

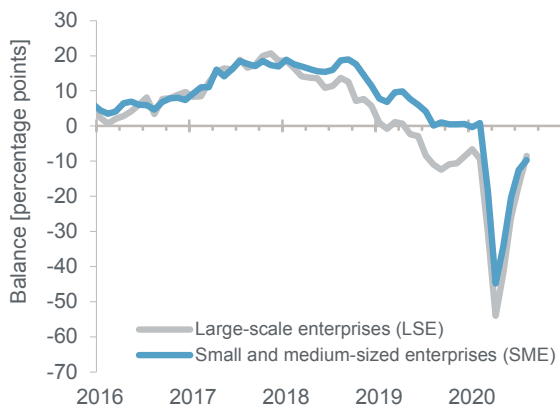
»» Sentiment improvement in SMEs is losing steam

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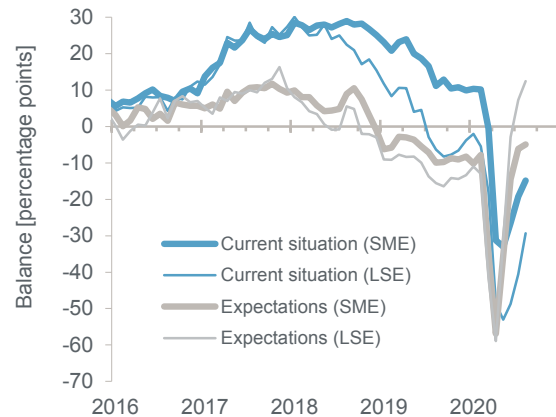
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- SME business sentiment is rising at a slower pace
- Situation assessments have improved noticeably but expectations are rising only moderately
- Large enterprises are more optimistic than SMEs for the first time in two and a half years
- Sustaining the recovery this coming autumn and winter is becoming more difficult

KfW-ifo business climate



KfW-ifo climate components



Source: KfW Research, ifo Institute

Pace of recovery in SME sector is slowing

The initially very strong sentiment improvement driven by the relaxation of coronavirus restrictions since May is weakening. In August, however, SME business confidence continued to brighten, but much less than in the preceding months, rising by +2.8 points to -9.7 balance points. That is still well below the pre-crisis level of February (0.9 balance points). The fourth consecutive improvement of the sentiment indicator is being driven by both components, although to varying degrees.

- Business expectations rose by a mere 1.2 points to -5.0 balance points. With new infections on the rise, it is rather more likely that coronavirus restrictions will be tightened again – especially at local level – than relaxed further. So the cautious rise in optimism is understandable.
- Situation assessments, on the other hand, improved more substantially in August, gaining 4.4 points to reach -14.9 balance points. A temporary, very strong growth surge over the summer is becoming increasingly apparent, following the historic slump in economic output in the second quarter.

Sentiment among large enterprises is almost back to pre-crisis levels

Confidence is rising among large firms as well and at a much higher rate than in the SME sector, climbing 8.4 points to -8.5 balance points in August. Large enterprises are thus slightly more upbeat than SMEs for the first time in two and a half years. But not only that: their sentiment indicator, although lower than that of SMEs, is also virtually back to its pre-crisis level. On closer inspection, however, this good result does not shine as bright as it may seem at first glance. It is mainly due to the significantly more optimistic level of expectations, which rose noticeably once again in August (+5.2 points to 12.5 balance points). The last time large firms were more optimistic than now is almost three years ago. In contrast, their situation assessments remain profoundly negative despite surging in August (+11.2 points to -29.3 balance points). In other words, large companies believe their business will improve again, but from what continues to be a modest level. The ongoing global spread of the pandemic, the US trade conflicts and the uncertainties surrounding Brexit may also potentially disappoint expectations.

Retailers stand out with greater confidence

The risks to the global economy are influencing large manufacturers' export expectations, for example, which are slipping again for the first time after recovering tangibly in previous months (-6.9 points to 4.6 balance points). Export expectations of SME manufacturers rose in August but only marginally, continuing on a low level (+1.1 points to -14.5 balance points). All in all, those sectors that are particularly engaged in international business – manufacturing and wholesale – continue to be found on the bottom end of the confidence table. In contrast, retailers exhibit very high confidence levels. In no other economic sector was the sentiment indicator for August in both company size classes above the zero line, which stands for the long-term average. The confidence of large retailers, which include car dealerships, for example, climbed by a staggering 18.8 points to 9.5 balance points. At the same time, SME retailers have virtually maintained their sentiment level, which has been positive already since July (-0.5 points to 8.0 balance points). Retailers are benefiting not just from the temporary VAT reduction that was introduced in the middle of the year. Other measures that stabilise private real purchasing power and, thus, consumption, are also having a positive impact on them. These include, above all, the extension of short-time work allowance, which was disbursed to more than 5 million workers in June and was recently extended until the end of 2021. Confidence in the services sector is clearly trending upwards as well, even though it is still on a lower level than the long-term average. In the construction sector, confidence has been divided between the size classes for some time now. Construction SMEs, which focus on residential dwellings, continue to be positive (+2.3 points to 8.6 balance points). In contrast, large construction firms remain negative, as they have been since April (-2.5 points to -12.5 balance points). This is likely a reflection of the poorer outlook for commercial construction, a component of business investment activity that is suffering above all from the pandemic-induced very high uncertainty.

The easy part of the economic recovery is over

The August findings of the KfW-ifo SME Barometer illustrate that the economic recovery continues irrespective of the recent resurgence in the number of new coronavirus infections from a low level in Germany – and that is clearly good news. Nevertheless, the increase in sentiment levels clearly slowed over the summer after business confidence initially soared in unprecedented leaps with the loosening of restrictions since May. The easy part of the recovery since the pandemic-induced historic slump in April is over and bringing economic activity closer to what it was before the crisis this coming autumn and winter will be rather challenging by comparison. Export-oriented industrial firms in particular have to adapt to growing headwinds from the demand side. The continuing rapid increase in the number of coronavirus infections around the globe means that uncertainty will remain extremely high, putting the brakes on business investment in Germany and abroad. This affects the German export industry in particular, which specialises in high-quality capital goods. Moreover, unemployment in Europe will likely continue to grow for the time being, and this is set to have second-round effects on consumption and especially on the sale of durable goods such as automobiles. In Germany, too, it is anything but certain that all workers affected by short-time work will in fact be able to subsequently return to their previous places of work. It is therefore important for a sustained economic recovery that as many persons as possible make use of the short-time work phase for further education and, for example, improving their digital skills. Overall, even with the recovery setting in from the third quarter, we expect Germany's gross domestic product to contract by around 6% in all of 2020, before growing again by 5% in the coming year. The pre-crisis level of the final quarter of 2019 will probably not be achieved again before the end of 2021. A severe second wave of infections remains the highest risk, although new restrictions – should they become necessary – will likely end up being more targeted than in spring. Continued vigilance and discipline in complying with hygiene protocols therefore remain crucial to prevent a further economic setback from a second wave of infections.

KfW Research

KfW-ifo SME Barometer: August 2020

KfW-ifo SME Barometer in figures

Balance [Percentage points]*			Month/Year					m-o-m	y-o-y	3m-o-3m	
			Mar/20	Apr/20	May/20	Jun/20	Jul/20				Aug/20
Business climate											
Manufacturing	SME	-12.3	-20.8	-46.3	-40.7	-28.5	-18.4	-16.5	1.9	-4.2	14.8
	LSE	-20.8	-34.6	-60.0	-50.5	-38.7	-27.5	-15.4	12.1	5.4	21.2
Construction	SME	29.2	12.4	-9.0	-3.5	1.8	6.3	8.6	2.3	-20.6	5.6
	LSE	13.1	4.2	-24.2	-19.9	-17.4	-10.0	-12.5	-2.5	-25.6	0.0
Retail trade	SME	11.9	-12.6	-43.6	-21.7	-1.5	8.5	8.0	-0.5	-3.9	31.0
	LSE	4.9	-25.8	-52.9	-28.0	-13.7	-9.3	9.5	18.8	4.6	31.1
Wholesale trade	SME	-7.9	-27.2	-56.0	-37.4	-29.2	-16.2	-11.6	4.6	-3.7	21.2
	LSE	-11.7	-28.4	-47.1	-30.5	-23.0	-13.2	-16.1	-2.9	-4.4	17.9
Services	SME	0.6	-23.9	-52.9	-38.3	-23.2	-15.6	-12.4	3.2	-13.0	21.3
	LSE	-4.7	-28.8	-46.5	-38.0	-18.4	-10.1	-2.5	7.6	2.2	27.4
Germany	SME	0.2	-18.7	-44.8	-34.2	-20.4	-12.5	-9.7	2.8	-9.9	18.4
	LSE	-11.0	-30.5	-54.0	-41.8	-26.1	-16.9	-8.5	8.4	2.5	24.9
Current situation	SME	11.1	-0.6	-31.3	-33.1	-26.6	-19.3	-14.9	4.4	-26.0	1.4
	LSE	-6.3	-18.0	-48.6	-53.0	-48.7	-40.5	-29.3	11.2	-23.0	0.4
Expectations	SME	-10.0	-34.8	-56.9	-35.6	-14.6	-6.2	-5.0	1.2	5.0	33.8
	LSE	-15.5	-41.5	-58.9	-31.2	-2.9	7.3	12.5	5.2	28.0	49.5
Employment expectations	SME	0.7	-8.1	-24.4	-17.0	-11.3	-8.4	-5.2	3.2	-5.9	8.2
	LSE	-0.7	-14.9	-27.0	-26.2	-19.5	-19.2	-12.7	6.5	-12.0	5.6
Sales price expectations	SME	4.1	-4.5	-13.7	-12.0	-8.6	-4.0	-2.9	1.1	-7.0	4.9
	LSE	0.1	-5.5	-15.7	-15.3	-12.2	-8.9	-4.9	4.0	-5.0	3.5
Export expectations of manufacturing	SME	-11.4	-25.3	-57.3	-41.1	-20.3	-15.6	-14.5	1.1	-3.1	24.4
	LSE	-15.7	-31.7	-60.5	-30.0	-4.5	11.5	4.6	-6.9	20.3	44.6

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-)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.