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Contents

Abstracts

1. Conclusions for monetary policy

The Swiss National Bank adhered to its generous monetary policy in the second quarter of 1999. Following a lowering of the discount rate at the beginning of April, the three-month Swiss franc eurorates fell to just below 1%. Since the Swiss franc rate also weakened, monetary conditions were still a little more expansive than in the first few months of the year. In planning its monetary policy, the National Bank must, on the one hand, support the economic recovery and, on the other, not endanger price stability. So far, the expansionary monetary policy has been justified. It contributed significantly to stabilising economic activity without jeopardising price stability. Should the expected economic upswing actually set in, it would in principle be desirable for short-term interest rates to firm somewhat. At the same time, the National Bank has to ensure that the year-end passes without a hitch. It is well prepared for this task and ready to meet any disruptions in the financial sector with a flexible supply of liquidity.

2. Economic and monetary developments

The international economic situation brightened in the first half-year. Several small East Asian countries overcame the recession, and in Japan the strong decline in business activity came to a standstill. In Europe, although economic growth remained restrained, confidence in the economy grew perceptibly. The main pillar of the world economy, however, continued to be robust domestic demand in the United States.

In Switzerland, economic activity began to stabilise in the second quarter of 1999. Real gross domestic product increased by 1.1% compared with the previous year. While private consumption and investment in plant and equipment lost some of their momentum, building investment increased substantially following the strong decline in the first quarter. Overall, however, domestic demand expanded somewhat less markedly than in the previous period. By contrast, stronger stimuli emanated from the export of goods and services. The labour market - with a certain time lapse - showed the effects of the economic slowdown. Employment rose only insignificantly in the second quarter compared with the previous period. Unemployment continued to fall, albeit at a slower rate. In June, for the first time since August 1992, it had again dropped below 100,000. The number of job seekers also receded.

Inflation edged up slightly between April and August, one main reason being the prices of imported goods, which were rising again for the first time since the fourth quarter of 1997. This was a reflection of the higher oil prices and of the marked decline in the export-weighted real Swiss franc rate since October 1998. In addition, robust consumer demand in certain service sectors led to substantial price advances.

3. Risks and costs in payment and settlement systems

In most countries, payment and settlement systems are overseen by a government regulatory body. This supervision derives from the fact that disruptions in the flow of payments can threaten the stability of the financial system and do harm to the economy. Overseers of payment and settlement systems face a trade-off of risks and costs that have to be combined in a socially optimal way. This paper presents these risks and costs in relation to the Swiss interbank payment system (SIC) and the securities settlement system SECOM. Furthermore, the project of a new foreign exchange settlement system, the CLS-Bank, as well as some other foreseeable developments are discussed.

4. Chronicle of monetary events

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1. Conclusions for monetary policy

After temporarily losing momentum in 1998, the Swiss economy stabilised during the first half of the year. The brighter international economic situation and the generous monetary conditions prevalent for some time now were factors supporting this process. Exports increased slightly and – after the weather-induced sharp drop at the beginning of the year – construction activity picked up. Private spending and investment in plant and equipment remained high. The dynamic pace of this development did slow down somewhat, however, compared to the second half of 1998. The labour market – with a certain time lapse – showed the effect of the economic slowdown. Employment rose only insignificantly in the second quarter compared with the previous period and unemployment continued to fall, albeit at a slower rate. However, the growing number of employment openings and the more optimistic employment outlook point to higher growth in the second half of the year.

Inflation edged up slightly between April and August. One main reason was the price of imported goods, which rose for the first time since the fourth quarter of 1997. This was a reflection of the higher oil prices and of the marked decline in the export-weighted real Swiss franc rate since October 1998. In addition, robust consumer demand in certain service sectors led to substantial price advances. Other factors, such as the continually falling prices for communications services and the stable prices for durable goods helped to keep inflation at bay. This continued downward pressure on prices is largely the result of the heavy competition inside and outside of Switzerland as well as cheaper production processes.

Given the restrained economic development, the National Bank continued to pursue its generous monetary policy. Following a lowering of the discount rate on 8 April, the three-month Swiss franc eurorates fell to just below 1%. Since the Swiss franc rate also weakened, monetary conditions were still slightly more expansive than in the first few months of the year. This was only partially reflected in the monetary aggregates, however. As a result of the commercial banks' falling demand for sight deposits with the National Bank, growth of the seasonally-adjusted monetary base weakened despite the generous supply of liquidity. The expansion of the money stock M1, by contrast, which includes the most liquid bank deposits, accelerated. The money stock M3, which comprises savings and term deposits in addition to M1, grew at a slightly higher rate than in the first quarter. It was especially bank loans to domestic borrowers that rose significantly for the first time in several years.

While short-term interest rates remained low, the long-term rates firmed toward the middle of the year. In addition to the developments emanating from the international interest rates, slightly higher inflation and stronger demand for capital from domestic borrowers may also have been factors favouring rising interest rates. Coupled with an increase in the banks' lending activity, this is a sign that the temporary economic downward trend is over. Improved consumer sentiment in July, growing confidence in the construction sector as well as optimistic expectations in the industrial sector point in the same direction. Positive cyclical signals are also coming from abroad. The US economy remains dynamic with moderate inflation. In Europe, too, there are now clear signs that the economy has come out of its lull and economic activity is picking up. The Swiss export industry is likely to benefit especially from this new-found momentum.

The National Bank seeks to pursue a monetary policy which, on the one hand, supports the economic recovery and, on the other hand, does not endanger price stability. So far, the expansionary monetary policy has been justified. It contributed significantly to stabilising the economic activity without jeopardising price stability. Should the expected economic upswing actually set in, it would in principle be justified for short-term interest rates to firm somewhat. At the same time, the National Bank has to alliviate any financial concerns regarding the passage into the next century. It is well prepared for this task and ready to meet any disruptions in the financial sector with a flexible supply of liquidity.

4. Chronicle of monetary events

Federal Decree on Switzerland's cooperation in international monetary measures amended to increase credit limit

The Federal Decree on Switzerland's cooperation in international monetary measures enables the country to take part in international support operations intended to prevent or remedy serious disruptions in international monetary relations. Loans are generally financed by the National Bank, with the Federal Government guaranteeing their repayment, including interest. So far, the available credit line amounted to 1 billion Swiss francs. At the end of 1998, Switzerland had outstanding guarantee and lending obligations of just under 930 million Swiss francs. The credit line had thus practically run out. The Federal Council, therefore, submitted a proposal to parliament to double the credit limit. In view of the significant rise in the flow of capital and goods since the mid-eighties, the increasing globalisation of the financial system, and its inherently greater proneness to crisis, the Federal Council considered such an increase to be justified. Parliament thus followed the proposal and in June of 1999 approved an increase of the ceiling from 1 to 2 billion Swiss francs.