

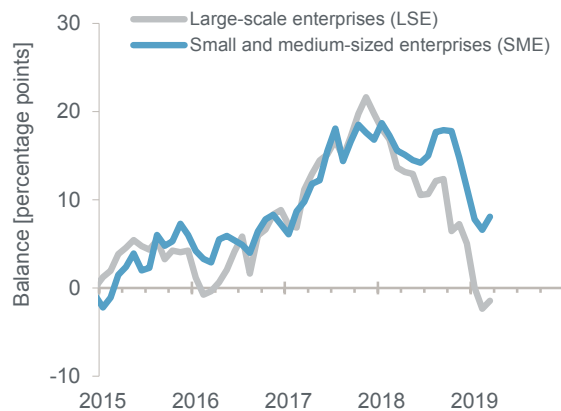
»» SMEs: Downturn in sentiment has bottomed out

4 April 2019

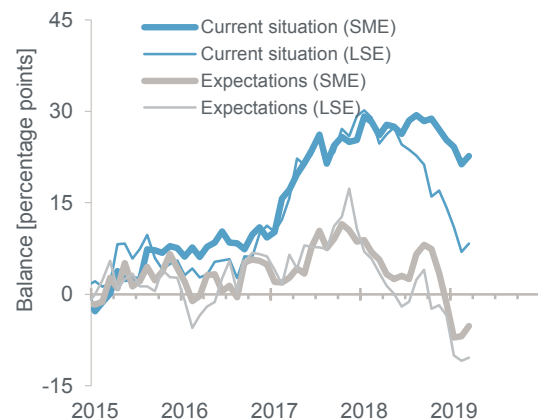
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- SME business sentiment has brightened slightly
- Situation assessments and expectations are up a notch
- Sentiment among large enterprises has also improved moderately
- However, export-oriented manufacturers are increasingly worried

KfW-ifo business climate



KfW-ifo climate components



Source: KfW Research, ifo Institute

SME business sentiment rallies for now

At a time of economic uncertainty and after the latest twist in the Brexit drama, SMEs stand out with positive news. In March their business climate improved by 1.5 points to 8.1 balance points, ending a series of five consecutive declines. Both sentiment indicator components contributed to the minor increase.

- At 22.7 balance points, SMEs now rate their current business situation 1.4 points better than in the previous month. The situation indicator thus remains on an historically high level. Across the first-quarter average, however, it dropped noticeably below the fourth quarter 2018, confirming our expectation that Germany's economic output probably grew only slightly at the start of 2019.
- Business expectations for the next six months rose 1.7 points to now -5.2 balance points. SMEs are slightly less anxious about the near future again but remain concerned. This is because despite the improvement, the indicator continues clearly below the zero line, which represents the long-term average.

Sentiment among large enterprises is less negative

At the beginning of spring, large enterprises were not quite as gloomy as they were in February. They slightly upgraded their situation assessments (+1.4 points to 8.3 balance points) but also their expectations (+0.5 points to -10.4 balance points). At -1.5 balance points, however, up 0.9 points on the previous month, the business climate of large enterprises remains in negative territory and the gap to SMEs has widened again.

Export expectations have plummeted

A look across the sectors reveals a widening gap in sentiment between domestic sectors (construction, retail and wholesale, services) and export-oriented manufacturing. Manufacturing is the only sector in which sentiment fell again significantly and now slipped below the zero line in both size classes (SMEs: -2.2 points to -1.2 balance points; large enterprises: -2.9 points to -8.9 balance points). That makes large enterprises clearly the most pessimistic segment of the German economy at this time. It reflects concern over global trade in general but also fear of the immediate consequences of what may be a chaotic Brexit in particular, which could happen as soon as 12 April after the brief extension offered to the UK at the recent EU summit. This fear can clearly be seen from export expectations, which went into a veritable

tailspin in March. They dropped by three times the typical monthly variation among manufacturing SMEs (-5.6 points to -8.2 balance points) and even three and a half times that among large manufacturers (-11.8 points to -13.6 balance points). The last time enterprises rated their export outlook as poorly was during the euro crisis of 2012. Only during the severe global recession of 2009 did they rate it even worse.

Domestic sectors are generally positive

By comparison, sentiment in the domestic sectors is not just good overall but even improved noticeably again in the vast majority of segments in March. SME construction firms, retailers, large wholesalers and service providers in particular currently report significantly or even very significantly higher business confidence levels.

Expansion continues at a moderate pace

The March result of the KfW-ifo SME Barometer thus confirms the familiar picture. External trade is a cause for concern while the domestic economy remains steady and stabilises Germany's business cycle. At the same time, it is sending out a signal of hope that sentiment will not crash through the floor despite numerous international uncertainties. Against this backdrop, we remain very comfortable with our forecast of moderate 0.8% real GDP growth for 2019. The coming weeks and months will hopefully provide more clarity with respect to Brexit and the looming threat of the US to impose punitive tariffs on automobile imports from the EU. ■

KfW Research

KfW-ifo SME Barometer: March 2019

KfW-ifo SME Barometer in figures

| Balance [Percentage points]* | | Month/Year | | | | | | | m-o-m | y-o-y | 3m-o-3m |
|---|------------|-------------|-------------|-------------|-------------|------------|-------------|-------------|------------|--------------|-------------|
| | | Mar/18 | Oct/18 | Nov/18 | Dec/18 | Jan/19 | Feb/19 | Mar/19 | | | |
| Business climate | | | | | | | | | | | |
| Manufacturing | SME | 15.2 | 11.4 | 9.6 | 6.4 | 2.2 | 1.0 | -1.2 | -2.2 | -16.4 | -8.5 |
| | LSE | 16.9 | 5.0 | 5.1 | 1.9 | -3.4 | -6.0 | -8.9 | -2.9 | -25.8 | -10.1 |
| Construction | SME | 26.4 | 40.2 | 37.2 | 36.0 | 26.4 | 25.7 | 28.5 | 2.8 | 2.1 | -10.9 |
| | LSE | 23.7 | 38.8 | 35.9 | 38.3 | 31.7 | 24.2 | 23.8 | -0.4 | 0.1 | -11.1 |
| Retail trade | SME | 9.2 | 9.5 | 9.8 | 11.8 | 6.1 | 11.4 | 14.6 | 3.2 | 5.4 | 0.3 |
| | LSE | -4.5 | -13.3 | -1.7 | -7.3 | -8.8 | -6.1 | -0.5 | 5.6 | 4.0 | 2.3 |
| Wholesale trade | SME | 15.2 | 10.7 | 9.1 | 6.6 | 2.6 | 2.1 | 0.4 | -1.7 | -14.8 | -7.1 |
| | LSE | 10.6 | 6.6 | 5.2 | 6.5 | -6.6 | -1.4 | 3.8 | 5.2 | -6.8 | -7.5 |
| Services | SME | 14.5 | 17.4 | 14.7 | 9.6 | 8.1 | 4.9 | 10.2 | 5.3 | -4.3 | -6.2 |
| | LSE | 17.2 | 15.5 | 14.0 | 15.2 | 8.2 | 6.8 | 9.1 | 2.3 | -8.1 | -6.9 |
| Germany | SME | 15.6 | 17.8 | 14.8 | 11.3 | 7.8 | 6.6 | 8.1 | 1.5 | -7.5 | -7.1 |
| | LSE | 13.6 | 6.4 | 7.2 | 5.0 | 0.0 | -2.4 | -1.5 | 0.9 | -15.1 | -7.5 |
| Current situation | SME | 26.1 | 28.8 | 27.0 | 25.3 | 24.2 | 21.3 | 22.7 | 1.4 | -3.4 | -4.3 |
| | LSE | 24.7 | 16.0 | 17.0 | 14.2 | 11.0 | 6.9 | 8.3 | 1.4 | -16.4 | -7.0 |
| Expectations | SME | 5.7 | 7.4 | 3.5 | -1.5 | -7.1 | -6.9 | -5.2 | 1.7 | -10.9 | -9.5 |
| | LSE | 3.5 | -2.4 | -1.8 | -3.5 | -10.0 | -10.9 | -10.4 | 0.5 | -13.9 | -7.9 |
| Employment expectations | SME | 12.3 | 11.7 | 10.5 | 9.9 | 9.1 | 9.1 | 7.4 | -1.7 | -4.9 | -2.2 |
| | LSE | 16.1 | 12.0 | 15.3 | 15.8 | 10.2 | 8.6 | 5.3 | -3.3 | -10.8 | -6.3 |
| Sales price expectations | SME | 11.0 | 13.6 | 14.7 | 15.8 | 14.8 | 9.5 | 8.1 | -1.4 | -2.9 | -3.9 |
| | LSE | 3.9 | 6.6 | 10.5 | 13.6 | 12.3 | 7.3 | 3.9 | -3.4 | 0.0 | -2.4 |
| Export expectations of manufacturing | SME | 3.8 | 0.7 | 4.5 | -1.5 | -3.5 | -2.6 | -8.2 | -5.6 | -12.0 | -6.0 |
| | LSE | 5.4 | -0.7 | -1.4 | -1.4 | -6.1 | -1.8 | -13.6 | -11.8 | -19.0 | -6.0 |

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-)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. The KfW-ifo SME Barometer was fundamentally revised for the reporting month of April 2018 (new aggregation process, inclusion of services, start of time series now 2005 instead of 1991, consideration of export expectations, discontinuation of regional indicators for western and eastern Germany). Publications prior to and from April 2018 are therefore comparable to a limited extent only.

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 economic surveys which are used to calculate, among other things, the well-known ifo Business Climate Index. Each month about 9,500 enterprises from trade and industry, construction, wholesale, retail and services (without the banking and insurance sectors or the state) are polled on their business situation, among them some 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 a more accurate analysis, however, these quantitative distinctions have to be drawn more narrowly for retail trade (maximum annual turnover of EUR 12.5 million), the building and the construction industry (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 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 and – exclusively for manufacturing – export expectations are also captured as balance figures for the next three months. All time series are seasonally and mean adjusted. The zero line therefore marks the long-term 'cycle-neutral' average since January 2005. Indicators above (or below) zero point to an above average or favourable (below average or negative) business situation.