

## »» Sentiment brightened at the end of the year

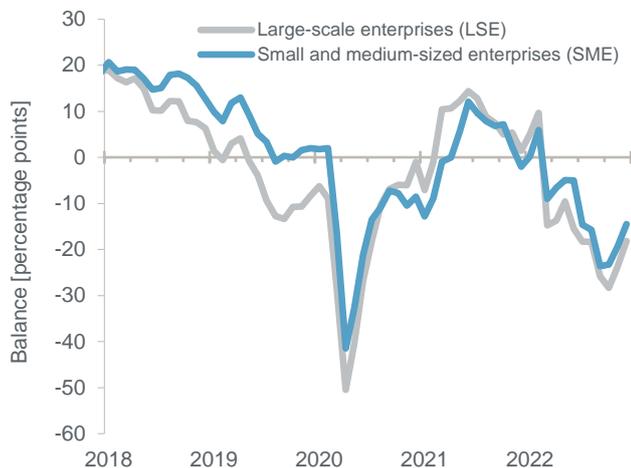
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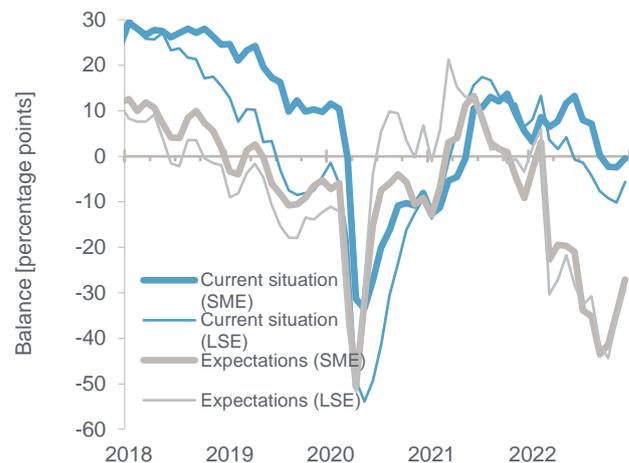
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- SME business confidence up sharply in the lead-up to Christmas
- Expectations rose for third consecutive month, situation assessments are also brighter for first time since June
- Sentiment has risen across the board apart from construction
- Year ends on conciliatory note with hope for a milder recession in the new year

KfW ifo Business Climate Index



KfW ifo sentiment components



Source: KfW Research, ifo Institute

### Confidence improved in the lead-up to Christmas

SME business sentiment improved for the third consecutive month. It rose 4.9 points to -14.5 balance points in the lead-up to Christmas. Expectations began to improve already in October and continued to rise but situation assessments also improved now for the first time since June.

- Business expectations brightened significantly, as they did in the previous month, this time by 7.3 points to -27.1 balance points. Risks such as a gas shortage are being priced out and relief provided by the now approved energy price brake is also set to improve the outlook for a number of businesses. Nevertheless, despite the most recent positive trend, businesses remain anything but optimistic. Their expectations are still on a level that has only been this low in the coronavirus and financial crises.
- Situation assessments improved by 2.0 points to -0.5 balance points in December. But given their steep drop at the beginning of autumn, they nonetheless fell by 6.8 points

on average for the quarter, which points to a drop in economic output in the fourth quarter.

### All sectors but construction are more positive

SMEs from almost all sectors reported improved situation assessments and expectations in December. Business sentiment has increased most markedly among retailers, however (+6.7 points to -21.0 balance points), whose expectations for the next six months have brightened somewhat and situation assessments indicated that Christmas business was not going quite so badly, rising from -16.3 points to -7.3 balance points. But manufacturers, too, reported noticeably brighter sentiment, which was up by 6.4 points, mainly a result of less pessimistic expectations. Only the construction and civil engineering sector reported a continuing decline in sentiment. In this particularly interest rate-sensitive sector, situation assessments and expectations remained near the negative record set in October.

### **Large enterprises are also less pessimistic**

Confidence also improved among large enterprises in the lead-up to Christmas. Their business confidence rose by 5.6 points to -18.2 balance points, with construction also reporting a minor sentiment improvement more broadly across this group than in SMEs.

### **Price increase expectations dropped significantly**

Sales price expectations in December fell noticeably among both SMEs and large enterprises, as they already did in the previous month. However, it is still a long road to the zero line, which stands for the long-term average of price increase plans and, thus, roughly corresponds with the 2% inflation target. Even so, the trend is clearly going in the right direction and it should be noted that business expectations have brightened significantly at the same time, indicating that the mostly cost-driven surge in inflation is waning.

### **Prospects for a mild recession**

Businesses are increasingly ditching the temporary doom and gloom attitude, for which well-filled gas storage tanks and relief for businesses and households provided by the energy price brake are likely to play an important role. As a result, there are definitely upside risks to our economic forecast, which sees a 1% contraction in Germany's GDP next year. However, despite the noticeable improvement in business sentiment since October, a clear majority of SMEs and large enterprises still expect their business situation to deteriorate in the next six months and the forecast uncertainty also surveyed by the ifo Institute remains extraordinarily high as well. Both could cause businesses to hold off on investments and accelerate the downturn. Besides, filling gas storage tanks will likely become more difficult next year without Russian gas supplies and possibly higher demand for LNG from China than in 2022, which will limit the potential for a recovery in the energy-intensive industrial sectors. Ultimately, however, the good Christmas news remains that the deep recession suggested by the sentiment indicators of previous months will most probably not occur.

## KfW-ifo SME Barometer in figures

Balance [Percentage points]*		Month/Year							m-o-m	y-o-y	3m-o-3m
		Dec 2021	Jul 2022	Aug 2022	Sep 2022	Oct 2022	Nov 2022	Dec 2022			
<b>Business climate</b>											
Manufacturing	SME	3.8	-19.2	-20.9	-26.9	-26.1	-24.1	-17.7	6.4	-21.5	-0.3
	LSE	7.6	-10.6	-14.8	-18.5	-21.9	-18.8	-17.6	1.2	-25.2	-4.8
Construction	SME	12.8	-10.2	-8.6	-15.8	-18.5	-15.8	-16.8	-1.0	-29.6	-5.5
	LSE	9.3	-16.0	-8.4	-18.3	-16.2	-14.4	-13.5	0.9	-22.8	-0.5
Retail trade	SME	-12.6	-29.8	-30.3	-35.6	-34.7	-27.7	-21.0	6.7	-8.4	4.1
	LSE	-17.9	-34.9	-32.2	-38.5	-35.5	-30.5	-25.0	5.5	-7.1	4.9
Wholesale trade	SME	-5.1	-21.1	-25.9	-29.5	-29.8	-27.9	-23.6	4.3	-18.5	-1.6
	LSE	-0.5	-23.8	-27.6	-31.4	-31.8	-34.5	-27.5	7.0	-27.0	-3.7
Services	SME	-10.8	-8.9	-11.1	-18.4	-18.1	-16.2	-11.8	4.4	-1.0	-2.6
	LSE	-9.2	-21.6	-17.8	-29.9	-32.1	-26.8	-23.1	3.7	-13.9	-4.2
<b>Germany</b>	<b>SME</b>	<b>-2.0</b>	<b>-14.6</b>	<b>-15.7</b>	<b>-23.6</b>	<b>-23.3</b>	<b>-19.4</b>	<b>-14.5</b>	<b>4.9</b>	<b>-12.5</b>	<b>-1.1</b>
	<b>LSE</b>	<b>1.4</b>	<b>-18.3</b>	<b>-18.4</b>	<b>-25.9</b>	<b>-28.4</b>	<b>-23.8</b>	<b>-18.2</b>	<b>5.6</b>	<b>-19.6</b>	<b>-2.6</b>
Current situation	SME	5.5	7.9	7.1	0.1	-2.3	-2.5	-0.5	2.0	-6.0	-6.8
	LSE	6.4	-1.4	-4.2	-7.7	-9.2	-10.2	-5.6	4.6	-12.0	-3.9
Expectations	SME	-9.2	-33.9	-35.2	-43.6	-41.3	-34.4	-27.1	7.3	-17.9	3.3
	LSE	-3.4	-32.7	-30.8	-41.4	-44.4	-35.7	-29.3	6.4	-25.9	-1.5
<b>Employment expectations</b>	SME	8.0	3.9	2.6	0.5	-1.4	0.6	1.0	0.4	-7.0	-2.3
	LSE	14.8	10.2	8.3	2.8	2.9	4.6	2.7	-1.9	-12.1	-3.7
<b>Sales price expectations</b>	SME	34.4	37.8	36.9	42.8	39.9	34.2	26.5	-7.7	-7.9	-5.6
	LSE	34.2	34.8	35.6	39.4	40.1	35.5	29.3	-6.2	-4.9	-1.6
<b>Export expectations of manufacturing</b>	SME	-0.2	-13.4	-15.8	-19.6	-19.5	-17.7	-11.0	6.7	-10.8	0.2
	LSE	7.7	-8.8	-8.9	-9.1	-7.9	1.8	-0.8	-2.6	-8.5	6.6

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 9,500 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.