

The Riksbank's Company Interviews

DECEMBER 2009

■ The Riksbank's company interviews in September 2009

"WE ARE SLOWLY MOVING IN THE RIGHT DIRECTION, BUT FROM VERY LOW LEVELS."

The company interviews conducted by the Riksbank in December indicate that the recovery is continuing but is proceeding slowly.¹ It is above all the companies in the manufacturing industry that are disappointed that international demand has not improved more rapidly. The companies now expect demand and production to continue to increase slowly in the early part of 2010. The survey also reveals that the companies have ample spare machine capacity and labour and that they are still restrictive in their investment planning. Expectations regarding wage increases in this year's round of collective bargaining differ quite widely between the different business sectors. Companies in the manufacturing industry are among those that have the lowest expectations with regard to wage increases during the year. The companies also say that price increases are expected to be low in the period ahead as there is a lot of unutilised capacity while competition is strong and demand weak.

Most of the companies in the survey say that the economic situation has continued to improve compared with the situation in September (see Figure 1). The perception that the economic situation is poor is mainly attributable to companies in the manufacturing industry and their subcontractors. Companies in the retail sector are, on the other hand, generally satisfied with the economic situation and refer primarily to the historically-low interest rates, rising household incomes and the fact that their customers are now less worried about unemployment.

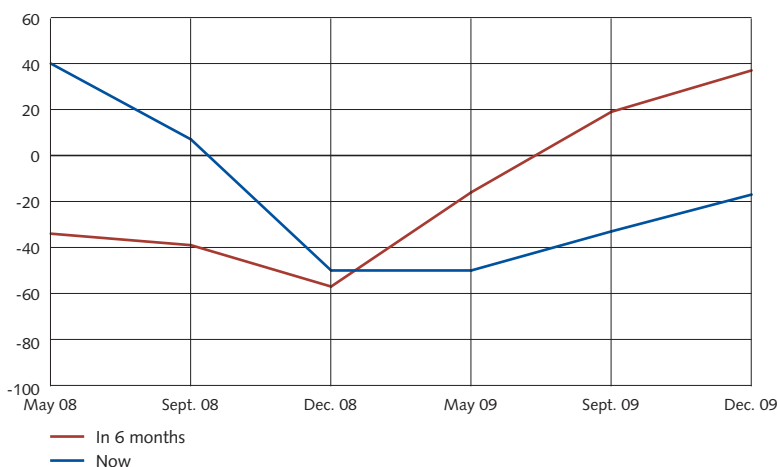
Many of the companies are cautious in their assessment of the development of the economy over the next six months and say things like "we are budgeting and acting as though 2010 will be a normal recession year" or "the first six months of 2010 are already a lost cause, we don't expect demand to increase significantly until 2011".

¹ The Riksbank's company interviews mainly took place in December 2009 and covered 56 companies. For a more detailed presentation of the survey's purpose, methods, sample etc. we refer to "The design of the Riksbank's company interviews", 2 February 2009 on the Riksbank's website, www.riksbank.se, under the heading Press& published/Reports. This makes it clear that the sample of companies is not representative of the business sector as a whole but focuses on large companies. The manufacturing, construction and retail sectors are also overrepresented.

The recovery is taking longer than expected

Most of the companies in the manufacturing industry say that the situation has stabilised, but in many cases at a relatively low level. No marked recovery has taken place as yet; it is rather a question of hopes of better times in the future. Assessments regarding new orders are still positive, but optimism has declined somewhat since the survey conducted in September (see Figure 2). Although most of the companies increased their production during the autumn, the general picture is that these increases began from historically-low levels. Several companies that export a large proportion of their production say that they must see a stronger recovery abroad before they dare to increase the rate of production any further. In general, the manufacturing companies are now relatively satisfied with their stocks of finished products and see only a limited need for further reductions. Nevertheless, several companies point out that as far as possible they wish to avoid once again building up "too large" stocks of finished goods and that they are constantly observant and adapt their production to prevailing demand.

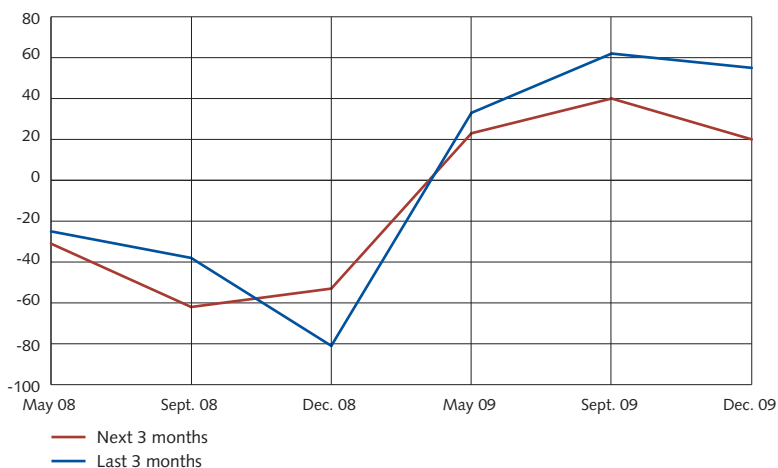
Figure 1. The economic climate now and in six months' time
Net figures



Note. Weighted net figures 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 companies stating that the economic climate is (is expected to be) good (better) or poor (worse).

Source: The Riksbank

Figure 2. New orders in the manufacturing industry
Net figures



Note. Weighted net figures based on the number of employees in Sweden at the interviewed companies. The question relates to the companies' order intake 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 companies stating that orders have increased (are expected to increase) or decreased (are expected to decrease).

Source: The Riksbank

"Asia is the driving force at the moment, Asia is the locomotive!" and "India and China are running at full steam" are two of the comments that indicate that demand from Asia is still strong. However, demand has not picked up on the major export markets in the euro area and the USA.

Several companies note that 2010 will be a more difficult year than 2009 as they have in principle now worked through the large stock of orders that built up during the good years. One company noted that "2006-2008 were incredibly good years", while another company stated that "we are eating up our order stock". Subcontractors to heavy industries say that the situation in this sector has improved only marginally since September.

Capacity utilisation in the manufacturing industry is generally perceived to be very low. Many companies would not find it difficult to considerably increase their production without needing to invest or to employ new personnel. The main reason why the companies do not intend to increase their investments in the period ahead is that they do not believe that demand is strong enough. A common comment is that it will take a long time before the need to make new investments arises.

A similar picture emerges among service suppliers who often have the large manufacturing companies as customers. The last twelve months have been tough and in several cases these companies have been forced to reduce the prices they charge to their customers in order to keep their employees in work: "we have struggled along by

finding work for our consultants on open accounts at low prices in order to weather the storm. The consultants are resources that we will need when the customers get going again and begin to place new orders." The companies also say that their customers are cautious about starting up large projects: "major contracts are conspicuous by their absence". However, there is also a certain degree of optimism about the future among the service companies: "we see no signs among the companies that we work with that things will get worse and in most cases we are beginning to see that things are getting better".

A slight improvement for the construction sector ("...better, but still fragile")

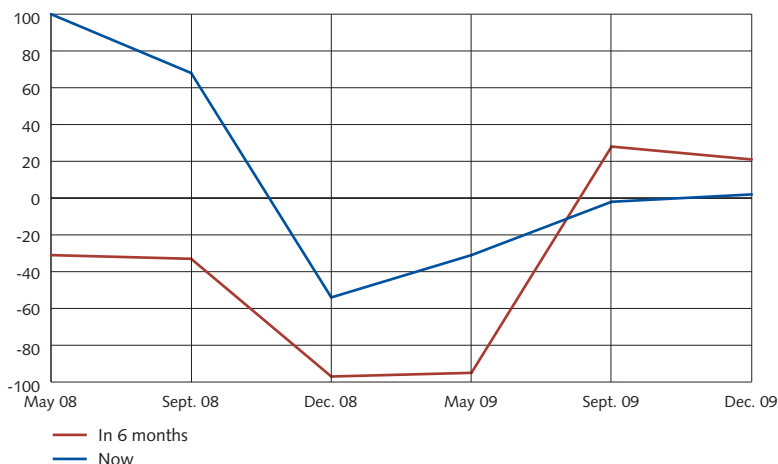
The situation in the various parts of the construction sector varies significantly. While the construction of commercial properties continues to decline, the companies say that the demand for housing has begun to increase somewhat at the same time as civil engineering operations continue to be strong. However, although activity is continuing to increase, the recovery for the construction sector as a whole is proving to be slower than the companies expected when interviewed by the Riksbank in September.

"2010 WILL BE TOUGH AND 2011 WILL BE EXTREMELY TOUGH".

It is said that the profitability of the major construction companies is still good, largely because these companies are still completing projects for which contracts were signed during the latest boom. However, prices are now under pressure on the market and the conditions in the new contracts that are being signed are not as favourable for the construction companies. The companies also fear that their costs may increase when economic activity gathers momentum once again.

Ongoing infrastructure projects regarding roads, tunnels, bridges and harbours are helping to keep civil engineering operations very strong. Several new projects are now out to tender and additional projects are planned for the next few years, which means that the level of production in this area is expected to remain high. Infrastructure projects are in progress and under planning throughout Sweden, but this applies particularly to the Stockholm region. In the case of commercial properties development is still very weak, mainly because so much of the existing stock of properties is unlet.

Figure 3. The economic climate now and in six months' time in the construction sector
Net figures



Note. Weighted net figures 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 companies stating that the economic climate is (is expected to be) good (better) or poor (worse).

Source: The Riksbank

"THE LIMITING FACTOR AT THE MOMENT IS THE COMBINATION OF LOW DEMAND AND A SHORTAGE OF CAPITAL."

The companies interviewed state that the construction of housing is continuing to increase, but that the increase is still limited. Most of the construction companies' stock of housing that was completed before and during the crisis has now been sold. New construction projects have been started, mainly in the major urban areas where demand is highest. In the previous survey in September, several construction companies stated that the funding situation was the factor that was restricting the construction of housing the most. It was primarily the lower leverage ratios of the banks that were mentioned. These leverage ratios have since been increased, although not to the levels that prevailed during the early part of 2008. The construction companies underline the fact that funding is still an area that is creating problems for them.

Builders merchants noted an increase in sales during the summer and this positive trend continued during the autumn. According to the merchants, this increase in sales is due to the low interest rate, the possibility for the households to get tax deductions for building and renovation work under the so-called ROT scheme and tax cuts. The products sold have primarily been used for renovation projects, which has also benefited small construction companies.

Wheels still not turning in the transport sector

While passenger transport operations are at a satisfactory level, the situation for freight transport is still poor according to the companies even though demand is increasing somewhat from previously low levels. There is still excess capacity in the transport sector and prices in freight transport segment are under pressure. The transport sector is dependent on the development of the manufacturing and construction sectors and an upturn in these sectors is required if the transport sector is to be able to increase its sales. There are some positive signs, however, and a slight increase in the need for transport can be noted. International air-freight prices are, for example, increasing.

Increased sales but fiercer price competition in the retail sector

Most of the companies in the retail sector report a continuing increase in sales volumes during the autumn more or less in line with what the sector expected in the previous round of interviews in September. Most of the companies are positive about the prospects for the development of sales in early 2010. Companies commonly comment that they believe they are moving back towards more normal sales patterns, although others emphasise that there is still a certain degree of anxiety that is holding back consumption.

As previously, several of the companies highlight regional differences in the development of sales. Growth has been good in the Stockholm region and in southern Sweden, while development in western Sweden, for example, is often characterised as weaker.

Several retail companies report that food sales are being stimulated by the fact that the households are not eating out to the same extent as before. More customers than previously are continuing to buy from the low-price range of goods and retail chains with a low-price profile say that they have gained market shares. Many representatives of the retail sector also say that price competition has increased.

Corporate funding – continuing improvement...

It has become easier for the companies to fund their operations. When asked whether "access to external funding has changed during the last quarter", the most common response of the companies is that the situation is "unchanged", while others say that access has "improved". This time, no company says that access to external funding has "deteriorated". At the same time, there is a further reduction in the minority of companies that report that "they are not getting the funding they need" to approximately five per cent of the companies interviewed. The corresponding figure in September was approximately 10 per cent. Several of the companies who say that they did not get

the funding they believed they needed in December have operations in the construction sector. In other words, it appears that the funding situation improved during the autumn, although it should be pointed out that this survey primarily reflects the situation for large companies.

The comments of the large companies often reflect an increase in the supply of financial capital and lower borrowing costs for market funding via corporate bonds and certificates. Some of the large companies report that they have increased their funding through bond issues as they are concerned about future access to large syndicated bank loans given that many international banks have chosen to leave the Swedish finance market.

It also seems that the possibility for the large companies' customers and subcontractors to get loans from the banks has improved. Fewer of the large companies feel that they are forced to "act as a bank" by allowing their customers a higher level of credit than under normal circumstances. Generally speaking, therefore, the responses indicate that the supply of bank funding has increased but also that some problems still remain. In December, far fewer companies were critical of the behaviour of the banks than in the surveys conducted earlier in the year. The criticism that is levelled at the banks relates most often to their high lending margins.

...but still not a normal situation

In this survey, the companies were also asked whether they believe that conditions on the financial markets have normalised.² Nearly all of the companies answered the question, but they often stressed the difficulty of defining what can be regarded as normal. The assessment of approximately half of the companies was that the situation on the financial markets has not yet returned to normal. This was the response of most of the companies in the construction sector, while most of the retail companies consider that the situation has normalised. In the manufacturing industry the responses were evenly distributed between normal and not normal. In general, the large companies covered by the survey tend to say the situation has returned to normal to a greater extent than the small companies.

The companies that state that the situation on the financial markets has normalised were also asked when they feel this happened. Relatively few companies answered this question, but among those who did the most common answer is that the situation normalised during the second and third quarters of 2009.

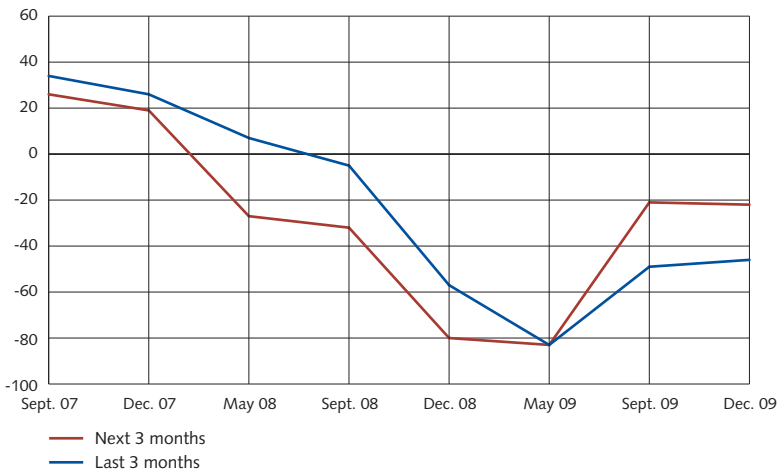
² The question asked in the survey was: "Do you consider that conditions in the financial markets have normalised (for your company)?"

“The dramatic effects of the crisis seem to have abated”

Following a period marked by a wave of redundancy notices and lay-offs, the assessment of a great majority of the companies interviewed is that the employment situation has now stabilised. Employment continued to decline even during the latter part of 2009 according to the companies (see Figure 4). However, the situation differed from sector to sector. The responses from the retail sector indicate that there has actually been a slight increase in employment, while employment in the manufacturing industry, which carries a lot of weight in this survey, continued to decline. However, the negative trend for the manufacturing industry has weakened compared with previous surveys. Several industrial companies have chosen to retain personnel by negotiating agreements to shorten the working week.

When asked about the prospects for the future, most of the companies state that they now have the workforce they need and that no major redundancy or rationalisation programmes are to be expected. However, there are still more companies that intend to reduce their workforce than intend to employ new personnel over the next few months (see Figure 4). Once again, it is primarily companies in the manufacturing industry that have a more pessimistic view of the future while the retail sector is more optimistic. One manufacturing company described the situation by saying: “We are not even close to employing new personnel”. It is important to note in this context that the cutbacks the companies are planning for the early part of 2010 consist mainly of natural wastage concerning jobs for which there will be no new recruitment rather than of redundancies or lay-offs.

Figure 4. Employment
Net figures



Note. Weighted net figures 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 diagram represent the balance between the percentage of companies stating that employment has increased (is expected to increase) or decreased (is expected to decrease).

Source: The Riksbank

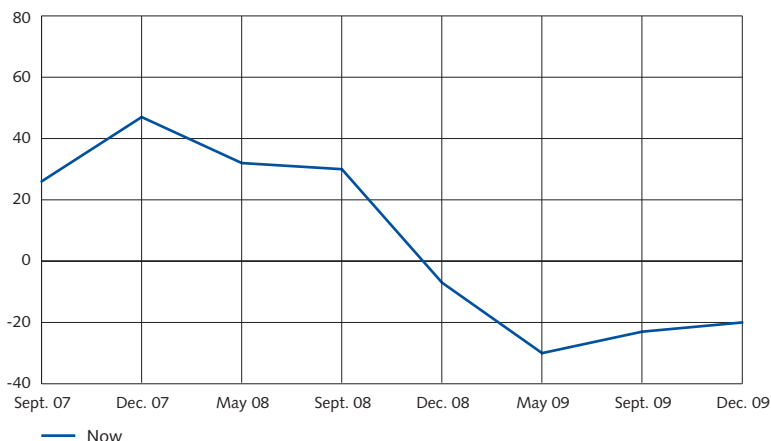
Profitability still low according to the companies...

In December, the companies' assessments of their profitability³ were largely the same as in September (see Figure 5). Among the manufacturing companies the response was usually "poor". When asked why profitability is low in this sector, the manufacturing companies commonly cite the low level of demand for their products. In the other sectors, the companies' assessments of their profitability are generally positive and there is a tendency towards an improvement compared with the responses in the interviews conducted in September.

...but costs have fallen

Several companies that report an improvement in profitability say that the reason for this is "a better-adjusted cost structure". Some of the companies that report that profitability is still poor also say that various cost reductions have nevertheless led to certain improvements in profitability. This applies, for example, to several companies in the manufacturing industry. Various savings programmes and measures to improve efficiency, lower wage costs and lower purchasing costs are some of the cost savings mentioned by the companies. Some companies also mention the development of the exchange rate and an improvement in demand as reasons for an improvement in profitability. The companies' profitability assessments are of interest because, among other things, they affect wage and price formation in the economy.

Figure 5. Profitability
Net figures



Note. Weighted net figures based on the number of employees in Sweden at the interviewed companies. The question relates to the companies' assessments of their profitability at present. The net figures in the diagram represent the balance between the percentage of companies stating that profitability is good and those stating that profitability is poor.

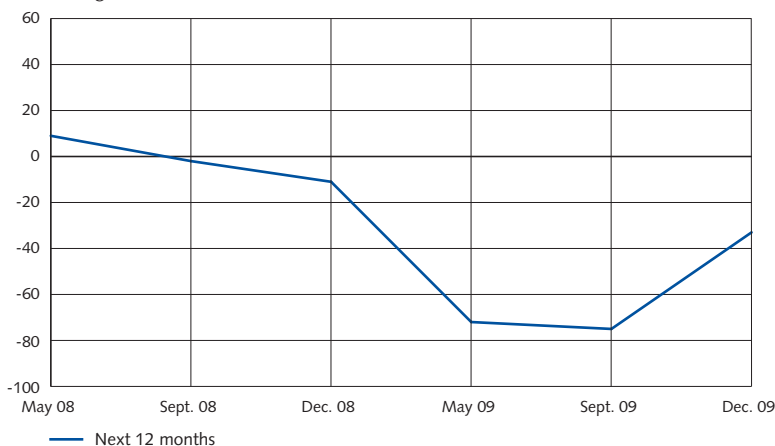
Source: The Riksbank

³ The companies' assessments of their profitability are often based on to what extent they attain internally-set profit targets. These profit targets vary dramatically, in particular between sectors.

Still limited increases in wage costs

Wage cost increases are expected to be lower in 2010 than last year according to the companies' responses in December. In the interviews conducted in December, however, fewer companies say that wage costs will be lower compared with the interviews conducted in May and September (see Figure 6). This is largely due to the fact that there are more companies in the manufacturing industry that believe there will be higher wage cost increases this year than in the two previous surveys. This in turn is probably due to the fact that local "crisis agreements" entailing reduced monthly wages and working hours for employees in the manufacturing industry were entered into in 2009, but also that the pay reviews for 2009 were moved forward to 2010 at several companies. This postponement of pay reviews may also have been a component of the "crisis agreements". All-in-all, this meant that wage cost increases at many companies in the manufacturing industry were very low in 2009, which is also why these companies believe that wage cost increases will be higher this year. Some companies also explicitly mention these factors as explanations of their assessments of the development of wage costs this year.

Figure 6. The companies' future wage costs
Net figures



Note. Weighted net figures based on the number of employees in Sweden at the interviewed companies. The question relates to the companies' assessments of their wage costs over the next 12 months. The net figures in the diagram represent the balance between the percentage of companies stating that wage costs will increase and those stating that wage costs will decrease.

Source: The Riksbank

The manufacturing industry is budgeting for lower wage cost increases than other sectors

The companies were also asked to quantify the level of wage cost increases they had budgeted for 2010.⁴ Most of the companies answered this question and the levels quantified varied substantially between the sectors. The manufacturing companies have budgeted for significantly lower wage cost increases than the other sectors covered by the survey. However, this result should be interpreted with a certain degree of caution as some companies felt that the question was difficult to answer and a number of them provided relatively vague information. It is also possible that the answers were affected by the prudence principle that the companies apply in their budgeting processes.

Risk of tension in the approaching round of collective bargaining

The interviews also included a question on what the companies think the result of this year's round of collective bargaining will be. A number of companies chose not to give a specific answer to this question but referred to the organisations that conduct the central wage negotiations on the labour market. Some of the companies chose to paint a more general picture of the round of collective bargaining this year. The expectations of the companies range from the belief that the bargaining process will go smoothly to the belief that it will be marked by tension and disagreement. Several of the companies that expect to see tension claim that the social partners are now more polarised than during previous rounds. Relatively substantial differences in the economic climate in the different sectors are also mentioned as one reason why the process could lead to industrial unrest.

"Shorter agreement periods in turbulent times"

Some companies believe that the duration of the central pay agreements will be shorter this year; that is that the agreements will run over one or two years. One important reason for this belief is the uncertainty about the development of the economic climate and profitability that prevails at the moment. Other companies believe that the agreement periods will be short but are hoping for three-year agreements. They would prefer longer agreements as this would enable them to work undisturbed and avoid the operational inefficiency that arises during the collective bargaining process. Several

4 The question in the survey was: "What increase in wage costs have you budgeted for in the next calendar year? (please state as an annual percentage change)."

companies point out the importance of knowing what the budget for pay costs will be over a longer period in order to have a solid basis for planning for the future. In this context, one company says that "there is a risk that a one-year wage agreement will lead to fewer investments". Finally, a number of companies believe that a three-year agreement period, which has been the norm over the last 15 years, will also be the result of this round of collective bargaining. Overall, slightly more companies believe that the wage-agreement periods will be shorter, although several of them also hoped that the periods would be longer.

Price pressures will continue to be low in the period ahead

The companies' responses regarding expected price changes in 2010 indicate that price increases will be limited. However, the responses differ somewhat from sector to sector. While most of the companies in the manufacturing and retail sectors see very little potential for price increases, those that hope that it will be possible to increase prices are slightly higher in the service sector. In the manufacturing sector, fewer companies now expected price increases than in the earlier surveys conducted in 2009. A possible explanation for this is the belief that the improvement in economic activity in the manufacturing industry will not come as quickly as was previously hoped. The interviews conducted at companies in the retail sector indicate that it is likely that a substantial part of the price increases for imported goods that were motivated by the weak exchange rate last year have now been implemented.

The picture of low price pressures is reinforced by the fact that a number of the companies interviewed point out that for their part it is not a question of a decline in price increases in the period ahead but rather a question of falling prices. In the December survey, about the same number of companies say that their sales prices may fall in the period ahead as in the September survey, and the majority of these are manufacturing companies.



Sveriges Riksbank
SE - 102 37 Stockholm

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