Business cycle signals

Results of the SNB company talks

Second quarter of 2018

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 244 company talks were conducted between mid-April and the beginning of June.

Regions	Delegates
Central Switzerland	Walter Näf
Eastern Switzerland	Urs Schönholzer
Fribourg/Vaud/Valais	Aline Chabloz
Geneva/Jura/Neuchâtel	Jean-Marc Falter
Italian-speaking Switzerland	Fabio Bossi
Mittelland	Roland Scheurer
Northwestern Switzerland	Daniel Hanimann
Zurich	Rita Kobel

Key points

- In the second quarter, growth in the Swiss economy continued to be robust and broad-based.
- Technical capacity utilisation increased further. In many industries, utilisation is at a normal level. In parts of manufacturing, bottlenecks have become an issue.
- In the previous quarter, profit margins reattained a level regarded by company representatives as normal. In the quarter under review, higher purchase prices, in particular, appear to be exerting slightly greater pressure on margins.
- Company representatives are confident about the second half of the year. They expect the positive dynamic in real turnover to continue unabated in the next two quarters, due in large part to the favourable economic environment internationally.
- Companies are planning to hire more staff. Meanwhile, there is a growing shortage of specialised personnel.

CURRENT SITUATION

Ongoing turnover growth

In the second quarter, too, momentum has remained distinctly high in many companies and across all three sectors of the economy, namely services, manufacturing and construction. Company representatives report considerably stronger quarter-on-quarter growth in real turnover, i.e. turnover adjusted for changes in sales prices (cf. chart 1; for guidance on interpreting the charts, refer to the relevant section at the end of this report). A comparison with the corresponding year-back quarter also points to vigorous growth. Momentum has, however, not strengthened further.

Export-oriented companies are still looking at a favourable and geographically very broad-based demand situation. Company representatives attribute this development to trade with Europe, North America and Asia, In Brazil, meanwhile, there are signs of improvement. Companies supplying capital goods as well as goods for the automotive and medical technology industries recorded particularly dynamic results.

Utilisation of capacity normal

All in all, utilisation of technical capacity is at a normal level. The upward trend in capacity utilisation, which has been underway for roughly two years now, continued (cf. chart 2). This notwithstanding, the situation still varies considerably depending on the industry.

Around 40% of the companies rate their technical capacity utilisation as normal. However, one-third of the companies are reporting slight or substantial overutilisation. Some firms have added more shifts to meet increased demand and avoid delivery backlogs. With supply shortages more frequently considered a problem, companies are taking precautionary measures and increasing some of their stocks, particularly of raw materials as well as technical and electronic components. Around one-third of the companies still report underutilisation.

Staff and specialised personnel in short supply

According to company representatives in all three sectors, current staff numbers are still slightly too low. One-third of the companies describe their staffing as slightly too low or much too low.

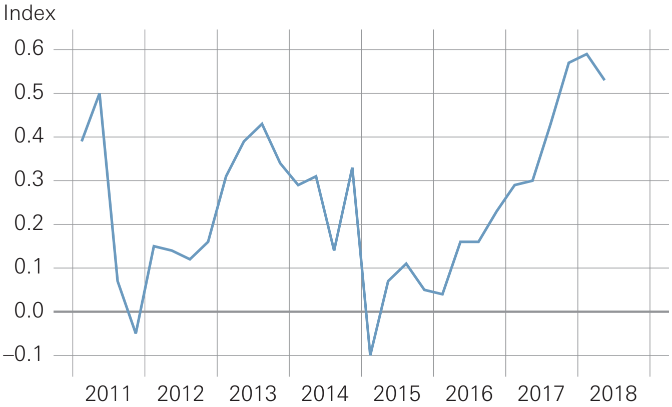
In addition, recruitment problems have become significantly more pronounced in the quarter under review and have reached the highest level since this time series began. A total of 42% of the companies find that it has become harder to source staff. On the one hand, this reflects the improved situation in the domestic labour market. On the other, the increasingly difficult recruitment of staff abroad, particularly in Germany, is frequently cited as a possible cause. This effect is a reflection of the improved economic situation in the target countries. The recruitment of engineers, professionals and – in all industries – IT specialists continues to be difficult. Companies are also reporting that they are still finding it increasingly challenging to source enough apprentices.

Higher purchase prices push down margins in places

In the previous quarter, profit margins had attained a level that company representatives regarded as normal. Higher turnover, a weaker franc year-on-year, and potential for price increases in some areas had contributed to this normalisation. In the quarter under review, pressure on margins appears to have increased once again. One of the reasons cited are the more expensive purchases of raw materials and intermediate inputs, which cannot (yet) be passed on entirely to the customer. Another factor contributing to the narrowing margins is that some companies have reached their capacity limit and are having to react with measures such as adding more shifts, working weekends and recruiting more temporary staff.

Chart 1

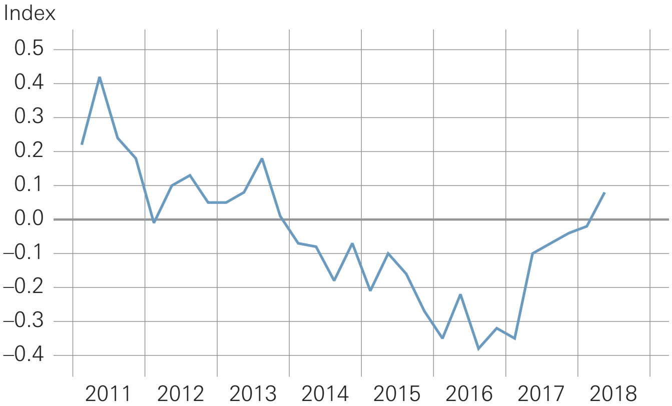
TURNOVER COMPARED TO PREVIOUS QUARTER



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

In the retail business, structural changes – particularly the accelerating shift to online shopping – remains a recurring topic; the importance of stationary trade continues to wane. Real turnover is significantly higher quarter-on-quarter, both in the wholesale and retail trade, and company representatives rank consumer confidence as generally favourable. There are individual reports that cross-border shopping is tapering off. However, margins in both trades are considerably tighter than usual. Frequently cited in this connection is more expensive procurement abroad, which until now has only been partially passed on to customers.

The finance sector made a positive showing, albeit less robust than in the previous quarter. Banks' margins, meanwhile, are falling short of the levels considered to be normal. Capacity remains underutilised, which company representatives linked in part to the still overly extensive network of bank branches.

In the hotel industry, real turnover was above that of the previous quarter. The majority of foreign guests hail from China, the US, the UK and, to an increasing extent again, Germany. Given that price increases are often possible, the margin situation is improving. In addition, an increased demand by companies for seminar locations has been noted. The situation in catering is less favourable, however, with turnover at the same level as the previous quarter and margins lower than normal.

Transportation and logistics companies, law firms, fiduciary companies, engineering and consultancy offices, as well as facility management services report continued favourable results.

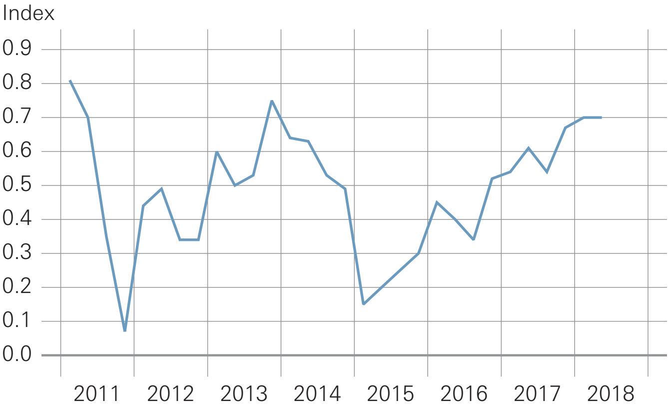
Turnover in the information and communications technology industry has risen further, however margin pressure remains high amid strong competition, increasing personnel expenses and investment in infrastructure.

In manufacturing, most industries have recorded higher turnover than in the previous quarter. Utilisation has risen again and is now at its highest level in five years. The chemical and pharmaceutical industries report particularly strong performance, with high utilisation. The picture is similar in mechanical engineering and metal processing. In addition, margins here are slightly higher than usual. In the watchmaking industry, companies and their suppliers have regained a foothold, with turnover mostly higher than the previous quarter and the previous year. However, their margins remain slightly under pressure. Companies in printing and packaging as well as in the furniture trade report tighter-than-usual margins.

Momentum in construction remains relatively high, with moderate to marked overutilisation of production capacity, both in the building industry and in ancillary trades. Turnover growth is high in the finishing trade and civil engineering in particular. Margin pressure persists, however. There are few signs that construction activity may be noticeably slowing in the short term. Several company representatives talked about the growing number of vacant housing units and a barely sustainable price situation. Major construction projects by institutional investors are tending to enlarge these imbalances.

Chart 3

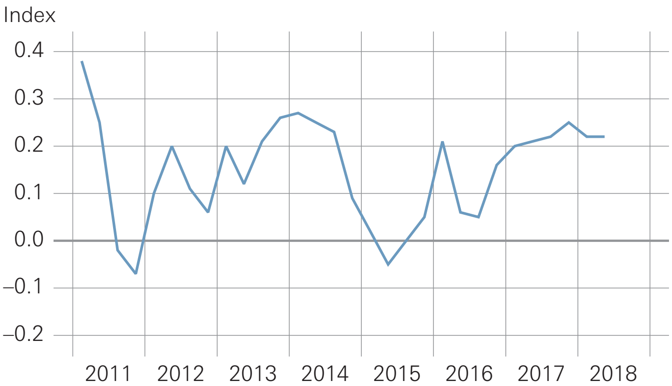
EXPECTED TURNOVER



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

Chart 4

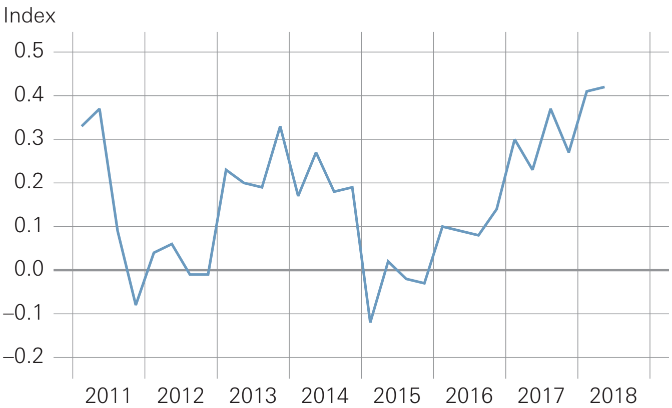
EXPECTED CAPACITY UTILISATION



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

Chart 5

EXPECTED EMPLOYMENT



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

OUTLOOK

Confidence about second half of year

Company representatives remain highly optimistic about their business prospects for the next two quarters. Overall, real turnover is expected to rise (cf. chart 3); this applies to all three sectors. The main factor contributing to this optimism is the favourable international economic situation, but also current exchange rate conditions and, to some extent, the possibility of pushing through price increases. Many representatives see a major opportunity in the favourable positioning of their companies in terms of size, product range, sales markets and social trends. The order situation of many companies is extremely positive through to the end of the year.

The confidence of the business community is also reflected in higher expected utilisation of technical capacity and in infrastructure in the next two quarters (cf. chart 4). Almost one-third of the companies investing in equipment are also expanding capacity. Higher investment is forecast particularly in the mechanical and electrical engineering industries.

Slight price rises

Company representatives anticipate that both purchase and sales prices will rise in the next two quarters. However, for purchase prices, the increase is not expected to be as pronounced as in the previous quarter.

In the discussions, higher purchase prices were linked to demand-induced increases in raw material prices and to a weakening of the Swiss franc relative to last year. Such price increases are normally passed on to the customer. Since there can be a certain delay before these feed through, however, profit margins are temporarily affected.

Further staff increases planned

Personnel shortages and the prospect of higher capacity utilisation are affecting companies' recruitment plans. Managers from all three sectors are planning to increase staff numbers relatively significantly in the second half of the year (cf. chart 5), provided suitable candidates can be found. Many firms are placing a greater focus on in-house training and apprenticeships in an effort to attract and retain personnel. A number of the banks visited are planning to reduce staff numbers.

Rising wages

Based on information obtained in the talks, salary increases already granted or planned for 2018 average 1.2%, and many companies are intending to pay general bonuses. Wages are rising in the vast majority of industries. Above-average wage increases are being offered in the IT industry, in financial consulting and at engineering firms.

ENVIRONMENT AND RISKS

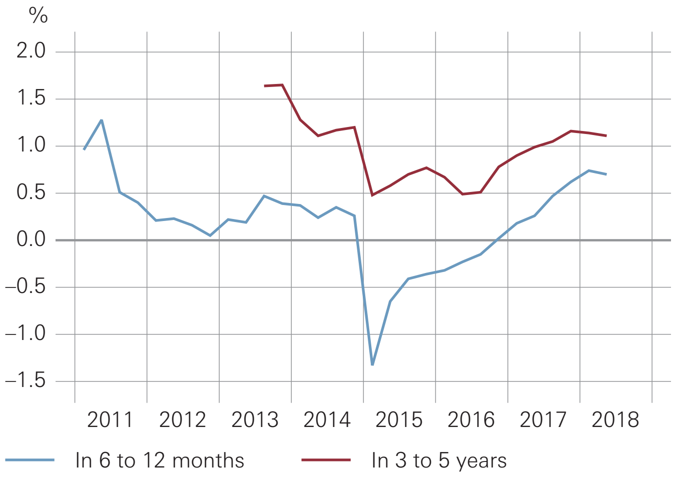
Companies rate uncertainty in their operating environment as relatively low. Internationally, potential hazards mentioned include geopolitical risks and protectionist tendencies, or even a trade dispute. With respect to Europe, a number of company representatives addressed unresolved structural problems. A renewed appreciation of the Swiss franc is also cited as a risk. The vast majority of managers describe the weakening of the franc against the euro since the summer of 2017 as 'helpful', while importers in particular allude to the increased procurement costs.

However, in the current, generally favourable economic environment, the companies indicate that opportunities more frequently outweigh risks. In this regard, intense competition over resources has resulted in a growing shortage of specialist staff as well as supply shortages of raw materials. Owing to the fact that the economy is performing so well almost everywhere, some managers feel that, realistically speaking, an economic weakening must be expected.

Many company representatives continue to find the complex domestic regulatory environment burdensome. Digitalisation is still being actively debated and explored in many industries; opinion among representatives as to whether it is an opportunity or a risk is divided, however. The pending corporate tax reform is also a frequently raised point in the discussions. In addition, managers expressed unease about the impact of low interest rates on the real estate market.

Chart 6

EXPECTED INFLATION



Source: SNB

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, as measured by the consumer price index.

Inflation expectations have stabilised, both in the short and the medium term. Expectations for the next six to twelve months average 0.7%, just as in the previous quarter (blue line in chart 6). Medium-term inflation expectations – with a time horizon of three to five years – also remain unchanged from the previous quarter at 1.1% on average (red line in chart).

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 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*.

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