Monetary policy challenges and the monetary policy strategy

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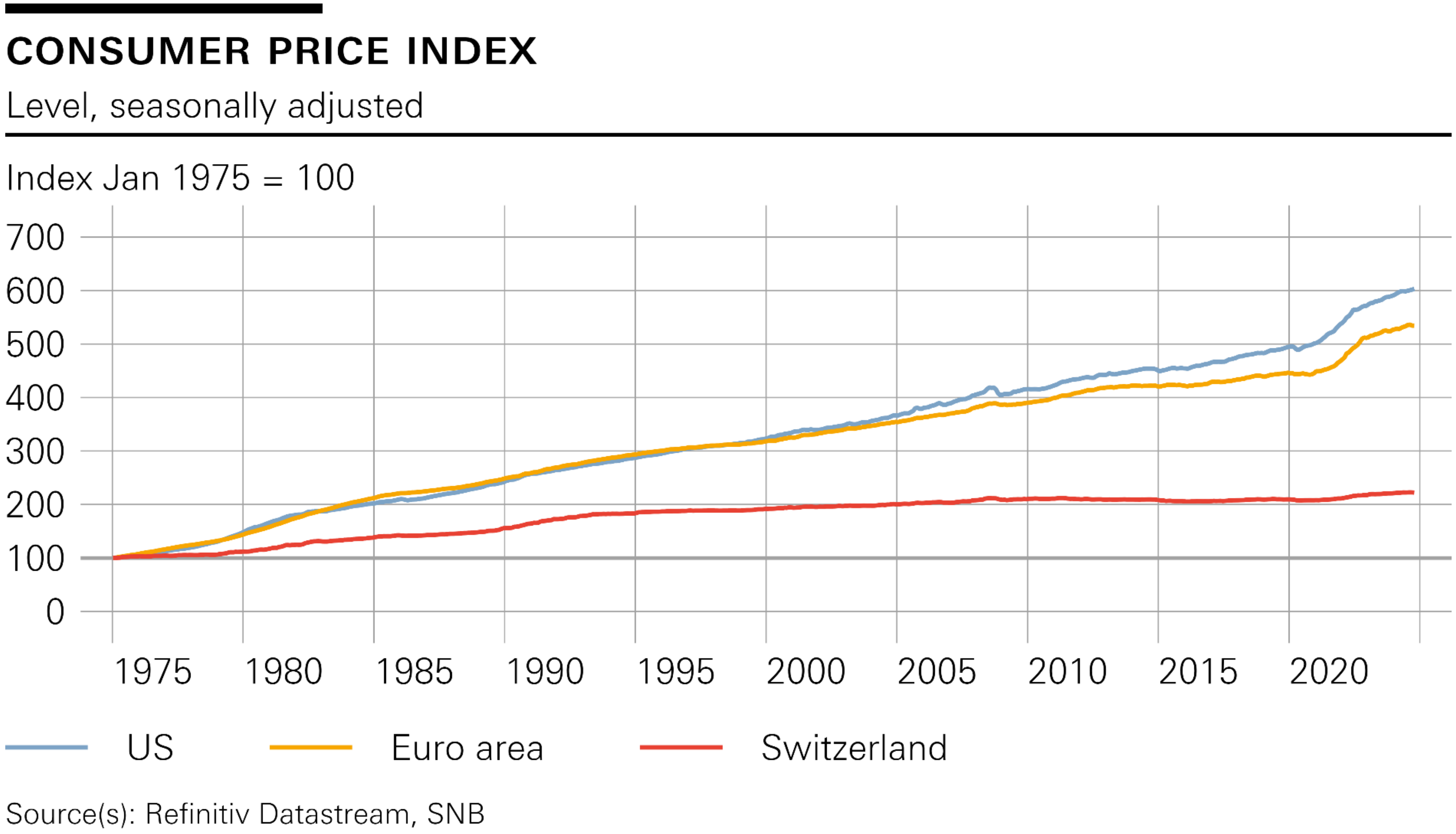
Monetary policy strategy

- Monetary policy strategy: explains how the SNB operationalises its mandate to ensure price stability.

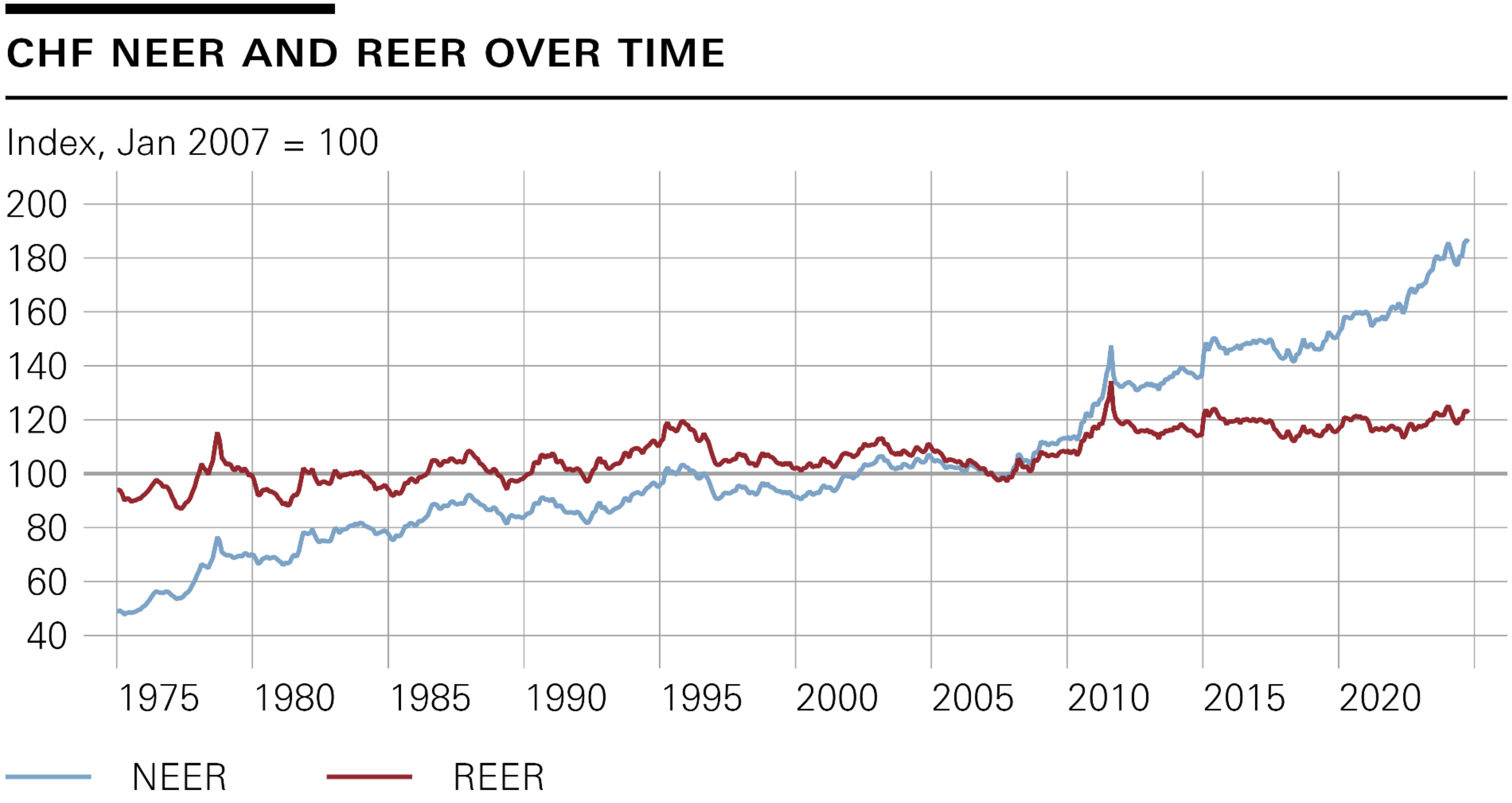
- Three elements:
  1. **Definition of price stability**
  2. **Conditional inflation forecast**: the main indicator for monetary policy and a central instrument of communication
  3. **Description of how the SNB implements its monetary policy**: To ensure price stability, the SNB maintains appropriate monetary conditions. These are determined by the interest rate level and exchange rates. The SNB sets the level of the SNB policy rate. In so doing, it seeks to keep the secured short-term Swiss franc money market rates close to the SNB policy rate. The most important secured short-term Swiss franc interest rate is SARON (Swiss Average Rate Overnight). If necessary, the SNB may also use additional monetary policy measures to influence the exchange rate or the interest rate level.

Three stylized facts and some challenges

1. Price stability as a long-run feature of the Swiss economy



2. A history of substantial movements of both the nominal and real exchange rate

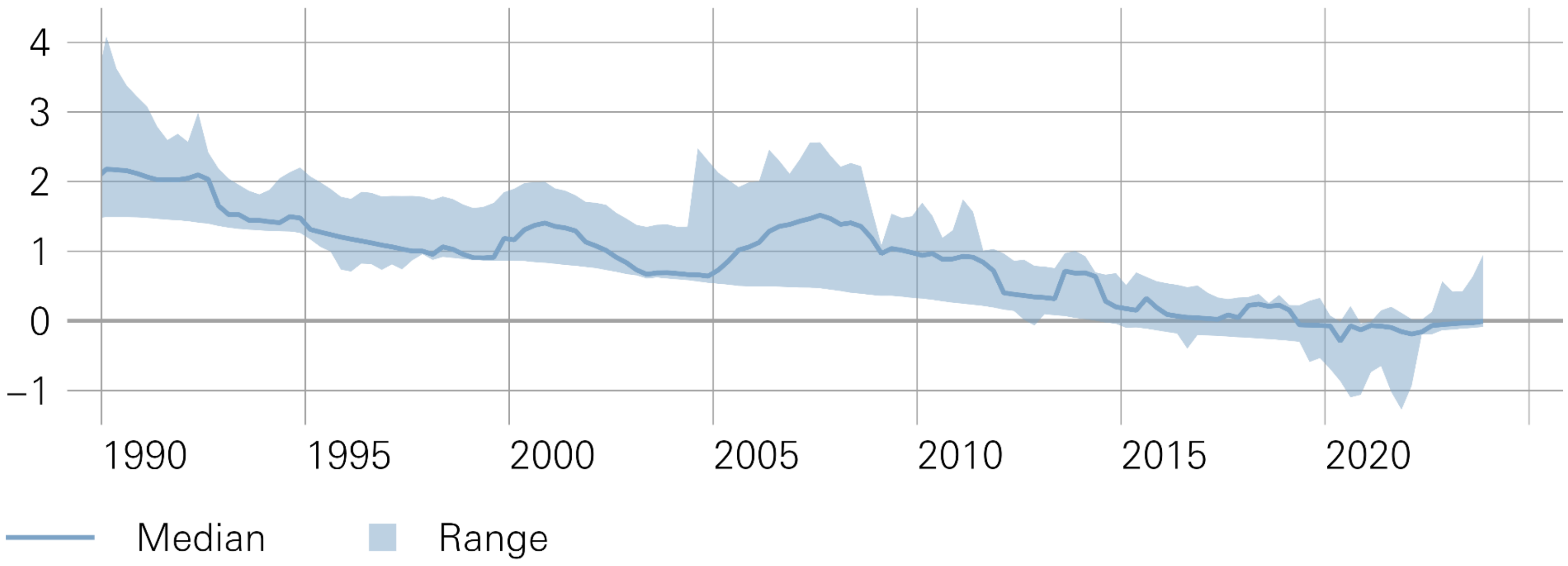


Source: SNB

3. r* estimates seem to have levelled-off after protracted downward trend

SWITZERLAND: RANGE AND MEDIAN OF r* ESTIMATES

In percent



Note: The range indicates the difference between the highest and lowest available r* estimates in each quarter.

Source(s): SNB

Safe-haven shocks

Triggers and form of safe-haven demand are diverse

Safe haven flows can be triggered by a variety of factors…

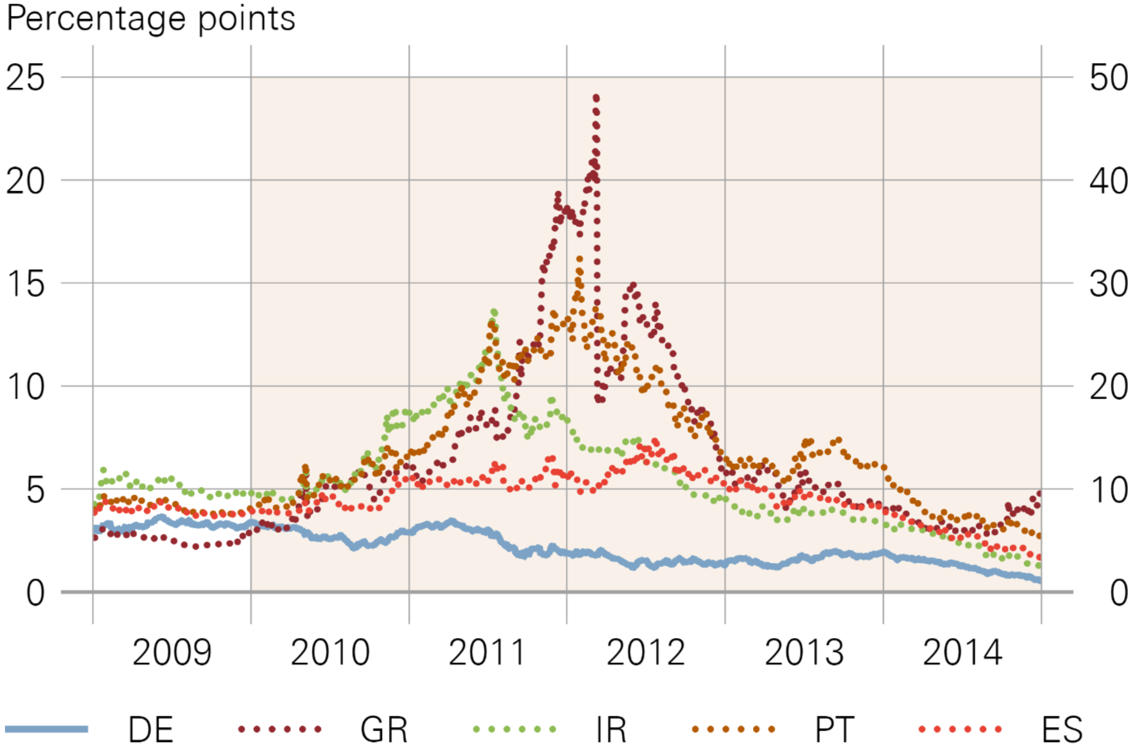
- Global financial and macroeconomic shocks (e.g. Euro area sovereign debt crisis, Covid-19)
- Geopolitical tensions (e.g. Russia's invasion of Ukraine)
- Political risks (e.g. Brexit, major elections)

…and their intensity and duration is difficult to predict

Example 1: Euro area sovereign debt crisis

WIDENING OF PERIPHERY BOND SPREADS

Government bond yields of selected eurozone countries



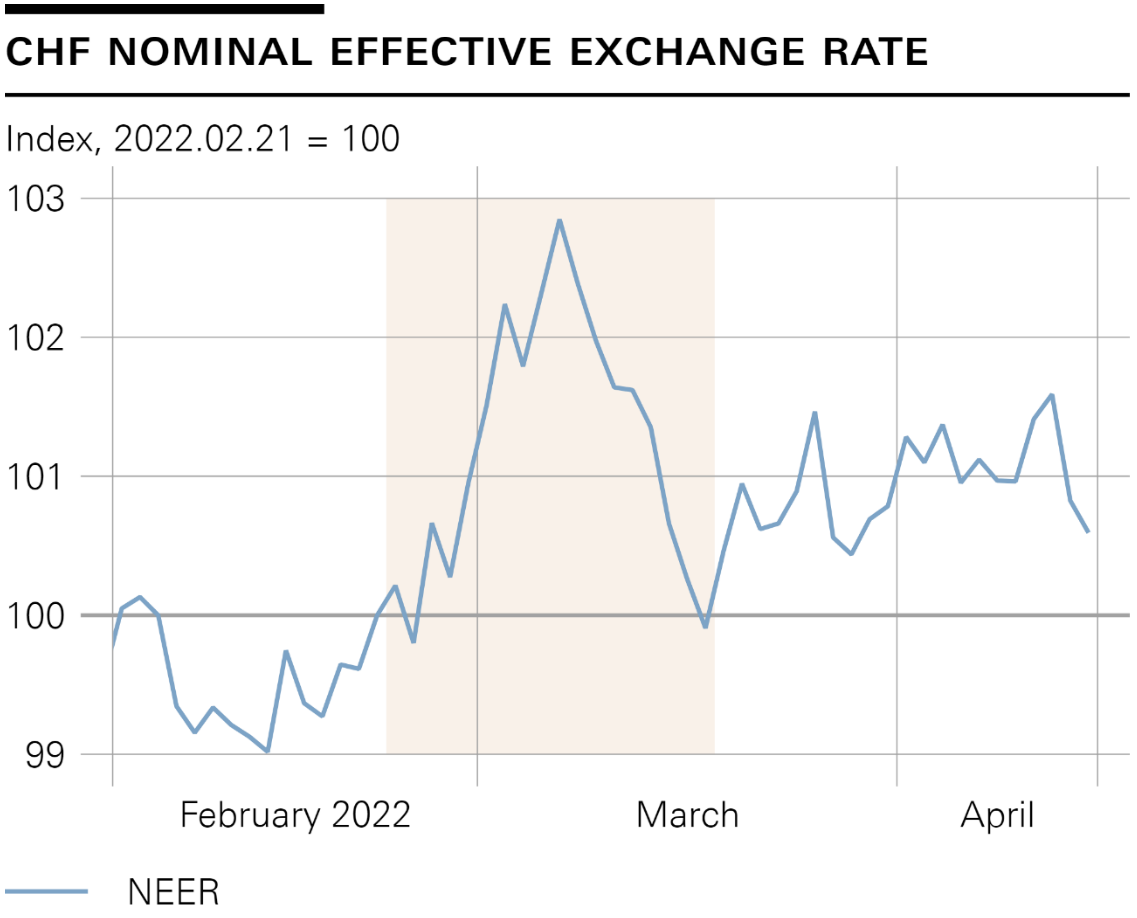
Sources: LSEG Datastream, SNB

CHF NOMINAL EFFECTIVE EXCHANGE RATE

Source: SNB

Example 2: Geopolitical tensions from Russia's war on Ukraine

Source: Caldara and Iacoviello, AER 2022

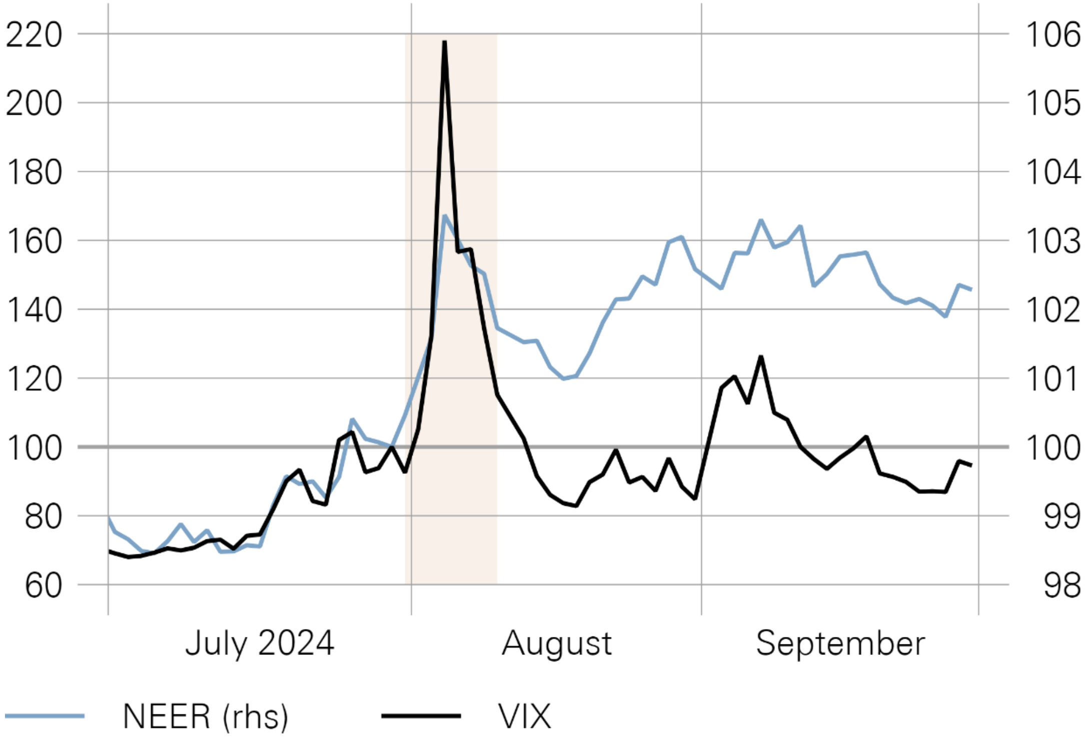


Source: SNB

Example 3: Uncertainty vs. Fed's policy repricing

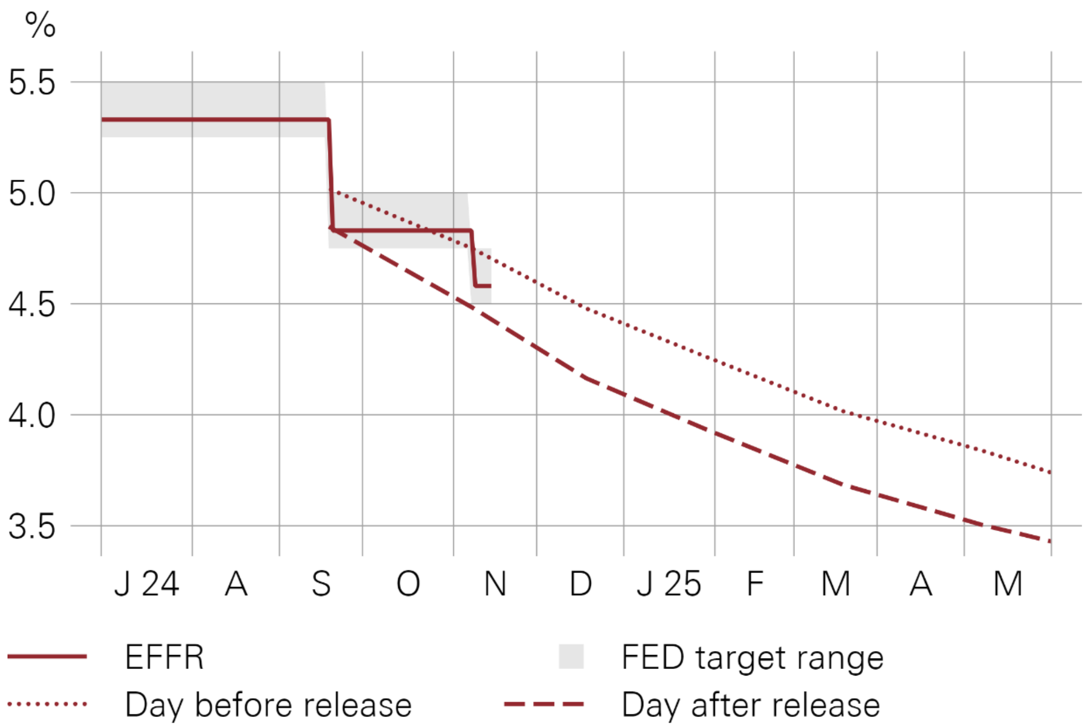
CHF NOMINAL EFFECTIVE EXCHANGE RATE AND VIX

Index, 2024.07.30 = 100



FED POLICY RATE EXPECTATIONS

Derived from meeting-dated OIS contracts



Sources: Bloomberg, SNB

Conclusion

- SNB's policy rate is the SNB's main policy instrument. But monetary policy strategy allows for needed flexibility.

- Movements in the nominal and real exchange rate can vary substantially in terms of their drivers, magnitude, duration and the context in which they occur.

- No mechanical link between nominal exchange rate movements and policy reaction. Price stability goal is always the ultimate guidance.

Thank you for your attention.

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