Growth of business activity maintained in July, but outlook gloomiest since 2014

KEY FINDINGS

- Business Activity Index slips to six-month low of 54.5
- Slower increases in new business and employment
- Future expectations sink to lowest since December 2014

The service sector remained an area of growth for Germany’s economy at the start of the third quarter, according to the latest PMI® survey, seeing rises in business activity, new orders and employment. That said, rates of expansion slowed on all fronts and firms’ optimism with regards to future output sank to its lowest for more than four-and-a-half years.

The survey’s price indicators meanwhile showed the continuation of inflationary pressures, driven in part by rising wages.

The headline seasonally adjusted IHS Markit Germany Services PMI Business Activity Index – which is based on responses to a single question asking about changes in the volume of business activity compared with one month previously – registered a final reading of 54.5 in July (flash was 55.4). This was down from June’s nine-month high of 55.8 and the lowest reading since January, but still indicative of a marked rate of growth overall.

A breakdown of the data by sub-sector indicated that Hotels & Restaurants was the strongest-performing area, followed by Financial Intermediation.

Increased workloads led service providers to take on additional staff during July, thereby extending the current record sequence of job creation that stretches back to late-2013. In line with trends elsewhere in the data, however, the rate of employment growth slowed, easing further from April’s 11-and-a-half-year peak to the weakest since January.

The volume of outstanding business across the service sector was unchanged in July. This followed increases in backlogs in each of the previous five months.

Elsewhere, latest data showed that cost pressures remained elevated across the service sector at the start of the third quarter, underpinned by higher fuel prices, rents and wages in particular. The rate of overall input cost inflation was little-changed since June and remained comfortably above the historical series average.

Service providers raised charges accordingly. As was the case for costs, the rate of output price inflation was broadly in line with that recorded in the previous survey period and in excess of the long-run trend.

The gloomier outlook for business activity in July extended a run of five consecutive months of weaker expectations among service providers. Though remaining positive overall, sentiment reached its lowest since December 2014, as more firms reported concerns towards the economic growth outlook and the health of the car industry.
Composite output growth eases closer to stagnation in July

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

The combination of a deepening downturn in manufacturing output and slower service sector business activity growth saw the Composite Output Index register 50.9 in July, down from 52.6 in June and its lowest reading in just over six years.

Latest data showed a drop in total new business in July, marking the fifth time in the past seven months that a decrease has been recorded. Manufacturing and exports in general remained the principal areas of order book weakness, with still-robust domestic demand maintaining an upturn in services new business.

July saw a noticeable slowdown in the rate of employment growth to the weakest since April 2015. The result reflected an acceleration of job losses across manufacturing and weaker hiring in the service sector. The current downturn in backlogs of work meanwhile extended to a ninth straight month, with the rate of decline gathering pace to the quickest since June 2013.

On the price front, latest data indicated a general softening of inflationary pressures. Input costs rose at the slowest rate for almost three years, weighed on by a quicker fall in manufacturing purchases prices. The rate of increase in charges levied by firms meanwhile hit a 32-month low.

As has been the case in every month since March, firms’ confidence towards the year-ahead outlook for output weakened in July. A sharp deterioration in manufacturing sentiment provided the biggest drag on overall expectations, which reached the lowest since late-2014.

Commenting on the PMI data, Phil Smith, Principal Economist at IHS Markit said:

“The final services reading came in below the flash estimate, while the survey’s forward-looking indicators are also signalling a loss of momentum. It’s very early stages, but the PMI figures suggest that the economy is heading for another weak GDP performance over the third quarter, on the back of what is generally expected to have been a slight contraction in the three months to June. A further weakening of the data flow in the coming months and Germany’s economy could be staring down the barrel of a mild technical recession.

“Growth in the service sector has so far compensated for the weakness in manufacturing, but it barely did so in July and service providers are steadily losing confidence in the outlook.

“The PMI data show that the pace of job creation in Germany is now at its slowest for over four years, which is a risk in itself to growth prospects. The good news for households and the health of consumer spending in general is that there is still evidence of robust wage growth and overall price pressures are subdued.”
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Methodology

The IHS Markit Germany 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.

July 2019 data were collected 12-26 July 2019.

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

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