

Quarterly Enterprise Survey

Nº 4 (30)
November 2009

- The Industrial Confidence Indicator increased from -0.13 in July to -0,01 in October.
- The majority of polled enterprises managers (54.7%) do not expect any significant changes of the overall economic situation over the next six months.
- The share of managers who consider the regulatory climate to be an obstacle to the production growth decreased significantly compared to July.
- According to the managers in the 3rd quarter the availability and the affordability of bank loans for enterprises increased.
- As managers expected, the production volumes did not change significantly in the 3rd quarter compared to the 2nd one.
- Managers plan to increase output in the 4th quarter.
- Managers of enterprises expect the growth in the number of new orders during the next three months.
- In the 3rd quarter the trend of employment increase on enterprises continued. Managers do not expect any significant changes of employment in the 4th quarter.
- In the 4th quarter managers predict the continuing rise of raw materials prices and sales prices but at lower rates than in the 3rd quarter.

A panel of 300 manufacturing enterprises is used to monitor their managers' perceptions and expectations towards changes in general business climate and towards the indicators of company performance.

This issue presents the results of the survey conducted from October 5 till November 11, 2009

Performance: Q3' 09 vs. Q2' 09

Expectations: Q4' 09 vs. Q3' 09

Business climate: Assessment for October' 09, expectations for the next 6 months

GENERAL INDICATORS

Industrial Confidence Indicator

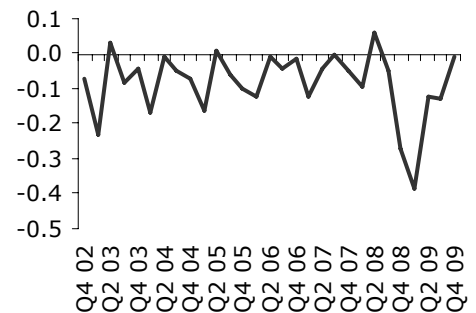
In October *the Industrial Confidence Indicator* made up -0.01. After the decrease in July compared to April by 1 point (from -0.12 to -0.13), it has increased by 12 points in comparison to July. It happened because of improvement of all three components of *the Industrial Confidence Indicator*. The improvement of the production plans of the enterprises for the next 3 months was observed: the value of the corresponding indicator grew up from 0.05 to 0.14 (for details see PRODUCTION INDICATORS). There was some increase in the value of the component "orders book" (from -0.66 in July to -0.52 in October) and the value of the component "the stock of finished goods" decreased (from -0.23 in July to -0.34 in October).

Business climate

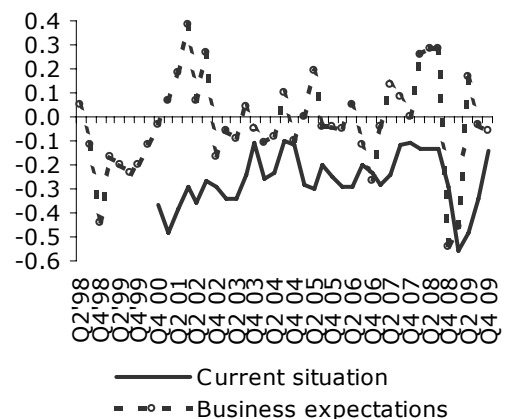
In October the managers' assessment of the current overall economic situation improved significantly compared to July: the value of the *index of the current business situation* increased from -0.34 to -0.14. It happened due to the increase of the share of polled managers who assess the business climate as good one (from 8.0% in July to 11.2% in October) and simultaneously due to the considerable decrease of the share of those who consider the climate to be poor (from 47.6% to 29.9%). In addition, the share of managers who estimate the business climate as satisfactory increased significantly from 44.4% in July to 59.0% in October. This is typical for enterprises of all industries, ownerships and sizes. Besides, the smaller the enterprise, the worse are the assessment of business climate.

At the same time, the managers' expectations concerning the changes in the business climate over the next six months remain without significant changes. In October *the index of business expectations* made up -0.06 (in July — -0.03). The share of the surveyed managers who anticipate positive changes decreased from 23.3% in July to 16.7% in October. At the same time, the share of managers that expect the worsening of overall economic situation

Survey based Industrial Confidence Indicator



Indices of Overall Business Climate



Authors:
Yana Dvorak
Oksana Kuziakiv

Institute for Economic Research
and Policy Consulting
Reytarska St. 8/5-A, 01034 Kyiv
Tel. (+38044) 228-6342
Fax (+38044) 228-6336
E-mail: institute@ier.kiev.ua
http://www.ier.com.ua

practically has not changed (28.9% in July and 28.6% in October). While the share of those who expect neither positive, nor negative changes of overall economic situation during the next six months increased from 47.8% in July to 54.7% in October.

Regulatory climate

The share of managers, according to whom the unfriendly regulatory climate is a significant obstacle to the growth of production volumes at their enterprises, reduced significantly in October compared to July from 49.0% to 33.8%. At the same time it is worth mentioning that the both absolute value and change of this indicator essentially vary by enterprise's size:

- in the group of small enterprises the number of managers who consider the unfriendly regulatory climate to be a significant obstacle to the production growth decreased from 50.0% in July to 40.0% in October and is the highest compared to other groups of enterprises;
- in the group of medium-sized enterprises the number of the polled managers, according to whom the unfriendly regulatory climate is a significant obstacle to the production growth, decreased by half (from 51.5% in July to 25.5% in October);
- in the group of large enterprises the number of managers who estimate the unfriendly regulatory climate as an important obstacle to the production growth reduced from 43.3% in July to 35.8% in October.

The number of respondents considering the unfriendly regulatory climate as a significant obstacle to the production growth reduced due to the decrease of the values of all three components of the combined indicator of "unfavorable regulatory climate", namely: the high regulatory pressure (from 39.1% to 25.5%), frequent changes in economic legislation (from 10.5% to 7.7%) and corruption (from 14.7% to 7.7%). (See IMPEDIMENTS TO PRODUCTION GROWTH).

Assessment of the Government Economic Policy

Average rating of the Government activities by respondents increased to 2.40 points in October compared to 2.17 points in July (by a 5-point scale). According to the results of the survey, it happened due to the increase of the share of interviewed managers who asses positively to the work of the Government (from 6.7% in July to 10.0% in October) and simultaneously due to the decrease of the share of those who evaluate it negatively (from 62.0% to 49.8%). Besides, the share of enterprises managers hesitating with formulating their opinions on the matter, increased: 40.2% of respondents chose the option "difficult to answer" or did not respond to the question.

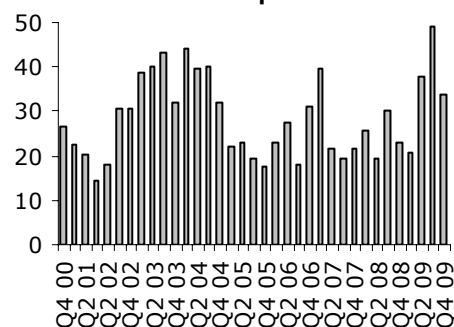
The assessments of the Government activities significantly depend on the regional location of the enterprises. The poorest assessment of economic policy has been given in Sumy (2.08), then goes Khmelnytsky (2.35), Kyiv (2.40) and Kharkiv (2.43). The highest evaluation of the Government activities is given in Lviv (2.59 points).

Lending Climate

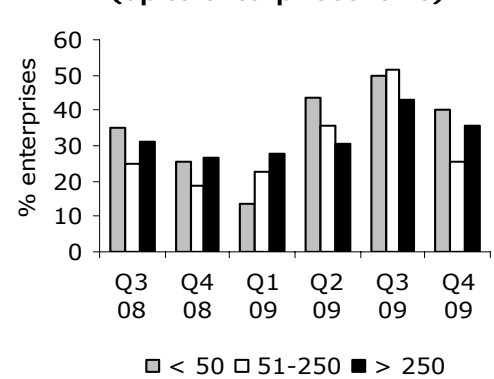
In the 3rd quarter the lending climate has somewhat improved, and it was characterized on the one hand by a slight increase of the volume of offers of bank loans. The share of managers who believe that banks are willing to provide short-term loans to such enterprises like theirs increased from 34.1% in the 2nd quarter to 37.4% in the 3rd one. The value of the corresponding indicator for long-term loans went up from 22.7% to 27.8%.

Also, according to respondents, the affordability of loans for the enterprises has increased. In particular, the share of managers who believe that their company can afford to take loans, increased respectively for short-term loans from 20.7% in the 2nd quarter to

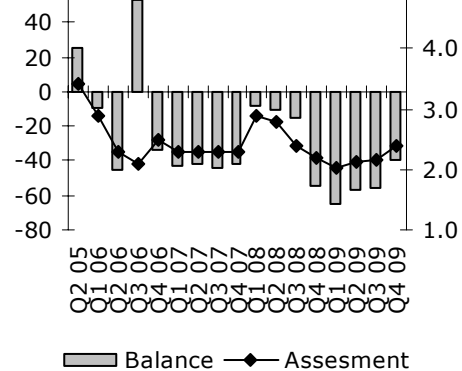
Unfriendly regulatory environment, % of enterprises



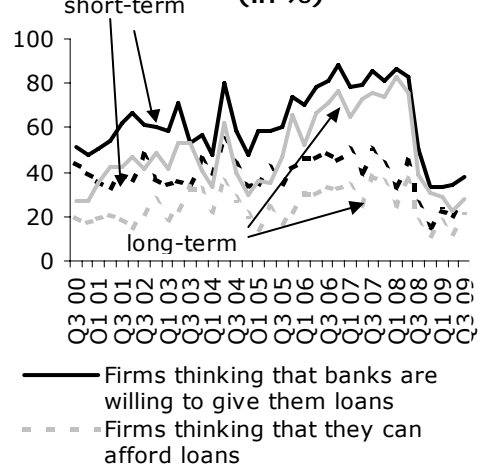
Unfriendly regulatory environment (up to enterprises' size)



Government Policy Assessment



Affordability of Loans (in %)



27.4% in the 3rd, and for the long-term ones — from 12.4% to 19.8%.

PRODUCTION INDICATORS

As managers expected, the volumes of industrial production did not change significantly in the 3rd quarter compared to the 2nd one. Thus, the value of *the index of expected production* for the 3rd quarter made up 0.05, whereas the actual value of *the index of production* for this quarter equals to 0.08.

The highest value of *index of production* has been recorded for the enterprises of printing industry (0.16), and the lowest one – for light industry (-0.18). The most considerable growth of production is observed for large enterprises (over 1000 employees). The value of the respective index increased considerably from -0.25 in the 2nd quarter to 0.26 in the 3rd one. Managers of medium enterprises report about less significant growth of production compared to the 2nd quarter (from 0.02 to 0.12). However, small enterprises have slowed down the reduction of production and remain practically at the same level as in the 2nd quarter (-0.14 in the 3rd quarter and -0.16 in the 2nd one). The highest value of *index of production* has been recorded for the state enterprises (0.15), for the privatized and private ones it amounts to 0.03 and 0.00 respectively.

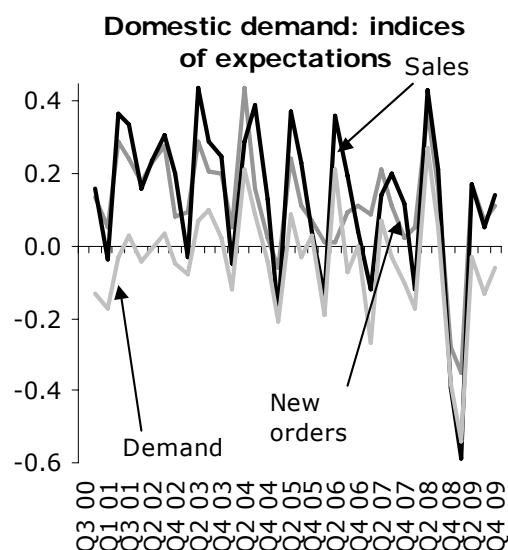
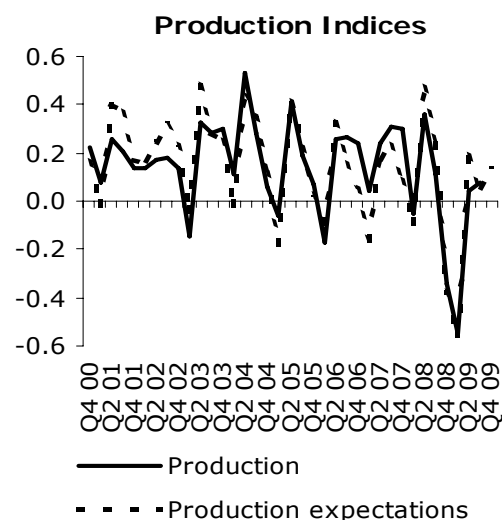
In the 4th quarter managers of enterprises have plan to increase their production activity. *The index of expected production* grew up from 0.05 (for the 3rd quarter) to 0.14 (for the 4th quarter). At the same time, every second surveyed firm (49.4%) plans no changes in the volume of production for the 4th quarter compared to the 3rd one, 30.9% have intention to increase output and 19.7% plan to reduce the production volumes (for comparison: in the 3rd quarter the output gained in 34.2% of firms, whereas reduced — in 30.0% of firms).

Increase of *the index of expected production* has been recorded for enterprises of all fields of industry, except construction materials industry: the value of the respective index diminished from 0.14 (for the 3rd quarter) to -0.39 (for the 4th quarter). The most optimistic production plans have the enterprises of heavy (0.40), wood processing (0.27) and printing (0.24) industries. Compared to other types of size the best production plans are observed for large-scale enterprises (over 1000 employees): the value of the respective index equals to 0.58. The attitudes of the managers of small and medium-sized enterprises do not significantly differ: the values of *the index of production expectations* are equal to 0.04 and 0.06 respectively. Private-owned firms have the most optimistic production plans compared to other types of ownership: *their index of production expectations* is equal to 0.14, while the respective values for state and privatized firms make up 0.11 and 0.10.

Demand, Sales, New Orders

After the increase of domestic demand, observed in the 2nd quarter, there were no significant changes in indicators of demand in the 3rd quarter. The value of *the index of domestic demand* remains practically at the same level as in the 2nd quarter (-0.25 in the 3rd quarter and -0.29 in the 2nd). 19.2% of polled managers of enterprises informed about growth in demand and 46.1% – about its decline. In the 2nd quarter these indicators were equal to 16.1% and 48.0% respectively. In the 4th quarter the majority of enterprises managers (52.1%) do not expect any significant changes of domestic demand. The value of *the index of expected demand* is -0.06.

According to the respondents' estimations, in the 3rd quarter the volume of sales did not change significantly compared to the 2nd quarter: the value of the corresponding index amounts to 0.03 (in the 2nd quarter — 0.01). For the following quarter one third of enterprises managers (32.3%) expect a decrease of this indicator:



the index of expected sales is 0.14.

In the 3rd quarter managers do not note increase in the number of new orders. The value of *the index of new orders* makes up 0.01 (in the 2nd quarter — -0.03). The share of managers assessing the order book as a satisfactory one increased to 36.3% in October compared to 26.9% in July. On the contrary, the share of companies those have no stock of orders fell from 31.6% in July to 23.8% in October.

In the 4th quarter managers forecast a slight increase in the number of new orders compared to the 3rd quarter (from 0.01 to 0.11). Managers of heavy (0.19), food (0.19) and printing (0.12) industries are most optimistic about receiving new orders in the 4th quarter, while the most pessimistic are the managers of light (-0.36) and construction materials (-0.17) industries.

Impediments to Production Growth

Traditionally low demand (65.7%) and excessive taxation (56.2%) took first and second places in the ranking of obstacles for production growth. Problems of liquidity rose to the third position in the list of impediments: the number of surveyed managers, according to which the lack of working capital is a barrier for production growth, increased from 36.4% in July to 39.4% in October.

Unstable political situation still remains at the fourth place in the list of impediments. The importance of this barrier slightly decreased from 39.1% in July to 36.5% in October.

On the contrary, in October the relevance of the barrier "high interest rates" significantly increased for enterprises (from 18.6% to 28.8%), and the problem of the availability of bank loans still remains considerable (24.8% in July and 26.6% in October).

The percentage of respondents noting "high competitive pressure" as a barrier for production growth slightly increased to 27.7% in October compared to 25.2% in July.

The share of managers, according to whom the shortage of raw materials is a significant barrier for production growth, after diminution in July, compared to April, increased in October from 17.1% to 22.3%, which apparently concerned with the rising of raw materials prices.

In addition, it should be noted that the importance of the obstacle "shortage of skilled workers" increased sharply in October (from 3.5% to 10.6). The absolute values of the outdated technologies problem and shortage of production capacities also increased in October compared to July from 5.8% to 8.8% and from 3.9% to 5.1%, respectively.

In October a further reduction of the importance of the problems with energy supply was observed. The share of managers who considered it to be a major obstacle to production growth, reduced from 8.5% in July to 3.6% in October.

Employment

In the 3rd quarter the trend of the gradual increase of employment level at enterprises continued. The value of *the index of employment* rose to -0.16 in the 3rd quarter from -0.30 in the 2nd one. The share of managers who believe that the level of employment in their companies is satisfactory for the existing volumes of production increased from 67.8% in July to 68.2% in October.

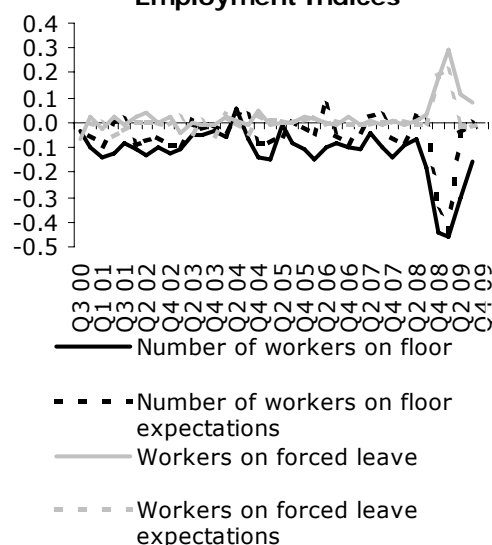
The vast majority of managers (87.7%) do not expect any significant changes of employment in the 4th quarter. The value of *the index of expected employment* equals to -0.05. This is typical for enterprises of all industries, ownerships and sizes.

The share of enterprises with reduced work time decreased from

Impediments to production growth

	Q1 09	Q2 09	Q3 09	Q3 09 vs. Q2 09
Low demand	68,0	65,9	65,7	-0,2
Excessive taxation	50,2	49,2	56,2	+7,0
Liquidity problems	39,8	36,4	39,4	+3,0
Unstable political situation	42,9	39,1	36,5	-2,6
Unfavorable regulatory climate	37,7	49,0	33,8	-15,2
High regulatory burden	25,5	39,1	25,5	-13,6
Corruption	14,3	14,7	7,7	-7,0
Changes in economic legislation	19,0	10,5	7,7	-2,8
High interest rates	18,6	18,6	28,8	+10,2
High competitive pressure	33,8	25,2	27,7	+2,5
Access to credits	17,3	24,8	26,6	+1,8
Shortage of raw materials	19,5	17,1	22,3	+5,2
Shortage of skilled workforce	4,8	3,5	10,6	+7,1
Outdated technologies	3,9	5,8	8,8	+3,0
Shortage of capacities	1,7	3,9	5,1	+1,2
Problems with energy supply	15,6	8,5	3,6	-4,9

Employment Indices



35.9% in the 2nd quarter to 24.0% in the 3rd one. The value of the corresponding index diminished from 0.11 to 0.08. Managers expect a further decrease of this indicator (-0.01) in the 4th quarter. The percentage of enterprises with partial employment will decrease to 20.7%.

According to the polled managers, it became more difficult to find qualified staff in the 3rd quarter. The value of the corresponding index rose from 0.17 to 0.27. In particular, 49.6% of respondents indicated that the search for skilled workers became difficult in the 3rd quarter, while 17.8% of the polled noted the facilitation of their search. According to the respondents' estimations, the search of the unskilled workers has also become more difficult in the 3rd quarter. The value of the corresponding index increased from -0.16 to -0.13.

FINANCIAL PERFORMANCE INDICATORS

Prices

In the 3rd quarter the prices of raw materials and sales prices continued to rise and even with higher rates than managers of enterprises had expected. Thus, the value of *the expected index of raw materials prices* for the 3rd quarter was 0.39, and the value of the actual index for this quarter is 0.66. For sales prices corresponding indices equal 0.27 and 0.37.

For the 4th quarter managers expect the continuing rise of prices but at lower rates than in previous quarter. This applies both to sales prices and raw materials prices. *The index of expected purchase price* is 0.45 for the 4th quarter, and *the index of the expected sales price* amounts to 0.21.

Profitability

As managers expected, the financial results of their enterprises did not change significantly in the 3rd quarter compared to the 2nd one. Namely, the value of *the index of the expected profitability* on the 3rd quarter was 0.00, and the actual value of *profitability index* for this quarter is -0.02 (in the 2nd quarter — -0.15). 25.7% of the surveyed managers indicated a deterioration in financial results; they did not change in 53.3% of the enterprises, and 21.0% of managers noted that the financial results of their enterprises improved during the last three months. In the 2nd quarter these indicators were equal to 34.9%, 49.6% and 15.5% respectively.

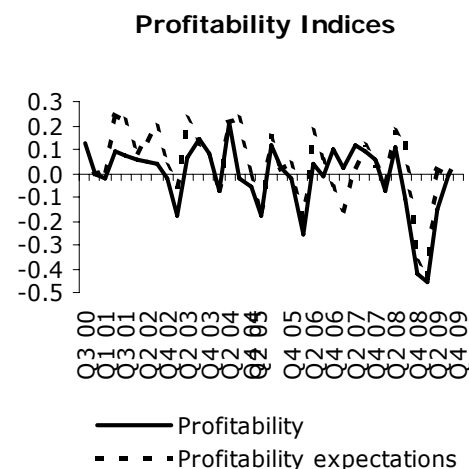
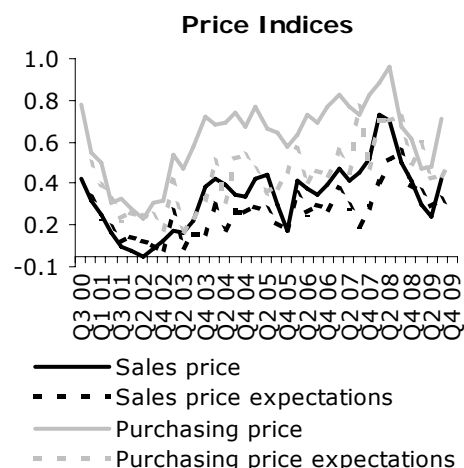
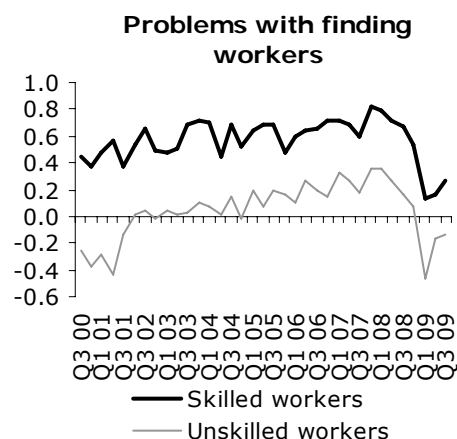
The improvement of financial performance in comparison to the previous quarter has been recorded only at the enterprises of heavy industry: the value of *profitability index* increased from -0.12 in the 2nd quarter to 0.07 in the 3rd one. There were no observed any significant changes in all other fields of industry.

The vast majority of managers (71.3%) consider the financial results of their enterprises will not change significantly in the 4th quarter compared to the 3rd one; 15.0% — expect an improvement and 13.8% — predict the worsening of financial performance. The value of *the index of expected profitability* is 0.04.

COMPETITIVE PRESSURES

According to the managers of enterprises, the level of competitive pressure from domestic producers virtually did not change in the 3rd quarter. The value of the corresponding index was -0.08 in the 2nd quarter and -0.03 in the 3rd.

The managers of wood processing, light and construction materials industry report the increase of pressure (from -0.55 to -0.23, from -0.13 to 0.16 and from -0.04 to 0.17, respectively). According to the managers of heavy and printing industries, competitive pressures, on the contrary, have decreased significantly. The value of the corresponding index dropped respectively from -0.01 to -0.32 and from 0.19 to 0.07.



At the same time, managers note that the pressure from manufacturers in Russia/CIS countries and other foreign producers has slightly decreased compared to the 2nd quarter. The values of the indices fell respectively from -0.37 to -0.46 and from -0.43 to -0.47.

Thus, the main rivals of Ukrainian enterprises at the domestic market, as estimated by their managers, are domestic producers: 31.9% of respondents defined the level of competitive pressure from their side as strong.

Appendix 1: Methodology

All indices are calculated using the same methodology. For each positive answer we score +1, for each negative answer -1, and for each answer indicating no change we score 0. For example, if 20 respondents report an increase in production, 50 respondents report a decrease, and 30 report no change, the corresponding index level would be -0.30. Thus, a positive (negative) value, for instance for the production index, indicates that the number of firms increasing their production is greater (less) than the number of firms decreasing it. Any score approximately greater than +0.09 or less than -0.09 is statistically significant at the 5% level.

The *Industrial Confidence Indicator* is defined as the arithmetic mean of the *indices of production expectations*, *assessments of the volumes of new orders* and *assessment of the stock of finished products* (the latter with an inverted sign).

The general category "unfriendly regulatory climate" has been broken into three factors, namely: (1) high regulatory burden due to a large number of inspections, unclear procedures etc., (2) frequent changes in regulations and (3) corruption. The indicator "unfriendly regulatory climate" reflects the share of firms that have selected at least one of these three factors as an impediment to production.

The methodology of calculation for the indices of competitive pressure is similar to that for the other indices. Scale: -1 – no or weak pressure, 0 – moderate, 1 – strong.

Size classification of enterprises is based on the number of workers. We sort out the following size groups of enterprises: small (up to 50 workers), medium (51-200 workers), large medium (251-500 workers), large (501-1000 workers) and largest (over 1000 workers). In certain cases, if there are no significant differences among groups, the latter three groups are classified as large-size enterprises.

For further information concerning the sample characteristics, the questionnaire, the index methodology and full data sets please contact Oksana Kuziakiv kuziakiv@ier.kiev.ua.

Index of competitive pressure from Ukrainian producers

Industry	Q1'09	Q2'09	Q3'09
Heavy	0.29	-0.01	-0.32
Machine build.	-0.47	-0.47	-0.44
Woodworking	-0.09	-0.55	-0.23
Construct. Mat	-0.10	-0.04	0.17
Light industry	-0.09	-0.13	0.16
Food processing	0.34	0.31	0.32
Printing	0.07	0.19	0.07

Number of employees, %

	Q3'09
Fewer than 50	36.4
51 – 250	34.2
251 – 500	13.5
501 – 1000	9.1
Over 1000	6.9

Regions, %

Lviv	14.5
Kyiv	32.4
Kharkiv	32.7
Khmelnytsky	10.9
Sumy	9.5

Industries, %

	Q3'09
Heavy ¹ industry	10.2
Machine building	24.7
Wood working	4.4
Construction materials	12.0
Light industry	8.4
Food processing	21.8
Printing	9.8
Other	8.7

¹ The heavy industry includes metallurgy, chemical, petrochemical and fuel industries.