ACRA

SOVEREIGNS

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# ACRA AFFIRMS LT AAA TO SWITZERLAND, OUTLOOK STABLE


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ACRA has affirmed the following ratings to the Swiss Confederation (hereinafter, Switzerland, or the country) under the international scale:

- Long-term foreign currency credit rating at AAA and local currency credit rating at AAA.
- Short-term foreign currency credit rating at S1+ and local currency credit rating at S1+.

The outlook on the long-term foreign currency credit rating is Stable and local currency credit rating is Stable. The Stable outlook assumes that the rating will highly likely stay unchanged within the 12 to 18-month horizon.

Positive rating assessment factors

- Very high level of wealth.
- Developed, diversified, innovative and competitive national economy.
- Moderate level of public debt, its safe structure, and a large domestic financial market.
- Developed institutional base.

Negative rating assessment factors

- High level of private debt.
- Large size of the banking sector, which may potentially become a source of contingent liabilities for the government in adverse scenarios, including serious changes to European financial sector regulations.

## CREDIT RATING RATIONALE

Switzerland's AAA sovereign credit rating is based on a developed, diversified, innovative and competitive economic structure, and a moderate level of public debt. In ACRA's opinion, the risks of a high level of private debt and the large size of the banking sector, combined with the latest changes in the sector's landscape, potentially influencing contingent liabilities for the government, are balanced by the high level of household assets, as well as the sound fiscal policy and institutional quality.

**Macroeconomics**

In ACRA's opinion, the economy of Switzerland, one of the ten richest countries in the world in terms of GDP per capita, is expected to grow by 1.3–1.5% in 2024–2025 on average, which is close to its long-term potential growth (estimated at around 1.5% by the country's State Secretariat for Economic Affairs (SECO)). Headwinds to country's economic growth may primarily come from trade partners' subpar growth.

ACRA expects inflation in Switzerland to remain moderate in the near future. Although relatively low by global standards, in 2022–2023 the CPI rate was above the 0–2% target corridor set by

the Swiss National Bank (SNB). In 2024–2025, ACRA expects it to moderate toward 1.5%. The disinflationary effect, which partly came from the SNB hiking the policy rate from -0.75% in December 2022 to 1.75% in June 2023, was significant. In March 2024, the SNB became one of the first major central banks to start lowering its policy rate.

**Public finances**

Unlike many developed countries, after a relatively large anti-crisis package in 2020–21, Switzerland easily managed to preserve its room to maneuver for extensive countercyclical fiscal policies, even in the higher interest rate environment. ACRA expects the country's public debt level to remain lower than 40% of GDP in the foreseeable future and the general government balance will most probably stay slightly positive (close to 0.5% of GDP in 2024).

ACRA assumes that the strong fiscal rule at the confederation budget level will keep the structural balance of the general government close to 0% in the medium term. The fiscal rule mandates balancing the budget throughout the business cycle by allowing for a certain level of deficit during times of recession and suggesting surpluses during times of economic growth, while also making exceptions for extraordinary circumstances.

However, in the medium to long term, maintaining public debt at a moderate level may be challenged by the need to increase spending due to the country's population ageing. In September 2022, the OASI (or AHV, first pillar of the pension system) reform was accepted in a popular vote after many years of discussion (the changes incurred by the reform have been in effect since January 2024). It includes increasing the women's retirement age to 65, making it equal to that of men, and additional value-added tax to fund the system. Although these developments will temporarily and partly alleviate the rising burden on the pension system, the second pillar (BVG) still needs to be revised to balance the system. In March 2023, the reform of BVG was passed by the parliament and currently awaits a referendum in 2024.

It is also worth noting that the total volume of banking sector assets amounts to more than 400% of nominal GDP. The sheer size of the banking sector poses a contingent liability risk and places Switzerland in the group of countries whose economies are highly dependent on the banking sector — the sector generates 5–10% of annual GVA.

In March 2023, an important development significantly changed the Swiss banking landscape. On March 16 and 19, 2023, the Federal Council decided on various measures to prevent the imminent failure of Credit Suisse, one of the two major globally oriented national banks. After a series of market losses and reputational pressure, Credit Suisse was bought by its peer and rival, UBS. This private takeover was supported by a liquidity backstop provided by the SNB with a CHF 100 bln limit. In addition, to enable the takeover, the federal government provided a loss guarantee of up to CHF 9 bln for a specific portfolio of difficult-to-assess Credit Suisse assets.

In ACRA's view, even without immediate financial implications, the aforementioned takeover should be assessed as a rise in long-term contingent liabilities of the government. As a result of the deal, a newly created banking group makes the whole banking sector of Switzerland more interconnected, which may bring more risks to overall financial stability. The enormous size of the group also puts the two banks even more in the public focus in the too-big-to-fail logic.

**External position**

Switzerland's external position is comparatively strong; it is supported by persistently high current account surpluses and a very high positive international investment position (mostly due to international reserves). ACRA assumes that Switzerland's export structure, which has a big share of pharmaceutical, chemicals and jewelry exports, will allow the country to maintain a high current account surplus in 2024 and beyond in line with the pre-pandemic levels of 5–8% of GDP.



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A relatively high level of external debt coverage by reserves and investors' perception of the Swiss franc as a stable global currency also support the strength of the country's external position. ACRA notes that investors turn to franc-denominated assets during periods of global economic slowdown and heightened international uncertainty. This triggers appreciation of the franc and creates deflationary pressure. To prevent this in 2020–21, the SNB resorted to monetary policy measures aimed at preventing the appreciation of the franc, including injecting francs into the market and accumulating foreign currency liquidity. In 2022–2023, international reserves contracted moderately due to both market operations and exchange rate changes — ACRA expects them to stay at around 100% of GDP in the mid-term.

**Institutions**

In ACRA's view, Switzerland can still be, in some sense, considered a "safe haven" due to the highest level of trust in its public institutions and authorities and high quality of public governance. Over the past ten years, Switzerland has had some of the highest and most stable World Governance Indicators (WGIs) as measured by the World Bank. This is a reflection of the high quality of institutional governance and the very favorable environment for allocating resources within the economy.

However, it may be very important in the future that the EU is creating new capital guidelines with higher EU market access barriers for non-EU banks (Switzerland is not an EU member). If implemented, these guidelines will prevent banks without a physical presence in an EU country from actively serving customers there. This could pose a significant risk for Switzerland's globally oriented systemically important banks — Credit Suisse and UBS. A number of other sectors may also be affected by the result of negotiations between Swiss and EU officials concerning the details of bilateral agreements in the economic sphere (the so-called, 3rd Bilateral Package).

## SOVEREIGN MODEL APPLICATION RESULTS

Switzerland has been assigned an AAA Indicative credit rating in accordance with the core part of ACRA's sovereign model. One of the modifiers in the modifiers part of the model allows the Indicative credit rating to be decreased. This includes the following, which is determined by the Methodology for Credit Rating Assignment to Sovereign Entities under the International Scale:

- Contingent liabilities and the risk of them materializing.

A positive adjustment has been made for the following modifiers:

- Sustainability of economic growth.
- Fiscal policy and budget flexibility.
- Debt sustainability and market access.
- Balance of payments stability.

In view of the abovementioned modifiers, Switzerland's Indicative credit rating has not been changed, and the Final credit rating of AAA has been assigned. There are no analytical adjustments and limitations that could result in an adjustment of the Final rating. In connection with this, the long-term foreign currency credit rating remains at AAA.

## POTENTIAL OUTLOOK OR RATING CHANGE FACTORS

A negative rating action may be prompted by:

- Serious financial shock for Switzerland's banking sector associated with the loss-generating repercussions of a global recession.
- Negative scenario of developments in the negotiations between Switzerland and the EU on financial regulations or trade.

## REGULATORY DISCLOSURE

The sovereign credit ratings have been assigned to the Swiss Confederation under the international scale based on the Methodology for Credit Rating Assignment to Sovereign Entities under the International Scale and the Key Concepts Used by the Analytical Credit Rating Agency Within the Scope of Its Rating Activities.

The sovereign credit ratings of the Swiss Confederation were published by ACRA for the first time on September 10, 2019. The sovereign credit ratings and their outlooks are expected to be revised within 182 days following the publication date of this press release as per the Calendar of sovereign credit rating revisions and publications.

The sovereign credit ratings are based on information from publicly available sources and ACRA's own databases. The sovereign credit ratings are unsolicited. The Swiss government did not participate in the credit rating assignment.

In assigning the credit ratings, ACRA used only information, the quality and reliability of which were, in ACRA's opinion, appropriate and sufficient to apply the methodologies.

ACRA provided no additional services to the Swiss government. No conflicts of interest were discovered in the course of the sovereign credit rating assignment.

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