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Abstracts

1. Swiss monetary policy in 1999

The Governing Board of the Swiss National Bank, in agreement with the Federal Government, intends to continue implementing a pragmatic monetary policy in 1999. The Swiss economy will thus be granted the monetary leeway necessary for a balanced development. In particular, the uncertainties emanating from the forthcoming introduction of the euro are to be taken into account.

2. Economic and monetary developments

The seasonally-adjusted monetary base grew at an accelerated pace from July to October 1998. This was mostly due to the strong expansion of liquidity with which the National Bank countered the signs of strain in the money market and the higher Swiss franc. As a result, short-term interest rates declined markedly. The growth of the broadly defined money stock M3 moved up slightly compared to the previous period, but remained weak year-on-year.

The recovery of the Swiss economy continued in the third quarter. While private consumer spending and investment in plant and equipment gained some momentum, exports picked up at roughly the same rate as in the first half of the year. Real gross domestic product exceeded the previous year's level by 1.8%. The different economic sectors showed a significantly different picture. In the strongly export-oriented manufacturing sector buoyancy weakened markedly chiefly as a result of the recession in East Asia. The service sector, however, continued to develop favourably. The employment outlook was also considerably brighter in this sector than in manufacturing. Employment on the whole stagnated in the third quarter compared to the previous period. The unemployment rate continued to decline and only amounted to 3.4% in October. Consumer prices remained stable from July to October; in November they even declined somewhat. While the price increase in the service sector was slightly higher than in the second quarter the prices for goods declined mostly as a result of lower crude oil prices.

3. Seigniorage and central bank profit

This article deals with the problem of measuring seigniorage in a paper money system. Seigniorage, i.e. the income from the money-issuing prerogative, is separated from central bank profits. The paper also discusses the issue of distribution of central bank profits to the government. Two conclusions for economic policy are drawn. First, achieving seigniorage in countries with full-fledged fiscal and tax systems should not be a consideration when laying down an optimal monetary policy. Second, the transfer of central bank profits to the government should be carried out without jeopardising the implementation of a well-conceived monetary policy.

4. Direct investment in 1997

Direct investment abroad went up significantly in 1997. Capital exports grew by 20% to Sfr 24 billion.

Capital holdings abroad rose by Sfr 41 billion to Sfr 232 billion, and the labour force abroad increased by 9% to 1.59 million persons employed. Foreign direct investment in Switzerland doubled as a result of the higher influx from the EU to Sfr 7.2 billion. Foreign capital holdings in Switzerland reached Sfr 82 billion (previous year: Sfr 73 billion).

5. Switzerland's investment position in 1997

Both Switzerland's foreign assets and foreign liabilities again rose markedly in 1997. In addition to the direct investment holdings, they comprise, in particular, portfolio investments, bank loans and deposits as well as the National Bank's monetary reserves. Foreign assets increased by 17% to Sfr 1459 billion. Foreign liabilities rose by 29% to Sfr 1016 billion. The strong growth was mainly due to new investments and the price hikes of securities investments. The net investment position decreased by Sfr 10 billion to Sfr 443 billion. In the case of the foreign assets, investments denominated in Swiss francs became less significant. With regard to foreign liabilities, however, the Swiss franc share rose significantly.

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1. Swiss monetary policy in 1999

The Governing Board of the Swiss National Bank, in agreement with the Federal Government, intends to continue conducting a basically generous monetary policy in 1999. The Swiss economy will thus be granted the monetary leeway necessary for an enduring economic recovery. The problems in East Asia and the slowdown in growth in the United States are likely to lead to a weakening of economic activity in western Europe. The Swiss economy should, however, achieve further satisfactory growth. The intentions of the Governing Board duly take into account the uncertainties associated with the forthcoming launch of the euro.

The Swiss National Bank - as is known - has the task of pursuing a monetary policy serving the interests of the country as a whole. Within the scope of monetary policy, the National Bank must help to create conditions that facilitate balanced - and also sustained - economic development. The best contribution monetary policy can make is to guarantee price stability. The National Bank considers this to be achieved with an annual inflation rate of 1% - 2%.

Once more it must be emphasised that for the National Bank price stability is a means to an end rather than an end in itself. Economic theory shows convincingly that the absence of price stability can lead to a considerable loss of growth, and consequently a loss of welfare. To this must be added that notably the weaker members of the community suffer from inflation. Price stability is therefore an important social issue.

The economic recovery, which got under way in 1997 and was initially supported mainly by exports, spread to every sector of the economy in 1998. Despite the slowdown triggered by the problems in various parts of the world, the real rate of growth of Switzerland's gross domestic product in 1998 is expected to be approximately 2%, in line with the National Bank's forecast. Exports to East Asia contracted considerably. Nevertheless, these losses were offset by a vigorous expansion of exports into the countries of the European Union and the United States and by the revival of domestic demand. Inflation, at 0.1%, is below original expectations.

In 1999, economic growth is likely to weaken somewhat both in Switzerland and in other countries in continental Europe. In Switzerland, real gross domestic product is still expected to expand by approximately 1.5%. The export sector will come to feel the results of the external disturbances, while domestic demand should continue to act as a welcome pillar of the economy. In view of the moderate real growth, unused production capacities are unlikely to be reduced any further. The pressure on consumer prices will therefore remain insignificant. Inflation will probably rise to 1%, with about half this amount being attributable to the increase in value-added tax.

In the past year the development of the Swiss franc rate was only affected to a minor degree by preparations for the European Monetary Union. Of decisive importance, however, were the turbulences in the international financial markets, which boosted the demand for Swiss francs. The National Bank countered the effects on the exchange rate by repeatedly supplying the money market with generous liquidity. Currently the exchange rate is on an adequate level. Should the introduction of the euro pass without a hitch, no particular difficulties are to be expected for Switzerland. The National Bank and the European Central Bank will pursue similar policies. There is considerable agreement both as regards the goals and the operational framework of monetary policy. This will be conducive to exchange rate stability.

As early as a year ago, the National Bank pointed out that the development of the monetary base is becoming more and more difficult to interpret. While the circulation of one-thousand-franc banknotes, which had risen considerably in the previous years, seems to have returned to normal the development of sight deposits exceeded the National Bank's forecasts. In the wake of international financial problems several banks increased their liquid funds. The already mentioned additional supplies of liquidity also contributed to the growth of sight deposits.

The problems of interpretation referred to induced the National Bank to pay closer attention to the course of the broader money stock M3. After having risen markedly in 1996 and at the beginning of 1997, its growth has since levelled off considerably. The moderate development does not point to inflationary risks. In the implementation of the monetary policy intentions for 1999 no marked change in money market rates is to be expected.

There are no indications of an immediate danger of inflation. Nevertheless, it is necessary to be on the alert. It is a well-known fact that monetary policy decisions only have an influence on developments with a time lag of approximately two years.

The National Bank will in future, too, watch a number of other indicators. Particular attention is paid to factors pointing to the cyclical development of economic activity and the exchange rate. In the present environment it is difficult to gauge the future economic development. Should it deviate considerably from present perceptions, the Governing Board would, of course, reassess the situation.

6. Chronicle of monetary events

Financial aid to Brazil

On 19 November 1998, the Swiss National Bank, in agreement with the Federal Department of Finance, gave its approval to an activation of the New Arrangements to Borrow (NAB) in favour of Brazil to the amount of 9.2 billion Special Drawing Rights, equivalent to approximately Sfr 17.5 billion. The National Bank's share will amount to 455 million SDRs (approximately Sfr 880 million) in the form of a credit to the International Monetary Fund (IMF). Since a number of NAB members are currently unable to make a contribution, the proportion to be provided by the remaining members has increased correspondingly - from 4.6 percent to 4.99 percent in the case of the National Bank. This is the first time that the New Arrangements to Borrow of the IMF have been activated. The NAB constitute parallel agreements to the General Arrangements to Borrow (GAB). They entered into force on 17 November 1998 after having been signed by the Group of Ten and 14 other participating countries. By this agreement, the 25 participating countries undertake to grant the IMF credits in exceptional circumstances and in the event of a shortage of funds according to a distribution key laid down in advance. Under the GAB and the NAB the IMF can borrow up to 34 billion SDRs. That is double the amount previously available under the GAB alone. The Federal Parliament already passed a decision on Switzerland's accession to the NAB in December 1997.

The Bank for International Settlements (BIS) also participated in the extensive international financial aid totalling $ 41.5 billion in favour of Brazil. The BIS extended a credit of $ 13.28 billion. The members of the Group of Ten and eight additional countries provided a guarantee for US $ 12.93 billion to the BIS. Switzerland's contribution amounts to $ 250 million. It will be granted by the Swiss National Bank in the context of the Federal Decree on Switzerland's cooperation in international monetary measures and is equipped with a federal guarantee.