

Quarterly Bulletin
2/2013 June

SCHWEIZERISCHE NATIONALBANK
BANQUE NATIONALE SUISSE
BANCA NAZIONALE SVIZZERA
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2/2013 June

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Monetary policy report

Report for the attention of the Governing Board of the Swiss National Bank for its quarterly assessment of June 2013

The report 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. The first section ('Monetary policy decision of 20 June 2013') is an excerpt from the press release published following the assessment.

This report is based on the data and information available as at 20 June 2013. 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 20 June 2013

SNB reaffirms minimum exchange rate

The Swiss National Bank (SNB) is maintaining its minimum exchange rate of CHF 1.20 per euro. 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. In the current environment, the minimum exchange rate remains important in order to avoid an undesirable tightening of monetary conditions for Switzerland in the event of sudden upward pressure on the Swiss franc. The SNB stands ready to enforce the minimum exchange rate, if necessary, by buying foreign currency in unlimited quantities, and to take further measures, as required. The target range for the three-month Libor will be left unchanged at 0.0–0.25%.

Since March, the SNB's conditional inflation forecast has remained almost unchanged, apart from inflation for the current year, which is slightly lower due to a reduction in the oil price. The forecast is again based on an unchanged three-month Libor of 0.0% over the next three years. For 2013, the SNB now anticipates slightly lower inflation of –0.3%. For 2014, the inflation forecast is unchanged at 0.2% and for 2015, at 0.7%. Consequently, inflation in Switzerland will remain very low in the foreseeable future.

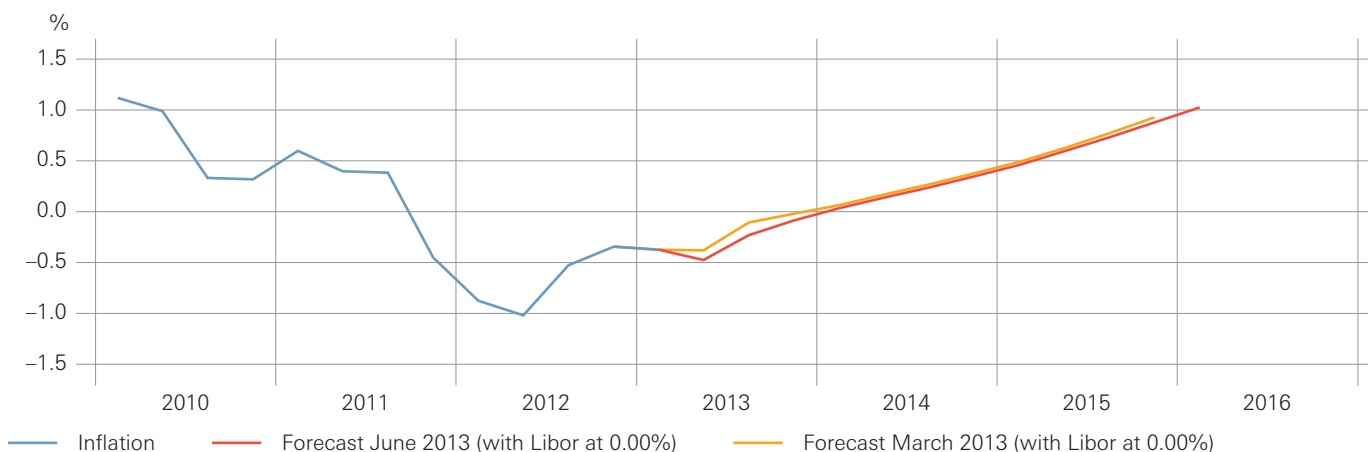
In the first quarter of 2013, the global economy was weaker than expected. The recession continued in the euro area. In the US, the recovery remained hesitant and in China, economic activity lost strength. In Switzerland, real GDP rose significantly in the first quarter. However, the SNB expects a perceptible weakening in growth for the second quarter. Overall, it still anticipates growth of 1.0–1.5% for 2013.

The risks for the Swiss economy remain high. They continue to originate, for the most part, from the international environment. A weakening in global economic momentum cannot be excluded. Further developments in the euro area financial and sovereign debt crisis remain uncertain. Tensions can reappear at any moment on global financial markets. Domestically, there is a risk that the imbalances on the mortgage and real estate markets will grow, given the sustained period of exceptionally low interest rates.

Chart 1.1

CONDITIONAL INFLATION FORECAST OF JUNE 2013

Percentage change in Swiss consumer price index from previous year



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.

Table 1.1

OBSERVED INFLATION IN JUNE 2013

	2010				2011				2012				2013				2010	2011	2012
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
Inflation	1.1	1.0	0.3	0.3	0.6	0.4	0.4	-0.5	-0.9	-1.0	-0.5	-0.3	-0.4				0.7	0.2	-0.7

CONDITIONAL INFLATION FORECAST OF JUNE 2013

	2013				2014				2015				2016				2013	2014	2015	
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4				
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
Forecast June 2013, Libor at 0.00%		-0.5	-0.2	-0.1	0.0	0.1	0.2	0.3	0.5	0.6	0.7	0.9	1.0					-0.3	0.2	0.7

Source: SNB

2 Global economic environment

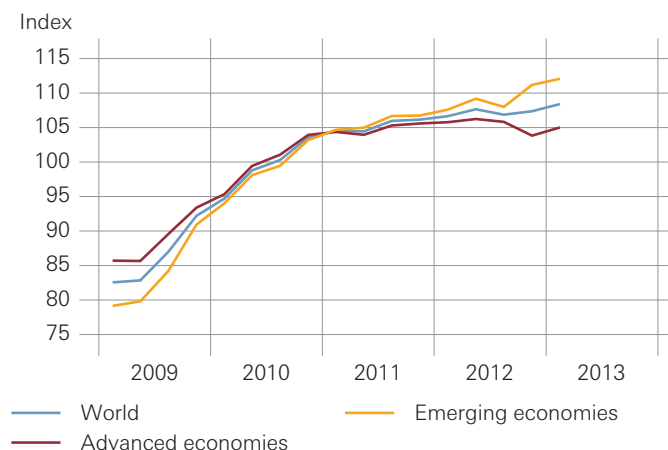
In the first quarter, the global economy was weaker than expected. In the emerging markets, particularly China, economic activity lost strength. In the euro area, GDP continued to decline perceptibly, and in the US, the recovery remained hesitant. The only advanced economy to gain significant momentum was Japan. Overall, global growth came to around 3%, while world trade volume increased by a modest amount (cf. chart 2.1).

However, in the quarters ahead, global GDP growth is likely to firm up gradually. In the US, consumer spending is being driven by the slow but steady recovery on the labour market and rising asset prices. In Japan, the very expansionary economic policy is having an invigorating effect. Finally, owing to the observed easing of financial market conditions and the upturn in world trade, the euro area is also likely to emerge gradually from recession. In addition, the fiscal policy burden will decline in most member states next year. The rally in world trade will lend momentum to emerging economies. As several of these countries are endeavouring to curb strong credit growth and lower inflation expectations, economic growth is unlikely to reach the peaks seen in the recent past.

Chart 2.1

GLOBAL EXPORTS

Period average = 100

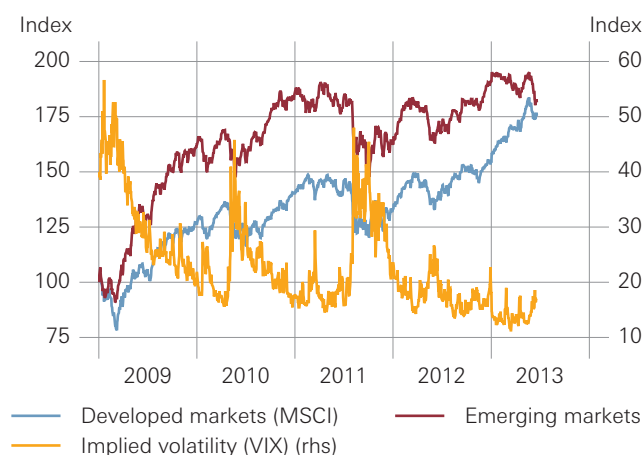


Sources: CPB, Thomson Financial Datastream

Chart 2.2

STOCK MARKETS

Beginning of period = 100 (lhs), daily figures



Sources: Reuters, Thomson Financial Datastream

Table 2.1

BASELINE SCENARIO FOR GLOBAL ECONOMIC DEVELOPMENTS

	Scenario					
	2010	2011	2012	2013	2014	2015
GDP, year-on-year change in percent						
Global ¹	5.1	3.7	2.9	3.0	4.3	4.6
US	2.4	1.8	2.2	2.0	2.8	3.5
Euro area	1.9	1.5	-0.5	-0.6	1.2	2.2
Japan	4.7	-0.5	2.0	1.9	2.3	1.1
Oil price in USD per barrel ²						
	79.6	111.4	111.7	105.4	103.0	103.0

¹ PPP-weighted (United States, Euro area, United Kingdom, Japan, China, South Korea, Taiwan, Hong Kong, Singapore, India, Brazil and Russia).

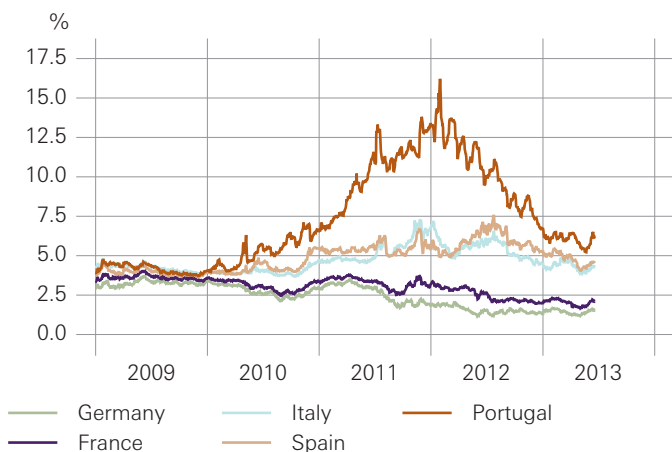
² Level.

Sources: SNB, Thomson Financial Datastream

Chart 2.3

EUROPEAN LONG-TERM INTEREST RATES

10-year government instruments, daily figures



Source: Thomson Financial Datastream

Chart 2.4

INTERNATIONAL LONG-TERM INTEREST RATES

10-year government instruments, daily figures

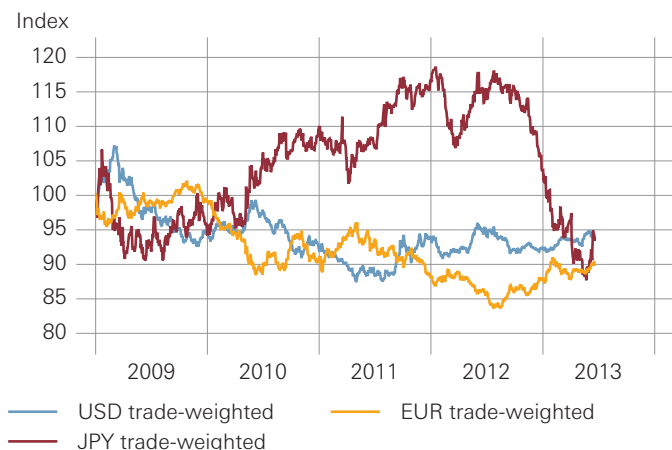


Source: Thomson Financial Datastream

Chart 2.5

EXCHANGE RATES

Beginning of period = 100, daily figures



Sources: Reuters, Thomson Financial Datastream

The SNB has revised its short-term global growth forecast slightly downwards. This is largely due to the persistently weak growth in individual EU member states. The outlook for the global economy remains highly uncertain, and the downside risks continue to prevail. The main risk remained the European financial and government debt crisis. In its baseline scenario, the SNB assumes that the crisis will eventually be overcome as the problems are gradually resolved. In the short term, however, renewed tensions on the financial markets cannot be ruled out. In some emerging markets there is also a risk that structural problems are not being dealt with decisively enough and that the current economic weakness will therefore persist.

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 103 per barrel; USD 13 lower than assumptions made three months ago. On balance, international commodity prices have fallen in recent weeks. For the euro, the SNB assumes an exchange rate of USD 1.30.

INTERNATIONAL FINANCIAL AND COMMODITY MARKETS

Since the monetary policy assessment in mid-March, the financial markets have been characterised by increased volatility. The mood initially improved, driven by the European Central Bank's (ECB) more expansionary monetary policy and the new economic policy in Japan. In addition, both the ongoing reduction of oversupply in the real estate market and private household debt in the US had a positive effect. In May, however, uncertainty increased again in the wake of speculation that the US Federal Reserve may start scaling back its securities purchases and following disappointment over initial structural reform plans in Japan.

Against this background, global stock market indices trended upwards at first (cf. chart 2.2). In the US, the stock market reached a historical high, while in Europe and Japan, it rallied once again. However, as of mid-May, the strong price gains seen in previous weeks eroded again to some extent. The euro trended sideways against the US dollar. Influenced by a change of monetary policy in Japan, the yen depreciated further on a trade-weighted basis (cf. chart 2.5). On the bond markets, risk premia on southern European government instruments declined again against German government bonds. Government bond yields in the US, Japan and Germany rose in recent weeks, but remained low in historical terms (cf. chart 2.4).

The commodities markets were slightly weaker overall. Growth-related fears with regard to China squeezed prices of cyclical industrial commodities. On the back of modest global demand, an increasing oil supply and high oil inventories in the US, oil prices fell (cf. chart 2.6). By contrast, prices for agricultural commodities remained largely unchanged.

UNITED STATES

The US economy expanded by 2.4% in the first quarter of 2013, after having virtually stagnated the previous quarter as a result of temporary factors (cf. chart 2.7). Private domestic demand remained the driving force in the first quarter, while lower defence spending and a negative external contribution hampered growth. Aggregate economic capacity utilisation is still low and unemployment remains high, at 7.6% in May (cf. chart 2.10).

The SNB expects private domestic demand and equipment investment to pick up gradually towards the end of the year. Residential construction should continue to expand briskly, but owing to its small contribution to GDP, it is likely to have only a relatively minor impact on growth. Fiscal policy is expected to have a dampening effect over the next few years. Overall, the SNB has revised its growth forecast slightly downwards for the US economy. For 2013 and 2014, it now expects growth of between 2.0% and 2.8% (cf. table 2.1). As a result of the restrictive fiscal policy, the government budget deficit will probably decline rapidly, and the ratio of debt to GDP should decrease slowly from the end of 2014.

Inflation measured in terms of consumer prices eased in May to 1.4% (cf. chart 2.11). The less volatile core inflation also fell slightly to 1.7% (cf. chart 2.12). As aggregate economic capacity utilisation is still low and wages are exhibiting weak growth, inflationary pressure is likely to remain moderate for the time being.

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 stays above 6.5%, its medium-term inflation forecast does not exceed 2.5%, and long-term inflation expectations remain well anchored, the Federal Reserve does not intend to raise its key interest rate. It will continue to purchase securities amounting to USD 85 billion each month as long as there is no significant improvement in the outlook on the labour market and price stability is not endangered.

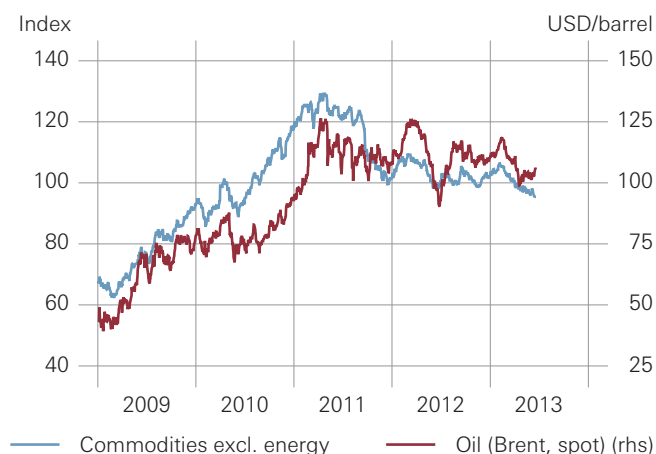
EURO AREA

The recession in the euro area continued. GDP declined by 0.8% in the first quarter, following a drop of 2.3% in the previous quarter (cf. chart 2.7). The fall was thus more pronounced than originally forecast. Exports and investments continued to contract. Moreover, unfavourable weather conditions had a dampening effect on value added in construction. In Germany, GDP increased slightly, but declined further in France. The recession remained pronounced in the southern member states. In addition to fiscal consolidation measures, uncertainty over elections in Italy and the banking crisis in Cyprus contributed to the weak demand in the euro area. The recession – which has now persisted for six

Chart 2.6

COMMODITY PRICES

Daily figures

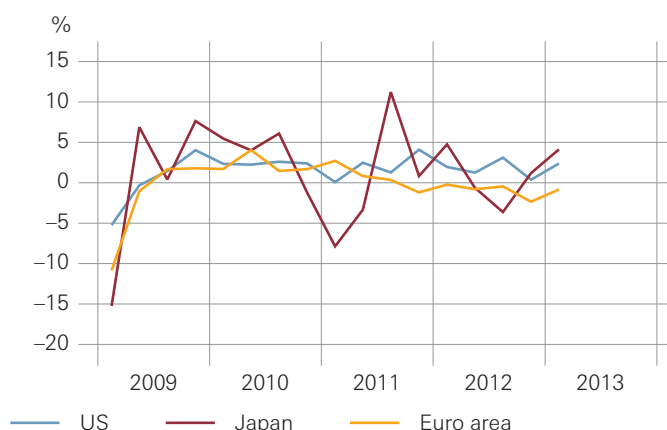


Sources: Reuters, Thomson Financial Datastream

Chart 2.7

REAL GDP: ADVANCED ECONOMIES

Change from previous period

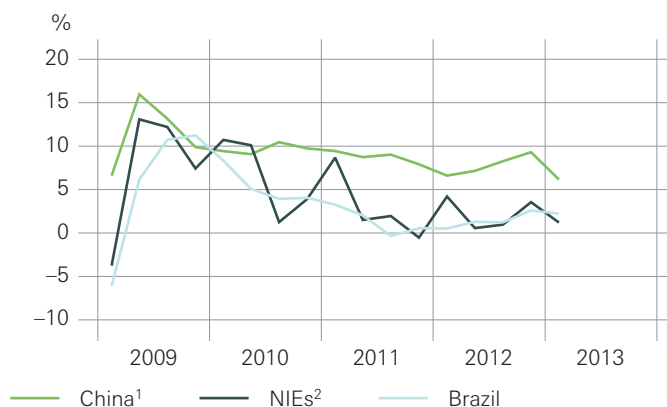


Source: Thomson Financial Datastream

Chart 2.8

REAL GDP: EMERGING ECONOMIES

Change from previous period



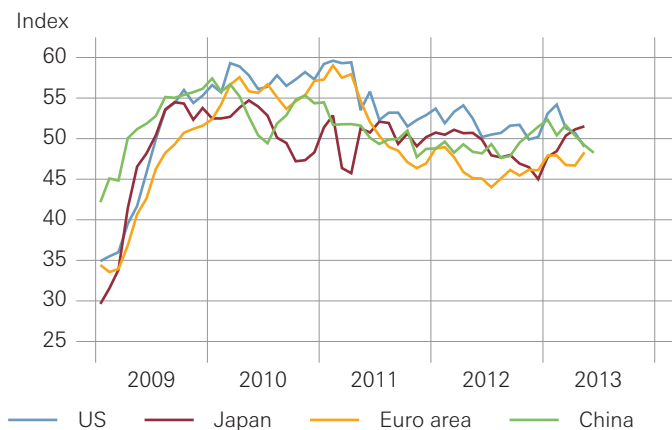
1 Estimate: SNB.

2 PPP-weighted (South Korea, Taiwan, Hong Kong, Singapore).

Source: Thomson Financial Datastream

Chart 2.9

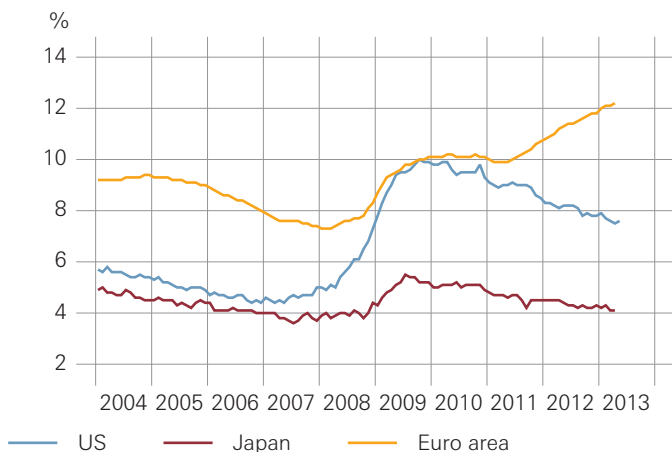
PURCHASING MANAGERS' INDICES (MANUFACTURING)



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

Chart 2.10

UNEMPLOYMENT RATES

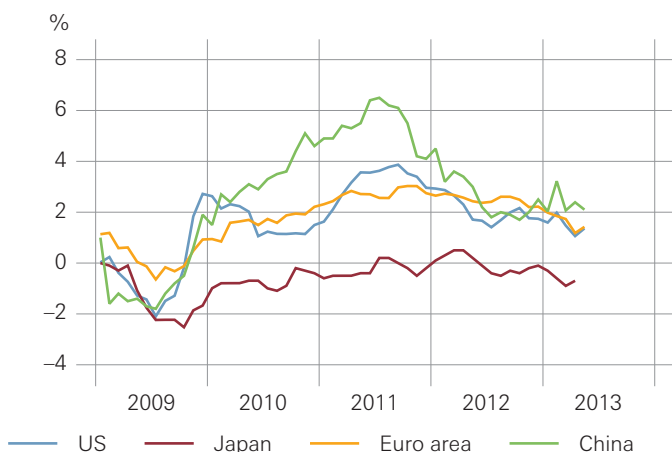


Source: Thomson Financial Datastream

Chart 2.11

CONSUMER PRICES

Year-on-year change



Source: Thomson Financial Datastream

quarters – is reflected in record-high unemployment rates (cf. chart 2.10).

Available indicators suggest that the economic situation in the euro area remained difficult in the second quarter, too. There is hardly any sign of a revival in investment activity so far. Corporate demand for credit is still declining and employment plans remain cautious. The easing on financial markets and the expected gradual recovery in exports should help bring the recession to an end in the course of the year, however. As of year-end, the restrictive effects of fiscal policy should dwindle.

The SNB has lowered its GDP forecast for 2013 to -0.6%. This reflects the disappointing developments in France and Italy. For 2014, however, the SNB still expects to see growth of just over 1%.

Consumer price inflation in the euro area declined to 1.4% in May, owing to lower energy prices (cf. chart 2.11). Core inflation remained at around 1.2% (cf. chart 2.12). The inflation expectations derived from surveys and financial market data for the current year are still low.

In May, the ECB lowered its main refinancing rate by 25 basis points to 0.50% (cf. chart 2.13). Furthermore, as part of its refinancing transactions, it is providing banks with unlimited liquidity until at least mid-2014. Additional easing measures are being reviewed and include improving the credit supply for small and medium-sized enterprises in cooperation with other EU institutions.

JAPAN

Influenced by the economic policy measures implemented since the beginning of the year, Japanese GDP grew substantially in the first quarter, to 4.1% (cf. chart 2.7). Exports picked up, and private spending recorded robust growth, partly a result of the boost in confidence after the stock market peak and the positive effect of the announced economic programmes. Corporate investment remained weak, declining for the fifth consecutive quarter.

The Japanese economy is likely to maintain its growth trajectory in the quarters to come, with the planned public sector infrastructure projects and the positive momentum for exports generated by the yen's sharp depreciation. Household and business confidence has improved considerably since December 2012 and is now at the highest level since summer 2007, when the economy was still expanding rapidly. The boost in business confidence also seems to be gaining ground across all sectors. Against this background, it is likely that corporate investment will gradually increase again. The SNB raised its GDP forecast for 2013 to around 2% and still expects to see growth of just over 2% for 2014. In the medium term, Japan will have to adopt a course of financial policy consolidation, which will slow growth.

Even after excluding prices for energy and food, Japanese consumer prices in April were around half a percentage point below their year-back level (cf. charts 2.11 and 2.12). The yen's depreciation, which has continued since mid-2012, and the increases in electricity prices planned for this year will push up inflation in the months ahead. Furthermore, the gradual rise in inflation expectations could generate positive momentum for prices in the medium term.

The Bank of Japan implemented a regime change in April. The core element of the new monetary policy is the planned doubling of the monetary base – i.e. the sum of sight deposits and cash in circulation – to JPY 270 trillion, which corresponds to around half of nominal GDP (cf. chart 2.14). The liquidity injection will be implemented by means of large-scale purchases of Japanese government bonds with long maturities. The aim is to bring inflation to 2% within around two years.

EMERGING ECONOMIES

The economic upswing in emerging economies slowed in the first quarter. Key common factors included the muted demand from advanced economies, uncertainty surrounding the outcome of the European financial and sovereign debt crisis, and weaker consumer demand.

Following a recovery in autumn 2012, the Chinese economy lost some ground again (cf. chart 2.8). New anti-corruption measures in the public sector, in particular, dampened demand, while state infrastructure investment continued to shore up the economy. By contrast, in India the cyclical industries contributed to a tentative economic recovery, thanks to more favourable financing conditions. GDP growth in the newly industrialised economies of Asia was weaker overall in the first quarter, although the trends varied quite sharply from country to country. Growth in Brazil was moderate, as the high inflation rate squeezed real disposable incomes and thus also private consumption.

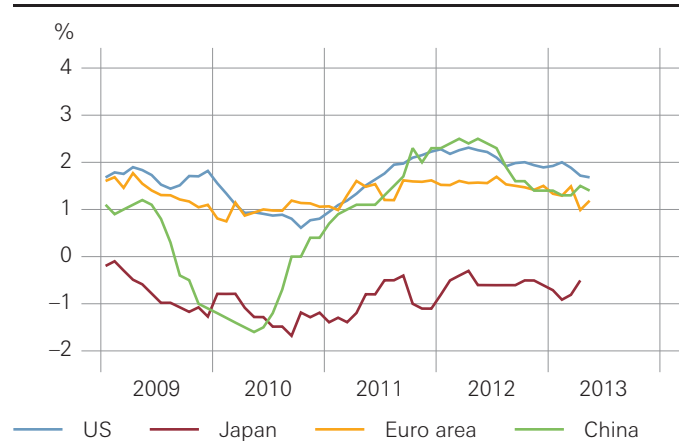
Generally speaking, it can be assumed that the economic uptrend in emerging economies will improve again. The sharp depreciation in the yen is weighing on the export prospects of some economies such as South Korea and Taiwan, whose export sectors compete directly with Japan, while others are benefiting from the rising Japanese demand for intermediate products. Consumer spending by private households is likely to pick up, owing to robust growth in incomes. The monetary and fiscal policy easing introduced in recent quarters also helped drive this trend.

Consumer price inflation in emerging economies has developed to differing degrees since the beginning of the year. In China it remained moderate; with core inflation of under 2%, the annual inflation rate in May stood at 2.1% (cf. charts 2.11 and 2.12). In India, annual inflation dropped to 4.7%, while in Brazil it climbed to 6.5% in

Chart 2.12

CORE INFLATION RATES¹

Year-on-year change



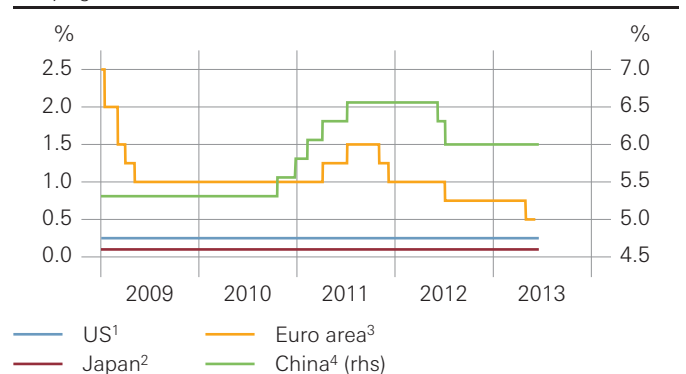
1 Excluding food and energy.

Sources: CEIC, Thomson Financial Datastream

Chart 2.13

OFFICIAL INTEREST RATES

Daily figures



1 Federal funds rate.

2 Call money target rate.

3 Main refinancing rate.

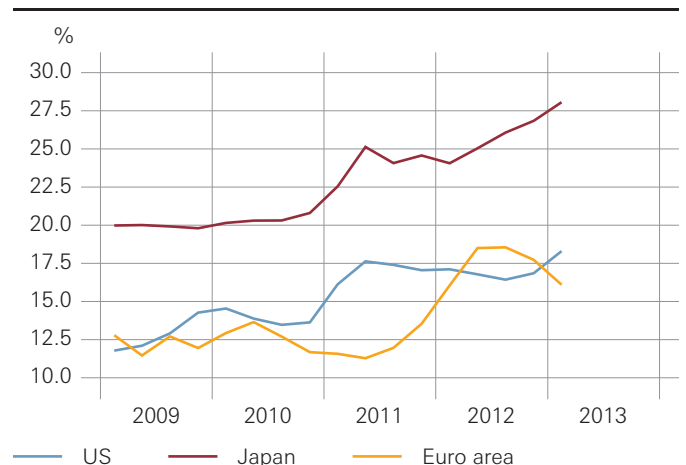
4 One-year lending rate.

Source: Thomson Financial Datastream

Chart 2.14

MONETARY BASE

Relative to GDP



Source: Thomson Financial Datastream

the wake of higher import and food prices, thus coming to rest in the upper end of the central bank's target range.

Differences in economic and inflation trends also shaped monetary policy. Brazil's central bank raised key interest rates in April and May, after having been massively scaled back up to October 2012. In India, meanwhile, the decline in inflation prompted the central bank to ease monetary policy even further. The Bank of Korea also lowered its leading interest rate in May in order to support the fiscal economic measures implemented in April. China's central bank tolerated strong credit growth, but in a countermove also permitted the currency to continue appreciating on a trade-weighted basis.

3 Economic developments in Switzerland

As expected, GDP growth in Switzerland experienced a temporary revival in the first quarter. According to preliminary estimates by the State Secretariat for Economic Affairs (SECO), real GDP increased by 2.3% in the first quarter. While private consumer spending and construction investment showed a positive trend, stimuli from abroad remained weak. In contrast to the previous quarter, foreign trade contributed to growth, but this was mainly due to a marked decrease in imports. Equipment investment also declined.

The robust GDP growth meant that the negative output gap narrowed slightly in the first quarter. Capacity utilisation in manufacturing went up, but remained at a low level. However, the situation on the labour market deteriorated further, resulting in another slight rise in unemployment figures in spring.

For the second quarter, the SNB is forecasting a perceptible weakening in growth. Afterwards, economic activity is likely to gradually regain some momentum in step with developments in the global economy. For 2013, the SNB still expects to see GDP growth of 1.0–1.5%.

AGGREGATE DEMAND AND OUTPUT

Growing value added in construction and financial industries

GDP grew strongly in the first quarter of 2013. Growth stimuli mainly came from the construction and financial industries (cf. chart 3.1). Healthcare continued its dynamic performance as well. Other industries, however, exhibited only weak growth. After a decline in the previous quarter, value added in manufacturing increased slightly. Trade stagnated. However, the hospitality industry, which had stabilised in the past few quarters, suffered a setback.

Positive foreign trade contribution despite falling exports

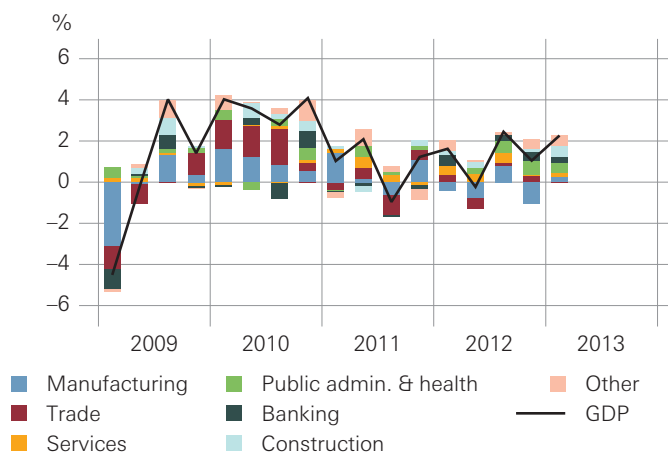
Net exports (excluding valuables) increased substantially in the first quarter (cf. chart 3.2). While exports registered a slight decline compared with the previous quarter (cf. chart 3.3), imports dropped sharply (cf. chart 3.4). This resulted in a positive foreign trade contribution to GDP growth of roughly 2.5 percentage points.

The weak global economy had a dampening effect on machinery and metals exports. By contrast, exports of goods in the watches and jewellery segment as well as

Chart 3.1

CONTRIBUTIONS TO GROWTH, BY SECTOR

Change from previous period

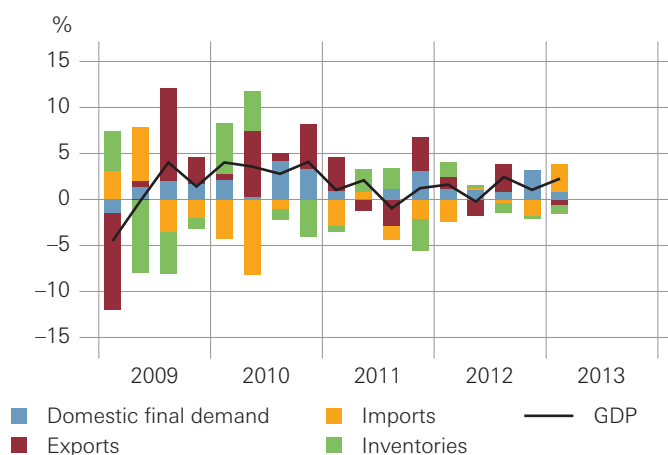


Source: State Secretariat for Economic Affairs (SECO)

Chart 3.2

CONTRIBUTIONS TO GROWTH IN DEMAND

Change from previous period

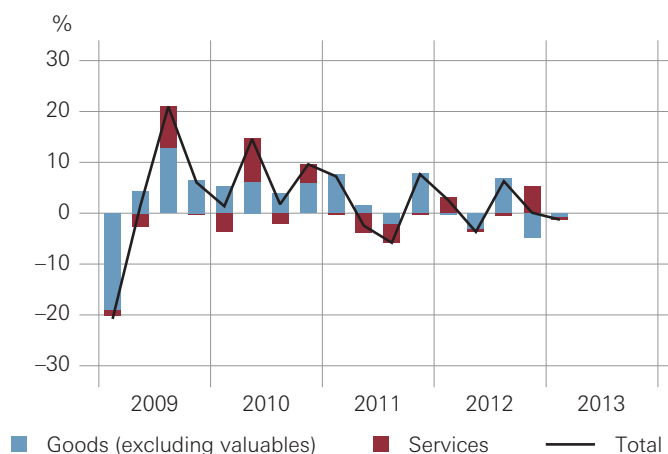


Source: SECO

Chart 3.3

CONTRIBUTIONS TO EXPORT GROWTH

Change from previous period

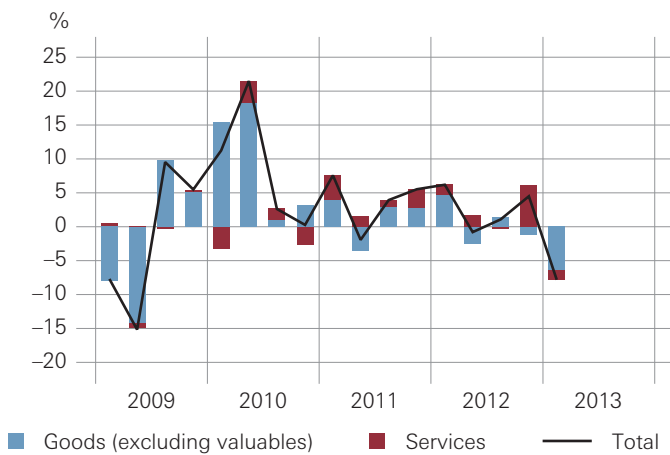


Source: SECO

Chart 3.4

CONTRIBUTIONS TO IMPORT GROWTH

Change from previous period



Source: SECO

exports of railway rolling stock increased. The officially reported decline in goods exports was largely due to a revision in the methodology of recording electricity trading.

Exports of services also declined overall. Receipts from transport and tourism exports fell. By contrast, receipts from merchanting rose considerably after three weak quarters.

Sound domestic demand

Domestic final demand continued to expand in the first quarter (cf. chart 3.5 and table 3.1). Benefiting from immigration, rising real income over the past few quarters, as well as the recent improvement in consumer confidence, private consumption once again proved to be an important economic driver. In particular, private households spent more on healthcare and housing. Especially the cold weather led to higher heating oil consumption.

Table 3.1

REAL GDP AND COMPONENTS

Growth rates on previous period in percent, annualised

	2009	2010	2011	2012	2011			2012				2013
					Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1
Private consumption	1.8	1.6	1.2	2.5	1.7	0.9	3.3	3.9	1.6	1.3	4.5	2.5
Government consumption	3.3	0.7	2.0	0.5	7.8	3.6	3.2	-7.9	1.6	4.7	3.6	-3.5
Investment in fixed assets	-8.0	4.8	4.0	-0.2	-8.3	1.2	4.2	-0.8	-0.6	-2.2	0.8	-1.4
Construction	3.0	3.5	2.4	-3.2	-3.9	-2.4	-3.6	-11.9	4.6	1.8	0.8	1.0
Equipment	-15.5	5.8	5.2	2.4	-11.7	4.2	11.0	9.1	-4.5	-5.3	0.9	-3.3
Domestic final demand	-0.4	2.2	1.9	1.7	0.0	1.3	3.5	1.3	1.1	0.9	3.6	0.9
Change in inventories ¹	0.1	0.5	-0.2	0.1	2.4	2.3	-3.5	1.5	0.3	-1.0	-0.4	-1.0
Total exports ²	-7.3	7.5	3.8	1.2	-2.4	-5.8	7.7	2.6	-3.7	6.3	0.1	-1.3
Goods ²	-11.1	9.4	6.3	1.6	2.3	-3.1	11.4	-0.3	-4.4	9.9	-6.9	-0.9
Services	1.2	3.7	-1.4	0.3	-12.0	-11.7	-0.7	10.0	-2.1	-1.4	17.3	-2.1
Total imports ²	-5.3	8.1	3.9	3.2	-1.9	3.9	5.5	6.2	-0.8	1.1	4.5	-7.8
Goods ²	-8.3	10.6	3.1	1.7	-4.3	3.5	3.3	5.8	-3.0	1.7	-1.4	-8.1
Services	9.0	-1.5	7.3	9.4	8.7	5.6	15.2	8.1	8.9	-1.4	31.0	-6.9
Net exports ³	-1.6	0.6	0.4	-0.6	-0.5	-4.4	1.6	-1.1	-1.5	2.6	-1.7	2.5
GDP	-1.9	3.0	1.9	1.0	2.1	-1.0	1.2	1.6	-0.2	2.4	1.0	2.3

1 Contribution to growth in percentage points (including statistical discrepancy).

2 Excluding valuables (precious metals, precious stones and gems as well as works of art and antiques).

3 Contribution to growth in percentage points.

Source: SECO

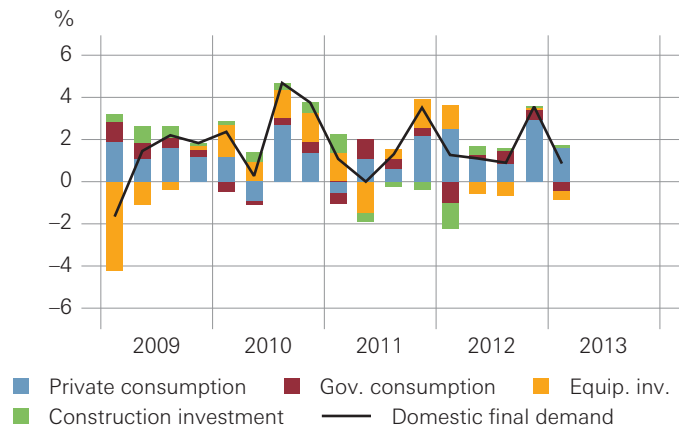
Due to capacity shortages and adverse weather conditions, construction investment rose only modestly in the first quarter. Development in the different construction segments varied quite considerably. While there was no growth in civil engineering, turnover in structural engineering – driven by dynamic residential construction – increased. This trend is likely to continue in the quarters ahead. Thus fewer new orders were received in civil engineering, according to the Swiss Federation of Master Builders, while new residential construction clearly exceeded the previous year’s level.

Equipment investment declined in the first quarter. Investment in machinery, in particular, suffered from the still low utilisation of technical capacity. Given the uncertain global economic outlook, companies continue to be reticent about investing.

Chart 3.5

DOMESTIC FINAL DEMAND, GROWTH CONTRIBUTIONS

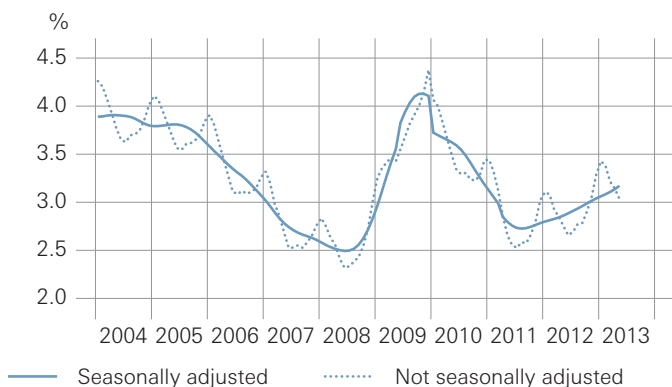
Change from previous period



Source: SECO

Chart 3.6

UNEMPLOYMENT RATE



Unemployed 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

LABOUR MARKET

The situation on the labour market has deteriorated slightly since mid-2011. Even though job creation has continued to increase, unemployment is up. By international standards, however, the situation on the Swiss labour market continues to be favourable.

Rising unemployment

Unemployment has been rising slowly, but steadily for two years now. Between February and May, the number of people registered as unemployed with regional employment offices increased by almost 3,700 on a seasonally adjusted basis. The unemployment rate climbed to 3.2% (cf. chart 3.6).

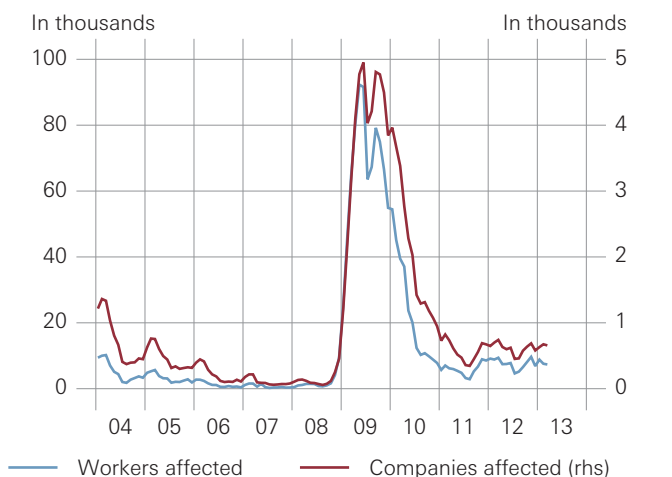
Short-time working remained low in the first quarter (cf. chart 3.7). In March, approximately 7,400 people were affected by short-time working.

Employment growth flagging

According to the statistics on employment published by the Swiss Federal Statistical Office (SFSO), employment momentum abated somewhat in the first quarter. The number of full-time and part-time jobs increased by 1.4% compared with the previous quarter. Expressed in terms of full-time equivalents, the rise in employment amounted to 1.1%. As in previous quarters, the growth in job numbers is essentially limited to the construction industry and the services sector (cf. chart 3.8). Manufacturing, financial services and the hospitality industry, however, cut jobs.

Chart 3.7

SHORT-TIME WORKING

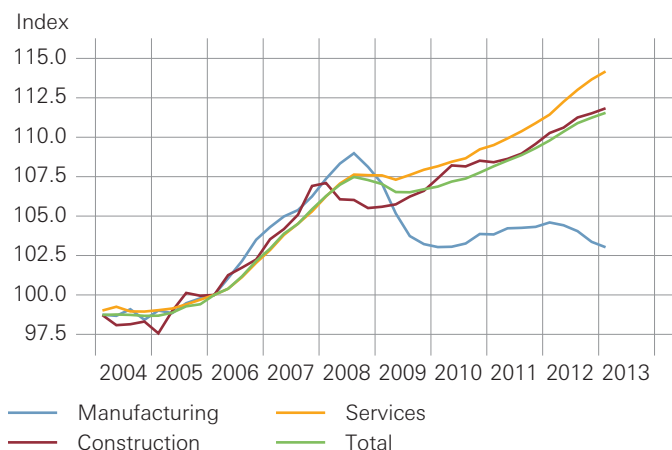


Source: SECO

Chart 3.8

FULL-TIME EQUIVALENT EMPLOYMENT

Q1 2006 = 100



Source: Swiss Federal Statistical Office (SFSO)

CAPACITY UTILISATION

Manufacturing sees slight recovery

According to the survey conducted by KOF Swiss Economic Institute, in the first quarter utilisation of technical capacity in manufacturing rose for the first time in nearly two years. At 81.3%, it was significantly higher than in the fourth quarter (80.2%), but remained well below the long-term average (cf. chart 3.9). In construction too, the level of machine utilisation increased again. Thus, capacity utilisation in this sector remains exceptionally high (cf. chart 3.10). As a result, many of the companies surveyed were still reporting bottlenecks in machine and equipment capacity as well as labour shortages. In the services sector, surveys still suggest average utilisation.

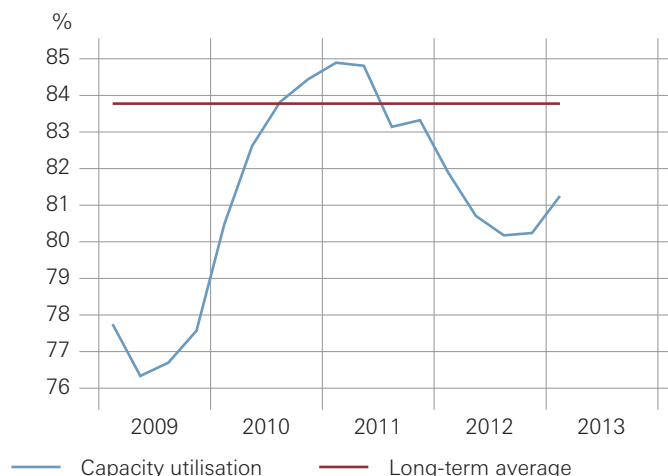
Negative output gap

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. While robust GDP growth in the first quarter narrowed the gap somewhat, it remains negative. Estimated potential output calculated by means of the production function approach shows an output gap of -1.3% for the first quarter (cf. chart 3.11). Estimates using other methods (Hodrick-Prescott filter and multivariate filter) suggest a somewhat narrower output gap (-0.7% in both cases).

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 purely statistical filtering methods.

Chart 3.9

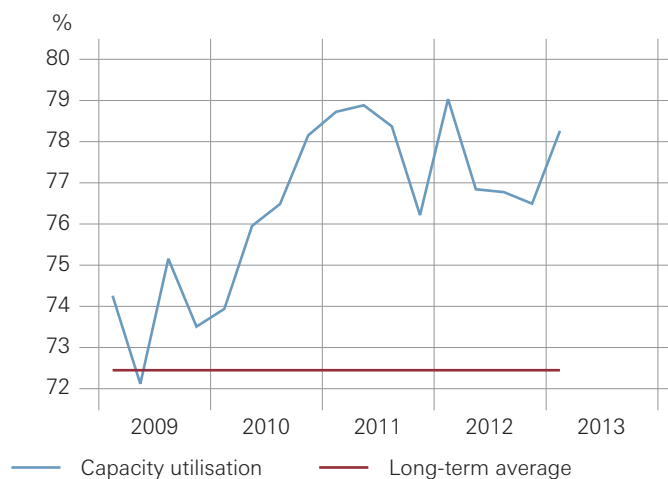
CAPACITY UTILISATION IN MANUFACTURING



Source: KOF Swiss Economic Institute

Chart 3.10

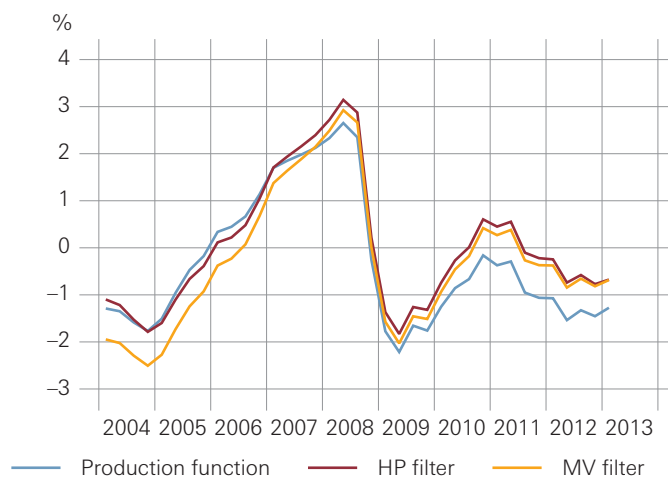
CAPACITY UTILISATION IN CONSTRUCTION



Source: KOF Swiss Economic Institute

Chart 3.11

OUTPUT GAP



Source: SNB

Chart 3.12

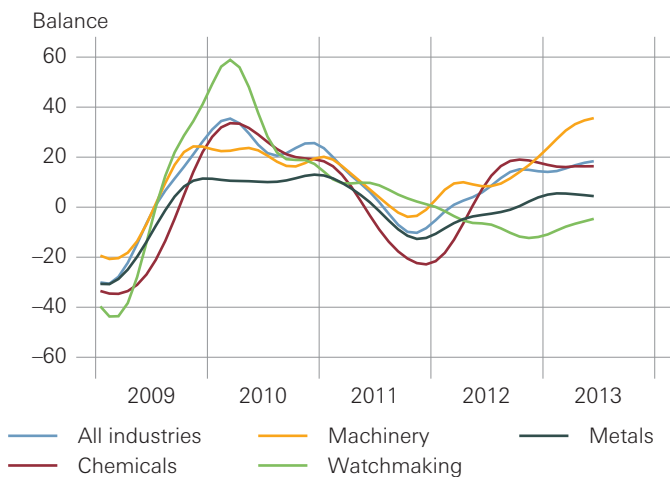
PURCHASING MANAGERS' INDEX (MANUFACTURING)



Source: Credit Suisse

Chart 3.13

EXPECTED NEW ORDERS

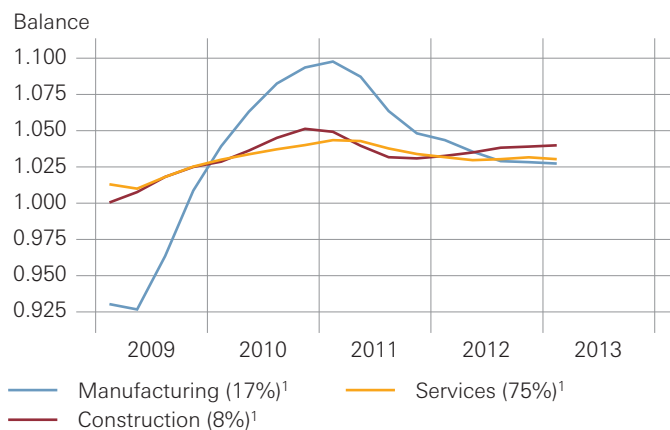


Source: KOF Swiss Economic Institute

Chart 3.14

EMPLOYMENT OUTLOOK INDICATOR

Seasonally adjusted



¹ 2010 employment share in brackets.
Source: SFSO; seasonal adjustment: SNB

OUTLOOK FOR THE REAL ECONOMY

The growth outlook for Switzerland has changed little since the last monetary policy assessment. After the temporary revival in the first quarter, the SNB is expecting a perceptible weakening in growth for the second quarter. Positive momentum is once more to be expected from industries with a domestic focus, which are benefiting from the comparatively robust labour market, immigration and favourable lending conditions. However, sluggish economic growth abroad, in particular in the euro area, has dampened the mood of Swiss export companies again somewhat. Value added in both in the export-based industries and manufacturing is therefore not likely to increase in the short term.

The SNB expects that, in step with the overall recovery of the global economy, economic activity in Switzerland will gradually gather pace again. For 2013 as a whole, it is predicting GDP growth of 1.0–1.5%. The output gap is likely to remain negative for the time being and unemployment will probably increase again in the short term.

Under the baseline scenario for the global economy, which is described in chapter 2, risks are still tilted mainly to the downside. The economic forecast for Switzerland, therefore, is also subject to a downside risk.

4

Prices and inflation expectations

Consumer prices are still slightly below the previous year's level, which is mainly attributable to lower prices on imported goods. Domestic goods prices, by contrast, remained largely stable. The same applies to supply prices, which have an upstream effect on consumer prices. They stayed virtually unchanged year-on-year.

Inflation expectations as reported in surveys have hardly changed over the past few quarters. Medium-term expectations are still in the low positive range, which is consistent with the SNB's definition of price stability.

CONSUMER PRICES

CPI inflation remains in negative territory

The annual inflation rate as measured by the national consumer price index (CPI) has been negative since autumn 2011. It sank slightly in the past few months, amounting to -0.5% in May, following -0.3% recorded in January and February (cf. table 4.1).

Lower prices of imported goods

The decline in annual inflation is driven by developments in the CPI's foreign components (cf. chart 4.1). The annual rate fell significantly from -1.7% in January to -2.7% in May, which is mainly attributable to oil products. Changes in price increases for oil products are, however, influenced by a statistical base effect. Whereas current-year prices for oil products were lower in May than in January, they recorded a rise over the same period in 2012.

Table 4.1

NATIONAL CONSUMER PRICE INDEX AND COMPONENTS

Year-on-year change in percent

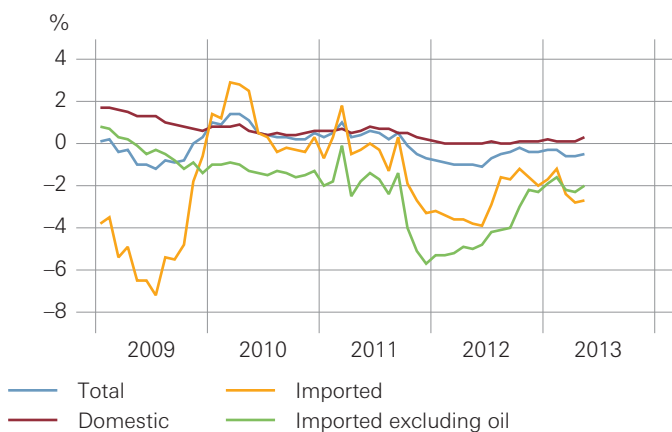
	2012	2012			2013	2013		
		Q2	Q3	Q4	Q1	March	April	May
Overall CPI	-0.7	-1.0	-0.5	-0.3	-0.4	-0.6	-0.6	-0.5
Domestic goods and services	0.0	0.0	0.0	0.1	0.1	0.1	0.1	0.3
Goods	-1.8	-2.1	-1.8	-1.0	-0.8	-0.8	-0.6	-0.7
Services	0.6	0.6	0.6	0.4	0.4	0.3	0.3	0.6
Private services excluding rents	0.6	0.6	0.6	0.5	0.5	0.5	0.5	0.6
Rents	0.6	0.7	0.6	0.2	-0.2	-0.3	-0.3	0.3
Public services	0.4	0.3	0.3	0.6	1.1	1.1	1.1	1.1
Imported goods and services	-2.7	-3.8	-2.1	-1.6	-1.8	-2.4	-2.8	-2.7
Excluding oil products	-4.2	-4.9	-4.1	-2.5	-1.9	-2.2	-2.3	-2.0
Oil products	5.0	2.2	8.7	3.0	-1.0	-3.2	-5.5	-6.3

Sources: SFSO, SNB

Chart 4.1

CPI: DOMESTIC AND IMPORTED GOODS AND SERVICES

Year-on-year change

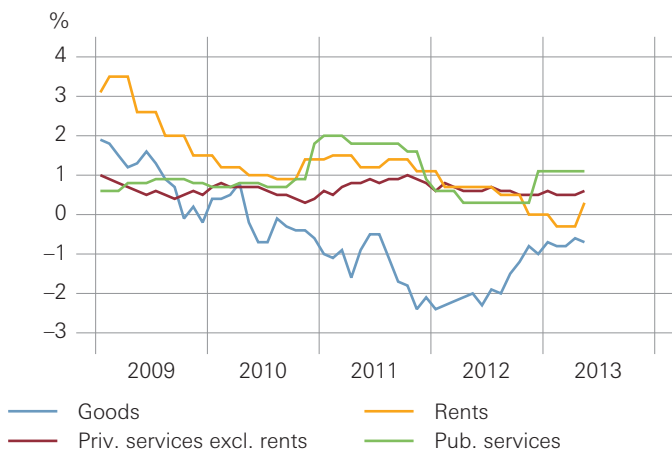


Sources: SFSO, SNB

Chart 4.2

CPI: DOMESTIC GOODS AND SERVICES

Year-on-year change

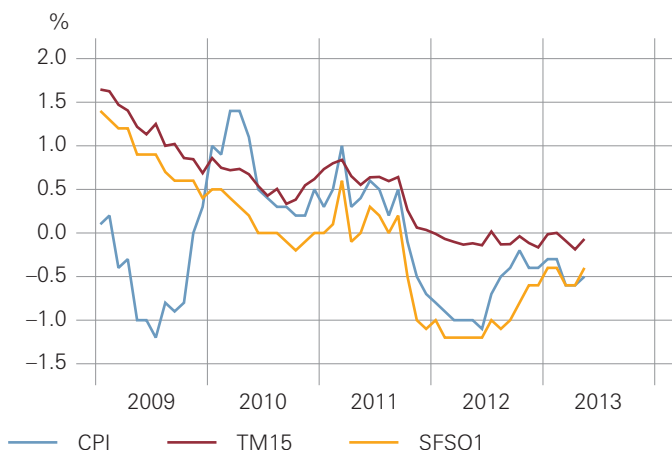


Sources: SFSO, SNB

Chart 4.3

CORE INFLATION RATES

Year-on-year change



Sources: SFSO, SNB

Slightly higher rental prices

Annual inflation for domestic CPI components increased slightly in May, due especially to developments in rents surveyed on a quarterly basis. These were slightly higher in May than in February, putting annual rent inflation, which between February and April had been negative for the first time since 1998, back into positive territory. Inflation rates for other domestic goods and services remained largely unchanged in the first few months of the current year (cf. chart 4.2).

Core inflation remains low

Core inflation rates depicted in chart 4.3 show a historically low inflationary trend that has remained stable over the past few months. In May, the trimmed mean calculated by the SNB (TM15) and the SFSO's core inflation rate 1 (SFSO1) amounted to -0.1% and -0.4%, respectively.

TM15 and SFSO1 are calculated on the basis of a reduced CPI basket of goods. The difference between the two lies in the method applied to achieve this reduction. TM15 excludes the CPI goods with the highest price change rates every month (15% at either end of the distribution curve), whereas SFSO1 excludes the same CPI products every month (fresh and seasonal products, energy and fuel).

PRODUCER AND IMPORT PRICES

Stable supply prices

The index of producer and import prices in May was at virtually the same level as one year before (-0.2%). In January, by contrast, the year-on-year comparison had shown an increase (0.8%).

Measured against annual inflation rates, the advance in producer prices has slowed down since January, whereas the decline in import prices has become steeper (cf. chart 4.4). However, this development primarily reflects statistical base effects. Over the past months, producer and import prices have remained largely stable compared to the previous quarter, suggesting that there is currently little inflationary or deflationary pressure on downstream consumer prices.

REAL ESTATE PRICES

Further increase in residential property prices

Prices for owner-occupied apartments have risen sharply over the past few years. This development continued in the first quarter. Indices published by Wüest & Partner, IAZI and Fahrländer Partner confirm that transaction prices are continuing to climb (cf. chart 4.5). The asking prices of owner-occupied apartments advertised in the media, too, have again increased significantly.

This also applies to single-family homes, albeit to a somewhat lesser extent than in the case of owner-occupied apartments. All available indices show a further rise as against the previous quarter, although with some differences regarding momentum. Whereas Fahrländer Partner's index of single-family home prices suggests a stronger-than-average advance compared to the last few quarters, both other transaction price indices (IAZI, Wüest & Partner) imply a more moderate increase.

Existing rents virtually unchanged – unlike asking rents

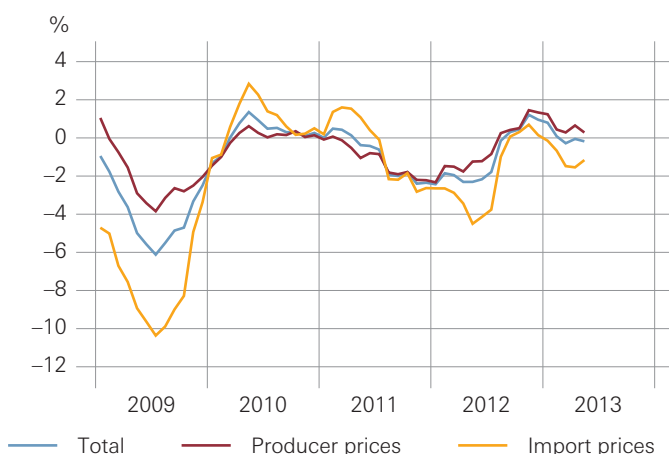
Rents for apartments offered on the market (asking rents) continued to rise in the first quarter. According to Wüest & Partner, annual inflation in the case of asking rents is, at 2.1%, still significantly higher than in the case of rents under existing contracts (existing rents). The rental component of the CPI, which is dominated by existing rents, remained virtually unchanged year-on-year (cf. chart 4.6).

Rents for existing contracts are tied by law to the reference interest rate, which has been steadily reduced in recent years and currently stands at 2.25%. The latest reduction in the reference interest rate was made in June 2012.

Chart 4.4

PRODUCER AND IMPORT PRICES

Year-on-year change

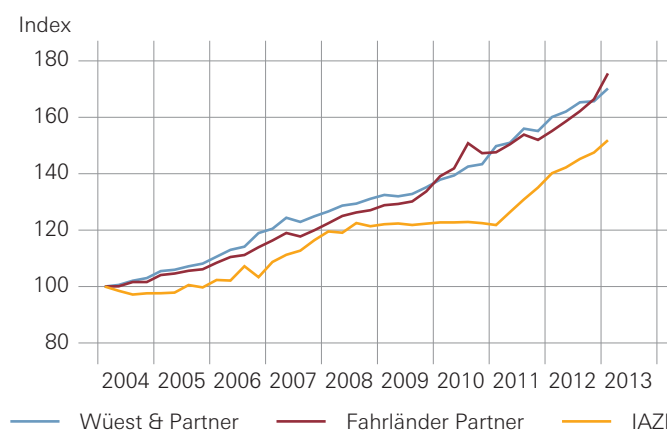


Source: SFSO

Chart 4.5

TRANSACTION PRICES, OWNER-OCCUPIED APARTMENTS

Beginning of period = 100, nominal (hedonic)



Sources: Fahrländer Partner, IAZI, Wüest & Partner

INFLATION EXPECTATIONS

Short-term inflation expectations remain low

Short-term inflation expectations recorded by surveys remain unchanged at a low level. Medium-term inflation expectations are somewhat higher, but are still within a range that is consistent with the SNB's definition of price stability.

The quarterly survey conducted by SECO shows that, in April, 46% of the households surveyed expect prices to remain unchanged, as against 39% that anticipate a slight decline in prices over the next twelve months. The proportion of respondents expecting either a fall or a strong increase in prices remains low (cf. chart 4.7).

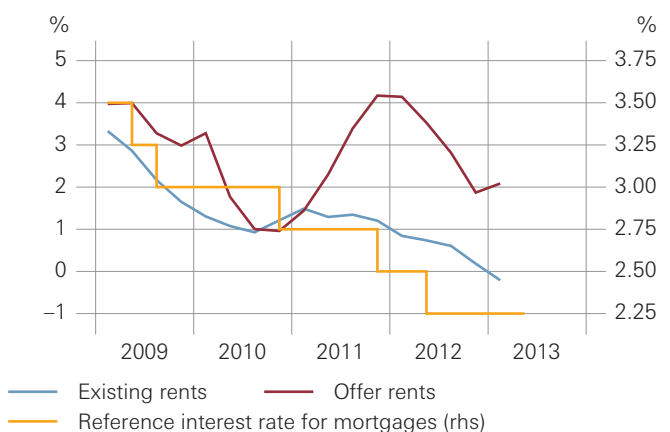
According to the *Credit Suisse ZEW Financial Market Report*, a large majority of financial analysts surveyed in May (78%) predicted that annual inflation rates would stay unchanged at a low level for the next six months. This majority has grown larger over the past few months, whereas the share of those expecting rising inflation rates has diminished. The number of survey participants anticipating declining inflation rates remains very low.

Talks held by the SNB delegates for regional economic relations with companies from all regions of Switzerland, as well as the survey conducted by Deloitte among CFOs and heads of finance at companies based in Switzerland, provide information on quantitative inflation expectations. The talks held by SNB delegates in the second quarter indicate that inflation expectations over a six to twelve-month horizon stand at 0.2%, as in the previous quarter. However, the survey by Deloitte in the first quarter showed that inflation was expected to amount to 1.4% in two years, which is slightly higher than the values obtained in the third and fourth quarter surveys of 2012.

Chart 4.6

APARTMENT RENTS AND REFERENCE INTEREST RATE

Nominal, year-on-year change (lhs)

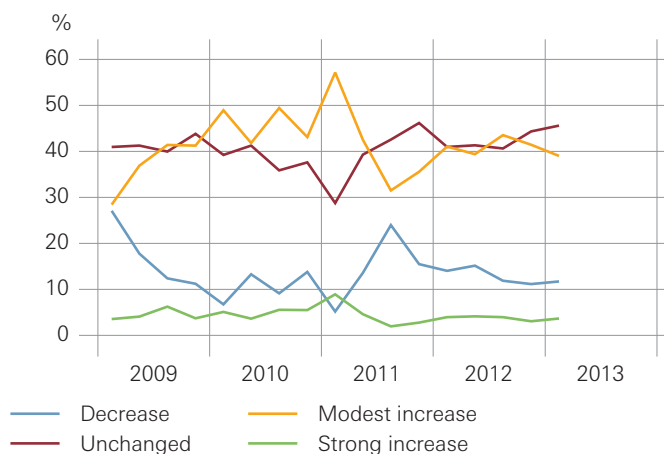


Sources: Federal Office for Housing (FOH), SFSO, Wüest & Partner

Chart 4.7

PRICE EXPECTATIONS

Survey on expected movements in prices for coming 12 months



Sources: SECO, SNB

5

Monetary developments

In recent weeks, volatility in financial markets has again increased. Recent developments suggest that safe-haven considerations continue to play an important role in the demand for Swiss francs. Overall, the value of the Swiss franc remains high and should fall further over the next few quarters.

The level of interest rates in Switzerland remained very low in the first quarter. On the secured Swiss franc money market, interest rates are in negative territory. Yields at issue for Confederation money market debt register claims also continue to be negative. By contrast, yields on ten-year Confederation bonds have risen slightly from the lows reached last December. Movements in long-term interest rates show that demand for secure investments reacts strongly to the international environment.

Banks' sight deposits at the SNB have not increased any further since September 2012. However, growth in the M1, M2 and M3 monetary aggregates, which measure the amount of money held by households and companies, remained strong. This growth in money was accompanied by robust lending on the part of banks. Although the rate of growth in mortgage loans to households has declined since mid-2012, it is still at a high level. Most recently, mortgage lending to companies, in particular in residential construction, has increased significantly.

Overall, lending has been growing faster than nominal GDP for several years. In addition, residential property prices have risen strongly in the past few years. Given the sustained period of exceptionally low interest rates, there is a risk that the imbalances on the mortgage and real estate markets will increase further. This development poses a threat to financial stability and, in the event of an abrupt correction, can have wide-reaching consequences for the real economy.

SUMMARY OF MONETARY POLICY SINCE THE LAST ASSESSMENT

Continuation of monetary policy announced in September 2011

In the past quarter, the SNB maintained unchanged 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% in August of the same year.

Sight deposits at SNB stable

Since the March monetary policy assessment, total sight deposits held at the SNB have remained largely unchanged. In the week ending 14 June 2013 (last calendar week before the mid-June assessment), sight deposits totalled CHF 370.7 billion, compared to CHF 370.5 billion in the last calendar week before the mid-March assessment. Between the assessments in mid-March and mid-June, they averaged CHF 371.1 billion. Of this amount, CHF 280.4 billion was accounted for by the sight deposits of domestic banks and the remaining CHF 90.7 billion by other sight deposits.

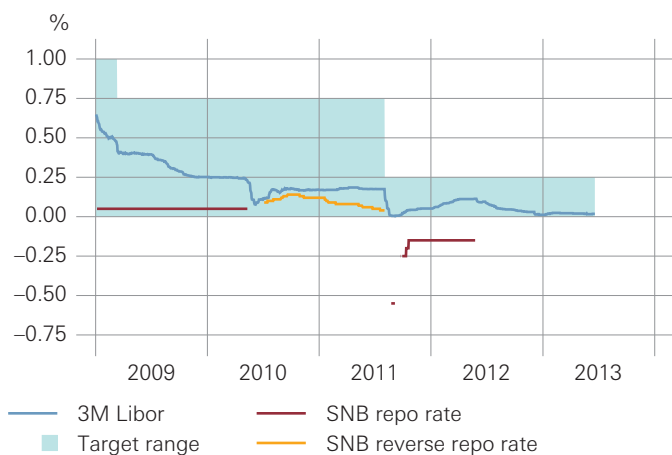
Banks' surplus reserves remain high

Statutory minimum reserves averaged CHF 13.5 billion between 20 February and 19 May 2013. They were thus unchanged from the preceding period (20 November 2012 to 19 February 2013). On average, banks exceeded the requirement by around CHF 274.9 billion (previous period: CHF 279.8 billion). Thus, banks' surplus reserves continue to be exceptionally high.

Chart 5.1

MONEY MARKET RATES

Daily figures

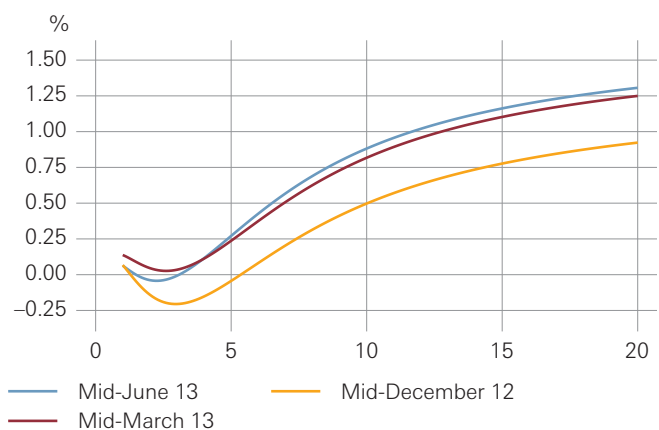


Sources: Bloomberg, Reuters, SNB

Chart 5.2

TERM STRUCTURE OF SWISS CONFEDERATION BONDS

After Nelson-Siegel-Svensson. Years to maturity (hor. axis)



Source: SNB

Chart 5.3

ESTIMATED REAL INTEREST RATE

10-year Confederation bonds
Inflation expectations estimated with VAR model



Source: SNB

MONEY AND CAPITAL MARKET INTEREST RATES

Money market rates remain low

Activity on the money market has remained low in the period since the March assessment. The high level of liquidity supply is reflected in money market interest rates, which also remain low (cf. chart 5.1). Thus the three-month Libor was just under 2 basis points in mid-June. Interest rates in the secured money market and issuing yields for money market debt register claims of the Swiss Confederation continued to be negative.

In March and April, the mood on the financial markets was dominated by the problems facing banks in Cyprus. Prevailing uncertainty led to an increase in demand for government bonds seen as being secure, for instance Swiss Confederation bonds. The yields on Confederation bonds therefore temporarily fell from 0.8% to 0.6%.

In the course of the second quarter, speculation about normalisation of monetary policy in the US contributed to the recovery of yields on long-term government bonds. As a result of this development, Confederation bond yields also rose slightly. In mid-June, the yield on ten-year Swiss Confederation bonds was around 0.9%, and as such, still at a historically low level.

Yield curve marginally steeper

As long-term interest rates in June are slightly higher than they were in March, the yield curve of Confederation bonds illustrated in chart 5.2 is somewhat steeper than it was three months ago. The spread between the yield on ten-year Confederation bonds and that on the three-month Libor stood at 0.9 percentage points in mid-June, or 0.1 percentage points more than in mid-March.

Real interest rates almost unchanged

Since the previous quarter, estimated ten-year real interest rates have remained almost unchanged and are still at the low level of barely 0.3% (cf. chart 5.3).

The real interest rates shown 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.

EXCHANGE RATES

Swiss franc temporarily weaker against euro and US dollar

The demand for Swiss francs on the foreign exchange market continues to be strongly influenced by the international environment. The Swiss franc weakened during May as financial markets' confidence in the euro area began to grow again after a provisional end to the Cyprus crisis. This was compounded by speculation about a possible reduction in securities purchases by the Federal Reserve. At the end of May and the beginning of June, however, the Swiss franc regained the ground lost during the depreciation against the euro and the US dollar (cf. chart 5.4). The Swiss franc continued to rise against the yen, which lost value against all major currencies in April.

The result of these movements was that the export-weighted nominal external value of the Swiss franc was slightly greater in mid-June compared to the time of the quarterly assessment in March.

Slightly tighter monetary conditions

As short-term interest rates have remained almost constant, any changes to monetary conditions are determined at present almost solely by exchange rate movements. In mid-June, the monetary conditions were thus slightly tighter than at the time of the monetary policy assessment in March. The Monetary Conditions Index (MCI) illustrated in chart 5.5 shows that monetary conditions eased slightly in the interim period. According to the MCI, the temporary weakening of the Swiss franc in May corresponded to an interest rate reduction of 20 to 40 basis points.

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

Real external value of Swiss franc still at high level

The real export-weighted external value of the Swiss franc was slightly lower in May than in the previous months. However, this value is still well above the long-term average (cf. chart 5.6).

Chart 5.4

EXCHANGE RATES

Daily figures

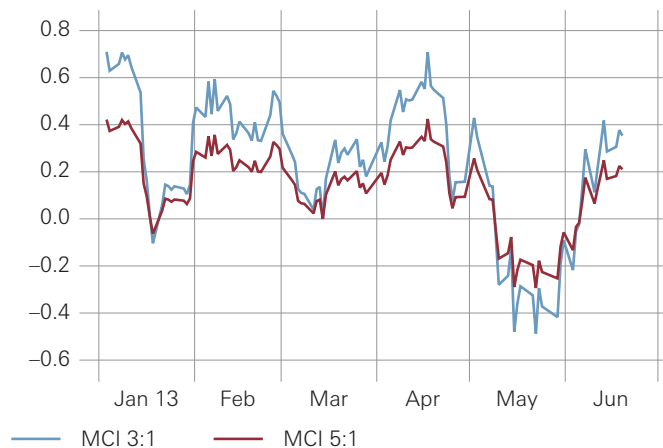


Source: SNB

Chart 5.5

MCI NOMINAL

Daily figures



Source: SNB

Chart 5.6

EXTERNAL VALUE OF SWISS FRANC

Export-weighted, January 1999 = 100



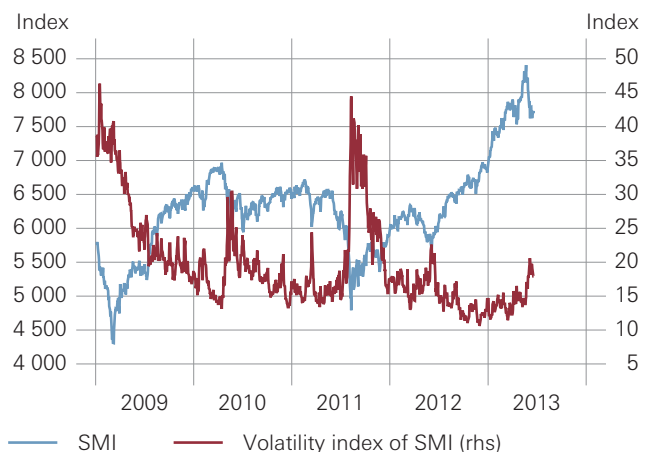
In real terms (24 countries)

Source: SNB

Chart 5.7

SHARE PRICES AND VOLATILITY

Daily figures

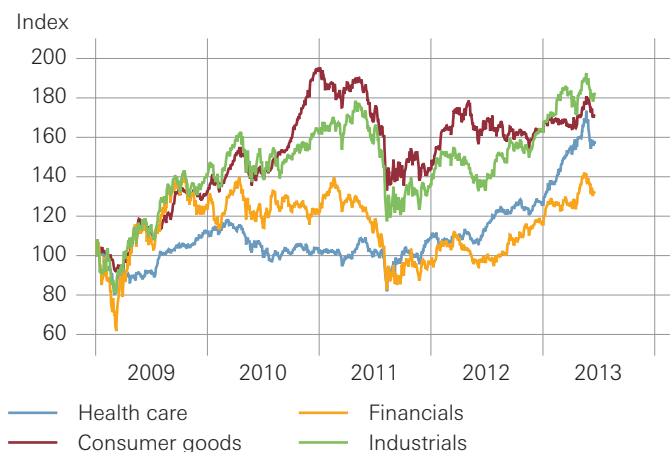


Source: Thomson Financial Datastream

Chart 5.8

SELECTED SPI SECTORS

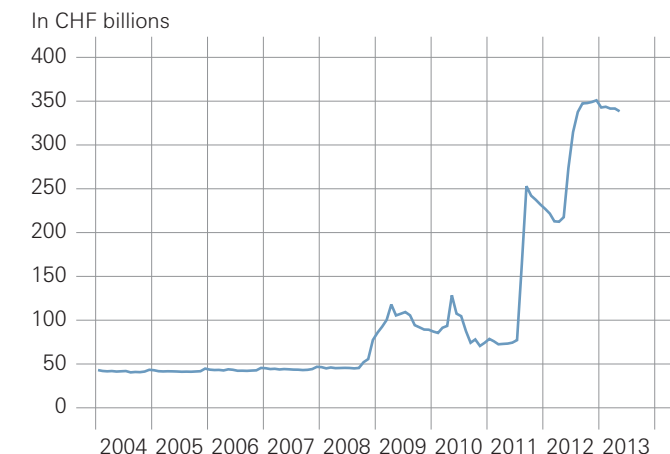
Beginning of period = 100, daily figures



Source: Thomson Financial Datastream

Chart 5.9

MONETARY BASE



Source: SNB

STOCK MARKETS

Correction on stock market

Developments on the Swiss stock market were similar to most foreign stock market indices. Amid growing uncertainty about the continuation of expansionary monetary policy around the world, prices decreased in mid-May. Uncertainty regarding the impact of the banking crisis in Cyprus had already led to a temporary decline in prices during March and April.

In mid-June, the Swiss Market Index (SMI) was down around 8% on the annual peak it recorded in May. The uncertainty on the stock market, as measured by the index of the 30-day expected volatility of the SMI, increased slightly in the same period. Despite the correction on the stock market, the SMI remains above the level recorded at the beginning of the year (cf. chart 5.7).

The breakdown of the Swiss Performance Index shows all important sectors to have suffered price losses in recent weeks. Share prices in healthcare have recorded the best performance since the beginning of the year (cf. chart 5.8).

MONETARY AND CREDIT AGGREGATES

Robust monetary transmission

Transmission of monetary policy by the banking sector has remained strong in recent months. Although the monetary base, which comprises banknotes in circulation plus domestic banks' sight deposits with the SNB, has stabilised since September 2012 (cf. chart 5.9), commercial banks continued to generate new loans and deposits.

Further increase in broad monetary aggregates

The monetary aggregates, which measure the amount of money held by households and companies, continued to grow substantially (cf. chart 5.10). In May, the M1 monetary aggregate (notes and coins in circulation, sight deposits and transaction accounts) exceeded the previous year's level by 12.2%. In the same period, M2 (M1 plus savings deposits) and M3 (M2 plus time deposits) grew by 10.5% and 9.7% respectively (cf. table 5.1).

The strong growth in these monetary aggregates mainly reflects credit and deposit generation in the banking sector, which has been boosted by the low interest rates. Households and companies are deciding to finance new acquisitions with loans. The money and credit supply continues to expand, although interest rates are not declining any further.

The growth of the monetary and credit aggregates shows that the transmission of monetary stimuli to the economy is working well, which is partially offsetting the negative impact of global economic activity on aggregate demand in Switzerland.

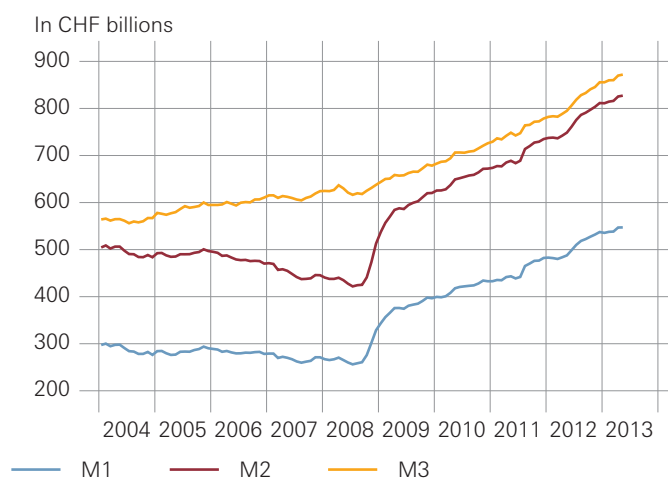
Strong credit growth continues

In the first quarter of 2013, growth in bank loans declined slightly. The annual growth rate was down from 4.0% in the fourth quarter of 2012 to 3.8% in the first quarter of 2013. This slight slowdown in credit growth is attributable to other loans, i.e. those not secured by mortgages (cf. table 5.1).

The volume of other loans has shown a flat path since the beginning of the financial and economic crisis. Since other loans are usually highly cyclical, this development is in line with a subdued level of economic activity. The breakdown of other loans into secured and unsecured loans shows a slight rise in secured loans since 2009, while unsecured loans have seen a slight decrease (cf. chart 5.11).

Chart 5.10

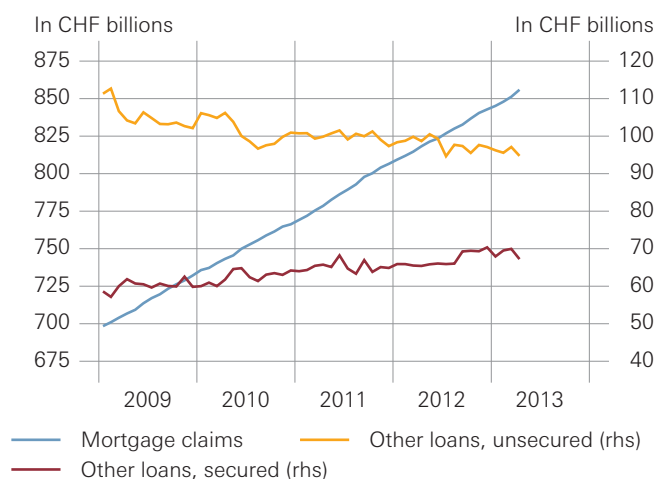
MONETARY AGGREGATES



Source: SNB

Chart 5.11

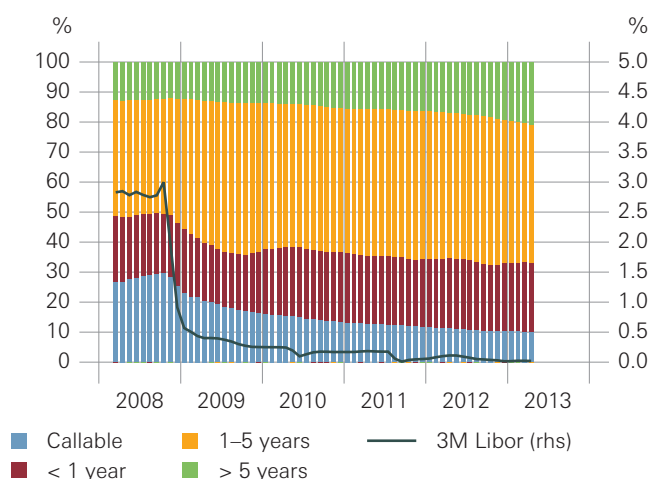
MORTGAGE CLAIMS AND OTHER LOANS



Source: SNB

Chart 5.12

BREAKDOWN OF MORTGAGES BY RESIDUAL TERM



Source: SNB

As in the previous quarter, mortgage claims, which account for four-fifths of all bank lending, were up 4.5% year-on-year. The low level of interest rates also supported the continued strong growth of mortgage lending.

When interest rates are low, long-term, fixed-rate mortgages tend to be preferred to those with variable interest rates. As shown in chart 5.12, mortgages with an early repayment option, which generally tend to be variable-rate mortgages, still accounted for 30% of all mortgage claims in October 2008. By April 2013, this share had fallen to below 10%. In turn, the proportion of mortgages with a residual term of over five years increased from 13% to 21%.

Countercyclical capital buffer activated

On 13 February 2013, for the first time, the Federal Council made use of the possibility foreseen in the Capital Adequacy Ordinance and activated the countercyclical capital buffer (CCB) on the proposal of the SNB. The CCB is to be held from 30 September 2013 and applies in addition to other capital requirements for banks. It is targeted at residential mortgage loans and amounts to 1% of the relevant risk-weighted positions.

The SNB hopes that the activation of the CCB will, first and foremost, improve the banking sector's resilience. Moreover, the idea of the CCB is to help counter a further build-up of imbalances on the mortgage and real estate markets, by making it less attractive for banks to grant residential mortgage loans compared to other forms of lending.

Table 5.1

MONETARY AGGREGATES AND BANK LOANS

Year-on-year change in percent

	2012	2012			2013	2013		
		Q2	Q3	Q4	Q1	March	April	May
M1	11.5	11.1	12.6	11.3	11.5	12.1	13.1	12.2
M2	9.9	9.5	10.8	10.1	10.4	10.8	11.2	10.5
M3	8.0	7.0	8.9	9.4	9.7	9.9	10.3	9.7
Bank loans total ^{1, 3}	4.0	3.9	3.7	4.0	3.8	3.9	3.6	
Mortgage claims ^{1, 3}	4.8	4.9	4.6	4.5	4.5	4.5	4.6	
Households ^{2, 3}	4.9	5.0	4.8	4.5	4.2	4.1	4.2	
Private companies ^{2, 3}	4.9	5.0	4.4	4.9	5.5	5.9	6.1	
Other loans ^{1, 3}	-0.1	-1.1	-0.8	1.6	0.4	1.0	-1.3	
Secured ^{1, 3}	3.0	-0.9	3.2	7.9	5.1	6.8	2.8	
Unsecured ^{1, 3}	-2.1	-1.2	-3.3	-2.5	-2.7	-2.7	-4.0	

1 Monthly balance sheets.

2 Credit volume statistics.

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

Source: SNB

Business cycle trends

SNB regional network

Report for the attention of the Governing Board of the Swiss National Bank for its quarterly assessment of June 2013

Second quarter of 2013

The Swiss National Bank's delegates for regional economic relations are constantly in touch with companies from different areas of the economy. This report is based on discussions conducted in April and May 2013 with 241 managers and entrepreneurs on the current and future situation of their companies and on the economy in general. The selection of companies differs from one quarter to the next. It reflects the industrial structure of the Swiss economy, based on the breakdown of GDP (excluding agriculture and public services).

Regions

Central Switzerland
Eastern Switzerland
Geneva
Italian-speaking Switzerland
Mittelland
Northwestern Switzerland
Vaud-Valais
Zurich

Delegates

Walter Näf
Jean-Pierre Jetzer
Jean-Marc Falter
Fabio Bossi
Martin Wyss
Daniel Hanimann
Aline Chabloz
Markus Zimmerli

SUMMARY

According to this survey, the Swiss economy continued growing at a moderate pace in the second quarter of 2013. The main growth drivers were construction and the services sector. In manufacturing, the level of business activity remained modest.

Exporters benefited from an upturn in demand from the US. The relatively buoyant domestic economy also acted as a stimulus. By contrast, demand from within Europe was still lacking. The importance of the minimum exchange rate against the euro was once again stressed by many respondents.

Margins in manufacturing and in the services sector remained below average. In construction, high demand led to a significant improvement in margins. Moreover, the large number of streamlining measures effected recently are having a beneficial impact. Overall, demand for labour remained unchanged from the previous quarter.

The outlook for real growth in turnover over the next few months remains cautiously optimistic in all sectors. The demand for staff is likely to increase slightly.

Latent uncertainty about developments in Europe remains, but is no longer so marked. In addition, companies find that various political initiatives in Switzerland are adding a slight element of uncertainty.

BUSINESS ACTIVITY

Manufacturing: Slight improvement

Manufacturing has seen only a slight improvement in business activity since the last survey. Over one-third of the companies surveyed posted higher sales than in the previous quarter, while turnover was static at almost half the companies.

An upturn in business was reported by the food industry, plastics manufacturing and producers of electrical equipment and precision instruments. The chemical industry reported slightly lower turnover than in the previous period. Business activity remained flat in the textiles and watchmaking industries as well as in mechanical engineering.

Exporters continued to be seriously affected by the recession in southern Europe. Demand from the rest of Europe was also subdued. However, demand stimuli emanated from Asia, the US (where business activity was noticeably stronger in places) and Russia, as well as from the domestic economy.

Construction: Business still brisk

In real terms, turnover in construction rose significantly compared with the previous quarter, and was also much higher than a year ago. Although weather conditions were less than ideal, business was buoyed up by a backlog of demand from the previous quarters. About half the companies surveyed reported a quarter-on-quarter rise in seasonally adjusted turnover, while one-third stated that turnover was unchanged from the previous quarter.

The momentum of business activities in the finishing trade was very lively. Structural and civil engineering also reported turnover well in excess of the previous and year-back periods. Whereas residential construction remained brisk, commercial and industrial construction activity was modest.

A number of respondents referred to real estate risks. Price reductions in the luxury residential segments – already mentioned in previous surveys – were also confirmed. Banks' lending policies were not judged to be a limiting factor.

Services: Moderate but broader-based growth

The services sector continued to report moderate growth. This sector's situation has improved further since the previous survey, and progress is broader-based in terms of industries. Just under half the companies stated that their sales were as high as or higher than in the previous quarter.

Companies in the following industries reported a good level of business momentum: hospitality, IT, real estate, auditing, and staff recruitment. Retailers and car dealers recorded a further upturn in business activity. Although business volumes in border regions continue to be impacted by cross-border shopping, this trend has stabilised.

Banks and insurance companies reported a rather flat business trend compared with the previous quarter. Various industries stated that banks' economy drives are continuing to affect business. The shake-up in the banking industry has not yet run its course.

Hospitality reported a noticeable upturn in business after stagnation in the previous quarter. It has become highly volatile, however, with bookings coming in at very short notice. Resorts in mountainous regions that are highly dependent on day trippers were badly hit by the unusually adverse weather conditions.

CAPACITY UTILISATION

On balance, utilisation of production capacity and infrastructure was again judged to be normal. Construction was the only industry to report higher capacity utilisation than in the previous quarter. In many cases, this was due to a backlog of work that had built up owing to bad weather. Within the industries, however, capacity utilisation remained rather uneven.

Companies in the manufacturing industry rated their overall capacity utilisation as normal. As in the previous quarter, vehicle manufacturers and producers of electrical equipment reported rather high levels of capacity utilisation. The metals processing industry indicated a further improvement in workload compared to the previous quarter. In the chemical industry, however, capacity utilisation deteriorated and was much lower than usual. It also remained low in the machine industry. Companies in the food industry and in plastics manufacturing reported normal levels of capacity utilisation.

In construction, technical capacity utilisation was generally higher than is usual for this time of year. This applied not only to companies in structural and civil engineering, but also to those in the finishing trade. In many cases, order books are already full for the rest of the year.

In the services sector, utilisation of infrastructure (i.e. primarily office and retail space) was reported to be at a normal level. Providers of building management services and IT firms continue to report rather high capacity utilisation. This was also the case in the wholesale trade. Hotels and recruitment agencies were again beset by low utilisation levels, whereas the automotive industry, restaurants, and architectural and engineering firms reported normal levels of capacity utilisation.

DEMAND FOR LABOUR

Little change in demand for staff

As in previous quarters, overall demand for labour remained virtually unchanged. Very little mention was made of any specific changes in staffing policy. Various measures such as longer working hours for the same salary had already been rescinded as of the start of the year. However, there were still marked differences between the different industries in terms of their assessment of appropriate staffing levels.

The manufacturing companies surveyed felt that their headcounts had still been slightly too high in the preceding quarter, but that these now corresponded almost exactly to requirements. Manufacturers of precision instruments and electrical equipment considered their headcounts to be on the low side. Companies in the food industry, mechanical engineering and plastics manufacturing industries stated that headcounts were more or less in line with requirements, whereas metals processing firms, furniture makers, processors of paper and cardboard products, and printing companies considered themselves somewhat overstaffed.

The construction industry indicated that its headcounts were generally rather low. Staff numbers were seen as slightly low in the finishing industry, in particular, but were rated as roughly in line with requirements in structural and civil engineering.

In the services sector, staff levels were considered appropriate overall. IT companies, in particular, again stated that staff levels were somewhat low and that the need to recruit was fairly acute. Fiduciary companies, consultancies and auditors also indicated recruitment needs. Banks and some retailers again stated that their headcounts were slightly too high.

Increase in spontaneous job applications

Overall, the companies surveyed considered the process of recruiting staff to be more or less as challenging and time-consuming as ever. In many cases, the required personnel can only be found abroad. A number of respondents mentioned a pronounced rise in spontaneous job applications, especially from southern Europe. A significantly larger number of applicants are responding to recruitment advertisements. However, their profiles often fail to meet the requirements of companies.

Companies in the metals and food industries as well as in banking and hospitality were finding the recruitment process somewhat easier than usual. By contrast, recruitment was perceived as more difficult than usual by architectural and engineering firms. As before, the construction industry is finding it difficult to hire site foremen and machine technicians.

PRICES, MARGINS AND EARNINGS SITUATION

Margins slightly lower than usual

Margins are still lower than usual overall. In construction, the assessment has changed for the better. By contrast, margins in manufacturing and in the services sector are still rated as somewhat narrower than usual. Companies are continuing to focus on optimising costs and raising efficiency. New markets, products and customer segments, as well as isolated price rises, are helping to boost margins – as is the addition of new 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 or so months.

In manufacturing, profit margins in many areas are lower than usual. This applies, in particular, to the metals processing and machine industries and to wood, paper and plastics processing firms. The chemical industry and furniture manufacturers are also reporting lower-than-average margins. By contrast, margins are relatively good at pharmaceutical companies. The exchange rate problem still poses a challenge for some manufacturing firms. These companies expect purchase prices to remain stable in the coming months while sale prices recede, thus keeping up the downward pressure on prices.

In construction, the companies surveyed reported above-average margins in all subsectors – structural and civil engineering, and finishing – owing to buoyant demand. Moreover, as it anticipates a slight fall in the cost of construction materials in the next few months while construction prices remain stable, margins should improve still further.

In the services sector, most industries were again confronted with unusually low margins. The worst-affected areas were once again hospitality and banking. Recruitment agencies complained of below-average margins – as did building management companies, which reported that competition had become significantly fiercer. Retailers stated that their margin situation had largely returned to normal. The margin situation was also rated as normal by IT and transport enterprises as well as by fiduciary companies and law firms. Insurers reported margins above the long-term average, owing in part to the favourable development of claims. A slight improvement in margins is expected in hospitality in particular, as purchase and sale prices are expected to move in a positive direction over the next few months.

OUTLOOK: GUARDED OPTIMISM

Uncertainty about future developments has hardly changed since the last survey. In terms of international risks, companies are still concerned about the possibility of a renewed flare-up in the European debt crisis. The subdued economic outlook for Europe is also causing a degree of uncertainty, whereas respondents remain confident about developments in demand from other parts of the world and in Switzerland. A relatively large number of companies surveyed mentioned the numerous political initiatives within Switzerland and the increasingly complex regulatory environment, coupled with the international tax debate, as adding a slight degree of uncertainty to future business conditions.

Overall, companies in all three sectors expect turnover to rise in the next six months. Corporate recruitment plans envisage a slight increase in headcounts over this time horizon. For seasonal reasons, the construction industry is predicting the largest rise.

In manufacturing, companies remain confident about their business outlook: representatives from almost all industries are anticipating slight rises in turnover over the next six months.

In construction, seasonally adjusted turnover should continue to rise slightly over the next few months, as should capacity utilisation. This industry remains optimistic overall: it is not expecting a significant downturn in the current year.

Services sector companies surveyed are also generally upbeat about their business outlook for the next six months. As in the previous quarter, no industry is forecasting a downturn in turnover within this time horizon, and only banks are expecting flat growth. The outlook in retailing and IT has improved further. Both capacity utilisation and headcounts can be expected to rise slightly again in the services sector over the next few months. Companies' investment plans in all three sectors for the year ahead suggest that these expenditures will increase only very slightly.

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.

<p>At its quarterly assessment of 20 June 2013, the SNB reaffirms that it will maintain the minimum exchange rate of CHF 1.20 per euro. In the view of the SNB, the Swiss franc is still high. The minimum exchange rate remains important in order to avoid an undesirable tightening of monetary conditions in the event of sudden upward pressure on the Swiss franc. The SNB continues to stand ready to enforce the minimum exchange rate, if necessary, by buying foreign currency in unlimited quantities, and to take further measures as required. The target range for the three-month Libor remains unchanged at 0.0–0.25%.</p>	<p>June 2013</p>
<p>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.</p>	<p>March 2013</p>
<p>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.</p>	<p>February 2013</p>
<p>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.</p>	<p>December 2012</p>
<p>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.</p>	<p>September 2012</p>
<p>On 25 June 2012, the SNB concludes a Swiss franc/zloty swap agreement with the National Bank of Poland. 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.</p>	<p>June 2012</p>
<p>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%.</p>	

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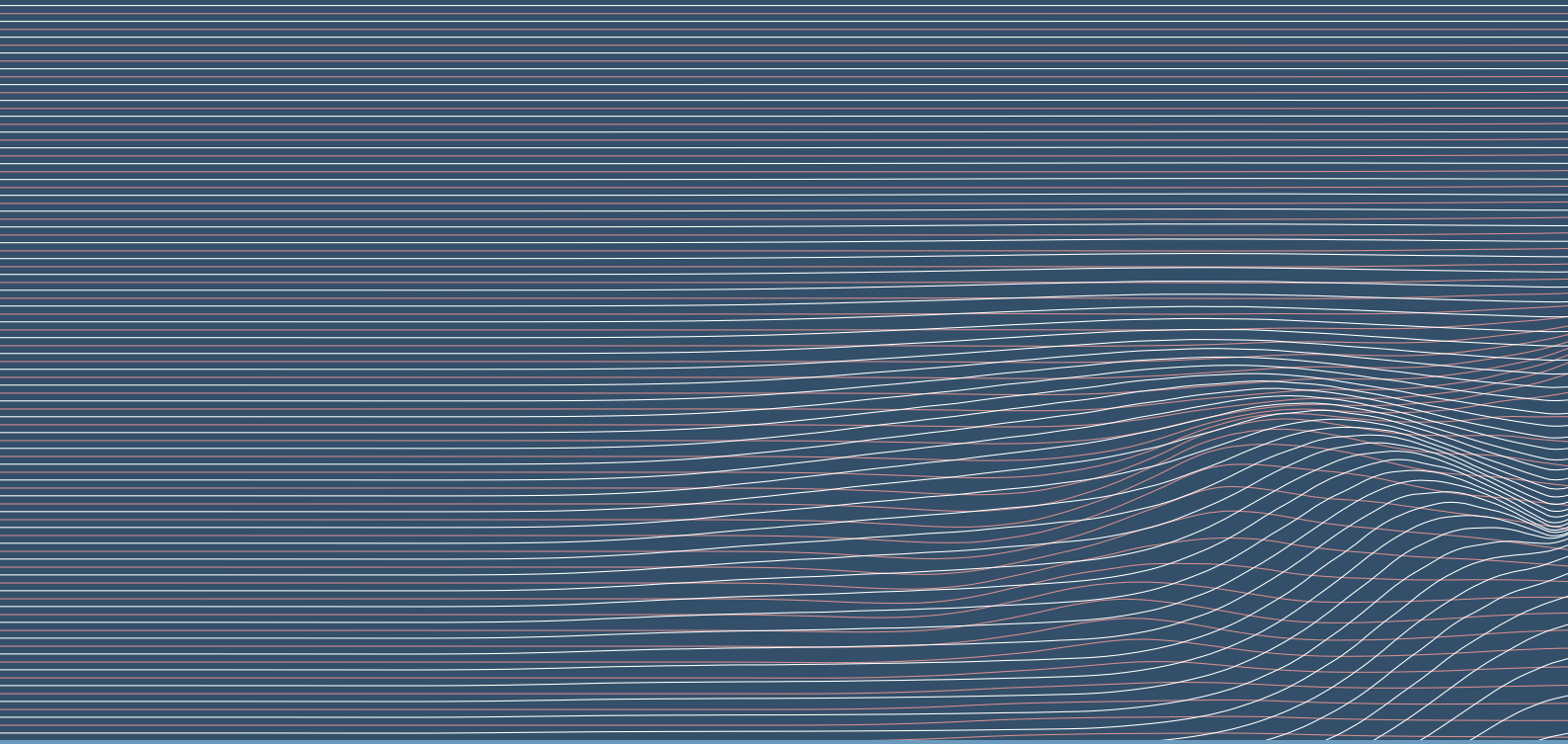
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