PREVIEW: SNB Policy Announcement due Thursday, 21st September 2023

- Pricing has shifted in favour of a hike following the ECB's September meeting and the latest Reuters poll points to a 25bp move
- Further tightening is justified by a number of factors which could result in a resurgence of inflationary pressures over the medium term.
- However, an unchanged announcement is merited by current inflation and growth data.
- The policy announcement is at 08:30BST and commentary from Chairman Jordan begins from 09:00BST onwards.

Overview: The SNB is expected to hike by 25bp to 2.00%, according to 30/37 respondents in a poll conducted by Reuters, and with the remainder looking for an unchanged verdict. Market pricing currently ascribes around a 65% probability to a hike, but it is worth caveating that pricing was in favour of an unchanged outcome before the September ECB. Current inflation and growth data err in favour of those expecting the SNB to leave rates unchanged. However, factors which could result in a resurgence of inflationary pressures as the SNB forecast in June are present and expected to impact in the months ahead, which the Bank believes will push headline YY CPI back above the 0.0-2.0% target from Q1-2024. September's rate decision aside, the SNB may not provide explicit guidance that the policy rate is at the current cycle peak in order to preserve CHF appreciation and given potential inflationary factors ahead. Finally, the SNB has continued to be very active in the FX space as evidenced via available reserve data, and while an alteration to currency language is possible it is on balance unlikely at this gathering given the above inflation-related factors.

Previous Meeting: In June, the SNB hiked by 25bp to 1.75% in-line with the majority of expectations, but disappointing some calls for 50bp. The statement said that medium-term inflationary pressures had increased once again, and as such additional hikes could not be ruled out. Furthermore, while the SNB trimmed its Q3- & Q4-2023 inflation projections it lifted forecasts for 2024 and 2025 as a whole to above the 0.0-2.0% target band, at 2.2% and 2.1% respectively. On the higher forecasts, which were based on the new 1.75% policy rate, the SNB wrote "The reasons for this are ongoing second-round effects, higher electricity prices and rents, and more persistent inflationary pressure from abroad.". In terms of growth, the statement pointed to an expectation for modest upside for the remainder of the year. On FX, the SNB once again made clear that it is willing to be active in the FX market as necessary, adding that in the current environment the focus is on the sale of foreign currency.

Inflation: Headline YY CPI printed at 1.6% in both July and August, in line with and slightly above market expectations respectively; but, crucially, below the SNB's Q3-2023 forecast of 1.70%. Additionally, the core reading moderated to 1.7% in July and further to 1.5% in August YY. Within the August release, FSO highlighted that the MM upside was due to several factors including increased pricing for fuel and heating oil. However, the August data came with the caveat that it is not yet possible to assess the scale and speed of the reference interest rate for tenancies increase which occurred in June, the influence of which will not be visible until November's inflation release. As a reminder, the Federal Housing Office approved the first increase to the reference rate for housing to 1.50% (prev. 1.25%), which allows for an effective rental increase of 3.0%, which the SNB itself has acknowledged could "temporarily result in higher overall inflation". Rents aside, expectations for further inflation upside may stem from the upcoming VAT increase to 8.1% (current 7.7%) effective January 2024, ongoing labour negotiations for next year and broader energy price pressures which were cited in the August release and have been seen more explicitly in the EZ and US readings.

Overall, the SNB will welcome the recent inflation readings which spurred market pricing towards an unchanged announcement. However, a hike cannot be dismissed given uncertainty over the medium-term trajectory based on the above factors which may well serve as justification for a hike to 2.00%. Additionally, market pricing has been pushed back to being just in favour of a hike following the ECB's September move. Irrespective of whether a hike occurs or not, the SNB may not provide explicit guidance that the policy rate is at the current cycle peak in order to preserve CHF appreciation and given the prospect of looming inflationary factors, which should be assessable to some degree before the December gathering.

Growth: Q2 GDP saw a slightly larger than expected slowdown in economic activity to 0.00% QQ (prev. 0.3%), while the YY figure moderated to growth of 0.5% (prev. 0.6%). Elsewhere, the unemployment rate remains around the 2.0% mark, while the latest KOF indicator slipped slightly to 91.1 (prev. 92.2) with the August Manufacturing PMI continuing to languish well in contractionary territory and print sub-40.0. In sum, the Swiss economy has performed slightly softer than expected in recent months, but is still faring markedly better than some of its peers. From a policy perspective, the data adds conviction to those looking for an unchanged outcome; as it would allow the SNB time to assess the domestic situation before potentially taking action in December, if inflationary pressures re-emerge as outlined above.

CHF: Since the June meeting, the SNB's level of sight deposits has seen a marked fall from CHF 496.6bln at domestic banks to CHF 463.6bln, as of 18th September data. While sight deposit action of this type is generally CHF-negative, it has been offset by a substantial fall of near CHF 40bln equivalent in the overall FX reserves level, which are primarily held in USDs and EURs at the SNB. Currently, EUR/CHF resides around 0.9550 which is slightly above the post-June 0.9514 trough, but still markedly lower than the 0.9810 open price from the June meeting. Appreciation which, engineered or not, will undoubtedly be welcome by those at the SNB in light of the role FX plays in combating inflation. Given the supporting role that FX action has possibly played in the easing of July/August inflation data, the September statement will likely continue to place emphasis on a willingness to be active in the FX market. While an alteration of the language on this is possible, it is not likely to arise unless officials are convinced that inflation will remain sub-2.0% over the medium-term.