

## The economic situation from the vantage point of the delegates for regional economic relations

Summary report to the attention of the Governing Board of the Swiss National Bank for its quarterly assessment of June 2004

The Swiss National Bank's delegates for regional economic relations are constantly in touch with a large number of enterprises from the different industries and economic sectors. Their reports, which contain the subjective evaluations of these companies, are an important additional source of information for assessing the economic situation. In the following, the main results of the talks held from March to May 2004 on the current and future economic situation are summarised.

## Summary

There was a further improvement in corporate sentiment and in the general business situation from March to May. The economic recovery became more broad-based and gradually spread to companies that focus on the domestic market. Exports, however, continued to be the main driving force. In the service sector, the turnaround in tourism – and, to a lesser extent, in the company-related services segment – was confirmed. The retail trade benefited from the gradual improvement in the consumer climate, which resulted above all in rising sales of consumer durables. The construction companies were satisfied with the level of residential construction but have not yet seen any rebound in commercial construction.

A number of indicators point to a gradual rise in investor confidence. The earnings situation has improved and some companies have now reached their capacity limits. In addition, some companies have already increased their workforce or are considering doing so. Many industries were affected by the surge in raw material prices but for the most part were unable to pass on the higher costs.

The companies surveyed were still guardedly optimistic in their outlook for the economy; for the current year, most of them are expecting stable or rising turnover. Scepticism about the sustainability of the economic pickup, which was still widespread at the beginning of the year, has waned.

# 1 Production

## **Manufacturing**

Most export-oriented industries have recorded a further pickup in business activity since the talks held in February. A number of companies are now working to capacity and have a solid orders backlog. Demand from Asia remained brisk while incoming orders from the US were rather disappointing for many companies. After the dollar had regained some ground, complaints about the low dollar exchange rate declined. Increasingly, the companies reported higher demand from the EU, particularly from southern Europe; in some areas, demand from Germany has also revived somewhat recently.

In addition to the relatively non-cyclical chemicals/pharmaceuticals industry, the representatives from the specialty chemicals and plastics industries now also reported a pickup in business. The medical technology segment has continued to develop favourably, though this industry is beginning to be affected by cost-cutting pressures in the health care sector.

The metal manufacturing industry is on the road to recovery. It has benefited from the vibrant demand for concrete-reinforcing and quality steel from Switzerland and abroad (China). Business activity in the electronics segment has also trended stronger. The mechanical and electrical engineering industries, by contrast, are recovering at a somewhat slower pace. However, suppliers for the automotive industry in particular saw a surge in incoming orders. Manufacturers of textile machinery, which are heavily geared to the Asian market, were still very positive in their assessment. In general, the mechanical engineering industry faces fierce competition from increasingly high-quality imports and has to contend with extremely price-conscious customers. The watch-making industry was also satisfied with the business situation, as it was able to increase its first-quarter exports significantly; this also benefited the suppliers. Stocks of finished products and components in the watchmaking industry have now been reduced to a normal level.

## **Services**

In the retail trade, signs of a rebound multiplied in April and May, but consumers remained price-conscious and selective. The big trade fairs in Basel and Geneva yielded much better results than expected. In general, demand for consumer durables and luxury items seems to be reviving gradually. On the back of the weaker CHF/EUR exchange rate, shopping in the regions bordering Switzerland has become somewhat less attractive.

The situation in tourism is brightening slowly. While the number of visitors from Asia and the US has risen, demand from the EU has remained slack as yet. Overall, the catering trade's summer-season predictions were guardedly optimistic. The pickup in tourism has also benefited the airlines, which reported rising passenger numbers.

The business situation of trading and consulting companies in the IT and computer segment has started to brighten. This industry is expecting demand to pick up significantly as a large amount of pent-up demand has accumulated since the pre-Millennium investment boom. Likewise, the fields of company and project financing have seen gradual signs of a recovery. By contrast, the advertising industry has not yet turned the corner.

The level of business reported by the banks ranges from good to excellent; at the same time, though, they have encountered fiercer competition. The banks have benefited in particular from the vibrant demand for mortgages and from the recovery on the financial markets. Demand for corporate loans, however, hardly strengthened. Banks in Ticino in particular have felt the strong pressure on commissions and have been confronted with increasingly price-sensitive customers from abroad.

## **Construction**

The construction industry has felt the revival in residential construction, which had already been signalled by the rising number of building permits last year. Commercial construction still failed to provide any stimuli. A number of public construction projects have been approved, but their implementation has in many cases been delayed by pressure to cut public spending. Construction activity is still strongest in the agglomerations; moreover, the harsh price competition has continued unabated. Owing to the large amount of renovation work in progress, construction-related industries have enjoyed a healthy level of business.

## 2 Labour market

With business activity more lively, some companies have hired new staff, albeit partly on a temporary basis. While a number of the companies surveyed considered increasing their workforce, a recruitment wave is not yet imminent.

## 3 Prices, margins and earnings situation

The earnings situation of many companies has improved. In general, however, companies were still not reporting much scope for price increases. Many of them mentioned the surge in energy and raw materials prices (oil, steel, cellulose and raw cotton). Only few companies were able to pass on the higher costs. An exception was the metals industry, which – given the brisk demand – had no problem pushing through higher steel prices.

The favourable CHF/EUR exchange rate has had a positive effect on the export sector and lowered the pressure from imports. Many companies were nevertheless exposed to relentlessly strong price competition, which they tried to counter by increasing volumes and productivity. Shifting production to Eastern Europe or Asia was mentioned repeatedly.