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2021 ARTICLE IV CONSULTATION—PRESS RELEASE; STAFF REPORT; STAFF STATEMENT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR SWITZERLAND

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2021 Article IV consultation with Switzerland, the following documents have been released and are included in this package:

- A **Press Release** summarizing the views of the Executive Board as expressed during its June 11, 2021 consideration of the staff report that concluded the Article IV consultation with Switzerland.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on June 11, 2021, following discussions that ended on April 7, 2021, with the officials of Switzerland on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on May 25, 2021.
- An **Informational Annex** prepared by the IMF staff.
- A **Staff Statement** updating information on recent developments.
- A **Statement by the Executive Director** for Switzerland.

The documents listed below have been or will be separately released.

Selected Issues

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

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PRESS RELEASE

PR21/186

IMF Executive Board Concludes 2021 Article IV Consultation with Switzerland

FOR IMMEDIATE RELEASE

Washington, DC – June 21, 2021: On June 11, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation[1] with Switzerland.

Switzerland has navigated the pandemic well. COVID-19 has had major social and economic impacts, but an early, strong, and sustained health and economic policy response helped contain the contraction of activity. Also playing important roles were strong pre-pandemic fiscal, financial sector, and household buffers, robust exports (pharmaceuticals, chemicals, gold), low dependency on contact-facing sectors, a capable health system, and targeted containment. Coordinated efforts aimed at households and firms stemmed a loss of purchasing power and a rise of unemployment and bankruptcies.

Prior to the pandemic, Switzerland enjoyed robust growth and buffers. Growth was underpinned by employment gains from immigration and cross-border workers. Exports continue to be well-diversified among high value-added goods and services. Banks were well-capitalized and liquid, although credit growth was modest, and concentrated on mortgages. Public finances were strong, anchored by the debt-brake rule, federal budget surpluses, and low and declining public debt. Faced with low or negative inflation, the Swiss National Bank maintained a highly-negative policy interest rate; sustained current account surpluses, appreciation pressures, and periodic, safe-haven inflows contributed to accumulation of substantial foreign exchange reserves.

Recovery has commenced, but risks and uncertainty are high, dominated by the pandemic. The rebound should deepen, as vaccination proceeds, containment is eased, and domestic and global demand picks up. Growth is projected at 3.5 percent in 2021 and 2.8 percent in 2022. Fiscal support has been extended, and monetary policy remains accommodative. Risks stem from lagged COVID-19 impacts, search-for-yield behavior, real estate market imbalances, and an uneven global recovery. Post-pandemic challenges include limiting scarring—especially among vulnerable groups and workers, sustaining competitiveness, tackling pension system gaps, and addressing climate change.

[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board.

Executive Board Assessment[2]

Directors commended the authorities for the strong, timely, and multi-pronged policy response to the COVID-19 pandemic. Noting the still high uncertainty, Directors stressed the need to maintain supportive policies until the recovery is on a firm path. They underscored the importance of rebalancing the policy mix and fostering green, digital, and inclusive growth.

Given Switzerland's ample fiscal space, Directors welcomed the extension of targeted fiscal support to 2021 and the authorities' readiness to deploy additional support, if needed. They recommended operational refinements to the fiscal rule to avoid headwinds to the recovery, and in this regard, welcomed the authorities' consideration of a longer period to offset extraordinary expenditures. Directors noted that expeditious reforms of the withholding tax and stamp duty would help ease tax and administrative burdens and improve capital market functioning. They encouraged increased spending in support of green, digital investment and emission reduction plans.

Directors agreed that monetary policy should remain accommodative, with clear communication to help anchor inflation expectations, and mindful of potential risks to financial stability. They encouraged the authorities to review the monetary policy framework and tools regularly and adapt them to new challenges as needed. Directors took note of the external assessment, recognizing its complexity, given COVID-19 related uncertainties and data revisions. They concurred that foreign exchange interventions should be limited to mitigating excessive appreciation and deflationary pressures, provided trend appreciation is allowed.

Directors welcomed the resilience of the banking sector. They highlighted the need to monitor asset quality and risks closely, particularly those related to residential and commercial real estate. Directors recommended that the authorities review and expand the macroprudential toolkit to enhance its ability to react swiftly to financial stability risks. They looked forward to further progress in implementing the 2019 FSAP recommendations.

Directors agreed that structural reforms should focus on supporting post-COVID transformation and addressing important long-standing issues. In particular, they encouraged continued efforts to promote flexibility and mobility in the labor market, and ambitious reforms of the pension system to better align it with demographic and economic trends. Directors also called for decisive actions to achieve Switzerland's climate change targets. Finally, some Directors noted the recent cessation in discussions on an institutional agreement with the European Union and encouraged the parties to engage constructively to avoid negative impacts over time.

[2] At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: http://www.IMF.org/external/np/sec/misc/qualifiers.htm.

Switzerland: Selected Economic Indicators, 2019–22

Population (2020): 8.55 million
Quota (current; millions SDRs / % of total): 5,771.1 / 1.21%
Key export markets: Euro area (44%), US (18%)

	2019	2020	2021 Proj.	2022 Proj.
Output				
Real GDP growth (%)	1.1	-3.0	3.5	2.8
Unemployment				
Unemployment (%)	2.3	3.1	3.5	3.4
Prices				
Inflation (period average, %)	0.4	-0.7	0.1	0.3
General government finances				
Revenue (% GDP)	32.9	33.6	33.2	33.0
Expenditure (% GDP)	31.5	36.2	36.6	33.7
Fiscal balance (% GDP)	1.4	-2.6	-3.4	-0.7
Public debt (% GDP)	39.8	42.9	45.3	44.5
Monetary and credit				
Broad money (% change)	0.8	6.5	…	…
Credit to the private sector (% change)	4.2	2.4	…	…
3-month Treasury bill interest rate (%)	-0.8	-0.8	…	…
Balance of payments				
Current account (% GDP)	6.7	3.8	6.7	7.5
Net FDI (% GDP)	4.8	8.5	3.6	5.7
Reserves (end-of-period, billions of US dollars)	854.8	1083.6	…	…
External debt (% GDP)	264.4	284.9	…	…
Exchange rates				
REER (% change)	1.1	3.8	…	…

Sources: IMF's Information Notice System; Swiss Institute for Business Cycle Research; Swiss National Bank; and IMF staff estimates.

INTERNATIONAL MONETARY FUND

SWITZERLAND

STAFF REPORT FOR THE 2021 ARTICLE IV CONSULTATION

May 25, 2021

KEY ISSUES

Context. Switzerland has navigated the COVID-19 pandemic well. The pandemic has had major social and economic impacts, but an early, strong, and sustained health and economic policy response helped contain the contraction of activity. Coordinated efforts targeting households and firms stemmed a loss of purchasing power and a rise of unemployment and bankruptcies. Recovery has commenced, but uncertainty and risks remain high, dominated by pandemic dynamics. The rebound should deepen, as vaccination proceeds, containment is eased, and domestic and global demand picks up. Fiscal support has been rightly extended in 2021, and monetary policy remains accommodative. Policies should remain supportive until there are clear signs of sustained recovery; the authorities should expand support if needed. Redirection to fostering green, digital transformation with attention to low-income earners will be needed, including to ensure that prolonged emergency support does not hinder structural changes in the economy.

Key recommendations. Discussions focused on fiscal, monetary, and financial sector frameworks and long-term challenges (labor markets, pensions, climate), including:

- Avoiding early withdrawal of fiscal support, with adjustments under the fiscal framework (longer offset for COVID-19 spending, limiting spending underruns).
- Keeping fiscal policy accommodative until there are signs of sustained recovery, with expanded support if needed.
- Enhancing, where possible, fiscal support for green-digital growth building on existing programs and plans and with attention to low-income earners.
- Keeping monetary policy accommodative, in light of uncertainties and risks of an extended period of very low or negative inflation.
- Continual review of the monetary framework and tools post-COVID-19 to consider whether adjusting targets and instruments would help respond to new challenges.
- Close monitoring of financial sector risks (COVID-19 losses, search for yield, leveraged exposures, residential/commercial real estate), with new measures as needed.
- Protective labor policies in the near term to limit scarring and inequality, with increased focus on mobility and flexibility, in light of ongoing structural changes.
- More decisive pension reforms (retirement age, conversion rates, pension fund arrangements) to head off emerging financial gaps.
- Putting in place of a clear, monitorable action plan to support the ambitious new long-term climate strategy.

Approved By
Philip Gerson (EUR) and Martin Kaufman (SPR)

Discussions took place (virtually) during March 17–April 7, 2021. The staff team comprised Mark Horton (chief), Karina Garcia, Svitlana Maslova, and Li Zeng and was assisted at headquarters by Rachelle Vega and Ben Park (all EUR). Zhongxia Zhang (EUR) joined the mission for discussions on the financial sector. Albi Tola and Caroline Wehrle (OED) joined the mission. Staff met with Federal Councilor Maurer, Swiss National Bank Chairman Jordan, FINMA CEO Branson, officials from various federal departments, central bank, FINMA and cantonal governments; representatives from think tanks and corporate sector. A press conference was held at the end of the mission.

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CONTEXT: STRONG PRE-CRISIS BUFFERS

1. **Prior to the COVID-19 pandemic, Switzerland enjoyed robust growth and buffers**. Growth was faster than in other advanced economies (AEs), underpinned by employment gains (immigration, cross-border). Exports continue to be diversified among high value-added goods and services, with increasing importance of chemical and pharmaceuticals. Strong private and public buffers were maintained, with banks well-capitalized and liquid. Credit growth was modest, however, and concentrated on mortgages. Anchored by the debt-brake rule, the federal budget ran surpluses, contributing to lower public debt. Faced with low or negative inflation, the Swiss National Bank (SNB) maintained a highly-negative policy interest rate. Sustained current account surpluses contributed to appreciation of the franc (CHF), and periodic, safe-haven inflows led to accumulation of substantial foreign exchange (FX) reserves.

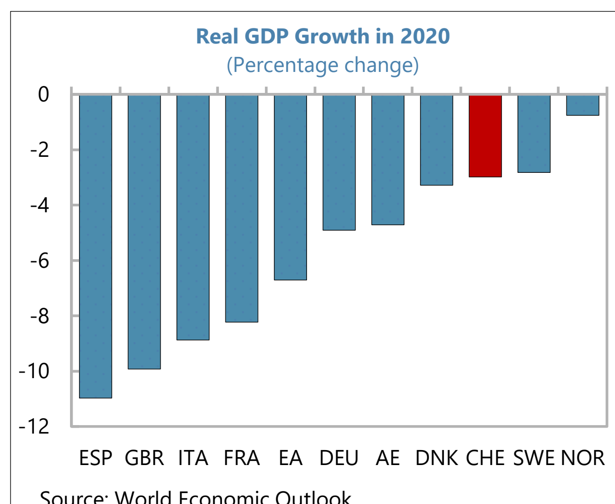
2. **Implementation of past IMF policy advice has been good** (Annex I). The authorities advanced several important reforms, notably of corporate taxation, tax transparency, and climate policy. The SNB increased the frequency of publication of data on its FX interventions (FXIs). Progress on other IMF recommendations, including from the 2019 Financial Sector Assessment Program (FSAP) has been more limited (Annex II).

3. **While COVID-19 has dominated the agenda, other developments are ongoing**. Finalizing an institutional agreement with the EU has been held up, including by a 2020 referendum to limit cross-border movement of EU nationals for work and study (rejected). Remaining issues involve protection of wages, state aid, and the EUR citizens directive (including access by EU citizens to Swiss social benefits, citizenship, movement). Lack of agreement would lead to progressive non-renewal of arrangements that have given Switzerland favorable EU single market access. On June 13, referenda will take place on the COVID-19 Law, the legal basis for pandemic response measures, and the CO_2 Law (and, by extension, the new climate strategy). Federal parliament elections will be in 2023.

RECENT DEVELOPMENTS: COVID-19 IMPACT AND RESPONSE

4. **COVID-19 hit Switzerland early and in waves**. After early clusters of infections and a nationwide lockdown from mid-March 2020, the economy gradually reopened from late-April to June. However, new infections surged after summer, and containment measures were restored. Cautious reopening is continuing, balancing health risks and economic costs. Vaccination started in January 2021, but has been affected by supply constraints and administrative challenges. As of late-April, 20 percent had received at least one shot, with 10 percent fully vaccinated and higher coverage among the elderly and other vulnerable groups. The aim is to make vaccines available to all adults by end-July. Lockdown fatigue has grown, with pressure and demonstrations for faster reopening.

5. The Swiss economy was hit hard in H1:2020, but is recovering. Activity contracted sharply in the first and second quarters, but rebounded strongly with reopening in Q3. Despite new containment measures, activity remained stable in Q4. For 2020 as a whole, the economy contracted by 3 percent, less than other AEs, reflecting strong fiscal, financial sector, and household buffers, exports that held up well (pharmaceuticals, chemicals, gold), relatively-low dependency on contact-intensive sectors, a well-resourced health system, and targeted containment measures (e.g., no widespread manufacturing closure). High-frequency indicators suggest that a slowdown in Q1:2021 will likely be mild, given continued adaptation to containment and support.



6. A timely, strong, and multi-pronged response has supported the economy. The authorities quickly passed comprehensive measures to limit the pandemic fallout, including:

- A fiscal package exceeding 10 percent of GDP. Key actions targeted affected firms and households, especially the short-time work program (STWP), which compensated for lost earnings. STWP coverage was adjusted to cover contractuals and apprentices and raised to 100 percent for low-wage workers. Other important measures included income-loss compensation for self-employed and a large federal loan-guarantee program (Box 1).

- SNB support for liquidity and credit. The SNB raised its exemption threshold for application of negative interest rates on sight deposits easing pressures on bank profits, established a COVID-19 refinancing facility (CRF) for the federal- and cantonal-guaranteed loans, and ensured U.S. dollar liquidity via a swap line with the U.S. Federal Reserve. It also kept the policy rate at -0.75 percent, and in March–May 2020 bought very substantial FX linked to safe-haven pressures.

- Support to banks via temporary steps, including exclusion of SNB reserves from leverage-ratio calculations and deactivation of a sectoral countercyclical capital buffer (CCyB) targeted at mortgages.

The response provided critical support to households and firms, kept credit flowing, and stemmed the rise of unemployment and bankruptcies.

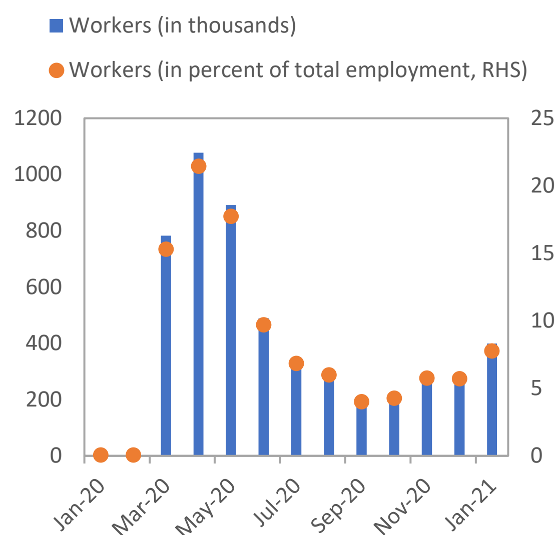
7. The authorities' response was adjusted as conditions evolved. The SNB announced that it will discontinue longer USD repo auctions due to limited demand, and almost all of the macroprudential measures were reversed. Fiscal support was fine-tuned, and in some cases, extended, given the take-up of measures and pandemic impacts. Loan guarantees ended in July 2020, but support for self-employed was extended. A "hardship support" program was launched, with grants, loans, and guarantees to affected firms, co-financed by the confederation and cantons.

Rollout of some measures slowed—notably the hardship program—following lapse of federal emergency authority in September and the need to coordinate across 26 cantons.

8. The fiscal position swung to deficit after years of surpluses. The overall fiscal balance deteriorated by 4 percentage points to -2.6 percent of GDP in 2020. COVID-19-response spending amounted to 2.4 percent of GDP, mostly at the federal level (STWP, self-employed support, unemployment benefits). The take-up of federal COVID-19 measures was about half of approved allocations; this reflected both the large "headline" size of the initiatives and better-than-expected outcomes. Some restrictions, for example, to limit dividend payouts by firms receiving support, may have affected take-up. Revenues performed relatively well—supported by higher SNB profits. Public debt increased to 43 percent of GDP, from 40 percent a year ago.

Box 1. Short-Time Work Program and Guarantees

The short-time work program (STWP) has been a key support instrument during the pandemic. Companies and employees may apply for lost-earnings compensation, normally up to 80 percent. Besides adjusting coverage, disincentives on finding other employment while on STWP were also eased. During the first wave, a fifth of all employees were covered, and the federal contribution to the unemployment insurance fund to compensate for COVID-19-related payments in 2020 was CHF10.8 billion (~1½ percent of GDP). Registration has picked up again since late 2020, with the second wave of infections. For 2021, CHF6 billion has been budgeted.



Sources: SECO, Haver Analytics, and IMF staff calculations.

Loan guarantees were also established. From mid-March through end-July, firms could obtain federally-guaranteed loans from Swiss banks.

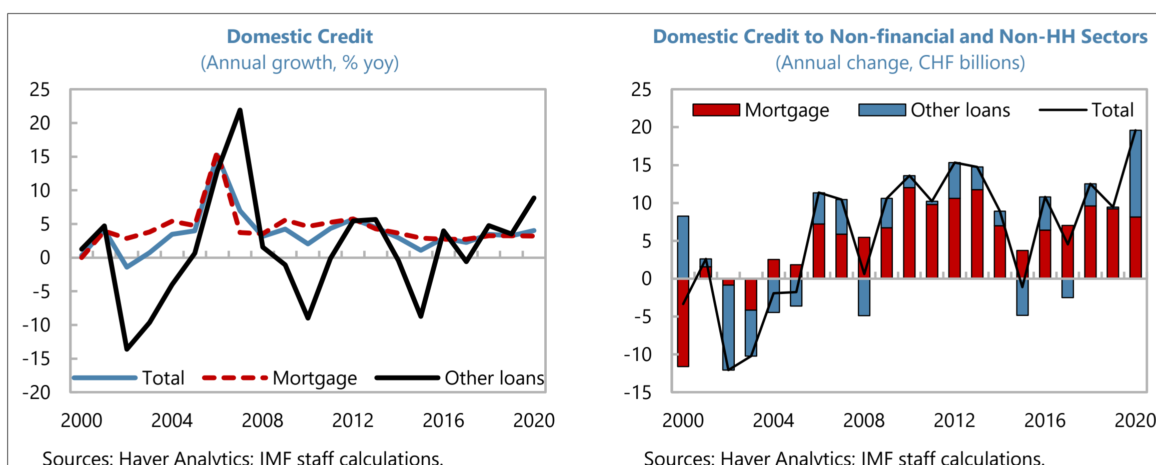
- Loans less than CHF 0.5 million were 100 percent guaranteed, at zero interest rate, with no collateral.
- Loans greater than CHF 0.5 million were 85 percent guaranteed, at 0.5 percent interest rate (guaranteed portion); banks could request collateral and charge a different rate for their part.
- A new SNB "COVID-19 facility" refinanced the loans at -0.75 percent.

Demand for guarantees was less than envisaged. From a CHF40 billion overall envelope for the guarantees, loans of CHF17 billion were disbursed. The envelope was purposefully large, and there were some restrictions on borrowers (e.g., use of funds, dividend payouts). Applicants were mostly small firms in trade, services, manufacturing, construction, food, and accommodations. Refinancing of the loans via the SNB's COVID-19 facility has amounted to around CHF11 billion; CHF2 billion of loans has been fully repaid.

9. Financial conditions tightened when COVID-19 hit, but eased with the policy response. Initial liquidity strains were relieved by the loan guarantees and refinancing. A spike of dollar funding

costs came down with drawing on the U.S. Fed swap line and injection of dollar liquidity. Policy actions not only alleviated direct impacts, but prevented cascading by shoring up confidence, and the stock market experienced a V-shaped rebound. SNB FX purchases in March–May amounted to CHF 90 billion (13 percent of GDP), providing additional liquidity and countering safe-haven inflows and deflationary pressures. Notwithstanding the purchases, the CHF appreciated in 2020 by 6 percent and 4 percent in nominal and real effective exchange rate terms, respectively.

10. The financial sector has so far weathered the crisis well. Supported by loan guarantees and SNB refinancing, non-mortgage lending grew by 6.8 percent in 2020, the fastest rate since 2007 and exceeding mortgage growth for the first time since 2000. Mortgages grew by 3.2 percent, same as in 2019, and residential property prices rose in all segments, fueling concerns on imbalances and affordability. Bank loan provisions rose sharply in Q2, but NPLs rose only modestly and remained at very low levels. Boosted by brokerage and trading income, the large banks saw substantial profit increases in 2020, although overall bank profitability declined. One of the two Swiss GSIBs, Credit Suisse (CS), suffered sizable losses in early 2021, on large exposures to supply-chain finance funds and a U.S. hedge fund; it has overhauled senior management and raised capital. For insurance companies and pension funds, the challenge of low/negative interest rates has remained; there have been few signs that COVID-19 brought additional negative impacts. Reinsurers suffered large pandemic losses, although underlying performance was strong, along with capital.

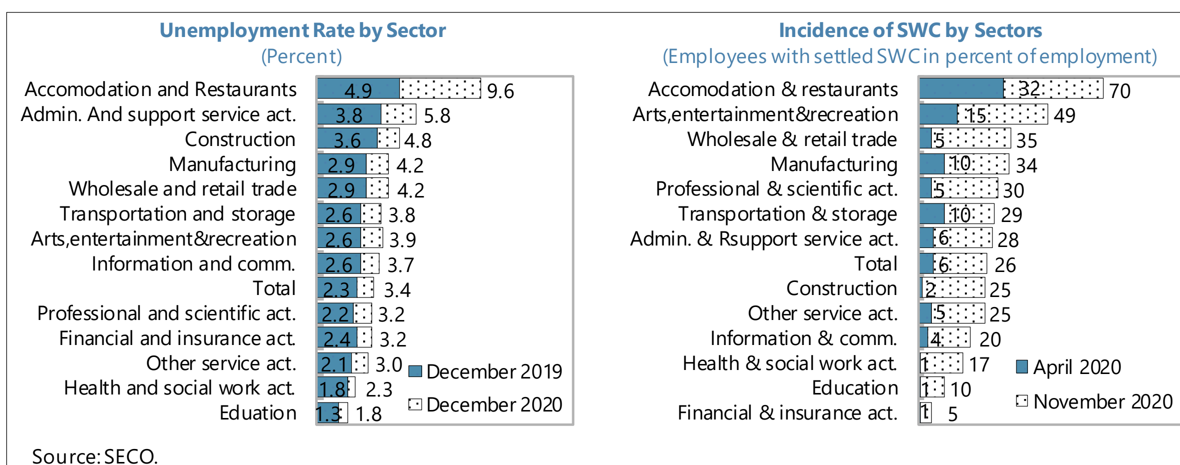


11. Although vulnerabilities have been elevated, especially in contact-intensive sectors, bankruptcies declined. Bankruptcies were 6.6 percent lower in 2020 than 2019, largely reflecting substantial public support. However, the overall picture concealed a severe hit for contact-intensive firms. Surveys in early 2021 indicated that nearly 20 percent of hotels and restaurants had closed with the pandemic, with others in tenuous condition.[1]

12. The pandemic impact on the labor market was also limited overall, but varied across sectors and groups. Unemployment rose by just 1 percentage point, reflecting STWP support. Pressures differed greatly, however, with hospitality and entertainment affected most. Health/social

[1] See Selected Issues Paper on corporate vulnerabilities and policy measures.

care, ICT, retail trade, posts, and finance and insurance were least affected. The crisis had similar effects on men and women, but affected young workers (15–24 years) more than others; there are signs that young workers took more training.



13. Inflation was negative, reflecting lower energy prices and depressed demand, as well as CHF appreciation. Energy and tourism (air travel, hotels, package holidays) were drags on inflation; both were more than 8 percent lower than in 2019. Other imported goods and most services also had a negative impact on overall inflation. Housing rental prices increased.

14. The external current account surplus narrowed sharply. Current account surpluses averaged over 9 percent of GDP during 2010–19, but statistical revisions in December incorporated substantial downward revisions of surpluses in 2018–19.[2] These reflected both updated reporting on income transactions and improved coverage of multinational companies with complex group structures (Box 2). In 2020, the current account surplus decreased to 3.8 percent of GDP, from 6.7 percent in 2019.[3] The decline was broad-based and appears to reflect mainly temporary shocks related to COVID-19: weaker balances for gold (Annex III) and luxury watches and lower investment income, the latter likely due to relatively better performance of Switzerland (expenses) than the rest of the world (income) during the pandemic. The U.S. Treasury designated Switzerland as a currency manipulator in a December 2020 biannual report, after Switzerland met three U.S. criteria for the first time—on the overall current account surplus, on the bilateral trade surplus in goods, and on the extent, frequency, and direction of FXI. The designation led to enhanced U.S-Swiss bilateral consultations in early 2021. The manipulator label was dropped in the Treasury's April 2021 report, although Switzerland continued to meet the three criteria.

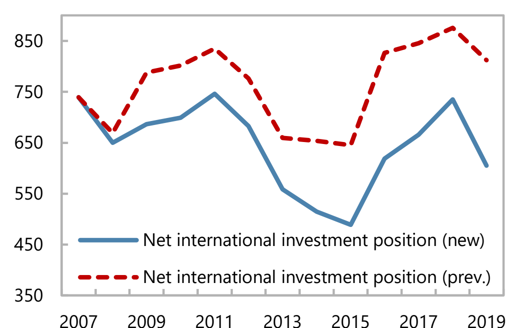
[2] Starting from January 2021, Switzerland has adhered to the IMF's Special Data Dissemination Standard (SDDS) Plus—the highest tier of the Fund's Data Standards Initiative.

[3] Historically, data gaps on investment income between quarterly surveys, the basis for preliminary annual BOP statistics, and annual surveys, the basis for final BOP statistics, have led to significant statistical revisions. To address the gaps, the SNB adopted a new model starting with 2020 data to account for industry and firm-level information in estimating preliminary annual BOP statistics.

Box 2. BOP/IIP Data Revisions in December 2020

In December 2020, the SNB published major revisions to the BOP/IIP data. There were two reasons for the revisions: (a) closing a data gap with regard to domiciliary companies; and (b) reflecting data newly available from reporting institutions. Changes under (b) included both information from a newly-completed 2019 annual survey and corrections for previous reporting periods concerning companies with especially complex structures. The revisions due to (a) affected only the IIP data from 2008 to 2019; due to (b) affected the entire BOP (current account, capital account, financial account) and the IIP for the period from 2014 to 2019. As a result: the net IIP showed an average decrease between 2008 and 2019 of CHF 128 billion (around 17%); and the current account surpluses for 2018 and 2019 decreased significantly, mostly due to adjustments in primary income expenses, while the 2014–17 balances changed less and in both directions.

Effect of the Revisions on the Net IIP
(CHF Billions)



Source: SNB.

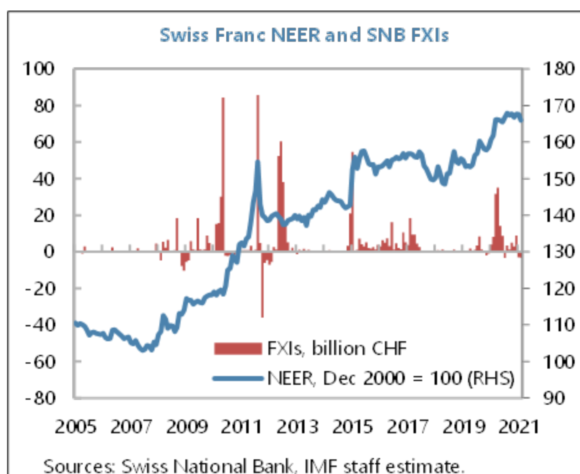
Current Account Balance: December 2020 Vintage versus September 2020 Vintage

CA balance		2014	2015	2016	2017	2018	2019	2020Q1	2020Q2	2020Q3
December 2020 revision	CHF billion	54.6	69.4	61.7	50.0	48.0	48.8	15.4	13.1	8.8
	Percent of GDP	8.1	10.3	9.0	7.2	6.7	6.7	2.2	1.9	1.3
September 2020 vintage	CHF billion	54.6	75.5	68.0	47.0	61.9	79.5	14.5	9.9	
	Percent of GDP	8.1	11.2	9.9	6.8	8.6	10.9	2.1	1.4	

Source: SNB.

15. The 2020 external position is assessed as broadly in line with the level implied by medium-term fundamentals and desirable policies. The assessment reflects the IMF staff-estimated external current account gap, as well as staff judgment on the strength of Switzerland's external balance sheet, macroeconomic policy mix (and scope to rebalance the mix), and buffers (Annex IV). The assessment and the change from 2019 ("moderately stronger") is subject to higher-than-usual uncertainty related to the recent, large BOP data revisions and to accuracy of the COVID-related adjustments applied. The assessment reflects a cyclically-adjusted current account surplus of 3.9 percent of GDP, an IMF external balance assessment (EBA) current account norm of 5.6 percent, and an overall EBA-estimated current account gap of -1.6 percent of GDP in 2020. Adjustments for: (i) specific factors relevant for Switzerland that are not appropriately treated in the income account (valuation losses on fixed-income securities arising from inflation and retained earnings on portfolio equity investment), and (ii) transitory COVID-19 impacts, widen the gap to -3.1 percent of GDP (± 2 percentage points). The adjusted EBA gap suggests REER overvaluation in 2020 of approximately 5.9 percent. However, the strength of the external balance sheet—including the net international investment position and net reserve assets—as well as the policy mix and

Swiss Franc NEER and SNB FXIs



Sources: Swiss National Bank, IMF staff estimate.

buffers lead to the overall staff assessment of the external position as broadly-in-line with fundamentals and desirable policies.

Authorities' Views

16. The authorities consider the Swiss franc as highly valued and the current account surplus in 2020 as smaller than warranted. They considered that staff's traditional approach, which typically emphasizes the current account gap, would have implied an assessment of the Swiss external position as weaker than fundamentals and desirable policies. Staff pointed out that the external sector assessment is intended to be a holistic exercise taking into account the totality of country circumstances.

OUTLOOK AND RISKS

17. Activity should recover with wide vaccination and continued support. GDP is projected to grow by 3.5 percent and 2.8 percent in 2021 and 2022, respectively, led by higher private consumption and investment and an improved global environment. Low interest rates, further STWP support, compensation for self-employed, and extended unemployment insurance will help, along with roll-out of federal-cantonal hardship loans and grants.

18. Over the medium term, growth should converge to potential, with some permanent loss of output. Potential growth of 1½ percent is expected, somewhat below the long-term average growth rate (1.8 percent), reflecting some scarring from the pandemic, including lower labor participation and dislocation and protracted recovery and lower investment in hard-hit industries, such as hospitality and aviation. The external current account surplus is expected to recover as COVID-19 impacts fade and global recovery lifts Switzerland's goods and income balances.

19. Inflation will likely remain subdued. The output gap is expected to close in 2025, adding to other factors that have kept inflation low for a decade. Inflation expectations could be affected by an extended period of low or negative inflation, making it more challenging to boost inflation. The inflation path is clouded by uncertainties on the pandemic, inflation in major advanced economies, commodity prices, and pressures on the franc.

20. Amidst high uncertainty, risks are tilted to the downside in the near term and more balanced over the medium term (Annex V). Near-term risks are connected mainly with COVID-19 developments—delays or insufficient vaccine coverage, new more-contagious or vaccine-resistant strains. NPLs, bankruptcy, and unemployment may pick up as support is withdrawn and scarring may emerge. Also, national referenda on June 13 pose uncertainties on COVID-19-relief programs and climate actions, and there are risks connected with residential and commercial real estate and relations with the EU. Weaker-than-expected and divergent global recovery, renewed trade or geopolitical tensions, and a possible tightening in financial conditions pose external risks. On the upside, expedited vaccine rollout and stronger-than-expected global growth would boost the Swiss economy.

Authorities' Views

21. The authorities broadly shared staff's assessment on the outlook and risks. They noted that strong buffers and the policy response should limit lasting, adverse COVID-19 impacts. They expect a broad and robust recovery once containment measures are durably withdrawn. The authorities shared staff's concerns on global developments, given the importance of external demand for the Swiss economy. They agreed on the key downside risks, and flagged concerns with a surge of public debt internationally noting that this may depress confidence and contribute to fragmentation or possibly trigger a sharp tightening of financial conditions.

POLICY DISCUSSIONS: SUPPORTING RECOVERY AND POST-COVID TRANSFORMATION

22. In the near term, policies should remain accommodative to continue to fight the pandemic and support strong, sustained recovery. Measures implemented thus far have been essential to contain adverse COVID-19 impacts. As the pandemic recedes, fiscal policy should continue to play a lead role, given substantial fiscal space and to avoid cliff effects, ensure sustained recovery, and ease pressure on monetary policy. In light of expected prolonged negative/very low inflation, monetary policy should remain accommodative. Financial market policies should aim to contain vulnerabilities by enhanced monitoring of risks and ensuring strong buffers, while addressing challenges from negative interest rates, search-for-yield behavior, and digitization. Labor market policies should remain focused on addressing uneven impacts of the pandemic and skills gaps, mitigating scarring, and increasingly, fostering necessary reallocation. As recovery advances, policies should enhance and accelerate efforts to foster green, digital, inclusive transformation, while addressing structural challenges (e.g., pensions).

A. Fiscal Policy: Maintaining Adequate Support

23. The authorities are appropriately extending fiscal support in 2021, including rolling out targeted initiatives. As the pandemic continues to affect the economy, the authorities announced COVID-19-related measures totaling CHF24 billion or 3.2 percent of GDP in 2021. These include extension of the STWP and self-employed compensation and CHF10 billion of hardship support for firms. If fully implemented, this would increase COVID-19-related expenditures from CHF15 billion in 2020 and lead to a further widening of the overall deficit by 0.8 pp. to -3.4 percent of GDP. However, implementation may again be below headline budgeted amounts, especially if the recovery is strong.

24. Given continuing uncertainty and available fiscal space, the authorities should expand near-term support, if needed. Fiscal space is substantial, as indicated by low public debt and gross financing needs, access to financing at low/negative interest rates, and scope to raise revenues or redirect spending, if needed (Annex VI). COVID-19-response measures are set to phase out at end-2021, and the authorities should continue careful monitoring of stresses on households and firms with a view to avoiding cliff effects. If COVID-19 resurges or is prolonged, further support should be

put in place, possibly involving funding for viable companies and affected individuals, or for hard-hit hospitals, cantons, municipalities, and transit systems. The design of measures should draw on lessons from support already employed in Switzerland (and elsewhere). As previously, measures should be temporary and targeted to limit distortions and disincentives for post-COVID-19 transformation.

Announced and Implemented COVID-19 Related Federal Measures
(In percent of GDP)

	2020		2021
	Announced	Implemented	Announced
Total expenditures	4.5	2.1	3.2
Contribution to unemployment insurance	2.9	1.5	0.8
Loss of earnings compensation	0.8	0.3	0.4
Hardship support	0.0	0.0	1.1
Health	0.4	0.1	0.4
Losses on COVID-19 bridge loans	0.1	0.0	0.1
Transport	0.1	0.1	0.1
Culture and leisure	0.1	0.0	0.1
Other	0.1	0.1	0.1
Memo:			
Extraordinary expenditures	4.4	2.1	2.7
Sureties and guarantees	6.1	2.5	0.0

Sources: Swiss authorities and IMF Staff calculations. Data as of April 28, 2021

25. Policy implementation under the fiscal framework requires fine tuning. As noted, the pace of normalization should be calibrated to COVID-19 and economic conditions. The fiscal framework calls for amortization of extraordinary outlays over six years (offsetting through expenditure cuts or revenue measures). The amount to be amortized is significant—likely about CHF30 billion, 4 percent of GDP, by end-2021—and extending the offset period to 10 or 15 years or offsetting the outlays against past accumulated surpluses would limit headwinds for the recovery. Also, while the fiscal framework mandates structural balance over the cycle, underspending and revenue overperformance have led to persistent surpluses. The authorities should continue to improve revenue forecasting, and to limit spending underruns, explore expenditure ceilings that build in a buffer or margin, are more flexible (e.g., multi-year), or are contingent on developments. Enhancing canton-federal and cross-canton cooperation would increase efficiency/effectiveness of operations.

26. Important tax reforms are underway. Corporate income tax (CIT) reforms in line with international best practices/standards came into force in 2020; several cantons are considering adjustments to CIT rates and investment incentives. International agreement on a minimum CIT rate and other provisions (e.g., digitax) could require further changes, with offsets under the debt-brake rule, if there are revenue losses. Another reform relates to withholding taxes and stamp duties. Issuance of debt securities in Switzerland is low, partly reflecting a sizable withholding tax on most capital revenues. The authorities have proposed to abolish the withholding tax on fixed-income investments and one of three stamp duties. Tax changes should ensure sufficient revenues, ease compliance burdens, and reduce or eliminate distortions.

27. Beyond immediate challenges and narrow adjustments under the debt-brake framework, policies should be rebalanced to provide additional support, especially for post-

COVID-19 green, digital transformation. Measures to enhance physical and digital infrastructure and human capital are already being implemented or are in the pipeline. Efforts to support post-COVID-19 transformation should build on these programs and plans. The ambitious new Long-Term Climate Strategy, launched in January 2021, targets zero-net carbon emissions from 2050 and substantial investments in energy, transportation, and building renovations. It would benefit from accelerated and/or additional outlays (Box 3) to allow Switzerland to maintain the quality and comparative advantage of its infrastructure and human capital. This would correspond to similar programs being initiated in EU member countries and in other AEs. An increase in fiscal outlays would help rebalance the policy mix, easing pressures on monetary policy. Depending on the size of these outlays, a review of the fiscal framework may be needed.

Authorities' Views

28. The authorities agreed that fiscal policy should continue to play a central role in supporting the economy throughout the pandemic. They believed that the debt-brake framework performed very well during COVID-19, as the shock underscored the importance of maintaining robust buffers to be ready for adverse events and of flexibility to respond quickly and forcefully with extraordinary outlays. The authorities stand ready to deploy additional resources if needed, but also stressed that prolonged aid should not impede post-COVID-19 transformation. They agreed that fine-tuning under the framework is needed: a longer offset period (from 6 to 15 years) for emergency spending (or offsetting against past surpluses), along with efforts to limit spending underruns and improve revenue forecasting.

29. The authorities consider that their current policy framework and planned outlays are broadly sufficient for post-COVID-19 recovery and transformation. In response to suggested higher medium- and long-term outlays for climate mitigation, digitization, and R&D, they pointed to existing plans for major public investments in physical and digital infrastructure, ongoing support for the green economy, relatively limited infrastructure gaps, and preference for private-sector involvement and leadership. In 2019, parliament adopted a 10-year, CHF13 billion investment program in railway infrastructure. Subject to a referendum on June 13, 2021, a new Climate Fund, financed by CO_2 and air travel levies, will provide about CHF1 billion annually for climate investment and R&D. They did agree that additional or accelerated investments of high effectiveness and efficiency in energy, agriculture, building renovation, transport, R&D, adaptation, and mitigation could help ensure that Switzerland meets its ambitious CO_2 targets and retains competitiveness, provided that these have synergies with ongoing programs.

Box 3. Long-Term Climate Strategy

Climate change is being felt acutely in Switzerland in agricultural and tourism, with more frequent heat waves, droughts, floods, and landslides, and lack of snowfall. In January 2021, the Federal Council adopted a new long-term climate strategy (LTCS) through 2050, in line with Paris Agreement commitments. The LTCS is based on a net-zero emissions target for 2050 and revisions to the CO_2 Act, which provide the legal basis for climate actions through 2030. The LTCS lays out principles to guide policy actions for both activities and users through 2030. A fifty percent emissions reduction target is in place for 2030 overall, with sector specific targets for: buildings (-65 percent), industry (-35 percent), transport (-25 percent), and

Box 3. Long-Term Climate Strategy (concluded)

agricultural (-20 percent). Other actions target the financial sector, aviation, and waste management. Negative emissions technology will be needed to achieve the 2050 targets.

Emissions reductions through 2030 will take place via regulation (e.g., fuel standards, required offsets by fuel importers), taxation, financial incentives, investments, and new technologies. The LTCS lays out sectoral investment needs, noting significant needs in energy, building retrofits, industry, and transport. A new Climate Fund (CF) will provide CHF 1 billion annually for reduction, mitigation, adaptation, and new technology, financed by levies on heating fuels, a new air-travel levy, payments by vehicle importers, penalties, and receipts from auction of emission rights. Federal and cantonal budgets will provide additional funding. CF resources will not cover needs, however, and additional public and private actions and outlays will be required. For example, for building renovations, the LTCS notes that existing federal and cantonal tax allowances and the current low-interest rate environment will provide support. Devolution of responsibility in some areas to cantons—notably buildings regulations—could complicate achievement of reduction targets, although importantly, there is a ban on CO_2 emissions from *new* buildings constructed from 2023.

Some important sectors and activities receive lighter treatment for now. Agriculture emissions are to be cut by a third through 2050, and while livestock production and meat and dairy consumption are key contributors, the LTCS does not make specific proposals for taxation or regulation, although food waste reduction will be targeted. The LTCS calls out the financial sector for not supporting sufficiently climate goals (e.g., lack of reporting requirements on the short- and long-term climate impacts of financing decisions). It envisages a voluntary approach for now, indicating that regulation may eventually be needed, possibly following the lead of other jurisdictions or an emerging global consensus. Higher motor fuel taxes have not gained public or parliamentary support; the LTCS calls for lower emissions through offsets by fuel importers (up to 75 percent abroad) and payments by vehicle importers. Higher carbon levies are envisaged for fuels used in heating. Switzerland's energy mix poses challenges, particularly as nuclear generators are expected to be phased out when they reach the end of operating lives, and projected demand increases due to electrification of transport and heating/AC. The LTCS also notes that actions will be needed to decarbonize supply chains for Swiss imports and to ensure no leakage of emissions abroad (two-thirds of Switzerland's carbon footprint is generated abroad). The authorities are closely monitoring EU and global consideration of carbon border adjustment mechanisms.

On June 13, 2021, a national referendum will be held on the revised CO_2 Act. There is opposition from some businesses (fuels, transport), the main conservative party, and some who consider that the revisions do not go far enough. If the Act is voted down, the current 2030 reduction target of 21 percent and tax rates will remain in place. With passage and in time, new legislation will be needed for subsequent periods.

B. Monetary and Exchange Rate Policy: Continuing Accommodation

30. The SNB is rightly keeping monetary policy accommodative. The pandemic continues to have a strong, adverse effect on the economy, and expansionary policy has helped stabilize activity by providing favorable financing conditions and support for liquidity and credit. The SNB has kept its policy rate at −0.75% and expressed a willingness to intervene in the FX market—a key mechanism for quantitative easing—as needed. The CRF—with banks in the lead in originating loans and the government mitigating credit risk with guarantees—was an innovative and critical extension of the SNB's toolkit. Lending was further supported by increased exemption thresholds for application of negative interest rates on sight deposits—easing profitability pressures, by suspension of a sectoral CCyB, and earlier, by drawing on the dollar swap line. Unconventional monetary policy in the form of unsterilized FXI should continue if strong safe-haven inflows resume, and if needed, to lean against

particularly strong appreciation pressures that would worsen deflation, but not to prevent a continued appreciation trend.

31. Following COVID-19, the SNB may find it increasingly difficult to achieve its price-stability mandate. The long-standing challenge of low inflation may have worsened: inflation has been negative since the onset of the pandemic and may remain negative, or at very low positive rates, for an extended period. The SNB forecasts inflation at 0.2 percent in 2021, 0.4 percent in 2022 and 0.5 percent for 2023. Inflation expectations may settle at lower levels with an extended period of negative or very low inflation, with adverse consequences for savings, credit, demand, pensioners, and financial institutions. Monetary policy may be facing more limited room for maneuver: lower policy rates of other central banks have cut the SNB's traditional margin, and further SNB rate cuts, while possible, may have undesirable side effects on profitability of financial institutions, housing prices, or cash hoarding. FXIs have expanded the SNB's balance sheet and provided franc liquidity, but together with negative interest rates, have not kept inflation consistently within the price band or translated into strong growth of non-mortgage credit.

32. Like other major central banks, the SNB should review its monetary policy framework and tools, especially in light of the experience during COVID-19. This would consider whether adjusting or extending targets, instruments, and communications would enable the SNB to continue to respond to new challenges. The SNB should continue to assess whether extended instruments—such as the purchase of a wider range of assets for QE or funding-for-lending programs (following on the successful CRF experience)—may help to secure price stability (Box 4).

Box 4. Switzerland's Monetary Framework

Swiss monetary policy aims to ensure price stability, defined as annual inflation of less than 2 percent. Since the global financial crisis (GFC), policies have also had to navigate appreciation pressures and occasional safe-haven surges via negative interest rate policy (NIRP), forward guidance (publication of conditional forecasts), and as needed, FXI. There are limited CHF-denominated assets for quantitative easing (QE). During the post-GFC period, credit growth has focused on mortgages. The COVID-19 shock may involve additional challenges if inflation remains at negative or very low rates.

Growth has averaged around 2 percent since the GFC, and the Swiss economy is flexible, resilient, diverse, and competitive. However, monetary policy has faced challenges in delivering price stability. Inflation was virtually zero over the post-GFC period and negative in five years. Other advanced economies (AEs) have also dealt with low inflation, but the challenge appears especially acute in Switzerland. There is a risk that inflation expectations will be driven even lower with the COVID-19 shock, with a drag on consumption, bank profits, lending, investment, and growth.

Chronically-low or negative inflation, despite sound growth, suggests examining the effectiveness of monetary transmission. Over the past decade, market interest rates have moved in tandem with SNB policy rate changes, including in negative territory. Driven by FXI, the monetary base has expanded rapidly, although broad money did not grow at nearly the same pace or magnitude, and the money multiplier declined sharply, more than in other AEs. Credit growth involved mainly mortgages. Non-mortgage loans to non-financial corporations remained unchanged in nominal terms during 2009–19.

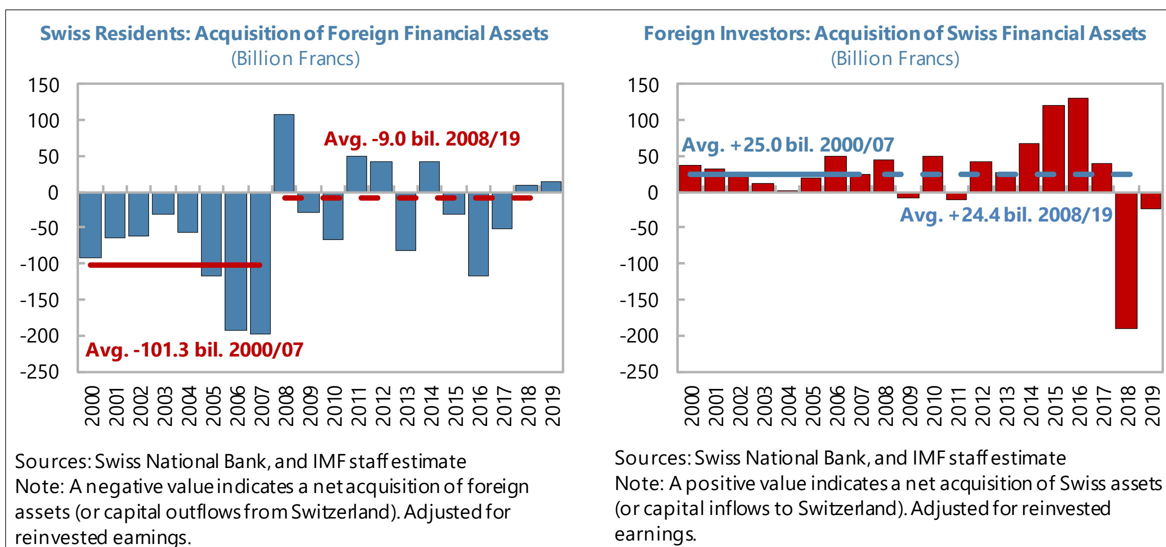
A key consideration is whether there is sufficient policy space or instruments to tackle "lowflation," given pressures on profits of financial firms, risks from "search-for-yield" behavior, possible cash

Box 4. Switzerland's Monetary Framework (concluded)

hoarding, and for FXI, concerns with effectiveness in stemming low inflation and balance-sheet risks. What can the SNB do, on its own and with the government? Although the economy is not lacking liquidity or demand for mortgage credit, there may to be room to boost credit demand for consumption and investment. However, structural or business-culture factors (e.g., taxation, bank competition) may need attention. Pre-COVID-19, most SMEs had not taken loans, and Swiss households typically do not access credit, except for housing. Possible measures could include further forward guidance, yield-curve control (YCC), adjustments to tiering and exemptions for negative interest rates (to incentivize lending), or possibly, targeted credit support ("funding-for-lending") for specific maturities, borrowers, or activities, building on the experience with the new COVID-19 Refinancing Facility. Additional macroprudential actions could address price risks and facilitate policy flexibility, as needed.

Each of these actions faces challenges and constraints. As government bond yields at all maturities are already negative, YCC may not help much. Changes in tiering could fuel disintermediation and cash hoarding, muting expansion. Funding-for-lending may bring the SNB close to a fiscal function (and possibly impede post-COVID-19 transformation). Fiscal policy could help, with stepped up spending on education, R&D, digitization, or climate mitigation; tax cuts could be considered. However, the debt-brake framework and policy preferences are constraints. Other central banks have recently undertaken monetary policy reviews, including the U.S. Fed, the ECB, the Bank of England, Bank of Japan, and Bank of Canada. These have assessed price targets, the effectiveness of existing tools, and costs/benefits of new instruments. The SNB continually reviews its tools and framework, with consideration to effectiveness, feasibility, side effects, and other factors (e.g., independence).

33. **Easing appreciation pressures in a fundamental way is important**. Upward pressures on the franc have been persistent since the global financial crisis (GFC) in 2008–09, with occasional, strong safe-haven inflows. A contributor to post-GFC pressures has been greater reluctance by residents to invest abroad, combined with Swiss firms not tapping domestic savings. With limited private outflows or even net inflows, the SNB has needed to employ "defensive tools" such as negative policy rates and FXIs to dissuade and absorb excess funds. A self-reinforcing element may



Sources: Swiss National Bank, and IMF staff estimate
Note: A negative value indicates a net acquisition of foreign assets (or capital outflows from Switzerland). Adjusted for reinvested earnings.

Sources: Swiss National Bank, and IMF staff estimate
Note: A positive value indicates a net acquisition of Swiss assets (or capital inflows to Switzerland). Adjusted for reinvested earnings.

have developed with the shift, as franc appreciation has reduced the appeal of investing abroad.[4] A review of factors contributing to "home bias"—such as regulatory issues, tax considerations, or asset management guidelines—may identify possible actions. More expansionary fiscal policy over the medium-long term could help reduce domestic savings.

Authorities' Views

34. The SNB agreed that policies should remain accommodative. In light of strong, continuing, adverse effects of the pandemic on the Swiss and global economies, the SNB will maintain expansionary policy. The authorities noted that the recovery in Switzerland has lost some momentum since late 2020 with a second wave of the pandemic. They noted that the franc remains highly valued and expressed continued readiness to intervene in the FX market as needed to counter deflationary pressures. They also observed that the inflation and growth outlook in Switzerland and abroad are subject to high uncertainty.

35. The SNB expressed commitment to regular, continuous review of its policy framework, especially given its experience during COVID-19, while noting that the framework has served the Swiss economy very well. The SNB is following with interest the policy reviews of other major central banks, notably the ECB, given close links to neighboring eurozone countries, as well as the introduction of new tools and instruments. They explained that they continuously review the SNB's framework and tools, expressing strong preference for the current 0–2 percent price stability definition. This definition has provided both guidance and flexibility, while facilitating prompt response to difficult situations, including the quick rollout of the CRF and other measures. Publication of conditional inflation forecasts has supported policy guidance, although the SNB agreed that communications could be further bolstered. As a small, open economy, they expressed doubts about the feasibility of a point target for inflation, as well as prospects for expanded domestic quantitative easing or funding-for-lending programs, which could move the SNB towards a fiscal-policy function. The SNB sees sufficient space under both the negative interest rate policy and FXIs. They were interested in review of post-GFC "home bias" of Swiss investors, but noted concern with greater FX exposure, especially pension funds.

C. Financial Sector Policies: Monitoring Risks and Reinforcing Stability

36. Most emergency regulatory adjustments for banks have appropriately expired. Direct support at the beginning of the crisis was short, including a two-week debt standstill and a 90-day extension of rental payments. The exclusion of central bank reserves from leverage-ratio calculations released resources for lending and was extended once, in May 2020, to the beginning of 2021. Most other temporary provisions—aimed at reducing volatility or ensuring business continuity—have phased out after conditions stabilized. An important exception is suspension of the sectoral CCyB, which has not been reactivated.

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[4] See Selected Issues Paper on home bias and recycling current account surpluses.

37. The banking sector remains strong, but asset quality review should be enhanced, especially for banks with lower capital and higher exposure to COVID-19-sensitive sectors. Banks entered the crisis with strong buffers, and losses have been limited, reflecting strong policy support and prudential measures. Deteriorating asset quality is a risk, although bank exposure to contact-heavy firms is limited, and the new hardship grants will help. The authorities should continue to review preemptively asset-quality conditions and improve resolution mechanisms. A pick-up of defaults and bankruptcies could affect smaller banks with higher exposures or lower buffers.

38. Residential property prices have risen during the crisis, increasing affordability and imbalance concerns; commercial real estate faces risks from negative COVID-19 effects. Rising house prices have increased imbalances, especially among rentals, where vacancies are higher.[5] A deterioration of affordability may take place when income support is withdrawn and should be monitored. Commercial real estate, especially outside core central business districts, also faces risks from negative pandemic effects and changes in occupancy, rents, and valuations. Voluntary self-regulation by financial institutions may face limits in terms of timeliness and stringency, and proactive measures (e.g., LTV or DTI restrictions) may be needed. The sectoral CCyB deactivation was appropriate, but should remain temporary, with buffers reset for potential real estate developments when conditions allow. Review of restrictions on housing supply in core urban areas and possible tax distortions may help identify measures to address imbalances.

39. While the financial sector has weathered negative interest rates well so far, prospects for further prolonged negative rates calls for continued close monitoring of side effects. Financial firms have reacted to low margins by reducing costs and seeking higher returns—mortgages, other assets/investments, including leveraged—with higher risks. Smaller banks are under pressure from digitization, and domestic SIFI PostFinance faces challenges from low margins and business restrictions. Risks may quickly materialize—as shown by the recent negative experience of Credit Suisse—underscoring the importance of enhanced supervision, regulation—particularly of complex products, and international cooperation. The authorities should continue to monitor risk-controls and buffers, and be prepared to take early actions.

40. Progress has been made in implementing recommendations from the 2019 FSAP, but gaps remain. A new ordinance has clarified the powers of the regulator, FINMA, and how they relate to those of the Federal Council and Federal Department of Finance, although further work is needed to strengthen FINMA's autonomy, governance, and accountability. FINMA's resource constraint has been eased, including through cost saving from a more effective auditing process. This has allowed FINMA to strengthen information collection in key areas, carry out more on-site inspections, and allocate resources to new coverage of climate issues and cyber security risks. Less progress has been made by the authorities in making macroprudential policymaking more agile and proactive, in reducing regulatory gaps on fintech activities, particularly involving retail investor protection, and in making far-reaching structural changes to the deposit insurance set-up.

[5] See Selected Issues Paper on breakeven vacancy rate in residential real estate.

Authorities' Views

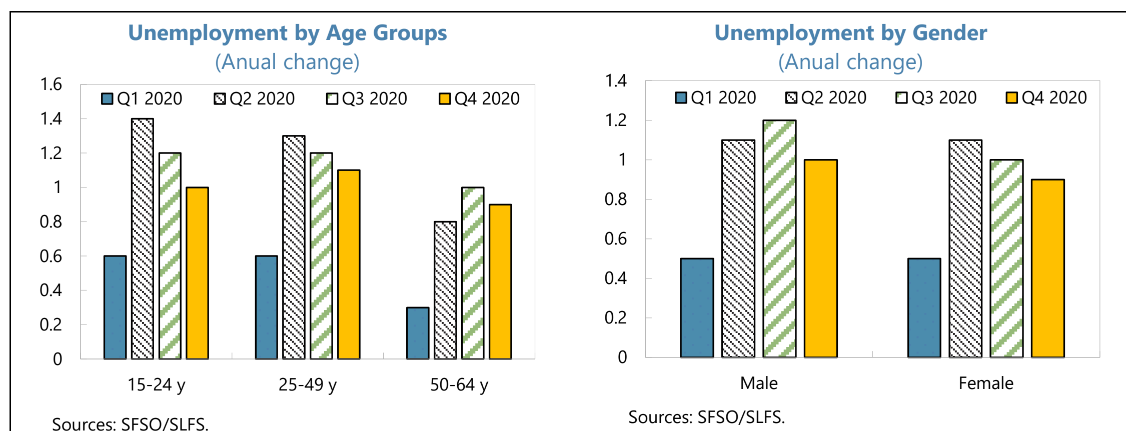
41. The authorities also see risks from real estate and search-for-yield behavior and are monitoring these carefully. They shared staff's overall assessment and agreed that lagged effects of the COVID-19 crisis, real estate developments, and "lower-for-longer" pressures may have potentially important implications for financial stability. They will continue to monitor developments closely, as well as fintech and crypto activities. They highlighted progress made in implementing FSAP advice, especially on resources for FINMA, strengthening data collection and analysis, increasing risk-based on-site inspections, and improving recovery and resolution planning. They noted that the traditional approach of bank self-regulation in Switzerland has advantages—especially ownership—and stressed that self-regulatory measures may become binding and are augmented when needed. SNB and FINMA pointed to the effectiveness of new, stronger self-regulation on LTV ratios and faster amortization of mortgage loans for investment purposes from January 2020. Recent large market losses and risk controls are being closely examined. Smaller regional and cantonal banks have strong capital buffers and are prepared for further competitive pressures, including digitization. A solution is being sought for PostFinance.

D. Structural Policies: Addressing Long-Standing Challenges

Labor Market

42. Policy actions helped cushion crisis impacts on the labor market; however, impacts have been uneven across different groups. The STWP has provided essential support, especially to lower-skilled workers, while income compensation for the self-employed and regular unemployment benefits have also helped. Measures supporting apprenticeships and career-mentoring programs dampened youth-unemployment impacts. However, first-time job seekers face increasing difficulties, and young workers have experienced disruptions in education that could dampen future prospects. While the labor market started to normalize in the second half of 2020, scarring risks remain, especially for workers in contact-intensive sectors. As women and lower-skilled workers comprise a high share of employees in these sectors and among part-time workers, pre-COVID-19 employment gaps and income-insecurity risks may be magnified.

43. Policies should continue to provide support to mitigate scarring, but also increasingly promote flexibility and mobility, as well as longer and wider participation. Pre-COVID-19 structural changes, especially technological advances, helped the labor market adapt to containment measures by remote working, e-commerce, and cashless payments. But the pandemic also brought significant challenges, and vulnerabilities remain. Ensuring reemployment and reallocation of workers from the most-affected sectors will require well-targeted active labor market policies (ALMPs), focused on upskilling and reskilling for jobs with high future demand. Expanded training and mentorship programs would improve prospects for young workers and first-time job seekers. Policies should also address pre-pandemic gaps, including by measures to encourage women to remain in the labor force (e.g., better childcare) and removing disincentives for hiring or retaining older workers.



Authorities' Views

44. The authorities agreed with the need to implement labor-market measures to mitigate scarring and facilitate reallocation. They agreed that measures implemented thus far have been effective in sustaining labor-force participation and arresting adverse impacts. They agreed that there is potential for scarring in some sectors and that crisis-related changes to eligibility, coverage, and duration of STWP support should remain in place, along with extended support for self-employed and unemployed, until sustained recovery is underway. They expressed concern that keeping support measures in place for too long could impede post-COVID-19 transformation. Targeted ALMPs would help facilitate and respond to structural change, supported by the proven flexibility of the Swiss labor market.

Pension System

45. Pensions are not well-aligned with demographic or economic trends. The population is aging fast, with life expectancy also increasing. With old-age dependency expected to more than double over the next few decades and statutory retirement well below average life expectancy, the length of time in retirement will become one of the longest among OECD countries. The first pillar (PAYGO) of the pension system is expected to run into large funding gaps by 2030—3 percent of GDP—and the long period of very low interest rates is placing strains on second-pillar pension funds (PFs).[6] With a minimum-guaranteed return via an above-market mandatory conversion rate, some PFs are underfunded, especially those with government guarantees.[7] The situation has pushed some PFs to take increasing risks to compensate for low returns or to fund shortfalls at the expense of voluntary savings.

46. Without decisive reforms, pension adequacy and equality are at risk. The pension system currently provides for adequate retirement income; however, replacement rates from mandatory schemes are expected to decline significantly over the next decades. While voluntary high saving may provide a cushion for falling future pension benefits, lower-income earners are less able to

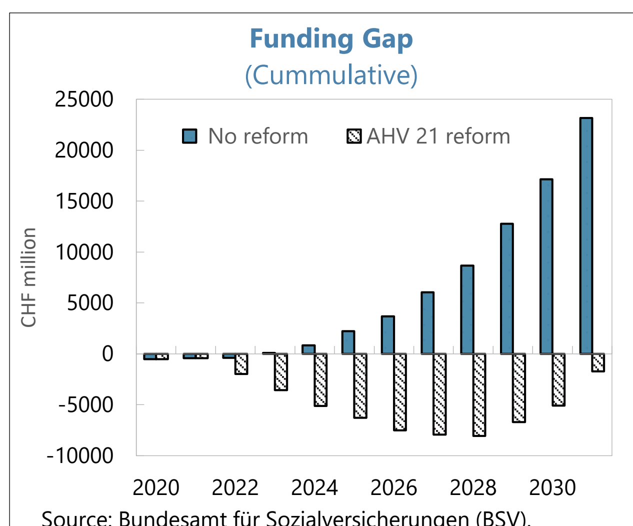
[6] See Selected Issues Paper on the pension system and reform options.

[7] The mandatory 6.8% conversion rate implies returns of 4.8%—well above market.

compensate through savings. There are gender gaps, as lower hours work of women result in less lifetime earnings; with a projected longer lifespan, women are at greater risk of old-age poverty.

47. Parliament is considering first- and second-pillar reforms. These aim at enhancing sustainability while maintaining pension levels. Second-pillar reforms also aim to improve benefits for low-income earners, part-time workers, and those with multiple jobs. To address the first-pillar funding gap, a gradual male-female retirement age harmonization has been proposed, increasing the retirement age for women by a year to 65; a VAT rate hike will provide additional funding. Second-pillar reforms aim to reduce PF financial pressures through a one-time conversion rate cut to 6 percent. To address negative pension-level impacts from the changes, transitional compensation has been proposed for the higher female retirement age and the conversion-rate cut. Post-retirement-age incentives to stay in the labor force have also been proposed, together with greater flexibility seeking employment while in retirement.

48. The proposals are steps in the right direction, but more ambitious reforms are needed. The proposals are sufficient to stabilize the funding gap over the next decade, but the gain is mostly shouldered by higher VAT funding, providing only a temporary solution. The retirement age harmonization does not go far enough to close gaps, increasing the likely need for more budget support. Given the fiscal framework, this would have to be offset elsewhere, competing with other spending needs. Continuous increases of the VAT rate are not an attractive solution. Sustainable reforms call for a larger increase of the retirement age and automatic links to longer life expectancy to keep up with demographic changes.



Source: Bundesamt für Sozialversicherungen (BSV).

49. Second-pillar reforms should align parameters with market trends. The proposed expansion of coverage will help reduce incidence of inadequate retirement income, especially for those with low salaries or part-time jobs. However, while the conversion-rate cut will help alleviate pressure on PFs, it should go further and align more closely with market trends: some studies suggest that a 5 percent conversion rate is needed. Simplifying the regulatory environment, continued optimizing of PF investment practices (while accounting for pension-fund risk profiles and risk-return trade-offs), and strengthening PF governance arrangements would help improve PF performance and reduce costs. A further reduction of the number of PFs would help achieve economies of scale. More ambitious reforms of both pillars are challenging as changes are likely to be unpopular and subject to national referenda.

Authorities' Views

50. The authorities agreed with the need for pension reforms. They pointed out that the financial situation of the Swiss pension system is less dire than in other countries and noted that reforms should be well-designed and calibrated—with tradeoffs—to gain support. They observed that second-pillar reforms will need to consider compensatory measures to help maintain pension levels at current levels and ensure that the reforms will pass the political process. They agreed that more needs to be done to improve PF performance but cautioned that comparison to PFs in other countries is not straightforward. They consider that the regulatory framework for PF asset management has flexibility to invest across the whole spectrum of asset classes with built-in safeguards. They agree with the need to further consolidate PFs, noting that this is happening organically. They also noted advantages in having many PFs: greater investor choice.

Climate Change

51. A new long-term climate strategy (LTCS) was approved by the government in January, with guidelines and targets through 2050. By 2019, Switzerland had recorded a 14 percent decline in CO_2 emissions compared to 1990; pandemic-related restrictions may have helped achieve the 20 percent reduction target for 2020. The LTCS is a welcome extension of targets, principles, guidelines, and tools, including the new Climate Fund. A clear, monitorable emissions action plan will be needed to support the LTCS and address gaps and risks. Other advanced economies in Europe and North America are devising large "green new deal" programs to meet climate targets and digitization and inclusive growth objectives. These programs involve investments in transport, green and renewable energy generation and storage, building retrofits, R&D, and digital infrastructure. While recognizing that the Swiss authorities are undertaking and planning green investments of their own, consideration should be given to further targeted measures and whether investments should be increased or accelerated to help meet ambitious targets and retain competitiveness. A robust public financial management and governance framework will be needed for the new Climate Fund.

Authorities' Views

52. The authorities will continue and advance efforts to further the climate agenda domestically and internationally and reduce emissions. They noted that Switzerland has already made significant contributions and has substantial climate-related outlays in the pipeline. They acknowledged that the road ahead will be challenging, including on building retrofits, fuels, denuclearization, agriculture, finance, and import supply chains. They noted that the LTCS will be fleshed out with concrete measures and pointed to the Climate Fund as a major step forward in providing substantial dedicated funding for investment, mitigation, and new technology. They agreed that its resources will need to be used effectively and transparently to facilitate change and sustain support.

Governance

53. Several measures to strengthen governance have been implemented recently or are underway. The authorities have initiated a review of the effectiveness of COVID-19-related spending. The Federal Audit Office has conducted several interim assessments of support measures to date; these have found quite limited abuse (e.g., less than 1 percent of loan guarantees have been called to date and less than 1 percent have involved criminal complaints). Parliament recently adopted legal changes to strengthen the AML framework, although a proposal to subject lawyers and fiduciaries to due diligence requirements was rejected. The authorities should persevere with efforts to ensure accountability of COVID-19-related spending and enhance the AML/CFT framework.[8]

Authorities' Views

54. The authorities are committed to ensuring sound COVID-19-related spending and improving the AML/CFT framework. They noted efforts in both areas and their engagement on corruption and governance issues in the international forums.

STAFF APPRAISAL

55. Switzerland has navigated COVID-19 well. The pandemic has had major social and economic impacts, but an early, strong, and sustained public health and economic policy response helped contain the contraction of activity. Other important factors were strong fiscal, financial, and household buffers, contributions from important export industries (pharmaceuticals, chemicals), relatively low reliance on contact-intensive sectors, a well-resourced health system, targeted containment measures, and progressive adaptation. The authorities' actions appropriately targeted liquidity of households and firms. Comprehensive and coordinated efforts stemmed a loss of purchasing power and a rise of unemployment and bankruptcies, while countering deflationary pressures.

56. Recovery has commenced, but Switzerland has been affected by further waves of infection, and uncertainty and risks remain high. Near-term risks are dominated by pandemic dynamics, including more contagious or virulent strains and slow or incomplete vaccination. The recovery should accelerate as vaccination proceeds, containment measures are lifted, and domestic and global demand picks up. A weak global recovery, adverse risk sentiments, a tightening of global financial conditions (possibly associated with higher debt levels internationally), worsening trade frictions, or faster deglobalization may adversely affect the outlook. The crisis is likely to have scarring effects, especially in sectors where demand is likely to recover slowly (e.g., hospitality, events). Although unemployment, NPLs, and bankruptcies have not risen sharply, this could change. Progress in discussions with the EU is needed to secure continued market access on favorable terms.

[8] The IMF's assessment of Switzerland's framework for dealing with bribery of foreign officials and AML/CFT (foreseen for this cycle) will take place in 2022.

57. The authorities have rightly extended fiscal support in 2021. Fiscal policy should remain accommodative until there are signs of sustained recovery, and in light of continuing uncertainty and availability of fiscal space, the authorities should expand support if needed. Policies should focus on ensuring a strong rebound, protecting vulnerable groups, mitigating labor-market dislocation and scarring, and ensuring that viable firms stay in business. Avoiding an early withdrawal of fiscal support or headwinds from too-rapid adjustment is essential, and adjustments under the existing fiscal framework will be important—especially lengthening the amortization period for extraordinary spending. Strengthening federal-cantonal coordination would increase the efficiency, effectiveness, and timeliness of intervention. Extraordinary support is scheduled to phase out at the end of 2021; this will help ensure that prolonged support does not impede post-COVID-19 reallocation and transformation. Stamp duty, withholding tax, and OECD-led CIT reforms under consideration should ease tax and compliance burdens and improve capital market functioning. Over the medium term, Switzerland should continue—and enhance, where possible—fiscal support for green and digital growth, in an efficient and targeted way and with particular attention to low-income earners. Rebalancing the policy mix by increasing the role of fiscal policy would also help to ease pressures on monetary policy and maintain the external position broadly in line with medium-term fundamentals and desirable policies.

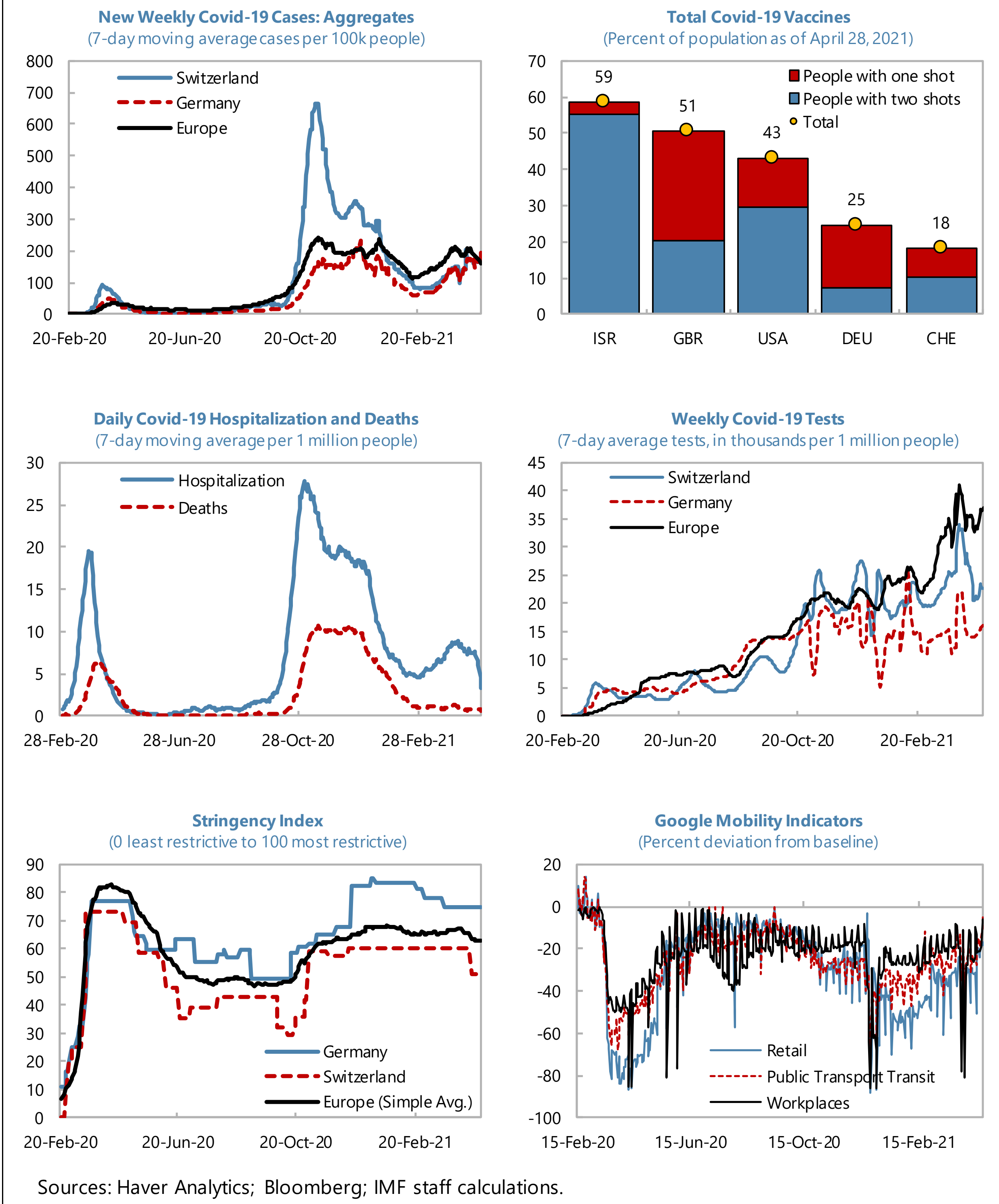
58. Accommodative monetary policies should continue. In light of continuing uncertainty and risks of an extended period of very low or negative inflation, monetary policy should remain accommodative, including using unconventional policies via unsterilized FX intervention (FXI) in case of particularly strong appreciation pressures that would worsen deflation risks—FXI during periods of high, safe-haven capital inflows should not prevent trend appreciation of the franc and should be a complement rather than a substitute for other policy adjustments, such as rebalancing the fiscal-monetary policy mix. The SNB should continually review its monetary framework and tools, especially in light of the COVID-19 experience, to consider whether adjusting or extending targets and instruments—including a wider array of assets for quantitative easing, if needed—would help respond to new challenges. A review of greater "home bias" of Swiss investors over the past decade may identify actions to help ease appreciation pressures.

59. While the financial sector entered the COVID-19 crisis with strong buffers, continued close monitoring of asset quality and risks is warranted. Banks have incurred limited losses so far, but asset-quality deterioration is a risk. Deactivation of the sectoral CCyB was appropriate, but should remain temporary, in light of potential adverse real estate market developments. Residential property price risks should be monitored, especially as income support is withdrawn, along with commercial real estate risks, given negative pandemic effects and possible changes in occupancy, rents, and valuations. Self-regulation may not be sufficiently timely or stringent, and new macro-prudential tools may be needed, along with sufficient resources for high-quality data collection and oversight, including of fintech activities. Financial firms have reacted to negative interest rates and low margins by reducing costs and seeking higher returns. The authorities are rightly monitoring risk controls and buffers and should take early action if needed.

60. Efforts should continue to address major structural challenges. Labor market policies should remain protective in the near term to prevent scarring and inequality (contact-intensive sectors, lower-skilled workers). Crisis-related support via the STWP, compensation for self-employed, and unemployment benefits should remain until recovery is sustained. Policies will need to increasingly support mobility and flexibility, given structural changes that are being accelerated by COVID-19. Keeping support measures too long may impede transformation. The pension system is not well-aligned with demographic or economic trends, and gaps will grow without decisive reforms. Progress has been made to advance reforms, but more far-reaching actions are needed, including on retirement ages, conversion rates, and pension fund arrangements. An ambitious new climate strategy was approved in January. To meet new emissions targets, substantial investment will be required in energy, transportation, and buildings. A clear, monitorable action plan is needed to support the strategy and address gaps and risks; consideration should be given to increasing or accelerating investments to help ensure that Switzerland meets its ambitious targets and retains competitiveness.

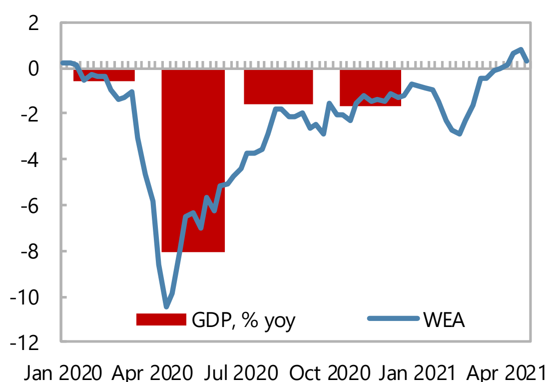
61. It is recommended that the next Article IV consultation take place on the regular 12-month cycle.

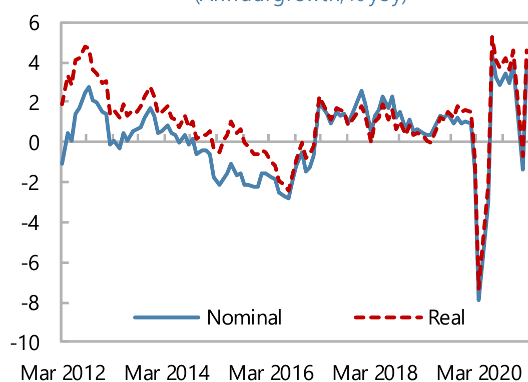
Figure 1. Switzerland: COVID-19 Pandemic

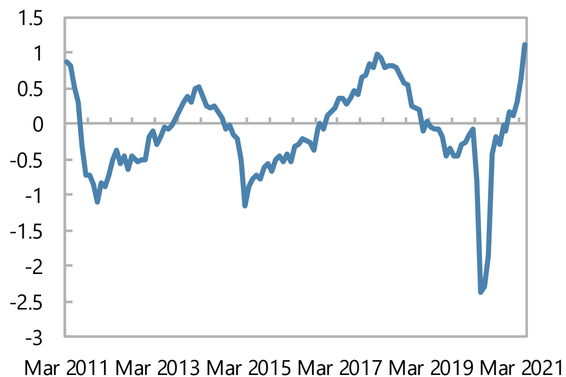


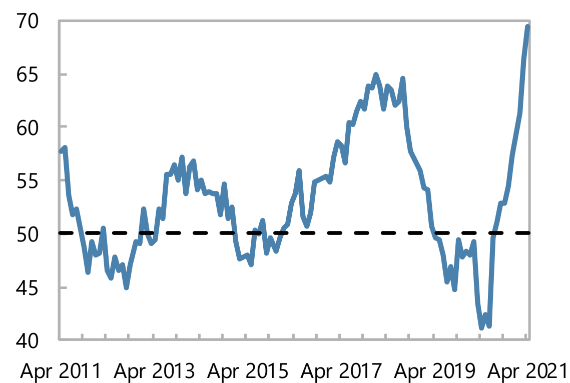
Sources: Haver Analytics; Bloomberg; IMF staff calculations.

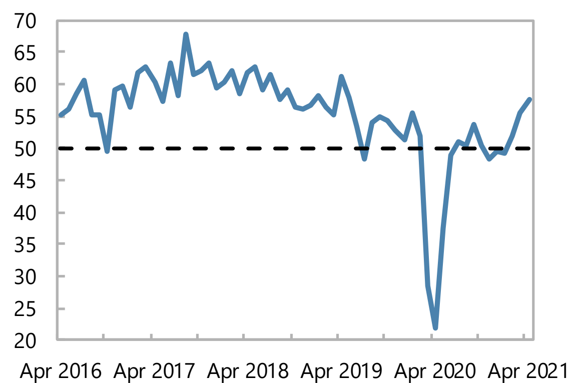
Figure 2. Switzerland: High Frequency and Leading Economic Indicators





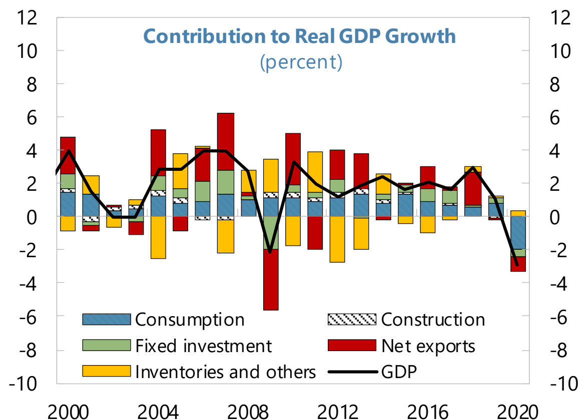


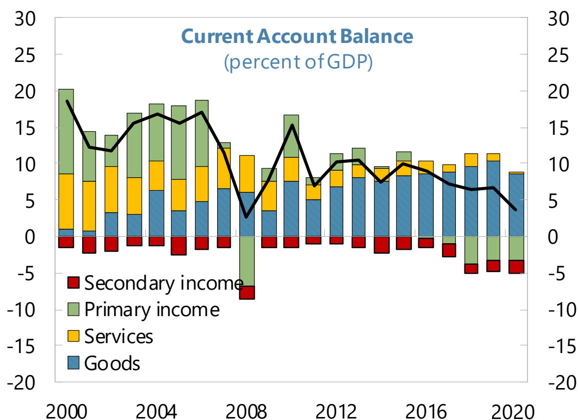


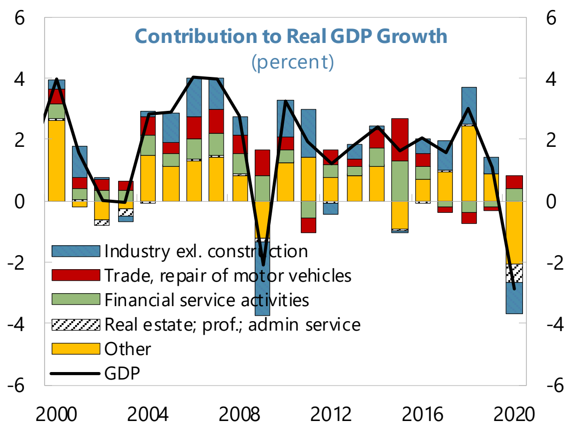


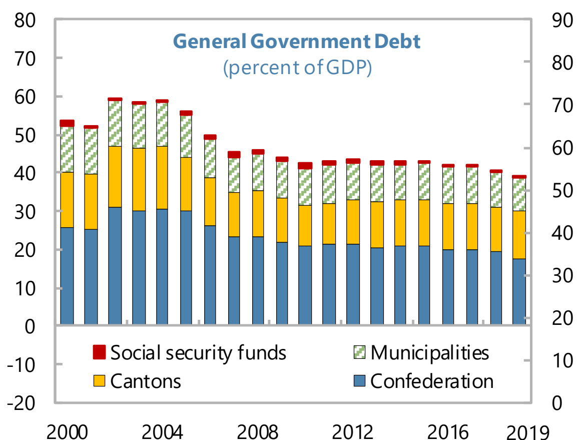
Sources: Haver Analytics; SECO.

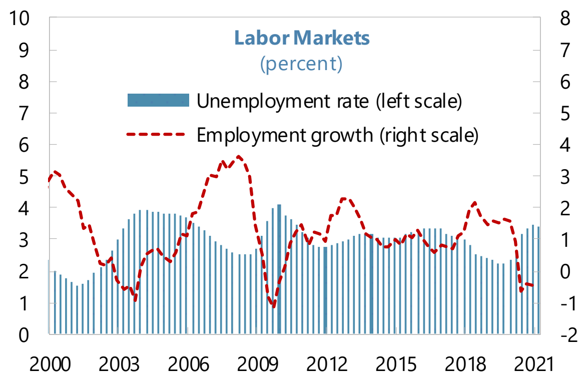
Figure 3. Switzerland: Key Macroeconomic Indicators, 2000–21

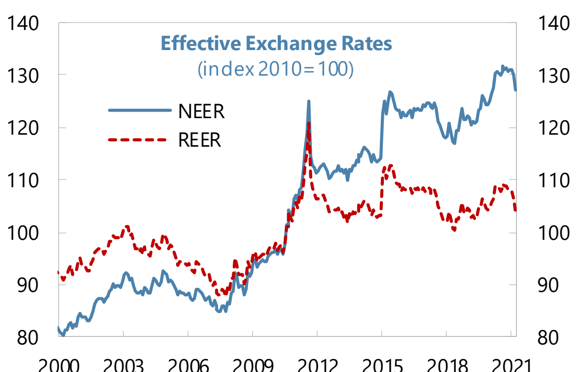






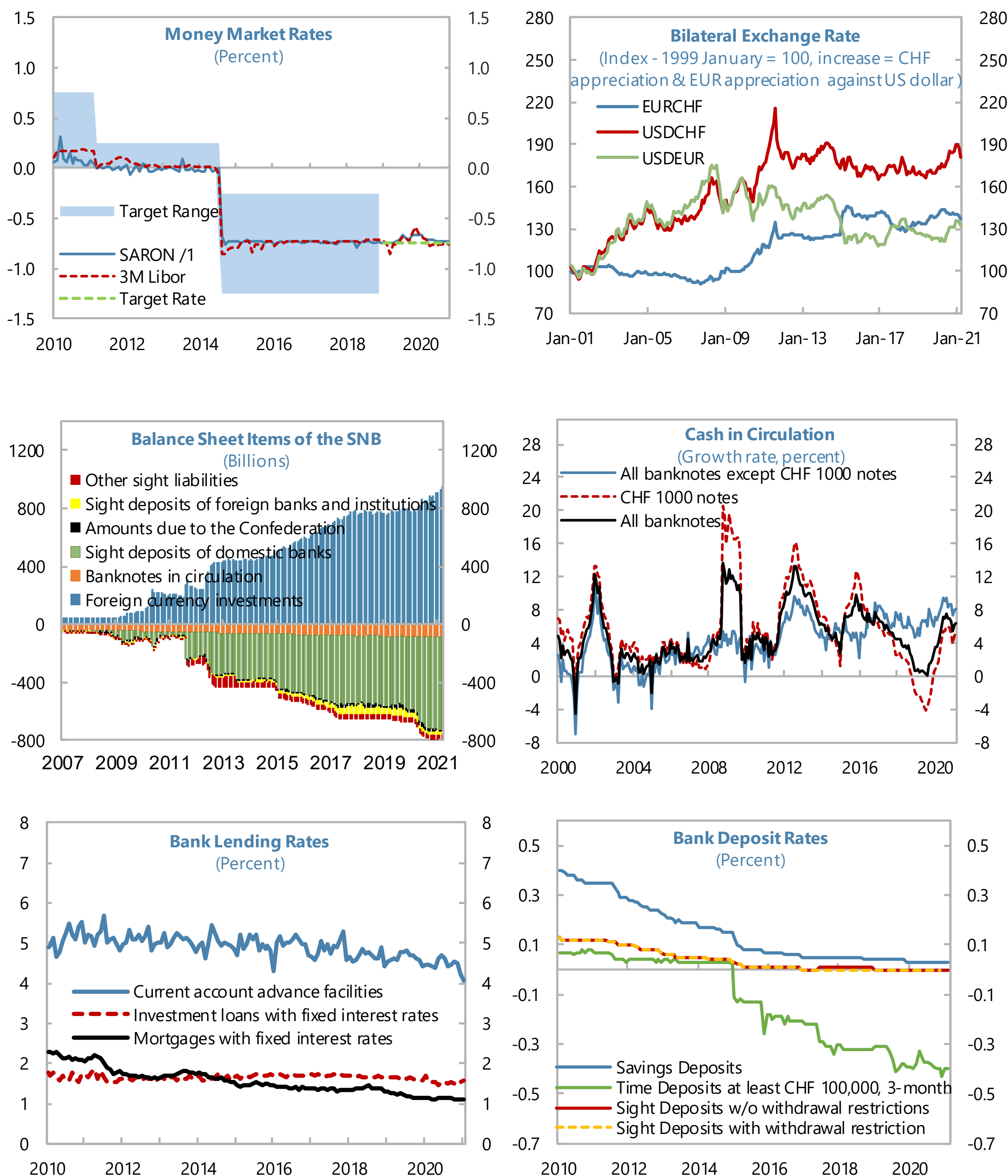






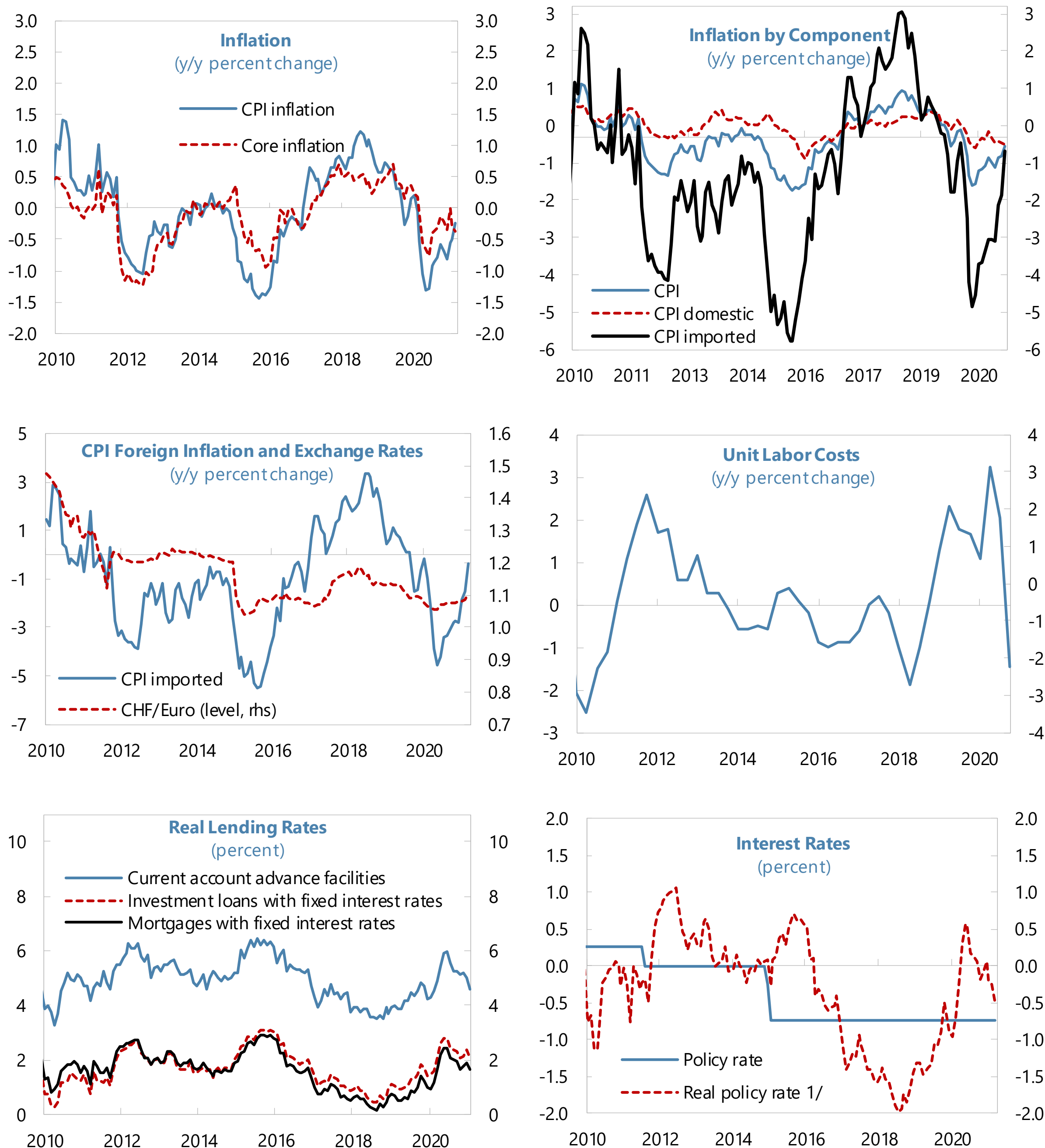
Sources: Haver Analytics; Federal Finance Administration; Information Notice System; State Secretariat for Economic Affairs; and Swiss National Bank.

Figure 4. Switzerland: Monetary Policy, 2000–21



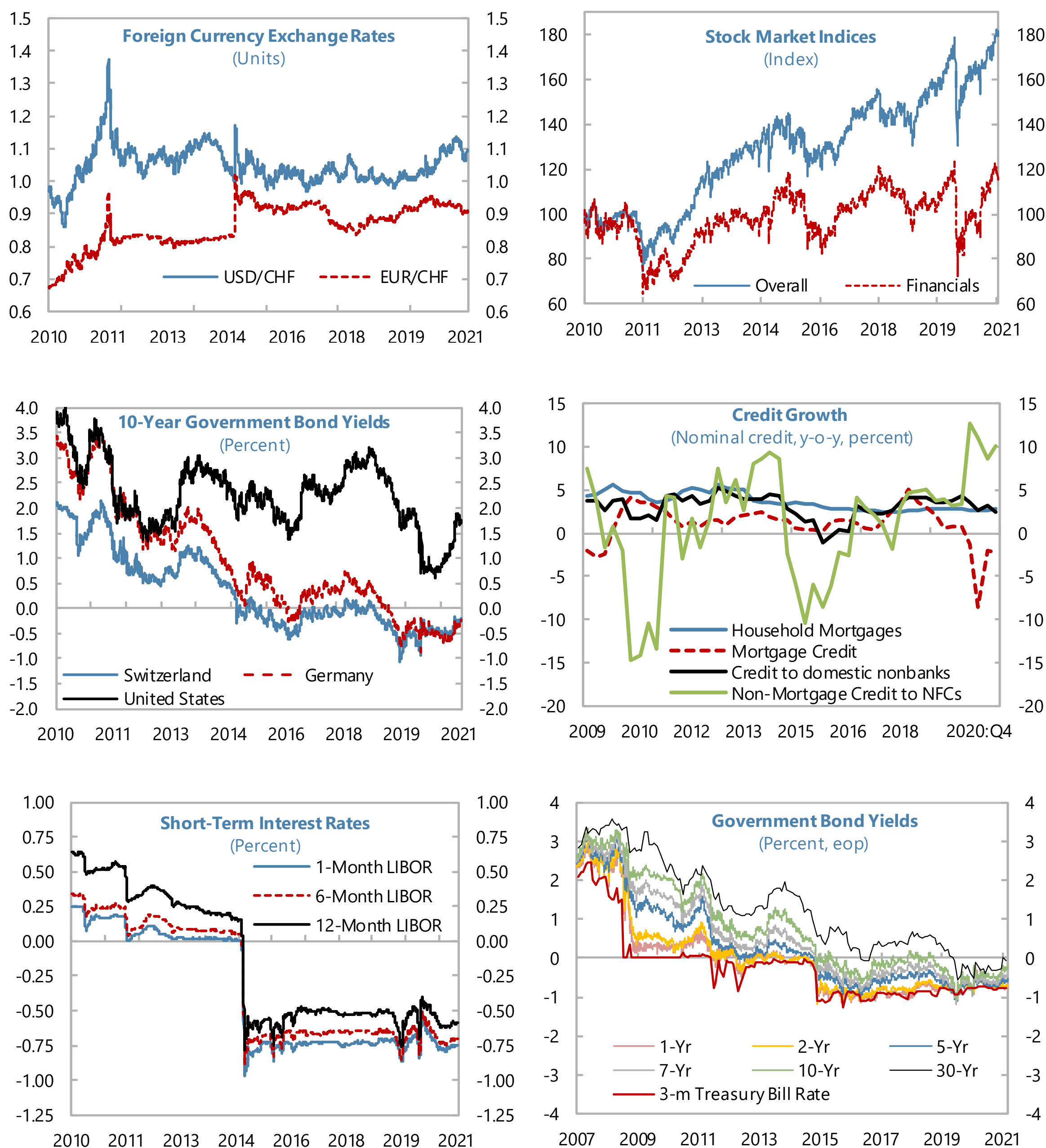
Sources: Swiss National Bank; Bloomberg Finance L.P; Haver; and IMF staff calculations.
1/ SARON (Swiss Average Rate Overnight) is an overnight average rate referencing the Swiss Franc interbank repo market.

Figure 5. Switzerland: Selected Inflation and Monetary Indicators, 2010–21



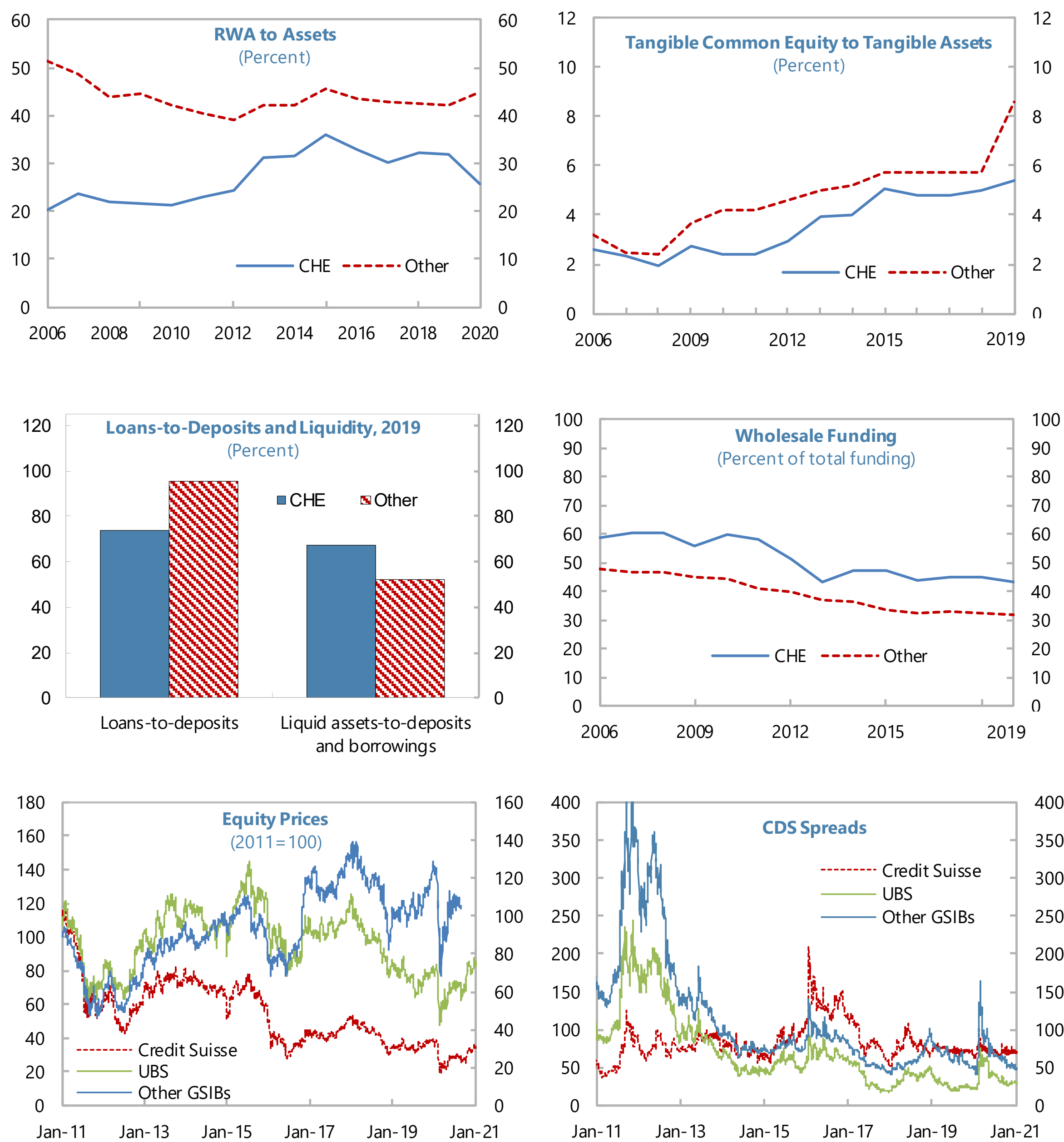
Sources: Haver Analytics; Swiss Federal Statistics Office; and Swiss National Bank.
1/ Nominal rate minus inflation.

Figure 6. Switzerland: Selected Financial Indicators, 2007–21



Sources: Thomson Reuters Datastream; Haver; and IMF staff calculations.

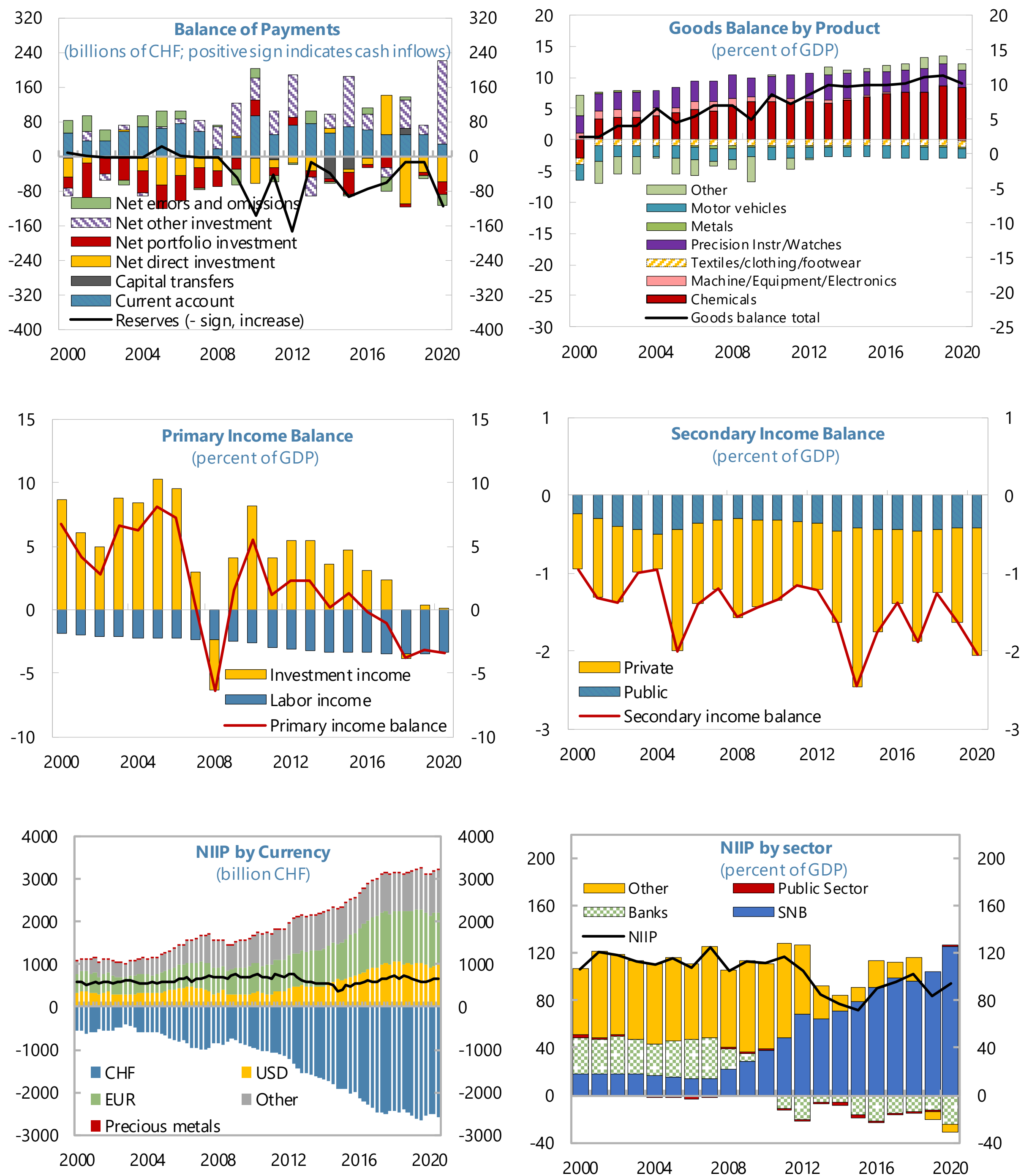
Figure 7. Switzerland: Indicators for Global Systemic Banks, 2006–21 1/



Sources: Thomson Reuters Datastream database; S&P Global Market Intelligence database; and IMF staff calculations.

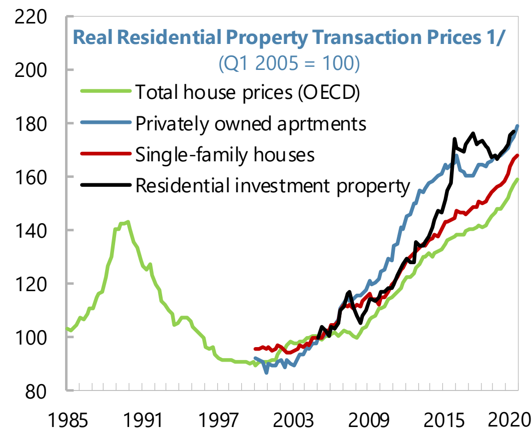
1/ Switzerland numbers are for Credit Suisse and UBS. "Other"includes Citigroup, Deutsche Bank, HSBC, JP Morgan Chase, Barclays, BNP, Bank of America, New York Mellon, Goldman Sachs, Mitsubishi, Morgan Stanley, Royal Bank of Scotland, Bank of China, BBVA, BPCE, Crédit Agricole, ING, Mizuho, Nordea, Santander, Société Générale, Standard Chartered, State Street, Sumitomo, UniCredit, Wells Fargo, Commerzbank, and Lloyds.

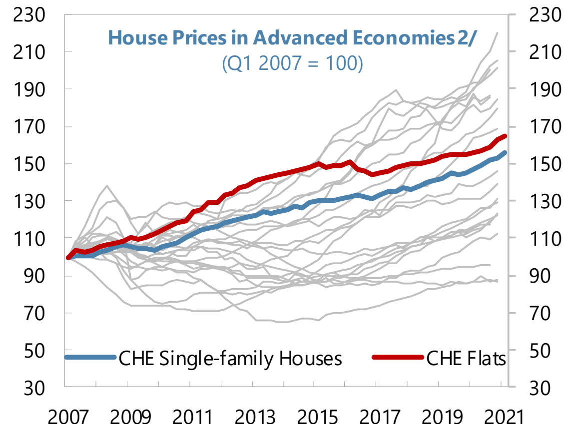
Figure 8. Switzerland: External Accounts, 2000–20

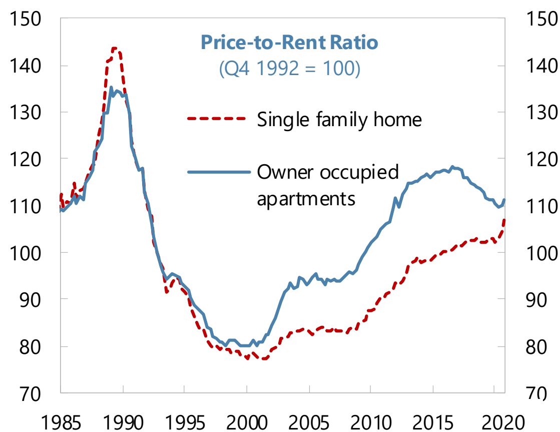


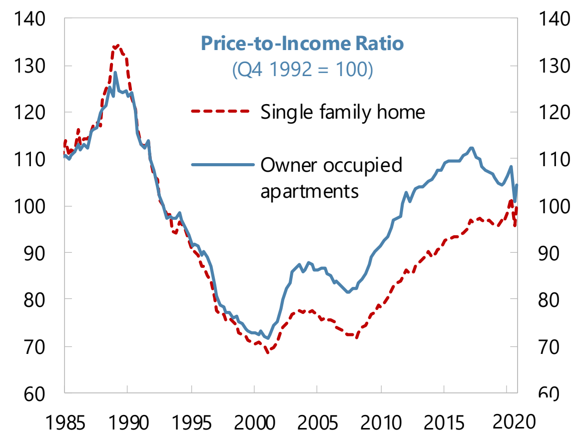
Sources: Swiss National Bank; World Development Indicators database; and Haver Analytics.

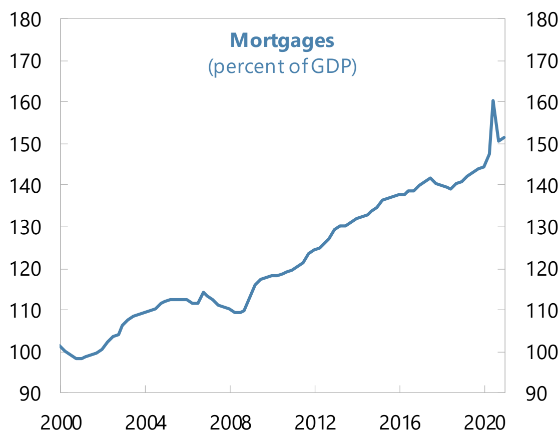
Figure 9. Switzerland: Housing Markets, 1985–20

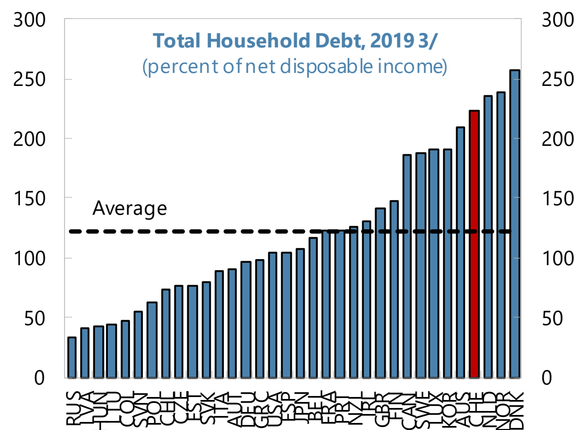












Sources: Haver Analytics; BIS IMF Global House Price Index; OECD; State Secretariat for Economic Affairs; EMF; Swiss National Bank; Wuest and Partner; and IAZI.
1/ Data on privately owned apartments, single-family houses, and residential investment property provided by Wuest Partner and IAZI.
2/ Shown in the chart are selected EU members and other advanced economies, including AUT, AUS, BEL, CAN, CHE, CHE, CYP, DEU, DNK, ESP, FRA, GBR, HRV, HUN, ITA, LTU, LUX, NLD, NZL, SWE, SVN, SVK, and USA. For other countries, shown in the chart are price indices for all types of dwellings
3/ 2018 data for RUS, COL, POL, CHL, USA, JPN, NZL, LUX, NOR.

Table 1. Switzerland: Selected Economic Indicators, 2018–26

	2018	2019	2020	2021	2022	2023	2024	2025	2026
				Staff projections					
Real GDP (percent change)	3.0	1.1	-3.0	3.5	2.8	1.4	1.8	1.2	1.8
Total domestic demand	1.2	1.4	-2.0	3.4	2.1	1.4	1.2	1.2	1.2
Private consumption	0.8	1.4	-4.5	4.2	2.4	1.2	1.1	1.1	1.1
Public consumption	0.9	0.9	2.9	1.8	1.0	1.0	1.0	1.0	1.0
Gross fixed investment	0.8	1.2	-1.7	3.0	2.7	1.9	1.6	1.5	1.5
Inventory accumulation 1/	0.3	0.1	0.6	0.1	-0.2	0.0	-0.1	0.0	-0.1
Foreign balance 1/	2.0	-0.1	-1.3	0.5	1.0	0.2	0.8	0.2	0.8
Nominal GDP (billions of Swiss francs)	720.1	727.6	701.8	727.8	750.7	765.5	784.8	800.8	821.7
Savings and investment (percent of GDP)									
Gross national saving	31.2	31.2	30.6	32.9	33.5	33.6	34.0	34.0	34.3
Gross domestic investment	24.5	24.5	26.8	26.2	26.0	26.3	26.5	26.8	26.8
Current account balance	6.7	6.7	3.8	6.7	7.5	7.2	7.5	7.2	7.5
Prices and incomes (percent change)									
GDP deflator	0.7	-0.1	-0.6	0.2	0.3	0.5	0.7	0.8	0.8
Consumer price index (period average)	0.9	0.4	-0.7	0.1	0.3	0.8	0.9	1.0	1.0
Consumer price index (end of period)	0.7	0.2	-0.8	0.1	0.6	0.7	1.0	1.0	1.0
Nominal hourly earnings	0.5	0.9	0.7	0.2	0.5	0.5	0.5	0.5	0.5
Unit labor costs (total economy)	-0.9	1.3	-2.6	-3.6	-1.3	0.4	-0.3	0.1	-0.5
Employment and slack measures									
Unemployment rate (in percent)	2.5	2.3	3.1	3.5	3.4	3.2	3.0	3.0	3.0
Output gap (in percent of potential)	1.7	1.6	-2.9	-1.3	0.0	0.1	0.1	0.1	0.0
Capacity utilization	73.8	74.6	71.8	…	…	…	…	…	…
Potential output growth	1.8	1.8	0.0	2.9	1.8	1.1	1.2	1.3	1.5
General government finances (percent of GDP)									
Revenue	32.6	32.9	33.6	33.2	33.0	33.0	33.0	33.0	33.0
Expenditure	31.3	31.5	36.2	36.6	33.7	33.1	33.1	33.0	33.0
Balance	1.3	1.4	-2.6	-3.4	-0.7	-0.1	-0.1	0.0	0.0
Cyclically adjusted balance	0.9	1.2	-1.8	-2.7	-0.3	0.1	0.0	0.0	0.0
Gross debt 2/	39.2	39.8	42.9	45.3	44.5	43.8	42.8	42.1	41.2
Monetary and credit (percent change, average)									
Broad money (M3)	3.2	0.8	6.5	…	…	…	…	…	…
Domestic credit, non-financial	4.0	4.2	2.4	…	…	…	…	…	…
Three-month SFr LIBOR	-0.7	-0.7	-0.7	…	…	…	…	…	…
Yield on government bonds (7-year)	-0.2	-0.7	-0.6	…	…	…	…	…	…
Exchange rates (levels)									
Swiss francs per U.S. dollar (annual average)	1.0	1.0	0.9	…	…	…	…	…	…
Swiss francs per euro (annual average)	1.2	1.1	1.1	…	…	…	…	…	…
Nominal effective rate (avg., 2000=100)	120.1	123.1	130.1	…	…	…	…	…	…
Real effective rate (avg., 2000=100) 3/	103.1	104.1	108.1	…	…	…	…	…	…

Sources: Haver Analytics; IMF's Information Notice System; Swiss National Bank; and IMF Staff estimates.

1/ Contribution to growth. Inventory accumulation also includes statistical discrepancies and net acquisitions of valuables.

2/ Reflects new GFSM 2001 method, which values debt at market prices. Calculated as the sum of Federal, Cantonal, Municipal and Social security gross debts.

3/ Based on relative consumer prices.

Table 2. Switzerland: Balance of Payments, 2016–26

	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
						Staff projections					
	(In billions of Swiss francs, unless otherwise indicated)										
Current account	**62**	**50**	**48**	**49**	**27**	**49**	**56**	**55**	**59**	**58**	**62**
Goods balance	60	63	72	75	64	69	74	75	76	76	77
Exports	322	323	339	345	334	355	372	389	407	426	446
Imports	261	260	267	270	270	286	299	315	332	350	369
Service balance	13	7	13	9	1	2	4	2	5	3	5
Net primary income	-2	-7	-28	-23	-24	-9	-8	-9	-8	-8	-8
Net secondary income	-9	-13	-9	-12	-14	-14	-13	-13	-13	-13	-13
Private capital and financial account	**67**	**22**	**82**	**35**	**4**	**52**	**58**	**58**	**61**	**60**	**64**
Capital transfers	-5	1	14	-3	0	2	1	1	1	1	1
Financial account	72	21	68	38	4	51	57	56	60	59	63
Net foreign direct investment	16	-90	109	35	60	26	43	35	39	37	38
Net portfolio investment	5	26	10	6	30	15	23	19	21	20	20
Net financial derivatives	8	-1	4	2	-9	1	-4	-2	-3	-2	-3
Net other investment	-35	24	-69	-21	-194	8	-5	4	3	4	7
Change in reserves	77	61	13	16	117	0	0	0	0	0	0
Net errors and omissions	**15**	**-30**	**6**	**-8**	**-23**	**0**	**0**	**0**	**0**	**0**	**0**
	(In percent of GDP, unless otherwise indicated)										
Current account	**9.0**	**7.2**	**6.7**	**6.7**	**3.8**	**6.7**	**7.5**	**7.2**	**7.5**	**7.2**	**7.5**
Goods balance	8.8	9.1	10.0	10.3	9.1	9.5	9.8	9.8	9.6	9.5	9.4
Exports	46.9	46.6	47.1	47.4	47.5	48.8	49.6	50.9	51.9	53.2	54.3
Imports	38.1	37.5	37.2	37.1	38.4	39.3	39.8	41.1	42.3	43.7	44.9
Service balance	1.8	1.1	1.8	1.2	0.1	0.3	0.6	0.3	0.6	0.4	0.6
Net primary income	-0.2	-1.0	-3.8	-3.2	-3.4	-1.2	-1.1	-1.1	-1.0	-1.0	-1.0
Net secondary income	-1.4	-1.9	-1.2	-1.6	-2.0	-1.9	-1.8	-1.7	-1.6	-1.6	-1.6
Private capital and financial account	**9.8**	**3.1**	**11.4**	**4.9**	**0.6**	**7.2**	**7.7**	**7.5**	**7.8**	**7.5**	**7.7**
Capital transfers	-0.7	0.2	2.0	-0.3	0.0	0.2	0.1	0.1	0.1	0.1	0.1
Financial account	10.5	3.0	9.5	5.2	0.6	7.0	7.6	7.4	7.7	7.3	7.6
Net foreign direct investment	2.4	-12.9	15.2	4.8	8.5	3.6	5.7	4.5	5.0	4.6	4.6
Net portfolio investment	0.8	3.8	1.4	0.8	4.3	2.1	3.0	2.5	2.7	2.5	2.5
Net financial derivatives	1.1	-0.2	0.6	0.3	-1.3	0.1	-0.5	-0.2	-0.4	-0.3	-0.3
Net other investment	-5.0	3.5	-9.6	-2.9	-27.6	1.1	-0.6	0.6	0.4	0.5	0.8
Change in reserves	11.2	8.8	1.9	2.2	16.6	0.0	0.0	0.0	0.0	0.0	0.0
Net errors and omissions	**2.1**	**-4.4**	**0.8**	**-1.2**	**-3.2**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Memorandum items:											
Net IIP (in percent of GDP)	90.3	95.9	102.0	83.2	94.3	86.0	86.0	88.9	90.2	92.3	93.0
Official reserves											
(billions of U.S. dollars, end-period)	644.3	762.2	794.8	830.8	1003.9	…	…	…	…	…	…

Sources: Haver Analytics; Swiss National Bank; and IMF staff estimates.

Table 3. Switzerland: SNB Balance Sheet, 2012–20

	2012	2013	2014	2015	2016	2017	2018	2019	2020
	(Millions of Swiss francs; unless otherwise indicated)								
Assets									
Gold	50,772	35,565	39,630	35,467	39,400	42,494	42,237	49,111	55,747
Foreign currency reserves	432,209	443,275	510,062	593,234	696,104	790,125	763,728	794,015	910,001
IMF, international, and monetary assistance loans	7,332	6,834	6,664	6,486	5,903	5,577	5,889	6,026	7,121
Swiss franc repos	...	...	...	...	...	...	...	6,529	550
U.S. dollar repos	...	...	...	...	...	...	...	...	8,842
Swaps against Swiss francs	...	...	...	...	...	...	...	...	...
Money market, Swiss franc securities, other	9,121	4,709	4,845	4,965	5,095	5,110	5,214	11,805	26,159
Total assets	499,434	490,382	561,202	640,152	746,502	843,306	817,069	860,956	999,028
Liabilities									
Currency in circulation (banknotes)	61,801	65,766	67,596	72,882	78,084	81,639	82,239	84,450	89,014
Sight deposits	369,732	363,910	387,666	469,034	530,049	573,679	574,827	591,454	702,862
Repo, SNB bills and time liabilities	...	...	...	...	...	...	...	...	9,027
Foreign currency and other liabilities	9,825	12,682	19,635	37,183	53,841	50,821	39,770	17,970	14,175
Provisions and equity capital	58,075	48,023	86,305	61,053	84,527	137,168	120,232	167,083	183,951
Total liabilities	499,434	490,382	561,202	640,152	746,502	843,306	817,069	860,956	999,028
Memorandum items:									
Nominal GDP (billions of Swiss francs)	649	661	673	676	685	694	720	727	702
Balance sheet, percent of GDP	77.0	74.2	83.4	94.7	108.9	121.6	113.5	118.4	142.3
Banknotes, percent of total liabilities	12.4	13.4	12.0	11.4	10.5	9.7	10.1	9.8	8.9
Refinancing operations, percent of total assets	...	...	...	...	...	...	...	...	...
Provisions and equity capital, percent of total assets	11.6	9.8	15.4	9.5	11.3	16.3	14.7	19.4	18.4
Monetary base 1/	284,381	360,765	375,305	455,863	504,140	551,849	549,374	564,161	674,297

Sources: Swiss National Bank; and IMF staff estimates.

1/ Currency in circulation and sight deposits of domestic banks.

Table 4. Switzerland: General Government Finances, 2018–26

	2018	2019	2020	2021	2022	2023	2024	2025	2026
			Staff projections						
	(In billions of Swiss francs, unless otherwise specified)								
General government									
Revenue	234	239	236	241	248	253	259	264	271
Expenditure	225	229	254	266	253	253	259	264	271
Net lending/net borrowing	9	10	-18	-25	-5	-1	0	0	0
Confederation (Federal government) 1/									
Revenue	78	80	75	77	79	80	82	84	86
Expenditure	73	74	91	98	81	80	83	84	86
Net lending/net borrowing	5	6	-16	-21	-3	1	0	0	0
Cantons									
Revenue	95	97	91	93	95	97	100	102	104
Expenditure	93	94	100	110	98	99	100	102	104
Net lending/net borrowing	3	3	-3	-4	-2	-2	-1	0	0
Communes/municipalities									
Revenue	49	50	47	48	49	50	51	52	53
Expenditure	49	50	51	52	50	51	51	52	53
Net lending/net borrowing	0	0	-1	-1	-1	-1	0	0	0
Social security 2/									
Revenue	64	65	75	73	69	70	72	74	76
Expenditure	63	64	69	75	69	71	74	74	74
Net lending / net borrowing	1	1	5	1	1	1	1	0	0
General government gross debt 3/	282	289	301	329	334	335	336	337	339
Confederation (Federal government) 1/	133	137	146	169	171	169	169	171	172
Cantons	85	92	94	98	100	101	102	102	102
Communes/municipalities	65	61	62	63	64	64	64	64	64
Social security 2/	2	1	0	0	0	0	0	0	0
	(In percent of GDP)								
General government operations									
Revenue	32.6	32.9	33.6	33.2	33.0	33.0	33.0	33.0	33.0
Expenditure	31.3	31.5	36.2	36.6	33.7	33.1	33.1	33.0	33.0
Net lending/net borrowing	1.3	1.4	-2.6	-3.4	-0.7	-0.1	-0.1	0.0	0.0
Confederation (Federal government) 1/	0.7	0.8	-2.3	-2.9	-0.4	0.1	-0.1	0.0	0.0
Cantons	0.4	0.5	-0.4	-0.5	-0.3	-0.2	-0.1	0.0	0.0
Communes/municipalities	0.0	0.0	-0.1	-0.1	-0.1	-0.1	0.0	0.0	0.0
Social security	0.1	0.1	0.8	0.1	0.1	0.1	0.1	0.0	0.0
General government gross debt 3/	39.2	39.8	42.9	45.3	44.5	43.8	42.8	42.1	41.2
Confederation (Federal government) 1/	18.5	18.9	20.8	23.2	22.7	22.1	21.6	21.3	21.0
Cantons	11.8	12.7	13.4	13.4	13.3	13.3	13.0	12.8	12.4
Communes/municipalities	9.1	8.4	8.8	8.6	8.5	8.4	8.2	8.0	7.8
Social security 2/	0.2	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:									
Nominal GDP (billions of francs)	720	727	702	728	751	765	785	801	822
Output gap (percent)	1.7	1.6	-2.9	-1.3	0.0	0.1	0.1	0.1	0.0
General Government cyclically adjusted balance	0.9	1.2	-1.8	-2.7	-0.3	0.1	0.0	0.0	0.0

Sources: Federal Ministry of Finance; and IMF staff estimates.

1/ Includes the balance of the Confederation and extrabudgetary funds (Public Transport Fund, ETH, Infrastructure Fund, Federal Pension Fund).

2/ Includes old age, disability, survivors protection scheme as well unemployment and income loss insurance.

3/ Forcasted.

Table 5. Switzerland: General Government Operations, 2010–20

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
	(In billions of Swiss francs, unless otherwise specified)										
Revenue	198.4	204.2	205.3	210.3	212.5	220.5	221.4	229.9	234.5	239.3	236.3
Taxes	123.0	125.5	126.1	129.1	130.9	135.9	138.0	144.6	144.0	146.9	145.1
Taxes on income, profits, and capital gains	73.6	75.7	76.2	78.3	79.3	83.7	85.0	89.9	87.3	89.1	88.0
Taxes on goods and services	37.6	38.3	38.3	38.6	38.8	39.1	38.9	40.2	43.1	44.0	43.4
Taxes on property	10.0	9.8	9.9	10.4	10.9	11.2	12.0	12.4	11.5	11.8	11.6
Taxes on international trade and transactions	1.1	1.0	1.0	1.1	1.1	1.1	1.1	1.1	1.2	1.2	1.2
Social contributions	38.7	41.3	42.3	43.2	43.7	44.5	45.0	45.5	48.3	48.8	47.0
Grants	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Other revenue	36.5	37.2	36.6	37.8	37.6	39.8	38.2	39.5	42.0	43.4	43.9
Of which: property income	8.5	8.7	7.1	7.5	6.5	8.3	7.3	7.9	8.4	8.5	8.4
Expenditure	196.2	199.9	203.7	213.1	214.2	216.8	219.8	222.2	225.3	229.2	254.5
Expense	194.8	198.5	201.9	211.7	212.8	215.0	218.1	219.6	235.2	237.4	229.0
Compensation of employees	44.8	45.9	47.0	47.9	48.7	49.6	50.2	50.9	53.2	53.7	51.8
Purchases/use of goods and services	21.7	22.1	22.8	23.7	24.1	24.3	24.4	24.6	26.3	26.5	25.6
Interest expense	5.2	4.7	4.4	4.0	3.7	3.6	3.2	2.7	2.7	2.8	2.9
Social benefits	67.3	67.6	69.3	71.5	73.0	74.3	76.4	77.5	84.5	86.1	83.5
Expense n.e.c.	55.9	58.1	58.4	64.7	63.2	63.2	64.0	63.8	68.4	68.3	65.2
Net acquisition of nonfinancial assets	1.4	1.4	1.9	1.4	1.4	1.8	1.7	2.6	-9.9	-8.2	25.5
Net operating balance	3.6	5.7	3.4	-1.4	-0.2	5.5	3.3	10.3	-0.7	1.9	7.3
Net lending/borrowing	2.2	4.3	1.5	-2.8	-1.6	3.6	1.6	7.7	9.2	10.1	-18.2
Net acquisition of financial assets	-18.0	12.3	21.6	-5.2	42.0	-23.7	14.1	77.5	18.3	22.5	26.7
Net incurrence of liabilities	-20.2	7.9	20.1	-2.4	43.7	-27.3	12.5	69.8	9.2	12.5	44.9
	(In percent of GDP)										
Revenue	31.5	31.8	31.6	31.8	31.6	32.6	32.3	33.1	32.6	32.9	33.6
Taxes	19.5	19.6	19.4	19.5	19.5	20.1	20.1	20.8	20.0	20.2	20.7
Taxes on income, profits, and capital gains	11.7	11.8	11.7	11.9	11.8	12.4	12.4	13.0	12.1	12.3	12.5
Taxes on goods and services	6.0	6.0	5.9	5.8	5.8	5.8	5.7	5.8	6.0	6.0	6.2
Taxes on property	1.6	1.5	1.5	1.6	1.6	1.7	1.7	1.8	1.6	1.6	1.7
Taxes on international trade and transactions	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Social contributions	6.2	6.4	6.5	6.5	6.5	6.6	6.6	6.6	6.7	6.7	6.7
Other revenue	5.8	5.8	5.6	5.7	5.6	5.9	5.6	5.7	5.8	6.0	6.3
Expenditure	31.2	31.2	31.4	32.3	31.8	32.1	32.1	32.0	31.3	31.5	36.2
Expense	31.0	31.0	31.1	32.0	31.6	31.8	31.8	31.7	32.7	32.7	32.6
Compensation of employees	7.1	7.2	7.2	7.2	7.2	7.3	7.3	7.3	7.4	7.4	7.4
Purchases/use of goods and services	3.5	3.5	3.5	3.6	3.6	3.6	3.6	3.5	3.7	3.7	3.6
Interest expense	0.8	0.7	0.7	0.6	0.5	0.5	0.5	0.4	0.4	0.4	0.4
Social benefits	10.7	10.5	10.7	10.8	10.9	11.0	11.2	11.2	11.7	11.8	11.9
Expense n.e.c.	8.9	9.1	9.0	9.8	9.4	9.4	9.3	9.2	9.5	9.4	9.3
Net acquisition of nonfinancial assets	0.2	0.2	0.3	0.2	0.2	0.3	0.2	0.4	-1.4	-1.1	3.6
Net operating balance	0.6	0.9	0.5	-0.2	0.0	0.8	0.5	1.5	-0.1	0.3	1.0
Net lending/borrowing	0.4	0.7	0.2	-0.4	-0.2	0.5	0.2	1.1	1.3	1.4	-2.6
Net acquisition of financial assets	-2.9	1.9	3.3	-0.8	6.2	-3.5	2.1	11.2	2.5	3.1	3.8
Net incurrence of liabilities	-3.2	1.2	3.1	-0.4	6.5	-4.0	1.8	10.1	1.3	1.7	6.4

Source: Federal Ministry of Finance.

Table 6. Switzerland: Bank Soundness Indicators, 2011–20

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Capital adequacy										
Regulatory Tier I capital as percent of risk-weighted assets 1/	15.4	15.7	17.8	16.1	16.6	15.7	18.2	18.3	19.0	19.3
Regulatory Tier 1 capital as percent of assets	5.5	5.5	6.1	6.9	7.3	7.1	8.0	8.3	8.6	8.0
Non-performing loans										
Non-performing loans net of provisions as percent of tier I capital	5.4	5.0	4.5	3.7	3.8	3.9	3.0	3.2	3.0	3.5
Non-performing loans as percent of total gross loans	0.8	0.8	0.8	0.7	0.7	0.7	0.6	0.7	0.6	0.7
Return on assets	...	0.1	0.3	0.1	0.2	0.3	0.3	0.4	-0.1	0.0
Liquidity coverage ratio	33.9	35.4	47.4	47.4	140.3	152.7	150.9	158.3	160.6	179.2
Asset quality and exposure										
Non-performing loans as percent of gross loans	0.8	0.8	0.8	0.7	0.7	0.7	0.6	0.7	0.6	0.7
Sectoral distribution of bank credit to the private sector (percent)										
Households	67.3	66.9	66.2	66.6	67.6	67.4	67.6	67.2	66.9	66.1
Agriculture and food industry	0.8	0.8	0.8	0.8	0.9	0.9	0.9	0.9	0.9	0.8
Mining and Quarry	0.2	0.2	0.2	0.2	0.2	0.2	0.1	0.1	0.2	0.1
Manufacturing	3.2	3.0	2.6	2.4	2.2	2.1	2.1	2.1	2.0	2.0
Utilities	0.6	0.6	0.7	0.6	0.6	0.6	0.6	0.6	0.5	0.5
Construction	1.6	1.6	1.6	1.5	1.6	1.5	1.6	1.6	1.6	1.7
Retail	3.1	3.0	2.7	2.8	2.5	2.7	2.5	2.6	2.4	2.6
Hotels and restaurants / Hospitality sector	1.0	1.0	0.9	0.9	0.9	0.8	0.8	0.8	0.8	0.9
Transportation & Storage	0.8	0.8	0.8	0.8	0.8	0.8	0.7	0.8	0.7	0.7
IT, R&T	12.2	12.6	13.0	13.2	13.2	13.4	13.6	13.9	14.2	14.5
Finance and Insurance	5.0	5.2	5.7	5.3	4.8	4.7	4.7	5.0	5.4	5.7
Public Administration and Defence	1.7	1.7	2.3	2.3	2.3	2.3	2.0	1.9	1.8	1.7
Education	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Health & Social services	1.2	1.3	1.3	1.4	1.4	1.5	1.5	1.5	1.4	1.5
Art and Entertainment	1.0	1.0	0.9	0.9	0.9	0.9	0.9	1.0	1.0	1.0
Extraterritorial Organization	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Source: Swiss National Bank.

1/ Based on parent company consolidation. This consolidation basis equals the CBDI approach defined in FSI compilation guide plus foreign bank branches operating in Switzerland, and minus overseas deposit-taking subsidiaries.

Annex I. Status of Previous Article IV Recommendations

2019 Article IV Recommendations	Policy Actions
Fiscal Policy	
Reduce structural overperformance through operational refinements to the debt-brake rule.	The Federal Council (FC) has proposed to simplify the procedures for supplementary budgets to reduce "safety margins." New accounting changes to introduce accruals were also proposed. Efforts have been made to refine revenue forecasts to limit revenue overperformance (which results in lower planned spending and surplus bias). Adjustments to the asymmetric operation of the debt-brake rule were considered but rejected.
Redress fiscal-monetary policy imbalances. In case downside risks to activity materialize, fiscal policy should contribute more decisively to supporting growth.	The authorities have taken strong, swift, and sustained fiscal measures in response to the COVID-19 pandemic, with coordinated support from monetary policy and regulatory adjustments.
Monetary Policy	
Foreign exchange intervention (FXI) should be reserved mainly for leaning-against-the-wind of large safe-haven pressures that would otherwise cause excessive volatility in inflation and output, but while preserving the trend appreciation.	The COVID-19 pandemic triggered large safe-haven inflows. In response, the SNB purchased CHF 90 billion foreign exchanges in H1:2020, and another CHF 20 billion in H2:2020. Notwithstanding these FXIs, the franc appreciated by 6 percent and 4 percent, in nominal and real effective exchange rate terms, respectively.
Improve transparency of SNB operations with regular and timely publication of FXI data.	The SNB started to publish quarterly net FXI information from September 2020. Previously FXI data were only released on an annual basis.
Financial Sector Policy	
New targeted macroprudential measures are needed to restrain demand for high-risk mortgages on residential investment property.	A partial tightening of the self-regulation regime on mortgages for investment properties was recognized by FINMA in August 2019 and became effective in January 2020.
The toolkit for mandated measures should be expanded, supported by a framework with enhanced expectations to act.	No new mandated tools have been introduced, and no formal changes have been made to the decision-making framework on accountability or expectations to act.
The authority and independence of the financial supervisor should be further strengthened to be commensurate with the very large and complex financial sector and institutions that it supervises.	A new Ordinance to the Financial Market Supervision Act came into force in February 2020. But no steps have been taken to lessen the Federal Council's oversight of FINMA or to strengthen FINMA's autonomy, governance, and accountability.
Structural Reforms	
Eliminate remaining gaps in international commitments and in compliance with international standards, and implement the corporate income tax reform expeditiously.	The Federal Act on Tax Reform and AHV Financing (TRAF) was approved in May 2019 and became effective in January 2020. Many recommendations in the 2018 OECD Working Group on Bribery (WGB) Phase 4 evaluation have been implemented, but some reforms (e.g., maximum fines for legal persons, whistleblower protection) have fallen short. AMT/CTF procedures have been enhanced in some areas (sanctions, bearer shares, exchange of FIU information and mutual legal assistance).
Better adapt to demographic trend and technological changes, including by raising the retirement age, amending the pension system, continuing to welcome foreign workers, tailoring education to facilitate life-long learning, and ensuring social safety nets are compatible with new work arrangements.	Pension reform effects have continued for both Pillar 1 and Pillar 2. Additional support measures for childcare services have been adopted, with the aim to raise labor force participation. A new package of measures was adopted in 2019 to strengthen the promotion of the domestic labor force potential, with a special focus on older people, including those who have exhausted their unemployment benefits, and job seekers who are difficult to place.
Source: IMF staff.	

Annex II. Status of Recommendations from the 2019 FSAP

	Recommendation and Responsible Authority	Timing*	Implementation[1]
1.	Strengthen FINMA's autonomy, governance, and accountability, and preserve the primacy of its prudential mandate (FDF/FINMA; ¶32–34)	C	A new Ordinance to the Financial Market Supervision Act came into force in February 2020. But steps have not been taken to lessen the Federal Council's oversight of FINMA or to strengthen FINMA's autonomy, governance, and accountability.
2.	Increase resources for high-quality data gathering and analysis of financial system risks, especially for the fast-moving fintech sector, and to advance recovery and resolution planning (SNB/FINMA/OAK BV; ¶15, ¶29, ¶36 ¶41, ¶51, ¶54, ¶58, ¶63)	MT	Progress has been made by FINMA in some areas (fintech, asset management, recovery and resolution planning, FMI), but gaps remain in all areas identified by the FSAP.
Financial Stability Policy Framework			
Macroprudential			
3.	Expand the macroprudential toolkit with mandated supply- and demand-side tools, and strengthen accountability and expectations to act in decision-making (SNB/FINMA/FDF; ¶35–36)	ST	A partial tightening of the self-regulation regime on mortgages for investment properties was recognized by FINMA in August 2019 and became effective in January 2020. New mandated tools have not been introduced, and changes have not been made to the decision-making process to strengthen accountability and expectations to act.
Banking			
4.	Ensure that FINMA—rather than banks—contracts and pays directly for supervisory audits using 'audit-level' practices in critical areas (FDF/FINMA; ¶38)	ST	No progress.
5.	Focus supervisory audits and increase FINMA's risk-based on-site inspections (FINMA; ¶38)	ST	FINMA has made progress in implementing a more risk-based on-site inspection approach. The number of on-site inspections (supervisory reviews and deep dives) by FINMA has increased over time.
6.	Strengthen assessments of key risk management and control practices (FINMA; ¶39)	MT	Progress has been made with establishment of a new cross-sectoral governance barometer and dedicated measures for outlier institutions. Additional measures are needed, particularly to incentivize banks to take the appropriate remedial action to address material risk management and control weaknesses.

	Recommendation and Responsible Authority	Timing*	Implementation[1]
Financial Market Infrastructures			
7.	Strengthen recovery and resolution planning for financial market infrastructures (FMIs) (FINMA/SNB/SIX; ¶49)	I	Limited progress has been made in ensuring that recovery arrangements support effectively continuity of FMI critical services, including in extreme scenarios. There has been some progress in developing resolution strategies. There has been limited progress in developing firm-specific resolution plans.
8.	Improve independence of FMIs' governance arrangements (SNB/SIX; ¶48)	ST	No progress. Analysis and discussions are ongoing.
Asset Management			
9.	Better monitor and manage concentration risk of regulated funds, and empower FINMA to impose administrative fines (FDF/FINMA; ¶52–53)	ST	Legislation is pending on additional tools for risk monitoring and managing. Discussions on additional monitoring, including of concentration risks, are ongoing. The authorities do not intend to empower FINMA to impose fines.
Fintech and Crypto-Assets			
10.	Enhance the monitoring of activities and address regulatory gaps (FDF/FINMA; ¶58–59)	ST	No progress.
Financial Safety Net and Crisis Management			
11.	Enhance, expand, and expedite recovery and resolution planning, including resolvability (FDF/FINMA; ¶63–66)	ST	Partial progress has been made, largely on resolvability of G-SIBs and D-SIBs. No progress on expanding recovery and resolution planning.
12.	Thoroughly reform the DIS with a public DIA that is included in the crisis management framework, ex-ante DIS funding, and the authority to use deposit insurance funds for resolution funding, subject to safeguards (FDF; ¶67–68)	MT	No progress. The current reforms fall short of international norms on several levels. The authorities do not intend to overhaul the DIS as recommended.
* C = Continuous; I = Immediate (within one year); ST = Short Term (within 1–2 years); MT = Medium Term (within 3–5 years).			
[1] Based on information provided by the Swiss authorities.			

Annex III. Gold Trade during the COVID-19 Pandemic

1. **In 2020, Switzerland recorded a gold trade deficit of CHF15.3 billion, 2.2 percent of GDP, down from a modest surplus of CHF1 billion in 2019**. Switzerland is a leading gold importer and exporter, with a small annual net balance in value terms since 2013 (differences in import and export prices reflect value added and margins of refineries). In 2020, imports grew much faster than exports. In 2020, Swiss gold exports to India and China delined, but exports surged to the U.S. and Germany.

2. **Unlike other goods, gold trade is driven by both real and financial investment demand, and may respond differently to shocks**. Real demand (e.g., jewelry, industrial inputs) may decline if incomes are strongly affected. At the same time, interest in safe-haven assets may push up financial investment demand.

3. **Switzerland's imports of gold may be decomposed into three parts: (i) inputs for gold exports; (ii) domestic real demand (jewelry, luxury watches, inputs for other products such as electronics), and (iii) domestic financial investment demand**. As Switzerland does not produce or import much gold ore, component (i) should be close, in quantity, to gold exports (although there may be occasional build-up and draw down of inventories). While there are insufficient data to clearly separate domestic real (ii) and financial investment (iii) demand, their different tendencies in response to shocks—real demand tends to drop while financial investment demand rises—makes it possible to estimate how much of the increase of imports in 2020 was driven by financial investment demand.

4. **We estimate that over half of the 2019/20 gold trade balance shift—around 1.4 percent of GDP—was driven by an**

Top 10 Gold Importers and Exporters in 2019

USD bil.	Imports	USD bil.	Exports
GBR	70.8	**CHE**	**61.9**
CHE	**60.6**	HKG	25.2
CHN	43.9	GBR	23.3
ARE	32.1	ARE	19.1
IND	31.2	USA	17.2
HKG	14	AUS	16.2
TUR	11.3	CAN	15.7
SGP	10.1	SGP	11.6
USA	9.7	THA	7.3
THA	6.2	PER	6.8

Source: UN COMTRADE

Gold Trade, 2012-2020

		2012	2013	2014	2015	2016	2017	2018	2019	2020
Quantity	Exp.	1.6	2.9	1.8	1.9	2.1	1.7	1.6	1.4	1.3
1000 tons	Imp.	2.3	3.1	2.2	2.6	2.8	2.4	2.3	2.1	2.2
	Bal.	-0.65	-0.24	-0.42	-0.65	-0.72	-0.72	-0.68	-0.70	**-0.88**
Value	Exp.	82.0	120.7	67.9	69.1	80.6	66.6	62.6	61.5	67.2
CHF bil.	Imp.	89.4	110.2	65.4	68.6	82.5	69.6	62.1	60.6	82.6
	Bal.	-7.4	10.5	2.5	0.5	-1.8	-3.0	0.4	1.0	**-15.3**
Average price	Exp.	50.4	42.3	37.2	35.9	39.1	39.6	39.6	43.9	52.4
(CHF/g)	Imp.	39.2	35.6	29.1	26.7	29.7	29.0	27.5	28.8	38.1

Source: Swiss Federal Customs Administration

Gold Exports by Destination

Exports	Value			Quantity		
	2015-19	2020	%yoy	2015-19	2020	%yoy
India	16.1	9.4	-41.6	415.7	178.9	-57.0
China	13	1.5	-88.1	331.1	30.5	-90.8
Hong Kong	10.4	1.3	-87.8	271.5	27.0	-90.1
UK	8.7	7.4	-15.1	203.9	132.6	-35.0
France	2.7	3.1	14.6	66.4	58.3	-12.2
Singapore	2.7	1.5	-45.7	69.5	28.0	-59.7
Germany	2.5	4.7	86.9	63.9	89.2	69.6
Thailand	1.7	1.1	-31.0	42.1	21.2	-49.7
Turkey	1.6	4.1	163.9	39.1	77.3	97.5
Italy	1.6	1.1	-30.6	42.4	36.0	-15.0
US	1.3	27.4	2047.8	31.7	516.6	1531.4
ROW	6.2	4.6	-25.9	159.5	86.5	-45.8
Total	68.5	67.2	9.3	1736.8	1282.1	-8.5

Note: 2015-19 denotes the 5-year average; ROW is the rest of the world.

Source: Swiss federal customs administration

increase of demand and imports by Swiss financial investors. Having a clearer picture is important to assess the strength of the external current account and the durability of developments affecting it. This was estimated by decomposing Switzerland's imports of gold into three parts by purpose: (i) inputs for gold exports; (ii) domestic real demand (e.g., for jewelry and for inputs into production other goods like luxury watches or automobile components), and (iii) domestic financial demand. As Switzerland does not produce or import much gold ore, (i) should be close, in quantity, to Switzerland's gold exports. Although there is not adequate information available publicly to separate domestic real and financial demand for gold precisely, their different tendencies in response to shocks—real demand tends to drop while financial investment demand tends to rise—make it possible to estimate potentially how much of the increase of net gold imports in 2020 was driven by financial demand. The estimate was based on the average net imports in recent non-crisis years ("regular" demand), the surge of net imports in 2020 ("extraordinary," for financial purposes), and the sharp decline of gold exports for real demand to most countries (besides Germany, Turkey and the U.S.) in 2020. The result of the estimations is around 1.4 percent of GDP worth of additional net imports of gold due to the crisis and increased Swiss financial investment demand.

Annex IV. External Sector Assessment

<table>
<tr><td colspan="8">Overall Assessment: Switzerland’s external position in 2020 was broadly in line with the level implied by medium-term fundamentals and desirable policies. However, this change from the previous assessment, where the external position was judged to be moderately stronger, is subject to higher than usual uncertainty related to recent large downward statistical revisions to historical current account balances.[1] The 2019 current account balance is now nearly 5 percentage points of GDP lower than estimated at the time of the 2020 ESR. The revisions suggest a weakening in the external position and add to uncertainty. Data and time will be needed to assess the durability of this downward shift in the external accounts, distinguishing transitory and COVID-19-related effects from structural impacts. A number of pandemic-influenced developments, especially concerning the trade and income accounts, are expected to unwind in the coming years. More broadly, the continued strength of Switzerland’s external balance sheet and macroeconomic policy mix are at odds with an assessment of the overall external position as weaker. Net foreign assets increased in 2020, with reserves now exceeding 130 percent of GDP, reflecting FX operations conducted for monetary policy reasons in the context of FX inflow surges rather than reserve accumulation or exchange rate management purposes. Policy buffers also remain strong, in particular, fiscal buffers, notwithstanding the comprehensive response to the pandemic. Overall, these circumstances suggest caution in assessing the external position.
Potential Policy Responses: Fiscal policy should continue to play a key role in responding to the pandemic and ensuring a strong and sustained recovery. Monetary policy should remain accommodative and directed at price stability; macroprudential policies should focus on reducing financial sector risks. FX intervention may be used to partially mitigate strong appreciation pressures that would otherwise push the economy further into deflation. The Swiss National Bank (SNB) should continually review its framework and tools, especially in light of the experience during COVID-19, to consider whether adjusting or extending targets, instruments, and communications would enable it to continue to respond effectively to new challenges. Medium-term policies should be geared to ensuring balanced domestic and external contributions to growth, while improving the public-private mix in financial outflows and thereby easing pressures on the franc. In the post-pandemic environment, fiscal policy should remain supportive, continuing—and enhancing or accelerating, where possible—efforts to foster green, digital transformation and productivity gains and to address important challenges (e.g., competitiveness, aging).</td></tr>
<tr><td>Foreign Asset and Liability Position and Trajectory</td><td colspan="7">Background. Switzerland is a major financial center with a positive NIIP of 94.2 percent of GDP and gross foreign asset and liability positions of 758 and 664 percent of GDP, respectively, at end-2020. The NIIP reflects both a history of large CA surpluses and valuation changes.[2] Valuation changes reflect fluctuations of exchange rates (ERs) and prices of securities and precious metals that interact with differences among assets and liabilities in terms of currencies and instruments.[3] Statistical revisions in 2020, to better account for foreign liabilities on FDI and portfolio equity investment, have involved large, downward adjustments in NIIP estimates for 2008–19. On the basis of the revised series, the NIIP rose in 2020 by 11 percentage points of GDP, mainly driven by an increase in reserve assets. Projections of the NIIP in 2021 and beyond are complicated by heightened uncertainty: because of the large gross positions and compositional differences among assets and liabilities, even modest changes in ERs, asset prices, and returns may have a material effect on the NIIP.
Assessment. Switzerland’s large gross liability position and the volatility of financial flows and investment returns present some risk, but this is mitigated by the large gross asset position and the Swiss franc denomination of about two-thirds of external liabilities.</td></tr>
<tr><td>2020 (% GDP)</td><td colspan="2">NIIP: 94.2</td><td>Gross Assets: 758.0</td><td>Res. Assets: 135.9</td><td colspan="2">Gross Liab.: 663.8</td><td>Debt Liab.: 205.2</td></tr>
<tr><td>Current Account (CA)</td><td colspan="7">Background. Switzerland’s CA surpluses averaged over 9 percent of GDP during 2010–19, although statistical revisions reflecting conclusion of the reporting calendar and improved coverage of domiciliary-company foreign liabilities led to downward revisions of surpluses for 2018–19. In 2020, the CA surplus decreased from 6.7 percent of GDP in 2019 to 3.8 percent. The decline likely reflected temporary shocks, especially related to COVID-19, such as weaker trade balances for gold and luxury watches and a larger drop in investment income receipts than expenses due to the relatively better performance of the Swiss economy in the pandemic. Other factors may persist. On balance, the CA position is likely to return towards 2018–19 levels in 2021, as the global economy recovers and the drag from temporary COVID-19-related shocks eases.
Assessment. The EBA CA norm of 5.6 percent of GDP is slightly lower than last year’s norm. Based on a cyclically-adjusted CA surplus of 3.9 percent and the norm, the overall EBA-estimated CA gap equaled -1.6 percent of GDP in 2020. Domestic policy gaps account for -1.1 percentage points of the gap and include excessive private sector credit (-0.7) and fiscal overspending (-0.3), while policy gaps in the rest of the world contribute 2.4 pp. Adjustments for: (i) specific factors relevant for Switzerland that are not treated appropriately in the income account—namely valuation losses on fixed-income securities arising from inflation (-2.8) and retained earnings on portfolio equity investment (-0.6), and (ii) transitory impacts of the COVID-19 pandemic (1.9), widened the gap to -3.1 percent of GDP (± 2 percentage points).[4,5]</td></tr>
<tr><td>2020 (% GDP)</td><td>CA: 3.8</td><td>Cycl. Adj. CA: 3.9</td><td>EBA Norm: 5.6</td><td>EBA Gap: -1.6</td><td>COVID-19 Adj.: 1.9</td><td>Other Adj.: -3.4</td><td>Staff Gap: -3.1</td></tr>
<tr><td>Real Exchange Rate</td><td colspan="7">Background. A narrower domestic-foreign interest rate differential and heightened risk aversion, especially at the outbreak of the pandemic, contributed to strong appreciation pressure in H1:2020; this pressure subsequently eased. Relative to 2019, the average NEER and CPI-based REER appreciated by 6.1 and 3.9 percent, respectively, notwithstanding sizable FX interventions. From a long-term perspective, the NEER has appreciated by 27 percent since end-2010, while the CPI-based REER has appreciated by 2.8 percent (reflecting lower domestic inflation).
Assessment. The staff CA gap implies a REER overvaluation of 5.9 percent in 2020 (applying an estimated elasticity of 0.52). The EBA REER index and level models suggest that the average REER in 2020 was overvalued by 15.2 and 26.4 percent, respectively, with policy gaps accounting for a small amount of the total gap. This finding largely reflects a “reversion to trend” property of the empirical model in the context of prior rapid appreciation episodes. However, due to measurement issues, the results may not fully capture a secular improvement in productivity, especially in knowledge-based sectors. Consistent with the staff CA gap, staff assess the REER to be overvalued in the range of 1.9 to 9.9 percent, with a midpoint of 5.9 percent.[6]</td></tr>
</table>

Capital and Financial Accounts: Flows and Policy Measures	**Background.** Net financial outflows totaled 1.8 percent of GDP in 2020, with private inflows (14.8 percent of GDP) more than offset by SNB reserve increases (16.6 percent of GDP). This contrasted with 2019, when more moderate SNB reserve gains (2.2 percent of GDP) and private outflows (3.0 percent of GDP) jointly led to net financial outflows of 5.2 percent of GDP. During 2009–20, net private inflows averaged 3.6 percent of GDP, while the average annual increase in SNB reserves was 10.5 percent of GDP. **Assessment.** Financial flows are large and volatile, reflecting Switzerland's status as a financial center and safe haven. From a long-term perspective, sizable net private financial outflows prior to the global financial crisis have declined, and on average, turned into net capital inflows, adding to appreciation pressures.
FX Intervention and Reserves Level	**Background.** Official reserve assets (including gold) amounted to US$1,085 billion (135 percent of GDP) at end-2020, up US$229 billion from end-2019 (including valuation changes). While FXIs had been occasional and moderate since exiting the ER floor in 2015, the SNB purchased CHF110 billion of FX (net) in 2020, the highest amount since 2012. **Assessment.** Reserves are large relative to GDP, but more moderate in comparison with short-term foreign liabilities. The high level of reserves also reflects monetary operations aimed at avoiding persistent undershooting of inflation as a result of FX inflow surges and given the limited scope for significant easing via other monetary pool tools. In particular, the supply of domestic assets for purchase is limited, and the marginal interest rate on bank deposits at the SNB of -0.75 percent is already the lowest in the world. The SNB's initiation of quarterly publication of (net) FXI information in 2020 was an important step to enhance transparency.

[1] In December 2020, the SNB published major revisions to the BOP/IIP data. There were two reasons for the revisions: (i) closing a gap data with regard to domiciliary companies; and (ii) reflecting data newly available from reporting institutions. Changes under (ii) included both information from a newly-completed 2019 annual survey and corrections for previous reporting periods concerning companies with especially complex structures. The revisions due to (i) affected only the IIP data from 2008 to 2019; those due to (ii) affected the entire BOP (current account, capital account, financial account) and the IIP for the period from 2014 to 2019. As a result: the net IIP showed an average decrease between 2008 and 2019 of CHF 128 billion (around 17%); and the current account surpluses for 2018 and 2019 decreased significantly, mostly due to adjustments in primary income expenses, while the 2014–17 balances changed less and in both directions.

[2] Other stock-flow adjustments include changes in statistical sources, such as changes in the number of entities surveyed and items covered, although their quantitative importance is not known.

[3] As a result, an appreciation (depreciation) of the Swiss franc has a negative (positive) effect on the NIIP, whereas a symmetric percentage increase in share prices in Switzerland and abroad would reduce the NIIP.

[4] The underlying CA is adjusted for Switzerland-specific factors in the income account : (1) retained earnings on portfolio equity investment that are not recorded in the income balance of the CA under the sixth edition of the IMF *Balance of Payments and International Investment Position Manual*, and (2) recording of nominal interest on fixed income securities under the *Balance of Payments Manual* framework, which compensates for expected valuation losses (due to inflation and/or nominal exchange rate movements), even though this stream compensates for the (anticipated) erosion in the real value of debt assets and liabilities. In addition, the CA balance is also adjusted for transitory impacts of the COVID-19 pandemic on trade of goods and services, including adjustors for (i) tourism (0.5 ppts including the impact on the decline in sales of luxury watches reflecting the decline in international travel); (ii) oil (-0.3 ppts); (iii) household consumption composition shift (-0.4 ppts); (iv) medical products (0.7 ppts); and (v) precious metals (1.4 ppts). Adjusting for these COVID-19 related effects, the underlying CA would need to be increased by about 1.9 percent of GDP (i.e., resulting in a smaller negative gap).

[5] The CA gap range reflects the uncertainty inherent in the assessment.

[6] The country-specific CA-REER elasticity of 0.52 is relatively large due to the high openness of the Swiss economy. The IMF staff CA gap for 2020 was -3.1 percent of GDP, with a range of ±2 percentage points. With an estimated CA-REER semi-elasticity of 0.52, the IMF staff CA gap implies an REER gap of 1.9 to 9.9 percent, with a midpoint of 5.9 percent.

Annex V. Risk Assessment Matrix[1]

Source of Risks	Relative Likelihood	Time Horizon	Expected Impact	Policy Response
Global Risks				
Prolonged pandemic. COVID-19 proves hard to eradicate, for example, due to new virus strains, short effectiveness of vaccines, or widespread unwillingness to take them, requiring costly containment efforts and prompting persistent behavioral changes rendering many activities unviable. For countries with policy space, prolonged support—while needed to cushion the economy—exacerbates stretched asset valuations, fueling financial vulnerabilities. For those with limited space, especially EMs, policy support is insufficient.	Medium	ST, MT	**High** Stricter containment measures would lead to lower GDP growth, larger sales losses, and higher likelihood of bankruptcy.	Maintain and intensify public health measures. Allow sustained countercyclical support. Implement targeted measures for the most-affected companies and relieve liquidity and sustainability challenges. If needed, in case of excessive currency volatility, consider preannounced regular foreign exchange purchases.
Accelerating de-globalization. Despite renewed efforts to reach multilateral solutions to existing tensions, geopolitical competition leads to further fragmentation. Reshoring and less trade reduce potential growth.	Medium	MT	**High** The economy is open and highly integrated in trade and capital markets. The large current account surplus is driven in part by goods and services. Obstacles to trade or capital flows would impact growth.	Work with international partners to secure the benefits of trade integration and cooperation. Consider options to increase diversification of the trade partners. Strengthen supervision of bank and nonbank financial sector to increase resilience. In case of growth downturn, consider fiscal loosening.
Sharp rise in global risk premia exposes financial and fiscal vulnerabilities. A reassessment of market fundamentals (e.g., in response to adverse COVID-19 developments) triggers a widespread risk-off event. Risk asset prices fall sharply and volatility spikes, leading to significant losses in major non-bank financial institutions. Higher risk premia generate financing difficulties for leveraged firms (including those operating in unviable activities) and households, and a wave of bankruptcies erode banks' capital buffers. Financing difficulties extend to sovereigns with excessive public debt, leading to cascading debt defaults.	Medium	ST, MT	**Medium** The nonfinancial private sector, especially households, have a large debt stock (although household financial assets are larger than liabilities). An abrupt and prolonged increase in interest rates could stress leveraged borrowers. May reduce real estate prices. May trigger safe haven inflows and appreciation pressures. Higher interest rates and global effects may affect growth.	Given substantial fiscal space, a countercyclical discretionary fiscal stimulus would be warranted. Support to viable but insolvent companies may be needed. If rising risk premia causes elevated volatility or safe haven pressures which would lead to the franc appreciation increasing risks of deflation, consider use of targeted FXI.

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly.

Source of Risks	Relative Likelihood	Time Horizon	Expected Impact	Policy Response
Switzerland-Specific Risks				
Resumption of safe haven inflows in response to renewed global risk-off sentiment. CHF appreciation.	Medium	ST, MT	High Switzerland is a major financial center and is seen as a safe haven. Flight to safety would lead to sharp appreciation pressures on CHF. Appreciation adds to deflation and hurts competitiveness and growth.	Use targeted FXI to prevent sharp appreciation. Allow full operation of the structural-balance fiscal rule and allow a temporary discretionary fiscal stimulus if the downturn is deep and/or sustained. Further enhance the anti-corruption and AML/CFT frameworks to protect the financial sector against inflows from foreign illicit proceeds.
Early withdrawal of fiscal policy support, depressing GDP growth and deepening scarring of corporate balance sheets and labor market.	Medium	MT	Medium Non-financial corporates would face elevated liquidity and solvency challenges. Some industries would be particularly affected. May translate into widespread layoffs and a decline in household incomes, prompting social vulnerabilities.	Allow for gradual withdrawal of support. Adjust policies based on developments in pandemic and the economy. Delay the required amortization of COVID-19-related extraordinary spending.
Prolonged low-growth and low-inflation environment, leading to persistent very low interest rates that increase risk of a significant adjustment in real estate prices and financial stability risks.	Medium	MT	High Continued low interest rates could encourage search for yield, especially in real estate. Given the large exposure to the property market, a decline of property prices could create stress for domestic financial institutions with large balance-sheet exposure, posing stability risks.	Expand monetary and macroprudential toolkits ease policies and reduce vulnerabilities. Strengthen bank buffers against real estate-related exposure. Assess risks in the construction sector. Consider changes to limits on portfolio allocations for pension funds (indicative) and insurance companies.
Political developments negatively affect Swiss-EU relations. Failure of ongoing negotiations on an institutional agreement could lead to worsening trade and labor relationships with Switzerland's largest partner. Tensions in relations relate to pressure for wider/full applicability of EU legislation and regulations to Switzerland and on specific issues like cross-border movement of labor.	Medium	MT	High Disruptions could (progressively) undermine trade, investment, and labor relations with the EU, adversely impacting the real economy.	Seek to limit economic fallout by preserving efficient flows of goods, labor and financial services with the EU. Fiscal response may be needed if developments are adverse.

Annex VI. Debt Sustainability Assessment

Table 1. Switzerland: External Debt Sustainability Framework, 2016–26

(In percent of GDP, unless otherwise indicated)

	Actual							Projections						
	2016	2017	2018	2019	2020			2021	2022	2023	2024	2025	2026	**Debt-stabilizing non-interest current account 6/**
Baseline: External debt	258.3	278.8	250.5	266.9	301.0			**248.2**	**231.2**	**224.7**	**213.3**	**205.6**	**195.7**	**1.6**
Change in external debt	12.1	20.6	-28.4	16.5	34.1			-52.8	-17.0	-6.5	-11.4	-7.7	-9.9	
Identified external debt-creating flows (4+8+9)	-8.5	-17.8	0.5	-3.3	13.8			-10.5	-6.1	-3.8	-4.4	-3.1	-4.4	
Current account deficit, excluding interest payments	-10.4	-8.7	-8.4	-8.4	-5.3			-8.1	-8.8	-8.4	-8.7	-8.3	-8.6	
Deficit in balance of goods and services	-10.6	-10.1	-11.7	-11.5	-9.2			-9.8	-10.4	-10.1	-10.2	-9.9	-10.1	
Exports	64.8	64.5	65.5	65.3	62.9			64.3	65.4	66.7	68.3	69.7	71.4	
Imports	54.2	54.3	53.7	53.8	53.7			54.5	55.0	56.7	58.1	59.9	61.3	
Net non-debt creating capital inflows (negative)	2.8	-7.4	17.7	5.2	11.0			5.8	7.9	6.6	7.0	6.6	6.6	
Automatic debt dynamics 1/	-0.9	-1.7	-8.8	-0.1	8.1			-8.2	-5.3	-2.0	-2.7	-1.3	-2.5	
Contribution from nominal interest rate	1.4	1.5	1.8	1.7	1.5			1.3	1.3	1.2	1.2	1.1	1.1	
Contribution from real GDP growth	-4.9	-4.2	-8.1	-2.8	7.8			-9.5	-6.6	-3.2	-3.9	-2.5	-3.5	
Contribution from price and exchange rate changes 2/	2.6	0.9	-2.4	1.0	-1.2			...	...	...	...	...	...	
Residual, incl. change in gross foreign assets (2-3) 3/	20.6	38.4	-28.9	19.7	20.3			-42.3	-10.9	-2.7	-7.1	-4.6	-5.5	
External debt-to-exports ratio (in percent)	398.4	432.6	382.4	408.7	478.3			386.0	353.4	336.8	312.3	294.8	274.1	
Gross external financing need (in billions of US dollars) 4/	1057.9	1120.2	1154.0	1093.0	1131.2			1241.5	1125.6	1113.4	1113.3	1109.8	1106.3	
in percent of GDP	152.1	158.9	156.7	149.3	151.3	10-Year	10-Year	150.5	128.8	123.0	117.2	112.3	106.4	
Scenario with key variables at their historical averages 5/								**248.2**	**234.5**	**226.6**	**216.3**	**207.7**	**199.4**	**4.3**
Key Macroeconomic Assumptions Underlying Baseline						Historical Average	Standard Deviation							
Real GDP growth (in percent)	2.0	1.7	3.0	1.1	-3.0	1.4	1.6	3.5	2.8	1.4	1.8	1.2	1.8	
GDP deflator in US dollars (change in percent)	-2.9	-0.3	1.4	-1.7	5.2	1.0	6.7	6.6	3.1	2.1	3.1	2.8	3.4	
Nominal external interest rate (in percent)	0.6	0.6	0.7	0.7	0.6	0.6	0.1	0.5	0.5	0.5	0.5	0.5	0.5	
Growth of exports (US dollar terms, in percent)	4.4	0.8	6.2	-0.8	-1.7	2.3	8.7	12.8	7.8	5.6	7.4	6.2	7.8	
Growth of imports (US dollar terms, in percent)	5.6	1.6	3.4	-0.5	1.9	2.6	10.5	12.0	7.0	6.6	7.6	7.2	7.9	
Current account balance, excluding interest payments	10.4	8.7	8.4	8.4	5.3	9.6	2.1	8.1	8.8	8.4	8.7	8.3	8.6	
Net non-debt creating capital inflows	-2.8	7.4	-17.7	-5.2	-11.0	-3.7	6.8	-5.8	-7.9	-6.6	-7.0	-6.6	-6.6	

1/ Derived as [r - g - r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock, with r = nominal effective interest rate on external debt; r = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate, e = nominal appreciation (increase in dollar value of domestic currency), and a = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as [-r(1+g) + ea(1+r)]/(1+g+r+gr) times previous period debt stock. r increases with an appreciating domestic currency (e > 0) and rising inflation (based on GDP deflator).

3/ For projection, line includes the impact of price and exchange rate changes.

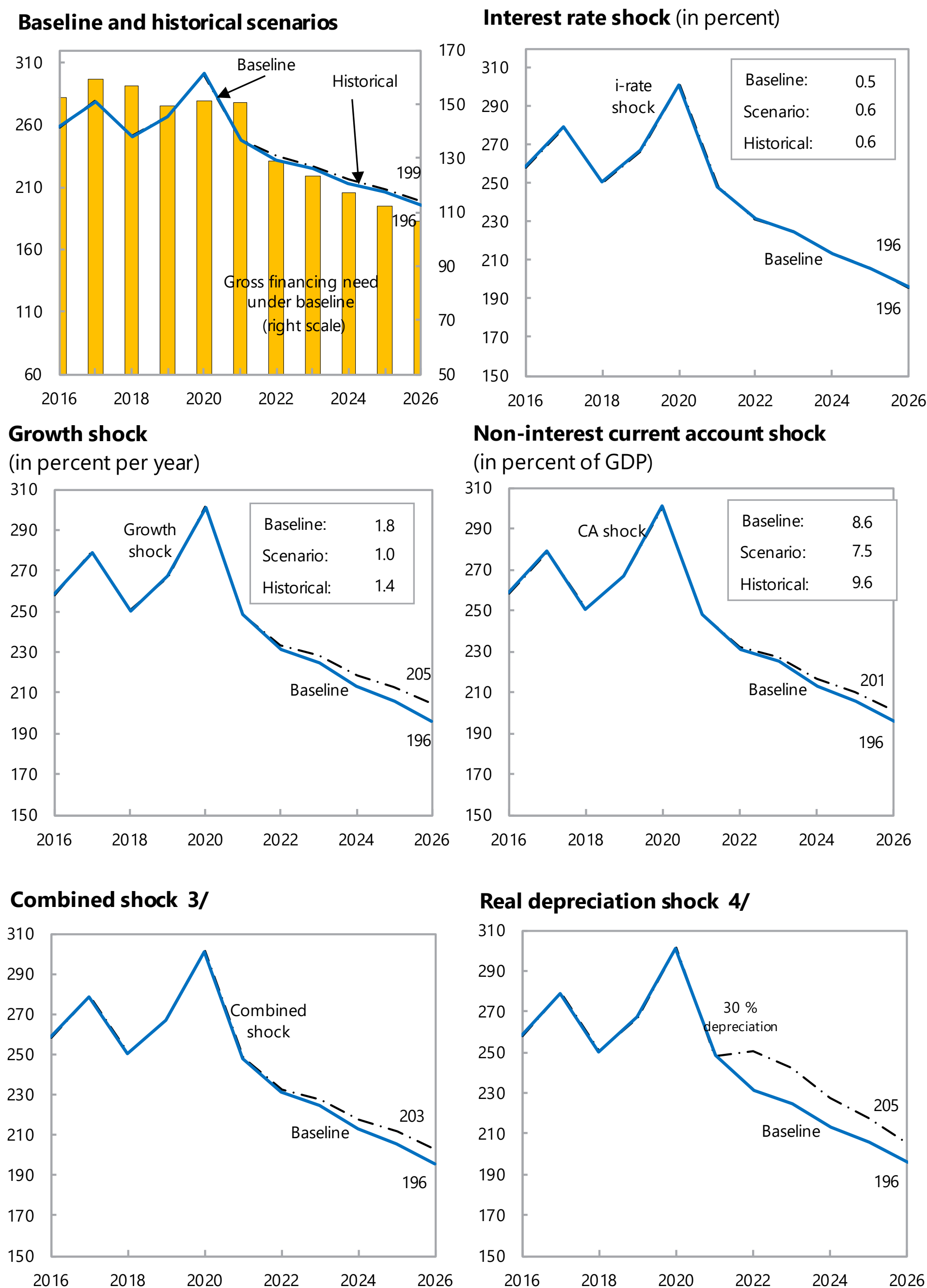
4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Figure 1. Switzerland: External Debt Sustainability: Bound Tests 1/ 2/

(External debt in percent of GDP)



Sources: International Monetary Fund, Country desk data, and staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.
3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
4/ One-time real depreciation of 30 percent occurs in 2021.

Figure 2. Switzerland: Public Sector Debt Sustainability Analysis (DSA)—Baseline Scenario

(In percent of GDP, unless otherwise indicated)

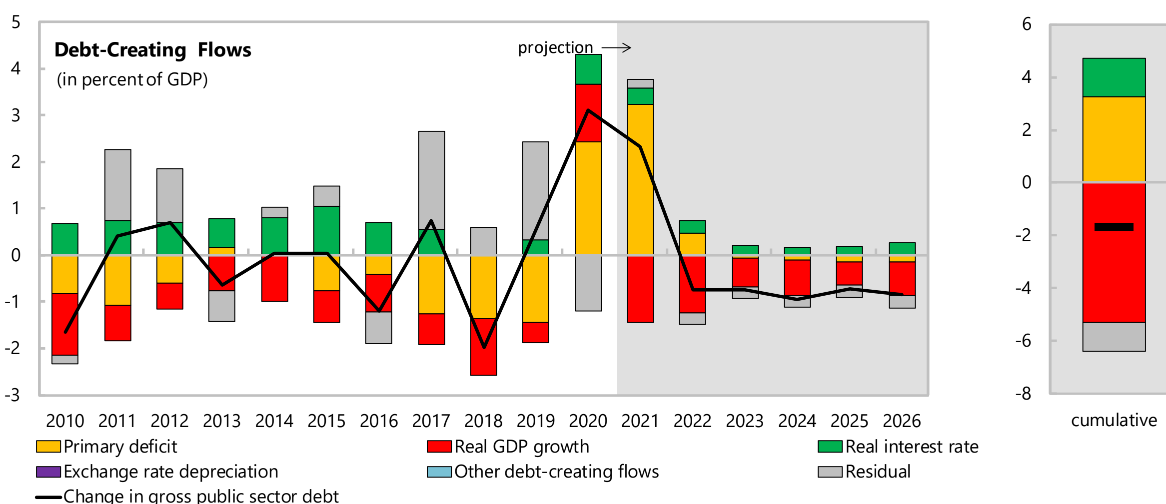
Debt, Economic and Market Indicators [1/]

	Actual			Projections					
	2010-2018 [2/]	2019	2020	2021	2022	2023	2024	2025	2026
Nominal gross public debt	41.2	39.8	42.9	45.3	44.5	43.8	42.8	42.1	41.2
Public gross financing needs	3.7	2.6	6.9	8.3	6.4	5.5	5.4	5.3	5.2
Net public debt	41.2	39.8	42.9	45.3	44.5	43.8	42.8	42.1	41.2
Real GDP growth (in percent)	2.1	1.1	-3.0	3.5	2.8	1.4	1.8	1.2	1.8
Inflation (GDP deflator, in percent)	-0.2	-0.1	-0.6	0.2	0.3	0.5	0.7	0.8	0.8
Nominal GDP growth (in percent)	1.9	1.0	-3.4	3.6	3.2	2.0	2.5	2.0	2.6
Effective interest rate (in percent) [4/]	1.4	0.7	1.0	1.1	0.9	1.0	1.1	1.3	1.5

As of April 29, 2021		
Sovereign Spreads		
EMBIG (bp) 3/		0
5Y CDS (bp)		11
Ratings	Foreign	Local
Moody's	Aaa	Aaa
S&Ps	AAA	AAA
Fitch	AAA	AAA

Contribution to Changes in Public Debt

	Actual			Projections							
	2010-2018	2019	2020	2021	2022	2023	2024	2025	2026	cumulative	debt-stabilizing primary balance [9/]
Change in gross public sector debt	-0.4	0.6	3.1	2.3	-0.7	-0.7	-1.0	-0.7	-0.9	-1.7	
Identified debt-creating flows	-0.9	-1.6	4.3	2.1	-0.5	-0.5	-0.7	-0.5	-0.6	-0.6	
Primary deficit	-0.7	-1.4	2.4	3.2	0.5	-0.1	-0.1	-0.1	-0.1	3.3	-0.5
Primary (noninterest) revenue and grants	31.8	32.7	33.4	32.9	32.7	32.7	32.7	32.7	32.7	196.7	
Primary (noninterest) expenditure	31.1	31.2	35.8	36.1	33.2	32.7	32.6	32.6	32.6	199.9	
Automatic debt dynamics [5/]	-0.2	-0.1	1.9	-1.1	-1.0	-0.4	-0.6	-0.3	-0.5	-3.9	
Interest rate/growth differential [6/]	-0.2	-0.1	1.9	-1.1	-1.0	-0.4	-0.6	-0.3	-0.5	-3.9	
Of which: real interest rate	0.6	0.3	0.6	0.4	0.3	0.2	0.2	0.2	0.3	1.4	
Of which: real GDP growth	-0.9	-0.4	1.2	-1.4	-1.2	-0.6	-0.8	-0.5	-0.7	-5.3	
Exchange rate depreciation [7/]	0.0	0.0	0.0	…	…	…	…	…	…	…	
Other identified debt-creating flows	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual, including asset changes [8/]	0.5	2.1	-1.2	0.2	-0.3	-0.3	-0.3	-0.3	-0.3	-1.1	



Source: IMF staff.

1/ Public sector is defined as general government.

2/ Based on available data.

3/ Long-term bond spread over German bonds.

4/ Defined as interest payments divided by debt stock (excluding guarantees) at the end of previous year.

5/ Derived as $[(r - \pi(1+g) - g + ae(1+r)]/(1+g+\pi+g\pi))$ times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).

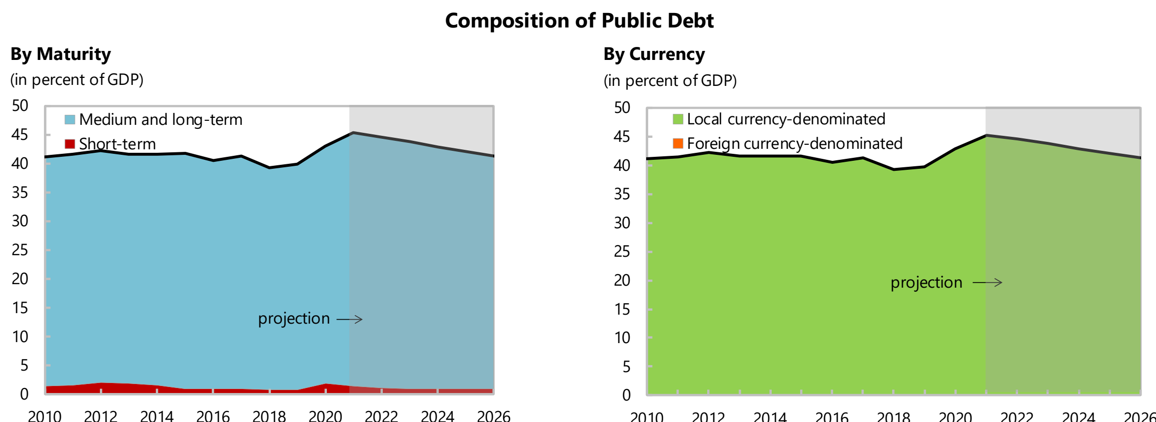
6/ The real interest rate contribution is derived from the numerator in footnote 5 as $r - \pi(1+g)$ and the real growth contribution as -g.

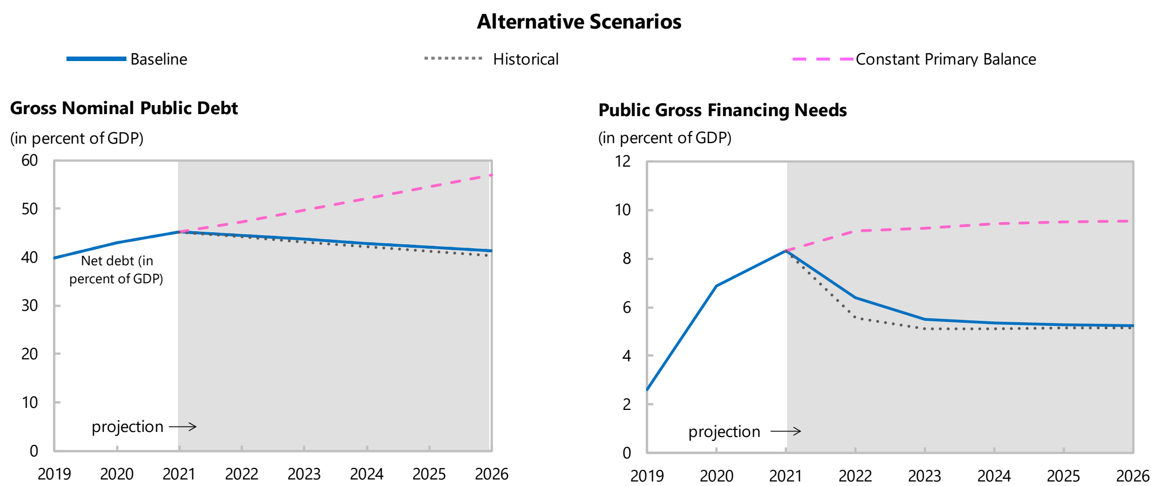
7/ The exchange rate contribution is derived from the numerator in footnote 5 as $ae(1+r)$.

8/ Includes asset changes and interest revenues (if any). For projections, includes exchange rate changes during the projection period.

9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Figure 3. Switzerland: Public DSA—Composition of Public Debt and Alternative Scenarios





Underlying Assumptions
(in percent)

Baseline Scenario	2021	2022	2023	2024	2025	2026
Real GDP growth	3.5	2.8	1.4	1.8	1.2	1.8
Inflation	0.2	0.3	0.5	0.7	0.8	0.8
Primary Balance	-3.2	-0.5	0.1	0.1	0.1	0.1
Effective interest rate	1.1	0.9	1.0	1.1	1.3	1.5
Constant Primary Balance Scenario						
Real GDP growth	3.5	2.8	1.4	1.8	1.2	1.8
Inflation	0.2	0.3	0.5	0.7	0.8	0.8
Primary Balance	-3.2	-3.2	-3.2	-3.2	-3.2	-3.2
Effective interest rate	1.1	0.9	1.0	1.1	1.2	1.4

Historical Scenario	2021	2022	2023	2024	2025	2026
Real GDP growth	3.5	1.4	1.4	1.4	1.4	1.4
Inflation	0.2	0.3	0.5	0.7	0.8	0.8
Primary Balance	-3.2	0.4	0.4	0.4	0.4	0.4
Effective interest rate	1.1	0.9	1.1	1.3	1.6	1.9

Source: IMF staff.

INTERNATIONAL MONETARY FUND

SWITZERLAND

May 25, 2021

STAFF REPORT FOR THE 2021 ARTICLE IV CONSULTATION—INFORMATIONAL ANNEX

Prepared By European Department

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FUND RELATIONS

(As of April 30, 2021)

Membership Status: Joined May 29, 1992; Article VIII.

General Resources Account

	SDR Million	Percent of Quota
Quota	5,771.10	100.00
Fund holdings of currency	4,485.64	77.73
Reserve position in Fund	1,285.48	22.27
New arrangements to borrow	158.45	

SDR Department

	SDR Millions	Percent Allocation
Net cumulative allocation	3,288.04	100.00
Holdings	3,405.26	103.56

Outstanding Purchases and Loans: None

Financial Arrangements: None

Projected Payments to Fund:[1]
(SDR Million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2021	2022	2023	2024	2025
Principal					
Interest	0.06	0.06	0.06	0.06	0.06
Total	0.06	0.06	0.06	0.06	0.06

Exchange Rate Arrangement:

The de jure exchange rate arrangement is free floating. The exchange rate of the Swiss franc is determined by market forces in the foreign exchange market, and all settlements are made at free market rates. However, the SNB reserves the right to intervene in the foreign exchange market. The SNB publishes quarterly information regarding its foreign exchange transactions on the SNB data

[1] When a member has overdue financial obligations outstanding for more than three months, the amount of such arrears will be shown in this section.

portal, starting with data for Q1:2020.[2] The de facto exchange rate arrangement was reclassified from floating to crawl-like, effective May 19, 2020.

Switzerland has accepted the obligations of Article VIII, Sections 2, 3, and 4, and maintains a system free of restrictions on the making of payments and transfers for current international transactions except for restrictions in place for security reasons notified to the Fund pursuant to Decision No. 144-(52/51).

On August 10, 2020, Switzerland notified the IMF of the exchange restrictions that have been imposed against certain countries, individuals, and entities, in accordance with relevant UN Security Council resolutions and EU regulations. More information on the restrictions can be found at the Swiss State Secretariat for Economic Affairs (SECO) site.

Latest Article IV Consultation: The last Article IV consultation was concluded on June 17, 2019, with the staff report published on June 27, 2019. Switzerland is on the standard 12-month consultation cycle, but due to pandemic-related crisis response and travel restrictions, the 2020 consultation did not take place.

Technical Assistance (TA): No receipt of IMF TA. Switzerland is a major financial supporter of IMF externally-financed capacity development (TA and training), including country-specific and region-wide projects globally as well as IMF's multi partner vehicles (regional and thematic trust funds and capacity development centers). Switzerland has also been a financial supporter of other IMF initiatives, including for low-income countries via the Poverty Reduction and Growth Trust and for debt relief.

Resident Representatives: None

Financial System Stability Assessment Update and ROSCs:

- Missions for the 2019 FSAP were held in November 2018 and January 2019. The findings were discussed with the authorities during Article IV consultation discussions in March 2019 and were presented to the Executive Board for discussion alongside the Article IV staff report on June 17, 2019. The report for the previous FSAP update was issued on May 28, 2014.

- Reports on the Observance of Standards and Codes (Basel core principles, IAIS core principles, and IOSCO objectives and principles) were conducted in 2013–14, and the report was issued on May 28, 2014.

[2] Annual information for previous years was published by the SNB in its annual accountability report.

STATISTICAL ISSUES

(As of May 12, 2021)

I. Assessment of Data Adequacy for Surveillance
General: Data provision is adequate for Fund surveillance. Switzerland publishes timely economic statistics and posts most of the data and the underlying documentation on the Internet.
National Accounts: National accounts are timely (including the expenditure, production, and income approaches). GDP by canton are published with a significant lag, however, with 2018 data being released in January 2021. Responsibility for national accounts compilation is split between two different agencies: quarterly national accounts are published by the State Secretariat for Economic Affairs, and annual national accounts are published by the Federal Statistics Office (FSO).
Price Statistics: Consumer price indices and producer and import price indices are collected by the FSO. They are published monthly with a base period of December 2020. The FSO is developing additional producer price indexes for services and construction (currently published just twice a year).
Government Finance Statistics: General government finance statistics are compiled by the Federal Finance Administration. Data for general government are finalized with eight months lag, mainly due to delays in compiling fiscal accounts at the level of cantons and communes. The concept and methodology of every account, including the most recent addition of financial transactions in financial assets and liabilities and other economic flows, have been fully reconciled with the Swiss system of national accounts of the FSO with the publication of September 28, 2020. The Swiss National Bank (SNB) publishes statistics on outstanding and new bond issues by the Swiss Confederation.
Monetary and Financial Statistics: The SNB has submitted monetary and financial statistics data using the Standardized Report Forms for central bank (1SR) and depository corporations (2SR) for publication in the IMF's International Financial Statistics (IFS). The data are currently being reviewed for dissemination. Switzerland reports data on some basic series and indicators of the Financial Access Survey (FAS), including two indicators of the United Nations Sustainable Development Goals.
Financial Sector Surveillance: Switzerland reports 11 of the 12 core Financial Soundness Indicators (FSIs) and 9 additional FSIs for deposit takers, and 4 FSIs for real estate markets. All FSIs are reported on an annual basis on the IMF's FSI website. Some FSIs are also reported on a quarterly basis on the Swiss National Summary Data Page.
External Sector Statistics: Balance of Payments (BOP) and international investment position (IIP) statistics are published based on the sixth edition of the IMF's *Balance of Payments and International Investment Position Manual* (BPM6). Official data in BPM6 format are available from 1999 onwards. Switzerland reports to the IMF annual data on the Coordinated Direct Investment Survey (CDIS); semi-annual and annual data on the Coordinated Portfolio Investment Survey CPIS); and monthly data on the International Reserves and Foreign Currency Liquidity. Switzerland is also reporting quarterly external debt data to the World Bank database.

II. Data Standards and Quality
In January 2021, Switzerland adhered to the IMF's Special Data Dissemination Standard (SDDS) Plus—the highest tier of the Data Standards Initiatives, having been an SDDS subscriber since 1996 and maintaining SDDS flexibility options on dissemination of production index data (for periodicity and timeliness) and of wages/earnings data (for periodicity). Switzerland's SDDS Plus data are accessible through the *Dissemination Standards Bulletin Board*.

Switzerland: Table of Common Indicators Required for Surveillance

(As of May 7, 2021)

	Date of Latest Observation	Date Received	Frequency of Data[7]	Frequency of Reporting[7]	Frequency of Publication[7]
Exchange Rates	Same day	Same day	D and M	M and M	D and M
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	Mar 21	Apr 21	M	M	M
Reserve/Base Money	Mar 21	Apr 21	M	M	M
Broad Money	Mar 21	Apr 21	M	M	M
Central Bank Balance Sheet	Mar 21	Apr 21	M	M	M
Consolidated Balance Sheet of the Banking System	Feb 21	Apr 21	M	M	M
Interest Rates[2]	Same day	Same day	D and M	M and M	D and M
Consumer Price Index	April 21	May 21	M	M	M
Revenue, Expenditure, Balance and Composition of Financing[3]–General Government[4]	2019	Mar 21	A	A	A
Revenue, Expenditure, Balance and Composition of Financing[3]–Central Government	2019	Mar 21	A	A	A
Stocks of Central Government and Central Government-Guaranteed Debt[5]	2019	Mar 21	A	A	A
External Current Account Balance	Q4/20	Mar 21	Q	Q	Q
Exports and Imports of Goods and Services	Q4/20	Mar 21	Q	Q	Q
GDP/GNP	Q4/20	Mar 21	Q	Q	Q
Gross External Debt	Q4/20	Mar 21	Q	Q	Q
International Investment Position[6]	Q4/20	Mar 21	Q	Q	Q

[1] Any reserve assets that are pledged or otherwise encumbered should be specified separately. Also, data should comprise short-term liabilities linked to a foreign currency but settled by other means as well as the notional values of financial derivatives to pay and to receive foreign currency, including those linked to a foreign currency but settled by other means.

[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.

[3] Foreign, domestic bank, and domestic nonbank financing.

[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) state and local governments.

[5] Including currency and maturity composition.

[6] Includes external gross financial asset and liability positions vis-à-vis nonresidents.

[7] Daily (D); weekly (W); monthly (M); quarterly (Q); annually (A); irregular (I); and not available (NA).

Statement by the Staff Representative on Switzerland
June 11, 2021

This statement provides information that has become available since the staff report was issued to the Executive Board on May 25, 2021. The thrust of the staff appraisal remains unchanged.

1. **The Swiss Federal Council (FC) announced on May 26 that due to remaining differences, it would not sign an institutional agreement (IA) with the European Union**. Issues identified by the FC were the application of the EU Citizens' Rights Directive (CRD), wage protection, and state aid. Dynamic adoption of changes in EU law and the role of the EU Court of Justice in dispute resolution were also noted. The decision may mean that the 120+ bilateral accords now in place may not be updated or may expire. The EU expressed regret with the decision. Economic impacts are difficult to assess, as they depend on future dialogue and decisions. If the EU does not renegotiate expiring accords or agree to new deals, Switzerland's favorable access to the European single market may erode over time. Trade in medical devices, which employs 60,000 workers and accounts for 3 percent of Swiss GDP, will be affected first, as the EU halted mutual recognition and trade facilitation for Swiss-made devices on May 26. Export of Swiss medical devices may be more complex going forward. Developments on the IA do not warrant a change in the thrust of staff appraisal, as there may be prospects for agreement on specific issues in the future that would minimize significant disruptions, and in any event, the effects will not be immediate. Staff will continue to assess implications going forward and encourages the parties to find acceptable compromises.

2. **New national accounts data published on June 1 showed a somewhat milder contraction in 2020 than indicated by previous data**. According to the latest information, real GDP declined by about 2.7 percent in 2020, compared with a contraction close to 3 percent based on the first release in March 2021. Real GDP in Q1:2021 declined by 0.5 percent compared to the previous quarter. These updates do not materially change staff's assessment of the economic outlook and risks.

3. **The 2020 Annual Report of the Swiss Federal Audit Office (SFAO) was recently published and found that the federal response to the COVID-19 crisis was effective**. The report noted that the number of cases of suspicious use of public support had remained low, although it had risen over time. For COVID-19 bridge loans, the SFAO flagged 4,646 cases, comprising around 7 percent of the total loan amount, to the State Secretariat for Economic Affairs for further examination. The cases mainly concerned possible improper payment of dividends by companies that received the bridge loans or issues in reported turnover numbers. The SFAO also noted possible issues under the short-time work program, mainly due to simplified application procedures during the crisis. The SFAO did not detect systematic abuses in the loss compensation program for self-employed. It concluded that support to the culture sector was performed appropriately and that compensation decisions were justified.

Statement by Marcel Peter, Alternate Executive Director for Switzerland
Caroline Wehrle, Senior Advisor to Executive Director
and Albi Tola, Advisor to Executive Director
June 11, 2021

On behalf of our Swiss authorities, we thank staff for their insightful reports and the thorough analyses of macroeconomic and financial sector developments. We broadly share staff's views on the challenges going forward, and appreciate their recommendations, many of which are in line with policies that are currently being implemented.

Policy Response to the COVID-19 Crisis

The authorities share staff's assessment of the policy response to the COVID-19 crisis. Swift, strong, and flexible policy support was key to mitigate its impact. Fiscal and monetary policy acted in a complementary and effective way.

Fiscal policy intervened forcefully to support households and firms, avoid unwarranted bankruptcies, contain the increase in unemployment, and support purchasing power. In 2020, the federal deficit reached a record-high overall level of CHF 15.8 billion (USD 17.5 billion), as outlays and guarantees amounting to a total of 10 percent of GDP were quickly approved. This targeted fiscal support was essential and effective to limit the pandemic fallout. Key measures included the short-time work program, which compensated for lost earnings; income-loss compensation for the self-employed; and a large federal loan-guarantee program. General government debt, according to the IMF definition, is provisionally expected to increase from 40 percent in 2019 to 46 percent in 2021. The authorities agree that fiscal policy should continue to play a central role in supporting the economy throughout the pandemic, and they stand ready to deploy additional resources if needed. For 2021, additional outlays of 3.3 percent of GDP have been approved at this point and a deficit of more than CHF 20 billion (USD 22.2 billion) is expected according to recent estimates.

Monetary policy was also confronted with extraordinary challenges, as the domestic and global demand shock was exacerbated by substantial and prolonged safe-haven pressures on the exchange rate. These pressures bore the risk of an abrupt and unwarranted tightening of monetary conditions, in an environment of very low or negative inflation and modest inflation expectations. The SNB's response relied on a multi-pronged approach. First, various steps were aimed at providing ample liquidity and supporting credit activity, including the deactivation of the countercyclical capital buffer and the creation of a specific refinancing facility for COVID-19-loans guaranteed by the federal government. Second, the SNB maintained its negative policy rate at -0.75 percent, the lowest worldwide. Third, in March 2020, the SNB communicated its willingness to intervene "more strongly" in the foreign exchange (FX) market. The announcement was intended to have a signaling effect and to ease appreciation pressures on the Swiss franc. Fourth, strong demand for the Swiss franc forced the SNB to actually intervene in

the FX market. The franc still appreciated by 6 percent in nominal effective exchange rate terms. According to the staff's assessment, the franc was clearly overvalued in 2020.

In general, the authorities are guided by the view that the policy mix should depend on the nature of the economic issues and associated challenges that need to be addressed. They consider the current policy mix to be appropriate under current circumstances.

Outlook and Risks

The authorities broadly agree with staff on the outlook and risks. So far, Switzerland has come through the crisis relatively unscathed, not least because of less restrictive containment measures. If immunization proceeds as planned and the remaining containment measures can be durably eased, the recovery should continue in line with official forecasts and become more broad-based across economic sectors. The authorities are of the view that their targeted policy response, combined with Switzerland's competition-oriented environment and a well-functioning credit market, will allow the economy to adjust to the challenges and limit any lasting adverse impact from the pandemic. Overall, the Swiss economy is set to grow at a significantly above-average rate of 3.0 percent in 2021 (according to March forecasts).

While activity is likely to return to pre-crisis levels in the second half of this year, production capacity will remain underutilized for some time. In addition, the Swiss franc is still highly valued and at risk of renewed safe-haven pressures if global uncertainty rises again. Inflation is thus likely to remain muted and deflationary risks persist. Under the SNB's baseline scenario, CPI inflation is expected to increase only gradually, reaching 0.5 percent in 2023.

With progressing vaccination campaigns in Switzerland and other countries, risks have become broadly balanced in the short term. Upside risks include higher than expected catch-up effects and a faster than expected end of the pandemic. Major downside risks persist at the international level, including those related to the surge in sovereign and corporate debt. Domestic risks stem mainly from higher than expected corporate insolvencies or a major correction in the real estate sector. While there are also uncertainties related to the future relationship between Switzerland and the EU, Switzerland remains a reliable and committed partner for the EU even in the absence of the institutional agreement. In the view of the Federal Council, it is in the shared interest of Switzerland and the EU to continue with their proven bilateral approach.

Fiscal and Monetary Policy

The debt-brake framework has served Switzerland well. With a pre-crisis general government debt of about 40 percent of GDP, Switzerland entered the crisis with a strong fiscal position and was able to finance record high outlays to effectively contain the contraction of activity. The countercyclical design of the debt-brake rule also allowed the government to continue all public investment projects as planned. To avoid headwinds to the recovery, the authorities are considering extending the amortization delay for extraordinary outlays beyond the six years envisaged by the debt-brake rule. More generally, the cautious fiscal policy framework controls

expenditure growth, enables the financing of a well-developed social security system, and ensures Switzerland's fiscal sustainability and resilience to future shocks. Since its introduction in 2003, the fiscal rule was instrumental in correcting a spending bias that led to unwarranted structural deficits, even during economic upswings, while providing valuable fiscal space in the event of unforeseen crises or severe economic downturns.

The Swiss authorities are committed to supporting a green and digital transformation, with major public investments already underway. In 2019, a 10-year, CHF 13 billion (USD 14.4 billion) investment program was launched to improve railway infrastructure. A heavy vehicle fee and a CO_2 levy incentivize efficient fossil fuel consumption and generate annual revenues of about CHF 2.8 billion (USD 3.1 billion), corresponding to 0.4 percent of GDP. A good part of these revenues are earmarked for reducing the burden on the environment, for example through energy efficient renovations and road-to-rail policies. The planned Climate Fund, subject to a popular vote on June 13, will provide a further approximately CHF 1 billion (USD 1.1 billon) annually for climate investments and R&D. It will be financed by a new air ticket levy and an increase in the CO_2 levy. These investments are large as a share of GDP, also relative to those planned in other countries, and the authorities do not currently see the need for further increases in fiscal outlays in these areas.

The authorities concur with staff that monetary policy should remain accommodative until there are clear signs of a sustained recovery, in line with the mandate of the SNB to ensure price stability while taking due account of economic developments. The negative policy rate and the SNB's willingness to intervene in the FX market when needed remain essential. The SNB remains very vigilant and will continue to assess whether additional measures might be necessary to achieve its mandate.

External Sector Assessment

We take good note of the IMF's external assessment. The estimated current account gap amounts to -3.1 percent of GDP, implying a Swiss current account balance that is weaker than warranted by fundamentals. Also, staff assesses the Swiss franc to be overvalued by close to 6 percent.

This year's assessment for Switzerland departs from the standard approach adopted in the past. The latter typically derived the assessment of a country's external position from the current account balance metrics. A more holistic approach, relying on a broader set of indicators, was adopted in the present case. We welcome the adoption of a more holistic approach. For instance, we have repeatedly stressed the importance of giving similar weight to the REER models as to the CA model. At the same time, the departure from the standard approach shows that more work is needed to establish a robust external sector assessment, possibly extended to an even broader set of indicators. Ultimately, the approach adopted needs to be applied in a consistent and transparent manner over time and across countries to ensure evenhandedness.

The rationale for departing from a mechanical link between the current account gap and the assessment of the external position is in line with a point we have made in the past. There are

significant limitations to focusing only on the current account balance to gauge a country's external position and exchange rate valuation. First, the current account balance does not encompass all relevant aspects of the external position. Second, current account balances are notoriously difficult to measure. Third, and relatedly, current account numbers can undergo substantial revisions. Thus, relying on current account first releases to gauge a country's external position can be strongly misleading. Fourth, headline current account developments, in particular in small open economies, might be strongly affected by particular factors unrelated to fundamentals.

Financial Sector Policies

The Swiss authorities share the staff's view that banks entered the crisis with strong capital buffers and incurred limited losses, leaving the banking sector's loss absorption capacity largely intact.

The authorities are well-aware that the prospects of a further prolongation of negative interest rates entails risks and creates challenges to existing business models and the profitability of financial firms over the medium term. They are closely monitoring developments and are continuously evaluating the need for additional regulatory and supervisory action to ensure financial stability.

In addition, the authorities will continue to closely monitor developments in the mortgage and real estate markets. Despite the pandemic, residential transaction prices have continued to rise, thereby increasing the risk of a sudden price correction. If and when the need arises, the authorities will consider options for additional macroprudential measures and for strengthening existing measures to limit the build-up of risks, such as a reactivation of the countercyclical capital buffer.

Various financial sector reforms have been implemented since the 2019 FSAP. These include improvements in recovery and resolution planning for financial market infrastructures and the publication of a new ordinance specifying FINMA's powers at the international level and in terms of regulation. Other recommendations are still being considered or implemented in the context of the implementation of international standards.

Structural Issues

Crisis-related labor market support measures have proven effective in preserving jobs and mitigating scarring. The authorities concur with staff that these measures should be maintained until the recovery takes hold. At the same time, they are very cognizant that keeping support measures in place for too long could impede post-COVID-19 structural transformation. The authorities are thus preparing and implementing measures to further increase labor force participation and labor market flexibility, including through training.

The authorities agree that pension reform is essential to maintain a sustainable and effective social safety net against the backdrop of an aging population and the sustained low interest environment. For the first mandatory pillar (government pension scheme) of the pension system, the latest reform helped reduce the expected yearly financing shortfall by about CHF 2 billion (USD 2.2 billion). Ongoing reform proposals aim to provide more flexibility in the retirement age, with incentives to work longer, and to address the funding gap through the alignment of the retirement age at 65 for women and men as well as the mobilization of additional earmarked revenue. For the second pillar (employers' pension schemes), the proposal seeks to reduce the financing gap through a cut in the conversion rate from 6.8 to 6 percent. The proposal also includes transitional and permanent compensatory measures to help offset negative impacts of the reforms.