

E4S BRIEF

Do Managers Care About Energy Prices?

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IN A NUTSHELL

Are energy costs important to decision-makers in Swiss firms? To answer this question, we conducted a survey between June and August 2023 among decision-makers in 882 Swiss firms across all industries. We find a paradox: Swiss managers care about energy prices (more than half of them consider energy prices as very important or rather important), although the typical energy cost share is very low (about 3% for the median firm).

The energy cost share does matter for some firms. First, some firms are highly exposed to energy prices through a high energy cost share (one out of ten report an energy cost share of 14% or more). Second, the reported importance of energy prices is strongly related to the energy cost share, suggesting that energy prices matter to firms through a direct cost channel for those with a high energy cost share.

We also asked firms about their recent energy price changes. Firms typically experienced a large price increase (10% over the past 12 months for the median firm), but some reported a very large increase (one out of ten report an increase of 40% or more). Managers who have experienced a larger increase also reported a higher importance of energy costs, suggesting that the reported importance is related to managers' recent experience and can evolve quickly. These firms are also more uncertain about future energy price developments. Both the high price increase and the high uncertainty pose a direct threat to these firms' investment decisions.

Because some firms are highly exposed to energy prices, and most firms care about energy prices, this should thus be a concern to policymakers. Since energy price changes are heterogeneous across firms, the promotion of fair-priced energy price insurance could be an attractive policy option.

WHAT WE DO AND WHY IT MATTERS

Firms operate in a risky environment, facing multiple types of risk that pertain, among others, to their demand, their human resources, physical risk and their production costs. Recently, the surge in energy prices has brought to the fore this specific type of risk. Are energy prices an important variable for firms? If so, what are the channels through which firms are exposed to energy prices? We design a new firm survey to answer this question and examine the relation between the firms' reported energy cost importance and their energy cost share. We assess whether the reported importance can be explained by the direct exposure of firms to energy costs. It is important for policy makers to understand firms' exposure to energy prices and whether it pertains to factors internal or external to the firms.

HOW WE DO IT AND MAIN FINDINGS

Between mid-June and mid-August 2023, respondents from 882 Swiss enterprises participated in an online survey. For the analysis, we restricted the sample further to private commercial enterprises only. This retained 737 respondents.

Respondents were asked what percentage of their firm's total operating expenses was spent on energy products (e.g., electricity, fuel, and other oil or gas products) in 2022. Responses indicated that this percentage is often small, with energy products only accounting for 3% of total operating expenses for the typical (median) firm. However, one out of ten respondents indicated that their firm spent 14% or more of total expenses on energy products.

Taken at face value, these responses might suggest that the evolution of energy prices is of secondary importance to Swiss firms, since for most of them the direct share in expenditures is rather small. However, energy prices can be important via other channels, such as the cost of intermediary inputs, or they can affect the strength of demand for firms' products and services. To directly gauge the subjective importance of energy prices for their enterprise, respondents were asked to rate the importance of the following five factors, which we noted "may play a role in your costs or the demand for your products/services": (i) exchange rates (e.g. Swiss franc to euro); (ii) the general interest rate level in Switzerland; (iii) the general price level / inflation in Switzerland; (iv) energy costs; and (v) the evolution of average wages in Switzerland. The factors were shown in random order; we focus here in particular on the perceived importance of energy costs.

Overall, 54% of respondents stated that energy costs were rather or very important for their enterprise, while 30% stated that energy costs were rather or completely unimportant. Compared to other factors, energy prices are relatively less important than wage and price inflation (respectively 77% and 75% of firms consider those as very or rather important) and the interest rate (62%), but still more important than the exchange rate (42%).

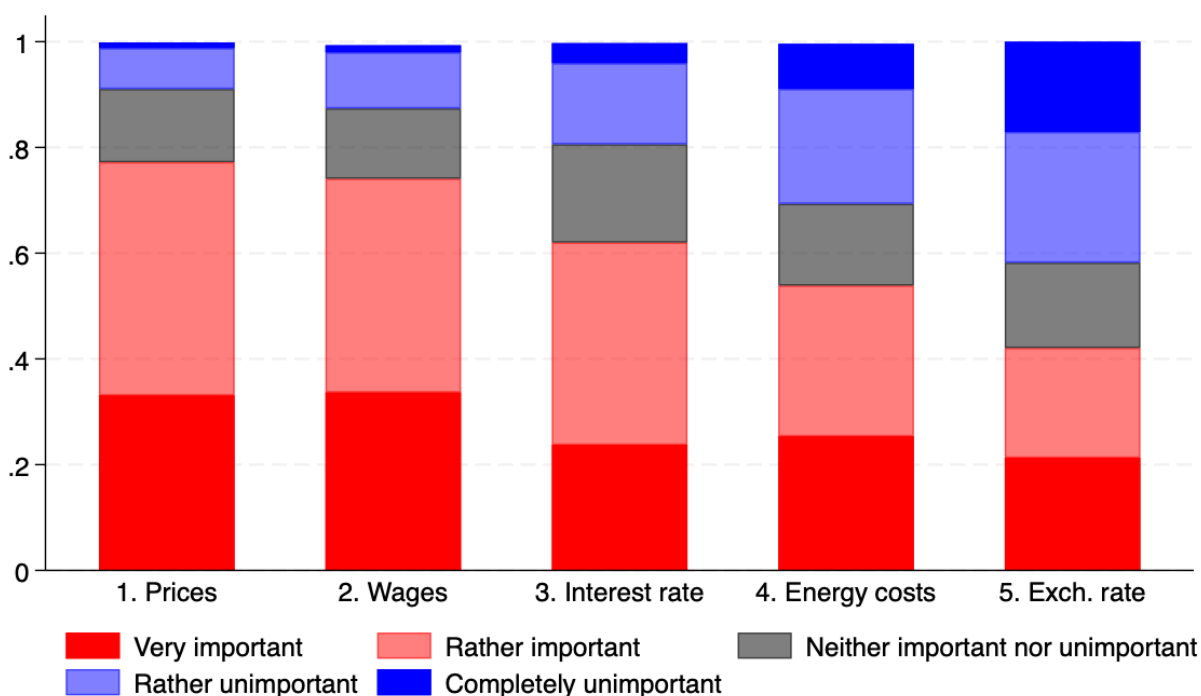


Figure 1: Importance of energy costs as compared to other factors as reported by Swiss managers

We performed an econometric analysis to understand these results. The cost structure plays a role, as we find that firms in the industry and construction sectors, and more generally firms with a higher energy cost share, typically consider energy costs to be more important. However, this still cannot explain why the majority of managers consider the energy costs to be important despite a low cost share. It could be because firms have low profit margins. Yet, we did not find that managers’ reported importance was robustly and significantly related to the firm’s profit margins. However, we found that it is strongly related to the reported intensity of competition in the sector where the firm operates.

We also asked firms about their recent experience with energy costs. The typical firm experienced a 10% rise in the past 12 months. However, energy costs changes were unequally distributed among firms, with one out of ten firms experiencing an increase of 40% or more. Interestingly, managers which have experienced a larger energy cost increase also reported a higher importance of energy costs, suggesting that the reported importance is related to managers’ recent experience and can evolve quickly. These firms are also more uncertain about future energy cost developments. Both the high price increase and the high uncertainty pose a direct threat to these firms’ future profitability and investment decisions.

CALL FOR ACTION

Managers do care about energy costs. Some firms are highly exposed to energy costs through their cost structure and because they operate in highly competitive markets, some have experienced very large energy cost increases. Surges in energy costs pose a direct threat to these firms’ investments through two channels. First, their internal funds may be drained by the increased costs. Second, these firms become more uncertain about future energy cost developments, which could reduce their demand for investment. Preventing this requires helping firms shield against this risk, for instance, through fair-priced derivative contracts. Better

insurance is especially appealing since energy cost changes are unequally distributed across firms.

Some managers care about energy costs beyond their firm's direct cost exposure. In this case, there is an externality and firms underinsure, which implies that policymakers should intervene more actively. We unfortunately do not know through which other channels (demand, labor costs, costs of intermediate goods, etc.) managers believe to be exposed. Policy recommendations will depend on the relative prevalence of these channels and on their distribution across firms. This is left for future research.

Our study has implications for the firms' green transition. From an environmental point of view, increases in energy prices may well be desirable from an aggregate perspective if this leads firms to become more energy-efficient, but rapid increases (and more broadly, heightened volatility) likely depress economic activity.

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