

Quarterly Bulletin
2/2016 June

SCHWEIZERISCHE NATIONALBANK
BANQUE NATIONALE SUISSE
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Monetary policy report

Report for the attention of the Governing Board of the Swiss National Bank for its quarterly assessment of June 2016.

The report describes economic and monetary developments in Switzerland and explains the inflation forecast. It shows how the SNB views the economic situation and the implications for monetary policy it draws from this assessment. The first section ('Monetary policy decision of 16 June 2016') is an excerpt from the press release published following the assessment.

This report is based on the data and information available as at 16 June 2016. Unless otherwise stated, all rates of change from the previous period are based on seasonally adjusted data and are annualised.

1 Monetary policy decision of 16 June 2016

Monetary policy remains expansionary

The Swiss National Bank (SNB) is maintaining its expansionary monetary policy. Interest on sight deposits at the SNB is to remain at -0.75% and the target range for the three-month Libor is unchanged at between -1.25% and -0.25% . At the same time, the SNB will remain active in the foreign exchange market, as necessary. The negative interest rate and the SNB's willingness to intervene in the foreign exchange market are intended to make Swiss franc investments less attractive, thereby easing pressure on the currency. The Swiss franc is still significantly overvalued. The SNB's expansionary monetary policy is aimed at stabilising price developments and supporting economic activity.

The new conditional inflation forecast suggests inflation will rise faster over the coming quarters than the SNB predicted in March, principally due to the significant increase in oil prices in the intervening period (cf. chart 1.1). The effect of this oil price rise on annual inflation vanishes after the first quarter of 2017. The new conditional forecast subsequently moves closer to that of the last quarter, and is in line with it from 2018. At -0.4% , the inflation forecast for 2016 is 0.4 percentage points higher than in March. For 2017, the SNB expects an inflation rate of 0.3%, compared to 0.1% forecast in the last quarter, while still anticipating a rate of

0.9% for 2018. The conditional inflation forecast is based on the assumption that the three-month Libor remains at -0.75% over the entire forecast horizon.

The moderate recovery in the global economy continues. It is particularly well advanced in the US, which is on the cusp of full employment. Economic growth in the euro area is gradually becoming more broad-based. In China, growth remains robust thanks to economic policy measures aimed at stimulating demand. Overall, international growth is principally being driven by domestic demand. By contrast, international trade and global manufacturing remain subdued. All in all, positive economic signals in recent months have helped ease the situation on the international financial markets, which were dominated by turbulence at the start of the year. Against a backdrop of rising confidence, commodity prices have also recovered from their lows. The SNB expects the moderate growth in the global economy to sustain over the coming quarters.

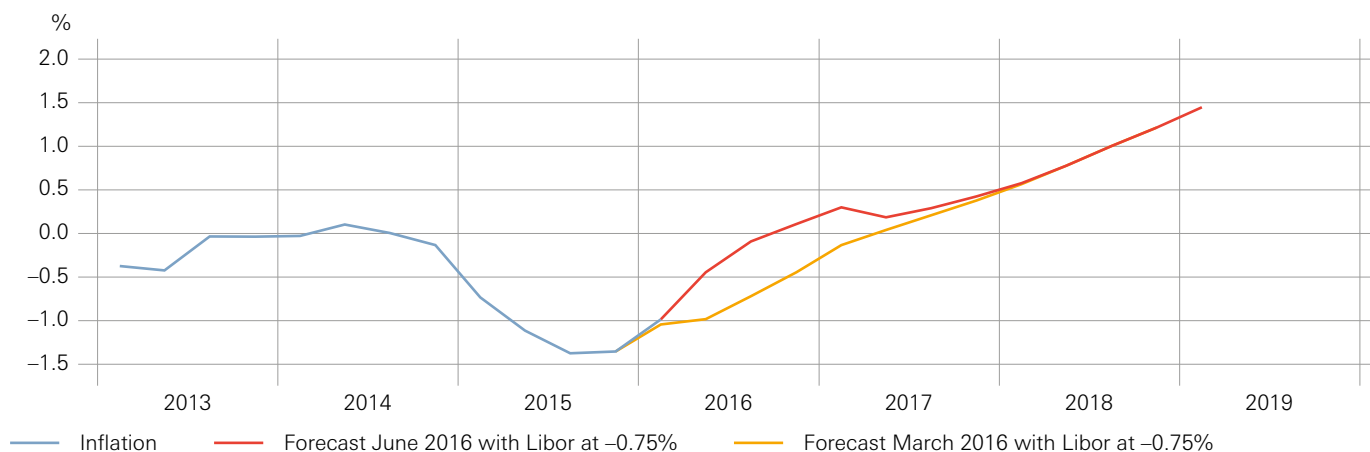
Nevertheless, significant risks remain for the global economy. Furthermore, the imminent UK referendum on whether to stay in the European Union may cause uncertainty and turbulence to increase.

In Switzerland, real GDP grew at an annualised rate of 0.4% in the first quarter. Available indicators suggest that the recovery will be ongoing. The gradual improvement in the international environment will also benefit Switzerland. Exports are likely to continue to recover, and this should stimulate corporate investment and have a positive impact on the labour market. The SNB expects the unemployment rate to stabilise in the second half of the year. For 2016 as a whole, it still anticipates real GDP growth of between 1% and 1.5%.

Chart 1.1

CONDITIONAL INFLATION FORECAST OF JUNE 2016

Year-on-year change in Swiss consumer price index in percent



Source: SNB

Growth on the mortgage market once again slowed somewhat in the first quarter of 2016. Real estate prices, by contrast, climbed at a marginally faster rate. Despite restrained momentum in recent quarters, imbalances on the mortgage and real estate markets increased slightly due to comparatively weak growth in fundamentals. The SNB will continue to monitor developments on the mortgage and real estate markets closely, and will regularly reassess the need for an adjustment of the countercyclical capital buffer.

Monetary policy strategy at the SNB

The SNB has a statutory mandate to ensure price stability while taking due account of economic developments.

The SNB has specified the way in which it exercises this mandate in a three-part monetary policy strategy. First, it regards prices as stable when the Swiss consumer price index (CPI) rises by less than 2% per annum. This allows it to take account of the fact that the CPI slightly

overstates actual inflation. At the same time, it allows inflation to fluctuate somewhat with the economic cycle. Second, the SNB summarises its assessment of the situation and of the need for monetary policy action in a quarterly inflation forecast. This forecast, which is based on the assumption of a constant short-term interest rate, shows how the SNB expects the CPI to move over the next three years. Third, the SNB sets its operational goal in the form of a target range for the three-month Swiss franc Libor.

Table 1.1

OBSERVED INFLATION IN JUNE 2016

	2013				2014				2015				2016				2013	2014	2015
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
Inflation	-0.4	-0.4	0.0	0.0	0.0	0.1	0.0	-0.1	-0.7	-1.1	-1.4	-1.4	-1.0				-0.2	0.0	-1.1

CONDITIONAL INFLATION FORECAST OF JUNE 2016

	2016				2017				2018				2019				2016	2017	2018		
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4					
Forecast March 2016, with Libor at -0.75%	-1.0	-1.0	-0.7	-0.4	-0.1	0.0	0.2	0.4	0.6	0.8	1.0	1.2							-0.8	0.1	0.9
Forecast June 2016, with Libor at -0.75%		-0.4	-0.1	0.1	0.3	0.2	0.3	0.4	0.6	0.8	1.0	1.2	1.4						-0.4	0.3	0.9

Source: SNB

2 Global economic environment

The moderate recovery in the global economy continued in the first few months of 2016, supported by ongoing highly expansionary monetary policy worldwide.

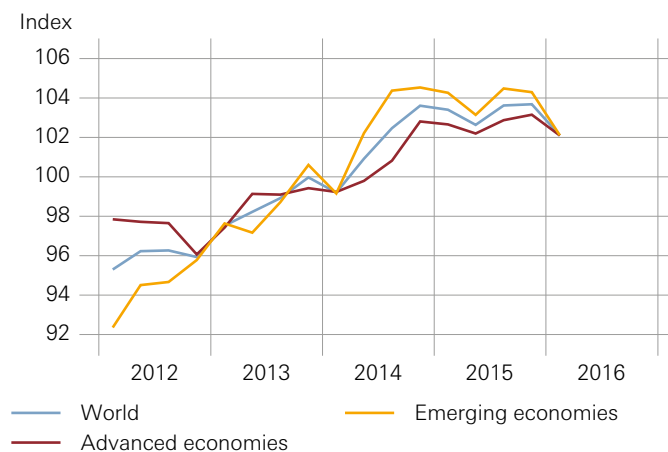
Economic recovery is particularly well advanced in the US. The country's labour market has developed favourably overall since the beginning of the year, with the economy on the cusp of full employment for the first time since the onset of the financial crisis in 2008. Economic growth in the euro area is gradually becoming more broad-based and this is increasingly spilling over into the labour market. The unemployment rate has again fallen slightly in recent months. In China, growth remains robust, thanks to various economic policy measures aimed at stimulating domestic demand. Overall, international growth is principally being driven by domestic demand and the services sector. By contrast, global manufacturing and trade remain subdued.

The international financial markets were dominated by turbulence at the start of the year, however positive economic signals since then have helped to ease the situation. Risk premiums and volatility have fallen perceptibly in recent months. At the same time, commodity prices have also recovered from multi-year lows.

Chart 2.1

GLOBAL EXPORTS

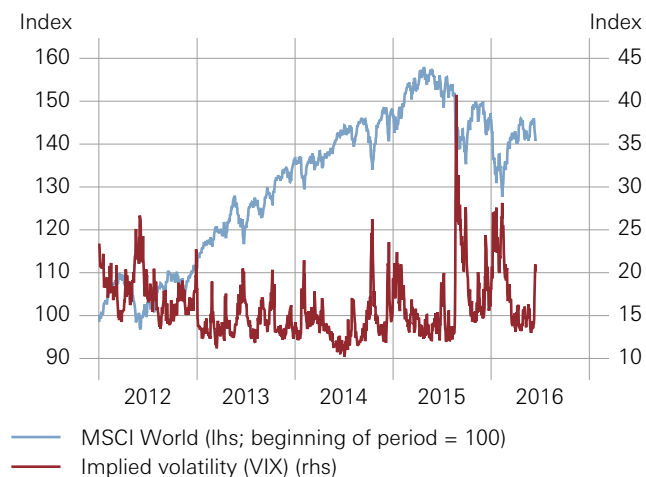
Reporting period average = 100



Sources: CPB, Thomson Reuters Datastream

Chart 2.2

STOCK MARKETS



Source: Thomson Reuters Datastream

Table 2.1

BASELINE SCENARIO FOR GLOBAL ECONOMIC DEVELOPMENTS

	2012	2013	2014	2015	Scenario	
					2016	2017
GDP, year-on-year change in percent						
Global ¹	3.1	3.2	3.4	3.2	3.3	3.6
US	2.2	1.5	2.4	2.4	2.0	2.3
Euro area	-0.9	-0.3	0.9	1.7	1.6	1.7
Japan	1.7	1.4	-0.1	0.6	0.7	0.8
Oil price in USD per barrel	111.7	108.7	99.0	52.5	43.0	46.0

¹ PPP-weighted (US, euro area, UK, Japan, China, South Korea, India, Brazil and Russia).

Sources: SNB, Thomson Reuters Datastream

Chart 2.3

EXCHANGE RATES

Trade-weighted, beginning of period = 100

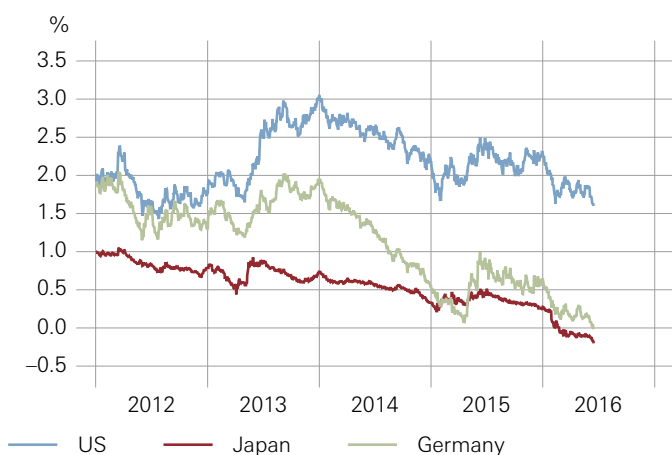


Source: Thomson Reuters Datastream

Chart 2.4

INTERNATIONAL LONG-TERM INTEREST RATES

10-year government instruments

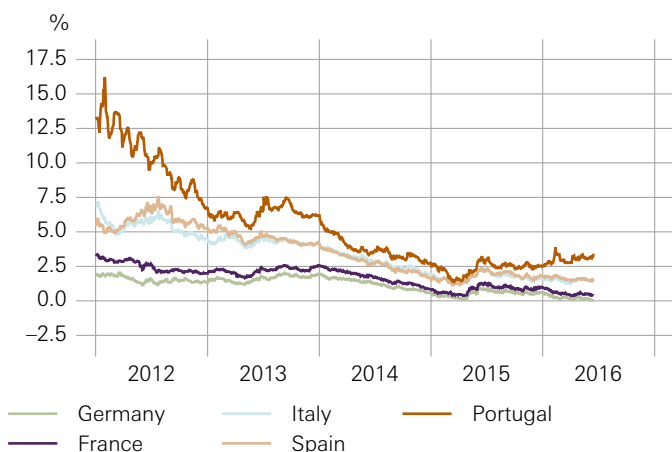


Source: Thomson Reuters Datastream

Chart 2.5

EUROPEAN LONG-TERM INTEREST RATES

10-year government instruments



Source: Thomson Reuters Datastream

In its baseline scenario, the SNB expects the modest pace of growth in the global economy to sustain over the coming quarters. Nevertheless, significant risks remain. Furthermore, uncertainty emanating from political events – especially the imminent referendum in the UK on whether to leave the EU (Brexit) – could mount sharply and hamper economic development.

The SNB’s forecasts are based on assumptions about the oil price and the EUR/USD exchange rate. The SNB is assuming an oil price for Brent crude of USD 46 per barrel (compared with USD 33 three months ago) and an exchange rate of USD 1.14 to the euro. Both correspond to the 20-day average when the baseline scenario was drawn up.

INTERNATIONAL FINANCIAL AND COMMODITY MARKETS

The mood on the global financial markets has calmed since the last monetary policy assessment and the turmoil at the beginning of the year. The positive effects of economic policy measures taken in many countries have become increasingly evident. Accordingly, concerns over prospects for global growth have receded somewhat. The MSCI World Index initially gained ground, although recent days have seen increased uncertainty in connection with the imminent Brexit referendum in the UK. Share prices have receded somewhat again, and there has been a rise in the implied volatility of US stocks as measured by option prices (VIX), which serves as an indicator of market uncertainty (cf. chart 2.2).

The exchange rates of the major currencies have continued to fluctuate significantly. Due to the cautious approach of the US Federal Reserve, the US dollar has lost considerable value since the beginning of the year (cf. chart 2.3). Conversely, the euro and the yen have appreciated. Yields on long-term government bonds have mainly trended downwards, reaching all-time lows in several countries (cf. chart 2.4).

Many commodity prices have recovered from multi-year lows (cf. chart 2.6). The oil price, in particular, picked up sharply from the beginning of the year onwards, as oversupply receded due to a decline in production.

US

The recovery in the US economy continued. However, economic performance as measured by GDP was less dynamic than in the first quarter, expanding by 0.8% (cf. chart 2.7). Private consumption temporarily slowed, despite higher levels of disposable income. Investment in fixed assets receded. Further investment cuts in the energy sector due to the low oil price had a particularly dampening effect. By contrast, the labour market improved overall, with the unemployment rate continuing to decline (cf. chart 2.10). The economy has now almost reached full employment.

The growth outlook is favourable. Following higher levels of household savings in the first quarter, strong turnover in the retail sector in April and May suggests that private consumption is once more on the rise. Furthermore, the US dollar depreciated somewhat and credit conditions for companies have eased. After the weak performance in the first quarter, the economy is likely to regain momentum. The SNB is forecasting growth of 2.0% for 2016 and 2.3% for 2017 (cf. table 2.1).

Inflation in the US is trending upwards. In May, the annual inflation rate as measured by the consumer price index stood at 1.0% (cf. chart 2.11). It will rise further over the course of the year due to the higher oil price. Inflationary pressure emanating from the labour market is also likely to gradually increase. Various measures of core inflation suggest that inflation is approaching the target set by the Federal Reserve.

The Federal Reserve has made no adjustments to its monetary policy since raising its target range for the federal funds rate in December. In the current environment, markets expect a further normalisation in the course of the year.

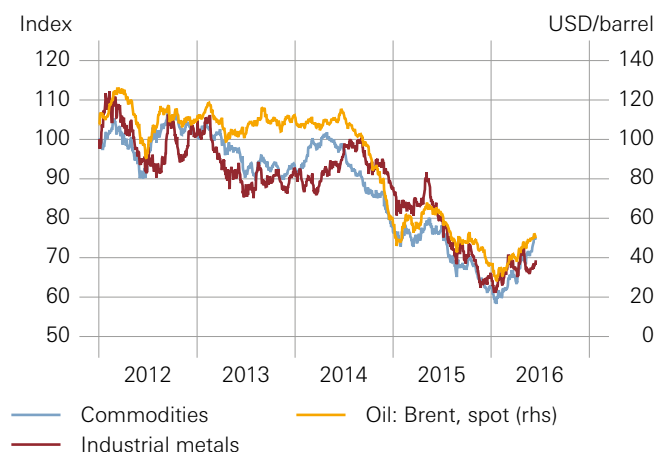
EURO AREA

In the euro area, GDP grew in the first quarter by 2.2%, which was somewhat higher than expected (cf. chart 2.7). This constituted the first time that economic performance had surpassed the level recorded before the financial crisis. Growth remained broad-based, with mild weather making a significant contribution to robust construction activity. Unemployment receded further; the figure of 10.2% in April represents the lowest level since August 2011 (cf. chart 2.10).

Chart 2.6

COMMODITY PRICES

Beginning of period = 100

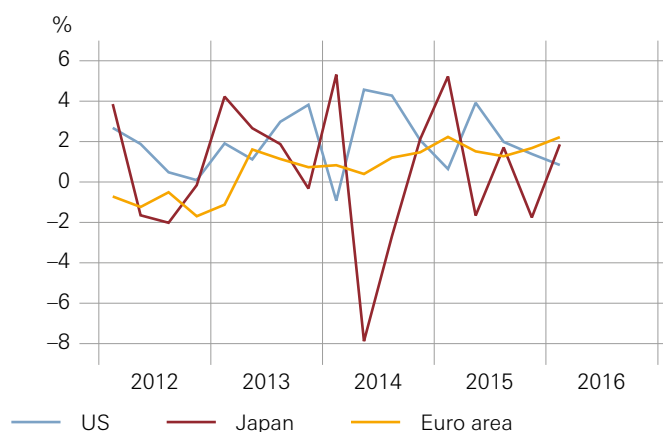


Source: Thomson Reuters Datastream

Chart 2.7

REAL GDP: ADVANCED ECONOMIES

Change from previous period

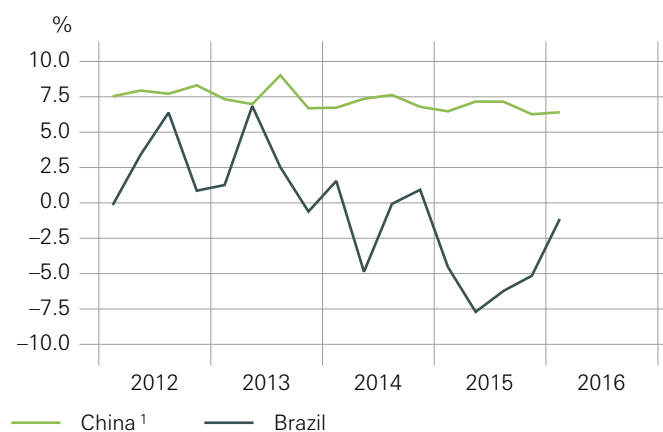


Source: Thomson Reuters Datastream

Chart 2.8

REAL GDP: EMERGING ECONOMIES

Change from previous period

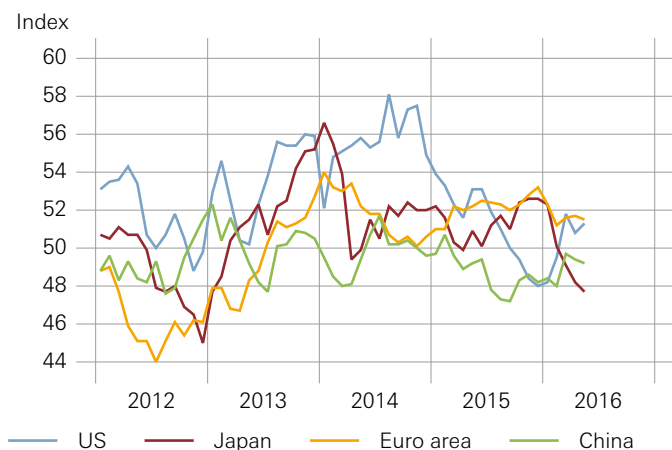


¹ Estimate: SNB.

Source: Thomson Reuters Datastream

Chart 2.9

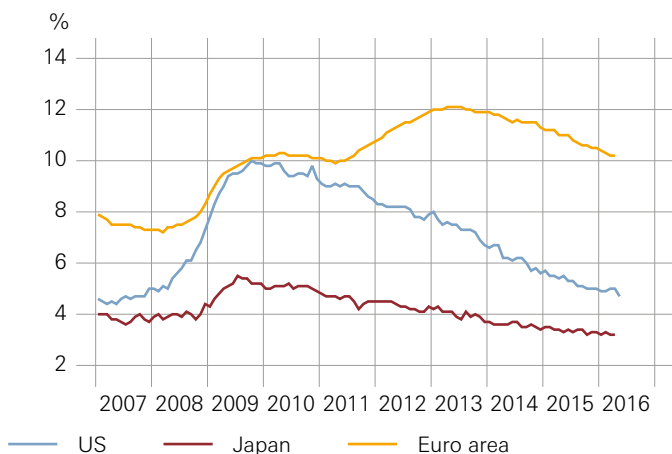
PURCHASING MANAGERS' INDICES (MANUFACTURING)



Source: Markit Economics Ltd 2009; all rights reserved

Chart 2.10

UNEMPLOYMENT RATES

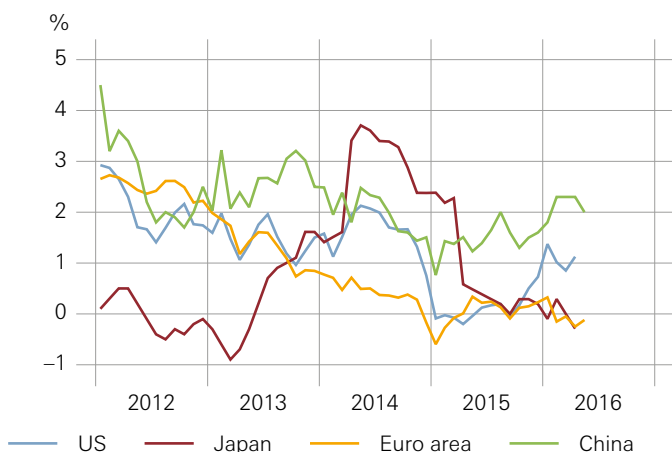


Source: Thomson Reuters Datastream

Chart 2.11

CONSUMER PRICES

Year-on-year change



Source: Thomson Reuters Datastream

Supported by expansionary monetary policy, the economic recovery looks set to continue. Fiscal policy is also likely to provide mild stimuli. Growth prospects, however, remain moderate. In view of sluggish global trade and the somewhat stronger euro, companies have revised their export expectations for the second quarter slightly downwards. A further source of concern are uncertainties stemming from political events, including the imminent UK referendum on leaving the EU (Brexit) as well as banking problems in certain euro area member states. Moreover, the implementation of growth-stimulating reforms continues to pose a serious challenge. The SNB's growth forecast for the euro area is largely unchanged. Due to favourable developments at the beginning of the year, GDP is likely to advance by 1.6% in 2016. For 2017, the SNB expects growth of 1.7%.

Recent months have seen consumer price inflation in the euro area in slightly negative territory. In May, annual inflation stood at -0.1% (cf. chart 2.11). At 0.8%, core inflation remained virtually unchanged compared to February (cf. chart 2.12). With petrol prices rising since March, inflation looks set to move into positive territory from mid-year onwards. However, medium-term inflation expectations derived from financial indicators have remained comparatively low.

The ECB began the implementation of extensive monetary easing measures, which were decided in March. In April, it increased its monthly securities purchases, as planned, by CHF 20 billion to CHF 80 billion, and, in June, purchased corporate bonds for the first time.

JAPAN

Economic trends in Japan continued to be volatile. GDP grew in the first quarter by 1.9%, thereby compensating the decline recorded in the preceding period (cf. chart 2.7). The development of private demand remained weak. Investment in equipment was down, and private consumption did not exceed its year-back level, despite a slight recovery. The recovery on the labour market continued; at 3.2%, the unemployment rate in April was at its lowest since the end of the 1990s (cf. chart 2.10).

The further appreciation of the yen and higher oil price have somewhat hampered growth prospects for the short term. Accordingly, companies are more cautious in their assessment of the business environment than at the beginning of the year. Another factor is the effect of the earthquake in Kumamoto in mid-April, which led to temporary production losses, particularly in the automotive industry. The government approved a supplementary budget amounting to 0.16% of GDP to support reconstruction. The SNB forecasts GDP growth of 0.7% for 2016. At the beginning of June, the government decided to postpone the planned VAT increase from April 2017 to October 2019. Accordingly, economic growth in 2017 is likely to be higher than expected in the SNB baseline scenario.

Under the influence of volatile goods prices, consumer price inflation declined once more into negative territory. In April, annual inflation stood at -0.3% (cf. chart 2.11), although excluding energy and food prices, it remained unchanged at 0.7% (cf. chart 2.12). The stronger yen will dampen inflation in the coming months. However, energy prices are likely to climb again somewhat, thereby reducing their negative effect on annual inflation. Overall, consumer prices look set to stagnate this year. Based on company surveys, longer-term inflation expectations continued to fall slightly, thus remaining significantly below the Japanese central bank's inflation target of 2%.

The Bank of Japan made no changes to its monetary policy, in place since the introduction of a negative interest rate in January. Following the earthquake, it decided on a credit facility totalling JPY 300 billion for banks in the affected region. It also lowered its growth forecast, and expects to attain its 2% inflation target by March 2018 at the latest.

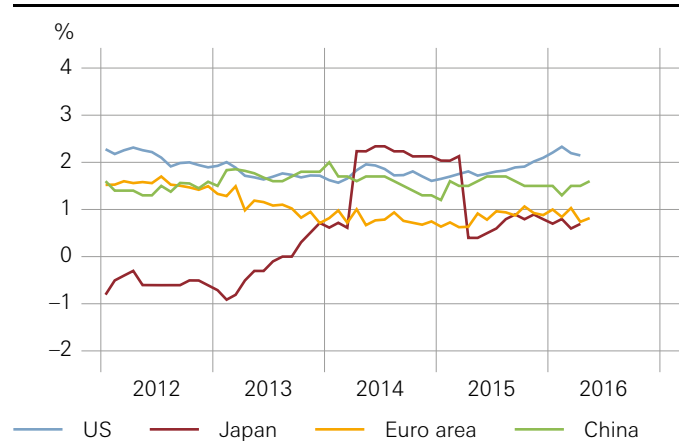
EMERGING ECONOMIES

Developments among the emerging economies remain mixed. In China, public infrastructure projects and strong lending growth as a result of expansionary monetary policy helped to stabilise the economy in the first quarter (cf. chart 2.8). Construction sector activity and the real estate market, in particular, picked up significantly. In India, the economy regained some momentum. In Russia and Brazil, however, the recession persisted.

Chart 2.12

CORE INFLATION RATES ¹

Year-on-year change

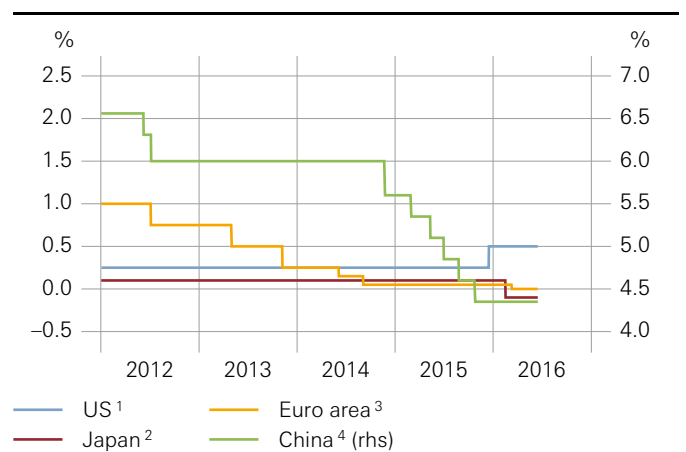


¹ Excluding food and energy.

Source: Thomson Reuters Datastream

Chart 2.13

OFFICIAL INTEREST RATES



¹ Federal funds rate.

² Call money target rate.

Source: Thomson Reuters Datastream

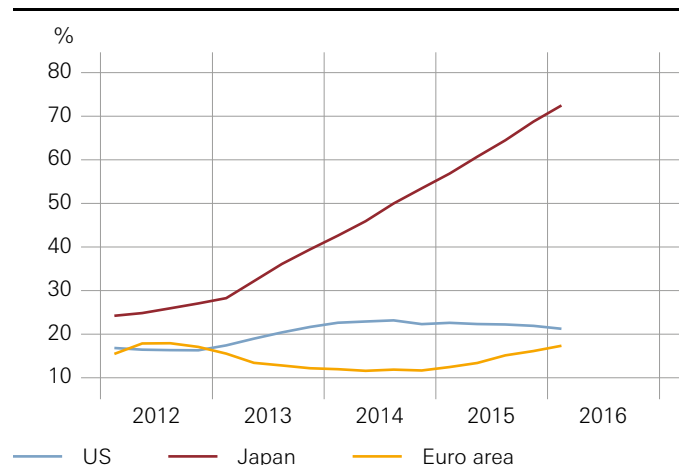
³ Main refinancing rate.

⁴ One-year lending rate.

Chart 2.14

MONETARY BASE

Relative to GDP



Source: Thomson Reuters Datastream

In China, the prospects for the current year have improved somewhat on the back of monetary and fiscal stimulus measures. Overall, value added is likely to continue to advance more strongly in services than in manufacturing. The SNB forecasts GDP growth of 6.7% for 2016, which lies within the target range set by the government. However, risks associated with high levels of corporate debt and overcapacity in heavy industry persist. In India, economic indicators point to a palpable revival in the first half of the year. For the whole year, the SNB continues to forecast growth within the range of the country's potential of approximately 7%.

In Russia, the higher oil price will support the economy. The recession, which has persisted since mid-2014, should end gradually over the course of this year. The forecast for Brazil remains muted due to high inflation and unemployment, although political uncertainty has lessened somewhat since the new government took office.

Inflation in the emerging economies has hardly changed in recent months. In China, inflation stood at 2.0% in May, thereby remaining below the central bank's target of 3% (cf. chart 2.11). In India, it was virtually unchanged at 5.8%, thereby remaining within the upper part of the target range of between 2% and 6%. In Russia and Brazil, inflation persisted at a high level (7.3% and 9.3% respectively), due in part to their weak currencies.

In March, the Chinese central bank again lowered its minimum reserve ratio to underpin the economy. The Indian central bank also decided on further monetary policy easing measures, lowering the reference rate in April by 25 basis points to 6.5% – after having left the rate unchanged since September of last year – and loosening the conditions of its standing facilities for credit. In Russia, the central bank reduced the reference interest rate by 50 basis points to 10.5%. By contrast, the Brazilian central bank kept the reference rate unchanged at a high level in order to combat inflation and currency depreciation.

3 Economic developments in Switzerland

In Switzerland, economic growth weakened in the first quarter of 2016. Growth momentum in manufacturing slowed and value added declined in many services sub-sectors. On the demand side, the picture was somewhat more favourable, with domestic final demand increasing strongly. Exports and imports also continued to expand, although the trend was subdued.

Overall, the utilisation of Swiss economic capacity remained unsatisfactory. In the first quarter, the output gap remained in negative territory and the seasonally adjusted unemployment figures again increased slightly over those at the previous quarterly assessment.

In the coming quarters, Switzerland's economy is likely to grow somewhat more strongly again. The SNB's growth forecast for 2016 remains unchanged at between 1% and 1.5%.

AGGREGATE DEMAND AND OUTPUT

Slower growth in the first quarter

According to the first official estimate, GDP in the first quarter was up by 0.4%, following growth of 1.7% in the fourth quarter of 2015. The performance of different industries varied. The subdued growth figures reflected, on the one hand, lower but still positive manufacturing momentum. On the other, value added in many services sub-sectors declined. This was particularly the case in the finance industry and in public administration. However, in the health industry and in construction, value added recorded a significant increase (cf. chart 3.1).

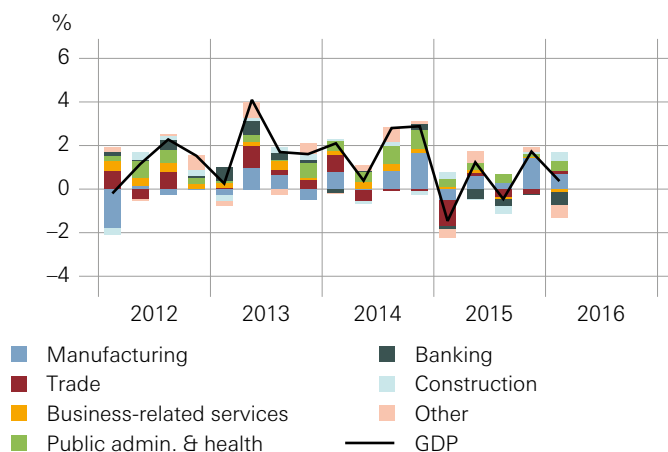
Sound growth in exports, apart from merchanting

Due to a decline in merchanting, growth in exports was down in the first quarter. However, other exports of goods and services increased markedly. Goods deliveries to Japan, Latin America and the OPEC states registered particularly significant advances. Exports of jewellery and precision instruments gained momentum, while those of machinery and metal products also developed favourably. Looking at services, the licence fees and business services positions made a particularly positive contribution.

Chart 3.1

CONTRIBUTIONS TO GROWTH, BY SECTOR

Change from previous period

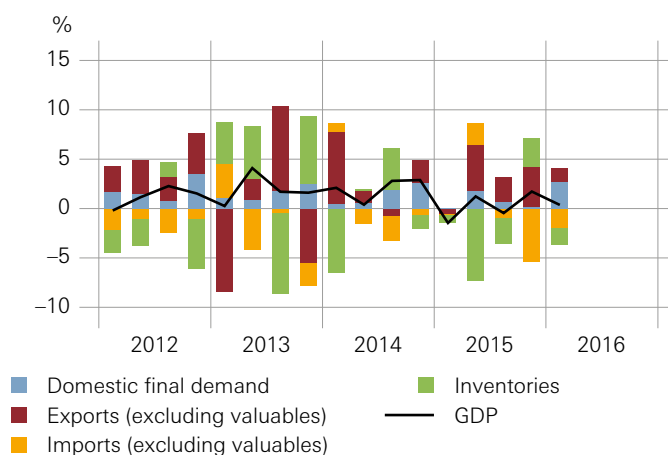


Source: State Secretariat for Economic Affairs (SECO)

Chart 3.2

CONTRIBUTIONS TO GROWTH IN DEMAND

Change from previous period

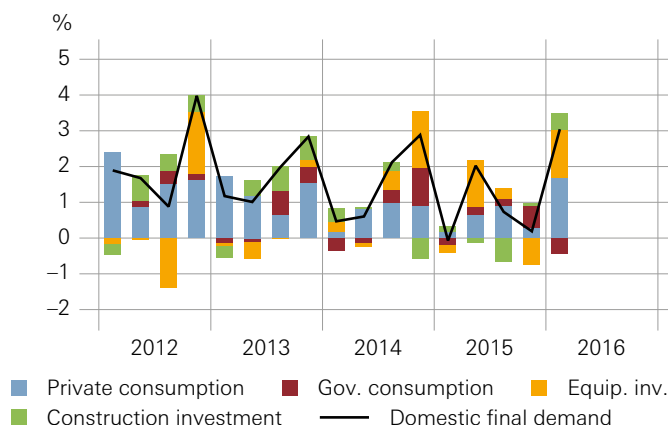


Source: SECO

Chart 3.3

DOMESTIC FINAL DEMAND, GROWTH CONTRIBUTIONS

Change from previous period



Source: SECO

Imports also lost some momentum overall. However, since they grew faster than exports, just as they had in the fourth quarter of 2015, net exports were once again slightly negative (cf. table 3.1). In the area of business, telecommunications, computer and information services, imports increased significantly. By contrast, goods imports were up only minimally, following the substantial increase in the previous quarter.

Equipment investment rose significantly, driven mainly by purchases of aircraft and spacecraft from abroad. Construction investment and, in particular, residential construction also expanded further. The downward trend in commercial construction persisted.

Strong domestic final demand

Domestic final demand rose strongly in the first quarter (cf. chart 3.3 and table 3.1). Thus consumer expenditure by private households caught up overall, following the weak previous quarters. Expenditure on health and heating registered particularly strong growth. In other areas, the increase in consumer expenditure remained subdued, despite sound growth in income.

Table 3.1

REAL GDP AND COMPONENTS

Growth rates on previous period in percent, annualised

	2012	2013	2014	2015	2014			2015				2016
					Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1
Private consumption	2.7	2.2	1.3	1.1	1.3	1.6	1.5	0.3	1.1	1.5	0.4	2.7
Government consumption	2.1	1.3	1.3	2.4	-1.0	3.0	8.6	-1.4	1.8	1.6	5.0	-3.3
Investment in fixed assets	2.9	1.2	2.1	1.5	-0.2	2.9	3.6	-0.2	4.3	-1.3	-2.5	6.9
Construction	2.9	3.1	3.3	-1.2	0.6	2.4	-5.4	1.7	-1.2	-6.2	0.8	4.5
Equipment	2.8	0.0	1.3	3.4	-0.8	3.3	9.9	-1.4	8.0	1.9	-4.5	8.5
Domestic final demand	2.7	1.8	1.5	1.3	0.6	2.1	2.9	-0.1	2.0	0.7	0.2	3.0
Change in inventories ¹	-1.0	0.7	-0.4	-1.5	0.1	4.2	-1.4	-0.8	-7.4	-2.6	2.9	-1.7
Total exports ²	3.0	0.0	4.2	3.4	2.4	-1.3	4.5	-0.9	9.0	4.8	7.7	2.6
Goods ²	0.9	-2.3	5.1	5.0	9.6	-5.2	1.1	2.8	11.8	5.8	17.9	0.2
Goods excluding merchanting ²	1.7	-1.0	4.0	0.6	2.7	10.8	-4.5	-9.6	4.3	4.8	13.4	8.6
Services	7.4	4.7	2.4	0.2	-10.7	7.0	11.6	-8.0	3.3	2.9	-11.1	8.4
Total imports ²	4.4	1.3	2.8	1.6	3.6	6.2	1.5	0.2	-5.4	2.5	13.6	4.9
Goods ²	2.3	0.7	1.7	-1.3	10.1	2.0	-8.0	0.4	-11.2	-0.6	22.4	1.5
Services	9.3	2.9	5.1	7.4	-8.8	15.7	24.0	-0.5	6.6	8.5	-1.1	11.7
Net exports ³	-0.2	-0.6	1.0	1.1	-0.3	-3.3	1.7	-0.6	6.8	1.5	-1.4	-0.6
GDP	1.1	1.8	1.9	0.9	0.4	2.8	2.9	-1.5	1.2	-0.5	1.7	0.4

1 Contribution to growth in percentage points (including statistical discrepancy).

2 Excluding valuables (non-monetary gold and other precious metals, precious stones and gems as well as works of art and antiques).

3 Contribution to growth in percentage points.

Source: SECO

LABOUR MARKET

Indications that the labour market is firming up have become stronger in recent months, with employment increasing further. In addition, the labour market indicators based on the KOF and Swiss Federal Statistical Office (SFSO) surveys have recovered further, as have the employment components of the purchasing managers' index (PMI). In contrast, unemployment continued to edge up.

Rise in employment

Employment statistics show that the seasonally adjusted number of employed persons again rose somewhat more strongly in the first quarter, after minimal increases in the previous quarters (cf. chart 3.4).

However, according to employment statistics, the total number of full-time equivalent jobs declined overall. In manufacturing, in particular, further jobs were lost, while employment in the services sector, which accounts for around three-quarters of jobs, more or less stagnated (cf. chart 3.5). Nevertheless, when measured by the number of people employed, the decline in the number of jobs in the overall economy is less pronounced because of a shift towards part-time work. It is also important to note that conclusions based on the employment statistics are unreliable as these figures are currently being revised.

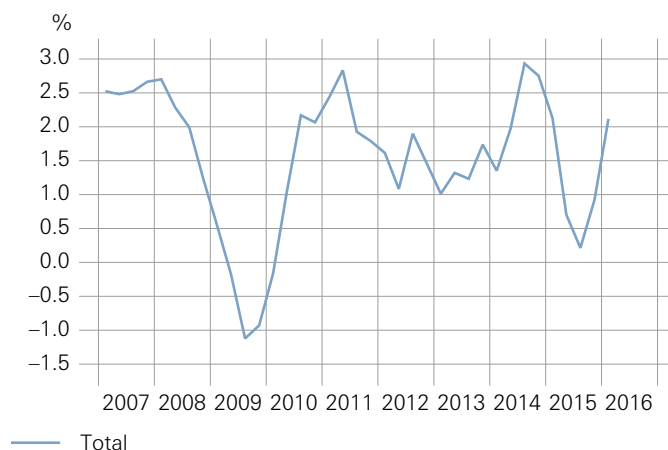
Slight increase in unemployment

The number of people registered as unemployed at the regional employment offices continued to rise. At the end of May, a total of 150,000 people were recorded as unemployed, excluding seasonal fluctuations. This is an increase of around 14,000 people since the end of 2014. In May, the seasonally adjusted unemployment rate was 3.5% (cf. chart 3.6). Unemployment figures measured in line with the International Labour Organization (ILO) definition, which are obtained in a survey of households, increased only slightly. However, in recent years these figures have risen somewhat more strongly overall than those for unemployment as measured by the regional employment offices.

Chart 3.4

EMPLOYED PERSONS

Change from previous period

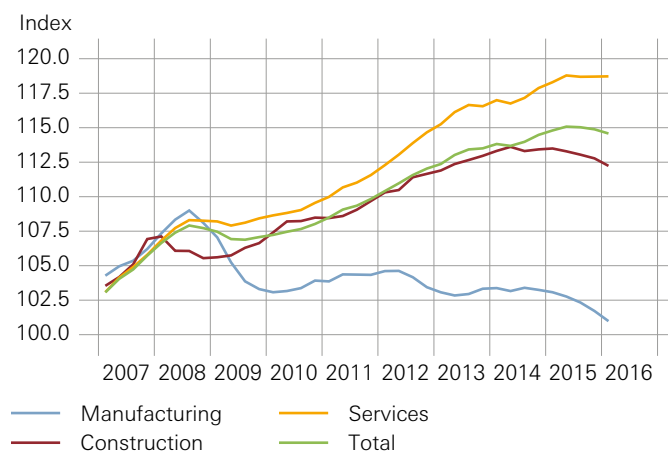


Source: Swiss Federal Statistical Office (SFSO); seasonal adjustment: SNB

Chart 3.5

FULL-TIME EQUIVALENT JOBS

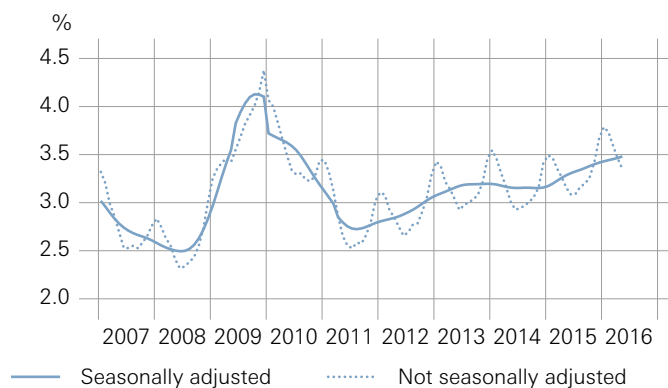
Q1 2006 = 100



Source: SFSO; seasonal adjustment: SNB

Chart 3.6

UNEMPLOYMENT RATE

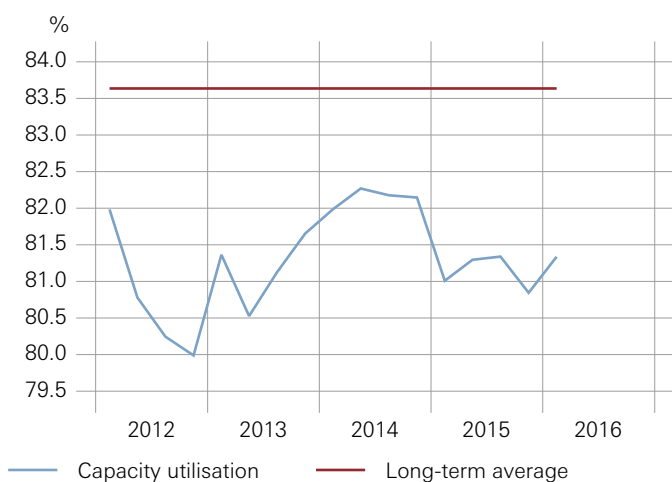


Unemployed registered with the regional employment offices, as a percentage of the labour force according to the 2000 census (labour force: 3,946,988 persons) up to 2009, and according to the 2010 census (labour force: 4,322,899 persons) from 2010.

Source: SECO

Chart 3.7

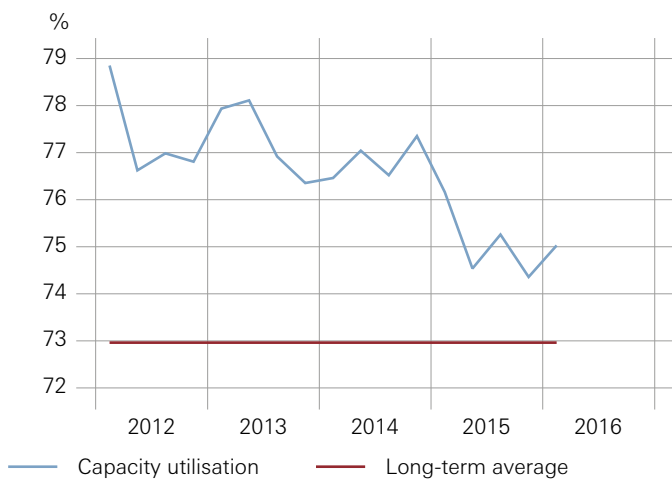
CAPACITY UTILISATION IN MANUFACTURING



Source: KOF Swiss Economic Institute

Chart 3.8

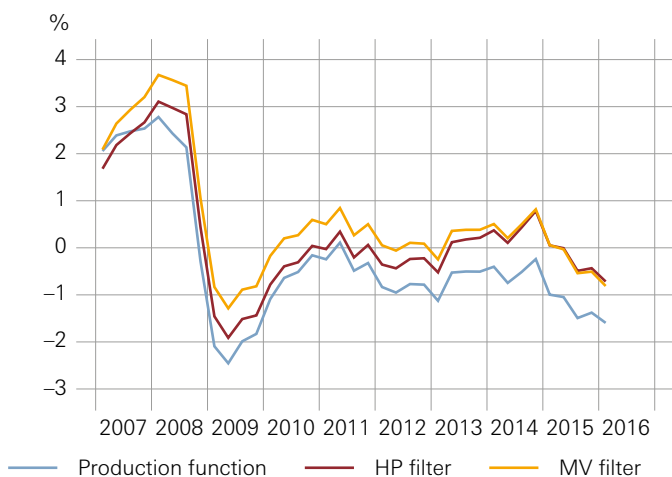
CAPACITY UTILISATION IN CONSTRUCTION



Source: KOF Swiss Economic Institute

Chart 3.9

OUTPUT GAP



Source: SNB

CAPACITY UTILISATION

Underutilisation in manufacturing

According to the KOF survey, utilisation of technical capacity in manufacturing increased, from 80.9% to 81.5%, in the first quarter. It nonetheless remains well below the long-term average (cf. chart 3.7). Machine utilisation in the construction industry also increased in the first quarter. Unlike in manufacturing, capacity utilisation in construction remains above its long-term average (cf. chart 3.8). As for the services sector, the surveys continue to point to an average level of capacity utilisation.

Negative output gap

The output gap, which is defined as the percentage deviation of observed GDP from estimated aggregate potential output, shows how well the production factors in an economy are being utilised. Given the subdued GDP growth in the first quarter, the output gap again widened. Estimated potential, calculated by means of a production function, showed an output gap of -1.6%, for the first quarter, compared to -1.4% in the previous quarter. Other methods for estimating potential output (Hodrick-Prescott filter and multivariate filter) suggest a less pronounced negative output gap (cf. chart 3.9).

The different estimates reflect the various ways of calculating potential output. The production function approach considers the labour market situation and the stock of capital in the economy. Since the supply of labour, in particular, has risen steadily in recent years – primarily as a result of immigration – potential output and, hence, the output gap are larger when calculated with this method than with purely statistical filtering methods.

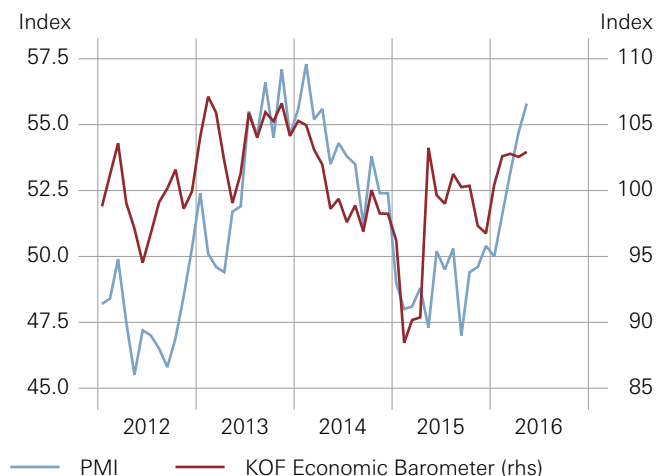
OUTLOOK FOR THE REAL ECONOMY

After a short-term softening in growth in the first quarter, the economy in Switzerland is likely to advance more positively over the rest of the year. Indicators available so far suggest a recovery in the second quarter. Since the beginning of the year, the purchasing managers' index in manufacturing has risen markedly, and the upward trend in exports continued in April. The KOF economic barometer also points to sound growth (cf. chart 3.10). In addition, the outlook for employment has brightened somewhat recently (cf. chart 3.11).

Two main factors are responsible for the favourable economic outlook. First, the global economy is likely to strengthen (cf. chapter 2). Second, the dampening effect on GDP growth of the past appreciation in the Swiss franc is gradually fading. In this context, exports are likely to recover further, while the positive trend in the domestic economy will probably continue. Sounder growth will lead to a gradual narrowing of the negative output gap, and the labour market will stabilise. For 2016, the SNB continues to forecast GDP growth of between 1.0% and 1.5%.

Chart 3.10

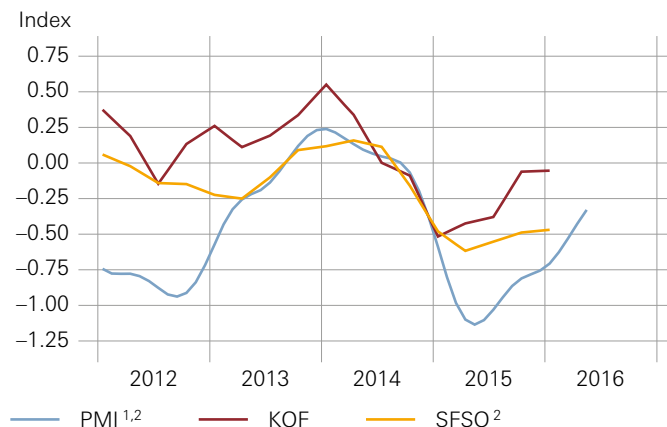
LEADING INDICATORS



Sources: Credit Suisse, KOF Swiss Economic Institute

Chart 3.11

EMPLOYMENT LEADING INDICATORS



1 Monthly figures.

2 Trend component: SNB.

Sources: Credit Suisse, KOF Swiss Economic Institute, SFSO

In the last few months, consumer prices have ceased their month-on-month decline, following the extensive stabilisation of producer prices in the second half of 2015. While both prices indices still remain lower than their year-back value, the negative annual rates of inflation have receded.

Recent months saw little change in inflation expectations, with negative annual rates of inflation expected to continue in the short term. By contrast, longer-term inflation expectations remain in the low positive range and are thereby consistent with the SNB's definition of price stability.

CONSUMER PRICES

Annual CPI inflation rate still negative

The annual inflation rate as measured by the national consumer price index (CPI) was -0.4% in May 2016, thus remaining in negative territory. The negative annual rates have, however, declined significantly since the beginning of the year (cf. table 4.1). This is primarily due to the easing of effects associated with the appreciation of the Swiss franc following the discontinuation of the minimum exchange rate in January 2015.

Table 4.1

SWISS CONSUMER PRICE INDEX AND COMPONENTS

Year-on-year change in percent

	2015	2015			2016	2016		
		Q2	Q3	Q4	Q1	March	April	May
Overall CPI	-1.1	-1.1	-1.4	-1.4	-1.0	-0.9	-0.4	-0.4
Domestic goods and services	0.1	0.2	0.0	-0.3	-0.4	-0.2	-0.1	-0.1
Goods	-0.7	-0.7	-1.0	-1.0	-1.3	-1.0	-0.8	-0.7
Services	0.3	0.5	0.3	-0.1	-0.2	0.0	0.0	0.1
Private services excluding housing rents	0.4	0.5	0.4	-0.2	-0.2	0.0	0.2	0.1
Housing rents	0.8	1.2	0.9	0.3	0.1	0.2	0.2	0.2
Public services	-0.8	-0.9	-0.9	-0.5	-0.5	-0.5	-0.5	-0.3
Imported goods and services	-4.7	-4.8	-5.4	-4.4	-2.8	-2.8	-1.0	-1.4
Excluding oil products	-2.5	-2.7	-3.1	-2.7	-1.5	-1.3	0.3	-0.2
Oil products	-17.4	-16.6	-18.5	-14.9	-11.3	-12.8	-9.5	-9.2

Sources: SFSO, SNB

Slightly negative contribution to annual inflation rate from import goods

The price index for CPI imported goods, excluding oil products, has risen since the beginning of 2016. This reflects price increases for a number of products, including package holidays and air travel. The contribution made by import goods excluding oil products to the annual inflation rate moved back into positive territory in April for the first time in a long while (cf. chart 4.1).

Prices for oil products have also been rising since February. However, they remain significantly lower than the year-back prices and are almost solely responsible for the negative annual CPI inflation rate.

Domestic goods also make small negative contribution

The prices for domestic goods remain marginally down year-on-year, despite also increasing somewhat since the beginning of the year. The negative contribution made by domestic goods to inflation reflects the decline in prices of goods compared to the previous year (cf. chart 4.2). By contrast, the prices of services are at almost the same level as a year earlier.

Rent inflation close to zero

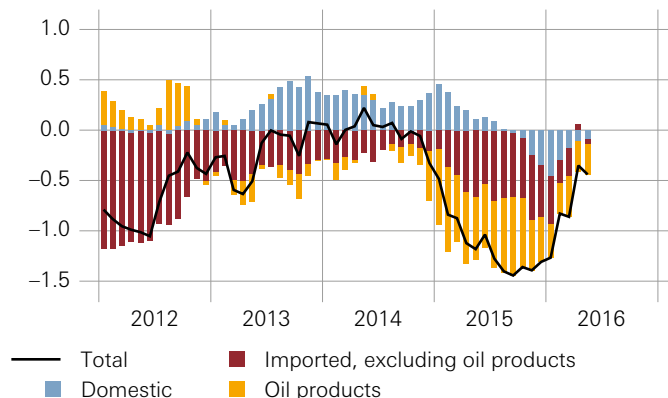
Housing rents make up almost one-third of services included in the CPI. As chart 4.3 shows, the annual inflation of housing rents has been close to zero since November 2015. This stability is partially attributable to the reference interest rate, which has remained unchanged since June 2015 (cf. chart 4.3)

The reference interest rate is based on banks' average mortgage rates. It is decisive for the adjustment of rents based on mortgage rate changes.

Chart 4.1

CPI: DOMESTIC AND IMPORTED GOODS AND SERVICES

Year-on-year change in CPI in percent. Contribution of individual components, in percentage points.

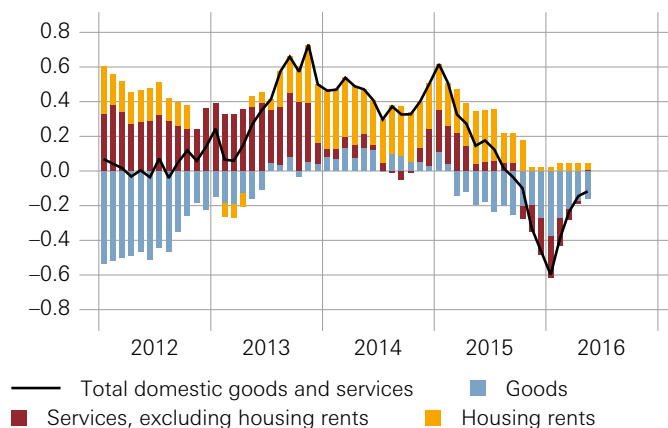


Sources: SFSO, SNB

Chart 4.2

CPI: DOMESTIC GOODS AND SERVICES

Year-on-year change in domestic CPI in percent. Contribution of individual components, in percentage points.

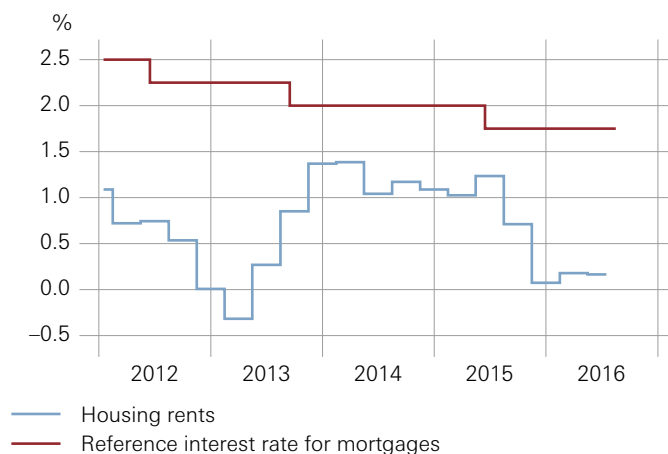


Sources: SFSO, SNB

Chart 4.3

HOUSING RENTS

Year-on-year change

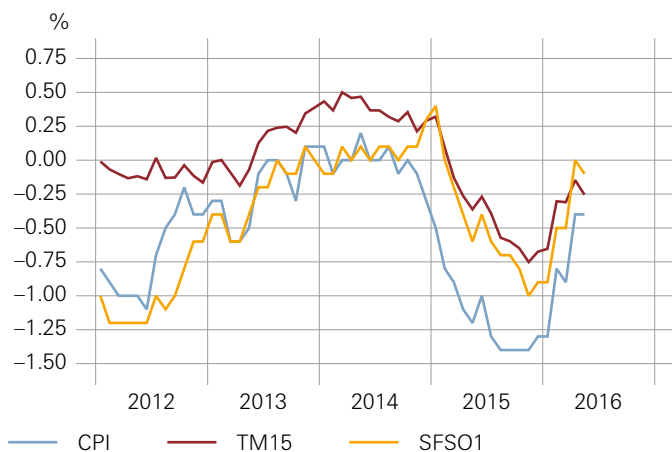


Sources: Federal Office for Housing (FOH), SFSO

Chart 4.4

CORE INFLATION RATES

Year-on-year change

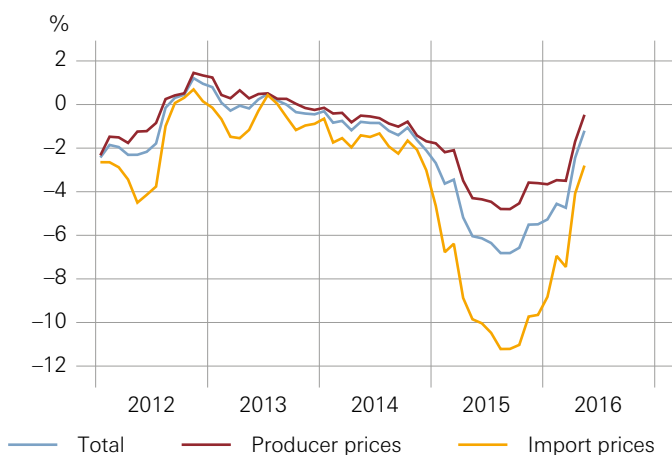


Sources: SFSO, SNB

Chart 4.5

PRODUCER AND IMPORT PRICES

Year-on-year change

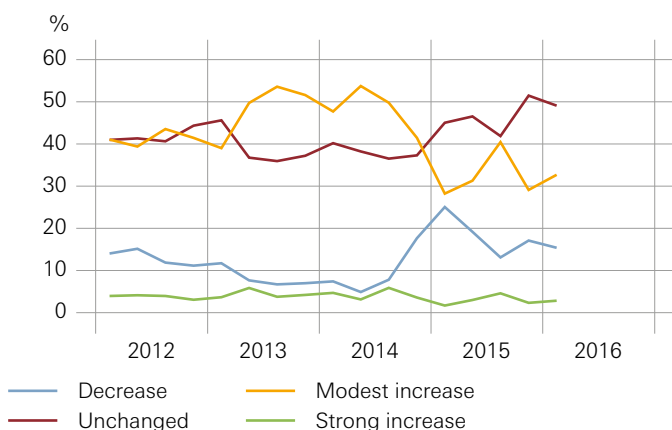


Source: SFSO

Chart 4.6

PRICE EXPECTATIONS

Survey of households on expected movements in prices for coming 12 months



Sources: SECO, SNB

Core inflation rates rise towards zero

While core inflation rates remain in negative territory, they have risen considerably since January (cf. chart 4.4). In May 2016, the SFSO core inflation rate 1 (SFSO1) and the trimmed mean calculated by the SNB (TM15) were -0.1% and -0.3% respectively. The core inflation rates thus continue to show smaller deviations from price stability than the annual CPI inflation rate.

PRODUCER AND IMPORT PRICES

Annual inflation rate for producer and import prices still negative

Producer prices have largely stabilised since summer 2015, while the considerably more volatile import prices decreased only slightly in the same time period. The negative annual inflation rates for both price indices have thus declined significantly; a marked convergence of the two indices may also be observed (cf. chart 4.5).

INFLATION EXPECTATIONS

Stable inflation expectations

Inflation expectations have remained largely unchanged in recent months. They are negative for 2016 but positive as of 2017. The medium and long-term inflation expectations are consistent with price stability, which the SNB equates to a rise in the CPI of less than 2% per year.

Rates of inflation expected to increase

According to the survey of households conducted by SECO in April 2016, the share of respondents expecting prices to rise over the next twelve months has increased slightly (cf. chart 4.6). By contrast, slightly fewer households than three months ago expected no change or a drop in prices.

According to the *Credit Suisse ZEW Financial Market Report*, the share of financial analysts surveyed expecting inflation rates to rise in the next six months increased from 35% in February 2016 to 43% in May. Simultaneously, the share of respondents expecting lower inflation rates, i.e. that rates would move further into negative territory, receded from 12% to 3% . The number of respondents expecting no change was almost the same as three months earlier.

Talks held by the SNB delegates for regional economic relations with companies from all sectors of the economy also show the stability of short-term inflation expectations. The respondents surveyed in the second quarter of 2016 expected inflation of -0.2% over the next 6–12 months, compared to -0.3% in the previous quarter.

**Medium and long-term inflation expectations
in positive range**

In addition, the discussions with the SNB's delegates for regional economic relations indicated that in the second quarter of 2016, the respondents surveyed expect the inflation rate to be 0.5% in three to five years (first quarter 2016: 0.7%). Participants in Deloitte's CFO survey in the first quarter put inflation in two years' time at 0.7%, unchanged from the previous quarter.

Surveys on inflation expectations over longer-term horizons suggest that these are still firmly anchored, with only minor fluctuations within their historical ranges.

5

Monetary developments

At its monetary policy assessment of mid-March 2016, the SNB left its monetary policy unchanged. Short-term interest rates remained largely stable in the three months that followed, while long-term interest rates fell to a new all-time low in June. Sight deposits held at the SNB increased further.

On the foreign exchange market, the Swiss franc weakened somewhat over the months of April and May, but quickly made up these losses by mid-June. This was mainly due to the growing uncertainty surrounding the outcome of the referendum in the UK on whether to leave the EU (Brexit). By historical standards, the Swiss franc remains highly valued.

Monetary aggregates are still exhibiting low growth rates. Slackening growth in monetary aggregates observed in the past two years thus continued. Lending growth rates also fell substantially in this period. As a result of the strong money and lending growth from 2008 to 2013, monetary and credit aggregates remain at a very high level, however.

SUMMARY OF MONETARY POLICY SINCE THE LAST ASSESSMENT

Expansionary monetary policy remains unchanged

The SNB confirmed its monetary course at its monetary policy assessment on 17 March 2016. It decided to leave the target range for the three-month Libor unchanged at between -1.25% and -0.25% . It also left unchanged, at -0.75% , the interest rate on sight deposits held by banks and other financial market participants at the SNB which exceed a given threshold.

The SNB reaffirmed its willingness to play an active role in the foreign exchange market in order to influence exchange rate developments, where necessary. The negative interest rate and the SNB's willingness to intervene in the foreign exchange market serve to ease pressure on the Swiss franc. In this way, the SNB's monetary policy helps to stabilise price developments and support economic activity.

Higher sight deposits at the SNB

Since the monetary policy assessment of March 2016, total sight deposits held at the SNB have increased. In the week ending 10 June 2016 (last calendar week before the mid-June assessment), they amounted to CHF 493.8 billion, up by CHF 12.5 billion compared to the last calendar week preceding the mid-March 2016 assessment (CHF 481.3 billion). Between the assessments in mid-

March and mid-June 2016, sight deposits at the SNB averaged CHF 490.5 billion. Of this amount, CHF 420.6 billion were accounted for by the sight deposits of domestic banks and the remaining CHF 69.9 billion by other sight deposits.

High level of banks' surplus reserves

Between 20 February and 19 May 2016, statutory minimum reserves averaged CHF 14.8 billion. Overall, banks exceeded the requirement by some CHF 411.5 billion on average (previous period: CHF 396.3 billion). Banks' surplus reserves have increased further.

MONEY AND CAPITAL MARKET INTEREST RATES

Stable money market interest rates

In the second quarter of 2016, money market interest rates remained close to the interest rate on sight deposits at the SNB (-0.75%). As shown in chart 5.1, this applies to both secured (SARON) and unsecured money market transactions (three-month Libor).

Long-term interest rates at all-time low

The yield on ten-year Confederation bonds edged up briefly in April, before falling again in May and June. In mid-June, it was at a new all-time low of 0.5% (cf. chart 5.2).

Flatter yield curve

The short end of the yield curve for Confederation bonds rose slightly compared to the previous quarter. This increase is consistent with indicators for short-term interest rate expectations, which also rose marginally in the course of the second quarter of 2016. By contrast, longer-term Confederation bonds fell slightly, which resulted in a somewhat flatter yield curve overall than three months ago (cf. chart 5.2).

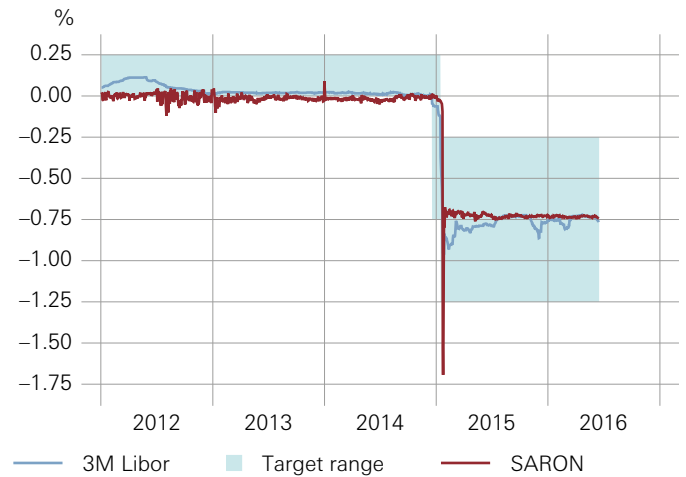
Low long-term real interest rates

As in the previous quarter, the estimated long-term real interest rate was close to 0% in mid-June (cf. chart 5.3). The long-term real interest rate thus remains at a historically low level.

The real interest rate estimate is based on the development of the ten-year yield on Confederation bonds and the estimated inflation expectations for the same time horizon, determined using a vector autoregressive (VAR) model.

Chart 5.1

MONEY MARKET RATES

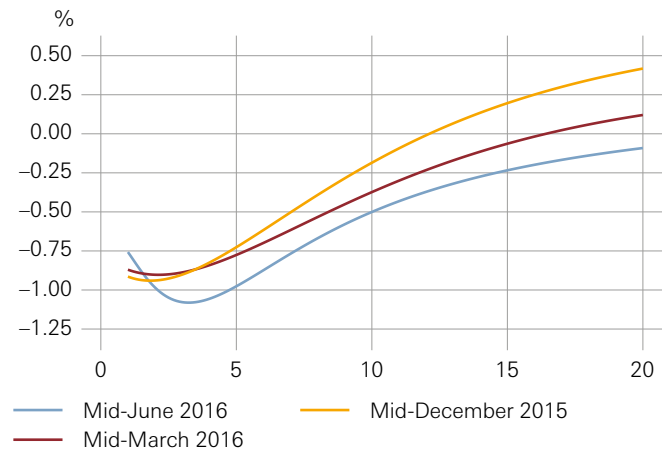


Sources: Bloomberg, SIX Swiss Exchange Ltd, SNB

Chart 5.2

TERM STRUCTURE OF CONFEDERATION BONDS

Years to maturity (hor. axis), Nelson-Siegel-Svensson method.



Source: SNB

Chart 5.3

ESTIMATED REAL INTEREST RATE

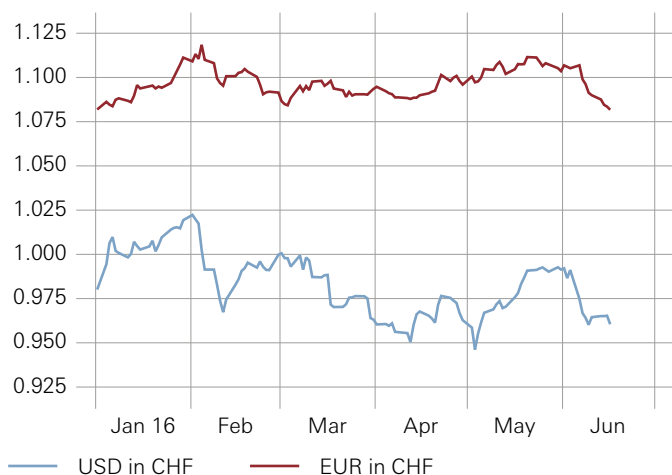
10-year Confederation bonds
Inflation expectations estimated with VAR model



Source: SNB

Chart 5.4

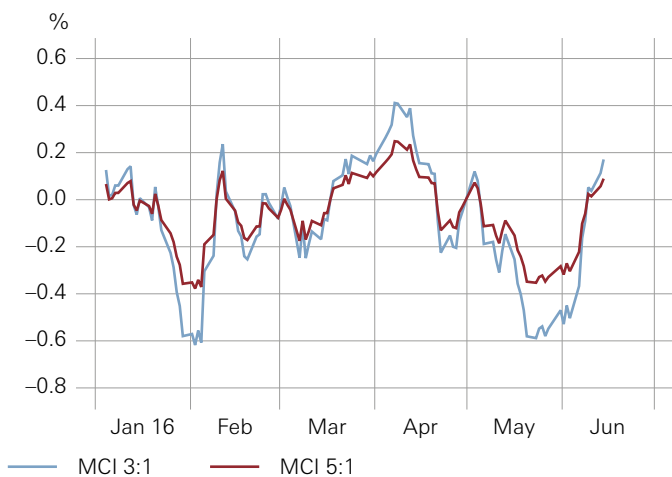
EXCHANGE RATES



Source: SNB

Chart 5.5

MCI NOMINAL



Source: SNB

Chart 5.6

REAL EXTERNAL VALUE OF SWISS FRANC

Export-weighted, January 1999 = 100



Source: SNB

EXCHANGE RATES

Appreciation of the Swiss franc against the euro and the US dollar in June

The Swiss franc lost a little ground against the euro and the US dollar between the beginning of April and the end of May. Amid growing uncertainty regarding the outcome of the EU referendum in the UK, it largely made up these losses so that by mid-June, it was trading somewhat higher against these two currencies than three months earlier (cf. chart 5.4.)

Monetary conditions somewhat tighter

In nominal, export-weighted terms, the Swiss franc has appreciated slightly since the monetary policy assessment in March. With short-term interest rates virtually unchanged, monetary conditions have tightened somewhat.

The Monetary Conditions Index (MCI) in chart 5.5 combines changes in the three-month Libor with the nominal export-weighted external value of the Swiss franc to provide a measure of monetary conditions. To take account of uncertainty regarding the relative impact of changes in interest rates and exchange rates, two versions of the index are used, with each version assigning a different weight to the two components. The index is reset to zero at the time of the last monetary policy assessment. Positive MCI values indicate a tightening of monetary policy.

Slight decline in Swiss franc's real external value until May

The export-weighted real external value of the Swiss franc in May was slightly below its level in March and more than 4% lower than one year ago. The Swiss franc's real appreciation has thus declined by about half since the discontinuation of the minimum exchange rate. Yet in a longer-term comparison, it remains significantly overvalued (cf. chart 5.6).

SHARE AND REAL ESTATE PRICES

Share prices declined in June

After having recorded significant losses at the beginning of 2016, share prices in Switzerland partially recovered between mid-February and the end of May. Speculation about the outcome of the referendum in the UK on whether to leave the EU led to a renewed decline (cf. chart 5.7).

Implied volatility derived from options on SMI futures contracts, which serves as a measure of the uncertainty on the stock market, increased significantly in January and at the beginning of February 2016. It subsequently decreased in step with the recovery in share prices, before rising again in June as a result of speculation around Brexit.

Bank shares under pressure

Of the four SMI sub-indices shown in chart 5.8, industrials, consumer goods and health care have performed significantly better than financial services since the beginning of 2016. As a result of weak quarterly figures for domestic and foreign banks, bank share prices remained under pressure.

Rising prices for residential property

Overall, real estate price indices based on transaction prices suggest that prices for residential property rose somewhat more strongly in the first quarter of 2016 than in previous quarters (cf. chart 5.9). Against the background of modest GDP growth, imbalances on the real estate market thus increased slightly.

The price increase affected privately owned apartments significantly more than single-family houses. In a longer-term comparison, too, i.e. over the past ten years, prices of privately owned apartments rose more strongly than those of single-family houses.

Chart 5.7

SHARE PRICES AND VOLATILITY

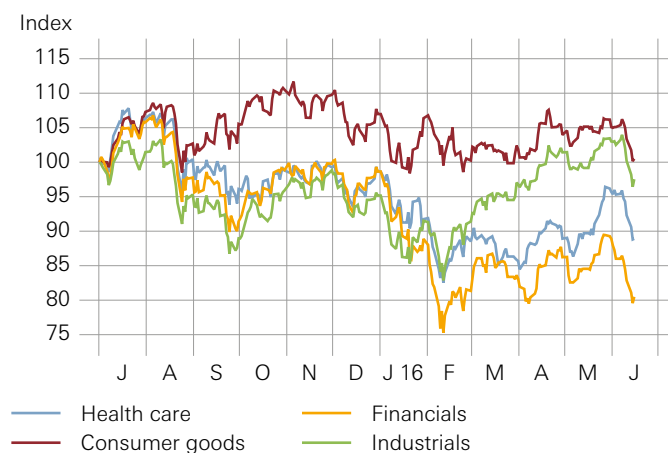


Sources: Bloomberg, Thomson Reuters Datastream

Chart 5.8

SELECTED SPI SECTORS

Beginning of period = 100

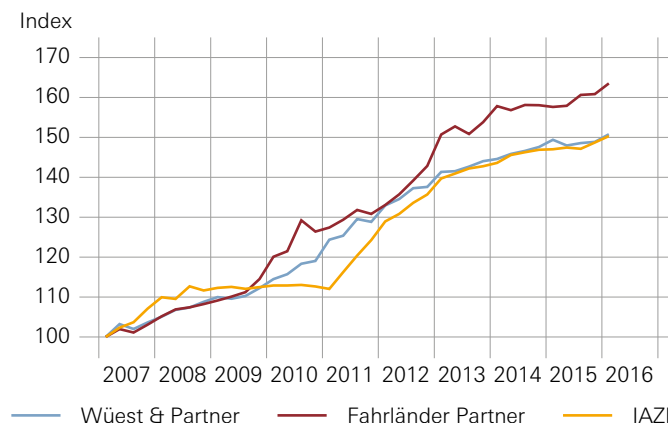


Source: Thomson Reuters Datastream

Chart 5.9

TRANSACTION PRICES, PRIVATELY OWNED APARTMENTS

Nominal (hedonic), beginning of period = 100



Sources: Fahrländer Partner, IAZI, Wüest & Partner

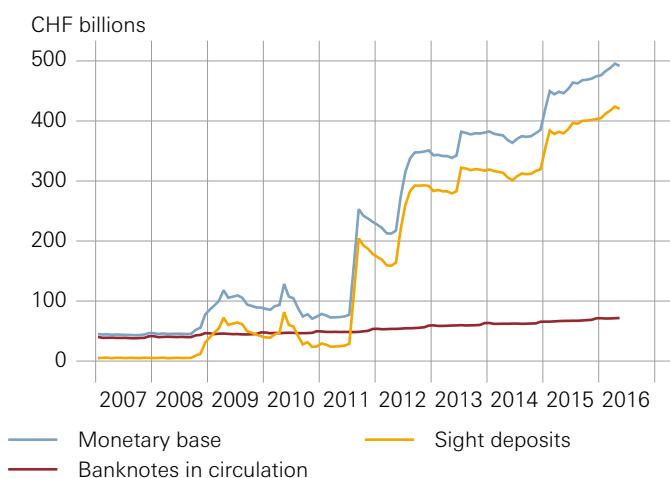
MONETARY AND CREDIT AGGREGATES

Growing monetary base

The monetary base, which consists of banknotes in circulation and sight deposits of domestic banks held at the SNB, increased further between February and May 2016, to an average of CHF 492 billion in May (cf. chart 5.10). While banknotes in circulation increased by CHF 0.9 billion, domestic banks' sight deposits rose by CHF 7.6 billion. Aside from other factors, movements in domestic banks' sight deposits are also influenced by the SNB's interventions on the foreign exchange market.

Chart 5.10

MONETARY BASE



Source: SNB

Table 5.1

MONETARY AGGREGATES AND BANK LOANS

Year-on-year change in percent

	2015	2015	2015	2015	2016	2016	2016	2016
		Q2	Q3	Q4	Q1	March	April	May
M1	-0.1	0.2	0.7	-2.3	-0.6	-0.2	0.9	0.9
M2	1.2	0.9	1.0	1.1	1.8	2.1	2.6	2.4
M3	1.9	1.7	1.6	1.8	1.6	1.7	2.3	2.0
Bank loans, total ^{1,3}	1.9	1.6	1.6	1.7	1.5	1.6	1.9	
Mortgage claims ^{1,3}	3.3	3.5	3.2	2.9	2.6	2.6	2.6	
Households ^{2,3}	3.4	3.5	3.4	3.2	2.9	2.8	2.8	
Private companies ^{2,3}	3.3	3.7	3.0	2.6	2.4	2.5	2.6	
Other loans ^{1,3}	-5.3	-7.3	-6.4	-4.4	-4.5	-4.0	-2.1	
Secured ^{1,3}	-0.4	0.5	0.1	-5.8	-2.7	-2.7	0.6	
Unsecured ^{1,3}	-8.5	-12.2	-10.8	-3.4	-5.8	-4.9	-4.1	

1 Monthly balance sheets.

2 Credit volume statistics.

3 Growth rates for the bank loans item and its components include information provided by banks on changes in their classification practices. Consequently, they may deviate from growth rates published on the SNB's data portal, data.snb.ch.

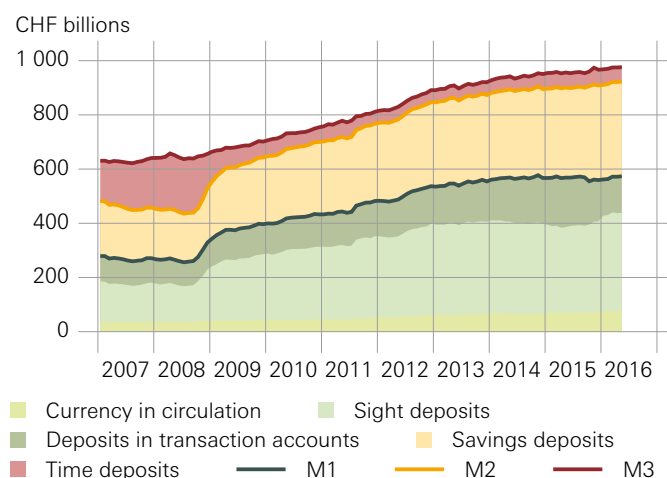
Source: SNB

Marginal changes in broad monetary aggregates

After recording a robust increase from 2008 to 2013 (cf. chart 5.11), the M1, M2 and M3 monetary aggregates, which measure monetary aggregates held by the public, have shown minor changes over the past two years. At the end of May, they were all slightly higher than one year earlier (cf. table 5.1). The M1 monetary aggregate (notes and coins in circulation, sight deposits and transaction accounts) was CHF 573.6 billion, whereas M2 (M1 plus savings deposits) amounted to CHF 922.9 billion and M3 (M2 plus time deposits) to CHF 976.1 billion.

Chart 5.11

MONETARY AGGREGATES



Source: SNB

Lending growth slows

Slower growth in bank lending observed since 2014 continued in the first quarter of 2016 (cf. chart 5.12). While the annual growth rate of bank lending had always amounted to roughly 4% from the onset of the financial and economic crisis to mid-2014 – with only modest fluctuations – it was 1.5% in the first quarter of 2016. This slowdown in lending growth is attributable to developments in both mortgage claims and other loans.

Despite mortgage rates being at historically very low levels, growth in banks' mortgage claims, which make up roughly 85% of all bank lending, continued to lose momentum. Mortgage loans recorded a 2.6% year-on-year increase in the first quarter of 2016. Other loans, which are significantly more volatile, decreased by 4.5% in the same period (cf. table 5.1).

Growth in lending by sector

Both households and non-financial companies have benefited from favourable financing conditions since the beginning of the financial and economic crisis, as reflected in a fairly continuous rise in bank loans extended to these two important client segments (cf. chart 5.13). At the end of March 2016, loans to households were up CHF 18.7 billion (2.6%) year-on-year, while loans to non-financial companies, with an increase of CHF 0.2 billion (0.1%), remained virtually unchanged. Loans to financial companies, which exhibit greater volatility at a significantly lower volume, declined by CHF 4.4 billion (–8.5%) compared to the previous year.

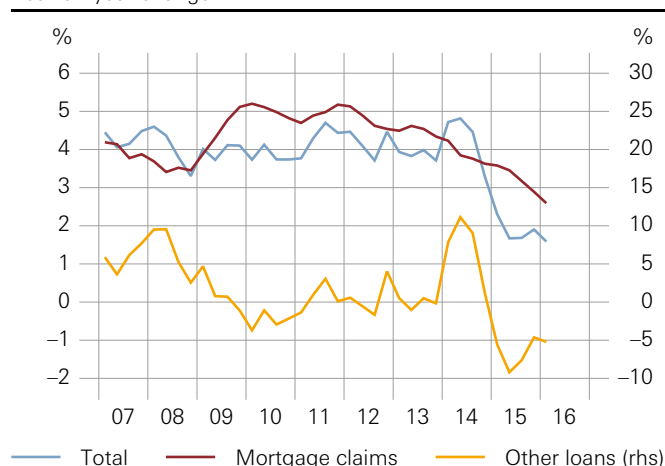
Rising loan ratio

The robust growth in bank lending recorded in the last ten years is reflected in the loan ratio, i.e. the ratio of bank loans to nominal GDP (cf. chart 5.14). After a sharp rise in the 1980s, this ratio remained largely unchanged until 2008. Since the onset of the financial and economic crisis, it has increased again substantially. Despite the slowdown in lending growth in the past two years, bank loans continue to grow more strongly than nominal GDP. Risks to financial stability emanating from the Swiss mortgage and real estate markets could thus intensify further.

Chart 5.12

BANK LOANS, IN SWISS FRANCS

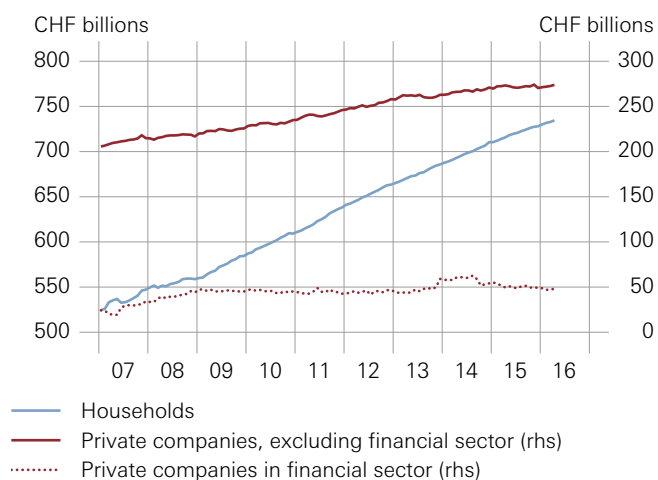
Year-on-year change



Source: SNB

Chart 5.13

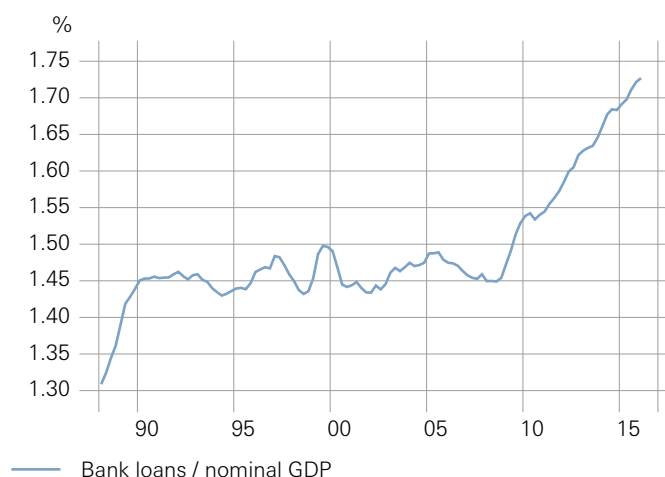
LOANS TO HOUSEHOLDS AND COMPANIES



Source: SNB

Chart 5.14

BANK LOANS AS A PERCENTAGE OF GDP



Source: SNB

Business cycle trends

SNB regional network

Report for the attention of the Governing Board of the Swiss National Bank for its quarterly assessment of June 2016

Second quarter of 2016

The Swiss National Bank's delegates for regional economic relations are constantly in touch with companies from different areas of the economy. This report is based on discussions conducted from the beginning of April to the end of May 2016 with 240 managers and entrepreneurs on the current and future situation of their companies and on the economy in general. The selection of companies differs from one quarter to the next. It reflects the industrial structure of the Swiss economy, based on the composition of GDP (excluding agriculture and public services).

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

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Martin Wyss
Daniel Hanimann
Aline Chabloz
Rita Kobel
Markus Zimmerli

SUMMARY

According to this survey, the Swiss economy recorded slightly higher growth than in the previous quarter. Real turnover at the companies surveyed was up compared to the first quarter of 2016 and increased noticeably year-on-year, although differences from one segment to another remain. The margin situation has eased somewhat at numerous companies, but is still challenging. Production capacity overall remains underutilised.

Companies have expressed confidence that real turnover will continue to develop positively in the coming months, and a further upturn in foreign demand is expected. Moreover, margins are likely to continue to improve, due to enhanced efficiency and cost-cutting measures. The exchange rate situation also contributes to this more favourable assessment.

Staff numbers in the services sector are likely to increase somewhat in the next few months, whereas those in manufacturing will probably again decrease slightly. Willingness to invest is marginally up compared to previous quarters.

BUSINESS ACTIVITY

Overall turnover slightly on the rise

Real turnover in manufacturing remained unchanged at the level of the previous quarter, but was noticeably higher than one year ago. Only the pharmaceutical industry registered an increase in real turnover in the quarter under review. In all other lines of manufacturing, business was flat. The marked weakness in demand recorded by watchmaking companies is having knock-on effects in several other industries as well.

As to export business, sales to North America, northern Europe and Germany remain fairly dynamic. Demand from the automotive industry continues to be particularly high. The improvement in economic activity in Italy is having a positive impact, and there are some instances of increased demand from Japan. By contrast, many industries are feeling the effects of the unfavourable economic situation in Russia and Brazil, as well as the slowdown in China and the Middle East.

Business in construction has accelerated, particularly in structural and civil engineering. Turnover in the finishing trade remained at the level of the preceding quarter.

In the services sector, real turnover rose slightly compared to the previous quarter. Several services showed a similar development, notably the hospitality industry, specialised asset management, engineering and architecture firms as well as facility management services. Retailing continued to present a heterogeneous picture, albeit with a slightly upward trend overall. Cross-border shopping and the shift to online shopping, which continues to experience strong growth, present a significant challenge to a large number of companies.

CAPACITY UTILISATION

Ongoing underutilisation

Overall, the companies surveyed stated that production capacity remains underutilised. 35% of the survey respondents rated their utilisation as lower than usual.

Around half the responding companies in manufacturing reported a slight to significant underutilisation of capacity, with most lines being affected. Underutilisation is particularly marked in the mechanical and electrical engineering industries (MEM industries) and among firms producing precision instruments.

In construction, seasonally adjusted utilisation of technical capacity was somewhat higher than in the previous quarter, due to developments in the main lines of construction business. Lower-lying areas continue to notice the increased competitive pressure from mountain-region construction firms. The reason usually cited is a lack of projects in the mountain areas as a result of the vote to curb second-home ownership ('Zweitwohnungsinitiative').

The services sector presented a heterogeneous picture, albeit an improved one over the preceding quarter. Around half the segments reported underutilisation of infrastructure (office and retail space as well as IT and transport capacity), among them retailing, logistics, hotels and banks. By contrast, representatives of ICT (information and communication technology) and auditing companies described their utilisation rates as higher than usual.

Mountain hotels continue to report low utilisation, predominantly due to very low numbers of European guests, in particular from Germany, but also from Russia. Guests from Asia and the US are also showing reticence, owing to a fear of terrorist attacks in Europe on the one hand, and to new visa requirements in the Schengen Area on the other.

DEMAND FOR LABOUR

Staff numbers still slightly too high

Overall, staff numbers tend to be seen as marginally too high. However, the situation differs from one sector to another.

Most representatives of manufacturing firms continue to rate their staff numbers as slightly too high. This applies in particular to precision instrument and machine manufacturers. In construction, headcounts are, to a large extent, considered appropriate. Regarding the services sector, respondents from banks and retailing indicate that headcounts are somewhat too high. In contrast, ICT, fiduciary and auditing companies and specialised asset managers are recruiting more staff.

Some of the companies that introduced longer working hours in reaction to the appreciation of the Swiss franc have since reversed this measure, whereas others have retained it. Given their industry's weakness, a few watchmaking companies are considering the introduction of short-time working.

Overall, respondents find staff recruitment somewhat easier than before. Representatives from several industries ascribe this to a higher number of job seekers from the banking and watchmaking industries. The hitherto frequently cited shortage of engineers has eased, especially in the MEM industries. Numerous companies are receiving a comparatively high number of spontaneous job applications. On average, the quality of such applications is considered better than in the past.

PRICES, MARGINS AND EARNINGS SITUATION

Margin pressure eased slightly

The pressure on margins has eased slightly overall, but margins remain below what is considered as normal levels. Almost half the companies surveyed rated their margins as lower than usual. Measures taken to reduce costs and raise efficiency are proving to be effective. In certain cases, prices can be increased, especially abroad. In the domestic market, it has been possible to reduce some of the discounts granted.

Considerable margin pressure still prevails in manufacturing, where respondents from nearly all industries considered their margins to be lower or even significantly lower than usual. However, a slight improvement against the previous quarter has been recorded in this sector, too.

In the services sector, margins remain under significant pressure in retailing as well as in the hospitality and financial industries. By contrast, margins are considered to be at a normal level in the case of wholesalers, auditors and the ICT industry.

Expectations regarding price developments point to a continuing downward trend for purchase and sale prices. A number of respondents, however, anticipate a further rise in commodity prices.

Certain information relating to the real estate market indicates a slight reduction in prices for residential property in the top market segment and a shift in demand towards cheaper segments. In the case of commercial property, there are ongoing signs that rents are, in some cases, under a lot of pressure. This applies in particular to property in prime locations, where tenants are aiming to renegotiate their contracts.

OUTLOOK

Optimism reiterated

Respondents from all three sectors expect a slight rise in real turnover and margins over the coming months. This optimism is in line with the assessment of the past quarter. Reasons behind it include the current exchange rate conditions, anticipated economic developments abroad and the impact of the measures taken to raise efficiency and innovation. This constellation is expected to lead to further improvement in the margins.

Predictability of business performance is deemed to be comparatively low, which is why the outlook for the near future remains characterised by caution. In the present environment, companies from various industries expect a stabilisation of capacity utilisation overall at the current level. Investment plans for the coming 12 months point to a slight upturn. This trend has now persisted for a few quarters.

As to employment plans, survey respondents in the services sector anticipate a marginal increase, whereas those in manufacturing and construction by and large expect slight staff reductions. Hardly anything has changed in this respect compared to the previous quarter.

Companies' inflation expectations (as measured by the consumer price index) average -0.2% over the short term of 6–12 months (previous quarter: -0.3%). Expectations over the longer-term horizon of 3–5 years are 0.5% (previous quarter: 0.7%).

Concerns expressed by respondents include the Brexit scenario (the UK voting to leave the EU), economic and political instability in certain emerging economies, accelerated structural transformation in Switzerland, increasing regulatory requirements and potentially negative consequences of the implementation of the initiative against mass immigration. While most companies have found a way of coping with the current exchange rate conditions, the situation remains challenging for others, and their representatives have expressed the hope that the Swiss franc does not appreciate again. The current interest rate environment continues to be viewed critically with regard to the long-term outlook for pension funds.

Chronicle of monetary events

The chronicle summarises the most recent monetary events. For events dating further back, please refer to SNB press releases and the *Annual Report* at www.snb.ch.

At its quarterly assessment of 16 June 2016, the SNB maintains its expansionary monetary policy. Interest on sight deposits at the SNB remains at -0.75% and the target range for the three-month Libor is unchanged at between -1.25% and -0.25% . The SNB reaffirms that the Swiss franc is still significantly overvalued and that it will remain active in the foreign exchange market, as necessary. The negative interest rate and the SNB's willingness to intervene in the foreign exchange market are intended to make Swiss franc investments less attractive, thereby easing pressure on the currency.

June 2016

At its quarterly assessment of 17 March 2016, the SNB leaves its target range for the three-month Libor unchanged at between -1.25% and -0.25% and the interest rate on sight deposits with the SNB at -0.75% . The SNB reaffirms that it will remain active in the foreign exchange market, in order to influence exchange rate developments where necessary. In the SNB's view, the Swiss franc is still significantly overvalued. The negative interest rate and the SNB's willingness to intervene in the foreign exchange market serve to ease pressure on the Swiss franc. The SNB's monetary policy thus helps to stabilise price developments and support economic activity.

March 2016

At its quarterly assessment of 10 December 2015, the SNB leaves its target range for the three-month Libor unchanged at between -1.25% and -0.25% and the interest rate on sight deposits with the SNB at -0.75% . The SNB reaffirms that it will remain active in the foreign exchange market in order to influence the exchange rate situation, as necessary. The negative interest rate and the SNB's willingness to intervene in the foreign exchange market are intended to ease pressure on the Swiss franc. The SNB's monetary policy thus helps to stabilise price developments and support economic activity.

December 2015

At its quarterly assessment of 17 September 2015, the SNB leaves its target range for the three-month Libor unchanged at between -1.25% and -0.25% and the interest rate on sight deposits with the SNB at -0.75% . The SNB reaffirms that it will remain active in the foreign exchange market as necessary, in order to take account of the impact of the exchange rate situation on inflation and economic developments. In the SNB's view, the Swiss franc is still significantly overvalued, despite a slight depreciation. The negative interest rates in Switzerland and the SNB's willingness to intervene as required in the foreign exchange market serve to ease the pressure on the franc.

September 2015

At its quarterly assessment of 18 June 2015, the SNB leaves its target range for the three-month Libor unchanged at between -1.25% and -0.25% and the interest rate on sight deposits with the SNB at -0.75% . Negative interest rates in Switzerland help to make holding investments in Swiss francs less attractive. In the view of the SNB, the Swiss franc is significantly overvalued. The SNB reaffirms that it is taking account of the exchange rate situation and its impact on inflation and economic developments. It therefore remains active in the foreign exchange market, as necessary, to influence monetary conditions.

June 2015

On 22 April 2015, the SNB reduces the group of sight deposit account holders that are exempt from negative interest; the only exemptions now are those of the central Federal Administration and the compensation funds for old age and survivors' insurance, disability insurance and the fund for loss of earned income (AHV/AVS; IV/AI; EO/APG).

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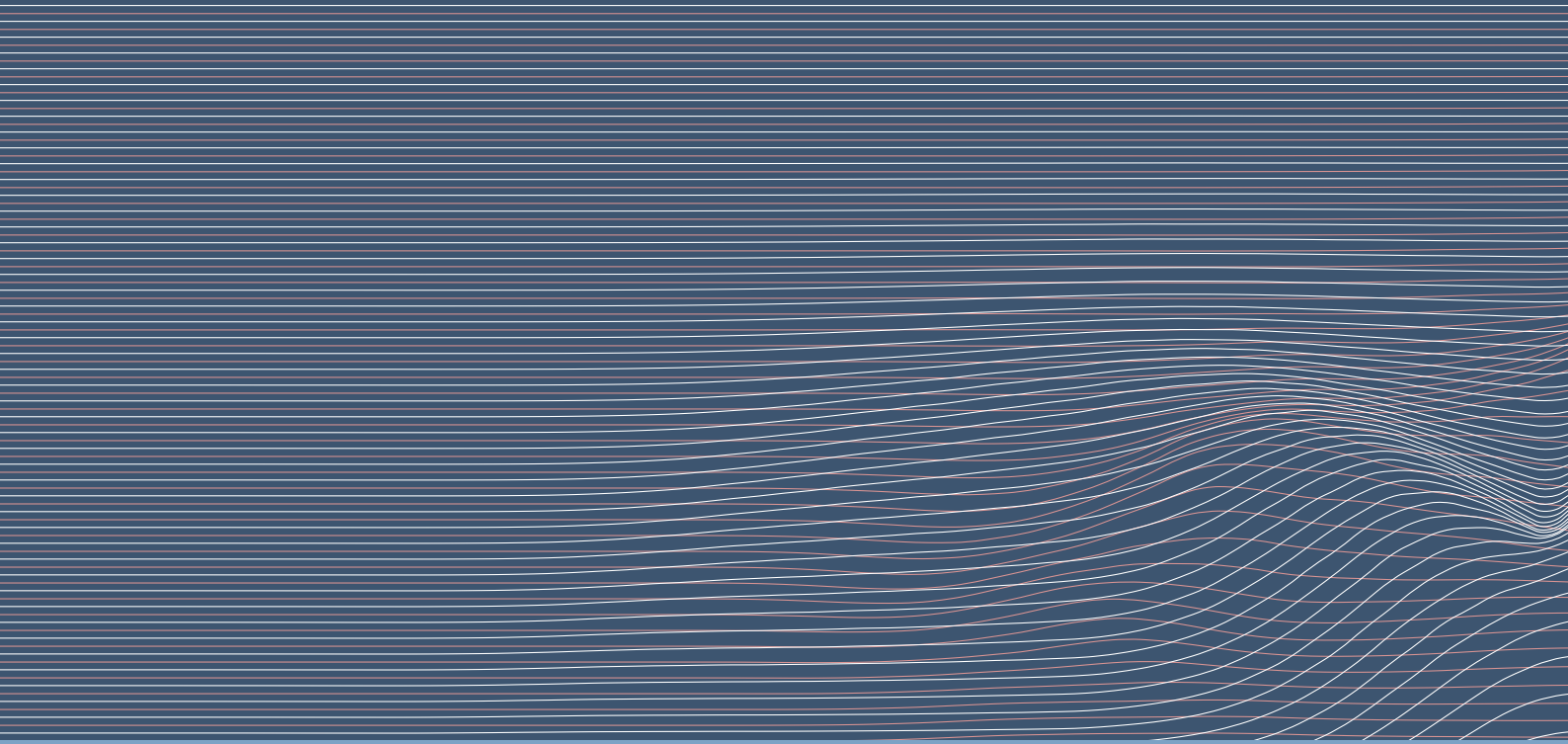
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