SNB Review: June 2021

Executive Summary:

- **The SNB kept policy unchanged, with the Sight Deposit Rate and main Policy Rate at -0.75%.**
- **The Bank retained their view that the CHF is "highly valued" but moderated their FX intervention language**
- **Marginal shifts higher for inflation and growth forecasts, but CPI seen below target across the forecast horizon**

Links:

- Monetary Policy Assessment: **https://www.snb.ch/en/mmr/reference/pre_20210617_2/source/pre_20210617_2.en.pdf**

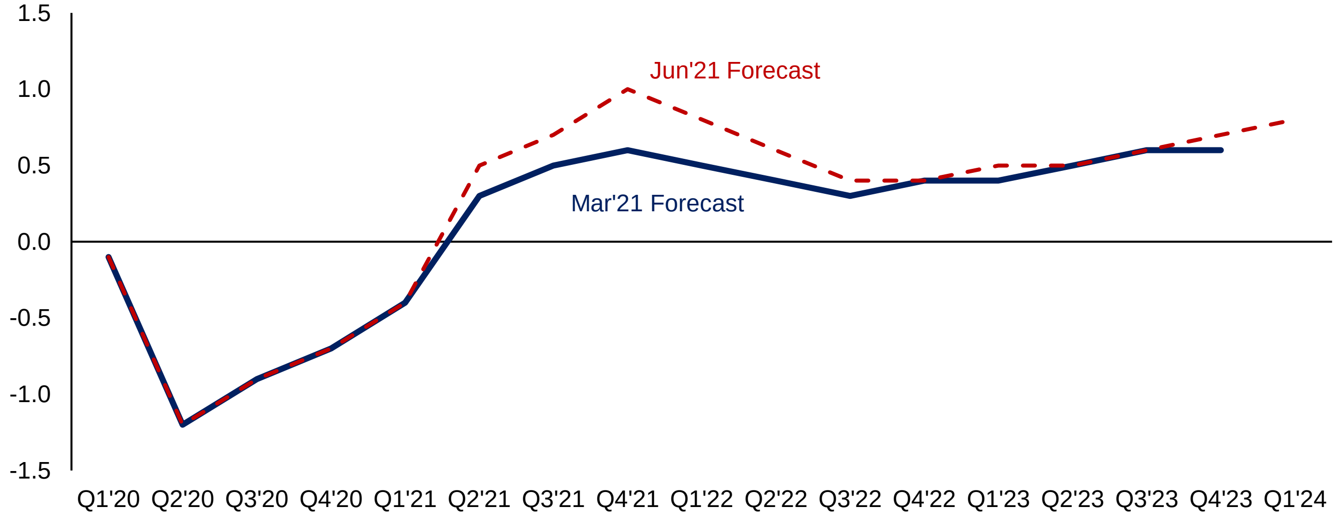
Key Takeaways:

The SNB kept policy unchanged in June, with the board looking to further ensure price stability and add "ongoing support to the Swiss economy in its recovery". They retained their language around the CHF, describing the currency as "highly valued", but declined to re-introduce their previous missive that they would intervene "more strongly" despite the CHF strength seen March's decision.

The SNB joined other global central banks in forecasting near-term upward pressure on inflation, resulting in Y/Y Swiss inflation rising to 1% in Q4, the highest rate since mid-2018. The Bank sees inflation being driven by higher oil prices, strong price rises for tourism-related services and supply bottlenecks as the economy recovers from COVID restrictions. Nonetheless, these price pressures are seen fading from end-2021, with CPI seen below target across the entirety of the forecast horizon.

As such, the SNB are likely comfortable with their current easy policy stance, and that should remain the case for the foreseeable future, even with the assumption of a -0.75% main policy rate. GDP forecasts saw a similar bump higher, with the board now seeing 3.5% growth for 2021, with the GDP level equalling that seen pre-crisis by the mid-point of the year. As such, it appears the Bank's assumptions for low and slow inflation stem from the continued slack in the economy, with the board stating that "production capacity will remain underutilised for some time yet".

Figure 1: SNB bump CPI forecasts higher, but still expected to remain subdued across the forecast horizon



Source: MNI/Swiss National Bank

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In keeping policy unchanged, the SNB continue to signal to markets that they will look through low and slow inflationary conditions and that the bar to further rate cuts is high – despite the Committee stressing that it remains an option. Instead, it seems the SNB will continue to rely on FX intervention to defend against financial market fragmentation and the continued use of the negative rate exemption thresholds to shield the domestic banking sector against the pitfalls of negative interest rate policy.

Dates to Watch

July 1st – June CPI

August 2nd – July CPI

September 2nd – August CPI

September 23rd – Q3 Monetary Policy Decision

Analyst Views (Alphabetic Order):

Goldman Sachs: Continues to expect SNB on hold across the forecast horizon

- The SNB left the policy rate and the interest rate on sight deposits unchanged at -0.75%. The Monetary Policy Assessment left the language around FX interventions unchanged, continuing to highlight that the SNB remains "willing to intervene in the foreign exchange market as necessary," while taking into account the overall exchange rate situation.
- The new conditional inflation forecast was revised upwards in the near term relative to March on the back of higher oil and travel prices, and supply bottlenecks (+0.2pp to 0.4% in 2021, +0.2pp to 0.6% in 2022, +0.1pp to 0.6% in 2023). The SNB also upgraded the growth outlook and now expects Swiss GDP to expand by 3.5% this year, compared with 2.5%-3% at the time of the March meeting.
- Looking ahead, GS continue to expect the SNB to remain on hold over our forecast horizon, with the timing of lift-off in line with the ECB's lift-off in 2025 to avoid appreciation pressure on the Franc.

UBS: SNB maintains accommodative policy stance, lifts macro forecasts

- As expected, the SNB left its policy rate unchanged at -0.75% and maintained the language in its statement that it "remains willing to intervene in the foreign exchange market as necessary" and that the "Swiss franc remains highly valued".
- The main change was an upgrade to its macro projections which was slightly larger than UBS had expected. The GDP growth projection for 2021 was lifted to "around 3.5%" (close to their own forecast of 3.4%) from "2.5%-3%" in the March meeting.
- The inflation forecast was lifted to 0.4% for 2021 (up 20bp), and 0.6% for both 2022/23 (up 20bp and 10bp, respectively); this compares to our forecast of 0.4% and 0.3% for 2021/22. While the increased SNB projection reflected primarily energy base effects, the SNB also noted that the upgrade incorporated the impact of higher prices of tourism-related services (due to the opening of the economy) as well as some pass-through of higher input prices from supply bottlenecks.
- The peak in the inflation rate is seen at 1% in Q4 2021 (matching their own forecast) before falling back to 0.4% by Q4 2022 with an end-point for the projection of 0.8% in Q1 2024, well within the SNB's target range of "below 2%".
- Commenting on the inflation outlook in the press conference, Chairman Jordan noted that the SNB expected the pressure on prices from supply bottlenecks and pent-up consumer spending to continue over the coming months but then to abate "in a few quarters' time". He also pointed out that Swiss inflation remained low by international comparison.
- In contrast to some other countries, longer-term inflation expectations had not risen in Switzerland and remained at 1% in surveys. Looking ahead, he said that any tightening of the policy stance would only be considered if inflation over a 2-3 year horizon moved above the 0-2% target range (and this would be reflected in the SNB inflation forecasts which is conditional on unchanged SNB policy).
- More pointedly, he remarked that the SNB was "far away from having any inflationary problem". The highly valued Swiss franc, a large output gap (which he argued may only be closed in around a year's time despite

GDP reaching its pre-Covid level this year) and well anchored inflation expectations were keeping inflation down.

- According to Jordan, this situation could change going forward in a scenario where the Swiss franc were to depreciate in a context of rising interest rates abroad. Baseline outlook is for no policy rate change until at least end-2022 Overall, the macro outlook and statement suggest that the accommodative policy will be maintained for the foreseeable future, and UBS project the policy rate to remain at -0.75% until at least end-2022 (the end of our projection horizon).
- They think the SNB will aim to at least maintain the policy rate differential to the ECB, which argues in favour of hiking rates only after the ECB has done so (and perhaps with some delay on the part of the SNB). They do not foresee rate hikes by the ECB over our current projection horizon, but an earlier-than-assumed ECB rate hike (perhaps linked to a much more durable increase in inflation) would also bring forward expectations for SNB tightening.
- Conversely, if there were a need for an easier SNB policy stance, perhaps as a result of further franc appreciation dampening the inflation outlook, UBS think the SNB would scale up foreign exchange interventions before considering any rate cuts.

MNI Policy

MNI STATE OF PLAY: SNB Ups Outlook, Inflation Still Seen Low

The Swiss National Bank revised growth and consumer price forecasts slightly higher on Thursday, but said the rate of price increases would remain well below target over its forecast horizon, and reaffirmed its willingness to intervene in currency markets to counter any upward pressure on the "highly valued" Swiss franc.

Supply bottlenecks, plus higher prices for oil products and tourism-related services, pushed the 2021 inflation forecast to 0.4%, with 0.6% predicted in both 2022 and 2023, compared with the 0.2%, 0.4% and 0.6% forecast in March.

Short-term inflation expectations are now rising globally, with upward pressure on prices likely to continue over coming months, but such effects are likely to abate within a few quarters' time, Chairman Thomas Jordan said.

The franc, which has been trading around its strongest level in four months at about 1.09 to the euro, remains "highly valued," said the SNB, which kept the policy rate on sight deposits unchanged at -0.75% and "remains willing to intervene in the foreign exchange market as necessary, while taking the overall currency situation into consideration."

--FRANC DAMPENS INFLATION

The SNB dropped its commitment to intervene "more strongly" in FX markets in March.

"The SNB's expansionary monetary policy provides favourable financing conditions, contributes to an appropriate supply of credit and liquidity to the economy, and counters upward pressure on the Swiss franc," it said in Thursday's monetary policy assessment.

While any return to policy normalisation at a global level would be positive for Switzerland, Swiss inflation would need to run above the SNB's price stability target of less than 2% for two to three years before a significant adjustment in policy were justified, Jordan said.

The franc was one of the key factors keeping inflation down, he said, alongside the output gap, incomplete capacity utilisation, and well-anchored inflation expectations.

The fact that inflation expectations have risen in some countries "primarily reflects a return to normal," he added, "given that long-term inflation expectations had fallen significantly in many countries."

The SNB now anticipates GDP growth of around 3.5% for 2021, compared with the 2.5-3% expected in March, with "risks on the upside and downside alike." The after-effects of the pandemic are set to weigh on both demand and production capacity for "some time yet."

GDP fell again in the first quarter of 2021 in many countries, and remains significantly below pre-crisis levels, Jordan said. At the same time, Switzerland and others have made progress in their vaccination efforts, and Swiss GDP is expected to return to its pre-crisis level by the middle of the year.

The SNB's baseline scenario is that major advanced economies will ease containment measures further through to the summer, resulting in "strong" growth in both Q2 and Q3 2021 and signs of labour market improvement.