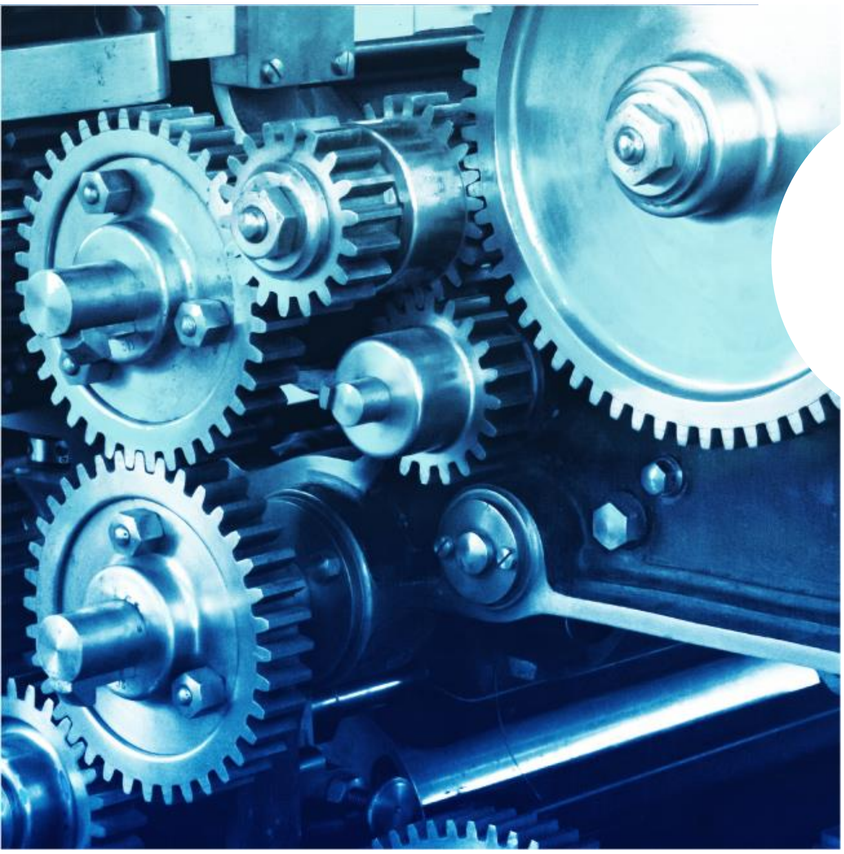
THE RIKSBANK'S

BUSINESS SURVEY



Costs accelerating, economy slowing down

SEPTEMBER 2022

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

The Riksbank's Business Survey in September 2022[1]

The economic situation remains good for most companies, but there are also growing signs that demand is beginning to decline. It is mainly respondents in the manufacturing industry who are most satisfied with the situation, while parts of the retail trade believe that demand is already weak as a result of high inflation undermining households' purchasing power. In the construction industry, the production rate is still high, but there are clearly fewer orders for new housing. A clear majority of companies expect the economic situation to deteriorate over the next six months. They point out energy prices and how they will develop as the greatest risk factor.

Costs have risen rapidly in recent years due to strong demand, together with production and supply disruptions and a shortage of key inputs. This has also led to higher prices. Prices are now rising more frequently and in larger steps than before. It has also become difficult to reach agreements on prices for deliveries in the future, as there is greater uncertainty about how much these costs will increase. The companies are generally planning to increase prices in the coming year as well.

The expected economic downturn has not yet affected employment. On the contrary, the demand for specialist skills has increased and their shortage is now more evident. Although the salaries of specialists have increased, both companies and the social partners that the Riksbank has interviewed believe that salaries over and above agreements, so-called wage drift, are currently a relatively small problem compared with other cost increases. Both the companies and the social partners expect the forthcoming wage bargaining rounds to be more challenging than for many years, given the macroeconomic situation with high inflation. There is also great uncertainty as to how long the agreements will apply. At the same time, there is strong confidence that the negotiations will lead to central wage agreements that the whole labour market will follow. Several factors suggest higher general wage demands than in the wage bargaining rounds of recent years. For example, there is now a greater shortage of labour, wages in competing countries are higher and companies have a relatively good profitability.

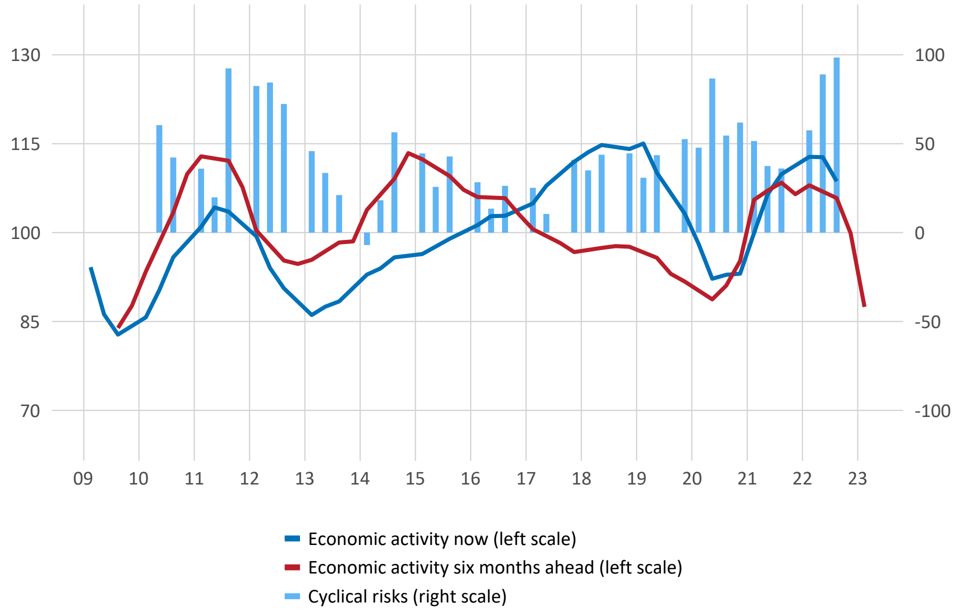
[1] During the period 20-30 September, the Riksbank held interviews with 39 companies in the manufacturing, construction, retail trade and service sectors, as well as with 9 social partners. The Riksbank's Business Survey is published on the Riksbank's website. All quotations in this report are from respondents to the survey.

"We are preparing for a downturn"

The rates of production and sales are still high, but at the same time economic activity has slowed somewhat compared with the survey last spring, see Figure 1. Several indicators suggest that economic activity is beginning to weaken. For example, world market prices for several commodities that were previously high have fallen, which may indicate that global demand is now weaker. The number of transports abroad seems to be decreasing, while transport vehicles are used less frequently in Sweden and fewer containers are shipped both to and from the country. Earlier this year, the manufacturing industry met a very strong demand, but is now seeing somewhat fewer orders for capital-intensive equipment, which is a pattern that is normally seen in connection with an economic slowdown. Sales are sluggish in the non-durable goods trade in particular, and several companies are now describing the economic situation as poor. On the whole, companies in all sectors believe that the economic situation will be poorer in six months' time.

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 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.

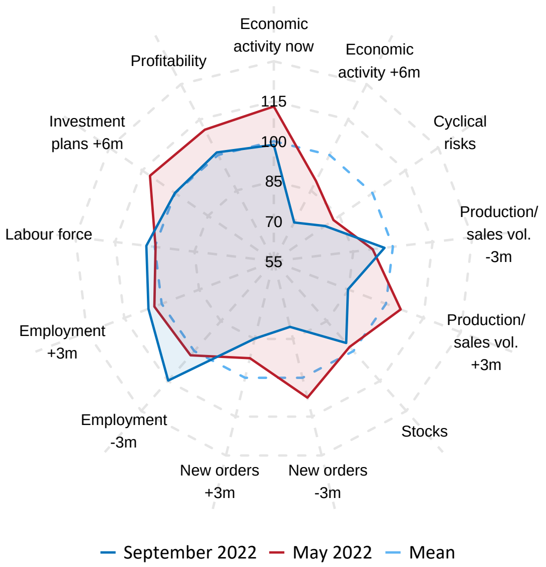
"Difficult to envisage Europe not having a fairly hard landing"

Companies point to several risks which, taken together, make it more difficult than normal to assess how the economy will develop. It is primarily the development of energy prices that is worrying, but also the rise in inflation and interest rates, and the effects this may have on household demand for goods and services. Retail trade companies, which generally import goods, mention in particular the weak development of the krona recently as a major uncertainty factor.

The exporting manufacturing companies, on the other hand, benefit from the weak Swedish krona. One manager states that "the best thing that can happen is that the dollar gradually appreciates". It is also noted that demand for Swedish goods in the Americas remains high. In Asia, it is more mixed situations where some countries have strong demand, while China, for example, has weaker demand, partly as a result of the previous pandemic-related shutdowns there. Economic activity in Europe is more worrying and manufacturing companies see several signs of a slowdown. For example, the inflow of orders to the manufacturing industry has generally weakened over the past three months and companies assess that it will continue to develop weakly over the coming three months, see Figure 2.

Figure 2. The companies' overall response patterns

Index



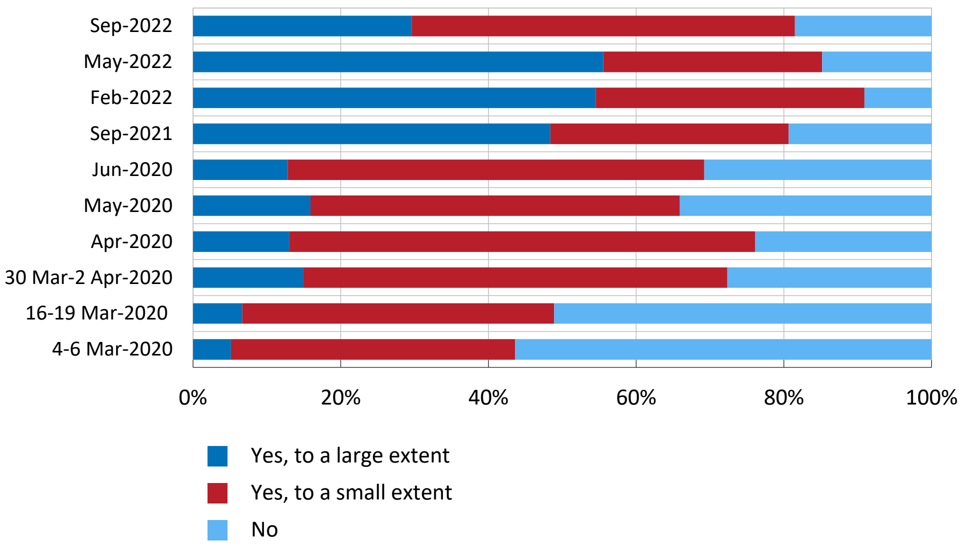
Note. The responses to the questions are plotted along 'spokes' in the figure, where an index figure closer to the centre is worse. Increased risks to economic activity entail a deterioration and therefore a lower index figure. Stocks refer to stocks of finished goods and reduced stock size means a higher index figure. The historical average is calculated from the date when the question concerned was first included in the survey. The 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.

"The disruptions have already declined"

Disruptions to companies' operations are less now than in the spring, see Figure 3. This is partly explained by the improvement in container capacity and the reduction in the shortages of several inputs. However, although the overall situation is better, there is still a significant shortage of semiconductors. Moreover, the construction industry says that there is still a shortage of construction materials, such as windows, wooden flooring and fan systems, but that it is not as tangible as in the spring. In the manufacturing industry, the disruptions have led to the building up of input stocks. While this is costly, companies do so to deliver their finished goods on time, thus avoiding any deterioration in customer relations. Compared to the May survey, only one third of companies now believe that the disruptions will affect their operations for more than six months.

Figure 3. 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 is a significant slowdown in housing construction"

The large construction companies are satisfied with the current economic activity, which is mainly due to the fact that they have several projects waiting for construction to start. "In order-stock terms, things look good" as one respondent expresses it.

However, construction companies are pessimistic about how construction activity will develop in the future and believe that there will be a generally weaker demand, especially for new housing. The number of requests for tenders has decreased, as has the demand for construction companies' own tenant-owned housing projects. In general, demand for commercial construction is judged to be weaker than for public sector construction. However, the demand for premises and infrastructure remains stable and good. Here there is an increased demand for construction of new transmission capacity, such as new power line corridors, and wind farms.

"There are a lot of factors now that mean customers have less in their wallets"

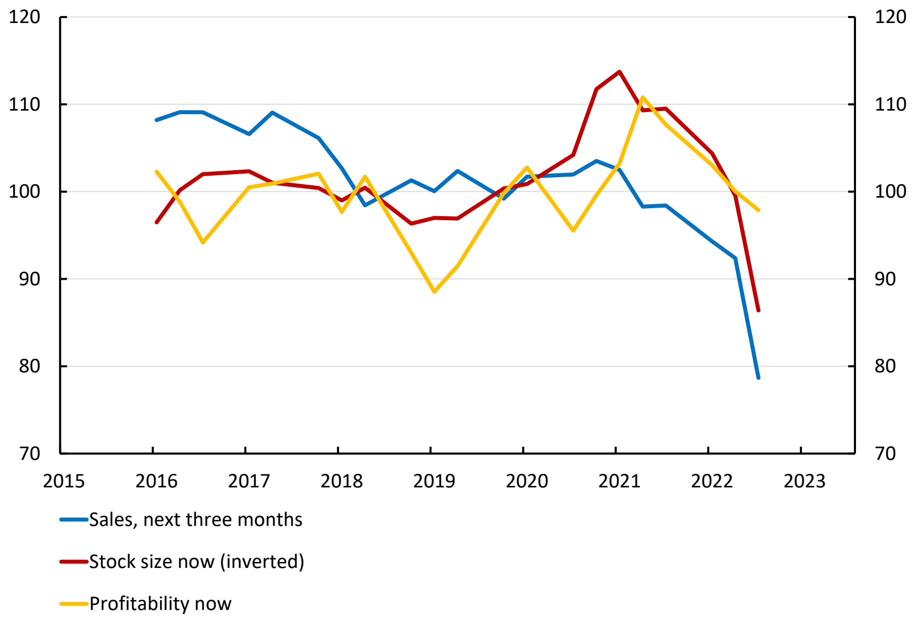
The expectations of trading companies for sales over the next three months are now clearly lower than earlier this year, see Figure 4. The non-durable goods trade, which has had good sales during the summer, is now seeing a decline in demand, which is judged to be largely due to the high inflation that is eroding household purchasing power. Some say that customers adapt their shopping basket so that expenditure is the same level as before, despite rising prices. The fact that households are more price-conscious favours low-price shops in the grocery trade. Rising interest expenditure also risks leading to households becoming more restrained in their purchases, especially with regard to durable goods. One manager comments that "people will buy less for Christmas and at the end of the year because they feel stressed, poorer and worried about finances."

In the durable goods segment, the pandemic effects with high demand for consumer electronics and home furnishings, for instance, have decreased and sales are expected to continue to fall in the next three months. The clothing trade reports that households' pent-up demand for new clothes after the pandemic has now slowed down. The fact that the krona has depreciated against the US dollar is mentioned by several in the retail trade as a major contributing factor to the deterioration in profitability. They consider it difficult at present to raise prices to fully compensate for the increased costs.

At the same time, while profitability has deteriorated and sales are expected to decline going forward, the retail companies also consider inventories to be somewhat too large, see Figure 4. The main reason for this is that they previously experienced disruptions in production and supply and therefore brought forward orders and ordered extra goods to avoid being left with empty shelves. The recent subdued demand has also contributed to the fact that sales have not been as large so far this autumn as was hoped for.

Figure 4. Sales, stock size and profitability in the retail trade

Index, three observations moving average



“The big problem is that all costs are increasing”

Costs have increased over the past three months and increases in costs of purchasing goods are described as both larger and more frequent than before. Manufacturing companies are describing an “enormous inflation” on prices of inputs, while the costs of energy and transport are continuing to rise. Although spot prices for freight have fallen since the spring, prices in the longer contracts have, on the contrary, risen. To secure transports, companies need to accept higher prices for longer contracts.

There are several examples in retail trade of costs now increasing more often and in greater steps than before. For example, one retail company has hired extra staff to have time to change prices at the same pace as costs increase. Another respondent explains that during July they had cost increases of twice the value of a normal year.

For service companies, it is above all higher wages that are pushing up costs. However, they believe that these cost increases are manageable and have so far been able to pass them on to customers. However, service companies are not used to other costs, such as fuel prices and rents, increasing as much as they are doing now. Like many in the retail trade, they are concerned about the increase in rents that will take place at the turn of the year, which is based on the outcome of the consumer price index in October. There is uncertainty over how much of the increased costs can be passed on to customers going forward. One manager notes that "cost control will be very important in 2023”.

“We're constantly raising prices”

More than two out of three companies respond that they are now raising prices more often than normal, and that this is mainly because their costs are constantly increasing. Those who consider the rate of price increases to be more normal are those who follow world market prices or those who have fixed price contracts. Of those aiming to raise prices in the coming year, nine out of ten companies expect the increases to be higher than normal.

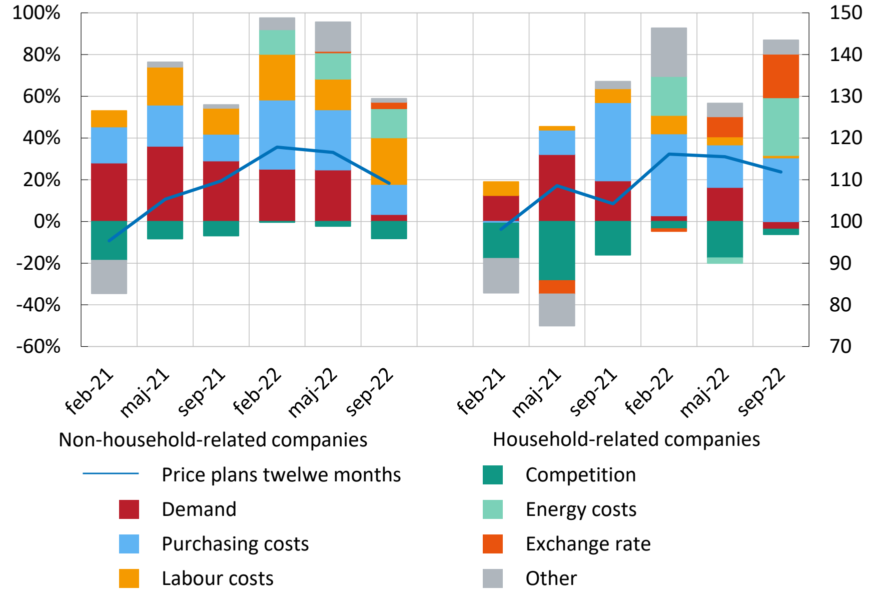
One manager in the manufacturing industry notes that some prices that have largely remained stable for ten years have now been raised several times in a short space of time. Another respondent in the retail trade points out that “most people who work here have never experienced raising prices” and price increases are therefore a new exercise for them. A further change in how companies tend to set their prices is also noted. Normally, prices on old or outgoing models are not increased. In the past, only prices for new models with better quality were increased, while prices for old or outgoing models were reduced. But one respondent observes: “Now prices are being raised on both old and new goods. This has never happened before”. While there are some companies that are unable to keep up with raising prices as at the same pace as costs, there are others that are raising prices a little extra now to compensate for expected higher costs in the future: “When we get an increase in the purchase price, we might add a little, little extra.”

“The base scenario is that we should continue to raise prices”

The companies are planning to increase prices in the coming year. It is mainly increased costs for purchased goods and energy that are expected to contribute to price increases going forward, see Figure 5.

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 rental costs.

In all sectors, companies are pointing out that energy costs are not normally very important for pricing, but that they are now expected to have a major impact on price developments going forward.

For non-household-related companies, it is primarily weaker demand and stiff competition that are expected to hold back price increases going forward. In the Riksbank's survey in May, demand was judged to contribute to future price increases, but this effect has now largely disappeared.

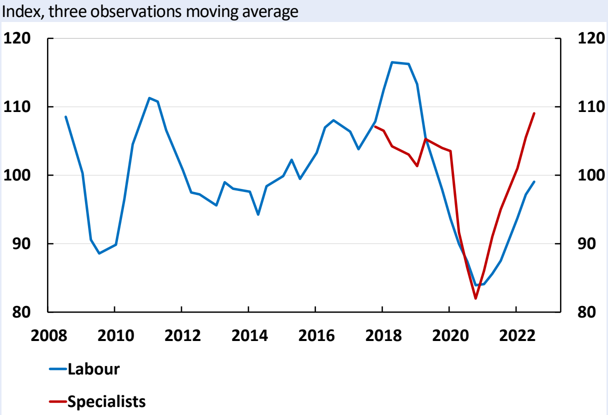
The companies selling to households believe that the exchange rate will have a major impact on sales prices: "What stands out and has the greatest impact in the short term is the dollar. No question about it." Competition, which in the past limited the ability of household-related companies to raise prices, is now of little importance because "everyone is raising now". Similarly, demand is considered to have a dampening effect on price developments.

ARTICLE – "The Swedish model will be preserved. This is in everyone's interests."

In this survey, we asked companies and some of the social partners about labour shortages and wage drift, i.e. wage increases over and above the central wage agreements. The shortage of specialists continues to be more tangible than the general shortage of labour. It is mainly the shortage of specialists that is leading to higher salaries and longer recruitment times. Wage drift is currently considered to be of less concern than other cost increases for companies. Both companies and the social partners say that they have great confidence in the Swedish wage formation model, although there are concerns that it may be difficult to reach agreement in the forthcoming wage bargaining rounds in the light of high inflation, for instance.

"There is a shortage of highly skilled, trained and at the same time driven people"
The poorer economic outlook has not yet had any negative impact on employment. In September, the shortage of specialists continued to increase, see Figure 6. Since the beginning of 2021, it has become more difficult to obtain both types of labour.

Figure 6. Is there a general shortage of labour and/or a shortage of specialists?
Index, three observations moving average

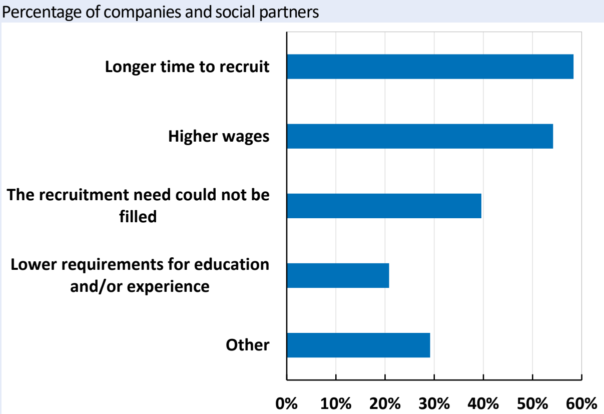


Note. The graph heading presents the two questions (composed) submitted to companies as from the November 2017 survey. The question regarding labour shortages was then expanded into two questions: one regarding general labour shortages and one regarding the shortage of specialists. The reason for this is that so many companies responded to the previous question that there was no general shortage of labour, but there was a shortage of specialists.

"Everything to do with IT is difficult to get hold of"
Examples of specialists companies often mention include personnel in support functions such as finance, marketing, engineering, law, IT, logistics, and research and development. In particular, the difficulties in obtaining IT personnel are mentioned: "If you want an IT consultant, you have to decide quickly or they will disappear." Other specialists mentioned are skilled workers such as "qualified chefs". However, it is generally easier to obtain manufacturing industry workers and shop staff, for example, when needed. Some also point to the fact that Russia's invasion of Ukraine has increased the shortage in professions such as lorry drivers, construction workers and tree planters.

"Shortages driving wage drift"
Both companies and social partners generally consider the shortage of labour and specialists to have led to longer recruitment times, higher salaries and to companies failing to meet recruitment needs, see Figure 7.

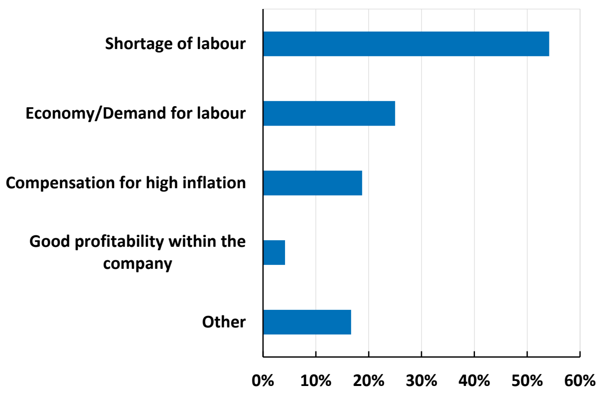
Figure 7. What consequences has the shortage of labour/specialists had in the last six months?
Percentage of companies and social partners



Note. The question, stated in the figure heading, was addressed to a total of 39 companies, as well as 9 social partners. Two companies and one social partner chose not to answer the question for various reasons. The item "Other" includes less expansion/turnover than desired in the business, cancellations of business deals, delays in projects, closures of parts of the business, redistribution of tasks to existing staff, changes in geographical location for hard-to-recruit positions, recruitment abroad, and increased use of consultants, contractors and/or temporary employment agencies.

Labour shortages can lead to wage increases over and above the agreements, so-called wage drift, which can push up companies' costs.[2] The companies and social partners estimate that it is mainly the shortage of labour that is driving wage drift, see Figure 8.

Figure 8. In your assessment, what are the main factors driving wage drift at the moment?
Percentage of companies and social partners



Note. The question, stated in the figure heading, was addressed to a total of 39 companies, as well as 9 social partners. 8 companies chose for various reasons not to answer the question. The item "Other" includes new recruitment, matching of competitors' offers, staff turnover, wage claims from job-seekers, changes in the composition of the workforce, and investments in research and development.

The rate of wage drift is normal or slightly higher than normal

A large-scale wage drift may, for example, lead to an increase in the starting wages, which in turn may lead to an impact on the entire internal wage structure. Three out of five companies considered that wage drift is now developing normally, while the remainder consider it to be somewhat higher than normal. Those working in the manufacturing and construction industries in particular believe that wage drift is now higher than normal.

"Wage increases pale into insignificance compared to other cost increases"

Many companies consider that the increase in wage costs has been manageable or less worrying in relation to other cost increases in the past year. Others emphasised that wage drift only occurs for a small part of the workforce and therefore does not have major implications for the business as a whole. For example, it was observed that wage drift only exists for certain officials, and that for the vast majority of employees, it is the collective agreements that determine their wage development. The companies generally take a restrictive approach to wage drift as they want to maintain the wage structure.

The wage bargaining rounds in 2023: "I cannot imagine a situation where the Swedish model has been under greater pressure"

Both companies and the social partners have strong confidence in the Swedish wage agreement model as a means of achieving central wage agreements that all of the social partners will follow. The coming negotiations are expected to be more challenging than previously as a result of the high inflation that is eroding wage earnings. The parties are uncertain as to how inflation will develop and this may make it more difficult to conclude multi-year agreements. It is possible that the negotiations will take a long time and will not be complete by the end of March next year, when the current agreements expire. Several other factors also play a role, such as whether the social partners can coordinate centrally and remain in agreement all the way. In addition to wage increases, there is a possibility that lump-sum payments may be included in the agreements as a means of keeping the level of agreed wage increases low. Macroeconomic factors such as higher wages in European countries that compete with Sweden, a generally stronger labour market and relatively good profitability for companies suggest that wage increases may be higher than in previous wage bargaining rounds.

[2] Wage drift refers to wage increases in addition to wage revisions according to the current collective wage agreements. This also includes higher wages for new employees and compensation to retain existing staff.

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 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 and video interviews with companies and trade associations in 2020. Nowadays, between 30 and 50 companies and trade associations are interviewed on each occasion. As of May 2022, part of the interviews are once again being conducted in the form of visits. They 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 percent.

The results of the survey are usually presented in a report published on the Riksbank's website three times a year The report for September 2022 presents the results of interviews with 38 companies and 9 employers' and employees' organisations, and they were conducted mainly during the period 20-30 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 figures 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.

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

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