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SNB faces a difficult interest rate decision

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The Swiss National Bank will likely cut its key interest rate to zero on June 19. We recommend gradually investing excess cash holdings into dividend-rich equities.

The Swiss National Bank's (SNB) board, which was restructured last year, must consider a variety of factors this week when deciding whether and how far to cut the key interest rate. First and foremost is the inflation outlook. Inflation in Switzerland slipped into negative territory in April for the first time since 2021. In other words, on average, prices for a typical basket of goods and services are falling. Lower energy prices, transportation costs, and, for example, cheaper used cars have now more than offset those product groups that still show slight price increases. As a result, inflation in Switzerland has fallen below the SNB's price stability target range of 0 to 2 percent, clearly calling for a further rate cut, in our view.

Added to this is the delicate economic situation. Although newly published GDP figures for the first quarter showed a surprisingly strong increase in real value creation of around 2 percent compared to the same quarter last year, this was likely somewhat exaggerated by special effects. There are indications that many Swiss companies exported an unusually high volume of goods to the US in the first quarter to get ahead of impending US import tariffs. Due to the resulting uncertainty, foreign trade is likely to weaken significantly from the second quarter onward, and economic growth for the rest of the year is expected to be subdued.

The SNB leadership will also closely monitor developments in the foreign exchange market. They are likely to react more sensitively to further surges in the franc's value against the euro than against the US dollar. For one, the euro is already trading at an undervalued level against the franc, while the US dollar, even at around 0.82 francs, is still considered slightly overvalued. Furthermore, most Swiss SMEs are more exposed to the European single currency than to the greenback.

All in all, there is much to suggest that the SNB will cut the key rate by another 25 basis points to zero. Some market participants now even see a fairly high probability of a 50-basis-point cut to -0.25 percent. However, the SNB must carefully weigh how much of its limited “ammunition” for further rate cuts it wants to use up now. Should the franc unexpectedly appreciate sharply, it will have to think twice about whether and to what extent to counter franc strength with its alternative tool—massive foreign exchange interventions. Given ongoing negotiations with the US to avoid high tariffs, it would probably be unwise to risk accusations of currency manipulation.

Regardless of the decision, for Swiss investors, this means they are unlikely to earn positive returns on their cash holdings or on Swiss franc bonds for some time. We therefore continue to recommend gradually investing excess cash into well-diversified, income-generating portfolios.

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Non-traditional asset classes are alternative investments that include hedge funds, private equity, real estate, and managed futures (collectively, alternative investments). Interests of alternative investment funds are sold only to qualified investors, and only by means of offering documents that include information about the risks, performance and expenses of alternative investment funds, and which clients are urged to read carefully before subscribing and retain. An investment in an alternative investment fund is speculative and involves significant risks. Specifically, these investments (1) are not mutual funds and are not subject to the same regulatory requirements as mutual funds; (2) may have performance that is volatile, and investors may lose all or a substantial amount of their investment; (3) may engage in leverage and other speculative investment practices that may increase the risk of investment loss; (4) are long-term, illiquid investments, there is generally no secondary market for the interests of a fund, and none is expected to develop; (5) interests of alternative investment funds typically will be illiquid and subject to restrictions on transfer; (6) may not be required to provide periodic pricing or valuation information to investors; (7) generally involve complex tax strategies and there may be delays in distributing tax information to investors; (8) are subject to high fees, including management fees and other fees and expenses, all of which will reduce profits.

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