
Business cycle signals

Results of the SNB company talks

Third quarter of 2019

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 211 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

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Key points

- The Swiss economy clearly lost momentum in the third quarter. Growth in real turnover slowed further and there was a marked increase in uncertainty. This reflects, first and foremost, a slowdown in the global economy.
- All in all, utilisation of technical capacity is at a normal level, albeit with more pronounced differences between the sectors than has been the case. Staff numbers are still viewed as being slightly on the low side, but less so than in previous quarters.
- Pressure on profit margins has increased somewhat overall, but the levels are mostly described as being 'sustainable' or 'comfortable'.
- Looking to the next two quarters, company representatives expect moderate growth in turnover, staff levels and investment.
- For the first time since the beginning of 2017, representatives no longer expect an increase in purchase and sales prices.
- The main risks cited concern the effects of trade tensions, the outlook for the global economy, and a further appreciation of the Swiss franc.

CURRENT SITUATION

Momentum slows further

The Swiss economy lost momentum in the third quarter as the gradual weakening from the high recorded at the beginning of 2018 persisted.

Compared with the previous quarter, company representatives reported weaker 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 slowdown in new orders is weighing more heavily on sentiment than the current developments with regard to turnover.

The weakening in the German economy is having a marked impact on various companies that are (directly or indirectly) oriented towards exports. Meanwhile, business with the US remains largely favourable. In the case of trade with Asia and Europe, the signals are very mixed from sector to sector and from company to company. This is partly the result of the trade dispute between the US and China. Certain sectors are also feeling the impact of the turmoil stemming from the protests in Hong Kong.

Production capacity utilisation normal

Utilisation of technical capacity remains at a normal level overall (cf. chart 2). Around 40% of companies gave this assessment, whereas 30% said capacity was substantially underutilised and 30% substantially overutilised. In manufacturing, capacity is marginally underutilised, and the problems cited until just recently with regard to supply bottlenecks and long delivery times in certain cases are now scarcely mentioned. Capacity utilisation in the construction sector remains high.

Staff shortage problem improving

Company representatives continue to view their staff numbers as being somewhat on the low side, albeit much less so than in the previous quarter. In manufacturing in particular, levels are now in line with demand overall. In certain instances, companies are planning not to replace departing staff.

Many industries are reporting that recruitment is more difficult than usual. This is partly due to a lack of applicants but also to higher qualification and skill requirements in job profiles, especially as regards IT. The shortage of specialists continues to be one of the main concerns for many companies, although not to quite the same extent as in previous quarters. IT and technical specialists as well as engineers are still in high demand. Many representatives say their companies are prioritising in-house training and maintaining their appeal as an employer in an effort to attract and retain staff.

Slightly higher pressure on profit margins

The pressure on margins has increased slightly overall, and they are just below levels regarded by the companies as normal. That being said, 85% of the representatives describe margins as being sustainable or even comfortable.

Chart 1

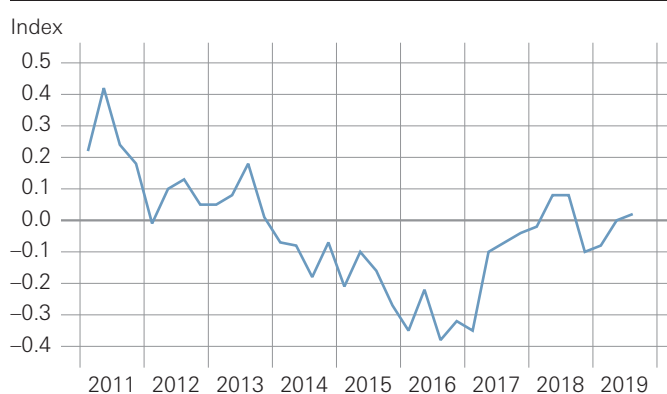
TURNOVER COMPARED TO PREVIOUS QUARTER



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 / business infrastructure compared to a normal level. A positive (negative) index value signals utilisation is higher (lower) than normal.
Source: SNB

DEVELOPMENTS IN INDIVIDUAL INDUSTRIES

Real turnover in the trade sector was on a par with the previous quarter. This applies to wholesale, retail and vehicle trade alike. Meanwhile infrastructure is underutilised in both the retail and wholesale trade. The pressure on margins in the stationary retail trade has increased further. Crossborder shopping is not seen as an acute problem, but rather as a risk were the Swiss franc to appreciate further.

In the financial sector – i.e. among banks, insurers and asset managers – turnover remains unchanged from the previous quarter. The situation with regard to margins has heightened yet further throughout the sector, and this is particularly noticeable in the case of banks. Profit margins are substantially lower than would be considered normal. The reasons for this are the general fall in interest rates, the ongoing decline in net interest margins that can only be partly offset by the volume growth in customer deposits and lending, and the costs involved in implementing digitalisation and regulation. Added to this are the greater caution discernible in customers' investment behaviour and increasing competition from new players entering the market.

Business performance in the hospitality industry is rather dynamic, with turnover up on Q2 2019 and clearly higher year-on-year. Both hotels and restaurants assess capacity utilisation as being normal, with the former also reporting profit margins as well above normal levels. Mountain tourism in Switzerland profited from the heatwave and stronger domestic demand.

Turnover in the ICT industry is reported as being substantially higher quarter-on-quarter and compared with 2018. The factors cited as driving this performance are digital transformation, rising demand from the fintech area, and cybersecurity. However, the persisting shortage of specialist staff is having a curbing effect.

Consultancies and auditors, engineering and architecture firms, and facility management services providers are all experiencing strong sales momentum. Companies in the healthcare sector report dynamic business performance with margins higher than normal.

In manufacturing, the majority of industries recorded higher turnover quarter-on-quarter. The pharmaceuticals industry reports that business is excellent, with turnover well in excess of the comparison periods. Plastics manufacturers, producers of electrical equipment and energy suppliers also assess their business as being dynamic. However, turnover is down quarter-on-quarter for the metal products and processing industry and in the machinery industry, and margins are below normal levels.

The watchmaking industry is exhibiting solid business performance overall although this continues to vary considerably between companies. Suppliers in the automotive industry are still feeling the effect of uncertainty in this market stemming from technological change, new test procedures and heightened environmental awareness among customers.

In seasonally adjusted terms, turnover in the construction sector is up on the previous quarter and higher year-on-year, with production capacity overutilised. This overall result is particularly attributable to civil engineering and the finishing trade. In the case of structural engineering, business is roughly on a par with last quarter, and profit margins here are under strong pressure despite the fact that the order situation remains healthy. In the construction sector as a whole, there is little sign of a marked slowdown in the short term. Although the pace of growth in residential construction may ease back somewhat, new opportunities are opening up amid the increasing need for renovation and refurbishment in the case of buildings and infrastructure and as a result of high-density construction. Rising vacancy rates are additionally driving the demand for renovation of older buildings.

Chart 3

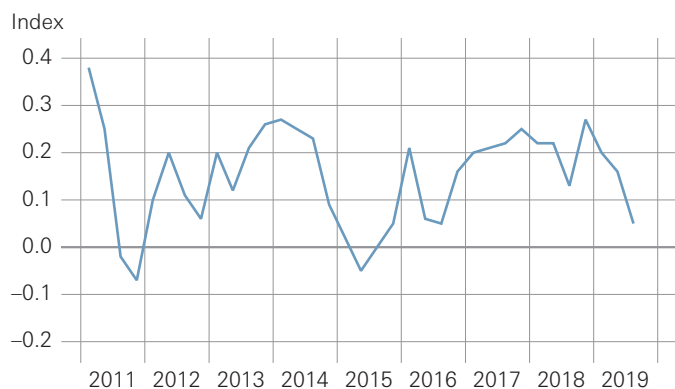
EXPECTED TURNOVER



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

Chart 4

EXPECTED CAPACITY UTILISATION



Expected developments in utilisation of technical capacity / business infrastructure over the coming two quarters. Positive (negative) index values indicate utilisation is expected to be higher (lower). Source: SNB

Chart 5

EXPECTED EMPLOYMENT



Expected developments in staff numbers over the coming two quarters. Positive (negative) index values indicate an expected increase (decrease). Source: SNB

OUTLOOK

Muted optimism

Company representatives anticipate slightly higher real turnover in the next two quarters. However, their expectations are somewhat more cautious than in 2018 (cf. chart 3), this being above all attributable to the weaker outlook for the global economy and a decline in new orders.

Manufacturing and construction companies are less confident than in the previous quarter, although this is partly offset by brighter prospects in the services sector. As regards technical capacity and available infrastructure at their companies, representatives do not expect any change in the review period, with utilisation thus remaining at normal levels (cf. chart 4).

Somewhat greater caution regarding investment

Companies' willingness to invest has waned slightly against the backdrop of reduced economic momentum and as a result of trade tensions. Companies in all three sectors envisage increasing their expenditure on investment in equipment and construction only slightly in the next twelve months. That said, the low interest rate environment is still having a favourable impact on investment projects. Just under a quarter of companies will use their spending on equipment specifically to increase production capacity. Investment is focused above all on the expansion and modernisation of IT.

Price expectations marginally lower

Over the past two years, company representatives have mostly expected purchase and sale prices to increase, but for the coming two quarters they now anticipate a slight fall. Representatives from manufacturing in particular envisage price reductions. Upward pressure on prices of raw materials and preliminary products was still visible in the spring; this has now dissipated, and the recent high level of capacity utilisation among suppliers is likewise no longer noticeable.

Hiring demand remains

Representatives say their companies are planning to further increase headcount over the coming two quarters (cf. chart 5), albeit this view is not as widely held as in recent quarters. 37% of companies want to hire more staff, compared with 41% in Q2 2019. Instances of companies that intend to reduce staff levels are to be found in industries such as foodstuffs and printing.

ENVIRONMENT AND RISKS

As regards the perceived international risks, the representatives' focus is primarily on the trade dispute between the US and China and the potential impact, be it direct or indirect, on their companies. They also referred to other sources of geopolitical uncertainty. Brexit is an issue that is often raised, and one that could have a positive or negative impact depending on the company in question. Other risks cited stem from the slowdown in the global economy and the high levels of public debt.

Domestically, the shortage of specialised staff remains one of the main challenges mentioned. Various companies also reported that they had been unable to fill all their apprenticeship positions. Also frequently mentioned were the risks arising from the low interest rate environment and potentially even lower rates, particularly for pension schemes. The appreciation of the Swiss franc is being given more emphasis as a risk than before. A number of representatives see cause for concern in the situation on the real estate market, where construction activity is continuing despite residential vacancy rates already being high in some regions. Digitalisation is an issue that is being actively debated and explored.

INFLATION EXPECTATIONS

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

Short-term inflation expectations are marginally higher. The average for the next six to twelve months (blue line in chart 6) is 0.5%, compared to 0.4% in the previous quarter. Over the medium term – i.e. with a time horizon of three to five years (red line in chart) – the average is unchanged at 0.8%.

About this report

Approach

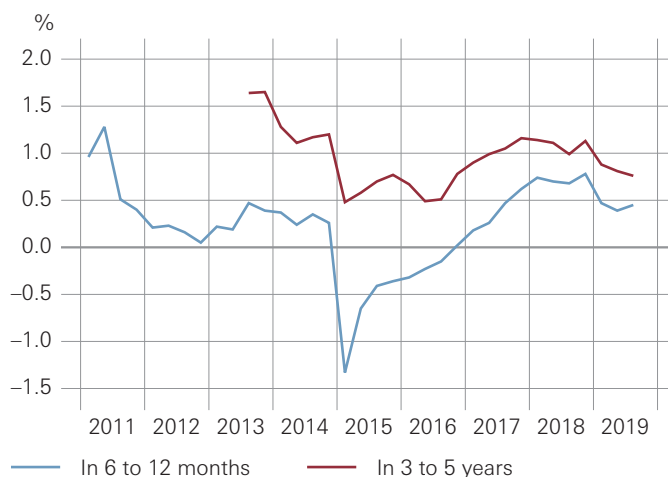
Each quarter, the SNB's delegates for regional economic relations hold talks with managers of companies throughout Switzerland. The main results of these discussions are summarised in the 'Business cycle signals' report.

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

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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