

Luxembourg Business Compass
Edition II/2009

LBC: slight recovery from **-2.1** to **-0.4**

January 2010

With the support of the Luxembourg Chamber of Commerce

Executive Summary

	April 2009	November 2009
LBC (in view of the next 6 months)	- 2.1	- 0.4
LBC (in view of the next 12 months)	- 1.4	+ 0.2

1. Economic expectations:

Less pessimistic, but no euphoria

2. Image as a business location:

Luxembourg's image remains very positive

3. The economic crisis:

More companies affected by the crisis. Entrepreneur's expectations more optimistic - albeit not when it comes to staffing

4. Companies' investment plans:

More money for introducing new products and for marketing and a Sales, less money for staff and for expanding existing facilities

5. Balancing the national budget:

Entrepreneurs advocate reducing too high administrative costs

6. Bureaucratic obstacles:

Too much bureaucracy in Luxembourg, authorities take too much time to process paperwork



Introduction

In April 2009, top decision-makers at the largest companies in Luxembourg, as defined by the number of employees, were interviewed for the first time within the framework of the "Luxembourg Business Compass." Using this instrument, the aim is to establish an economic indicator - for the first time ever - that can be employed to ascertain Luxembourg business leaders' expectations regarding the future economic trend in Luxembourg at regular intervals. The survey focuses particularly on how business leaders expect the Luxembourg economy will develop in the next six or, respectively, 12 months, along with their expectations and plans for their own companies. These core questions are supplemented by varying questions pertaining to business or politics.

The present report documents the findings of the second survey wave, which was just completed in October/November 2009, about a half a year following the first survey.

We would like to thank all respondents for their contribution. The next edition of the LBC is foreseen for Mai 2010.



Message by Mr Pierre Leyers

Our economy needs its own confidence-index

In the realm of economy, psychological factors count as much as facts and numbers.

Collective expectations influence economical trends and vice versa. That is the reason why surveys are so popular: by showing the statistical average of many opinions, they offer an objectivity which a single individual can never attain. Gauging the mood of the Luxembourg decision makers at regular intervals provides thus a precious navigational instrument. With the help of the coordinate system offered by the survey, an executive can see where he stands and – if necessary – adjust strategic decisions. Like fine wine, which gets better with age, the Luxembourg Business Compass Index improves its expressiveness with each new edition. Therefore, KPMG and the „Luxemburger Wort“ are strongly committed to establishing the LBC as a leading measuring instrument of the Luxembourg entrepreneur’s confidence. Given the openness of the national economy and its dependency on forces abroad, one might question the use of such an endeavour. Is it not enough to feel the pulse of the Eurozone in order to know at what pace the heart is beating in Luxembourg? The answer is no. The dependency on industrial exports and the heavy weight of the financial sector make the Luxembourg economy vulnerable, but also unique. Rarely a situation from abroad can be extrapolated to these national particularities. That is why our economy needs its own confidence-index.

The majority of entrepreneurs interviewed in November 2009 expect that it will take at least a year before the economy in Luxembourg starts recovering again. Put in a nutshell, the message extracted from this second survey wave says: „brighter, but no euphoria“. The real depth of the recovery will show itself with the results of the third wave, scheduled in spring. Let’s meet again in April this year!

Pierre Leyers
Financial Editor Luxemburger Wort



Message by Mr Pierre Gramegna

The use of a compass is vital for every sailor

The use of a compass pointing to the right direction is crucial, not to say vital, for every sailor. This proves to be all the more true when visibility is limited or when weather conditions are harsh. Forecast and prediction are key elements related to human survival instincts: we do generally dislike uncertainty and insecurity and, as a consequence, we try to reduce it accordingly.

Evidently, this figure of speech also fully applies to socio-economic matters. Economic science not only tries to understand broader socio-economic phenomena, but above all endeavours to forecast and to anticipate trends and to predict future developments. One major difficulty lies in the fact that various economic models at our disposal fall somewhat short of the human factors. Human behaviour, which may from time to time seem unpredictable, prevents economic science from being an exact one. This does not preclude economic research from being a decisive factor for the understanding of modern-day society. This equally applies to tools aiming at defining the most likely economic evolution in the short and medium run, which include qualitative surveys among entrepreneurs and business people in general.

In times when crisis seems to bottom out, it remains without doubt extremely difficult to forecast the economic future, even in the short term. In this context, the Luxembourg Business Compass helps in gathering opinions, challenges, concerns, and priorities of the Luxembourg economic decision-makers. By doing so, it truly becomes a compass, indicating certain trends inherent to the current experience, be it quantitatively or qualitatively speaking, of daily business life as well as of expectations and perspectives.

The Chamber of Commerce, whose members have been invited to take an active part in the survey, supports this initiative of KPMG and the Luxemburger Wort. Participation is a key investment, and not an additional administrative burden, as the results of the LBC do provide precious insights to businesses as well as to political leaders, employees, civil servants, students and other stakeholders.

Among its various assignments, the Chamber of Commerce is the national coordinator of several qualitative surveys on economic growth and competitiveness at international, European and national levels. Thus, the LBC initiative, which is updated bi-annually, is complementary to surveys and studies already being carried out among Luxembourg companies.

In this context, the Chamber of Commerce particularly wishes to point out the recently published Eurochambres survey, for which it is a key stakeholder and which involved over 750 Luxembourg companies and whose results largely corroborate those delivered by the current update of the LBC.

Indeed, via the Eurochambres survey, quite a few entrepreneurs have recently expressed a strong pessimism with regard to their anticipated 2009 business results in terms of turnover, investment activity, employment and evolution of the general business environment. According to the same survey, the 2010 forecasts are somewhat less pessimistic, thus confirming the relative improvement of a number of the LBC metrics. Having said this, companies remain really careful as far as their 2010 business outlook is concerned.

Moreover, both surveys deliver quite similar messages towards the authorities encouraging them to pursue their efforts in cutting red tape and administrative paperwork. The key challenge for Government is to enhance the attractiveness of the business environment and to restore competitiveness after several years of negative trend. The businessmen also point out a number of structural problems related to public finances and to the sustainability of the social security system, which need to be duly addressed and not postponed.

Pierre Gramegna
Director of the Luxembourg Chamber of Commerce

Findings

Less pessimistic but no euphoria

1. Economic expectations

The majority of entrepreneurs interviewed in October/November 2009 expect that it will take at least a year before the economy in Luxembourg starts recovering again. Only 9 percent expected the recovery process to start in the second half of 2009, whereas an additional 19 percent anticipate such a recovery in the first half of the year 2010. Most of the entrepreneurs interviewed, however, do not expect that the Luxembourg economy will start to recover before either the second half of 2010 (26 percent), 2011 (31 percent) or even later than that. Despite these restrained economic expectations, there are still signs of a more optimistic mood among respondents now than was the case in April 2009.

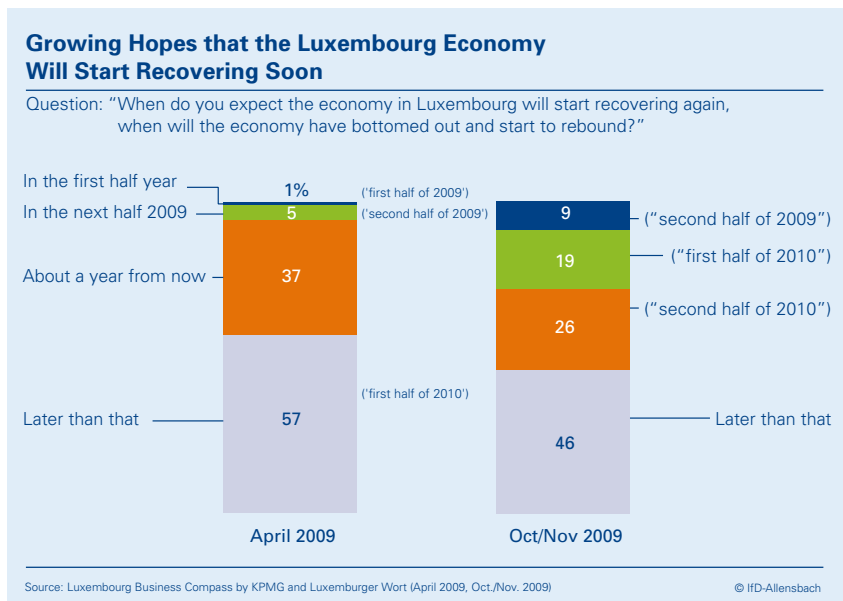


Figure 1

These findings are confirmed by a more differentiated question asking respondents to assess the future development of the Luxembourg economy using an 11-step scale ranging from '-5' ("economy will contract very strongly") to '+5' ("economy will grow very strongly"). In view of the next 6 months, the expectations measured indicate an average decline of -0.4. On average, therefore, the entrepreneurs surveyed anticipate a slightly negative economic trend in Luxembourg over the course of the next

6 months. In comparison with the value ascertained in April 2009, however, when the corresponding figure was -2.1, this indicator points in a clearly positive direction. With respect to the next 12 months, Luxembourg entrepreneurs even expect to see a slightly positive economic trend: here, the average indicator value is currently at +0.2, as compared to -1.4 in April 2009 (Figure 2). On the whole, these findings would appear to reflect the view that the economic crisis has now reached its worst point.

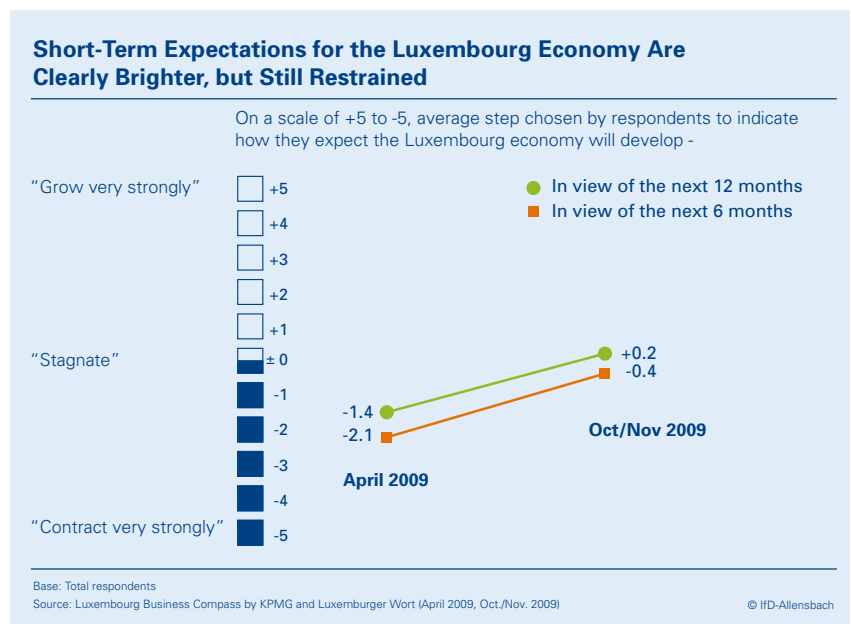


Figure 2

2. Image as a business location

Luxembourg's image remains very positive but has been tarnished by the crisis

Luxembourg continues to enjoy an excellent reputation as a business location: 63 percent of the top decision-makers interviewed assess Luxembourg's image from their own personal perspective as "good," while an additional 8 percent even say it is "very good". Nevertheless, the current economic crisis also seems to have had some impact in this regard. On comparing the findings of the second wave with the assessments given in April 2009 - when 18 percent described Luxembourg's image as "very good" and 65 percent as "good" - it would appear that skepticism is on the rise.

Compared to April 2009, more companies now feel affected by the crisis. Nevertheless, entrepreneurs' expectations for their own companies are becoming more optimistic - albeit not when it comes to staffing

3. The economic crisis

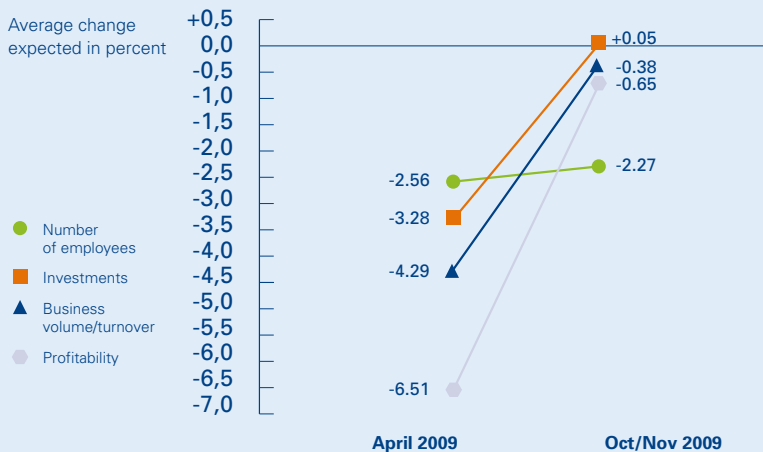
Companies tend to be feeling the impact of the economic crisis more strongly today than they did in April 2009. 59 percent of the decision-makers interviewed currently say that their company is affected by the global economic downturn either "very strongly" (13 percent) or "strongly" (46 percent). Half a year ago, the corresponding figure was only 47 percent.

Nevertheless, in comparison to the last survey, the business leaders interviewed are clearly more optimistic when it comes to some key economic indicators at their own companies. In this respect, however - as is the case with the economy as a whole - they do not expect to see any positive results within a short period of time. Hence, entrepreneurs anticipate a slight decline in business volume (-0.38 percent on average) and in profits (-0.65 percent) over the next six months. In contrast, they already expect a slight increase in investment volume (+0.05 percent). In April 2009, the values obtained for these indicators were clearly situated on the negative side of the spectrum: investment volume was expected to decline by an average of 3.28 percent, turnover by 4.29 percent, and profitability by as much as 6.51 percent.

When it comes to the number of employees, however, there are hardly any signs of optimism. Here, expectations have remained practically unchanged since April 2009, at a clearly negative level (-2.27 percent, Figure 3). This finding gives us reason to fear that the crisis has not yet fully impacted the labor market and that further job losses may still lie ahead.

Clearly Improved Expectations among Luxembourg Entrepreneurs Regarding Profitability, Turnover and Investments - Yet Pessimism Remains When It Comes to the Number of Employees

Question: "How do you expect the following areas or indicators will develop at your Luxembourg company over the next 6 months?"



Source: Luxembourg Business Compass by KPMG and Luxemburger Wort (April 2009, Oct./Nov. 2009)

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Figure 3

More money for introducing new products and for marketing and sales, less money for staff and for expanding existing facilities

4. Companies' investment plans

In the coming 6 months, the largest Luxembourg companies primarily plan to increase their expenditures for introducing new products and for marketing and sales. Other areas that are most likely to increase are expenditures for information technology and for training. The companies are most likely to plan to limit expenditures in the areas of advertising, staff and expanding existing facilities. In the remaining areas, the majority of respondents do not anticipate any changes in the level of expenditures (Figure 4).

On comparing the findings of this second survey wave with the plans ascertained in April 2009, the higher budgets anticipated for introducing new products and for marketing and sales are especially striking.

In addition, planned expenditures for training and continuing professional training also show a positive trend. In contrast, plans for staffing expenditures remain negative on balance, although the share of companies that are planning to decrease staffing expenditures is not quite as pronounced now as it was in April 2009.

When it comes to expenditures for company expansion - be it in the form of geographic expansion, acquisitions of other businesses or expanding existing facilities - companies tend to be showing more budgetary restraint compared to six months ago.

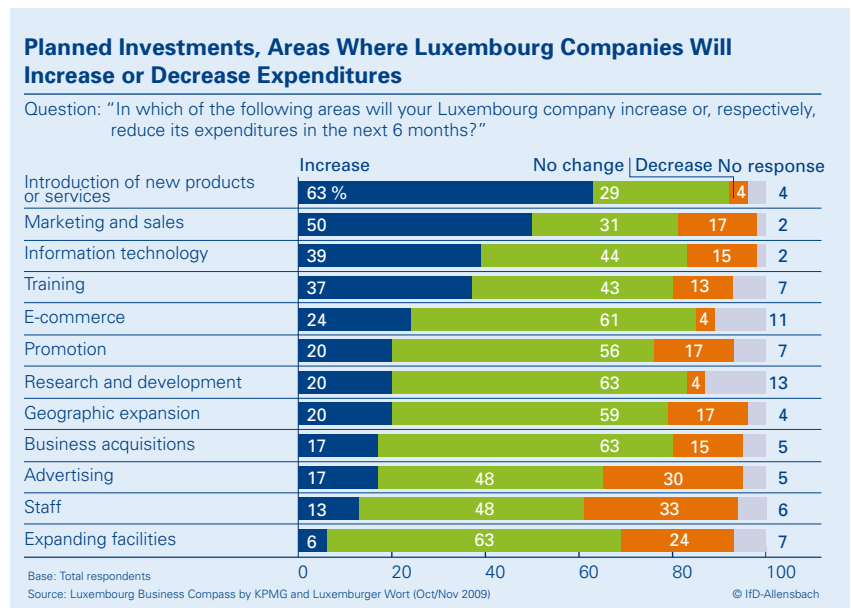


Figure 4

The most important foreign markets for Luxembourg businesses (3 possible answers) are Luxembourg's neighboring countries: Germany (46 percent), Belgium (26 percent, along with 4 percent for Benelux) and France (26 percent). Europe or, respectively, the European Union, is cited by 20 percent of the entrepreneurs interviewed, along with 6 percent who expressly cite Eastern Europe and an additional 4 percent who cite Western Europe. About one out of six entrepreneurs count Great Britain or, the United States among their most important foreign markets (17 percent each).

5. Balancing the national budget

Entrepreneurs advocate reducing administrative costs, which they believe are too high

To balance the Luxembourg national budget in the near future, almost all of the entrepreneurs interviewed advocate reducing administrative costs (93 percent). In contrast, only about one out of six business leaders favor raising taxes or, respectively, reducing the economic stimulus package (17 percent each). Practically no Luxembourg entrepreneurs support the idea that there is no need to take any action, since future economic growth will balance out current budget deficits on its own (6 percent).

There is a clear gap between those measures favored by business leaders and the measures that they expect the government will actually implement in order to balance the budget. Only entrepreneurs 50 percent of expect that the government will reduce administrative costs, whereas about one third of all respondents expect the government will raise taxes or, respectively, reduce the economic stimulus package (35 percent or, respectively, 33 percent). And the share of respondents who assume the government will take no action at all in this respect, but will instead wait for the budget problem to resolve itself via future economic growth, is as high as 19 percent (Figure 5).

The fact that practically all entrepreneurs interviewed support reducing administrative costs is understandable given that the vast majority also believes that these costs are too high in Luxembourg. Over three quarters of entrepreneurs are convinced that the government could save more in this respect (76 percent). Only 20 percent believe the current costs are appropriate and none of the top decision-makers interviewed believes that the government is already saving too much.

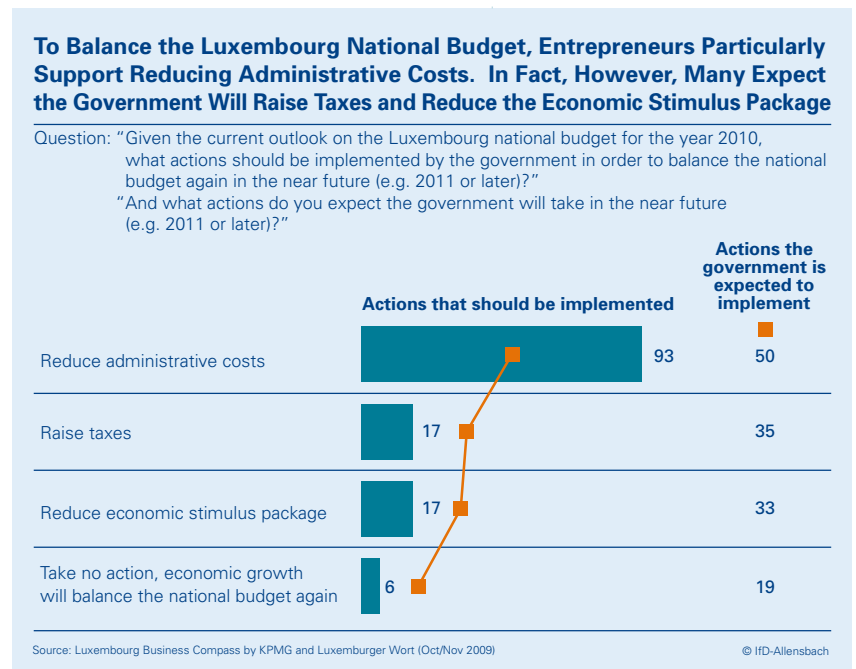


Figure 5

6. Bureaucratic obstacles

Many entrepreneurs complain that there is too much bureaucracy in Luxembourg, particularly emphasizing that the authorities take too much time to process paperwork

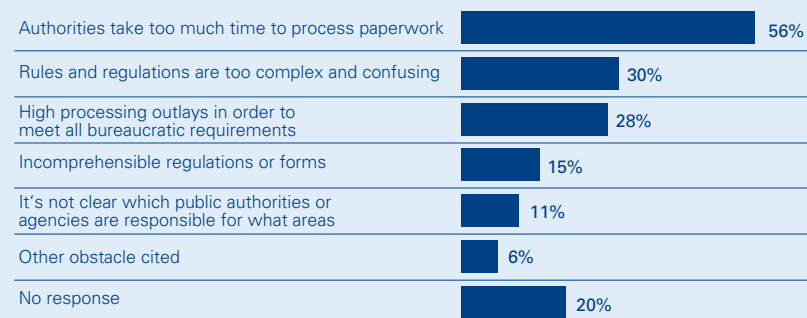
When it comes to public administration, however, many entrepreneurs criticize more than just what they view as inflated administrative costs.

About two thirds of major Luxembourg companies state that their business operations are “often” (11 percent) or “occasionally” (54 percent) unduly impeded by the public authorities and by bureaucratic rules and regulations. Only 4 percent of the companies report that this is “never” the case.

The most frequent complaint in this regard is that the authorities take too much time to process paperwork (56 percent). This is followed by the complaint that rules and regulations are too complex and confusing (30 percent), along with the high outlays entailed in meeting all bureaucratic requirements (28 percent). In comparison, relatively few entrepreneurs cite incomprehensible regulations or forms (15 percent) or confusion as to which public authorities are responsible for what areas (11 percent, Figure 6).

When It Comes to Bureaucratic Obstacles, Entrepreneurs Mainly Complain about the Amount of Time the Authorities Need to Process Paperwork

Question: “And what are the main administrative obstacles for your Luxembourg business?”



Source: Luxembourg Business Compass by KPMG and Luxemburger Wort (Oct/Nov 2009)

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Figure 6

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