

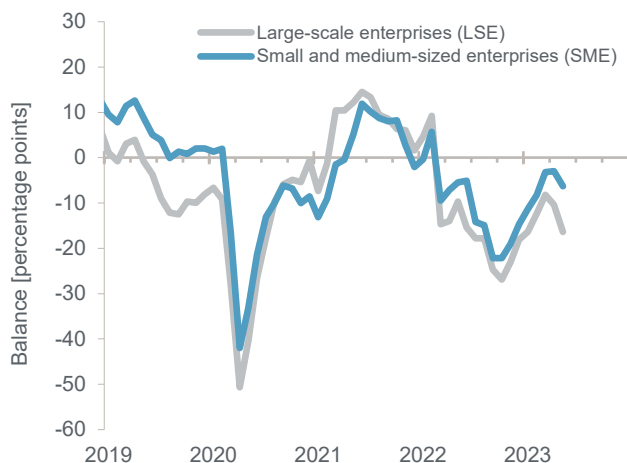
# »» SME business sentiment: situation OK, expectations more pessimistic again

6 June 2023

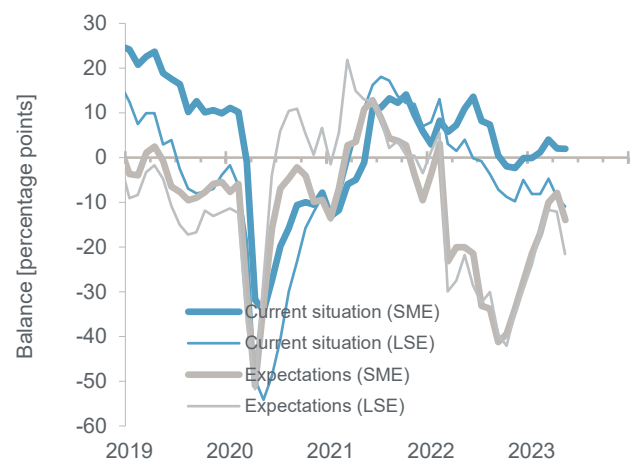
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- SME business sentiment drops for first time after six consecutive increases
- Situation assessments moving sideways, expectations increasingly pessimistic
- Sentiment among large enterprises has turned significantly bleaker
- Sales price expectations continue trending downward

KfW ifo Business Climate Index



KfW ifo sentiment components



Source: KfW Research, ifo Institute

## Sentiment rebound has stalled

The recovery in SME business sentiment is taking a break. After six consecutive rises, in April it was almost back to its historic average, which is marked by the zero line. Yet in May it drops by 3.3 points to -6.3 balance points. This was caused by a sharp decline in business expectations:

- In late summer and autumn of 2022, businesses' expectations had dropped to a low recently only seen in the financial and COVID-19 crisis. This was followed by a rebound after the threat of a natural gas shortage dissolved, state support measures were expanded and wholesale energy prices began trending sharply downward. SMEs' business expectations are now falling again for the first time, and by a noticeable 6.1 points to -14.0 balance points.
- Situation assessments, on the other hand, are currently trending sideways (-0.1 points) on a roughly average level (2.0 balance points). The SME business cycle is likely to roughly stagnate.

## Mixed sectoral development

The economic sectors exhibited very mixed trends in May. Whereas sentiment in manufacturing SMEs deteriorated noticeably (-5.4 points), especially in retail and wholesale (-9.5 and -10.3 points), construction and civil engineering trended slightly upward (+0.5 points), as did services (+0.3 points). After converging temporarily, sentiment is now diverging again quite significantly, in the two large sectors of manufacturing and services. In manufacturing, situation assessments as well as expectations are slipping into negative territory again. Service providers, on the other hand, reported a better than average business situation which improved again in May, but more pessimistic expectations. This appears to be a continuing sign of the global shift in consumption back to services and away from goods. Besides, manufacturers are likely to be feeling the impact of global monetary tightening more strongly and, to a certain degree, a decline in competitiveness. One reason for the renewed decline in sentiment in May could also be increasing disenchantment with the economic recovery in China. At the same time, despite turnovers trending downward in real terms since early 2022, SME retailers have reported a surprisingly good business situation

for months now. But here, too, situation assessments fell significantly in May, and expectations were clearly more pessimistic.

### **Sentiment among large enterprises clouded over noticeably**

Business confidence among large enterprises fell even more steeply in May (-6.0 points) than among SMEs. Sentiment among large enterprises is currently well below that of SMEs (LEs: -16.4 vs. SMEs: -6.3 points), particularly as a result of significantly worse situation assessments (LEs: -10.9 vs. SMEs: +2.0 balance points). Situation assessments developed again more negative among large enterprises than SMEs in May, falling by -2.1 points, although it was primarily large enterprises' expectations that fell sharply (-9.5 points). Specifically, it is in the trade and services sectors that large enterprises are now much more pessimistic than SMEs, while their mood in the manufacturing and construction sectors was slightly better but converged again with SMEs in the construction sector as a result of a drop in sentiment in May.

### **Price pressure continues to ease noticeably**

The sales price expectations of enterprises of both size classes continued trending downward unabated in May. After rising to an all-time high a year ago, they are now at 4.3 balance points among SMEs and 0.4 balance points among large enterprises – very close to their historic average, which should be roughly compatible with a 2% inflation rate. Significantly lower employment expectations also indicate a normalisation of inflation rates.

### **Sobering expectations**

The KfW ifo Business Climate Index has interrupted or ended its rebound from the depths of 2022 even though sentiment has not yet fully normalised. Enterprises remain sceptical about their business outlook and indeed, economic headwinds continue to blow hard as monetary policy around the world is putting on the brakes and inflation-induced purchasing power losses are reverberating. Recent disappointment about the recovery in China and omnipresent geopolitical risks in connection with Germany's most important trading partner (by turnover) are making matters worse. After the technical recession in the past winter half-year, we nevertheless expect the German economy to return to a moderate path of growth in the current quarter and GDP to contract only minimally in 2023 as a whole. In the past quarter, growth was slowed primarily by the slump in public-sector consumption, which will hardly repeat itself to the same extent. Furthermore, significant increases in nominal wages will stabilise private consumption, and production will benefit from the dissolution of supply bottlenecks, at least in the short term. In any case, the KfW-ifo SME Barometer delivers a positive message with respect to the development of inflation: The share of enterprises planning to increase their prices in the coming months has dropped to the level typically seen since the beginning of the timeseries in the year 2005. The chances are therefore good that inflation in Germany will be close to 2% again in the foreseeable future.

## KfW-ifo SME Barometer in figures

Balance [Percentage points]*		Month/Year							m-o-m	y-o-y	3m-o-3m
		May 2022	Dec 2022	Jan 2023	Feb 2023	Mar 2023	Apr 2023	May 2023			
<b>Business climate</b>											
Manufacturing	SME	-9.4	-16.8	-12.3	-9.1	-6.1	-4.8	-10.2	-5.4	-0.8	5.7
	LSE	2.9	-15.5	-11.1	-10.5	-2.3	-1.9	-6.3	-4.4	-9.2	8.9
Construction	SME	-6.4	-16.4	-16.4	-14.9	-12.0	-13.0	-12.5	0.5	-6.1	3.4
	LSE	-8.4	-13.1	-10.5	-6.0	-11.3	-0.3	-7.5	-7.2	0.9	3.5
Retail trade	SME	-6.4	-16.6	-10.3	-0.7	1.8	5.6	-3.9	-9.5	2.5	10.4
	LSE	-26.1	-21.8	-18.2	-8.8	-11.2	-15.8	-14.6	1.2	11.5	2.4
Wholesale trade	SME	-9.1	-19.6	-12.9	-10.2	-9.3	-10.7	-21.0	-10.3	-11.9	0.6
	LSE	-7.7	-24.4	-20.7	-18.2	-15.8	-17.4	-34.0	-16.6	-26.3	-1.3
Services	SME	-1.4	-11.7	-9.0	-5.8	1.7	0.4	0.7	0.3	2.1	9.8
	LSE	-16.6	-22.5	-22.3	-20.4	-17.2	-19.4	-24.2	-4.8	-7.6	1.5
<b>Germany</b>	<b>SME</b>	<b>-5.5</b>	<b>-14.7</b>	<b>-11.4</b>	<b>-8.3</b>	<b>-3.2</b>	<b>-3.0</b>	<b>-6.3</b>	<b>-3.3</b>	<b>-0.8</b>	<b>7.3</b>
	<b>LSE</b>	<b>-9.7</b>	<b>-18.1</b>	<b>-16.4</b>	<b>-12.4</b>	<b>-8.2</b>	<b>-10.4</b>	<b>-16.4</b>	<b>-6.0</b>	<b>-6.7</b>	<b>4.0</b>
Current situation	SME	11.0	-0.1	-0.1	1.2	4.1	2.1	2.0	-0.1	-9.0	2.4
	LSE	4.0	-5.0	-8.1	-8.1	-4.7	-8.8	-10.9	-2.1	-14.9	-1.1
Expectations	SME	-20.1	-27.6	-21.6	-17.0	-10.1	-7.9	-14.0	-6.1	6.1	11.4
	LSE	-21.8	-29.5	-24.0	-16.6	-11.7	-12.1	-21.6	-9.5	0.2	8.2
<b>Employment expectations</b>	SME	10.3	1.3	6.0	3.5	5.4	5.1	2.3	-2.8	-8.0	0.7
	LSE	15.5	3.2	4.2	4.1	3.0	2.3	-0.3	-2.6	-15.8	-2.2
<b>Sales price expectations</b>	SME	44.3	26.2	21.1	14.2	11.1	8.1	4.3	-3.8	-40.0	-12.7
	LSE	48.4	28.8	23.9	15.2	10.7	5.1	0.4	-4.7	-48.0	-17.2
<b>Export expectations of manufacturing</b>	SME	-9.4	-11.0	-9.9	-11.0	-10.6	-8.1	-10.3	-2.2	-0.9	1.0
	LSE	-0.4	-0.7	-0.3	2.3	3.1	2.9	-3.1	-6.0	-2.7	0.5

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 timeseries 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 timeseries 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.