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Contents

Monetary policy report

Report to the attention of the Governing Board of the Swiss National Bank for its quarterly assessment of March 2012.

This report is based primarily on the data and information available as at 15 March 2012.

Monetary policy report

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About this report

The Swiss National Bank (SNB) has a statutory mandate to pursue a monetary policy serving the interests of the country as a whole. It ensures price stability while taking due account of economic developments.

It is a particular concern of the SNB that its monetary policy be understood by a wider public. Moreover, it is obliged by law to inform regularly of its policy and to make its intentions known. This monetary policy report performs both of these tasks. It describes economic and monetary developments in Switzerland and explains the inflation forecast. It shows how the SNB views the economic situation and the implications for monetary policy it draws from this assessment.

Sections 2–5 of the present report were drawn up for the Governing Board's assessment of March 2012. Section 1 ('Monetary policy decision of 15 March 2012') is an excerpt from the press release published following the monetary policy assessment.

Unless otherwise stated, all rates of change from the previous period are based on seasonally adjusted data and are annualised.

1 Monetary policy decision of 15 March 2012

The Swiss National Bank (SNB) will continue to enforce the minimum exchange rate of CHF 1.20 per euro with the utmost determination. It is prepared to buy foreign currency in unlimited quantities for this purpose. The target range for the three-month Libor will remain unchanged at 0.0–0.25%. The SNB will continue to maintain liquidity on the money market at an exceptionally high level.

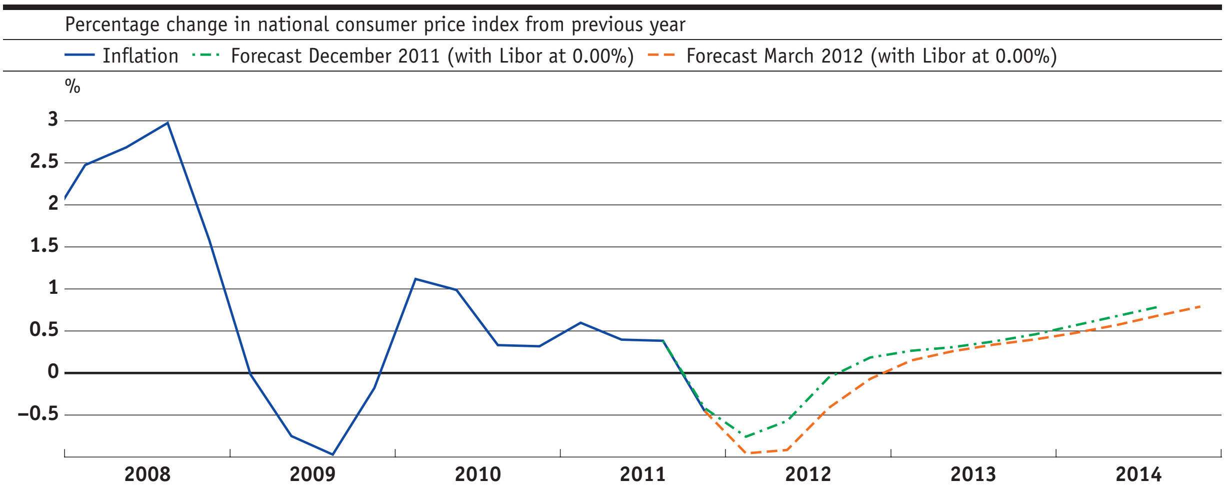
Even at the current rate, the Swiss franc is still high. In the foreseeable future, there is no risk of inflation in Switzerland. Compared to December, the inflation forecast has even fallen further. If developments in the international economy are worse than foreseen, or if the Swiss franc does not weaken further, as expected, downside risks for price stability could re-emerge. The SNB stands ready to take further measures at any time if the economic outlook and the risk of deflation so require.

Developments in the global economy are mixed. While growth in the US was surprisingly positive in the fourth quarter, GDP fell in the euro area and Japan. In Switzerland, growth has slowed significantly over the course of the past year. Added value declined in the fourth quarter in industries affected by exchange rate movements. While the high value of the Swiss franc continues to present enormous challenges to the economy, the minimum exchange rate is having an impact. It has reduced exchange rate volatility and given business leaders a better basis for planning. There are growing indications that Switzerland's economy is stabilising. For 2012, the SNB is now forecasting moderate growth, at close to 1%.

The situation on the financial markets has eased somewhat recently. Uncertainty remains very high, however. It is unclear whether the advances in solving the European sovereign debt crisis will succeed in defusing the situation permanently. Moreover, there is a risk that geopolitical tensions will lead to a further rise in the price of oil. On the Swiss mortgage and real estate market for residential property there are growing signs of imbalances. Should these imbalances increase further, this could lead to considerable risks to financial stability.

The SNB's conditional inflation forecast, which is based on the assumption of a three-month Libor of 0.0%, has been adjusted downwards once again compared to that of December (cf. chart 1.1). In the short term, inflation will move further into negative territory. Last summer's appreciation of the Swiss franc had a stronger dampening effect on prices than anticipated. In the longer term, inflation will be lowered by the worsening growth outlook for the euro area and the continuing high valuation of the Swiss franc. For 2012, the forecast shows an inflation rate of –0.6%. For 2013, the SNB is expecting inflation of 0.3% and for 2014, of 0.6%.

Chart 1.1
Conditional inflation forecast of December 2011 and of March 2012



Source: SNB

Observed inflation in March 2012 Table 1.1

	2008				2009				2010				2011				2009	2010	2011
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
Inflation	2.5	2.7	3.0	1.6	0.0	−0.7	−1.0	−0.2	1.1	1.0	0.3	0.3	0.6	0.4	0.4	−0.5	−0.5	0.7	0.2

Conditional inflation forecast of December 2011 with Libor at 0.00% and of March 2012 with Libor at 0.00%

	2011				2012				2013				2014				2012	2013	2014
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
Forecast December 2011, Libor at 0.00%				−0.4	−0.8	−0.6	−0.1	0.2	0.3	0.3	0.4	0.5	0.6	0.7	0.8		−0.3	0.4	
Forecast March 2012, Libor at 0.00%					−1.0	−0.9	−0.4	−0.1	0.1	0.3	0.3	0.4	0.5	0.6	0.7	0.8	−0.6	0.3	0.6

Source: SNB

Monetary policy strategy at the SNB

The SNB has a statutory mandate to ensure price stability while taking due account of economic developments.

The SNB has specified the way in which it exercises this mandate in a three-part monetary policy strategy. First, it regards prices as stable when the national consumer price index (CPI) rises by less than 2% per annum. This allows it to take account of the fact that the CPI slightly overstates actual inflation. At the same time, it allows inflation to fluctuate somewhat with the economic cycle. Second, the SNB summarises its assessment of the situation and of the need for monetary policy action in a quarterly inflation forecast. This forecast, which is based on the assumption of a constant short-term interest rate, shows how the SNB expects the CPI to move over the next three years. Third, the SNB sets its operational goal in the form of a target range for the three-month Swiss franc Libor. In addition, a minimum exchange rate against the euro is currently in place.

2 Global economic environment

Developments in the global economy were mixed in the fourth quarter. GDP growth in the US was stronger than in the previous quarter, which came as a positive surprise. Output in Japan and the euro area, on the other hand, slowed. With regard to emerging economies, robust growth in China and Russia stood in contrast to weaker results in India and Brazil, and in smaller Asian economies.

The SNB has once again revised downwards its assumptions for economic growth in the euro area. It also anticipates lower growth in the global economy in 2012 than it did in December.

Despite the easing of volatility in the financial markets, uncertainty about the future outlook for the global economy remains high. It is not clear whether advances in resolving the European sovereign debt crisis will succeed in defusing the situation permanently. The risks for the international financial system and the real economy are still considerable. Moreover, further geopolitical tension could lead to increased volatility in crude oil prices.

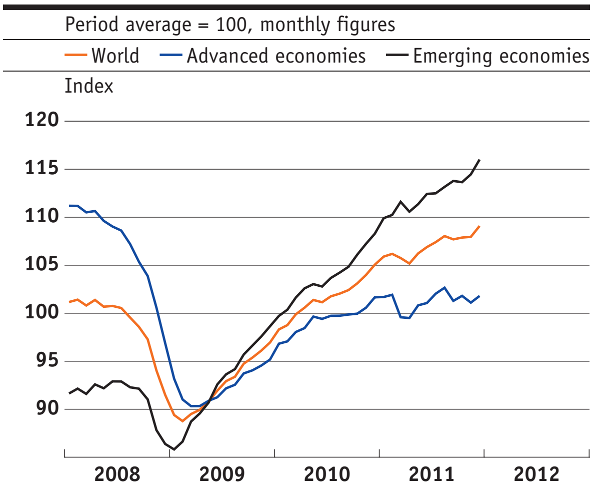
2.1 International financial and commodity markets

Since the monetary policy assessment in mid-December, the situation on the financial markets has eased. Reasons for this include positive economic news from the US, the copious amounts of liquidity provided to the markets by central banks around the world, reform efforts in the euro area, and the agreement among euro area member states on a further rescue package for Greece.

Equity markets around the world posted considerable gains, while uncertainty – as measured by volatility indices – decreased (cf. chart 2.3). By introducing three-year refinancing operations, the European Central Bank (ECB) contributed to reducing credit and liquidity risks. For the most part, the yield premium on the government bonds of certain euro area member countries over German government bond yields declined. On the foreign exchange markets, the exchange rates of the major currencies stabilised; from mid-January onwards, on a trade-weighted basis, the euro even strengthened again slightly (cf. chart 2.4). Commodity prices reacted to robust global economic data and again trended marginally upwards, while energy prices received additional stimulus as a result of geopolitical concerns, notably Iran's nuclear programme (cf. chart 2.5).

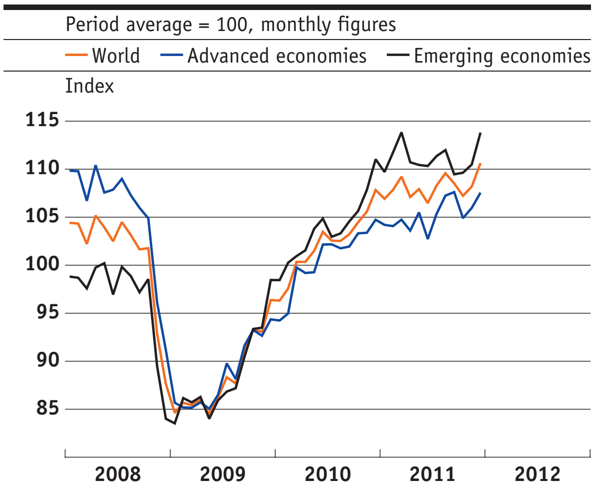
The SNB's forecasts are based on assumptions about the oil price and the dollar/euro exchange rate; over the forecast horizon it is assuming an oil price for Brent crude of USD 110 per barrel, and an exchange rate of USD 1.29 to the euro.

Chart 2.1
Global industrial production



Sources: Netherlands Bureau for Economic Policy Analysis (CPB), Thomson Financial Datastream

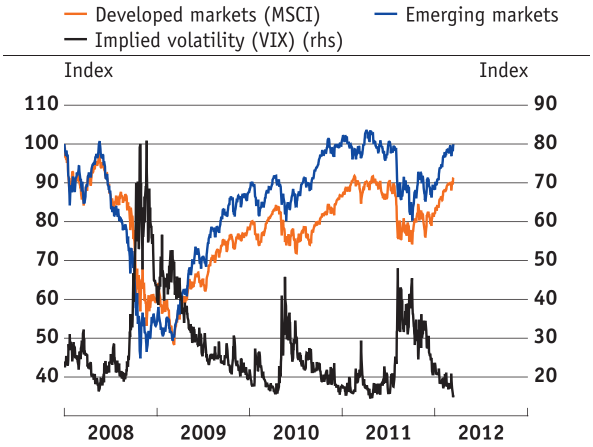
Chart 2.2
Global exports



Sources: CPB, Thomson Financial Datastream

Chart 2.3
Stock markets

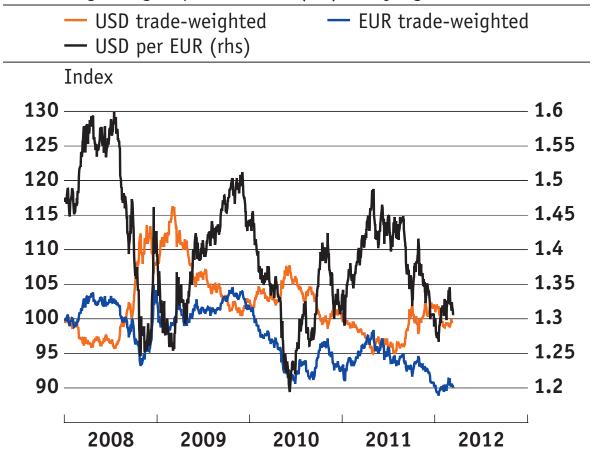
Beginning of period = 100 (lhs), daily figures



Sources: Reuters, Thomson Financial Datastream

Chart 2.4
Exchange rates

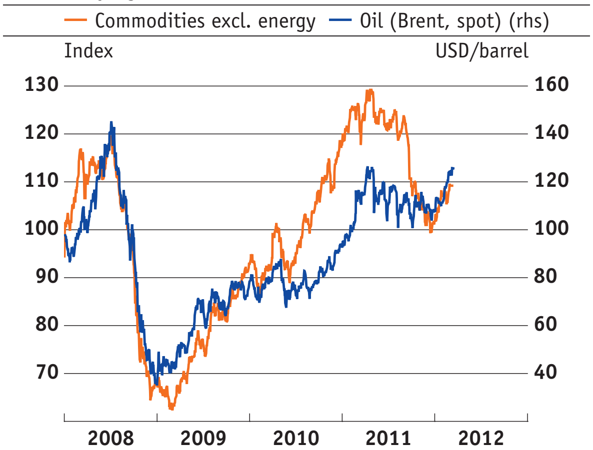
Beginning of period = 100 (lhs), daily figures



Sources: Reuters, Thomson Financial Datastream

Chart 2.5
Commodity prices

Daily figures



Sources: Reuters, Thomson Financial Datastream

2.2 United States

With fourth-quarter growth of 3.0%, US GDP expanded above potential for the first time in a year. Employment also picked up, although it remained significantly below its pre-crisis level at the end of 2007. For 2011 as a whole, GDP grew by 1.7%. Per capita GDP was still around 2.5% below the level in 2007.

Growth prospects remain moderate. Activity in manufacturing has revived somewhat, and most indicators for domestic demand and employment have trended upwards. The sharp decline in real estate prices continues to weigh on household budgets, however, and growth in consumer expenditure will likely remain muted in the coming quarters. Furthermore, the impending fiscal consolidation measures are dampening growth prospects. An additional cause of forecast uncertainty continues to be the European sovereign debt crisis. On the back of surprisingly positive data at the turn of 2011/2012, the SNB has adjusted its GDP forecast for the US in 2012 slightly upwards, to 2.2%.

Consumer price inflation decreased to 2.9% in February (cf. chart 2.10). Core inflation, by contrast, remained at its long-term average of 2.2% (cf. chart 2.11). Due to base effects, the annual inflation rate should continue to decline over the next few months, despite rising energy prices. The ongoing high level of unemployment should ensure that wage growth and upward pressure on prices remain low for the medium term.

The Federal Reserve maintained its expansionary monetary policy. It left the target range for the federal funds rate at 0.0–0.25%, and announced in January that, in view of the economic outlook, exceptionally low levels for the federal funds rate were warranted until at least the end of 2014. Furthermore, it began as planned to extend the average maturity of its holdings of US government securities in order to reduce long-term interest rates and thereby underpin economic recovery. It also announced, for the first time, a long-term inflation target, which was set at 2%.

2.3 Euro area

In the fourth quarter of 2011, for the first time in two and a half years, GDP contracted in the euro area (–1.3%). The average growth for 2011 as a whole was 1.4%. With the exception of France, all of the major euro area economies registered a GDP downturn in the fourth quarter. In Portugal and Greece, the recession deepened. The economic slowdown in the euro area affected all demand components, with private households' and companies' loss of confidence exacerbating the fall in domestic demand. Exports also declined. The rate of unemployment continued to climb, reaching 10.7% in January.

The economic outlook for the euro area remains highly uncertain. Indicators point to a mild recession. Business confidence was enhanced somewhat by, in particular, the agreement among member states of the euro area on a further rescue package for Greece. The package of measures approved in February contains a second loan programme totalling EUR 130 billion, lower interest rates on the assistance loans, and an agreement by private sector bondholders to accept losses of over 50% on their investments.

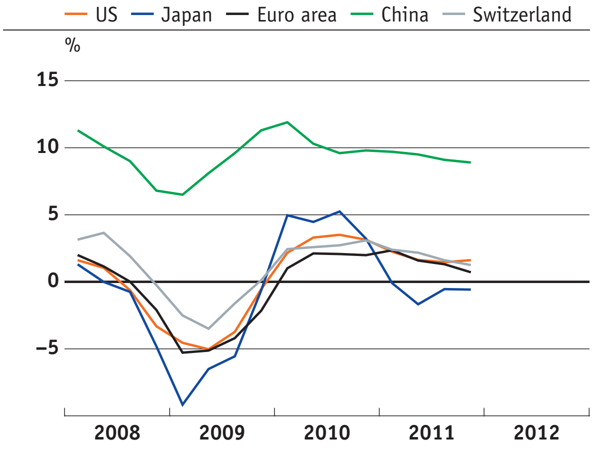
Numerous factors, however, are clouding growth prospects in the euro area. These include ongoing concerns about the fiscal sustainability of some member states, as well as the dampening effects on the economy of the impending consolidation measures. The banks' difficult capital situation could also constrain lending and limit corporate investment. Against this backdrop, the SNB has again lowered its growth expectations for the euro area, and now anticipates that GDP will contract by 0.3% in 2012.

Consumer price inflation in the euro area declined slightly to 2.7% in February. This was mainly due to base effects from energy prices. Core inflation remained virtually unchanged at 1.5%. Although some euro area countries' plans to increase indirect taxes will temporarily exert mild upward pressure on inflation, overall, inflation is likely to decline due to weak economic growth.

The ECB maintained its expansionary monetary policy, and added some unconventional measures. It continued to provide the banks with unlimited liquidity. In December and February, it conducted three-year refinancing operations for the first time, which resulted in a palpable easing of tension on the money market. In addition, the list of assets eligible as collateral was expanded to make it easier for smaller financial institutions, in particular, to participate in refinancing operations.

Chart 2.6
Real GDP

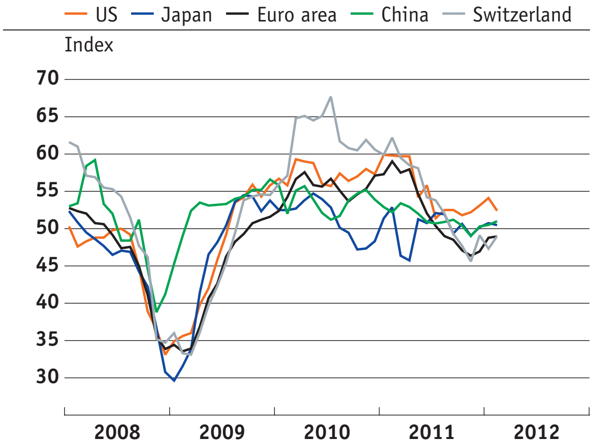
Year-on-year change



Sources: State Secretariat for Economic Affairs (SECO), Thomson Financial Datastream

Chart 2.7
Purchasing managers' indices (manufacturing)

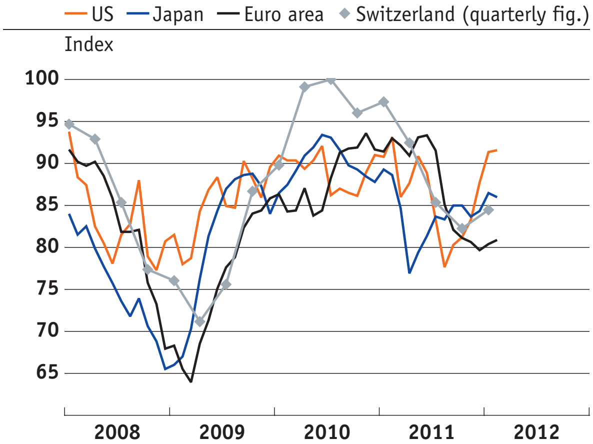
Monthly figures



Source: Thomson Financial Datastream; copyright and database rights: Markit Economics Ltd 2009; all rights reserved

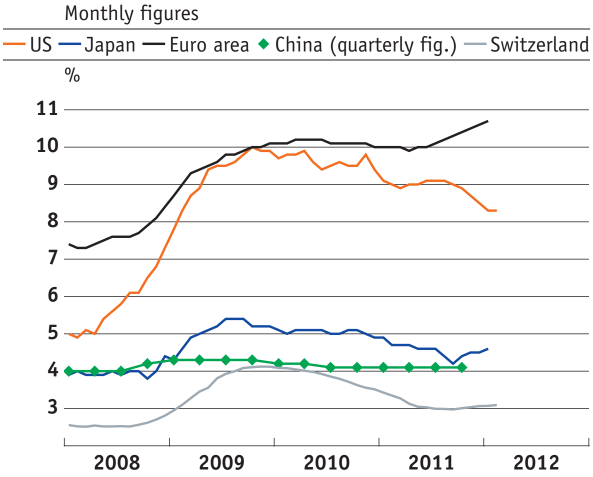
Chart 2.8
Consumer confidence index

April 2007 = 100, monthly figures



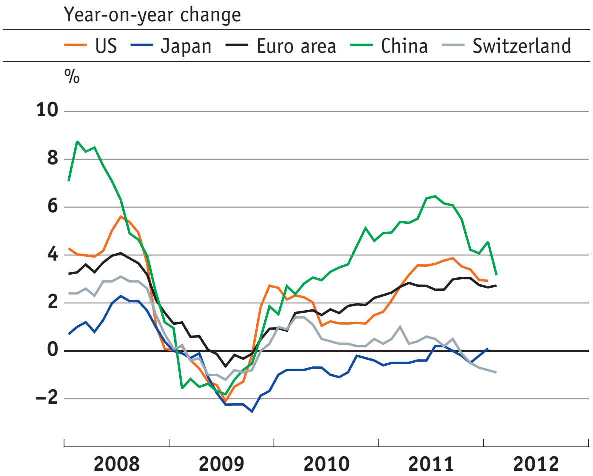
Sources: SECO, Thomson Financial Datastream

Chart 2.9
Unemployment rates



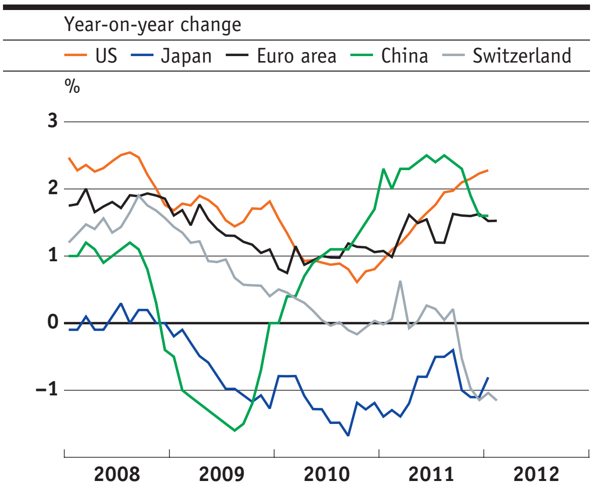
Sources: SECO, Thomson Financial Datastream

Chart 2.10
Consumer prices



Sources: Swiss Federal Statistical Office (SFSO), Thomson Financial Datastream

Chart 2.11
Core inflation rates



Sources: SFSO, Thomson Financial Datastream

2.4 Japan

The economic situation in Japan remained difficult. The strong appreciation of the yen in the second half of the year reduced exporters' price competitiveness. In addition, flooding in Thailand in autumn brought important production plants in the supply chain for the Japanese electronics and automobile industries to a standstill. This resulted in a contraction in fourth-quarter GDP of 0.7%. Average GDP in 2011 also fell by 0.7%.

The outlook for growth in 2012 is subdued, given that investment is being discouraged by unfavourable export prospects. After the production losses caused by the catastrophe in Thailand, however, a catch-up effect is likely at the beginning of the year. For reconstruction in areas afflicted by the earthquake disaster, the Japanese government agreed in February on a fourth supplementary budget totalling JPY 2,500 billion, or 0.5% of GDP. One of the budget's purposes is to finance the reintroduction of purchasing incentives to revive the battered automobile industry. The SNB is expecting Japan's GDP to grow by 1.9% in 2012.

Consumer prices in January were slightly higher than a year earlier, due to a temporary rise in the price of fresh food. Excluding energy and food, however, prices were 0.8% lower compared to the previous year. With capacity utilisation still a long way off its normal level, there continues to be no prospect of inflationary pressure in the near future.

The Bank of Japan increased its budget for the purchase of Japanese government bonds under the Asset Purchase Program by a further JPY 10,000 billion to JPY 19,000 billion. It left the call money rate unchanged at 0.0–0.1%. In addition, for the first time, the Bank of Japan set an inflation target, as measured by the consumer price index, of 1%.

2.5 Emerging economies

The end of 2011 saw a loss of momentum in the emerging economies due to weak growth in the advanced economies and tight monetary policy.

The newly industrialised economies in Asia (NIEs) – South Korea, Taiwan, Hong Kong and Singapore – were increasingly afflicted by weakening demand for exports. Further burdens on domestic demand were the uncertain economic and financial situation in Europe, increased inflation (in some cases), and stricter credit conditions. At 4.0%, the average GDP growth of the NIEs in 2011 remained robust, although markedly less so than in the previous year (8.5%). In China, the major driver of growth in recent years, GDP in 2011 rose by 9.2%, which was slightly below the average for the last ten years. Tight monetary policy slowed investment in the second half of the year, while robust income growth and state subsidies underpinned consumer demand. This had the desired effect of shifting growth onto domestic consumption. In India, GDP growth in 2011 amounted to 7.1%, which was also lower than in recent years. With regard to Latin America, GDP growth in Brazil in the second half of the year came to a near-standstill. There, too, domestic demand suffered due to tight monetary policy. In particular, demand for consumer durables and activity in the manufacturing industry declined.

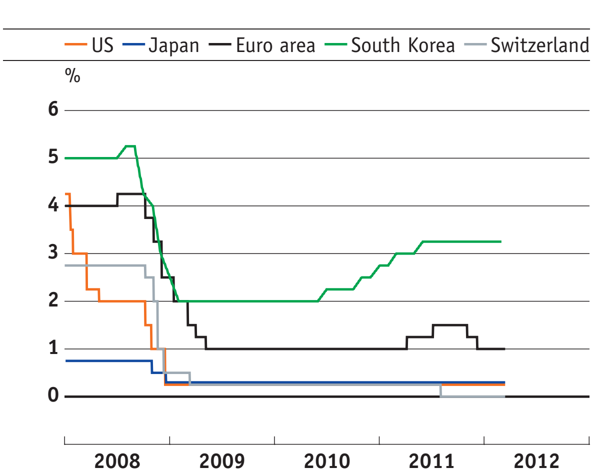
The emerging economies are likely to continue suffering in the months ahead on account of the weak performance by the advanced economies. In major emerging economies like China, India and Brazil, private consumption should play a key role in 2012, as inflation gradually subsides and economic policy measures support households' purchasing power. One source of risk to China's level of domestic consumption are the emerging signs of a real estate price correction. In the NIEs, solid demand from China as well as the scope for fiscal policy measures are likely to provide an economic boost.

For 2012, the SNB expects moderate economic growth in the emerging economies, although it anticipates that growth in China will slow to around 8.5%.

The decline in food price inflation, in particular, is contributing to a reduction in consumer price inflation in the emerging economies. In China, annual inflation reached a three-year high of 6.5% in July 2011; in February 2012 it stood at 3.2%. In India, the annual inflation rate fell from around 10% in the middle of last year to 7.0% in February. In Brazil, it declined to 5.8%. In most of the emerging economies, inflation is likely to subside further as a result of moderate growth.

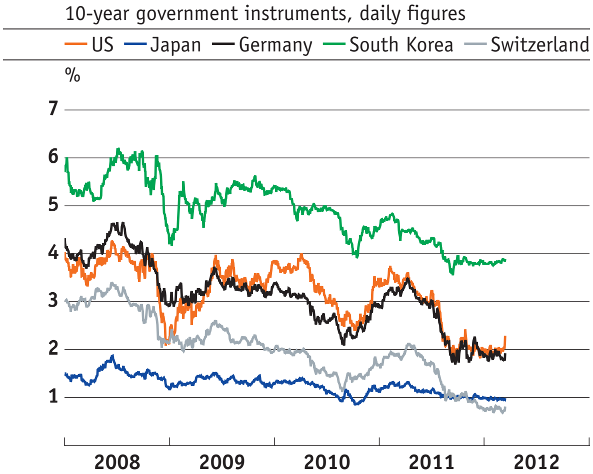
Monetary policy remains firmly focused on the economic risks. Brazil's central bank again lowered the reference interest rate. China's central bank again lowered the minimum reserve requirements for banks, in order to manage the supply of liquidity. In addition, as of the beginning of the year, it has permitted no further appreciation of the Chinese currency on a trade-weighted basis. In India, at the beginning of the year, minimum reserve requirements for the banks were also loosened. In the smaller Asian economies, monetary policymakers for the most part adopted a wait-and-see approach.

Chart 2.12
Official interest rates



Sources: SNB, Thomson Financial Datastream

Chart 2.13
International long-term interest rates



Sources: SNB, Thomson Financial Datastream

3 Economic developments in Switzerland

Economic growth in Switzerland slowed further in the fourth quarter. According to preliminary estimates, annualised real GDP increased by only 0.4%. The introduction of the minimum exchange rate in September 2011 has reduced the Swiss franc's substantial overvaluation and given companies a sounder basis on which to plan their investments. This has checked the impact on economic growth. Nevertheless, the continued strength of the Swiss franc has left its mark: in many sectors with strong exposure to exchange rates – manufacturing, wholesaling, retailing and tourism – value added declined in the fourth quarter. While value added recorded no more than modest growth on the output side of the economy, final demand rose substantially. This difference is reflected in a negative contribution from inventories.

The economic slowdown has widened the negative output gap further, with continued high immigration contributing to robust growth in production potential. The Swiss labour market remained buoyant in the fourth quarter: employment growth was stable, while unemployment only rose slightly.

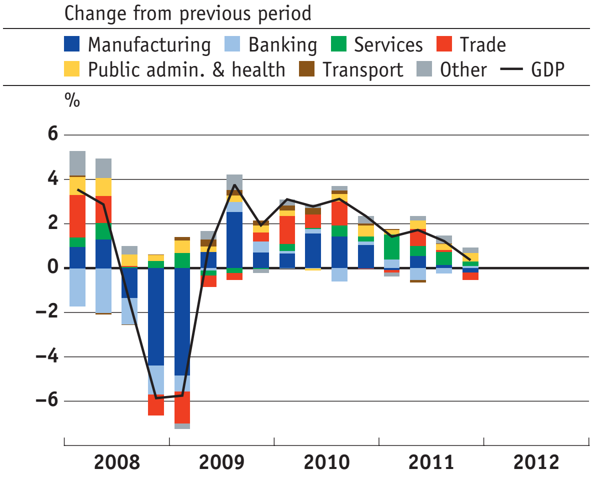
Thanks to favourable momentum in the first half of the year, an economic growth rate of 1.9% was achieved for 2011 as a whole. Following a temporary dip in the second half of the year, the Swiss economy should pick up again somewhat. The SNB is projecting moderate economic growth of close to 1% for 2012.

3.1 Aggregate demand and output

Weak production momentum in the fourth quarter

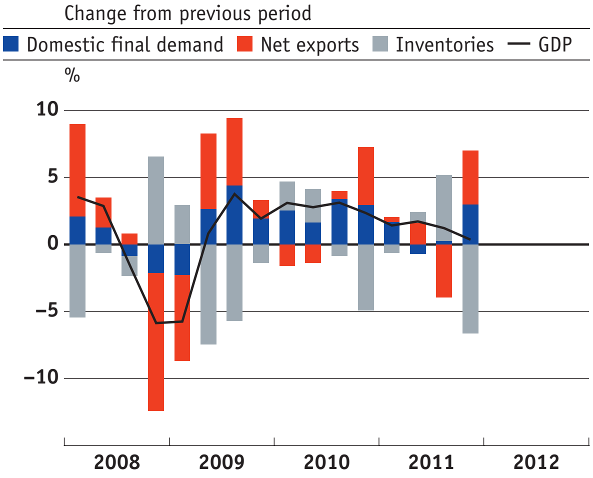
According to provisional estimates by the State Secretariat for Economic Affairs (SECO), GDP increased by just 0.4% in the fourth quarter, compared with 1.2% in the third quarter. The year-on-year rise was 1.3%. The reduction in growth momentum affected all industries on the output side of the economy. While many areas of the services industry posted only modest growth, value added in manufacturing and domestic trading (wholesaling and retailing) actually declined slightly (cf. chart 3.1). The downward trend in the hospitality industry continued unabated. In addition to sluggish growth in real value added, producers in some sectors had to accept lower selling prices.

Chart 3.1
Contributions to growth, by sector



Source: SECO

Chart 3.2
Contributions to growth in demand



Source: SECO

Strong rise in exports

Net exports increased substantially in the fourth quarter (cf. chart 3.2), having been clearly negative in the previous quarter. While imports (excluding valuables) declined slightly (cf. chart 3.3), exports (excluding valuables) grew by a robust 7.2% compared with the previous quarter (cf. chart 3.4). The foreign trade contribution was thus strongly positive overall (4.0 percentage points).

In the fourth quarter, goods exports were able to make up for their weakness in the summer. Exports of chemical products (especially pharmaceuticals) grew particularly strongly. However, exports by other sectors also defied the predominantly weak global conditions; the upward trend in the export of watches continued, while the decline in machine exports came to an end. Looking at the main markets for exports, strong growth was registered in exports to the US and oil-exporting countries.

Exports of services fell further in the fourth quarter, but the downward trend was less pronounced than in the second and third quarters. Commission income from cross-border banking transactions decreased, as the industry was not yet benefiting from the stabilisation of the financial markets. In addition, tourism exports slipped further because the valuation of the Swiss franc remained high, although the downtrend was not as significant as in preceding quarters. By contrast, there was a slight increase in receipts from commodity trading (merchanting).

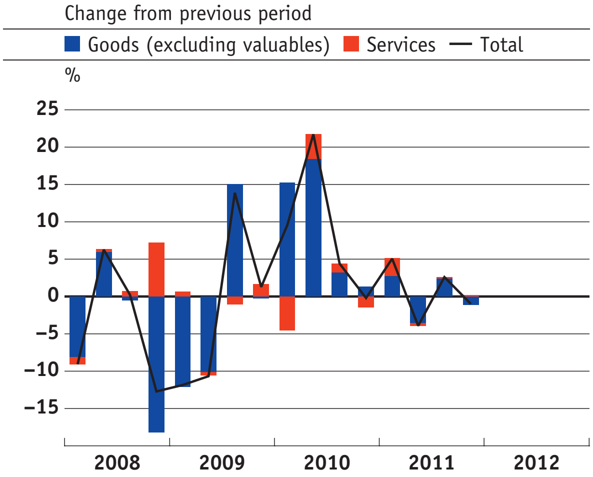
The development of imports remained sluggish in the fourth quarter. Despite sound consumer confidence, the Directorate General of Customs did not register an increase in spending on imports of consumer goods. This may also be due to the fact that very few direct imports by private households are recorded. Imports of semi-finished products actually recorded another slight fall. By contrast, owing to the upturn in investment, imports of machinery rose. There was also a modest rise in imports of services (especially in tourism).

Strong domestic final demand, negative contribution from inventories

Domestic final demand increased considerably at year end (cf. chart 3.5 and table 3.1). Gross investment in fixed assets and consumption contributed to GDP growth. Inventories, by contrast, exerted a substantial downward pull.

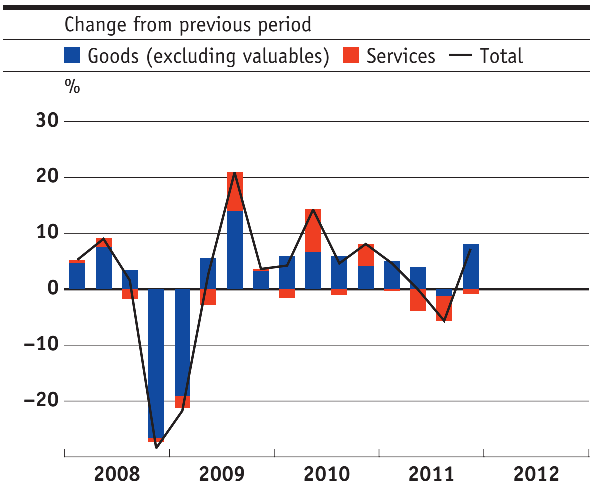
Following significant declines in preceding quarters, at 12.2% a sharp rise in equipment investment was registered in the fourth quarter of 2011. Construction investment also improved con-

Chart 3.3
Contributions to import growth



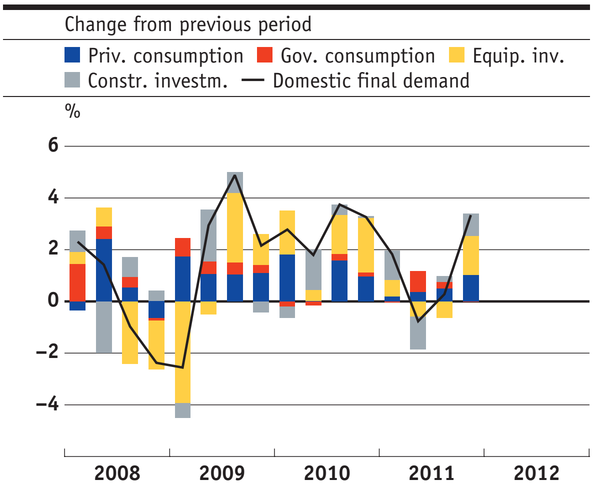
Source: SECO

Chart 3.4
Contributions to export growth



Source: SECO

Chart 3.5
Domestic final demand, growth contributions



Source: SECO

Real GDP and components Table 3.1

Growth rates on previous period, annualised

	2008	2009	2010	2011	2010				2011			
					Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Private consumption	1.4	1.4	1.7	1.0	2.8	0.0	2.4	1.5	0.3	0.6	0.8	1.6
Government consumption	2.7	3.3	0.8	1.7	–1.5	–1.2	2.0	1.2	–0.2	6.4	2.0	–0.2
Investment in fixed assets	0.5	–4.9	7.5	3.9	5.3	8.6	8.4	9.3	7.4	–7.8	–1.9	10.3
Construction	0.0	3.0	3.5	2.5	–4.2	15.5	3.9	0.7	10.8	–11.7	2.1	8.0
Equipment	0.8	–10.8	10.9	5.1	13.7	3.4	12.2	16.7	4.9	–4.4	–5.1	12.2
Domestic final demand	**1.3**	**0.1**	**2.9**	**1.7**	**2.8**	**1.8**	**3.7**	**3.3**	**1.8**	**–0.8**	**0.3**	**3.3**
Domestic demand	**0.5**	**0.6**	**1.5**	**0.9**	**4.8**	**2.4**	**6.7**	**–4.6**	**2.3**	**0.1**	**5.4**	**–6.0**
Total exports	3.1	–8.6	8.4	3.4	9.3	11.3	1.1	8.9	5.3	0.3	–5.1	4.7
Goods[1]	2.1	–11.1	9.4	6.2	8.9	9.7	8.6	6.0	7.4	5.9	–1.6	11.6
Services	4.3	–1.7	5.4	–1.5	–4.9	24.6	–3.3	12.7	–1.1	–12.0	–14.4	–2.6
Aggregate demand	**1.5**	**–3.0**	**4.0**	**1.9**	**6.5**	**5.7**	**4.5**	**0.4**	**3.4**	**0.2**	**1.3**	**–2.0**
Total imports	0.3	–5.5	7.3	1.9	15.3	13.1	7.9	–4.2	8.1	–3.4	1.5	–7.5
Goods[1]	–1.0	–8.5	10.8	2.3	19.5	23.1	4.0	1.6	3.4	–4.4	2.9	–1.4
Services	4.1	7.4	–1.9	3.0	–20.7	16.4	6.2	–7.2	12.0	–1.9	1.2	0.7
GDP	**2.1**	**–1.9**	**2.7**	**1.9**	**3.1**	**2.8**	**3.1**	**2.3**	**1.4**	**1.7**	**1.2**	**0.4**

1 Goods: excluding valuables (precious metals, precious stones and gems as well as works of art and antiques)
Source: SECO

siderably in the fourth quarter (+8.0%). Residential construction in particular saw another strong rise. The large number of new building permits approved in the past few quarters indicates that activity in this area is likely to remain brisk. Civil engineering continued to benefit from high demand for infrastructure projects. By contrast, commercial construction remained weak.

While private consumption had grown only slightly in preceding quarters, it picked up considerably to 1.6% in the fourth quarter, as consumer spending was boosted by price discounts in many segments, notably in food and residential property. New car registrations also rose steadily, and by the end of 2011 had reached the highest level since 1990.

3.2 Labour market

Further robust growth in employment

Despite flagging momentum in production, employment growth remained stable in the fourth quarter. Full and part-time employment increased by 0.9%. Expressed in full-time equivalents, this constitutes an increase in employment of 1.3% (cf. chart 3.6).

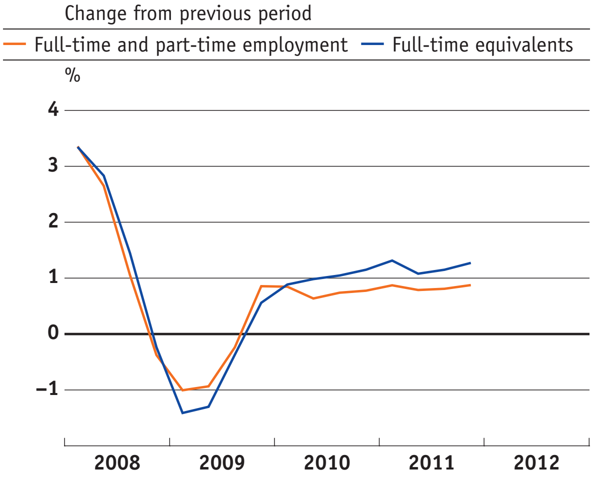
Employment in the construction sector continued its robust development. In manufacturing, the positive growth momentum eased off only slightly. However, the number of jobs in this sector is still well below the pre-crisis level registered in summer 2008. The employment situation in the services sector as a whole remained favourable, with only hospitality, retailing and financial services cutting jobs.

Marginal increase in unemployment

Unemployment rose slightly between November and February. The number of people registered as unemployed with regional employment offices increased by around 2,000 (seasonally adjusted), which represents a rise in the unemployment rate from 3.0% to 3.1% (cf. chart 3.7). By contrast, the proportion of job-seekers remained stable at 4.4% in this period.

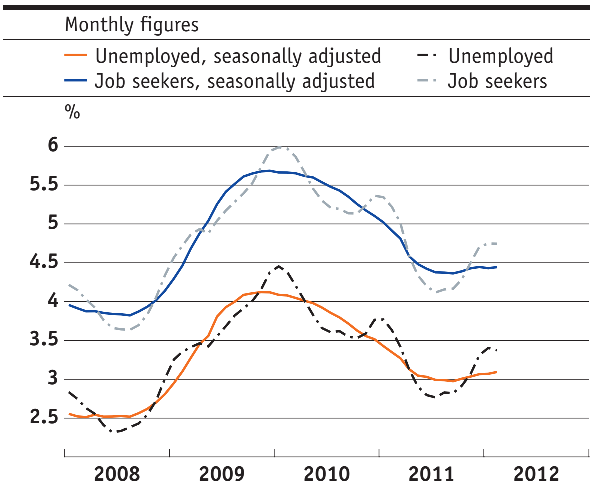
There was no significant change in short-time working either: it remained low to December 2011 (cf. chart 3.8).

Chart 3.6
Employment



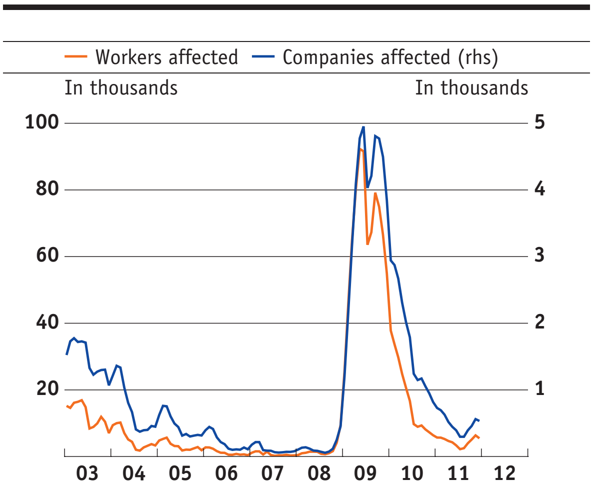
Source: SFSO, seasonal adjustment: SNB

Chart 3.7
Unemployment and job seeker rates



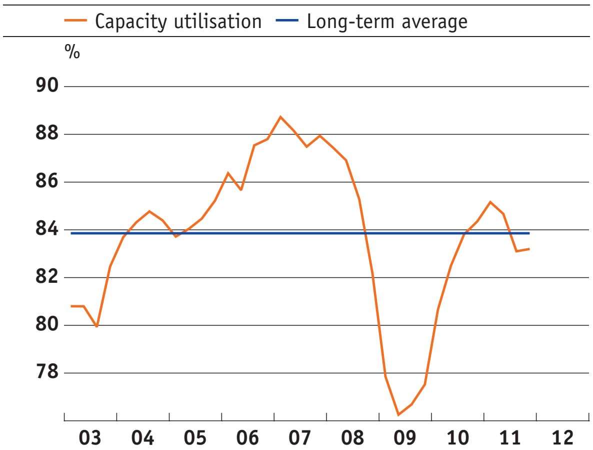
Unemployed and job seekers registered with the regional employment offices, as a percentage of the labour force according to the 2000 census (labour force: 3,946,988 persons).
Source: SECO

Chart 3.8
Short-time working



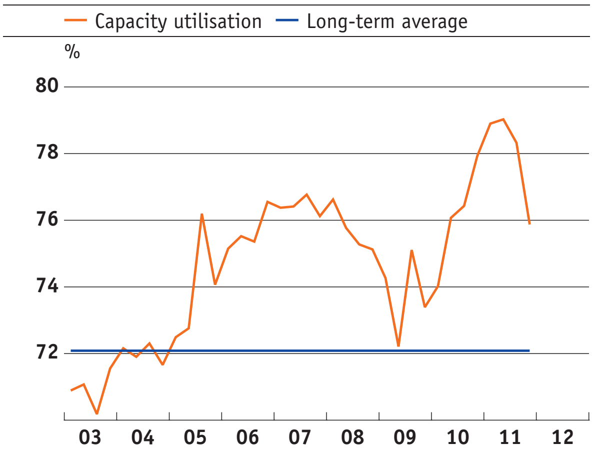
Source: SECO

Chart 3.9
Capacity utilisation in manufacturing



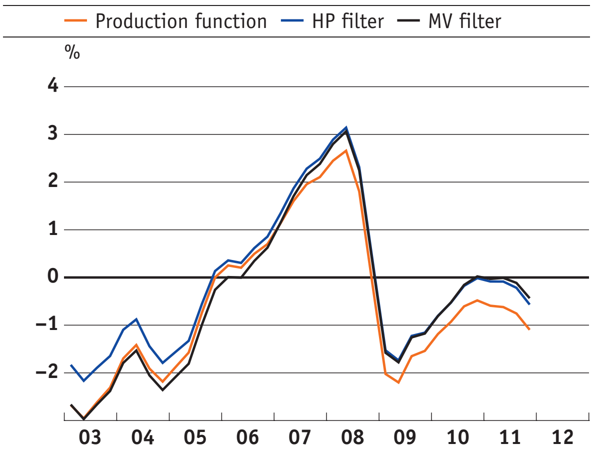
Source: KOF Swiss Economic Institute

Chart 3.10
Capacity utilisation in construction



Source: KOF Swiss Economic Institute

Chart 3.11
Output gap



Source: SNB

3.3 Capacity utilisation

Capacity utilisation is stabilising

Technical capacity utilisation in manufacturing stabilised in the fourth quarter. According to the survey conducted by the KOF Swiss Economic Institute, at 83.2% it remained slightly below its long-term average (cf. chart 3.9).

Although there was a noticeable decline in machine utilisation in construction in the fourth quarter, at 75.9% this was still well above average (cf. chart 3.10). Accordingly, many of the companies surveyed were still reporting bottlenecks in machine and equipment capacity, as well as labour shortages. Companies in the services sector reported normal capacity utilisation in the fourth quarter. The utilisation rate at hotels and restaurants actually rose again to its long-term average. In view of the ongoing decline in value added, this could point to a reduction in capacity.

Slight widening in output gap

The output gap, which is defined as the percentage deviation of GDP from estimated aggregate potential output, shows how well the production factors in an economy are being utilised.

The negative output gap widened further in the fourth quarter. Estimated potential output based on the production function approach indicates that the output gap amounted to –1.1% in the fourth quarter (cf. chart 3.11). Estimates using other methods (Hodrick-Prescott filter and multivariate filter) indicated that the output gap had narrowed (–0.6% and –0.4%).

The different estimates reflect the various ways of calculating production potential. The production function approach considers the labour market situation and the stock of capital in the economy. Since potential labour levels have risen steadily in recent years – to some extent because of immigration – the estimate of production potential based on this method is higher than production potential estimated on the basis of statistical filters. Accordingly, the output gap calculated using the production function approach is wider.

3.4 Outlook for the real economy

The outlook for the Swiss economy has recently brightened somewhat. The latest survey results suggest that the situation is stabilising, and the favourable development of goods exports and retail turnover in January point in the same direction. The resilience of the Swiss economy is doubtless partly due to the introduction of the minimum exchange rate for the Swiss franc against the euro. This has reduced the substantial appreciation of the Swiss franc and made it somewhat easier for businesses to plan ahead.

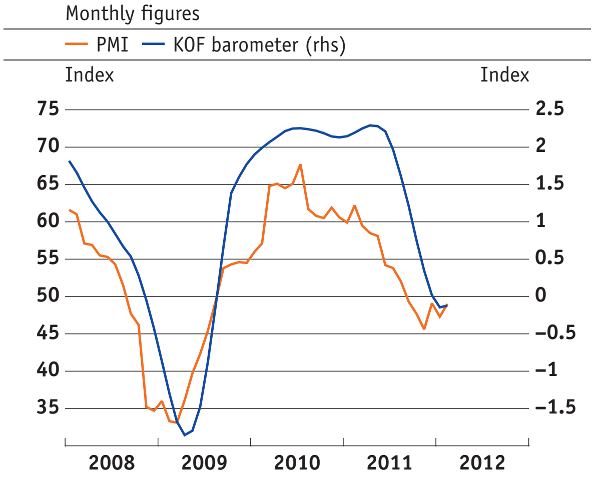
Nevertheless, the high value of the Swiss franc remains a burden. Many companies are faced with declining prices, which is eroding turnover in nominal terms. In particular, companies which have considerable depth of production in Switzerland find that this is putting pressure on profit margins. The muted outlook for the business climate in other countries and ongoing uncertainty about the outcome of the European sovereign debt crisis are exacerbating this situation and companies are likely to hold back on investment as a result.

Domestic economic factors, such as low interest rates, are also still having a favourable impact. In addition, domestic demand is buoyed up by persistently high levels of immigration. The construction industry and various areas of the services sector should benefit from these factors.

The SNB expects the Swiss economy to post positive growth again in the first quarter. For 2012 as a whole, it is predicting GDP growth of close to 1%. The subdued business climate is likely to be reflected in a slight increase in unemployment over the following quarters. The output gap will remain negative.

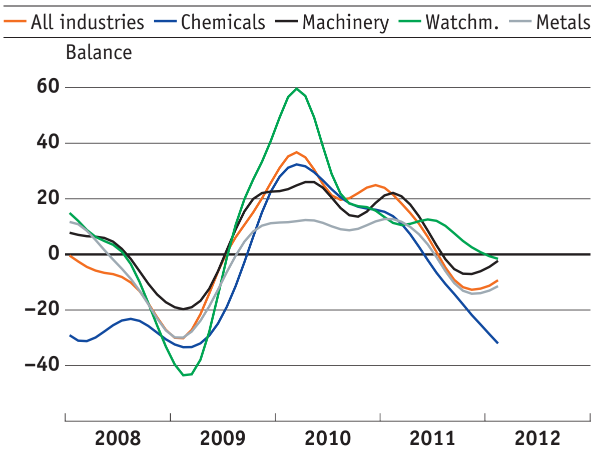
As long as no sustainable solution for the European sovereign debt crisis is implemented, however, the outlook remains highly uncertain.

Chart 3.12
Leading indicators



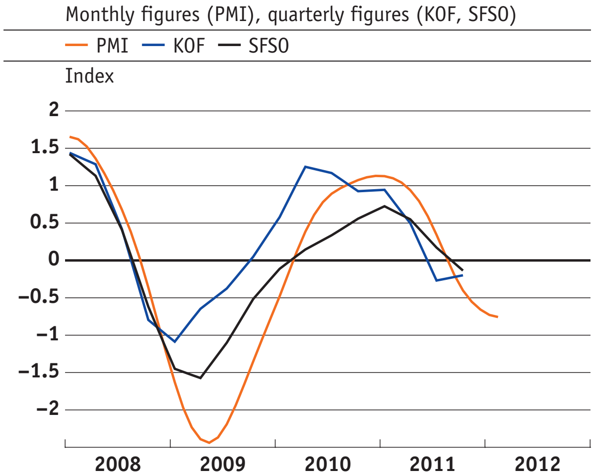
Sources: Credit Suisse, KOF Swiss Economic Institute

Chart 3.13
Expected new orders



Source: KOF Swiss Economic Institute

Chart 3.14
Employment leading indicators



Sources: Credit Suisse, KOF Swiss Economic Institute, SFSO

4 Prices and inflation expectations

Inflation is still influenced by last year's sharp appreciation of the Swiss franc. Producer and import prices as well as consumer prices have not fallen further in recent months. However, both consumer prices and producer and import prices are still lower than a year ago.

Surveys of inflation expectations show that in the short term, the general expectation is that the price level will remain unchanged. On a medium term horizon, inflation expectations are still in the low positive range.

4.1 Consumer prices

Further decline in CPI inflation

The annual inflation rate as measured by the national consumer price index (CPI) has fallen further in recent months. In February, it stood at –0.9% compared with –0.5% in November (cf. table 4.1). However, there is no indication that the decline in prices is gaining momentum. In fact, the downward trend that had started in June 2011 came to a halt.

The negative annual inflation rate is due mainly to the change in prices of foreign goods. Influenced by the strong appreciation of the Swiss franc, they fell sharply until February 2012. February then saw a slight increase compared with the previous month. Even though oil products became more expensive (cf. chart 4.1), prices of foreign goods fell by 3.4% in the space of a year.

National consumer price index and components
Year-on-year change in percent

Table 4.1

	2011	2011				2011	2012	
		Q1	Q2	Q3	Q4	December	January	February
Overall CPI	**0.2**	**0.6**	**0.4**	**0.4**	**–0.5**	**–0.7**	**–0.8**	**–0.9**
Domestic goods and services	0.6	0.6	0.6	0.7	0.3	0.2	0.1	0.0
Goods	–1.3	–1.0	–1.0	–1.1	–2.1	–2.1	–2.4	–2.3
Services	1.1	1.1	1.1	1.2	1.1	0.9	0.8	0.7
Private services excluding rents	0.8	0.6	0.8	0.9	0.9	0.8	0.6	0.8
Rents	1.3	1.5	1.3	1.3	1.2	1.1	1.1	0.7
Public services	1.8	2.0	1.8	1.8	1.4	0.9	0.6	0.6
Imported goods and services	–0.7	0.5	–0.3	–0.4	–2.6	–3.3	–3.2	–3.4
Excluding oil products	–2.5	–1.3	–1.9	–1.8	–5.0	–5.7	–5.3	–5.3
Oil products	9.3	10.5	8.9	7.5	10.5	10.0	8.1	6.2

Sources: SFSO, SNB

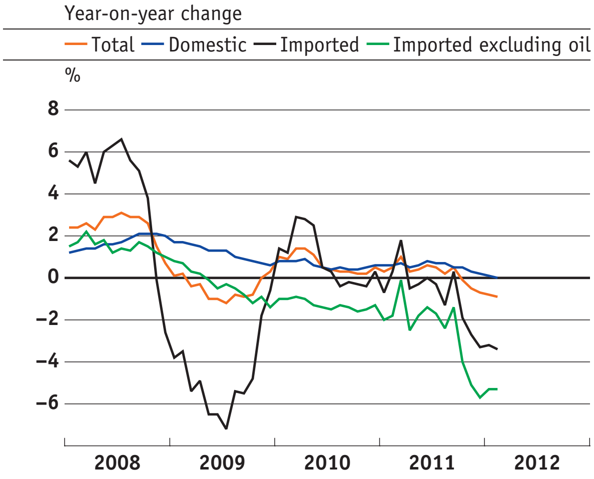
There is still a clear disparity between the price trends for domestic goods and for domestic services (cf. chart 4.2). Prices of domestic goods had fallen slightly since November and in February, they were well below their level a year ago. By contrast, prices for domestic services continued to rise. Against the backdrop of the lowering of the reference interest rate in December 2011, the rise in rents between November and February was weaker than a year earlier. As a consequence, year-on-year rent inflation declined from 1.1% in November to 0.7% in February.

Exceptionally low core inflation

For the evaluation of the CPI, the SFSO's core inflation rate (SFSO1), the trimmed mean (TM15) and dynamic factor inflation (DFI) can be used. The latter two are calculated by the SNB. In February, all three indicated lower core inflation than three months earlier (cf. chart 4.3). In February, the TM15 slipped into negative territory for the first time since these calculations were first made in 1978 (–0.1%). At –1.2%, the SFSO1 was even lower, while DFI was positive (0.5%). DFI is calculated using an empirically estimated dynamic factor model that includes other real and nominal economic data in addition to price data, whereas the TM15 and SFSO1 are based on a reduced CPI basket.

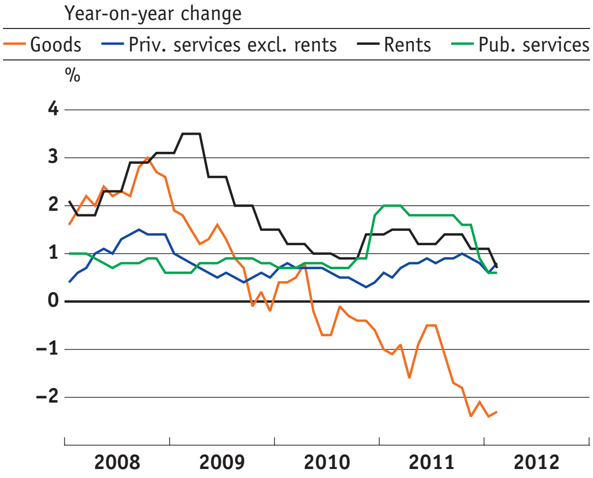
At present, the big difference between the two core inflation rates based on a reduced CPI basket is striking. The difference between the TM15 and SFSO1 is based on the following. The SFSO1 always excludes the same goods (fresh and seasonal products, energy and fuel). The TM15, on the other hand, excludes each month the goods with the highest and lowest inflation rates over the past twelve months (15% at either end of the distribution). This is why extreme price fluctuations of individual products often have a stronger impact on the SFSO1 than on the TM15. Following the significant appreciation of the Swiss franc in the first half of 2011, the SFSO1 registered a far greater decrease than the TM15, and even dropped by more than the annual CPI inflation. The TM15 is currently likely to be a more accurate reflection of the inflation trend than the SFSO1.

Chart 4.1
CPI: domestic and imported goods and services



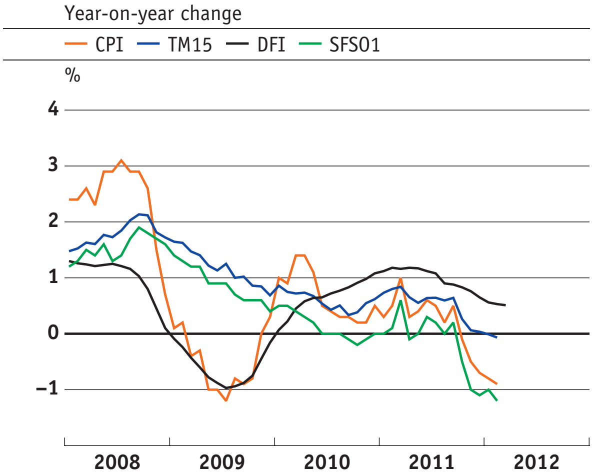
Sources: SFSO, SNB

Chart 4.2
CPI: domestic goods and services



Sources: SFSO, SNB

Chart 4.3
Core inflation rates



Sources: SFSO, SNB

4.2 Producer and import prices

Slightly higher prices for overall supply

Producer and import prices have registered a slight increase since November. Since import prices, in particular, usually respond rapidly to changes in exchange rates, this is likely to indicate that the inflation-dampening effect of the Swiss franc's appreciation is gradually subsiding. Year-on-year inflation is still in negative territory (cf. chart 4.4), due mainly to the sharp drop in producer and import prices in the second half of 2011.

Looking at classification by use, price reductions were registered for consumer goods and agricultural and forestry products. By contrast, price indices for the other categories increased. In some cases, the rise was even considerable.

4.3 Real estate prices

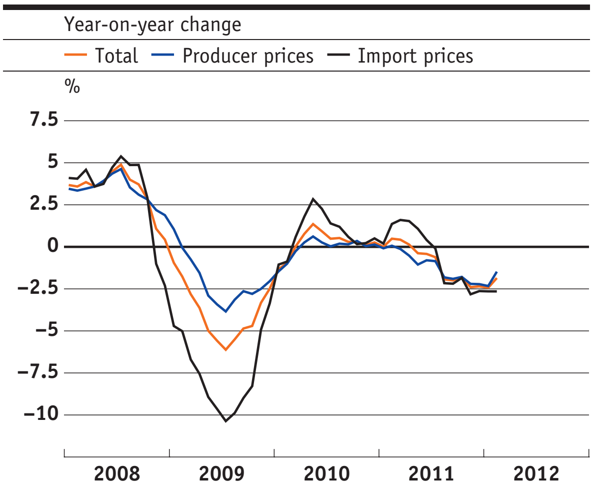
Uneven development of various indices in fourth quarter

Real estate prices showed a mixed pattern in the fourth quarter. On the one hand, prices for owner-occupied apartments and single-family houses offered for sale in newspapers and via the internet saw another sharp increase. On the other hand, according to the index calculated by Wüest & Partner, transaction prices for single-family homes rose only modestly, while transaction prices for owner-occupied apartments actually declined slightly (cf. chart 4.5).

While the various indices deliver a mixed picture of developments in the fourth quarter, they all clearly indicate that prices for residential real estate have risen sharply over a period of several years. This applies particularly to owner-occupied apartments, where prices have risen by 50–70% over the past ten years, depending on the index. That is well above the increase in consumer prices and nominal per capita income registered in the same period.

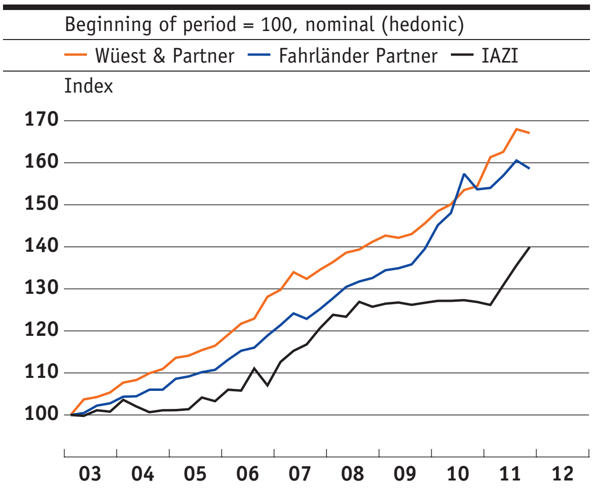
Once again, apartment rents rose only marginally in the fourth quarter. However, this applies to rents in existing rental contracts. By contrast, rents for housing units offered on the market (quoted rents) continued to rise (cf. chart 4.6). Rents in

Chart 4.4
Producer and import prices



Source: SFSO

Chart 4.5
Transaction prices, owner-occupied apartments



Sources: Fahrländer Partner, IAZI, Wüest & Partner existing contracts are tied by law to the reference mortgage rate, which has dropped by one percentage point since 2008. As long as the reference rate does not rise, inflation in existing rents should remain low.

4.4 Inflation expectations

Inflation expectations remain low

Surveys of households and experts on expected price trends and inflation rates are still indicating low inflation expectations.

The quarterly survey of households conducted by SECO shows that in January just under half of respondents expected prices to remain unchanged over the next twelve months (cf. chart 4.7). About one-fifth expected prices to fall, while the remaining third anticipated that prices will rise. The proportion of respondents who expected prices to remain unchanged increased for the third time in succession. By contrast, fewer respondents expected prices to fall. Three months earlier, there was a considerable rise in the proportion expecting prices to fall, presumably because of the strong Swiss franc.

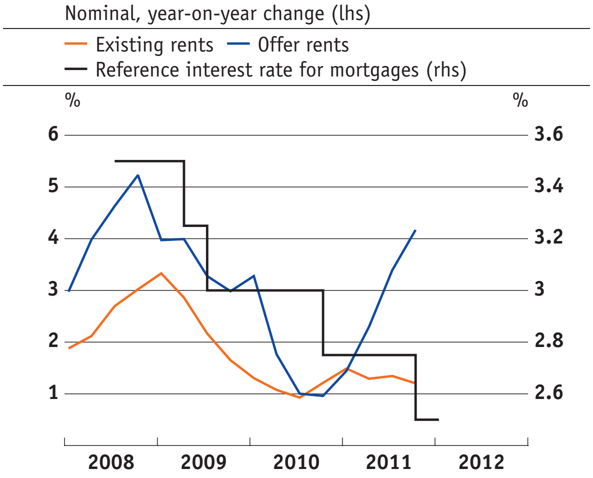
The monthly *Credit Suisse ZEW Financial Market Report* showed that in February – as in December and January – the majority of financial market experts surveyed (69%) expected inflation rates to remain unchanged over the next six months, while the number expecting them to rise or fall was balanced.

Other surveys provide information on quantitative inflation expectations. Talks held by the SNB delegates for regional economic relations in January and February show that the companies surveyed expect an average inflation rate of 0.2% on a six to twelve-month horizon, compared with 0.4% in the previous quarter. The longer-term inflation expectations derived by Deloitte are higher. In the fourth quarter, the CFOs and heads of finance from companies based in Switzerland who took part in this survey expected the inflation rate to be 1.6% in two years.

No change expected in producer purchase prices

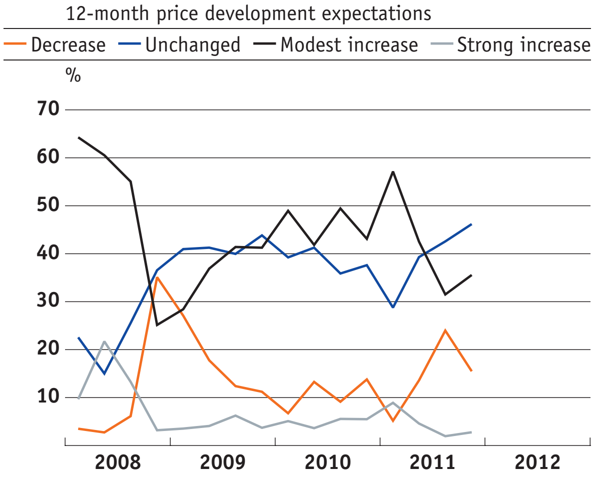
A survey conducted by KOF Swiss Economic Institute shows that, in January, wholesale and industrial companies expected a trend towards stable purchase prices and falling sale prices over a three-month period. In October, the majority still expected to see a downtrend in both purchase and sale prices. The results of the KOF survey on purchase prices therefore suggest that the fall in the price level should slow further in the near future.

Chart 4.6
Apartment rents and reference interest rate



Sources: Federal Office for Housing (FOH), SFSO, Wüest & Partner

Chart 4.7
Survey on expected movements in prices



Sources: SECO, SNB

5 Monetary developments

Since September 2011, the SNB has rigorously enforced the announced minimum exchange rate against the euro. However, the Swiss franc remains high, and has even appreciated marginally against both the euro and the US dollar since the monetary policy assessment of December.

In the quarter under review, interest rates remained very low across all maturities. The slight increase in the three-month Libor reflects a certain normalisation of conditions on the interbank money market, and not a tightening of monetary policy. This is also evidenced by the fact that interest rate futures have recently stopped predicting negative interest rates.

Despite a slight decline in sight deposits at the SNB, the monetary base is still at a historically high level. The broad monetary aggregates also expanded strongly. However, the high valuation of the Swiss franc and the negative output gap are preventing any inflationary effect from the growth of monetary aggregates.

Growth in lending eased off somewhat in the fourth quarter of 2011, but remained robust. The weaker lending growth was due to the stagnation of other lending; mortgage lending growth continued to gather pace. Overall, there are no indications that corporate lending is being reined in. Nevertheless, this sustained growth in lending does increase the risks to financial stability.

5.1 Summary of monetary policy since the last assessment

Continuation of monetary policy announced in September 2011

Over the past few months, the SNB has maintained the monetary policy announced on 6 September 2011, and reiterated at the mid-September and mid-December assessments. On 6 September, the SNB had set a minimum exchange rate of CHF 1.20 to the euro. The target range for the three-month Libor had already been narrowed in August, to 0.0–0.25%.

Sight deposits at SNB still high

Having expanded sharply in August and September 2011, sight deposits at the SNB remained high. Between the assessments in mid-December 2011 and mid-March 2012, sight deposits at the SNB averaged CHF 218.8 billion. Of this amount, CHF 170.9 billion was accounted for by the sight deposits of domestic banks and CHF 47.9 billion by other sight deposits. In the week ending 9 March 2012 (the last calendar week before the March monetary policy assessment), total sight deposits at the SNB were reported at CHF 217.3 billion, almost the same as the average level of sight deposits since the December assessment.

Liquidity-providing open market operations

Since the December assessment, the SNB has conducted regular liquidity-providing repo operations with one-week maturities. In addition, at regular intervals in December, it made liquidity available for longer maturities. For example, one-month repo transactions were carried out for year-end liquidity purposes. The SNB also engaged in foreign exchange swaps at irregular intervals, in order to provide temporary Swiss franc liquidity. In a foreign exchange swap, the SNB buys foreign currency against Swiss francs in a spot transaction, and simultaneously sells the Swiss francs in a forward transaction.

At the time of the December 2011 assessment, SNB Bills amounting to CHF 18.6 billion were outstanding. Since then, SNB Bills worth approximately CHF 11.3 billion have fallen due.

Rise in banks' surplus reserves

Statutory minimum reserves averaged CHF 11.7 billion between 20 November 2011 and 19 February 2012, an increase of around CHF 1 billion compared to the preceding period (20 August 2011 to 19 November 2011). On average, banks exceeded the requirement by around CHF 169.3 billion (previous period: CHF 188.8 billion). The average compliance level fell from 1,859% to 1,547%.

5.2 Money and capital market interest rates

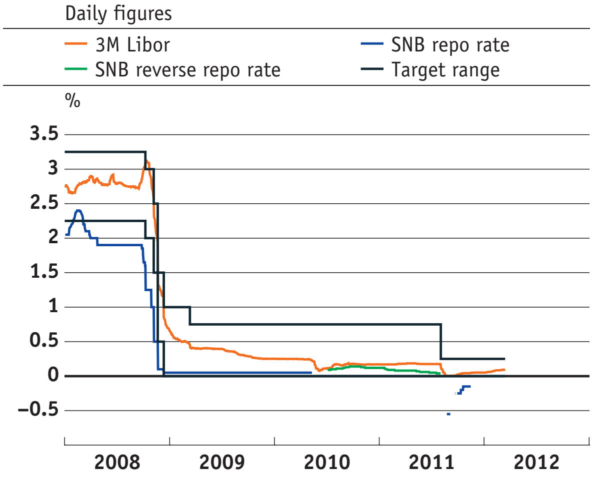
Over the past few months, money market rates have continued to be around zero, although with a slight upward trend. The three-month Libor increased from 0.05% at the time of the December 2011 assessment to 0.10% in mid-March 2012. (cf. chart 5.1). Rising Libor rates have also been observed for other maturities.

The slight increase in the three-month Libor reflects a certain normalisation on the money market, after the exceptional liquidity expansion in summer 2011 had resulted in unusually low interest rates.

Long-term interest rates still at historically low levels

Owing to the subdued economic outlook and the European debt crisis, interest rate expectations are low, and safe assets such as Swiss Confederation bonds continue to be attractive. Against this background, yields on medium and long-term Confederation bonds fell to new historical lows. In mid-March, the yield on ten-year Confederation bonds was 0.8%.

Chart 5.1
Money market rates



Sources: Bloomberg, Reuters, SNB

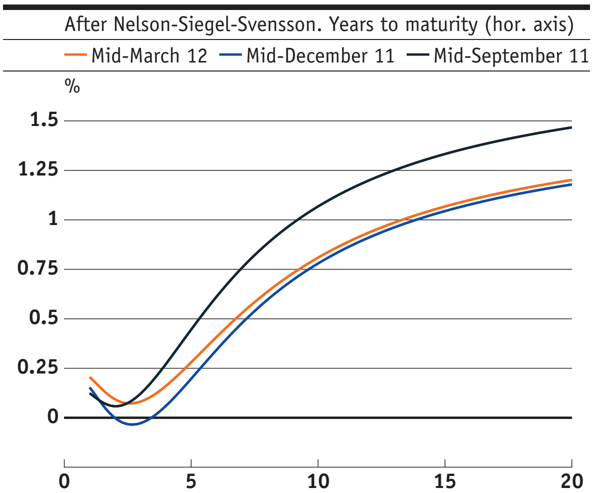
Further flattening of yield curve

The slight rise in short-term interest rates resulted in a flattening of the yield curve (cf. chart 5.2). The spread between the yield on ten-year Confederation bonds and the three-month Libor declined from 0.8 percentage points in mid-December to 0.7 percentage points in mid-March.

Real interest rates still low

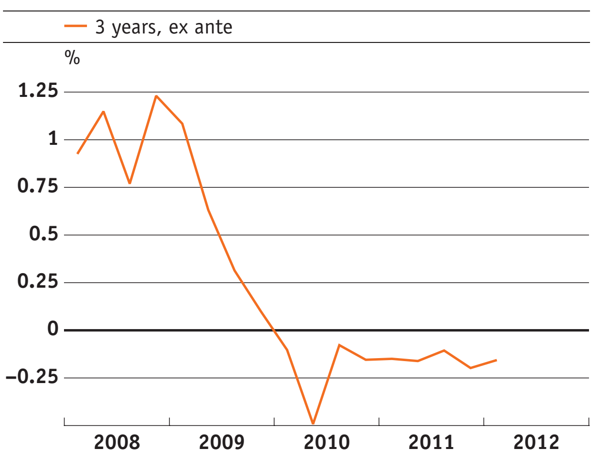
Estimated real three-year rates are currently around –0.1%, practically unchanged from their value of mid-December 2011 (cf. chart 5.3). Real rates are calculated using the three-year yield on Confederation bonds and the estimated inflation expectations based on the inflation forecasts produced by various SNB models.

Chart 5.2
Term structure of Swiss Confederation bonds



Source: SNB

Chart 5.3
Estimated real interest rate



Source: SNB

5.3 Exchange rates

Slight appreciation of Swiss franc

The Swiss franc has strengthened somewhat since the December monetary policy assessment (cf. chart 5.4). In mid-March, one euro cost CHF 1.21, compared to CHF 1.23 in mid-December. Over the same period, the Swiss franc/dollar exchange rate fell from CHF 0.94 to CHF 0.93. As a result, the export-weighted nominal exchange rate has also appreciated slightly since December.

Monetary conditions dominated by exchange rate movements

As the three-month Libor has hardly changed, the Monetary Conditions Index (MCI) is currently being driven almost exclusively by exchange rate movements. The positive value of the MCI in March indicates that monetary conditions have become marginally less expansionary since the last assessment (cf. chart 5.5).

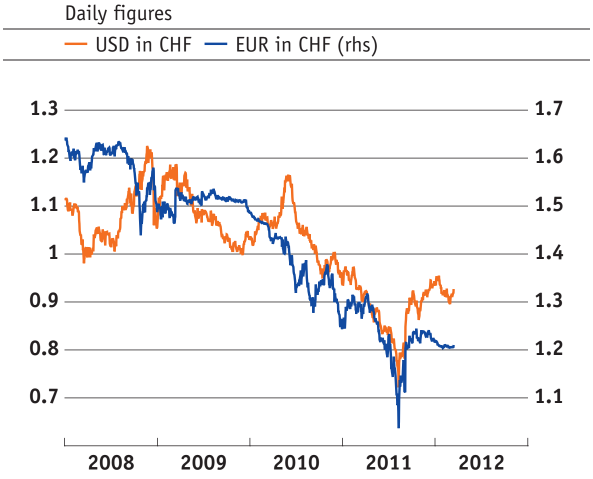
The MCI combines changes in the three-month Libor and in the nominal export-weighted external value of the Swiss franc. To take account of uncertainty regarding the relative impact of changes in interest rates and exchange rates, two different weightings are used for the MCI (3:1 and 5:1). The index is reset to zero at the time of the last monetary policy assessment, so a positive MCI value signifies a tightening of monetary conditions.

Real external value of Swiss franc remains high

The real export-weighted external value of the Swiss franc has decreased considerably since the introduction of the minimum exchange rate, but remains at a historically high level (cf. chart 5.6). It increased again marginally when the Swiss franc appreciated slightly in January. The real external value of the Swiss currency was still well above the long-term average, and even exceeded the previous peak of 1995. Thus, the Swiss franc is still high.

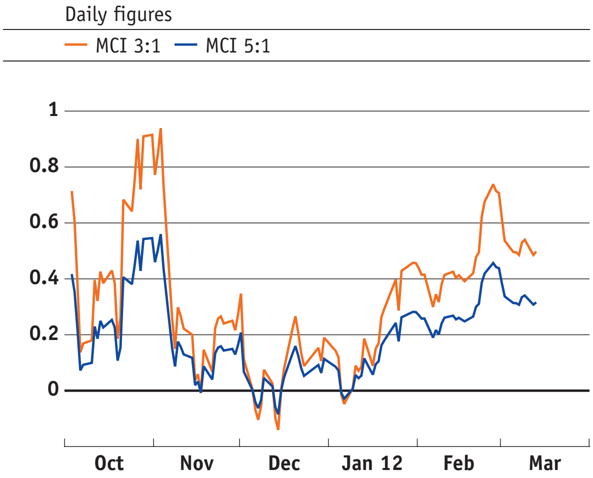
Notwithstanding the high real external value of the Swiss franc, Switzerland's current account surplus rose further in 2011. Investment income was responsible for the bulk of this rise. Structural factors, such as the capital-based old age pension system and the high proportion of international companies, ensure that there is virtually no link between Switzerland's net current account and exchange rate developments.

Chart 5.4
Exchange rates



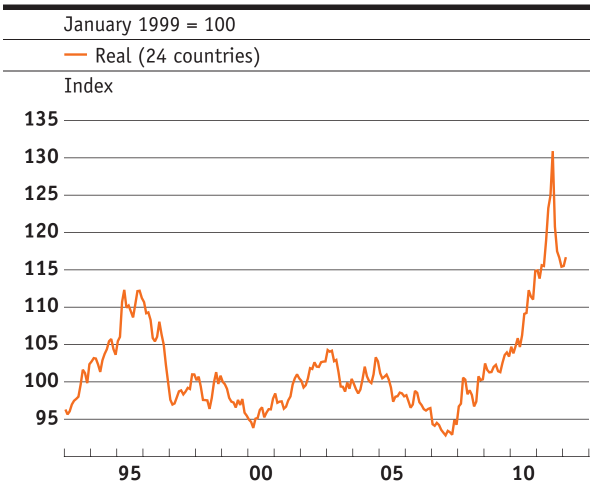
Source: SNB

Chart 5.5
MCI nominal



Source: SNB

Chart 5.6
Export-weighted external value of Swiss franc



Source: SNB

5.4 Stock markets

Rising share prices

Since the December monetary policy assessment, share prices have recovered further, mirroring the developments on international stock markets. The SMI has now recouped the bulk of the losses sustained in summer 2011, although in mid-March it was still lower than the average for the first half of 2011 (cf. chart 5.7).

The recovery from the low levels reached in August occurred in an environment of increased risk appetite on the part of investors. The index of 30-day expected SMI volatility had risen sharply in summer 2011, and subsequently declined to the levels seen in the first half of that year. Since the assessment of mid-December, the index has changed very little.

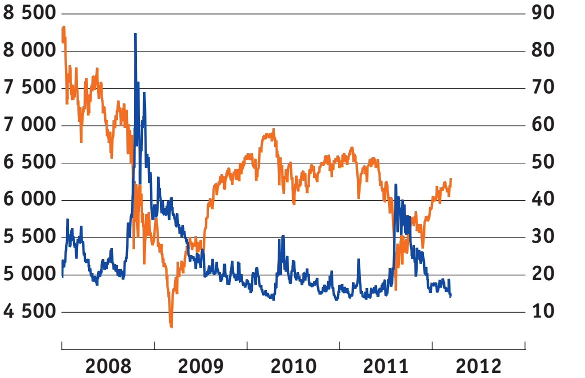
Industrial and financial stocks still lower than in first half of 2011

The sectoral breakdown of the SPI shows that the industrial and consumer goods sectors have recovered strongly over the past few months (cf. chart 5.8). While industrial share prices are still below the levels recorded in the first half of 2011, the consumer goods segment has already picked up sufficiently to match those levels. Prices of shares in the health care sector are trading higher than in the first half of 2011, whereas financial stocks are still distinctly below the levels recorded in that period.

Chart 5.7
Share prices and volatility

Daily figures

— SMI — Volatility index of SMI (rhs)

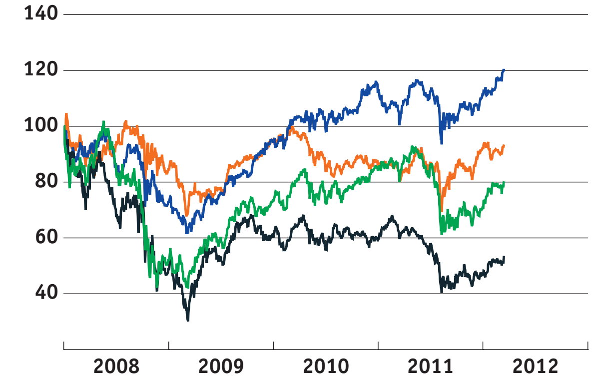


Source: Thomson Financial Datastream

Chart 5.8
Selected SPI sectors

Beginning of period = 100, daily figures

— Health care — Consumer goods — Financials — Industrials



Source: Thomson Financial Datastream

5.5 Monetary and credit aggregates

Monetary base at historically high level

The monetary base, which comprises banknotes in circulation plus domestic banks' sight deposits with the SNB, has decreased slightly since September but is still close to its historical peak, reached in the wake of the measures taken in August and September to expand liquidity (cf. chart 5.9). In February 2012, it amounted to CHF 222 billion, compared to CHF 253 billion in September 2011 and around CHF 45 billion before the escalation of the financial and economic crisis in autumn 2008.

Strong growth of broad monetary aggregates

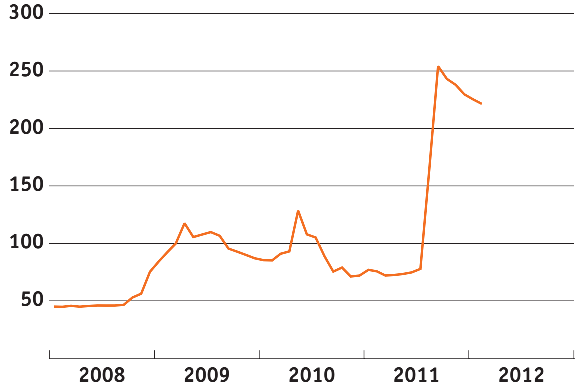
The broad monetary aggregates, which are defined as means of payment held by households and companies, have once again shown strong growth over the past few months. In February, M1 (cash in circulation, sight deposits and transaction accounts) was 10.6% above its level a year earlier, while M2 (M1 plus savings deposits) was 8.9% higher and M3 (M2 plus time deposits) rose by 6.4% in the same period (cf. table 5.1).

In autumn 2008, M1 and M2 had grown substantially as a result of reallocations from term deposits to sight and savings deposits. Since then, all three broad monetary aggregates have risen steadily and independently of the wide fluctuations in the monetary base. This reflects the fact that banks' excess reserves have been extremely high since the end of 2008, and that money creation within the banking system is not currently being constrained by the regulatory requirements on minimum reserves. The steady increase in the broad monetary aggregates essentially stems from the low interest rates and the high lending activity by banks.

Chart 5.9
Monetary base

Seasonally adjusted

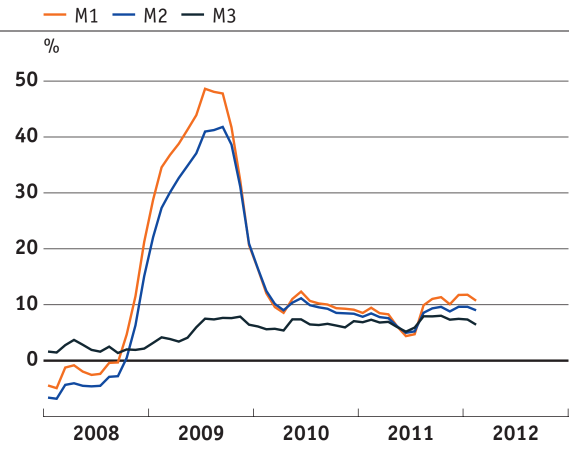
In CHF billions



Source: SNB

Chart 5.10
Growth of monetary aggregates

Year-on-year change



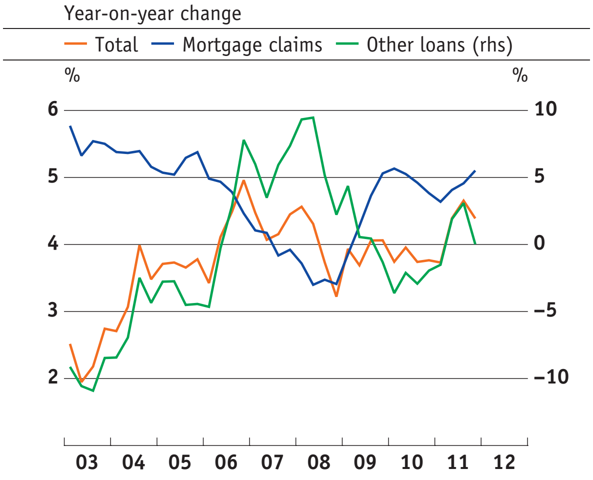
Source: SNB

Growth in lending growth slows a little

Compared to previous years, lending growth has slowed a little. In the fourth quarter of 2011, bank lending was 4.3% above the level one year earlier, following an increase of 4.6% year-on-year in the third quarter. The decline is mainly due to developments in the other loans category (cf. chart 5.11), which increased year-on-year by 0.3%, compared with 3.1% in the previous quarter. Both secured and unsecured other loans contributed to this marked slowdown (cf. table 5.1). Since growth in other loans is highly cyclical, the weaker growth points to a further slowdown in economic activity. In contrast to the other loans category, growth in mortgage claims, which make up around four-fifths of total bank lending, accelerated slightly.

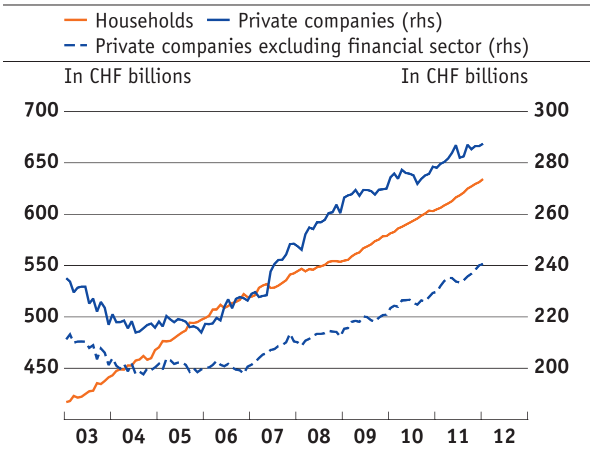
The lending breakdown shows that lending to both households and private companies increased further, although the results of the SNB's quarterly lending survey suggest that banks tightened their lending conditions slightly in the fourth quarter. Lending to households grew by around CHF 28 billion (4.7%), compared to the same quarter one year earlier. As regards corporate lending, loans to financial corporations decreased by CHF 1 billion (–2.0%), while loans to companies in other sectors rose by CHF 11 billion (4.7%).

Chart 5.11
Growth in bank loans in CHF



Source: SNB

Chart 5.12
Loans to households and companies



Source: SNB

Monetary aggregates and bank loans Table 5.1

Year-on-year change in percent

	2011	2011 Q1	Q2	Q3	Q4	2011 December	2012 January	February
M1	**8.7**	**8.7**	**6.3**	**8.7**	**11.0**	**11.7**	**11.7**	**10.6**
M2	**7.8**	**7.9**	**6.2**	**7.8**	**9.3**	**9.6**	**9.5**	**8.9**
M3	**7.0**	**7.0**	**6.0**	**7.3**	**7.6**	**7.4**	**7.3**	**6.4**
Bank loans total [1, 3]	**4.1**	**3.6**	**3.8**	**4.6**	**4.3**	**3.9**	**4.2**	
Mortgage claims [1, 3]	4.8	4.6	4.8	4.9	5.1	5.2	5.1	
Households [2, 3]	4.5	4.4	4.4	4.5	4.8	4.9	5.0	
Private companies [2, 3]	5.6	5.2	5.5	5.7	6.1	6.2	5.6	
Other loans [1, 3]	0.6	−0.8	−0.3	3.1	0.3	−1.8	−0.4	
Secured [1, 3]	4.0	6.6	3.6	4.4	1.7	1.6	3.4	
Unsecured [1, 3]	−1.6	−5.1	−2.8	2.4	−0.5	−4.0	−2.9	

1 Monthly balance sheets.
2 Credit volume statistics.
3 Growth rates for the bank loans item and for its components include information provided by banks on changes in their classification practices. Consequently, they may deviate from growth rates published in the *Monthly Bulletin of Banking Statistics*.

Source: SNB

Business cycle trends
SNB regional network

Report for the attention of the Governing Board of the Swiss National Bank for its quarterly assessment of March 2012

First quarter of 2012
The Swiss National Bank's delegates for regional economic relations are constantly in touch with a large number of companies from the different economic sectors and industries. Their reports, which contain evaluations by these companies, are a valuable source of information for assessing the economic situation. The following pages contain a summary of the most important results of the talks held in January and February 2012 with 243 representatives of various industries on the current and future situation of their companies and the economy in general. The selection of companies is made according to a model that reflects Switzerland's industrial structure. The reference parameter is GDP excluding agriculture and public services. The companies selected differ from one quarter to the next.

Region	Delegate
Central Switzerland	Walter Näf
Eastern Switzerland	Jean-Pierre Jetzer
Geneva	Marco Föllmi
Italian-speaking Switzerland	Fabio Bossi
Mittelland	Martin Wyss
Northwestern Switzerland	Daniel Hanimann
Vaud-Valais	Aline Chabloz
Zurich	Markus Zimmerli

Summary

The economic situation stabilised in the first quarter of 2012. Uncertainty about future developments has decreased slightly. Margins remained a focus of attention, but the exchange rate situation was no longer given the same prominence as in the previous quarter. The minimum exchange rate for the Swiss franc against the euro has made it easier for many companies to plan ahead and has mitigated the hectic element of these companies' business activities. The global economy remains fragile but this did not depress confidence to the same extent as in the previous quarter.

There are, however, still considerable differences between sectors. In construction, business activity was below the dynamic level seen in preceding quarters, as a result of weather conditions. In the manufacturing industry and the services sector, business stagnated. Overall, demand for labour was also unchanged from the previous quarter.

The outlook for real growth in turnover has brightened slightly in all sectors. However, capital expenditure and demand for staff are likely to stagnate. Average technical capacity utilisation is normal to high in all three sectors and is likely to remain stable in the coming months.

The main worries about future developments focus on uncertainty relating to the consequences of the European debt crisis, the risk of a slowdown in the global economy, and further exchange rate developments. Substantial portions of the economy are experiencing persistently heavy pressure on their margins. In many places, therefore, a range of measures are being implemented to cut costs further.

1 Business activity

Manufacturing

In manufacturing, business activity has stabilised. Consequently, the marked loss of momentum registered in the previous quarter did not continue. Overall, real turnover remained unchanged compared with both the previous quarter and the same quarter of the previous year. In a number of sectors, the exchange rate situation remained a dominant issue, although it was less prominent than in the previous quarter.

The situation varied from one industry to another. In the chemical, pharmaceutical, plastics and watchmaking industries, turnover was higher than in the previous quarter. By contrast, a downward trend was registered by the metals processing industry, in particular.

Demand from the emerging economies of Asia was again the main driver for the export sector, though slightly less so than in the previous quarter. Stimulus also came from North America and Brazil. In Europe, demand mainly came from Germany, Scandinavia and Eastern Europe. Within the euro area, a clear gap became evident between the countries bordering the Mediterranean (excluding France), where demand dropped significantly in some cases, and the other member states.

Construction

The construction industry saw another relatively significant fall-off in momentum, in many cases due to weather conditions. Turnover declined slightly compared with the previous quarter. Developments were especially negative in civil engineering; a slight drop in turnover was registered from both preparatory construction work and the finishing trade. While residential construction continued to boom, the situation in commercial and industrial construction remained subdued.

Once again, a number of respondents expressed misgivings about real estate market risk, while others regarded the risk as non-existent. They pointed in particular to the generally more cautious lending policies adopted by the banks.

Services

In the services sector, real turnover remained around the same level as in the previous quarter but improved slightly year-on-year.

Good business momentum was registered by architectural and engineering firms, the travel industry and banks, with the latter reporting a continuation of the slightly positive trend that had asserted itself in the previous quarter, due in particular to lending business. The previous quarter's negative trend at transport operators and logistics companies was no longer in evidence.

Business activity in wholesaling declined again but the situation in retailing eased somewhat, with turnover remaining virtually unchanged from the previous quarter. Cross-border shopping remained a serious problem for many companies. A stabilisation was registered in the hotel industry, which had previously suffered from declining turnover. However, in many cases extensive promotional campaigns and price discounts were needed to achieve this. The tourist trade in mountain regions saw a pronounced decrease in guests from Germany and the Netherlands due to exchange rate factors. In some cases, the shortfall has been offset by increased demand from visitors from Asia, Russia and Brazil, as well as from within Switzerland. In the area of seminars and company events, hotels are noticing that companies are paring down their costs.

2 Capacity utilisation

Overall, capacity utilisation was judged to be normal. The previous wide variation between the sectors has decreased. Finished product inventories are still considered somewhat too high.

In manufacturing, capacity utilisation is rated as normal, whereas in the previous quarter it was still considered to be relatively high. It remained very high among producers of electrical appliances and relatively high in the watchmaking industry and the related supply trade. Utilisation of production capacity was very low among textile companies, while in the machinery and metal processing industries it was relatively low.

In construction, technical capacity utilisation was rated as relatively high, although not quite as high as in the previous quarter. Most of the companies that took part in the survey were very satisfied with their level of utilisation. Some companies were unable to meet demand in full.

In the services sector, capacity utilisation was rated as normal overall, as in the preceding quarters. A relatively high level of capacity utilisation was recorded by architectural and engineering firms, real estate companies and IT companies. Representatives from the financial industry reported a normal level of capacity utilisation. Retailers and the hotel industry reported persistently low utilisation, although hotels in cities, in particular, reported buoyant business tourism.

3 Demand for labour

Overall, the demand for labour has remained virtually unchanged. In manufacturing, it declined further compared with the previous quarter. The companies included in the survey still considered that their headcounts were slightly too high and continued to exercise great restraint in staffing policy. On the whole, they were not replacing employees when they left, and any seasonal increases in demand were met by taking on temporary staff or through overtime work. The benefits of free movement of labour were often mentioned.

In construction, the demand for labour increased only slightly. The majority of respondent companies rated the size of the current workforce as being in line with demand. The difficulties experienced in recruiting suitable personnel have not intensified further. Some companies reported that the situation had eased slightly. Specialised staff are still highly sought-after, however, and some companies cited the shortage of staff as a constraint.

In the services sector, staff levels were generally considered appropriate. High staff requirements were reported by IT companies, architectural and engineering firms and telecommunications companies. The hotel industry was still overstaffed. In addition, some staff recruitment agencies reported that headcounts were on the high side.

Overall, recruiting was considered to be as difficult and time-consuming as usual. Staff availability was very tight in the electrical appliance industry. In construction, it was mainly civil engineering firms that complained of a dearth of specialists. Architectural and engineering firms, real estate companies and travel agencies also reported difficulties in recruiting staff.

Per capita labour costs increased considerably across all three sectors compared with the previous quarter. In many industries, the market for specialists has dried out, leading to cost pressure in some instances. The new collective agreements for the hospitality industry, which took effect on 1 January 2012, also increased per capita labour costs. Architectural and planning firms, staff recruitment agencies and freight forwarders also faced higher per capita labour costs.

4 Prices, margins and earnings situation

Many companies are still facing the problem of low or unsatisfactory profitability, accompanied by relatively high capacity utilisation. In all sectors of the economy margins were judged to be lower than usual, although this view was held by fewer respondents than in the previous quarter. Tougher competition, flagging demand and the sustained strength of the Swiss franc were given as the main reasons for the contraction of margins. Pressure to optimise costs is continuing.

The minimum exchange rate for the Swiss franc against the euro brought welcome planning security for many companies and even prevented some from going out of business. However, some manufacturing companies and service providers still regard the current exchange rate level as critical. It was felt that the situation would worsen if sales volumes were to come under pressure as well as margins.

Of the 243 companies surveyed, 121 said their margins were lower than usual. However, across all three sectors the vast majority of these firms have positive or very positive margins. Only a very low proportion of companies reported zero or negative margins.

At the 121 companies where margins are lower than usual, the majority (nearly 60%) said they were responding with efforts to raise productivity. Although around a quarter of these 121 companies reduced the size of their workforce in Switzerland and about 10% relocated some production to other countries, only one-third said that these measures had been taken principally in response to the exchange rate. Moreover, similar measures had been decided on by companies that reported margins to be within the usual range or above it. In particular, 10% of companies in this group also reported that they were relocating some production to other countries. Such action is mainly being taken by companies that already have a foreign presence. Companies considering such action showed higher demand for specialists with experience of building up sales organisations and production plants in the Far East. Other widespread measures include hiring freezes, investment freezes and increased working hours without any increase in pay.

With regard to the change in the margin situation in recent months, 50 of the 243 companies surveyed reported that their margins had decreased. They cited price discounts in Swiss francs and lower sales volumes as the main reasons for this.

The manufacturing industry is still suffering most from pressure on profit margins. All industries are affected, but the phenomenon has been particularly pronounced in the textile industry. On the one hand, most companies expect to see a slight reduction in purchase prices in the coming months; on the other hand they anticipate a need to make further concessions in selling prices in Swiss francs.

In construction, below-average margins were more common in structural engineering than in civil engineering or the finishing trade. Low interest rates have made it far easier for new construction firms to enter the market, leading to further pressure on margins. Forecasts show that both purchase and selling prices are expected to decline.

Within the services sector, wholesaling, retailing and the hotel industry still reported low margins. Staff recruitment agencies have now joined their ranks. Representatives of the financial industry, who have been complaining about tight margins for some time, also gave a relatively negative assessment of the situation. By contrast, IT and telecommunications companies and travel agencies rated their margins as being normal to above average.

5 Outlook

The uncertainty about future developments is still in evidence, but has lessened somewhat. Companies' employment and investment plans in Switzerland remain cautious to restrained. Turnover expectations for the coming months have increased in all sectors compared to the previous quarter.

In manufacturing, companies in all industries apart from machinery expect turnover to rise slightly over the next six months. Accordingly, technical capacity utilisation should be slightly higher in these industries. By contrast, there are no signs of a positive effect on employment.

In construction, seasonally adjusted turnover and capacity utilisation should increase slightly in the coming months. Many companies report that their order books for this year are already either well-filled or very full. This could also stimulate employment to some extent.

In general, companies in the services sector are cautiously optimistic about the business trend in the next six months. Most industries in this sector expect to see a slight rise in turnover. Capacity utilisation and headcounts are likely to remain largely unchanged from their current levels. Representatives of real estate firms, the IT industry and transport operators are very optimistic about their turnover prospects, while commercial banks and insurers are relatively confident. Retailers and the hotel industry expect that turnover will be flat and that capacity utilisation in the months ahead will remain at the present relatively low level.

With regard to global risks, the uncertainty stemming from the European debt crisis and the slowdown in the global economy were the most frequently cited factors.

The unusually low margins remain a source of concern for the companies affected. Further price discounts are considered inevitable by many respondents and, together with the persistently tough competitive situation, will keep up the high pressure on margins. A few respondents expressed unease about the persistently low interest rates and the associated risks in the real estate segment. There were also, however, reports of banks exercising slightly greater caution in lending.

The slightly lower overall uncertainty with regard to the future path of the economy is reflected in investment plans: equipment investment in all three sectors is likely to at least remain unchanged at current levels. This represents a marginal improvement over the previous quarter, when expectations were negative. In the manufacturing industry in particular and to a lesser extent in the services sector, there are plans to boost capital expenditure slightly, especially in the area of equipment investment. Manufacturing companies are still showing a greater willingness to invest abroad rather than in Switzerland. This applies particularly to companies already operating abroad.

Chronicle of monetary events

The chronicle summarises the most recent monetary events. For events dating further back, please refer to SNB press releases and the *Annual Report* at www.snb.ch.

March 2012

At its quarterly assessment of 15 March 2012, the SNB reaffirms that it will continue to enforce the minimum exchange rate with the utmost determination and is prepared to buy foreign currency in unlimited quantities for this purpose. The target range for the three-month Libor will remain unchanged at 0.0–0.25%. The SNB will continue to maintain liquidity on the money market at an exceptionally high level. Even at the current rate, it considers the Swiss franc to be still high. The SNB stands ready to take further measures at any time if the economic outlook and the risk of deflation so require.

On 8 March, the SNB publishes its annual results for 2011, reporting a consolidated profit of CHF 13.5 billion, following a loss of CHF 19.2 billion in the previous year. At CHF 13.0 billion, the result for the parent company, upon which the profit distribution is based, is CHF 440.2 million less than the consolidated result. The difference is due to the inclusion of the stabilisation fund companies in the consolidated result.

December 2011

At its quarterly assessment of 15 December, the SNB reaffirms that it will continue to enforce the minimum exchange rate with the utmost determination and is prepared to buy foreign currency in unlimited quantities. It is leaving the target range for the Libor at 0.0–0.25%, and continues to aim for a three-month Libor close to zero. Even at the current rate, the SNB considers the Swiss franc to be still high and should continue to weaken over time. The SNB goes on to say that it will continue to maintain liquidity at exceptionally high levels, but has decided not to set a specific target level for sight deposits at present. The SNB stands ready to take further measures at any time if the economic outlook and the risk of deflation so require.

September 2011

On September 15, the SNB decides, in coordination with the Bank of England, the Bank of Japan, the European Central Bank and the Federal Reserve, to offer US dollar liquidity with a term of 84 days to cover the end of the year. These tenders will be conducted in addition to the 7-day operations. The first 84-day US-dollar liquidity operation will be carried out on 12 October 2011.

At its quarterly assessment of 15 September, the SNB affirms that it will enforce the minimum exchange rate of CHF 1.20 per euro set on 6 September with the utmost determination. It is prepared to buy foreign currency in unlimited quantities. It continues to aim for a three-month Libor at zero and will maintain total sight deposits at the SNB at significantly above CHF 200 billion. If the economic outlook and deflation risks so require, the SNB will take further measures.

On 6 September, the SNB announces that, with immediate effect, it will no longer tolerate a EUR/CHF exchange rate below the minimum rate of CHF 1.20. It will enforce this minimum rate with the utmost determination and is prepared to buy foreign currency in unlimited quantities. In addition, the SNB emphasises that, even at a rate of CHF 1.20 per euro, the Swiss franc is still high and should continue to weaken over time. If the economic outlook and deflation risks so require, the SNB will take further measures.

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