Private sector demand weakens amid tax hike in August

The latest PMI® data covering Saudi Arabia’s non-oil private sector economy signalled a renewed decline in business conditions in August. After stabilising in July, the economy fell back into a downturn as firms registered a solid drop in new business, in part linked to the rise in VAT charges and ongoing social distancing measures. Business activity and employment both declined, whilst the tax rate change led to the sharpest rise in output charges for 11 years.

The headline IHS Markit Saudi Arabia PMI is a composite single-figure indicator of non-oil private sector performance. It is derived from indicators for new orders, output, employment, suppliers’ delivery times and stocks of purchases. Any figure greater than 50.0 indicates overall improvement of the sector.

The headline seasonally adjusted IHS Markit Saudi Arabia Purchasing Managers’ Index™ (PMI) fell from the neutral 50.0 threshold in July to 48.8 in August, to signal a renewed deterioration in the non-oil private sector economy. The rate of decline was modest though, and softer than that seen across the previous period of downturn between March and June.

Driving the latest decline was a solid fall in new business at Saudi Arabia firms, as panelists highlighted that higher VAT charges led to weaker consumer demand during August. Coupled with ongoing measures designed to curb the coronavirus disease 2019 (COVID-19) pandemic, businesses noted that market conditions were generally depressed, although some did see a pick-up in demand as more sectors reopened. Foreign sales remained mired by weak global economic conditions, falling at a sharp pace overall.

Commenting on the latest survey results, David Owen, Economist at IHS Markit, said:

“Newly-imposed VAT changes stalled consumer spending across the Saudi Arabia economy in August, latest PMI data suggested. New business was down solidly from July, as several firms commented that the sharp uptick in prices kept some customers away from markets.

“The lasting effects of the COVID-19 crisis were also apparent, with plenty of businesses noting that consumer confidence remained weak despite efforts to reopen the economy. Some areas saw an improvement though, especially with firms highlighting a pick-up in tourism.

“Business confidence strengthened to its highest for six months while inventories also expanded, suggesting there are positive signs for future growth.”
With business levels remaining weak in August, Saudi Arabia companies made further efforts to reduce capacity. Output was lowered for the sixth month running, as was employment. That said, both recorded relatively modest declines, with the fall in workforces the slowest since May.

Meanwhile, the rise in VAT from 5% to 15% had a marked impact on prices in the private sector economy. Firms reported the sharpest uptick in input costs since September 2012, as suppliers hiked prices for raw materials. In addition, output charges grew at the fastest pace in 11 years.

On a more positive note, there was growing confidence regarding future private sector activity. Confidence among Saudi Arabia firms strengthened to a six-month high in August, as panelists cited that the reopening of sectors should allow the economy to stabilise.

This confidence led firms to purchase more inputs than required, despite overall purchases falling relative to July. Stocks subsequently built up for the second consecutive month, commonly linked to expectations of stronger growth, although the rate of accumulation slowed.

Companies saw a further stabilisation in supply chains in August as COVID-19 restrictions loosened. Delivery times lengthened overall, but to the least extent for seven months.

Sources:
- IHS Markit, GaStat.
- David Owen, Economist, IHS Markit, +44 2070 646 237, david.owen@ihsmarkit.com
- Katherine Smith, Public Relations, IHS Markit, +1 781-301-9311, katherine.smith@ihsmarkit.com

Methodology
The IHS Markit Saudi Arabia 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.

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 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.

Data were collected 12-20 August 2020.

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

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