Frankfurt, 3rd August 2015

KfW-ifo SME Barometer: July 2015

German SME business climate climbs to annual high

- *Breathing a sigh of relief after tension eases over reform dispute with Greece*
- *Business assessments improve significantly, expectations slightly*
- *Sentiment picks up among large enterprises as well*

SME business climate resumes upward trend

In a last-ditch attempt, Greece has agreed with its European partners to start negotiations on a third bailout package. This is also a relief for German SMEs. After falling in the previous month, their business climate is resuming the positive trend that started in autumn of last year, climbing by 2.6 points in July to reach 17.1 balance points. This is the highest level in thirteen months. Both components of the indicator are on the up:

- The assessment of the current business situation has improved by a strong 4.1 points to 26.4 balance points. The start of the third quarter thus rides on upbeat sentiment, which gives hope that economic momentum will pick up in the summer.
- Expectations have risen by 1.3 points to 7.8 balance points. Now that the Grexit risk has subsided, SMEs are now shifting their focus to the positive economic drivers such as the labour market and the euro exchange rate. The nuclear deal with Iran is also good news for the German economy.

Source: KfW Research, ifo Institute Munich
Sentiment improves across the board

A glance across the various sectors shows that the upbeat mood among SMEs builds on a broad base. It is particularly pronounced in manufacturing and wholesale – the export-sensitive sectors, which had still reported a noticeable business climate deterioration in June as a reaction to the acute escalation of the Greek crisis. They more than reversed this decline in July. What is also impressive, however, is the renewed, tangible improvement in retail sentiment, which reached the highest level since March 2011. Private consumption remains strong. Only in the SME construction sector did sentiment decline somewhat, although it continues on a very high level in a long-term comparison.

Large enterprises are also more confident

Business sentiment among large companies has even improved across all sectors, including construction. The sentiment indicator for large companies rose by 2.4 points to 15.0 balance points overall and, as was experienced among SMEs, business assessments improved more strongly (+4.2 points to 24.7 balance points) than business expectations (+0.6 points to 5.2 balance points). The muted improvement in expectations among both large companies and SMEs is probably due primarily to the international environment. In contrast to the reliable impetus coming from domestic demand, there is currently little momentum in the global economy, with global trade even slowing since the beginning of the year. Emerging economies are facing structural adjustments, particularly China, where growth rates are expected to be lower in the long term. It is encouraging, however, that the recovery in the major euro area countries is solidifying and the US economy is gradually picking up steam after a bungled start to the year.

Germany's upswing continues

The key message of the July KfW-ifo SME Barometer is that the German economy has proven to be resilient in a sometimes difficult international environment. As the tension over the Greek debt drama has eased, private consumption is soaring and the recovery of capital formation in Germany approaches, it is predominantly the restrained growth prospects of the emerging economies that prevent an even more dynamic rise in sentiment. On balance, the German upswing is on a path towards real growth of at least 1.5% this year.

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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.