

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 December 2006

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 most important results of the talks held from September to November 2006 on the current and future economic situation are summarised.

Summary

The talks held by the SNB delegates for regional economic relations with around 140 representatives from various economic sectors and industries from September to November 2006 yielded a picture of an economy that was in excellent shape. Right through to the end of the period, the companies surveyed detected no evidence of any slowing trend, and in some cases even stated that business was accelerating. The most flourishing sectors included the export industry, tourism, construction and the banks. By contrast, the retail trade presented a muted picture. Prospects for 2007

were viewed as positive. While a number of respondents were expecting a slowdown in the pace of expansion, they considered this part of the process of 'returning to normal'.

Helped by the generally high level of earnings, companies showed a greater propensity to invest. As before, however, investment projects were scrutinised carefully, with consideration also given to alternatives such as relocating some production facilities. A mood of caution also continued to permeate the question of permanent hirings. Increasing problems with the procurement of commodities were cited as a primary concern.

1 Production

Manufacturing

Most export companies reported a persistently firm level of new orders and full order books, in many cases guaranteeing capacity utilisation until well into the new year. Demand remained broad-based. Respondents stressed the strong business trend in the EU region, specifically in Germany and in the East European countries. Demand from Asia, Latin America and the US also showed a positive trend. Suppliers of products destined for the US construction and automotive industries nevertheless detected a significant slowdown in new orders. Many respondents spoke of supply bottlenecks in the case of primary products, which in turn resulted in extended delivery times for their customers. They expressed concern about developments on the commodity markets. Alongside higher prices for key raw materials such as metals, steel and timber, there was mention of the growing difficulties in obtaining the required quantities within a reasonable time frame.

The healthy business climate extended across all sectors. Energy technology benefited from considerably higher capital investment on the part of the petrochemical and electricity sectors. Representatives of the metalworking industry, medical technology, civil aviation and a broad segment of mechanical engineering also expressed satisfaction with the way sales were developing. Moreover, excellent levels of business were reported by suppliers of upmarket consumer products, including the watchmaking industry and the luxury end of the food, clothing and fashion accessories sectors.

Services

Representatives of the tourism and hospitality industries were able to look back on a successful summer season. The fine autumn weather was more than sufficient to offset the impact of a rainy August. Both the number of guests and the average expenditure per guest rose by a gratifying margin. 2006 has so far been a record year for the city tourism sector. There was widespread optimism about the forthcoming winter season, as a large volume of bookings had already been received by the autumn.

The travel industry and transportation sector, and aviation in particular, also reported a good to excellent business trend. Load factors and average

revenue per passenger kilometre both rose significantly. Suppliers of business services also made positive statements. While the business consultancy sector in general has been enjoying an upswing for some time now, representatives of the ICT sector are also beginning to note a significant increase in the willingness to invest – albeit against a backdrop of persistently heavy pressure on prices.

Respondents from the banking sector saw no signs of a downturn in economic activity. Commission and fee business showed a pleasing trend, driven partly by the stock market recovery. Mortgage business expanded despite higher interest rates, though margin pressures remained high. Most representatives reported an improvement on the corporate banking side. Profitability among corporate clients was judged to be very strong, thereby improving the quality of the banks' loan books. The abundant liquidity provided an opportunity for many corporate clients to repay their bank loans. As for customer deposits, there was evidence of a switch to higher-interest products. Views on developments in the real estate sector were again mixed. Some respondents witnessed signs of overheating, while others stressed the speed at which new properties could be sold or let even though a large number were being built.

Views also diverged in relation to private consumption. While representatives of B2C services expressed satisfaction with the way business was progressing, a majority of spokespersons for the retail trade viewed the situation as muted. Although the number of customers and their willingness to spend increased, the sales trend remained volatile. On top of that, demand presented a very mixed picture in terms of the different price segments. In general, sales in the top and bottom price brackets were distinctly firmer, whereas the middle segment was sluggish. At the major retailers, price cuts for food and other day-to-day items depressed the nominal sales figures. Despite a difficult business situation in some areas, most respondents were optimistic about Christmas trading following the encouraging level of sales in November.

Construction

Representatives of the construction sector rated the utilisation rate and order backlog as good to excellent. Residential construction was once again the principal driving force; commercial con-

struction and civil engineering, together with a high level of renovation activity, are now providing an additional fillip, however. To some extent, the healthy order situation afforded companies the luxury of being selective when deciding which contracts to take on. Prospects were viewed as positive. None of the respondents expected the trend to reverse in the near future. A small number mentioned signs of saturation in the new residential construction sector, pointing in particular to dwindling land reserves.

2 Labour market

Many companies increased their staffing levels. In most cases, however, the expansion was incremental and only came about following in-depth analysis of longer-term staffing requirements. Spikes in production were generally countered by hiring temporary personnel. In the few instances where staffing levels increased sharply, the firms in question were expanding into foreign markets for the first time. Recruitment firms mentioned a rise in staff turnover, especially among middle and senior management. Recruitment of specialist technical personnel continued to pose problems, with senior managers in particular proving very difficult to find. In addition, the labour market in regions close to the German and French borders has now dried up at this level.

3 Prices, margins and earnings situation

Most representatives found that profitability had improved significantly. While export-oriented firms in particular continued to face downward pressure on prices, this does appear to be easing. A number of companies were able to pass on higher costs for energy and raw materials, or improve their margins through selective customer acquisition and/or marketing efforts. In many instances, price increases were considered inevitable in 2007 in order to offset rising costs. Representatives of the construction sector continued to see only limited opportunities to raise prices, and in some cases reported a deterioration in profitability as a consequence of higher wage and material costs. On the other hand, clients frequently cited significantly higher construction prices. This contrasting picture may reflect the fact that discounts are now almost impossible to obtain, which the construction firms do not necessarily view as a rise in prices.

Companies were expecting larger wage increases for 2007 compared with the previous year, with most quoting figures in the region of 2.0% to 2.5%. No discernible differences were identified between the sectors.

The current euro exchange rate of around 1.60 Swiss francs offers clear benefits for most of the companies surveyed, and in some cases facilitates considerable margin gains. Companies nonetheless remain cautious, and are basing their calculations on a significantly lower euro exchange rate. The fate of the dollar is being watched with some concern.