

# 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 2007

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 March to May 2007 on the current and future economic situation are summarised.

## Summary

The talks held by the SNB delegates for regional economic relations with around 160 representatives from various economic sectors and industries conveyed a picture of an economy with virtually no problems in the period from March to May 2007. The first few months of the year significantly exceeded the expectations of many of the companies surveyed. There were no signs of a slowdown in sight; indeed some respondents even reported an acceleration in business activity. Moreover, this upbeat sentiment was found in all sectors, including companies which had only recently been struggling with problems.

By and large, capacity is utilised to a very high degree and the market situation is increasingly making it possible to raise prices. Investment is taking place and additional staff are being taken on, but respondents are adopting a prudent approach as they expect the pace of growth to normalise sooner or later. Many are therefore attempting to deal with the high order volume by outsourcing some of their production, rather than permanently expanding in-house capacity. However, many of these outside suppliers are now also coming up against capacity limits. Respondents continued to cite massive price hikes and procurement problems affecting commodities and primary products as their main concern and there were more frequent references to capacity bottlenecks.

# 1 Production

## Manufacturing

The companies surveyed in industry were very pleased with the volume of orders received since the beginning of the year. In most cases, budget targets were achieved or even exceeded. Sales were often well above year-back levels, raising the prospect of another record year. Demand remained broad-based, with no sign of a slowdown in sight. The most important impetus is currently coming from the EU, particularly from Germany, which has now seen an increase in consumer demand as well as investment demand. While demand from Asia (in particular China) and Eastern Europe remained strong, some companies said they had felt the impact of the economic slowdown in the US. Against a background of capacity bottlenecks, delays in deliveries and rising commodity and primary product prices, many spoke of overheating.

The boom in the manufacturing sector has now taken hold of all sectors and their suppliers. A particularly dynamic trend was in evidence in the energy sector, which is benefiting from a large backlog of demand for investment in power generation plants and growing demand for alternative energy sources. However, the mechanical engineering industry is also enjoying an upturn across a broad range of segments, as is the consumer goods industry. In addition to the booming watchmaking industry, sectors such as textiles and foodstuffs, which in some cases had been facing problems in the past years, are also benefiting increasingly from the economic upswing in Switzerland and abroad.

## Services

For some time now, retailers have also been feeling the impact of the upturn, though this took some time to kick in. The representatives of this sector expressed satisfaction with the trend of business during the first few months of the year. Consumer sentiment has improved markedly in all segments – notably in non-food areas – and turnover is up on last year despite lower prices. Retailers in Switzerland's border regions benefited from the softening of the Swiss franc against the euro, which reversed the flow of cross-border shopping in favour of domestic outlets.

Despite a serious shortage of snow, representatives of the hospitality trade were satisfied with last winter's season and were optimistic about the prospects for the summer. The fine spring weather

led to large numbers of guests in many locations and booking levels for the summer season look promising. In general, respondents reported significantly higher spending and longer stays. They also mentioned an increase in seminar and conference-related tourism, which is giving a further boost to city tourism in particular. At some destinations, hotels are now coming up against capacity limits.

A consistently positive picture also emerged from the talks with other service providers from the consumer and corporate sectors. This includes airlines, which reported significantly brisker activity than a year ago. The rest of the transport sector, consultancy service providers, the IT sector, logistics operators and travel companies were also very satisfied with the way business was developing.

The representatives of the banking sector continued to speak of a very gratifying trend. Asset investment and trading business were booming, as was mortgage business. However, in the mortgage segment, competition is reported to be persistently strong and margins are seen as low. The corporate clients segment was more subdued. Many clients have high levels of liquidity which they are using to pay off loans.

## Construction and real estate

The representatives of the construction industry reported buoyant business conditions, particularly in the housing sector. Capacity utilisation in both the construction industry proper and in related trades is tight, so in the case of private sector contracts, in particular, it is now becoming possible to push through price increases. Business is showing no sign of slowing down, although now and again some respondents mentioned saturation tendencies, particularly in relation to owner-occupied apartments. Signs of this can be seen in the growing numbers of vacant apartments in old buildings and in the postponement of projects. Like residential construction, the commercial and industrial construction segment also enjoyed a satisfactory to positive trend, whereas the situation in the civil engineering sector was mostly assessed as unsatisfactory. When questioned about the real estate market, the companies surveyed noted that there had been no let-up in the strong foreign demand for second homes in good locations and that prices were continuing to rise in this segment.

## 2 Labour market

Many companies have increased their staffing levels in recent months. Banking specialists and technical personnel are particularly in demand. However, some respondents were wary of expanding staff numbers permanently and preferred to opt for temporary personnel.

There are wide variations in assessments of the availability of staff. Some respondents thought there was a serious shortage of specialists, whereas others mentioned that although it was not easy to recruit specialists, they were still able to find people with the skills they needed. The situation has been significantly eased by the fact that staff can now be recruited in the EU, although the economic recovery has made it more difficult to find suitable staff there as well.

On the question of pay trends, many respondents reported noticing increasing pressure on salaries. However, given the positive trend of business and the favourable earnings situation, this does not appear to be a source of great concern. Various respondents also said that they were enabling employees to share in the positive business trend with bonus payments.

## 3 Prices, margins and earnings situation

Most representatives spoke of positive to very positive profitability, although the margins of industrial companies are being squeezed by the sharp rises in the price of commodities and primary products (particularly high-grade steel). Companies facing strong competition are still finding it hard to pass on higher costs to consumers. These companies, however, also see stable selling prices as a means of rewarding customer loyalty.

Across all sectors, the scope for price adjustments appears to have increased thanks to the positive economic situation. The exceptions include the retail sector, and in particular major retail chains and their suppliers, where prices remain under pressure and further price reductions are planned.

The strengthening of the euro against the Swiss franc is a welcome development for respondents from the export sector. Several took advantage of this to increase their prices in Swiss franc terms. In particular, it enabled them to offset the rise in commodity prices. Some companies that mainly export to the dollar zone expressed concern about the dollar's exchange rate.