

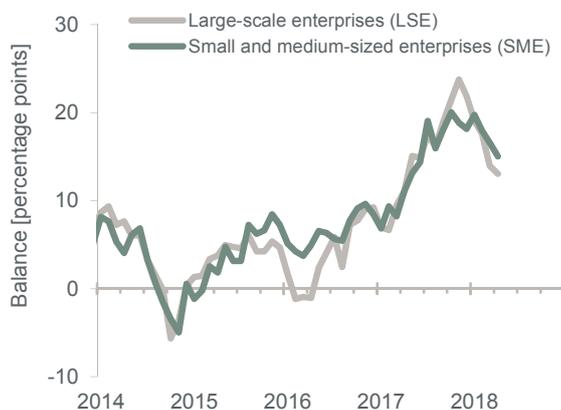
## »» Reformed business climate indicator confirms continuing decline in sentiment

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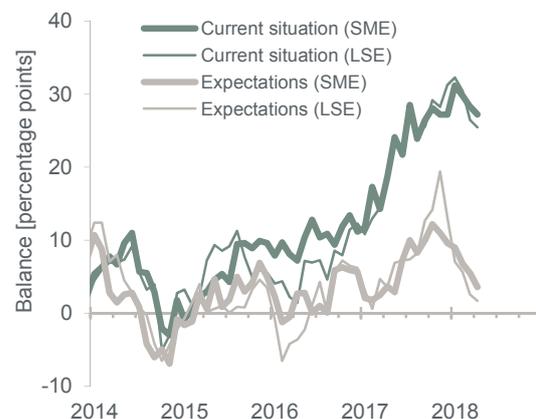
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- KfW-ifo SME Barometer now includes services and export expectations
- SMEs' situation assessments and business expectations are down
- Large enterprises are particularly concerned over protectionism
- Upswing is slowing down but remains robust

### KfW-ifo business climate



### KfW-ifo climate components



Source: KfW Research, ifo Institute

### New barometer with the same message

Confidence continued to drop across broad sections of the German economy in April. That is the core message of the debut edition of the fundamentally revised KfW-ifo SME Barometer. Along with export expectations, the inclusion of the service sector is the most important new feature of the first conceptual reform to the barometer since it was first published in December 2004. Business confidence among SMEs fell by 1.5 points to 15.0 balance points, the third consecutive drop which confirms the downward trend that has set in. Both components were down:

- Situation assessments fell by a moderate 1.1 points to now 27.2 balance points. Historically, this is still a very good level, not far below the all-time high of January (31.2 balance points).
- Expectations were down 1.9 points in April, the sixth monthly decline in a row. At 3.6 balance points, business expectations were only slightly above the long-term average since the start of the revised time series in January 2005.

### Downward trend among large enterprises is more pronounced

Confidence among large enterprises has dropped significantly more sharply in the past half-year than among SMEs. After the slightly more moderate recent declines in situation assessments (-1.0 points to 25.4 balance points), business expectations (-0.9 points to 1.7 balance points) and, thus, overall business confidence (-0.9 points to 13.1 balance points), the negative gap to small and medium-sized enterprises narrowed again to around two points in April. As recently as in November, however, confidence among large enterprises was five points higher than in SMEs, mostly because of the clearly more optimistic business expectations of large enterprises.

### Hope and concern over global trade

In this rollercoaster ride, hope and apprehension over global trade, which is particularly important for large export-oriented firms, probably play a dominant role. Around the turn of the year, the prevailing notion was that the global business cycle and with it global trade was picking up noticeably while the protectionist tone of the US administration that had already been perceptible for some time appeared to be a placebo primarily directed at a domestic audience. Perceptions have

changed considerably with the introduction of specific punitive tariffs on steel and aluminium, from which the EU is exempted temporarily until 1 June, and the growing tension between the US and China over trade policy. There is growing fear of a global trade war, while at the same time the declining export figures for January and February were disappointing. This is consistent with the fact that manufacturing and wholesale, the two sectors most closely linked to global trade, have recorded the strongest downturn in sentiment since last winter – a trend that has continued until now with at times significant declines in confidence. At the same time, manufacturers' export expectations have dropped sharply from their multi-year highs in autumn, although they stabilised slightly in April (SMEs: unchanged at 3.0 balance points; large enterprises: +2.0 points to 6.9 balance points). Confidence in the services sector dropped further but remains on a high level (SMEs: -3.3 points to 12.6 balance points, large enterprises: -0.9 points to 17.7 balance points). The important segment of business services in particular is unlikely to remain unaffected from the downward trend in manufacturing.

### **Positive signals from construction and retail**

On the other hand, construction and retail, the two sectors primarily focused on the domestic economy, are sending out positive signals. In these two sectors, business confidence rose in April – both in SMEs and in large enterprises. Construction posted by far the highest confidence levels in both size classes and remains a mainstay of the business cycle. The recovery in the retail sector gives reason to hope that the most recent phase of weakness in private consumption was a temporary outlier. The main drivers of vigorous consumption – employment growth, rising real wages and a significant increase in pension payouts from the middle of the year – remain intact in any case.

### **Confidence levels and business cycle have passed their peak**

On balance, the April findings of the revamped KfW-ifo SME Barometer are neither cause for excessive pessimism nor uncritical optimism. The economy has passed its cyclical peak and it appears doubtful whether last year's very high average quarterly GDP growth rates of a good 0.7% can be reached again in the short term. After the most recent disappointing industrial output, retail turnover and export figures, it is primarily the first quarter that will likely fail to meet the previously high expectations and the annual growth rate will reflect this in purely arithmetic terms. That means a considerable downward risk for our previous growth forecast of 2.5% for this year. Nevertheless, we remain optimistic that the upswing will merely slow down but not come to an end. The year 2018 is likely to show very decent real growth that will be clearly above the potential rate. In addition to reliable robust domestic demand, the still good to very good sentiment across the breadth of enterprises speaks in favour of this: All indicators of the KfW-ifo SME Barometer have continued on positive to very positive levels despite the declines in the past months. In other words, they are significantly higher than the historic average in most cases. During the course of the year 2017, business confidence had climbed to previously unprecedented levels and was thus removed to some extent from the cyclical reality – one that was certainly very good but not unique. Seen in this light, the most recent corrections show a return to more realistic, down-to-earth sentiment. That is not the same as fear of imminent recession. A continuation of the upturn will crucially depend on whether the threat of protectionism can be effectively contained together with European and international partners before fears of new trade barriers begin to weigh more strongly on businesses' willingness to invest. ■

# KfW Research

## KfW-ifo SME Barometer: April 2018

### KfW-ifo SME Barometer in figures

Balance [Percentage points]*		Month/Year							m-o-m	y-o-y	3m-o-3m
		Apr/17	Nov/17	Dec/17	Jan/18	Feb/18	Mar/18	Apr/18			
<b>Business climate</b>											
Manufacturing	SME	12.4	19.8	19.6	20.4	17.8	15.6	12.8	-2.8	0.4	-4.5
	LSE	14.8	28.3	23.9	24.1	19.6	17.5	13.4	-4.1	-1.4	-8.6
Construction	SME	21.7	26.4	27.1	27.2	24.7	28.2	29.9	1.7	8.2	0.7
	LSE	24.5	27.8	31.2	28.0	27.1	23.8	27.8	4.0	3.3	-2.8
Retail trade	SME	18.0	15.6	16.3	17.1	16.4	10.0	11.3	1.3	-6.7	-3.8
	LSE	10.1	4.6	12.2	5.9	4.9	-2.5	1.3	3.8	-8.8	-6.3
Wholesale trade	SME	16.5	18.7	19.9	16.6	19.7	15.5	5.6	-9.9	-10.9	-4.8
	LSE	16.3	18.6	16.9	16.3	15.2	9.2	5.8	-3.4	-10.5	-7.2
Services	SME	7.0	17.1	15.5	18.6	15.9	15.9	12.6	-3.3	5.6	-2.3
	LSE	8.2	23.0	22.6	17.7	20.2	18.6	17.7	-0.9	9.5	-2.3
<b>Germany</b>	<b>SME</b>	<b>11.0</b>	<b>18.8</b>	<b>18.1</b>	<b>19.7</b>	<b>17.9</b>	<b>16.5</b>	<b>15.0</b>	<b>-1.5</b>	<b>4.0</b>	<b>-2.4</b>
	<b>LSE</b>	<b>11.1</b>	<b>23.8</b>	<b>21.9</b>	<b>19.1</b>	<b>17.6</b>	<b>14.0</b>	<b>13.1</b>	<b>-0.9</b>	<b>2.0</b>	<b>-6.7</b>
Current situation	SME	18.7	27.2	27.2	31.2	29.8	28.3	27.2	-1.1	8.5	-0.1
	LSE	19.0	28.2	31.2	32.2	30.4	26.4	25.4	-1.0	6.4	-3.1
Expectations	SME	3.7	11.0	9.6	9.0	6.8	5.5	3.6	-1.9	-0.1	-4.6
	LSE	3.6	19.4	13.0	7.1	5.7	2.6	1.7	-0.9	-1.9	-9.8
<b>Employment expectations</b>	SME	6.0	12.9	13.3	14.8	14.4	13.7	13.0	-0.7	7.0	0.0
	LSE	10.3	17.5	19.4	21.4	19.3	17.5	17.4	-0.1	7.1	-1.4
<b>Sales price expectations</b>	SME	8.8	11.8	12.2	12.2	13.1	12.0	9.8	-2.2	1.0	-0.4
	LSE	2.0	5.2	10.0	9.4	7.6	5.2	11.0	5.8	9.0	-0.3
<b>Export expectations of manufacturing</b>	SME	3.0	7.7	5.6	3.9	3.5	3.0	3.0	0.0	0.0	-2.6
	LSE	6.7	12.7	14.6	11.8	10.4	4.9	6.9	2.0	0.2	-5.6

Source: KfW Research, ifo Institute

Explanations and abbreviations:

\*Seasonally and mean adjusted (long-term mean since January 2005 = 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 adjustments as well as rounding. The KfW-ifo SME Barometer was fundamentally revised from the reporting month of April 2018 (new aggregation method, inclusion of services, start of time series now 2005 instead of 1991, export expectations taken into account, discontinuation of regional indicators for western and eastern Germany). Publications prior to and from April 2018 are therefore only comparable to a limited extent.

### 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 ifo Business Survey, from which the well-known ifo Business Climate Index is calculated. Around 9,500 companies from the manufacturing, construction, wholesale, retail and services sectors (excluding financial services, insurance and government) are surveyed each month on their economic situation, including around 8,000 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 an analytically more significant evaluation, however, these quantitative limits have to be drawn more narrowly for retail trade (maximum annual turnover of EUR 12.5 million), construction (up to 200 employees) and services (maximum annual turnover of EUR 25 million). 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 the assessments of the current business situation (percentage of positive answers less percentage of negative answers), the balance of business expectations for the next six months, calculated in the same way, and the inferred mean value of these two components as the business climate. Moreover, employment expectations, domestic sales price expectations and – solely for manufacturing – export expectations are reported as balance figures, in each case with an expectations horizon of three months. All time series are seasonally and mean adjusted. The zero line therefore marks the long-term 'cycle-neutral' average since January 2005. Indicator values above (or below) zero point to an above average or favourable (below average or negative) economic situation.