# Swiss National Bank
# Quarterly Bulletin

March 1/2013 Volume 31

# Contents

# Monetary policy report

Report for the attention of the Governing Board of the Swiss National Bank for its quarterly assessment of March 2013
This report is based primarily on the data and information available as at 14 March 2013.

## 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 monetary policy assessment of March 2013. Section 1 ('Monetary policy decision of 14 March 2013') is an excerpt from the press release published following the 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 14 March 2013

## Swiss National Bank maintains minimum exchange rate

The Swiss National Bank (SNB) is leaving the minimum exchange rate of CHF 1.20 per euro unchanged. The Swiss franc is still high. An appreciation of the Swiss franc would compromise price stability and would have serious consequences for the Swiss economy. The minimum exchange rate is an important instrument in avoiding an undesirable tightening of monetary conditions. The SNB will therefore enforce this minimum rate with the utmost determination and, if necessary, is prepared to buy foreign currency in unlimited quantities for this purpose. In addition, the SNB is leaving the target range for the three-month Libor unchanged at 0.0–0.25%. It stands ready to take further measures at any time.

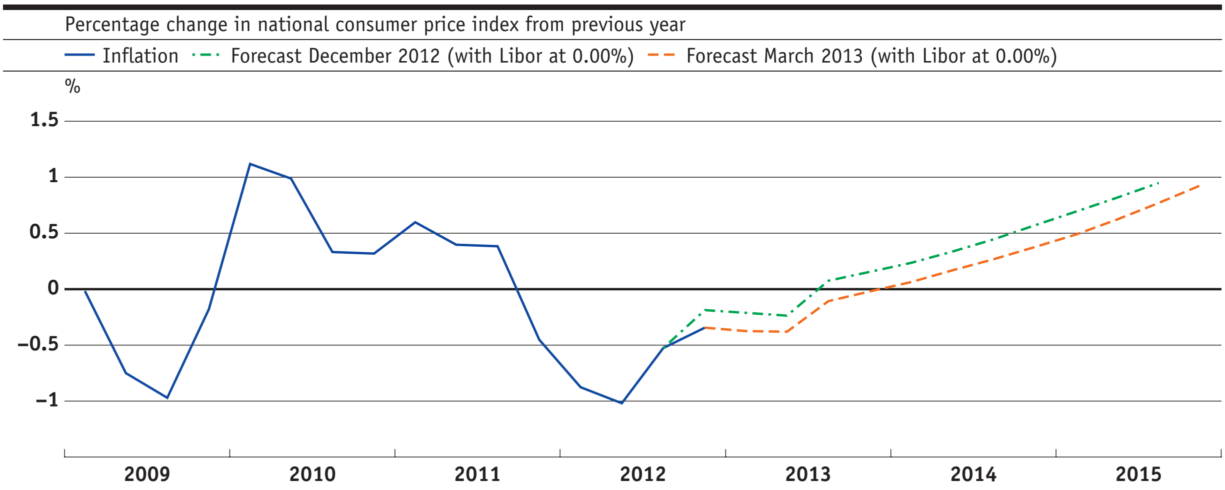
The SNB's conditional inflation forecast has been adjusted downwards appreciably over the entire forecast period compared to the previous quarter (cf. chart 1.1). In the fourth quarter of 2012, inflation was lower than expected due to the continued decline in import inflation. Furthermore, the economic outlook is once again somewhat subdued, especially for the euro area. The inflation forecast is based on an unchanged three-month Libor of 0.0% over the next three years. Under this assumption, the Swiss franc weakens over the forecast period. The SNB is expecting an inflation rate of –0.2% for 2013, 0.2% for 2014, and 0.7% for 2015. In the foreseeable future, therefore, there continues to be no threat of inflation in Switzerland.

Despite a considerable easing of tensions on the international financial markets, global economic growth was rather weak in the fourth quarter. In Switzerland, economic activity slowed as expected. The unemployment rate rose again slightly, despite a rise in employment. The SNB continues to anticipate growth of 1.0–1.5% for Switzerland in 2013.

On 13 February 2013, at the proposal of the SNB, the Federal Council activated the countercyclical capital buffer (CCB). As of September, banks will therefore be required to provide more capital backing for residential mortgage loans in Switzerland. The aim of the CCB is to strengthen the resilience of banks and counter imbalances on the mortgage and real estate markets. These imbalances have reached such a level that they pose a risk to the stability of the banking system and hence the Swiss economy. The SNB continues to monitor the momentum on the domestic residential mortgage and real estate markets closely.

Downside risks to the Swiss economy remain considerable. There is a risk that tensions in the euro area will increase again. In addition, uncertainty about future developments in the fiscal policies of numerous advanced economies is dampening consumer and investment confidence and poses risks to growth. The global economic situation and sentiment on the financial markets therefore remain vulnerable.

Chart 1.1
Conditional inflation forecast of December 2012 and of March 2013



Source: SNB

**Observed inflation in March 2013** Table 1.1

| | 2009 Q1 | Q2 | Q3 | Q4 | 2010 Q1 | Q2 | Q3 | Q4 | 2011 Q1 | Q2 | Q3 | Q4 | 2012 Q1 | Q2 | Q3 | Q4 | 2010 | 2011 | 2012 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Inflation | 0.0 | −0.7 | −1.0 | −0.2 | 1.1 | 1.0 | 0.3 | 0.3 | 0.6 | 0.4 | 0.4 | −0.5 | −0.9 | −1.0 | −0.5 | −0.3 | 0.7 | 0.2 | −0.7 |

**Conditional inflation forecast of December 2012 with Libor at 0.00% and of March 2013 with Libor at 0.00%**

| | 2012 Q1 | Q2 | Q3 | Q4 | 2013 Q1 | Q2 | Q3 | Q4 | 2014 Q1 | Q2 | Q3 | Q4 | 2015 Q1 | Q2 | Q3 | Q4 | 2013 | 2014 | 2015 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Forecast December 2012, Libor at 0.00% | | | | −0.2 | −0.2 | −0.2 | 0.1 | 0.2 | 0.2 | 0.3 | 0.4 | 0.6 | 0.7 | 0.8 | 0.9 | | −0.1 | 0.4 | |
| Forecast March 2013, Libor at 0.00% | | | | | −0.4 | −0.4 | −0.1 | 0.0 | 0.1 | 0.2 | 0.3 | 0.4 | 0.5 | 0.6 | 0.8 | 0.9 | −0.2 | 0.2 | 0.7 |

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.

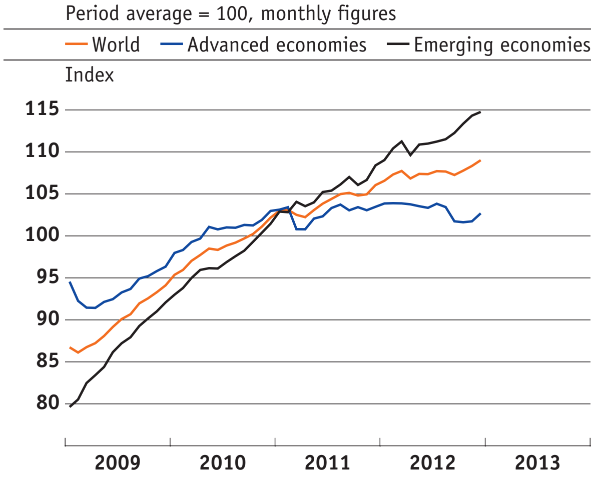
# 2 Global economic environment

Despite the notable easing on the international financial markets, global economic activity developed more weakly than expected in the fourth quarter of 2012. GDP stagnated in the US and Japan. The recession in the euro area worsened. Only in the emerging markets, above all in China, did the economy gain momentum.

Looking ahead, the SNB continues to assume a gradual recovery for the global economy. Global industrial production picked up somewhat towards the end of last year, but major regional differences remain (cf. chart 2.1). For 2013 and 2014, the SNB is forecasting slightly lower growth in the global economy than it did three months ago. This revision is primarily because of a weaker growth outlook in the euro area. Domestic demand in the euro area remains significantly impaired by restrictive fiscal policy, the deteriorating situation on the labour market and subdued investment prospects. In the US, the weak fourth quarter was marked by special factors. Investment and retail consumption should improve in the current year. For the Japanese economy, the SNB revised its growth forecast upwards on account of the fiscal package announced in January and the significant depreciation of the yen. Growth in the emerging economies, especially in Asia, should remain robust.

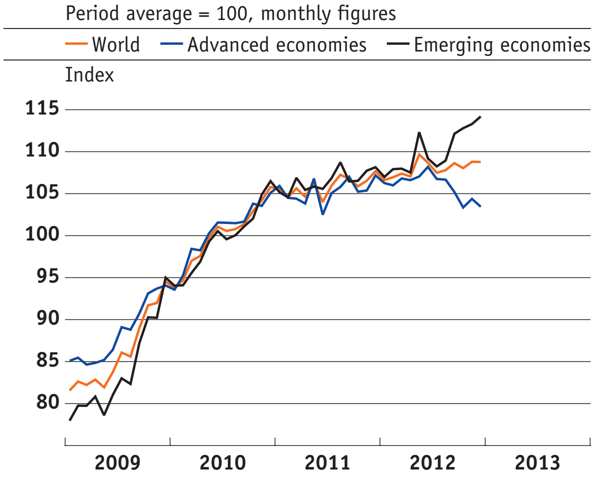
The global economy continues to face considerable downside risks. Measures taken by the European Central Bank (ECB) and an initial agreement on the impending spending cuts in the US have contributed to a calming of the financial markets. However, finding a lasting solution to the European financial and sovereign debt crisis continues to be a substantial challenge. Fiscal policy in other advanced economies also remains a source of uncertainty. Against this backdrop, it is to be expected that monetary policy in the advanced economies will remain characterised by low interest rates and high liquidity.

Chart 2.1
Global industrial production



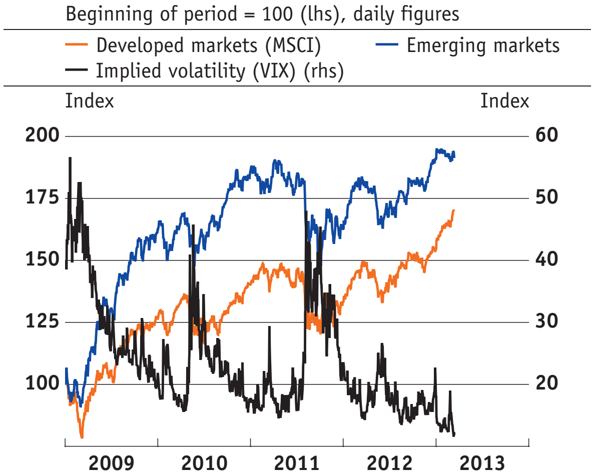
Sources: Netherlands Bureau for Economic Policy Analysis (CPB), Thomson Financial Datastream

Chart 2.2
Global exports



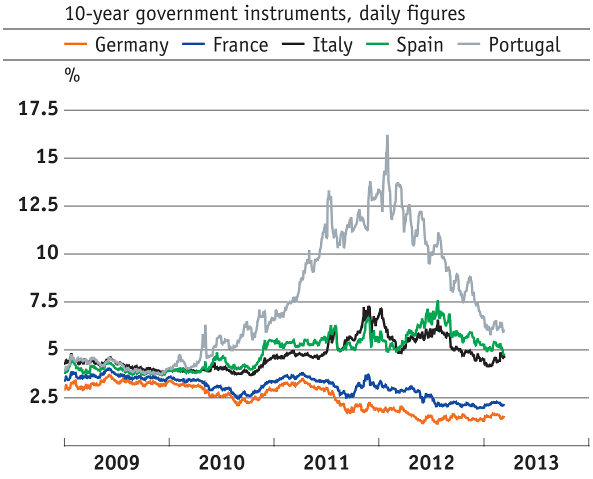
Sources: CPB, Thomson Financial Datastream

Chart 2.3
Stock markets



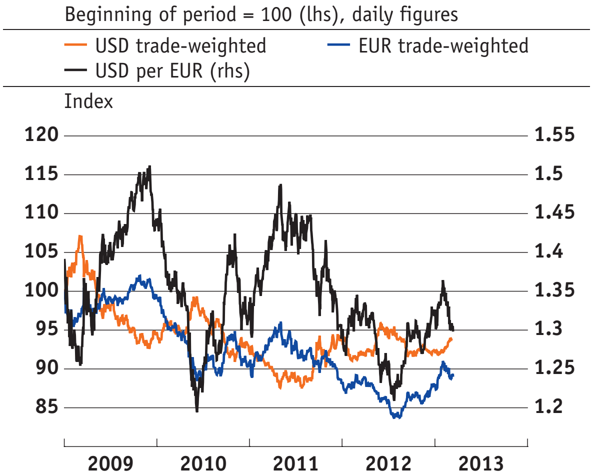
Sources: Reuters, Thomson Financial Datastream

Chart 2.4
European long-term interest rates



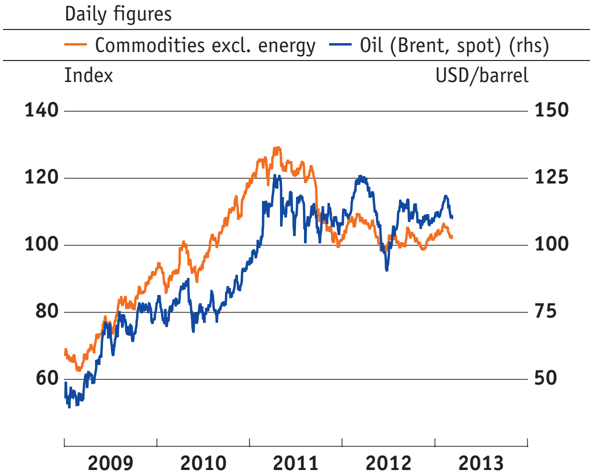
Source: Thomson Financial Datastream

Chart 2.5
Exchange rates



Sources: Reuters, Thomson Financial Datastream

Chart 2.6
Commodity prices



Sources: Reuters, Thomson Financial Datastream

## 2.1 International financial and commodity markets

The mood on the financial markets initially continued to improve at the beginning of 2013. Two factors contributed substantially to this. Fears about the future of the euro area receded further after the ECB announced its new securities purchase programme (Outright Monetary Transactions, OMT). And in the US, an initial fiscal policy agreement meant that a substantial correction to the national budget (fiscal cliff) could, for the time being, be avoided.

Global equity markets posted considerable gains at the beginning of the year (cf. chart 2.3). The S&P500 Index reached the level recorded at the end of 2007, and the Eurostoxx50 was at its highest level for the past 18 months. At the same time uncertainty, as measured by volatility indices, decreased. On the bond markets, yields fell on southern European government bonds (cf. chart 2.4) and risk premia declined against German bonds. Against this backdrop, the euro appreciated on a trade-weighted basis, while the US dollar remained stable (cf. chart 2.5).

In February, however, uncertainty on the European financial markets increased again slightly, following the elections in Italy.

Commodity prices fluctuated considerably at times, but on the whole trended sideways (cf. chart 2.6). Both oil prices and industrial commodity prices were at the same level in mid-March as in mid-December. By contrast, the prices of agricultural commodities dipped slightly due to positive harvest forecasts.

The SNB's forecasts are based on assumptions about the oil price and the EUR/USD exchange rate; over the forecast period it is assuming an oil price for Brent crude of USD 116 per barrel and an exchange rate of USD 1.34 to the euro.

## 2.2 United States

Fourth-quarter GDP in the US was stagnant after having grown considerably in the previous quarter (cf. chart 2.7). This weakening, however, was primarily the result of temporary factors such as reduced inventories and lower public spending on defence. Private domestic final demand continued to expand moderately. In 2012 overall, GDP rose by 2.2%. Aggregate economic capacity utilisation is still low and unemployment remains high, at 7.7% in February 2013 (cf. chart 2.10).

In the first quarter of 2013, a partial rebound effect is probable after the weak previous quarter. GDP should grow moderately thereafter. The SNB expects that private domestic demand and equipment investment will only pick up slowly. Residential construction should continue to expand strongly, though since it now makes a small contribution, it will only have a limited impact on economic activity. Fiscal policy will strongly curb growth this year. Overall, the SNB is projecting that annual GDP growth will remain practically unchanged at 2.2% for 2013 and 2.9% for 2014.

Consumer price inflation dropped to 1.6% in January, while core inflation has remained largely unchanged in recent months, at 1.9% (cf. charts 2.11 and 2.12). The rise in petrol prices in February might result in a slight increase in inflation in the coming months. However, given the high unemployment and weak wage growth, there is unlikely to be inflationary pressure in the medium term.

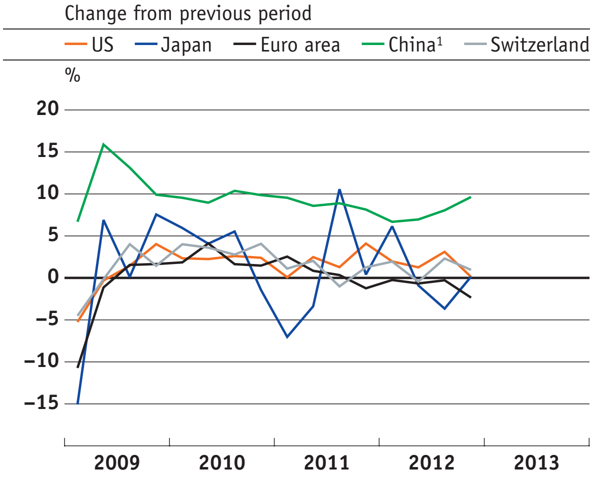
US monetary policy continues to be highly expansionary. The target range for the federal funds rate has been 0.0–0.25% since December 2008 (cf. chart 2.13), and as long as unemployment remains above 6.5%, its medium-term inflation forecast does not exceed 2.5%, and long-term inflation expectations continue to be well anchored, the US Federal Reserve anticipates that it will leave its target rate unchanged. As planned, it is also purchasing USD 85 billion worth of longer-term securities a month in order to keep long-term interest rates low.

## 2.3 Euro area

In the euro area, the recession deepened by more than expected. Economic output fell in the fourth quarter by 2.3%, which is the biggest fall for almost four years (cf. chart 2.7). GDP declined significantly in Germany and France, after having risen slightly in the previous quarter. The recession deepened in the southern member states. Investment activity in the euro area decreased further, which was also reflected in companies' continuing low demand for credit. Exports, which had hitherto been a key growth driver, now also fell for the first time since the last recession. Deliveries to the US and Japan in particular declined markedly. Unemployment reached a new high in January, at 11.9% (cf. chart 2.10).

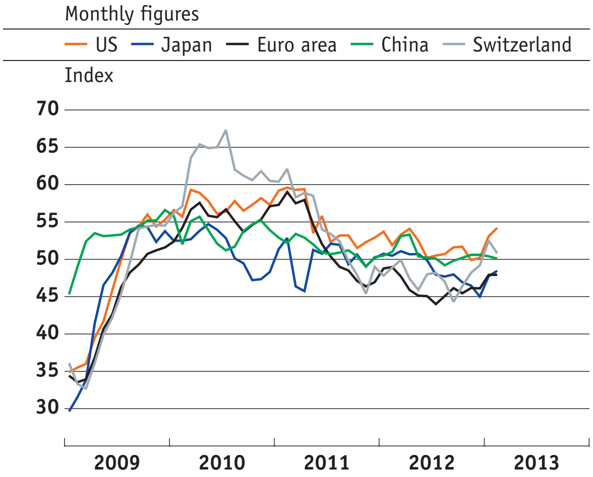
Indicators suggest that economic activity in the euro area will soon bottom out. In most countries, business confidence has improved slightly since the beginning of the year, especially so in Germany. This improvement in confidence – from levels that were at their lowest for three years – primarily reflects the expected pick-up in foreign trade. But the recession will probably only be overcome slowly. Restrictive fiscal policy continues to weigh on the economy of the euro area. Other inhibiting factors are the difficult labour market situation, uncertainty surrounding further structural reforms, the uneven transmission of expansionary monetary policy through the national credit systems, and structural problems in the construc-

Chart 2.7
Real GDP



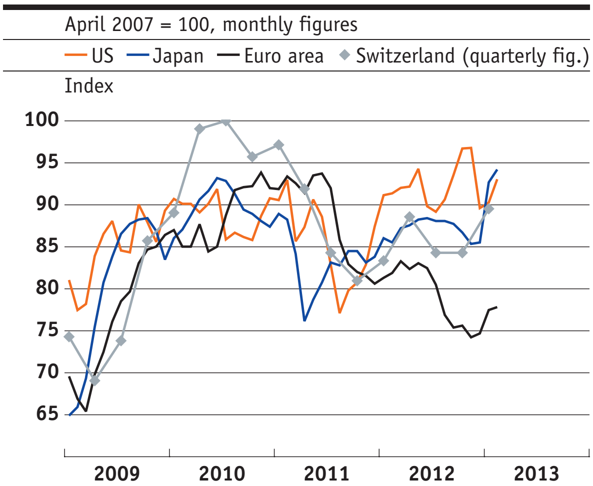

1 Estimate: SNB.
Sources: State Secretariat for Economic Affairs (SECO), Thomson Financial Datastream

Chart 2.8
Purchasing managers' indices (manufacturing)



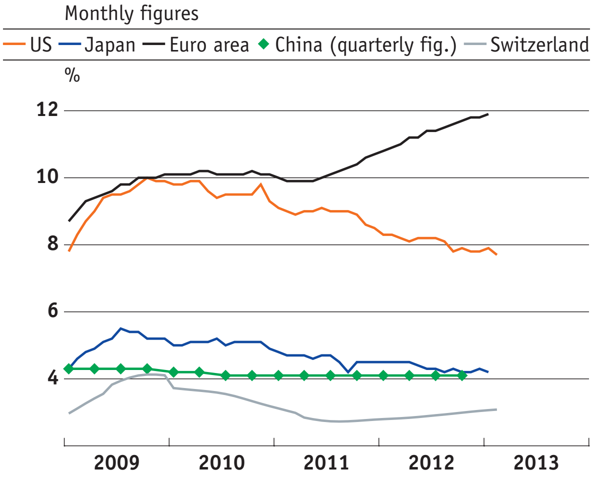

Source: Thomson Financial Datastream; copyright and database rights: Markit Economics Ltd 2009; all rights reserved

Chart 2.9
Consumer confidence index



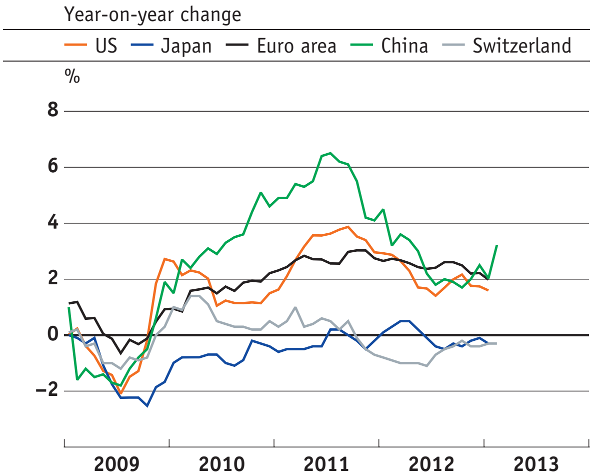

Sources: SECO, Thomson Financial Datastream

Chart 2.10
Unemployment rates



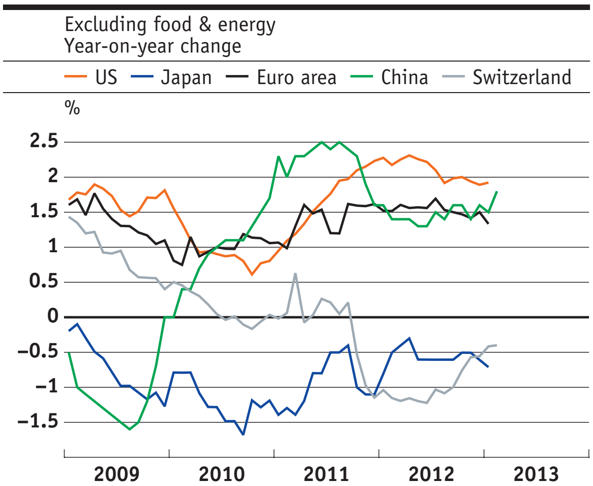
Sources: SECO, Thomson Financial Datastream

Chart 2.11
Consumer prices



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

Chart 2.12
Core inflation rates



Sources: CEIC, SFSO, Thomson Financial Datastream

tion industry. For this reason, continuing major differences in growth between the member states are to be expected. The SNB has revised its euro area GDP forecast downwards. For 2013, it expects a decline in GDP of 0.4%, similar to that of the previous year, while for 2014 it anticipates growth of 1.3%.

Consumer price inflation has continued to edge down. In February, according to a flash estimate, it reached 1.8%, in line with the ECB's price stability goal of "below, but close to, 2%" (cf. chart 2.11). Core inflation in January dropped only slightly, to 1.3% (cf. chart 2.12). In the coming months, consumer price inflation should be below 2%.

The ECB left its main refinancing rate unchanged at 0.75% (cf. chart 2.13). Since September it has been poised to implement its OMT programme if necessary. For the first time, commercial banks were also able to pay back some of the liquidity provided to them by the ECB a year ago for a maximum of three years. The ECB expects surplus liquidity to remain high, however.

## 2.4 Japan

In 2012, GDP increased by 2.0%. Major sources of stimulus were a subsidy programme and public investment for reconstruction following the earthquake in March 2011. In the second half of the year, however, exports and business investment declined considerably. GDP was stagnant in the final quarter (cf. chart 2.7).

Since the end of the year there have been increasing signs of a recovery: Industrial production and exports increased again, while business and household confidence improved considerably. The substantial depreciation of the Japanese currency since the middle of last year should provide a positive stimulus for the export industry. Furthermore, in January, the new government announced a further economic stimulus package worth some 2% of GDP. The core elements of the package are further public investment in reconstruction and the renewal of obsolete infrastructure. The SNB expects GDP growth of 1% for 2013 and a little over 2% for 2014.

In January, Japanese consumer prices were 0.3% lower than a year earlier (cf. chart 2.11). If prices for energy and food are excluded, they were even somewhat lower (cf. chart 2.12). The depreciation of the yen will cause inflation to rise in the coming months, but price momentum in the medium term should remain weak due to the negative output gap and low inflation expectations.

The Bank of Japan issued a joint declaration with the government, setting an inflation target of 2%, to be achieved "at the earliest possible time". Until now, the target had been 1%. Furthermore, it decided to continue its asset purchase programme indefinitely after having reached its objective for the end of 2013. It left the call money rate at 0.0–0.1% (cf. chart 2.13).

## 2.5 Emerging economies

The monetary – and in some cases fiscal – policy easing introduced in some emerging economies in 2012 contributed to a further economic recovery in the fourth quarter. However, demand from the advanced economies remained sluggish, and uncertainty surrounding global growth prospects continued to take its toll on investments.

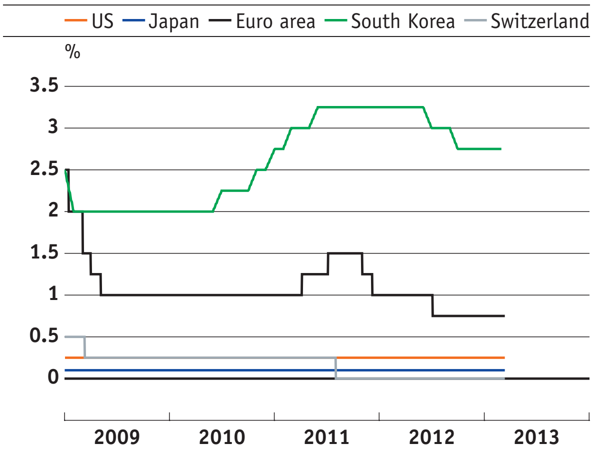
In China, GDP grew by 7.8% in 2012, the lowest value since the Asian crisis in the late 1990s. After earlier tightening measures had slowed down investment activity until the middle of the year, economic activity gained momentum again (cf. chart 2.7). This was aided by the more expansive monetary and fiscal policy, especially the targeted state investment in infrastructure and residential construction, and a recovery in intra-Asian trade. Activity increased in the newly industrialised economies in Asia such as South Korea, especially in the electronic and automotive industries. In Brazil, the moderate recovery continued thanks to comprehensive stimulus measures.

While the economic recovery in 2012 was most marked in China, the other emerging economies should also pick up in the coming months. In India and Brazil, investment demand is expected to join private consumption as a key growth driver, due especially to planned infrastructure projects and government incentives for foreign direct investment.

Consumer price inflation in the emerging economies fell last year. In China, as a result of a decline in food price inflation, it decreased from an average of 5.4% in 2011 to 2.6% in 2012, and in February 2013 it amounted to 3.2% (cf. chart 2.11). Core inflation in recent months has remained below 2% (cf. chart 2.12). In India, the annual inflation rate fell significantly, to 6.8% in February. In Brazil, however, it increased to 6.3% on account of the weak currency.

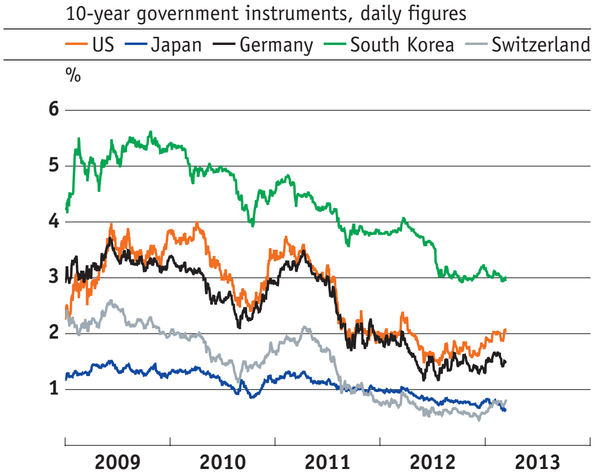
Monetary policy in the emerging economies has remained largely unchanged in recent months. India is a significant exception, where the decrease in inflation made it possible to ease minimum reserve requirements for banks, and to reduce reference interest rates in January.

Chart 2.13
Official interest rates




Sources: SNB, Thomson Financial Datastream

Chart 2.14
International long-term interest rates




Sources: SNB, Thomson Financial Datastream

# 3 Economic developments in Switzerland

Economic activity in Switzerland slowed significantly in the fourth quarter. According to the preliminary estimates of the State Secretariat for Economic Affairs (SECO), real GDP rose by 1.0% in the fourth quarter, following a rise of 2.3% the previous quarter. The slowdown in growth is attributable to a lack of stimuli from abroad: Above all, the weak European environment weighed on goods exports and therefore on value creation in manufacturing. By contrast, the domestic economy supported growth. Consumer spending in particular increased sharply, but investment also contributed to growth, rising for the first time in a year.

Due to the slowdown in growth, the negative output gap widened once again. Capacity utilisation in manufacturing remained at a low level. The labour market situation deteriorated again slightly.

With these quarterly estimates, the first preliminary results for 2012 as a whole are now available. With annual growth of 1.0%, economic development remained below its long-term average. For 2013, the SNB is expecting growth of 1.0–1.5%. The main burden on growth is likely to be weak demand from Europe.

## 3.1 Aggregate demand and output

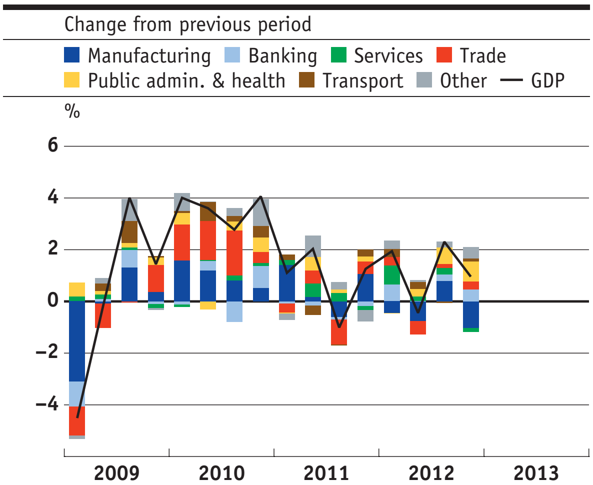
### Decline of value added in manufacturing

As expected, GDP growth recorded a quarter-on-quarter decline in the fourth quarter. In manufacturing, in particular, there was a significant decline in value added (cf. chart 3.1). However, business-related services also experienced a decline. By contrast, value added in most other industries increased in the fourth quarter. The finance sector and healthcare performed particularly dynamically. Value added in the hospitality industry increased for the third time in succession.

### Very negative contribution by foreign trade

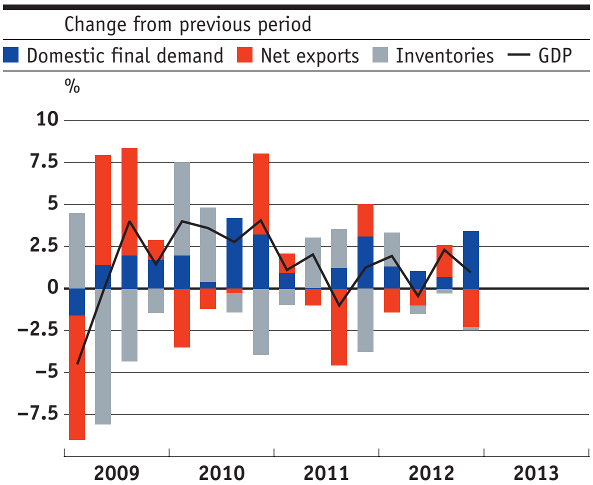
Net exports (excluding valuables) recorded a sharp decline in the fourth quarter (cf. chart 3.2). Whereas total exports stagnated compared to the previous quarter (cf. chart 3.3), total imports increased sharply (cf. chart 3.4). This resulted in a negative foreign trade contribution of 2.3 percentage points.

Chart 3.1
Contributions to growth, by sector




Source: SECO

Chart 3.2
Contributions to growth in demand




Source: SECO

Exports of goods and services revealed diverging tendencies. In most categories, goods exports recorded a significant decline, having posted strong growth in the previous quarter. The only export growth came from watches and precision instruments, as well as agricultural and forestry products. Weak demand from Europe weighed on the goods exports, whereas deliveries to Asia picked up.

In contrast to goods exports, exports of services rose strongly in the fourth quarter. A key factor here was higher receipts from licence and patent fees, but tourism exports likewise rose strongly. By contrast, receipts from merchanting stagnated, while receipts from private insurance even declined.

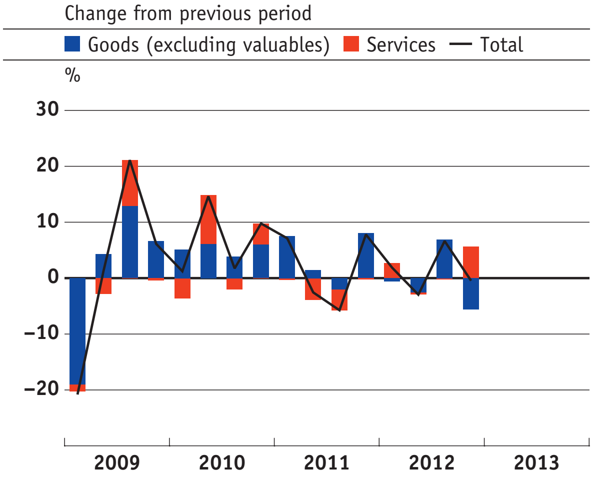
Imports rose sharply. This is attributable to a brisk rise in services imports, particularly in the area of licences and patents. In contrast to tourism exports, tourism imports declined noticeably after a strong summer period. Goods imports decreased slightly.

**Sound domestic demand**

Domestic final demand increased sharply at year-end (cf. chart 3.5 and table 3.1). The strongest growth driver was consumer spending, but investment activity also recovered to a degree.

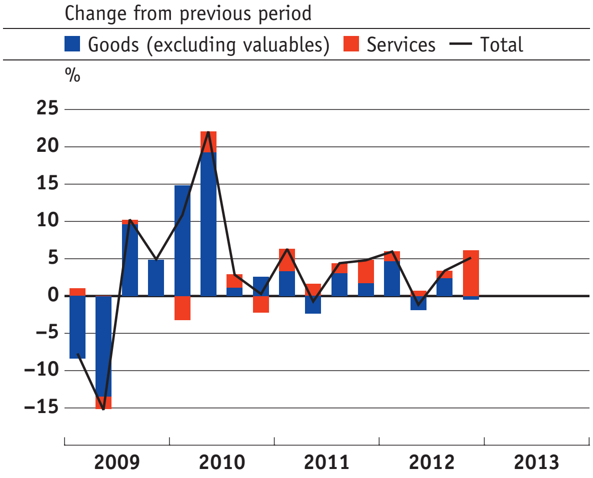
Private consumption increased noticeably in the fourth quarter (4.4%), with spending on food, health, insurance and financial services enjoying particularly dynamic growth. Consumer spending for 2012 as a whole totalled 2.5%, considerably above average. This was supported not just by robust development in incomes, but also by lower prices.

Chart 3.3
Contributions to export growth



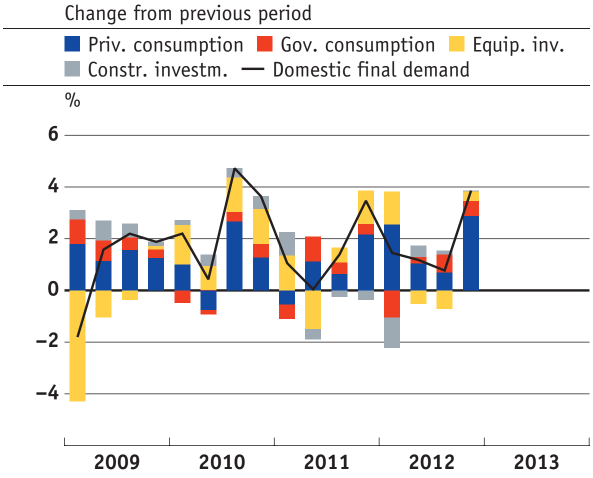

Source: SECO

Chart 3.4
Contributions to import 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

| | 2009 | 2010 | 2011 | 2012 | 2011 Q1 | Q2 | Q3 | Q4 | 2012 Q1 | Q2 | Q3 | Q4 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Private consumption | 1.8 | 1.6 | 1.2 | 2.5 | –0.8 | 1.7 | 1.0 | 3.4 | 3.9 | 1.6 | 1.0 | 4.4 |
| Government consumption | 3.3 | 0.7 | 2.0 | 0.7 | –4.5 | 7.8 | 3.6 | 3.2 | –8.1 | 2.1 | 5.6 | 4.6 |
| Investment in fixed assets | –8.0 | 4.8 | 4.0 | 0.1 | 9.8 | –8.3 | 1.4 | 4.0 | 0.0 | –0.4 | –2.6 | 1.8 |
| Construction | 3.0 | 3.5 | 2.4 | –3.2 | 8.9 | –4.0 | –2.4 | –3.6 | –11.6 | 4.5 | 1.6 | 0.4 |
| Equipment | –15.5 | 5.8 | 5.2 | 2.8 | 10.7 | –11.6 | 4.6 | 10.4 | 10.3 | –4.1 | –5.7 | 3.0 |
| **Domestic final demand** | **–0.4** | **2.2** | **1.9** | **1.7** | **1.1** | **0.0** | **1.4** | **3.5** | **1.4** | **1.2** | **0.8** | **3.9** |
| **Domestic demand** | **0.0** | **2.3** | **1.9** | **1.5** | **–2.7** | **5.3** | **3.9** | **0.0** | **2.6** | **–1.3** | **2.9** | **–0.8** |
| Total exports | –7.7 | 7.8 | 3.8 | 1.1 | 9.6 | –1.7 | –3.2 | 0.6 | 1.3 | 1.5 | 3.7 | 6.7 |
| Goods[1] | –11.1 | 9.4 | 6.3 | 1.6 | 11.2 | 2.1 | –3.0 | 11.7 | –0.8 | –3.7 | 10.1 | –8.1 |
| Services | 1.2 | 3.7 | –1.4 | 0.3 | –1.0 | –12.1 | –11.7 | –0.7 | 8.7 | –1.3 | –0.6 | 18.4 |
| **Aggregate demand** | **–2.9** | **4.3** | **2.6** | **1.3** | **1.7** | **2.6** | **1.2** | **0.2** | **2.2** | **–0.3** | **3.2** | **1.9** |
| Total imports | –5.2 | 7.4 | 4.2 | 2.3 | 3.1 | 4.0 | 6.6 | –2.2 | 2.8 | 0.2 | 5.3 | 4.1 |
| Goods[1] | –8.3 | 10.6 | 3.1 | 2.0 | 4.0 | –2.9 | 3.7 | 2.1 | 5.8 | –2.3 | 3.0 | –0.6 |
| Services | 9.0 | –1.5 | 7.3 | 9.3 | 16.8 | 9.1 | 7.2 | 16.4 | 7.0 | 3.7 | 5.0 | 30.7 |
| **GDP** | **–1.9** | **3.0** | **1.9** | **1.0** | **1.1** | **2.0** | **–1.0** | **1.3** | **1.9** | **–0.4** | **2.3** | **1.0** |

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

Construction investment rose only slightly in the fourth quarter and thus remained lower than the year-back level. According to surveys carried out by the Swiss Federation of Master Builders, each segment showed a different level of development. While civil engineering and commercial construction experienced growth, residential construction declined. The order situation remains positive in all segments, however. Since the level of new orders remained consistently high and production was partly limited by capacity shortages, overall outstanding orders in the fourth quarter recorded a significant year-on-year increase.

Equipment investment recovered slightly in the fourth quarter. This positive development is primarily attributable to investment in vehicles, however, which is susceptible to considerable fluctuation. However, investment in the area of electronic data processing also increased. By contrast, the persistently low utilisation of technical capacity and considerable uncertainty over the growth of the global economy contributed to a further decline in investment in machinery and electrical equipment.

## 3.2 Labour market

**Rising unemployment**

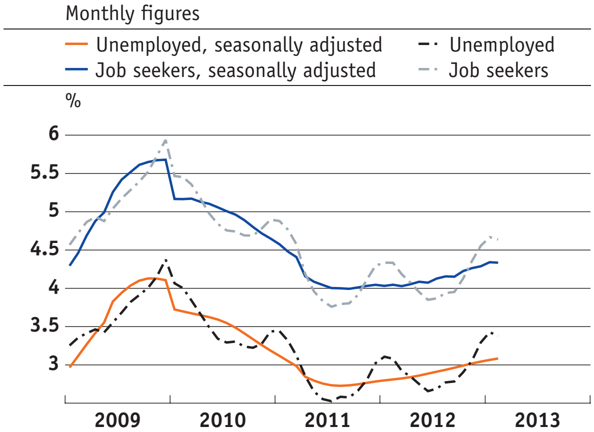
Unemployment has been rising slowly but continuously for more than a year now. Between November and February, the number of people registered as unemployed with regional employment offices increased by almost 3,300 on a seasonally adjusted basis. The unemployment rate rose to 3.1% (cf. chart 3.6).

Short-time working remained low in the fourth quarter (cf. chart 3.7). In December, 6,888 people were working short-time, more or less the same as the year before.

**Employment growth flagging**

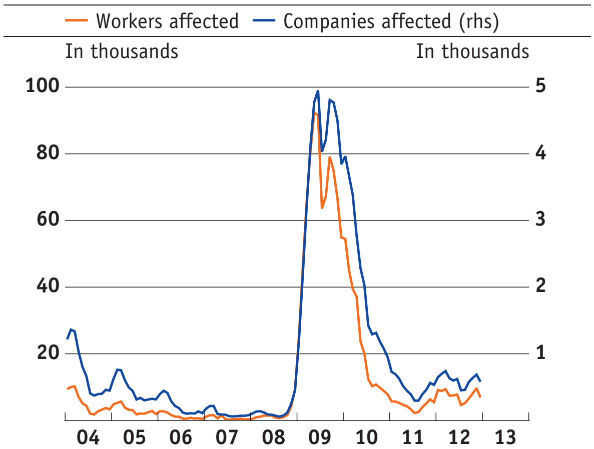
According to the official employment statistics published by the Swiss Federal Statistical Office (SFSO), there was a slight decline in employment momentum in the fourth quarter. The number of full-time and part-time jobs increased by 1.9%. Expressed in terms of full-time equivalents, the rise in employment amounted to 1.4% (cf. chart 3.8). New jobs were created in service-related industries and in construction, in particular. By contrast, there was a decrease in headcount in both manufacturing and the financial industry.

Chart 3.6
Unemployment and job seeker rates



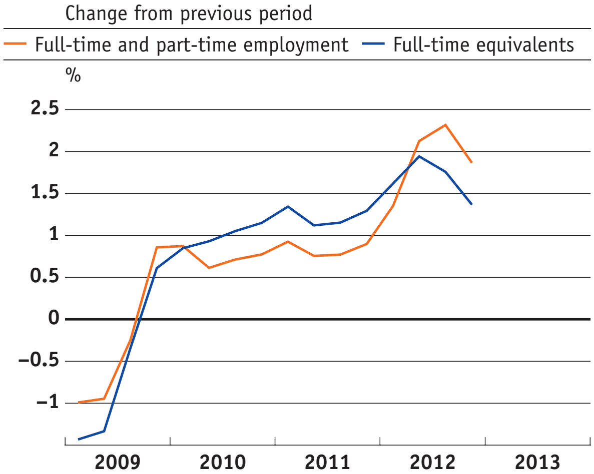

Unemployed and job seekers registered with the regional employment offices, as a percentage of the labour force according to the 2000 census (labour force: 3,946,988 persons) to 2009, and according to the 2010 census (labour force: 4,322,899 persons) from 2010.
Source: SECO

Chart 3.7
Short-time working



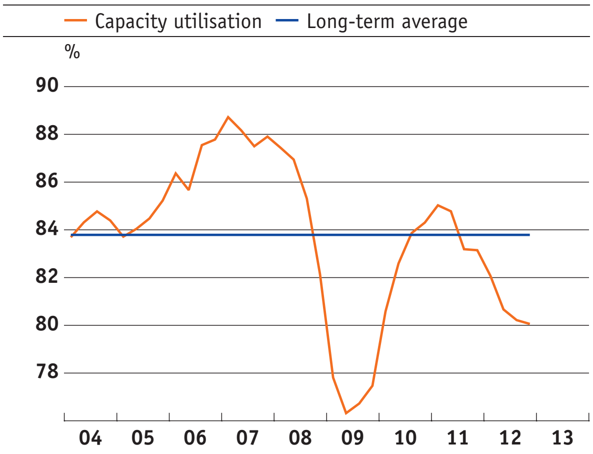

Source: SECO

Chart 3.8
Employment



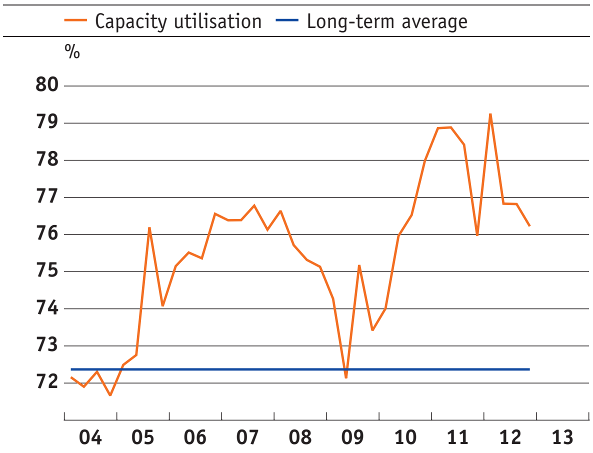

Source: SFSO, seasonal adjustment: SNB

Chart 3.9
Capacity utilisation in manufacturing



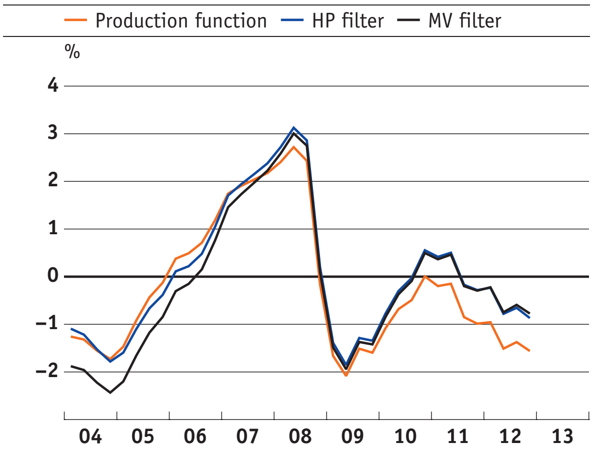
Source: KOF Swiss Economic Institute

Chart 3.10
Capacity utilisation in construction



Source: KOF Swiss Economic Institute

Chart 3.11
Output gap



Source: SNB

## 3.3 Capacity utilisation

**Decline in industrial capacity utilisation**

According to the survey carried out by KOF Swiss Economic Institute, the utilisation of technical capacity in the manufacturing industry receded further to 80.1% in the fourth quarter. It therefore remains well below the long-term average (cf. chart 3.9). In construction too, the level of machine utilisation declined slightly, although capacity utilisation in this sector is high overall (cf. chart 3.10). Many companies in construction again complained about bottlenecks in machine and equipment capacity as well as labour shortages. Capacity utilisation in the services sector as a whole remained normal.

**Negative output gap**

The output gap, which is defined as the percentage deviation of observed GDP from estimated aggregate potential output, shows how well the production factors in an economy are being utilised. As a result of weak GDP growth, the negative output gap widened further in the fourth quarter. Estimated potential output based on the production function approach indicates that the output gap was –1.6% in the fourth quarter, compared to –1.4% in the third quarter (cf. chart 3.11). Estimates using other methods (Hodrick-Prescott filter and multivariate filter) indicate that the output gap is slightly less pronounced (–0.9 % and –0.8%).

The different estimates reflect the various ways of calculating potential output. The production function approach takes the labour market situation and the stock of capital in the economy into account. Since the supply of labour, in particular, has risen steadily in recent years – primarily as a result of immigration – potential output and, hence, the output gap are larger when calculated with this method than with statistical filter methods.

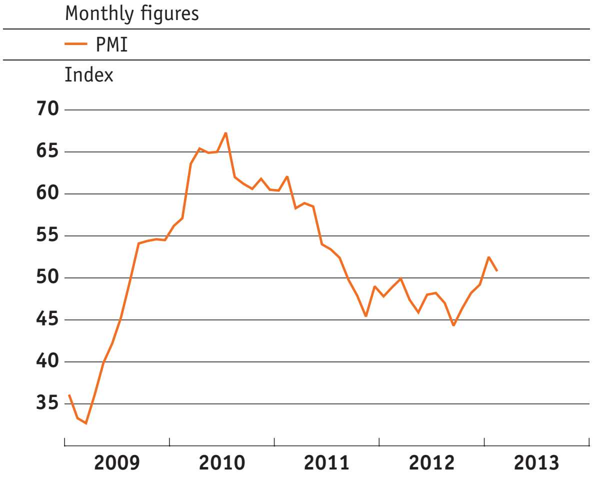
## 3.4 Outlook for the real economy

The SNB is expecting the global economy to recover gradually. Stronger demand from Germany, the US, and the emerging markets of Asia is likely to support Swiss exports. Confidence among Swiss exporters improved somewhat at the beginning of the year. However, the anticipated stimuli from abroad are not powerful enough to bring about a broad-based rise in value added and employment in manufacturing. Domestically oriented industries are likely to continue to benefit – despite rising unemployment – from the relatively robust labour market situation and immigration.

The SNB is expecting growth to pick up in the first quarter of 2013. For the year as a whole, it expects GDP growth of 1.0–1.5%. The output gap is therefore likely to remain negative. In view of the fragile international environment, downside risks for the Swiss economy remain considerable.

Chart 3.12

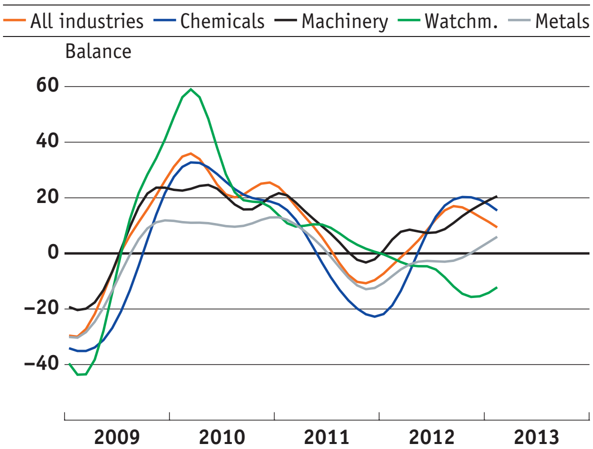
Purchasing managers' index (manufacturing)




Source: Credit Suisse

Chart 3.13

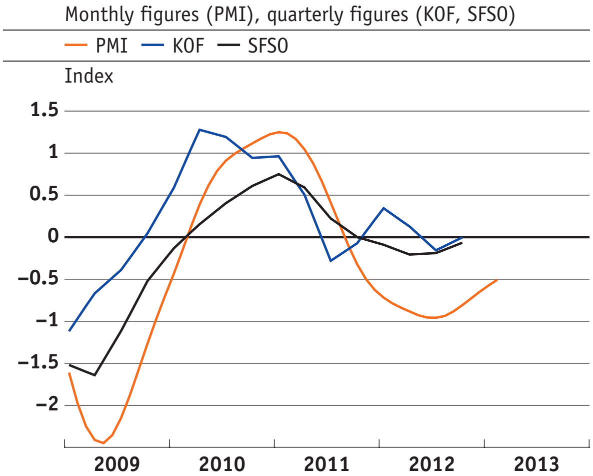
Expected new orders




Source: KOF Swiss Economic Institute

Chart 3.14

Employment leading indicators




Sources: Credit Suisse, KOF Swiss Economic Institute, SFSO

# 4 Prices and inflation expectations

Consumer prices remain below their previous year's level, which is attributable to lower goods prices in particular. In contrast to goods, services are rather more expensive than a year ago, even though apartment rents recently recorded a year-on-year decline. Supply prices, which have an upstream effect on consumer prices, have also increased slightly on last year's level.

Inflation expectations remain at a low level. In the medium term, they will remain in a range which the SNB considers compatible with price stability.

## 4.1 Consumer prices

**CPI inflation still negative**

The annual inflation rate, as measured by the national consumer price index (CPI), has barely changed over the last six months. In February, it amounted to –0.3%, exactly the same as in January and the fourth quarter of 2012 (cf. table 4.1).

**Year-on-year decline in prices of imported goods**

A breakdown into individual components reveals that foreign goods and services (excluding oil products) remain less expensive than a year ago. However, the annual inflation rates, while still negative, have been significantly less so since December 2011 (cf. chart 4.1). This is a reflection of the stabilising effect that the minimum exchange rate against the euro has had on import prices.

The more volatile annual inflation of oil products, which was slightly negative in both December and January, moved back into positive territory in February.

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

Table 4.1

| | 2012 | 2012 Q1 | Q2 | Q3 | Q4 | 2012 December | 2013 January | February |
|---|---|---|---|---|---|---|---|---|
| **Overall CPI** | **–0.7** | **–0.9** | **–1.0** | **–0.5** | **–0.3** | **–0.4** | **–0.3** | **–0.3** |
| Domestic goods and services | 0.0 | 0.0 | 0.0 | 0.0 | 0.1 | 0.1 | 0.2 | 0.1 |
| Goods | –1.8 | –2.3 | –2.1 | –1.8 | –1.0 | –1.0 | –0.7 | –0.8 |
| Services | 0.6 | 0.7 | 0.6 | 0.6 | 0.4 | 0.5 | 0.5 | 0.3 |
| Private services excluding rents | 0.6 | 0.7 | 0.6 | 0.6 | 0.5 | 0.5 | 0.6 | 0.5 |
| Rents | 0.6 | 0.8 | 0.7 | 0.6 | 0.2 | 0.0 | 0.0 | –0.3 |
| Public services | 0.4 | 0.6 | 0.3 | 0.3 | 0.6 | 1.1 | 1.1 | 1.1 |
| Imported goods and services | –2.7 | –3.4 | –3.8 | –2.1 | –1.6 | –2.0 | –1.7 | –1.2 |
| Excluding oil products | –4.2 | –5.2 | –4.9 | –4.1 | –2.5 | –2.3 | –1.9 | –1.6 |
| Oil products | 5.0 | 6.2 | 2.2 | 8.7 | 3.0 | –0.7 | –1.0 | 1.3 |

Sources: SFSO, SNB

**Prices of domestic goods largely unchanged**

The prices of domestic goods and services in February were virtually at the same level as a year earlier. While the prices of goods declined, the majority of services became more expensive over the same timeframe (cf. chart 4.2). Annual inflation in public services rose significantly, driven by fare increases in public transport. By contrast, annual rent inflation declined in February to –0.3%, thereby entering negative territory for the first time since 1998.

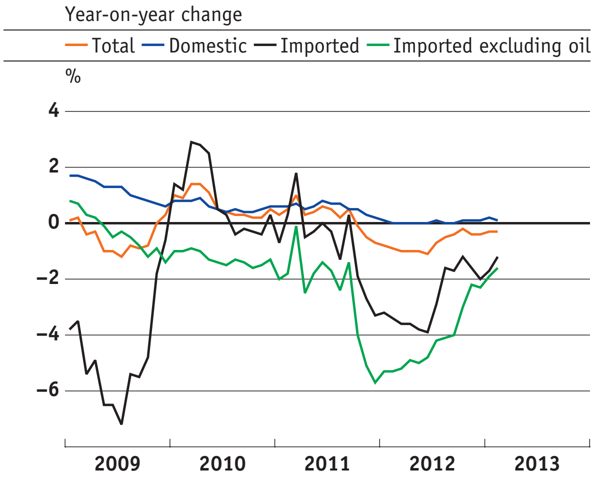
**No change in low core inflation**

The trimmed mean calculated by the SNB (TM15) shows that the inflationary trend remains broadly unchanged (cf. chart 4.3). In February, the TM15 was around –0.0%, which is very low in a historical comparison.

Just like the TM15, dynamic factor information (DFI) also suggests no change in inflationary pressure. DFI extracts the inflationary trend as a common component from a large number of monetary and real indicators.

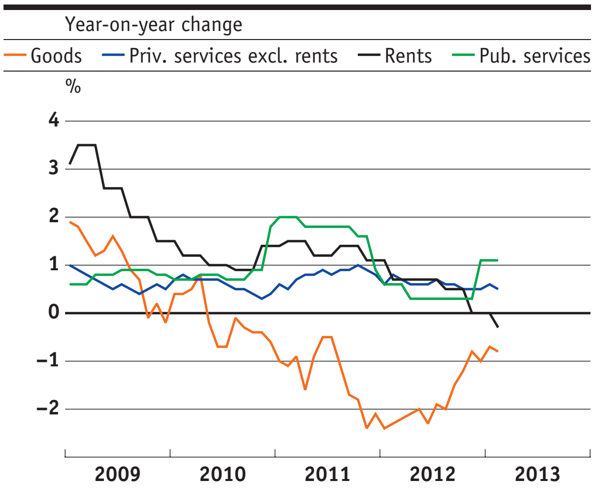
In contrast to the TM15 and DFI, the core inflation measure of the Swiss Federal Statistical Office (SFSO1) lies clearly in negative territory. However, this measure has continuously converged towards the TM15 and DFI since September 2012. Like the TM15, the SFSO1 is based on a reduced CPI basket of goods. However, whereas the SFSO1 always excludes the same products every month (fresh and seasonal products, energy and fuel), the TM15 excludes the goods with the greatest price changes every month (15% at either end of the distribution curve).

Chart 4.1
CPI: domestic and imported goods and services



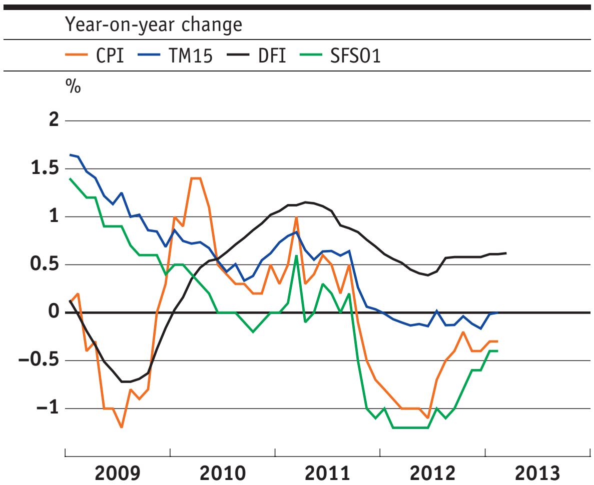

Sources: SFSO, SNB

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

**Stable supply prices**

The annual rate of inflation for supply prices (producer and import prices) has decreased slightly in recent months. In January, it amounted to 0.1%, having briefly risen to 1.2% in November (cf. chart 4.4). Producer prices in January were 1.2% higher than their level a year earlier, while import prices fell slightly over the same period.

The price pressure on downstream consumer prices can be evaluated by observing the prices of domestically sold manufactured goods. Overall, the prices of these goods have remained virtually unchanged since the end of 2011, which suggests that the minimum exchange rate against the euro has had a stabilising effect, and that no upward or downward pressure from supply prices is currently being exerted on downstream consumer prices.

## 4.3 Real estate prices

**Residential property prices increase further**

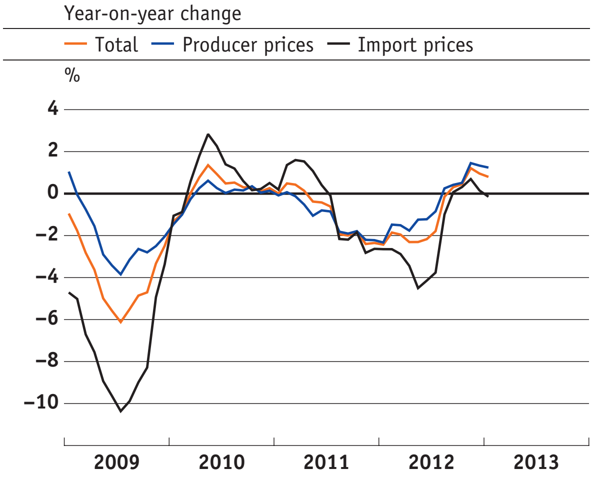
Prices of single-family homes and owner-occupied apartments continued to rise in the fourth quarter. While the rise in transaction prices for owner-occupied apartments may have flattened off according to Wüest & Partner, the corresponding indices of Fahrländer Partner and IAZI once again rose sharply (cf. chart 4.5). The asking price indices of Wüest & Partner, based on advertisements in newspapers and on the internet, likewise increased further.

As a result of the persistently strong price rises of recent years, the risks of the residential property market overheating have increased sharply. On 13 February 2013, the Federal Council responded to the growing imbalances in the mortgage and real estate markets by activating the countercyclical capital buffer at the proposal of the SNB (cf. chapter 5.5, Monetary and credit aggregates).

**Existing rents almost unchanged, offer rents rise sharply**

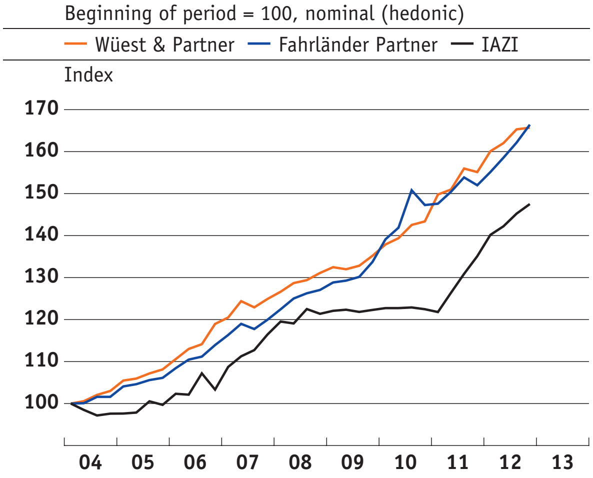
Rents for apartments offered on the market (offer rents) rose further in the fourth quarter. According to Wüest & Partner, while the annual rate of inflation for offer rents may have fallen slightly, it remains significantly higher than rent inflation for existing rental contracts (existing rents). The rental component of the CPI, which is dominated by existing rents, recorded only a very

Chart 4.4
Producer and import prices



Source: SFSO

Chart 4.5
Transaction prices, owner-occupied apartments



Sources: Fahrländer Partner, IAZI, Wüest & Partner slight year-on-year rise in the fourth quarter (cf. chart 4.6). In February, annual rent inflation was even slightly negative.

Rents for existing contracts are tied by law to the reference interest rate, which has declined steadily in recent years and remained at 2.25% since June 2012.

## 4.4 Inflation expectations

**Short-term inflation expectations remain low**

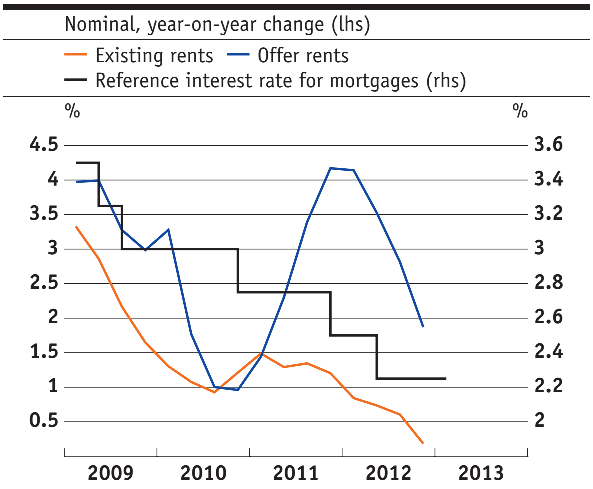
Surveys of households and experts continue to indicate low short-term inflation expectations. While medium-term expectations exceed short-term expectations, the former remain subdued too.

The quarterly survey of households conducted by SECO in January shows that little has changed with respect to expectations of price developments in recent months (cf. chart 4.7). Over the next 12 months, 44% of households are expecting prices to remain the same, while 41% are expecting an increase. The proportion of respondents anticipating either falling or sharply rising prices declined further in January.

According to the *Credit Suisse ZEW Financial Market Report*, a majority of experts surveyed in February (60%) once again predicted that inflation rates would remain unchanged over the next six months. The remaining respondents expected rising inflation. In contrast to previous months, none of the respondents expected lower rates of inflation.

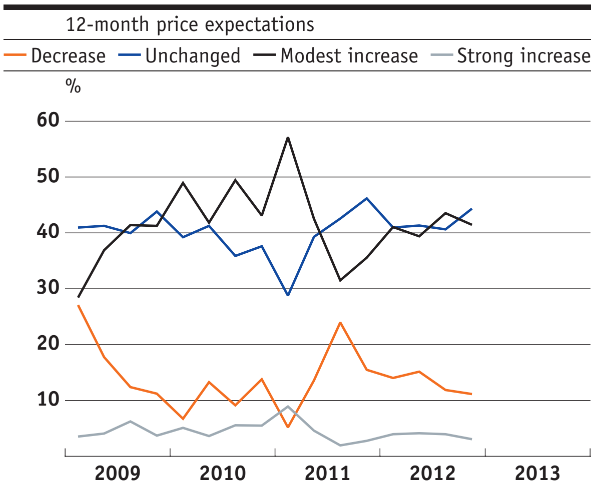
Point forecasts for expected inflation are provided by the Deloitte survey of CFOs and heads of finance in companies based in Switzerland, as well as talks between the SNB delegates for regional economic relations and companies from all parts of Switzerland. The talks held by SNB delegates in the first quarter of 2013 indicate that inflation expectations over a six to twelve-month horizon will remain low at 0.2%. The average expected two-year-ahead inflation rate derived by Deloitte in the fourth quarter of 2012 amounted to around 1.3%. This is virtually unchanged from expectations in the second and third quarters of 2012.

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

Monetary and financial conditions have not changed substantially compared to the previous quarter. Interest rates in the money market remain close to zero. Against a backdrop of calmer financial markets at the beginning of the year, share prices continued to recover and yields on Swiss Confederation bonds rose. The decline in demand for safe investments can also be observed in the yield increase on money market debt register claims of the Swiss Confederation, which are now only marginally negative.

The export-weighted external value of the Swiss franc has weakened slightly since December. The franc depreciated a little against the euro and the dollar, while it strengthened against the yen.

The monetary and credit aggregates continued to grow in the quarter under review. At the proposal of the SNB, the Federal Council has therefore activated the countercyclical capital buffer in order to protect the banking sector against imbalances in the mortgage and real estate markets.

## 5.1 Summary of monetary policy since the last assessment

**Continuation of monetary policy announced in September 2011**

Over the last quarter, the SNB has continued to pursue the monetary policy which it announced in September 2011 and has reiterated at subsequent assessments. On 6 September 2011, the SNB had set a minimum exchange rate of CHF 1.20 to the euro, after narrowing the target range for the three-month Libor to 0.0–0.25% and greatly increasing liquidity in August of that year.

**Sight deposits at SNB stable**

Total sight deposits held at the SNB have remained virtually unchanged since the last assessment in December. In the week ending 8 March 2013 (last calendar week before the mid-March assessment), sight deposits totalled CHF 370.5 billion, compared to CHF 372.6 billion in the last calendar week before the mid-December assessment. The average between the mid-December and mid-March assessment was CHF 370.5 billion. Of this amount, CHF 285.1 billion was accounted for by the sight deposits of domestic banks and the remaining CHF 85.4 billion by other sight deposits.

**Banks surplus reserves remain high**

Statutory minimum reserves averaged CHF 13.5 billion between 20 November 2012 and 19 February 2013, an increase of CHF 0.6 billion compared to the preceding period (20 August 2012 to 19 November 2012). This rise is due to continued robust increases in the sight deposits held by commercial banks. On average, banks exceeded the requirement by around CHF 279.8 billion (previous period: CHF 284.1 billion). Thus, bank surplus reserves have remained extremely high.

## 5.2 Money and capital market interest rates

### Money market rates remain low

With the level of trading activity still low, money market interest rates remained largely unchanged in the first few months of 2013 (cf. chart 5.1). The three-month Libor stood at 2 basis points in mid-March. Repo rates were predominantly negative.

### Slight rise in long-term interest rates

The upbeat sentiment on the financial markets prompted investors to reduce their investments in safe-haven government bonds. As a result, yields on Confederation bonds recovered from their record lows in December 2012. In mid-March, the yield on ten-year Confederation bonds was around 0.8% – still a low figure by historical standards. This shows that while investors' risk appetite has increased, safe investments remain attractive.

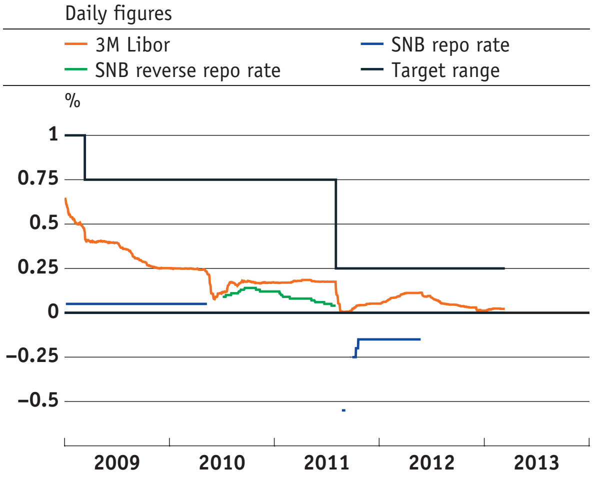
### Steeper yield curve

The yield curve for Confederation bonds has moved to a higher level since the mid-December assessment and has become slightly steeper. This is due to the fact that long-term interest rates have risen while short-term interest rates have remained virtually unchanged (cf. chart 5.2). The spread between the yield on ten-year Confederation bonds and the three-month Libor was around 0.8 percentage points in mid-March, compared with 0.5 percentage points in mid-December.

### Real interest rates rise marginally

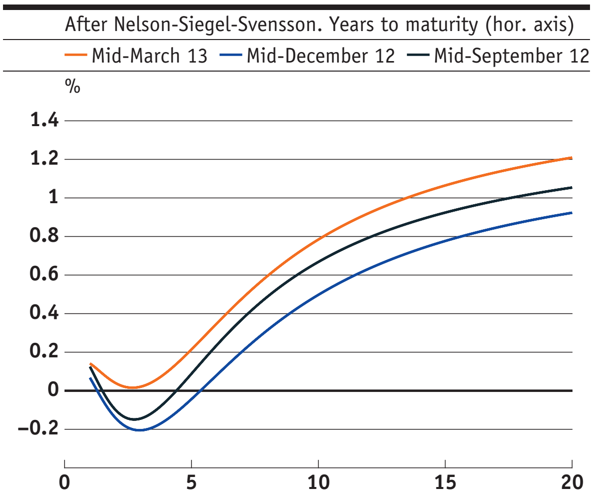
Since the mid-December monetary policy assessment, estimated ten-year real interest rates have risen from a low level of 0.1% to almost 0.3%, reflecting higher long-term nominal interest rates and virtually unchanged long-term inflation expectations. The real interest rates shown in chart 5.3 are calculated using the ten-year yield on Confederation bonds and the estimated inflation expectations for the same time horizon, determined using a VAR model.

Chart 5.1
Money market rates



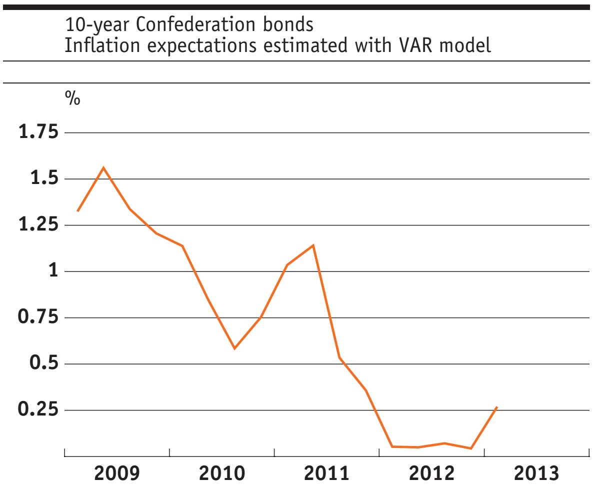

Sources: Bloomberg, Reuters, SNB

Chart 5.2
Term structure of Swiss Confederation bonds



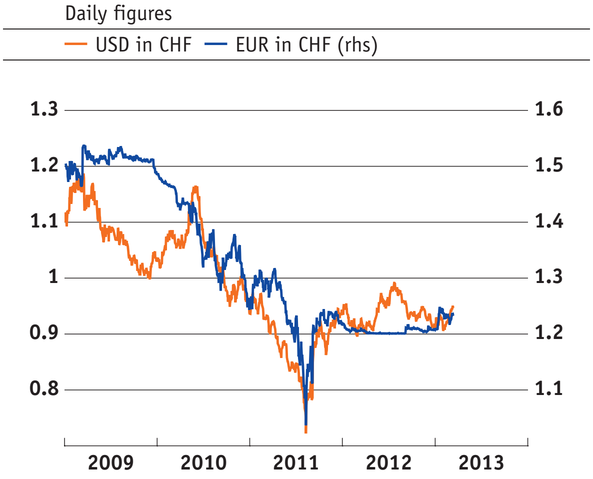

Source: SNB

Chart 5.3
Estimated real interest rate



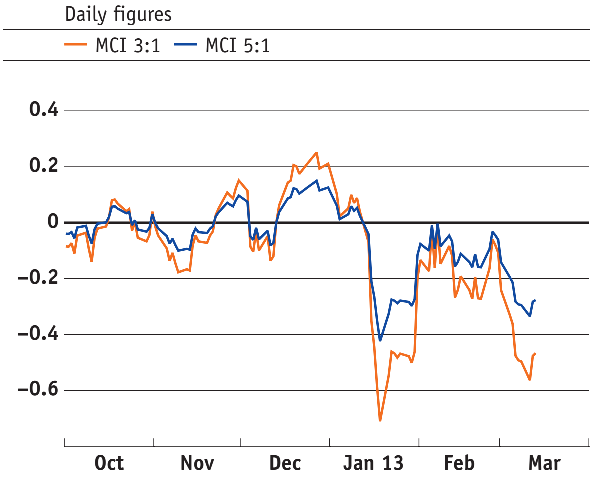

Source: SNB

Chart 5.4
Exchange rates



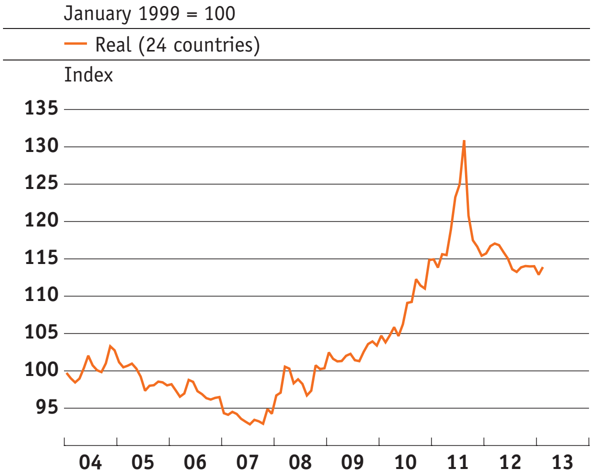

Source: SNB

Chart 5.5
MCI nominal




Source: SNB

Chart 5.6
Export-weighted external value of Swiss franc




Source: SNB

## 5.3 Exchange rates

### EUR/CHF exchange rate above 1.20

Swiss franc exchange rate movements since the December assessment mainly reflect the renewed strengthening of the euro and the dollar as well as the continuing weakness of the Japanese yen. Following the ECB's monetary policy decision in January, the euro rose against the Swiss franc from 1.21 to 1.25 before settling at 1.23 (cf. chart 5.4). In mid-March, the Swiss franc also traded somewhat lower against the US dollar than in mid-December, while it gained around 10% against the yen. These price movements translate into a slight decline in the export-weighted nominal external value of the Swiss franc.

### Weaker Swiss franc leads to easing in monetary conditions

Monetary conditions have eased somewhat as a result of the slight weakening of the Swiss franc. The Monetary Conditions Index (MCI) has consequently been in negative territory since January (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 calculation of the MCI (3:1 and 5:1). The index is reset to zero at the time of the latest monetary policy assessment. A negative MCI value signifies an easing of monetary conditions. As the three-month Libor has barely changed in recent months, the MCI is currently almost entirely a reflection of exchange rate movements.

### High real external value of Swiss franc

The real export-weighted external value of the Swiss franc has largely remained unchanged since July 2012 (cf. chart 5.6). It remains significantly above its long-term average. The slight temporary decline registered in January was primarily attributable to the nominal depreciation of the franc against the euro.

## 5.4 Stock markets

### Rising share prices

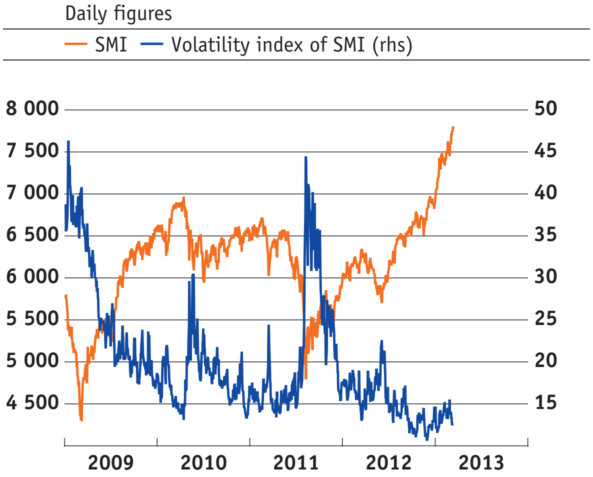
The price of Swiss shares rose significantly in the first few months of 2013, following a trajectory similar to that of the indices in the US and the UK, but substantially outperforming the indices in Germany and the euro area as a whole. Using the example of the Swiss Market Index (SMI), chart 5.7 shows that recent developments are a continuation of an upward trend that started in the autumn of 2011. Swiss share prices are currently at their highest level since January 2008.

Chart 5.8 indicates that the Swiss stock market's strong performance was broad-based. All the key sectors in the Swiss Performance Index (SPI) reported gains throughout recent months.

### Low expected volatility

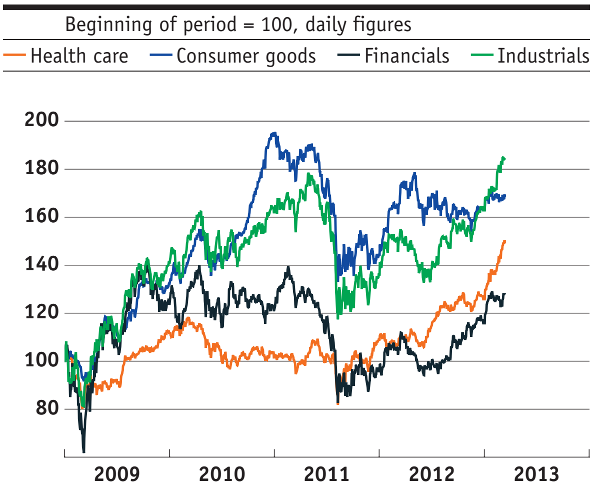
The global rise in share prices is an expression of increased risk appetite among investors and is linked to low expected market volatility. In Switzerland, the SMI index of expected 30-day volatility is currently at a very low level (cf. chart 5.7). Announcements by major central banks that they intend to pursue their relaxed monetary policy for a prolonged period of time have calmed financial markets. Nevertheless, this low volatility should not be interpreted as a sign that deeper underlying problems have been solved.

Chart 5.7
Share prices and volatility



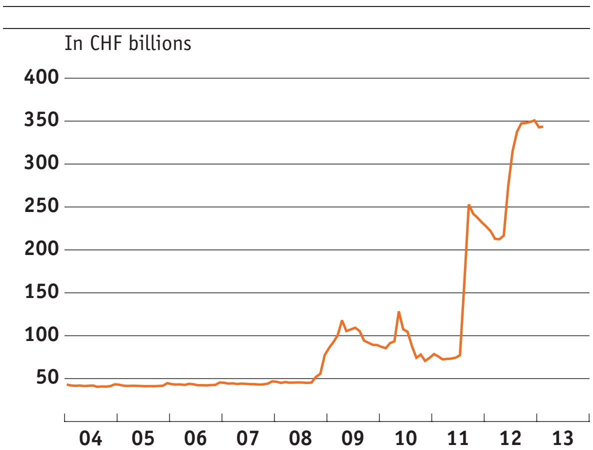

Source: Thomson Financial Datastream

Chart 5.8
Selected SPI sectors



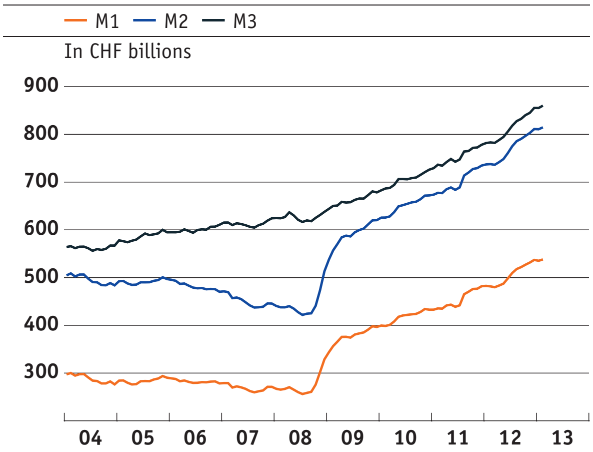

Source: Thomson Financial Datastream

Chart 5.9
Monetary base



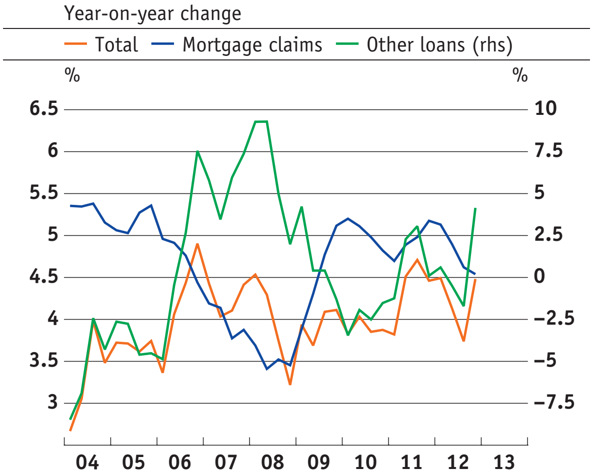

Source: SNB

Chart 5.10
Monetary aggregates



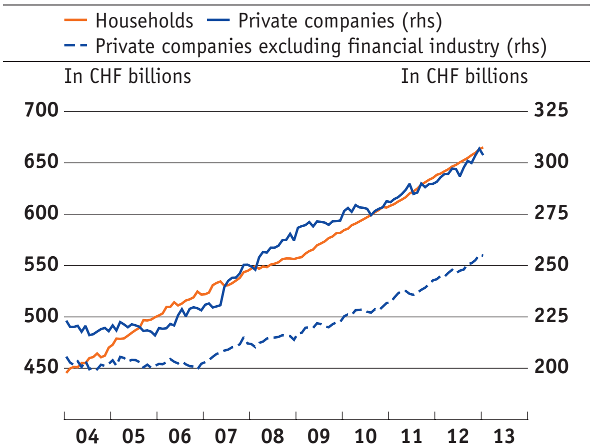

Source: SNB

Chart 5.11
Growth in bank loans, in Swiss francs




Source: SNB

Chart 5.12
Loans to households and companies




Source: SNB

## 5.5 Monetary and credit aggregates

**Monetary base largely unchanged**

The monetary base, which is composed of banknotes in circulation plus sight deposits of domestic banks held with the SNB, has stabilised at around CHF 350 billion since September (cf. chart 5.9). In January, it fell slightly compared to the previous month.

The stabilisation was prompted by the ECB's decision in early September to purchase, under certain conditions, unlimited quantities of Government bonds. Over the preceding few months, foreign exchange purchases by the SNB, required for the enforcement of the minimum exchange rate against the euro, had resulted in a strong expansion in sight deposits, and hence the monetary base.

**Further increase in broad monetary aggregates**

Despite the stabilisation of domestic banks' sight deposits at the SNB, broad monetary aggregates, which measure the amount of money held by households and companies, have continued to grow (cf. chart 5.10). In February, M1 (currency in circulation, sight deposits, and transaction accounts) was 11.7% higher than one year earlier. In the same time period, M2 (M1 plus savings deposits) rose by 10.4% and M3 (M2 plus time deposits) was up by 9.8% (cf. table 5.1). The strong growth in the monetary aggregates mainly reflects credit and deposit generation in the banking system, which has been stimulated by low interest rates.

When interest rates are low, factors such as monetary and credit aggregates can supply additional information (i.e. information that is not contained in interest rates) on the transmission of monetary policy stimuli. The continued growth of monetary and credit aggregates underscores that expansionary monetary policy is affecting the economy and stimulating overall economic demand.

**Strong lending growth continues**

Bank lending was higher year-on-year in the fourth quarter of 2012 than in the third. The main factor behind the slight acceleration in loan growth was other (i.e. non-mortgage-backed) loans. As a rule, other loans keep pace with economic developments, however the correlation is loose. Chart 5.11 shows that the decrease in other loans during the recent recession was distinctly smaller than that during the relatively mild recession at the beginning of the last decade.

**Monetary aggregates and bank loans** Table 5.1

Year-on-year change in percent

| | 2012 | 2012 Q1 | Q2 | Q3 | Q4 | 2012 December | 2013 January | February |
|---|---|---|---|---|---|---|---|---|
| **M1** | **11.4** | **10.8** | **11.0** | **12.5** | **11.2** | **11.4** | **10.9** | **11.7** |
| **M2** | **9.8** | **9.0** | **9.4** | **10.8** | **10.0** | **10.4** | **10.0** | **10.4** |
| **M3** | **8.0** | **6.7** | **7.0** | **8.9** | **9.4** | **9.9** | **9.4** | **9.8** |
| **Bank loans total**[1, 3] | **4.0** | **4.2** | **3.9** | **3.7** | **4.0** | **4.3** | **3.7** | |
| Mortgage claims[1, 3] | 4.8 | 5.2 | 4.9 | 4.6 | 4.5 | 4.5 | 4.4 | |
| Households[2, 3] | 4.9 | 5.1 | 5.0 | 4.8 | 4.6 | 4.8 | 4.6 | |
| Private companies[2, 3] | 4.9 | 5.4 | 5.0 | 4.4 | 5.0 | 5.4 | 5.5 | |
| Other loans[1, 3] | −0.1 | −0.1 | −1.1 | −0.8 | 1.6 | 3.3 | −0.1 | |
| Secured[1, 3] | 3.0 | 1.8 | −0.9 | 3.2 | 8.0 | 8.6 | 3.1 | |
| Unsecured[1, 3] | −2.1 | −1.3 | −1.2 | −3.3 | −2.5 | −0.2 | −2.2 | |

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

In contrast to the growth of other loans, annual growth of mortgage claims fell slightly, however it remained robust, supported by low interest rates (cf. table 5.1). As chart 5.11 illustrates, the rate of growth in mortgage claims rose sharply following the SNB's lowering of the target range for the three-month Libor in October 2008. Since then, mortgage claims – which make up around four-fifths of total bank lending – grew at annual rates of 4.5% to 5.2%.

### Lending growth broad based

Overall, all borrower categories benefited from favourable financing costs. The breakdown of bank lending by borrower category shows that, as of December 2012, loans to households increased by CHF 28.1 billion or 4.4% in the space of a year. Loans to financial corporations rose by CHF 4.6 billion (9.9%) over the same period, while loans to other industries increased by CHF 12.5 billion (5.1%) (cf. chart 5.12).

### Countercyclical capital buffer activated

On 13 February 2013 – at the proposal of the SNB – the Federal Council for the first time opted to activate the countercyclical capital buffer (CCB) provided for in the Capital Adequacy Ordinance. The capital buffer is to be held from 30 September 2013 and applies in addition to other capital requirements for banks. The CCB is targeted towards residential mortgage loans and is set at 1% of the associated risk-weighted positions.

The activation of the countercyclical capital buffer for specific market segments was motivated by the strong growth of the mortgage and real estate markets over several years. This continued strong momentum has led to imbalances which pose a considerable medium-term risk to the stability of the Swiss banking sector, and hence to the entire Swiss economy. While the imbalances are currently still less pronounced than those immediately prior to the onset of the real estate and banking crisis at the end of the 1980s, experience shows that they can rapidly intensify, and that action must be taken early. Given the minimum exchange rate against the euro, the economic environment and the subdued inflation outlook, there is currently limited scope for a rise in interest rates, which would also exert a dampening effect on the mortgage and real estate markets.

The SNB's primary motivation for activating the capital buffer is to strengthen the resilience of the banking sector. Moreover, the CCB acts to counter a further build-up of such imbalances, by making it less attractive for banks to grant residential mortgage loans compared to other forms of lending.

# 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 2013

**First quarter of 2013**
The Swiss National Bank's delegates for regional economic relations are constantly in touch with 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 2013 with 238 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 | Jean-Marc Falter |
| Italian-speaking Switzerland | Fabio Bossi |
| Mittelland | Martin Wyss |
| Northwestern Switzerland | Daniel Hanimann |
| Vaud-Valais | Aline Chabloz |
| Zurich | Markus Zimmerli |

## Summary

Economic activity revived in the first quarter of 2013 according to this survey. This development was supported above all by an improvement in manufacturing and – to a lesser extent – the services sector.

The differences between the sectors have once again become less pronounced. The export industry experienced a renewed weakening in demand, particularly from southern Europe, whereas the more favourable economic situation in other parts of the world and in Switzerland had a stimulating effect. The significance of the minimum exchange rate for the Swiss franc against the euro was once again stressed by many respondents.

Although the pressure on margins persisted, it has weakened somewhat. Many implemented process optimisations, cost reductions, and measures to improve efficiency are beginning to bear fruit. Overall, demand for labour remained unchanged from the previous quarter.

The outlook for real growth in turnover over the next few months has brightened further in all sectors. The demand for staff is likely to increase slightly.

Latent uncertainty about developments in Europe remains, but has receded somewhat.

# 1 Business activity

### Manufacturing

Business activity in manufacturing has improved. Real turnover was up quarter on quarter, but also recorded a significant year-on-year increase. The better overall situation compared to the previous company survey is broadly supported across different industries.

In addition to the chemical, watchmaking, electrical equipment and food industries, all of which recorded sales increases in the previous quarter too, companies in the pharmaceutical, plastics and textile industries have now also reported an upturn in business. Real turnover in the machinery industry remained on a par with the previous quarter; by contrast, the metals processing industry recorded a quarter-on-quarter decline in turnover.

The export sector once again felt the effects of the recession in southern Europe, and recorded either a decline in sales or a complete absence of demand. The austerity measures pursued in the public sector were felt particularly keenly. Demand from Asia, the US, South America, the Middle East and Russia had a stimulating effect, as did domestic demand.

### Construction

In construction, real turnover remained at the level of the previous quarter. However, quarterly sales were still significantly higher than a year before. The persistently strong construction economy, more favourable weather conditions, and the need to make good the backlog from last year were all conducive to business development. A number of companies are now looking to consolidate their business.

The finishing trade segment developed robustly. By contrast, turnover in civil engineering was slightly below that of the previous quarter, which in many cases can be attributed to the completion of major projects. Unlike residential construction, commercial-industrial construction remained subdued.

There was sporadic mention of real estate market risk; institutional investors were in some cases mentioned as the principal drivers of the momentum in residential construction and the related price surge. On the other hand, oversupply in a number of market segments also resulted in some price falls, such as rents for luxury apartments in urban areas. The lending policies of banks were not particularly spotlighted, but a number of delegates did refer to greater restraint on the part of banks in mortgage lending.

### Services

In the services sector, real turnover overall proved moderately above the level of the previous quarter, as well as – somewhat more markedly – above the level of the previous year. The situation has improved further compared to the last survey.

Business activity developed dynamically in the travel industry and IT, as well as in services connected with facility management and maintenance. Retailing recorded a further improvement. Cross-border shopping remained a concern, but was not emphasised as strongly as in previous surveys. Business activity for banks and wholesalers was only slightly up on the previous quarter. A number of industries are feeling the effects of operational cost-cutting measures implemented by banks.

In the hotel industry, turnover stagnated at the level of the previous quarter. Hotels in holiday regions again complained of the absence of guests from other European countries, particularly Germany, the Netherlands and the UK.

## 2 Capacity utilisation

Overall, utilisation of production capacity and infrastructure was judged to be normal. The differences between the individual sectors have continued to narrow, but within the sectors themselves the capacity utilisation picture remains very heterogeneous.

Companies in manufacturing rated their overall capacity utilisation as slightly lower than normal, whereas capacity utilisation was comparatively high among producers of electrical appliances, in the automotive construction industry, and in pharmaceuticals. By contrast, capacity utilisation in the machinery and metals processing industries was low or even very low. Underutilisation was also reported by plastics processing firms and companies in the printing and paper industry.

In construction, technical capacity utilisation was slightly higher than is normal for this time of year. Whereas companies in structural engineering and the finishing trade were working to healthy capacity, civil engineering companies were suffering from capacity underutilisation.

In the services sector, infrastructure utilisation was normal overall. A relatively high level of capacity utilisation was again registered by architectural and engineering firms, as well as by providers of facility management services. The automotive industry and IT industries likewise reported fairly high capacity utilisation. By contrast, hotels once again recorded low occupancy rates. The reasons cited were the continually low numbers of foreign tourists, greater cost awareness on the part of companies, and the restructuring of the banking sector. Nevertheless, a slight upturn was apparent in business travel, while a number of regions reported the return of guests from Germany. The robust demand from Swiss guests made a positive contribution to capacity utilisation.

## 3 Demand for labour

As in recent quarters, overall demand for labour remained virtually unchanged. In the manufacturing industry, the surveyed companies once again assessed their staff numbers as being slightly too high. They continue to exercise restraint in their personnel policy; departing employees are often not replaced, although short-time working was not a widespread theme. In addition, various measures such as longer working hours for the same salary were rescinded at the start of the year. Pharmaceutical companies and manufacturers of precision instruments in particular reported staffing levels in keeping with their requirements.

In construction, staff numbers were generally assessed as being appropriate. Headcount in the finishing trade was deemed to be somewhat on the low side, whereas in civil engineering it was felt to be rather high. While specialists remain extremely rare on the job market, the problem of recruiting staff generally has abated somewhat.

In the services sector, staff levels were considered appropriate overall. The need to recruit was seen as fairly acute by architectural and engineering firms, as well as by IT companies. The hotel industry reported appropriate staffing levels, whereas in the previous quarter these had been too high. Banks and fiduciary companies deemed their headcount as slightly too high.

Overall, the surveyed companies considered the process of recruiting staff to be as challenging and time-consuming as ever. In certain areas they identified a marked increase in spontaneous applications, particularly from abroad. A significantly larger number of applicants are responding to recruitment advertisements. As before, however, the profiles of job-seekers frequently failed to meet the requirements of companies. Many industries continue to point out that they can only source the personnel they require abroad. Companies in the MEM industries, retailers, banks and some pharmaceutical companies were finding the process of recruitment somewhat easier than usual. By contrast, recruitment was perceived as rather more difficult in the case of insurers and IT companies.

## 4 Prices, margins and earnings situation

Overall, the margin situation was deemed by companies across all sectors to have improved slightly compared to the previous quarter. Whereas margins in manufacturing and in the services sector continued to be rated as weaker than usual, representatives of the construction industry considered their margins to be normal. Companies are experiencing continued pressure to optimise costs and boost efficiency. Persistent marketing efforts are made in an intensive search for new markets, products and client segments. In many cases, companies are looking to differentiate themselves from their competitors by providing additional services.

Numerous companies from all three sectors of the economy stressed the importance of the minimum exchange rate against the euro for their companies over the last 18 months. On average, companies in all three sectors are now expecting stable or slightly rising purchase prices over the next few months.

Representatives of the manufacturing industry once again emphasised the problem of squeezed profit margins. A great many branches of industry are affected, particularly the metals processing and machinery industries, as well as companies that process wood, paper and plastics. The situation also appeared rather problematic for various companies in automotive construction and textiles. By contrast, pharmaceutical companies reported a relatively normal margin situation. Although the exchange rate problem is no longer quite the focus it was for the manufacturing sector, it remains a challenge.

In construction, representatives of the civil engineering segment in particular reported below-average margins; in structural engineering these were assessed as normal, and in the finishing trade slightly higher than normal. According to respondents, the market presence of foreign companies or companies from outside the region was now also an increasingly prevalent phenomenon in the main lines of construction business. Nonetheless, construction prices are expected to rise more strongly than purchase prices, which should see margins improve further.

In the services sector, the majority of business areas found themselves confronted with unusually low margins. The worst-affected industries were once again the hotel industry, transport and logistics companies, banks, wholesalers and retailers. Representatives of the transport industry cited the current overcapacity in their business as the principal reason behind the slump in prices. IT companies and insurers considered the margin situation to be within the normal range, while margins reported by estate agents were above the long-term average.

## 5 Outlook

Uncertainty over future developments has noticeably decreased since the last survey. In terms of global risks, fears over a resurgence of the European debt crisis remain in the foreground, albeit less prominently. Also causing a degree of uncertainty are the subdued economic prospects for Europe, whereas there is confidence surrounding the development of demand from other parts of the world.

In all three sectors, turnover expectations for the next six months are actually a little more optimistic than in the previous quarter. This is also reflected in recruitment plans, with companies expecting to increase their headcount slightly over the same period.

In manufacturing, the overall commercial outlook of companies has brightened further in comparison to the previous quarter. Representatives of almost all industry sectors are anticipating slight rises in sales over the next six months. By contrast, companies in the metals processing industry expect turnover to stagnate. Representatives from the pharmaceutical, chemical, plastics processing and textile industries are fairly optimistic with respect to future sales development.

In construction, seasonally adjusted turnover should continue to rise slightly over the next few months, as should capacity utilisation. This industry is exuding optimism and expects no significant slowdown in 2013. A slight increase in headcount is anticipated.

In general, companies in the services sector are upbeat about their business prospects for the next six months. Most industries in this sector now expect to see a slight increase in turnover. The hotel industry in particular is looking to the future with more confidence than in the previous quarter, and the outlook for automotive retailers and wholesalers has also improved. Both capacity utilisation and headcount can be expected to rise slightly in the services sector over the next few months.

As to the investment plans of companies, the current level of equipment investment and investment in buildings is expected to remain largely unchanged in all three sectors. This results less from an assessment of economic developments than from a certain caution exercised by companies.

# 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 2013**

At its quarterly assessment of 14 March 2013, the SNB reaffirms that it will continue to enforce the minimum exchange rate of CHF 1.20 per euro with the utmost determination and will, if necessary, buy foreign currency in unlimited quantities for this purpose. The minimum exchange rate is an important instrument in avoiding an undesirable tightening of monetary conditions. The Swiss franc is still high. The target range for the three-month Libor remains unchanged at 0.0–0.25%. The SNB stands ready to take further measures at any time.

**February 2013**

On 13 February 2013, the Federal Council activates the countercyclical capital buffer, following the SNB's proposal. This move is in reaction to the growing imbalances on the mortgage and real estate markets. The level of the capital buffer is set at 1% of risk-weighted mortgage loans financing residential property located in Switzerland. The deadline for compliance by the relevant banks is 30 September 2013.

**December 2012**

At its quarterly assessment of 13 December 2012, the SNB reaffirms that it will continue to enforce the minimum exchange rate of CHF 1.20 per euro with the utmost determination and is prepared to buy foreign currency in unlimited quantities for this purpose. Even at the current rate, the SNB considers the Swiss franc to be still high. The SNB is leaving the target range for the three-month Libor unchanged at 0.0–0.25%. If necessary, it stands ready to take further measures at any time.

**September 2012**

At its quarterly assessment of 13 September 2012, the SNB reaffirms that it will maintain the minimum exchange rate of CHF 1.20 per euro and will enforce it with the utmost determination. It remains prepared to buy foreign currency in unlimited quantities for this purpose. In the view of the SNB, the Swiss franc is still high and is weighing on the Swiss economy. The target range for the three-month Libor remains unchanged at 0.0–0.25%. If necessary, the SNB stands ready to take further measures at any time.

**June 2012**

On 25 June 2012, the SNB concludes a Swiss franc/zloty swap agreement with the National Bank of Poland (NBP). In the event of tensions in the Swiss franc interbank market, the facility enables the NBP to provide Swiss franc liquidity to banks in Poland.

At its quarterly assessment of 14 June 2012, the SNB reaffirms that it will maintain the minimum exchange rate of CHF 1.20 per euro and will enforce it with the utmost determination. It remains prepared to buy foreign currency in unlimited quantities for this purpose. Even at the current rate, it considers the Swiss franc to be still high. If necessary, the SNB stands ready to take further measures at any time. The target range for the three-month Libor will remain unchanged at 0.0–0.25%.

**March 2012**

At its quarterly assessment of 15 March 2012, the SNB reaffirms that it will continue to enforce the minimum exchange rate of CHF 1.20 per euro 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.

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