

German SMEs report lower business situation assessments but the outlook is a bit less pessimistic

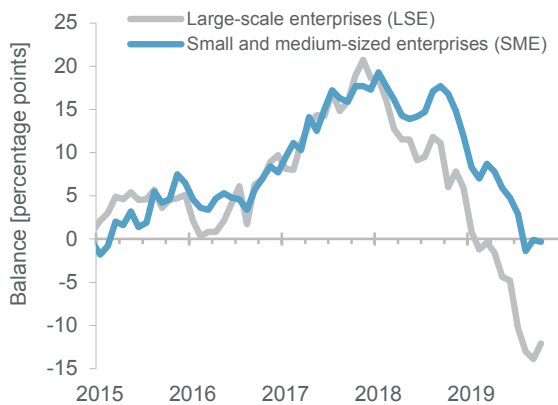
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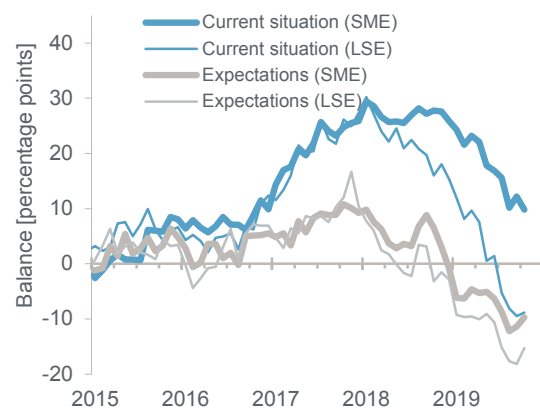
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- SME business sentiment is moving almost sideways
- Situation assessments have fallen but business expectations are brightening slightly
- Large enterprises' expectations have picked up, stopping the slump in confidence
- Export expectations of large enterprises rise noticeably

KfW-ifo business climate



KfW-ifo climate components



Source: KfW Research, ifo Institute

SMEs show a mixed picture

Business confidence among Germany's small and medium-sized enterprises dropped marginally by 0.2 points and thus remains on a level close to the zero line which indicates an average business situation (-0.3 balance points). Sentiment is stabilised at the beginning of the autumn quarter by less pessimistic expectations for the future. However, the business situation is deteriorating:

- Situation assessments fell by 2.4 points, which roughly corresponds to an average monthly variation. They thus remain on the consolidation course that began in the autumn of 2018 but are still at an above average level of 9.8 balance points.
- The recently very pessimistic business expectations improved by 1.7 points for the second consecutive month and are now at -9.7 balance points.

Have large enterprises pulled up from their nosedive?

October saw positive signals coming primarily from large enterprises, whose business confidence was up by 1.8 points. The gap to the SME sector has thus narrowed somewhat but their business confidence is still much lower than that of SMEs, at -12.1 balance points. Situation assessments improved by 0.6 points to -8.9 balance points. Furthermore, pessimism subsided slightly (business expectations: +2.9 points to -15.3 balance points). This feeds the hope that the seemingly unending collapse of business sentiment since the end of 2018 might come to an end. Since August, sentiment among large enterprises has even dropped below the record lows during the euro crisis. In the month under review, confidence has picked up notably in the particularly pessimistic large-scale industrial sector. The upturn in sentiment here by 3.4 points to -18.5 balance points, however, is due solely to improved business expectations, while situation assessments deteriorated again. The more optimistic business expectations and a distinct rise in export expectations by 8.1 points are likely due to emerging signs that point to an easing of the acute trade risks. The EU and the UK government agreed on a revised withdrawal agreement during the survey period and

agreement on a partial deal was announced in the trade conflict between the US and China.

Manufacturing SMEs remain in the doldrums

Both events, however, so far do not appear to have impressed manufacturing SMEs. Their business confidence fell in October (-1.6 points to -15.0 balance points) as a result of further deteriorating business situation assessments as well as even more pessimistic expectations for the future than in the previous month. SMEs' export expectations, on the other hand, picked up slightly. But their increase of 0.8 points was much lower than among large manufacturers. Confidence in the wholesale sector, which is closely connected with manufacturing, also rose somewhat (+0.8 points to -9.7 balance points).

Only few signs of contagion effects

In recent months, there have been more and more reports of large industrial firms planning job cuts. That has led to concern that the industrial recession could spread to other areas of the economy. Indeed, sentiment among small and medium-sized retailers and construction firms fell slightly in October. In the construction sector, the minor drop of 0.5 points was put into perspective by the continuing very high confidence level of 29.3 balance points, however, which is surely being buoyed by prospects of continuing low interest rates. Confidence in the retail sector is not euphoric at 8.5 balance points but still far above the average. The second consecutive decline (-1.2 points) still does not suggest a downward trend but the movement is consistent with the slightly weakening consumer confidence identified by the market research institute GfK in October.

SME service providers going downhill?

Sentiment among small and medium-sized service providers is now merely on a good average level (+2.7 balance points). A downward trend seemed to have stopped in September but confidence fell again by a moderate -1.4 points in October. Among the large service providers, however, which tend to be more dependent on the business cycle, sentiment stabilised slightly after dropping below average since August (+1.8 points to -4.8 balance points).

Employment expectations moved sideways

In line with the staff reduction plans reported in the media, employment expectations in manufacturing have fallen further and further in the past months and are now clearly negative on balance. This is true of both large-scale enterprises and manufacturing SMEs, whose employment expectations dropped further in October as well. But in other sectors an above-average number of enterprises are still planning to hire more workers. This applies to SMEs in particular, whose employment expectations are on an average level overall. A minimal decline in October does nothing to change this either (-0.2 points to 0.7 balance points). Employment expectations of large-scale enterprises rose slightly at the same time (+0.3 points to -2.8 balance points) and are thus approaching the zero line from below.

Sentiment may brighten towards the end of the year

The KfW-ifo SME Barometer shows that SMEs got off to a weak start to the autumn quarter. However, there is potential for confidence levels to pick up in the months ahead. A chaotic Brexit without a withdrawal agreement has become unlikely, which could also impact positively on manufacturing SMEs' business expectations in the coming months. Furthermore, there is a chance that a first partial agreement may be signed in the trade dispute between the US and China. However, these trade risks affect the small and medium-sized enterprise sector much less than the significantly more export-oriented large enterprises. On the other hand, there is the danger that the US administration may decide to impose new tariffs targeting car imports from the EU in November. It is true that a continuation of the trade talks is much more likely. But given the high economic importance of the automotive industry, which is under cyclical and structural pressures, the mere threat may cause the mood to turn sour again. At least in the autumn quarter, Germany's cyclical momentum will probably remain clearly below average again. But if new US tariffs on automobile imports can be prevented and the trade conflict between the US and China eases further, we expect rising quarterly growth rates again in the course of 2020.

KfW-ifo SME Barometer in figures

Balance [Percentage points]*		Month/Year							m-o-m	y-o-y	3m-o-3m
		Oct/18	May/19	Jun/19	Jul/19	Aug/19	Sep/19	Oct/19			
Business climate											
Manufacturing	SME	11.4	-4.0	-5.6	-11.0	-13.2	-13.4	-15.0	-1.6	-26.4	-7.0
	LSE	5.1	-12.7	-15.8	-23.4	-22.0	-21.9	-18.5	3.4	-23.6	-3.5
Construction	SME	38.5	31.0	29.5	30.7	30.2	29.8	29.3	-0.5	-9.2	-0.6
	LSE	37.1	31.0	28.5	25.1	14.2	24.9	19.9	-5.0	-17.2	-8.5
Retail trade	SME	9.6	11.1	14.0	11.5	13.1	9.7	8.5	-1.2	-1.1	-1.8
	LSE	-12.4	4.3	12.2	-1.3	5.3	0.4	-2.0	-2.4	10.4	-3.8
Wholesale trade	SME	10.4	-1.0	-1.2	-4.5	-8.1	-10.5	-9.7	0.8	-20.1	-7.2
	LSE	6.8	-0.2	-2.0	-16.5	-10.9	-16.9	-16.4	0.5	-23.2	-8.5
Services	SME	16.7	6.4	4.7	4.4	-0.7	4.1	2.7	-1.4	-14.0	-3.1
	LSE	14.8	0.8	4.1	2.7	-5.8	-6.6	-4.8	1.8	-19.6	-8.3
Germany											
	SME	16.8	5.9	4.8	2.9	-1.4	-0.1	-0.3	-0.2	-17.1	-5.1
	LSE	6.0	-4.4	-4.8	-10.3	-13.0	-13.9	-12.1	1.8	-18.1	-6.5
Current situation	SME	27.8	17.8	16.9	15.6	10.2	12.2	9.8	-2.4	-18.0	-6.0
	LSE	16.0	0.5	1.4	-5.3	-8.1	-9.5	-8.9	0.6	-24.9	-7.7
Expectations	SME	6.5	-5.1	-6.3	-8.7	-12.2	-11.4	-9.7	1.7	-16.2	-4.4
	LSE	-3.2	-9.1	-10.6	-15.2	-17.7	-18.2	-15.3	2.9	-12.1	-5.4
Employment expectations	SME	11.7	4.9	2.3	3.0	0.2	0.9	0.7	-0.2	-11.0	-2.8
	LSE	13.3	1.4	1.4	-3.8	-1.5	-3.1	-2.8	0.3	-16.1	-2.1
Sales price expectations	SME	13.3	4.4	3.6	2.4	3.0	1.0	3.2	2.2	-10.1	-1.1
	LSE	7.7	2.0	1.1	-1.1	-0.9	-0.4	-0.3	0.1	-8.0	-1.2
Export expectations of manufacturing	SME	0.6	-5.8	-10.2	-12.3	-12.6	-14.4	-13.6	0.8	-14.2	-4.1
	LSE	-0.8	-12.6	-12.8	-15.1	-14.0	-20.0	-11.9	8.1	-11.1	-1.8

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 9,000 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 7,500 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.