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# Business cycle signals

Results of the SNB company talks

## **Third 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 208 company talks were conducted between mid-July and the beginning of September.

### **Regions**

Central Switzerland  
Eastern Switzerland  
Fribourg/Vaud/Valais  
Geneva/Jura/Neuchâtel  
Italian-speaking Switzerland  
Mittelland  
Northwestern Switzerland  
Zurich

### **Delegates**

Walter Näf  
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Fabio Bossi  
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## Key points

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- The Swiss economy continued to perform robustly in the third quarter. Growth was broad-based across industries and markets.
- All in all, utilisation of technical capacity and infrastructure is at a normal level. Bottlenecks are becoming increasingly evident in parts of manufacturing. The shortage of specialists has also become more acute.
- As in the past two years, profit margins have gradually continued to improve. They nonetheless remain under pressure in some segments of the economy.
- Company representatives are confident about the next two quarters, albeit not quite as optimistic as they were in the previous quarter. Key factors are the favourable economic environment internationally and the positioning of their companies.
- Companies are planning to increase staff numbers considerably and are prepared to step up investment.

## CURRENT SITUATION

### Ongoing robust economic momentum

In the third quarter, economic momentum was robust, although slightly less so than in the preceding quarters. 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 same period in 2017 also indicates vigorous growth.

Both domestically focused and export-oriented companies are benefiting from the generally favourable economic situation. Export demand remains geographically broad-based. Company representatives mention, in particular, very good business with Europe (especially Germany, the Benelux countries, Scandinavia and the UK), the US and several countries in Asia. Signals are mixed with regard to Italy and Russia. Sales of capital goods as well as goods for the automotive and medical technology industries were especially brisk.

### Utilisation of production capacity normal

Utilisation of technical production capacity remains at a normal level (cf. chart 2). Capacity utilisation at some companies, especially in manufacturing, is very high.

Technical capacity utilisation is normal at 42% of companies, while a further 33% report slight or substantial overutilisation. Some representatives noted the absence of the usual summer lull in demand this year. Problems with supply shortages and in some cases considerably longer delivery times, particularly for raw materials as well as technical and electronic components, were mentioned by various company representatives. Companies'

responses to this challenge include increasing their inventory levels, adding more shifts, reducing holidays and employing temporary staff. In addition, more investment is going into expanding production capacity.

### Staff numbers remain low

According to company representatives in all three sectors, staff numbers are slightly too low. They report that staff shortages have become rather more pronounced compared with the previous quarter. Headcounts are described by 37% of companies as slightly too low or much too low, while just 7% of companies consider their staffing levels too high.

In manufacturing, recruitment has become even more difficult. Half of the companies report that it has become harder to source staff. The recruitment of professionals, engineers and IT specialists continues to be challenging. The shortage of IT specialists is evident in various industries. Companies also say that they are still struggling to find enough apprentices.

### Margins just below normal

Profit margins have improved somewhat since the previous quarter. Overall, they remain just below levels company representatives regard as normal. One reason for margins still being squeezed in some areas is the higher purchase prices for raw materials and intermediate inputs, which cannot (yet) be fully passed on to customers. A second factor contributing to narrowing margins is that some companies have reached their capacity limit and are having to respond with costly measures such as adding more shifts, working weekends and recruiting more temporary staff. Thirdly, underutilised infrastructure and pricing pressure from customers is adversely affecting margins in parts of the economy.

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 trade, real turnover is significantly up quarter-on-quarter and substantially higher year-on-year. This is primarily attributable to wholesale trade rather than retail trade where infrastructure is still underutilised. Company representatives rate consumer confidence as generally favourable. Some report a continuing decline in cross-border shopping, and there are signs that cross-border commuters are increasingly shopping in Switzerland again. In the vehicle trade, by contrast, business is flat or slightly down. Overall, profit margins in trade remain well below normal levels.

Business in the finance sector has gathered pace compared to the previous quarter. Margins at banks are slightly below levels considered to be normal, while at insurance companies they are well below target levels due to their claims experience and high IT investment. Capacity utilisation rates in the finance sector are approaching normal levels. Some banks still regard their branch networks as too dense.

Over the summer months, many tourism businesses benefited from the excellent weather and the generally favourable economic conditions. In the hotel and catering industries, real turnover was significantly higher both quarter-on-quarter and year-on-year. Margins, too, are higher than usual. Overall, capacity utilisation is at a normal level. However, peaks are causing some businesses to investigate how tourism flows can be staggered better. New applications of pricing models are also being tested. As regards foreign source markets, the mainstays are China, the US and the UK, with Germany, the Netherlands and Italy picking up again. Greater demand from companies has also been noted (seminars, events). Hoteliers are very upbeat about the coming winter season.

Companies in the ICT industry report extremely strong business activity with a sharp rise in turnover. Business performance also remains positive for transportation and logistics companies, auditors, as well as engineering and consultancy firms.

In manufacturing, most industries recorded higher turnover and higher capacity utilisation than in the previous quarter. Companies in the mechanical engineering, electrical engineering and metals industries are reporting particularly strong performance, although the margin situation still varies considerably from company to company. The continued positive performance of the watchmaking industry is also being observed in other industries. The pharmaceutical industry rates its production facilities as tending more towards underutilised.

Momentum in construction remains robust. Turnover growth is high in the finishing trade and civil engineering in particular. The slight overutilisation of production capacity reported in this sector over recent quarters continues. In some cases, new orders are being turned down due to capacity bottlenecks and staff shortages. Margin pressure persists in structural engineering. The order situation remains good. Several representatives are concerned about the growing number of vacant housing units and high real estate prices, especially in peripheral locations.

Chart 3

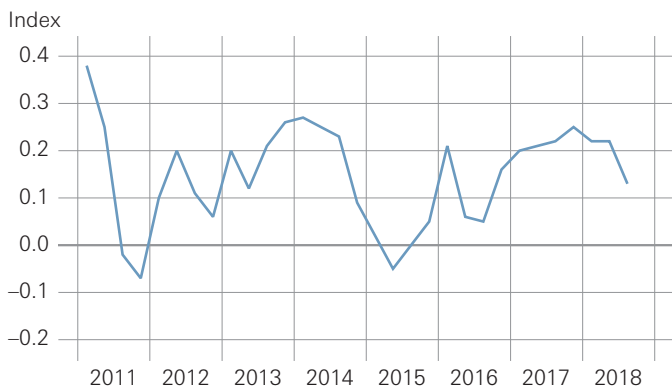
**EXPECTED TURNOVER**



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 looking forward to next year**

Company representatives remain optimistic about their business prospects for the next two quarters. Overall, they expect real turnover to rise, albeit not quite so strongly as predicted in the previous quarter (cf. chart 3). The reason given for this optimism is the positive economic situation, both internationally and domestically. The frequently discussed expectation that it will become easier to push through price rises is also having a positive impact. In this quarter too, many representatives continue to see a major opportunity in the favourable positioning of their companies in terms of size, product range, innovation, flexibility, sales markets and social trends. The order situation of many companies is extremely positive; in some cases, order books are full well into next year.

Company representatives expect utilisation of technical production capacity or infrastructure in the next two quarters to be marginally higher than current levels (cf. chart 4). However, there too, the anticipated rise is not as high as was expected in previous quarters. This is partly due to the fact that numerous companies now have plans to expand their production facilities and infrastructure.

In all three sectors, companies are intending to increase their investments in both equipment and buildings over the next twelve months. About one-third of companies investing in equipment are also expanding their production capacity. The persistently low interest rate environment supports investment. The retail trade, however, is anticipating lower total investment.

**Ongoing slight rise in prices**

Expectations regarding the development of purchase and sale prices have hardly changed from the previous quarter; company representatives expect both to continue to rise slightly in the next two quarters. A number of companies are planning price increases from the beginning of 2019. In the retail trade, on the other hand, it is anticipated that prices will continue to fall.

In the discussions, higher purchase prices were linked to increases in raw material prices as well as good capacity utilisation among suppliers. Several company representatives expect that these price rises can readily be passed on to customers, albeit only with a certain delay in some cases, which can in turn temporarily affect profit margins.

**Staff increases planned**

The personnel shortages and prospects of higher capacity utilisation mentioned by many representatives are affecting companies' recruitment plans. Managers from all three sectors are planning notable increases to staff numbers in the next two quarters (cf. chart 5), provided suitable candidates can be found. In the quarter under review, numbers reached their highest level since this time series began. Many firms are continuing to focus

on in-house training and apprenticeships in an effort to attract and retain personnel. No industry has plans to reduce staff numbers.

## ENVIRONMENT AND RISKS

In the current generally supportive economic environment, company representatives are talking more about opportunities than risks. They rate uncertainty in their operating environment as relatively low. Owing to the fact that the economy is performing so well across a broad front, some managers feel that it is realistic to anticipate a slowdown.

Internationally, potential hazards mentioned include the US trade disputes with China and the EU and their potential direct or indirect impact on companies. Other risks cited were a slump in the global economy, Brexit and unresolved structural problems in Europe.

Domestically, the main challenges referred to were the distinct shortage of specialised staff and delivery bottlenecks for raw materials. Renewed appreciation of the Swiss franc was also identified as a risk.

Digitalisation is still being actively debated and explored in many industries. Expressions of unease regarding developments on the real estate markets surfaced even more frequently than in previous quarters. Company representatives mentioned, in particular, growing vacancy rates in apartments, very low returns on investment properties, and risks being taken by investors. Many company representatives continue to find the complex domestic regulatory environment burdensome, although this issue is preoccupying them less than in the past.

## About this report

### Approach

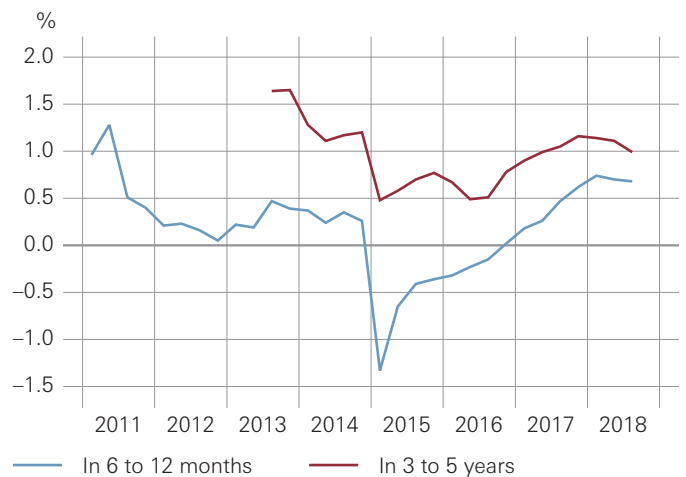
Each quarter, the SNB's delegates for regional economic relations hold talks with managers of companies throughout Switzerland. The main results of these discussions are summarised in the 'Business cycle signals' report.

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.

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 remain stable in the short term. Expectations for the next six to twelve months average 0.7% (blue line in chart 6). Medium-term inflation expectations – with a time horizon of three to five years – are somewhat lower than in the previous quarter, averaging 1% (1.1% in the previous quarter; red line in chart). The slight downward trend observed since the end of 2017 is thus continuing.

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](http://www.snb.ch), The SNB, SNB regional network.

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