The Riksbank's Company Interviews

JANUARY 2011

The Riksbank's company interviews in January 2011[1]

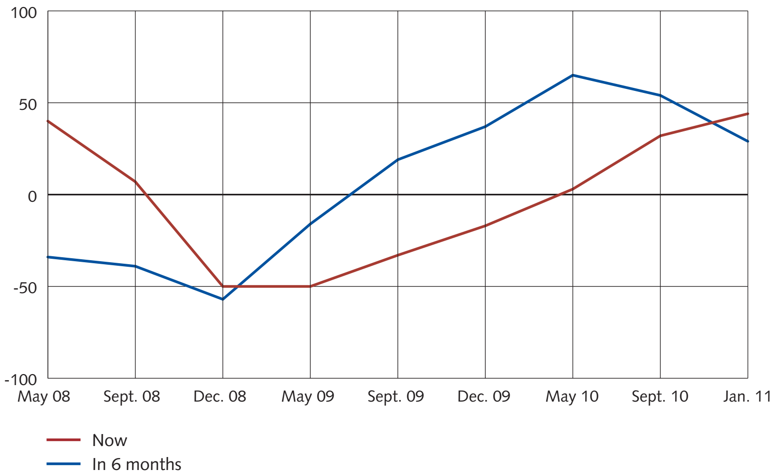
Production and profitability recovering

The economic situation has continued to improve since September according to the Riksbank's company interviews in January. The companies now generally report that the economic situation is positive, although it can also be noted that expectations concerning a further upturn are somewhat more subdued. The companies believe that demand and employment will continue to increase, but investment plans remain cautious. The companies' assessment is that there is very little need to expand production capacity while, with the exception of the construction sector and certain specialists, there is still a good supply of labour. Wage costs and wage drift are expected to increase compared to last year. Slightly more companies than in the previous survey now say that they intend to increase prices over the next 12 months. Increased costs for raw materials and input goods are given as reasons for these price increases, but also the high level of demand. The companies are now more satisfied with profitability than at any other time during the last two years.

The economic situation has continued to improve according to the companies. The upturn appears to be broadly based, with the strongest improvement in the construction sector. In general the companies also expect to see a continued improvement over the next six months, although at a declining rate as shown in Figure 1. Two relatively typical comments are: "*We are back to a stable level*" and "*all the curves are pointing upwards for the various international markets, it's just that some a rising slightly more sharply than others*". Some companies are, however, a little more restrained and make comments such as: "*Things have levelled out now*".

1 This time, the survey was conducted in a slightly different way to previously. Only the very largest 25 companies were interviewed this time, as opposed to 60 companies previously. The total number of employees in Sweden at the interviewed companies therefore fell, but only to approximately 210 000, as compared to 270 000 in September. As the number of interviews was lower than previously it was possible to conduct them all in a more concentrated way in January instead of in December/January.

Figure 1. Assessment of the economic climate now and in six months' time
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 companies stating that the economic climate is (is expected to be) good (better) or poor (worse).

Source: The Riksbank

Similarly, the companies' responses on the development of production volumes indicate a positive development of economic activity. However, the retail sector, which reports falling sales for the fourth quarter, deviates from this general trend.

The interviews with companies in the transport sector confirm the picture of an upturn. There has been a clear increase in domestic and international transportation. It seems, however that domestic transportation has increased much more slowly, with the exception of transportation for the construction sector and of packages. One transport company expresses surprise that transport volumes have increased less than GDP and believes that the difference could have something to do with the fact that growth has been stronger in the service sector than in manufacturing.

INTEREST-RATE INCREASES AND A STRONG KRONA ARE NEW CAUSES FOR CONCERN

More than half of the companies said in January that the risks associated with the development of economic activity were "normal". Some companies said that these risks were "higher than normal", while only a few said that they were "lower than normal". It is above all manufacturing companies in the export sector that assess the risks as being higher than normal. Two comments that reflect the most common responses are: "*There are uncertainties, as there usually are*" and "*As long as there are no new debt crises the situation will improve*". Compared to the survey in September, the companies' responses indicate that there has been a marginal reduction in the risk level.

The risks the companies generally refer to concern developments in Europe and the United States, often linked to imbalances in central government finances, and fears that these may lead to a renewed downturn in economic activity. This time, some companies mention risks associated with interest-rate increases and the strong exchange rate for the krona. These risks were not mentioned in September.

STILL SPARE CAPACITY IN THE MANUFACTURING INDUSTRY

The rapid improvement of economic activity has resulted in a higher level of resource utilisation, but there is still unutilised capacity in most branches of the manufacturing industry. As in September, most of the companies say that it would not be a problem to deal with an unexpected increase in demand. Previously, some engineering companies believed that capacity restrictions at their sub-contractors posed a problem. In January, however, this was not mentioned. The companies' cautious investment plans reinforce the impression that production capacity is still available at the existing plants.

Nor does the supply of labour seem to be a general problem for the manufacturing companies we interviewed. Most of the companies say that their workforce is well adapted to the current production volumes. There is, however, a tendency for more companies to say that their workforce is too small in relation to the level of production and sales, which indicates that employment may be expected to continue to increase in the period ahead.

The picture is different in the construction sector. Here the companies say that the number of employees is too low in relation to demand and that there is a shortage of certain types of labour – above all white-collar workers. The construction companies deal with the capacity restrictions to a certain extent by using skilled workers from abroad.

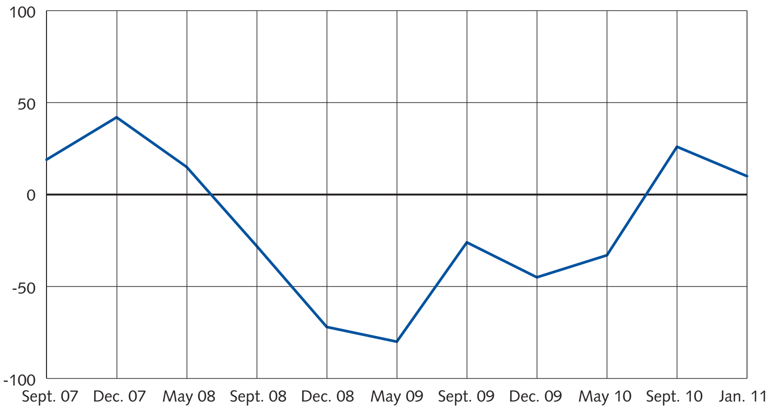
In general, it appears that the companies in all sectors see the labour market as being relatively flexible, which makes it easier for them to adapt their workforce to the level of demand. Those companies that have a shortage of labour are usually in need of key specialist skills or know-how.

INVESTMENT FOR IMPROVED EFFICIENCY AND RESTRUCTURING

The manufacturing companies' investment plans for the next six months are somewhat more cautious than in the previous round of interviews. A majority of the companies still say that investment will increase, but relatively fewer than in the previous survey in September (see Figure 2). The investments that are now being made relate to improving efficiency and to restructuring programmes, while only a small proportion of companies state that they are investing to increase production in Sweden. In September, many companies said that they would invest to replace worn-out capital, but fewer companies said so in January.

The companies' cautious attitude to increasing production capacity in Sweden may be linked to the fact that many of them still have unutilised production capacity. Remaining uncertainty about international demand may also have contributed to this. On the other hand, neither the level of profitability, nor access to funding, appear to impose limitations on investment for the large manufacturing companies. Some of these international groups appear to be planning to increase production abroad in the first instance.

Figure 2. Investment plans in the manufacturing industry for the next six months
Net figures



Note. Weighted net figures are based on the number of employees in Sweden at the interviewed companies. The net figures in the diagram 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.

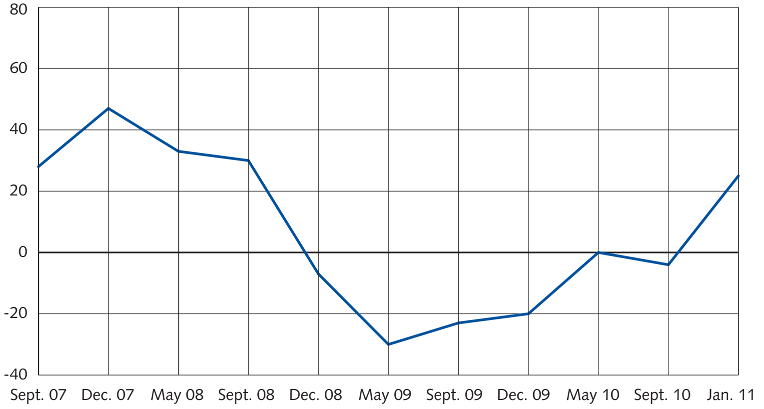
Source: The Riksbank

The picture of only a slow increase in industrial investment matches the responses from the construction sector. The construction companies report relatively weak growth in commercial construction as a whole but very strong growth in the construction of housing.

IMPROVED PROFITABILITY THROUGH COST REDUCTIONS

Profitability is better now than in the September survey (see Figure 3). Some companies say that this good level of profitability is due to the fact that they have managed to retain their margins and at the same time keep costs down. The improvement in profitability is thus not only an effect of the increase in demand. A company in the manufacturing industry expresses this by commenting: *"Our profitability is good given our turnover"*.

Figure 3. Assessment of profitability
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 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.

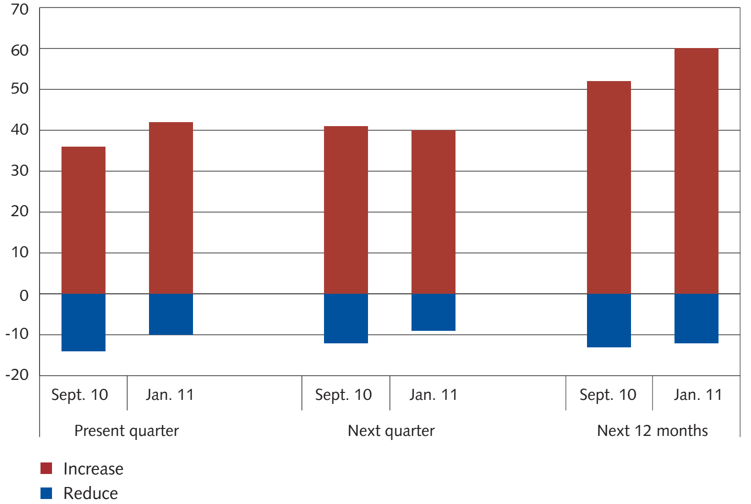
Source: The Riksbank

The responses regarding profitability differ, however, from sector to sector. In the retail sector there is dissatisfaction with the level of profitability. Companies in the non-durables sector say that consumer demand has shifted to durables, which has led to lower sales volumes and poorer profitability. Some companies in the retail sector believe that they need to improve the efficiency of their operations to achieve good profitability: *"One explanation is inefficiency. Sales are high enough"*.

HIGHER DEMAND LEADS TO HIGHER PRICES

A slightly larger percentage of companies state now that they are intending to raise their prices during the current quarter and the coming twelve months, than did so in September (see Figure 4). Few companies are planning any major price increases, and the companies interviewed often state price increases twelve months ahead of two to three per cent. Companies intending to lower their prices over the coming twelve months state as their primary reason the increased price pressure stemming from tougher competition.

Figure 4. Companies' pricing plans



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

Source: The Riksbank

A majority of manufacturing companies state that they intend to raise their prices, which is a higher percentage than in September. Many of the manufacturing companies also say that transport companies have begun to raise their prices. At the same time, the export-oriented companies often emphasise that the competition makes it difficult to raise their prices, despite a price rise being justified by an increase in commodity prices and the strong Swedish krona. One company commented on the situation by saying: "*The exchange rate is a non-issue for pricing*." The export companies often say that the stronger krona will have a negative effect on profitability: "*We'll have to eat into our margins*".

Companies in the non-durable goods segment, which often contains a large percentage of imports, see a need to raise prices as a result of increased commodity costs, but the impact is lessened by the strong krona and intensive competition. One of these companies commented the situation by saying: "*We have substantial increases in commodity prices, but we also have the exchange rate and we are trying to hold back*." There is concern in the retail trade for upward pressures on prices in Asia, primarily China, partly as a result of increased domestic demand. "*These price increases will affect consumer prices in Sweden*," says a company in the retail trade.

In connection with the questions about price changes, the companies were asked to state which factors affect their pricing plans twelve months ahead. The factors that pushed up prices most were costs of materials or purchasing costs and demand. Demand now has greater significance for companies' pricing than it did in September. The factors that the companies see as likely to hold prices down are mainly increased productivity and spare capacity. Like in September, some of the companies interviewed this time that consider themselves "price takers" in the market say that competition is an important factor that can hold back prices. "*If competitors are making large profits they can keep prices low and take larger market shares. It is then impossible for us to raise our prices*."

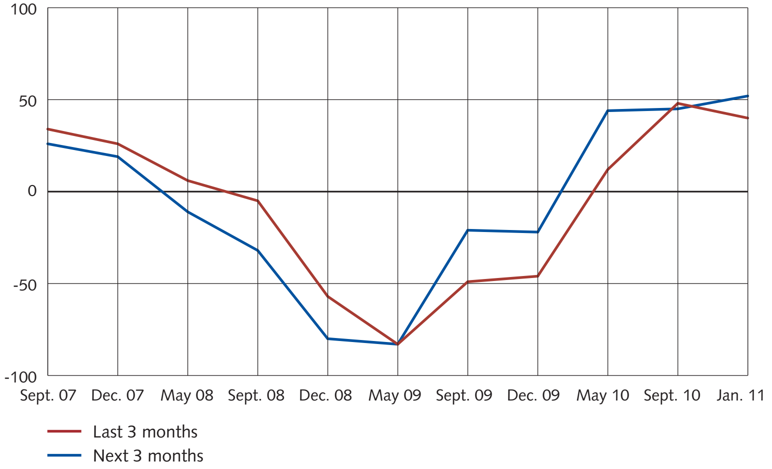
RECRUITMENT NEED HIGHEST IN THE CONSTRUCTION SECTOR

Approximately half of the interviewed companies state that they have increased the number of employees over the past three months. Roughly the same proportion say that they will continue to increase their workforce during the coming quarter (see Figure 5).

The most marked increase is in the construction sector, where all of the companies interviewed state that they will take on employees as construction volumes continue to rise. Another important reason for recruiting is that there is a shortage of some personnel categories, both white-collar and blue-collar workers. In addition, there are plans to deal with approaching retirements. This means that the number of employees will be increased, and there will also be recruitment to replacing employees who are retiring. One of the larger construction companies states that this entails a recruitment need over the coming years equivalent to 20 per cent of their current staff.

Employment has also recovered to some extent in the manufacturing industry. Half of the responding companies have

Figure 5. Assessment of employment
Net figures



Note. Weighted net figures are based on the number of employees in Sweden at the interviewed companies. The question concerns how the number of employees has developed over the past three months and how it will develop over the coming three months. The net figures in the diagram represent the balance between the percentage of companies stating that the number of employees has increased (is expected to increase) or decreased (is expected to decrease).

Source: The Riksbank

increased their workforce and it appears they will continue to do so in the coming quarter. One respondent says: "*There is an underlying increase in production that will lead to new recruitment*".

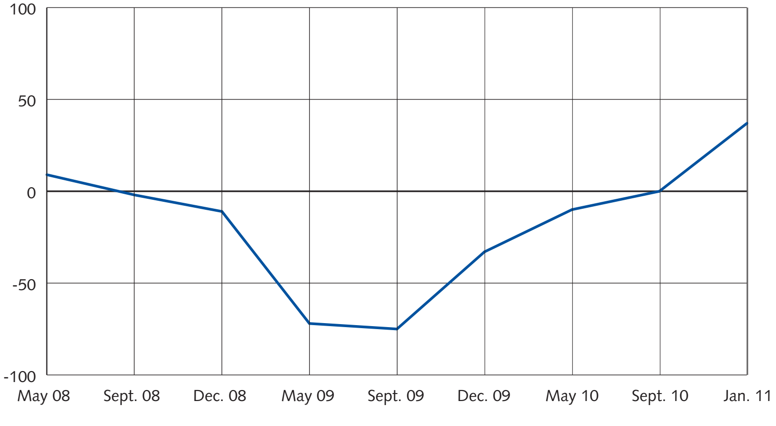
A majority of companies in the service sector have also increased their employees recently and plan to continue recruiting. In some cases, however, there are doubts over whether the prevailing market situation is sufficiently good to allow new recruitment, which is described by one respondent thus: "*There is pressure within the organisation to recruit new staff, but the management is monitoring productivity and is very restrictive*".

Some companies also plan to use employment agencies to a greater extent. This trend is confirmed by the employment agencies who state that their operations have increased substantially in the recent period for both white-collar and blue-collar workers.

WAGES RISING AFTER CRISIS YEARS

An increasing number of companies state that wage costs will increase over the coming year (see Figure 6). This is to some extent because wage increases have been low during the crisis years, when different types of crisis agreement were signed to safeguard jobs, and this means that there is greater pressure to increase wages now that economic activity is improving. This tendency appears to be widespread across all sectors. A common assessment by the companies interviewed is that the increase in wage costs will amount to two to three per cent in 2011.

Figure 6. Assessment of wage costs
Net figures



Note. Weighted net figures are based on the number of employees in Sweden at the interviewed companies. The question refers to the companies' assessment of how wage costs will develop over the coming 12 months. The net figures in the digram are the balance between the number of companies stating that they expect wage costs to increase more than before in relation to those expecting them to increase less than before.

Source: The Riksbank

In the construction sector, companies are now expecting an increase in both wage drift and the costs for subcontracting. Wage drift as a percentage of total wage costs is expected to rise to the levels prevailing prior to the crisis.

In the service sector, too, where there is a greater element of individual agreements, it is probable that wage drift will increase as the new recruitment of specialist competence increases and economic activity improves.

A general problem faced by many companies is keeping the necessary skills within the company. One company expressed the problem as follows: "*Wage drift will increase because we will have to compete for labour. We will have to review our wage structure to be able to hold on to key personnel*."

LARGE COMPANIES HAVE LITTLE PROBLEM WITH FUNDING

As in September, a very high proportion of the companies interviewed in January stated that conditions on the financial markets have normalised with regard to their own company. One comment was that the financial markets are functioning normally for their own company, but that their customers' customers (medium and small customers) were not finding it as easy to gain access to capital. The few companies that still do not consider conditions to be normal state that access to capital from the banks deteriorates as soon as the discussion regarding fiscal problems in Europe surfaces again.

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