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 2016

Second quarter of 2016

The Swiss National Bank's delegates for regional economic relations are constantly in touch with companies from different areas of the economy. This report is based on discussions conducted from the beginning of April to the end of May 2016 with 240 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 composition of GDP (excluding agriculture and public services).

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SUMMARY

According to this survey, the Swiss economy recorded slightly higher growth than in the previous quarter. Real turnover at the companies surveyed was up compared to the first quarter of 2016 and increased noticeably year-on-year, although differences from one segment to another remain. The margin situation has eased somewhat at numerous companies, but is still challenging. Production capacity overall remains underutilised.

Companies have expressed confidence that real turnover will continue to develop positively in the coming months, and a further upturn in foreign demand is expected. Moreover, margins are likely to continue to improve, due to enhanced efficiency and cost-cutting measures. The exchange rate situation also contributes to this more favourable assessment.

Staff numbers in the services sector are likely to increase somewhat in the next few months, whereas those in manufacturing will probably again decrease slightly. Willingness to invest is marginally up compared to previous quarters.

BUSINESS ACTIVITY

Overall turnover slightly on the rise

Real turnover in manufacturing remained unchanged at the level of the previous quarter, but was noticeably higher than one year ago. Only the pharmaceutical industry registered an increase in real turnover in the quarter under review. In all other lines of manufacturing, business was flat. The marked weakness in demand recorded by watchmaking companies is having knock-on effects in several other industries as well.

As to export business, sales to North America, northern Europe and Germany remain fairly dynamic. Demand from the automotive industry continues to be particularly high. The improvement in economic activity in Italy is having a positive impact, and there are some instances of increased demand from Japan. By contrast, many industries are feeling the effects of the unfavourable economic situation in Russia and Brazil, as well as the slowdown in China and the Middle East.

Business in construction has accelerated, particularly in structural and civil engineering. Turnover in the finishing trade remained at the level of the preceding quarter.

In the services sector, real turnover rose slightly compared to the previous quarter. Several services showed a similar development, notably the hospitality industry, specialised asset management, engineering and architecture firms as well as facility management services. Retailing continued to present a heterogeneous picture, albeit with a slightly upward trend overall. Cross-border shopping and the shift to online shopping, which continues to experience strong growth, present a significant challenge to a large number of companies.

CAPACITY UTILISATION

Ongoing underutilisation

Overall, the companies surveyed stated that production capacity remains underutilised. 35% of the survey respondents rated their utilisation as lower than usual.

Around half the responding companies in manufacturing reported a slight to significant underutilisation of capacity, with most lines being affected. Underutilisation is particularly marked in the mechanical and electrical engineering industries (MEM industries) and among firms producing precision instruments.

In construction, seasonally adjusted utilisation of technical capacity was somewhat higher than in the previous quarter, due to developments in the main lines of construction business. Lower-lying areas continue to notice the increased competitive pressure from mountain-region construction firms. The reason usually cited is a lack of projects in the mountain areas as a result of the vote to curb second-home ownership (‘Zweitwohnungsinitiative’).

The services sector presented a heterogeneous picture, albeit an improved one over the preceding quarter. Around half the segments reported underutilisation of infrastructure (office and retail space as well as IT and transport capacity), among them retailing, logistics, hotels and banks. By contrast, representatives of ICT (information and communication technology) and auditing companies described their utilisation rates as higher than usual.

Mountain hotels continue to report low utilisation, predominantly due to very low numbers of European guests, in particular from Germany, but also from Russia. Guests from Asia and the US are also showing reticence, owing to a fear of terrorist attacks in Europe on the one hand, and to new visa requirements in the Schengen Area on the other.

DEMAND FOR LABOUR

Staff numbers still slightly too high

Overall, staff numbers tend to be seen as marginally too high. However, the situation differs from one sector to another.

Most representatives of manufacturing firms continue to rate their staff numbers as slightly too high. This applies in particular to precision instrument and machine manufacturers. In construction, headcounts are, to a large extent, considered appropriate. Regarding the services sector, respondents from banks and retailing indicate that headcounts are somewhat too high. In contrast, ICT, fiduciary and auditing companies and specialised asset managers are recruiting more staff.

Some of the companies that introduced longer working hours in reaction to the appreciation of the Swiss franc have since reversed this measure, whereas others have retained it. Given their industry's weakness, a few watchmaking companies are considering the introduction of short-time working.

Overall, respondents find staff recruitment somewhat easier than before. Representatives from several industries ascribe this to a higher number of job seekers from the banking and watchmaking industries. The hitherto frequently cited shortage of engineers has eased, especially in the MEM industries. Numerous companies are receiving a comparatively high number of spontaneous job applications. On average, the quality of such applications is considered better than in the past.

PRICES, MARGINS AND EARNINGS SITUATION

Margin pressure eased slightly

The pressure on margins has eased slightly overall, but margins remain below what is considered as normal levels. Almost half the companies surveyed rated their margins as lower than usual. Measures taken to reduce costs and raise efficiency are proving to be effective. In certain cases, prices can be increased, especially abroad. In the domestic market, it has been possible to reduce some of the discounts granted.

Considerable margin pressure still prevails in manufacturing, where respondents from nearly all industries considered their margins to be lower or even significantly lower than usual. However, a slight improvement against the previous quarter has been recorded in this sector, too.

In the services sector, margins remain under significant pressure in retailing as well as in the hospitality and financial industries. By contrast, margins are considered to be at a normal level in the case of wholesalers, auditors and the ICT industry.

Expectations regarding price developments point to a continuing downward trend for purchase and sale prices. A number of respondents, however, anticipate a further rise in commodity prices.

Certain information relating to the real estate market indicates a slight reduction in prices for residential property in the top market segment and a shift in demand towards cheaper segments. In the case of commercial property, there are ongoing signs that rents are, in some cases, under a lot of pressure. This applies in particular to property in prime locations, where tenants are aiming to renegotiate their contracts.

OUTLOOK

Optimism reiterated

Respondents from all three sectors expect a slight rise in real turnover and margins over the coming months. This optimism is in line with the assessment of the past quarter. Reasons behind it include the current exchange rate conditions, anticipated economic developments abroad and the impact of the measures taken to raise efficiency and innovation. This constellation is expected to lead to further improvement in the margins.

Predictability of business performance is deemed to be comparatively low, which is why the outlook for the near future remains characterised by caution. In the present environment, companies from various industries expect a stabilisation of capacity utilisation overall at the current level. Investment plans for the coming 12 months point to a slight upturn. This trend has now persisted for a few quarters.

As to employment plans, survey respondents in the services sector anticipate a marginal increase, whereas those in manufacturing and construction by and large expect slight staff reductions. Hardly anything has changed in this respect compared to the previous quarter.

Companies' inflation expectations (as measured by the consumer price index) average –0.2% over the short term of 6–12 months (previous quarter: –0.3%). Expectations over the longer-term horizon of 3–5 years are 0.5% (previous quarter: 0.7%).

Concerns expressed by respondents include the Brexit scenario (the UK voting to leave the EU), economic and political instability in certain emerging economies, accelerated structural transformation in Switzerland, increasing regulatory requirements and potentially negative consequences of the implementation of the initiative against mass immigration. While most companies have found a way of coping with the current exchange rate conditions, the situation remains challenging for others, and their representatives have expressed the hope that the Swiss franc does not appreciate again. The current interest rate environment continues to be viewed critically with regard to the long-term outlook for pension funds.

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