

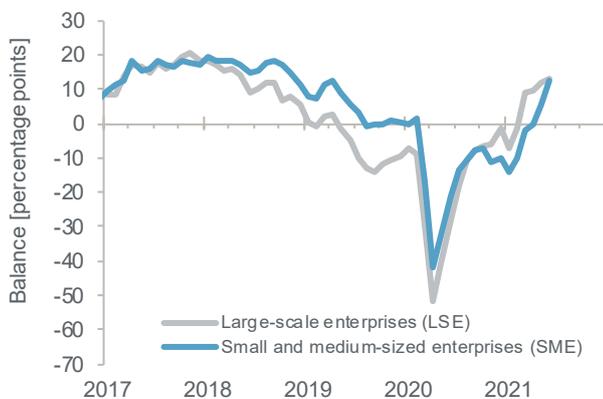
## »» Economic indicators are turning green

7 July 2021

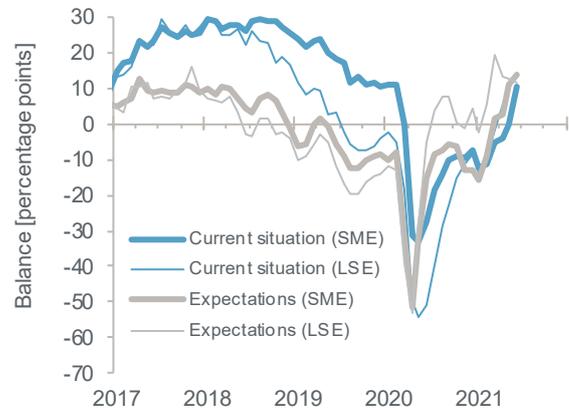
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- SME business sentiment surges again
- Large enterprises are also more upbeat
- Employment and price expectations have risen sharply
- Growth spurt in the further course of the year, Delta variant is a risk

KfW-ifo business climate



KfW-ifo climate components



Source: KfW Research, ifo Institute

### SME sentiment hits two-and-a-half-year high

The seven-day incidence of new coronavirus infections has dropped to single digits, more than half of the population has received at least their first dose and restrictions on social life are being lifted. As the pandemic situation has clearly eased, sentiment in June surged about as much again as in May. Business confidence among SMEs rose by 6.7 points to 12.3 balance points at the beginning of the summer, nearly matching levels in the large enterprise segment. The last time sentiment was more positive was in November 2018. Both business sentiment components drove the most recent sharp increase:

- With the easing of coronavirus restrictions, situation assessments climbed 10.7 points to 10.5 balance points. That is four times the typical monthly variation and the second highest increase ever recorded. Only once during the upturn after the global financial crisis was there slightly more impetus (April 2010: +11.5 points).
- At the same time, however, SMEs also upgraded their business expectations by a noteworthy 2.8 points. They are now more optimistic than at any time in more than ten years, at 13.8 balance points.

### Large enterprises are more positive about their situation

Sentiment among large enterprises also brightened in June, although driven solely by improved situation assessments, as was the case already in April and May. They rose by 3.7 points to 14.4 balance points. By contrast, business expectations of large enterprises now stand at 11.5 balance points, just barely holding the previous month's level (-0.9 points). The continuing minor consolidation of expectations on a nonetheless still high level comparable to that of SMEs indicates persistent shortages of supplies and raw materials, which is why output, especially in the manufacturing and construction sector, cannot fully keep up with growing demand for the time being. On balance, business sentiment among large enterprises improved by 1.4 points to now 13.1 points.

### Sentiment is positive across the board

Confidence levels are now positive in all segments of the national economy, both by economic sector and enterprise size class, meaning business sentiment is above the zero line, which stands for the long-term average. Those segments that benefited most from the easing of coronavirus restrictions and the return of social life reported the most significant month-on-month improvements in business sentiment. SME retailers showed a particularly distinct increase (+13.8 points to 17.8 balance points), as did SME service providers, which account for the bulk of contact-intensive offerings in

the arts and culture, entertainment, hospitality and personal services (+11.0 points to 8.6 balance points). But sentiment improvements were also noteworthy among large-scale retailers (+8.3 points to 8.2 balance points) and manufacturers – who were already on a high level to begin with (SMEs: +5.1 points to 17.6 balance points; large enterprises: +3.7 points to 25.4 balance points). The positive sentiment among manufacturers is also being bolstered by their export expectations (SMEs: +4.7 points to 14.7 balance points; large enterprises: +0.1 points to 13.7 balance points), which at least puts concern over industrial output being limited by supply shortages into perspective. This concern currently appears to be slightly higher among large construction firms, where business sentiment dropped marginally (-0.6 points to 1.2 balance points), as it did among large service providers (-0.2 points to 4.4 balance points). In SME construction firms, on the other hand, which focus on residential dwellings, business sentiment continued to rise in June, reaching the highest level this year (+1.3 points to 11.7 balance points). After moderate increases in both size classes, confidence in the wholesale sector is distinctly positive in both size classes (SMEs: +2.7 points to 14.2 balance points; large enterprises: +0.2 points to 16.0 balance points).

#### **Employment and prices are rising noticeably**

The high confidence expressed by the general business sentiment indicators is rounded off by businesses' specific expectations about the development of employment levels and sales prices. Thus, SMEs' employment expectations rose by 6.3 points, actually hitting a new all-time high of 14.5 balance points in June. The strongest contribution to the increase came from service providers, who are now looking to start hiring again after the significant relaxation of pandemic measures. Large enterprises' business expectations increased by 4.3 points to 7.9 balance points, the highest level since early 2019. Sales price expectations also rose steeply, reaching new record highs in both enterprise size classes (SMEs: +6.6 points to 30.7 balance points; large enterprises: +6.9 points to 28.1 balance points). Nonetheless, it would be wrong to conclude that they fear persistently high inflation rates. The price expectations refer to a time horizon of only three months, just like employment expecta-

tions. That means they currently refer to September, the middle of the second half of 2021, for which noticeably higher monthly inflation rates are to be expected temporarily simply because of the temporary value-added tax reduction a year ago. That base effect will end at the end of the year. The currently high short-term price expectations across the breadth of the business community are therefore mainly a counter-movement to the weak price trend since the outbreak of the pandemic and not a sign of long-term risks to price stability. That would require a wage-price spiral but the declining wage levels currently indicate otherwise. In the first quarter of 2021, wages fell by a nominal 0.7% and even by 2.0% in real terms on the same quarter in the previous year.

#### **All signs point to an upswing**

The good news of the KfW-ifo SME Barometer in June is that all signs point to an upturn. All indicators of the barometer have improved significantly since the beginning of the year, in fact, two thirds of them by more than 20 points. A look at the streetscape alone shows that the turnovers of most pandemic-stricken service providers have increased substantially. Many people are now catching up on all the things they missed during the long coronavirus winter. As they were forced to save during lockdown periods, many might be more willing to increase their spending. Manufacturers and construction firms have had no significant sales problems for quite some time and instead have been grappling a bit more with supply shortages. While incoming orders in the manufacturing sector already exceed the pre-crisis level of February 2020 by a good 6% despite the most recent setback in May, industrial output in May was still 5% lower. But the bottlenecks and the post-coronavirus boom in manufacturing are two sides of the same coin. For all the problems caused by supply shortages, it is helpful to remember that severe excess demand a year ago would have been deemed a highly positive scenario. After a difficult start to the year, Germany can therefore look forward to a growth surge in the further course of the year. The successes in containing the pandemic are making this possible. Now it is crucial – for the government and also for each individual – to take responsibility for the regained freedom and to continue rolling out vaccines at a high pace, especially given the accelerating spread of the highly infectious Delta variant of the virus.

### KfW-ifo SME Barometer in figures

Balance [Percentage points]*		Month/Year						Jun 2021	m-o-m	y-o-y	3m-o-3m
		Jun 2020	Jan 2021	Feb 2021	Mar 2021	Apr 2021	May 2021				
<b>Business climate</b>											
Manufacturing	SME	-27.7	-3.9	0.1	7.0	10.2	12.5	17.6	5.1	45.3	12.4
	LSE	-36.4	1.6	10.9	19.7	20.2	21.7	25.4	3.7	61.8	11.7
Construction	SME	2.6	1.1	3.9	8.9	7.8	10.4	11.7	1.3	9.1	5.3
	LSE	-14.1	-4.5	-5.8	0.5	-1.3	1.8	1.2	-0.6	15.3	3.8
Retail trade	SME	-1.3	-26.6	-23.1	-7.8	-2.9	4.0	17.8	13.8	19.1	25.5
	LSE	-14.4	-22.7	-27.3	-7.1	-5.2	-0.1	8.2	8.3	22.6	20.0
Wholesale trade	SME	-26.9	-13.0	-12.9	-0.5	3.3	11.5	14.2	2.7	41.1	18.5
	LSE	-22.1	-3.9	-0.4	4.3	10.0	15.8	16.0	0.2	38.1	13.9
Services	SME	-23.4	-23.4	-19.8	-11.8	-14.0	-2.4	8.6	11.0	32.0	15.7
	LSE	-22.1	-13.8	-12.9	-2.6	-2.8	4.6	4.4	-0.2	26.5	11.8
<b>Germany</b>	<b>SME</b>	<b>-21.1</b>	<b>-14.3</b>	<b>-10.1</b>	<b>-1.8</b>	<b>-0.4</b>	<b>5.6</b>	<b>12.3</b>	<b>6.7</b>	<b>33.4</b>	<b>14.6</b>
	<b>LSE</b>	<b>-28.1</b>	<b>-7.4</b>	<b>-1.5</b>	<b>9.1</b>	<b>9.7</b>	<b>11.7</b>	<b>13.1</b>	<b>1.4</b>	<b>41.2</b>	<b>11.4</b>
Current situation	SME	-27.5	-12.6	-11.5	-5.3	-3.8	-0.2	10.5	10.7	38.0	12.0
	LSE	-50.6	-13.4	-9.1	-1.8	5.6	10.7	14.4	3.7	65.0	18.3
Expectations	SME	-15.0	-16.0	-8.9	1.5	2.8	11.0	13.8	2.8	28.8	17.0
	LSE	-5.2	-2.1	5.4	19.4	13.4	12.4	11.5	-0.9	16.7	4.9
<b>Employment expectations</b>	SME	-10.6	-3.7	-4.2	1.3	3.7	8.2	14.5	6.3	25.1	11.0
	LSE	-19.2	-10.1	-7.0	-1.2	-0.2	3.6	7.9	4.3	27.1	9.9
<b>Sales price expectations</b>	SME	-8.3	-0.7	1.1	10.0	15.6	24.1	30.7	6.6	39.0	20.0
	LSE	-11.9	0.8	0.9	9.6	15.1	21.2	28.1	6.9	40.0	17.7
<b>Export expectations of manufacturing</b>	SME	-19.4	-7.1	-2.0	4.3	7.4	10.0	14.7	4.7	34.1	12.3
	LSE	-4.3	1.7	4.1	22.1	19.1	13.6	13.7	0.1	18.0	6.2

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.