



Quarterly Bulletin
3/2016 September

SCHWEIZERISCHE NATIONALBANK
BANQUE NATIONALE SUISSE
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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 September 2016.

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 15 September 2016') is an excerpt from the press release published following the assessment.

This report is based on the data and information available as at 15 September 2016. 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 15 September 2016

Swiss National Bank leaves expansionary monetary policy unchanged

The Swiss National Bank (SNB) is maintaining its expansionary monetary policy. Interest on sight deposits at the SNB is to remain at -0.75% and the target range for the three-month Libor is unchanged at between -1.25% and -0.25% . At the same time, the SNB will remain active in the foreign exchange market, as necessary. The negative interest rate and the SNB's willingness to intervene in the foreign exchange market are intended to make Swiss franc investments less attractive, thereby easing upward pressure on the currency. The Swiss franc is still significantly overvalued. The SNB's expansionary monetary policy is aimed at stabilising price developments and supporting economic activity.

The new conditional inflation forecast has been revised slightly downwards compared to the June forecast (cf. chart 1.1). Up to the first quarter of 2017, the path of inflation remains almost the same. Thereafter, the slightly less favourable global economic outlook dampens inflation in Switzerland. For 2016, the inflation forecast remains unchanged at -0.4% . For 2017, the SNB expects inflation of 0.2% , compared to 0.3% forecast in the last quarter, while for 2018, the forecast has fallen from 0.9% to 0.6% (cf. table 1.1). The conditional inflation forecast

is based on the assumption that the three-month Libor remains at -0.75% over the entire forecast horizon.

The gradual recovery of the global economy continued in the second quarter. In the US, economic activity was driven mainly by strong consumer demand, and labour market developments continued to be favourable. In European countries, economic performance varied. In France and Italy, it stagnated, whereas Germany, Spain and the UK once again saw healthy growth. The Chinese economy, too, expanded robustly on the back of monetary and fiscal stimulus measures. Overall, international growth was principally driven by domestic demand and the services sector. By contrast, global manufacturing and trade remained subdued.

The SNB still expects the moderate growth in the global economy to sustain over the coming quarters. However, the vote for the UK to leave the European Union has caused considerable uncertainty and makes an assessment of the global economic outlook more difficult. The SNB has revised downwards its growth expectations for the UK and the euro area. As regards the global economy, the risks remain to the downside, owing to numerous structural problems.

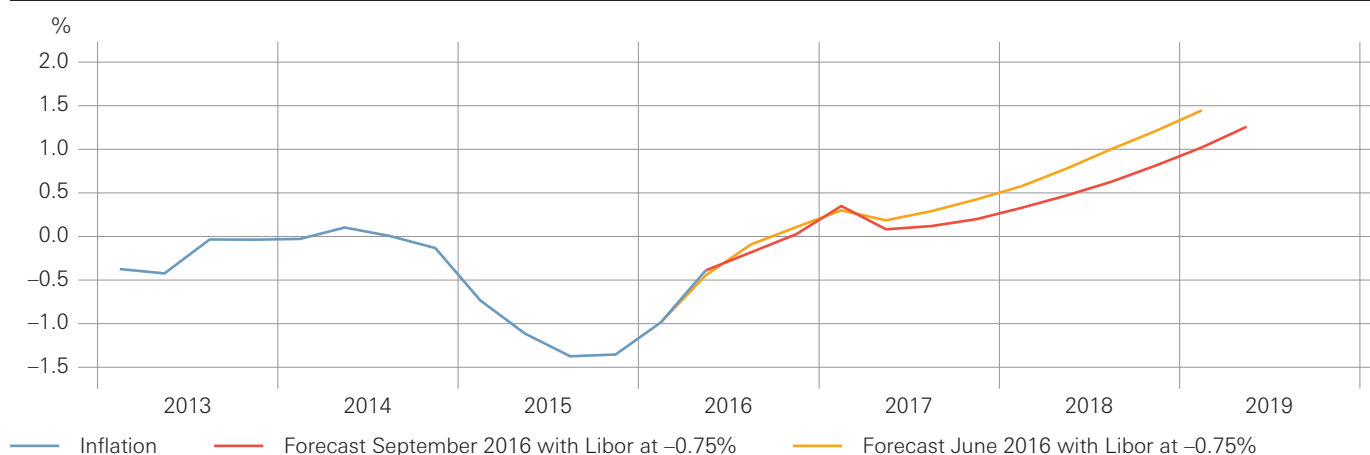
In the second quarter, the Swiss economy posted growth of 2.5% on an annualised basis. Overall, the revised quarterly estimates for GDP suggest a somewhat stronger recovery of the Swiss economy since the middle of last year. Nonetheless, on the whole, capacity utilisation remains unsatisfactory. Moreover, not all industries have benefited equally from the recovery. As a result, margins at a large number of companies continue to be strained.

The SNB is anticipating a continuation of the recovery. In the second half of the year, however, growth is likely to

Chart 1.1

CONDITIONAL INFLATION FORECAST OF SEPTEMBER 2016

Year-on-year change in Swiss consumer price index in percent



Source: SNB

be more modest than in the first half, partly owing to a temporary weakening of growth in Europe. For 2016 as a whole, the SNB now expects growth of approximately 1.5%. The recovery is likely to spread gradually to the labour market. The seasonally adjusted unemployment rate should stabilise over the coming months.

While growth in real estate prices weakened overall in the second quarter, growth in mortgage lending was virtually unchanged compared to the previous quarter. According to the SNB's assessment, imbalances on the mortgage and real estate markets persist. The SNB will continue to monitor developments on these markets closely, and will regularly reassess the need for an adjustment of the countercyclical capital buffer.

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 2016

	2013				2014				2015				2016				2013	2014	2015	
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4				
Inflation	-0.4	-0.4	0.0	0.0	0.0	0.1	0.0	-0.1	-0.7	-1.1	-1.4	-1.4	-1.0	-0.4				-0.2	0.0	-1.1

CONDITIONAL INFLATION FORECAST OF SEPTEMBER 2016

	2016				2017				2018				2019				2016	2017	2018	
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4				
Forecast June 2016, with Libor at -0.75%		-0.4	-0.1	0.1	0.3	0.2	0.3	0.4	0.6	0.8	1.0	1.2	1.4					-0.4	0.3	0.9
Forecast September 2016, with Libor at -0.75%			-0.2	0.0	0.3	0.1	0.1	0.2	0.3	0.5	0.6	0.8	1.0	1.3				-0.4	0.2	0.6

Source: SNB

2 Global economic environment

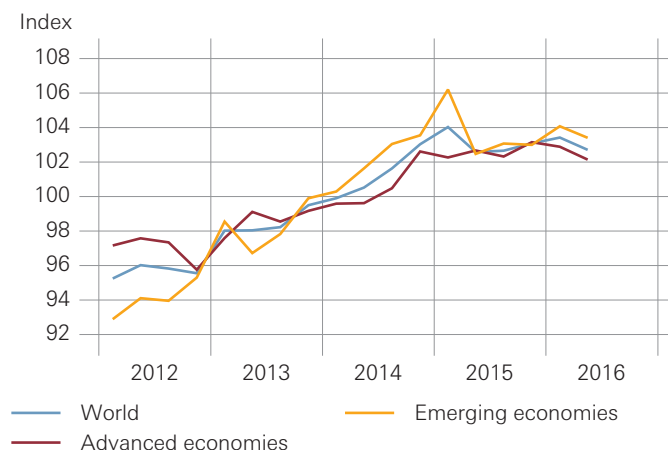
The gradual recovery of the global economy continued in the second quarter. In the US, GDP growth was mainly driven by strong consumer demand. Labour market developments continued to be favourable. In European countries, economic performance varied. In France and Italy it stagnated, whereas Germany, Spain and the UK once again saw healthy growth. The Chinese economy, too, expanded robustly on the back of monetary and fiscal stimulus measures. Overall, international growth continues to be principally driven by domestic demand and the services sector. By contrast, global manufacturing and trade remain lacklustre (cf. chart 2.1).

In its baseline scenario, the SNB continues to expect the modest pace of growth in the global economy to sustain over the coming quarters. However, the vote for the UK to leave the European Union (Brexit) has caused considerable uncertainty. As a result, the SNB has revised downwards its growth expectations for the UK and, to a lesser extent, also for the euro area. As regards the global economy, the risks remain to the downside, owing to numerous structural problems.

Chart 2.1

GLOBAL EXPORTS

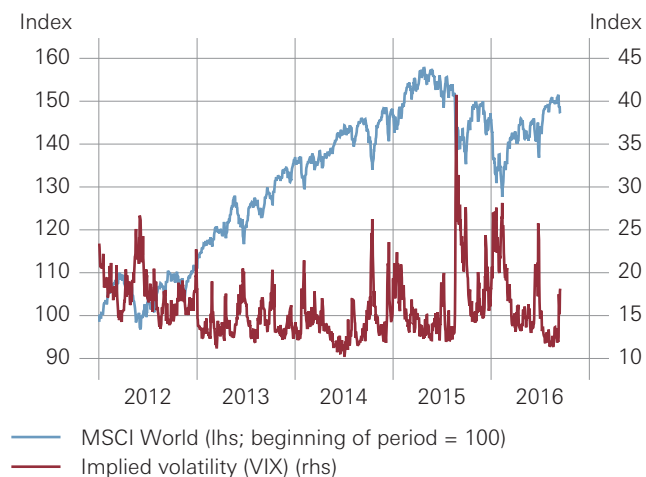
Reporting period average = 100



Sources: CPB, Thomson Reuters Datastream

Chart 2.2

STOCK MARKETS



Source: Thomson Reuters Datastream

Table 2.1

BASELINE SCENARIO FOR GLOBAL ECONOMIC DEVELOPMENTS

	2012	2013	2014	2015	Scenario	
					2016	2017
GDP, year-on-year change in percent						
Global ¹	3.1	3.2	3.4	3.2	3.2	3.5
US	2.2	1.7	2.4	2.6	1.5	2.3
Euro area	-0.9	-0.3	1.1	2.0	1.6	1.4
Japan	1.7	1.4	-0.1	0.6	0.5	1.0
Oil price in USD per barrel						
	111.7	108.7	99.0	52.5	43.0	46.0

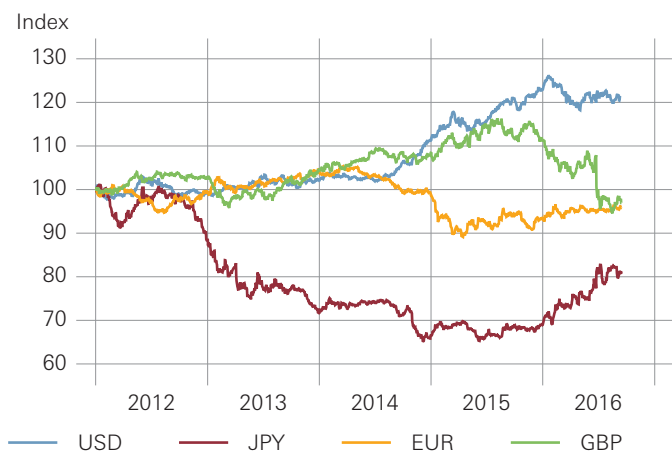
1 PPP-weighted (US, euro area, UK, Japan, China, South Korea, India, Brazil and Russia).

Sources: SNB, Thomson Reuters Datastream

Chart 2.3

EXCHANGE RATES

Trade-weighted, beginning of period = 100



Source: Thomson Reuters Datastream

Chart 2.4

INTERNATIONAL LONG-TERM INTEREST RATES

10-year government instruments

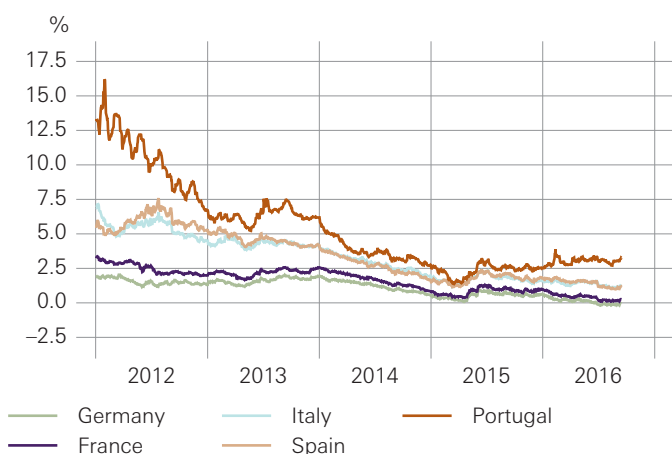


Source: Thomson Reuters Datastream

Chart 2.5

EUROPEAN LONG-TERM INTEREST RATES

10-year government instruments



Source: Thomson Reuters Datastream

The SNB's forecasts for the global economy are based on assumptions about the oil price and the EUR/USD exchange rate. The SNB continues to assume an oil price for Brent crude of USD 46 per barrel and an exchange rate of USD 1.11 to the euro. Both correspond to the 20-day average when the current baseline scenario was drawn up.

INTERNATIONAL FINANCIAL AND COMMODITY MARKETS

Since the last monetary policy assessment, the mood on the global financial markets has fluctuated strongly. The EU referendum in the UK triggered financial market turbulence. The MSCI World Index receded perceptibly for a brief period and the implied volatility of US stocks as measured by option prices (VIX), which serves as an indicator of market uncertainty, once again climbed close to its high level at the beginning of the year (cf. chart 2.2). Yet the willingness of central banks in the advanced economies to ease monetary policy as necessary, as well as market expectations that monetary policy would remain expansionary for some time, helped to contain these fluctuations. The VIX normalised within a few days after the vote and share prices recovered. As a result of a change in market expectations regarding monetary policy in the US, the VIX rose again somewhat at the beginning of September.

On the foreign exchange markets, the euro and the US dollar trended sideways on a trade-weighted basis, while the yen continued to appreciate, exceeding the year-back level by approximately 18% in mid-September. By contrast, the pound sterling depreciated significantly after the Brexit decision (cf. chart 2.3). Yields on long-term government bonds in the advanced economies presented an uneven picture. In the US, they trended sideways; in the euro member states, they fell slightly, with yields on ten-year German government bonds sliding into negative territory for the first time. In Japan, yields on long-term government bonds were negative. However, after the Japanese central bank eased monetary policy at the end of July, they increased significantly, as markets had expected more comprehensive measures (cf. charts 2.4 and 2.5).

On the commodity markets, oil prices came under pressure at times, after having risen considerably in the first half of the year. Starting in August, however, they recovered amid speculation about oil-producing countries curbing the oil supply. As a result of tighter supply and increasing demand from China, prices for industrial metals recovered (cf. chart 2.6).

US

In the wake of the annual revision of the national accounts, average economic growth in the US for the last three years was somewhat higher than previously assumed.

Nonetheless, in the first half of 2016, GDP growth lost momentum. GDP expanded by 1.1% in the second quarter (cf. chart 2.7). The sluggish performance mainly reflected a decline in equipment and construction investment and a renewed reduction in inventories. However, growth was supported by a significant expansion of consumer spending since households reduced their savings. Despite the subdued growth rates in the first half of the year, momentum on the labour market remained positive. Sound growth in employment continued and the unemployment rate was 4.9% in August (cf. chart 2.10). There is almost full employment.

Supported by the recovery in oil prices and the stabilisation of the US dollar, corporate investment in energy and other sectors should pick up in the second half of the year, thereby contributing to sound economic growth. Business indicators in manufacturing have improved somewhat and industrial output improved again in June and July. Owing to weak GDP growth in the second quarter, the SNB has lowered its growth forecast for 2016 to 1.5%; for 2017, the forecast remains unchanged, at 2.3% (cf. table 2.1).

Under the influence of oil prices, the annual inflation rate as measured by the consumer price index fell slightly to 0.8% in July (cf. chart 2.11). Inflationary pressure emanating from the labour market is gradually increasing, however. In addition, various measures of core inflation suggest that inflation is approaching the target set by the US Federal Reserve. It has made no adjustments to its monetary policy since raising its target range for the federal funds rate last December. Global risks and weaker GDP development have kept the Federal Reserve from making any further interest rates moves. Markets currently expect that there is roughly a 50% chance of the Federal Reserve lifting key rates further this year.

Chart 2.6

COMMODITY PRICES

Beginning of period = 100

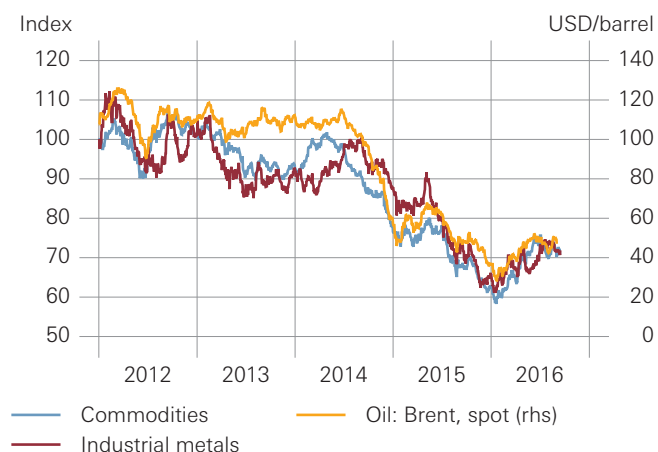


Chart 2.7

REAL GDP: ADVANCED ECONOMIES

Change from previous period

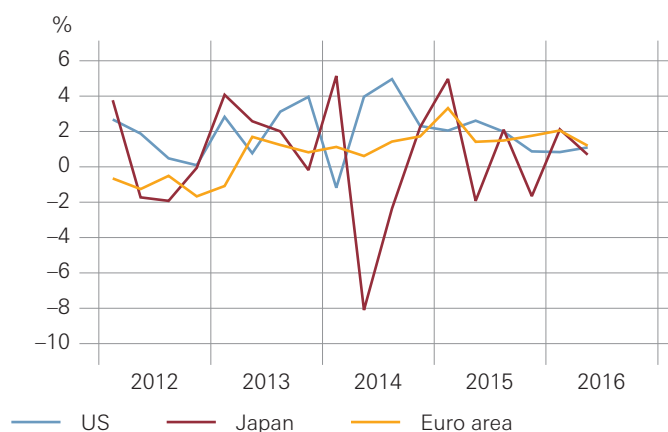


Chart 2.8

REAL GDP: EMERGING ECONOMIES

Change from previous period

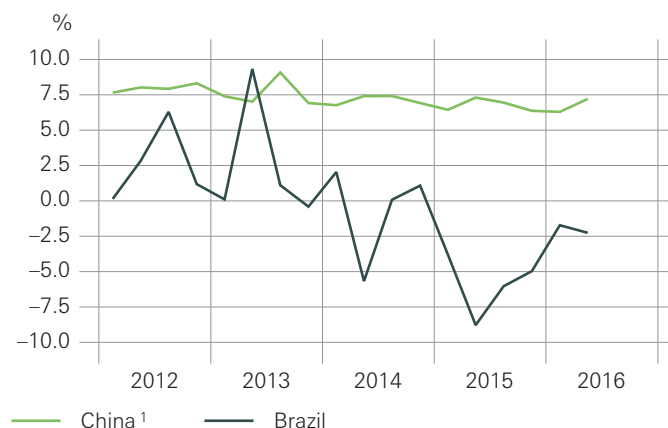
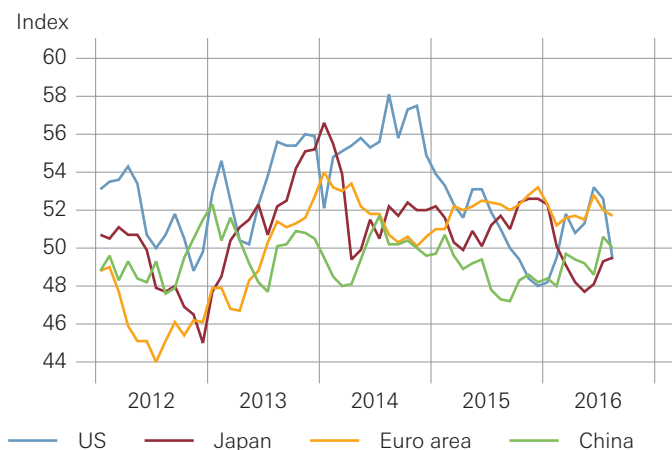


Chart 2.9

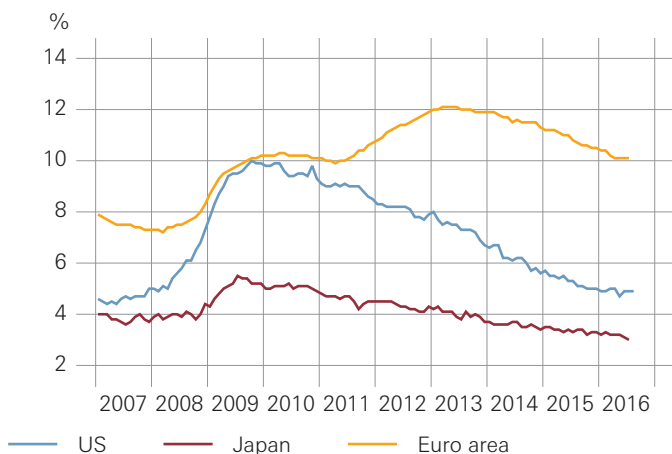
PURCHASING MANAGERS' INDICES (MANUFACTURING)



Source: Markit Economics Ltd 2009; all rights reserved

Chart 2.10

UNEMPLOYMENT RATES

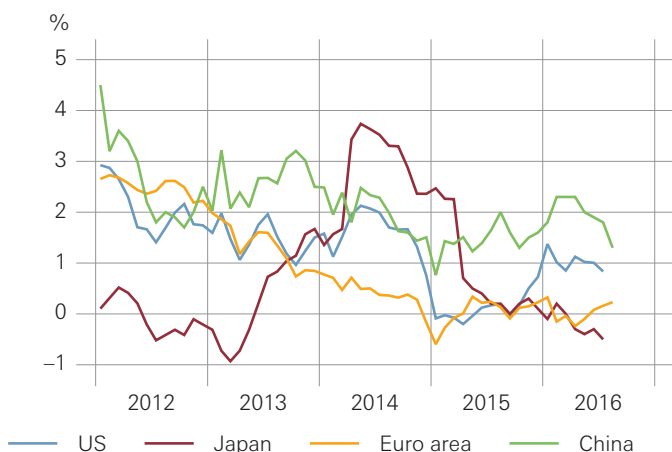


Source: Thomson Reuters Datastream

Chart 2.11

CONSUMER PRICES

Year-on-year change



Source: Thomson Reuters Datastream

EURO AREA

In the euro area, GDP grew by 1.2%, after 2.1% in the previous quarter (cf. chart 2.7). Growth was mainly supported by consumer spending and exports, while investment stagnated. Germany and Spain remained the driving forces among the large member countries, while economic performance stagnated in France and Italy. Unemployment in the euro area continued to fall despite the modest growth.

Supported by expansionary monetary policy, the economic recovery looks set to continue in the euro area. Numerous factors, however, continue to cloud growth prospects. These include concerns surrounding the banking sector in Italy as well as the difficult political situation in some member countries. Another source of concern is the impact of the UK vote to leave the EU. As a result, growth prospects for the euro area have become more uncertain and will be influenced by the progress of the UK's negotiations with the EU. In the short term, a dampening effect on investment is to be expected. In addition, exports to the UK are likely to suffer as a result of the weaker pound sterling and the subdued economic outlook for the UK. The SNB continues to expect GDP growth of 1.6% for the euro area in 2016, but is revising its forecast for 2017 downwards to 1.4%.

Consumer price inflation moved back into positive territory in June, edging up to 0.2% by August (cf. chart 2.11). Core inflation continued to fluctuate within a narrow range just under 1% (cf. chart 2.12). Medium-term inflation expectations derived from financial indicators remained at a low level.

The European Central Bank made no adjustments to its monetary policy. It intends to continue purchasing securities totalling EUR 80 billion until at least March 2017.

JAPAN

In Japan, GDP expanded by 0.7% in the second quarter. This was a slower rate than in the previous quarter (cf. chart 2.7). The two earthquakes in Kumamoto in April had a temporary dampening effect on production. Exports fell as well. However, residential construction and public sector investment proved to be driving forces. Supported by increasing real incomes, private consumption also expanded slightly. The recovery on the labour market continued. At 3.0%, the unemployment rate was at its lowest in July since the mid-1990s (cf. chart 2.10).

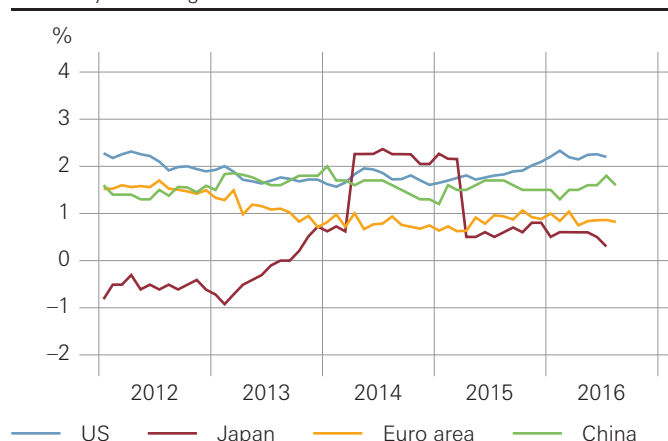
The economic situation is likely to recover further in the coming quarters. The strong appreciation of the yen since the beginning of the year comes with challenges, however. Against this background, the government launched a multi-year economic stimulus package at the beginning of August. New government expenditure amounts to approximately JPY 7.5 trillion (1.5% of GDP) and essentially comprises investment in rail transport as well as measures aimed at mitigating the negative impact of an ageing population. Initial growth stimuli are to be expected towards the end of the year. In addition, the government postponed to October 2019 the VAT hike planned for April 2017. On the whole, GDP is likely to grow by 0.5%, which roughly corresponds to the growth potential. For 2017, the forecast is 1.0%, slightly higher than three months ago.

Impacted by energy prices, consumer price inflation remained in negative territory. In July, annual inflation stood at -0.5% (cf. chart 2.11). Excluding energy and food prices, it amounted to 0.3% (cf. chart 2.12). The appreciation of the yen will dampen inflation further in the coming months. Longer-term inflation expectations figures derived from company surveys remain well below the Japanese central bank's inflation target of 2%. In July, the Bank of Japan decided to increase exchange-traded funds from JPY 3.3 trillion to JPY 6 trillion a year. Holdings of Japanese government bonds were to be further expanded at an annual rate of roughly JPY 80 trillion. At the same time, the central bank planned to conduct a comprehensive assessment of its current programme before its next monetary policy meeting on 20 and 21 September.

Chart 2.12

CORE INFLATION RATES ¹

Year-on-year change

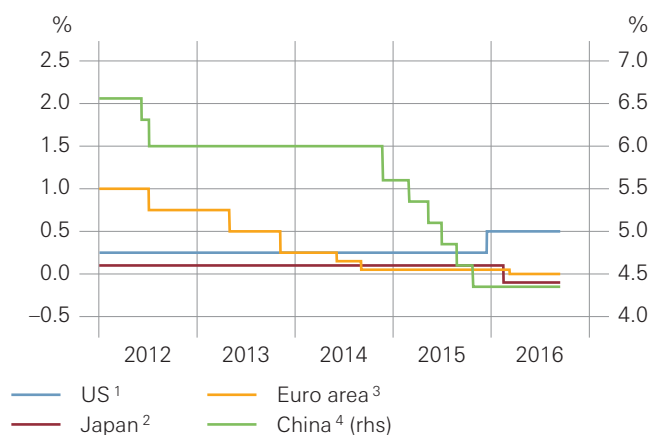


¹ Excluding food and energy.

Source: Thomson Reuters Datastream

Chart 2.13

OFFICIAL INTEREST RATES



¹ Federal funds rate.

² Call money target rate.

Source: Thomson Reuters Datastream

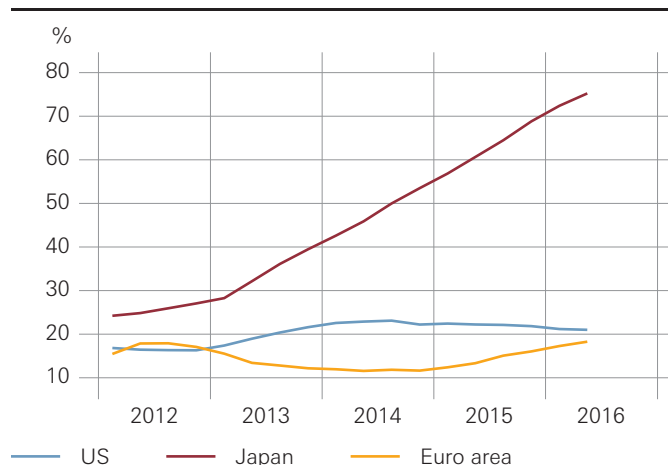
³ Main refinancing rate.

⁴ One-year lending rate.

Chart 2.14

MONETARY BASE

Relative to GDP



Source: Thomson Reuters Datastream

EMERGING ECONOMIES

Economic activity in the large emerging economies continued to vary from one country to another. In China, the economy regained some momentum in the second quarter. Once again, the main drivers were construction, which benefited from public infrastructure projects and the real estate market. In India, GDP once again expanded vigorously. In Russia and Brazil, however, the recession continued.

In China and India, the short-term outlook remains favourable. In China, the monetary and fiscal stimulus measures will continue to support the economy, even though growth stimuli are likely to abate gradually. This is supported by the fact that lending expanded less strongly in recent months, albeit still significantly faster than nominal GDP. In addition, the moderate depreciation of the renminbi since the beginning of the year is likely to translate into a slight stimulus for the export industry. The SNB forecasts China's GDP to increase by 6.7% for 2016 and 6.3% for 2017. High levels of corporate debt and overcapacity in heavy industry still carry significant risks.

In India, the short-term economic outlook has improved further. For 2016, the SNB expects India's GDP to grow by approximately 8.0%. In Russia, the slight recovery in oil prices since the beginning of the year will ease the pressure on the economy somewhat. The recession, which has persisted since mid-2014, will probably end in the second half of the year. Owing to high inflation and unemployment, the outlook for Brazil remains subdued.

Inflation receded somewhat in the emerging economies. In China, annual inflation fell to 1.3% in August as a result of food prices. In India, it dropped to 5.0% and thus remained within the target range of 2% to 6%. Inflation trended downwards in Russia and Brazil due to tight monetary policy and exchange rate stabilisation, but it remained unsatisfactorily high (6.8% and 9.0% respectively).

In China and India, monetary policy remained expansionary. In Russia and Brazil, however, the central banks kept reference rates unchanged at a high level in order to combat inflation.

3 Economic developments in Switzerland

In Switzerland, economic activity grew noticeably in the second quarter, resulting in a decrease in the underutilisation of overall production capacity. However, unemployment went up slightly since the last monetary policy assessment (seasonally-adjusted).

As a result of the latest revision of data by the Swiss Federal Statistical Office (SFSO), the economic situation in Switzerland since March 2015 appears somewhat more favourable. The latest figures confirm that economic activity has recovered gradually since its slump at the start of 2015. However, not all industries have benefited equally from the recovery. On the whole, utilisation of production capacity remains unsatisfactory. As a result, margins at a large number of companies continue to be strained.

For the second half of the year, economic growth is expected to be somewhat more modest than in the first half of the year, partially due to a temporary softening of growth in Europe. For 2016 as a whole, the SNB now expects GDP growth of approximately 1.5%. Economic recovery looks set to continue at a moderate pace next year.

AGGREGATE DEMAND AND OUTPUT

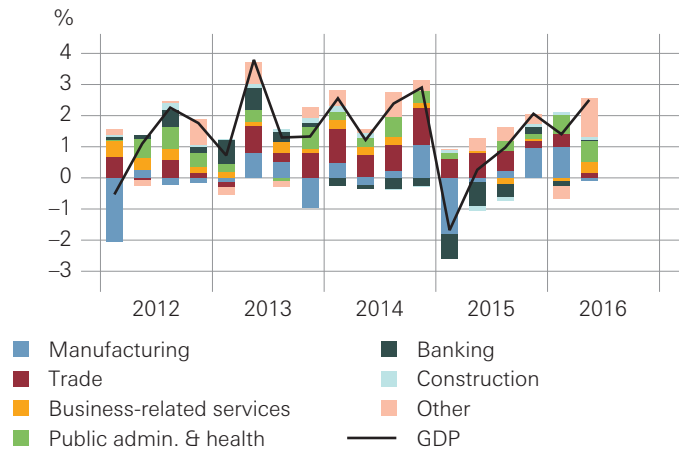
Robust growth in second quarter

According to the first official estimate by the State Secretariat for Economic Affairs (SECO), GDP in the second quarter was up by 2.5%, following growth of 1.4% in the prior quarter. On the output side, growth was broader-based than in previous quarters. Substantial contributions to GDP growth came from business-related services, public administration, healthcare and social services as well as energy and water supply. In manufacturing, value added receded slightly after considerable increases in both of the previous quarters, while the value added in financial services and insurance stagnated (cf. chart 3.1).

Chart 3.1

CONTRIBUTIONS TO GROWTH, BY SECTOR

Change from previous period

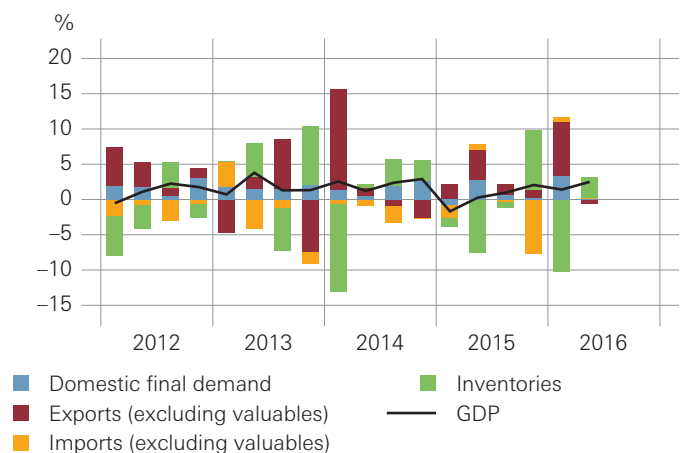


Source: State Secretariat for Economic Affairs (SECO)

Chart 3.2

CONTRIBUTIONS TO GROWTH IN DEMAND

Change from previous period

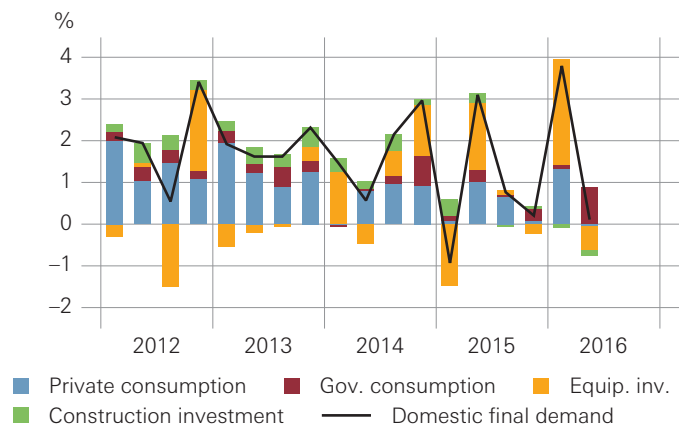


Source: SECO

Chart 3.3

DOMESTIC FINAL DEMAND, GROWTH CONTRIBUTIONS

Change from previous period



Source: SECO

Weak export performance in second quarter

After solid growth in the previous quarter, exports of goods and services receded slightly in the second quarter overall. This was primarily due to a decrease in merchanting. However, exports lost momentum even without the inclusion of merchanting. One exception was the export of pharmaceutical products, which once again saw strong growth. Geographically, exports to the emerging economies, in particular, declined. In contrast, goods deliveries to the US and Japan increased considerably.

Imports were also down slightly overall. However, as exports contracted more than imports, net exports registered a negative result (cf. table 3.1).

Disparate development in domestic demand

The strong economic growth recorded in the second quarter was reflected in a positive contribution from inventories (including statistical errors) on the demand side and a sharp increase in public consumption. Private consumption stagnated, however. Expenditure on health registered robust growth again. In other areas, the increase in consumer expenditure remained subdued. Retail sales continued to decline.

Investment activity remained volatile. Equipment investment receded slightly in the second quarter, after having been driven mainly by purchases of aircraft and spacecraft from abroad in the previous quarter. Construction investment decreased overall; this can be attributed to civil engineering. Residential construction investment maintained its upwards trend. According to the annual data published by the SFSO in July, this category has risen steadily for the last seven years. As a result, the share of empty housing units in the housing stock continued to rise, reaching 1.3% as at 1 June 2016, the highest level since June 2000.

Table 3.1

REAL GDP AND COMPONENTS

Growth rates on previous period in percent, annualised

	2012	2013	2014	2015	2014		2015				2016	
					Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
Private consumption	2.6	2.2	1.2	1.1	1.6	1.5	0.1	1.6	1.1	0.1	2.2	-0.1
Government consumption	2.1	2.3	1.5	2.2	1.7	5.6	1.0	2.4	0.2	2.4	0.9	7.0
Investment in fixed assets	2.9	1.1	2.8	1.6	3.7	5.1	-4.1	6.8	0.3	-0.6	9.0	-2.6
Construction	2.9	3.1	3.2	2.2	3.9	1.2	3.7	2.1	-0.5	0.6	-0.7	-1.2
Equipment	2.8	-0.2	2.6	1.3	3.6	7.7	-8.9	10.0	0.8	-1.4	15.7	-3.5
Domestic final demand	2.6	1.9	1.7	1.3	2.2	3.0	-0.9	3.1	0.8	0.2	3.8	0.1
Change in inventories ¹	-1.0	0.6	-0.8	-0.3	3.7	2.9	-1.3	-7.6	-0.8	8.5	-10.3	2.8
Total exports ²	3.0	0.0	5.2	2.2	-1.7	-5.0	4.2	8.3	3.0	2.1	14.7	-1.2
Goods ²	0.9	-2.3	5.8	2.5	-5.9	-8.7	8.6	10.2	2.8	-1.7	25.7	-1.6
Goods excluding merchanting ²	1.7	-1.0	4.0	0.7	12.2	-4.9	-9.7	4.0	6.3	12.4	9.5	3.3
Services	7.4	4.7	4.0	1.6	7.4	2.7	-3.9	4.7	3.5	10.2	-4.1	-0.2
Total imports ²	4.4	1.4	3.2	3.0	5.6	0.1	4.1	-2.0	1.0	19.8	-1.6	-0.3
Goods ²	2.3	0.7	1.7	0.0	0.4	-6.1	3.7	-10.8	2.7	20.1	2.3	1.9
Services	9.3	2.9	6.4	9.0	17.3	13.8	4.9	16.7	-1.9	19.3	-8.5	-4.5
Net exports ³	-0.2	-0.6	1.3	-0.1	-3.3	-2.7	0.5	5.1	1.1	-6.6	8.3	-0.5
GDP	1.0	1.8	2.0	0.8	2.4	2.9	-1.7	0.3	1.0	2.1	1.4	2.5

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

Indications that the labour market is recovering have become stronger, with a rise in both the number of employed persons and the number of jobs. In addition, the labour market indicators based on the various industry surveys maintained their upwards trend. By contrast, unemployment continued to edge up.

Renewed rise in employment

According to the employment statistics of the SFSO, the (seasonally adjusted) number of gainfully employed persons markedly increased once again in the second quarter (cf. chart 3.4).

The employment statistics are based on a survey of households. On the other hand, the national job statistics are based on a survey of companies. The latter shows a slight increase in the number of full-time equivalent positions overall, although this varied from one sector to another. The number of jobs in the services sector rose, whereas in manufacturing and construction it receded (cf. chart 3.5).

Slight rise in unemployment according to SECO

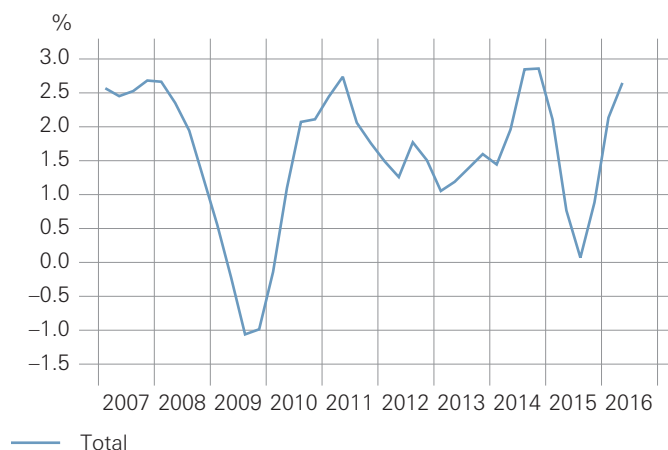
The number of people registered as unemployed at the regional employment offices has risen continuously since 2014, however this increase has only been slight in recent months. At the end of August 2016, a total of 151,000 people were recorded as unemployed, excluding seasonal fluctuations, corresponding to an unemployment rate of 3.4% (cf. chart 3.6).

Unemployment figures measured in line with the International Labour Organization (ILO) definition, which are obtained in a survey of households, decreased for the first time since the end of 2014. However, at 4.6%, this figure remains above unemployment as measured by the regional employment offices because the survey of households includes unemployed people who are not registered, or no longer registered, with these offices.

Chart 3.4

EMPLOYED PERSONS

Change from previous period

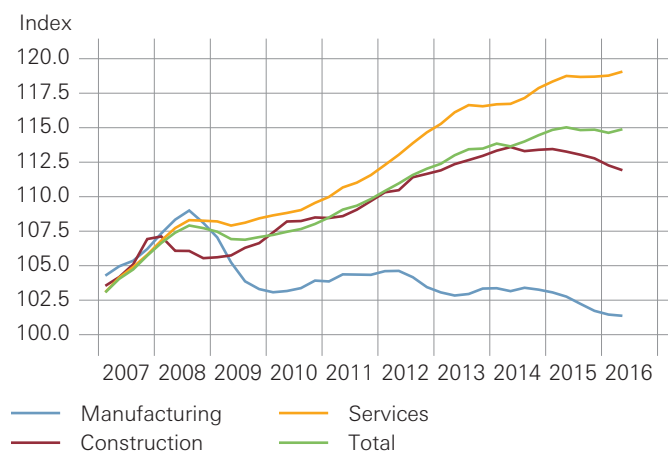


Source: Swiss Federal Statistical Office (SFSO); seasonal adjustment: SNB

Chart 3.5

FULL-TIME EQUIVALENT JOBS

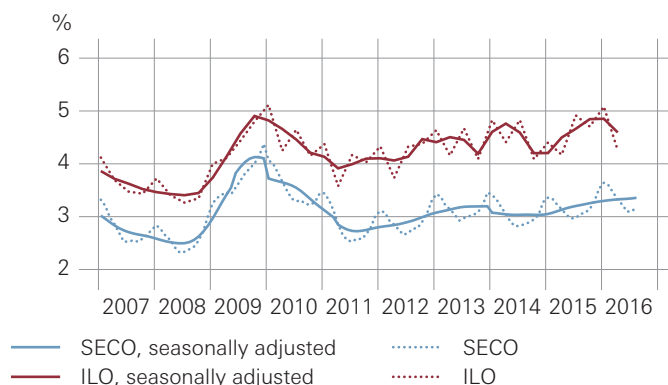
Q1 2006 = 100



Source: SFSO; seasonal adjustment: SNB

Chart 3.6

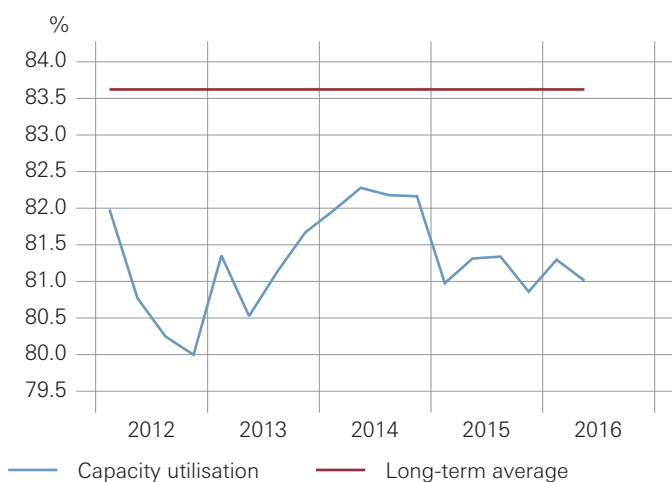
UNEMPLOYMENT RATE



SECO: Unemployed registered with the regional employment offices, as a percentage of the labour force according to the 2000 and 2010 censuses and the 2012 to 2014 structural surveys.
ILO: Unemployment rate based on International Labour Organization definition.
Sources: SFSO, SECO

Chart 3.7

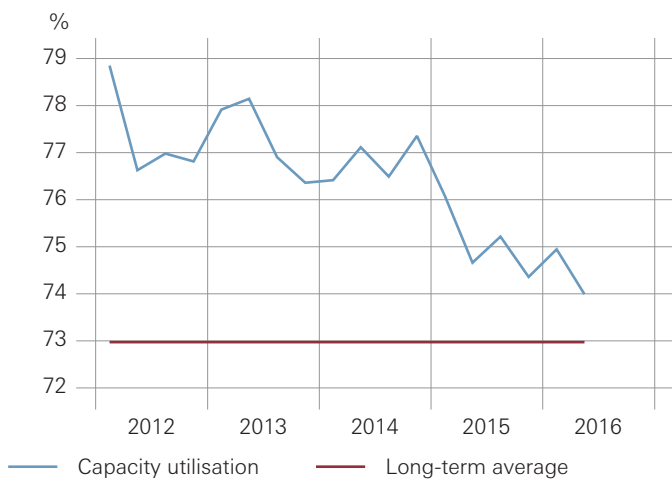
CAPACITY UTILISATION IN MANUFACTURING



Source: KOF Swiss Economic Institute

Chart 3.8

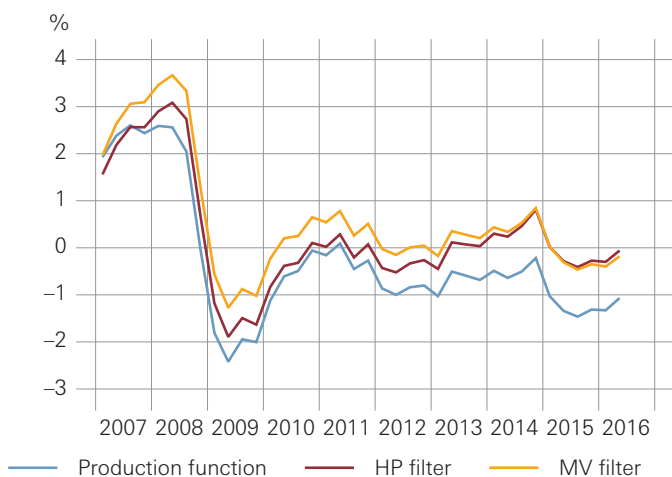
CAPACITY UTILISATION IN CONSTRUCTION



Source: KOF Swiss Economic Institute

Chart 3.9

OUTPUT GAP



Source: SNB

CAPACITY UTILISATION

Underutilisation in manufacturing

According to the KOF survey, utilisation of technical capacity in manufacturing decreased, from 81.3% to 81.0%, in the second quarter. It thus remains well below the long-term average (cf. chart 3.7). Machine utilisation in the construction industry also declined in the second quarter. However, unlike in manufacturing, capacity utilisation in construction remains above its long-term average (cf. chart 3.8). As for the services sector, while surveys continue to suggest average utilisation overall, capacities in individual areas, for example in tourism and retailing, were underutilised.

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. Given the strong GDP growth in the second quarter, the output gap narrowed. However, it does continue to indicate that the production factors are underutilised. Estimated potential, calculated by means of a production function, showed an output gap of -1.1% for the second quarter, compared to -1.3% in the previous quarter. Other methods for estimating potential output (Hodrick-Prescott filter and multivariate filter) suggest the output gap is almost closed (cf. chart 3.9).

The different estimates reflect the various ways of calculating potential output. 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

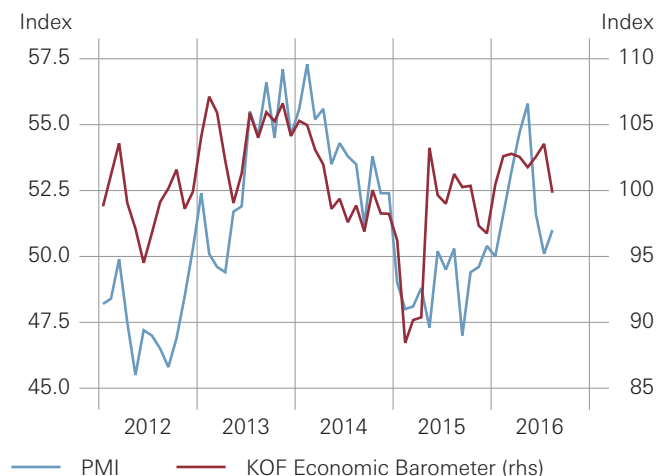
Economic recovery is expected to continue in Switzerland. However, growth momentum is likely to be weaker in the second half of the year than in the first half. Available indicators to date thus suggest a slowdown in the growth of GDP for the third quarter. In recent months, the purchasing managers' index in manufacturing fell once again, and goods exports stagnated of late. The KOF economic barometer also receded slightly again (cf. chart 3.10). A temporary weakening of growth in Europe is likely part of the cause.

Overall, however, the outlook remains favourable. This is due to two factors in particular. First, despite the downward revision of the international scenario following the Brexit decision, the global economic situation is expected to continue to stimulate demand in Switzerland (cf. chapter 2). Second, the dampening effect on GDP growth of the past appreciation in the Swiss franc is fading. In this context, both exports and the domestic economy are likely to experience a positive trend.

For 2016, the SNB forecasts GDP growth of approximately 1.5% and expects moderate economic growth again for the coming year. As a result, the negative output gap is expected to gradually narrow and the labour market situation to improve. Surveys of companies regarding recruitment plans suggest improvement (cf. chart 3.11).

Chart 3.10

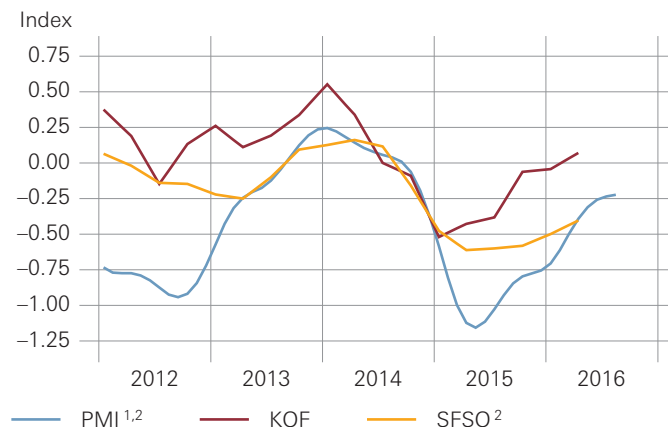
LEADING INDICATORS



Sources: Credit Suisse, KOF Swiss Economic Institute

Chart 3.11

EMPLOYMENT LEADING INDICATORS



1 Monthly figures.

2 Trend component: SNB.

Sources: Credit Suisse, KOF Swiss Economic Institute, SFSO

4

Prices and inflation expectations

Over the last 12 months, consumer prices have remained largely unchanged. As a result, annual inflation, which at the beginning of the year was still clearly negative, rose to -0.1% in August 2016. With the exception of prices for oil products – which continue to be well below last year’s level – all key components of the consumer price index are posting inflation rates close to zero. Core inflation rates, too, are around zero.

Inflation expectations remained more or less unchanged, and are in line with the SNB’s definition of price stability.

CONSUMER PRICES

CPI inflation rate close to zero

The annual inflation rate as measured by the national consumer price index (CPI) has risen further in recent months (cf. table 4.1), posting -0.1% in August 2016 as opposed to -1.3% in January. This is primarily due to the easing of effects associated with the appreciation of the Swiss franc in January 2015.

Oil products still cheaper than last year

Although oil prices have increased since the beginning of 2016, the contribution of oil products to the CPI inflation rate continues to be strongly negative (cf. chart 4.1). By contrast, imported goods and services excluding oil products recorded annual inflation rates close to zero.

Prices of domestic goods and services unchanged year-on-year

Annual inflation rates for both domestic goods and domestic services were zero in August. At the beginning of the year, the contribution of these two components to annual inflation in this category was still clearly negative (cf. chart 4.2).

Table 4.1

SWISS CONSUMER PRICE INDEX AND COMPONENTS

Year-on-year change in percent

	2015		2016		2016		2016	
		Q3	Q4	Q1	Q2	June	July	August
Overall CPI	-1.1	-1.4	-1.4	-1.0	-0.4	-0.4	-0.2	-0.1
Domestic goods and services	0.1	0.0	-0.3	-0.4	-0.1	-0.1	0.0	0.0
Goods	-0.7	-1.0	-1.0	-1.3	-0.7	-0.7	-0.1	0.0
Services	0.3	0.3	-0.1	-0.2	0.1	0.1	0.1	0.0
Private services excluding housing rents	0.4	0.4	-0.2	-0.2	0.2	0.2	0.2	0.1
Housing rents	0.8	0.9	0.3	0.1	0.2	0.2	0.2	0.2
Public services	-0.8	-0.9	-0.5	-0.5	-0.4	-0.3	-0.3	-0.7
Imported goods and services	-4.7	-5.4	-4.4	-2.8	-1.2	-1.3	-0.9	-0.5
Excluding oil products	-2.5	-3.1	-2.7	-1.5	-0.1	-0.5	0.2	0.5
Oil products	-17.4	-18.5	-14.9	-11.3	-8.5	-6.8	-7.8	-7.0

Sources: SFSO, SNB

Low rent inflation

Rent inflation in August was 0.2%, well below the long-term average. This low rate of inflation for rents is in line with the reference interest rate, which has been unchanged since June 2015 (cf. chart 4.3).

The reference interest rate is based on banks' average mortgage rates. It is decisive for the adjustment of rents based on mortgage rate changes.

Core inflation around zero

Core inflation rates, which were still deeply in negative territory at the beginning of 2016, rose rapidly during the course of the year (cf. chart 4.4). In August, the SFSO core inflation rate 1 (SFSO1) and the trimmed mean calculated by the SNB (TM15) were 0.0% and -0.2% respectively.

The increase in core inflation rates, like the increase in the CPI inflation rate, is attributable to the fading impact from the Swiss franc appreciation of January 2015. The highly volatile prices for oil products, by contrast, have hardly any impact on the path of core inflation. Both SFSO1 and TM15 are based on a reduced CPI goods basket. The SFSO1 always excludes the same products every month (fresh and seasonal products, energy and fuel), whereas the TM15 excludes the goods with the greatest price changes every month in a year-on-year comparison (15% at either end of the distribution curve).

PRODUCER AND IMPORT PRICES

Producer and import prices remain stable

Producer and import prices fell substantially between January and August 2015. Since then, they have remained largely stable. As a result, the negative annual inflation rates climbed back up towards zero (cf. chart 4.5).

Year-on-year, import prices have once again receded by slightly more than producer prices. However, the gap between the two annual rates of inflation has narrowed considerably since the beginning of the year.

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.

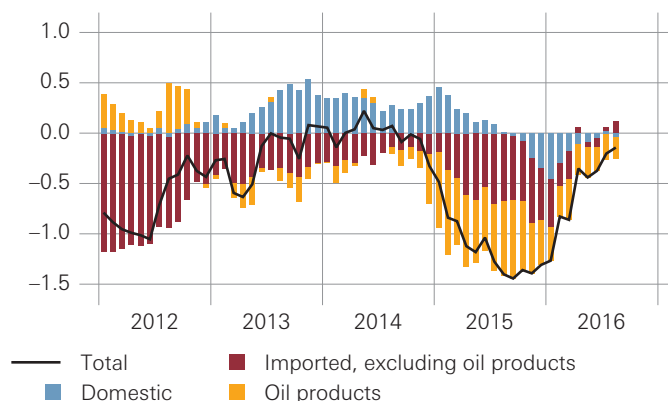


Chart 4.2

CPI: DOMESTIC GOODS AND SERVICES

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

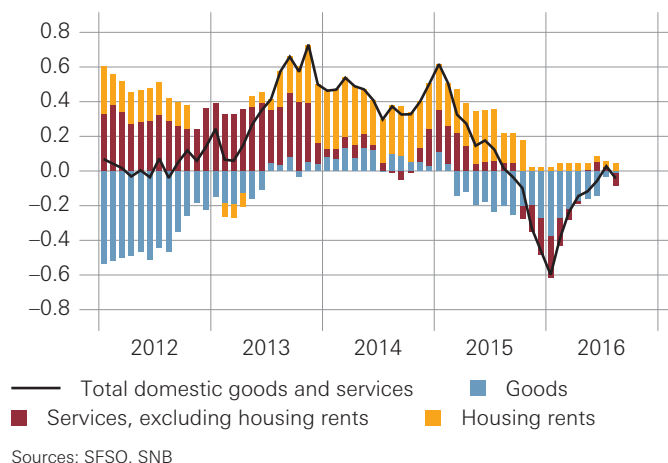


Chart 4.3

HOUSING RENTS

Year-on-year change

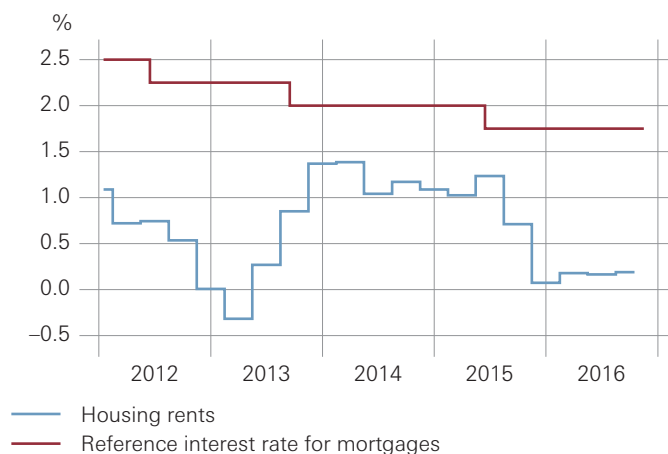
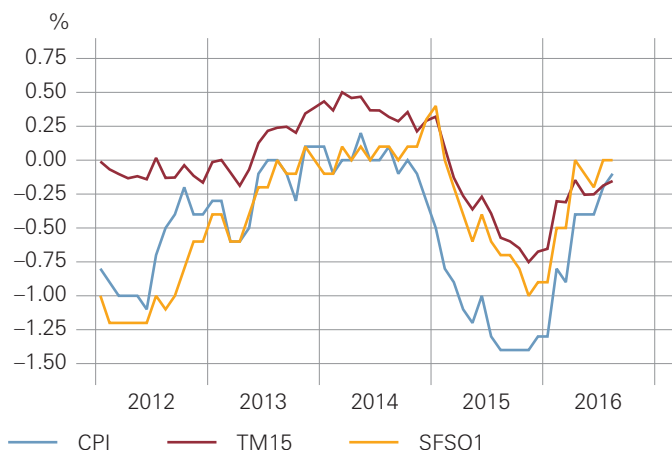


Chart 4.4

CORE INFLATION RATES

Year-on-year change

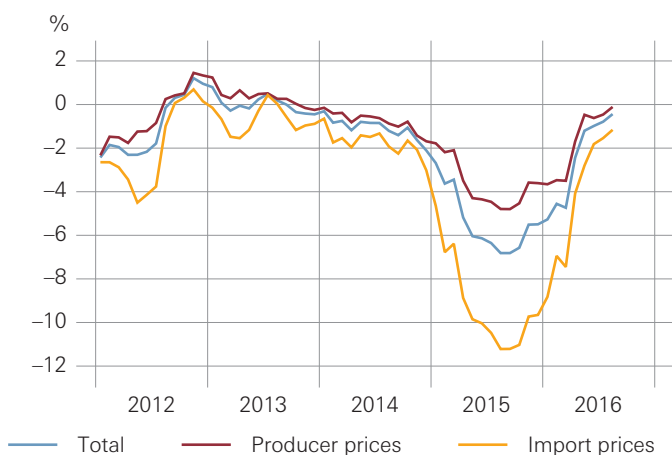


Sources: SFSO, SNB

Chart 4.5

PRODUCER AND IMPORT PRICES

Year-on-year change

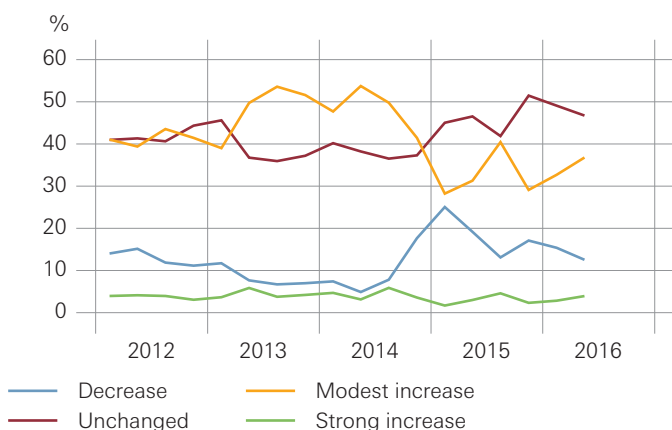


Source: SFSO

Chart 4.6

PRICE EXPECTATIONS

Survey of households on expected movements in prices for coming 12 months



Sources: SECO, SNB

INFLATION EXPECTATIONS

Stable inflation expectations

Inflation expectations have changed little over the past two quarters. They continue to be negative for 2016 as a whole, and positive for 2017. Medium and long-term inflation expectations are still consistent with price stability, which the SNB equates with a rise in CPI of less than 2% per year.

Rates of inflation expected to increase

According to the survey of households conducted by SECO in July 2016, the share of respondents expecting prices to rise over the next 12 months has increased, from 35% in April to 41% in July (cf. chart 4.6). By contrast, slightly fewer households than three months ago expected no change or a drop in prices.

According to the *Credit Suisse ZEW Financial Market Report*, the share of financial analysts surveyed who expect inflation rates to rise in the next six months decreased, from 43% in May to 29% in August. This decrease is probably mainly due to the fact that the inflation rate has already risen considerably over the last few months. In August, 69% of survey respondents expected inflation rates in six months' time to be unchanged, while only 3% expected falling inflation rates.

Talks held by the SNB delegates for regional economic relations with companies from all areas of the economy confirmed the impression of generally stable short-term inflation expectations. In the third quarter of 2016 – as in the previous quarter – respondents expected an inflation rate of -0.2% over the next 6–12 months.

Medium and long-term inflation expectations in positive territory

The discussions with the SNB delegates also revealed that, in the third quarter of 2016, respondents were projecting inflation in 3–5 years at 0.5%, the same as in the previous quarter. Participants in Deloitte's CFO survey in the second quarter put inflation in two years' time at 0.6%, compared to 0.7% in the first quarter.

Surveys on inflation expectations over longer-term horizons suggest that these are still in low positive territory.

5

Monetary developments

At its monetary policy assessment of mid-June 2016, the SNB left its monetary policy unchanged. Short-term interest rates have remained largely stable since then, close to the level of the negative interest rate that the SNB imposes on sight deposit accounts held by banks and other financial market participants. Yields on longer-term Confederation bonds are also negative, which suggests that market participants anticipate negative short-term interest rates for the foreseeable future.

Exchange rates generally remained more or less unchanged in recent months. Although the result of the EU referendum in the UK (23 June 2016) caused the Swiss franc to appreciate against the British pound, it lost value against the Japanese yen and remained stable against the US dollar and the euro.

Monetary aggregates and bank loans expanded moderately over the last 12 months. Loans thus once again rose at a faster rate than nominal GDP so that the rise in the loan ratio which has been observable in 2009 continued.

SUMMARY OF MONETARY POLICY SINCE THE LAST ASSESSMENT

Expansionary monetary policy remains unchanged

The SNB confirmed its monetary course at its monetary policy assessment on 16 June 2016. It decided to leave the target range for the three-month Libor unchanged at between -1.25% and -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.

The SNB reaffirmed its willingness to remain active in the foreign exchange market in order to influence exchange rate developments, where necessary. The negative interest rate and the SNB's willingness to intervene in the foreign exchange market serve to ease pressure on the Swiss franc. In this way, the SNB's monetary policy helps to stabilise price developments and support economic activity.

Higher sight deposits at the SNB

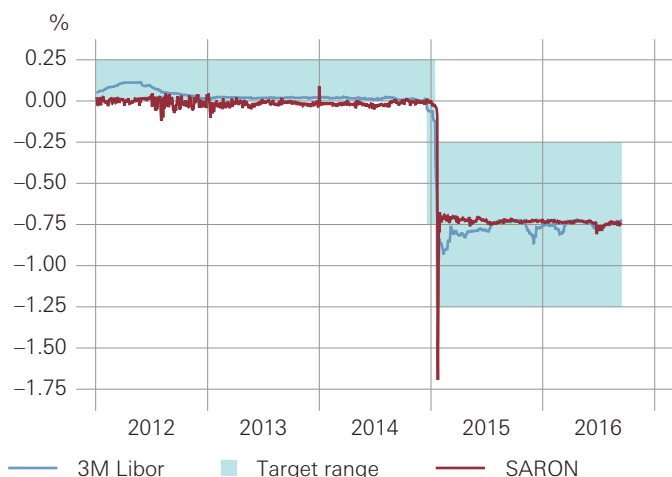
Since the monetary policy assessment of June 2016, total sight deposits held at the SNB have increased. In the week ending 9 September 2016 (last calendar week before the mid-September assessment), they amounted to CHF 515.8 billion, up by CHF 22.0 billion compared to the last calendar week preceding the mid-June assessment (CHF 493.8 billion). Between the assessments in mid-June and mid-September 2016, sight deposits at the SNB averaged CHF 511.6 billion. Of this amount, CHF 434.4 billion was accounted for by the sight deposits of domestic banks and the remaining CHF 77.2 billion by other sight deposits.

High level of banks' surplus reserves

Between 20 May 2016 and 19 August 2016, statutory minimum reserves averaged CHF 15.1 billion. Overall, banks exceeded the minimum reserve requirement by some CHF 419.2 billion on average (previous period: CHF 411.3 billion). Banks' surplus reserves have thus increased once again.

Chart 5.1

MONEY MARKET RATES

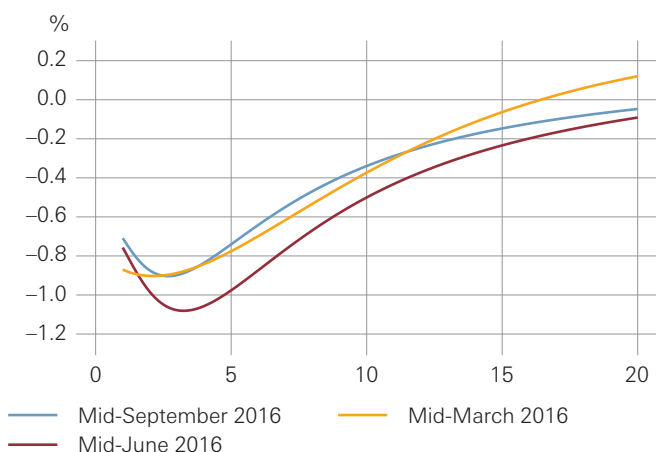


Sources: Bloomberg, SIX Swiss Exchange Ltd, SNB

Chart 5.2

TERM STRUCTURE OF CONFEDERATION BONDS

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



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

Stable money market interest rates

The surprise outcome of the EU referendum in the UK created volatility in the world's financial markets. However, the situation on the Swiss franc money market soon normalised. Both secured (SARON) and unsecured money market transactions (three-month Libor) settled close to the interest rate of -0.75% on sight deposits held at the SNB (cf. chart 5.1).

Long-term interest rates still negative

The yield on ten-year Confederation bonds fluctuated between -0.3% and a new historical low of -0.6% in the course of the third quarter. At the time of the mid-September assessment it stood at -0.3% , marginally higher than three months earlier (cf. chart 5.2).

Slight flattening of yield curve

Medium-term Confederation bond yields rose somewhat more strongly from their mid-June level than long-term yields. The yield curve has thus flattened out slightly (cf. chart 5.2).

Low long-term real interest rates

The estimated long-term real interest rate was around -0.1% in mid-September 2016, which was virtually on a par with the previous quarter (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, estimated using a vector autoregressive (VAR) model.

EXCHANGE RATES

Franc stable against euro and US dollar

There has been little overall change in the value of the Swiss franc against the euro and the US dollar over recent months (cf. chart 5.4). The EU referendum in the UK, however, generated uncertainty in the markets. The SNB subsequently issued a statement that it had intervened in the foreign exchange market to stabilise the situation and that it would remain active in the market.

Weak pound and strong yen

Chart 5.5 depicts the development of the Swiss franc exchange rate for various currencies, with the rates on the day before the EU referendum of 23 June 2016 indexed to 100. It shows that the result of the referendum led to a sharp depreciation of the pound sterling against the Swiss franc and all other currencies. The Japanese yen strengthened the most, appreciating against all currencies, including the Swiss franc.

Monetary conditions somewhat eased

In nominal, export-weighted terms, the Swiss franc has weakened slightly since the mid-June monetary policy assessment. With short-term interest rates virtually unchanged, monetary conditions have become slightly more expansionary.

The Monetary Conditions Index (MCI) in chart 5.6 combines changes in the three-month Libor with 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 shown, 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 largely unchanged

The export-weighted real external value of the Swiss franc has remained largely unchanged since November 2015. Although in August it was more than 1% below its previous year's level, it still significantly exceeded its longer-term average.

Chart 5.4

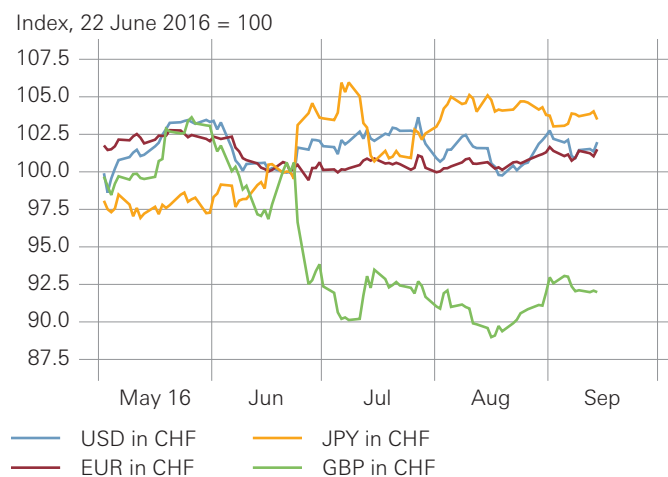
EXCHANGE RATES



Source: SNB

Chart 5.5

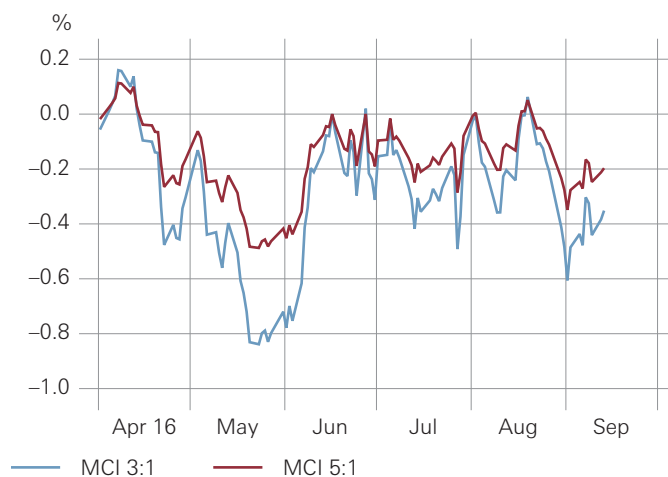
BREXIT REFERENDUM AND EXCHANGE RATES



Source: SNB

Chart 5.6

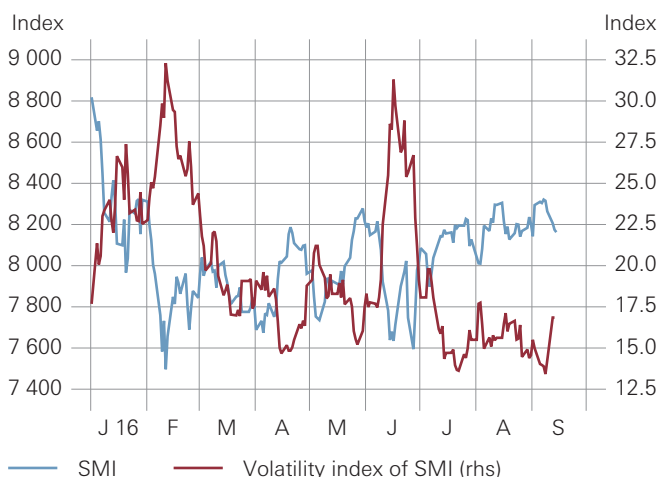
MCI NOMINAL



Source: SNB

Chart 5.7

SHARE PRICES AND VOLATILITY

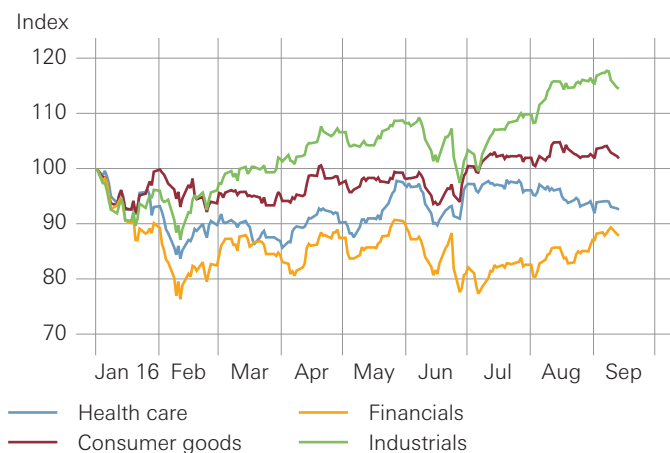


Sources: Bloomberg, Thomson Reuters Datastream

Chart 5.8

SELECTED SPI SECTORS

Beginning of period = 100

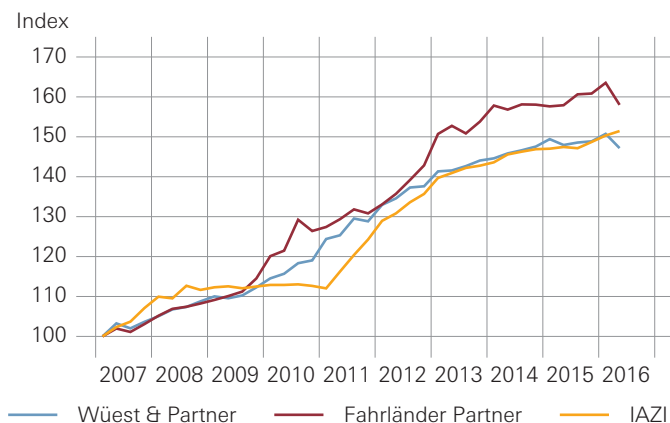


Source: Thomson Reuters Datastream

Chart 5.9

TRANSACTION PRICES, PRIVATELY OWNED APARTMENTS

Nominal (hedonic), beginning of period = 100



Sources: Fahrländer Partner, IAZI, Wüest & Partner

SHARE AND REAL ESTATE PRICES

Temporary decline in share prices following EU referendum in UK

After recording substantial losses at the beginning of 2016 and then stabilising, share prices in Switzerland suffered a new setback at the end of June following the EU referendum in the UK (cf. chart 5.7). However, share prices made a strong recovery in July when investors seemed to conclude that the economic and political costs of the UK's exit from the EU might be less than initially feared. This reassessment was made in the light of signals from central banks that they would intervene in the financial markets, as necessary, in order to stabilise the situation.

Implied volatility derived from options on SMI futures contracts, which serves as a measure of the uncertainty on the stock market, increased sharply in June and then declined once again in line with the recovery in share prices.

Broad-based price losses and gains

In the four Swiss Performance Index (SPI) sub-indices shown in chart 5.8, industrials and financials displayed the greatest fluctuations in connection with the EU referendum in the UK. While the industrials sub-index was quick to recover, reaching a new annual high in September, the financials sub-index remained under pressure as a result of weak quarterly figures for domestic and foreign banks.

Residential property prices slightly higher than previous year

Overall, real estate price indices suggest that transaction prices for privately owned apartments fell slightly in the second quarter following a surprisingly sharp rise in the previous quarter (cf. chart 5.9). Taking an average of the three available indices, transaction prices for privately owned apartments saw a moderate increase of just under 1% compared to the year-earlier quarter, while transaction prices for single-family houses climbed by about the same amount year-on-year.

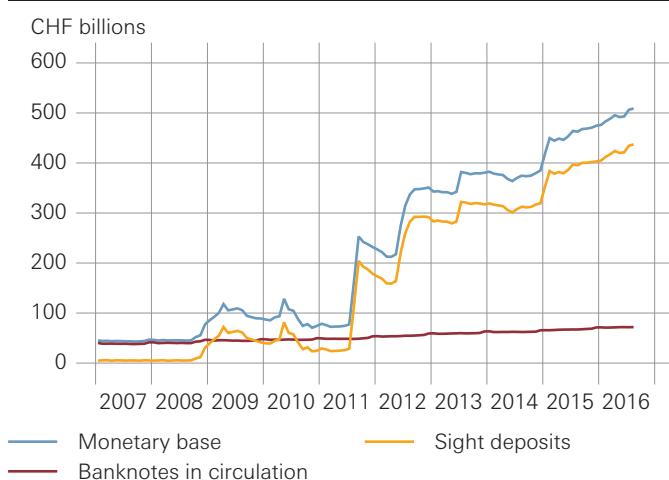
MONETARY AND CREDIT AGGREGATES

Continuing growth in monetary base

The monetary base, which consists of banknotes in circulation and sight deposits of domestic banks held at the SNB, increased further over recent months and stood at an average of CHF 509.0 billion in August 2016 (cf. chart 5.10). This increase primarily reflects movements in domestic banks' sight deposits, which grew by CHF 17.3 billion between May and August 2016. This was due to the SNB's interventions on the foreign exchange market in the context of the EU referendum in the UK. There was little change in banknotes in circulation.

Chart 5.10

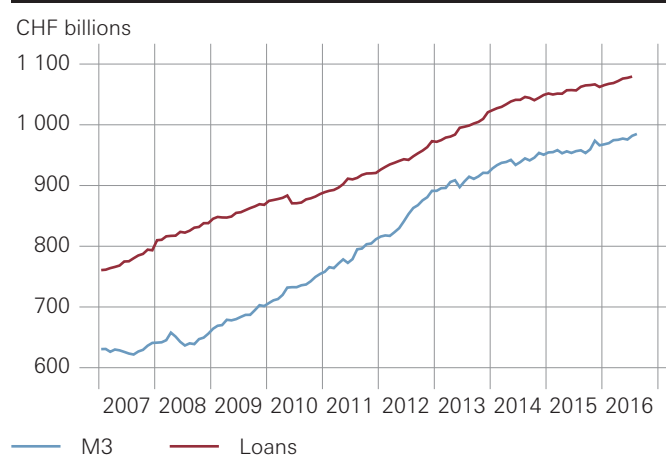
MONETARY BASE



Source: SNB

Chart 5.11

M3 MONETARY AGGREGATE AND BANK LOANS IN SWISS FRANCS



Source: SNB

Table 5.1

MONETARY AGGREGATES AND BANK LOANS

Year-on-year change in percent

	2015	2015	2016	2016	2016	2016	2016	2016
		Q3	Q4	Q1	Q2	June	July	August
M1	-0.1	0.7	-2.3	-0.6	1.2	1.3	2.1	2.4
M2	1.1	1.0	1.1	1.8	2.7	2.7	3.1	3.3
M3	1.9	1.5	1.7	1.6	2.3	2.3	2.6	2.8
Bank loans, total ^{1,3}	1.9	1.6	1.7	1.5	2.0	2.2	2.3	
Mortgage claims ^{1,3}	3.3	3.2	2.9	2.6	2.6	2.7	2.7	
Households ^{2,3}	3.4	3.4	3.2	2.9	2.8	2.8	2.7	
Private companies ^{2,3}	3.3	3.0	2.6	2.4	2.8	2.9	3.0	
Other loans ^{1,3}	-5.3	-6.4	-4.4	-4.5	-1.5	-0.6	0.0	
Secured ^{1,3}	-0.4	0.1	-5.8	-2.7	-1.4	-1.1	-1.0	
Unsecured ^{1,3}	-8.5	-10.8	-3.4	-5.8	-1.5	-0.2	0.7	

1 Monthly balance sheets (domestic bank offices, domestic positions, all currencies).

2 Credit volume statistics (domestic bank offices, domestic positions, all currencies).

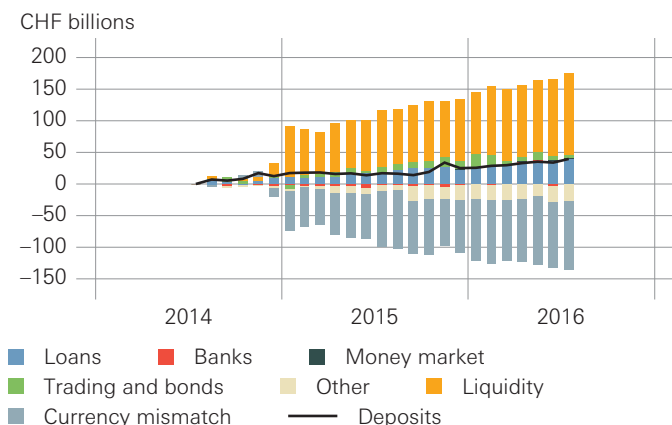
3 Growth rates for the bank loans item and its components include information provided by banks on changes in their classification practices. Consequently, they may deviate from growth rates published on the SNB's data portal, data.snb.ch.

Source: SNB

Chart 5.12

DEPOSITS COUNTERPARTS, CUMULATIVE CHANGE SINCE JUNE 2014

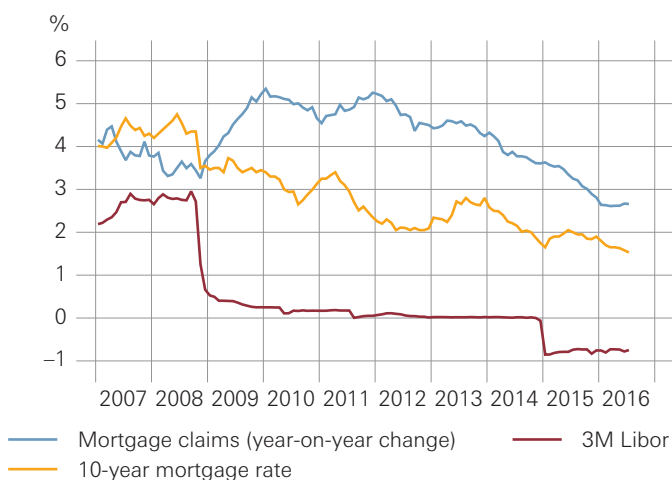
Domestic bank offices, domestic positions in CHF



Source: SNB

Chart 5.13

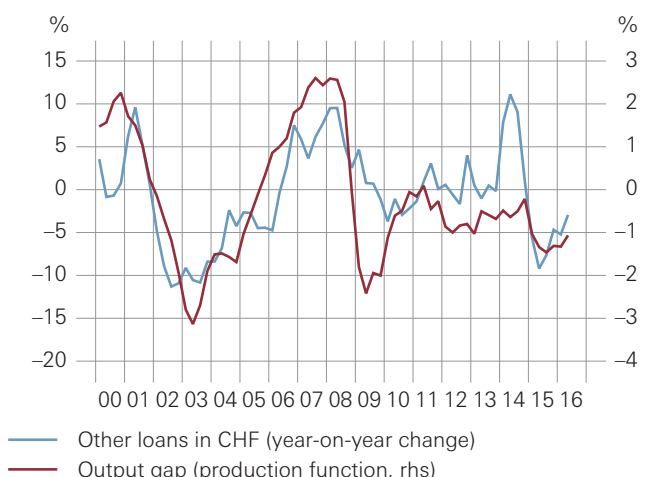
MORTGAGE CLAIMS AND 3M LIBOR



Sources: Bloomberg, SNB

Chart 5.14

OTHER LOANS AND OUTPUT GAP



Source: SNB

Slight growth in broad monetary aggregates

The M1, M2 and M3 monetary aggregates, which measure monetary aggregates held by the public, grew slightly between May and August 2016 and stood just above their previous year's level at the end of August (cf. table 5.1). The M1 monetary aggregate (notes and coins in circulation, sight deposits and transaction accounts) was CHF 586.2 billion, whereas M2 (M1 plus savings deposits) amounted to CHF 933.6 billion and M3 (M2 plus time deposits) to CHF 984.9 billion.

Parallel movement of monetary aggregates and loans

Swiss franc lending by domestic bank offices moved largely parallel with the M3 monetary aggregate over the last two to three years, after it had recorded considerably slower growth than the M3 aggregate for some five years (cf. chart 5.11).

Chart 5.12 shows the cumulated changes in domestic bank offices' balance sheet positions in Swiss francs since mid-2014. The parallel movement in loans and Swiss franc deposits of domestic customers (which roughly corresponds with the M3 monetary aggregate) can be seen here too. What is striking is that Swiss franc liquidity of domestic bank offices, i.e. the deposits of domestic banks held at the SNB, rose substantially with no acceleration in money supply and lending growth. Instead, balance sheet positions in foreign currencies and/or in respect of non-residents have, in particular, changed in the last two years, as reflected in the chart in the currency mismatch residual item (cf. 'The effect of the monetary base expansion on the balance sheets of domestic banks' by L. Altermatt and R. Baeriswyl, SNB Quarterly Bulletin 1/2015, pp. 34 et seq.).

Sustained growth in mortgage lending

Mortgage loans, which make up roughly 85% of total bank lending (all currencies), recorded a 2.6% year-on-year increase in the second quarter of 2016 (cf. table 5.1). This halted the slowdown in growth observed since 2012 (cf. chart 5.13). Mortgage interest rates remained at a historically very low level. The ten-year mortgage interest rate even hit an all-time low of 1.5% in July.

Decline in other loans

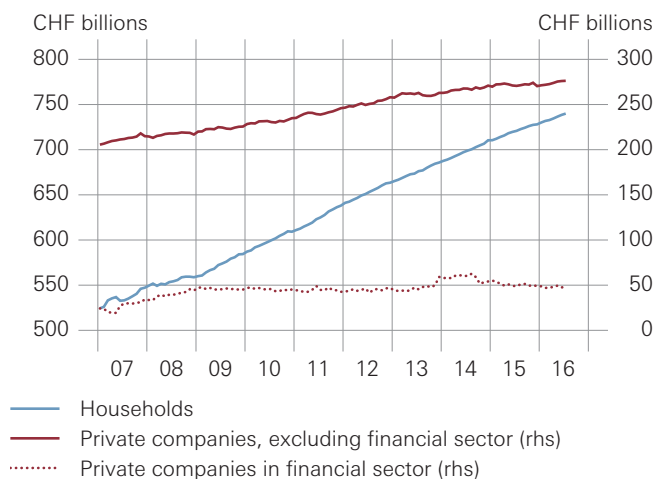
Year-on-year, the volume of other loans has declined over several quarters. Movements in other loans are generally driven by economic activity. The decline in other loans in Swiss francs observed since the beginning of 2015 is therefore in line with the widening output gap (cf. chart 5.14).

Growth in lending by sector

Both households and non-financial companies have benefited from favourable financing conditions since the beginning of the financial and economic crisis, as reflected in a continuous rise in bank loans (all currencies) extended to these two important client segments (cf. chart 5.15). At the end of July 2016, loans to households rose by CHF 19.1 billion (2.7%) and loans to non-financial companies were up by CHF 5.6 billion (2.1%) year-on year. Loans to financial companies, which exhibit greater volatility at a significantly lower volume, declined by CHF 0.8 billion (-1.7%) compared to the previous year.

Chart 5.15

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 2016

Third quarter of 2016

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 from mid-July to the end of August 2016 with 208 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 composition 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
Urs Schönholzer
Jean-Marc Falter
Fabio Bossi
Martin Wyss
Daniel Hanimann
Aline Chabloz
Rita Kobel

SUMMARY

Based on company surveys conducted in the third quarter, the Swiss economy grew somewhat in the quarter under review, compared to both the previous quarter and the previous year. This applies to all three sectors. Margins are stable but are still strained. Production capacity overall remains underutilised.

Companies expect a further slight increase in real turnover over the coming months, and an upturn in foreign demand. Margins are likely to improve through enhanced efficiency and cost-cutting measures, but also due to innovation. The stable exchange rate situation contributes to this relatively favourable assessment.

Staff numbers in the services sector are likely to increase somewhat in the next few months, whereas those in manufacturing and construction will decrease slightly. The willingness to invest remains very subdued.

BUSINESS ACTIVITY

Moderate rise in turnover overall

Real turnover in manufacturing was slightly higher than the year-back quarter and also marginally above the previous quarter. The economic situation has improved in a number of industries, including pharmaceuticals, food manufacturers and producers of electrical appliances. By contrast, the marked sluggishness in the watchmaking industry persists or has spread further.

As to export business, sales to Germany remain relatively dynamic, and North America and northern Europe are generally also cited as strong sales markets. Demand from Asia is trending upwards; there are increasing signs that this is particularly the case for China. On the other hand, several industries are feeling the effects of the very depressed economic situation in Russia and Brazil. Demand from the automotive and medical technology sectors remains high, and is increasing in the aviation industry.

Overall, business performance in construction continues to be positive, especially in structural engineering and the finishing trade. In the services sector, real turnover was slightly above that of the previous quarter. This is the case for a number of industries, namely transport, travel, IT and hotels. In retailing too, although border regions continue to be affected by cross-border shopping, sales were marginally higher than in the previous quarter. Retailing is experiencing a structural shift: while some online traders are expanding vigorously, other retailers are also attempting to diversify into this business, but with mixed success.

CAPACITY UTILISATION

Still substantial underutilisation

Overall, production capacity at the companies surveyed remains underutilised, with 45% of the survey respondents rating their utilisation as lower than usual.

Over half of the responding companies in manufacturing reported a slight to significant underutilisation of capacity, with most industry categories being affected. This was particularly pronounced in the mechanical and electrical engineering industries (MEM industries).

In construction, seasonally adjusted utilisation of technical capacity exceeded the previous quarter, both in the main construction and finishing trades. Lower-lying areas continue to notice the increased competitive pressure from mountain-region construction firms. This is partly attributable to a shortage of projects in the mountain areas as a result of the vote to curb second-home ownership (Zweitwohnungsinitiative).

The services sector continued to present a heterogeneous picture, but here too more company representatives than in the preceding quarter reported an underutilisation of infrastructure (office and retail space as well as IT and transport capacity). This applies particularly to banks, hotels and trading.

DEMAND FOR LABOUR

Staff numbers generally adequate

Overall, staff numbers are currently considered to be in line with demand. However, the situation differs from one sector to another.

Most representatives of manufacturing firms rate their staff numbers as slightly too high. This applies in particular to the MEM industries. Given the weaknesses in the watchmaking industry, some companies have already introduced short-time working, while others are considering introducing this measure in the coming months.

Staff numbers in construction are generally considered appropriate; in structural engineering, however, they are slightly low. In the services sector, headcounts in retailing and hotels are somewhat too high, while ICT companies are on a recruitment drive. Banks are continuing to expand their compliance units.

Overall, the time and effort required for staff recruitment is rated as normal. Construction is finding it easier than before to find specialised staff. The hitherto frequently cited shortage of engineers has eased somewhat, especially in the MEM industries. By contrast, staff recruitment in the IT sector is more laborious and difficult than usual. In general, a slight trend in appointing more temporary than permanent staff is discernible, for reasons of increased flexibility.

PRICES, MARGINS AND EARNINGS SITUATION

Margin pressure persists

The assessment of the margin situation has hardly changed, with margins remaining below what is considered normal. Half the companies surveyed rated their margins as lower than usual. In certain cases, prices can still be increased, especially abroad.

Considerable margin pressure still prevails in manufacturing. In the services sector, margins remain under significant pressure in trading as well as in the hotel and financial industries.

Expectations regarding developments in purchase and sales prices have shown a downward trend for quite some time. However, the situation is gradually stabilising.

Some of the data on the real estate market confirm the observation made in the previous quarter that commercial property rents are under a great deal of pressure in some cases, particularly in prime locations.

OUTLOOK

Moderate optimism

Overall, a slight increase is expected in real turnover over the coming months. Respondents are optimistic, particularly in the services sector, and to a lesser degree also in manufacturing. Reasons for this optimism include the stable exchange rate conditions, anticipated economic developments abroad and the impact of measures taken to raise efficiency and promote innovation. This constellation is expected to lead to gradual improvement in margins. Investment plans for the coming 12 months, however, still indicate no upturn in investment activity.

As to employment plans, survey respondents in the services sector anticipate a further slight increase, and that in almost all industry categories, whereas those in manufacturing and construction by and large expect marginal staff reductions. Hardly anything has changed in this respect compared to the previous quarter.

Respondents perceive increasing security risks in Europe as a threat. They identify further risks associated with an accelerated structural transformation in Switzerland, stricter regulatory requirements, the impact of the current corporate tax reform and the negative consequences of the implementation of the mass immigration initiative. The topic of cybercrime was also mentioned somewhat more frequently than previously. By contrast, the negative consequences of the Brexit decision – one of the main worries in the preceding quarter – were scarcely mentioned. While most companies have found a way of coping with the current exchange rate conditions and particularly appreciate the stability, exchange rates remain more of a challenge for others, especially for SMEs. The low interest rate environment is increasingly viewed with concern in relation to the long-term outlook for pension funds.

Companies' inflation expectations (as measured by the consumer price index) remain unchanged quarter-on-quarter, averaging –0.2% over the next 6–12 months. Expectations over a horizon of 3–5 years are 0.5% (previous quarter: 0.5%).

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.

September 2016

At its quarterly assessment of 15 September 2016, the SNB leaves the interest rate on sight deposits with the SNB at -0.75% and its target range for the three-month Libor unchanged at between -1.25% and -0.25% . The SNB reaffirms that it will remain active in the foreign exchange market, as necessary. In the SNB's view, the Swiss franc is still significantly overvalued. The negative interest rate and the SNB's willingness to intervene in the foreign exchange market are intended to make Swiss franc investments less attractive, thereby easing upward pressure on the currency. The expansionary monetary policy aims to stabilise price developments and support economic activity.

June 2016

At its quarterly assessment of 16 June 2016, the SNB maintains its expansionary monetary policy. Interest on sight deposits at the SNB remains at -0.75% and the target range for the three-month Libor is unchanged at between -1.25% and -0.25% . The SNB reaffirms that the Swiss franc is still significantly overvalued and that it will remain active in the foreign exchange market, as necessary. The negative interest rate and the SNB's willingness to intervene in the foreign exchange market are intended to make Swiss franc investments less attractive, thereby easing pressure on the currency.

March 2016

At its quarterly assessment of 17 March 2016, 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, in order to influence exchange rate developments where necessary. In the SNB's view, the Swiss franc is still significantly overvalued. The negative interest rate and the SNB's willingness to intervene in the foreign exchange market serve to ease pressure on the Swiss franc. The SNB's monetary policy thus helps to stabilise price developments and support economic activity.

December 2015

At its quarterly assessment of 10 December 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 in order to influence the exchange rate situation, as necessary. The negative interest rate and the SNB's willingness to intervene in the foreign exchange market are intended to ease pressure on the Swiss franc. The SNB's monetary policy thus helps to stabilise price developments and support economic activity.

September 2015

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.

June 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.

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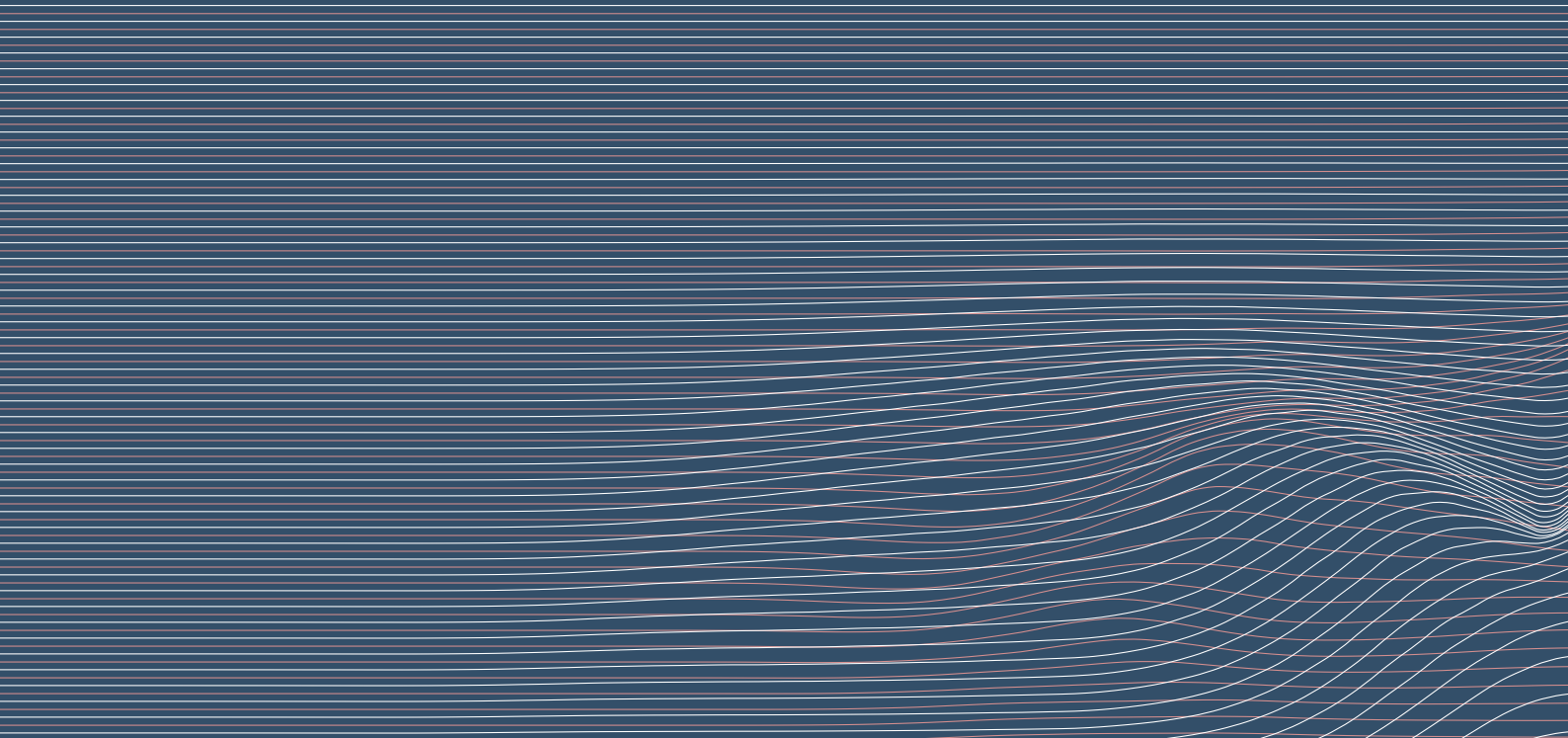
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