Swiss Confederation
Rating Report

SCOPE AAA STABLE OUTLOOK

Credit strengths

- Wealthy and diversified economy
- Institutional strengths
- Very robust public finances
- Excellent external resilience

Credit challenges

- Financial imbalances, large, concentrated banking sector; transition phase after UBS and Credit Suisse merger
- Uncertainties about future Swiss-EU trade relations

Rating rationale:

Wealthy and well-diversified economy: Switzerland's ratings are supported by a competitive economy, a highly skilled labour force and institutional strengths including a stable, consensus-oriented, effective policy framework, which, in aggregate, underpin its economic resilience. The Swiss economy grew robustly in 2022, although growth is slowing due to repercussions of the war in Ukraine on inflation, monetary policy, private consumption and investments.

Prudent fiscal management and low public debt: Solid public finances and the authorities' strong commitment to longer-term debt sustainability remain core credit strengths. This is underpinned by stringent, constitutionally anchored budgetary rules and favourable financing conditions.

Very robust external sector: Switzerland benefits from a significant net external asset position, highly competitive exporting industries and the safe haven status of the Swiss franc.

Rating challenges include: i) a very large, concentrated banking sector in relation to GDP, posing contingent liability risk to public finances; and ii) imbalances in the real estate market, with high levels of residential overvaluation, increasing vulnerability to market corrections. Switzerland's withdrawal from negotiations on the institutional framework agreement with the EU prolongs uncertainty over trade relations. A recent announcement by the Federal Council for the adoption of a negotiation mandate at the end of the year points towards a constructive stance by the two parties.

Switzerland's sovereign rating drivers

Risk pillars		Quantitative		Reserve currency	Qualitative*	Final rating
		Weight	Indicative rating	Notches	Notches	
Domestic Economic Risk		35%	aaa	CHF [+0]	+1/3	AAA
Public Finance Risk		20%	aaa		+2/3	
External Economic Risk		10%	aaa		+2/3	
Financial Stability Risk		10%	a+		-2/3	
ESG Risk	Environmental Factors	5%	aaa		0	
	Social Factors	7.5%	bb+		+1/3	
	Governance Factors	12.5%	aaa		0	
Indicative outcome		**aaa**			**+1**	
Additional considerations					**0**	

Note: *The qualitative scorecard adjustments, capped at one notch per rating pillar, are weighted equally with an aggregate adjustment rounded to the nearest integer. The reserve-currency adjustment applies to currencies in the IMF's SDR basket. For details, please see Scope's 'Sovereign Ratings' methodology. Source: Scope Ratings.

Outlook and rating triggers

The Stable Outlook reflects Scope's view that risks to the ratings are balanced over the next 12 to 18 months.

Positive rating-change drivers

- N/A

Negative rating-change drivers

- Financial stability risks materialise with significant negative implications for economic growth and public finances
- Significant worsening of the economic outlook, for example due to a material deterioration in relations with the EU and trade disruptions

Ratings and Outlook

Foreign currency

Long-term issuer rating	AAA/Stable
Senior unsecured debt	AAA/Stable
Short-term issuer rating	S-1+/Stable

Local currency

Long-term issuer rating	AAA/Stable
Senior unsecured debt	AAA/Stable
Short-term issuer rating	S-1+/Stable

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Bloomberg: RESP SCOP

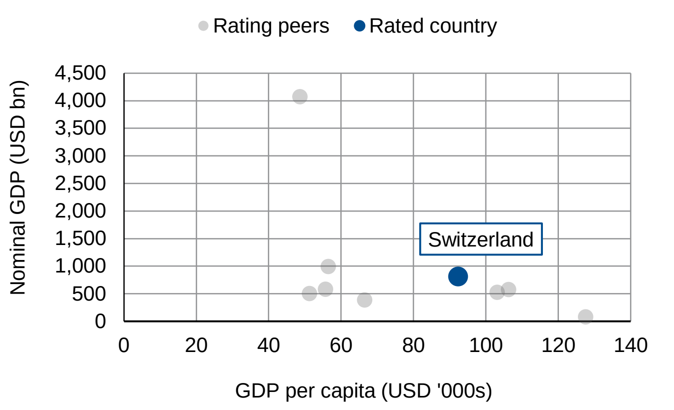
Domestic Economic Risks

- **Growth outlook:** Switzerland's economy grew by 2.1% in 2022, following the recovery at 4.2% in 2021 after the Covid-19 pandemic, although remaining below the 3.3% estimate of the 2022 federal budget. Growth was mainly driven by a recovery in service activities and private consumption which, despite rising inflation, was supported by a solid labour market performance. Growth slowed to 0.7% YoY in the last quarter of 2022, due to weaking external demand and globally increasing interest rates, which curbed investments, as well as activities in the manufacturing and service sectors. Persistent inflationary pressures weigh on private consumption, foreign trade and investments. We expect real GDP growth to slow down to 1.0% in 2023, before recovering to 2.1% in 2024.
- **Inflation and monetary policy:** Swiss consumer price inflation started to increase at the end of 2021 due to rising energy prices and rose further in 2022, averaging 2.8% YoY over the full year. Still, it remained low in an international comparison, partly due to the lower energy-intensity of the economy and the Swiss franc's nominal appreciation. CPI inflation peaked at 3.4% YoY in February 2023, before starting to decline, reaching 2.2% YoY in May, on the back of easing energy prices. However, inflation has become broad-based, resulting in higher core inflation, which peaked at 2.4% YoY in February and has remained around 2% YoY since then. To counter inflationary pressures, the Swiss National Bank (SNB) tightened monetary policy and raised its key policy rate by a total of 250bps between June 2022 and June 2023 to 1.75%. The SNB's balance sheet remains large due to high foreign currency investments, with total assets at CHF 931bn in April 2023, up from CHF 883bn in January 2023, although still remaining below the CHF 1.07trn peak reached in May 2022. The recent increase reflects substantial liquidity provision to Credit Suisse to support the government-brokered takeover by UBS, amounting to CHF 88bn on 31 May 2023.
- **Labour markets:** The labour market performed robustly over 2020-22, despite the Covid-19 pandemic and energy shocks. After dipping in Q2 2020, employment has been on a robust upward trend, standing around 130,000 persons above its level two years ago in Q1 2023. The unemployment rate was at a low 2% in May 2023. The Swiss labour market remains tight and vacancies high with companies experiencing difficulties in recruiting. Despite the economic slowdown we expect the labour market to remain solid and the unemployment rate to increase only modestly to 2.2% in 2023 and 2.3% in 2024.

Overview of Scope's qualitative assessments for Switzerland's *Domestic Economic Risks*

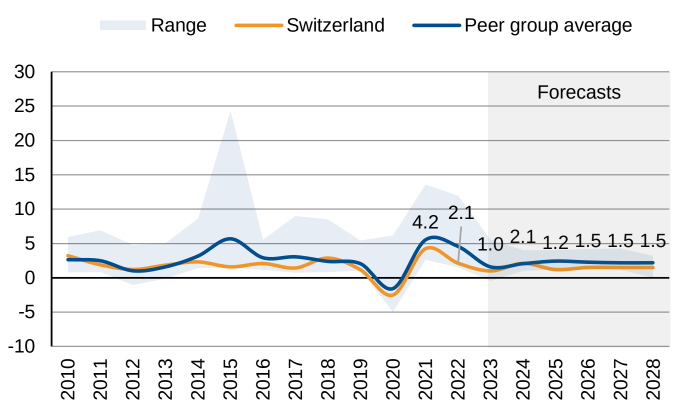
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aaa	Growth potential of the economy	Neutral	0	Moderate growth potential, in line with peers
	Monetary policy framework	Neutral	0	Swiss National Bank is a credible central bank. Flexibility is relatively constrained due to the sensitivity to FX developments
	Macro-economic stability and sustainability	Strong	+1/3	Very competitive and diversified economy, highly skilled labour force, well-developed infrastructure

Nominal GDP and GDP per capita, USD



Source: IMF World Economic Outlook (WEO), Scope Ratings

Real GDP growth, %



Source: IMF WEO, Scope Ratings forecasts

Public Finance Risks

- **Fiscal outlook:** Switzerland's ratings are further supported by very robust public finances. The central government's debt brake and debt brakes in most cantons call for balanced budgets over the economic cycle. This has resulted in general government budget surpluses averaging 0.9% of GDP over 2015-19. The government's fiscal response to the Covid-19 crisis was effective, targeted and sizeable, with total federal fiscal support of around CHF 40bn between 2020 and 2022. This led to general government deficits of 3.1% of GDP in 2020 and 0.3% in 2021. Covid-19 spending decreased significantly in 2022 to CHF 3.7bn, although Russia's invasion of Ukraine required around CHF 1.2bn additional spending mostly for refugees' integration. However, expenditure remained overall contained and revenue grew robustly, driven by VAT and direct federal taxes, resulting in a general government budget surplus of 1% of GDP. The temporary economic slowdown will be reflected in the revenue performance and some costs will remain moderately high, such as the ones related to housing and integrating Ukrainian refugees and higher defence spending, set to reach 1% of GDP by 2030.

  Overall, fiscal consolidation should progress, and we expect very slight, continued general government surpluses in coming years. Despite having recorded profits for CHF 26.9bn in Q1 2023, the SNB is not likely to resume paying out dividends to the Confederation and the cantons, as high market volatility still poses uncertainty around full-year profits.

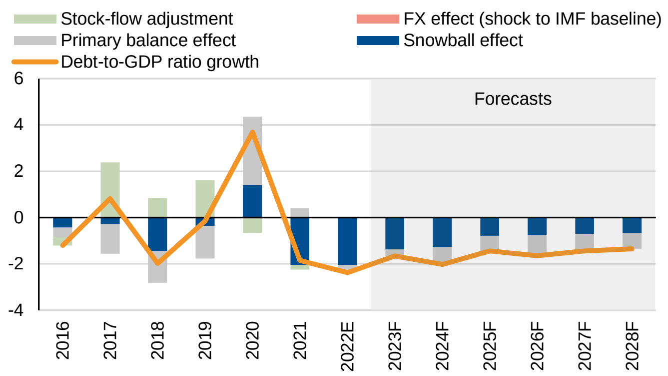
- **Debt trajectory:** The improvement in the general government fiscal balance is accompanied by a decline in the general government debt-to-GDP ratio, which we project to decrease to 39.7% of GDP this year, from 41.4% of GDP in 2022, and to trend towards 32% by the end of 2028. We expect contingent liability risks, including liability risks from the UBS-Credit Suisse merger, to be modest and in any case spread out over multiple years.

- **Debt profile and market access:** The Swiss Confederation's market access is very strong. The 10-year government bond yield remained negative at -0.4% and -0.2% in 2020 and 2021, respectively. It has started to increase in 2022 and peaked above 1.5% in Q1 2023, amid monetary tightening and financial market turmoil, before returning around 0.9% on average in June. A conservative debt profile limits market and interest-rate risks, as bond issues are entirely denominated in Swiss francs, are fixed-rate and have a long average maturity of 10.2 years. Finally, the Confederation had a sizeable cash buffer of CHF 16.6bn at YE 2022.

Overview of Scope's qualitative assessments for Switzerland's *Public Finance Risks*

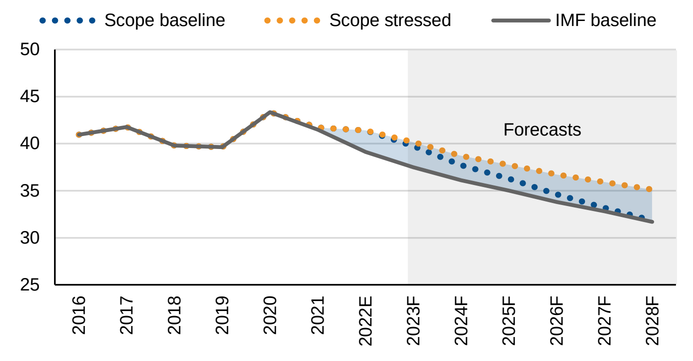
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aaa	Fiscal policy framework	Strong	+1/3	Stringent, constitutionally anchored fiscal rules, track record of prudent and stable fiscal policies
	Debt sustainability	Neutral	0	Moderate public debt levels, strong commitment to longer-term debt sustainability
	Debt profile and market access	Strong	+1/3	Highly developed and liquid capital markets supported by Swiss franc's safe-haven status, favourable debt financing costs, long debt maturity

Contributions to changes in debt levels, pps of GDP



Source: IMF WEO, Scope Ratings forecasts

Debt-to-GDP forecasts, % of GDP



Source: IMF WEO, Scope Ratings forecasts

External Economic Risks

- **Current account:** Switzerland's ratings benefit from high and consistent current account surpluses. These averaged 6.2% of GDP over 2015-19. After a significant contraction to 0.4% of GDP in 2020, the current account surplus started to recover rapidly in 2021 and reached 10.3% of GDP in 2022, boosted by a widening of the goods current account, increasing from 8.6% in 2020 to 15.1% in 2022. Switzerland's current account resilience is underpinned by highly specialised, price-insensitive exporting industries, such as pharmaceuticals, which made up around 35% of goods exports in 2022.

- **External position:** Switzerland's robust external position is underpinned by a high net international investment position of 93.6% of GDP as of Q4 2022, below the peak of 131% of GDP in Q1 2021, but in line with pre-pandemic levels. External debt of 285% of GDP in Q1 2023 is relatively high. Most external debt is short-term and held by banks (79% of GDP at Q1 2023), followed by other sectors, including non-financial corporations (45%).

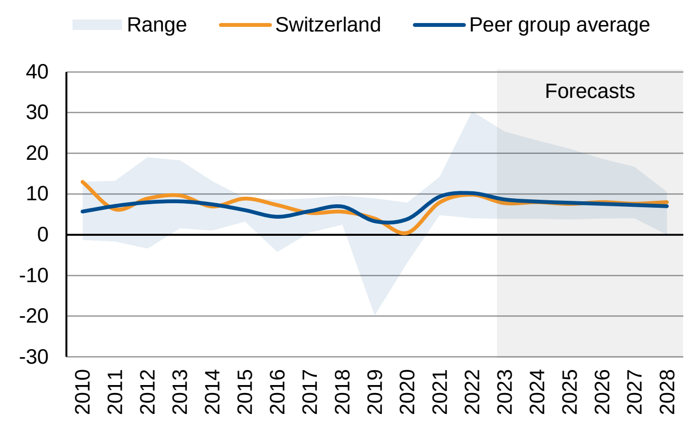
- **Resilience to shocks:** The Swiss franc is a safe haven currency, and the SNB holds large foreign currency investments of around 100% of GDP as of April 2023. As a highly open economy, Switzerland is sensitive to global trade shocks and relies on favourable trade relations with its main trading partners, such as the EU. The breakdown of negotiations in May 2021 on the institutional framework agreement with the EU, which was supposed to consolidate existing bilateral trade agreements among the two parties, represents a moderate longer-term risk to the Swiss economic outlook, since lapsing trade arrangements are re-negotiated only on a case-by-case basis and might not all be rolled over.

  A re-engagement between the Swiss delegation and the EU started in March 2022 in the form of exploratory talks, having currently reached the 10th round. Talks have shown progress in a number of areas, including state aid and the free movement of persons, preparing the ground for actual negotiations. The Federal Council recently announced work on key parameters for a negotiating mandate, to be adopted by the end of the year.

Overview of Scope's qualitative assessments for Switzerland's *External Economic Risks*

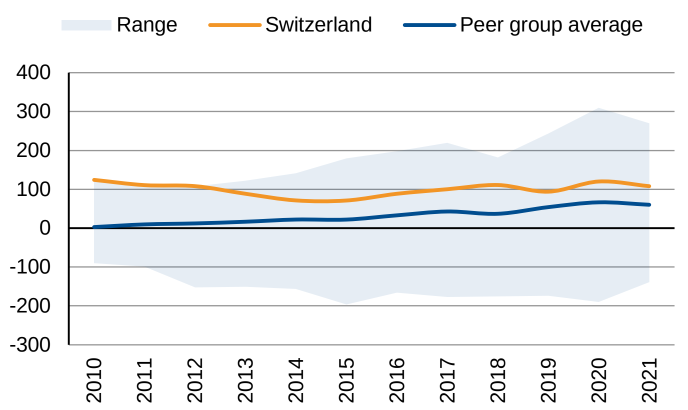
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aaa	Current account resilience	Strong	+1/3	Persistent current account surpluses, reflecting a competitive external sector and a substantial share of price-intensive exports
	External debt structure	Neutral	0	Large net external asset position, around two thirds of external liabilities and denominated in local currency
	Resilience to short-term external shocks	Strong	+1/3	Large net external asset position and Swiss franc's safe haven currency status underpin external-sector resilience

Current-account balance, % of GDP



Source: IMF WEO, Scope Ratings

Net international investment position (NIIP), % of GDP



Source: IMF, Scope Ratings

Financial Stability Risks

- **Banking sector:** The Swiss banking system is very large (total assets of CHF 3.5trn, or 448% of GDP as of Q1 2023) and concentrated, resulting in relevant financial stability risks for the risk profile.

  In March 2023, following a confidence crisis and substantial deposit outflows at Credit Suisse, Swiss authorities brokered a merger between UBS and Credit Suisse, which was completed on 12 June 2023. The merger was supported by a significant liquidity provision by the SNB. Outstanding net borrowings from the SNB amounted to CHF 88bn as of 31 May 2023, consisting of CHF 38bn under emergency liquidity assistance (ELA) and CHF 50bn under ELA+. A novel Public Liquidity Backstop (PLB) facility has been repaid. Further, the government provided a guarantee of up to CHF 9bn for losses incurred on a specific Credit Suisse portfolio, which would only become effective if losses exceed CHF 5bn.

  The prompt intervention of regulators, the strength of UBS' business model and balance sheet and the forceful liquidity provision helped stabilise market confidence and financial stability. At the same time, the merger results in greater concentration of financial system contingency risks. According to the unaudited, pro-forma condensed balance sheet, total assets of the combined entity were around USD 1.73trn as of December 2022 (CHF 1.6trn, or around 208% of 2022 Swiss GDP).

  The Federal Council is currently holding consultations to convert into permanent law some of the crisis measures used to support the UBS-Credit Suisse merger, including the PLB. In addition, a more comprehensive revision of the too-big-to-fail regulation is expected to take place in the spring of 2024.

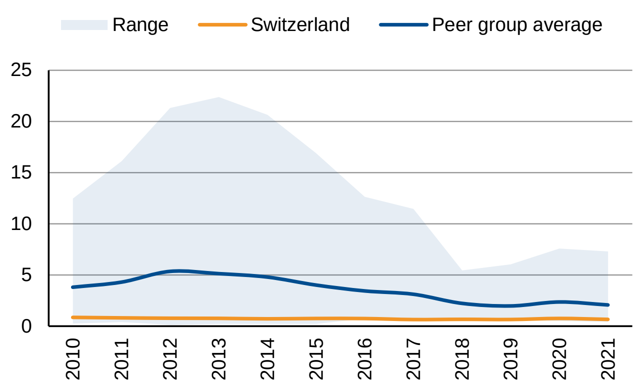
- **Private debt:** Private sector debt is elevated at around 271% of GDP as of Q4 2022, one of the highest ratios among peers. Household debt was 128% of GDP in Q4 2022, representing mostly mortgages. This is offset by household wealth estimated at 385% of GDP in 2022.

- **Financial imbalances:** Low interest rates have resulted in a continued increase in residential property prices starting from the second half of 2020. Price increases for single-family dwellings and apartments peaked at 8.8% YoY and 7.5% YoY, respectively, in H1 2022. However, monetary tightening and the consequent increase in interest rates cooled mortgage markets and moderated real estate price growth to around 3.6% YoY on average for single-family dwellings and apartments in Q1 2023. Banks' mortgage lending grew by 3.3% YoY in March 2023, in line with its long-term trend.

Overview of Scope's qualitative assessments for Switzerland's *Financial Stability Risks*

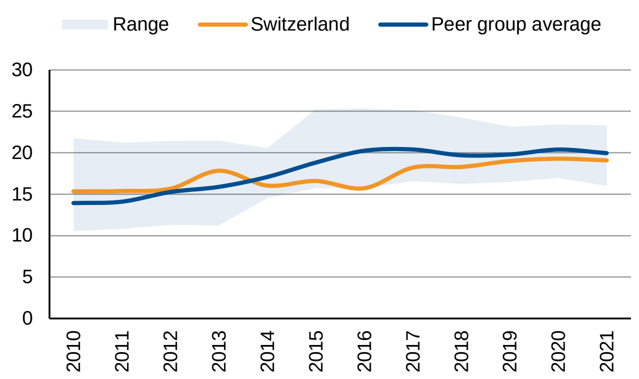
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
a+	Banking sector performance	Weak	-1/3	Well-capitalised and liquid banking sector with strong asset quality, although highly concentrated. Bank profitability remains structurally constrained. The Credit Suisse crisis highlights contingency risks
	Banking sector oversight	Neutral	0	Effective financial policymaking and stringent regulatory financing requirements mitigate financial system risk
	Financial imbalances	Weak	-1/3	A very large banking sector represents a risk of contingent liabilities; persistent risk of correction in the real estate market

Non-performing loans, % of total loans



Source: IMF, Scope Ratings

Tier 1 ratio, % of risk-weighted assets



Source: IMF, Scope Ratings

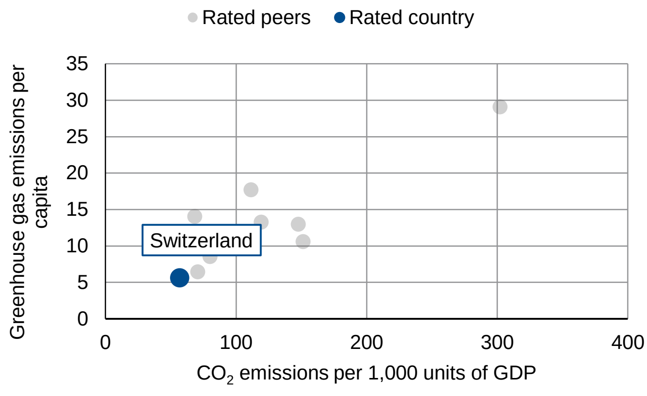
ESG Risks

- **Environment:** Switzerland's environmental risk profile is strong. Natural disaster risks are limited and the economy's carbon intensity (our proxy for transition risk to a greener economic model) is very low. However, the country has a relatively poor performance in terms of its footprint of consumption relative to available biocapacity, given the country's import dependency for many of its natural resources. Switzerland has no natural gas reserves on its territory and no domestic storage capacities, therefore relies entirely on imported natural gas, representing 15.4% of the country's final energy consumption in 2021. The rest of the energy mix is mostly composed of petroleum and motor fuels (43%) and electricity (26%, of which 62% produced using hydropower and 29% nuclear power). Renewable energy sources made up 28% of final energy consumption in 2021. The government is aiming for a 50% reduction in carbon emissions by 2030 relative to 1990 levels. A new CHF 3.2bn climate bill recently backed by almost 60% of voters targets carbon neutrality by 2050. Further, the country imposes a carbon levy on fossil fuels, which was increased to CHF 120 per tonne of CO_2 (around USD 130) in 2022 from CHF 96 in 2021.
- **Social:** Social outcomes in Switzerland are very strong, reflecting a low risk of poverty (8.7% of the population affected by income poverty in 2021) and strong educational outcomes, as shown by a high share of persons with tertiary education and high average performance in mathematics, reading and sciences according to 2018 PISA results. Challenges relate to a high share of part-time labour among women (around 58% in 2022), reflecting high costs for child-care and high wages, and second, a relatively high unemployment rate among foreigners. In the longer term, an ageing population will make the pension system's first pillar, the AHV system, more costly. A reform of the system to improve long term financial viability was passed by the Parliament and approved by a popular referendum, now set to come into effect in 2024.
- **Governance:** We assess Switzerland's governance as very strong given its excellent institutions, stable political conditions and effective policy making. As a direct democracy, key political issues are decided by popular referenda. The federal council consists of seven members from the four major political parties, each heading one government department, and takes decisions based on consensus. The next general election is scheduled for October 2023.

Overview of Scope's qualitative assessments for Switzerland's *ESG Risks*

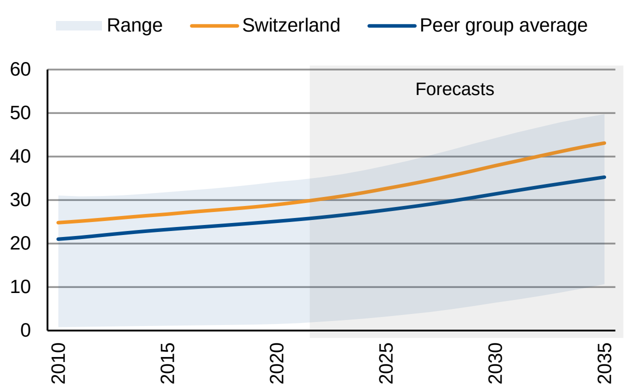
CVS indicative rating	Analytical component	Assessment	Notch adjustment	Rationale
aaa	Environmental factors	Neutral	0	Transition risk mitigated by a robust regulatory framework, including a carbon levy of CHF 120bn of CO_2 and considerable public expenditure
	Social factors	Strong	+1/3	Very high human development and employment rate, significant R&D expenditure, high labour market flexibility
	Governance factors	Neutral	0	Stable political environment, institutional effectiveness and a consensus-oriented policy framework; failure to reach institutional framework agreement with the EU creates uncertainty over future EU-Swiss relationship

Emissions per GDP and per capita, $mtCO_2e$



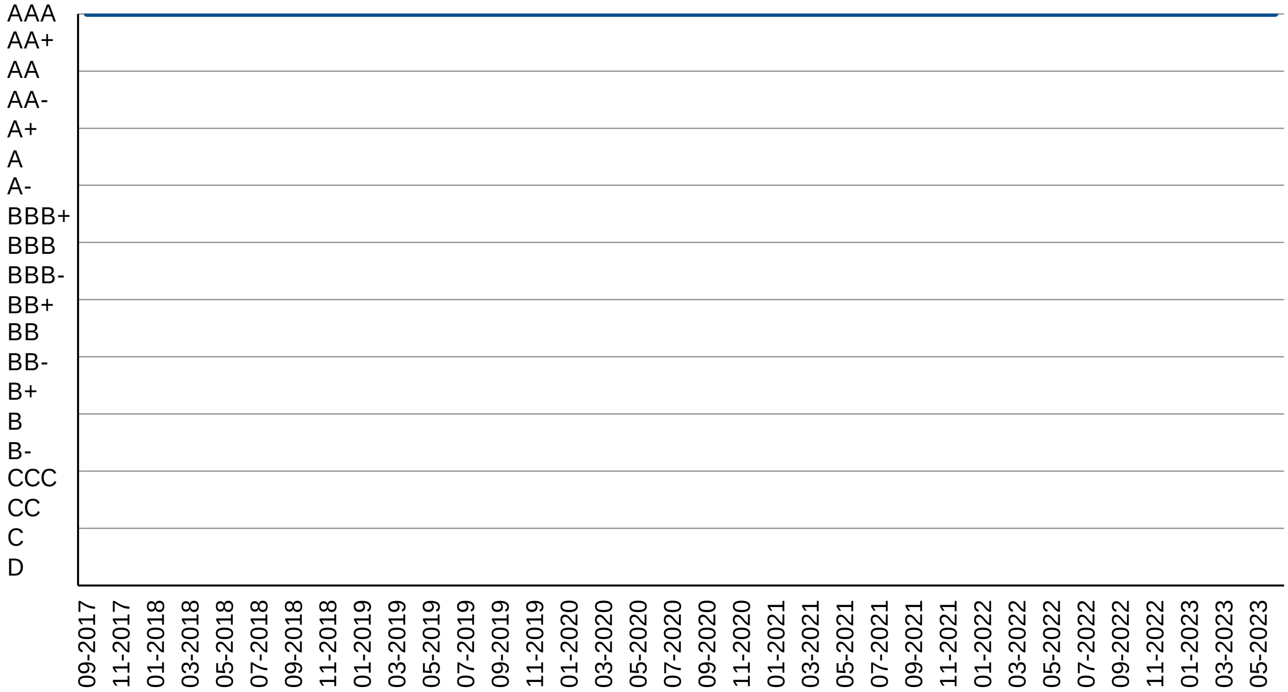
Source: European Commission, Scope Ratings

Old age dependency ratio, %



Source: United Nations, Scope Ratings

Appendix I. Rating history (foreign-currency long-term debt)



NB. Positive/Negative Outlooks are treated with a +/-0.33-notch adjustment. Credit Watch positive/negative with a +/-0.67-notch adjustment.

Appendix II. Rating peers

Rating peers are related to sovereigns with an indicative rating in the same rating category or in adjacent categories per Scope's Core Variable Scorecard, including a methodological reserve-currency adjustment.

Peer group*
Denmark
Germany
Ireland
Luxembourg
Netherlands
Norway
Sweden

*Publicly rated sovereigns only; the full sample may be larger.

Appendix III. Statistical table for selected CVS indicators

This table presents a selection of the indicators (24 out of 30 – with the governance indicator reflecting a composite of six indicators) used in Scope's quantitative model, the Core Variable Scorecard, in line with Scope's Sovereign Rating Methodology. The metrics and sources for the data presented here ensure comparability across global peers and may therefore differ from national and other selective international statistics.

Pillar	Core variable	Source	2018	2019	2020	2021	2022
Domestic Economic	**GDP per capita, USD '000s**	IMF	85.5	84.5	85.9	92.2	92.4
	Nominal GDP, USD bn	IMF	725.8	721.8	739.0	799.7	807.2
	Real growth, %	IMF	2.9	1.2	-2.5	4.2	2.1
	CPI inflation, %	IMF	0.9	0.4	-0.7	0.6	2.8
	Unemployment rate, %	WB	4.7	4.4	4.8	5.1	-
Public Finance	**Public debt, % of GDP**	IMF	39.8	39.6	43.3	41.5	39.1
	Net interest payment, % of revenue	IMF	0.3	0.2	0.2	0.4	0.4
	Primary balance, % of GDP	IMF	1.4	1.4	-3.0	-0.4	0.3
External Economic	**Current-account balance, % of GDP**	IMF	5.6	3.9	0.4	7.9	9.8
	Total reserves, months of imports	WB	15.3	16.7	22.0	19.8	-
	NIIP, % of GDP	IMF	111.1	94.0	120.2	108.1	96.5
Financial Stability	**NPL ratio, % of total loans**	IMF	0.7	0.6	0.8	0.7	-
	Tier 1 ratio, % of risk-weighted assets	IMF	18.2	18.6	17.8	18.4	18.8
	Credit to the private sector, % of GDP	BIS	242.8	263.1	274.3	278.0	-
ESG	**CO_2 per EUR 1,000 of GDP, $mtCO_2e$**	EC	64.4	63.4	57.6	57.0	-
	Income share of bottom 50%, %	WID	22.9	22.6	22.6	22.6	-
	Labour-force participation rate, %	WB	84.2	84.2	-	-	-
	Old-age dependency ratio, %	UN	28.0	28.4	29.0	29.6	30.2
	Composite governance indicators*	WB	1.8	1.7	1.7	1.7	-

* Average of the six World Bank Worldwide Governance Indicators.

Appendix IV. Economic development and default indicators

IMF Development Classification	Advanced economy
5y USD CDS spread (bps) as of 3 July 2023	20bps

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