

Press Release

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KOF Economic Forecast for Spring 2018: Broad-based Upturn

The Swiss economy is currently on an upward trajectory. This year it will achieve a relatively high GDP growth rate of 2.5%, and KOF is forecasting fairly robust growth of 1.8% for 2019. However, some of this increase is attributable to license fees received from sporting events, which have little to do with the actual performance of the Swiss economy. The labour market is doing well, with unemployment falling slightly. Inflation is gradually moving into positive territory.

The international environment

Last year can be described as a successful one for the global economy, even though the pace of this upturn slowed somewhat towards the end of the year. World trade surged by 4.5% in 2017 following a five-year period during which growth had averaged around 2%. The prices of energy and other commodities rose over the course of the year without severely affecting consumer prices. This year the Federal Reserve, the US central bank, is expected to raise interest rates by about the same amount as it did last year. Although the European Central Bank (ECB) will probably reduce the net volume of its bond purchases to zero this year, it is likely to leave interest rates on hold until 2019. KOF expects the strong growth in the global economy to gradually weaken over the forecast period.

The Swiss economy

The Swiss economy is currently performing extremely well. Internationally and domestically focused sectors alike are growing strongly. KOF reckons that the main reasons for this positive trend are the improved economic situation of major trading partners and the depreciation of the Swiss franc against the euro. This latter factor has enabled exporting companies to widen their profit margins. KOF expects growth in gross domestic product (GDP) for the current year to be 2.5%, which would be higher than its last forecast in December 2017. Some of this increase, however, has little to do with the actual performance of the Swiss economy and can be attributed to the fact that Switzerland hosts the headquarters of some of the major international sports federations and associations (IOC, FIFA etc.). A fair chunk of the license fees from large-scale international events such as the Olympic Games in South Korea is included in Switzerland's GDP figures. KOF estimates that this factor accounts for roughly 0.3% of Switzerland's GDP. The absence of such major sporting events next year means that economic growth will come in lower. Adjusted for the impact of sporting events, however, the GDP growth rate forecast for 2019 is not much lower than that for this year.

Given this exceptional effect, it is not entirely surprising that employment growth is fairly modest and that the unemployment rate – as defined by the International Labour Organization (2018: 4.6%) – will fall more slowly than would be expected for this level of GDP growth. Consequently, there is no significant pressure for wage increases, and the impact on labour costs remains moderate. However, the Swiss franc's depreciation against the euro and the slightly higher price of oil are likely to push up inflation to 0.7% this year. Nonetheless, it should remain at this low level and subsequently even weaken slightly. From an inflationary perspective, there is thus no need for a more restrictive monetary policy. Given the current situation, KOF expects the Swiss National Bank to replicate ECB's monetary policy in order to maintain the usual interest-rate differential between franc- and euro-denominated investments.

Capital spending on machinery and equipment will grow robustly this year, as will construction investment. The latter, however, is expected to weaken next year, as rising interest rates are likely to hit construction investment. Swiss exports are expanding and will continue to do so for some time. Demand for imports will also probably remain high over the coming months.

US Policies Fuelling Uncertainty

The fiscal and trade policies being pursued by the US administration under President Trump are creating economic uncertainty. The punitive tariffs already imposed on steel and aluminium imports are unlikely to have any noticeable direct impact on Europe in macroeconomic terms because the United States imports relatively little crude metal from Europe. In the short term, however, any escalation of the trade conflict is likely to hit Europe much harder than America because economic activity in Europe is currently heavily reliant on exports. The recent surge in capital spending could slow if export prospects deteriorate sharply.

A further uncertainty factor is the fairly unpredictable effects of the recently adopted US tax reforms. In the short term these reforms are likely to boost local private consumption and capital spending. This additional demand will also bring short-term benefits for European companies in the form of higher exports (assuming that no further import restrictions are imposed). Because capacity utilisation in the US economy is already high, the boost to the real economy resulting from these tax reforms will probably increasingly decline over the forecast period, while consumer and asset prices will come under growing pressure. This will make it more likely that the Federal Reserve will raise interest rates sooner than previously assumed. Any sudden correction of this monetary stance poses a risk of disruption in international financial and currency markets and, potentially, a highly adverse impact on the global economy.

The US tax reforms will enhance America's ability to attract further foreign direct investment. At the same time, the exemption granted for foreign subsidiaries' profits in the United States means that high-tax countries such as Germany and France will be less attractive for US direct investment than low-tax countries such as Ireland. Over the medium term, therefore, high-tax countries will lose out unless they take on the tax competition initiated by the United States and make fiscal adjustments of their own.

On our website you will find the full KOF Economic Forecast for spring 2018 containing detailed information on all key industries and sectors:

<https://www.kof.ethz.ch/en/news-and-events/media/press-releases.html> →

An Executive Summary of the forecast can also be found on our website:

<https://www.kof.ethz.ch/en/news-and-events/media/press-releases.html> →

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