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January 14, 1965

Economic Developments in Switzerland,
September-November 1964

17 pages

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Economic Developments in Switzerland, September-November 1964

Summary

In the period under review, the level of economic activity in Switzerland continued to expand, with the overall level of output stimulated by a high rate of construction activity and renewed export demand. 1/ Under the influence of a persistent labor shortage, capital expenditures on machinery and equipment continued strong, but the upward pace of consumer demand slowed over the summer and into the fall months (July-October), probably as the result of the instalment credit restrictions imposed in June and smaller numbers of foreign workers entering Switzerland.

The anti-inflationary measures initiated by the authorities last spring have so far had little visible effect beyond a tightening of financial markets and some reduction in construction plans in response to building controls. Demand pressures continued to push prices slightly upward in this period, while the acute labor shortage--which has been made more severe as a result of tighter restrictions imposed on the inflow of foreign workers--is exerting an increasingly restraining influence on the expansion of output in some sectors of the economy. Imports continued to expand but were outpaced by export growth in the third quarter, as a result of which Switzerland's large trade deficit has shown some tendency to stabilize. But because of restrictions on

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1/ See "Recent Economic Developments in Switzerland, June-August 1964," dated September 10, 1964.

foreign-owned short-term capital, financial markets began to reflect the impact of the large trade deficit: credit conditions remained generally tight, and interest rates in all maturities climbed to new highs.

Since late October, large Zurich banks have been paying as much as 3.75 per cent per annum for 3-month deposits, compared with 3 per cent in August. Rates on 3-8 year certificates of deposit (Kassenobligationen) were increased on the average by 1/4 per cent to a 4.27 per cent level in November, only five months after a similar increase. Finally, larger offerings on the bond market required 5 per cent coupons on some issues--the first 5 per cent coupons on domestic issues in recent times--and drove the yield on outstanding federal government bonds to a peak of 4.10 per cent in early October. However, pressures in the long-term market have eased slightly since then, allowing the yield on government bonds to fall to 4.04 per cent.

A vast inflow of "flight funds" during the November sterling crisis apparently moderated any additional seasonal tightening in the money market in December. During the last three weeks of November, liquidity increased significantly, which suggests that the "flight funds" were largely Swiss-owned, since foreign-owned funds are sterilized either in special accounts at the BNS[1/] or by reinvestment abroad, and are not available to domestic financial markets.

During the November sterling crisis, the BNS intervened extensively in the foreign exchange market in order to keep the Swiss franc from rising above its ceiling of 23.178 cents per U.S. dollar. The Bank's official reserves jumped $137 million in November, and in

1/ Banque Nationale Suisse

order to improve its gold ratio, the Bank obtained $100 million equivalent in gold through a SF/gold swap with the BIS.

Prospects for approval of the government's March 13, 1964 anti-inflationary program by popular referendum, now set for February 28, are uncertain. There is considerable opposition to the program, but the government is still optimistic that it can obtain approval. However, draft legislation is being prepared that will give the BNS greater anti-cyclical powers by authorizing it to (1) impose minimum reserve requirements on the commercial banks, (2) establish credit ceilings, and (3) issue its own securities.

Economy still operating at peak levels

The Swiss economy continued to operate at capacity during the third quarter, although seasonal influences slowed the growth of industrial activity slightly from second quarter levels. The overall level of output, however, was higher than in the third quarter of 1963, owing primarily to burgeoning construction activity and stronger export demand. Over 4,800 new dwelling units were completed in the 65 largest cities in Switzerland in July-September, compared with slightly more than 4,400 in July-September last year. (See Table 1.) In addition, some industrial sectors, such as paper, textiles, and metals--which lagged behind general expansion in 1963--continued to experience a more than seasonal upturn in output, which was reflected by new quarterly peaks in their raw material imports. Demand for investment goods also remained strong as the shortage of labor spurred industry to increase investment in machinery and equipment--especially electrical machinery and equipment--and foster productivity growth. (See Table 2.)

Table 1. Switzerland: Residential Construction in the 65 Largest Cities, quarterly totals, 1962-64 (in number of units)

Quarter	New Dwelling Units Constructed 1962	1963	1964	New Dwelling Units Authorized 1962	1963	1964
I	4,323	4,534	4,424	6,854	5,887	10,440
II	6,929	5,494	5,829	6,997	7,455	5,821
III	5,647	4,427	4,807	6,228	6,705	5,942
IV	6,773	5,714		5,826	6,273	

Source: Banque Nationale Suisse, Bulletin mensuel.

Table 2. Switzerland: Imports of Industrial Raw Materials, Machinery and Equipment (month or monthly average)

	Industrial Raw Materials (000's metric tons)				Machinery & Equipment (millions of francs)		
	Fuels	Chemicals	Paper & Textiles	Metals	Non-Elec.	Elec.	Other
1963	783	89	24	108	137	48	24
I	548	50	19	107	129	44	22
II	918	95	26	105	144	46	24
III	988	132	26	111	138	47	24
IV	679	81	25	110	138	56	28
1964 I	673	59	19	90	142	52	26
II	805	113	23	104	154	53	28
III	758	112	29	120	138	58	26
July	919	147	34	121	163	61	28
Aug.	702	95	25	111	120	55	23
Sept.	653	94	27	129	130	59	27

Source: Banque Nationale Suisse, Bulletin mensuel; Commission de recherches économiques, La Situation Économique.

Table 3. Switzerland: Retail Sales
(Year-to-year percentage increases adjusted for sales days)

Year	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sept	Oct	Nov	Dec
1963	9.4	8.9	12.0	3.6	11.2	7.0	7.2	14.2	6.6	8.3	9.3	8.8
1964	9.0	10.9	16.7	-0.6	15.3	-0.6	5.8	7.1	6.8	14.1	--	--

Source: Département Fédéral de L'économie Publique, La Vie Économique.

On the other hand, there appears to have been some relaxation of consumer demand in the July-October period. The year-to-year increase in retail sales for these four months averaged only 8.5 per cent, compared to an annual increase of 10 per cent in the first half of 1964 and of 9.3 per cent in July-October 1963 (over 1962). This modest slowdown may be due in part to the instalment credit restrictions imposed last June and the reduced inflow of immigrant workers. (See Table 3.)

The pace of new industrial and commercial construction has recently been reduced--directly by the effects of controls on building and indirectly through the decreased availability and higher cost of credit. During the third quarter, 8 per cent fewer industrial building permits were issued than during the same period in 1963, and the number of factories and workshops registered with the federal authorities increased by only 61 compared with 144 in the third quarter of 1963. Permits issued for construction of new residential units were also substantially down from previous levels in the third quarter. This general slowdown in building permits will mean lower overall construction output for the final quarter of this year as well as in the early months of 1965. (See Table 1.)

Finally, the acute labor shortage is beginning to limit output increases in some areas. For example, in the textile industry, which depends on foreign labor for more than half its total factory personnel, new restrictions imposed on November 1 on the employment of foreign labor will act as a further constraint on expanding production.

Although the expected decline in industrial and commercial construction would be in line with the government's anti-cyclical objectives, any slowdown in residential building is not currently welcome in Switzerland because of its socio-political implications. To encourage a continued high rate of housing construction, the Federal Council hopes to have operative by early summer 1965 a Federal aid program that will insure construction of an average of 50,000 new dwellings annually during the next five years. Inasmuch as this projected rate is somewhat higher than the recent pace of residential building, nonresidential construction may have to be reduced further if the building sector is to contribute much to the anti-inflation effort.

Prices continue uptrend; tighter controls on foreign workers

The persistence of demand pressures in the Swiss economy produced slight price advances in the fall. While in the third quarter prices on the average stabilized and even fell slightly at the wholesale level, more recently, higher prices on consumer items, particularly clothing and food, and increased prices for foreign commodities pushed both consumer and wholesale price indexes above their summer levels. (See Table 4.) At the end of October consumer prices were 2 per cent and wholesale prices 1.2 per cent higher than at the beginning of the year.

Conditions in the labor market continued very tight throughout the period under review, although a relative decline in registered job vacancies suggests some let-up in the demand for labor. Registered vacancies rose a bit in August from the July low, but remained considerably below year-earlier levels in the following two months. (See Table 5.)

The August 1964 census of foreign workers subject to government control showed a 4.5 per cent increase over August 1963 in the foreign labor force in Switzerland. Although this was the lowest percentage

Table 4. Switzerland: Price Indices
(August 1939 = 100; month or monthly averages)

		Consumer Price Index	Wholesale Price Index Total	Domestic	Foreign
1963	I	199	230	231	228
	II	201	231	231	231
	III	202	228	227	229
	IV	205	235	234	234
	year	202	231	231	230
1964	I	206	234	232	236
	II	208	236	236	235
	III	208	235	234	236
	July	208	233	233	234
	August	208	235	234	236
	September	209	237	236	237
	October	209	238	237	238

Source: Banque Nationale Suisse, Bulletin mensuel.

Table 5. Switzerland: Unemployment and Job Vacancies, 1962-64
(numbers)

End of Month	Registered Unemployed 1962	1963	1964	Registered Job Vacancies 1962	1963	1964
January	2,022	4,896	1,049	5,563	5,044	6,039
February	882	2,174	303	6,161	5,571	7,134
March	377	454	242	6,474	6,210	6,996
April	249	261	174	6,699	6,288	6,760
May	238	230	129	6,313	6,269	6,411
June	170	185	139	6,342	6,374	6,207
July	177	148	111	6,259	6,545	6,018
August	185	142	130	6,262	6,701	6,133
September	199	171	119	6,085	6,902	6,283
October	324	194	196	5,847	6,739	5,954
November	484	263	--	5,053	5,912	--
December	1,886	778	--	4,741	4,954	--

Source: Banque Nationale Suisse, Bulletin mensuel.

rise since the censuses began in 1959, the increase of 30,888 workers raised the foreign labor component to a record 720,901 and sparked another, though minor, restrictive action. Effective November 1, Swiss firms are allowed to hire new foreign workers only when the total work force of the firm, both foreign and domestic, falls below 95 per cent of the company's March 1, 1964 total work force. The previous cut-off point had been 97 per cent.

The August count showed workers of Italian origin in overwhelming majority, but their overall share was down from previous levels because of added immigration from Spain. (See Table 6.) Of the increase of 30,888 workers, between August 1963 and August 1964, 60 per cent were Spanish (the majority of whom were employed in the construction and hotel industries), 9 per cent were French, and 7 per cent were Italian. The census also disclosed that two-thirds of the 721,000 foreign workers now resident in Switzerland are concentrated in five industries: construction (196,000), metalworking and machinery (138,000), hotel industry (76,000), clothing (45,000) and textiles (36,000).

Financial markets tighten; interest rates rise

In late September conditions in the Swiss money market tightened, ending a two-month period of relative ease, and by mid-November rates on short-term funds had climbed above the earlier high point reached in June. Whereas some large Zurich banks had been able to attract funds at rates as low as 3 per cent in early August, the Zurich three-month deposit rate has been as high as 3.75 per cent since late November. This is attributed primarily to continued restraint on the inflow of foreign money, the

Table 6. Switzerland: Composition of Foreign Labor Force 1/
(August figures in 000's of workers)

Country of Origin	1955 thous.	1955 per cent	1960 thous.	1960 per cent	1963 thous.	1963 per cent	1964 thous.	1964 per cent
Germany	59	21.8	72	16.6	78	11.4	79	10.9
France	8	3.0	12	2.7	21	3.1	24	3.3
Italy	163	59.9	303	69.6	472	68.4	474	65.8
Austria	35	13.1	32	7.3	28	4.0	28	3.8
Spain	--	--	6	1.5	64	9.2	82	11.5
other	6	2.2	10	2.3	27	3.9	34	4.7
Total	271	100	435	100	690	100	721	100

1/ Includes only those foreign workers whose entrance into and residence in the country is under government control.

Source: Département Fédéral de L'économie Publique, La Vie Économique, Vol. XXXVII, No. 10 (October, 1964), p. 453.

Table 7. Switzerland: Selected Financial Indicators

	1964 Jan. 31	April 24	June 26	Aug. 28	Sept. 25	Oct. 30	Dec. 11
Interest rates							
3-month yields:							
Zurich banks a/	2.94	3.37	3.25	3.25	3.38	3.50	c/3.69
Euro-dollars b/	3.44	4.51	3.67	3.60	4.10	4.50	4.39
U.S. Treasury bills b/	2.80	3.75	2.74	2.81	3.43	3.53	3.50
Euro-Swiss francs	3.12	4.12	3.88	3.69	3.56	4.25	4.12
Deposit certificates (3 to 8 years):							
12 cantonal banks	3.88	3.90	4.11	4.15	4.18	4.18	c/4.19
5 large banks	3.85	3.85	4.14	4.14	4.14	4.14	c/4.27
Long-term government bonds	3.56	3.85	4.05	4.08	4.07	4.03	4.04
Stock prices (1958=100)	249.5	238.7	228.5	242.8	238.9	237.5	234.9
Exchange rates							
Spot francs (U.S. cents)	23.164	23.178	23.178	23.145	23.163	23.175	23.176
Forward premium (+) discount (-) on francs d/	+0.68	-0.32	+0.71	+0.65	+0.09	0.00	+0.30

a/ Most frequently quoted rates of the five large Swiss banks in Zurich.
b/ Return in Swiss francs after cost of exbhange cover.
c/ Preliminary.
d/ Per cent per annum.

liquidity-absorbing moves of the BNS in August,[1] higher rates abroad, and early commercial bank preparations for year-end window-dressing. (See Table 7.)

The sterling crisis in late November resulted in a heavy reflow of Swiss funds from London. An increase of SF 224 million[2] in BNS sight obligations to banks, together with a rise of SF 443 million in currency in circulation during the last three weeks of November, are indicative of the sizable additions to domestic liquidity before and during the crisis period. Only Swiss-owned funds were available to help ease conditions in the money market because, under current regulations, foreign-owned funds must be paid into special frozen accounts at the central bank if they are not re-invested abroad within a month. It is not known how much of the recent inflow has been truly Swiss-owned, but it appears that Swiss repatriations were enough to forestall any additional seasonal tightening of short-term funds, as is usual in the first two weeks of December.

Medium-term funds continued scarce throughout the period under review as demand for construction credits remained large. In early September, the slow rate of sales of 3- to 8-year certificates of deposit forced banks to shorten maturity terms as a means of increasing effective yields. And in early November (only five months after their last increase), the large Zurich banks generally raised the rates they pay on certificates of deposit (Kassenobligationen) by 1/4 per cent on the average to a level

1/ See "Recent Economic Developments in Switzerland, June-August 1964," September 10, 1964, page 10.
2/ One Swiss franc = 23.25 U.S. cents.

of 4.27 per cent. (See Table 7.) Finally, 56 local banks recently announced the formation of coöperative organization for the issuance of bonds to supplement their assets. These 56 banks compose about one-third of all local banks in Switzerland.

After limiting domestic offerings on the bond market from mid-June to August, the monetary authorities allowed larger amounts of funds to be raised during September, October and November. Domestic bond issues totalled only $43 million in July and August, but $124 million in September and October and $43.5 million in November. Cantonal and mortgage banks have been the heaviest borrowers, pointing up the continuing need for long-term funds, especially for mortgages among financial institutions. (See Table 8.)

Almost all new issues have been easily absorbed--in fact, some have even been oversubscribed--despite indications at times of definite market strain. This has been particularly true of some electric power issues, which have recently offered a 5 per cent coupon to attract investors--the first 5 per cent coupon on a domestic Swiss issue in recent times.

Table 8. Switzerland: New Capital Market Issues, 1962-64
(month or monthly average, millions U.S. dollars)

	1963			1964					
	II	III	IV	I	II	III	Sept.	Oct.	Nov.2/
Swiss borrowers1/									
Bonds	32.3	36.0	55.5	66.9	37.1	37.3	68.6	46.0	43.5
Stocks	10.0	3.6	12.5	11.9	24.3	5.0	6.2	2.7	--
Total	42.3	39.6	68.0	78.8	61.4	42.3	74.8	48.7	--
Foreign borrowers1/									
Bonds	18.1	4.3	13.9	7.6	10.1	10.0	0	4.8	0
Total1/	60.4	43.9	81.9	86.4	71.5	52.3	74.8	53.5	-
Foreign borrowing as % of total	30.0	9.8	17.0	8.8	14.1	19.1	0	9.0	0

1/ Amounts are gross.
2/ Preliminary figures.
Source: Banque Nationale Suisse, Bulletin mensuel.

Table 9. Switzerland: Industrial Share Index, 1964
(1958 = 100)

1964 High : January 6, 258.1
1964 Low : June 3, 218.6

1963	
September 27	266.4
December 30	253.1
1964	
January 31	249.5
February 28	245.8
March 26	246.2
April 24	238.7
May 29	229.1
June 26	228.5
July 24	248.0
August 28	242.8
September 4	241.2
11	239.3
18	239.7
25	238.9
October 2	240.1
9	233.8
16	231.3
23	233.7
November 6	238.4
13	238.3
20	239.2
27	238.5
December 4	236.4
11	234.9
18	232.8
28	233.4

Source: Swiss Bank Corporation

Yields on outstanding issues have not always reflected the intensity of issue activity; yields steadied through late September, jumped to a high of 4.10 per cent per annum in early October, and have since retreated to 4.04 per cent. Since the real estate boom appears to have topped out and the government will make some funds available to the capital market through debts repayment, no further increases in yields are expected in the immediate future.

However, if the housing promotion program, which officials hope to have operative by early summer, develops as planned, the government will be raising long-term funds on the open market in order to subsidize building directly under the program. SF 320 million will be made available at low rates on dwellings for old people, invalids, and large families; if conditions warrant, SF 600 million will be added to that sum. In addition, federal guarantees will be made available on 40 per cent of the value of second mortgages up to a total of SF 1 billion.

The authorities continue to be very restrictive on new foreign bond issues. Only $5 million of foreign bonds has been allowed in the Swiss market since September 1, and indications are that new money will continue to be raised predominantely for domestic needs. (See Table 8.)

Swiss stock prices generally eased from September through December, although they rose slightly in November. (See Table 9.) This sluggishness in the stock market reflects in part the higher yields obtainable on bonds--currently 4.75 to 5 per cent, compared with an average yield of 2.17 per cent on stocks. It is significant, however, that despite the present inflationary momentum in the Swiss economy and the prospects for further inflation, Swiss stock prices are actually lower than the very high level registered in the second half of 1963.

Increased powers for BNS proposed

Because of the very limited scope for monetary action presently available to the BNS and the tenuous legal status of the current anti-inflationary emergency measures, the government wants the central bank to have permanently expanded powers to deal with business cycle fluctuations. The debate on the anti-inflationary program in the September session of the Federal Assembly disclosed continued unpopularity for some aspects of the program, particularly the restraint on construction and the shortage and higher cost of mortgage credit. In fact, feeling that the anti-inflationary program will be rejected at the February 28 referendum is currently quite widespread.

Under these circumstances, the government has proposed that the BNS be given the power (1) to impose on commercial banks legal minimum reserves and to regulate these reserves as the economy requires, (2) to establish credit ceilings, and (3) to issue securities in its own name. The proposed powers should permit the BNS to exercise a greater degree of control over the economy as a whole. However, strong opposition to expanding BNS powers is building up in the Swiss financial community, which is already quite critical of the "authoritarian" spirit with which the central bank has implemented the emergency measures.

Sterling crisis and tightening money send Swiss franc to ceiling; official reserves build up

Rates in the Swiss foreign exchange markets during the September-December period were determined chiefly by tight money-market conditions, except during periods of weakness in sterling. The spot Swiss franc climbed quickly toward its ceiling of 23.178 cents against the U.S. dollar in

mid-October as the demand for domestic funds strengthened and stayed at the ceiling in late November and mid-December as the BNS was required to take up dollars in the foreign exchange markets because of the weakness in sterling. (See Table 10.)

The usual premium on Swiss francs for 3-month forward delivery has remained relatively narrow since mid-September because higher domestic yields have worked to keep at home funds normally invested abroad.

BNS official holdings of gold and foreign exchange changed little in August and September but rose $145 million from the end of October to mid-December, owing almost entirely to the inflow of "flight funds" during the November crisis in sterling. Foreign exchange holdings rose $137 million in November alone as the BNS intervened in the foreign exchange market in support of the dollar. (See Table 11.)

In order to improve its gold ratio, the BNS acquired $136 million equivalent of gold in early December in a series of swap transactions that concurrently reduced its holdings of dollars. As reported in the BNS weekly statement of December 7, most of the gold was obtained through a Swiss franc/gold swap with the Bank for International Settlements (BIS). The BIS transferred the Swiss franc proceeds to the Federal Reserve under its currency swap arrangements, and the Federal Reserve in turn used them to reduce the BNS's dollar holdings by an equivalent amount.

The weekly report also disclosed BNS participation in the $3 billion aid package granted on November 25 to the Bank of England: the BNS has placed at the Bank's disposal SF 345 million, under a new item called "rate-secured balances with foreign central banks," subject to the terms of its association with the International Monetary Fund's General Arrangements to Borrow.

Table 10. Switzerland: Spot Rates for the Swiss Franc 1/
(U.S. cents per Swiss franc)
Par Value--22.868; Lower Limit--22.472; Upper Limit--23.178 2/
1964

June	5	23.176	September	4	23.141
	12	23.176		11	23.150
	19	23.176		18	23.150
	26	23.178		25	23.163
July	3	23.168	October	2	23.148
	10	23.160		9	23.160
	17	23.130		16	23.175
	24	23.123		23	23.175
	31	23.125		30	23.175
August	7	23.150	November	6	23.175
	14	23.153		13	23.176
	21	23.146		20	23.176
	28	23.145		27	23.175
			December	4	23.178
				11	23.176
				18	23.178

1/ Selling rates in the New York market.
2/ Recent upper limit imposed by the BNS in the Swiss market; however, the Swiss authorities are not committed to hold the rate below 23.283.
Source: Federal Reserve Board.

Table 11. Switzerland: Official Reserves
(end-of-month figures, million U. S. dollars)

	1963	1964							
	Dec.	Mar.	June	July	Aug.	Sept.	Oct.	Nov.	Dec. 15
Gold	2,820	2,543	2,599	2,560	2,530	2,532	2,532	2,532	2,668
Foreign Exchange	254	201	352	350	312	318	308	445	317
Total	3,074	2,744	2,951	2,910	2,842	2,850	2,840	2,977	2,985
Change	+373	-330	+207	-41	-68	+8	-10	+137	+8
Gold Ratio	92	93	88	88	89	89	89	85	89

Source: Banque Nationale Suisse

Foreign trade deficit stabilizes

Switzerland's foreign trade deficit, which reached disturbing proportions in the early months of this year, has recently shown a tendency to stabilize. Owing to improved export performance, the $300 million deficit registered between July and October was no larger than in the same period in 1963. (See Table 12.) Whereas exports decreased between the second and third quarters of 1963, they increased this year at an annual rate of almost 11 per cent. Imports, on the other hand, advanced at a rate of slightly over 7 per cent, as they had the year before. However, this rate of increase was lower than during the first ten months of the year.

Table 12. Switzerland: Foreign Trade
(Seasonally-adjusted monthly average or month, millions U.S. dollars)

	1963				1964						
	I	II	III	IV	I	II	III	July	Aug.	Sept.	Oct.
Imports, c.i.f.	249	273	278	280	296	296	302	296	301	308	303
Exports, f.o.b.	191	204	200	210	212	219	225	219	223	232	233
Deficit	-58	-69	-78	-70	-83	-77	-77	-77	-78	-76	-70

Source: OECD, Main Economic Indicators; Neue Zürcher Zeitung.

Switzerland's trade deficit for the first ten months of this year increased 14 per cent over January-October 1963, reaching a record of $781 million, almost $100 million higher than last year's figure. For the year as a whole the trade deficit is expected to reach $920 million, about $110 million higher than in 1963. The factors chiefly responsible for this year's record deficit are the growth in imports of consumer goods and rising raw material prices. In addition, increased capital expenditures, stimulated by the heightening boom earlier in the year led to sharply increased purchases from abroad of industrial machinery and equipment.