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## What Is Behind the ifo Business Climate? Evidence from a Meta-Survey

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# What Is Behind the ifo Business Climate? Evidence from a Meta-Survey

## Abstract

The ifo Business Climate Index is considered as one of the most important leading indicators for the German economy. It is based on a monthly survey of about 9,000 companies located in Germany and composed of two main questions from the monthly questionnaire: the assessment of the current business situation and the business expectations for the next six months. The terms 'business situation' and 'business expectations' are formulated deliberately vague and not explicitly defined. Thus, each survey participant can consider its own main driving factors. But what are these underlying factors? Do they differ between sectors or by firm size? To answer these questions, we conducted a meta-survey among all survey participants. The results suggest, that especially internal company factors, such as the profit situation, demand, and turnover, are crucial. Generally, using a principal component analysis we show, that these factors can be decomposed into three components: (1) the overall financial situation, (2) the demand and order situation, and (3) external influences. Our findings provide some insights concerning the high predictive power of the ifo Business Climate Index and its components. Furthermore, the identified factors might also be useful for business cycle analyses in practice.

JEL-Codes: C530, C830, L200.

Keywords: ifo Business Climate, business expectations, business situation, meta-survey.

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# 1 Introduction

The Ifo Business Climate Index, derived from the Ifo Business Survey (IBS), is widely recognized as one of the most critical leading indicators for the German economy due to its ability to influence financial markets and provide early signals of economic shifts (Mittnik et al., 2013; Kerstenfischer and Schmeling, 2024). Each month, approximately 9,000 companies across Germany participate in the survey, yielding a sample that is broadly representative of the German economy, albeit with a slight over-representation of larger firms (Hiersemenzel et al., 2022). The IBS, initially launched in 1949 for the manufacturing sector, has been progressively expanded to include retailing (1950), wholesaling (1951), construction (1956), and, more recently, the service sector in 2001. The harmonization of survey questions across all sectors allows for comprehensive analyses of the overall economy, as detailed by Sauer et al. (2023).

Recent surveys conducted in 2019 and 2023 indicate that over 90% of respondents hold senior management positions, such as owners, CEOs, or department heads (Sauer and Wohlrabe, 2019; Hennrich et al., 2023), enhancing the credibility and reliability of the survey data. The IBS encompasses questions covering a wide range of firm activities, including assessments of current business conditions (*status quo*), recent developments (*ex post*), and future plans and expectations (*ex ante*). The survey places particular emphasis on core variables such as production levels, pricing strategies, and employment figures. In addition to these core questions, the IBS includes supplementary questions on topics of current economic relevance or specific company information relevant to research projects (Demmelhuber et al., 2022). The responses are primarily qualitative, using a three-point Likert scale, which captures the nuanced perspectives of firms.

At the heart of the IBS are two fundamental questions: the assessment of the current business situation and expectations for the next six months. These questions form the foundation of the widely recognized Ifo Business Climate Index (Sauer and Wohlrabe, 2018). The precise wording of these core questions is as follows:

- Business situation: 'We assess our current business situation as: good/satisfactory/bad.'

- Business expectations: 'The expectations for the next 6 months: Our business situation is expected to: become more favorable/remain roughly the same/become more unfavorable.'

Despite the importance of these questions, the ifo Institute does not provide explicit definitions for the terms 'business situation' and 'business expectations,' allowing for varied interpretations among companies. This ambiguity raises critical research questions: What factors do companies consider when responding to these questions? How does the relative importance of these factors vary across different firms and sectors? Moreover, how do these factors collectively contribute to the overall assessment of the business climate, and what does this imply for the forecasting power of the ifo Business Climate Index?

To address these questions, we conducted a comprehensive meta-survey among all IBS participants to evaluate the importance of various factors influencing firms' assessments of their business situation and expectations. The factors considered in this meta-survey range from firm-specific elements, such as internal financial performance and market dynamics, to broader external influences like sectoral trends and macroeconomic conditions. Additionally, the meta-survey investigates the benchmarks companies use to assess their current business situation and the time horizons they adopt for formulating business expectations.

The extensive use of IBS results in forecasting, business cycle analysis, and economic research underscores the significance of understanding the underlying factors influencing these survey responses.<sup>1</sup> Lehmann (2023) provides a comprehensive review of the use of ifo indicators in economic forecasting, highlighting their competitive advantage. This study aims to build on this foundation by uncovering the factors that explain why the ifo Business Climate Index has demonstrated strong forecasting properties.

Our analysis reveals that internal company factors – such as profit situation, demand, and turnover – exert the most significant influence on firms' assessments of both the business situation and expectations. A Principal Component Analysis (PCA) further categorizes these factors into three main components: the firm's financial situation, demand and order

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<sup>1</sup>Recent examples include Bachmann et al. (2013), Balleer et al. (2020), Buchheim et al. (2022), Enders et al. (2022), Link (2019), Dovern et al. (2023), and Link et al. (2023).

conditions, and external influences. These insights deepen our understanding of the key drivers behind the ifo Business Climate Index, enhancing its interpretive value for economic forecasting and business cycle analysis.

This paper is structured as follows: Section 2 provides detailed background information on the meta-survey, including its design, objectives, and methodology. Section 3 outlines the empirical approach and presents the main findings of the study. Finally, Section 4 discusses the implications of the results for economic forecasting and policy-making, concluding with suggestions for future research.

## 2 Background and Procedure of the Meta-Survey

In 1952, 1956 and 1963, the ifo Institute already conducted meta-surveys among all participating companies to collect background information about the IBS. They were called 'We are testing the business survey' and were limited to questions about the general relevance of the business survey as a method of data collection. Subsequent meta-surveys dealt with the answering behavior of the survey participants and focused on individual sectors: manufacturing (1976), construction (1978), and trade (2009).<sup>2</sup> However, no meta-survey had been simultaneously conducted for all sectors. This gap was closed in 2019. The ifo Institute performed a meta-survey among all survey participants of the IBS to uncover the most important factors for the assessment of the current business situation and of the business expectations for the next months. Moreover, the survey included questions about benchmarks for the assessment of the business situation and about the time perspective of the business expectations. In addition, further questions of the survey dealt with the response behavior of the participating companies regarding price setting, number of employees, order backlogs, and capacity utilization. Furthermore, information about the survey participants was collected. Finally, text fields for criticism and for suggestions for improvement were included.

The drafting phase of the questionnaire ran from January to May 2019. Survey experts and business cycle experts of the ifo Institute identified the relevant topics of the meta-

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<sup>2</sup>The results of the meta-survey in the trade sector can be found in Abberger et al. (2011).

survey and formulated the questions. Subsequently, the ifo Institute conducted pre-tests with selected participants from each sector. These pre-tests took place in the form of interviews by email or by phone to validate the survey questions, detect ambiguities in the wording of the questions, or to discover other important answer categories, that were still missing. This led to necessary adjustments of the questionnaire.

In total, 10,305 questionnaires were sent out on September 18, 2019. The data collection lasted until October 25. Table 1 shows the sample size and response rate by sector and by firm size. A total of 4,046 participants answered the questionnaire. This corresponds to an overall response rate of 39.3%. The response rates by sector range between 36.3% in the retailing sector and 47.9% in the construction sector. Differentiated by firm size<sup>3</sup>, smaller firms responded more frequently than large ones.

Table 1: Sample size and response rate by sectors and firm size

	<b>Total</b>	<b>Manufacturing</b>	<b>Services</b>	<b>Wholesaling</b>	<b>Retailing</b>	<b>Construction</b>
Questionnaires sent out	10,305	2,649	3,435	1,490	1,707	1,024
Share	100%	25.7%	33.3%	14.5%	16.6%	9.9%
By firm size						
1	29.6%	13.1%	3.6%	1.0%	4.2%	7.7%
2	30.5%	5.7%	6.0%	7.4%	10.1%	1.2%
3	18.6%	2.9%	11.9%	2.3%	0.9%	0.6%
4	8.7%	1.9%	4.2%	1.6%	0.7%	0.3%
5	12.6%	2.1%	7.5%	2.2%	0.7%	-
Questionnaires received	4,046	1,158	1,192	587	619	490
Response rate	39.3%	43.7%	34.7%	39.4%	36.3%	47.9%
Share by firm size						
1	33.6%	15.9%	3.7%	0.9%	3.6%	9.5%
2	29.7%	5.9%	5.6%	7.2%	9.6%	1.5%
3	17.8%	3.3%	10.6%	2.4%	0.9%	0.7%
4	8.4%	1.8%	3.7%	1.8%	0.7%	0.4%
5	10.5%	1.8%	5.9%	2.2%	0.5%	-

Note: The definition of firm size is stated in Table B1 in the Appendix.

<sup>3</sup>The companies can be divided into five firm size categories, with group one representing the smallest enterprises and group five the largest ones. Construction is only divided into four firm sizes. Detailed information on the firm sizes can be found in Table B1 in the Appendix.



## 3 Empirical Analysis

### 3.1 Methods

In this paper, we focus on three main issues from the meta-survey, which concern questions on the current business situation and the business expectations for the next 6 months:

1. What are the underlying factors of the business situation and the business expectations?

The participating companies were asked to classify the importance of various factors for the assessments of the business situation and the business expectations. They could assign values between 0 (no importance) and 6 (very high importance) to each factor depending on its degree of importance.

2. What are comparative benchmarks for the assessment of the current business situation?

Firms could choose between the business situation in previous months, the average situation in previous months or years as well as the expectations and goals for the current month.

3. How do the firms perceive or use the forecast horizon of the business expectations?

Participants of the IBS are asked about the “expectations for the next six months’. In the meta-survey the respondents were interrogated about their interpretation of the time designation. Firstly, they could choose between two options: the situation in six months (point of time) or the situation within the next six months (time period). Secondly, they were asked, whether they consider the change of the business situation or the upcoming business situation.

The exact wording (original and English translation) of the corresponding questions can be found in the Appendix.

First, we carried out a descriptive analysis of the data. Therefore, we quantified the respective importance of each factor by calculating the arithmetic mean. Besides the full sample, we report also results for sectors and by firm size.

Building on this descriptive analysis, we performed a Principal Component Analysis (PCA) for a better interpretation of the relation and importance of the underlying factors. PCA was first introduced by Pearson (1901) and developed independently by Hotelling (1933). The central idea is to reduce the dimensionality - and thereby the redundancies and the noise - of a data set with interrelated variables, while retaining as much as possible of the present variation in the data set. This reduction is achieved by transforming the variables to a new underlying set of uncorrelated variables, the principal components (PCs) (Jolliffe, 2002).

Our PCA transforms the original data matrix with the companies' responses to all variables into orthogonal components using a varimax rotation as proposed by Kaiser (1958). Therefore, we restrict the PCA to a complete case analysis, which means that all participants with missing variables are eliminated from the analysis. For the decision on the number of PCs we used the Kaiser rule (Kaiser, 1960). This rule says, that only components whose eigenvalues exceed one are retained. The idea of this rule is that any PC with an eigenvalue smaller than one contains less information than one of the original variables and, therefore, is not worth keeping. Table 2 shows that for the business situation as well as for the business expectations the result contains three PCs. These three PCs account for 58 percent of the total variation of the business situation and for 63 percent of the variation of the business expectations respectively.

Table 2: PCA - eigenvalues and explained variance

	Business situation			Business expectations		
	eigenvalues	variance	cum. variance	eigenvalues	variance	cum. variance
PC1	3.29	32.95	32.95	3.34	33.42	33.42
PC2	1.28	12.80	45.75	1.57	15.73	49.15
PC3	1.22	12.22	57.96	1.36	13.58	62.74
PC4	0.97	9.72	67.69	0.96	9.59	72.32
PC5	0.78	7.84	75.52	0.72	7.21	79.54
PC6	0.70	7.01	82.53	0.53	5.32	84.85
PC7	0.56	5.65	88.18	0.46	4.58	89.43
PC8	0.48	4.75	92.93	0.41	4.09	93.53
PC9	0.40	3.96	96.89	0.37	3.71	97.24
PC10	0.31	3.11	100	0.28	2.76	100

Abbreviations: cum. - cumulative.

Moreover, we performed the PCA separately on the sector level. The Kaiser rule resulted in a choice of three PCs for the business situation and the business expectations for each sector.

## **3.2 Results**

### **3.2.1 Influencing Factors for the Business Situation and the Business expectations: Overall Results**

The participating companies rated the importance of various factors influencing their assessments of the business situation and business expectations on a scale from 0 (no importance) to 6 (very high importance). Figure 1 presents the overall arithmetic mean for each factor. It is immediately apparent that there is only a slight difference between the importance assigned to factors for the business situation and those for business expectations, suggesting that companies perceive the determinants of their current state and future outlook in a similar manner. Moreover, all factors included in the survey were rated as having some relevance, with average ratings ranging from 3 (moderate importance) to 6 (very high importance).

'Profit situation' stands out as the most critical factor for both the current business situation and future expectations, followed closely by 'turnover' and 'demand.' In contrast, external factors, such as 'business constraints', 'economic policy framework,' 'sector sentiment,' and 'general economic sentiment,' are ranked lower in importance. This pattern clearly indicates that companies predominantly base their assessments on internal factors rather than external economic conditions.

While internal company factors are the most influential in shaping firms' assessments, it is also important to acknowledge the role played by broader, general factors 'sector sentiment' and 'general economic situation. Although these external factors were rated lower in importance compared to internal ones, they still contribute to the overall business climate perception. This suggests that firms are not entirely insulated from broader economic conditions and industry trends. These general factors likely provide context or a backdrop against which internal assessments are made, particularly in uncertain or volatile economic

environments. For instance, a negative shift in the general economic outlook or sector-specific challenges could temper otherwise positive internal assessments, or conversely, a favorable external environment might amplify the optimism derived from a firm's strong internal metrics. Thus, while internal factors remain paramount in the evaluation process, the moderate weight given to general economic conditions underscores their supplementary role in refining and contextualizing firms' business expectations and situational assessments.

The finding that internal factors are more important than external ones is crucial because it suggests that the survey captures firm-specific dynamics rather than just reflecting general economic trends that are already accessible to the public. If external conditions were more influential, the business climate index might risk merely mirroring widely known economic information, thereby losing its unique predictive value derived from proprietary firm-level insights.

To better understand the distribution of responses beyond the average ratings, Figures 2 and 3 display histograms of the importance scores assigned to each factor. These histograms reveal that a large majority of survey participants attributed at least some level of importance to all factors, with the rating of 0 (totally unimportant) being rarely selected. For the more crucial factors, such as 'profit situation,' responses are heavily skewed towards the upper end of the scale, with slightly more than 60% of participants assigning it the highest importance (6) for the business situation and slightly less than 60% for business expectations. Similarly, 'turnover' and 'demand' also show a significant concentration of responses in the highest categories, around 40%. In contrast, the factors rated lower in importance tend to exhibit a more normal distribution, with most responses clustered around the mid-range scores of 3 and 4. This distribution pattern further underscores the primacy of internal, firm-specific factors in shaping business sentiment as captured by the Ifo Business Climate Index.

Figure 1: Importance of the factors for the business situation vs. expectations

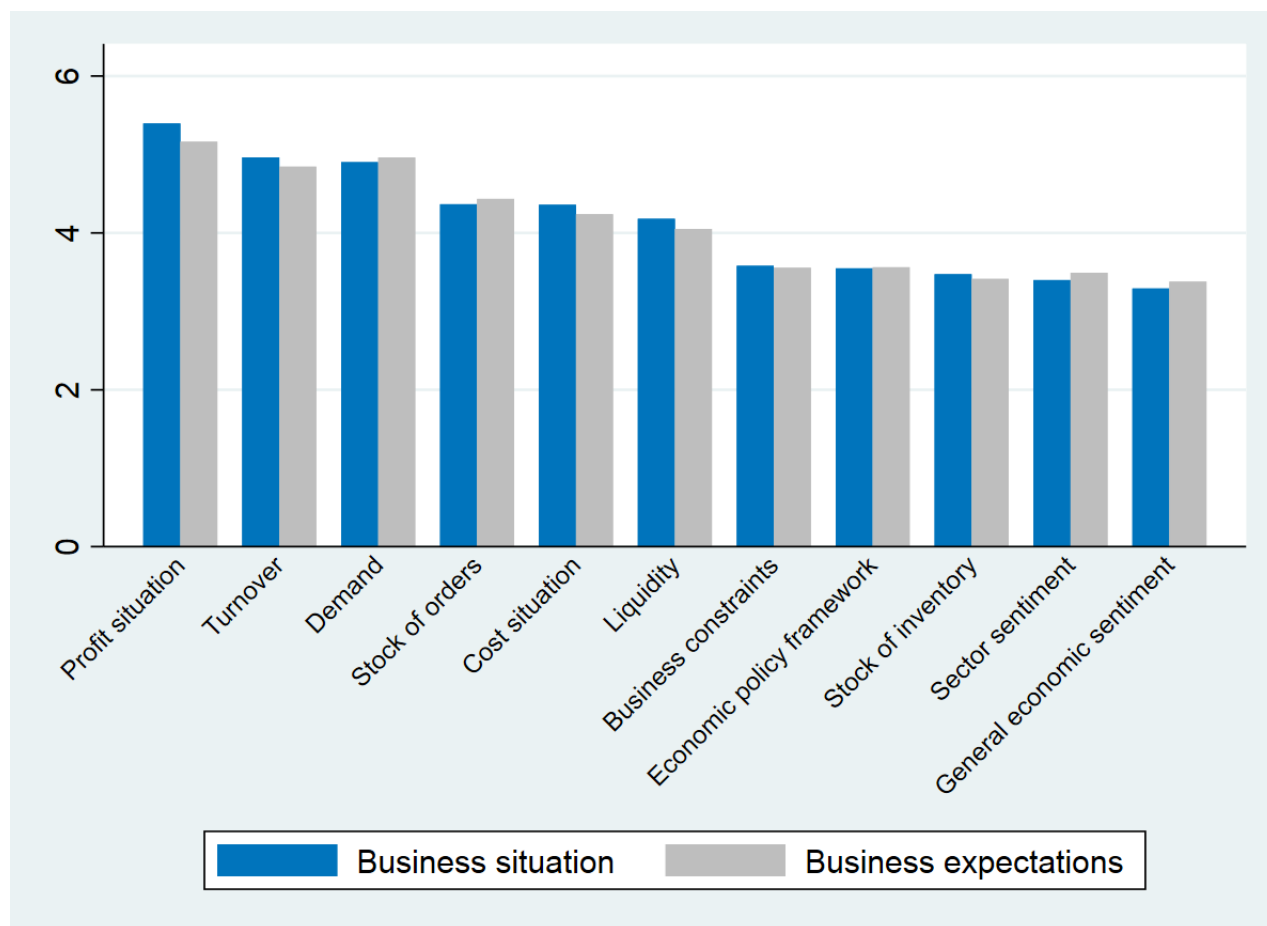


Figure 2: Business situation: Distribution of the response behavior of the participants

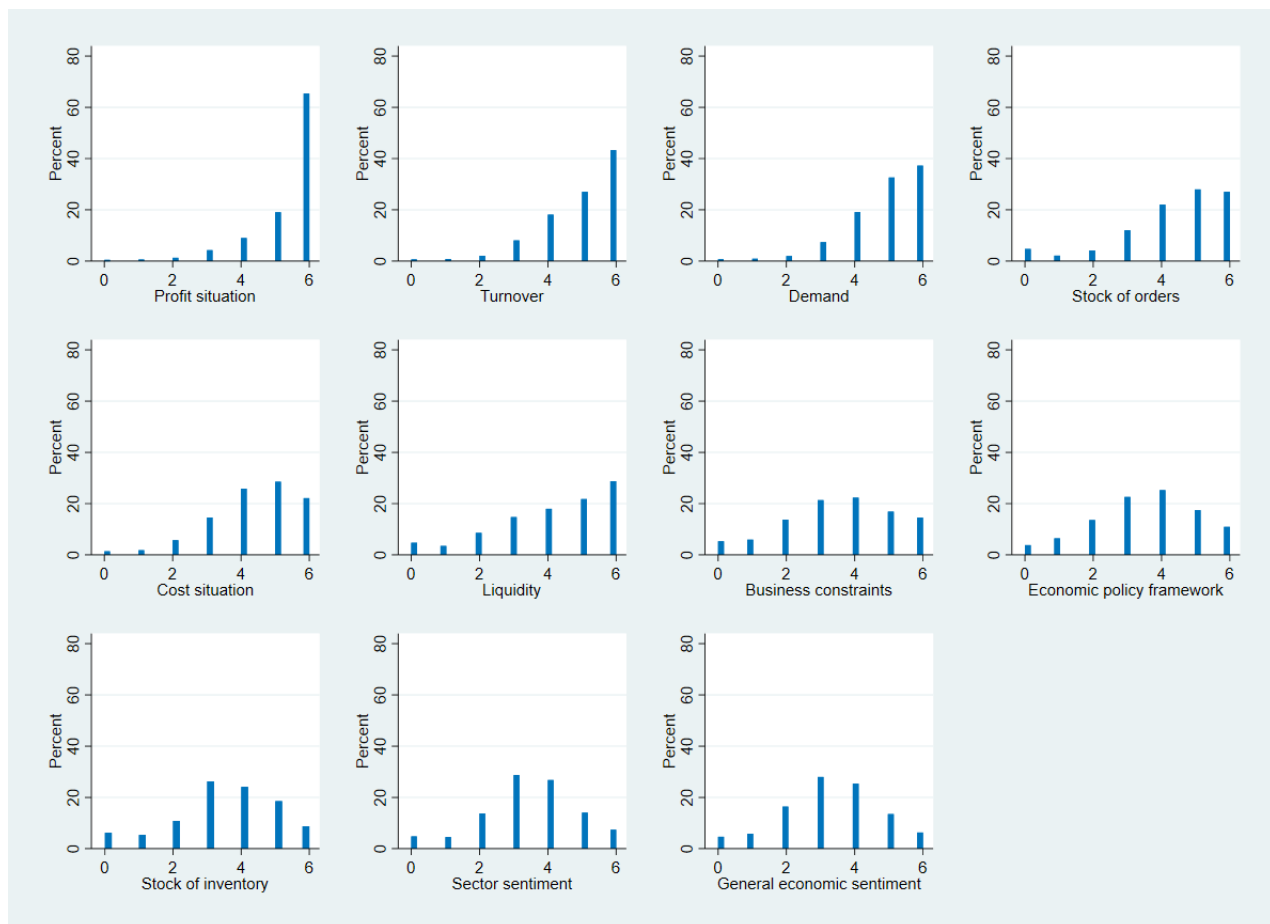


Figure 3: Business expectations: Distribution of the response behavior of the participants

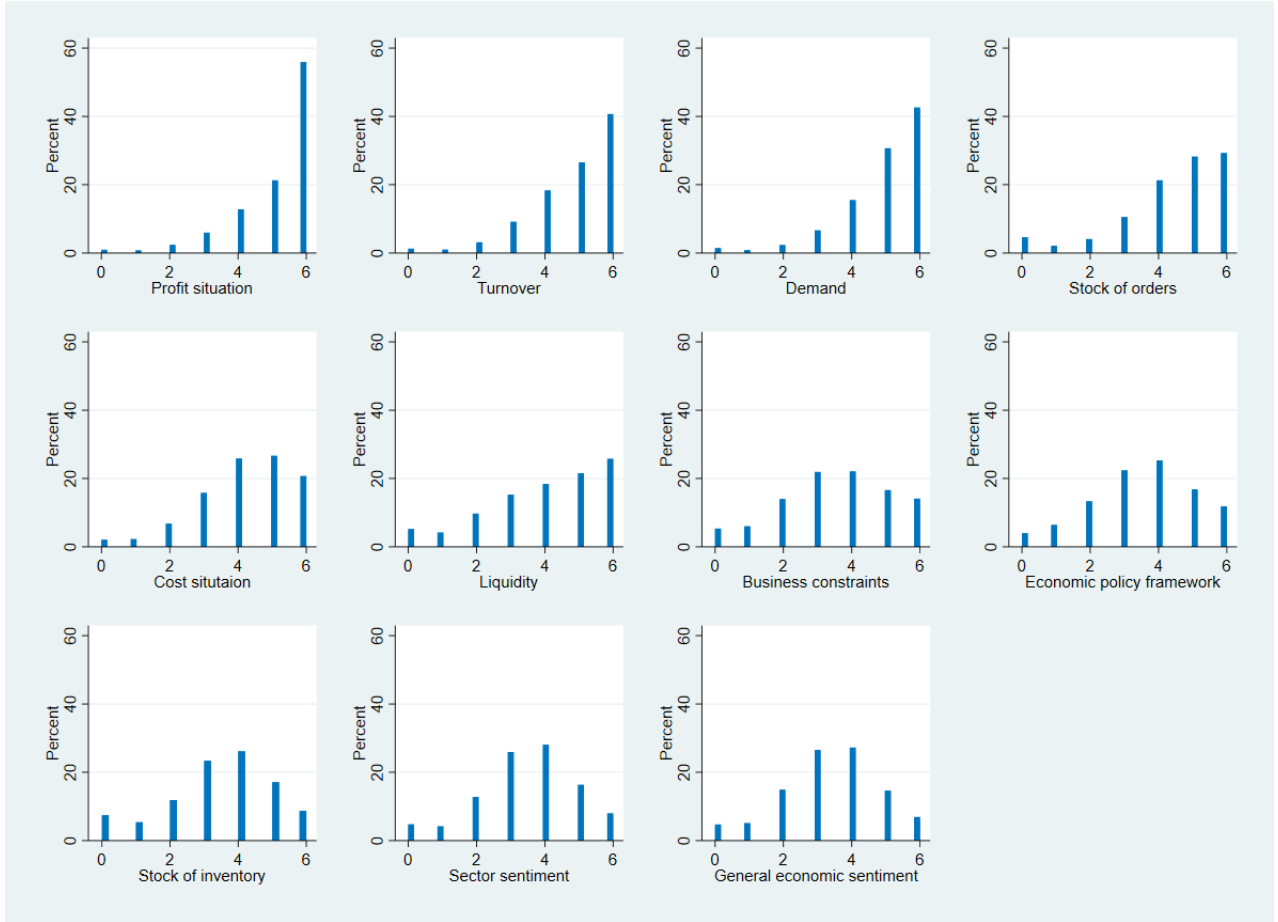


Figure 4 illustrates the similarity in response patterns between the business situation and business expectations across various factors. The bubble plots display the distribution of response combinations for each factor, with the size of each bubble representing the number of responses for a specific combination of importance ratings assigned to both the business situation and expectations. Notably, most factors exhibit a very high correlation (over 0.8) between their importance ratings for the business situation and business expectations, suggesting that firms generally apply consistent criteria when evaluating their current state and future outlook.

However, there are exceptions to this pattern, particularly for the most influential factors: 'profit situation', 'turnover', and 'demand'. These factors show less correlation, indicating

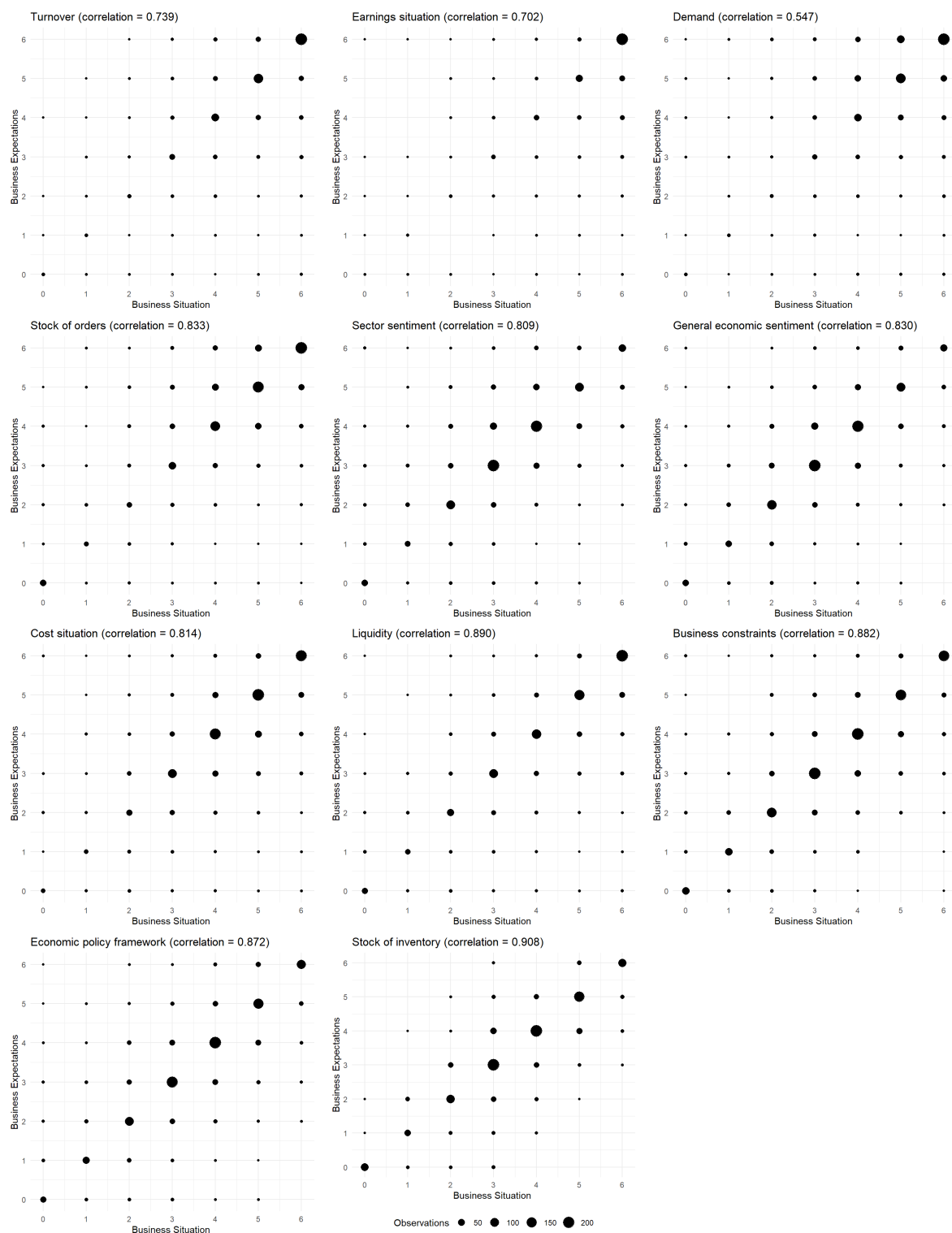
that firms might differentiate more distinctly between their current and future evaluations based on these internal metrics. This differentiation could be due to varying degrees of uncertainty or differing expectations about future market conditions that affect these specific factors more than others.

Furthermore, the plots reveal that very few companies rate 'overall sentiment' or 'sector sentiment' as highly important (i.e., assigning the maximum score) for either their business situation or expectations. This further supports the earlier finding that firms prioritize internal factors over broader external conditions.

The distribution of points outside the diagonal line in the plots indicates that not all firms align perfectly in their response behavior between assessing the business situation and expectations. This variance suggests that some companies might weigh certain factors differently when considering their present circumstances versus their expectations for the future, reflecting diverse strategic outlooks or sector-specific conditions. Such nuances highlight the complexity of interpreting the Ifo Business Climate Index and suggest that while there is a general consistency in firms' evaluations, individual differences still play a crucial role in shaping overall economic sentiment.



Figure 4: Distribution and correlation for the business situation vs. expectations



Building on this descriptive analysis of the underlying factors for the business situation as well as for the business expectations, we performed a Principal Component Analysis with three Principal Components for a better interpretability. Table 3 shows the loadings of each factor on these PCs.

Table 3: PCA with three components - loadings

	<b>Business Situation</b>			<b>Business Expectations</b>		
	<b>PC1</b>	<b>PC2</b>	<b>PC3</b>	<b>PC1</b>	<b>PC2</b>	<b>PC3</b>
Liquidity	0.511			0.112	-0.441	
Cost situation	0.500			0.177	-0.431	
Profit situation	0.379	-0.274	0.356		-0.575	
Business constraints	0.454	0.160	-0.142	0.390	-0.187	-0.110
Economic policy framework	0.351	0.329	-0.138	0.496		-0.111
General economic sentiment		0.570		0.525		
Sector sentiment		0.596	0.103	0.490	0.115	0.161
Turnover		-0.199	0.552	-0.183	-0.480	
Demand		0.186	0.548			0.686
Stock of orders		0.176	0.461			0.684

Note: Only loadings  $\geq 0.1$  or  $\leq -0.1$  are displayed.

The results of the Principal Component Analysis (PCA) presented in Table 3 reveal distinct groupings of factors influencing both the business situation and business expectations. For the business situation, the first principal component (PC1) is primarily characterized by high loadings on variables related to the overall financial health of a company, including 'cost situation', 'liquidity', and 'profit situation'. This suggests that PC1 reflects the broader financial status of a firm, encompassing both its cost management and financial liquidity, as well as its profitability. Essentially, this component captures a company's internal financial stability and performance, indicating that firms heavily weigh these aspects when assessing their current business situation.

The second principal component (PC2) is dominated by external factors such as 'general economic sentiment', 'sector sentiment', and the 'economic policy framework'. This component represents the external environment in which a company operates, highlighting the importance of macroeconomic conditions and sector-specific trends. The emphasis on these factors suggests that, while firms prioritize their internal financial health, they also remain cognizant of broader economic and sectoral influences when evaluating their business

situation.

The third principal component (PC3) predominantly loads on variables that pertain to internal, short-term operational metrics, such as 'turnover', 'demand', and 'stock of orders'. This indicates that PC3 captures a more immediate, operational outlook, reflecting factors that directly influence day-to-day business operations and short-term planning.

A similar pattern is observed in the PCA results for business expectations. Here, PC1 also reflects external factors, with strong loadings on 'general economic sentiment', 'sector sentiment', and 'economic policy framework', suggesting that firms consider the broader economic and sectoral outlook when forming expectations about the future. However, there is a notable shift in the composition of the components compared to the business situation. In the case of business expectations, PC2 captures the overall financial situation of the firm, including 'profit situation' and 'liquidity', indicating that financial stability remains a crucial consideration for firms when projecting their future outlook.

Interestingly, PC3 for business expectations is primarily influenced by variables related to 'demand' and 'order situation', similar to the business situation PCA. However, unlike the business situation, 'turnover' here is associated more closely with the overall financial component (PC2) rather than being grouped with operational metrics in PC3. This shift suggests that when thinking about the future, firms may view turnover more as a financial outcome linked to profitability and liquidity rather than just an immediate operational concern. This distinction underscores how firms might differentially weigh internal financial factors versus external conditions when assessing their current status compared to their future outlook.

### **3.2.2 Results by Economic Sector and Firm Size**

In addition to the overall results, we conducted further analysis by subdividing the data by economic sector and firm size to understand better how these dimensions influence the importance of various factors in assessing the business situation and business expectations. Table 4 presents the arithmetic mean and standard deviation for each influencing factor across different sectors, allowing us to quantify the relative importance of these factors within specific industry contexts.

The results reveal that while the prioritization of factors is generally consistent across most sectors, there are some notable differences. For instance, in the construction sector, 'stock of orders' and 'liquidity' are significantly more important compared to other sectors. This could be due to the project-based nature of the construction industry, where order backlogs and cash flow are critical for ongoing operations and future planning. In contrast, for the retailing sector, 'turnover' is of greater importance than in other sectors, reflecting the sector's focus on sales performance as a key indicator of business health. Interestingly, 'stock of orders' is less critical for retail companies, likely due to the rapid turnover of inventory that characterizes this sector. Meanwhile, in the service sector, 'sector sentiment' is rated below average in importance, which may suggest that service-oriented firms rely more on direct client interactions and firm-specific conditions rather than broad industry trends. Additionally, the 'stock of inventory' factor, included only for the trade sector, is considered moderately important, underscoring its relevance to sectors heavily dependent on inventory management.

We also conducted Principal Component Analyses (PCAs) separately for each sector to examine whether the factors influencing business assessments could be similarly grouped. The sector-specific PCA results do not show significant deviations from the overall PCA results, confirming that across all sectors, both the business situation and business expectations can be effectively interpreted using three main components: the overall financial situation of a company, external sentiments and frameworks, and the current demand and order situation. This consistency suggests that despite sectoral differences in factor prioritization, the underlying structure of how companies form their business assessments remains broadly similar across industries.

Table 5 shows the average scores for each factor differentiated by firm size. The analysis reveals some distinct patterns. Larger firms place less emphasis on 'stock of orders' compared to smaller firms. This could indicate that larger companies have more diversified operations or greater financial resilience, making them less sensitive to fluctuations in order backlogs. Conversely, 'liquidity' is a significantly more critical factor for smaller firms, which might reflect their relative vulnerability to cash flow constraints and a higher reliance on immediate

financial stability for ongoing operations. The Kruskal-Wallis equality-of-population rank test ( $p = 0.001$  for both business situation and business expectations) supports these observations, highlighting that the importance of 'liquidity' and 'stock of orders' differs significantly by firm size.

These findings suggest that while the overall framework for evaluating business conditions is consistent across sectors and firm sizes, there are important nuances in how specific factors are weighted depending on the industry context and company size.

Table 4: Importance of the influencing factors by sector

	Manufacturing	Services	Wholesaling	Retailing	Construction
<b>Business situation</b>					
Profit situation	5.4 (1.1)	5.2 (1.1)	5.5 (0.9)	5.5 (0.9)	5.5 (0.9)
Turnover	5.0 (1.2)	4.9 (1.2)	5.0 (1.1)	5.3 (1.0)	4.6 (1.3)
Demand	5.0 (1.1)	4.8 (1.2)	5.0 (1.1)	4.9 (1.2)	4.8 (1.2)
Stock of orders	4.7 (1.3)	4.4 (1.5)	4.0 (1.6)	3.4 (2.0)	5.0 (1.0)
Cost situation	4.4 (1.3)	4.2 (1.4)	4.3 (1.3)	4.5 (1.3)	4.5 (1.2)
Liquidity	4.1 (1.7)	4.0 (1.7)	4.0 (1.8)	4.4 (1.6)	4.7 (1.5)
Business constraints	3.5 (1.6)	3.5 (1.7)	3.5 (1.6)	3.9 (1.7)	3.7 (1.6)
Economic policy framework	3.5 (1.5)	3.5 (1.6)	3.5 (1.4)	3.8 (1.5)	3.6 (1.5)
Stock of inventory			3.5 (1.6)	3.5 (1.6)	
Sector sentiment	3.5 (1.4)	3.1 (1.5)	3.6 (1.3)	3.4 (1.5)	3.5 (1.4)
General economic sentiment	3.3 (1.4)	3.3 (1.5)	3.3 (1.4)	3.4 (1.4)	3.3 (1.5)
<b>Business expectations</b>					
Profit situation	5.1 (1.3)	5.0 (1.3)	5.3 (1.1)	5.4 (1.0)	5.2 (1.1)
Demand	5.3 (1.0)	4.8 (1.3)	5.0 (1.1)	4.5 (1.6)	5.0 (1.1)
Turnover	4.8 (1.3)	4.8 (1.4)	4.9 (1.2)	5.2 (1.1)	4.5 (1.4)
Stock of orders	4.7 (1.3)	4.5 (1.5)	4.2 (1.6)	3.4 (2.0)	5.1 (1.0)
Cost situation	4.3 (1.4)	4.1 (1.5)	4.2 (1.4)	4.4 (1.4)	4.4 (1.3)
Liquidity	3.9 (1.7)	3.9 (1.8)	3.9 (1.8)	4.3 (1.6)	4.6 (1.6)
Economic policy framework	3.5 (1.5)	3.5 (1.7)	3.6 (1.4)	3.8 (1.5)	3.5 (1.6)
Business constraints	3.5 (1.6)	3.4 (1.7)	3.5 (1.6)	3.9 (1.7)	3.7 (1.6)
Sector sentiment	3.6 (1.4)	3.2 (1.5)	3.8 (1.3)	3.5 (1.5)	3.6 (1.5)
General economic sentiment	3.4 (1.4)	3.3 (1.5)	3.4 (1.4)	3.5 (1.4)	3.4 (1.5)
Stock of inventory			3.4 (1.6)	3.4 (1.6)	

Note: The tables state the mean and the corresponding standard deviations in parentheses for each factor.

Table 5: Importance of the influencing factors by firm size

	<b>Total</b>	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>
<b>Business situation</b>						
Profit situation	5.4 (1.0)	5.3 (1.1)	5.5 (1.0)	5.4 (1.1)	5.5 (0.9)	5.4 (1.0)
Turnover	5.0 (1.2)	4.8 (1.3)	5.1 (1.1)	5.0 (1.1)	5.0 (1.1)	5.1 (1.1)
Demand	4.9 (1.2)	4.9 (1.2)	4.9 (1.2)	4.9 (1.2)	5.0 (1.0)	4.9 (1.1)
Stock of orders	4.4 (1.6)	4.7 (1.3)	4.1 (1.7)	4.5 (1.5)	4.3 (1.5)	4.0 (1.7)
Cost situation	4.4 (1.3)	4.4 (1.3)	4.4 (1.3)	4.3 (1.4)	4.4 (1.3)	4.2 (1.3)
Liquidity	4.2 (1.7)	4.4 (1.6)	4.3 (1.7)	4.0 (1.7)	4.0 (1.7)	3.6 (1.7)
Business constraints	3.6 (1.6)	3.6 (1.7)	3.6 (1.7)	3.6 (1.6)	3.5 (1.5)	3.4 (1.6)
Economic policy framework	3.5 (1.5)	3.5 (1.6)	3.6 (1.5)	3.6 (1.5)	3.6 (1.4)	3.5 (1.5)
Stock of inventory	3.5 (1.6)	3.6 (1.6)	3.4 (1.6)	3.7 (1.3)	3.4 (1.5)	3.4 (1.7)
Sector sentiment	3.4 (1.4)	3.4 (1.5)	3.4 (1.4)	3.4 (1.5)	3.4 (1.4)	3.4 (1.4)
General economic sentiment	3.3 (1.4)	3.2 (1.5)	3.3 (1.4)	3.4 (1.4)	3.3 (1.4)	3.3 (1.4)
<b>Business expectations</b>						
Profit situation	5.2 (1.2)	5.1 (1.2)	5.3 (1.2)	5.1 (1.3)	5.2 (1.2)	5.1 (1.2)
Turnover	5.0 (1.2)	5.0 (1.1)	4.8 (1.4)	5.0 (1.2)	5.0 (1.1)	5.0 (1.2)
Demand	4.8 (1.3)	4.7 (1.4)	5.0 (1.2)	4.9 (1.3)	4.8 (1.3)	4.9 (1.2)
Stock of orders	4.4 (1.6)	4.7 (1.3)	4.2 (1.7)	4.5 (1.5)	4.4 (1.5)	4.1 (1.8)
Cost situation	4.2 (1.4)	4.2 (1.4)	4.3 (1.4)	4.2 (1.5)	4.2 (1.4)	4.2 (1.4)
Liquidity	4.1 (1.7)	4.2 (1.7)	4.2 (1.7)	3.9 (1.7)	3.9 (1.7)	3.5 (1.8)
Business constraints	3.6 (1.6)	3.5 (1.6)	3.6 (1.5)	3.6 (1.5)	3.7 (1.4)	3.5 (1.5)
Economic policy framework	3.6 (1.6)	3.6 (1.7)	3.6 (1.7)	3.6 (1.6)	3.5 (1.5)	3.4 (1.6)
Stock of inventory	3.5 (1.5)	3.4 (1.5)	3.5 (1.4)	3.4 (1.5)	3.6 (1.4)	3.5 (1.4)
Sector sentiment	3.4 (1.5)	3.3 (1.5)	3.4 (1.4)	3.4 (1.5)	3.5 (1.4)	3.4 (1.4)
General economic sentiment	3.4 (1.6)	3.5 (1.6)	3.4 (1.6)	3.7 (1.3)	3.2 (1.7)	3.2 (1.8)

Note: Firm size 1 to 5 applies to all sectors apart from construction, which is only classified from 1 to 4 (the firm size categories are listed in detail in Appendix Table B1).

### 3.2.3 Benchmarks for the Business Situation

For the business situation, our second research question focused on identifying which comparative benchmarks companies use for their assessments. The meta-survey results indicate that the vast majority of companies (96.5%) rely on one or more benchmarks when evaluating their current business situation, highlighting the importance of contextual comparisons in their assessment processes.

Among the various benchmarks, the most commonly used is a comparison with the business situation in the same month of the previous year, cited by 58.2% of respondents. This suggests that firms often look to historical data from the same period to gauge performance, likely to account for seasonal variations and cyclical trends. Additionally, expectations and goals for the current month are also a significant reference point, utilized by 50.3% of com-

panies, indicating that many firms align their assessments with their internal targets and short-term strategic objectives.

Other benchmarks are also employed, though to a lesser extent. The business situation of the previous month is used by 44.2% of firms, slightly more frequently than comparisons to the usual situation in previous years (42.1%). The latter could provide a broader historical context but may be less immediately relevant than more recent or specific comparisons. Meanwhile, comparing to the usual situation in the same month of previous years is the least commonly used benchmark, referenced by only 35.3% of companies, suggesting that while year-over-year comparisons are valuable, firms may prefer more dynamic or immediate benchmarks for their current assessments.

When examining benchmark usage by sector, notable differences emerge. In the services, retailing, and wholesaling sectors, firms predominantly rely on the business situation in the same month of the previous year. This reliance could reflect these sectors' sensitivity to seasonal patterns and consumer behavior, which are crucial for accurately assessing business conditions. In contrast, construction companies most frequently compare their current business situation to the previous month, which may reflect the project-driven nature of the industry and the need for more immediate, short-term benchmarks. Manufacturing firms, on the other hand, most commonly use expectations and goals for the current month as their benchmark, suggesting a focus on internal performance targets and forward-looking assessments.

Analysis by firm size also reveals distinct patterns. Small and medium-sized enterprises primarily use the business situation of the same month from the previous year as a benchmark. However, large firms, differ in their approach; they most frequently use expectations and goals for the current month as their benchmark. This could indicate that larger firms, with more resources and strategic flexibility, are more inclined to focus on achieving their immediate operational goals and are less reliant on historical comparisons.

### 3.2.4 Time Perspective for the Business Expectations

Another intriguing aspect of the business expectations concerns the time perspective that firms adopt when responding to the ifo Business Survey. The survey specifically inquires about firms' 'expectations for the next six months,' a phrasing that can be interpreted in two distinct ways: either as a 'point in time', referring to the expected situation exactly six months from now, or as a 'time period' referring to the expected situation throughout the upcoming six months. The results indicate a clear preference among firms for the 'time period' interpretation, with 82.1% of respondents opting for this view. In contrast, only 16.4% of firms consider the 'point in time' perspective, and a minimal number of respondents (1.5%) selected both options. This strong inclination towards the 'time period' suggests that most firms are more concerned with the overall trend or evolution of their business conditions over the coming months rather than focusing on a specific future point.

In addition to the time frame, the survey also explores whether firms are more focused on 'the change in the business situation' or 'the upcoming business situation'. Here, a majority of firms (60.2%) indicated that they focus on 'the change in the business situation', suggesting an emphasis on how their circumstances might shift from the current state. Meanwhile, 38.0% of firms think more about 'the upcoming business situation', implying a focus on the anticipated state of affairs in the future, irrespective of past or current conditions. Again, very few respondents (1.8%) selected both options, indicating clear distinctions in their thought processes.

Differences across economic sectors and firm sizes in terms of these perspectives are minor and statistically insignificant. However, a slight trend is observed where larger companies are more likely to emphasize 'the change in the business situation' compared to smaller firms. This tendency among larger firms could reflect their broader strategic planning capabilities and a focus on adjusting to dynamic market conditions. In contrast, smaller firms may find it more practical to consider their anticipated situation in absolute terms, given their often more limited ability to adapt quickly to changes.



## 4 Discussion and Outlook

Business cycle indicators, such as the ifo Business Climate Index, are invaluable tools for both analyzing the current state of an economy and forecasting its near-term development. Many of these indicators rely on survey data, which offers timely and often unique insights into economic conditions that are not immediately captured by traditional quantitative data. Examples of similar survey-based indicators include the European Commission’s Joint Harmonised EU Programme of Business and Consumer Surveys (BCS)<sup>4</sup> and the Purchasing Manager Indices (PMIs), both of which are widely used across Europe and globally. Extensive research has demonstrated the utility of such survey data for macroeconomic forecasting, as evidenced by studies such as Claveria et al. (2007), Carstensen et al. (2011), Girardi et al. (2016), Basselier et al. (2018), de Bondt (2019), Garnitz et al. (2019), and Lehmann and Reif (2021), among others.

Despite their widespread use, the question remains: What specifically underlies the strong forecasting power of the ifo Business Climate Index, as reviewed comprehensively by Lehmann (2023)? This paper contributes to answering this question by leveraging a meta-survey to uncover the factors that firms consider when responding to the key questions about their current business situation and expectations for the next six months. Our findings suggest that the robust predictive capabilities of the ifo time series can be attributed to several interrelated factors.

First, our decomposition of survey responses into three principal components: (1) the overall financial situation of the firm, (2) the demand and order situation, and (3) external influences highlights that firms predominantly base their assessments on internal factors. The first two components, capturing a firm’s financial health and demand dynamics, provide unique insights that are typically unavailable in official statistics or public news at the time of the survey. These internal elements, such as profit margins, liquidity, order backlogs, and immediate demand conditions, are closely monitored by firms but may not yet be visible in broader economic data. This unique, firm-level insight enables the ifo Business Climate

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<sup>4</sup>For more details on the BCS Programme, see: [http://ec.europa.eu/economy\\_finance/db\\_indicators/surveys/index\\_en.htm](http://ec.europa.eu/economy_finance/db_indicators/surveys/index_en.htm)

Index to offer an early indication of economic turning points, providing valuable information that might not yet be reflected in macroeconomic indicators.

Second, the strong emphasis on internal company factors such as profit situation, demand, and turnover implies that the ifo survey captures firm-specific expectations and conditions directly tied to firms' operational realities and strategic decisions. This focus distinguishes the ifo survey from other economic indicators or expert surveys that might rely more heavily on public sentiment or broad economic forecasts. By capturing the direct perceptions and expectations of firms' upper management – who are typically well-informed about their firm's performance and market conditions – the survey provides a more accurate and immediate reflection of economic dynamics. This bottom-up approach helps explain why the ifo Business Climate Index has been successful in forecasting short-term economic developments; it aggregates detailed, firm-level data that reflect immediate economic conditions.

Third, while internal factors are crucial, the meta-survey results also demonstrate that firms do not operate in isolation from the broader economic environment. The third principal component, which captures external influences such as general economic sentiment and industry-specific trends, underscores the role of external factors in shaping firms' expectations. This suggests that the ifo Business Climate Index incorporates a balanced perspective that reflects both microeconomic (firm-level) and macroeconomic (economy-wide) conditions. The inclusion of these external factors allows the index to dynamically adjust to shifts in the broader economic environment, enhancing its relevance for economic forecasting. For instance, during periods of macroeconomic instability or sector-specific disruptions, firms' assessments – reflected in the index – provide early warnings of potential downturns or recoveries.

Moreover, the meta-survey reveals that firms employ a variety of benchmarks to evaluate their business situation, such as comparisons to the same month in the previous year or to internal targets for the current month. This diversity of benchmarks introduces a rich variety of perspectives into the survey responses, allowing the index to capture a wide range of economic signals. This variety enhances the robustness of the index against biases that could arise from overly narrow or homogeneous data sources, providing a more comprehensive

view of economic sentiment.

Linking these findings back to our research questions, the analysis reveals that the forecasting power of the ifo Business Climate Index can be largely attributed to its ability to synthesize firm-level insights with broader economic conditions, offering a comprehensive and timely indicator of economic sentiment. The dual focus on internal and external factors, combined with an emphasis on forward-looking expectations, makes the index a uniquely valuable tool for economic analysis and forecasting. It not only captures the current economic reality from the perspective of firms but also their anticipations and strategic responses to potential future changes in the economic environment.

These insights have broader implications for economic forecasting and policy-making. For policymakers, understanding the specific factors that firms consider when forming their business expectations is crucial for interpreting the ifo Business Climate Index and making informed policy decisions. For instance, if a deterioration in the index is driven by declining internal financial conditions across firms, it may suggest different policy responses than if the decline were driven by external macroeconomic shocks. Moreover, during economic downturns or periods of instability, the ability of the index to provide early warnings can help policymakers respond more swiftly and effectively to mitigate negative impacts on the economy.

Looking ahead, future research could further enhance our understanding of these dynamics by examining how the importance of different factors evolves over various phases of the business cycle or in response to extraordinary economic events. Additionally, exploring the role of digitalization, technological change, and globalization in shaping firms' assessments could provide valuable insights into the evolving nature of economic forecasting.

The micro-data from the meta-survey is accessible at the LMU-ifo Economics & Business Data Center (EBDC). The data is available free of charge for non-commercial, scientific usage (Sauer et al., 2023) and can be linked to the micro-data of the IBS for further research and analysis.

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# Appendix

## A Questionnaire

Figure A1: Excerpt from the original questionnaire

1. GESCHÄFTSLAGE	2. GESCHÄFTSERWARTUNGEN
<p>a) Bitte geben Sie an, welche Bedeutung jeder der nachfolgend aufgeführten Faktoren für Sie bei der Beurteilung der <b>aktuellen Geschäftslage</b> hat. Bitte tragen Sie pro Kategorie einen Wert von 0–6 ein (0 = keine Bedeutung, 6 = sehr hohe Bedeutung).</p> <p>_____ Umsatz</p> <p>_____ Ertragslage</p> <p>_____ Nachfrage</p> <p>_____ Auftragsbestand</p> <p>_____ Stimmung in der Branche</p> <p>_____ Stimmung in der Gesamtwirtschaft</p> <p>_____ Kostensituation</p> <p>_____ Liquidität</p> <p>_____ Behinderungen der Geschäftstätigkeit</p> <p>_____ wirtschaftspolitische Rahmenbedingungen</p>	<p>Wenn Sie Fragen zu Ihren <b>Geschäftserwartungen in den nächsten 6 Monaten</b> beantworten:</p> <p>b) Denken Sie eher an die Situation zum <b>Ende</b> der Periode (Zeitpunkt) oder an die Situation <b>während</b> dieses Zeitraums?</p> <p><input type="checkbox"/> Wir denken daran, wie die Situation in 6 Monaten sein wird (<b>Zeitpunkt</b>).</p> <p><input type="checkbox"/> Wir denken daran, wie die Situation innerhalb der nächsten 6 Monate sein wird (<b>Zeitraum</b>).</p> <p>c) Denken Sie eher an ...</p> <p><input type="checkbox"/> die <b>zukünftige</b> Geschäftslage</p> <p><input type="checkbox"/> die <b>Veränderung</b> der Geschäftslage ausgehend von heute</p>
<p>b) Welche <b>Vergleichsmaßstäbe</b> nutzen Sie zur Beurteilung Ihrer aktuellen Geschäftslage? (Mehrfachnennungen möglich)</p> <p><input type="checkbox"/> Erwartungen/Ziele für den Berichtsmonat</p> <p><input type="checkbox"/> Geschäftslage des Vormonats</p> <p><input type="checkbox"/> Geschäftslage des Vorjahresmonats</p> <p><input type="checkbox"/> übliche Lage in den vorangegangenen Jahren</p> <p><input type="checkbox"/> übliche Lage im entsprechenden Monat der vorangegangenen Jahre</p> <p><input type="radio"/> wir führen keine Vergleiche durch</p>	
2. GESCHÄFTSERWARTUNGEN	
<p>a) Bitte geben Sie an, welche Bedeutung jeder der nachfolgend aufgeführten Faktoren für Sie bei der Beurteilung Ihrer <b>Geschäftserwartungen für die kommenden 6 Monate</b> hat. Bitte tragen Sie pro Kategorie einen Wert von 0–6 ein (0 = keine Bedeutung, 6 = sehr hohe Bedeutung).</p> <p>_____ Umsatz</p> <p>_____ Ertragslage</p> <p>_____ Bestelleingang bzw. erwartete Nachfrageentwicklung</p> <p>_____ Auftragsbestand</p> <p>_____ Stimmung in der Branche</p> <p>_____ Stimmung in der Gesamtwirtschaft</p> <p>_____ Kostensituation</p> <p>_____ Liquidität</p> <p>_____ Behinderungen der Geschäftstätigkeit</p> <p>_____ wirtschaftspolitische Rahmenbedingungen</p>	

## Excerpt from the Original Questionnaire - English Translation

### 1. Business Situation

(a) Please specify how important you consider the following factors for your assessment of the current business situation. Please enter a value from 0 to 6 for each category (0 = no importance, 6 = very high importance).

- Turnover
- Profit situation
- Demand
- Stock of orders
- Sector sentiment
- General economic sentiment
- Cost situation
- Liquidity
- Business constraints
- Stock of inventory

(b) Which benchmarks do you use for the assessment of your current business situation? (multiple answers possible)

- Expectations/Goals for the current month
- Business situation of the previous month
- Business situation in the respective month of the previous year
- Usual situation in previous years
- Usual situation in the respective month of previous years
- We do not make any comparisons



## 2. Business Expectations

(a) Please specify how important you consider each of the following factors for your assessment of the business expectations for the next 6 months. Please enter a value from 0 to 6 for each category (0 = no importance, 6 = very high importance).

- Turnover
- Profit situation
- Demand
- Stock of orders
- Sector sentiment
- General economic sentiment
- Cost situation
- Liquidity
- Business constraints
- Stock of inventory

When you answer questions about the business expectations for the next 6 months:

(b) Are you thinking about the situation at the end of the period (point of time) or the situation within that period?

- We think about the situation in 6 months' time (point of time).
- We think about the situation within the next 6 months (time period).

(c) Are you thinking more about ...

- the future business situation (upcoming business situation)
- the change of the business situation from today's perspective (change of business situation)

## B Firm Size Definition

Table B1: Classification of the sectors by firm sizes

	<b>Manufacturing</b>	<b>Services</b>	<b>Wholesaling</b>	<b>Retailing</b>	<b>Construction</b>
1	<99	<250,000	<1 M	<1 M	<99
2	100-249	250,000-1M	1-12.5 M	1-12.5 M	100-199
3	250-499	1-5 M	12.5-25 M	12.5-25 M	200-499
4	500-999	5-10 M	25-50 M	25-50 M	>500
5	>1000	>10 M	>50 M	>50 M	

Note: The firm sizes of manufacturing and construction are based on the number of employees. In services, wholesaling and retailing they are based on turnover (in Euro). M = million.