Information on the condition of the enterprise sector, including the economic climate in 2009 Q1 and forecasts for 2009 Q2

synthesis

The report is based on the results of NBP quick monitoring carried out in March 2009 on a sample of 888 non-financial entities representing all sections of the Polish Classification of Activities (PKD – NACE equivalent) (excluding farming, fishing and forestry), both public and non-public sectors, SMEs and large entities.

In view of the results of NBP quick monitoring and the data of the public statistics, the following conclusions on economic climate may be drawn:

Business climate is currently assessed as pessimistic. 2009 Q1 brought a clear deterioration in the economic situation of the enterprises sector. In 2009 Q2 enterprises expect its further worsening, yet the scale of decline will be weaker than in 2009 Q1. Assessments of the situation continue to be diversified depending on the class and branches of activity. Yet, the previously observed differences between the situation of exporters and that of non-exporters diminished.

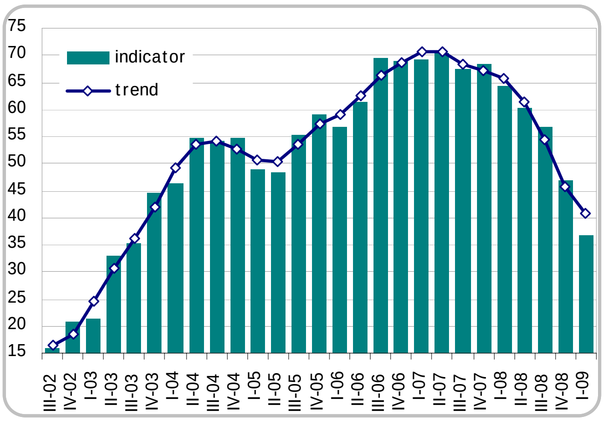


Fig. 1 Current economic condition indicator (proportion difference: number of companies in a good and very good condition minus the number of companies in a poor, bad and very bad condition)

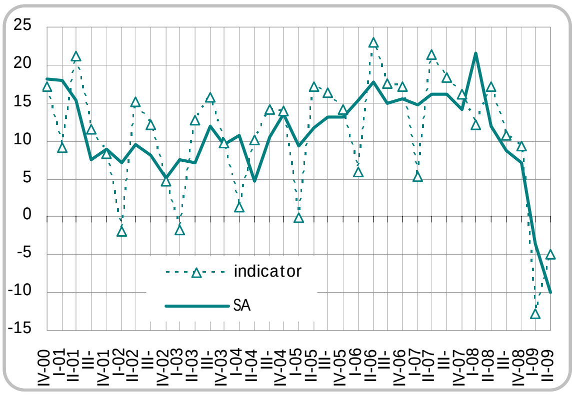


Fig. 2 Economic condition forecast indicator (proportion difference: number of companies expecting an improvement in their condition minus the number of companies expecting a deterioration in their condition)

1. Low demand continued to be the major source of problems faced by enterprises in 2009 Q1. Demand barrier is currently signalled by 30% of the surveyed companies – the largest number in the survey history. Capacity utilization in Manufacturing has declined considerably, yet, it should be pointed out that, as compared with other EU countries, Poland faced a relatively smaller decline in capacity utilization[1]. Difficulties with sales result in excessive build-up of inventories of finished goods.

[1] According to Eurostat

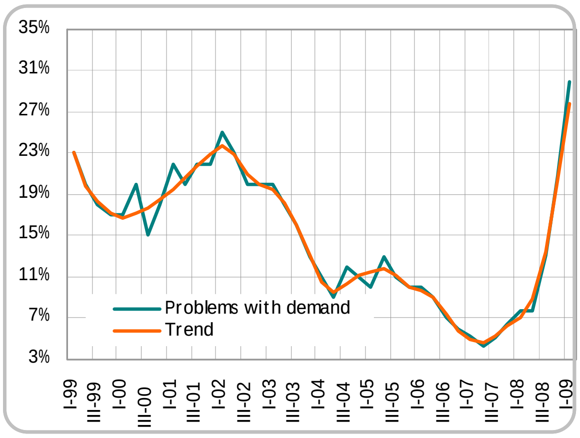


Fig. 3 Low demand as a growth barrier (percentage of companies reporting problems with finding buyers for their products)

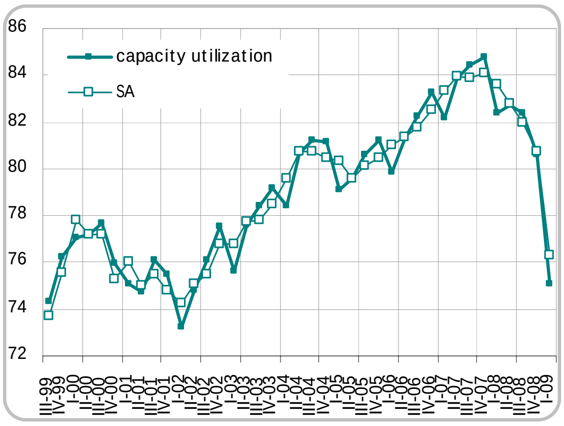


Fig. 4 Capacity utilization

2. The strongest decline in demand is recorded by exporters with high share of exports in income, among NACE section – *Construction*, and enterprises offering investment goods. Assessment of demand for consumer goods and services is relatively better, albeit it also recorded a slight deterioration. Minor signs of improvement have been noted in orders forecasts. This increase has translated, to a slight extent, into the output volume – Q2 forecasts assume its further decline. In 2009 Q2 majority of the analysed sections and classes plan to reduce production.

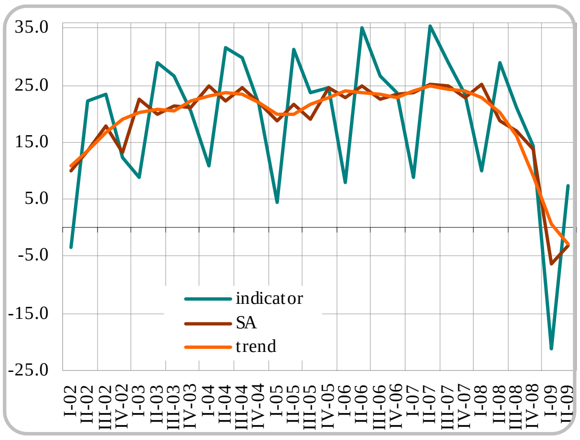


Fig. 5 New orders forecast indicator (percentage of responses) and the new orders forecast trend

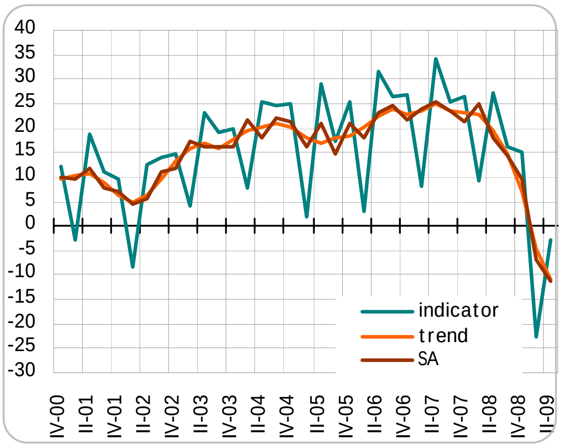
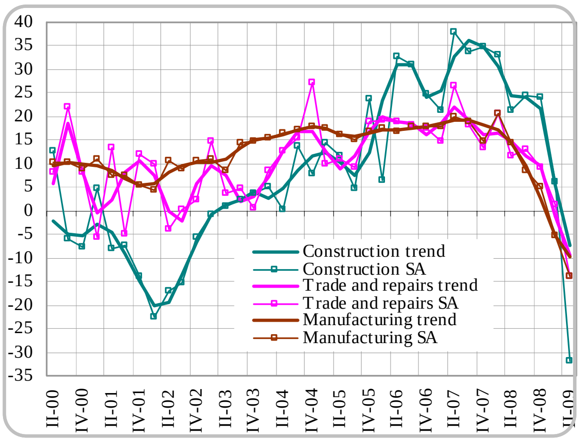


Fig. 6 Output forecast indicator (percentage of responses) and the output forecast indicator trend.



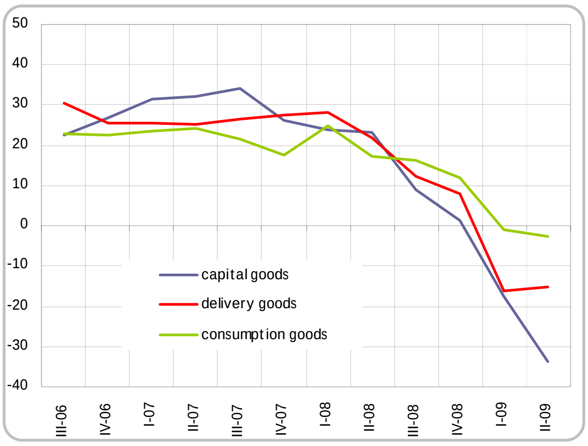
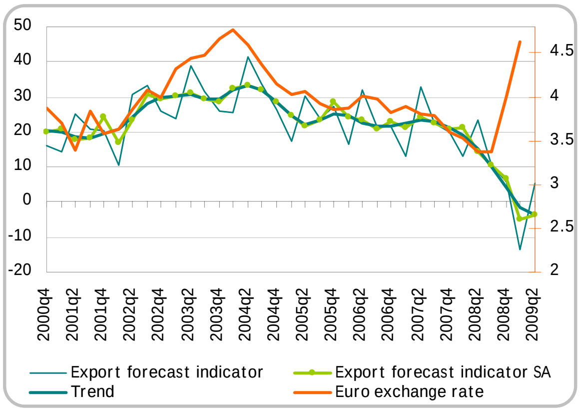


Fig. 7 Demand forecast indicator (percentage of responses after seasonal adjustment) in manufacturing, construction and trade.

Fig. 8 Output forecast indicator in the group of companies offering investment, consumer and delivery goods (section: Manufacturing; percentage of responses after seasonal adjustment)

3. Half of the enterprises which noted a worsening of the situation do not anticipate the economic slowdown to continue for a long time; they expect the economic conditions to improve already in 2009.
4. Enterprises report further declines in export volumes in Q1 and increasing number of cases of abandonment of foreign sales. Although the forecasts for Q2 suggest the likelihood of a slight improvement, majority of enterprises in the sample continue to expect export declines. According to exporters' own assessments, their situation is deteriorating, especially as regards companies with high share of exports in income. This happens despite a clear rise in profitability of export sales.



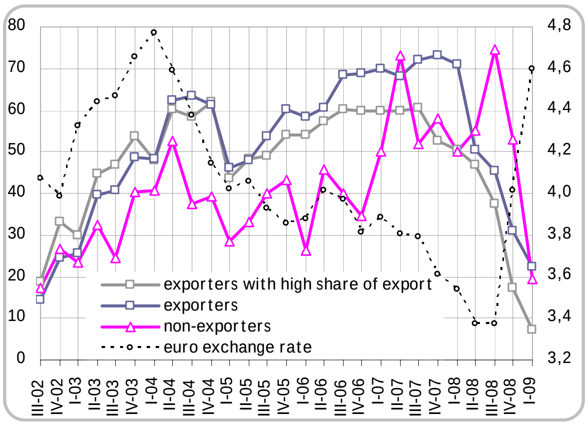


Fig. 9 Export forecast indicator and Euro exchange rate

Fig. 10 Current economic condition indicator in the group of exporters and non-exporters (*Manufacturing)*

5. Low demand translates into declining investment activity in the enterprise sector. The percentage of newly planned investment projects for Q2 has fallen to its lowest level since 2001. At the same time, the group of enterprises intending to limit or give up completing investment under construction has increased considerably. Deterioration in investment climate is mainly the result of pessimistic assessment of

current and future business conditions. This decline is enhanced by growing problems with obtaining bank financing. Thus, the role of enterprises' own funds in investment financing is rising.

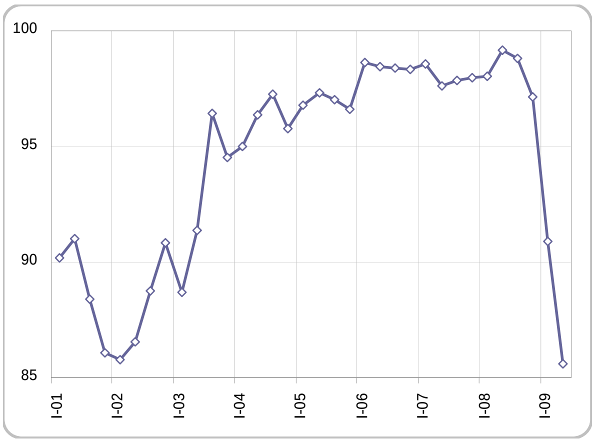


Fig. 11 Investment continuation indicator (subgroup of investors)

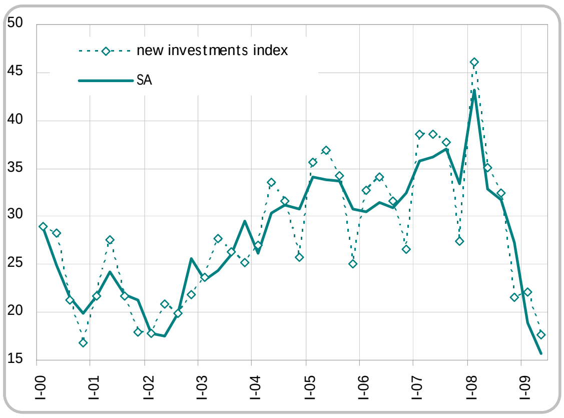


Fig. 12 New investments index - share of enterprises planning the commencement of new investments within a quarter

6. In Q1 bank loan availability diminished considerably – every third company applying for a loan faced refusal (the number of companies applying for a loan was slightly lower than in the past few quarters). The reasons for loan refusal remained generally the same. Loan refusal was, in the opinion of enterprises, basically unrelated to the enterprise's condition; the second reason for loan refusal was the lack of creditworthiness, and the third reason the lack of relevant collateral.

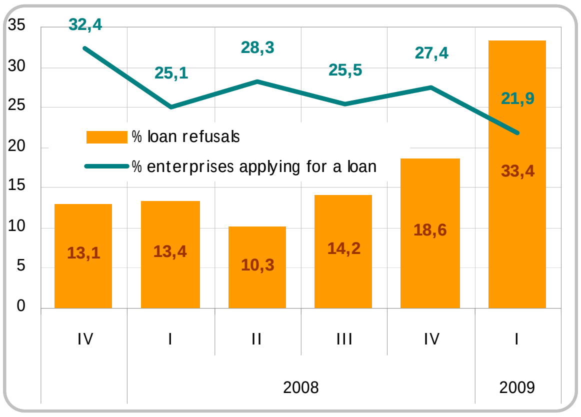


Fig. 13 Share of enterprises applying for a loan and percentage of enterprises refused the loan (in the sample of enterprises applying for a loan)

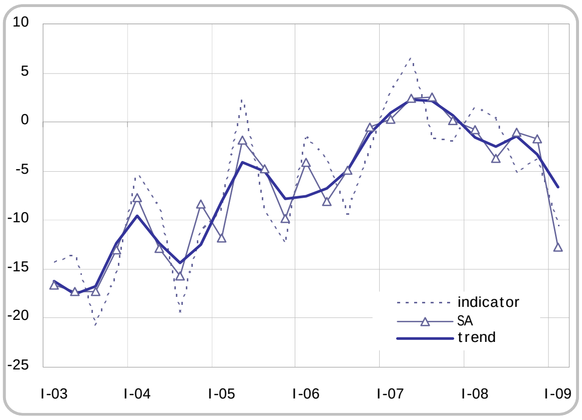


Fig. 14 Loan debt forecast indicator (proportion of responses: debt increase - debt decrease)

7. As a result of declining investment activity and growing difficulties in obtaining external financing, the surveyed enterprises declare to have lower debt resulting from bank credit. Only the largest enterprises in the sample plan to increase the credit volume.`

8. Despite considerable deterioration in business conditions, liquidity situation of companies continues to be, in their assessment, relatively good, and it is deteriorating only gradually. This is the consequence of high profits generated until 2008 Q3. Therefore, despite a slight decline, assessments of liquidity of enterprises remain favourable; especially good are assessment of the capacity to repay bank debt. Similarly to the previous quarters, the timeliness of trade payables settlement is considerably lower than in the case of bank loan; yet, the last quarter brought a significant deterioration also in bank loan repayment.

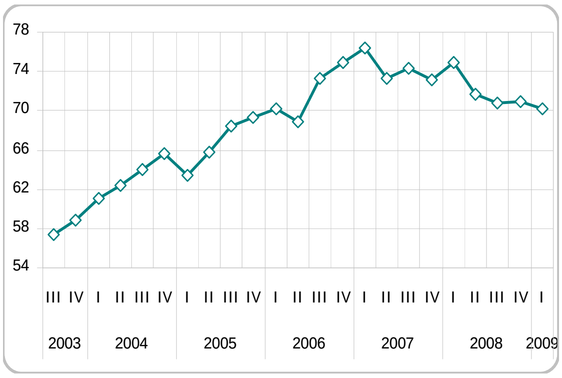


Fig. 15 Share of enterprises not reporting any problems with maintaining financial liquidity

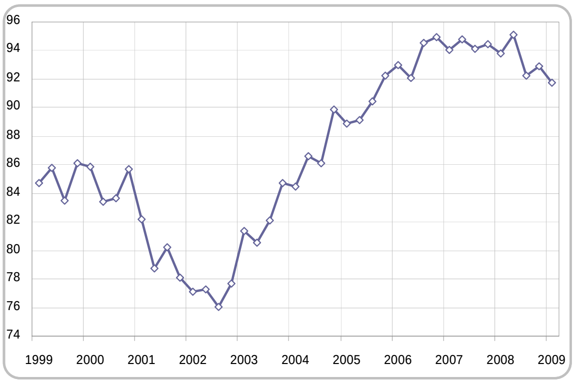


Fig. 16 Share of entities making loan repayments in accordance with loan contracts

9. Output decline translates into plans of employment reduction. Every fourth company in the sample plans to reduce employment, while only 5% of companies plan to increase employment. Plans of employment reduction prevail over growth plans in majority of classes and sections in the sample.

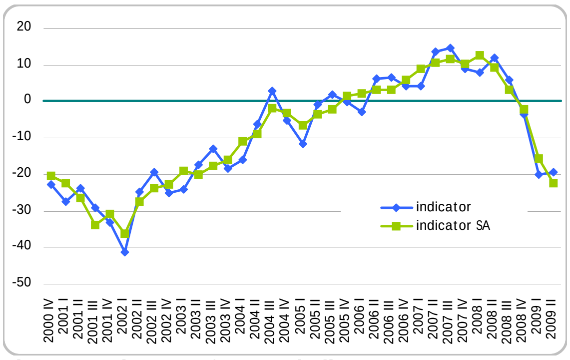


Fig. 17 Employment forecast indicator

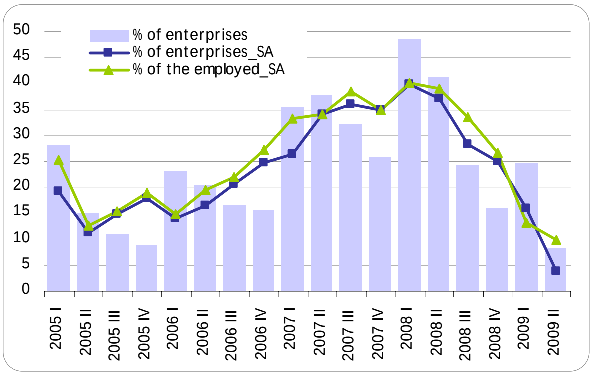


Fig. 18 Proportion of enterprises planning wage increases and proportion of employees benefiting from wage increases

10. Along with deteriorating business conditions, including, in particular weakening labour demand, also the proportion of companies planning wage increases is diminishing. In 2009 Q2 slightly over 8% of respondents plan wage increases and 9.5% of companies plan wage cuts. The scale of wage increases will be two times lower than the scale of wage cuts. Yet, since the plans to change wages are asymmetrical

in the sample – large companies announce wage increases, while the SMEs sector plans wage cuts – finally, the average remuneration in the sample should minimally increase. In two out of three cases, wage cuts are planned by companies also intending to reduce employment.

11. The number of enterprises intending to increase prices of their products and services is falling, and the number of companies ready to reduce prices of their finished goods is growing. On the one hand, this is the effect of the anticipated decline in the growth rate of prices of commodities and raw materials used in production, and, on the other hand, an attempt to improve their competitiveness. Plans to reduce prices are announced by both exporters, which may be supported by zloty depreciation, as well as enterprise offering their products on the domestic market only. In the latter group, the number of such decisions has considerably increased during the last quarter.

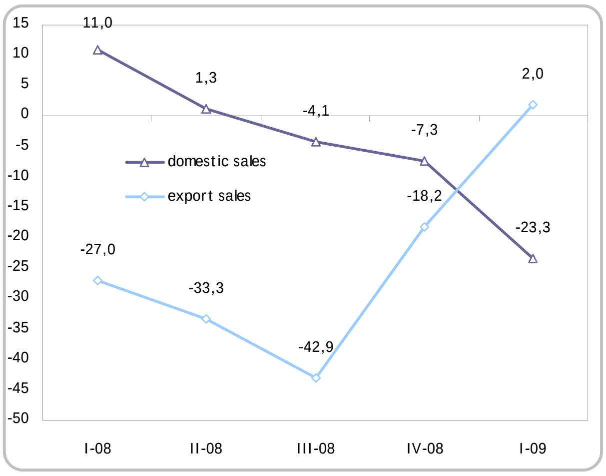


Fig 19. Changes in margins on domestic and foreign sales (percentage of enterprises declaring margin increase minus percentage of enterprises declaring margin reduction)

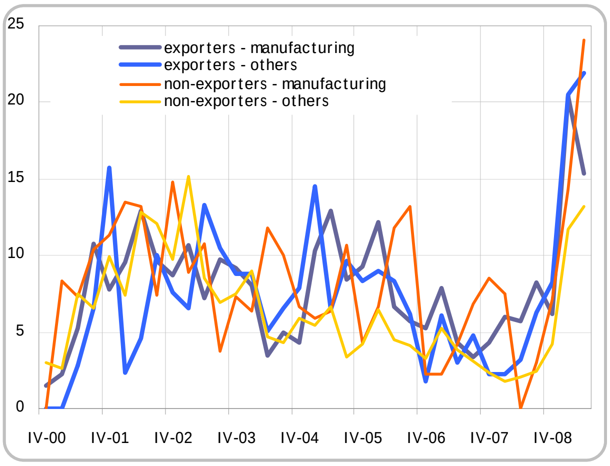


Fig. 20 Proportion of enterprises planning to reduce prices within a quarter in selected groups of enterprises.

12. A marked decline in profit margins on production for domestic market has been observed. The most commonly given reason for such decline is the reduction in the volume of output and in rarer cases rising costs of production or declining prices of own products and services. The fall in margins is mainly observed in construction and manufacturing. High profit margins persist in the service sector, power industry and mining. The situation in the group of exporters is quite different – despite falling demand, profit margins on foreign sales are increasing. The growth in export margins is mainly the result of the weakening of the zloty.

13. Growing profitability of foreign sales and financial losses suffered by enterprises as a result of the use of derivative instruments (especially, FX options) have brought about a significant decline in the number of exporters that use instruments hedging against foreign exchange risk – fall from 41% to 32%.

14. Financial losses resulting from the use of derivatives were suffered by 15% of enterprises in the sample, while less than half of this group considered them as a considerable charge to the financial result. Such problems were signalled more often by large enterprises, which resulted from larger representation of exporters in this group and, consequently, higher proportion of companies using derivative instruments. For the same reason losses were reported by the section *Manufacturing* and by companies with foreign capital. The situation of enterprises which suffered minor financial losses did not differ considerably from the situation of entities not using derivatives. Yet, the assessment of enterprises which suffered major financial losses of their condition was much worse than in the case of other companies, which translated into more frequent plans of employment reduction and lower investment activity of this group. Yet, it should be noted that enterprises which are not able to achieve full export profitability and whose assessment of their situation (also for this reason) is relatively worse than that of other companies, have recourse to derivatives much more often. In such case, financial losses constitute a major problem and may pose a real threat to the company's ability to continue as a going concern.