THE FUTURE OF THE GERMAN MITTELSTAND 2020

Finanzgruppe
Deutscher Sparkassen-
und Giroverband

6 quick facts

S-Mittelstand Fitness Index sees sharp fall due to coronavirus.

After a slight decline in 2019, the S-Mittelstand Fitness Index has dropped below its 2009 level in 2020. The recovery process is expected to start quickly, but it will be highly sector-specific and extend over a long period in some cases. Whereas some industries are only slightly affected by the corona pandemic, many will not return to their pre-crisis level even by the end of 2022. The S-Mittelstand Fitness Index does not typically reflect the situation for freelancers, individual professionals or the smallest companies.

Fast growth in borrowing and liquidity at corporate clients of savings banks.

Many SMEs are investing despite the crisis, but in some cases also specifically because of it. H1 2020 figures from the savings banks show a 25% increase in lending commitments for investments. Strong growth in loan portfolio, particularly in the hospitality sector. Liquidity buffer for all companies up by € 10 billion.

Direct insights from corona-related advisory meetings with German mid-market companies.

Three quarters of all companies have business relations with a company in the Savings Bank Finance Group in Germany. Especially at such a time of crisis, local advisers are having many meetings with their corporate clients. Our survey of the Mittelstand experts at all 376 German savings banks reveals how adaptable the companies are. Many companies are very willing to keep investing in the future of their business. Insolvency risks are said to be only moderate.

2019 was a good year for growth overall, with big differences between sectors.

The domestic economy (construction, services, retail) was driving growth until the corona crisis hit. Export-led sectors such as metal-working, engineering and automotive were already slowing before the crisis, however.

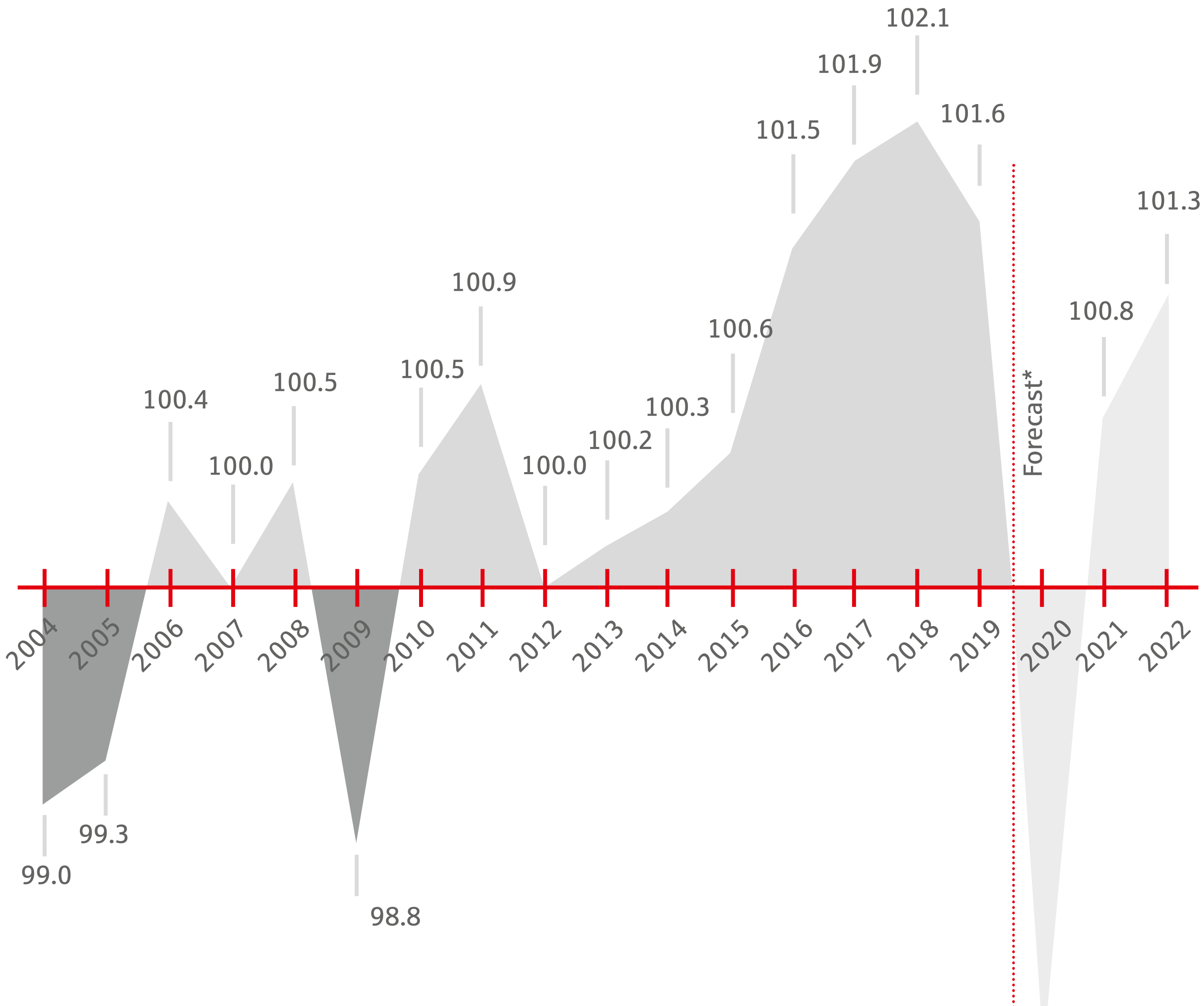
Steepest falls in tourism, event management, hospitality, creative industries and automotive.

Not all sectors are suffering. Construction, healthcare and social services have continued to grow in 2020. Corona has had the biggest impact on tourism, event management, hospitality, the creative industries and car makers. Sales are expected to fall by an average of 5.7% across all sectors in 2020. Profits are mostly harder hit than top-line growth. Most companies will remain in the black, however. This means that company equity is not expected to contract so severely. Companies are managing to stay in good financial shape. Simulations show that about 5% of SMEs are expecting to suffer a loss for the full year 2020 due to the corona pandemic.

Mittelstand has saved for hard times.

The Mittelstand is benefiting from its great financial resilience in this crisis. High liquidity reserves and strong equity ratios thanks to the steady retention of earnings will enable most companies to overcome this crisis on their own. However, some companies have been hit harder than they can cope with themselves. And for these businesses the many different forms of state support are vitally important.

S-Mittelstand Fitness Index 2020



Average fitness 2004 to 2014 = 100,
Companies with sales of up to €250m
*Forecasts for 2020 to 2022

Source: DSGV-Branchendienst

Athlete or couch potato?

The Future of the German Mittelstand survey is based on an analysis of performance indicators for corporate clients and corporate lending by the savings banks, as well as on the DSGV sector forecasts. The study examines the economic situation and outlook for small and medium enterprises in Germany. Its core component is the S-Mittelstand Fitness Index, which measures the long-term performance, productivity, innovation and financial strength of Mittelstand companies.

Athlete or couch potato: the S-Mittelstand Fitness Index shows what shape Germany's small and medium-sized businesses are in. What are the companies capable of? How productive are they and their employees? And how well are they set up for the future? Answers to these and other questions are provided by an analysis of selected performance indicators that DSGV carries out by scrutinising some 300,000 anonymous balance sheets every year. The data is used to compile the S-Mittelstand Fitness Index, which provides a benchmark for the condition and sustainability of the German Mittelstand.

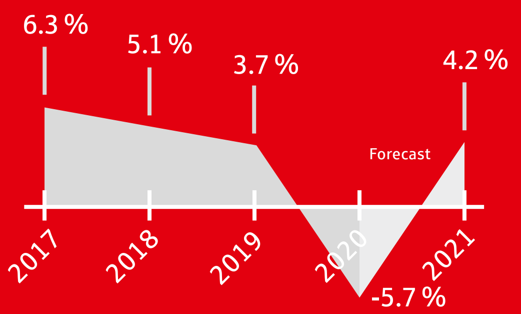
The S-Mittelstand Fitness Index 2020 in detail

Performance: business and profits

How attractive are their markets, and how successful are the companies in them?

How fast are the companies growing?

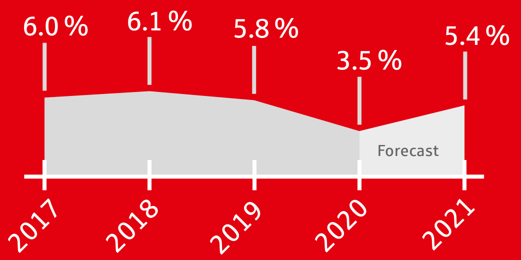
→ **Sales growth***



*Year-on-year change in sales

How profitable are the companies?

→ **Return on sales***



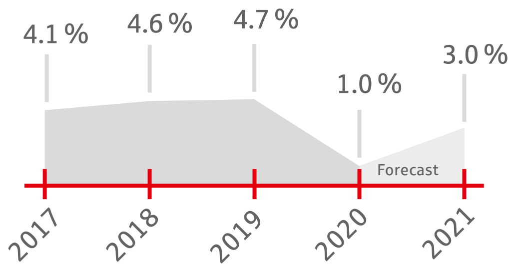
*Operating profit in relation to sales.

Strength: investment and innovation

How much are companies investing and how innovative are they?

How much are companies investing?

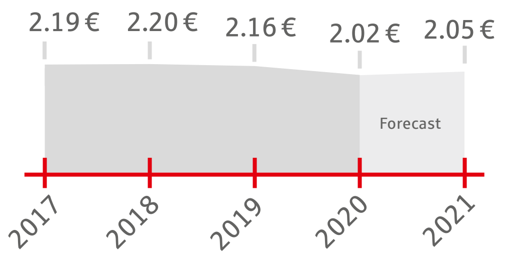
→ **Fixed asset growth***



*Year-on-year change in property, plant and equipment.

How much revenue is generated for every euro of fixed assets?

→ **Asset effectiveness***

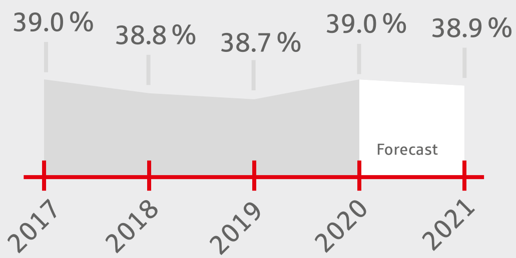


*Sales in relation to property, plant and equipment.

Stamina: stability and sustainability

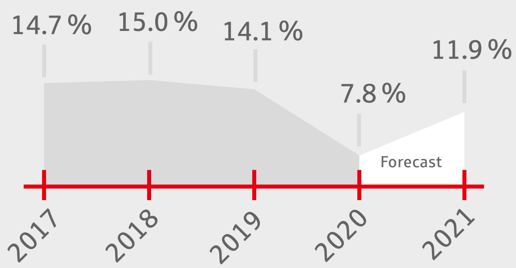
How solid is the companies' financing structure and how profitable are they for their owners?

How financially stable are the companies?
→ **Equity ratio***



*Equity in relation to total assets.

How well is the capital employed?
→ **Return on equity***

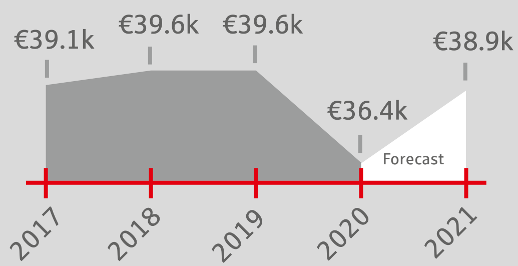


*Operating profit in relation to equity.

Team spirit: employees and their contribution

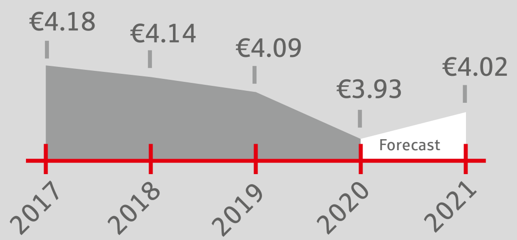
How productive are the company's employees and what do they contribute to its success?

What does each employee contribute to a company's success?
→ **Gross profit per employee***



*Sales less cost of material and staff costs in relation to total workforce.

How much revenue is generated for every euro of staff costs?
→ **Personnel productivity***



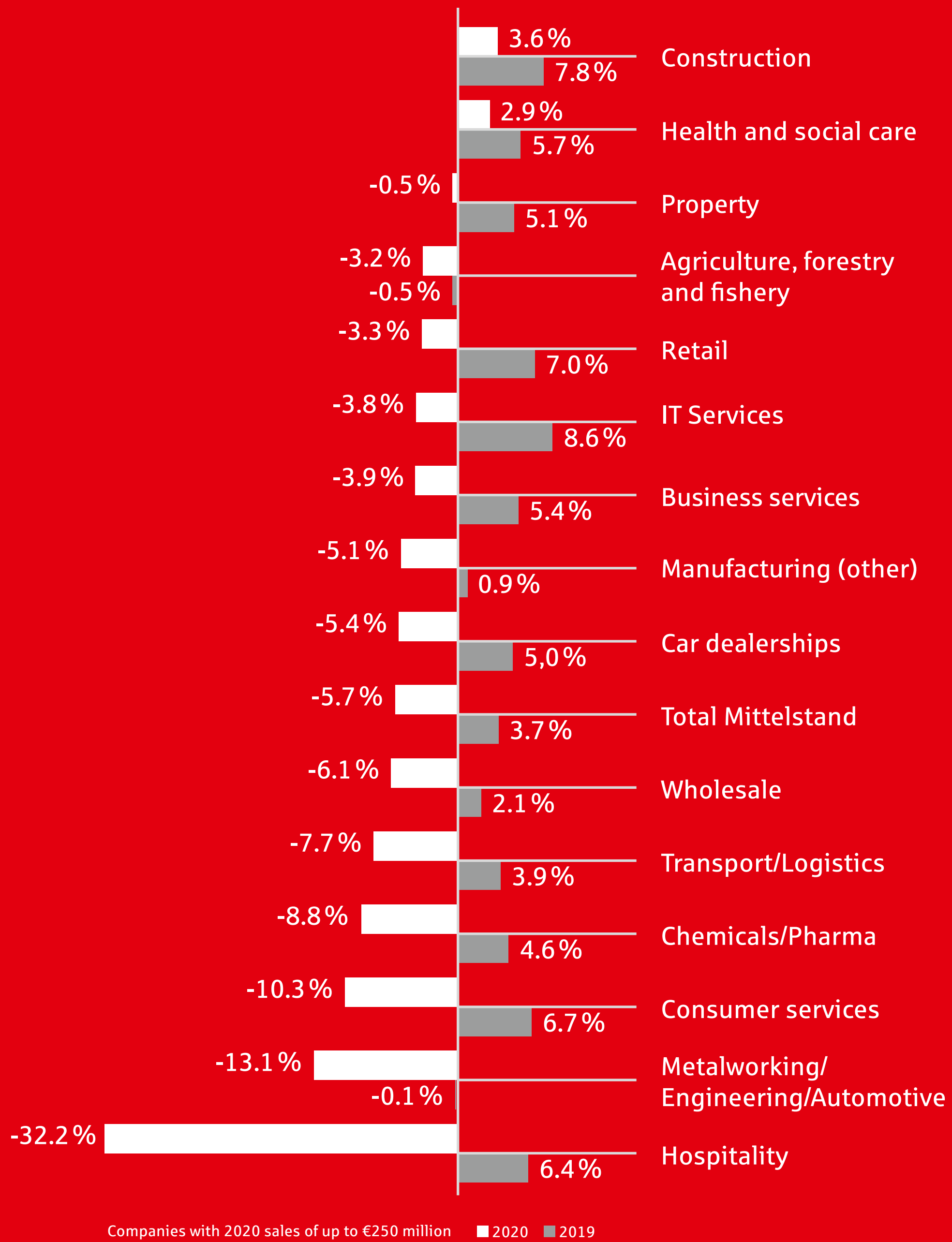
*Sales in relation to staff costs

Focus: Mittelstand has saved for hard times

The corona pandemic hit the German Mittelstand hard and without warning. It put a sudden stop to years of growth in many industries. The worst falls in sales are expected in tourism, event management, hospitality, the creative industries and car manufacturers. But there are also a few sectors that are managing to grow in the current crisis. Construction, as well as healthcare and social services, all reported positive growth rates in 2020. And then there are plenty of niche markets that are currently seeing something like a mini-boom. Generally speaking, the collapse in sales is without precedent in post-war Germany, however, and company profits have fallen even faster.

Simulating the performance of key balance sheet figures on the basis of more than 300,000 individual balance sheets for larger Mittelstand companies shows that most companies are still managing to stay profitable thanks to their flexible cost management. On average, these profits are slightly increasing the amount of retained earnings. What the simulations also show is that around 5% of companies will make a loss as a result of covid-19. Extrapolated for the economy as a whole, this represents a good 18,000 companies in the category of €2-50 million in annual sales.

Sales growth 2020 and 2019



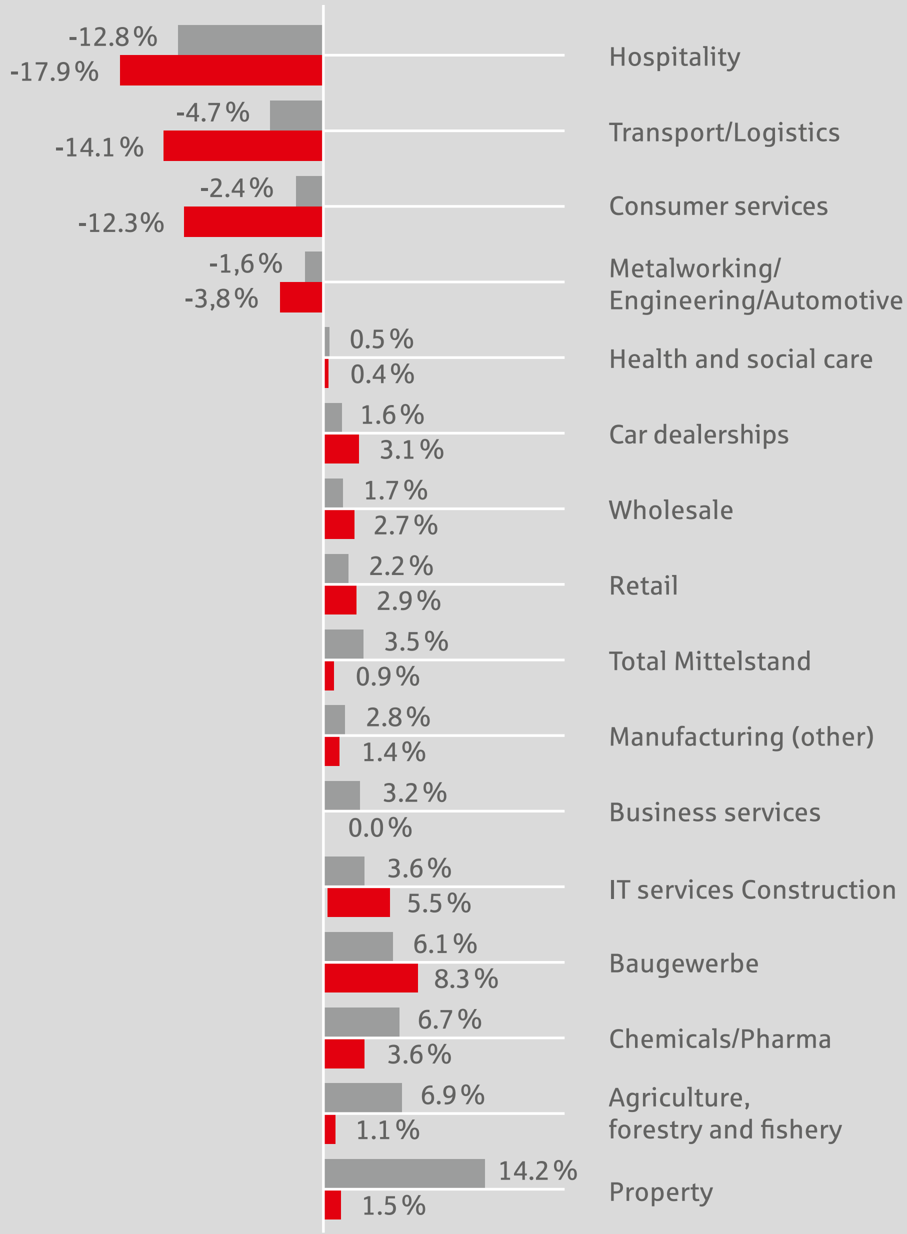
Companies with 2020 sales of up to €250 million
Source: DSGV-Branchendienst

The crisis came as a surprise, but the Mittelstand was not unprepared. Many years of strong profits did not go to waste. Our balance sheet analysis shows that companies have performed excellently since the last big crisis in 2009. On a consistent basis the bulk of earnings was not paid out as dividends, but rather retained and invested in the companies themselves. Equity ratios and liquidity reserves have grown significantly in all sectors since then, assets are being used very efficiently and the employees are highly productive. This is a great help to companies in the current difficult situation. Their outstanding financial stability enables most businesses to cope with the crisis on their own by offsetting temporary losses against equity.

But although many companies are able to manage the situation themselves, there are others who do need financial assistance. The temporary suspension of the obligation to file for insolvency, short-time working hours, subsidies for operating costs and special loans all give companies the time and money they need to rebuild their businesses. Then there are the measures to boost consumption, such as the temporary reduction in the VAT rate. Altogether, these policies safeguard employee's jobs and income and bolster demand in key consumer sectors such as restaurants and retail.

The obligation to file for insolvency has been suspended until year-end, which makes it possible for companies to remain on stand-by, ready to participate actively when the economy picks up again, and indeed to enable this upturn. Every company that had ceased trading because of covid-19, sold its assets to pay off its creditors and made its staff redundant would have been sorely missed when the economy starts up again. But to ensure the risks remain quantifiable, this measure can only apply for a limited period of time.

Return on sales and equity growth in 2020 in %

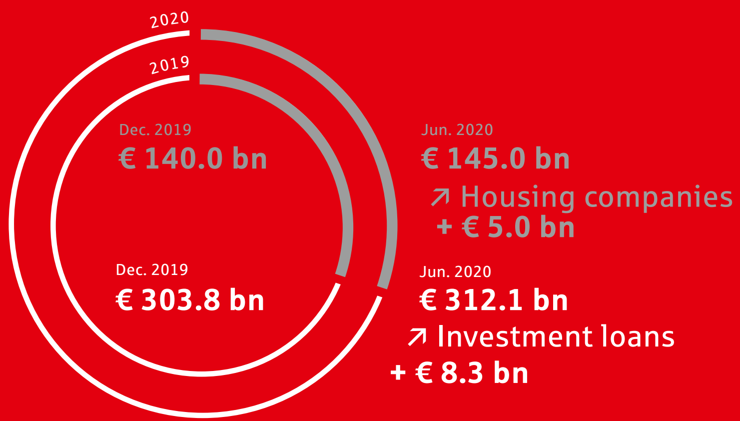


Companies with sales of up to €250 million
Source: DSGV-Branchendienst

Latest figures for 2020 from the savings banks

Investment continues, even at times of crisis. In the first half of 2020 the savings banks approved € 54 billion in new corporate loans. € 39 billion of the total was for investment, which is 35% more than in the same period a year ago. On balance, the total volume of corporate loans increased by € 13 billion.

Growth in corporate loans*



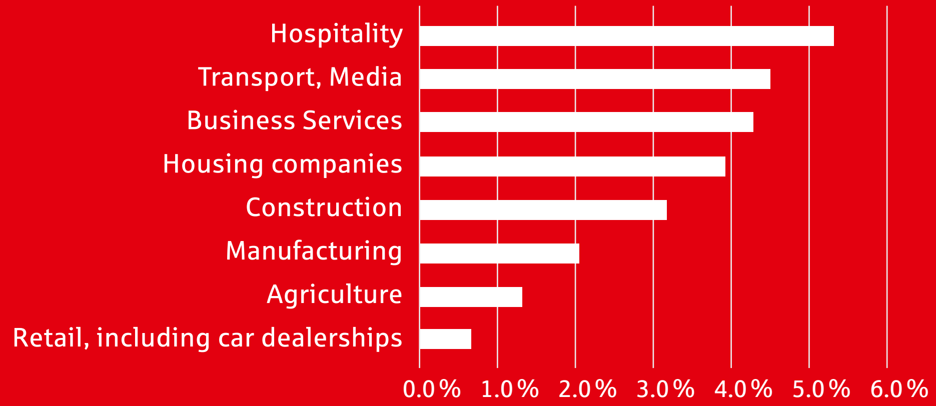
*Lending by savings banks in Germany.

Source: DSGV

The hospitality industry saw particularly fast increases in percentage terms. A strong performance in lending for commercial housing projects also shows that the construction industry is not being held back by the crisis.

As expected, some of the credit growth has been kept in companies' treasuries as a liquidity reserve to see them through the crisis. This pattern was also visible in the last major crisis in 2009. Deposits from corporate clients with savings banks rose accordingly in the first half-year 2020 by a good € 10 billion or around 7%. On the other hand, many SMEs have also made important investments in their business during the pandemic.

New lending in selected industries*



*Net change since start of year as of 30 June 2020, savings bank business.
Source: DSGV.

Liquidity reserves + 7.1%

Savings bank business.

Source: DSGV

S-Mittelstand Fitness Index 2020

What are the hot topics for the German Mittelstand? What are the latest trends in terms of investment and financing? Every year, the corporate client advisers at the savings banks discuss these and other topics with Germany's small and medium-sized enterprises. Three quarters of all the companies in Germany have a business relationship with the Savings Bank Finance Group. At the high point of the corona pandemic the staff of the 376 savings banks held a large number of advisory meetings with their corporate clients. The S-Mittelstand Fitness Index presents the essence of what our Mittelstand experts took away from these meetings. Insights from the market leader: direct, up-to-date, relevant.

Current news: dealing with the crisis

Exactly a year ago our survey indicated that the German Mittelstand was already actively preparing for an economic downturn. After years of growth, there were already signs that the economic expansion in Germany was slowing. Companies were taking action by making their businesses more flexible, outsourcing certain functions and implementing cost-cutting programmes. When the corona pandemic hit in spring 2020, these efforts served many companies well. This year's survey now looks specifically at how companies are acting to cope with the crisis and at the prospects they foresee for when it is over.

1. Insolvency risk

The question:
How high is the risk that Mittelstand clients become insolvent because of the economic effects of the corona pandemic?

The experts' answer:
In the opinion of slightly over three quarters of all the finance experts surveyed, less than 2% of corporate clients will have to file for insolvency in the next 6 months (regardless of the suspension of the mandatory insolvency filing).

2. Investment patterns

The question:
Are corporate clients still pursuing long-term/strategic investment projects in the wake of the corona pandemic?

The experts' answer:
86% of the experts surveyed consider that their corporate clients are generally standing by their long-term investment plans, but have put them on hold temporarily. 11% of the Mittelstand experts even reported that their corporate clients are still investing without change. Only 3% said that investments had been abandoned altogether.

3. Companies' adaptability

The question:
Are companies reacting to the new situation partly by adapting their business models?

The experts' answer:
83% of those surveyed said that their corporate clients had responded flexibly and adapted their business models. So clothing manufacturers switched to the production of medical protective equipment, for instance. 3% reported even more radical changes to the business model, such as engineering companies that moved into medical devices. 14% found that their corporate clients maintained their established business models unchanged.

4. Prospects for recovery

The question:
In which sectors are the prospects for a medium-term recovery good? Where should long-term disruption be expected?

The experts' answer:
Almost all the corporate finance experts expect a rapid recovery in the construction, property, services, agriculture and logistics sectors. Positive expectations predominate for industrial sectors at 64%, but a good third of respondents is anticipating longer-term difficulties. For the hospitality sector, retailers, and the travel industry in particular, a majority of those surveyed think that things will not return to normal without major changes and far-reaching cuts.