COVID-19 impact drives record decline in business activity

Key findings

Unprecedented contractions in output, new business and employment

Business expectations turn pessimistic

Output charges fall at sharpest rate on record

The latest data signalled a substantial decline in business activity across the U.S. service sector in April, as the COVID-19 outbreak escalated and emergency public health measures intensified. The rate of contraction accelerated to the fastest on record as client demand slumped and many businesses closed temporarily. New order inflows fell significantly as customers postponed or cancelled orders amid ongoing global lockdowns. Subsequently, expectations for the year ahead sank to their most pessimistic in the series history. Uncertainty and a further reduction in confidence led to the steepest decrease in workforce numbers on record.

In an effort to retain clients, firms passed lower costs on to clients through the fastest decrease in output charges in the series history.

The seasonally adjusted final IHS Markit US Services Business Activity Index registered 26.7 in April, down notably from 39.8 in March and fractionally lower than the previously published 'flash' figure of 27.0. Efforts to adhere to social distancing and stay-at-home measures resulted in many services firms struggling to remain open, with client demand also dropping significantly.

The escalation of emergency public health procedures resulted in the cancellation and postponement of customer orders, with new business contracting at the most severe rate since the series began in October 2009. Firms that rely on face-to-face custom generally stated they were working at reduced capacity or had closed temporarily.

Foreign client demand also tumbled due to the global nature of lockdown measures and travel restrictions, and the intensification of the outbreak in key export destinations. The drop in new business from abroad far outpaced any fall seen in the series history so far.

Reflecting a slump in new business, firms reduced their workforce numbers in April. The fall was the most marked in the series history and largely stemmed from excess capacity at service providers. Although many stated that lay-offs had been made, others noted that they had furloughed workers in the hope that demand would pick-up after the lockdown eased. Excess capacity also stemmed from the steepest decline in outstanding business on record.

Expectations towards business activity over the coming 12 months sank in April, with firms recording the first instance of pessimism in the outlook since the series began. Sentiment tumbled to a series low as ongoing uncertainty as to when the lockdown will end, and fears surrounding the timespan of any recovery weighed on confidence.

At the same time, service providers registered the fastest fall in cost burdens on record. The decline in input prices partially stemmed from lower wage costs. In an effort to retain clients and kick-start sales, companies sought to pass on reduced input costs to customers through the sharpest fall in average prices charged in the series history.
IHS Markit U.S. Composite PMI®

Unprecedented slump in private sector business activity

Overall output contracted in April at the fastest pace since data collection began in October 2009.

The IHS Markit Composite PMI Output Index* dropped significantly from 40.9 in March to 27.0 at the start of the second quarter. The overall decline was driven by historic downturns in both the manufacturing and service sectors following the escalation of the COVID-19 outbreak.

New business at private sector firms slumped, as client demand fell at the sharpest rate on record. Social distancing and stay-at-home measures were often reported to have led to temporary business closures. The global nature of lockdowns also drove new export orders to fall at a substantial pace.

Meanwhile, private sector firms reduced their workforce numbers at the steepest rate in the series history, amid pessimistic expectations for business activity over the coming year. Lower new order inflows led to greater spare capacity which pushed firms to cut staffing levels.

On the price front, manufacturers and service providers recorded lower cost burdens in April as demand for inputs fell. In an effort to retain clients and revive new business, private sector firms cut their output charges for the second month running, and at the sharpest pace in the series history.

*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 U.S. Composite Output Index is a weighted average of the U.S. Manufacturing Output Index and the U.S. Services Business Activity Index.

Comment

Commenting on the latest survey results, Chris Williamson, Chief Business Economist at IHS Markit, said:

“The slump in the business survey indicators to all-time lows in April indicates how the 4.8% rate of economic decline seen in the first quarter will likely be dwarfed by what’s to come in the second quarter. Measures to fight the COVID-19 outbreak mean vast swathes of the service sector has been especially hard hit by travel restrictions and social distancing, with temporary company closures and dramatically reduced demand resulting in an overall drop in activity of even greater magnitude than seen during the height of global financial crisis.

“With hope, infections rates have peaked and the economic downturn should start to ease as virus-related restrictions are lifted. However, while manufacturing may see a rebound in production as increasing numbers of factories are allowed to re-open, prospects look bleaker for many parts of the services economy, especially where businesses rely on travel, social gatherings or close contact with customers. Businesses such as airlines, bars, restaurants, cinemas, sports arenas and other recreational activities will likely be at the back of the line in terms of being able to re-open to anything like previous capacity levels, meaning the recovery will be long and slow.”
Methodology

The IHS Markit U.S. 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.

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

Survey dates and history

April data were collected 7-29 April 2020.
Data collection began in October 2009.

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