Business Outlook Survey

Conducted by the Bank's Regional Offices

Results of the Winter 2009–10 Survey

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Overview

- The results of the winter survey provide some evidence that confidence in the recovery is growing. While the balance of opinion on future sales is little changed, and respondents still expect the recovery to be gradual, more firms are planning to increase investment spending and employment than in the previous two surveys.
- Most firms continue to have excess capacity. While firms expect faster growth in input and output prices over the next 12 months, in many cases, this reflects expectations that prices will stabilize or move up following a year of declines. Inflation expectations have moderated but remain well anchored within the Bank's inflation-control range.
- On balance, firms reported that credit conditions eased over the past three months, although responses suggest that improvements have been modest and have been concentrated among large firms.

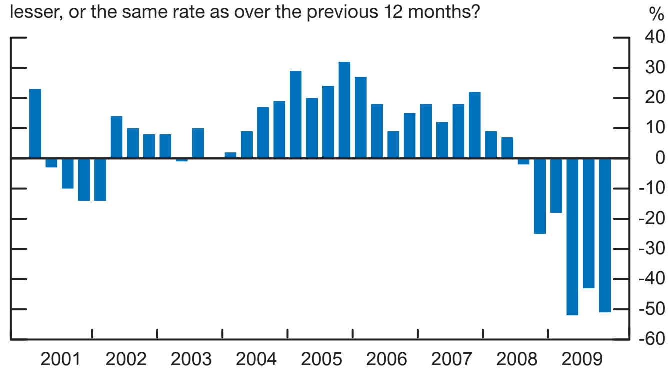
Business Activity

Reflecting the effects of the recession, the balance of opinion on past sales growth remains near its record low for a third consecutive quarter **(Chart 1)**. The balance of opinion on future sales growth is roughly unchanged at a high level, indicating that firms expect sales to grow at a faster pace over the next 12 months than over the past 12 months **(Chart 2)**. Many firms indicated that faster sales growth will result from

Chart 1: While firms report a slowing in sales growth over the past 12 months . . .

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?



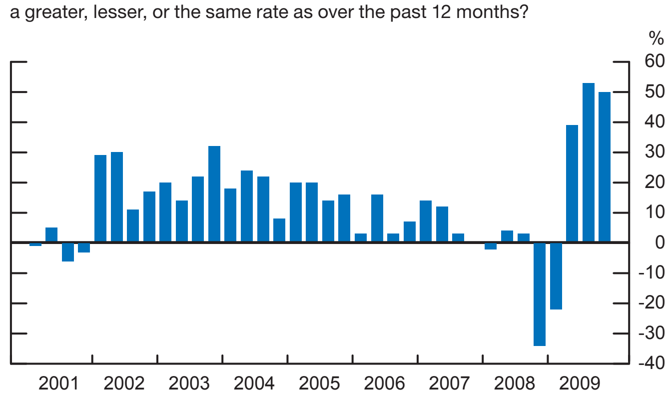
Greater: 19% Same: 10% Lesser: 70% No response: 1%

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

Chart 2: . . . they expect sales growth to pick up 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: 70% Same: 8% Lesser: 21% No response: 1%

* 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 <http://www.bankofcanada.ca/en/bos/index.html>. The winter 2009–10 survey was conducted from 16 November to 11 December 2009. 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.

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a stabilization or modest increase in sales volumes, following declines over the past year. The anticipated improvement in U.S. economic growth is positively affecting sales expectations for a number of firms.

After having remained cautious regarding investment in the previous two surveys, more firms are willing to proceed with investment plans. The balance of opinion on investment in machinery and equipment is now solidly positive, pointing to an increase in investment spending over the next 12 months **(Chart 3)**. Those firms planning on higher spending are intending either to expand output or to repair or replace existing equipment.

The balance of opinion on employment has also risen from its level in the autumn survey, as more firms expect to increase employment over the next 12 months **(Chart 4)**.

The improvement in the balances of opinion on investment and employment was led by firms located in Western Canada and Ontario—regions that were particularly hard hit during the recession and where expectations that business activity will pick up over the next year are more widespread.

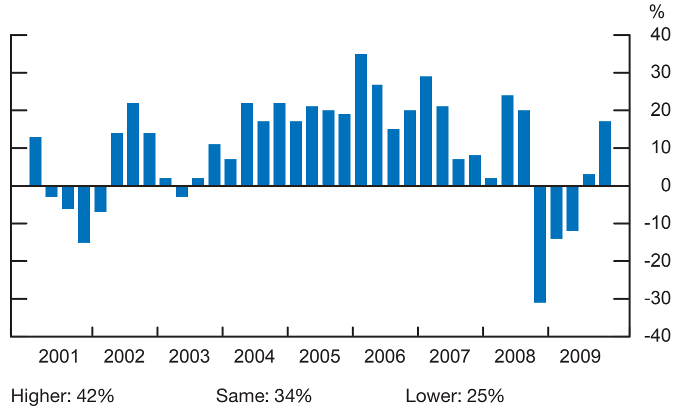
Pressures on Production Capacity

The percentage of firms reporting that they would have difficulty meeting an unexpected increase in demand has moved up from the record low in the autumn survey **(Chart 5)**, but continues to indicate subdued capacity pressures. Most firms still have excess capacity and anticipate that this situation will persist for at least the next six months, consistent with the expectation that demand will recover only gradually.

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?

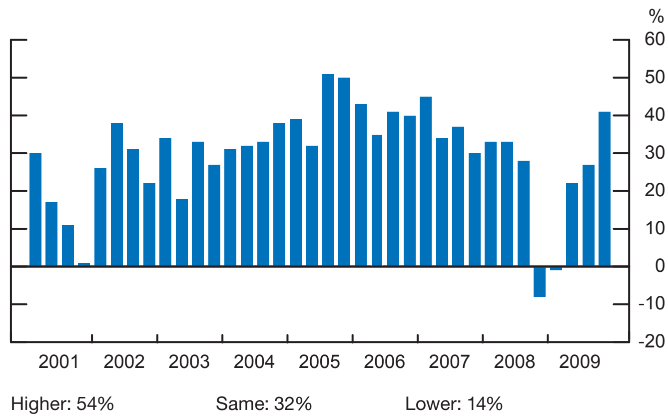


* Percentage of firms expecting greater investment minus the percentage expecting less investment

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?



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

Chart 5: Capacity pressures remain low

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

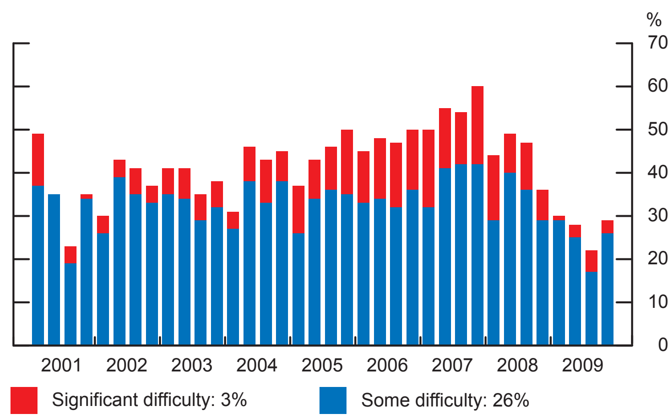
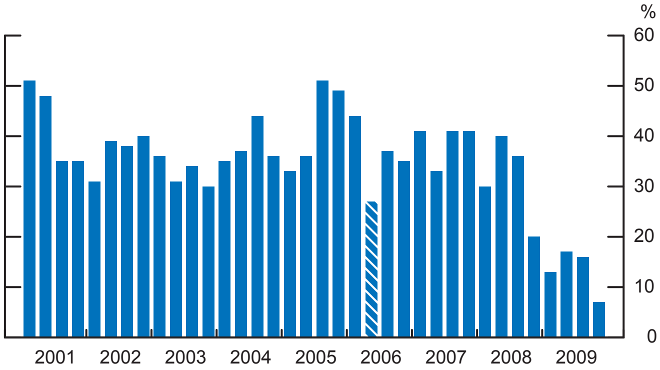


Chart 6: Few firms report labour shortages

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



Yes: 7%

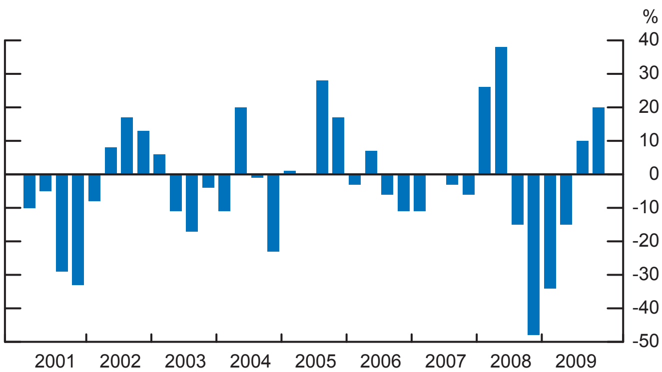
The summer 2006 results are not strictly comparable with those of the other surveys, owing to a difference in the interview process for that survey.

With businesses able to access the large pool of skilled labour that became available during the recession, the percentage of firms reporting that labour shortages are restricting their ability to meet demand has fallen to a record low for the survey **(Chart 6)**.

Chart 7: Firms expect input prices to grow at a faster 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: 36% Lesser: 22% No response: 1%

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

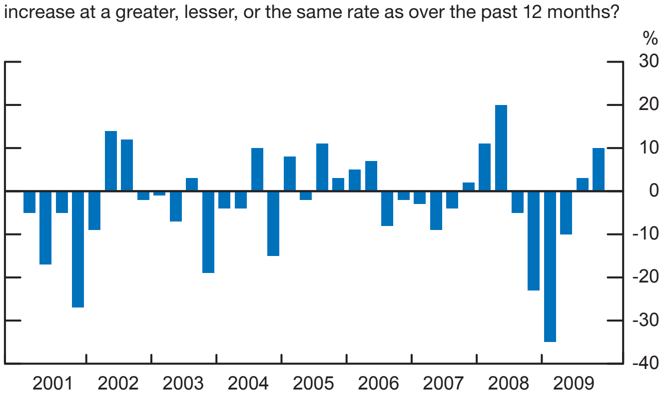
Prices and Inflation

The balance of opinion on input prices is positive, indicating that firms expect the prices of inputs to rise at a faster pace over the next 12 months **(Chart 7)**. An expectation of firmer prices for commodities and related inputs was the most frequently cited factor driving this result. Many firms reported that they expect input prices to rise or stabilize over the next 12 months, following price declines during the past year.

Chart 8: Firms expect output prices to grow at a faster rate

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: 33% Lesser: 28% No response: 2%

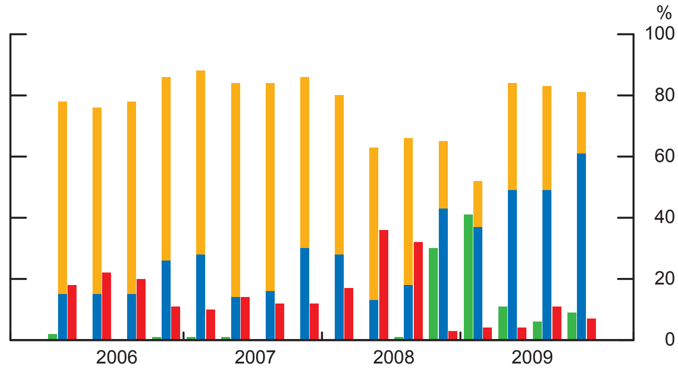
* Percentage of firms expecting greater price increases minus the percentage expecting lesser price increases

On balance, firms also expect their own output prices to grow at a faster pace than over the past 12 months **(Chart 8)**. For many firms, this reflects the end of a period of price discounting, as they plan to keep prices stable or try to partly reverse past discounts to restore profit margins. Some firms plan to pass on part of the higher cost of inputs to customers, although, for others, the ability to raise prices is limited, given soft market conditions.

Expectations regarding the level of total CPI inflation over the next two years have moderated since the autumn survey. While the vast majority of firms continue to expect inflation to be within the Bank's inflation-control range of 1 to 3 per cent **(Chart 9)**, expectations have shifted further into the bottom half of that range.

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?



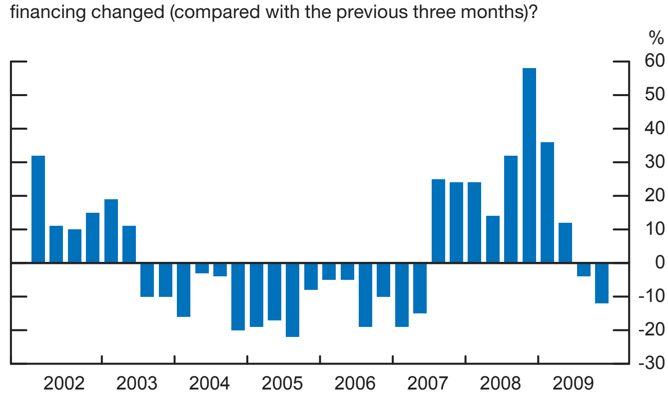
Credit Conditions

After indicating a stabilization in credit conditions in the autumn survey, the balance of opinion in the winter survey suggests that conditions have improved over the past three months, as the percentage of firms reporting an easing in credit conditions is now notably above the percentage reporting a tightening **(Chart 10)**. The negative balance of opinion is driven primarily by large firms; small and medium-sized firms tended to report that credit conditions had merely stabilized following the period of tightening. Firms that source their financing from capital markets continue to be the most likely to report an easing, although access to credit is beginning to ease among firms that borrow from domestic chartered banks as well. Responses indicate that the degree of easing has been modest in comparison with the extent of the tightening that has taken place since the onset of the financial crisis.

Chart 10: Credit conditions have begun to ease after a period of tightening

Balance of opinion*

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



Tightened: 13% Not changed: 61% Eased: 26%

* 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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