Survey-record fall in service sector activity amid emergency measures to slow COVID-19 pandemic

KEY FINDINGS

- Fastest decline in activity since survey began in July 1996
- Rapid drop in new work and widespread job cuts
- Margins under pressure as charges fall while costs rise

March data indicated the steepest downturn across the UK service sector for more than two decades. The slump in activity was almost exclusively linked by survey respondents to business shutdowns and cancelled orders in response to the coronavirus disease 2019 (COVID-19) pandemic.

The headline seasonally adjusted IHS Markit/CIPS Final UK Services PMI® Business Activity Index posted 34.5 in March, below the earlier ‘flash’ reading of 35.7 and down sharply from 53.2 in February. This reading exceeded the previous record low seen at the height of the global financial crisis and signalled by far the fastest downturn in service sector output since the survey began in July 1996. The latest survey data were collected between 12-27 March.

Sharp reductions in activity were broad-based across the sector during March, with only the technology services sub-category recording pockets of continued business expansion. Mirroring the trend for output volumes, latest data indicated a survey-record drop in new work received by service providers. The rate of decline was also much sharper than the previous record seen in November 2008. Survey respondents overwhelmingly attributed lower demand to a slump in business and consumer spending amid emergency public health measures to halt the spread of COVID-19. New business from abroad fell at an even faster pace than that signalled for total orders during March, reflecting international travel restrictions and widespread business closures across Europe. A number of firms noted that existing projects had been placed on hold and new enquires from abroad had virtually ceased.

A rapid drop in new orders quickly translated into excess business capacity to meet existing workloads, as highlighted by the largest decline in unfinished business in more than two decades of data collection.

Employment numbers fell for the first time in five months and at the fastest rate since June 2009. Service providers commented on a mixture of hiring freezes and forced redundancies amid the slump in business activity seen during March. That said, a number of companies reported placing staff on furlough, which appears to have softened the overall scale of job cuts recorded in the latest survey period.

Average cost burdens increased at the slowest pace for just over four years in March, helped by falling fuel prices and efforts to reduce non-essential expenditure. Where a rise in input costs was reported, survey respondents often cited higher staff salaries. In contrast, prices charged by service sector companies fell at the steepest rate since August 2009.

Meanwhile, business expectations for the next 12 months dropped to the lowest in more than twenty years of data collection. Survey respondents overwhelmingly cited the public health crisis and uncertainty about the likely length of disruption to business operations.

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Slump in private sector output, led by rapid downturn in the service economy

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

The UK Composite Output Index is a weighted average of the UK Manufacturing Output Index and the UK Services Business Activity Index.

At 36.0 in March, down sharply from 53.0 in February, the IHS Markit/CIPS UK Composite Output Index dropped to its lowest level since this series began in January 1998. The latest reading was below the earlier ‘flash’ reading of 37.1 in March and pointed to a slightly faster reduction in private sector output than that seen at the height of the global financial crisis (index at 38.1 in November 2008).

The downturn in overall business activity was driven by a rapid fall in service sector activity (index at 34.5), alongside the fastest decline in manufacturing production since July 2012.

March data also highlighted a survey-record reduction in new orders received by UK private sector companies and a slump in business expectations to the lowest since comparable data were first compiled in mid-2012.

The seasonally adjusted Employment Index registered 43.6 in March, down sharply from 50.6 in February. However, the fall in payroll numbers was less steep than those signalled by the equivalent survey measures for business activity and incoming new work.

COMMENT

Tim Moore, Economics Director at IHS Markit, which compiles the survey:

“A record slump in UK service sector activity reported in March adds to the increasingly bleak economic statistics seen recently across the developed world. Emergency public health measures to combat the COVID-19 pandemic continue to mothball business operations, force aggressive cutbacks on non-essential expenses and trigger distress for household finances.

“The severe impact on service sector activity in March was by no means limited to consumer-facing businesses or those directly hit by international travel restrictions. Technology services were the only area to signal a rise in business activity, but even this pocket of growth looks fragile as new workloads dropped more quickly in this category than at any time since 2011.

“There were numerous reports from survey respondents that placing staff on furlough had helped to mitigate more widespread job losses in March. However, employment levels across the service sector still dropped at the fastest pace for more than a decade, reflecting some forced redundancies and the non-replacement of departing staff amid widespread hiring freezes.

“With the UK economy now almost certain to experience a deep contraction in the second quarter of the year, perhaps the most important aspect of the Services PMI to watch for hopeful signs will be any recovery in the business expectations sub-index from the record low seen in March.”

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

“The services sector was sucked into a black hole and flung into the unknown by the forceful impact of the COVID-19 coronavirus, affecting every area of supply chains from transport to purchasing levels and job creation.

“The abrupt drop in new orders was the sharpest since the survey began in 1996 according to the PMI data. Export orders were hit particularly hard and, in some cases, dissolved into nothing as border closures and travel restrictions resulted in the immediate cessation of normal business activities.

“Predictably this had a severe knock-on effect on employment as job losses accelerated to levels last seen in June 2009. As the pandemic raged, some companies resorted to hasty redundancies and a freeze on job hires to stay afloat in the short-term.

“It’s increasingly difficult to find the words to describe the devastation as every region in the world fights to save human life as the first priority. The likelihood of a global recession is now a given, though its duration and severity has yet to reveal itself. One thing is for certain, with the lowest business optimism for over 20 years, the immediate outlook for the services sector is beyond grim.”
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 Composite Output Index is a weighted average of the Manufacturing Output Index and the Services Business Activity Index. The weights reflect the relative size of the manufacturing 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.

March data were collected 12-27 March 2020.

The final United Kingdom Services PMI follows on from the flash estimate which is released around a week earlier and is typically based on approximately 85%-90% of total PMI survey responses each month. The March 2020 flash was based on 84% of the replies used in the final data.

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

Sources: IHS Markit, ONS.