
Business cycle signals

Results of the SNB company talks

Second quarter of 2017

Report submitted to the Governing Board of the Swiss National Bank for its quarterly assessment.

The appraisals presented here are based on discussions between the SNB's delegates for regional economic relations and company managers. A total of 240 company talks were conducted between mid-April and the end of May.

Regions

Central Switzerland
Eastern Switzerland
Geneva
Italian-speaking Switzerland
Mittelland
Northwestern Switzerland
Vaud-Valais
Zurich

Delegates

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Key points

- Interviews conducted with companies in the second quarter paint the picture of a recovering Swiss economy. In addition, the outlook for the coming six months continues to improve.
- Real turnover made further moderate gains on the preceding quarter. In a year-on-year comparison, turnover growth increased. This was especially apparent in manufacturing.
- Companies' utilisation of production capacity rose, although it is still slightly below normal levels. While the margin situation has improved noticeably since the end of 2015, on the whole margins remain tighter than usual, with considerable differences being reported from one company to another.
- For the second half of the year, the company representatives expect real turnover to rise more strongly. This is largely due to the more favourable international economic situation, but also to the relatively stable exchange rate conditions.
- In the coming months, companies plan to slightly increase investment expenditure as well as staff numbers.
- The chief uncertainties reported were geopolitical risks and the possibility of burgeoning protectionism.

CURRENT SITUATION

Further rise in turnover

The results of the company talks conducted during the second quarter show that the gradual recovery of the Swiss economy is continuing.

Company representatives reported further moderate gains on the previous quarter in real (i.e. adjusted for changes in sale prices) turnover (cf. chart 1; for guidance on interpreting the charts, see the corresponding section at the end of this report). These gains were reflected across all three sectors, i.e. services, manufacturing and construction.

In a year-on-year comparison, growth in turnover accelerated in the second quarter. Manufacturing, in particular, recorded noticeably higher real turnover than in 2016. These results reflect the revival in manufacturing activity observed since last autumn.

The primary driver behind turnover growth was export business. Most export industries are experiencing a stronger dynamic. Europe, especially Germany and Scandinavia, is a notable sales market. Stronger demand is also being felt from Italy, France and Spain, but also from Russia. In addition, the US, Southeast Asia, China, Japan and the Arab region were reported as drivers behind this development. Business is particularly good for companies supplying goods to the automotive and healthcare industries.

Lower underutilisation

The utilisation of technical production capacity declined from the beginning of 2014 until mid-2016, before

stabilising thereafter (cf. chart 2). This was the net result of two opposing trends in capacity utilisation, namely an improvement in the case of manufacturing (having started from a low level) and a slight deterioration in construction. The results for the second quarter indicate significantly higher utilisation now, in line with improved business performance. Overall, however, capacity utilisation remains below the level regarded as normal, with 31% of the companies visited reporting utilisation as being lower than usual (compared with 39% last quarter). Both services and manufacturing are affected.

Staff numbers adequate

Across all three sectors, staff numbers are currently considered to be in line with demand. This confirms the assessment made in the first quarter. In the course of 2016, staff numbers were still considered rather too high.

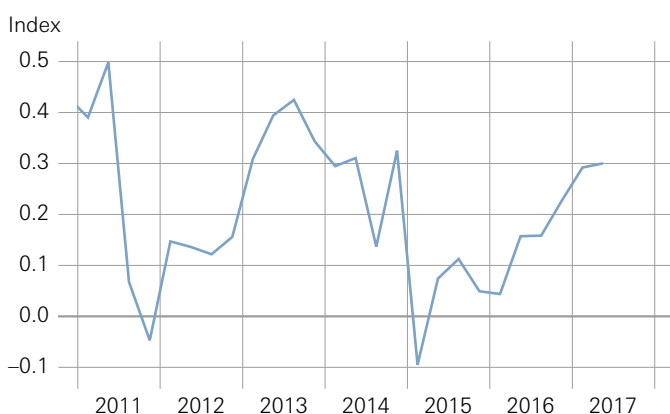
While companies are still hiring temporary staff to manage workload peaks, more permanent positions are also being offered.

Pressure on margins persists

The assessment of the margin situation compared to the previous quarter has hardly changed. Overall, profit margins remain below what the company representatives regard as usual. This applies to all three sectors. Within the sectors, however, the margin situation varies considerably from one company to another. This can be attributed to various factors. First, certain markets are still suffering from modest demand due to cyclical factors. Second, not all companies were able to react to the same extent to the appreciation of the Swiss franc. And third, some industries and companies face specific structural challenges.

Chart 1

TURNOVER COMPARED TO PREVIOUS QUARTER



Developments in real turnover compared to the previous quarter. Positive (negative) index values signal an increase (decrease). Source: SNB

Chart 2

CAPACITY UTILISATION



Current utilisation of technical capacity or infrastructure compared to a normal level. A positive (negative) index value signals a higher (lower) utilisation than normal. Source: SNB

DEVELOPMENTS IN INDIVIDUAL INDUSTRIES

Trade continues to be affected by structural phenomena such as cross-border shopping and the shift to online purchases. While the situation in retail has not greatly improved, companies in wholesale trade reported slightly higher real turnover than in the previous quarter, and improved utilisation.

The hotel and hospitality industries recorded substantial gains in real turnover compared to the previous quarter. This was partially due to Easter falling in the second quarter this year. Underutilisation of infrastructure has receded. Switzerland's reputation as a safe destination has helped demand.

In the finance sector too, business momentum has slightly picked up. However, infrastructure (office and retail space as well as IT capacity) continues to be underutilised or oversized, and margins remain under pressure. Companies in commission business have profited from favourable stock market conditions, although the low interest rate environment continues to be a challenge. Banks still consider themselves somewhat overstaffed.

Companies in the ICT industry continue to report strong business activity, with high growth in turnover, solid utilisation, favourable margin situations and expansive hiring plans. Factors contributing to this situation include advances in automation, digitalisation, but also regulatory influences, as well as higher risks of cyber attacks.

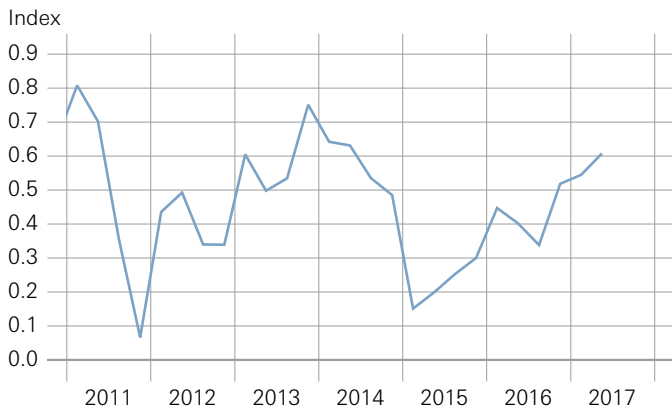
In manufacturing, the situation is brightening further. Companies in the metal processing and machinery industries and producers of precision instruments report higher turnover quarter-on-quarter. There are early signs that the situation in the watchmaking industry is bottoming out, although production capacity continues to be underutilised and pressure on margins remains high. Companies in food production as well as in metals and plastic processing have recorded tighter than usual margins.

In construction, business performance is rated as positive, both in the main construction and finishing trades, although there was talk in a number of regions of intensified predatory competition. Qualified staff are very hard to find.

Digitalisation was a topic of conversation in numerous industries, with practically all companies giving it thought. In the majority of cases, companies associate it with opportunities.

Chart 3

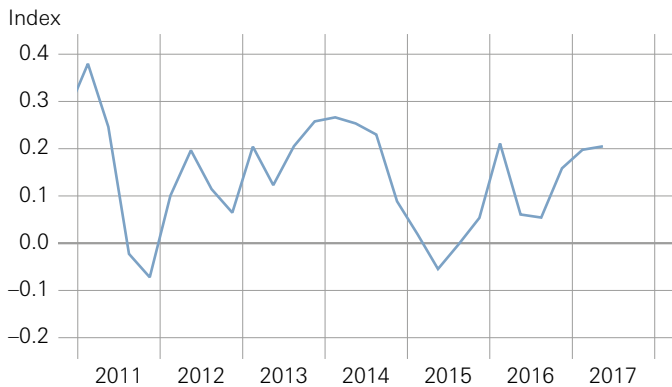
EXPECTED TURNOVER



Expected developments in real turnover in the coming six months. Positive (negative) index values indicate higher (lower) turnover expectations. Source: SNB

Chart 4

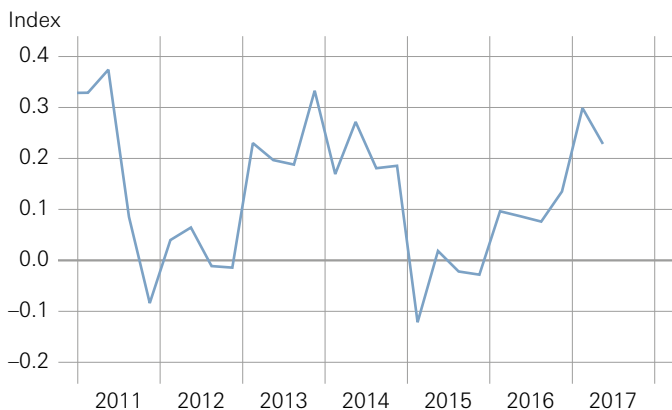
EXPECTED CAPACITY UTILISATION



Expected developments in utilisation of technical capacity or infrastructure in the coming six months. Positive (negative) index values indicate higher (lower) utilisation expectations. Source: SNB

Chart 5

EXPECTED EMPLOYMENT



Expected developments in staff numbers in the coming six months. Positive (negative) index values indicate higher (lower) expectations. Source: SNB

OUTLOOK

Greater confidence

The company representatives are generally optimistic about business prospects in the coming six months. They expect a further rise in real turnover (cf. chart 3). This applies to all three sectors. Their assessment is mainly based on the more favourable global economic outlook, although the relatively stable exchange rate conditions and the effects of measures implemented to boost efficiency have played an additional, important role.

This confidence is also evident in the anticipation of slightly higher utilisation of technical production capacity and infrastructure in the next six months (cf. chart 4), as well as in a slightly greater willingness to invest, particularly in equipment. A third of companies who invest in equipment thereby also expand their production capacity.

In the coming six months, company representatives expect few changes in purchase and sale prices. This confirms the stabilisation evident in recent quarters. In certain cases, companies are considering an increase in sale prices in the coming months, which some have justified based on higher raw material prices.

Slight increase in staff planned

The prospects of higher capacity utilisation are also affecting recruitment plans, with companies intending to raise staff numbers somewhat (cf. chart 5). This applies to all three sectors.

Wages slightly up

Based on information provided by the company representatives, the wage increases made so far for 2017 are just over 0.8% on average.

ENVIRONMENT AND RISKS

When asked about potential dangers, companies mainly expressed concern about geopolitical risks and protectionist tendencies. With regard to Europe, risk perceptions eased following the presidential election in France. Domestically, the increasingly complex regulatory environment was perceived as a burden. Cybercrime was frequently mentioned as a threat. Company-specific factors were discussed more often than previously. The new energy strategy of the Swiss Confederation was mostly associated with opportunities, and only occasionally with risks. With reference to growing vacancy rates in residential property, some company representatives expressed concerns about developments in the real estate market. It was noted that the considerable investment needs of institutional investors were making themselves felt.

Most companies have been able to come to terms with the current exchange rate conditions. The stability on the foreign exchange market is welcomed. At the same time, a renewed appreciation of the Swiss franc would be a source of concern.

Many company representatives consider the low interest rate environment as problematic in relation to the long-term position of pension funds.

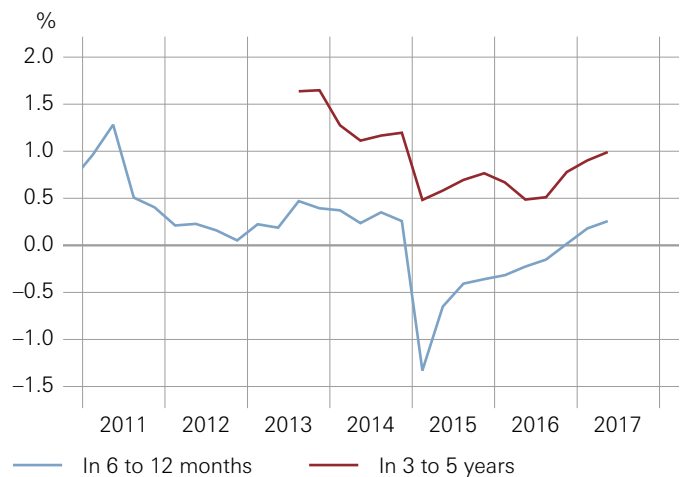
INFLATION EXPECTATIONS

As part of the exchange of views, the delegates also regularly ask company representatives about their short and long-term inflation expectations as consumers, in terms of the consumer price index.

At the beginning of 2015, both short and medium-term inflation expectations dipped sharply in the wake of the Swiss franc's strong appreciation. In the interim, however, both have gradually risen again. Inflation expectations continue to trend upwards in the second quarter, with average expectations for the next six to twelve months increasing from 0.2% in the previous quarter to 0.3%, and those for the next three to five years from 0.9% to 1.0% (these short and medium-term expectations are represented in chart 6 by the blue and red lines, respectively). The inflation expectations are thus back at levels comparable to those at the end of 2014.

Chart 6

EXPECTED INFLATION



Source: SNB

About this report

Approach

Each quarter, the SNB's delegates for regional economic relations hold talks with managers of companies throughout Switzerland. The main results of these discussions are summarised in the 'Business cycle signals' report.

Approximately 240 companies are visited every quarter. The selection of companies reflects the industrial structure of the Swiss economy based on GDP and employment. Industries subject to stronger cyclical fluctuations are somewhat over-represented, while the public sector and agriculture are not taken into consideration. Different companies are visited from one quarter to the next.

In the talks, the SNB's delegates capture primarily qualitative information. The discussions are nevertheless structured in such a way as to allow the delegates to grade a part of the received qualitative information according to a numeric scale. This enables the results to be aggregated and represented graphically.

The five-tier scale ranges from 'substantially higher' or 'much too high' (+2), 'slightly higher' or 'somewhat high' (+1), 'the same' or 'normal' (0), 'slightly lower' or 'somewhat low' (-1), to 'substantially lower' or 'much too low' (-2).

Interpreting the charts

The charts are to be regarded as a numeric summary of the qualitative information received. The index value shown represents the average of the findings from all companies visited. When interpreting the curves, particular relevance should be attached to their overall development, rather than to their numeric level or individual changes.

Additional information

Further information on the 'Business cycle signals' report is available at www.snb.ch, *The SNB*, *SNB regional network*.