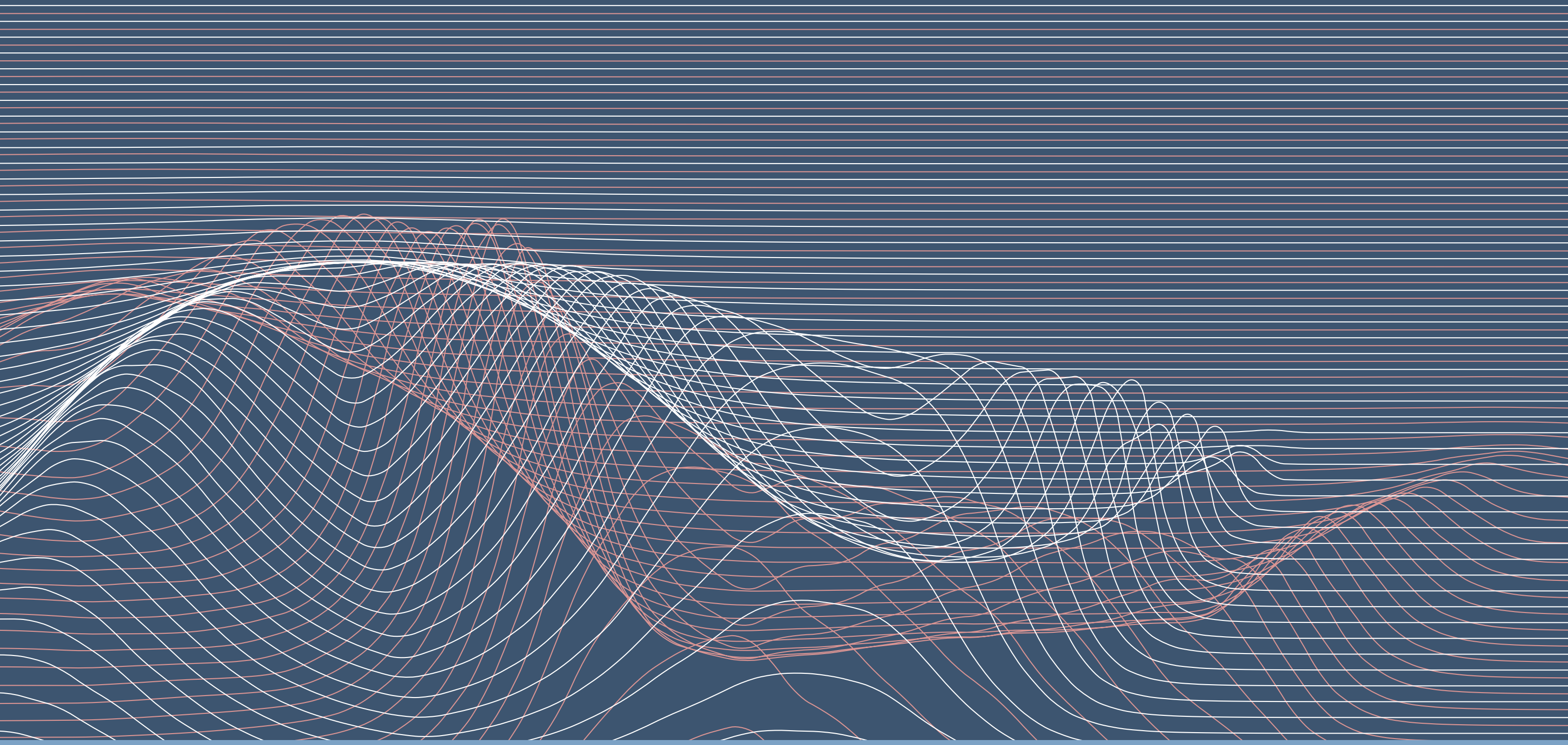

Quarterly Bulletin
3/2015 September

SCHWEIZERISCHE NATIONALBANK
BANQUE NATIONALE SUISSE
BANCA NAZIONALE SVIZZERA
BANCA NAZIUNALA SVIZRA
SWISS NATIONAL BANK

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3/2015 September

Volume 33

SNB BNS

Contents

Monetary policy report

Report for the attention of the Governing Board of the Swiss National Bank for its quarterly assessment of September 2015

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 17 September 2015') is an excerpt from the press release published following the assessment.

This report is based on the data and information available as at 17 September 2015. 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 17 September 2015

Swiss National Bank leaves monetary policy unchanged
The Swiss National Bank (SNB) is leaving the target range for the three-month Libor unchanged at between –1.25% and –0.25%. The interest rate on sight deposits with the SNB remains at –0.75%. Furthermore, the SNB will remain active in the foreign exchange market as necessary, in order to take account of the impact of the exchange rate situation on inflation and economic developments. Overall, the Swiss franc is still significantly overvalued, despite a slight depreciation. The negative interest rates in Switzerland and the SNB's willingness to intervene as required in the foreign exchange market make investments in Swiss francs less attractive; both of these factors serve to ease the pressure on the franc.

Overall, the new conditional inflation forecast differs very little from that in the June assessment (cf. chart 1.1). Owing primarily to the drop in oil prices, the forecast for the short term is somewhat lower than that presented in the previous quarter. For the current year, the forecast decreases by 0.2 percentage points to –1.2%; for 2016, it drops from –0.4% to –0.5%. The SNB continues to expect inflation to move back into positive territory at the beginning of 2017. Averaged over the year, the conditional inflation forecast for 2017 increases by 0.1 percentage points to 0.4% (cf. table 1.1). The forecast assumes that the three-month Libor will remain at –0.75% over the entire forecast horizon and that the Swiss franc will weaken further.

Global economic growth continued in the second quarter in line with the SNB's expectations. In the advanced economies, growth was slightly more positive than in the first quarter; this was mainly attributable to the economic recovery in the US. The muted recovery in the euro area continued, due partly to the favourable exchange rate situation. Internationally, however, growth was not broad-based. This was reflected, for instance, in the lack of momentum in global trade and in low commodity prices.

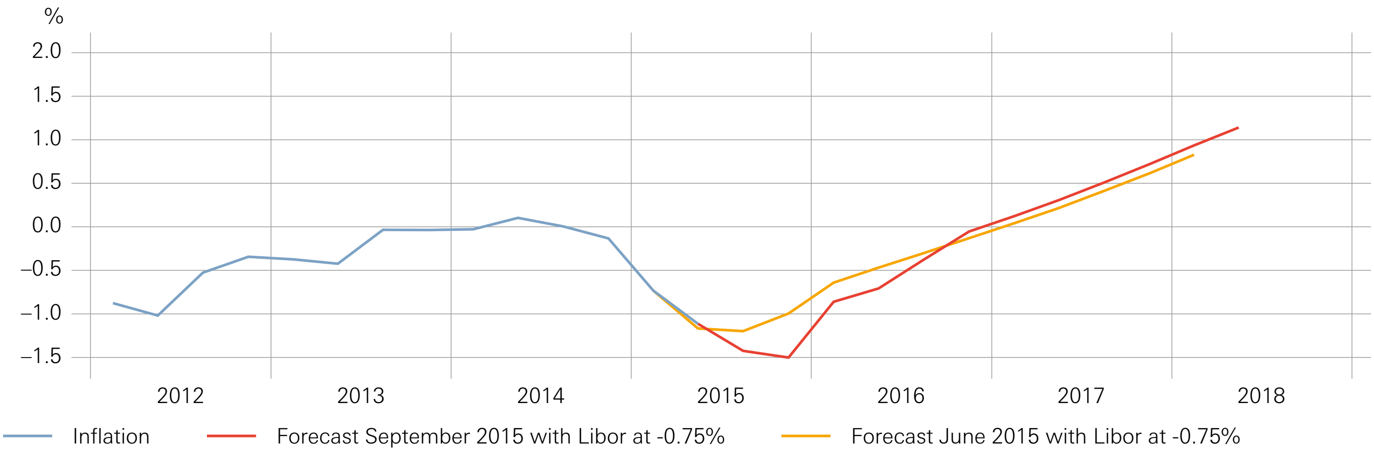
The SNB expects the moderate pace of global economic recovery to continue. In the advanced economies, the recovery is likely to be underpinned by monetary policies which are still very expansionary, as well as favourable energy prices. Consequently, underutilisation of production capacity should decrease further in these countries. In a number of the major emerging economies, however, activity remains weak.

The global economic recovery is fraught with risks. In particular, uncertainty regarding economic developments in China has increased perceptibly. By contrast, the agreement of a new bailout programme for Greece has soothed concerns over an escalation of the sovereign debt crisis for the time being. Renewed turbulence in the international financial markets could have a major impact on global monetary policy.

In Switzerland, GDP rose slightly in the second quarter, after having declined somewhat in the previous quarter. Thus, overall economic output stagnated in the first half

Chart 1.1

CONDITIONAL INFLATION FORECAST OF SEPTEMBER 2015
Year-on-year change in Swiss consumer price index in percent



Source: SNB

of the year. Growth in employment continued at a slower pace. However, in manufacturing, employment decreased further. The seasonally adjusted unemployment rate continued to increase slightly during the summer months. Despite the fact that output remained stable overall following the appreciation of the Swiss franc in the first half of the year, the situation remains challenging for many companies. In view of the lower margins, these companies are under pressure to raise efficiency and reduce costs.

The SNB expects economic activity to pick up gradually in the second half of the year. Domestic demand is likely to further support the economy. If the international environment continues to improve and the overvaluation of the Swiss franc eases, exports should once again make a greater contribution to economic growth. For the current year, the SNB still expects real GDP growth of close to 1%.

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 Swiss 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.

Table 1.1

OBSERVED INFLATION IN SEPTEMBER 2015

	2012				2013				2014				2015				2012	2013	2014
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
Inflation	−0.9	−1.0	−0.5	−0.3	−0.4	−0.4	0.0	0.0	0.0	0.1	0.0	−0.1	−0.7	−1.1			−0.7	−0.2	0.0

CONDITIONAL INFLATION FORECAST OF SEPTEMBER 2015

	2015				2016				2017				2018				2015	2016	2017
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
Forecast June 2015, with Libor at -0.75%		−1.2	−1.2	−1.0	−0.6	−0.5	−0.3	−0.1	0.0	0.2	0.4	0.6	0.8				−1.0	−0.4	0.3
Forecast September 2015, with Libor at -0.75%			−1.4	−1.5	−0.9	−0.7	−0.4	−0.1	0.1	0.3	0.5	0.7	0.9	1.1			−1.2	−0.5	0.4

Source: SNB

2
Global economic environment

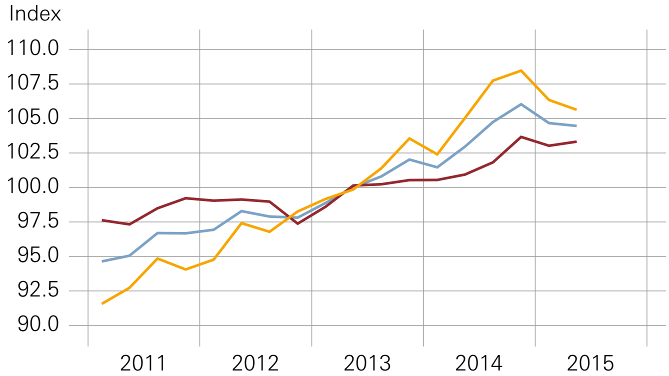
Global economic growth continued in the second quarter in line with expectations. In the advanced economies, growth was stronger than in the first quarter; this was mainly attributable to an economic revival in the US. Global recovery is not broad-based, however. To some extent, this is reflected in the lack of momentum in global trade and in low commodity prices (cf. charts 2.1 and 2.6).

The US economy picked up again after a weak first quarter. In the euro area, recovery continued at a moderate pace, buoyed by the favourable exchange rate situation. Developments in the large emerging economies were mixed. In China, positive developments in the services sector contributed to a slight strengthening of GDP growth. By contrast, economic output in Brazil and Russia dipped further.

Chart 2.1

GLOBAL EXPORTS

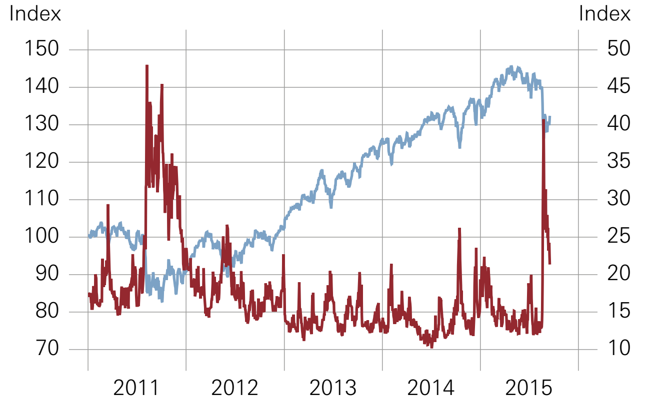
Period average = 100



Sources: CPB, Thomson Reuters Datastream

Chart 2.2

STOCK MARKETS



Source: Thomson Reuters Datastream

Table 2.1

BASELINE SCENARIO FOR GLOBAL ECONOMIC DEVELOPMENTS

	2011	2012	2013	2014	Scenario 2015	2016
GDP, year-on-year change in percent						
Global [1]	3.9	3.1	3.2	3.5	3.3	3.8
US	1.6	2.2	1.5	2.4	2.5	2.8
Euro area	1.6	–0.8	–0.3	0.9	1.5	2.0
Japan	–0.4	1.7	1.6	–0.1	0.7	1.4
Oil price in USD per barrel	111.4	111.7	108.7	99.0	54.0	50.0

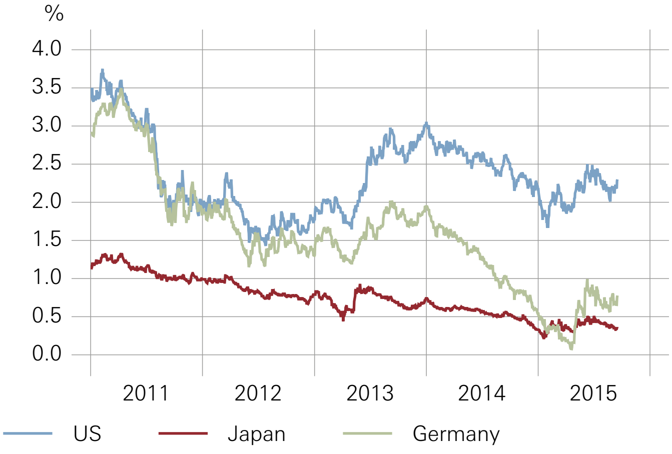
1 PPP-weighted (US, euro area, UK, Japan, China, South Korea, India, Brazil and Russia).

Sources: SNB, Thomson Reuters Datastream

Chart 2.3

INTERNATIONAL LONG-TERM INTEREST RATES

10-year government instruments

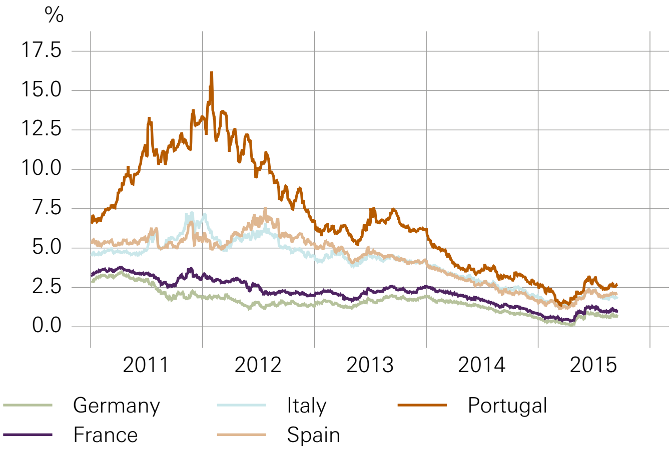


Source: Thomson Reuters Datastream

Chart 2.4

EUROPEAN LONG-TERM INTEREST RATES

10-year government instruments

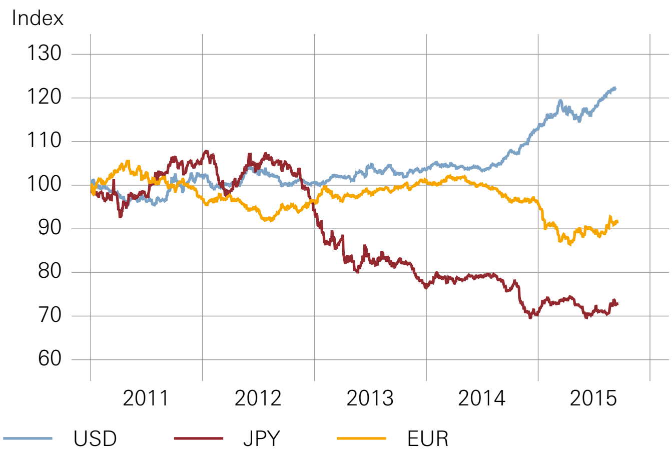


Source: Thomson Reuters Datastream

Chart 2.5

EXCHANGE RATES

Trade-weighted, beginning of period = 100



Source: Thomson Reuters Datastream

The SNB's baseline scenario for the world economy has remained largely unchanged. The moderate recovery is expected to continue in the coming quarters. Very expansionary monetary policy and low energy prices continue to support the recovery in the advanced economies. Consequently, underutilisation of production capacity should decrease further in these countries. In a number of the major emerging economies, however, activity remains weak. In August, fears of a sudden decline in economic activity in China caused turmoil in the global financial markets, which led the government to take further expansionary measures.

This baseline scenario is fraught with considerable risks. In particular, uncertainty regarding economic developments in China has increased. By contrast, the agreement of a new bailout programme for Greece has soothed concerns over an escalation of the sovereign debt crisis for the time being. Renewed turbulence in the international financial markets could have a major impact on global monetary policy.

The SNB's forecasts are based on assumptions about the oil price and the EUR/USD exchange rate. The SNB is assuming an oil price for Brent crude of USD 50 per barrel and an exchange rate of USD 1.10 to the euro. This corresponds to the 20-day average when the baseline scenario was drawn up.

INTERNATIONAL FINANCIAL AND COMMODITY MARKETS

The financial markets have been volatile since the monetary policy assessment in June. Until the agreement on a new financing programme, the crisis in Greece caused considerable uncertainty. In addition, increasing concerns regarding economic developments in the emerging economies, particularly China, contributed to turmoil in the stock and commodity markets. In mid-June, the Chinese stock market slumped. In August, there was renewed upheaval. The Chinese government reacted gradually with a range of stabilisation measures. Nevertheless, by mid-September, the Shanghai Composite Index lost around 35%, thereby falling to the level at the beginning of the year. The effects on the international financial markets were significant. The MSCI World Index fell to below the level at the beginning of the year. Implied volatility of US stocks (VIX) as measured by option prices – which serves an indicator of market uncertainty – rose at times to the highest level since 2011 (cf. chart 2.2).

Against this backdrop, yields on long-term government bonds in the advanced economies have fallen since mid-June (cf. chart 2.3). However, in the meantime, they have risen somewhat in some peripheral euro area economies, in the wake of the crisis in Greece. Market expectations regarding US monetary policy influenced movements in the foreign exchange market. Initially, the US dollar appreciated across a broad front. This was due in part to the fact that markets expected the Federal Reserve to lift key interest rates. At the end of August, fears of a slowdown in the world economy meant that this interest rate rise was postponed. As a result, the US dollar weakened somewhat against the euro and the yen, while it continued to gain value against currencies of emerging markets. Most recently, the euro and the yen appreciated somewhat on a trade-weighted basis (cf. chart 2.5).

Commodity prices declined across the board in the light of plentiful supply and modest demand (cf. chart 2.6). In particular, prices for industrial metals and oil were significantly lower because of concerns regarding China's economy.

UNITED STATES

The US economy gained momentum in the second quarter. After a weak first quarter, GDP expanded by 3.7% in the second quarter (cf. chart 2.7). Supported by lower petrol prices, private consumption recovered considerably. Moreover, special factors including cold weather and strikes at West Coast ports that had put strain on growth in the first quarter ceased. The unemployment rate stood at 5.1% in August (cf. chart 2.10). The low participation rate and increased part-time work suggest that labour force potential is still underutilised.

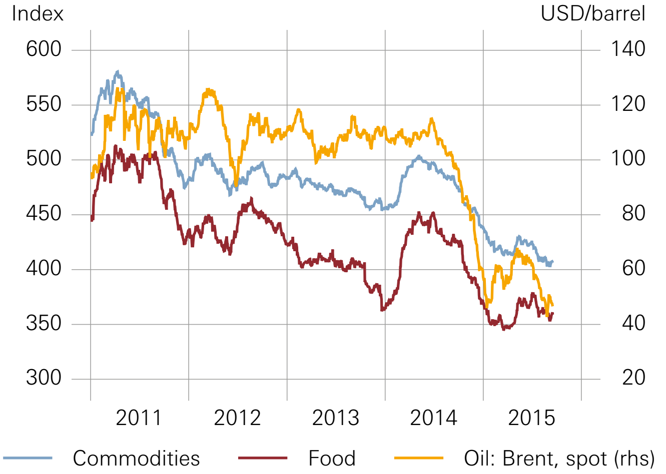
The economic outlook is favourable overall. The robust increase in employment and higher wage growth are likely to stimulate aggregate potential output in the next few quarters. By contrast, the appreciation of the US dollar is continuing to have a dampening effect. In addition, as part of an annual revision of data, average economic growth for the last three years was adjusted downwards by the Bureau of Economic Analysis. Against the backdrop of lower productivity, lower growth potential is expected in the coming quarters. Owing to strong growth in the second quarter, the SNB has raised its growth forecast for 2015 to 2.5%; for 2016 by contrast, expectations are somewhat lower than three months ago, at 2.8% (cf. table 2.1).

Due to lower oil prices, annual inflation measured in terms of consumer prices has remained at zero over the past few months. In August, it stood at 0.2%, while core inflation remained almost unchanged, at 1.8% (cf. charts 2.11 and 2.12). Based on the assumption of higher oil prices in the baseline scenario, consumer prices in the US are likely to virtually stagnate, averaged over 2015.

The Federal Reserve left the target range for the federal funds rate unchanged at 0.0–0.25% (cf. chart 2.13). It still assumes that the situation in the US economy will, for some time yet, require lower interest rates than usual, even after price stability and full employment have been achieved. In the current environment, the markets expect gradual normalisation to begin towards the end of the year.

Chart 2.6

COMMODITY PRICES

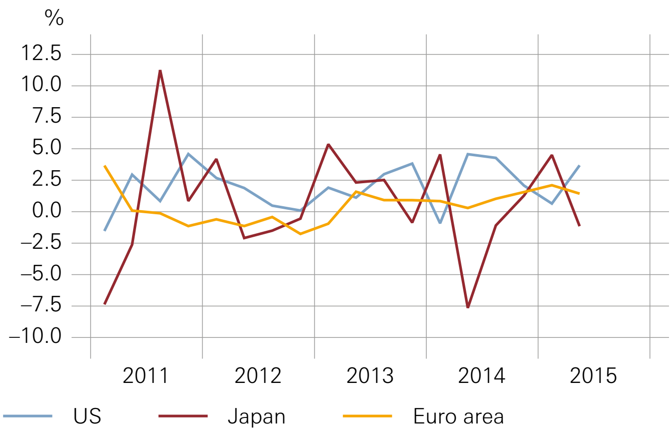


Source: Thomson Reuters Datastream

Chart 2.7

REAL GDP: ADVANCED ECONOMIES

Change from previous period

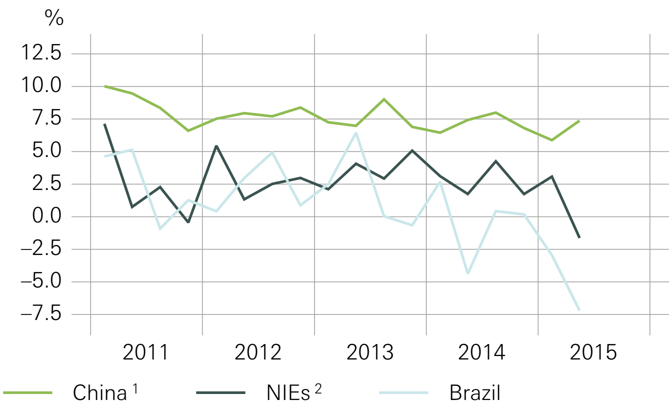


Source: Thomson Reuters Datastream

Chart 2.8

REAL GDP: EMERGING ECONOMIES

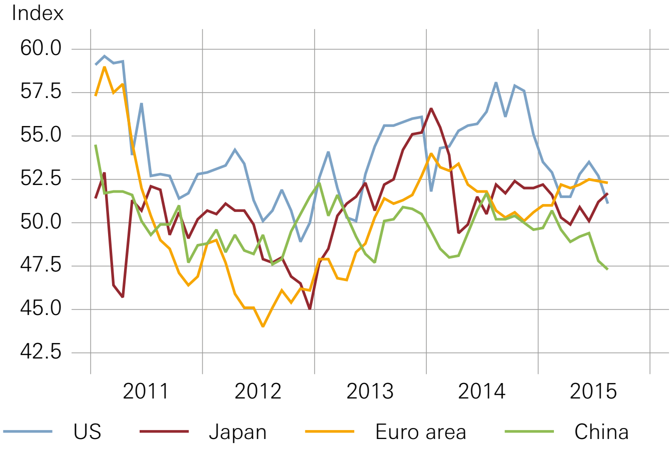
Change from previous period



1 Estimate: SNB.
2 PPP-weighted (South Korea, Taiwan, Hong Kong, Singapore).
Source: Thomson Reuters Datastream

Chart 2.9

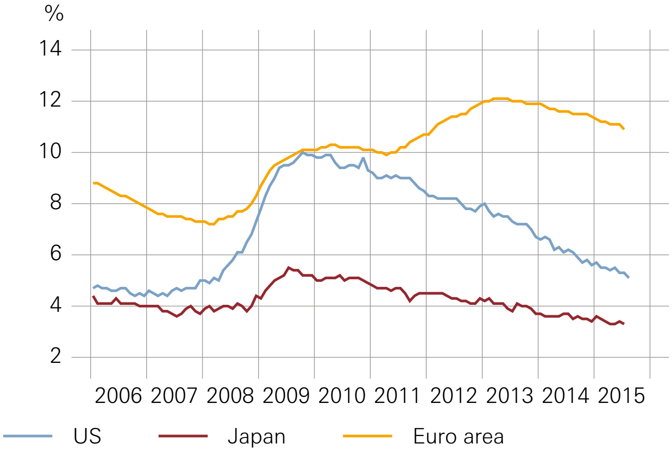
PURCHASING MANAGERS' INDICES (MANUFACTURING)



Source: Markit Economics Ltd 2009; all rights reserved

Chart 2.10

UNEMPLOYMENT RATES

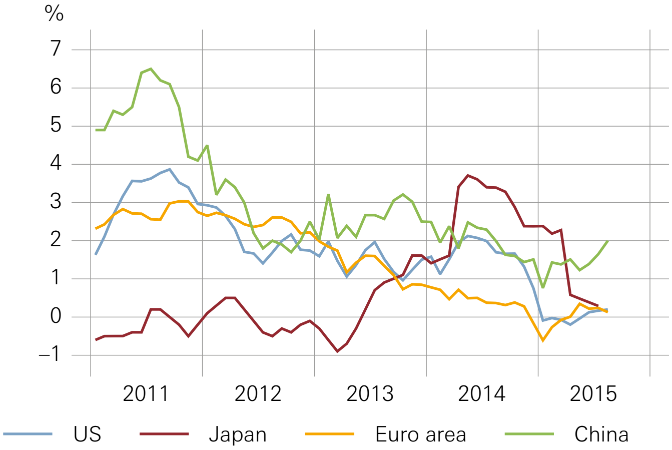


Source: Thomson Reuters Datastream

Chart 2.11

CONSUMER PRICES

Year-on-year change



Source: Thomson Reuters Datastream

EURO AREA

The moderate recovery in the euro area continued. GDP increased by 1.4% in the second quarter (cf. chart 2.7). Growth was mainly underpinned by exports and private consumption, while investments decreased for the first time in a year. Compared to previous periods of economic growth, the expansion that began in the euro area at the beginning of 2013 is slower. Unemployment has decreased only slightly since its peak in mid-2013, and stood at 10.9% in July (cf. chart 2.10).

Expansionary monetary policies and low oil prices continue to provide positive growth stimuli. Financing conditions for private households and companies have improved. Moreover, uncertainty about Greece's future has decreased since the agreement of a third financing programme. Against this backdrop, the surveys point to moderate economic recovery. Nevertheless, Greece continues to face major challenges. The path of monetary policy following the new elections of 20 September remains uncertain and the economic effects of the capital controls introduced at the end of June are difficult to assess. In some other euro area member states, the restructuring of public sector finances and the implementation of reforms for the promotion of growth also pose major challenges. Overall, the SNB has left its growth forecast for the euro area almost unchanged. It anticipates growth of 1.5% for 2015 and 2.0% for 2016.

Owing to falling oil prices, consumer price inflation in the euro area declined slightly and stood at 0.1% in August (cf. chart 2.11). Core inflation remained unchanged at 0.9% (cf. chart 2.12). Surveys of companies showed that inflation expectations and wage growth remained moderate.

The European Central Bank left its key rates unchanged (cf. chart 2.13). The asset purchase programme initiated in March is being carried out as planned and will run until at least September 2016. As a consequence of the programme, surplus liquidity rose further and the three-month Euribor remained almost unchanged in negative territory.

JAPAN

The Japanese economy lost momentum in the second quarter. GDP shrank by 1.2% after growth of 4.5% in the first quarter (cf. chart 2.7). Exports declined for the first time in six quarters. Consumer spending also decreased although this was, in part, due to special factors.

Buoyed by the weak yen, stronger demand from abroad and cheaper energy imports, recovery should strengthen again in the third quarter. In the light of high corporate earnings and favourable financing conditions, sentiment in the export industry remains upbeat. However, for some industries with a domestic focus, the situation continues to be difficult because of subdued consumer growth. Due to better utilisation of labour market capacity, overall wage growth is likely to pick up gradually and support consumer spending by private households. In addition, at the end of June, the Japanese government announced that it had no further measures planned until 2018 for putting its finances on a sounder footing, and that economic growth would be the priority for the next three years. The SNB is leaving its growth forecast for Japan largely unchanged (cf. table 2.1).

Since April, inflation has trended downwards slightly, with higher food prices partly offsetting the decline in energy prices. In July, annual inflation stood at 0.3% (cf. chart 2.11). For the time being, it is likely to carry on receding under the impact of lower oil prices. In the past few months, longer-term inflation expectations have continued to stagnate below the Japanese central bank's inflation target of 2%. Since relaxing its monetary policy at the end of October 2014, the Bank of Japan has not made any further adjustments to its policy, which is geared to an expansion of the monetary base (cf. chart 2.14).

EMERGING ECONOMIES

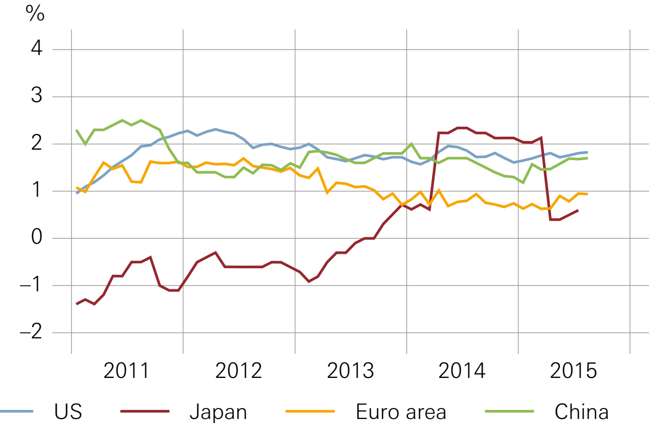
The economic trend in the emerging economies varied from one country to another. In China, economic growth accelerated somewhat in the second quarter, supported by monetary and fiscal easing measures introduced since the end of last year (cf. chart 2.8). In India, GDP continued to grow strongly, while it receded further in Brazil and Russia.

The SNB expects economic growth of just under 7% in China this year. The recent turmoil in the Chinese stock market has, however, highlighted the risks associated with structural change. Although the direct effects of the stock market correction on the overall economy can be considered limited, in particular as private households and banks hold relatively few equities, and stock market financing of companies is still negligible in China, a high level of overcapacity and indebtedness in manufacturing and construction continue to weigh on the economic outlook, and carry high risks. The latest surveys in manufacturing suggest a slowdown in industrial activity in the second half of the year. The government has

Chart 2.12

CORE INFLATION RATES [1]

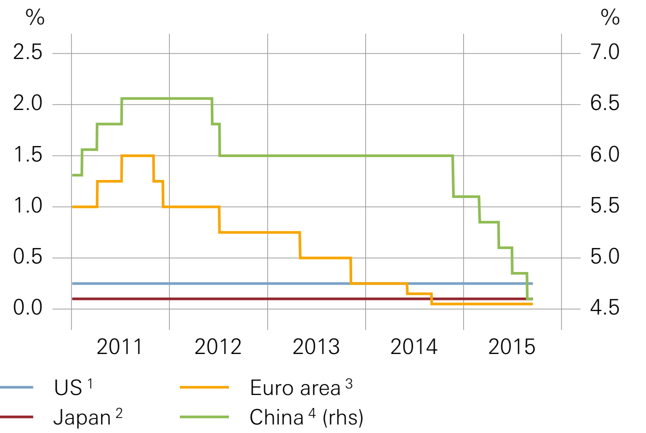
Year-on-year change



1 Excluding food and energy.
Source: Thomson Reuters Datastream

Chart 2.13

OFFICIAL INTEREST RATES

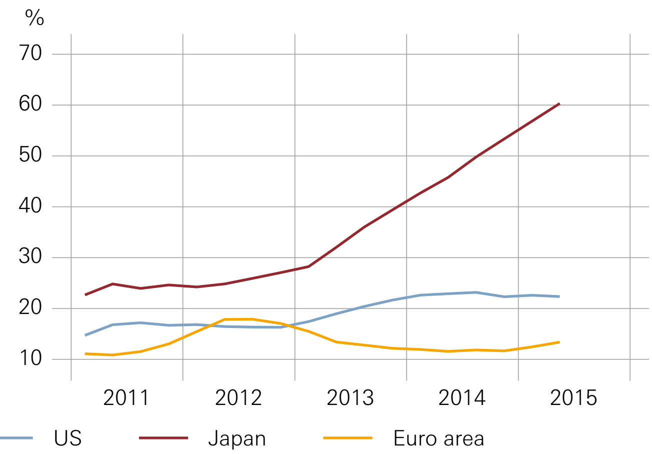


1 Federal funds rate.
2 Call money target rate.
3 Main refinancing rate.
4 One-year lending rate.
Source: Thomson Reuters Datastream

Chart 2.14

MONETARY BASE

Relative to GDP



Source: Thomson Reuters Datastream

expedited the implementation of infrastructure projects to stabilise the economy in the short term.

The SNB forecasts short-term growth close to potential for India. However, the rise in non-performing loans and delays in the implementation of economic reforms pose slight downside risks. In both Russia and Brazil, it is becoming apparent that economic output will decline again this year. The Russian economy, which is dependent on oil and gas exports, is suffering from low commodity prices and the sanctions imposed by the West. In Brazil, the economic crisis is likely to continue in the short term because of declining real incomes, increasing unemployment and political uncertainty.

Inflation in the emerging economies is developing unevenly. In China it rose, but was still below the central bank's target figure of 3.0% for 2015 (cf. chart 2.11). In India, inflation once again receded perceptibly in the light of declining food prices (3.7%). In Brazil and Russia, by contrast, inflation lingered at an exceptionally high level (9.5% and 15.8% respectively), due in part to their weak currencies.

China's central bank decreased its key interest rate and reserve ratio further at the end of July and the end of August, to support the economy and to restore trust in the market against the backdrop of falling share prices (cf. chart 2.13). In addition, it permitted a moderate depreciation of the renminbi against the US dollar, in the context of an adjustment of the exchange rate regime in mid-August. The central banks of India and Russia also decreased their key interest rates. The Russian central bank reduced its rate further to 11.0% in an effort to support the economy; however, the objective is to stabilise the currency by maintaining a high level. The Brazilian central bank, by contrast, raised its key interest rate further in order to combat inflation and the depreciation of the Brazilian real.

3
Economic developments in Switzerland

After a negative trend at the beginning of the year, economic activity in Switzerland stabilised in the second quarter as expected. According to an initial estimate by the State Secretariat for Economic Affairs (SECO), GDP was up by 1.0% in the second quarter, thereby regaining the level attained at the end of 2014. Growth was broad-based on the demand side. On the output side, a recovery in manufacturing made a significant contribution to stimulating growth. In view of the difficult exchange rate situation since the discontinuation of the minimum exchange rate, profit margins remain under considerable pressure in numerous sectors.

The aggregate output gap remained in negative territory in the second quarter. Manufacturing experienced a slight increase in capacity utilisation. Employment growth weakened and unemployment continued to edge up.

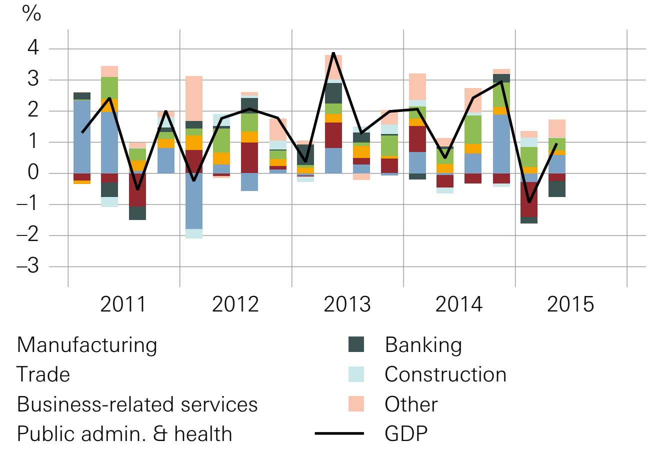
The Swiss franc is still significantly overvalued, and this situation continues to have an impact on economic development. However, the incremental improvement of the global economy is likely to result in a gradual firming of foreign demand for Swiss goods and services and counteract the unfavourable exchange rate situation. The SNB continues to expect growth of close to 1.0% for 2015.

AGGREGATE DEMAND AND OUTPUT

Slight growth recovery in second quarter
Stabilisation in the second quarter was driven by two sectors in particular. First, value added in manufacturing began to increase again; second, the decrease in value added in the trade sector slowed considerably after the previous quarter's setback (cf. chart 3.1). The other sectors presented a mixed picture. Value added in several service industries (e.g. business-related services, insurance and public administration) increased in both the first and second quarters, helping to stabilise the economic situation after the appreciation of the Swiss franc.

Chart 3.1

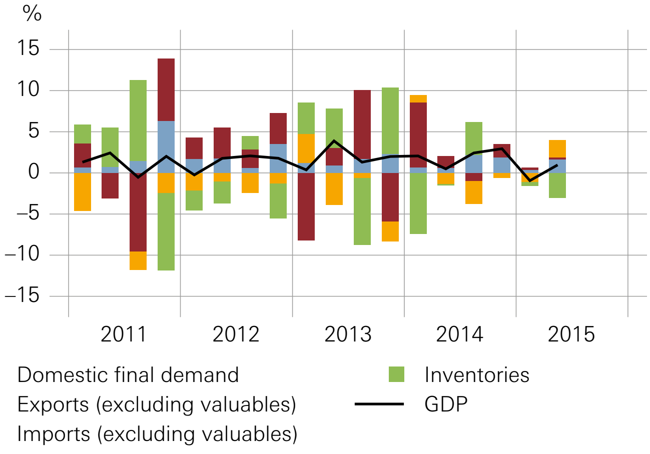
CONTRIBUTIONS TO GROWTH, BY SECTOR
Change from previous period



Source: State Secretariat for Economic Affairs (SECO)

Chart 3.2

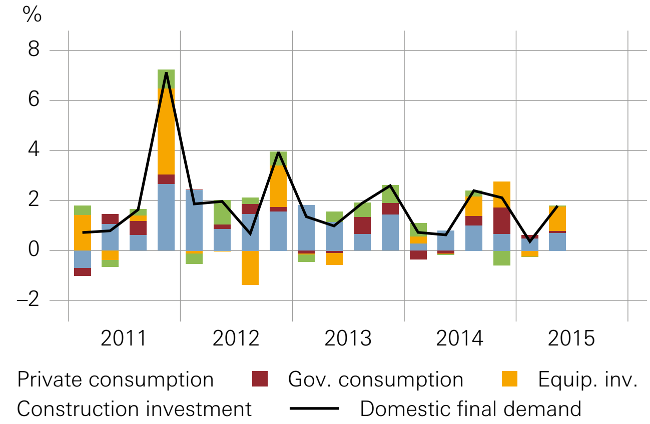
CONTRIBUTIONS TO GROWTH IN DEMAND
Change from previous period



Source: SECO

Chart 3.3

DOMESTIC FINAL DEMAND, GROWTH CONTRIBUTIONS
Change from previous period



Source: SECO

Domestic demand gathers momentum

Domestic final demand gained slightly in momentum in the second quarter (cf. chart 3.3 and table 3.1). Robust growth in equipment investment – reinforced by considerably lower prices for capital goods – made a substantial contribution here. Consumer spending also rose somewhat more strongly than in the previous period. However, despite continued high levels of immigration and favourable income developments, consumer spending again registered below average growth. Moreover, spending growth was essentially limited to vehicle purchases and the health sector. The small rise in construction investment was driven by civil engineering. Residential construction saw another slight decline.

Positive foreign trade contribution

Exports rose only slightly in the second quarter, while imports declined substantially. This resulted in a robust foreign trade contribution to GDP growth (cf. table 3.1). Trade in goods, including merchanting, was down in both directions. While traditional goods exports (excluding merchanting) increased slightly, these were still considerably below the level of the previous year. Exporting companies not only suffered as a result of the difficult exchange rate situation, but also because of the slowdown in the global industrial cycle, which is reflected in the lack of momentum in global trade.

Table 3.1

REAL GDP AND COMPONENTS

Growth rates on previous period in percent, annualised

	2011	2012	2013	2014	2013		2014				2015	
					Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
Private consumption	0.8	2.7	2.2	1.3	1.1	2.3	0.4	1.3	1.6	1.1	0.8	1.2
Government consumption	2.1	2.1	1.3	1.3	5.6	3.7	–2.8	–1.0	3.0	8.6	1.1	0.6
Investment in fixed assets	4.3	2.9	1.2	2.1	2.1	2.6	3.1	–0.2	3.9	1.6	–1.0	3.8
Construction	2.5	2.9	3.1	3.3	5.6	6.9	5.0	–0.4	2.2	–5.6	–0.3	0.5
Equipment	5.3	2.8	0.0	1.3	0.0	0.0	1.8	0.0	4.9	6.5	–1.4	6.0
Domestic final demand	1.9	2.7	1.8	1.5	1.9	2.6	0.7	0.6	2.4	2.1	0.4	1.8
Change in inventories [1]	0.3	–1.0	0.7	–0.4	–8.2	8.0	–7.4	–0.2	4.1	0.0	–0.5	–3.0
Total exports [2]	3.5	3.0	0.0	4.2	16.3	–11.1	15.4	2.8	–1.8	3.1	0.6	0.5
Goods [2]	6.2	0.9	–2.3	5.1	27.6	–17.6	19.7	9.7	–6.1	1.7	3.8	–1.0
Goods excluding merchanting [2]	6.5	1.7	–1.0	4.0	2.9	–4.4	12.1	2.2	9.9	–3.8	–8.6	2.1
Services	–2.2	7.4	4.7	2.4	–2.7	3.2	7.5	–9.8	7.5	5.8	–5.4	3.5
Total imports [2]	4.7	4.4	1.3	2.8	1.4	5.8	–2.1	3.1	6.7	1.3	2.6	–5.2
Goods [2]	3.1	2.3	0.7	1.7	–0.1	13.3	–10.0	10.1	2.2	–7.1	2.6	–13.6
Services	8.6	9.3	2.9	5.1	4.6	–8.9	17.1	–10.2	17.1	20.8	2.3	12.7
Net exports [3]	–0.1	–0.2	–0.6	1.0	7.8	–8.3	8.8	0.1	–3.8	1.0	–0.8	2.4
GDP	**1.8**	**1.1**	**1.8**	**1.9**	**1.3**	**2.0**	**2.1**	**0.5**	**2.4**	**2.9**	**–0.9**	**1.0**

1 Contribution to growth in percentage points (including statistical discrepancy).
2 Excluding valuables (non-monetary gold and other precious metals, precious stones and gems as well as works of art and antiques).
3 Contribution to growth in percentage points.

Source: SECO

LABOUR MARKET

The slowdown in economic activity in Switzerland registered since the discontinuation of the minimum exchange rate has impacted on the labour market. Employment growth declined appreciably and unemployment increased slightly.

Diminished employment growth

According to the employment statistics of the Swiss Federal Statistical Office, the number of gainfully employed persons advanced by 1.1% (seasonally adjusted) in the second quarter (cf. chart 3.4). Compared to the previous quarters, growth was thus weaker. This can, at least partially, be attributed to the sharp appreciation of the Swiss franc at the beginning of the year.

Based on the national job statistics (JOBSTAT), new jobs were created in the services sector, which accounts for approximately three-quarters of full-time equivalent positions. By contrast, employment in manufacturing once again declined slightly (cf. chart 3.5).

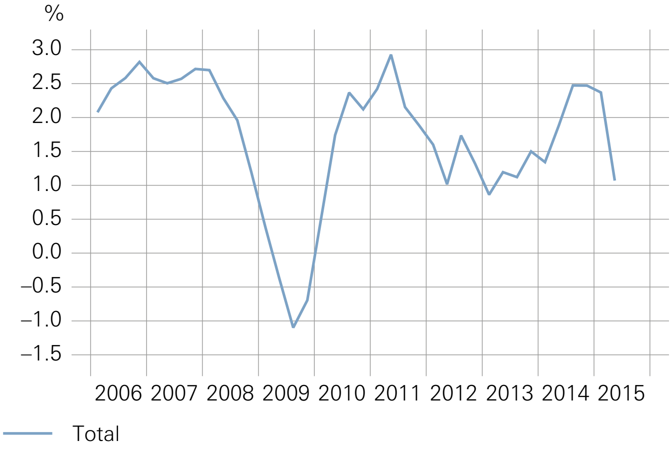
Slight rise in unemployment

The seasonally adjusted rate of unemployment continued to rise. Excluding seasonal fluctuations, 145,000 people were unemployed at the end of August. This amounts to an increase of around 8,000 people compared to the low point recorded in November 2014. The seasonally adjusted unemployment rate was 3.3% in August (cf. chart 3.6).

Chart 3.4

EMPLOYED PERSONS

Change from previous period

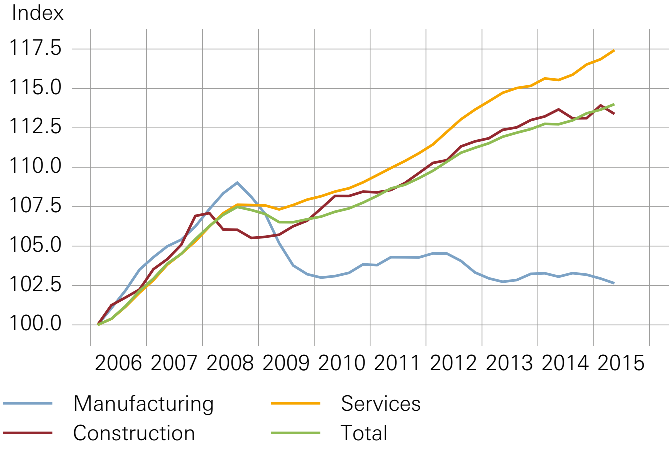


Source: Swiss Federal Statistical Office (SFSO); seasonal adjustment: SNB

Chart 3.5

FULL-TIME EQUIVALENT JOBS

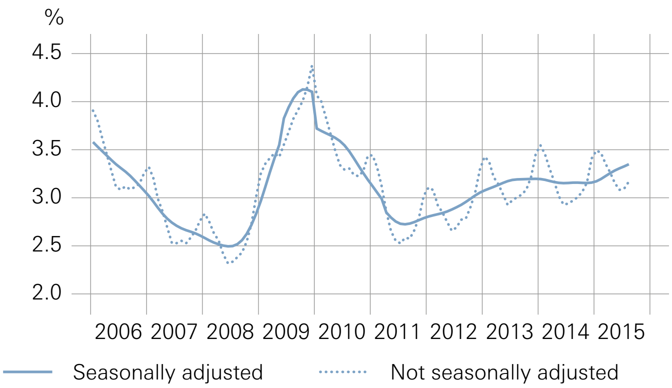
Q1 2006 = 100



Source: SFSO; seasonal adjustment: SNB

Chart 3.6

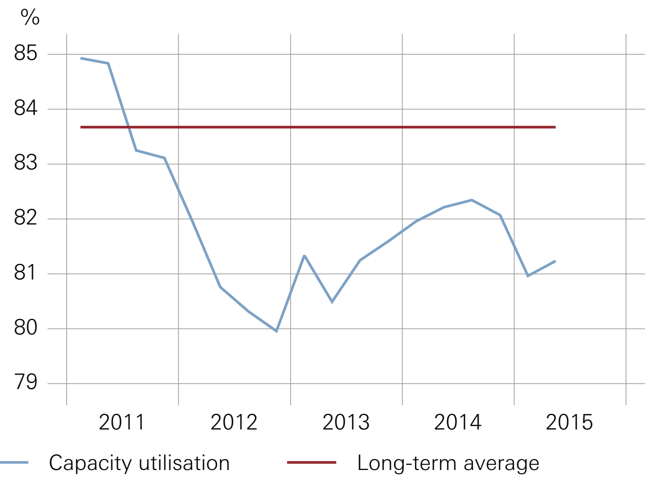
UNEMPLOYMENT RATE



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) up to 2009, and according to the 2010 census (labour force: 4,322,899 persons) from 2010.
Source: SECO

Chart 3.7

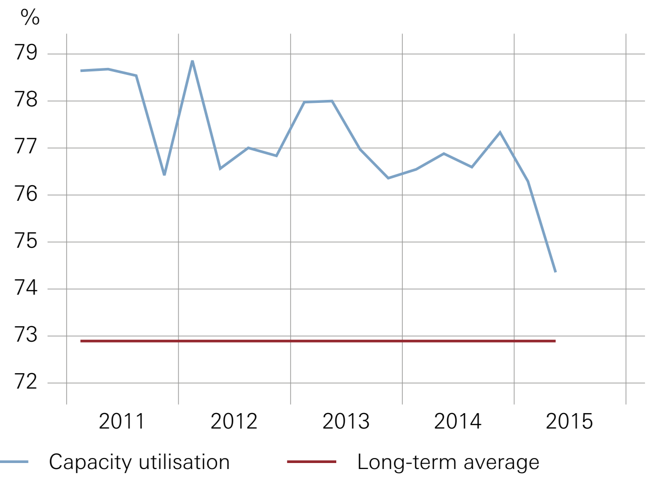
CAPACITY UTILISATION IN MANUFACTURING



Source: KOF Swiss Economic Institute

Chart 3.8

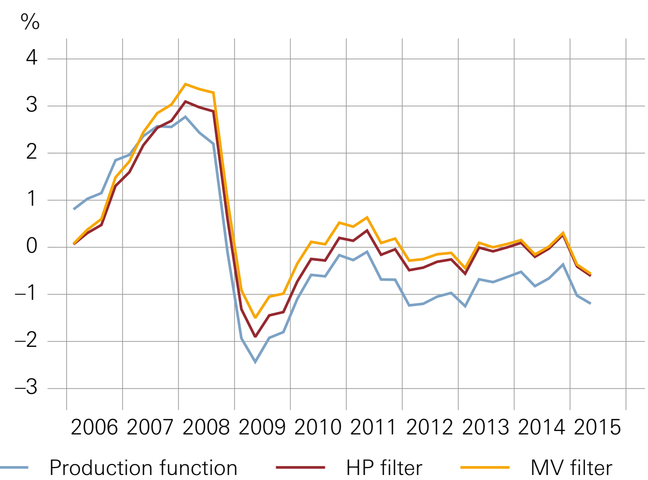
CAPACITY UTILISATION IN CONSTRUCTION



Source: KOF Swiss Economic Institute

Chart 3.9

OUTPUT GAP



Source: SNB

CAPACITY UTILISATION

Underutilisation in manufacturing

According to the survey by KOF Swiss Economic Institute, utilisation of technical capacity in manufacturing increased slightly to 81.2% in the second quarter. It is thus still well below the long-term average (cf. chart 3.7). By contrast, machine utilisation in the construction industry was down considerably in the second quarter. However, unlike in manufacturing, capacity utilisation in construction remains above the long-term average (cf. chart 3.8). The surveys continue to point to an average level of capacity utilisation in the services sector.

Negative output gap widening

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. Given the subdued GDP growth in the second quarter, underutilisation of production capacity in the economy as a whole intensified. Estimated potential, calculated by means of a production function, showed an output gap of –1.2% for the second quarter, compared to –1.0% in the previous quarter. Estimates using other methods (Hodrick-Prescott filter and multivariate filter) suggest a slightly narrower gap (cf. chart 3.9).

The different estimates reflect the various ways of calculating production potential. The production function approach considers the labour market situation and the stock of capital in the economy. 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.

OUTLOOK FOR THE REAL ECONOMY

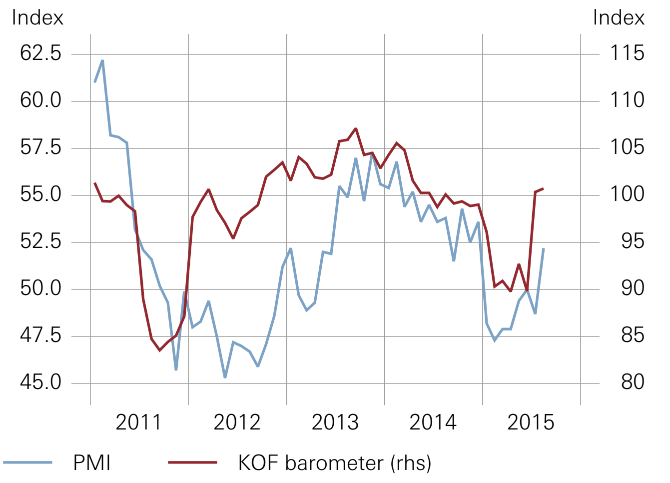
Growth in Switzerland is likely to pick up gradually during the second half of 2015. Various indicators suggest that the economic situation in the third quarter has improved somewhat. For instance, the KOF economic barometer and the manufacturing purchasing managers' index are clearly above the low they recorded at the beginning of the year (cf. chart 3.10).

Domestic demand is likely to further support the economy. Thanks to the improved global environment and the slight easing in the overvaluation of the Swiss franc, exports may also be expected to gradually start making a greater contribution to growth. The SNB continues to expect GDP growth of close to 1% for 2015.

The impact of Swiss franc appreciation nevertheless remains palpable. Companies, especially those competing directly with businesses abroad, are under considerable price pressure. Domestic businesses are also facing increased pressure on prices as a result of exposure to import competition. In many cases, sales volumes can only be maintained at the expense of profit margins. Companies are therefore under pressure to raise efficiency and reduce costs.

Chart 3.10

LEADING INDICATORS

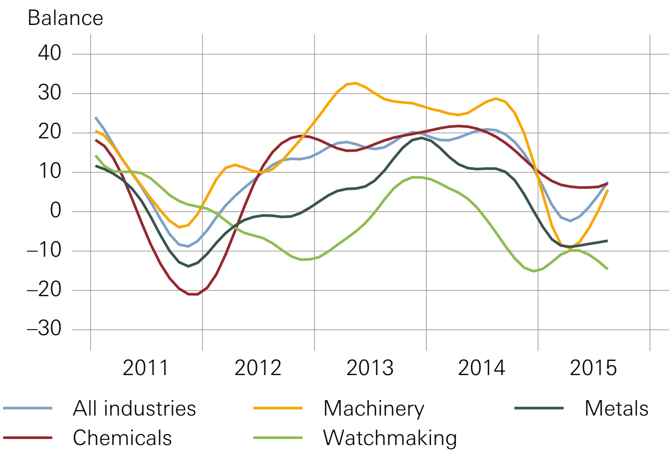


Sources: Credit Suisse, KOF Swiss Economic Institute

Chart 3.11

EXPECTED NEW ORDERS

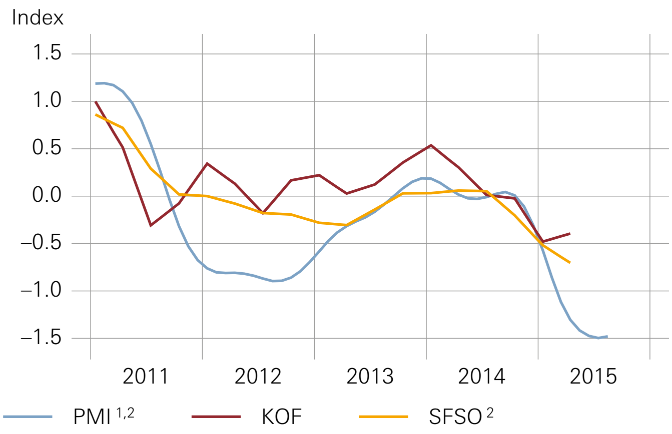
Trend component



Source: KOF Swiss Economic Institute

Chart 3.12

EMPLOYMENT LEADING INDICATORS



1 Monthly figures.
2 Trend component: SNB.
Sources: Credit Suisse, KOF Swiss Economic Institute, SFSO

4 Prices and inflation expectations

Annual consumer price inflation remains clearly in negative territory. Influenced by oil prices, it was lower again in August (–1.4%) than in May, the month prior to the mid-June monetary policy assessment.

At present, positive contributions to annual consumer price inflation come almost exclusively from services, in particular from rents. But even there, the inflation rates are modest. Owing to the decrease in the reference interest rate relevant for the setting of rents, rent inflation is expected to remain low.

Producer and import prices have declined much more steeply than consumer prices over the past 12 months. The downward pressure of producer and import prices on downstream consumer prices therefore remains strong.

Surveys show that inflation expectations have stabilised in the past few months, having dropped markedly following the discontinuation of the minimum exchange rate. Since then, they have risen again slightly.

On the real estate market, prices for owner-occupied apartments and single-family homes continued to rise. Imbalances and risks on the real estate market thus persist.

CONSUMER PRICES

Lower negative inflation rate

The annual inflation rate as measured by the national consumer price index (CPI), having already dropped considerably since autumn 2014, again receded slightly between May and August 2015. In August it amounted to –1.4%, compared to –1.2% in May (cf. table 4.1).

Stable contributions to inflation from main components excluding oil

Contributions to inflation made by domestic goods and services and by foreign goods and services excluding oil products remained largely unchanged between May and August 2015 (cf. chart 4.1). The decline in the CPI annual inflation rate registered in this period is therefore primarily due to movements in prices for oil products.

Table 4.1

SWISS CONSUMER PRICE INDEX AND COMPONENTS

Year-on-year change in percent

	2014	2014		2015		2015		
		Q3	Q4	Q1	Q2	June	July	August
Overall CPI	**0.0**	**0.0**	**–0.1**	**–0.7**	**–1.1**	**–1.0**	**–1.3**	**–1.4**
Domestic goods and services	0.4	0.3	0.4	0.5	0.2	0.2	0.1	0.0
Goods	0.3	0.3	0.2	0.0	–0.7	–0.8	–1.1	–0.9
Services	0.4	0.3	0.5	0.6	0.5	0.4	0.5	0.3
Private services excluding rents	0.4	0.3	0.6	0.8	0.5	0.4	0.4	0.4
Rents	1.2	1.1	1.1	1.0	1.2	1.2	1.2	0.7
Public services	–0.8	–0.9	–1.2	–0.8	–0.9	–1.0	–1.0	–0.8
Imported goods and services	–1.2	–0.9	–1.6	–4.2	–4.8	–4.4	–5.3	–5.5
Excluding oil products	–1.0	–0.7	–0.8	–1.5	–2.7	–2.4	–3.2	–3.1
Oil products	–2.4	–1.8	–6.7	–19.3	–16.6	–16.1	–16.8	–18.9

Sources: SFSO, SNB

Prices of domestic goods and services in August were at exactly the same level as one year back. Positive contributions to inflation made by services were offset by negative contributions from domestic goods. The quarterly rents survey shows that inflation in rentals receded slightly in August (cf. chart 4.2).

Negative core inflation rates

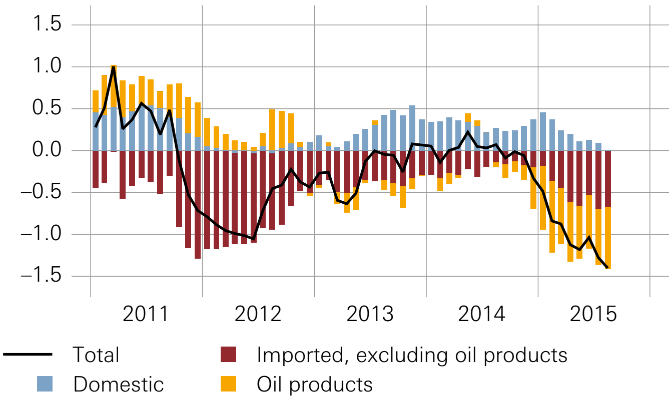
Core inflation rates have been in negative territory since March, dropping substantially up to May and only slightly since (cf. chart 4.3). The core inflation rate calculated by the SFSO (SFSO1) decreased from –0.6% in May to –0.7% in August. Over the same period, the trimmed mean calculated by the SNB (TM15) fell from –0.4% to –0.6%.

The difference between the CPI annual inflation rate and the two core inflation rates primarily reflects the movements in prices for oil products. When calculating SFSO1, fresh and seasonal products as well as energy and fuel are excluded, whereas TM15 takes the distribution of weighted annual rates of price change for CPI products, and excludes 15% from each end. The goods and services for which prices have fallen most sharply over the past 12 months are mainly oil products.

Chart 4.1

CPI: DOMESTIC AND IMPORTED GOODS AND SERVICES

Year-on-year change in CPI in percent. Contribution of individual components, in percentage points.

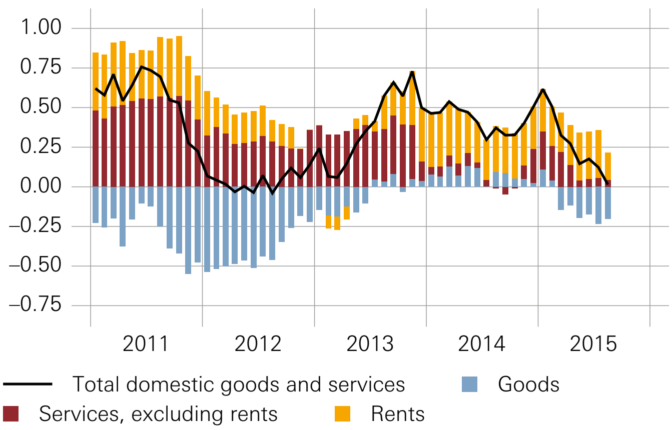


Sources: SFSO, SNB

Chart 4.2

CPI: DOMESTIC GOODS AND SERVICES

Year-on-year change in domestic CPI in percent. Contribution of individual components, in percentage points.

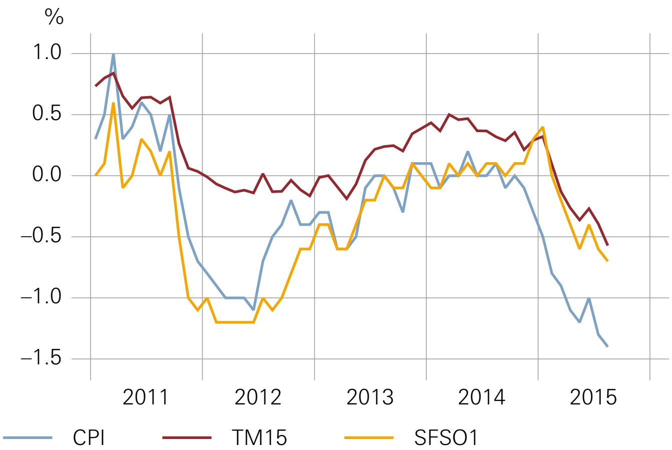


Sources: SFSO, SNB

Chart 4.3

CORE INFLATION RATES

Year-on-year change

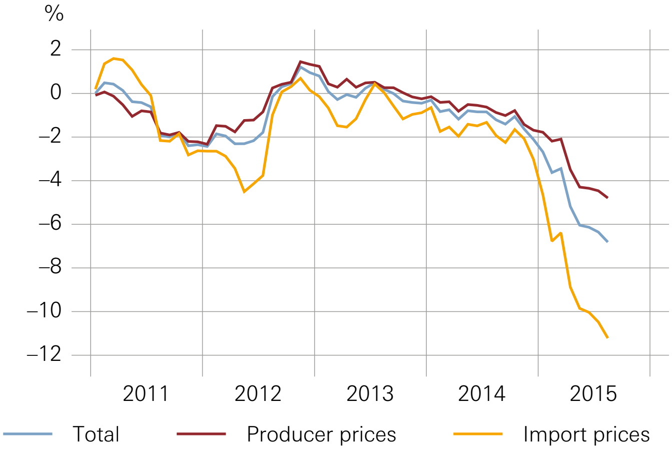


Sources: SFSO, SNB

Chart 4.4

PRODUCER AND IMPORT PRICES

Year-on-year change

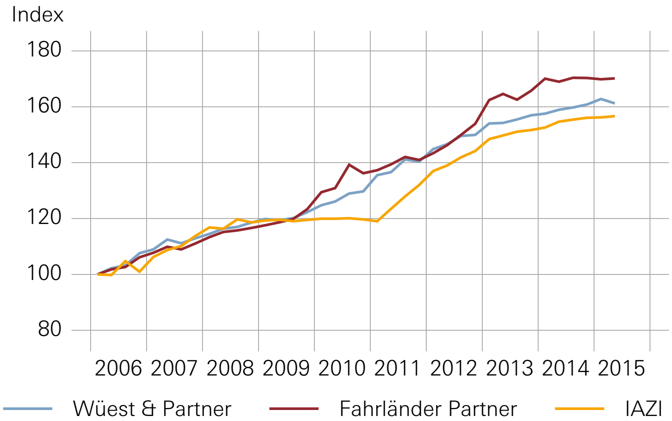


Source: SFSO

Chart 4.5

TRANSACTION PRICES, OWNER-OCCUPIED APARTMENTS

Nominal (hedonic), beginning of period = 100

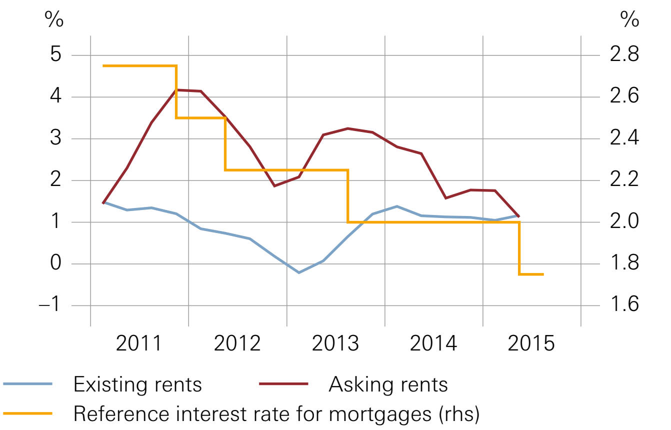


Sources: Fahrländer Partner, IAZI, Wüest & Partner

Chart 4.6

APARTMENT RENTS AND REFERENCE INTEREST RATE

Nominal, year-on-year change (lhs)



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

PRODUCER AND IMPORT PRICES

Decline in producer and import prices

The annual inflation rate of producer and import prices amounted to –6.8% in August, compared to –6.0% in May. The year-on-year decline in import prices is still considerably more pronounced than that in producer prices (cf. chart 4.4).

The producer and import price level had dropped sharply between November and May under the influence of the steep decline in oil prices and the appreciation of the Swiss franc following the discontinuation of the minimum exchange rate; this decline in producer and import prices slowed from May onwards.

REAL ESTATE PRICES

Slight rise in prices for residential property

According to most available indices, prices for residential property (owner-occupied apartments and single-family homes) rose slightly in the second quarter of 2015. The Wüest & Partner price index for owner-occupied apartments was an exception; it receded, having made considerable gains in the previous quarter (cf. chart 4.5).

The upward pressure on prices has diminished since the beginning of 2013, more markedly in the case of owner-occupied apartments than for single-family homes. Viewed over the past ten years, however, the price increase for owner-occupied apartments is still distinctly stronger than that for single-family homes.

Moderate rise in existing rents

Annual inflation in rents recorded in the CPI, which may be regarded as a benchmark for existing rents, continued to be moderate in the second quarter (cf. chart 4.6).

Inflation in existing rents may weaken further in the coming quarters, for two reasons. First, the price increase in rents for apartments offered on the market (asking rents) recorded by Wüest & Partner slowed noticeably in the second quarter of 2015. And second, the mortgage reference rate relevant for the setting of rents dropped to 1.75% as of 1 June 2015.

INFLATION EXPECTATIONS

Stabilisation of inflation expectations
The survey of households conducted by SECO in July shows that just under half of the respondents expect prices to remain unchanged over the next twelve months (cf. chart 4.7). This is a slightly higher proportion compared to the survey of April this year. The share of respondents expecting a rise in prices also grew, whereas the percentage of those anticipating price declines was down.

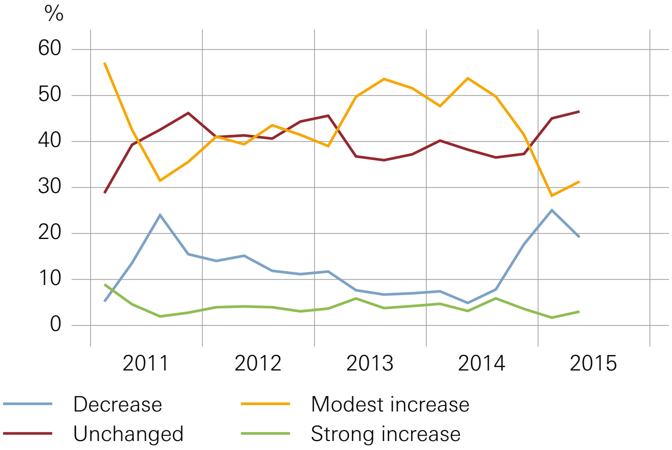
A growing proportion (71% in August as against 63% in May) of the financial analysts surveyed for Credit Suisse's ZEW Financial Market Report assume that the inflation rate will remain unchanged over the six months ahead. The number of respondents expecting rising inflation rates remained largely the same at 15%. By contrast, the proportion of respondents anticipating lower, i.e. more strongly negative, inflation rates has decreased (15% in August compared to 21% in May).

Talks held by the SNB delegates for regional economic relations with companies from all sectors of the economy confirmed the stabilisation of short-term inflation expectations. In the third quarter, respondents expected the inflation rate to be –0.4% in six to twelve months, compared with –0.6% in the previous quarter.

Chart 4.7

PRICE EXPECTATIONS

Survey on expected movements in prices for coming 12 months



Sources: SECO, SNB

Higher medium-term inflation expectations
Medium-term inflation expectations increased slightly, after having declined following the discontinuation of the minimum exchange rate. Participants in Deloitte's CFO survey in the second quarter put inflation in two years' time at 0.7%, compared to 0.6% in the first quarter. Talks held by the SNB delegates for regional economic relations yielded similar results. In the third quarter, respondents expected the inflation rate to be 0.6% in three to five years (previous quarter's expectation: 0.5%).

No new surveys on long-term inflation expectations have been published since the monetary policy assessment of June. The results available at the time for six-to-ten-year inflation expectations indicate that long-term inflation expectations have not been influenced by the discontinuation of the minimum exchange rate.

5
Monetary developments

Overall, monetary indicators have changed little since May, presenting a similar picture to that reported at the last monetary policy assessment in June.

Short-term interest rates were shaped by negative interest on sight deposits at the SNB, which had been left unchanged at –0.75% at the mid-June assessment. Money market interest rates – on secured as well as unsecured money market transactions – thus remained in negative territory.

Long-term interest rates have declined slightly since the last monetary policy assessment. The yield on ten-year Confederation bonds, which had already dipped temporarily into negative territory in the first half of the year, was negative in August and September. The yield curve of Confederation bonds flattened slightly in line with the fall in long-term interest rates.

In September, the Swiss franc traded lower against both the euro and the US dollar than it had done at the time of the June assessment. The Swiss franc exchange rate against the euro was largely unaffected by the turbulence emanating from China. However, both the Swiss franc and the euro strengthened against the US dollar for a time.

Growth in bank lending continued to weaken. Annual growth rates for monetary as well as credit aggregates were in the low single digits. Meanwhile, bank lending continued to grow faster than nominal GDP.

SUMMARY OF MONETARY POLICY SINCE THE LAST ASSESSMENT

Continuation of current monetary policy

At its monetary policy assessment of 18 June 2015, the SNB reaffirmed its continuation of the monetary policy measures announced on 15 January 2015 and decided to leave the target range for the three-month Libor unchanged at –1.25% to –0.25%. It also left unchanged, at –0.75%, the interest rate on sight deposits held by banks and other financial market participants at the SNB which exceed a given threshold.

Furthermore, the SNB underlined its commitment to taking account of the exchange rate situation, and its impact on inflation and economic developments, in formulating its monetary policy. It would remain active in the foreign exchange market to influence monetary conditions as necessary.

Higher sight deposits at the SNB

Since the monetary policy assessment of June 2015, total sight deposits held at the SNB have increased slightly. In the week ending 11 September 2015 (last calendar week before the mid-September assessment), they amounted to CHF 464.3 billion, up by CHF 9.2 billion compared to the calendar week preceding the mid-June assessment (CHF 455.1 billion). Between the two assessments, sight deposits at the SNB averaged CHF 461.7 billion, of which CHF 395.7 billion was accounted for by the sight deposits of domestic banks and the remaining CHF 66.0 billion by other sight deposits.

High level of banks' surplus reserves

Between 20 May 2015 and 19 August 2015, statutory minimum reserves averaged CHF 14.4 billion. Overall, banks exceeded the requirement by some CHF 382.8 billion (previous period: CHF 372.1 billion). Banks' surplus reserves have thus once again increased.

MONEY AND CAPITAL MARKET INTEREST RATES

Money market interest rates virtually unchanged
Money market interest rates have barely moved since the June monetary policy assessment. In mid-September, interest rates on secured (Swiss Average Rates) and unsecured money market transactions (Libor) were close to the interest rate on sight deposits at the SNB of –0.75%. The three-month Libor thus consistently remained close to the middle of the target range (cf. chart 5.1).

Long-term interest rates back in negative territory
The yield on ten-year Confederation bonds, which had already briefly turned negative in the first half of the year, once again dropped below zero at the end of July and remained negative throughout August and September. Mid-September saw the yield at just under –0.1%, which was lower than in mid-June.

This decline principally reflects increased demand for secure investments. Ongoing low inflation also contributed to this dip in Confederation bond yields.

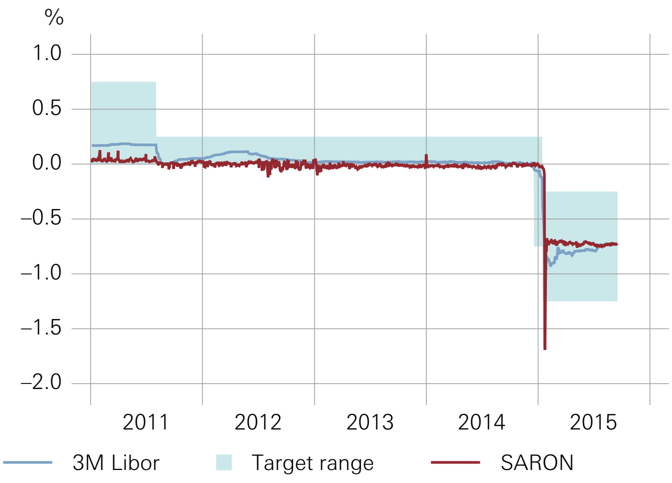
Flatter yield curve
The yield curve for Confederation bonds was flatter in mid-September than in mid-June (cf. chart 5.2), mainly due to the fact that long-term interest rates were lower than they had been during the previous quarter.

Low long-term real interest rates
In mid-September, the estimated long-term real interest rate was approximately 0.2% – lower than in the previous quarter but roughly on a par with the level two or three quarters earlier (cf. chart 5.3).

The real interest rate estimate is based on the development of the ten-year yield on Confederation bonds and the estimated inflation expectations for the same time horizon, determined using a vector autoregressive (VAR) model.

Chart 5.1

MONEY MARKET RATES

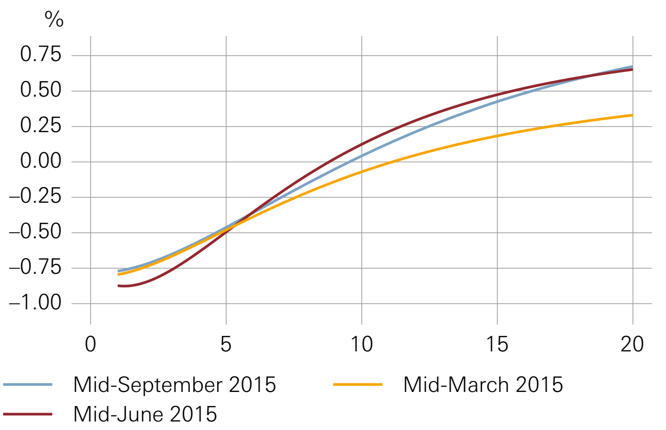


Sources: Bloomberg, SIX Swiss Exchange Ltd, SNB

Chart 5.2

TERM STRUCTURE OF SWISS CONFEDERATION BONDS

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



Source: SNB

Chart 5.3

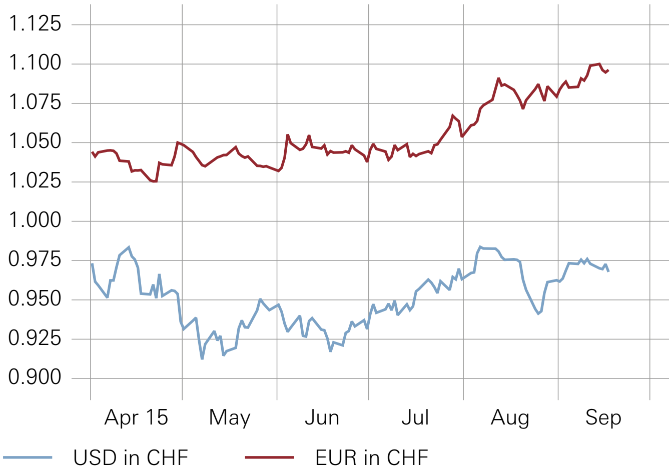
ESTIMATED REAL INTEREST RATE

10-year Confederation bonds
Inflation expectations estimated with VAR model

Source: SNB

Chart 5.4

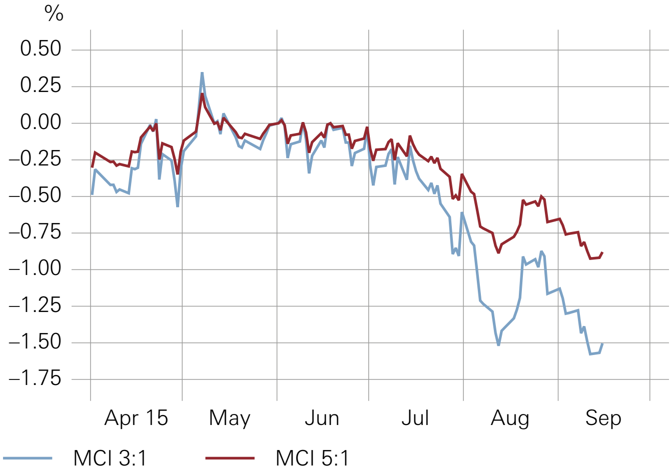
EXCHANGE RATES



Source: SNB

Chart 5.5

MCI NOMINAL



Source: SNB

Chart 5.6

REAL EXTERNAL VALUE OF SWISS FRANC

Export-weighted, January 1999 = 100

Source: SNB

EXCHANGE RATES

Weakening of Swiss franc against euro

The Swiss franc weakened against the euro between mid-July and mid-August (cf. chart 5.4). This was primarily due to the nascent agreement between Greece and its creditors on a new rescue package. In September, the exchange rate stood at CHF 1.10 per euro for a short time. The Swiss franc also weakened against the US dollar between mid-June and mid-August.

Uncertainty among investors, which translated into turbulence on the stock markets, then contributed to another temporary strengthening of the euro and the Swiss franc against the US dollar.

Slightly more expansionary monetary conditions

On an export-weighted basis, the Swiss franc was weaker in mid-September than it had been at the time of the June assessment. With short-term interest rates virtually unchanged, monetary conditions have become slightly more expansionary.

The Monetary Conditions Index (MCI) in chart 5.5 combines changes in the three-month Libor with changes in the nominal export-weighted external value of the Swiss franc to provide a measure of monetary conditions. To take account of uncertainty regarding the relative impact of changes in interest rates and exchange rates, two versions of the index are used, with each version assigning a different weight to the two components. The index is reset to zero at the time of the last monetary policy assessment. Negative MCI values indicate an easing of monetary conditions.

Real external value of Swiss franc at very high level

The real, export-weighted external value of the Swiss franc has decreased slightly since the June monetary policy assessment. As the price level abroad increased more strongly than in Switzerland during this period, the real external value of the Swiss franc fell somewhat more markedly than the nominal value; it nonetheless remains at a very high level (cf. chart 5.6).

STOCK MARKETS

Stock market setback
The Swiss stock market suffered a setback in August as a direct result of turbulence emanating from China.

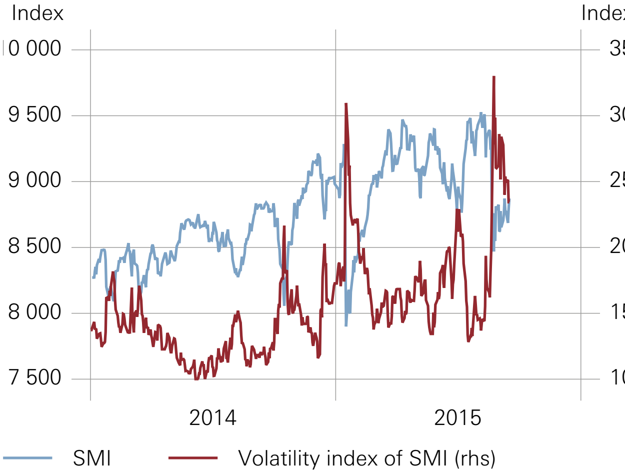
The Swiss Market Index (SMI), which, for a while in early August, was close to its 2007 peak, lost up to 14% at times. The only period in 2015 when the SMI temporarily traded lower still was in the wake of the discontinuation of the minimum exchange rate in January. In mid-September, it was around 2% lower than at the end of 2014 (cf. chart 5.7).

The expected volatility of the SMI, which is calculated using option prices, increased considerably in August, even briefly exceeding the level recorded following the discontinuation of the minimum exchange rate in January 2015. In September, the volatility expected by the market decreased again but nevertheless remained relatively high.

All major sectoral indices affected more or less equally
The setback in August 2015 affected all the major sub-indices of the Swiss Performance Index (SPI) in almost equal measure. The movements of four sector sub-indices are shown in chart 5.8, which was indexed at 100 on 14 January 2015 (the day before the discontinuation of the minimum exchange rate). This chart reveals that, overall, the health care, consumer goods and industrials sectoral indices have all followed a very similar trajectory since mid-January; financials performed better over this period.

Chart 5.7

SHARE PRICES AND VOLATILITY

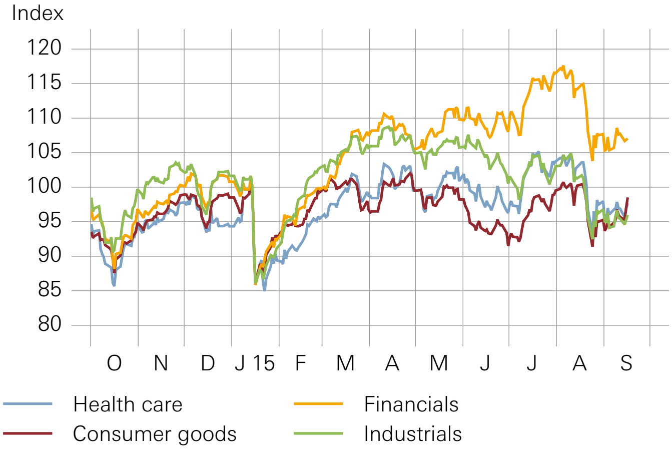


Sources: Bloomberg, Thomson Reuters Datastream

Chart 5.8

SELECTED SPI SECTORS

14 January 2015 = 100



Source: Thomson Reuters Datastream

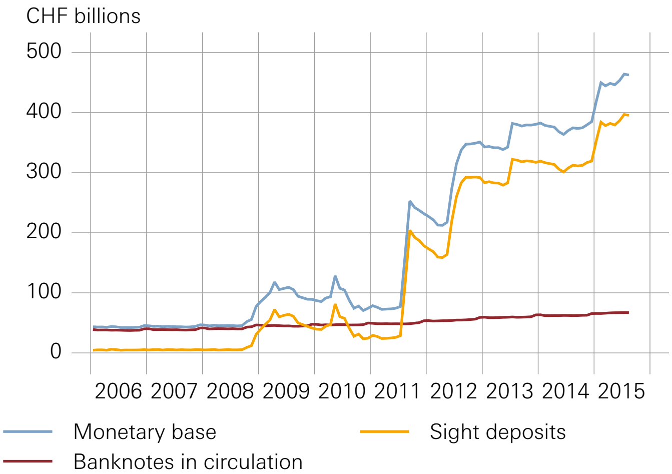
MONETARY AND CREDIT AGGREGATES

Broad monetary aggregates virtually unchanged
The monetary base, which is composed of banknotes in circulation plus sight deposits of domestic banks with the SNB, increased by CHF 16.4 billion between May and August (cf. chart 5.9), principally due to the rise in sight deposits. Banknotes in circulation increased only slightly over the same period.

The broader monetary aggregates, which measure money stocks held by the domestic non-banking sector, also changed little between May and August (cf. chart 5.10). In August, the M1 monetary aggregate (notes and coins in circulation, sight deposits and transaction accounts) was up by 0.5% year-on-year. Over the same period, M2 (M1 plus savings deposits) rose by 0.9% and M3 (M2 plus time deposits) rose by 1.4% (cf. table 5.1).

Chart 5.9

MONETARY BASE

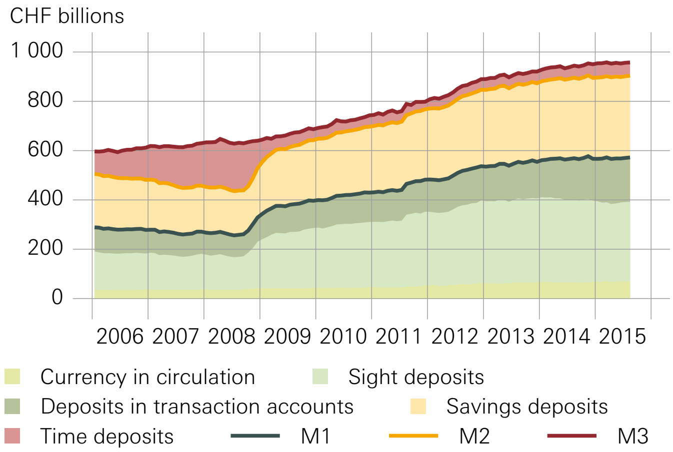


Source: SNB

Chart 5.10

MONETARY AGGREGATES

Including PostFinance



Source: SNB

Table 5.1

MONETARY AGGREGATES AND BANK LOANS

Year-on-year change in percent

	2014	2014 Q3	Q4	2015 Q1	Q2	2015 June	July	August
M1 [1]	**3.7**	**3.0**	**2.7**	**1.0**	**0.2**	**0.8**	**0.7**	**0.5**
M2 [1]	**3.4**	**3.0**	**2.8**	**1.6**	**0.9**	**1.2**	**1.1**	**0.9**
M3 [1]	**3.8**	**3.4**	**3.4**	**2.4**	**1.7**	**2.1**	**1.9**	**1.4**
Bank loans, total [2, 4]	**4.1**	**4.4**	**3.5**	**2.5**	**1.6**	**1.4**	**1.3**	
Mortgage claims [2, 4]	3.9	3.8	3.6	3.6	3.5	3.3	3.3	
Households [3, 4]	3.5	3.4	3.3	3.5	3.5	3.5	3.4	
Private companies [3, 4]	4.8	4.5	4.4	3.9	3.7	3.4	3.0	
Other loans [2, 4]	5.3	8.0	2.6	–2.9	–7.3	–8.2	–8.2	
Secured [2, 4]	4.3	8.8	8.0	4.2	0.5	0.0	–0.8	
Unsecured [2, 4]	6.0	7.5	–1.0	–7.2	–12.3	–13.4	–13.1	

1 On 26 June 2013, PostFinance was granted a banking licence. The growth rates are based on monetary aggregate figures adjusted retroactively for the period January 2005 to May 2013 (cf. *Monthly Statistical Bulletin*, table B2a online, and 'Information on SNB statistics', August 2013, p. III).
2 Monthly balance sheets.
3 Credit volume statistics.
4 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

Slowdown in mortgage lending growth

In the second quarter of 2015, banks' mortgage claims, which make up roughly 85% of all domestic bank lending, were up 3.5% on the same period a year earlier, having increased by 3.6% year-on-year in the first quarter of 2015. Growth in mortgage lending thus continued to slow, in line with a trend that has been underway for over three years now (cf. chart 5.11). The breakdown by borrower indicates that growth in mortgage lending to households remained constant, while growth in mortgage lending to private companies declined (cf. table 5.1).

The weaker growth in mortgage lending may be attributed to various measures taken since 2012 to restrain the banks' risk appetite and strengthen their resilience. These include the banks' own self-regulation measures, which subject mortgage lending to stricter minimum requirements. Furthermore, at the proposal of the SNB, the Federal Council activated the countercyclical capital buffer in 2013 and increased it in 2014. This instrument requires the banks to back their mortgage loans on residential property with additional capital.

Decline in other loans

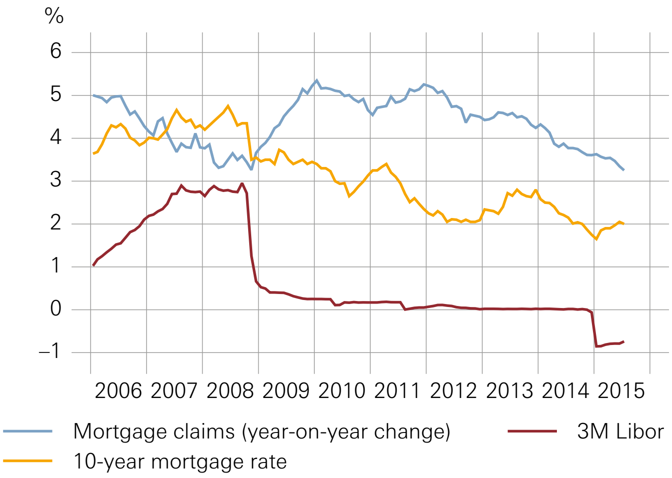
Other loans are significantly more volatile than mortgage loans. In the second quarter of 2015, other loans were 7.3% below their year-back level. Since 2008, the trend for other loans has remained relatively flat. The decline in unsecured other loans recorded over this period is largely offset by the rise in secured other loans (cf. chart 5.12).

Growth in lending by sector

The fact that both households and non-financial companies have benefited from the favourable financing conditions of recent years is reflected in a continuous rise in bank loans (cf. chart 5.13). At the end of July 2015, loans to households were up by CHF 21.9 billion (3.1%) and loans to non-financial companies advanced by CHF 3.0 billion (1.1%) year-on-year. By contrast, loans to financial companies, which exhibited greater volatility at significantly lower volumes, declined by CHF 11.3 billion (–18.9%).

Chart 5.11

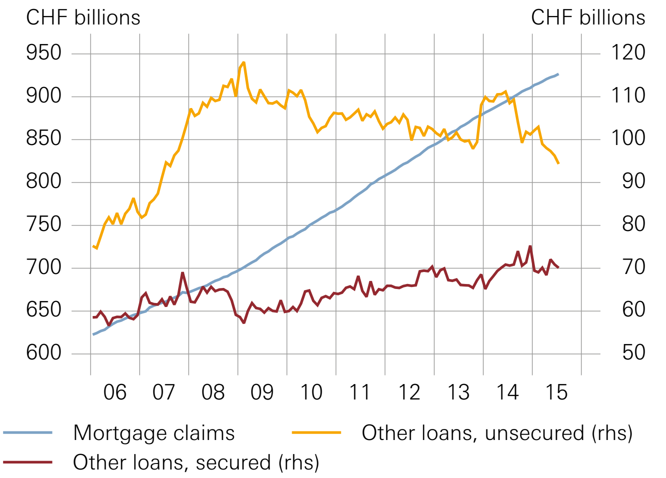
MORTGAGE CLAIMS AND 3M LIBOR



Sources: Bloomberg, SNB

Chart 5.12

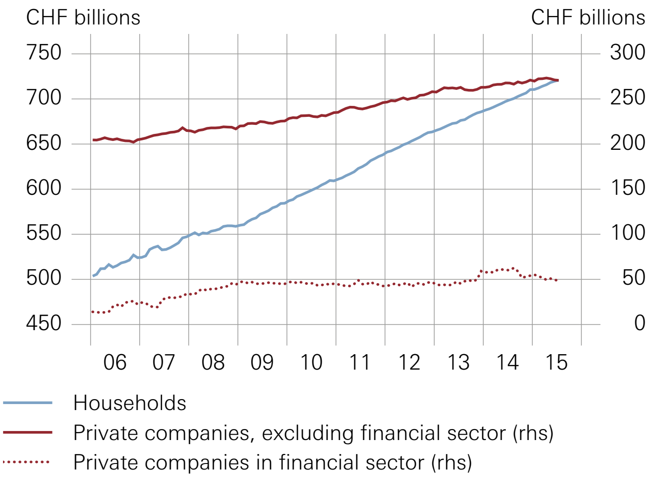
MORTGAGE CLAIMS AND OTHER LOANS



Source: SNB

Chart 5.13

LOANS TO HOUSEHOLDS AND COMPANIES



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 September 2015

Third quarter of 2015

The Swiss National Bank's delegates for regional economic development are constantly in touch with companies from different areas of the economy. This report is based on discussions conducted from mid-July to early September 2015 with 182 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	**Delegates**
Central Switzerland	Walter Näf
Eastern Switzerland	Urs Schönholzer
Geneva	Jean-Marc Falter
Italian-speaking Switzerland	Fabio Bossi
Mittelland	Martin Wyss
Northwestern Switzerland	Daniel Hanimann
Vaud-Valais	Aline Chabloz
Zurich	Markus Zimmerli

SUMMARY

According to this survey, the economy showed weak signs of recovery in the quarter under review following the sharp appreciation of the Swiss franc due to the discontinuation of the minimum exchange rate on 15 January 2015. Recent exchange rate developments helped to ease the situation somewhat, as did the measures implemented by the entrepreneurs. These measures primarily resulted in cheaper conditions for procurement in Switzerland and abroad (cf. the separate exchange rate survey, pp. 32–37). Overall, real turnover was maintained at the level of the previous quarter; nominal turnover, however, continued to decline because of developments in selling prices. Margins were therefore still strained for many companies.

The outlook for real turnover growth in the months ahead has improved marginally. Companies are focusing their efforts on bringing margins back to a sustainable level. The headcount will continue to decrease slightly in the manufacturing industry, whereas investment activity is likely to remain at the current level overall.

BUSINESS ACTIVITY

Marginal improvement

In manufacturing, real turnover is roughly unchanged against the previous quarter, but there has been a marginal improvement. In nominal terms, however, turnover is in many instances still far lower than in the previous period because of low sales prices.

The machinery industry continues to register lower real turnover against the previous quarter. Plastics processing companies generated slightly higher real turnover, as did the food industry. The pharmaceutical industry is showing robust growth. The watchmaking industry, notably its suppliers, has experienced a noticeable slowdown.

As to foreign trade, sales to the US remain dynamic. An increase in demand from some European countries is also becoming more apparent, with Germany again as the driving force. Demand from the Arab region is also holding up well. The automotive industry is still a major contributor, as is the medtech industry. Many industries are registering a marked slowdown in business activity with Russia, but also with India and Brazil. Signals from China are mixed depending on the industry concerned.

Construction recorded a quarter-on-quarter decline in seasonally adjusted turnover, which still remains at a high level. This effect was observed both in structural and civil engineering. By contrast, momentum in the finishing trade is still strong.

In the services sector, real turnover is slightly higher than in the previous quarter. The picture remains mixed between sectors: higher turnover was generated by the transport industry, car dealers, information and communications technology (ICT) and, in some cases, the hotel industry. Passenger transport companies attribute this development mainly to the good weather. In the hotel industry, the large number of Asian tour groups coupled with higher domestic demand has helped to dampen the negative effects of the strong Swiss franc.

Retailers registered a noticeable drop in turnover. They attribute this development to cross-border shopping, among other factors. Shopping centres close to the border continue to report that they are empty at the weekend.

CAPACITY UTILISATION

The companies surveyed again rated production capacity as marginally underutilised overall. A total of 40% of responding companies assessed their capacity utilisation as lower than usual.

In manufacturing, almost half of the responding companies reported an underutilisation of capacity, with most industries being affected. Machinery manufacturers, the metals processing industry and some of the plastics processing firms considered their production capacity to be significantly underutilised. The machinery industry, in particular, has thus experienced a marked deterioration compared to the previous quarter.

In construction, utilisation of technical capacity is higher than normal overall, despite occasional signs of cooling; this is particularly true for the finishing trade.

In the services sector, most industries recorded a slight to significant underutilisation of infrastructure (primarily office and retail space as well as transport capacity). Passenger transport business was an exception, as it benefited from high numbers of day tourists taking advantage of the good weather.

DEMAND FOR LABOUR

Demand for staff unchanged
Overall, staff numbers are currently considered more or less adequate, however, manufacturing did indicate that staff numbers are slightly too high. This is particularly true for producers of electrical appliances and for the plastics processing industry. In construction, staff numbers are adequate. Within the services sector, headcounts in the catering and retail industries are slightly too high. By comparison, ICT companies tend to be looking for more staff.

The discontinuation of the minimum exchange rate against the euro has triggered a variety of personnel measures including hiring freezes and longer working hours for the same pay. A few companies laid off staff, with temporary employees being affected in particular (cf. information contained in the special survey below, pp. 32–37).

PRICES, MARGINS AND EARNINGS SITUATION

Margins still under severe pressure
The overall margin situation has improved somewhat compared with the previous quarter. However, margins remain under severe pressure in all three sectors of the economy. The pressure on prices triggered by the discontinuation of the minimum exchange rate is being felt. Over the past few months, many companies have lowered prices in order to remain competitive. In some instances, the measures implemented are already having an effect, and many industries are seeing signs of a recovery in margins. Among other factors, this can be attributed to the significant expansion of procurement abroad. By contrast, only rarely is there room for price increases.

A total of 55% of the respondent companies assessed their margins as being lower than usual, half of them even as significantly lower. Almost 30% of companies reported that margins were within the normal range. These percentages have not changed from the previous quarter. Numerous measures are currently being implemented to counter the tougher competitive situation (cf. results of the special survey below).

With the exception of the pharmaceutical industry, profit margins were judged to be lower or even significantly lower than usual in all branches of manufacturing.

Companies in the services sector also rated margins as narrower than usual overall. Wholesalers and catering companies had to contend with particularly narrow margins. By contrast, the banks' margin situation has improved somewhat.

OUTLOOK

Slightly brighter outlook
Uncertainty about the future development of the economy remains high. Nevertheless, real turnover is expected to increase marginally overall in the months ahead in all three sectors of the economy. The slightly improved economic situation in Europe and the more favourable exchange rate conditions against the euro and the US dollar will contribute to this development. Respondents in the services sector are the most confident in terms of the expected development of real turnover.

In all sectors of the economy, purchase and sales prices are expected to decline further, though to a lesser extent than in the previous quarter.

As to employment plans, the survey respondents in manufacturing anticipate further slight staff reductions, whereas the services sector and construction industry expect no changes.

Many companies imposed an immediate freeze on investment following the discontinuation of the minimum exchange rate. Overall, investment plans for the next twelve months show no signs of recovery. Only a few of the plans that were put on hold are now being implemented.

Respondents' inflation expectations – measured by the consumer price index – are still within negative territory, at –0.4% over the short term (6–12 months), compared to around –0.6% in the last survey. Expectations over the longer-term horizon of 3–5 years are 0.6%, as against 0.5% in the last survey.

Respondents' main concern is still the tight margin situation. At the same time, they are perceptibly relieved that the exchange rate situation has eased somewhat. Some of the discussions revealed fears that further effects from the strength of the Swiss franc may yet be felt in the economy over the coming months. In manufacturing, respondents are concerned about an accelerated and irreversible structural change. The implementation of the initiative against mass immigration has again shifted somewhat more prominently into the focus of entrepreneurs. Criticism was levelled at excessive regulation and an increasing bureaucratic burden. With regard to the international environment, the recent weak growth in China has raised some uncertainty.

Exchange rate survey: Effects of Swiss franc appreciation and company reactions

SNB regional network

Report for the attention of the Governing Board of the Swiss National Bank for its quarterly assessment of September 2015

In the economic survey for the third quarter, which was carried out from mid-July to the beginning of September 2015, delegates from the SNB's regional network also systematically raised the exchange rate issue with companies, with the aim of quantifying the effects of the Swiss franc appreciation. A total of 182 companies took part in the survey. The selection of companies differs from one quarter to the next. It reflects the industrial structure of the Swiss economy, based on the composition of GDP (excluding agriculture and public services).

The discontinuation of the EUR/CHF minimum exchange rate on 15 January 2015 presents a great challenge for many companies. For this reason, the delegates from the SNB's regional network once again conducted a special survey on the topic in the third quarter.

Overall, the results of this survey were similar to those in the previous quarter. What is more, the further forward we move from the discontinuation of the minimum exchange rate, the harder it becomes to separate the effects relating to these measures from other effects. The SNB will therefore discontinue the special exchange rate survey as of the fourth quarter. The delegates will of course continue to broach exchange rate concerns as part of their standard survey discussions.

OVERALL RESULTS OF THE SURVEY

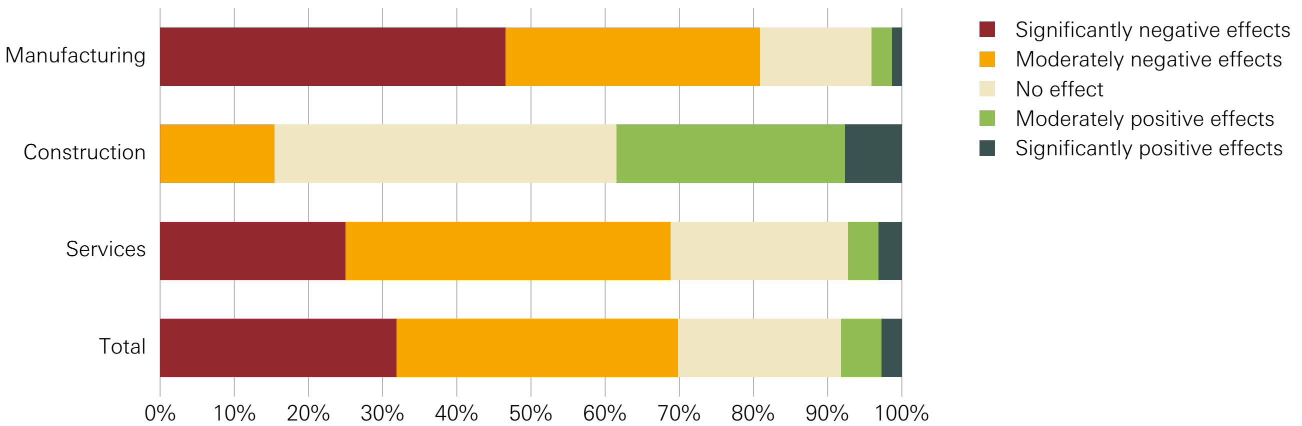
As is evident from chart 1, 70% of respondents report experiencing negative effects from the appreciation of the Swiss franc (32% significantly and 38% moderately negative). A total of 22% of companies said they had not felt any significant effect on their business activities from the Swiss franc appreciation. Positive effects have been experienced by the remaining 8% of companies included in the survey. However, the different sectors of the economy are very differently affected by the appreciation.

Manufacturing has most commonly experienced negative effects from the strength of the Swiss franc (81%). In the services sector, this figure is 69%. In construction, only 15% of the respondent companies reported experiencing negative effects, with just under 40% benefiting from the strong Swiss franc through increased purchasing power. It should be noted that industrial companies with construction-related activities are included under manufacturing in this survey.

Chart 1

EFFECTS OF CHF APPRECIATION

182 companies



Source: SNB

NEGATIVE EFFECTS – WHERE AND HOW?

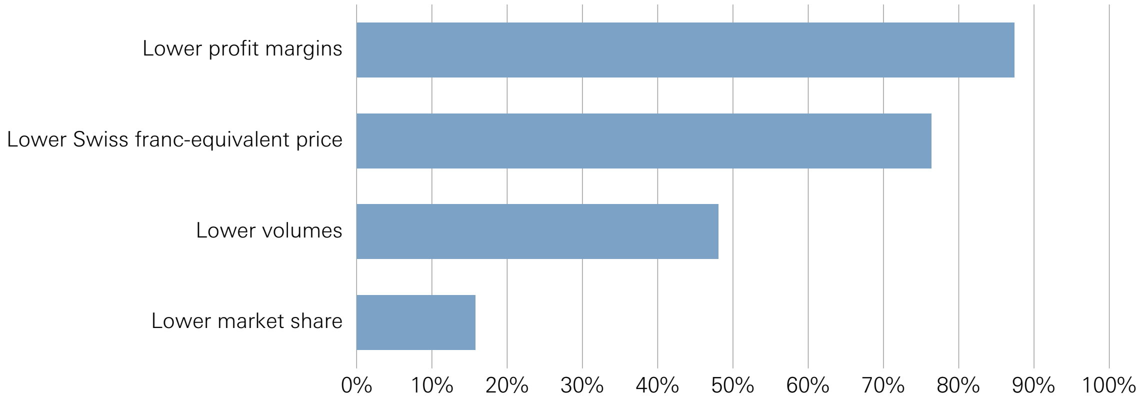
In total, 127 companies (70%) report moderate or significantly negative effects from the appreciation of the Swiss franc. Chart 2 shows the form these negative effects are taking. The negative effects are primarily felt in the form of reduced margins and lower sales prices (in Swiss francs and Swiss franc-equivalent prices). On the domestic market, roughly 90% of the negatively affected companies cite this as the reason; on the export markets, around 75%.

A decline in sales volumes is given as the third most important factor (almost 50% of the negatively affected companies). Domestic sales are particularly affected. It is also becoming evident that in 15% of the cases market share is being lost because of the unfavourable competitive situation.

Chart 2

NEGATIVELY AFFECTED COMPANIES: EFFECTS OF CHF APPRECIATION

127 companies, multiple answers possible



Source: SNB

NEGATIVE EFFECTS – HOW ARE COMPANIES REACTING?

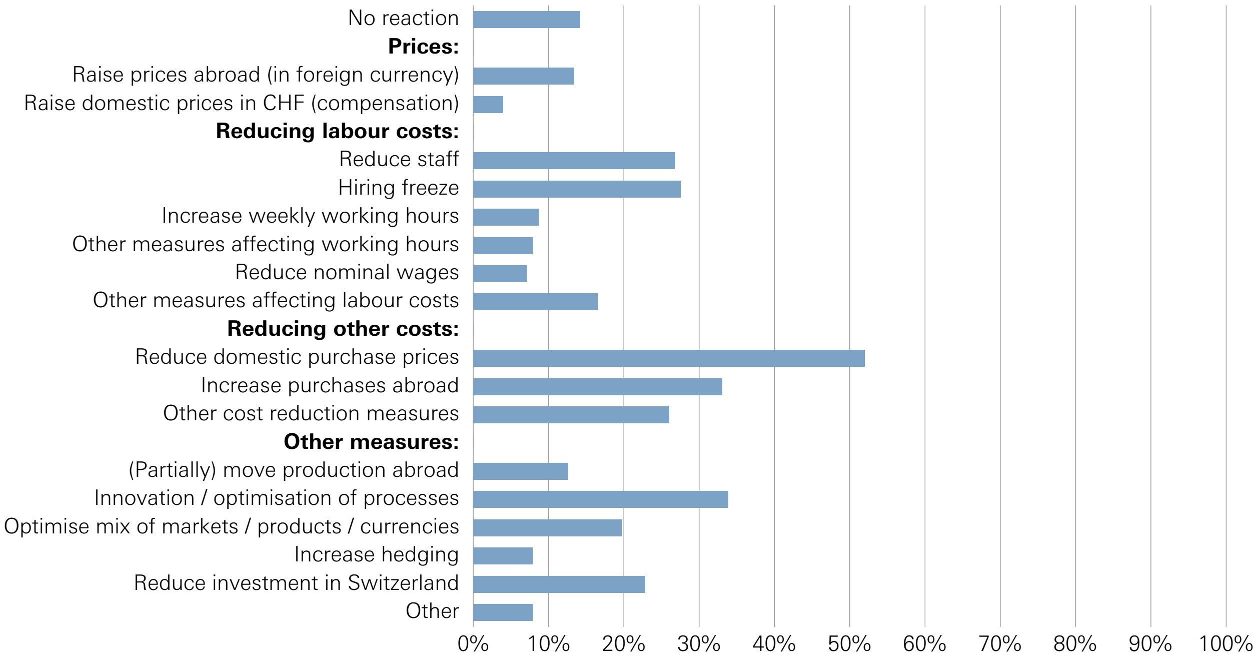
Companies were also asked about the measures they had already taken to counter the negative effects of the Swiss franc appreciation and the erosion of margins. Chart 3 shows the range of these measures. Roughly 85% of the negatively affected companies have opted to take measures. The measures reported most frequently were reducing purchase prices in Switzerland (52% of companies), taking steps to optimise processes and innovate (34%) and increased purchasing abroad (33%), with some companies increasing the share of their purchases abroad massively.

Labour costs are mainly being cut by implementing hiring freezes (28%) or reducing staff numbers (27%). Just under 10% of companies surveyed have increased working hours. A reduction of investment in Switzerland as well as optimising the mixture of markets, products and currencies are among the further strategies being implemented. Of the companies negatively affected by the strong Swiss franc, 13% are moving parts of their production abroad.

Chart 3

NEGATIVELY AFFECTED COMPANIES: MEASURES TAKEN IN REACTION TO CHF APPRECIATION

127 companies, multiple answers possible



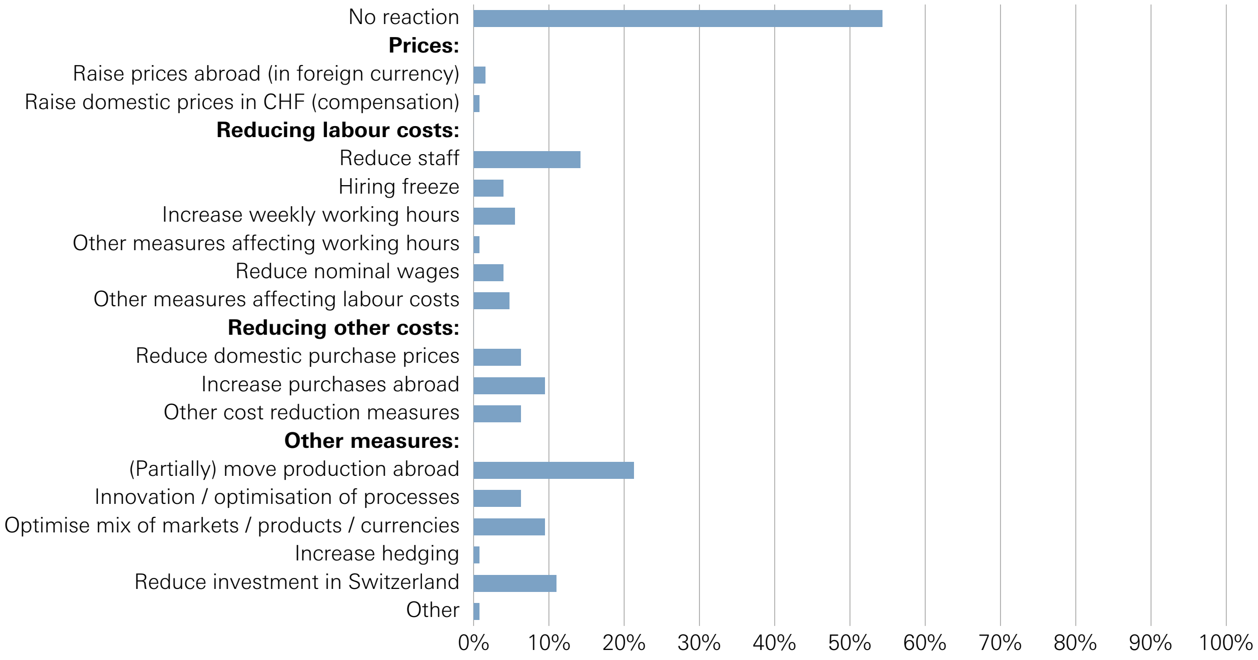
Source: SNB

Chart 4 shows the measures still being considered by negatively affected companies. Approximately half of these companies indicated that, despite the negative impact, they are not planning to evaluate any measures in future. For those companies which are evaluating measures, the main measure under discussion is the partial relocation of production processes abroad. Reducing staff numbers, reducing investment in Switzerland and increasing purchases abroad are also being considered.

Chart 4

NEGATIVELY AFFECTED COMPANIES: MEASURES BEING CONSIDERED DUE TO CHF APPRECIATION

127 companies, multiple answers possible



Source: SNB

NO EFFECTS – WHAT ARE THE REASONS?

As is to be expected, the 22% of companies that report experiencing no significant effects from the Swiss franc appreciation on their business activity mainly consist of companies not exposed to exchange rate movements (in approximately 60% of cases). However, exchange rate effects can also be neutralised, through positive and negative factors offsetting each other (approximately 30%), or through hedging transactions conducted before the discontinuation of the minimum exchange rate (5%).

POSITIVE EFFECTS – WHERE AND HOW?

Of all respondent companies, 8% experienced minimal or even significantly positive effects from the appreciation of the Swiss franc. The greater part of the positive effects came in the form of lower input costs and/or improved profit margins. Just under half of the companies experiencing positive effects mentioned larger sales volumes and, in one-quarter of cases, more favourable conditions for investing as well as for research and development.

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.

At its quarterly assessment of 17 September 2015, the SNB leaves its target range for the three-month Libor unchanged at between –1.25% and –0.25% and the interest rate on sight deposits with the SNB at –0.75%. The SNB reaffirms that it will remain active in the foreign exchange market as necessary, in order to take account of the impact of the exchange rate situation on inflation and economic developments. In the SNB's view, the Swiss franc is still significantly overvalued, despite a slight depreciation. The negative interest rates in Switzerland and the SNB's willingness to intervene as required in the foreign exchange market serve to ease the pressure on the franc.

September 2015

At its quarterly assessment of 18 June 2015, the SNB leaves its target range for the three-month Libor unchanged at between –1.25% and –0.25% and the interest rate on sight deposits with the SNB at –0.75%. Negative interest rates in Switzerland help to make holding investments in Swiss francs less attractive. In the view of the SNB, the Swiss franc is significantly overvalued. The SNB reaffirms that it is taking account of the exchange rate situation and its impact on inflation and economic developments. It therefore remains active in the foreign exchange market, as necessary, to influence monetary conditions.

June 2015

On 22 April 2015, the SNB reduces the group of sight deposit account holders that are exempt from negative interest; the only exemptions now are those of the central Federal Administration and the compensation funds for old age and survivors' insurance, disability insurance and the fund for loss of earned income (AHV/AVS; IV/AI; EO/APG).

April 2015

At its quarterly assessment of 19 March 2015, the SNB leaves the target range for the three-month Libor unchanged at between –1.25% and –0.25%. The interest rate on sight deposits with the SNB remains at –0.75% and the exemption thresholds remain unchanged. Negative interest helps to make it less attractive to hold investments in Swiss francs. In the view of the SNB, the Swiss franc is significantly overvalued overall and should continue to weaken over time. The SNB affirms that it will continue to take account of the exchange rate situation and its impact on inflation and economic developments. It will therefore remain active in the foreign exchange market, as necessary, in order to influence monetary conditions.

March 2015

On 15 January 2015, the SNB discontinues the minimum exchange rate of CHF 1.20 per euro. At the same time, it lowers the interest rate on sight deposit account balances at the SNB that exceed a given exemption threshold by 0.5 percentage points, to –0.75%, with effect from 22 January 2015. The target range for the three-month Libor now amounts to between –1.25% and –0.25% (previously between –0.75% and 0.25%). The reduction in interest rates is aimed at ensuring that the discontinuation of the minimum exchange rate does not lead to an inappropriate tightening of monetary conditions. The SNB stresses that it will continue to take account of the exchange rate situation in future. If necessary it will therefore remain active in the foreign exchange market.

January 2015

On 18 December 2014, the SNB announces that it will impose an interest rate of –0.25% on sight deposit account balances at the SNB from 22 January 2015. Negative interest will be levied on balances exceeding a given exemption threshold. The SNB's aim is to take the three-month Libor into negative territory. The target range for the three-month Libor now amounts to between –0.75% and 0.25% (previously 0–0.25%). The introduction of negative interest rates makes it less attractive to hold Swiss franc investments, and thereby supports the minimum exchange rate.

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