

The Riksbank's Company Interviews

MAY 2011

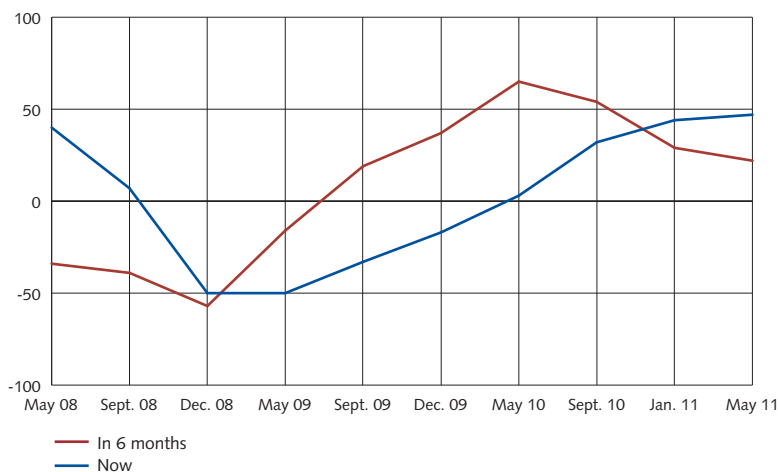
■ The Riksbank's company interviews in May 2011

Strong economic activity levelling off

The Riksbank's company interviews in May 2011 show that demand and production in the Swedish economy continue to develop well. This is due to strong growth in exports, good domestic demand and an ongoing demand for labour. At the same time, companies assess that access to labour is still good and that some spare plant capacity remains. The economic situation is expected to strengthen further over the next six months, but lower expectations concerning production and new orders indicate that the upturn in economic activity is now entering a calmer phase. Many export companies point out that the current level of the exchange rate for the krona has a negative effect on international competitiveness and profitability. Companies intend to raise their prices both in the coming quarter and during the course of the year, which is mainly due to the manufacturing industry's pricing plans.

Companies assessed in May that the economic situation was good and that it remained largely unchanged since January this year (see Figure 1). However, there are some factors that have a negative effect on the assessment, such as rising commodity prices and a strong Swedish krona. One manufacturing company describes the economic situation as follows: "The demand situation is still good. It is the increases in commodity prices and the strong krona that are causing problems." The economic situation six months ahead is often assessed to be better, even if fewer companies believed in a continuing upturn now in May than thought so in January. Several companies stating that the economic situation would remain unchanged went on to clarify by saying "we mean it will still be good".

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

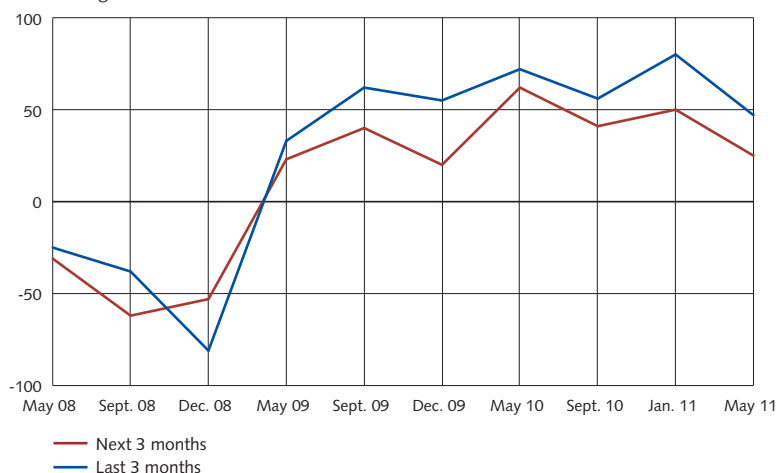


Note: The question concerns the companies' assessment of the economic climate now and in six months' time. The net figures in the diagram represent the balance between the percentage of companies stating that the economic climate is good or bad, or that it is expected to be better or worse. The figure shows weighted net figures that are based on the number of employees in Sweden at the companies interviewed.

Swedish export companies on the whole paint a positive picture of the situation, with strong demand from, for instance, Germany, China and Brazil, while demand from southern Europe is still showing slow development. "The recovery in the global economy is continuing, but it is unevenly divided across the different regions" is the description of global economic activity given by one export company.

The positive outlook for the manufacturing industry is confirmed by the companies' views on production volumes and orders, although some slowdown can be discerned compared with the previous survey in January. Figure 2 shows a continuing increase in orders in the manufacturing industry, although not as fast as before. The corresponding outlook for production volumes also indicates a slowdown in activity in the manufacturing industry in the future.

Figure 2. New orders in the manufacturing industry
Net figures



Note: 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 or decreased, or are expected to increase or to decrease. The figure shows weighted net figures that are based on the number of employees in Sweden at the companies interviewed.

The shortage of components resulting from the natural disaster in Japan only appears to have led to marginal disruptions in production in the Swedish manufacturing industry. Some companies were able to manage the situation by buying more expensive components on the global market.

"THE TURNAROUND CAME IN APRIL"

The retail trade's assessment of the economic situation remained largely unchanged in May compared with January. Over the coming six months, however, demand is expected to improve significantly after a weak outcome for the retail trade during the first quarter of 2011. Several retail trade companies stated that they had experienced a significant improvement in sales in April, which contributed to their optimism regarding the future.

The construction industry describes good activity, with residential construction accounting for the continuing large demand. The companies say that there is a pent-up need for new housing, as too little has been built for several decades now. One construction company considered the situation to be "good, but not great".

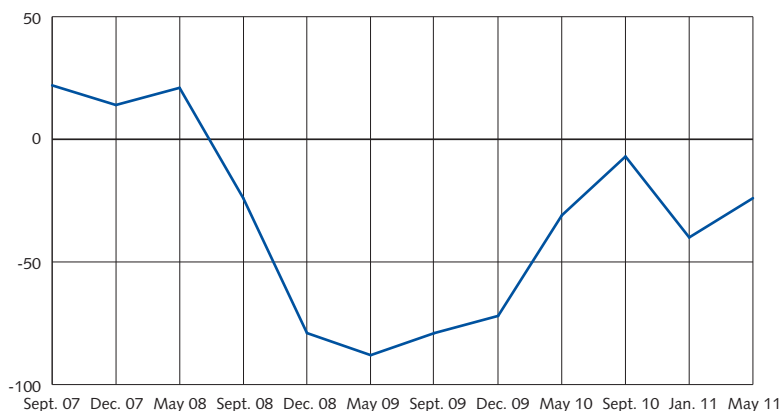
REDUCED RISKS

The percentage of companies that perceived the risks from cyclical activity to be higher than normal in May was slightly lower than in January. The risks still largely concern the fiscal unease in Europe, the stronger Swedish krona and fears of interest rates rising too quickly. The companies identified the same risks in January.

STILL SPARE RESOURCES IN THE ECONOMY

A weighing together of the companies' responses regarding the supply of labour and the ability to handle an unexpected increase in demand indicates that the utilisation of spare capacity in the business sector rose slightly in May compared with January (see Figure 3). All in all, the responses nevertheless do not point in general to any significant shortage of either spare capacity or available labour.

Figure 3. Capacity utilisation indicator
Net figures



Note: The indicator 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. 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.

The manufacturing sector companies have increased production gradually, which has led to higher capacity utilisation, although it is not yet at the pre-crisis levels. According to the manufacturing sector companies, there is still spare technical capacity available and there are few companies stating that they would have major problems in increasing production.

Most of the manufacturing sector companies are planning to increase investment over the coming six months, and in this context an increasing number of companies are talking about investments to enable an increase in production capacity. This means that the gradual shift in investment, from replacing worn-out capital to increasing production, is continuing. At the same time, few companies are implementing or planning to make major investments, in fact in most cases they are considering only small additions to their production capacity. As there is still spare plant capacity, these investment plans are probably more focussed on long-term needs to extend capacity and improve productivity rather than on an urgent need arising as

a result of increased production. The decisions may also have been affected by companies perceiving the economic situation to be more stable than before.

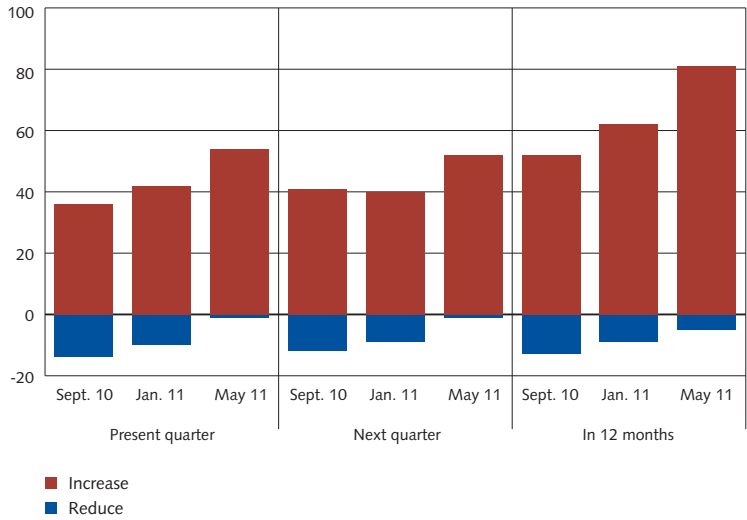
Around half of the companies stated in May, as they did all last year, that they plan to increase their staff over the coming three months, which points to a continuing high demand for labour. Within the manufacturing sector and the retail trade, these increases are on a broad front, but are usually relatively small additions at the company level. Most of the companies use employment agencies to adjust the size of their staff to fluctuations in demand. However, the scope varies between sectors and branches and in many cases employment agencies have only marginal significance. As employment has increased, the use of these agencies has also increased.

Companies in the retail trade stated, as before, that there is no general shortage of labour. However, in the construction industry they consider it difficult to find labour with the right competence. The staffing levels in the construction industry are considered too small in relation to the prevailing production levels, and one company expresses the situation as "the pool of potential labour is much too small". In the manufacturing industry, however, most companies consider that their staffing levels are well-adjusted to their production. There is a shortage of some specific competence, such as engineers, and some companies express concern that this may hamper future development.

RISING PRICE PRESSURE IN MANUFACTURING INDUSTRY

In May, more companies stated that they plan to increase their prices during the coming twelve months than said so in the previous surveys in January 2011 and September 2010. Figure 4 shows that a slightly larger number of companies is expecting to raise prices in the present quarter and next quarter, compared with January. These differences are mainly due to manufacturing companies saying to a greater extent than before that they would increase their prices. At the same time, the manufacturing companies expressed their plans to increase prices in relatively vague terms, often in the form of a hope. The results should therefore be interpreted with some caution. The retail trade companies' responses indicate no clear differences between January and May for any of the time periods.

Figure 4. Companies' pricing plans
Per cent

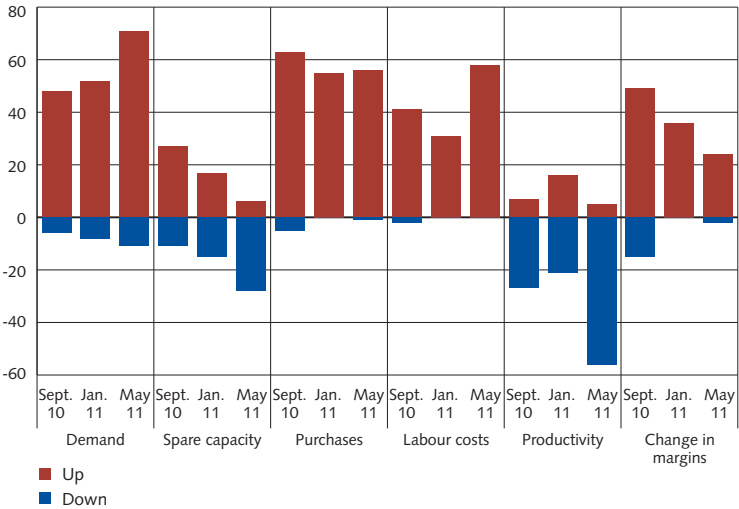


Note: The columns show the percentage of companies that intend to increase or reduce prices during the present quarter, next quarter and next 12 months. The figure shows weighted percentages based on the number of employees in Sweden at the interviewed companies.

As before, around half of the companies also stated the size of the price changes they are planning. The responses varied considerably, depending on the different conditions in different sectors and industries. All in all, however, these responses only point to marginal changes in price pressures for both the manufacturing industry and the retail trade.

Supplementary comments from the retail trade do, however, express some concern that price levels may need to be increased. The rising international food prices have so far been largely balanced by the stronger krona exchange rate, but now the retail trade is not expecting any further appreciation on the Swedish krona. In addition, some companies point to the fact that they have had long contracts that have delayed the impact of higher purchasing costs on consumer prices.

Figure 5. Factors that will affect pricing in the coming twelve months
Per cent



Note: The columns show the percentage of companies specifying the upward or downward impact of the various factors on prices 12 months ahead. The figure shows weighted percentages based on the number of employees in Sweden at the interviewed companies.

The companies also responded to a follow-up question about how their pricing plans over the coming twelve months would be affected by factors such as demand, spare capacity, materials and purchasing costs, labour costs, developments in productivity and changes in margins (see Figure 5). They were asked to state whether the respective factor affects prices in an upward or downward direction or whether it has no effect.

The companies consider that high demand and increased labour costs are important reasons for being able to implement price increases in the coming period. Rising purchasing costs are also an important reason, but their significance is roughly the same as during the previous interviews. In May, considerably more companies than before stated that productivity developments were pushing down prices. Fewer companies felt that they could improve their margins compared with January and with September 2010. These average results are affected significantly by the responses from the large manufacturing companies. The responses from the companies in the retail trade have a partly different pattern, where for instance increased demand is expected to have a much smaller significance for pricing.

WAGES ON THE WAY UP

A majority of the companies are assuming that wages will rise more rapidly over the coming twelve months than before. "There is definitely upward pressure," as one interviewee put it. This expectation is also mirrored in the factors affecting the companies' pricing plans in Figure 5. Companies in the manufacturing industry are expecting wage demands to rise, partly as a result of the rapid upturn in economic activity and partly because the previous agreement was signed during the financial crisis.

Almost half of the companies are also expecting wage drift to increase. The reasons for this are partly a general increase in the demand for labour and partly a shortage of certain specialists. Companies in the manufacturing industry are experiencing a shortage of engineers and there is also an increase in the turnover of higher-qualified staff in the retail trade. One company expresses this as "the economic climate has improved for competent staff".

PROFITABILITY UNDER PRESSURE

Companies' assessments regarding their own profitability remained at roughly the same high level as in January, but with a tendency towards weakening. Production and sales have increased over the year, but nevertheless the companies do not consider that profitability has improved. According to the companies, this is because various types of cost increase together with stiffer competition have reduced profit margins. Export companies' profit margins have declined as a result of the stronger krona exchange rate and construction companies are dissatisfied with profitability in contracts signed during the crisis. Fewer companies than before see an opportunity to strengthen their margins, which is illustrated in Figure 5.

"WE ARE FORCED TO MAKE SUBSTANTIAL IMPROVEMENTS IN PRODUCTIVITY"

The comments from many of the export companies indicate that they regard the strong krona as permanent, and that they consider they need to become more productive to maintain their profitability and international competitiveness. Many companies commented on this situation with wording such as, "we are forced to make substantial improvements in productivity as a result of the strong krona".



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