



The Riksbank's Business Survey

Industrial activity stronger than
expected

February 2017

The Riksbank's Business Survey in February 2017¹

According to Swedish manufacturing companies, international demand was stronger than expected and the economic situation has therefore continued to improve since last autumn.

It is primarily the export industry that is increasingly optimistic as production has increased and orders have risen. The companies believe that in the coming six months economic activity will remain good, although there is some concern over political developments abroad.

Companies that have Sweden as their primary market are still satisfied with developments. The retail trade and services sector report that consumers have good purchasing power, at the same time as construction is at full throttle. The construction sector is still experiencing an economic boom and personnel shortages are becoming increasingly apparent in several professional groups. Other sectors are not perceiving any general problems in obtaining personnel, but as before are still finding it difficult to recruit specialists.

Global market commodity prices have risen and this, combined with increasing demand from abroad, is making the manufacturing industry in particular believe that it is possible to raise their sales prices in the coming period. However, competition in the retail trade is still very stiff. It is therefore more difficult to raise sales prices and many retailers are being put under pressure by low profit margins.

“Surprisingly strong in Europe – I hadn't expected that!”

Companies in Sweden are increasingly satisfied with the financial situation, see Figure 1. In September, there was some concern regarding future developments and expectations were subdued, despite a promising outlook for production and sales. The recent strengthening in demand on Swedish export markets has surprised several of the manufacturing companies. The export industry is now more positive than before and has clearly strengthened its profitability thanks to increased production and a relatively weak Swedish krona, see Figure 2. Rising commodity prices have also contributed to a general increase in demand in several commodity-exporting economies. Furthermore, manufacturing and construction activity in several countries in Europe has improved, and the United Kingdom is also showing continued good demand, despite uncertainty resulting from the coming negotiations on withdrawal from the EU. At the same time, demand in China is continuing to increase steadily and companies appear increasingly less concerned over economic activity in Asia.

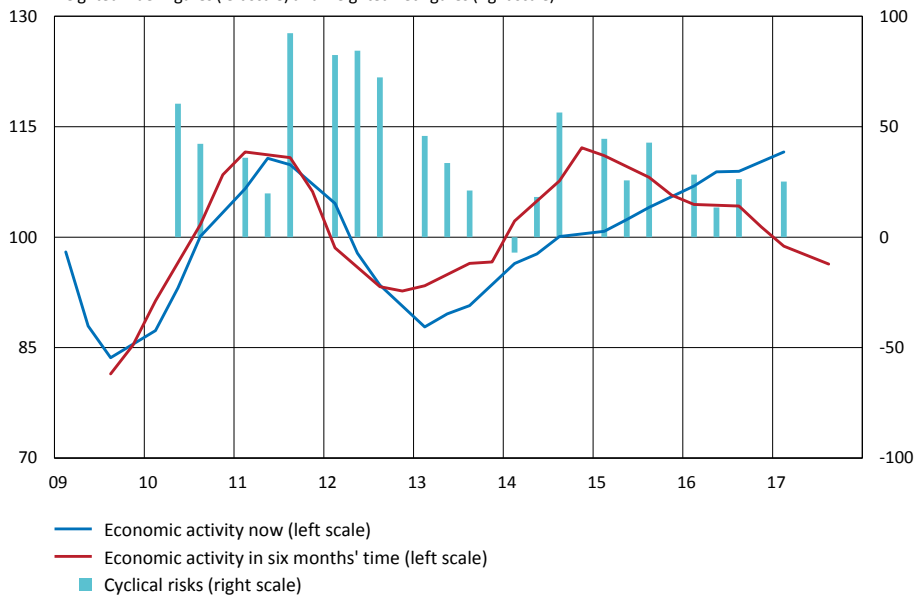
¹ Three times a year, the Riksbank interviews the largest companies in the construction, retail, manufacturing and part of the service sectors. Representatives of 29 companies with a total of 230,000 employees in Sweden were interviewed this time.

Uncertain global political developments

Several companies express some concern regarding international political developments, for instance, the uncertainty of the outcomes in the coming parliamentary elections in several European countries and the new political administration in the United States. However, the respondents are on the whole positive with regard to developments in the near term and the concerns have not caused them to change their plans for the future, with a couple of exceptions. In a longer-term perspective, however, the manufacturing companies see risks that new trade restrictions will be introduced, which could in the long run affect production, employment and investment in Sweden.

The retail trade does not see any risks that consumers' purchasing power will deteriorate, but they are concerned over the increased competition and the changes in consumer behaviour caused by e-commerce. Expressions such as the following are significant: "There is demand out there, the challenge is how the participants in the retail trade will act and how purchasing behaviour will change." Construction companies see few risks that economic activity will deteriorate going forward and in total the risks have not increased since the previous survey, see Figure 1.

Figure 1. Economic situation and economic risks
Weighted index figures (left scale) and weighted net figures (right scale)



Note. The weighted index figures show a standardised value (mean value = 100 and standard deviation = 10) of the net figures for the companies that say that the economic situation is good or bad and for those who say that the economic situation will improve or deteriorate in six months' time. The series for the economic situation in six months' time has been moved forward two quarters. The lines show the weighted index figures expressed as a moving average based on three observations. The columns show the weighted net figures for those companies that say that the risks are currently greater or smaller than normal. This survey is made three times a year, which means that there are only observations for the first three quarters of each year in the figure.

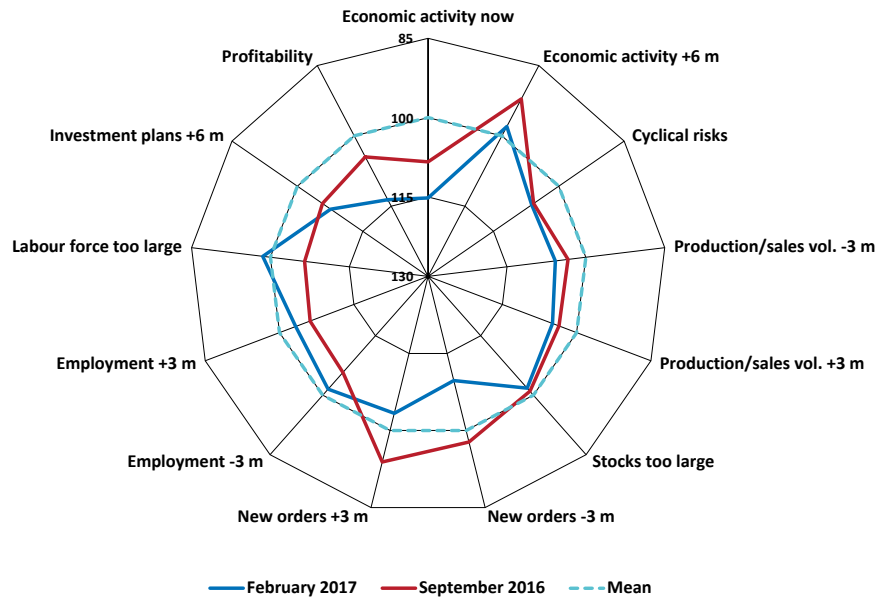
Continued good demand in Sweden

Companies that have Sweden as their primary market see, as before, a good economic situation. The construction sector is still very strong, with a high level of production and well-filled order books for all types of construction and public works. A good description of the construction companies views of economic activity is contained in the quotation: "We are full steam ahead and things can only level off from here."

The retail trade and the companies that sell services directly to households, such as restaurants and travel companies, also perceive a continued strong demand with consumers with good spending power. The retail trade for durables (such as clothing trade) is not satisfied with its profitability, while other retail trade areas and other sectors in general are satisfied. The overall response pattern from companies shows that developments have

strengthened in several areas since September, see Figure 2. The situation is now very good and on the whole stronger than the historical average.

Figure 2. The companies' overall response patterns
Weighted index

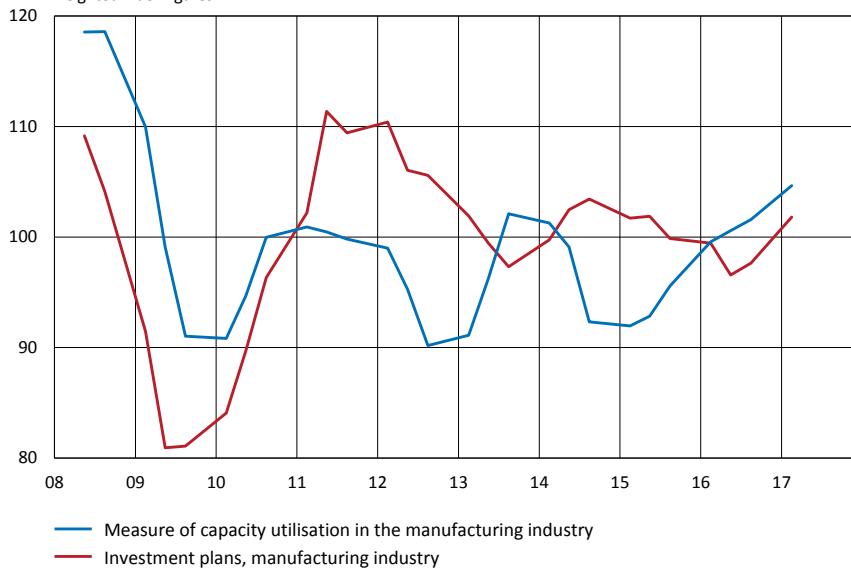


Note. The responses to the questions are plotted along "spokes" in the figure where an index figure closer to the centre is better. The historical average is calculated for the periods when the questions were put and for all sectors. The term -3 m / +3 m refers to the most recent three months and the coming three months respectively. +6 m refers to the coming six months.

Capacity utilisation in the manufacturing industry rising

There has long been spare production capacity in Swedish factories. Following the recent increase in demand, an increasing number of manufacturing companies are saying that it is no longer as easy to manage increases in demand, see Figure 3. Even if there is still spare capacity in the factories, the lead times are now a little longer than before if one needs to increase production further. This applies in particular to the automotive industry, which has experienced a number of bottlenecks in the production flow in connection with increasing the rate of production. Most companies do not yet have any plans to invest in increased production capacity, and in the cases there is a need for it, Sweden is rarely the first alternative. The fact that investment plans are increasing somewhat is mainly linked to maintenance initiatives after a relatively restrained rate of investment in 2016.

Figure 3. Measure of capacity utilisation in the manufacturing industry and its investment plans
Weighted index figures



Note. The weighted index figures show a standardised value (mean value = 100 and standard deviation = 10) of the net figures for the manufacturing companies that say that they at present have major difficulties or have no difficulties in managing an unexpected increase in demand (measure of capacity utilisation in the manufacturing industry) and the net number of manufacturing companies responding that they have increasing or declining investment plans for the coming six months.

Continued staff shortage in the construction sector

The construction sector is still experiencing difficulty in obtaining sufficient personnel. This means that companies are forced to prioritise among tenders and sometimes refrain from making tenders for projects when they lack resources. As one company manager in the construction sector said: "Housing production has been affected by the shortage of labour, we have been forced to say no to several tenders due to lack of resources." On the other hand, despite good demand, companies in the manufacturing industry, retail trade and services sector are not experiencing any general shortage of labour. But as before there are shortages in some specialist professions, such as engineers, IT specialists and some specific professional groups.

The February survey included some in-depth questions on how companies use personnel from staffing agencies. The responses show that the companies use personnel from staffing agencies mainly to obtain specialist competence for certain projects and to have flexibility in connection with changes in demand. For instance, some manufacturing companies have now increased production by primarily taking on personnel from staffing agencies. At the same time, others are cautious about taking on too many people from staffing agencies as they say this can undermine competence levels in the company. The discussions regarding personnel from staffing agencies also indicate that it may be difficult to draw a clear distinguishing line between these staff and the use of sub-contractors for various tasks. Often, consultants work very closely with the companies and can vary between being employed, hired through staffing agencies or sub-contractors, often in the same project.

Wages and wage drift expected to increase somewhat

During March and April many of the collective wage agreements in the labour market will expire. More companies than before now believe that wage costs and wage drift, that is, wage increases over and above those stated in the collective wage agreements, will be higher during the coming year in relation to the previous year. However, in discussions with the companies it becomes clear that the actual wage increases are only expected to increase by a few tenths in relation to the earlier period. Wage drift is expected to increase in the manufacturing industry, but particularly in the construction sector, where one company

manager was quoted as saying: "We already have a significant wage drift." At the same time, companies are working actively on making their operations more efficient and thereby keeping down total wage costs.

Rising commodity prices affect the manufacturing industry with some time lag

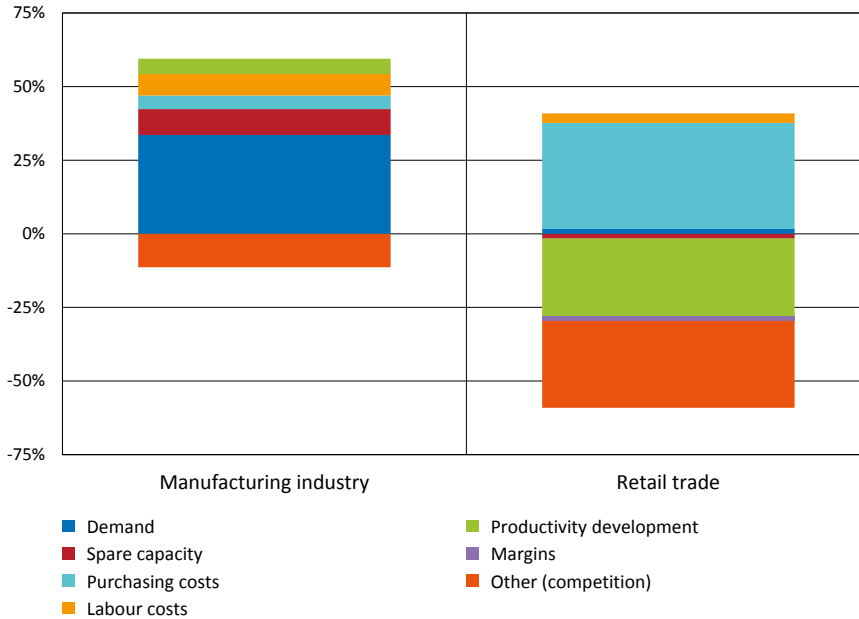
Global market commodity prices have risen during 2016. Most manufacturing companies have not yet been affected by the cost increases, but the impact is expected to come later in 2017. The speed at which changes in commodity prices affect purchasing prices varies, but is often regulated in agreements and thus does not always have an immediate effect. The impact usually comes after some quarters when regulations regarding commodity price changes in agreements have an effect or in connection with manufacturing companies completely renegotiating purchasing agreements for input goods. In other sectors, on the other hand, some commodity prices have a direct impact as with higher prices for fruit and vegetables. At the same time, the construction sector is affected by rising purchasing costs, where it is primarily the strong demand that pushes up prices of input goods.

A generally rising price trend in the manufacturing sector

Companies are planning to raise their sales prices in 2017. It is primarily the manufacturing industry that now believes it is possible to have smaller price increases in stages. Pricing in the manufacturing industry is based on guide prices and there is usually some scope for negotiation with the customers before the final sales prices are determined. In recent months, the price outlook has been stable in so far as one has not needed to reduce the guide prices as often as before. This is regarded as an incipient sign of demand, which in turn creates expectations of future price rises.

The reasons for raising sales prices differ between in particular the retail trade and the manufacturing sector, see Figure 4. There is a rising price trend regarding commodities that is expected to have an effect during the year, at the same time as there is clear demand pressure within the manufacturing industry that enables them to raise sales prices. One business leader expressed this as: "I am quite sure that inflation is about to rise, we see it everywhere." Within the retail trade it is increased purchasing costs, partly due to the relatively weak Swedish krona, that mean they are expecting somewhat higher sales prices in the near future. However, there are several factors that contribute to counteracting price increases in the retail trade. For instance, companies are constantly trying to make their operations more efficient and to keep their costs down. At the same time, competition is still stiff, which makes it difficult for these companies to transfer their increased costs to consumers. One business leader expressed this as: "Our costs are increasing and our incomes are declining, which is tough." It is thus uncertain how much prices can actually be increased.

Figure 4. Factors behind pricing in the twelve months ahead
Weighted net percentages



Note. The columns 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. The column "Other for the retail trade and the manufacturing industry is solely comprised of competition in February. Refers to companies' responses in February 2017.

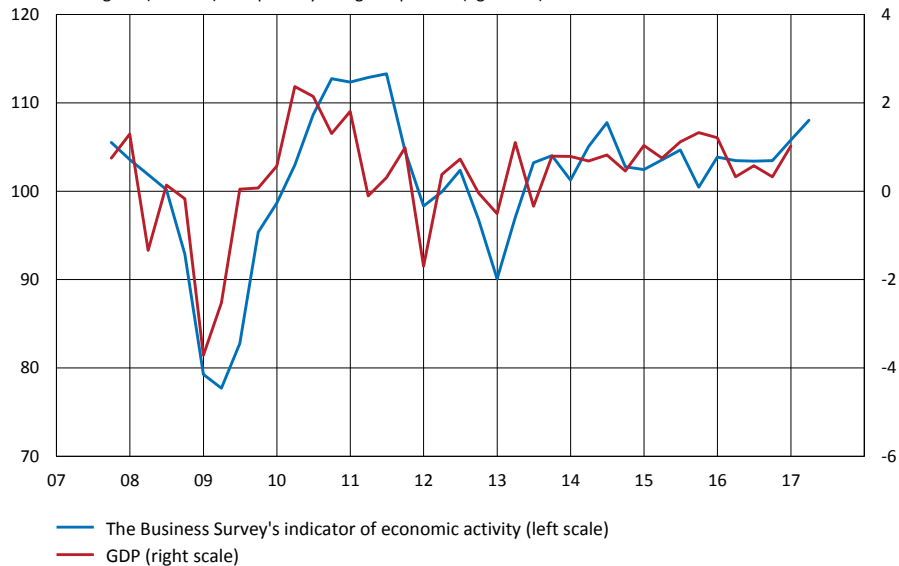
E-commerce - an increasingly important sales channel

Competition is still stiff in the clothing trade and it is increasing apace with developments in e-commerce. E-commerce enables participants to sell to Swedish consumers without having shops in Sweden. Moreover, producers of goods can skip the retail channel and sell directly to customers. There is also increased focus in the consumer goods trade on developing e-commerce as a channel, one indication is the following quotation: "E-commerce will be the biggest change for the consumer goods trade since the dawn of the supermarket." To meet consumers' changing purchasing patterns and increased price awareness, which follow on from developments in e-commerce, retail trade companies are continuing to invest in various technological solutions that give customers several choices when making purchases. These include, for instance, that the customer can order an item online, but pick it up or return it in a physical shop, or vice versa. One striking quote is: "It is e-commerce that is driving the need to invest in physical shops, too."

The indicator of economic activity points to good growth

In the February survey companies express optimism regarding economic developments and all in all, the Business Survey's economic indicator points to a further improvement in economic activity, see Figure 5.

Figure 5. The Business Survey's indicator of economic activity
Index figures (left scale) and quarterly changes in per cent (right scale)



Note. The Business Survey's indicator of economic activity is calculated as a weighted average of the responses to various questions in the survey. The responses are then weighed together on the basis of their ability to predict seasonally adjusted GDP changes from quarter to quarter. The indicator is calculated up to two months before the outcome for GDP is published and provides an early indication of developments in economic activity. The indicator has been standardised so that the mean value = 100 and the standard deviation = 10. This means that a value above (below) 100 should be interpreted as a somewhat stronger (weaker) business cycle than the average. Figures for quarterly GDP growth are seasonally adjusted.

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 retail sectors and in 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.

The survey is conducted by personnel from the Riksbank who visit the companies for approximately one hour. 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.

Around 40 companies are normally interviewed in May and November, and around 30 companies in February. Over 300 companies have taken part in the survey since it was started in 2007.

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. The February 2017 report presents the results of interviews with 29 companies, which were mainly held between 16 February and 1 March.

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://www.riksbank.se/Documents/Rapporter/POV/2012/rap_pov_artikel_3_121017_eng.pdf



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