Swiss National Bank makes jumbo rate cut

Once again, the Swiss National Bank decided to surprise the markets with a 50bp rate cut, compared with the expected 25bp cut. The SNB's key rate is now 0.5%, compared with 1% previously

Inflation continues to decline and is approaching 0%

The SNB justified this measure by the fact that inflationary pressures have eased further. While consumer price inflation stood at 1.1% in August, it fell to 0.7% in November, with weaker price growth for both goods and services. Inflation in Switzerland remains within the SNB's defined range for price stability (0 to 2%), but it consistently falls short of forecasts. The SNB's inflation forecasts for 2025 have again had to be revised downwards. The central bank now expects inflation to average 0.3% in 2025, compared with the 0.6% expected at the September meeting. The SNB expects inflation to reach 0.2% in the second quarter of 2025. But given the surprises of recent months, the uncertainty surrounding inflation forecasts is very high. The risk is that the appreciation of the Swiss franc will continue to push inflation down via its impact on import prices and economic activity and that at some point, the inflation figure will move into negative territory. While the SNB has indicated that it is prepared to tolerate inflation temporarily going into negative territory, it does not seem to want this situation to continue for several months. This seems to be the justification for today's decision.

The probability of negative rates in 2025 has increased, but this is still not the base case

Going forward, we expect a major internal debate within the SNB. Since the European Central Bank still has 125bp of rate cuts to come (after today's expected 25bp cut), the SNB could in theory be forced to go negative again after all in order to ease pressure on the Swiss franc. With the SNB's key rate now at 0.5%, it will be difficult to cut rates without going back into negative territory, whereas the ECB, with a rate of 3.25% this morning, has much more room. A series of rate cuts by the ECB that is not followed by the SNB could lead to a further rise in the Swiss franc against the euro. All the more so given that next year's environment will be characterised by trade tensions, which generally tend to push the Swiss franc higher. Added to this is the risk of being labelled as a currency manipulator by the Trump administration, which will probably limit the SNB's willingness to intervene in the foreign exchange market and leave it with few tools to work with other than interest rates.

The question remains whether it is really worthwhile for the SNB to deprive itself of ammunition for possible future negative shocks and to suffer the adverse effects of negative interest rates once again, against a backdrop in which the Swiss economy is likely to see its inflation rate next year remain low, but above zero on average over the year, i.e. within the price stability range, and its GDP growth remain between 1 and 1.5%. We remain sceptical.

In our view, today's decision can be seen as a front-loading of rate cuts rather than a sign that negative rates will soon be back. In contrast to the 2025 forecast, the SNB's inflation forecasts for 2026 and 2027 have been revised slightly upwards. The SNB expects average inflation to be 0.8% in 2026, compared with 0.7% previously forecast. For the first three quarters of 2027, inflation is expected to be 0.7%. These figures seem to indicate that the SNB is not anticipating a prolonged period of deflation in Switzerland and is not overly concerned that the objective of price stability will not be met in the medium term. At this stage, we therefore believe that the SNB could continue to cut rates in 2025 but will avoid moving into negative territory. That said, given today's large rate cut, the probability of a negative rate next year has increased.

Temporary relief for EUR/CHF

EUR/CHF has enjoyed a good bounce on the delivery of a more aggressive 50bp SNB rate cut. The relief should be temporary, however, with the ECB set to 'out-cut' the SNB through 2025.

In a world of lower interest rates, the low-yielding Swiss franc typically outperforms and 2025 should be no exception. Yes, the SNB does actively control the Swiss franc as part of its monetary policy toolkit for a small, open economy, but we suspect the market will question the ability of the SNB to intervene heavily given the advent of a new Trump administration. Remember that heavy FX intervention would tick the third of the three boxes for the US Treasury to name Switzerland a currency manipulator – as it did in 2020. Despite SNB protestations of policy independence when it comes to FX intervention, Switzerland runs a large trade surplus with the US and investors will question whether there is political appetite in Switzerland to irk Washington.

Given the prospect of a winter recession in the eurozone, tariffs and broader geopolitical risks all year, we look for EUR/CHF to grind towards 0.90 in 2025.

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