

Thomas Jordan: Price stability thanks to forward-looking monetary policy

Speech by Mr Thomas Jordan, Chairman of the Governing Board of the Swiss National Bank, at the 116th Ordinary General Meeting of Shareholders of the Swiss National Bank, Berne, 26 April 2024.

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Madam President of the Bank Council

Dear Shareholders

Dear Guests

I am delighted to see you here today at the SNB's General Meeting of Shareholders. A warm welcome to you all. This is already my thirteenth General Meeting as Chairman of the Governing Board, and also my last. It is therefore a particular honour and pleasure for me to be able to speak to you again here one more time.

'The spectre of inflation is back' – this was the sort of headline that was commonplace in the media from mid-2021 onwards, both in Switzerland and abroad. After years when it had been exceptionally low, inflation suddenly returned with all its might across the world as the coronavirus pandemic subsided. All at once it became clear that inflation was not simply a relic of a bygone era. Instead it is much more a phenomenon that can abruptly resurface and become an issue that preoccupies – and above all weighs on – the population.

The recent episode of inflation demonstrated once again how important price stability is. Inflation curbs the growth of an economy and reduces the prosperity of all. However, inflation imposes the greatest burden on the people in our society that are most vulnerable economically, since they are hardest hit by a loss of purchasing power. It is therefore not surprising that the inflation that emerged following the pandemic attracted so much public attention. This was particularly the case abroad. In some countries, inflation was in the double digits. In Switzerland, it was always significantly lower, and since mid-2023 it has been back in the range consistent with price stability. Nevertheless, inflation was an issue for people here, too.

I would like to set out for you today what the SNB has done in recent years to fulfil its mandate, namely to ensure price stability while taking due account of the economy. I will concentrate on the years since the outbreak of the pandemic. Over this period, price stability was threatened in a number of different ways. In all of these situations, our monetary policy strategy served us well. There are two important points worth noting in this context. First, we do not target a specific inflation rate, but rather regard price stability as having been achieved if inflation is between 0% and 2%. Second, when it comes to ensuring price stability we always look to the medium term. With this flexible approach, and using the appropriate measures, we have been able to safeguard price stability well in very different phases. I would like to explain how we did so.

Downward pressure on prices

The years before the pandemic were characterised by low inflation. The interest rates of many central banks were either at zero or negative. Ensuring price stability in Switzerland in this environment called for an expansionary monetary policy. We used negative interest, and were willing to intervene in the foreign exchange market if necessary.

The outbreak of the pandemic triggered a serious downturn in the global economy, and the Swiss franc as a safe haven once more came under strong appreciation pressure. In Switzerland, too, the economy experienced its strongest decline in decades. Inflation fell clearly into negative territory, and the risk of deflation was acute. To fulfil our mandate in this exceptional situation, negative interest and foreign exchange market interventions were more necessary than ever. We bought foreign currency on a large scale to curb the appreciation of the Swiss franc and so to counter the threat of deflation. Negative interest also allowed us to maintain favourable financing conditions. This supported the economy, while at the same time helping to stabilise prices. Thanks also to this monetary policy, the economic downturn in Switzerland was ultimately less pronounced than in many other countries.

Abrupt turnaround

Towards the end of the pandemic, a considerable economic recovery took hold worldwide. As the economy picked up, inflation also rose strongly across the globe. Given the pent-up demand among companies and households, goods were much more sought after. At the same time, the supply of goods had been reduced during the pandemic owing to the various containment measures. It took some time before the disrupted supply chains were restored and production gathered momentum again. Hence in 2021, strong demand met reduced goods supply, leading to a sharp rise in inflation. At the beginning of 2022, the war in Ukraine brought another sudden change in the monetary policy environment. Already elevated energy prices shot up, giving additional impetus to inflation.

The scale and pace of monetary policy responses to the pronounced rise in inflation differed across the various currency areas. The SNB tightened its monetary policy early by international comparison. We did so not only via the SNB policy rate but also by means of the exchange rate.

In the initial phase of fighting inflation, when it had already risen markedly in other countries but still remained moderate in Switzerland, we tightened our monetary policy via the exchange rate. Already in the second half of 2021, we deliberately allowed the Swiss franc to appreciate by being restrained in our purchases of foreign currency. After the first quarter of 2022, we ultimately stopped buying foreign currency altogether.

In mid-2022 we then raised the SNB policy rate. At that time, inflation here in Switzerland stood at around 3%. In many countries, the first rate hikes were only made when inflation was already above 8%. We subsequently raised our policy rate in several steps, reaching 1.75% in June 2023. This corresponds to a tightening of 2.5 percentage points in total in the space of just one year. The rate rises countered the inflationary pressure via their effect on overall demand.

In the second half of 2022, we started to sell foreign currency. This resulted in a further appreciation of the Swiss franc. Through to spring 2023, the appreciation of the Swiss franc approximately corresponded to the inflation differential between Switzerland and other countries. The real exchange rate, which is crucial for the competitiveness of the economy, thus remained remarkably stable despite the turbulent times. The Swiss franc thereafter appreciated in real terms as well. This contributed to an additional tightening in monetary conditions. All in all, with the appreciation of the Swiss franc since 2021, we were able to shield Switzerland to a significant extent from the rapid rise in inflation worldwide.

Act rather than delay

With the forward-looking tightening of monetary policy, both via the exchange rate and the SNB policy rate, we were also able to limit second-round effects, i.e. price increases in response to higher costs. Elevated second-round effects can create a self-perpetuating development of inflation, tackling which can be a protracted exercise. Or, to be quite blunt: Without early monetary policy tightening, the SNB policy rate would have had to have been raised much more strongly at a later stage, with potentially negative consequences for the economy and the labour market. In this scenario, rent inflation would also have been temporarily stronger as a result of the higher reference interest rate, which would have significantly delayed the decline in inflation.

So where do we stand today? We have not raised the SNB policy rate further since mid-2023, and last December we decided to no longer focus on foreign currency sales. In March this year, we were ultimately able to lower the SNB policy rate by a quarter of a percentage point to 1.5%. This decision takes into account the significantly reduced inflationary pressure as well as the appreciation of the Swiss franc in real terms over the past year. At the same time, the rate cut also supports economic activity.

The easing of our monetary policy in March this year was made possible because the fight against inflation over the past two and a half years has been successful. Inflation has now been back below 2% for some months, and according to our most recent forecast is also likely to remain within the range consistent with price stability over the next few years. Of course, there is no guarantee that this will be the case. In the current environment uncertainty remains elevated, and new shocks can occur at any time. We will therefore monitor the ongoing development of inflation closely and adjust our monetary policy again if necessary.

Closing remarks

The past few years have been shaped by extraordinarily high uncertainty. How have we dealt with this? As a central bank, we are used to uncertainty. We always have to think in terms of scenarios, and weigh up different courses of action against each other. When making decisions, we adopt a risk management approach. In doing so, it is better to make monetary policy decisions that deliver satisfactory results for a broad range of scenarios, rather than those that would be ideal for one specific scenario but would have very poor results in many others.

Ladies and gentlemen, in recent years the SNB has succeeded in performing its mandate despite exceptionally adverse circumstances.

In addition to a decisive focus on pursuing our mandate, successful monetary policy also calls for foresight and flexibility when it comes to implementation. Our monetary policy strategy has allowed us to respond flexibly to the various sets of circumstances we have faced in recent years. Our definition of price stability and medium-term horizon enable us to guide monetary policy with a steady hand, without having to react to every time inflation deviates from a target. This reduced, for example, the need for extreme monetary policy measures during the pandemic, since we are also able to accept inflation forecasts close to the lower end of the price stability range. On the other hand, our strategy allows us to take swift and early action if we see a risk of inflation leaving the range consistent with price stability for a protracted period. This was the case in the second half of 2021, and we therefore took quick and decisive measures to address the rising inflationary pressure.

The focus on our mandate and our monetary policy strategy have proven their worth in a wide variety of situations. But they alone are no guarantee of a successful monetary policy. We must always critically examine our own assessments, identify changes in conditions as early as possible, and analyse their impact. In my view, the SNB is well equipped to continue ensuring price stability in Switzerland in the future, and so – to return to the headlines I mentioned at the start of my speech – to protect citizens from future spectres of inflation. The SNB will remain committed to doing its utmost to safeguard price stability in Switzerland, in the interests of the country as a whole.

Thank you for your attention.

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