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# Business cycle trends

SNB regional network

Report for the attention of the Governing Board of the Swiss National Bank for its quarterly assessment of June 2015

## **Second quarter of 2015**

The Swiss National Bank's delegates for regional economic development are constantly in touch with companies from different areas of the economy. This report is based on discussions conducted from mid-April to early June 2015 with 225 managers and entrepreneurs on the current and future situation of their companies and on the economy in general. The selection of companies differs from one quarter to the next. It reflects the industrial structure of the Swiss economy, based on the breakdown of GDP (excluding agriculture and public services).

### **Regions**

Central Switzerland  
Eastern Switzerland  
Geneva  
Italian-speaking Switzerland  
Mittelland  
Northwestern Switzerland  
Vaud-Valais  
Zurich

### **Delegates**

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Urs Schönholzer  
Jean-Marc Falter  
Fabio Bossi  
Martin Wyss  
Daniel Hanimann  
Aline Chabloz  
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## SUMMARY

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Discussions conducted with managers and entrepreneurs in the second quarter were still shaped to a large degree by the effects of the discontinuation of the minimum exchange rate against the euro on 15 January. According to this survey, which does not factor in the public sector, economic growth – measured by real turnover – was unchanged in the quarter under review. However, turnover sank further in nominal terms because of movements in sales prices. Margins are therefore very strained for many companies, causing firms to implement a wide range of countermeasures (cf. the exchange rate survey on pp. 34 et seq.).

Following a sharp correction in the previous quarter, the outlook for real turnover growth in the coming months has improved marginally. Despite this, conditions remain very uncertain. Headcounts and the investment volume will remain at the current level.

## BUSINESS ACTIVITY

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### Ongoing stagnation

Overall, real turnover in the manufacturing industry was unchanged against one quarter earlier. This was already the case in the previous period under review. In nominal terms however, turnover was in many instances far lower than in the previous quarter because of major reductions in sales prices.

Moreover, there are marked differences between industry categories: The machinery industry and precision instrument manufacturers reported lower real turnover against the previous quarter. Plastics processing companies reported slightly higher real turnover, as did some companies in the chemical industry.

The US as well as the Asian and Arab regions are still among the export markets enjoying high momentum. Demand in Europe remains stable overall, with sporadic signs of improvement. The automobile industry remains a major contributor. Some sectors are registering a noticeable slowdown in business activity with Russia.

The construction industry reported stable to slightly higher turnover than in the previous quarter in seasonally adjusted terms. In the finishing trade, momentum is high. Activity appears to have slowed further in residential construction, at least locally.

Real turnover is slightly higher than in the previous quarter in the services sector. Consequently, there has been a slight improvement overall since the previous quarter, when services stagnated. However, the picture is very mixed: the catering, car dealing, retail and transport industries reported higher turnover than in the previous quarter, with some segments affected positively by higher import volumes. The hotel industry and recruitment firms reported noticeably lower turnover.

Although retail saw a marginal improvement overall, the topic of cross-border shopping was frequently raised; in particular, shopping centres close to the border report that they are empty at the weekend. In the hotel industry, continued high demand from Asian tour groups and guests from the Middle East has helped to cushion the negative effects of the strong Swiss franc.

## **CAPACITY UTILISATION**

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The companies surveyed rated production capacity as marginally underutilised overall.

Around 30% of responding companies in the manufacturing industry reported an underutilisation of capacity. There are marked differences between categories here too. Capacity utilisation was assessed as significantly lower than normal by producers of electrical equipment and precision instruments as well as in the food industry. By contrast, in the machinery and plastics industries, capacity utilisation is higher than usual thanks to the backlog of orders and additional sales efforts.

In the construction industry, utilisation of technical capacity was still reported as slightly higher than normal overall. However, signs of a slowdown were identified by a number of respondents. In this regard, the effects of the vote to curb second-home ownership are often cited.

In the services sector, most sectors reported a slight to significant underutilisation of infrastructure (i.e. primarily office and retail space as well as transport capacity). Car dealers are an exception, reporting slightly higher than usual infrastructure utilisation thanks to orders from the first quarter and increased demand for services.

## **DEMAND FOR LABOUR**

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### **Demand for staff hardly changed**

The discontinuation of the minimum exchange rate against the euro triggered numerous staffing policy measures, including hiring freezes, longer working hours for the same pay, and pay freezes – in some cases even after increases had already been decided on (cf. information in exchange rate survey below). Some companies are planning to reduce headcounts, with the focus remaining primarily on temporary staff.

Overall, staff numbers are currently rated as appropriate. In manufacturing, producers of electrical appliances reported that staff numbers are too high. In construction, staff numbers are slightly too low. Within the services sector, respondents in the hotel industry and some engineering firms and architectural practices reported that headcounts are slightly too high. By comparison, IT companies are still looking for more staff.

In all three categories, the lack of specialists has become somewhat less acute. Many companies continued to report that the level of spontaneous job applications was still high to very high, particularly in Ticino and French-speaking Switzerland.

## **PRICES, MARGINS AND EARNINGS SITUATION**

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### **Margins still under serious pressure**

In all three main industry categories, margins overall were reported as being under serious pressure, as in the previous quarter. The discontinuation of the minimum exchange rate has triggered strong pressure on prices. Many companies have rapidly lowered prices to counter the risk of losing customers. Pressure on prices is also being passed on to domestic suppliers in order to reduce costs.

A total of 55% of the respondent companies assessed their margins as being lower than usual, half of them as significantly lower. A further 30% of companies reported that margins were within the normal range. Several measures are currently being implemented to counter the tougher competitive situation (cf. results of the exchange rate survey below).

In all branches of the manufacturing industry, profit margins were judged to be lower or even significantly lower than usual. In the construction industry, the companies surveyed reported margins to be narrower than usual.

Companies in the services sector also rated margins as lower than usual overall. Trade, the transport industry, the finance industry and recruitment firms had to contend with particularly low margins. In the banking sector, a high volume of foreign exchange and securities trading dampened this effect.

## OUTLOOK

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### **Marginally more favourable outlook**

Uncertainty about the future development of the economy remains high because of the exchange rate situation. Nevertheless, real turnover is expected to increase marginally over the coming months, whereas in the previous quarter stagnation was still expected.

There are, however, considerable differences from one industry or segment to another; the construction industry is quite sceptical. Respondents in the services sector are the most confident. Many respondents continue to assess the situation in the light of the more volatile exchange rate situation.

In all industry categories, significant reductions in purchase and sales prices are still expected. Where feasible, however, companies are not reducing their sales prices by as much as the drop in purchase prices, in order to improve their margins again, at least to a certain extent.

While the survey participants in the manufacturing industry anticipate further slight staff reductions, respondents from the services sector and construction expect headcounts to remain unchanged. The sectors reporting the highest demand for staff are the pharmaceutical industry, wholesalers and telecommunications.

Many companies imposed an immediate freeze on investment following the discontinuation of the minimum exchange rate and are now thoroughly reviewing their capital expenditure. Overall, investment plans are still cautious, although slightly less so than in the previous quarter. The primary aim of investment planned within Switzerland is to increase efficiency or to meet replacement needs.

Respondents' inflation expectations – measured by the consumer price index – are still within negative territory, at –0.6% over the short term (6–12 months), compared to around –1.3% in the last survey. Expectations over the longer-term horizon of 3–5 years remain unchanged at 0.5%.

Respondents' main concern is still the tight margin situation and, linked to this, future movements in the exchange rate. Some of the discussions revealed fears that further effects from the strength of the Swiss franc may only be felt in the economy over the coming months. One of the reasons for this is that order books are rather less well filled. The uncertainty is also a result of the Greek debt situation and other existing geopolitical risks. With regard to the domestic market, criticism was levelled at both unfavourable economic conditions – which could, for example, arise as a result of the implementation of the mass immigration initiative – and increasing regulation.

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