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Overview

Monetary policy assessment (p. 8)

At its assessment of 20 March 2003, the National Bank decided to leave the target range for the three-month Libor rate unchanged at 0%–0.75%, after having lowered it by half a percentage point on 6 March. By loosening the monetary reins, the National Bank wished to ward off a tightening of monetary conditions that would arise from an appreciation of the Swiss franc. At the present time, this expansionary monetary policy does not pose any risk to price stability in Switzerland. Assuming that the three-month Libor rate will remain stable at 0.25%, average annual inflation is expected to lie between 0.7% and 1.9% in the next three years, with the inflation forecast for the second half of 2005 pointing to a rise to over 2%. The National Bank believes that it will have sufficient time to make adjustments to its monetary policy, and that it can keep inflation within the price stability range.

Economic and monetary developments (p. 12)

International economic activity has been shaped in recent months by the tensions surrounding Iraq. The uncertainty has been reflected in a depreciating dollar, rising oil prices, and declining equity markets. In the USA and Europe, economic growth slackened further towards the end of 2002. Sentiment remained flat among manufacturers and consumers in most industrialised countries at the beginning of 2003.

At 1.4%, the rise of real gross domestic product in Switzerland in the fourth quarter of 2002 was slower than in the previous period. This is a year-on-year increase of 0.8%. The economic situation remained fragile until the end of the year. Private consumption showed little growth, and investment continued to fall. By contrast, exports – driven by rising demand from Asia – made a positive contribution to growth. Together with the continuing decline in imports, foreign trade made a positive contribution to growth. There were no signs of an economic rebound at the beginning of 2003. Industrial activity remained weak, and prospects were judged more pessimistically than in the fourth quarter. The situation on the labour market continued to deteriorate. Employment was down in the fourth quarter, and both the unemployment rate and the number of job-seekers climbed to 3.5% and 5.1% respectively by the end of February.

Short- and long-term interest rates continued their downward slide until February. In February, the yield on a 10-year Confederation bond was 2.3%, or 0.4 percentage points lower than in November. Coupled with the low short-term interest rates and the vigorous growth of monetary aggregates and mortgage lending, this development suggested expansionary monetary conditions.

The role of the National Bank in cashless payments (p. 44)

A stable financial system is a key prerequisite for the smooth functioning of an economy. The two main elements of a stable financial system are a healthy financial sector and a secure and efficient financial market infrastructure comprising stock exchanges and clearing and settlement systems for payments, securities and other financial instruments. Smooth functioning of cashless payments is of primary importance to the SNB because it needs these systems for the day-to-day implementation of its monetary policy. It uses market-oriented policies to achieve its objective of ensuring a secure and efficient payments infrastructure. The actual operation of payment systems is normally left to the private sector. The National Bank facilitates the flow of funds between financial intermediaries through providing sight deposit accounts and thus makes a major contribution to the stability of the financial system. At the same time, it is responsible for overseeing payment systems that could pose systemic risks because of the volume or type of payments handled. It defines its role in overseeing these systems as all of its efforts to influence the rules and architecture of payment systems. The Swiss National Bank welcomes the fact that the growing importance of this role is reflected in the draft version of the revised National Bank Law, which explicitly defines the overseeing of payment and securities clearing systems as one of its key functions.

Geldpolitische Lagebeurteilung (S. 8)

Die Nationalbank beschloss an der Lagebeurteilung vom 20. März 2003, das Zielband für den Dreimonats-Libor bei 0%–0,75% zu belassen, nachdem sie dieses am 6. März um einen halben Prozentpunkt gesenkt hatte. Mit der Lockerung der Geldpolitik wollte die Nationalbank einer Verschärfung des monetären Umfelds über eine Aufwertung des Franken entgegenreten. Die expansive Geldpolitik stellt derzeit keine Gefährdung der Preisstabilität in der Schweiz dar. In den nächsten drei Jahren dürfte die durchschnittliche Jahresteuern bei einem konstanten Dreimonats-Libor von 0,25% zwischen 0,7% und 1,9% liegen, wobei die Inflationsprognose für die zweite Hälfte des Jahres 2005 einen Anstieg auf über 2% anzeigt. Die Nationalbank ist der Ansicht, dass ihr genügend Zeit für eine Korrektur der Geldpolitik bleiben wird und sie die Teuerung im Bereich der Preisstabilität halten kann.

Wirtschafts- und Währungslage (S. 12)

Die internationale Konjunktur war in den letzten Monaten von den Spannungen um den Irak geprägt. Die Unsicherheit widerspiegelte sich in einem sinkenden Dollarkurs, in steigenden Erdölpreisen und in fallenden Aktienkursen. In den USA und in Europa schwächte sich das Wirtschaftswachstum gegen Ende 2002 weiter ab. Anfang 2003 blieb die Stimmung bei Produzenten und Konsumenten in den meisten Industrieländern gedrückt.

In der Schweiz stieg das reale Bruttoinlandsprodukt im vierten Quartal 2002 mit 1,4% etwas langsamer als in der Vorperiode. Im Vorjahresvergleich erhöhte es sich um 0,8%. Die konjunkturelle Lage blieb bis zum Jahresende fragil. Der private Konsum wuchs nur wenig und die Investitionen sanken weiter. Positive Impulse gingen dagegen von den Exporten aus, die von der anziehenden Nachfrage aus Asien profitierten. Zusammen mit den weiter rückläufigen Importen trug damit der Aussenhandel positiv zum Wirtschaftswachstum bei. Anfang 2003 zeichnete sich keine konjunkturelle Besserung ab. Die Industriekonjunktur blieb schwach und die Aussichten wurden pessimistischer beurteilt als im vierten Quartal. Die Lage am Arbeitsmarkt verschlechterte sich weiter. Die Beschäftigung nahm im vierten Quartal ab und die Arbeitslosenquote sowie die Quote der Stellensuchenden stieg bis Februar auf 3,5% bzw. 5,1%.

Die kurz- und langfristigen Zinssätze bildeten sich bis Februar weiter zurück. Im Februar betrug die Rendite einer zehnjährigen eidgenössischen Anleihe 2,3% und lag damit 0,4 Prozentpunkte tiefer als im November. Zusammen mit den tiefen kurzfristigen Zinssätzen sowie den kräftig wachsenden Geldaggregaten und Hypothekarkrediten deutete dies auf ein expansives monetäres Umfeld hin.

Die Rolle der Nationalbank im bargeldlosen Zahlungsverkehr (S. 44)

Ein stabiles Finanzsystem ist eine wichtige Voraussetzung für die wirtschaftliche Leistungsfähigkeit einer Volkswirtschaft. Die zwei bedeutendsten Elemente eines stabilen Finanzsystems sind ein gesunder Finanzsektor und eine sichere und effiziente Finanzmarktinfrastruktur, bestehend aus Börsen sowie Clearing- und Abwicklungssystemen für Zahlungen, Wertschriften und andere Finanzinstrumente. Vor allem die reibungslose Funktionsweise der bargeldlosen Zahlungssysteme ist für die Nationalbank ein wichtiges Anliegen, da sie bei der täglichen Umsetzung der Geldpolitik auf diese Systeme angewiesen ist. Die Nationalbank verfolgt ihr Ziel einer sicheren und effizienten Zahlungsverkehrsinfrastruktur mittels einer marktwirtschaftlich orientierten Politik und überlässt den Betrieb der Zahlungssysteme in der Regel dem Privatsektor. Indem die Nationalbank Girokonten zur Verfügung stellt, erleichtert sie die Abwicklung des Zahlungsverkehrs zwischen den Finanzintermediären und leistet damit einen wichtigen Beitrag zur Stabilität des Finanzsystems. Zudem überwacht die Nationalbank diejenigen Zahlungssysteme, von denen aufgrund der Höhe des Umsatzes oder der Art der Zahlungen systemische Risiken ausgehen können. Unter der Überwachung versteht die Nationalbank alle ihre Bestrebungen, die Regeln und die Architektur eines Zahlungssystems zu beeinflussen. Die Nationalbank begrüsst es, dass die wachsende Bedeutung dieser Notenbankaufgabe auch im Entwurf des neuen Nationalbankgesetzes zum Ausdruck kommt, indem die Überwachung von Zahlungs- und Effektenabwicklungssystemen ausdrücklich als eine ihrer Hauptaufgaben aufgeführt ist.

Appréciation de la situation économique et monétaire (p. 8)

Le 20 mars 2003, lors de son analyse trimestrielle de la situation, la Banque nationale a décidé de maintenir à 0%–0,75% la marge de fluctuation du Libor à trois mois. Elle l'avait abaissée d'un demi-point le 6 mars. En assouplissant sa politique monétaire, l'institut d'émission a voulu contrer un durcissement, dû à une revalorisation du franc, des conditions monétaires. La politique monétaire expansionniste ne met pour le moment pas en jeu la stabilité des prix en Suisse. Avec un Libor à trois mois inchangé à 0,25%, le renchérissement annuel moyen devrait s'inscrire entre 0,7% et 1,9% ces trois prochaines années; selon la prévision faite en mars, il passera au-dessus de 2% au second semestre de 2005. La Banque nationale estime disposer de suffisamment de temps pour procéder à une correction de sa politique monétaire et pouvoir maintenir le renchérissement dans la zone de la stabilité des prix.

Situation économique et monétaire (p. 12)

Ces derniers mois, les tensions en rapport avec l'Irak ont influé sur la conjoncture internationale. Les incertitudes ont pesé sur le cours du dollar et sur les marchés des actions, mais ont aussi poussé à la hausse les prix des produits pétroliers. La croissance économique a continué à faiblir, vers la fin de 2002, aux Etats-Unis et en Europe. Tant du côté des producteurs que de celui des consommateurs, le climat est resté morose, au début de 2003, dans la plupart des pays industrialisés.

En Suisse, le produit intérieur brut réel a augmenté de 1,4% au quatrième trimestre, soit à un rythme inférieur à ce qui avait été enregistré au trimestre précédent. En comparaison annuelle, la croissance a été de 0,8%. La conjoncture est restée fragile jusqu'à la fin de l'année. La consommation privée n'a progressé que légèrement, et les investissements ont encore reculé. En revanche, des impulsions positives sont venues des exportations qui ont bénéficié de la demande plus ferme de pays asiatiques. Comme les importations ont de surcroît diminué, le commerce extérieur a fourni une sensible contribution à la croissance économique. Aucune amélioration de la conjoncture n'était perceptible au début de 2003. L'activité dans le secteur industriel est restée faible, et les entrepreneurs ont porté sur les perspectives des jugements plus pessimistes qu'au quatrième trimestre. Sur le marché du travail, la situation s'est encore dégradée. L'emploi a diminué au quatrième trimestre. En outre, le taux de chômage et le taux de demandeurs d'emploi ont augmenté pour atteindre respectivement 3,5% et 5,1% en février.

Les taux d'intérêt à court et à long terme ont encore fléchi jusqu'en février. Le rendement des emprunts à dix ans de la Confédération s'établissait à 2,3% en février, soit à un niveau inférieur de 0,4 point à celui de novembre. Ce repli, le bas niveau des taux d'intérêt à court terme, mais aussi la vive expansion des agrégats monétaires et des créances hypothécaires sont autant de signes d'un environnement monétaire expansionniste.

Le rôle de la Banque nationale dans le trafic des paiements sans numéraire (p. 44)

Un système financier stable est une condition importante à l'efficacité d'une économie. La stabilité d'un système financier dépend essentiellement de deux facteurs: un secteur financier sain et une infrastructure du marché financier sûre et efficace. Celle-ci est constituée de bourses et de systèmes de compensation et de règlement des paiements et des opérations sur valeurs mobilières et autres instruments financiers. Le bon fonctionnement des systèmes de paiement sans numéraire est l'une des préoccupations principales de la Banque nationale qui recourt quotidiennement à ces systèmes pour la mise en œuvre de sa politique monétaire. Afin d'atteindre son objectif, soit une infrastructure sûre et efficace pour le trafic des paiements, la Banque nationale a choisi une politique axée sur des principes d'économie de marché et laisse en règle générale au secteur privé le soin de gérer les systèmes de paiement. En mettant à disposition des comptes de virements, l'institut d'émission facilite le déroulement du trafic des paiements entre les intermédiaires financiers et contribue ainsi dans une large mesure à la stabilité du système financier. En outre, il surveille les systèmes de paiement qui présentent des risques systémiques en raison de l'importance du volume des transactions ou de la nature des paiements passant par ces systèmes. Par surveillance, la Banque nationale entend l'ensemble de ses efforts qui tendent à influencer les règles et l'architecture d'un système de paiement. Elle salue le fait que l'importance croissante de cette tâche des banques centrales ait été prise en compte dans le projet de révision totale de la loi qui la régit. La surveillance des systèmes de paiement et de règlement des opérations sur titres y figure en effet expressément comme l'une de ses tâches principales.

Valutazione della situazione monetaria (p. 8)

In occasione della valutazione della situazione economica del 20 marzo 2003, la Banca nazionale ha deciso di mantenere il margine di oscillazione del Libor a tre mesi allo 0-0,75%, livello raggiunto con la riduzione di mezzo punto percentuale decretata il 6 marzo. Con quest'ultimo intervento di politica monetaria la Banca nazionale si è opposta all'inasprimento delle condizioni monetarie derivante dall'apprezzamento del franco. La politica monetaria espansiva attualmente seguita non minaccia la stabilità dei prezzi in Svizzera. Nell'ipotesi di un Libor a tre mesi costante dello 0,25%, il tasso d'inflazione medio annuale dovrebbe situarsi, nel corso del prossimo triennio, tra lo 0,7% e l'1,9%. Per la seconda metà del 2005, la previsione d'inflazione indica tuttavia un superamento della soglia del 2%. La Banca nazionale ritiene di disporre di sufficiente tempo per modificare il corso della politica monetaria e che le sarà perciò possibile mantenere il rincaro ad un livello compatibile con la stabilità dei prezzi.

Situazione economica e monetaria (p. 12)

In questi ultimi mesi, la congiuntura internazionale è stata dominata dalle tensioni con l'Iraq. L'incertezza si è riflessa in un deprezzamento del dollaro, un aumento dei prezzi del petrolio e un calo dei corsi azionari. La crescita economica negli Stati Uniti e in Europa è ulteriormente rallentata verso la fine del 2002. All'inizio del 2003, la fiducia di produttori e consumatori nella maggior parte dei Paesi industrializzati è rimasta debole.

In Svizzera la crescita del prodotto interno lordo reale nel quarto trimestre del 2002, pari all'1,4%, è risultata leggermente inferiore al periodo precedente. Rispetto all'anno precedente è stato registrato un aumento dello 0,8%. La situazione congiunturale è rimasta fragile sino alla fine dell'anno, con una crescita dei consumi privati debole e un ulteriore calo degli investimenti. Impulsi positivi sono invece provenuti dalle esportazioni che hanno beneficiato di una ripresa della domanda nei Paesi asiatici. In concomitanza con un'ulteriore contrazione delle importazioni, il commercio estero ha perciò contribuito positivamente alla crescita economica. Gli indicatori disponibili non rilevano all'inizio del 2003 un miglioramento della situazione congiunturale. Nel settore industriale, la congiuntura è rimasta debole, e le prospettive sono state giudicate con maggiore pessimismo rispetto alla fine del 2002. La situazione sul mercato del lavoro ha continuato a deteriorarsi. Nel quarto trimestre del 2002, l'occupazione si è ridotta. Entro febbraio, il tasso di disoccupazione è salito al 3,5%, la quota delle persone in cerca d'impiego al 5,1%.

I tassi d'interesse a breve e lungo termine sono ulteriormente calati. Da novembre a febbraio, il rendimento dei prestiti svizzeri con una durata di dieci anni è sceso dal 2,7% al 2,3%. Unitamente a bassi tassi d'interesse a breve e a una vigorosa espansione degli aggregati monetari e dei crediti ipotecari, ne risulta un quadro monetario espansivo.

Il ruolo della Banca nazionale per i pagamenti senza contanti (p. 44)

Un sistema finanziario stabile è un presupposto importante per l'efficienza dell'economia nazionale. I due elementi principali di un sistema finanziario stabile sono un settore finanziario solido e un mercato finanziario dotato di un'infrastruttura sicura ed efficace, composta di borse e di sistemi di clearing e di regolamento di pagamenti, di titoli e altri strumenti finanziari. La Banca nazionale accorda particolare rilievo al buon funzionamento dei sistemi di pagamento senza contanti, ai quali deve fare affidamento ogni giorno per l'attuazione della politica monetaria. Allo scopo di garantire la sicurezza e l'efficienza dell'infrastruttura disponibile per le operazioni di pagamento, essa segue una politica basata sui principi di economia di mercato e affida di regola l'esercizio dei sistemi di pagamento al settore privato. I conti giro messi a disposizione dalla Banca nazionale facilitano il regolamento dei pagamenti tra intermediari finanziari e contribuiscono in modo importante alla stabilità del sistema finanziario. L'istituto d'emissione sorveglia inoltre i sistemi di pagamento dai quali potrebbero derivare – per il volume degli importi trattati o per il genere dei pagamenti effettuati – rischi sistemici. Per sorveglianza s'intendono tutte le misure adottate dalla Banca nazionale atte ad influire sulla regolamentazione e sull'architettura di un sistema di pagamento. Il progetto per una nuova legge sulla Banca nazionale riconosce la crescente importanza di quest'attività annoverando espressamente, tra le mansioni dell'istituto d'emissione, la sorveglianza dei sistemi di gestione dei pagamenti e delle operazioni su titoli.

Press release on the quarterly assessment of the situation of 20 March 2003

The National Bank has not made any further change to its monetary policy in its assessment of 20 March 2003. It cut the target range for the three-month Libor by 0.5 percentage points to 0%–0.75% on 6 March 2003 and announced that the rate is to be kept in the lower part of the new target range, i. e. at 0.25%, for the time being. The temporary narrowing of the target band from 100 to 75 basis points was prompted by technical factors.

After the outbreak of the Iraq conflict, the economic and political environment remains extremely uncertain. The economic recovery in Switzerland expected for 2003 may be delayed. Given this difficult situation, the National Bank wishes decisively to counter the tightening of monetary conditions that would arise from an appreciation of the Swiss franc. Low inflation has meant that the National Bank has been able to relax its monetary policy significantly over the last two years. Since March 2001, it has cut the target band for the three-month Libor rate in a total of seven stages by 3.25 percentage points to its current level. At the present time, this expansive monetary policy does not pose any risk to price stability in Switzerland. Assuming that the three-month Libor rate will remain stable at 0.25%, average annual inflation is expected to lie between 0.7% and 1.9% in the next three years. The National Bank now anticipates that economic growth will be just under 1% for 2003.

Economic activity

Despite a difficult climate worldwide, economic activity in Switzerland stabilised somewhat during the second half of 2002. After falling between the third quarter of 2001 and the first quarter of 2002, real gross domestic product has since been edging up again on a quarter-on-quarter basis. Nonetheless, the fourth quarter of 2002 saw growth flatten off once more compared with the third quarter of the year. Exports and consumer spending were the main stabilising factors.

The economic situation in Switzerland remains tight, however, with growth staying below its potential level. The deterioration of the labour market is depressing consumer sentiment and disposable incomes. Incoming orders and the order backlog are still unsatisfactory, and there is insufficient capacity utilisation in the industrial and construction sectors. Capital spending remains in sharp decline.

There must be a sustainable recovery in exports and investment activity before Switzerland can return to higher real growth, and this cannot be expected until the global economy begins to pick up. The Swiss economy will thus expand only moderately up to mid-2003 and will not begin to accelerate somewhat until after this point. The National Bank anticipates that real gross national product will increase by just under 1% in 2003 as a whole.

Inflation and inflation forecast

Year-on-year inflation, as measured by the national consumer price index, rose to 1.0% in the fourth quarter of 2002 from 0.3% in the third quarter. In January and February 2003, it was 0.8% and 0.9% respectively. These fluctuations are due primarily to statistical effects. The core rate of inflation calculated by the National Bank (trimmed mean method), which is a reliable indicator of the inflation trend, has been around 1% for some time now.

At the end of 2002, the National Bank decided in future to publish its inflation forecast every quarter. This March forecast is the first of these. The graph shows both the inflation forecast of December 2002 (the dotted red curve) and the forecast of March 2003, drawn up after the latest interest rate cut (red dashed curve).

The National Bank's new inflation forecast is based on the assumption that growth in the US will pick up again from the second quarter of 2003 onward. The US economy is likely to grow more strongly in 2004 and again reach its potential output. In the EU, however, the recovery has been delayed, and growth rates of over 2% are not to be expected until 2004. Given the uncertain geopolitical situation, the price of oil is likely to fluctuate around USD 30 a barrel for some time yet, before coming back down to around USD 25 a barrel.

On the assumption that the three-month Libor rate will remain stable at 0.25% during the next three years, inflation should average 0.7% in 2003, moving up to 0.9% in 2004 and to 1.9% in 2005. Inflation is forecast to remain under 1% until mid-2004. Thereafter, it will accelerate, reaching 2.5% in the fourth quarter of 2005. This is above the level that the National Bank equates with price stability. It should be noted that these forecasts assume that monetary policy will remain expansive over the next three years.

Despite the most recent interest rate cut, the new forecast up to mid-2004 is virtually the same as that published at the end of last year. In the short term, inflation will be held back by the delayed economic recovery and the weakness of the US dollar. In the new forecast, however, inflation rises more markedly at the end of the forecasting horizon owing to the more expansionary monetary policy.

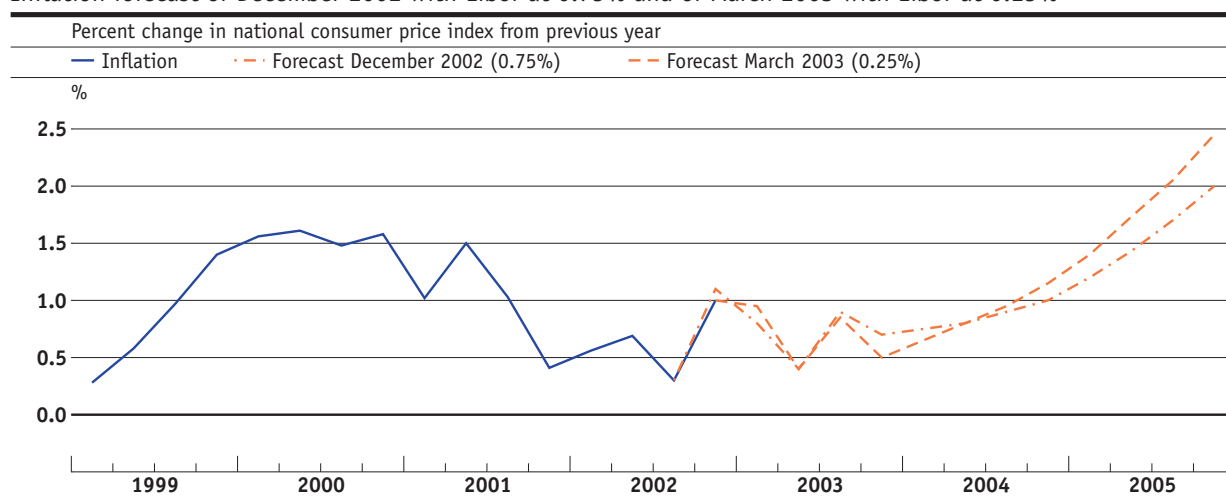
Expansionary monetary policy

With its latest interest rate cut, the National Bank relaxed its policy significantly again and responded once more to increasing uncertainty about economic trends. In this critical phase, the aim of the National Bank is to support economic recovery in Switzerland and keep the attractiveness of Swiss franc investments at a low level.

As the risks are still pointing mainly downward, the National Bank intends to maintain its expansionary monetary policy. Under the current circumstances, it will endeavour to take decisive steps to counter a tightening of monetary conditions through the appreciation of the Swiss franc. In spite of the fact that money market rates are already very low, the National Bank still has effective instruments at its disposal. In particular, these include intervention on the foreign exchange market.

At present, the National Bank's highly expansionary monetary policy – as reflected in extraordinarily low interest rates and strong growth in monetary aggregates – poses no threat to price stability. The latest forecast expects inflation to rise to over 2% in the second half of 2005, given a constant interest rate of 0.25%. The National Bank nonetheless believes that it still has sufficient time to make later adjustments to its monetary policy, and that it can keep inflation within the price stability range.

Inflation forecast of December 2002 with Libor at 0.75% and of March 2003 with Libor at 0.25%



Inflation forecast March 2002 with Libor at 0.25%	2002	2003	2004	2005
Annual average inflation in %	0.6	0.7	0.9	1.9

The main ticks on the horizontal axis indicate the beginning of the first quarter of the respective year.

**Swiss National Bank lowers the target range
for the three-month Libor rate
by 0.5 percentage points to 0%–0.75%**

With immediate effect, the Swiss National Bank is lowering its target range for the three-month Libor rate by 0.5 percentage points to 0%–0.75%. The temporary narrowing of the target range from 100 to 75 basis points brought about by this move is due to technical factors. For the time being, the National Bank intends to keep the three-month Libor rate at around 0.25%, i. e. at the lower end of the new target range.

The global economic and political uncertainties are persisting. This is adversely affecting the business climate in Switzerland and could delay the economic upturn that was expected to materialise in 2003. Given this difficult situation, the National Bank wishes to ward off a tightening of monetary conditions that would arise from an appreciation of the Swiss franc. The easing of monetary policy does not pose a threat to price stability in Switzerland.

As planned, the National Bank will present its detailed monetary policy assessment, including the inflation forecast, on Thursday, 20 March 2003.

Economic and monetary developments in Switzerland

Report for the attention of the Governing Board with a view to its quarterly assessment of the situation and to the attention of the Bank Council

The report was passed on 20 March 2003.

Data which became available at a later date has been included whenever possible. Unless indicated otherwise, quarter-on-quarter comparisons are always based on data adjusted for seasonal and random variations.

1 International environment

1.1 Economic activity

International economic activity has been dominated in recent months by the tensions surrounding Iraq. Uncertainty about the outbreak of war – and about the possible duration of such a war – has been reflected in the depreciation of the dollar, the rising price of oil and declining equity markets. In the US and Europe, economic growth slackened further towards the end of 2002, while fourth-quarter expansion in the Japanese economy was surprisingly strong on the back of lively demand from the rest of Asia. Sentiment remained gloomy among manufacturers and consumers in most industrialised countries at the beginning of 2003.

Faced with economic weakness and a favourable outlook for inflation, the US Federal Reserve maintained its relaxed monetary policy, and the European Central Bank cut its key interest rates again in early March. Low interest rates are sustaining expectations of a gradual economic recovery during the remainder of the year. Stimuli can also be expected from expansive fiscal policy in the United States and United Kingdom. However, persistent consumer uncertainty and changes in the price of oil pose a considerable threat to economic activity.

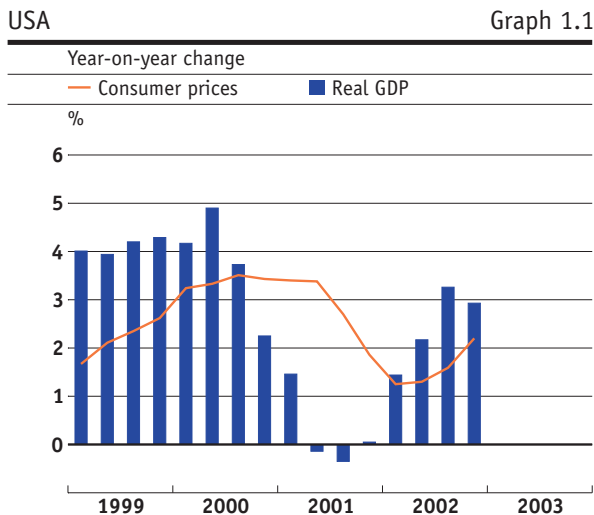
Weak growth in the US

In the United States, real GDP rose at an annualised rate of 1.4% in the fourth quarter compared with 4.0% in the previous period. This corresponds to rise of 2.9% year-on-year (Q3: 3.3% yoy). This slowdown in growth is the result of only a small increase in private consumer spending, combined with declining exports. By contrast, public spending and investment gathered momentum.

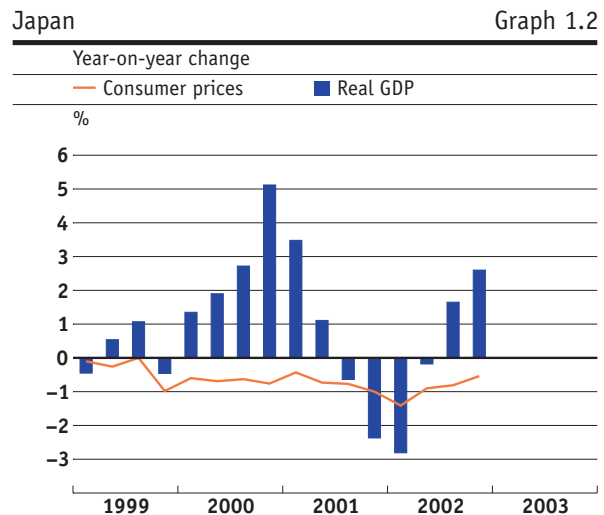
The first quarter is likely to have seen only a slight increase in gross domestic product once again. Consumers have been very unsettled, with sentiment slumping in January to its lowest point since 1993. Owing to sluggish economic activity in Europe and Japan, exports did not take off either, despite the cheaper dollar. Meanwhile, industrial orders were slack and output stagnated.

Stagnation in the EU

Economic growth in the euro area weakened towards the end of 2002. In the fourth quarter, real GDP edged up only very slightly, growing at an annualised 0.7%, compared with 1.6% in the third quarter. Economic activity was shored up by private and public spending, but investment continued to decline and exports stagnated. While Germany saw its real GDP contract just a little, growth in France and most of the euro area's smaller countries fell back more heavily. In Italy, however, it made modest advances.



Source: Bank for International Settlements (BIS)



Source: BIS

The economic slump continued in the first quarter. From 8.5% in November, the euro area's unemployment rate rose to 8.7% in February. In Germany, another 0.3 percentage points were added to the jobless figure, taking it to 8.7%. The latest surveys show that consumer confidence has dwindled significantly in the light of further deterioration on the labour market. The industrial sentiment indicator lost ground, even though new orders picked up slightly.

The United Kingdom's economy also lost momentum during the fourth quarter. Real GDP rose by an annualised 1.6% compared with the previous period, after growth of almost 4% for the third quarter. Recessionary trends in industry were accentuated, while growth slowed in the service sector in general and the financial sector in particular. Leading indicators point to restrained growth in the first quarter. The unemployment rate remained unchanged at 3.1%.

Uneven growth in Japan

Japan's real GDP advanced by an annualised 2.2% during the fourth quarter, having already made substantial gains in the previous period. The main driver was the buoyant export market, which benefited from lively demand from Japan's Asian neighbours – especially China – while domestic demand failed to provide any stimuli. With unemployment high in Japanese terms at 5.5%, consumer sentiment in particular remained subdued.

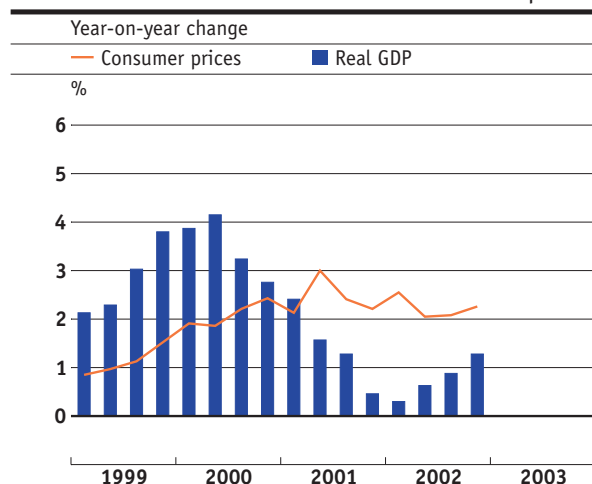
Economic difficulties persist in Latin America

The Argentine economy remained mired in the crisis that began in early 2002. In January 2003, this highly indebted country received a temporary reprieve from the International Monetary Fund in the form of a short-term deferment of loan repayments falling due. The seven-month extension should enable Argentina and the IMF to work out a comprehensive programme for the ailing economy. During 2002, Argentina stopped servicing a large proportion of its foreign debt.

More key-rate hikes in Brazil

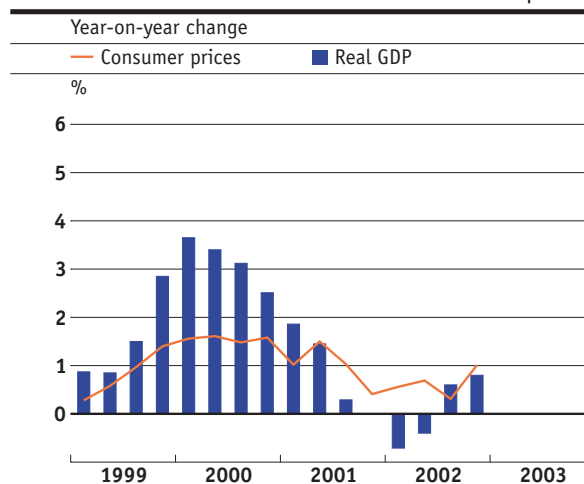
The economic situation in Brazil remained difficult, even after the new government took office at the beginning of 2003. The risk premium on government paper persisted at a high level, and the Brazilian currency – which had depreciated sharply last year – stayed weak. Furthermore, rising inflation forced the Brazilian central bank to tighten its monetary policy.

Euro area Graph 1.3



Source: BIS

Switzerland Graph 1.4



Sources: Swiss Federal Statistical Office (SFSO)
State Secretariat for Economic Affairs (seco)

1.2 Monetary policy and interest rates

Slight rise in inflation

Within the OECD (excluding high-inflation countries), average consumer price inflation rose from 1.8% in October to 2.1% in January. This increase was due entirely to higher oil prices – the price of a barrel of Brent crude was up to USD 34 in February, which is USD 10 above October's level. Core inflation (excluding food and energy) remained steady at 1.9% between October and January.

Prices rose at faster-than-average rates in the United States and United Kingdom. Between October and January, the US posted a 0.6 percentage point increase in inflation to 2.6%, while UK inflation was 0.8 percentage points higher at 2.9%. In the euro area, the higher oil price was offset to some extent by the lower dollar/euro exchange rate, and inflation eased a little from 2.3% in October to 2.2% in January. Germany's rate (1.0%) continued to be the lowest and Ireland's the highest at 4.7%. In Japan, deflation slowed from -0.9% in October to -0.3% in January.

Europe relaxes monetary policy

With the economy stagnating and the prospects for inflation looking good, most central banks in Europe relaxed their monetary policy during the first quarter. The European Central Bank cut its key rates by 25 basis points to 2.5% (the minimum offered rate for refinancing transactions) on 6 March, after its last rate reduction of half a percentage point in December. On 6 March the Norwegian and Danish central banks also cut their key interest rates by 0.5 and 0.25 percentage points respectively to 5.5% and 2.5%. On 18 March, the Swedish central bank followed suit with a 0.25 percentage-point reduction, bringing its key rate down to 3.5%. Back at the beginning of February, the Bank of England reduced its repo rate by 25 basis points to 3.75% in its first base rate move for over a year.

No change in expansionary monetary stance of US and Japan

The US Federal Reserve left its target call rate at 1.25% in the first quarter, following the half percentage point reduction in early November 2002. Japan's rate for overnight funds stuck at zero percent, while the Canadian central bank raised its target call rate slightly to 3% at the beginning of March in order to counter a rise in inflation.

Long-term interest rates on the decline

Long-term interest rates declined slightly between November and February, reflecting both political uncertainty and the fragility of the equity markets – factors which prompted investors to seek the security of government bonds. In February, the yield on 10-year government paper in the United States was 3.9%, or 0.2 percentage points lower than in November. In the United Kingdom, it fell by 0.3 percentage points to 4.3%, in the euro zone by 0.5 percentage points to 4.1% and in Japan by 0.2 percentage points to 0.8%. This means that the yields on 10-year government bonds in the US and euro area have fallen by one percentage point in the space of a year. Yields in the UK and Japan have contracted by 0.8 percentage points over the same period.

1.3 Economic outlook

Between December and March, most of the forecasting institutes revised down their growth forecasts for 2003. The consensus forecast¹ published in mid-March puts real GDP growth in the US at 2.4%, compared with a forecast of 2.7% in December. By contrast, the figure for Japan was raised slightly from 0.4% to 0.6%. Real growth in the euro area was put at 1.1%, as against 1.5% three months earlier. The forecast for France was corrected downwards by a particularly wide margin. At 2.1%, the consensus forecast for the UK is 0.2 percentage points lower than it was in December. In its mid-March forecast, the EU Commission put average real growth in the EU countries at about 1%.

Forecasts

Table 1

	Economic growth ²				Inflation ³			
	OECD		Consensus		OECD ⁴		Consensus	
	2003	2004	2003	2004	2003	2004	2003	2004
European Union	1.9	2.7	1.4	2.2	2.2	2.0	1.8	1.6
Germany	1.5	2.5	0.7	1.8	1.4	1.1	1.2	1.3
France	1.9	2.9	1.3	2.2	1.8	1.8	1.8	1.6
United Kingdom	2.2	2.5	2.1	2.5	1.8	2.1	2.7	2.4
Italy	1.5	2.5	1.3	2.2	2.3	1.9	2.3	2.0
United States	2.6	3.6	2.4	3.7	1.9	1.8	2.3	2.1
Japan	0.8	0.9	0.6	0.7	-1.1	-1.1	-0.6	-0.6
Switzerland	1.4	2.2	0.9	2.0	0.5	0.3	0.7	1.1

1 Consensus forecasts are monthly surveys conducted among approximately 200 leading companies and economic research institutes in roughly 20 countries, covering predictions for the development of GDP, prices, interest rates and other relevant economic indicators.

The results are published by Consensus Economics Inc., London.

2 Real GDP, change from previous year in percent

3 Consumer prices, change from previous year in percent

4 Inflation EU: euro area; inflation UK: excluding mortgage costs

Sources: OECD: Economic Outlook November 2002; Consensus: March Survey

2 Monetary situation

Declining interest rates at both the short and long ends, high growth in money stocks and higher mortgage lending all indicate an expansive monetary climate in Switzerland. At the same time, falling prices on the stock exchange, a slight appreciation of the Swiss franc and stagnant aggregate domestic borrowing are restricting monetary growth.

2.1 Interest rates

Money market rates on the wane

On 6 March 2003, the National Bank lowered the target range for the 3-month Libor rate by 0.5 percentage points to 0%–0.75%. This narrowing of the target band from 100 to 75 basis points was prompted by technical factors. The National Bank intends to keep the three-month Libor rate at around 0.25%, i.e. at the lower end of the new target range.

Swiss money market rates eased slightly between November 2002 and February 2003. The three-month Libor rate fell from an average 0.72% in November to 0.59% in February. Indeed, January and February saw the yield curve for money market investments flatten off considerably. By the end of February, money market rates for all durations of up to one year were at virtually the same level. Between November and February, the call money rate was an average of 14 basis points, and the issuing yield on federal money market debt register claims was 31 basis points below the three-month Libor rate.

Foreign money market rates, especially those within the euro area, fell more sharply than Swiss rates. This has cut the interest differential between Switzerland and international markets. On the basis of the three-month Libor rate, the spread between Swiss franc and dollar investments averaged 0.74 percentage points between November and February while that between the Swiss franc and the euro averaged 2.24 percentage points and that between the Swiss franc and the yen –0.59 percentage points.

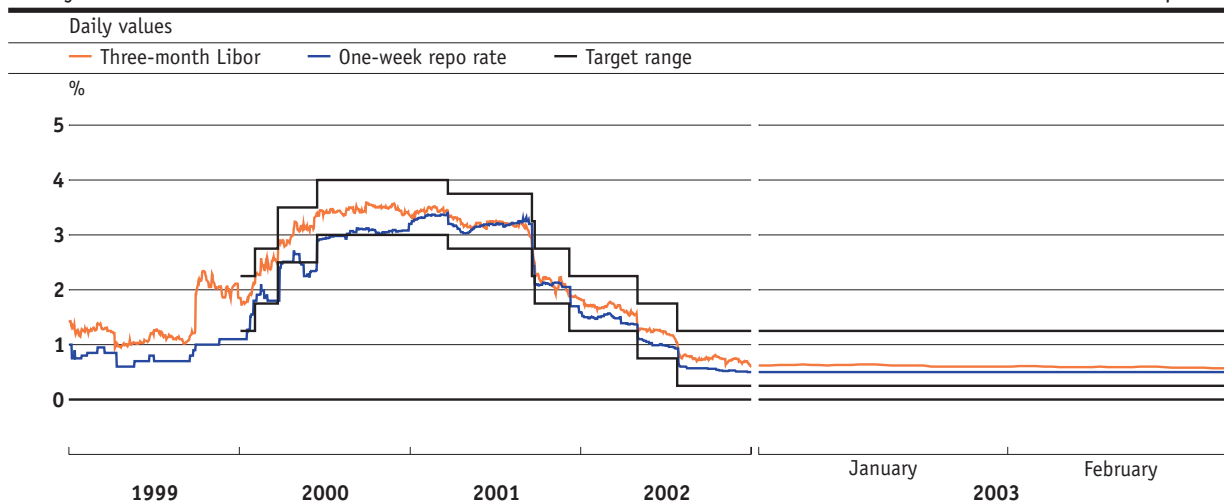
Bond yields falling

Between November 2002 and February 2003, yields on Swiss and other European government bonds with 10-year maturities fell steeply; those on US government bonds also declined, though only slightly.

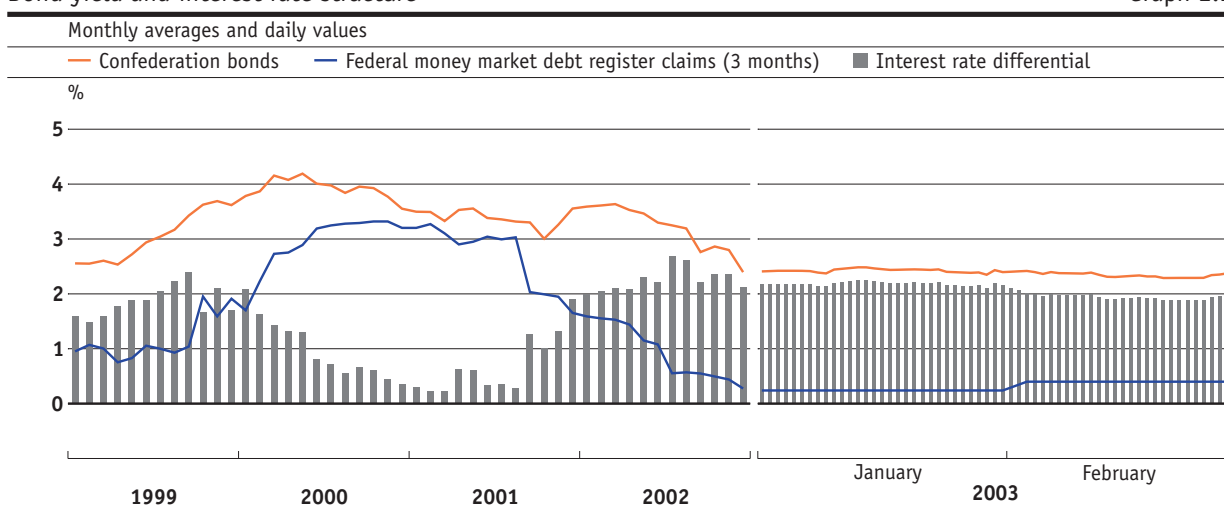
The yield on a Confederation bond with a maturity of 10 years dropped from 2.75% in November to 2.34% in February¹. As a result, the maturity premium – i.e. the spread between this yield and the yield on federal money market debt register claims with a three-month maturity – narrowed further from 2.31% in November to 1.94% in February.

The yield spread between foreign and domestic government bonds presented an uneven picture between November and February. Whereas the differential to US bonds widened slightly, the spread versus EU paper remained virtually unchanged and that vis-à-vis Japanese bonds narrowed slightly. Average yield differentials between November and February were as follows: 1.49 percentage points in relation to US bonds, 1.82 percentage points vis-à-vis EU bonds and –1.62 percentage points in relation to Japanese bonds.

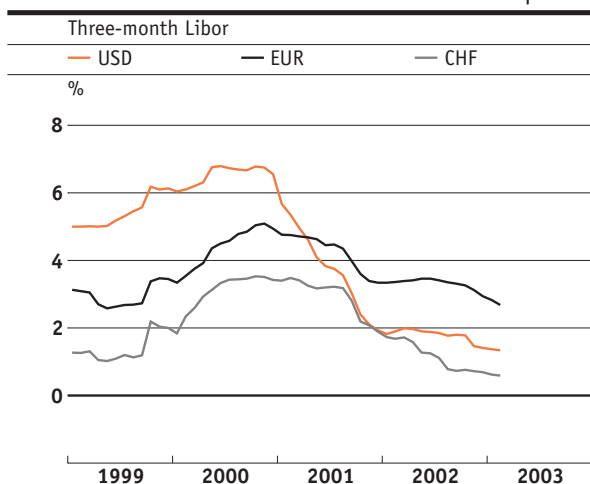
1 see Graph 2.2



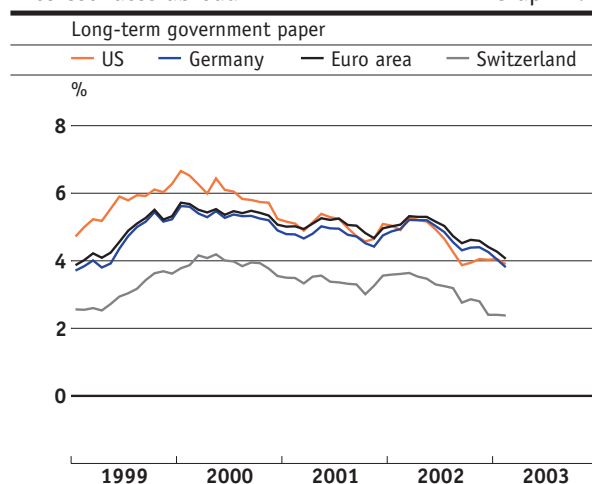
Bond yield and interest rate structure



Interest rates abroad



Interest rates abroad



Graphs 2.1 and 2.3: Source: SNB

Graph 2.2: Confederation bonds: until the end of 2000, average yield calculated by maturity: as of 2001, spot interest rate of 10-year discount bonds. Money market debt register claims: yield at auction. If several auctions per month: the last of the month. Source: SNB

Graph 2.4: US: yield on 10-year US treasury paper, secondary market. Germany: current yield on quoted 10-year German Federal securities. Switzerland: Confederation bonds; see graph 2.2. Source: BIS

Lower rates for new mortgages

Yields on medium-term notes, interest rates on savings accounts and mortgage rates all followed the downtrend in long-term interest rates. The big banks lowered their medium-term note coupons from 2.17% at the beginning of November to 1.53% at the beginning of March, while interest rates on savings deposits were cut from 1.04% at the beginning of November to 0.80% at the beginning of March. Thanks to the steep fall in money market rates, the cost of refinancing long-term loans remained low. After something of a time-lag, this helped to ease the situation on the mortgage market. However, rates for new mortgages fell more sharply than those for existing mortgages. Between the beginning of November and the beginning of March, the interest rate for existing mortgages declined by 16 basis points to 3.67% while that for new mortgages dropped by 49 basis points to 3.29%.

Equity markets fall to new lows

After a recovery in November, prices on the international equity markets continued to slide between December and February. Only the US stock-market indices were higher in February than at their lows of last October. On the other stock exchanges, prices were lower than in October 2002 across the board.

By the end of February, the SMI had dropped 50% below its 2000 high. The falls in America's Dow Jones Index (-33%) and S&P 500 Index (-45%) were not quite so dramatic, nor was that in the UK's FTSE 100 (-46%). However, Japan's Nikkei Index has lost about 60% since 2000; at the end of February, Germany's DAX was down by 68% and the Nasdaq by as much as 74% from their 2000 peaks.

2.2 Exchange rates

Weak dollar

After having stabilised in mid-2002, the US dollar depreciated further between December and February. The yen followed the dollar's downtrend.

Versus the euro, the dollar declined steadily from December onwards. By end-February the exchange rate was 1.08 USD/EUR, representing a 7% fall in the dollar since November. The dollar also depreciated slightly against the British and Japanese currencies, losing 2.4% against sterling and 1.8% against the yen since November.

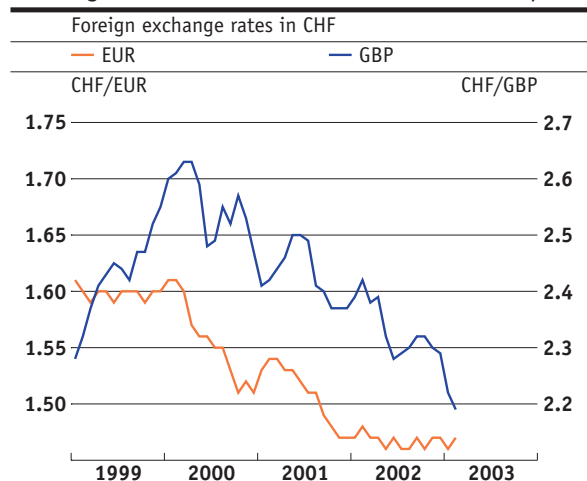
In December, the yen resumed its downtrend against most major currencies that had begun in mid-2002. By February, however, it had recovered again slightly. In relation to the euro, the yen lost 6% between November and February.

Slight firming of the Swiss franc

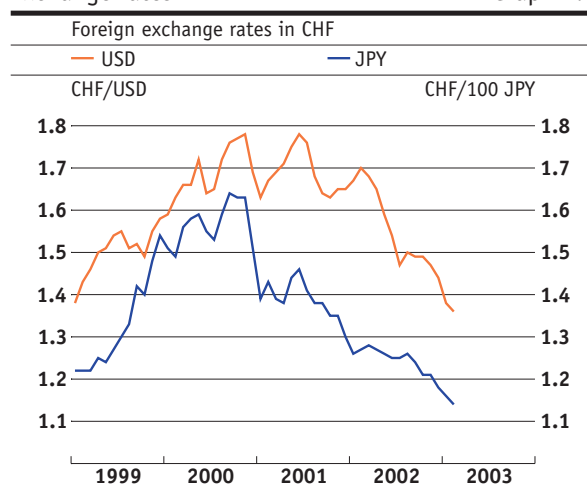
The export-weighted external value of the Swiss franc continued to rise between November and February. This was due mainly to its gains against the dollar and the yen, whereas it remained stable in relation to the euro. The dollar lost a total of 7% during this period, ending February at Sfr 1.36. The yen declined by 5% from November to Sfr 1.14 in February. The euro fluctuated between Sfr 1.45 and Sfr 1.48 – the same band in which it had been moving since autumn 2001. The pound sterling fell from Sfr 2.30 to Sfr 2.19 over the period.

The export-weighted real Swiss franc exchange rate increased by 1.9% between October and January. Its appreciation against the currencies of Switzerland's Asian trading partners (5.2%) and North America (8.4%) was particularly marked, while the rise against the European trading partners' currencies was just 0.4%.

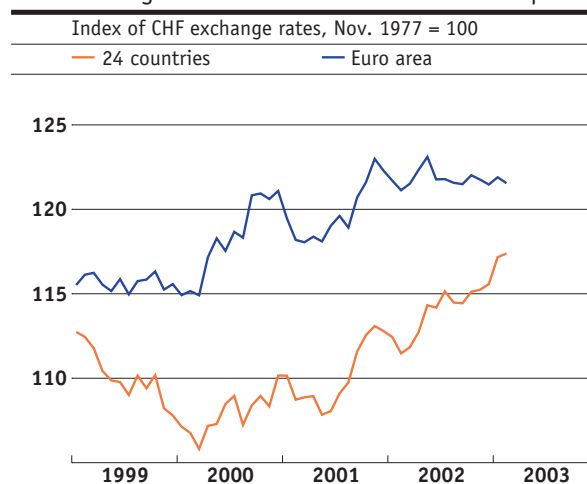
Exchange rates Graph 2.5



Exchange rates Graph 2.6



Real exchange rate indices Graph 2.7



Graphs 2.5, 2.6 and 2.7:
Source: SNB

2.3 Monetary aggregates

Rising number of notes in circulation

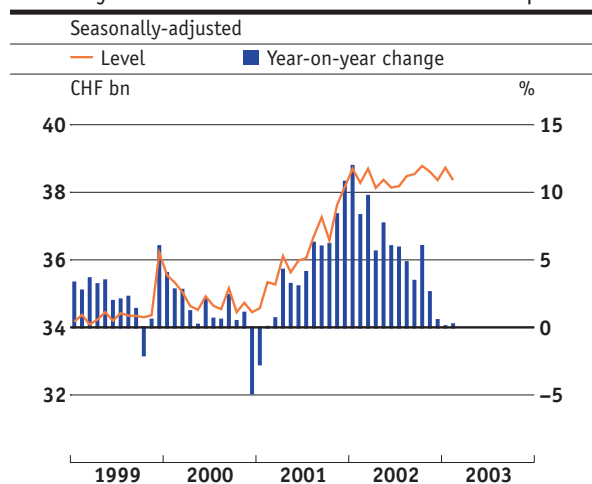
After falling between January and April 2002, the seasonally-adjusted figure for the number of notes in circulation has been edging up again since the summer of last year. In the fourth quarter, it was up by an annualised 2.2% compared with the previous quarter, although in January 2003 it was still 0.7% lower than its January 2002 peak. Movements in sight deposits do not exhibit any particular trend. January's 9.9% year-on-year growth is due entirely to the low figure recorded for January 2002. Overall, January's seasonally adjusted monetary base was 0.1% higher than the corresponding year-back figure.

The rise in seasonally adjusted banknote circulation since summer 2002 is due mainly to large denominations (thousand-franc notes). In the fourth quarter, these increased by an annualised rate of 1.8% on a seasonally adjusted basis, whereas medium value notes (hundreds and two-hundreds) expanded by 0.8% and the volume of small notes (tens, twenties and fifties) in circulation declined by 2.6%.

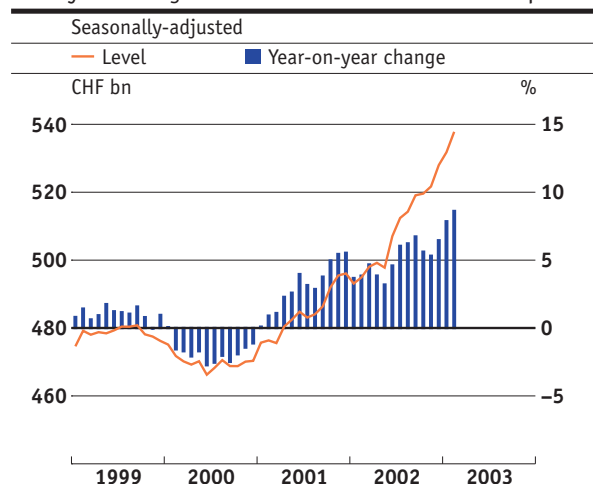
High growth rates for broader monetary aggregates

The M_1 , M_2 and M_3 monetary aggregates continued to rise in the fourth quarter and at the beginning of the year. Almost all components of the monetary aggregates posted increasing annual growth rates between November and January. The year-on-year fall in cash in circulation was more than offset by the 20.9% increase in sight deposits and the 8.7% expansion in transaction accounts, so that the M_1 money stock was 13% higher in January than a year earlier. Savings deposits were up by 15.5%, producing a 14.1% rise in M_2 . Time deposits advanced a little in January, but were still 15.0% below their year-back level. This produced 7.9% growth in the M_3 money stock. Money stock growth was last seen on this scale in 1996 and 1997.

Monetary base Graph 2.8



Money stock M_3 Graph 2.9



Graphs 2.8 and 2.9:
Source: SNB

Monetary base and its components

Table 2

	2001	2002	2001	2002						
			Q4	Q1	Q2	Q3	Q4	Dec.	Jan.	Feb.
Banknote circulation ¹	33.0	35.1	34.6	35.9	34.9	34.4	35.4	37.2	36.7	35.2
Change ²	4.7	6.3	8.7	10.8	7.3	5.2	2.4	1.5	-0.3	-0.6
Sight deposit accounts ¹	3.3	3.3	3.3	3.1	3.3	3.3	3.4	3.1	3.0	3.4
Change ²	0.2	0.4	6.0	0.1	-0.3	-1.6	3.6	-14.4	9.9	9.9
MB ^{1,3}	36.3	38.4	37.8	39.0	38.1	37.8	38.8	40.3	39.7	38.6
SAMB^{1,4}	36.3	38.4	37.5	38.6	38.2	38.4	38.6	38.4	38.7	38.4
Change ²	4.1	6.0	8.4	10.0	6.4	4.7	3.0	0.5	0.1	0.2

Broadly defined monetary aggregates and their components⁵

Table 3

	2001	2002	2001	2002						
			Q4	Q1 ^p	Q2 ^p	Q3 ^p	Q4 ^p	Dec. ^p	Jan. ^p	Feb. ^p
Currency in circulation	5.1	5.1	9.6	10.5	6.8	3.6	0.1	-2.0	-1.7	-0.5
Sight deposits	-0.7	11.7	2.8	4.7	6.5	17.5	18.1	18.5	20.9	19.5
Transaction accounts	1.6	8.5	7.0	8.1	8.3	9.7	8.0	6.4	8.7	9.8
M₁	1.0	9.6	5.3	6.8	7.2	12.5	11.6	10.7	13.0	12.9
Savings deposits	-6.1	9.9	-1.2	3.8	8.7	12.8	14.6	15.5	15.5	15.5
M₂	-2.3	9.7	2.3	5.4	7.9	12.7	12.9	12.8	14.1	14.0
Term deposits	26.9	-11.0	17.2	-0.6	-9.3	-14.4	-19.0	-17.1	-15.0	-11.6
M₃	3.1	5.0	5.3	4.1	3.9	6.3	5.8	6.5	7.9	8.7

1 In billions of Swiss francs; average of monthly values; monthly values are averages of daily values
 2 From previous year in percent
 3 MB = monetary base = bank-note circulation + sight deposit accounts

4 SAMB = seasonally-adjusted monetary base = monetary base divided by the corresponding seasonal factors

5 Definition 1995, change from previous year in percent
 p Provisional

2.4 Loans and capital market borrowing

Slight fall-off in domestic lending in 2002

Domestic lending covers loans by banks to borrowers domiciled in Switzerland or Liechtenstein and comprises secured and unsecured customer claims, as well as mortgage claims.¹ At the end of 2002, aggregate domestic lending stood at Sfr 619.8 billion. At 85%, secured domestic lending (comprising secured customer claims and mortgage claims) accounted for the lion's share of the total; of this figure, 90% is attributable to mortgage claims.

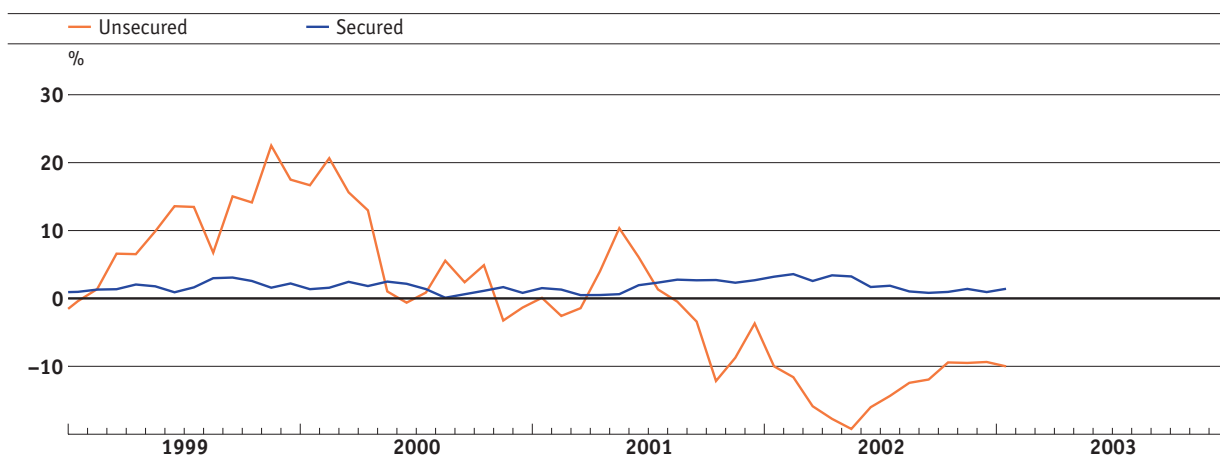
Domestic lending fell by 0.2% quarter-on-quarter in Q4 2002. In December, it was 0.7% lower than the previous year's level. As was the case in the third quarter of 2002, secured customer claims posted the steepest decline, falling another 8.4% compared with the previous quarter. Year-on-year, they registered a drop of 15.5%. Unsecured customer claims remained unchanged quarter-on-quarter during Q4 2002. There was nonetheless a substantial 9.4% drop compared with 2001 owing to the steep falls in the first three quarters of 2002. Mortgage claims continued to rise, putting on 0.9% compared with the previous quarter. In December they stood 3.2% higher year-on-year. The increase in mortgage claims is due mainly to more building of single-family dwellings.

While the cantonal banks and the regional banks raised their lending by 0.4% and 1.9% respectively year on year, domestic lending by the big banks declined by 3.8%. With the big banks occupying a high (39.4%) proportion of the domestic lending market, this segment overall was 0.7% down year-on-year.

Figures for January indicate that domestic lending is picking up slightly, as the total rose by 0.5% compared with December. Unsecured customer claims were the only lending component to post a month-on-month fall (-2.4%). Secured customer claims recorded a sharp 7.9% rise compared with December, while mortgage claims rose by 0.2% month-on-month in January.

Annual rates of change: secured and unsecured loans

Graph 2.10



¹ Owing to a change in the scope of the surveys conducted by the Raiffeisen banks in December 2002, these have been excluded for reasons of comparability.

High level of bond issuing among foreign borrowers

The fourth quarter of 2002 confirmed the trend of the preceding quarters, in which the Swiss bond issuing market was dominated by foreign borrowers. The volume of foreign bond issues reached a new high of almost Sfr 44 billion in 2002. Despite a high level of redemptions, foreign bonds accounted for more than 80% of net borrowing on the Swiss capital market.

Bond issues of domestic borrowers dropped to their lowest quarterly figure for almost 10 years. There were several reasons for this. First, public-sec-

tor borrowers – the Confederation, cantons and municipalities – were issuing only a very limited volume of bonds. At the same time, the subdued economic prospects meant that other types of borrowers were also reluctant to tap the bond market for funds.

The fourth quarter of 2002 saw the only major equity issue of the past year (Zurich Financial Services). Owing to large reductions in the two big banks' share capital in 2002, however, net borrowing on the equity market was negative over the year as a whole. A negative result on this scale had not been seen in the past decade.

Capital marked borrowing in billions of Swiss francs

Table 4

	2001	2002	2001 Q4	2002 Q1	Q2	Q3	Q4
Bonds and shares, total							
Price of issue ¹	73.4	77.3	21.6	24.0	20.5	13.6	19.3
Conversions/Redemptions	60.4	60.5	14.6	13.7	9.4	19.7	17.7
Net borrowing	13.0	16.8	7.0	10.3	11.1	-6.1	1.5
Swiss bonds							
Price of issue ¹	27.0	26.2	4.7	8.0	9.2	5.5	3.4
Conversions/Redemptions	21.1	22.5	4.5	6.9	4.0	5.5	6.0
Net borrowing	5.9	3.7	0.2	1.1	5.3	0.0	-2.6
Swiss shares							
Price of issue ¹	12.3	7.4	9.4	1.5	0.2	0.7	5.1
Redemptions	7.3	9.1	0.4	0.8	0.9	6.6	0.8
Net borrowing	5.0	-1.7	8.9	0.7	-0.8	-5.9	4.3
Foreign bonds²							
Price of issue ¹	34.0	43.7	7.5	14.4	11.1	7.4	10.8
Redemptions	32.0	28.9	9.6	5.9	4.4	7.6	11.0
Net borrowing ³	2.1	14.8	-2.1	8.5	6.7	-0.2	-0.2

1 By date of payment

2 Without foreign-currency bonds

3 Without conversions

3 Aggregate demand and output

3.1 GDP and industrial output

Business climate remains subdued

On an annualised basis, Switzerland's real GDP rose by 1.4% in the fourth quarter of 2002 compared with the year-back figure. This was a slower rate than in the previous quarter. The year-on-year growth figure was 0.8%, compared with 0.6% in the third quarter.

The economic recovery remained fragile through to year-end, and was driven by only a small number of demand components. Private consumption showed little growth, and construction investment continued to fall. Capital spending declined sharply again. By contrast, exports – driven in particular by rising demand from Asia – made a positive contribution to growth. Demand from the leading European trading partners, however, continued to wane. Since imports fell sharply owing to the downturn in domes-

tic demand, foreign trade made a strongly positive contribution to economic growth for the second time running.

Industrial activity still weak

Despite a slight upward movement, both the Purchasing Managers Index (PMI) and the results of the KOF/ETH survey pointed to further contraction in the industrial sector between October and February. This applies to exporters as well as to companies producing for the home market. Output probably decreased again in both sectors, though less markedly than in the third quarter. As order intake was lower than production, the volume of outstanding orders shrank. Almost half the companies surveyed considered order intake to be inadequate. With signs of a recovery still not forthcoming, companies continued to wind down their stocks of finished products. In order to cut costs, moreover, they implemented further headcount reductions.

GDP and its components

At prices of 1990; percentage-point contribution to year-on-year change in GDP

Table 5

	2001	2002	2001	2002			
			Q4	Q1	Q2	Q3	Q4
Private consumption	1.1	0.5	1.0	0.9	0.4	0.5	0.2
Govt. and social insurance consumption	0.4	0.3	0.4	0.1	0.4	0.5	0.4
Investment in fixed assets	-1.4	-1.6	-3.0	-2.1	-1.6	-0.9	-1.9
Construction investment	-0.6	-0.2	-0.7	0.0	0.2	-0.4	-0.4
Equipment investment	-0.8	-1.5	-2.3	-2.0	-1.8	-0.5	-1.5
Domestic final demand	0.1	-0.8	-1.6	-1.2	-0.8	0.1	-1.3
Inventories	0.7	-0.5	0.0	-0.8	1.0	-1.8	-0.3
Exports, total	0.0	0.2	-1.6	-1.5	-1.2	1.5	1.8
Aggregate demand	0.7	-1.1	-3.3	-3.5	-1.0	-0.2	0.1
Imports, total	-0.1	-1.2	-3.3	-2.7	-0.6	-0.8	-0.7
GDP	0.9	0.1	0.0	-0.7	-0.4	0.6	0.8

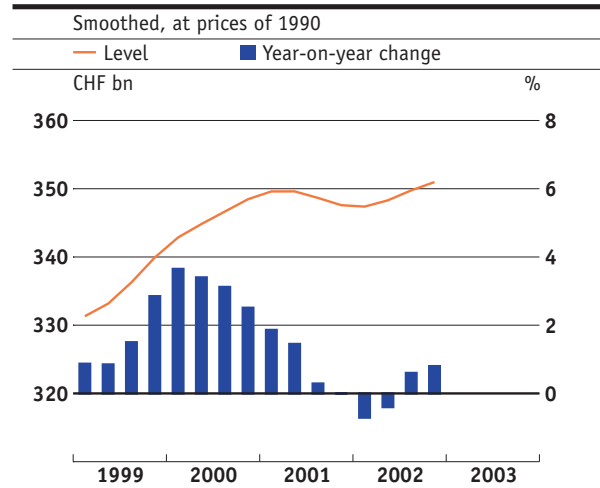
Sources: SFS0, seco

Growing uncertainty

With the world economy remaining weak, companies took a more pessimistic view of the outlook than they had in autumn 2002. By February only a small majority of firms were anticipating any rise in orders in the next few months. In fact, demand was expected to decline slightly overall during the next three to six months. Consequently, few companies were planning to increase their output, and stocks of unfinished goods were being cut back sharply. Companies focusing mainly on the domestic market were rather more optimistic about the short to medium-term outlook than exporters.

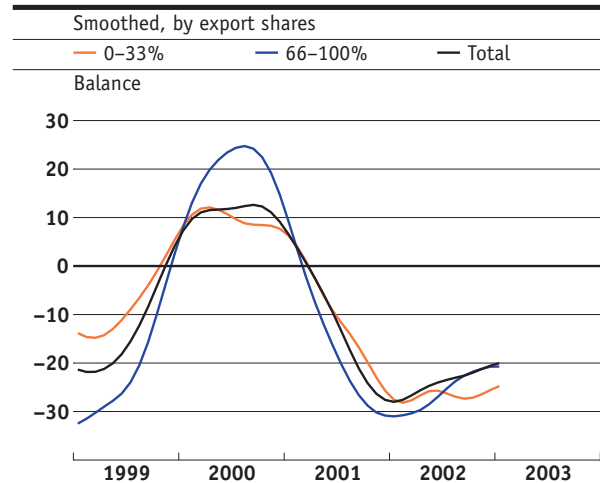
GDP

Graph 3.1



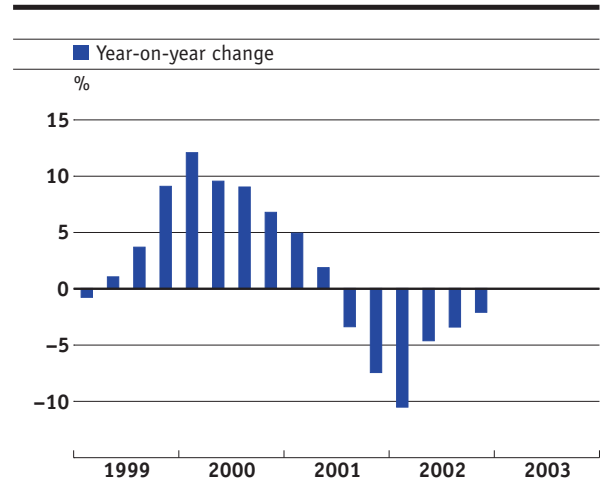
Industrial activity

Graph 3.2



Industrial output

Graph 3.3



Graph 3.1:
Annualised estimate for the quarter
Source: seco

Graph 3.3: Source: SFSO

Graph 3.2: The synthetic index of industrial activity consists of the results of the following four questions: orders received and output compared with the corresponding year-earlier month, as well as evaluation of the order backlog and of the finished goods inventories.
Source: Swiss Institute for Business Cycle Research at the Federal Institute of Technology (KOF/FIT)

3.2 Foreign trade and current account

Large trade surplus

In real terms, exports of goods and services rose by an annualised 4.8% from the previous period in the fourth quarter, exceeding the year-back level by 3.9%. Exports of services rose much faster than those of goods. By contrast, the downturn in imports of goods and services accelerated: the quarterly figure was 1.6% lower than a year earlier. As a result, foreign trade contributed 4.1 percentage points to the quarter-on-quarter rise in real GDP and 2.5 percentage points to year-on-year growth.

Higher goods exports

According to the General Directorate of Customs (OZD)¹, goods exports in the fourth quarter were 5.4% higher than a year earlier in real terms. All of the export types (which are classified by use) recorded year-on-year gains, but the growth was slower than in the previous period. Buttressed by pharmaceutical shipments, exports of consumer goods again grew at an exceptionally fast rate, exceeding the year-back figure by 7.3%. Deliveries of raw materials and semifinished products expanded further, and exports of investment goods were also – for the first time in five quarters – higher than a year earlier.

Real exports by use²

Change from previous year in percent

Table 6

	2001	2002	2001	2002			
			Q4	Q1	Q2	Q3	Q4
Total	2.9	1.8	-2.3	-3.5	0.5	5.3	5.4
Raw materials and semi-manufactures	-1.5	-0.4	-7.4	-8.6	1.6	1.0	5.8
Capital goods	-0.4	-4.4	-7.6	-12.4	-5.7	-2.0	2.8
Consumer goods	9.4	8.5	6.9	8.2	4.9	14.6	7.3
Export prices	1.2	-2.7	-0.1	-2.5	-0.5	-3.9	-4.3

Real imports by use²

Change from previous year in percent

Table 7

	2001	2002	2001	2002			
			Q4	Q1	Q2	Q3	Q4
Total	1.1	-2.5	-7.3	-6.1	-0.6	-1.3	-1.7
Raw materials and semi-manufactures	0.1	-2.5	-8.6	-9.7	-2.6	0.5	2.8
Energy sources	7.9	-2.1	7.4	6.0	-0.8	-1.7	-11.1
Capital goods	-5.0	-6.2	-13.5	-12.1	-7.9	-2.0	-2.3
Consumer goods	5.8	0.0	-3.5	-0.6	6.2	-2.0	-2.9
Import prices	0.1	-2.9	-2.3	-3.1	-2.9	-3.5	-2.2

1 Real exports of goods according to the definition by the Swiss General Directorate of Customs (total 1) correspond to real exports of goods reported by seco excluding exports of electrical energy and the subcategory "Other goods".

2 Without precious metals, precious stones and gems as well as objets d'art and antiques (total 1). Source: Swiss General Directorate of Customs

Lower demand from the EU

After a temporary rise in the third quarter, nominal exports of Swiss goods to the EU dropped back below the year-earlier level (-2.8%). This was due mainly to the sharp fall in shipments to the two largest export markets, Germany and France. By contrast, exports to Italy rose. Following a decline in the third quarter, deliveries to central Europe were again slightly higher than in the year-back period (up 1.4%).

Buoyant demand from Asia

Nominal exports to the US were lower in Q4 than they had been in the previous quarter. Owing to vigorous growth at the beginning of 2002, however, they were still significantly (13.0%) above the year-back figure. In contrast to this, exports to Japan, and especially to China, expanded strongly, gaining 12.1% and 62.6% respectively. Consistently buoyant demand from China has raised this country's share of total nominal Swiss exports from 0.9% to 1.6% between 1997 and 2002.

Export outlook clouded by uncertainty

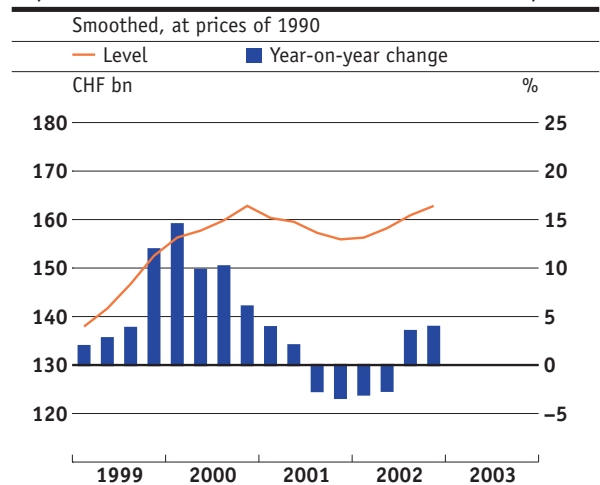
January and February saw only a minor rise in real goods exports over the previous month, producing an average year-on-year decline of 3%. The scale of the downturn may well have been amplified somewhat by a sharp drop in pharmaceutical exports. As order intake in the export industry has been unsatisfactory, however, a fall-off had been expected. Switzerland's export industry is geared in large part to the production of capital goods. There is no prospect as yet of any substantial worldwide recovery

in capital spending, from which Swiss exporters would derive particular benefits.

Downturn in goods imports

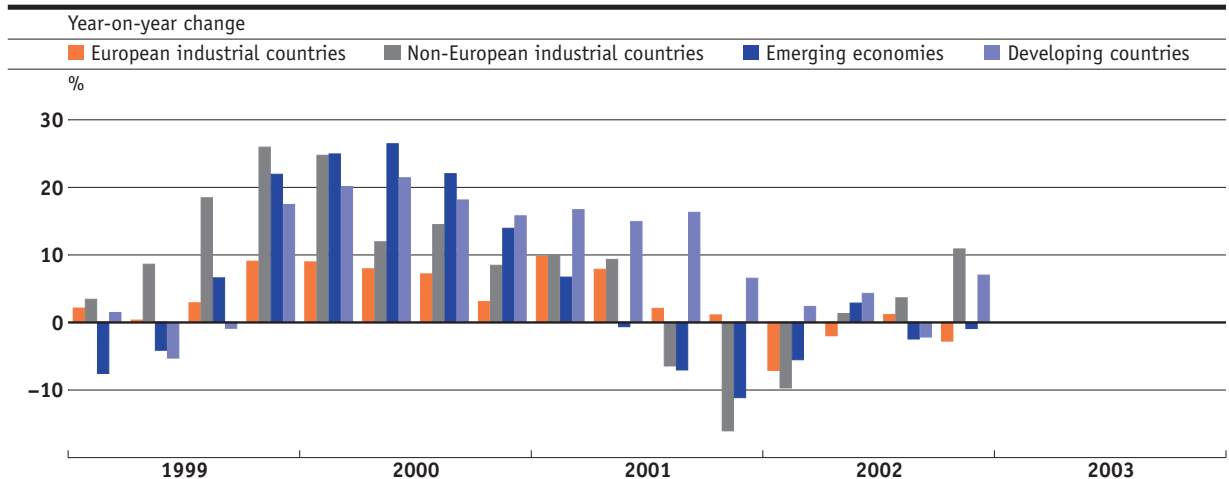
According to the fourth-quarter figures published by the General Directorate of Customs, real goods imports were 1.7% below the year-back level. This decline affected three of the four groups of imports (classified by use). Above-average falls were registered by imports of consumer goods (-2.9%) and capital goods (-2.3%). The latter have been declining continuously for almost two years. Deliveries of energy sources plunged even more dramatically, falling by 11.1% year on year. By contrast, imports of raw materials and semi-manufactures were above the year-earlier level (2.8%).

Exports Graph 3.4



Exports by trading partners

Graph 3.5



Graph 3.4: Annualised estimate for the quarter, without precious metals, precious stones and gems as well as objets d'art and antiques (total 1). Source: seco

Graph 3.5: Without precious metals, precious stones and gems as well as objets d'art and antiques (total 1). Source: Swiss General Directorate of Customs

Slide in export and import prices

In the fourth quarter, export prices (mean figures) were 4.3% lower than a year earlier. This was the fifth fall in succession. As in the previous period, the producer price index for goods earmarked for export also declined. This suggests that the rise in real exports took place at the expense of margins again. Import prices measured on a mean-price basis showed a slightly less pronounced fall (-2.2%), owing partly to the higher prices for oil products. The terms of trade, i.e. the relationship between export and import prices, deteriorated by 2.1% compared with the fourth quarter of 2001.

Current account surplus widens slightly

Nominal exports rose by 0.8% year on year in the fourth quarter of 2002, while imports (special trade, not working day-adjusted) declined by 3.8%. The trade surplus thus widened from Sfr 1.6 to Sfr 3.1 billion in the space of a year. The balance of the total goods trade – i.e. also including trade in electrical energy plus imports and exports of precious metals, precious stones and gems, etc. – closed with a surplus of Sfr 1.9 billion. However, the surplus from services increased only slightly versus the year-back quarter, growing by Sfr 0.6 billion to Sfr 5.9 billion. This rise was due to higher receipts from tourism and cross-border insurance business. In the fourth quarter of 2001 this income had been exceptionally low owing to the events of 11 September. The banks' commission income decreased again from the previous year. Owing to lower net earnings from direct invest-

ments, the surplus from labour income and investment income declined by Sfr 1.7 billion to Sfr 6.2 billion. This resulted in a current account surplus of Sfr 12.6 billion in the fourth quarter, up from Sfr 11.9 billion in Q4 2001.

The current account surplus grew by Sfr 11.7 billion to Sfr 49.6 billion in 2002. This sharp rise was due in large part to the transition from a negative to a positive balance of trade. As a percentage of nominal GDP, the current account surplus grew from 9.1% in 2001 to 11.9%.

Current account Balances in billions of Swiss francs

Table 8

	2001 ¹	2002 ²	2001 ¹	2002 ²			
			Q4	Q1	Q2	Q3	Q4
Goods	-4.6	4.5	0.9	0.1	0.6	1.9	1.9
Special trade	1.7	7.3	1.6	0.9	1.4	1.9	3.1
Services	24.2	24.9	5.3	7.7	5.1	6.2	5.9
Tourism	2.0	1.1	0.0	1.3	-0.3	0.1	0.1
Labour income and investment income	25.2	26.7	7.9	6.0	6.7	7.8	6.2
Investment income	33.8	35.9	10.1	8.2	9.0	10.1	8.6
Current transfers	-6.9	-6.6	-2.2	-2.2	-1.5	-1.5	-1.4
Total current account	37.9	49.6	11.9	11.6	11.0	14.4	12.6

1 Provisional

2 Estimates

3.3 Investment

The economic slowdown has had an appreciable impact on investment activity. Capital spending (investment in construction and equipment) fell off more sharply in Q4 2002 than in the previous quarter, undershooting the year-back level by 7.6%.

Construction investment pointing downwards

The downturn in construction investment continued in the fourth quarter. In a year-on-year comparison, it eased 3.9%. Residential building activity, measured in terms of the number of dwellings under construction, was 1.6% higher than a year earlier. On the other hand, the Q4 2002 survey of the Swiss contractors' association indicated that the volume of civil engineering work was continuing to diminish.

Building activity expected to remain sluggish

At present, there is no sign that investment in construction will provide any boost to the economy. Civil engineering is feeling the impact of public-sector spending cuts. Given the high level of vacancies, the commercial segment of the building sector also looks set to contract further until the end of the year. Residential construction, however, gives grounds for cautious optimism. More building permits were issued for dwellings in Q4 2002 than a year earlier, and although economic worries might cause some residential construction projects to be deferred, the price and rent patterns identified by property consultants Wüest & Partner suggest that demand is still buoyant. Declining construction costs and low mortgage rates are fundamentally conducive to house-building activity, so it would be reasonable to expect a gradual revival in this segment.

Sharp drop in equipment investment

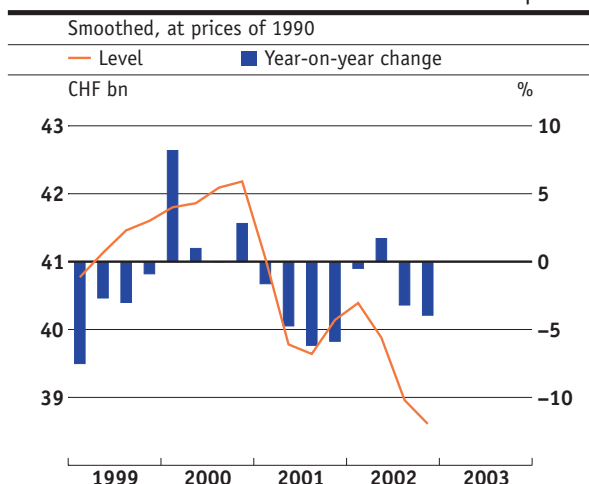
The downturn in investment in plant and equipment observable since mid-2001 continued in the final quarter of 2002. In a year-on-year comparison, it eased 10.5%. Imports of capital goods experienced another sharp drop. According to a fourth-quarter survey in the Swiss mechanical and electrical engineering industries (Swissmem), domestic sales of Swiss-made capital goods also fell steeply.

Growth stimuli set to emerge in second half

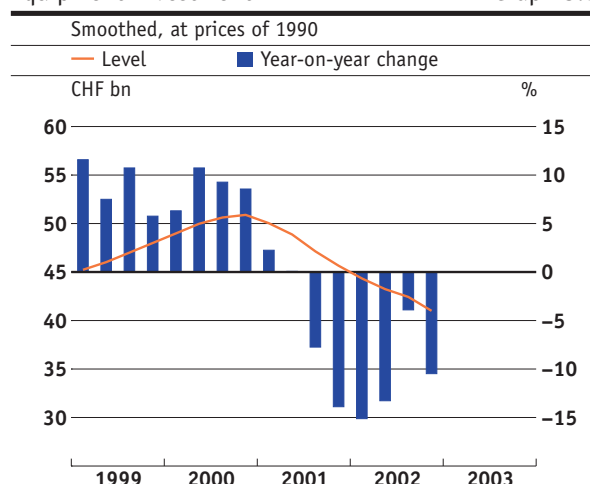
Stagnating capacity utilisation in industry coupled with a depressed earnings situation continue to inhibit investment activity. However, the necessary preconditions are in place for a rapid revival once the business climate starts to improve. There is now a pressing need for capital goods with a short service life to be replaced. According to the annual KOF/ETH investment survey, companies are not yet planning to invest in expansion this year. Nevertheless, all sectors apart from banking are planning to boost investment on replacement and upgrading, though investment plans were rated as less concrete than in the 2002 survey.

The implementation of investment projects makes heavy demands on the service sector. An upswing in investment activity would thus provide a major growth stimulus for the economy as a whole even if a high proportion of capital goods are imported.

Construction investment Graph 3.6



Equipment investment Graph 3.7



Graphs 3.6 and 3.7:
Annualised estimate for the
quarter
Source: seco

3.4 Consumption

Subdued growth in consumer spending

Although sentiment was subdued, consumer spending continued to drive economic activity in the second half of 2002. After staying almost flat in the third quarter, private consumption rallied slightly in Q4. Year on year, consumer spending grew by 0.4% compared with 0.9% in the third quarter. Growth thus remained well below the long-term trend figure of approximately 1.3%. Private consumption was driven mainly by spending on the relatively non-cyclical areas of housing and health care.

The other components mirrored the general slowdown in consumer spending. In the retail sector, which accounts for about a third of private consumption, the real volume of sales was 1.6% lower in Q4 2002 than a year earlier, whereas the third quarter had shown no change from the previous year. While the hotel sector enjoyed a further rise in domestic demand, thus continuing a trend that began in mid-2002, the number of overnight stays in the fourth quarter was still 2.2% below the year-back figure. New car registrations – an indicator of demand for consumer durables – dropped 6.6% and was thus in the negative zone for the fourth quarter in succession.

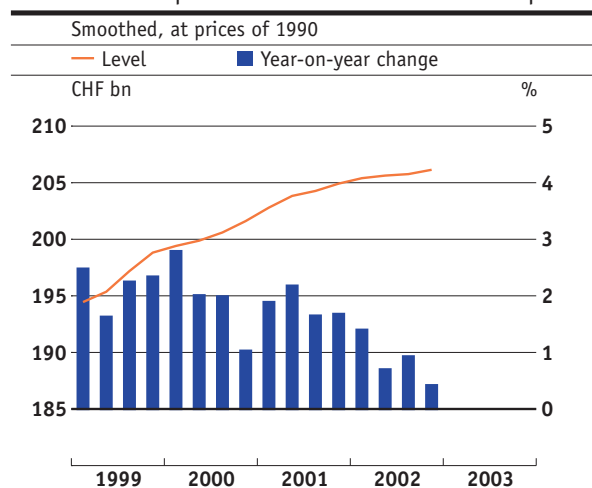
Consumer sentiment clouded

Consumer sentiment remains clouded. Although the consumer sentiment index improved from –39 to –25 points in January, it continued to languish at a relatively low level. Households took a less pessimistic view of the general economic situation and of their personal financial situation than in the past twelve months. The indicator for people's assessment of their financial situation in the next twelve months remained in the positive zone. On the other hand, households judged their job security to have deteriorated again and were deferring major purchases.

Worsened outlook

According to KOF/ETH surveys, retail companies have increasingly considered their business situation to be unsatisfactory since mid-2002. In January and February, the majority of companies stated that their year-on-year sales figures were either flat or had fallen slightly. Whereas in Q4 2002 they had been predominantly upbeat about sales in the next three months, their forecasts were now slightly negative on the whole. The catering trade, and hotels in particular, expect demand to continue falling.

Private consumption Graph 3.8



Annualised estimate for the quarter
Source: seco

3.5 Capacity utilisation

The rate of capacity utilisation of an economy's aggregate production factors provides a good basis for assessing the cyclical situation and future price developments. Since the rate of capacity utilisation cannot be monitored as such, the National Bank bases its assessments on two indicators: the macro-economic output gap and the utilisation rate of technical capacities in industry.

Output gap unchanged

"Production potential" indicates the level of production that can be achieved without triggering inflation. The output gap is the percentage difference between actual real GDP and production potential. A negative output gap signifies under-utilisation of capacity, while a positive output gap indicates that the production factors are being over-utilised.

Owing to the cyclical downturn, overall utilisation of production factors in 2001 declined and the output gap turned negative. After having expanded to -2% by the first quarter of 2002, the output gap did not widen any further up to the end of the year. This can be ascribed to slightly slower growth in production potential, which was due in turn to the low level of capital spending in 2002. In the final quarter of the year, production potential expanded in step with real GDP. As a result, the output gap was the same as in the previous period (2%).

Capacity utilisation in industry stagnating

Capacity utilisation in industry is measured by the quarterly KOF/FIT survey. Approximately 1600 companies are asked to report on the average utilisation of their technical production capacity during the quarter.

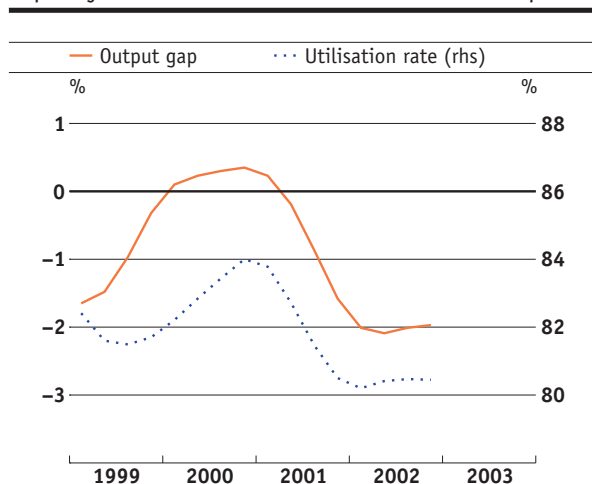
After declining from 84% to 80.5% in 2001, capacity utilisation stabilised at the latter level in 2002. The long-term average is 84%. Most companies judged the level of technical capacity to be adequate. Weak demand remained the chief problem. In recent quarters, this – together with price concessions that have resulted partly from exchange rate changes – has greatly worsened companies' profit figures, especially in the export industry.

3.6 Economic outlook and forecasts

Most of the forecasting institutes that published new forecasts for Swiss economic growth in 2003 have revised these downwards. On average, real GDP is now expected to increase by just under 1% in the current year. Some of the forecasts for individual demand components vary widely, reflecting the fact that forecasting risks are currently very high.

For this year, the National Bank is expecting real GDP to grow by just under 1%. It bases its assumptions on a pick-up in economic activity in the second half of the year. The main stimuli are likely to come from abroad: a recovery in exports should translate into higher capital spending. With the global economic outlook remaining uncertain, however, there is still a considerable risk of the upswing being delayed.

Capacity utilisation Graph 3.9



Source: KOF

4 Labour market

4.1 Employment

Employment levels falling

The state of the labour market deteriorated again in the fourth quarter of 2002. After an unexpected rise in Q3, the number of people in employment declined by a seasonally adjusted 0.7% compared with the previous quarter. In a year-on-year comparison, employment was down 0.8%. The number of full-time positions continued to decline. For the first time in the current economic cycle, part-time employment was also lower than in the previous quarter, though it was still 1.4% higher than a year previously.

The number of jobs in industry declined again both in comparison with the previous quarter (-0.9%) and with Q4 2001 (-3.5%). For the first time, the service sector also reported a significant decrease in employment: the number of jobs diminished by 0.8% compared with the previous period and was 0.1% short of the corresponding year-earlier level. Within the service sector, the largest job losses were in catering, insurance and recently also banking. On the other hand, new jobs were created in retailing, IT, health care and social services. In construction, employment was slightly higher than in the third quarter but unchanged in a year-on-year comparison.

Fewer job vacancies

The low demand for labour is also reflected in the development of job vacancies. The job vacancies index compiled by the Swiss Federal Statistical Office (SFSO) on the basis of survey results fell again in the fourth quarter. The Manpower Index, which measures the space occupied by job advertisements in Swiss newspapers, also continued to fall until February, as did the number of job vacancies registered with employment offices.

Labour market Figures not seasonally-adjusted

Table 9

	2001		2002		2003				2003	
			Q4	Q1	Q2	Q3	Q4	Jan.	Feb.	
Full- and part-time employed ¹	1.1	-0.4	0.4	-0.3	-0.3	-0.2	-0.8	-	-	
Full-time employed ¹	0.7	-1.3	0.0	-1.0	-1.3	-1.3	-1.6	-	-	
Unemployment rate ²	1.9	2.8	2.1	2.6	2.5	2.7	3.3	3.8	3.9	
Unemployed ³	67.2	100.5	77.3	93.5	91.2	97.1	120.2	138.9	142.0	
Jobseekers ³	109.4	149.6	119.9	139.8	139.7	146.3	172.6	192.6	197.5	
Persons on short working hours ³	2.4	9.1	6.6	9.8	11.6	4.4	6.8	9.8	-	
Registered vacancies ¹	-18.3	-40.3	-39.2	-38.0	-46.3	-39.5	-35.9	-	-	

1 Change from previous year in percent

2 Registered unemployed in percent of the economically active population according to the 1990 national census (working population: 3,621,716 persons)

3 In thousands; yearly and quarterly values are averages of monthly values

Sources: SFSO, seco

4.2 Unemployment

Continuing rise in jobless numbers

Unemployment continued to rise between October and February. In February, the number of unemployed persons registered at employment offices was a seasonally adjusted 127,100, up from 116,000 in October. The number of job seekers rose at roughly the same pace and totalled 183,200 persons in February. The proportion of long-term unemployed, which lags behind the unemployment figure by about a year, has been increasing since mid-2002 and reached 14.6% in February.

In February, unemployed persons and job seekers accounted for 3.5% and 5.1% respectively of the total active population (seasonally adjusted figures). Both of these percentages are calculated on the basis of the active population as established by the 1990 census. Between 1990 and 2003, the active population rose from 3.62 million to about 4 million. The unemployment figures expressed in terms of this higher statistical base are thus lower than the officially published figures by approximately 0.3 and 0.4 percentage points respectively. Adjustment of the calculation method to the new situation is planned for the second half of 2003.

In 2002, the number of job seekers rose on average by 40,000 while the number of persons in employment decreased by a much smaller margin (13,600). The pronounced discrepancy is due to the continuing rise in the number of jobs on offer.

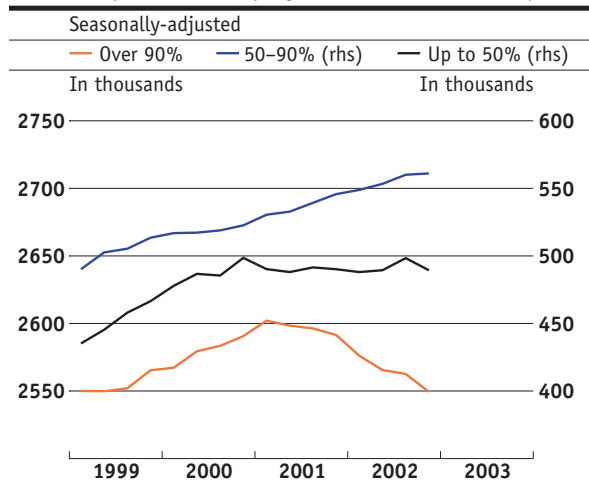
Less short-time working

After a rise in the first half of 2002, short-time working decreased sharply in the second half. The downturn in short-time working in tandem with a fall-off in employment suggests that companies are expecting a persistently sluggish business climate.

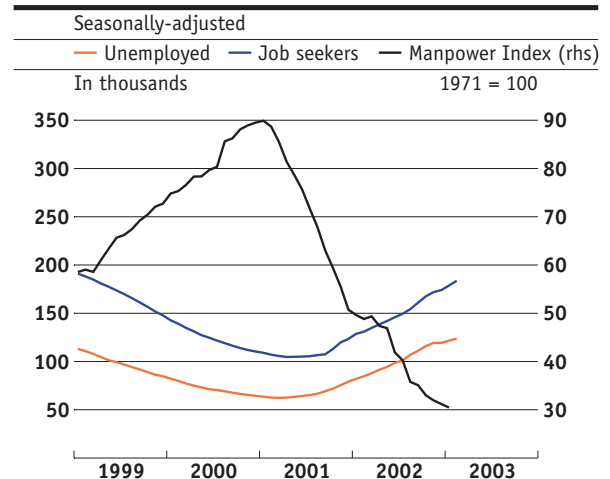
Employment prospects gloomy

According to KOF/ETH surveys of industry and the service sector, and in view of the employment prospects depicted by the SFSO, demand for labour will remain soft in the next few months, spelling a further rise in unemployment. The situation on the labour market is unlikely to improve until the expected economic recovery takes effect in the second half of 2003.

Full- and part-time employment Graph 4.1



Unemployment and vacancies Graph 4.2

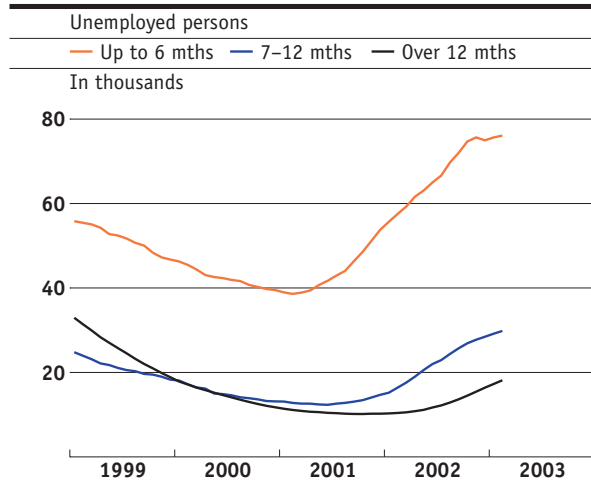


Graphs 4.1, 4.2:
Source: SFSO

4.3 Wages and salaries 2003

According to SFSO figures, nominal pay rose by 1.8% in the first three quarters of 2002 compared with year-back levels. This rise takes account of the agreement among the main supermarket chains to abolish net minimum wages of less than Sfr 3000 per month. According to a pay survey conducted by UBS in October 2002, nominal pay levels should rise by 1.3% in 2003.

Duration of unemployment Graph 4.3



Source: SFSO

5 Prices

5.1 Consumer prices

After easing to 0.8% in January, annual inflation (as measured by the national consumer price index) rose in February to 0.9%, thus returning to its level in November and December. Whereas prices for domestic goods and services in particular declined again between November and February, the inflation rate for foreign goods rose owing to higher oil prices.

Another slight fall in domestic inflation

Between November and February, annual inflation in domestic goods and services shed 0.2 percentage points to 1.0%. Between June and October, the rate was 1.3%. This downturn in domestic inflation affected both goods and services. By February, annual inflation for goods was down to 0.1% from 0.7% in November. Inflation for services, which make up about three-quarters of the domestic commodities basket, recorded a much smaller fall (to 1.2%). The quarterly rents survey in February showed that annual inflation in rentals had fallen from 0.5% to 0.3%, the lowest level since April 1999, while price rises for other private services moderated from 1.9% to 1.5% in the space of a year. By contrast, annual inflation in public services rose by 1.1 percentage points to 2.4%. This surge in inflation was due mainly to higher hospital charges and a rise in radio and television licences.

Foreign-goods inflation on the rise

Owing to higher oil prices, the price index for foreign goods rose in the second half of 2002; since October it has been above the year-back levels again. In February, oil prices were 10.0% higher than a year previously – the strongest rise for two years. On the other hand, prices of other imported goods fell by 0.5%.

New weightings for the commodities basket

Since the last major adjustment in May 2000, the national consumer price index has been calculated as a chain index with annual reweighting of the commodities basket. This should ensure that constantly changing consumer habits are more accurately reflected and inflation is more precisely measured. The reweighting of the commodities basket performed at the beginning of 2003 is based on the EVE survey of income and consumer habits conducted in 2001. Compared with that performed at the beginning of 2002, this reweighting caused only slight shifts in the twelve main commodity groups used for the national price index. The relative importance of healthcare and clothing & footwear groups was increased, whereas the weightings for living & energy costs and for leisure & entertainment were reduced. At 19.7%, the weighting for rentals remains the highest in the basket. The weighting for oil products (fuel and heating oil) was reduced again to 3.6%.

Breakdown of the national consumer price index

Change in percent

Table 10

	2002		2002				2003	
			Q2	Q3	Q4	November	December	January
National consumer price index total	0.6	0.7	0.3	1.0	0.9	0.9	0.8	0.9
Domestic goods and services	1.4	1.5	1.3	1.2	1.2	1.1	1.0	1.0
Goods	1.1	1.2	0.7	0.6	0.7	0.3	-0.2	0.1
Services	1.5	1.6	1.4	1.3	1.3	1.3	1.3	1.2
Private services without rents	1.9	2.0	1.8	1.9	1.9	1.8	1.5	1.5
Rents	1.0	1.1	0.9	0.6	0.5	0.5	0.5	0.3
Public services	1.5	1.6	1.6	1.3	1.3	1.3	2.4	2.4
Imported goods and services	-1.7	-1.8	-2.6	0.5	0.2	0.3	0.5	1.0
Without oil products	-0.8	-0.1	-1.7	0.5	0.1	-0.2	-0.7	-0.5
Oil products	-6.8	-10.2	-7.6	0.2	-0.2	2.8	8.5	10.0

Sources: SFSO, SNB

5.2 Core inflation

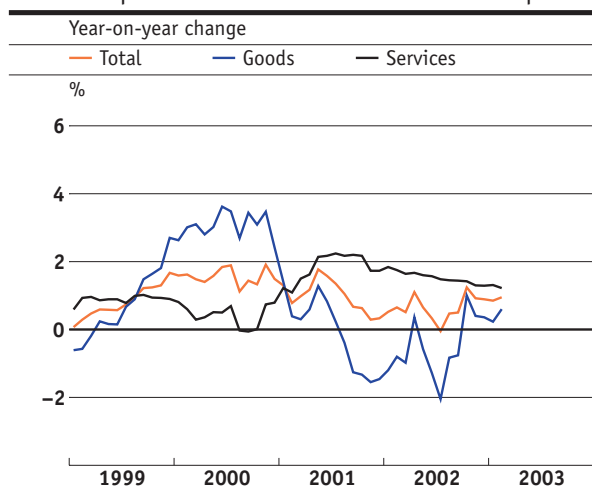
Slightly lower SNB figure for core inflation

Since inflation, measured by the national consumer price index, is subject to numerous short-term influences that tend to obscure the view of the general price trend, the National Bank computes a core inflation rate. This core inflation rate excludes, in any period, the 15% of goods with the highest annual inflation rate and the 15% of goods with the lowest annual inflation rate from the commodities basket of the consumer price index. The core inflation rate calculated in this way was an unchanged 0.9% in the period November-January, but dropped to 0.8% in February. This suggests that prices are still very stable. As inflation-dampening special effects were more or less cancelled out by inflationary effects, core inflation differed only slightly from the annual inflation rate reflected in the overall national index.

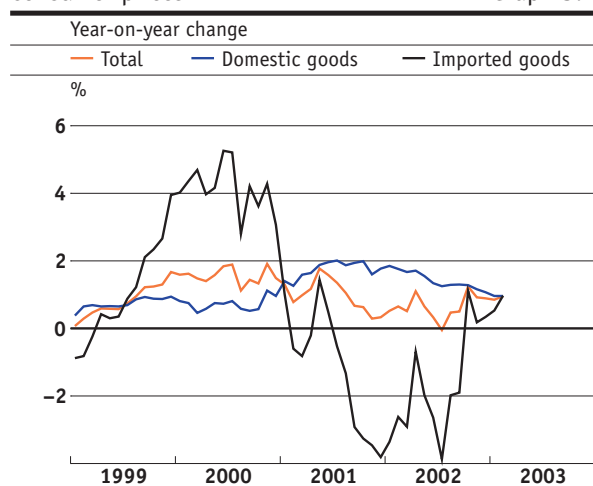
Decline in SFSO core inflation

Unlike the core inflation rate of the National Bank, the two core inflation rates calculated by the SFSO always exclude the same goods from the commodities basket in any period. In the case of core inflation 1, these are foodstuffs, beverages, tobacco, seasonal products, energy and fuel. Core inflation 2 additionally excludes products with administered prices. Both of the core inflation figures decreased from their November levels, falling to 0.7% and 0.4% respectively by February.

Consumer prices Graph 5.1



Consumer prices Graph 5.2



Graphs 5.1, 5.2:
Sources: SFSO

5.3 Prices of total supply

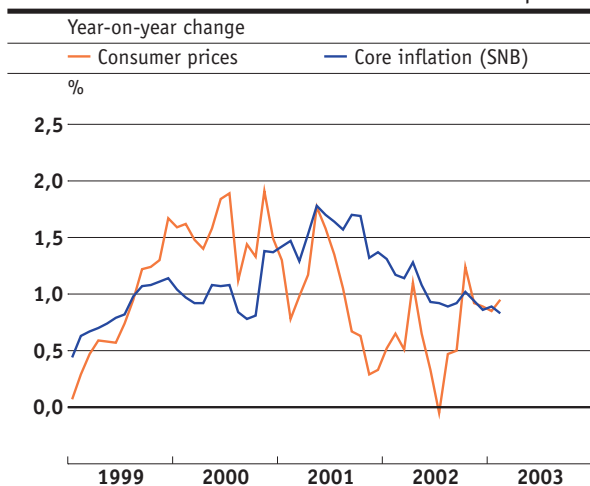
Total supply prices remain stable

The price level for total supply (index of producer and import prices) has remained virtually stable since mid-2002. Overall, therefore, these prices still did not generate any inflationary stimuli for the downstream consumer level. Whereas goods produced in Switzerland became slightly cheaper, prices for imported goods rose again.

Producer prices declined year-on-year, though somewhat more slowly than in mid-2002. By February they were 0.2% down from the year-back level. Prices for consumer goods and capital goods rose (by 1.1% and 0.3% respectively) while semi-manufactures became cheaper (-1.0%). Owing to statistical effects, commodity prices were 3.0% higher in February than they had been a year ago, even though they had fallen in the two preceding months.

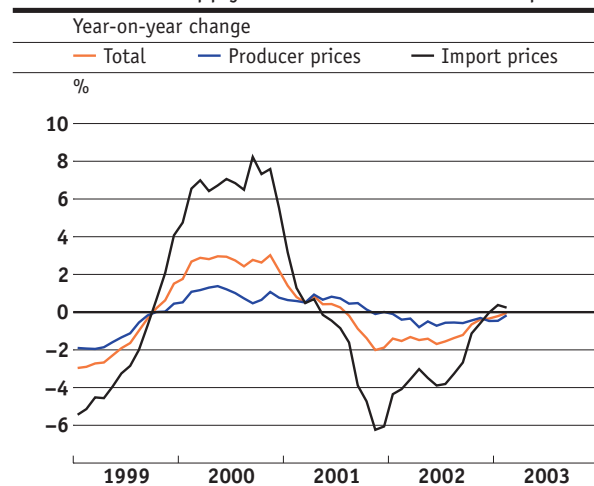
The price index for imported goods as at February 2003 was 0.2% over its year-back level. This rise was due mainly to consumer goods, which rose 1.3% year-on-year. Prices for commodities and semi-manufactures increased by 0.7% and 0.5% respectively. Capital goods prices continued to slide, moving down by 2.1% compared with the year-back period.

Core inflation Graph 5.3



Sources: SFSO, SNB

Prices of total supply Graph 5.4



6.1 International price development

Oil-related rise in import prices

Between end-November and end-February, the price of oil (Brent quality) rose by about USD 10 and at times topped USD 34 per barrel. In Swiss franc terms, the average oil price in February was 30% higher than a year earlier. This surge was due mainly to the worsening Iraq crisis: although OPEC had declared its willingness to make up output shortfalls in the event of war, the markets feared that supplies would become short. In mid-March, forward prices for the next three months were still indicating oil prices in excess of USD 30 per barrel. On the other hand, any inflationary stimuli emanating from other imported goods look set to remain weak owing to the sluggish international economy and the higher external value of the Swiss franc.

6.2 Price development in Switzerland

Low cost pressures

In the last few months, upward pressure on prices of domestic goods and services has eased further. Since production capacity is not fully utilised, it is unlikely to be increased in the near future. As the situation on the labour market will not improve until the second half of the year at the very least, salaries in particular will not generate any cost pressure. According to the salary survey conducted by UBS in November 2002, nominal salaries and wages are set to grow by 1.3% in 2003. With a projected inflation rate of 0.7% and an increase in labour productivity of around 1.5%, real unit wage costs should actually decrease this year. With competition remaining fierce, moreover, the scope for price increases remains limited.

Industry expects prices to stay flat

The results of the business climate tests conducted in industry by KOF/ETH indicate that inflationary pressure on commodities will remain low. A large majority of the industrial companies that focus on the domestic economy expects sales prices to remain steady or even to fall. At the same time, the vast majority of companies are predicting that purchase prices will remain stable.

Rents virtually static

Changes in residential rent levels play a key role in inflation forecasts, as they have a weighting of almost 20% in the commodities basket used to calculate the consumer price index. The quarterly rents survey in February showed that annual inflation in rentals had fallen from 0.5% to 0.3%, the lowest level since April 1999. The mortgage rate cuts effected in the second half of 2002 should be passed on to tenants in spring 2003, thus containing rent inflation. However, as dwellings are still in extremely short supply – especially in the Zurich and Lake Geneva regions – landlords should be able to raise rents on tenant changes or when letting out new property.

6.3 Inflation forecast for 2003–2005

At its quarterly monetary policy assessment of 20 March 2003, the National Bank published a new inflation forecast for the period 2003–2005. At the end of 2002, it had decided henceforth to publish an inflation forecast each quarter rather than only twice a year (in June and December) as previously. The 20 March inflation forecast is based on the assumption that the three-month Libor will remain steady at 0.25% over the next three years.

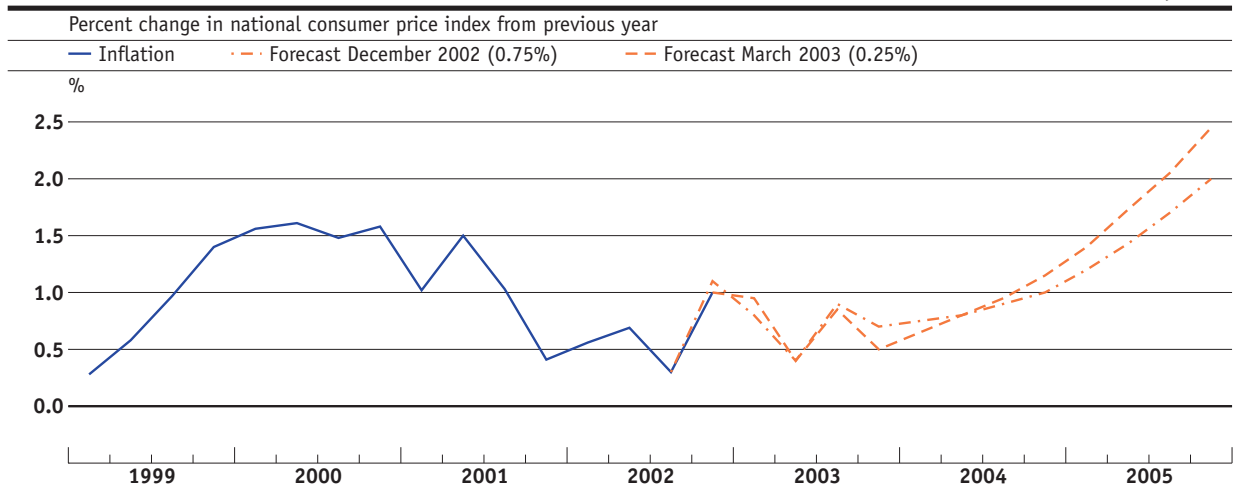
The National Bank is assuming that the economic climate in the United States will start to recover in the second half of 2003 and that the production potential of US industry will be reached again in 2004. An upswing in the EU, however, has been delayed, and growth is unlikely to exceed 2% until 2004. A further assumption underlying the forecast is that geopolitical concerns will keep the price of oil at around USD 30 per barrel for some time yet before it drops back to about USD 25.

The inflation forecast of March 2003 is shown alongside that of December 2002 in Graph 6.1. The new inflation forecast corresponds roughly to the December forecast up to mid-2004, even though monetary policy was eased again at the beginning of March. The average inflation rate is put at 0.7% for 2003, rising gently to 0.9% in 2004. In the near term, the delayed economic upswing and the cheaper dollar will be the main factors holding back price rises.

During 2005, inflation will accelerate, rising to 2.5% by the fourth quarter. The National Bank regards prices as being stable when the national consumer price index rises by less than 2% per annum. At the end of the forecasting horizon, therefore, inflation will exceed the level equated with price stability by the National Bank. This development can be ascribed to the fact that the National Bank – responding to growing concern about the business cycle – eased its monetary policy more than had been envisaged when the December 2002 forecast was prepared.

The National Bank feels that this pronounced loosening of monetary policy does not as yet pose any threat to price stability. It believes that it will have sufficient time to make adjustments to this policy, and that it can keep inflation within the price stability range.

Inflation forecast of December 2002 with Libor at 0.75% and of March 2003 with Libor at 0.25% Graph 6.1



7 Assessment of the economic situation from the regional vantage point

The bank offices of the National Bank are constantly in touch with a large number of enterprises from various sectors of the economy. Their reports, which contain the subjective evaluations of the enterprises, are an important additional source of information for assessing the economic situation. Below we summarise the main results of the talks held between November 2002 and February 2003 on the current and future economic situation.

7.1 Production

The majority of companies surveyed were still suffering from a low level of business, and continued to regard the economic situation as difficult. Overall, there were no signs of any general improvement or deterioration. At many companies, order intake stabilised at a low level.

Uncertainty about the future course of the economy was reflected in a reduced order volume and a trend towards shorter-term orders. Investments were cancelled or deferred, as most companies limited their capital spending to essential replacements and downsizing. Very few firms invested in expanding their capacity.

No clear trend is emerging for the current year: many of the companies surveyed are decidedly reticent about their expectations. Owing to slack business activity, competition has become fiercer. With margins being squeezed by pricing constraints, many companies have been compelled to lower their costs. The ongoing restructuring process is likely to exacerbate the employment situation. At the same time, however, it will improve companies' profitability.

Manufacturing

Export-driven manufacturing companies continued to be beset by the sluggish economic climate and the Swiss franc's high valuation, especially in relation to the dollar. Sales were again driven primarily by Asian business, with China emerging as the top market. In addition, there were growing signs of an upturn in demand from the US and eastern Europe (including Russia). By contrast, the continuing lull in demand from Germany remains a headache for many exporters. Fiercer competition from imports also made itself felt.

As in the previous period, capital goods manufacturers and suppliers of intermediate products were particularly hard hit. Although some producers benefited from a slight upturn in foreign demand, the majority of companies in the capital goods industry were still suffering from dwindling sales and falling prices. For this reason, many companies in the mechanical engineering and metalworking industries continued to report downturns in output and employment over the last three months. Most firms in the electronics and telecom sectors had to contend with very difficult operating conditions. Some of them, however, are guardedly optimistic about the coming year.

The situation for manufacturers of near-consumer products was mixed. Apart from a few niche products, companies in the textile, furniture and paper industries experienced a sharp downturn in sales in the last few months. Their assessment of the future outlook was correspondingly gloomy. By contrast, the current economic slowdown has had little or no impact on the pharmaceutical and foodstuff sectors, companies in the bio-engineering and medical technology fields, or the upmarket segment of the watchmaking industry.

Service sector and commerce

The majority of the service-sector companies surveyed have been complaining of sluggish business in the last few months. Sagging consumer sentiment has had a serious impact on the retail trade. Christmas business was disappointing at many locations, and turnover in January and February was below expectations despite the sales season. Spending on clothing and consumer durables fell significantly, while sales of luxury goods continued their decline. By contrast, demand for foodstuffs and other day-to-day products was buoyant. The demand shift away from expensive and towards lower-priced goods continued. This is reflected in a sharp fall-off in sales by specialist outlets and a rise in turnover at the major retail chains. Although aggressive pricing eroded these retailers' earnings, too, they are still planning to substantially increase their sales-floor areas.

The banking sector is still being hit by the shaky performance of the financial markets and the downturn in commission and trading income. Further workforce reductions are on the cards for this sector. Consulting firms in particular, as well as printing companies, have witnessed a steep decline in demand owing to the indifferent business climate.

The tourist sector got off to a good start to 2003. Thanks to good snow and weather conditions, hotels in the winter-sports regions enjoyed a healthy level of bookings in the first two months of the year, notwithstanding the very price-conscious behaviour of guests. City hotels also reported a satisfactory level of bookings by business travellers, though the slack economic trend does not augur well for the rest of the year.

Construction

Overall, the building industry's view of the business situation remained unremittingly pessimistic. Many projects are being deferred because of the uncertain economic outlook. The majority of building firms are faced with a declining order intake. Despite lower interest rates and reduced building costs, many segments of the residential construction sector have been hit by the low profitability of new-build projects. For investors and building firms alike, conversion and renovation work is currently more attractive. Although certain construction companies are benefiting from large transport-infrastructure projects, civil engineering has been hit by spending cuts in the public sector. Construction of office and industrial property is expected to taper off further in the current year. Owing to the excess capacity in the building sector, prices – especially in large-scale projects – have been pushed down dramatically. The earnings situation at many companies has worsened again. Based on the tenders situation, many companies are pessimistic about the outlook for 2003.

7.2 Labour market

The situation on the labour market has deteriorated further in the last few months. Many companies were no longer expecting any imminent or substantial recovery in output. For cost reasons, they have been compelled to cut back their workforces as short-time working proves insufficient as a means of bridging the gap. As staffing levels have not yet been fully adjusted, further dismissals are planned. Jobs are being cut in practically all sectors.

7.3 Prices and margins

Price competition has become stiffer in many sectors. The pressure on margins has been acutely felt, not only by industries exposed to international markets but also by construction and retailing. In order to boost their profitability, most companies have thus initiated rigorous cost management measures.

The role of the Swiss National Bank in the electronic payment system

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Introduction

A stable financial system is a key prerequisite for a country's economic performance. The two main pillars of a stable financial system are a healthy financial sector and a safe and efficient financial market infrastructure comprising stock exchanges and clearing and settlement systems for payments, securities and other financial instruments. Smooth functioning of electronic payment systems is of primary importance to the Swiss National Bank (SNB) because it needs these systems for the implementation of its monetary policy.

The first part of this article briefly highlights the economic significance of payments. The second part presents the main participants and systems of the Swiss payments infrastructure. The third part then discusses the reasons why safety and efficiency are the main objectives of the SNB in electronic payments. The fourth part describes the SNB's activities in the field of electronic payments and how it contributes to a safe and efficient financial market infrastructure. The fifth part elaborates on the proposal made as part of the revision of the National Bank Law that oversight of payment and securities settlement systems should be explicitly defined as one of the SNB's key tasks. Finally, the sixth part shows how the SNB informs the general public and the parties concerned about its objectives and its role in the field of electronic payments.

1 The economic significance of payments

Transactions in the real and financial sectors are the heart of any market economy. For instance, private individuals purchase goods and services, companies procure raw materials and semi-finished goods from other companies and pay wages to their employees, while investors manage their wealth by buying and selling securities. All of these transactions result in financial obligations that have to be met either immediately or at a later date, depending on the underlying agreement. Facilities that allow convenient and inexpensive settlement of these financial obligations are of great practical benefit to all sides and facilitate trade in goods, services and financial instruments.

In Switzerland, cash is commonly used to settle transactions between individuals, especially transactions involving relatively small amounts where there is personal contact between the parties involved. Notes and coins thus play a key role in the payments infrastructure. The Swiss National Bank has a statutory monopoly on the issue of bank notes, which it supplies to the economy through the banking system and the post office. The bank notes it issues meet high security and quality standards. The federal government has also appointed the SNB to supply coins. However, in transactions involving large sums of money or where there is no personal contact between the parties involved, electronic transfers are the norm. The total amount of cash transactions is thus far lower than the sum of electronic transactions.

The main payments turnover is triggered by transactions in the financial sector. The big economic significance of this sector in Switzerland means that massive amounts are transferred back and forth between banks every day. Payments equivalent to about half the country's annual GDP are handled daily. It is thus clear that problems in the settlement of these reciprocal obligations could easily have far-reaching implications for the financial system or even the entire economy. Consequently, a safe and smoothly functioning infrastructure for the flow of payments is in the interests of both the financial sector and the general public.

2 Electronic payment systems in Switzerland

Participants in electronic payment systems in Switzerland can basically be divided into three categories: the SNB, financial intermediaries (i. e. banks and Postfinance) and what are known as non-banks, i. e. companies and private individuals. Financial intermediaries channel most reciprocal payments through sight deposit accounts held at the SNB. Non-banks, which do not have direct access to accounts at the SNB, channel payments through bank accounts or a Postfinance account. In other words, companies and private individuals use balances held with banks or Postfinance to settle transactions, while banks use balances on their accounts at the SNB.

Payment systems (see Box 1) are used to process electronic payments. In terms of turnover, the most important payment system in Switzerland is the Swiss Interbank Clearing (SIC) system, which banks use for high-value payments and some retail payment transactions. High-value payments normally relate to foreign exchange transactions or money and capital market transactions, but also include transactions involving large amounts in the non-banking sector. The remaining payments by the corporate sector and private individuals are referred to as retail payments. The number of high-value payments is relatively low compared with the number of retail transactions, but the amounts involved are a good deal larger.

SIC settles payments via the banks' sight deposit accounts at the SNB. It is what is known as a real-time gross settlement system (RTGS), in other words, it undertakes irrevocable real-time settlement of individual payments, provided the bank placing the settlement order has sufficient funds at sight in its account at the SNB. The SNB does not operate SIC. Instead, it has delegated this task to Swiss Interbank Clearing Ltd, a private-sector company owned by the Swiss banks and Postfinance. Swiss Interbank Clearing Ltd is responsible for day-to-day operation and technical development of the system.

SIC is linked to SECOM, the securities settlement system run by SIS SegInterSettle AG. This allows settlement of securities transactions on the principle of delivery versus payment. In other words, securities are transferred in SECOM and payment is settled through SIC at the same time. This eliminates principal risk involved in securities transactions.

Since September 2002, foreign exchange transactions in seven major currencies, including the Swiss franc, may be settled via the Continuous Linked Settlement (CLS) system. CLS, which is operated by the US CLS Bank, is a payment system that allows principal risk to be eliminated by applying a payment versus payment settlement mechanism. Settlement of Swiss franc obligations in CLS is made possible by a remote access of CLS Bank to SIC.

To facilitate payment in euros within Switzerland and between Switzerland and the EU, the Swiss banks and Postfinance established the Swiss Euro Clearing Bank (SECB) in Frankfurt am Main, Germany. SECB operates the euroSIC system, which functions along similar lines to SIC and is also linked to the SECOM securities settlement system. However, euroSIC handles a far lower turnover than SIC.

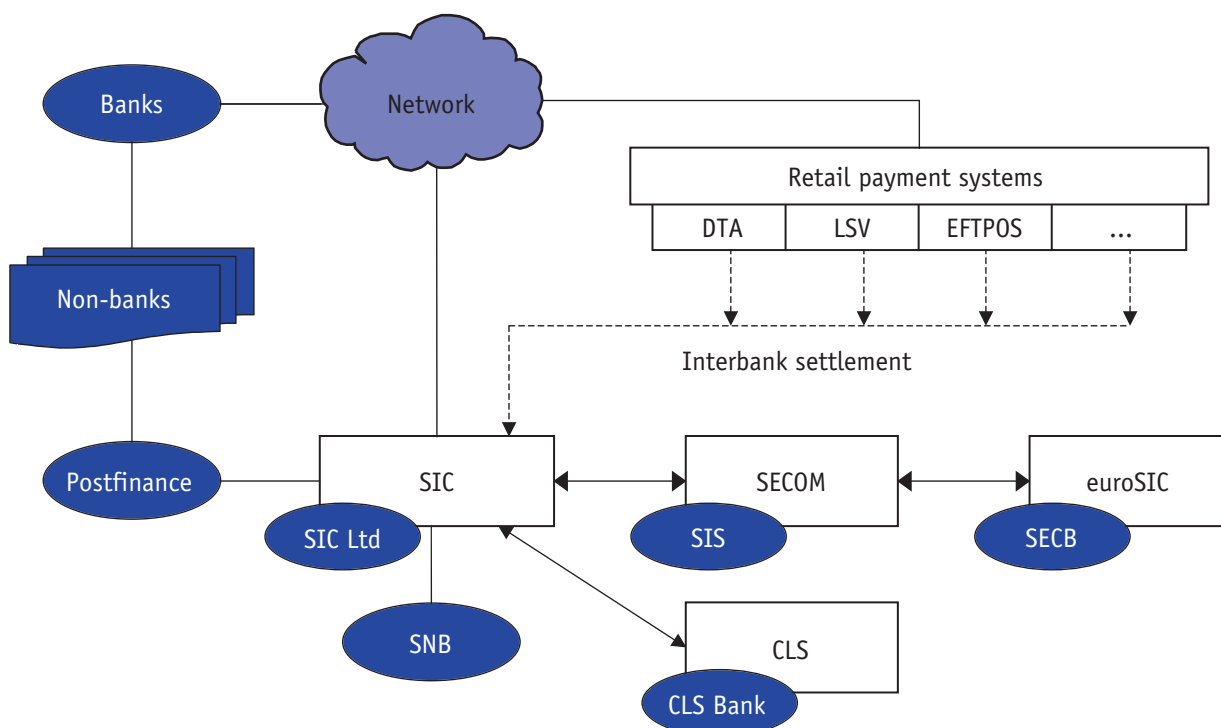
Financial intermediaries offer their clients a variety of non-cash payment instruments for retail payments. The methods used depend on various factors such as general acceptance, costs, safety and convenience. These instruments include credit and debit cards, cheques and pay-in slips. Other payment services include data carrier exchange, the banks' direct debit and electronic funds transfer (EFT-POS) systems, as well as Debit Direct from Postfinance. These systems enable companies and private individuals to transmit payments data electronically to their bank or to Postfinance.

The chief differences between the various payment instruments relate to how payments are triggered. However, they are all used to settle financial obligations by transferring funds from one account to another. If both parties hold an account with the same financial intermediary, the accounts concerned can simply be debited and credited as appropriate by the latter (in-house settlement). Where the parties have accounts with different financial institutions, an interbank transaction is necessary to transfer the funds from one to another. In such cases, the payment instructions may either be sent to the SIC system for direct settlement or channelled through an automated clearing house where they are collected, sorted and grouped by bank. The payments are then settled by SIC at predefined times once or twice a day. The central role played by SIC in Swiss payment transactions is evident from Fig. 1, which shows the main elements of the payment infrastructure in Switzerland.

In addition to the payment systems outlined above, which are used throughout the country, Switzerland has a number of single-purpose and limited-purpose card systems. With single-function cards, the system provider and service provider, i.e. the agent accepting the card, are identical. Examples are store cards and electronic phone cards. Limited-purpose systems are cards that can be used in a small number of stores (e.g. a chain) or at a certain location (e.g. at a shopping centre or in a specific tourist area).

Payment infrastructure in Switzerland

Figure 1



3 The objectives of the SNB

Safety and efficiency are the SNB's overriding objectives for electronic payment systems. These objectives are derived from the Bank's principal functions, which are monetary and foreign exchange policy. The interaction between the payment system, monetary policy and the stability of the financial system plays a major role in this.

In the implementation of its monetary policy, the SNB needs an efficient and safe payment system such as SIC. Disruption of the system could prevent monetary policy having the desired impact. At the same time, a stable financial system facilitates the achievement of monetary policy objectives. It enhances the SNB's room for manoeuvre and ensures rapid transmission of monetary policy to other sectors. For monetary policy reasons, the SNB therefore has a vested interest in strengthening the stability of the financial system wherever possible, for instance by promoting a safe and efficient infrastructure for the financial markets.

When considering the safety of a payment system, a distinction can be made between two aspects. Firstly, a payment system should have the technical and operational capability to ensure that it does not itself cause disruption to the financial system. Secondly, it should be designed to ensure that any disruption within the financial system, such as the insolvency of one party, does not spread to the other parties in an uncontrolled way.

The operational reliability of a system depends on a large number of components. First and foremost, these comprise the hardware and software used, the telecommunications network, the interfaces with those parties using the system, power supply and, last but not least, the staff employed. The technical integrity of a system depends primarily on control mechanisms regulating physical and electronic access to the system, e.g. the encryption technology used for data interchange. However, extremely high system availability and integrity are not sufficient. It is equally important to ensure that there are regularly tested back-up facilities and contingency plans to ensure that the system continues to operate in all circumstances.

To prevent the uncontrolled spread of failures in the financial system to other parties via the payment system, the latter needs to be placed on a sound legal basis and there should be clear rules and procedures for the settlement of transactions. One major principle is that once a payment order transmitted to the system has undergone all risk controls and other checks, it can no longer be reversed (irrevocable settlement).

All payment systems should meet minimum standards with regard to the safety aspects mentioned above. However, with increasing importance of a specific payment system for the economy and the financial system, the safety precautions need to be stepped up. Safety is particularly important for payment infrastructures that are of systemic significance. These are systems where internal disruption or financial difficulties on the part of one party could have a knock-on effect on other parties or even wide sections of the financial system (systemic risk). Systemically important payment systems should therefore adopt the ten Core Principles set out by the Bank for International Settlements (BIS; see Box 2).

The importance of a payment system for the financial system depends primarily on the turnover and the type of payments it handles. Infrastructures used for the settlement of high-value transactions tend to be particularly important to the economic system as a whole. By contrast, infrastructures that only handle small amounts or retail transactions represent little or no systemic risk. Whether or not an alternative payment system exists through which payments could be settled in case of need is also relevant for the assessment of a payment system's economic significance.

Alongside the safety of payment systems, the SNB is interested in their efficiency. A payment infrastructure can be considered efficient if it offers users the required functionality and the necessary safety at the lowest possible cost and ensures that resources are not squandered. As in other areas of the economy, the resources required for settlement of payments should be minimised. In this respect, it is particularly important to consider the efficiency of the infrastructure as a whole, rather than the efficiency of individual systems.

A safe and efficient infrastructure for the flow of payments is not merely desirable for the SNB; it is also in the interests of all parties affected by the system. Nevertheless, free market forces are not always sufficient to achieve the goals of safety and efficiency. This is because the market for payment services includes many factors that could lead to market failure, and thus to economically sub-optimal operation, if the regulatory framework is inadequate.

This is particularly evident in the case of systemically important payment systems. The probability of a systemic chain reaction can be reduced by taking suitable action, such as improving safety precautions and risk management. However, such measures raise operating costs. If the design of the system is left entirely to the direct users, they are unlikely to pay much if any attention to the negative externalities of a systemic crisis when weighing up the cost/benefit ratio of reducing risks. Negative externalities include all costs that are not borne directly by the originator of the crisis. As a result, in comparison with the economic optimum, a system selected entirely on the basis of market forces entails higher risks and is more vulnerable to systemic crises.

The retail payments sector also involves a number of factors that can result in a situation that is economically sub-optimal. Possible reasons for shortcomings in this market segment include market entry barriers such as high fixed costs, economies of scale and scope, and network effects. One consequence may be an imperfect and uncompetitive market structure with sub-optimal rates of innovation. The services required by companies and private individuals may not be available, or may be overpriced. Accordingly, ensuring sufficient competition and consumer protection are justified concerns in the retail segment.

These examples show that there is a potential for market failures in the market for payment services. In the case of systemically important payment systems, this is primarily manifested by inadequate levels of safety, while in the retail market, lack of efficiency is often the problem. Regulatory measures in the public sector – including the SNB – are therefore justified if they improve market performance. It goes without saying that the costs of regulation must not exceed the user benefits of regulation.

4 The SNB's policy principles

The statutory basis for the SNB's activities in the field of electronic payments is the current National Bank Law, which specifies that the Bank's role includes facilitating payment transactions. There are essentially two ways in which the SNB can help promote a safe and efficient payment infrastructure. Firstly, it can offer certain payment services itself. Secondly, it can take suitable action to ensure that the systems provided by private-sector operators are as safe and efficient as possible.

The SNB's strategy is based on the principle of leaving the private sector to operate payment systems and only acting as an operator if the private sector does not provide a suitable infrastructure. Given this market-based approach, the SNB has two chief tasks in electronic payments. Both functions contribute to the stability and, to a certain extent, to the efficiency of the financial system.

The first main task is the provision of liquidity for settling payments between financial intermediaries. By this, the SNB makes a major contribution to the stability of the financial system. The advantage of using central bank money for payments is that, in the final analysis, the recipient of the funds has a claim on the SNB in the form of the balance held on a sight deposit account. Unlike claims on private-sector banks, there are no credit or liquidity risks attached to claims on the SNB because its monopoly on the creation of money means that it can always meet its obligations in full. A system that settles payments via balances held on accounts at the central bank thus implies lower financial risks to the parties involved than an identical system where a different means of payment is used to settle reciprocal commitments. Consequently, the use of central bank money is one of the Core Principles recommended for systemically important payment systems (see Box 2, Core Principle VI).

In the past, the SNB has also encouraged less important payment systems to use central bank money. Consequently, all retail payment systems used by the banks are now channelled via SIC. However, this development was based on efficiency rather than risk considerations. By using a single payment system for all interbank payments, the banks are able to pool their liquidity and thus reduce the cost of liquidity management.

The second main task of the SNB in electronic payments is to oversee payment systems. Like other central banks, the SNB defines oversight as all of its efforts to influence the rules and architecture of a payment system. The SNB pays special attention to systemically important systems, where negative externalities can be particularly significant. The SNB's role in overseeing such systems is closely aligned to generally accepted international standards, especially the ten Core Principles issued by the BIS. The SNB exercises its influence over such systems and their operators primarily through moral suasion rather than formal rulings.

Given the turnover and type of payments handled by SIC, the SNB concentrates primarily on this system. Problems in retail systems such as data carrier exchange, direct debit processes and the payments systems used by Postfinance may inconvenience a large number of customers, but they are hardly likely to pose a threat to the stability of the financial system as a whole. The same applies to the euroSIC system. In terms of systemic risk, single-purpose and limited-purpose card systems also tend to be irrelevant. The SNB thus intervenes to a far lesser extent in the design of these less significant payment systems than it does in the case of SIC.

The oversight of SIC is made easier by the fact that payments are settled through accounts held at the SNB. An agreement between the SNB and the operating company, Swiss Interbank Clearing Ltd, sets out their reciprocal rights and obligations. This agreement ensures that the SNB has far-reaching powers of oversight. Additional agreements between the operating company and the parties that use the system specify that participants must observe the rules and procedures of the system at all times. These are described in detail in a user manual and technical directives.

The SNB is also represented on the Board of Directors of Swiss Interbank Clearing Ltd. All decisions, especially those relating to the structure of the system, require the approval of the SNB. This is designed to prevent the company taking decisions that are against the public interest. In addition, the SNB has representatives on a number of other interbank bodies that include representatives of the users of the system (banks and Postfinance) and Swiss Interbank Clearing Ltd. These bodies deal mainly with operational issues relating to payment transfers. Insofar as regulatory issues are affected, the SNB outlines its intentions to these committees very early on. In this way, it helps minimise the operator's regulatory expenses.

The increasing globalisation of payment transactions requires intensive international cooperation. The SNB thus works closely with the main regulators of cross-border systems such as CLS. It also maintains bilateral and multilateral contacts with other central banks. These relationships play an important role in improving the understanding of relevant issues and thus help enhance policy on payment systems. By participating in international working groups organised by the BIS, the SNB is involved in drafting specialist reports and international standards, and thereby has the opportunity for input.

In the area of retail payment systems, where efficiency has top priority, the SNB endeavours to take suitable action to counteract market inefficiencies and works towards economically meaningful solutions. For instance, in the event of a conflict of interests it offers its services as an impartial arbitrator. Issues relating to the standardisation of products and interoperability or crosslinking of systems are of particular importance in this sector. However, it should be stressed that, as a matter of principle, the SNB does not intervene directly in decisions taken by operators.

The SNB's activities in the retail payments sector are geared to areas in which it has a comparative advantage over other public and private-sector institutions. Ensuring adequate competition and consumer protection, in particular, are not among its core competencies. Federal agencies such as the Competition Commission and the price supervisor, and private-sector organisations such as consumer protection associations, are better-placed to protect such interests.

5 The new National Bank Law

The above description of the activities of the SNB shows that its role in overseeing the payments infrastructure is based either on private contracts with the system operators or their goodwill. This arrangement has proven effective in the past, especially for SIC, which is particularly significant from a systemic viewpoint. Nevertheless, the SNB welcomes the proposal made as part of the revision of the National Bank Law that oversight of payment and securities settlement systems should be explicitly defined as one of its key tasks. Subject to approval by parliament, the new Law is expected to come into effect in 2004.

There are various reasons for providing a statutory basis for the oversight of payment systems. Firstly, it is possible that, in future, Switzerland could have systemically important payment systems that do not use central bank money. This would doubtless make it more difficult for the SNB to influence the structure of the system than has been the case with SIC in the past. Consequently, the draft revision of the National Bank Law provides for the SNB to oversee payment systems, regardless of whether they use central bank money or not. At the same time, statutory regulation reflects the growing importance of oversight of payment systems as part of general efforts to enhance the stability of the financial system. This trend is not confined to Switzerland. Other jurisdictions such as Australia, Canada and the European Union have also put the oversight of their payment systems on a statutory footing in recent years.

In addition to overseeing payment systems, under the new law the SNB will be responsible for the oversight of clearing and settlement systems used for securities and other financial instruments (referred to collectively as securities settlement systems in the subsequent text). If, due to its banking status, the operator of such a system is also subject to supervision by the Swiss Federal Banking Commission (SFBC), the supervisory function will be shared

between the SNB and the SFBC. The SNB will be responsible for the system element and the SFBC for the institutional element. Oversight of systems and supervision of institutions are thus essentially complementary activities, both of which contribute to the stability of the financial system. Nevertheless, the supervisory functions of the SNB and SFBC are closely linked, so efficient implementation of this role requires a coordinated approach by both bodies. If deemed necessary to ensure effective oversight, the SNB may also cooperate with foreign supervisory or oversight authorities. The information that may be provided to foreign authorities is limited to information of direct relevance to system oversight. An exchange of information on system participants or even their customers is inadmissible.

The revised National Bank Law formally empowers the SNB to set requirements for payment and securities settlement systems which could potentially destabilise the financial system. This enables it to minimise systemic risk and to reduce disruptions to the payment system, which would hinder the implementation of monetary policy. A three-step approach is proposed. In the first step, operators of payment systems would be required to provide statistical data. This would give the SNB an overview of the payment systems available in Switzerland and the extent to which different types of means of payment are used. This information would enable it to exclude smaller payment systems from its close oversight from the outset. The second step comprises extended disclosure requirements and would apply to both securities settlement systems and payment systems where a systemic risk cannot be ruled out a priori. Extensive information on such systems is required to give the SNB the certainty it needs to decide whether or not a specific system is of systemic importance. Finally, in the third step the SNB can impose qualitative minimum requirements on systems that could jeopardise

the stability of the financial system. These relate to organisational principles, the precautions required to ensure the safe operation of the system and contingency plans if parties using the system encounter fulfilment problems. Moreover, the SNB would be able to examine the terms of business, means of payment used and conditions of admission to the system. The draft legislation proposes sanctions under administrative law for operators who fail to meet these minimum requirements. For example, the operator could be denied access to its account at the SNB or the SNB could issue a public warning on the shortcomings of the system. However, other sanctions could only be imposed by the authorities directly responsible for supervising the operator and parties using the system in Switzerland and abroad, rather than by the SNB.

6 Communication

The SNB regards the publicising of its objectives, role and policy principles as key to actually achieving its goals. It therefore informs the parties concerned and, to some extent, the general public of its intentions and of any major changes and developments in the field of payments infrastructure.

Transparent information on the goals and activities of the SNB is particularly important for system operators and payment service providers. By disclosing its objectives, the SNB enables the private sector to predict business conditions with sufficient certainty. This is a basic requirement for private-sector investment in ongoing improvements to the payment infrastructure. Regulatory changes affecting the operators and users of payment systems are normally drawn up by the SNB in consultation with the parties concerned. This ensures that they have plenty of time to prepare for the changes.

The SNB also provides regular information to the general public on its goals and activities in the field of payment transactions and payment systems. The information available on these topics is being expanded through more efficient use of the present communication channels. The central element in communication with interested parties is the SNB's website (www.snb.ch), which provides extensive information on basic issues and current developments in this field. The information available on the Internet is supplemented by official papers, press releases and regular and ad hoc publications. In its official papers the SNB mainly provides information on its objectives and activities. Information on major changes and developments is given and commented on in press releases, while the annual report summarises events over the past year. More extensive background information on policy principles or relevant developments in the field of payments is published in newspaper articles and academic journals. Last but not least, the present publication is designed to raise public awareness of issues relating to payments transactions and the role of the SNB.

A payment system is a central facility to settle financial claims and obligations between various parties, normally banks. It is based on a uniform set of rules and procedures and comprises three elements. The first is the technical infrastructure, i.e. the communication systems and hardware and software components required by the system operator and participants to exchange data and settle transactions. Secondly, it needs a system of accounts where the financial assets to be transferred are held and to which they can be transferred. In practice, these are account-based claims on the central bank or another financial intermediary who acts as a settlement agent. The third element comprises the rules used to exchange information and transfer funds from one account to another. Clear rules enable users to assess the risks involved in the system. Detailed information on the procedures used to settle payments also allows standardisation and automation of the system and thus minimises costs.

The exchange of payment-related information between system participants and any regulations under which payments are settled on a bilateral or multilateral basis is known as clearing. By contrast, settlement comprises the actual discharge of an obligation, i.e. by debiting the amount from the payee's account and crediting it to the recipient's account. Systems used only for clearing are often referred to as payment systems. For instance, the data carrier exchange (DTA) facility is purely a clearing system, because the actual settlement of inter-bank obligations is carried out by a different system, SIC.

In January 2001 the Committee on Payment and Settlement Systems (CPSS) of the Bank of International Settlements issued ten Core Principles for systemically important payment systems. The CPSS is a forum for the central banks of the G10 countries. Its role is to monitor and analyse developments in payment and securities settlement systems and coordinate the oversight of payment systems. The Core Principles are summarised below. The full report is available at www.bis.org.

- I. The system should have a well-founded legal basis under all relevant jurisdictions.
- II. The system's rules and procedures should enable participants to have a clear understanding of the system's impact on each of the financial risks they incur through participation in it.
- III. The system should have clearly defined procedures for the management of credit risks and liquidity risks, which specify the respective responsibilities of the system operator and the participants and which provide appropriate incentives to manage and contain those risks.
- IV.* The system should provide prompt final settlement on the day of value, preferably during the day and at a minimum at the end of the day.

- V.* A system in which multilateral netting takes place should, at a minimum, be capable of ensuring the timely completion of daily settlement in the event of an inability to settle by the participant with the largest single settlement obligation.
- VI. Assets used for settlement should preferably be a claim on the central bank; where other assets are used, they should carry little or no credit risk and little or no liquidity risk.
- VII. The system should ensure a high degree of security and operational reliability and should have contingency arrangements for timely completion of daily processing.
- VIII. The system should provide a means of making payments which is practical for its users and efficient for the economy.
- IX. The system should have objective and publicly disclosed criteria for participation, which permit fair and open access.
- X. The system's governance arrangements should be effective, accountable and transparent.

* Systems should seek to exceed the minima included in these two Core Principles.

Risks in payment systems

Box 3:

The Bank for International Settlements distinguishes between the following types of risks in payment systems:

Credit risk: the risk that a counterparty will be unable to fully meet its financial obligations either on the due date or at a later date.

Principal risk: the risk that a party within the system will be unable to fully meet its financial obligations under a securities or foreign exchange transaction either on the due date or at a later date, even though the other party meets its obligation on time and in full (specific type of credit risk).

Liquidity risk: the risk that a counterparty within the system will have insufficient funds to meet financial obligations on the due date, although it may be able to do so at some time in the future.

Legal risk: the risk that a poor legal framework or legal uncertainties will cause or exacerbate credit or liquidity risks.

Operational risk: the risk that operational factors such as technical malfunctions or human error will cause or exacerbate credit or liquidity risks.

Systemic risk: the risk that the failure of one of the participants to meet its obligations, or a disruption in the system itself, will cause other system participants or financial institutions to be unable to meet their obligations when due. Such a failure may cause significant liquidity or credit problems and, as a result, might threaten the stability of financial markets or even of the economy as a whole.

Swiss Interbank Clearing System (SIC)

SIC is a real-time system used by the banks and Postfinance to settle major payments and some retail payments. The SNB has delegated operation of this system to Swiss Interbank Clearing Ltd.

euroSIC

euroSIC is a real-time system used by banks and Postfinance to settle domestic payment transactions in euros. A link to TARGET, the high-volume payment system of the EU, allows settlement of cross-border payments in euros to and from Switzerland.

Data carrier exchange (DTA)

This is an electronic payment system offered by banks to private individuals and companies. Payment instructions are given via online file transmission or by sending a data carrier to the bank.

Direct debit (LSV)

The direct debit system is used primarily for regular payments. The payee authorises the recipient to debit the amount from his/her bank account. To use this service, both parties must have a bank account.

Electronic payment order (EZAG)

This is an electronic payment facility offered by Postfinance to companies and private individuals with Postfinance accounts. Payment instructions are transmitted via the internet or an electronic data interchange system.

Debit Direct (DD)

The Postfinance direct debit system is suitable for regular payments. The payee authorises the recipient to charge the amount due directly to his/her Postfinance account. To use this service, both parties must have an account with Postfinance.

Debit cards

Debit cards are mainly used in the retail trade. Customers trigger the immediate debit of the amount to be paid from their account via a terminal operated by the retailer (EFT-POS). Debit cards can normally also be used to withdraw cash from ATMs. The most common debit cards in Switzerland are ec/Maestro and Postcard.

Credit cards

Credit cards are mainly used in the retail sector, but may also be used for telephone orders and electronic transactions via the Internet. They enable the purchaser to pay for goods and services at a later date. The most common credit cards in Switzerland are Visa and Eurocard/Mastercard.

The main payment systems used in Switzerland
Transaction volumes and turnover in 2002

Table 1

System	Transaction volume	Turnover
	in million	in billion Swiss francs
SIC	177,0	44,750,2
euroSIC ¹	1,6	438,6
DTA	67,1	288,6
LSV	36,1	67,7
EZAG (Postfinance)	293,6	1,047,1
Debit Direct (Postfinance)	13,9	5,0
Debit cards (ec/Maestro, Postcard)	226,2	38,1
Credit cards (AMEX, ECA/MC, Diners, Visa)	81,7	15,3

1 Turnover in billion euros

Chronicle of monetary events

Lowering of the target range for the three-month Libor rate

On 6 March 2003, the Swiss National Bank lowered the target range for the three-month Libor rate by half a percentage point to 0%–0.75%. The move was intended to counter a tightening of the monetary conditions that would arise from an appreciation of the Swiss franc.

Total revision of the National Bank Law

Initial consideration of Message and draft law in the Council of States

On 18 and 19 March 2003, the Council of States dealt with the Federal Council's Message and draft for a total revision of the National Bank Law (NBL; cf. Quarterly Bulletin 2/2002, p. 75). The draft law met with a positive reception in the small Chamber. In particular, the proposed National Bank mandate was accepted unchanged. The opinion of the Council of States only differed from the Federal Council's bill on two issues: firstly, it decided that postal account balances are to be counted as part of the minimum reserve requirements. Secondly, the Bank Council's right to make proposals for the election of members of the Governing Board and their deputies – appointments that are made by the Federal Council – was replaced by the right of consultation. The draft of the revision will now be submitted to the National Council.

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