

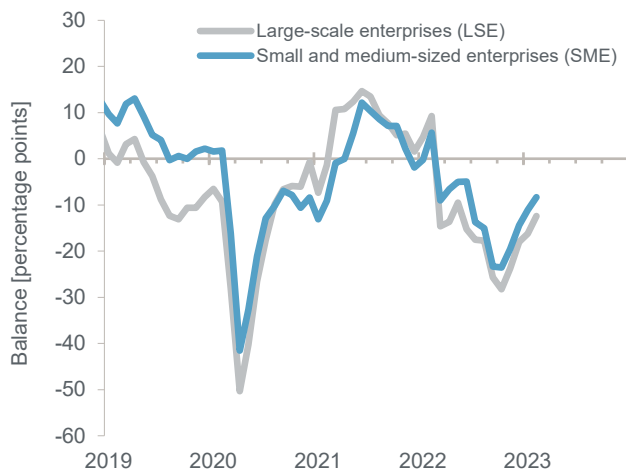
»» SMEs are more upbeat going into Lent

8 March 2023

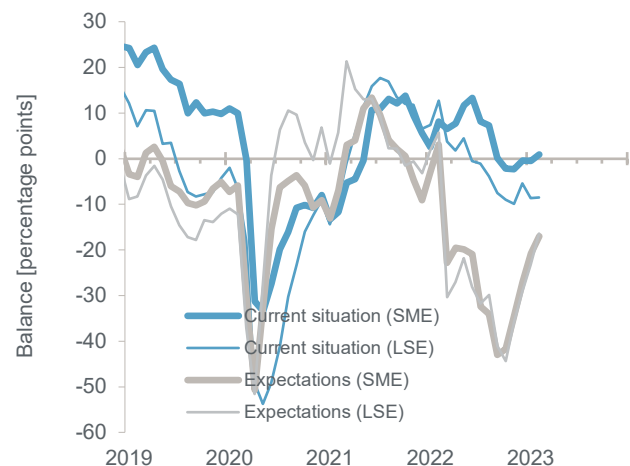
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- Business sentiment continues to improve
- Expectations and situation assessments better than in the previous month
- Sales price expectations have dropped again sharply
- Economic output will almost stagnate in 2023

KfW ifo Business Climate Index



KfW ifo sentiment components



Sources: KfW Research, ifo Institute

SME business confidence continues to rise

SME sentiment continues to improve going into Lent. In February, confidence rose by 2.8 points on January to now -8.3 balance points. That is the highest level since June of last year. Unlike in the previous month, this time both sentiment components contributed to the improvement:

- Business expectations were once again much less pessimistic, improving by 3.8 points to -17.0 balance points. Companies are reassessing their views of opportunities and risks and are no longer pricing in the greatest fears. However, the fact that this indicator remains on a very low level shows that the outlook on the future continues to be shaped by much scepticism.
- Business situation assessments, on the other hand, improved in February by a relatively moderate 1.4 points to now 0.9 balance points. That means situation assessments continue to hug the zero line, which conceptually stands for the long-term average.

Sentiment has improved in all main economic sectors

The mood has brightened in all main economic sectors without exception. Retailers experienced the strongest increase, with sentiment improving by 9.8 points to -0.6 balance points, almost two and a half times a typical monthly variation. SME retailers thus topped the list in February, which suggests that concerns over lost purchasing power among households are easing. Significant improvements in business sentiment were also reported by SME wholesalers (+3.9 points to -9.2 balance points), manufacturers (+3.4 points to -9.5 balance points) and services businesses (+3.3 points to -5.9 balance points), if less pronounced than among retailers. Construction reported the lowest improvement in business sentiment: +1.7 points to -15.8 balance points. In no other main economic sector is the mood among SMEs currently as gloomy as in construction. More than anything, this most likely reflects the current problems in the particularly interest-rate-sensitive area of residential construction, the focus of SME construction activity.

Expectations rose sharply among large enterprises

In February, the mood also improved among large enterprises, where the increase was steeper (+3.8 points) but the sentiment level (-12.4 balance points) still lower than in the SME sector. The main driver was business expectations, which improved by a strong 6.8 points to -16.4 balance points and are now virtually on a par with SMEs. Business situation assessments, however, increased only minimally by 0.1 points and, at now -8.5 balance points, are still well below the long-term average, unlike in the SME sector. The clearly below-average situation assessments of large companies and the only average level among SMEs combined point to a slight drop in economic output in the first quarter. In a sectoral breakdown of large enterprises, services businesses experienced the smallest improvement in sentiment (+1.9 points to -20.8 balance points) and retailers the strongest rise (+8.2 points to -9.8 balance points) – as occurred among SMEs.

Sales price expectations in a continuing downward spiral

The specific inflation expectations of businesses of both size classes are again exhibiting a pleasing trend. Sales price expectations continued to nosedive from the record level on which they started in April 2022, plunging again by a steep -6.9 points to 14.0 balance points among SMEs and by -8.6 points to 15.0 balance points in large enterprises. But they were still too high to be already compatible with the 2% monetary policy inflation target. By contrast, employment expectations followed an opposing trend this time (SMEs: -3.5 points to 3.1 balance points; large enterprises: +0.1 points to 4.5 balance points) but maintained their above-average level. Despite the difficult economic situation, the labour market remained steady, while it is also increasingly shaped by competition for scarce skilled workers.

German economy is set for quasi-stagnation in 2023

The period of Lent has now begun, but according to the current KfW-ifo SME Barometer, the coming months will not be nearly as lean as businesses had long feared. Business sentiment remained below average in February as well but was again better than in the previous month and, above all, much better than in autumn of last year. Last September, under the impression of the approaching energy crisis, expectations in particular had fallen to the deepest recession level, with fears of a broad economic downturn running deep. The threat of a gas shortage has now been averted for this winter, and noticeable price drops on the previous highs of summer 2022 can now be observed in the natural gas, oil and electricity markets. Furthermore, the energy price breaks are easing the pressure on households, and the inflation rate is trending downward, as highlighted for example by the KfW-ifo sales price expectations. Nonetheless, stiff economic headwinds are still blowing because the slack global economy is dimming the outlook for exports, monetary policy measures are likely to fully unfold their restrictive effect only this year, and real wage losses are reverberating. In addition, the Russia-Ukraine war that broke out more than a year ago continues to create enormous uncertainties, and the conditions around the supply of natural gas and other energy sources in the winter of 2023/2024 remain difficult to predict. On balance, we expect a moderate technical recession for Germany in the current winter half-year and a slight 0.3% contraction of GDP for the year 2023 as a whole. If we consider that 2023 has two fewer working days than 2022 and this fluctuation in the number of working days alone will take away 0.2 percentage points of growth, our new forecast materially reflects a stagnation in the current year. Measured against the very grave fears of last autumn, however, such an economic performance would itself have to be deemed a success.

KfW-ifo SME Barometer in figures

Balance [Percentage points]*		Month/Year							m-o-m	y-o-y	3m-o-3m
		Feb 2022	Sep 2022	Oct 2022	Nov 2022	Dec 2022	Jan 2023	Feb 2023			
Business climate											
Manufacturing	SME	9.4	-26.7	-25.5	-22.5	-17.4	-12.9	-9.5	3.4	-18.9	11.6
	LSE	14.4	-18.3	-21.5	-17.9	-16.2	-12.2	-10.2	2.0	-24.6	6.4
Construction	SME	12.8	-15.9	-18.5	-15.6	-16.5	-17.5	-15.8	1.7	-28.6	0.1
	LSE	14.5	-18.2	-16.0	-14.1	-13.1	-10.6	-6.6	4.0	-21.1	6.0
Retail trade	SME	9.4	-35.7	-34.4	-26.7	-16.7	-10.4	-0.6	9.8	-10.0	23.0
	LSE	-5.3	-38.4	-35.2	-29.4	-22.3	-18.0	-9.8	8.2	-4.5	17.6
Wholesale trade	SME	5.9	-29.7	-30.1	-27.3	-20.5	-13.1	-9.2	3.9	-15.1	14.8
	LSE	11.0	-31.0	-31.2	-33.4	-25.3	-21.2	-18.6	2.6	-29.6	10.2
Services	SME	-0.5	-18.4	-18.1	-16.1	-11.8	-9.2	-5.9	3.3	-5.4	8.6
	LSE	0.7	-29.6	-31.9	-26.5	-22.9	-22.7	-20.8	1.9	-21.5	7.2
Germany	SME	5.7	-23.3	-23.5	-19.5	-14.4	-11.1	-8.3	2.8	-14.0	10.8
	LSE	9.3	-25.7	-28.2	-23.7	-18.0	-16.2	-12.4	3.8	-21.7	10.3
Current situation	SME	8.1	0.1	-2.2	-2.3	-0.4	-0.5	0.9	1.4	-7.2	1.5
	LSE	12.7	-7.5	-9.0	-9.9	-5.4	-8.6	-8.5	0.1	-21.2	1.3
Expectations	SME	3.1	-43.0	-41.7	-34.6	-27.0	-20.8	-17.0	3.8	-20.1	18.2
	LSE	5.7	-41.1	-44.4	-35.8	-29.1	-23.2	-16.4	6.8	-22.1	17.5
Employment expectations	SME	13.1	0.4	-1.4	0.7	1.2	6.6	3.1	-3.5	-10.0	3.7
	LSE	18.5	2.9	2.8	4.8	3.1	4.4	4.5	0.1	-14.0	0.5
Sales price expectations	SME	34.9	42.5	39.6	34.1	26.2	20.9	14.0	-6.9	-20.9	-18.4
	LSE	38.9	39.1	39.7	35.3	28.9	23.6	15.0	-8.6	-23.9	-15.5
Export expectations of manufacturing	SME	5.2	-19.6	-19.2	-17.1	-11.4	-10.0	-10.9	-0.9	-16.1	7.9
	LSE	6.4	-9.2	-8.1	1.6	-1.1	-0.2	2.7	2.9	-3.7	5.7

Sources: 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.