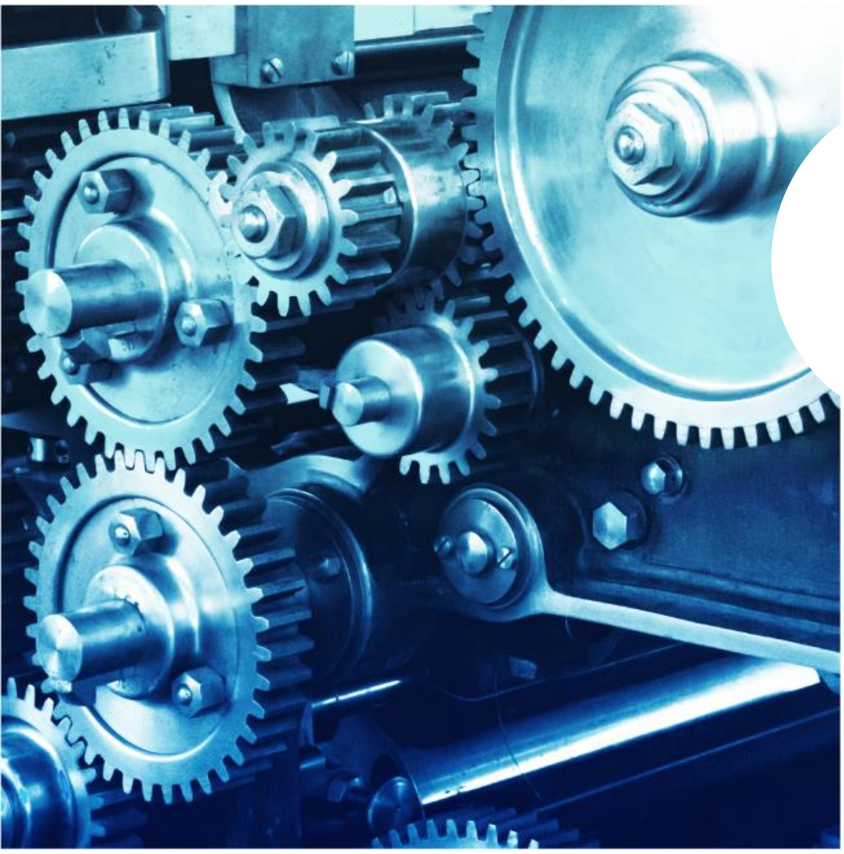
The Riksbank's Business Survey

"As soon as you find one component, you realise you're missing another"



September 2021

S V E R I G E S R I K S B A N K

The Riksbank's Business Survey in September 2021[1]

Economic activity has continued to strengthen for major Swedish companies since the spring due to strong domestic and global demand. At the same time, parts of the manufacturing sector have periodically been forced to limit output due to logistics problems in combination with shortages of key components such as semiconductors. The shocks are now being reported as more comprehensive than at the start of the pandemic and they are also expected to persist next year. The trade sector is also being affected of delivery delays, as well as shortages of certain goods. Global logistics chains are stretched due to a strong increase in demand, unbalanced trade flows and a general shortage of capacity.

Heavy price increases for commodities, energy and so on, together with more expensive transport and shortages of components, are increasing companies' costs. At the same time, profitability is good and the high level of demand means companies can see good possibilities to raise sales prices. Companies that mainly sell to other companies are raising their sales prices and planning for further increases over the year. The trade sector and companies selling services to households are also seeing rising costs but with some delay for parts of the trade sector. Whether this will have an impact on sales prices and how large this would be is uncertain due to the tough competition.

Manufacturing companies are making new investments in new technology to reduce the impact on the environment and climate but they are also expanding their production and storage capacity.

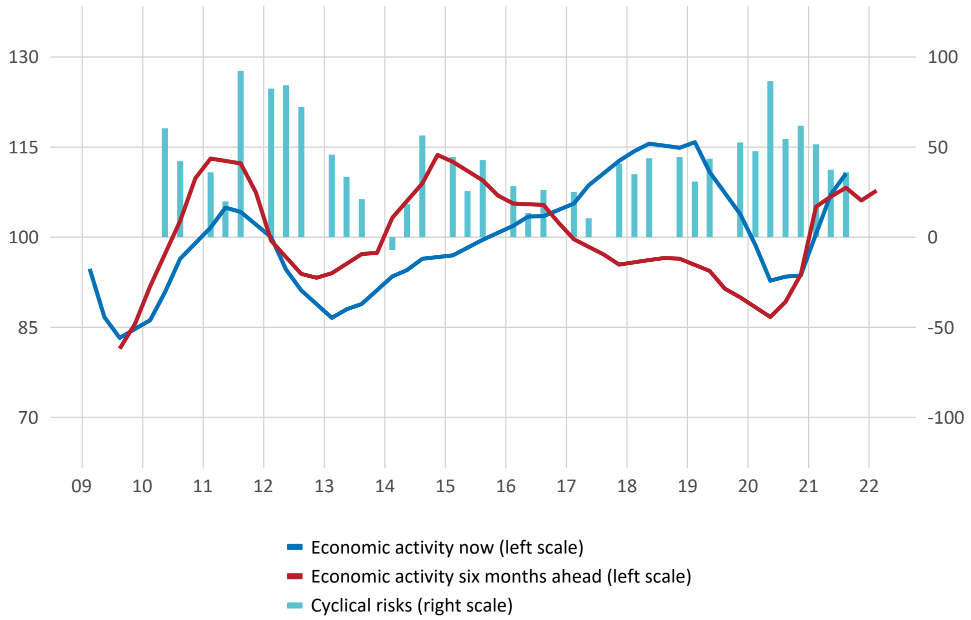
[1] During the period 21-29 September, the Riksbank held interviews, via telephone or video call, with 51 companies in the manufacturing, construction, trade and service sectors, as well as trade associations. The Riksbank's Business Survey is published on the Riksbank's website. All quotations in this report are from companies participating in the survey.

Strong demand but major disruptions

Strong domestic and global demand means that the economic situation has continued to strengthen in September and the strong economic situation is expected to continue over the next six months (see Figure 1). In particular, the manufacturing sector and corporate service sectors are facing strong demand and have good profitability. The demand combined with the shortage of input goods is affecting production volumes, and export companies, above all, are not managing to produce at the rate at which the goods are being demanded. The strong economic situation in the manufacturing sector is also benefiting temporary employment agencies. Staff for hire in production and warehousing have been particularly in demand, as many companies do not have time to recruit staff in the necessary numbers.

Figure 1. Economic situation and economic risks

Index (left scale) and net figures (right scale)



Note. The index figures show a standardised value (mean = 100 and standard deviation = 10) of the net figures for companies that say that the economic situation is currently good or bad and those who say that the economic situation will be better or worse in six months' time. The red line, the economic situation in six months' time, has been moved forward two quarters. The series for the economic situation has been smoothed out with a moving average based on three observations. The bars show the net figures for companies that say that the risks to economic development are currently greater or smaller than normal. As more business surveys than normal were conducted in 2020, there are observations for all quarters.

Eased restrictions are leading to optimism about the future

Economic developments have been normalised for several branches in the trade sector, such as the non-durable goods segment and building supplies segment, which benefited from the pandemic. Their sales have slowed down slightly now that households are consuming services to an increased extent. For other parts of the trade sector, such as the clothing trade, sales are increasing from relatively low levels. There is deemed to be a pent-up need to purchase new clothes now that many people are returning to work in offices and social occasions are becoming increasingly common. The situation remains difficult for the hospitality industry but companies are generally optimistic about the future now that the restrictions have been eased. Sales for hotels and restaurants increased over the summer when many households decided to holiday in Sweden. Travel companies have also noticed a marked increase in bookings.

Continually improved construction activity

Construction activity is continuing to improve but demand for various types of construction has not changed significantly since the spring. Demand for housing, infrastructure and facilities remains strong. Public construction is developing satisfactorily, while demand for commercial construction is continuing to develop weakly. Demand for conversions is also expected to increase in the period ahead. However, there are challenges to manage when commercial premises are converted to housing, for example different VAT regulations.[2]

There are also geographical differences in demand. In parts of southern Sweden, demand is strong and it is difficult to increase the number of construction projects at short notice. The rest of the country, on the other hand, has spare capacity. However, access to cement for the construction sector in the future is an issue that is causing unease and creating uncertainty over construction in the period ahead. On the other hand, the construction sector is experiencing considerably fewer disruptions to production and deliveries than the manufacturing sector.

The disruptions will also continue next year

Industrial and trade companies are generally experiencing major disruptions in output and deliveries and these are deemed to be more comprehensive now than they were at the start of the pandemic (see Figure 2). Above all, the disruptions are due to a substantial shortage of input goods and to capacity problems in the transport sector. High demand is intensifying the disruptions.

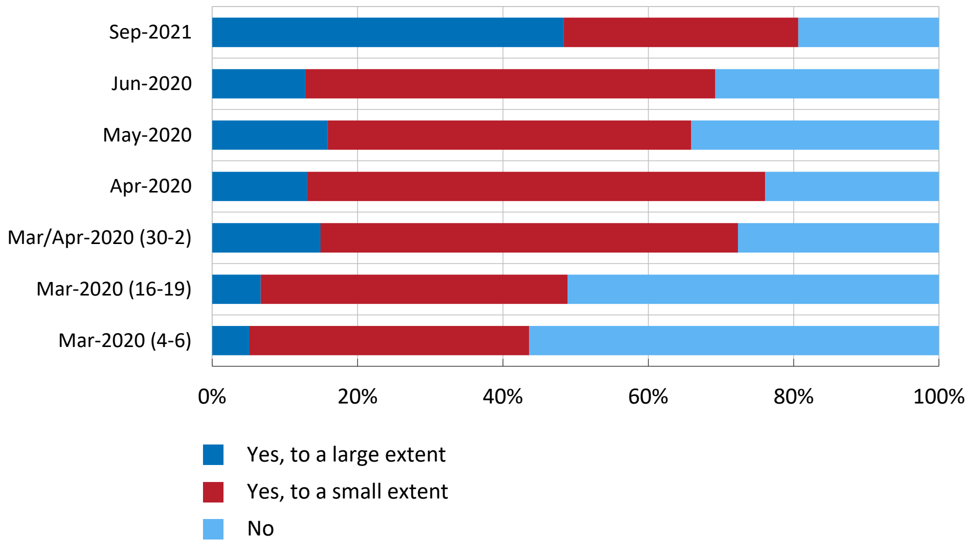
It is not unusual for bottlenecks to arise and for subcontractors to be unable to make changes to production following rapid cyclical turnarounds. However, the combina-

[2] See *Förutsättningar för omvandling av lokaler till bostäder* [Conditions for conversion of premises to housing], 2021, Boverket (National Board of Housing, Building and Planning).

tion of input goods shortages, delayed deliveries and reduced freight capacity is entailing larger challenges than normal and is making the situation difficult to assess with short periods for forward planning. In addition, the disruptions are expected to persist to varying extents and a majority of companies expect the disruptions to affect their operations for another six months or more. One respondent notes, "there's nothing to indicate that things will be better in the first six months of 2022."

Figure 2. In the last three months, have you noticed disruptions to output in Sweden and/or problems in delivering your products?

Percentage of companies



Note. The figure shows results from the manufacturing sector, construction sector and trade sector. The figure heading presents the question asked to companies in the manufacturing sector. To trade companies: Have you experienced disruptions to deliveries to Sweden in the last three months? To construction companies: In the last three months, have you noticed disruptions to output, construction projects and/or problems in deliveries of construction material?

"There's a massive shortage of components"

Many companies in the manufacturing sector emphasise that there are shortages of several different input goods: "You name it, there'll soon be a shortage of it." There is not just a shortage of semiconductors, there is a relatively general shortage of components. Metal, wood and rubber goods such as building frames and hydraulic hoses are mentioned, among others. Purchasing departments are actively working to find equivalent components or possible substitutes for them. "Some components can't be found at all", while there are delays until other can be obtained. The higher costs for electricity are also pointed out: "The cost of electricity now sometimes exceeds the price of the product." There is a certain shortage of goods in the trade sector, for example of goods containing semiconductors for the electronics trade. However, the disruptions in the trade sector are primarily due to delivery delays in goods imports from Asia due to limited freight and port capacity.

"The entire transport market is a bit shaky"

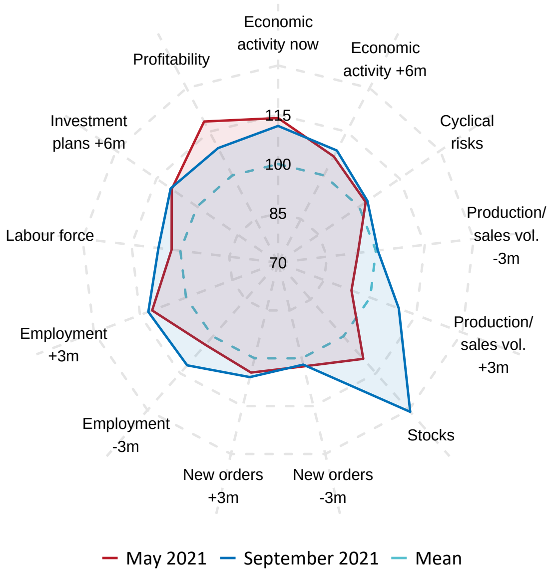
The pandemic has noticeably affected logistics for global trade. Capacity shortages and congestion in the ports mean that ships are being forced to wait longer to load and unload. The shortage of containers is continuing to be tangible: "There is still an extremely messy situation in the container market." The largest bottleneck concerns transport from Asia to the United States and Europe: "The price for transportation of a container from there has increased tenfold." At the same time, profitability for shipping companies is good and companies are trying to make use of all conceivable alternatives: "Everything that can float is on the water." The increase in e-commerce during the pandemic has contributed to increasing demand for shipping, which has benefited other parts of the transport sector, such as courier transport on land. Capacity shortages are also occurring in this sector, which is resulting in delayed deliveries and other kinds of freight problems: "There's no problem with demand, it's a supply problem that's holding the sector back."

Synergy effects can be large in these contexts, as relatively small shocks can have major consequences along the entire transport chain: "When there are delays in all port terminals and in all warehouses, the delay effect becomes large." Larger companies have sometimes used alternative solutions to manage problems with deliveries, for example by hiring freight ships themselves and buying their own containers. Smaller companies do not have this possibility. Some trading companies are also attempting to redirect their purchases to closer countries, such as those in Eastern Europe. However, this is unrealistic for many goods: "It's not possible to recreate this production chain with the pricing that exists in Asia."

"A lot of our stock is out at sea just now"

Companies' stocks of finished goods are deemed too small for the strong demand (see Figure 3). For certain goods, however, customers are accepting the absence of certain components upon delivery just so they can get the goods delivered more quickly. The size of manufacturing companies' stocks of input goods is also being affected by the strong demand, as well as by disruptions to production. There are substantial shortages of certain input goods, while others are actually being delivered, and this is leading to the build-up of stocks that, in many cases, are becoming larger than normal. The production stops are reinforcing this in that input goods can wait for a long time. At the same time, several companies report that they have chosen to expand their stocks of input goods due to the strong demand: "It's larger than normal, but not alarming or worrying." In the trade sector too, more companies than previously deem that their stocks are too small, which is primarily due to delivery delays.

Figure 3. Companies' overall response patterns
Index



Note. The responses to the questions are plotted along "spokes" in the figure, where an index figure closer to the centre is worse. Increased risks to economic activity are assumed here to be deteriorations and thus entail a lower index figure. Stocks refer to stocks of finished goods and reduced stock size means a higher index figure. The historical average is calculated from the date when the question concerned was first included in the survey. The term -3m / +3m refers to the most recent three months and the coming three months respectively. +6 m refers to the coming six months.

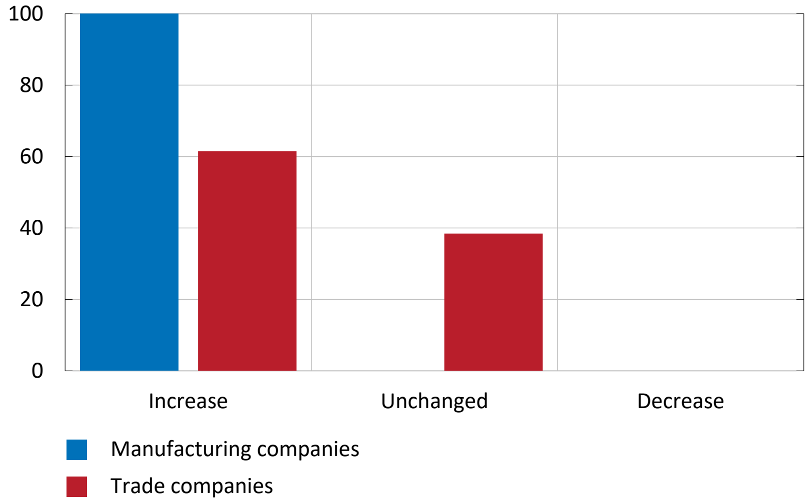
Cost pressures are pushing sales prices up

Companies in almost all sectors have seen their costs rise due to the strong demand and shortages of input goods. These cost pressures are the result of prices of, for instance, energy, commodities, steel, metals, timber and electronic components, as well as transport, storage and logistics costs, having risen heavily over the year. In addition, higher fuel prices and capacity problems in the sector are pushing transport companies' costs up.

There is a great need to compensate for the cost increases and the manufacturing sector is raising sales prices, with further increases being planned for later (see Figures 4 and 5). However, competition is setting limits on the possible size of increases: "It's difficult to cover the cost increases and simultaneously raise our margins." One respondent also says: "At some point, price rises will also have to become apparent for ordinary consumers." Construction companies also consider that they will have to pass the cost increases on to their customers to retain their margins and they are therefore planning to raise offer prices.

Figure 4. What impact will the disruptions have on your sales prices?

Percentage of companies



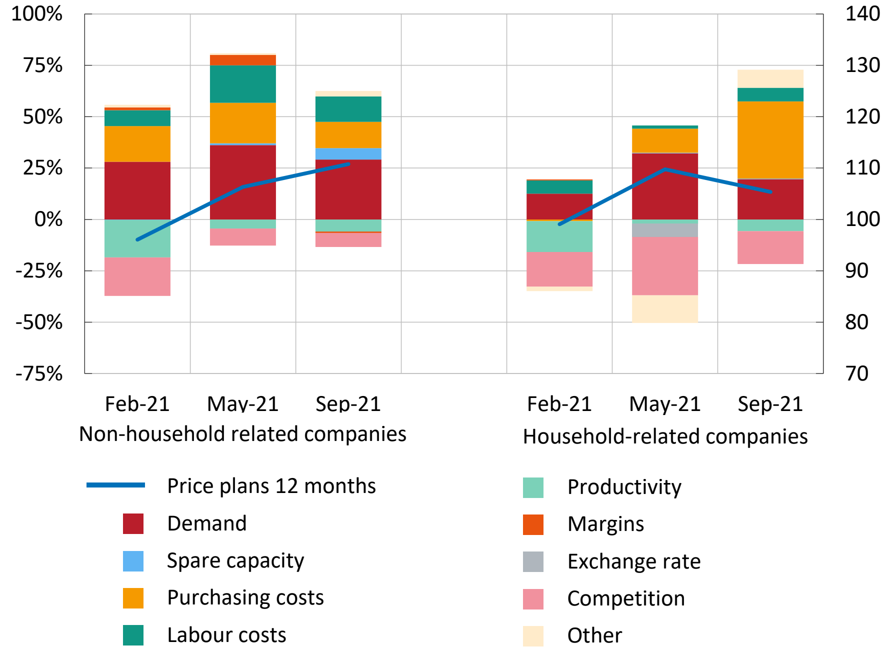
Note. The figure heading presents the question asked to those manufacturing and trading companies stating that they have experienced disruptions in the last three months.

Price rises in the trade sector are being delayed

The strong demand and high purchasing prices in the trade sector are also having an impact on sales prices, but how large this will be and when it will happen is generally more uncertain (see Figures 4 and 5). The building supplies and non-durable goods segments see possibilities to raise sales prices and price rises among suppliers have already started to have an impact on price setting here. In other parts of the trade sector, such as the clothing and sport segments, which carry out large seasonal purchases, the impact from increased purchasing and freight costs will come later and the assessment is that sales prices will have to be raised later on. However, tough competition is partly restraining price rises in the trade sector and hospitality industry. Some companies are therefore trying to manage the increased costs by increasing productivity or reducing margins instead of raising sales prices: "If we raise our price, we'll lose all our customers. If we lower our price, we'll lose money. We always have to match our competitors."

Figure 5. Factors behind pricing in the next 12 months

Net percentages and index



Note. The bars (left scale) show the net balance between responses that the factor concerned will have an upward or downward effect on prices in the year ahead. A bar above (below) zero means that the factor will contribute to rising (falling) prices in the period ahead. Index figures (right scale) show a standardised value (mean value = 100 and standard deviation = 10) of the net figures for companies that responded to the question regarding whether sales prices will be raised or lowered in the coming twelve months. Non-household related companies refers to manufacturing companies and those companies that mainly sell services to companies. Household-related companies refers to the trade sector and those companies that mainly sell services to households.

"People have very high wage demands just now"

The strong economic activity is being reflected by the labour market, where increasing numbers of companies are competing for persons with in-demand skills. Many companies need new recruitment and they report a relatively large shortage of competence: "It is a constant level of pain to find skilled labour." The hospitality industry has fairly small hopes of attracting previously employed staff back again: "They haven't been waiting for 18 months to be re-employed, but instead have moved on to other sectors or started studying." Staff turnover is relatively high and job seekers have high wage demands, which is also reflected by an increasing number of companies that expect rising rates of wage drift in the period ahead.

"The problem is that we have the same level of knowledge as prior to the pandemic"

Overall, companies consider that productivity increased during the pandemic but experience that the effect differs over the short and long terms: "Cancelled conferences, training courses and travel raise productivity in the short term but reduce it in the longer term." Creativity, the exchange of ideas, the acquisition of knowledge, productivity growth and workplace training have all suffered during the pandemic and are expected to restrain productivity growth in the long term. At the same time, many companies consider that digitalisation is increasing productivity. Different measures of productivity, for example sales per square metre of retail space or occupancy rate, which are used in the trade sector and by consultants, have also been high during the pandemic.

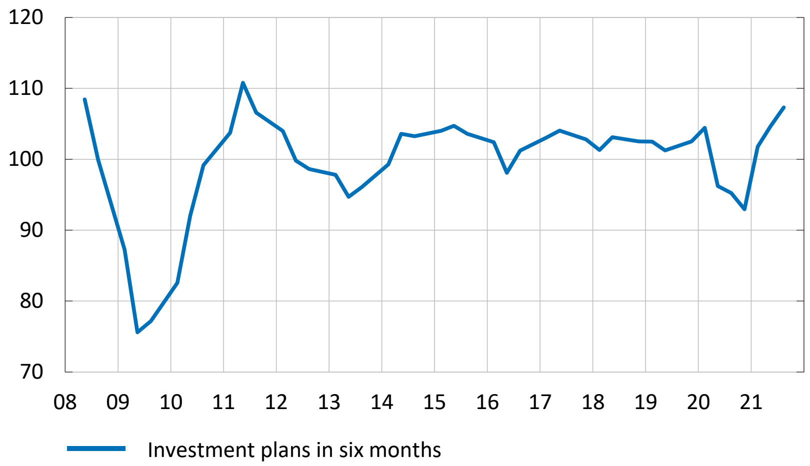
New technology is driving investments

Compared with the spring, more companies now plan to increase investments (see Figure 6). Among other things, investments are being aimed at increasing production and storage capacity, automation, electrification and IT. "We're having the most investment-heavy period in our history" says one business leader in the trade sector. The ongoing electrification and climate transition of society involves major investments in new technology in parts of the manufacturing sector. The investments are costly for companies and they already have a need to compensate themselves, in part, for that in their pricing. Many of the investments being made also benefit consultancy companies in technology, economics, IT and elsewhere.

Most companies in both the manufacturing sector and the trade sector report that investments over the last year have mainly been funded using equity and cash flows. Some companies have used bank loans and securities borrowing to fund larger investments but, for most, no new capital has been needed: "We haven't needed to increase our loans to fund our investments but have generated enough and more via cash flows."

Figure 6. Investment plans in six months, all companies

Index



Note. The series has been smoothed out with the moving average of three observations.

About the Riksbank's Business Survey

The Riksbank's Business Survey aims to reflect developments in prices and economic activity in the manufacturing, construction and trade sectors and some service sector segments. As only a few players account for a very large part of the Swedish business sector, relatively few interviews 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 enterprises.

Over 300 companies have taken part in the survey since it was started in 2007. In the surveys carried out during the period 2007-2019, around 30 companies were interviewed in February every year and around 45 companies in May and November. The interviews were carried out by Riksbank staff during visits of around one hour. As a result of the pandemic and its effects on the economy, the Riksbank held a total of eight rounds of telephone interviews with the larger Swedish companies during 2020. The interviews are, as a rule, 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.

This report for September 2021 reports the result of telephone interviews with 51 companies and trade associations, mainly conducted over the period 21-29 September. Unless otherwise stated, the figures 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 companies' reflections during the interviews.

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.

http://archive.riksbank.se/Documents/Rapporter/POV/2012/rap_pov_artikel_3_121017_eng.pdf

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