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Press release

Monetary policy assessment of 17 March 2005

National Bank leaves the target range for the three-month Libor rate unchanged at 0.25–1.25%.

The Swiss National Bank leaves the target range for the three-month Libor rate unchanged at 0.25–1.25%. It intends to keep the rate in the middle of the target range at around 0.75% for the time being.

Switzerland’s economy has lost more momentum than expected. The sluggish economic environment in Europe, in particular, has had a dampening effect. The National Bank anticipates economic growth of around 1.5% in 2005, and thus a continuation of the moderate economic recovery. It expects inflation to recede slightly during the year under review. The annual inflation rate should average 1%. On the assumption that the three-month Libor will remain unchanged at 0.75%, annual inflation is expected to stand at 1% in 2006 and reach 2.1% in 2007. Compared with the December assessment, the inflation prospects have improved slightly. An interest rate hike is therefore currently not appropriate. The National Bank’s monetary policy has an expansionary effect and continues to underpin the recovery. Should unexpected developments push up the Swiss franc, the National Bank will take appropriate action.

International environment

The SNB’s inflation forecast is based on a global economic scenario. At the time of the forecast, this scenario is considered to represent the most likely development. The current scenario has been modified slightly compared with that of December 2004: in the US, the economy is performing as projected. In the EU, however, the growth rate in the third and fourth quarters of 2004 was lower than anticipated. Compared with the December expectations, the recovery this year is likely to be delayed somewhat.

Oil price

The price of oil has risen again. The National Bank bases its current inflation forecast on the assumption that oil prices will persist at a high level. The oil-price-induced increase in the price level in 2004 will, however, push down this year’s inflation, which is measured in terms of annual growth rates.

Economic outlook

The development of prices in the middle of the three-year forecasting horizon is primarily determined by economic performance. For 2005, the National Bank anticipates real GDP growth of around 1.5%. The moderate economic recovery thus continues and will be driven by the export sector and equipment investment. Following the perceptible slowdown in the course of 2004, private consumption is also expected to pick up speed. As the economy is likely to recover at a measured pace overall, economic resources are not expected to be fully utilised before the second half of 2006. If monetary policy were to remain unchanged until then, inflation rates would rise subsequently.

Monetary development

Recently, the monetary aggregates have either contracted (M1 and M2) or expanded only modestly (M3). Mortgage loans, by contrast, have continued to increase at a rather rapid pace. Well aware that its monetary policy is still expansionary, the National Bank is keeping a close eye on the developments in the real estate sector.

Inflation outlook

Given the current inflation outlook, it can be assumed that price stability is guaranteed for the next two years. If the economy recovers as expected and the interest rate level is not appropriately raised in the future, price stability will be jeopardised as of 2007.

Reasons behind the monetary policy decision

In view of the above-mentioned developments, the Swiss National Bank has decided to leave the target range for the three-month Libor rate unchanged at 0.25–1.25%. Its decision is based on two main reasons. First, the inflation prospects have improved slightly since the last assessment, indicating that the scope for monetary policy action has broadened. Second, the National Bank has made a slight downward adjustment to its assessment of the economy. The GDP growth rate for 2005 was revised downwards from 1.5–2% in December to around 1.5%. At the same time, some risks have had to be weighted more heavily than in the December assessment. In particular, the higher oil prices could slow the global economy more than anticipated. Another risk is that the European economy might perform below expectations.

Inflation forecast with Libor at 0.75%

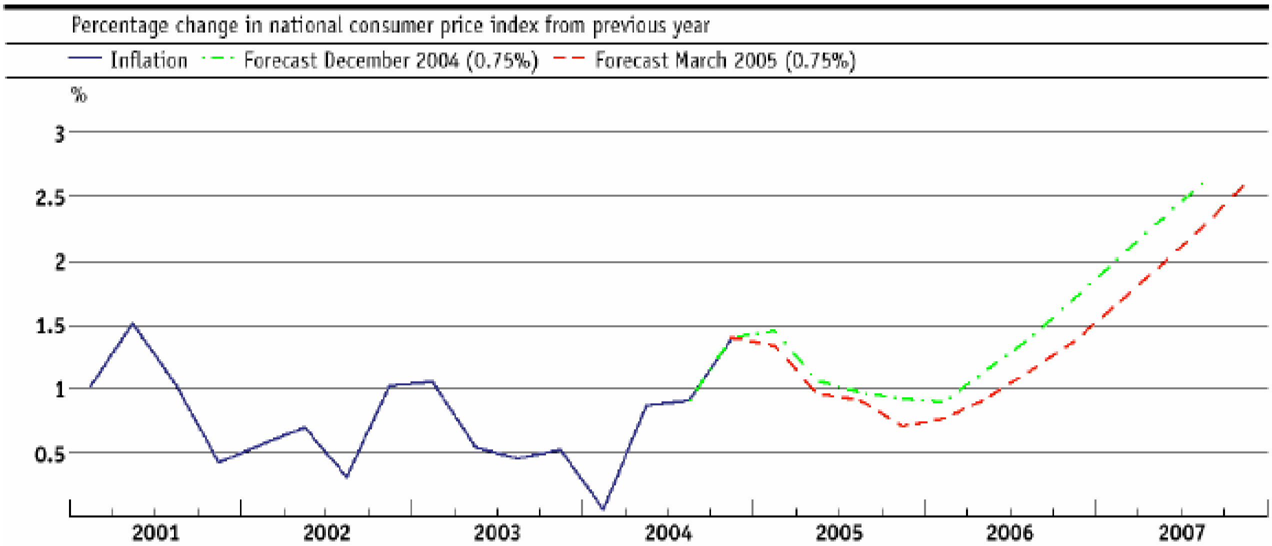
The new inflation forecast (dashed red line), which – as in the previous period – is based on the assumption of an unchanged three-month Libor of 0.75%, extends from the first quarter of 2005 to the fourth quarter of 2007. The dash-dotted green line shows the inflation forecast of December 2004. The inflation rate of 1.4% realised in the fourth quarter of 2004 corresponded to the figure predicted in December.

The new forecast is lower than the previous one across the entire forecasting horizon and reaches a low point of 0.7% in the fourth quarter of 2005. As in the December forecast, the decline in inflation in 2005 is largely due to a base effect. With the expansionary monetary policy remaining unchanged, the high degree of utilisation of economic resources triggers an increase in inflation towards the end of 2006. If the three-month Libor were to remain steady at 0.75%, inflation would hit 2.6% at the end of the forecasting horizon, thus exceeding the range that the National Bank equates with price stability. The forecast thus makes it clear that the current interest rate level cannot be sustained and that the National Bank will have to raise interest rates when the output gap narrows. Owing to data adjustments, the new forecast is slightly lower overall than the December projection.

Continuation of expansionary monetary policy

With its decision to leave the three-month Libor unchanged, the National Bank is adhering to its current monetary policy course and is making use of its monetary policy leeway to support the recovery of the economy without jeopardising long-term price stability. Should the economic recovery be delayed due to unforeseen events, or should the Swiss franc appreciate rapidly, the National Bank will take appropriate action. As in the past, it shall keep all its options open.

Inflation forecast of December 2004 with Libor at 0.75% and of March 2005 with Libor at 0.75%



Observed inflation March 2005

	2001				2002				2003				2004			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Inflation	1.02	1.50	1.03	0.41	0.56	0.69	0.31	1.01	1.05	0.54	0.45	0.52	0.06	0.87	0.91	1.38

Inflation forecast of December 2004 with Libor at 0.75% and of March 2005 with Libor at 0.75%

	2004				2005				2006				2007			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Forecast December 2004, Libor at 0.75%				1.40	1.45	1.06	0.97	0.92	0.90	1.15	1.40	1.70	2.00	2.30	2.60	
Forecast March 2005, Libor at 0.75%					1.33	0.96	0.91	0.70	0.76	0.93	1.14	1.36	1.65	1.94	2.25	2.60

Inflation forecast of March 2005

Swiss National Bank