



# The Riksbank's Company Interviews

DECEMBER 2008 – JANUARY 2009



## ■ The Riksbank's company interviews December 2008 – January 2009

### Ongoing decline in economic activity and increasing difficulties for the companies to find funding

*The companies the Riksbank has interviewed state that economic activity has further declined during the autumn. The decline is reflected, for example, by a rapid fall in orders and more difficult access to credit. Half of the companies in the survey state that access to external funding (including bank loans) has deteriorated over the past quarter. Several companies state that the situation worsened following the bankruptcy of the US investment bank Lehman Brothers. The companies' view of the future is generally pessimistic. Two out of three companies believe that the economic climate will be even worse in six months time.*

The Riksbank's interviews with Swedish companies were mainly conducted in December 2008. Approximately one fifth of the total of 60 interviews were conducted in early January.<sup>1</sup>

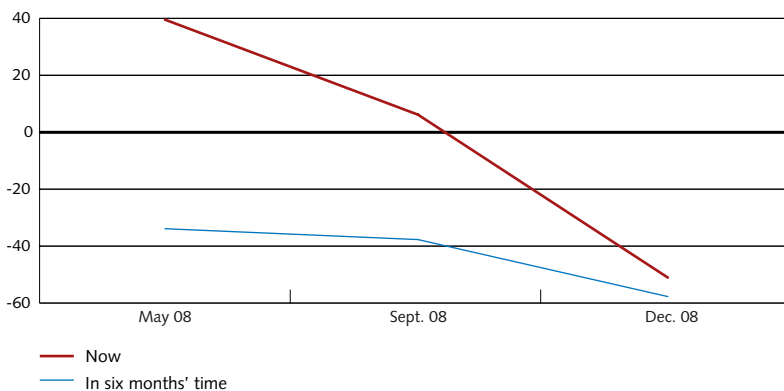
When the companies were asked how they perceived the present economic situation, the majority described the situation as "Poor". In the previous survey in September, slightly more companies described the situation as "Good" compared with those who said the situation was "Poor". More than one in two companies now state that the current economic situation is poor and two out of three companies expected the situation to be even worse in six months' time (see Figure 1). The largest deterioration is among manufacturing companies. There are very few manufacturing companies in the survey that say that the situation is good. The situation in the construction sector and the retail trade is also considered to be poor.<sup>2</sup> Among the companies in the private services sector the dominant response is "poor", but not as clearly as in the other sectors.

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1 For a more detailed presentation of the survey's purpose, methods, sample etc, we refer to "The design of the Riksbank's company interviews" in this document.

2 The "net figures" presented illustrate the tendencies in the survey but the levels should be interpreted with a certain degree of caution as the number of companies interviewed is relatively small. The changes in net figures between the surveys appear, however, to correspond fairly well with the results of other surveys, for example the Business Tendency Survey of the National Institute of Economic Research. For more discussion see "The design of the Riksbank's company interviews" in this document.

Figure 1. Assessment of the economic climate now and in six months' time



Note. The net figures represent the balance between the percentage of companies that reported an increase and those that reported a decrease. The question concerns the companies' assessment of the economic climate now and in six months time. See also "The design of the Riksbank's company interviews" in this document.

Source: The Riksbank

## Rapid and broad decline in economic activity during the autumn

In the course of the Riksbank's discussions with the companies, many of the company representatives state that the decline in economic activity has been both exceptionally rapid and extensive. Some quotes from the company representatives that may illustrate the situation are, for example: "This is the weakest economic climate that we have experienced in 35 years"; "The market came to a crashing halt during the autumn". A large export company described the situation as follows: "At the start of October, the mental attitude changed in all sectors in all countries within the space of 14 days". Another major export company said that: "Something happened in November" in connection with a fall in the order intake of "several tens of per cent". The same company also noted that the demand for maintenance and repairs has declined and that this is a sign of a serious deterioration as the customers "obviously don't even need to keep their equipment running". Several manufacturing companies also said that there were longer production shutdowns than normal over the Christmas and New Year holidays.

Companies in the retail sector also described the current economic climate as very weak. Motor vehicle retailers compared the situation for the sector with the situation that prevailed around 1992/1993. The sudden drop in demand that the manufacturing industry noted in the autumn has also been noted in the retail sector. Several retailers reported that sales were affected during a couple of weeks when unease about the situation was at its height. Food shops also experienced a period in which there was a marked fall in sales. Food retailers have clearly noted that the consumers are buying low-price products rather than more expensive products to a greater extent.

In the service sectors the decline is not as pronounced as in the other sectors, but there has been a clear deterioration here too. The decline is clearest for those businesses that are in some way related to the development of the property sector, such as real-estate agents and property consultants. There has also been a decline in demand for the services of companies that provide service and maintenance for other companies.

## Decline in demand and increasing unease

The companies responded slightly differently when asked about the causes of the weak development during the autumn. The manufacturing companies generally mentioned global factors as the most important cause. The clearest sign was said to be a dramatic fall in order intake together with the large-scale cancellation of already placed orders during the autumn.

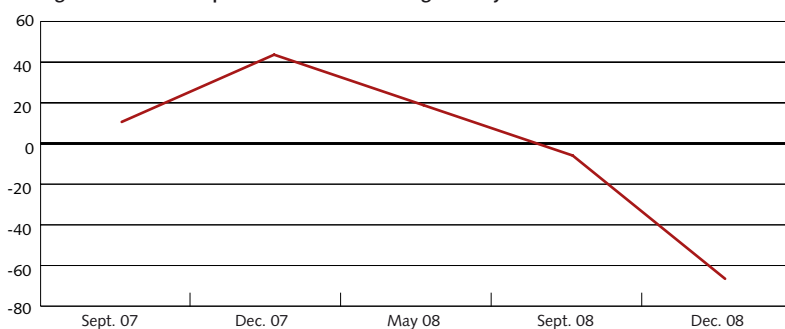
On the other hand, retail companies and companies that sell directly to consumers tended to mention expectations and psychological factors as an important cause. The companies said that the consumers have been worried by "all the bad news in the media" and have thus reduced their consumption. The retail companies also seem to believe that if uncertainty about the future and the economic outlook declined, then "a more normal pattern of consumption" could be resumed. At the same time, they also noted that the situation is not solely due to expectations and that things may become even worse in the period ahead given the expectations regarding the economy in terms of higher unemployment, falling property prices and so on.

Already in September, the companies in the construction sector noted a decline in the demand for the construction of housing, but during the autumn the demand for the construction of commercial properties and civil engineering works has also fallen. Investments in projects funded by the public sector have, however, been unaffected. The construction companies previously had a large order stock but as this has declined, above all for the construction of housing, construction is expected to decline in the period ahead. The companies stated that an important reason for the decline in the construction of housing is the tightening of access to credit. The construction companies reported that the development of the sector is highly dependent on the customers' possibilities to get loans. Several companies said that banks, for various reasons, have withdrawn previous loan commitments with the result that it has not been possible to start a number of projects. The construction companies have also been approached by customers who have found it difficult to get loans and have been asked to provide assistance in the form of different types of temporary funding.

## Extensive revisions of the companies' investment plans

Already in the previous survey in September, a majority of the companies said that they intended to make staff cuts during the autumn. In the December survey, this tendency has increased in all sectors. The weaker demand has also led the companies to radically change their investment plans during the autumn. In the manufacturing industry, a large majority of the companies said that investments will decline over the next six months (see Figure 2). Another strong contributing factor to the decline in investment is an increased focus on the companies' liquidity situation in the wake of more expensive borrowing facilities and a weaker supply of credit. There are several examples of companies that intend to improve their liquidity by not going ahead with all their previously planned investments. In some industrial sectors, all investments that are not absolutely necessary to maintain production have been postponed. There are also examples of companies where investments in development projects have had to be postponed.

Figure 2. Investment plans in the manufacturing industry



Note. The net figures represent the balance between the percentage of companies that reported an increase and those that reported a decrease in investments over the next six months. See also "The design of the Riksbank's company interviews" in this document.

Source: The Riksbank

## The companies' funding situation has become more difficult during the autumn

The funding of operations and access to credit for investments were discussed in detail with the companies during the interviews. Almost half of the companies responded that access to external funding has deteriorated during the autumn.<sup>3</sup> Approximately the same number said that there has been no change since the previous survey in September. There is a wide variation between the companies in terms of the debt/equity ratio and the funding requirement.

The companies reported that interest costs had increased since September but that they expected these costs to fall again, partly as a result of the fall in interest rates towards the end of the year. Many companies also said that the banks' loan margins have increased. Nevertheless, most of the companies seem to be meeting their borrowing requirements in various ways. This applies above all to the large companies. Several of the largest companies responded that borrowing on the market for corporate bonds and commercial papers has gradually become more difficult and/or more expensive during the year. The companies reported, for example, that they had refrained from borrowing via corporate issues as the interest rate was too high.<sup>4</sup> In some cases, unconventional methods have also been used. One company described the problem as follows: "Traditional funding via the banks is not working any more and the company has therefore approached potential investors directly." The companies are aware that the banks are able to borrow from the Riksbank by providing good-quality commercial papers as collateral, but they do not believe that this has had any significant impact on the companies' funding situation. According to the companies, it seems that this relates to the banks' limited ability and willingness to further increase their lending and their credit risks.

Despite the fact that many companies believe that it has become more difficult to get traditional funding from the banks, this still seems to be the most common form of funding. Several large companies responded that the interest of major international banks in lending to Swedish companies has declined and that competition between the banks is thus also declining. According to the companies, it appears that the banks are withdrawing to their domestic markets. This means that the companies are now borrowing from Swedish and/or Nordic banks to a greater extent than previously. The large companies themselves fear that this may be making it more difficult for small companies to get loans. One company pointed out a risk relating to the problems in borrowing on the market for corporate bonds: "The banks will dry up unless the corporate issues get going again."

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3 As the interviews were primarily conducted with large and medium-sized companies, the sample is not representative of industry as a whole.

4 Several large companies said that the costs of insuring corporate bonds have risen by "several hundred points" (one hundred basis points equals one per cent) and that this is affecting the companies' borrowing costs in connection with new bond issues.

## Some companies are acting as banks for other companies

The large companies noted that some subcontractors and customers have found it more difficult to get funding and that this has had consequences for the large companies too. A few small subcontractors have gone bankrupt for various reasons. The manufacturers cooperate particularly closely with, and are more dependent on, certain subcontractors. Some of the subcontractors are said to be finding it difficult to get any loans at all in the current situation. One consequence of this has been that they have been unable to purchase raw materials for their manufacturing processes. One solution to this problem has been that larger and more solid companies have instead assumed part of the bank's credit risk by guaranteeing a part of the loan to the subcontractor. In this way, the bank's credit risk lies with the large company rather than with the small subcontractor. When this is not sufficient, the large company may also need to buy raw materials for the subcontractor as the bank is unwilling to provide any credit at all. In this way, the large and financially strong companies can act as providers of credit to other financially weaker companies.

The provision of credit between companies has also been affected in some cases. An extended credit period may be of great importance to a company's cash flow. It appears that the duration of the credit period has become an increasingly important factor in negotiations on new contracts. Credit losses that arise from a failure to pay have increased somewhat according to the companies but are still said to be relatively moderate. At the same time, several companies pointed out that they are more restrictive about granting credit to other companies and also that they require more collateral than previously. A company in the construction sector said: "At the least sign of problems at a client we put ongoing projects on hold until we feel that the collateral is satisfactory." Other companies said instead that they supply smaller quantities to customers who they suspect may get into financial difficulties.

## Difficulties in obtaining loans in the long term

Many of the companies interviewed by the Riksbank stated that it is a problem that funding can not be arranged or guaranteed at longer maturities. It is in most cases possible to arrange borrowing in the short term, but there is also a demand for loans at longer maturities among the companies. As the possibility to get funding on the market for corporate bonds has declined, the companies said that they have turned to the banks instead. The companies have agreements with and loan commitments from the banks that they can use, so-called lines



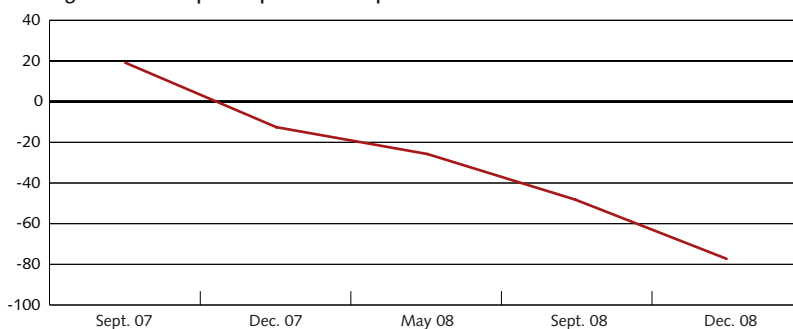
of credit and other credit facilities. However, most of the companies included in the survey in December reported that they have been restrictive about using their lines of credit and special loan facilities.

Several export companies stated that the increase in funds for the Export Credit Guarantee Board and Svensk Exportkredit AB decided on by the government is expected to make it easier to do export business abroad. Several companies reported that they have taken loans from the European Investment Bank in order to fund various research and development projects and that this has also eased the funding situation to a certain extent.

## Companies plan to hold back price increases

The companies point out that several important costs have declined recently. This applies to various commodities that previously were subject to dramatic price increases, for example different metals, oil and food. Several companies also mentioned that transport costs, particularly for the transport of freight by sea, have fallen considerably. When asked about the development of wage costs, most of the companies state that wage increases are expected to be in line with those stipulated in the collective agreements at the same time as wage drift is expected to be lower this year than last year. The latter is due to the weaker development of the labour market. On the whole, there are considerably fewer companies that plan to increase prices more than previously compared to earlier surveys (see Figure 3).

Figure 3. The companies' price increase plans



Note. The net figures represent the balance between the percentage of companies that reported an increase and those that reported a decrease. The question relates to how much the companies plan to increase prices within the next 12 months compared to the previous 12 months. See also "The design of the Riksbank's company interviews" in this document.

Source: The Riksbank

## Exchange rate effects within the next six months

The importance of the exchange rate to the companies varies greatly from sector to sector and even between companies in the same sector. It depends on how much the company imports or exports and on what costs and income the company has in different currencies. For companies with costs mainly in Swedish krona and income in foreign currencies, a weakening of the exchange rate entails higher income and higher profitability. Of the companies in the survey that it was relevant to ask about the importance of the exchange rate, three out of four responded that changes in the exchange rate had an impact on the company's prices within a time horizon of six months. The time lag depends on the duration of the company's currency hedging contracts, the duration of its contracts with various suppliers and how often the company changes the prices it charges to its customers. Some of the interviewed companies' prices have a direct impact on consumer prices. This applies above all to companies in the retail sector. According to the companies interviewed, the time lag between changes in the exchange rate and changes in sales prices was approximately the same for the manufacturing industry and the retail sector.





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