SCHWEIZERISCHE NATIONALBANK
BANQUE NATIONALE SUISSE
BANCA NAZIONALE SVIZZERA
BANCA NAZIUNALA SVIZRA
SWISS NATIONAL BANK

News Conference

Zurich, 14 December 2006

Introductory remarks by Jean-Pierre Roth

As stated in our press release, the Swiss National Bank is raising its target range for the three-month Libor with immediate effect by 0.25 percentage points to 1.50–2.50%. The SNB intends to hold the rate in the middle of the target range for the time being.

Economic activity in Switzerland is very robust. Next year, the economic trend is likely to continue favourable, albeit somewhat less pronounced. This will have a positive effect on the labour market. The National Bank is expecting real GDP to grow by just under 3% in 2006 and by around 2% in 2007.

Declining oil prices have pushed back inflation. Average inflation for 2006 is likely to stand at 1.1%. By lifting the target range, the National Bank ensures that the inflation outlook will remain favourable, even in view of the high level of utilisation of economic resources. On the assumption of an unchanged three-month Libor of 2.00%, it expects annual inflation to reach 0.4% in 2007 and 0.9% in 2008. If the economy performs as expected, the SNB will further pursue its strategy of gradual normalisation of its interest rates.

The economy is currently in excellent shape and has clearly strengthened during the past two years. At the monetary policy assessment at the end of 2004, we had suspended a normalisation of the interest rates after previously having lifted the three-month Libor from a low point of 0.25% to 0.75% in June and September. The three-month Libor remained at that level up to December 2005 when we made the decision to resume the normalisation process, given the improved economic outlook. Today's decision – an interest rate hike for the fifth time in succession – confirms the stance we have taken.

International environment

The change in the international environment with the most tangible impact since the monetary policy assessment in September concerns the price of oil. The current oil prices are clearly below the highest level of 78 dollars per barrel of Brent crude which was reached in August. Will we see higher oil prices again? There is no real conclusive answer to this question. What we have witnessed is nonetheless the longest interruption of a rising trend since the beginning of 2004. This decline will weaken inflation in most countries in the year ahead. However, the economic impact of the reduced oil prices is likely to be low, if we bear in mind that the oil price is still approximately three times higher than it was five years ago. At least the oil price has not put any additional damper on the economy since the last monetary policy assessment.

Another significant factor for Switzerland is the marked improvement of the economic situation in Europe, in particular in Germany. For 2006, growth forecasts in our neighbouring countries have been gradually revised upward; for 2007, development is expected to be more muted. Economic activity in the United States, however, has slowed at a somewhat faster pace than anticipated. In 2007, the US economy is set to expand in the area of potential growth again. Asia will continue its dynamic growth pattern.

Economic situation

What does the situation look like in Switzerland? As anticipated at the last monetary policy assessment, the economic situation has continued to improve. It is both balanced and broadly based. As the latest employment figures reveal, the momentum in the economy has spilled over into the labour market. A great many new jobs were created in the third quarter, and unemployment continued to decline. The number of gainfully employed persons rose by approximately 100,000 from Q3 2005 to Q3 2006. The unemployment rate is likely to fall below the 3% mark at the beginning of 2007. The brighter outlook on the labour market has improved job security and strengthened consumer confidence. Expenditure by private households is soaring. Companies appear upbeat as well. Many industries, such as manufacturing, construction and the hotel trade, report full employment. According to our assessment, this translates into unchanged growth in real gross domestic product (GDP) of just under 3% in 2006.

For 2007, we predict a decline in economic momentum. Almost all components of demand continue to grow, albeit at a more moderate pace. Private consumption will benefit from the healthy improvement in disposable income. Equipment investment is being stimulated by the high rate of utilisation of production capacity and the favourable business outlook in many industries. Residential construction is likely to see a measure of calm. Yet increased investment in commercial and industrial building may offset this development to some extent. The somewhat weaker global economic development – though still favourable overall - will probably continue to have a positive impact on exports. For 2007, we expect overall GDP growth of about 2%.

Monetary developments

Allow me to explain developments in the financial markets and the monetary aggregates. Two topics merit particular attention: the development of credit and money supply and the exchange rate.

In addition to long-term interest rates and exchange rates, loans – among other things – play an important role when changes in key interest rates are transmitted to the economy. What information can we derive from the development of lending activity? Loans are registering constant growth. Mortgage loans, which account for the great majority of all bank loans, have grown at a rate of more than 5% since 2003. This is a reflection of the clearly expansionary monetary policy at that time. The growth rate of mortgage loans has gradually slowed, however, and is now slightly below 5%. This is nevertheless still a high growth rate.

Other loans, however, are witnessing stronger growth and are currently expanding by 6%. Unsecured loans, in particular, are rising substantially. During phases of favourable economic development, there is greater willingness to grant unsecured loans. This was the case in 1999, when the economy found itself in a similarly robust state. There is a long-term correlation between loan volume and the M3 aggregate. Loan development typically lags behind the development of money supply. Monetary aggregates have grown only moderately for the past three years. The M3 monetary aggregate is currently growing at a modest 2%, while M1 and M2 are even registering a decline. The measured development of the monetary aggregates suggests a slowdown in lending.

The development of the Swiss franc attracted considerable attention as it has weakened vis-à-vis the euro since the beginning of the year, although it has firmed against the US dollar. To gauge the effects of exchange rates on the economy, we need to make use of the inflation-adjusted exchange rate that is also weighted to take account of the importance of individual trading partners. Measured by this real, effective exchange rate, the Swiss franc today is at the same level as it was in 2000.

In what way do exchange rate developments enter into our decision-making process? The exchange rate is important to the extent that it influences inflation, either directly via the prices of imported goods or indirectly via the business cycle.

Volatility of the Swiss franc against the euro has been negligible as of late. This relative calm should not, however, deceive us. It is not necessarily going to last. Experience has shown that phases of a weaker Swiss franc can be followed by periods in which the franc exhibits an upward trend. Financial market players and businesses should therefore be aware of the exchange rate risks they take.

Monetary policy decision

The inflation outlook forms the basis for the monetary policy decision. How does this look to us? As has already been pointed out in the considerations on the economic situation, there is likely to be an above-average utilisation of economic resources. The monetary analysis shows that lending is still growing vigorously and that the Swiss franc is trending relatively lower against the euro. Yet the inflation outlook remains favourable. The reasons are three-fold: First, falling oil prices will push inflation down considerably next year, at least during the first six months. Second, the opening of the labour market is making production more flexible, thereby exerting a favourable influence on inflation. Third, the National Bank lifted its interest rates at an early stage. The chief contribution of today's interest rate adjustment is to prevent resources from being over-utilised in 2007 and 2008. As a consequence, inflation is also likely to be muted in 2008 and 2009.

Inflation forecast graph

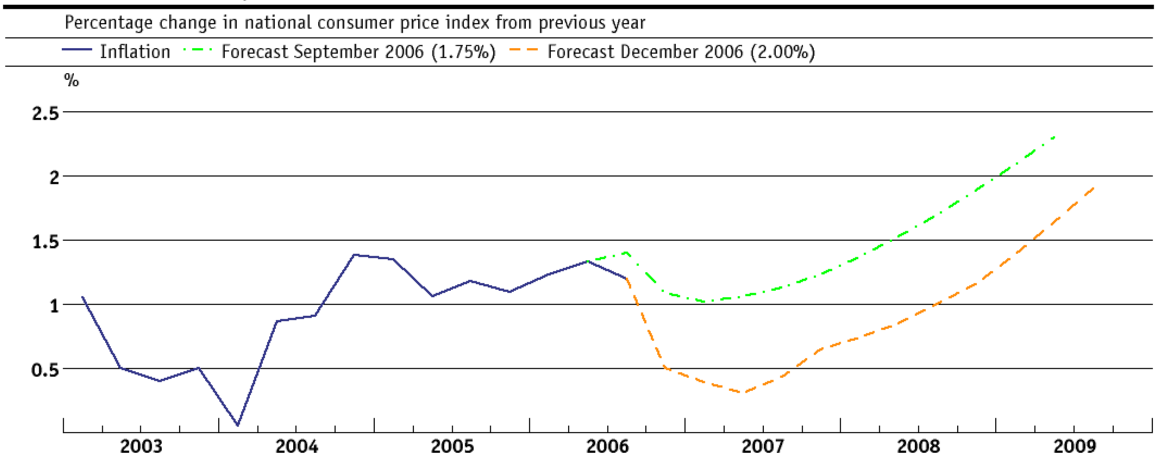
The new inflation forecast is shown in the graph as a red dashed line. It covers the time span from Q4 2006 to Q4 2009 and depicts the inflation forecast on the assumption that the interest rate remains at 2.00% during this period of time. The dash-dotted green curve shows the inflation outlook published after the interest increase of September, which was based on a constant three-month Libor of 1.75%. The red line is clearly lower than the green one. This is partly due to falling oil prices and partly results from the dampening effect of today's interest rate increase. The level of inflation expected in 2007 is 0.4%.

However, as is evident from the inflation dynamic, the effect of a 2.00% interest rate is still expansionary.

Continuation of previous monetary policy

With today's decision to increase the three-month Libor by 25 basis points, we are adhering to our previous monetary policy course of gradual normalisation. In so doing, we are pursuing the goal of continuing to ensure long-term price stability. If the economy performs as expected, we will further pursue this strategy.

Inflation forecast of September 2006 with Libor at 1.75% and of December 2006 with Libor at 2.00%



Observed inflation December 2006

	2003				2004				2005				2006			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Inflation	1.05	0.50	0.40	0.50	0.06	0.87	0.91	1.38	1.35	1.06	1.18	1.10	1.23	1.33	1.20	

Inflation forecast of September 2006 with Libor at 1.75% and of December 2006 with Libor at 2.00%

	2006				2007				2008				2009			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Forecast September 2006, Libor at 1.75%			1.40	1.09	1.02	1.06	1.13	1.23	1.36	1.53	1.70	1.89	2.09	2.30		
Forecast December 2006, Libor at 2.00%				0.50	0.40	0.31	0.44	0.65	0.74	0.85	1.00	1.17	1.38	1.64	1.90	