



Business Outlook Survey

Conducted by the Bank's Regional Offices

Results of the Winter 2010–11 Survey

Vol. 7.4 10 January 2011

Overview

- Overall, businesses continue to be positive about the outlook for the next 12 months. While survey responses generally still indicate modest growth, with many firms citing headwinds from strong competition and moderate demand, the strength in commodity prices has led to increased optimism among those firms tied to commodity-related activity.
- The balances of opinion on investment and employment continue to be high, supported in part by firms' efforts to become more competitive and to create new growth opportunities, or by their expectations that demand will continue to improve over the next 12 months.
- Capacity pressures are little changed for the second consecutive survey. Firms expect input and output prices to increase at a greater rate over the next 12 months, but still anticipate that the magnitude of increases in output prices will be contained by competitive forces. Inflation expectations are well anchored within the Bank's inflation-control range.
- On balance, firms reported an easing in credit conditions.

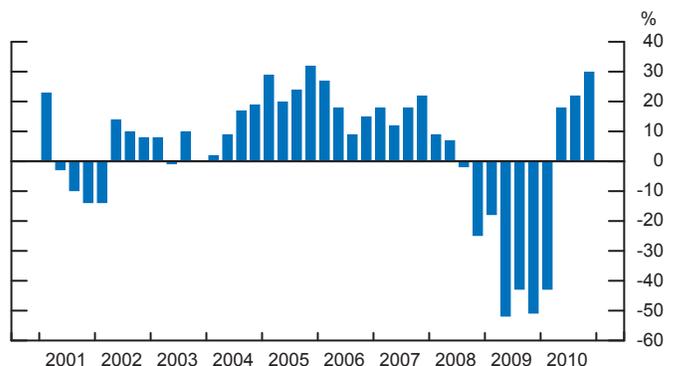
Business Activity

As the recovery advances, firms continue to report higher sales growth over the past 12 months than over the previous 12 months (**Chart 1**). On balance, businesses expect sales to increase at a greater rate over the next 12 months (**Chart 2**), driven by firms in the services sector. While pursuing strategies

Chart 1: Firms report a pickup in sales growth over the past year . . .

Balance of opinion*

Over the past 12 months, did your firm's sales volume increase at a greater, lesser or the same rate as over the previous 12 months?



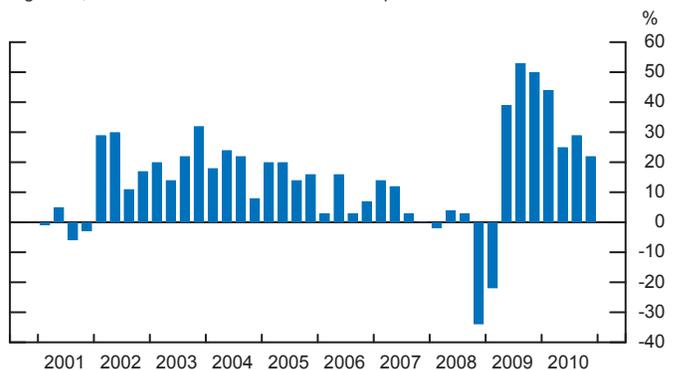
Greater: 56% Same: 18% Lesser: 26%

* Percentage of firms reporting faster growth minus percentage reporting slower growth

Chart 2: . . . and they expect sales volumes to rise at a greater rate over the next 12 months

Balance of opinion*

Over the next 12 months, is your firm's sales volume expected to increase at a greater, lesser or the same rate as over the past 12 months?



Greater: 51% Same: 20% Lesser: 29%

* Percentage of firms expecting faster growth minus percentage expecting slower growth

The Business Outlook Survey summarizes interviews conducted by the Bank's regional offices with the senior management of about 100 firms selected in accordance with the composition of Canada's gross domestic product. The survey's purpose is to gather the perspectives of these businesses on topics of interest to the Bank of Canada (such as demand and capacity pressures) and their forward-looking views on economic activity. Additional information on the survey and its content is available on the Bank of Canada's website at <www.bankofcanada.ca/en/bos/index.html>. The winter 2010–11 survey was conducted from 15 November to 10 December 2010. The balance of opinion can vary between +100 and -100. Percentages may not add to 100 because of rounding.

The opinions expressed are those of the respondents and do not necessarily reflect the views or policies of the Bank of Canada. The method of sample selection ensures a good cross-section of opinion. Nevertheless, the statistical reliability of the survey is limited, given the small sample size.

to position themselves for growth, many firms continue to indicate that their expectations for sales growth are modest, citing such factors as strong domestic and foreign competition and moderate demand. Sales expectations are generally more robust among those involved in, or benefiting from, commodity-related activity—particularly in oil and mining.

While moderating somewhat from its record-high level in the autumn survey, the balance of opinion on investment in machinery and equipment remains elevated and continues to point to an increase in investment over the next 12 months (**Chart 3**). Efforts to improve competitiveness by raising productivity or by expanding into new areas, or intentions to expand output in line with strengthening demand, feature prominently among the factors driving firms' investment intentions.

Following a decline in the autumn survey, the balance of opinion on employment moved back up to the level recorded in the preceding three surveys, and indicates that firms expect to increase employment over the next 12 months (**Chart 4**). This positive sentiment, supporting firms' sales expectations and planned investment for expansion, is widespread across all sectors and all regions.

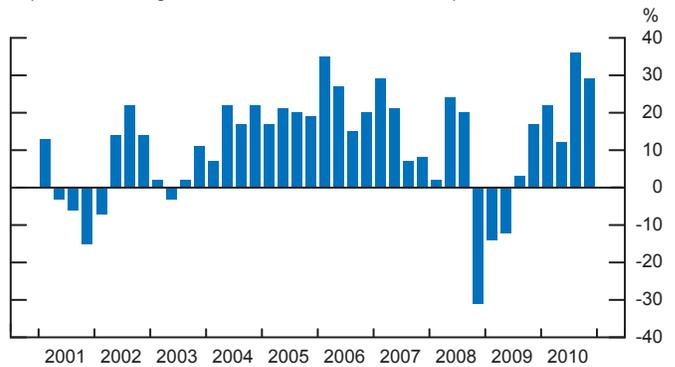
Pressures on Production Capacity

While reports of capacity constraints were somewhat more prevalent among firms in Western Canada, there was little change in the overall percentage of firms reporting that they would have difficulty meeting an unexpected increase in demand (**Chart 5**). This indicator first moved up from its recession lows in the summer 2010 survey and has been essentially stable since then, staying within a range just below the historical average for the survey.

Chart 3: Firms expect to increase investment in machinery and equipment

Balance of opinion*

Over the next 12 months, is your firm's investment spending on M&E expected to be higher, lower or the same as over the past 12 months?



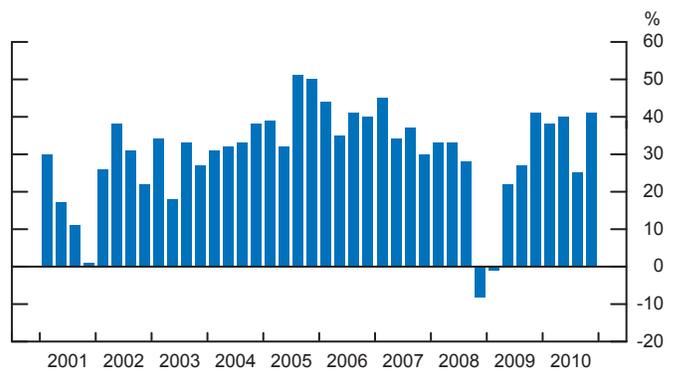
Higher: 44% Same: 41% Lower: 15%

* Percentage of firms expecting greater investment minus the percentage expecting less investment

Chart 4: Firms expect to increase employment

Balance of opinion*

Over the next 12 months, is your firm's level of employment expected to be higher, lower or the same as over the past 12 months?

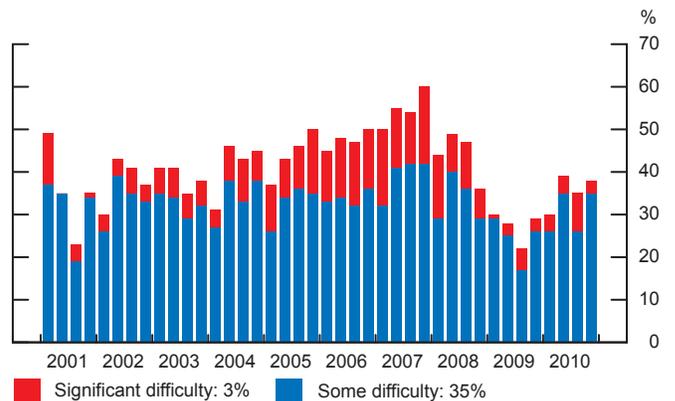


Higher: 49% Same: 43% Lower: 8%

* Percentage of firms expecting higher levels of employment minus the percentage expecting lower levels

Chart 5: Capacity pressures are little changed . . .

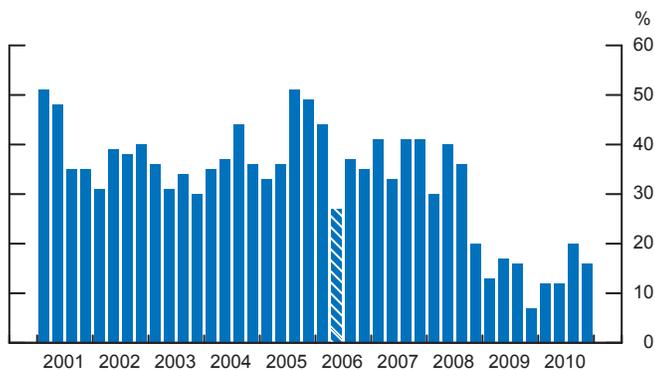
How would you rate the current ability of your firm to meet an unexpected increase in demand?



Significant difficulty: 3% Some difficulty: 35%

Chart 6: . . . and reports of labour shortages remain low

Does your firm face any shortages of labour that restrict your ability to meet demand?



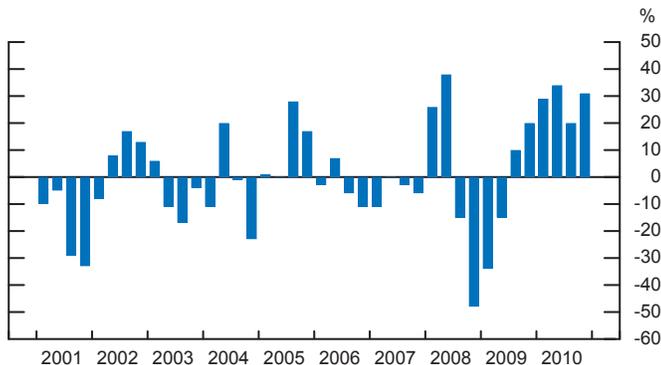
Yes: 16%

The summer 2006 results are not strictly comparable with those of the other surveys, owing to a difference in the interview process for that survey.

Chart 7: Firms expect input prices to increase at a greater rate . . .

Balance of opinion*

Over the next 12 months, are prices of products/services purchased expected to increase at a greater, lesser or the same rate as over the past 12 months?



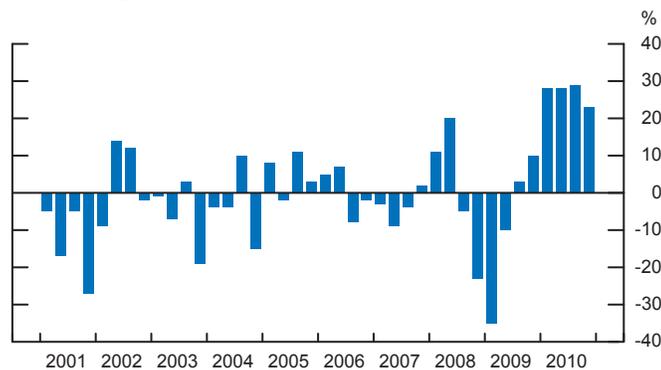
Greater: 42% Same: 45% Lesser: 11% No response: 2%

* Percentage of firms expecting greater price increases minus the percentage expecting lesser price increases

Chart 8: . . . and output prices to increase at a greater rate as well

Balance of opinion*

Over the next 12 months, are prices of products/services sold expected to increase at a greater, lesser or the same rate as over the past 12 months?



Greater: 38% Same: 46% Lesser: 15% No response: 1%

* Percentage of firms expecting greater price increases minus the percentage expecting lesser price increases

The percentage of firms reporting that labour shortages are restricting their ability to meet demand is relatively unchanged from the previous survey, and remains well below average (**Chart 6**). An increase in the number of firms in Western Canada reporting labour shortages was offset by fewer reports of shortages among firms in other parts of the country.

Prices and Inflation

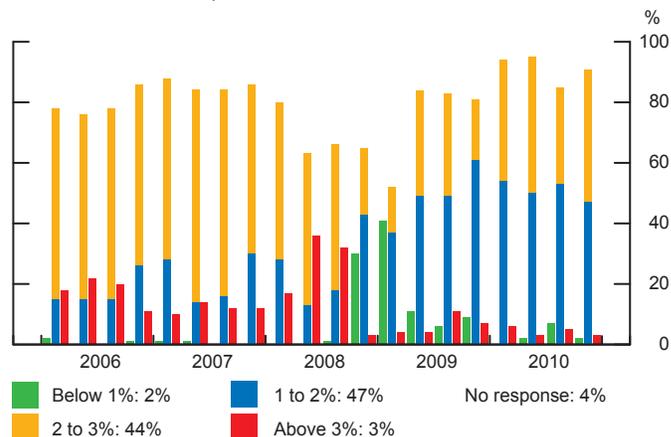
The balance of opinion on input prices moved back up after easing in the autumn survey (**Chart 7**), and indicates that businesses expect input prices to increase at a faster rate over the next 12 months. Firms most often cited strength in the prices of commodities and related inputs as the main driver of their expectations for input costs. The balance of opinion is positive for all sectors and all regions.

The balance of opinion on output prices eased but remains positive, as firms continue to expect output prices to increase at a greater rate over the next 12 months (**Chart 8**). This result largely reflects firms' intentions to at least partially pass their higher costs through to output prices, as well as their attempts to restore margins. Nonetheless, many firms noted that competitive pressures continue to limit the expected magnitude of price increases. Cost-conscious consumers and excess supply in the industry were also noted by some firms as factors limiting potential price increases.

After easing in the autumn survey, expectations regarding total CPI inflation over the next two years have moved up but remain well anchored within the Bank's inflation-control range of 1 to 3 per cent. As in the summer survey, the percentage of firms expecting inflation to be in the upper half of the range is similar to the percentage expecting it to be in the lower half (**Chart 9**).

Chart 9: Inflation expectations remain anchored within the Bank's inflation-control range

Over the next two years, what do you expect the annual rate of inflation to be, based on the consumer price index?



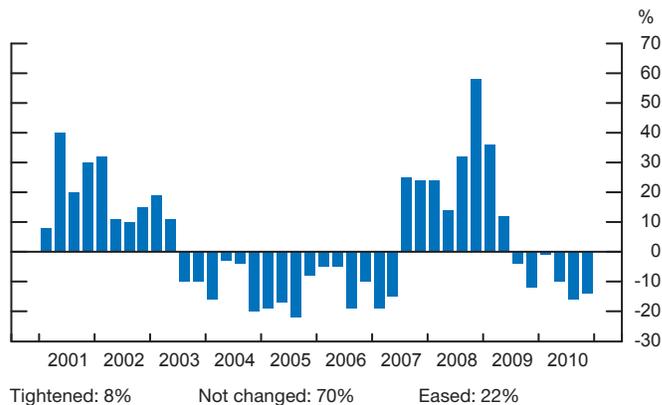
Credit Conditions

The balance of opinion on credit conditions is negative and is essentially unchanged from the autumn survey (**Chart 10**), pointing to an improvement in credit conditions over the past three months. On balance, the easing was widespread across all sources of financing (domestic capital markets, chartered banks and other financial institutions). As in recent quarters, large and medium-sized firms were the beneficiaries of the improvement in credit conditions.

Chart 10: Credit conditions eased over the past three months

Balance of opinion*

Over the past three months, how have the terms and conditions for obtaining financing changed (compared with the previous three months)?



* Percentage of firms reporting tightened minus percentage reporting eased. For this question, the balance of opinion excludes firms that responded "not applicable."

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