Business conditions worsen sharply amid tightening of COVID-19 measures

Key findings

Output and new orders fall at sharper rates

Renewed decline in purchasing activity

Business sentiment increasingly pessimistic

Having moved close to stabilisation in June, Hong Kong’s business conditions worsened sharply at the start of the third quarter, according to the latest PMI data, amid a tightening of containment measures due to a rise in new infections.

Business activity and new orders both declined at steeper rates during July. Firms in turn scaled back their purchasing activity substantially, while inventories contracted sharply. Business confidence deteriorated further, with rising concerns over the adverse impact of a new wave of coronavirus disease 2019 (COVID-19) cases on the economy.

The seasonally adjusted headline IHS Markit Hong Kong SAR Purchasing Manager’s Index™ (PMI™) fell from 49.6 in June to 44.5 in July, and registered a marked deterioration in the health of the private sector. The latest reading was not as severe as seen during the worst of the pandemic from February to April, but signalled a setback to the current recovery of private sector conditions.

The tightening of COVID-19 restrictions during July, in response to a rising number of new infections, dealt a further hit to business conditions across Hong Kong’s private sector. Business activity shrank sharply, accompanied by a similarly steep contraction in new orders. Some respondents noted that the retail sector was especially hard hit as consumers were reluctant to spend. New export orders also deteriorated at a faster pace.

Business confidence was consequently dented further, with the proportion of firms anticipating a decline in business activity over the next 12 months increasing noticeably from June. A resurgence of new infections and its associated impact on economic activity were concerns dominant among respondents.

Comment

Commenting on the latest survey results, Bernard Aw, Principal Economist at IHS Markit, said:

"Latest PMI data pointed to a marked deterioration in private sector conditions across Hong Kong SAR, representing a setback to the economic recovery. The tightening of COVID-19 related measures in response to a rise in new infections dealt a new blow to the economy.

"Business activity and new orders both fell at steeper rates. Companies consequently cut back substantially on their purchasing activity and inventories. Business sentiment remained deeply pessimistic as firms worried about the possibility of stricter measures and their subsequent impact on economic activity.

"While employment remained broadly unchanged, the concern is that further severe deteriorations in business conditions will see a new round of job losses."
With sales weakening at a faster pace during July, firms in turn reduced their input purchases as part of efforts to control costs and avoid keeping excessive stocks. Purchasing activity was cut severely, dropping at a pace comparable to those during the height of the lockdown measures earlier in the year. Input inventories consequently contracted at a substantial rate.

The level of backlogs fell further in July, and at a quicker rate, reflecting rising spare capacity. That said, employment remained broadly unchanged, as was the case in June.

Finally, overall input prices dropped at the start of the third quarter after a marginal increase in June. Deflation was driven by a renewed (and sharp) fall in purchase costs and a further decline in wages. As part of efforts to boost sales, firms offered discounts. Output charges fell for a thirteenth straight month, and at a marked pace that was the fastest since April.

Methodology
The IHS Markit Hong Kong SAR PMI™ is compiled by IHS Markit from responses to questionnaires sent to purchasing managers in a panel of around 400 private sector companies. The panel is stratified by detailed sector and company workforce size, based on contributions to GDP. The sectors covered by the survey include manufacturing, construction, wholesale, retail and services. Hong Kong is a Special Administrative Region of China.

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 then are seasonally adjusted.

The headline figure is the Purchasing Managers’ Index™ (PMI). The PMI is a weighted average of the following five indices: New Orders (30%), Output (25%), Employment (20%), Suppliers’ Delivery Times (15%) and Stocks of Purchases (10%). For the PMI calculation the Suppliers’ Delivery Times Index is inverted so that it moves in a comparable direction to the other indices.

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 2020 data were collected 13-28 July 2020.

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

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