Business cycle signals
Results of the SNB company talks

First quarter of 2018

Report submitted to the Governing Board of the Swiss National Bank for its quarterly assessment.

The appraisals presented here are based on discussions between the SNB's delegates for regional economic relations and company managers. A total of 240 company talks were conducted between mid-January and the end of February.

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Central Switzerland	Walter Näf
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Geneva/Jura/Neuchâtel	Jean-Marc Falter
Italian-speaking Switzerland	Fabio Bossi
Mittelland	Roland Scheurer
Northwestern Switzerland	Daniel Hanimann
Zurich	Rita Kobel

Key points

- Discussions with company representatives indicate that growth in the Swiss economy remained robust and broad-based in the first quarter of 2018 and that the outlook is favourable. Risk is perceived to have eased and companies are focusing on opportunities.
- Quarter-on-quarter and relative to the same quarter a year earlier, real turnover once again increased noticeably, and utilisation of technical production capacity has normalised in many industries.
- Margins improved considerably, especially in manufacturing, thanks to higher turnover, productivity increases, price rises and the stronger euro since mid-2017; overall, they are now at the level that company representatives regard as normal.
- Company representatives expect the positive dynamic in real turnover to be sustained over the coming six months, due in large part to the favourable economic environment internationally.
- Companies say they are planning to hire more staff and increase investment slightly, however they also drew attention to the shortage of specialised personnel more frequently than in the past.

CURRENT SITUATION

Ongoing strong turnover growth

Many companies continued to benefit from the positive momentum apparent at the end of 2017 in the first quarter of 2018 – indeed, in some cases, their position even strengthened. The company talks confirm that business performance remains buoyant – particularly in manufacturing, as in the previous quarters.

Company representatives report robust quarter-on-quarter growth in real turnover, i.e. turnover adjusted for changes in sale prices (cf. chart 1; for guidance on interpreting the charts, see the relevant section at the end of this report). A comparison with the corresponding quarter a year ago also points to vigorous growth, with all three sectors – services, manufacturing and construction – contributing to this favourable development.

Export industries continue to perform strongly; company representatives attribute this to trade with Europe (including Eastern Europe), North America and Asia. There are signs of improvement in Russia, and positive signals are emanating from India. Companies supplying capital goods as well as goods for the automotive and medtech industries recorded particularly solid results.

Utilisation of production capacity normal overall

Overall, utilisation of technical production capacity, which had been recovering since the second half of 2016 (cf. chart 2), has now normalised.

Around half of the companies interviewed rated their technical capacity utilisation as normal. A further 30% reported slight or substantial overutilisation. Certain firms have added more shifts to meet increased demand and avoid delivery backlogs; more orders are to be delivered immediately and in full rather than in tranches.

Staff numbers on the low side

At present, staff numbers in all three sectors are judged to be slightly too low. The situation has thus tightened quarter-on-quarter. A third of the companies interviewed described their staffing as somewhat low or much too low.

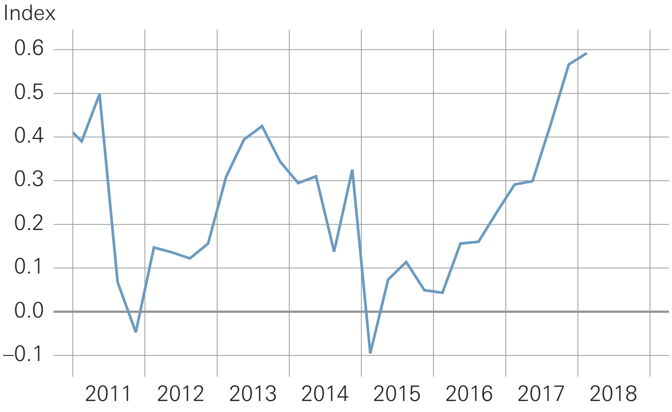
Recruitment problems became more pronounced in manufacturing during the quarter under review. This is partly due to improved labour market conditions in Switzerland and partly to the fact that it has become harder to recruit staff from neighbouring countries as their economies have picked up. It is proving particularly difficult to recruit engineers, professionals and – in all industries – IT specialists. Companies are also reporting that they are finding it increasingly challenging to source enough apprentices.

Margins normalise

Discussions with company representatives indicate that profit margins have returned to normal. In manufacturing in particular, the situation has improved considerably since mid-2017. Higher turnover and potential for price increases in some areas have played a big role here. Margins are now at roughly the same level as before the discontinuation of the minimum exchange rate against the euro.

Chart 1

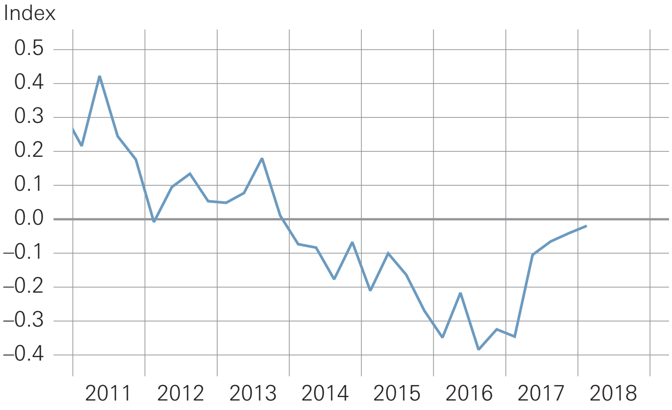
TURNOVER COMPARED TO PREVIOUS QUARTER



Developments in real turnover compared to the previous quarter. Positive (negative) index values signal an increase (decrease).
Source: SNB

Chart 2

CAPACITY UTILISATION



Current utilisation of technical capacity or infrastructure compared to a normal level. A positive (negative) index value signals a higher (lower) utilisation than normal.
Source: SNB

DEVELOPMENTS IN INDIVIDUAL INDUSTRIES

The challenges posed by structural changes, notably the accelerating shift to e-commerce, remain an important topic. The course of business is currently pleasing, with real turnover slightly up quarter-on-quarter and with respect to the same period a year earlier; retail trade has even performed slightly better than wholesale. Nonetheless, retailers continue to report below-normal margins. The decline in sales prices, which was still evident in many areas in 2017, is now only apparent in the non-food segment. There are also some signs that cross-border shopping is tapering off.

Finance once again made a positive showing, with all business lines contributing. Higher trading volumes on the stock markets have been an important driver here, helping to lift the first-quarter margins of companies active in this area significantly. The managers interviewed described their margins as 'within the normal range' overall.

Business in the hospitality industry improved notably. Real turnover was significantly higher quarter-on-quarter and markedly higher compared to the same quarter the previous year. Most regions recorded an uptick in tourism, particularly from Asia and the US – but also increasingly from Germany and the Netherlands. This positive development was due to a general improvement in the economic environment, exceptional weather and snow conditions (a base effect, as weather conditions were much less favourable the previous year), the exchange rate situation and Switzerland's reputation as a safe destination. Although margins at hotels the SNB visited were higher than normal, margins at restaurants were still slightly below normal levels.

Transportation and logistics companies as well as law firms, fiduciary companies, consultancies and facility management services reported favourable results.

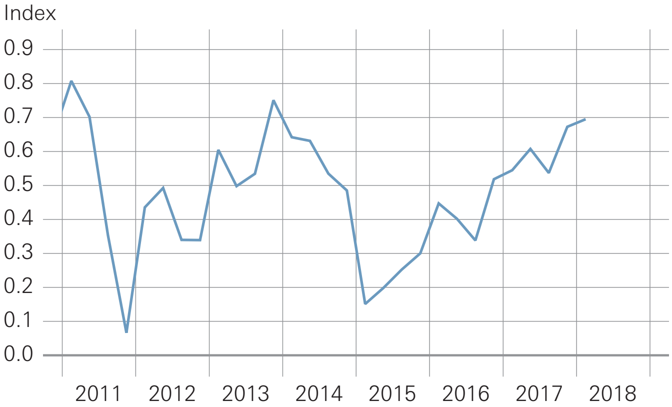
Momentum in the information and communications technology industry, which had been very high, seems to have moderated slightly, and margin pressure remains on the high side. The key business drivers continue to be digitalisation, automation and regulation.

In manufacturing, all industries reported higher turnover than in the previous quarter. For the first time in five years, company representatives judged capacity utilisation to be above normal; it was particularly high in metals manufacturing and processing. The trend of noticeably improved performance in the watchmaking industry and its suppliers was maintained in the first quarter of 2018. Having improved substantially, mechanical engineering is now very well placed and deems its margins to be somewhat higher than normal. By contrast, companies in printing and packaging continued to report tighter-than-usual margins.

Momentum in construction remains relatively high, both in the building industry and in ancillary trades. In the quarter under review, this was not primarily due to residential construction, but to activity in the finishing trade and – owing to favourable weather – civil engineering work. Margin pressure persists, especially in structural engineering. There are few signs that construction activity may be slowing, however it should be noted that the supportive effect of public infrastructure projects is substantial.

Chart 3

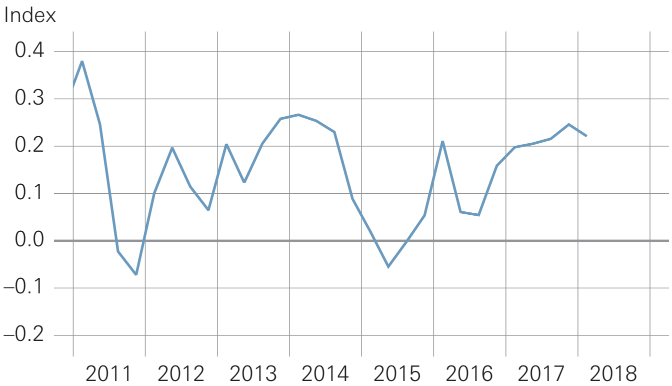
EXPECTED TURNOVER



Expected developments in real turnover in the coming six months. Positive (negative) index values indicate higher (lower) turnover expectations.
Source: SNB

Chart 4

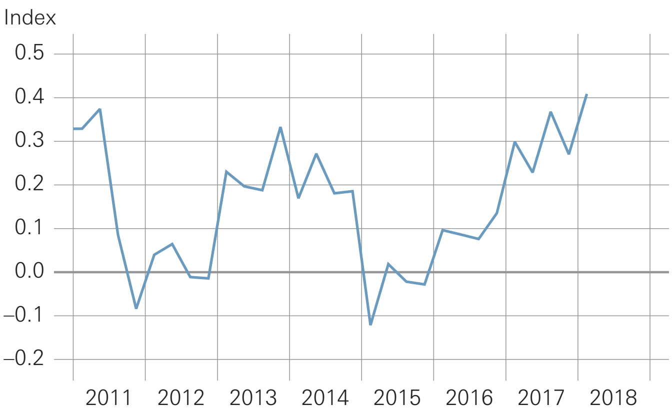
EXPECTED CAPACITY UTILISATION



Expected developments in utilisation of technical capacity or infrastructure in the coming six months. Positive (negative) index values indicate higher (lower) utilisation expectations.
Source: SNB

Chart 5

EXPECTED EMPLOYMENT



Expected developments in staff numbers in the coming six months. Positive (negative) index values indicate higher (lower) expectations.
Source: SNB

OUTLOOK

Widespread confidence

The company managers interviewed by the SNB delegates remain markedly optimistic about their business prospects for the coming six months. Overall, real turnover is expected to rise (cf. chart 3) in all three sectors. Factors contributing to this optimism include the favourable international economic situation, intensified market development efforts, improved exchange rate conditions, and the possibility of pushing through price increases in some areas. Orders for 2018 (and beyond in some cases) are looking very solid for many companies.

The confidence of the business community is also reflected in higher expected utilisation of technical production capacity and/or infrastructure in the next two quarters (cf. chart 4). Companies are thus planning to invest slightly more in both equipment and buildings. More than a quarter of the companies investing in equipment are simultaneously expanding their production capacity. With the exception of the pharmaceutical industry, manufacturing companies in particular are intending to make larger investments.

Slight price rises

As in the fourth quarter of 2017, company representatives anticipate that both purchase and sales prices will rise in the coming six months. They typically expect rises in purchase prices to be linked to demand-induced increases in raw material prices and to a weakening of the Swiss franc relative to last year. Any such price increases are normally passed on to customers. Managers claim that it has generally become easier to push through price increases, some of which were even implemented at the beginning of 2018.

Significant staff increases planned

The indications of personnel shortages and the prospect of higher capacity utilisation are affecting companies' recruitment plans: managers from all three sectors are planning to increase staff numbers in 2018 (cf. chart 5). More temporary hires are being contracted on a permanent basis. Many firms are focusing on in-house training and apprenticeships in an effort to attract and retain personnel. No industry indicated plans to cut staff.

Rising wages

Based on information obtained in the talks, salary increases already granted or planned for 2018 average 1.1%, and many companies are intending to pay general bonuses – a rarity in recent years. Above-average wage increases are being offered in the IT industry.

ENVIRONMENT AND RISKS

Not only do companies rate uncertainty in their operating environment as relatively low, they also say that they are actively looking for opportunities given the favourable economic situation. They highlight the increasing shortage of specialist staff and delivery bottlenecks (commodities) as risks in this regard.

Internationally, potential hazards mentioned include geopolitical risks and protectionist trends. With respect to Europe, a number of company representatives pointed to unsolved structural problems.

Many company representatives continue to find the complex domestic regulatory environment very burdensome. A renewed appreciation of the Swiss franc is also seen as a risk. Digitalisation is being actively debated and explored in many industries; most company representatives believe opportunities outweigh any risks. On the other hand, they express unease about the impact of low interest rates on the real estate market, where the number of vacant housing units is on the rise.

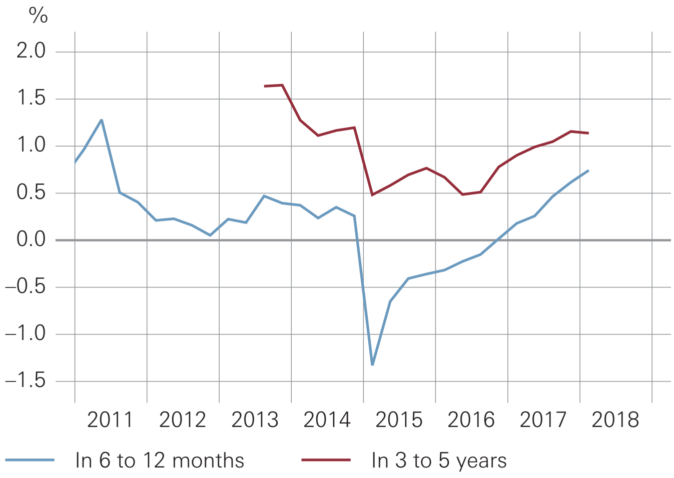
Most managers describe the weakening of the Swiss franc against the euro since the summer of 2017 as 'helpful'.

INFLATION EXPECTATIONS

As part of the exchange of views, the delegates regularly ask company representatives about their short and long-term inflation expectations as consumers, as measured by the consumer price index.

Chart 6

EXPECTED INFLATION



Source: SNB

In the first quarter of 2018, the upward trend in short-term inflation expectations, which had begun during 2015, continued: expectations for the next six to twelve months now average 0.7%, compared to 0.6% in the previous quarter (blue line in chart 6). The rising trend of mid-term inflation expectations (time horizon of 3–5 years) since 2016 has flattened out: company representatives expect inflation to average 1.1% over this period, whereas they had projected 1.2% in the previous quarter (red line in chart).

About this report

Approach
Each quarter, the SNB's delegates for regional economic relations hold talks with managers of companies throughout Switzerland. The main results of these discussions are summarised in the 'Business cycle signals' report.

Approximately 240 companies are visited every quarter. The selection of companies reflects the industrial structure of the Swiss economy based on GDP and employment. Industries subject to stronger cyclical fluctuations are somewhat over-represented, while the public sector and agriculture are not taken into consideration. Different companies are visited from one quarter to the next.

In the talks, the SNB's delegates capture primarily qualitative information. The discussions are nevertheless structured in such a way as to allow the delegates to grade part of the qualitative information received according to a numeric scale. This enables the results to be aggregated and represented graphically.

The five-tier scale ranges from 'substantially higher' or 'much too high' (+2), 'slightly higher' or 'somewhat high' (+1), 'the same' or 'normal' (0), 'slightly lower' or 'somewhat low' (–1), to 'substantially lower' or 'much too low' (–2).

Interpreting the charts
The charts are to be regarded as a numeric summary of the qualitative information received. The index value shown represents the average of the findings from all companies visited. When interpreting the curves, particular relevance should be attached to their overall development, rather than to their numeric level or individual changes.

Additional information
Further information on the 'Business cycle signals' report is available at www.snb.ch, *The SNB, SNB regional network*.

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