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News Release

UBS Outlook Switzerland: New risks for the Swiss economy

UBS economists expect the Swiss franc to return to a fair valuation in the next several months after years of overvaluation. The shift will benefit some industries more than others. The future may look bright for the Swiss economy, but global risks still loom. The biggest such risk is protectionism, which open economies like Switzerland will need to take seriously in the long run.

Zurich, 12 July 2018 – UBS economists forecast the Swiss economy will grow 2.4% this year, for two main reasons. First, the economy should benefit from the franc's considerable weakening against the euro in recent quarters. Second, the strong global economy should keep Swiss activity humming in the second half of the year, benefiting exporters and supporting investment in machinery and equipment.

The economists at UBS expect Swiss inflation to reach 0.8% this year and 0.9% in 2019. The volatile political situation in the Middle East will likely keep oil prices high for the next several quarters and, combined with the weaker franc, push up inflation in Switzerland.

After nearly a decade of overvaluation, the economists at UBS expect that the Swiss franc will return to a fair valuation against the euro in the coming quarters. To be sure, international competitiveness varies from industry to industry, so what constitutes as "fair" valuation will vary by sector. What may be considered fair value for the export industry may be too high for certain domestically oriented sectors, particularly if they face increasing international competition. A fair value for the competitive export industry would be much too high for certain segments of the domestic-oriented economy, particularly if they face increasing international competition. Shopping tourism and e-commerce, for example, remain major challenges for retailers.

Protectionism: the new threat

The positive outlook comes with caution against global risks, including an economic slowdown in the Eurozone, trade protectionism in the US, and the fiscal policies of the new Italian government. US President Donald Trump's restrictive trade measures pose a serious long-term threat to the Swiss export sector, which has only just begun to recover from the franc's overvaluation.

The United States is Switzerland's second-largest trading partner after Germany. Since the recent US tariffs have been limited to select industries and regions, their effect on the Swiss economy, where pharmaceuticals make up 54% of total exports to the US, have been marginal thus far. However, any escalation of the trade dispute, especially if it involved import duties on European-made automobiles, could hurt Switzerland's open economy, largely through second-round effects.

More cautious national bank

These risks have prompted the European Central Bank (ECB) to assume a more cautious stance and caused the Swiss franc to notch up small gains against the euro. Given these factors, the Swiss National Bank (SNB) will proceed more cautiously in the quarters ahead and only slowly normalize its monetary policy. UBS economists expect the SNB's first interest-rate hike, from -0.75% to -0.5%, to come no sooner than

September 2019 provided that the ECB starts moving interest rates at that time. The economists at UBS believe the SNB will not likely bring interest rates to positive territory before 2020.

While UBS economists expect European monetary policy to normalize very cautiously, they do anticipate more interest rate hikes from the US Federal Reserve in the second half of the year. The market has already factored these increases into prices, however, so yields on both sides of the Atlantic will probably not rise much.

UBS Swiss economic forecasts

	% change yoy in real terms, adjusted for seasonal and calendar effects					Forecasts UBS	
	Level*	2015	2016	2017	2018F	2019F	
Gross domestic product	668.2	1.2	1.4	1.1	2.4	1.9	
Private consumption	358.9	1.8	1.5	1.2	1.4	1.7	
Government spending	80.1	1.2	1.6	1.0	0.6	0.7	
Capital spending	163.7	2.3	3.0	3.2	3.5	2.0	
Construction	62.1	1.5	0.9	2.0	0.9	0.8	
Equipment	101.7	2.8	4.4	3.8	5.0	2.7	
Exports**	362.1	2.1	6.9	3.0	3.5	3.4	
Imports**	286.8	3.1	4.8	2.2	3.5	3.0	
Inflation		-1.1	-0.4	0.5	0.8	0.9	
Unemployment rate***		3.2	3.3	3.2	2.9	2.7	

*Year 2017 (in CHF bn at current prices) ** excluding non-monetary gold and valuables ***annual average
F: Forecasts UBS

Source: Seco, UBS

In developing the UBS CIO WM economic forecasts, UBS CIO WM economists worked in collaboration with economists employed by UBS Investment Research. Forecasts and estimates are current only as of the date of this publication and may change without notice.

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UBS Switzerland AG

Media contact

Daniel Kalt, Regional CIO Switzerland
Phone +41 44 234 25 60, daniel.kalt@ubs.com

Sibille Duss, UBS Chief Investment Office WM
Phone +41-44 235 69 54, sibille.duss@ubs.com

Alessandro Bee, UBS Chief Investment Office WM
Phone +41 44 234 88 71, alessandro.bee@ubs.com

www.ubs.com