



The Riksbank's Business Survey

Economic upswing gradually slowing down
but trade conflicts are a source of concern

May 2019

The Riksbank's business survey in May 2019¹

The major Swedish companies consider that the economic situation remains good but their view of it has become slightly less favourable since the previous survey in February. Like previously, they expect weakened economic activity in the period ahead. They consider the risks to be greater than before and are concerned, above all, that the ongoing trade conflicts will have consequences for economic activity in the world. The view of economic developments is otherwise somewhat divided, not least in the manufacturing sector: some export companies have received fewer orders and are experiencing weaker demand in parts of Europe and Asia, while others say that demand is still good in these regions. Demand from the United States continues to be experienced as good.

While unease has increased in the manufacturing sector, the situation is more stable in the construction sector and trade. It is true that demand for housing construction has been decreasing for some time but, overall, the situation is considered to be stable. Construction companies are in the middle of a process in which they are shifting from housing construction in Stockholm to segments and regions with better demand. In the trade sector, demand continues to be good in the low-price sector.

The relatively weak exchange rate is generally increasing export companies' profits, but several export companies repeatedly point out that a stable and predictable currency facilitates their long-term planning. At the same time, the weak krona is exerting pressure on import companies' margins in cases where they cannot raise their prices, but several trading companies say that the net effect of the interest rate policy and the weak krona is nonetheless positive for them. The positive effects of a long economic upswing, households with good spending power and stable and good sales offset the negative effects of a weak currency and increased purchasing costs.

Higher costs and continued good demand mean that the percentage of consumer-related companies planning to raise their prices within a year is continuing to increase. More detailed questions on how companies decide their sales prices show that strong competition is leading companies, particularly consumer-related ones, to be cautious about adjusting their prices. Moreover, when companies see that costs are rising, they nevertheless generally choose to raise their prices.

Sentiment among major companies is less positive

In the survey conducted in May, the major Swedish companies generally have a slightly less optimistic view of the present economic situation than they had in the survey from February,

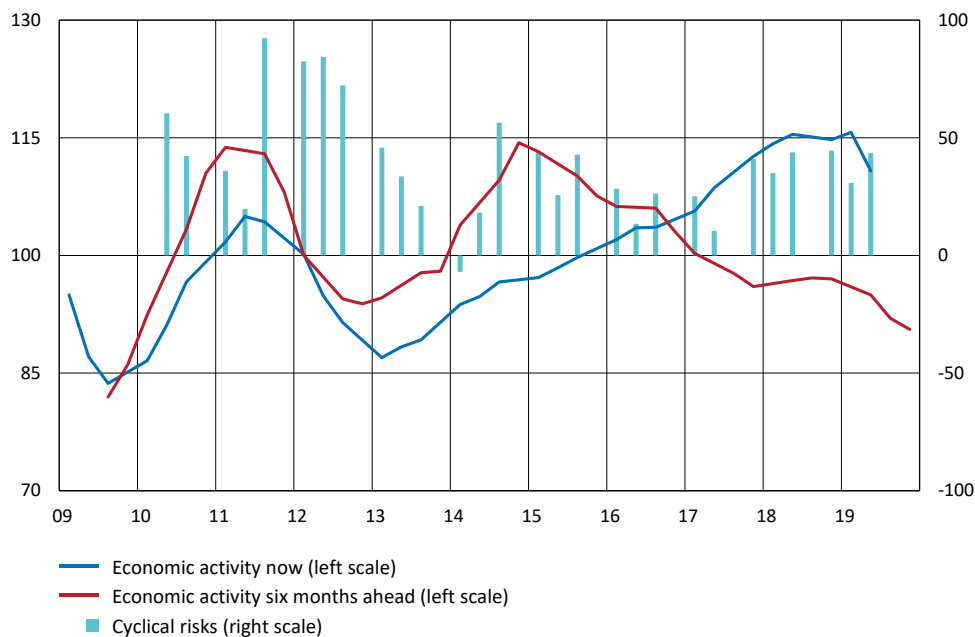
¹ Three times a year, the Riksbank interviews the largest companies in the construction, trade and industrial sectors as well as parts of the service sector. Representatives of 39 companies with approximately 265,000 employees in Sweden were interviewed during the period 26 April to 24 May.

see Figure 1. Like earlier, they expect the economic situation to be weaker in six months' time.

However, the view of the economic situation is divided on sector and branch levels. Export companies point to a slow weakening of international demand in most markets. There is also concern that specific events, such as geopolitical crises, will speed up and exacerbate a downturn. In the construction sector, it is the weaker demand on the housing market that is impairing the economic situation. The economic situation is also experienced as less favourable in the services sector, which may partly be due to lower demand from manufacturing companies. On the other hand, in the trade sector, the economic situation is perceived as slightly better in comparison with the survey in February.

Figure 1. Economic situation and economic risks

Weighted index (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 companies that say that the economic situation is currently good or bad and those who say that the economic situation will improve or deteriorate in six months' time. The red line, the economic situation in six months' time, has been moved forward two quarters. The lines show the weighted index figures expressed as a three-month moving average, based on three observations. The bars show the weighted net figures for those companies that say that the risks to economic development are currently greater or smaller than normal. The survey is performed three times a year, which means that there are only observations for three quarters of each year in the figure. As of 2017, there are observations for the two first quarters and for the final quarter of every year in the figure.

The view of international demand also varies on both the sector and branch levels. Some export companies report continued strong demand from the United States ("In the United States, it's going very, very well"), while others say that the country is undergoing a gradual slowdown from a high level. The view of Europe is also divided: "Europe looks good", "Above all, it is demand in Europe that has slowed down" and "Europe is the uncertainty factor in the period ahead, but it's not visible in the figures yet". Assessments of the development of demand in various European countries also differ. Demand from Germany, France and Italy is assessed to be developing weakly, while it continues to be strong from the United Kingdom, which could partly be a currency effect but could also be due to Brexit uncertainty leading to stocks being built up in the United Kingdom. There is also talk of an east/west dimension in demand in Europe, in which demand is increasing more rapidly in the eastern part of Europe than in the western part.

The view of Asia, and China in particular, is also mixed. Several respondents point to a downturn in Asia, which is largely driven by China, but demand in Japan is also experienced as being a little weaker than before. Demand in China has been supported by fiscal policy stimulation measures and infrastructure investments, which have directly or indirectly

affected some of the Swedish companies' activities positively and these therefore have a more optimistic view of developments in the country.

“Relations between the United States and China are vital for economic activity in the world”

The economic risks have been on approximately the same level in recent years but are now considered to have increased slightly since the survey in February, see Figure 1. One common response is that a risk is perceived of the trade conflict between the United States and China escalating. As one respondent puts it: “Relations between the United States and China are vital for economic activity in the world”. Both export companies and transportation and harbour companies also mention the risk of a hard Brexit.

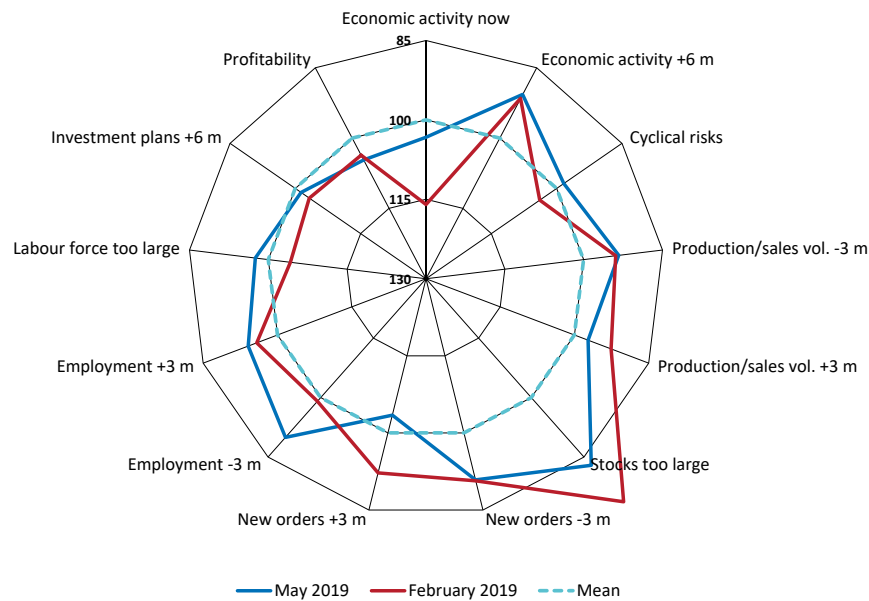
Apart from risks of a geopolitical nature, there are risks associated with economic developments. How will the economy, domestic and international, develop when the prolonged economic upswing ends? In the event of a (sudden and powerful) deteriorated economic situation, economic imbalances will arise and companies' unease about this is partly captured by the quotations: “Economic activity is chugging along, but the way it's constructed doesn't feel particularly satisfying” and “The fact that it is low-price actors who are doing well in an economic upswing should give pause for thought.” Respondents in the trade sector take up risk factors such as a substantial interest rate rise and a further weakening of the krona.

There is also increased caution in the planning for new investments and recruitments, which may have been caused by the risk developments. It is also reported that subcontractors are unwilling to invest to increase capacity. In addition, all companies are cautious about offering new permanent positions, as they may have to be able to reduce staffing rapidly in the event of a slowdown. Similarly, they may be more restrictive about employing new staff for support functions such as HR, accounts and purchasing.

Overall, the response pattern indicates that the present economic situation is still considered better than normal but that it is not on the same level that it was at the start of the year, see Figure 2. Companies continue to believe that economic activity will slow down six months ahead, while economic risks overall are considered to have increased slightly since the survey in February.

Figure 2. 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 from the date 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. +6m refers to the coming six months.

“At present things are fairly good, not great”

Companies in **the manufacturing sector** in general perceive the current economic situation to be still good or at least satisfactory. The optimism regarding the current economic situation has declined since the February survey, but it is still considered to be somewhat better than normal. At the same time, one should bear in mind that last year was an unusually good financial year for many companies, with high or record-high sales and good profitability. The quotation “The economic situation is satisfactory – we are falling from high levels but fairly slowly” describes sentiment in the manufacturing industry pretty well. However, there is a greater spread in the responses now, which is evident in the quotations going from “Right now it is really great actually” to “It is not so good now”.

Export companies are reporting unchanged or reduced output to a greater extent than before, which could be due to demand from abroad having declined, but also to the fact that they are trying to reduce their stocks, for instance by periodic stoppages. However, some companies still feel they have too large stocks, which is illustrated by the quotation “The stocks are as large as our storage space allows for – we haven't seen anything like this for ten years”. It is mainly in the forestry industry that they are concerned about the build-up of stocks. Overall, however, this type of build-up of stocks is not regarded as a major problem and the companies consider that there are good reasons for them. For instance, they have wanted to maintain a good level of service towards their customers and some companies have also experienced transport difficulties due to the weather during the winter and early spring.

Export companies' possibilities to manage a rapid increase in demand have, on the whole, improved since the survey in February. This is the first time since 2014 that this measure of capacity utilisation has fallen, but it is nevertheless still at a relatively high level. Some companies are reporting that their production plants are operating at full capacity, but that they have nevertheless decided not to extend their capacity as they consider this too costly and risky.

“The luxury apartment market is dead”

Construction activity remains good, but it is not at the same level as last year, which appears to have been a peak year for the **construction industry**. It is primarily the weak demand on the housing market that has dampened economic activity, but this is more a question of stabilisation, which is evident in the quotation “The level of housing construction this year is more normal. A bit like 2017”. The large construction companies also have a broad range of activities and can change direction when one segment is not doing so well. In particular, public sector construction is mentioned as an area of activity that is strong and compensating for part of the decline in housing construction. Infrastructure/civil engineering works and commercial property construction are, at the same time, showing stable development. The quotation “All in all, we think it’s going quite well, although the housing market is very challenging, of course” summarises the situation fairly well. With regard to housing construction, focus has shifted from tenant-owned apartments to rented apartments, as there has been a change in demand.

The large construction companies describe construction activity overall as stable, but at the same time they point out that things look different in different parts of the country and for different companies, where for instance smaller housing developers are experiencing harder times. “In general we are seeing a stabilisation of the market. However, there are geographical differences”. One company considers that construction activity is satisfactory in the rest of the country but that in Stockholm it can be characterised as poor. Another notes that demand is now much lower in Stockholm, while it is strong in Gothenburg. There, they have a lot to do and, in the rest of the country, demand is stable. With regard to construction activity, one company notes, “even if things were to come to a halt today, we have projects planned up to the end of 2021 so we will be busy for at least a couple of years to come”.

Property companies, on the other hand, see no clear slowdown in activity, which is indicated in the quotation: “There is a lot of talk about economic activity slowing down, but we aren’t really seeing this in our business” and “We hear in the media and read in the newspaper about a slightly more negative segment, but we aren’t seeing any change in the market”. The property companies see that many companies are expanding and thereby demand for offices, businesses and other commercial premises remains strong and “rents are still on the way up”. On the other hand, they state that “The luxury apartment market is dead”.

Low interest rates and households with good spending power benefit non-durable goods trade

In the **retail trade**, they are overall satisfied with the prevailing financial situation, which is perceived as better than normal. Companies are reporting increased sales and better profitability over the past three months. In general, they expect the economic situation to be weaker in six months’ time. However, they are more optimistic now than they were in February and now believe the deterioration will be smaller, so that the economic situation will be largely the same in six months’ time. The branch is marked by continued stiff competition, not least from e-commerce participants: “In these times of e-commerce, it is difficult for retail companies to attain growth”. The stiff competition also contributes to companies constantly having to adapt their operations to the customers’ needs. A company’s sensitivity to customers’ needs is summed up by the quotation: “Customer behaviour is changing. Their tolerance of friction is declining. Everything has to go smoothly now”. Several companies have an explicit low-price philosophy and their operations are assessed to be relatively independent of the economic situation. They are not so worried about economic developments and some believe that an economic slowdown could increase their sales: “An economic slowdown might actually be a positive thing for us”.

Those active in the **non-durable goods segment** are, on the whole, satisfied with the economic situation and they also expect it to remain good in six months’ time. Their view of

economic activity is reflected in the quotation “We see no major changes in economic activity in relation to 2018, if anything it has improved”. The low interest rates and households with good spending power are mentioned as contributing factors to the good economic activity. At the same time, there is a stream of customers from the non-durable goods segment to restaurants, which has a negative effect on sales. The risks to economic activity are on the whole toned down by the participants in the non-durable goods segment. In the event of an economic downturn, households are primarily expected to cut back on other purchases than non-durable goods.

Staffing companies: “Somewhere between satisfactory and poor”

Staffing companies assess that economic activity is, at present, “somewhere between satisfactory and poor”. Their economic activity peaked last year and is now declining. The economic situation for the **travel industry**, with the exception of the Swedish **hotel industry**, is perceived to be poor and is expected to remain so. Declining demand, poor profitability and cost savings, such as staff cutbacks, characterise this industry. In addition to economic activity, demand for air travel is also affected by the weaker krona and increased environmental awareness.

The **transport industry**, on the other hand, is more positive with regard to both the prevailing situation and developments in economic activity. For instance, one company with freight operations noted: “The volumes are still good and our statistics show no sign at all of a slowdown”. The increased e-commerce is affecting the industry positively.

No general shortage of labour but more difficult to find experienced staff

Companies’ shortages of specialists are now tangible and increasing from an already high level. As before, it is a question of professional categories such as IT staff, engineers, economists and project managers. On the other hand, there is no general shortage of labour and most companies consider it relatively easy to get hold of staff.

However, there are signs that it is increasingly difficult to get hold of experienced and trained staff. Several quotations illustrate this: “There is a general shortage of employable labour. As a shop assistant, one doesn't just need to be able to speak Swedish, one also needs knowledge of computers and IT today”, “There is a general shortage of experienced staff” and “There is stiff competition for the skilled workers in all areas”. With the exception of the retail trade, several companies report that they are planning to reduce their staff, as part of a cost-cutting programme.

Despite statements such as “We exercise tough discipline in ensuring that wage adjustments take place in connection with the annual rounds”, a larger percentage of the companies than usual are expecting wage drift to increase during the coming year. In the retail trade and services sectors, the responses indicate that wage costs are expected to increase more than before.

The Swedish krona: “The level is one thing, but the rapid change is difficult because the systems don't have time to adapt”

For the export **industry**, the weak krona contributes to improved competitiveness. However, several companies point out that competition today is so tough that the weaker krona does not affect their work on making operations more effective, this is continuing as usual. Refraining from doing this would mean losing competitiveness and could be devastating in the long run. During periods when the krona is weak, it may instead be the case that they try to be extra vigilant that productivity work is really continuing. However, some companies

admit that, during periods when the krona is weak, they may have a more forgiving attitude to cost discipline, which could ultimately show in productivity figures.

Commodity-producing companies, whose prices are set on an international market, have attained a good or “fantastic” cash flow and improved profits as a result of the krona depreciation. For companies that produce goods containing a large share of components from foreign subcontractors, on the other hand, the weak krona may mean poorer net margins and profits. Few companies have strong views on the krona exchange rate, but comments such as “It feels as though the krona is weaker than it should be” and “Our concern is that the Swedish krona is so extremely weak that the margins in the Swedish part of our business activities are becoming much weaker” arise. Export companies are more focused on the problems that can arise as a result of the krona being unstable and volatile: “The level is one thing, but the rapid changes are difficult as systems don't have time to adapt” and “The krona rate over the past year has been rather a challenge for us”. However, some export companies are relatively unconcerned over the krona exchange rate, which is captured in the quotation: “The krona depreciation hasn't really affected our planning, but it has had a positive effect on our results”.

Companies in the **construction sector** are not generally affected very much by exchange rate developments, but one construction company states: “We haven't changed our purchasing behaviour as a result of the weak krona. Foreign purchases are much cheaper than Swedish ones anyway”.

In the **retail trade**, some companies mention the weak krona as a problem: “One of the major problems is the currency”, “The weak krona has not benefited us” and “The exchange rate is a little painful right now”. At the same time, several companies say that the net effect of the interest rate policy and the weak krona is actually positive for them. The positive effects of a long economic upswing, households with good spending power and stable and good sales offset the negative effects of a weak currency and increased purchasing costs. As in the manufacturing industry, the retail trade companies can hedge against a particular krona rate at different time horizons, but most companies do not do so as they feel that the losses and gains from exchange rate fluctuations even out in the long run. Some retail trade companies also note that the weaker krona has contributed to a larger number of foreign tourists in their department stores and shops.

In the **services sector**, the effects of the exchange rate on their operations vary from one sub-section to another. Some of them, such as staffing, transport and harbour companies, are not directly affected by the exchange rate, but can be affected indirectly by demand from customer companies. Others, such as the travel and air industries, are directly affected by exchange rate fluctuations. They often have their income in Swedish krona but their expenditure in euros and US dollars. Companies in the hotel industry point out that the competition on the market for overnight stays has a greater impact on their pricing than the exchange rate.

“We will continue raising our prices, unless there is a drastic appreciation of the krona”

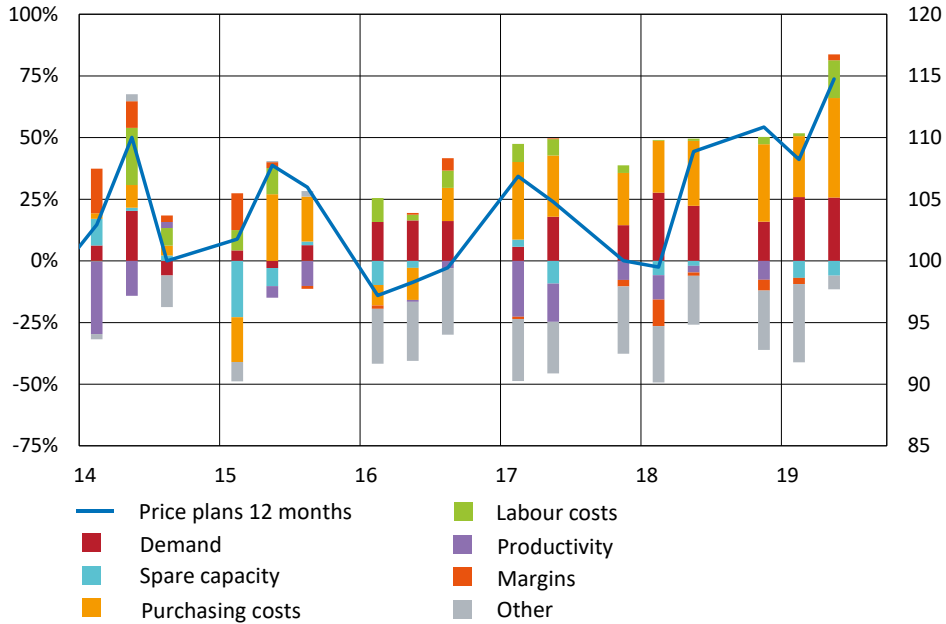
The percentage of consumer-related companies planning to raise their prices during the coming year is continuing to increase. The plans for price increases are, as before, driven by high demand and high purchasing costs, but now higher labour costs are also mentioned as a reason, see Figure 3. There are slightly different views as to whether the companies will succeed in implementing their plans, which is illustrated by the quotation: “You are really scared to raise prices, but it feels as though there are other things much more important than the price. We believe people have the money” and “There is a tendency towards discounts now. It is the increased price transparency via technological advances that is driving this”. Companies may have difficulty in implementing price increases in that technological advances not only increase competition between physical shops in Sweden, but also the competition from foreign e-commerce. As one company states: “We will try to raise our prices. If we

notice that agents who do not need to buy in SEK aren't raising their prices, we won't be able to raise ours either. We Swedish agents are too small to have an influence”.

Developments among manufacturing, construction and some service companies (that is, other companies) look rather different. These companies once again see fewer hopes of being able to raise prices. They look ahead to a decline in demand and more spare capacity that can hold back price increases, even though they also expect higher labour costs.

Figure 3. Driving forces behind pricing in consumer-related companies in the coming twelve months

Weighted net percentages and weighted index figures



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. The “Other” bar otherwise consists mainly of competition. The weighted 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 coming twelve months.

ARTICLE – Why don't prices change more?

Understanding the driving forces behind companies' pricing is important when monetary policy is being formed. We therefore asked more detailed questions on companies' pricing in the survey in May. A majority of companies decide their sales prices themselves. In the trade sector, it is relatively common for prices to change every day, while, in the manufacturing sector, prices are changed on more of an annual basis. It is common, particularly in consumer-related companies, to be cautious about adjusting prices, as competitors may not follow suit. It is also common for companies to raise their prices when they see costs increasing. The results of this study are thereby in line with the results of previous studies of companies' pricing behaviour.

A majority of companies decide their sales prices themselves

One recurrent question in the Riksbank's business survey concerns the factors that companies expect to drive sales prices over the coming year. This time, we have asked them to answer further questions and decide which statements best describe how they determine their sales prices.²

To the introductory question about which customer group provides most revenues, just over half of the companies respond that it is other companies. For 2/5 of the companies, revenues come mainly from households, while a couple of companies state that the public sector gives the highest revenues at the moment.

To the question of who decides sales prices, the great majority of companies respond that they do this themselves. However, a few of them say that their prices are determined internationally via world market prices for commodities, for example. No company considers that its prices are determined completely by regulations or by a public authority.

How often do companies adjust their prices?

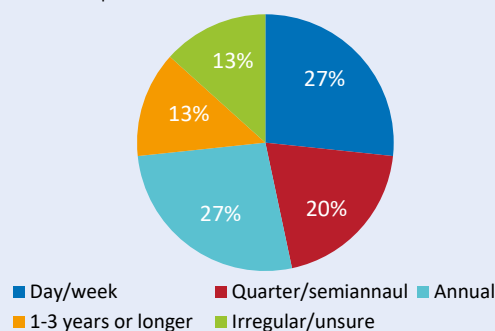
Another question concerns how often companies adjust their sales prices. Figure 4 illustrates the responses. Just over one-quarter of companies adjust their sales prices every day, or at least once a week. Those doing so are often active in the trade sector and the service sector. A similarly large proportion of companies adjust their prices once per year. These are companies in the manufacturing sector or service sector that sell to other companies.

² These extra price questions have been developed within a network of central banks that regularly carry out business surveys.

Among the one-fifth of companies adjusting their prices once a quarter or every six months are companies in the manufacturing sector and trade sector. Among those that seldom adjust their prices (which is to say less than once every three years) are property and harbour companies.

Figure 4. How often do you adjust the sales price of the good or service responsible for the largest share of your revenues?

Proportion of companies. Per cent.



Note. The question asked of the companies is identical to the figure heading.

What are the companies' most common price strategies?

It is common for companies to raise prices when they see that costs are increasing, see Figure 5.³ About 3/5 of companies do this, regardless of whether they make sales mainly to households or to other companies. One kind of behaviour that is less common, but about equally common among consumer-related companies and among companies that sell to other companies, is to adjust factors other than prices, such as guarantees, delivery times and other customer services. About 1/5 of companies report that they prefer this approach.

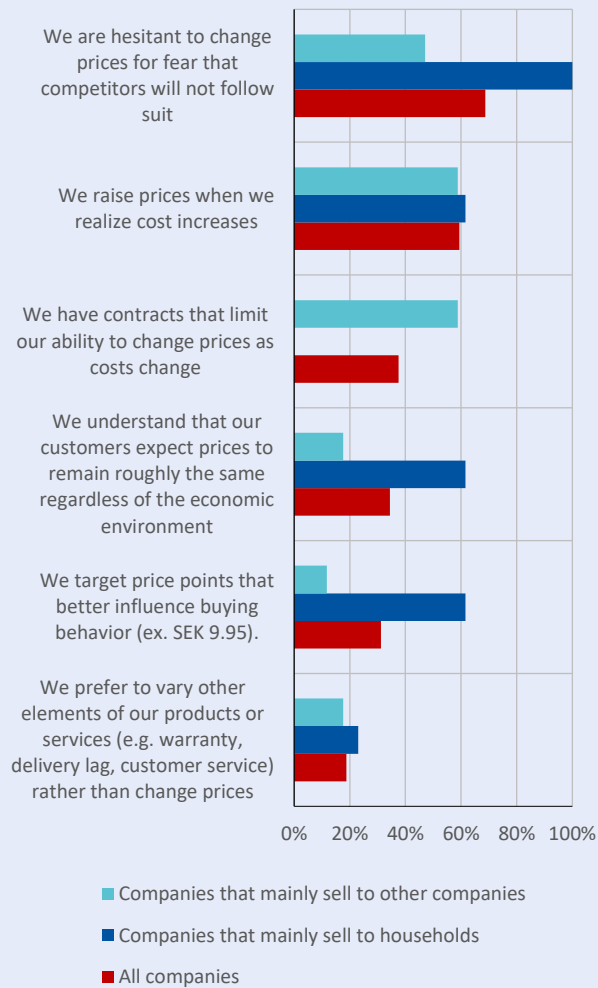
A number of circumstances also cause pricing behaviour among different types of company to differ.

³ Figure 5 shows the percentage of companies choosing each response alternative. If the companies are weighted by number of employees, the ranking of the response alternatives is largely the same, even if the percentages vary a little.

About 2/3 of companies state that they are cautious about adjusting their prices, as their competitors may not follow suit. However, this caution is significantly more common among consumer-related companies than among companies selling to other companies. All consumer-related companies in the survey state that competition reasons make them cautious about adjusting their prices, while just under half of the companies selling to other companies make such considerations.

Figure 5. Statements that companies think best describe their pricing behaviour.

Proportion of companies choosing each response alternative. Per cent.



Note. The question was: Which of the following statements corresponds best with how you decide your sales prices (choose one or more alternatives)? In total, 32 companies answered the question, of which two companies stated that the public sector was responsible for the greatest share of their revenues.

For companies selling to other companies, it may instead be the formulation of the contract that restricts possibilities for adjusting prices when costs change. This circumstance is mentioned by 3/5 of these companies. For consumer-related companies, it is instead a form of implicit contract that may be making prices sluggish. About the same percentage of consumer-related companies report that they take into account that their customers expect approximately the same prices, regardless of economic situation.

To a relatively great extent, consumer-related companies also choose price levels that increase sales or, to put it another way, improve customers' purchase behaviour. One example of this is avoiding passing threshold values, which is to say setting the price at SEK 9.95 instead of SEK 10.00. Of the consumer-related companies, 3/5 follow such a strategy, while it is significantly less common among companies selling to other companies.

In addition to the response alternatives discussed above, the companies were asked to respond to four further statements, but these were not chosen to any great extent and are therefore not included in Figure 5.⁴

It is important for central banks to understand the forces that drive pricing

The results of this survey resemble fairly closely the results of other, significantly more comprehensive surveys carried out in Sweden and internationally, even if these are a few years old.⁵ For example, companies being cautious about adjusting their prices due to concern that competitors will not follow suit has been described as a coordination problem that could lead to prices becoming sluggish.

Understanding the driving forces behind companies' pricing is important when monetary policy is being formed. For example, the analytical models usually used by central banks are based on the assumption that some prices are sluggish. This fact allows central banks, at least in the short term, to affect the real economy. An increased understanding of what makes some prices sluggish can improve the monetary policy analysis of how changes in nominal interest rates lead to changed real interest rates, which in turn affect the real economy and, ultimately, the rate of inflation.⁶

⁴ These statements were: "It is costly for us to raise prices", "Bureaucracy/delays within the organisation slow down pricing decisions", "Our variable unit costs do not change substantially when we increase production and we are trying to maintain a normal profit margin" and "We do not reduce prices because our customers may take this as a reduction in the quality of our goods and services".

⁵ See, for example, Apel, Friberg and Hallsten (2001), "Micro Foundations of Macroeconomic Price Adjustment: Survey Evidence from Swedish Firms", *Working*

Paper 128, Sveriges Riksbank, and Fabiani et al. (2005), "The Pricing Behaviour of Firms in the Euro Area. New Survey Evidence", *Working Paper 535*, ECB.

⁶ See, for example, Klenow and Malin (2010), "Microeconomic Evidence on Price-setting", in *Handbook of Monetary Economics* vol. 3, for a review of microeconomic studies of companies' pricing and implications for macro models.

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 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.

Approximately 30 companies are interviewed in the survey in February and about 45 companies in May and November. 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 indices in the figures capture upturns and downturns in the pattern of responses well. These responses are then combined with the companies' reflections during the interviews. The May 2019 report presents the results of interviews with 39 companies, which were mainly held between 26 April and 24 May.

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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