Renewed decline in service sector activity during August

The Italian service sector dipped back into contraction territory in August. Business activity declined moderately, amid a further drop in total new business and a marked reduction in foreign demand. Subsequently, the year-ahead outlook for activity moderated, with sentiment the lowest for three months and subdued in the context of historical data.

The headline index from the report, the seasonally adjusted Business Activity Index – which is based on a single question asking respondents to report on the actual change in business activity at their companies compared to one month ago – registered 47.1 in August, down from 51.6 in July, and signalled a renewed contraction in Italian service sector output. That said, the latest fall was noticeably softer than the unprecedented reductions seen during the height of the pandemic.

Central to the renewed downturn was a further and faster reduction in total new business during August, with panellists reporting muted client demand.

Export markets were the primary source of weakness, as foreign order book volumes fell markedly again, amid reports that lockdown restrictions from key markets had stifled demand from abroad.

Concurrently, capacity pressures remained weak during August. The level of outstanding business fell again, with the decline quickening to a solid pace. Italian service providers also reduced their staffing levels, with survey respondents mentioning the non-renewal of contracts and the use of the government furlough scheme. The rate of job shedding was the slowest in the sequence of falling employment and only moderate.

Italian service providers signalled a rise in input prices during August, as has been the case in each of the past three months. Greater maintenance costs and additional expenditure on personal protection equipment (PPE) were the primary drivers of inflation, according to panellists.

In spite of higher cost burdens, companies continued to reduce their average charges in August. Respondents noted that greater competitive pressures as a result of muted demand conditions had forced firms to discount prices to attract clients. Albeit solid,, the rate of charge deflation was the slowest since February.

Looking ahead, the 12-month outlook for activity remained positive during August. Anecdotal evidence linked confidence to hopes of improved demand conditions. The level of positive sentiment moderated to a three-month low, however, and was historically subdued. A number of firms expressed concerns about the length and shape of the recovery in the coming year.
Renewed fall in private sector output

The Composite Output Index* registered below the 50.0 neutral mark in August to signal a renewed reduction in Italian private sector output. That said, at 49.5, the figure was indicative of only a fractional rate of decline overall.

August data highlighted a back-to-back increase in order book volumes at Italian private sector firms. The rate of expansion slowed from July and was only mild, however. In contrast, foreign demand for Italian goods and services declined again, as ongoing lockdown measures designed to stem the coronavirus pandemic continued to stifle export sales. The rate of reduction in foreign order books was solid.

With client demand still below pre-covid levels, firms made further job cuts in August. The rate of job shedding was the slowest in the current six-month sequence of reduction, but modest.

There was further evidence of spare capacity, as the level of outstanding business fell at a quicker rate in August and sharply overall.

At the same time, August data highlighted a third successive increase in cost burdens facing Italian private sector firms. The rate of price inflation eased slightly from July and was marginal.

Nonetheless, firms continued their discounting efforts in August. Average prices charged by Italian companies fell for the fourteenth consecutive month, with deflation remaining solid.

Commenting on the PMI data, Lewis Cooper, Economist at IHS Markit said:

“August data highlighted a renewed fall in Italian service sector activity, as weak client demand continued to weigh on the sector’s performance. The level of incoming new business declined at a quicker rate, with foreign demand a key drag as new export orders fell markedly again.

“Furthermore, expectations with regards to activity over the coming 12 months remained historically subdued, with survey respondents signalling concerns about the longevity of any recovery from the pandemic.

“Whilst the easing of lockdown restrictions around the world will help to give any recovery legs, demand conditions need to revive noticeably to enable firms to ramp up output to make up the lost ground.”

*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 Italy Composite Output Index is a weighted average of the Italy Manufacturing Output Index and the Italy Services Business Activity Index.
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Methodology
The IHS Markit Italy Services PMI® is compiled by IHS Markit from responses to questionnaires sent to a panel of around 400 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. The Composite Output Index may be referred to as the ‘Composite PMI’ but is not comparable with the headline manufacturing PMI figure.

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.

August 2020 data were collected 12—25 August 2020.

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

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Purchasing Managers’ Index® (PMI®) surveys are now available for over 40 countries and also for key regions including the eurozone. They are the most closely watched business surveys in the world, favoured by central banks, financial markets and business decision makers for their ability to provide up-to-date, accurate and often unique monthly indicators of economic trends.

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