

The Riksbank's Business Survey

Bargain hunting intensifies

May 2023

The Riksbank's Business Survey in May 2023¹

The economic situation is expected to remain weak in the coming six months. But the business sector is clearly divided, both in terms of its view of economic activity and the need to continue raising sales prices.

The manufacturing sector in general, and the export industry in particular, state that demand is strong, there are plenty of orders and the production rate remains high. Profitability is good and is also reinforced by the weak krona. Over the past year, the manufacturing sector has been prepared for a slowdown in economic activity, and has been surprised that it has not yet happened.

For the retail trade, however, demand is weaker than normal. High inflation has weakened households' finances and sales volumes are declining. It is also clear that households are increasingly looking for cheaper alternatives and/or choosing not to buy certain goods, which further impairs the profitability of the sector. The cost increases continue to be a concern for the retail trade, which experiences increased purchasing costs when the krona is weak.

For the construction sector, the sharp fall in demand for new housing has led to a rapid changeover to other types of construction, particularly community buildings and infrastructure. The larger construction companies have thus managed to reallocate their resources and have so far avoided major staff reductions. However, small companies in the construction industry, which are often less diversified, are having a more difficult time.

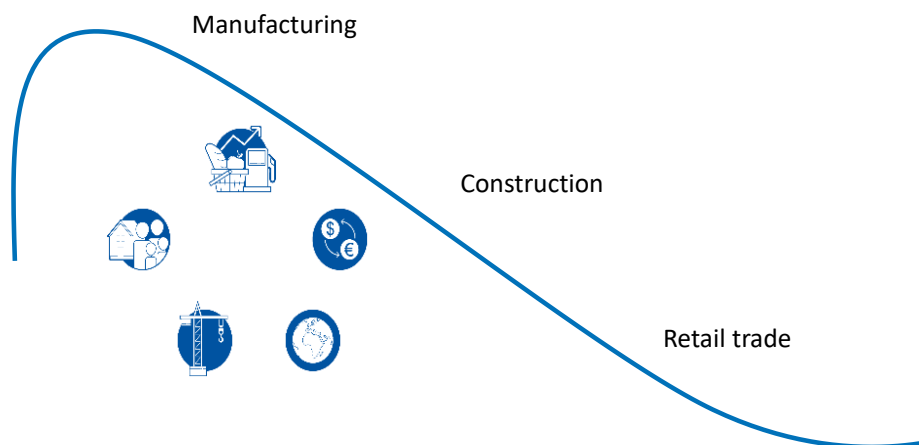
The division in economic activity is also reflected in companies' pricing plans. The manufacturing sector, which previously raised its prices quickly and rapidly, now states that cost pressures have declined, and that it is not planning to raise sales prices to the same extent as before. On the other hand, the retail trade plans to continue raising sales prices to compensate for the increased costs and declining profitability.

¹ During the period 26 April-10 May, the Riksbank held interviews with 43 companies in the manufacturing, construction, trade and service sectors. The Riksbank's Business Survey is published on the Riksbank's website. All quotations in this report are from respondents to the survey.

"The picture of the economy is divided"

Economic activity remains weak, but has not deteriorated quite as much as companies expected in February. The differences in how the economic situation is currently perceived between companies in different sectors can be illustrated as in Figure 1. There is a clear division in the view of economic activity, which is mainly related to the deterioration in household purchasing power and the weak krona. It is still the companies with close links to households that feel the effects of the poor economic activity. For example, the retail trade is noticing that households' purchasing power has deteriorated and thus also their demand. Demand for residential construction has also declined further since February, but the larger construction companies are doing relatively well as they have to a large extent been able to convert their production from housing to community buildings and infrastructure.

Figure 1. Good economic activity for the manufacturing sector, but worse for the retail trade sector



Note. The figure illustrates how the differences in the economic situation are currently perceived between companies in different sectors. The images represent the uncertainty regarding international developments, the exchange rate, housing construction, inflation and the deterioration in household purchasing power.

In contrast to other sectors, the manufacturing sector continues to meet strong demand, especially globally. Over the past year, they have been prepared for the economy to slow down, but continue to be surprised that it hasn't happened yet. One business leader says: "There should be a downturn but it keeps getting postponed." "The indications are there but they are not strong," says another with regard to an expected slowdown. Another sign of economic slowdown that is mentioned is that it takes somewhat longer to conclude deals as a result of the uncertainty over how demand will develop going forward. So far, however, there is no sign of a decline in the manufacturing sector's order books.

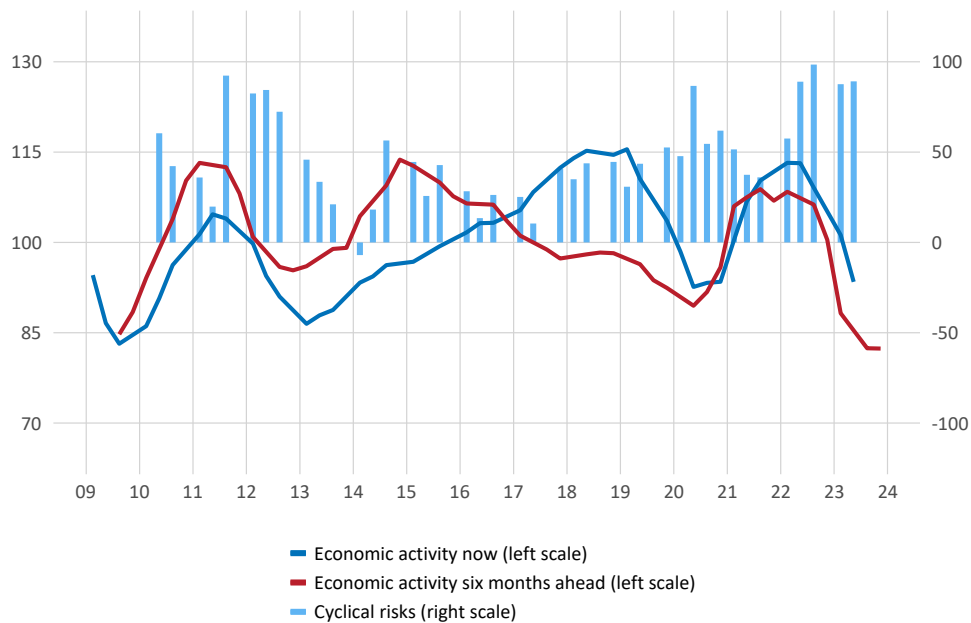
“The situation is more uncertain than usual, where are inflation and interest rates headed?”

The risks that economic activity will deteriorate are still considered to be substantial, see Figure 2. The reasons are the previously known global risks related to the war in Ukraine and China's relations with Taiwan, but also foreign exchange developments play a part. It is especially difficult to know how well households can cope with high inflation and higher interest rates. "So far we haven't seen the real effects of the interest rate hikes," says one business leader, reflecting the concern that household purchasing power will deteriorate further.

There are still considerably more people who believe that the economic situation will be worse in six months' time than believe that it will be better. But expectations seem to have stabilised somewhat – at least no more than in February believe that the economic situation will deteriorate, see Figure 2.

Figure 2. 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 columns 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.

“Manufacturing sector - the big engine has been chugging along”

Export companies see a relatively unchanged strong situation compared with February. Profitability is good and it is reinforced by the weak krona. Investment plans remain at high levels. Transport, consultancy and staffing companies that have the manufacturing companies as customers also confirm this picture, and they are also developing favourably.

It is particularly the automotive and technology industries that have a strong order intake and a continued high rate of production. Some mention that order intake has normalised somewhat, although from a high level. The food industry is satisfied with economic activity. “Everyone needs to eat,” even in hard times, as one business leader puts it. The forest, wood and pulp industries, on the other hand, are experiencing a much worse demand situation than in February as sales of wood, board and paper are decreasing. The shrinking residential construction also affects the demand for building materials manufactured in certain parts of the manufacturing sector.

“A year ago, housing accounted for 40 per cent of our orders, now that figure has been more than halved”

Major construction companies note that orders have declined in recent months. In particular, the project mix in the order book has changed, as the proportion of new housing projects has decreased rapidly. Weakened purchasing power among households and falling prices on the secondary market have made it more difficult to balance the budget when building new tenant-owned housing projects. Balancing the budget is also more difficult for rental apartments, where the client is often a large property company.

For larger construction companies, this is partly offset by good demand for other projects such as civil engineering works, infrastructure and community buildings. One respondent noted that “a year ago, community buildings accounted for a few per cent of total new orders, now they account for half”. Small companies in the construction industry, which are often less diversified, generally have a tougher financial situation, and several have also given redundancy notices to parts of the workforce, says a larger construction company.

“There is competition for projects”

When demand for residential construction decreases, construction companies need to review staffing. One actor noted: “We have too many employees in housing. On the other hand, we need more labour in community buildings, infrastructure and civil engineering works. We are primarily solving this through internal relocations.” This has led to increased competition for these projects. Several of the construction companies note that negotiations on these projects are now tougher and that this leads to lower profitability for them.

Residential construction: An ice cold streak through the business sector

The reduction in demand for housing has a clear impact on other sectors as well. The forestry and steel industry, which supplies building materials, notes that housing construction is particularly weak and that demand for, for example, wooden frames for new homes is largely non-existent. Engineering consultants also note lower demand for housing-related projects. The transport industry is worried about future developments and one business leader says: “[Construction] is a large sector with a lot of transportation, so it has a major impact.” Among those who supply other input goods, such as electrical components, to construction several testify to weak demand and one respondent notes that “there is a broader decline in sales to new construction now than in February”.

“Consumers are more price-conscious nowadays”

Retailers and food producers note that households are much more price-conscious now than in February. For one grocery retailer, this is reflected in a sharp increase in the proportion of goods sold on campaign. Another respondent testifies that bargain hunting has led to more and more people shopping for a smaller amount than before: “Previously, 10 items were purchased for SEK 200, now it is 10 items for SEK 150.”

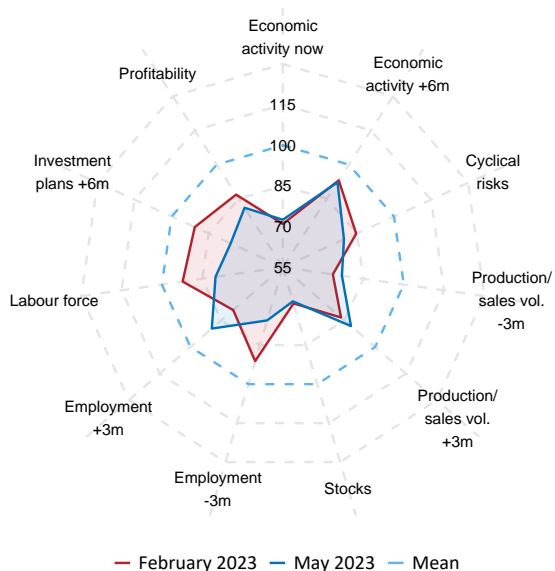
In the durable goods sector, the situation with regard to sales and economic activity is described as gloomy, as evidenced by a smaller share of store visitors choosing to make a purchase. In the manufacturing sector, the decline in sales is reflected in the reduced demand for packaging board. The building trade is experiencing weaker demand for goods related to certain renovations, but there is higher demand for goods that can lead to energy savings: “Roof and window renovations are doing better, it's about an increased need for energy savings”.

“I think that it will take a little longer before the retail trade bottoms out”

Sales in the retail sector have declined, and one respondent notes that they are “coping as best they can” and that many have reduced their staff. This has mainly taken place through natural departures, but some companies have also actively reduced their workforce. Many companies in the retail sector have also chosen to cut back on their investment plans, see Figure 3. One business leader notes, with regard to investments, that “we have put the brakes on”.

Figure 3. Retail trade overall response pattern

Index

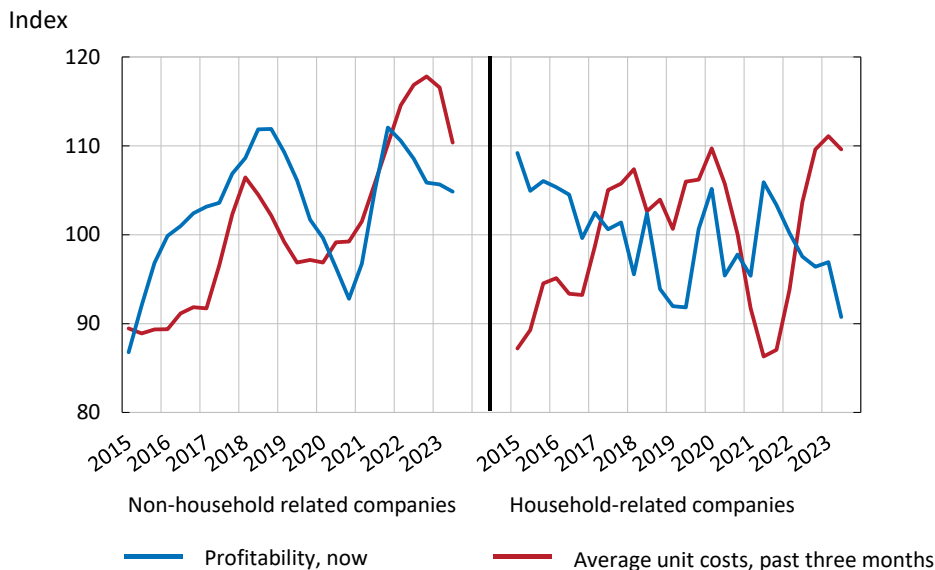


Note. The responses to the questions are plotted along ‘spokes’ in the figure, where an index figure closer to the centre is worse. The historical average is calculated from the date when the question concerned was first included in the survey. The terms -3m and +3m refer to the most recent three months and the coming three months respectively. The term +6 m refers to the coming six months. Increased risks to economic activity entail a deterioration and therefore a lower index figure.

Cost pressures easing

Companies’ costs are rising, but not as fast as before, see Figure 4. Costs for freight and commodities, such as coal and iron, have fallen. Energy costs have also not risen as much as expected. However, agreements that were signed earlier mean in many cases that the impact will come with some delay. The larger construction companies believe that material costs have “begun to correct themselves”, while the manufacturing sector continues to see that subcontractors want to compensate for their own cost increases in their pricing. The retail trade and the services sector still see the increased costs as a problem. They also mention rent increases, and above all the weak krona, which has a negative effect on their purchasing prices for goods and services. Labour costs are generally increasing as a result of the new central wage agreements.

Figure 4. Profitability and average unit costs, last three months



Note. The index figures show a standardised value (average = 100) and standard deviation = 10) of the net total for the companies that currently assess the company's profitability as good and bad, and the net total for those companies that estimate that unit costs have increased or decreased over the last three months. The series have been smoothed out with a moving average based on three observations. Non-household related companies refers to manufacturing and construction 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.

Poorer profitability in line with declining sales

Among household-related companies, profitability has deteriorated sharply compared with February, see Figure 4. They mention that they have not fully succeeded in compensating themselves for cost increases. In addition, sales are declining and some are now accepting poorer margins in order to sell more. One respondent notes, for instance, that “we have a low price brand that we try to protect and reinforce” and “we therefore try to manage the cost increases as far as possible with lower margins”.

Export companies are instead experiencing good profitability that is above the historical average. The weak krona gives a “doping effect” that keeps their margins up, while the strong demand has made it possible to transfer the increased costs to customers to a large extent. Margins have strengthened further, as the impact of previous sales price increases is now taking effect, at the same time as some costs have begun to slow down. One business leader says: "Inflation is not a problem for us, we just raise prices."

“We don't get a rush in the shops when we don't have a sale”

Competition, which held down prices in the retail trade prior to the upswing in inflation, does not affect the plans of household-related companies to raise sales prices to

the same extent as before. "I think everyone is in the same boat here," concludes one respondent. Companies are looking at their own needs to cover increased costs and following competitors' pricing to a lesser extent.

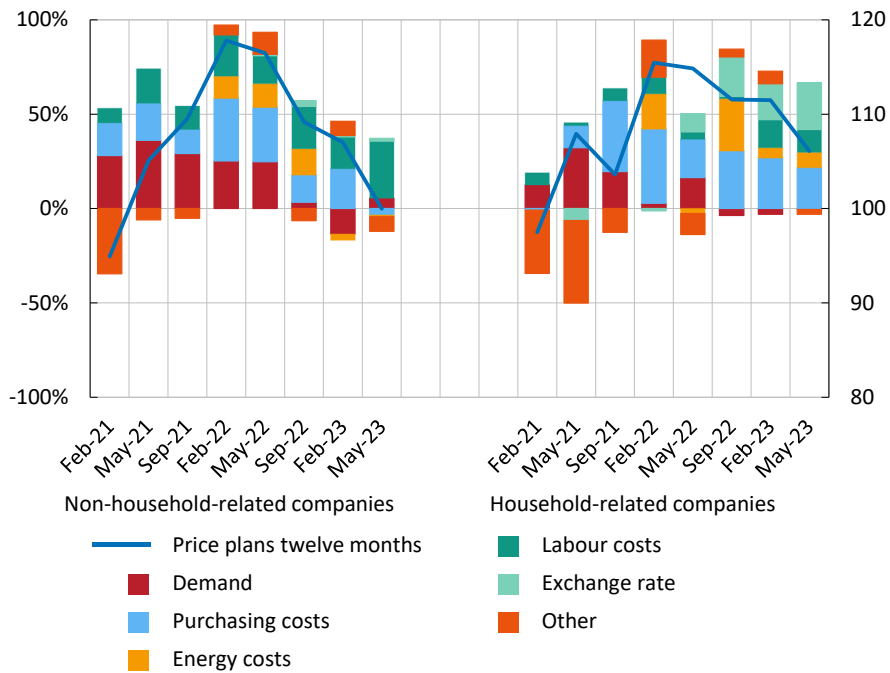
However, competition for customers' declining purchasing power is mentioned as an important factor leading to discounts and reduced prices. There is considerable pressure in the retail sector to hold campaigns, but it has declined somewhat since the first quarter of this year. Now several respondents describe how they are trying to reduce the use of discounts, but that it is difficult because of the stiff competition and declining sales. However, the strategies regarding discounts versus regular sales prices look different in different companies. One retail sector business leader says: "We are increasing the outward prices and trying to keep the discounts at a minimum." Others choose to reduce the discounts but instead try to push down the regular sales prices. Several companies in the durable goods trade report that they are starting to implement new measures to avoid further price increases. It is mentioned, for instance, that they are buying fewer goods that have increased a lot in purchasing price. The aim of the different strategies is the same, that is, to attract customers and increase sales volumes.

"We will try to increase prices if possible"

The view of future price developments differ between household-related and non-household-related companies. For those planning to raise sales prices, it is mainly labour costs, purchasing costs and the exchange rate that are affecting them, see Figure 5. Fewer companies than in February are planning to raise sales prices and more, especially in manufacturing, are planning to lower sales prices in the coming year. Manufacturing and construction companies, whose costs are no longer increasing as quickly, intend not to raise sales prices to the same extent as before. The retail trade sector is instead planning to continue raising sales prices in the coming year to compensate for cost increases and thus avoid "selling at a loss".

Figure 5. Driving forces behind pricing in the twelve months ahead

Net percentages and index figures



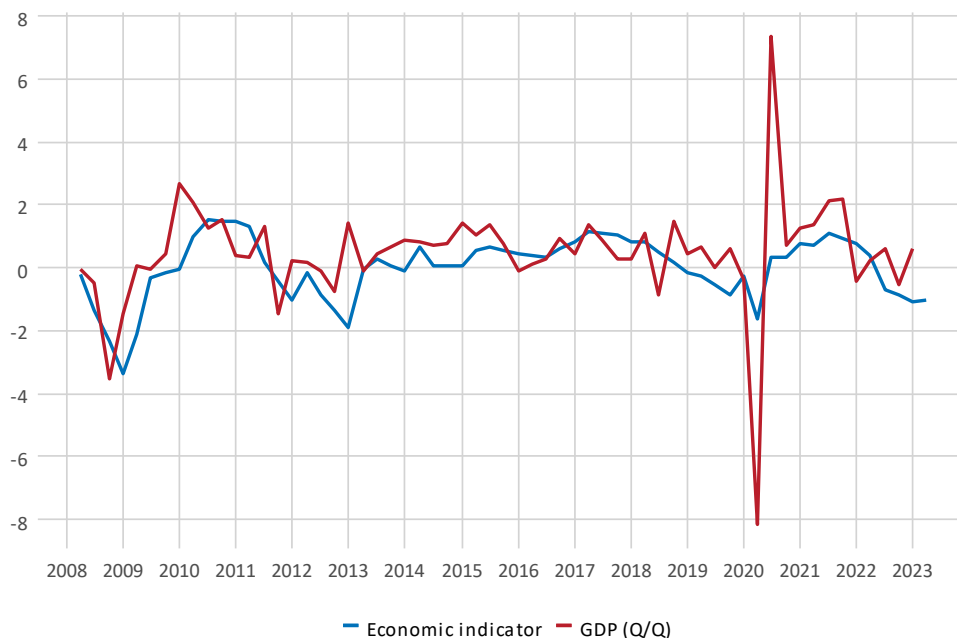
Note. The columns (left scale) show the net balance between responses that the factor concerned will have an upward or downward effect on prices in the year ahead. A column above (below) zero means that the factor will contribute to rising (falling) prices in the period ahead. Index figures (right scale) show a standardised value (mean value = 100 and standard deviation = 10) of the net figures for companies responding to the question regarding whether sales prices will be raised or lowered in the coming twelve months. Non-household-related companies refers to manufacturing and construction 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. The item "Other" includes, among other things, spare capacity, marginal changes, productivity growth, and competition.

ARTICLE - An early indicator of economic activity

The Riksbank has produced an economic indicator to make use of the information from the Business Survey and to obtain an overall picture of the economic situation in Sweden. The economic indicator for the second quarter of 2023 indicates that the economic situation will continue to be worse than average, see Figure 6. Compared with the second quarter of last year, the economic indicator has decreased significantly.

Figure 6. Business Survey's economic indicator and quarterly GDP change

Standard units and quarterly change, per cent



Note. The economic indicator has been standardised to mean zero and standard deviation one. A positive value indicates that the situation is better than the historical average and a negative value indicates that the situation is worse. The GDP series is seasonally adjusted.

Sources: Statistics Sweden and the Riksbank.

The economic indicator has been produced with the aid of what is known as a principal component analysis. Such analysis aims to identify the most important patterns and relationships between a set of by variables and is considered an effective means of summarising information from a large dataset.² By extracting common movements from the data material, the analysis generates a number of latent variables - principal components - where the first component captures most of the variation in the data material.³ The Business Survey's economic indicator is made up of the first principal component and it explains about 56 per cent of the variation in the data.

² See for example Bernanke and Boivin (2003), Stock and Watson (2002 and 2006).

³ For a more detailed description of principal component analysis, see, for example, Jolliffe (2002).

In the process of developing the economic indicator, several different sets of variables were tested and then evaluated based on how well they correlate with Sweden's GDP development and how well they can predict GDP development. The final economic indicator consists of eleven variables.⁴ The companies' responses to the eleven questions in the Business Survey are included as variables in the economic indicator have been weighted against the size of the companies (number of employees) and then the net totals have been standardised to mean zero and standard deviation one. As the Business Survey is only conducted three times a year, the series have been interpolated to quarterly data before standardisation. The economic indicator has been standardised in the same way as the individual variables, which means that a positive value indicates that the situation is better than the historical average and a negative value indicates that the situation is worse.

The correlation between the Business Survey's economic indicator and Swedish GDP development is relatively strong, see Figure 6. A linear regression shows that the correlation coefficient of the indicator with quarterly changes in GDP is 0.81. During the three quarters that the Business Survey is conducted, the results are published about two months before the official GDP outcome is published. The economic indicator can therefore provide valuable information about the economic situation in Sweden at an early stage.

References

Bernanke, Ben S. and Jean Boivin (2003), "Monetary Policy in a Data-Rich Environment", *Journal of Monetary Economics*, Vol. 50, No. 3, pp. 525-546.

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⁴ The eleven variables are: Economic situation now, Economic situation in six months, Investment plans, Profitability, Access to external financing, Number of employees in the last and next three months, Production/sales in the last and next three months, and New orders in the last and next three months.

About the Riksbank's Business Survey

The Riksbank's Business Survey should reflect developments in prices and economic activity in the manufacturing and construction industries, the retail sector and parts of the service sector. 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 companies interviewed 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 and video interviews with companies and trade associations in 2020. Nowadays, between 30 and 50 companies and trade associations are interviewed on each occasion. With effect from May 2022, a number of the interviews are once again conducted in the form of visits. The interviews are usually conducted with members of the company's management. The interviews 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. The response rate for the survey is high and is often around 95 per cent.

The results of the survey are presented in a report published on the Riksbank's website, usually three times a year. The May 2023 report presents the results of interviews with 43 companies. The survey was conducted mainly during the period 26 April -10 May. 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 reflect 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.

[The Riksbank's business survey – a quick indicator of economic activity](#)



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