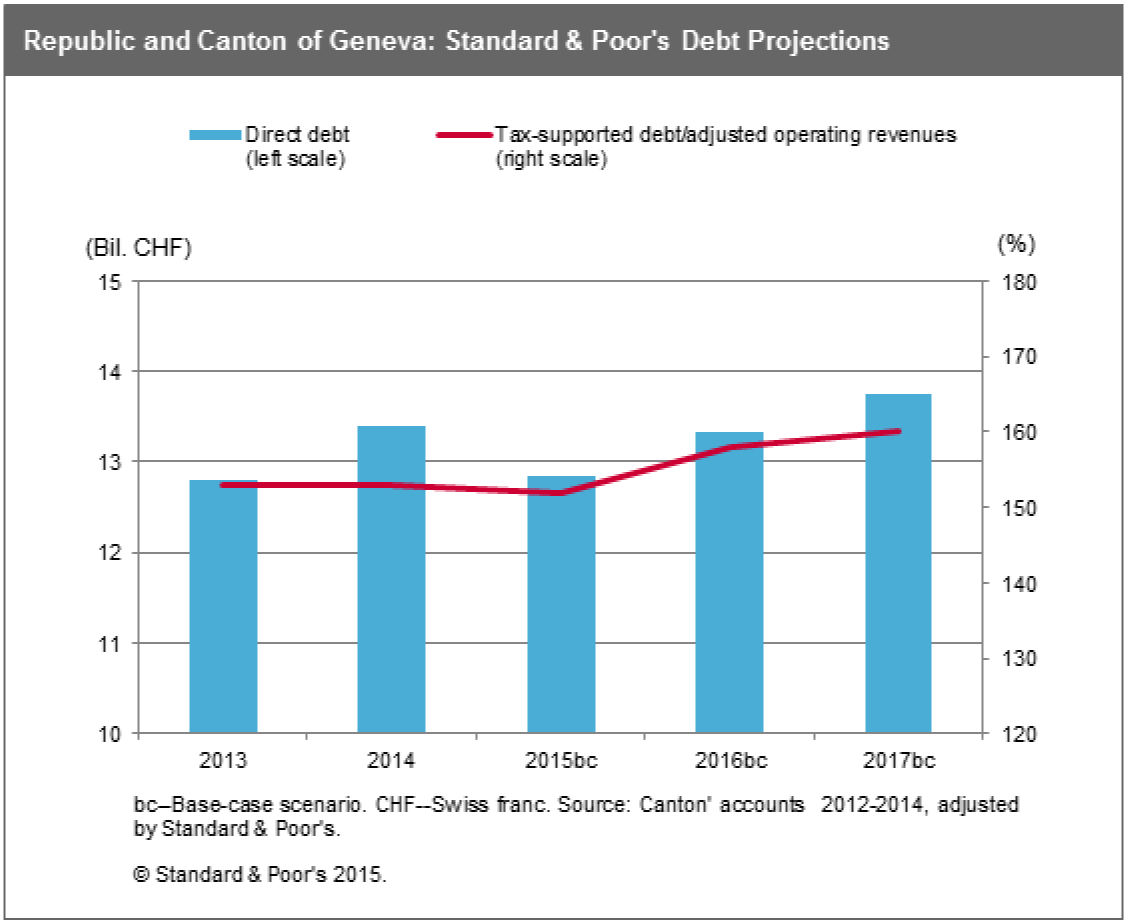


Very High Debt Burden Including Sizable Unfunded Pension Liabilities

High tax-supported debt

We view Geneva's tax-supported debt as high, at 153% of consolidated revenue at the end of 2014 (stable in comparison with 2013) (see chart 4). 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. Given lower working capital needs on the back of sizable tax prepayments by individuals and corporates, we anticipate that the canton's tax-supported debt will slightly decrease in 2015 to 152% of consolidated operating revenues from 154% in 2014 and then increase to 160% at year-end 2017.

Chart 4



Debt service represented a high 13% of operating revenue in 2014 (down from 16.5% in 2013) and we expect it to remain stable by 2017, reflecting low interest rates and low debt repayment instalments. Interest charges represented 2.8% of operating revenues in 2014 and will remain stable until 2017 under our base-case scenario. At year-end 2014, the amount of short-term debt represented close to 21% of the total amount of Geneva's direct debt (17% at year-end 2013), which is below the 25% threshold set up by the Executive.

Large unfunded pension liabilities

The reform of Geneva's public pension funds came into effect on January 1, 2014. In order to meet new national minimum mandatory coverage ratios and keep their defined benefits and mixed financing, 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-médicaux du canton de Genève (CEH) for medical personnel--have merged to create a new public pension fund, Caisse de prévoyance de l'Etat de Genève (CPEG), aiming to generate economies of scale, raise the combined fund's coverage ratio, and better balance the demographic profile. The reform also included structural measures like hikes in the retirement age and in contribution rates, as well as a sizable CHF549 million cash injection by the canton into CIA in December 2013. Moreover, the canton has injected a further CHF146 million into another public pension fund in 2014.

In that context, as of Dec. 31, 2014, Geneva's new public pension fund recorded unfunded pension liabilities of CHF7.3 billion at a 3% discount rate, or over 91% of its operating revenues, which is very high by international standards and weighs negatively in our assessment of Geneva's debt burden.

Despite this comprehensive reform, we estimate that pension liabilities will remain very high for Geneva, and that they may entail further capital injections in the future, if financial markets plummet and lead to falling coverage ratios for public pension funds. Capital injections and/or adjustments to the pension plans might be needed also to allow public pension funds to comply with national regulation requiring minimum mandatory coverage ratios, meaning 100% coverage for retirees and 80% coverage for workers contributing to the plan--to be achieved within a 40-year period by 2052--with a mandatory 60% in 2020 and 75% in 2035. As of Dec. 31, 2014, the coverage ratio of the new public pension fund stood at 61.6%.

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 (CHF0.82 billion at the end of 2014) were partly granted to social housing foundations (CHF0.3 billion). Debt guarantees granted to the canton's non self-supporting entities like TPG are included in our calculation of its tax supported-debt (See section above "High debt burden and sizable unfunded pension fund liabilities").

The canton's main contingent liability relates to BCGE, a cantonal bank in which it controls 49.8% of voting rights. Until the end of 2009, Geneva's largest contingent liabilities were related to past problems, including bad loans and lengthy real-estate problems. BCGE had to be bailed out by the canton in 1999 under a cash injection and in 2000, through an ad hoc defeasance structure set up by the canton, 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 CHF1.98 billion at the end of 2014 and will decrease in the short term. This is because the canton has decided to end this guarantee scheme by 2017.

The canton has also granted its guarantee on life annuities proposed by Rentes Genevoises (not rated), a public right, not-for profit, mutual insurance institution. At the end of 2014, these guarantees amounted to CHF1.45 billion. We view related risk as limited, given the entity's current solid coverage ratio (114% as of end 2014).

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.

Key Statistics

Table 1

Republic and Canton of Geneva Financial Statistics

	--Financial year ending Dec. 31--				
(Mil. CHF)	**2013**	**2014**	**2015bc**	**2016bc**	**2017bc**
Operating revenues	7,796	8,060	7,904	7,903	8,039
Operating expenditures	7,453	7,479	7,566	7,648	7,787
Operating balance	343	581	338	255	252
Operating balance (% of operating revenues)	4.4	7.2	4.3	3.2	3.1
Capital revenues	82	78	154	61	79
Capital expenditures	1,215	772	639	708	742
Balance after capital accounts	(790)	(113)	(147)	(392)	(411)
Balance after capital accounts (% of total revenues)	(10.0)	(1.4)	(1.8)	(4.9)	(5.1)
Debt repaid	1,061	852	850	780	1,000
Gross borrowings	1,933	1,448	700	1,172	1,411
Balance after borrowings	82	483	(297)	0	0
Modifiable revenues (% of operating revenues)	78.1	78.8	77.3	77.9	77.6
Capital expenditures (% of total expenditures)	14.0	9.4	7.8	8.5	8.7
Direct debt (outstanding at year-end)	12,792	13,389	12,839	13,331	13,742
Direct debt (% of operating revenues)	164.1	166.1	162.4	168.7	170.9
Tax-supported debt (% of consolidated operating revenues)	152.6	153.5	152.3	157.9	160.1
Interest (% of operating revenues)	2.9	2.8	3.0	3.1	3.3
Debt service (% of operating revenues)	16.5	13.4	13.8	13.0	15.8

The data and ratios above result in part from Standard & Poor's own calculations, drawing on national as well as international sources, reflecting Standard & Poor's 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 Standard & Poor's expectations of the most likely scenario. CHF--Swiss franc.

Table 2

Republic and Canton of Geneva Economic Statistics

	--Financial year ending Dec. 31--				
(Mil. CHF)	**2013**	**2014**	**2015bc**	**2016bc**	**2017bc**
Population	463,919	466,918	470,512	476,006	482,545
GDP per capita (CHF)	104,166	103,495	110,548	111,978	113,472
Real GDP growth (%)	4.1	0.3	1.5	2.2	2.1
Unemployment rate (%)	6.5	5.4	5.3	5.6	5.5

The data and ratios above result in part from Standard & Poor's own calculations, drawing on national as well as international sources, reflecting Standard & Poor's independent view on the timeliness, coverage, accuracy, credibility, and usability of available information. Sources typically include national statistical offices, Eurostat, and Experian Limited. bc--base-case reflects Standard & Poor's expectation of the most likely scenario. Source: Canton of Geneva's Statistics Office (OCSTAT). CHF--Swiss franc.

Ratings Score Snapshot

Table 3

Republic and Canton of Geneva - Ratings Score Snapshot*	
Key rating factors	
Institutional framework	Extremely predictable and supportive
Economy	Very strong
Financial management	Strong
Budgetary flexibility	Average
Budgetary performance	Average
Liquidity	Adequate
Debt burden	Very high
Contingent liabilities	Moderate

*Standard & Poor's ratings on local and regional governments are based on eight main rating factors listed in the table above. Section A of Standard & Poor's "Methodology For Rating Non-U.S. Local And Regional Governments," published on June 30, 2014, summarizes how the eight factors are combined to derive the rating.

Key Sovereign Statistics

- Sovereign Risk Indicators, Oct. 12, 2015. A free-of charge interactive version is available at http://www.spratings.com/sri

Related Criteria And Research

Related Criteria

- Methodology For Rating Non-U.S. Local And Regional Governments, June 30, 2014
- 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

Related Research

- Default, Transition, and Recovery: 2014 Annual International Public Finance Default Study And Rating Transitions, June 8, 2015
- Public Finance System Overview: Swiss Cantons, May 4, 2015.
- Swiss National Bank Exchange Rate Policy Shift Has Manageable Impact For Rated Swiss Cantons' And Cities' Pension Funds, Feb. 6, 2015
- Standard & Poor's Publishes Latest Institutional Framework Assessments For International Local And Regional Governments, Feb. 5, 2015

Ratings Detail (As Of December 11, 2015)	
Geneva (Republic and Canton of)	
Issuer Credit Rating	AA-/Stable/--
Senior Unsecured	AA-
Issuer Credit Ratings History	
20-Sep-2010	AA-/Stable/--
11-Dec-2008	A+/Stable/--
02-Apr-2004	A/Stable/--

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable

Ratings Detail (As Of December 11, 2015) (cont.)

across countries. Standard & Poor's 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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