
Business cycle signals

Results of the SNB company talks

Third 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 213 company talks were conducted between mid-July and the end of August.

Regions

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

Delegates

Jean-Marc Falter
Fabio Bossi
Roland Scheurer
Daniel Hanimann
Urs Schönholzer
Aline Chabloz
Walter Näf
Rita Kobel

Key points

- Interviews conducted with companies in the third quarter suggest Switzerland's economic situation is brightening appreciably and that the outlook for the next six months remains favourable.
- Quarter-on-quarter, real turnover once again increased – and year-on-year, it even increased significantly.
- Companies' utilisation of technical production capacity is now close to normal levels, however some industries undoubtedly still face difficulties.
- Margins continue to improve, but on the whole they remain below what company representatives regard as usual.
- Company managers expect real turnover to continue rising in the coming six months thanks in large part to the more favourable international economic situation.
- There is a noticeable uptick in companies' willingness to invest as well as in their demand for staff.
- Company representatives rate the international environment as less uncertain than during the second quarter, however they are cautious in their assessment of recent exchange rate developments.

CURRENT SITUATION

Stronger turnover growth

Discussions with companies in the third quarter suggest that economic activity in Switzerland is continuing to gather pace, most notably in manufacturing.

Company representatives reported robust quarter-on-quarter growth in real turnover, i.e. turnover adjusted for changes in sale prices (cf. chart 1; for guidance on interpreting the charts, see the relevant section at the end of this chapter). Year-on-year, turnover was even significantly higher. These gains were broad based in that they were observable across all three sectors, i.e. services, manufacturing and construction.

Turnover growth was principally driven by exports, with most export industries enjoying solid and sustained momentum. Sales to various European countries are strong and company representatives also mention Asia, especially China, as an important growth driver. Signals from the US are mixed but predominantly positive. Business is particularly dynamic for companies supplying goods to the automotive and railway industries as well as to healthcare and aviation.

In addition to strong exports, companies reported somewhat brisker domestic sales.

Capacity utilisation close to normal

Having deteriorated between the beginning of 2014 and mid-2016 (cf. chart 2), the utilisation of technical production capacity stabilised from the second half of 2016. Since then, underutilisation has been falling consistently.

Half of the companies interviewed rated their technical capacity utilisation as normal. Of the remaining 50%, around half reported underutilisation and half overutilisation. Certain firms have added more shifts to meet increased demand.

Staff numbers adequate

As in the two previous quarters, staff numbers are currently considered to be in line with demand across all three sectors. In the course of 2016, staff numbers were still considered somewhat too high.

While in the previous quarter managers had reported that recruitment was as challenging as ever, in the quarter under review they noted that hiring had become more difficult. In particular, they claim they have seen a decline in the availability of staff from Germany. A further observation was that companies are increasingly poaching staff from one another.

Lower margin pressure

Margins continue to follow the trajectory of normalisation that began in early 2016, with rising sales volumes playing a major role. On the whole, profit margins remain below what the company representatives regard as usual; nevertheless, their overall assessment is now on a par with their assessment prior to the discontinuation of the minimum exchange rate against the euro. Margins continue to vary widely within the sectors and between companies.

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

While the situation has improved slightly, trade continues to be affected by structural changes, such as the shift to online shopping. Industries and segments that have hitherto not offered their products on the internet are now also jumping on this bandwagon. The environment for stationary retail remains challenging – there is talk of an ‘overstore’ (too many shops) in some areas. Notwithstanding this, there are some signs that price erosion may be slowing or stopping altogether. In wholesale trade, the trend points towards slightly increasing real turnover and improved capacity utilisation.

The finance sector once again made a positive showing. Margin pressure remains, but it is falling in places thanks to cost-cutting measures. Infrastructure (office and retail space as well as IT capacity) continues to be underutilised or oversized; companies are thus typically reducing their store count. Companies in commission business have profited from ongoing favourable stock market conditions, although the low interest rate environment continues to be a challenge.

The hotel industry reported very strong third-quarter performance. Tourism has increased in various regions, with Switzerland’s reputation as a safe destination helping to stimulate demand. Infrastructure utilisation has practically returned to normal and margins have improved considerably, not least due to cost savings and, where possible, price increases.

The ICT industry, which had already reported very strong performance and high turnover growth in previous quarters, recorded a substantial year-on-year turnover increase in the third quarter.

The situation continues to brighten in manufacturing, with the majority of industries reporting higher turnover than in the previous quarter. Signs that the watchmaking industry was emerging from its low have been confirmed, although production capacity continues to be underutilised and margin pressure persists. Companies in food production as well as in metal and plastic processing, mechanical engineering and energy supply have also recorded tighter-than-usual margins.

In construction, in both the building industry and ancillary trades, business performance remains positive. There was once again talk in a number of regions of intensified predatory competition.

Digitalisation and cybersecurity are a focus of concern in numerous industries, with virtually all companies giving thought to the subject and/or initiating projects.

Chart 3

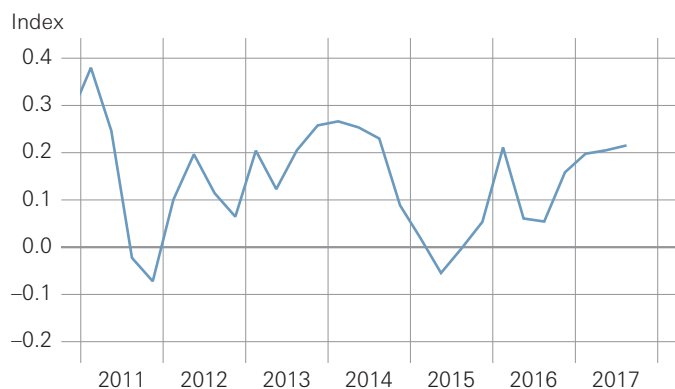
EXPECTED TURNOVER



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

Chart 4

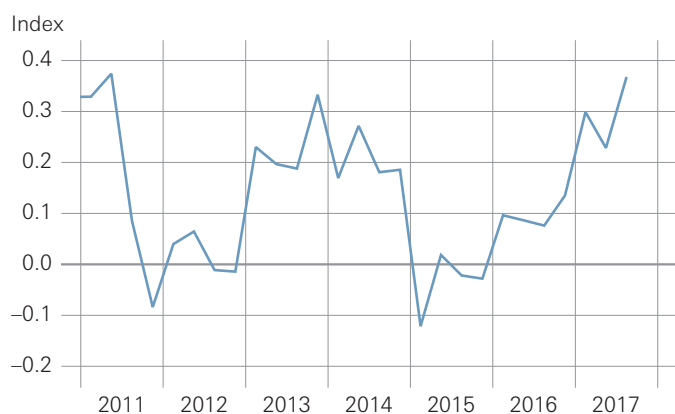
EXPECTED CAPACITY UTILISATION



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

Continued confidence

The company representatives interviewed by the SNB remain optimistic about their business prospects for the coming six months; real turnover is expected to rise in all three sectors (cf. chart 3). This assessment is principally based on the favourable global economic outlook. Companies also highlighted the importance of somewhat more advantageous exchange rate conditions – notably a stronger euro – and the clear effects of efficiency drives.

The confidence of company representatives is also reflected in slightly higher expected utilisation of technical production capacity and/or infrastructure in the next two quarters (cf. chart 4). Their willingness to invest – both in equipment and in buildings – has likewise increased notably compared to previous quarters. In investing in equipment, over a quarter of the companies are simultaneously expanding their production capacity.

For the first time since the beginning of 2014, the managers interviewed by the SNB say they expect to see a slight uptrend in both purchase and sales prices over the coming six months. They attribute this partly to higher prices for raw materials.

Moderate staff increases planned

The prospect of higher capacity utilisation is also affecting companies' recruitment plans: company representatives are planning moderate increases in staff numbers (cf. chart 5); these increases will affect all three sectors, but especially services. Manufacturing companies remain slightly more cautious on the hiring front.

ENVIRONMENT AND RISKS

Company representatives rate the environment as less uncertain than during the second quarter. While risks in Europe are perceived as having receded further, the consequences of Brexit remain hard to quantify. When asked about potential dangers, companies mainly expressed concern about geopolitical risks and, to a lesser extent, protectionist tendencies. Domestically, the complex regulatory environment is perceived as a burden and cybercrime was mentioned as a serious threat in certain segments. Company representatives are counting on a pragmatic outcome with respect to corporate tax reform.

Some company representatives see the low interest rate environment as problematic for the long-term position of pension funds. They also indicated some unease regarding the effects of low interest rates on the real estate market. It was noted that the considerable investment needs of institutional investors are making themselves felt. Growing vacancy rates in residential property are also a concern.

While the weakening of the Swiss franc against the euro during the third quarter was welcomed by most of the company representatives, caution prevails, as the movement will only have an effect if it turns out to be sustainable. The large majority of those surveyed said the impact of the weaker Swiss franc had yet to feed through to their businesses.

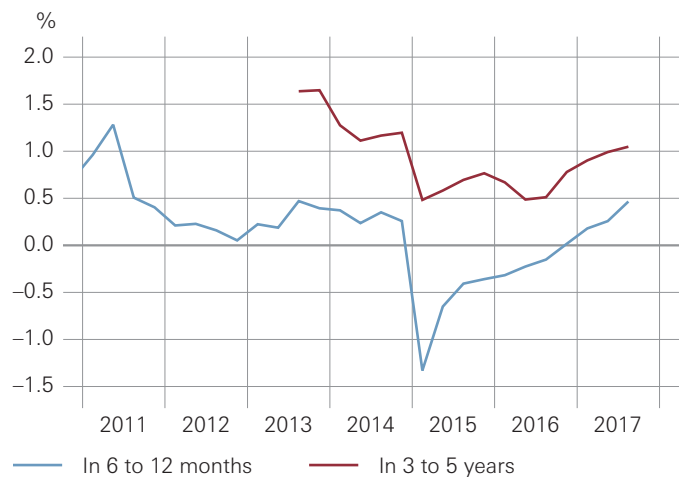
INFLATION EXPECTATIONS

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. However, both have gradually risen again in the interim. Inflation expectations continued to trend upwards in the third quarter, with average expectations for the next six to twelve months increasing from 0.3% in the previous quarter to 0.5% in the quarter under review; however, expectations for the next three to five years remained unchanged, at 1.0% (these short and medium-term expectations are represented in chart 6 by the blue and red lines respectively). Inflation expectations have thus returned to the kind of levels recorded 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 strong business cycle 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 part of the qualitative information received 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*.