The Riksbank's Company Interviews

JANUARY 2012

The Riksbank's company interviews in January 2012

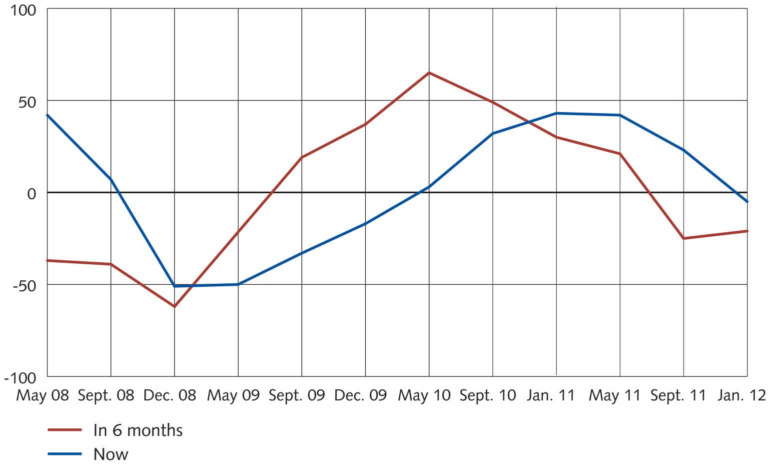
Cutbacks in a weaker economic climate

The company interviews conducted by the Riksbank in January 2012[1] reveal that demand weakened towards the end of last year and the manufacturing companies began to cut back their production levels and the number of jobs. The companies still say that their workforces are somewhat too large at present and we can thus expect further job cuts. Expectations of a fall in new orders also indicate that development will be weak in the period ahead and the companies believe that the economic climate will deteriorate in the six months ahead. Fewer companies believe that they will be able to increase prices during the year given the fall in demand, but also as a result of lower purchasing costs. The weaker economic climate has not yet had any tangible impact on investment. Given the improvements in profitability in recent years and the increases in operational flexibility, the companies appear to be equipped to face a period of weaker economic activity.

Following the wait-and-see phase that the companies described in the previous survey in September 2011, demand has fallen and economic activity has declined. All-in-all, economic activity is expected to weaken further over the next six months and some cutbacks in production and employment have already been made in the manufacturing industry. However, companies in the retail sector are somewhat more optimistic about the course of development over the next six months and sales volumes are expected to increase slightly in the first quarter. In general the companies feel that 2011 was a good year, but that demand weakened during the fourth quarter. The situation is, however, not the same as during the crisis of 2008–2009. One comment was that: "The economic situation is more like a hammock than a bungee jump this time". The difference today is that access to funding is regarded as being more stable and the companies have learnt the lessons of the previous crisis. Given the improvements in profitability in recent years and the high level of flexibility in production and the use of labour, the companies give the impression that they are prepared to cope with a decline in economic activity.

1 This report presents the results of interviews that were mainly conducted between 9 January and 20 January 2012. As in January 2011, the interviews were conducted with a smaller sample; 24 companies were interviewed and the survey focused on the largest companies, with an emphasis on manufacturing companies. The total number of employees at these companies was approximately 200 000, compared to approximately 250 000 employees at 40 companies in September.

Figure 1. The economic climate
Weighted net figures



Note: Weighted net figures are based on the number of employees in Sweden at the interviewed companies. The question concerns the companies' assessment of the economic climate now and in six months' time. The net figures in the diagram represent the balance between the percentage of responses that the economic climate is good (is expected to be better) or poor (is expected to be worse).

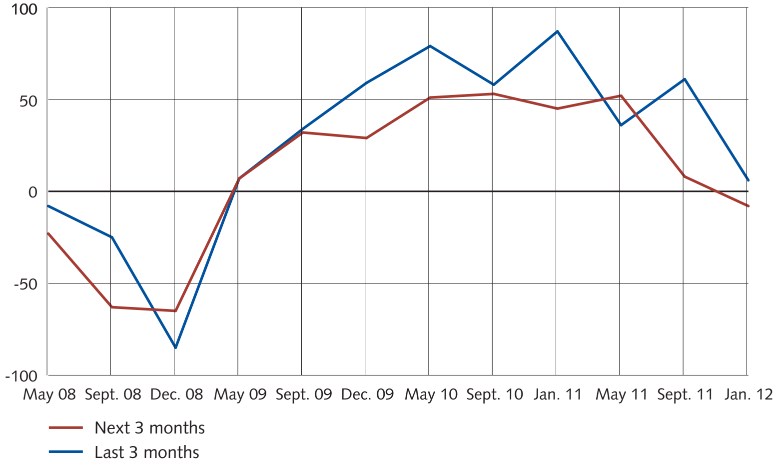
"THE DEVELOPMENT OF ECONOMIC ACTIVITY IN EUROPE WILL BE A MORE IMPORTANT FACTOR FOR DEMAND THAN NORMAL"

The manufacturing companies in particular described a clear decline in economic activity, above all on the export markets but also on the Swedish market. Order intake was weaker during the autumn and is expected to fall over the next three months (see Figure 2). The construction companies, which normally note a fall-off in economic activity later in the economic cycle, are still working on the order stock from 2010, but see a decline in the production of housing that is expected to have an impact on the production of new buildings in the period ahead.

The European market is the most important market for the majority of the export companies and demand has continued to decline. Development in the northern part of Europe is more stable compared to the markets in southern Europe, where economic activity is very weak. The weaker European demand, together with a stronger krona, has had a significant impact on the export companies. At present, there is no clear driving force on the other export markets that can compensate for the fall in demand in Europe and the transport companies also confirm the picture of declining global demand. Although the signals are somewhat divided, some companies feel that things are looking a little brighter on the US market, while activity in Asia and on emerging markets in other parts of the world appears to have levelled out at a high level.

It is clear that lower demand has had an impact on Swedish industry. However, although production volumes have fallen over the last three months, the companies have at the same time continued to build up their stocks, which, as in September, are seen as being somewhat too large. "Stocks are too large because companies haven't really adapted to the fall in demand" was one comment. The companies do not appear to be particularly concerned about this build-up of stocks, despite the fact that new orders are expected to fall in the three months ahead.

Figure 2. New orders
Weighted net figures



Note: Weighted net figures are based on the number of employees in Sweden at the interviewed companies. The question relates to order intake in the manufacturing and construction sectors over the last three months and an assessment of development over the next three months. The net figures in the diagram represent the balance between the percentage of responses that orders have increased (are expected to increase) or decreased (are expected to decrease).

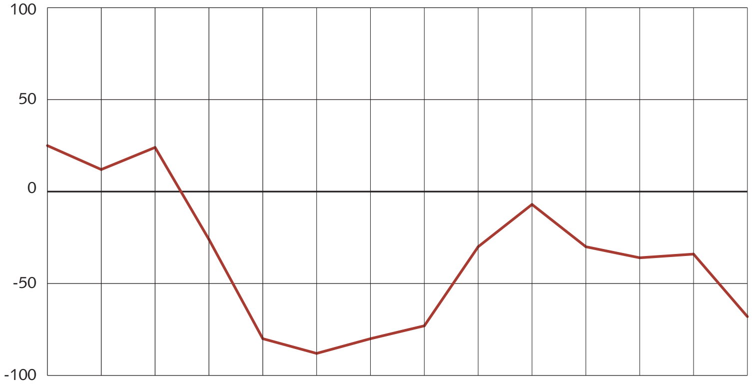
As in September, the companies' assessment is that the risks associated with the development of economic activity are extremely high and that these risks stem from the public-finance crisis in Europe and its impact on demand and exports. One of the main risks mentioned is that the crisis in Europe may lead to funding problems for the companies. Another is that a country may have to leave the monetary union, which could have serious consequences for growth in Europe.

The companies are adhering to their already adopted investment plans, but they are cautious about planning additional investment. The view of development six months ahead thus indicates that investment activity will remain largely unchanged compared to September. Although the companies say that funding conditions have deteriorated, it is the uncertainty about developments in Europe that explains why they are choosing not to increase investment. One company described the limited propensity to invest as follows: "Companies will only invest if there are really good reasons for doing so".

“THE ORDER BOOK MUST INCREASE, OTHERWISE WE WILL BE SOMEWHAT OVER-DIMENSIONED”.

In September, the companies said that there was a relatively high level of spare resources in the economy with a good supply of both labour and plant capacity. Resource utilisation has now fallen even further, particularly in the manufacturing industry. This is because output has declined over the last three months while the same plant capacity has been retained. Some companies said that they have retained capacity as they do not expect the downturn to be particularly severe or long lasting.

Figure 3. Indicator of spare capacity
Weighted net figures

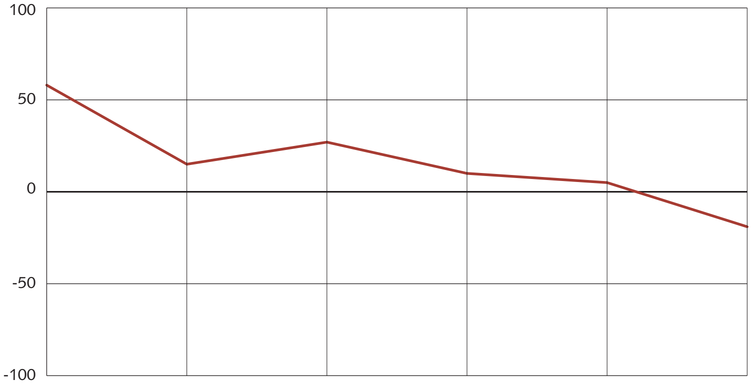


Note: The indicator of spare capacity is based on two different questions. Manufacturing sector companies were asked: What possibilities do you have to manage an unexpected increase in demand? Major problems, some problems or no problems. Other sectors were asked: Is there a shortage of labour? Yes or no. A positive net figure indicates high resource utilisation while a negative net figure indicates low resource utilisation. In the indicator above, the responses to these two questions have been combined with weighted percentages based on the number of employees in Sweden at the companies interviewed.

WORKFORCE TOO LARGE

For the first time for almost two years, the companies say that the workforce is too large in relation to production and sales (see Figure 4). A majority of the companies reported that they increased the number of employees over the same period (see Figure 5), which is well in line with the increase in employment in the economy as a whole. However, in January of this year the companies said that they reduced their workforces already at the end of 2011 and that they intend to continue to make job cuts in the period ahead. It thus appears that the continuous increase in the number of employees during the last two years has now come to an end.

Figure 4. Workforce in relation to production/sales
Weighted net figures



Note: Weighted net figures are based on the number of employees in Sweden at the interviewed companies. The question relates to the companies' assessments of the size of the workforce in relation to production/sales. The net figures in the diagram represent the balance between the percentage of companies stating that the workforce is too small and those stating that it is too large.

No major redundancies have been announced in the manufacturing industry, but minor cutbacks have been made that have mainly affected temporary employees (those on fixed-term and other limited contracts, consultants and so on) and personnel from employment agencies. The employment agencies confirm that some contracts in the manufacturing industry were cancelled in late 2011. Manufacturing companies also said that the current high exchange rate for the krona, and the fact that this reduces competitiveness, will maintain the pressure to rationalise operations and that further job cuts cannot therefore be ruled out.

Figure 5. Employment
Weighted net figures

Note: Weighted net figures are based on the number of employees in Sweden at the interviewed companies. The question relates to the companies' assessments regarding employment in the last and the next three months. The net figures in the figure represent the balance between the percentage of responses that employment has increased (is expected to increase) or decreased (is expected to decrease).

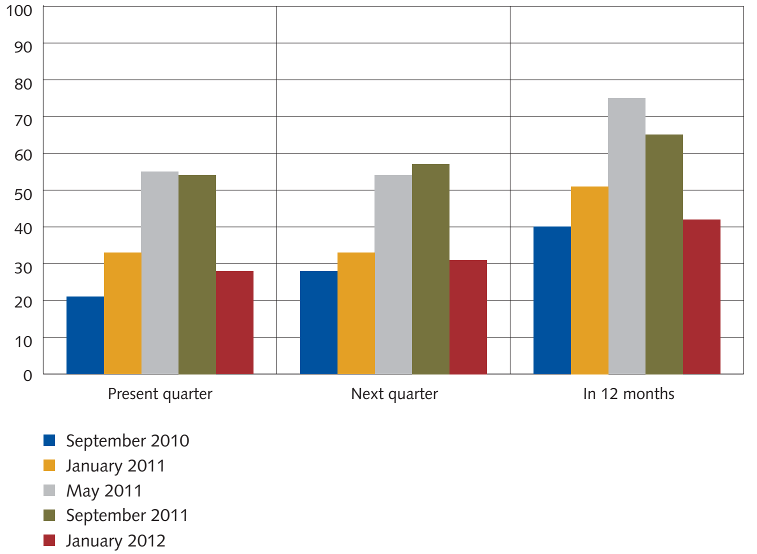
LIMITED WAGE DRIFT

The round of collective bargaining in the manufacturing industry was completed in the autumn. The companies' present view of the increase in wage costs in the year ahead does not differ significantly from their view in September. In general they expect wage drift (wage increases over and above those in collective agreements) to fall somewhat compared to what they believed in previous interviews. This is linked to the companies' expectations of a general weakening of demand which in turn is expected to affect the demand for labour and thus wage drift.

"NO-ONE DARES TO RAISE PRICES NOW – BUT NO-ONE DARES TO LOWER PRICES EITHER"

The decline in economic activity and the concern about the future have had a significant impact on the companies' pricing plans. As can be seen in Figure 6, a majority of the companies are still expected to continue to raise prices, but far fewer than in September. This applies to all three time horizons (present quarter, next quarter and in 12 months' time). Many companies were also cautious when talking about the size of the price increases and the possibility to actually implement them. In the latter case it is often the level of competition and the behaviour of the competitors that ultimately decides whether price increases can actually be realised. This also makes it difficult to reduce prices as the companies risk losing income it their competitors also cut their prices. A compilation of the companies' responses indicates that price increases will be well under two per cent looking one year ahead. It should, however, be pointed out that the survey mainly covers companies that sell their goods and services to other companies (this is true, for example, for most of the manufacturing companies in the survey) and that consequently their pricing plans do not relate to consumer prices. Nevertheless, it appears that the possibility of the companies to increase their prices is relatively limited in the present economic climate, and much more limited than in September.

Figure 6. The companies' planned price increases
Weighted net figures

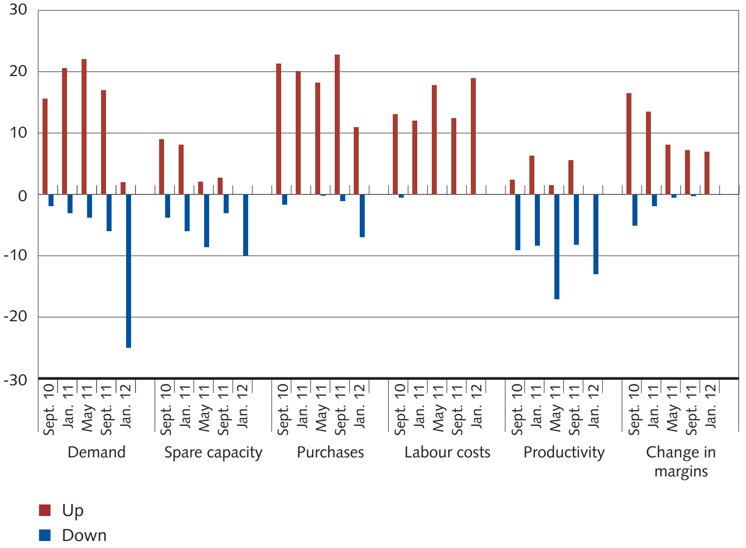


Note: Weighted net figures are based on the number of employees in Sweden at the interviewed companies. The columns show the net percentage of companies that intend to increase their prices in the present quarter, next quarter or next 12 months. Each column relates to the responses in a particular survey.

REDUCED DEMAND HOLDING BACK PRICE INCREASES

Reduced demand is the main reason why fewer companies believe that they will be able to increase their prices (see Figure 7). The figure also shows to what extent other factors affect pricing one year ahead (upwards or downwards). From the autumn of 2010 and throughout 2011, high demand was one of the most important reasons given by the companies for the fact that they were able to increase prices (illustrated by the red columns in Figure 7), while a few companies said that the demand situation would squeeze prices downwards (blue columns). The economic climate also improved during this period, but the percentage of companies reporting that the demand situation could lead to price reductions gradually increased during the course of 2011. The really significant turnaround came in January this year in that a majority of the companies then said that the fall in demand was squeezing prices. Weak demand also tends to lead to more spare capacity at the companies and this also seems to exert downward pressure on the level of prices.

Figure 7. Factors that will affect pricing in the coming twelve months
Weighted percentages



Note: Weighted percentages are based on the number of employees in Sweden at the interviewed companies. The columns show the relative percentages for the different factors affecting prices upwards or downwards 12 months ahead.

Of the other factors, wage costs are mentioned as a common cause of price increases, as well as the prices of purchased and input goods ("Wage costs" and Input goods" in Figure 7). However, it is worth noting that more companies than ever before now say that purchasing prices are keeping down their own prices. In discussions with the companies it emerged that several international commodity prices had fallen during the year and that the stronger Swedish krona also means that the prices of input goods purchased abroad have been held back or fallen when converted to Swedish krona.

A fairly constant proportion of the companies say that the need or the possibility to increase their own margins is an important reason for increasing prices. This proportion has not changed since the previous survey in September and has remained relatively constant in net terms since autumn 2010. This in turn may be because many companies have been satisfied with the development of profitability during the upturn following the financial crisis. In January, however, assessments of profitability were somewhat lower than the previously relatively high levels.

One conclusion regarding the companies' pricing in the period ahead is that demand is generally of great significance and that the companies are now feeling the effects of a decline in demand that is also affecting their pricing plans. Another conclusion is that many companies are finding it difficult to increase their prices for other reasons that have become apparent during the interviews. The level of competition on the market and the behaviour of the competitors are, for example, important to pricing, and prices are also affected by the development of prices for input goods and by the relatively strong krona.

FUNDING MORE EXPENSIVE AND MORE COMPLICATED

Following the difficulties that several companies experienced in obtaining external funding during the autumn of 2008, the funding situation has steadily improved. However, the companies' responses concerning access to external funding, both in September and in January, indicate that it has become increasingly expensive and complicated to get bank loans. The companies report several examples in which the banks have been reluctant to grant new loans or renegotiate lines of credit; that is a promise to provide access to loans. This reluctance may, for example, be demonstrated by the banks quoting unreasonable interest rates or loan conditions. According to the companies, the behaviour of the banks may be due to an inability to grant new loans because they are now subject to new, stricter capital requirements. In the case of the large companies with operations abroad, the loan volumes or credit lines they are looking for are so large that several international banks often become involved. But even in such cases it happens that some banks pull out of the deal. This in turn may be because an individual bank feels that it already has a substantial exposure to a certain country or a certain sector and instead wishes to spread the risks by doing business with other borrowers. Companies reported during the financial crisis of a few years ago that some international banks withdrew to their "domestic markets" in order to concentrate on the customers they were closest to. For the large Swedish companies it is therefore even more important to negotiate with many banks and to use the international bond market to ensure that they get adequate funding.

It is important to point out that the companies do not believe that conditions on the credit markets are anything like as bad as they were in the autumn of 2008, and that the companies are able to meet their funding needs. It is of course the case that profitable and well-known companies find it easier to arrange funding than smaller companies with a higher level of debt.

Sveriges Riksbank
SE - 102 37 Stockholm

Tel +46 8 787 00 00
Fax +46 8 21 05 31
registratorn@riksbank.se
www.riksbank.se