July data signalled a slight improvement in the performance of the UK service sector, with a renewed increase in new work supporting the fastest pace of business activity growth since October 2018. However, the rate of expansion remained subdued overall and much softer than seen on average over the past decade. Meanwhile, job creation softened in July and business expectations for the year ahead eased to the weakest since March.

At 51.4 in July, the seasonally adjusted IHS Markit/CIPS UK Services PMI® Business Activity Index registered above the 50.0 no-change mark for the fourth consecutive month and signalled a modest increase in service sector output. The latest reading was up from 50.2 in June and the highest for nine months, but still well below the trend recorded since the recovery from the global financial crisis began in the second half of 2009 (54.4).

Higher levels of business activity were driven by a solid rebound in new work during July. The rate of new business growth was the strongest since September 2018. There were again widespread reports that domestic political uncertainty had held back decision-making among clients, particularly large corporates.

A number of survey respondents commented on improved sales to clients in external markets, helped by the weak sterling exchange rate against the euro and US dollar. Moreover, the latest survey indicated the fastest increase in new work from abroad since June 2018.

Service providers reported a modest increase in staffing levels during July, but the rate of expansion eased since the previous month. A lack of pressure on business capacity continued to dampen employment growth, as highlighted by a drop in backlogs of work for the tenth month running. In some cases, service providers noted that rising payroll costs had also resulted in more cautious hiring strategies.

Latest data indicated another sharp rise in average cost burdens across the service economy. The rate of input price inflation was unchanged since June and still below the levels seen in 2018. Companies reporting a rise in their business expenses generally cited the weak pound, higher staff wages and greater fuel prices.

Meanwhile, prices charged by service sector firms increased at only a modest pace, reflecting intense competition for new work and a resultant squeeze on margins.

Business optimism towards the year-ahead outlook eased for the second month running and reached its lowest level since March. Survey respondents continued to cite domestic political uncertainty and concerns about the global economic outlook, although some firms noted hopes of a boost from pent up demand following clarity about the path to Brexit.
IHS MARKIT UK ALL SECTOR PMI®

Service sector growth offset by falls in manufacturing and construction output

Composite Output Index
sa, >50 = growth since previous month

All Sector PMI indices are weighted averages of comparable manufacturing, construction and services PMI indices. Weights reflect the relative size of the manufacturing, construction and service sectors according to official GDP data.

The UK All Sector Output Index is a weighted average of the UK Manufacturing Output Index, the UK Total Construction Activity Index and the UK Services Business Activity Index.

At 50.3 in July, the seasonally adjusted All Sector Output Index picked up from 49.2 in June and signalled a fractional expansion of private sector business activity.

Stronger growth of service sector activity was offset by the steepest fall in manufacturing production for seven years, as well as another reduction in construction sector output.

COMMENT

Chris Williamson, Chief Business Economist at IHS Markit, which compiles the survey:

"An improved rate of growth in the service sector to the highest since October is welcome news after other PMI surveys showed the sharpest drop in manufacturing output for seven years and a construction sector that is mired in its deepest downturn for a decade. However, the overall picture is one of an economy that is only just managing to skirt recession, with July's performance among the worst since the height of the global financial crisis in 2009.

"The latest PMI numbers are indicative of the economy stagnating at the start of the third quarter after indicating a 0.1% decline in the second quarter.

"Even growth in the service sector remains worryingly subdued, constrained by a marked fall in business services activity, where the rate of decline in July has been exceeded only once in the past ten years. The best performing sector was consumer services, highlighting how the economy remains dependent on consumer spending to avoid contraction.

"Inflationary pressures remained muted, with average prices charged for goods and services rising at one of the weakest rates recorded over the past three years, as firms increasingly resorted to competing on price to help drive sales."

Duncan Brock, Group Director at the Chartered Institute of Procurement & Supply, said:

"While services activity grew in July, this marginal improvement on last month is a smokescreen. Fundamental weaknesses remain in a sector pinned down by Brexit uncertainty and increasingly stagnant global economic growth.

"New order growth rose modestly, however the weakening pound was a boon to overseas customers, especially in the EU and US, as export orders rose to their highest levels since June 2018.

"The downside to domestic currency weakness was that margins were placed under intense pressure. Firms were caught between an intensely competitive marketplace, and rising fuel and salary costs. This anxiety prevented firms from passing on costs, and translated into the lowest levels of business optimism since March this year.

"Supply chain managers voiced grave concerns that without a sustained period of stability, this will amplifiy the risk to the largest contributor to UK GDP and services could follow the construction and manufacturing sectors into contraction territory within a few short months."
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Methodology

The IHS Markit/CIPS UK Services PMI® is compiled by IHS Markit from responses to questionnaires sent to a panel of around 650 service sector companies. The sectors covered include consumer (excluding retail), transport, information, communication, finance, insurance, real estate and business services. The panel is stratified by detailed sector and company workforce size, based on contributions to GDP.

Survey responses are collected in the second half of each month and indicate the direction of change compared to the previous month. A diffusion index is calculated for each survey variable. The index is the sum of the percentage of ‘higher’ responses and half the percentage of ‘unchanged’ responses. The indices vary between 0 and 100, with a reading above 50 indicating an overall increase compared to the previous month, and below 50 an overall decrease. The indices are then seasonally adjusted.

The headline figure is the Services Business Activity Index. This is a diffusion index calculated from a question that asks for changes in the volume of business activity compared with one month previously. The Services Business Activity Index is comparable to the Manufacturing Output Index. It may be referred to as the ‘Services PMI®’ but is not comparable with the headline manufacturing PMI® figure.

The All Sector Output Index is a weighted average of the Manufacturing Output Index, the Construction Total Activity Index and the Services Business Activity Index. The weights reflect the relative size of the manufacturing, construction and service sectors according to official GDP data.

Underlying survey data are not revised after publication, but seasonal adjustment factors may be revised from time to time as appropriate which will affect the seasonally adjusted data series. July 2019 data were collected 12-29 July 2019.

For further information on the PMI survey methodology, please contact economics@ihsmarkit.com.

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