

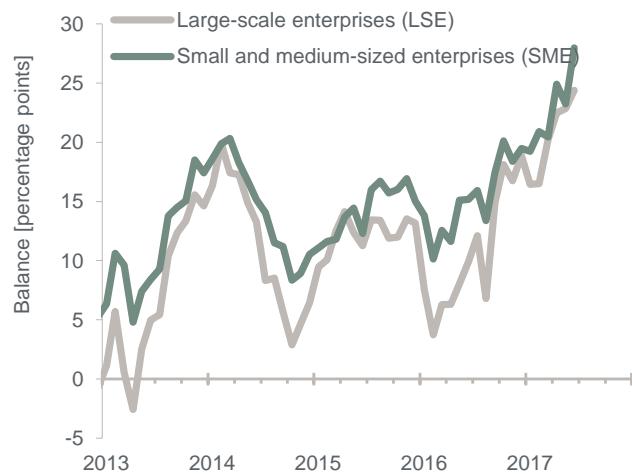
» Soaring confidence in a roaring economy

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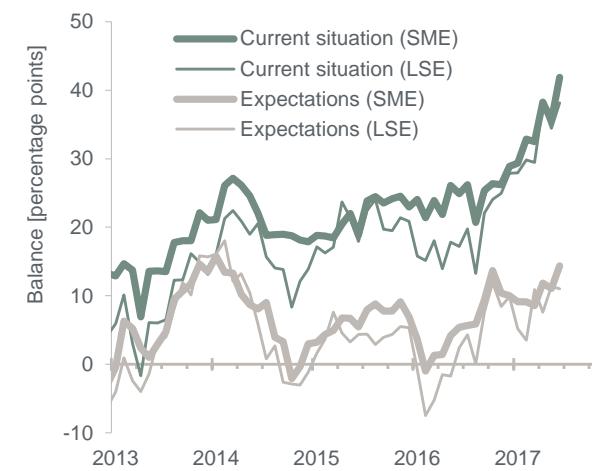
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- SME business climate leaps to new all-time high
- SMEs' expectations and, above all, situation assessments have risen strongly
- Large enterprises are just slightly less optimistic
- Euphoric sentiment overdraws what is nevertheless a strong business cycle

KfW-ifo business climate



KfW-ifo climate components



Source: KfW, ifo

Business climate rises to new record level

Confidence on the executive floors of small and medium-sized enterprises is booming. In June the business climate rose by a distinctive 4.8 points – nearly two and a half times the usual monthly variation – to now 28.0 balance points. That makes it the second time in only three months that confidence in Germany has climbed to new post-unification record highs. Both components contributed strong increases to the upbeat mood in the SME sector.

- Business expectations are on levels not seen in the last three and a half years; they improved by 3.4 points to 14.4 balance points. This probably reflects both the global economic recovery and the fading political risks in Europe after the French election.
- This surge in optimism is nevertheless astonishing because the basis on which expectations are formed – the assessment of the business situation – at the same time made a giant leap of 6.2 points to the unprecedented level of 41.8 balance points. Businesses are therefore expecting the current peak level to rise even further. That increases the risk of disappointment.

Situation assessments boost confidence among large enterprises

Large enterprises presented themselves very upbeat in June as well, although business confidence improved much more moderately month-on-month than among SMEs, rising by 1.6 points to 24.4 balance points. Essentially, this reflects a slightly less euphoric outlook on the future. While situation assessments improved noticeably (up 3.6 points to 38.1 balance points), business expectations were down slightly (-0.4 points to 11.0 balance points). That may be an expression of the continuing uncertainties in the relationship with the USA and the UK. These uncertainties are set to remain for some time to come and make large exporters in particular anxious.

Second wind for domestic demand

Domestic demand in Germany, which has been growing reliably for some years now, is currently getting its second wind. The most recent oil price decline, combined with a moderate appreciation of the euro, is bolstering consumers' purchasing power while employment growth is continuing with high momentum. Enterprises' hiring plans, which have been on a very high level for a long time already, underscore

the solid condition of the labour market. In June they were up by a very strong 3.7 points on May for SMEs and reached 19.0 balance points – another all-time high. This provides a fundamentally excellent outlook for private consumption, also reflected in significant improvements in the business climate of retailers and wholesalers in June. The top margin of the increases is marked by SME wholesalers, which reached a highly unusual month-on-month increase of 12.1 points – to now 32.9 balance points. But climate indicators also showed extraordinarily strong increases among retailers of both size classes. In the construction industry, confidence remains on a record level among SMEs and just slightly lower among large enterprises, after slipping slightly from May – the only drop in a sub-indicator of the business climate this month. The construction boom in Germany is not set to end anytime soon. The very strong improvement in sentiment among industrial SMEs (+4.1 points to 25.9 balance points) and a rather moderate one among large manufacturers (+0.7 points to 25.1 balance points) rounds off the positive profile of sectors.

Outlook remains ‘merely’ good for the time being

Expressed in a simple formula, the finding of the KfW-ifo SME Barometer in June is that German businesses are booming with confidence across all sectors with no exceptions. This shows that the upswing rests on a broad foundation. The hard monthly cyclical indicators such as industrial output, incoming orders and exports, however, so far have not been able to impress with top results. One reason for the discrepancy may be that businesses rated their business climate quite positively already in the winter half even though the further destabilisation of the euro area was hanging over the economy like a sword of Damocles. These economic risks have since faded substantially, which appears to have motivated firms to issue an even better assessment. All in all, we expect quarterly GDP to have grown at roughly the same rate in the spring quarter as in the first quarter (+0.6 %). That means our ‘merely’ good cyclical outlook for Germany of 1.6 % for both 2017 and 2018 remains on track. However, the risks to our forecast are mounting increasingly on the upside. ■

Annex: SME business cycle in figures

KfW-ifo SME Barometer

Balance [Percentage points]*		Month/Year							m-o-m	y-o-y	3m-o-3m
		Jun/16	Jan/17	Feb/17	Mrz/17	Apr/17	Mai/17	Jun/17			
Business climate											
Manufacturing	SME	9.2	15.7	18.2	17.6	22.3	21.8	25.9	4.1	16.7	6.2
	LSE	6.4	16.6	17.6	22.4	21.4	24.4	25.1	0.7	18.7	4.8
Construction	SME	25.9	30.2	29.3	29.7	31.3	31.8	33.7	1.9	7.8	2.5
	LSE	27.3	37.4	26.0	37.1	38.6	39.8	37.5	-2.3	10.2	5.2
Retail trade	SME	21.7	18.3	20.2	18.2	26.1	19.0	25.4	6.4	3.7	4.6
	LSE	5.1	4.8	1.3	4.0	18.3	10.1	17.4	7.3	12.3	11.9
Wholesale trade	SME	21.8	23.6	25.0	22.4	27.6	20.8	32.9	12.1	11.1	3.4
	LSE	22.7	21.0	22.5	20.3	25.9	23.2	24.8	1.6	2.1	3.4
All economic sectors	SME	15.2	19.2	20.9	20.4	24.9	23.2	28.0	4.8	12.8	5.2
	LSE	9.9	16.5	16.5	20.2	22.5	22.8	24.4	1.6	14.5	5.5
Current situation	SME	24.9	29.3	32.8	32.5	38.3	35.6	41.8	6.2	16.9	7.0
	LSE	17.2	27.9	29.8	29.5	37.9	34.5	38.1	3.6	20.9	7.8
Expectations	SME	5.4	9.1	9.1	8.5	11.8	11.0	14.4	3.4	9.0	3.5
	LSE	2.4	5.2	3.5	10.9	7.6	11.4	11.0	-0.4	8.6	3.5
West Germany	SME	15.7	19.8	22.1	21.2	25.9	23.9	28.6	4.7	12.9	5.1
	LSE	10.0	16.8	16.4	20.6	22.7	22.8	24.8	2.0	14.8	5.5
East Germany	SME	12.4	15.7	13.2	15.9	18.9	19.0	24.0	5.0	11.6	5.7
	LSE	6.8	9.3	17.9	11.9	17.9	23.7	15.0	-8.7	8.2	5.8
Employment expectations	SME	9.5	12.1	14.4	13.7	16.9	15.3	19.0	3.7	9.5	3.7
	LSE	11.2	16.5	17.5	14.2	17.6	18.9	18.0	-0.9	6.8	2.1
Sales price expectations	SME	-1.4	7.2	8.5	9.7	9.8	10.1	8.1	-2.0	9.5	0.9
	LSE	-0.8	5.3	7.0	6.2	2.3	3.4	2.1	-1.3	2.9	-3.6

Difference due to rounding possible, Source: KfW, ifo

Explanations and abbreviations:

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

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

L(arge-)Scale 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 adjustments 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 building 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.