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CURRENT PROBLEMS OF THE SWISS ECOMONY

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Talk given to the Swiss Mercantile Society

by Benedikt von Tscharner, Counsellor (Economic and Labour), Swiss Embassy, London,

on 9th October, 1974

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Some months ago we read in the newspapers that Switzerland – by some quirk of monetary statistics – had just become the wealthiest country in the world, the country with the highest income per head. Why, then, should we talk at all about problems? Can't we just sit back and be proud, be satisfied . . . and complacent?

Indeed, there are problems, perhaps not of the magnitude of those besetting countries torn by never-ending industrial strife, or, even worse, of those against which some African and Asian nations have to fight with little hope of ever succeeding and an almost certain prospect of losing more and more ground against the prosperous frontrunners, amongst which Switzerland will undoubtedly be found.

So let's be precise: in trying to analyse problems I do not want to create the impression that Switzerland is struggling against poverty, economic crisis and social disorder. What I do mean to say, however, is that looking very critically indeed at our economic performance is in itself something we constantly need to do, and the more incisively we do it, the better we shall be armed to cope with our problems. Knowing our weaknesses is one of the prerequisites of continuing success.

In trying to understand the Swiss economy and the reasons for our prosperity one shouldn't be afraid to recognise that Switzerland is not originally a rich country. It has no natural resources such as oil or minerals, its soil is poor, its climate rigorous. The lack of access to the sea and the rugged mountains make the transport of goods expensive.

So it is often said that the one thing which is responsible for Switzerland's prosperity is the sheer hard work of its people, their inventiveness, their sense of quality, their determination to sell to the remotest corners of the world's markets.

With due respect for the large measure of truth which is contained in this often-heard, very flattering, assertion, we cannot overlook the fact that in the last 25 years a number of additional factors have favoured the expansion of the Swiss economy. These factors explain why hard work and all the other estimable qualities have been able to produce such a result. And in trying to define those factors we shall also have to ask ourselves whether they still work in our favour today. I shall not be able to deal with all of them at length, but I shall try to give you a reasonably full list as I see it.

One of the factors which have contributed most to the growth of our economy has been the plentiful and relatively cheap foreign labour, which for years gave rapid returns on new investment at little cost to the community in social infrastructure. We all know that this source of wealth is no longer flowing. I shall deal with this problem in a moment.

A second very helpful factor was the cheapness of raw materials and energy. Cheap oil has, of course, favoured all industrialised countries. But it has made it particularly easy for countries like Switzerland to stay in the top league and import all raw materials and energy. These times are now past and it has again become a fact of life that natural resources contribute very much indeed to a country's wealth.

Switzerland was also able in the past to profit from a very low rate of inflation by any standards. There are many and complex reasons for this. But we have to recognise that in the last few years we have suddenly dashed forward and placed ourselves amongst the countries with the higher rates of inflation. At present we are running at something between 10 and 12 per cent. There can be no doubt that we have lost a very important advantage. I shall elaborate on this point later.

Another traditional asset seems to be gone for good, namely the stability of the Swiss currency. In January 1973 the Swiss franc had to be set free and it has floated rather dramatically, mostly up but occasionally downwards as well. This new situation is bound to make it more difficult for our industry to compete on world markets, although, for the time being, exports are still doing surprisingly well.

I don't want to make the list too long, but I must mention the very sharp upward trend in taxation. For a long time Switzerland was known as a tax haven. Today we have almost given up this advantage and welcome, but expensive, improvements in social security, not to speak of other costly new programmes such as the protection of the environment, will rapidly put us in the same league as other European welfare states.

So we still have our basic capital of our hands and heads. Do we really? Haven't we become somewhat lazy, somewhat spoiled by success, somewhat reluctant to do the less prestigious jobs? I leave the answer to you. But I would like to add another question: Have we kept up with competitors in our capacity to innovate, are we investing enough in research, are our schools still the best, are our universities equipped to provide us with the intellectual power to master tomorrow's problems?

What is somewhat frightening with all these developments is the fact that the swing-back has set in at almost the same time in many fields I mentioned. Nevertheless, it is extremely difficult to see how seriously our competitive capacity is jeopardised. While it is in my view certain that all these changes are of economic significance, it might just be that other countries are in as adverse a situation or even worse off, which would again give Switzerland a certain comparative advantage. But this is a dangerous kind of consolation. The trick might work if the recession brought about by the world energy crisis turns out to be short and mild. If it deepens into a real crisis, Switzerland might be doubly

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penalised because of its very great dependence on exports, on returns from capital investment abroad, from tourism, from banking and insurance. We have prospered in an expanding world economy and we have no large home market to fall back upon now that this world-wide expansion shows signs of exhausting itself.

Record dependence on imported oil

Let us now look more closely at a few of the problems I have mentioned.

Energy is my first point. This might seem awfully topical, but then energy is indeed one of those things which make the economy tick. So by talking about energy we really are looking at the heart of the matter.

Switzerland is, together with Japan, one of the countries with the highest dependence on foreign sources of energy. The figures are very interesting: 80 per cent of our energy requirements are met by oil and all oil has to be imported either in the form of crude or in the form of refined petroleum products. The latter predominate, since we have only two refineries and their capacity is comparatively small. Electricity covers 16 per cent of our needs, and at the moment this can virtually all still be produced in our own hydro-electric power stations and in the three existing nuclear plants. Coal has gone down to 2 per cent, and the remaining 2 per cent are accounted for by natural gas. These two sources of energy also have to be imported, which pushes our dependence on foreign sources of energy up to 83 per cent.

May I remind you that Britain has to import only about half of its energy and, as you know, thanks to North Sea oil, this proportion is bound to fall in a few years.

Now, this very high dependence of Switzerland on foreign sources of energy has a number of consequences. But before trying to assess some of them, let me point out that this situation cannot be changed quickly. Practically all sites which are suitable for the construction of hydro-electric stations have been exploited. The main new source is, of course, nuclear energy, which will not only increase the supply of electricity but also provide heat for industrial and private needs and thus replace heating fuel. Work has now finally started on the construction of three new plants. Popular opposition to new stations caused long delays and has still only lost a little of its force. Important contracts for the import of natural gas have also been concluded, and finally the search for oil and gas on Swiss soil is now being more actively pursued than in the past. Yet, with rising consumption, all this has hardly succeeded in reducing substantially the proportion of imported oil in our total energy balance.

Of course, the two major problems with oil are supply and price, the latter almost certainly being the more serious one. The higher price of oil, be it 8, 10 or $15 per barrel, will cause profound changes in the entire economic life of a country.

The major part of the oil we import is used for heating houses, in fact 79 per cent of our energy is turned into heat and oil-heating has almost totally replaced all other methods. This development probably should and could have been prevented, but it also shows where savings will have to be achieved.

Luckily, in many respects, Swiss industry is somewhat less energy-hungry than the industry of most other industrialised countries. Of course, you do find industries such as aluminium-smelters or cement factories. But proportionally we have less of that kind than others. Also, oil is not used in very large quantities as a raw material in the manufacture of such things as plastics, synthetic fibres or fertilisers. Furthermore, we have no car industry, a sector which has become rather vulnerable under the new circumstances.

But what is not produced in the country has to be imported and paid for. In addition, slower growth abroad will also influence the development of exports of Swiss products. The economies of the industrialised countries have become so interdependent that the increases in the prices of oil and also of other essential raw materials such as copper, wool and foodstuffs, will mean slower growth in Switzerland as well. The additional cost of dearer oil for our economy will be something like 2.5 to 3 thousand million Swiss francs, roughly what we earn on balance from tourism. But the compound cost might, of course, be much higher if the present crisis means a loss of export opportunities and a self-sustaining rate of inflation of South American proportions.

The whipping-boys of inflation

Inflation was probably the major problem of our economy even before the oil crisis started, and the outlook has become much more discouraging since then. Of the 12 per cent increase in the cost of living we had last year, probably one-third only was due to higher oil prices, and the major impact did not, of course, come before 1974.

As we all know, inflation is not a problem with which only Switzerland has to cope. Yet inflation is not created in the same way in all countries and the methods of fighting it are very dissimilar. In Switzerland the whipping-boys have traditionally been the building trade and the banks. The construction boom was held responsible for inflated demand for credit, materials, land and manpower. The very high liquidity of the banks, on the other hand, was held responsible for an inflated money supply and therefore credit restrictions were deemed to be the best way to slow down demand. One of the reasons for the high liquidity of our banks was the attraction Switzerland – for various good reasons, but certainly not interest rates – has always had for foreign capital.

Now, with the floating of the franc and the abolition of the American restrictions on capital outflow, the situation has changed quite radically and we are now much more eager to retain capital in Switzerland or even attract it rather than to keep it away. Also, with the persisting labour shortage and general slow-down of business, construction has become a much less powerful inflationary force. Still, the urgent measures adopted in December 1972 were approved by the people one year later. This result at least points to the fact that there is widespread popular support for an effective anti-inflationary policy.

In the past twelve months the major source of inflation has been the tremendous increases in the price of our imports, not just of oil but of almost all commodities including, of course, food. We have to realise that Switzerland is importing more foodstuffs per head than any other country, including Britain. And we are very near the top of the list when it comes to comparing imports with the gross national product. Last year the balance of trade closed with a deficit of 6,665 million Swiss francs and in the first half of this year it has already reached the sum of 4,367 million. It now seems hardly possible to maintain the traditional surplus in our current balance of payments. Yet, with monetary reserves standing at well over 20,000 million Swiss francs, we – unlike Britain – should be able to finance most of that deficit from our own reserves and without having recourse to recirculated oil money. It seems that the Swiss franc does not react to these changes as one might expect it to do on the basis of monetary theory. So the Swiss franc may well remain overvalued for quite some time, which can help to limit the effects of imported inflation.

Experts say that lately inflation has again become rather more home-grown, reflecting among other things the continuing boom in the export industry and increased budgetary deficits at all levels of government. But, whatever the source, we are still — just — in the two-figure league and our highly cartelised home market will not react quickly to a weakening in demand.

Foreign labour, a political problem

The problem of *foreign workers* remains one of Switzerland's main worries. It is primarily a political problem, since there are still three initiatives on the table which, if they were successful, would lead to a drastic reduction in foreign labour. But it is also an economic headache, since the stabilisation measures which the government had to take to strike a balance between the militant anti-foreigners and a manpower-hungry economy are putting a very strong brake on further expansion.

So far the government has succeeded fairly well in sticking to the "magic figure" of 603,000 foreign workers with either a yearly or a permanent permit. However, the very strict limitation of yearly permits has led to a sharp increase over the last few years in seasonal workers and also in frontier workers.

This has caused the Federal Council to introduce a quota system even for these two categories. Furthermore, categories of workers which have hitherto been exempt, like hospital or farm workers, are now subject to restrictions too. The system should, therefore, now be almost totally watertight and it seems quite certain that we shall have to live with this policy — which is in many ways unpleasant — for quite a number of years, even if on the 20th October the Swiss voters reject, as I am confident they will, the utterly irresponsible initiative of the National Action movement.

What is the outlook for our economy?

We most certainly have to learn to live with very little real growth, with continuing inflation, dear food, high interest rates, chilly houses, a continuing shortage of manual labour. On the other hand, we may have a better chance to find a flat in Switzerland, to find a hotel room or a qualified white-collar employee. We are on the way to higher taxes, more government involvement in the economy but also better social security and fewer road accidents etc. I could go on, but I don't know whether these educated guesses about tendencies can really answer the question of how our country will fare in the future.

In spite of the many unpleasant things that have to be said when analysing our present and future problems, I believe we can remain basically confident that we shall not only cope with them but also get on somewhat better than a number of other countries. In declaring this strong faith in our capacity to manage the difficulties, I am deliberately taking the risk of being accused of chauvinism. Yet when we see how many European governments have got into trouble these last few months as a consequence of the worsening of the economic situation, I feel that the Swiss people have so far kept a cool head, they have not blamed their government for the unpleasant statistics but have tried to find out what they personally could do to adapt. To me, this seems to be the key to an answer: being prepared to change old habits in investment, production, marketing, labour relations and so on, cutting down on waste of all kinds, trying to find new ways of staying competitive, accepting structural changes and, as always, working a little harder still. I sincerely hope this attitude will prevail, even if things get worse, because I am convinced that this is the right answer.

WELFARE OFFICE
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(Nearest Underground Station:
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