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RFD 456

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

Division of International Finance

REVIEW OF FOREIGN DEVELOPMENTS

December 5, 1963

Recent Economic Developments in Switzerland,
September-November 1963 13 pages

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December 9, 1963.

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Recent Economic Developments in Switzerland, September-November, 1963

Summary

Interest rates increased in all sectors of the financial market during the period under review in face of the continued overheating in Switzerland's economy, less easy credit conditions and higher interest rates in the United States, and tightening credit conditions in several neighboring countries. Money rates (3-month deposit rates) increased from 2.88 per cent at mid-September to 3.25 per cent by mid-October, while yields on Federal Government bonds rose from 3.21 per cent on September 1 to an average of 3.37 per cent on November 1. Commercial banks continued to raise funds through long-term bond issues to meet persistent demands for longer-term advances. The Swiss authorities hope that credit supplies will ease somewhat in 1964 and check further rate advances, but prospective measures to liberalize foreign loans in the country (as a result of the recent Copenhagen Loan) may lead to some additional foreign issues early in the new year.

Although the rate of economic expansion in the Swiss economy has slackened somewhat, the economy is still marked by excess demands, and the spectre of accelerated inflation is now feared. Construction, although off from earlier quarters, still continues to advance as does consumer demand. Consumer prices rose 3 per cent from the fourth quarter of last year to the end of September, while wholesale prices remained stable. Increases which have already taken place in bank and Federal Government salaries, in pension payments, and in rates on all new mortgages and even on some old ones taken by the smaller banks, and possible increases in 1964 in milk prices and rates on old mortgages by the larger banks herald more price and wage pressure.

The labor shortage has gotten so critical on Swiss farms that the government is negotiating for immigrant farm labor from Spain while maintaining restraints against additional foreign labor for other industries.

Switzerland's foreign trade deficit was up 20 per cent over the second quarter of the year. Exports recovered considerably in September and kept the monthly deficit to about $58 million. It is unlikely that the deficit will fall much below this level as the strong demand for imports continues and increasing prices put a competitive squeeze on exports.

International reserves increased over the period under review a net of $99 million as foreign funds flowed into the country before the IMF meeting in September and from Italy during October. The SNB supported the spot dollar during those two months, but since November 1 it has fluctuated narrowly above the intervention point.

Demand pressures reflected in financial markets

The overheating in the Swiss economy, not heretofore evident in the domestic financial market because of an abundance of funds flowing into the country from abroad, was acutely reflected in the financial scene during the September to November period. Although foreign funds flowed into the country rather heavily in September before the annual IMF meeting and from Italy during October, increased demands for Swiss francs and rising interest rates or tightened credit conditions in the United States, and in several neighboring countries pushed up rates throughout all sectors of the market. (See Table 1.)

Table 1.

Switzerland: Selected Financial Indicators for Selected Dates, 1963
(in per cent per annum of index)

	January 25	April 26	July 26	October 25	November 15
Interest rates					
3-month yields:					
Zurich banks[a]	2.69	2.69	2.94	3.25	3.25
Euro-dollars[b]	3.19	3.36	4.10	3.80	3.85
U.S. Treasury bills[b]	2.53	2.53	3.16	3.11	3.25
Deposit certificates (3 to 8 years):					
12 cantonal banks	3.39	3.41	3.44	3.63	3.63
5 large banks	3.39	3.39	3.39	3.64	3.64
Long-term government bonds	3.13	3.06	3.18	3.26	3.35
Stock prices (1958 = 100)	250.0	263.1	255.7	256.4	263.7
Exchange rates					
Spot francs (U.S. cents)	23.13	23.14	23.15	23.17	23.17
Forward premium on franc[c]	+ 0.40	+ 0.36	+ 0.02	+ 0.32	+ 0.27

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

Toward the end of September the money market tightened because of quarter-end liquidity needs; however, liquidation of dollar assets and a return flow of notes tended to ease the money situation. Nonetheless, despite actions of the Swiss authorities to ease the cash positions of the banks through purchases of spot dollars in the exchange market, the 3-month deposit rate in Zurich climbed from 2.88 per cent in mid-September to 3.25 per cent in mid-October, where it has since stabilized. (See Table 1.)

The bond market was under continuous pressure throughout September and October and yields on Federal bonds rose from 3.21 per cent on September 1 to an average of 3.37 per cent at the beginning of November. The "Kraftwerke Linth-Limmern AG" (Electric Power Station) 4 per cent $9.3 million bond issue early in September was the first domestic issue of any importance to be offered at 4 per cent since April. It was successful, but a $10 million 4 per cent loan offered by the Canton of Geneva at the end of October was only 77 per cent subscribed.

Interest in foreign issues have remained high because they continue to carry the 4-1/2 per cent coupon rate that has generally prevailed this year on foreign issues. However, the recently offered Phoenix-Rheinrohr Company (pipeline and metal manufacturers) $11.6 million 4-1/2 per cent loan was issued at 99 per cent to keep it attractive,and it was oversubscribed.

In addition, several Swiss commercial banks have continued a practice started in July to obtain long-term funds by offering long-term obligations for their own account.

Some commentators in Switzerland seem to think that the pressure on interest rates will ease sometime after the new year: they expect the economic boom to contine to level out and for funds to become more available to the

Swiss market. In a recent circular sent by the Swiss National Bank to the country's two principle banking associations in which their requests for increases in interest rates on medium-term bank bonds (Kassenobligationen) were rejected, the Swiss authorities stated that they anticipated additional liquidity in the Swiss markets in the near future. They pointed particularly to the large supply of U. S. dollars they have received since July which they consider to be in part a repatriation of Swiss investments abroad; they consider that these funds may well flow into the capital market in the near future.

Reaction to "Copenhagen Loan" could contribute to continued tightness in financial markets

Official Swiss reaction to the recently very successful "Copenhagen Loan" placed outside the country may work to offset the foreseen easing of the capital market in Switzerland. An international syndicate of bankers headed by Morgan Grenfell of London offered a $14 million loan denominated in Swiss francs for the City of Copenhagen simultaneously in London, Paris, Brussels, and Amsterdam without Swiss participation. The loan, which bore a coupon rate of 5 per cent and was subscribed three times over, created considerable stir in official Swiss banking circles, for it seemed to bear out a fear currently acute to the country: that a move is afoot to elevate the Swiss franc to an international reserve currency, a position they feel it is not able to assume owing to the smallness of the Swiss economy. And furthermore, if this practice of issuing Swiss franc denominated loans outside the country should become more popular, the SNB policy of regulating foreign issues so they just absorb the excess liquidity in the Swiss market would be frustrated.

Swiss concern about this aspect of monetary control, about the loss of commissions, and about the effects of a higher return on Swiss franc securities floated outside the country than prevails inside, have led the authorities to communicate their opposition to such floatations to other monetary authorities. At the same time, they have relaxed somewhat the ground rules under which foreign loans may be floated in Switzerland. The latter action will surely increase foreign issues in Switzerland, which were very small during the third quarter, and could take up any additional liquidity available in Switzerland in the near future, particularly as long as interest rates there are below those in other major financial centers. As a result, this reaction could maintain the pressure on financial markets which the authorities now see diminishing.

Domestic economy remains overheated

Although the very high rate of expansion in the Swiss economy in 1962 and early 1963 has eased somewhat, business continues to be very good. Nearly all segments of public opinion agree, especially as they have watched interest rate and price increases accelerate during the past quarter, that the economy is still overheated. Construction (which might, however, be affected by the higher interest rates) and continued strong consumer demand are the major factors responsible for the present intensity of economic activity.

Building continues to boom but the level of activity has slipped somewhat below the high point of the boom and even below the level of the last few months. The number of new dwellings completed in the 65 principal Swiss towns and cities was down to 4,427 in the third quarter (1963) from 5,647 a year ago and 5,494 in the second quarter 1963. Permits for new construction totaled 6,705 during the third quarter of the current year, up from 6,228 a year ago but down from 7,455 in the previous quarter. Increased interest rates, which go into effect rather promptly on outstanding mortgages in Switzerland, may probably dampen still further the surge of construction.

Consumer demand remained strong as retail sales on a seasonally adjusted monthly average basis rose. Increased payments to the retired and surviving dependents from the National Insurance Program may enter consumption almost entirely and help to put further pressures on retail prices.

Inflationary pressures build up

Most recently, retail prices in Switzerland have been advancing faster than in many other industrial economies. Prices of consumer items, up already 3 per cent this year, rose about 1 per cent during the third quarter. By contrast, domestic wholesale prices are virtually unchanged from a year ago and even decreased during the third quarter from first and second quarter levels. (See Table 2.) However, recent developments may add further inflationary pressures within the country. They include:

a. Bank salaries up 7 per cent (with an additional 2 per cent increase for employees with over eight years service);

b. Federal government salaries up 3.5 per cent (a cost-of-living increase retroactive to the beginning of the year);

c. Milk producers' demands for a higher milk price is pending before a special Federal commission;

d. A 10 per cent rise in chocolate prices announced for January 1;

e. Increases of 33 per cent in maximum rates payable under the Old Age and Surviving Dependents Insurance Program recommended by the Federal Council.

At the same time, the Swiss Bankers' Association has asked the central bank to terminate at the end of the year the Gentlemen's Agreement to discourage

Table 2.

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

	Consumer Price Index	Wholesale Price Index		
		Total	Domestic	Foreign
1961	187	215	213	217
1962	195	222	224	220
I	192	219	219	219
II	194	222	222	221
III	196	223	226	218
IV	197	225	227	222
1963				
I	199	230	231	228
II	201	231	231	231
III	202	228	227	229
April	200	231	231	230
May	201	233	233	232
June	201	230	229	232
July	202	228	227	229
August	202	226	226	226
September	203	230	229	230

Source: Swiss National Bank Monatsbericht.

the inflow of foreign funds, and a member of parliament has called for the release of $348 million the commercial banks have in special blocked accounts with the SNB, Both measures would feed the present boom although they would help relieve pressures on the financial markets. Furthermore, higher mortgage rates may become more widespread during 1964, an increase which would have direct effects on rents and farm cost and would help to set up demands for more wage and price advances.

Labor market remains under strain

The acute labor shortage that has been another major source of inflationary pressure in Switzerland has continued throughout the third quarter and into October, when seasonally it tends to improve.1/ (See Table 3.) At the end of October only 194 persons were completely unemployed and searching for work in contrast to 6,739 registered vacancies. The hotel, metals, and construction industries pulled labor away from the farms even during the planting and harvest seasons of this year, and the farm labor force fell by 12 per cent. Agriculture's manpower needs have induced the government to negotiate with the Spanish government for immigrant labor for next season even though Swiss policy is to limit any further increase in foreign labor.

Table 3. Unemployment and Job Vacancies in Switzerland

End of Month	Number Unemployed	Registered Job Vacancies
1962		
September	199	6,085
October	324	5,847
1963		
August	142	6,701
September	171	6,902
October	194	6,739

Source: U. S. Embassy, Bern.

1/ See "Recent Economic Developments in Switzerland, April to August 1963," dated September 23, 1963.

Foreign trade deficit continues to increase

Preliminary figures for the third quarter show Switzerland's foreign trade deficit (seasonally adjusted monthly average) up approximately $13 million (or 20 per cent) over the second quarter 1963 and up some $9 million above the same quarter last year, in spite of a strong export position. (See Table 4.) Third quarter imports (seasonally adjusted monthly average) held at just below the second quarter level while a $14 million decrease in exports, most of which came during July and August, was almost entirely responsible for the increased trade deficit.

Exports recovered considerably in September, the latest month for which figures are available; they were the highest ever recorded for September, but the strong continuing demand for imports kept the September deficit well above the $50 million mark.

Gold and foreign exchange reserves increase as the Swiss National Bank takes in dollars

During September and October, Switzerland's international reserves registered gains of $51 and $65 million, respectively, as the SNB took in large amounts of dollars in those months. (See Table 5.) The two weeks from September 23 through October 3 alone saw Swiss reserves increased little less than $100 million, attributable to continued "nervousness" on the international financial scene and, in October, to capital inflow from Italy. Dollar-franc swaps between Swiss banks and the SNB to increase bank liquidity in Swiss francs also added to foreign reserves.

The $19 million drop in foreign exchange reserves during the first fortnight of November can be attributed primarily to the conversion of the Swiss francs

Table 4. Swiss Foreign Trade: 1962 - September 1963
(seasonally adjusted, monthly average or month, in millions of U.S. dollars)

		Imports c.i.f.	Exports f.o.b.	Trade balance
1962	I	250	181	-69
	II	244	186	-58
	III	256	186	-70
	IV	251	187	-64
1963	I	247	192	-55
	II	271	205	-66
	III	270	191	-79
	January	240	186	-54
	February	243	194	-49
	March	260	197	-63
	April	273	197	-76
	May	281	208	-73
	June	259	212	-47
	July	291	195	-96
	August	1/ 256	1/ 172	1/ -84
	September	1/ 264	1/ 206	1/ -58

1/ Preliminary figures subject to adjustment.
Source: OECD; U.S. Embassy, Bern.

Table 5. Switzerland: Official Reserves
(end of period figures, in millions of U.S. dollars)

Date		Gold	Foreign Exchange	Total	Change	% of Reserves held in Gold
1962	I	2444	164	2608	-151	94%
	II	2409	297	2705	+ 97	89%
	III	2453	176	2629	- 76	93%
	IV	2667	205	2872	+243	93%
1963	I	2461	177	2638	-234	93%
	II	2530	178	2708	+ 70	93%
	April	2453	179	2632	- 6	--
	May	2453	177	2630	- 2	93%
	June	2530	178	2708	+ 78	93%
	July	2444	180	2624	- 84	93%
	August	2451	198	2649	+ 25	93%
	September	2501	200	2701	+ 51	93%
	October	2520	246	2766	+ 65	91%
	November 15	2522	227	2749	- 17	92%

Source: International Financial Statistics; Swiss National Bank.

paid in by subscribers to the Copenhagen Loan. Since the proceeds of the loan will not be spent in Switzerland, the National Bank of Denmark swapped the $14 million in Swiss francs directly with the SNB for foreign exchange. This alleviated some of the Swiss fears surrounding the loan, especially the fears that if it were to be spent in Switzerland it would abet the current boom or if it were converted through the foreign exchange market it would have disrupting effects.

Dollar remains at intervention point throughout September and October

The U. S. dollar remained at the SNB's support price in five of the first eight weeks of the period under review. (See Table 6.) Strong commercial needs kept it above its lower limit during early September in spite of a vigorous demand for francs caused by continuing tightness in the Swiss money market and by institutional anticipation of end-of-quarter liquidity needs. However, this soon gave way to the almost continual intervention of the SNB as funds flowed heavily into Switzerland prior to the IMF meetings in September and a substantial flow of funds from Italy built up during October using the dollar as a vehicle currency.

Towards the end of October the dollar began to move up from its lower intervention point and throughout November has fluctuated narrowly between 23.171 cents and 23.175 cents to the franc on a rather quiet foreign exchange market that was not even affected by the rising French rediscount rate. At the end of November it was maintaining its position at 23.171 cents to the franc without Swiss intervention.

Table 6. Foreign Exchange Rate for the Spot Swiss Franc 1/
(in U.S. cents per Swiss franc)

Par Value	22.868
Lower Limit	22.472
Upper Limit 2/	23.178

Month		Daily Average	Week Ending		End of Week
1963	January	23.120	September	6	23.171
	February	23.123		13	23.178
	March	23.102		20	23.178
	April	23.099		27	23.176
	May	23.127	October	4	23.178
	June	23.125		11	23.175
	July	23.129		18	23.178
	August	23.164		25	23.178
	September	23.176	November	1	23.171
	October	23.176		8	23.173
	November 3/	23.171		15	23.175
				22	23.171

1/ Noon buying rate.
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.
3/ Based on first 22 days of the month.
Source: Federal Reserve Board.