Swiss economy slows sharply

Switzerland's GDP stagnated in the second quarter, with its industry suffering from the global economic slowdown. While inflationary pressures continue to ease, the Swiss economy is likely to remain sluggish over the next few quarters

Swiss industry suffers

Switzerland's GDP stagnated in the second quarter, following growth of 0.9% in the first quarter (adjusted for sporting events). This marked slowdown is primarily due to the downturn in manufacturing (-2.9% over the quarter), with the cyclical sectors suffering from the global economic slowdown. In addition, after years of very strong growth, the chemical-pharmaceutical industry is also contracting. This is weighing on Swiss exports of goods (-1.2% over the quarter).

Meanwhile, the construction sector is being battered by rising interest rates. Investment in construction fell over the quarter (-0.8%), as did investment in capital goods (-3.7%).

Private consumption remained strong (up 0.4% over the quarter), still buoyed by the post-pandemic rebound in the consumption of services, particularly in the hotel and catering sectors. Exports of services have also rebounded.

Headwinds likely to intensify

Ultimately, while the Swiss economy has largely outperformed its European neighbours since the pandemic (Swiss GDP has risen by 5.6% since the end of 2019, compared with 3.1% for the eurozone), it now seems to have been caught up by major headwinds, namely the global economic slowdown and interest rate rises. It is only the strength of the service sector caused by the post-pandemic recovery, and in particular tourism, that has enabled Switzerland to avoid a contraction in GDP in the second quarter.

The Swiss economy is likely to remain sluggish over the next few quarters, with all the leading indicators pointing to a continued slowdown. In particular, the PMI index for the manufacturing sector fell below 50 in December 2022 and has continued to decline since then, now reaching 39.9, its lowest level since 2008. Businesses are less confident and their order books are shrinking, while consumer confidence remains at a very low level.

The Swiss economy is therefore likely to remain close to stagnation over the next few quarters. Ultimately, thanks to the strong start to the year, we are expecting growth to average 0.7% in 2023, compared with 2.7% in 2022. Growth in 2024 should remain weak and below the long-term average, at 0.6% for the year.

Inflationary pressures increasingly subdued

Against this negative backdrop, one more positive factor remains. Inflationary pressures in Switzerland continue to moderate, and the loss of household purchasing power is smaller than elsewhere. In August, consumer price inflation stood at 1.6%, the same level as in July and slightly lower than in June (1.7%). For the past three months, Swiss inflation has therefore remained below 2%, in line with the Swiss National Bank's (SNB's) target.

With wage growth remaining moderate, producer price growth back below 2%, import prices down year-on-year and the economy slowing, a sharp pick-up in inflation over the next few months seems unlikely. By intervening in the foreign exchange market to stabilise the overall effective exchange rate, as it did extensively in 2022, the SNB is able to control external inflationary pressures fairly easily. The only risk lies in rising rents, which in Switzerland are often indexed to the central bank's key rates, and could push inflation up a little in early 2024.

An uncertain central bank meeting

Against this backdrop, the outcome of the SNB's monetary policy meeting scheduled for 21 September remains uncertain. It is not impossible that the SNB decides to make a final rate hike, focusing on the risks to inflation in the medium term and choosing to seize the opportunity as the end of the global rate hike cycle approaches. This would take the key rate to 2%, a total increase of 275 basis points since 2022, compared with 500 points for the Fed and 450 points expected for the ECB over the same period. However, with inflationary pressures moderating and the economy slowing, the likelihood of a further rate hike has clearly diminished.

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