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Press Release

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KOF Economic Forecast for winter 2020/2021: second wave weighing on the labour market

KOF expects GDP to fall by 3.5 per cent this year (baseline scenario). For 2021 and 2022 it expects to see growth of 3.2 per cent and 2.6 per cent respectively. The second wave of the pandemic is placing a strain on the labour market. Employment is likely to stagnate in the winter half-year, and historically low wage increases are expected for the next two years. The number of companies that believe their survival is at risk has risen again.

The COVID-19 pandemic returned with a vengeance in the autumn. However, the economic impact has so far been less severe than during the first wave. In its baseline scenario, KOF expects gross domestic product (GDP) to decline by 3.5 per cent for 2020 as a whole (previous forecast: decrease of 3.6 per cent). The fact that this decline is fairly mild by international standards is also due to the strong performance of merchanting (trading in commodities and pharmaceutical products, among other things). Without merchanting's contribution to growth, the decline in GDP this year would have been 5 per cent. GDP is then expected to grow by 3.2 per cent in 2021 and by 2.6 per cent in 2022.

The baseline scenario is based on the assumption that the pandemic will abate slightly in the first few months of next year without the need for longer-term, drastic additional measures. Under this scenario, value added will return to its pre-crisis levels at the end of 2021.

However, other outcomes are also possible and, unfortunately, not unlikely. Under the negative scenario, the pandemic could gain further momentum at the beginning of next year, making even more drastic restrictions necessary. The situation would improve much later than assumed in the baseline scenario. Under the negative scenario, KOF expects GDP to fall in the first quarter of 2021 and to recover only gradually during the rest of the year. An increase of only 0.6 per cent would then be expected for 2021 as a whole. Pre-crisis levels would only be reached at the turn of the year 2022/2023, i.e. one year later than under the baseline scenario.

Historically low wage increases expected

The second wave is also weighing on the labour market. This can be seen most clearly in the numbers of advance notifications of short-time working. In November the cantonal job centres approved short-time working for around 626,000 employees. These figures have risen further since late summer. The key question will be to what extent companies will retain those employees who are currently on short-time working. Employment is likely to stagnate during the winter half-year before increasing from the second quarter of 2021. Overall, KOF expects full-time-equivalent employment to grow by 0.4 per cent in 2021. The unemployment rate is not expected to fall until the second half of the year. The International Labour Organization (ILO) reckons that the average rate next year will be a relatively high 5.2 per cent. Switzerland's State Secretariat for Economic Affairs (SECO) expects that the rate should peak in the first quarter of 2021 and amount to 3.3 per cent for the year as a whole.

According to initial estimates by the Swiss Federal Statistical Office, nominal wage growth this year will amount to 1.3 per cent, although these estimates involve great uncertainty owing to the data situation. This is the highest figure in more than ten years. This means that wage growth does not reflect the fallout from the current crisis but, rather, the trends in the run-up to it. KOF expects to see a 1 per cent increase this year and historically low wage rises of 0.3 per cent in each of the next two years according to the Swiss Wage Index (SLI).

One in ten companies fear for their survival

Since May the regularly conducted KOF Business Tendency Surveys have been supplemented by specific questions on the coronavirus crisis. After the situation had calmed down in the summer, more companies indicated in the November survey that the pandemic was affecting customer demand. The number of companies that consider their survival to be at risk has also increased – from 8 per cent in October to 11 per cent in November. Fears of bankruptcy have grown particularly in construction, retail, other services and manufacturing.

The recovery in manufacturing has stalled slightly in the current quarter. The situation should improve in early 2021. However, value added will not return to its pre-crisis levels until 2022. Although the retail sector recovered quickly from the crisis, confidence fell slightly in November. Consumer spending is expected to fall by 4.8 per cent this year. This is partly due to the rising unemployment rate and uncertainty about future household incomes. The savings rate has reached an all-time high of 27 per cent. Private consumption is set to grow by 4 per cent next year.

Investment in equipment is reacting very sensitively
Companies cut back sharply on capital spending on equipment during the first half of the year. KOF expects this investment to decline by 5.4 per cent this year. Next year is likely to see companies taking on both postponed and new projects. However, investment in equipment is reacting particularly sensitively to developments during the course of the pandemic. If the second wave lasts longer than was assumed in the baseline scenario, this will dampen investment activity.

Although the situation in foreign trade improved in the third quarter, it has not yet returned to its pre-crisis levels. Exports by the engineering sector, which is sensitive to economic trends, are recovering especially slowly. Overall, exports should increase by 5.7 per cent in 2021. Services exports will remain in the doldrums: tourism in particular will have to contend with restrictions for some time to come and is unlikely to stage a gradual recovery until spring 2021 at the earliest.

Compared with other countries the crisis has so far had only a minor impact on Switzerland's public finances. Most of the federal government's expenditure to date has gone into unemployment insurance: its additional expenditure this year amounts to around CHF 11 billion, of which CHF 9 billion is for short-time working compensation. Short-time working compensation is likely to be much lower next year, whereas spending on unemployment benefits is set to increase. In addition, revenues from income tax and profit tax will fall sharply in the coming years.

The situation in Europe is deteriorating
From Switzerland's perspective, the global economy is likely to contract in the fourth quarter of 2020, and no rapid improvement is expected in the first quarter of 2021 either. The epidemiological situation has recently deteriorated significantly, particularly in Europe, which is important for Swiss exporters. Despite the vaccination campaigns being launched, restrictions to prevent the pandemic will remain in place in many areas and will continue to have a negative impact on capacity utilisation and productivity. In addition, the fallout from the crisis is likely to be felt for some time to come. Higher unemployment and lower employment levels in many countries could reduce the propensity to consume and invest.

Forecasting risks
The further course of the pandemic will also determine how the economy performs next year. There is a risk that there will be a huge wave of insolvencies in the coming months. As far as Brexit is concerned, KOF expects that there will be a fairly clean separation in formal terms. In practice, however, the transition is likely to be handled pragmatically so that hardly any disruption is to be expected. Nonetheless, this assumption is subject to great uncertainty.

Further information on KOF's economic forecast for winter 2020/2021 is available here:
https://kof.ethz.ch/en/forecasts-and-indicators/forecasts/kof-economic-forecast.html →

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