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Press release

Monetary policy assessment

The National Bank has not made any further change to its monetary policy in its assessment of 20 March 2003. It cut the target range for the three-month Libor by 0.5 percentage points to 0%-0.75% on 6 March 2003 and announced that the rate is to be kept in the lower part of the new target range, i.e. at 0.25%, for the time being. The temporary narrowing of the target band from 100 to 75 basis points was prompted by technical factors.

After the outbreak of the Iraq conflict, the economic and political environment remains extremely uncertain. The economic recovery in Switzerland expected for 2003 may be delayed. Given this difficult situation, the National Bank wishes decisively to counter the tightening of monetary conditions that would arise from an appreciation of the Swiss franc. Low inflation has meant that the National Bank has been able to relax its monetary policy significantly over the last two years. Since March 2001, it has cut the target band for the three-month Libor rate in a total of seven stages by 3.25 percentage points to its current level. At the present time, this expansive monetary policy does not pose any risk to price stability in Switzerland. Assuming that the three-month Libor rate will remain stable at 0.25%, average annual inflation is expected to lie between 0.7% and 1.9% in the next three years. The National Bank now anticipates that economic growth will be just under 1% for 2003.

Economic activity

Despite a difficult climate worldwide, economic activity in Switzerland stabilised somewhat during the second half of 2002. After falling between the third quarter of 2001 and the first quarter of 2002, real gross domestic product has since been edging up again on a quarter-on-quarter basis. Nonetheless, the fourth quarter of 2002 saw growth flatten off once more compared with the third quarter of the year. Exports and consumer spending were the main stabilising factors.

The economic situation in Switzerland remains tight, however, with growth staying below its potential level. The deterioration of the labour market is depressing consumer sentiment and disposable incomes. Incoming orders and the order backlog are still unsatisfactory, and there is insufficient capacity utilisation in the industrial and construction sectors. Capital spending remains in sharp decline.

There must be a sustainable recovery in exports and investment activity before Switzerland can return to higher real growth, and this cannot be expected until the global economy begins to pick up. The Swiss economy will thus expand only moderately up to mid-2003 and will not begin to accelerate somewhat until after this point. The National Bank anticipates that real gross national product will increase by just under 1% in 2003 as a whole.

Inflation and inflation forecast

Year-on-year inflation, as measured by the national consumer price index, rose to 1.0% in the fourth quarter of 2002 from 0.3% in the third quarter. In January and February 2003, it was 0.8% and 0.9% respectively. These fluctuations are due primarily to statistical effects. The core rate of inflation calculated by the National Bank (trimmed mean method), which is a reliable indicator of the inflation trend, has been around 1% for some time now.

At the end of 2002, the National Bank decided in future to publish its inflation forecast every quarter. This March forecast is the first of these. The graph shows both the inflation forecast of December 2002 (the dotted green curve) and the forecast of March 2003, drawn up after the latest interest rate cut (red dashed curve).

The National Bank's new inflation forecast is based on the assumption that growth in the US will pick up again from the second quarter of 2003 onward. The US economy is likely to grow more strongly in 2004 and again reach its potential output. In the EU, however, the recovery has been delayed, and growth rates of over 2% are not to be expected until 2004. Given the uncertain geopolitical situation, the price of oil is likely to fluctuate around USD 30 a barrel for some time yet, before coming back down to around USD 25 a barrel.

On the assumption that the three-month Libor rate will remain stable at 0.25% during the next three years, inflation should average 0.7% in 2003, moving up to 0.9% in 2004 and to 1.9% in 2005. Inflation is forecast to remain under 1% until mid-

2004. Thereafter, it will accelerate, reaching 2.5% in the fourth quarter of 2005. This is above the level that the National Bank equates with price stability. It should be noted that these forecasts assume that monetary policy will remain expansive over the next three years.

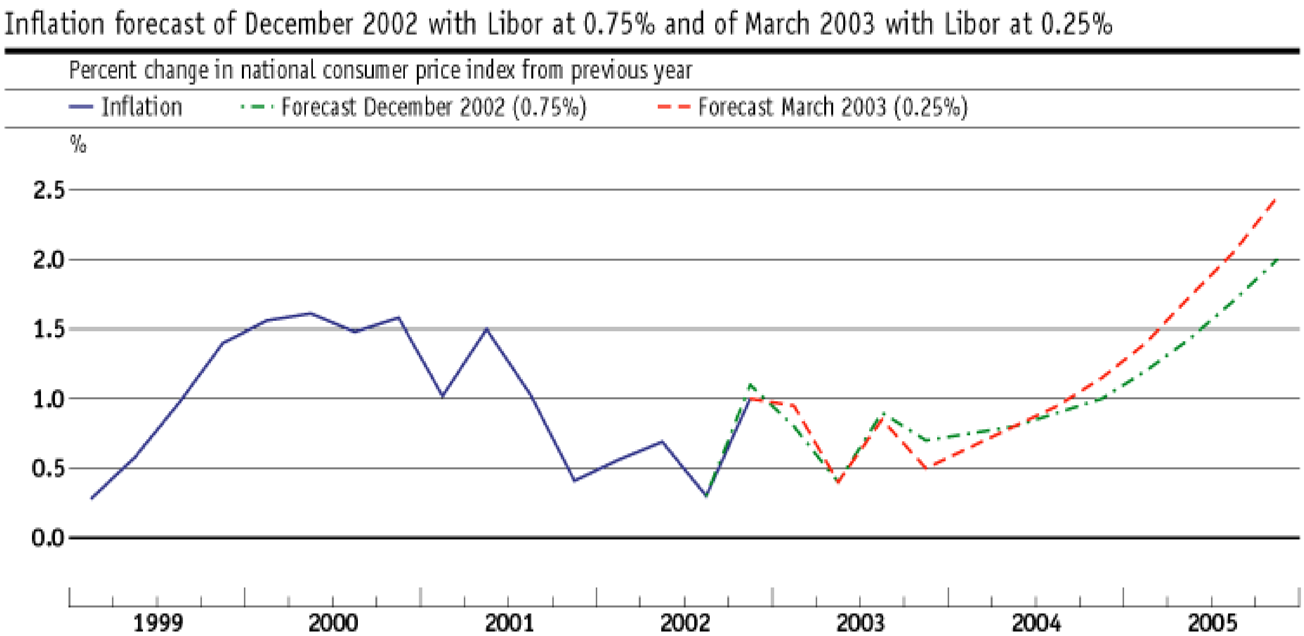
Despite the most recent interest rate cut, the new forecast up to mid-2004 is virtually the same as that published at the end of last year. In the short term, inflation will be held back by the delayed economic recovery and the weakness of the US dollar. In the new forecast, however, inflation rises more markedly at the end of the forecasting horizon owing to the more expansionary monetary policy.

Expansionary monetary policy

With its latest interest rate cut, the National Bank relaxed its policy significantly again and responded once more to increasing uncertainty about economic trends. In this critical phase, the aim of the National Bank is to support economic recovery in Switzerland and keep the attractiveness of Swiss franc investments at a low level.

As the risks are still pointing mainly downward, the National Bank intends to maintain its expansionary monetary policy. Under the current circumstances, it will endeavour to take decisive steps to counter a tightening of monetary conditions through the appreciation of the Swiss franc. In spite of the fact that money market rates are already very low, the National Bank still has effective instruments at its disposal. In particular, these include intervention on the foreign exchange market.

At present, the National Bank's highly expansionary monetary policy – as reflected in extraordinarily low interest rates and strong growth in monetary aggregates – poses no threat to price stability. The latest forecast expects inflation to rise to over 2% in the second half of 2005, given a constant interest rate of 0.25%. The National Bank nonetheless believes that it still has sufficient time to make later adjustments to its monetary policy, and that it can keep inflation within the price stability range.



Inflation Forecast March 2003 with Libor at 0.25%	2002	2003	2004	2005
Annual average inflation in %	0.6	0.7	0.9	1.9

Swiss National Bank