



The Riksbank's Business Survey

MAY 2014

SMALL STEPS TOWARDS STRONGER ECONOMIC ACTIVITY AND RISING PRICES

■ The Riksbank's business survey in May 2014

According to the business survey conducted by the Riksbank in May 2014, economic activity has strengthened since January. The improvements are small but are noticeable in most sectors. Increased demand from abroad has benefited the export companies at the same time as domestic demand has strengthened, in part due to an increase in housing construction and rising household consumption.

Economic activity in Sweden is expected to continue to strengthen in the period ahead although there are risks of setbacks in the global economy, for example as a result of concern about developments in China. A great challenge facing the companies is weak profitability due to fierce competition. To raise productivity they plan to increase investments in new technology.

Over the past year, price increases have been held back by weak demand, strong competition and relatively low cost increases for wages and intermediate goods. Expectations of an improved economic climate in the period ahead mean that the companies are planning to increase prices and at the same time improve margins. However, overall price increases are expected to be moderate over the next 12 months and will be highly dependent on the development of economic activity.

Prior to each Monetary Policy Report, three times a year, the Riksbank interviews the largest companies in the construction, retail, manufacturing and service sectors. Representatives of 46 companies with a total of approximately 276,000 employees in Sweden were interviewed this time. The interviews were mainly held between 2 and 26 May and the results are presented in this report.

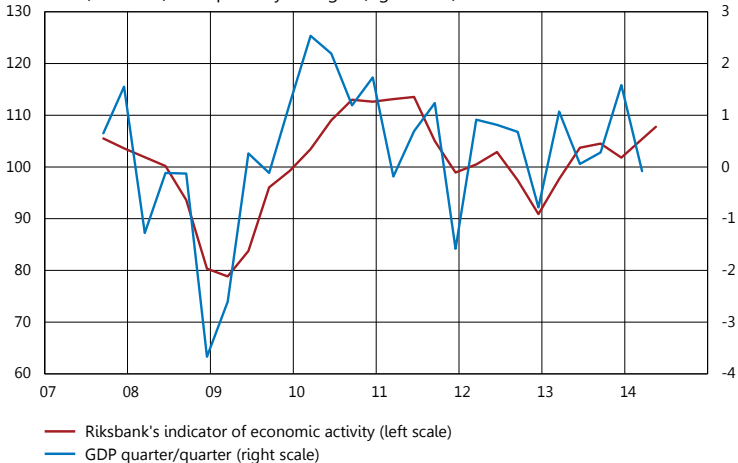
"THINGS ARE SLOWLY MOVING IN THE RIGHT DIRECTION"

The Business Survey's overall indicator¹ suggests that the economic situation is better than in January, see Figure 1. The companies' com-

¹ The indicator is calculated as an average of the responses to the questions on production volumes, employment, investment plans, profitability and the development of productivity and prices. The questions are then weighed together on the basis of their ability to predict seasonally-adjusted GDP changes from quarter to quarter. The indicator is calculated up to two months before the quarterly outcome of GDP is published and provides an early indication of developments in economic activity.

ments also indicate that they expect to see an ongoing, although slow, recovery.

Figure 1. **The Riksbank's indicator of economic activity and changes in GDP**
Index (left scale) and quarterly changes (right scale)



Note. The Business Survey is carried out three times a year. The indicator has been standardised so that the mean value = 100 and the standard deviation = 10. This means that a value above (below) 100 should be interpreted as a somewhat stronger (weaker) business cycle than the average. Figures for quarterly GDP growth are seasonally adjusted.

Assessments of the economic situation still differ from sector to sector. The construction sector is going well and is benefiting from the positive effects of significant migration to the major cities and the consequent increased demand for housing. The consumer-related sectors continue to benefit from increasing household incomes, which are strengthening consumption overall. The situation is satisfactory in the manufacturing sector, but figures for new orders and production are relatively weak.

The companies also believe that the recovery will continue in the period ahead, see Figure 2.

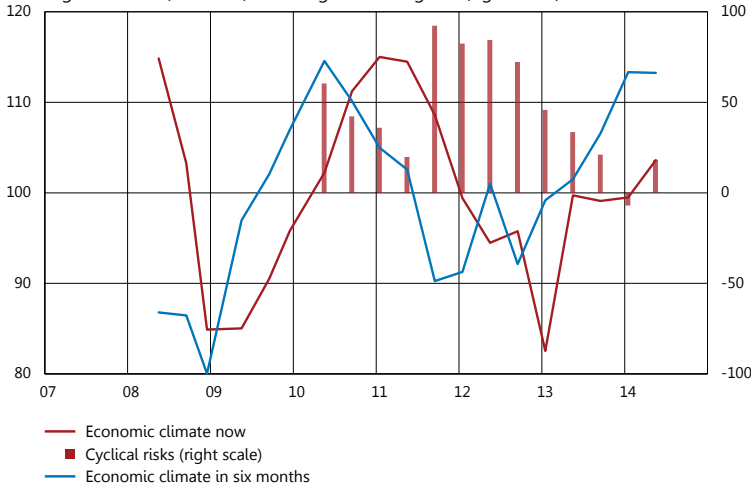
"WE SEE A MORE STABLE EUROPE"

There are still companies that express concern about a weakening of economic activity, but the risks have changed. Previously, the companies often spoke about a negative course of development in Europe as the greatest cyclical risk. This risk is now perceived to be less acute: "The risks stemming from the euro crisis have waned and are not on the agenda at the moment."

Companies that do business on global markets instead highlight the situation in the BRIC countries (Brazil, Russia, India and China) as a new source of concern about the development of economic activity.

The comments mainly relate to China, where there are several types of risk that may have a negative impact on global economic activity.

Figure 2. **The economic climate now and in the future**
Weighted index (left scale) and weighted net figures (right scale)



Note. The index shows a standardised value (mean value = 100 and standard deviation = 10) for the balance between the percentage of responses that the economic situation is good or bad and that the situation will be better or worse in six months' time. The net figures show the balance for responses that cyclical risk is perceived to be higher or lower than normal.

Apart from a general decline in demand, the companies also mention the problems relating to the shadow banking sector in China and the high levels of debt in the country.

Although the Swedish export companies' direct sales to China are relatively limited, the assessment is that the contagion effects of potential problems could be extensive and serious. For example, China has a lot of influence on the global market prices of several commodities, which can have an indirect effect on the sales of Swedish companies.

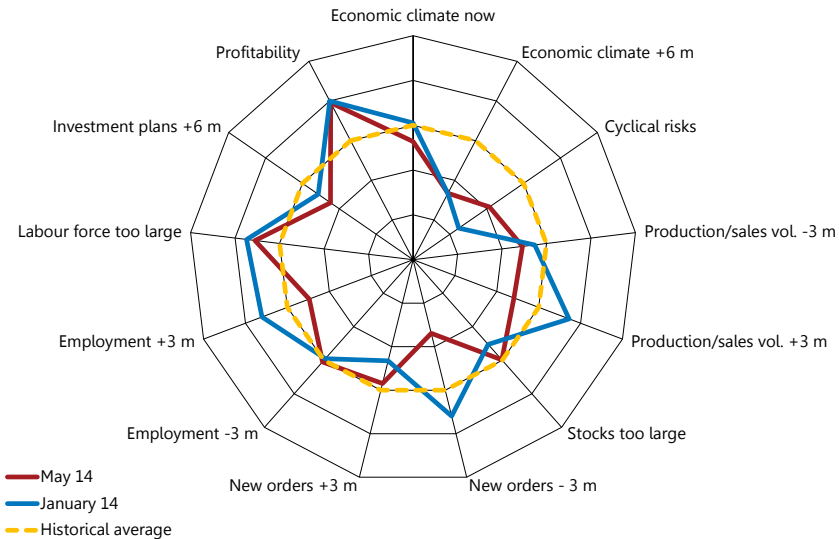
Several of the interviewed companies also reported that they were affected in May by the turbulent situation in Ukraine. However, they also reported that their concern is not based on any impact on their order or sales figures; it is rather a question of a more general unease.

"SLUGGISH BUT MARKED UPTURN"

The companies' overall assessment was that the figures for production, sales and new orders have improved since January, see Figure 3. The responses to most of the questions are also above their historical averages, which means that more companies than usual believe in an upturn. The companies also predict increased production, sales and

employment in the quarter ahead and this hope is strengthened by the increase in new orders in recent months.

Figure 3. **The companies' overall response patterns**
Weighted index



Note. The responses to the questions are plotted along a "spoke" in the figure and an index figure closer to the centre entails an improvement. The historical averages are calculated for the periods since the questions have been asked. The term -3m / +3m refers to the most recent three months and the coming three months respectively. +6m refers to the coming six months.

Several large manufacturing companies that do business on global markets are still cautious in their assessments of the period immediately ahead. These companies are also often dissatisfied with their profitability. The reason in many cases is a low level of resource utilisation resulting from relatively small production volumes. Several export companies also mentioned increasing international competition and the relatively strong krona as factors that are counteracting a rapid economic upswing.

"IN GENERAL, IT'S EASIER TO ACCESS CAPITAL"

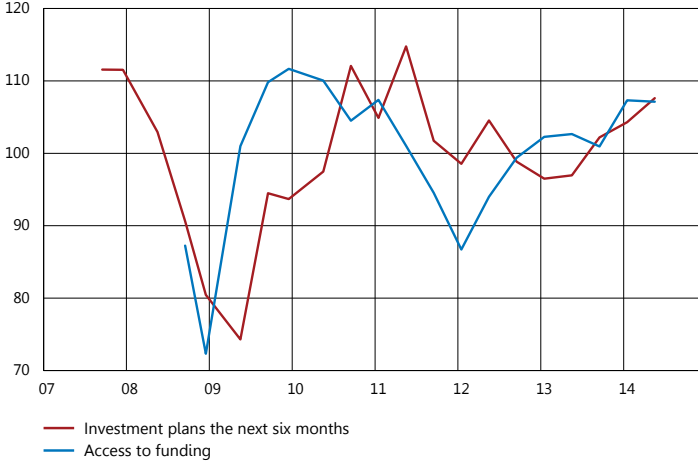
The companies' investment plans indicate a slight increase in investment over the next six months, see Figure 4. In the manufacturing sector, most investments will be made due to the need to change to more energy-efficient and automated production methods.

The consumer-related companies usually report unchanged or increasing investment plans. Most of their investments relate to the development of IT systems, improved logistic flows and other technical solutions to improve productivity.

The companies' funding situation continues to improve and in May no company reported that the situation had worsened. Funding is

increasingly conducted on the securities markets, where the companies are offered good terms and conditions. One company representative expressed this by saying: "We have no problems at all in accessing capital, we can usually close a deal in the course of a morning."

Figure 4. **Investment plans and access to external funding**
Weighted index



Note. Indexes show a standardised value (mean value = 100 and standard deviation = 10) for the balance between the percentage of responses that planned investments will increase or decrease over the next six months and whether access to funding has improved or worsened over the last three months.

NO GENERAL SHORTAGE OF LABOUR

In May, few companies reported that they were finding it difficult to recruit staff, see Figure 5. However, as in previous surveys, several companies reported that it is still difficult to recruit personnel with special skills and expertise. The specialists mentioned include supervisors in the construction sector, sales staff, engineers and some management categories. The way the companies deal with these shortages differs from sector to sector. The service companies recruit foreign personnel to a greater extent, have larger wage differentials than other companies and work with attractive benefit packages. Some retail companies deal with the problem by using overtime and re-prioritising tasks, while the construction companies turn down assignments that require many specialists.

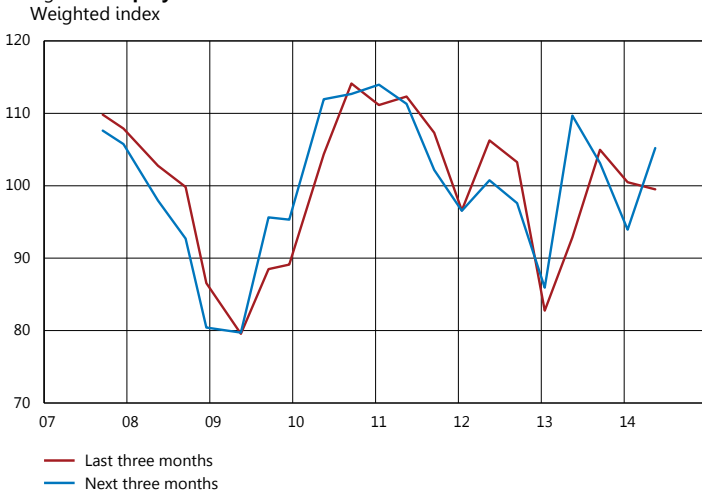
Figure 5. **Labour shortages**



Note. Index shows a standardised value (mean value = 100 and standard deviation = 10) for the balance between the percentage of responses that there is shortage of labour or not.

Slightly more companies than previously have reduced their labour forces over the last three months, see Figure 6. Labour-force cutbacks have been underway in most sectors for several years now, and this adjustment is continuing in the manufacturing sector. In other sectors, employment is expected to increase over the next quarter, which appears to be in line with the increase in domestic demand in the retail and other service-producing sectors.

Figure 6. **Employment now and in the future**



Note. The index shows a standardised value (mean value = 100 and standard deviation = 10) for the balance between the percentage of responses that employment has increased or decreased and whether it will increase or decrease in the future.

"WAGE EXPECTATIONS HAVE BECOME MORE REALISTIC"

On the whole, wage costs have developed in accordance with wage agreements and the companies believe that they will continue to do so in the year ahead. However, wages adapt slowly to the general price level and one company representative commented on this by saying: "Inflation is low and sooner or later wage costs will have to adapt to that too".

Several retail and service companies were particularly uncertain about how wage costs will develop in the period ahead. These companies indicated that wage costs may increase in the future if employers' contributions are increased following the general election in the autumn. This relates primarily to companies that to a large extent offer jobs to young people and where the requirements for professional skills or educational qualifications are lower.

ADDITIONAL QUESTIONS ON COSTS AND MARGINS

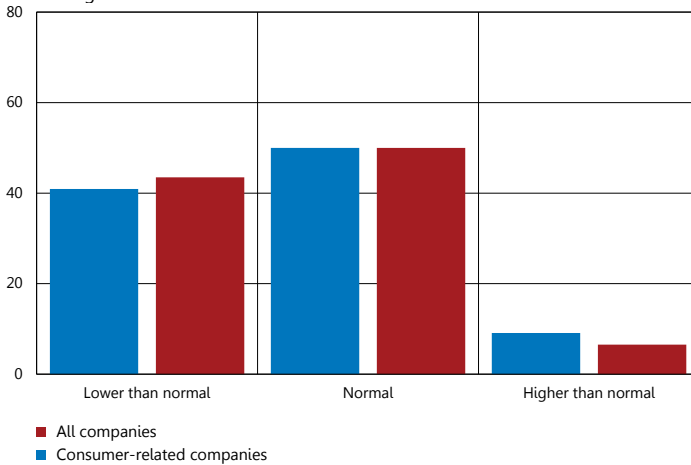
In April, the Riksbank, in cooperation with the National Institute of Economic Research, circulated a survey to a large number of companies with questions about their costs, margins and prices. The aim was to determine what affects the companies' pricing and thus to contribute to a more in-depth analysis of inflation.

As a complement to this survey, the Riksbank has now interviewed more companies that sell goods or services directly to private individuals than previously. The interviews in May also comprised several new questions on the companies' cost increases and margins; questions that were also central in the larger survey. As usual, the Riksbank's Business Survey only covers large companies in the respective sectors. There may systematic differences between large and small companies, which means that the results here may differ from those in the larger survey.

"THERE IS NO PARTICULAR PRESSURE ON COSTS"

Approximately half of the companies responded that both cost increases and margins have been more or less as usual over the last 12 months. More companies also responded that cost increases have been lower rather than higher than normal, see Figure 7.

Figure 7. **Companies' total cost increases over the last 12 months**
Percentage share



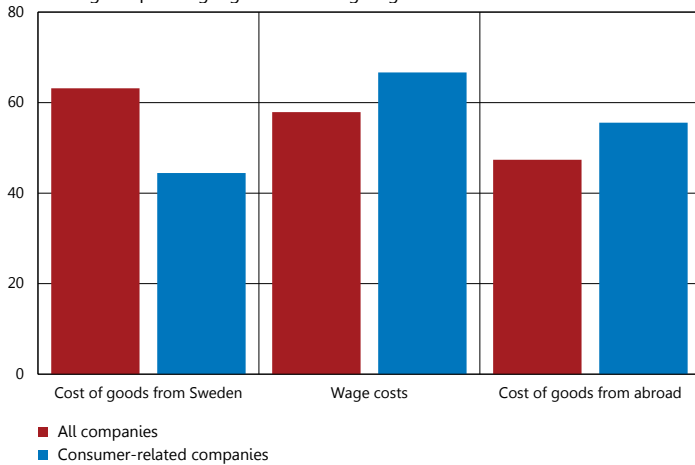
Note. The question was worded as follows: How have the total cost increases for a representative good or service developed over the last 12 months?

"WAGE COSTS HAVE INCREASED LESS THAN NORMAL"

A factor common to all of the companies is that the largest cost items are intermediate goods and wages, which on average account for approximately two thirds of their total costs. It is also these two items that are the most significant factors behind the slower than normal increase in costs.

Several of the consumer-related companies reported that wage costs were the most significant factor, while the purchase of goods and services from abroad was the second most significant. These companies also said that the lower costs for purchases abroad were due to the relatively strong krona. One comment was: "We have no inflation because we import goods – and they are not expensive."

Figure 8. **Most significant factors behind the lower than normal cost increases**
Percentage responding high or rather high significance



Note. The question was worded as follows: How significant have the following factors been for the total cost increases for a representative good or service being lower than normal over the last 12 months? The factors listed were wage costs, funding costs, transport costs, costs for premises, costs for the purchase of goods and services in Sweden, costs for the purchase of goods and services abroad and other (the respondents could specify what). The factors were then graded on a scale where 4 = High significance, 3 = rather high significance, 2 = some significance and 1 = no significance.

MARGINS HAVE BEEN NORMAL

The companies' margins have been as normal over the last 12 months, see Figure 9. The development of the margins has also been as expected. Several of the consumer-related companies reported that their margins had been higher than normal over the past year. The most important explanation of this is that cost increases were lower than usual. This is also in line with the companies' responses to the question about cost increases over the last 12 months.

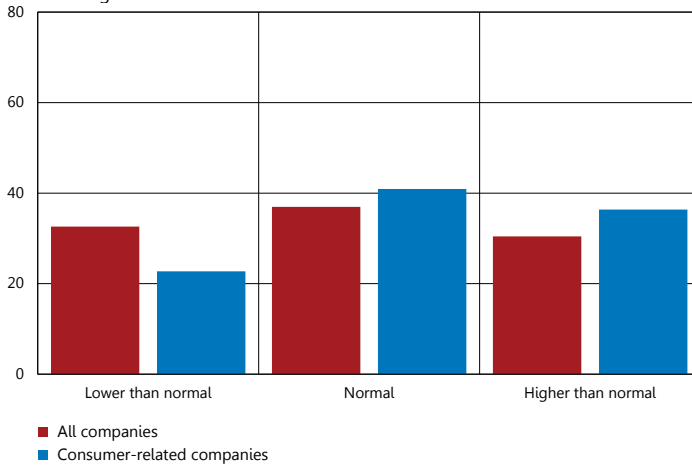
"E-COMMERCE OVER TIME? EVERYONE BELIEVES IT WILL INCREASE"

Those companies that responded that margins have been *lower* than normal over the last 12 months also said that the most significant factors are that competition has been more severe than normal and that demand has been lower than normal.

In the case of the consumer-related companies, competition has increased mainly due to new ways of doing business. Examples mentioned include e-commerce and price comparison websites which make it easier for small companies and foreign companies to compete for the same customers as the established Swedish companies.

Export companies are facing fiercer competition because demand has been low since the financial crisis. They are competing with more or less the same companies as before the crisis, but for a smaller and smaller market.

Figure 9. **Margins/price mark-ups over the last 12 months**
Percentage share



Note. The question was worded as follows: How have margins/price mark-ups for a representative good or service developed over the last 12 months?

"PRICING IS BASED ON LOCAL CONDITIONS"

In May, the companies were asked how often they change their prices and if it has become more common for them to offer discounts. Campaigns have become much more common in the non-durable goods segment, which is largely because competition between local shops has increased.

Travel and airline companies change their prices several times per hour and make price cuts on an ongoing basis. For these companies it is important to always have full capacity, which is achieved with the help of improved IT systems that enable increasingly rapid price adjustments in line with supply and demand.

Those companies whose customers are other companies report an increasingly tough negotiating situation in which purchasing departments in both the private and public sectors have improved and become more price conscious. This has led to an increase in the number as well as the size of the discounts offered.

Companies in the manufacturing sector seldom change their price lists, usually no more than once or twice per year. Discounts and special agreements are the rule rather than the exception and list prices act more as benchmark in relation to the companies' competitors.

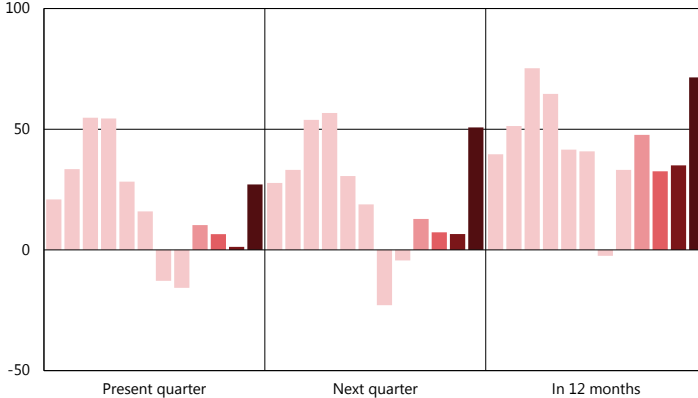
"WE ARE NOW PLANNING TO INCREASE OUR PRICES"

The optimistic view of the economic climate in the period ahead is also reflected in the companies' pricing plans. There are now more companies than previously that plan to raise their prices in the period

ahead, see Figure 10. The level of the planned price increases is low in many cases and few companies mentioned increases of more than two per cent over the next 12 months. One comment was: "We'll be happy if we manage one per cent." Some company representatives also expressed concern about being the first to increase prices, which could lead to a loss of market shares.

The consumer-related companies and the manufacturing companies still believe in lower price increases in the period ahead than the construction companies and employment agencies do. The latter are planning for price increases averaging over two per cent.

Figure 10. **Planned price changes**
Weighted net figures



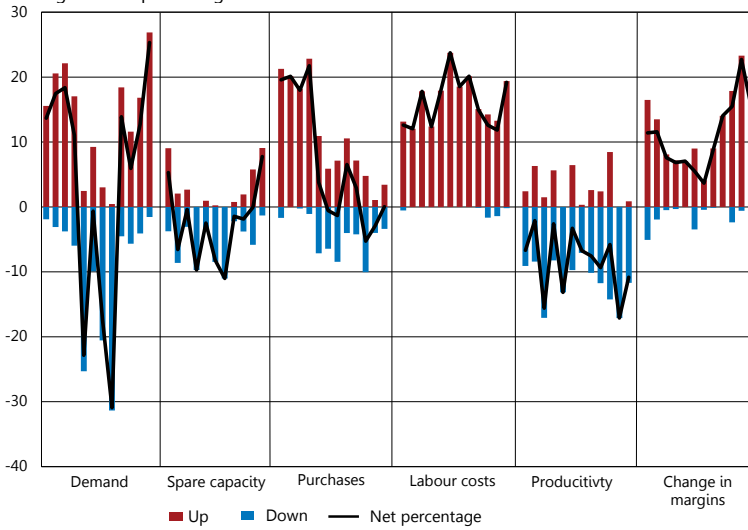
Note. The columns show the net figures for the companies that intend to increase/lower their prices during the present quarter, next quarter or next 12 months. The darker columns relate to the last four surveys.

"HIGHER DEMAND WILL PROVIDE SCOPE FOR PRICE INCREASES"

As previously, the companies consider that higher demand is the most important factor for higher prices, see Figure 11. Strong competition, both domestically and globally, in combination with low demand have previously held back price increases. When demand increases, material and wage costs are also expected to increase, which in turn will increase the need to raise prices.

The factor that is most expected to hold back price increases is a positive development of productivity, which is expected to reduce costs and provide scope for improved margins.

Figure 11. **Factors behind pricing in the 12 months ahead**
Weighted net percentages



Note. The red bars show the percentage of responses that the factor will have an upward effect on prices, while the blue bars show the percentage of responses that the factor will have a downward effect on prices. The black lines show the net percentages.

In the May survey, there were smaller differences between the manufacturing and retail sectors than previously. Expectations that rising demand will provide scope for price increases and that wage costs will increase are clear in both sectors.

ABOUT THE RIKSBANK'S BUSINESS SURVEY

The survey aims to reflect developments in prices and economic activity in the manufacturing and construction industries, the retail sector and (parts of) the service sector. As a few companies account for a very large part of the Swedish business sector, relatively few interviews among these companies can provide information about a large part of the sector. Many of the interviewed companies also provide information about other parts of the business sector through their contacts with, for example, small and medium-sized companies.

The survey is carried out by Riksbank staff who visit the companies. The visits normally last about an hour. The interviews are usually conducted with members of the company's management. The discussions give the companies an opportunity to develop their answers and the interviewer the chance to ask more detailed follow-up questions. From time to time, specific questions are asked about current issues in monetary policy.

Around 40 companies are normally interviewed in May and September, and around 25 companies in January. Over 300 companies have taken part in the survey since it was started in 2007.

The diagrams in the report present the companies' responses weighted in terms of the respective companies' number of employees in Sweden. The indexes in the diagrams capture upturns and downturns in the pattern of responses well. These responses are then combined with the respondents' reflections on the questions. The May 2014 report presents the results of interviews with 46 companies, which were mainly held during the period 2-26 May.

A more detailed description of the survey can be found on the Riksbank's website: Hokkanen, Melin and Nilson (2012), "The Riksbank's Business Survey – a quick indicator of economic activity", Sveriges Riksbank Economic Review 2012:3.



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