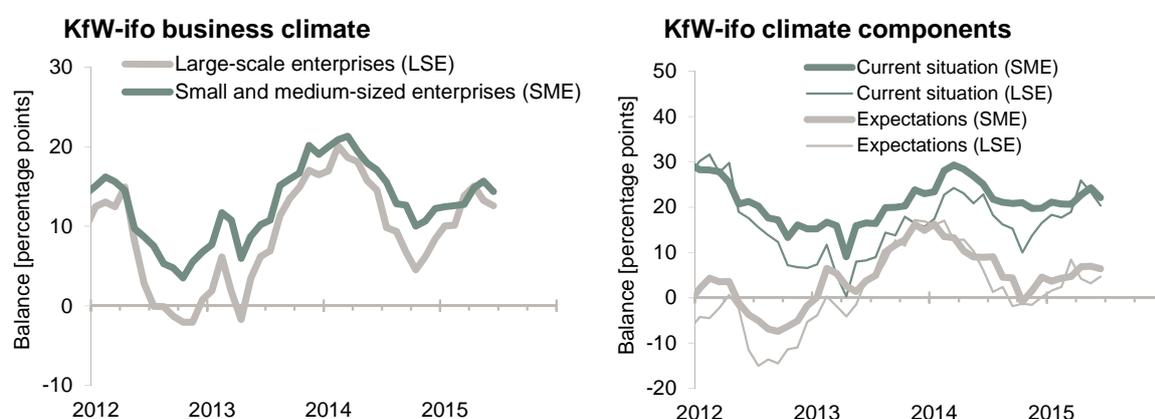


KfW-ifo SME Barometer: June 2015

Unease in Europe causes disquiet in SME sector

- *Situation assessments and expectations in SME sector fall*
- *Decline in sentiment, especially in export-sensitive segments*
- *However, large enterprises rather more confident*



Source: KfW Research, ifo Institute Munich

SME business climate clouding over

European unease surrounding the seemingly endless negotiation drama with Greece has left its mark. The German SME sector looks anxious and has made a distinctly tentative start to the summer. Its business climate index fell 1.3 points in June to 14.4, surrendering virtually half the gains it had made in the previous two months. Both components are in negative territory:

- The current business situation assessment figures fell 2.1 points in June to 22.1. Despite this setback, situation assessments in the second quarter were, on average, still somewhat better than those in the first quarter: an indication of solid economic growth in the spring.

- At the same time, however, SME managers felt the outlook was a little gloomier, with their expectations falling 0.5 points to 6.4. Given the rather sluggish momentum in key emerging economies such as China and the unresolved problems in the euro area, it is entirely realistic for them to rein in their confidence levels; this should protect them from any future disappointments that may come along.

Gloomy sentiment concentrated in SME industrial and wholesale segments

A look at individual segments shows that the deterioration in sentiment in the SME sector can be exclusively traced back to the much gloomier climate afflicting the manufacturing industry and wholesale segments – a strong indicator, in our view, that the deterioration can be attributed principally to the European and international environments. These, after all, are the segments of the economy that tend to be most export-sensitive. In contrast, the business climate indicator for the SME retail segment - already at a very high level - made some further slight gains (up 0.1 points to 21.2), while the construction segment even managed to record strong gains (up 2.7 points to 21.3). The two segments linked most directly to the domestic economy thus led June's sentiment "league" by a substantial margin, providing further evidence that domestic demand is healthy.

Large enterprises: expectations slightly better but distinct deterioration in business situation

Although the business climate figures for large enterprises were down slightly in June, the decline remained within reasonable limits (-0.7 points to 12.6 points). Indeed, large enterprises also assessed their current situation as distinctly worse (down 3.0 points to 20.3). Nonetheless, and in contrast to their small and mid-sized counterparts, large companies were rather more optimistic than they had been the previous month. Their expectations rose 1.4 points to 4.6, thus compensating, to some extent, for the decline in their situation assessments – hopeful, no doubt, that the global economy will be able to gain some momentum over the rest of the year now that the US has managed to get out of the economic starting blocks. Furthermore, the devaluation of the euro still has an impact. Given that small and mid-sized companies involved in cross-border business tend to focus more on business opportunities closer to home, the continuing uncertainty regarding which countries will be part of the euro area in future and the economic consequences of an escalation of the Greek crisis are sufficient reason in themselves for expectations to have clouded over somewhat.

Decent growth in second quarter but outlook more uncertain

We expect Germany's real growth figure for the current year to come out at a perfectly acceptable 1.5%. June's cloudy skies are unlikely to affect this in any way. Quite the reverse, in fact – we believe our relatively cautious forecast is substantially on track. Looking back, we believe Germany will have achieved a decent level of growth in the second quarter, as suggested by the overall rise in situation assessments across all economic sectors. However, Greece's de facto default on its repayments to the IMF together with the difficult negotiations ahead following the "No" vote in the referendum mean that the outlook for both Europe and Germany is increasingly uncertain. Up to now, companies and financial markets have reacted in a reasonably relaxed manner, trusting in established stabilisation mechanisms such as

the ESM and the support policy pursued by the ECB. However, these are no longer a given. What will be decisive from the point of view of the economy is whether companies, notwithstanding the current unease, will lose their recently won courage to invest. When all is said and done, conditions are good. Consumption is buzzing, interest rates are low and the major economies in the euro area, at least, are back on track to achieve growth.

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Attachment: SME business climate in figures

KfW-ifo SME Barometer

| Balance [Percentage points]* | | Month/Year | | | | | | | m-o-m | y-o-y | 3m-o-3m |
|---------------------------------|-----|------------|--------|--------|--------|--------|--------|--------|-------|-------|---------|
| | | Jun/14 | Jan/15 | Feb/15 | Mrz/15 | Apr/15 | Mai/15 | Jun/15 | | | |
| Business climate | | | | | | | | | | | |
| Manufacturing | SME | 14.7 | 10.0 | 10.7 | 11.8 | 13.2 | 13.6 | 11.3 | -2.3 | -3.4 | 1.8 |
| | LSE | 14.4 | 10.7 | 10.8 | 15.0 | 15.5 | 13.2 | 11.8 | -1.4 | -2.6 | 1.3 |
| Construction | SME | 20.2 | 19.3 | 18.3 | 15.9 | 17.5 | 18.6 | 21.3 | 2.7 | 1.1 | 1.3 |
| | LSE | 16.8 | 8.2 | 11.9 | 12.4 | 22.1 | 17.8 | 15.0 | -2.8 | -1.8 | 7.5 |
| Retail trade | SME | 21.2 | 18.3 | 16.5 | 18.0 | 18.7 | 21.1 | 21.2 | 0.1 | 0.0 | 2.8 |
| | LSE | 7.6 | 4.2 | 4.8 | 9.8 | 8.1 | 9.9 | 6.8 | -3.1 | -0.8 | 2.0 |
| Wholesale trade | SME | 25.1 | 14.3 | 10.5 | 9.5 | 14.7 | 16.8 | 12.5 | -4.3 | -12.6 | 3.3 |
| | LSE | 18.6 | 11.7 | 10.8 | 13.1 | 16.9 | 13.5 | 17.7 | 4.2 | -0.9 | 4.2 |
| All economic sectors | SME | 17.1 | 12.4 | 12.6 | 12.7 | 14.8 | 15.7 | 14.4 | -1.3 | -2.7 | 2.4 |
| | LSE | 14.5 | 10.0 | 10.1 | 13.8 | 15.0 | 13.3 | 12.6 | -0.7 | -1.9 | 2.3 |
| Current situation | SME | 25.1 | 21.1 | 20.7 | 20.6 | 22.7 | 24.2 | 22.1 | -2.1 | -3.0 | 2.2 |
| | LSE | 22.8 | 18.3 | 17.7 | 18.9 | 25.9 | 23.3 | 20.3 | -3.0 | -2.5 | 4.9 |
| Expectations | SME | 8.9 | 3.6 | 4.3 | 4.7 | 6.8 | 6.9 | 6.4 | -0.5 | -2.5 | 2.5 |
| | LSE | 6.0 | 1.6 | 2.4 | 8.4 | 4.2 | 3.2 | 4.6 | 1.4 | -1.4 | -0.1 |
| West Germany | SME | 17.6 | 13.1 | 12.8 | 13.0 | 15.0 | 16.8 | 15.3 | -1.5 | -2.3 | 2.8 |
| | LSE | 14.2 | 9.8 | 10.0 | 13.6 | 15.2 | 13.1 | 12.7 | -0.4 | -1.5 | 2.5 |
| East Germany | SME | 14.2 | 9.0 | 11.7 | 11.4 | 14.0 | 8.4 | 8.4 | 0.0 | -5.8 | -0.4 |
| | LSE | 21.1 | 15.0 | 13.8 | 18.4 | 10.6 | 17.1 | 9.7 | -7.4 | -11.4 | -3.3 |
| Employment expectations | SME | 6.0 | 5.8 | 5.6 | 5.3 | 6.0 | 6.6 | 5.9 | -0.7 | -0.1 | 0.6 |
| | LSE | 8.9 | 8.5 | 8.5 | 9.7 | 10.9 | 9.2 | 10.0 | 0.8 | 1.1 | 1.2 |
| Sales price expectations | SME | -2.3 | -3.4 | -2.1 | -2.2 | -0.9 | 0.8 | -0.6 | -1.4 | 1.7 | 2.3 |
| | LSE | -4.6 | -9.5 | -6.2 | -4.6 | -3.0 | -3.4 | -2.5 | 0.9 | 2.1 | 3.8 |

Explanations and abbreviations:

Differences due to rounding possible, Sources: KfW, ifo

* Seasonally and mean adjusted (long-term mean since January 1991 = 0)

S(mall and) **M**(edium-sized) **E**(nterprises)

L(arge-) **S**cale **E**(nterprises)

Change in percentage points **m**(onth)-**o**(ver)-**m**(onth)

Change in percentage points **y**(ear)-**o**(ver)-**y**(ear)

Change in percentage points **3 m**(onths period)-**o**(ver)-**3 m**(onths period)

Revisions relative to previous publications may occur due to seasonal and mean adjustment as well as rounding.

Construction and interpretation of the KfW-ifo SME Barometer. The KfW-ifo SME Barometer indicator family is based on a scale-of-enterprise evaluation of the well-known ifo business climate index for which about 7,000 enterprises from trade and industry (manufacturing, construction, wholesale and retail trades) from western and eastern Germany are polled every month on current and future business, including around 5,600 SMEs. Enterprises are generally classed as small to medium-sized if they employ a workforce of not more than 500 and record an annual turnover not exceeding EUR 50 million. For a more accurate analysis, however, these quantitative limits have to be drawn more narrowly for retail trade (maximum annual turnover of EUR 12.5 million) and the construction industry (up to 200 employees). All enterprises that exceed at least one of these thresholds are classed as large-scale enterprises. The KfW-ifo SME Barometer reports the balance of current business assessments (percentage of positive answers less percentage of negative answers), the balance of business expectations for the next six months, ascertained in a similar way, and the inferred mean average value for the business climate. Moreover, the enterprises' employment and domestic sales price expectations are also expressed as balance figures. All time series are seasonally and mean adjusted. The zero line therefore marks the long-term 'cycle-neutral' average. Indicators above (or below) zero point to an above average or favourable (below average or negative) business situation.